



Credit Rating Announcement

GCR affirms Hospitality Property Fund's rating of A_{-(ZA)} on the back of sustained financial discipline. Outlook Stable

Rating Action

Johannesburg, 12 September 2019 – GCR Ratings ("GCR") has affirmed the long-term national scale Issuer rating assigned to Hospitality Property Fund Limited ("HPF" or "the REIT") of A_{-(ZA)} and revised the short-term Issuer rating to A2_(ZA). The Outlook has also been revised to Stable, as the previous Positive Outlook was predicated on the finalisation of Project Aurora, which did not proceed.

Rated Entity / Issue	Rating class	Rating scale	Rating	Outlook / Watch
Hospitality Property Fund Limited	Issuer Long Term	National	A _{-(ZA)}	Stable Outlook
	Issuer Short Term	National	A2 _(ZA)	

Rating Rationale

The ratings are underpinned by a well-positioned portfolio of hotel properties and conservative gearing metrics, which serve to counterbalance the inherent volatility in the hospitality industry. Specifically, HPF's LTV registered at c.16% at FY19, with management intending to increase debt to fund ongoing capex and potential acquisitions within its internal LTV threshold of approximately 30%. Note is also taken of a secured debt to EBITDA covenant of 3.5x currently in place in respect of Standard Bank facilities. While the REIT has reported substantial cumulative revaluation losses of R1.3bn over the past two years (mostly driven by certain marquee Western Cape properties), expectations of an uptick in key performance metrics have markedly reduced the potential for further material write downs over the rating horizon. Interest coverage was reported at 4.5x at FY19, and is expected to remain relatively strong over the rating horizon.

The underlying performance of the hotels has evidenced weakness in recent times due to a combination of factors, with the Western Cape properties impacted by the drought, while a general slowdown in demand and rising competitive pressures were experienced across the rest of South Africa. HPF has also observed a change in corporate behaviour that curtailed demand traditionally derived from conferences. These factors saw the REIT's overall occupancy rates and RevPAR come under further pressure in FY19.

According to management, certain market segments have returned a strong performance into FY20, while the repricing of some offerings (amongst other initiatives) is expected to contribute to improved volumes. Overall, HPF is expected to sustain sound performance through the cycle, supported by strong relationships with tenants, property managers and international brands, as well as ongoing investment in its properties. That said, the inherent seasonality of the hospitality sector and its susceptibility to a range of exogenous factors constrains HPF's business profile assessment. The REIT also exhibits high tenant concentration as well as relatively high exposures to certain regions and its top ten assets, although this is counterbalanced by the contribution of well-positioned marquee properties.

HPF continues to focus on sound treasury management, displaying no material debt maturities over the next two years (albeit there is some lumpiness in 2020), and reflecting liquidity coverage of 12 months' requirements of at least 1.0x. Counterbalancing this is the encumbrance of its properties, although GCR has noted the headroom to leverage operations further per existing covenants. The overall financial profile is also curtailed somewhat, as HPF's bank facilities are expected to continue to reflect counterparty concentration, although cognisance is taken of the active, proven

access to debt capital markets through the R10bn medium term note programme, which has seen participation by other financial institutions.

Outlook Statement

The Stable Outlook factors in GCR's expectations that conservative financial policies will be sustained, even as the REIT continues to identify opportunities to enhance its portfolio.

Rating Triggers

Upward rating migration could be achieved by further progression in the portfolio, achieved within the fund's targeted leverage thresholds. Conversely, negative rating action could be result from 1) sustained weakness in earnings 2) unduly aggressive leveraging due to acquisitions that significantly curtails covenant headroom 3) further material revaluation losses 4) a deterioration in the liquidity profile.

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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, published June 2019
GCR's SA Sector Risk Score report, published June 2019
GCR's Industry Research on the SA Commercial Property Market, July 2019

Ratings history

Hospitality Property Fund Limited					
Rating class	Review	Rating scale	Rating	Outlook/Watch	Date
Issuer Long term	Initial	National	BBB ⁻ _(ZA)	Stable Outlook	Nov 2012
Issuer Short Term	Initial	National	A3 _(ZA)		
Issuer Long term	Last	National	A ⁻ _(ZA)	Positive Outlook	Sep 2018
Issuer Short Term	Last	National	A1 ⁻ _(ZA)		

Risk Score Summary

Risk score	13.00
Operating environment	14.50
Country risk score	7.50
Sector risk score	7.00
Business profile	-2.50
Portfolio quality	-2.50
Management and governance	0.00
Financial profile	1.00
Leverage and Capital Structure	1.50
Liquidity	-0.50
Comparative profile	0.00
Group Support	0.00
Peer analysis	0.00

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.
Capital	The sum of money that is invested to generate proceeds.
Cash Flow	The inflow and outflow of cash and cash equivalents. Such flows arise from operating, investing and financing activities.
Concentrations	A high degree of positive correlation between factors or excessive exposure to a single factor that share similar demographics or financial instrument or specific sector or specific industry or specific markets.
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.
Debt Service Ratio	A measure of a company's ability to service its interest and principal redemption costs, expressed as the ratio of earnings or cash flows over a period to the sum of interest and principal payments over the same timeframe.
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
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.
Renewal	The re-establishment of the in-force status of a policy, the term of which has expired or will expire unless it is renewed.
Rent	Payment from a lessee to the lessor for the temporary use of an asset.
RevPAR	Revenue per available room. It is calculated by multiplying a hotel's average daily room rate by its occupancy rate.
Risk	The chance of future uncertainty (i.e. deviation from expected earnings or an expected outcome) that will have an impact on objectives.
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 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; c.) such ratings were an independent evaluation of the risks and merits of the rated entity, security or financial instrument; and d.) the validity of the ratings is for a maximum of 12 months, or earlier as indicated by the applicable credit rating document.

The credit ratings have been disclosed to Hospitality Property Fund Limited. 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.

Hospitality Property Fund Limited participated in the rating process via face-to-face management meetings, teleconferences and other written correspondence. Furthermore, the quality of information received was considered adequate and has been independently verified where possible. The information received from Hospitality Property Fund Limited and other reliable third parties to accord the credit ratings included:

- the 2019 audited annual financial statements (plus four years of audited comparative numbers);
- results presentations;
- a breakdown of debt facilities available and related counterparties at 31 July 2019;
- projections of income and capex for FY20.

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