

# Singapore Company Update

# Keppel Pacific Oak US REIT

Bloomberg: KORE SP | Reuters: KP.LSI

Refer to important disclosures at the end of this report

DBS Group Research . Equity

16 Feb 2024

## FULLY VALUED (Downgrade from BUY)

Last Traded Price (15 Feb 2024): US\$0.151 (STI : 3,176.69)  
Price Target 12-mth: US\$0.10 (34% downside) (Prev US\$0.48)

### Analysts

Rachel TAN +65 6682 3713 racheltanr@db.com

Derek TAN +65 6682 3716 derektan@db.com

### What's New

- Downgrade to FULLY VALUED; lower TP to US\$0.10, based on 0.15x P/B
- KORE is suspending dividends until end-2025 in a proactive strategy to build up liquidity
- Gearing (43%) and ICR ratio (3.2x) within MAS limits, despite better-than-expected asset value adjustment (-7% y-o-y)
- 2<sup>nd</sup> US REIT to suspend dividends, attention will likely turn to PRIME US REIT, whose financial metrics are weaker

### Price Relative



### Forecasts and Valuation

FY Dec (US\$m)	2022A	2023A	2024F	2025F
Gross Revenue	148	151	141	146
Net Property Inc	84.3	86.1	82.1	84.9
Total Return	48.5	(67.7)	43.2	44.7
Distribution Inc	60.6	52.2	44.4	46.0
EPU (US cts.)	4.64	(6.5)	4.10	4.19
EPU Gth (%)	(38)	nm	nm	2
DPU (US cts.)	5.80	2.50	0.0	0.0
DPU Gth (%)	(9)	(57)	(100)	nm
NAV per shr (US cts.)	81.0	69.2	72.8	76.3
PE (X)	3.3	nm	3.7	3.6
Distribution Yield (%)	38.4	16.6	0.0	0.0
P/NAV (x)	0.2	0.2	0.2	0.2
Aggregate Leverage (%)	38.0	43.0	42.4	41.6
ROAE (%)	5.7	(8.6)	5.8	5.6

Distn. Inc Chng (%): (8) -  
Consensus DPU (US \$): 5.30 5.00  
Other Broker Recs: B: 3 S: 0 H: 0

Source of all data on this page: Company, DBS Bank Ltd, Bloomberg Finance L.P.

## Down the same path

### Investment Thesis:

Unique technology tenants with office assets located in office growth markets in the US. Keppel Pacific Oak US REIT (KORE)'s assets in the tech hubs of Seattle, Austin, and Denver contribute more than 60% of its net property income (NPI). Despite a potential slowdown in the tech sector, these submarkets remain office growth markets in the US.

Delivered stable performance despite a volatile market over the past few years. KORE has successfully delivered resilient DPU in the past few years despite a volatile market during the pandemic and subsequently high inflation in the US economy. Operationally, KORE has also kept its portfolio at above 90% thus far, a commendable effort given the headwinds impacting the sector. However, unfortunately, the sector's structural concerns have subsequently impacted its funding.

Suspension of distributions to build up liquidity a surprise. Despite its operational & financial metrics coming in line with estimates, we were surprised by management's decision to suspend dividends for 2H24 up to end-2025, which we see as a conservative and proactive stance taken to manage its financial liquidity situation. We believe that the manager is probably proactively building up further liquidity to refinance its near-term debt expiry in case there is a "funding gap" when refinancing discussions start sometime in the coming quarters. However, this will cause an overhang on the stock in the interim.

Downgrade to FULLY VALUED; lower TP to US\$0.10. We downgrade our rating to Fully Valued and TP is cut to US\$0.10 from US\$0.48. Our TP is based on 0.15x P/B to factor in the suspension of distributions and risks of capital management.

### Key Risks

Economic growth impacted by inflation and/or recession. The key risk to our view is lower-than-expected rental income arising from slower demand for office if economic growth slows either due to inflation and/or a recession.

### At A Glance

Issued Capital (m shrs)	1,044
Mkt. Cap (US\$m/US\$m)	158 / 158
Major Shareholders (%)	
Temasek Holdings Pte	10.9
HILLSBORO CAPITAL LT	8.7
Keppel Corp Ltd	6.1
Free Float (%)	74.3
3m Avg. Daily Val (US\$m)	0.86
GIC Industry : Real Estate / Equity Real Estate Investment (REITs)	

## WHAT'S NEW

### Down the same path

#### Gearing kept within limits but dividends suspended until 2H2025

- Keppel Pacific Oak US REIT (KORE) announced, together with its 4Q23 results, that the manager intends to suspend dividends till 2H25 and announced a recapitalisation plan with a goal to meet the leverage ratio requirements of the MAS and banks.
- We note that the overall results were in line. Gearing of 43.2% (vs. the MAS limit of 50%/banks' limit of 45%) post FY23 revaluation loss of 7% y-o-y, was better than expected. ICR ratio of 3.2x is above the 2.5x MAS floor.
- The REIT has a weighted debt expiry profile (WADE) of 2.7 years with US\$75m (or 12.5% of loans) expiring in end-2024. As of 4Q23, KORE has close to S\$43.8m in cash on the balance sheet.
- In terms of operational results, 2H23/FY23 net property income (NPI) was up 2.3%/2.2% y-o-y to S\$42.2m/S\$86.1m.
- After netting financing and operational expenses, distributable income was down 10% to S\$26.1m, mainly due to higher interest costs.

#### Key Operational Highlights

- Portfolio occupancy remained relatively stable, trending down marginally to 90.7% from 91.2%. It has commendably kept occupancy above 90% in FY23, given the challenging US office sector.
- KORE recorded FY23 rental reversions of -1.8%, mainly due to Spectrum's renewal/expansion. Excluding Spectrum's lease renewal, FY23 reversions were at +0.9%. 4Q23 reversions were -4.4%, mainly due to the renewal of a lease of a tenant at The Plaza Building.
- The leases expiring in FY24 (9.7% of CRI) are mainly from The Plaza Building and Westpark. Management expects some potential vacancy at The Plaza Building, which may impact occupancy, slightly reducing it to 88% in FY24, which is still at a good level given the headwinds hitting the sector.
- Physical occupancy at KORE's properties were at 57.5% as at end-2023, remaining higher vs. gateway cities' <50% and second tier cities' c.50%.
- Management expects average interest costs could creep up marginally to 4.3% to 4.4%, post the early refinancing of loans due in 2024 and 2025.
- Management does not intend to cut management fees.

**Downgrade to FULLY VALUED; TP of US\$0.10.** We downgrade our rating to FULLY VALUED from BUY and lower our TP to US\$0.10. We pegged our TP to 0.15x P/B to factor in the suspension of distribution and higher capital management risks.

Despite operational & financial metrics coming in line with estimates, we were surprised by management's decision to suspend dividends for 2H24 up to end-2025, which we see as a conservative and proactive stance taken to manage its financial liquidity situation. We believe that the manager is probably proactively building up further liquidity to refinance its near-term debt expiry in case there is a "funding gap" when refinancing discussions start sometime in the coming quarters. We believe that this strategy of a dividend suspension will come as a surprise to unitholders during the execution of its recapitalisation plan, and the stock will remain under pressure in the interim.

#### Company Background

Keppel Pacific Oak US REIT (KORE) is a pure-play US office REIT listed in Singapore. Its portfolio consists of 13 freehold office assets located in Austin, Atlanta, Denver, Houston, Sacramento, Seattle, and Orlando with an aggregate net lettable area of around 4.7m sqft.

### Summary of results

Key operational data	4Q2023	3Q2023	%q-o-q	4Q2022	% y-o-y	FY2023	FY2022	% y-o-y
Revenue	36.4	38.4	-5.1%	36.7	-0.6%	150.8	148.0	1.9%
NPI	20.1	22.1	-8.9%	20.0	0.6%	86.1	84.3	2.2%
DI	13.0	13.1	-0.7%	14.4	-9.9%	52.2	60.6	-13.8%
DPU (est)	1.25	1.25	0.0%	1.38	-9.4%	2.50	5.80	-56.9%
Adj DPU (for mgmt fees in cash)	1.25	1.25	0.0%	1.38	-9.4%	2.50	5.65	-55.8%
Portfolio occupancies	90.3%	91.4%	-1.1 ppt	92.6%	-2.3 ppt			
Rental reversions	-4.4%	3.8%	-8.2 ppt	8.0%	-12.4 ppt			
WALE (years)	3.6	3.4	0.2	3.4	0.2			
Gearing (%)	43.2%	39.1%	4.1 ppt	38.2%	5 ppt			
Av cost of debt (%)	4.12%	4.06%	0.1 ppt	3.2%	0.9 ppt			
ICR (x)	3.2	3.3	(0.1)	4.0	(0.8)			
Hedging ratio	74%	76%	-2.2 ppt	78%	-4.1 ppt			
Leases expiring in FY2024	9.7%	13.0%	-3.3 ppt	16.5%	-6.8 ppt			
Leases expiring in FY2025	18.1%	17.3%	0.8 ppt	17.3%	0.8 ppt			

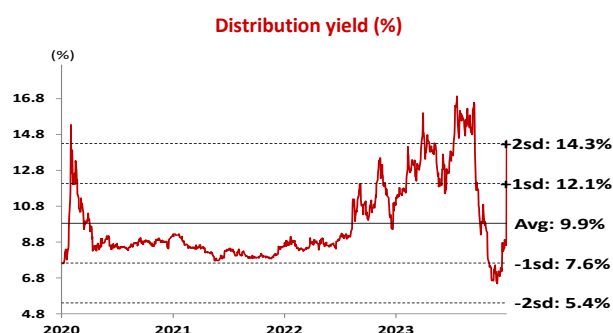
Source: Company, DBS Bank Ltd

### Interim Income Statement (US\$m)

FY Dec	2H2022	1H2023	2H2023	% chg yoy	% chg hoh
Gross revenue	73.9	75.9	74.8	1.3	(1.4)
Property expenses	(32.6)	(32.0)	(32.6)	0.1	1.8
Net Property Income	41.3	43.9	42.2	2.3	(3.7)
Other Operating expenses	(5.3)	(5.0)	(4.3)	(19.3)	(15.3)
Other Non Opg (Exp)/Inc	14.4	0.83	(10.3)	nm	nm
Associates & JV Inc	0.0	0.0	0.0	-	-
Net Interest (Exp)/Inc	(10.3)	(11.4)	(12.5)	(20.8)	(9.5)
Exceptional Gain/(Loss)	0.19	0.0	0.0	nm	-
<b>Net Income</b>	<b>40.2</b>	<b>28.3</b>	<b>15.2</b>	<b>(62.1)</b>	<b>(46.1)</b>
Tax	4.53	(4.2)	35.2	677.0	nm
Minority Interest	0.0	0.0	0.0	-	-
<b>Net Income after Tax</b>	<b>44.8</b>	<b>24.1</b>	<b>50.4</b>	<b>12.6</b>	<b>109.0</b>
Total Return	5.58	24.1	(91.8)	nm	(480.8)
Non-tax deductible Items	23.5	1.99	118	402.9	5,827.5
Net Inc available for Dist.	29.0	26.1	26.1	(10.1)	0.0
<b>Ratio (%)</b>					
Net Prop Inc Margin	55.9	57.8	56.4		
Dist. Payout Ratio	0.0	0.0	0.0		

Source of all data: Company, DBS Bank Ltd

### Historical Distribution yield and PB



Source: Bloomberg Finance L.P., DBS Bank Ltd estimates



Source: Bloomberg Finance L.P., DBS Bank Ltd estimates

### Income Statement (US\$m)

FY Dec	2021A	2022A	2023A	2024F	2025F
Gross revenue	141	148	151	141	146
Property expenses	(58.6)	(63.7)	(64.7)	(58.9)	(60.9)
<b>Net Property Income</b>	<b>82.7</b>	<b>84.3</b>	<b>86.1</b>	<b>82.1</b>	<b>84.9</b>
Other Operating expenses	(8.8)	(10.1)	(9.3)	(10.4)	(11.1)
Other Non Op (Exp)/Inc	11.8	31.3	(9.4)	0.0	0.0
Associates & JV Inc	0.0	0.0	0.0	0.0	0.0
Net Interest (Exp)/Inc	(14.6)	(18.5)	(23.8)	(28.5)	(29.1)
Exceptional Gain/(Loss)	19.2	(39.0)	(142)	0.0	0.0
<b>Net Income</b>	<b>90.3</b>	<b>48.0</b>	<b>(98.7)</b>	<b>43.2</b>	<b>44.7</b>
Tax	(13.0)	0.45	31.0	0.0	0.0
Minority Interest	0.0	0.0	0.0	0.0	0.0
Preference Dividend	0.0	0.0	0.0	0.0	0.0
<b>Net Income After Tax</b>	<b>77.4</b>	<b>48.5</b>	<b>(67.7)</b>	<b>43.2</b>	<b>44.7</b>
Total Return	77.4	48.5	(67.7)	43.2	44.7
Non-tax deductible Items	(14.9)	12.1	120	1.14	1.32
Net Inc available for Dist.	62.4	60.6	52.2	44.4	46.0
<b>Growth &amp; Ratio</b>					
Revenue Gth (%)	1.2	4.8	1.9	(6.5)	3.4
N Property Inc Gth (%)	(0.4)	1.9	2.2	(4.7)	3.4
Net Inc Gth (%)	37.2	(37.3)	nm	nm	3.3
Dist. Payout Ratio (%)	100.0	100.0	50.0	0.0	0.0
Net Prop Inc Margins (%)	58.5	57.0	57.1	58.2	58.2
Net Income Margins (%)	54.8	32.8	(44.9)	30.7	30.6
Dist to revenue (%)	44.2	40.9	34.6	31.5	31.5
Managers & Trustee's fees	6.2	6.8	6.2	7.4	7.6
ROAE (%)	9.5	5.7	(8.6)	5.8	5.6
ROA (%)	5.4	3.2	(4.6)	3.0	3.0
ROCE (%)	4.9	5.4	5.8	5.5	5.6
Int. Cover (x)	5.1	4.0	3.2	2.5	2.5

Source: Company, DBS Bank Ltd

**Interim Income Statement (US\$m)**

FY Dec	2H2021	1H2022	2H2022	1H2023	2H2023
Gross revenue	72.9	74.1	73.9	75.9	74.8
Property expenses	(30.8)	(31.1)	(32.6)	(32.0)	(32.6)
Net Property Income	42.1	43.0	41.3	43.9	42.2
Other Operating	(4.1)	(4.8)	(5.3)	(5.0)	(4.3)
Other Non Opg (Exp)/Inc	6.62	16.9	14.4	0.83	(10.3)
Associates & JV Inc	0.0	0.0	0.0	0.0	0.0
Net Interest (Exp)/Inc	(7.6)	(8.2)	(10.3)	(11.4)	(12.5)
Exceptional Gain/(Loss)	0.0	0.0	0.19	0.0	0.0
<b>Net Income</b>	<b>37.1</b>	<b>47.0</b>	<b>40.2</b>	<b>28.3</b>	<b>15.2</b>
Tax	(9.2)	(4.1)	4.53	(4.2)	35.2
Minority Interest	0.0	0.0	0.0	0.0	0.0
<b>Net Income after Tax</b>	<b>27.8</b>	<b>42.9</b>	<b>44.8</b>	<b>24.1</b>	<b>50.4</b>
Total Return	47.0	42.9	5.58	24.1	(91.8)
Non-tax deductible Items	(14.6)	(11.4)	23.5	1.99	118
Net Inc available for Dist.	32.5	31.5	29.0	26.1	26.1
<b>Growth &amp; Ratio</b>					
Revenue Gth (%)	7	2	0	3	(1)
N Property Inc Gth (%)	4	2	(4)	6	(4)
Net Inc Gth (%)	(8)	54	4	(46)	109
Net Prop Inc Margin (%)	57.8	58.0	55.9	57.8	56.4
Dist. Payout Ratio (%)	0.0	0.0	0.0	0.0	0.0

**Balance Sheet (US\$m)**

FY Dec	2021A	2022A	2023A	2024F	2025F
Investment Properties	1,456	1,423	1,326	1,359	1,387
Other LT Assets	2.56	26.9	18.3	18.3	18.3
Cash	51.0	63.4	43.8	69.4	102
ST Investment	0.0	0.0	0.0	0.0	0.0
Inventory	0.0	0.0	0.0	0.0	0.0
Debtors	3.99	3.90	4.28	4.70	4.86
Net Intangibles Assets	0.0	0.0	0.0	0.0	0.0
Other Current Assets	0.22	1.93	1.03	1.03	1.03
<b>Total Assets</b>	<b>1,514</b>	<b>1,520</b>	<b>1,394</b>	<b>1,452</b>	<b>1,513</b>
ST Debt	123	10.2	75.0	75.0	75.0
Creditor	24.1	27.4	33.3	31.3	32.4
Other Current Liab	7.25	7.42	7.83	7.83	7.83
LT Debt	438	567	525	541	555
Other LT Liabilities	66.7	60.9	29.8	29.8	29.8
Unit holders' funds	854	846	723	768	814
Minority Interests	0.0	0.0	0.0	0.0	0.0
<b>Total Funds &amp; Liabilities</b>	<b>1,514</b>	<b>1,520</b>	<b>1,394</b>	<b>1,452</b>	<b>1,513</b>
Non-Cash Wkg. Capital	(27.1)	(29.0)	(35.8)	(33.4)	(34.3)
Net Cash/(Debt)	(511)	(514)	(556)	(547)	(527)
<b>Ratio</b>					
Current Ratio (x)	0.4	1.5	0.4	0.7	0.9
Quick Ratio (x)	0.4	1.5	0.4	0.7	0.9
Aggregate Leverage (%)	37.1	38.0	43.0	42.4	41.6

Source: Company, DBS Bank Ltd

## Keppel Pacific Oak US REIT

## Cash Flow Statement (US\$m)

FY Dec	2021A	2022A	2023A	2024F	2025F
Pre-Tax Income	90.3	48.0	(98.7)	43.2	44.7
Dep. & Amort.	0.0	0.0	0.0	0.0	0.0
Tax Paid	0.0	0.0	0.0	0.0	0.0
Associates & JV Inc/(Loss)	0.0	0.0	0.0	0.0	0.0
Chg in Wkg.Cap.	1.77	2.38	6.32	(2.4)	0.91
Other Operating CF	(9.1)	29.0	177	1.14	1.32
<b>Net Operating CF</b>	<b>82.9</b>	<b>79.4</b>	<b>84.2</b>	<b>42.0</b>	<b>46.9</b>
Net Invt in Properties	(131)	(43.6)	(46.7)	(32.7)	(27.8)
Other Invt (net)	0.0	35.9	0.0	0.0	0.0
Invt in Assoc. & JV	0.0	0.0	0.0	0.0	0.0
Div from Assoc. & JVs	0.0	0.0	0.0	0.0	0.0
Other Investing CF	0.07	0.15	0.82	0.0	0.0
<b>Net Investing CF</b>	<b>(131)</b>	<b>(7.6)</b>	<b>(45.9)</b>	<b>(32.7)</b>	<b>(27.8)</b>
Distribution Paid	(65.5)	(58.0)	(55.1)	0.0	0.0
Chg in Gross Debt	43.0	15.1	21.7	16.4	13.9
New units issued	64.1	0.87	0.0	0.0	0.0
Other Financing CF	0.0	(17.3)	(24.6)	0.0	0.0
<b>Net Financing CF</b>	<b>41.6</b>	<b>(59.3)</b>	<b>(58.0)</b>	<b>16.4</b>	<b>13.9</b>
Currency Adjustments	0.0	0.0	0.0	0.0	0.0
Chg in Cash	(6.3)	12.5	(19.7)	25.6	33.0
Operating CFPS (US cts.)	7.80	7.37	7.46	4.21	4.31
Free CFPS (US cts.)	(4.6)	3.42	3.59	0.88	1.79

Source: Company, DBS Bank Ltd

## Target Price &amp; Ratings 12-mth History



Note: Share price and Target price are adjusted for corporate actions.

S.No.	Date of Report	Closing Price	12-mth Target Price	Rating
1:	21 Jun 23	0.31	0.48	BUY

Source: DBS Bank Ltd

Analysts: Rachel TAN

Derek TAN

DBS Bank Ltd recommendations are based on an Absolute Total Return\* Rating system, defined as follows:

**STRONG BUY** (>20% total return over the next 3 months, with identifiable share price catalysts within this time frame)

**BUY** (>15% total return over the next 12 months for small caps, >10% for large caps)

**HOLD** (-10% to +15% total return over the next 12 months for small caps, -10% to +10% for large caps)

**FULLY VALUED** (negative total return, i.e., > -10% over the next 12 months)

**SELL** (negative total return of > -20% over the next 3 months, with identifiable share price catalysts within this time frame)

\*Share price appreciation + dividends

Completed Date: 16 Feb 2024 06:13:09 (SGT)

Dissemination Date: 16 Feb 2024 07:13:23 (SGT)

Sources for all charts and tables are DBS Bank Ltd unless otherwise specified.

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### DBS Regional Research Offices

#### HONG KONG

##### DBS Bank (Hong Kong) Ltd

Contact: Dennis Lam  
13th Floor One Island East,  
18 Westlands Road,  
Quarry Bay, Hong Kong  
Tel: 852 3668 4181  
Fax: 852 2521 1812  
e-mail: dbsvhk@dbs.com

#### SINGAPORE

##### DBS Bank Ltd

Contact: Andy Sim  
12 Marina Boulevard,  
Marina Bay Financial Centre Tower 3  
Singapore 018982  
Tel: 65 6878 8888  
e-mail: groupresearch@dbs.com  
Company Regn. No. 196800306E

#### INDONESIA

##### PT DBS Vickers Sekuritas (Indonesia)

Contact: Maynard Priajaya Arif  
DBS Bank Tower  
Ciputra World 1, 32/F  
Jl. Prof. Dr. Satrio Kav. 3-5  
Jakarta 12940, Indonesia  
Tel: 62 21 3003 4900  
Fax: 6221 3003 4943  
e-mail: indonesiaresearch@dbs.com

#### THAILAND

##### DBS Vickers Securities (Thailand) Co Ltd

Contact: Chanpen Sirithanarattanakul  
989 Siam Piwat Tower Building,  
9th, 14th-15th Floor  
Rama 1 Road, Pathumwan,  
Bangkok Thailand 10330  
Tel. 66 2 857 7831  
Fax: 66 2 658 1269  
e-mail: research@th.dbs.com  
Company Regn. No 0105539127012  
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