

MRCB - Quill REIT (BUY ↔, EPS ↔)

INDUSTRY: NEUTRAL

EARNINGS EVALUATION

21 May 2015

Target Price: RM1.34 (↔)

Share Price: RM1.16

1Q15 Results
Results

- 1QFY15 gross revenue of RM18.6m (+8.3% yoy, 2.3% qoq) was translated into normalised net profit of RM8.3m (+1.4% yoy), accounting for 16.0% and 16.5% of HLIB and consensus FY forecasts, respectively.

Deviations

- In-line.

Dividends

- None (1Q14 : None).
- Dividends normally declared semi-annually – during second and fourth quarter.

Highlights

- During the quarter, gross revenue increase by +8.3% yoy on the back of higher rental rates and recoveries. Operating expenses also increase by +18.2% yoy due to higher repair and maintenance cost and also recognition of property expenses for Plaza Mont' Kiara upon its expiry of master lease agreement in Sept 2014.
- Both NPI margin and occupancy level remain healthy (Figure #4 and Figure #5 respectively).
- Acquisition of Platinum Sentral has been completed on 30 March and two days revenue contribution has been recognised during the quarter. Post-acquisition, 47% of properties are now concentrated in KL Sentral area (Figure #6) and GLCs have emerged as a substantial tenant of the portfolio (Figure #7).
- As at 31 March 2015, fixed and floating borrowing was at 62:38. However, on 21 April 2015, management has entered into interest rate swap to convert its floating interest rate to become fully fixed interest rate.
- We understand that there are few assets held by sponsors which are ready to be evaluated for injection purpose, such as Shell Tower & Ascott Residence, Quill Building 6, Quill Building 9 and Quill Building 18.

Risks

- Management continuity following the entry of MRCB.
- Slow rental reversion rate.

Forecasts

- Unchanged.

Rating
BUY ↔, TP: RM1.34 ↔
Valuation

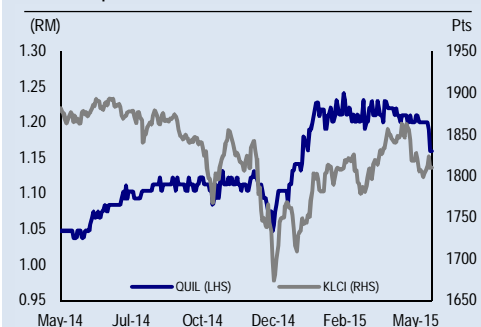
- Positives: (1) higher possibility of asset injections from MRCB and EPF, following the injection of Platinum Sentral, resulting in MRCB taking control of QCM and major unitholder of QCT; (2) Resilient earnings growth with undemanding valuations – 8.6% DY (FY15E).
- Negatives: (1) Small asset base; (2) illiquid; (3) lack of retail assets.
- Maintain BUY recommendation on the equity and unchanged TP of RM1.34.
- Our valuation was pegged to targeted yield of 6.9% based on 2SD below historical average yield spread of MRCB-Quill REIT and 7-year government bond in view of high potential for yield accretive injection(s).

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KLCI	1810.1
Expected share price return	15.5%
Expected dividend return	7.4%
Expected total return	22.9%

Share price

Information

Bloomberg Ticker	QUIL MK
Bursa Code	5123
Issued Shares (m)	661
Market cap (RM m)	767
3-mth avg. volume ('000)	159
SC Shariah-compliant	No

Price Performance	1M	3M	12M
Absolute	-3.3	-5.7	1.8
Relative	-1.3	-5.8	5.7

Major Shareholders

MRCB	31.2%
Quill Group	17.7%

Summary Earnings Table

FYE Dec (RMm)	2014A	2015E	2016E	2017E
Revenue	70.2	128.3	133.0	137.9
NPI	53.2	100.4	104.1	107.9
Net invest income	56.1	101.0	105.6	109.3
PAT	36.6	56.9	61.2	64.5
EPU (sen)	10.3	8.6	9.2	9.8
Norm. PER (x)	11.2	13.5	12.5	11.9
FD PER (x)	11.2	13.5	12.5	11.9
EV/ EBITDA (x)	28.0	63.5	53.5	47.6
Net DPU (sen)	8.4	8.6	9.2	9.8
Distrib. yield (%)	7.2	7.4	8.0	8.4
BVPS (RM)	1.4	1.3	1.3	1.3
P/B (x)	0.8	0.9	0.9	0.9

HLIB

Figure #1 Quarterly Results Comparison

FYE Dec (RMm)	1Q14	4Q14	1Q15	YoY (%)	QoQ (%)	Comments
Gross revenue	17.18	18.18	18.61	8.29	2.34	Higher revenue from: (i) higher rental rates; (ii) higher revenue from Plaza Mont' Kiara; and (iii) higher recoveries of some properties.
Property operating expenses	(4.17)	(4.77)	(4.93)	18.16	3.36	Higher repair and maintenance cost and expenses related to Plaza Mont' Kiara.
Net property income	13.01	13.41	13.68	5.12	1.98	
Interest income	0.11	0.10	0.13	10.94	28.28	Higher cash balance in the current quarter.
Net investment income	13.13	19.63	13.81	5.17	(29.68)	
Finance costs	(3.43)	(3.45)	(3.54)	3.12	2.45	Additional borrowings drawdown during the quarter.
Valuation fees	(0.05)	(0.05)	(0.05)	(0.00)	(0.01)	
Administrative expenses	(0.14)	(0.08)	(0.19)	37.56	155.22	AGM conducted in the current quarter.
Total Expenses	(4.96)	(5.01)	(5.53)	11.33	10.22	
Normalised PBT	8.16	8.50	8.28	1.43	(2.58)	
Normalised PAT	8.16	8.50	8.28	1.43	(2.58)	
EPU after mgmt fee	2.09	2.18	2.09	0.00	(4.13)	
DPU (sen)	0.00	4.28	0.00	NM	NM	

Company Data

Figure #2 1Q15 Results vs. HLIB's Estimates and Consensus

	Actual 1Q15	HLIB FY15	Actual vs. HLIB (%)	Consensus FY15	Actual vs. Consensus (%)	Comments
Revenue	18.6	116.1	16.0	113.0	16.5	In-line
Normalised PAT	8.3	56.9	14.5	53.1	15.6	In-line
EPU (sen)	2.1	8.6	24.3	8.7	24.0	In-line
DPU (sen)	0.0	8.6	0.0	8.5	0.0	NM

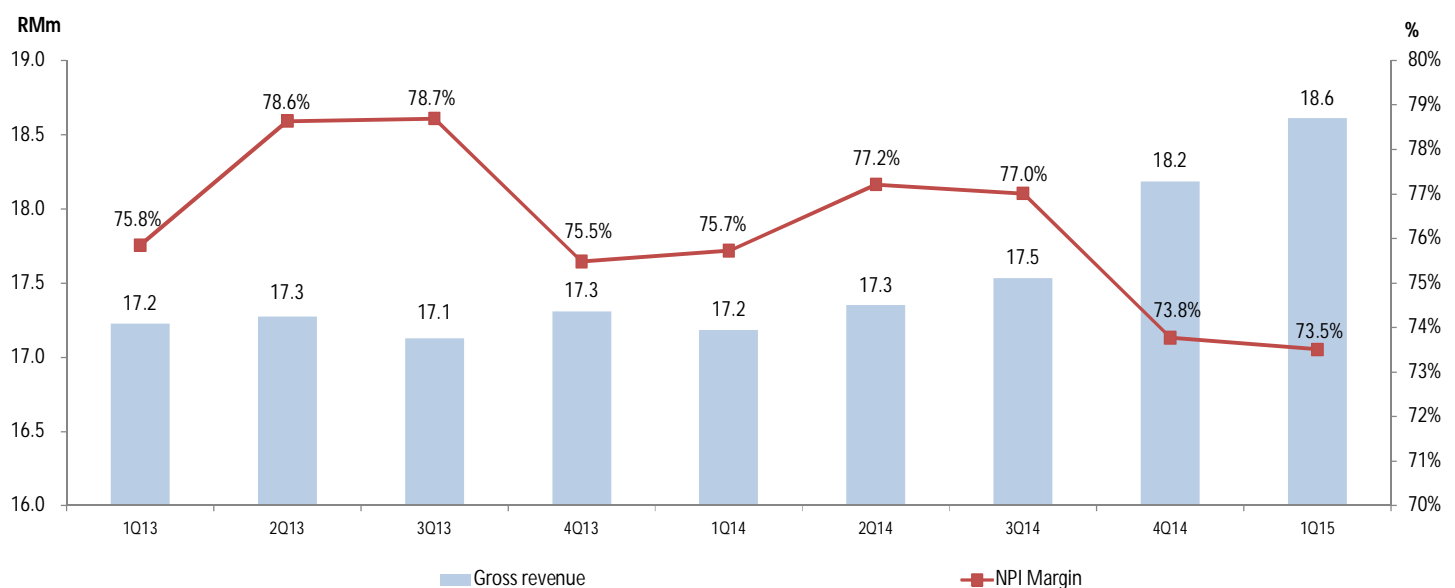
Company Data, HLIB, Bloomberg

Figure #3 HLIB Forecasts vs. Consensus

RMm	FY16E			FY17E		
	HLIB	Consensus	%	HLIB	Consensus	%
Normalised PAT	61.2	57.6	6.2	64.5	59.3	8.9
DPU (sen)	9.2	8.8	5.1	9.8	9.0	8.4

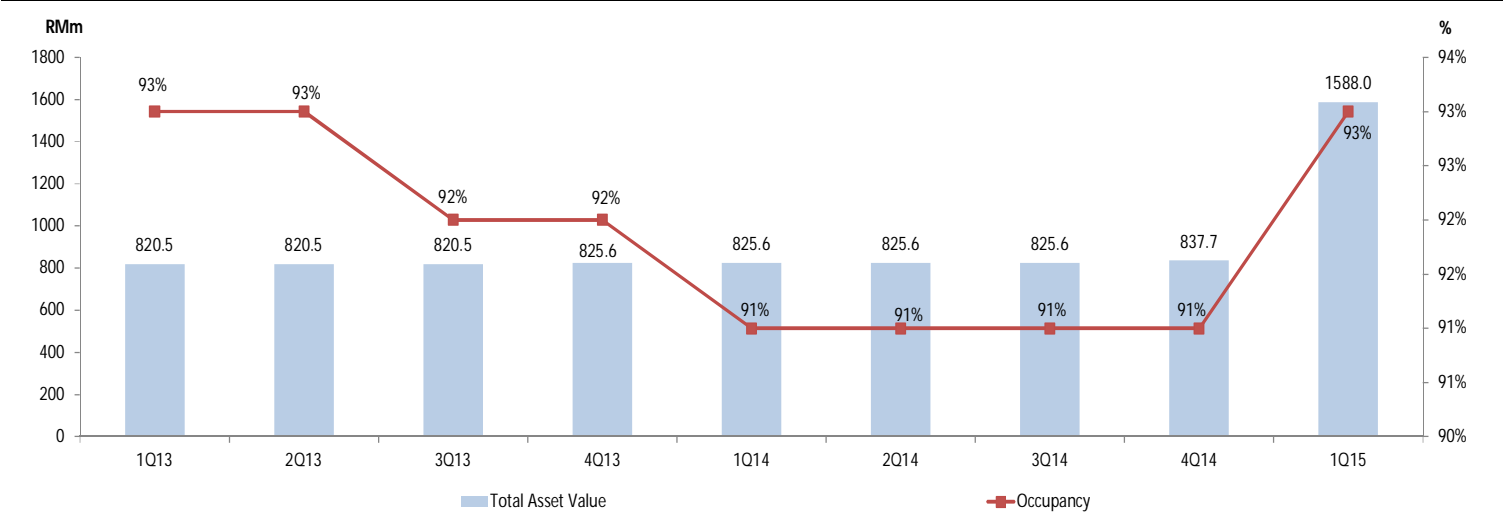
HLIB, Bloomberg

Figure #4 Gross Revenue & NPI Margin



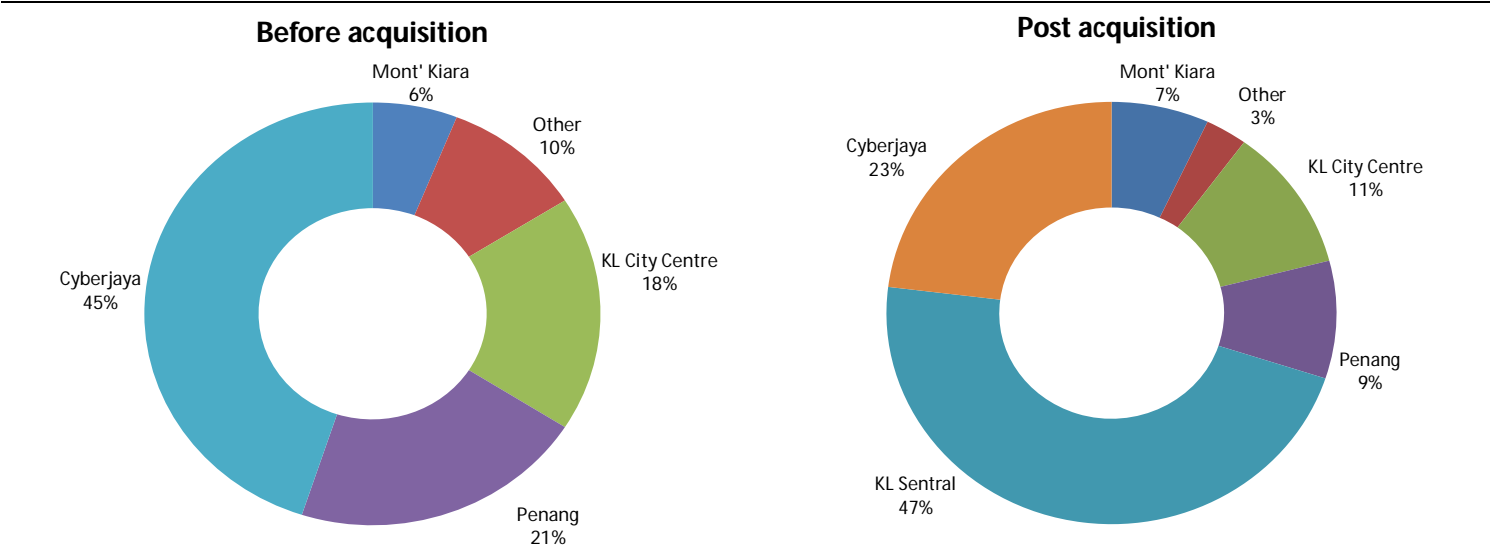
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Figure #5 Total Asset Value & Occupancy



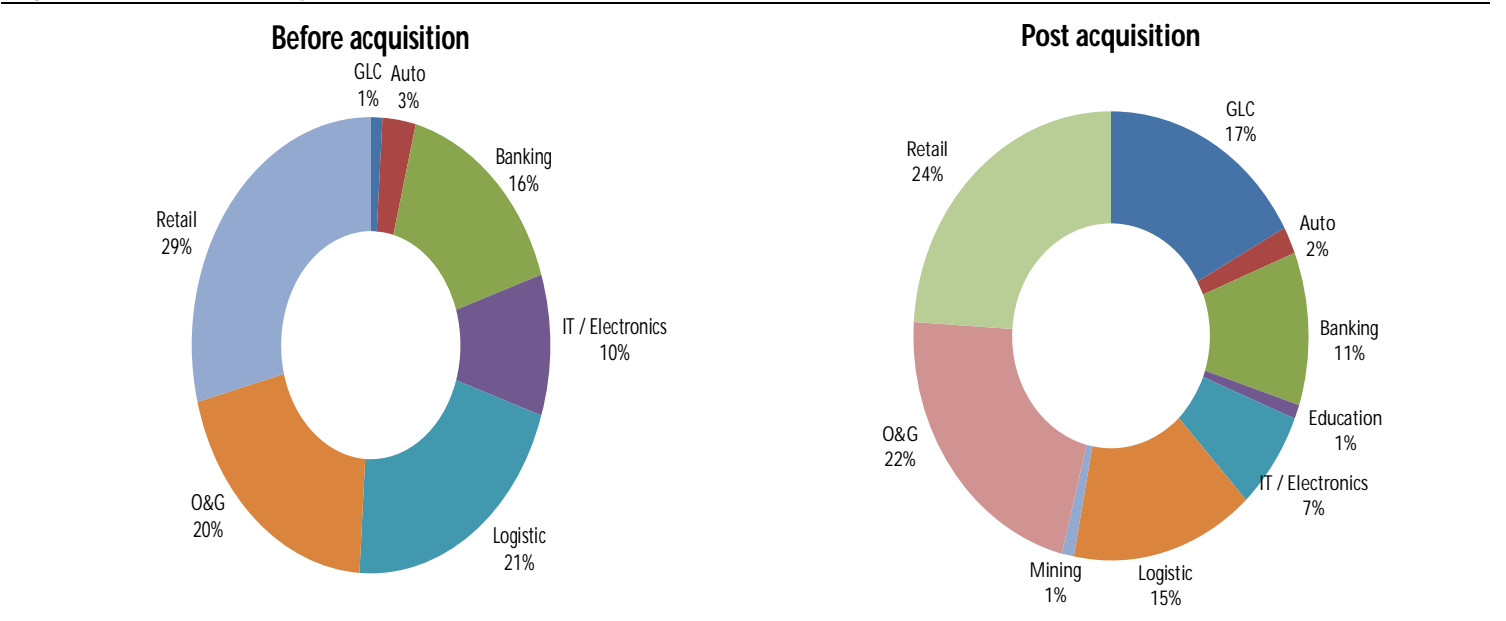
HLIB, Bloomberg

Figure #6 Geographical Diversification



Company Data, HLIB

Figure #7 Tenancy Mix



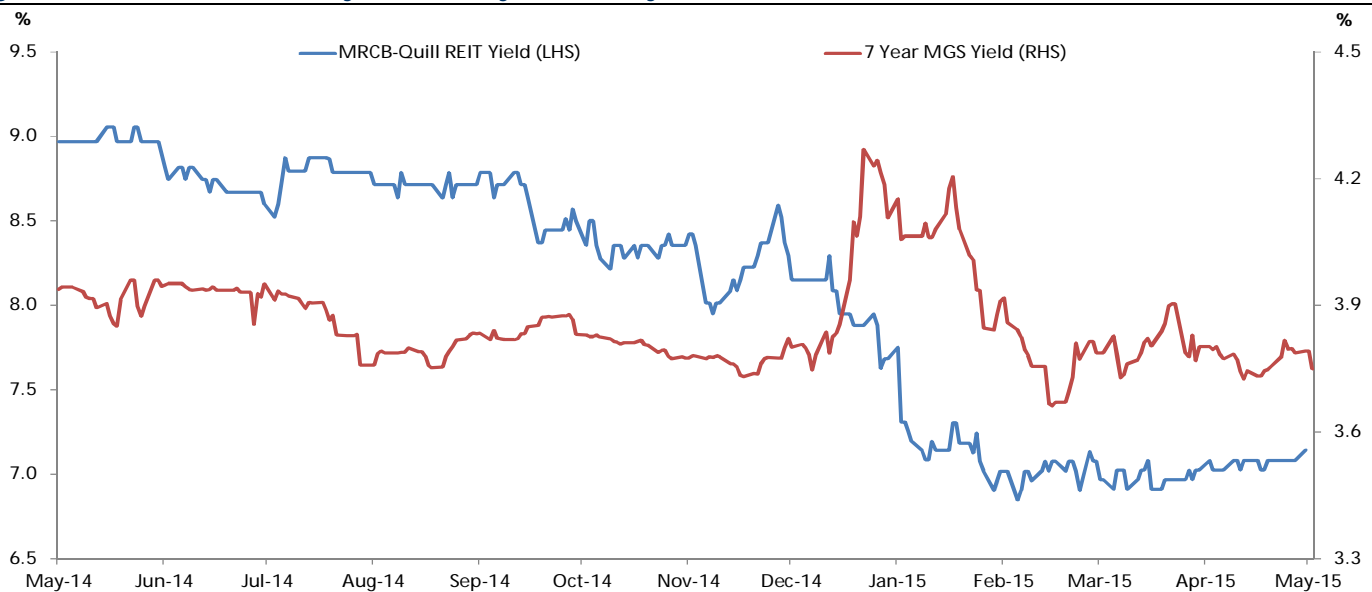
Company Data, HLIB

Figure #8 Peers Comparison

Company	FYE	Price @ 20 May 2015		Market Cap (m)	P/E (x)		P/B (x)		Gross DY (%)
					2014	2015	2014	2015	2014
Amanah Harta Tanah PNB	Dec	MYR	1.07	107.0	NA	NA	NA	NA	NA
Al-Aqar Healthcare REIT	Dec	MYR	1.33	926.0	14.9	14.8	1.1	1.1	6.3
AmFIRST Real Estate Investment Trust	Mar	MYR	0.95	648.6	11.8	10.5	0.8	0.8	7.4
Amanahraya Real Estate Investment Trust	Dec	MYR	0.93	530.2	11.6	11.6	0.9	0.9	8.6
Atrium Real Estate Investment Trust	Dec	MYR	1.16	141.3	11.6	11.6	0.9	0.9	8.6
Axis Real Estate Investment Trust	Dec	MYR	3.51	1,922.6	17.5	17.0	1.5	1.5	5.5
CapitaMalls Malaysia Trust	Dec	MYR	1.46	2,597.3	16.4	15.2	1.1	1.1	6.0
Hektar Real Estate Investment Trust	Dec	MYR	1.54	617.0	12.8	12.8	1.0	1.0	7.1
IGB Real Estate Investment Trust	Dec	MYR	1.35	4,670.1	19.0	18.2	1.3	1.2	5.7
KLCCP Stapled Group	Dec	MYR	7.28	13,142.8	18.8	18.1	1.4	1.4	4.8
Pavilion Real Estate Investment Trust	Dec	MYR	1.55	4,674.7	19.6	18.9	1.3	1.3	5.2
MRCB-Quill REIT	Dec	MYR	1.16	767.2	13.3	12.2	0.8	0.9	7.3
YTL Hospitality REIT	Jun	MYR	1.05	1,390.6	11.7	11.7	0.8	0.7	8.6
Sunway Real Estate Investment Trust	Jun	MYR	1.69	4,961.1	19.9	17.2	1.3	1.3	5.0
Tower Real Estate Investment Trust	Dec	MYR	1.27	356.2	10.6	10.6	0.7	0.7	9.4
UOA Real Estate Investment Trust	Dec	MYR	1.60	676.6	13.3	13.3	1.1	1.1	7.5
Average					14.9	14.9	1.1	1.1	6.9

HLIB, Bloomberg

Figure #9 MRCB - Quill yield vs. 7 year MGS yield



HLIB, Bloomberg

MRCB – Quill REIT (BUY, TP: RM1.34, CP: RM1.16)

Income Statement

FYE Dec (RM m)	2013A	2014A	2015E	2016E	2017E
Gross rental income	57.4	59.3	116.1	120.4	124.9
Car park income	3.5	5.2	3.7	3.9	4.0
Other revenue	8.0	5.7	8.5	8.8	9.0
Total Revenue	68.9	70.2	128.3	133.0	137.9
Assessment & quit rent	(2.8)	(2.8)	(5.8)	(6.0)	(6.3)
Depreciation	(0.0)	0.0	(0.0)	(0.0)	(0.0)
Insurance	(0.4)	(0.4)	(0.8)	(0.8)	(0.9)
Property management fees	(2.0)	(2.0)	(3.9)	(4.0)	(4.1)
Service contracts	(4.1)	(4.7)	(7.0)	(7.2)	(7.5)
Utilities	(6.5)	(7.0)	(10.4)	(10.8)	(11.2)
Total Opex	(15.7)	(16.9)	(27.9)	(28.9)	(30.0)
Net property income	53.2	53.3	100.4	104.1	107.9
Net investment income	56.1	60.2	101.0	105.6	109.3
Pretax profit	36.6	34.2	56.9	61.2	64.5
Taxation	0.0	0.0	0.0	0.0	0.0
Net profit	36.6	34.2	56.9	61.2	64.5
No of units (m)	390.1	390.1	661.4	661.4	661.4
EPU (sen)	9.4	8.8	8.6	9.2	9.8

Cash Flows

FYE Dec (RM m)	2013A	2014A	2015E	2016E	2017E
PBT	40.1	40.3	56.9	61.2	64.5
Finance costs	13.9	(14.1)	0.0	0.0	0.0
Depreciation	0.0	0.0	0.0	0.0	0.0
Fair value gain of assets	(5.6)	(6.1)	0.0	0.0	0.0
Interest income	(0.7)	(0.7)	0.0	0.0	0.0
Others	(20.2)	11.7	9.9	0.6	0.6
Operating cashflow	27.5	31.1	66.8	61.8	65.2
Capex	(0.0)	(6.0)	(740.0)	(2.0)	(2.0)
Disposal / (purchase)	(0.0)	(16.7)	(0.0)	(0.0)	(0.0)
Others	0.0	0.0	0.0	0.0	0.0
Investing Cashflow	(0.0)	(5.3)	(740.0)	(2.0)	(2.0)
Distribution paid	(32.8)	(32.7)	(56.9)	(61.2)	(64.5)
Proceeds from borrowings	0.0	15.0	430.0	0.0	0.0
Repayment of borrowings	0.0	(15.0)	0.0	0.0	0.0
Financing cashflow	0.0	0.0	342.0	0.0	0.0
Net cash flow	(32.8)	(46.7)	715.1	(61.2)	(64.5)

Balance Sheet

FYE Dec (RM m)	2013A	2014A	2015E	2016E	2017E
PPE	0.0	0.0	0.0	0.0	0.0
Investment properties	820.5	837.7	1,577.7	1,579.7	1,581.7
Derivatives	0.0	1.2	1.2	1.2	1.2
Non-current assets	820.5	838.9	1,579.0	1,581.0	1,583.0
Trade receivables	8.9	6.1	5.1	5.3	5.5
Cash	30.5	8.4	65.2	63.8	62.4
Total Current Assets	39.7	29.4	70.3	69.1	67.9
Total assets	860.2	868.4	1,649.3	1,650.0	1,650.9
Unitholders' capital	411.7	411.7	753.7	753.7	753.7
Undistributed profit	117.1	129.5	129.5	129.5	129.5
Total Equity	528.8	541.3	883.3	883.3	883.3
Borrowings	305.5	305.1	735.1	735.1	735.1
Security Deposits	14.5	7.5	9.8	9.8	9.8
Derivatives	0.0	305.1	0.0	0.0	0.0
Trade payables	11.3	12.2	21.1	21.9	22.7
Total liabilities	331.4	327.1	766.0	766.8	767.6
Total liabilities & equity	860.2	868.4	1,649.3	1,650.0	1,650.9

Valuation Ratios

FYE Dec (RM m)	2013A	2014A	2015E	2016E	2017E
EPU before mgr's fee	10.8	11.7	10.0	10.7	11.2
EPU after mgr's fee	9.4	10.3	8.6	9.2	9.8
PER (x)	12.3	11.2	13.5	12.5	11.9
No of units	390.1	390.1	661.4	661.4	661.4
Net DPU	8.4	8.4	8.6	9.2	9.8
Net DY (%)	7.2	7.2	7.4	8.0	8.4
NTA/ share (sen)	136.0	137.7	132.8	132.6	132.5
P/NTA (x)	0.9	0.8	0.9	0.9	0.9
FCF/ share (sen)	18.4	17.9	13.9	18.9	19.9
FCF yield (%)	15.9	15.4	12.0	16.3	17.2
Enterprise value	726.5	734.4	1,437.1	1,438.6	1,439.9
EV/ EBITDA (x)	31.6	28.0	63.5	53.5	47.6
ROE (%)	6.9	7.4	6.4	6.9	7.3
Net gearing (x)	0.3	0.3	0.4	0.4	0.4
Total gearing (x)	0.4	0.4	0.4	0.4	0.4
BVPS (RM)	1.4	1.4	1.3	1.3	1.3
P/B (x)	0.8	0.8	0.9	0.9	0.9

Assumption metrics

Gross Rental Income	2015E	2016E	2017E
Quill Building 1 - DHL 1	4.7	4.8	4.9
Quill Building 4 - DHL 2	5.0	5.1	5.3
Quill Building 2 - HSBC	9.3	9.5	9.8
Quill Building 3 - BMW	4.8	5.0	5.1
Wisma Technip	11.8	12.0	12.3
Part of Plaza Mont' Kiara	3.7	3.8	3.9
Quill Building 5 - IBM	3.7	3.8	3.9
Quill Building 6 - DHL XPJ	3.0	3.1	3.2
Quill Building 10 - Section 13	0.0	0.0	0.0
Tesco Building - Penang	13.9	14.2	14.6
Platinum Sentral	56.2	59.0	62.0
Total	116.1	120.4	124.9

Quarterly Financial Summary

FYE Dec (RM m)	1Q14	4Q14	1Q15	YoY (%)	QoQ (%)
Gross revenue	17.18	18.18	18.61	8.29	2.34
Property operating expenses	(4.17)	(4.77)	(4.93)	18.16	3.36
Net property income	13.01	13.41	13.68	5.12	1.98
Interest income	0.11	0.10	0.13	10.94	28.28
Revaluation gains	0.00	6.12	0.00	NM	NM
Net investment income	13.13	19.63	13.81	5.17	(29.68)
Finance costs	(3.43)	(3.45)	(3.54)	3.12	2.45
Valuation fees	(0.05)	(0.05)	(0.05)	(0.00)	(0.01)
Administrative expenses	(0.14)	(0.08)	(0.19)	37.56	155.22
Total Expenses	(4.96)	(5.01)	(5.53)	11.33	10.22
Normalised PBT	8.16	8.50	8.28	1.43	(2.58)
Normalised PAT	8.16	8.50	8.28	1.43	(2.58)
EPU after mgmt fee	2.09	2.18	2.09	0.00	(4.13)
DPU (sen)	0.00	4.28	0.00	NM	NM

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Published & Printed by
Hong Leong Investment Bank Berhad (10209-W)
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Equity rating definitions

BUY	Positive recommendation of stock under coverage. Expected absolute return of more than +10% over 12-months, with low risk of sustained downside.
TRADING BUY	Positive recommendation of stock not under coverage. Expected absolute return of more than +10% over 6-months. Situational or arbitrage trading opportunity.
HOLD	Neutral recommendation of stock under coverage. Expected absolute return between -10% and +10% over 12-months, with low risk of sustained downside.
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Industry rating definitions

OVERWEIGHT	The sector, based on weighted market capitalization, is expected to have absolute return of more than +5% over 12-months.
NEUTRAL	The sector, based on weighted market capitalization, is expected to have absolute return between -5% and +5% over 12-months.
UNDERWEIGHT	The sector, based on weighted market capitalization, is expected to have absolute return of less than -5% over 12-months.