IGB REIT's rental income growth remains robust

The Editor / TheEdge
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IGB Real Estate Investment Trust(May 2, RM1.19)Maintain buy with target price of RM1.34: IGB REIT registered realised net profit of RM57.7 million (+17.1% year-on-year [y-o-y]) for the first quarter ended March 31 of financial year 2014 (1QFY14). Annualised, it was 6% higher than our estimate of RM208.6 million (but in line with consensus' forecast), but we deem the results to be within our full year expectations due to the seasonal factor in 1QFY14.

Meanwhile, no dividend per unit (DPU) was announced for shareholders this quarter (1QFY13: Nil). Gross rental income grew by a robust 12.6% y-o-y due to tenancy renewals at both Mid Valley Megamall (MVM) and The Gardens Mall (TGM) in Kuala Lumpur last year; 33% of MVM's net lettable area (NLA) and 54% of TGM's NLA were renewed at a higher rental rate of 15%.

Quarter-on-quarter (q-o-q), realised net profit was up 8.8% due to lower operating expenses (-12.6% q-o-q). The occupancy rates as at 1QFY14 stood at 99.9% at MVM and 98.8% at TGM.

The operating outlook in FY14 remains challenging as IGB REIT may have to cope with uncertainties given higher operating costs (tenants have to bear with higher assessment rates and electricity costs through higher service charges) against a backdrop of potentially weaker retail sales. But we believe in IGB REIT's key strengths, which are: (i) stable occupancy rates of (close to 100%); (ii) strong visitor and retailer attraction — MVM and TGM are key suburban shopping destinations; and (iii) yield-accretive asset enhancement initiatives which will continue to sustain the REIT.

Asset injection plans of Southkey Megamall in Johor Baru (1.5 million sq ft NLA) and 18@Medini (in Iskandar Malaysia) are expected after FY16E.

We maintain our “buy” rating on IGB REIT based on an unchanged discount dividend model (DDM) derived price target of RM1.34, premised on a 8.2% cost of equity, 6% equity risk premium and 3.0% terminal growth rate.

At RM1.16, IGB REIT is trading at a 13.3% discount to our net asset value estimate (DDM of future DPU). Year-to-date, IGB REIT has underperformed the other pure retail REITs such as CapitaMalls Malaysia Trust and Pavilion REIT.

For FY14E and FY15E, DPU yields are at 6.3% and 6.6% respectively against the overall big cap Malaysian REITs’ yield of 5.9% for FY14E and 6.2% for FY15E.

Given a low gearing ratio of 24.3%, the impact of a hike in rates of 25 basis points (bps) to 50bps should be minimal on FY14 and FY15E net profit. — Affin IB Research, May 2

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