



MRCB-Quill REIT (MQREIT MK) : HOLD

Mkt. Cap: US\$274m | **3m Avg. Daily Val:** US\$0.08m

Last Traded Price (7 Aug 2019): RM1.07

Price Target 12-mth: RM1.15 (7% upside) (Prev RM1.20)

Analyst

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Office space to remain under pressure

- 1HFY19 earnings below expectations
- Lower income from Platinum Sentral, Wisma Technip and QB5
- Cut earnings to reflect lower occupancy rates; portfolio occupancy at 89% from 92% previously
- Maintain HOLD with lower TP of RM1.15

Forecasts and Valuation

FY Dec (RMm)	2018A	2019F	2020F	2021F
Gross Revenue	173	167	171	175
Net Property Inc	134	126	127	128
Total Return	73.1	75.5	75.6	76.4
Distribution Inc	86.6	73.2	73.4	74.1
EPU (sen)	6.82	7.03	7.03	7.09
EPU Gth (%)	4	3	0	1
DPU (sen)	8.08	6.82	6.82	6.88
DPU Gth (%)	(4)	(16)	0	1
NAV per shr (sen)	128	128	128	129
PE (X)	15.7	15.2	15.2	15.1
Distribution Yield (%)	7.6	6.4	6.4	6.4
P/NAV (x)	0.8	0.8	0.8	0.8
Aggregate Leverage (%)	37.6	37.8	38.0	38.1
ROAE (%)	5.3	5.5	5.5	5.5

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

What's New

2QFY19 results below expectations. MQREIT's 2QFY19 core earnings came in at RM16.5m (-22.7% y-o-y; -15.2% q-o-q). 1HFY19 numbers trailed our and consensus expectations.

The earnings decline in the quarter was mainly due to lower revenue generated from Platinum Sentral, Wisma Technip, QB5 as well as loss of revenue from the disposal of QB8 – DHL XPI which took place on 12 April 2018.

Property operating expenses amounted to RM9.7m (-3.4% y-o-y; +3.8% q-o-q) as it tightened control on costs and reduced expenses from the disposal of QB8. Net property income (NPI) for the quarter came in at RM29.1m (-12.8% y-o-y; -9.2% q-o-q).

Outlook

Occupancy under pressure. Portfolio occupancy fell to 89% in 2QFY19 vs 96% in 2QFY18. We understand there was lower occupancy in QB5 – IBM, as well as Platinum Sentral and Wisma Technip, as tenants opted to downsize operations.

We cut our forecasts by 5% for FY19F-21F to account for the lower occupancy rates for Platinum Sentral, QB5 and Wisma Technip. IBM has moved out from QB5 leaving the asset at 0% occupancy however this is only 80k sq ft which represents 4% of total portfolio NLA and c.2.4% of total revenue. We expect MQREIT to enjoy slightly better earnings in 2HFY19 as there will be a new tenant for Platinum Sentral following the exit of myHSR and SPAD.



About 19.0% of total NLA is due for renewal in FY19, of which c.11.0% has been renewed and 4% not renewed. The expiring leases in FY20 form 18% of total NLA. We understand rental reversions were flattish 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.

Valuation and Recommendation

We maintain our HOLD call with a lower TP of RM1.15. Our DDM-derived TP employs 7.4% cost of equity and 1% terminal growth. The key concerns for the stock include the challenge of filling up vacancies, as well as downward pressure on rental rates as it grapples with incoming supply of new office space. As we factor in weakness in the office market, we see limited upside for the stock at this juncture. Downside risks include longer-than-expected time in filling up vacancies.

Quarterly Income Statement (RMm)

FY Dec	2Q2018	1Q2019	2Q2019	% chg yoy	% chg qoq
Gross revenue	43.4	41.4	38.8	(10.7)	(6.3)
Property expenses	(10.0)	(9.3)	(9.7)	(3.4)	3.8
Net Property Income	33.4	32.0	29.1	(12.8)	(9.2)
Other Operating expenses	(3.0)	(3.6)	(3.5)	15.0	(3.9)
Other Non Opg (Exp)/Inc	0.0	0.0	0.0	N/A	N/A
Net Interest (Exp)/Inc	(9.1)	(9.0)	(9.2)	(1.1)	(1.5)
Exceptional Gain/(Loss)	2.20	0.0	0.0	N/A	N/A
Net Income	23.5	19.4	16.5	(29.9)	(15.2)
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	23.5	19.4	16.5	(29.9)	(15.2)
Total Return	23.5	19.4	16.5	(29.9)	(15.2)
Non-tax deductible Items	0.0	0.0	0.0	nm	nm
Net Inc available for Dist.	21.3	19.4	16.5	(22.7)	(15.2)
Ratio (%)					
Net Prop Inc Margin	76.9	77.4	75.0		
Dist. Payout Ratio	101.9	0.0	101.7		

Source of all data: Company, AllianceDBS

Target Price & Ratings History



S. No.	Date of Report	Closing Price	12-mth Target Price	Rating
1:	09 Aug 18	1.18	1.27	BUY
2:	28 Nov 18	1.07	1.24	BUY
3:	18 Jan 19	1.11	1.15	HOLD
4:	10 May 19	1.09	1.15	HOLD
5:	10 Jul 19	1.08	1.20	HOLD

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

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