

14 August 2024

Property | REITS

Prime US REIT (PRIME SP)

Buy (Maintained)

Delivering On Strategies; BUY

Target Price (Return): USD0.23 (24.9%)
 Price (Market Cap): USD0.18 (USD238m)
 ESG score: 3.2 (out of 4)
 Avg Daily Turnover (USD/USD) 0.95m/m

- **Keep BUY and USD0.23 TP, 25% upside.** Prime US REIT's 1H24 results were in line. Operationally, the REIT had a commendable year so far, delivering on its two key priorities of loan refinancing and deleveraging via asset sale. Portfolio occupancy (2Q24) dipped slightly QoQ but guided encouraging prospective leasing signs with the US office market showing increasing signs of bottoming. The stock has surged 40% over the last month but is still trading at 0.3x PB and we see further room for recovery with a rate cut on the cards.
- **Successfully refinanced USD550m loans**, comprising a USD400m term loan and a USD150m revolving credit – removing a key overhang. The loans will be extended for an initial term of two years (until July 2026), with an additional one-year extension option, leaving it with no refinancing needs until mid-2027. As the REIT has USD330m of existing debt hedges in place (until July 2026), c.67% of its debt will remain hedged. Post refinancing, we expect overall borrowing cost at c.5% for FY24F and c.5.5% for FY25F.
- **Portfolio occupancy (2Q) of 83.9%** (-0.8 ppt QoQ), excluding the Washingtonian Center, which is undergoing asset enhancements. Leasing momentum has picked up with leasing volume for 2Q/1H increasing 46%/105% YoY. Notably, 59% of the leases signed in 2Q were new leases (1Q:49%). Occupancy improvements (2Q) came from Reston Square (61%, +14.1ppt) and 171 7th Street (73.5%, +2.5ppt) while decline was seen at Promenade I & II (85.7%, -6.3ppt). Prime is in late-stage negotiation with a large tenant at Park Tower that could improve asset occupancy to c.90% from 68% at present. Rent reversions (2Q) stood at -1.3% (1Q: -1.8%).
- **Adjusted gearing of 46.4%**, post the completion of One Town Center divestments which was completed in 10 Jul 2024. The asset was sold for USD82m, c.3% discount to Dec-2023 valuation of USD84.8m. We expect Prime's interest coverage ratio (ICR) to be at c.2.5x for FY24F – still within maximum allowable gearing limit of 50%. With increased market odds of at least two US Federal Reserve rate cuts by end-2024, we believe further cap rate expansions are unlikely. Hence, we expect its overall asset value to remain stable during year-end valuation, with a recovery seen in FY25F.
- **1H24 DPU of USD0.18** with a 10% dividend pay-out ratio similar to 2H23. Distributable income (1H24) declined 20% YoY to USD23.3m, in line with expectations. The retained distributable income will be used for capex and to repay debt. We expect the REIT to maintain a similar 10% payout ratio for 2H24 and restore to 90% payout in FY25F. No changes to our earnings estimates. It has an ESG score of 3.2, resulting in a 2% ESG premium.

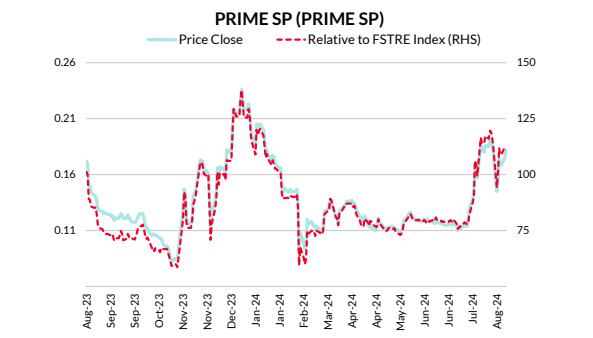
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Share Performance (%)

	YTD	1m	3m	6m	12m
Absolute	(16.5)	41.1	67.0	23.8	4.0
Relative	(4.7)	44.8	67.5	28.6	14.4
52-wk Price low/high (USD)				0.08	-0.24



Source: Bloomberg

Overall ESG Score: 3.2 (out of 4)

E: EXCELLENT

11 out of the 12 properties in PRIME's portfolio are US Green Building Council Leadership in Energy and Environmental Design ("LEED") or Energy Star certified. Prime has also undertaken additional long-term energy saving initiatives across six key assets.

S: GOOD

Prime enhanced its workplace safety in light of COVID-19 using technology to ensure social distancing, upgrading air filters and increased cleaning frequency of high touch areas. To engage with tenants specifically, the property managers at Prime's properties regularly held events with overall wellbeing in mind, ie Ice cream Socials, Lemonade Stands, Hot Dog events, Holiday Breakfasts, Puppy Therapy, Friday Popcorn, as well as fitness classes.

G: GOOD

Majority independent board and clear delineation of roles between the Board and Management. Improving stakeholder engagements since listing. Greater details in earnings quality as well as market outlook and update disclosures.

Note:

Small cap stocks are defined as companies with a market capitalisation of less than USD0.5bn.

Forecasts and Valuation	Dec-22	Dec-23	Dec-24F	Dec-25F	Dec-26F
Total turnover (USDm)	163	160	145	149	158
Net property income (USDm)	97.9	93.6	82.4	84.6	89.3
Reported net profit (USDm)	(27)	(116)	12	42	56
Total distributable income (USDm)	77.1	57.8	43.4	40.7	44.9
DPS (USD)	0.07	0.03	0.00	0.03	0.03
DPS growth (%)	(3.5)	(58.8)	(87.7)	744.8	10.2
P/B (x)	0.24	0.30	0.33	0.32	0.32
Dividend Yield (%)	36.1	14.9	1.8	15.4	17.0
Return on average equity (%)	(2.9)	(14.4)	1.7	5.8	7.6
Return on average assets (%)	(1.7)	(7.6)	0.9	3.1	4.0

Source: Company data, RHB

Financial Exhibits

Asia	Financial summary	Dec-22	Dec-23	Dec-24F	Dec-25F	Dec-26F
Singapore	Recurring EPS (USD)	(0.02)	(0.10)	0.01	0.03	0.04
Property	EPS (USD)	(0.02)	(0.10)	0.01	0.03	0.04
Prime US REIT	DPS (USD)	0.07	0.03	0.00	0.03	0.03
PRIME SP	BVPS (USD)	0.76	0.60	0.55	0.56	0.58
Buy	Return on average equity (%)	(2.9)	(14.4)	1.7	5.8	7.6
	Weighted avg adjusted shares (m)	1,175.26	1,189.33	1,308.54	1,308.80	1,309.05
Valuation basis						
DDM						
Key drivers	Valuation metrics	Dec-22	Dec-23	Dec-24F	Dec-25F	Dec-26F
i. Under-rented portfolio in a good mix of growth markets;	Recurring P/E (x)	na	na	19.42	5.63	4.23
ii. 100% Class A office buildings; and	P/E (x)	na	na	19.42	5.63	4.23
iii. Trading at distress valuations.	P/B (x)	0.2	0.3	0.3	0.3	0.3
	FCF Yield (%)	41.4	28.3	12.1	20.1	27.7
	Dividend Yield (%)	36.1	14.9	1.8	15.4	17.0
	EV/EBITDA (x)	(8.07)	(6.15)	(6.96)	(6.96)	(6.93)
	EV/EBIT (x)	(8.07)	(6.15)	(6.96)	(6.96)	(6.93)
Key risks	Income statement (USDm)	Dec-22	Dec-23	Dec-24F	Dec-25F	Dec-26F
i. Continued decline in US office portfolio valuations resulting in potential gearing breach;	Total turnover	163	160	145	149	158
ii. Prolonged WFH trends resulting in continued structural decline in office demand; and	EBITDA	87	85	74	76	80
iii. Regulatory changes and changes to tax efficient structure.	Operating profit	87	85	74	76	80
	Net interest	(22)	(28)	(30)	(34)	(35)
	Pre-tax profit	(41)	(116)	7	45	62
	Taxation	14	(0)	6	(3)	(5)
	Recurring net profit	(27)	(116)	12	42	56
Company Profile	Cash flow (USDm)	Dec-22	Dec-23	Dec-24F	Dec-25F	Dec-26F
Prime US REIT ("PRIME") is a diversified Singapore real estate investment trust ("REIT") with a focus on stabilised income-producing office assets in the US. PRIME offers investors a unique exposure to a high-quality portfolio of 14 prime and freehold office properties, strategically located in 10 primary markets in the US.	Change in working capital	(2.8)	1.0	(11.1)	0.8	1.1
	Cash flow from operations	89.2	85.6	54.1	71.2	86.4
	Capex	(0.6)	(24.4)	(25.3)	(23.2)	(20.5)
	Cash flow from investing activities	(30.1)	(24.3)	52.7	(23.2)	(20.4)
	Dividends paid	(76.9)	(64.3)	(4.3)	(36.7)	(40.4)
	Cash flow from financing activities	(61.3)	(61.1)	(125.2)	(52.7)	(56.2)
	Cash at beginning of period	13.9	11.6	11.8	14.3	11.2
	Net change in cash	(2.2)	0.2	(18.5)	(4.7)	9.8
	Ending balance cash	11.6	11.8	14.3	11.2	12.5
	Balance sheet (USDm)	Dec-22	Dec-23	Dec-24F	Dec-25F	Dec-26F
	Total cash and equivalents	12	12	14	11	13
	Total investments	1,572	1,424	1,343	1,379	1,427
	Total assets	1,589	1,444	1,361	1,394	1,443
	Short-term debt	0	478	0	0	0
	Total long-term debt	666	218	607	627	649
	Total liabilities	695	730	635	659	688
	Shareholders' equity	894	714	726	735	755
	Total equity	894	714	726	735	755
	Net debt	654	685	592	616	637
	Total liabilities & equity	1,589	1,444	1,361	1,394	1,443
	Key metrics	Dec-22	Dec-23	Dec-24F	Dec-25F	Dec-26F
	Revenue growth (%)	4.0	(2.0)	(9.1)	2.9	6.0
	Recurrent EPS growth (%)	(137.3)	325.3	0.0	244.7	33.2
	Operating EBITDA margin (%)	53.5	53.2	50.7	50.6	50.3
	Net profit margin (%)	(16.5)	(72.5)	8.4	28.3	35.6
	Dividend payout ratio (%)	(286.6)	(27.8)	35.4	86.8	71.8
	Capex/sales (%)	0.4	15.3	17.5	15.5	12.9
	Interest cover (x)	4.04	3.02	2.48	2.19	2.25

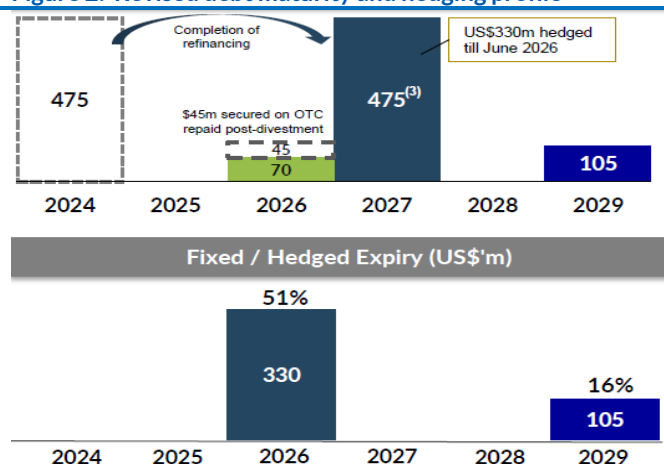
Source: Company data, RHB

Figure 1: Portfolio occupancy and carrying value

Properties ¹ (As at 30 June 2024)	% Contribution by Carrying Value	PRIME's Occupancy	Submarket Occupancy ²
222 Main (Salt Lake City)	13.7%	99.3%	87.8%
171 17th Street (Atlanta)	12.9%	73.5%	72.6%
Village Center Station II (Denver)	10.9%	100.0%	78.4%
Park Tower (Sacramento)	10.7%	68.1%	91.4%
Sorrento Towers (San Diego)	9.4%	96.3%	94.2%
Tower I at Emeryville (San Francisco Bay Area)	7.8%	74.2%	78.5%
Crosspoint (Philadelphia)	7.2%	100.0%	82.6%
Tower 909 (Dallas)	5.6%	91.5%	74.4%
Village Center Station I (Denver)	5.3%	55.1%	78.4%
Promenade I & II (San Antonio)	5.1%	85.7%	84.5%
101 South Hanley (St. Louis)	5.1%	89.7%	84.6%
Reston Square (Suburb Virginia, DC)	2.0%	61.1%	77.0%
Portfolio (exclude asset undergoing enhancement)	95.7%	83.9%	
Asset undergoing Asset Enhancement Initiative			
One Washingtonian Center (Suburb Maryland, DC)	4.3%	33.3%	92.8%
Portfolio (include asset undergoing enhancement)	100.0%	80.0%	

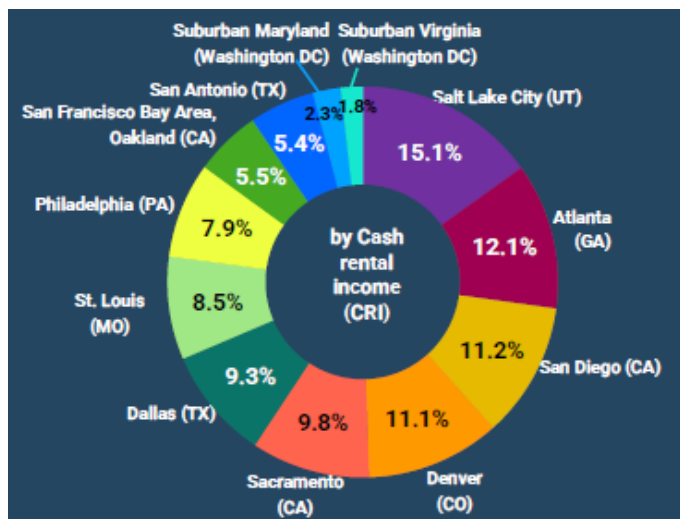
1. Excludes One Town Center which was divested on 10 July 2024
2. CoStar as of 9 July 2024

Figure 2: Revised debt maturity and hedging profile



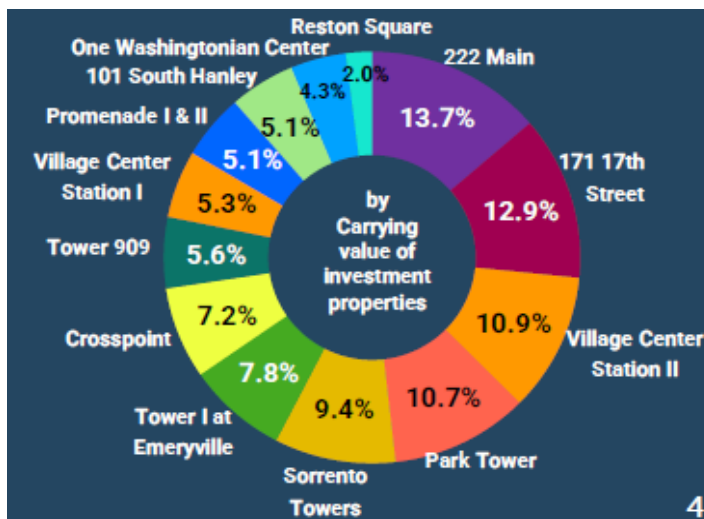
Source: Company data

Figure 3: Market exposure by rental income



Source: Company data

Figure 4: Asset value breakdown



Source: Company data

Emissions And ESG

Trend analysis

In 2023, Prime's operations totalled 24,409 tCO₂e, of which 95% was attributed to Scope 2 emissions. This represents an 8% decrease in GHG emissions over the previous year, partially attributable to lower physical occupancy and management efforts to actively manage energy consumption. Overall water consumption from operations too saw a 1.3% YoY reduction for 13 properties (excluding One Town Center).

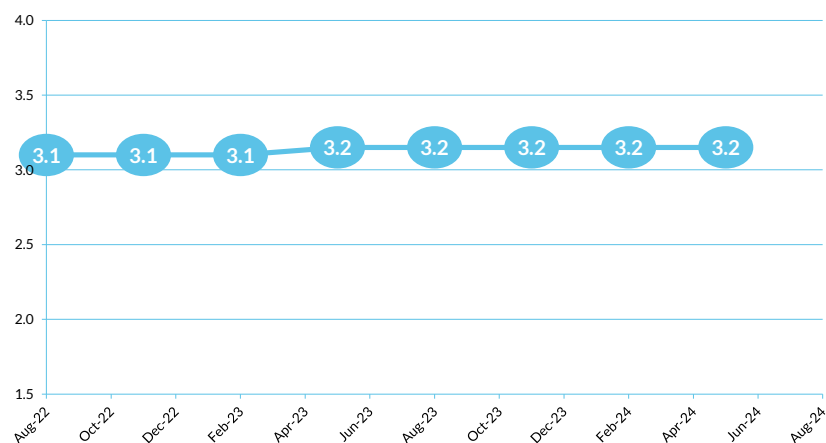
Emissions (tCO ₂ e)	Dec-21	Dec-22	Dec-23
Scope 1	na	1,023	1,162
Scope 2	18,761	25,501	23,247
Scope 3	na	na	na
Total emissions	18,761	26,524	24,409

Source: Company data, RHB

Latest ESG-Related Developments

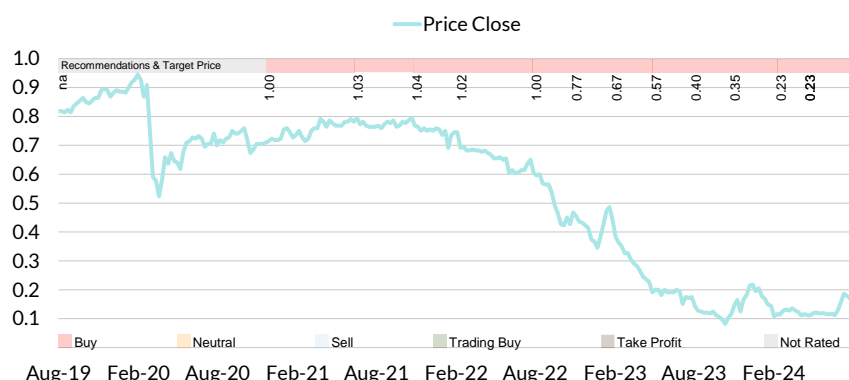
- In Feb 2023, Prime partnered with Gridium to achieve significant energy savings and attract ESG-focused tenants.
- The newly implemented Gridium software combines utility smart meter data, utility bill data, weather data and industry benchmarking into tools to help better manage energy performance.
- Prime also engaged in various tenant and community activities across its assets in order to improve tenant bonding.

ESG Rating History



Source: RHB

Recommendation Chart



Source: RHB, Bloomberg

Date	Recommendation	Target Price	Price
2024-07-16	Buy	0.23	0.14
2024-05-21	Buy	0.23	0.13
2024-02-23	Buy	0.23	0.12
2023-11-08	Buy	0.35	0.14
2023-08-11	Buy	0.40	0.18
2023-05-11	Buy	0.57	0.19
2023-02-09	Buy	0.67	0.45
2022-11-09	Buy	0.77	0.44
2022-08-08	Buy	1.00	0.66
2022-02-17	Buy	1.02	0.75
2021-11-07	Buy	1.04	0.80
2021-08-04	Buy	1.03	0.75
2021-06-24	Buy	1.03	0.80
2021-02-18	Buy	1.00	0.76
2020-12-03	Buy	1.00	0.70

Source: RHB, Bloomberg

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Buy:	Share price may exceed 10% over the next 12 months
Trading Buy:	Share price may exceed 15% over the next 3 months, however longer-term outlook remains uncertain
Neutral:	Share price may fall within the range of +/- 10% over the next 12 months
Take Profit:	Target price has been attained. Look to accumulate at lower levels
Sell:	Share price may fall by more than 10% over the next 12 months
Not Rated:	Stock is not within regular research coverage

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