

MALAYSIA REITS

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The Asia
BUSINESS
FORUM

LEVERAGING ON THE DIFFERENT CLASSES OF PROPERTY ASSETS

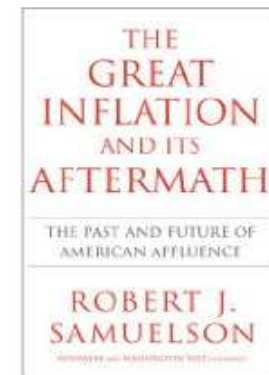


By **ELVIN FERNANDEZ, FISM, FRICS**
MANAGING DIRECTOR
CHARTERED SURVEYOR

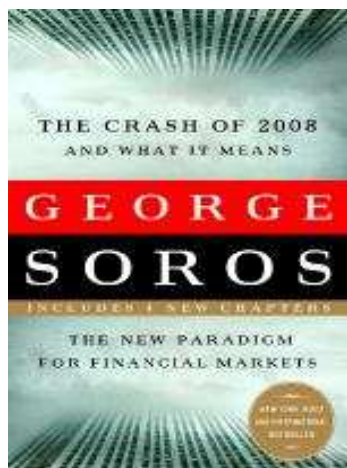


This paper will be presented with the aid of three excel based financial models that will firstly show value at risk analysis in support of REITs in any portfolio and an outline model of a Malaysian REIT to show, the link from the critical need for in-depth understanding of property to corporate aspects in REIT valuation, REIT management and REIT investment. The third model is the Markowitz model to derive the optimal asset allocation - equities vs REITs

1. "The Great Inflation and its Aftermath" by Robert Samuelson who traces the rise and fall of inflation in the lead economy of the world, the U.S economy as the principal background setting for the crisis. The central message of the book was: thinking the world less risky, people took actions that made it more risky. The pleasures of prosperity backfired and the book concludes with some suggestions but on the note that if the lessons of the past are not properly learnt, the sequel will be even more devastating.



2. George Soros in his recent book "The Crash of 2008 and what it means", that "The bursting of the U.S housing bubble served as a detonator that set off a much larger explosion: the bursting of a super-bubble that has been growing since the 1980s..."



ANDREW ROSS SORKIN

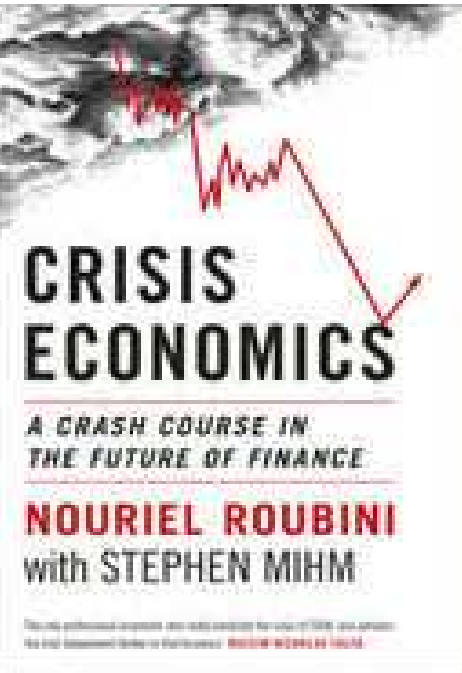
TOO BIG TO FAIL

INSIDE THE BATTLE
TO SAVE WALL STREET



5. It was only through a massive dose of capital injections and stimuli that the world was saved. To start the ball rolling, according to Andrew Ross Sorkin's Bestseller "Too Big To Fail", "Paulson told Bush in no uncertain terms that the financial system was collapsing.

' If we don't act boldly, Mr. President,' he said, 'we could be in a depression deeper than the Great Depression,' an assessment with which Bernanke concurred." Indeed the U.S. and the whole world did act boldly as they, in a coordinated manner, pumped billions of dollars into the world economy.



7. A takeaway from a more recent publication: *Crisis Economics* by Nouriel Roubini and Stephen Mihm is the contrasting remedies for severe economic downturns by Keynesian "pump-priming" on the one hand and Joseph Schumpeter's "creative destruction" on the other hand. The authors accept both ideas and say that whilst Keynesian pump-priming is essential for the short term, aspects of "winnowing" or painful but positive adjustments are needed in the medium to long term so that survivors will create a new economic order.

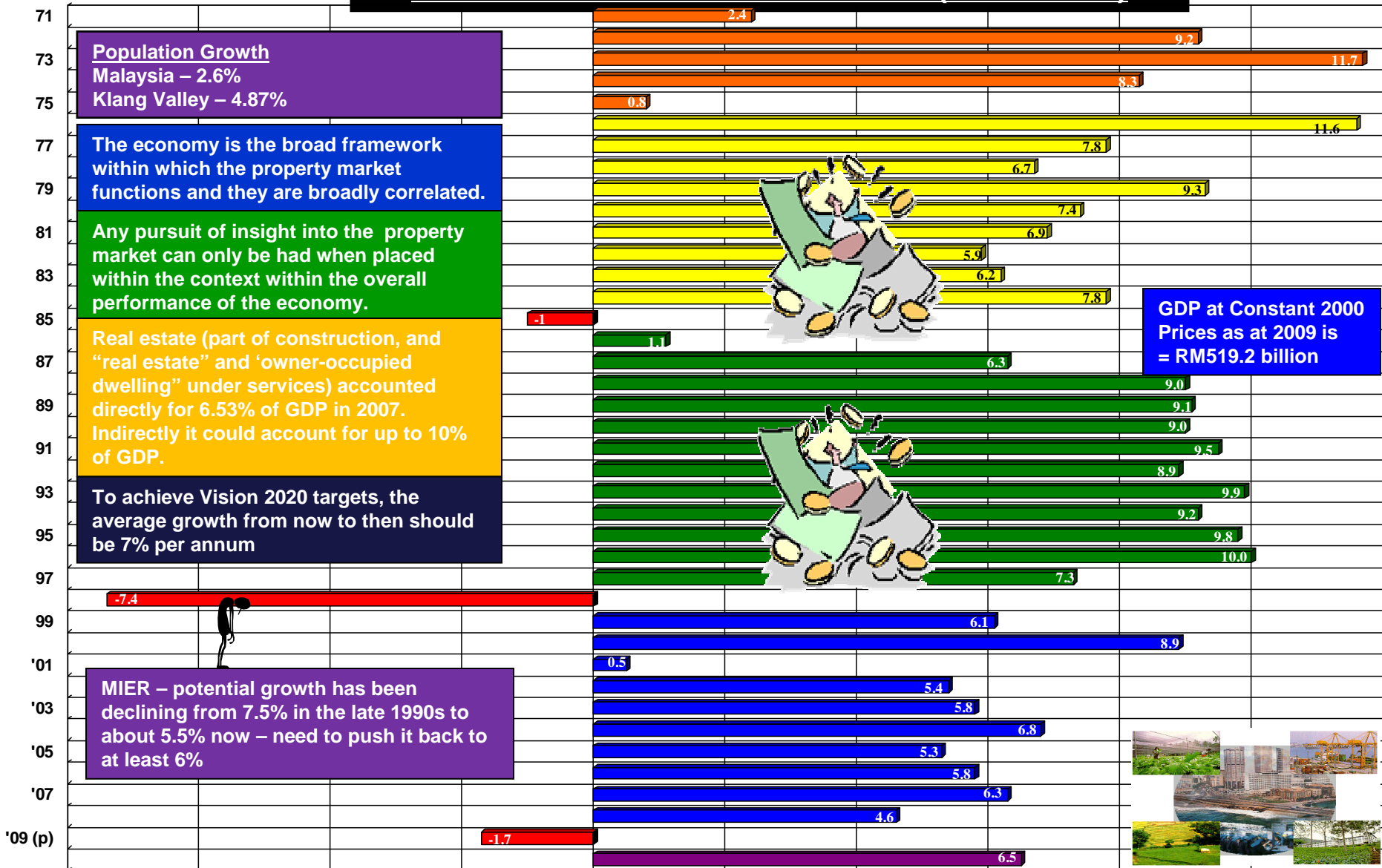
8. In a recent article in the Financial Times, July 12, 2010, By Nouriel Roubini and Ian Bremmer think that the **"global economy is heading for a serious slowdown this year.**

- a) Emergency austerity programmes in some countries will put a drag on growth.
- b) Inventory adjustments will run their course.
- c) The effects of tax policies that steal demand from the future – such as the US “cash for clunkers” scheme, tax credits for home buyers or cash for green appliances – will fizzle out.
- d) Labour market conditions will remain weak.
- e) The slow and painful deleveraging of balance sheets and income-challenged households, financial institutions and governments will continue.
- f) The result is governments and consumers that spent too much and now need to deleverage – in the US, Britain, Spain, Greece and elsewhere – will spend, consume and import less.



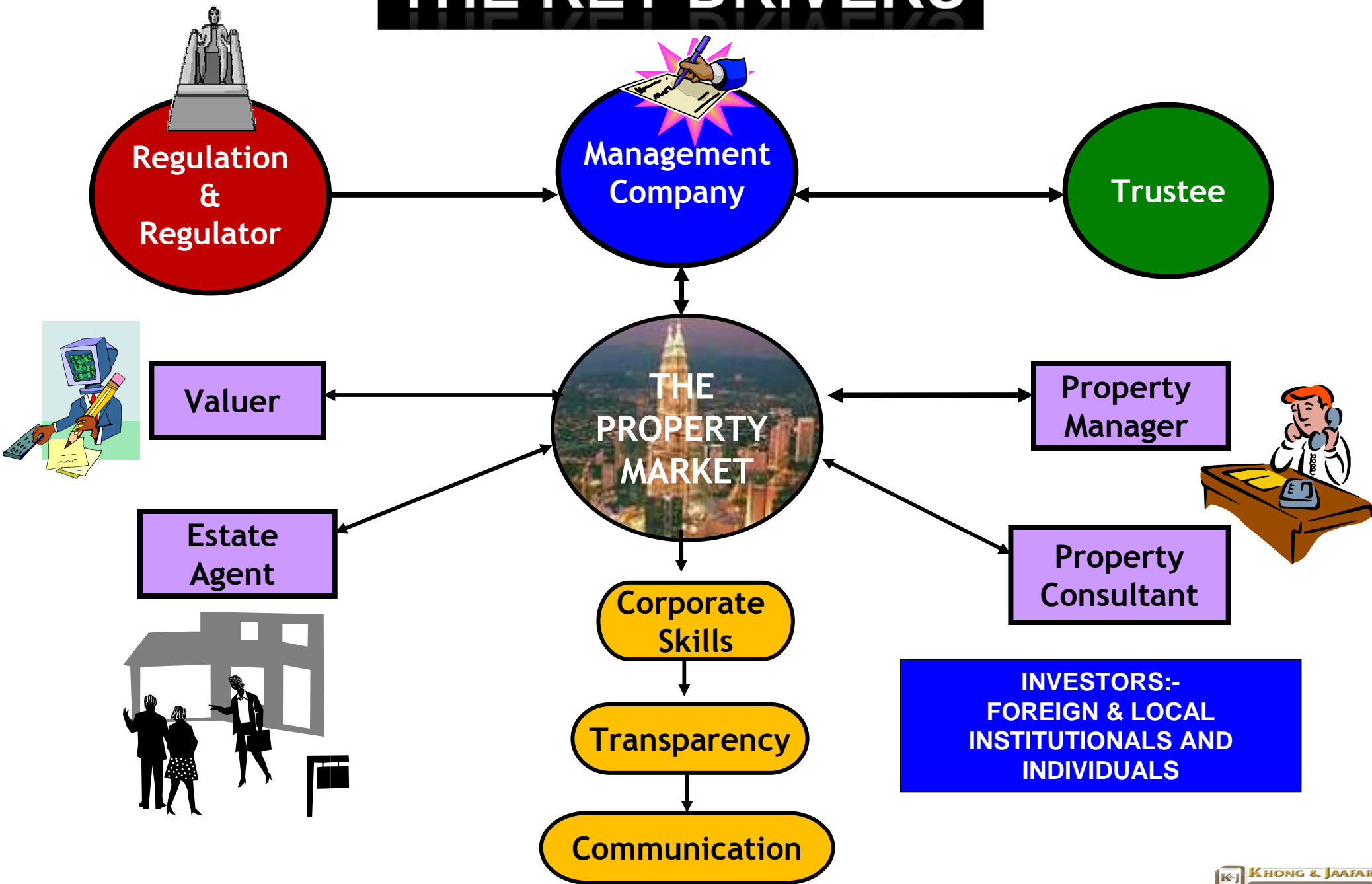
9. But those governments and consumers that saved too much – in China, emerging Asia, Germany and Japan – are not spending more. In a world of excess supply, the recovery of global aggregate demand will be weak, pushing global growth much lower. **The most realistic scenario for global growth is painful, even if we avoid a double dip. In the US, 1.5 per cent growth in the second half of this year and into 2011 will feel like a recession, given a probable further rise in unemployment, larger budget deficits, a further fall in home prices, larger losses by banks on mortgages and loans, and the risk that a protectionist surge will further damage relations with China."**

THE MALAYSIAN ECONOMY - GDP (% CHANGE)



| | | | | | | | | | | | |
|--------------|--------------|--------------|------------|-------------|------------|------------|------------|------------|------------|------------|------------|
| 1Q03 = 4.6 | 2Q03 = 4.6 | 3Q03 = 5.3 | 4Q03 = 6.6 | 1Q04 = 7.8 | 2Q04 = 8.4 | 3Q04 = 6.7 | 4Q04 = 5.8 | 1Q05 = 6.1 | 2Q05 = 4.1 | 3Q05 = 5.3 | 4Q05 = 5.2 |
| 1Q06=6.0 | 2Q06=6.1 | 3Q06=6.0 | 4Q06= 5.9 | 1Q07=5.5 | 2Q07=5.7 | 3Q07=6.7 | 4Q07=7.4 | 1Q08 = 7.4 | 2Q08 = 6.7 | 3Q08 = 4.7 | 4Q08 = 0.1 |
| 1Q09 = (6.2) | 2Q09 = (3.9) | 3Q09 = (1.2) | 4Q09 = 4.4 | 1Q10 = 10.1 | | | | | | | |

THE KEY DRIVERS



SUPPLY AND TAKE-UP OF OFFICE SPACE IN MALAYSIA AS AT JUNE 2010

| STATE | TOTAL (GVT & PRIVATE BUILDINGS) | | | | | PRIVATE BUILDINGS | | | | |
|-----------------|---------------------------------|--------------------------|-----------------------------------|---------------------------|--------------------|-------------------|--------------------------|-----------------------------------|---------------------------|--------------------|
| | NO OF BLDGS | TOTAL SPACE IN SQ FT MIL | TOTAL SPACE OCCUPIED IN SQ FT MIL | VACANT SPACE IN SQ FT MIL | OCCUPANCY RATE (%) | NO OF BLDGS | TOTAL SPACE IN SQ FT MIL | TOTAL SPACE OCCUPIED IN SQ FT MIL | VACANT SPACE IN SQ FT MIL | OCCUPANCY RATE (%) |
| WP KL | 385 | 71.93 | 58.43 | 13.5 | 81.23% | 339 | 66.89 | 53.64 | 13.25 | 80.19% |
| SGOR | 144 | 24.51 | 19.26 | 5.25 | 78.58% | 131 | 22.38 | 17.14 | 5.24 | 76.59% |
| WP PJ'JAYA | 27 | 16.81 | 16.01 | 0.8 | 95.24% | 5 | 1.49 | 0.74 | 0.75 | 49.66% |
| K VALLEY | 556 | 113.25 | 93.7 | 19.55 | 82.74% | 475 | 90.76 | 71.52 | 19.24 | 78.80% |
| JOHOR | 211 | 11.00 | 8.22 | 2.78 | 74.73% | 137 | 7.71 | 5.58 | 2.13 | 72.37% |
| P PINANG | 235 | 11.60 | 9.14 | 2.46 | 78.79% | 178 | 9.39 | 6.97 | 2.42 | 74.23% |
| PERAK | 205 | 6.51 | 6.18 | 0.33 | 94.93% | 64 | 2.50 | 2.21 | 0.29 | 88.40% |
| N SEMBILAN | 94 | 2.87 | 2.65 | 0.22 | 92.33% | 37 | 1.21 | 1.05 | 0.16 | 86.78% |
| MELAKA | 74 | 2.90 | 2.66 | 0.24 | 91.72% | 43 | 1.72 | 1.48 | 0.24 | 86.05% |
| KEDAH | 89 | 3.09 | 2.84 | 0.25 | 91.91% | 47 | 1.65 | 1.50 | 0.15 | 90.91% |
| PAHANG | 132 | 3.03 | 2.81 | 0.22 | 92.74% | 67 | 1.51 | 1.30 | 0.21 | 86.09% |
| T'GGANU | 110 | 3.16 | 3.07 | 0.09 | 97.15% | 31 | 0.94 | 0.90 | 0.04 | 95.74% |
| KELANTAN | 271 | 3.73 | 3.73 | 0 | 100.00% | 121 | 1.84 | 1.67 | 0.17 | 90.76% |
| PERLIS | 42 | 0.98 | 0.98 | 0 | 100.00% | 19 | 0.44 | 0.44 | 0 | 100.00% |
| SABAH | 94 | 7.24 | 6.36 | 0.88 | 87.85% | 68 | 5.34 | 4.48 | 0.86 | 83.90% |
| WP LABUAN | 11 | 0.71 | 0.53 | 0.18 | 74.65% | 5 | 0.53 | 0.41 | 0.12 | 77.36% |
| SARAWAK | 92 | 6.23 | 5.73 | 0.5 | 91.97% | 63 | 4.46 | 3.97 | 0.49 | 89.01% |
| MSIA | 2,216 | 176.3 | 148.6 | 27.7 | 84.29% | 1,355 | 130 | 103.48 | 26.52 | 79.60% |

* Purpose-built (as opposed to multi-purpose) signifies one primary use with supporting uses complementing it. The intended use incorporates an original design, which optimises space for its benefit. When the original design is renovated by 75% to benefit another use, the original intention is replaced by the new use. NAPIC publication of purpose built office inventory includes places where service-orientated businesses are carried out as opposed to goods being manufactured or sold. The office space is required to attend to paperwork, communication and other office activity. Therefore the term purpose-built office is used to denote buildings that are intentionally built with office as a dominant use. In data capturing and dissemination by NAPIC, dominant use means office use not less than 75% of the net lettable area. Office space information is disseminated based on the net lettable floor area according to the Uniform Methods of Measurement of Buildings published by the Institution of Surveyors Malaysia.

Source : Property Market Report, JPPH, 2Q 2010

To fully test the attraction of Malaysian REITs I have developed two separate excels models as follows:-

1. The **Markovitz Model** derives the optimal asset allocation between assets, tested here for equities (proxied by the KLCI index) and REITS (proxied by Axis Reit for Malaysia and Ascendas and Capitamall Trust for Singapore). The results for Malaysia show that for the period August 2005 - June 2009, the optimal asset allocation between these 2 asset classes is 100% equities (higher return per unit risk - sharpe) , which gives the highest portfolio Sharpe ratio. For Singapore, the results are the reverse, giving an optimal allocation of 100% to REITS and 0% to equity. Both results suggest there is little diversification between the equity and REITS asset classes.
2. The **VAR Model** quantifies the possible loss of a portfolio over a specified time horizon and with a given confidence interval. The higher the VAR amount, the more risky the portfolio.

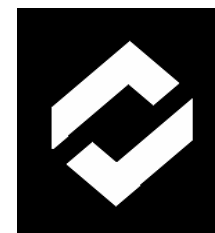
CONCLUSIONS

1. Looking at the REIT industry and its development on a regional basis, **Singapore is a shining model** to benchmark against.
2. The REIT Managers must emphasise **total returns** and promise and deliver such total returns in the order of **15 to 20%** per annum.
3. **In-depth property knowledge is key** and **transparency** to investors is fundamental.
4. The REIT industry (and beyond) is the Blue Ocean for the Property Market in Malaysia

5. The Malaysian property market **must be anchored by fundamentals**. In the **housing** market, the two fundamentals are **household income** and **rental returns**. From time to time, the market may advance on speculative binges. However, in the longer term, the market returns to the gravitational pull of the fundamentals. Different fundamentals apply for the commercial market – rental returns backed by factors such as **company profitability** or **consumer spending** or **corporate activity and tourism** for **offices**, **retail** and **hotels** respectively.
6. To make Malaysia into a property hub, the better road to take is to **strengthen the securitisation industry** which can then lead to a possible derivatives market which in fact is **“property unlimited”**. To hitch our wagon to the sale of physical property to foreigners may not be substantially fruitful. Foreigners will automatically buy property when there is sufficient long-term investment strength in the local market and in which case no selling is required. They will and they ought to come to you as a matter of investment choice. The smart money does not need to be told about investment opportunities in property. Smart money knows how to find it.



**ELVIN FERNANDEZ, FISM, FRICS
REGISTERED VALUER,
CHARTERED SURVEYOR
MANAGING DIRECTOR
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benchmark
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ISO 9001

KL HQ

57-1 Jalan Telawi Tiga
Bangsar Baru
59100 Kuala Lumpur
Tel : +6 03 2282 9699
Fax : +6 03 2282 9799
H/P : +6 012 2184542
www.khongjaafar.com.my
Email : khongja@po.jaring.my

PENANG BRANCH

89A, Lebuhr Farquhar
10200 Penang
Tel : 604 – 2614 184 / 2163 501
Fax : 604 – 262 1075
Email: khongjaa@tm.net.my

IPOH BRANCH

8, Jalan Sultan Idris Shah
30000 Ipoh
Perak Darul Ridzuan
Tel : 605 – 2411 322 / 1924
Fax : 605 – 255 2828
Email: kjipoh@po.jaring.my

**KHONG & JAAFAR PROPERTY
CONSULTANCY**

(INDIA) PVT LTD
Bangalore – 560043, Karnataka State, INDIA
Tel No : + 91-9880477461
Email : kevinrajesh@rediffmail.com