

6 August 2021

Sentral REIT (SENTRAL MK)

Occupancy Still Going Strong; Maintain BUY

- **Maintain BUY and MYR1.00 TP, 11% upside with 7.7% FY21F yield.** Sentral REIT's results came in within expectations despite flattish YoY growth due to 1H21 rebates granted on a case-by-case basis to qualifying tenants. While we expect for there to be pressure on reversion rates, we believe occupancy should remain largely supported – albeit with slight non-renewals – owing to the quality of the prime assets in Kuala Lumpur and Malaysia's encouraging vaccination progress.
- **Results are in line with expectations.** 2Q21 core earnings of MYR18.3m (-11.5% QoQ, -6.5% YoY), excluding the MYR3.75m gain on the divestment of Quill Building 5, brought 1H21 earnings to MYR39m (-2.2% YoY). At 49-53% of our and Street's full-year estimates, we deem the results to be in line with expectations. 1H21 revenue growth was 5% lower YoY due to lower contributions generated from Quill Building 3, Wisma Technip, Plaza Mont Kiara, and Platinum Sentral. Considering that occupancy rates remain supported, the negative growth is attributed to rental rebates granted to tenants on a case-by-case basis. 1H21 earnings saw -2.2% YoY growth, supported in part by the lower total expenditure YTD – namely manager's fees and finance costs.
- **22% leases up for expiry in FY21.** Leases up for expiry in 1H21 saw a 73% renewal rate, and we note that this makes up only c.14% of the leases up for renewal for FY21. Because most of its leases up for renewal are due in 2H21 and that negotiations are ongoing, we believe reversions dipping into negative territory may be a risk in the face of COVID-19 and ensuing work-from-home trend. Nevertheless, the encouraging vaccination progress and our channel checks suggest that demand for office space is likely to stay, albeit at a softer magnitude – proven by Sentral REIT's robust occupancy rates demonstrated so far. The bulk of leases up for expiry, as per management's guidance, is for space at Wisma Technip and Menara Shell.
- **Occupancy largely stable at 92%.** Sentral REIT's blended occupancy rate remains stable at 92% from 89% in the previous quarter after having excluded the newly divested vacant Quill Building 5. We gather there was a slight drop in occupancy at Platinum Sentral due to an existing tenant downsizing – in line with our expectation of a mild non-renewal risk. While we expect there to be pressure on reversion rates, we believe occupancy should remain largely supported, owing to the quality of the prime assets in Kuala Lumpur and Malaysia's encouraging vaccination progress.
- **Maintain BUY.** We make no changes to our earnings forecast, expecting a softer 2H21 due to rebates that may be granted due to a prolonged lockdown. Rolling forward our base year to FY22 and tweaking our risk premium assumption in our DDM valuation to reflect the non-renewal risk, our TP is maintained at MYR1.00.

Forecasts and Valuation	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)	72.1	81.0	73.8	75.0	76.1
Total distributable income (MYRm)	72.1	81.0	73.8	75.0	76.1
DPS (MYR)	0.07	0.08	0.07	0.07	0.07
DPS growth (%)	(16.2)	10.9	(9.7)	1.6	1.4
P/B (x)	0.73	0.73	0.73	0.73	0.73
Dividend Yield (%)	7.6	8.4	7.6	7.7	7.8
Return on average equity (%)	5.3	6.1	5.6	5.7	5.7
Return on average assets (%)	3.2	3.6	3.3	3.4	3.4

Source: Company data, RHB

Malaysia Results Review

Property | REITS

Buy (Maintained)

Target Price (Return):	MYR1.00 (11.1%)
Price:	MYR0.90
Market Cap:	USD229m
Avg Daily Turnover (MYR/USD)	0.34m/0.08m

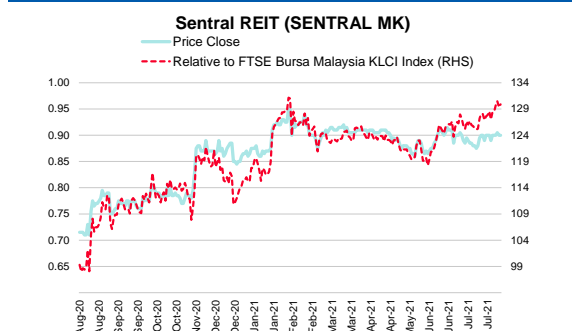
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Share Performance (%)

	YTD	1m	3m	6m	12m
Absolute	2.9	1.1	0.6	0.0	25.0
Relative	11.3	3.9	6.7	5.9	30.4
52-wk Price low/high (MYR)				0.71	0.95



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. It doubled the capacity of Platinum Sentral's solar power system and subscribes to the Feed-In-Tariff (FiT) for the solar photovoltaic or PV programme.

S: Good

67% of Sentral REIT's workforce is female, and it provides sufficient training to employees through the MRCB Training Academy, MRCB Learning Zone, and industrial practical training. To ensure health and safety, it also conducts activities with external parties, eg the Fire & Rescue Department.

G: Excellent

We view positively the establishment of a Policy on Giving and Receiving Gifts, and commitment to the Corruption-Free Pledge by the Malaysian Anti-Corruption Commission. Directors' tenures range between four and six years on average.

Note:

Small cap stocks are defined as companies with a market capitalisation of less than USD1bn.

Financial Exhibits

Asia	Financial summary	Dec-19	Dec-20	Dec-21F	Dec-22F	Dec-23F
Malaysia	Recurring EPS (MYR)	0.07	0.08	0.07	0.07	0.07
Property	EPS (MYR)	0.07	0.08	0.07	0.07	0.07
Sentral REIT	DPS (MYR)	0.07	0.08	0.07	0.07	0.07
SENTRAL MK	BVPS (MYR)	1.23	1.23	1.24	1.24	1.24
Buy	Return on average equity (%)	5.3	6.1	5.6	5.7	5.7
	Weighted avg adjusted shares (m)	1,071.78	1,071.78	1,071.78	1,071.78	1,071.78
Valuation basis	Valuation metrics	Dec-19	Dec-20	Dec-21F	Dec-22F	Dec-23F
Dividend discount model.	Recurring P/E (x)	13.38	11.91	13.07	12.86	12.68
	P/E (x)	13.38	11.91	13.07	12.86	12.68
Key drivers	P/B (x)	0.7	0.7	0.7	0.7	0.7
Higher-than-expected demand of office space and inorganic growth opportunities arising from Malaysian Resources Corp and Quill Group.	FCF Yield (%)	7.1	8.0	7.2	7.3	7.4
	Dividend Yield (%)	7.6	8.4	7.6	7.7	7.8
Key risks	EV/EBITDA (x)	(3.75)	(3.29)	(2.97)	(2.49)	(2.43)
Downside risks oversupply of office properties might affect the portfolio's office property occupancy and rental rates.	EV/EBIT (x)	(3.75)	(3.29)	(2.97)	(2.49)	(2.43)
Company Profile	Income statement (MYRm)	Dec-19	Dec-20	Dec-21F	Dec-22F	Dec-23F
Sentral REIT is a mid-cap MREIT that focuses on office/commercial assets. Assets are largely concentrated in the Klang Valley and Cyberjaya.	Total turnover	162	166	152	153	154
	EBITDA	108	113	106	108	109
	Operating profit	108	113	106	108	109
	Net interest	(36)	(32)	(33)	(33)	(33)
	Pre-tax profit	72	81	74	75	76
	Recurring net profit	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	70	79	71	72	73
	Capex	(2)	(2)	(2)	(2)	(2)
	Cash flow from investing activities	(2)	(2)	(2)	(2)	(2)
	Dividends paid	(80)	(77)	(77)	(74)	(75)
	Cash flow from financing activities	(442)	54	(77)	(74)	(75)
	Cash at beginning of period	86	63	85	69	20
	Net change in cash	(374)	131	(8)	(3)	(4)
	Ending balance cash	(288)	194	77	65	17
	Balance sheet (MYRm)	Dec-19	Dec-20	Dec-21F	Dec-22F	Dec-23F
	Total cash and equivalents	63	85	69	20	17
	Total investments	2,144	2,097	2,057	2,057	2,057
	Total other assets	0	40	0	0	0
	Total assets	2,214	2,227	2,229	2,230	2,231
	Short-term debt	333	218	218	218	218
	Total long-term debt	503	627	627	627	627
	Total liabilities	890	904	904	905	906
	Shareholders' equity	1,323	1,324	1,324	1,325	1,326
	Total equity	1,323	1,324	1,324	1,325	1,326
	Net debt	772	760	776	825	828
	Total liabilities & equity	2,214	2,227	2,229	2,230	2,231
	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 (%)	(11.2)	12.3	(8.8)	1.6	1.4
	Operating EBITDA margin (%)	66.9	68.5	69.9	70.2	70.5
	Net profit margin (%)	44.5	48.9	48.5	48.9	49.3
	Dividend payout ratio (%)	101.2	100.0	99.0	99.0	99.0
	Capex/sales (%)	1.2	1.2	1.3	1.3	1.3
	Interest cover (x)	2.74	3.21	3.00	3.03	3.06

Source: Company data, RHB

Results At a Glance

Figure 1: Sentral REIT's 1H20 results summary

FYE Dec (MYRm)	2Q20	1Q21	2Q21	QoQ (%)	YoY (%)	1H20	1H21	YoY (%)	Comments
Revenue	40.6	41.0	37.6	(8.3)	(7.4)	82.8	78.7	(5.0)	Lower YoY on lower income from Quill Building 3, Wisma Technip, Plaza Mont Kiara, and Platinum Sentral.
Net property income (NPI)	31.5	31.4	29.0	(7.6)	(7.8)	64.3	60.5	(5.9)	
Interest expense	(8.9)	(7.7)	(7.8)	0.8	(13.0)	(18.5)	(15.4)	(16.4)	
Interest income	0.5	0.5	0.5	1.0	(9.9)	1.1	1.0	(13.2)	
Associates	0.0	0.0	0.0	nm	nm	0.0	0.0	nm	
Others	(3.5)	(3.5)	(3.5)	(2.0)	(1.5)	(7.1)	(7.0)	(0.8)	
Pre-tax profit	19.1	20.7	22.6	9.4	18.7	38.9	43.3	11.5	
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	19.1	20.7	22.6	9.4	18.7	38.9	43.3	11.5	
Core profit	19.6	20.7	18.3	(11.5)	(6.5)	39.9	39.0	(2.2)	Within expectations.
Core earnings per unit (sen)	1.78	1.93	2.11	9.3	18.5	3.63	4.04	11.3	
Dividends per unit (sen)	3.43	0.00	3.43	nm	0.0	3.43	3.43	0.0	
NPI margin (%)	77.5	76.6	77.2			77.6	76.9		
Pre-tax margin (%)	47.0	50.4	60.2			46.9	55.1		
Net margin (%)	48.2	50.4	48.7			48.2	49.6		

Source: Company data, RHB

Recommendation Chart



Source: RHB, Bloomberg

Date	Recommendation	Target Price	Price
2021-01-19	Buy	1.00	0.91
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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