REIT

Maintain POSITIVE

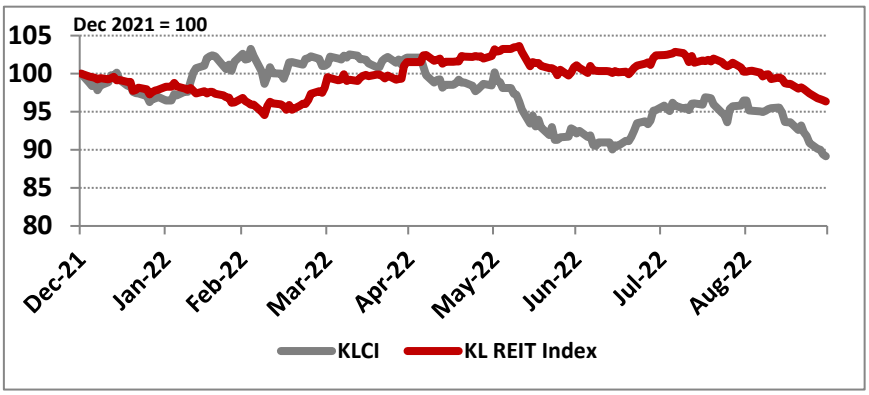
Positive outlook intact

KEY INVESTMENT HIGHLIGHTS

- **KL REIT Index outperformed KLCI**
- **Outlook for retail segment remains bright**
- **Industrial segment remains resilient**
- **Challenging outlook for office segment**
- **Retail segment and hotel segment may benefit from Budget 2023**
- **Maintain POSITIVE on REIT**

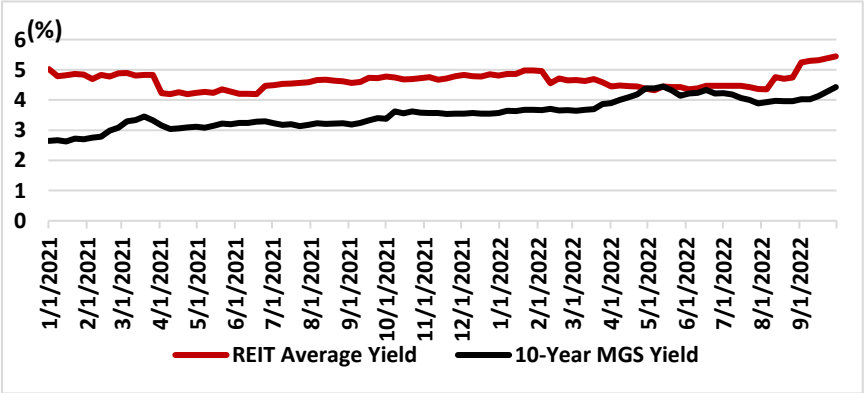
KL REIT Index outperformed KLCI. As broader market succumbed to sell off due to backdrop of rising interest rate, KL REIT Index outperformed KLCI by registering lower YTD loss of -3.7% against KLCI YTD losses of -10.8% due to the defensiveness of REITs. The decline in KL REIT Index is also due to hike in OPR and narrowing spread between MGS yield and yield of REIT which reduced attractiveness of REIT. While we reckon that rising interest rate would increase financing cost of REITs, we see the broader outlook for REITs remain positive in 4QCY22 and CY23 due to recovery in rental income and higher tourist arrivals. Besides, average distribution yield of REIT is expected to recover to 5.7% in CY23 which we deem remains attractive against MGS yield of 4.4%.

Figure 1: Performance of KL REIT Index against KLCI



Source: Bloomberg, MIDF Research

Figure 2: Spread between MGS Yield and REIT



Source: Bloomberg, MIDF Research

COMPANY IN FOCUS

IGB REIT

Maintain **BUY** | Unchanged Target price: RM1.78
Price @ 30th Sept 2022: RM1.60

- Earnings surged by 92% in 1HFY22, underpinned by lower rental support to tenants and higher footfall.
- Earnings outlook remains positive due to positive rental reversion at Mid Valley Megamall and The Gardens Mall.
- Distribution yield is estimated at 5.1%.

Share price chart



Sunway REIT

Maintain **BUY** | Unchanged Target price: RM1.68
Price @ 30th Sept 2022: RM1.40

- Earnings jumped by 131%yoy, driven by earnings recovery of retail division
- Earnings in 2HFY22 to remain strong due to recovery of retail and hotel division.
- Distribution yield is estimated at 5.5%.

Share price chart



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Outlook for retail segment remains bright. Retail REITs reported earnings recovery in 1HCY22 due to recovery in shopper footfall and significant lower rental assistance to tenants. We gather that shopper footfall at the established malls such as Sunway Pyramid and Mid Valley Megamall had recovered close to pre-pandemic level. Meanwhile, tenant sales improved and that led to rental reversion returned to positive territory. Looking ahead, we expect earnings of retail REITs to remain strong in 4QCY22 mainly due to positive rental reversion outlook. Besides, year-end shopping spree and holiday season should also support earnings of retail REITs due to higher turnover rents.

Industrial segment remains resilient. Earnings of industrial REITs namely Axis REIT were resilient as it recorded core earnings growth of +29%yoy and +14.5%yoy growth in core EPU. The solid earnings were underpinned by positive rental reversion and contribution from newly acquired assets. We see that performance of industrial REITs would remain stable going forward due to solid demand for industrial space particularly due to growing demand from e-commerce. While we may see a slowdown in e-commerce post Covid as people spend at physical store, we think that e-commerce will remain doing well in long-term and demand for industrial space will stay supported.

Challenging outlook for office segment. Demand for office space was weaker in the past two years due to Covid-19 pandemic following structural shift of more hybrid working. Nevertheless, with the reopening of economic activities and more employees are encouraged to work from office, we expect demand for office space to recover gradually. In this context, we expect occupancy rate of office building to improve. Nevertheless, we think that office space will remains tenants' market due to the oversupply concern of office space. Hence, we see challenging outlook for office segment with rental reversion outlook to remain in flattish to negative territory.

Retail segment and hotel segment may benefit from Budget 2023. The tabling of Budget 2023 is set to be on 7th October 2022 and it is widely expected that cash goodies will be dished out to B40 group. If the expectation of cash goodies materializes, we would expect some spillover effect to retail REIT as people will allocate a portion of the cash goodies for retail spending. Besides, we see the potential incentives from Budget 2023 to promote tourism sector of Malaysia would be positive to REITs. The higher tourist arrival would help improve footfall of shopping malls and help in tenants' sales. The higher tourist arrival will also help hotel industry as some REITs such as Sunway REIT and KLCCP Stapled Group have exposure to hotel industry.

CY23 outlook remains positive. Outlook for REITs is expected to remain positive in CY23 as risk of another lockdown is low. As Malaysia is transitioning from Covid-19 pandemic to endemic, economic activities are expected to fully normalized in CY23 and that would support recovery of REITs. In addition, potential more country border reopening in CY23 particularly China is expected to benefit retail and hotel industry of Malaysia as that will lift tourist arrival significantly. In this context, we see REITs such as Pavilion REIT, KLCCP Stapled Group and Sunway REIT to benefit from higher tourist arrival in CY23 as their retail malls are tourist destinations.

Maintain POSITIVE on REIT. We maintain our Positive stance of REIT as we expect REITs especially retail REITs to continue registering earnings recovery in 4QCY22 and CY23 due to improving shopper footfall and tenant sales. Besides, industrial REITs and healthcare REIT are expected to deliver stable earnings going forward due to resilient earnings from industrial and healthcare assets. Our top picks for the sector are **IGB REIT (BUY, TP: RM1.78)** and **Sunway REIT (BUY, TP: RM1.68)** as we see earnings outlook to underpin by positive rental reversion outlook and good quality retail assets namely Mid Valley Megamall and Sunway Pyramid. Distribution yields for IGB REIT and Sunway REIT are estimated at 5.1% and 5.5% respectively.

Figure 3: Peer comparison table

Stock	Rec.	Price @ 30-Sept	Target Price (RM)	Core EPU (sen)			Core PE (x)		Net DPS (sen)		Net Dvd Yield (%)	
				FY21	FY22F	FY23F	FY22F	FY23F	FY22F	FY23F	FY22F	FY23F
IGB REIT	BUY	1.60	1.78	5.6	8.9	9.9	18.0	16.2	8.2	9.1	5.1	5.7
KLCCP Stapled Group	NEUTRAL	6.59	7.15	34.2	39.2	42.1	16.8	15.6	33.9	36.5	5.2	5.5
Al-Aqar Healthcare REIT	BUY	1.18	1.38	9.2	9.6	8.8	12.2	13.5	7.4	7.1	6.2	6.0
Axis REIT	BUY	1.89	2.16	9.2	10.8	11.0	17.5	17.2	9.5	9.6	5.0	5.1
Sunway REIT	BUY	1.40	1.68	7.4	9.2	9.5	15.3	14.8	7.7	8.5	5.5	6.1
Pavilion REIT	BUY	1.26	1.56	3.7	7.5	7.8	16.9	16.2	6.9	7.2	5.5	5.7
Average											**5.4**	**5.7**

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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 *rise* 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 *fall* 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.
ESG RECOMMENDATIONS* - source Bursa Malaysia and FTSE Russell	
☆☆☆☆	Top 25% by ESG Ratings amongst PLCs in FBM EMAS that have been assessed by FTSE Russell
☆☆☆	Top 26-50% by ESG Ratings amongst PLCs in FBM EMAS that have been assessed by FTSE Russell
☆☆	Top 51%- 75% by ESG Ratings amongst PLCs in FBM EMAS that have been assessed by FTSE Russell
☆	Bottom 25% by ESG Ratings amongst PLCs in FBM EMAS that have been assessed by FTSE Russell

* ESG Ratings of PLCs in FBM EMAS that have been assessed by FTSE Russell in accordance with FTSE Russell ESG Ratings Methodology