REIT

***Maintain* POSITIVE**

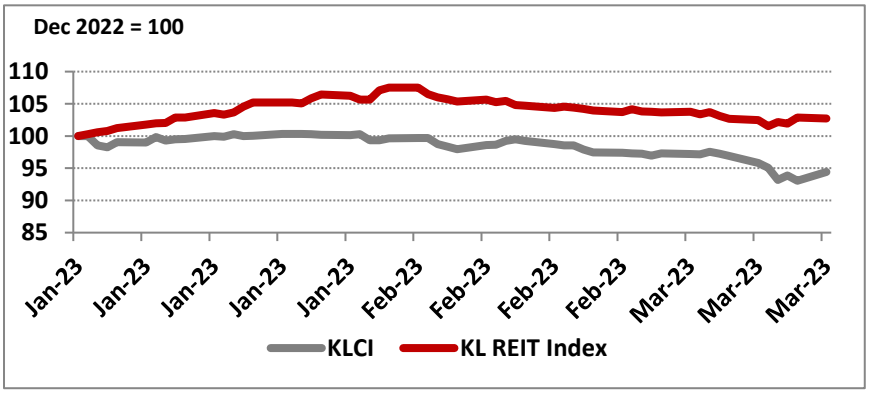
A safe haven during market turmoil

KEY INVESTMENT HIGHLIGHTS

- **Resilient KL REIT Index**
- **Tapering of MGS yield is positive to REIT**
- **Solid performance of retail REIT**
- **Industrial segment remains defensive**
- **Hotel industry sees light at the end of tunnel**
- **Maintain POSITIVE on REIT**

Resilient KL REIT Index. Broader market suffered heavy losses due to collapse of Silicon Valley Bank and fallout of Credit Suisse which trigger worries over a banking crisis. KLCI lost -1.5% in a week after the collapse of Silicon Valley Bank. Nevertheless, performance of KL REIT Index was resilient by registering a gain of +0.2% during the same period. The outperformance of KL REIT Index could be attributed to the defensiveness of REIT which provide stable yield. Meanwhile, KL REIT Index outperformed KLCI by recording gains of +2.3% YTD against KLCI's losses of -6% YTD. We see that investors could be seeking shelter in REIT amid market uncertainty as overall outlook for REIT in Malaysia remains positive, unfazed by the turmoil in oversea markets.

Figure 1: Performance of KL REIT Index against KLCI



Source: Bloomberg, MIDF Research

Tapering of MGS yield. The 10-year Malaysian Government Securities (MGS) yields raised to above 4.5% in October 2022 due to hike of interest rate by Federal Reserves and OPR hikes in Malaysia. The increasing MGS yield hampered interest on REIT as higher MGS yield reduced attractiveness of REIT. Nevertheless, MGS yield tapered down to below 4% in March 2023 as BNM paused its rate hike. Looking ahead, we expect MGS yield to remain below 4% as our economist expect BNM may continue to maintain OPR at 2.75% for the rest of 2023 due to uncertainty over local and global market conditions. In a nutshell, the tapering of MGS yield is positive to REIT as it widened spread between 10-Year MGS Yield and yield of REITs and thus increases attractiveness of REIT for yield seeking investors.

COMPANY IN FOCUS

IGB REIT

Maintain **BUY** | Unchanged Target price: RM1.86
Price @ 21st March 2023: RM1.72

- Strong earnings growth (+68%yoy) in FY22 due to recovery in rental income and car park income.
- Positive earnings outlook in FY23 due to high shopper footfall and high occupancy rates of Mid Valley Megamall and The Gardens Mall.
- Distribution yield is estimated at 5.3%.

Share price chart



Sunway REIT

Maintain **BUY** | Unchanged Target price: RM1.73
Price @ 21st March 2023: RM1.55

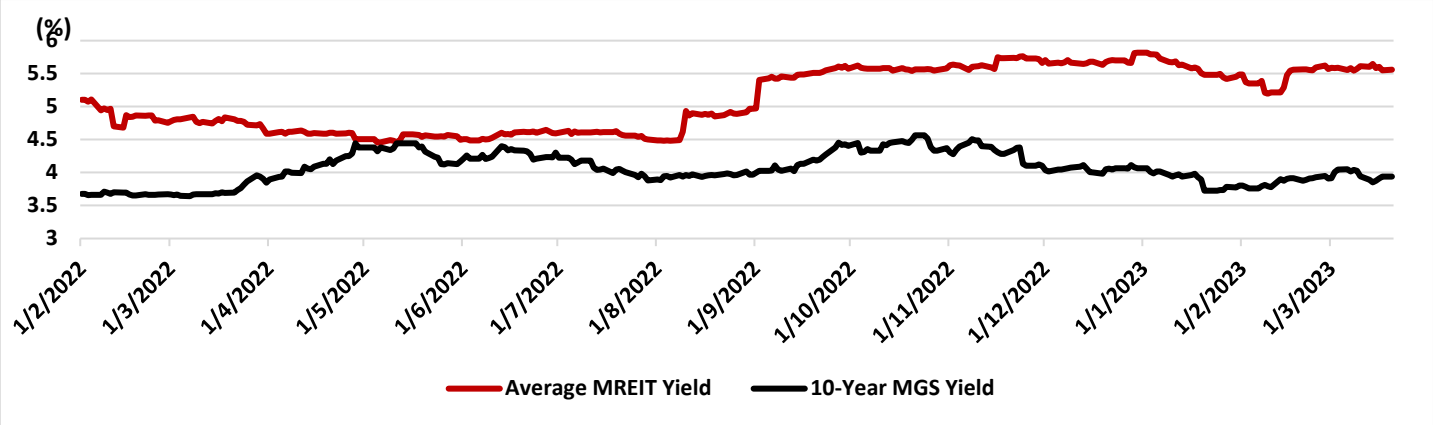
- FY22 earnings jumped to RM336.6m (+82%yoy), supported by recovery of retail and hotel divisions.
- Positive earnings outlook due to positive rental reversion outlook for retail segment and higher contribution from hotel division.
- Distribution yield is estimated at 5.9%.

Share price chart



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Figure 2: Spread between MGS Yield and REIT



Source: Bloomberg, MIDF Research

Solid performance of retail REIT. Most of the retail REIT reported earnings growth in CY22 due to recovery in rental income and lower assistance to tenants. Tenant sales and shopper footfall recovered to pre-pandemic level post reopening of economy. That led to rental reversion of shopping malls in prime location returning to positive territory in CY22. Looking forward, performance of retail REIT is expected to remain steady particularly for REIT with mall in good location such as IGB REIT, Sunway REIT, Pavilion REIT and KLCCP Stapled Group. Besides, retail spending is also expected to be supported by festive season in 2QCY23 and higher tourist arrival. Hence, we expect stronger tenant sales in 2QCY23 and rental reversion to remain in positive territory.

Industrial segment remains defensive. Earnings performance of industrial REIT was encouraging, relatively unfazed by Covid-19 pandemic as demand for industrial space remained strong. Despite consumers shop at physical store post reopening of economy, consumers remain shopping on-line and that support demand for warehousing space. Meanwhile, the defensiveness of industrial assets attracted interest of several REITs such as KIP REIT and Capitaland Malaysia Trust (CLMT) venturing into industrial space. We see that the growing competition among REITs in the industrial space may compress acquisition yield for industrial assets going forward.

Hotel industry sees light at the end of tunnel. Hotel industry is expected to turnaround in CY23 due to growth in domestic tourism and higher tourist arrival. Recall that hotel industry suffered from heavy losses in CY20 and CY21 due to closure of country border. With recovery of tourism industry and opening of more country borders particularly China, tourist arrival is expected to increase significantly in CY23 and that will support recovery of hotel industry. Occupancy rate and average room rate (ARR) of hotels improved in 2HCY22 post reopening of economy and we expect further recovery of occupancy rate and ARR in CY23 due to higher tourist arrival. In this context, we expect REIT with exposure to hotel industry namely Sunway REIT and KLCCP Stapled Group to see better earnings contribution from hotel division.

Cost of borrowings. BNM paused OPR hike for two consecutive time in 2023. As our economist expect OPR to remain unchanged at 2.75% for the rest of 2023, we see that to be positive for REIT as it eases concern over rising borrowing cost for REIT. Particularly, the pause in OPR provides relief to REIT with high floating rate borrowings such as Al-Aqar Healthcare REIT with 100% Islamic financing on floating rate, Sunway REIT with 68% debt on floating rate and Pavilion REIT with 65% financing on floating rate. Hence, we see risk of higher borrowing cost for REIT is low in the near-term and earnings growth should remain intact.

Maintain POSITIVE on REIT. Overall, we see earnings of REIT with exposure to retail and hotel industry to improve further in CY23 due to recovery of consumer spending at malls and higher tourist arrivals. Similarly, industrial REIT namely Axis REIT is expected to report stable earnings due to solid demand for industrial space. In a nutshell, we are positive on earnings outlook for REIT in CY23 which offer decent average yield of 5.3%. We think that the defensiveness of REIT could provide shelter for investors amid market uncertainty. Hence, we maintain **POSITIVE** on REIT with top picks are **IGB REIT (BUY, TP: RM1.86)** and **Sunway REIT (BUY, TP: RM1.73).**

Figure 3: Peer comparison table

Stock	Rec.	Price @ 21-March	Target Price (RM)	Core EPU (sen)			Core PE (x)		Net DPS		Net Dvd Yield (%)	
				FY22	FY23F	FY24F	FY23F	FY24F	FY23F	FY24F	FY23F	FY24F
IGB REIT	BUY	1.72	1.86	9.4	10.0	10.4	17.3	16.5	9.1	9.5	5.3	5.5
KLCCP Stapled Group	NEUTRAL	6.83	7.15	37.9	42.2	43.1	16.2	15.8	36.7	36.7	5.4	5.4
Al-Aqar Healthcare REIT	BUY	1.32	1.38	9.5	8.8	8.6	15.1	15.3	7.1	7.0	5.4	5.3
Axis REIT	BUY	1.89	2.06	9.5	9.1	9.3	20.8	20.2	8.0	8.2	4.2	4.3
Sunway REIT	BUY	1.55	1.73	9.8	10.2	10.4	15.2	14.8	9.2	9.4	5.9	6.1
Pavilion REIT	BUY	1.32	1.63	8.1	8.2	8.1	16.2	16.4	7.7	7.4	5.9	5.6

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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