

27 October 2016

Property | REITS

MRCB-Quill REIT

Boosted By Platinum Sentral

We believe MRCB-Quill REIT to sustain its growth in 2H16, bolstered by long-term leases at the majority of its assets. It has benefitted from the injection of Platinum Sentral in March 2015, and the upcoming injection of Menara Shell would provide another source of long-term growth to the portfolio. We maintain our DDM-based TP of MYR1.32 (4% upside), but downgrade to NEUTRAL (from Buy) as the share price has had a good run, appreciating by 18% YTD. Hence, at the current price, we believe the stock is fairly valued.

Consistently high occupancy rate. We anticipate the REIT's overall occupancy rate, now 97.2%, to remain stable moving forward, as most of the tenants are on long-term leases. 43% of its tenants' lease renewals are coming within 2020 and 2032, while another 37% in 2018-2019. This should provide stability to weather the upcoming supply of office space in the Klang Valley.

Menara Shell acquisition to be completed by end-2016. We expect the injection of Menara Shell to provide a jump in growth of the portfolio size and its revenue and earnings from 2017 onwards. The REIT is acquiring the asset for MYR640m, increasing total portfolio value by 41% to MYR2.27bn.

Downgrade to NEUTRAL, keeping our FY16F-18F earnings and DDM-based TP of MYR1.32. We reduce our call from Buy, as the stock price has had a good run this year, appreciating 18% YTD, and we believe the stock is currently fairly valued. Key risks to our call include prolonged weak domestic consumer sentiment.

3Q16 earnings: in line

(MYRm)	3Q16	2Q16	QoQ (%)	3Q15	YoY (%)	Comments
Revenue	32.5	32.6	-0.2	31.8	2.2	Rental reversions
NPI	25.5	25.7	-0.7	25.5	0.2	
NPI (%)	78.6%	78.9%		80.1%		
Pretax income	15.2	14.7	3.9	15.7	-3.2	
Pretax margin (%)	46.9%	45.0%		49.5%		
NP – reported	15.2	14.7	3.9	15.7	-3.2	
NM – reported (%)	46.9%	45.0%		49.5%		
NP – recurring	15.2	15.4	-1.0	15.7	-3.2	
NM – recurring (%)	46.9%	47.2%		49.5%		

Source: Company data, RHB

9M16 results within expectations. 9M16 core net profit of MYR45.9m (21.8% YoY) was in line with expectations at 76% and 78% of our and street estimates respectively. 9M16 revenue and earnings growth were attributed mainly to the full contribution from Platinum Sentral, acquisition of which was completed on 30 Mar 2015.

Forecasts and Valuations	Dec-14	Dec-15	Dec-16F	Dec-17F	Dec-18F
Total turnover (MYRm)	70	110	124	174	178
Net property income (MYRm)	53	87	94	132	137
Reported net profit (MYRm)	34.1	53.9	60.5	86.4	91.5
Total distributable income (MYRm)	34.1	53.9	60.5	86.4	91.5
DPS (MYR)	0.08	0.08	0.09	0.08	0.08
DPS growth (%)	0.0	(1.3)	4.1	(9.3)	4.2
Recurring P/E (x)	14.5	14.0	13.9	15.7	14.8
P/B (x)	0.92	0.92	1.01	1.01	1.01
Dividend Yield (%)	6.6	6.5	6.8	6.1	6.4
Return on average equity (%)	6.3	7.4	5.4	6.4	6.8
Return on average assets (%)	3.9	4.3	3.1	3.8	4.0
Interest cover (x)	3.38	2.95	3.20	3.19	3.32
Our vs consensus EPS (adjusted) (%)			(1.6)	(15.7)	(10.8)

Source: Company data, RHB

Neutral (from Buy)

Target Price: MYR1.32

Price: MYR1.27

Market Cap: USD202m

Bloomberg Ticker: MQREIT MK

Share Data

Avg Daily Turnover (MYR/USD)	0.44m/0.11m
52-wk Price low/high (MYR)	1.05 - 1.36
Free Float (%)	40
Shares outstanding (m)	390
Estimated Return	4%

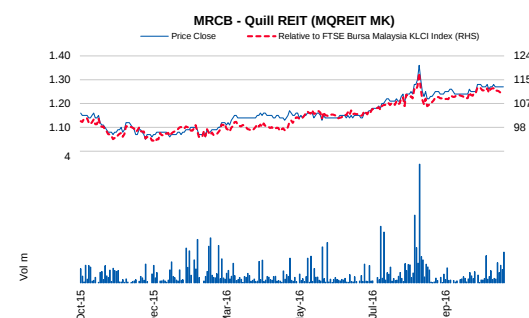
Shareholders (%)

CapitaCommercial Trust	30.0
Quill Group	30.0

Share Performance (%)

	YTD	1m	3m	6m	12m
Absolute	17.6	2.4	4.1	9.5	10.4
Relative	18.5	1.9	3.1	10.4	12.1

Source: Bloomberg



Source: Bloomberg

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Financial Exhibits

Financial model updated on : 2016-10-26.

Asia
Malaysia
Property
MRCB-Quill REIT
Bloomberg MREIT MK
Neutral
Valuation basis
Dividend discount model, with CoE of 7.95% and TG of 1.8%.
Key drivers
Improvement in domestic consumer sentiment leading to strong consumer spending.
Key risks
Downside risks include prolonged weak domestic consumer sentiment, while upside risks include stronger demand for its assets – leading to higher occupancy rates and rental reversion rates at its assets.
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.

Financial summary	Dec-14	Dec-15	Dec-16F	Dec-17F	Dec-18F
Recurring EPS (MYR)	0.09	0.09	0.09	0.08	0.09
EPS (MYR)	0.09	0.09	0.09	0.08	0.09
DPS (MYR)	0.08	0.08	0.09	0.08	0.08
BVPS (MYR)	1.39	1.38	1.26	1.26	1.26
Weighted avg adjusted shares (m)	390	594	661	1,068	1,068

Valuation metrics	Dec-14	Dec-15	Dec-16F	Dec-17F	Dec-18F
Recurring P/E (x)	14.5	14.0	13.9	15.7	14.8
P/E (x)	14.5	14.0	13.9	15.7	14.8
P/B (x)	0.92	0.92	1.01	1.01	1.01
FCF Yield (%)	5.1	6.7	(43.8)	6.1	6.5
Dividend Yield (%)	6.6	6.5	6.8	6.1	6.4
EV/EBITDA (x)	(1.30)	(0.78)	(1.08)	(1.32)	(1.28)
EV/EBIT (x)	(1.30)	(0.78)	(1.08)	(1.32)	(1.28)

Income statement	Dec-14	Dec-15	Dec-16F	Dec-17F	Dec-18F
Total turnover (MYRm)	70.2	109.6	123.9	174.3	177.8
EBITDA (MYRm)	47.4	80.4	87.0	124.8	129.9
Operating profit (MYRm)	47.4	80.4	87.0	124.8	129.9
Net interest (MYRm)	(13.3)	(26.5)	(26.5)	(38.4)	(38.4)
Pre-tax profit (MYRm)	34.1	53.9	60.5	86.4	91.5
Recurring net profit (MYRm)	34.1	53.9	60.5	86.4	91.5

Cash flow (MYRm)	Dec-14	Dec-15	Dec-16F	Dec-17F	Dec-18F
Change in working capital	(3.1)	(3.3)	(3.5)	(3.6)	(3.8)
Cash flow from operations	31.1	52.6	59.1	84.8	89.6
Capex	(6.0)	(2.0)	(427.0)	(2.0)	(2.0)
Cash flow from investing activities	(6.0)	(2.0)	(427.0)	(2.0)	(2.0)
Proceeds from issue of shares	0.2	365.3	0.0	0.0	0.0
Dividends paid	(32.7)	(40.9)	(53.0)	(70.2)	(85.1)
Cash flow from financing activities	(32.2)	722.4	176.0	(70.2)	(85.1)
Cash at beginning of period	30.9	23.3	60.3	247.7	260.4
Net change in cash	(7.1)	773.0	(191.9)	12.6	2.5
Ending balance cash	23.8	796.3	(131.6)	260.4	262.9

Balance sheet (MYRm)	Dec-14	Dec-15	Dec-16F	Dec-17F	Dec-18F
Total cash and equivalents	23	60	248	260	263
Total investments	839	1,552	2,192	2,192	2,192
Total other assets	0	0	0	0	0
Total assets	868	1,637	2,296	2,300	2,304
Total long-term debt	305	703	932	932	932
Other liabilities	8	8	8	8	8
Total liabilities	327	725	954	955	955
Shareholders' equity	541	911	1,342	1,345	1,350
Total equity	541	911	1,342	1,345	1,350
Net debt	282	643	684	672	669
Total liabilities & equity	868	1,637	2,296	2,300	2,304

Key metrics	Dec-14	Dec-15	Dec-16F	Dec-17F	Dec-18F
Revenue growth (%)	1.9	56.0	13.1	40.7	2.0
Recurrent EPS growth (%)	(1.2)	3.8	0.8	(11.6)	5.8
Operating EBITDA margin (%)	67.5	73.4	70.2	71.6	73.1
Net profit margin (%)	48.6	49.2	48.9	49.6	51.4
Dividend payout ratio (%)	95.8	91.0	91.0	91.0	91.0
Capex/sales (%)	8.6	1.8	344.6	1.1	1.1
Interest cover (x)	3.38	2.95	3.20	3.19	3.32

Source: Company data, RHB

Figure 1: MRCB-Quill REIT's 9M16 earnings summary

FYE Dec (MYRm)	3Q15	2Q16	3Q16	QoQ (%)	YoY (%)	9M15	9M16	YoY (%)	Comments
Revenue	31.8	32.6	32.5	(0.2)	2.2	82.6	97.7	18.3	Higher YoY revenue growth due to the additional contribution coming from Platinum Sentral, Plaza Mont Kiara and rental rate increases for some other properties.
Net property income (NPI)	25.5	25.7	25.5	(0.7)	0.2	63.5	76.7	20.8	The REIT incurred higher property operating expenses due to additional repair and maintenance costs and acquisition of Platinum Sentral.
Interest expense	(8.3)	(8.0)	(8.1)	1.6	(2.6)	(20.0)	(23.9)	19.4	Higher interest expense due to interest on additional borrowings on Platinum Sentral.
Interest income	0.4	0.4	0.5	25.2	35.2	0.6	1.2	100.6	
Associates	0.0	0.0	0.0	nm	nm	0.0	0.0	nm	
EI	0.0	0.0	0.0	nm	nm	0.0	0.0	nm	
Others	(2.4)	(2.7)	(2.7)	(1.6)	12.3	(7.0)	(8.1)	16.1	
Pretax profit	15.7	14.7	15.2	3.9	(3.2)	37.6	45.9	21.8	
Tax	0.0	0.0	0.0	nm	nm	0.0	0.0	nm	
Minority Interest	0.0	0.0	0.0	nm	nm	0.0	0.0	nm	
Net Profit	15.7	14.7	15.2	3.9	(3.2)	37.6	45.9	21.8	
Core Profit	15.7	15.4	15.2	(1.0)	(3.2)	37.6	45.9	21.8	Within expectations
Core earnings per unit (sen)	2.38	2.33	2.30	(1.3)	(3.4)	7.63	6.93	(9.2)	
Dividends per unit (sen)	0.00	4.23	0.00	nm	nm	4.10	4.23	3.2	
NPI Margin (%)	80.1	78.9	78.6			76.8	78.5		
Pretax Margin (%)	49.5	45.0	46.9			45.6	46.9		
Net Margin (%)	49.5	47.2	46.9			45.6	46.9		

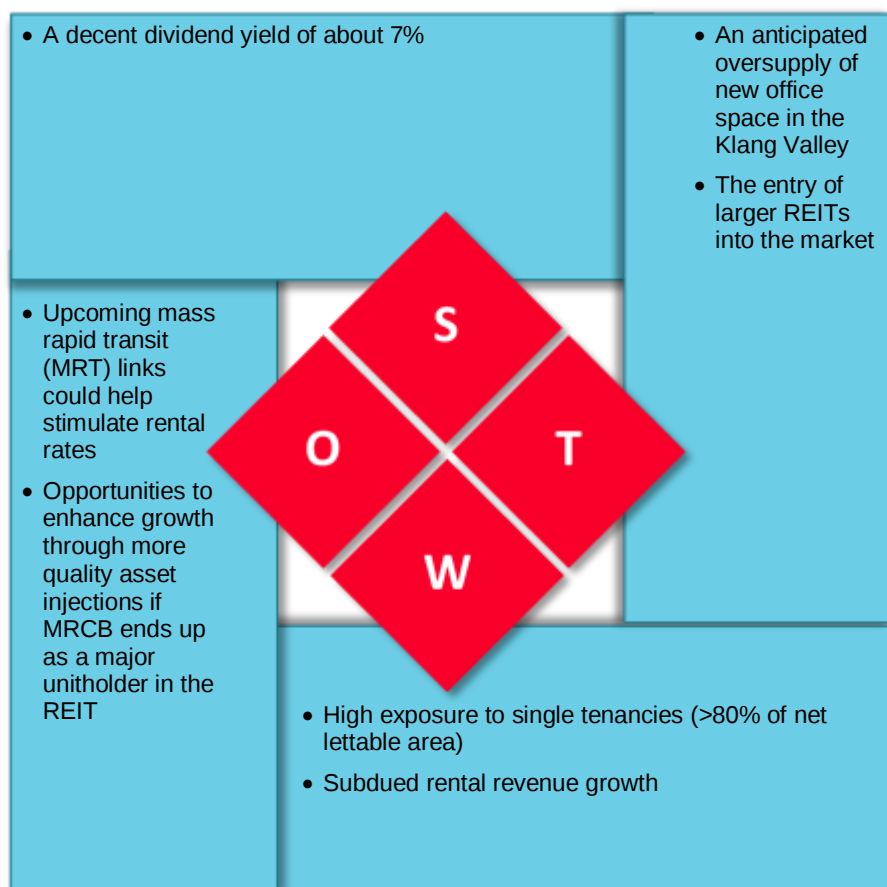
Source: RHB, Company data

Figure 1: Forecast assumptions

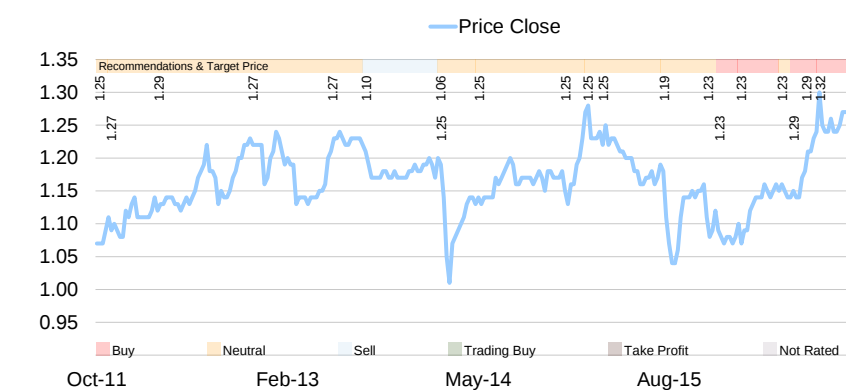
Asset	NLA / GFA (sf)	Average Rental Rates (MYR psf)		
		FY16	FY17	FY18
QB 1- DHL 1	92,284	4.37	4.45	4.53
QB 4 - DHL 2	99,183	4.37	4.45	4.53
QB 2 - HSBC	184,453	4.37	4.45	4.53
QB 3 - BMW	117,198	4.37	4.45	4.53
QB 5 - IBM	81,602	3.21	3.33	3.45
Plaza MK	73,408	8.52	8.53	8.54
Wisma Technip	233,021	5.68	5.85	6.02
QB 10 - HSBC	68,377	3.21	3.33	3.45
QB 8 - DHL	65,205	3.21	3.33	3.45
Tesco Penang	275,020	3.03	3.09	3.15
Platinum Sentral	475,857	8.91	9.04	9.17
Shell Tower	557,053	7.04	7.21	7.38
DPU (sen)		8.61	7.81	8.00

Source: RHB, Company data

SWOT Analysis



Recommendation Chart



Date	Recommendation	Target Price	Price
2016-08-03	Buy	1.32	1.24
2016-07-01	Buy	1.29	1.17
2016-05-31	Buy	1.29	1.14
2016-05-03	Neutral	1.23	1.14
2016-01-25	Buy	1.23	1.08
2015-12-04	Buy	1.23	1.12
2015-11-06	Neutral	1.23	1.16
2015-07-23	Neutral	1.19	1.19
2015-02-26	Neutral	1.25	1.23
2015-01-20	Neutral	1.25	1.25

Source: RHB, Bloomberg

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