

MRCB-Quill REIT (BUY ↔, EPS ↔)

INDUSTRY: NEUTRAL
EARNINGS EVALUATION

5 May 2017
Target Price: RM1.45 (↑)
Share Price: RM1.32

A good start to FY17

Results

- Reported 1QFY17 gross revenue of RM45.6m (+33.7% qoq, +39.5% yoy) which translated to normalised net profit of RM23.2m (+73.2% qoq, +52.0% yoy), accounting for 26.9% and 25.9% of HLIB and consensus forecasts, respectively.

Deviations

- None.

Dividends

- No dividend was declared as the dividend is paid on a half yearly basis.

Highlights

- YoY:** Higher profit (+52%) recorded on the back of additional revenue from the newly acquired Menara Shell and higher rental income due to step up rent adjustments from QB2, QB3 and Wisma Technip.
- QoQ:** Profit grew by 73.2% mainly due to additional income from Menara Shell and higher rental income from QB2 and Wisma Technip.
- Overall occupancy rate slightly reduced to 97% (from 98%) but still remained healthy. Meanwhile, 2% of total lease expiry in FY17 (14% of total NLA) has been renewed.
- MQREIT has completed the refinancing of RM190m borrowings in March 2017. As a result, the average debt to maturity has improved to 2.91 years (from 2.69 years) while average cost of debt (4.4% p.a.) is maintained. The gearing level of MQREIT remained unchanged at 37% which is still below the limit of 50%.
- With the acquisition of Menara Shell, asset size has ballooned to RM2.27bn from RM837m in 2014. The increase in asset size allowed management to enjoy greater operating efficiency arising from economies of scale.
- Outlook:** Despite the lacklustre overall office market, MQREIT's performance is expected to remain stable due to its healthy occupancy rate and long WALE (5.6 years) with well-spread NLA expiry (26% and 13% expiring in FY18 and FY19, respectively).

Risks

- High gearing compare to industry average.
- Slower rental reversion rate for office market.

Forecasts

- Unchanged.

Rating

BUY ↔, TP: RM1.45 ↑

- We continue to like MQREIT given its high dividend yield (highest among REITs in our universe), stable assets in prime location of KL Sentral with high occupancy rate and healthy WALE profile. The larger portfolio size allows MQREIT to enjoy greater operating efficiency arising from economies of scale.

Valuation

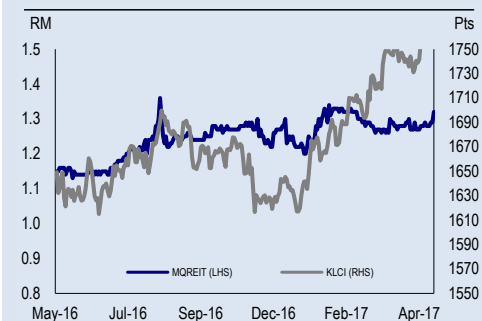
- Maintain **BUY** with higher TP of **RM1.45** as we roll forward our valuation horizon from FY17 to FY18 with unchanged targeted yield of 6.2%.

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KLCI	1758.7
Expected share price return	9.8%
Expected dividend return	6.6%
Expected total return	16.4%

Share price



Information

Bloomberg Ticker	MQREITMK
Bursa Code	5123
Issued Shares (m)	1,068
Market cap (RM m)	1,410
3-mth avg. volume ('000)	387
SC Shariah-compliant	No

Price Performance	1M	3M	12M
Absolute	3.1	-0.8	19.6
Relative	2.3	-4.9	11.9

Major Shareholders

MRCB	27.9%
Capita Commercial Trust	11.0%
EPF	7.3%
Quill Estates SB	5.2%

Summary Earnings Table

FYE Dec (RMm)	2016A	2017E	2018F	2019F
Revenue	136.6	185.3	189.1	192.9
NPI	107.2	138.5	141.3	144.1
Netinvestincome	108.2	140.1	142.5	144.8
PAT	62.8	86.1	89.3	91.5
EPD (sen)	9.3	8.0	8.3	8.4
Norm. PER (x)	14.9	16.3	15.9	15.6
FD PER (x)	14.9	16.3	15.9	15.6
EV/EBITDA (x)	18.2	18.0	17.7	17.5
NetDPU (sen)	8.4	8.7	9.0	9.1
Distrib. yield (%)	6.4	6.6	6.9	6.9
BVPS (RM)	2.0	1.3	1.3	1.3
P/B (x)	0.6	1.0	1.0	1.0
HLIB				

Figure #1 Quarterly Results Comparison

FYE Dec (RMm)	1Q16	4Q16	1Q17	QoQ (%)	YoY (%)	Comments
Gross revenue	32.7	34.1	45.6	33.7	39.5	Higher due to additional revenue from Menara Shell and higher rental income post rent adjustment from QB2, QB3 and Wisma Technip.
Property operating expenses	-7.2	-8.5	-9.4	-11.7	-30.9	Higher due to acquisition of Menara Shell.
Net property income	25.4	30.5	36.1	18.5	42.0	
Interest income	0.4	1.1	0.5	-60.3	16.1	
Gain on divestment	0.0	0.0	0.0	NM	NM	
Net investment income	25.8	30.3	36.6	20.7	41.6	
Finance costs	-7.9	-9.1	-9.7	-6.9	-23.8	Increase due to higher borrowings after the additional borrowings incurred to finance Menara Shell and to refinance existing CP/MTN.
Valuation fees	-0.0	-0.2	-0.0	78.2	-8.9	
Administrative expenses	-0.2	-1.5	-0.1	95.9	61.4	
Total Expenses	-10.6	-13.4	-13.4	-0.2	-26.5	
Normalised PBT	15.2	13.4	23.2	73.2	52.0	
Normalised PAT	15.2	13.4	23.2	73.2	52.0	Higher due to additional revenue from Menara Shell.
EPU (realised)	2.27	1.99	2.17	9.1	-4.2	YoY: Lower due to higher share base from placement exercise.
DPU (sen)	0.00	4.15	0.00	NM	NM	

Company Data, HLIB

Figure #2 FY16 Results vs. HLIB's Estimates and Consensus

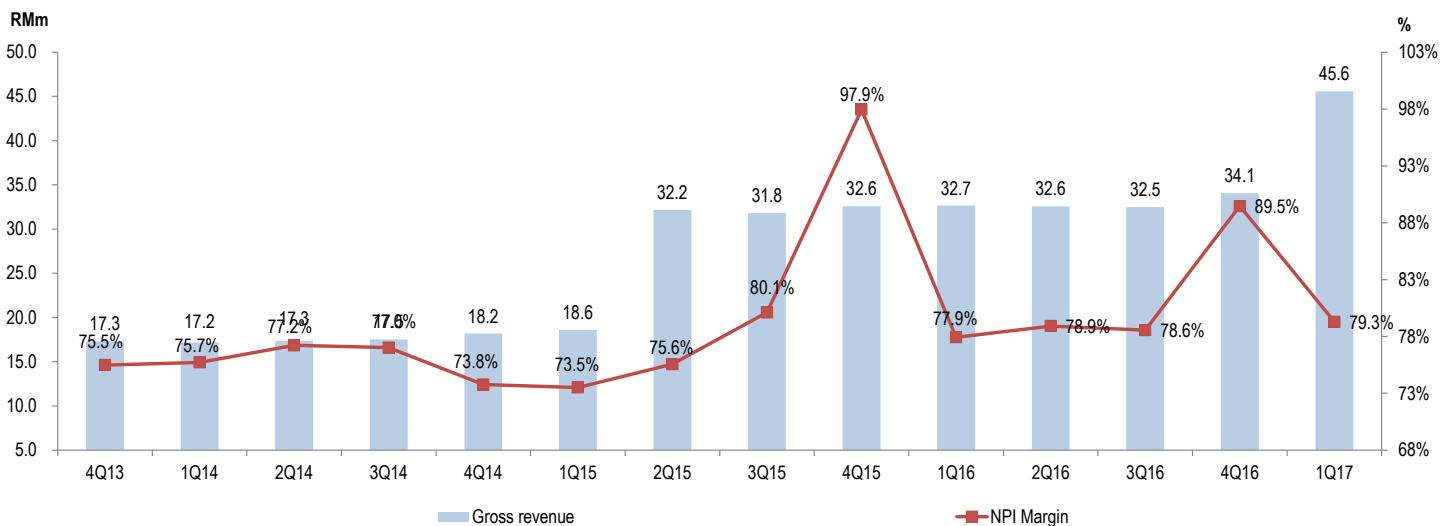
	Actual 1QFY17	HLIB FY17	Actual vs. HLIB (%)	Consensus FY17	Actual vs. Consensus (%)	Comments
Revenue	45.6	185.3	24.6	182.5	25.0	In line.
Normalised PAT	23.2	86.1	26.9	89.3	25.9	In line.
EPU (sen)	2.2	8.0	27.1	8.0	27.1	In line.
DPU (sen)	0.0	8.7	0.0	8.1	0.0	In line.

Company Data, HLIB, Bloomberg

Figure #3 HLIB Forecasts vs. Consensus

RMm	FY18F			FY19F		
	HLIB	Consensus	%	HLIB	Consensus	%
Normalised PAT	89.3	92.9	(4.0)	91.5	96.8	(5.5)
DPU (sen)	9.0	8.3	8.8	9.1	8.3	9.4

HLIB, Bloomberg

Figure #4 Gross Revenue & NPI Margin

HLIB, Bloomberg

Figure #5 Peers Comparison

Company	FYE	Price	Market Cap (m)	P/E (x)		P/B (x)		Gross DY (%)
				2017	2018	2017	2018	2017
Amanah Harta Tanah PNB	Dec	MYR 0.95	207.9	NA	NA	NA	NA	NA
Al-Aqar Healthcare REIT	Dec	MYR 1.54	1,121.5	17.9	NA	1.3	NA	5.5
AmFIRST Real Estate Investment Trust	Mar	MYR 0.78	535.4	NA	NA	NA	NA	NA
Amanahraya Real Estate Investment Trust	Dec	MYR 0.94	538.8	14.9	14.0	NA	NA	5.9
Atrium Real Estate Investment Trust	Dec	MYR 1.14	138.9	NA	NA	NA	NA	NA
Axis Real Estate Investment Trust	Dec	MYR 1.70	1,878.8	19.1	19.5	1.3	1.3	5.1
CapitaMalls Malaysia Trust	Dec	MYR 1.49	3,031.6	18.4	17.7	1.1	1.1	5.8
Hektar Real Estate Investment Trust	Dec	MYR 1.59	637.0	13.8	14.5	1.0	1.2	6.6
IGB Real Estate Investment Trust	Dec	MYR 1.68	5,885.8	21.3	20.2	1.7	1.7	5.4
KLCCP Stapled Group	Dec	MYR 7.91	14,280.2	19.5	18.5	1.0	1.0	4.9
MRCB-Quill Real Estate Investment Trust	Dec	MYR 1.32	1,409.8	14.5	16.7	0.9	1.1	6.4
Pavilion Real Estate Investment Trust	Dec	MYR 1.72	5,205.2	19.8	18.5	1.2	1.2	5.2
Al-Salam Real Estate Investment Trust	Mar	MYR 1.04	603.2	16.0	16.0	1.0	1.0	5.8
Sunway Real Estate Investment Trust	Jun	MYR 1.71	5,036.1	18.8	17.4	1.2	1.2	5.3
Tower Real Estate Investment Trust	Dec	MYR 1.20	336.6	NA	NA	NA	NA	NA
UOA Real Estate Investment Trust	Dec	MYR 1.79	735.8	NA	NA	NA	NA	NA
YTL Hospitality REIT	Jun	MYR 1.19	2,028.2	16.3	15.3	0.9	0.9	6.2
Average				17.5	17.1	1.1	1.2	5.7

HLIB, Bloomberg

MRCB-Quill REIT (BUY, TP: RM1.45, CP: RM1.32)

Income Statement

FYE Dec (RM m)	2015A	2016A	2017E	2018F	2019F
Gross rental income	99.5	115.9	165.8	169.1	172.5
Car park income	10.3	10.3	13.9	14.2	14.4
Other revenue	5.4	5.6	5.7	5.8	5.9
Total Revenue	120.3	136.6	185.3	189.1	192.9
Assessment & quit rent	(4.5)	(5.4)	(7.8)	(7.9)	(8.1)
Depreciation	(0.0)	(0.0)	(0.0)	(0.0)	(0.0)
Insurance	(0.7)	(0.9)	(1.2)	(1.3)	(1.3)
Property management fees	(2.2)	(3.5)	(5.0)	(5.1)	(5.2)
Service contracts	(7.3)	(8.8)	(12.9)	(13.2)	(13.5)
Utilities	(10.2)	(10.9)	(19.9)	(20.3)	(20.7)
Total Opex	(24.9)	(29.5)	(46.8)	(47.8)	(48.7)
Net property income	95.4	107.2	138.5	141.3	144.1
Net investment income	99.1	108.2	140.1	142.5	144.8
Pretax profit	60.7	62.8	86.1	89.3	91.5
Taxation	0.0	0.0	0.0	1.0	2.0
Net profit	53.4	59.2	86.1	89.3	91.5
No of units (m)	596.0	672.5	1,074.1	1,081.3	1,088.4
EPU (sen)	10.2	9.3	8.0	8.3	8.4

Cash Flows

FYE Dec (RM m)	2015A	2016A	2017E	2018F	2019F
PBT	60.7	62.8	86.1	89.3	91.5
Finance costs	28.0	33.0	0.0	0.0	0.0
Depreciation	0.0	0.1	0.0	0.0	0.0
Fair value gain of assets	(7.3)	(3.5)	0.0	0.0	0.0
Interest income	(0.9)	(2.4)	0.0	0.0	0.0
Others	(21.5)	(19.7)	(22.1)	0.3	0.3
Operating cashflow	59.0	70.3	64.1	89.6	91.8
Capex	(751.9)	(647.4)	(2.0)	(2.0)	(2.0)
Disposal / (purchase)	(0.2)	(1.5)	(0.0)	(0.0)	(0.0)
Others	24.9	0.0	0.0	0.0	0.0
Investing Cashflow	(727.3)	(648.9)	(2.0)	(2.0)	(2.0)
Distribution paid	(38.7)	(56.9)	(85.3)	(88.4)	(89.6)
Proceeds from borrowings	534.0	164.0	200.0	100.0	0.0
Repayment of borrowings	(145.0)	0.0	(189.1)	(117.0)	0.0
Placement / New shares	342.0	487.9	0.0	0.0	0.0
Financing cashflow	692.3	595.1	(74.4)	(105.4)	(89.6)

Balance Sheet

FYE Dec (RM m)	2015A	2016A	2017E	2018F	2019F
PPE	0.2	0.2	0.2	0.2	0.2
Investment properties	1,569.8	2,222.0	2,224.0	2,226.0	2,228.0
Others	3.6	2.7	2.7	2.7	2.7
Non-current assets	1,573.6	2,225.0	2,227.0	2,229.0	2,231.0
Trade receivables	6.1	18.3	17.4	17.7	18.1
Cash	44.9	54.1	41.7	24.0	24.1
Total Current Assets	51.7	72.4	59.1	41.7	42.2
Total assets	1,625.3	2,297.3	2,286.1	2,270.6	2,273.1
Unitholders' capital	751.3	1,231.9	1,231.9	1,231.9	1,231.9
Undistributed profit	152.6	127.8	128.6	129.5	131.3
Total Equity	903.9	1,359.7	1,360.6	1,361.5	1,363.3
Borrowings	689.7	851.6	862.5	845.5	845.5
Security Deposits	18.1	29.3	29.3	29.3	29.3
Derivatives	0.0	1.0	1.0	1.0	1.0
Trade payables	13.6	55.8	32.8	33.4	34.1
Total liabilities	721.5	937.6	925.5	909.2	909.9
Total liabilities & equity	1,625.3	2,297.3	2,286.1	2,270.6	2,273.1

Valuation Ratios

FYE Dec (RM m)	2015A	2016A	2017E	2018F	2019F
EPU before mgr's fee	9.0	8.8	8.0	8.3	8.4
EPU after mgr's fee	10.2	9.3	8.0	8.3	8.4
PER (x)	14.6	14.9	16.3	15.9	15.6
No of units	596.0	672.5	1,074.1	1,081.3	1,088.4
Net DPU	8.5	8.4	8.7	9.0	9.1
Net DY (%)	6.5	6.4	6.6	6.9	6.9
NTA/ share (sen)	151.0	201.3	126.0	125.2	124.4
P/NTA (x)	0.9	0.7	1.0	1.0	1.1
FCF/ share (sen)	16.2	19.5	13.1	18.2	16.9
FCF yield (%)	12.3	14.9	10.0	13.9	12.9
Enterprise value	1,425.6	1,678.5	2,227.8	2,237.9	2,247.2
EV/ EBITDA (x)	17.4	18.2	18.0	17.7	17.5
ROE (%)	6.7	4.6	6.3	6.6	6.7
Net gearing (x)	0.4	0.3	0.4	0.4	0.4
Total gearing (x)	0.4	0.4	0.4	0.4	0.4
BVPS (RM)	1.5	2.0	1.3	1.3	1.3
P/B (x)	0.9	0.6	1.0	1.0	1.0

Assumption metrics

Gross Rental Income	2017E	2018F	2019F
Quill Building 1 - DHL 1	4.8	4.9	5.0
Quill Building 4 - DHL 2	5.2	5.3	5.4
Quill Building 2 - HSBC	9.6	9.8	10.0
Quill Building 3 - BMW	5.0	5.1	5.2
Wisma Technip	12.2	12.4	12.7
Part of Plaza Mont' Kiara	3.9	4.0	4.1
Quill Building 5 - IBM	3.9	4.0	4.0
Quill Building 6 - DHL XPJ	3.1	3.2	3.3
Tesco Building - Penang	14.4	14.6	14.9
Platinum Sentral	56.5	57.6	58.8
Menara Shell	47.2	48.1	49.1
Total	165.8	169.1	172.5

Quarterly Financial Summary

FYE Dec (RM m)	1Q16	4Q16	1Q17	QoQ (%)	YoY (%)
Gross revenue	32.7	34.1	45.6	33.7	39.5
Property operating expenses	(7.2)	(8.5)	(9.4)	(11.7)	(30.9)
Net property income	25.4	30.5	36.1	18.5	42.0
Interest income	0.4	1.1	0.5	(60.3)	16.1
Revaluation gains	0.0	3.5	0.0	(100.0)	NM
Net investment income	25.8	30.3	36.6	20.7	41.6
Finance costs	(7.9)	(9.1)	(9.7)	(6.9)	(23.8)
Valuation fees	(0.0)	(0.2)	(0.0)	78.2	(8.9)
Administrative expenses	(0.2)	(1.5)	(0.1)	95.9	61.4
Total Expenses	(10.6)	(13.4)	(13.4)	(0.2)	(26.5)
Normalised PBT	15.2	13.4	23.2	73.2	52.0
Normalised PAT	15.2	13.4	23.2	73.2	52.0
EPU after mgmt fee	2.3	2.0	2.2	9.1	(4.2)
DPU (sen)	0	4	0	(100.0)	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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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.
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