21 August 2020

kopi-C: the Company brew

United Hampshire US REIT: Recession-Proof Resilience

Renaissance painter and sculptor Michelangelo famously said - at the ripe old age of 87 - "Ancora Imparo" or "I am still learning", and the same goes for Robert Schmitt, whose career is a powerful testimony to that motto.

"The proverb 'You can't teach an old dog new tricks' is very last year," said the 56-year-old CEO of the manager of SGX-listed United Hampshire US REIT.

"What's the point of doing what you are doing, if you are not learning, experiencing new things, or challenging yourself every day? It's never too late, and I assure you, old dogs can certainly pick up new tricks!" he laughed.

Schmitt, a self-confessed numbers person, transitioned from an early career in infrastructure engineering to real estate and fund management, all because he wanted to try something different.

"After a few years at the drafting table, I was going crazy looking at formulas and crunching numbers all day, and it was then that I realised I didn't want to be an engineer anymore. So I went back to school to get my MBA," recalled the Bachelor of Science in Civil and Environmental Engineering graduate from Clarkson University.

Armed with an MBA in Finance from Boston University, Schmitt moved into the real estate industry in 1991, taking on the role of Asset Manager with Legg Mason Real Estate Advisors. There was no looking back after that.

"Real estate works for me because of its diversity - you're involved in different aspects of the business, ranging from finance and lending to investor relations and tenant management," he noted.

"And tenants are the lifeblood of real estate - without leases, commercial buildings have no value. Tenants create cashflow, and cashflow is what real estate is all about," he added.

"Because tenants come in all shapes and sizes from various sectors, they each have their own particular story. So you're always learning something new about another business and another industry that you can apply to your own."

Defensive Stability

In 1995, Schmitt moved to The Hampshire Companies. He rose through the ranks to become Principal, serving as the Fund Manager of Hampshire's Core Plus Fund Platform that consisted primarily of retail and industrial properties, with an aggregate asset value in excess of US$1 billion.

Prior to assuming his role as CEO of United Hampshire US REIT, he served on Hampshire's Senior Leadership Team, an internal governing body that establishes and implements strategy and policy to support the company's mission of organisational excellence.

Schmitt's years in The Hampshire Companies proved to be a solid training ground. "The key takeaway from managing a fund is the importance of cashflow, and the ability to balance risks with growth. Communicating with investors and establishing trust with a variety of stakeholders is also critical," he said.

"Trust is very difficult to obtain. Once obtained, if you mess up, it's really easy to lose it. And open, honest communication is one of the key ways to build that trust."

Listed on the Mainboard of Singapore Exchange in March 2020, United Hampshire US REIT (UHU REIT) has the strategy of investing in a diversified portfolio of stabilised income-producing, grocery-anchored and necessity-based retail properties, as well as modern, climate-controlled self-storage facilities, located in the US.

Targeted tenants for its assets include those resilient to the impact of e-commerce, such as restaurants, discounters, home-improvement stores, fitness centres, warehouse clubs, and operators with strong physical and digital distribution platforms.

The REIT's initial portfolio comprises 22 predominantly freehold Grocery & Necessity properties as well as Self-Storage assets, concentrated in Northeastern US, with an appraised value of approximately US$599.2 million, and an aggregate net lettable area of about 3.17 million square feet.

"This isn't a high-risk portfolio - it basically produces a stable income or yield over time, and incorporates moderate risk to generate some growth," Schmitt pointed out.

Tenant Stickiness

The advantages are obvious - consumption accounts for about two-thirds of the US economy, and grocery-anchored centres provide direct access to the consumer's wallet.

"Whether you make US$40,000 or US$200,000 a year, you still buy groceries," he added. "Both segments are also relatively recession-proof, and these are the assets and tenants best suited to the current economic climate."

Grocery & Necessity assets offer stable cashflow with long leases - the weighted average lease expiry (WALE) is 8.4 years on base rental incomes. As at 30 June 2020, occupancy levels stood at 95%, while tenant retention rates over the past year ended 30 September 2019 are holding above 97%. More than 80% of existing Grocery & Necessity leases also have built-in rental escalations.

Focused on leading anchors in growing sectors, the top 10 tenants include the largest grocers, wholesalers, home-improvement and discount retailers in the US, such as Walmart, Home Depot USA, as well as Ahold Delhaize, whose brands include Stop & Shop and Giant Food.

Likewise, Self-Storage is billed as one of the fastest-growing sectors in the US. Same-store net operating income has expanded at a compound annual growth rate (CAGR) of 4.6% over the last 24 years, outpacing inflation and major US property sectors by 2.4% and 1.8% respectively, according to independent market research data.

"Obviously this segment is not going to continue growing at this pace forever, but the outlook remains bullish due to high barriers to entry," Schmitt noted.

"Americans generally live in small homes, but they have a propensity to buy and store a lot of extra stuff that they may not end up using. Once that's placed in storage, it's not taken out often, which leads to tenant stickiness."

Also stoking demand for self-storage assets are specific life events, such as divorce, job disruptions, economic dislocations, even death, he added. "With self-storage assets now mostly situated in traditional retail locations, synergies with the retail sector have increased, and we will continue to see more of that."

Ticking the Right Boxes

Meanwhile, the portfolio's e-commerce resistant characteristics enhances the REIT's defensiveness. "E-commerce is real, it's happening, and we're not in denial. But online purchases of groceries - including fresh vegetables and produce - command a relatively small share of the e-commerce market, estimated at about 2%, as compared to say, apparel or furniture. This is because of deep-rooted consumer attitudes - most Americans prefer to pick their food before they buy."

Another factor is prohibitively high last-mile logistics and delivery costs, particularly in the far-flung, suburban US markets with lower density populations. This makes the brick-and-mortar stores convenient locations for fulfillment of both physical as well as online orders, he added.

"E-commerce will grow, but not at the expense of the physical stores, which are already incorporating omni-channel strategies - embracing multiple channels of distribution, including BOPIS, or Buy Online and Pick-up In Store."

UHU REIT will also focus more on tenants that offer experiential types of services and facilities, such as pet stores, doggy day care, and even preloved luxury clothing retailers that offer buyers the thrill - akin to a treasure hunt - of discovering a hugely discounted branded item. "For such services, you would definitely require a brick-and-mortar presence."

The portfolio's focus on the densely populated and affluent Northeastern US markets also lends an edge. "The Northeast is the most mature and developed part of the US in terms of population density and household income - it has 24% higher spending power per square feet of retail space, but 28% lower retail square feet per capita, and 38% lower supply growth, as compared to the US top 50 average," he pointed out.

"The right combination for each asset centres on having a dominant anchor grocer in a suburban location, with the competition already present, so that there's no opportunity for them to break in later on - this creates high barriers to entry. Each location would also have the right infrastructure and transportation networks in place - this is why we started in the Northeast, which has ticked all the right boxes."

Discipline and Prudence

UHU REIT is also open to the idea of venturing beyond this geography into other populous and affluent markets in the US, though the REIT's focus still remains in the Northeast and Southeast regions.

"We're cautiously seeking new opportunities, focusing on states with strong buying power and economic drivers. The key is to be disciplined with our acquisition criteria, and not stray too far from what has made us successful."

In the meantime, recognising the difficult business environment caused by the outbreak, UHU REIT has been working closely with its retail tenants to provide short-term rental relief on a case-by-case basis. For certain tenants, rent relief was granted in exchange for lease extensions.

The Manager also actively supports its tenants through initiatives that include designating selected parking spaces at its properties for curbside pick-up, and permitting new outdoor dining areas, thus enabling tenants to set up outdoor tents.

While cases have recently spiked up in other states, primarily in the south and western regions, UHU REIT's properties in those areas are not located in the hot spots and remain open for business. As the status of the outbreak and various regional guidelines regarding loosening of restrictions on businesses remain fluid, the REIT Manager will continue to monitor the situation closely.

Meanwhile, UHU REIT's disciplined capital structure and prudent capital management strategy stands it in good stead, Schmitt noted. The REIT's aggregate leverage remains comfortable at 36.2%, with an interest coverage ratio of 6.1 times. The REIT had earlier entered into interest rate swaps to hedge the floating rate of its term loan facilities into fixed rates, which removes any near-term interest rate risk.

"We believe the REIT will continue to remain resilient due to our tenant profile, which comprises mostly essential businesses, and the suburban locations of our properties," he added. "Over the medium to longer term, we might also see more of a flight to suburbs by city dwellers as work-from-home arrangements continue to evolve."

When the father of two boys and a girl - aged 21 to 26 - is not managing the REIT's operations, he's focused on family.

His life's mantra - which he wants his children to remember - is to embrace change and recalibrate. That's because, as English singer-songwriter and Beatles founder John Lennon succinctly pointed out, "Life is what happens when you're busy making other plans."

"Yes you can get frustrated, you can get upset, but let's face it, life never goes the way you think it will. If you can't achieve what you want now, you will need to pivot, and be patient," he added.

"This is the true test of character - how you deal with setbacks, how quickly you're able to jump back on that horse and move on."

United Hampshire US REIT

Listed on the Mainboard of Singapore Exchange on 12 March 2020, United Hampshire US REIT is a Singapore real estate investment trust established with the principal investment strategy of investing in a diversified portfolio of stabilised income-producing (i) grocery-anchored and necessity-based retail properties, and (ii) modern, climate-controlled self-storage facilities, located in the US. The tenants targeted by United Hampshire US REIT are tenants resilient to the impact of e-commerce, including but not limited to restaurants, home improvement stores, fitness centers, warehouse clubs and other uses with strong omni-channel platforms. The initial portfolio of United Hampshire US REIT comprises 22 predominantly freehold Grocery & Necessity Properties, and Self-Storage Properties, primarily concentrated in the Northeast markets of the US, with an appraised value of approximately US$599.2 million and an aggregate net lettable area of approximately 3.17 million square feet.

The company website is: **uhreit.com.**

Click **here** for the company's StockFacts page.

For reporting period 12 March 2020 (IPO date) to 30 June 2020, click **here**.

About kopi-C: the Company brew

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Photo: Company file

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