ALLIANCEDBS RESEARCH

Malaysia Property

A tale of two worlds

Industry Focus 30 June 2023

- Resilient demand for residential properties despite interest rate normalisation
- Oversupply of high-rise properties remain key concern
- Improving overall supply demand dynamics point to sustained sector recovery on a gradual basis

Stable property market. Overall property market remains resilient in 1Q23 as residential property loans grew healthily by 6.8% (vs 6.9% in 4Q22). Nevertheless, 1Q23 property prices grew at a moderated pace of 2%, marking two consecutive quarters of slower growth. The relatively measured growth has been largely expected, reflecting similar trend in Malaysia's economic growth. We believe that sustained strength in the labour market condition will continue to underpin a steadily recovering property market.

Improving residential overhang. Residential overhang has improved considerably over the past one year (-24% y-o-y, -3% q-o-q) to reach 26,872 units in 1Q23 which is the lowest in five years. More importantly, overhang for landed residential properties has dropped to 2016 levels, signifying the successful monetisation of unsold inventories over the past few years. This has clearly paved the way for better growth prospects for landed properties-centric developers going forward.

Headwinds for high-rise properties. Inclusive of SOHO and serviced apartments, high-rise overhang has hit a record high in 1Q23, accounting for a worrying 82% of the total overhang with the bulk mainly concentrated in the Klang Valley and Johor. As affordability remains a perennial issue amid a high living cost environment, future launches in cities would see larger volume of small high-rise units in a single project which could contribute to more unsold inventory. Therefore, developers have to be more cautious with the take-up of their high-rise projects.

Banking on resilient domestic demand. While the recent rise of benchmark interest rate to pre-pandemic level of 3% may affect buying interest, we are hopeful the robust employment market with record high labour participation will remain supportive of the property market. We are confident that landed properties remain the bright spot in Malaysia's property market due to a balanced supply-demand dynamics. We believe township developers such as Eco World, Sime Darby Property and IOI Properties could be the largest beneficiaries of the sustained recovery for landed properties.

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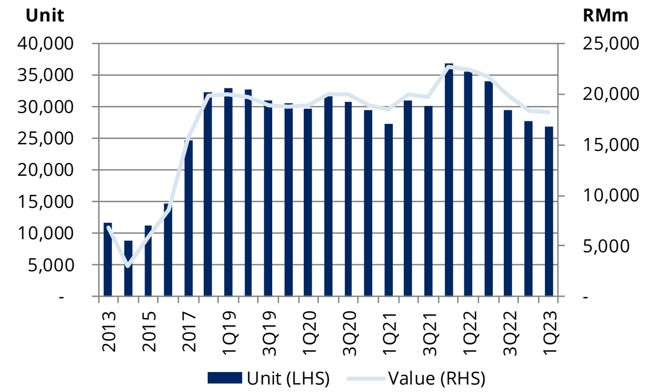
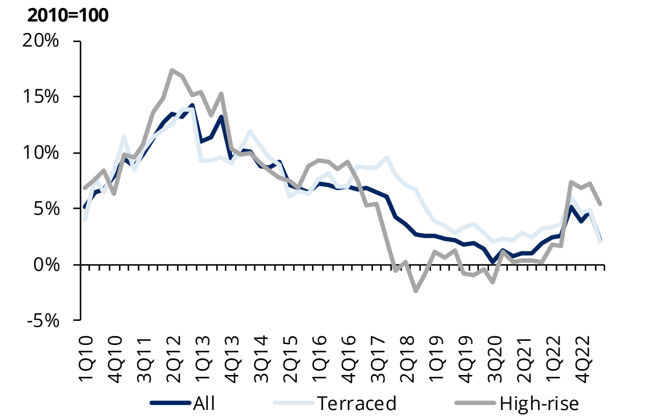
Lower unsold units of residential properties



Source: AllianceDBS, NAPIC

Stable Malaysian House Price Index (MHPI)



Source: AllianceDBS, NAPIC

Recovery momentum intact

Global inflation has been showing a disinflation trend in recent months due to the high base last year. Nevertheless, the US Federal Reserve has indicated possibility of additional two rate hikes of 25 bps for the remaining of 2023 due to the relatively high and sticky core inflation while its economy remains on a firm trajectory despite a whopping 5% interest rate increase over the past 15 months.

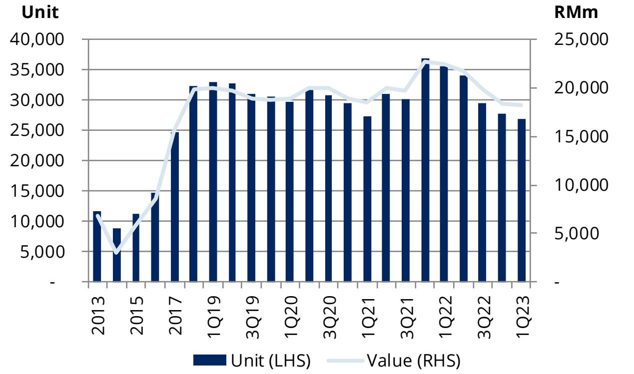
Meanwhile, China's recent manufacturing activities, retail sales and property market have lagged market expectations, though services activity remains healthy. The weaker-than-expected recovery has also resulted in declining commodity prices in recent months given the lacklustre demand for goods. The subdued economic recovery could prompt the Chinese government to undertake more policy easing to stimulate demand as inflation has been rather weak.

On the domestic front, Malaysia's property market remains resilient in 1Q23 following a robust sales performance in 2022. We are hopeful of a steady property market performance in 2023 given the resilient domestic demand which is supported by continued strength in household spending. Labour market condition has also witnessed a sustained recovery to 3.5% in Apr 2023, compared to 4.2% in Jan 2022. This has also been reflected in the steady residential property loans growth of 6.8% in 1Q23 (vs 6.9% in 4Q22).

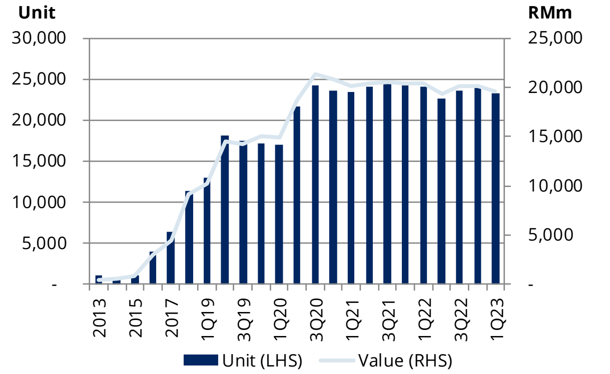
Taking a look at the perennial concern of supply glut, it continues to show sequential improvement though the property overhang remains high. As at end-1Q23, residential overhang dipped by 3% q-o-q and 24% y-o-y due to the solid demand for landed properties. It is noteworthy that residential overhang for landed properties has been declining for five quarters consecutively, reaching the level last seen in 2016. This illustrates the successful monetisation of unsold inventory that has been going on over the past few years.

On the other hand, high-rise overhang is seeing a worrying trend as unsold completed units (inclusive of SOHO and serviced apartments) hit a record high in 1Q23. This could probably be attributed to the newly completed projects after the full reopening of the economy in 2022. High-rise units account for a whopping 82% of total overhang, an unprecedented record for Malaysia's property market. As affordability remains a key issue amid a high living cost environment, future launches in cities would see larger volume of small high-rise units in a single project which could contribute to more unsold inventory.

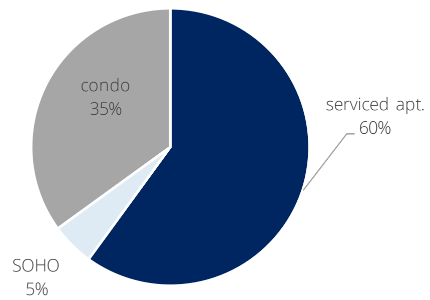
Completed but unsold residential units



Completed but unsold serviced apartments



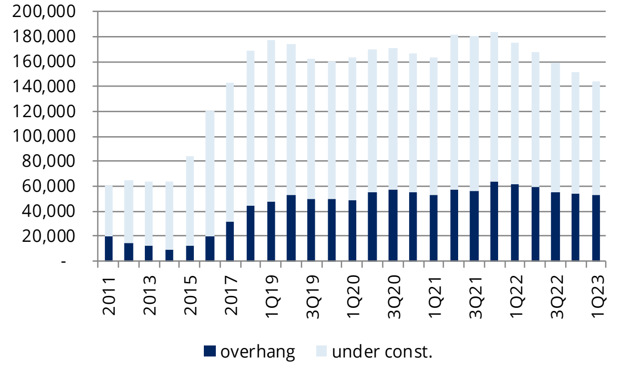
Overhang of high-rise properties



Source: AllianceDBS, NAPIC

On an aggregate basis, total unsold units (completed and under construction) are slowly reducing in the system as Malaysia's economy remains on a growth momentum. Nevertheless, improvement in the overall supply-demand dynamics will take place on a gradual basis as total supply remains relatively high by historical standards.

Total unsold units in Malaysia's property market



We believe that Malaysia's property market could mark an inflection point in 2023 after weathering a long downturn since 2015 where supply overhang and low affordability plague the market for years. While it is still premature to conclude that the Malaysia's property market is heading towards a sustained recovery, a resilient economic recovery momentum in 2023 will position the property market on a stronger footing, notwithstanding the external uncertainties.

Similar to the global monetary tightening, Bank Negara Malaysia (BNM) has raised the benchmark interest rate by five times with 25 bps hike each since May 2022, bringing the Overnight Policy Rate (OPR) to 3.0% which is similar to pre-pandemic level. We believe that BNM will stand pat on the OPR for the remaining of 2023 amid normalising inflation and steady growth trajectory in our economy.

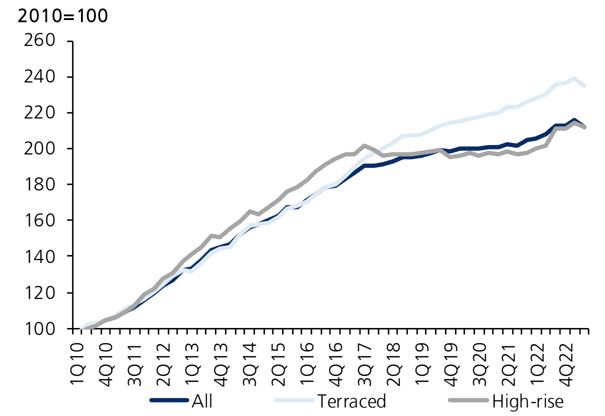
In the near term, property developers may be more cautious with their launches given the rising building material prices and concerns on lower purchasing power from potential buyers after the latest rate hike and high living cost. Meanwhile, critical labour shortage issue has largely been resolved, enabling smooth construction progress for most property developments.

At the same time, potential property buyers may prioritize non-discretionary expenses instead of properties due to the high inflation environment which has weakened their purchasing power. The impending elections for six states may also result in wait-and-see attitude for the property market given the potential change in state governments.

Property prices grew at a more measured pace of 2% in 1Q23 after achieving 5.1% in 3Q22 and 3.9% in 4Q22. This deceleration does not come as a surprise as 2023 has been expected to see a normalisation after the stellar performance 2022 due to the economy reopening. Nevertheless, price growth is likely to remain on a healthy trend given the improvement in supply overhang, sustained growth trend in the overall economy and cost-push inflation for building materials.

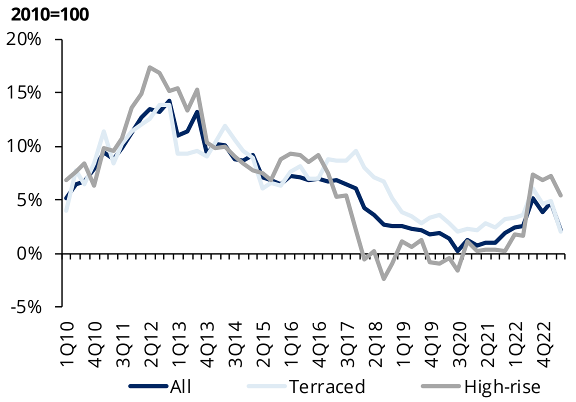
Therefore, we believe the worst is over for Malaysia's property market after weathering a subdued property market over the past few years. More importantly, Malaysia's employment market has been growing steadily, and has far exceeded the pre-pandemic employment level, thanks to the growing economy. It is even more encouraging that labour participation has hit a record high of 70% in Apr 2023 which could partly explain the steady and resilient domestic demand. This positive development is expected to continue given our favourable demography which will further underpin the resilience of Malaysia's domestic demand.

Malaysian House Price Index (MHPI)



Source: AllianceDBS, NAPIC

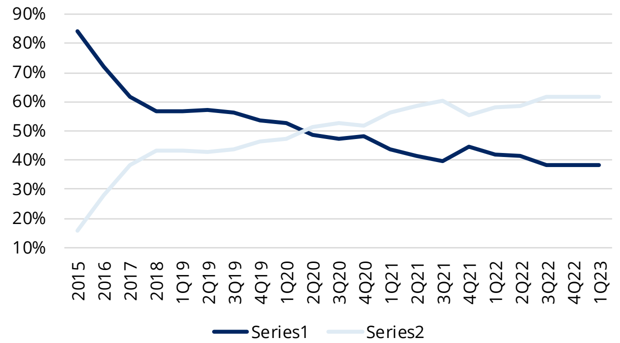
Malaysian House Price Index growth trend



Source: AllianceDBS, NAPIC

We believe that the landed property segment will continue to outperform given its more balanced supply-demand dynamics, though the overhang in the serviced apartments segment is a cause for concern. Overall, the rental market has not shown much improvement over the past 12 months as the nationwide lockdown has dampened demand to a great extent. Nevertheless, we believe this may improve gradually as Malaysia's economy continues to maintain its recovery momentum, underpinned by robust labour market and strong economic and social activities, especially the tourism-related activities.

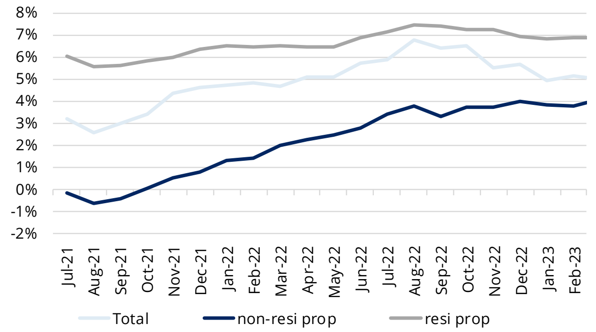
Composition of residential overhang



Source: AllianceDBS, NAPIC

We note that the composition of landed properties in the supply overhang has been declining over the years, as demand remains resilient and Malaysians typically favour landed housing. Expensive land prices have also limited the supply of landed properties which made supply less speculative in nature, compared to high-rise housing. Therefore, we are confident that landed properties are now on a sustained recovery going forward given the more balanced supply-demand dynamics.

Resilient residential loans growth



Source: AllianceDBS, BNM, CEIC

Commonly used abbreviations

Adex = advertising expenditure
bn = billion
BV = book value
CF = cash flow
CAGR = compounded annual growth rate
Capex = capital expenditure
CY = calendar year
Div yld = dividend yield
DCF = discounted cash flow
DDM = dividend discount model
DPS = dividend per share
EBIT = earnings before interest & tax
EBITDA = EBIT before depreciation and amortisation
EPS = earnings per share
EV = enterprise value
FCF = free cash flow
FV = fair value
FY = financial year
m = million
M-o-m = month-on-month
NAV = net assets value
NM = not meaningful
NTA = net tangible assets
NR = not rated
p.a. = per annum
PAT = profit after tax
PBT = profit before tax
P/B = price / book ratio
P/E = price / earnings ratio
PEG = P/E ratio to growth ratio
q-o-q = quarter-on-quarter
RM = Ringgit
ROA = return on assets
ROE = return on equity
TP = target price
trn = trillion
WACC = weighted average cost of capital
y-o-y = year-on-year
YTD = year-to-date

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