

Listed Property

GARDA Property Group (ASX Code: GDF)

1 October 2020

FY20 Results: Solidifying the base

Accumulate

GARDA Property Group (ASX: GDF)

Contents

1.	Overview	2
2.	Key Metrics	3
3.	Summary & FY20 Results	4
4.	Financial Forecasts & Valuation	6
5.	Property Portfolio	7
6.	Appendix: Financial Summary	8
7.	Ratings Process for A-REITs	9
8.	Disclaimer & Disclosure	10

About Core Property Research

Core Property Research Pty Ltd was established in July 2017 to provide market leading and insightful research on the property funds sector for its clients and investors. Our ratings and research cover sector level research, ratings and recommendations on listed and unlisted property funds, and is built upon the extensive research experience of its staff.

The Core Property team collectively, has over 50 years' experience across property, financial services and investment markets. The team has also evaluated over 500 different funds across multiple sectors and a range of investment structures over the last decade.

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Accumulate

See the end of this document for a description of Core Property's ratings. The rating must be viewed in the context of comparable A-REITs and not across all products.

Core Property forecasts

Forecast Distribution:	6.9%
Forecast 12 Month Capital Return:	30.5%
Total Expected Return:	37.3%

Company Data

ASX Code:	GDF
Price:	\$1.05
Market Capitalisation:	\$239.0M
Securities on Issue:	227.6M
52 Week Range:	\$0.80 - \$1.49

FY20 Results: solidifying the base

- ◆ *FY20 FFO of 8.2cpu (from 8.7cpu in prior year). Strong 26.0% growth in FFO was offset by the issue of new units to fund acquisitions and internalisation of management operations.*
- ◆ *COVID-19 impacts were very marginal - \$6,500 of rent was waived. A further \$0.4M of rent deferred and expected to be collected by end of the year.*
- ◆ *Management guidance for FY21 earnings to be around 7.2 – 7.6cpu and distributions of 7.2 cpu, implying a 6.9% yield on current price.*
- ◆ *Recommendation upgraded to Accumulate (previously Hold). We see value at current price levels, however further upside is likely to come in FY22 onwards once acquisitions are fully included. Upside potential also once Botanica 9 is leased.*

GDF delivered a solid FY20 result with Funds From Operations (FFO) of up 26% for the year, off the back of acquisitions undertaken during the year. FFO per security was -5.7% after taking into account the issue of new securities for the acquisitions and internalisation of management operations. These acquisitions are expected to contribute positively once included for the full year.

COVID-19 has only marginally impacted GDF with \$6,500 of rent waived. A further \$0.4M of rent was deferred and expected to be collected by the end of the year. This highlights the relatively resilient nature of GDF's portfolio to COVID-19.

Portfolio remains well placed with 52% office / 48% industrial split. WALE of 5.9 years. Portfolio occupancy of 80% continues to be impacted by Botanica 9 in Richmond VIC (14.1% of portfolio) which remains unoccupied. **Management guidance for FY21** is for distributions of 7.2 cpu with earnings expected to be around 7.2 – 7.6 cpu.

At current price levels, we consider GDF offers an attractive distribution yield of 6.9% for a diversified office/industrial portfolio. We have updated our forecasts to adjust for recent acquisitions and delayed the potential lease up of Botanica 9. Our DCF valuation is \$1.28 per unit and we have a 12 month roll forward value of \$1.37 per unit. Whilst we expect GDF to deliver solid earnings in FY21 through the full inclusion of acquisitions, we would see any early leasing success at Botanica 9 as providing potential for a further upgrade. Our recommendation has been upgraded to **Accumulate** (prior Hold).

Share price performance



Source: IRESS

Year Ended 30 June	FY20A	FY21F	FY22F	FY23F
NPAT - Reported - \$M	5.6	16.1	21.8	24.7
NPAT – FFO basis - \$M	16.6	16.1	21.8	24.7
Price/Earnings Ratio	14.4	14.9	10.9	9.7
FFO per unit - cents	8.2	7.4	9.6	10.8
FFO per unit - growth		-10.6%	30.0%	13.0%
DPU - cents	8.6	7.2	7.6	7.9
Distribution Yield	8.1%	6.9%	7.2%	7.5%
NTA per unit	\$1.18	\$1.23	\$1.26	\$1.31
Gearing	37.2%	35.0%	34.8%	34.1%

Source: Core Property estimates

Note: Gearing = (net debt – cash) / (net debt – cash + net assets)

Key Metrics

Strategy

To provide sustainable and growing distributable income derived from commercial and industrial real estate across the east coast of Australia. GDF focuses on a combination of newer and high yielding assets that is diversified across building type, location and tenants. The Fund is relatively defensive as it focuses on maintaining a conservative capital structure.

Board & Management

Board of the RE: Matthew Madsen (Executive Chairman), Mark Hallet (Executive Director), Morgan Parker (Independent Director), Philip Lee (Non-Executive Director), Paul Leitch (Independent and Non-Executive Director), Andrew Thornton (Non-Executive Director).

Senior Management: Matthew Madsen (Executive Chairman and Managing Director), David Addis (Chief Operating Officer), Paul Brown (Manager, Investor Relations), Paul Lohr (Asset Manager), Ikram Patel (Financial Controller).

Portfolio		Key Properties		Key Tenants		Geography	
Metric	June 20	June 20	% Portfolio	June 20	% Portfolio	June 20	% Portfolio
No of Properties	17	7-19 Lake St, Cairns QLD	14.5%	J Blackwood & son	10.9%	NSW	-
Valuation	\$416.2M	588A Swan St, Richmond VIC	14.1%	Planet Innovation	10.6%	Queensland	65.0%
Capitalisation Rate	6.60%	572-576 Swan St, Richmond VIC	12.9%	Volvo Group	10.0%	Victoria	35.0%
Locations	Australia	326 & 340 Thynne Rd, Morningside QLD	10.0%	Qld Govt (DTMR)	7.2%	ACT	-
Sector	Office (52%) Industrial (48%)	41 Bivouac Place, Wacol QLD	9.3%	Golder Associates	7.1%	WA	-
Occupancy	80%					SA	-
WALE	5.9 years	Top 5	60.8%	Top 5	45.8%	Total	100%

Debt	June 2020	Expenses	June 2020	Historical	FY18	FY19	FY20
Gearing	36.7%	RE Fee	NA ¹	EPU – FFO per Unit	8.7	8.7	8.2
Target Gearing	30-35%	Direct Property Expenses	21.0% of gross	DPU – Distributions per Unit	9.0	9.0	8.55
Drawn Debt	\$188.1M	Other Expenses	14.4% of gross income	Payout Ratio	100.7%	104.7%	104.5%
Facility limit	\$200M	Note 1: The RE forms part of GDF as a stapled security. All fees to the RE are eliminated on consolidation.		Distribution Frequency	Qtrly	Qtrly	Qtrly
Weighted Average Cost of Debt	~2.4%			NTA per Unit	\$1.28	\$1.37	\$1.18
Weighted Average Debt Maturity	2.7years			Note: Results up to 29 November 2019 are for GARDA Diversified Property Fund only, prior to the internalisation.			
% Hedged	53%						
LVR	45%						
LVR Covenant	50%						
ICR	3.7x						

Summary

GDF delivered FY20 results with FFO up 26.0% driven by acquisitions, with FFO per unit down 5.7% after taking into account the issue of new securities and the internalisation of the management structure. GDF's portfolio has been largely unimpacted from COVID-19 with only \$6,500 of rent being waived and \$0.4M deferred through the remainder of calendar year 2020.

The Botanica 9 office building in Richmond, Victoria continues to be a key focus, contributing 14% to the portfolio vacancy with potential to add around \$4.7M p.a. in net income once fully leased. GDF are also targeting development completions and progress at three industrial sites in Berrinba, Wacol and Acacia Ridge, with pre-commitments for each secured.

Management guidance for FY21 is for distributions of 7.2 cps, after taking a conservative view in excluding any revenue from Botanica 9. This reflects a payout ratio of between 95% - 100%, implying FFO of 7.2 – 7.6 cps. We have updated our forecasts for Botanica 9 to be leased up January 2022, given the current economic climate, and we have adjusted for recent acquisitions.

FY20 Results

Figure 1: FY20 Results to 30 June 2020

FY20 results	FY20	FY19 ¹	Change
Earnings			
Statutory Net Profit*	\$5.6M	\$28.8M	-80.7%
Funds From Operations	\$16.6M	\$13.2M	+26.0%
FFO per security (on weighted units)	8.2 cps	8.7 cps	-5.7%
Distributions Paid	\$17.4M	\$13.8M	+26.1%
Distribution per security	8.55 cps	9.0cps	-5.0%
Payout ratio	104.5%	104.7%	-0.2%
Movement over 12 months			
	As at Jun 2020	As at Jun 2019 ¹	Change
Balance Sheet			
NTA per security	\$1.18	\$1.37	-13.9%
Gearing (%)	36.7%	32.5% ²	+4.2%
Weighted average cost of debt	2.4%	3.16%	-0.76%
Weighted average debt maturity	2.7 years	1.15 years	+1.55 years
Borrowings – on balance sheet	\$188.1M	\$139.7M	+34.6%
Portfolio			
Property Valuation	\$416.2M	\$332.8M	+25.1%
Occupancy rate	80% ³	83%	-3.0%
Number of properties	13	12	+ 1 asset
Weighted Average Capitalisation Rate	6.60%	6.79%	-19 bps
WALE (Weighted Average Lease Expiry)	5.9 years	5.3 years	+0.6 years

Source: GDF, Core Property *Statutory Net Profit includes non-cash items which distorts operating income. Fund From Operations is a more appropriate measure to assess changes. Note 1: FY19 Results reflect the GARDA Diversified Property Fund prior to the internalisation of management into GARDA Property Group. Note 2: LVR (%) in FY19. Note 3: 94% occupancy excluding Botanica 9.

Key Points

- **Internalisation of Management:** On 29 November 2019, GDF became a stapled security through the internalisation. GARDA Diversified Property Fund is its management function. It should be noted that FY19 results quoted are of the former GARDA Diversified Property Fund, prior to the stapling of securities.
- **Impact of COVID-19:** Direct impacts from the COVID-19 pandemic were minimal. Through the year, only \$6,500 in rent was waived. An additional \$0.4M was provided in rent deferrals, of which, \$0.3M remains outstanding and due to be repaid over the remainder of CY20
- **Funds From Operations (FFO)** of \$16.6M increased by 26.0% for the year, driven predominantly by net acquisitions. FFO per security was down 5.7% after taking into account the issue of new units to fund acquisitions and complete the internalisation process.
- **Portfolio metrics:**
 - **Occupancy levels** fell to 80% (83% at June 2019) with two tenant departures at Varsity Lakes (QPS) and Lytton (Visy) decreasing occupancy by 3%. GDF continues to look to lease up Botanicca 9 (588A Swan St, Richmond VIC) which accounts for around 14% of portfolio occupancy. Excluding Botanicca 9, occupancy is 94%.
 - **Portfolio WALE** of 5.9 years, up from 5.3 years, as a result of positive leasing outcomes and tenant departures.
 - **The investment portfolio** increased to \$416.2M (from \$332.8M at June 2019), an increase of \$83.4M. Key movements during the period include:
 - **Acquisition of four industrial properties in Acacia Ridge and Archerfield** for \$31.0M.
 - **Acquisition of two industrial warehousing and distribution assets in Morningside** for \$41.0M (plus costs); and
 - **Development works at Berrinba and Wacol** for \$6.8M. GDF also invested \$5.2M in capital expenditure to the Group's capital improvements program, with a majority allocated to 7-19 Lake Street, Cairns.
 - **Revaluation gains** of \$0.8M, with independent valuations completed across five commercial and industrial assets.
- **Debt:** GDF's gearing increased to 36.7% (from an LVR of 32.5% in FY19), driven by net acquisitions and development expenditure. During the year, GDF restructured existing debt facilities with incumbent lenders into a syndicated facility; including an increase in the facility limit to \$200.0M and extension of term to February 2023. This has increased GDF's liquidity to \$32.3M, increased the weighted average debt maturity to 2.7 years and reduced the all-in cost of debt to 2.4%.
- **Net Tangible Assets (NTA)** decreased 13.9% to \$1.18 per unit, driven largely by the goodwill acquired on internalisation.
- **Distributions** of \$13.8M were paid, up 26.1% for the year. Distributions per security of 8.55 cps fell on FY19 (9.0 cps), after adjusting for the issue of new units.
- **Management has advised that its focus for FY21** will be on:
 - 1) completing the leasing of Botannica 9, with potential net revenue of around \$4.7M p.a on a fully leased basis.
 - 2) leasing up recent industrial developments at Berrinba (completion expected early FY21), Wacol (completion expected early FY21) and Acacia Ridge, which have already seen 15,125 sqm project leasing for lease terms of 5, 10 and 7 years respectively.
- **FY21 Guidance** was provided with GDF expecting distributions of 7.2 cps (compared to 8.55cps in FY20). This is based on the assumption that Botanicca 9 remains unleased and reflects a payout ratio of 95% - 100%, implying FFO of 7.2 – 7.6 cps.

Core Property considers the FY21 distribution guidance of 7.2cpu as providing a relatively strong yield in the current environment, based on the current security price. The continued uncertainty of leasing at Botanicca 9 has held back much of GDF's potential for growth over the period. We expect that once GDF is able to successfully lease Botanicca 9, this will deliver a strong boost earnings and free up capital for additional growth over the medium term.

Financial Forecasts & Valuation

We have updated our financial forecasts to take into account the results and updated portfolio.

Our FY21 forecast earnings have been updated to include nil revenue from Botanicca 9, given the uncertain economic environment. We have moved our expectations for Botanicca 9 to be leased up by January 2022. Berrinba, Wacol and Acacia Ridge are assumed to contribute a minor contribution (~\$0.5M) after leasing incentives are taken into account, with further upside flowing through in FY22.

We value GDF on a Discount Cashflow (DCF) basis at \$1.28 per unit, with a 12 month roll forward valuation of \$1.37 per unit. We would see further upside to our valuation through the successful leasing of Botanicca 9.

Figure 2: Earnings Forecast – Core Property

Financial Forecasts - \$M	FY20A	FY21F	FY22F	FY23F
Property Revenue	28.6	28.5	34.4	37.5
Property Expenses	-6.4	-8.3	-8.4	-8.5
RE Fees	-1.1	0.0	0.0	0.0
Finance Costs	-3.8	-3.9	-3.9	-3.9
Other Expenses	-2.3	-2.0	-2.0	-2.2
Funds from Operations	15.0	14.4	20.1	22.9
Earnings per Unit	8.2	7.4	9.6	10.8
Payout Ratio	94.0%	99.7%	79.2%	72.9%
Distributions per Unit	8.55	7.20	7.60	7.90
Guidance – Distn per unit		7.20		

Source: Core Property forecasts

Property Portfolio

The following table is a summary of GDF's portfolio as at 30 June 2020.

Property Portfolio – as at 30 June 2020

Property	Valuation \$M		Capitalisation Rate %		Occupancy %		WALE (years)	
	Jun20	Dec19	Jun20	Dec19	Jun20	Dec19	Jun20	Dec19
7-19 Lake Street, Cairns QLD (including land at 26-30 Grafton St, Cairns QLD)	\$60.56M	\$58.0M	8.25%	8.25%	88%	93%	4.8	3.2
154 Varsity Parade, Varsity Lakes QLD	\$12.0M	\$12.5M	8.50%	8.25%	60%	82%	2.9	2.4
142-150 Benjamin Place, Lytton QLD	\$8.725M	\$9.8M	7.25%	7.00%	42%	100%	2.5	1.4
436 Elgar Road, Box Hill VIC	\$33.25M	\$32.0M	6.00%	6.25%	100%	100%	7.4	7.9
572-576 Swan Street, Richmond VIC	\$53.69M	\$53.5M	5.75%	5.75%	100%	100%	3.4	3.9
69-79 Diesel Drive, Mackay QLD	\$30.1M	\$30.0M	7.50%	7.50%	100%	100%	8.5	9.0
41 Bivouac Place, Wacol QLD	\$39.0M	\$39.0M	5.75%	5.75%	100%	100%	8.0	8.5
70-82 Main Beach Road, Pinkenba QLD	\$20.5M	\$20.0M	6.75%	6.75%	100%	100%	13.1	13.6
588A Swan Street, Richmond VIC (Botanica 9)	\$59.04M	\$59.0M	5.75%	5.75%	0%	0%	NA	NA
67 Noosa Street, Heathwood QLD	\$11.25M	\$11.25M	6.75%	6.75%	100%	100%	7.7	8.2
1-9 Kellar St, Berrinba QLD	\$7.35M	\$3.1M	NA	NA	NA	NA	NA	NA
498 Progress Road, Wacol QLD	\$9.22M	\$6.3M	NA	NA	NA	NA	NA	NA
326 & 340 Thynne Rd, Morningside QLD	\$41.625M	\$41.0M	5.75%	5.75%	100%	100%	4.6	5.0
38 Peterkin St, Acacia Ridge QLD	\$6.0M	\$6.0M	7.50%	7.50%	100%	100%	0.8	0.7
56 Peterkin St, Acacia Ridge QLD	\$6.8M	\$6.7M	7.25%	7.25%	NA	NA	NA	NA
69 Peterkin St, Acacia Ridge QLD	\$11.08M	\$10.9M	7.25%	7.25%	NA	NA	NA	NA
839 Beaudesert Rd, Archerfield QLD	\$6.0M	\$6.0M	7.50%	7.50%	92%	92%	1.0	1.5
Capital Expenditure post valuation	-	\$1.0M	NA	NA	NA	NA	NA	NA
Total Portfolio	\$416.2M	\$405.1M	6.60%	6.60%	80%	84%	5.9	5.6

Source: GDF

Appendix: Financial Summary

GARDA Property Group (ASX: GDF)

Profit & Loss	FY20A	FY21F	FY22F	FY23F
Operating Revenue	28.6	28.5	34.4	37.5
Property Expenses	-6.4	-8.3	-8.4	-8.5
Net Property Income	22.2	20.3	26.1	29.0
Other Income & Expenses	-0.7	-0.3	-0.3	-0.4
RE Fees	-1.1	0.0	0.0	0.0
EBITDA	20.4	20.0	25.8	28.6
Depn & Amort	-0.2	0.0	0.0	0.0
EBIT	20.3	20.0	25.8	28.6
Net Interest	-3.8	-3.9	-3.9	-3.9
Pre Tax Profit	16.5	16.1	21.8	24.7
Tax	0.1	0.0	0.0	0.0
Minorities	0.0	0.0	0.0	0.0
NPAT - adj	16.6	16.1	21.8	24.7
Non Recurring Items	-11.1	0.0	0.0	0.0
NPAT - Statutory	5.6	16.1	21.8	24.7

Summary	FY20A	FY21F	FY22F	FY23F
NPAT - adj	16.6	16.1	21.8	24.7
Price Earnings Multiple	14.4	14.9	10.9	9.7
Revenue Growth	19.0%	-0.2%	19.6%	8.6%
EBIT Growth	26.6%	-1.4%	28.7%	11.0%
Value of Properties	417.4	454.8	463.6	472.9
Net Assets	280.6	314.5	321.4	330.7
NTA per Unit	\$1.18	\$1.23	\$1.26	\$1.31
Prem(Disc) to NTA per unit	-11.3%	-14.9%	-16.9%	-19.6%
DPU	8.55	7.20	7.60	7.90
Payout Ratio		97.6%	79.2%	72.9%
DPU Growth		-15.8%	5.6%	3.9%
Yield	8.1%	6.9%	7.2%	7.5%

Cashflow	FY20A	FY21F	FY22F	FY23F
Operating Activities	19.6	21.2	27.0	29.9
Net Interest	-5.1	-3.9	-3.9	-3.9
Tax Paid	-0.5	0.0	0.0	0.0
Other	0.0	0.0	0.0	0.0
Operating Cashflow	14.0	17.2	23.0	26.0
Capex	-0.2	-6.3	-6.3	-6.3
Maintainable Operating CF	13.7	11.0	16.8	19.7
Distributions	-16.9	-16.0	-17.3	-18.0
Acquisitions	-78.9	0.0	0.0	0.0
Disposals	0.0	0.0	0.0	0.0
Other	0.0	0.0	0.0	0.0
Free Cashflow	-82.1	-5.1	-0.5	1.7
Change in Debt	51.5	5.4	4.9	0.5
Change in Equity	30.9	0.0	0.0	0.0
Net Cashflow	0.3	0.3	4.4	2.2

Key Ratios	FY20A	FY21F	FY22F	FY23F
EPU (adj)	8.2	7.4	9.6	10.8
EPU - Reported	2.8	7.4	9.6	10.8
EPU (adj) - Growth		-10.6%	30.0%	13.0%
LVR	44.7%	41.0%	40.3%	39.5%
Net Debt/(Net Debt + Equity)	37.2%	35.0%	34.8%	34.1%
Net interest Cover	5.4	5.1	6.6	7.3
Distn / Maintainable CF	123.2%	146.3%	103.1%	91.3%
ROE	6.0%	5.1%	6.8%	7.5%

Balance Sheet	FY20A	FY21F	FY22F	FY23F
Cash	20.5	17.1	15.1	15.3
Debtors	5.3	5.0	6.2	6.3
Investments	0.0	0.0	0.0	0.0
Other Assets	451.5	488.4	497.2	506.4
Total Assets	477.3	510.6	518.5	528.1
Creditors	3.9	3.7	4.6	4.7
Borrowings	186.7	186.7	186.7	186.7
Provisions	0.0	0.0	0.0	0.0
Other Liabilities	6.1	5.6	5.9	6.0
Total Liabilities	196.7	196.0	197.2	197.4
Net Assets	280.6	314.5	321.4	330.7

Valuation	
Discount Rate	9.0%
Terminal Growth Rate	2.5%
DCF Valuation per Share	\$1.28
12 Month Target Price	\$1.37 DCF rolled forward 12 mths
12 month Dividend Yield	6.9%
12 month Target Price	30.5%
Total Est. 12 mth return	37.3%

Source: Core Property forecasts

Note: Gearing = (net debt - cash) / (net debt - cash + net assets)

Ratings Process for A- REITs

Core Property Research evaluates recommendations on listed A-REITs continuously, based on a range of qualitative and quantitative criteria ranging from management, appropriateness of the A-REIT's capital structure and the property portfolio metrics. From a quantitative perspective, Core Property's recommendations are based on Total Expected Returns (forecast distribution yield plus forecast capital gain or loss) for a 12-month time horizon, using a range of valuation methodologies. The two most commonly used valuation techniques are Discounted Cash Flow (DCF), which uses an A-REI's expected free cash flow, and the net Asset Valuation (NAV) approach.

The 12-month Total Return is compared with set total return bands and assigned a 12-month recommendation based on the Recommendation Definitions below.

Recommendation Definitions

Recommendation	Definition
Buy	If the 12-month Total Expected Return is forecast to be 15% or more.
Accumulate	If the 12-month Total Expected Return is forecast to be at least 10% and less than 15%.
Hold	If the 12-month Total Expected Return is forecast to be at least 5% and less than 10%.
Reduce	If the 12-month Total Expected Return is forecast to be at least 0% and less than 5%.
Sell	If the 12-month Total Expected Return is forecast to be less than 0%.

At times of extreme volatility, it is quite possible that the recommendations will swing between each of our bands. During such times, Core Property will adopt a more flexible approach to recommending stocks, based on a slightly longer duration, and as such, recommendations may appear to be inconsistent when compared with the bands. This is to avoid clouding value judgments with short-termism.

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