

HLIB Research

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Farah Diyana Kamaludin

farahdiyana@hlib.hongleong.com.my

(603) 2083 1719

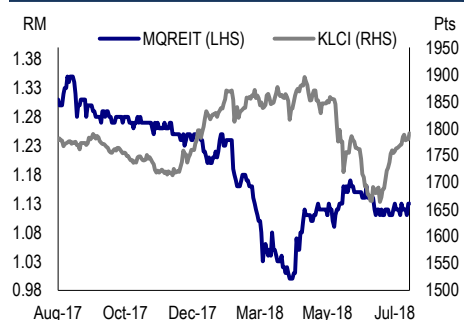
BUY (Maintain)

Target Price: **RM1.29**
Previously: **RM1.29**
Current Price: **RM1.17**

| | |
|-----------------------|-------|
| Capital upside | 10.3% |
| Dividend yield | 7.6% |
| Expected total return | 17.9% |

Sector coverage: REIT

Company description: MRCB-Quill REIT invests in office and retail buildings, business/technology parks, data processing centres, and car parking facilities primarily in Malaysia.

Share price


| | | | |
|-----------------------|------|-----|-------|
| Historical return (%) | 1M | 3M | 12M |
| Absolute | 5.4 | 4.5 | -10.0 |
| Relative | -2.8 | 6.9 | -11.2 |

Stock information

| | |
|------------------------------|----------|
| Bloomberg ticker | MQREITMK |
| Bursa code | 5123 |
| Issued shares (m) | 1,072 |
| Market capitalisation (RM m) | 1,254 |
| 3-mth average volume ('000) | 282 |
| SC Shariah compliant | No |

Major shareholders

| | |
|--------------------------|-------|
| MRCB | 27.8% |
| Capita Commercial Trust | 10.9% |
| Employees Provident Fund | 7.5% |

Earnings summary

| | | | |
|-------------------|------|-------|-------|
| FYE (Dec) | FY17 | FY18f | FY19f |
| PAT – core (RM m) | 88.1 | 89.7 | 90.7 |
| EPU – core (sen) | 6.5 | 8.4 | 8.4 |
| P/E (x) | 14.2 | 14.0 | 13.9 |

MRCB-Quill REIT

Strive for continued stable performance

MQREIT 1H18 core net profit RM44.5m (-1.6% YoY) was in line. Declared semi-annual dividend of 4.23 sen per unit. The decline was due to the disposal of QB8 along with higher operating expenses and finance costs. Going forward, MQREIT will be focussing on cost management and tenant retention to ensure sustainability of yield. We retain our forecast. Reiterate BUY call with unchanged TP of RM1.29 based on targeted yield of 6.9%.

Within expectations. 1H18 revenue of RM87.5m (-3.5% YoY) translated into core net profit of RM44.5m (-1.6% YoY). The results were in line with ours and consensus expectations, accounting for 49.6% and 50.2%, respectively.

Dividend. Declared semi-annual dividend of 4.23 sen per unit (1H17: 4.23 sen) going ex on 21 August 2018.

QoQ. Revenue declined by 1.5% to RM43.4m mainly caused by loss of contribution after the disposal of QB8-DHL XPJ (QB8) since April 2018. However, core net profit increased by 11.8% to RM23.5m. This was essentially due to lower property operating expenses with efficient cost control initiatives.

YoY. Core net profit increased by 6.5% to RM23.5m. The improvement was driven by lower property expenses and expenditure incurred. Lower property operating expenses was attained thanks to tighter control on costs and lower expenses incurred. Nevertheless, the increment was partly mitigated by higher finance costs.

YTD. Revenue for 1H18 decreased by 3.5% to RM87.5m. The lower revenue was due to (1) loss of revenue from QB8 after disposal in April 2018; (2) lower occupancy rate from Platinum Sentral and Menara Shell. Likewise, core net profit of RM44.5m showed a decrement of 1.6% attributable to higher administrative expenses incurred pertaining to the disposal of QB8. Similarly, finance costs increase due to higher interest in borrowings after the drawdown made in March 2017.

Occupancy and gearing. Overall occupancy rate remained healthy at 96% (1Q18: 96%). Average debt to maturity has decreased slightly from 2.55 years to 2.30 years, while average cost of debt maintained at 4.4%. The gearing level decreased slightly to 37% (1Q18: 38%), which is still comfortably below the 50% limit.

Outlook. Out of the 14% total NLA that are due for renewal in 1H18, management has achieved approximately 70% renewal rate and are currently in advanced negotiations with tenants for the balance of leases due in 2H18. Also, management has successfully secured new leases with demand driving from IT, business consultancy, medical and retail sectors. Going forward, management will be focussing on cost management and tenant retention. We continue to like MQREIT given its attractive dividend yield of 7.6% (highest among REITs in our universe), stable assets in prime location of KL Sentral with high occupancy rate.

Forecast. Maintain as the results were in line.

Maintain BUY, TP: RM1.29. We maintain our BUY call with unchanged TP of RM1.29 based on targeted yield of 6.9% which is derived from 2 years historical average yield spread of MQREIT and 10-year MGS.

Financial Forecast

All items in (RM m) unless otherwise stated

Balance Sheet

| FYE Dec | FY16 | FY17 | FY18f | FY19f | FY20f |
|-----------------------|----------------|----------------|----------------|----------------|----------------|
| Cash | 54.1 | 76.0 | 61.1 | 61.8 | 73.1 |
| Receivables | 18.3 | 6.0 | 6.1 | 6.2 | 6.2 |
| Investment properties | 2,222.0 | 2,179.2 | 2,181.2 | 2,183.2 | 2,185.2 |
| PPE | 0.2 | 0.2 | 0.1 | 0.1 | 0.1 |
| Others | 2.7 | 27.0 | 27.0 | 27.0 | 27.0 |
| Assets | 2,297.3 | 2,288.4 | 2,275.5 | 2,278.2 | 2,291.6 |
| Payables | 55.8 | 20.3 | 23.5 | 23.9 | 24.2 |
| Debt | 851.6 | 853.5 | 836.5 | 836.5 | 847.5 |
| Security deposits | 29.3 | 29.2 | 29.2 | 29.2 | 29.2 |
| Derivatives | 1.0 | 0.7 | 0.7 | 0.7 | 0.7 |
| Liabilities | 937.6 | 903.7 | 889.9 | 890.2 | 901.5 |
| Unitholders' capital | 1,231.9 | 1,231.9 | 1,231.9 | 1,231.9 | 1,231.9 |
| Undistributed profit | 127.8 | 152.8 | 153.7 | 156.1 | 158.2 |
| Equity | 1,359.7 | 1,384.7 | 1,385.6 | 1,388.0 | 1,390.1 |

Cash Flow Statement

| FYE Dec | FY16 | FY17 | FY18f | FY19f | FY20f |
|---------------------------|---------------|---------------|---------------|--------------|--------------|
| Profit before taxation | 62.8 | 69.9 | 89.7 | 90.7 | 92.1 |
| Finance costs | 33.0 | 40.5 | 0.0 | 0.0 | 0.0 |
| Depreciation | 0.1 | 0.1 | 0.1 | 0.0 | 0.0 |
| Fair value gain of assets | -3.5 | 18.2 | 0.0 | 0.0 | 0.0 |
| Interest income | -2.4 | -3.6 | 0.0 | 0.0 | 0.0 |
| Others | -19.7 | 4.0 | 3.1 | 0.2 | 0.2 |
| CFO | 70.3 | 129.1 | 92.9 | 90.9 | 92.3 |
| Capex | -647.4 | -0.4 | -2.0 | -2.0 | -2.0 |
| Disposal / (purchase) | -1.5 | 0.0 | 0.0 | 0.0 | 0.0 |
| Others | 0.0 | 2.2 | 0.0 | 0.0 | 0.0 |
| CFI | -648.9 | 1.8 | -2.0 | -2.0 | -2.0 |
| Distribution paid | -56.9 | -72.6 | -88.8 | -88.8 | -90.2 |
| Proceeds from borrowings | 164.0 | 191.0 | 100.0 | 0.0 | 400.0 |
| Repayment of borrowings | 0.0 | -190.0 | -117.0 | 0.0 | -389.0 |
| Placement / new share | 487.9 | -37.2 | 0.0 | 0.0 | 0.0 |
| CFF | 595.1 | -108.8 | -105.8 | -88.8 | -79.2 |
| Net cash flow | 16.5 | 22.0 | -14.9 | 0.1 | 11.1 |

Assumptions

| FYE Dec | FY16 | FY17 | FY18f | FY19f | FY20f |
|----------------------------|------|------|--------------|--------------|--------------|
| Gross rental income | | | | | |
| Quill Building 1 - DHL 1 | | | 4.9 | 5.0 | 5.1 |
| Quill Building 4 - DHL 2 | | | 5.3 | 5.4 | 5.5 |
| Quill Building 2 - HSBC | | | 9.8 | 10.0 | 10.2 |
| Quill Building 3 - BMW | | | 5.1 | 5.2 | 5.3 |
| Wisma Technip | | | 12.4 | 12.7 | 12.9 |
| Part of Plaza Mont' Kiara | | | 4.0 | 4.1 | 4.2 |
| Quill Building 5 - IBM | | | 4.0 | 4.0 | 4.1 |
| Quill Building 8 - DHL XPJ | | | 0.0 | 0.0 | 0.0 |
| Tesco Building - Penang | | | 14.6 | 14.9 | 15.2 |
| Platinum Sentral | | | 57.6 | 57.6 | 57.6 |
| Menara Shell | | | 48.1 | 49.1 | 50.1 |
| Total: | | | 165.9 | 168.1 | 170.3 |

Income Statement

| FYE Dec | FY16 | FY17 | FY18f | FY19f | FY20f |
|----------------------------|--------------|--------------|--------------|--------------|--------------|
| Gross rental income | 115.9 | 162.1 | 165.9 | 168.1 | 170.3 |
| Car park income | 10.9 | 12.8 | 14.2 | 14.4 | 14.7 |
| Other revenue | 5.0 | 5.2 | 5.8 | 5.9 | 6.1 |
| Total revenue | 136.6 | 181.5 | 185.9 | 188.5 | 191.1 |
| Assessment & quit rent | -5.3 | -8.5 | -14.2 | -14.4 | -14.6 |
| Depreciation | -0.1 | -0.1 | -0.1 | -0.1 | -0.1 |
| Insurance & Prop mgmt | -3.1 | -3.9 | -4.0 | -4.0 | -4.1 |
| Service contracts | -9.6 | -10.9 | -11.2 | -11.3 | -11.5 |
| Utilities | -11.5 | -16.7 | -17.1 | -17.4 | -17.6 |
| Total opex | -29.5 | -40.2 | -46.6 | -47.2 | -47.8 |
| Net property income | 77.7 | 101.2 | 92.7 | 94.1 | 95.5 |
| Net investment income | 108.2 | 125.4 | 144.4 | 145.3 | 147.4 |
| Pretax profit | 62.8 | 69.9 | 89.7 | 90.7 | 92.1 |
| Taxation | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 |
| Net profit | 59.2 | 88.1 | 89.7 | 90.7 | 92.1 |
| No. of units (units) | 1,068.0 | 1,068.0 | 1,073.7 | 1,080.6 | 1,087.6 |

Valuation & Ratios

| FYE Dec | FY16 | FY17 | FY18f | FY19f | FY20f |
|------------------|---------|---------|---------|---------|---------|
| Core EPU (sen) | 5.9 | 6.5 | 8.4 | 8.4 | 8.5 |
| P/E (x) | 21.1 | 14.2 | 14.0 | 13.9 | 13.8 |
| EBITDA | 92.3 | 128.7 | 129.5 | 130.4 | 132.3 |
| EBIT | 92.3 | 128.6 | 129.4 | 130.4 | 132.3 |
| EV | 2,047.1 | 2,027.0 | 2,031.6 | 2,039.0 | 2,046.9 |
| EV/EBITDA (x) | 22.2 | 15.8 | 15.7 | 15.6 | 15.5 |
| DPU (sen) | 8.4 | 8.4 | 8.9 | 9.0 | 9.0 |
| Dividend yield | 7.2 | 7.2 | 7.6 | 7.7 | 7.7 |
| NTA/ share (sen) | 126.8 | 129.0 | 128.3 | 127.6 | 126.8 |
| P/ NTA | 0.9 | 0.9 | 0.9 | 0.9 | 0.9 |
| BVPS (RM) | 1.3 | 1.3 | 1.3 | 1.3 | 1.3 |
| P/B (x) | 0.9 | 0.9 | 0.9 | 0.9 | 0.9 |
| EBITDA margin | 67.6% | 70.9% | 69.7% | 69.2% | 69.2% |
| EBIT margin | 67.5% | 70.9% | 69.6% | 69.2% | 69.2% |
| PBT margin | 45.9% | 38.5% | 48.3% | 48.1% | 48.2% |
| Net margin | 43.3% | 48.5% | 48.3% | 48.1% | 48.2% |
| ROE | 4.6% | 5.0% | 6.5% | 6.5% | 6.6% |
| ROA | 2.6% | 3.8% | 3.9% | 4.0% | 4.0% |
| Net gearing | 34.7% | 34.0% | 34.1% | 34.0% | 33.8% |

Quarterly financial summary

| FYE Dec | 2Q17 | 1Q18 | 2Q18 | QoQ (%) | YoY (%) |
|-------------------------|--------------|--------------|--------------|------------|------------|
| Gross revenue | 45.1 | 44.0 | 43.4 | -1.5 | -3.7 |
| Property opex | -10.2 | -9.8 | -10.0 | -2.9 | 1.2 |
| Net property income | 34.9 | 34.3 | 33.4 | -2.7 | -4.4 |
| Interest income | 0.6 | 0.7 | 0.9 | 20.2 | 35.0 |
| Revaluation gains | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 |
| Net investment income | 35.6 | 35.0 | 36.4 | 4.1 | 2.5 |
| Finance costs | -9.8 | -9.7 | -9.9 | -2.5 | -1.0 |
| Valuation fees | -0.1 | -0.1 | -0.1 | 49.4 | 32.6 |
| Administrative expenses | 0.0 | -0.7 | 0.6 | >100 | >100 |
| TOTAL EXPENSES | -13.5 | -14.0 | -12.9 | 7.6 | 4.2 |
| Normalised PBT | 22.0 | 21.0 | 23.5 | 11.8 | 6.5 |
| Normalised PAT | 22.0 | 21.0 | 23.5 | 11.8 | 6.5 |
| EPU (realised) | 2.3 | 2.0 | 2.2 | 11.8 | -2.7 |
| DPU (sen) | 4.2 | 0.0 | 4.2 | NM | 0.0 |

Figure #1 **Quarterly results comparison**

| FYE Dec (RM m) | 2Q17 | 1Q18 | 2Q18 | QoQ (%) | YoY (%) | 1H17 | 1H18 | YoY (%) |
|-----------------------------|-------------|-------------|-------------|----------------|----------------|-------------|-------------|----------------|
| Gross revenue | 45.1 | 44.0 | 43.4 | -1.5 | -3.7 | 90.6 | 87.5 | -3.5 |
| Property operating expenses | -10.2 | -9.8 | -10.0 | -2.9 | 1.2 | -19.6 | -19.8 | 1.0 |
| Net property income | 34.9 | 34.3 | 33.4 | -2.7 | -4.4 | 71.0 | 67.6 | -4.8 |
| Interest income | 0.6 | 0.7 | 0.9 | 20.2 | 35.0 | 1.1 | 1.6 | 45.8 |
| Gain on divestment | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 |
| Net investment income | 35.6 | 35.0 | 36.4 | 4.1 | 2.5 | 72.1 | 71.5 | -0.9 |
| Finance costs | -9.8 | -9.7 | -9.9 | -2.5 | -1.0 | -19.6 | -19.6 | 0.3 |
| Valuation fees | -0.1 | -0.1 | -0.1 | 49.4 | 32.6 | -0.1 | -0.2 | 37.8 |
| Administrative expenses | 0.0 | -0.7 | 0.6 | >100 | >100 | -0.1 | -0.1 | 53.3 |
| Total expenses | -13.5 | -14.0 | -12.9 | 7.6 | 4.2 | -26.9 | -27.0 | 0.1 |
| Core PBT | 22.0 | 21.0 | 23.5 | 11.8 | 6.5 | 45.2 | 44.5 | -1.6 |
| Core PAT | 22.0 | 21.0 | 23.5 | 11.8 | 6.5 | 45.2 | 44.5 | -1.6 |
| Distributable adjustments | 0.0 | 1.4 | 1.0 | -28.0 | NM | 0.0 | 2.4 | NM |
| Distributable income | 22.0 | 22.4 | 24.5 | 9.3 | 11.1 | 45.2 | 46.9 | 3.7 |
| Core EPU (sen) | 2.3 | 2.0 | 2.2 | 11.8 | -2.7 | 4.4 | 4.2 | -6.0 |
| DPU (sen) | 4.2 | 0.00 | 4.2 | NM | 0.0 | 4.2 | 4.2 | 0.0 |

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Hong Leong Investment Bank Berhad (10209-W)

Level 28, Menara Hong Leong,

No. 6, Jalan Damanlela,

Bukit Damansara,

50490 Kuala Lumpur

Tel: (603) 2083 1800

Fax: (603) 2083 1766

Stock rating definitions

| | |
|---------------------|---|
| BUY | Expected absolute return of +10% or more over the next 12-months. |
| HOLD | Expected absolute return of -10% to +15% over the next 12-months. |
| SELL | Expected absolute return of -10% or less over the next 12-months. |
| UNDER REVIEW | Rating on the stock is temporarily under review which may or may not result to a change from the previous rating. |
| NOT RATED | Stock is not or no longer within regular coverage. |

Sector rating definitions

| | |
|--------------------|--|
| OVERWEIGHT | Sector expected to outperform the market over the next -12 months. |
| NEUTRAL | Sector expected to perform in-line with the market over the next -12 months. |
| UNDERWEIGHT | Sector expected to underperform the market over the next -12 months. |