

MRCB-Quill REIT (BUY ↔, EPS ↓)

INDUSTRY: NEUTRAL

EARNINGS EVALUATION

23 July 2015

Target Price: RM1.29 (↓)

Share Price: RM1.17

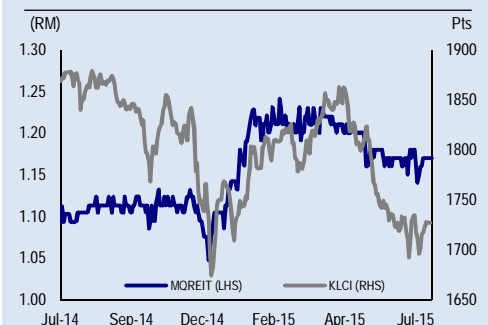
6M15 Results

Results	<ul style="list-style-type: none"> 6MFY15 gross revenue of RM50.8m (+47.1% yoy) was translated into normalised net profit of RM21.9m (+31.0% yoy), accounting for 38.5% and 41.4% of HLIB and consensus FY forecasts, respectively.
Deviations	<ul style="list-style-type: none"> Higher than expected cost arising from acquisitions particularly from repair and maintenance as well as administrative expenses.
Dividends	<ul style="list-style-type: none"> YTD dividend of 4.10 sen (1H14: 4.10 sen), accounting for 49.9% of our full year DPU assumptions.
Highlights	<ul style="list-style-type: none"> Full contribution from newly-acquired Platinum Sentral has kicked-in during the current quarter evident by 31% increase in normalised net profit. Improvement in normalised net profit is also attributable to higher contribution from Plaza Mont' Kiara, as well as higher rental rate for other properties. NPI margin has improved sequentially from 73.5% to 75.6% (Figure #5). We believe with potential asset injections and positive rental reversion from existing portfolio, NPI margin should be able to show favourable improvements. We reiterate our positive views on consistently high occupancy rate achieved by MQREIT (circa 93%) as shown in Figure #6, compared with an average of 85% for office market in Klang Valley. Also note that management has successfully renewed 94% of the leases due in 1H15.
Risks	<ul style="list-style-type: none"> Management continuity following the entry of MRCB. Slow rental reversion rate.
Forecasts	<ul style="list-style-type: none"> We tweaked our forecast to factor in higher cost upon completion of the acquisition exercise. As such, our DPU assumptions for FY15-17 are diluted by 4% and thereby our TP reduced to RM1.29.
Rating	<p>BUY ↔, TP: RM1.29 ↓</p> <ul style="list-style-type: none"> Positives: (1) higher possibility of asset injections from MRCB and EPF, following the injection of Platinum Sentral, resulting in MRCB taking control of QCM and major unitholder of QCT; (2) Resilient earnings growth with undemanding valuations – 7.1% DY (FY15E). Negatives: (1) Small asset base; (2) illiquid; (3) lack of retail assets.
Valuation	<ul style="list-style-type: none"> Maintain BUY recommendation on the equity but our TP lowered to RM1.29 post earnings forecasts adjustments. Our valuation was pegged to targeted yield of 6.9% based on 2SD below historical average yield spread of MRCB-Quill REIT and 7-year government bond in view of high potential for yield accretive injection(s).

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KLCI	1729.5
Expected share price return	10.3%
Expected dividend return	7.1%
Expected total return	17.4%

Share price

Information

Bloomberg Ticker	MQREIT MK
Bursa Code	5123
Issued Shares (m)	661
Market cap (RM m)	774
3-mth avg. volume ('000)	272
SC Shariah-compliant	No

Price Performance	1M	3M	12M
Absolute	0.0	-3.3	-1.7
Relative	0.2	3.7	6.4

Major Shareholders

MRCB	31.2%
Quill Group	17.7%

Summary Earnings Table

FYE Dec (RMm)	2014A	2015E	2016E	2017E
Revenue	50.8	128.3	133.0	137.9
NPI	53.2	98.1	101.7	105.4
Net invest income	56.1	98.7	103.2	106.9
PAT	36.6	54.6	58.8	62.1
EPU (sen)	10.3	8.3	8.9	9.4
Norm. PER (x)	11.3	14.2	13.2	12.5
FD PER (x)	11.3	14.2	13.2	12.5
EV/ EBITDA (x)	28.2	71.0	58.9	52.0
Net DPU (sen)	8.4	8.3	8.9	9.4
Distb. yield (%)	7.2	7.1	7.6	8.0
BVPS (RM)	1.4	1.3	1.3	1.3
P/B (x)	0.8	0.9	0.9	0.9

HLIB

Figure #1 Quarterly Results Comparison

FYE Dec (RMm)	2Q14	1Q14	2Q15	YoY (%)	QoQ (%)	Comments
Gross revenue	17.35	18.61	32.18	85.46	72.90	Higher revenue mainly attributable to contribution from newly-acquired Platinum Sentral, as well as higher rental rates for other properties.
Property operating expenses	(3.95)	(4.93)	(7.86)	98.89	59.48	Similarly, increase in operating expenses attributable to cost related to acquisition, as well as higher repair and maintenance cost for Plaza Mont Kiara.
Net property income	13.40	13.68	24.31	81.50	77.74	
Interest income	0.29	0.13	0.14	(51.05)	14.14	
Net investment income	13.69	13.81	24.46	78.66	77.16	
Finance costs	(3.57)	(3.54)	(8.19)	129.66	131.49	Interest on additional borrowings drawdown o fund acquisition.
Valuation fees	(0.05)	(0.05)	(0.05)	0.00	0.00	
Administrative expenses	(0.07)	(0.19)	(0.32)	389.54	65.14	
Total Expenses	(5.13)	(5.53)	(10.82)	111.13	95.87	
Normalised PBT	8.56	8.28	13.63	59.22	64.67	
Normalised PAT	8.56	8.28	13.63	59.22	64.67	
EPU after mgmt fee	2.19	2.09	2.20	0.46	5.26	
DPU (sen)	4.10	0.00	4.10	0.00	NM	

Company Data, HLIB

Figure #2 Cumulative Results Comparison

FYE Dec (RMm)	6M14	6M15	YoY (%)	Comments
Gross revenue	34.53	50.78	47.06	Same as above.
Property operating expenses	(8.12)	(12.79)	57.44	
Net property income	26.41	37.99	43.86	
Interest income	0.41	0.27	(33.77)	
Net investment income	26.81	38.26	42.69	
Finance costs	(7.00)	(11.73)	67.61	
Valuation fees	(0.09)	(0.09)	(0.00)	
Administrative expenses	(0.21)	(0.51)	149.12	
Total Expenses	(10.09)	(16.35)	62.03	Same as above.
Normalised PBT	16.72	21.91	31.02	Same as above.
Normalised PAT	16.72	21.91	31.02	Same as above.
EPU after mgmt fee	4.28	4.29	0.23	
DPU (sen)	4.10	4.10	0.00	

Company Data, HLIB

Figure #3 6M15 Results vs. HLIB's Estimates and Consensus

	Actual 6M15	HLIB FY15	Actual vs. HLIB (%)	Consensus FY15	Actual vs. Consensus (%)	Comments
Revenue	50.8	116.1	43.7	113.0	44.9	Below expectations.
Normalised PAT	21.9	56.9	38.5	52.9	41.4	Below expectations.
EPU (sen)	4.3	8.6	49.9	8.8	48.8	In-line.
DPU (sen)	4.1	8.6	47.6	8.4	48.8	In-line.

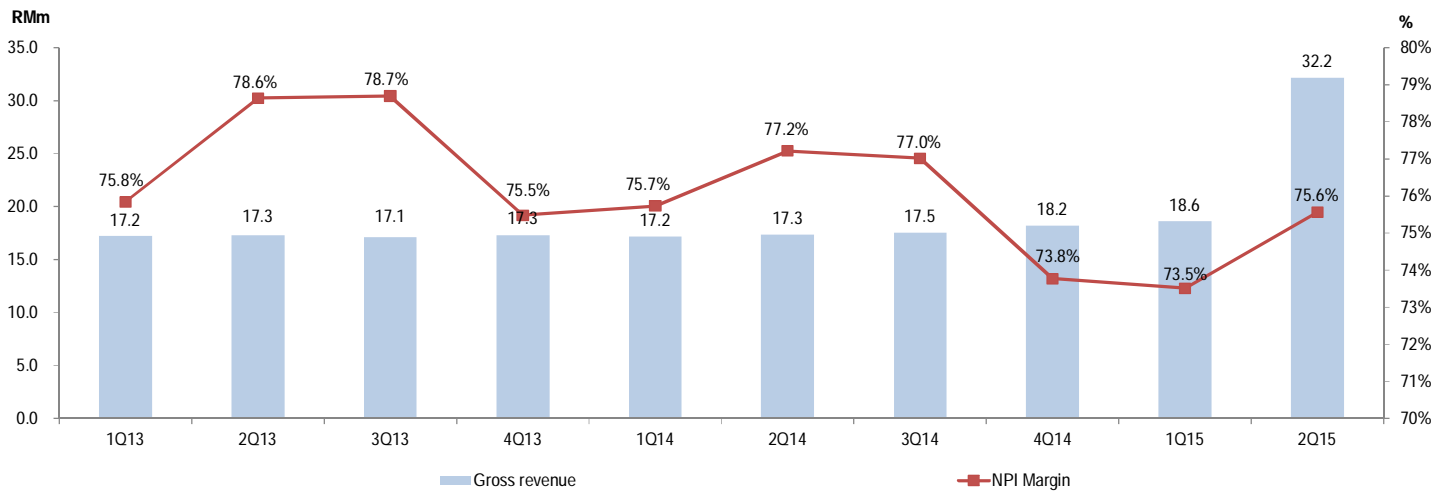
Company Data, HLIB, Bloomberg

Figure #4 HLIB Forecasts vs. Consensus

RMm	FY16E			FY17E		
	HLIB	Consensus	%	HLIB	Consensus	%
Normalised PAT	58.8	57.2	2.7	62.1	59.0	5.3
DPU (sen)	8.9	8.7	2.2	9.4	8.9	5.5

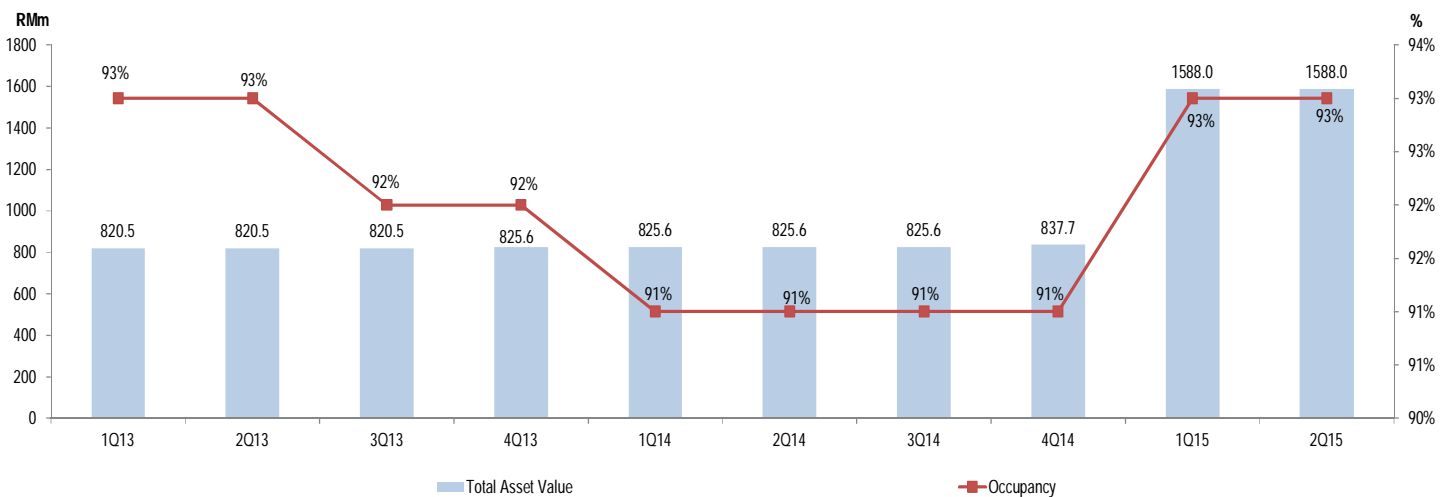
HLIB, Bloomberg

Figure #5 Gross Revenue & NPI Margin



HLIB, Bloomberg

Figure #6 Total Asset Value & Occupancy



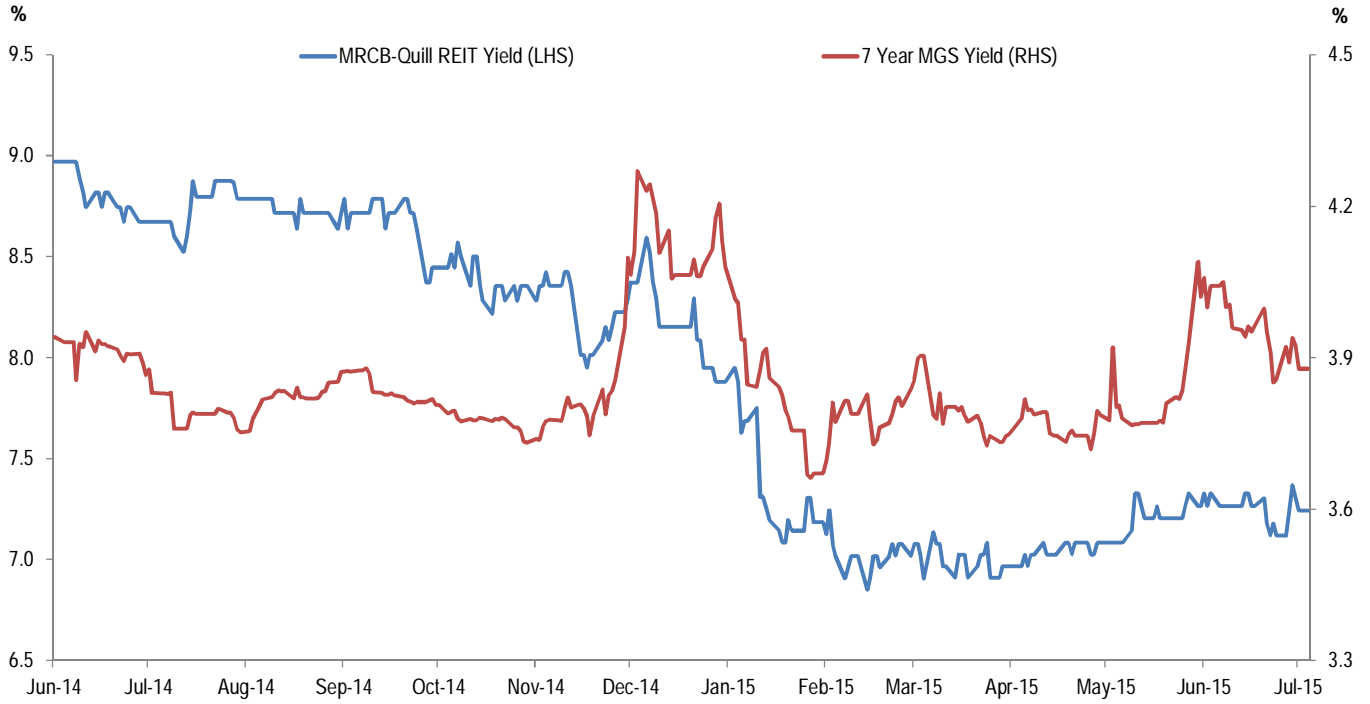
HLIB, Bloomberg

Figure #7 Peers Comparison

Company	FYE	Price @ 22 July 2015		Market Cap (m)	P/E (x)		P/B (x)		Gross DY (%)
		2014	2015		2014	2015			
Amanah Harta Tanah PNB	Dec	MYR 1.06	106.0	NA	NA	NA	NA	NA	
Al-'Aqar Healthcare REIT	Dec	MYR 1.31	912.1	14.7	14.6	1.1	1.1	6.4	
AmFIRST Real Estate Investment Trust	Mar	MYR 0.87	593.7	9.6	10.8	0.7	0.7	9.2	
Amanahraya Real Estate Investment Trust	Dec	MYR 0.88	504.4	11.0	11.0	0.9	0.9	9.1	
Atrium Real Estate Investment Trust	Dec	MYR 1.15	140.1	11.5	11.5	0.8	0.8	8.7	
Axis Real Estate Investment Trust	Dec	MYR 3.51	1,922.6	17.6	16.9	1.5	1.5	5.5	
CapitaMalls Malaysia Trust	Dec	MYR 1.36	2,745.3	15.6	14.2	1.1	1.1	6.5	
Hektar Real Estate Investment Trust	Dec	MYR 1.50	601.0	12.5	12.5	1.0	1.0	7.3	
IGB Real Estate Investment Trust	Dec	MYR 1.31	4,531.7	18.5	17.7	1.2	1.2	5.8	
KLCCP Stapled Group	Dec	MYR 7.10	12,817.9	18.3	17.7	1.4	1.4	4.9	
Pavilion Real Estate Investment Trust	Dec	MYR 1.52	4,584.2	19.2	18.1	1.2	1.2	5.3	
MRCB-Quill REIT	Dec	MYR 1.17	773.8	13.3	12.7	0.8	0.9	7.2	
YTL Hospitality REIT	Jun	MYR 1.05	1,390.6	11.7	11.7	0.8	0.7	8.6	
Sunway Real Estate Investment Trust	Jun	MYR 1.56	4,582.7	18.4	15.9	1.2	1.2	5.4	
Tower Real Estate Investment Trust	Dec	MYR 1.24	347.8	10.3	10.3	0.7	0.7	9.7	
UOA Real Estate Investment Trust	Dec	MYR 1.62	685.1	13.5	13.5	1.1	1.1	7.4	
Average				14.4	14.5	1.0	1.1	7.1	

HLIB, Bloomberg

Figure #8 MRCB-Quill yield vs. 7 year MGS yield



HLIB, Bloomberg

MRCB-Quill REIT (BUY, TP: RM1.29, CP: RM1.17)

Income Statement

FYE Dec (RM m)	2013A	2014A	2015E	2016E	2017E
Gross rental income	57.4	59.3	116.1	120.4	124.9
Car park income	3.5	5.2	3.7	3.9	4.0
Other revenue	8.0	5.7	8.5	8.8	9.0
Total Revenue	68.9	50.8	128.3	133.0	137.9
Assessment & quit rent	(2.8)	(2.8)	(5.8)	(6.0)	(6.3)
Depreciation	(0.0)	0.0	(0.0)	(0.0)	(0.0)
Insurance	(0.4)	(0.4)	(0.8)	(0.8)	(0.9)
Property management fees	(2.0)	(2.0)	(3.9)	(4.0)	(4.1)
Service contracts	(4.1)	(4.7)	(9.3)	(9.6)	(10.0)
Utilities	(6.5)	(7.0)	(10.4)	(10.8)	(11.2)
Total Opex	(15.7)	(12.8)	(30.2)	(31.3)	(32.5)
Net property income	53.2	38.0	98.1	101.7	105.4
Net investment income	56.1	38.3	98.7	103.2	106.9
Pretax profit	36.6	21.9	54.6	58.8	62.1
Taxation	0.0	0.0	0.0	0.0	0.0
Net profit	36.6	21.9	54.6	58.8	62.1
No of units (m)	390.1	390.1	661.4	661.4	661.4
EPU (sen)	9.4	10.3	8.3	8.9	9.4

Cash Flows

FYE Dec (RM m)	2013A	2014A	2015E	2016E	2017E
PBT	36.6	40.3	54.6	58.8	62.1
Finance costs	13.7	14.1	0.0	0.0	0.0
Depreciation	0.0	0.0	0.0	0.0	0.0
Fair value gain of assets	(2.1)	(6.1)	0.0	0.0	0.0
Interest income	(0.8)	(0.7)	0.0	0.0	0.0
Others	(11.3)	(16.4)	11.6	0.7	0.7
Operating cashflow	36.1	31.1	66.2	59.5	62.8
Capex	(3.0)	(6.0)	(740.0)	(2.0)	(2.0)
Disposal / (purchase)	0.0	(0.0)	(0.0)	(0.0)	(0.0)
Others	0.0	0.0	0.0	0.0	0.0
Investing Cashflow	(3.0)	(6.0)	(740.0)	(2.0)	(2.0)
Distribution paid	(32.7)	(32.7)	(54.6)	(58.8)	(62.1)
Proceeds from borrowings	117.0	15.0	430.0	0.0	0.0
Repayment of borrowings	(117.0)	(15.0)	0.0	0.0	0.0
Financing cashflow	0.0	0.0	342.0	0.0	0.0
Net cash flow	(32.7)	(32.7)	375.4	(58.8)	(62.1)

Balance Sheet

FYE Dec (RM m)	2013A	2014A	2015E	2016E	2017E
PPE	0.0	0.0	0.0	0.0	0.0
Investment properties	825.6	837.7	1,577.7	1,579.7	1,581.7
Derivatives	1.0	1.2	1.2	1.2	1.2
Non-current assets	826.6	838.9	1,579.0	1,581.0	1,583.0
Trade receivables	2.6	6.1	5.1	5.3	5.5
Cash	30.9	23.3	66.9	65.6	64.3
Total Current Assets	33.5	29.4	72.1	70.9	69.8
Total assets	860.1	868.4	1,651.0	1,651.9	1,652.7
Unitholders' capital	411.7	411.7	753.7	753.7	753.7
Undistributed profit	121.7	129.5	129.5	129.5	129.5
Total Equity	533.5	541.3	883.3	883.3	883.3
Borrowings	304.9	305.1	735.1	735.1	735.1
Security Deposits	10.1	9.8	9.8	9.8	9.8
Derivatives	0.0	0.0	0.0	0.0	0.0
Trade payables	11.7	12.2	22.9	23.7	24.6
Total liabilities	326.7	327.1	767.8	768.6	769.5
Total liabilities & equity	860.1	868.4	1,651.0	1,651.9	1,652.7

Valuation Ratios

FYE Dec (RM m)	2013A	2014A	2015E	2016E	2017E
EPU before mgr's fee	10.8	11.7	9.6	10.3	10.8
EPU after mgr's fee	9.4	10.3	8.3	8.9	9.4
PER (x)	12.5	11.3	14.2	13.2	12.5
No of units	390.1	390.1	661.4	661.4	661.4
Net DPU	8.4	8.4	8.3	8.9	9.4
Net DY (%)	7.2	7.2	7.1	7.6	8.0
NTA/ share (sen)	136.0	137.7	132.8	132.6	132.5
P/NTA (x)	0.9	0.8	0.9	0.9	0.9
FCF/ share (sen)	18.4	17.9	13.4	18.2	19.2
FCF yield (%)	15.7	15.3	11.5	15.5	16.4
Enterprise value	730.4	738.3	1,442.0	1,443.3	1,444.7
EV/ EBITDA (x)	31.8	28.2	71.0	58.9	52.0
ROE (%)	6.9	7.4	6.2	6.7	7.0
Net gearing (x)	0.3	0.3	0.4	0.4	0.4
Total gearing (x)	0.4	0.4	0.4	0.4	0.4
BVPS (RM)	1.4	1.4	1.3	1.3	1.3
P/B (x)	0.9	0.8	0.9	0.9	0.9

Assumption metrics

Gross Rental Income	2015E	2016E	2017E
Quill Building 1 - DHL 1	4.7	4.8	4.9
Quill Building 4 - DHL 2	5.0	5.1	5.3
Quill Building 2 - HSBC	9.3	9.5	9.8
Quill Building 3 - BMW	4.8	5.0	5.1
Wisma Technip	11.8	12.0	12.3
Part of Plaza Mont' Kiara	3.7	3.8	3.9
Quill Building 5 - IBM	3.7	3.8	3.9
Quill Building 6 - DHL XPJ	3.0	3.1	3.2
Quill Building 10 - Section 13	0.0	0.0	0.0
Tesco Building - Penang	13.9	14.2	14.6
Platinum Sentral	56.2	59.0	62.0
Total	116.1	120.4	124.9

Quarterly Financial Summary

FYE Dec (RM m)	2Q14	1Q15	2Q15	YoY (%)	QoQ (%)
Gross revenue	17.3	18.6	32.2	85.5	72.9
Property operating expenses	(4.0)	(4.9)	(7.9)	98.9	59.5
Net property income	13.4	13.7	24.3	81.5	77.7
Interest income	0.3	0.1	0.1	(51.0)	14.1
Revaluation gains	13.7	13.8	24.5	78.7	77.2
Net investment income	(3.6)	(3.5)	(8.2)	129.7	131.5
Finance costs	(0.0)	(0.0)	(0.0)	0.0	0.0
Valuation fees	(0.1)	(0.2)	(0.3)	389.5	65.1
Administrative expenses	(5.1)	(5.5)	(10.8)	111.1	95.9
Total Expenses	8.6	8.3	13.6	59.2	64.7
Normalised PBT	8.6	8.3	13.6	59.2	64.7
Normalised PAT	2.2	2.1	2.2	0.5	5.3
EPU after mgmt fee	4.1	0.0	4.1	0.0	NM
DPU (sen)	17.3	18.6	32.2	85.5	72.9

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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.
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