

MRCB-Quill REIT (BUY ↔, EPS ↔)

INDUSTRY: NEUTRAL
EARNINGS EVALUATION
20 November 2017
Target Price: RM1.48 (↔)
Share Price: RM1.27

9MFY17 Results- In line

Results

- **Within expectations.** 3QFY17 normalised net profit of RM21.4m (qoq: -3.0%; yoy: +40.4%) translated into 9MFY17 normalized net profit of RM66.6m (+45.3% yoy). The results were within ours and consensus expectations, accounting for 76.0% of our and 73.4% of consensus estimates.

Deviations

- None.

Dividends

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

Highlights

- **YoY:** Normalized net profit increased 40.4% on the back of additional revenue from the newly acquired Menara Shell and higher rental income from QB2, QB3, QB5 and Wisma Technip.
- **QoQ:** Normalized net profit decreased 3% due to higher property operating expenses.
- **YTD:** Normalized net profit increased 45.3% due to additional revenue from the newly acquired Menara Shell (full year impact as it was acquired in Dec 2016) and rental rate increases from QB2, QB3, QB5 and Wisma Technip.
- Overall occupancy rate remained healthy at 96.6%. Meanwhile, c.57% of total lease expiry in FY17 (14% of total NLA) has been renewed.
- Average debt to maturity has improved to 3.05 years (from 2.70) while average cost of debt (4.4% p.a.) was maintained. The gearing level of MQREIT remained unchanged at 37% which is still below the limit of 50%.
- **Outlook:** Despite the lacklustre overall office market, MQREIT's office space will remain stable and well-guarded from its long weighted average term to expiry (5.5 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

- Maintained.

Rating

BUY ↔, TP: RM1.48 ↔

- 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 allowed MQREIT to enjoy greater operating efficiency arising from economies of scale.

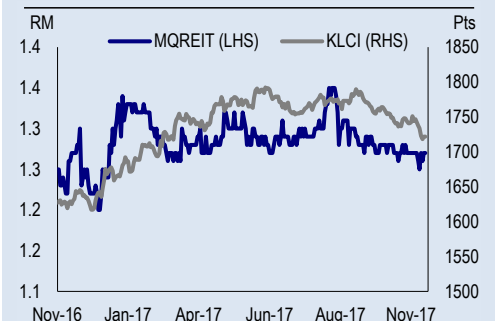
Valuation

- Maintain **BUY** with unchanged TP of **RM1.48** with unchanged targeted yield of 6.2%.

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KLCI	1721.7
Expected share price return	16.5%
Expected dividend return	6.9%
Expected total return	23.5%

Share price



Information

Bloomberg Ticker	MQREITMK
Bursa Code	5123
Issued Shares (m)	1,068
Market cap (RM m)	1,356
3-mth avg. volume ('000)	333

Price Performance

	1M	3M	12M
Absolute	0.0	-5.9	3.3
Relative	1.1	-2.9	-2.6

Major Shareholders

MRCB	27.9%
Capita Commercial Trust	11.0%
EPF	7.2%

Summary Earnings Table

FYE Dec (RMm)	2016A	2017E	2018F	2019F
Revenue	136.6	185.3	189.1	192.9
NPI	107.2	140.3	143.1	146.0
Net invest income	108.2	141.9	144.4	146.7
PAT	62.8	87.9	91.0	93.3
EPU (sen)	9.3	8.2	8.4	8.6
Norm. PER (x)	14.4	15.5	15.1	14.8
FD PER (x)	14.4	15.5	15.1	14.8
EV/EBITDA (x)	17.9	17.4	17.1	16.9
Net DPU (sen)	8.4	8.8	9.2	9.2
Distrib. yield (%)	6.6	7.0	7.2	7.3
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)	3Q16	2Q17	3Q17	QoQ (%)	YoY (%)	Comments
Gross revenue	32.5	45.1	44.8	-0.6	37.9	YoY: Higher due to additional revenue from Menara Shell and higher rental income post rent adjustment from QB2, QB3, QB5 and Wisma Technip.
Property operating expenses	-7.0	-10.2	-10.5	-3.6	-51.2	Higher due to acquisition of Menara Shell.
Net property income	25.5	34.9	34.3	-1.8	34.3	
Interest income	0.5	0.6	0.7	15.1	57.3	Higher due to higher bank balances.
Gain on divestment	0.0	0.0	0.0	NM	NM	
Net investment income	26.0	35.6	35.0	-1.5	34.7	
Finance costs	-8.1	-9.8	-10.0	-1.1	-22.8	Increase due to higher borrowings incurred to finance Menara Shell.
Valuation fees	-0.1	-0.1	-0.1	0.0	-31.1	
Administrative expenses	-0.0	0.0	-0.0	1,570.0	-77.8	
Total Expenses	-10.8	-13.5	-13.7	-1.0	-26.7	
Normalised PBT	15.2	22.0	21.4	-3.0	40.4	
Normalised PAT	15.2	22.0	21.4	-3.0	40.4	
EPU (realised)	2.30	2.26	2.00	-11.5	-13.0	Due to higher share base from placement exercise (excl. the divestment gain).
DPU (sen)	0.00	4.23	0.00	-100.0	NM	

Company Data, HLIB

Figure #2 Cumulative Results Comparison

FYE Dec (RMm)	9MFY16	9MFY17	YoY (%)	Comments
Gross revenue	97.7	135.5	38.6	Additional revenue arising from the acquisition of Menara Shell on 22 Dec 2016 and higher rental rates for QB2, QB3, QB5 and Wisma Technip.
Property operating expenses	-21.0	-30.1	-43.2	Higher due to acquisition of Menara Shell.
Net property income	76.7	105.3	37.4	
Interest income	1.2	1.8	48.6	
Gain on divestment	0.0	0.0	NM	
Net investment income	77.9	107.2	37.5	
Finance costs	-23.9	-29.5	-23.3	Higher due to financial drawdown to fund acquisitions.
Valuation fees	-0.2	-0.2	-14.3	
Administrative expenses	-0.2	-0.1	59.1	
Total Expenses	-32.1	-40.6	-26.5	
Normalised PBT	45.8	66.6	45.3	
Normalised PAT	45.8	66.6	45.3	Higher net property income and interest income, net of finance cost and expense.
EPU (realised)	6.93	6.23	-10.0	
DPU (sen)	4.23	4.23	0.0	

Company Data, HLIB

Figure #3 9MFY17 Results vs. HLIB's Estimates and Consensus

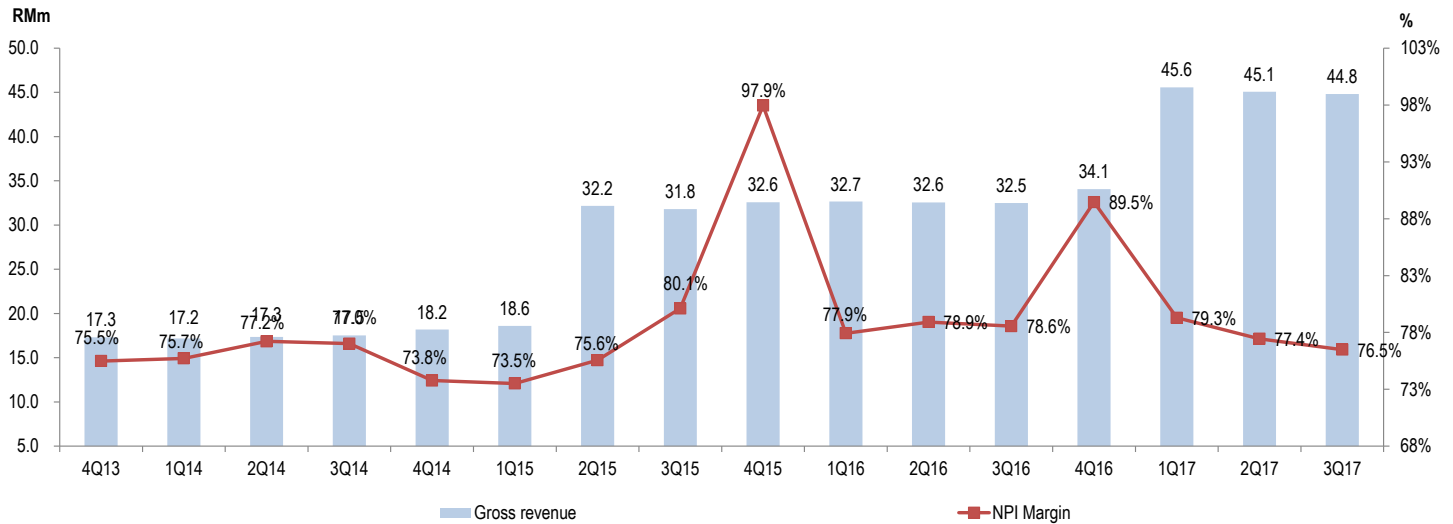
	Actual 9MFY17	HLIB FY17	Actual vs. HLIB (%)	Consensus FY17	Actual vs. Consensus (%)	Comments
Revenue	135.5	185.3	73.1	183.4	73.8	In line.
Normalised PAT	66.6	87.9	75.7	90.0	74.0	In line.
EPU (sen)	6.2	8.2	76.0	8.5	73.4	In line.
DPU (sen)	4.2	8.8	47.8	8.1	52.2	In line.

Company Data, HLIB, Bloomberg

Figure #4 HLIB Forecasts vs. Consensus

RMm	FY18F			FY19F		
	HLIB	Consensus	%	HLIB	Consensus	%
Normalised PAT	89.3	93.5	(4.5)	91.5	96.7	(5.4)
DPU (sen)	9.0	8.2	10.1	9.1	8.4	8.1

HLIB, Bloomberg

Figure #5 Gross Revenue & NPI Margin

HLIB, Bloomberg

Figure #6 Peers Comparison

Company	FYE	Price		Market Cap (m)	P/E (x)		P/B (x)		Gross DY (%)
					2017	2018	2017	2018	
Amanah Harta Tanah PNB	Dec	RM	0.85	185.9	NA	NA	NA	NA	6.39
Al'Aqar Healthcare REIT	Dec	RM	1.44	1,048.6	16.0	15.3	NA	NA	5.63
AmFIRST Real Estate Investment Trust	Mar	RM	0.71	487.3	NA	NA	NA	NA	6.00
Amanahraya Real Estate Investment Trust	Dec	RM	0.94	536.0	14.8	14.0	NA	NA	6.52
Atrium Real Estate Investment Trust	Dec	RM	1.11	135.2	NA	NA	NA	NA	6.67
Axis Real Estate Investment Trust	Dec	RM	1.50	1,823.5	17.2	17.4	1.2	1.2	5.73
CapitaMalls Malaysia Trust	Dec	RM	1.46	3,397.8	17.2	16.2	1.1	1.1	5.89
Hektar Real Estate Investment Trust	Dec	RM	1.26	582.1	12.6	12.6	0.8	0.9	7.14
IGB Real Estate Investment Trust	Dec	RM	1.62	5,877.2	19.5	18.4	1.6	1.6	5.80
KIP Real Estate Investment Trust	Jun	RM	0.91	457.3	13.1	12.7	0.9	0.9	7.62
KLCCP Stapled Group	Dec	RM	7.80	14,424.6	18.8	18.3	0.9	0.9	4.92
MRCB-Quill Real Estate Investment Trust	Dec	RM	1.27	1,377.7	15.5	15.1	1.0	1.0	6.93
Pavilion Real Estate Investment Trust	Dec	RM	1.65	5,235.5	21.7	18.1	1.3	1.3	4.73
Al-Salam Real Estate Investment Trust	Mar	RM	1.00	580.0	15.4	14.3	0.9	0.9	6.00
Sunway Real Estate Investment Trust	Jun	RM	1.67	5,095.0	16.7	16.1	1.2	1.2	5.99
Tower Real Estate Investment Trust	Dec	RM	1.20	336.6	NA	NA	NA	NA	5.78
UOA Real Estate Investment Trust	Dec	RM	1.64	693.5	NA	NA	NA	NA	5.10
YTL Hospitality REIT	Jun	RM	1.21	2,062.3	14.9	14.2	0.9	0.9	6.61
Average					16.8	15.9	1.1	1.1	6.0

HLIB, Bloomberg

MRCB-Quill REIT (BUY, TP: RM1.48, CP: RM1.27)**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	10.9	13.9	14.2	14.4
Other revenue	5.4	5.0	5.7	5.8	5.9
Total Revenue	120.3	136.6	185.3	189.1	192.9
Assessment & quit rent	(4.5)	(5.3)	(7.8)	(7.9)	(8.1)
Depreciation	(0.0)	(0.1)	(0.0)	(0.0)	(0.0)
Insurance	(0.7)	(0.7)	(1.1)	(1.1)	(1.1)
Property management fees	(2.2)	(2.3)	(5.0)	(5.1)	(5.2)
Service contracts	(7.3)	(9.6)	(12.9)	(13.2)	(13.5)
Utilities	(10.2)	(11.5)	(18.2)	(18.6)	(19.0)
Total Opex	(24.9)	(29.5)	(45.0)	(45.9)	(46.8)
Net property income	95.4	107.2	140.3	143.1	146.0
Net investment income	99.1	108.2	141.9	144.4	146.7
Pretax profit	60.7	62.8	87.9	91.0	93.3
Taxation	0.0	0.0	0.0	1.0	2.0
Net profit	53.4	59.2	87.9	91.0	93.3
No of units (m)	596.0	672.5	1,074.1	1,081.3	1,088.5
EPU (sen)	10.2	9.3	8.2	8.4	8.6

Cash Flows

FYE Dec (RM m)	2015A	2016A	2017E	2018F	2019F
PBT	60.7	62.8	87.9	91.0	93.3
Finance costs	28.0	33.0	0.0	0.0	0.0
Depreciation	0.0	0.1	0.1	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)	(23.3)	0.3	0.3
Operating cashflow	59.0	70.3	64.6	91.4	93.6
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)	(87.0)	(90.1)	(91.4)
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	(76.1)	(107.1)	(91.4)

Balance Sheet

FYE Dec (RM m)	2015A	2016A	2017E	2018F	2019F
PPE	0.2	0.2	0.2	0.2	0.1
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	2,226.9	2,228.9	2,230.9
Trade receivables	6.1	18.3	17.4	17.7	18.1
Cash	44.9	54.1	40.5	22.8	23.0
Total Current Assets	51.7	72.4	57.9	40.5	41.0
Total assets	1,625.3	2,297.3	2,284.8	2,269.4	2,271.9
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	131.4
Total Equity	903.9	1,359.7	1,360.6	1,361.5	1,363.4
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	31.5	32.1	32.8
Total liabilities	721.5	937.6	924.3	907.9	908.5
Total liabilities & equity	1,625.3	2,297.3	2,284.8	2,269.4	2,271.9

Valuation Ratios

FYE Dec (RM m)	2015A	2016E	2017E	2018F	2019F
EPU before mgr's fee	9.0	8.8	8.2	8.4	8.6
EPU after mgr's fee	10.2	9.3	8.2	8.4	8.6
PER (x)	14.2	14.4	15.5	15.1	14.8
No of units	596.0	672.5	1,074.3	1,081.7	1,089.2
Net DPU	8.5	8.4	8.8	9.2	9.2
Net DY (%)	6.7	6.6	7.0	7.2	7.3
NTA/ share (sen)	151.0	201.3	126.0	125.1	124.3
P/NTA (x)	0.8	0.6	1.0	1.0	1.0
FCF/ share (sen)	16.2	19.5	13.3	18.5	17.2
FCF yield (%)	12.7	15.4	10.5	14.6	13.5
Enterprise value	1,401.8	1,651.6	2,186.4	2,196.6	2,205.8
EV/ EBITDA (x)	17.1	17.9	17.4	17.1	16.9
ROE (%)	6.7	4.6	6.5	6.7	6.8
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)	0.8	0.6	1.0	1.0	1.0

Assumption metrics

Gross Rental Income	2017F	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)	3Q16	2Q17	3Q17	QoQ (%)	YoY (%)
Gross revenue	32.5	45.1	44.8	(0.6)	37.9
Property operating expenses	(7.0)	(10.2)	(10.5)	(3.6)	(51.2)
Net property income	25.5	34.9	34.3	(1.8)	34.3
Interest income	0.5	0.6	0.7	15.1	57.3
Revaluation gains	0.0	0.0	0.0	NM	NM
Net investment income	26.0	35.6	35.0	(1.5)	34.7
Finance costs	(8.1)	(9.8)	(10.0)	(1.1)	(22.8)
Valuation fees	(0.1)	(0.1)	(0.1)	0.0	(31.1)
Administrative expenses	(0.0)	0.0	(0.0)	1,570.0	(77.8)
Total Expenses	(10.8)	(13.5)	(13.7)	(1.0)	(26.7)
Normalised PBT	15.2	22.0	21.4	(3.0)	40.4
Normalised PAT	15.2	22.0	21.4	(3.0)	40.4
EPU after mgmt fee	2.3	2.3	2.0	(11.5)	(13.0)
DPU (sen)	0	4	0	(100.0)	NM

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Equity rating definitions

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.
HOLD	Neutral recommendation of stock under coverage. Expected absolute return between -10% and +10% over 12-months, with low risk of sustained downside.
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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.
UNDERWEIGHT	The sector, based on weighted market capitalization, is expected to have absolute return of less than -5% over 12-months.