Singapore

Flash Note

Refer to important disclosures at the end of this report

Manulife US Real Estate Inv (MUST SP) : BUY

Mkt. Cap: US$1,098m I **3m Avg. Daily Val:** US$5.9m

Last Traded Price (24 Mar 2020)**:** US$0.70

Price Target 12-mth: US$1.15 (64% upside)

Analyst

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Company Guide

Summary of our point of view, and highlights the relevant data points, which are actively tracked

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Manulife US Real Estate Inv - Institution Login

Stronger than you think

- MUST's management believes its portfolio, comprising Class A/trophy assets, strong top 10 tenant profile and a good set of credit metrics, is stable and resilient to weather the short-term pain and potential recession
- While it is still early stages of the COVID-19 outbreak in the US, management expects leasing activities and the transaction market to slow down as tenants/buyers/sellers take a wait-and-see approach
- Management does not expect refinancing risks at the moment and credit metrics still provide some debt headroom
- While valuations look attractive at price levels between 55 US Scts and 61 US Scts, share price could remain volatile as it trades in tandem with the US market/and sentiment on its economy

Forecasts and Valuation

FY Dec (US$m)	2018A	2019A	2020F	2021F
Gross Revenue	145	178	203	233
Net Property Inc	90.7	111	130	151
Total Return	64.5	47.6	87.6	101
Distribution Inc	71.0	83.3	100.0	116
EPU (US cts.)	5.06	3.03	5.53	6.05
EPU Gth (%)	(10)	(40)	82	9
DPU (US cts.)	5.57	5.96	6.31	6.96
DPU Gth (%)	(5)	7	6	10
NAV per shr (US cts.)	83.4	80.2	79.4	83.1
PE (X)	13.8	23.1	12.7	11.6
Distribution Yield (%)	8.0	8.5	9.0	9.9
P/NAV (x)	0.8	0.9	0.9	0.8
Aggregate Leverage (%)	37.2	37.7	38.0	39.5
ROAE (%)	6.7	4.1	7.0	7.6

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

What's New

MUST organised an update call on the morning of 24 March 2020 to address the numerous questions on the impact from the current situation and to give further comfort on the resilience of its portfolio.

In summary, MUST's management believes that its portfolio remains resilient amid the current headwinds following the COVID-19 outbreak. As it is still early stages in the US (only one week of lockdown/movement restriction measures being implemented), management expects leasing activities to slow down as existing/prospective tenants take a wait-and-see approach. Management's base-case expectations are a sharp downturn in 1H2020 and potentially a sharp rebound when the COVID-19 situation stabilises in 2H2020. As such, management believes that its portfolio, comprising Class A/trophy assets, strong top 10 tenant profile and a good set of credit metrics, is stable and resilient to weather the short-term pain and potential recession.

After a 48% drop from its peak in Jan 2020 to its lowest level just yesterday, MUST's share price has rebounded by 11% today (as of time of writing). We update our ballpark stress-test scenarios based on the latest price of 61 US Scts in the table below:

Stress-test scenario analysis

Current price = 61 US Scts	Dividend yield FY2020F	Dividend yield FY2021F	P/NAV FY2019	Gearing FY2019	ICR FY2020F	DI / 1-yr debt expiry FY2020F
Current	10.2%	11.2%	0.76	37.7%	4.2	1.3
Assume 20% cut in NPI	7.7%	8.5%			3.4	0.9
Assume 30% cut in NPI	6.3%	7.0%			2.9	0.8
Assume 10% cut in NAV			0.85	41.9%		

Source: DBS Bank, Company, Thomson Reuters

Key highlights:

- **Possible reasons for the sharp drop in share price.** Management believes that the possible reasons for the sharp drop could be segregated into three groups as follows: i) following the index inclusion at end-2019, MUST's shareholder base has improved to include large funds such as pension funds. Sell-off positions from these funds possibly led to the sharp drop in prices, ii) margin calls from HNW investors especially HNW Chinese individuals. However, MUST's management reassured that there were minimal HNW Chinese individuals in its register, iii) fund redemption or repositioning.

- **Majority of MUST's shareholders are institutional investors.** MUST's shareholders comprise 60% institutions and 40% individuals.

- **Current occupancy is less than 20%; F&B retail outlets are closed.** Given that most corporates have implemented work-from-home arrangements, the current occupancy in the office buildings are below 20%, thus reducing risks of a potential COVID-19 case in the office buildings and also staffing needs. F&B retail outlets, which contribute only 1% of portfolio income, are now temporarily closed.
- **No rental rebates for office tenants, that for F&B tenants are on a case-by-case basis.** Rental rebates are not offered to office tenants, not even during the GFC. However, MUST is looking to provide some form of help for its F&B tenants (a very small portion of the portfolio) on a case-by-case basis. MUST highlighted that the pandemic does not qualify for business interruption insurance.

- **Security deposits of up to four months are in place.** The security deposits collected from MUST's tenants ranges from zero to four months, based on the credit profile and length of tenant relationship with MUST. Typically, landlords (MUST) will make a decision whether to classify a tenant as 'default' if rent payments are 60 days in arrears.

- **Majority of (seven out of nine) MUST's assets are Class A assets which are more resilient.** According to management, Class A assets are typically more attractive and resilient during a recession. In addition, Class A assets tend to benefit from a potential flight to quality if rental rates look attractive. The majority (seven out of nine) of MUST's assets are Class A assets while the remaining two are trophy assets.

- **During the GFC, occupancy dropped to between 80% and 90%; valuers may remain "sticky" due to lack of transactions.** As a point of reference, occupancies at Figueroa, LA and Peachtree, Atlanta fell to c.90% and c.80% during the GFC. Management expects valuers to remain "sticky" and be more reactionary given the expected lack of transactions as most buyers and sellers would take a wait-and-see approach.

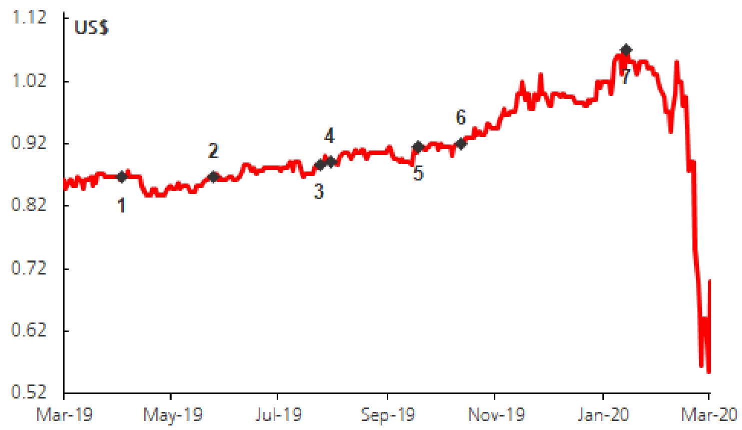
- **Risk of top 10 tenants right-sizing from more flexible working arrangement moving forward is low.** While there are comments that there could be a structural shift of tenants right-sizing their office space needs with a more flexible working arrangement moving forward, management believes that the structural change is minimal and their top 10 tenants have either right-sized recently or are unlikely to change as many of the corporates in the US would have existing flexible work arrangements.

- **Management does not expect refinancing risks but possibly some interest savings from lower interest rates; sufficient undrawn debt facilities.** As there is limited refinancing in FY2020, management does not expect any refinancing risks, but there could be some interest savings from lower interest rates. In addition, unencumbered debt will likely improve to 41% from 34% currently, post refinancing. Undrawn debt facilities stood at US$290m comprising US$90m of RCF and US$200m of lines for acquisition. ICR as at Dec 2019 stood at 3.8x vs debt covenant of 2x. Based on management's stress testing of its cashflow needs, EBITDA needs to fall by >50% (c.US$60m) before the ICR is triggered.

- **Sponsor to be supportive with payout ratio and management fee in units to remain.** MUST expects payout ratio and management fee in units to remain status quo.

- **Risks on removal from FTSE EPRA NAREIT Global Developed Index is small.** Management believes the risk on being removed from the FTSE EPRA NAREIT Global Developed Index is small as MUST's market cap fell in tandem with the market and the index.

Target Price & Ratings 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 Apr 19	0.87	0.92	BUY
2:	17 Jun 19	0.87	1.00	BUY
3:	16 Aug 19	0.89	1.00	BUY
4:	22 Aug 19	0.89	1.10	BUY
5:	11 Oct 19	0.92	1.10	BUY
6:	04 Nov 19	0.92	1.10	BUY
7:	06 Feb 20	1.07	1.15	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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