

'Prospects for property stocks positive'

BY Racheal Lee

The current good property sales trend is expected to continue for at least the next 12 months in spite of concerns over the potential of further hikes in the overnight policy rate (OPR), ECM Libra Capital Sdn Bhd head of research Bernard Ching said at *The Edge* Investment Forum on Real Estate 2010.

This, he added, is because of the attractive mortgage schemes offered by banks and the upfront cost absorption by developers.

"Anecdotal evidence shows that property sales in fact remained strong a week after the recent 25bps OPR hike announced by Bank Negara [Malaysia] recently. I personally visited some property launches and noticed some were sold out within three hours. Against such a backdrop, the prospects for property counters on Bursa Malaysia remain positive. Furthermore, some property stocks are still trading at a decent valuation," he said.

'Look at the fundamentals'

Ching warned property stock investors not to buy them just because they are cheap. Investors should look at the fundamentals of the property development company rather than its stock price, he said during the panel discussion on investing in "Property, REITs or property stocks".

This, he noted, is especially crucial when "most of the property counters listed on Bursa Malaysia are trading below their book value".

Among the fundamentals that investors should take into consideration are the developers' gearing, management, sales track record, product delivery, landbank replenishment as well as their products and geographical segmentation to current demand.

While landbank replenishment creates higher value for property developers, the alignment of a company's products and geographical segmentation to current demand can be determined by categorising the company into business type, product type and project location.

Business segmentation involves tagging a company either as a pure property development company, a property investment company or a REIT (real estate investment trust). Product segmentation, meanwhile, focuses on the core product type which a company develops, such as residential, office or retail.

Geographical segmentation refers to the location where the developer's projects are located.

Ching said investors can look out for the stocks of high-growth developers for capital gains and invest in REITs for stable dividends.



ABDUL GHANI ISMAIL/THE EDGE

Ching: Don't buy property stocks just because they are cheap

The average return on Malaysian REITs since their initial public offering is 10.4% while the dividend yield for 2010 is at 8.8%, he added.

Physical property against property stocks

The size of investments in the equity market is smaller than investments in physical property, as the former is now traded in quantum of 100 units, allowing investors to pay less than RM500 even for the most expensive property stock on Bursa Malaysia.

Liquidity is one of the biggest advantages of property stock investments. The property equity market has relatively higher liquidity than physical property because property stocks offer easy diversification, said Ching. "Diversification of physical property is possible but capital intensive."

The Malaysian property stock market tends to have a reputation for being the least liquid compared with other equities, he noted.

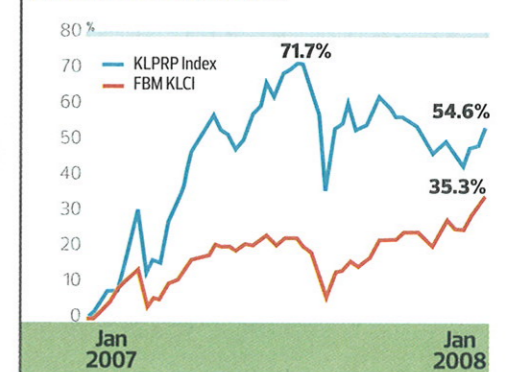
"Property stocks offer dividends and capital appreciation, while physical property can bring in rental returns and capital appreciation. For physical property investors, income tax will be imposed on the rental and RPGT (real property gains tax) will be imposed on the properties that are disposed of within five years. Property stocks have no capital tax and single-tier dividends are normally tax-free," Ching said, adding that property stocks also involve a lower transaction cost of less than 1% compared with physical property.

But there are more funding opportunities in buying physical property, such as from savings in the Employees Provident Fund (EPF) and bank loans of up to 90%. Margin financing for stocks tends to be quite expensive.

With property stocks, one can invest in different types of underlying properties such as hotels, industrial, malls and hospitals. Such investment opportunities would be impossible for most physical property investors.

"Property stock investors do not have management control over a property, while physical property investors do. The question is, does everybody want control? Control also comes with responsibility. If you own a property, the tenant might call you in the middle of the night to tell you that the pipe just burst or something. In that sense, property stocks come with less maintenance," Ching said.

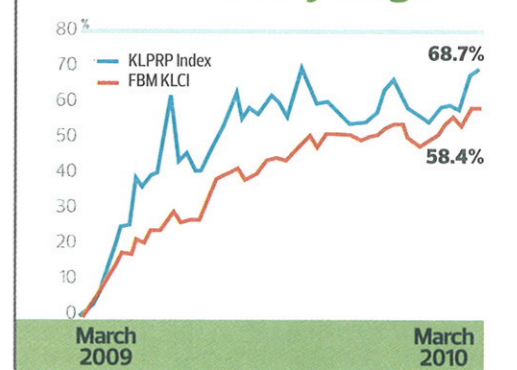
Property stocks outperform in a bull market



Property stocks underperform in a bear market



Property stocks perform better in recovery stage



Property stocks are also more volatile than physical property, as property stocks are subject to not only the demand and supply of a developer's products but also to the performance of the global economic market.

Ching observed that property counters performed better than the FBM KLCI during the economic recovery, although they were more volatile during the downturn. Property counters also outperformed the FBM KLCI before the economic downturn.

"Over the last few cycles, property stocks outperformed the benchmark index. From January to June 2007, the property index appreciated 71.7%. However, property stocks tend to be more volatile during a downturn and underperform the broad market. Since the global economic crisis, the property index has shed almost 54% versus a 44% loss in the FBM KLCI.

"On the other hand, property stocks have done very well during the current recovery cycle. Since March last year, property stocks have actually appreciated 69% compared with a 58% increase in the FBM KLCI," Ching said.

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