KDN: PP 10251/07/2013 (032736)

SECTOR UPDATE

3 June 2014

AFFIN INVESTMENT BANK
INVESTMENT BANKING • INVESTMENT MANAGEMENT • MARKET TRADING & RESEARCH
A member of the Affin Banking Group

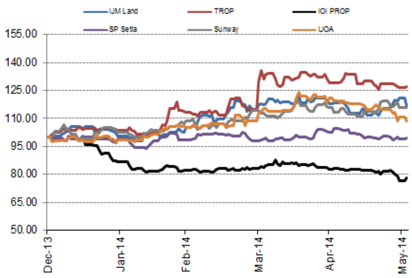
Property

NEUTRAL (maintain)

Absolute Performance (%)

	1M	3M	12M
IJM Land	+0.7	+15.2	-7.9
IOIPG	-6.3	-3.1	na
SP Setia	-5.5	0.0	-21.1
Sunway	+1.6	+6.2	-14.5
Trop	-2.6	+10.3	-28.9
UOA	-9.5	+4.5	-21.1

Relative Performance



Source: Affin, Bloomberg

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A mixed bag of results

1Q14 results – a mixed bag

The developers' 1Q14 results were mixed – 3 developers reported higher earnings yoy while 2 came in weaker due to the absence of uneven property sales (office block, development land). Sequentially, developers' earnings were on a downtrend with most developers (except IJM Land) reporting weaker earnings on lower revenue and lower profit margins. We noticed that results for developers with a stronger focus on landed properties / mid-range condominiums fared better than their counterparts who focus on mid-high end condominiums / integrated development. Overall, the sector results were slightly below our expectations (3 below, 2 in line, 1 above).

In general, weaker development profit margin

Developers are facing a margin squeeze – cost pressure is rising (higher land prices, building material costs, labour costs and compliance costs) but the ability to pass on the higher costs is limited by higher competition, tightening of banks' lending policy and weaker property market sentiment. The developers' 1Q14 EBIT margin were generally weaker qoq (except IJM Land) and we expect the sector's profit margin to remain subdued in the coming quarters.

Modest 1Q14 property sales, new launches should pick up in 2H14

The developers' 1Q14 property sales were modest. However, against a low base in 1Q13 (buying interest was low as buyers held back on purchases awaiting the outcome of the general election), the developers' 1Q14 property sales were generally higher yoy. We note, however, that the sector's 1Q14 property sales were the weakest quarterly sales since 2Q13. The introduction of new property cooling measures during Budget 2014 (end-October 2013) has affected the availability of credit, property market sentiment and the number of new property launches. The developers had generally held back their launches in 1Q14 in response to the new property cooling measures. We expect property sales to pick up slightly in 2H14 as developers adjust their pricing strategy/ product mix and step up new property launches in 2H14.

Maintain NEUTRAL

We maintain our **NEUTRAL** rating on the sector. While we remain cautious on the 2014 property market outlook, we believe that the negatives are largely priced in and the downside risk to share prices is limited, given: (i) the developers are now trading at a fair 0.6-0.7x P/RNAV (except Tropicana), broadly within their historical trading ranges; (ii) the sector's CY15E PER of 10.4x is grossly below KLCI's 14.6x; (iii) the developers' balance sheets are generally strong and their 2014-15 earnings are still resilient; and (iv) the long-term fundamentals (demographics, economic environment) have remained supportive.

Top picks are IJM Land and Tropicana

For exposure to the sector, we prefer developers with a strong focus in the Klang Valley and landed properties / mass housing segment. Our top pick for the property sector is **IJM Land (BUY, TP: RM3.80).** We like the group for its strong management, good branding, geographically diversified land bank and strong focus on townships/ mass housing developments. We also like **Tropicana (BUY, TP: RM1.83)** for its strategic land bank, undemanding valuation of 0.4x P/RNAV and ongoing asset monetisation and de-gearing exercise.

Peers Comparison

Stock	Rating	Sh Pr (RM)	TP (RM)	Mkt Cap (RMm)	Year End	Core PE (x) CY14	Core PE (x) CY15	EPS growth (%) CY14	EPS growth (%) CY15	P/RNAV (x)	P/B (x)	ROE (%) CY14	ROE (%) CY15	Div Yield (%) FY14	Div Yield (%) FY15
IOIPG	REDUCE	2.52	2.50	8,162	June	13.2	9.9	28.0	33.7	0.6	0.7	4.2	7.0	1.4	1.6
SP Setia	REDUCE	2.91	2.80	7,155	Oct	16.0	14.7	-9.6	8.7	0.6	1.3	7.8	8.4	4.5	4.8
Sunway	REDUCE	3.09	3.15	5,326	Dec	11.3	11.0	-14.8	2.9	0.7	1.0	8.6	8.3	3.2	3.2
IJMLand	BUY	3.04	3.80	4,739	Mar	11.5	10.6	4.6	8.1	0.7	1.4	13.2	11.6	2.3	2.5
UOA Dev	ADD	2.10	2.22	2,814	Dec	8.6	8.5	-5.8	2.1	0.7	1.1	12.9	12.5	6.7	7.1
Tropicana	BUY	1.50	1.83	2,083	Dec	6.7	7.5	30.8	-10.7	0.4	0.8	11.7	10.0	4.7	4.7

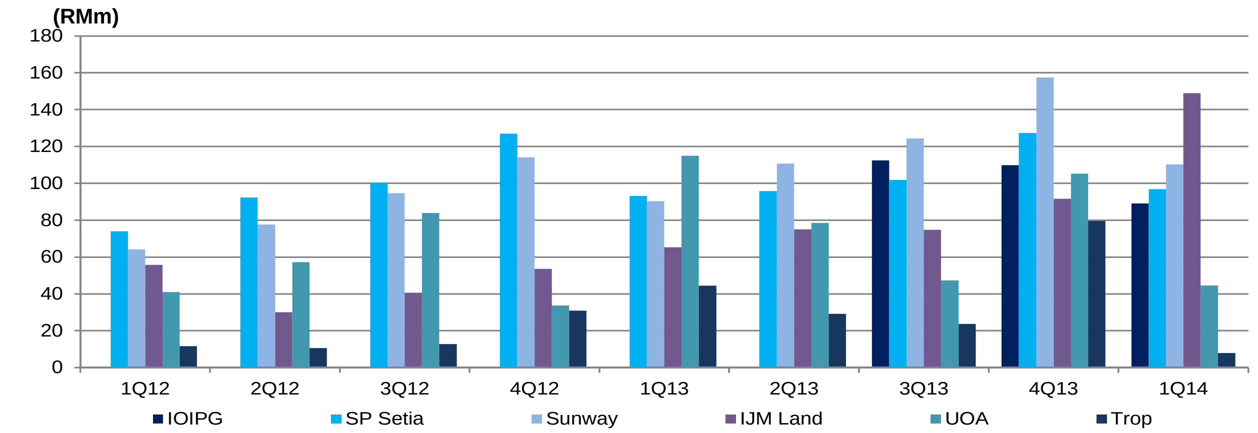
Source: Affin Note: Pricing as of close on 2 June 2014

1Q14 results: A mixed bag

1Q14 earnings slightly disappoint

The developers' 1Q14 results were mixed – 3 developers reported higher earnings yoy (on higher progress billings) while 2 came in weaker due to the absence of uneven property sales (office block, development land). Sequentially, developers' earnings were clearly on a downtrend as most developers (except IJM Land) reported weaker earnings on lower revenue and lower profit margins. However, we noticed that earnings for developers with a strong focus on landed properties / mid-range condominiums had fared better than their counterparts who focus on mid-high end condominiums / integrated development. Overall, the sector results were slightly below our expectations (1 above, 2 in line, 3 below).

Fig 1: Developers' sequential core net profit

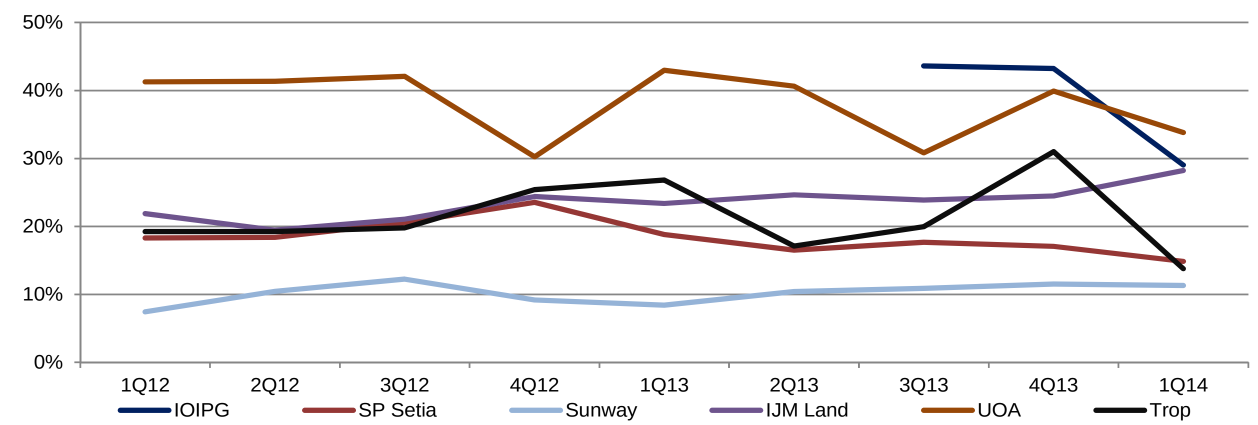


Source: Company, Affin

Weaker development profit margin

We opine that developers are generally facing a margin squeeze. Higher land prices, building material costs, labour costs and compliance costs have pushed up property development costs while the developers face challenges in passing on the cost due to higher competition and weaker property market sentiment. As a result, the developers' 1Q14 EBIT margins were generally weaker qoq (except IJM Land). Notable declines include IOIPG (due to a change in product mix), UOA (absence of sales of near completion/ completed projects) and Tropicana (absence of land sales). IJM Land bucked the trend, reporting higher EBIT margins qoq due to the completion of some key development projects. Also, we believe that IJM Land's strong focus in the landed residential market has helped to sustain its profit margin (due to low historical land cost and lower competition, for now).

Fig 2: Developers' EBIT margin trend



Source: Company, Affin

Key earning changes

Our key earnings cuts / upgrades post the results include:

(i) IOIPG – Earnings disappointed on weaker-than-expected Singapore property sales and weak profit margins. We cut our FY14E EPS forecast by 23%, imputing a lower sales projection for FY14 after deferring the launches of Cape Royale and South Beach Residences to FY15. We have also lowered the projects' take-up rate and margin assumption;

(ii) SP Setia – Earnings were below expectations due to margin erosion as a result of rising costs as well as lower operational efficiency due to the high staff turnover. We have cut our FY14-16E EPS forecast by 10-12%;

(iii) Tropicana – Results fell short of our forecast due to higher-than-expected project costs. We cut our FY14 EPS by 8%, imputing higher admin and marketing costs; and

(iv) IJM Land – Results beat our expectations on higher-than-expected progress billings and profit margins from its ongoing projects (Rimbayu, Seremban 2, Shah Alam 2). We raised our FY15 EPS forecast by 5%, imputing a higher margins assumption. We opine that IJM Land's profit margins from its landed residential properties will likely hold up better than those from its peers' high rise/ integrated developments.

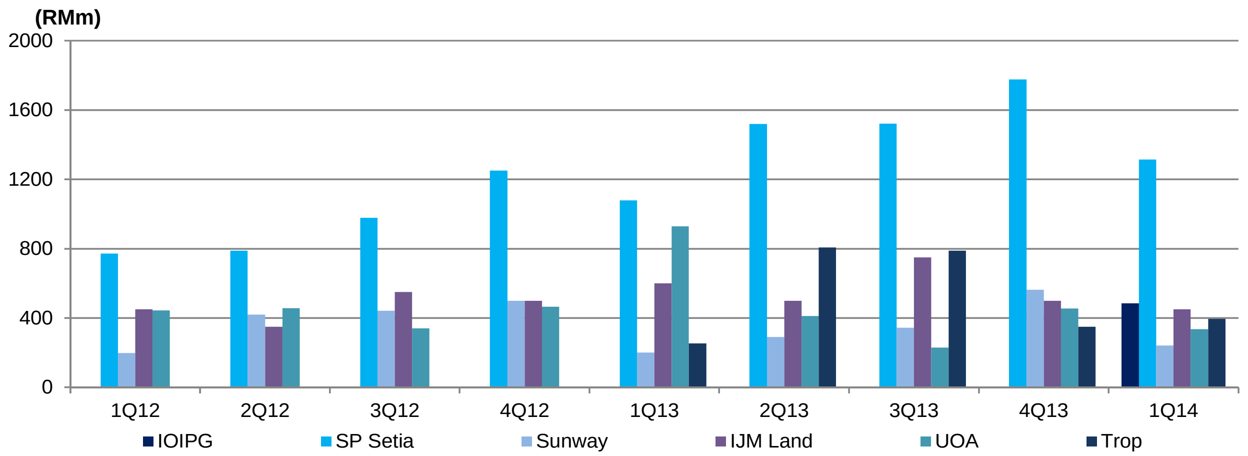
Sales trend: Modest 1Q sales, launches should pick up in 2H

Modest 1Q14 property sales

The developers' 1Q14 property sales were modest. However, against a low base in 1Q13 (buying interest was low as buyers held back on purchases awaiting the outcome of the general election), the developers' 1Q14 property sales were generally higher yoy. We note, however, that the sector's 1Q14 property sales were the weakest quarterly sales since 2Q13. The introduction of new property cooling measures during Budget 2014 (end-October 2013) has affected the availability of credit, property market sentiment and the number of new property launches.

The developers had generally held back their launches in 1Q14 in response to the new property cooling measures. We expect property sales to pick up slightly in 2H14 as developers adjust their pricing strategy/ product mix and step up new property launches in 2H14.

Fig 3: Property sales trend (excluding Australia and UK projects)



Source: Company, Affin

Valuation and Recommendation

Maintain NEUTRAL

We maintain our **NEUTRAL** rating on the sector. While we remain cautious on the property market outlook for 2014 and are mindful of the ongoing profit margin squeeze, we believe that the negatives are largely priced in and the downside risk to share prices is limited, given:

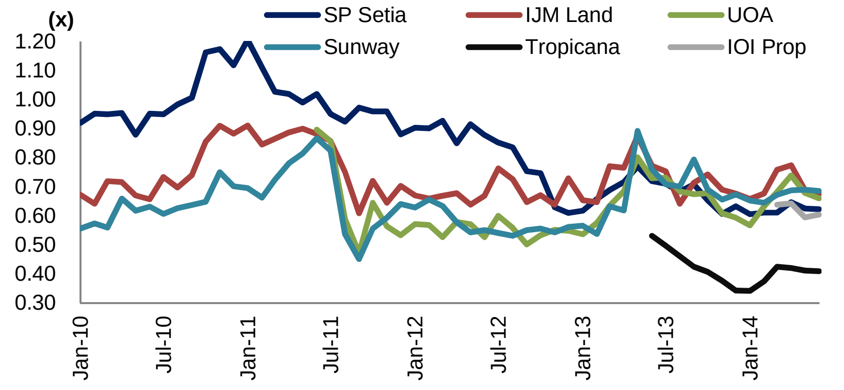
(i) the developers now trade at a fair 0.6-0.7x P/RNAV (except Tropicana), broadly within their historical trading ranges;

(ii) the property sector's CY15 PER of 10.4x is grossly below KLCI's 14.6x;

(iii) developers' balance sheets are generally strong and their 2014-15 earnings are still resilient, backed by high unbilled sales; and

(iv) the long-term fundamentals (demographics, economic environment) have remained supportive.

Fig 4: Developers' historical P/RNAV



Source: Bloomberg, Affin

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Fig 5: Property peers comparison

Stock	Rating	Sh Pr	TP	Mkt Cap	Year	Core PE (x)		EPS growth (%)		P/RNAV	P/B	ROE (%)		Div Yield (%)	
		(RM)	(RM)	(RMm)	End	CY14	CY15	CY14	CY15	(x)	(x)	CY14	CY15	FY14	FY15
IOIPG	REDUCE	2.52	2.50	8,162	June	13.2	9.9	28.0	33.7	0.6	0.7	4.2	7.0	1.4	1.6
SP Setia	REDUCE	2.91	2.80	7,155	Oct	16.0	14.7	-9.6	8.7	0.6	1.3	7.8	8.4	4.5	4.8
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Tropicana	BUY	1.50	1.83	2,083	Dec	6.7	7.5	30.8	-10.7	0.4	0.8	11.7	10.0	4.7	4.7

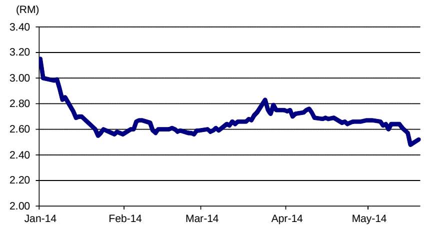
Source: Affin
Note: Pricing as of close on 2 June 2014
Note: When a report covers six or more subject companies please access important disclosures for Daiwa Capital Markets Hong Kong Limited at http://www.daiwacm.com/hk/research_disclaimer.html or contact your investment representative or Daiwa Capital Markets Hong Kong Limited at Level 26, One Pacific Place, 88 Queensway, Hong Kong.

Key investment risks

Key upside risks to our **NEUTRAL** view on the sector are: (i) stronger-than-expected property sales where demand turns out to be more resilient than expected; and (ii) higher-than-expected market valuation for the upcoming major property IPOs (Iskandar Waterfront Holdings, Medini Iskandar Malaysia).

Key downside risks include: (i) weaker-than-expected property sales; (ii) higher-than-expected competition induced by the entry of foreign developers; and (iii) a steeper-than-expected hike in the mortgage financing cost.

Stock summary



Source: Affin, Bloomberg

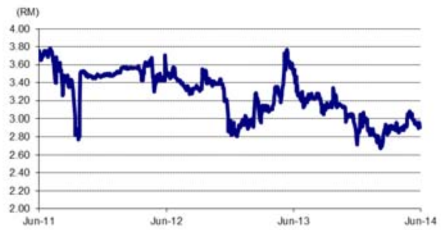
IOIPG (REDUCE, TP: RM2.50)

We are generally cautious on the broad property market outlook, especially in certain market segments such as high-end condos and integrated developments in Johor, Singapore and China where IOIPG has large exposure. Our TP of RM2.50 is based on a 40% discount to RNAV.

Earnings & Valuation Summary

FYE 30 Jun	2012	2013	2014E	2015E	2016E
Revenue (RMm)	1,052.2	1,323.3	1,619.0	1,982.5	2,888.1
EBITDA (RMm)	514.0	636.9	621.0	784.8	1,098.4
Pretax profit (RMm)	755.7	904.8	811.1	992.0	1,141.7
Net profit (RMm)	599.8	693.6	636.7	791.6	863.2
EPS (sen)	18.5	21.4	19.7	24.4	26.7
PER (x)	13.6	11.8	12.8	10.3	9.5
Core net profit (RMm)	447.4	520.9	446.3	791.6	863.2
Core EPS (sen)	13.8	16.1	13.8	24.4	26.7
Core EPS growth (%)	(11.4)	16.4	(14.3)	77.4	9.0
Core PER (x)	18.2	15.7	18.3	10.3	9.5
Net DPS (sen)	-	-	3.5	4.0	4.5
Dividend Yield (%)	-	-	1.4	1.6	1.8
EV/EBITDA (x)	-	12.9	13.4	10.9	8.2
Consensus profit (RMm)	-	-	478.8	662.7	916.8
Affin/Consensus (x)	-	-	0.9	1.2	0.9

Source: Affin, Bloomberg



Source: Affin, Bloomberg

SP Setia (REDUCE, TP: RM2.80)

We believe the persistent uncertainty over the group's strategic direction and leadership transition will lead to a further exodus of talent. This will, in turn, affect its operations and profit margins. We value SP Setia at a 40% discount to its RNAV, a discount to peers' average valuation. That said, we believe the downside risk to the share price will be partly cushioned by the group's strategic land bank and strong unbilled sales of over RM10bn.

Earnings & Valuation Summary

FYE 31 Oct	2012	2013	2014E	2015E	2016E
Revenue (RMm)	2,526.6	3,060.5	3,589.5	4,524.7	5,823.6
EBITDA (RMm)	532.5	543.2	639.8	778.3	963.4
Pretax profit (RMm)	567.5	570.3	660.0	756.6	943.3
Net profit (RMm)	393.4	417.9	474.9	537.4	677.5
EPS (sen)	20.5	17.9	19.3	21.9	27.6
PER (x)	14.2	16.2	15.1	13.3	10.6
Core net profit (RMm)	393.4	417.9	474.9	537.4	677.5
Core EPS (sen)	20.5	17.9	19.3	21.9	27.6
Core EPS growth (%)	27.1	(12.6)	7.7	13.2	26.1
Core PER (x)	14.2	16.2	15.1	13.3	10.6
Net DPS (sen)	10.5	10.6	13.0	14.0	14.0
Dividend Yield (%)	3.6	3.6	4.5	4.8	4.8
EV/EBITDA (x)	15.4	16.5	13.3	10.8	8.2
Consensus profit (RMm)	-	-	508.7	648.3	782.2
Affin/Consensus (x)	-	-	0.9	0.8	0.9

Source: Affin, Bloomberg

Source: Affin, Bloomberg

Sunway (REDUCE, TP: RM3.15)

While we like Sunway for its integrated real estate business model and experience in the construction sector, we opine that the current share price has fairly reflected these positive attributes. Further weakness in the high-end condominium / integrated development segment may potentially drag on the group's property sales and share price performance. Our TP of RM3.15 is based on a 30% discount to RNAV.

Earnings & Valuation Summary

FYE 31 Dec	2012	2013	2014E	2015E	2016E
Revenue (RMm)	3,849.2	4,527.6	5,470.0	5,496.3	5,879.0
EBITDA (RMm)	469.6	608.3	656.2	664.2	683.4
Pretax profit (RMm)	722.9	1,007.8	699.3	705.4	751.2
Net profit (RMm)	530.6	839.3	469.8	483.4	543.0
EPS (sen)	41.1	55.7	27.3	28.0	31.5
PER (x)	7.5	5.6	11.3	11.0	9.8
Core net profit (RMm)	350.6	482.7	469.8	483.4	543.0
Core EPS (sen)	27.1	32.0	27.3	28.0	31.5
Core EPS growth (%)	7.2	18.0	(14.8)	2.9	12.3
Core PER (x)	11.4	9.7	11.3	11.0	9.8
Net DPS (sen)	6.0	10.0	10.0	10.0	12.0
Dividend Yield (%)	1.9	3.2	3.2	3.2	3.9
EV/EBITDA (x)	11.9	10.9	10.7	10.1	9.6
Consensus profit (RMm)	-	-	494.0	534.8	553.4
Affin/Consensus (x)	-	-	1.0	0.9	1.0

Source: Affin, Bloomberg

Source: Affin, Bloomberg

IJM Land (BUY, TP: RM3.80)

IJM Land is our top pick for the sector. We believe IJM Land's property sales will be more resilient relative to peers, given its primary focus on township projects / mass market housing development and better geographical diversification. We value IJM Land at a 15% discount to RNAV.

Earnings & Valuation Summary

FYE 31 Mar	2013	2014	2015E	2016E	2017E
Revenue (RMm)	1250.1	2046.2	2254.6	2274.2	2279.1
EBITDA (RMm)	288.6	534.5	550.9	531.7	557.4
Pretax profit (RMm)	320.1	701.0	610.8	635.1	695.5
Net profit (RMm)	215.1	533.2	397.0	419.0	456.4
EPS (sen)	15.2	34.2	25.5	26.9	29.3
PER (x)	20.0	8.9	11.9	11.3	10.4
Core net profit (RMm)	189.7	390.3	397.0	419.0	456.4
Core EPS (sen)	13.4	25.0	25.5	26.9	29.3
Core EPS growth (%)	-3.9	86.8	1.7	5.5	8.9
Core PER (x)	22.7	12.1	11.9	11.3	10.4
Net DPS (sen)	5.0	6.0	7.0	7.5	8.0
Dividend Yield (%)	1.6	2.0	2.3	2.5	2.6
EV/EBITDA (x)	14.6	9.2	8.1	7.9	7.0
Consensus profit (RMm)	-	-	385.7	435.6	504.0
Affin/Consensus (x)	-	-	1.0	1.0	0.9

Source: Affin, Bloomberg

Source: Affin, Bloomberg

UOA (ADD, TP: RM2.22)

We like UOA for its strong cash position and good dividend yield. The key risk is its high project concentration in the integrated, high-rise property market. Our TP of RM2.22 is based on a 30% discount to RNAV.

Earnings & Valuation Summary

FYE 31 Dec	2012	2013	2014E	2015E	2016E
Revenue (RMm)	799.2	1,245.5	1,216.1	1,248.7	1,262.9
EBITDA (RMm)	321.8	501.3	453.8	466.3	418.6
Pretax profit (RMm)	414.2	577.9	471.6	488.5	463.2
Net profit (RMm)	301.3	362.8	326.0	332.9	344.1
EPS (sen)	23.7	27.1	24.3	24.8	25.7
PER (x)	8.9	7.8	8.6	8.5	8.2
Core net profit (RMm)	215.9	346.1	326.0	332.9	344.1
Core EPS (sen)	17.0	25.8	24.3	24.8	25.7
Core EPS growth (%)	4.9	52.1	(5.8)	2.1	3.4
Core PER (x)	12.4	8.1	8.6	8.5	8.2
Net DPS (sen)	12.0	13.0	14.0	15.0	15.0
Dividend Yield (%)	5.7	6.2	6.7	7.1	7.1
EV/EBITDA (x)	7.2	4.0	5.2	5.1	5.6
Consensus profit (RMm)	-	-	345.3	368.3	397.5
Affin/Consensus (x)	-	-	0.9	0.9	0.9

Source: Affin, Bloomberg

Source: Affin, Bloomberg

Tropicana (BUY, TP: RM1.83)

We like Tropicana for its strategic land bank, proactive management and attractive valuation of 0.4x P/RNAV. A timely, well executed asset monetization plan would be the key re-rating catalyst.

Earnings & Valuation Summary

FYE 31 Dec	2012	2013	2014E	2015E	2016E
Revenue (RMm)	630.4	1475.5	1267.7	1266.0	1456.3
EBITDA (RMm)	143.5	304.6	493.7	419.4	364.6
Pretax profit (RMm)	224.9	503.6	441.5	383.6	337.0
Net profit (RMm)	171.1	362.3	312.0	288.1	242.4
EPS (sen)	32.5	35.2	22.5	20.1	16.9
PER (x)	4.6	4.3	6.7	7.5	8.9
Core net profit (RMm)	66.0	177.0	312.0	288.1	242.4
Core EPS (sen)	12.5	17.2	22.5	20.1	16.9
Core EPS growth (%)	-9.3	37.3	30.9	-10.9	-15.8
Core PER (x)	12.0	8.7	6.7	7.5	8.9
Net DPS (sen)	4.8	7.4	7.0	7.0	7.5
Dividend Yield (%)	3.2	4.9	4.7	4.7	5.0
EV/EBITDA (x)	16.8	9.7	7.4	8.6	9.7
Consensus profit (RMm)	-	-	217.5	218.8	210.0
Affin/Consensus (x)	-	-	1.4	1.3	1.2

Source: Affin, Bloomberg

Equity Rating Structure and Definitions

BUY	Total return is expected to exceed +15% over a 12-month period
TRADING BUY (TR BUY)	Total return is expected to exceed +15% over a 3-month period due to short-term positive development, but fundamentals are not strong enough to warrant a Buy call. This is to cater to investors who are willing to take on higher risks
ADD	Total return is expected to be between 0% to +15% over a 12-month period
REDUCE	Total return is expected to be between 0% to -15% over a 12-month period
TRADING SELL (TR SELL)	Total return is expected to exceed -15% over a 3-month period due to short-term negative development, but fundamentals are strong enough to avoid a Sell call. This is to cater to investors who are willing to take on higher risks
SELL	Total return is expected to be below -15% over a 12-month period
NOT RATED	Affin Investment Bank does not provide research coverage or rating for this company. Report is intended as information only and not as a recommendation
OVERWEIGHT	Industry, as defined by the analyst's coverage universe, is expected to outperform the KLCI benchmark over the next 12 months
NEUTRAL	Industry, as defined by the analyst's coverage universe, is expected to perform inline with the KLCI benchmark over the next 12 months
UNDERWEIGHT	Industry, as defined by the analyst's coverage universe is expected to under-perform the KLCI benchmark over the next 12 months

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