HLIB Research
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MRCB-Quill REIT

Stable performance

MQREIT 1Q18 core net profit RM21.0m (-2.3% QoQ, -9.3% YoY) was broadly in line with our expectation and consensus. The reduction was driven by a decline in revenue, higher operating expenses & administrative expenses but slightly mitigated by lower finance costs. We lower our FY18-20 earnings by 2% followed by a decrease in FY18-20 DPU by 5% as we take into account the completion for the disposal of QB8-DHL (XPJ). We maintain BUY call with lower TP of RM1.40 (from RM1.44) based on unchanged targeted yield of 6.4%

BUY (Maintain)

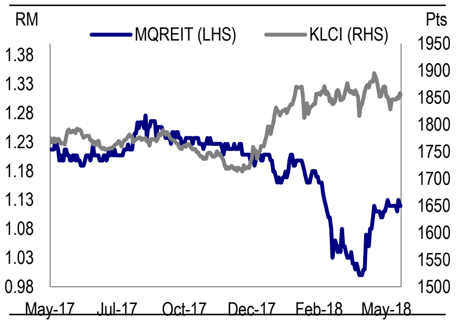
Target Price:	**RM1.40**
Previously:	**RM1.44**
Current Price:	**RM1.12**

Capital upside	25.0%
Dividend yield	7.9%
Expected total return	32.9%

Sector coverage: REIT

Company description: MRCB-Quill REIT invests in office and retail buildings, business/technology parks, data processing centers, and car parking facilities primarily in Malaysia.

Share price



Historical return (%)	1M	3M	12M
Absolute	1.8	-5.1	-13.8
Relative	3.2	-5.9	-17.9

Stock information

Bloomberg ticker	MQREIT MK
Bursa code	5123
Issued shares (m)	1,072
Market capitalisation (RM m)	1,200
3-mth average volume ('000)	657
SC Shariah compliant	No

Major shareholders

MRCB	27.8%
Capita Commercial Trust	10.9%
Employees Provident Fund	7.2%

Earnings summary

FYE (Dec)	FY17	FY18f	FY19f
PAT – core	89.7	91.5	93.7
EPU – core (sen)	8.4	8.5	8.6
P/E (x)	13.4	13.2	13.0

Within expectations. 1Q18 gross revenue of RM44.0m (-1.4% QoQ, -3.3% YoY) translated into core net profit of RM21.0m (-2.3% QoQ, -9.3% YoY). The results were broadly in line with ours and consensus expectations, accounting for 22.8% and 23.2%, respectively.

Deviation. We deem it to be in line as we feel the administrative expenses would normalise in the coming quarters.

Dividend. None as dividend is usually payable semi-annually.

QoQ. Total gross revenue declined by 1.4% to RM44.0m (from RM44.7m in 4Q17), following a decrease in core net profit at RM21.0m. The reduction was caused by lower revenue contribution and higher administrative expenses pertaining to the disposal of QB8-DHL (XPJ). However, this was slightly offset by the decrease in finance costs for the quarter.

YoY. Core net profit declined by 9.3% at RM21.0m. The was driven by (1) lower revenue contribution, mainly from Platinum Sentral and Menara Shell, (2) increase in routine property operating expenses, (3) higher administrative expenses related to the proposed disposal of QB8-DHL (XPJ). This is slightly cushioned by lower finance costs due to lower amortisation of transaction costs incurred.

Occupancy and gearing. Overall occupancy rate remained healthy at 96.2% (4Q17: 96.3%). Average debt to maturity has decreased slightly from 2.79 years to 2.55 years, while average cost of debt maintained at 4.4%. The gearing level increased slightly to 38% (4Q17: 37%), which is still comfortably below the 50% limit.

Outlook. Despite the lacklustre overall office market, MQREIT's office space will remain relatively stable and well-guarded by its long weighted average term to expiry with well-spread NLA expiry. To date, management has successfully completed 81% renewals due in 1Q18. We continue to like MQREIT given its attractive dividend yield of 8.2% (highest among REITs in our universe), stable assets in prime location of KL Sentral with high occupancy rate and healthy WALE profile.

Forecast. Although the results were broadly in line, we take this opportunity to adjust our FY18-20 earnings marginally lower by 2% to account for the completion of the disposal of QB8-DHL (XPJ) building. As a result, our FY18-20 DPS forecast is also reduced by 5%.

Maintain BUY, TP: RM1.40. While we maintain our BUY call, our TP is lowered from RM1.44 to RM1.40 following the lowered DPU projection. Our TP is based on FY18 targeted yield of 6.4% which is derived from 1SD below 2 years historical average yield spread of MQREIT and 10-year MGS.

Financial Forecast

All items in (RM m) unless otherwise stated

Balance Sheet

FYE Dec	FY16	FY17	FY18f	FY19f	FY20f
Cash	54.1	76.0	61.1	61.8	73.1
Receivables	18.3	6.0	6.1	6.2	6.3
Investment properties	2,222.0	2,179.2	2,181.2	2,183.2	2,185.2
PPE	0.2	0.2	0.1	0.1	0.1
Others	2.7	27.0	27.0	27.0	27.0
Assets	**2,297.3**	**2,288.4**	**2,275.5**	**2,278.3**	**2,291.7**
Payables	55.8	20.3	23.5	24.0	24.5
Debt	851.6	853.5	836.5	836.5	847.5
Security deposits	29.3	29.2	29.2	29.2	29.2
Derivatives	1.0	0.7	0.7	0.7	0.7
Liabilities	**937.6**	**903.7**	**889.9**	**890.4**	**901.9**
Unitholders' capital	1,231.9	1,231.9	1,231.9	1,231.9	1,231.9
Undistributed profit	127.8	152.8	153.7	155.9	157.9
Equity	**1,359.7**	**1,384.7**	**1,385.6**	**1,387.9**	**1,389.8**

Income Statement

FYE Dec	FY16	FY17	FY18f	FY19f	FY20f
Gross rental income	115.9	162.1	165.9	169.2	172.6
Car park income	10.9	12.8	14.2	14.4	14.7
Other revenue	5.0	5.2	5.8	5.9	6.1
Total revenue	136.6	181.5	185.9	189.6	193.4
Assessment & quit rent	-5.3	-8.5	-14.2	-14.5	-14.8
Depreciation	-0.1	-0.1	-0.1	-0.1	-0.1
Insurance & Prop mgmt	-3.1	-3.9	-4.0	-4.1	-4.2
Service contracts	-9.6	-10.9	-11.2	-11.4	-11.7
Utilities	-11.5	-16.7	-17.1	-17.5	-17.8
Total opex	-29.5	-40.2	-46.6	-47.5	-48.5
Net property income	77.7	101.2	92.7	94.6	96.5
Net investment income	108.2	125.4	144.4	146.2	149.1
Pretax profit	62.8	69.9	89.7	91.5	93.7
Taxation	0.0	0.0	0.0	0.0	0.0
Net profit	59.2	88.1	89.7	91.5	93.7
No. of units (units)	1,068.0	1,068.0	1,074.0	1,081.2	1,088.5

Cash Flow Statement

FYE Dec	FY16	FY17	FY18f	FY19f	FY20f
Profit before taxation	62.8	69.9	89.7	91.5	93.7
Finance costs	33.0	40.5	0.0	0.0	0.0
Depreciation	0.1	0.1	0.1	0.0	0.0
Fair value gain of assets	-3.5	18.2	0.0	0.0	0.0
Interest income	-2.4	-3.6	0.0	0.0	0.0
Others	-19.7	4.0	3.1	0.4	0.4
CFO	**70.3**	**129.1**	**92.9**	**91.9**	**94.1**
Capex	-647.4	-0.4	-2.0	-2.0	-2.0
Disposal / (purchase)	-1.5	0.0	0.0	0.0	0.0
Others	0.0	2.2	0.0	0.0	0.0
CFI	**-648.9**	**1.8**	**-2.0**	**-2.0**	**-2.0**
Distribution paid	-56.9	-72.6	-88.8	-89.6	-91.8
Proceeds from borrowings	164.0	191.0	100.0	0.0	400.0
Repayment of borrowings	0.0	-190.0	-117.0	0.0	-389.0
Placement / new share	487.9	-37.2	0.0	0.0	0.0
CFF	**595.1**	**-108.8**	**-105.8**	**-89.6**	**-80.8**
Net cash flow	**16.5**	**22.0**	**-14.9**	**0.2**	**11.3**

Valuation & Ratios

FYE Dec	FY16	FY17	FY18f	FY19f	FY20f
Core EPU (sen)	5.9	6.5	8.4	8.5	8.6
P/E (x)	20.2	13.6	13.4	13.2	13.0
EBITDA	92.3	128.7	129.5	131.2	134.0
EBIT	92.3	128.6	129.4	131.2	133.9
EV	1,993.7	1,973.6	1,978.2	1,985.7	1,993.5
EV/EBITDA (x)	21.6	15.3	15.3	15.1	14.9
DPU (sen)	8.4	8.4	8.9	9.0	9.2
Dividend yield	7.5	7.5	7.9	8.1	8.2
NTA/ share (sen)	126.8	129.0	128.3	127.5	126.7
P/ NTA	0.9	0.9	0.9	0.9	0.9
BVPS (RM)	1.3	1.3	1.3	1.3	1.3
P/B (x)	0.9	0.9	0.9	0.9	0.9
EBITDA margin	0.7	0.7	0.7	0.7	0.7
EBIT margin	0.7	0.7	0.7	0.7	0.7
PBT margin	0.5	0.4	0.5	0.5	0.5
Net margin	0.4	0.5	0.5	0.5	0.5
ROE	4.6	5.0	6.5	6.6	6.7
ROA	2.6	3.8	3.9	4.0	4.1
Net gearing	0.3	0.3	0.3	0.3	0.3

Assumptions

FYE Dec	FY16	FY17	FY18f	FY19f	FY20f
Gross rental income					
Quill Building 1 - DHL 1			4.9	5.0	5.1
Quill Building 4 - DHL 2			5.3	5.4	5.5
Quill Building 2 - HSBC			9.8	10.0	10.2
Quill Building 3 - BMW			5.1	5.2	5.3
Wisma Technip			12.4	12.7	12.9
Part of Plaza Mont' Kiara			4.0	4.1	4.2
Quill Building 5 - IBM			4.0	4.0	4.1
Quill Building 8 - DHL XPJ			0.0	0.0	0.0
Tesco Building - Penang			14.6	14.9	15.2
Platinum Sentral			57.6	58.8	59.9
Menara Shell			48.1	49.1	50.1
Total:			165.9	169.2	172.6

Quarterly financial summary

FYE Dec	1Q17	4Q17	1Q18	QoQ (%)	YoY (%)
Gross revenue	45.6	44.7	44.0	-1.4	-3.3
Property opex	-9.4	-10.0	-9.8	2.7	-3.4
Net property income	36.1	36.0	34.3	-4.8	-5.1
Interest income	0.5	1.7	0.7	-58.1	61.3
Revaluation gains	0.0	-18.2	0.0	N/A	N/A
Net investment income	36.6	18.2	35.0	92.5	-4.3
Finance costs	-9.7	-11.0	-9.7	11.8	0.3
Valuation fees	0.0	-0.1	-0.1	-27.1	-192.8
Administrative expenses	-0.1	-0.3	-0.7	-157.3	-1,008.6
TOTAL EXPENSES	-13.4	-14.9	-14.0	5.8	-4.4
Normalised PBT	23.2	21.5	21.0	-2.3	-9.3
Normalised PAT	23.2	21.5	21.0	-2.3	-9.3
EPU (realised)	2.2	2.0	2.0	-2.3	-9.3
DPU (sen)	0.0	4.2	0.0	N/A	N/A

Figure #1 Quarterly results comparison

FYE Dec (RM m)	1Q17	4Q17	1Q18	QoQ (%)	YoY (%)
Gross Revenue	45.6	44.7	44.0	*-1.4*	*-3.3*
Property operating expenses	-9.4	-10.0	-9.8	*2.7*	*-3.4*
Net property income	36.1	36.0	34.3	*-4.8*	*-5.1*
Interest income	0.5	1.7	0.7	*-58.1*	*61.3*
Gain on divestment	0.0	0.0	0.0	*N/A*	*N/A*
Net interest income	36.6	18.2	35.0	*92.5*	*-4.3*
Finance costs	-9.7	-11.0	-9.7	*11.8*	*0.3*
Valuation fees	-0.0	-0.1	-0.1	*-27.1*	*-192.8*
Administrative expenses	-0.1	-0.3	-0.7	*-157.3*	*-1,008.6*
Total expenses	-13.4	-14.9	-14.0	*5.8*	*-4.4*
Core PBT	23.2	21.5	21.0	*-2.3*	*-9.3*
Core PAT	23.2	21.5	21.0	*-2.3*	*-9.3*
Distributable adjustments	0.0	0.0	1.4	*N/A*	*N/A*
Distributable income	23.2	21.5	22.4	*N/A*	*N/A*
EPU (realised)	2.17	2.01	1.97	*-2.3*	*-9.3*
DPU (sen)	0.00	4.16	0.00	*N/A*	*N/A*

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BUY	Expected absolute return of +10% or more over the next 12-months.
HOLD	Expected absolute return of -10% to +15% over the next 12-months.
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