

2 February 2023

Property | REITS

Keppel Pacific Oak US REIT (KORE SP)

Buy (Maintained)

Calm Amidst The Storm; Keep BUY

Target Price (Return): USD0.69 (26.6%)
 Price (Market Cap): USD0.55 (USD569m)
 ESG score: 3.00 (out of 4)
 Avg Daily Turnover (USD/USD) 0.73m/0.73m

- **Stay BUY with revised DDM-derived USD0.69 TP from USD0.74, 27% upside.** Keppel Pacific Oak US REIT's results were slightly below (96% of forecast), while valuations surprised on the upside. Operational numbers remained strong despite very challenging office market conditions – we attribute this to assets in right markets and a strong leasing team. Gearing remains comfortable at below 40%. YTD, KORE's share price has bounced back c.19%, but remains cheap at 30% below book and offers 10% yield.

- **4Q adjusted NPI down 6% QoQ** due to lower income from assets divested during the quarter and higher repair and maintenance expenses. Adjusted DPU (2H) was 2.8% lower YoY as higher revenue was offset by an increase in interest and property expenses. Overall portfolio value surprised on the upside, coming in relatively flat (+0.2% YoY) on an absolute basis, but declined 2.7% when including capex and tenant improvements. In comparison, its peer Manulife US REIT (MUST SP, BUY, TP: USD0.43) earlier announced a 11% valuation decline. This again differentiates a relatively positive outlook on KORE's submarket and its limited tenant concentration risks.

- **Outlook moderated but still positive.** Rent reversions are expected to remain in positive low single digits (FY22: 3.8%, 4Q: 8.1%) with asking rents still c.6% below average in place rents. Despite uncertainty and negative news flows from the tech sector, its overall portfolio occupancy remained flat QoQ at 92.6%. For FY23, while some fluctuations in occupancy are anticipated from known tenant exits, it remains in active discussion with various prospects and confident of maintaining its high occupancy levels with demand staying relatively firm for smaller leases. The impact from big tech layoffs and cutbacks is not expected to be significant in its Seattle and Sacramento submarkets and overall portfolio as such. Physical occupancy in its assets have instead seen an improvement from market cool-off and is currently at c.60%, which it sees as positive.

- **Strong balance sheet** with 77% of its debt hedged and no debt maturing until 4Q24. Every 50bps rate increase should have a c.1.2% DPU impact.

- **Acquisitions not the focus**, as it sees limited opportunities in the market currently and its high cost of capital limits any accretion potential. Overall gearing is comfortable at 37.5%. It has earmarked two assets in its portfolio which it could potentially divest at the right price.

- **We have lowered FY23-24F DPU by 5-6%** by tweaking our occupancy assumptions, with higher interest costs. ESG score of 3.0 (out of 4.0) is in line with country median, and we applied a 0% premium/discount to our DDM-derived TP.

Analyst

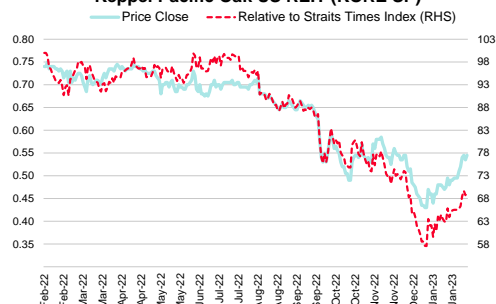
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Share Performance (%)

	YTD	1m	3m	6m	12m
Absolute	18.5	18.5	0.0	(22.7)	(26.4)
Relative	14.6	14.6	(7.9)	(27.0)	(30.3)
52-wk Price low/high (USD)				0.43 – 0.75	

Keppel Pacific Oak US REIT (KORE SP)



Source: Bloomberg

Forecasts and Valuation	Dec-21	Dec-22	Dec-23F	Dec-24F	Dec-25F
Total turnover (USDm)	141	148	148	150	152
Net property income (USDm)	82.7	84.3	88.2	89.3	91.3
Reported net profit (USDm)	77.4	48.5	28.7	42.9	57.7
Total distributable income (USDm)	62.4	60.6	56.4	56.1	57.2
DPS (USD)	0.06	0.06	0.05	0.05	0.05
DPS growth (%)	2.1	(8.4)	(7.1)	(0.8)	1.9
P/B (x)	0.63	0.67	0.70	0.71	0.71
Dividend Yield (%)	11.6	10.7	9.9	9.8	10.0
Return on average equity (%)	9.5	5.7	3.5	5.3	7.2
Return on average assets (%)	5.4	3.2	1.9	2.9	3.8

Source: Company data, RHB

Overall ESG Score: 3.00 (out of 4)

E: GOOD

Target to reduce Greenhouse Gas Emissions by 30% by 2030 from 2019. Manager also plans to embark on various energy saving initiatives, water saving efforts and waste conservation efforts.

S: GOOD

In 2020, an Employee Assistance Programme (EAP) was introduced to provide mental health support for employees and their families, to help them cope with the challenges of working from home, family responsibilities and living in an acutely changed world due to the pandemic.

G: GOOD

KORE Increased its outreach of investor education and interaction to both institutional and retail investors in FY20. Improving transparency levels in earnings and information disclosure. Well established corporate governance frameworks relating to board matters

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Financial Exhibits

Asia

Singapore

Property

Keppel Pacific Oak US REIT

KORE SP

Buy

Valuation basis

DDM

Key drivers

i. Portfolio focussed on secondary growth markets;
ii. Minimal tenant concentration and strong lease execution;
iii. Under rented portfolio and growth from rent escalations

Key risks

i. Protracted increase in interest rates;
ii. US economy tipping into deep recession, and
iii. Structural reduction in office demand

Company Profile

Keppel Pacific Oak US REITs strategy is to principally invest in a diversified portfolio of income-producing commercial assets and real estate-related assets in key growth markets of the USA, with favourable economic and office fundamentals that are above the national average, so as to provide sustainable distributions and strong total returns for unit holders.

Financial summary	Dec-21	Dec-22	Dec-23F	Dec-24F	Dec-25F
Recurring EPS (USD)	0.08	0.05	0.03	0.04	0.06
EPS (USD)	0.08	0.05	0.03	0.04	0.06
DPS (USD)	0.06	0.06	0.05	0.05	0.05
BVPS (USD)	0.87	0.81	0.78	0.77	0.77
Return on average equity (%)	9.5	5.7	3.5	5.3	7.2
Weighted avg adjusted shares (m)	983.53	1,042.05	1,044.05	1,046.05	1,048.05

Valuation metrics	Dec-21	Dec-22	Dec-23F	Dec-24F	Dec-25F	
Recurring P/E (x)	6.93	11.71	19.80	13.29	9.89	
P/E (x)	6.93	11.71	19.80	13.29	9.89	
P/B (x)	0.6	0.7	0.7	0.7	0.7	
FCF Yield (%)	10.3	6.3	16.0	14.2	14.4	
Dividend Yield (%)	11.6	10.7	9.9	9.8	10.0	
EV/EBITDA (x)	-	5.37	-	4.09	-	3.79
EV/EBIT (x)	-	5.37	-	4.09	-	3.79

Income statement (USDm)	Dec-21	Dec-22	Dec-23F	Dec-24F	Dec-25F
Total turnover	141	148	148	150	152
EBITDA	76	78	81	82	84
Operating profit	76	78	81	82	84
Net interest	(15)	(19)	(21)	(22)	(23)
Pre-tax profit	90	48	29	43	58
Taxation	(13)	0	0	0	0
Recurring net profit	77	48	29	43	58

Cash flow (USDm)	Dec-21	Dec-22	Dec-23F	Dec-24F	Dec-25F
Change in working capital	2	2	11	(0)	(1)
Cash flow from operations	83	79	96	86	87
Capex	(27)	(44)	(5)	(5)	(5)
Cash flow from investing activities	(131)	(8)	(5)	(5)	(5)
Dividends paid	(66)	(58)	(56)	(56)	(57)
Cash flow from financing activities	42	(59)	(87)	(77)	(79)
Cash at beginning of period	57	51	63	67	72
Net change in cash	(6)	12	4	4	4
Ending balance cash	51	63	67	72	76

Balance sheet (USDm)	Dec-21	Dec-22	Dec-23F	Dec-24F	Dec-25F
Total cash and equivalents	51	63	67	72	76
Total investments	1,456	1,423	1,400	1,391	1,396
Total other assets	3	27	27	27	27
Total assets	1,514	1,520	1,501	1,497	1,506
Short-term debt	123	10	5	5	5
Total long-term debt	438	567	561	569	577
Total liabilities	660	673	683	692	700
Shareholders' equity	854	846	818	805	806
Total equity	854	846	818	805	806
Net debt	511	514	498	502	506
Total liabilities & equity	1,514	1,520	1,501	1,497	1,506

Key metrics	Dec-21	Dec-22	Dec-23F	Dec-24F	Dec-25F
Revenue growth (%)	1.2	4.8	0.0	1.2	1.2
Recurrent EPS growth (%)	31.0	(40.8)	(40.8)	48.9	34.4
Operating EBITDA margin (%)	53.9	52.4	54.9	54.8	55.4
Net profit margin (%)	54.8	32.8	19.4	28.6	38.1
Dividend payout ratio (%)	80.7	124.9	196.3	130.8	99.1
Capex/sales (%)	19.5	29.5	3.4	3.3	3.3
Interest cover (x)	5.19	4.16	3.83	3.67	3.60

Source: Company data, RHB

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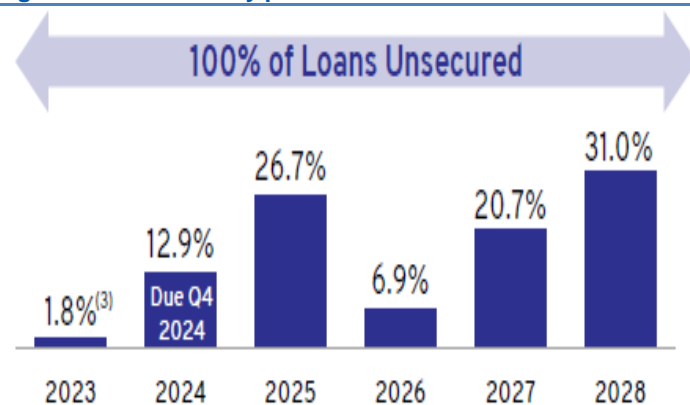
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Figure 1: DDM valuation

	FY23F	FY24F	FY25F	FY26F	FY27F	Terminal Value
DPU (US cents)	5.40	5.36	5.46	5.67	5.80	76.3
Intrinsic value (USD)	0.69					
ESG premium/(discount)	0.00					
Target price (USD)	0.69					
Current Price (USD)	0.55					
Price Upside	26.6%					
Distribution Yield FY22F	9.9%					
Total Returns	37%					
Assumptions						
Risk-free rate (%)	3.0					
Beta	0.9					
Cost of equity (%)	9.8					
Terminal growth (%)	2.0					

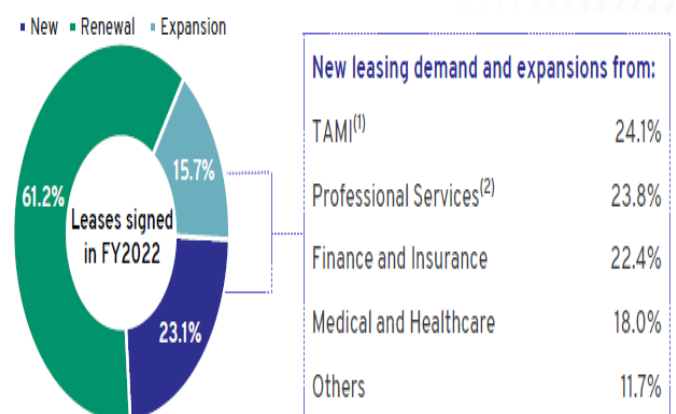
Source: RHB

Figure 2: Debt maturity profile



Source: Company data

Figure 3: Leasing demand by type and tenant sectors



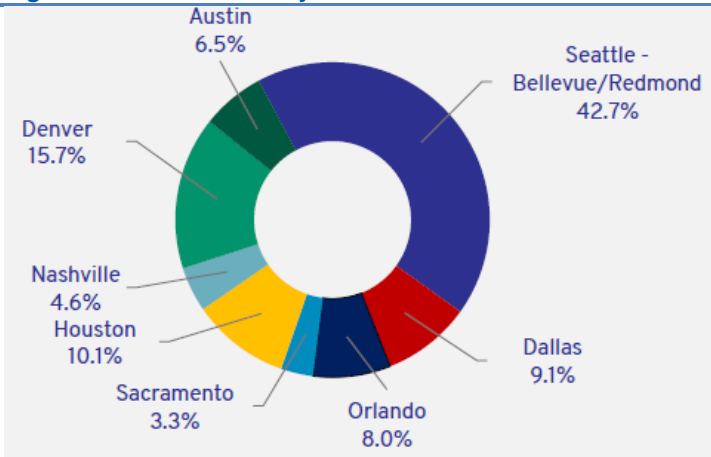
Source: Company data

Figure 4: Portfolio valuation changes by asset

Property	31 December 2021 (US\$ 'million)	Capex	Disposal	FV gain/(loss) on Investment Property	31 December 2022 (US\$ 'million)	Change (US\$ 'million)
The Plaza Buildings Seattle, Bellevue CBD	339.0	5.8	-	(4.8)	340.0	1.0
Bellevue Technology Center Seattle, Eastside Bellevue	151.0	9.3	-	(5.3)	155.0	4.0
The Westpark Portfolio Seattle, Redmond	224.0	4.2	-	1.8	230.0	6.0
Great Hills Plaza Austin, Northwest	42.7	(0.1)	-	(1.4)	41.2	(1.5)
Westech 360 Austin, Northwest	48.3	2.1	-	(3.1)	47.3	(1.0)
Westmoor Center Denver, Northwest	130.0	2.8	-	(2.6)	130.2	0.2
105 Edgeview Denver, Broomfield	60.0	0.5	-	(0.5)	60.0	-
Bridge Crossing Nashville, Brentwood	46.6	0.2	-	(3.5)	43.3	(3.3)
1800 West Loop South Houston, Galleria/Uptown	79.3	5.7	-	(8.1)	76.9	(2.4)
Bellaire Park Houston, Galleria/Bellaire	51.5	2.2	-	(2.4)	51.3	(0.2)
One Twenty Five Dallas, Las Colinas	106.6	2.9	-	(3.9)	105.6	(1.0)
Maitland Promenade I & II Orlando, Maitland	97.3	2.0	-	(5.5)	93.8	(3.5)
Iron Point Sacramento, Folsom	44.9	3.8	-	0.1	48.8	3.9
Subtotal excluding Powers Ferry and Northridge I & II ⁽¹⁾	1,421.2	41.4	-	(39.2)	1,423.4	2.2
Powers Ferry ⁽¹⁾ Atlanta, Georgia	15.7	(0.1)	(15.6)	-	-	NM
Northridge Center I & II ⁽¹⁾ Atlanta, Georgia	18.9	1.2	(20.1)	-	-	NM
Total Portfolio Value	1,455.8	42.5	(35.7)	(39.2)	1,423.4	NM

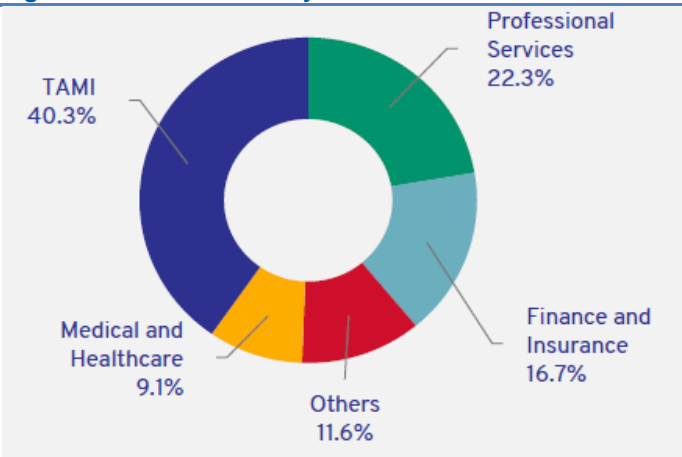
Source: Company data

Figure 5: Rental income by markets



Source: Company data

Figure 6: Rental income by tenant sectors



Source: Company data

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Recommendation Chart

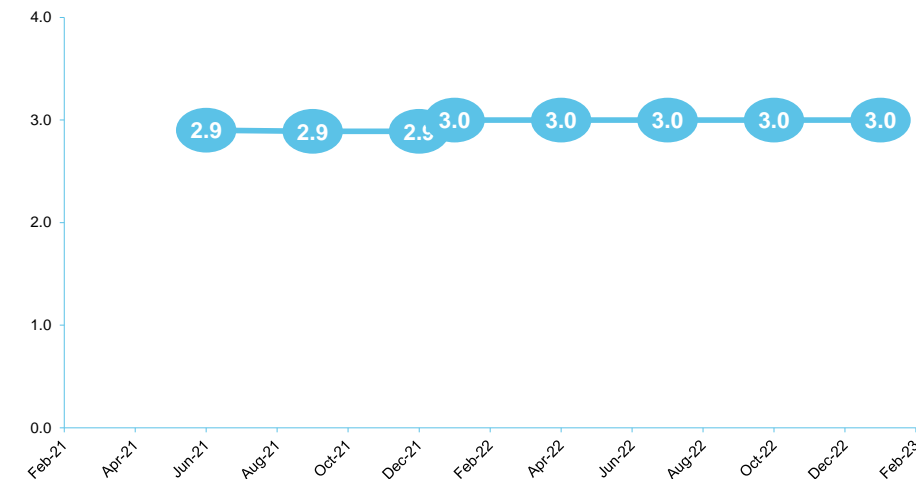


Source: RHB, Bloomberg

Date	Recommendation	Target Price	Price
2022-10-27	Buy	0.74	0.55
2022-07-27	Buy	0.87	0.69
2022-01-27	Buy	0.92	0.76
2021-09-22	Buy	0.90	0.78
2021-07-27	Buy	0.90	0.80
2021-01-28	Buy	0.84	0.73
2020-10-22	Buy	0.80	0.71
2020-06-07	Buy	0.80	0.73
2020-04-13	Buy	0.76	0.54
2020-01-22	Buy	0.88	0.79
2019-10-16	Buy	na	0.76
2019-09-09	Buy	na	0.75
2019-09-06	Buy	na	0.75
2019-07-18	Buy	na	0.81
2019-07-17	Buy	na	0.82

Source: RHB, Bloomberg

ESG Rating History



Source: RHB

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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
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Not Rated:	Stock is not within regular research coverage

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Analyst	Company
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