

Company Update

MRCB-Quill REIT



Bloomberg: MQREIT MK | Reuters: MQRE.KL

Refer to important disclosures at the end of this report

AllianceDBS Research, Malaysia Equity

12 Nov 2020

BUY

Last Traded Price (11 Nov 2020): RM0.795 (KLCI : 1,570.08)

Price Target 12-mth: RM1.20 (51% upside) (Prev RM1.10)

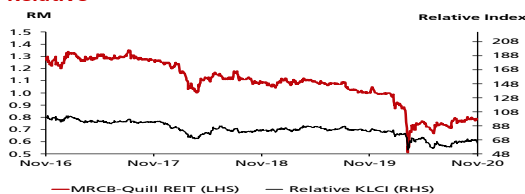
Analyst

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

What's New

- 3MFY20 earnings grew 22% y-o-y and 13% q-o-q; above expectations
- Steady revenue growth coupled with lower interest expense boosted bottomline
- Raise FY20-22F earnings by 4% factoring in lower cost of debt
- Reiterate BUY with higher TP of RM1.20; MQREIT is our top pick in the sector

Price Relative



Forecasts and Valuation

FY Dec (RMm)	2019A	2020F	2021F	2022F
Gross Revenue	162	167	171	176
Net Property Inc	123	124	125	126
Total Return	29.1	77.5	76.9	77.6
Distribution Inc	72.9	77.5	76.9	77.6
EPU (sen)	2.72	7.23	7.17	7.24
EPU Gth (%)	(60)	166	(1)	1
DPU (sen)	6.80	7.23	7.17	7.24
DPU Gth (%)	(16)	6	(1)	1
NAV per shr (sen)	123	123	123	123
PE (X)	29.3	11.0	11.1	11.0
Distribution Yield (%)	8.6	9.1	9.0	9.1
P/NAV (x)	0.6	0.6	0.6	0.6
Aggregate Leverage (%)	37.8	38.0	38.3	38.5
ROAE (%)	2.2	5.9	5.8	5.9

Distn. Inc Chng (%):	4	4	4
Consensus DPU (sen):	6.20	6.60	5.30
Other Broker Recs:	B: 6	S: 0	H: 2

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

Standout earnings; fantastic buying opportunity

Investment Thesis

Reiterate BUY. We expect the group to register resilient earnings given its high-quality tenant base, strategically-located assets and long-term leases. This has helped the group successfully keep its portfolio occupancy rate high at 90.5%. Coupled with savings from lower interest expenses, MQREIT registered solid 3QFY20 earnings.

Yields are attractive at this juncture. MQREIT currently offers attractive yields at c.9.3% vs. our REIT universe average of 5.4%. The group is also trading at a 35% discount to NAV of RM1.20. We believe the stock is undervalued and offers an attractive buying opportunity.

Expiry profile is relatively manageable with 14%-21% of total NLA due for renewal in FY20-22F. Solid tenant list includes many multinational corporations (MNCs) requiring high-quality and well-managed assets.

Valuation:

Our DDM derived target price (TP) is RM1.20. Our TP factors in 7.4% cost of equity and 1.0% terminal growth.

Where we differ:

Solid tenant base underappreciated: We believe MQREIT is oversold given its 35% discount to NAV. In our view, the stock should re-rate as it demonstrates its portfolio is relatively unaffected by the pandemic and delivers steady dividends.

Key Risks to Our View:

Delayed leasing could be a drag on earnings. The office sector faces challenges due to excess supply, especially in Kuala Lumpur and Cyberjaya where the REIT has exposure. Delayed leasing of released spaces may result in reduced earnings.

At A Glance

Issued Capital (m shrs)	1,072
Mkt. Cap (RMm/US\$m)	852 / 206
Major Shareholders (%)	
Malaysian Resources Corp	27.9
Quill group of companies	5.5
Capitaland Financial Ltd	10.9
Free Float (%)	28.4
3m Avg. Daily Val (US\$m)	0.10

GIC Industry : Real Estate / Equity Real Estate Investment (REITs)



MRCB-Quill REIT

WHAT'S NEW

Portfolio remains steady amid stormy weather

What's New

3QFY20 results above expectations. MRCB-Quill REIT's (MQREIT) 3QFY20 core earnings came in at RM21.5m (+21.8% y-o-y; +12.6% q-o-q). This brings 9MFY20 earnings to RM60.3m, which is ahead of our and consensus expectations.

The higher 3QFY20 earnings were mainly due to higher revenue generated from Menara Shell, Wisma Technip and Tesco Building Penang. Revenue came in at RM42.1m (+5.4% y-o-y; +4.9% q-o-q). This was backed by higher portfolio occupancy of 90% in 3QFY20 vs. 89% in 3QFY19.

Property operating expenses amounted to RM9.3m (-4.3% y-o-y; +1.8% q-o-q), as MQREIT incurred less expenses for some properties. This resulted in a higher net property income (NPI) for the quarter of RM33.4m (+8.0% y-o-y; +5.9% q-o-q).

Outlook

Occupancy steady; more room to grow. MQREIT's portfolio occupancy remained steady at 90% in 3QFY20 vs. 89% in 3QFY19. We understand that there were higher occupancies for Platinum Sentral and Wisma Technip. MQREIT is still looking for tenants to replace the vacancy in QB5 after its tenant IBM moved out in 1Q19.

About 19.0% of MQREIT's total NLA is expiring in FY20, of which c.11% has been renewed. It has another 7% of leases expiring in 4Q20. We understand that rental reversions were

flattish, as MQREIT prioritised tenant retention to cope with a challenging operating environment.

Bump up earnings for lower interest expense. MQREIT has 54% of its debt under floating rates that benefited from the lower overnight policy rate (OPR). As such, finance cost incurred during the quarter was 14.4% lower y-o-y and 8.3% lower q-o-q. Average cost of debt for the quarter was 4.09% compared to 4.22% in 2Q20. We have adjusted our average cost of debt to reflect the lower rate, which increased our FY20-22F earnings forecast by 4%.

Valuation and Recommendation

We maintain our BUY call with a higher TP of RM1.20. Its current valuation offers an attractive yield of 9.3%; the highest among its peers. We believe the negatives of an office supply glut have been overly priced in at its current valuation level. Despite factoring in conservative assumptions for MQREIT, the stock still offers ample upside with attractive distribution yields.

Company Background

MRCB-Quill REIT is a real estate investment trust that focuses on office properties. Its largest asset is Platinum Sentral with 445k-sq-ft NLA in the Kuala Lumpur Sentral transport hub. Its other assets include five office assets in Cyberjaya, one retail/commercial asset, one industrial asset and one hypermarket.

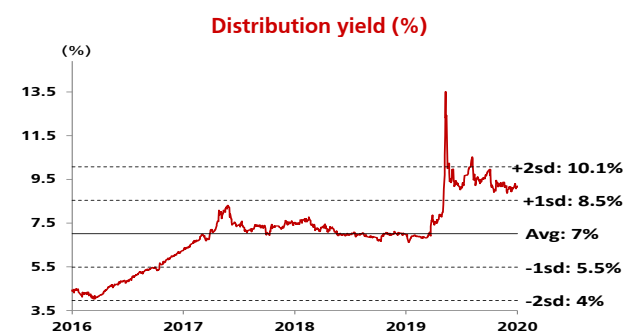
MRCB-Quill REIT

Quarterly Income Statement (RMm)

FY Dec	3Q2019	2Q2020	3Q2020	% chg yoy	% chg qoq
Gross revenue	39.9	40.1	42.1	5.4	4.9
Property expenses	(9.7)	(9.1)	(9.3)	(4.3)	1.8
Net Property Income	30.2	31.0	32.8	8.5	5.8
Other Operating expenses	(3.5)	(3.5)	(3.6)	1.8	1.9
Other Non Opg (Exp)/Inc	0.0	0.0	0.0	N/A	N/A
Associates & JV Inc	0.0	0.0	0.0	nm	nm
Net Interest (Exp)/Inc	(9.0)	(8.4)	(7.7)	14.9	8.1
Exceptional Gain/(Loss)	0.0	0.0	0.0	N/A	N/A
Net Income	17.6	19.1	21.5	21.8	12.6
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	17.6	19.1	21.5	21.8	12.6
Total Return	17.6	19.1	21.5	21.8	12.6
Non-tax deductible Items	0.0	0.0	0.0	nm	nm
Net Inc available for Dist.	17.6	19.1	21.5	21.8	12.6
Ratio (%)					
Net Prop Inc Margin	75.6	77.2	77.9		
Dist. Payout Ratio	0.0	94.6	90.6		

Source of all data: Company, AllianceDBS

Historical Dividend yield and PB band



Source: Bloomberg Finance L.P., AllianceDBS estimates



Source: Bloomberg Finance L.P., AllianceDBS estimates

MRCB-Quill REIT**Key Assumptions**

FY Dec	2018A	2019A	2020F	2021F	2022F
Portfolio NLA (k sq ft)	2,214.8	2,214.8	2,214.8	2,214.8	2,214.8
Agg. occupancy rate (%)	96%	90%	90%	90%	90%

Income Statement (RMm)

FY Dec	2018A	2019A	2020F	2021F	2022F
Gross revenue	173	162	167	171	176
Property expenses	(39.7)	(39.2)	(43.3)	(46.6)	(50.2)
Net Property Income	134	123	124	125	126
Other Operating expenses	(14.9)	(14.4)	(13.6)	(13.6)	(13.7)
Other Non Opg (Exp)/Inc	0.0	0.0	0.0	0.0	0.0
Associates & JV Inc	0.0	0.0	0.0	0.0	0.0
Net Interest (Exp)/Inc	(36.3)	(36.4)	(32.8)	(34.3)	(34.6)
Exceptional Gain/(Loss)	(9.4)	(43.0)	0.0	0.0	0.0
Net Income	73.1	29.1	77.5	76.9	77.6
Tax	0.0	0.0	0.0	0.0	0.0
Minority Interest	0.0	0.0	0.0	0.0	0.0
Preference Dividend	0.0	0.0	0.0	0.0	0.0
Net Income After Tax	73.1	29.1	77.5	76.9	77.6
Total Return	73.1	29.1	77.5	76.9	77.6
Non-tax deductible Items	(13.5)	(43.8)	0.0	0.0	0.0
Net Inc available for Dist.	86.6	72.9	77.5	76.9	77.6
Growth & Ratio					
Revenue Gth (%)	(3.7)	(6.5)	3.1	2.5	2.8
N Property Inc Gth (%)	(4.5)	(8.1)	0.8	0.7	0.8
Net Inc Gth (%)	4.6	(60.2)	166.1	(0.8)	0.9
Dist. Payout Ratio (%)	105.0	101.1	100.0	100.0	100.0
Net Prop Inc Margins (%)	77.1	75.8	74.1	72.8	71.5
Net Income Margins (%)	42.2	18.0	46.4	44.9	44.1
Dist to revenue (%)	49.9	45.0	46.4	44.9	44.1
Managers & Trustee's fees	8.6	8.9	8.1	8.0	7.8
ROAE (%)	5.3	2.2	5.9	5.8	5.9
ROA (%)	3.2	1.3	3.5	3.4	3.5
ROCE (%)	5.3	4.9	5.0	5.0	5.1
Int. Cover (x)	3.3	3.0	3.4	3.2	3.2

Source: Company, AllianceDBS

MRCB-Quill REIT**Quarterly Income Statement (RMm)**

FY Dec	3Q2019	4Q2019	1Q2020	2Q2020	3Q2020
Gross revenue	39.9	42.0	41.7	40.1	42.1
Property expenses	(9.7)	(10.5)	(9.4)	(9.1)	(9.3)
Net Property Income	30.2	31.5	32.3	31.0	32.8
Other Operating expenses	(3.5)	(3.8)	(3.5)	(3.5)	(3.6)
Other Non Opg (Exp)/Inc	0.0	0.0	0.0	0.0	0.0
Associates & JV Inc	0	0	0	0	0
Net Interest (Exp)/Inc	(9.0)	(9.1)	(9.0)	(8.4)	(7.7)
Exceptional Gain/(Loss)	0.0	(43.0)	0.0	0.0	0.0
Net Income	17.6	(24.4)	19.8	19.1	21.5
Tax	0.0	0.0	0.0	0.0	0.0
Minority Interest	0.0	0.0	0.0	0.0	0.0
Net Income after Tax	17.6	(24.4)	19.8	19.1	21.5
Total Return	17.6	(24.4)	19.8	19.1	21.5
Non-tax deductible Items	0.0	(36.7)	0.0	0.0	0.0
Net Inc available for Dist.	17.6	18.6	19.8	19.1	21.5
Growth & Ratio					
Revenue Gth (%)	3	5	(1)	(4)	5
N Property Inc Gth (%)	4	4	2	(4)	6
Net Inc Gth (%)	7	(238)	(181)	(4)	13
Net Prop Inc Margin (%)	75.6	75.0	77.4	77.2	77.9
Dist. Payout Ratio (%)	0.0	49.5	0.0	94.6	90.6

Balance Sheet (RMm)

FY Dec	2018A	2019A	2020F	2021F	2022F
Investment Properties	2,179	2,144	2,154	2,163	2,171
Other LT Assets	0.35	0.36	0.36	0.36	0.36
Cash & ST Invt	85.8	63.3	63.9	64.5	65.2
Inventory	0.0	0.0	0.0	0.0	0.0
Debtors	6.34	6.31	6.50	6.67	6.85
Other Current Assets	0.0	0.0	0.0	0.0	0.0
Total Assets	2,271	2,214	2,224	2,234	2,243
ST Debt	0.0	333	343	352	360
Creditor	15.8	15.7	16.5	17.3	18.2
Other Current Liab	16.2	5.72	5.72	5.72	5.72
LT Debt	854	503	503	503	503
Other LT Liabilities	13.4	33.1	33.1	33.1	33.1
Unit holders' funds	1,372	1,323	1,323	1,323	1,323
Minority Interests	0.0	0.0	0.0	0.0	0.0
Total Funds & Liabilities	2,271	2,214	2,224	2,234	2,243
Non-Cash Wkg. Capital	(25.6)	(15.1)	(15.7)	(16.4)	(17.0)
Net Cash/(Debt)	(768)	(772)	(782)	(790)	(798)
Ratio					
Current Ratio (x)	2.9	0.2	0.2	0.2	0.2
Quick Ratio (x)	2.9	0.2	0.2	0.2	0.2
Aggregate Leverage (%)	37.6	37.8	38.0	38.3	38.5
Z-Score (X)	0.9	0.7	0.7	0.7	0.7

Source: Company, AllianceDBS

MRCB-Quill REIT

Cash Flow Statement (RMm)

FY Dec	2018A	2019A	2020F	2021F	2022F
Pre-Tax Income	79.3	35.4	77.5	76.9	77.6
Dep. & Amort.	0.0	0.0	0.0	0.0	0.0
Tax Paid	0.0	0.0	0.0	0.0	0.0
Associates & JV Inc/(Loss)	0.0	0.0	0.0	0.0	0.0
Chg in Wkg.Cap.	(11.7)	3.97	0.59	0.66	0.68
Other Operating CF	36.3	36.4	32.8	34.3	34.6
Net Operating CF	104	75.7	111	112	113
Net Invt in Properties	(3.8)	(2.1)	(10.0)	(9.0)	(8.0)
Other Invt (net)	0.0	0.0	0.0	0.0	0.0
Invt in Assoc. & JV	0.0	0.0	0.0	0.0	0.0
Div from Assoc. & JVs	0.0	0.0	0.0	0.0	0.0
Other Investing CF	3.69	2.72	3.16	3.19	3.23
Net Investing CF	(0.2)	0.59	(6.8)	(5.8)	(4.8)
Distribution Paid	(89.8)	(78.0)	(77.5)	(76.9)	(77.6)
Chg in Gross Debt	0.0	(19.0)	10.0	9.00	8.00
New units issued	3.97	0.0	0.0	0.0	0.0
Other Financing CF	(39.2)	(38.5)	(35.9)	(37.5)	(37.8)
Net Financing CF	(125)	(136)	(103)	(105)	(107)
Currency Adjustments	0.0	0.0	0.0	0.0	0.0
Chg in Cash	(21.3)	(59.2)	0.59	0.66	0.68
Operating CFPS (sen)	10.8	6.69	10.3	10.4	10.5
Free CFPS (sen)	9.33	6.86	9.41	9.59	9.78

Source: Company, AllianceDBS

Target Price & Ratings History



S.No.	Date of Report	Closing Price	12-mth Target Price	Rating
1:	26 Nov 19	1.02	1.10	HOLD
2:	18 Jun 20	0.71	1.10	BUY
3:	17 Aug 20	0.78	1.10	BUY
4:	09 Sep 20	0.77	1.10	BUY

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

Source: AllianceDBS

Analyst: Siti Ruzanna Mohd Faruk

MRCB-Quill REIT

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

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Wong Ming Tek, Executive Director

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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