

CHINA  
DEVELOPMENT  
FINANCIAL

# Manulife US REIT

## (MUST SP/MANU.SI)

### 2Q18 results in line with expectations; lower DPU on enlarged unit base

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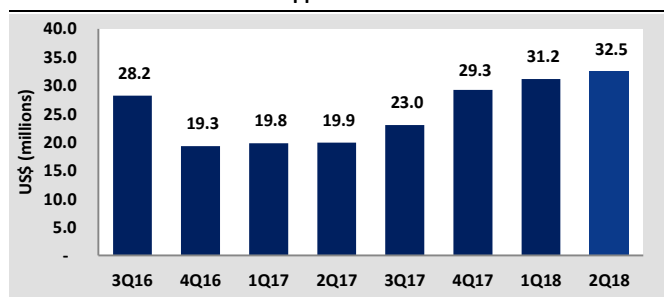
- **Positive 2Q18 results.** Manulife US REIT (MUST) reported 2Q18 distributable income of US\$16.5mn (+65% YoY), mainly led by higher contribution from acquisitions of Plaza, Exchange, Penn and Phipps.
- **DPU fell 17%.** Largely due to the drag from the enlarged unit base from the issuance of preferential offering and only 9 days of income contribution from Penn and Phipps.
- **But up 5.5% on an adjusted basis.** Normalising the impact of the enlarged unit base from the issuance of preferential offering, DPU would have been higher.

Financials & Key Operating Statistics					
YE Dec USD mn	2016	2017	2018F	2019F	2020F
Gross revenue	47.5	92.0	139.6	145.4	168.7
Net property income	30.0	58.4	89.4	93.1	108.0
Distributable income	22.3	46.7	78.4	91.9	99.3
DPU (US cents)	3.6	5.8	5.9	6.9	7.4
DPS growth (%)	-	62.5	1.7	17.2	8.1
Div Yield (%)	4.7	6.4	6.8	7.9	8.6
NAV (USD)	87.0	82.0	140.7	140.7	139.9
Price / Book (x)	0.9	1.1	0.6	0.6	0.6
NPI Margin (%)	63.1	63.4	64.0	64.0	64.0
Net Margin (%)	108.8	63.0	46.7	46.4	48.1
Gearing (%)	33.6	33.5	36.3	36.3	36.3
ROE (%)	9.4	6.8	6.0	6.2	7.5

Source: Company Data, KGI Research

**Portfolio statistics still remain robust.** MUST's portfolio occupancy remained robust at 96.0% (as at 2Q18) with less than 10.0% of leases, by NLA, expiring between 2H18 and 2019. The overall Weighted Average Lease Expiry (WALE), by NLA, has increased significantly from 5.7 to 6.3 years, with 60.4% of the leases, by NLA, expiring in 2023 and beyond. We noted that gross gearing has inched up slightly from 34% to 37% as a result of MUST's recent acquisitions. Debt maturity remains unchanged at 3.2 years and 100% of its debt remains fixed, at an average rate of 3.3% (as at 2Q18).

Figure 1: Quarterly revenue trend (2Q18 only accounts for 9 days of contribution from Penn and Phipps)



Source: Company Data, KGI Research

**2Q18 results supported by positive rental reversions of 7.2%.** As at 2Q18, 94% of leases by Gross Rental Income have contractual rental escalation clauses. The positive reversions in 1H18 was mainly led by the 3 new/renewed leases in Figueroa and Exchange, which represented about 2% of the enlarged portfolio's NLA.

Buy (Maintain)		Performance (Absolute)	
Price as of 13 Aug 18 (USD)	0.85	1 Month (%)	1.2
12M TP (US\$)	0.97	3 Month (%)	-7.1
Previous TP (\$)	1.02	12 Month (%)	4.3
Upside, incl div (%)	22.0		
Trading data		Perf. vs STI Index (Red)	
Mkt Cap (\$mn)	1,073		
Issued Shares (mn)	1,270		
Vol - 3M Daily avg (mn)	1.3		
Val - 3M Daily avg (\$mn)	1.1		
Free Float (%)	92.6%		
Major Shareholders		Previous Recommendations	
Manulife Financial Corp	7.3%	21-Feb-18	1.01
DBS Group Holdings	3.3%	17-Apr-18	1.01
Vanguard Group	2.7%	2-May-18	1.02

**Inorganic growth strategy still unchanged; Higher emphasis on enlarged portfolio.** In view of the rising interest rate environment, the management has expressed its intention to concentrate on organic growth by proactively managing leases and capital management e.g. securing early renewals of leases. Focus is on Figueroa, which will be refinanced in 2019 (16.4% of total debt).

**US office market remains upbeat.** The annualised real GDP for 2Q18 was reported at 4.1% from a revised 2.2% in 1Q18. The strong GDP growth in 2Q18 was mainly led by higher consumer spending, exports and government spending. Unemployment rate decreased 0.1% from the previous quarter to 4.0%. The US economy generated 213,000 non-farm jobs in June 2018, primarily in the professional and business services, health care and manufacturing sectors. While the numbers are assuring, volatility in the financial markets remain high, driven by geopolitical rhetoric. We take comfort in MUST's diversified tenant mix with no tenant contributing more than 7.5% of Gross Rental Income.

**Valuation & Action: Maintained BUY with TP of US\$0.97, revised down from US\$1.02 previously.** We adjust our DPU forecast of 5.9/6.9/7.4 US cents in 2018/19/20F. Risk free assumption was adjusted from 2.54% to 2.67% (consensus forecast); Discount rate adjusted down from 9.54% to 9.39%.

**Risks:** Interest rate risk in the medium term (near term impact of rising rates mitigated). Trade tension may have a far-reaching impact on economic activity, which could have a trickle-down effect on the REIT and its ability to renew leases. Additional supply in the respective micro markets could have a direct impact on market rents.

## Results update

Figure 2: Results comparison

FYE Dec (USD mn)			yoy %		qoq %		Comments
	2QFY18	2QFY17	chg	1QFY18	chg	FY19F	
Gross revenue	32.5	19.9	63.4	31.2	4.4	145.4	Mainly attributed to contributions from the acquisitions of Plaza, Exchange, Penn & Phipps
Property expenses	(12.1)	(7.1)	70.6	(11.5)	5.6	(52.4)	
<b>Net property income</b>	<b>20.4</b>	<b>12.8</b>	<b>59.3</b>	<b>19.7</b>	<b>3.7</b>	<b>93.1</b>	
<i>NPI margin (%)</i>	<i>63%</i>	<i>64%</i>		<i>63%</i>		<i>64%</i>	
REIT Manager's fees	(1.7)	(1.0)	65.3	(1.6)	5.6	(9.2)	
REIT Trustee's fees	(0.1)	(0.0)	41.0	(0.1)	3.8	(0.2)	
Net interest expense	(3.748)	(1.987)	88.6	(3.7)	0.5	(13.6)	Due to incremental borrowings used to partially fund the acquisitions of Plaza, Exchange, Penn and Phipps
Other expenses	(0.622)	(0.393)	58.3	(0.5)	26.2	(2.6)	
<b>Net profit/(loss)</b>	<b>14.301</b>	<b>9.371</b>	<b>52.6</b>	<b>13.8</b>	<b>3.5</b>	<b>67.4</b>	
Change in FV - invt ppty	10.8	20.2	(46.5)	(0.9)	nm	0.0	Recognised gains from 30 June 2018 appraisals
<b>Total return before tax</b>	<b>25.1</b>	<b>29.5</b>	<b>(15.1)</b>	<b>12.9</b>	<b>94.9</b>	<b>67.4</b>	
Income tax	(6.1)	(8.3)	(26.7)	(1.3)	355.9	0.0	Due to lower deferred tax expense resulting from lower net fair value gain in investment properties
<b>Total return after tax</b>	<b>19.0</b>	<b>21.2</b>	<b>(10.5)</b>	<b>11.5</b>	<b>64.8</b>	<b>67.4</b>	Largely due to lower net fair value gain in investment properties
Income avail for distribution	16.5	10.0	65.3	15.6	5.6	91.9	Due to higher NPI
DPU (cents)	1.30	1.44	(9.7)	1.51	(13.9)	6.9	

Source: Company Data, KGI Research

Figure 3: DDM valuation

USD cents, YE 31 December	FY17	FY18F	FY19F	FY20F	FY21F	FY22F	FY23F	FY24F	FY25F
<b>DPU</b>	5.8	5.9	6.9	7.4	7.6	7.8	8.0	8.2	8.4
<i>YoY (%)</i>		<i>1.7%</i>	<i>17.2%</i>	<i>8.1%</i>	<i>2.5%</i>	<i>2.5%</i>	<i>2.5%</i>	<i>2.5%</i>	<i>2.5%</i>
<b>Terminal value per unit</b>									120.2
Cost of Equity		9.67%							
<b>Target Price (US\$)</b>		<b>0.97</b>							
<i>Upside/(Downside)</i>		<i>15.1%</i>							

Source: KGI Research

Figure 4: Local peers

Company Name	Last Price	Currency Adj. Market Cap (US\$ m)	Gearing (%)	Dividend yield (%)		P/B (x)		6M Average daily trading volume (\$'000)	(YTD) Price Performance
				FY17	FY18F	FY17	FY18F		
<b>Manulife US REIT</b>	<b>USD 0.85</b>	<b>1,073.0</b>	<b>37.3%</b>	<b>6.4%</b>	<b>6.9%</b>	<b>1.1</b>	<b>1.0</b>	<b>1,114.1</b>	<b>-5.7%</b>
<b>Singapore Listed Office REITs</b>									
Capitaland Commercial Trust	SGD 1.72	4,679.7	29.8%	4.5%	5.2%	1.1	1.0	20,937.7	-10.9%
Suntec REIT	SGD 1.91	3,702.7	35.9%	4.7%	5.2%	1.0	0.9	14,877.4	-11.2%
Keppel REIT	SGD 1.16	2,874.0	33.9%	4.5%	5.1%	0.9	0.8	5,672.3	-7.9%
OUE Commercial REIT	SGD 0.68	760.1	38.6%	6.5%	6.5%	0.8	0.5	112.5	-6.3%
Frasers Commercial Trust	SGD 1.40	900.8	36.7%	7.1%	7.0%	0.9	0.9	2,239.0	-6.0%
<b>Average</b>		<b>2,583.5</b>	<b>35.0%</b>	<b>5.5%</b>	<b>5.8%</b>	<b>0.9</b>	<b>0.8</b>	<b>8,767.8</b>	<b>-8.5%</b>
<b>Median</b>		<b>2,874.0</b>	<b>35.9%</b>	<b>4.7%</b>	<b>5.2%</b>	<b>0.9</b>	<b>0.9</b>	<b>5,672.3</b>	<b>-7.9%</b>

Source: Bloomberg, KGI Research

## Financials

INCOME STATEMENT (USD mn)	2016A	2017A	2018F	2019F	2020F
Gross revenue	47.5	92.0	139.6	145.4	168.7
Property expenses	(17.5)	(33.7)	(50.3)	(52.4)	(60.7)
<b>Net property income</b>	<b>30.0</b>	<b>58.4</b>	<b>89.4</b>	<b>93.1</b>	<b>108.0</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)	(13.6)	(13.6)
Other expenses	(0.8)	(1.6)	(2.5)	(2.6)	(3.0)
<b>Net profit/(loss)</b>	<b>21.7</b>	<b>42.4</b>	<b>65.2</b>	<b>67.4</b>	<b>81.2</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>67.4</b>	<b>81.2</b>
Income tax	(22.4)	(15.8)	0.0	0.0	0.0
Total return after tax	51.7	58.0	65.2	67.4	81.2
Distributable income	22.3	46.7	78.4	91.9	99.3
BALANCE SHEET (USD mn)	2016A	2017A	2018F	2019F	2020F
Cash and cash equivalents	38.4	49.7	53.0	53.1	50.1
Trade and other receivables	2.3	5.9	8.8	9.2	10.6
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>61.6</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>1,813.9</b>
Trade and other payables	9.8	18.2	26.9	28.0	32.4
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>33.4</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>731.8</b>
Unitholders' funds and reserves	547.0	852.1	1,088.7	1,088.0	1,082.1
<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>1,813.9</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>67.4</b>	<b>81.2</b>
Depreciation & Amortisation	(3.3)	(3.5)	(3.5)	(3.5)	(3.5)
Other non-cash adjustments	(48.3)	(23.6)	13.7	24.9	18.6
Changes in working capital	(11.4)	(1.9)	5.8	0.8	3.1
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>99.3</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)	(87.3)
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>(87.3)</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>(2.9)</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>50.1</b>
KEY RATIOS	2016A	2017A	2018F	2019F	2020F
DPU (USD cents)	3.6	5.8	5.9	6.9	7.4
Dividend yield %	4.7	6.4	6.8	7.9	8.6
NAV per share (USD cents)	87.0	82.0	140.7	140.7	139.9
Price/NAV (x)	0.9	1.1	0.6	0.6	0.6
<b>Profitability (%)</b>					
NPI Margin	63.1	63.4	64.0	64.0	64.0
Net Margin	108.8	63.0	46.7	46.4	48.1
ROE	9.4	6.8	6.0	6.2	7.5
ROA	5.9	4.2	3.6	3.7	4.5
<b>Financial Structure (x)</b>					
Interest Coverage	5.3	5.5	5.8	5.9	6.9
Gearing	33.6	33.5	36.3	36.3	36.3

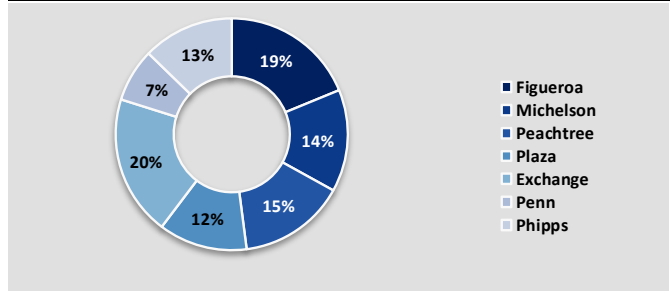
Source: Company Data, KGI Research

Figure 5: 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.

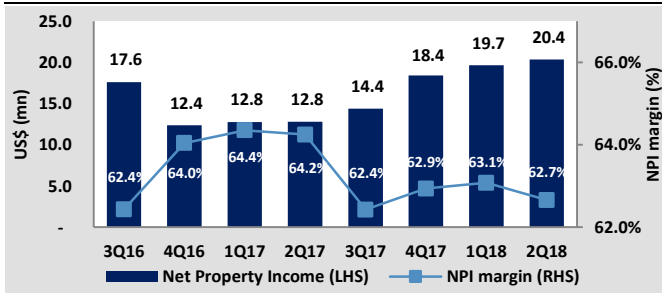
Source: Company

Figure 6: Portfolio breakdown by NLA



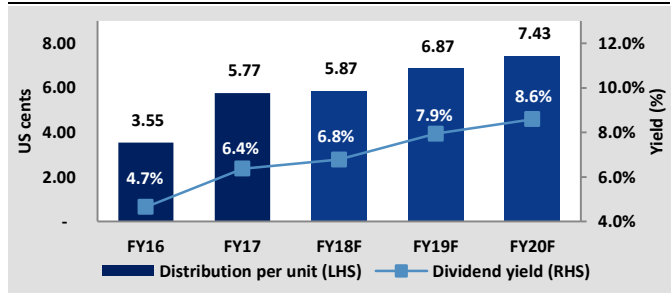
Source: Company Data, KGI Research

Figure 7: NPI vs NPI margins



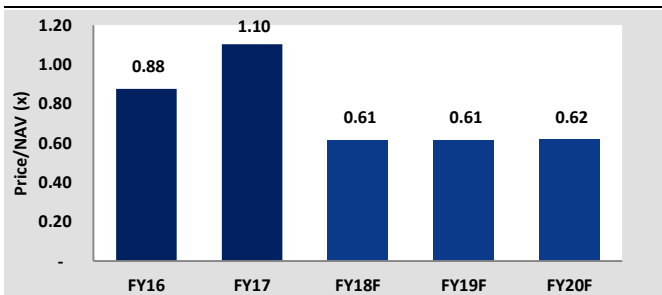
Source: Company Data, KGI Research

Figure 8: DPU and Dividend yield



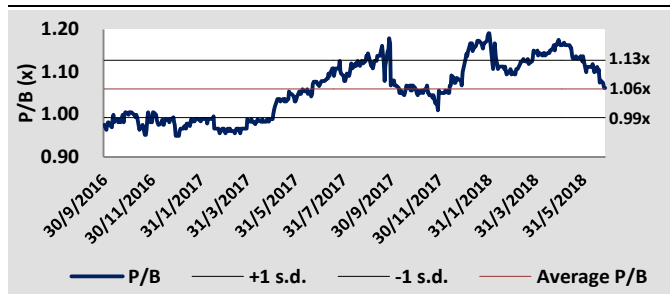
Source: Company Data, KGI Research

Figure 9: Price/NAV



Source: Company Data, KGI Research

Figure 10: Historical P/B band



Source: Company Data, KGI Research

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<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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