

MRCB-Quill REIT (BUY ↔, EPS ↔)

INDUSTRY: NEUTRAL
EARNINGS EVALUATION
26 January 2016
Target Price: RM1.29 (↔)
Share Price: RM1.08

FY15 Results: Growing Steadily

Results

- FY15 gross revenue of RM115.2m (+64% yoy) was translated into normalised net profit of RM53.43m (+56.4% yoy), accounting for 99.5% and 101.4% of HLIB and consensus FY forecasts, respectively.

Deviations

- None.

Dividends

- Declared 2HFY15 dividend of 4.37 sen (2014: 4.28 sen) and full year dividend of 8.47 sen accounting for 98.4% of our full year DPU assumptions at a yield of 7.84%, albeit at a lower payout ratio circa 94% vs 96% in FY14.

Highlights

- Encouraging results in FY15 with additional income post Platinum Sentral acquisition, higher rental reversion from other properties, and cost savings from Platinum Sentral.
- Overall occupancy rate improved to 97.5% with another record high of NPI margin at 82.2% as compared to previous high at 80.1% in Q3 (Figure #5), thanks to cost savings measure from Platinum Sentral.
- 94% of the leases due in 2015 (430k sqft.) has been renewed and 70% of the remaining non-renewed space has been taken up by new lessee. This translated to only ~0.48% of the total NLA (~8160 sqft) not being renewed.
- Ongoing acquisition of Menara Shell is expected to complete in Q1FY16. Assuming 9m contribution, it will contribute additional 29% of rental income to our FY16 forecasted rental income.
- Despite challenging outlook for 2016, only 7% of the NLA is due for renewal, hence, active acquisition activities are expected to pursue for non-organic growth to add to its ever growing NAV at RM1.6bn.
- We reiterate our **BUY** recommendation on MQREIT given the consistent high DPU yield (>7%) and huge assets injection in the pipeline from its sponsor.

Risks

- High gearing compare to industry average.
- Slow rental reversion rate.

Forecasts

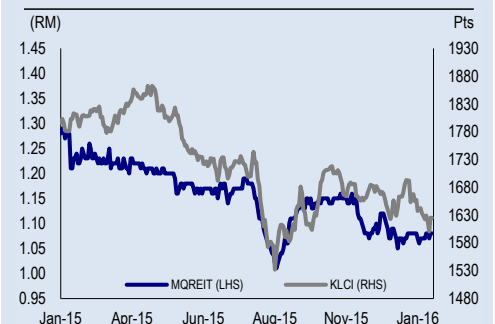
- Unchanged.

Rating
BUY ↔, TP: RM1.29 ↔
Valuation

- Maintain **BUY** recommendation with unchanged TP of **RM1.29**.
- Our valuation was pegged to targeted yield of 6.94% based on 2SD below 1 year historical average yield spread of MRCB-Quill REIT and 10-year government bond in view of high potential for yield accretive injection(s).

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KLCI	1625.2
Expected share price return	19.4%
Expected dividend return	8.3%
Expected total return	27.8%

Share price

Information

Bloomberg Ticker	MQREIT MK
Bursa Code	5123
Issued Shares (m)	5123
Market cap (RM m)	661
3-mth avg. volume ('000)	714
SC Shariah-compliant	No

Price Performance	1M	3M	12M
Absolute	0.9	-6.1	-15.0
Relative	3.3	-1.1	-5.7

Major Shareholders

Capita Commercial Trust	17.7%
Quill Group	17.7%

Summary Earnings Table

FYE Dec (RMm)	2014A	2015A	2016E	2017E
Revenue	115.2	115.2	133.0	137.9
NPI	53.2	90.3	102.5	106.3
Net invest income	56.1	98.5	103.9	107.7
PAT	36.6	60.7	62.5	66.2
EPU (sen)	10.3	10.2	9.5	10.0
Norm. PER (x)	10.5	10.6	11.4	10.8
FD PER (x)	10.5	10.6	11.4	10.8
EV/ EBITDA (x)	26.8	39.4	42.1	37.8
Net DPU (sen)	8.4	8.5	9.0	9.5
Distb. yield (%)	7.8	7.8	8.3	8.8
BVPS (RM)	1.4	1.5	1.4	1.4
P/B (x)	0.8	0.7	0.8	0.8

HLIB

Figure #1 Quarterly Results Comparison

FYE Dec (RMm)	4Q14	3Q15	4Q15	YoY (%)	QoQ (%)	Comments
Gross revenue	18.18	31.81	32.58	79.17	2.41	Yoy: Higher revenue attributable to contribution from newly-acquired Platinum Sentral, higher revenue from Plaza Mont's Kiara and higher rental rates for other properties. Qoq: Higher rental reversion kicked in during current quarter.
Property operating expenses	(4.77)	(6.33)	(5.78)	21.29	(8.56)	Yoy: Higher operating expenses attributable to acquisition of Platinum Sentral. Qoq: Lower by 8.6% due to cost savings from Platinum Sentral.
Net property income	13.41	25.49	26.79	99.74	5.13	
Interest income	0.10	0.35	0.31	213.46	(12.79)	Yoy: Higher by 213.5% due to higher bank balances in the current quarter. Qoq: Lower due to lower bank balance after payment of income distribution in previous quarter.
Gain on divestment	0.00	0.59	0.00	NM	(100.00)	
Net investment income	19.63	26.43	33.78	72.05	27.79	
Finance costs	(3.45)	(8.32)	(7.94)	129.93	(4.55)	Yoy: Higher by 129.9% due to interest on additional borrowings drawdown on 30 Mac 2015. Qoq: Lower due to reduction in borrowings by RM30m in 4Q2015.
Valuation fees	(0.05)	(0.05)	(0.10)	111.58	111.59	
Administrative expenses	(0.08)	0.20	(0.07)	(7.44)	NM	
Total Expenses	(5.01)	(10.70)	(10.73)	113.91	0.26	
Normalised PBT	8.50	15.14	16.37	92.69	8.16	
Normalised PAT	8.50	15.14	16.37	92.69	8.16	
EPU (realised)	2.18	2.29	2.48	13.66	8.16	
DPU (sen)	4.28	0.00	4.37	2.10	NM	

Company Data, HLIB

Figure #2 Cumulative Results Comparison

FYE Dec (RMm)	FY14	FY15	YoY (%)	Comments
Gross revenue	70.25	115.17	63.95	Higher attributable to additional revenue arising from the acquisition of Platinum Sentral on 30 Mac 2015, higher revenue from Plaza Mont's Kiara and higher rental rates for other properties.
Property operating expenses	(16.92)	(24.90)	47.14	Higher due to acquisition of Platinum Sentral and higher repairs and maintenance expenses for Plaza Mont Kiara.
Net property income	53.33	90.27	69.29	
Interest income	0.72	0.93	28.07	
Gain on divestment	0.00	0.59	NM	
Net investment income	60.17	98.47	63.66	
Finance costs	(14.05)	(27.98)	99.12	Higher due to financial drawdown.
Valuation fees	(0.19)	(0.24)	27.89	
Administrative expenses	0.05	(0.38)	NM	Higher due to write back of over-accrued professional fee in the preceding year.
Total Expenses	(19.89)	(37.77)	89.87	
Normalised PBT	34.15	53.43	56.42	
Normalised PAT	34.15	53.43	56.42	Higher net property income, net cost and expense, exclude gain on divestment of QB10.
EPU (realised)	8.75	9.05	3.43	
DPU (sen)	8.38	8.47	1.07	

Company Data, HLIB

Figure #3 FY15 Results vs. HLIB's Estimates and Consensus

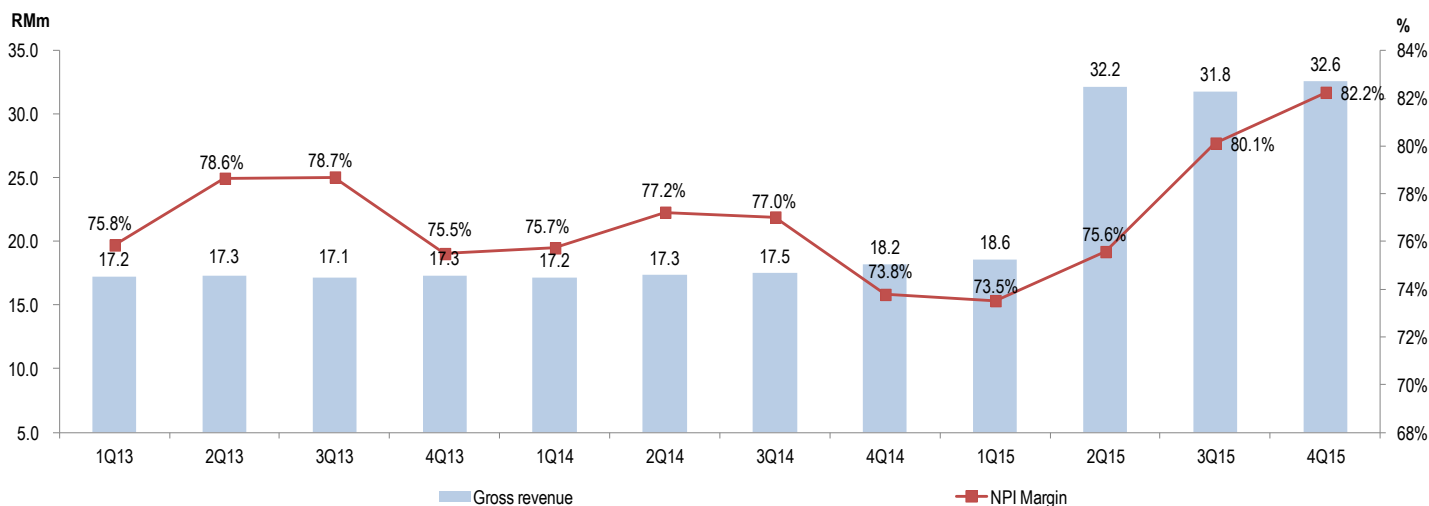
	Actual FY15	HLIB FY15	Actual vs. HLIB (%)	Consensus FY15	Actual vs. Consensus (%)	Comments
Revenue	115.2	114.3	100.8	111.8	103.1	In line.
Normalised PAT	53.4	53.7	99.5	52.7	101.4	In line.
EPU (sen)	9.1	9.1	100.0	9.7	93.3	In line.
DPU (sen)	8.5	8.6	98.4	8.2	103.3	In line.

Company Data, HLIB, Bloomberg

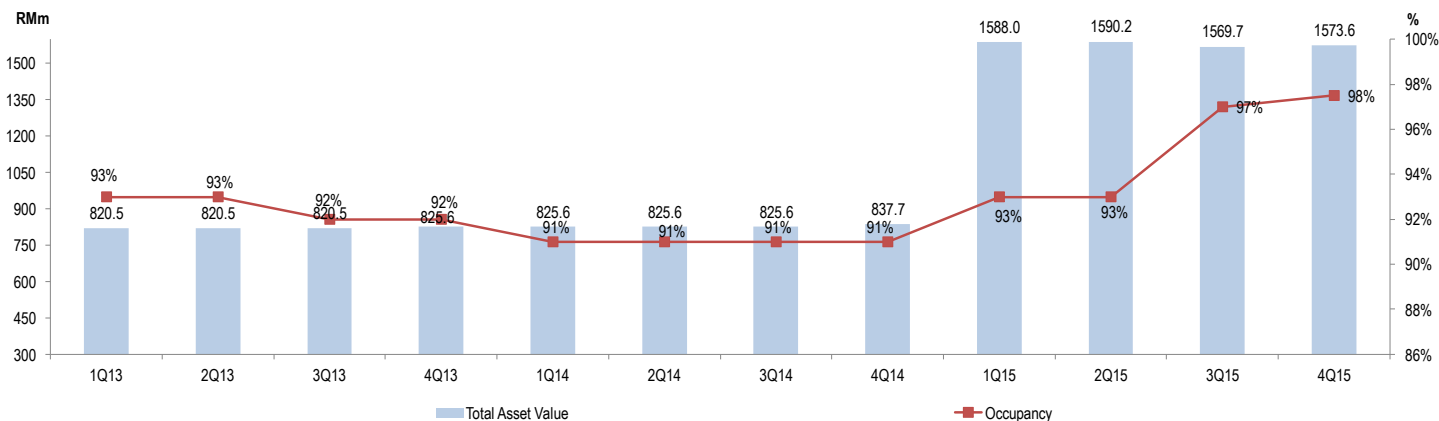
Figure #4 HLIB Forecasts vs. Consensus

RMm	FY16E			FY17E		
	HLIB	Consensus	%	HLIB	Consensus	%
Normalised PAT	62.5	54.1	15.7	66.2	56.2	17.9
DPU (sen)	9.0	8.4	7.0	9.5	8.8	8.1

HLIB, Bloomberg

Figure #5 Gross Revenue & NPI Margin

HLIB, Bloomberg

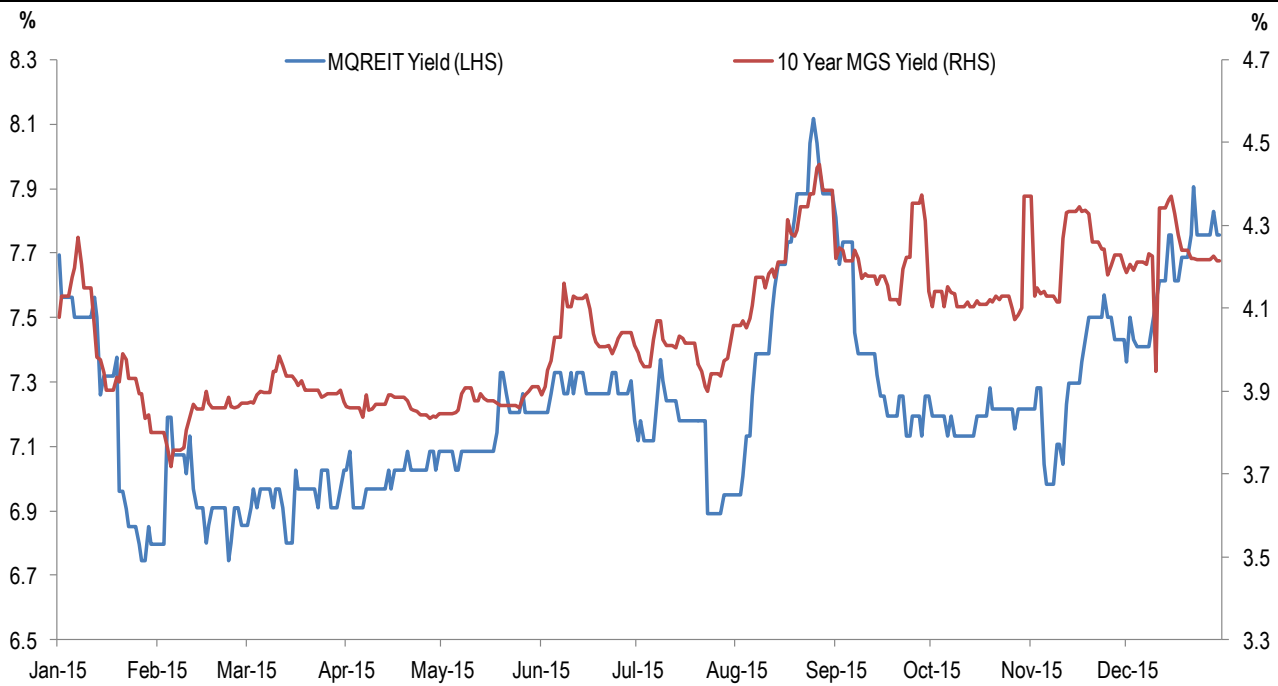
Figure #6 Total Asset Value & Occupancy

HLIB, Bloomberg

Figure #7 Peers Comparison

Company	FYE	Price	Market Cap (m)	P/E (x)		P/B (x)		Gross DY (%)
				2015	2016	2015	2016	2015
Amanah Harta Tanah PNB	Dec	MYR 1.01	101.0	NA	NA	NA	NA	NA
Al-'Aqar Healthcare REIT	Dec	MYR 1.41	1,026.8	17.6	15.7	1.2	1.2	5.7
AmFIRST Real Estate Investment Trust	Mar	MYR 0.71	487.3	11.8	10.1	0.6	0.6	8.5
Amanahraya Real Estate Investment Trust	Dec	MYR 0.86	493.0	12.3	12.3	0.7	0.7	8.1
Atrium Real Estate Investment Trust	Dec	MYR 1.09	132.8	10.9	10.9	0.8	0.8	9.2
Axis Real Estate Investment Trust	Dec	MYR 1.57	1,726.7	17.1	17.1	1.2	1.2	5.6
CapitaMalls Malaysia Trust	Dec	MYR 1.42	2,875.2	16.0	15.3	1.0	1.0	6.2
Hektar Real Estate Investment Trust	Dec	MYR 1.52	609.0	12.7	12.7	1.0	1.0	7.2
IGB Real Estate Investment Trust	Dec	MYR 1.36	4,721.6	18.0	16.7	1.3	1.3	5.6
KLCCP Stapled Group	Dec	MYR 7.00	12,637.3	18.2	17.6	2.5	2.3	4.9
MRCB-Quill Real Estate Investment Trust	Dec	MYR 1.08	714.3	11.9	11.4	0.7	0.8	7.7
Pavilion Real Estate Investment Trust	Dec	MYR 1.58	4,768.2	19.8	18.1	1.3	1.3	5.0
Al-Salam Real Estate Investment Trust	Mar	MYR 0.97	562.6	NA	NA	NA	NA	5.5
Sunway Real Estate Investment Trust	Jun	MYR 1.45	4,264.7	15.6	15.1	1.2	1.2	6.7
Tower Real Estate Investment Trust	Dec	MYR 1.23	345.0	10.3	10.3	0.7	0.7	9.8
UOA Real Estate Investment Trust	Dec	MYR 1.61	680.8	13.4	13.4	1.1	1.1	7.5
YTL Hospitality REIT	Jun	MYR 1.04	1,377.4	13.0	14.9	0.7	0.9	5.8
Average				14.6	14.1	1.1	1.1	6.8

HLIB, Bloomberg

Figure #8 MRCB-Quill yield vs. 10 year MGS yield

HLIB, Bloomberg

MRCB-Quill REIT (BUY, TP: RM1.29, CP: RM1.08)**Income Statement**

FYE Dec (RM m)	2014A	2015A	2016E	2017E	2018E
Gross rental income	59.3	102.0	120.4	124.9	129.6
Car park income	5.2	3.7	3.9	4.0	4.1
Other revenue	5.7	8.5	8.8	9.0	9.3
Total Revenue	115.2	115.2	133.0	137.9	142.9
Assessment & quit rent	(2.8)	(4.8)	(5.7)	(5.9)	(6.1)
Depreciation	0.0	(0.0)	(0.0)	(0.0)	(0.0)
Insurance	(0.4)	(0.7)	(0.8)	(0.9)	(0.9)
Property management fees	(2.0)	(3.1)	(3.9)	(4.0)	(4.1)
Service contracts	(4.7)	(7.1)	(8.5)	(8.9)	(9.2)
Utilities	(7.0)	(9.2)	(11.6)	(12.0)	(12.4)
Total Opex	(24.9)	(24.9)	(30.5)	(31.6)	(32.8)
Net property income	90.3	90.3	102.6	106.3	110.2
Net investment income	98.5	98.5	103.9	107.7	111.7
Pretax profit	53.4	60.7	62.5	66.2	70.8
Taxation	0.0	0.0	0.0	0.0	1.0
Net profit	53.4	60.7	62.5	66.2	70.8
No of units (m)	390.1	596.0	661.4	661.4	661.4
EPU (sen)	8.8	9.0	9.5	10.0	10.7

Cash Flows

FYE Dec (RM m)	2014A	2015A	2016E	2017E	2018E
PBT	40.3	60.7	62.5	66.2	70.8
Finance costs	14.1	28.0	0.0	0.0	0.0
Depreciation	0.0	0.0	0.0	0.0	0.0
Fair value gain of assets	(6.1)	(7.3)	0.0	0.0	0.0
Interest income	(0.7)	(0.9)	0.0	0.0	0.0
Others	(16.4)	(21.5)	2.1	0.4	0.4
Operating cashflow	31.1	59.0	64.7	66.6	71.2
Capex	(6.0)	(751.9)	(2.0)	(2.0)	(2.0)
Disposal / (purchase)	(0.0)	(0.2)	(0.0)	(0.0)	(0.0)
Others	0.0	24.9	0.0	0.0	0.0
Investing Cashflow	(6.0)	(727.3)	(2.0)	(2.0)	(2.0)
Distribution paid	(32.7)	(38.7)	(59.4)	(62.9)	(67.2)
Proceeds from borrowings	15.0	534.0	190.0	0.0	100.0
Repayment of borrowings	(15.0)	(145.0)	(190.0)	0.0	(117.0)
Financing cashflow	0.0	342.0	0.0	0.0	0.0
Net cash flow	(32.7)	350.3	(59.4)	(62.9)	(84.2)

Balance Sheet

FYE Dec (RM m)	2014A	2015A	2016E	2017E	2018E
PPE	0.0	0.2	0.2	0.3	0.3
Investment properties	837.7	1,569.8	1,571.8	1,573.8	1,575.8
Derivatives	1.2	1.6	1.6	1.6	1.6
Non-current assets	838.9	1,571.6	1,573.6	1,575.7	1,577.7
Trade receivables	6.1	5.7	6.7	6.9	7.1
Cash	23.3	44.9	48.1	49.8	34.7
Total Current Assets	29.4	51.3	55.4	57.3	42.5
Total assets	868.4	1,622.9	1,629.1	1,633.0	1,620.2
Unitholders' capital	411.7	751.3	751.3	751.3	751.3
Undistributed profit	129.5	152.6	155.7	159.0	162.6
Total Equity	541.3	903.9	907.0	910.3	913.8
Borrowings	305.1	689.7	689.7	689.7	672.7
Security Deposits	9.8	18.1	18.1	18.1	18.1
Derivatives	0.0	0.0	0.0	0.0	0.0
Trade payables	12.2	13.6	16.7	17.3	18.0
Total liabilities	327.1	721.5	724.5	725.1	708.8
Total liabilities & equity	868.4	1,625.3	1,631.5	1,635.4	1,622.6

Valuation Ratios

FYE Dec (RM m)	2014A	2015A	2016E	2017E	2018E
EPU before mgr's fee	11.7	11.6	10.9	11.5	12.2
EPU after mgr's fee	10.3	10.2	9.5	10.0	10.7
PER (x)	10.5	10.6	11.4	10.8	10.1
No of units	390.1	596.0	661.4	661.4	661.4
Net DPU	8.4	8.5	9.0	9.5	10.2
Net DY (%)	7.8	7.8	8.3	8.8	9.4
NTA/ share (sen)	137.7	151.0	136.2	136.6	137.0
P/NTA (x)	0.8	0.7	0.8	0.8	0.8
FCF/ share (sen)	17.9	16.2	19.1	19.9	23.8
FCF yield (%)	16.6	15.0	17.7	18.4	22.0
Enterprise value	703.2	1,288.5	1,355.9	1,354.2	1,352.3
EV/ EBITDA (x)	26.8	39.4	42.1	37.8	32.8
ROE (%)	7.4	6.7	6.9	7.3	7.7
Net gearing (x)	0.3	0.4	0.4	0.4	0.4
Total gearing (x)	0.4	0.4	0.4	0.4	0.4
BVPS (RM)	1.4	1.5	1.4	1.4	1.4
P/B (x)	0.8	0.7	0.8	0.8	0.8

Assumption metrics

Gross Rental Income	2016E	2017E	2018E
Quill Building 1 - DHL 1	4.8	4.9	5.0
Quill Building 4 - DHL 2	5.1	5.3	5.4
Quill Building 2 - HSBC	9.5	9.8	10.0
Quill Building 3 - BMW	5.0	5.1	5.2
Wisma Technip	12.0	12.3	12.7
Part of Plaza Mont' Kiara	3.8	3.9	4.0
Quill Building 5 - IBM	3.8	3.9	4.0
Quill Building 6 - DHL XPJ	3.1	3.2	3.3
Quill Building 10 - Section 13	0.0	0.0	0.0
Tesco Building - Penang	14.2	14.6	14.9
Platinum Sentral	59.0	62.0	65.1
Total	120.4	124.9	129.6

Quarterly Financial Summary

FYE Dec (RM m)	4Q14	3Q15	4Q15	YoY (%)	QoQ (%)
Gross revenue	18.2	31.8	32.6	79.2	2.4
Property operating expenses	(4.8)	(6.3)	(5.8)	21.3	(8.6)
Net property income	13.4	25.5	26.8	99.7	5.1
Interest income	0.1	0.4	0.3	213.5	(12.8)
Revaluation gains	6.1	0.0	6.7	9.1	NM
Net investment income	19.6	26.4	33.8	72.1	27.8
Finance costs	(3.5)	(8.3)	(7.9)	129.9	(4.5)
Valuation fees	(0.0)	(0.0)	(0.1)	111.6	111.6
Administrative expenses	(0.1)	0.2	(0.1)	(7.4)	(134.9)
Total Expenses	(5.0)	(10.7)	(10.7)	113.9	0.3
Normalised PBT	8.5	15.1	16.4	92.7	8.2
Normalised PAT	8.5	15.1	16.4	92.7	8.2
EPU after mgmt fee	2.2	2.3	2.5	13.7	8.2
DPU (sen)	4	0	4	2	NM

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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.
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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.