GCR affirms Resilient REIT Limited's $AA_{(ZA)}$/$A1+_{(ZA)}$ national scale issuer ratings; Outlook Stable

Rating Action

Johannesburg, 26 November 2020 – GCR Ratings ("GCR") has affirmed Resilient REIT Limited's ("Resilient" or "the REIT") national scale long and short-term issuer ratings of $AA_{(ZA)}$ and $A1+_{(ZA)}$ respectively. The ratings remain on Stable Outlook.

Rated Entity / Issue	Rating class	Rating scale	Rating	Outlook / Watch
Resilient REIT Limited	Long Term Issuer	National	$AA_{(ZA)}$	Stable Outlook
	Short Term Issuer	National	$A1+_{(ZA)}$	

Rating Rationale

Resilient's issuer ratings counterbalance its asset management rigour and conservative funding philosophy against its direct portfolio concentration and increasing scale disparity relative to market leaders.

Portfolio quality remains sound, with the domestic properties' solid performance further illustrating their defensive positioning relative to regional shopping centres in over-traded metropolitan areas. Resilient also has a demonstrated track record of strong through-the-cycle returns from offshore investments, which have historically supported robust cash generation.

That said, offshore earnings could be curtailed by, *inter alia*; investees' lower distributable income, reduced pay-out ratio(s), withheld distributions, or scrip paid out in *lieu* of cash in the short-term. In GCR's view, pressure on rentals amidst double-digit municipal cost inflation will also constrain net property income. As such, we expect the combined cash margin to moderate to a new low in FY21, before recovering fairly quickly thereafter. Overall, while the portfolio quality assessment is expected to remain positive, our view could be moderated by unmitigated value attrition and/or earnings underperformance that persists beyond the current market uncertainty.

The positive leverage assessment is underpinned by strong treasury management, mainly evidenced by consistently proactive refinancing and well-managed debt exposures. Despite some attrition of the security portfolio value, the LTV ratio remains comfortably below 40% (including planned capex) and is expected to trend between 30.0% – 37.5%. Beyond the short-term earnings distortion, interest coverage should also normalise between 2.5x – 3.75x. The well-managed capital structure notwithstanding, significant pressure on values or earnings beyond FY21 would weaken the leverage assessment.

GCR RATINGS

The burgeoning Lighthouse Capital ("Lighthouse") investment represents mixed opportunities for the REIT. Specifically, while Lighthouse's strategy is geared towards more developed economies relative to Resilient's other exposures, this is counterbalanced by its small scale and high exposure to listed securities. GCR has noted Lighthouse's low leverage (September 2020: 21%), although it is still our view that debt could rise in the medium-term to fund acquisition-led growth. In this regard, Resilient will be expected to still adhere to a conservative funding profile as it grows its offshore earnings.

Liquidity continues to be supported by well-established relationships with leading domestic financial institutions, and strong secured facility headroom. Covenant risk and asset encumbrances are well managed, supporting sound access to capital despite the risk aversion presently impacting the capital markets. Notwithstanding that Resilient has maintained a 100% pay-out ratio, GCR expects the 12 months' liquidity coverage to continue to be managed comfortably above 1.25x over the outlook period, with further financial flexibility afforded by negligible capital commitments and the recycling of capital.

Outlook Statement

The Stable Outlook reflects the REIT's consistently conservative treasury management and proactive de-risking of its balance sheet, as well as GCR's expectation that earnings will remain robust despite the pressures facing the property sector.

Rating Triggers

A further upgrade is only likely over the medium term if growth is underpinned by a higher earnings and investment contribution from highly developed jurisdictions. In addition, moderation of the net debt to operating income ratio to 3.0x – 3.5x, interest cover managed at/above 4.0x, and LTV ratios sustained within the 30% – 35% range would bode positively. Conversely, persistent downside pressure on interest cover, or upward creep in the LTV ratio due to 1) curtailed offshore earnings 2) international investments whose leverage is managed more aggressively than Resilient's conservative levels or 3) material pressure on investment portfolio valuations would be negatively viewed.

Analytical Contacts

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Related Criteria and Research

Criteria for the GCR Ratings Framework, May 2019
Criteria for Rating Real Estate Investment Trusts and Other Commercial Property Companies, May 2019
GCR's Country Risk Score report, November 2020
GCR Rating Scales Symbols and Definitions, May 2019
GCR's Commercial Property Sector Risk Score report, August 2020
GCR places South African commercial property on negative trend as fragile economy continues to drive high asset, liquidity and funding risks, August 2020

Ratings History

Resilient REIT Limited

Rating class	Review	Rating scale	Rating	Outlook/Watch	Date
Long Term Issuer	Initial	National	A-$_{(ZA)}$	Stable Outlook	Jun 2010
Short Term Issuer		National	A1-$_{(ZA)}$		
Long Term Issuer	Last	National	AA$_{(ZA)}$	Stable Outlook	Sep 2020
Short Term Issuer		National	A1+$_{(ZA)}$		

Risk Score Summary

Rating components & factors	Risk Score
Operating environment	**14.00**
Country risk score	7.50
Sector risk score	6.50
Business profile	**1.50**
Portfolio quality	1.50
Management & governance	0.00

Financial profile	**0.50**
Leverage & capital structure	0.50
Liquidity	0.00
Comparative profile	**0.00**
Peer comparative	0.00
Group support	0.00
Government support	0.00
Total risk score	**16.00**

Glossary

Cash Flow	The inflow and outflow of cash and cash equivalents. Such flows arise from operating, investing and financing activities.
Country Risk	The range of risks emerging from the political, legal, economic and social conditions of a country that have adverse consequences affecting investors and creditors with exposure to the country, and may also include negative effects on financial institutions and borrowers in the country.
Covenant	A provision that is indicative of performance. Covenants are either positive or negative. Positive covenants are activities that the borrower commits to, typically in its normal course of business. Negative covenants are certain limits and restrictions on the borrowers' activities.
Debt	An obligation to repay a sum of money. More specifically, it is funds passed from a creditor to a debtor in exchange for interest and a commitment to repay the principal in full on a specified date or over a specified period.
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.
Exposure	Exposure is the amount of risk the holder of an asset or security is faced with because of holding the security or asset. For a company, its exposure may relate to a product class or customer grouping. Exposure may also arise from an overreliance on one source of funding. In insurance, it refers to an individual or company's vulnerability to various risks

Fair Value	The fair value of a security, an asset or a company is the rational view of its worth. It may be different from cost or market value.
Financial Flexibility	The company's ability to access additional sources of capital funding.
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.
Issuer	The party indebted or the person making repayments for its borrowings.
Leverage	In corporate analysis, leverage (or gearing) typically 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.
Loan to value	The principal balance of a loan divided by the value of the property and other investments that it funds.
Long Term Rating	See GCR Rating Scales, Symbols and Definitions.
Market Risk	Volatility in the value of a security/asset due to movements in share prices, interest rates, currencies, commodities or wider economic factors.
Outlook period	See GCR Rating Scales, Symbols and Definitions.
Portfolio	A collection of investments held by an individual or institutional investor. These may include (*inter alia*) private/listed stocks, debt securities, 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.
Refinancing	The issue of new debt to replace maturing debt. New debt may be provided by existing or new lenders, with a new set of terms in place.
Short Term Rating	See GCR Rating Scales, Symbols and Definitions.
Upgrade	See GCR Rating Scales, Symbols and Definitions.

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 the rated entity. The ratings above were solicited by, or on behalf of, the rated entities, and therefore, GCR has been compensated for the provision of the ratings.

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

- Audited 2020 financial results (plus four years of comparative, audited financials)
- SENS announcements
- The latest market updates in respect of trading, leverage, and liquidity management
- The latest investees' results and trading updates