Singapore Company Update

10 November 2022

Property | REITS

Prime US REIT (PRIME SP)

Buy (Maintained)

Positive Leasing Momentum; Stay BUY

Target Price (Return):	USD0.77 (+59%)
Price (Market Cap):	USD0.48 (USD566m)
ESG score:	3.10 (out of 4)
Avg Daily Turnover (USD/USD)	0.94m/0.94m

- **BUY, new TP of USD0.77 from USD1, 59% upside.** Prime US REIT's 3Q22 and 9M22 earnings are in line. There were positive read-throughs, with a healthy pick-up in office leasing activity (in 3Q), on par with the total of 1H22. Management also gave more colour on debt hedges and interest rate risk management strategies, which lends us some comfort. The counter has been oversold along with its peers, and trading close to distressed levels (ie below pandemic levels) – at 0.6x P/BV with a c.14% FY22F yield, amid an overly bearish outlook for the US office sub-sector.
- **3Q22 leasing volume picked up to 246k sqf** (1H22: 258k sqf, 3Q21: 187ksqf). More importantly, leasing activity was broad-based at eight of its 13 assets. Serviced office player Regus took up two-thirds of the space WeWork vacated at Tower 1 at Emeryville, lifting the occupancy rate by 18ppt to 77%. PRIME is also in active discussions with a tenant to backfill the space vacated by Whitley Bradley & Brown in Reston Square in July. Its portfolio occupancy rate, as a result, remained stable QoQ at 89.6%. Physical occupancy rates (return to office) in its office buildings have been improving and now vary from the mid-20% to high 70% levels, with lower utilisation rates mainly at its California, Washington and Denver assets and from government tenants. JLL data shows that office re-entry levels reached a post-pandemic high in late September, with more companies issuing stricter return-to-office guidelines.
- **Office rental rates show little signs of slowing down.** Despite the hike in vacancies, there has been little sign of the rental market slowing down, as tenants have been willing to pay more for good-quality premium spaces in order to woo tenants. This was reflected in PRIME registering its 10th straight quarter of positive rental reversions (3Q22: +10.1%), although management noted that tenant incentives have gone up a little. Portfolio average in-place rental rates are still 6.7% below asking rates, and we expect rental reversions to be in the positive mid-single digits in 2023.
- **No debt maturity until Jul 2024, with two-thirds of debts hedged until mid-2026 and beyond.** PRIME has extendable options under its current loan arrangement, which can be exercised at minimal cost and from longer-tenure interest rate swaps. 83% of its debt is hedged, with every 100bps rate increase expected to decrease DPU by c.2%. Gearing remains comfortable, at 38.7%. We expect a cap rate expansion on the back of rising interest rates, but do not anticipate its portfolio value to decline by >10%.
- **We cut FY22-24F DPU by 1%, 4% and 4%**, adjusting our occupancy rate and financing cost assumptions. We also lift our COE assumption by 175bps to impute higher interest rates and market risks. PRIME has an ESG score of 3.1 out of 4.0. As this score is one notch above the country median score, we apply a 2% premium to our intrinsic value to derive our TP.

Forecasts and Valuation	Dec-20	Dec-21	Dec-22F	Dec-23F	Dec-24F
Total turnover (USDm)	144	157	165	168	174
Net property income (USDm)	95	101	104	106	109
Reported net profit (USDm)	23.2	68.2	65.1	75.3	76.8
Total distributable income (USDm)	72.1	75.6	81.2	80.4	82.2
DPS (USD)	0.07	0.07	0.07	0.07	0.07
DPS growth (%)	119.8	(2.0)	1.3	(1.9)	1.5
P/B (x)	0.55	0.54	0.58	0.58	0.58
Dividend Yield (%)	14.5	14.2	14.3	14.1	14.3
Return on average equity (%)	2.7	7.2	6.6	7.7	7.8
Return on average assets (%)	1.7	4.4	3.9	4.4	4.4

Source: Company data, RHB

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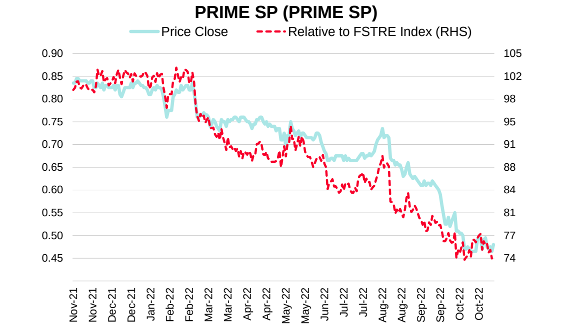
Share Performance (%)

	YTD	1m	3m	6m	12m
Absolute	(42.5)	(5.9)	(33.3)	(32.4)	(42.5)
Relative	(26.5)	0.2	(17.2)	(16.8)	(24.4)
52-wk Price low/high (USD)					0.47 – 0.85



Source: Bloomberg

Overall ESG Score: 3.10 (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. The REIT 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 of the REIT's assets regularly held events with overall wellbeing in mind, such as ice cream socials, lemonade stands, hot dog events, holiday breakfasts, puppy therapy, Friday popcorn, as well as fitness classes.

G: GOOD
PRIME has been improving its stakeholder engagement since its listing. It also provides greater details on earnings quality as well as market outlook and update disclosures. There is a clear delineation of roles between the Board and management.

Financial Exhibits

Asia
Singapore
Property
Prime US REIT
PRIME SP
Buy

Valuation basis

DDM

Key drivers

i. Under-rented portfolio in growth markets with a well diverse tenant base;
ii. Inbuilt rental rate escalations providing organic growth;
Inorganic growth potential via acquisitions

Key risks

i. US economy faltering into s deep recession;
ii. Rising work-from-home trends resulting in a structural decline in office space demand;
iii. Regulatory changes and changes to the tax-efficient structure

Company Profile

Prime US REIT is a diversified Singapore REIT with a focus on stabilised income-producing office assets in the US. The REIT offers investors unique exposure to a high-quality portfolio of 14 prime and freehold office properties, strategically located in ten primary markets in the US.

Financial summary	Dec-20	Dec-21	Dec-22F	Dec-23F	Dec-24F
Recurring EPS (USD)	0.02	0.06	0.06	0.06	0.06
EPS (USD)	0.02	0.06	0.06	0.06	0.06
DPS (USD)	0.07	0.07	0.07	0.07	0.07
BVPS (USD)	0.87	0.89	0.83	0.83	0.82
Return on average equity (%)	2.7	7.2	6.6	7.7	7.8
Weighted avg adjusted shares (m)	1,039.00	1,111.62	1,179.57	1,188.98	1,198.65

Valuation metrics	Dec-20	Dec-21	Dec-22F	Dec-23F	Dec-24F
Recurring P/E (x)	21.49	7.83	8.70	7.58	7.49
P/E (x)	21.49	7.83	8.70	7.58	7.49
P/B (x)	0.5	0.5	0.6	0.6	0.6
FCF Yield (%)	17.5	16.9	16.3	15.4	16.9
Dividend Yield (%)	14.5	14.2	14.3	14.1	14.3
EV/EBITDA (x)	- 5.43	- 5.56	- 5.08	- 5.05	- 4.93
EV/EBIT (x)	- 5.43	- 5.56	- 5.08	- 5.05	- 4.93

Income statement (USDm)	Dec-20	Dec-21	Dec-22F	Dec-23F	Dec-24F
Total turnover	144	157	165	168	174
EBITDA	85	91	93	95	98
Operating profit	85	91	93	95	98
Net interest	(15)	(17)	(19)	(21)	(23)
Pre-tax profit	25	73	65	80	82
Taxation	(2)	(5)	0	(5)	(5)
Recurring net profit	23	68	65	75	77

Cash flow (USDm)	Dec-20	Dec-21	Dec-22F	Dec-23F	Dec-24F
Change in working capital	4	2	9	1	2
Cash flow from operations	90	96	109	105	114
Capex	(2)	(6)	(17)	(17)	(17)
Cash flow from investing activities	(176)	(260)	(17)	(17)	(17)
Dividends paid	(65)	(69)	(81)	(80)	(82)
Cash flow from financing activities	86	141	(85)	(79)	(83)
Cash at beginning of period	38	37	14	17	16
Net change in cash	(0)	(24)	7	9	14
Ending balance cash	37	14	17	16	15

Balance sheet (USDm)	Dec-20	Dec-21	Dec-22F	Dec-23F	Dec-24F
Total cash and equivalents	37	14	17	16	15
Total investments	1,405	1,655	1,670	1,703	1,737
Total assets	1,447	1,673	1,691	1,724	1,757
Total long-term debt	480	629	646	670	694
Total liabilities	539	682	708	739	770
Shareholders' equity	908	991	983	985	987
Total equity	908	991	983	985	987
Net debt	443	615	629	654	679
Total liabilities & equity	1,447	1,673	1,691	1,724	1,757

Key metrics	Dec-20	Dec-21	Dec-22F	Dec-23F	Dec-24F
Revenue growth (%)	136.7	9.2	5.1	1.7	3.8
Recurrent EPS growth (%)	(38.7)	174.6	(10.1)	14.8	1.2
Operating EBITDA margin (%)	59.5	58.0	56.7	56.5	56.2
Net profit margin (%)	16.2	43.5	39.5	44.9	44.1
Dividend payout ratio (%)	310.6	110.9	124.8	106.7	107.1
Capex/sales (%)	1.7	3.5	10.0	10.0	9.8
Interest cover (x)	5.74	5.35	4.99	4.49	4.34

Source: Company data, RHB

Figure 1: DDM valuation table

	FY22F	FY23F	FY24F	FY25F	FY26F	Terminal value
DPU (US cents)	6.89	6.76	6.86	6.93	7.01	81.4
Intrinsic Value (USD)	0.75					
ESG Premium/(discount)	0.02					
Target Price (USD)	0.77					
Current Price (USD)	0.48					
Price Upside (%)	59.0%					
Distribution Yield FY19F (%)	14.3%					
Total Return (%)	73.3%					
Assumptions						
Risk-free rate (%)	3%					
Beta	1.0					
Cost of equity (%)	10.8%					
Terminal growth (%)	2%					

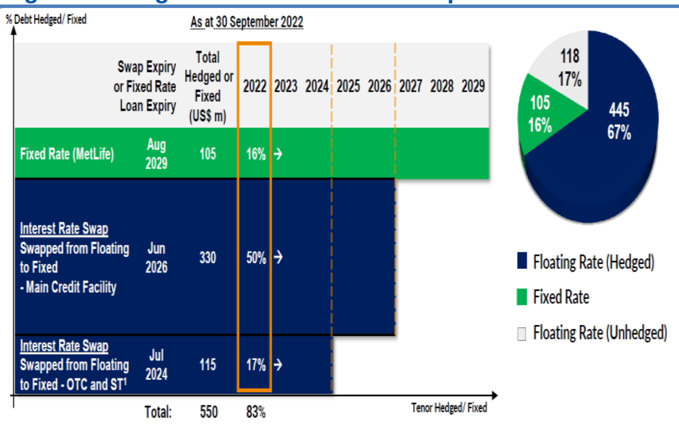
Source: RHB

Figure 2: Weighted debt maturity of 2.9 years (post extension)

Facility	Lender	Tranches	Facility Available (US$ m)	Outstanding Principal (US$ m)	Hedge/ Fixed	Loan Maturity
Main Credit Facility – Floating	Syndicate led by Bank of America	Revolver	200	48	Unhedged	Jul-2023 Extendable to 2024
		Term Loan 1	200	200	Hedged: US$330m	Jul-2023 Extendable to 2024
		Term Loan 2	200	200		Jul-2024
Total Main Credit Facility			600	448		
Fixed (Secured)	MetLife	Fixed Rate Loan	105	105	Fixed Rate	Aug-2029
Total Fixed MetLife Loan			105	105		
One Town Center – Secured Floating	Citizens Bank	Term Loan	45	45	Hedged	Jul-2024 Two one-year extension options Fully extended maturity in Jul-2026
		Revolver	20	-		
Sorrento Tower – Secured Floating		Term Loan	70	70	Hedged	
		Revolver	25	-		
Total Citizens Loans			160	115		
			865	668		

Source: Company data

Figure 3: Long-tenure interest rate swaps



Source: Company data

Figure 4: PRIME's average rental rates are 7% below the asking rental rates

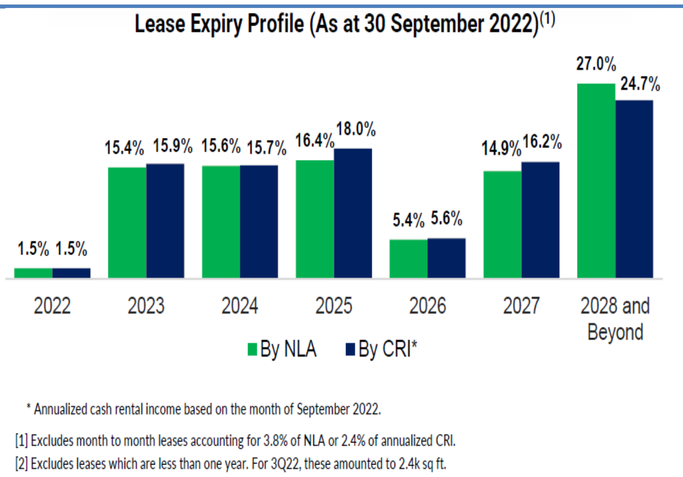
Name of Property	% Contribution by Asset Carrying Value	Occupancy	WALE (years)	% Lease expiry remaining in 2022 by CRI[1]	Annual In Place Rent (US$)	Annual Asking Rent (US$)	Potential Rental Reversion
222 Main	13.7%	96.8%	4.3	0.1%	$39.71	39.50	-0.5%
171 17th Street	12.4%	95.0%	5.7	0.6%	$29.16	$28.00	-4.0%
Park Tower	9.5%	87.1%	3.7	0.3%	$33.46	$37.21	11.2%
Village Center Station II	9.3%	100.0%	5.8	0.0%	NA[2]	NA[2]	NA[2]
Sorrento Towers	9.0%	97.0%	5.5	0.1%	$41.06	$49.80	21.3%
Tower I at Emeryville	6.9%	77.1%	4.3	0.1%	$56.65	$55.80	-1.5%
CrossPoint	6.2%	97.1%	2.8	0.1%	$35.68	$42.00	17.7%
One Town Center	6.1%	98.0%	5.2	0.0%	$34.91	$37.00	6.0%
One Washingtonian Center	5.6%	81.2%	2.2	0.0%	$36.19	$36.50	0.8%
Tower 909	5.0%	84.7%	3.4	0.1%	$29.37	$33.20	13.0%
Village Center Station I	4.9%	69.9%	1.9	0.0%	$22.57	$24.50	8.6%
101 South Hanley	4.9%	95.8%	3.7	0.1%	$29.08	$31.50	8.3%
Promenade I & II	4.5%	98.6%	2.2	0.0%	$28.57	$28.50	-0.2%
Reston Square	2.0%	47.1%	3.1	0.0%	$39.76	$40.00	0.6%
Total / Weighted Average	100.0%	89.6%	4.1	1.5%	$34.10[2]	$36.37[2]	6.7%[2]

3Q2022 RESULTS | NOVEMBER 2022

[1] Lease expiry excludes month to month leases accounting for 2.4% of CRI
[2] Excludes Village Center Station II which is fully leased until 2028

Source: Company data

Figure 5: 16% of PRIME's leases will expire in 2023



Source: Company data

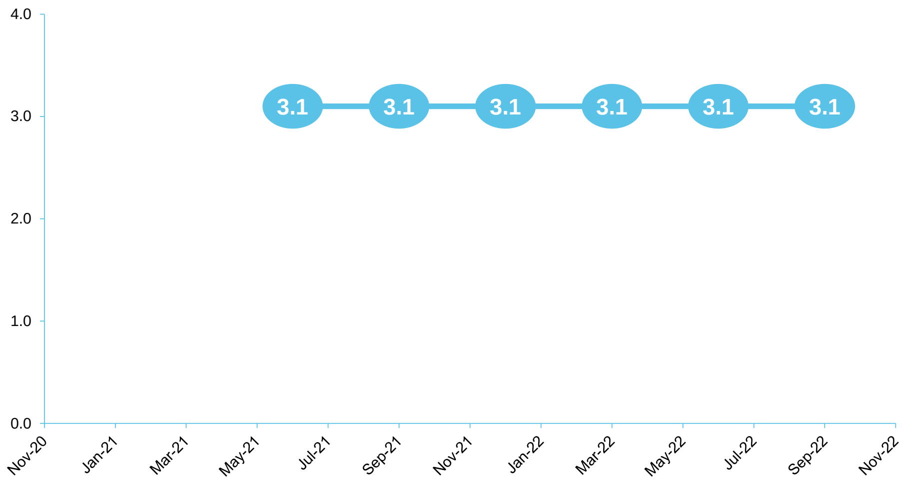
Recommendation Chart

Source: RHB, Bloomberg

Date	Recommendation	Target Price	Price
2022-08-08	Buy	1.00	0.72
2022-02-17	Buy	1.02	0.82
2021-11-07	Buy	1.04	0.88
2021-08-04	Buy	1.03	0.83
2021-06-24	Buy	1.03	0.88
2021-02-18	Buy	1.00	0.83
2020-12-03	Buy	1.00	0.77

Source: RHB, Bloomberg

ESG Rating History



Source: RHB

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