

27 October 2023

Property | REITS

Pavilion REIT (PREIT MK)

Neutral (Maintained)

Earnings Dragged By Higher Expenses

Target Price (Return):	MYR1.29 (7.5%)
Price (Market Cap):	MYR1.20 (USD917m)
ESG score:	3.0 (out of 4)
Avg Daily Turnover (MYR/USD)	2.03m/0.44m

- Maintain NEUTRAL, lower MYR1.29 TP from MYR1.32, 8% upside and c.7% yield.** Pavilion REIT's 9M23 results missed expectations due to higher-than-expected expenses. Pavilion KL (PKL) and Elite Pavilion remained strong with high single to double-digit revenue growth YoY, but the outlook for the REIT's other properties may be more challenging. While the results mark the first full-quarter contribution from Pavilion Bukit Jalil (PBJ), its NPI margin is relatively low at 49% as some of the signed tenants are still undergoing renovations.
- Results missed estimates.** 3Q23 core profit of MYR70.6m (+12.2% QoQ, +15.4% YoY) brought 9M23 earnings to MYR203.5m (+12.2% YoY). This was only at 70% of our and Street's full-year estimates. The revenue growth was mostly driven by the inclusion of PBJ, which was only acquired in June. However, NPI margin dropped to 60.9% (2Q23: 63.1%), dragged down by PBJ's lower margins. Interest expenses increased by MYR11.3m QoQ (+19.6m YoY) from the drawdown of borrowings for the acquisition. The REIT recorded a 9M23 DPU of 6.56 sen (9M22: 6.16 sen).
- Strong growth in its flagship malls.** Off a seasonally slower base in 2Q23, PKL and Elite Pavilion recorded strong 6% and 10% QoQ revenue growth (+7% and 17% YoY). The REIT has completed the reconfiguration of the tenancy lots at PKL's Fashion Avenue and Elite Pavilion to increase visibility and clear up space for new tenants (capex: MYR5.7m). We think asset enhancement initiatives (AEIs) such as these are key to ensure the malls maintain their competitiveness.
- Narrowing losses for Da Men Mall.** The mall's net property losses narrowed slightly to -MYR1.98m during the quarter (2Q23: -MYR2.24m, 3Q22: -MYR2.69m). The mall has also seen consistently higher occupancy rates – from 59% in Jun 2022 to 72% in Jun 2023 – but we remain cautious on the mall's prospects. We expect the mall to only break even in FY25F as occupancy rates improve. We are similarly cautious on Pavilion Tower's outlook, with its occupancy only at 66%. While securing new tenants would be difficult – given the challenging office segment – downside risks are mitigated as major tenants include the REIT's sponsor.
- Earnings adjustment.** We lower our FY23-25F earnings estimates by 4% after adjusting our interest rate and property expense assumptions. 87% of the REIT's borrowings are on floating rates, and as such, it would benefit from potential interest rate cuts. Our DDM-derived TP (Ke: 8.2%) incorporates a 0% ESG premium/discount.
- Risks:** Faster/slower-than-expected tourism industry recovery and higher/lower-than-expected occupancy rates.

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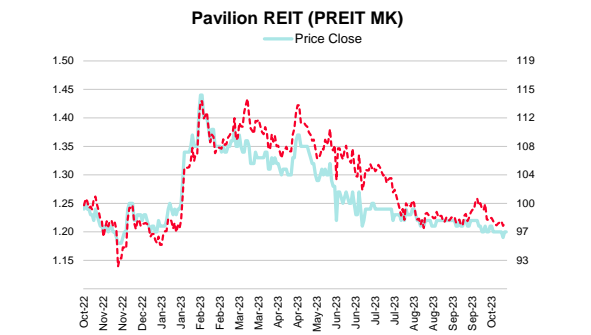
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Share Performance (%)

	YTD	1m	3m	6m	12m
Absolute	(0.8)	(1.6)	(2.4)	(9.8)	(3.2)
Relative	2.8	(1.4)	(1.9)	(11.8)	(2.3)
52-wk Price low/high (MYR)	1.18 – 1.44				



Source: Bloomberg

Forecasts and Valuation	Dec-21	Dec-22	Dec-23F	Dec-24F	Dec-25F
Total turnover (MYRm)	489	570	710	841	877
Net property income (MYRm)	237	364	436	527	551
Reported net profit (MYRm)	126	246	280	309	338
Total distributable income (MYRm)	135	256	288	318	348
DPS (MYR)	0.04	0.08	0.09	0.09	0.09
DPS growth (%)	7.0	88.9	2.7	1.5	2.9
P/B (x)	0.94	0.90	0.86	0.85	0.90
Dividend Yield (%)	3.7	7.0	7.2	7.3	7.5
Return on average equity (%)	3.3	6.2	6.4	6.3	6.5
Return on average assets (%)	2.0	3.9	3.8	3.7	3.9

Source: Company data, RHB

Overall ESG Score: 3.0 (out of 4)

E: GOOD

Pavilion REIT targets to reduce electricity consumption by 3% per annum for the next three years based on pre-pandemic position. The REIT also tracks its water consumption (using its installed groundwater harvesting system) and waste management.

S: GOOD

Community engagement is an integral part of PREIT's sustainability efforts, with events held by the malls such as OKU Art Exhibition and Charity At Heart. The Manager also provides extensive training programmes for its employees and monitors their learning curve.

G: GOOD

The Manager reviews its internal anti-corruption policies in line with the Malaysian Anti-Corruption Act 2018. The Board meets at least once every quarter, and have adopted the responsibilities as listed in the Malaysian Code on Corporate Governance 2017.

Financial Exhibits

Asia	Financial summary	Dec-21	Dec-22	Dec-23F	Dec-24F	Dec-25F
Malaysia	Recurring EPS (MYR)	0.04	0.08	0.08	0.08	0.09
Property	EPS (MYR)	0.04	0.08	0.08	0.08	0.09
Pavilion REIT	DPS (MYR)	0.04	0.08	0.09	0.09	0.09
PREIT MK	BVPS (MYR)	1.27	1.33	1.40	1.42	1.33
Neutral	Return on average equity (%)	3.3	6.2	6.4	6.3	6.5
	Weighted avg adjusted shares (m)	3,036.70	3,055.72	3,350.80	3,648.92	3,874.32
Valuation basis	Valuation metrics	Dec-21	Dec-22	Dec-23F	Dec-24F	Dec-25F
Dividend discount model	Recurring P/E (x)	28.95	14.88	14.38	14.17	13.78
	P/E (x)	28.95	14.88	14.38	14.17	13.78
	P/B (x)	0.9	0.9	0.9	0.8	0.9
	FCF Yield (%)	6.5	8.5	11.9	11.8	11.5
	Dividend Yield (%)	3.7	7.0	7.2	7.3	7.5
	EV/EBITDA (x)	-	0.23	0.41	0.15	0.26
	EV/EBIT (x)	-	0.23	0.41	0.15	0.26
Key drivers	Income statement (MYRm)	Dec-21	Dec-22	Dec-23F	Dec-24F	Dec-25F
i. Improvement in domestic consumer sentiment;	Total turnover	489	570	710	841	877
ii. Increasing number of foreign tourists;	EBITDA	210	332	398	487	510
iii. Strong market positioning of Pavilion KL.	Depreciation and amortisation	(1)	(0)	(0)	(0)	(0)
	Operating profit	209	332	398	487	509
	Net interest	(84)	(85)	(118)	(178)	(172)
	Pre-tax profit	126	246	280	309	338
	Recurring net profit	126	246	280	309	338
Key risks	Cash flow (MYRm)	Dec-21	Dec-22	Dec-23F	Dec-24F	Dec-25F
Downside risks include weaker-than-expected retail performance occupancy rates, and rental reversions.	Change in working capital	15	(40)	60	8	2
	Cash flow from operations	246	322	489	527	545
	Capex	(10)	(10)	(10)	(10)	(10)
	Cash flow from investing activities	(7)	(153)	(2,188)	12	12
	Dividends paid	(130)	(195)	(272)	(303)	(333)
	Cash flow from financing activities	(185)	(219)	1,257	161	(493)
	Cash at beginning of period	341	312	333	0	684
	Net change in cash	54	(49)	(441)	700	64
	Ending balance cash	396	263	(108)	700	748
Company Profile	Balance sheet (MYRm)	Dec-21	Dec-22	Dec-23F	Dec-24F	Dec-25F
A retail-focused REIT in Malaysia. Owner of the iconic Pavilion KL Mall.	Total cash and equivalents	312	333	0	684	726
	Tangible fixed assets	1	1	1	1	1
	Total investments	5,880	6,045	8,245	8,245	8,245
	Total assets	6,239	6,483	8,125	8,758	8,760
	Short-term debt	395	800	800	950	950
	Total long-term debt	1,778	1,394	2,394	2,406	2,418
	Total liabilities	2,380	2,423	3,423	3,585	3,597
	Shareholders' equity	3,858	4,060	4,702	5,173	5,163
	Total equity	3,858	4,060	4,702	5,173	5,163
	Net debt	1,861	1,861	3,194	2,672	2,642
	Total liabilities & equity	6,239	6,483	8,125	8,758	8,760
Key metrics	Key metrics	Dec-21	Dec-22	Dec-23F	Dec-24F	Dec-25F
	Revenue growth (%)	(4.2)	16.6	24.6	18.5	4.3
	Recurrent EPS growth (%)	7.9	94.6	3.5	1.5	2.9
	Operating EBITDA margin (%)	43.1	58.3	56.1	58.0	58.1
	Net profit margin (%)	25.8	43.3	39.4	36.8	38.5
	Dividend payout ratio (%)	106.9	103.8	103.0	103.0	103.0
	Capex/sales (%)	2.0	1.8	1.4	1.2	1.1
	Interest cover (x)	2.37	3.61	3.18	2.64	2.85

Source: Company data, RHB

Emissions And ESG

Trend analysis

FY22 emissions are 15% lower compared to FY19, and GHG emission intensity is 17% lower. Pavilion has replaced the chiller systems in Pavilion KL to be more efficient.

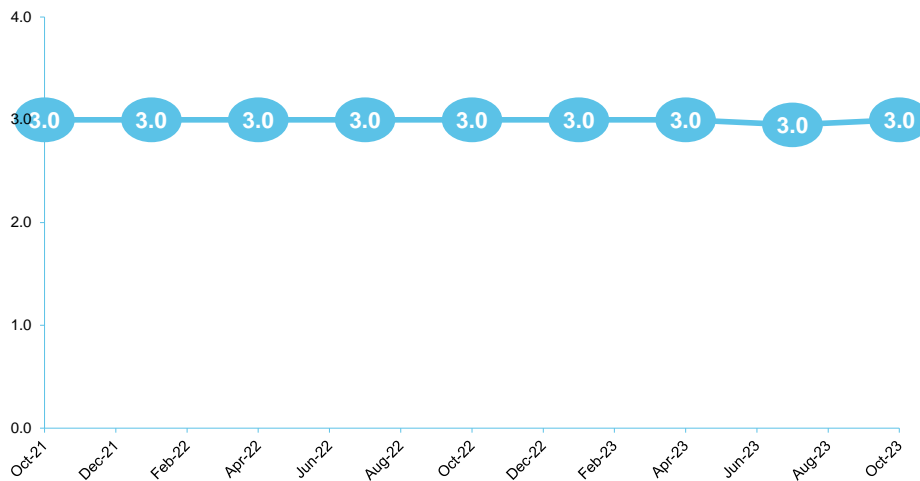
Emissions (tCO2e)	Dec-20	Dec-21	Dec-22
Scope 1	-	-	-
Scope 2	53,044	48,271	55,056
Scope 3	-	-	-
Total emissions	53,044	48,271	55,056

Source: Company data, RHB

Latest ESG-Related Developments

- Signed memorandum of understanding with five renewable companies to explore the purchase of electricity generated by solar for three malls.
- Subscribed to Green Energy Tariff scheme for Pavilion KL to pivot towards green energy

ESG Rating History



Source: RHB

Results at a Glance

Figure 1: Pavilion REIT's results summary

FYE Dec (MYRm)	3Q22	2Q23	3Q23	QoQ (%)	YoY (%)	9M22	9M23	YoY (%)	Comments
Revenue	143.6	160.0	199.2	24.5	38.7	423.9	515.6	21.6	3Q23 includes full quarter contribution from PBJ vs only one month in 2Q23
Net property income (NPI)	90.2	101.0	121.4	20.1	34.5	267.3	324.5	21.4	
Interest expense	(23.3)	(31.6)	(42.9)	35.7	84.1	(66.8)	(100.8)	50.9	Drawdown of additional borrowings for the acquisition
Interest income	2.0	2.5	3.0	20.9	50.9	4.4	8.2	87.2	
EI	0.0	0.0	0.0	nm	nm	0.0	0.0	nm	
Others	(30.8)	(40.1)	(53.3)	32.9	73.1	(23.6)	(28.4)	20.6	
Pretax profit	61.2	62.9	70.6	12.2	15.4	181.4	203.5	12.2	
Tax	0.0	0.0	0.0	nm	nm	0.0	0.0	nm	
Minority Interest	0.0	0.0	0.0	nm	nm	0.0	0.0	nm	
Net Profit	61.2	62.9	70.6	12.2	15.4	181.4	203.5	12.2	
Core Profit	61.2	62.9	70.6	12.2	15.4	181.4	203.5	12.2	Missed expectations, at only 70% of our and Street's estimates.
Earnings Per Unit (sen)	2.00	1.93	1.91	(1.0)	(4.5)	5.94	6.13	3.2	
Dividends Per Unit (sen)	2.08	2.04	2.15	5.4	3.4	6.16	6.56	6.5	
NPI Margin (%)	62.8	63.1	60.9			63.1	62.9		
Pretax Margin (%)	42.6	39.3	35.4			42.8	39.5		
Net Margin (%)	42.6	39.3	35.4			42.8	39.5		

Source: Company data

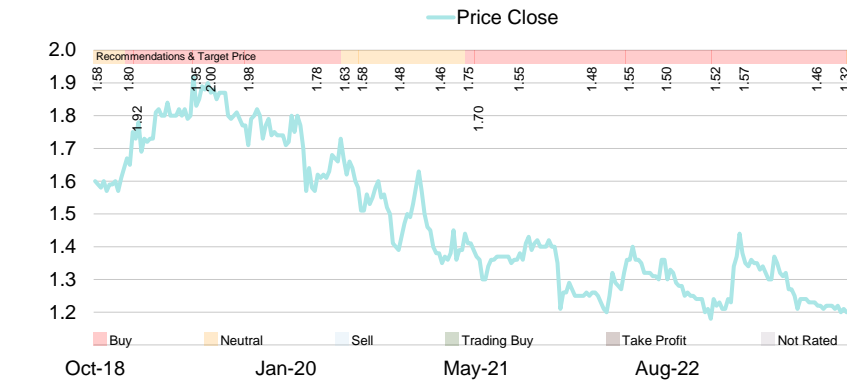
Figure 2: Pavilion REIT's revenue by property

FYE Dec (MYRm)	3Q22	2Q23	3Q23	QoQ (%)	YoY (%)	9M22	9M23	YoY (%)
Pavilion KL Mall	115.3	116.3	122.9	5.7	6.7	341.2	366.8	7.5
Intermark Mall	6.1	6.2	6.4	3.8	5.8	17.9	18.9	5.8
Da Men Mall	3.4	3.5	3.5	0.3	2.6	9.9	10.4	4.6
Pavilion Tower	2.4	2.2	2.1	(2.1)	(12.6)	7.4	6.6	(10.7)
Elite Pavilion	16.5	17.6	19.2	9.5	16.9	47.6	53.7	12.9
Pavilion Bukit Jalil	nm	14.3	45.0	215.7	nm	0.0	59.3	nm
Total revenue	143.6	160.0	199.2	24.5	38.7	423.9	515.6	21.6

Figure 3: Pavilion REIT's net property income by property

NPI by Property	3Q22	2Q23	3Q23	QoQ (%)	YoY (%)	9M22	9M23	YoY (%)
Pavilion KL Mall	78.8	82.3	85.6	4.0	8.6	233.2	259.3	11.2
Intermark Mall	2.3	2.4	2.8	12.8	20.4	6.4	8.0	25.9
Da Men Mall	(2.7)	(2.2)	(2.0)	(11.4)	(26.3)	(5.9)	(6.7)	13.8
Pavilion Tower	1.0	0.9	0.5	(45.2)	(48.0)	3.3	1.9	(42.0)
Elite Pavilion	10.8	10.3	12.3	19.6	13.6	30.3	32.5	7.3
Pavilion Bukit Jalil	nm	7.3	22.1	203.9	nm	0.0	29.4	nm
Total net property income	90.2	101.0	121.4	20.1	34.5	267.3	324.5	21.4

Recommendation Chart



Source: RHB, Bloomberg

Date	Recommendation	Target Price	Price
2023-10-16	Neutral	1.32	1.20
2023-07-28	Buy	1.46	1.23
2023-04-25	Buy	1.57	1.33
2023-02-01	Buy	1.57	1.35
2022-11-24	Buy	1.52	1.18
2022-10-28	Buy	1.50	1.24
2022-07-29	Buy	1.50	1.36
2022-04-29	Buy	1.55	1.32
2022-01-28	Buy	1.48	1.26
2021-10-29	Buy	1.55	1.42
2021-10-20	Buy	1.55	1.40
2021-08-06	Buy	1.55	1.36
2021-04-30	Buy	1.70	1.39
2021-04-06	Buy	1.75	1.42
2021-01-29	Neutral	1.46	1.38

Source: RHB, Bloomberg

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Trading Buy:	Share price may exceed 15% over the next 3 months, however longer-term outlook remains uncertain
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