Malaysian REITs remain a safe haven amid market volatility, says MIDF Research | CEO Morning Brief

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KUALA LUMPUR (March 22): Malaysian real estate investment trusts (REITs) remain as safe-haven investments for investors amid market uncertainty, owning to growing contagion fears with the collapse of Silicon Valley Bank and the fallout of Credit Suisse Group AG.

According to MIDF Research analyst Jessica Low Jze Tieng, local REITs could provide shelter for investors amid market volatility, as they could offer a decent average yield of 5.3% to act as an inflation hedge.

On top of that, Low is positive on the earnings outlook for local REITs this year, given that earnings of REITs with exposure to the retail and hotel industry are seen improving further this year, due to recovery of consumer spending at malls and higher tourist arrivals.

The performance of retail REITs is expected to remain steady, particularly for REITs with malls in good locations, such as IGB REIT, Sunway REIT, Pavilion REIT and KLCCP Stapled Group.

"Besides, retail spending is also expected to be supported by the festive season in the second quarter of 2023 (2Q2023), and higher tourist arrivals. We expect stronger tenant sales in 2Q2023, and rental reversion to remain in positive territory,” Low added.

Low also expects REITs with exposure to the hotel industry, namely Sunway REIT and KLCCP Stapled Group, to see better earnings contributions from their hotel divisions.

She expects the hotel industry to turn around this year, due to growth in domestic tourism and higher tourist arrivals.

Similarly, an industrial REIT, namely Axis REIT, is expected to report stable earnings, due to solid demand for industrial space.

Low said despite consumers shopping at physical stores since the reopening of the economy, the online shopping trend remains, and that supports demand for warehousing space.

As such, the defensiveness of industrial assets attracted interest of several REITs, such as KIP REIT and CapitaLand Malaysia Trust, to venture into the industrial space.

Nonetheless, Low foresees that growing competition among REITs in the industrial space may compress acquisition yields for industrial assets going forward.

With MIDF economists projecting Bank Negara Malaysia (BNM) to keep its overnight policy rate (OPR) at 2.75% for the rest of 2023, Low sees this to be a positive for REITs, as it eases concern over rising borrowing costs.

The central bank has paused the OPR twice in 2023, and the pause provides relief to REITs 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, said Low.

“Hence, we see risk of higher borrowing cost for REITs as low in the near term, and earnings growth should remain intact,” she added.

Low maintained her "positive" recommendation for the REIT sector, with her top picks being IGB REIT ("buy"; target price: RM1.86) and Sunway REIT ("buy"; RM1.73).