ORYX PROPERTIES LIMITED

Operational Update & Extraordinary General Meeting

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On the 8th of June Oryx released an operational update informing unitholders of the impact that the COVID-19 pandemic has so far had on the business.

Despite most of the lockdown measures being lifted, Oryx notes that many of its tenants are still struggling to operate in the current economic environment. Consumers are under financial strain as many lost their jobs or were forced to take a pay cut, and are not able to spend at the same levels as before. Furthermore, some tenants are still not able to import their required inventory from South Africa due to the fact that its lockdown is more restrictive than Namibia's. As a result of the above mentioned, many tenants are not able to pay their rent. Oryx points out that rental collections for April and May fell by 50% compared to previous months and are expected to continue through the recovery period. Management points out that they are still overwhelmed by requests for rental relief from tenants in all sectors of the economy. These relief packages put considerable strain on Oryx' cashflows. In April alone, N$9.4 million worth of rental relief was passed on to tenants.

The rental relief has at least meant that Oryx has not seen significant increases in vacancy rates thus far. Vacancy rates are still in line with the 1H20 results (4.3%) and are continuously being monitored. Managing vacancies is crucial in our view, as it will be extremely difficult to fill these vacancies on the back of a very difficult economic environment, coupled with a government that could re-implement lockdown measures quite quickly.

While Oryx has passed rental relief on to tenants, it has not received any formal relief from its financiers. The company also noted that the N$100 million loan facility with Standard Bank Namibia that was announced with the 1H20 results has not materialised as intended, which impacts available facilities and cash flows.

In instances where Oryx' financiers made relief packages available, restrictions regarding distribution payments were attached which are beyond the scope of authority of the Board of Directors and are in conflict with the Debenture Trust Deed. Oryx is a loan stock company, not a REIT, and its directors thus cannot decide to cancel or reduce distribution payments without the approval of its unitholders in the same way that its South African REIT counterparts have been able to do.

In Croatia, one of Oryx' tenants, VMD, was granted a 15% rental reduction for April and May and it is expected that assistance will need to be provided to Konzum, which holds the head lease over Croatian retail assets. The depreciation of the Namibian dollar against the Euro in April has resulted in an increase in gearing, but Oryx notes that it remains below the internal limit of 40%. Management notes that any relief measure attained will be in the form of additional debt which will further increase the gearing ratio and affect future capability to obtain funding.

Preserving cash in the business is thus crucial for Oryx' long-term sustainability. The Board's decision to only pay out 90% of distributable income in FY19 has not been in place long enough to improve cashflows significantly.

The above has thus led Oryx to call for an extraordinary General Meeting of the debenture holders on Monday, 29 June 2020 to pass the following special resolutions:

SPECIAL RESOLUTIONS

1	**Waiving of Notice Period** Resolved that the notice period of 21 days to continue with this meeting, be waived.
2	**Interim Debenture Interest Payment** Resolved that, as a result of the impact of the State of Emergency of the Country, due to COVID-19, on the revenue of the Company, the debenture holders enter into a compromise or arrangement with the company **to reduce the interim debenture interest**, declared on 2 March 2020 (distribution number 34) and which is due to debenture holders at this point in time, **to zero,** and debenture holders waive all accrued interest entitlements.
3	**Final Debenture Interest Payment** Resolved that the debenture holders enter into a compromise or arrangement with the company that **accrued interest will be reduced to zero and** that accordingly **no final debenture interest payment will be declared or paid for the financial year ending 30 June 2020**, and debenture holders waive all accrued interest entitlements.
4	**Future Interest Payments** Resolved that the rights of the debenture holders be varied or modified by amending the Debenture Trust Deed to ensure the sustainability of the company, by **placing a moratorium on the payment of interest for the financial year ending 30 June 2021.**
5	**Trust Deed Amendment** Resolved that the rights of the debenture holders be varied or modified to allow the **change of the Debenture Trust Deed** to ensure the sustainability of the company, **by changing the interest entitlement** in par 4.3 of the Sixth Supplemental Debenture Trust Deed to the Principal Debenture Trust deed **from 90% to 75%** and that this reduced interest entitlement shall apply to all debentures in issue at the date hereof with effect from the commencement of the financial year ending 30 June 2022.

In order to protect the company's cashflows and ensure the long-term sustainability of the company, the Board is asking debenture holders for permission to pay out zero distributions in FY20 and FY21 and to change the minimum payout rate from 90% to 75%, effective from FY22. The Board states that the above measures will remove the need for a possible rights issue to debenture holders and allows for long-term decision making.

Impact and Verdict

Our understanding of the resolutions to be voted on is that there are both short-term and long-term components. The short-term issues facing Oryx are largely cash flow related. Tenants are struggling to pay rent and have been accommodated to some extent through rental relief. Given the aforementioned economic climate it is very likely that some tenants would have closed shop leading to an increase in vacancies and thus the rental relief strategy should support a lower vacancy rate than would have been the case without such relief. However, this does lead to cash flow constraints as Oryx still needs to service its debt and pay expenses.

Special resolutions 1 through 4 deal with the short to medium term impact of the current crisis on Oryx and the resulting pressure on cash flows. We believe that the first three resolutions are justifiable and necessary to mitigate the cash flow issues being experienced. It is likely that unitholders will vote in favour of these resolutions, removing much shorter-term pressure from the company. It is unclear whether passing these resolutions will lead to relief from lenders, but we assume not as it would need to be applied retrospectively.

Raising further debt in order to assist the cash flow position will place pressure on the company's gearing ratio, and commercial banks will likely be reluctant to do so unless Oryx waives its distribution payments to unitholders. The only other option is to do a rights issue, which is unlikely to be supported by the majority of unitholders. Oryx' rights issue in 2019 (which was during arguably better economic times) was already not well received/subscribed to by the market. From a long-term sustainability view, we thus agree that it will be in Oryx' best interest to withhold distributions for the current financial year (FY20).

Special resolution number 4 deals with the coming financial year (FY21) which will see continued pressure on Oryx' tenants through second round effects stemming from increased unemployment and a decrease in disposable incomes. In our view it would be beneficial for unitholders to vote in favour of this resolution as it will provide Oryx with flexibility to deal with these challenges. A favourable vote is likely to allow some relief from lenders, further aiding cash flows. However, it implies a second consecutive year of no distributions, and hence special resolution 4 will be met with little enthusiasm from unitholders and we believe that this resolution will be met with more opposition than the first three.

Special resolution number 5 deals with the change in payout ratio of distributable income and is essentially a subtle change in Oryx' business model as the company is trying to align itself with a REIT structure. This resolution thus deals with the longer-term consequences of the current crisis. Historically, the company paid out between 90% and 100% of distributable income (or in some years even more by tapping into realised reserves) to debenture holders. This is easier to do when valuations are steadily going up. The times where capital appreciation and positive property revaluations resulted in the deleveraging of the balance sheet, and thereby enabling debt funded acquisitions, may be behind us for at least the next three to five years.

Lowering the payout ratio to 75% from FY22 means that Oryx can build up capital which frees up balance sheet space for possible future acquisitions and smaller capital expenditure projects, instead of continuously using debt to do so. This makes sense in an environment where upward revaluations of properties are much more uncertain. Management also noted that the capital could possibly be used to repay debt which might be a wise decision due to concerns that commercial banks might be considering offering amortising loans going forward instead of interest-only loans.

Despite the rationale behind lowering the payout ratio and the longer-term flexibility that this provides in a more uncertain environment we believe that this resolution may see even more opposition than special resolution number 4 and is likely to be rejected at this time. We do not necessarily believe that passing this resolution is necessary at next week's meeting and it may be more appropriate to revisit at a later date.

As a property loan stock company Oryx distributes income to investors before company tax, meaning that unitholders are not taxed at a corporate level. Changing the payout ratio, however, means that Oryx will be paying tax on the earnings that it retains, which does detract from the funds retained for balance sheet management. In prior annual statements Oryx has mentioned unused tax losses which are not recognised as deferred tax assets as it was thus far not considered probable that there would be future taxable profits available. This is likely to be reassessed in the event that distributions are deferred and the payout ratio changed which should aid in offsetting corporate taxes to some extent. Taxation is but one consideration that may see unitholders refrain from passing special resolution 5 at the upcoming meeting.

While we understand that the rationale behind the resolutions proposed by Oryx is the focus on stability in the short term and flexibility in the long-term, we argue that it might be better to let unitholders vote on the payout of future distributions in future financial periods. There is still a lot of uncertainty surrounding the impact of COVID-19 which will make planning difficult. It furthermore makes it less compelling for unitholders to stay invested in the company if lower or no distributions will be paid out in future.

Valuation

This report does not constitute a target price update as the special resolutions to be voted on by Oryx' unitholders may necessitate changes to our valuation model. To the extent that the special resolutions are passed we may change our valuation methodology of the company as a comparative yield basis may no longer be appropriate. The earnings guidance from the operating update is furthermore still in line with our expectations. Thus, for the time being, we leave our **target price for Oryx unchanged at N$1491c per unit**. The elevated unit price currently makes Oryx an unattractive purchase and as such we maintain our **SELL** recommendation on the stock.

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