IJG
Securities (Pty) Ltd.
Member of the NSX

ORYX PROPERTIES LIMITED

FY16 Results Review

November 2016

Oryx Properties Limited

FY16 Results review

Target Price (c)	1680
Current Price (c)	2125

Year End 30 June	2015A	2016A	F2017	F2018
Revenue (N$ m)	269.4	288.3	301.7	327.0
Vacancies (%)	0.7	2.1	2.0	2.0
HEPU (c)	159.6	163.0	161.2	174.8
HEPU growth (%)	-1.6	2.1	-0.1	8.4
DPU (c)	158.5	167	161.2	174.8
DY (%)	7.9	7.8	7.6	8.2
P/E (x)	12.5	13.1	13.2	12.2
D/A (%)	38.8	29.0	30.2	30.7

Source: ORYX PROPERTIES LIMITED, IJG

Recommendation	SELL
NSX Code	ORY
Market Cap (N$m)	1,655
Shares in Issue (m)	77.9
Free float (%)	100
52 week high (c)	2154
52 week low (c)	2040
Expected Total Return (%)	7.6

FY16 Results Review

Oryx Properties Limited (Oryx) released its results for the financial year ended 30 June 2016, reporting 5.4% distribution growth to 167cpu from 158.5cpu reported for FY15. The distribution was supported by a 1c dividend per unit which is included in the 167cpu. Over the same period EPU decreased by 29%, from 448.11c to 316.64c, largely due to lower fair value adjustments on the property portfolio. HEPU rose by 2.1% to 163.01c in FY16.

Net rental income increased by 1.5% y/y to N$196.7m, in stark contrast to the 19% increase in FY15 as a result of a negative straight line basis adjustment, and higher than anticipated rental expenses. Rental expenses increased by 21% to N$91.5m, close to, but exceeding IJG's expectations. Oryx reported a profit of N$105.6m for the period, down 45% y/y, as a result of lower valuation gains on the property portfolio which is reasonable in the current economic climate.

At FY16 the property portfolio was valued at N$2.326bn, up 8.4% from FY15. This is a less aggressive upward revision in the value of the portfolio than seen in FY15. We are less optimistic about the short term growth potential of the property portfolio than the Oryx management team due to a slowdown in the economy and we expect to see less aggressive valuations of the property portfolio in FY17 and FY18.

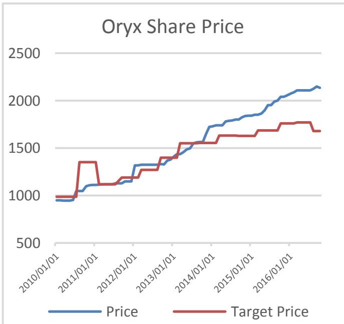
Vacancies as a percent of lettable area grew to 2.1% for the year compared to 0.7% in FY15. The office portfolio accounted for the bulk of the vacancies with 1.1%, retail added 0.6% and industrial 0.4%. The spike in office vacancies was due to a large government tenant relocating to new offices while the Joule Street tenant contributed to the industrial vacancies. At the time that the financials were released vacancies had decreased to 0.5%. Given the economic climate we forecast revenue for FY17 using a 2% vacancy rate.

Net asset value per liked unit increased by 6.2% to 2,034 cents per unit compared to 1,915 cents per unit in FY15, according to the company financials. The Oryx share price is thus trading at a 4.5% premium to net asset value.

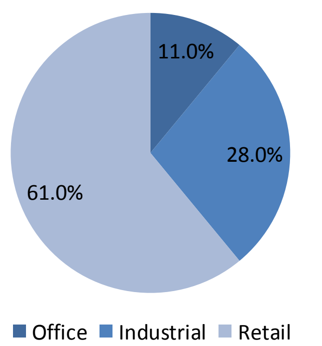
The weighted average interest rate paid on the company's debt has increased to 9.4% as at the end of FY16 from 8.7% at the end of FY15. Financial gearing has dropped to 29% due to the successful rights issue in October 2015 and as a result unutilised borrowing facilities now stand at N$286m. Decreasing relatively more expensive debt by issuing cheaper rights could prudent at present as high yielding opportunities are rare but may become more numerous as the economy moves through this downswing.

The FY17 distribution yield of 7.6% represents a further decline from the previous period's 7.9%, and is based on distributions of 161.2cpu. The average yield on the IJG Generic 10-year bond over the last 14 years is 9.65%. **We have decided to use this as a reasonable benchmark with which to calculate our target price of N$16.80 for FY17**, a 21% discount to the current price of N$21.25. **We therefore change our recommendation from a hold to a SELL.**

Unit Price (c)



Property Portfolio (Revenue Contribution)



Distributions

Notice is hereby given that an interim distribution of 86.75 cents per linked unit was declared for the period ended 30 June 2015.

- Last day to trade cum distribution: 4 September 2015
- First day to trade ex-distribution: 7 September 2015
- Record date: 11 September 2015
- Payment date: 25 September 2015

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Economic environment

Our view of the macroeconomic conditions at the start of 2015 was one of an overheating economy and deteriorating future outlook. Much of our fears have proven to be justified as various high frequency data indicates that the Namibian economy is very likely contracting at present. Government has slashed spending in nominal terms and is reprioritising current expenditure due to disappointing revenue collection and the inability to raise further debt in a sustainable manner. Government spending has in the past been a major driver of economic growth and the extensive budget cuts which are to take place are likely to cause the economy to contract. These conditions above spell tough times for businesses in Namibia.

Revenue

Revenues increased by 7% during FY16, much lower growth than the 31.5% growth experienced in FY15. Much of the FY15 growth was however due to the manner in which rental expense was calculated. The bulk metering of electricity at various properties, notably Maerua Mall, increased rental expenses as well as revenues while providing a margin between the bulk cost of electricity paid by Oryx and the retail cost of electricity collected by Oryx from its tenants. The 31.5% revenue growth exhibited in the FY15 figure is thus offset by increases in rental expense to a large extent. FY16 was the first year in which bulk metering of electricity was captured for a full 12-month period.

Net rental income growth provides a clearer picture of tenant retention, rental escalation, and increases in rental expense not due to the electricity metering changes. Net rental income grew at 1.5% in FY2016, markedly slower than the 19% growth experienced in FY15 and 23.7% seen in FY14. This figure is also lower than our forecast of 6% growth due to higher than expected rental expenses as well as a negative straight line basis adjustment to rental income in the current period. This is the first negative straight line basis adjustment since 2010 and is typical of a period with high renewals and new lease agreements.

According to Oryx 26% of leases expired in FY16. Such a large amount of leases expiring during a single period in which the economy likely contracted, by IJG's estimates, has been challenging to the company. Despite this Oryx states that rental renewals have been successful with rental escalations in excess of 8% for major Namibian and South African retailers. This is offset by vacancies in the smaller units in the mall and thus overall escalations will not be as high as 8%. Stripping out the additional rental income due to electricity costs passed on to tenants as well as the bulk cost of electricity carried in rental expenses shows the extent to which revenue growth disappointed. By adjusting revenue for the electricity component now included in it (and disregarding the margin between what Oryx pays and what clients are charged – would add to the top line), the increase in revenue falls to 2%. The increase in rental expenses, after adjusting for the electricity component, was 4.5% which results in the 1.5% increase in net rental income.

Revenue Growth Projections

The Namibian economy is coming under increasing pressure and this is likely to affect Oryx' tenants broadly. Larger tenants are better able to weather the storm and rental escalations have proven resilient among this class of tenant while various smaller tenants struggle and we assume that rent and rental escalations are more negotiable for this group. We do not expect to see overall rental escalations of 8% in FY17 and have adjusted our revenue forecasts accordingly. We have taken into account the sale of the various Port Elizabeth properties as well which puts further pressure on revenues. However, a lower percentage of GLA up for renewal during the year should relieve some pressure as this should lead to less negotiation on rent for vacated space and more escalations flowing through to revenue as a result of GLA filled in FY16. As a result, we forecast revenue growth of around 4.7% for FY17 and 8.4% for FY18 as new GLA is added.

Expenditure

The net rental expense ratio (with electricity metering stripped out) fell to 12% in FY16 versus 12.9% in FY15. Current economic pressures have resulted in renewed efforts from the management team to reduce costs and improve efficiencies. Other rental expenses were well contained and increased by 4.5% for the year, a slower increase than seen in revenue growth. Total rental expenses grew by N$16 million in FY16 while revenue grew by N$18.89 million (including the straight line basis adjustment) and while the whole N$16 million would not have been due to the bulk metering of electricity it would have made up the vast majority of this increase (N$14 million). This highlights the extent to which revenue growth disappointed.

Other expenses increased by 35.9% in FY16 to N$15.9 million, largely as a result of a N$2.9 million provision for impairment of receivables. This is yet another sign of the current economic climate and the effects of this flowing through to the financial results. Provision for impairment is provided at 50% of the rent balance outstanding for 60 days or 90 days subject to managements discretion, and 100% of the outstanding balance for debt that has aged more than 120 days.

Further contributing to the increase in other expenses was an increase of 12.8% in director's emoluments to a total of N$5.58 million. Executive and non-executive director emoluments increased by similar proportions with the majority of the total balance accruing to the two executive directors.

Borrowings

Oryx' long term borrowing decreased by 20.2% y/y to N$695.9m in FY16, from N$872.1m reported as at FY15. The proceeds from the rights issue on the 30th of September 2015 were partially utilised to reduce gearing from 38.8% in FY15 to 29% in FY16. Total loan facilities amount to N$972.7m which means that as a result of the deleveraging Oryx has access to N$286m with which to fund expansion projects such as the Gustav Voigts upgrade. Oryx' weighted average interest rate for FY16 was 9.4%, moderately higher than the 8.7% rate at the end of FY15. The weighted average interest rate of variable rate borrowings was 9.3% versus 9.4% in FY15.

The ratio of fixed rate to floating rate borrowings was 57:43 at the end of FY16, with four swap contracts hedging exposure to floating rate debt. The weighted average fixed rate of the swap contracts is 7.5% and they are priced against 3 month JIBAR. These contracts mitigate some of the interest rate risk associated with the long term borrowings and are a prudent measure in the current interest rate environment and uncertainty regarding the South African credit rating.

The cost of debt at 9.4% (FY16) is substantially higher than the cost of servicing the debentures and as such raising funds for development and/or acquisitions would be cheaper through further rights issues than utilising debt. In order to justify the use of debt any acquisition or development would need to yield in excess of the cost of the current facilities within a relatively short period of time. Opportunities with the aforementioned characteristic are few and far between in the overheated central Namibian market.

Oryx management continue to look for opportunities in other markets due to the high cost of debt in our own market. Europe may well offer opportunities due to low interest rates and has been flagged by management as a possible next step although there are many hurdles to clear and thus management is taking a risk averse approach to such opportunities.

We still do not feel that at current interest rates Oryx will pursue financing through their registered medium term note program. The facility does however add further room to raise funds should attractive opportunities present themselves.

CEO Change

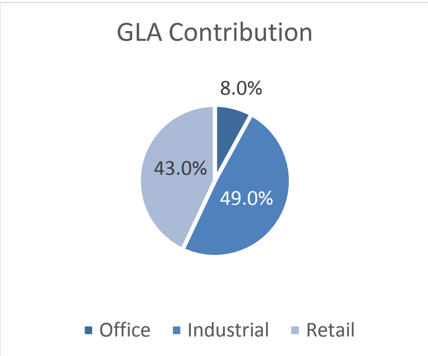
Oryx unitholders were notified on 22 November 2016 that there will be another change in CEO. Effective 28 February 2017, current CEO Gerhard van Zyl will be stepping down from the position he filled on 1 July 2016. Current Chief Operating Officer (COO), Carel Fourie, will be taking over from Mr van Zyl effective 1 March 2017. The company press release stated that the Board and Mr van Zyl mutually agreed that it would be best for Oryx unitholders if the company did not continue operating under the current management structure with both a CEO and COO. We are of the view that Mr Fourie is more than capable of fulfilling the role of CEO and do not see this change in CEO as a reason for concern.

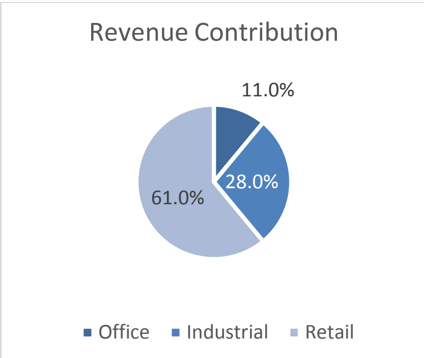
Property Portfolio

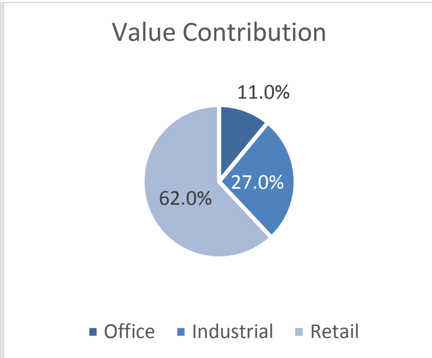
The property portfolio of Oryx was valued at N$2.326 billion for FY2016, 5.5% up from the FY2016 value of N$2.206 billion. The valuation was independently executed by Broll Valuation and Advisory Services using similarly conservative estimates, according to management, as used last year. A fair value gain of N$84.4 million was recorded for the year as a result.

During the year Oryx expended N$95 million on capital projects which partially includes the N$80 million Virgin Active development at Maerua Mall as well as a 1MW solar installation at the retail node. The Virgin Active facility is nearing completion at the time of writing of this report and the tenant is expected to relocate before the end of the calendar year. This is an important development for the Maerua property as Virgin Active has agreed to a 10-year lease, providing stability and predictability of earnings for a large portion of GLA. Similarly, the solar installation has proven to be a yield accretive addition to the Mall, yielding in excess of the expected 13%, and Oryx is exploring the possibility of increasing the output potential to 3MW to take further advantage of expected future tariff hikes.

During the year Oryx sold a single tenant industrial property in Port Elizabeth. The company felt that the risk that the lease would not be renewed in 2018 was too great and as such chose to dispose of the property for N$60.9 million before costs. A loss of N$786,000 attributed to the disposal of the Port Elizabeth property was recorded in the income statement as a result of sales costs. Oryx management concede that the sale of the property will have an "initial dilutionary effect on the portfolio's performance", as the exit yield of the portfolio was 15.2%. An additional sale of two South African properties for N$19 million and N$11 million was agreed upon by the end of the financial year, but not concluded. Subsequent to year end the property valued at N$19 million was sold and a decision was made to retain the smaller property.







Maerua Mall

The largest property in the Oryx portfolio was valued at N$1.231 billion in FY16, N$82 million or 7.1% higher than in FY15, and thus makes up the bulk of the fair value adjustment of N$84.4 million. Rental escalations for the major SA and Namibian tenants have been in excess of 8% for the most part which justifies the fair value adjustment, however smaller tenants have come under some pressure due to the current economic climate. We are concerned that the slowdown in government spending will negatively affect consumption, placing pressure on tenants, especially the more niche tenants.

Renewals were a concern for FY16 as a large portion of the GLA was up for renewal during the year. A total of 96.1% of the retail space rentals that were up for renewal were successfully renewed and tenant retention of 96% for the retail portfolio was achieved. These figures are positive in the current economic climate although they may come at a cost as rental escalations seen in the past are unlikely to be sustainable in the short term (visible in FY16 revenue). Retail vacancies have been kept to a minimum at 0.6% in FY16 versus 0.4% in FY15. Low retail vacancies are once again a positive sign of the resilience of Maerua Mall as well as the other retail properties in the portfolio. Vacancies for the entire node stood at 2.2% in FY2016 with office space making up the bulk of these vacancies.

An issue facing the mall at present is the size of some of the smaller shops. Opportunities exist to place medium sized tenants in the mall but the dispersion and size of smaller vacated shops makes this difficult. These are often not adjacent making it almost impossible to enlarge the stores without displacing or disrupting current tenants. Management is making efforts to accommodate more medium sized tenants and improve the tenant mix but the process is likely to be slow.

The new Virgin Active (VA) premises currently under construction at a development cost of N$80 million is sure to be a positive addition to the Maerua portfolio provided that the space currently occupied by this tenant is effectively utilised. Oryx plans to turn the old VA site into an entertainment and leisure space. Development of this space is expected to start early in 2017 and will include an upgrade or "facelift" to the food court. The Panarotti's is likely to return at some point in 2017 and a John Dory's will complement the current tenant composition.

A focus to stimulate evening trade has been made and the development of the old Virgin Active space as well as the upgraded food court aim to increase foot count during the late afternoon and evening.

Gustav Voigts

The Gustav Voigts upgrade has been in the works for a few years now and has received the go-ahead after the end of the financial year. To quote management, "The upgrade will mostly entail cosmetic changes to the inside of the centre and a relocation of the Avani lobby area to the street front. Also included in the project, will be a new rooftop restaurant and banqueting area for the hotel". These upgrades are to be complemented by the addition of two new parking decks with the whole project budgeted at N$110 million and construction expected to commence early in 2017.

Office Portfolio

The office portion of the Oryx portfolio contributed the bulk of the vacancies for FY2016. A large government tenant vacated the Channel Life building leading to a substantial drop in tenant retention for the entire office portfolio in terms of GLA. This space was subsequently rented out to a number of smaller tenants with the last of the vacancies all filled according to management. Oryx management view the office space as the most competitive of the three sectors due to an oversupply of office space and the preference of tenants to purchase or develop their own space.

Industrial Portfolio

The industrial portfolio makes up 27% of the Oryx property portfolio in terms of value, below the target range of 30% to 40% of total portfolio value. In total 91.4% of the GLA up for rental agreement renewal in the industrial portfolio was renewed during 2016 with much of the rest of the area that was vacated subsequently being filled after year end. All in all, vacancies in the industrial portfolio increased from 0% to 0.4%, and this portion of the portfolio continues to yield good results.

Cap Rates

	Capitalisation Rate %		**Discount Rate %**	
Property Type	**2016**	**2015**	**2016**	**2015**
Retail	8.6	8.7	14.1	14.2
Industrial	9.5	9.9	14.6	15.4
Office	9.5	9.8	15.2	15.6
Portfolio average	9	9.1	14.2	14.4

Source: Oryx Properties

The cap rates used to value the property portfolio have decreased in FY2016 as is evident in the table above. The discount rate used in the property valuation methodology has also been reduced which results in an upward fair value adjustment in a similar manner to lower capitalisation rates. While these rates have decreased only slightly and thus do not provide major reason for concern, we would not expect to see further decreases in these rates going forward due to adverse economic conditions.

Rights Issue

Oryx concluded its rights issue at the end of September 2015 with moderate success as 89.4% of the rights were exercised and 11,809,781 new shares were issued. Rights were issued inclusive of antecedent dividends which supported the full-year distribution and allowed Oryx to increase distributions. The rights issue allowed Oryx to pay down debt with an average interest rate higher than the cost of servicing the debentures. This is a prudent measure in the current economic climate as opportunities are few and far between in the local market and reducing the debt servicing burden should allow for increased funds to flow through to distributions until such a time that higher yielding investments can be made.

Relative comparison

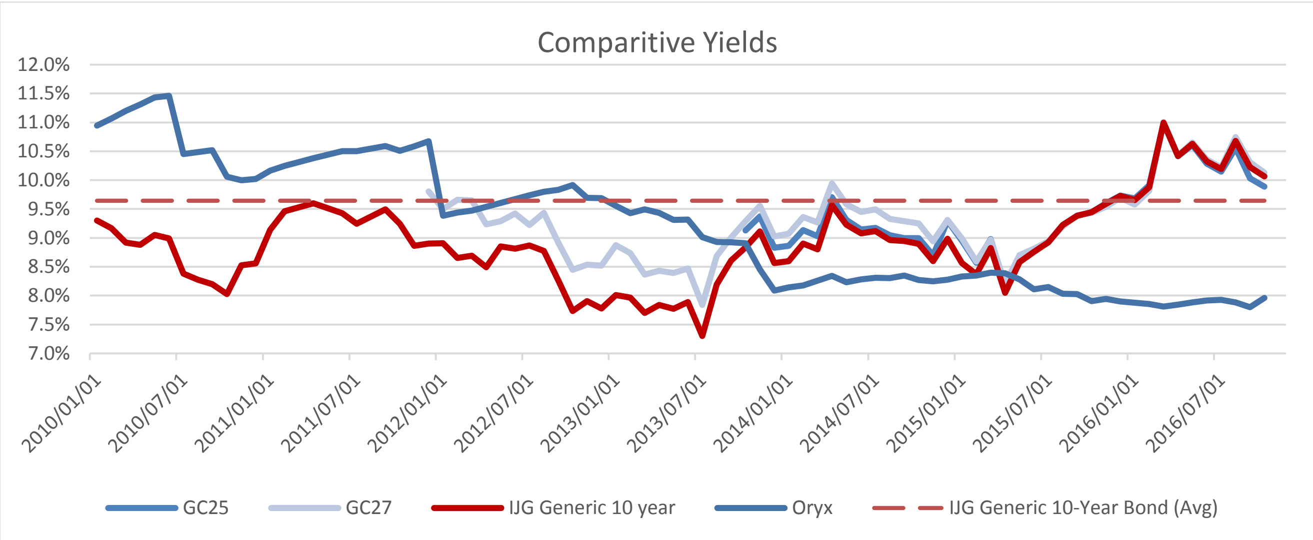
The below figure is a peer comparison composed of JSE listed REITS that Oryx uses as performance benchmarks in order to determine remuneration of key employees. The Oryx annual report highlights the fact that in FY15 Oryx distributions increased by 7.1% versus 10.6% for the top quartile of this peer group. In FY16 Oryx' distributions grew by 5.4% versus 9.7% for the top quartile of the peer group.

The figure below is sorted according to dividend yield with some outlying data removed for comparative purposes.

	Distribution Growth	3Yr Distribution Growth (Bloomberg)	Dividend Yield	Price to Book	Price to Sales	P/E	Market Cap
Texton Property Fund Ltd	10.24	11.27	12.98	0.84	4.68	6.03	3 005
Tower Property Fund Ltd	5.99	Unavailable	12.19	0.76	4.62	10.66	2 568
Delta Property Fund Ltd	8.01	Discredited	11.88	0.72	3.26	14.71	5 429
Arrowhead Properties Ltd	Removed	Discredited	11.78	1.13	5.29	14.41	8 925
Emira Property Fund Ltd	8.81	8.43	10.25	0.82	3.92	8.65	7 275
Dipula Income Fund Ltd	5.00	5.00	9.42	1.06	4.16	5.29	3 982
Fairvest Property Holdings Ltd	10.29	Discredited	9.36	0.88	4.05	9.87	1 189
Vukile Property Fund Ltd	7.00	3.61	8.00	0.99	4.78	10.89	12 639
Accelerate Property Fund Ltd	9.07	Unavailable	7.83	0.95	5.76	12.17	5 889
Oryx Properties Ltd	**5.40**	**6.03**	**7.82**	**1.05**	**3.90**	**13.10**	**1 662**
SA Corporate Real Estate Ltd	10.19	9.92	7.52	1.23	6.89	8.69	13 296
Redefine Properties Ltd	7.21	7.70	7.45	1.06	7.43	14.39	56 192
Growthpoint Properties Ltd	6.00	7.25	7.34	1.01	6.65	17.82	70 894
Investec Property Fund Ltd	Removed	(1.56)	5.83	1.03	7.09	9.86	11 414
Hyprop Investments Ltd	14.16	13.50	5.43	1.21	9.01	9.85	28 377
Average	**8.26**	**7.11**	**9.00**	**0.98**	**5.43**	**11.09**	**15 515.76**

Source: Bloomberg, IJG Securities

In terms of distribution yield Oryx is close to the median value but well down on the average. Distribution growth is lagging behind as highlighted by management in the annual report. The 3-year growth in distributions is below the average as well with price-to-book relatively in line with the average, and price-to-earnings on the high side. The comparison above was compiled using data from Bloomberg and may be inaccurate in some instances although we have tried to account for this where possible. This comparison suggests that Oryx is expensive on multiple measures when compared to its peers and would not be our most preferred purchase from this basket of stocks based on the above fundamentals.



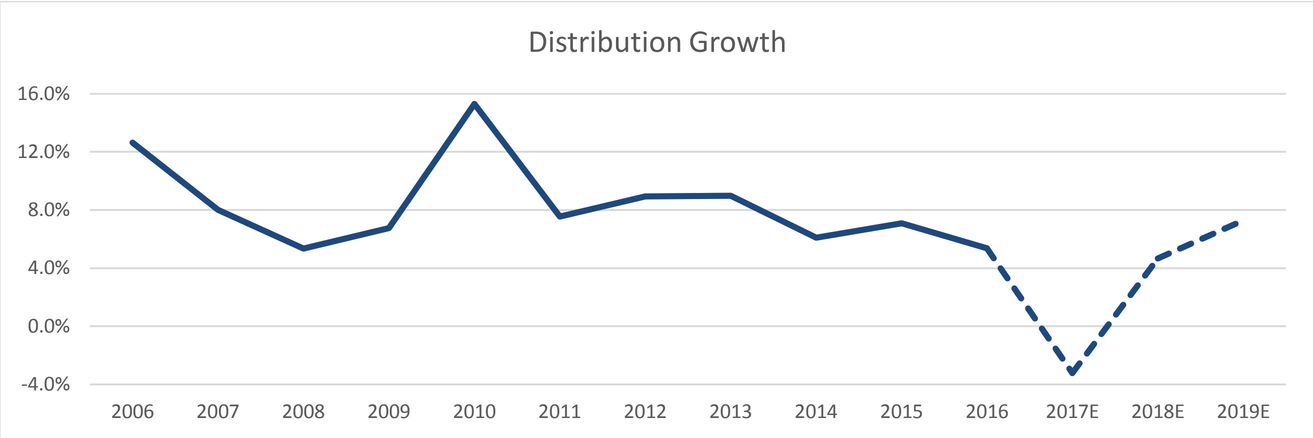
Source: IJG Securities

The above figure compares the Oryx distribution yield to the yield to maturity of the GC25 and GC27 government bonds as well as the IJG Generic 10-year bond. For much of the last seven-odd years the Oryx distribution yield was higher than the yield on government debt. In 2013 the relationship reversed and the Oryx distribution yield has lagged the risk free rate ever since. The Oryx distribution yield has trended lower over most of the comparison period stabilising somewhat around 8% over the last two years while yields on government debt have been trending up. The downward trend in Oryx' distribution yield is due to the share price increasing at a quicker rate than the growth in distributions. Total returns have thus been good over the comparison period, providing investors with annualised total returns of over 21% for the five-year period leading up to the writing of this report.

Valuation

Namibia has been through a period of high growth fuelled by foreign direct investment and rapid increases in government spending. Property prices have risen at elevated rates for a number of years, supported in part by a demand supply mismatch and in part by rapid economic growth. The economy is now showing signs of cooling and we expect that this will lead to some stagnation in property prices as well which will in turn affect Oryx' property valuations. We do not expect to see cap rates decrease, as mentioned earlier, and rental escalations are expected to be lower than has been the case previously. These factors lead us to expect minimal fair value adjustments to the property portfolio for FY17.

We value Oryx on a distribution yield basis relative to the risk free rate as represented by the IJG Generic 10-year bond yield. On this basis Oryx is expensive at present and with few of the up side factors present that previously drove growth in the share price we cannot justify a hold recommendation any longer. Over the last year the average rate on the IJG Generic 10-year bond has been 10.4% versus 9.0% quoted in the IJG FY15 results review. This is a steep increase in the risk free rate compared to the time of writing of the previous full year report. Last year we used the one-year average rate for the IJG Generic 10-year to calculate the target price on Oryx. This rate was chosen as it more closely reflected the risks that we saw in the market at the time. One year later these risks are playing out in the economy and we believe that the next twelve months will be more challenging than the previous twelve.



By our forecasts maintaining distributions for FY17 at the current 167c will be challenging due to rental escalations as a whole disappointing and costs increasing. Maintaining current distributions will be contingent on minimising rental expenses as well as "other expenses". By our forecasts distributions for the period will be in the region of **162c** per linked unit putting further downward pressure on our valuation. Using the aforementioned distribution and a required yield of 10.4% leads to a target price of N$15.60, a 27% discount to the current share price. This is also 22% down from the rights issue price which showed that there was decent support at N$20.00. At that time however, growth expectations for the Namibian economy were substantially higher than they are now.

The average yield on the IJG Generic 10-year bond over the last 14 years (as far back a history as we have for this benchmark) is **9.65%.** Using the average yield over the long term provides a longer term benchmark yield with which to compare Oryx's distribution yield. We have thus decided to use this as a reasonable benchmark with which to calculate our **target price of N$16.80 for FY17**, a 21% discount to the current price of N$21.25.

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