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REITs become preferred option for cautious investors

By EUGENE MAHALINGAM
eugenicz@thestar.com.my

Zarina: REITs are backed by high yields and this has proven to be attractive.

WITH the current global economic uncertainties and sluggish Malaysian property market, real estate investment trusts (REITS) have become a favoured option for many cautious investors to grow their income.

Zarina Halim, chief corporate officer and executive director of Hektar Asset Management Sdn Bhd, the manager of Hektar Real Estate Investment Trust (Hektar REIT), acknowledges that interest in REITS is growing at a time of uncertainty.

"REITs are backed by high yields and this has proven to be attractive. Furthermore, REITs are backed by hard assets – commercial property – which is historically seen as a hedge against inflationary or a reliable store of wealth," she tells StarBizweek in an e-mail.

Zarina explains that there is a confluence of events now, namely the US-China trade war which is turning into a currency war, geo-political tensions and rising economic tensions which are converging into a "flight to safety" by investors.

"The US-China trade war may see collateral damage. Many trading nations inter-dependent on the US-China industrial supply chain will be affected, South-East Asian countries included.

"Furthermore, the US Federal Reserve has reduced interest rates which have being echoed by other central banks around the world and in the region. Combine all these factors and you can understand that with all this uncertainty, investors are choosing to go with stable investments backed by hard assets. Even precious metals are tending up as investors are looking for safe havens."

Within the Malaysian context, Zarina says the most conservative investor will still keep their money in cash, adding however that even local banks have reduced their fixed deposit rates due to the recent overnight policy rate cut in the last quarter.

"Malaysian REITs, which are yielding anywhere between 5% and 8%, are therefore a very compelling vehicle for investors to hide, while riding out the turbulence. Another possible reason is that the investors prefer the quarterly or half year distribution that REITs such as Hektar REIT offer."

The Malaysia REIT Index has been on an uptrend since March 2018, hitting a high of 1, 015.45 on Aug 2, 2019, according to Bloomberg. Year-to-date, the index has risen 9.58%.

Hektar REIT is Malaysia's first listed retail-focused REIT and was listed on the Main Market of Bursa Malaysia on Dec 4, 2006. It currently owns two million square ft of retail space in four states with assets valued at RM1.2bil as at Dec 31, 2018.

Hektar REIT's portfolio of commercial properties includes Subang Parade in Selangor; Mahkota Parade in Melaka; Wetex Parade & Classic Hotel in Muar, Johor; Central Square in Sungai Petani, Kedah; Kulim Central in Kedah and Segamat Central in Johor.

Going forward, Zarina says Hektar REIT intends to double or even triple its assets in the next 10 years and provide a more diversified and balanced portfolio for its investors.

"We envision Hektar REIT to have a presence in many major urban and suburban areas throughout Malaysia. Half of our portfolio consists of malls which are typically the only mall in town and the other half are considered leaders in their respective markets.

"At the end of the day, we hope to extrapolate this portfolio on a nation-wide basis, including East Malaysia. We would like to see Hektar malls as a bellwether for domestic middle-class consumption. To reach this objective, obviously we need to increase the size of the portfolio."

She says this will be achieved organically as well as via third-party acquisitions.

"Specifically, we are exploring more consulting work as a prelude to development work, mainly in the form of joint venture partnerships with developers. The idea is to partner with township developers to leverage our leasing relationships and track record with retailers to develop relevant retail concepts for the catchment market.

"So you would see that within a decade, we hope to expand our capabilities from just management to also include development, but once again strictly focused on our core competencies, which is retail."

Looking at the track record of larger retail-focused REITs in the US and Australia, Zarina says that a "template" already exists.

"Therefore, within a decade, we hope to diversify our earnings with property management, retail consultancy and retail development income."

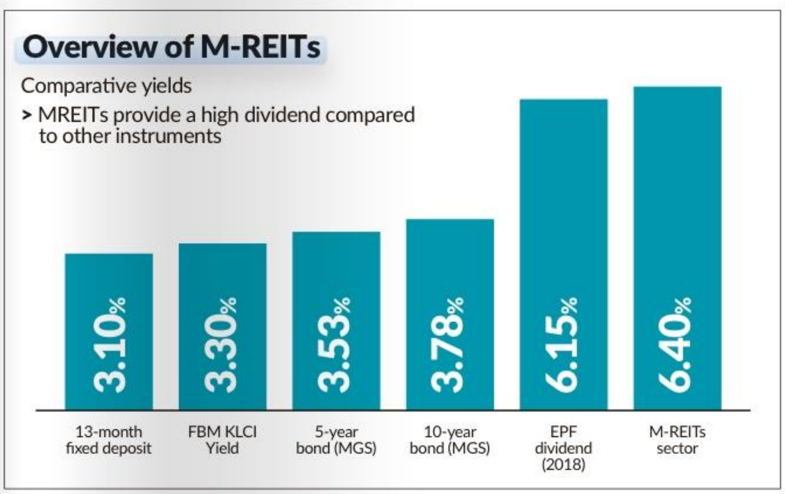
With the REIT sector investing in commercial property assets, Zarina says that there will be opportunities for REITs wherever there is growth in new types of commercial estate.

"The office and retail sectors are subjected to cycles. The new REIT guideline which took effect in 2018 has allowed REITs to engage in property development and has boosted the growth of industrial sector, because it generally requires shorter time and lesser capital expenditure to construct industrial property compared to structuring acquisitions.

"Currently, it is experiencing growth drivers due to the rise of logistics players, driven by online commerce growth and international companies setting up manufacturing hub and logistics centres in Malaysia."

Zarina says that the self-storage sector is one for investors to watch.

"It is a large space in the US REIT market and as Malaysians become more affluent, they too, will likely need to rent more storage space. Essentially, any commercial property sector which is experiencing improving commercial prospects has an opportunity to consider REITs as a vehicle."



On the subject of healthcare REITS, Zarina says there is the common assumption that as the population grows, there will be a demand for more hospitals.

"Healthcare is known to be a recession-resistant industry and healthcare REITs seem resilient against downturns due to the nature of the industry and its demand. However, the healthcare REIT's dividend growth is comparatively slow because of its long leases.

"Data centre REITs is another example. There are five in the US, supported by the growth of the Internet. So long as there is prospects for long term growth in the commercial property type, then there is a business case for the REIT."

Going forward, Zarina reiterates emphasizes that the company's focus will remain in retail.

"We believe retail still has a strong, long-term business case in Malaysia. We do continue to observe new commercial property types and particularly areas adjacent to retail. Optimally we would like to find synergies with commercial properties and retail."

She notes that for retail REITs, private consumption and consumer sentiment play a part in the portfolio's performance.

"During economic downturn, consumers tend to spend lesser and this impacts directly tenants operation's cash flows and their ability to pay their rental which affects the REITs bottom line and valuation.

"Yes, we are optimistic that the REIT industry will recover and that steps are taken to ensure that we are back on track. We do the best we can to manage the factors that are in our control and keep ourselves updated to ensure that the situation remains favourable towards our REIT."