

06 June 2018 | Sector Update

REITs

Upside Limited After Unit Price Increase

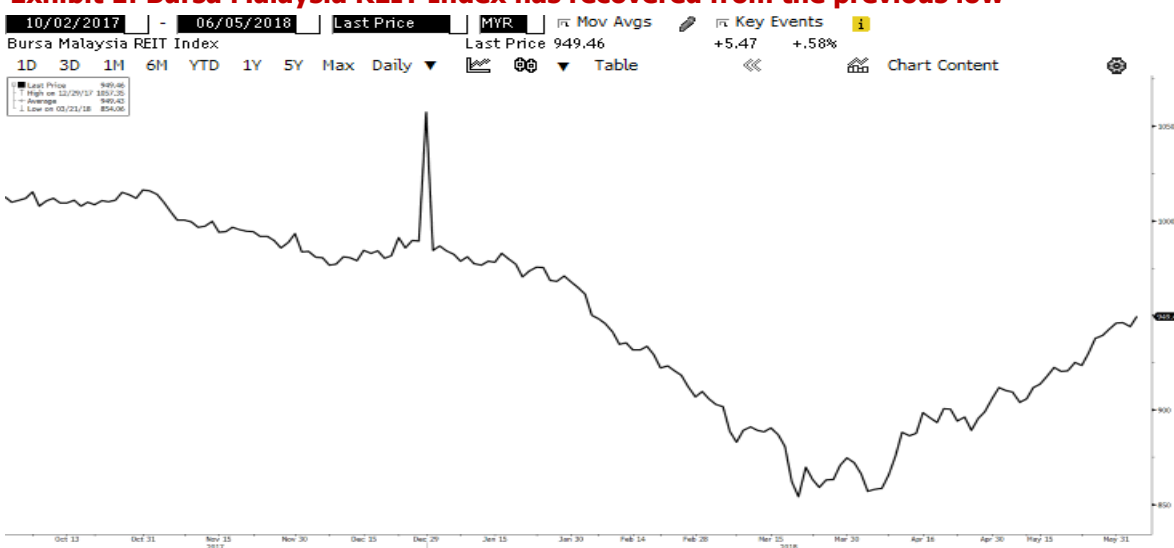
Downgrade to NEUTRAL
(Previously Overweight)

KEY HIGHLIGHTS

- Prices of REITs under our coverage have recovered
- Yield spread narrowing
- 1QCY18 earnings of REITs under coverage were mixed
- We downgrade the sector to **NEUTRAL** with **SUNWAY REIT (BUY; TP: RM1.90)** as our Top Pick

Prices of REITs under our coverage have recovered. Since our report dated April 10th, 2018 titled "Looking more attractive", Bursa Malaysia REIT index has climbed +8.5%. For stocks under our coverage, share price had climbed by +3% to +21%. Prior to that, they have fallen by about -12.6% on average since the beginning of 2018. In view of the limited upside from the current share price, we are downgrading the sector to NEUTRAL.

Exhibit 1: Bursa Malaysia REIT Index has recovered from the previous low



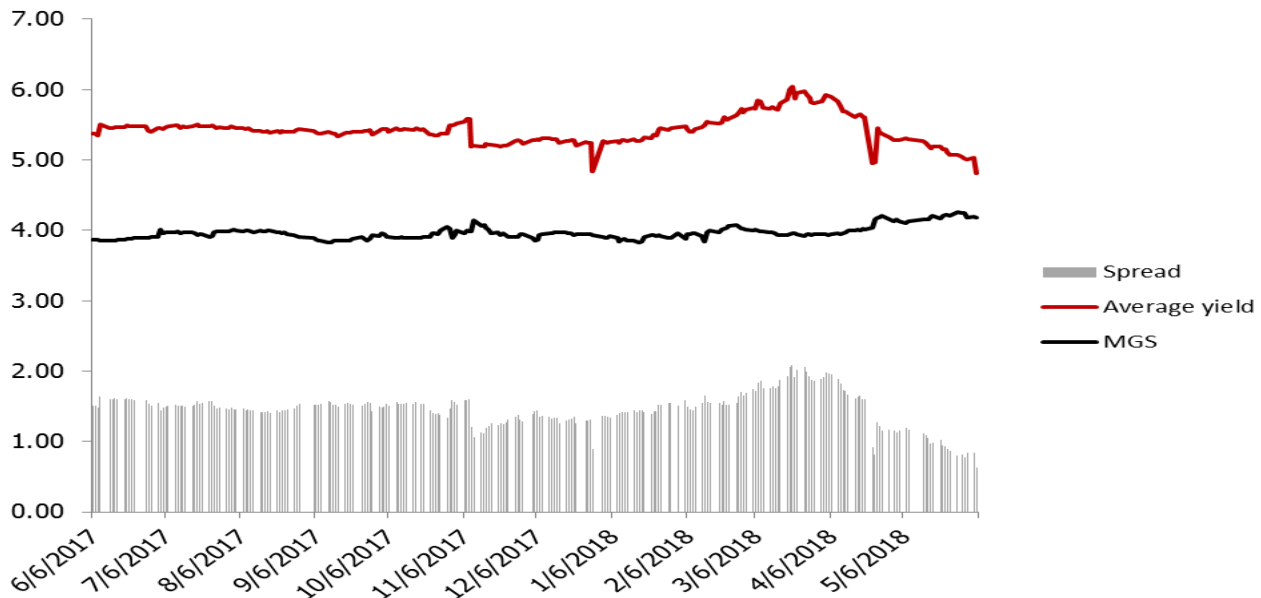
Source: Bloomberg, MIDF Research

Exhibit 2: Price changes for REITs under our coverage since our sector report on April 10

Axis REIT	21%
Amanahraya REIT	3%
CMMT	10%
IGB REIT	9%
KLCCP	9%
Pavilion REIT	9%
Sunway REIT	12%

Yield spread narrowing. Previously, yield spread between MREITs and Malaysian Government Securities (MGS) widened to about 2.3 percentage point (ppt). However, this has changed following the uptrend of MGS yield, which now averages at 4.0% ytd compared with 3.95% in our previous sectoral update. The current spread is just under 0.7 ppt. We maintain our MGS yield assumption of 4.0% for the year but we notice that the spread between MGS yield and REITs under our coverage has narrowed to a less attractive level.

Exhibit 3: Spread between average yield of REITs under coverage and MGS-10 year yield narrowing



Source: Bloomberg, MIDF Research


1QCY18 earnings of REITs under coverage were mixed. Results for five out of the seven REITs that we track were largely in-line with our full year forecasts. The two REITs with earnings below our expectations were Amanahraya REIT and Axis REIT, mainly due to higher than expected expenses. We have recently downgraded Axis REIT to NEUTRAL (TP:RM1.55) as its unit price has increased by about 20% since April.

Exhibit 4: Summary of REITs under coverage

Stock	FYE	Rec.	Price @ 4 Jun	Target Price (RM)	Core EPU (sen)			Core PE (sen)		Net DPU		Net Dvd Yield		Price to NAV
					FY17	FY18	FY19	FY18	FY19	FY18	FY19	FY18	FY19	
AXREIT	Dec	NEUTRAL	1.54	1.55	8.3	9.1	10.0	16.9	15.4	8.0	8.8	5.2	5.7	1.2
CMMT	Dec	NEUTRAL	1.25	1.11	7.8	7.9	8.0	15.8	15.6	7.5	7.7	6.0	6.2	0.9
IGBREIT	Dec	BUY	1.64	1.73	8.6	8.7	9.2	18.9	17.8	9.4	8.8	5.7	5.4	1.5
PAVREIT	Dec	NEUTRAL	1.54	1.41	7.7	8.3	8.4	18.6	18.3	7.7	7.8	5.0	5.1	1.2
KLCC	Dec	NEUTRAL	7.75	7.59	40.0	40.7	41.9	19.0	18.5	35.4	36.4	4.6	4.7	1.0
SUNREIT	Jun	BUY	1.70	1.90	9.2	9.7	10.3	17.5	16.5	8.7	9.3	5.1	5.5	1.2
ARREIT	Dec	BUY	0.86	0.94	5.5	6.5	7.3	13.2	11.7	5.6	6.4	6.5	7.5	0.5
Average												5.5	5.7	1.1

Source: Companies, MIDF Research

2HCY18 could be better for retail REITs given the upcoming Raya celebration, which is followed by World Cup 2018, which may see higher footfall in major malls that usually organise crowd pulling events and promotions. The reduction of GST from 6% to 0% starting June 1 should also spur consumer spending, which could spill over to shopping malls. We expect malls at strategic locations to command single-digit positive rental reversion while growth for rental reversion for neighbourhood malls may be tepid or flat.

Downgrade to NEUTRAL from OVERWEIGHT. We downgrade the sector to NEUTRAL from OVERWEIGHT as unit prices for REITS have recovered by between 3% to 21% since our previous report "Looking more attractive" in April. While earnings are expected to be resilient in the near-term, the recovery in unit prices had narrowed the valuation gap. Our top pick for the sector is Sunway REIT (BUY; TP: RM1.90) due to its positive earnings outlook that is backed by positive rental reversion from Sunway Pyramid and growth from its hotel division. We also have a BUY call on AmanahRaya REIT (TP: RM0.96) for its diversified assets base with exposure to education property. We also like IGB REIT (BUY; TP: RM1.73) for its ability to command positive rental reversion for its crown jewel Mid Valley Megamall. 

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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.