REHDA

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Less-than-stellar earnings season, ongoing glut fail to dampen sentiment

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PETALING JAYA: Despite the less-than-stellar performance of many listed property companies during the recent corporate earnings season, investor confidence in local property stocks has actually been steadily increasing this year.

Year-to-date, the KL Property Index (made up of the listed shares of property companies) has risen by 14%, outperforming the FBM KLCI which has grown just 8% during the same period.

This is in spite of the ongoing property glut that some experts reckon will last until next year.

The performance of the KL Property Index this year has many industry observers and analysts believing that the market has likely bottomed out, and that an improved earnings performance is on the horizon for local property stocks.

A similar trend is being seen in Singapore, where property stocks are set for their best annual performance in five years, with some strategists believing that the rally is far from over.

According to a Bloomberg report last week, with an expected pick-up in real estate following the easing of curbs on housing, developers are expected to be the bright spot in Singapore equities as gains in the city-state's stocks may be limited for the rest of the year.

It said the city-state's government sparked renewed interest in the Singapore real estate market after it rolled back some curbs in March, following a 3½-year slump in home prices – the longest stretch of decline since the data was first published in 1975.

"In the same month, housing sales surged to the highest in nearly four years as developers sold more than twice the number of homes compared with the previous year," Bloomberg reported from government data.

In a sector report last month, MIDF Research said Malaysian property sales are poised to grow in 2017 after three consecutive months of year-on-year (y-o-y) increase in approved loans.

"Based on Bank Negara's monthly statistical bulletin for March 2017, approved loans for the purchase of property has increased 3% y-o-y to RM11.43bil.

"The increase is mainly driven by the 20% increase in loan applications, which implies that demand has improved significantly."

MIDF said "the uptrend of better sales" for developers was confirmed after approved loans registered positive growth for its third consecutive month in March.

For the first quarter of 2017 (1Q17), approved loans grew by 9% to RM28.62bil. On a monthly basis, approved loans surged 35% month-on-month due to a 40% increase in loan applications.

"In our view, the higher approved loans disbursed into the market is a good leading indicator that property transaction values have increased and hence property developers' sales should naturally improve."

JP Morgan in a recent research note said the pick-up in property loans could be attributed to "quality customers" coming back, as well as affordable properties below RM500,000 per unit.

"The loan rejection rate also declined to 50% in March 2017," it said.

MIDF said the Consumer Sentiment Index (CSI) also improved in 1Q17.

"The latest publication from the Malaysian Institute of Economic Research shows that the 1Q17 CSI had improved to 76.6 from 69.8 and 72.9 in 4Q16 and 1Q16, respectively.

"We gather that consumers are generally more optimistic and have indicated their cautiously ambitious spending plans. We believe that the data suggests that the demand outlook for property among the potential buyers has improved and this should translate to better sales in 2017."

The research house added that the House Price Index (HPI) growth was stable as at 4Q16.

HPI growth remains positive as it grew by 5.6% y-o-y to 243.3 in 4Q16 although it is lower than the five-year average growth of 9.1%.

"There is also some decline quarter-on-quarter but we think that this should be temporary, as the Malaysian economy has picked up."

Among the key states, MIDF said the highest y-o-y growth was recorded in Selangor (8.2% y-o-y to 244.5).

"This is followed by Johor (7.7% growth), Kuala Lumpur (5.3%) and Penang (0.7%). We believe that the outlook for property price growth is better in Greater KL due

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to the support from the urbanisation factor."

According to JP Morgan, the batch of property stocks that it covers, namely Eco World Development Group Bhd, SP Setia Bhd, UEM Sunrise Bhd, Sunway Bhd and Mah Sing Group Bhd, have unbilled sales from domestic projects at 0.6 to 1.9 times of the 2016 property revenue, with Eco World recording the highest ratio.

"For developers with overseas projects (SP Setia, Sunway and UEM Sunrise), total unbilled sales stand at 1.2 to two times the 2016 property revenue.

"Overseas projects in Australia and the UK will have back-ended earnings and cash-flow recognition, coming onstream from 2016 or 2017 for SP Setia and since 2016 for UEM Sunrise."

Of the stock it covers, JP Morgan said only Sunway had exposure to dollar debt (RM2.13bil or 37% of total debt), although this is fully hedged.

"Balance sheets are generally healthy. Following completion of a de-gearing exercise, Eco World's net gearing will also be reduced to more comfortable levels of 67% and 56% for 2017 and 2018 respectively."

JP Morgan pointed out that potential corporate restructuring activities within the local property sector will also lead to more liquid property plays by late 2017.

The research house said Sime Darby's proposed demerger of its property division, as well as SP Setia's proposed acquisition of I&P Group Sdn Bhd, will lead to larger property plays.

"Sime Darby Property's asset turnover to realise earnings for the division has been slow, but longer term, it benefits from a large asset base and strategically located landbank.

"SP Setia's proposed acquisition of I&P will raise its domestic landbank size by 80% to 9,508 acres (10,078 acres including landbank for international projects), with exposure to the growth areas of Klang Valley and Johor, which will likely strengthen its market position."

In view of price discounts, incentives and aggressive promotions, the shift to more affordable product mixes, cost pressures and increased compliance costs, JP Morgan said domestic margins for local property stocks are expected to remain under pressure.

"However, margins for SP Setia and UEM Sunrise are expected to hold up or improve due to increased contributions in 2017 and 2018 from overseas projects, which fetch stronger operating margins."

The research house said UEM Sunrise's margins are also recovering from a low base (as seen in its Q1'17 results) from the reversion of an over-estimation in construction costs in 2016 for projects approaching completion.

"Eco World's margins are also anticipated to rise, given the low base and its exit from the start-up phase with higher economies of scale.

"The company's overall operating margins are anticipated to normalise to between 14% and 16% by 2018 or 2019."

The Kuala Lumpur-Singapore high-speed rail project, which is slated for completion by 2026, is expected to benefit local property players with projects where the track runs through.

JP Morgan said Greater KL is likely to benefit first from the project - with Eco World's Bukit Bintang City Centre being a key beneficiary.

"There are expected to be two stations in the Greater KL area, at Bandar Malaysia in the Kuala Lumpur city centre (the main terminal/end station) and at Putrajaya in the southern part.

"In the city, the centre of gravity of the Golden Triangle/KL is likely to shift over the long term to the south and east of KL, encompassing the Bukit Bintang area away from the northeast of KL currently, where KLCC is located," according to JP Morgan

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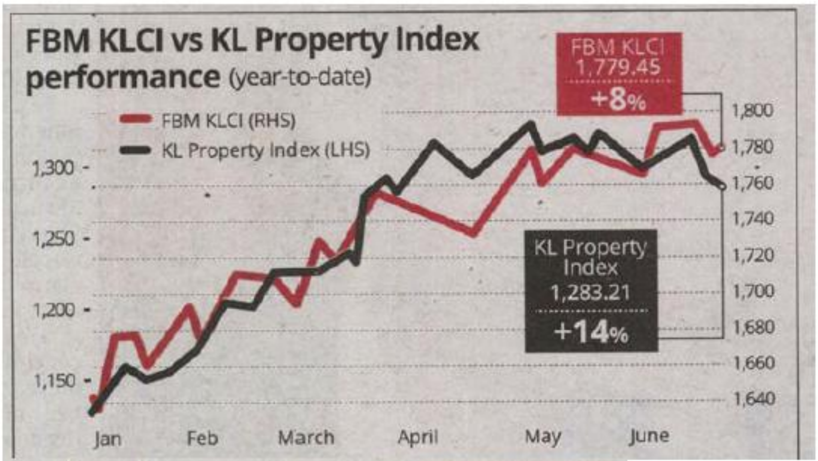

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