

08 August 2019

MRCB-Quill REIT

1H19 Slightly Below

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1H19 realised net income (RNI) of RM35.9m came in below our and consensus expectations at 42.6% and 43.3%, respectively, on lower-than-expected margins caused by a weakening top-line. 1H19 dividend of 3.43 sen is also slightly below at 44.5%. FY19-20 will see 19-18% of NLA expiring on flattish reversions. We lower FY19-20E CNP by 10-9%. Downgrade to MP (from OP) on a lower TP of RM1.05 (from RM1.15).

1H19 realised net income (RNI) of RM35.9m came in slightly below our and consensus expectations at 42.6% and 43.3%, respectively. The reason for the deviation in our and consensus estimates was mostly due to weak margins as top-line only came in at 46% of both estimates on ongoing weakness possibly due to tenant movement at Platinum Sentral, QB5 and Wisma Technip, which resulted in RNI margin compressions to 44.7% (vs. our FY19E of 48.4%). 1H19 GDPU of 3.43 sen per unit (which includes a non-taxable portion of 0.12 sen) was also slightly below at 44.5% of our FY19E GDPU of 7.7 sen (7.2% gross yield).

Results' highlights. YoY-Ytd, top-line was down by 8% mainly from lower contributions at Platinum Sentral, QB5 and Wisma Technip likely due to tenant movements, which resulted in lower portfolio occupancy of 89% (vs. 96%), as well as loss of revenue from the disposal of QB8 - DHL XPJ, which was completed in 2Q18. All in, bottom-line decreased by 15% on slightly lower NPI margins (-1.1ppt) due to the weak top-line, while financing cost remained flattish. QoQ, top-line was down by 6% due to lower contributions from Platinum Sentral, QB5 and Wisma Technip likely due to similar reasons mentioned above. This coupled with slightly higher property expenses caused NPI margins to lower by 2.4ppt, resulting in RNI declining by 15%.

Outlook. FY19-20E will see 19-18% of net lettable assets (NLA) up for expiry, which is not overly significant given the tough office market conditions due to the oversupply of office spaces in KL and the overall Klang Valley, and risk of tenant attrition. Going forward, we are expecting flattish reversions for MQREIT's assets, and expect minimal capex of RM12-10m, mostly for maintenance.

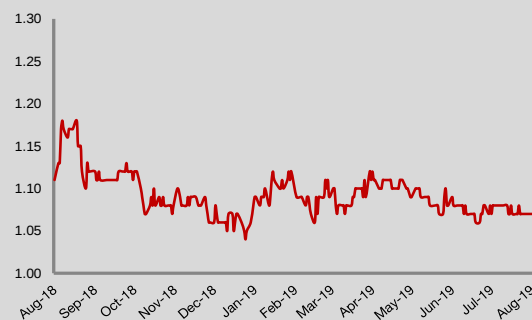
Trimming FY19-20E CNP by 10-9% to RM76-77m (from RM84-84m). We lower our earnings on marginally lower top-line on weaker portfolio occupancy to 90-92% (from 92-95% in FY19-20E) as well as lower RNI margin assumptions closer to current levels of 45% (from 48%). As a result, we lower our FY19-20E GDPU to 7.0-7.0 sen (NDPU of 6.3-6.3 sen), from GDPU 7.7-7.7 sen, (NDPU of 7.0-7.0 sen) suggesting gross yield of 6.5-6.5% (net yield of 5.9-5.9%), respectively.

Downgrade to MARKET PERFORM (from OUTPERFORM) on a lower Target Price of RM1.05 (from RM1.15). Our new TP is based on lowering our earnings and post rolling valuation forward to FY20E GDPU of 7.0 sen on an unchanged +3.1ppt spread to the 10-year MGS target of 3.70%. We are comfortable with our applied spread on MQREIT as it is the highest compared to other sizeable MREITs under our coverage (+1.3ppt to +3.1ppt) due to tough market conditions on concerns of oversupply in the office space. MQREIT is commanding decent gross yield of 6.5%, which is above its peers' average gross yield of 5.5%, but we believe this is justifiable given the abovementioned concerns for office assets. However, we are comfortable with our call as we believe we have priced in most downside risks into MQREIT's valuations and earnings.

MARKET PERFORM

Price: **RM1.07**
Target Price: **RM1.05**

Share Price Performance



KLCI 1,604.70
YTD KLCI chg -5.1%
YTD stock price chg 0.9%

Stock Information

Shariah Compliant	No
Bloomberg Ticker	MQREIT MK EQUITY
Market Cap (RM m)	1,146.8
Shares Outstanding	1,071.8
52-week range (H)	1.19
52-week range (L)	1.04
3-mth avg daily vol:	306,421
Free Float	49%
Beta	0.5

Major Shareholders

Malaysian Resources Corporation Berhad	27.8%
Employees Provident Fund Board	12.1%
CapitaLand Limited	10.9%

Summary Earnings Table

FY Dec (RM'm)	2018A	2019E	2020E
Turnover	173.4	169.5	170.7
EBIT	133.7	114.2	115.1
PBT	79.3	75.6	76.5
Net Profit	79.3	75.6	76.5
Core NP*	82.5	75.6	76.5
Consensus (CNP)	N.A.	82.8	84.4
Earnings Revision	N.A.	-10%	-9%
Core EPS (sen)	7.7	7.0	7.1
Core EPS growth (%)	-6%	-9%	1%
NDPS (sen)	7.3	6.3	6.3
BVPS (RM)	1.28	1.30	1.31
Core PER	13.9	15.2	15.1
Price/BV (x)	0.8	0.8	0.8
Gearing (x)	0.38	0.38	0.38
Net Div. Yield (%)	6.8	5.9	5.9

*Core NP refers to RNI



08 August 2019

OTHER POINTS

Risks to our call include bond yield expansions or compressions and weaker/stronger-than-expected rental reversions.

Result Highlight								
FYE 31 Dec (RM'm)	2Q19	1Q19	QoQ	2Q18	YoY	1H18	1H19	YoY-Ytd
Gross revenue	38.8	41.4	-6%	43.4	-11%	87.5	80.2	-8%
Prop Opex	-9.7	-9.3	4%	-10.0	-3%	-19.8	-19.0	-4%
NPI excl unrealised rental income	29.1	32.0	-9%	33.4	-13%	67.6	61.1	-10%
Interest Income	0.6	0.8	-32%	0.9	-36%	1.6	1.4	-13%
Gain on divestment prop	0.0	0.0	n.a.	2.2	n.m.	2.2	0.0	n.m.
Surplus on revaluation	0.0	0.0	n.a.	0.0	n.a.	0.0	0.0	n.a.
Total Trust Income	29.6	32.9	-10%	36.4	-19%	71.5	62.5	-13%
Expenditure	-3.5	-3.6	-4%	-3.0	15%	-7.3	-7.1	-4%
Finance Cost	-9.7	-9.9	-1%	-9.9	-2%	-19.6	-19.6	0%
Income Before Tax	16.5	19.4	-15%	23.5	-30%	44.5	35.9	-19%
Tax	0.0	0.0	n.a.	0.0	n.a.	0.0	0.0	n.a.
Net Income	16.5	19.4	-15%	23.5	-30%	44.5	35.9	-19%
Realised Net income (RNI)	16.5	19.4	-15%	21.3	-23%	42.3	35.9	-15%
Core EPU (sen)	1.54	1.81	-15%	1.99	-23%	3.96	3.35	-16%
DPU (sen)	3.43	0.00	n.a.	4.23	-19%	4.23	3.43	-19%
NAV/unit (RM)	1.27	1.26		1.30		1.30	1.27	
Gearing (x)	0.37	0.37		0.37		0.37	0.37	
NPI Margins	75.0%	77.4%		76.9%		77.4%	76.2%	
RNI Margins	42.4%	46.9%		49.0%		48.4%	44.7%	

Source: Company, Kenanga Research

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08 August 2019

Peer Comparison

Name	Last Price	Market	Shariah	Current	Revenue Growth		Core Earnings Growth		PER (x) - Core Earnings			PBV (x)		ROE (%)	Net Div.Yld. (%)	Target	Rating
	(RM)	Cap (RM'm)	Compliant	FYE	1-Yr. Fwd.	2-Yr. Fwd.	1-Yr. Fwd.	2-Yr. Fwd.	Hist.	1-Yr. Fwd.	2-Yr. Fwd.	Hist.	1-Yr. Fwd.	1-Yr. Fwd.	1-Yr. Fwd.	Price (RM)	
<u>MREITs UNDER COVERAGE</u>																	
AXIS REIT	1.84	2,276.6	Y	12/2019	3.3%	3.2%	1.3%	1.9%	20.1	19.8	19.4	1.4	1.4	6.9%	4.6%	1.85	MP
CAPITALAND MALAYSIA MALL TRUST	1.05	2,146.4	N	12/2019	-2.3%	4.3%	-16.0%	3.9%	13.3	15.9	15.3	0.8	0.8	5.0%	5.7%	1.10	MP
IGB REIT	2.00	7,091.7	N	12/2019	3.9%	1.7%	2.8%	1.6%	23.3	22.7	22.5	1.9	1.9	8.4%	4.3%	1.80	MP
KLCCP STAPLED GROUP	7.94	14,334.3	Y	12/2019	5.5%	0.7%	4.9%	1.2%	19.8	19.6	19.4	1.1	1.1	6.1%	4.5%	7.65	MP
MRCB-QUILL REIT	1.07	1,146.8	N	12/2019	-8.1%	0.7%	-16.4%	1.2%	13.9	15.2	15.1	0.8	0.8	5.4%	5.8%	1.05	MP
PAVILION REIT	1.87	5,683.0	N	12/2019	10.8%	2.0%	4.5%	2.6%	22.3	21.3	20.8	1.4	1.4	6.8%	4.4%	1.80	MP
SUNWAY REIT	1.89	5,566.2	N	06/2019	9.1%	6.9%	6.0%	2.7%	19.7	18.5	18.2	1.3	1.1	6.6%	4.8%	1.90	MP
Simple Average					3.2%	2.8%	-1.8%	2.1%	18.7	19.0	18.7	1.2	1.2	6.5%	5.0%		
<i>* Core NP and Core PER</i>																	
<u>CONSENSUS NUMBERS</u>																	
YTL HOSPITALITY REIT	1.35	2,300.9	N	06/2020	5.6%	3.3%	44.3%	4.6%	22.0	15.2	14.6	0.9	0.8	0.0	6.1%	1.40	BUY
AL-'AQAR HEALTHCARE REIT	1.52	1,118.7	Y	12/2019	-2.1%	1.9%	-32.9%	2.9%	12.2	18.2	17.7	1.2	N.A.	0.1	5.2%	1.50	N.A.
AMANAHRAYA REIT	0.830	475.8	N	12/2019	27.4%	-0.8%	-52.4%	4.1%	5.9	12.3	11.8	0.6	N.A.	0.1	7.3%	0.910	BUY
AMFIRST REIT	0.510	350.1	N	03/2020	N.A.	N.A.	N.A.	N.A.	15.7	N.A.	N.A.	0.4	N.A.	N.A.	N.A.	N.A.	N.A.
HEKTAR REIT	1.02	471.2	N	12/2019	N.A.	N.A.	N.A.	N.A.	14.2	N.A.	N.A.	0.7	N.A.	N.A.	N.A.	N.A.	N.A.
TOWER REIT	0.925	259.5	N	06/2019	N.A.	N.A.	N.A.	N.A.	49.3	N.A.	N.A.	0.5	N.A.	N.A.	N.A.	N.A.	N.A.
UOA REIT	1.30	549.7	N	12/2019	N.A.	N.A.	N.A.	N.A.	9.6	N.A.	N.A.	0.8	N.A.	N.A.	N.A.	N.A.	N.A.
ATRIUM REIT	1.18	172.5	N	12/2019	N.A.	N.A.	N.A.	N.A.	14.9	N.A.	N.A.	0.8	N.A.	N.A.	N.A.	N.A.	N.A.
AL-SALAM REIT	0.910	527.8	Y	12/2019	7.0%	5.1%	-26.7%	4.2%	13.1	17.9	17.1	0.9	0.9	0.0	5.2%	0.830	N.A.
KIP REIT	0.845	427.0	N	06/2020	N.A.	N.A.	N.A.	N.A.	12.5	N.A.	N.A.	0.8	N.A.	N.A.	N.A.	N.A.	N.A.

Source: Bloomberg, Kenanga Research

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Stock Ratings are defined as follows:**Stock Recommendations**

OUTPERFORM	: A particular stock's Expected Total Return is MORE than 10%
MARKET PERFORM	: A particular stock's Expected Total Return is WITHIN the range of -5% to 10%
UNDERPERFORM	: A particular stock's Expected Total Return is LESS than -5%

Sector Recommendations***

OVERWEIGHT	: A particular sector's Expected Total Return is MORE than 10%
NEUTRAL	: A particular sector's Expected Total Return is WITHIN the range of -5% to 10%
UNDERWEIGHT	: A particular sector's Expected Total Return is LESS than -5%

*****Sector recommendations are defined based on market capitalisation weighted average expected total return for stocks under our coverage.**

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