



Sunway Real Estate Investment Trust

Robust Earnings Growth Priced In

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TP: RM 1.57 (+14.6%)

Last Traded: RM 1.37

Hold

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Review

- Sunway REIT's 9MFY14 realised net profit of RM175.9mn came in within expectations, accounting for 78% of both ours' and consensus's full-year estimates.
- A distribution per unit (DPU) of 2.1sen was declared for this quarter, bringing YTD DPU to 6.3sen. This was also in line with our full-year DPU projections of 8.2sen for FY14. Based on yesterday's closing price, this translates to an annualized yield of 6.1%. Note that Sunway REIT is committed to distribute 100% of its distributable income for FY14.
- Sunway REIT's 9MFY14 gross revenue and net property income grew 2.1% and 5.0% YoY to RM318.6mn and RM242.2mn respectively. This was driven by: 1) higher rental rates for Sunway Pyramid Shopping Mall and Sunway Carnival Mall (double-digit rental reversion for a 3 year-term), 2) contribution from additional NLA of 20,362 sq. ft. and reconfigured NLA of 23,432 sq. ft. created at Sunway Pyramid Shopping Mall's Oasis Boulevard 5 (opened in 2Q2014), and 3) better performance of the two hotels in Sunway Resort City with 9MFY14 occupancy rates improved to 79.3%-82.4% compared to 71.3%-78.7% in FY13.
- 9MFY14 realised net profit advanced further by 7.7% YoY to RM175.9mn, mainly attributable to RM0.7mn (or -1.5% YoY) decrease in finance costs. The lower finance costs was arising from lower amortization of loan upfront expenses and reduction in underwriting fee for commercial papers (CPs) following the reduction of the CPs programme underwritten limit.

Impact

- We leave our FY14-16 earnings forecasts unchanged at this juncture as we have factored in higher operating expenses arising from the electricity hike and assessment revision.

Conference Call Highlights

- The impact of electricity hike and revision in assessment rates of KL properties were the key discussions during the briefing. The 16% electricity tariff hike effective Jan-14 had partly contributed to 5.5% YoY increase in 3QFY14 property expenses for retail assets (excludes SPP Mall which is closed for refurbishment). Meanwhile, the revision in assessment rates for properties in Kuala Lumpur is a double whammy to Sunway REIT's office assets. As a result, property expenses of the office segment jumped 15.7% YoY in 3QFY14. On the other hand, the hotel properties which are under hotel master lease agreement, incurred minimum property operating expenses which comprise mainly quit rent, assessment and insurance. Nevertheless, higher provision for assessment for Sunway Putra Hotel has largely contributed to a RM0.2mn (or 26.9% YoY) increase in property operating expense. See **Table 1** for the proposed revision.

Share Information

Bloomberg Code	SREIT MK
Stock Name	SUNREIT
Stock Code	5176
Listing	Main Market
Units in circulation (mn)	2926.3
Market Cap (RMmn)	4009.1
Par Value	1.00
52-wk Hi/Lo (RM)	1.70/1.22
12-mth Avg Daily Vol ('000 shrs)	1645.0
Estimated Free Float (%)	41.9
Beta	0.7

Major Shareholders (%)

Sunway Berhad	(34.5)
Capital Income Builder	(11.1)
EPF	(9.7)
Nomura	(8.4)
Skim Amanah Saham Bumiputera	(8.3)

Forecast Revision

	FY14	FY15
Forecast Revision (%)	0.0	0.0
Net profit (RMmn)	226.6	258.1
Consensus	226.6	249.9
TA's / Consensus (%)	100.0	103.3
Previous Rating	Buy (Downgraded)	

Financial Indicators

	FY14	FY15
Gearing (%)	33.9	36.1
FCPS (sen)	1.9	5.2
Price / FCPS (x)	70.4	26.6
ROE (%)	6.5	7.4
ROA (%)	4.2	4.6
NTA/Share (RM)	1.3	1.3
Price/NTA (x)	1.1	1.1

Scorecard

	% of FY	
vs TA	78.0	Within
vs Consensus	78.0	Within

Share Performance (%)

Price Change	SunREIT	FBM KLCI
1 mth	0.7	0.5
3 mth	7.0	3.1
6 mth	3.0	2.9
12 mth	(14.4)	8.2

(12-Mth) Share Price relative to the FBM KLCI



Source: Bloomberg

Table1: New Assessment Rate for Sunway REIT's KL Properties

	Old	New	Increase (X)
Sunway Putra Mall (RM/psf)	2.9	6.4	1.2
Sunway Putra Tower (RM/psf)	2.7	3.6	0.3
Sunway Putra Hotel (RM/room)	460	1400	2.0
Sunway Tower (RM/psf)	2.9	4.1	0.4

Source: Sunway REIT

- Management believes it is not a daunting task to pass on the higher operating costs to its retail tenants and intends to increase the service and promotion charges in July-14 (1QFY15). However, it is unlikely to do the same to the office tenants given the oversupply of office spaces.
- In view of the substantial jump in assessment payment, management stated that it has submitted an objection letter but the local authority (DBKL) has yet to revert on the matter. As such, management has decided to make provisions for the higher assessment rate based on the proposed rates issued by DBKL. Should the appeal succeed, the provision will be written back.
- There are no major updates on potential asset injections from its parent company or asset acquisitions from any third parties. For FY14, Sunway REITs aims to focus on the execution of the AElS for its assets, particularly Sunway Putra Place (SPP). According to management, the works progress at SPP has reached 45%, and is on track for completion in early next year.

Valuation

- After adjusting the time period, we raise our DDM-derived target price to RM1.57/share (from RM1.50/share previously), based on unchanged discount rate of 9.25%. We believe the anticipated earnings boost from SPP has largely been reflected in Sunway REIT's current price levels. In addition, retail sales growth is expected to moderate, no thanks to the various government subsidy rationalization measures, which would reduce consumers' disposable income. As such, we downgrade Sunway REIT to **Hold** from Buy.

Earnings Summary (RM mn)

FYE June	FY12	FY13	FY14F	FY15F	FY16F
Gross Rental Income	406.4	415.9	444.8	505.1	554.9
Net Property Income	299.2	309.2	327.4	368.2	405.9
NPI Margins	73.6	74.3	73.6	72.9	73.1
Pretax profit	190.3	218.8	226.6	258.1	294.5
Core Net Profit	190.6	218.8	226.6	258.1	294.5
Distributable income	202.1	231.1	239.9	272.3	309.2
EPU (Sen)	7.1	7.9	7.7	8.8	9.9
EPU Growth (%)	13.7	11.2	(1.8)	13.4	13.5
PER (x)	19.4	17.4	17.7	15.6	13.8
DPU (sen)	7.5	8.3	8.2	9.2	10.4
Div Yield (%)	5.5	6.1	6.0	6.7	7.6
ROE (%)	6.6	6.7	6.5	7.4	8.4

3Q14 Results Analysis (RM mn)

FYE June	3Q13	2Q14	3Q14	QoQ (%)	YoY (%)	9MFY13	9MFY14	YoY (%)
Total revenue	106.4	110.3	108.1	(2.0)	1.5	312.0	318.6	2.1
- Retail	76.3	74.9	77.6	3.6	1.7	225.2	222.6	(1.1)
- Hospitality	15.1	19.9	14.9	(25.0)	(1.1)	51.4	49.1	(4.4)
- Office	10.3	10.8	10.7	(1.1)	3.5	30.7	32.4	5.5
- Healthcare	4.8	4.8	4.9	3.5	3.5	4.8	14.4	>100
Total Net Property Income	79.7	84.4	80.6	(4.5)	1.2	230.7	242.2	5.0
- Retail	53.6	53.3	54.9	3.0	2.5	155.8	159.7	2.5
- Hospitality	14.2	19.2	13.8	(28.0)	(2.9)	48.9	46.4	(5.1)
- Office	7.1	7.2	7.0	(2.8)	(1.9)	21.1	21.7	2.4
- Healthcare	4.8	4.8	4.9	3.5	3.5	4.8	14.4	>100
Other Income	0.4	0.6	0.5	(29.5)	18.7	1.0	1.6	72.8
Changed in fair value	0.0	0.0	0.0	nm	nm	0.0	0.0	nm
Net Investment Income	80.1	85.1	81.1	(4.7)	1.3	231.6	243.8	5.3
Manager & Trustee Fee	(6.5)	(6.8)	(6.6)	(2.4)	1.9	(18.7)	(20.1)	7.2
Finance Costs	(17.5)	(16.0)	(15.7)	(1.7)	(10.4)	(47.9)	(47.2)	(1.5)
Other expenses	(0.8)	(0.3)	(0.3)	6.2	(66.4)	(1.7)	(0.6)	(62.2)
Income Before Taxation	55.2	62.1	58.5	(5.8)	5.9	163.4	175.9	7.7
Net Profit	55.2	62.1	58.5	(5.8)	5.9	163.4	175.9	7.7
Realised Net Profit	55.2	62.0	58.5	(5.7)	5.9	163.4	175.9	7.7
Realised EPU (sen)	2.0	2.1	2.0	(5.7)	(1.5)	6.0	6.0	(0.3)
DPU (sen)	2.1	2.2	2.1	(5.8)	1.9	6.3	6.3	0.8
NPI Margin (%)	74.8	76.5	74.6	(1.9)	(0.2)	73.9	76.0	2.1
Realised Net Margin (%)	51.9	56.2	54.1	(2.1)	2.2	52.4	55.2	2.9

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