

CHINA
DEVELOPMENT
FINANCIAL

Manulife US REIT

(MUST SP/MANU.SI)

Back to the office

Joel Ng / 65 6202 1192 / joel.ng@kqi.com

- **Upgrade to Outperform.** US office properties are likely to see improving demand as more employees return, even if it is on a part time basis. Improving fundamentals may finally lift investor confidence in the sector.
- MUST provides an excellent proxy to ride on the “return to office” theme in the US, while offering an attractive 7.4% forward dividend yield.

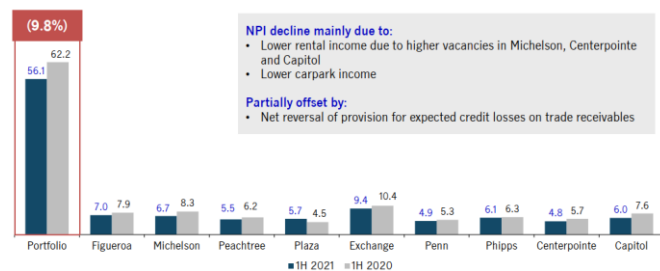
Financials & Key Operating Statistics

YE Dec USD mn	2019	2020	2021F	2022F	2023F
Gross revenue	177.9	194.3	193.7	199.0	203.5
Net property income	110.8	115.8	120.1	123.4	126.2
Distributable income	83.3	89.0	86.1	88.9	91.3
DPU (US cents)	6.0	5.6	5.4	5.5	5.6
DPU growth (%)	67.9	(5.4)	(4.5)	1.9	1.3
Div Yield (%)	5.6	7.6	7.4	7.5	7.6
NAV (US cents)	80.0	73.0	88.1	88.4	88.7
Price / Book (x)	1.3	1.0	0.8	0.8	0.8
NPI Margin (%)	62.3	59.6	62.0	62.0	62.0
Net Margin (%)	26.7	(22.3)	34.8	35.3	35.7
Gearing (%)	38.8	31.0	31.0	31.0	31.0
ROE (%)	3.8	(3.7)	4.7	4.9	4.9

Source: Company Data, KGI Research

Impact from Covid-19. MUST declared a 1H2021 DPU of 2.70 US cents, a decline of 11.5% YoY. The decline comes amid a fall in portfolio occupancy from 96.2% as at end 2Q2020 to 91.7% as at end 2Q2021. Three out of its nine buildings – Michelson, Centrepoint and Capitol – led the decline in rental income.

Figure 1: NPI Income 1H2021 vs 1H2020



Source: Company presentation 1H2021

Positive news. Management has indicated that leasing activity is accelerating. Around 60% of MUST’s tenants have indicated their plans to return to the office from September, lifting revenue such as car park income. MUST has committed occupancy of 91.7% and only 2.9% of leases by NLA due over the remainder of 2021.

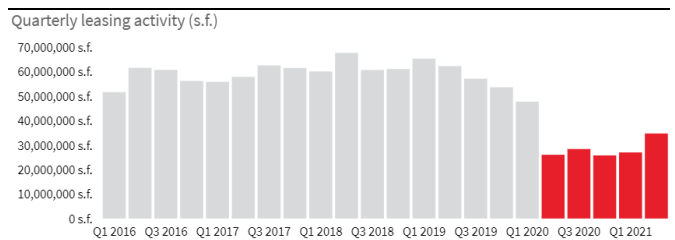
Easing of restrictions and increased vaccinations. The US population has been increasingly vaccinated since January 2021, with 53% of the population vaccinated as of 2 September 2021. Stay-home orders have also been lifted in most states from April to May 2021 and restrictions have been eased for certain indoor and outdoor recreational activities. We foresee a larger percentage of the population returning to the workforce in 2021.

OUTPERFORM - Upgrade

Price as of 7 Sep 21 (USD)	0.73	Performance (Absolute)	
12M TP (USD)	0.82	1 Month (%)	-3.0
Previous TP (USD)	0.86	3 Month (%)	0.2
Upside, incl div (%)	19.8%	12 Month (%)	5.4
Trading data		Perf. vs STI Index (Red)	
Mkt Cap (USD mn)	1,168		
Issued Shares (mn)	1,600		
Vol - 3M Daily avg (mn)	1.9		
Val - 3M Daily avg (USD mn)	1.5		
Free Float (%)	16.2		
Major Shareholders		Previous Recommendations	
Manulife Financial Corp	6.2%	13-Aug-20	NEUTRAL US\$0.86
Prudential PLC	5.5%	10-Feb-20	NEUTRAL US\$1.11
DBS Group Holdings	3.0%	6-Nov-19	OP US\$1.03

US office transactions volume picking up. After more than four quarters of a subdued office market in the US, leasing activity has started to pick up in 2Q2021. Gross leasing activity rose by 29% QoQ to 35mn sqft in 2Q2021, the first time it has gone above 30mn sqft since the start of Covid-19. Occupancy losses have slowed, and many tenants have now withdrawn space previously placed on the sublease market. According to JLL Research, the positive momentum will accelerate in the second half of 2021, albeit with wide variance based on asset quality and location.

Figure 2: Overall transaction volume of US office space rose by 29% in 2Q2021 as tenants executive long-awaited deals



Source: JLL Research

Valuation & Action: Upgrade to Outperform with a TP of US\$0.82. MUST offers a decent yield of 7.4%, 7.5% and 7.6% for FY2021, FY2022 and FY2023 respectively. MUST’s gearing of 42.1% as of 30 June 2021 remains well below the regulatory 50% limit, while borrowing costs have declined to 2.99%, an improvement of around 20bps from Dec 2020.

Risks: US tax changes would be the key risk, as it would have a negative impact on MUST’s DPU. Forex risks for local investors as revenues, unit price and dividends are in USD. Another potential risk from the impact of Covid-19 is the increased acceptance of work from home and higher-than-expected working from home rate, which may lead to soft office demand.

Valuations

Figure 2: DDM valuation

USD cents, YE 31 December	FY17	FY18	FY19	FY20	FY21F	FY22F	FY23F	FY24F	FY25F
DPU	5.8	6.1	6.0	5.6	5.4	5.5	5.6	5.6	5.7
<i>YoY (%)</i>					(4.5%)	1.9%	1.3%	1.5%	1.5%
Terminal value per unit									88.4
Cost of Equity		8.1%							
Target Price (US\$)		0.82							
<i>Capital Appreciation</i>		12.4%							
<i>Forward Dividend</i>		7.4%							

Source: KGI Research

About Manulife US REIT

Manulife US Real Estate Investment Trust is the first pure-play U.S. office REIT listed in Asia. It is a Singapore listed REIT established with the investment strategy principally to invest, directly or indirectly, in a portfolio of income-producing office real estate in key markets in the United States ("U.S."), as well as real estate-related assets.

Manulife US REIT's portfolio comprises nine prime, freehold and Trophy or Class A quality office properties strategically located in California, Atlanta, New Jersey and Washington D.C. and Virginia. The current portfolio valued at US\$2.0 billion, has an aggregate Net Lettable Area of 4.7 million sq ft and an occupancy rate of 91.7% as at 30 June 2021.

KGI's Ratings

Rating	Definition
Outperform (OP)	We take a positive view on the stock. The stock is expected to outperform the expected total return of the KGI coverage universe in the related market over a 12-month investment horizon.
Neutral (N)	We take a neutral view on the stock. The stock is expected to perform in line with the expected total return of the KGI coverage universe in the related market over a 12-month investment horizon.
Underperform (U)	We take a negative view on the stock. The stock is expected to underperform the expected total return of the KGI coverage universe in the related market over a 12-month investment horizon.
Not Rated (NR)	The stock is not rated by KGI Securities.
Restricted (R)	KGI policy and/or applicable law regulations preclude certain types of communications, including an investment recommendation, during the course of KGI's engagement in an investment banking transaction and in certain other circumstances.

Disclaimer

This report is provided for information only and is not an offer or a solicitation to deal in securities or to enter into any legal relations, nor an advice or a recommendation with respect to such securities. This report is prepared for general circulation. It does not have regard to the specific investment objectives, financial situation and the particular needs of any recipient hereof. You should independently evaluate particular investments and consult an independent financial adviser before dealing in any securities mentioned in this report.

This report is confidential. This report may not be published, circulated, reproduced or distributed and/or redistributed in whole or in part by any recipient of this report to any other person without the prior written consent of KGI Securities. This report is not intended for distribution and/or redistribution, publication to or use by any person in any jurisdiction outside Singapore or any other jurisdiction as KGI Securities may determine in its absolute discretion, where the distribution, publication or use of this report would be contrary to applicable law or would subject KGI Securities and its connected persons (as defined in the Financial Advisers Act, Chapter 110 of Singapore) to any registration, licensing or other requirements within such jurisdiction.

The information or views in the report ("Information") has been obtained or derived from sources believed by KGI Securities to be reliable. However, KGI Securities makes no representation as to the accuracy or completeness of such sources or the Information and KGI Securities accepts no liability whatsoever for any loss or damage arising from the use of or reliance on the Information. KGI Securities and its connected persons may have issued other reports expressing views different from the Information and all views expressed in all reports of KGI Securities and its connected persons are subject to change without notice. KGI Securities reserves the right to act upon or use the Information at any time, including before its publication herein.

Except as otherwise indicated below, (1) KGI Securities, its connected persons and its officers, employees and representatives may, to the extent permitted by law, transact with, perform or provide broking, underwriting, corporate finance-related or other services for or solicit business from, the subject corporation(s) referred to in this report; (2) KGI Securities, its connected persons and its officers, employees and representatives may also, to the extent permitted by law, transact with, perform or provide broking or other services for or solicit business from, other persons in respect of dealings in the securities referred to in this report or other investments related thereto; and (3) the officers, employees and representatives of KGI Securities may also serve on the board of directors or in trustee positions with the subject corporation(s) referred to in this report. (All of the foregoing is hereafter referred to as the "Subject Business".)

However, as of the date of this report, neither KGI Securities nor its representative(s) who produced this report (each a "research analyst"), has any proprietary position or material interest in, and KGI Securities does not make any market in, the securities which are recommended in this report.

Each research analyst of KGI Securities who produced this report hereby certifies that (1) the views expressed in this report accurately reflect his/her personal views about all of the subject corporation(s) and securities in this report; (2) the report was produced independently by him/her; (3) he/she does not carry out, whether for himself/herself or on behalf of KGI Securities or any other person, any of the Subject Business involving any of the subject corporation(s) or securities referred to in this report; and (4) he/she has not received and will not receive any compensation that is directly or indirectly related or linked to the recommendations or views expressed in this report or to any sales, trading, dealing or corporate finance advisory services or transaction in respect of the securities in this report. However, the compensation received by each such research analyst is based upon various factors, including KGI Securities' total revenues, a portion of which are generated from KGI Securities' business of dealing in securities.

Copyright 2021. KGI Securities (Singapore) Pte. Ltd. All rights reserved.