

12 APR 2022

Fitch Assigns Growthpoint Properties First-Time IDR 'BB+'; Outlook Stable

Fitch Ratings - London - 12 Apr 2022: Fitch Ratings has assigned Growthpoint Properties Limited a 'BB+' Long-Term Foreign-Currency Issuer Default Rating (FC IDR). The Outlook is Stable. Fitch has also assigned a foreign-currency senior unsecured rating of 'BB+' with a Recovery Rating of 'RR4'. A full list of ratings is detailed below.

The ratings reflect Growthpoint's large, diverse property portfolio, mainly comprising office, industrial and retail assets in South Africa's (SA) largest conurbations. The group has international diversification through equity investments in Australia, the UK and eastern and central Europe (CEE). Cashflow leverage is low, with Fitch-calculated net debt/EBITDA of 5x on a deconsolidated basis at FY21 (year-ending June) or 7x on a reported, consolidated basis.

SA's operating environment remains volatile with long-term economic weakness, which has been exacerbated by the effects of the pandemic. Growthpoint's SA portfolio vacancies were a high 10.5% at end-2021 and passing rents on re-leasing declined around 15%.

Key Rating Drivers

Large, Diverse SA Portfolio: Growthpoint has a strong market position in SA through its wholly-owned property portfolio (excluding assets in funds) valued at around ZAR65 billion (EUR3.9 billion) with more than 400 properties across the office (43%), retail (38%) and industrial (19%) sectors. Properties are spread across the country with 58% of assets by value in Gauteng Province where about a quarter of the SA population lives (mainly in greater Johannesburg and Pretoria). The group holds a 50% interest in V&A Waterfront, a 123-hectare mixed-use property on Cape Town's original harbour. The tenant base is diverse and includes some of SA's largest companies.

Challenging Operating Environment: SA has suffered from a weak economy and recessions for more than a decade, which is exacerbated by the effects of the pandemic. The economy contracted more than 6% in 2020, but is now recovering. Fitch expects GDP to return to pre-pandemic levels by end-2022 despite market volatility. Unemployment remains about 30%.

High Vacancies: The weak economy continues to affect the SA portfolio. Vacancy rate of 10.5% at end-2021 was mainly driven by office vacancies exceeding 20%. Offices are oversupplied as economic volatility has pushed businesses to rationalise space. Low-rise offices in the greater Johannesburg area have average vacancies above 20%, while high-rise offices, mainly in Cape Town, are around 12%. Low-rise offices comprise only around 15% of the total property portfolio. The industrial portfolio, which had a vacancy rate of 6.5% at end-2021, is less oversupplied. Retail vacancies were 4.7% (end-2021) as

the group protected occupancy through tenant incentives.

Declining Rents: Passing rents on re-leasing for the SA portfolio are under pressure, falling by 15%, with an average renewal success rate of 77% in 1HFY22. Passing rents on re-leasing also declined by about 15% in FY21. Leases include average in-force annual escalations of more than 7%, mitigating some of the impact of the declining rents. We expect the retail and industrial portfolios to recover in line with the economy, but the office portfolio to remain challenged due to the acute oversupply.

Deconsolidated Financial Profile: Growthpoint holds majority shares in Growthpoint Australia (GOZ) and UK-based Capital & Regional (C&R), which are separately funded and consolidated into its accounts. Management representation on these entities' boards is limited. The group also owns minority, equity-accounted stakes in V&A Waterfront and Globalworth Real Estate Investment Ltd (Globalworth, BBB-/Stable) in CEE. Fitch has deconsolidated GOZ and C&R, excluding their debt, but including their rental-derived recurring cash dividends and those from other associates.

Stable Dividends from International Investments: Growthpoint owns 62% of GOZ, an ASX-listed REIT owning 57 office and industrial assets; 61% of LSE-listed REIT C&R, which has seven secondary retail properties in the UK; and a 29% share of LSE-listed REIT Globalworth, which owns 66 properties, mainly offices, in Romania and Poland. GOZ, which has low net debt/EBITDA of around 6.0x, generates consistently large dividends that account for around 15% of the group's deconsolidated EBITDA and is uncorrelated to the SA economy and the volatile rand. C&R, which has operational issues and recently restructured its debt, is not currently remitting dividends.

Australia Country Ceiling Applicable: While around 80% of Growthpoint's deconsolidated EBITDA is generated in SA, we have applied the Australian Country Ceiling as hard-currency dividends cover deconsolidated hard-currency gross interest expense by 2.9x, exceeding the minimum 1x under Fitch's Non-Financial Corporates Exceeding the Country Ceiling Criteria. Growthpoint holds offshore accounts for its hard-currency dividend receipts.

Focus on Liquidity Management: Growthpoint has grown mainly through mergers and acquisitions, but, given current market difficulties, is now focused on balance-sheet-and-liquidity management. Development spending and capex in FY21 was limited to ZAR1 billion and acquisitions to ZAR309 million, while the group has disposed of ZAR559 million of assets. Growthpoint also boosted liquidity through a ZAR4.3 billion equity raise, a ZAR557 million dividend reinvestment plan, and a reduced dividend pay-out ratio of 80% compared with historical levels of 100%. SA REITs must pay a minimum dividend of 75% of distributable earnings.

Low Leverage: Growthpoint maintains low cashflow leverage, even considering the high income-yielding domestic portfolio (8.6%). Fitch-calculated deconsolidated FY21 net debt/EBITDA, which includes SA rental income, plus cash dividends from GOZ, Globalworth and V&A, was only 5.0x. Fitch forecasts an average of 5.1x over the next three years as the portfolio recovers and modest development and acquisitions limit new debt. EBITDA interest cover is expected to remain just under 3.0x (FY21: 3.1x). Most of the non-recourse debt for the international investments' activities are secured, but only 43% of SA debt (excluding V&A) is secured, resulting in a deconsolidated

unencumbered investment property assets/unsecured debt of 1.4x.

Derivation Summary

Growthpoint, like many SA peers, has invested abroad to reduce exposure to the volatile rand. It is unlikely to expand into other countries beyond its current exposure to Australia, the UK and eastern Europe, but will focus on refining and optimising its current portfolio. The overseas dividends are positive for Growthpoint's credit profile, contributing stable and predictable income streams with no correlation to the volatile SA economy.

Growthpoint's most comparable domestic peer is Redefine Properties Limited, one of SA's largest real-estate investment trusts (REITs). Like Growthpoint, Redefine has a strong market position, based on a ZAR59 billion property portfolio across office, industrial, retail and specialised assets in the country's largest urban areas. Redefine also has international investments with exposure to Poland through EPP, an office and industrial REIT. The company owns 45% of EPP, but is in the process of taking over the company and is expected to delist the company in March (final ownership percentages remain unclear).

Like Growthpoint, Redefine is predominately exposed to the SA operating environment, which has weakened its operational metrics. Its weighted average lease term is 3.4 years, similar to Growthpoint's, and passing rents have similarly declined at around 16%. Redefine's total vacancy was around 8% compared with around 11% for Growthpoint.

Growthpoint does not have a comparable rated EMEA peer. The combination of retail, office and industrial is unique, although some REITs combine office and retail assets. Growthpoint operates in a more difficult operating environment than most other EMEA REITs, apart from Turkey-based retail REIT Ronesans Gayrimenkul Yatirim A.S. (RGY, B/Stable). The Turkish economy has been weak for several years and is beset by high inflation and a volatile currency. RGY has high exposure to foreign-exchange (FX) risk as most of its debt is denominated in euros or the US dollar, but rents are in Turkish lira, which has pushed net debt/EBITDA to more than 15x.

Growthpoint has a much lower exposure to hard-currency debt than RGY with only around 16% of total deconsolidated debt in hard currency. The rand has also been less volatile than the lira. Turkey does not have the oversupply issue of office and industrial space that the SA market has.

Key Assumptions

Fitch's Key Assumptions Within Our Rating Case for the Issuer

-SA retail rents to stabilise in FY22 and recover to pre-pandemic levels in FY23, in line with the economy. Office rental income continues to see weak performance in the forecast period to FY25, due to chronic oversupply. Stable rents from the industrial portfolio in FY22 and FY23, with rental reversion improving in FY24

-Stable dividends from GOZ during FY22-FY23 and with mild growth in FY24-FY25, given the stable operating environment in Australia

-No dividend contribution from C&R to FY25

-No significant acquisitions to FY25. Capex is largely for refurbishing the SA portfolio. Disposals of non-core assets in FY22 and FY23 on average at ZAR900 million annually, premised on sale agreements signed

-USD425 million bonds maturing May 2023 and other debts to be refinanced

-Dividend pay-out of 80%

RATING SENSITIVITIES

Factors that could, individually or collectively, lead to positive rating action/upgrade:

-Improvement of the SA real estate market, especially for the office sector, such that Growthpoint materially reduces vacancies and increases passing rents

-Improvement in the SA operating environment

-Further material geographic diversity into investment-grade jurisdictions, yielding quality, sustainable cashflows

Factors that could, individually or collectively, lead to negative rating action/downgrade:

-Further deterioration of the real estate operating environment in SA, materially weakening operational and financial metrics

-Significant weakening of dividends from international investments

-Fitch-calculated deconsolidated net debt/EBITDA increasing to above 7x

Best/Worst Case Rating Scenario

International scale credit ratings of Non-Financial Corporate issuers have a best-case rating upgrade scenario (defined as the 99th percentile of rating transitions, measured in a positive direction) of three notches over a three-year rating horizon; and a worst-case rating downgrade scenario (defined as the 99th percentile of rating transitions, measured in a negative direction) of four notches over three years. The complete span of best- and worst-case scenario credit ratings for all rating categories ranges from 'AAA' to 'D'. Best- and worst-case scenario credit ratings are based on historical performance. For more information about the methodology used to determine sector-specific best- and worst-case scenario credit ratings, visit <https://www.fitchratings.com/site/re/10111579>.

Liquidity and Debt Structure

Healthy Liquidity: At FYE21, Growthpoint, on a deconsolidated basis, had a liquidity ratio of 3.2x. This reflected ZAR709 million of cash and undrawn, committed facilities of ZAR6.5 billion (FYE20: ZAR3.1 billion) from several banks, and free cash flow (FCF) of ZAR253 million. This comfortably covers

debt maturing in FY22 of ZAR2.3 billion. To preserve liquidity Growthpoint has cut capex to ZAR1 billion in FY21 from ZAR2 billion in FY20 and ZAR2.7 billion in FY19.

The nearest material debt maturity is USD425 million of eurobonds maturing in May 2023, which Growthpoint intends to refinance.

Issuer Profile

Growthpoint is the largest REIT with a primary listing on the Johannesburg Stock Exchange in SA; (BB-/Stable, Country Ceiling: BB).

REFERENCES FOR SUBSTANTIALLY MATERIAL SOURCE CITED AS KEY DRIVER OF RATING

The principal sources of information used in the analysis are described in the Applicable Criteria.

ESG Considerations

Unless otherwise disclosed in this section, the highest level of ESG credit relevance is a score of '3'. This means ESG issues are credit-neutral or have only a minimal credit impact on the entity, either due to their nature or the way in which they are being managed by the entity. For more information on Fitch's ESG Relevance Scores, visit www.fitchratings.com/esg

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Rating Actions

ENTITY/DEBT	RATING		RECOVERY	PRIOR
Growthpoint Properties Ltd	LT IDR	BB+ 	New Rating	
	Natl LT	AAA(zaf)	New Rating	
	• senior unsecured LT	BB+	New Rating	RR4

RATINGS KEY OUTLOOK WATCH

POSITIVE		
NEGATIVE		
EVOLVING		
STABLE		

Applicable Criteria

[Corporate Rating Criteria \(pub.15 Oct 2021\) \(including rating assumption sensitivity\)](#)

[Corporates Recovery Ratings and Instrument Ratings Criteria \(pub.09 Apr 2021\) \(including rating assumption sensitivity\)](#)

[National Scale Rating Criteria \(pub.22 Dec 2020\)](#)

[Non-Financial Corporates Exceeding the Country Ceiling Rating Criteria \(pub.08 Jan 2021\)](#)

[Parent and Subsidiary Linkage Rating Criteria \(pub.01 Dec 2021\)](#)

Applicable Models

Numbers in parentheses accompanying applicable model(s) contain hyperlinks to criteria providing description of model(s).

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