

07 September 2017 | 2QCY17 Earnings Wrap

REITs

2QCY17 earnings largely in line

Maintain NEUTRAL

KEY HIGHLIGHTS

- 2QCY17 earnings of REITs largely within expectations
- Slew of asset acquisitions announced
- Few changes to target prices
- Easing MGS yield may provide catalyst to REITs
- We remain **NEUTRAL** on the sector with **SUNWAY REIT (BUY; TP: RM1.93)** as Top Pick. We also have **BUY** call on **AmanahRaya REIT (TP: RM1.15)**

2QCY17 earnings of REITs largely within expectations – For the recently concluded 2QCY17 earnings reporting season, most of the REITs under our coverage reported in line earnings. Among seven REITs under our coverage, only Pavilion REIT's earnings came in below expectations due to higher than expected property operating expenses incurred. Meanwhile, Sunway REIT registered highest earnings growth among seven REITs under our coverage where its cumulative earnings grew 7.2%yoy, mainly supported by the higher earnings contribution from Sunway Pyramid, Sunway Carnival, and Sunway Putra Mall. Overall, earnings of REITs were mixed in 2QCY17 whereby three REITs reported earnings growth while four REITs recorded lower earnings.

Figure 1: Summary of REITs earnings in 2QCY17

| No | Stock | Date of earnings released | Period Under Review | Cumulative Qtr Core Net Income (RM m) | Core Net Income % of our estimate | Earnings growth (yoy) | Against Estimates | Comment |
|----|---------------------|---------------------------|---------------------|---------------------------------------|-----------------------------------|-----------------------|-------------------|--|
| 1 | CMMT | 19-Jul | 2QFY17 | 80.2 | 48% | -0.8% | Within | Lower earnings due to weaker contribution from Sungei Wang Plaza (negative rental reversion) and The Mines (loss of an anchor tenant and lower rental rates) |
| 2 | Axis REIT | 24-Jul | 2QFY17 | 46.3 | 50% | 2.2% | Within | Earnings contribution from Scomi Facility in Rawang cushioned loss of income from Axis Eureka (disposed in March 2017) |
| 3 | Pavilion REIT | 27-Jul | 2QFY17 | 111.4 | 42% | -7.9% | Below | Lower earnings due to higher property expenses, higher borrowing cost, and temporary lower occupancy rate in Pavilion KL |
| 4 | IGB REIT | 2-Aug | 2QFY17 | 143.1 | 49% | 3.1% | Within | Earnings growth supported by positive rental reversion in Mid Valley Megamall and the Gardens Mall |
| 5 | Sunway REIT | 10-Aug | 4QFY17 | 270.4 | 100% | 7.2% | Within | Earnings growth mainly supported by growing contribution from Sunway Pyramid, Sunway Carnival, and Sunway Putra Mall. |
| 6 | KLCCP Stapled Group | 15-Aug | 2QFY17 | 354.7 | 49% | -1.6% | Within | Lower earnings from retail division while earnings from office division was flattish |
| 7 | AmanahRaya REIT | 29-Aug | 2QFY17 | 16.5 | 46% | -10.1% | Within | Topline growth of 5%yoy was offset by higher property operating expenses and higher manager's fees |

Source: MIDF Research

Slew of asset acquisitions announced. REITs are on acquisition trail with few asset acquisitions were announced recently. Firstly, Axis REIT had on 24th July 2017 announced that it is acquiring a pipe-coating factory in Kuantan for RM155m at net yield of 7%. Secondly, Pavilion REIT had on 27th July 2017 that is injecting Elite Pavilion Mall which is an extension of Pavilion KL shopping mall (NLA: 242k sf) for RM580m at gross acquisition yield of 6.4%. Lastly, Sunway REIT had on 3rd August 2017 announced the acquisition of Sunway Clio from Sunway Berhad for RM340m at yield of 6%. We are positive on the asset acquisitions as the asset acquisitions are estimated to be yield accretive.

Few changes to target prices – Over the 2QCY17 earnings reporting season, we have made few changes to target prices of REITs under our coverage. Firstly, target price for Sunway REIT revised upwards to RM1.93 from RM1.88, in line with earnings upward revision of 2.8% after factoring in earnings contribution from proposed acquisition of Sunway Clio. Similarly, target price for Axis REIT has been revised upwards to RM1.73 from RM1.68, after factoring in earnings contribution from proposed acquisition of a pipe-coating factory in Kuantan. On the other hand, target price for Pavilion REIT was reduced to RM1.70 from RM1.77 after we cut our earnings to account for the higher property expenses. Meanwhile, recommendations for REITs under our coverage remain intact. REITs with BUY calls include Sunway REIT (TP: RM1.93) and AmanahRaya REIT (TP: RM1.15) while REITs with NEUTRAL calls are Axis REIT (TP: RM1.73), IGB REIT (TP: RM1.73), KLCCP Stapled Group (TP: RM7.60), CMMT (TP: RM1.69), and Pavilion REIT (TP: RM1.70).

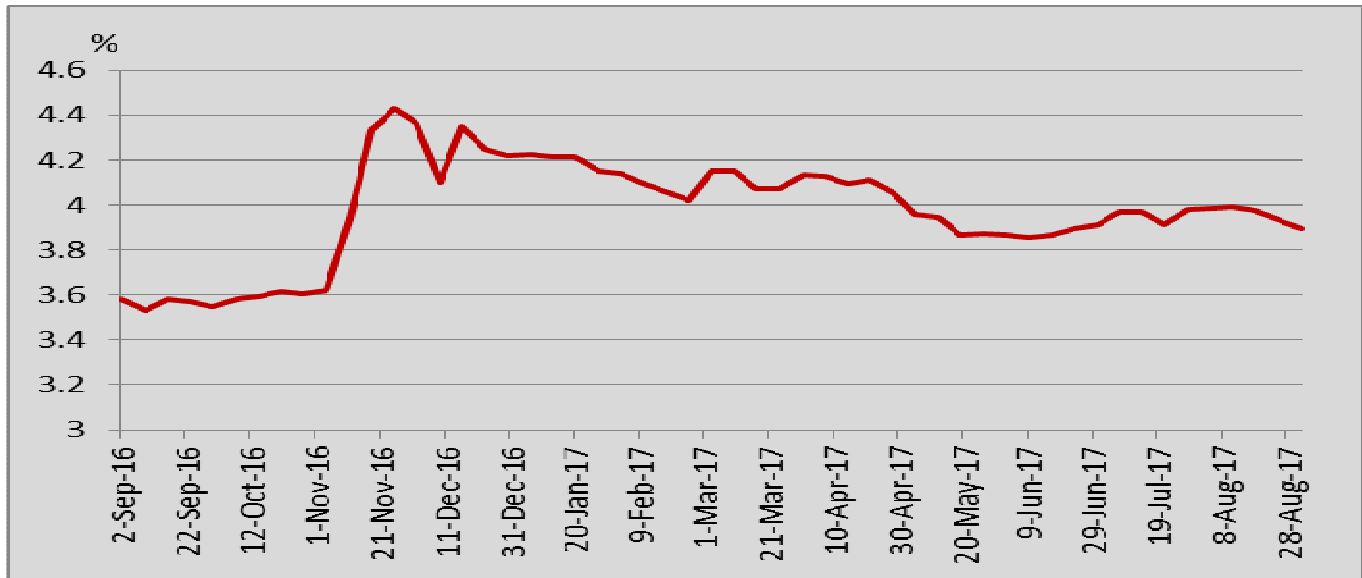
Figure 2: Peers comparison

| Stock | FYE | Rec. | Price @ 6-Sept | Target Price (RM) | Core EPU (sen) | | | Core PE (sen) | | Net DPS | | Net Dvd Yield | |
|----------------|-----|---------|----------------|-------------------|----------------|------|------|---------------|------|---------|------|---------------|------------|
| | | | | | FY16 | FY17 | FY18 | FY17 | FY18 | FY17 | FY18 | FY17 | FY18 |
| SUNREIT | Jun | BUY | 1.72 | 1.93 | 8.6 | 9.2 | 10.3 | 18.7 | 16.7 | 8.9 | 9.9 | 5.2 | 5.8 |
| ARREIT | Dec | BUY | 0.95 | 1.15 | 6.2 | 6.3 | 6.7 | 15.2 | 14.1 | 5.5 | 5.9 | 5.8 | 6.2 |
| AXREIT | Dec | NEUTRAL | 1.60 | 1.73 | 8.4 | 8.3 | 9.7 | 19.3 | 16.6 | 7.4 | 8.5 | 4.6 | 5.3 |
| CMMT | Dec | NEUTRAL | 1.47 | 1.69 | 8.1 | 8.2 | 8.5 | 18.0 | 17.4 | 7.8 | 8.1 | 5.3 | 5.5 |
| IGBREIT | Dec | NEUTRAL | 1.71 | 1.73 | 8.1 | 8.3 | 8.8 | 20.5 | 19.4 | 8.4 | 8.9 | 4.9 | 5.2 |
| PAVREIT | Dec | NEUTRAL | 1.73 | 1.70 | 7.8 | 7.7 | 8.6 | 22.6 | 20.2 | 7.1 | 7.9 | 4.1 | 4.6 |
| KLCC | Dec | NEUTRAL | 7.91 | 7.60 | 39.8 | 40.1 | 40.7 | 19.7 | 19.4 | 35.9 | 36.4 | 4.5 | 4.6 |
| Average | | | | | | | | | | | | 4.8 | 5.2 |


Source: MIDF Research

Easing MGS yield – 10-year MGS yield fell below 3.9% in September from ~4.0% in July due to flight to safety. Currently, 10-year MGS yield is hovering at 3.86%, close to its 5-year mean of 3.8%. We view the declining MGS yield to be positive to REITs as spread between yield of REITs and MGS yield widened, making REITs a more attractive yield asset. Further decline in MGS yield would provide catalyst to REITs. At this juncture, we are keeping our MGS yield assumption at 4%.

Figure 3: 10-Year MGS yield



Source: Bloomberg, MIDF Research

Maintain Neutral on REITs sector - Maintain Neutral on REITs sector with top pick being Sunway REIT. Our top pick for the sector is Sunway REIT (BUY; TP: RM1.93) due to its positive earnings outlook. We believe its retail division (Sunway Pyramid, Sunway Carnival, Sunway Putra Mall) will continue to spur earnings growth going forward. We also have Buy call on AmanahRaya REIT (TP: RM1.15) for its diversified assets base with exposure to education property and attractive dividend yield of 5.8%. 

Jessica Low Jze Tieng
jessica.low@midf.com.my
 03-21738391

MIDF RESEARCH is part of MIDF Amanah Investment Bank Berhad (23878 - X).

(Bank Pelaburan)

(A Participating Organisation of Bursa Malaysia Securities Berhad)

DISCLOSURES AND DISCLAIMER

This report has been prepared by MIDF AMANAH INVESTMENT BANK BERHAD (23878-X). It is for distribution only under such circumstances as may be permitted by applicable law.

Readers should be fully aware that this report is for information purposes only. The opinions contained in this report are based on information obtained or derived from sources that we believe are reliable. MIDF AMANAH INVESTMENT BANK BERHAD makes no representation or warranty, expressed or implied, as to the accuracy, completeness or reliability of the information contained therein and it should not be relied upon as such.

This report is not, and should not be construed as, an offer to buy or sell any securities or other financial instruments. The analysis contained herein is based on numerous assumptions. Different assumptions could result in materially different results. All opinions and estimates are subject to change without notice. The research analysts will initiate, update and cease coverage solely at the discretion of MIDF AMANAH INVESTMENT BANK BERHAD.

The directors, employees and representatives of MIDF AMANAH INVESTMENT BANK BERHAD may have interest in any of the securities mentioned and may benefit from the information herein. Members of the MIDF Group and their affiliates may provide services to any company and affiliates of such companies whose securities are mentioned herein. This document may not be reproduced, distributed or published in any form or for any purpose.

MIDF AMANAH INVESTMENT BANK : GUIDE TO RECOMMENDATIONS

STOCK RECOMMENDATIONS

| | |
|--------------|--|
| BUY | Total return is expected to be >15% over the next 12 months. |
| TRADING BUY | Stock price is expected to <i>rise</i> by >15% within 3-months after a Trading Buy rating has been assigned due to positive newsflow. |
| NEUTRAL | Total return is expected to be between -15% and +15% over the next 12 months. |
| SELL | Total return is expected to be <-15% over the next 12 months. |
| TRADING SELL | Stock price is expected to <i>fall</i> by >15% 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. |