

UOBKH HIGHLIGHTS

MRCB-Quill REIT (MQREIT MK/HOLD/RM1.10/Target: RM1.10)

1Q19: Slightly Below Expectations

Year to 31 Dec	1Q19 (RMm)	4Q18 (RMm)	qoq % chg	yoy % chg	Year	EPU (sen)	PE (x)
Gross Revenue	41.4	42.7	(3.0)	(6.0)	2019F	7.58	14.5
Operating Expenses	(9.3)	(10.0)	(6.5)	(4.3)	2020F	7.93	13.9
Net Property Income	32.0	32.7	(1.9)	(6.5)	2021F	8.26	13.3
Finance Cost	(9.9)	(10.9)	(9.5)	1.7			
Core Net Profit	19.4	19.6	(1.0)	(7.6)			
EPU (sen)	1.8	1.3	(1.0)	(7.9)			
DPU (sen)	0.0	3.9	n.m.	n.m.			

Source: MRCB-Quill Reit, UOB Kay Hian

RESULTS

- **Slightly below expectations.** MRCB-Quill REIT (MQREIT) reported revenue of RM41.4m (-3.0% qoq, -6.0% yoy) and core net profit of RM19.6m (-1.0% qoq, -7.6% yoy) in 1Q19. Core net profit accounts for 23% of our and consensus' full-year forecasts. We deem results slightly below our expectations.
- MQREIT typically declares dividend in the second and final quarters.
- **Net profit declined 7.6% yoy**, due to: a) absence of income from QB8-DHL XPJ which was sold in Apr 18, and b) lower revenue from Platinum Sentral and Menara Shell on lower occupancies. Leases due in 1Q19 (c.59,000 sf) which are predominantly in Platinum Sentral, were not renewed. However, approximately 48,000 sf of new leases commenced almost immediately in April. We also gathered that rents were slightly lower for the new leases. Total lease for renewal for 2019 and 2020 are 19% and 18% of total NLA respectively.
- **Decline in occupancy rate.** Occupancy rate declined to 89% as at 31 Mar 19 (4Q18: 93%) but is still higher than the average of 80% in 2017 for offices in the Klang Valley. This is mainly due to MQREIT's purpose-built strategy which allows it to lock in long-term leases. MQREIT's WALE is 4.84 years.
- **Gearing at 37.5%.** We think MQREIT's current gearing ratio is healthy (on a par with peers), which allows it to tap into the debt and equity markets for future acquisitions.
- We reduce our earnings forecasts by 5.8-8.1% for 2019-21F as we have lowered our occupancy rates (portfolio occupancy from 96% to 94%) and rental rates.

VALUATION/RECOMMENDATION

- **Maintain HOLD with lower target price of RM1.10** (from RM1.15) after our earnings adjustment. Our target price is based on a dividend discount model (required rate of return: 6.8%, terminal growth: 1.1%) and represents an implied dividend yield of 6.9%. We are maintaining our HOLD call despite the attractive 6.9% yield as rental rates are depressed with a slight downtrend in occupancy rates. We take a cautious stance until we see an improvement in their occupancy rates. Entry price is RM1.05.

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