



Credit Rating Announcement

GCR revises UPDC Real Estate Investment Trust's national scale long term Issuer rating to A_(NG) on Criteria Review, Outlook Stable.

Rating Action

Lagos, Nigeria, 29 April 2022 – GCR Ratings (“GCR”) has revised UPDC Real Estate Investment Trust's (“UPDC REIT” or “the REIT”) national scale long term Issuer rating to A_(NG), from BBB_(NG) previously, with the Outlook accorded as Stable. Concurrently, GCR has assigned UPDC REIT a national scale short-term Issuer rating of A2_(NG).

Rated Entity / Issue	Rating class	Rating scale	Rating	Outlook / Watch
UPDC Real Estate Investment Trust	Long Term Issuer	National	A _(NG)	Stable Outlook
	Short Term Issuer	National	A2 _(NG)	-

GCR announced that it had released an updated Criteria for Rating Real Estate Investment Trusts and Other Commercial Property Companies in January 2022. Consequently, the ratings for UPDC Real Estate Investment Trust were placed 'Under Criteria Observation'. GCR finalised the review for UPDC REIT under the released Criteria. As a result, the ratings for UPDC REIT have been reviewed in line with the new methodology and subsequently removed from 'Under Criteria Observation'.

Rating Rationale

The ratings of UPDC REIT reflects its low leverage, strong liquidity and high quality asset base. However, these ratings strengths are counterbalanced by its small size and relatively weak portfolio performance through COVID-19, as well as the less sophisticated nature of the market.

GCR considers Nigerian commercial property sector to evidence moderate risk characteristics, underpinned by below average cyclicality, and the presence of fixed assets that generate relatively stable annuity income. The formal market is still at infancy, with only three trading REITs and total net assets value at N37.2bn (USD88.7m) at end-December 2021. This is small compared to the potential size of the market because of the relatively weaker yields (compared with other investment classes) and limited investor knowledge. In recent periods, industry performance has moderated due to growing pressure on tenants in view of the prevailing economic slowdown. However, as more companies resume work in physical offices, the demand for commercial office spaces is expected to increase, lowering vacancy rates. In a bid to support future earnings and returns, industry players are increasing focus towards retail (shopping malls and parks), industrial-use properties and purpose-built student accommodations as these sub-sectors have proven economically resilient.

UPDC REIT is the largest REIT fund in Nigeria but is relatively small when compared with property funds in the frontier and developed markets, with only six properties. The Fund is exposed to significant income volatility due to the concentrated nature of the tenant base, with short lease maturity and valuation inconsistencies. Its largest asset, with capacity to generate about 45% of the REIT's annual rental income, recorded a 25% vacancy rate in 2021 due to consolidation of space requirements by tenants, while rental rates were reviewed downward to maintain some level of occupancy. This followed the impacts of the COVID-19 on tenants' businesses and the adoption of work-from-home model across board. Notwithstanding, the property portfolio appears to be of strong quality in terms of condition and

location, supporting strong potential for lease renewal. The REIT manager, Stanbic IBTC Asset Management Limited, expects conservative rental income for FY22 on account of the moderated occupancy position amidst slow economic recovery. However, there are efforts towards portfolio optimization and cost efficiency to enhance earnings and returns.

Leverage and capital structure are strong rating factors as UPDC REIT has maintained ungeared position since inception and its investment policy does not anticipate the need for debt. However, a negligible N14.7m in lease liabilities was reported at FY21, which represent future lease payments (of more than 2 years' tenor). While the lack of debt underpins the accorded ratings, additional rating support is constrained by the unproven ability to manage debt, and lack of demonstrated access to diverse banking sources or the debt capital market.

The REIT's sources versus uses liquidity coverage is estimated at 2.4x for the 12-month period to December 2022. This is predicated on relatively strong cash flows of around N1.1bn for FY22 and existing cash holding of N2.5bn at end-December 2021, which should be utilised to finance the development of an additional income producing asset and for distributions to unitholders. GCR expects the REIT to maintain sufficient liquidity over the rating horizon.

Outlook Statement

The Stable Outlook reflects GCR's view that UPDC REIT will continue to maintain a high-quality property portfolio in terms of condition and location, underpinning lease renewals, earnings sustainability, and future cash flows. Moreover, potential risk factors are limited by the lack of debt.

Rating Triggers

A positive rating migration could follow 1.) the development of new income generating assets, which strengthens income generating capacity and 2.) a significant reduction in tenant concentration, and attainment of long tenor leases which support strong rentals and performance metrics. GCR could take negative rating action if the economic recovery remained sluggish, with sustained weakness in portfolio performance due to continuous pressure on vacancies.

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Related Criteria and Research

Criteria for the GCR Ratings Framework, January 2022

Criteria for Rating Real Estate Investment Trusts and Other Commercial Property Companies, January 2022

GCR Ratings Scales, Symbols & Definitions, May 2019

GCR Country Risk Scores, December 2021

GCR Nigeria Corporate Sector Risk Scores, April 2022

Ratings History

UPDC Real Estate Investment Trust						
Rating class	Review	Rating scale	Rating	Outlook/Watch	Date	
Long Term Issuer	Initial	National	BBB _(NG)	Stable	March 2013	
Long Term Issuer	Last	National	A _(NG)	Stable	April 2022	
Short Term Issuer	Last	National	A2 _(NG)	--		

RISK SCORE SUMMARY

Risk score	
Operating environment	6.25
Country risk score	3.75
Sector risk score	2.50
Business profile	(3.00)
Portfolio quality	(3.00)
Management and governance	0.00
Financial profile	4.50
Leverage & capital structure	3.00
Liquidity	1.50
Comparative profile	0.00
Group support	0.00
Peer analysis	0.00
Total Risk Score	7.75

GLOSSARY

Assets	A resource with economic value that a company owns or controls with the expectation that it will provide future benefit.
Credit Rating	See GCR Rating Scales, Symbols and Definitions.
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 as a consequence of holding the security or asset. For a company, its exposure may relate to a particular 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
Issuer	The party indebted or the person making repayments for its borrowings.
Lease	Conveyance of land, buildings, equipment or other assets from one person (lessor) to another (lessee) for a specific period of time for monetary or other consideration, usually in the form of rent.
Long Term Rating	See GCR Rating Scales, Symbols and Definitions.
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.
Provision	The amount set aside or deducted from operating income to cover expected or identified loan losses.
Rating Horizon	The rating outlook period, typically 18 to 24 months.
Rating Outlook	See GCR Rating Scales, Symbols and Definitions.
Real Estate Investment Trust	A REIT is a company that owns or finances income-producing real estate. REITs are subject to special tax considerations and generally pay out all of their taxable income as distributions to shareholders.
Short Term Rating	See GCR Rating Scales, Symbols and Definitions.
Short Term	Current; ordinarily less than one year.
Vacancy	In commercial property, usually expressed as a percentage of unoccupied floor space in relation to the GLA.
Valuation	An assessment of the property value, with the value being compared to similar properties in the area.

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 UPDC Real Estate Investment Trust. 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.

UPDC Real Estate Investment Trust participated in the rating process via tele-conferences and other written correspondence. Furthermore, the quality of information received was considered adequate and has been independently verified where possible. The information received from UPDC Real Estate Investment Trust and other reliable third parties to accord the credit ratings included:

- 2021 audited annual financial statement, and prior four years annual financial statements;
- Full details of the property portfolio;
- Internal and/or external management reports;
- Industry comparative data and regulatory framework.

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