IGB REIT - Poised for stronger rental reversion in FY23F | I3investor

Clipped from: https://klse.i3investor.com/web/blog/detail/AmInvestResearch/2023-04-28-story-h-272345130-IGB_REIT_Poised_for_stronger_rental_reversion_in_FY23F

Investment Highlights

- We upgrade our recommendation on IGB REIT to **BUY** from HOLD with a higher **fair value (FV) of RM1.92/unit** (from RM1.90/unit previously) based on our revised dividend discount model (DDM) (Exhibit 6). No change to our neutral 3-star ESG rating (Exhibit 7).

- The FV implies a FY24F distribution yield of 6%, at parity to its 5-year median.

- The higher FV stems from increasing FY23F/FY24F/FY25F distributable income by 6%/7%/9% to account for increased rental reversion assumptions of 3%-5% for both Mid Valley Megamall (MVM) and The Gardens Mall (TGM), up from our earlier more conservative assumption of 1%-3%. This is in view of higher-than-anticipated rental rate in 1QFY23 (Exhibits 2 & 3) as well as the improving retail industry outlook in Malaysia.

- IGB REIT's 1QFY23 distributable income of RM103mil came in within our and consensus' estimates. It accounted for 28% of our earlier FY23F earnings and 29% of consensus.

- In 1QFY23, IGB REIT's gross revenue improved 16% YoY while net property income (NPI) climbed 10% YoY. The improvement was driven by stronger gross monthly rental income of RM17 psf in MVM and RM16 psf in TGM as a result of favourable FY22 rental reversion (Exhibits 2, 3).

- On a QoQ comparison, IGB REIT's 1QFY23 gross revenue expanded 4% while NPI grew 12%. The lower property operating expenses were mainly due to the decline in upgrading and reimbursement costs in 1QFY23.

- In 1QFY23, the occupancy rates for MVM and TGM are close to 100% (Exhibits 2, 3). We are confident of IGB REIT's ability to maintain its high occupancy rate due to the mall's strategic location. To date, IGBREIT has completed the renewal of a majority of leases that are expiring in FY23 (Exhibit 4).

- IGB REIT declared a gross distribution per unit (DPU) of 2.8 sen in 1QFY23 (+14% QoQ, +12% YoY), representing a 12-month trailing distribution yield of 6%.

- We anticipate the US Fed rate to peak in 1HFY23 as a result of weaker economic data and softening inflation. Our inhouse economist projects another 0.25% hike in the US Fed rate in 1HCY23 from the current level of 4.75%-5%. Meanwhile, the 10-year MGS yield is forecasted to be 3.8%-4% by the end of 2023. However, we do not rule out the possibility that the 10-year MGS yield could ease further if there are signals affirming a less hawkish tone by the US Federal Reserve, resulting in a pause in the Fed Funds rate hikes, as well as the tapering of inflation rates globally which will reduce pressures on Central Banks including BNM to continue raising interest rates.

- From FY23F onwards, we anticipate IGB REIT’s distribution yield spread against 10-year MGS to widen to 2% vs. 5- year median of 1%. Hence, we expect IGB REIT to be appealing to yield-seeking investors with its higher distribution spread against 10-year MGS (Exhibit 5).

- IGB REIT currently offers a compelling FY24F distribution yield of 6% vs. current 10-year MGS yield of 3.7%. 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 comparatively better-balanced footfall profile 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]() - 28 Apr 2023