

CHINA  
DEVELOPMENT  
FINANCIAL

# Manulife US REIT

## (MUST SP/MANU.SI)

### 3Q18 results in line with expectations; opportunity to accumulate after sell-off

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- **Positive 3Q18 results.** Manulife US REIT (MUST) reported 3Q18 distributable income of US\$19.3mn (+65% YoY), mainly led by higher contribution from acquisitions of Plaza, Exchange, Penn and Phipps.
- **Up 3.4% on an adjusted basis.** Normalising the impact of the enlarged unit base from the issuance of preferential offering on 20 June 2018, 3Q18 DPU would have increased by 3.4% YoY to 1.52 US cents.
- **Short-term concerns.** MUST's unit price collapsed 10% over two weeks to a low of 69.5 US cents on 31 October following concerns that an unfavourable tax ruling could result in a 30% cut to MUST's distribution to unitholders.
- **Maintain BUY.** Following a change of analyst, we maintain our BUY recommendation but lower our TP to US\$0.92 on changes to our forecasts.

#### Financials & Key Operating Statistics

| YE Dec USD mn        | 2016  | 2017 | 2018F | 2019F | 2020F |
|----------------------|-------|------|-------|-------|-------|
| Gross revenue        | 47.5  | 92.0 | 139.6 | 145.4 | 162.9 |
| Net property income  | 30.0  | 58.4 | 89.4  | 93.1  | 104.3 |
| Distributable income | 22.3  | 46.7 | 78.4  | 84.4  | 88.3  |
| DPU (US cents)       | 3.6   | 5.8  | 5.8   | 6.2   | 6.4   |
| DPU growth (%)       | -     | 62.5 | 1.1   | 6.6   | 3.5   |
| Div Yield (%)        | 4.7   | 6.4  | 7.7   | 8.2   | 8.5   |
| NAV (USD)            | 87.0  | 82.0 | 85.3  | 84.4  | 83.4  |
| Price / Book (x)     | 0.9   | 1.1  | 0.9   | 0.9   | 0.9   |
| NPI Margin (%)       | 63.1  | 63.4 | 64.0  | 64.0  | 64.0  |
| Net Margin (%)       | 108.8 | 63.0 | 46.7  | 41.3  | 43.0  |
| Gearing (%)          | 33.6  | 33.5 | 36.3  | 36.3  | 36.3  |
| ROE (%)              | 9.4   | 6.8  | 6.0   | 5.5   | 6.5   |

Source: Company Data, KGI Research

**Concerns on the impact of new tax rules.** MUST's unit price hit an all-time low of 69.5 US cents on 31 October on worries that a new tax ruling contained in the US tax reform passed in 2017 could result in a 30% cut to MUST's DPU. At the closing price as of 2 Nov, MUST's unit price had declined 15% over the past one year.

**Worst case scenario.** In a conference call arranged by the REIT manager last week to clarify matters, it was suggested that in the worst case scenario, the potential impact would be around 15% to DPU. However, there has been no updates from US tax authorities on this matter, and there is no clarity on if or when this may happen. As such, we think that initial fears may have been overblown and the current sell-off may have created an attractive entry point.

**Portfolio statistics remain robust.** MUST's portfolio occupancy remained robust at 96.5% as at end 3Q18, an improvement from 96.0% as at end 2Q18. It recorded a 13.5% positive rental reversion in the quarter as it signed eight leases with a total NLA of around 69k sqft. As a recap, 95% of leases by gross rental income have rental reversions built into the contracts.

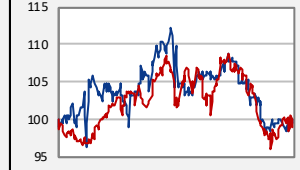
#### Buy (Maintain)

|                            |      |                               |       |
|----------------------------|------|-------------------------------|-------|
| Price as of 5 Nov 18 (USD) | 0.76 | <b>Performance (Absolute)</b> |       |
| 12M TP (US\$)              | 0.92 | 1 Month (%)                   | -3.8  |
| Previous TP (\$)           | 0.97 | 3 Month (%)                   | -9.7  |
| Upside, incl div (%)       | 29.9 | 12 Month (%)                  | -10.2 |

#### Trading data

|                           |       |
|---------------------------|-------|
| Mkt Cap (\$mn)            | 967   |
| Issued Shares (mn)        | 1,273 |
| Vol - 3M Daily avg (mn)   | 1.5   |
| Val - 3M Daily avg (\$mn) | 1.2   |
| Free Float (%)            | 92.6% |

#### Perf. vs STI Index (Red)



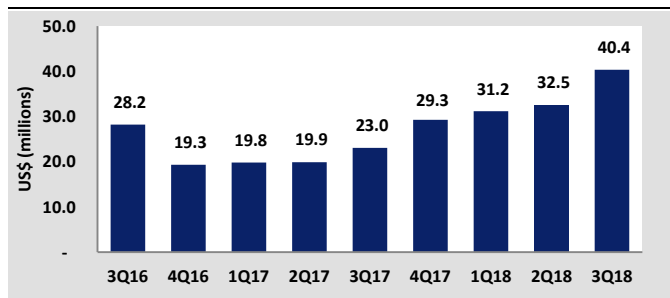
#### Major Shareholders

|                         |      |
|-------------------------|------|
| Manulife Financial Corp | 7.3% |
| DBS Group Holdings      | 3.3% |
| Vanguard Group          | 2.7% |

#### Previous Recommendations

|           |            |
|-----------|------------|
| 13-Aug-18 | BUY \$0.97 |
| 2-May-18  | BUY \$1.02 |
| 17-Apr-18 | BUY \$1.02 |

Figure 1: Quarterly revenue trend. Jump in 3Q18 figures due to acquisitions of Plaza, Exchange, Penn and Phipps)



Source: Company Data, KGI Research

#### Valuation & Action: Maintained BUY with TP of US\$0.92.

We adjust our DPU forecast to 5.8/6.5/6.6 US cents for 2018/19/20F (previously 5.9/6.9/7.4 US cents), mainly on the back of higher interest expenses and lower rental growth assumptions. We think that MUST's dividend yield of 7.7% and 8.2% for 2018/19F may already reflect the uncertainties of potential tax changes. Hence, the recent sell-off may be an opportunity to accumulate as fundamentals of the REIT remains healthy.

**Risks:** A key overhang in the short-term would be uncertainty with the tax changes that could have a negative impact on MUST's DPU. Forex risks for local investors as revenues and unit price are in USD.

## Valuations

Figure 2: DDM valuation

| USD cents, YE 31 December      | FY17 | FY18F       | FY19F | FY20F | FY21F | FY22F | FY23F | FY24F | FY25F |
|--------------------------------|------|-------------|-------|-------|-------|-------|-------|-------|-------|
| <b>DPU</b>                     | 5.8  | 5.8         | 6.2   | 6.4   | 6.6   | 6.8   | 6.9   | 7.1   | 7.3   |
| YoY (%)                        |      | 1.1%        | 6.6%  | 3.5%  | 2.5%  | 2.5%  | 2.5%  | 2.5%  | 2.5%  |
| <b>Terminal value per unit</b> |      |             |       |       |       |       |       |       | 112.0 |
| Cost of Equity                 |      | 9.2%        |       |       |       |       |       |       |       |
| <b>Target Price (US\$)</b>     |      | <b>0.92</b> |       |       |       |       |       |       |       |
| Upside/(Downside)              |      | 22.2%       |       |       |       |       |       |       |       |

Source: KGI Research

Figure 3: Local peers

| Company Name                         | Last Price      | Currency Adj.<br>Market Cap<br>(US\$ m) | Gearing (%)  | Dividend yield (%) |             | P/B (x)    |            | 6M Average<br>daily trading<br>volume<br>(S\$ '000) | (YTD) Price<br>Performance |
|--------------------------------------|-----------------|---|--------------|--------------------|-------------|------------|------------|---|----------------------------|
|                                      |                 |   |              | FY17               | FY18F       | FY17       | FY18F      |   |                            |
| <b>Manulife US REIT</b>              | <b>USD 0.77</b> | <b>973.6</b>                            | <b>37.3%</b> | <b>6.4%</b>        | <b>7.6%</b> | <b>1.1</b> | <b>0.9</b> | <b>1,136.5</b>                                      | <b>-14.6%</b>              |
| <b>Singapore Listed Office REITs</b> |                 |   |              |                    |             |            |            |   |                            |
| Capitaland Commercial Trust          | SGD 1.68        | 4,570.5                                 | 29.8%        | 4.5%               | 5.2%        | 1.1        | 0.9        | 18,600.8  | -13.0%                     |
| Suntec REIT                          | SGD 1.74        | 3,376.9                                 | 35.9%        | 4.7%               | 5.7%        | 1.0        | 0.8        | 13,367.5  | -19.1%                     |
| Keppel REIT                          | SGD 1.13        | 2,798.6                                 | 33.9%        | 4.5%               | 5.1%        | 0.9        | 0.8        | 6,021.8   | -10.3%                     |
| OUE Commercial REIT                  | SGD 0.47        | 963.0                                   | 38.6%        | 6.5%               | 8.2%        | 0.8        | 0.5        | 383.4   | -26.6%                     |
| Frasers Commercial Trust             | SGD 1.38        | 895.1                                   | 30.0%        | 6.6%               | 7.0%        | 0.9        | 0.9        | 1,921.3   | -7.4%                      |
| <b>Average</b>                       |                 | <b>2,520.8</b>                          | <b>33.6%</b> | <b>5.3%</b>        | <b>6.3%</b> | <b>0.9</b> | <b>0.8</b> | <b>8,058.9</b>                                      | <b>-15.3%</b>              |
| <b>Median</b>                        |                 | <b>2,798.6</b>                          | <b>33.9%</b> | <b>4.7%</b>        | <b>5.7%</b> | <b>0.9</b> | <b>0.8</b> | <b>6,021.8</b>                                      | <b>-13.0%</b>              |

Source: Bloomberg, KGI Research

## Financials

FYE 31 December

| INCOME STATEMENT (USD mn)              | 2016A          | 2017A          | 2018F          | 2019F          | 2020F          |
|--|----------------|----------------|----------------|----------------|----------------|
| Gross revenue                          | 47.5           | 92.0           | 139.6          | 145.4          | 162.9          |
| Property expenses                      | (17.5)         | (33.7)         | (50.3)         | (52.4)         | (58.6)         |
| <b>Net property income</b>             | <b>30.0</b>    | <b>58.4</b>    | <b>89.4</b>    | <b>93.1</b>    | <b>104.3</b>   |
| REIT Manager's fees                    | (2.2)          | (4.7)          | (7.8)          | (9.2)          | (9.9)          |
| REIT Trustee's fees                    | (0.1)          | (0.2)          | (0.2)          | (0.2)          | (0.2)          |
| Net interest expense                   | (5.1)          | (9.5)          | (13.6)         | (21.1)         | (21.1)         |
| Other expenses                         | (0.8)          | (1.6)          | (2.5)          | (2.6)          | (2.9)          |
| <b>Net profit/(loss)</b>               | <b>21.7</b>    | <b>42.4</b>    | <b>65.2</b>    | <b>60.0</b>    | <b>70.1</b>    |
| Change in fair value - investment ppty | 52.3           | 31.4           | 0.0            | 0.0            | 0.0            |
| <b>Total return before tax</b>         | <b>74.1</b>    | <b>73.8</b>    | <b>65.2</b>    | <b>60.0</b>    | <b>70.1</b>    |
| Income tax                             | (22.4)         | (15.8)         | 0.0            | 0.0            | 0.0            |
| Total return after tax                 | 51.7           | 58.0           | 65.2           | 60.0           | 70.1           |
| Distributable income                   | 22.3           | 46.7           | 78.4           | 84.4           | 88.3           |
| BALANCE SHEET (USD mn)                 | 2016A          | 2017A          | 2018F          | 2019F          | 2020F          |
| Cash and cash equivalents              | 38.4           | 49.7           | 53.0           | 53.1           | 52.8           |
| Trade and other receivables            | 2.3            | 5.9            | 8.8            | 9.2            | 10.3           |
| Other current assets                   | 0.7            | 0.8            | 0.8            | 0.8            | 0.8            |
| <b>Total current assets</b>            | <b>41.4</b>    | <b>56.4</b>    | <b>62.6</b>    | <b>63.0</b>    | <b>63.9</b>    |
| Investment properties                  | 833.8          | 1,312.8        | 1,752.3        | 1,752.3        | 1,752.3        |
| Intangibles, others                    | 0.0            | 0.0            | 0.0            | 0.0            | 0.0            |
| <b>Total assets</b>                    | <b>875.2</b>   | <b>1,369.2</b> | <b>1,814.9</b> | <b>1,815.3</b> | <b>1,816.2</b> |
| Trade and other payables               | 9.8            | 18.2           | 26.9           | 28.0           | 31.3           |
| Other current liabilities              | 0.2            | 1.0            | 1.0            | 1.0            | 1.0            |
| <b>Total current liabilities</b>       | <b>10.0</b>    | <b>19.2</b>    | <b>27.8</b>    | <b>29.0</b>    | <b>32.3</b>    |
| LT Borrowings                          | 294.2          | 458.4          | 658.9          | 658.9          | 658.9          |
| Other non-current liabilities          | 24.0           | 39.5           | 39.5           | 39.5           | 39.5           |
| <b>Total liabilities</b>               | <b>328.2</b>   | <b>517.1</b>   | <b>726.2</b>   | <b>727.3</b>   | <b>730.7</b>   |
| Unitholders' funds and reserves        | 547.0          | 852.1          | 1,088.7        | 1,088.0        | 1,085.5        |
| <b>Total liabilities and equity</b>    | <b>875.2</b>   | <b>1,369.2</b> | <b>1,814.9</b> | <b>1,815.3</b> | <b>1,816.2</b> |
| CASH FLOW STATEMENT (USD mn)           | 2016A          | 2017A          | 2018F          | 2019F          | 2020F          |
| <b>Total return before tax</b>         | <b>74.1</b>    | <b>73.8</b>    | <b>65.2</b>    | <b>60.0</b>    | <b>70.1</b>    |
| Depreciation & Amortisation            | (3.3)          | (3.5)          | (3.5)          | (3.5)          | (3.5)          |
| Other non-cash adjustments             | (48.3)         | (23.6)         | 13.7           | 32.3           | 26.1           |
| Changes in working capital             | (11.4)         | (1.9)          | 5.8            | 0.8            | 2.3            |
| Taxes paid                             | 0.0            | (1.0)          | 0.0            | 0.0            | 0.0            |
| <b>Cash flows from operations</b>      | <b>11.0</b>    | <b>43.8</b>    | <b>81.1</b>    | <b>89.6</b>    | <b>95.0</b>    |
| Capital expenditure                    | (0.5)          | (9.3)          | 0.0            | 0.0            | 0.0            |
| Acquisition of investment properties   | (758.4)        | (425.0)        | (408.1)        | (15.0)         | (15.0)         |
| Other investing cashflow               | 0.0            | 0.0            | 0.0            | 0.0            | 0.0            |
| <b>Cash flows from investing</b>       | <b>(758.9)</b> | <b>(434.3)</b> | <b>(408.1)</b> | <b>(15.0)</b>  | <b>(15.0)</b>  |
| Borrowings raised / (repaid)           | 296.0          | 165.9          | 200.5          | 0.0            | 0.0            |
| Equity raised / (bought back)          | 519.6          | 288.7          | 192.3          | 0.0            | 0.0            |
| Dividends paid                         | 0.0            | (42.5)         | (59.6)         | (74.5)         | (80.2)         |
| Other financing cashflow               | (29.3)         | (10.4)         | (2.9)          | 0.0            | 0.0            |
| <b>Cash flows from financing</b>       | <b>786.3</b>   | <b>401.7</b>   | <b>330.3</b>   | <b>(74.5)</b>  | <b>(80.2)</b>  |
| FX Effects, Others                     | (0.0)          | 0.1            | 0.0            | 0.0            | 0.0            |
| <b>Net increase in cash</b>            | <b>38.4</b>    | <b>11.2</b>    | <b>3.3</b>     | <b>0.1</b>     | <b>(0.3)</b>   |
| Beginning Cash                         | 0.0            | 38.4           | 49.7           | 53.0           | 53.1           |
| <b>Ending cash</b>                     | <b>38.4</b>    | <b>49.7</b>    | <b>53.0</b>    | <b>53.1</b>    | <b>52.8</b>    |
| KEY RATIOS                             | 2016A          | 2017A          | 2018F          | 2019F          | 2020F          |
| DPU (USD cents)                        | 3.6            | 5.8            | 5.8            | 6.2            | 6.4            |
| Dividend yield %                       | 4.7            | 6.4            | 7.8            | 8.3            | 8.6            |
| NAV per share (USD cents)              | 87.0           | 82.0           | 85.3           | 84.4           | 83.4           |
| Price/NAV (x)                          | 0.9            | 1.1            | 0.9            | 0.9            | 0.9            |
| <b>Profitability (%)</b>               |                |                |                |                |                |
| NPI Margin                             | 63.1           | 63.4           | 64.0           | 64.0           | 64.0           |
| Net Margin                             | 108.8          | 63.0           | 46.7           | 41.3           | 43.0           |
| ROE                                    | 9.4            | 6.8            | 6.0            | 5.5            | 6.5            |
| ROA                                    | 5.9            | 4.2            | 3.6            | 3.3            | 3.9            |
| <b>Financial Structure (x)</b>         |                |                |                |                |                |
| Interest Coverage                      | 5.3            | 5.5            | 5.8            | 3.8            | 4.3            |
| Gearing                                | 33.6           | 33.5           | 36.3           | 36.3           | 36.3           |

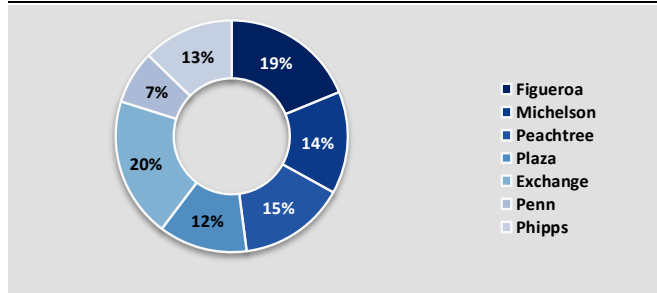
Source: Company Data, KGI Research

**Figure 4: Company profile**

Manulife US Real Estate Investment Trust (MUST) is a Singapore real estate investment trust (REIT) listed on Singapore Exchange Securities Trading Limited (the SGX-ST) since 20 May 2016. Its investment strategy is principally to invest in a portfolio of income-producing office real estate in the US, as well as real estate-related assets. The REIT is managed by Manulife US Real Estate Management Pte. Ltd. (the Manager) which is wholly owned by the Sponsor, The Manufacturers Life Insurance Company (Manulife), part of the Manulife Group.

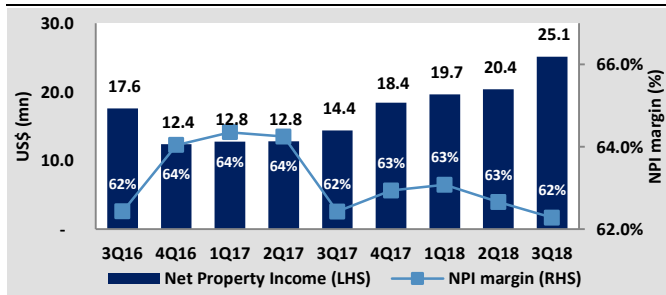
Source: Company

**Figure 5: Portfolio breakdown by NLA**



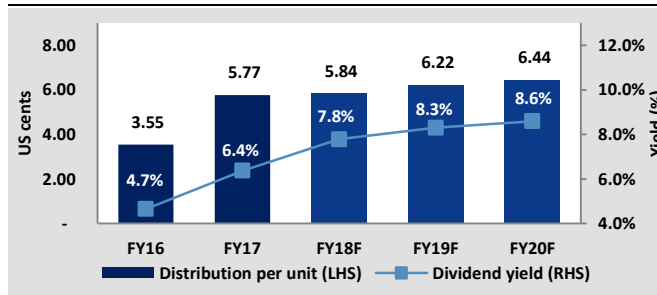
Source: Company Data, KGI Research

**Figure 6: NPI vs NPI margins**



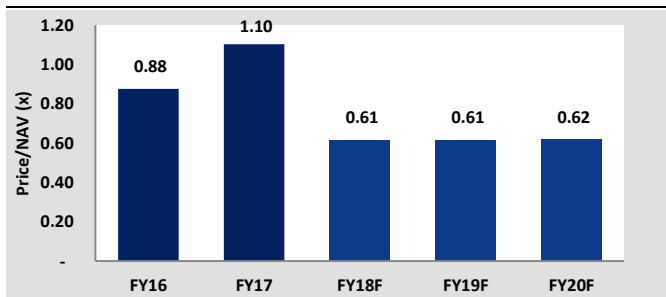
Source: Company Data, KGI Research

**Figure 7: DPU and Dividend yield**



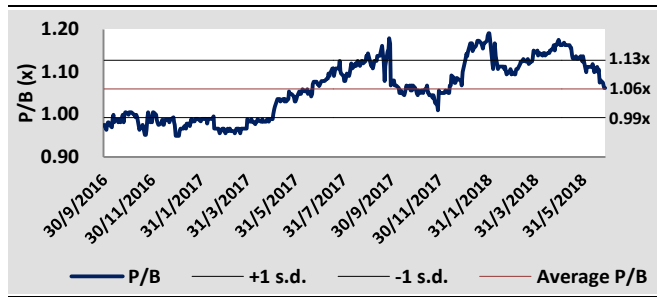
Source: Company Data, KGI Research

**Figure 8: Price/NAV**



Source: Company Data, KGI Research

**Figure 9: Historical P/B band**



Source: Company Data, KGI Research

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| <b>Rating</b> | <b>Definition</b>  |
|---------------|--|
|               | KGI Securities Research's recommendations are based on an Absolute Return rating system. |
| <b>BUY</b>    | >10% total return over the next 12 months  |
| <b>HOLD</b>   | -10% to +10% total return over the next 12 months  |
| <b>SELL</b>   | <-10% total return over the next 12 months   |

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