Positive earnings outlook seen for IGB REIT

IGB Real Estate Investment Trust (Dec 12, RM1.92)

Maintain buy with an unchanged target price of RM2.15: Listed in September 2012, IGB Real Estate Investment Trust (IGB REIT) has grown from strength to strength and fended off numerous challenges such as rising competition from new retail shopping malls/e-commerce and slowing economic/retail sales growth. The REIT has reported uninterrupted revenue and net property income (NPI) growth since its listing, attributable to its ever-popular shopping malls (Mid Valley Megamall and The Gardens Mall) and proactive management. Notably, the Mid Valley Megamall has outperformed its listed peers, delivering the highest NPI growth of 28% for financial year 2014 (FY14) to FY18. Meanwhile, The Gardens Mall is one of its top performers among the high-end shopping malls.

Looking ahead, we are positive on IGB REIT's earnings outlook. Despite soft consumer sentiment, its tenants' sales are still seeing robust growth, which should translate into higher turnover rent in FY19 to FY20. Also, IGB REIT's ongoing asset enhancement initiatives and tenant management should drive revenue and NPI growth. All in, we forecast IGB REIT to grow its earnings per unit by 3% to 4% per annum for FY19 to FY21.

With a relatively low gearing of 23%, IGB REIT has a debt headroom of about RM2.8 billion for future acquisitions. The newly opened Mid Valley Southkey Mall (70% owned by its sponsor IGB Bhd) is, in our view, an exciting target for a future injection. The mall has a large net lettable area (NLA) of 1.5 million sq ft (about 56% of IGB REIT's current NLA) and enjoys an occupancy rate of over 85%. Nonetheless, the management has guided that an acquisition, if it were to happen, would only materialise after the first tenancy cycle.

We expect IGB REIT's valuation to see further positive rerating and its distribution yield to compress towards 4.6%, driven by an anticipated overnight policy rate (OPR) cut and increasing scarcity premium for high-quality retail assets with robust growth prospects and low gearing.

Downside risks to our positive view on IGB REIT include: i) sharp deterioration in the retail mall market, leading to weaker-than-expected earnings; and ii) an unexpected hike in the OPR and/or global bond yields that may reduce the appeal of Malaysian REITs, including IGB REIT.

We derive our fair value (FV) using a dividend discount model based on a 7.3% cost of equity and 3% long-term growth. We estimate that every increase of 25 basis points (bps) in cost of equity will lower our FV by 5%, while every 50bps cut in our long-term growth assumption will decrease our FV by 7%. — *Affin Hwang Capital, Dec 12*

IGB Real Estate Investment Trust

FYE DEC (RM MIL)	2017	2018	2019E	2020E	2021E
Revenue	524.9	535.7	552.6	572.6	588.0
Net property income	373.6	386.3	399.2	415.8	427.7
Reported net profit	343.4	333.8	315.6	331.8	343.7
EPU (sen)	9.8	9.5	8.9	9.3	9.6
Distributable profit	342.8	341.4	353.2	370.3	382.8
Realised net profit	303.4	303.8	315.6	331.8	343.7
Realised EPU (sen)	8.7	8.6	8.9	9.3	9.6
Realised EPU chg	8.6	-0.5	3.2	4.5	2.9
Realised PER (x)	22.4	22.5	21.8	20.9	20.3
DPU (sen)	9.3	9.2	9.4	9.8	10.1
DPU yield (%)	4.8	4.7	4.9	5.1	5.2
P/RNAV (x)	1.8	1.8	1.8	1.8	1.8
Affin/consensus (x)			1.0	1.0	1.0

Sources: Company, Affin Hwang forecasts, Bloomberg