No change to 'buy' call on Pavilion REIT

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By S. BIRRUNTHA - April 29, 2024 @ 8:31am

Pavillion shopping mall at Kuala Lumpur. NSTP/ASYRAF HAMZAH

KUALA LUMPUR: Hong Leong Investment Bank (HLIB) is positive about the continued improvement in Pavilion Bukit Jail's (PBJ) rental contribution since being added to the real estate investment trust (REIT) in June 2023.

The investment bank said there remains a substantial rental contribution upside from PBJ, with a RM9.50 per sq ft of rental rate as of the fourth quarter of 2023 (4Q23), as well as 59 per cent of the net lettable area (NLA) up for renewal in 2024.

"Other than that, the expected improvement in tourist arrivals to Malaysia should result in higher shopper footfall and tenant sales for its prime malls, Pavilion KL and Elite Pavilion Mall.

"To note, despite the recent opening of The Exchange TX, management has said that footfall to its prime malls remains unaffected, as evidenced by its steady occupancy rates.

"Combined with management's guidance of mid-single digit rental reversions for financial year 2025 (FY25), earnings should continue to be sustained for the near to midterm," it said in a note.

Meanwhile, HLIB also said Pavilion REIT's first quarter ended March 31, 2024 (1 Q24) core net profit of RM83.2 million was within the investment bank's (23 per cent) and consensus' (25 per cent).

Its revenue increased by 9.2 per cent on the back of higher revenue rent from the retail malls.

Topline grew by 38.5 per cent thanks to an improved contribution from PBJ as well as higher occupancy rates and revenue rent from the existing retail malls.

Nonetheless, higher total operating expenses, largely due to increased utilities (up 68.7 per cent) and maintenance costs (up 83.7 per cent), resulted in a 33.2 per cent increase in net property income (NPI) in 1Q24.

Additionally, with higher financing costs (up 73.3 per cent), core net profit increased by a smaller magnitude of 18.8 per cent.

Meanwhile, the average occupancy for retail properties remained steady at 88 per cent in 1Q24 compared to 4Q23.

Office segment (Pavilion Tower) occupancy increased slightly to 75 per cent compared to 72 per cent in 4Q23, while gearing level increased to 42 per cent compared to 37.7 per cent in 4Q23.

HLIB has maintained a "buy" call on Pavilion REIT with a slightly higher target price of RM1.63.

The investment bank said its target price is based on FY25 distribution per unit (DPU) on a targeted yield of 5.4 per cent which is derived from the five-year historical average yield spread between Pavilion REIT and 10 year Malaysian Government Securities (MGS).

HLIB has also trimmed Pavilion REIT's earnings forecast for FY24 and FY25 by 1.5 per cent and 3.9 per cent after imputing annual report updates.

"We think that Pavilion REIT will continue to benefit from the stronger tourist numbers in Malaysia this year.

"Moreover, the stock provides an attractive forecasted FY24 dividend yield of 6.5 per cent," it noted