

3 August 2016

Property | REITS

MRCB-Quill REIT

Buy (Maintained)

Full Recognition From Platinum Sentral

Amidst the challenging office segment, we expect MQREIT to buck the trend and sustain stable growth in 2H16, benefiting from long-term leases at the majority of its assets. Clearly benefiting from the injection of Platinum Sentral in Mar 2015, the anticipated upcoming injection of Menara Shell by end-2016 will provide another source of long-term growth to the portfolio. We increase our DDM-based TP to MYR1.32 (from MYR1.29, 10% upside) as we lower our risk-free-rate assumption to 3.55% (from 3.70%) to reflect the recent OPR cut. Maintain BUY.

High and stable occupancy rate. We anticipate the portfolio occupancy rate of the MRCB-Quill REIT (MQREIT), which stands at 97.2%, to remain stable in 2H16, as most of the tenants are on long-term leases. 43% of its tenants' lease renewal comes within 2020-2032, while another 37% in 2018-2019. This should provide stability in the current economic environment and upcoming supply of office space.

Menara Shell injection to spur inorganic growth. The proposed injection of Menara Shell by end-2016 is expected to provide a jump in growth of the portfolio size and its revenue and earnings from 2017 onwards. MQREIT has proposed to acquire the office tower for MYR640m, which will increase the total property value of the REIT by 41% to MYR2.27bn.

Maintain Buy. We make no changes to our FY16-18 earnings forecasts. We maintain our BUY call with a higher DDM-based TP of MYR1.32 due to a lower risk-free-rate assumption. The key risk to our call would be a prolonged weak domestic consumer sentiment.

2Q16 (Jun) earnings : results in line

(MYRm)	2Q16	1Q16	QoQ (%)	2Q15	YoY (%)	Comments
Revenue	32.6	32.7	-0.3	32.2	1.2	Full contribution from Platinum Sentral.
NPI	25.7	25.4	1.0	24.3	5.7	
NPI (%)	78.9%	77.9%		75.6%		
Pretax income	14.7	15.2	-3.8	15.0	-2.5	
Pretax margin (%)	45.0%	46.7%		46.7%		
NP - reported	14.7	15.2	-3.8	15.0	-2.5	
NM - reported (%)	45.0%	46.7%		46.7%		
NP - recurring	15.4	15.2	1.0	13.6	12.9	
NM - recurring (%)	12.77%	12.46%		17.46%		

Source: Company data, RHB

1H16 results within expectations. MQREIT's 1H16 core net profit of MYR30.6m (39.8% YoY) came in line within expectations at 51%/53% of our/street estimates. A first DPU of 4.23 sen was declared for 1H16. Its 1H16 revenue and earnings were boosted by full contributions from Platinum Sentral, of which the acquisition was completed on 30 Mar 2015.

Forecasts and Valuations	Dec-14	Dec-15	Dec-16F	Dec-17F	Dec-18F
Total turnover (MYRm)	70	110	124	174	178
Net property income (MYRm)	53	87	94	132	137
Reported net profit (MYRm)	34.1	53.9	60.5	86.4	91.5
Total distributable income (MYRm)	34.1	53.9	60.5	86.4	91.5
DPS (MYR)	0.08	0.08	0.09	0.08	0.08
DPS growth (%)	0.0	(1.3)	4.1	(9.3)	4.2
Recurring P/E (x)	13.7	13.2	13.1	14.8	14.0
P/B (x)	0.86	0.87	0.96	0.95	0.95
Dividend Yield (%)	7.0	6.9	7.2	6.5	6.8
Return on average equity (%)	6.3	7.4	5.4	6.4	6.8
Return on average assets (%)	3.9	4.3	3.1	3.8	4.0
Interest cover (x)	3.38	2.95	3.20	3.19	3.32
Our vs consensus EPS (adjusted) (%)			(1.6)	(15.7)	(10.8)

Source: Company data, RHB

Target Price:	MYR1.32
Price:	MYR1.20
Market Cap:	USD196m
Bloomberg Ticker:	MQREIT MK

Share Data

Avg Daily Turnover (MYR/USD)	0.28m/0.07m
52-wk Price low/high (MYR)	1.01 - 1.24
Free Float (%)	40
Shares outstanding (m)	661
Estimated Return	10%

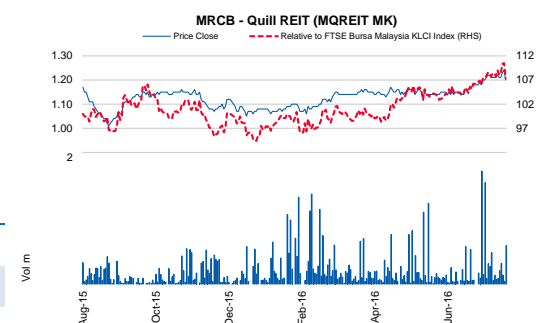
Shareholders (%)

CapitaCommercial Trust	30.0
Quill Group	30.0

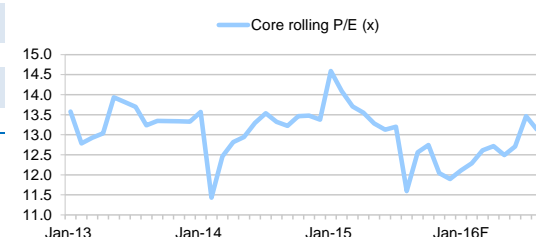
Share Performance (%)

	YTD	1m	3m	6m	12m
Absolute	11.1	2.6	3.4	9.1	1.7
Relative	13.0	1.7	4.2	8.7	5.4

Source: Bloomberg



Source: Bloomberg



Source: Bloomberg

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Figure 1: MRCB-Quill REIT's 1H16 earnings review

FYE Dec (MYRm)	2Q15	1Q16	2Q16	QoQ (%)	YoY (%)	1H15	1H16	YoY (%)	Comments
Revenue	32.2	32.7	32.6	(0.3)	1.2	50.8	65.2	28.4	Higher YoY revenue growth due to the additional contribution coming from Platinum Sentral, Plaza Mont Kiara and rental rate increases for some other properties.
Net property income (NPI)	24.3	25.4	25.7	1.0	5.7	38.0	51.1	34.6	MQREIT incurred higher property operating expenses due to additional repair and maintenance costs and acquisition of Platinum Sentral.
Interest expense	(8.2)	(7.9)	(8.0)	1.5	(2.6)	(11.7)	(15.8)	35.0	Higher interest expense due to interest on additional borrowings on Platinum Sentral.
Interest income	0.1	0.4	0.4	(2.4)	165.1	0.3	0.8	186.2	
Associates	0.0	0.0	0.0	nm	nm	0.0	0.0	nm	
EI	0.0	0.0	0.0	nm	nm	0.0	0.0	nm	
Others	(2.6)	(2.7)	(2.7)	(1.0)	3.1	(4.6)	(5.5)	18.1	
Pretax profit	15.0	15.2	14.7	(3.8)	(2.5)	23.3	25.9	11.3	
Tax	0.0	0.0	0.0	nm	nm	0.0	0.0	nm	
Minority Interest	0.0	0.0	0.0	nm	nm	0.0	0.0	nm	
Net Profit	15.0	15.2	14.7	(3.8)	(2.5)	23.3	25.9	11.3	
Core Profit	13.6	15.2	15.4	1.0	12.9	21.9	30.6	39.8	Within expectations
Core earnings per unit (sen)	2.20	2.30	2.33	1.1	5.9	4.31	4.63	7.4	
Dividends per unit (sen)	2.22	0.00	4.23	#DIV/0!	90.5	4.10	4.23	3.2	
<i>NPI Margin (%)</i>	<i>75.6</i>	<i>77.9</i>	<i>78.9</i>			<i>74.8</i>	<i>78.4</i>		
<i>Pretax Margin (%)</i>	<i>46.7</i>	<i>46.7</i>	<i>45.0</i>			<i>45.9</i>	<i>39.8</i>		
<i>Net Margin (%)</i>	<i>42.4</i>	<i>46.7</i>	<i>47.2</i>			<i>43.1</i>	<i>47.0</i>		

Source: Company data, RHB

Figure 1: Forecasts assumptions

Asset	NLA / GFA (sf)	Average Rental Rates (MYR psf)		
		FY16	FY17	FY18
QB 1 - DHL 1	92,284	4.37	4.45	4.54
QB 4 - DHL 2	99,183	4.37	4.45	4.54
QB 2 - HSBC	184,453	4.37	4.45	4.54
QB 3 - BMW	117,198	4.37	4.45	4.54
QB 5 - IBM	81,602	3.21	3.33	3.44
Plaza MK	73,408	8.52	8.53	8.54
Wisma Technip	233,021	5.68	5.85	6.02
QB 10 - HSBC	68,377	3.21	3.33	3.44
QB 8 - DHL	65,205	3.21	3.33	3.44
Tesco Penang	275,020	3.03	3.09	3.16
Platinum Sentral	475,857	8.91	9.04	9.17
Shell Tower	557,053	7.04	7.21	7.39
DPU (sen)		8.61	7.81	8.14

Source: RHB

Financial Exhibits

Financial model updated on : 2016-08-02.

Asia
Malaysia
Property
MRCB-Quill REIT
Bloomberg MQREIT MK
Buy
Valuation basis
Dividend discount model
Key drivers
Improvement in domestic consumer sentiment leading to strong consumer spending.
Key risks
Downside risks include prolonged weak domestic consumer sentiment while upside risks include stronger demand for its assets leading to higher occupancy rates and rental reversion rates at its assets.
Company Profile
MRCB-Quill REIT is a mid-cap MREIT that focuses on office/commercial assets. Assets are largely concentrated in the Klang Valley and Cyberjaya areas.

Financial summary	Dec-14	Dec-15	Dec-16F	Dec-17F	Dec-18F
Recurring EPS (MYR)	0.09	0.09	0.09	0.08	0.09
EPS (MYR)	0.09	0.09	0.09	0.08	0.09
DPS (MYR)	0.08	0.08	0.09	0.08	0.08
BVPS (MYR)	1.39	1.38	1.26	1.26	1.26
Weighted avg adjusted shares (m)	390	594	661	1,068	1,068

Valuation metrics	Dec-14	Dec-15	Dec-16F	Dec-17F	Dec-18F
Recurring P/E (x)	13.7	13.2	13.1	14.8	14.0
P/E (x)	13.7	13.2	13.1	14.8	14.0
P/B (x)	0.86	0.87	0.96	0.95	0.95
FCF Yield (%)	5.4	7.1	(46.4)	6.5	6.8
Dividend Yield (%)	7.0	6.9	7.2	6.5	6.8
EV/EBITDA (x)	(1.87)	(1.29)	(1.61)	(1.91)	(1.86)
EV/EBIT (x)	(1.87)	(1.29)	(1.61)	(1.91)	(1.86)

Income statement	Dec-14	Dec-15	Dec-16F	Dec-17F	Dec-18F
Total turnover (MYRm)	70.2	109.6	123.9	174.3	177.8
EBITDA (MYRm)	47.4	80.4	87.0	124.8	129.9
Operating profit (MYRm)	47.4	80.4	87.0	124.8	129.9
Net interest (MYRm)	(13.3)	(26.5)	(26.5)	(38.4)	(38.4)
Pre-tax profit (MYRm)	34.1	53.9	60.5	86.4	91.5
Recurring net profit (MYRm)	34.1	53.9	60.5	86.4	91.5

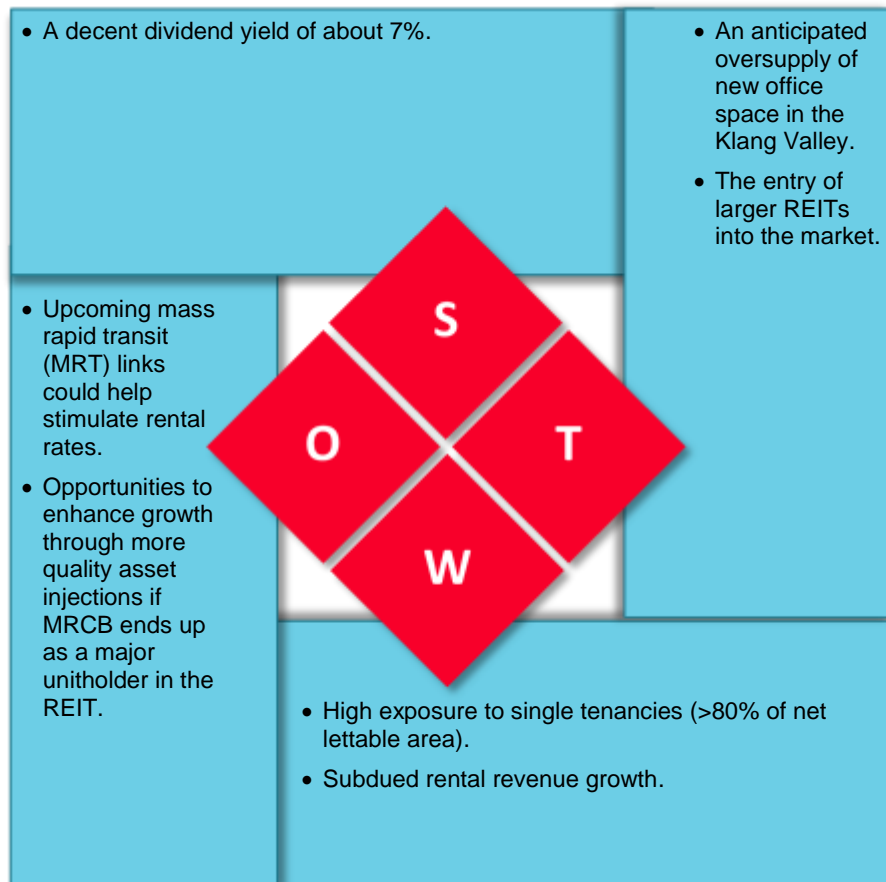
Cash flow (MYRm)	Dec-14	Dec-15	Dec-16F	Dec-17F	Dec-18F
Change in working capital	(3.1)	(3.3)	(3.5)	(3.6)	(3.8)
Cash flow from operations	31.1	52.6	59.1	84.8	89.6
Capex	(6.0)	(2.0)	(427.0)	(2.0)	(2.0)
Cash flow from investing activities	(6.0)	(2.0)	(427.0)	(2.0)	(2.0)
Proceeds from issue of shares	0.2	365.3	0.0	0.0	0.0
Dividends paid	(32.7)	(40.9)	(53.0)	(70.2)	(85.1)
Cash flow from financing activities	(32.2)	722.4	176.0	(70.2)	(85.1)

Balance sheet (MYRm)	Dec-14	Dec-15	Dec-16F	Dec-17F	Dec-18F
Total cash and equivalents	23	60	248	260	263
Total investments	839	1,552	2,192	2,192	2,192
Total other assets	0	0	0	0	0
Total assets	868	1,637	2,296	2,300	2,304
Other liabilities	8	8	8	8	8
Total liabilities	327	725	954	955	955
Shareholders' equity	541	911	1,342	1,345	1,350
Total equity	541	911	1,342	1,345	1,350
Net debt	282	643	684	672	669
Total liabilities & equity	868	1,637	2,296	2,300	2,304

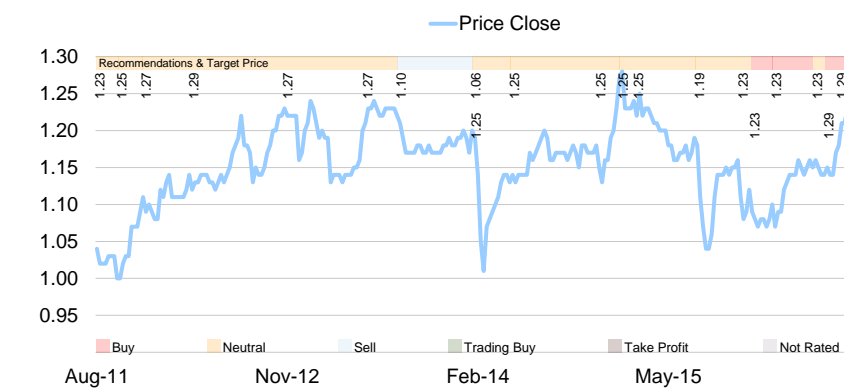
Key metrics	Dec-14	Dec-15	Dec-16F	Dec-17F	Dec-18F
Revenue growth (%)	1.9	56.0	13.1	40.7	2.0
Recurrent EPS growth (%)	(1.2)	3.8	0.8	(11.6)	5.8
Operating EBITDA margin (%)	67.5	73.4	70.2	71.6	73.1
Net profit margin (%)	48.6	49.2	48.9	49.6	51.4
Dividend payout ratio (%)	95.8	91.0	91.0	91.0	91.0
Capex/sales (%)	8.6	1.8	344.6	1.1	1.1
Interest cover (x)	3.38	2.95	3.20	3.19	3.32

Source: Company data, RHB

SWOT Analysis



Recommendation Chart



Date	Recommendation	Target Price	Price
2016-07-01	Buy	1.29	1.17
2016-05-31	Buy	1.29	1.14
2016-05-03	Neutral	1.23	1.14
2016-01-25	Buy	1.23	1.08
2015-12-04	Buy	1.23	1.12
2015-11-06	Neutral	1.23	1.16
2015-07-23	Neutral	1.19	1.19
2015-02-26	Neutral	1.25	1.23
2015-01-20	Neutral	1.25	1.25
2014-11-27	Neutral	1.25	1.18

Source: RHB, Bloomberg

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Trading Buy: Share price may exceed 15% over the next 3 months, however longer-term outlook remains uncertain

Neutral: Share price may fall within the range of +/- 10% over the next 12 months

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