IGBB is an Awakening Property Giant worth at least RM6.75 | I3investor

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Dragon Leong blog

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Introduction

IGB Berhad (IGBB) is listed on Bursa Main Board with a market capitalization of RM2.04 billion (share base of 905.43m x current share price of RM2.25). Its principle activities are in real estate development, retails mall and hotel management. I believe IGBB would be worth at least **RM6.75** per share on cashflow valuation and up to **RM10.80** per share on sum-of-parts valuation, giving an upside of **200% to 380%** over its current share price.

What IGBB owns are so valuable

IGBB owns a majority stake in two REITs in Malaysia: (1) 53.2% stakes in IGB REIT, and (2) 51.8% stakes in IGB Commercial REIT. IGBB also owns a portfolio of hotels and landbank primarily in Malaysia, some in Australia and the UK.

IGB Commercial REIT houses most of the office towers of the group: Menara IGB, CentrePoint South & North, Boulevard properties, Gardens South & North Towers, Southpoint properties, Menara Tan & Tan, G Tower and Hampshire Place office. These office assets has been enjoying steady occupancy rate of 78% to 80%.

IGBB successfully listed IGB Commercial REIT in September 2021 and raised a total of RM1,212.5 million. IGBB received a balance proceeds of RM327 million after using RM830m of the IPO proceeds to pare down borrowings. It declared a special dividend of 12 sen per share to reward shareholders after the listing of IGB Commercial REIT.

In October 2021, IGBB's subsidiary in the UK announced to sign a deal to sell off its 50% stakes in Black Pearl Ltd for a land sale value of 208.8 million pounds (RM1.1 billion). Upon completion, IGBB shall book in a one-off disposal gain of RM190 million and receive cash proceeds of RM550 million from the deal.

Besides the above, IGBB also owns many other unlisted assets:

- Mid Valley Southkey Megamall, JB (70% stakes)
- The Gardens Hotel & Residences
- St. Giles Tank Stream Hotel, Sydney
- Cititel Hotel at Mid Valley KL, Penang and Ipoh
- The Boulevard – St. Giles Premier Hotel, KL

- Cititel Hotel at Mid Valley KL, Penang and Ipoh
- The Boulevard - St. Giles Premier Hotel, KL
- Other new office buildings, hotels and landbanks

Latest Financials of IGB REIT and IGB Commercial REIT

The latest financials of IGB REIT and IGB Commercial REIT are summarized below:

	IGB REIT		**IGB Commercial REIT**	
RM million	H1FY2022	Annualised FY2022F	H1FY2022	Annualised FY2022F
Revenue	267.6	535.2	95.5	191.0
Operating costs	(82.3)	(164.6)	(35.0)	(70.0)
EBITDA	185.3	370.6	60.5	121.0
Depn & Amort	(0.6)	(1.2)	0.0	0.0
EBIT	184.6	369.2	60.5	121.0
Interest costs & Trust fees	(25.4)	(50.8)	(24.3)	(48.6)
Pretax Profit	168.9	337.8	36.3	72.6
Tax	0.0	0.0	0.0	0.0
Net Profit	168.9	337.8	36.3	72.6
EPS (sen)	4.72	9.44	1.60	3.20
Distributable Profit	181.7	363.4		
Dividend per Unit (sen)	5.0	10.0	1.9	3.8
Dividend payouts		354.3		88.0

IGB REIT issued share base = 3,543 million; IGB Commercial REIT share base = 2,315 million

* forecast by Hong Leong research

The Q1FY2022 (Jan-March 2022) has seen a surge in covid-19 omicron wave in Malaysia but yet IGB REIT managed to register solid rebounds in 1H earnings (92% y-on-y) supported by strong footfalls in its flagship malls in Mid Valley KL. IGB Commercial REIT registered 2% q-on-q improvement in revenue for Q2FY2022 indicating steady occupancy in its office towers, but operating expenses surged 15% due to upgrading works in some office buildings. With Malaysia entering the endemic phase of the covid-19 pandemic and borders re-opened from 1st May 2022, retails footfall is expected to increase in next few months and office occupancy is expected to be steady given that most economic sectors have reopened.

Latest Financials of IGBB

The latest financials of IGBB are summarized below:

RM million	Q4FY2021	Q1FY2022	**Annualised FY2022**
Revenue	300.4	288.2	1,152.7
Operating costs	(125.0)	(135.8)	(543.2)
EBITDA	175.5	152.4	609.5
Depn & Amort	(39.0)	(35.3)	(141.2)
Share of associates	0.3	17.2	68.9

Depn & Amort	(39.0)	(35.3)	(141.2)
Share of associates	0.3	17.2	68.9
EBIT	136.5	134.3	**537.3**
Interest costs	(43.5)	(38.4)	(153.6)
Interest & inv income	11.6	8.2	32.8
Exceptionals *	193.4	0	0
Pretax Profit	297.9	104.1	416.5
Tax	(26.0)	(19.0)	(76)
Net Profit	233.8	85.1	340.5
Minorities Interest		(42.4)	(169.6)
Core Net Profit	40.4	42.7	**170.9**
Core EPS (sen)	4.46	4.72	**18.9**

*exceptional was the net gain from disposal of the Brickfriar land in the UK

The segmental performance of IGBB various business segments for FY2021 and FY2019 (before pandemic) is summarized below:

RM million	FY2019	FY2021	FY2022F *
Revenue			
Property inv - retails	673.6	486.8	676.2
Property investment - commercial	177.2	169.1	183.9
Property development	150.9	92.2	48.1
Hotel	274.5	50.7	86.0
Others	166.4	131.3	158.5
Total Revenue	**1,442.7**	**930.1**	**1,152.7**
EBIT			
Property inv - retails	431.5	262.7	479.8
Property investment - commercial	80.0	48.8	66.9
Property development	122.4	96.4	61.1
Hotel	49.4	(73.1)	34.2
Others	(20.5)	197.9	(50.8)
Unallocated Expenses	(59.9)	(58.0)	(53.7)
Total EBIT	**604.3**	**474.7**	**537.3**

*FY2022F projections are based on annualized figures of actual Q1FY2022 results

As can be seen above, IGBB cash flows were very strong in FY2019 before the pandemic. Operating cashflows before interests and tax were at RM669.25 million in FY2019, minus off net interest expenses of RM158.4m and tax payment of RM103.4m operating cash flows before capex amounted to RM407.45 million or 45 sen per share.

For FY2021, operating cashflows = RM455.2m – RM121.2m (net interests) – RM110.6m (tax) + RM63.3m (dividends received) = RM286.7 million. This was much lower than FY2019 due to lower retails mall & office building income and losses in the hotel segment.

For FY2021, operating cashflows = RM[illegible] – RM[illegible] (net interests) – RM[illegible] (tax) + RM[illegible] (dividends received) = RM286.7 million. This was much lower than FY2019 due to lower retails mall & office building income and losses in the hotel segment.

From Q1FY2022 results of IGB REIT and IGB Commercial REIT, IGBB is on track to receiving dividends of 10 sen from IGB REIT and 3.7 sen from IGB Commercial REIT. For its stakes in these 2 REITs, IGBB will receive a total dividend payouts of RM188.5m + RM45.5m = **RM234.0 million or 25.8 sen per share** from these 2 REITs alone.

IGBB achieved a revenue of RM38.0m and pre-tax profit of RM6.2m for Q1FY2022 (Jan-Mar 2022) for its unlisted Mid Valley Southkey Megamall JB, after accounting for depreciation of RM9.4m and finance costs of RM8.9m. For Q4FY2021, Mid Valley Southkey achieved revenue of RM37.1m and pre-tax profit of RM9.1m after accounting for depreciation of RM9.4m and finance costs of RM9.4m. It is then conservative to project for an annual revenue of RM152 million from Mid Valley Southkey for FY2022. Annual pre-tax profit may come in at RM152m – RM37.6m (depreciation) – RM35.6m (finance costs) – RM44m (est. operating expenses) = RM34.8 million. Annual operating cashflows (before interest & tax) will be RM34.8m + RM37.6m +RM35.6m = RM108 million.

[Check: Mid Valley Southkey has 1.5 million square feet of leasable floor area. Assuming an average leasing rate of RM8.50 psf/month or 50% discount to average leasing rate of Mid Valley Megamall and The Gardens, Mid Valley Southkey shall generate income of 1.5m sf x RM8.50/psf x 12 mths = RM153 million of annual revenue.]

Projected Cash flows and Cashflow Valuation for IGBB

We can summarise the projected cashflows of IGBB in FY2022 or any year beyond as follow:

RM million	Projected Cash flows for FY2022	Remarks
IGB REIT	188.5	10 sen dividend
Other retails malls	108.0	annualised Q1FY22 MVSKey
IGB Commercial REIT	45.5	3.8 sen dividend
Other commercial offices	21.4	Annualised Q1FY22 - IGBCR
Property development	61.1	Annualised from Q1FY2022
Hotel	34.2	Annualised from Q1FY2022
Unallocated Expenses	(53.7)	Annualised from Q1FY2022
Others	(0.0)	Assumed zero
Cashflows before interest & tax	**405.0**	

IGBB had total debts of RM4,123 million and cash of RM1,292 million as of 31 Dec 2021. Total debts are expected to get reduced by RM830 million in 2022 using IPO proceeds from listing IGB Commercial REIT and by further RM550 million from the proceeds of its UK Blackfiars land disposal, so interest costs may be saved by RM(830m+550m) x 4.2% = RM58 million a year to become RM62.8 million (RM153.6 – 32.8 – 58) a year.

So IGBB shall have operating cashflows (before capex) of RM405.0m – 62.8m (interests) – 76m (tax) = **RM266.2 million or 29.4 sen per share** every year.

However, net profit shall be at a lower level due to depreciation of unlisted assets. Looking at the core net profit of RM42.7 million registered by IGBB in Q1FY2022, I estimate that net profit for FY2022 may come in at about RM42.7m x 4 + RM58m (interest saving) = RM228.8 million. If we take into account rebounds in the hotel segment after pandemic SOP relaxed from early April and borders reopened from 1st May 2022, it is safe to assume that IGBB net profit for FY2022 may top **RM220 million or EPS of 24.3 sen**.

If we assume a 100% dividend payout ratio, then IGBB may be able declare dividends of 24.3 sen per share every year. At 5% dividend yield, IGBB may be worth RM4.86 per share.

IGBB may improve on its net profit level by injecting Mid Valley Southkey Megamall JB into IGB REIT and possible injection of all of its unlisted hotels into a new hospitality REIT. This way, the bulk of the depreciation charges (RM156m a year) would be gone as REITs do not need to depreciate assets. Furthermore, REITs do not need to pay income tax if it distributes over 90% of income as dividends. Hence, IGBB would be able to save the bulk of the income tax payments (RM76m a year) too. Listing proceeds from injecting Mid Valley Southkey into IGB REIT or listing of hotels in a new REIT could be used to pare down borrowings at holding level and hence save on interest expenses (RM96m a year).

For now, I ignore the potential tax savings and interest expenses saving from the potential REIT listing but just take the projected cashflows of RM266.2 million above as a basis for my cashflow valuation of IGBB. At 7% free cash flow yield, IGBB should be worth RM4.20 per share.

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Sum-of-Part Valuation

The sum-of-parts valuation of IGBB is potentially much higher as it owns 2 REITs and many unlisted assets. I summarise the valuation as follow:

	RNAV (RM million)	RM per share
Adjusted Shareholders' Equity at Dec2021*	1,875	2.07
Listed Entities	**4,244**	4.69
IGB REIT (53.2% stakes of market cap @ tp 1.80)	3,393	
IGB CR (51.8% stakes @ IPO price 0.71)	851	
Net Revaluation Surplus of Major Properties	**3,144**	3.08
Mid Valley Southkey Megamall ^ (70% stakes)	1,512	
The Gardens Hotel & Residences KL #	260	
St Giles Tank Stream Hotel Sydney #	282	
Cititel Hotel MV KL #	151	
The Boulevard – St Giles Premier Hotel KL #	115	
Others (office buildings, hotels & landbank) #	824	
Net gain from Brickfiair land disposal	193	
Balance proceed from IGB CR listing	327	
TOTAL RNAV	**9,783**	**10.80**

*Adjusted shareholders' equity exclude book value of Mid Valley Megamall KL, The Gardens, Menara Southpoint, G Tower, Menara Tan & Tan and Hampshire Place Office

^Mid Valley Shouthkey Megamall is estimated to be worth RM2.16billion based on 5% dividend yield of projected EBIT of RM108 million for FY2022

estimated value as per CIMB research report dated 2 April 2022

Major Catalysts for IGBB

(1) Injection of Mid Valley Southkey Megamall into IGB REIT

Mid Valley Southkey Megamall has been operating for over 2 years and enjoyed occupancy rate of 87.61% as stated in IGBB Annual Report 2021. With the border with Singapore reopened since April 2022, retails footfall to Mid Valley Southkey Megamall has improved and occupancy rate is expected to rise further to above 90% later this year.

With Covid-19 pandemic largely behind us in Malaysia, this Mid Valley Southkey Megamall should enjoy steady rental income from now on and hence it is ripe for IGBB to inject Mid Valley Southkey Megamall into IGB REIT.

With 1.5 million sf of leasable floor area, Mid Valley Southkey Megamall may rake in annual revenue of RM152m and EBITDA of about RM108 million (i.e. revenue RM152m – operating expenses of RM44m) for FY2022. As the mall is relatively new, there is scope for further upsides in terms of occupancy rates and tenancy rates. With borders reopened from 1st April 2022, it is reasonable to expect for occupancy rate to improve from 87.61% in 2021 by 10% to 96.37% in next 1-2 years. Assuming that average leasing rate will improve by 10% from RM8.50 psf in 2021 to RM9.35 psf by 2023, annual revenue shall increase by 20% from RM152m currently to RM182m by 2023. The RM30m increase in revenue will flow directly to the bottom line assuming same operating expenses. Hence EBITDA or operating cashflows may improve to RM138 million by 2023.

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At 5.0% dividend yields, Mid Valley Southkey may be valued at RM2.76 billion which may be satisfied with a combination of cash and new shares when injected into IGB REIT (for comparison, Mid Valley Megamall KL is appraised at RM3.66 billion with 1.84 million sf of net lettable space, The Gardens at RM1.30 billion with 0.84 million sf, Sunway Pyramid at RM3.83 billion with 1.63 million sf, and Pavilion KL at RM4.85 billion with 1.35 million sf). Assuming that IGBB were to raise its stakes in IGB REIT to 70% (from current 53.2%), IGB REIT would issue new shares of 16.8% x 3,543m = 595 million new shares to IGBB, valued at RM982 million at issued share price of RM1.65. IGB REIT would need to raise new debts of RM1,778m for the balance considerations. IGB REIT's debt/asset ratio was at a comfortable 23% as of 31 Dec 2021 and would go up to (RM1,215+1,778)/(RM5,233+2,760) = 37.4% after completion of the injection.

IGBB on the other hand would receive a cool 70% x RM1.778 billion = RM1,245 million of cash from the deal, which would be handy to pare down its borrowings further. Its debts would drop from RM4,123m as of 31 Mar 2022 by RM830m (proceeds from IGB CR listing) and RM550m (proceeds from UK land disposal) to RM2,743m, and could drop by RM871m (70% of cash proceeds from injection of Mid Valley Southkey into IGB REIT) to RM1,872 million after the deal.

Assuming that IGBB would use 70% of the cash proceeds or RM871m to pare down borrowings, it would still have balance cash proceeds of RM373 million or 41.3 sen per share for possible special dividends to shareholders.

(2) Listing of Hotels in a new Hospitality REIT

IGBB owns a handful of unlisted hotels which may generate EBIT of RM50 million a year. At 5% dividend yield, these hotel assets may be worth RM1.0 billion if injected into a new hospitality REIT, call it IGB Hospitality REIT (IGBHR).

Assuming it injected all its hotel assets into the new REIT and maintained a 51% majority control, then IGBB would raise funds of RM490 million from this IPO proceeds. Assuming again that 70% of such proceeds would be used to pare down borrowings, IGBB would still get balance cash proceeds of RM147 million or 16.2 sen per share for possible special dividends to shareholders.

(3) Improved Cash flows and Higher Dividends from IGBB

If IGBB carries out the two suggestions above to inject Mid Valley Southkey into IGB REIT and inject hotel assets into a new hospitality REIT, then the holding company would be able to save a lot on interest expenses, estimated at (RM871m + RM343m)*4.2% = RM51.0 million of interest expense savings a year. When the profitable Mid Valley Southkey and the hotels are injected into REITs, then the taxable income and hence income tax expenses at the holding company level will be largely reduced, estimated at RM50 million per year.

So IGBB operating cashflows (before capex) would increase from RM266.2m above by RM(51+50)m to RM367.2 million a year, minus off RM24.5m contribution from the hotel segment after listing up 49% into a REIT and minus RM108m direct contribution from Mid Valley Southkey but add extra contribution of RM156.1m from higher stakes of 70% in IGB REIT) from Mid Valley Southkey after injecting it into IGB REIT, so free cash flows may top RM390 million or 43.2 sen per share every year. At 7% FCF yield, IGBB cashflow valuation would improve to **RM6.17 per share**. Plus potential special dividends of 41.3 sen + 16.2 sen from Mid Valley Southkey and hotels injection into REIT, IGBB will be worth RM6.17 + RM0.58 = **RM6.75 per share**.

(4) Ongoing and Future Projects

IGBB is undergoing the following projects:

- Southpoint Properties is a 55-storey tower comprising offices and residential units. It is scheduled for completion by 3Q 2022. I understand that the offices in Southpoint Properties have been injected into IGB Commercial REIT, but the residential units are still under IGBB providing good development profits.

- St. Giles Southkey JB is a proposed 4-star hotel at Mid Valley Southkey scheduled for soft opening in mid 2022. Once it begins commercial operations and earn steady profits, it could be injected into the new hospitality REIT suggested above.

- North Tower and South Tower at Mid Valley Southkey are quality office towers under construction at Mid Valley JB. North Tower is scheduled for completion by 3Q 2022 and handover for leasing by 2022 year end. South Tower completion should follow suit in 2023. Once completed and leased out with steady incomes, these 2 office towers may be injected into IGB Commercial REIT to unlock value.

- 18@Medini, Johor will be launched in near term as a mixed development in Iskandar Malaysia, JB.

- Improved committed occupancy at office towers owned by IGB Commercial REIT for 2022:

  - Southpoint Properties – 94.2% (from 72.1% in 2021)

- Improved committed occupancy at office towers owned by IGB Commercial REIT for 2022:

  - Southpoint Properties – 94.2% (from 72.1% in 2021)
  - Menara Tan & Tan Annex – 73.7% (from 68% in 2021)
  - Gardens South Tower – 81.4% (from 80.2% in 2021)
  - Centrepoint North – 83.3% (from77.8% in 2021)
  - Centrepoint South – 84% (from 82.4% in 2021)

- Suggestions for future projects:

  - To develop a Mid Valley Megamall in Ipoh – Ipoh city has a total population of 842,000 and nearby Batu Gajah, Simpang Pulai, Chemor & Gopeng towns (within 20 minutes drive distance) have total population of over 160,000. However, the largest shopping mall in Ipoh is AEON Station 18 with gross commercial floor area of 775,000 sf with Ipoh Parade (624,694 sf) coming second. These shopping malls are packed during weekends with almost 100% tenancy. It may be time for Ipoh to have a mega mall to the size of 1.0 – 1.2 million sf to tap the large size of 1.0 million consumers who are so far deprived of a mega mall that can offer more multi-national brands, higher end restaurants with different cuisine mix and indoor attractions.

  - To develop a Mid Valley Megamall at Batu Kawan / Butterworth / Sungai Petani to tap the large population (close to 2.0 million) in Penang island, Bukit Mertajam, Butterworth, Sungai Petani & Kulim.

Summary

IGBB is so undervalued that even its stakes in IGB REIT and IGB Commercial REIT alone are worth RM4.69, more than double its current share price.

IGBB net debt as of 31 Dec 2021 was at RM2,831 million and is set to go down to RM1,451 million once the proceeds of RM830m from IGBCR listing and RM550m from the UK land disposal are used to pare down borrowings. Net debt would go down further to RM580m with proceeds from injection of Mid Valley Southkey into IGB REIT, and would go down further to RM237m with proceeds from injecting all hotels into a new hospitality REIT.

Major catalysts will be injection of Mid Valley Southkey into IGB REIT, injection of hotel assets into a new REIT and injection of new completed office towers into IGBCR. Once these are done, IGBB would have a very good corporate structure that minimizes income tax, minimizes depreciation charges and very low interest expenses. IGBB cash flows may top RM396 million a year and net profit would be not too far off once the bulk of the depreciation charges are moved to REITs. I see IGBB progressively moving up to my cashflow valuation target of RM6.75 over next 2 years.

Table below summarises the net debt position of IGBB as of 31 Mar 2022 and how it will get reduced by the various corporate exercises discussed above, as well as the projected FY2022 annual operating cashflows which may improve after the proposed corporate exercises:

	Net Cash / (Debt) (RM mn)	Annual Cash Flows (RM mn)
As of 31 Mar 2022	(2,831)	405.0
Minus net interest costs		(120.8)
Minus tax payment		(76.0)
Proceeds from IGBCR listing	830	
Proceeds from UK land disposal	550	
Interest savings from above proceeds @ 4.2%		58.0
Injection of MV Southkey into REIT	871	
Interest saving from MVS injection		36.6
Minus CF from MVS after injection into IGB REIT		(108.0)
Add CF from additional 16.8% stakes in IGB REIT after MVS injection		156.1
Injection of hotels into REIT	343	

Injection of hotels into REIT	343	
Interest saving from hotel injection		14.4
Minus 49% CF after hotel injection		(24.5)
Tax savings after injection of MVS and hotels into REITs (est.)		50.0
After corporate exercises	**(237)**	**390.8**
		(or 43.2 sen per share)
Potential special dividend after MVS injection into REIT	373 (or 41.3 sen per share)	
Potential special dividend after hotel injection into REIT	147 (or 16.2 sen per share)	