

INITIATE COVERAGE

Prime US REIT (PRIME SP)

Rising From The Abyss

PRIME's Class A offices will benefit from a flight to quality despite the gloom in the US office market in 2H22. It is able to continue generating positive rental reversion as in-place passing rent was 6.7% below asking rent in 4Q22. It has prudently fixed or hedged 83% of its borrowings to fixed rates and has no refinancing till Jul 24. PRIME corrected 40% in 2H22. Valuation has bombed out with 2023 distribution yield at 15.2% and P/NAV at 0.56x. Initiate coverage with BUY and target price of US\$0.78.

WHAT'S NEW

- **Class A offices benefit from flight to quality...** PRIME US REIT (PRIME) invests in stabilised income-producing office assets in the US. It has a high-quality portfolio of 14 Class A freehold office properties in 13 key office markets, valued at US\$1.7b as at Jun 22. PRIME focuses on Class A office buildings, which are the best in class. Class A offices with amenities are well sought after to attract employees back to work from the office. Demand is skewed towards high-quality Class A office space. According to Cushman & Wakefield, Class A offices outperform in net absorption. Premium in rents commanded by newer Class A office buildings have also doubled during the COVID-19 pandemic.
- **...and attract blue chip tenants.** Key tenants are blue chip companies with strong credit standing. Charter Communications, Goldman Sachs, Sodexo, Dexcom, Wells Fargo and Bank of America are among its top-10 tenants. WALE for its top-10 tenants is healthy at 4.6 years. Some 73% of tenants are in the established and growth (STEM/TAMI) sectors.
- **18-hour and Super Sun Belt cities attract in-migration.** PRIME has sizeable exposure to 18-hour and Super Sun Belt cities, which attract an influx of companies and people. These high-growth cities have low or no state-level taxes, a highly educated workforce generated by renowned local universities, rich amenities and good infrastructure.
- **Room to consistently generate positive rental reversion.** PRIME has generated positive rental reversion consecutively for the past 10 quarters. On a portfolio basis, in-place passing rents were 6.7% below asking rents in 4Q22. Within its portfolio, Park Tower at Sacramento, Sorrento Towers at San Diego, Crosspoint at Philadelphia and Tower 909 at Irving have the potential to provide strong positive rental reversion of 11.2%, 21.3%, 17.7% and 13.0% respectively in 4Q22.

Click [here](#) for Blue Top dated 17 Jan 23

KEY FINANCIALS

Year to 31 Dec (US\$m)	2020	2021	2022F	2023F	2024F
Net turnover	144	157	164	168	171
EBITDA	84	89	90	93	95
Operating profit	84	89	90	93	95
Net profit (rep./act.)	22	66	(36)	66	67
Net profit (adj.)	67	67	62	66	67
EPU (US\$ cent)	6.5	6.1	5.3	5.5	5.6
DPU (US\$ cent)	6.9	6.8	6.7	6.3	6.4
PE (x)	6.4	6.8	7.9	7.5	7.4
P/B (x)	0.5	0.5	0.6	0.6	0.6
DPU Yld (%)	16.7	16.3	16.2	15.2	15.3
Net margin (%)	15.2	42.3	(21.9)	39.3	39.4
Net debt/(cash) to equity (%)	48.8	62.1	72.0	74.6	77.4
Interest cover (x)	5.6	5.2	4.1	3.7	3.7
ROE (%)	2.5	7.0	n.a.	7.5	7.7
Consensus DPU (US\$ cent)	n.a.	n.a.	7.0	7.1	7.0
UOBKH/Consensus (x)	-	-	0.96	0.89	0.91

Source: Prime US REIT, Bloomberg, UOB Kay Hian

BUY

Share Price	US\$0.415
Target Price	US\$0.78
Upside	+88.0%

COMPANY DESCRIPTION

PRIME invests in stabilised income-producing office assets in the US. It has a high-quality portfolio of 14 Class A freehold office properties strategically located in 13 key office markets valued at US\$1.7b as at Sep 22.

STOCK DATA

GICS sector	Real Estate
Bloomberg ticker:	PRIME SP
Shares issued (m):	1,183.0
Market cap (US\$m):	491.0
Market cap (US\$m):	491.0
3-mth avg daily t'over (US\$m):	0.7

Price Performance (%)

52-week high/low US\$0.835/US\$0.365

1mth	3mth	6mth	1yr	YTD
(8.8)	(11.7)	(38.5)	(48.8)	2.5

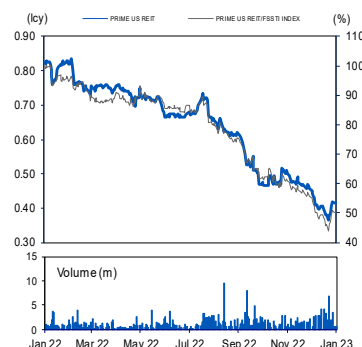
Major Shareholders

	%
KBS REIT	18.2
Keppel Corp	5.3

FY23 NAV/Share (US\$) 0.73

FY23 Net Debt/Share (US\$) 0.55

PRICE CHART



Source: Bloomberg

ANALYST(S)

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STOCK IMPACT

- **PRIME corrected 40% in 2H22.** We are of the view that the selling is overdone and current weakness presents a good opportunity to accumulate the stock.
- **Manageable rise in gearing.** We expect cap rate to increase by 50bp to 6.8% driven by higher interest rates. We estimate a US\$124.8m drop in the fair value of investment properties, which causes aggregate leverage to deteriorate by 3.4ppt to 42.1% but is well within the regulatory limit of 50%. We see NAV per unit dropping 13% to US\$0.75.
- **Exposure to fluctuations in US interest rates prudently hedged.** Some 83% of PRIME's borrowings is fixed rate or hedged to fixed rates. About 66% of its borrowings is fixed or hedged till mid-26. It does not have any refinancing obligations till Jul 24.

VALUATION/RECOMMENDATION

- **Bombed-out valuations.** PRIME provides 2023 distribution yield of 15.2% and yield spread of 11.7%. The stock is oversold with P/NAV at 0.56x.
- **We initiate coverage with BUY and target price of US\$0.78** based on DDM (cost of equity: 9.0%, terminal growth: 1.0%).

SHARE PRICE CATALYST

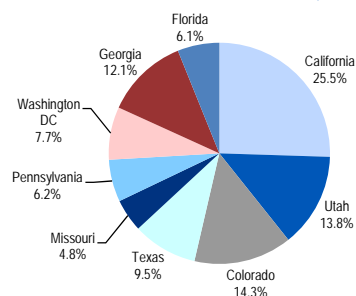
- Growth from Super Sun Belt and 18-hour cities driven by in-migration.
- Growth from continued positive rental reversion.

PEER COMPARISON – OFFICE REITS

Name	Ticker	Rec	Currency	Price 16 Jan 22	Target Price	Mkt Cap (US\$m)	Yield (%) Hist	Yield (%) Curr	Yield (%) Fwd	Yield (%) Fwd 2Y	Debt to Equity (%)	Debt to Assets (%)	P/NAV (x)
Singapore – Office REITs													
CapLand Int Comm Trust	CICT SP	BUY	S\$	2.04	2.29	10,245	5.1	5.2	5.5	5.6	68.9	41.2	0.96
Keppel REIT	KREIT SP	BUY	S\$	0.89	1.17	2,521	6.5	6.7	6.2	6.8	68.9	37.9	0.65
Suntec REIT	SUN SP	HOLD	S\$	1.36	1.37	2,960	6.4	6.7	5.6	5.6	78.7	43.1	0.65
Average							6.0	6.2	5.8	6.0	72.2	40.7	0.75
Singapore – Offshore Office REITs													
Cromwell REIT EUR	CERT SP	NR	Euro	1.46	n.a.	889	11.6	11.2	11.0	11.2	73.8	38.9	0.58
Elite Comm REIT GBP	ELITE SP	BUY	£	0.495	0.65	290	11.0	10.2	8.2	8.8	77.3	41.9	0.82
IREIT Global	IREIT SP	NR	S\$	0.52	n.a.	451	8.1	8.1	8.1	8.6	50.5	30.8	0.63
Keppel REIT USD	KORE SP	BUY	US\$	0.50	0.74	517	12.8	11.5	10.7	10.6	65.1	37.2	0.70
Manulife REIT USD	MUST SP	BUY	US\$	0.28	0.63	489	19.4	18.6	18.8	19.2	78.3	42.5	0.50
Prime US REIT USD	PRIME SP	BUY	US\$	0.415	0.78	491	16.3	16.2	15.2	15.3	65.8	38.7	0.56
Average							13.2	12.6	12.0	12.3	68.4	38.3	0.63
US – Office REITs													
Alexandria Real Estate Equities	ARE US	NR	US\$	155.57	n.a.	25,527	2.9	3.0	3.2	3.4	57.5	30.8	1.44
Boston Properties	BXP US	NR	US\$	71.2	n.a.	11,161	5.5	5.5	5.6	5.7	228.8	59.7	1.81
Kilroy Realty Corp	KRC US	NR	US\$	40.54	n.a.	4,738	5.1	5.2	5.4	5.6	77.1	39.6	0.87
Vornado Realty Trust	VNO US	NR	US\$	23.31	n.a.	4,471	9.1	9.1	7.5	7.1	177.8	52.0	0.85
Cousins Properties	CUZ US	NR	US\$	25.98	n.a.	3,934	4.8	4.9	5.1	5.2	49.0	30.6	0.85
Douglas Emmett	DEI US	NR	US\$	15.77	n.a.	2,772	7.1	7.0	6.0	6.2	207.9	53.7	1.07
Equity Commonwealth	EQC US	NR	US\$	25.58	n.a.	2,799	0.0	3.9	0.0	0.0	0.0	0.0	1.09
Highwoods Properties	HIW US	NR	US\$	29.86	n.a.	3,141	6.6	6.7	6.8	6.8	113.9	49.0	1.27
Corporate Office Properties	OFC US	NR	US\$	27.99	n.a.	3,147	3.9	3.9	4.0	4.1	141.8	54.0	1.89
SL Green Realty Corp	SLG US	NR	US\$	38.05	n.a.	2,459	16.5	9.8	8.8	8.7	109.6	44.9	0.55
JBG Smith Properties	JBGS US	NR	US\$	19.65	n.a.	2,236	4.6	4.6	4.7	4.8	85.2	38.9	0.81
Hudson Pacific Properties	HPP US	NR	US\$	10.57	n.a.	1,490	9.5	9.5	9.5	9.7	121.4	44.8	0.51
Easterly Government Properties	DEA US	NR	US\$	15.81	n.a.	1,436	6.7	6.7	6.7	5.8	94.4	42.9	1.15
Paramount Group	PGRE US	NR	US\$	6.17	n.a.	1,356	4.7	4.9	4.8	4.9	106.9	45.2	0.37
Piedmont Office Realty Trust	PDM US	NR	US\$	9.99	n.a.	1,233	8.4	8.4	8.7	8.9	105.2	47.8	0.69
Empire State Realty Trust	ESRT US	NR	US\$	7.58	n.a.	1,224	1.8	1.9	2.5	2.7	247.8	54.6	1.36
Brandywine Realty Trust	BDN US	NR	US\$	6.55	n.a.	1,124	11.6	11.6	11.6	12.1	111.1	48.8	0.69
Veris Residential	VRE US	NR	US\$	16.8	n.a.	1,530	0.0	0.4	1.2	2.0	188.1	53.3	1.27
Office Properties Income Trust	OPI US	NR	US\$	17.01	n.a.	826	12.9	12.9	12.9	12.9	172.2	60.8	0.59
Orion Office REIT	ONL US	NR	US\$	8.84	n.a.	501	1.1	4.5	4.5	n.a.	58.6	36.2	0.50
Average							6.1	6.2	6.0	6.1	122.7	44.4	0.98

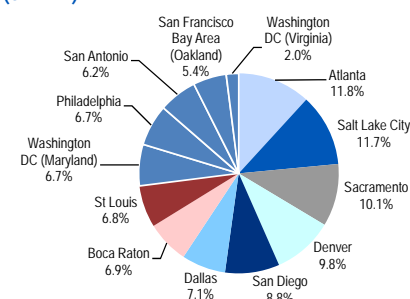
Source: Bloomberg, UOB Kay Hian

PORTFOLIO VALUATION BY STATE (SEP 22)



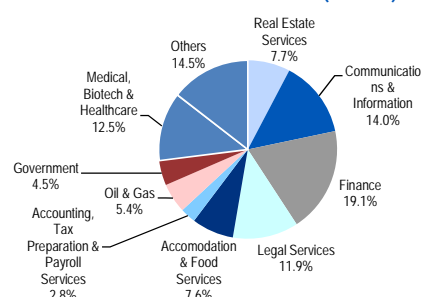
Source: PRIME

CASH RENTAL INCOME BY PRIMARY MARKET (SEP 22)



Source: PRIME

SECTOR DIVERSIFICATION BY CRI (SEP 22)



Source: PRIME

TOP 10 TENANTS AS % OF CRI (SEP 22)



Source: PRIME

PROFIT & LOSS

Year to 31 Dec (US\$m)	2021	2022F	2023F	2024F
Net turnover	156.7	164.4	167.6	171.0
EBITDA	89.1	89.7	92.9	94.9
Deprec. & amort.	0.0	0.0	0.0	0.0
EBIT	89.1	89.7	92.9	94.9
Net interest income/(expense)	(17.0)	(21.9)	(24.9)	(25.3)
Pre-tax profit	71.0	(30.5)	68.0	69.6
Tax	(4.7)	(5.5)	(2.1)	(2.2)
Net profit	66.3	(36.0)	65.9	67.4
Net profit (adj.)	67.4	62.4	65.9	67.4

BALANCE SHEET

Year to 31 Dec (US\$m)	2021	2022F	2023F	2024F
Fixed assets	1,653.0	1,545.0	1,557.0	1,569.0
Other LT assets	1.6	19.1	19.1	19.1
ST debt	n.a.	n.a.	n.a.	n.a.
Cash/ST investment	13.9	12.3	13.8	15.3
Other current assets	4.5	5.2	5.2	5.2
Total assets	1,672.9	1,581.5	1,595.1	1,608.6
Other current liabilities	26.5	23.4	23.9	24.4
LT debt	629.0	650.0	670.0	690.0
Other LT liabilities	26.4	21.9	22.0	22.0
Shareholders' equity	991.1	886.2	879.3	872.2
Total liabilities & equity	1,672.9	1,581.5	1,595.1	1,608.6

CASH FLOW

Year to 31 Dec (US\$m)	2021	2022F	2023F	2024F
Operating	95.7	90.5	93.7	95.6
Pre-tax profit	73.9	70.3	70.4	72.0
Deprec. & amort.	(3.5)	(3.1)	(4.4)	(4.4)
Working capital changes	1.7	(0.3)	0.3	0.3
Non-cash items	6.2	6.5	6.1	6.3
Other operating cashflows	17.4	17.2	21.3	21.5
Investing	(260.4)	(12.0)	(12.0)	(12.0)
Capex (growth)	(238.7)	0.0	0.0	0.0
Capex (maintenance)	(16.1)	(12.0)	(12.0)	(12.0)
Others	(5.5)	0.0	0.0	0.0
Financing	141.1	(80.1)	(80.1)	(82.2)
Distribution to unitholders	(69.4)	(79.3)	(75.2)	(76.9)
Issue of shares	80.0	0.0	0.0	0.0
Proceeds from borrowings	149.0	21.0	20.0	20.0
Others/interest paid	(18.4)	(21.9)	(24.9)	(25.3)
Net cash inflow (outflow)	(23.5)	(1.6)	1.6	1.4
Beginning cash & cash equivalent	37.4	13.9	12.3	13.8
Changes due to forex impact	(0.0)	0.0	0.0	0.0
Ending cash & cash equivalent	13.9	12.3	13.8	15.3

KEY METRICS

Year to 31 Dec (%)	2021	2022F	2023F	2024F
Profitability				
EBITDA margin	56.8	54.6	55.5	55.5
Pre-tax margin	45.3	(18.5)	40.6	40.7
Net margin	42.3	(21.9)	39.3	39.4
ROA	4.3	n.a.	4.1	4.2
ROE	7.0	n.a.	7.5	7.7
Growth				
Turnover	9.2	4.9	2.0	2.0
EBITDA	6.1	0.8	3.6	2.1
Pre-tax profit	198.3	(142.9)	n.a.	2.3
Net profit	204.5	(154.2)	n.a.	2.3
Net profit (adj.)	0.5	(7.4)	5.6	2.3
EPU	(6.3)	(12.9)	4.4	1.2
Leverage				
Debt to total capital	38.8	42.3	43.2	44.2
Debt to equity	63.5	73.3	76.2	79.1
Net debt/(cash) to equity	62.1	72.0	74.6	77.4
Interest cover (x)	5.2	4.1	3.7	3.7

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