

13 November 2020

Property | REITS

MRCB-Quill REIT (MQREIT MK)

Buy (Maintained)

Disposing An Underperformer; Maintain BUY

- **Maintain BUY and MYR0.87 TP, 5% upside and c.9% yield.** MRCB-Quill REIT is looking to dispose underperforming asset Quill Building 5 (QB5), which has been vacant since Apr 2019. Consecutive earnings beat this year's estimates from higher contributions from Wisma Technip and Menara Shell, and, paired with the overall stable occupancy, points to the REIT's strength in these uncertain times. It is trading at 0.67x P/BV – slightly below its 5-year average.
- **Disposing a vacant, underperforming asset.** In line with the objective of rejuvenating its property portfolio, MQREIT entered into a sales and purchase agreement with Derive Services for the proposed disposal of its underperforming asset, QB5, which has a MYR40m market value. The disposal should be for a cash consideration of MYR45m. QB5 is a 5-storey office building – with a sub-basement and carpark – that has been vacant since Apr 2019. Previously tenanted by IBM Malaysia, QB5's occupancy – as at Dec 2018 – stood at 56% and was estimated to have contributed only c.3% to topline in FY18.
- **Use of proceeds.** The disposal of QB5 is expected to be completed by 2Q21 and proceeds should be utilised to repay existing borrowings and fund any asset enhancement initiatives or investments in other assets, among others. This is expected to be utilised within 12 months from the completion of the disposal. Regardless, management guidance is that the use of the proceeds has not yet been finalised.
- **Cyberjaya now less of a concern.** We note that the renewal of DHL's leases at Quill Buildings 1 and 4 has already taken place – both for an additional five years. Previously thought to be a concern due to the location, we are now upbeat on the minimal non-renewal risk of the assets in Cyberjaya. Meanwhile, the average occupancy rate across all of MQREIT's buildings remains relatively stable at 90.5%, which is a marginal increase from 90.4% in 2Q20. The increased occupancy was demonstrated at Menara Shell and Plaza Mont Kiara, while the 1% non-renewal for this year was due to a tenant exiting Platinum Sentral.
- **Impact on earnings.** We are largely neutral on the news of the disposal, considering the minimal contribution of the vacant asset. Expected net gain is announced to be c.MYR3.7m. However, we trim off a marginal <1% of our FY21F-22F earnings, having previously assumed a 40% occupancy for QB5 from FY21 onwards and flat reversions. MQREIT is trading at 0.67x P/BV, slightly below its 5-year average of 0.7x.

Target Price (Return): MYR0.87 (+5%)
Price: MYR0.83
Market Cap: USD215m
Avg Daily Turnover (MYR/USD) 0.38m/0.09m

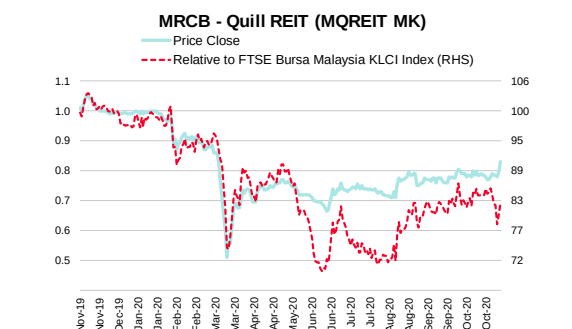
Analyst

Loong Kok Wen CFA
+603 9280 8861
loong.kok.wen@rhbgroup.com



Share Performance (%)

	YTD	1m	3m	6m	12m
Absolute	(17.0)	5.1	13.7	8.5	(17.0)
Relative	(17.1)	0.3	11.5	(6.8)	(15.8)
52-wk Price low/high (MYR)				0.51 – 1.05	



Source: Bloomberg

Forecasts and Valuation	Dec-18	Dec-19	Dec-20F	Dec-21F	Dec-22F
Total turnover (MYRm)	173	162	155	149	150
Net property income (MYRm)	134	123	119	115	116
Reported net profit (MYRm)	82.5	72.1	76.4	72.4	73.6
Total distributable income (MYRm)	82.5	72.1	76.4	72.4	73.6
DPS (MYR)	0.08	0.07	0.07	0.07	0.07
DPS growth (%)	(3.1)	(16.2)	3.6	(5.3)	1.7
P/B (x)	0.65	0.67	0.67	0.67	0.67
Dividend Yield (%)	9.8	8.2	8.5	8.1	8.2
Return on average equity (%)	6.0	5.3	5.8	5.5	5.6
Return on average assets (%)	3.6	3.2	3.5	3.3	3.3

Source: Company data, RHB

Note:
Small cap stocks are defined as companies with a market capitalisation of less than USD1bn.

Financial Exhibits

Asia	Financial summary	Dec-18	Dec-19	Dec-20F	Dec-21F	Dec-22F
Malaysia	Recurring EPS (MYR)	0.08	0.07	0.07	0.07	0.07
Property	EPS (MYR)	0.08	0.07	0.07	0.07	0.07
MRCB-Quill REIT	DPS (MYR)	0.08	0.07	0.07	0.07	0.07
MQREIT MK	BVPS (MYR)	1.28	1.23	1.24	1.24	1.24
Buy	Weighted avg adjusted shares (m)	1,071.8	1,071.8	1,071.8	1,071.8	1,071.8
Valuation basis	Valuation metrics	Dec-18	Dec-19	Dec-20F	Dec-21F	Dec-22F
Dividend discount model.	Recurring P/E (x)	10.5	12.3	11.6	12.3	12.1
	P/E (x)	10.5	12.3	11.6	12.3	12.1
	P/B (x)	0.6	0.7	0.7	0.7	0.7
Key drivers	FCF Yield (%)	13.1	13.1	12.0	11.9	11.4
Higher-than-expected demand of office space and inorganic growth opportunities arising from Malaysian Resources Corp and Quill Group.	Dividend yield (%)	9.7	8.2	8.5	8.1	8.2
	EV/EBITDA (x)	12.3	18.6	13.9	14.0	14.3
	EV/EBIT (x)	12.3	18.6	13.9	14.0	14.3
Key risks	Income statement (MYRm)	Dec-18	Dec-19	Dec-20F	Dec-21F	Dec-22F
Downside risk: The oversupply of office properties might affect the portfolio's office property occupancy and rental rates.	Total turnover	173	162	155	149	150
	Gross profit	134	123	119	115	116
	EBITDA	135	89	122	118	119
	Depreciation and amortisation	-	-	-	-	-
	Operating profit	135	89	122	118	119
	Net interest	(41)	(40)	(35)	(35)	(35)
	Income from associates & JVs	-	-	-	-	-
	Exceptional income - net	(3)	(37)	-	-	-
	Pre-tax profit	79	35	76	72	74
	Taxation	(6)	(6)	-	-	-
	Minority interests	-	-	-	-	-
	Recurring net profit(adj)	85	72	76	72	74
Company Profile	Cash flow (MYRm)	Dec-18	Dec-19	Dec-20F	Dec-21F	Dec-22F
MQREIT is a mid-cap MREIT that focuses on office/commercial assets. Assets are largely concentrated in the Klang Valley and Cyberjaya.	Change in working capital	(4)	(4)	(4)	(4)	(5)
	Cash flow from operations	117	106	106	102	103
	Capex	(2)	(2)	(2)	(2)	(2)
	Cash flow from investing activities	4	1	1	1	1
	Dividends paid	(88)	(80)	(74)	(74)	(72)
	Cash flow from financing activities	(129)	(120)	(109)	(109)	(107)
	Cash at beginning of period	52	43	31	29	24
	Net change in cash	(8)	(12)	(2)	(6)	(3)
	Ending balance cash	43	31	29	24	20
	Balance sheet (MYRm)	Dec-18	Dec-19	Dec-20F	Dec-21F	Dec-22F
	Total cash and equivalents	86	63	29	69	20
	Tangible fixed assets	2,179	2,144	2,144	2,104	2,104
	Intangible assets	-	-	-	-	-
	Total investments	-	-	-	-	-
	Total other assets	1	1	36	38	88
	Total assets	2,272	2,214	2,215	2,217	2,218
	Short-term debt	-	333	333	333	333
	Total long-term debt	854	503	503	503	503
	Other liabilities	46	54	55	56	57
	Total liabilities	899	890	891	892	892
	Shareholders' equity	1,372	1,323	1,324	1,325	1,326
	Minority interests	-	-	-	-	-
	Total equity	1,372	1,323	1,324	1,325	1,326
	Net debt	768	772	806	767	815
	Total liabilities & equity	2,272	2,214	2,215	2,217	2,218
	Key metrics	Dec-18	Dec-19	Dec-20F	Dec-21F	Dec-22F
	Revenue growth (%)	(3.7)	(6.5)	(4.7)	(3.6)	0.8
	Recurrent EPS growth (%)	(4.0)	(14.9)	5.9	(5.3)	1.7
	Gross margin (%)	77.1	75.8	77.1	77.1	77.1
	Operating EBITDA margin (%)	77.7	55.1	79.2	79.3	79.2
	Net profit margin (%)	48.8	44.5	49.5	48.6	49.1
	Dividend payout ratio (%)	102.1	101.0	99.0	99.0	99.0
	Capex/sales (%)	1.2	1.2	1.3	1.3	1.3
	Interest cover (x)	3.3	2.3	3.5	3.4	3.4

Source: Company data, RHB

Recommendation Chart



Source: RHB, Bloomberg

Date	Recommendation	Target Price	Price
2020-11-12	Buy	0.87	0.83
2020-08-17	Buy	0.83	0.78
2020-06-18	Buy	0.78	0.71
2020-04-06	Neutral	0.78	0.74
2020-01-20	Neutral	0.97	1.00
2019-11-26	Neutral	0.96	1.02
2019-08-08	Neutral	0.97	1.07
2019-05-10	Neutral	1.02	1.09
2019-01-18	Neutral	1.05	1.11
2019-01-10	Neutral	1.10	1.09
2018-11-28	Neutral	1.15	1.07
2018-08-09	Neutral	1.20	1.18

Source: RHB, Bloomberg

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KUALA LUMPUR

RHB Investment Bank Bhd

Level 3A, Tower One, RHB Centre
Jalan Tun Razak
Kuala Lumpur 50400
Malaysia
Tel : +603 9280 8888
Fax : +603 9200 2216

JAKARTA

PT RHB Sekuritas Indonesia

Revenue Tower, 11th Floor, District 8 - SCBD
Jl. Jendral Sudirman Kav 52-53
Jakarta 12190
Indonesia
Tel : +6221 509 39 888
Fax : +6221 509 39 777

BANGKOK

RHB Securities (Thailand) PCL

10th Floor, Sathorn Square Office Tower
98, North Sathorn Road, Silom
Bangrak, Bangkok 10500
Thailand
Tel: +66 2088 9999
Fax :+66 2088 9799

SINGAPORE

RHB Bank Berhad (Singapore branch)

90 Cecil Street
#04-00 RHB Bank Building
Singapore 069531