

14 February 2017

Property | REITS

Manulife US REIT

Buy (Maintained)

Riding The “Trumponomics”

Target Price: USD0.96
 Price: USD0.86
 Market Cap: USD540m
 Bloomberg Ticker: MUST SP

MUST reported a strong set of maiden FY16 results with DPU exceeding its IPO forecasts by 5%. Among S-REITs, MUST offers the best proxy to the strengthening US economy via its three quality freehold office properties. The US office market is gaining traction with strong jobs data and the new president’s pro-business policy stance likely to provide further impetus. With the REIT offering superior FY17F yields of 7.3%, above S-REITs average of 6.4%, we believe there is room for further yield compression. Maintain BUY and a TP of USD0.96 (12% upside).

Share Data

Avg Daily Turnover (USD/USD) 0.92m/0.92m
 52-wk Price low/high (USD) 0.79 - 0.86
 Free Float (%) 93
 Shares outstanding (m) 628
 Estimated Return 12%

US office market gaining momentum. Manulife US REIT’s (MUST) office properties achieved strong rent reversions of +10.5% for FY16 on the back of higher demand and favourable market dynamics. For 2017, about 5.5% of portfolio (as % of NLA) is up for renewal and we expect rent reversions to be in the mid-single digits. Figueroa was the best performing asset in 2016 with double digit rent reversions (+11.6%) for ~99,000 sqf of lease renewals (14% of total GFA). The strong reversions came on the back of more companies moving to Downtown LA to capitalise on the growing millennial population.

Shareholders (%)

Manulife Financial Corp 7.7
 Credit Suisse Group AG 3.1
 Vanguard Group 1.9

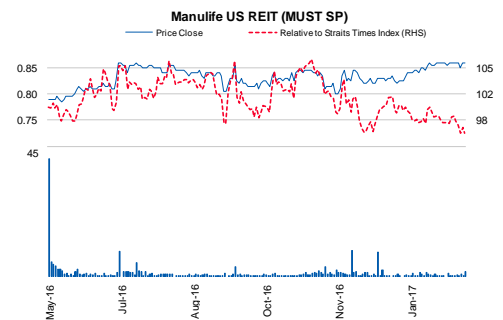
Watch out for acquisitions. Management has been actively looking for acquisitions and has placed bids for few assets. The acquisitions are expected to be bite sized at USD100-150m likely targeting secondary cities to provide diversification. Gearing has come down to 33.8% providing more flexibility. Its sponsor, Manulife Group, has a US office portfolio assets of >USD6bn, providing a strong pipeline in addition to third party assets.

Share Performance (%)

	YTD	1m	3m	6m	12m
Absolute	4.2	1.8	2.4	1.8	
Relative	(3.4)	(1.3)	(7.0)	(6.0)	

Source: Bloomberg

Muted impact from Federal Reserve (Fed) rate hikes. While the expectation of Fed rate hikes remains an overhang on REITs, the impact on MUST is minimal in our view. Key reasons being that such an event would coincide with a stronger US economy, resulting in higher office demand. It would also result in a stronger USD, benefitting Asian currency investors. With 100% of its borrowings fixed until Jul 2019, there is no impact to its finance costs from Fed rate hikes in the near-term.



Source: Bloomberg

4Q16 earnings announced on 13 Feb 2017 are in line

(SGDm)	4Q16	4Q16F*	% Chg	FY16	% Chg**	Comments
Revenue	19.3	19.7	(2.1)	47.5	(1.5)	Lower recovery revenue
NPI	12.4	12.4	0.2	30.0	1.0	Lower property tax and utilities
NPI (%)	64.2	62.6	1.6ppt	63.1	1.5ppt	
Net Income	18.0	6.8	163.4	51.7	217.1	Revaluation gains
Unitholders Distribution	9.7	9.4	3.6	22.3	4.8	Lower interest expenses
DPU	1.54	1.49	3.6	3.55	4.8	100% Payout ratio

*IPO forecast data; ** Compared to IPO forecast; Source: Company data, RHB

Maintain BUY with unchanged TP of USD0.96. Our TP is based on a 5-Year DDM model (COE: 8.5%, TG: 2%). MUST offers high FY17F-18F dividend yields of 7.3% and 7.5% respectively, a good 100bps above the office S-REITs average and 400bps above 10-year treasury yields. Key risks are the ability to retain its key office tenants, changes to the underlying tax-efficient structure, and the US economic growth faltering.

Forecasts and Valuations	Dec-15	Dec-16*	Dec-17F	Dec-18F	Dec-19F
Total turnover (USDm)	70.9	47.5	80.8	83.2	84.4
Net property income (USDm)	44.2	30.0	50.4	51.9	52.6
Reported net profit (USDm)	26.0	51.7	43.7	44.9	45.5
Total distributable income (USDm)	26.0	22.3	39.7	40.9	41.4
DPS (USD)	na	0.06	0.06	0.06	0.06
DPS growth (%)	0.0	0.0	8.8	2.3	0.3
Recurring P/E (x)	20.8	10.5	12.5	12.3	12.2
P/B (x)	1.10	0.99	0.99	0.98	0.97
Dividend Yield (%)	na	6.7	7.3	7.5	7.5
Return on average equity (%)	10.6	10.0	7.9	8.0	8.0
Return on average assets (%)	6.5	6.2	5.0	5.1	5.1
Interest cover (x)	4.01	5.27	6.17	6.21	6.14
Our vs consensus EPS (adjusted)					

*20 May – Dec 2016, DPS is annualised; Source: Company data, RHB

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Financial Exhibits

Financial model updated on : 2017-02-13.

		Dec-15	Dec-16*	Dec-17F	Dec-18F	Dec-19F
Asia						
Singapore						
Property						
Manulife US Real Estate Investment Trust						
Bloomberg	MUST SP					
Buy						
Financial summary						
	Recurring EPS (USD)	0.04	0.08	0.07	0.07	0.07
	EPS (USD)	0.04	0.08	0.07	0.07	0.07
	DPS (USD)	0.00	0.06	0.06	0.06	0.06
	BVPS (USD)	0.78	0.86	0.87	0.88	0.88
	Weighted avg adjusted shares (m)	629	630	635	640	645
Valuation basis						
DDM						
Key drivers						
i. Organic rental growth;						
ii. Growth from yield accretive acquisitions;						
iii. Positive demand-supply dynamics in US office market.						
Key risks						
i. Ability to retain key tenants,						
ii. Changes in tax structure, and						
iii. US economic growth falters						
Company Profile						
Manulife US Real Estate Investment Trust (MUST) is the first pure-play U.S. office REIT listed in Asia. It is a Singapore 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 US, as well as real estate-related assets.						
Valuation metrics						
	Recurring P/E (x)	20.8	10.5	12.5	12.3	12.2
	P/E (x)	20.8	10.5	12.5	12.3	12.2
	P/B (x)	1.10	0.99	0.99	0.98	0.97
	FCF Yield (%)	(136.4)	(138.7)	4.0	4.2	4.1
	Dividend Yield (%)	0.0	6.7	7.3	7.5	7.5
	EV/EBITDA (x)	20.0	33.9	19.7	19.2	19.2
	EV/EBIT (x)	21.1	29.7	18.4	18.0	17.9
Income statement						
	Total turnover (USDm)	70.9	47.5	80.8	83.2	84.4
	EBITDA (USDm)	40.6	23.5	41.7	43.1	43.6
	Depreciation and amortisation (USDm)	(2.1)	3.3	3.0	2.9	3.0
	Operating profit (USDm)	38.5	26.8	44.7	46.0	46.6
	Net interest (USDm)	(9.6)	(5.1)	(7.2)	(7.4)	(7.6)
	Pre-tax profit (USDm)	27.3	74.1	45.8	47.0	47.6
	Taxation (USDm)	(1.4)	(22.4)	(2.1)	(2.1)	(2.1)
	Recurring net profit (USDm)	26.0	51.7	43.7	44.9	45.5
Cash flow (USDm)						
	Change in working capital	(15)	(16)	(20)	(20)	(21)
	Cash flow from operations	31	11	26	27	27
	Capex	(769)	(763)	(4)	(4)	(4)
	Cash flow from investing activities	(769)	(763)	(4)	(4)	(4)
	Proceeds from issue of shares	491	492	0	0	0
	Dividends paid	(18)	0	(40)	(41)	(41)
	Cash flow from financing activities	762	786	(34)	(19)	(19)
	Cash at beginning of period	0	25	38	26	30
	Net change in cash	24	35	(12)	4	4
	Ending balance cash	24	59	26	30	34
Balance sheet (USDm)						
	Total cash and equivalents	25	38	26	30	34
	Tangible fixed assets	777	834	846	859	872
	Total assets	804	875	875	891	908
	Total long-term debt	294	294	301	308	315
	Other liabilities	4	23	4	5	6
	Total liabilities	314	328	320	328	336
	Shareholders' equity	490	547	555	563	572
	Total equity	490	547	555	563	572
	Net debt	269	256	275	278	282
	Total liabilities & equity	804	875	875	891	908
Key metrics						
	Revenue growth (%)	0.0	(33.0)	70.1	3.0	1.4
	Recurrent EPS growth (%)	0.0	98.5	(16.1)	2.0	0.4
	Operating EBITDA margin (%)	57.2	49.5	51.5	51.8	51.6
	Net profit margin (%)	36.6	108.8	54.1	54.0	53.8
	Capex/sales (%)	1084.5	1605.5	5.2	5.1	5.1
	Interest cover (x)	4.01	5.27	6.17	6.21	6.14

Note: *Performance since IPO on 20 May 2016

Source: Company data, RHB

Portfolio valuation up 7.2% since listing. In line with positive market fundamentals property valuations increased 5 - 10% across its properties, mainly aided by compressing capital rates. Gearing ratio correspondingly declined to 33.8%, from 36.8%. Portfolio occupancy remained steady at 97% with the remaining weighted average lease to expiry (WALE) of 5.8years.

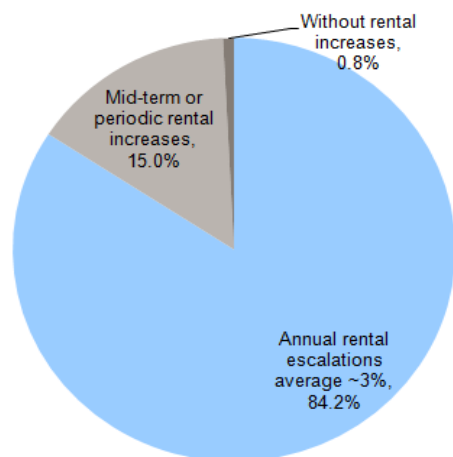
FY16 DPU beats IPO forecast by 4.8%, Results in line. FY16 gross revenue was 1.5% lower than its IPO forecasts due to lower recovery revenue while net property income (NPI) exceeded by 1% on the back of lower property taxes and utility expenses. DPU exceeded IPO forecasts by 4.8% on the back of interest cost savings from lower refinancing cost for its bridge loan. The results were in line with ours and consensus expectations.

Figure 1: DDM valuation table

	FY16	FY17F	FY18F	FY19F	FY20F	FY21F	Terminal Value
DPU (USD Cts)	5.8	6.3	6.4	6.4	6.5	6.7	105.8
Target price (USD)	0.96						
Current Price (USD)	0.86						
Price Upside (%)	11%						
Distribution Yield FY17F (%)	7.3%						
Assumptions							
Risk-free rate (%)	3%						
Beta	1.00						
Cost of equity (%)	8.5%						
Terminal growth (%)	2%						

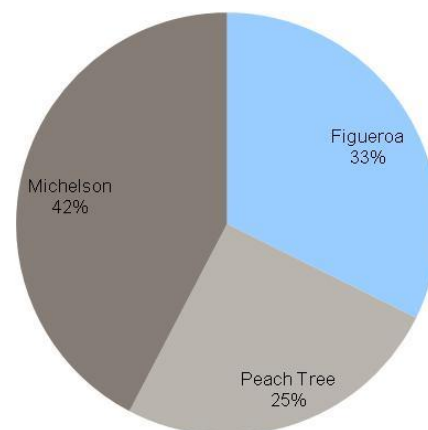
Source: RHB

Figure 2: Portfolio rental escalations breakdown



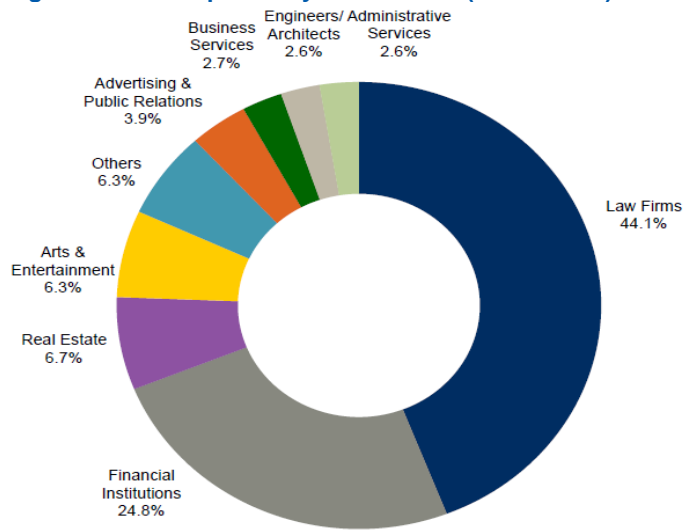
Source: Company data, RHB

Figure 3: NPI breakdown by property (FY16) *



Note: *20 May – Dec 2016 ;
Source: Company data, RHB

Figure 4: Tenant profile by trade sector (as % of CRI)



Source: Company data

Figure 5: Lease expiry profile



Source: Company data

Figure 6: Portfolio rent reversions – FY16

Property	Percentage of Total NLA	Net Lettable Area (sq ft)	Rental Reversion (%)
Figueroa	14.3%	99,127	11.6
Michelson	0.7%	3,889	9.9
Peachtree	5.0%	27,870	5.8
Total	7.3%	130,886	10.5

Source: Company data

Figure 7: Office market overview – portfolio locations

Market	RBA ¹ (mil sq ft)	Vacancy (%)	Gross Asking Rent	Net Absorption ('000 sq ft)	12 Month Rent Growth (%)	New Properties Under Construction ('000 sq ft)	Property Name	Delivery Year
Downtown Los Angeles	39.6	15.4	US\$38.15	(142)	7.3	370	Office Plaza at Wilshire Grand	2017
Irvine, Orange County	13.8	12.5	US\$32.30	(242)	7.3	537	The Boardwalk	2017
Midtown Atlanta	17.9	11.2	US\$31.92	105	7.6	485	NCR Corp Headquarters	2018
						760	Coda	2019

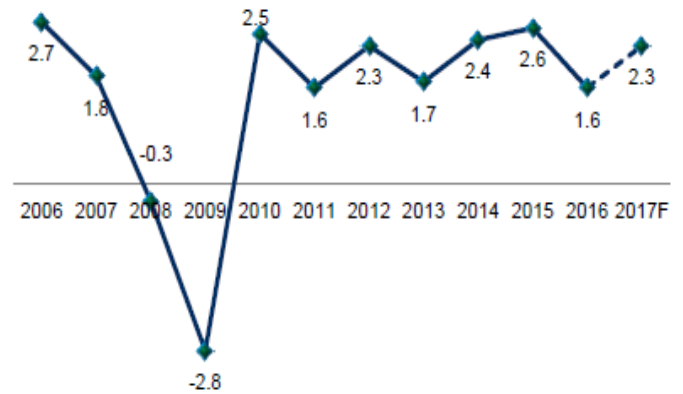
Source: Company data

Figure 8: US unemployment (%)



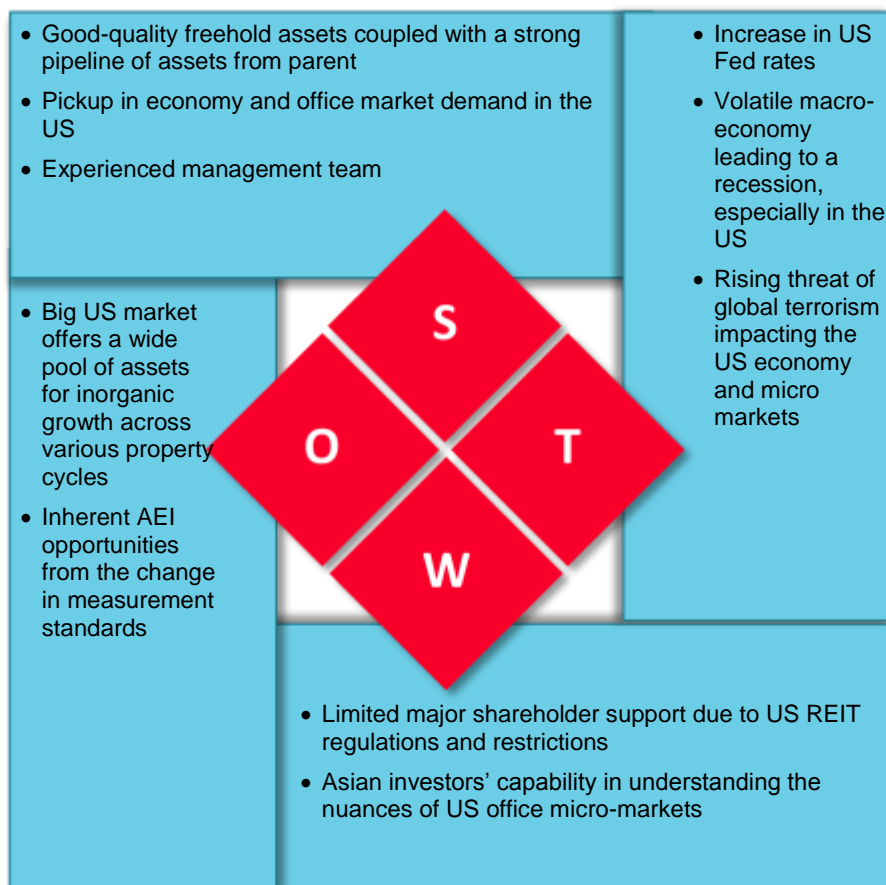
Source: Company data

Figure 9: US GDP growth



Source: Company data

SWOT Analysis



Recommendation Chart



Source: RHB, Bloomberg

Date	Recommendation	Target Price	Price
2017-01-05	Buy	0.96	0.84
2016-11-23	Buy	0.96	0.81

Source: RHB, Bloomberg

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Buy: Share price may exceed 10% over the next 12 months

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