

COMPANY RESULTS

Manulife US REIT (MUST SP)

1H23: Unit Price Near Capitulation; Upgrade to BUY

1H23 distributable income of US\$37.9m was in line with our expectations but distribution was halted as MUST breached financial covenant. The strategic review is still ongoing. MUST is continuing to scout for equity infusion from strategic investors and work on divestment of Phipps Tower at Atlanta, Georgia to sponsor Manulife Insurance. The path forward is uncertain but unit price appears to be near capitulation with 2024 distribution yield at 17.1% and P/NAV at 0.45x. Upgrade to BUY. Target price: US\$0.22.

1H23 RESULTS

Year to 31 Dec (US\$m)	1H23	yoy % Chg	Remarks
Gross Revenue	99.6	-0.8	Lower occupancies and the sale of Tanasbourne.
Net Property Income (NPI)	55.4	-3.9	Higher repair & maintenance, property taxes and utilities.
Distributable Income	37.9	-17.4	Interest expense increased 45% yoy.
DPU (US cents)	0.0	n.m.	Halted distribution for 1H23.

Source: MUST, UOB Kay Hian

RESULTS

- Manulife US REIT (MUST) reported distributable income of US\$37.9m (-17.4% yoy), which is in line with our expectations but investors would be disappointed that it has halted distribution for 1H23.
- NPI margin narrowed 1.8ppt yoy to 55.6%. Gross revenue and NPI dipped 0.8% yoy and 3.9% yoy respectively in 1H23 due to lower occupancies across the portfolio and the sale of Tanasbourne at Hillsboro, Oregon in Apr 23. Property operating expenses increased 3.3% yoy due to higher repair & maintenance, property taxes and utilities. Interest expense increased 45% yoy due to rising interest rates.
- Smaller non-renewals in 2Q23. Portfolio occupancy eased slightly by 1ppt qoq to 85.1% as of Jun 23 due to non-renewals at Diablo at Tempe, Arizona and Capitol at Sacramento, California. It achieved positive rent reversions of +3.7% (1Q23: +5.0%, 2Q23: -2.5%) and long WALE of 7.6 years for 443,000sf of leases executed in 1H23.
- Negative impact from mid-year review. Aggregate leverage has surged 7.2ppt qoq to 56.7%. Weighted average interest rate increased slightly by 12bp qoq to 4.10% as of Jun 23. NAV per unit was US\$0.40 after accounting for revaluation losses of US\$280m or 14.6%. Direct cap rates have expanded 0.73ppt to 7.06% for the mid-year review.

KEY FINANCIALS

Year to 31 Dec (US\$m)	2021	2022	2023F	2024F	2025F
Net turnover	185	203	193	167	167
EBITDA	98	102	95	83	83
Operating profit	98	102	95	83	83
Net profit (rep./act.)	39	(130)	(364)	77	83
Net profit (adj.)	68	86	55	51	54
EPU (US\$ cent)	4.2	4.9	3.0	1.4^	1.0^
DPU (US\$ cent)	5.3	4.8	0.0	1.3^	1.4^
PE (x)	2.1	1.8	3.0	5.3*	4.9*
P/B (x)	0.1	0.2	0.3	0.5*	0.5*
DPU Yld (%)	59.9	53.4	0.0	17.1*	17.9*
Net margin (%)	21.3	(64.0)	(189.1)	46.1	49.5
Net debt/(cash) to equity (%)	75.2	89.8	106.1	57.1	60.9
Interest cover (x)	3.4	3.0	2.6	3.0	3.3
ROE (%)	3.4	n.a.	n.a.	9.9	9.2
Consensus DPU (US\$ cent)	n.a.	n.a.	3.8	2.4	3.2
UOBKH/Consensus (x)	-	-	0.00	0.55	0.43

^ Fully diluted for 1,732,1,000 rights issue @ US\$0.07.  
 \* Based on theoretical ex-rights unit price of US\$0.077.  
 Source: Manulife US REIT, Bloomberg, UOB Kay Hian

BUY

(Upgraded)

Share Price	US\$0.089
Target Price	US\$0.22
Upside	+147.2%
(Previous TP)	US\$0.165)

COMPANY DESCRIPTION

MUST is the first pure play US office REIT listed in Asia. It invests in a portfolio of income-producing office real estate in key markets in the US. Its portfolio comprises 12 freehold office properties in Arizona, California, Georgia, New Jersey, Oregon, Virginia and Washington DC with NLA of 5.5m sf and valued at US\$1.9b as of Dec 22.

STOCK DATA

GICS sector	Real Estate
Bloomberg ticker:	MUST SP
Shares issued (m):	1,776.6
Market cap (US\$m):	158.1
Market cap (US\$m):	158.1
3-mth avg daily t'over (US\$m):	1.2

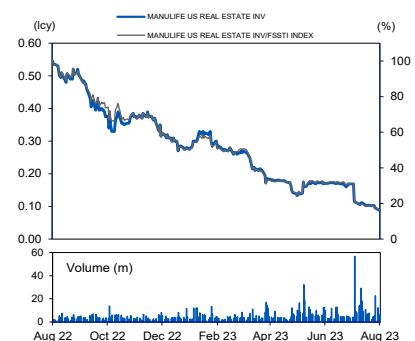
Price Performance (%)

52-week high/low	US\$0.545/US\$0.089			
1mth (47.3)	3mth (36.0)	1mth (70.3)	3mth (83.5)	1mth (70.3)

Major Shareholders

Manulife Financial Corp	9.1
FY23 NAV/Share (US\$)	0.35
FY23 Net Debt/Share (US\$)	0.37

PRICE CHART



Source: Bloomberg

ANALYST(S)

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STOCK IMPACT

- Leasing momentum continues to moderate.** According to CBRE, leasing volume for the US office market has slowed for the third consecutive quarter and declined 33% yoy and 3% qoq to 36.5m sf in 2Q23. Vacancy rate has increased 0.4ppt qoq to 18.2%, the highest in 30 years, due to the completion of 8.3m sf of new office space. Net absorption was negative at 8.5m sf in 2Q23, caused by companies' efforts in cost containment in light of popularity of hybrid work arrangements.
- Competition from shadow space.** More tenants are sub-leasing their underutilised office space. According to CBRE, sub-lease availability has increased 4.5m sf to a record high of 194m sf in 2Q23. Sub-lease space accounted for 19% of total available space. Tenants' negotiating power has strengthened.
- Seeking waiver from lenders.** All of MUST's loans are reclassified as current liabilities due to the breach of financial covenant. It has to generate proceeds to repay upcoming loan maturities and fund capex. Thus, distribution for 1H23 is halted. MUST has lowered its total unencumbered debt to total unencumbered assets ratio to 59.7% through a good faith payment in Aug 23 (Jun 23: 60.2%), bringing the ratio below 60%. It is still negotiating with its lenders to address the breach.
- Strategic review still ongoing.** MUST will evaluate all options, including divestments, capital injection and strategic transactions. It continues to scout for equity infusion from strategic investors. MUST and sponsor Manulife Insurance have entered into a letter of intent for the sale of Phipps Tower at Atlanta, Georgia. According to management, sponsor Manulife Insurance has completed its due diligence. The transaction has to be approved by unitholders during an EGM assuming the two parties proceed to sign a sale and purchase agreement.

EARNINGS REVISION/RISK

- We have further cut our fully diluted 2024 DPU by 15% to 1.3 US cents assuming:
  - Erosion in capital values.** We estimated fair value of MUST's investment properties to drop 22% or US\$419m (1H23: US\$280m, 2H23: US\$139m), to US\$1,342m as at end-23 assuming direct cap rate for its portfolio expands 100bp to 7.0%. Thus, we expect aggregate leverage to increase and hit 52% at end-23.
  - Deleveraging through divestment.** We assumed MUST's divestment of Phipps Tower at Atlanta to sponsor Manulife Insurance at a valuation of US\$178m obtained during the mid-year review.
  - Factoring in equity fund raising.** We hypothetically assumed MUST embarks on 1,732:1,000 rights issue with issue price at US\$0.07 to raise US\$230m and reduce aggregate leverage to 38.0% at end-24.
  - Halted distribution in 2023.** We assumed that MUST retain distributable income of US\$50.3m in 2023. The amount retained is subject to tax at 31% (US: 21%, Singapore: 10%). We assumed MUST will resume its usual distribution in 2024.
- Rights issue does not dilute minorities.** There is execution risk associated with launching a rights issue. Nevertheless, a rights issue has the virtue of not diluting minority unitholders' interest.

VALUATION/RECOMMENDATION

- Upgrade to BUY.** Our target price of US\$0.22 is based on DDM (cost of equity: 10.0%, terminal growth: 0.0%) fully diluted for 1,732:1,000 rights issue at issue price of US\$0.07 per unit but adjusted for rights entitlements.

SHARE PRICE CATALYST

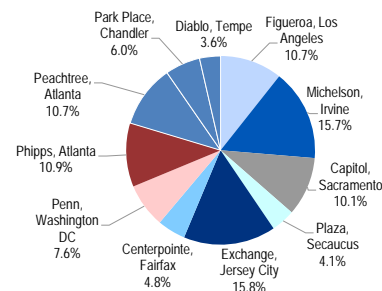
- Deleveraging to address the drop in portfolio valuation and higher aggregate leverage.
- Ongoing pressure on portfolio occupancy due to low physical occupancy.

KEY OPERATING METRICS

Key Metrics	2Q22	3Q22	4Q22	1Q23	2Q23	yoy % chg	qoq % chg*
DPU (US cents)	2.61	n.a.	2.14	n.a.	0.00	-100.0%	-100.0%
Occupancy	90.0%	88.1%	88.0%	86.1%	85.1%	-4.9ppt	-1ppt
Aggregate Leverage	42.4%	42.5%	48.8%	49.5%	56.7%	14.3ppt	7.2ppt
Average Cost of Debt	2.97%	3.34%	3.74%	3.98%	4.10%	1.2ppt	0.2ppt
% Borrowing in Fixed Rates	85.7%	81.1%	77.3%	80.2%	80.2%	-5.5ppt	0ppt
WALE by NLA (years)	5.0	4.9	4.7	5.0	7.6	2.6yrs	2.6yrs
Weighted Average Debt Maturity (years)	2.3	3.1	2.4	2.7	2.5	0.2yrs	-0.2yrs
Rental Reversions	1.0%	4.3%	0.7%	5.0%	-2.5%	-3.5ppt	-7.5ppt

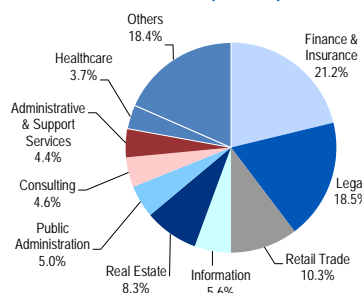
Source: MUST \* hoh % change for DPU

PORTFOLIO VALUATION BY PROPERTY (JUN 23)



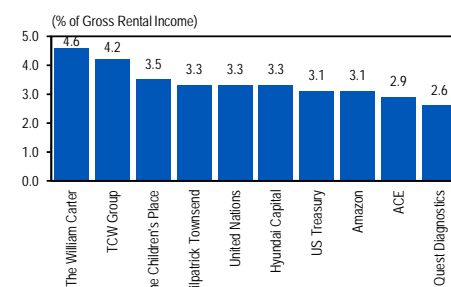
Source: MUST

TRADE SECTOR BY GRI (JUN 23)



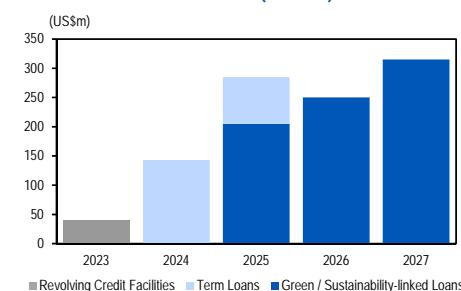
Source: MUST

TOP 10 TENANTS (JUN 23)



Source: MUST

DEBT MATURITY PROFILE (JUN 23)



Source: MUST

### PROFIT & LOSS

Year to 31 Dec (US\$m)	2022	2023F	2024F	2025F
Net turnover	202.6	192.6	166.6	167.4
EBITDA	101.7	95.2	83.0	83.4
Deprec. & amort.	0.0	0.0	0.0	0.0
EBIT	101.7	95.2	83.0	83.4
Net interest income/(expense)	(33.9)	(36.8)	(28.0)	(25.0)
Pre-tax profit	(147.8)	(360.6)	80.6	87.1
Tax	18.1	(3.5)	(3.8)	(4.3)
Net profit	(129.7)	(364.1)	76.7	82.8
Net profit (adj.)	85.9	54.8	51.2	54.1

### CASH FLOW

Year to 31 Dec (US\$m)	2022	2023F	2024F	2025F
Operating	92.0	66.7	50.2	58.6
Pre-tax profit	(147.8)	(360.6)	80.6	87.1
Tax	(0.1)	0.0	0.0	0.0
Working capital changes	1.2	(2.6)	(4.8)	0.2
Non-cash items	229.6	425.4	(19.5)	(22.2)
Other operating cashflows	9.0	4.5	(6.1)	(6.4)
Investing	(25.4)	153.0	(25.0)	(25.0)
Capex (growth)	0.0	0.0	0.0	0.0
Capex (maintenance)	(25.4)	(25.0)	(25.0)	(25.0)
Proceeds from sale of assets	0.0	178.0	0.0	0.0
Financing	(32.4)	(269.4)	(24.4)	(33.3)
Distribution to unitholders	(58.0)	(0.0)	(69.4)	(73.3)
Issue of shares	0.0	0.0	230.0	0.0
Proceeds from borrowings	16.8	(269.4)	(185.0)	40.0
Others/interest paid	8.8	0.0	0.0	0.0
Net cash inflow (outflow)	34.2	(49.7)	0.9	0.3
Beginning cash & cash equivalent	78.6	112.9	63.1	64.0
Changes due to forex impact	0.0	0.0	0.0	0.0
Ending cash & cash equivalent	112.8	63.1	64.0	64.3

### BALANCE SHEET

Year to 31 Dec (US\$m)	2022	2023F	2024F	2025F
Fixed assets	1,947.0	1,341.5	1,392.1	1,445.8
Other LT assets	47.7	47.7	47.7	47.7
Cash/ST investment	112.9	63.1	64.0	64.3
Other current assets	8.3	8.3	7.6	7.7
Total assets	2,115.9	1,460.6	1,511.4	1,565.4
ST debt	144.6	144.6	144.6	144.6
Other current liabilities	39.8	37.3	32.4	32.5
LT debt	884.4	615.0	430.0	470.0
Other LT liabilities	26.8	7.5	10.9	15.2
Shareholders' equity	1,020.3	656.2	893.5	903.0
Total liabilities & equity	2,115.9	1,460.6	1,511.4	1,565.4

### KEY METRICS

Year to 31 Dec (%)	2022	2023F	2024F	2025F
Profitability				
EBITDA margin	50.2	49.4	49.8	49.8
Pre-tax margin	(73.0)	(187.2)	48.4	52.0
Net margin	(64.0)	(189.1)	46.1	49.5
ROA	n.a.	n.a.	5.2	5.4
ROE	n.a.	n.a.	9.9	9.2
Growth				
Turnover	9.4	(4.9)	(13.5)	0.5
EBITDA	3.5	(6.4)	(12.8)	0.5
Pre-tax profit	(464.5)	n.a.	n.a.	8.1
Net profit	(429.1)	n.a.	n.a.	7.9
Net profit (adj.)	26.4	(36.2)	(6.7)	5.8
EPU	14.7	(39.0)	(51.9)	(28.7)
Leverage				
Debt to total capital	50.2	53.7	39.1	40.5
Debt to equity	100.8	115.8	64.3	68.1
Net debt/(cash) to equity	89.8	106.1	57.1	60.9
Interest cover (x)	3.0	2.6	3.0	3.3

<sup>^</sup> Fully diluted for 1,732:1,000 rights issue @ US\$0.07.

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