

Singapore Company Update

Manulife US Real Estate Inv

Bloomberg: MUST SP | Reuters: MANU.SI

Refer to important disclosures at the end of this report

DBS Group Research . Equity

10 Feb 2023

BUY

Last Traded Price (9 Feb 2023): US\$0.300 (STI : 3,359.48)

Price Target 12-mth: US\$0.45 (50% upside) (Prev US\$0.48)

Analysts

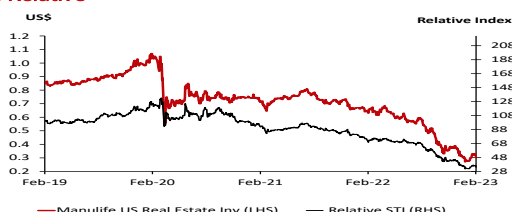
Rachel TAN +65 6682 3713 racheltanlr@dbs.com

Derek TAN +65 6682 3716 derektan@dbs.com

What's New

- FY22 DPU fell 11% y-o-y to 4.75 UScts, mainly due to lower payout. DPU (without retention) of 4.97 UScts is in line
- Key positives: i) In discussion with sponsor on potential asset disposition, ii) lower payout to conserve cash in the near term, iii) strategic review is ongoing and may likely see more developments in 2Q23
- Data to watch: i) Potential backfilling of vacancy, ii) higher interest costs, iii) physical occupancy which was at c.30%
- Maintain BUY; lower TP to US\$0.45 on lower dividend payout

Price Relative



Forecasts and Valuation

FY Dec (US\$m)	2021A	2022A	2023F	2024F
Gross Revenue	185	203	204	205
Net Property Inc	110	113	128	129
Total Return	39.4	(130)	72.4	72.8
Distribution Inc	85.6	87.9	81.2	81.8
EPU (US cts.)	2.23	(7.3)	4.05	4.04
EPU Gth (%)	nm	nm	nm	0
DPU (US cts.)	5.33	4.75	4.13	4.13
DPU Gth (%)	(5)	(11)	(13)	0
NAV per shr (US cts.)	67.3	57.4	57.5	57.4
PE (X)	13.4	nm	7.4	7.4
Distribution Yield (%)	17.8	15.8	13.8	13.8
P/NAV (x)	0.4	0.5	0.5	0.5
Aggregate Leverage (%)	42.7	48.6	48.8	49.1
ROAE (%)	3.4	(11.7)	7.1	7.1

Distn. Inc Chng (%): (2) (2)
 Consensus DPU (US): 4.60 4.60
 Other Broker Recs: B: 7 S: 0 H: 0

Source of all data on this page: Company, DBS Bank, Bloomberg Finance L.P.

Don't make me wait for love

Investment Thesis:

Rides on "flight to quality" trends in US office market. Manulife US REIT's (MUST) portfolio comprises trophy/class A office buildings located in key cities in the US that ride on the "flight to quality" trends as US corporates rationalise their office space.

Sponsor's support to acquire MUST's asset(s) will be a win-win approach for both and best-case scenario for MUST. MUST's portfolio valuation decline has caused gearing to spike up, resulting in a limited buffer for MUST. We believe the sponsor's support to acquire MUST's asset(s) will be a win-win approach for both and a best-case scenario for MUST.

Headwinds largely priced in and resolution on MUST's gearing position will lift share price overhang. We believe that markets have priced in a "rights issue" at current price. Given our worst case (potential rights issue), MUST's current share price could still offer an c.8% yield, above its historical mean. We believe that the headwinds are largely priced in and the share price is close to the bottom. Any potential resolution on MUST's current situation will lift the overhang on the share price towards our TP. Our total upside (including dividend) of 64% mainly considers 14% from dividends, 1.8% from terminal growth, and a valuation rerating of 48% in anticipation of the potential upliftment of the current overhang.

Maintain BUY; lower TP to US\$0.45. We maintain our BUY rating but trim our TP to US\$0.45 from US\$0.48. We lower our FY23F-FY24F DPU by c.11% on a lowered payout of 91%. Our DCF-based TP is based on a beta of 0.95x and risk-free rate of 4.2%.

Key Risks

Slower-than-expected economic recovery and potential recession in the US. This situation would impact businesses, and that may cause a rising risk of vacancy.

Non-renewal of leases. MUST's financials, operations, and capital growth may be adversely affected by bankruptcy, insolvency, or downturns in the businesses of its tenants, which may lead to the non-renewal of their leases.

At A Glance

Issued Capital (m shrs)	1,777
Mkt. Cap (US\$m/US\$m)	533 / 533
Major Shareholders (%)	
Manulife Financial Corp	5.5
Free Float (%)	94.5
3m Avg. Daily Val (US\$m)	1.3
GIC Industry : Real Estate / Equity Real Estate Investment (REITs)	

WHAT'S NEW

Don't make me wait for love

FY22/2H22 results were largely in line with expectations; lower dividend payout to 91% to conserve cash.

- FY22 DPU fell 11% y-o-y to 4.75 UScts, mainly due to a dividend payout cut to 91% from 100% in 2H22. DPU (without retention) -7% y-o-y to 4.97 UScts, in line with our forecasts.
- 2H22 DPU fell 19% to 2.14 UScts, mainly due to dividend retention. Excluding retention, DPU fell 10% y-o-y, mainly due to higher interest cost.
- On an h-o-h basis, 2H22 revenue and NPI +1.7% and -3.6%, respectively, to US\$102m and US\$56m.
- Gearing increased to 48.8% vs. 42.5% in 3Q22, as previously guided in Dec 22, mainly due to the c.11% decline in portfolio valuation.
- Average cost of debt increased by 40bps q-o-q to 3.74% from 3.34% and ICR ratio declined to 3.1x, as previously guided. This has yet to take into account the refinancing of S\$105m. We estimate the average cost of debt may rise another c.50bps taking into account a full-year impact of the refinancing.
- Hedging ratio reduced to 77% from 81% in 3Q22.
- Aside from the US\$105m refinancing, for which a loan facility has been obtained for Jun 23, there are no major refinancing needs in 2023.

Key Highlights/Observations

Portfolio occupancy held stable q-o-q despite large decline at Figueroa, as expected; management currently in discussion with sponsor on potential asset disposition – a positive, in our view; strategic review is ongoing, hopefully with more development in 2Q23.

- **Portfolio occupancy held relatively stable q-o-q at 88%, despite a large decline in occupancy at Figueroa (as expected).** In this quarter, Figueroa recorded the largest occupancy decline (-11ppt q-o-q) to 76.3%, mainly due to the downsizing of Quinn Emanuel, which has been previously guided, and some smaller tenants that vacated. Including TCW Group, which vacated in Dec 2023 occupancy at Figueroa might drop to 51%. However, management is working hard to backfill the space throughout the year. Other large occupancy declines include Peachtree (-4ppt), Plaza (-6ppt), and Centrepont (-4ppt). Diablo recorded an uptick in occupancy of 5ppt to 91%.
- **No immediate risks from top 10 tenants so far and no change in sublease space within the portfolio.**
- **FY22 recorded reversion of +0.7% and continues to expect positive low to mid-single-digit reversions in FY23.** Management recorded +0.7% reversions in FY22 vs. +1.7% in 9M22. In 4Q22, leasing activities doubled q-o-q to 123k sqft

of leases completed, with WALE of 8.2 years, and c.68% were new leases, a positive sign. Hopefully, the trend continues.

- Peachtree hotelisation and Plaza's Flex by JLL are on track.
- **Physical occupancy remained at c.30%**, mainly held down by New Jersey, Washington, and Los Angeles assets. The Atlanta market continues to show strong return-to-office, with high physical occupancy.
- **Portfolio valuation declined by 11% y-o-y, as previously guided, on the back of average cap rate expansion of 34bps.** Five assets accounted for 80% of the portfolio decline with Figueroa contributing c.50%. Excluding the five assets, portfolio valuation declined by c.7%, in line with the US office market. Overall, we saw cap rates expand by 25bps to 150bps, except for selected assets, which saw cap rates compress by 25bps to 50bps, in the Phoenix and Atlanta markets.
- **Management currently in discussion with sponsor for potential disposition – a positive development since Dec 22, in our view.** MUST remains focused on rebalancing its balance sheet and capital management. Management reiterated that asset disposition was preferred over EFR. Management is currently in talks with the sponsor on potential disposition and will likely announce when the plans are confirmed – a positive development since the last update in Dec 22. Management also highlighted that any divestment to the sponsor has to be made at a minimum of book value and that it might consider a partial stake instead of a full asset divestment to quicken the process.
- **Strategic review is still ongoing and would likely have more developments in 2Q23.** Based on the timeline, Citigroup is expected to conclude its first cut of the review in Mar 23 and have further discussions with MUST subsequently in 2Q23.

Maintain BUY rating; lower TP to US\$0.45. We maintain our BUY rating but lower our TP to US\$0.45 from US\$0.48. We trimmed our FY23F-FY24F DPU by c.11% on lower dividend payout of 91% vs. 100% previously. Despite the negative news that has caused a further decline in MUST's share price, we believe the share price has largely priced in all the negatives. Given our worst-case scenario (potential rights issue), MUST's current share price could still offer an c.8% yield, which implies that the share price is close to the bottom.

In addition, three out of the four options (except EFR option) for MUST would possibly cause an uplift to the share price that has been weighed down by high gearing and the low ICR ratio. As such, we believe the share price is closer to the bottom and we continue to watch out for positive developments from MUST in addressing its balance sheet issues, and we believe this will be key rerating catalyst for the stock.

Manulife US Real Estate Inv

Company Background

Manulife US REIT (MUST) is the first pure-play US office REIT listed in Asia. Its portfolio consists of eight freehold, class A, or trophy-quality office properties in Atlanta, Los Angeles, New Jersey, Washington DC, Virginia, and Orange County.

Summary of results

Summary of Results	2H2022	2H2021	% y-o-y	1H2022	% h-o-h	FY2022	FY2021	% y-o-y
Revenue	102.1	94.3	8.3%	100.4	1.7%	202.6	185.1	9.4%
NPI	55.5	53.5	3.9%	57.6	-3.6%	113.2	109.5	3.3%
DI	41.9	42.6	-1.7%	46.0	-8.8%	87.9	85.6	2.7%
DPU (before retention)	2.36	2.63	-10.3%	2.61	-9.6%	4.97	5.33	-6.8%
DPU (91% payout in 2H22)	2.14	2.63	-18.6%	2.61	-18.0%	4.75	5.33	-10.9%

Key Operational Highlights	4Q2022	4Q2021	% y-o-y	3Q2022	% q-o-q
Portfolio occupancies	88.0%	92.3%	-4.3 ppt	88.1%	-0.1 ppt
Rental reversions (cumulative)	0.7%	-0.8%	1.5 ppt	1.7%	-1 ppt
WALE (years)	4.7	5.1	(0.4)	4.9	(0.2)
Gearing	48.8%	42.8%	6 ppt	42.5%	6.3 ppt
Average cost of debt*	3.74%	2.82%	0.9 ppt	3.34%	0.4 ppt
DSCR	3.10	3.40	(0.3)	3.40	(0.3)
Hedging ratio	77%	87%	-9.2 ppt	81%	-3.8 ppt
Leases expiring in FY2023	10.8%	13.1%	-2.3 ppt	10.1%	0.7 ppt
Leases expiring in FY2024	10.8%	10.8%	0 ppt	11.9%	-1.1 ppt

Source: Company, DBS

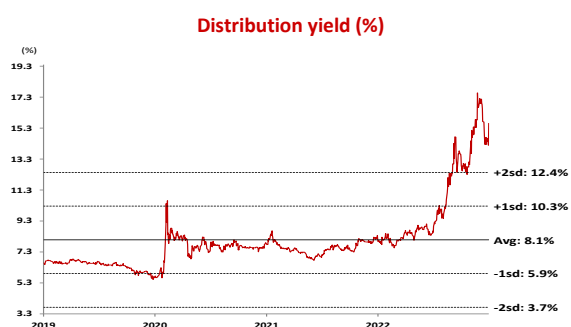
Interim Income Statement (US\$m)

FY Dec	2H2021	1H2022	2H2022	% chg yoy	% chg hoh
Gross revenue	94.3	100	102	8.3	1.7
Property expenses	(40.8)	(42.8)	(46.6)	14.2	8.9
Net Property Income	53.5	57.6	55.5	3.9	(3.6)
Other Operating expenses	(5.6)	(6.2)	(5.3)	(5.7)	(15.0)
Other Non Opg (Exp)/Inc	9.69	32.8	15.2	57.0	(53.6)
Associates & JV Inc	0.0	0.0	0.0	-	-
Net Interest (Exp)/Inc	(14.5)	(15.3)	(18.6)	(28.5)	(21.6)
Exceptional Gain/(Loss)	0.0	0.0	0.0	-	-
Net Income	43.1	68.9	46.9	8.8	(32.0)
Tax	(5.3)	(7.7)	25.8	nm	nm
Minority Interest	0.0	0.0	0.0	-	-
Net Income after Tax	37.8	61.2	72.7	92.2	18.8
Total Return	32.7	62.8	(192)	nm	(406.7)
Non-tax deductible Items	9.90	(15.2)	(30.8)	nm	102.3
Net Inc available for Dist.	42.6	46.0	41.9	(1.7)	(8.9)
Ratio (%)					
Net Prop Inc Margin	56.7	57.4	54.4		
Dist. Payout Ratio	100.0	100.0	91.0		

Source of all data: Company, DBS Bank

Manulife US Real Estate Inv

Historical PE and PB band



Source: Bloomberg Finance L.P., DBS Bank estimates



Source: Bloomberg Finance L.P., DBS Bank estimates

Income Statement (US\$m)

FY Dec	2020A	2021A	2022A	2023F	2024F
Gross revenue	194	185	203	204	205
Property expenses	(78.5)	(75.6)	(89.4)	(75.9)	(75.5)
Net Property Income	116	110	113	128	129
Other Operating expenses	(11.8)	(11.3)	(11.5)	(10.7)	(10.8)
Other Non Opg (Exp)/Inc	0.0	0.0	48.0	0.0	0.0
Associates & JV Inc	0.0	0.0	0.0	0.0	0.0
Net Interest (Exp)/Inc	(29.6)	(29.1)	(33.9)	(44.4)	(45.1)
Exceptional Gain/(Loss)	(140)	(28.5)	(264)	0.0	0.0
Net Income	(66.0)	40.6	(148)	73.1	73.5
Tax	22.7	(1.1)	18.1	(0.7)	(0.7)
Minority Interest	0.0	0.0	0.0	0.0	0.0
Preference Dividend	0.0	0.0	0.0	0.0	0.0
Net Income After Tax	(43.3)	39.4	(130)	72.4	72.8
Total Return	(43.3)	39.4	(130)	72.4	72.8
Non-tax deductible Items	132	46.2	218	8.79	9.04
Net Inc available for Dist.	89.0	85.6	87.9	81.2	81.8
Growth & Ratio					
Revenue Gth (%)	9.3	(4.7)	9.4	0.8	0.4
N Property Inc Gth (%)	4.6	(5.4)	3.3	13.3	0.9
Net Inc Gth (%)	nm	nm	nm	nm	0.5
Dist. Payout Ratio (%)	100.0	100.0	95.7	91.0	91.0
Net Prop Inc Margins (%)	59.6	59.2	55.9	62.8	63.1
Net Income Margins (%)	(22.3)	21.3	(64.0)	35.5	35.5
Dist to revenue (%)	45.8	46.2	43.4	39.8	39.9
Managers & Trustee's fees	6.1	6.1	5.7	5.3	5.3
ROAE (%)	(3.6)	3.4	(11.7)	7.1	7.1
ROA (%)	(2.0)	1.8	(5.9)	3.4	3.4
ROCE (%)	5.3	4.8	5.1	6.0	6.0
Int. Cover (x)	3.5	3.4	3.0	2.6	2.6

Source: Company, DBS Bank

Manulife US Real Estate Inv

Interim Income Statement (US\$m)

FY Dec	2H2020	1H2021	2H2021	1H2022	2H2022
Gross revenue	95.7	90.8	94.3	100	102
Property expenses	(42.0)	(34.7)	(40.8)	(42.8)	(46.6)
Net Property Income	53.7	56.1	53.5	57.6	55.5
Other Operating	(5.2)	(5.7)	(5.6)	(6.2)	(5.3)
Other Non Opg (Exp)/Inc	2.20	4.21	9.69	32.8	15.2
Associates & JV Inc	0.0	0.0	0.0	0.0	0.0
Net Interest (Exp)/Inc	(14.9)	(14.7)	(14.5)	(15.3)	(18.6)
Exceptional Gain/(Loss)	0.0	0.0	0.0	0.0	0.0
Net Income	35.8	39.9	43.1	68.9	46.9
Tax	7.74	4.13	(5.3)	(7.7)	25.8
Minority Interest	0.0	0.0	0.0	0.0	0.0
Net Income after Tax	43.5	44.0	37.8	61.2	72.7
Total Return	(7.7)	6.70	32.7	62.8	(192)
Non-tax deductible Items	(2.5)	(1.0)	9.90	(15.2)	(30.8)
Net Inc available for Dist.	41.0	43.0	42.6	46.0	41.9
Growth & Ratio					
Revenue Gth (%)	(3)	(5)	4	6	2
N Property Inc Gth (%)	(14)	4	(5)	8	(4)
Net Inc Gth (%)	4	1	(14)	62	19
Net Prop Inc Margin (%)	56.1	61.8	56.7	57.4	54.4
Dist. Payout Ratio (%)	100.0	100.0	100.0	100.0	91.0

Balance Sheet (US\$m)

FY Dec	2020A	2021A	2022A	2023F	2024F
Investment Properties	1,993	2,184	1,947	1,966	1,987
Other LT Assets	0.0	5.65	47.7	47.7	47.7
Cash & ST Invts	86.7	78.6	113	114	119
Inventory	0.0	0.0	0.0	0.0	0.0
Debtors	6.93	5.55	5.40	8.74	8.77
Other Current Assets	1.66	1.44	2.93	2.93	2.93
Total Assets	2,088	2,276	2,116	2,140	2,165
ST Debt	234	297	145	145	145
Creditor	18.1	58.8	31.3	30.8	31.0
Other Current Liab	6.88	8.25	8.50	8.50	8.50
LT Debt	619	675	884	901	919
Other LT Liabilities	52.9	49.6	26.8	26.8	26.8
Unit holders' funds	1,158	1,188	1,020	1,028	1,035
Minority Interests	0.0	0.0	0.0	0.0	0.0
Total Funds & Liabilities	2,088	2,276	2,116	2,140	2,165
Non-Cash Wkg. Capital	(16.4)	(60.0)	(31.4)	(27.7)	(27.7)
Net Cash/(Debt)	(766)	(893)	(916)	(932)	(945)
Ratio					
Current Ratio (x)	0.4	0.2	0.7	0.7	0.7
Quick Ratio (x)	0.4	0.2	0.7	0.7	0.7
Aggregate Leverage (%)	40.8	42.7	48.6	48.8	49.1
Z-Score (X)	1.0	1.0	1.0	1.0	1.0

Source: Company, DBS Bank

Manulife US Real Estate Inv

Cash Flow Statement (US\$m)

FY Dec	2020A	2021A	2022A	2023F	2024F
Pre-Tax Income	74.4	40.6	(148)	73.1	73.5
Dep. & Amort.	(0.7)	1.93	4.35	0.0	0.0
Tax Paid	(1.9)	(0.1)	(0.1)	(0.7)	(0.7)
Associates & JV Inc/(Loss)	0.0	0.0	0.0	0.0	0.0
Chg in Wkg.Cap.	(36.6)	(20.8)	1.25	(3.8)	0.09
Other Operating CF	187	69.1	234	8.79	9.04
Net Operating CF	222	90.6	92.0	77.4	81.9
Net Invt in Properties	(24.2)	(231)	(25.4)	(2.0)	(3.1)
Other Invt (net)	0.0	0.0	0.0	0.0	0.0
Invt in Assoc. & JV	0.0	0.0	0.0	0.0	0.0
Div from Assoc. & JVs	0.0	0.0	0.0	0.0	0.0
Other Investing CF	0.17	0.02	0.05	(17.1)	(17.4)
Net Investing CF	(24.0)	(231)	(25.4)	(19.2)	(20.5)
Distribution Paid	(70.7)	(84.0)	(88.6)	(73.9)	(74.5)
Chg in Gross Debt	38.6	215	56.0	17.1	17.4
New units issued	0.0	0.70	0.25	0.0	0.0
Other Financing CF	0.0	0.0	0.0	0.0	0.0
Net Financing CF	(32.2)	132	(32.4)	(56.8)	(57.1)
Currency Adjustments	0.05	0.0	0.03	0.0	0.0
Chg in Cash	166	(8.1)	34.3	1.50	4.38
Operating CFPS (US cts.)	16.4	6.32	5.11	4.54	4.54
Free CFPS (US cts.)	12.5	(8.0)	3.75	4.22	4.38

Source: Company, DBS Bank

Target Price & Ratings 12-mth History



Note: Share price and Target price are adjusted for corporate actions.

S.No.	Date of Report	Closing Price	12-mth Target Price	Rating
1:	26 May 22	0.59	0.70	BUY
2:	03 Nov 22	0.36	0.48	BUY
3:	08 Feb 23	0.33	0.48	BUY

Source: DBS Bank

Analyst: Rachel TAN

Derek TAN

DBS Bank recommendations are based on an Absolute Total Return* Rating system, defined as follows:

STRONG BUY (>20% total return over the next 3 months, with identifiable share price catalysts within this time frame)

BUY (>15% total return over the next 12 months for small caps, >10% for large caps)

HOLD (-10% to +15% total return over the next 12 months for small caps, -10% to +10% for large caps)

FULLY VALUED (negative total return, i.e., > -10% over the next 12 months)

SELL (negative total return of > -20% over the next 3 months, with identifiable share price catalysts within this time frame)

*Share price appreciation + dividends

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Sources for all charts and tables are DBS Bank unless otherwise specified.

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DBS Regional Research Offices

HONG KONG

DBS (Hong Kong) Ltd

Contact: Dennis Lam
13th Floor One Island East,
18 Westlands Road,
Quarry Bay, Hong Kong
Tel: 852 3668 4181
Fax: 852 2521 1812
e-mail: dbsvhk@dbs.com

SINGAPORE

DBS Bank Ltd

Contact: Paul Yong
12 Marina Boulevard,
Marina Bay Financial Centre Tower 3
Singapore 018982
Tel: 65 6878 8888
e-mail: groupresearch@dbs.com
Company Regn. No. 196800306E

INDONESIA

PT DBS Vickers Sekuritas (Indonesia)

Contact: Maynard Priajaya Arif
DBS Bank Tower
Ciputra World 1, 32/F
Jl. Prof. Dr. Satrio Kav. 3-5
Jakarta 12940, Indonesia
Tel: 62 21 3003 4900
Fax: 6221 3003 4943
e-mail: indonesiaresearch@dbs.com

THAILAND

DBS Vickers Securities (Thailand) Co Ltd

Contact: Chanpen Sirithanarattanakul
989 Siam Piwat Tower Building,
9th, 14th-15th Floor
Rama 1 Road, Pathumwan,
Bangkok Thailand 10330
Tel. 66 2 857 7831
Fax: 66 2 658 1269
e-mail: research@th.dbs.com
Company Regn. No 0105539127012
Securities and Exchange Commission, Thailand