GCR RATINGS

CREDIT RATING ANNOUNCEMENT

GCR affirms Equites Property Fund Limited's issuer rating of AA-(ZA), Stable Outlook

Rating action

Johannesburg, 26 June 2024 – GCR Ratings (GCR) has affirmed the national scale long and short-term issuer ratings of Equites Property Fund Limited (Equites or the REIT) at AA-(ZA) and A1+(ZA), respectively. The Outlook is Stable.

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

Equites' ratings reflect its strong income generation from a growing portfolio of high-quality logistics assets that is moderately diversified geographically. The REIT's current growth strategy centres solely on its sizeable South African development pipeline, with financial leverage expected to remain moderate through the ongoing application of planned sale proceeds.

Equites' portfolio continues to show strong operational metrics and has repositioned more towards South Africa following management's decision in the prior financial year to partially rotate out of the UK. As such, the REIT has progressed well with its planned disposals, with a significant ZAR3.6 billion (including land) in the UK and ZAR1.2 billion in South Africa concluded by financial year end 29 February 2024, and a further c.ZAR2.2 billion that could materialise in financial 2025. Positively, sale values have on average been close to book value. At the same time, the REIT's strategy remains centred on reinvesting the proceeds into new South African developments aligned with clearly articulated ESG strategic objectives, with growth on average of ZAR1 billion per annum envisioned over the medium term. While the high level of development activity does imply some additional risk, this is mitigated by the high pre-leasing and quality of tenants, as well as flexibility in structuring the development funding via joint ventures. Combined with the portfolio valuation uplifts, Equites' investment property portfolio value grew to ZAR28.4 billion (USD1.6 billion) in financial 2024, from ZAR27.6 billion in financial 2023.

The REIT's properties are modern and well-located in connectivity nodes across key trade hubs in South Africa and the UK. Equites has maintained high occupancies (nil at financial 2024), supported by sustained high demand fundamentals in the logistics sector and the high ESG credentials of its properties. This has also underpinned strong tenant credit quality, which together with some shared asset ownership partially mitigates some of the tenant concentration risk evident. The visibility and stability of rental income is supported by the portfolio's long weighted average lease expiry profile of 12.6 years, and average escalation rate of 6.2% in South Africa. On account of the growth in the portfolio size, and triple-net lease nature, net property-related income has remained robust, increasing by 13% in financial 2024 (5-year CAGR: 24%).

Equites' LTV is expected to remain moderately higher than previously estimated, but just below 40%. GCR expects that the already-committed or engaged asset sales will be used to fund the ongoing development activity and partially deleverage. While Equites has a strong track record of accessing both the debt and equity markets, we believe that raising equity capital amidst the current financial climate will remain limited. Interest coverage will remain pressurised at around 2.2x over the next 12-18 months, given the high interest rate environment and as the portfolio is in transition as income producing assets are sold and newly completed buildings are tenanted.

Equites' debt maturities are well spread, with no more than 23% maturing in any year. Moreover, the REIT has demonstrated consistent unsecured debt capital market access and should continue to receive high appetite for refinancing maturing notes. To this end, we positively note the high level of unencumbered properties (50.6% in financial 2024) which can support liquidity via sales or raising secured bank debt. Our liquidity coverage ratio, as determined by near-term sources and uses of funds over the next 12 months, is adequate at 1.3x, albeit that the ongoing need for development funding does imply continued liquidity pressure. As at February 2024, ZAR2.5 billion in debt is maturing in financial 2025, with development spend estimated at around ZAR1.4 billion. Likewise, a large demand on cash comes from maintaining a high dividend payout ratio of 100%, although the REIT has used dividend reinvestment alternative (DRIP) to retain some cash. Sources of liquidity include ZAR2.3 billion in available cash and unutilised committed facilities as at February 2024, DRIP proceeds of ZARR337 million and a conservative estimation of ZAR2.8 billion from the disposal programme (which largely incorporates already sold properties).

Outlook statement

The Stable outlook reflects GCR's view that Equites will continue to benefit from high demand in the resilient logistics segment, supporting strong portfolio growth in South Africa and thus cash flows. Furthermore, we believe the REIT will maintain moderate leverage as it pursues its growth strategy.

Rating triggers

Upward rating progression is only likely over the medium to longer term as Equites increases the scale of its portfolio and maintains strong performance metrics, whilst at the same time achieves sustained lower leverage and strong liquidity.

GCR could lower the rating if the LTV sustains above 40% or if interest coverage falls to or below 2.1x. This could occur if it continues its growth strategy with predominately debt financing or if operating performance unexpectedly weakens. We could also lower the rating if liquidity pressure becomes severe.

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Related criteria and research

Criteria for the GCR Ratings Framework, May 2024
GCR Rating Scales Symbols and Definitions, May 2023
Criteria for Rating Real Estate Investment Trusts and Other Commercial Property Companies, May 2024
GCR Country Risk Score report, June 2024
GCR SA Corporate Sector Risk Score report, March 2024
GCR Commercial Property Sector Risk Score report, June 2023

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	AA-(ZA)	Stable Outlook	July 2023
Short Term Issuer		National	A1+(ZA)		

Risk score summary

Rating Components & Factors	Score
Operating environment	**14.75**
Country risk score	8.25
Sector risk score	6.50
Business profile	**1.00**
Portfolio quality	1.00
Sustainability	0.00
Financial profile	**(0.75)**
Leverage & capital structure	(0.50)
Liquidity	(0.25)
Comparative profile	**0.00**
Group support	0.00
Peer comparison	0.00
Total Risk Score	**15.00**

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 rating

GCR affirms that a.) no part of the rating 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 of the rated entity, security or financial instrument.

The credit ratings have been disclosed to the rated entity. The ratings above were solicited by, or on behalf of, the rated entity.

The rated entity participated in the rating process via in person interaction and/or via online virtual interaction and/or via electronic and/or verbal communication and correspondence. Furthermore, the quality of information received was considered adequate and has been independently verified where possible. The information received from the rated entity and other reliable third parties to accord the credit ratings included:

- Exchange Rate Source: https://www.bloomberg.com/markets/currencies
- The audited annual financial statements to 28 February 2024 (plus four years of audited comparative numbers)
- The 2024 integrated report
- A breakdown of utilised and available debt facilities at February 2024 and June 2024
- Analyst Presentations, SENS announcements and roadshows
- 2-Year cash flow forecasts
- Property portfolio breakdown at February 2024

kind. GCR adopts all necessary measures so that the information it uses in assigning a credit rating is of sufficient quality and from sources GCR considers to be reliable including, when appropriate, independent third-party sources. However, GCR is not an auditor and cannot in every instance independently verify or validate information received in the rating process or in preparing its Publications.

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