

# Regional REIT

Retail eligible bond 4.5% 2024

Launch of bond issue

Despite continuing Brexit uncertainty and some slowing of UK economic growth regional property markets have remained robust in recent months, with industrial and office properties benefiting from a continuing positive supply-demand balance. Against this backdrop, Regional REIT (RGL) continues to actively manage its portfolio and has also launched an offer of retail-eligible bonds at a fixed rate of 4.5%. The bonds are intended to diversify and enhance RGL's overall debt portfolio and provide added flexibility as the group targets a medium term reduction in gearing from current levels.

Year end	Net rental income (£m)	Adj. EPRA EPS* (p)	EPRA NAV/ share (p)	DPS (p)	P/EPRA NAV (x)	Yield (%)
12/15**	4.6	0.9	107.8	1.00	0.88	1.1
12/16	38.1	7.8	106.9	7.65	0.88	8.1
12/17	45.8	8.6	105.9	7.85	0.89	8.3

Note: \*Adj. EPRA EPS excludes exceptional expenses and estimated performance fees.

\*\*56-day trading period only.

## Regional markets have remained robust

We have suspended our forecasts pending completion of the bond offering. However, we note that in its 17 May 2018 trading statement, RGL pointed to a continuing good performance in the industrial and office occupancy markets of the UK's regions, despite the economic and political uncertainties posed by Brexit. It said that it expected to benefit from this and remained confident of its ability to grow income, decrease the void rate and increase occupancy in the current year. This positive view was underpinned by the group's active asset management of existing assets and recent acquisitions. Over the past few months, it has continued to be active in recycling capital and has recently announced the completion of a number of significant property transactions, both acquisition and disposal. Early in July, RGL announced the completion of the sale of a regionally diverse industrial portfolio comprising 15 properties. The sale price was £39.1m, a 24.1% uplift versus the 31 December 2017 valuation, generating a gain of c £7.5m or c 2p per share.

## Retail eligible bond offering

The bond offer proceeds will enable RGL to part repay certain external debt facilities, will further diversify its sources of funding, and will extend the average maturity profile of its overall debt. The offer was launched on 18 July 2018 and the offer period runs until 12 noon on 1 August 2018. The bonds are unsecured and will pay a fixed rate of 4.5%, semi-annually in arrears, until maturity on 6 August 2024. The minimum initial subscription is £2,000 and the bonds are available in multiples of £100 thereafter. The bonds are expected to be listed on the Official List of the UK Listing Authority and admitted to trading on the regulated market of the London Stock Exchange (LSE). It is expected that the bonds will be eligible for the LSE's electronic Order book for Retail Bonds (ORB). We provide a summary of the key terms on page 3.

Real estate

20 July 2018

**Price** 94.4p  
**Market cap** £352m

Net debt (£m) at 31 March 2018	319.0
Net LTV at 31 March 2018	43.9%
Shares in issue	372.8m
Free float	97%
Code	RGL
Primary exchange	LSE
Secondary exchange	N/A

### Share price performance



%	1m	3m	12m
Abs	(0.2)	(5.8)	(8.8)
Rel (local)	(0.6)	(10.1)	(12.6)
52-week high/low	104.72p	93.7p	

### Business description

Regional REIT owns a highly diversified commercial property portfolio of predominantly offices and light industrial units located in the regional centres of the UK. It is actively managed and targets a total shareholder return of 10-15% with a strong focus on income.

### Next events

Q2 DPS announcement	31 August 2018
Interim results	11 September 2018

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## Capital recycling has continued in FY18

Since end-FY17, RGL has continued to take advantage of opportunities to recycle capital on properties that have met the individual plans set out for them by the investment manager. In its 17 May 2018 trading update, RGL reported on a number of property transactions, including the completion, in Q118, of disposals agreed in H217, amounting to £18.2m net of costs. Average sales prices on the disposals were 19.3% above the H117 valuations. Also during Q118, RGL completed the £4.9m acquisition of an office building at Port Solent, as part of the Northwood Investors transaction entered into in late 2017.

As at 31 March 2018, the investment portfolio was valued at £726.9m, comprising 160 properties and 1,339 individual letting units, with a total of nearly 1,000 tenants with a combined contracted rent roll of £61.7m on a weighted average unexpired lease term of 5.3 years (3.5 years to first break). The net initial yield on the portfolio at the end of FY17 was 6.5% and the reversionary yield was 9.2%.

More recently, on 20 June 2018, RGL announced the sale of The Point Trade & Retail Park in Glasgow, for £14.1m, 5.6% above the 31 December 2017 valuation, and completed the transaction on 5 July 2018. That was followed by the announced completion of the £35.2m acquisition of five regional offices and one office/distribution property on 26 June, and the announced completion of the sale of a regionally diverse industrial portfolio, comprising 15 properties, for £39.1m. The sale price of the latter represented a 24.1% uplift versus the 31 December 2017 valuation.

Announced sales since the beginning of FY18 are running ahead of announced acquisitions, although the asset manager reports having identified a strong pipeline of prospective investment opportunities.

## Further debt management opportunities

RGL uses gearing to enhance returns, where it believes this appropriate. End-FY17 net gearing, represented by the net loan-to-value ratio (LTV) was 45.0%, and was c 44.0% at end-Q118. Based on current market conditions, the board of RGL believes 40% LTV is a reasonable medium-term target, with a maximum level of 50%. The bond offer proceeds will enable RGL to part repay certain external debt facilities, will further diversify its sources of funding, and will extend the average maturity profile of its overall debt. A significant refinancing in December 2017 substantially simplified the group debt structure and increased average maturity from 2.5 to 6.2 years (as at 31 December 2017). We show the end-FY17 group debt facilities in Exhibit 1 and draw particular attention to the zero dividend preference share (ZDP) funding. The ZDP was acquired as part of the Conygar transaction in 2017 and matures in January 2019. Although the interest rate is shown as zero, it accrues at a rate of 6.5% pa, considerably above the blended average cost of debt.

**Exhibit 1: Summary of debt facilities as at 31 December 2017**

Debt provider	Total facility (£'000s)	Annual interest rate	Maturity
Regional REIT ZDP plc	39,869	0%	January 2019
ICG Longbow	65,000	Fixed 5.00%	August 2019
Royal Bank of Scotland	19,336	Libor plus 2.00%	December 2020
HSBC	20,998	Libor plus 2.15%	December 2021
Santander UK	70,700	Libor plus 2.15%	November 2022
Scottish Widows & Aviva Investors Real Estate Finance	165,000	Fixed 3.28%	December 2027

Source: Regional REIT

## Bond issue details

We show a summary of the key terms of the bond in Exhibit 2 and note that the prospectus and other important information are available on the RGL website, [www.regionalreit.com](http://www.regionalreit.com). Given the level of the minimum subscription, in addition to institutional and sophisticated investors, the bonds may also appeal to other private investors acting on the advice of their stockbrokers and financial advisers.

### Exhibit 2: Key terms of bond issue

Issuer	Regional REIT
ISIN number	XS1849479602
Listing	London Stock Exchange, ORB
Issue size	N/A
Selling restrictions	Only to be sold in UK, Isle of Man, and Channel Islands
Repayment	Bullet
Lead Manager	Peel Hunt
Authorised distributors	AJ Bell, iDealing, Redmayne Bentley initially confirmed
Coupon	4.5% semi-annual in arrears
Maturity	6 August 2024
Issue price	100% of nominal
Minimum investment	£2,000
Denominations	£100

Source: Regional REIT

**Exhibit 3: Financial summary**

Year end 31 December (£000's)	2015	2016	2017
PROFIT & LOSS	IFRS	IFRS	IFRS
Gross rental income	5,361	42,994	52,349
Non-recoverable property costs	(754)	(4,866)	(6,502)
Revenue	4,608	38,128	45,847
Administrative expenses (excluding performance fees)	(1,353)	(7,968)	(7,819)
Performance fees	0	(249)	(1,610)
EBITDA	3,255	29,911	36,418
EPRA cost ratio	N/M	29.6%	29.7%
EPRA cost ratio excluding performance fee	N/M	29.0%	26.6%
Gain on disposal of investment properties	87	518	1,234
Change in fair value of investment properties	23,784	(6,751)	5,893
Operating profit before financing costs	27,126	23,678	43,545
Exceptional items	(5,296)	0	0
Net finance expense	(820)	(8,629)	(14,513)
Net movement in the fair value of derivative financial investments and impairment of goodwill	115	(1,654)	(340)
Profit Before Tax	21,124	13,395	28,692
Tax	0	23	(1,632)
Profit After Tax (FRS 3)	21,124	13,418	27,060
Adjusted for the following:			
Net gain/(loss) on revaluation	(23,784)	6,751	(5,893)
Net movement in the fair value of derivative financial investments	(180)	865	(407)
Gain on disposal of investment properties	(86)	(518)	(1,234)
Other EPRA adjustments	0	557	3,064
Deferred tax adjustment	0	0	1,424
EPRA earnings	(2,926)	21,073	24,014
Performance fees	0	249	1,610
Exceptional items	5,296	0	0
Adjusted EPRA earnings	2,371	21,322	25,624
Period end number of shares (m)	274.2	274.2	372.8
Fully diluted average number of shares outstanding (m)	274.2	274.3	297.7
IFRS EPS - fully diluted (p)	7.7	4.9	9.7
EPRA EPS - adjusted (p)	0.9	7.8	8.6
EPRA EPS	(1.1)	7.7	8.1
Dividend per share (p) - declared basis	1.00	7.65	7.85
Dividend cover	N/A	102%	110%
BALANCE SHEET			
Non-current assets	407,492	506,401	740,928
Investment properties	403,703	502,425	737,330
Other non-current assets	3,790	3,976	3,598
Current Assets	35,803	27,574	66,587
Other current assets	11,848	11,375	21,947
Cash and equivalents	23,954	16,199	44,640
Current Liabilities	(21,485)	(23,285)	(42,644)
Bank and loan borrowings - current	(200)	0	(400)
Other current liabilities	(21,285)	(23,285)	(42,244)
Non-current liabilities	(126,469)	(218,955)	(371,972)
Bank and loan borrowings - non-current	(126,469)	(217,442)	(371,220)
Other non-current liabilities	0	(1,513)	(752)
Net Assets	295,341	291,735	392,899
Derivative interest rate swaps & deferred tax liability	416	1,513	2,802
EPRA net assets	295,757	293,248	395,701
IFRS NAV per share (p)	107.7	106.4	105.4
Fully diluted EPRA NAV per share (p)	107.8	106.9	105.9
CASH FLOW			
Cash (used in)/generated from operations	(2,232)	31,434	40,251
Net finance expense	(424)	(6,626)	(9,167)
Tax paid	0	(1,715)	(236)
Net cash flow from operations	(2,656)	23,093	30,848
Net investment in investment properties	1,157	(99,286)	(8,267)
Acquisition of subsidiaries, net of cash acquired	26,659	(5,573)	(51,866)
Other investing activity	13	60	25
Net cash flow from investing activities	27,828	(104,799)	(60,108)
Equity dividends paid	0	(15,723)	(23,321)
Bank debt drawn/(repaid)	(1,217)	91,417	13,921
Other financing activity	0	(1,744)	67,101
Net cash flow from financing activity	(1,217)	73,950	57,701
Net Cash Flow	23,955	(7,756)	28,441
Opening cash	0	23,955	16,199
Closing cash	23,955	16,199	44,640
Balance sheet debt	(126,669)	(217,442)	(371,620)
Unamortised debt costs	(1,875)	(2,618)	(4,693)
Closing net debt	(104,589)	(203,861)	(331,673)
LTV	25.9%	40.6%	45.0%

Source: Regional REIT, Edison Investment Research

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