

31 October 2018 | Initiate Coverage

Al-`Aqar Healthcare REIT

A defensive healthcare REIT

Initiate with BUY

Target Price: RM1.45

INVESTMENT HIGHLIGHTS


- **A defensive healthcare REIT**
- **Asset acquisition to expand portfolio**
- **Stable earnings in 1HFY18**
- **Steady earnings outlook**
- **Initiate Coverage with BUY Call and TP of RM1.45**

A defensive healthcare REIT. Al-`Aqar Healthcare REIT (Al-`Aqar) is the world's first listed Islamic Healthcare REIT and it is also the only healthcare REIT in Malaysia. Al-`Aqar is supported by its sponsor - KPJ Healthcare Berhad. As at Dec 2017, Al-`Aqar's properties comprise of 19 hospitals and 3 healthcare related properties in Malaysia and Australia with total portfolio value of RM1.46b. In terms of geographical exposure, 21 out of the 22 assets are located in Malaysia while the remaining one asset is located in Australia.

Asset acquisition to expand portfolio. Al-`Aqar is looking to expand portfolio via asset acquisition. Asset acquisitions in the pipeline are KPJ Batu Pahat (RM70m), KPJ Kluang (RM80m) and KPJ Segamat (RM70m). The asset acquisitions are expected to take place within the next two years. Aside from asset acquisitions, Al-`Aqar is also looking at building ambulatory care centre and hospital expansion projects (Ampang Puteri Specialist and Penang Specialist) to expand their portfolio.

Stable earnings in 1HFY18. FY17 core net income of RM59.9m was weaker by 2.7%yoy, in line with weaker topline (-4%yoy) mainly due to loss of income from Selesa Tower. Meanwhile, earnings in 1HFY18 were stronger at RM32.3m (+10.3%yoy), supported by renewal of leases, rental contribution from car park block at KPJ Selangor Specialist Hospital (acquired in December 2017) and lower sukuk financing cost.

Steady earnings outlook. We expect Al-`Aqar core net income to grow 1.4%yoy in FY18 assuming stable rental reversion of +2% per annum. Nevertheless, we forecast FY19 earnings to be flattish as we expect higher refinancing cost of sukuk to offset the higher rental income. Meanwhile, distribution per unit (DPU) of Al-`Aqar is expected to remain stable which translates into net dividend yield of 5.7%.

Initiate Coverage with BUY call and TP of RM1.45, based on Multi Stage Dividend Discount Model (Required rate of return: 7.2%, Perpetual growth rate: 2.2%). We like Al-`Aqar for: i) its unique positioning as a defensive healthcare REIT in Malaysia, ii) stable earnings growth and low earnings downside risk and iii) its distribution yield of 5.7% is slightly higher than peer's average of 5.6%. 

RETURN STATS	
Price (30 Oct 2018)	RM1.23
Target Price	RM1.45
Expected Share Price Return	17.9%
Expected Dividend Yield	5.7%
Expected Total Return	23.6%

STOCK INFO	
KLCI	1685.94
Bursa / Bloomberg	5116/AQAR MK
Board / Sector	Main/REITs
Syariah Compliant	Yes
Issued shares (mil)	728.23
Par Value (RM)	1.00
Market cap. (RM'm)	895.72
Price over NA	0.98
52-wk price Range	RM1.08-RM1.5
Beta (against KLCI)	0.62
3-mth Avg Daily Vol	0.01m
3-mth Avg Daily Value	RM0.01m
Major Shareholders	
Johor Corp	41.77%
Lembaga Tabung Haji	14.19%
KWAP	9.03%
EPF	8.47%
Pusat Pakar Tawakal M Sdn Bhd	7.5%
Skim Amanah Saham Bumiputera	6.32%
Amanah Saham Bumiputera	5.24%

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INVESTMENT STATISTICS

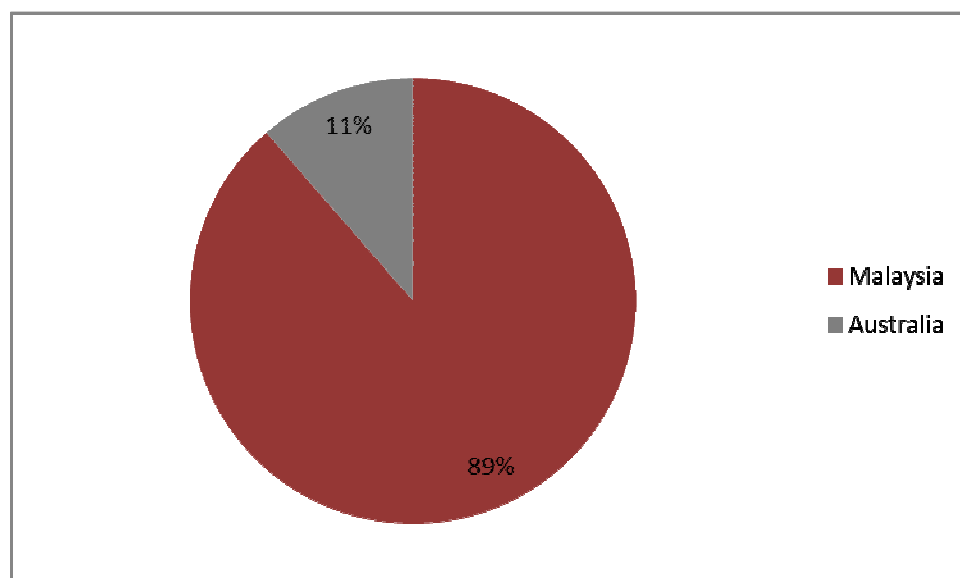
FYE Dec	FY15A	FY16A	FY17A	FY18F	FY19F
Revenue	110.9	103.8	99.6	102.0	102.4
Net Rental Income	104.6	97.6	93.2	95.4	95.7
Profit Before Tax	67.9	64.0	86.2	62.2	62.4
Net Income	67.4	63.4	84.6	60.7	60.9
Core Net Income	55.8	61.9	59.9	60.7	60.9
Basic EPS (sen)	9.26	8.71	11.62	8.34	8.37
Core EPS (sen)	7.67	8.50	8.22	8.34	8.37
Gross Dividend (sen)	7.70	7.70	7.70	7.75	7.82
Net Dividend (sen)	6.93	6.93	6.93	6.98	7.04
Net Distribution Yield	5.6%	5.6%	5.6%	5.7%	5.7%
Core PER	16.05	14.47	14.97	14.76	14.70
NAV per unit	1.21	1.23	1.26	1.28	1.31
P/NAV (x)	1.02	1.00	0.98	0.96	0.94
Core ROE	6.3%	6.9%	6.5%	6.5%	6.4%
Core ROA	3.5%	3.8%	3.8%	3.9%	3.9%

Source: Company, MIDF Research Forecast

1. Financial Review/Outlook

Malaysia operations the main earnings contributor. In terms of geographical exposure, assets in Malaysia contributed 89% of net property income of Al-`Aqar in FY17 while asset in Australia (Jeta Gardens Aged Care Facility and Retirement Village) contributed 11% of net property income in FY17.

Figure 1: Net Property Income breakdown by segment

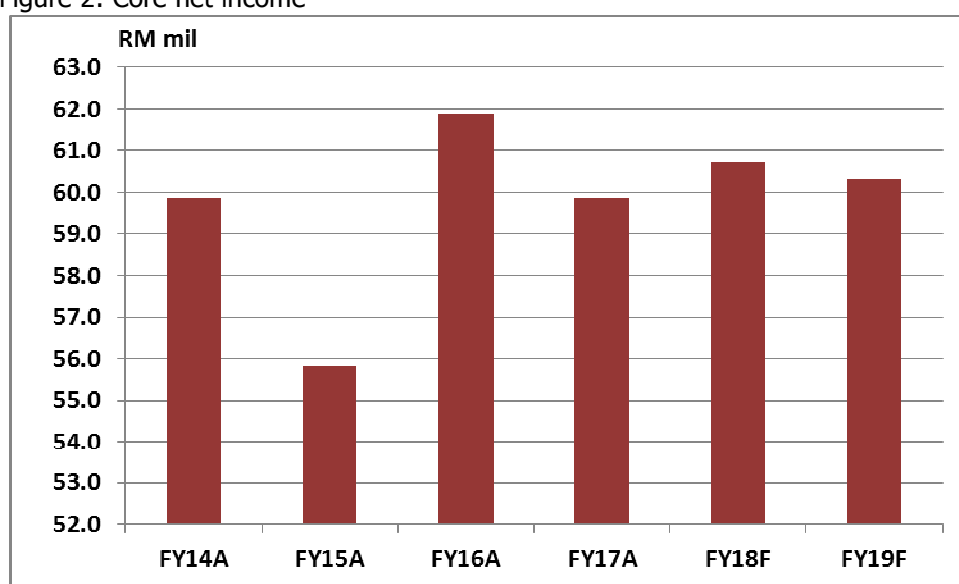


Source: MIDF Research

Lower core net profit in FY15 due to realised forex loss. FY15 core net profit (excluding fair value gain on properties) came in lower at RM55.8m (-6.7%yoy) despite higher topline (+2%yoy), mainly attributed to realised forex loss from disposal of subsidiaries of RM3.5m. Note that Al-`Aqar disposed two Indonesian properties to KPJ Healthcare in 16 December 2015, namely Rumah Sakit Medika Permata Hijau and Rumah Sakit Bumi Serpong Damai.

Marginally lower earnings in FY17 on disposal of Selesa Tower. FY17 core net income of RM59.9m was weaker at -2.7%yoy, in line with weaker topline (-4%yoy) mainly due to loss of income from Selesa Tower. Note that Al-`Aqar announced the disposal Selesa Tower (an integrated commercial development comprising hotel and office block) to Optimum Impress Sdn Bhd for RM100m on 14 November 2016.

Figure 2: Core net income



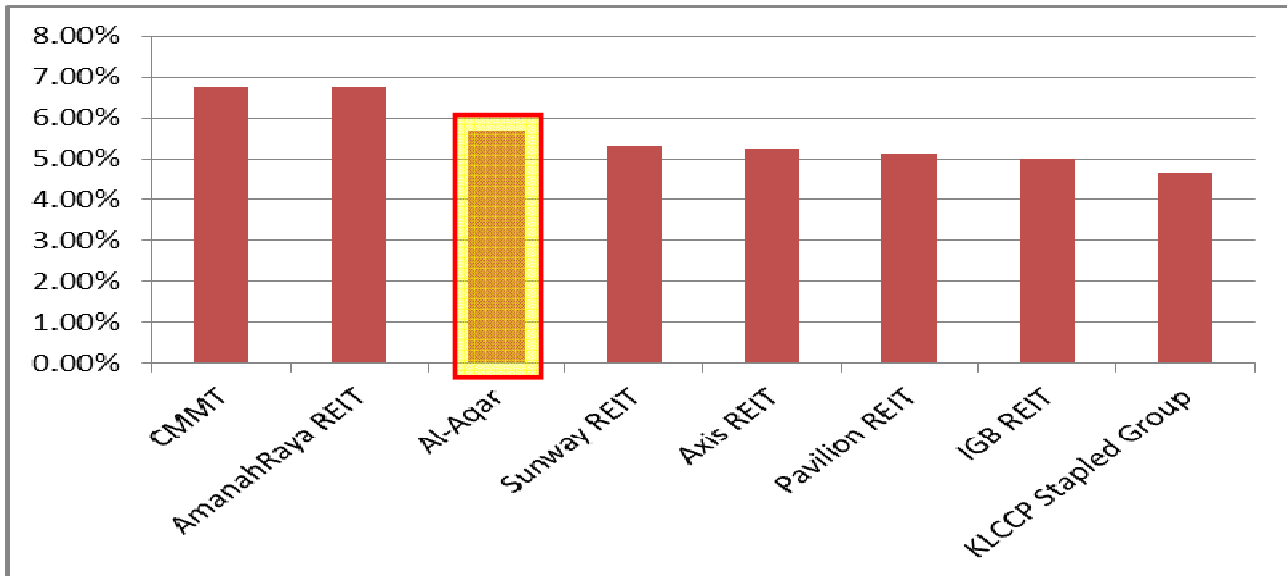
Source: MIDF Research

Stable earnings in 1HFY18. Al-`Aqar 2QFY18 core net income climbed 9.2%yoy, bringing cumulative earnings in 1HFY18 to RM32.3m (+10.3%yoy). The year-on-year positive earnings growth in 2QFY18 and 1HFY18 was in line with topline growth. Topline was supported by renewal of leases and rental contribution from car park block at KPJ Selangor Specialist Hospital (acquired in December 2017). Meanwhile, lower sukuk financing cost (-9.4%yoy) has also helped in earnings growth. Recall that Al-`Aqar redeemed sukuk amounting RM80m on 20 July 2017. Looking ahead, we expect Al-`Aqar core net income to grow 1.4%yoy in FY18, mainly underpinned by stable rental reversion of +2% per annum.

2. Peers Comparison

Distribution yield slight above peers' average. Distribution yield of Al-`Aqar is estimated at 5.7% based on estimated net DPU 7sen. Distribution yield of Al-`Aqar is marginally above peers' average of 5.6%. Estimated distribution yield of Al-`Aqar is lower than distribution yields of CMMT and AmanahRaya REIT but higher than distribution yields of other REITs under our coverage.

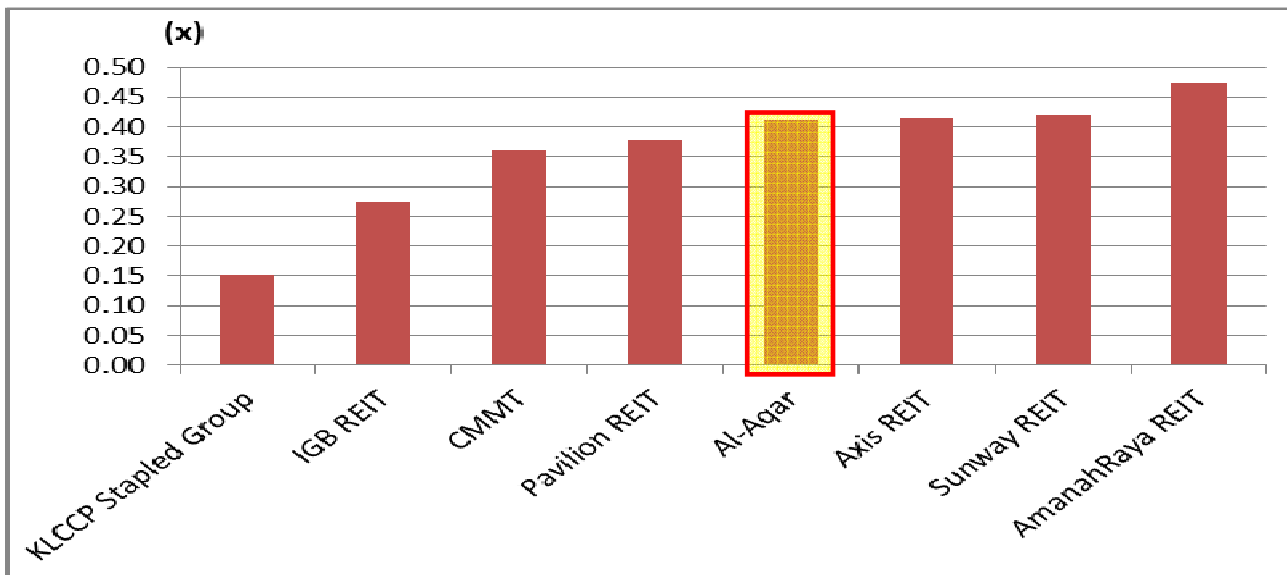
Figure 3: Distribution yield of REITs



Source: MIDF Research

Moderate gearing at 0.41x. Gearing of Al-Aqar is at 0.41x, lower than gearing of AmanahRaya REIT, Sunway REIT and Axis REIT. Meanwhile, gearing of Al-Aqar is higher than gearing of Pavilion REIT, CMMT, IGB REIT and KLCCP Stapled Group.

Figure 4: Gearing of REITs



Source: MIDF Research

3. Valuation and Recommendation

Initiate Coverage with BUY Call and TP of RM1.45, based on Multi Stage Dividend Discount Model (Required rate of return: 7.2%, Perpetual growth rate: 2.2%). We like Al-`Aqar for: i) its unique positioning as a defensive healthcare REIT in Malaysia, ii) stable earnings growth and low earnings downside risk and iii) its distribution yield of 5.7% is slightly higher than peer's average of 5.6%.

Figure 5: Key Variables Used In Valuation

CAPM Model Input		Value
Risk Free Rate, RFR		4.0%
Beta, β		0.46
Market Return, Rmarket		10.9%
Required Rate Of Return, E(R)		7.2%
DDM Model Input		
Required Rate Of Return, E(R)		7.2%
DDM Stage 1 Growth - FY18E		0.7%
DDM Stage 1 Growth - FY19E		0.3%
DDM Stage 2 Growth - Year 3 to Year 10		3.0%
Terminal Growth, g		2.2%

Source: MIDF Research Estimate

Figure 6: Peers Comparison Table

Stock	FYE	Rec.	Price @ 29 Oct	Target Price (RM)	Core EPU (sen)			Core PE (x)		Net DPU		Net Dvd Yield	
					FY17	FY18	FY19	FY18	FY19	FY18	FY19	FY18	FY19
AXREIT	Dec	NEUTRAL	1.52	1.55	10.0	9.1	10.0	16.7	15.2	8.0	8.8	5.3	5.8
CMMT	Dec	NEUTRAL	1.03	1.02	7.8	7.9	8.0	13.1	12.9	7.0	7.1	6.8	6.9
IGBREIT	Dec	NEUTRAL	1.68	1.73	8.6	8.7	9.2	19.2	18.3	8.4	8.8	5.0	5.2
PAVREIT	Dec	NEUTRAL	1.57	1.60	7.7	8.7	9.7	18.1	16.3	8.0	8.9	5.1	5.7
KLCC	Dec	NEUTRAL	7.62	7.59	39.9	40.7	41.9	18.7	18.2	35.4	36.4	4.6	4.8
SUNREIT	Jun	BUY	1.68	1.93	9.2	9.6	9.9	17.4	16.9	8.7	8.9	5.2	5.3
ARREIT	Dec	BUY	0.87	0.94	5.5	6.5	7.3	13.4	11.8	5.6	6.4	6.5	7.4
ALAQAR	Dec	BUY	1.23	1.45	8.22	8.34	8.28	14.8	14.9	7.0	7.0	5.7	5.7

Source: MIDF Research Estimate

4. Background

Figure 7: List of Properties

Assets	Location	Fair Value (RM m)
KPJ Ampang Puteri Specialist Hospital	Malaysia	135.0
KPJ Damansara Specialist Hospital	Malaysia	121.7
KPJ Johor Specialist Hospital	Malaysia	116.8
KPJ Ipoh Specialist Hospital	Malaysia	73.0
KPJ Selangor Specialist Hospital	Malaysia	80.8
KPJ Penang Specialist Hospital	Malaysia	64.0
KPJ Tawakkal Specialist Hospital	Malaysia	127.9
KPJ Seremban Specialist Hospital	Malaysia	66.3
Kedah Medical Centre	Malaysia	51.7
KPJ Perdana Specialist Hospital	Malaysia	45.0
KPJ Kajang Specialist Hospital	Malaysia	48.4
Tawakal Health Centre	Malaysia	47.0
Puteri Specialist Hospital	Malaysia	43.0
Sentosa Medical Centre	Malaysia	30.0
KPJ Kuantan Dialysis Centre	Malaysia	21.7
KPJ Healthcare University College, Nilai	Malaysia	100.6
KPJ International College, Bukit Mertajam	Malaysia	16.2
Damai Specialist Hospital	Malaysia	15.2
Taiping Medical Centre	Malaysia	10.0
Kluang Utama Specialist Hospital	Malaysia	4.3
KPJ Klang Specialist Hospital	Malaysia	101.5
Jeta Gardens Aged Care Facility and Retirement Village	Australia	139.6
Total		1459.7

Source: Company, MIDF Research

Figure 8: Details of Properties



Name of Property: KPJ Ampang Puteri Specialist Hospital

Lessee/Asset Operator : Ampang Puteri Specialist Hospital Sdn Bhd

Description: A purpose built private hospital comprising a seven (7) storey main building (NCB Block), an annexed five (5) storey specialist centre (PCB Block) both are with a common lower ground floor together with a part of the redevelopment land currently under construction with a 15 storey private hospital building and part of the redevelopment land being used as a car park area.

Gross Floor Area: 384,729 sq.ft.

Tenancy/Lease Expiry & Renewal: Expiry on 29 June 2021 and renewal on 30 June 2021.



Name of Property: KPJ Damansara Specialist Hospital

Lessee/Asset Operator : Damansara Specialist Hospital Sdn Bhd

Description: A six (6) storey purpose built hospital building with a basement level (inclusive of approximately one and a half (1½) levels of shell floors) together with open car park.

Gross Floor Area: 445,114 sq.ft.

Tenancy/Lease Expiry & Renewal: Expiry on 31 December 2018 and renewal on 1 January 2019.



Name of Property: KPJ Johor Specialist Hospital

Lessee/Asset Operator: Johor Specialist Hospital Sdn Bhd

Description: A six (6) level with mezzanine floor main hospital building, a four (4) level physician consulting building together with two (2) level basement car parks and open car parks.

Gross Floor Area: 477,234 sq.ft.

Tenancy/Lease Expiry & Renewal: Expiry on 31 December 2018 and renewal on 1 January 2019.



Name of Property: KPJ Puteri Specialist Hospital

Lessee/Asset Operator: Puteri Specialist Hospital (Johor) Sdn Bhd.

Description: A six (6) storey purpose built private hospital building.

Gross Floor Area: 118,019 sq.ft.

Tenancy/Lease Expiry & Renewal: Expiry on 29 June 2021 and renewal on 30 June 2021.



Name of Property: KPJ Selangor Specialist Hospital

Lessee/Asset Operator: Selangor Specialist Hospital Sdn Bhd.

Description: A six (6) storey main specialist centre building together with a basement and a six storey carpark block together with a basement.

Gross Floor Area: 212,612 sq.ft.

Tenancy/Lease Expiry & Renewal: Expiry on 29 June 2021 and renewal on 30 June 2021.



Name of Property: KPJ Ipoh Specialist Hospital

Lessee/Asset Operator: Ipoh Specialist Hospital Sdn Bhd.

Description: A purpose built private specialist hospital comprising three (3) to four (4) storey building (Old Wing) annexed to a five (5) storey building with a basement (New Wing).

Gross Floor Area: 348,166. Sq.ft

Tenancy/Lease Expiry & Renewal: Expiry on 31 December 2018 and renewal on 1 January 2019.



Name of Property: KPJ Perdana Specialist Hospital

Lessee/Asset Operator: Perdana Specialist Hospital Sdn Bhd

Description: A five (5) storey purpose built private specialist hospital with a sub-basement.

Gross Floor Area: 147,542 sq. ft.

Tenancy/Lease Expiry & Renewal: Expiry on 29 February 2020 and renewal on 1 March 2020.



Name of Property: KPJ Kuantan Dialysis Centre

Lessee/Asset Operator: Kuantan Specialist Hospital Sdn Bhd

Description: The building comprise two adjoining three (3) and five (5) storey blocks identified as Blocks A and B, respectively.

Gross Floor Area: 72,201 sq.ft.

Tenancy/Lease Expiry & Renewal: Expiry on 29 February 2020 and renewal on 1 March 2020.



Name of Property: Sentosa Medical Centre

Lessee/Asset Operator: Sentosa Medical Centre Sdn Bhd

Description: A seven (7) storey purpose private specialist hospital

Gross Floor Area: 115,331 sq.ft.

Tenancy/Lease Expiry & Renewal: Expiry on 29 February 2020 and renewal on 1 March 2020.



Name of Property: KPJ Kajang Specialist Hospital

Lessee/Asset Operator: Kajang Specialist Hospital Sdn Bhd

Description: A seven (7) storey purpose built private specialist hospital

Gross Floor Area: 191,144 sq.ft.

Tenancy/Lease Expiry & Renewal: Expiry on 29 February 2020 and renewal on 1 March 2020



Name of Property: Kedah Medical Centre

Lessee/Asset Operator: Kedah Medical Centre Sdn Bhd

Description: A ten (10) storey purpose built private specialist hospital(inclusive of one (1) shell floor) with a three (3) storey annexe block.

Gross Floor Area: 215,881 sq.ft.

Tenancy/Lease Expiry & Renewal: Expiry on 29 February 2020 and renewal on 1 March 2020



Name of Property: Damai Specialist Hospital

Lessee/Asset Operator: Kota Kinabalu Specialist Hospital Sdn Bhd

Description: A five (5) storey purpose built private specialist hospital building

Gross Floor Area: 42,286 sq.ft.

Tenancy/Lease Expiry & Renewal: Expiry on 11 June 2018 and renewal on 12 June 2018



Name of Property: KPJ Penang Specialist Hospital

Lessee/Asset Operator: Penang Specialist Hospital Sdn Bhd

Description: A five (5) storey main hospital building

Gross Floor Area: 182,824.00 sq.ft.

Tenancy/Lease Expiry & Renewal: Expiry on 13 October 2018 and renewal on 14 October 2018



Name of Property: Tawakkal Health Centre

Lessee/Asset Operator: Pusat Pakar Tawakal Sdn Bhd

Description: Twenty One (21) contiguous parcels of terraced commercial plots erected with a block of newly refurbished four (4) storey private hospital.

Gross Floor Area: 119,925 sq.ft.

Tenancy/Lease Expiry & Renewal: Expiry on 14 May 2018 and renewal on 15 May 2018.



Name of Property: KPJ Tawakkal Specialist Hospital

Lessee/Asset Operator: Pusat Pakar Tawakal Sdn Bhd

Description: A seven (7) storey purpose built specialist hospital with a single storey podium as the main lobby and a three (3) level elevated car park

Gross Floor Area: 333,514 sq.ft.

Tenancy/Lease Expiry & Renewal: Expiry on 5 July 2019 and renewal on 6 July 2019



Name of Property: KPJ Seremban Specialist Hospital

Lessee/Asset Operator: Seremban Specialist Hospital Sdn Bhd

Description: A purpose-built private specialist hospital comprising of a five (5) storey hospital building with a basement level together with a parcel of commercial land currently under construction with a new hospital building

Gross Floor Area: 182,012 sq.ft

Tenancy/Lease Expiry & Renewal: Expiry on 13 October 2024 and renewal on 14 October 2024



Name of Property: Taiping Medical Centre

Lessee/Asset Operator: Taiping Medical Centre Sdn Bhd

Description: Six (6) contiguous parcels of terraced commercial plots comprising 5 intermediate plots and a corner plot erected with a four storey private hospital together with a parcel of commercial land

Gross Floor Area: 40,858 sq.ft.

Tenancy/Lease Expiry & Renewal: Expiry on 30 April 2018 and renewal on 1 May 2018



Name of Property: KPJ Healthcare University College

Lessee/Asset Operator: Puteri Nursing College Sdn Bhd

Description: An Institutional premises comprising two (2) contiguous parcel of commercial land erected with a three (3) storey administrative cum academic block, a two (2) storey lecture hall, an eight (8) storey academic block, a single storey cafeteria, a guard house, a refuse compartment, an animal house, a surau and a TNB substation and two (2) contiguous parcels of residential land erected with a five (5) storey apartment block (hostel), eleven and a half (11 ½) storey apartment block (students hostel), two (2) guard houses, two(2) refuse compartments, a water tank and pump house buildings and two (2) TNB sub-stations.

Gross Floor Area: 454,883 sq.ft.

Tenancy/Lease Expiry & Renewal:

i- KPJUC (Existing Building) - Expiry on 30 April 2018 and

renewal on 1 May 2018.

ii- KPJUC (New Building) - Expiry on 30 November 2018 and

renewal 1 December 2018.



Name of Property: KPJ International College, Penang

Lessee/Asset Operator: Puteri Nursing College Sdn Bhd

Description: A six (6) storey purpose built private specialist hospital building known as "Bukit Mertajam Specialist Hospital" and two (2) parcels of development land

Gross Floor Area: 42,989 sq.ft.

Tenancy/Lease Expiry & Renewal: Expiry on 13 October 2018 and renewal on 14 October 2018



Name of Property: Kluang Utama Specialist Hospital

Lessee/Asset Operator: Pusat Pakar Kluang Utama Sdn Bhd

Description: 6 units of 3-storey shop-offices renovated into a private hospital known as Kluang Utama Specialist Hospital.

Gross Floor Area: 31,837 sq.ft

Tenancy/Lease Expiry & Renewal: Expiry on 5 January 2018 and renewal on 6 January 2018



Name of Property: KPJ Klang Specialist Hospital

Lessee/Asset Operator: Bandar Baru Klang Specialist Hospital Sdn Bhd

Description: A purpose built private hospital comprising a six (6) storey main building with two (2) levels of basement car park

Gross Floor Area: 391,358 sq.ft.

Tenancy/Lease Expiry & Renewal: Expiry on 25 June 2018 and renewal on 26 June 2018.



Name of Property: Jeta Gardens Aged Care & Retirement Village, Australia

Lessee/Asset Operator: Jeta Gardens (QLD) Pty Ltd

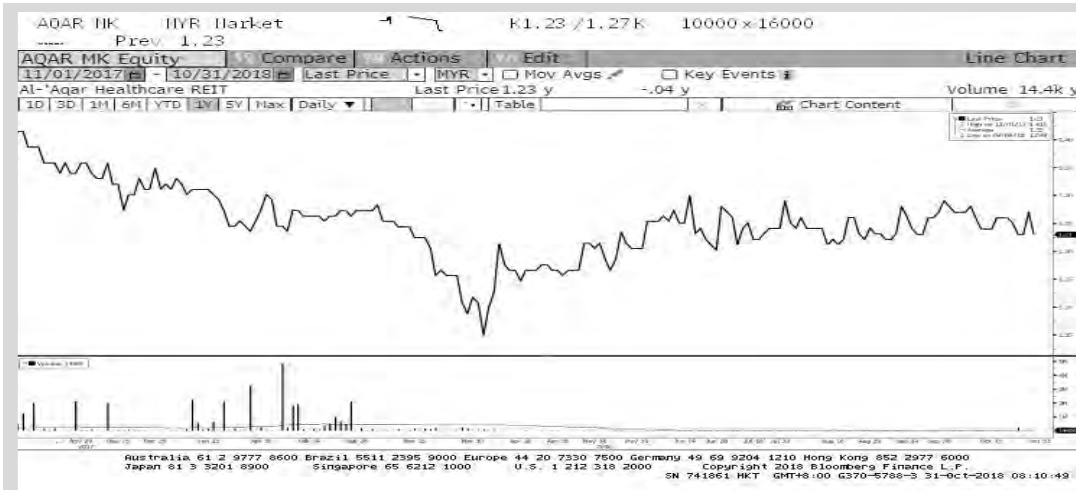
Description: Three (3) contiguous parcels of residential land erected with two (2) storey aged care building comprising 106 rooms (108-bed) aged care facility, 23 units of independent villas and 32 independent living apartment units

Gross Floor Area: 80,029.67 sq.ft.

Tenancy/Lease Expiry & Renewal: Expiry on 1 November 2020 and renewal on 2 November 2020

Source: MIDFR, Company

DAILY PRICE CHART



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MIDF AMANAH INVESTMENT BANK : GUIDE TO RECOMMENDATIONS

STOCK RECOMMENDATIONS

BUY	Total return is expected to be >10% over the next 12 months.
TRADING BUY	Stock price is expected to <i>rise</i> by >10% within 3-months after a Trading Buy rating has been assigned due to positive newsflow.
NEUTRAL	Total return is expected to be between -10% and +10% over the next 12 months.
SELL	Total return is expected to be <-10% over the next 12 months.
TRADING SELL	Stock price is expected to <i>fall</i> by >10% within 3-months after a Trading Sell rating has been assigned due to negative newsflow.

SECTOR RECOMMENDATIONS

POSITIVE	The sector is expected to outperform the overall market over the next 12 months.
NEUTRAL	The sector is to perform in line with the overall market over the next 12 months.
NEGATIVE	The sector is expected to underperform the overall market over the next 12 months.