

Analysis

Moody's Global Corporate Finance

November 2009

Growthpoint Properties Limited

South Africa

Corporate Profile

Growthpoint Properties Limited (Growthpoint), rated Baa2, was established in 1987 and is the largest listed property company by assets in South Africa. Its investment and development activities focus on a portfolio of over 430 retail, office and industrial properties that are geographically diversified across South Africa, Namibia and Australia.

As a Property Loan Stock (PLS) company, Growthpoint operates in a similar manner to a REIT (Real Estate Investment Trust), investing in and holding properties in a tax efficient manner for investors. As a PLS, Growthpoint's equity is composed of linked units - ordinary shares linked to unsecured, subordinated, variable rate debentures. Its unitholders are broadly spread with no single investor holding more than 10% with the exception of Public Investment Corporation (PIC) with a 29.1% holding. PIC is the manager of the South African government employees' pension fund. Refer to Figure 1 below for the spread of unitholders.

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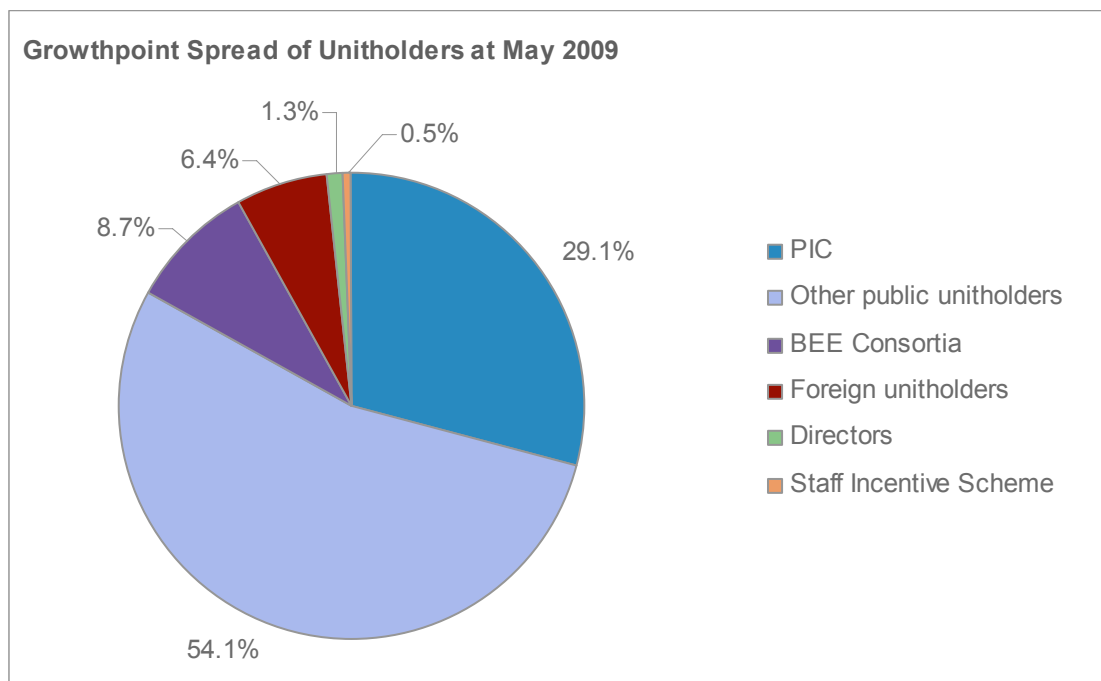
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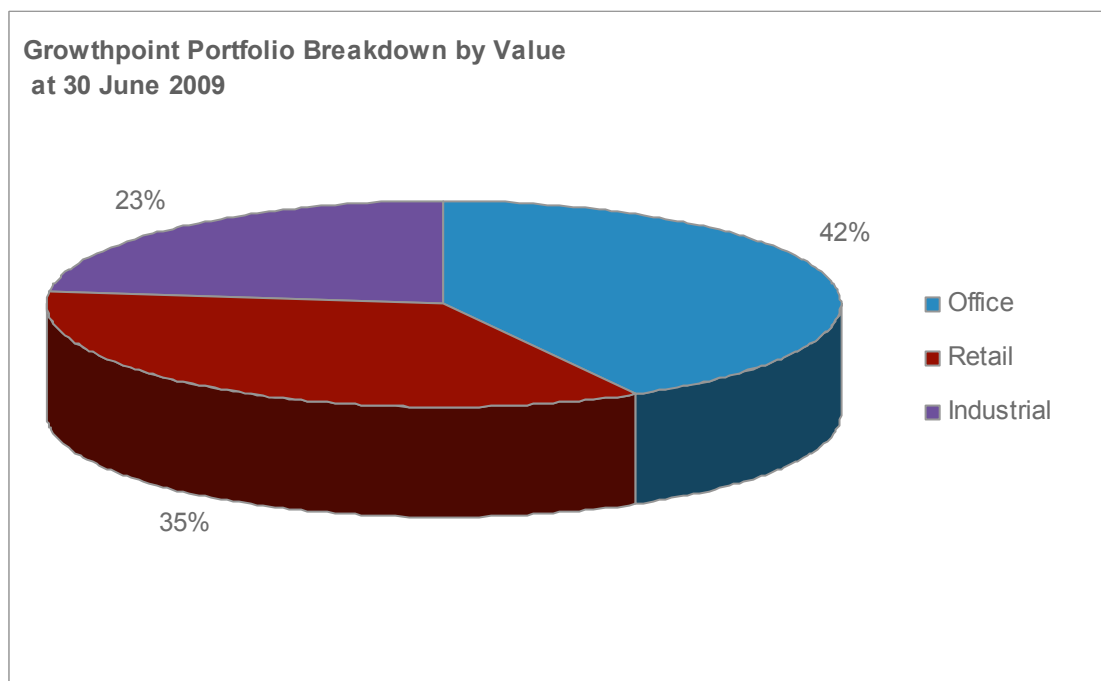
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Figure 1



At financial year-end 30 June 2009, the Company reported total property assets valued at R29.2 billion, producing gross revenues of R3.4 billion. For a breakdown of the property portfolio by sector, refer to Figure 2 below.

Figure 2



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Rating Rationale

The Baa2 long-term issuer rating reflects the size and quality of Growthpoint's property portfolio, which benefits from an active internal property management team and produces a solid, recurring rental income stream underpinned by (i) medium- to long-term leases, (ii) contractual annual rent escalation clauses, (ii) low vacancy rates, and (iii) a diversified tenant base. The properties are further diversified by sector – retail, office and industrial; however, a constraining factor is the geographic concentration of the portfolio; more than half of the properties by value are located in the province of Gauteng, South Africa, and rental levels and values are reliant on a relatively small economic area.

The ratings also incorporate Growthpoint's relatively strong credit metrics, with low leverage as measured by adjusted net debt/EBITDA of 3.6x and adjusted debt/property assets at 34% with good fixed charge coverage of 2.8x. However, the strength of the company's credit metrics is constrained by the high proportion of assets that are secured by debt. The ratio of secured debt to gross property assets at 34% is higher than its entire similarly-rated global peer group. Downward pressure on the rating would occur if the level of secured debt to property assets moves towards 40%.

The Group's liquidity risk profile is good; cash flow from operations and available credit facilities cover cash outflows and debt maturities over the next 12 months. Growthpoint has continued access to both debt and equity capital and has sufficient cash availability to repay the R1.6 billion maturing CMBS in November 2009. The ratings also factor in the modest development risk taken by the group, which is limited to letting risk on predominantly pre-let development projects. However, the rating assumes no material or transformational acquisitions take place.

The company recently acquired a listed property trust in Australia, which is characterized by good quality property and strong tenants. Growthpoint has also acquired an experienced property management team. A constraining factor on the rating is the possible extent to which this distant overseas acquisition will distract senior management from the core business in South Africa.

The principal methodology used in rating Growthpoint was Moody's Rating Methodology for REITs and Other Commercial Property Firms, published January 2006, and available on www.moodys.com in the Ratings Methodology subdirectory under the Research & Ratings tab. Growthpoint's overall performance measurements relative to the rating methodology indicate a rating score of Baa2, which at the same level as the long-term issuer rating.

Rating Drivers

The factors that influence Growthpoint's ratings are as follows:

Market Position and Asset Quality

Growthpoint's Baa2 rating is underpinned by the size and quality of its relatively new investment property portfolio that has an average age of less than 10 years. The buildings are of modern specification and are closely managed by the company's internal management team. Its multi-sector investment strategy provides diversification across a broader spectrum of the modestly-sized South African economy.

Growthpoint's tenants present a well-spread mix. The top 20 tenants by gross monthly income amount to around 24% of total rental income, of which approximately 10% are rated investment grade or non-rated blue chip office tenants and include the South African government (3%) and three major South African banks. The Company's larger retail tenant exposures are to some of the country's pre-eminent retail brands.

The South African economy is in recession and the property market is experiencing a downturn; however, values have not fallen as dramatically as in many other parts of the world because the banking sector has proved to be healthier. Funding is still generally available to South African companies, which have not faced problems of being unable to refinance debt. While tenants and property values have been fairly resilient, operating conditions have deteriorated. Newly completed office developments acquired since January 2009

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have been difficult to let at feasibility rents. Furthermore, the rate of defaulting tenants has increased, although arrears and bad debts are still low. The geographic concentration of the property portfolio in the province of Gauteng in South Africa is a constraining factor in the rating.

Growthpoint has a strong market position as the largest property loan stock company in South Africa. Given its size, Growthpoint will see most important property transactions on offer in South Africa. When the market recovers, the company will be among the first of its peers to benefit.

The current valuations of Growthpoint's South African properties are at a substantial discount to replacement cost (63%). Building costs are high and there is a shortage of zoned and serviced land, skilled labour and electricity. Although replacement costs are not expected to grow at the same high rate as the past few years, Growthpoint's average passing rents are likely to remain below the level of rent that would be required for new developments to be feasible. Therefore, incumbent property owners have an advantage because competing new supply in the market is unlikely for some time.

In July 2009, Growthpoint acquired a 50.1% controlling shareholding in Orchard Industrial Property Fund (OIF) for A\$55.6 million, approximately R361 million, and renamed it Growthpoint Properties Australia (GOZ). Shortly thereafter, GOZ's unitholders approved a rights issue, following which Growthpoint acquired for A\$140 million an additional 26.1% of units and its ownership rose to 76.2%. The proceeds of the rights issue were used to reduce the level of indebtedness. Key aspects of the transaction were:

- The company maintains its Australian public listing under the ticker "GOZ"
- Internalisation of Australian management team from the external fund manager
- Debt facilities reduced from about 75% to 50% loan-to-value and maturities extended until 2012

GOZ owns 23 industrial properties that are located in major metropolitan areas of Australia valued at A\$643 million (R4.18 billion) at 30 June 2009.

Cash Flows and Earnings

Growthpoint's ratings are underpinned by the sustainable rental income generated from medium-term leases from well-located properties let to a diversified tenant base across three property sectors in South Africa, Namibia and Australia. The vast majority of Growthpoint's leases are for terms of 3 to 5 years. While the company's average lease term of 4.2 years is similar to that in the US, it is shorter than what is generally seen across Europe where leases tend to be longer and span a wider range, from 5 to 25 years, depending on the property sector.

Growthpoint's consolidated annual revenue in FY2009 was R3.4 billion. The 18.4% year-on-year increase in gross revenue was due in large part to acquisitions that contributed R400 million. Like-for-like rental growth was 9.8% from 2008 to 2009 (excluding the Investec, which has a different rent escalation mechanism). Per sector, the like-for-like increases were: office 10.0%, retail 9.0% and industrial 10.5%.

Growthpoint is highly profitable compared to its global peers, as measured by the EBITDA margin at 78% for FY2009 and which has shown low volatility over the past four years. The company's financial profile is further supported by a good fixed charge cover (EBITDA to gross interest expense) of 2.8x owing to the moderate level of borrowings and a policy to hedge at least 75% of its borrowing costs.

Commercial leases in South Africa and Australia contain rent escalation clauses. In South Africa they currently range from around 8% to 9%, but in Australia the escalation rate is related to inflation and is currently about 2% per annum.

Growthpoint's vacancy rates are 5.4% overall, higher than estimates of South African overall property vacancies that are forecast to increase to 4.4% in 2009 from 3.5% in 2008. The company's higher than average vacancy level is due to the acquisition of the above-mentioned newly completed office properties, some of which were not fully pre-let, and it has proved more difficult to let the new space than was originally anticipated. Nevertheless, the drop in tenant demand has also restricted the start of new developments and, when conditions improve, the lack of new supply will improve the letting prospects of these new buildings.

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There is still good demand for retail space in well established centres, but smaller neighbourhood and community centres are not faring as well. Tenant demand for new industrial space is slowing and there are an increasing number of business failures among smaller industrial clients – especially those exposed to the auto, manufacturing and mining sectors. Growthpoint's vacancy rate by property sector at 30 July 2009 was: Office - 8.9%, but more modest levels experienced by Retail - 3.2% and Industrial - 4.4%.

Developments for Growthpoint comprise extensions of existing properties, redevelopments/ upgrades driven by tenant demand, and the acquisition of newly developed properties. With respect to newly developed properties, the company will take letting risk, provided the project is around 75% pre-let, but will not take construction risk. It will actively participate in the concept and design of developments, but enters into forward agreements with developers who take the development risk. Growthpoint has the appetite for growth and a strong balance sheet to acquire newly developed properties when market conditions are right; however, at present it has no pipeline of forward purchase agreements. Our stable outlook assumes the absence of large transformational acquisitions of developments and/or property portfolios.

Liquidity and Funding

Growthpoint's liquidity is good; sources of cash from operations, cash on hand and undrawn committed financing as at 30 June 2009 were sufficient to cover its cash requirements for the next 12 months, including the repayment of its R1.6 billion CMBS that matures in November 2009.

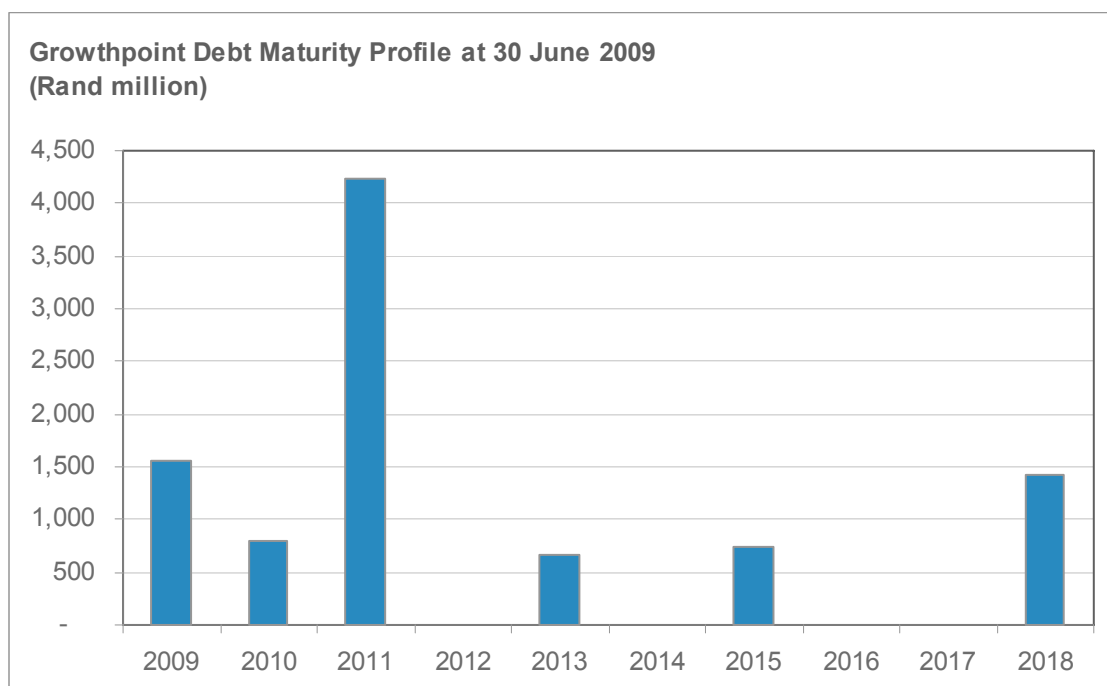
The funding markets are still open in South Africa and Growthpoint is considered one of the better credit risks in South Africa because of its importance within its sector. The company has more offers of finance than it requires at present. In the past six months, the company raised R1.265 billion in an equity raising exercise (more than twice over-subscribed) as well as an additional R500 million from its shareholders reinvesting their distributions into more linked securities.

Property Loan Stock companies generally distribute all their net operating profits, mainly as debenture interest with the balance being paid out as a dividend. Property acquisitions are financed through a combination of debt and the raising of new capital. Property churn carries a cost from a tax perspective as PLS companies are currently liable for capital gains tax on profits earned on the sale of properties.

Growthpoint's debt maturity profile is lumpy, with R3.17 billion to be refinanced during the course of 2011, but the company has already arranged sufficient bank credit facilities to refinance around half the total amount. (Refer to Figure 3) It is also establishing an unsecured R5.0 billion medium term note programme. It plans to use this initially for the issuance of short term commercial paper. Moody's expects the company to have sufficient liquidity to complete debt refinancings at least twelve months before their respective maturity dates.

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Figure 3



Leverage and Capital Structure

As a PLS, Growthpoint's capital structure is composed of linked units. These are ordinary shares linked to unsecured, subordinated, variable rate debentures in the ratio of one ordinary share of five cents linked to ten debentures of 250 cents each. Debenture interest is payable from net operating profits; if there are no profits, no interest payment is made. The linked securities enable PLS companies to pay a low rate of tax and these companies can be compared to REITs in other countries.

Moody's considers the linked units as equity in its analysis because all PLS companies in South Africa issue linked securities and, in the case of Growthpoint, its Memorandum of Association does not allow the company to issue any other form of share capital.

South African property companies have traditionally favoured secured debt - bank loans and CMBS - and Growthpoint is no exception. While it has low leverage, virtually all of its outstanding debt has been issued on a secured basis. At FYE 2009 leverage, as measured by adjusted net debt to EBITDA, was 3.6x and has improved in each of the past four years. Leverage, measured by adjusted total debt to gross property assets, has been stable over the past four years in a narrow range of 33% - 36% and at FYE 2009 it was 34.4%. Growthpoint's leverage is forecast to increase somewhat during FY2010. We expect adjusted net debt/ EBITDA to increase to 3.8x from 3.6x and adjusted total debt/ gross property assets to 37.5% from 34.4%. Adding further, incremental secured debt and exceeding the forecast level going forward would put downward pressure on the rating. We will monitor the extent to which secured debt increases compared to property assets because a rise approaching 40% would be increasingly disadvantageous to unsecured creditors and at that point we would therefore consider notching down the senior unsecured rating.

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Internal and External Factors

Management's strategy is to generate consistent, reliable income and long-term capital appreciation. Senior management's experience of corporate finance gives the company its strong M&A capabilities. Given Growthpoint's already large presence in South Africa, management believe that making well-targeted acquisitions abroad will improve portfolio diversification.

The company recently acquired a listed property trust in Australia, which is characterized by good quality industrial properties, strong tenants and an experienced internal property management team. A constraining factor on the rating is the possible extent to which this distant overseas acquisition will distract senior management from the core business in South Africa.

Figure 4

REITs / REOCs	Aaa-Aa	A	Baa	Ba	B
Factor 1: Liquidity & Funding					
a) Line of Credit Availability (LOC)				X	
b) Max. Annual Debt Maturity					32%
c) FFO Payout Ratio					>100%
d) Unencumbered Assets					17%
Factor 2: Leverage & Capital Structure					
a) Debt + Preferred / Gross Assets			34%		
b) Net Debt / EBITDA			3.6x		
c) Secured Debt / Gross Assets					34%
d) Access to Capital			Good		
Factor 3: Market Position & Asset Quality					
a) Franchise / Brand Name		Excellent			
b) Gross Assets (US\$ Billion)			4.5		
c) Diversity - location/tenant/industry/economic			Good		
d) Development % Gross Assets		X			
e) Asset Quality		Excellent			
Factor 4: Cash Flow & Earnings					
a) EBITDA / Revenues	78%				
b) Standard Deviation ROAA			2%		
c) ROAA			5%		
d) Fixed Charge Coverage			2.8x		
Factor 5: Internal & External Factors					
a) Management			Good		
b) JV / Fund Business % Revenues		6%			
Rating:					
a) Indicated Rating from Methodology			Baa2		
b) Actual Rating Assigned			Baa2		

[1] Based on 30 June 2009 consolidated accounts

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Peer Comparison

The table below shows the financial metrics of seven similarly-rated REITs. The United States REITs are all invested in a single-sector; however, Hammerson plc is a British REIT that is 70% retail/30% offices.

Figure 5

Company Name	Sector	Date	Gross Assets (\$m)	EBITDA Margin %	EBITDA / Interest Expense	Debt / EBITDA	Debt/ Gross Assets	Secured Debt/ Gross Assets
Growthpoint Properties - Baa2 STA	Mixed	30-Jun-09	3,846,890	78.00%	2.80x	3.60x	34.00%	34.00%
National Retail Properties - Baa2 STA	Retail	30-Jun-09	2,802,437	81.40%	3.10x	4.90x	40.00%	0.90%
Regency Centres - Baa2 STA	Retail	30-Jun-09	4,864,104	57.80%	1.90x	7.00x	48.20%	6.00%
Hammerson plc - Baa2 NEG	Retail	30-Jun-09	7,755,000	65.70%	1.30x	9.90x	51.00%	1.30%
Mack-Cali Realty - Baa2 STA	Office	30-Jun-09	5,608,535	54.80%	3.00x	5.10x	37.00%	13.50%
HPRT - Baa2 STA	Office	30-Jun-09	6,749,617	52.10%	2.10x	5.80x	37.70%	6.60%
Liberty Properties Trust Baa2 STA	Office	30-Jun-09	6,633,240	62.80%	2.50x	5.20x	49.90%	11.70%
ProLogis- Baa2 NEG	Industrial	30-Jun-09	18,740,730	71.80%	3.10x	6.30x	45.20%	6.80%

We can see from the peer comparison in Figure 4 above that while Growthpoint Properties is one of the smaller Baa2-rated REITs, but it is a very profitable company as evidenced by its 78% EBITDA margin. Furthermore, it has the lowest leverage and interest coverage is at the upper end of the spectrum. The one factor that is a negative outlier for Growthpoint is the high proportion of secured debt to gross assets.

Liquidity Profile

We view Growthpoint's liquidity risk profile as good and have assumed that the refinancing of upcoming debt maturities will have been arranged at least twelve months prior to the maturity dates. Our overall assessment takes into account restrictions in terms of material adverse change clauses and/or financial covenants. More detail is contained in the section on Liquidity and Funding.

Key Covenants

Growthpoint's credit facilities are provided by a variety of leading South African banks and are subject to relatively few covenants and continuing MAC clause, however there is a 30 day remedy period for the material adverse change. At present there is ample headroom between the company's credit metrics and the loan covenant ratios, as illustrated in Figure 5 and Figure 6.

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Figure 6

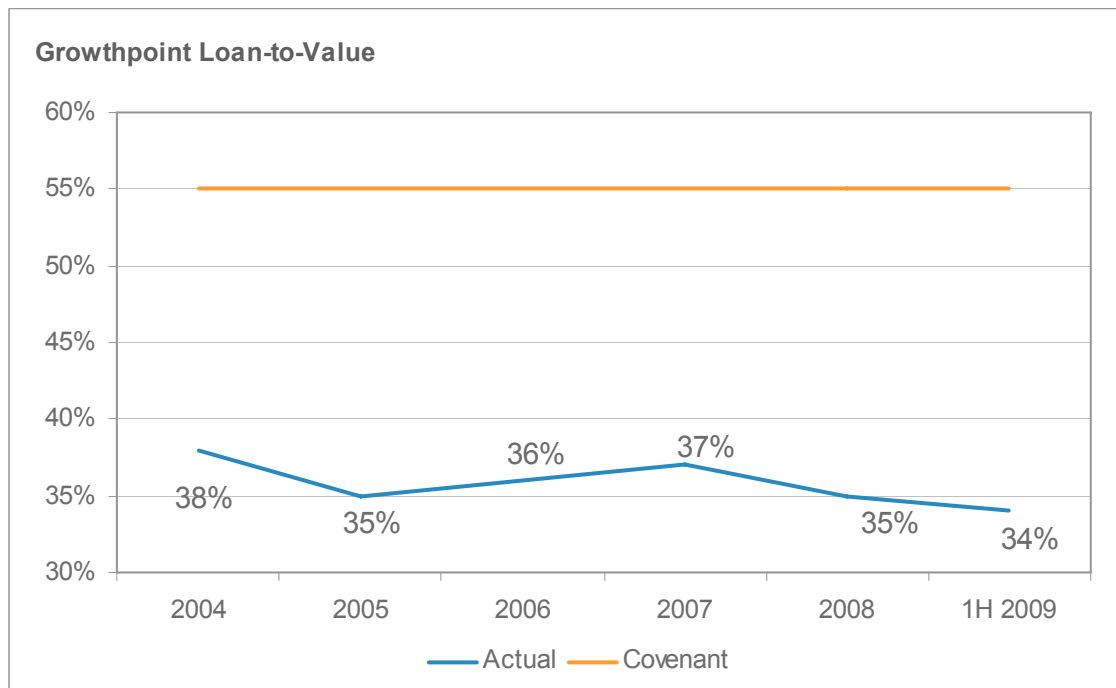
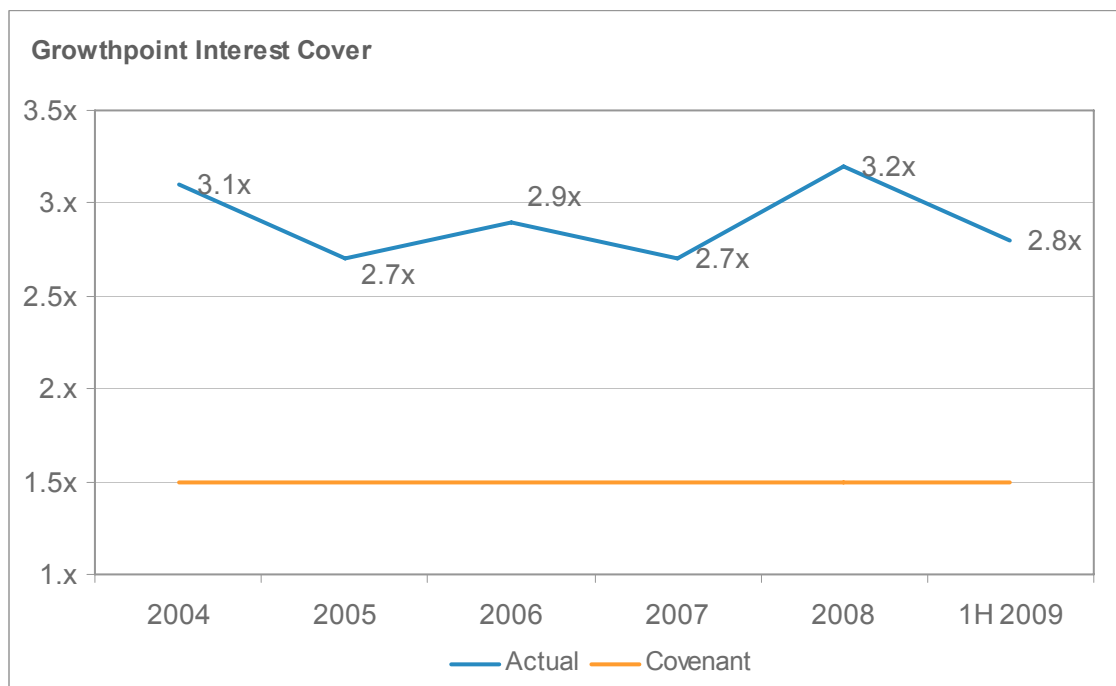


Figure 7



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Rating Outlook

Growthpoint is well positioned within its rating and the outlook for the Baa2 rating is stable. The stable outlook reflects our view that despite a weakening economic climate in South Africa, Growthpoint will continue to produce steady revenues and operating profits. The stable outlook also assumes that management will continue its financial policy to maintain (i) secured debt to total property assets close to current levels at around 35%, (ii) low leverage - both secured and unsecured and measured by adjusted net debt to EBITDA - at less than 4.0x, (iii) fixed charge coverage well above 2.5x and preserve its good liquidity profile. We note that the company has grown quickly but that acquisitions have been in sizes that the company could relatively easily digest, such as the recent acquisition in Australia, and the stable outlook assumes the absence of large, transformational future acquisitions.

What Could Change the Rating - Up

Positive pressure on the ratings is currently constrained by the level of secured debt and is unlikely in the short term. It would nevertheless start building if Growthpoint were to maintain its good liquidity risk profile, reduce the amount of secured debt to assets to at least less than 20% and improve its credit metrics, with inter alia , interest coverage of at least 3 times.

What Could Change the Rating - Down

The following could place downward pressure on the ratings: (i) a deterioration of the company's liquidity risk profile, (ii) unexpected merger/acquisition woes, (iii) secured debt to property assets rising towards 40%, (iv) a shift in leverage with adjusted net debt to EBITDA rising above 4.0x, or (v) adjusted total debt (secured and unsecured) to gross property assets increasing above 40%, or (vi) fixed charge coverage falling below 2.5x.

Moody's Related Research

Rating Methodologies

- Rating Methodology for REITs and Other Commercial Property Firms, January 2006 (96211)
- Key Ratios For Rating REITs and Other Commercial Property Firms, May 2007 (102760)

To access any of these reports, click on the entry above. Note that these references are current as of the date of publication of this report and that more recent reports may be available. All research may not be available to all clients.

Related Websites

Growthpoint Properties Limited

www.growthpoint.co.za

Growthpoint Properties Limited

Report Number: 120930

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