20 January 2021

Property | REITS

Sentral REIT (SENTRAL MK)

Buy (Maintained)

Ending FY20 On a Strong Note; Maintain BUY

Target Price (Return):	MYR1.00 (+10%)
Price:	MYR0.91
Market Cap:	USD241m
Avg Daily Turnover (MYR/USD)	0.36m/0.08m

- **Maintain BUY, new DDM-derived TP of MYR1.00 from MYR0.95, 10% upside with 7.6% FY21F yield.** Sentral REIT (formerly known as MRCB-Quill REIT) closed 2020 on a good note as full-year earnings beat expectations, due to higher contributions from Menara Shell and Wisma Technip. Its average occupancy rate has been stable, and we view the likelihood of positive reversions as a positive for the REIT. However, non-renewal risk remains a concern this year, with 21% of NLA up for expiry.
- **Earnings beat, again.** 4Q20 earnings of MYR20.6m (+10.8% YoY, -4% QoQ) brought FY20 net profit to MYR81m (+12.3% YoY), at 105-106% of our and Street full-year estimates. The encouraging performance was due to higher revenue from Menara Shell, Wisma Technip and Tesco. The REIT's blended occupancy rate as at end-FY20 stood at 90%, ie a marginal dip from 90.5% in 3Q20. Considering the resilient occupancy levels, we do not rule out the possibility that rental reversions may be positive – especially in view of the step-up in rental rates at Menara Shell (which takes place every three years).
- **15% non-renewals in FY20.** Only 85% of leases up for renewal in FY20 were renewed. The 15% non-renewals were at in Quill-Building 3, Platinum Sentral, Wisma Technip, and Menara Shell. From this trend, we have reason to believe that non-renewal risk remains a concern for the REIT in the new year – since 21% of leases are up for expiry in FY21. Although Sentral REIT has not seen a significant drop in occupancy rate, in the face of COVID-19 and the ensuing work-from-home trend, we believe that FY21 may possibly see higher vacancies in the REIT's buildings. The bulk of leases up for expiry, as per management's guidance, is for space at Wisma Technip and Menara Shell.
- **Use of proceeds from Quill Building 5 (QB5) disposal.** It is yet to be decided what the MYR45m cash proceeds from the disposal of the vacant QB5 last year will be used for. Options include paring down debt, funding any asset enhancement initiatives, and making investments in other assets. Management does not discount that the proceeds may be for a combination of uses, but the possibility of acquiring Menara Celcom is still on the backburner at this point in time.
- **Maintain BUY.** We introduce our FY23 earnings forecast of MYR76m, and increase FY21-22F net profit marginally by 1-3%, as we impute positive reversions (from flat-to-negative previously). Our TP increases to MYR1.00.

Forecasts and Valuations	Dec-19	Dec-20	Dec-21F	Dec-22F	Dec-23F
Total turnover (MYRm)	162	166	152	153	154
Net property income (MYRm)	123	128	117	118	119
Reported net profit (MYRm)	29	73	74	75	76
Total distributable income (MYRm)	72	81	74	75	76
DPS (MYR)	0.07	0.07	0.07	0.07	0.07
P/B (x)	0.73	0.73	0.73	0.73	0.73
Dividend Yield (%)	7.6	7.9	7.6	7.7	7.8
Return on average equity (%)	2.2	5.5	5.6	5.7	5.7
Return on average assets (%)	1.3	3.3	3.3	3.4	3.4
Gross gearing (%)	37.8	37.9	37.9	37.9	37.9

Source: Company data, RHB

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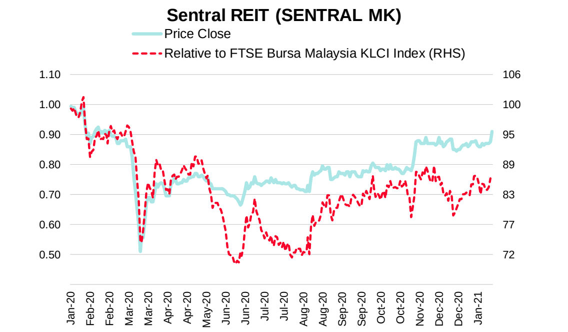
Share Performance (%)

	YTD	1m	3m	6m	12m
Absolute	4.0	7.7	16.7	23.0	(9.0)
Relative	5.1	10.3	10.7	22.2	(9.9)
52-wk Price low/high (MYR)					0.51 – 0.99



Source: Bloomberg

Overall ESG Score: 3.0 (out of 4)

E: Good

Sentral REIT has managed to reduce its overall water consumption in FY19 by 2% YoY, and is developing its own water management policy. The company also doubled the capacity of Platinum Sentral's solar power system, and subscribes to the Feed-In-Tariff (FiT) scheme for the Solar PV programme.

S: Good

67% of Sentral REIT's workforce are women, and they provide sufficient training to employees through MRCB Training Academy, MRCB Learning Zone, and industrial practical training. To ensure health and safety, it also conducts activities with external parties such as the Fire and Rescue Department of Malaysia.

G: Excellent

We view positively its establishment of a policy on giving and receiving gifts and the commitment to the Corruption-Free Pledge by the Malaysian Anti-Corruption Commission. Directors' tenure range between 4-6 years, on average.

Note:
Small cap stocks are defined as companies with a market capitalization of less than USD1bn.

Financial Exhibits

Asia
Malaysia
Property
Sentral REIT
SENTRAL MK
Buy

Valuation basis

DDM

Key drivers

i. Higher-than-expected demand for office space;
ii. Inorganic growth opportunities arising from MRCB and Quill Group.

Key risks

A downside risk is the oversupply of office properties, which may affect its portfolio's office property occupancy and rental rates.

Company Profile

Sentral 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-19**	**Dec-20**	**Dec-21F**	**Dec-22F**	**Dec-23F**
Recurring EPS (MYR)	0.07	0.08	0.07	0.07	0.07
EPS (MYR)	0.07	0.08	0.07	0.07	0.07
DPS (MYR)	0.07	0.07	0.07	0.07	0.07
BVPS (MYR)	1.23	1.23	1.24	1.24	1.24
Weighted avg adjusted shares (m)	1,071.8	1,071.8	1,071.8	1,071.8	1,071.8

Valuation metrics	**Dec-19**	**Dec-20**	**Dec-21F**	**Dec-22F**	**Dec-23F**
Recurring P/E (x)	13.4	11.9	13.1	12.9	12.7
P/E (x)	13.4	11.9	13.1	12.9	12.7
P/B (x)	0.7	0.7	0.7	0.7	0.7
FCF Yield (%)	12.1	11.0	11.5	10.8	10.9
Dividend yield (%)	7.6	7.9	7.6	7.7	7.8
EV/EBITDA (x)	19.4	14.0	14.5	14.8	14.7
EV/EBIT (x)	19.4	14.0	14.5	14.8	14.7

Income statement (MYRm)	**Dec-19**	**Dec-20**	**Dec-21F**	**Dec-22F**	**Dec-23F**
Total turnover	162	166	152	153	154
Gross profit	123	128	117	118	119
EBITDA	89	124	120	121	122
Depreciation and amortisation	-	-	-	-	-
Operating profit	89	124	120	121	122
Net interest	(40)	(35)	(35)	(35)	(35)
Income from associates & JVs	-	-	-	-	-
Exceptional income - net	(37)	(7)	-	-	-
Pre-tax profit	35	74	74	75	76
Taxation	(6)	(1)	-	-	-
Minority interests	-	-	-	-	-
Recurring net profit(adj)	72	81	74	75	76

Cash flow (MYRm)	**Dec-19**	**Dec-20**	**Dec-21F**	**Dec-22F**	**Dec-23F**
Change in working capital	(4)	(4)	(4)	(5)	(5)
Cash flow from operations	106	111	104	105	106
Capex	(2)	(2)	(2)	(2)	(2)
Cash flow from investing activities	1	1	1	1	1
Dividends paid	(80)	(77)	(77)	(74)	(75)
Cash flow from financing activities	(120)	(112)	(112)	(109)	(110)
Cash at beginning of period	43	31	31	24	20
Net change in cash	(12)	(0)	(8)	(3)	(4)
Ending balance cash	31	31	24	20	17

Balance sheet (MYRm)	**Dec-19**	**Dec-20**	**Dec-21F**	**Dec-22F**	**Dec-23F**
Total cash and equivalents	63	85	69	20	17
Tangible fixed assets	2,144	2,098	2,058	2,058	2,058
Intangible assets	-	-	-	-	-
Total investments	-	-	-	-	-
Total other assets	1	0	98	148	153
Total assets	2,214	2,228	2,229	2,230	2,232
Short-term debt	333	218	218	218	218
Total long-term debt	503	627	627	627	627
Other liabilities	54	59	60	60	61
Total liabilities	890	904	905	905	906
Shareholders' equity	1,323	1,324	1,324	1,325	1,326
Minority interests	-	-	-	-	-
Total equity	1,323	1,324	1,324	1,325	1,326
Net debt	772	760	776	825	828
Total liabilities & equity	2,214	2,228	2,229	2,230	2,232

Key metrics	**Dec-19**	**Dec-20**	**Dec-21F**	**Dec-22F**	**Dec-23F**
Revenue growth (%)	(6.5)	2.2	(8.2)	0.7	0.6
Recurrent EPS growth (%)	(14.9)	12.2	(8.8)	1.6	1.4
Gross margin (%)	75.8	77.1	77.1	77.1	77.1
Operating EBITDA margin (%)	55.1	74.6	79.0	79.0	79.0
Net profit margin (%)	44.5	48.9	48.5	48.9	49.3
Dividend payout ratio (%)	101.0	93.8	99.0	99.0	99.0
Capex/sales (%)	1.2	1.2	1.3	1.3	1.3
Interest cover (x)	2.3	3.5	3.4	3.4	3.4

Source: Company data, RHB

Results at a Glance

Figure 1: Sentral REIT's 4Q20 and FY20 results summary

FYE Dec (MYRm)	4Q19	3Q20	4Q20	QoQ (%)	YoY (%)	FY19	FY20	YoY (%)	Comments
Revenue	**42.0**	**42.1**	**41.8**	**(0.6)**	**(0.4)**	**162.1**	**165.7**	**2.2**	Increased YoY due to higher contributions generated from Tesco, Menara Shell, and Wisma Technip.
Net property income (NPI)	**31.5**	**32.7**	**31.8**	**(2.9)**	**0.9**	**122.8**	**127.8**	**4.1**	
Interest expense	(10.3)	(8.3)	(8.6)	3.2	(16.4)	(39.6)	(35.4)	(10.7)	
Interest income	1.1	0.6	1.2	83.2	2.8	3.2	2.9	(9.6)	
Associates	0.0	0.0	0.0	nm	nm	0.0	0.0	nm	
EI	(36.7)	0.0	(7.2)	nm	(80.5)	(36.7)	(7.2)	(80.5)	
Others	(3.8)	(3.6)	(3.8)	4.8	(0.5)	(14.4)	(14.4)	0.2	
Pretax profit	**(18.1)**	**21.5**	**13.4**	**(37.4)**	**(174.1)**	**35.4**	**73.8**	**108.7**	
Tax	(6.2)	0.0	(1.2)	nm	(80.5)	(6.2)	(1.2)	(80.5)	
Minority Interest	(6.2)	0.0	(1.2)	nm	(80.5)	(6.2)	(1.2)	(80.5)	
Net Profit	**(24.4)**	**21.5**	**12.2**	**(43.1)**	**(150.1)**	**29.1**	**72.6**	**149.2**	
Core Profit	**18.6**	**21.5**	**20.6**	**(4.0)**	**10.8**	**72.1**	**81.0**	**12.3**	Above expectations.
Core earnings per unit (sen)	**1.74**	**2.00**	**1.92**	**(4.0)**	**10.3**	**6.73**	**7.55**	**12.2**	
Dividends per unit (sen)	**3.37**	**2.00**	**3.65**	**82.5**	**8.3**	**8.45**	**9.08**	**7.5**	
NPI Margin (%)	*75.0*	*77.9*	*76.0*			*75.8*	*77.1*		
Pretax Margin (%)	*(43.2)*	*51.1*	*32.1*			*21.8*	*44.5*		
Net Margin (%)	*44.3*	*51.1*	*49.3*			*44.5*	*48.9*		

Source: Company data, RHB

Recommendation Chart

Source: RHB, Bloomberg

Date	Recommendation	Target Price	Price
2020-12-09	Buy	0.95	0.87
2020-11-12	Buy	0.87	0.83
2020-08-17	Buy	0.83	0.78
2020-06-18	Buy	0.78	0.71
2020-04-06	Neutral	0.78	0.74
2020-01-20	Neutral	0.97	1.00
2019-11-26	Neutral	0.96	1.02
2019-08-08	Neutral	0.97	1.07
2019-05-10	Neutral	1.02	1.09
2019-01-18	Neutral	1.05	1.11
2019-01-10	Neutral	1.10	1.09
2018-11-28	Neutral	1.15	1.07
2018-08-09	Neutral	1.20	1.18

Source: RHB, Bloomberg

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