REIT, A Safe Haven During Market Turmoil | BusinessToday

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The broader market suffered heavy losses due to collapse of Silicon Valley Bank and the 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, Kenanga points out that the 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 a stable yield. Meanwhile, KL REIT Index outperformed KLCI by recording gains of +2.3% YTD against KLCI's losses of -6% YTD. The research house says it sees that investors could be seeking shelter in REIT amid market uncertainty as the overall outlook for REIT in Malaysia remains positive, unfazed by the turmoil in oversea markets.

Most of the retail REIT reported earnings growth in CY22 due to a recovery in rental income and lower assistance to tenants. Tenant sales and shopper footfall recovered to pre-pandemic level post reopening of the economy. That led to rental reversion of shopping malls in prime locations returning to positive territory in CY22. Looking forward, the performance of retail REIT is expected to remain steady particularly for REIT with malls in a good locations 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.

The 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 the economy, consumers remain shopping on-line, and that support demand for warehousing space. Meanwhile, the defensiveness of industrial assets attracted the 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.

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

Cost of borrowings. BNM paused the OPR hike two consecutive times in 2023. Kenanga’s 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 costs
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 a floating rate, Sunway REIT with 68% debt on a floating rate, and Pavilion REIT with 65% financing on a floating rate. Hence, Kenanga said it sees the risk of higher borrowing costs for REIT is low in the near term and earnings growth should remain intact.

Overall, it is of view that earnings of REIT with exposure to the retail and hotel industry to improve further in CY23 due to the 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 a decent average yield of 5.3%. 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).