

24 January 2020

# Pavilion REIT

## FY19 Below Expectations

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**FY19 realised net income (RNI) of RM247.6m came in slightly below our and consensus expectations at 93% and 94%, respectively, on higher-than-expected borrowing cost. FY19 GDPS of 8.50 sen is also below (94%). Lower FY20E RNI by 6% to RM257m on lower rental from Damen mall and higher borrowing cost, and introduce FY21E RNI of RM266m. Maintain MARKET PERFORM but lower TP to RM1.80 (from RM1.90) with implied yield of 4.9%.**

FY19 realised net income (RNI) of RM247.6m came in slightly below our and consensus expectations, at 93% and 94%, respectively. Top-line was within at 95% but the reason for the deviation was mainly due to higher-than-expected financing cost (108%) as our estimates may have been too conservative. 4QFY19 dividend of 4.10 sen (which includes a non-taxable portion of 0.17 sen) brought FY19 dividend to 8.50 sen which is also below our expectation of 9.10 sen (at 94%), implying 4.9% gross yield.

**Results' highlights.** YoY, top-line was up by 5% driven by: (i) higher rental income from Pavilion Kuala Lumpur (PKL) on positive reversions post the repositioning exercise, and (ii) the inclusion of Elite Pavilion Mall (EPM) in April 2018 (2QFY18). Top-line growth was mildly dampened by Damen mall which registered lower rental and occupancy. However, RNI was down by 3% on higher operating expenditure (+17%) due to higher electricity and repairs for air conditioners and lifts and maintenance, and higher financing cost (+10%) due to Elite Pavilion and working capital. **QoQ**, top-line was flattish (+1%), while higher operating cost eroded top-line improvement, resulting in flat RNI.

**Outlook.** FY20-21 will see 22-19% of portfolio NLA expiring, on single-digit reversions. We are confident that PAVREIT's two main drivers Pavilion KL (PKL) and Pavilion Elite which cumulatively contribute c.95% to NPI would be able to secure positive reversions on the minimal leases up for renewal, but the outlook for Damen mall is expected to remain challenging in the near term pending the addition of the cinema in October 2020. Fahrenheit88 acquisition is still on the table, pending the sponsor's intention to sell, while we believe PAVREIT is eyeing cap rates closer to 6.5%.

**We lower FY20E RNI by 6% to RM257m and introduce FY21E RNI of RM266m.** We lowered FY20E earnings assumptions post increasing our loan drawdown assumptions closer to current levels for higher than expected working capital. Additionally, we also lowered Damen malls rental assumptions to account for weaker occupancy of 70% (vs. 80% previously) and lower rental reversions. FY20-21 will continue to be driven by single-digit rental reversions, stemming mainly from PKL and Pavilion Elite renewals. Our FY20-21E GDPU of 8.8-9.1 sen (NDPU of 7.9-8.2 sen) implies gross yield of 5.1-5.2% (net yield of 4.6-4.7%).

**Maintain MARKET PERFORM but on a lower TP of RM1.80 (RM1.90)** on a lower FY20E GDPS/NDPS of 8.8 sen/7.9 sen (from 9.3 sen/8.4 sen) and an unchanged gross yield spread of +1.5ppt to our 10-year MGS target of 3.40%. We like PAVREIT for its prime asset profile and resilient earnings and as such have applied thin spreads which are at the lower-end among retail MREITs under our coverage (between +1.3ppt to +2.6ppt). We are comfortable with our call (with potential return of 9%) as most upsides have been priced in (i.e. positive reversions and stable portfolio occupancy), while downside risks appear minimal.

## MARKET PERFORM ↔

Price : RM1.73  
Target Price : RM1.80 ↓

### Share Price Performance



KLCI 1,574.44  
YTD KLCI chg -0.9%  
YTD stock price chg -0.6%

### Stock Information

Shariah Compliant No  
Bloomberg Ticker PREIT MK EQUITY  
Market Cap (RM m) 5,257.5  
Shares outstanding 3,039.0  
52-week range (H) 1.92  
52-week range (L) 1.66  
3-mth avg daily vol: 620,900  
Free Float 13%  
Beta 0.6

### Major Shareholders

Qatar Investment Authority 33.2%  
Lim Siew Choon 27.8%  
Tan Kewi Yong 9.3%

### Summary Earnings Table

FY Dec (RM m)	2019A	2020E	2021E
Turnover	585.4	611.9	624.1
EBIT	375.2	357.5	364.7
PBT	262.6	256.5	266.3
<b>Net Profit</b>	<b>262.6</b>	<b>256.5</b>	<b>266.3</b>
<b>Core NP (RNI)</b>	<b>247.6</b>	<b>256.5</b>	<b>266.3</b>
Consensus (CNP)	n.a.	280.7	290.4
Earnings Revision	n.a.	-6%	n.a.
Core EPS (sen)	8.1	8.4	8.7
Core EPS growth (%)	-3	3	4
NDPS (sen)	7.7	7.9	8.2
BV/Share (RM)	1.27	1.30	1.30
Core PER (x)	21.2	20.5	19.8
Gearing (%)	0.34	0.35	0.35
N.Dividend Yield (%)	4.4	4.6	4.7

\*Core Net Profit refers to RNI



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**OTHER POINTS**

Risks to our call include: (i) bond yield compression and expansion, vs. our target 10-year MGS yield, and (ii) strengthening or weakening rental income.

**Results Highlights**

FYE Dec (RM m)	4Q19	3Q19	QoQ	4Q18	YoY	FY18	FY19	YoY-Ytd
Gross Rental Income (Gross Revenue)	146.0	144.4	1%	147.1	-1%	555.0	585.4	5%
Operating Costs	-54.7	-53.3	3%	-46.1	19%	-180.2	-210.2	17%
<b>Net Rental Income (NPI)</b>	<b>91.2</b>	<b>91.1</b>	<b>0%</b>	<b>101.0</b>	<b>-10%</b>	<b>374.8</b>	<b>375.2</b>	<b>0%</b>
Interest Income	2.6	2.8	-8%	2.7	-5%	10.9	11.3	4%
<b>Total Trust Income (Net Investment Income)</b>	<b>93.8</b>	<b>93.9</b>	<b>0%</b>	<b>103.7</b>	<b>-10%</b>	<b>385.7</b>	<b>386.5</b>	<b>0%</b>
Expenditure	-7.5	-7.8	-4%	-10.0	-25%	-32.8	-31.6	-4%
Financing Costs	-26.6	-26.6	0%	-27.1	-2%	-97.7	-107.3	10%
Fair Value Adjustments	15.0	0.0	n.a.	33.6	-55%	33.6	15.0	-55%
Gain on disposal of investment property	0.0	0.0	n.a.	0.0	n.a.	0.0	0.0	n.a.
<b>Pretax Income</b>	<b>74.7</b>	<b>59.4</b>	<b>26%</b>	<b>100.3</b>	<b>-25%</b>	<b>288.7</b>	<b>262.6</b>	<b>-9%</b>
Taxation	0.0	0.0	n.a.	0.0	n.a.	0.0	0.0	n.a.
<b>Income after Tax</b>	<b>74.7</b>	<b>59.4</b>	<b>26%</b>	<b>100.3</b>	<b>-25%</b>	<b>288.7</b>	<b>262.6</b>	<b>-9%</b>
<b>Realized Net Income</b>	<b>59.7</b>	<b>59.4</b>	<b>0%</b>	<b>66.7</b>	<b>-10%</b>	<b>255.1</b>	<b>247.6</b>	<b>-3%</b>
EPU (sen)	2.46	1.95	26%	3.30	-25%	9.51	8.64	-9%
GDPU (sen)	2.06	2.04	1%	2.30	-10%	8.78	8.50	-3%
NAV/unit (RM)	1.27	1.26		1.27		1.27	1.27	
Gearing (x)	0.34	0.34		0.34		0.34	0.34	
NPI Margins	62.5%	63.1%		68.7%		67.5%	64.1%	
RNI Margins	40.9%	41.2%		45.3%		46.0%	42.3%	

Source: Company, Kenanga Research

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## Peer Comparison

Name	Last Price	Market	Shariah	Current	Revenue Growth		Core Earnings Growth		PER (x) - Core Earnings			PBV (x)		ROE (%)	Net Div.Yld. (%)	Target Price (RM)	Rating
	(RM)	Cap (RM'm)	Compliant	FYE	1-Yr. Fwd.	2-Yr. Fwd.	1-Yr. Fwd.	2-Yr. Fwd.	Hist.	1-Yr. Fwd.	2-Yr. Fwd.	Hist.	1-Yr. Fwd.	1-Yr. Fwd.	1-Yr. Fwd.		
<b>STOCKS UNDER COVERAGE</b>																	
AXIS REIT	1.86	2,669.6	Y	12/2020	5.4%	2.9%	16.9%	2.0%	20.3	20.0	19.2	1.4	1.2	7.6%	4.1%	2.00	OP
CAPITALAND MALAYSIA MALL TRUST	1.02	2,092.8	N	12/2020	1.2%	1.4%	1.6%	0.8%	16.5	16.2	15.9	0.8	0.8	4.8%	5.6%	1.05	OP
IGB REIT	1.93	6,849.2	N	12/2020	2.5%	2.0%	0.4%	2.0%	21.7	21.7	21.4	1.8	1.8	8.5%	4.5%	2.05	OP
KLCCP STAPLED GROUP	7.98	14,406.6	Y	12/2020	5.0%	1.3%	1.5%	1.6%	19.7	19.4	19.1	1.1	1.1	6.0%	4.6%	8.25	MP
MRCB-QUILL REIT	0.980	1,050.3	N	12/2020	-2.2%	0.7%	-8.4%	1.2%	12.7	14.0	13.9	0.8	0.8	5.4%	6.4%	1.05	MP
PAVILION REIT	1.73	5,257.5	N	12/2020	4.5%	2.0%	3.6%	3.8%	21.2	20.5	19.8	1.3	1.3	6.8%	4.6%	1.80	MP
SUNWAY REIT	1.84	5,418.9	N	06/2020	8.1%	2.6%	2.5%	2.4%	19.2	18.8	18.2	1.2	1.2	6.6%	4.8%	1.90	MP
<b>Simple Average</b>					<b>3.5%</b>	<b>1.8%</b>	<b>2.6%</b>	<b>2.0%</b>	<b>18.8</b>	<b>18.7</b>	<b>18.2</b>	<b>1.2</b>	<b>1.2</b>	<b>6.5%</b>	<b>4.9%</b>		
<i>* Core NP and Core PER</i>																	
<b>CONSENSUS NUMBERS</b>																	
YTL HOSPITALITY REIT	1.36	2,318.0	N	06/2020	5.6%	3.1%	24.9%	6.8%	22.1	17.7	16.6	0.9	0.8	0.0	6.2%	1.51	BUY
AL-'AQAR HEALTHCARE REIT	1.35	993.6	Y	12/2019	-2.1%	1.9%	-32.9%	2.9%	10.9	16.2	15.7	1.0	n.a.	0.1	5.8%	1.54	BUY
AMANAHRAYA REIT	0.740	424.2	N	12/2019	25.3%	0.8%	-52.2%	2.1%	5.2	10.9	10.7	0.5	n.a.	0.1	8.0%	0.790	N.A.
AMFIRST REIT	0.510	346.6	N	03/2020	n.a.	n.a.	n.a.	n.a.	15.5	n.a.	n.a.	0.4	n.a.	n.a.	n.a.	n.a.	N.A.
HEKTAR REIT	0.990	457.3	N	12/2019	-4.8%	-2.3%	n.a.	n.a.	13.8	n.a.	n.a.	0.7	n.a.	n.a.	7.1%	n.a.	N.A.
TOWER REIT	0.800	224.4	N	06/2020	n.a.	n.a.	n.a.	n.a.	31.3	n.a.	n.a.	0.4	n.a.	n.a.	n.a.	n.a.	N.A.
UOA REIT	1.24	524.4	N	12/2019	-0.6%	1.3%	-30.5%	0.0%	9.1	13.1	13.1	0.7	0.7	0.1	7.3%	n.a.	N.A.
ATRIUM REIT	1.05	216.6	N	12/2019	n.a.	n.a.	n.a.	n.a.	18.7	n.a.	n.a.	0.8	n.a.	n.a.	n.a.	n.a.	N.A.
AL-SALAM REIT	0.855	495.9	Y	12/2019	7.0%	5.1%	-26.7%	4.2%	12.3	16.8	16.1	0.8	0.8	0.0	5.5%	0.865	N.A.
KIP REIT	0.910	459.8	N	06/2020	25.6%	0.3%	n.a.	n.a.	13.5	n.a.	n.a.	0.9	0.9	n.a.	7.8%	n.a.	N.A.

Source: Bloomberg, Kenanga Research

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**Stock Ratings are defined as follows:****Stock Recommendations**

OUTPERFORM	: A particular stock's Expected Total Return is MORE than 10%
MARKET PERFORM	: A particular stock's Expected Total Return is WITHIN the range of -5% to 10%
UNDERPERFORM	: A particular stock's Expected Total Return is LESS than -5%

**Sector Recommendations\*\*\***

OVERWEIGHT	: A particular sector's Expected Total Return is MORE than 10%
NEUTRAL	: A particular sector's Expected Total Return is WITHIN the range of -5% to 10%
UNDERWEIGHT	: A particular sector's Expected Total Return is LESS than -5%

**\*\*\*Sector recommendations are defined based on market capitalisation weighted average expected total return for stocks under our coverage.**

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