HLIB Research

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Sentral REIT

Occupancy rate trending down

Sentral REIT recorded 2QFY22 core net profit of RM18.5m (-9.4% QoQ, -2.3% YoY) and 1HFY22 core net profit of RM38.8m (-2.0% YoY). We deem the results to be below expectations despite accounting for 45%-48% of our and consensus estimates, as we are projecting sequentially weaker quarters due to non-renewal of tenants for two of their properties. The marginal drop in 1HFY22 performance was due to lower rental income generated from (i) Quill Building 2 – HSBC, (ii) Wisma Technip, (iii) Quill Building 3 – BMW and (iv) Menara Shell, as occupancy rate decreases. We trim our earnings forecast by 8.9%/8.5%/5.2%, as we lower our occupancy rate assumptions, given the challenging outlook. We revised our TP to RM0.91 (from RM0.99) and downgrade to HOLD (from Buy).

Below estimates. Sentral REIT's 2QFY22 core net profit of RM18.5m (-9.4% QoQ, -2.3% YoY) brought 1HFY22 core net profit to RM38.8m (-2.0% YoY). We deem the results to be below our estimates despite accounting for 45%-48% of our and consensus estimates, as we are projecting sequentially weaker quarters, given non-renewal of standalone tenants for two of their properties.

Dividend. Declared DPS of 3.40 sen (semiannual dividend) vs 3.43 sen SPLY.

QoQ. Top line fell to RM37.1m (-5.7%) mainly due to lower revenue generated from Quill Building 2 and Wisma Technip as leases of key tenants have expired at end April and June 2022, respectively without renewal. Meanwhile, property operating expenses rose to RM8.6 (+3.9%), leading to a reduction of net property income (NPI) to RM28.5m (-8.3%). This was, however, mitigated by slight decline in total expenditure to RM10.4m (-6.3%), mainly comprising manager's fee (-2.3%), finance costs (-2.9%; savings on interests after refinancing exercise in Mar 2022). All in, core net profit decreased to RM18.5m (-9.4%).

YoY/YTD. Revenue shrunk (-3.0% YoY, -3.6% YTD) due to lower rental income generated from (i) Quill Building 2 – HSBC, (ii) Wisma Technip, (iii) Quill Building 3 – BMW and (iv) Menara Shell. Accordingly, property operating expenses decreased (-0.1% YoY, -7.5% YTD), primarily attributable to lower expenses incurred by some properties. In tandem, these resulted in a marginal drop in net property income (-3.8% YoY, -2.5% YTD). Meanwhile, total expenditure fell (-6.9% YoY, -3.8% YTD), contributed by lower managers' fee (-2.8% YoY, 2.5% YTD) and finance costs (-8.5% YoY, -6.8% YTD). Hence, core net profit declined slightly (-2.3% YoY, -2.0% YTD).

Occupancy and gearing. With nine properties, the overall occupancy rate decreased to 78% (1QFY22: 86%). As for gearing level, it decreased slightly to 37.0% (1QFY22: 37.4%).

Outlook. As Quill Building 2 and Wisma Technip have been vacant since end April and June 2022, respectively with no prospective tenants in sight, we foresee the downward impact to be more prominent in the upcoming quarters. Management is exploring the strategy of filling up the buildings as a multi tenanted property as opposed to leasing to a single occupier. Overall, management guided that rental reversions for its assets portfolio are expected to remain flattish. On a macro basis, the office market remains challenging due to substantial incoming supply which exacerbates the prevailing office glut. This adds to the challenge of securing new tenants with promising rates.

Forecast. We trim our earnings forecast by 8.9%/8.5%/5.2%, as we lower our occupancy rate assumptions, given the challenging outlook.

HOLD (from Buy)

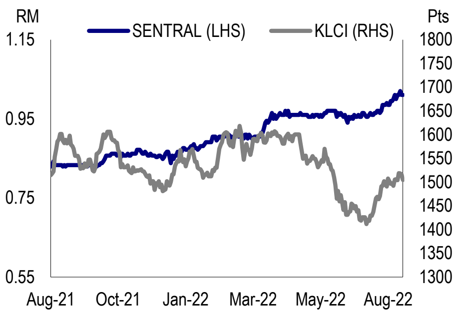
Target Price:	**RM0.91**
Previously:	**RM0.99**
Current Price:	**RM1.01**

Capital upside	-10.1%
Dividend yield	7.1%
Expected total return	-3.0%

Sector coverage: REIT

Company description: Sentral 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	5.2	5.8	12.2
Relative	-0.1	8.9	13.0

Stock information

Bloomberg ticker	SENTRAL MK
Bursa code	5123
Issued shares (m)	1,072
Market capitalisation (RM m)	1,083
3-mth average volume ('000)	192
SC Shariah compliant	No
F4GBM Index member	No
ESG rating	N.A.

Major shareholders

MRCB	27.8%
Employees Provident Fund	12.0%
CapitaLand Ltd	10.9%

Earnings summary

FYE (Dec)	FY21	FY22f	FY23f
PAT – core (RM m)	84.5	77.7	81.6
EPU – core (sen)	7.9	7.2	7.6
P/E (x)	12.8	13.9	13.3

Downgrade to HOLD, TP of RM0.91. The recent gain in share price has diminished upside for Sentral REIT. This is coupled with our earnings adjustment in view of its declining occupancy rate and subdued tenancy replenishment. However, we believe the downside is supported for Sentral REIT due to its attractive dividend yield at around 7% and prime office properties at strategic locations. All in, we revised our TP to RM0.91 (from RM0.99). Our TP is based on FY23 forward DPU on targeted yield of 8.3%, which is derived from 5-year historical average yield spread between Sentral REIT and 10-year MGS. Downgrade to HOLD (from Buy).

Financial Forecast

All items in (RM m) unless otherwise stated

Balance Sheet

FYE Dec	FY20	FY21	FY22f	FY23f	FY24f
Cash	85.0	93.5	94.0	92.3	92.5
Receivables	5.1	5.6	5.7	5.7	5.9
Investment properties	2,097.0	2,081.0	2,083.0	2,085.0	2,086.0
PPE	0.3	0.1	0.0	0.0	0.0
Others	40.3	0.1	0.1	0.1	0.1
Assets	**2,227.7**	**2,180.4**	**2,182.8**	**2,183.2**	**2,184.6**
Payables	19.1	19.2	20.5	20.5	20.5
Debt	845.0	805.6	805.2	804.7	805.3
Security deposits	40.1	37.7	37.7	37.7	37.7
Derivatives	0.0	0.0	0.0	0.0	0.0
Liabilities	**904.2**	**862.5**	**863.3**	**862.9**	**863.4**
Unitholders' capital	1,235.9	1,235.9	1,235.9	1,235.9	1,235.9
Undistributed profit	87.6	82.0	83.6	84.4	85.3
Equity	**1,323.5**	**1,317.9**	**1,319.4**	**1,320.3**	**1,321.2**
Total Liabilities & Equity	**2,227.7**	**2,180.4**	**2,182.8**	**2,183.2**	**2,184.6**

Income Statement

FYE Dec	FY20	FY21	FY22f	FY23f	FY24f
Gross rental income	148.0	146.6	147.1	149.4	154.6
Car park income	11.8	9.5	9.6	9.6	9.8
Other revenue	4.2	3.5	4.0	4.6	4.7
Total revenue	**164.0**	**159.6**	**160.7**	**163.6**	**169.1**
Property opex	-37.9	-37.0	-39.4	-39.4	-39.4
Net property income	**126.1**	**122.6**	**121.3**	**124.2**	**129.7**
Other income	-2.6	-8.3	2.9	2.9	2.9
Net invest income	**123.5**	**114.4**	**124.2**	**127.1**	**132.5**
Manager's fee	-12.8	-12.6	-13.5	-12.5	-12.7
Trustee's fee	-0.7	-0.7	-0.7	-0.7	-0.7
Finance costs	-35.4	-31.1	-31.1	-31.1	-31.1
Other non opex	-0.9	-1.2	-1.3	-1.3	-1.3
Profit before tax	**73.8**	**68.8**	**77.7**	**81.6**	**86.8**
Taxation	**-1.2**	**1.5**	**1.5**	**1.5**	**1.5**
Profit after tax	**72.6**	**70.2**	**79.1**	**83.0**	**88.3**
Core net profit	**81.0**	**84.5**	**77.7**	**81.6**	**86.8**
Distributable income	**81.0**	**84.5**	**77.7**	**81.6**	**86.8**
Consensus core net profit			85.8	87.0	89.0
HLIB/ Consensus			91%	94%	98%

Cash Flow Statement

FYE Dec	FY20	FY21	FY22f	FY23f	FY24f
Profit before taxation	73.8	68.8	77.7	81.6	86.8
Finance costs	35.4	31.1	0.0	0.0	0.0
Depreciation	0.2	0.2	0.1	0.0	0.0
Fair value gain of assets	7.2	15.7	0.0	0.0	0.0
Interest income	-2.9	-2.6	0.0	0.0	0.0
Others	4.7	-2.7	1.2	-0.1	-0.2
CFO	**118.4**	**110.5**	**79.0**	**81.5**	**86.7**
Capex	-1.2	-0.7	-2.0	-2.0	-1.0
Disposal / (purchase)	-0.1	0.0	0.0	0.0	0.0
Others	2.2	44.0	0.0	0.0	0.0
CFI	**0.9**	**43.3**	**-2.0**	**-2.0**	**-1.0**
Distribution paid	-72.9	-75.9	-77.5	-82.2	-87.4
Proceeds frm borrow'g	341.0	258.4	165.0	165.0	166.0
Repayment of borrow'g	-335.0	-300.0	-164.0	-164.0	-164.0
Others	-30.7	-27.7	0.0	0.0	0.0
CFF	**-97.5**	**-145.2**	**-76.5**	**-81.2**	**-85.4**
Net cash flow	**21.7**	**8.6**	**0.5**	**-1.7**	**0.2**
Beginning cash	63.3	85.0	93.5	94.0	92.3
Ending cash	85.0	93.5	94.0	92.3	92.5

Valuation & Ratios

FYE Dec	FY20	FY21	FY22f	FY23f	FY24f
Core EPU (sen)	7.6	7.9	7.2	7.6	8.1
P/E (x)	13.4	12.8	13.9	13.3	12.5
EBITDA	116.5	115.8	108.9	112.7	117.9
EBIT	116.3	115.6	108.7	112.6	117.9
EV	1,842.5	1,794.6	1,793.7	1,794.9	1,795.3
EV/EBITDA (x)	15.8	15.5	16.5	15.9	15.2
DPU (sen)	7.1	7.4	7.2	7.6	8.1
Dividend yield	7.0	7.3	7.1	7.5	8.0
NTA/ share (sen)	123.5	123.0	123.1	123.2	123.3
P/ NTA	0.8	0.8	0.8	0.8	0.8
BVPS (RM)	1.23	1.23	1.23	1.23	1.23
P/B (x)	0.8	0.8	0.8	0.8	0.8
EBITDA margin	71.1%	72.5%	67.7%	68.9%	69.7%
EBIT margin	70.9%	72.4%	67.7%	68.9%	69.7%
PBT margin	45.0%	43.1%	48.3%	49.9%	51.4%
Net margin	49.4%	52.9%	48.3%	49.9%	51.4%
ROE	6.1%	6.4%	5.9%	6.2%	6.6%
ROA	3.6%	3.9%	3.6%	3.7%	4.0%
Net gearing	34.12%	32.66%	32.58%	32.63%	32.63%

Assumptions

FYE Dec	FY22f	FY23f	FY24f
Gross rental income			
Quill Building 1 - DHL 1	5.2	5.3	5.4
Quill Building 4 - DHL 2	5.5	5.6	5.8
Quill Building 2 - HSBC	5.1	5.8	7.5
Quill Building 3 - BMW	5.8	5.9	6.0
Wisma Technip	5.5	5.2	6.8
Part of Plaza Mont' Kiara	3.6	3.7	3.8
Quill Building 5 - IBM	0.0	0.0	0.0
Tesco Building - Penang	15.6	15.9	16.2
Platinum Sentral	53.4	54.4	55.3
Menara Shell	47.4	47.6	47.9
Total:	147.1	149.4	154.6

Quarterly financial summary

FYE Dec	2Q21	1Q22	2Q22	QoQ (%)	YoY (%)
Gross Revenue	38.2	39.3	37.05	-5.7%	-3.0%
Property operating exper	-8.6	-8.3	(8.57)	3.9%	-0.1%
Net Property Income	29.6	31.0	28.48	-8.3%	-3.8%
Interest income	0.5	0.5	0.42	-9.3%	-15.2%
Net Investment Income	30.1	31.5	28.89	-8.3%	-4.0%
Total Expenses	-11.2	-11.1	(10.44)	-6.3%	-6.9%
Normalised PBT	18.9	20.4	18.45	-9.4%	-2.3%
Normalised PAT	18.9	20.4	18.45	-9.4%	-2.3%
Distributable income	18.9	20.4	18.45	-9.4%	-2.3%
EPU (realised)	1.8	1.9	1.72	-9.4%	-2.3%
DPU (sen)	3.43	0.0	3.40	NM	NM

Figure #1 **Quarterly results comparison**

FYE Dec (RM m)	2QFY21	1QFY22	2QFY22	QoQ (%)	YoY (%)	FY21	FY22	YoY (%)
Gross Revenue	**38.2**	**39.3**	**37.1**	**-5.7%**	**-3.0%**	**79.2**	**76.4**	**-3.6%**
Property operating expenses	-8.6	-8.3	-8.6	3.9%	-0.1%	18.2	16.8	-7.5%
Net Property Income	**29.6**	**31.0**	**28.5**	**-8.3%**	**-3.8%**	**61.0**	**59.5**	**-2.5%**
Interest income	0.5	0.5	0.4	-9.3%	-15.2%	1.0	0.9	-10.4%
Net Investment Income	**30.1**	**31.5**	**28.9**	**-8.3%**	**-4.0%**	**62.0**	**60.4**	**-2.6%**
Manager's fee	-3.13	-3.11	-3.04	-2.3%	-2.8%	-6.3	-6.1	-2.5%
Trustee's fee	-0.17	-0.16	-0.16	-1.7%	-3.6%	-0.3	-0.3	-3.0%
Finance costs	-7.8	-7.3	-7.1	-2.9%	-8.5%	-15.4	-14.4	-6.8%
Valuation fees	-0.1	-0.1	-0.1	0.0%	-10.1%	-0.2	-0.2	-10.2%
Administrative expenses	-0.0	-0.4	-0.0	-94.1%	-36.2%	-0.1	-0.5	+389.8%
Total Expenses	**-11.2**	**-11.1**	**-10.4**	**-6.3%**	**-6.9%**	**-22.4**	**-21.6**	**-3.8%**
Core PBT	18.9	20.4	18.5	-9.4%	-2.3%	39.6	38.8	-2.0%
Core PAT	**18.9**	**20.4**	**18.5**	**-9.4%**	**-2.3%**	**39.6**	**38.8**	**-2.0%**
Distributable income	18.9	20.4	18.5	-9.4%	-2.3%	39.6	38.8	-2.0%
EPU (realised)	1.76	1.90	1.72	-9.4%	-2.3%	3.69	3.62	-2.0%
DPU (sen)	3.43	0.00	3.40	-	-0.9%	3.43	3.40	0.9%

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Stock rating guide

BUY	Expected absolute return of +10% or more over the next 12 months.
HOLD	Expected absolute return of -10% to +10% 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 in a change from the previous rating.
NOT RATED	Stock is not or no longer within regular coverage.

Sector rating guide

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.

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