

06 October 2015 | Sector Update

**REITS***Safe choice but unexciting***Maintain NEUTRAL****KEY HIGHLIGHTS**


- **Latest quarterly results for REITs were in line with expectations**
- **Overall, average DPU for 6 REIT stocks under our coverage grew by 4.7%yoy**
- **We expect MGS yields to continue being volatile in the near-term**
- **We believe sluggish consumer sentiment and oversupply of office space will persist**
- **We remain NEUTRAL on the sector with Top Picks: IGBREIT (BUY; TP: RM1.46) and CMMT (BUY; TP: RM1.66).**

**Latest quarterly results for REITs were in line with expectations.** In our universe of 6 REIT stocks, only KLCC's earnings came in above expectations while the remaining reported earnings which were within expectations. Note that KLCC operating expenses unexpectedly declined by 3%yoy to RM160m possibly due cost saving measure implemented particularly within the hotel division. The remaining 5 REIT stocks with earnings that matched expectation are AXREIT, CMMT, IGBREIT, PAVREIT and SUNREIT.

**Overall, average DPU for 6 REIT stocks under our coverage grew by 4.7%yoy.** IGBREIT registered the strongest DPU growth of 11%yoy. The superior DPU growth was in line with a -8% reduction in operating expenses due to lower utilities and reimbursement costs.

**We expect MGS yields to continue being volatile in the near-term** due to global economic and interest rate uncertainties. This is likely to impact the stability of the spreads between REIT-MGS yield. Note that the standard deviation (SD) for MGS 10-year yield has increased to 0.16 for the period from 7-April-2015 to 6-Oct-2015. This is higher than its SD of 0.13 in the prior 6 months. On interest rates, our economist expects BNM to maintain OPR at 3.25% for the rest of the year. This should keep financing cost stable for all REIT players.

**We believe sluggish consumer sentiment will persist** with cautious approach taken given the weak Ringgit and GST implementation. This could affect REITs with exposure to shopping malls (IGBREIT, KLCC, CMMT, PAVREIT and SUNREIT) as rental reversion growth corresponds with tenants' business revenue. This could result in flattish FY15 CNI growth for REITs. Meanwhile, REITs with office exposure (AXREIT and SUNREIT) may face increased competition due to influx of new office space. We gather that an additional supply of 5.9m sq. ft. is expected to come in by end of this year.

**We remain NEUTRAL on the sector with Top Picks: IGBREIT (BUY; TP: RM1.46) and CMMT (BUY; TP: RM1.66).** We like IGBREIT due to: (i) dividend growth of 11%yoy in 1HFY15 is higher than peers' average of 3.4%, (ii) its strong ability to contain expenses, and (iii) minimal risk to interest rate increase as 98% of its loans are in fixed rate. Meanwhile, our BUY call on CMMT is premised on (i) our view that the market has underappreciated the earnings contribution from the acquisition of Tropicana City Mall, (ii) its net dividend yield at 5.8% is the highest among peers (sector average: 5.2%) and (iii) potential recovery in Sungei Wang Plaza occupancy rate after completion of MRT construction. We are NEUTRAL on KLCC (TP: RM6.93), AXREIT (TP: RM1.75), PAVREIT (TP: RM1.57) and SUNREIT (TP: RM1.62). 

**Table 1: Summary of REITS' Quarterly Results**

No	Stock	Period Under Review	Latest Qtr Core Net Income (RM'm)	Expectation (Above/Within/Below)	Core DPU Growth yoy %	Comments
1	AXREIT	2Q15 / 6M15	23.7	Within	5%	Growth supported by new acquisitions, i.e. MRO Hub, Axis Shah Alam DC3, SiLC and Axis Shah Alam DC2.
2	CMMT	2Q15 / 6M15	36.5	Within	0%	Revenue from The Mines, East Coast Mall and Gurney Plaza balanced lower contribution from Sungei Wang Plaza.
3	IGBREIT	2Q15 / 6M15	65.8	Within	11%	NLA increased by +1.5% due to reconfiguration of layout; -8% reduction in operating expenses.
4	KLCC	2Q15 / 6M15	179.9	Above	4%	Improvements in office and retail offset lower hotel (Mandarin Oriental) contributions.
5	PAVREIT	2Q15 / 6M15	59.3	Within	7%	Asset enhancement initiatives increased net leasable area. Recently, they have acquired Da Men USJ for RM488m which will increase FY16 CNI by 2%.
6	SUNREIT	4Q15 / 12M15	56.7	Within	1%	Double digit rental reversion and improved occupancy for retail segment offset weaker hotel and office segment

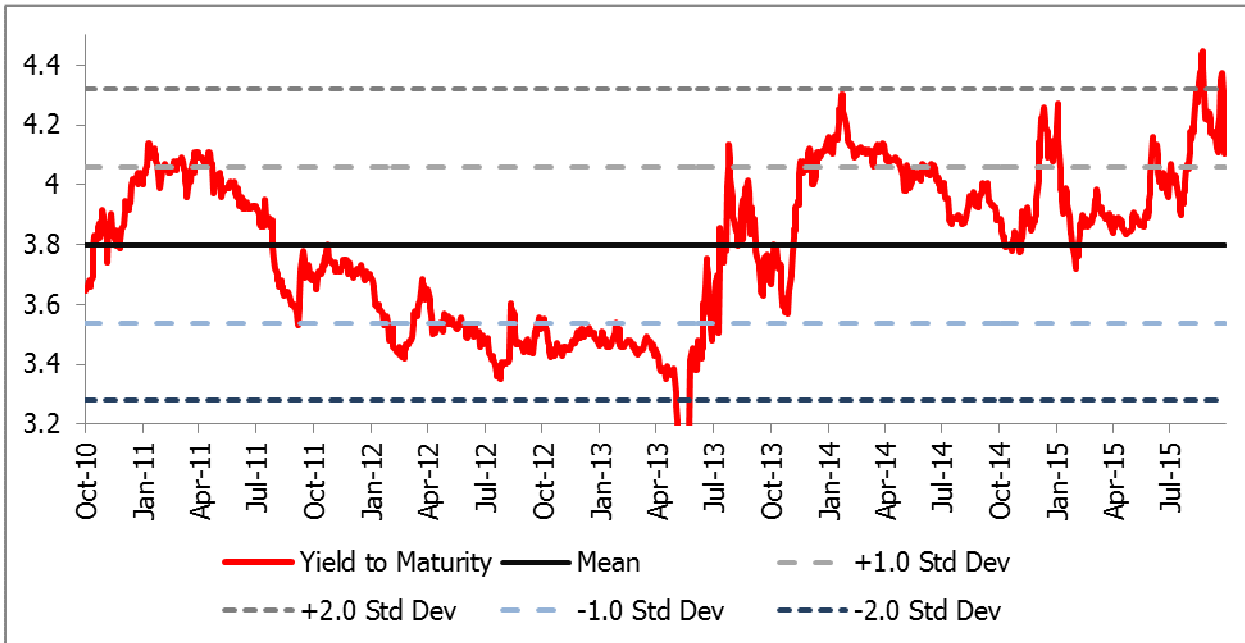
Source: Respective companies, MIDF Research

**Table 2: Peer Comparison**

Stock	FYE	Rec.	Price @ 5-Oct	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	1.65	1.75	8.75	9.19	1.8	5.0	18.9	17.9	8.47	8.33	5.1	5.0
CMMT	Dec	BUY	1.39	1.66	8.53	8.69	1.2	1.9	16.3	16.0	8.13	8.30	5.8	6.0
IGBREIT	Dec	BUY	1.30	1.46	7.14	7.23	5.5	1.1	18.2	18.0	7.31	7.40	5.6	5.7
PAVREIT	Dec	NEUTRAL	1.50	1.57	7.99	8.41	3.6	5.3	18.8	17.8	7.42	7.79	4.9	5.2
SUNREIT	Jun	NEUTRAL	1.54	1.62	8.23	8.59	3.7	4.4	18.7	17.9	7.85	8.21	5.1	5.3
KLCC	Dec	NEUTRAL	7.04	6.93	33.05	34.41	2.5	4.1	21.3	20.5	31.1	32.4	4.4	4.6
<b>Average</b>							<b>3.0</b>	<b>3.6</b>	<b>18.7</b>	<b>18.0</b>			<b>5.2</b>	<b>5.3</b>

Source: MIDF Research Estimate

Chart 1: 10yr MGS Yield to Maturity



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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.