

MRCB-Quill REIT (QUIL MK)

Property - REITS

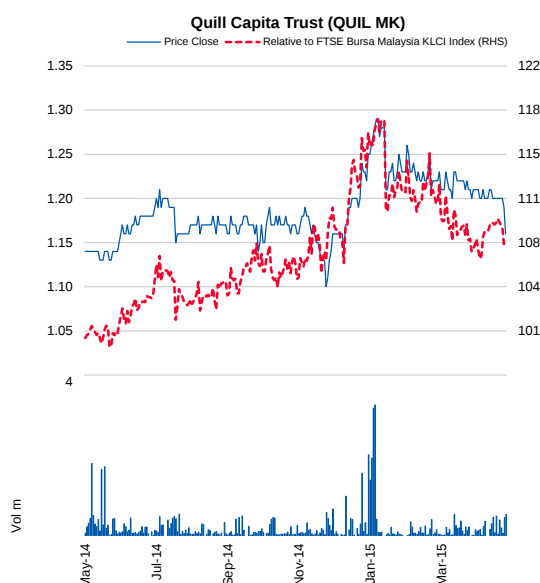
Market Cap: USD214m

Neutral (Maintained)

Target Price: MYR1.25

Price: MYR1.16

Short-Term Outlook Remains Challenging

Macro
Risks
Growth
Value


Source: Bloomberg

Avg Turnover (MYR/USD)	0.18m/0.05m
Cons. Upside (%)	8.6
Upside (%)	7.9
52-wk Price low/high (MYR)	1.10 - 1.29
Free float (%)	40
Share outstanding (m)	661
Shareholders (%)	
CapitaCommercial Trust	30.0
Quill Group	30.0

Share Performance (%)

	YTD	1m	3m	6m	12m
Absolute	(0.9)	(4.1)	(5.7)	0.0	1.8
Relative	(4.4)	(2.9)	(6.6)	0.1	5.2

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1Q15 earnings came broadly in line with our/street estimates. Maintain NEUTRAL and DDM-derived MYR1.25 TP (8% upside). As we expect the soft office market conditions to persist over the short term, we believe that all positives have been priced in for now. We note that earnings should be boosted from 2Q15 onwards as contribution from Platinum Sentral starts kicking in.

- ◆ **Within expectations.** MRCB-Quill REIT's (MQREIT) (formerly Quill Capita Trust) 1Q15 core net profit of MYR8.28m (-2.7% QoQ, +1.4% YoY) was broadly in line with our/street estimates. Revenue and earnings for the quarter were mainly underpinned by the kick-in of positive rental reversions from its assets. Out of the 26% leases due for renewal in FY15, 6% had been renewed as of end-1Q. Gearing level is currently at 44% (from 35% in 4Q14), arising from the acquisition of Platinum Sentral during the quarter. A 1.88 sen dividend was also proposed for the quarter. However, this will be paid out together with its 2Q15 dividend, given its semi-annual distribution policy.
- ◆ **Recent developments.** The REIT finally completed the acquisition of Platinum Sentral on 30 Mar. We expect the asset, which was acquired from Malaysian Resources Corp (MRCB) (MRC MK, NEUTRAL, TP: MYR1.31), to start contributing positively to the topline from 2Q onwards. On another note, management has reiterated that going forward, it will focus on exploring yield-accretive acquisition opportunities as well as continuously improving its existing assets. We believe that the proposed disposal of the non-performing Quill Building 10, which is due to be completed by end-1H15, will help to boost the REIT's war chest for future acquisitions (see our 26 Feb report [Quill Capita Trust : Finally Disposing Of Quill Building 10](#)).
- ◆ **Forecasts.** Maintained for now.
- ◆ **Still NEUTRAL.** We remain cautious on MQREIT's short-term outlook due to the persistently soft office market coupled with the REIT's higher post-acquisition gearing. That said, dividend yield remains attractive at 7.6% FY16F. Therefore, we maintain our NEUTRAL call and DDM-derived MYR1.25 TP.

Forecasts and Valuations	Dec-13	Dec-14	Dec-15F	Dec-16F	Dec-17F
Total turnover (MYRm)	69	70	107	122	124
Net property income (MYRm)	53.2	53.3	83.8	94.8	96.3
Reported net profit (MYRm)	34.5	34.1	55.9	60.4	61.7
Total distributable income (MYRm)	34.5	34.1	55.9	60.4	61.7
DPS (MYR)	0.08	0.08	0.09	0.09	0.09
DPS growth (%)	0.0	0.0	5.2	(0.3)	2.2
Recurring P/E (x)	13.1	13.3	10.4	12.2	12.4
P/B (x)	0.85	0.84	0.78	0.84	0.84
Dividend Yield (%)	7.2	7.2	7.6	7.6	7.7
Return on average equity (%)	6.5	6.3	7.7	6.6	6.8
Return on average assets (%)	4.0	3.9	4.5	3.7	3.8
Interest coverage ratio (x)	3.47	3.38	3.45	3.09	3.13
Our vs consensus EPS (adjusted) (%)			14.1	(13.4)	0.0

Source: Company data, RHB

Figure 1: MQREIT's earnings review

FYE Dec (MYRm)	1QFY14	4QFY14	1QFY15	QoQ (%)	YoY (%)	Comments
Revenue	17.2	18.2	18.6	2.3	8.3	Higher revenue YoY mainly due to rental rate increases, higher revenue from Plaza Mont Kiara, higher recoveries of some properties and additional revenue arising from the acquisition of Platinum Sentral during the quarter.
Net property income (NPI)	13.0	13.4	13.7	2.0	5.1	
Interest expense	(3.4)	(3.5)	(3.5)	2.5	3.1	Higher interest due to the additional borrowings drawdown as a result of the acquisition of Platinum Sentral during the quarter.
Interest income	0.1	0.1	0.1	28.3	10.9	
Associates	0.0	0.0	0.0	nm	nm	
EI	0.0	6.1	0.0	nm	nm	
Others	(1.5)	(1.6)	(2.0)	28.0	29.7	Higher administrative expenses, manager's and trustee's fees.
Pretax profit	8.2	14.6	8.3	(43.4)	1.4	
Tax	0.0	0.0	0.0	nm	nm	
Minority Interest	0.0	0.0	0.0	nm	nm	
Net Profit	8.2	14.6	8.3	(43.4)	1.4	
Core Profit	8.2	8.5	8.3	(2.7)	1.4	Broadly in line with expectations.
Core earnings per unit (sen)	2.09	2.18	2.09	nm	(0.1)	
Dividends per unit (sen)	0.00	4.28	0.00	nm	nm	
NPI Margin (%)	75.7	73.8	73.5			
Pretax Margin (%)	47.5	80.4	44.5			
Net Margin (%)	47.5	46.8	44.5			

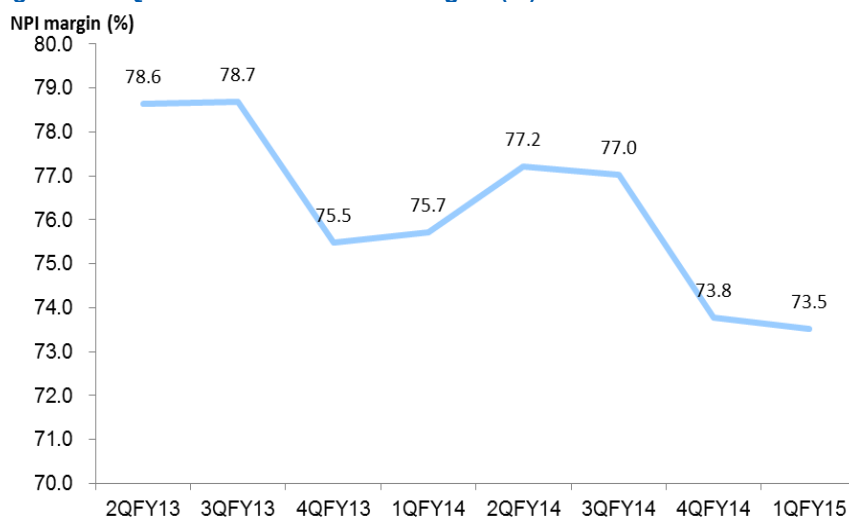
Source: RHB

Figure 2: MQREIT's historical eight quarters' earnings

FYE Dec (MYRm)	2QFY13	3QFY13	4QFY13	1QFY14	2QFY14	3QFY14	4QFY14	1QFY15
Revenue	17.3	17.1	17.3	17.2	17.3	17.5	18.2	18.6
Net property income (NPI)	13.6	13.5	13.1	13.0	13.4	13.5	13.4	13.7
Interest expense	(3.4)	(3.5)	(3.3)	(3.4)	(3.6)	(3.6)	(3.5)	(3.5)
Interest income	0.2	0.2	0.1	0.1	0.3	0.2	0.1	0.1
Associates	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
EI	0.0	0.0	2.1	0.0	0.0	0.0	6.1	0.0
Others	(1.5)	(1.2)	(1.3)	(1.5)	(1.6)	(1.2)	(1.6)	0.0
Pretax profit	8.9	8.9	10.7	8.2	8.6	8.9	14.6	8.3
Tax	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Minority Interest	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Net Profit	8.9	8.9	10.7	8.2	8.6	8.9	14.6	8.3
Core Profit	8.9	8.9	8.6	8.2	8.6	8.9	8.5	8.3
Core earnings per unit (sen)	2.28	2.29	2.20	2.09	2.19	2.29	2.18	2.09
Dividends per unit (sen)	4.10	0.00	4.28	0.00	4.10	0.00	4.28	0.00
NPI Margin (%)	78.6	78.7	75.5	75.7	77.2	77.0	73.8	73.5
Pretax Margin (%)	51.6	52.1	61.9	47.5	49.4	51.0	80.4	44.5
Net Margin (%)	51.6	52.1	49.7	47.5	49.4	51.0	46.8	44.5

Source: RHB

Figure 3: MQREITT's historical NPI margins (%)



Source: Company data

Figure 4: MQREIT's forecast assumptions

<u>Asset</u>	<u>NLA / GFA</u>	<u>Average Rental Rates (MYR psf)</u>		
	<u>(sf)</u>	<u>FY15</u>	<u>FY16</u>	<u>FY17</u>
QB 1 - DHL 1	92,284	4.08	4.16	4.24
QB 4 - DHL 2	99,183	4.08	4.16	4.24
QB 2 - HSBC	184,453	4.08	4.16	4.24
QB 3 - BMW	117,198	4.08	4.16	4.24
QB 5 - IBM	81,602	3.03	3.06	3.09
Plaza MK	73,408	8.51	8.52	8.53
Wisma Technip	233,021	5.31	5.46	5.63
QB 8 - DHL	65,205	3.03	3.06	3.09
Tesco Penang	275,020	2.92	2.97	3.03
Platinum Sentral	475,857	8.77	8.91	9.04
DPU (sen)		9.01	8.73	8.92

Source: RHB, Company data

Financial Exhibits

Profit & Loss (MYRm)	Dec-13	Dec-14	Dec-15F	Dec-16F	Dec-17F
Total turnover	69	70	107	122	124
Property operating expenses	(16)	(17)	(24)	(27)	(27)
Net property income	53	53	84	95	96
Management fees	(5)	(5)	(6)	(6)	(6)
Trust expenses	(0)	(0)	(1)	(1)	(1)
Operating EBIT	47	47	78	88	90
Operating EBITDA	47	47	78	88	90
Interest income	1	1	1	1	1
Interest expense	(14)	(14)	(22)	(29)	(29)
Pre-tax profit	35	34	56	60	62
Profit after tax & minorities	35	34	56	60	62
Reported net profit	35	34	56	60	62
Total distributable income	35	34	56	60	62

Source: Company data, RHB

Cash flow (MYRm)	Dec-13	Dec-14	Dec-15F	Dec-16F	Dec-17F
Operating profit	47	47	78	88	90
Change in working capital	(8)	(3)	(3)	(3)	(4)
Other operating cash flow	3	0	2	2	2
Operating cash flow	42	44	76	87	88
Interest received	1	1	1	1	1
Interest paid	(14)	(14)	(22)	(29)	(29)
Cash flow from operations	29	31	55	59	60
Capex	(2)	(6)	(2)	(2)	(2)
Cash flow from investing activities	(2)	(6)	(2)	(2)	(2)
Dividends paid	(33)	(33)	(43)	(56)	(59)
Proceeds from issue of shares	-	0	-	-	-
Increase in debt	116	0	-	-	-
Other financing cash flow	-	0	-	-	-
Cash flow from financing activities	84	(32)	(43)	(56)	(59)
Cash at beginning of period	30	31	23	60	34
Total cash generated	111	(7)	9	1	(1)
Implied cash at end of period	141	24	33	61	33

Source: Company data, RHB

Financial Exhibits

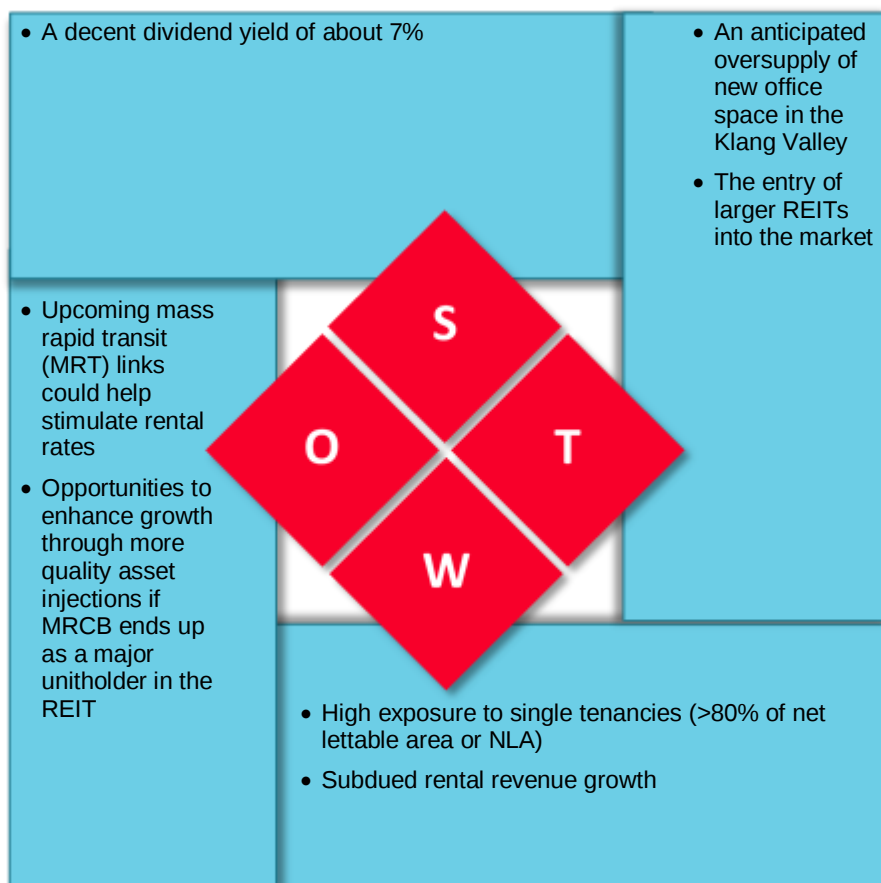
Balance Sheet (MYRm)	Dec-13	Dec-14	Dec-15F	Dec-16F	Dec-17F
Total cash and equivalents	31	23	60	34	33
Accounts receivable	3	6	6	6	6
Other current assets	-	-	-	29	32
Total current assets	34	29	66	69	71
Total investments	827	839	1,562	1,562	1,562
Total other assets	0	0	0	0	0
Total non-current assets	827	839	1,562	1,562	1,562
Total assets	860	868	1,629	1,631	1,634
Accounts payable	12	12	12	12	12
Other current liabilities	5	2	2	2	2
Total current liabilities	17	15	15	15	15
Total long-term debt	305	305	698	698	698
Other liabilities	5	8	8	8	8
Total non-current liabilities	310	313	705	705	706
Total liabilities	327	327	720	720	720
Share capital	412	412	676	676	676
Retained earnings reserve	122	130	233	235	238
Shareholders' equity	533	541	909	911	914
Total equity	533	541	909	911	914
Total liabilities & equity	860	868	1,629	1,631	1,634

Source: Company data, RHB

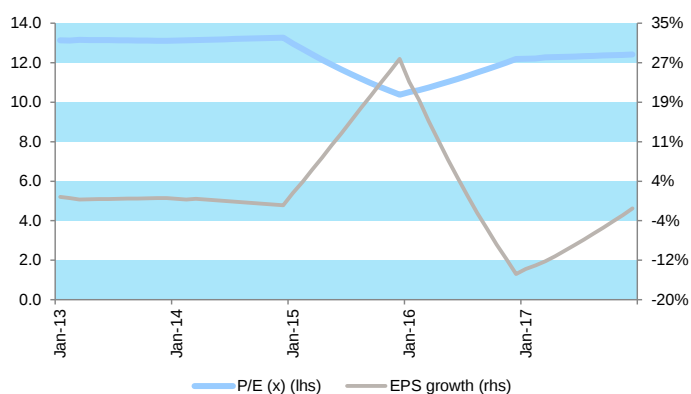
Key Ratios (MYR)	Dec-13	Dec-14	Dec-15F	Dec-16F	Dec-17F
Revenue growth (%)	(0.8)	1.9	53.0	13.1	1.6
Net profit growth (%)	0.2	(1.2)	63.7	8.1	2.2
EPS growth (%)	0.2	(1.2)	27.9	(14.9)	(1.8)
BVPS growth (%)	0.9	1.5	7.6	(7.6)	0.3
Net profit margin (%)	50.1	48.6	52.0	49.7	50.0
Return on average assets (%)	4.0	3.9	4.5	3.7	3.8
Return on average equity (%)	6.5	6.3	7.7	6.6	6.8
Net debt to equity (%)	51.4	52.1	70.2	72.9	72.7
DPS	0.08	0.08	0.09	0.09	0.09
Recurrent cash flow per share	0.07	0.08	0.11	0.09	0.09

Source: Company data, RHB

SWOT Analysis

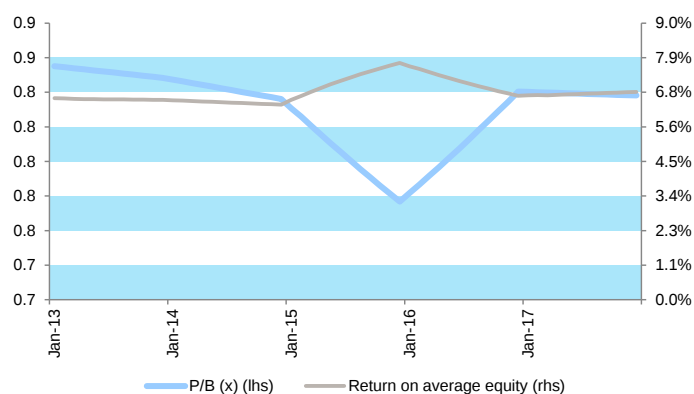


P/E (x) vs EPS growth



Source: Company data, RHB

P/BV (x) vs ROAE



Source: Company data, RHB

Company Profile

MRCB-Quill REIT is a mid-cap MREIT that focuses on office/commercial assets. Assets are largely concentrated in the Klang Valley and Cyberjaya areas.

Recommendation Chart



Source: RHB, Bloomberg

Date	Recommendation	Target Price	Price
2015-02-26	Neutral	1.25	1.23
2015-01-20	Neutral	1.25	1.25
2014-11-27	Neutral	1.25	1.18
2014-05-02	Neutral	1.25	1.13
2014-01-30	Neutral	1.25	1.20
2014-01-29	Sell	1.06	1.20
2013-08-02	Sell	1.10	1.22
2013-05-13	Neutral	1.27	1.21
2013-03-06	Neutral	1.27	1.14
2013-02-04	Neutral	1.27	1.20

Source : RHB, Bloomberg

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Trading Buy: Share price may exceed 15% over the next 3 months, however longer-term outlook remains uncertain

Neutral: Share price may fall within the range of +/- 10% over the next 12 months

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