



# Prime US REIT

Leasing is the top priority

## SINGAPORE | REAL ESTATE | 1Q23 Update

- 1Q23 distributable income was below expectations and 21% of FY23e forecast. The decline of 28.8% to US\$14.9mn was due to Prime increasing management fees paid in cash from 20% to 100%, higher interest expense, absence of lease termination income, and higher operating expenses. Excluding the higher proportion of management fees in cash, distributable income is still down 22.5%.
- Portfolio occupancy dipped slightly to 88.6% from 89.1% in 4Q22, with overall rental reversions of -2.6%.
- Maintain BUY, DDM-TP lowered from US\$0.70 to US\$0.46 as we lower our FY23e DPU forecast by 18% due to management fees paid all in cash, lower occupancy, and higher costs. We also cut FY24e and FY25e DPU by 18% and 15% respectively. Catalysts include improved leasing and a greater return to the office. Prime is currently trading at 0.3x P/NAV and below pandemic lows, and we believe that most of the negatives are already priced in. The current share price implies FY23e/FY24e DPU yield of 23/25%.

### Results at a glance

(US\$ mn)	1Q23	1Q22	YoY	Comments
Gross revenue	40.2	40.8	-1.7%	Lower due to occupancy decline.
Net property income	23.6	25.4	-7.2%	Higher property expenses as employees return to office.
Distributable Income	14.9	20.9	-28.8%	Increase in finance expenses, higher manager's base fees paid in cash, and absence of lease termination income received in 1Q22.

Source: Company, PSR

### The Positive

**+ Extension of debt maturities.** Prime is in the process of extending its 4-year term loan and RCF under its main credit facility (c.34% of total loans) by one year to July 2024 for an extension fee of 10bps. Expected completion is June 2023. This gives Prime some respite amid the credit crunch situation in the US.

### The Negatives

**- Portfolio occupancy dipped to 88.6% from 89.1% in 4Q22.** The biggest contributors to the decline were Tower 1 at Emeryville (-7ppts QoQ to 69.1%) and Sorento Towers (-2.8ppts QoQ to 94.4%).

**- Slowdown in leasing volumes.** Prime signed 64.4k sq ft of leases in 1Q23 (-62% YoY and -55% QoQ). However, leasing activity picked up in April 23 with c.38k sq ft of leases executed. Portfolio rental reversions for the quarter were -2.6%, impacted by two renewals with minimal upfront tenant improvements Capex, but with high positive net effective rent reversions. Excluding the two abovementioned renewals, 1Q23 rental reversions would have been +3.2%.

**- Gearing increased 1.6ppts QoQ to 43.7%,** due to the increase in borrowings to fund 2H22 distribution at the end of March 2023. 79% of debt is either on a fixed rate or hedged (82% in 4Q22), with 62% of debt hedged or fixed through to 2026 or beyond. After the extension of debt, Prime has no refinancing obligations till July 2024. Prime's effective interest cost for the quarter increased 30bps QoQ to 3.7%, and its interest coverage ratio is at 3.8x.

15 May 2023

### BUY (Maintained)

LAST CLOSE PRICE	USD 0.210
FORECAST DIV	USD 0.049
TARGET PRICE	USD 0.46
TOTAL RETURN	143.6%

### COMPANY DATA

BLOOMBERG CODE:	PRIME SP
O/S SHARES (MN) :	1,184
MARKET CAP (USD mn / SGD mn) :	249 / 249
52 - WK HI/LO (SGD) :	0.75 / 0.2
3M Average Daily T/O (mn) :	2.45

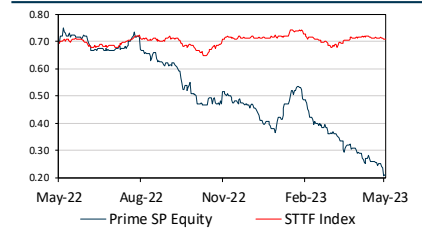
### MAJOR SHAREHOLDERS (%)

KBS PROPERTIES REIT III	18.3%
KEPPEL CORP LTD	5.3%
STEPPE INVESTMENTS PTE. LTD.	5.3%

### PRICE PERFORMANCE (%)

	1MTH	3MTH	YTD
COMPANY	(27.6)	(53.8)	(44.7)
STTF RETURN	(0.9)	(2.6)	0.8

### PRICE VS. STTF



Source: Bloomberg, PSR

### KEY FINANCIALS

Y/E Dec (US\$m)	FY21	FY22	FY23e	FY24e
Gross Revenue	156.7	163.0	171.8	179.2
NPI	100.7	97.9	100.3	104.6
Dist. Inc.	75.6	77.2	58.3	62.9
P/NAV (x)	0.25	0.28	0.28	0.28
DPU (US cents)	6.78	6.55	4.92	5.30
Dist. Yield (%)	32.29	31.19	23.42	25.25

Source: Company, PSR

### VALUATION METHOD

DDM (Cost of Equity: 13.75%; Terminal g: 1.75%)

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**Outlook**

Sodexo, Prime's second largest tenant (5% of income), is expected to vacate 165k sq ft of 191k sq ft leased at One Washingtonian Centre by Dec 2023. The balance space is currently sublet to other tenants who will likely remain. This could bring occupancy at One Washingtonian Centre to around 31%. With in-place rents c.6.8% below asking rents, there is still potential for positive rental reversions.

**Maintain BUY, DDM TP lowered from US\$0.70 to US\$0.46.** We lower our FY23e DPU forecast by 18% due to management fees paid all in cash, lower occupancy, and higher costs. We also cut FY24e and FY25e DPU by 18% and 15% respectively. We raise our cost of equity by 2.75% on the negative sentiment and credit crunch in the US commercial market. However, even though the US commercial market continues to face headwinds with higher vacancies and tighter credit, Prime is trading at 0.3x P/NAV and below pandemic lows, and we believe that most of the negatives are already priced in. Catalysts include improved leasing and a greater return to the office. The current share price implies FY23e/FY24e DPU yield of 23/25%.

**Financials**
**Income statement**

Y/E Dec, (US\$'000)	FY20	FY21	FY22	FY23e	FY24e
<b>Gross revenue</b>	<b>143,557</b>	<b>156,741</b>	<b>163,012</b>	<b>171,804</b>	<b>179,172</b>
Property expenses	(48,568)	(56,043)	(65,078)	(71,524)	(74,591)
<b>Net property income</b>	<b>94,989</b>	<b>100,698</b>	<b>97,934</b>	<b>100,281</b>	<b>104,581</b>
Net Finance (Expense)/Inc.	(14,868)	(16,982)	(21,599)	(26,962)	(27,069)
Manager's fees	(7,977)	(7,714)	(7,872)	(7,722)	(8,968)
Other items	(1,614)	(2,053)	(2,820)	(2,885)	(3,001)
FV change, derivatives & pptides	(45,291)	(1,052)	(106,450)	-	-
<b>Net income before tax</b>	<b>25,239</b>	<b>72,897</b>	<b>(40,807)</b>	<b>62,712</b>	<b>65,543</b>
Taxation	(2,030)	(4,709)	13,890	(6,271)	(6,554)
<b>Net income after Tax</b>	<b>23,209</b>	<b>68,188</b>	<b>(26,917)</b>	<b>56,441</b>	<b>58,989</b>
Distribution adjustments	48,869	7,413	104,067	1,812	3,909
<b>Income available for distribution</b>	<b>72,078</b>	<b>75,601</b>	<b>77,150</b>	<b>58,253</b>	<b>62,898</b>

**Per unit data**

Y/E Dec	FY20	FY21	FY22	FY23e	FY24e
NAV (US\$)	0.86	0.85	0.75	0.76	0.76
DPU (US cents)	6.94	6.78	6.55	4.92	5.30

**Cash Flow**

Y/E Dec, (US\$'000)	FY20	FY21	FY22	FY23e	FY24e
<b>CFO</b>					
<b>Net income before tax</b>	<b>25,239</b>	<b>72,897</b>	<b>(40,807)</b>	<b>62,712</b>	<b>65,543</b>
Adjustments	60,899	21,105	132,808	20,545	22,428
WC changes	3,754	1,724	(2,783)	858	862
<b>Cash generated from ops</b>	<b>89,892</b>	<b>95,726</b>	<b>89,218</b>	<b>84,115</b>	<b>88,833</b>
Others	406	345	534	6,121	6,397
<b>Cashflow from ops</b>	<b>90,298</b>	<b>96,071</b>	<b>89,752</b>	<b>90,236</b>	<b>95,230</b>

**CFI**

Acquisition of investment properti	(164,190)	(244,267)	(631)	-	-
Capex, net	(11,737)	(16,097)	(29,489)	(15,422)	(15,576)
Others	3	4	15	15	16
<b>Cashflow from investments</b>	<b>(175,924)</b>	<b>(260,360)</b>	<b>(30,105)</b>	<b>(15,407)</b>	<b>(15,560)</b>

**CFF**

Proceeds from issuance of units	120,000	80,000	-	-	-
Loans, net of repayments	32,829	132,044	15,530	(13,138)	(25,207)
Distributions	(65,004)	(69,441)	(76,852)	(58,253)	(62,898)
Others	(2,250)	(1,464)	(19)	(19)	(19)
<b>Cashflow from financing</b>	<b>85,575</b>	<b>141,139</b>	<b>(61,341)</b>	<b>(71,410)</b>	<b>(88,124)</b>
<b>Net change in cash</b>	<b>(51)</b>	<b>(23,150)</b>	<b>(1,694)</b>	<b>3,419</b>	<b>(8,454)</b>
Cash at the start of the period	37,862	37,442	13,873	11,581	15,003
FX changes	73	(38)	(28)	-	-
<b>Ending cash</b>	<b>37,884</b>	<b>14,254</b>	<b>12,151</b>	<b>15,000</b>	<b>6,549</b>

Source: Company, Phillip Securities Research (Singapore) Estimates

**Balance Sheet**

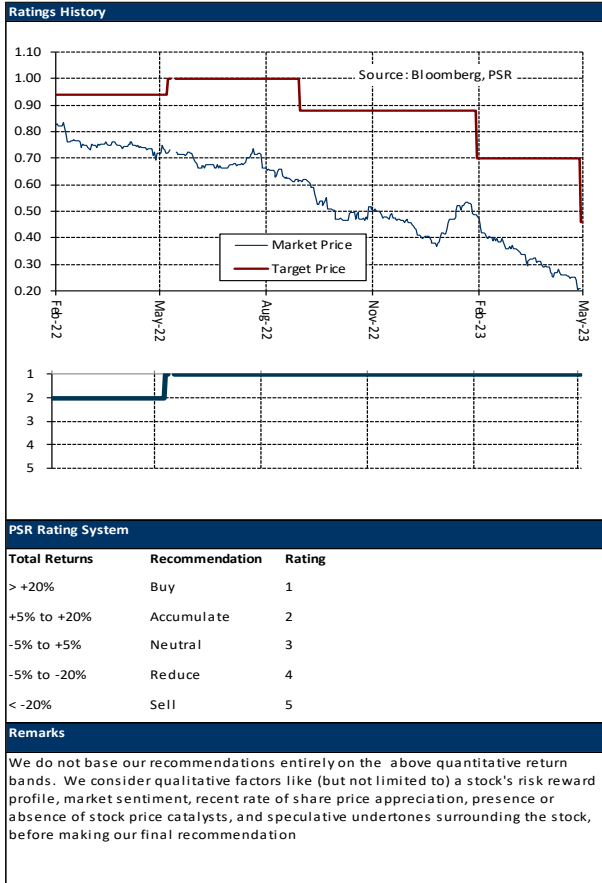
Y/E Dec, (US\$'000)	FY20	FY21	FY22	FY23e	FY24e
<b>ASSETS</b>					
Investment properties	1,405,200	1,653,000	1,542,200	1,557,622	1,573,198
Others	-	1,580	29,954	36,372	41,927
<b>Total non-current assets</b>	<b>1,405,200</b>	<b>1,654,580</b>	<b>1,572,154</b>	<b>1,593,994</b>	<b>1,615,126</b>
Trade receivables	1,623	2,997	3,859	1,256	4,078
Cash	37,442	13,873	11,581	15,003	6,552
Others	2,584	1,482	1,462	3,920	1,693
<b>Total current assets</b>	<b>41,649</b>	<b>18,352</b>	<b>16,902</b>	<b>20,179</b>	<b>12,324</b>
<b>Total Assets</b>	<b>1,446,849</b>	<b>1,672,932</b>	<b>1,589,056</b>	<b>1,614,173</b>	<b>1,627,449</b>
<b>LIABILITIES</b>					
Loans and borrowings	-	-	-	449,000	-
Trade payables	14,540	15,903	18,126	18,293	19,688
Rent received in advance	6,493	9,329	6,777	6,777	6,777
Others	860	1,253	843	1,635	1,559
<b>Total current liabilities</b>	<b>21,893</b>	<b>26,485</b>	<b>25,746</b>	<b>475,705</b>	<b>28,024</b>
Loans and borrowings	480,352	628,973	665,572	230,396	681,258
Others	36,812	26,390	3,945	9,895	16,509
<b>Total non-current liabilities</b>	<b>517,164</b>	<b>655,363</b>	<b>669,517</b>	<b>240,291</b>	<b>697,767</b>
<b>Total Liabilities</b>	<b>539,057</b>	<b>681,848</b>	<b>695,263</b>	<b>715,996</b>	<b>725,791</b>
<b>Net assets</b>	<b>907,792</b>	<b>991,084</b>	<b>893,793</b>	<b>898,177</b>	<b>901,658</b>
<b>Represented by:</b>					
Unitholders' funds	907,792	991,084	893,793	898,177	901,658

**Valuation Ratios**

Y/E Dec	FY20	FY21	FY22	FY23e	FY24e
P/NAV (x)	0.25	0.25	0.28	0.28	0.28
Distribution Yield (%)	33.0	32.3	31.2	23.4	25.2
NPI yield (%)	7.2	6.6	6.1	6.5	6.7

**Growth & Margins**

<b>Growth</b>					
Revenue	nm	9.2%	4.0%	5.4%	4.3%
Net property income (NPI)	nm	6.0%	-2.7%	2.4%	4.3%
Distributable income	nm	4.9%	2.0%	-24.5%	8.0%
DPU	nm	-2.3%	-3.4%	-24.9%	7.8%
<b>Margins</b>					
NPI margin	66.2%	64.2%	60.1%	58.4%	58.4%
<b>Key Ratios</b>					
Net Debt or (Net Cash)	442,910	615,100	653,991	664,393	674,705
Gearing	34.2%	38.1%	43.2%	43.6%	43.3%



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