

UOBKH HIGHLIGHTS

MRCB-Quill REIT (MQREIT MK/BUY/RM1.07/Target: RM1.13)

1H19: Below Expectations; Earnings To Recover in 2020

Year to 31 Dec	2Q19 (RMm)	1Q19 (RMm)	qoq % chg	yoy % chg	1H19 (RMm)	yoy % chg	Year	EPU (sen)	PE (x)
Gross Revenue	38.8	41.4	(6.3)	(10.7)	80.2	(8.3)	2019F	6.9	15.6
Operating Expenses	(9.7)	(9.3)	3.8	(3.4)	(19.0)	(3.8)	2020F	7.6	14.1
Net Property Income	29.1	32.0	(9.2)	(12.8)	61.1	(9.6)	2021F	7.8	13.8
Finance Cost	(9.7)	(9.9)	(1.3)	(2.1)	(19.6)	(0.2)			
Core Net Profit	16.5	19.4	(15.2)	(22.7)	35.9	(15.2)			
EPU (sen)	1.5	1.8	(15.2)	(23.0)	3.3	(15.5)			
DPU (sen)	3.4	0.0	n.a.	(18.9)	3.4	(18.9)			

Source: MRCB-Quill Reit, UOB Kay Hian

RESULTS

- **Below expectations.** MRCB-Quill REIT (MQREIT) reported revenue of RM80.2 m (-8.3% yoy) and core net profit of RM35.9m (-15.2% yoy) for 1H19. Core net profit accounts for 44.2% and 43.3% of our and consensus' full-year forecasts respectively. Results were below our expectations. We expect earnings to recover in 2020, stemming from improved occupancy for Menara Shell and Platinum Sentral.
- **Declared 3.43 sen dividend during the quarter**, which translates to an annualised dividend yield of 6.4%. This accounts for 47.2% and 45.7% of our and consensus full-year forecasts respectively.
- **1H19 net profit declined 15.2% yoy**, due to: a) absence of income from QB8-DHL XPJ which was sold in Apr 18, and b) lower revenue from Platinum Sentral, QB5 and Wisma Technip. The surprise came from the vacant QB5 property where IBM terminated their tenancy in April. However, QB5's contribution to total revenue is minimal at about 3-5%. Earnings declined on a qoq basis due to the absence of contribution from QB5 and new leases from core assets (Platinum Sentral and Menara Shell). We expect earnings to improve slightly for 2H19.
- **Occupancy rate to improve.** Occupancy rate for Menara Shell improved to 96% as at 28 Jun 19 (1Q19:90%). On a portfolio basis, occupancy rate remained at 89% (1Q19:89%, 2Q18: 96%) but is still higher than the average of 78% in 2018 for offices in the Kuala Lumpur. This is mainly due to MQREIT's purpose-built strategy which allows it to lock in long-term leases. MQREIT's WALE is 5.35 years. Total lease for renewal for 2019 and 2020 are 19% and 18% of total NLA respectively. MQREIT successfully renewed 88% of leases due for 2019, including advanced renewal of leases due in 4Q19.
- **Gearing at 37.1%.** We think MQREIT's current gearing ratio is healthy (on a par with peers), which allows it to tap into debt and equity markets for future acquisitions.
- We reduce our earnings forecasts by 9.3%/4.1%/5.9% for 2019/20/21 as we lower our assumptions on occupancy rates (2019:88%, 2020:91%) and rental rates and remove QB5's contribution. QB5 is located in Cyberjaya. Management guided that office space demand in Cyberjaya is not as high as that in the KL fringe.

VALUATION/RECOMMENDATION

- **Maintain BUY with lower target price of RM1.13** (from RM1.15), after our earnings adjustments and rolling forward our valuation to 2020. Total return inclusive of dividend yield is above 10%. Our target price is based on a dividend discount model (required rate of return: 6.6%, terminal growth: 1.3%) and represents an implied dividend yield of 6.6%. We expect the likely sustained overhang on share price from tenancy renewal risks to be compensated for by high dividend yields of 6.3-7.1% for 2019-21.

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