GCR RATINGS

Credit Rating Announcement

GCR upgrades Equites' rating to AA-(ZA)/ A1+(ZA) on sustained strong portfolio performance amidst the ongoing coronavirus pandemic

Rating Action

Johannesburg, 19 August 2021 – GCR Ratings ("GCR") has upgraded the national scale long and short-term issuer ratings of Equites Property Fund Limited ("Equites" or "the REIT") to AA-(ZA) and A1+(ZA), from A+(ZA) and A1(ZA) respectively. The Outlook has been revised to Stable from Positive previously.

Rated Entity / Issue	Rating class	Rating scale	Rating	Outlook / Watch
Equites Property Fund Limited	Long Term Issuer	National	AA-(ZA)	Stable Outlook
	Short Term Issuer	National	A1+(ZA)	

Rating Rationale

The upgrade to Equites' rating reflects the sustained improvement in portfolio quality, supported by positive externalities impacting the logistics sector as the domestic operating environment still faces pandemic related tailwinds. This has been characterised by growth in rental income, elimination of vacancies and stability of margins, notwithstanding its ongoing property development strategy.

The REIT has a growing property portfolio which was valued at R18.9bn at FY21 (FY20: R14.5bn), with 95% comprising A-grade, blue-chip tenants. The strong tenant profiles coupled with a boom in demand for logistics space in both the South African and UK markets sustained robust performance. The weighted average lease expiry improved significantly to 15.4 years (FY20: 10.2 years), while escalations for the SA portfolio remain comfortably above inflation, which together with the continuous completion of developments and acquisitions will continue to be the driving force behind growth in rental income. Although sector and tenant concentration are noted as constraints to the assessment, the diversity of tenants' business lines and persistently strong collection rates that averaged above 99% throughout the pandemic, mitigate these risks. Vacancies were reduced to below 1% of the portfolio from 3.4% previously, while margins are expected to remain stable owing to the triple-net-lease operating structure.

Equites' financial profile is characterised by rising gross debt, which was reported at R6.8bn (FY20: R4.8bn) and is channelled to fund growth through developments and acquisitions. Nonetheless, traditional leverage metrics such as the LTV and interest cover remain well managed and are forecast to remain in the 30%-35% and 3.0-3.5x range respectively, with comfortable headroom relative to covenant limits. GCR's calculated net debt to operating income ratio of 6.6x (FY20: 6.2x), remains relatively elevated as development funding is acquired upfront while the cash flows are only realised upon completion of the construction work. Shareholders have demonstrated support through the successful R1bn accelerated book build in July 2021 and would be expected to back an additional equity raise in the short term given the current value of the REIT's share price relative to net asset value. The REIT has historically managed to refinance debt ahead of its maturity and the DMTN programme has added to the diversity of funding sources available.

Liquidity cover is underpinned by funds made available through the recently completed book build, and strong access to funding through both debt and equity markets, where the REIT is building a good track record. Furthermore, Equites has capacity to generate strong cash flows from rental income and asset disposals. GCR estimates a uses versus sources coverage ratio of 1.3x over the coming 12 months. This is set to improve with the impending refinancing of some existing facilities in August 2021, which will see debt maturities termed out by a further three to five years.

Outlook Statement

The Stable outlook reflects the expectation that the REIT's portfolio quality will remain resilient relative to peers, backed by high occupancy rates with high quality tenants and largely pre-let development-led growth. Proactive management of the financial profile is expected to maintain the LTV ratio at the top end of the 30%-35% range, while earnings-based gearing is expected to improve over the long run.

Rating Triggers

The rating may be upgraded if Equites 1) increases its exposure to more stable and developed markets, while maintaining the quality of assets and tenants and increasing portfolio diversity, or 2) achieves a sustained moderation of the net debt to operating income and LTV ratios.

Negative rating action is considered unlikely, however, it may be triggered by an unexpected decline in portfolio quality or deterioration of the leverage profile.

Analytical Contacts

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Related Criteria and Research

Criteria for the GCR Ratings Framework, May 2019
GCR Rating Scales Symbols and Definitions, May 2019
Criteria for Rating Real Estate Investment Trusts and Other Commercial Property Companies, May 2019
GCR's Country Risk Score report, July 2021
GCR's Property Sector Risk Score report, March 2021

Ratings History

Equites Property Fund Limited

Rating class	Review	Rating scale	Rating	Outlook/Watch	Date
Long Term Issuer	Initial	National	A(ZA)	Stable Outlook	October 2018
Short Term Issuer		National	A1(ZA)		
Long Term Issuer	Last	National	A+(ZA)	Positive Outlook	September 2020
Short Term Issuer		National	A1(ZA)		

Risk Score Summary

Rating factors and sub-factors	Risk scores
Operating environment	**15.50**
Country risk score	8.75
Sector risk score	6.75
Business profile	**0.75**
Portfolio quality	0.75
Management and governance	0.00
Financial profile	**(1.00)**
Leverage and Capital Structure	(0.50)
Liquidity	(0.50)
Comparative profile	**0.00**
Group support	0.00
Peer analysis	0.00
Total Score	**15.25**

Glossary

Asset	A resource with economic value that a company owns or controls with the expectation that it will provide future benefit.
Bond	A long-term debt instrument issued by either a company, institution or the government to raise funds.
Diversification	Spreading risk by constructing a portfolio that contains different exposures whose returns are relatively uncorrelated. The term also refers to companies which move into markets or products that bear little relation to ones they already operate in.
Interest Cover	Interest cover is a measure of a company's interest payments relative to its profits. It is calculated by dividing a company's operating profit by its interest payments for a given period.
Interest	Scheduled payments made to a creditor in return for the use of borrowed money. The size of the payments will be determined by the interest rate, the amount borrowed or principal and the duration of the loan.
Issuer	The party indebted or the person making repayments for its borrowings.
Leverage	With regard to corporate analysis, leverage (or gearing) refers to the extent to which a company is funded by debt.
Liquidity	The speed at which assets can be converted to cash. It can also refer to the ability of a company to service its debt obligations due to the presence of liquid assets such as cash and its equivalents. Market liquidity refers to the ease with which a security can be bought or sold quickly and in large volumes without substantially affecting the market price.
Long Term Rating	See GCR Rating Scales, Symbols and Definitions.
Margin	A term whose meaning depends on the context. In the widest sense, it means the difference between two values.
Maturity	The length of time between the issue of a bond or other security and the date on which it becomes payable in full.
Portfolio	A collection of investments held by an individual investor or financial institution. They may include stocks, bonds, futures contracts, options, real estate investments or any item that the holder believes will retain its value.
Rating Outlook	See GCR Rating Scales, Symbols and Definitions.
REIT	Real Estate Investment Trust. A company that owns, operates or finances income-producing real estate.
Rent	Payment from a lessee to the lessor for the temporary use of an asset.
Short Term Rating	See GCR Rating Scales, Symbols and Definitions.
Weighted Average	An average resulting from the multiplication of each component by a factor reflecting its importance or, relative size to a pool of assets or liabilities.

Salient Points of Accorded Ratings

GCR affirms that a.) no part of the ratings process was influenced by any other business activities of the credit rating agency; b.) the ratings were based solely on the merits of the rated entity, security or financial instrument being rated; and c.) such ratings were an independent evaluation of the risks and merits of the rated entity, security or financial instrument.

The credit ratings have been disclosed to Equites Property Fund Limited. The ratings above were solicited by, or on behalf of, the rated entity, and therefore, GCR has been compensated for the provision of the ratings.

Equites Property Fund Limited participated in the rating process *via* face-to-face management meetings, teleconferences and other written correspondence. Furthermore, the quality of information received was considered adequate and has been independently verified where possible. The information received from Equites Property Fund Limited and other reliable third parties to accord the credit ratings included:

- The 2021 audited annual financial statements (plus four years of audited comparative numbers)
- The latest integrated report
- A breakdown of utilised and available debt facilities at 31 July 2021
- Analyst Presentations, SENS announcements and roadshows
- 2-Year forecasts
- Property portfolio breakdown at July 2021