

Westfield Retail Trust (WRT.AX)

Downgrade to Neutral on strong performance

- **Strong recent performer** – WRT has been one of the strongest performers in the Australian REIT sector in recent times. The Trust's performance since its FY11 results were released in February 2012 has been particularly strong: +30%, ahead of all other A-REITs (sector +17%) and the broader market (+2%). We believe WRT's rally has reduced the scope for near-term upside.
- **Fundamentals have proven resilient, but near-term outlook less positive** – In February, WRT reported the strongest LFL net operating income growth (+4.3%) of any of the Australian REITs. However, we believe this will prove to be a high hurdle, and anticipate slower near-term NOI growth, in part through lower inflation.
- **Lower inflation a headwind to NOI growth** – The majority of WRT's rental income stream is indexed to inflation, and recent inflation prints have been well below typical levels (June 2012: CPI +1.2% YoY – see [Q2 CPI result is Goldilocks to the RBA](#) for further details). We note that (1) any inflation spike associated with the carbon tax may help offset low recent inflation readings and benefit WRT, and (2) WRT, along with BWP and WDC, will likely be most affected, with a higher share of CPI-linked leases. Lower interest rates are likely to provide an offsetting earnings tailwind for WRT, although this will likely take time, with debt costs 94% hedged at December 2011. Access to lower cost debt (the Trust's MTNs yield c. 5.2%) may also provide WRT with medium-term growth opportunities – see [Quality Assets with Development Upside](#) for analysis of potential development returns.
- **Yield appeal declining on price rise, downgrade to Neutral** – While WRT continues to offer a solid dividend yield for income-focused investors (see [Solid Result, Payout Increase Boosts Yield Appeal](#)), the Trust's recent rally means that its valuation is now less attractive. WRT still offers a c. 6.2% FY12e dividend yield and trades 6% below NTA. Our \$3.05 target price suggests limited scope for upside, however, with our ETR for WRT (6.2%) now driven entirely by the Trust's yield. As a result, we downgrade WRT to a Neutral recommendation.

- Company Update
- Rating Change

Neutral	2
<i>from Buy</i>	
Price (31 Jul 12)	A\$3.05
Target price	A\$3.05
Expected share price return	0.0%
Expected dividend yield	6.2%
Expected total return	6.2%
Market Cap	A\$9,315M
	US\$9,784M

Price Performance (RIC: WRT.AX, BB: WRT AU)



WRT.AU revisions (Y/E Dec)	2010A	2011A	2012E	2013E	2014E
Reported Profit (A\$m)	na	851.7	577.6	588.3	611.7
% revision	na	0.0%	0.0%	0.0%	0.0%
Core Net Profit (A\$m)	na	561.6	577.6	588.3	611.7
% revision	na	0.0%	0.0%	0.0%	0.0%
Core EPS (A¢)	na	18.4	18.9	19.3	20.0
% revision	na	0.0%	0.0%	0.0%	0.0%
EPS Growth (%)	na	na	2.8	1.8	4.0
PE Ratio (x)	na	16.6	16.1	15.8	15.2
DPS (A¢)	na	16.5	18.9	19.3	20.0
Dividend Yield (%)	na	5.4	6.2	6.3	6.6
Franking Rate (%)	0.0	0.0	0.0	0.0	0.0

Source: Company Reports and dataCentral, Citi Research.


Adrian Dark
+61-2-8225-4870
adrian.dark@citi.com

Suraj Nebhani
suraj.nebhani@citi.com

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Fiscal year end 31-Dec	2010	2011	2012E	2013E	2014E				
Solvency & Return Ratios						Recommendation	2 (Neutral)		
Interest coverage adjusted (x)	na	1.9	1.9	1.8	1.8	Share price up/(downside) (%)	0.00		
Net debt to total assets (%)	na	20.8	22.1	22.3	22.6	Target price (A\$)	3.05		
Look through net debt/total assets (%)	na	20.8	22.1	22.3	22.6	Current price (A\$)	3.05		
ROE adjusted (%)	na	5.6	5.8	5.9	6.1	Market Cap (A\$M)	9,315		
ROA adjusted (%)	na	4.4	4.5	4.5	4.7	Average daily volume (k) (3mth)	12,070		
Geographic EBIT (A\$M)						1H11	2H11	1H12E	2H12E
Australia/NZ	na	801	740	778	808	387	414	365	375
USA	na	0	0	0	0	0	0	0	0
Europe	na	0	0	0	0	0	0	0	0
Funds under management	na	12,752	12,965	13,007	13,050	12,372	12,752	12,925	12,965
Divisional EBIT (A\$M)									
Net rent	na	730	779	818	849	362	368	383	395
Management fees	na	0	0	0	0	0	0	0	0
Development income/asset sale profits	na	0	0	0	0	0	0	0	0
Other	na	106	0	0	0	42	64	0	0
Corporate overheads	na	-35	-39	-40	-41	-17	-19	-19	-20
Per Share Data (A¢)									
EPS adjusted	na	18.4	18.9	19.3	20.0	9.0	9.4	9.4	9.5
DPS	na	16.5	18.9	19.3	20.0	8.1	8.4	9.4	9.5
EPS adjusted growth (%)	na	na	2.8	1.8	4.0	na	4.3	0.2	1.1
DPS growth (%)	na	na	14.6	1.8	4.0	na	3.7	12.0	1.1
NTA excl. def tax (A\$)	na	3.26	3.26	3.26	3.26	3.21	3.26	3.26	3.26
P/E adjusted (x)	na	16.6	16.1	15.8	15.2	16.9	16.2	16.2	16.0
Dividend yield (%)	na	5.4	6.2	6.3	6.6	5.3	5.5	6.2	6.2
Profit & Loss (A\$M)									
Net operating income (NOI)	na	343	365	384	398	164	179	178	187
Other income/expenses	na	458	375	394	410	223	235	187	188
EBIT including associates	na	801	740	778	808	387	414	365	375
Net interest	na	-161	-160	-188	-194	-62	-104	-76	-84
Non-oper./except.	na	214	0	0	0	123	90	0	0
Pre-tax profit	na	853	580	590	614	449	400	288	291
Tax, Extraord./Min. Int./Pref. Div.	na	-2	-2	-2	-2	-2	0	-1	-1
Reported net income	na	852	578	588	612	447	400	287	290
Analyst adjustment	0	-290	0	0	0	-172	-114	0	0
Adjusted earnings	na	562	578	588	612	275	287	287	290
Balance Sheet (A\$M)						Net Asset Value			
Total assets	na	12,820	13,032	13,074	13,118	Stated Wgtd. Av. Cap Rate (%)	na		
Cash & cash equivalent	na	19	19	19	19	Spot Cap Rate on Trust (%)	6.33		
Intangibles	na	0	0	0	0	EBIT multiple on Corp (x)	na		
Net fixed assets	na	6,200	6,413	6,455	6,498	NAV (A\$)	3.05		
Total liabilities	na	2,858	3,070	3,112	3,156	Implied Cap Rate at curr. pr. (%)	7.73		
Total Debt	na	2,686	2,899	2,941	2,984	Implied EBIT multiple at curr. pr. (x)	-0.58		
Other liabilities	na	171	171	171	171				
Net assets	na	9,962	9,962	9,962	9,962				
Cash Flow (A\$M)						Dividend Discount Model			
Operating cash flow	na	579	578	588	612	5 year DPS CAGR (%)	na		
Investing cash flow	na	-129	-213	-42	-44	Terminal Yield (%)	3.59		
Capital expenditure	na	-47	-203	-42	-44	Discount Rate (%)	7.59		
Acquisitions/disposals	na	1	-10	0	0	DDM Valuation (A\$)	4.00		
Financing cash flow	na	-446	-365	-546	-568	Valuation up/(downside) (%)	31.07		
Borrowings	na	1,451	213	42	44				
Dividends paid	na	-261	-578	-588	-612				
Change in cash	na	5	0	0	0				

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Westfield Retail Trust

Company description

Westfield Retail Trust was demerged from Westfield Group in 2010, co-owning its portfolio with WDC, which will also conduct property and development management for WRT. WRT is conservatively geared, and offers clean exposure to Australian and New Zealand retail assets. As at 30 June 2010, WRT held interests in 54 shopping centres, with gross assets of \$12.2b. The Trust's portfolio is considered high quality, with 90% located in Australia and 10% in New Zealand.

Investment strategy

We rate WRT Neutral (2). We see WRT as offering exposure to a high-quality portfolio of Australian and New Zealand retail property. We anticipate continued organic NPI growth, with the potential for development activity to add significant value over the long term, although the Trust does not offer compelling value at current levels.

Valuation

Our target price of \$3.05 is set with reference to our NAV based sum of the parts. For our NAV, we use a portfolio cap rate of 6.3% applied to 12-month forward net operating income, making deductions for the Trust's debt and other liabilities. We do not incorporate the potential for value accretion from unannounced developments.

Risks

We see WRT's asset base as likely to generate a very stable income stream, and gearing levels as conservative. As a relatively newly formed entity, however, investors face additional uncertainty in a number of respects, including the Trust's medium-term capital structure, cost of debt, and foreign exchange rate exposure.

General risks for WRT relate to retail spending trends and retailer health, while specific factors considered include the Trust's reliance on WDC, as well as the location and demographics of the Trust's centres, and centre tenant mix. Development returns will have a significant impact on medium term growth prospects. Valuation risks include changes to long-term capitalisation rates. A favourable or adverse movement in the above factors may cause the share price to deviate from our target price.

BWP Trust

(BWP.AX; A\$1.98; 2)

Valuation

Our target price of \$1.89 is set with reference our NAV based sum of the parts. For our NAV, we mark to market the investment portfolio using a 7.9% cap rate applied to 12 month forward net operating income, and incorporate a deduction for management fees. As a secondary valuation method, we calculate an NPV of \$2.46. Our DCF factors in a discount rate of 8.5%, a beta of 0.55, a risk free rate of 5.5% and an equity risk premium of 5.0%.

Risks

BWP faces certain risks with regard to a range of fundamental and quantitative factors. Over 90% of BWP's rental income is generated from leases to a wholly owned subsidiary of Wesfarmers Limited, Bunnings Group Limited. The stability of the income and value of the Trust's assets are dependent on Bunnings Group Limited delivering on its contractual obligations. Developments and acquisitions will have incremental returns on medium-term growth prospects. Risks pertain to real estate market conditions in general and encompass considerations of supply and the economic environment. Valuation risks include changes in the level of interest rates, trend gearing and changes to long-term capitalisation rates. A favourable or adverse movement in these risk factors may cause the share price to deviate from our target price.

Westfield Group

(WDC.AX; A\$10.00; 1)

Valuation

Our target price of \$10.00 is set in line with our NAV, and with reference to our \$10.22 DCF. Our DCF factors in a discount rate of 9.8%, a beta of 0.85, a risk free rate of 5.5% and an equity risk premium of 5.0%.

For our NAV-based sum of the parts, we mark to market the investment portfolio using a 6.3% market cap rate, and value the fee income using a combined 14x EBIT multiple. We add the book value of development land and work in progress, and complete a DCF on future anticipated development profits.

Risks

WDC faces certain risks with regard to a range of fundamental and quantitative factors inclusive of beta and yield. General risks for WDC pertain to the aggregate retail spend patterns in centre catchments. Specific factors considered include employment growth and retail sales growth. The return from the current development pipeline should form the basis of medium-term earnings growth prospects. Longer-term growth is dependent on sustaining portfolio growth and potential accretive acquisitions or development. This is both a risk and an opportunity if the rate of development varies materially from our current assumptions.

Other risks include changes of the level of interest rates, intensification of competition from global peers, and AUD currency movements versus USD, GBP and NZD, and to any unexpected further changes in consumer behaviour. A favourable or adverse movement in risk due to changes in the above factors may result in the share price not meeting our target price.

Appendix A-1

Analyst Certification

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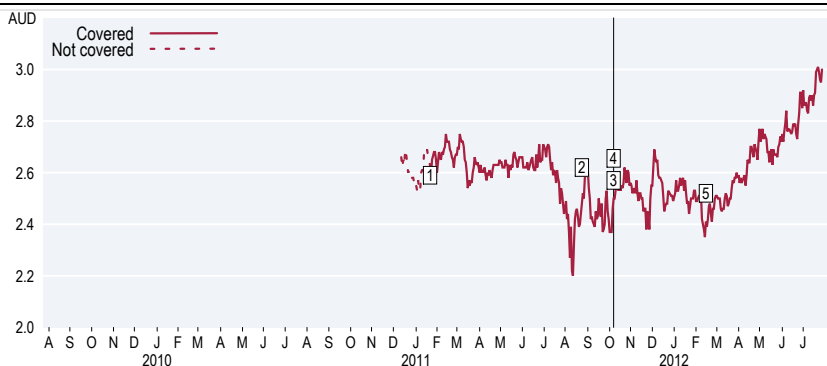
IMPORTANT DISCLOSURES

Westfield Retail Trust (WRT.AX)

Ratings and Target Price History Fundamental Research

Analyst: Adrian Dark

Covered since August 22 2011



	Date	Rating	Target Price	Closing Price
1	21-Jan-11	*1M	*3.01	2.63
2	24-Aug-11	1M	*3.09	2.48

* Indicates change

	Date	Rating	Target Price	Closing Price
3	7-Oct-11	Stock rating system changed		
4	7-Oct-11	*1	3.09	2.50

	Date	Rating	Target Price	Closing Price
5	15-Feb-12	1	*3.05	2.41

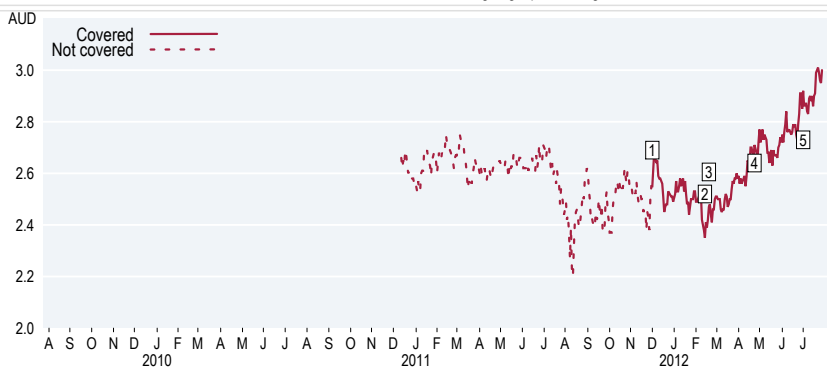
Rating/target price changes above reflect Eastern Standard Time

Westfield Retail Trust (WRT.AX)

Ratings and Target Price History Best Ideas Research Relative Call (3 Month)

Analyst: Adrian Dark

Covered since August 22 2011



	Date	Rating	Target Price	Closing Price
1	1-Dec-11	*ADD MP	-	2.55
2	14-Feb-12	*REM MP	-	2.35

* Indicates change

	Date	Rating	Target Price	Closing Price
3	20-Feb-12	*ADD MP	-	2.47
4	24-Apr-12	*REM MP	-	2.71

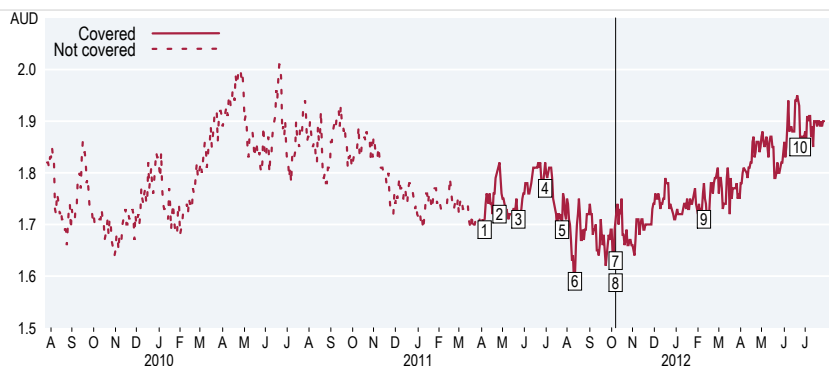
	Date	Rating	Target Price	Closing Price
5	30-Jun-12	*N	-	2.85

Rating/target price changes above reflect Eastern Standard Time

BWP Trust (BWP.AX)**Ratings and Target Price History****Fundamental Research**

Analyst: Adrian Dark

Covered since August 22 2011



	Date	Rating	Target Price	Closing Price
1	6-Apr-11	*1M	*1.86	1.71
2	27-Apr-11	*2M	1.86	1.82
3	24-May-11	*1M	1.86	1.72
4	30-Jun-11	*2M	1.86	1.82

* Indicates change

	Date	Rating	Target Price	Closing Price
5	25-Jul-11	*1M	1.86	1.70
6	11-Aug-11	1M	*1.90	1.60
7	7-Oct-11	Stock rating system changed		
8	7-Oct-11	*1	1.90	1.71

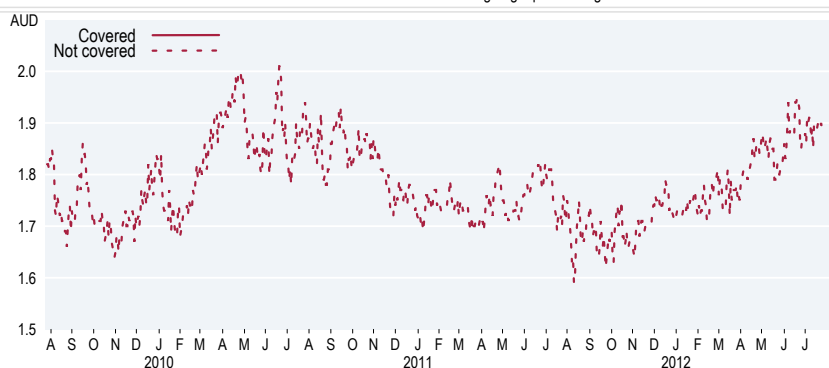
	Date	Rating	Target Price	Closing Price
9	9-Feb-12	*2	*1.89	1.78
10	25-Jun-12	2	*1.89	1.86

Rating/target price changes above reflect Eastern Standard Time

BWP Trust (BWP.AX)**Ratings and Target Price History****Best Ideas Research****Relative Call (3 Month)**

Analyst: Adrian Dark

Covered since August 22 2011



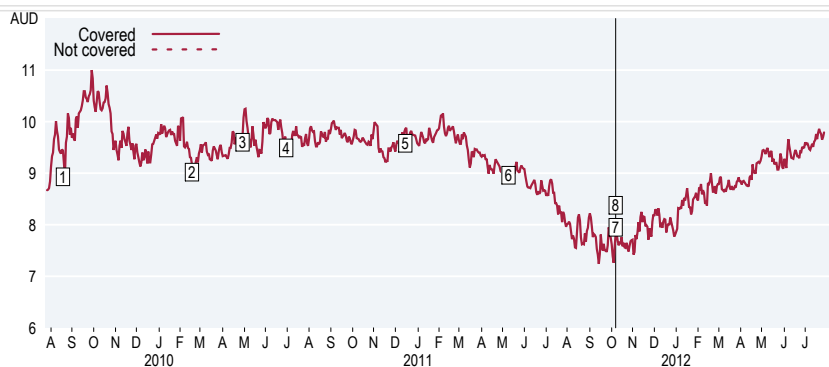
* Indicates change

Rating/target price changes above reflect Eastern Standard Time

Westfield Group (WDC.AX)**Ratings and Target Price History****Fundamental Research**

Analyst: Adrian Dark

Covered since February 14 2012



	Date	Rating	Target Price	Closing Price
1	19-Aug-09	1M	*10.77	9.44
2	17-Feb-10	*2M	*9.99	9.17
3	29-Apr-10	2M	*10.03	9.72

* Indicates change

	Date	Rating	Target Price	Closing Price
4	30-Jun-10	2M	*10.13	9.50
5	15-Dec-10	2M	*10.54	9.86
6	10-May-11	*1M	*10.00	9.07

	Date	Rating	Target Price	Closing Price
7	7-Oct-11	Stock rating system changed		
8	7-Oct-11	*1	10.00	7.82

Rating/target price changes above reflect Eastern Standard Time

Westfield Group (WDC.AX)

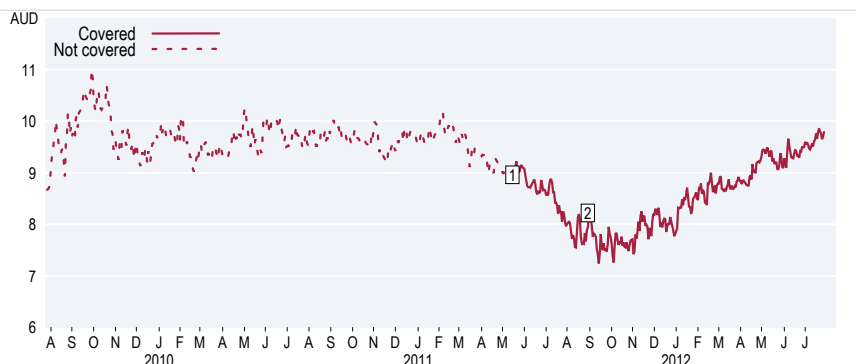
Ratings and Target Price History

Best Ideas Research

Relative Call (3 Month)

Analyst: Adrian Dark

Covered since February 14 2012



Date	Rating	Target Price	Closing Price
1 15-May-11	*ADD MP	-	9.08

* Indicates change

Date	Rating	Target Price	Closing Price
2 30-Aug-11	*REM MP	-	7.94

Rating/target price changes above reflect Eastern Standard Time

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Citi Research Ratings Distribution

Data current as of 30 Jun 2012

Citi Research Global Fundamental Coverage

% of companies in each rating category that are investment banking clients

12 Month Rating			Relative Rating		
Buy	Hold	Sell	Buy	Hold	Sell
53%	37%	10%	10%	80%	10%
44%	43%	40%	48%	43%	45%

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