

Redefine Properties Ltd.

Real estate

Company Update Report



Mixed 1H24 performance but valuation remains attractive

Analyst recommendation

Counter	Share price	Intrinsic value	Difference
RDF-ZA	R3.77	R4.61	22%

June 2024

Executive summary

We maintain our buy recommendation on Redefine Properties Limited (RDF) with an intrinsic value of R4.61 and an upside of 22%. RDF recently released its 1H24 results that were mixed but we have not changed our view on the company.

RDF's interest cover has decreased from 2.4x in FY23 to 2.2x in 1H24 but is still above its covenant of 2x. The loan-to-value (LTV) for the group increased from 41.1% in FY23 to 42.6% in 1H24 which is above the medium-term target range of 38% to 41%. The main drivers of the increase were the recent Mall of the South acquisition, but the group intends to lower the LTV to the medium-target range.

Revenue was up by 8% with distributable income up by 6% from 23.91 cents per share (cps) to 25.34cps. Dividends per share decreased marginally from 20.32cps compared to 20.27cps. The payout ratio for the period is at 80%, on the lower end of the FY24 guided range of 80% to 90%. Over the FY24 period the group anticipates that interest rate relief should only flow in FY25 due to the expected timing of the rate cuts but also the lagged effects of elevated interest rates that are still to play out.

Our intrinsic value has remained relatively unchanged from R4.60 to R4.61. The upside since our last report has expanded due to rising economic uncertainty influencing bond yield levels along with the performance of RDF and the property sector. Our view is that current bond yield levels (12.12%) are not the new normal but reflect market uncertainty. We anticipate yield levels to correct to similar or below 2 standard deviation (11.70%) levels above the long-term mean. The correction provides a base for upside potential in RDF and the property sector, positioning them as undervalued.

Valuation

We use a Price-to-Funds-From-Operations (P/FFO) multiple valuation to value RDF and have an intrinsic value with an upside of 22%. RDF is trading at a P/FFO that is at a 5% discount to its 5-year average. We view the current level of the multiple as subdued by the current yield levels, the uncertainty associated with the sector as well as the specific risk in office that RDF is exposed to.

What would change our minds?

- A deterioration in property fundamentals
 - Office occupancies falling below 80%, reversions below -17% (worst level in last five years)
 - Retail occupancies falling below 90%, reversions below -13% (worst level in last five years)
 - Industrial occupancies falling below 90%, reversions below -7% (worst level in last five years)
- An outlook change to government bonds increasing from current levels (above 2 standard deviations over the long-term average) to above 3 standard deviations (12.83% and above)



Table 2: Qualitative summary

Factor review	Rating	Description
Growth		We expect revenue growth of 5% for the FY24 period driven by the improving reversions across its assets. We also forecast a contraction in distribution of 3%, close to the midpoint of management's guidance as a factor of finance costs.
Valuation		We have an intrinsic value of R4.61 with an upside of 22%. The current P/FFO multiple trades at a 5% discount to its 5-year average.
Dividend yield		RDF trades with an 12% dividend yield, one of the highest amongst its peers.
Issuance		Share dilution due to incentive schemes over the period has been negligible.
Catalyst		Bond yield levels correcting from the current 12.12% to levels at/below 2 standard deviation (11.70%) from long term average.
Quality of earnings		We rank RDF's quality of earnings as medium. When using the average 3-year quality of earnings ratio (cash flows from operations/net income), RDF's ratio is in the middle when compared to its peer group.
Management and governance		The average tenure for management in the company is six years with no changes in its management team over the last year.
Balance sheet		RDF has an interest cover ratio of 2.2x with an LTV of 42.6%. The group has approximately 14% of debt due in CY24. Refinancing impacts on distributions have been guided by management to range from -7% to +1%.
Risks		RDF has material exposure to Office which is a risk as a result of a structural change in demand for office space driven by changes involving work from home policies. Demand indicated by rental reversions has remained negative for SA Office and SA Retail with SA Industrial being the only segment in the positive.
Regulation		RDF complies with REIT regulations and raises no immediate regulatory concerns.
ESG		RDF has a FactSet ESG score of 78/100.
Momentum price		RDF has negative price momentum.
Momentum earnings		RDF has negative earnings momentum.

Source: PSG Wealth



1H24 results

RDF's 1H24 results showed mixed performance. Revenue was up along with distributable income per share but dividends per share decreased marginally with the payout ratio at the lower end of the 80% to 90% target range. The interest cover ratio did deteriorate from 2.5x in 1H23 to 2.2x but remains above the 2x covenant. The LTV rose from 40.5% to 42.5% primarily driven by the acquisition of Mall of the South.

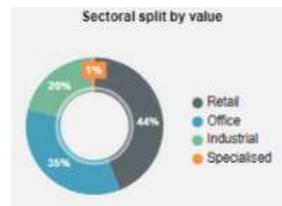
Occupancies on the SA portfolio are mixed with an overall detraction in occupancies with the exception of Office which saw an increase. Rental reversions for Industrial remain positive and improved further. Reversions for Retail and Office remained negative in the period at -0.5% (1H23: -3.7%) and -13.6% (1H23: -12.4%) respectively. Guidance for FY 24 has remained unchanged with a payout ratio range of between 80% to 90% and distributable income per share between 48cps and 52cps.

Table 3: Results summary

	1H23	1H24
Property revenue (R'm)	4 817	5 214
SA REIT FFO (R'm)	1 668	1 777
Distributable income per share	23.91	25.34
Dividends per share	20.32	20.27
Payout ratio	85%	80%
Interest cover ratio	2.5x	2.2x
Loan-to-value	40.5%	42.6%
SA portfolio:		
Occupancies:		
Portfolio	92.5%	92.1%
Retail	95.6%	94.5%
Office	85.7%	87.7%
Industrial	95.1%	92.9%
Rental reversions:		
Portfolio	-7.5%	-6.0%
Retail	-3.7%	-0.5%
Office	-12.4%	-13.6%
Industrial	1.3%	4.0%
Polish portfolio		
Occupancies		
Core EPP	97.1%	98.4%
ELI	94.1%	92.3%
Rental reversions		
Core EPP	-6.7%	2.7%
ELI	-	3.9%

Source: Company AFS

Graph 1: SA split



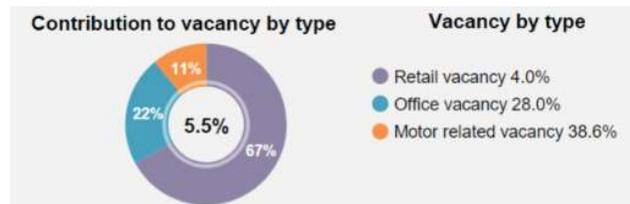
Source: Company presentation

Graph 2: Poland split



Source: Company presentation

Graph 3: SA retail vacancy split



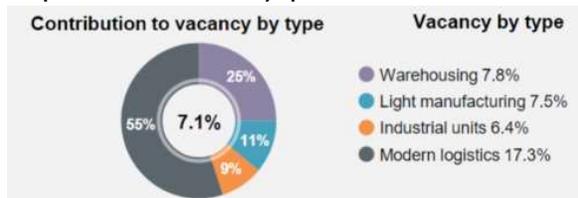
Source: Company presentation

Graph 4: SA office vacancy split



Source: Company presentation

Graph 5: SA office vacancy split



Source: Company presentation

Graph 6: LTV waterfall



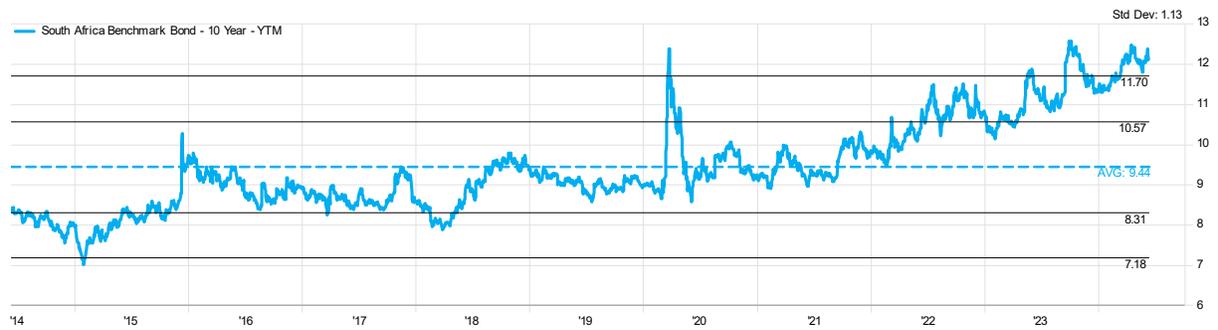
Source: Company presentation



Outlook

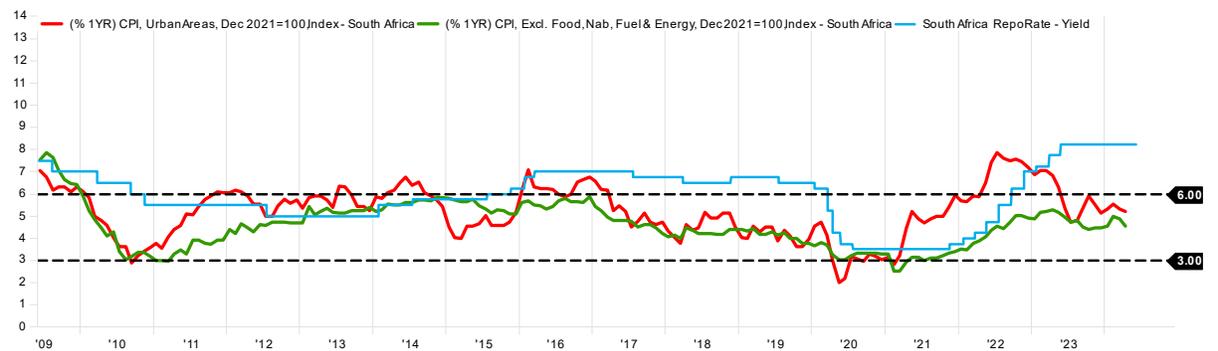
Bond yields have gone up by 83 basis points (bps) from the end of January 2024 (last company update report) to end of May 2024. The hike has been driven by growing economic uncertainty and despite being within the SARB's target range of between 3% to 6%, inflation is yet to reach the 4.50% midpoint. The economic uncertainty has seen yield levels rise while property performance slows when compared to the run it had in the last quarter of 2023. The rise in yields and slow down in property performance satisfies the directional relationship the sector has with bond yields. As such, we still anticipate RDF should benefit as yield levels correct with the catalyst being rate cuts as inflation moves closer to the midpoint of the target. However, as the MPC expects inflation to reach the midpoint in the second quarter of 2025, we can expect cuts to be later rather than sooner which positions the sector to be undervalued for longer.

Graph 7: SA 10-year Bond Yield



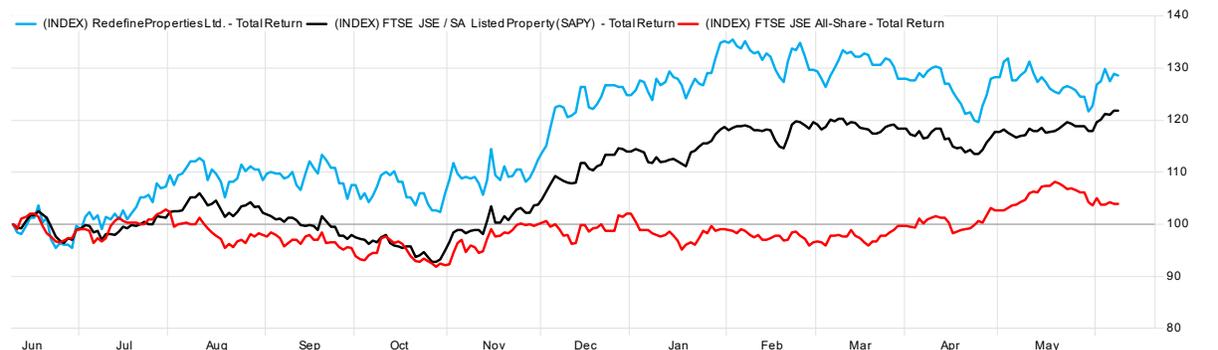
Source: FactSet

Graph 8: Inflation and repo rate



Source: FactSet

Graph 9: RDF, SAPY and ALSI indexed 1-year total returns



Source: FactSet



Valuation

Table 4: Valuation summary

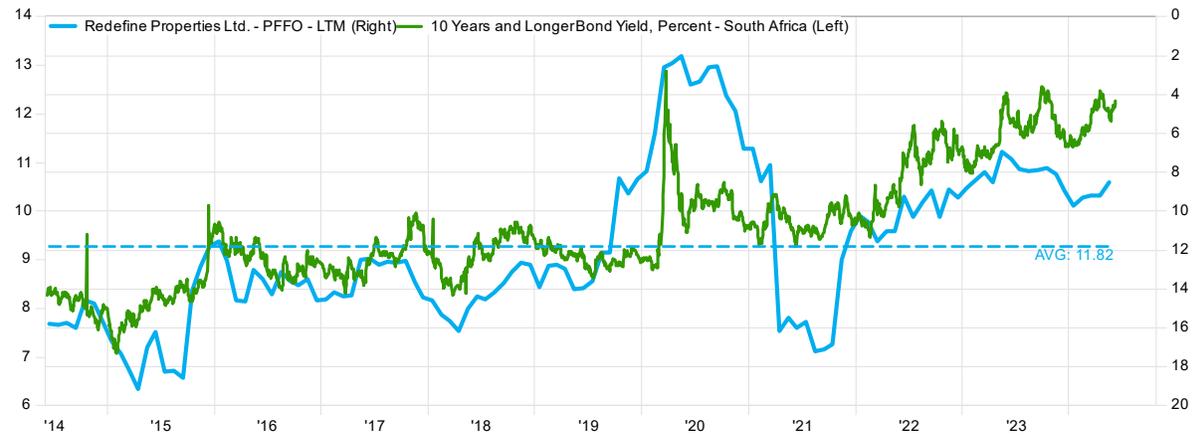
	Bear	Base	Bull	Weighted
FFO	3 661	3 696	3 731	3 696
FFO/share	0.5	0.5	0.6	0.5
Price/FFO multiple	9.0x	10.0x	11.0x	10.0x
Intrinsic value	4.11	4.61	5.12	4.61
Upside/(Downside)	9%	22%	36%	22%
Scenario	25%	50%	25%	-

Sources: PSG Wealth, FactSet

We value RDF using a product of the forecasted FFO per share and P/FFO discounted to compute our intrinsic value. Post RDF's 1H24 results, our view on the company remains unchanged and thus our assumptions remain unchanged as well. We anticipate topline performance to continue its 1H24 momentum into the second half driven by RDF's quality of assets held along with some improvement in demand showcased by improved rental reversions.

Given the directional relationship between bond yield levels along with RDF's valuation multiple, indicated by the graph below- we see RDF as undervalued with upside potential of 22% on a scenario weighted basis. The risk from a valuation perspective is skewed to the upside which drives us to maintain our buy recommendation.

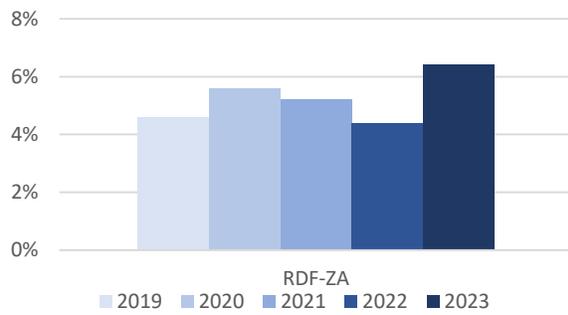
Graph 10: P/FFO (Inversed) and SA 10-year Bond Yield



Source: FactSet

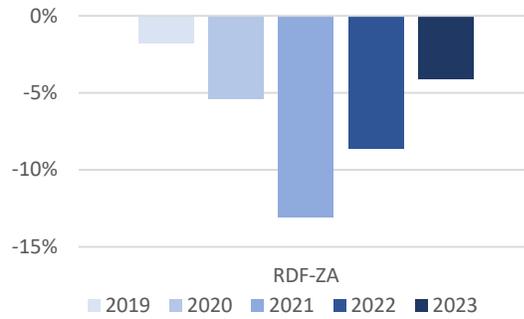


Graph 11: Retail vacancies



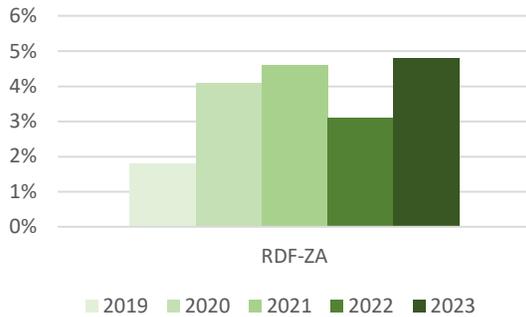
Source: Company AFS

Graph 12: Retail rental reversion



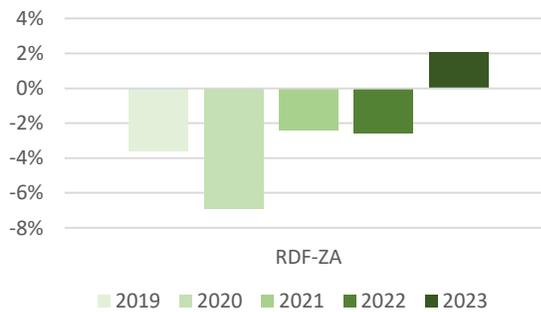
Source: Company AFS

Graph 13: Industrial vacancies



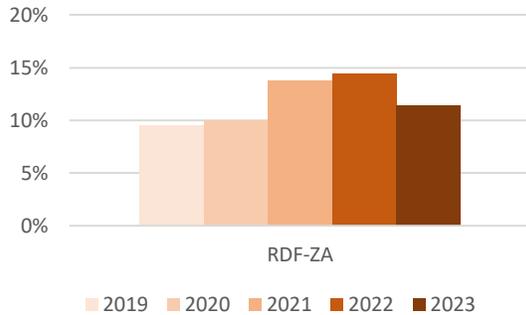
Source: Company AFS

Graph 14: Industrial rental reversion



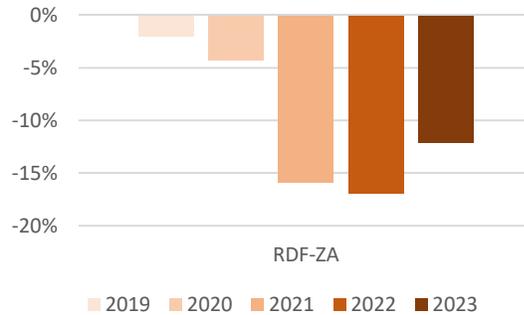
Source: Company AFS

Graph 15: Office vacancies



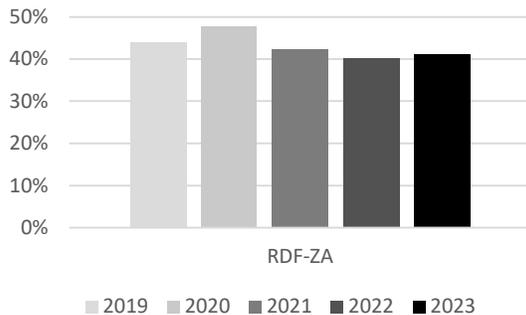
Source: Company AFS

Graph 16: Office rental reversion



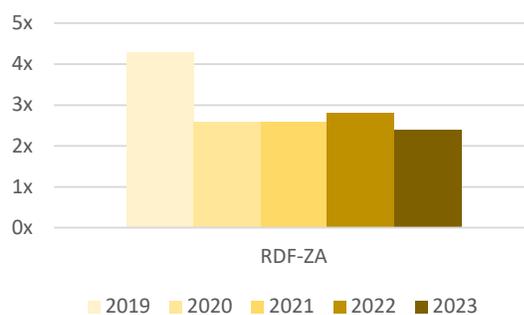
Source: Company AFS

Graph 17: Loan-to-value



Source: Company AFS

Graph 18: Interest cover ratio



Source: Company AFS

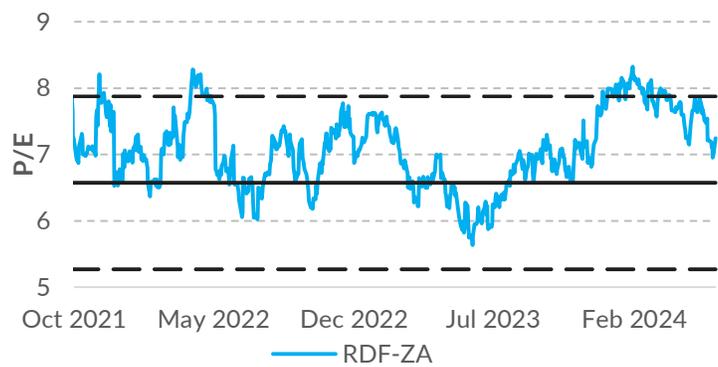


Table 5: Company data

52-week high	R4.24
52-week low	R3.13
Market value (bn)	R26.2
Price momentum	Negative
3m earnings revision	-5.8%
Fiscal year end	2024/08/31
Beta (3Y, daily)	0.59

Source: FactSet

Graph 19: Price to earnings



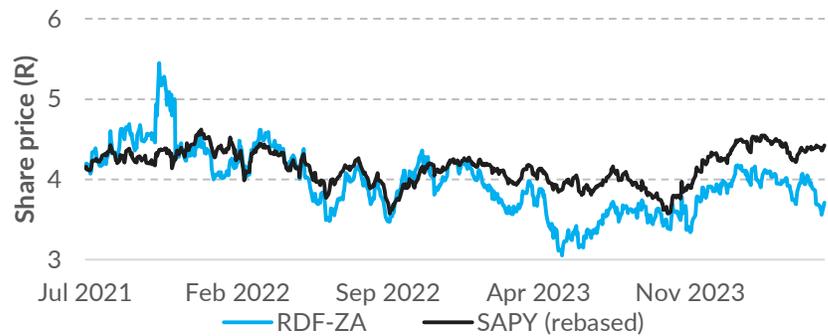
Source: FactSet

Table 6: Valuation multiples

Multiple	Latest: Jun-2024	Last note: Jan-2024
P/E	7.2x	5.1x
P/S	5.1x	5.9x
EV/EBITDA	-	-
EV/EBIT	8.8x	9.9x
EV/SALES	13.6x	13.9x
Dividend yield	11.7%	10.5%
FCF yield	11.3%	10.1%

Source: FactSet

Graph 20: Share price history vs benchmark



Source: FactSet

Table 7: Performance versus benchmark

Period	YTD	MTD	3M	6M	1Y	2Y	3Y	5Y	10Y
Redefine Properties Ltd.	-3.6%	3.3%	-7.0%	5.7%	14.9%	-7.9%	-11.9%	-59.9%	-60.7%
SAPY	2.7%	1.5%	-1.7%	10.9%	11.7%	5.8%	9.9%	-30.8%	-33.2%

Source: FactSet

Table 8: Key competitors

Code	Price (local)	Market Cap (Rbn)	Sales FY0 (Rbn)	EBIT FY0 (Rbn)	Net Income FY0 (Rbn)	EV/EBIT	P/E	Price % (3mo)	Price % (1YR)
RDF-ZA	3.7	26	6 333	4.9	3	13.2x	7.2x	-7.0%	14.9%
GRT-ZA	11.4	39	8 302	8.8	5	14.4x	8.0x	-3.1%	-5.0%
BTN-ZA	7.2	6	1 863	0.9	1	19.7x	7.4x	-6.4%	-4.6%
SAC-ZA	2.5	6	1 284	1.2	1	11.4x	9.1x	-0.4%	35.9%

Source: FactSet



Table 9: Key financials and ratios

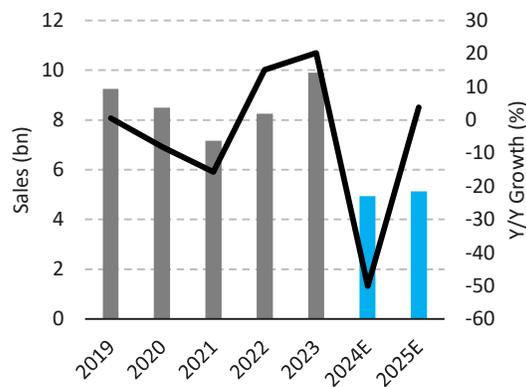
Income Statement (ZAR bn)	2018	2019	2020	2021	2022	2023	5Yr CAGR	2024E	2025E
Revenue	9.2	9.2	8.5	7.2	8.2	9.9	1.53%	4.9	5.1
Y/Y growth (%)	-	0.6	-8.0	-15.7	15.1	20.2		-50.1	3.8
Gross Income	6.5	6.1	5.3	4.1	4.9	5.9	-1.85%	5.0	5.2
Y/Y growth (%)	-	-5.1	-12.8	-22.6	17.4	21.1		-14.7	3.6
EBITDA	5.9	5.3	4.3	4.6	4.5	5.0	-3.24%	5.9	6.1
Y/Y growth (%)	-	-10.9	-18.5	8.2	-3.0	11.2		17.7	4.1
EBIT	5.5	4.6	1.7	5.7	6.5	4.9	-2.03%	5.9	6.1
Y/Y growth (%)	-	-15.7	-63.0	234.5	14.3	-24.5		19.6	4.1
Net Income	6.6	3.3	-16.2	2.9	8.7	1.4	-26.13%	3.3	3.3
Y/Y growth (%)	-	-49.2	-586.1	-118.0	198.4	-83.4		124.7	0.6
EPS	1.2	0.6	-3.1	0.5	1.4	0.2	-29.51%	0.5	0.5
Y/Y growth (%)	-	-49.8	-595.6	-116.4	181.4	-84.9		134.4	2.6

Balance sheet and cash flow (ZAR bn)	2018	2019	2020	2021	2022	2023	5Yr CAGR	2024E	2025E
Capex	0.0137	0.0093	0.0146	0.0286	0.0103	0.0061	14.95%	0.6	0.6
Cash from Operations	5.0	4.6	2.7	2.3	2.6	2.6	12.29%	3.1	3.4
Cash and ST Investments	0.4	0.4	0.4	1.5	1.8	0.8	12.51%	0.2	0.2
Total Assets	98.7	102.7	82.2	75.6	92.4	99.4	0.15%	101.5	103.3
ST Debt	2.5	4.5	1.9	2.3	4.3	5.8	18.48%	5.4	5.0
LT Debt	33.7	36.7	34.9	28.5	33.5	34.9	0.70%	36.9	37.7

Ratios (ZAR bn)	2018	2019	2020	2021	2022	2023	5Yr CAGR	2024E	2025E
Gross Margin (%)	70.4	66.4	62.9	57.8	58.9	59.4	61.1	101.5	101.2
EBIT Margin (%)	59.4	49.8	20.0	79.5	79.0	49.7	55.6	119.0	119.4
Net Income Margin (%)	71.6	36.2	-191.2	40.8	105.8	14.6	1.2	65.7	63.7
Total Debt to Equity	62.6	73.6	96.1	78.7	77.6	78.2	80.8	-	-
Total Debt to Assets	36.6	40.1	44.8	40.8	40.9	40.8	41.5	-	-
ROA (%)	6.9	3.3	-17.6	3.7	10.4	1.5	0.3	-	-
ROE (%)	11.8	5.9	-34.5	7.5	19.9	2.9	0.3	-	-

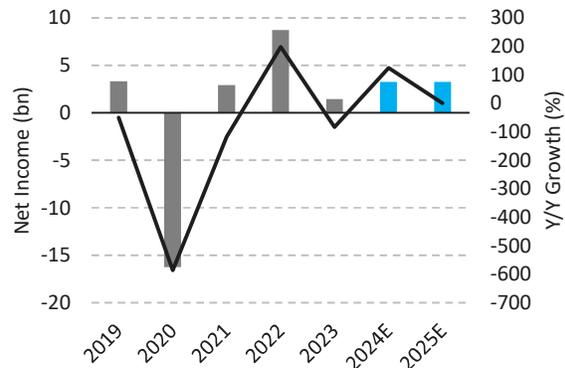
Source: FactSet

Graph 21: Annual sales



Source: FactSet

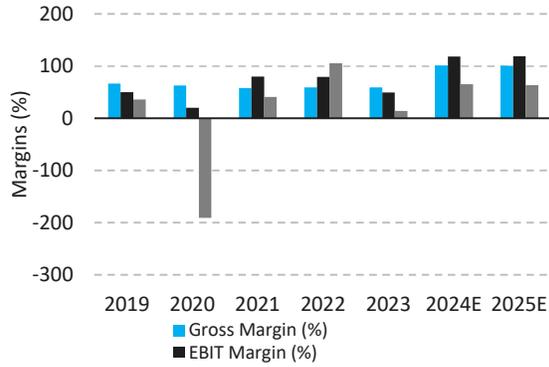
Graph 22: Annual net income



Source: FactSet

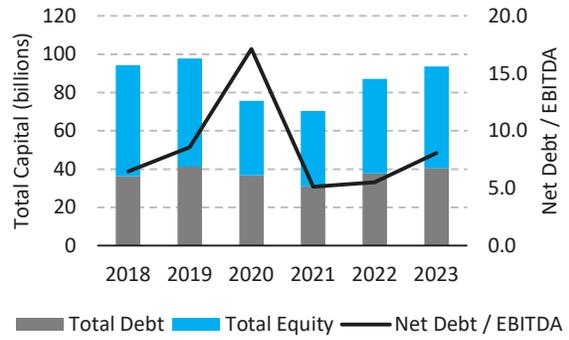


Graph 23: Gross, EBIT, net margins



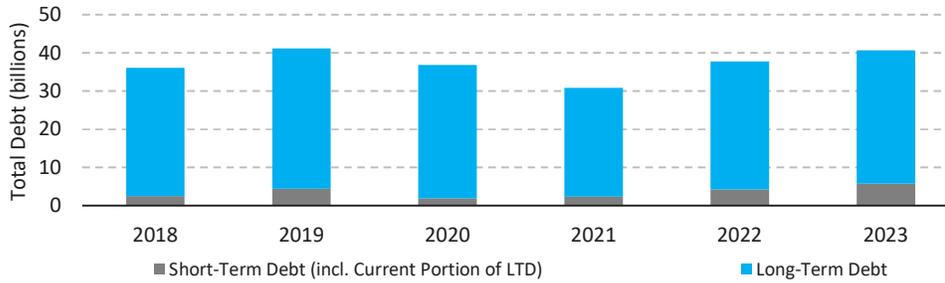
Source: FactSet

Graph 24: Capital structure & net debt / EBITDA



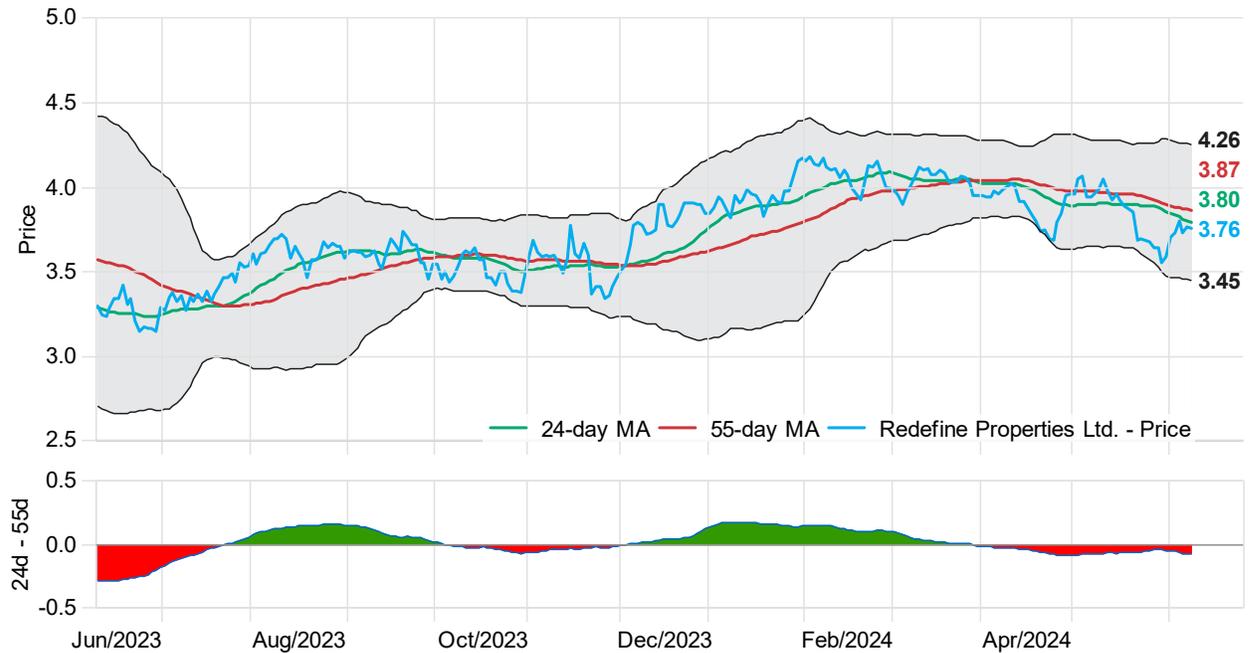
Source: FactSet

Graph 25: Short-term and long-term debt



Source: FactSet

Graph 26: Price momentum



Source: FactSet



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*Share price as at closing.

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