



MRCB-Quill REIT (MQREIT MK) : BUY

Mkt. Cap: US\$276m | **3m Avg. Daily Val:** US\$0.02m

Last Traded Price (27 Nov 2018): RM1.08

Price Target 12-mth: RM1.24 (14% upside) (Prev RM1.27)

Analyst

Siti Ruzanna Mohd Faruk +603 2604 3965; sruzannamf@alliancedbs.com

No surprises

- 3QFY18 earnings came in line with expectations
- Lower income from Sentral plus loss of income from Quil Building 8
- Factored in weak rental reversions; dividend yield still attractive
- Maintain BUY with lower TP of RM1.24

Forecasts and Valuation

| FY Dec (RMm) | 2017A | 2018F | 2019F | 2020F |
|------------------------|-------|-------|-------|-------|
| Gross Revenue | 180 | 175 | 180 | 184 |
| Net Property Inc | 140 | 134 | 136 | 136 |
| Total Return | 69.9 | 84.8 | 85.3 | 85.5 |
| Distribution Inc | 89.6 | 82.2 | 82.7 | 82.9 |
| EPU (sen) | 6.55 | 7.91 | 7.94 | 7.95 |
| EPU Gth (%) | 12 | 21 | 0 | 0 |
| DPU (sen) | 8.39 | 7.67 | 7.70 | 7.71 |
| DPU Gth (%) | 62 | (9) | 0 | 0 |
| NAV per shr (sen) | 130 | 130 | 130 | 130 |
| PE (X) | 16.5 | 13.7 | 13.6 | 13.6 |
| Distribution Yield (%) | 7.8 | 7.1 | 7.1 | 7.1 |
| P/NAV (x) | 0.8 | 0.8 | 0.8 | 0.8 |
| Aggregate Leverage (%) | 37.5 | 37.7 | 37.9 | 38.1 |
| ROAE (%) | 5.1 | 6.1 | 6.1 | 6.1 |

Source of all data on this page: Company, AllianceDBS, Bloomberg Finance L.P

What's New

3QFY18 results within expectations

MQREIT's 3QFY18 core net distributable income came in at RM20.6m (-3.7% y-o-y). This brings 9MFY18 distributable income to RM62.9m (-5.6% y-o-y). This is in line with our expectations but slightly below consensus.

The decrease for the quarter was mainly due to lower revenue generated from Platinum Sentral as well as loss of revenue from the disposal of QB8 – DHL XPJ which took place on 12 April 2018.

Property operating expenses inched down to RM9.9m (-5.8% y-o-y) as it tightened control on costs and reduced expenses from the disposal of QB8. NPI for the quarter came in at RM33.3m (-2.8% y-o-y).

Stable occupancy, some lease expiries coming up

Portfolio occupancy came down to 94% vs 96% in 2QFY18. About 28.0% of total NLA is due for renewal in FY18, of which c.9.0% have been renewed. The expiring leases in FY19 form 15% of total NLA, and 17% in FY20. We believe rental reversions were flattish, as per guidance by management, as it focused on tenant retention to cope with a challenging operating environment.

Going forward, we expect some challenges in negotiating positive rental reversions due to the oversupply of office space in the market.

Outlook

MRCB connection. MQREIT has the right of first refusal to MRCB's stable of investment properties, which is worth up to RM1.5bn in aggregate. Notable assets include Ascott Sentral (serviced apartments), Plaza Alam Sentral (retail),



Sooka Sentral (lifestyle/retail) and Kompleks Sentral (industrial). The REIT may also acquire office assets from the Quill Group, the original sponsor of MQREIT with a remaining stake of c.11%. However, MQREIT's current gearing of c.37% indicates that new equity issuance will likely be necessary for sizeable acquisitions in the near term.

Valuation

We maintain our BUY recommendation with a lower TP of RM1.24 as we factor in a higher risk-free rate of 4.2% vs 4.0% previously. Despite factoring in flat rental reversions, FY18 dividend yields are attractive at 7.1%. MQREIT's appeal is the availability of an asset acquisition pipeline of completed investment properties from MRCB. Confirmation of injections at accretive yields will be a re-rating catalyst for the stock. Our DDM-derived TP employs 7.5% cost of equity and 1% terminal growth.

Quarterly Income Statement (RMm)

| FY Dec | 3Q2017 | 2Q2018 | 3Q2018 | % chg yoy | % chg qoq |
|-----------------------------|-------------|-------------|-------------|--------------|---------------|
| Gross revenue | 44.8 | 43.4 | 43.3 | (3.5) | (0.3) |
| Property expenses | (10.5) | (10.0) | (9.9) | (5.8) | (1.2) |
| Net Property Income | 34.3 | 33.4 | 33.3 | (2.8) | (0.1) |
| Other Operating expenses | (3.7) | (3.0) | (3.7) | 0.0 | 22.7 |
| Other Non Opg (Exp)/Inc | 0.0 | 0.0 | 0.0 | N/A | N/A |
| Net Interest (Exp)/Inc | (9.2) | (9.1) | (9.1) | 1.7 | 0.1 |
| Exceptional Gain/(Loss) | 0.0 | 2.20 | 0.0 | N/A | N/A |
| Net Income | 21.4 | 23.5 | 20.6 | (3.7) | (12.3) |
| Tax | 0.0 | 0.0 | 0.0 | N/A | N/A |
| Minority Interest | 0.0 | 0.0 | 0.0 | N/A | N/A |
| Net Income after Tax | 21.4 | 23.5 | 20.6 | (3.7) | (12.3) |
| Total Return | 21.4 | 23.5 | 20.6 | (3.7) | (12.3) |
| Non-tax deductible Items | 0.0 | 0.0 | 0.0 | nm | nm |
| Net Inc available for Dist. | 21.4 | 21.3 | 20.6 | (3.7) | (3.3) |
| Ratio (%) | | | | | |
| Net Prop Inc Margin | 76.5 | 76.9 | 77.1 | | |
| Dist. Payout Ratio | 0.0 | 101.9 | 0.0 | | |

Source of all data: Company, AllianceDBS

Target Price & Ratings History



| S.No. | Date of Report | Closing Price | 12-mth Target Price | Rating |
|-------|----------------|---------------|---------------------|--------|
| 1: | 09 Jan 18 | 1.20 | 1.38 | HOLD |
| 2: | 22 Jan 18 | 1.24 | 1.27 | HOLD |
| 3: | 18 May 18 | 1.10 | 1.27 | BUY |
| 4: | 09 Aug 18 | 1.18 | 1.27 | BUY |

Note: Share price and Target price are adjusted for corporate actions.

Source: AllianceDBS

Analyst: Siti Ruzanna Mohd Faruk

DISCLOSURE

Stock rating definitions

| | | |
|--------------|---|--|
| STRONG BUY | - | > 20% total return over the next 3 months, with identifiable share price catalysts within this time frame |
| BUY | - | > 15% total return over the next 12 months for small caps, >10% for large caps |
| HOLD | - | -10% to +15% total return over the next 12 months for small caps, -10% to +10% for large caps |
| FULLY VALUED | - | negative total return > -10% over the next 12 months |
| SELL | - | negative total return of > -20% over the next 3 months, with identifiable catalysts within this time frame |

Commonly used abbreviations

| | | |
|--|---------------------------|---|
| Adex = advertising expenditure | EPS = earnings per share | PBT = profit before tax |
| bn = billion | EV = enterprise value | P/B = price / book ratio |
| BV = book value | FCF = free cash flow | P/E = price / earnings ratio |
| CF = cash flow | FV = fair value | PEG = P/E ratio to growth ratio |
| CAGR = compounded annual growth rate | FY = financial year | q-o-q = quarter-on-quarter |
| Capex = capital expenditure | m = million | RM = Ringgit |
| CY = calendar year | M-o-m = month-on-month | ROA = return on assets |
| Div yld = dividend yield | NAV = net assets value | ROE = return on equity |
| DCF = discounted cash flow | NM = not meaningful | TP = target price |
| DDM = dividend discount model | NTA = net tangible assets | trn = trillion |
| DPS = dividend per share | NR = not rated | WACC = weighted average cost of capital |
| EBIT = earnings before interest & tax | p.a. = per annum | y-o-y = year-on-year |
| EBITDA = EBIT before depreciation and amortisation | PAT = profit after tax | YTD = year-to-date |

DISCLAIMER

This report has been prepared for information purposes only by AllianceDBS Research Sdn Bhd ("ADBSR"), a subsidiary of Alliance Investment Bank Berhad ("AIBB") and an associate of DBS Vickers Securities Holdings Pte Ltd ("DBSVH"). DBSVH is a wholly-owned subsidiary of DBS Bank Ltd. This report is strictly confidential and is meant for circulation to clients of ADBSR, AIBB and DBSVH only or such persons as may be deemed eligible to receive such research report, information or opinion contained herein. Receipt and review of this report indicate your agreement not to distribute, reproduce or disclose in any other form or medium (whether electronic or otherwise) the contents, views, information or opinions contained herein without the prior written consent of ADBSR.

This report is based on data and information obtained from various sources believed to be reliable at the time of issuance of this report and any opinion expressed herein is subject to change without prior notice and may differ or be contrary to opinions expressed by ADBSR's affiliates and/or related parties. ADBSR does not make any guarantee, representation or warranty (whether express or implied) as to the accuracy, completeness, reliability or fairness of the data and information obtained from such sources as may be contained in this report. As such, neither ADBSR nor its affiliates and/or related parties shall be held liable or responsible in any manner whatsoever arising out of or in connection with the reliance and usage of such data and information or third party references as may be made in this report (including, but not limited to any direct, indirect or consequential losses, loss of profits and damages).

The views expressed in this report reflect the personal views of the analyst(s) about the subject securities or issuers and no part of the compensation of the analyst(s) was, is, or will be directly or indirectly related to the inclusion of specific recommendation(s) or view(s) in this report. ADBSR prohibits the analyst(s) who prepared this report from receiving any compensation, incentive or bonus based on specific investment banking transactions or providing a specific recommendation for, or view of, a particular company.

This research report provides general information only and is not to be construed as an offer to sell or a solicitation to buy or sell any securities or other investments or any options, futures, derivatives or other instruments related to such securities or investments. In particular, it is highlighted that this report is not intended for nor does it have regard to the specific investment objectives, financial situation and particular needs of any specific person who may receive this report. Investors are therefore advised to make their own independent evaluation of the information contained in this report, consider their own individual investment objectives, financial situations and particular needs and consult their own professional advisers (including but not limited to financial, legal and tax advisers) regarding the appropriateness of investing in any securities or investments that may be featured in this report.

ADBSR, AIBB, DBSVH and DBS Bank Ltd, their directors, representatives and employees or any of their affiliates or their related parties may, from time to time, have an interest in the securities mentioned in this report. AIBB, DBSVH and DBS Bank Ltd, their affiliates and/or their related persons may do and/or seek to do business with the company(ies) covered in this report and may from time to time act as market maker or have assumed an underwriting commitment in securities of such company(ies), may sell or buy such securities from customers on a principal basis and may also perform or seek to perform significant investment banking, advisory or underwriting services for or relating to such company(ies) as well as solicit such investment, advisory or other services from any entity mentioned in this report.

AIBB, DBSVH, DBS Bank Ltd (which carries on, inter alia, corporate finance activities) and their activities are separate from ADBSR. AIBB, DBSVH and DBS Bank Ltd may have no input into company-specific coverage decisions (i.e. whether or not to initiate or terminate coverage of a particular company or securities in reports produced by ADBSR) and ADBSR does not take into account investment banking revenues or potential revenues when making company-specific coverage decisions.

ADBSR, AIBB, DBSVH, DBS Bank Ltd and/or other affiliates of DBS Vickers Securities (USA) Inc ("DBSVUSA"), a U.S.-registered broker-dealer, may beneficially own a total of 1% or more of any class of common equity securities of the subject company mentioned in this report. ADBSR, AIBB, DBSVH, DBS Bank Ltd and/or other affiliates of DBSVUSA may, within the past 12 months, have received compensation and/or within the next 3 months seek to obtain compensation for investment banking services from the subject company. DBSVUSA does not have its own investment banking or research department, nor has it participated in any investment banking transaction as a manager or co-manager in the past twelve months. Any US persons wishing to obtain further information, including any clarification on disclosures in this disclaimer, or to effect a transaction in any security discussed in this report should contact DBSVUSA exclusively. DBS Vickers Securities (UK) Ltd is an authorised person in the meaning of the Financial Services and Markets Act and is regulated by The Financial Services Authority. Research distributed in the UK is intended only for institutional clients.

In reviewing this report, an investor should be aware that any or all of the foregoing, among other things, may give rise to real or potential conflicts of interest. Additional information is, subject to the overriding issue of confidentiality, available upon request to enable an investor to make their own independent evaluation of the information contained herein.



Wong Ming Tek, Executive Director

Published by
AllianceDBS Research Sdn Bhd (128540 U)
19th Floor, Menara Multi-Purpose, Capital Square, 8 Jalan Munshi Abdullah, 50100 Kuala Lumpur, Malaysia.
Tel.: +603 2604 3333 Fax: +603 2604 3921 email : general@alliancedbs.com