

SPEAR REIT LIMITED

(Incorporated in the Republic of South Africa)

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Approved as a REIT by the JSE

("Spear" or "the Company")



SPEAR
REIT LIMITED

VOLUNTARY OPERATIONAL AND FINANCIAL UPDATE FOR THE THIRD QUARTER, ENDING 30 NOVEMBER 2023, OF THE 2024 FINANCIAL YEAR

1. INTRODUCTION

Spear is pleased to provide a high-level operational and financial update for the three months ending 30 November 2023 ("Q3") of the financial year ending 29 February 2024 ("FY24").

To date, Spear remains the only regionally focussed REIT listed on the JSE. Spear's sole focus on the Western Cape has proven to be a sound investment strategy, despite the generally negative economic and political climate in South Africa. Spear has stood out as a counter-cyclical real estate investment, with the majority of Spear's key performance metrics outpacing its diversified peers with national asset ownership strategies. Despite Spear's regional focus and active asset management approach to operating its business, market headwinds cannot be fully mitigated at all times. Spear's core portfolio has for the most part traded consistently through Q3 FY24, largely in line with management's expectations. Q3 FY24 presented numerous challenges both within the operating environment and with the out of the ordinary "Cape Storms" of 2023.

By and large Q3 FY24 accomplished most of the key performance metrics set by management for the reporting period which will have a positive effect across the operating business over the next two to three quarters, as the major vacancy risk was mitigated, average in-force escalation rates were improved and a marginal improvement to the weighted average lease expiry profile was achieved. Despite a marginal increase in overall portfolio vacancies during Q3 FY24, management reports strong leasing demand across the core portfolio with longer than normal decision making by occupiers being largely responsible for the creep in the portfolio vacancy rate which is concentrated in the commercial portfolio.

Portfolio wide asset management initiatives are yielding strategy aligned outcomes, as rental reversion milestones are met and improved average in-force escalation rates are maintained. Spear's portfolio rental reversion rate for FY24 year to date was -1.12% (HY24: 3.57% and FY23: -3.69%) and the average portfolio in-force escalation rate was 7.44% for the FY24 year to date (FY23: 7.40%).

Trading conditions continue to be extremely tough, despite the Western Cape's appeal and performance and it therefore remains imperative that management continues to successfully implement its active asset management and hands-on property management strategies. As advised during the HY24 communications, Spear's renewal profile has seen a proactive decline as renewals are concluded timeously and, in some instances, well ahead of the expiry dates. Management is very pleased that this momentum has continued into Q3 FY24, as in excess of 139 900 m² of portfolio gross lettable area ("GLA") was either renewed or relet from Q1 to Q3 FY24, versus the 133 343 m² that was classified as portfolio GLA which would either reach expiry or become vacant during the same period.

Spear's business is not immune to the macroeconomic environment, that has been one of volatility, low growth and sustained inflationary pressures. Cost creep and rising interest rates have presented further challenges which had to be absorbed and where possible mitigated to defend the overall operating and financial performance of Spear on a year-to-date basis. Spear's Q3 FY24 update must be viewed in the context that the SARB will likely maintain a higher for longer approach to the interest rate environment with any potential rate cuts only foreseeable towards the second half of 2024. Diesel recovery from tenants has remained consistent, with 96% of the cost of diesel supplied across the portfolio to operate back-up power generators being successfully recovered.

The Western Cape provincial and municipal authorities continue to deliver on their commitment to improve and invest in infrastructure in the region, as population growth numbers consistently tick upwards due to

semigration to the Western Cape. Spear's Western Cape hands on property management approach will continue to contribute to improved core portfolio metrics and the ongoing financial and operational health of Spear, during FY24. Spear's high-quality portfolio remains defensive in nature, positioning the Company to take advantage of growth opportunities in the Western Cape.

The expansion of two major PV Solar roof projects were concluded during Q3 FY24, which will add 2.1 MW of additional solar capacity to the Spear portfolio once commissioned in Q4 FY24. The roof rental structure of the expansion projects will enhance non-GLA revenue with both projects being concluded on 25-year roof rental agreements which include annual escalation rates. Currently three wheeling projects are undergoing feasibility studies to ascertain the suitability and viability of implementation. Upon commissioning of the two expansion projects, Spear's total PV Solar installed energy production capacity will be just under 8 MW, generating 25% of Spear's total portfolio wide electricity demand.

Spear's balance sheet and income statement remain robust and well managed as cost of debt has improved by 4bps during Q3 FY24 and Spear's fixed debt ratio has increased to just under 40% (the strategic band of fixed debt is for 65% to 75% of Spear's debt to be fixed for a period of 24 to 36 months)

Cash collections for Q3 FY24 remain consistent at 97.76%, with sustainable cashflows across the portfolio, which management believes will be maintained throughout FY24. Receivables remain under control, despite the economic headwinds being experienced in South Africa.

2. OPERATIONAL UPDATE FOR THE THREE MONTHS ENDING 30 NOVEMBER 2023

Sectoral Update:

Industrial:

Spear's industrial portfolio remains a key performer within the core portfolio as well-located assets not materially impacted by the severity of loadshedding remain in high demand. The industrial portfolio has maintained its robust performance during Q3 FY24, with consistent demand for industrial rental opportunities. Spear's load curtailment initiatives in certain multi-let industrial parks offer users consistent energy supply, during certain stages of loadshedding when other metros are without electricity.

Operational metrics within the industrial portfolio have remained consistent and in line with management's expectations despite the tough trading and economic environment. Rental reversions for FY24 have printed a positive 5,40% and in-force average escalations being the highest of all sub-sectors of the Spear portfolio, at 7.66%. Spear's industrial portfolio vacancies have declined to 1.41% as at Q3 FY24 from a vacancy rate of 1.43% of total portfolio GLA in HY24.

Bulk infrastructure works have commenced on site at Spear's 30 000 m² GTX Industrial Park in George, which will continue for the next 4 months. Letting enquires have been strong since the launch of the development, resulting in the acceleration of top structure site development plans across the eight respective sites.

Spear's defensive industrial portfolio comprises multi-let industrial, urban logistics, warehousing, manufacturing and logistics assets in sought after locations within the Cape Metropole, at rental rates that remain attractive across the board for small, medium and large enterprises. Spear's industrial portfolio makes up 58% of total portfolio GLA further underpinning the high-quality nature and attractiveness of the regionally focussed core portfolio.

Convenience Retail:

Spear's convenience retail portfolio has made material strides during Q3 FY24, despite the growing pressure facing consumers, as living costs creep upwards and high interest rates impact disposable income. Spear has diligently stuck to its strategy of only investing into the convenience retail sub-sector, which has shown more resilience in the current macroeconomic climate.

Spear's retail assets have performed consistently and have returned to their historically high occupancy rates of 97.05% during Q3 FY24, generating stronger cashflows and generating a positive rental reversion rate of 4,65%, with in-force average escalations improving by 14 bps from HY24 to 7.24% in Q3 FY24. Spear's retail portfolio remains defensively positioned, in both location and tenant mix composition in a trading environment where tenant credit risk may be more prevalent with 41% of Spear's retail portfolio by GLA being occupied by national tenants on long-dated leases with excellent payment records.

Spear's retail portfolio is located in high-growth nodes servicing a wide range of LSM groups. The diverse mix and product offering of the retail portfolio has resulted in numerous brand additions by national retailers.

Commercial:

Despite a valiant effort to aggressively reduce the commercial office portfolio vacancy rate Q3 FY24 ended off with an increased office vacancy rate due to a protracted lease negotiations on a large commercial area that was vacated at 100 Fairways, Parow, Cape Town at the end of November 2023. The total area vacated at the end of November 2023 was 7,534 m² of which 2,203 m² has already been relet (effective immediately) at 5% higher gross rental than the exit rental of the previous tenant. As advised the balance of the vacant space being 5,330 m² is currently in an advanced stage of negotiation with a large occupier. Management is confident that this vacancy is transitory in nature and will not be maintained in the short term given the shortage of supply in the large occupier spaces in Cape Town.

Letting activity within the commercial portfolio has been remained consistent and encouraging, with additional inroads being made into office vacancies at No. 2 Long Street, Northgate Corporate Office Park and Sable Square.

Spear's commercial assets are all located in sought after locations, fitted with sufficient back-up power generation capacity, have generous parking ratios and are positioned to the market with attractive lease terms which have been key drivers to the letting activity year to date.

Outside of just the large occupier demand Spear's commercial portfolio remains well positioned to benefit from the return to office momentum as small and medium scale occupiers return to the office leasing market.

	FY24 Q3				Total FY24 Q3	FY23 Q3	FY23 Total
	Industrial	Commercial	Retail	Development Land			
Number of properties	9	13	6		28	30	28
Value of properties (R'000)	1,536,624	2,159,406	708,507	55,801	4,460,338	4,441,120	4,215,939
Value %	34%	49%	16%	1%	100%	-	-
Property revenue excl smoothing (R'000)	59,966	75,990	24,354	7	160,317	143,868	573,764
Revenue %	37.40%	47.40%	15.19%	0.00%	100%	-	-
GLA m ²	252,941	126,235	47,366	-	426,542	426,029	409,868
GLA %	59%	30%	11%	0%	100%	-	-
Vacant area m ²	6,033	19,724	1,397	-	27,154	29,303	32,034
Vacancy per sector %	2.39%	15.63%	2.95%	-	-	-	-
Vacancy on total GLA %	1.41%	4.62%	0.33%	-	6.37%	6.88%	7.82%
Reversion % YTD	5.40%	-2.60%	4.65%	-	-1.12%	-4.44%	-3.69%
Weighted average in-force escalation %	7.66%	7.42%	7.24%	-	7.44%	6.75%	7.40%
Weighted average lease expiry (Months)	25.55	29.38	24.00	-	27.09	26.81	26.93

		Group FY24 Q3	HY24 Total	FY23 Total
Loan to value	%	40.70	39.58	36.30
Interest cover ratio	Times	2.32	2.36	2.51
Tangible net asset value	R	11.46	11.62	11.47
Total distributable income	R'000	48,500	90,991	188,417
SA REIT Cost to Income	%	43.38	43.32	43.45
SA REIT Administrative cost to income	%	5.51	5.77	6.50
Weighted average cost of debt	%	9.55	9.59	8.66
Weighted average cost of variable debt	%	10.10	10.17	9.05

Weighted average cost of fixed debt	%	8.55	8.27	8.18
Fixed debt ratio	%	38.02	33.76	53.61
Weighted Average expiry of debt	Months	27.07	27.00	30.14
Number of net shares in issue	'000	222,780	223,173	226,065

Letting activity

The table below includes only leases that were concluded and signed during the 9 months ended 30 November 2023.

	Expiries and Vacated GLA m ²	Gross rental at expiry R'000	Average Gross expiry rental R/m ²	Renewals / New Lets GLA m ²	Gross New Rental R'000	Average Gross New Rental R/m ²	Rental reversion
Commercial	32,313	4,758	147.24	30,378	4,357	143.41	-2.60%
Industrial	89,958	5,033	55.95	98,776	5,825	58.97	5.40%
Retail	11,071	1,124	101.49	10,756	1,142	106.21	4.65%
Total	133,343	10,915	81.86	139,910	11,324	80.94	-1.12%

As communicated during the HY24 interim results presentation, improved reversionary metrics were starting to manifest in the commercial portfolio as a result of stronger letting activity and improved leasing terms being concluded with tenants. The latter improvements resulted in the negative rental reversion rate moving from -7.87% at HY24 to -2.60% for the FY24 year to date.

The industrial sub-sector showed a consistent positive rental reversion rate of 5,40%, as successful renewal terms were negotiated at improved rental rates given the prime locations of Spear's assets, the availability of more consistent electricity supply and the holistically attractive nature of Spear's rental terms.

The retail sub-sector showed a marked recovery in rental reversion profiles from HY24 with a positive rental reversion rate of 4,65%. Trading across the retail portfolio has been strong for the quarter and an overall improvement in the rental rate per square meter achieved on new leases has boosted the reversionary profile from a HY24 negative rate to a positive rental reversion rate for the FY24 year to date.

Post 30 November 2023 the following leases have been concluded:

Vacant Space Let circa 2 346 m²:

Offices – 415 m², No. 2 Long Street, Cape Town
Offices – 748 m², 34 Marine Drive, Paarden Eiland
Retail – 332 m², 78 on Edward, Tygervalley
Industrial – 290 m², Blackheath Park, Blackheath
Industrial – 560 m², Mega Park, Bellville South

FY24 lease renewal and letting activity momentum remains positive, as aggressive letting and marketing strategies yield results. The portfolio vacancy rate as at 13 December 2023 is 6.19% being a contraction of 0.18% since end of Q3 FY24.

3. FINANCIAL UPDATE

Group funding

Management has been actively monitoring the hedging environment to increase the group hedging profile in line with its strategy, either through market products or asset disposals. Debt hedging products have become less expensive as the interest rate cycle telegraphs a decline over the next 7 to 8 months. Management concluded fixes to the value of R194 million at a base rate of 7.80% for 3 years during Q3 FY24. Management is of the view that SWAP rates will in all likelihood start to taper off in Q4 FY24 and will allow it to act on its hedging strategy as and when feasible options become available. The strategy remains to have a defensive hedging profile in place of between 65% to 75%, as market conditions permit, without having a negative impact on earnings.

Covenants

	Covenant	30 November 2023
Loan-to-value	50%	40.70%
Interest cover ratio	2 times	2.32 times

Spear's LTV is in line with the LTV sensitivity as disclosed in the HY24 interim results presentation. Spear's internal strategy is to operate within a 38% to 43% LTV ratio at varying times within property cycles. Currently the Spear LTV is in the mid-point of the internal LTV band. The disposal of the Liberty Life Building in Century City will further reduce Spear's LTV by 5%, dropping the group LTV ratio to between 34% and 35%, prior to any fair value adjustments, by the end of FY24.

Cash Collections and availability

The Spear group's cash collections remain strong at just under 98% for the FY24 year to date. Post the HY24 distribution payment, the Spear group has R120 000 000 in available cash. The positive collections and increasing levels of available cash will support a continued dividend pay-out ratio of between 94% and 95%.

4. OUTLOOK

The macro-economic climate remains extremely challenging despite the stronger performance of the Western Cape provincially in various sectors of the economy. The national unemployment rate must be mitigated through jobs growth and investment by both the private and public sector in order to drive growth in gross domestic product. Headwinds in the national logistics eco-system within the ports and rail networks is a further growth inhibitor for South Africa and unnecessary contributor to cost price inflation. Amidst all of the aforesaid, green shoots continue to emerge as real strides are made to stem the impact of loadshedding within the Western Cape and South Africa. The Western Cape has lead by example in driving down the unemployment rate in the province and boasting the highest job growth numbers of a South African province and the lowest provincial unemployment rate in South Africa for 2023. 2024 will be another watershed year for South Africa and we emphatically encourage every South African who is willing and able to exercise their democratic right to cast their votes during the 2024 general elections.

The positive effects of semigration and strong return of the tourism and hospitality sector to the Western Cape will bode well for Spear for the balance of FY24 and beyond. Nodal expansion of residential areas and mixed use precincts have driven demand for space solutions across the Spear portfolio and will drive economic investment and development within the Western Cape for the foreseeable future as the entire province is positioned as an investment opportunity with dependable municipal infrastructure.

The trading environment will remain challenging on all fronts, as consumers absorb the higher cost of living and the operating- and occupancy- cost increases impact the net revenue base of tenants. The prospect of an interest rate tapering cycle in South Africa towards the second half of 2024, bodes well for the general South African economy as well as the real estate sector, as contracting finance costs coupled with stronger portfolio in-force escalations would result in improved profitability.

Management has maintained a highly strategic, obsessive and focussed approach to cost controls and asset management over the Q3 FY24 period and remain confident that Spear will continue to deliver credible, predictable and consistent outcomes for all stakeholders.

Despite the transitory increase in portfolio vacancies, the improved overall operating metrics of the portfolio have reversed the negative distributable income per share ("**DIPS**") as reported in the HY24 interim results presentation. Given the available information management has at its disposal at the time of this update, management guides that the full year FY24 DIPS will be within a range of a 0% to 1,5% higher than the DIPS of FY23.

Spear's guidance is based upon, informed by and impacted by the following:

- loadshedding stages are mostly limited to between stage 1 and stage 4 in City of Cape Town for the remainder of FY24;
- vacancies are reduced in line with management's forecast;
- lease renewals are concluded in line with management's forecast;
- no major tenant failures occur during the year;

- tenants continue to successfully absorb rising costs associated with utility charges, municipal rates and diesel charges;
- no further SA Reserve Bank interest rate hikes; and
- no civil unrest within Cape Town, the Western Cape or South Africa.

Any changes in the above assumptions may affect management's forecast for the year ending 29 February 2024.

The information and opinions contained above are recorded and expressed in good faith and are based on reliable information provided to management.

No representation, warranty, undertaking or guarantee of whatsoever nature is made or given with regard to the accuracy and/or completeness of such information and/or the correctness of such opinions.

The Q3 FY24 financial information contained in this announcement has not been audited or reviewed by the external auditors of the Company.

Cape Town
14 December 2023

Sponsor
PSG Capital

