Manulife US REIT

PRESS RELEASE

U.S. economic outlook improving; MUST lowers unencumbered gearing ratio, focuses on negotiations with lenders to bolster liquidity

- **1H 2023 distributions halted; negotiations underway for waiver of breach of unencumbered gearing ratio**
- **Portfolio occupancy at 85.1%; leases signed at +3.7% rent reversion, with WALE of 7.6 years in 1H 2023**
- **Executed 443,000 sq ft of leases, or 8.3% of portfolio NLA, in 1H 2023**
- **MAS' aggregate gearing ratio at 56.7% due to 14.6% decline in portfolio valuation; not considered a breach**
- **Working to generate proceeds to repay indebtedness including seeking disposal mandate**

Singapore, 14 August 2023 – Manulife US Real Estate Investment Trust ("MUST") reported a gross revenue of US$99.6 million for the half year ended 30 June 2023 ("1H 2023"), which was 0.8% lower year-on-year (YoY) from 1H 2022. Net property income (NPI) dipped 3.9% YoY to US$55.4 million, while distributable income (DI) decreased 17.4% YoY to US$37.9 million. This was largely due to lower rental and recoveries income from higher vacancies across the portfolio along with the sale of Tanasbourne in April 2023, coupled with higher property operating expenses such as repair and maintenance, property taxes and utilities as well as higher finance expenses. This was partially offset by higher lease termination fee income and higher parking income.

The distributions for 1H 2023 will be halted due to (i) the previously disclosed breach of a financial covenant in some of MUST's financing documents relating to the ratio of consolidated total unencumbered debt to consolidated total unencumbered assets[1], resulting in all of the REIT's loans reclassified as current liabilities, and (ii) the fact that the Manager would not be able to certify that it is satisfied on reasonable grounds that, immediately after making the distribution, MUST will be able to fulfil, from the deposited property of the property fund, its liabilities as they fall due[2]. The Manager is working to generate proceeds to repay upcoming loan maturities, and fund capital expenditure (capex) and leasing costs[3].

	1H 2023 (US$'000)	1H 2022 (US$'000)	Change (%)
Gross Revenue	99,568	100,418	(0.8)
Net Property Income	55,361	57,622	(3.9)
Distributable Income	37,948	45,966	(17.4)
Distribution Amount[4]	-	45,966	N.A.
DPU (US cents)[4]	-	2.61	N.A.

[1]The financial covenant in MUST loan agreements provides that the ratio of consolidated total unencumbered debt to consolidated total unencumbered assets shall be not more than 60:100.
[2] Under the Property Funds Appendix, if Manulife US REIT were to declare a distribution in excess of profits, the Manager must certify that MUST is able to fulfil its liabilities as they fall due, after making distributions in excess of its profits.
[3] MUST is not able to incur additional borrowings since it has exceeded the aggregate leverage limit stipulated by the Property Funds Appendix due to a depreciation in asset valuations.
[4]1H 2023 distribution halted due to breach of banks' unencumbered gearing ratio; all loans reclassified as current liabilities.

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Mr Tripp Gantt, Chief Executive Officer of MUST, said, “Together with our Sponsor, we are negotiating with our lenders to address the breach and embark on a plan to bolster MUST’s liquidity needs, be it the potential disposition of Phipps Tower or a potential alternative method. We are tackling the problem systematically to raise funds to pay down debt and fund essential capex, including leasing costs such as tenant incentives. Concurrently, we are pursuing a disposition mandate, subject to Unitholders' approval, to sell a certain amount of assets within set parameters to generate liquidity. All this is occurring against the backdrop of our ongoing strategic review, where we continue to engage with potential partners who are evaluating options such as asset sales, capital injection and strategic transactions around the REIT platform. We hope to share positive developments with the market soon.”

Capital management: Unencumbered gearing ratio lowered
MUST has lowered its bank unencumbered gearing ratio to 59.7%, from 60.2% (which was above the limit of 60%), via a good faith payment in August 2023. However, lowering the unencumbered gearing ratio in itself does not rectify the breach of the financial covenant. Once a breach has occurred, the lenders need to expressly waive the breach. These negotiations are ongoing.

As at 30 June 2023, MUST’s aggregate leverage ratio is 56.7%. According to the Monetary Authority of Singapore’s Property Funds Appendix, this is not considered a breach of the Property Funds Appendix as it had occurred due to a decline in portfolio valuation, which is beyond the Manager’s control. MUST’s interest coverage has declined to 2.6 times, from 2.9 times as at 31 March 2023, while its weighted average debt maturity stood at 2.5 years as at end-June 2023. Rising interest rates pushed MUST’s weighted average interest cost slightly higher to 4.10%, from 3.98% three months ago, while the percentage of fixed rate loans has held steady at 80.2%. MUST’s net asset value per unit is US$0.40 as at the end of June 2023, mainly due to its fair value loss on investment properties.

Portfolio performance: Positive rent reversion, long wale for 1H 2023 leases
While MUST’s occupancy declined slightly to 85.1% as at 30 June 2023, largely due to non-renewals at Diablo and Capitol, it saw positive rent reversions of +3.7% in the first half of 2023. ~443,000 sq ft of leases, representing ~8.3% of the portfolio net lettable area (NLA), has been executed. The bulk of this comprised renewals (~82.3%), while new leases made up ~13.8%, and expansions the remaining 3.8%. 6.3% of leases by NLA is expiring in 2023, with another 15.4% coming due in 2024. Long leases with WALEs averaging 7.6 years were signed in the first half of the year. As at end-June 2023, the portfolio weighted average lease expiry (WALE) by NLA stood at 4.9 years.

Post 30 June 2023, the Manager has also executed four leases totalling ~20,000 sq ft, including an expansion at Michelson, a renewal at Peachtree and two new deals at Phipps and Capitol, respectively. The leasing pipeline comprises 1.6 million sq ft of potential tenants from industries such as Finance & Insurance, Legal, Retail, and Information. The Manager has also announced the early termination by The Children’s Place at Plaza. The children apparel retailer is vacating its 197,949 sq ft of space on 31 May 2024 and has paid a termination penalty of ~US$4 million. It will continue to pay rent until the date it vacates.

As announced on 18 July 2023, the real estate valuation of MUST's portfolio has declined by 14.6% to US$1,633.6 million as at end-June 2023, from US$1,913.5 million as at 31 December 2022. This was due to higher discount (+ ~50 bps) and terminal cap rates (+ ~40 bps) since December 2022, reflecting market risks such as the lack of debt availability, a potential recession, net selling of U.S. office properties, as well as the continued softening of office demand, reflected by higher vacancy levels and leasing cost assumptions.

MUST’s portfolio valuation decline was in line with various U.S. office benchmarks which continued to deteriorate in 2Q 2023. The National Council of Real Estate Investment Fiduciaries (NCREIF)

Office Subindex recorded a 18.4% decline in market values YoY[5], while the Green Street Commercial Property Price Index for office declined 27% YoY[6] in 2Q 2023. Furthermore, notable office defaults and write-downs by U.S. property funds since January 2023 have been fuelling concerns of a commercial real estate debt crisis. MSCI Real Assets also reported that offices comprised more than four-fifths of US$6.7 billion of distressed assets added in 2Q 2023[7].

MUST's well-diversified tenant base comprises numerous multinational corporations across more than 16 different trade sectors. All its top 10 tenants are either public-listed companies, government agencies or corporate headquarters. As at 30 June 2023, no single tenant contributed more than 4.6% of gross rental income.

U.S. market outlook

Real GDP in the U.S. is showing signs of stabilising and may be rebounding, as evidenced by annual growth rates of 2.0% and 2.4% in 1Q and 2Q 2023, respectively. The U.S. labour market continues to be healthy, with unemployment at 3.5% as of July 2023. The Federal Reserve, in its continued effort to combat inflationary pressures, has kept its monetary stance by raising policy rates by an additional 100 basis points since the start of 2023. As a result, inflation is showing signs of alleviation. After peaking at a 9.1% annual rate in June 2022, inflation declined to 3.2% annual growth in July 2023. In addition to the Federal Reserve's monetary policy, other factors that have contributed to inflation began to show signs of easing, including supply chain constraints, pandemic restrictions, energy prices and consumer spending.

In terms of leasing demand and velocity in 2Q 2023, there were mixed signals. JLL's figures showed the U.S. office market indicating encouraging signs with an increase of 11.6% in leasing activity QoQ. On the other hand, CBRE's data showed that leasing activity fell by 3% in the same period. Focusing solely on MUST's submarkets only, JLL's data showed leasing activity growth of 8.2% QoQ, although this was well below historical averages. Despite 2Q 2023's green shoots, occupancy has continued to decline in the first half of 2023, with JLL's data showing negative net absorption of 33.2 million sq ft, leaving the national occupancy rate at 79.4%, down from 80.4% at 4Q 2022. Sublease space is at a historical high, up almost 25% YoY, with 194 million sq ft available, according to CBRE. This accounts for ~19% of available space and ~5% of total office inventory, adding to the pressures on occupancy.

Looking forward

With committed occupancy of 85.1% and a long WALE of 4.9 years, MUST's portfolio remains well-positioned to withstand additional market uncertainty from a slowing economy or weak occupational market in the office sector. The Manager continues to focus on asset, lease, and capital management, in addition to its commitment to sustaining and enhancing environmental, social and governance (ESG) to deliver long-term value to Unitholders.

The Manager is currently in negotiations with lenders to address the breach of financial covenant and bolster liquidity. It continues to pursue a disposition mandate to sell assets to reduce indebtedness and fund capex, while evaluating potential strategic options to recapitalise the balance sheet of the REIT.

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[5] Source: National Council of Real Estate Investment Fiduciaries (NCREIF), NCREIF Property Index. Based on more than 1,720 office properties worth over US$210 billion. Each property's market value is determined by real estate appraisal methodology, consistently applied.

[6] Source: Green Street Advisors, LLC, Green Street's Commercial Property Price Index® is a time series of unleveraged U.S. commercial property values that captures the prices at which commercial real estate transactions are currently being negotiated and contracted.

[7] Source: MSCI, 21 Jul 2023: Distress in US Commercial Property Increased Further - MSCI

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About Manulife US REIT

Manulife US Real Estate Investment Trust ("Manulife US REIT" or "MUST") is the first pure-play U.S. office REIT listed in Asia. It is a Singapore listed REIT established with the investment strategy principally to invest, directly or indirectly, in a portfolio of income-producing office real estate in key markets in the United States ("U.S."), as well as real estate-related assets. MUST's portfolio comprises 11 freehold office properties in Arizona, California, Georgia, New Jersey, Virginia and Washington D.C. The current portfolio has an aggregate net lettable area of 5.3 million sq ft and is valued at US$1.6 billion as at 30 June 2023.

About the Sponsor – The Manufacturers Life Insurance Company ("Manulife")

Manulife is part of a leading Canada-based financial services group with principal operations in Asia, Canada and the United States. The Sponsor operates as John Hancock in the U.S. and as Manulife in other parts of the world, providing a wide range of financial protection and wealth management products, such as life and health insurance, group retirement products, mutual funds and banking products. The Sponsor also provides asset management services to institutional customers. Manulife Financial Corporation is listed on the Toronto Stock Exchange, the New York Stock Exchange, the Hong Kong Stock Exchange and the Philippine Stock Exchange.

About the Manager – Manulife US Real Estate Management Pte. Ltd.

The Manager is Manulife US Real Estate Management Pte. Ltd., an indirect wholly-owned subsidiary of the Sponsor. The Manager's key objectives are to provide Unitholders with regular and stable distributions and to achieve long-term growth in DPU and NAV per Unit, while maintaining an appropriate capital structure.