

06 February 2015 | Sector Update

REIT 4QCY14 Earnings Wrap

Slower overall earnings growth

Maintain NEUTRAL

KEY HIGHLIGHTS

- 80% of REIT stocks' Core Net Income (CNI) came in within expectation.
- Earnings growth slowed down considerably to an average of 1.2%yoy.
- European QE has resulted in the decline of 10-year MGS yield. However, we expect the yield to edge up slightly moving ahead and hover at around 4.0%-4.5% by end of 2015. This is due to our expectation of US interest rate hike in 2HCY15.
- Challenging outlook in CY15 for REITs as GST and slower economic growth are likely to limit rental reversion growth for tenancies in shopping malls and industrial properties.
- Delay in the scheduled electricity tariff hike in 2015 will help to contain REITs' operating expenses.
- Reaffirm our NEUTRAL recommendation on the sector.

4QCY14 CNI (excluding revaluation gain on investment properties and other non-operating item) of REIT stocks was generally in line with expectations. In our universe of 5 REIT stocks, 4 stocks (80% of our coverage) reported earnings which came in within expectations while 1 was below expectation. AXREIT's FY14 Core Net Income (CNI) of RM80.1m came in lower than our estimate. This was due to an occupancy rate which was lower than what we had expected. We gather that this was attributed to Axis Business Campus (ABC) which has yet to be tenanted out. As for CMMT, IGBREIT, PAVREIT and SUNREIT, reported earnings of these 4 stocks fell within our estimates.

Marginal CNI growth of 1.2%yoy in 4Q14. Overall, average CNI for 5 REIT stocks under our coverage grew by a marginal 1.2%yoy. This was mainly caused by 7.5%yoy decline in AXREIT's CNI to RM19.5m as a result of the aforementioned reasons. On the other hand, IGBREIT registered the strongest CNI growth of 5.9%yoy to RM56.2m. We believe that this was likely contributed by the positive rental reversions for Mid Valley Megamall and The Gardens Mall.

MGS 10-year yield declined by 258 basis points (bp) but moving forward we expect volatility to persist in movement of the yield curve. Since the European Central Bank (ECB) announced Quantitative Easing (QE) on 22-Jan-2015, the yield on MGS 10-year yield has declined by 258bp to 3.718% up until 5th Feb 2015. Recall that ECB has announced its plan to buy €60b of euro-area bonds from central governments, agencies and European institutions government bonds on a monthly basis. Collectively up until Sep-2016, the amount to be spent will be circa 1.1 trillion euros (\$1.3 trillion). We believe that there has been some spill over effect of bond buying activities on MGS, consequently causing yields of MGS to decline. In our view, MGS yield should edge up slightly and stay around 4.0%-4.5% by end of 2015 as the US Fed is expected to raise interest rate in 2HCY15.

GST implementation may slow down consumer spending and limit FY15 CNI growth. After our recent meetings with several REIT players, we gather that there have been concerns on the implementation of GST (effective 1-Apr-2015) affecting consumer spending in the short term. We opine that REIT players will be affected albeit indirectly by GST as it may limit the potential rental reversion growth for shopping mall owners. As retailers face the risk of lower sales and higher cost (due to the need to pay additional 6% on top of the original rent), this may affect their ability to afford higher rental rates and hence limit the potential rental reversion growth for mall owners.

Delay in the scheduled electricity tariff hike in 2015 will temporarily halt REITs operating expenses from rising. In the recent Revised Budget 2015 on 20-Jan-2015, the Government has decided to postpone the scheduled electricity tariff hike this year. We are positive on this as “Utilities” (in which majority consist of Electricity cost) generally makes up between 33%-44% of total expenses for mall owners. Additionally, we believe that the assessment rate is unlikely to be raised again this year after the increase in 2014. Overall, we view the aforementioned delay as positive as it will contain the cost of REIT players from increasing.

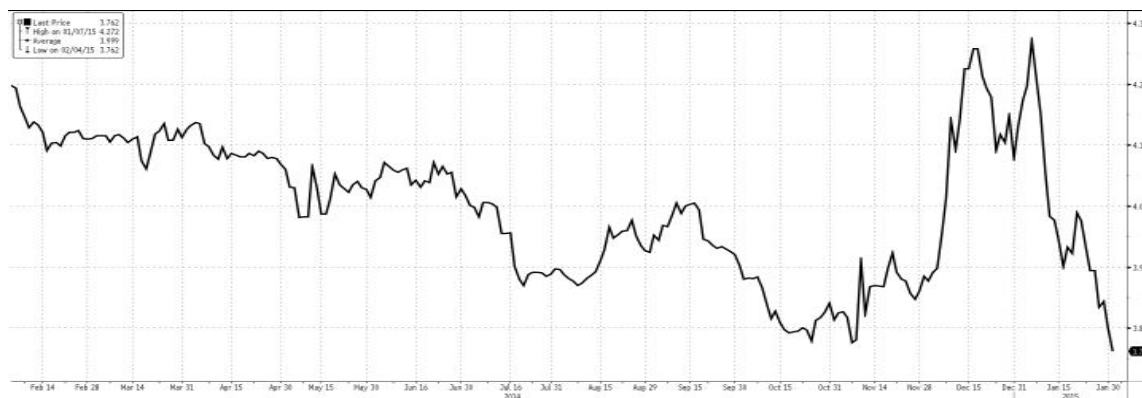
Reaffirm NEUTRAL on Malaysian REIT. We maintain our NEUTRAL view on the sector as we estimate that FY15 CNI growth is likely to be subdued in the range of 1.5%-5.3% for REITs under our coverage. As for MGS, we think that its yield may stay low in the short term (due to ECB’s QE) in 1QCY15. However, we do expect it to edge up slightly and stay around 4.0%-4.5% by end of 2015 as the US Fed is expected to raise interest rates in 2HCY15. Hence, we maintain our current assumption for average 10-year MGS yield at 4.20% (which is used as Risk Free Rate in our Dividend Discount Model).

Chart 1: Summary of REIT quarterly result

No	Stock	Period Under Review	Latest Qtr Core Net Income (RM m)	Growth yoy %	Expectation (Above/Within/Below)	Comment
1	AXREIT	4Q14 / FY14	19.5	-7.5%	Below	AXREIT FY14 CNI of RM80.1m came in below expectation accounting for only 90% of our estimate of RM88.6m. Overall occupancy rates was lower than expected as Axis Business Campus has yet to find its tenant.
2	CMMT	4Q14 / FY14	39.2	1.6%	Within	
3	IGBREIT	4Q14 / FY14	56.2	5.9%	Within	
4	PAVREIT	4Q14 / FY14	57.1	3.8%	Within	
5	SUNREIT	2Q15 / 1H15	63.3	2.0%	Within	

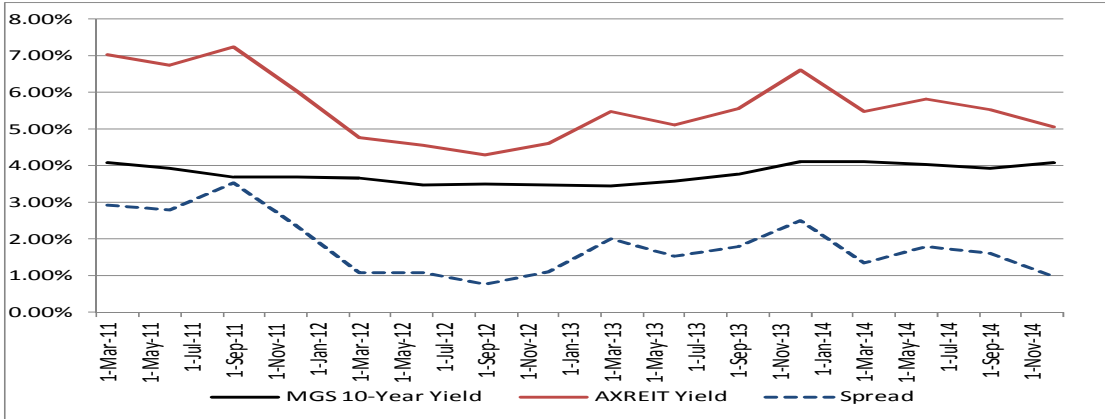
Source: Respective Company, MIDF Research

Chart 2: Malaysia Government Securities (MGS) 10-Year Yield



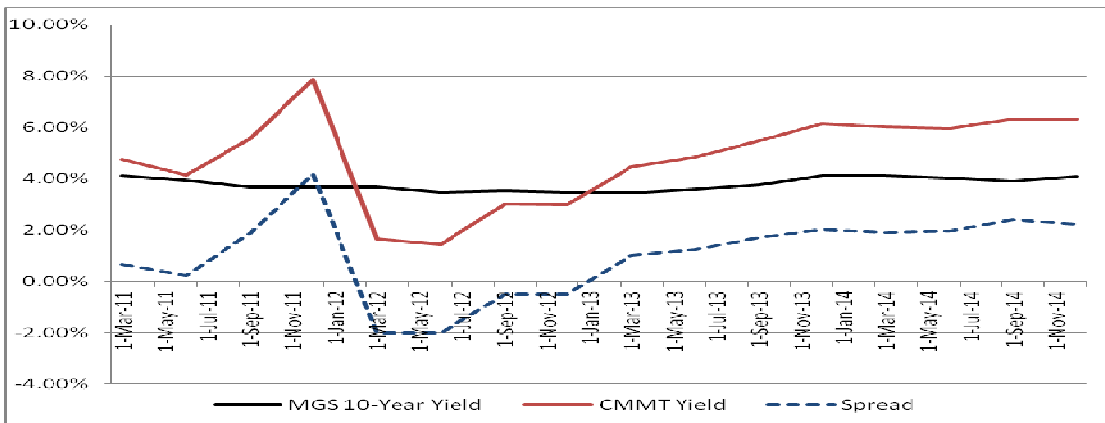
Source: Bloomberg

Chart 3: Spread between AXREIT Yield and 10 year MGS Yield



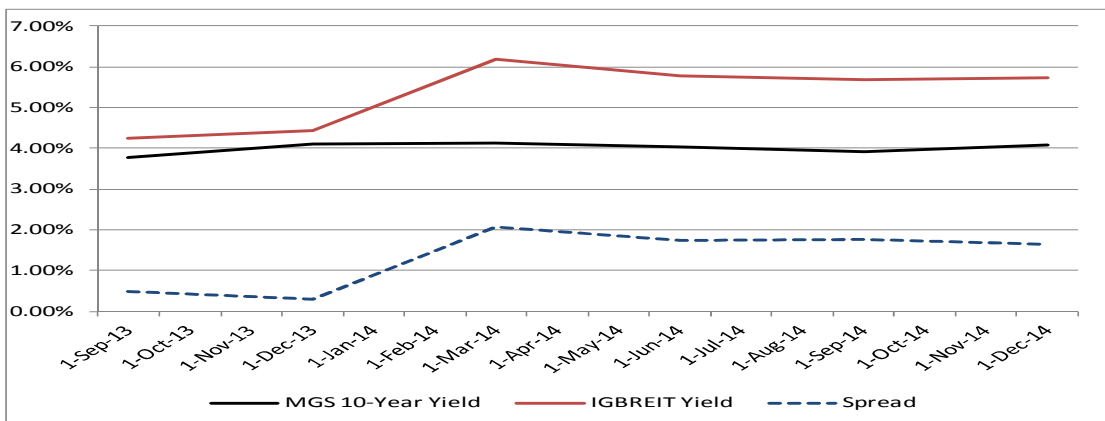
Source: Bloomberg

Chart 4: Spread between CMMT Yield and 10 year MGS Yield



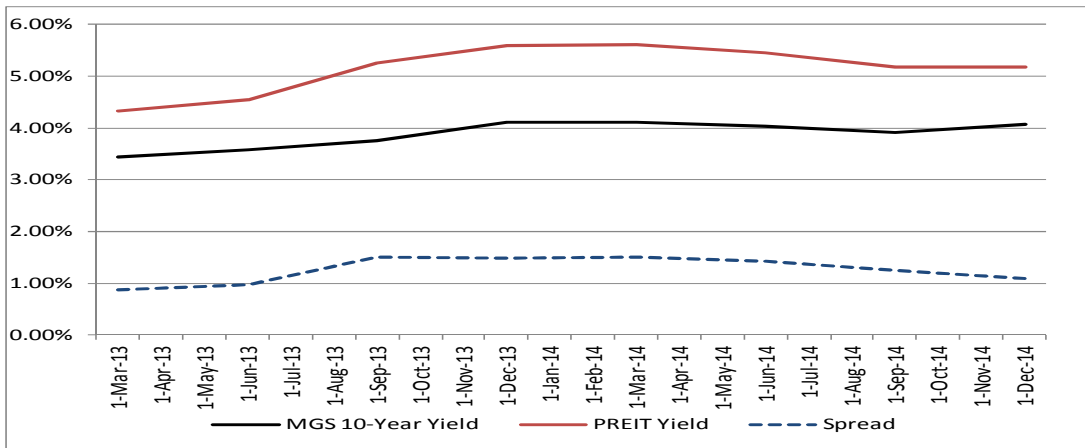
Source: Bloomberg

Chart 5: Spread between IGBREIT Yield and 10 year MGS Yield



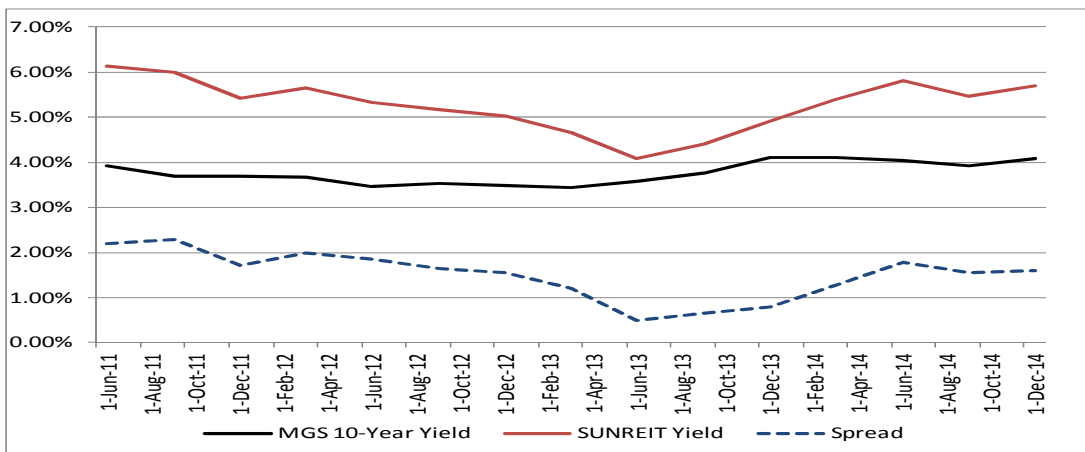
Source: Bloomberg

Chart 6: Spread between PAVREIT Yield and 10 year MGS Yield



Source: Bloomberg

Chart 7: Spread between SUNREIT Yield and 10 year MGS Yield



Source: Bloomberg

Chart 8: Peer Comparison

Stock	FYE	Recommendation	Price @ 5-Feb	Target Price (RM)	Core EPU (sen)		EPS (% chg)		Core PE (sen)		Net DPS		Net Dvd Yield	
					FY15	FY16	FY15	FY16	FY15	FY16	FY15	FY16	FY15	FY16
AXREIT	Dec	NEUTRAL	3.56	3.50	17.51	18.39	2.1%	5.0%	20.3	19.4	16.94	16.66	4.8	4.7
CMMT	Dec	NEUTRAL	1.43	1.66	8.31	8.71	1.5%	4.9%	17.2	16.4	7.92	8.30	5.5	5.8
IGBREIT	Dec	NEUTRAL	1.38	1.41	6.95	7.15	2.8%	2.8%	19.6	19.0	7.16	7.34	5.3	5.4
PAVREIT	Dec	NEUTRAL	1.48	1.57	7.99	8.41	3.6%	5.3%	18.5	17.6	7.42	7.79	5.0	5.3
SUNREIT	Jun	NEUTRAL	1.56	1.70	8.33	9.32	5.3%	11.9%	18.7	16.7	7.87	8.81	5.0	5.6

Source: MIDF Research Estimate

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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.