

IGB REIT - Near-to-full occupancy rates for malls | I3investor

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Investment Highlights

- We maintain **BUY** on IGB REIT with a higher **fair value (FV) of RM1.86/unit** (from RM1.85/unit previously) based on the dividend discount model (DDM) (Exhibit 5).
- The increase in our FV is mainly attributed to the stronger-than-expected rental income from Mid Valley Megamall (MVM) and The Gardens Mall (TGM), partially offset by higher risk-free rate due to a surge in 10-year Malaysian Government Securities (MGS) to 4.3% from 3.9%. No changes to our neutral 3-star ESG rating (Exhibits 6).
- IGB REIT's distributable income of RM271mil (+92% YoY) in 9MFY22 came in above our and consensus' expectations. It accounted for 89% of our and 85% of streets' full-year distributable income. The variance was mainly due to higher-than-expected base rent upon the renewal of tenancies as well as a stronger shopping volume. Additionally, higher tenant sales increased the variable portion of rents tied to the level of the retail stores' business transactions.
- We raise our FY22F/FY23F/FY24F distributable income forecast by 18%/5%/3%. This is after increasing our assumption on monthly average rental per net lettable area (NLA) of MVM to RM15/sq ft from RM14/sq ft and TGM to RM13.70/sq ft from RM13/sq ft following our observation of a stronger rental income in 9MFY22.
- In 3QFY22, IGB REIT's gross revenue surged 46% YoY while net property income (NPI) climbed by 81% YoY. The improvements were driven by higher occupancy rate in TGM to 99.95% in 3QFY22 from a low 90% in 3QFY21, coupled with lower rental rebates offered to tenants.
- On a QoQ comparison, IGB REIT's 3QFY22 gross revenue expanded by 5% while NPI declined 4%. The increase in property operating expenses in 3QFY22 was mainly attributed to higher maintenance expenses.
- QoQ, occupancy rates for MVM remained at 99.7% in 3QFY22. Meanwhile, the occupancy rate for TGM improved to almost 100% in 3QFY22 from 99.7% in 2QFY22 (Exhibit 2).
- We are confident of IGB REIT's ability to maintain its high occupancy rate due to its malls' strategic location and lower gross monthly

rental rates of RM13–15 per sq ft. compared to other shopping malls in Klang Valley, such as Suria KLCC (>RM40 per sq ft.), Pavilion Kuala Lumpur Mall (RM29 per sq ft.) and Sunway Pyramid Shopping Mall (RM16 per sq ft.).

- The rental reversion in FY22F is expected to be mildly positive for both malls with increments ranging from 0% to 3%. Nevertheless, we foresee a positive rental reversion in FY23F/FY24F of 1-3% with the expectation of stronger tenants' sales as compared to pandemic level, which will provide opportunity for the group to negotiate for higher rentals in subsequent years.
- IGB REIT's debt-to-asset ratio fell slightly to 23%, well below the REITs' statutory limit of 50% (statutory limit after 31 December 2022). It has the lowest debt-to-asset ratio among the REITs under our coverage.
- 100% of the group's borrowings are under medium-term notes (MTN) with a fixed coupon rate of 4.49% per annum. Hence, IGB REIT is envisaged to be able to enjoy relatively lower interest expenses as compared to other REITs under current rising interest rate environment.
- IGB REIT declared its gross distribution per unit (DPU) of 2.44 sen in 3QFY22, which represent a distribution payout ratio of 98%. It was 2x of the 1.18 sen declared in 3QFY21 and 6% higher than the 2.31 sen in 3QFY19 (pre-pandemic level).
- The recent aggressive policy rate hikes in the United States (US) has caused the US treasury yield to rise and this in turn has spilled over and resulted in an increase in 10-year MGS yield. However, we anticipate that the uptrend in 10- year UST yield to be tapering off with the expectation that the Federal Reserve may ease off aggressive rate hikes after the end of 2022 as a result of weaker economic data.
- Meanwhile, we anticipate the yield spread to be widening from FY22F onwards with the gradual recovery of retail footfalls and tenant sales, which will translate into higher distribution yields of 6-7% in FY22F-24F vs. 4% in FY21. We expect IGB REIT to be appealing to yield-seeking investors with its higher yield spread against 10-year MGS (Exhibit 4).
- IGB REIT currently trades at a compelling FY23F PE of 16x vs. 4-year average of 23x. Meanwhile, distribution yield for FY23F of 7% is attractive vs. 10-year MGS yield of 4.3%.
- We like IGB REIT due to its resilient long-term outlook underpinned by the group's strategically located assets in the heart of Klang Valley. In addition, it has a better balanced footfall profile comparatively with moderate exposure to tourists. This positions the group to be able to better capitalise on domestic consumption recovery while international tourist arrivals gradually regain

momentum.

Source: [AmInvest Research](#) - 4 Nov 2022