

GCP Student Living

FY20 results

Continuing growth punctuated by COVID-19

GCP Student Living's (DIGS's) FY20 financial performance was robust with increased rental income and fully adjusted earnings despite the impacts of the COVID-19 pandemic. Portfolio valuation gains drove NAV growth and including dividends paid the accounting total return was 7.6%. The pandemic will continue to negatively affect FY21, including reduced bookings for the 2020/21 academic year just commencing. However, beyond the current challenges we see no change in the positive fundamentals for DIGS's quality portfolio assets located primarily in and around London.

Year end	Gross profit (£m)	EPRA earnings* (£m)	EPRA EPS* (p)	EPRA NAV/share (p)	DPS (p)	P/NAV (x)	Yield (%)
06/19	35.0	18.9	4.7	165.5	6.15	0.74	5.0
06/20	38.1	14.9	3.4	171.8	6.15	0.71	5.0
06/21e	30.7	11.0	2.4	168.5	5.68	0.72	4.7
06/22e	48.0	25.5	5.6	168.4	5.68	0.72	4.7

Note: *Adjusted for revaluation movements, gains/losses on disposal, and other exceptional items. EPRA earnings includes £3.8m of abortive transaction costs in FY20.

Robust FY20 and continuing DPS

Prior to COVID-19 the portfolio had again been fully occupied for the 2019/20 academic year, which runs from mid-September, and had achieved rental growth of 4.4%, but students were selectively released from final rent payments as a result of the lockdown and closure of higher education institutions (HEIs). Reflecting a part of the impact, FY20 rental income (to 30 June 2020) of £47.8m (FY19: £44.4m) represented 92% of budgeted revenues for the financial year. EPRA earnings reduced to £14.9m but adding back £3.8m of aborted transactions costs and including licence fee accruals on continuing developments, adjusted earnings were £22.9m (FY19: £21.2m) and adjusted EPS 5.26p. Quarterly DPS continued and the aggregate for the year was unchanged at 6.15p, 86% covered.

Continuing challenges but fundamentals intact

At the time of reporting, reservations for the 2020/21 academic year were at 68%, up from 55% in July but below the five-year average 94% at this point; the investment manager anticipates a further increase. Our base case estimates assume 75% of potential 2020/21 rent is earned and a return to full occupancy for 2021/22. Weaker current bookings reflect the practical challenges for international students attending university in the UK, whereas strong application numbers from the Universities and Colleges Admissions Service (UCAS) confirm the attractions of the UK with its concentration of high-ranked HEIs, especially in London. Looking beyond the current uncertainty, we expect DIGS's high-quality portfolio of modern, purpose-built assets to continue to benefit from structural supply and demand imbalances for student residential accommodation in its chosen markets.

Valuation: Yield support and discount to NAV

We have assumed a continuation of the quarterly DPS at the Q420 rate of 1.42p. On this basis the shares yield 4.3%, with DPS cover dipping in FY21 and rebuilding in FY22. The more than 20% discount to NAV compares with an average 2% premium since IPO.

Real estate

5 October 2020

Price 122p
Market cap £555m

Net debt (£m) at 30 June 2020	221.4
Net LTV at 30 June 2020	21.9%
Shares in issue	455.0m
Free float	100%
Code	DIGS
Primary exchange	LSE
Secondary exchange	N/A

Share price performance



%	1m	3m	12m
Abs	(9.6)	(1.1)	(28.7)
Rel (local)	(8.9)	3.4	(15.3)
52-week high/low		213p	97p

Business description

GCP Student Living is a specialist UK real estate investment trust (REIT) investing in student residential assets, with a focus on London. The company seeks to provide shareholders with attractive total returns in the longer term through the potential for modest capital appreciation and regular, sustainable, long-term dividends.

Next events

AGM Nov 20 (est)

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Investment summary

Well positioned in strong markets

DIGS provides investors with exposure to a well-located, modern and high-quality portfolio of private student accommodation assets, with a focus on assets in and around London and other similar markets that the investment manager expects to benefit from strong supply and demand imbalances beyond the current pandemic. The UK, and London in particular, has some of the highest-ranking universities in the world and is well placed to continue to attract both domestic and international students. In the period since IPO this has resulted in full occupancy, above inflation rental growth and capital growth. DIGS's portfolio was again fully occupied with above-inflation rental growth (4.4%) for the 2019/20 academic year, until the onset of the COVID-19 pandemic in March 2020. Beyond the current pandemic challenges, the company's existing assets, low leverage and strong cash reserves position it well for a resumption of growth.

COVID-19 update

DIGS responded to the pandemic lockdown and closure of HEIs by allowing direct-let students (79% of budgeted income) to forgo rent related to the final 2019/20 academic year rent instalment (20% of the annual total) if rooms were vacated (or a reduced rate if retained for storage). This resulted in direct let rents collected being 84% of the previously budgeted total. For the 2020/21 academic year, the majority of HEIs to which DIGS is exposed have plans for on-campus learning and are looking to welcome as many students as possible with a hybrid approach to teaching. With most beds (c 80%) configured as self-contained studios and all within 10 minutes' walk of an HEI or major transport link, the portfolio is well-suited to the current situation. Student applications, especially international students, have continued to grow, but lockdown and travel restrictions have affected room bookings. At the time of reporting, 68% of rooms across the portfolio of student accommodation had been booked, compared with an average level of c 94% at the same date over the past five years. The investment manager expects the booking rate to increase, with a longer than normal booking cycle and positive impact in January as further postgraduate courses, with start states delayed by some higher education institutions, are scheduled to begin.

Financials

The shortfall in budgeted income for the 2019/20 academic year, which runs from mid-September, will also have a negative impact on Q121. Despite a positive first-time impact from the completion of Scape Brighton, the current level of bookings for the 2020/21 academic year will also weigh on the current FY21 financial year. Our forecasts assume that 75% of the 2020/21 direct let rent roll potential is earned as income, but we also provide a sensitivity analysis to alternative outcomes. Our base case also assumes a recovery of end-FY20 rent arrears in respect of nominations agreements and long-term leases without concessions or impairment. For the 2021/22 academic year we assume a 3% increase in rents with rent roll fully earned. This benefits FY22 strongly but will not be fully felt until FY23. We assume no overall change in like-for-like portfolio valuations, although the completion of Scape Brighton should have a positive impact. Nor do we assume any positive impact from acquisitions despite loan to value of c 22% at end-FY20 being well below the 30% medium-term target.

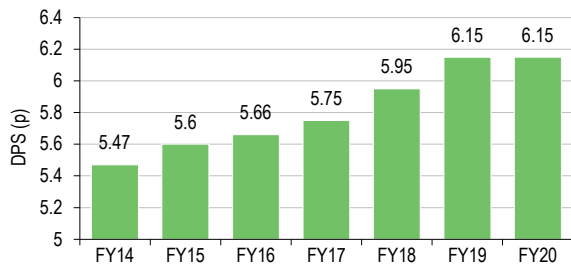
London-focused student accommodation

GCP Student Living (DIGS) is a UK real estate investment trust (REIT), externally managed by Gravis (see below), that invests in UK student residential property. The company is differentiated from listed peers by a focus on investment in properties that are located primarily in or around London. The investment manager believes that London and a small number of similar markets, will continue to benefit from structural supply and demand imbalances for student residential accommodation and will remain attractive to international students as a place of study.

The company has a premium listing on the official list of the FCA and its shares trade on the Premium segment of the London Stock Exchange (LSE) and are a constituent of the FTSE 250 Index. The company's investment objective is to provide shareholders with attractive total returns in the longer term through the potential for modest capital appreciation and regular sustainable dividends with RPI-inflation linked characteristics. Although a small minority of DIGS's rental income is contractually inflation linked, until the impact of COVID-19 like-for-like rental growth had increased in real inflation-adjusted terms for several years (with an average annualised uplift of 3.9% since IPO).

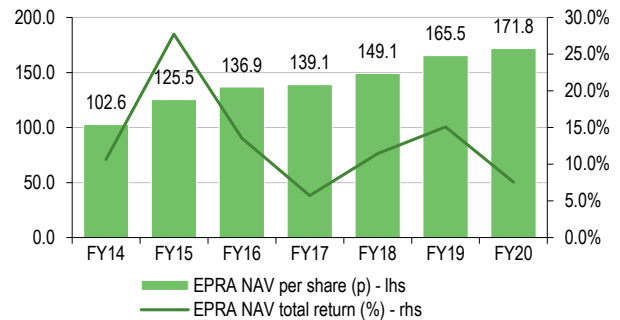
At the time of the IPO the company set a target annual shareholder total return (change in share price with dividends reinvested) of 8–10% and it had comfortably exceeded this in the period leading up to COVID-19. As a result of the pandemic, the total shareholder return in FY20 was a negative 20.6%, having been a positive 24.3% in the first half of the year, taking the annualised total shareholder return since IPO to 7.4%. This is still more than double the return on both the FTSE All-Share Index and the FTSE EPRA NARIET Index over the same period, even if slightly below the target set at IPO. NAV total return (the change in net assets plus dividends paid) continued to be positive in FY20 at 7.6% and the annual average compound return since IPO is 10.6% (or 12.9% assuming dividends are reinvested at the date declared as per company data).

Exhibit 1: DPS history



Source: GCP Student Living data

Exhibit 2: EPRA NAV and EPRA NAV total return*



Source: GCP Student Living data. Note: *Dividends added back but not reinvested.

DIGS has a fully independent board that is responsible for the effective stewardship of the company's affairs, including corporate strategy, corporate governance, risk assessment and overall investment policy. The chairman since IPO, Robert Peto has announced that he will retire from the board at the next AGM, to be held in late 2020. His replacement as chairman will be David Hunter who joined the board in May 2019. The other three independent non-executive directors and their dates of appointment are Malcolm Naish (2013 IPO), Marlene Wood (March 2015), and Gillian Day (February 2018). Collectively the board brings a depth of experience in finance and investment markets, real estate and corporate stewardship. Full biographies may be found at www.graviscapital.com/funds/gcp-student/company-info#the-team. The board of DIGS has appointed Gravis to provide day-to-day investment management services, and Scape Student Living as the primary property manager.

The investment and asset managers

Gravis is alternative investment manager, established in 2008, and privately owned by its directors and founding members. It manages c £3.2bn in assets including two other listed, closed-end vehicles: GCP Infra (market cap c £1bn), invested in long-term UK infrastructure projects; and GCP Asset Backed Income Fund (market cap c £400m), investing in asset-backed lending.

Nick Barker has day-to-day responsibility for the provision of investment advice to DIGS. Nick Barker is a chartered surveyor who joined Gravis in 2015 after eight years with Schroder Real Estate Management, where he was head of alternatives for the real estate business and a member of the fund management team.

Scape Student Living, a global developer, manager, and operator of purpose-built student accommodation (PBSA), provides property management services to DIGS in respect of all of the operational assets other than Water Lane Apartments in Bristol.

Revised fee arrangement

Revised investment and property management arrangements were recently announced, taking effect from the beginning of FY21. Since IPO, the investment management fee paid to Gravis has been set at 1.0% of net assets and from this entitlement, Scape has received c 0.25% of NAV pa. While Scape manages the facilities for which it is responsible, the actual asset management costs (such as on-site staff, utilities, etc) are paid directly by DIGS, a structure that is both operationally and tax-efficient, avoiding additional non-deductible VAT expenses that may otherwise arise.

Under the new arrangements DIGS will pay a reduced investment management fee to Gravis but will become directly responsible for payment of property management fees to Scape. The board believes that the revised management arrangements will provide DIGS with a competitive investment management fee basis and more closely align property management fees to relevant operational metrics in a manner that is more akin to the market standard seen in the UK sector.

The modified investment management fee introduces a sliding scale that allows shareholders to benefit more fully from the growth in net assets:

Exhibit 3: Revised investment management fees as % NAV		
NAV	Revised investment management fee	Previous combined investment manager and property management fee
Up to £950m	0.7500%	1.00%
Above £950m and up to £1.5bn	0.6375%	1.00%
Above £1.5bn	0.5625%	1.00%
Source: GCP Student Living		

The revised property management fee, to be paid directly by DIGS quarterly in arrears, comprises:

- 4% of the total PBSA income and 1.25% of the PBSA net operating income attributable to the assets managed by Scape.
- 2% of income in respect of the group's non-PBSA commercial space.

The property management fees related to PBSA are subject to a minimum level based on 80% of the relevant budgeted annual property management fees where group occupancy is materially adversely affected by a pandemic or epidemic, including COVID-19. Certain costs that are currently incurred by DIGS, amounting to c £0.8m in FY20, will be assumed by Scape.

DIGS says that by way of illustration, had the revised arrangements been in place during FY20 it would have benefited from approximately £0.6m of cost savings compared with those reported.

Modern, high-quality, London-focused portfolio

As at 30 June 2020 (end-FY20), the portfolio comprised the 10 modern, high-quality operational assets and one development asset (Scape Brighton), providing a total of 4,116 beds, fully occupied by students from 82 different HEIs at the start of the 2019/20 academic year. In aggregate, the number of assets was unchanged on FY19, although the student accommodation at Circus Street, Brighton, was completed on time and became operational under a 21-year lease with annual uplifts, to a subsidiary of Kaplan Inc, a global education provider. In the current financial year, Scape Brighton is expected to be fully operational during September and October 2020, having been affected by minor construction delays as a result of the pandemic.

The aggregate portfolio valuation at end-FY20 of just more than £1bn reflected an average net initial yield of 4.44% (FY19: 4.54%). During FY20 the portfolio experienced a 3.2% like-for-like valuation uplift (ie excluding ongoing development investment) driven primarily by modest yield contraction, with valuation gains focused on the London assets, Scape Mile End, Scape Wembley and Scape Bloomsbury.

The primary focus of the portfolio is on assets in and around London (80% by value) but more generally the investment manager seeks markets with good levels of demand and high supply-side barriers. At a more local level, the assets are located close to HEIs and/or major transport hubs. This convenient local position combined with the configuration of the accommodation (c 80% of rooms being self-contained studios) should be more than usually advantageous while COVID-19 remains a concern.

Exhibit 4: Summary of portfolio

Property	Location	Completion	Valuation (£m)	NIY*	Beds
Scape Mile End	East London	2012	164.4	4.42%	588
Scape Wembley	North London	2017	105.4	4.65%	578
Scape Brighton**	Brighton	2020	72.7	N/A	555
Scape Shoreditch	East London	2015	210.6	4.29%	541
Circus Street, Brighton***	Brighton	2020	77.8	3.56%	450
Scape Bloomsbury	Central London	2018	194.5	4.00%	432
Scape Greenwich	East London	2014	59.9	4.62%	280
The Pad	Egham	2012/2015	33.7	5.80%	220
Podium	Egham	2017	31.2	5.65%	178
Water Lane Apartments	Bristol	2015	22.3	5.15%	153
Scape Guildford	Guildford	2015	28.3	5.25%	141
Total			1,000.8	4.44%	4,116

Source: GCP Student Living. Note: *Net initial yield. **Scape Brighton is a forward funding agreement under construction at 30 June 2020 but completed in time for the 2020/21 academic year. ***The student accommodation element of Circus Street is in operation, but the office element was under construction at 30 June 2020.

Strong but selective portfolio growth since IPO has included properties acquired under an investment pipeline agreement in place with Scape Student Living, providing the company with the opportunity to acquire high-quality, purpose-built assets in good locations, while avoiding development risk and mitigating cash drag. Due to recent market uncertainty resulting from the COVID-19 pandemic, DIGS recently allowed its forward-purchase agreement in respect of Scape Canalside to lapse. The pipeline agreement with Scape has also now lapsed.

A conditional forward purchase agreement remains in place, providing the company with an opportunity to acquire a high-specification, purpose-built asset (Guildford II) in the same location as its existing Scape Guildford asset. The property has completed for the 2020/21 academic year, providing 403 beds. If acquired the property would form part of an enlarged Scape Guildford asset, providing a combined 544 beds in the same locality as the University of Surrey with potential to benefit from economies of scale. DIGS is not required to proceed with this acquisition and any decision is likely to take account of market conditions. However, with end FY20 gearing of c 22%

running well below the medium-term target of 30% and our assumption that market conditions are likely to revert to normal for the 21/22 academic year, we have included the acquisition of Guildford II in our forecasts. Using the valuation of Scape Guildford as a benchmark, we assume an acquisition in early FY22, for £81m (before costs of acquisition) at a net initial yield of 5.15%, generating c £4.3m of annual gross profit.

Positive student applications and the London difference

Increased number of students planning to start university

The number of students applying for university places continues to significantly exceed the number of places that are available by around one-third, and the pandemic has had no negative impact on the number of student applications for the 2020/21 academic year. Data from UCAS show that at the 30 June 2020 application deadline, total applications of more than 650k were up 2.3%. International (non-EU) student applications showed the strongest increase (9.6%) and UK applications also increased (1.6%), reflecting a further increase in the participation rate. EU applications were 2% lower but have previously benefited from government measures aimed at mitigating any impact from Brexit.

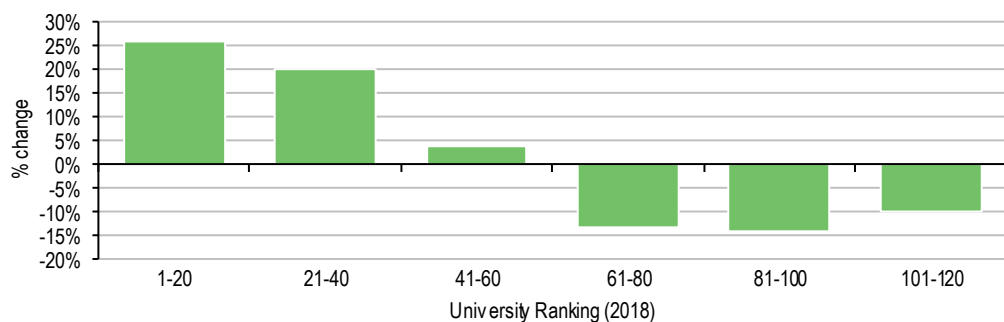
Amid the pandemic, what remains unclear is the number of student applicants who will actually take up their offers. Early September data from UCAS showed that undergraduates intending to start their chosen university courses were up 3.5% to more than 500k, with international students up 7.0% and UK students up 3.8%. EU students were showing a decline of 5.4%.

The continuing trends of more student applications and increasing numbers of international students are positive for DIGS, as too is the migration towards better performing universities.

Migration towards top-performing universities

Since the UK government raised tuition fees to a maximum of £9,000 pa in 2012 (and subsequently increased to £9,250), which was followed by a removal of the cap on undergraduate student numbers in 2015, there is clear evidence that many students are influenced in their choice of university by its cost and the expected future benefit. This has enabled the top universities to grow in size while maintaining their academic requirements. Given its concentration of top universities (home to six of the top 40), London has benefited.

Exhibit 5: Change in student applications by ranking of UK universities (2012–18)



Source: GCP Student Living, UCAS, Complete University Guide

The London difference

The demand for full-time higher education and the supply of purpose-built accommodation is not evenly distributed across the UK, and London, home to 23 universities, has one of the largest student populations of any city in the world. From a student demand-supply perspective, the differentiating features of the London market, where 83% of DIGS's assets are located, can be summarised as:

- London has five of the Russell Group universities in the UK and two of the top 10 universities in the world.
- As a result of the high standard of education available and the wider appeal of London as a place in which to live, a quarter of all international students studying in the UK are based there.
- London universities are only able to supply accommodation to c 30% of their first year and international students.
- New supply is constrained by planning restrictions and competing demands limit supply.
- It seems likely that the Mayor of London's 'London Plan' will negatively affect new private schemes by increasing complexity and diminishing the expected returns, adding further to supply constraints. This is likely to increase the scarcity value of DIGS's existing London assets.

Brighton shares similar market dynamics to London. It is home to the University of Sussex (a UK top 20 university) and the University of Brighton, with an aggregate c 32,000 students including c 8,000 international students. The city is also home to two of the largest English language foundation course providers in the UK.

Transactions activity supportive of yields

The investment attraction of PBSA in the core markets in which DIGS is invested has been reflected in yield compression since IPO. Overall UK student accommodation investment volumes of £5.2bn in 2019 were the highest since 2015 and Gravis estimates that a further £5.1bn has been traded or put under offer in the first half of 2020. Current year activity is dominated by the £4.7bn acquisition by Blackstone of the 28,000 bed (6,800 in London) IQ Student portfolio at a yield (estimated by Gravis) of 4.2%. Notably, the transaction completed in May, during the pandemic. Such investment activity, combined with the expectations of above-average rental growth over the long term, continues to support valuation yields

FY20 results

Until the COVID-19 pandemic came along, FY20 was shaping up to be another year of strong income growth, based on an increase in operational assets, fully occupied with above-inflation rent increases, and capital appreciation. At the half-year stage, rental income had been c 18% ahead year-on-year and adjusted earnings by more than 20%. Viewed against the unprecedented challenge of the pandemic, the full year outcome may justifiably be described as robust, although the pandemic effects will continue to be felt through the current year, as we discuss in the following section.

Exhibit 6: Summary of FY20 financials

£m unless stated otherwise	FY20	FY19	FY20/FY19
Rental income	47.8	44.4	7.5%
Property operating expenses	(9.7)	(9.4)	3.1%
Gross profit	38.1	35.0	8.7%
Gross margin	79.8%	78.9%	
Administrative expenses	(9.9)	(8.8)	12.0%
Aborted transaction costs	(3.8)		
Operating profit before gains on investment properties	24.5	26.2	-6.7%
Operating margin (exc. aborted project costs)	51.2%	59.1%	
Fair value gains on investment properties	33.9	73.9	-54.1%
Operating profit	58.4	100.1	-41.7%
Net finance expense	(9.8)	(7.3)	34.0%
PBT	48.6	92.8	-47.6%
Tax charge	0.0	0.0	
Profit for the year	48.6	92.8	-47.6%
Adjust for:			
Fair value gains on investment properties	(33.9)	(73.9)	
Fair value losses on financial assets	0.2		
EPRA earnings	14.9	18.9	-21.2%
License fees on forward funded developments	4.2	2.3	
Abortive transaction costs	3.8	0.0	
Adjusted earnings	22.9	21.2	8.0%
IFRS basic EPS (p)	11.17	22.92	
EPRA EPS (p)	3.42	4.67	
Group adjusted EPS (p)	5.26	5.23	0.5%
DPS (p)	6.15	6.15	0.0%
Dividend cover (adjusted earnings)	86%	85%	
IFRS & EPRA NAV per share (p)	171.78	165.52	3.8%
Net asset value	781.4	684.7	
Investment property value	1009.8	919.2	9.9%
Net debt	(221.4)	(236.6)	-6.5%
LTV	21.9%	25.7%	

Source: GCP Student Living data

- Rental income increased c 8% to £47.8m despite the negative impact of COVID-19, including a first-time contribution from Circus Street Brighton and a full-year contribution from Scape Bloomsbury. As a result of COVID-19, the IFRS income reported represented 92% of the company's budgeted income for the year and includes an accrual for outstanding rents relating to commercial rents and nominations agreements.
- After direct property operating expenses, the gross operating profit increased at a slightly faster c 9% with the gross margin increasing slightly to 80%. This reflects both underlying cost efficiency and the fact that Circus Street is let on a long-term lease with rents received on a net basis, generating no property costs. The increase in administrative costs was driven by investment manager fees, which in turn reflect higher average net assets. Additionally, the decision not to proceed with the acquisition of Scape Mile End Canalside as a result of COVID-19 uncertainty generated £3.8m of aborted transactions costs relating to a previously paid deposit, legal fees and lender due diligence fees. Although the abortive transaction costs had little impact on FY20 cash flow, they are included in EPRA earnings but are excluded from the company's underlying earnings.
- The increase in net finance expense is exaggerated by the non-recurrence of c £1.0m of FY19 finance income related to the particular accounting treatment of the Scape Brighton development. The increase in interest expense mainly reflects higher average borrowing as funds were drawn to finance the continuing developments in Brighton.
- Fair value gains on investment properties were £33.9m, with a like-for-like valuation gain on the year driven by yield tightening, particularly for the London assets. The end-FY20 portfolio net initial yield was 4.44% (FY19: 4.54%). Despite the impact of COVID-19, valuations were only slightly lower at end-FY20 compared with end-H120.

- Excluding the revaluation gains, EPRA earnings were lower as a result of the aborted transactions costs. Adjusting for these and including licence fees on forward funding developments (non-cash but rolled up and deducted from the acquisition cost), the company's adjusted earnings measure increased by c 8% to £22.9m or 5.26p per share (FY19: 5.23p).
- DIGS continued to declare quarterly DPS throughout the year and the Q420 DPS of 1.42p took the total declared for the year to 6.15p, unchanged on FY19, and 86% (FY19: 85%) covered by adjusted earnings.
- During the year the EPRA NAV per share increased to 171.8p (H120: 174.7p; FY19: 165.5p) and including dividends paid the EPRA NAV total return was 7.6%.

Liquid balance sheet and low gearing

To target selective asset growth, DIGS seeks a balance of equity and debt capital with a medium-term target for gearing of c 30% (end-FY20: 21.9%).

In late December 2019 DIGS raised gross proceeds of c £77m in a non-pre-emptive share placing, under existing shareholder authorities. The issue was launched in response to specific demand from APG Asset Management in its capacity as the discretionary manager of various pension funds, which had indicated its intention to subscribe for up to £75m of shares, subject to a minimum of £50m. The placing price of 186p was at a premium of 10.4% to the end-Q119 NAV per share and a discount of 6.3% to the share price immediately ahead of the launch. The placing was substantially oversubscribed requiring applications to be scaled back, with APG acquiring shares to a value of c £50m. The equity proceeds were raised in the context of the investment plans in place at the time, subsequently curtailed or at least deferred by the COVID-19 pandemic. This has left DIGS with a strong liquidity position and modest debt.

Available debt facilities at end-FY20 were £335m of which c £282m had been drawn. The facilities comprise £235m of long-term fixed-rate borrowing (at an average 2.96%) and £100m of shorter-term, more flexible floating rate debt. The latter comprises a £45m re-drawable debt facility of which c £15m was drawn at end-FY19 and a £55m development loan facility, £32m drawn. Once Scape Brighton is completed and stabilised, it will be possible to refinance the development loan, which is due in December 2021 with a conditional option to extend for a further 12 months. Undrawn debt facilities and cash resources (c £60m at end-FY19) provide ample near-term liquidity.

The average cost of the drawn debt at 30 June 2020 was 2.95% with a weighted average maturity of approximately five years. Allowing for c £60m of cash at end-FY20, the net debt was c £222m and the net loan to value ratio was 21.9%, well below the medium-term target of 30%.

Exhibit 7: Summary of debt portfolio

	PGIM		Wells Fargo RCF	
	Facility 1	Facility 2	RCF	Development loan
Principal	£170m	£65m	£45m	£55m
Drawn	£170m	£65m	£15m	£32m
Interest rate	Fixed 3.01%	Fixed 2.82%	1.85% + L	3.1% + L
Maturity	Sep-24	Apr-29	Jul-21	Dec-21
LTV/LTC covenant	60%	60%	60%	60%
ISCR/debt yield covenant	1.75x	1.75x	7.5%	7.5%

Source: GCP Student Living

DIGS's immediate investment plans include completion of Scape Brighton and a small amount of remaining investment on the office at Circus Street, Brighton. We estimate that these amount to c £25m. As discussed below, we have also assumed the acquisition of the 'Guildford II' forward purchase asset in H121, which we assume to be funded by the remaining undrawn debt facilities and additional debt of c £27m (as yet to be arranged) at assumed c 3% pa. This takes our forecast LTV to c 30%, in line with the medium-term target.

Uncertainties remain for near-term forecasting

Academic year versus accounting year

As noted above, FY20 rental income of £47.8m represented 92% of the budgeted total for the year. As the company's academic year runs for 51 weeks from mid-September, the student rental income reported for the year to 30 June 2020 (FY20) comprises c 25% of the 2018/19 academic year income and c 75% of the expected 2019/20 academic year income. The negative impact of the pandemic on 2019/20 academic year income has affected FY20 financial year income relative to budget and will also have a negative impact on Q121 compared with what would otherwise have been expected.

Exhibit 8: Rental income					
£m		FY20	FY19	FY20	FY19
Nomination rental income		6.2	6.0	13%	13%
Direct let rental income		35.5	35.0	74%	79%
Discounts		(0.3)	(0.3)	-1%	-1%
Total student income		41.4	40.7	87%	92%
Teaching space income		0.5	0.5	1%	1%
Commercial rental income		5.5	2.7	11%	6%
Gross rental income		47.4	43.9	99%	99%
Service charge income		0.4	0.5	1%	1%
Employee costs recharge		0.0	0.0	0%	0%
Rental income		47.8	44.4	100%	100%

Source: GCP Student Living

COVID-19 impact on 2019/20 academic year

Total budgeted income for the 2019/20 academic year was c £50.5m, comprising 79% from direct lets to students and 21% from nominations agreements and long-term leases (including a small amount of commercial space incorporated within the student accommodation assets). Rental payments for direct lets are made in three tranches for each academic year, with c 40% received in September, c 40% in January and the remaining c 20% in April, although in accounting terms the expected income is spread evenly across the year. For the 2019/20 academic year, 84% of budgeted direct let income was collected, with the shortfall emerging with the pandemic during the second half of the year. The company has also indicated that in cash terms, some of the budgeted rental payments in respect of the nominations agreements and long-term leases were in arrears, but that the income had been accrued as recovery was anticipated. In cash terms, 82% of all budgeted income (direct let, nominations agreements and long-term leases) was collected, representing a cash income shortfall of c £9m for the academic year. Due to the nominations/long-term lease accruals, the group accounting income shortfall is smaller and relates primarily to lower than budgeted direct let income. Some of the 2019/20 academic year income shortfall has been reported in FY20 but it will also have an impact on the first quarter of FY21.

2020/21 academic year bookings uncertainty

At the time of reporting, 68% of rooms across the portfolio of student accommodation, including Scape Brighton for the first time, had been booked. This compared with an average level of c 94% at the same date over the past five years. The pace of bookings contrasts with the growth in student applications and acceptances. The investment manager anticipates that students have delayed booking accommodation for the 2020/21 academic year due to COVID-19 uncertainty and expects bookings to increase from the current levels later in the enrolment cycle than is normally the case.

Nominations agreements and commercial arrears

DIGS has a long-term nominations agreement with a subsidiary of INTO University Partnerships, a provider of foundations courses, for 210 beds at Scape East. INTO accounted for c 5.9% of the 2019/20 academic year budgeted income (c £3m) and rents are in due in advance of three academic year terms. At the time of reporting, INTO was in arrears in respect of their latest rental instalment and DIGS is in discussions with INTO regarding the outstanding balance. Anticipating full collection, DIGS accrued the contractual income in FY20, with 83% having been received.

Rental income in respect of the lease at Circus Street, Brighton, continued to be received in line with expectations. The 450-bed student accommodation building is contracted on a 21-year lease to a subsidiary of Kaplan Inc, a global education provider.

A nominations agreement for 100 of the beds at Scape Greenwich has been treated in a similar manner to the direct lets and released from the final instalment of the 2019/20 academic year on a case by case basis.

Scape Shoreditch includes 49,000 sq ft of commercial space that is let on a long-term occupational lease to a subsidiary of WeWork and part-guaranteed by its US parent company. Rents are payable quarterly in advance and account for c 4.9% of the 2019/20 academic year annual budgeted income (c £2.5m). WeWork paid approximately half of the quarterly rent billed in advance in both March and June and discussions are underway regarding the outstanding payments. In anticipation of recovery, the outstanding rent was accrued in FY20, with c 90% having been received.

Scape Mile End includes 22,000 sq ft of teaching space let to Queen Mary University of London where rents continue to be received as expected.

2020/21 academic year scenarios

The key forecasting uncertainties for the current financial year (FY21) are with regard to the eventual outcome of direct let student accommodation bookings and whether payment patterns in respect of the nominations agreements and long-term leases return to normal without loss of future rental income or impairment of accrued receivables. Regarding the latter, given the covenant quality of the tenants and the encouraging fact that rents continued to be accrued in FY20, we will focus on the group income sensitivity to direct lets.

A two-week deposit is payable when direct bookings are made. This provides stickiness to bookings but is no guarantee that rents will be paid for the duration of the year. Final payment waivers in respect of 2019/20 were made at the discretion of the company, but had the pandemic struck earlier in the academic year rental receipts could have been lower. However, assuming no repeat of the conditions that applied in 2019/20, primarily the closure of HEIs, we use bookings as a guide to academic year rental income and Exhibit 9 shows a range of possible outcomes for FY21 group gross rental income and EPRA earnings. For simplicity we have assumed that nominations agreement and long-term lease (IFRS) income is unchanged on FY20 (ie no contractual rent uplifts, no negative impact from rent concessions/impairments, and no benefit from completion and letting of 29,000 sq ft of office space at Circus Street). Direct let rent roll (assuming full occupancy) is estimated to increase from the c £40m budgeted for (but not fully earned) in 2019/20 to c £46m for 2020/21 including Scape Brighton (we estimate a potential rent roll of £6.2m). We have not assumed a positive impact on direct let rent roll from rent uplifts and any discounting is effectively captured in the assumed percentage of rent roll earned.

Exhibit 9: Sensitivity of FY21 rental income and earnings to alternative 2020/21 academic year direct let rental income levels

£m unless stated otherwise	Assumed percentage of 2020/21 direct let rent roll earned						
	50%	60%	70%	75%	80%	90%	100%
Direct let	21.3	24.7	28.2	29.9	31.7	35.1	38.6
Other	12.3	12.3	12.3	12.3	12.3	12.3	12.3
Rental income	33.6	37.0	40.5	42.2	43.9	47.4	50.9
EPRA earnings	2.8	6.1	9.4	11.0	12.6	15.9	19.2
EPRA EPS (p)	0.62	1.34	2.06	2.42	2.77	3.49	4.21

Source: Edison Investment Research

We assume acquisition-led growth and normal markets for the 2021/22 academic year

For the 2021/22 academic year we have assumed a return to normal market conditions with rental income reflecting the full rent roll potential. Given the company's medium term 30% LTV target we also assume it proceeds with the acquisition of the 'Guildford II' forward-purchase asset. We estimate an increase in the direct-let student accommodation rent roll to £52.5m for the 2021/22 academic year including c £5.0m from Guildford II and 3% rent increases. For the group, we also assume a 2% increase in the nominations/long-term lease rent roll.

Edison forecast

Incorporating the above analysis, our central case forecast for FY21, perhaps better described as a scenario at this stage, is based on 75% of 2020/21 academic year direct rent roll being earned. Our assumptions of a return to normality for the 2021/22 academic year and the acquisition of Guildford II have a positive impact on the final three quarters of FY22 although Q122 will continue to reflect the 2020/21 academic year outcome. Our forecasts are shown in detail in Exhibit 13. We assume no net change in property valuation, which in reality is likely to include a positive impact from the completion and opening of Scape Brighton and the off-market acquisition of Guildford II (less acquisition costs) but may also be negatively affected by the continued near-term pressure on occupancy and income across the sector.

Dividends

The unchanged FY20 DPS was 86% covered by adjusted earnings and the company continues to target fully covered dividends over the longer term. No near-term dividend guidance has been provided and we have assumed a continuation of quarterly DPS at the same rate as Q420 with the 1.42p per quarter annualising at 5.68p. Our forecasts indicate a significant dip in DPS cover in FY21 (48%), based on adjusted earnings including licence fee income on the forward-funded developments, but substantially full cover in FY22 (with no difference between EPRA and Adjusted Earnings following completion of the existing developments in FY21). If DIGS opts to reduce DPS payments in FY21 and increase cover, this would enhance NAV per share such that there would be no impact on NAV total return.

Valuation and performance

At the time of the IPO the company set a target shareholder total return (change in share price with dividends reinvested) of 8–10% and had comfortably exceeded this in period leading up to COVID-19. As a result of the pandemic, the total shareholder return in FY20 was a negative 20.6%, having been a positive 24.3% in the first half of the year, taking the annualised total shareholder return since IPO to 7.4%. This is still more than double the return on both the FTSE All-Share Index and FTSE EPRA NARIET Index over the same period, even if slightly below the target set at IPO. NAV

total return (the change in net assets plus dividends paid) continued to be positive in FY20 at 7.6% and the annual average compound return since IPO is 10.6% (or 12.9% assuming dividends are reinvested at the date declared as per company data).

Exhibit 10: EPRA NAV total return since IPO (DPS added back but not reinvested)

	FY14*	FY15	FY16	FY17	FY18	FY19	FY20	FY14-20
Opening EPRA NAV per share (p)	97	102.64	125.51	136.93	139.08	149.12	165.52	97
Closing EPRA NAV per share (p)	102.64	125.51	136.93	139.08	149.12	165.52	171.78	165.52
Dividends paid during period (p)	4.70	5.60	5.63	5.72	5.90	6.10	6.29	33.65
EPRA NAV total return	10.7%	27.7%	13.6%	5.7%	11.5%	15.1%	7.6%	105.3%
Average annual return (compound)								10.6%

Source: GCP Student Living data, Edison Investment Research

Based on the 6.15p aggregate DPS paid for the year to 20 June 2020 (FY20) the trailing yield is 5.0%. Annualising the Q420 DPS of 1.42p (5.68p), the yield is 4.7%.

The current more than 20% discount to EPRA NAV per share compares with an average c 2% premium since IPO (and a peak of c 12%) and seems to reflect the current uncertainty more than the positive underlying fundamentals that we expect to remain in place as the pandemic comes under control.

Exhibit 11: P/NAV since IPO



Source: Refinitiv

In Exhibit 12 we show a summary valuation and share price performance comparison for the three UK-listed student accommodation companies: DIGS, Unite and Empiric Student Property. The DIGS P/NAV, based on the most recently reported EPRA NAV per share in each case, is a little below average, above Empiric and below Unite. A comparison of yields is currently challenging. While DIGS has continued to pay quarterly DPS amounting to 6.15p in the year to 30 June 2020, DPS payments have been disrupted at Unite and Empiric, both of which have slightly higher gearing than DIGS (Unite c 33% and Empiric c 35% at 30 June 2020), as a result of the pandemic. Having paid DPS of 1.25p per quarter in respect of the year to 31 December 2019 (including 1.25p declared 17 February 2020 in respect of Q419), Empiric has taken the decision to suspend dividend declarations pending an update in Q420. Unite cancelled payment of its final dividend in respect of the year to 31 December 2019 and while it says it anticipates reinstating dividend payments in 2020, including the potential to announce an interim dividend later this year, the timing of the reinstatement is still to be confirmed.

Exhibit 12: Student accommodation valuations and performance

	Price (p)	Market cap. (£m)	P/NAV* (x)	Yield** (%)	Share price performance			
					1 month	3 months	12 months	From 12m high
GCP Student Living	122	555	0.71	5.0	-9%	-3%	-29%	-43%
Unite Group	870	3462	1.04	1.2	-9%	-5%	-19%	-36%
Empiric Student Property	60	361	0.56	4.2	-15%	3%	-36%	-43%
Average			0.77	3.5	-11%	-2%	-28%	-40%
UK property index	1,440			3.1	-1%	-3%	-17%	-27%
FTSE All-Share Index	3,301			3.4	1%	-3%	-16%	-23%

Source: Refinitiv, Company data. Note: Prices at 2 October 2020. *Based on last reported NAV. **Based on trailing 12-month DPS declared. For GCP this includes four quarterly DPS amounting to 6.15p; for Empiric it includes the final two quarterly DPS in respect of FY19 amounting to 2.5p; for Unite it includes the FY19 interim DPS of 10.25p.

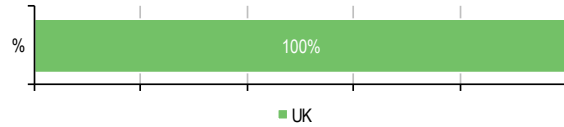
Exhibit 13: Financial summary

Year ending 30 June (£m)	2014	2015	2016	2017	2018	2019	2020	2021e	2022e
INCOME STATEMENT									
Rental income	9.1	11.5	22.5	28.8	35.8	44.4	47.8	42.2	60.5
Property operating expenses	(1.7)	(2.5)	(4.6)	(6.3)	(7.9)	(9.4)	(9.7)	(11.5)	(12.5)
Gross profit	7.5	9.0	17.9	22.5	27.8	35.0	38.1	30.7	48.0
Gross margin	0.8	0.8	0.8	0.8	0.8	0.8	79.8%	72.8%	79.4%
Administrative expenses	(2.4)	(2.0)	(5.7)	(6.1)	(7.4)	(8.8)	(9.9)	(10.1)	(11.0)
Abortive transaction costs	0.0	0.0	0.0	0.0	0.0	0.0	(3.8)	0.0	0.0
Operating profit before gains on investment properties	5.1	7.0	12.2	16.5	20.4	26.2	24.5	20.6	37.0
Operating margin	56.0%	60.6%	54.1%	57.1%	57.0%	59.1%	51.2%	48.9%	61.1%
Fair value gains on investment properties	5.0	25.7	27.2	11.9	47.6	73.9	33.9	0.0	0.0
Operating profit	10.1	32.6	39.3	28.3	68.0	100.1	58.4	20.6	37.0
Net finance expense - recurring	(2.4)	(1.3)	(3.4)	(4.8)	(6.9)	(7.3)	(9.8)	(9.6)	(11.5)
Non-recurring finance expense	0.0	0.0	(7.6)	0.0	0.0	0.0	0.0	0.0	0.0
PBT	7.7	31.3	28.3	23.5	61.1	92.8	48.6	11.0	25.5
Tax charge	0.0	(0.0)	0.0	(0.0)	0.0	0.0	0.0	0.0	0.0
Profit for the year	7.7	31.3	28.3	23.5	61.1	92.8	48.6	11.0	25.5
Adjust for:									
Fair value gains/(losses) on investment property	(5.0)	(25.7)	(27.2)	(11.9)	(47.6)	(73.9)	(33.9)	0.0	0.0
Fair value movement on financial derivative & close out fees	0.6	0.0	0.0	0.0	0.0	0.0	0.2	0.0	0.0
EPRA earnings	3.3	5.6	1.2	11.6	13.5	18.9	14.9	11.0	25.5
License fees on forward funded developments	0.0	0.0	0.0	1.4	1.5	2.3	4.2	1.5	0.0
Exceptional finance and other costs	0.0	0.0	7,635.9	0.4	0.4	0.0	0.0	0.0	0.0
Other	0.0	0.0	0.0	0.2	0.0	0.0	0.0	0.0	0.0
Adjusted earnings	3.3	5.6	7,637.1	13.6	15.4	21.2	22.9	12.5	25.5
Average number of shares (m)	73.4	109.9	183.0	290.5	384.3	404.8	434.8	455.0	455.0
IFRS EPS (p)	10.50	28.46	15.48	8.08	15.89	22.92	11.17	2.42	5.60
EPRA EPS (p)	4.49	5.11	.64	4.00	3.51	4.67	3.42	2.42	5.60
Adjusted EPS (p)	4.49	5.11	5.30	4.69	4.01	5.23	5.26	2.74	5.60
DPS declared (p)	5.47	5.60	5.66	5.75	5.95	6.15	6.15	5.68	5.68
Dividend cover (Adjusted earnings)	82%	91%	94%	82%	67%	85%	86%	48%	99%
BALANCE SHEET									
Investment property	151.6	177.2	424.8	634.6	784.4	919.2	1,009.8	1,034.8	1,118.1
Other non-current assets	1.0	0.3	0.8	0.3	3.0	0.3	0.0	0.0	0.0
Non-current assets	152.5	177.5	425.6	634.9	787.4	919.5	1,009.8	1,034.8	1,118.1
Cash & cash equivalents	3.6	106.3	66.3	55.1	29.2	15.5	60.4	21.3	18.5
Other current assets	1.4	18.7	6.9	7.5	9.0	17.2	18.0	18.0	18.0
Current assets	5.0	125.0	73.2	62.6	38.2	32.8	78.3	39.3	36.5
Interest bearing loans & borrowings	(39.5)	(39.6)	(128.2)	(217.5)	(232.8)	(249.1)	(279.5)	(280.3)	(361.1)
Other non-current liabilities	(1.0)	(0.5)	(0.8)	(0.3)	(0.3)	(0.3)	(11.5)	(11.5)	(11.5)
Non-current liabilities	(40.4)	(40.1)	(129.0)	(217.8)	(233.1)	(249.4)	(291.0)	(291.8)	(372.6)
Financial liabilities	0.0	(117.4)	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Other current liabilities	(4.2)	(7.3)	(11.3)	(12.8)	(18.3)	(18.2)	(15.8)	(15.8)	(15.8)
Total current liabilities	(4.2)	(124.7)	(11.3)	(12.8)	(18.3)	(18.2)	(15.8)	(15.8)	(15.8)
Net assets	112.9	137.7	358.5	467.0	574.2	684.7	781.4	766.6	766.2
EPRA adjustments	(0.0)	0.2	0.0	0.0	0.0	0.0	0.2	0.2	0.2
EPRA net assets	112.8	137.9	358.5	467.0	574.2	684.7	781.7	766.8	766.4
Period end number of shares (m)	109.9	109.9	261.8	335.8	385.1	413.7	455.0	455.0	455.0
IFRS NAV per share (p)	102.7	125.3	136.9	139.1	149.1	165.5	171.7	168.5	168.4
EPRA NAV per share (p)	102.6	125.5	136.9	139.1	149.1	165.5	171.8	168.5	168.4
CASH FLOW									
Net cash flow generated from other activities	5.9	6.4	4.2	14.2	21.4	25.6	17.0	20.6	37.0
Net cash used in investing activities	(87.0)	0.0	(210.6)	(195.5)	(101.4)	(66.2)	(41.4)	(25.0)	(83.3)
Net cash flow generated from financing activity	84.7	96.3	166.4	170.1	54.1	26.9	69.3	(34.7)	43.5
Change in cash	3.6	102.7	(40.0)	(11.2)	(25.9)	(13.7)	44.8	(39.1)	(2.8)
Opening cash	0.0	3.6	106.3	66.3	55.1	29.2	15.5	60.4	21.3
Closing cash	3.6	106.3	66.3	55.1	29.2	15.5	60.4	21.3	18.5
Debt as per balance sheet	(39.5)	(157.0)	(128.2)	(217.5)	(232.8)	(249.1)	(279.5)	(280.3)	(361.1)
Unamortised loan arrangement fees	(0.5)	(0.4)	(1.8)	(2.5)	(2.2)	(3.0)	(2.3)	(1.5)	(0.7)
Drawn debt	(40.0)	(157.4)	(130.0)	(220.0)	(235.0)	(252.2)	(281.7)	(281.7)	(361.7)
Net debt	(36.4)	(51.1)	(63.7)	(164.9)	(205.8)	(236.6)	(221.4)	(260.4)	(343.2)
Net LTV	24.0%	28.9%	15.0%	26.0%	26.2%	25.7%	21.9%	25.2%	30.7%

Source: GCP Student Living historical data, Edison Investment Research forecasts

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Revenue by geography

Leadership team
Non-executive chairman: Robert Peto

Mr Peto was non-executive chairman of Standard Life Investments Property Income Trust until 25 August 2020. He was non-executive chairman of DTZ Investment Management, the regulated arm of DTZ Investors, which he founded in 1992, until 2017. Mr Peto chairs a number of investment committees for property funds and is a non-executive director of Lend Lease Europe GP (Retail Fund), Western Heritable, Mactaggart Heritable and Bath & West Enterprises, the commercial subsidiary of the Royal Bath & West Society. He was global president of RICS in 2010/11, a member of the Bank of England Property Advisory Group from 2007 to 2011, chairman of DTZ UK from 1998 to 2008 and a member of the board of DTZ Holdings from 1998 to 2009.

Fund manager, Gravis: Nick Barker

Mr Barker has lead responsibility for provision of investment advice to the company. He qualified as a Member of RICS in 2007 while working at Cushman & Wakefield Investors. Mr Barker joined the investment manager in 2015 from Schroder Real Estate Investment Management, where he worked for eight years, being head of alternatives for the real estate business and a member of the fund management team for the Schroder UK Real Estate Fund. Mr Barker's early career also included working in property in Brazil for DTZ's local representative and subsequently Jones Lang LaSalle.

Head of investment companies, Gravis: Dion Miceli

Mr Di Miceli has responsibility for liaising with the client boards, investors and advisers and leading product development alongside the fund managers. A member of the Chartered Institute for Securities & Investment since 2005, Mr Di Miceli qualified as a chartered accountant with Arthur Andersen in 2002 and subsequently spent four years in the Investment Funds practice at Ernst & Young. He joined the investment companies team at Cenkos Securities in 2007 where, as a senior corporate adviser, he worked with investment company boards and their managers advising on and structuring a broad range of transactions covering IPOs, secondary issuance, mergers and corporate reconstructions. Mr Di Miceli joined the investment manager in 2016.

Fund management associate, Gravis: Joe McDonagh

Mr McDonagh is responsible for financial analysis, market research and providing support to the wider investment team. Mr McDonagh joined the investment manager from Grant Thornton, where he qualified as a chartered accountant and was part of the advisory team providing advice to clients predominately in the infrastructure and real estate sectors. He was responsible for consulting on new investments, creating bespoke financial models, performing due diligence and conducting option analysis on different funding structures for his clients. Mr McDonagh joined the investment manager in 2018.

Principal shareholders (source: FY20 Annual Report)

	(%)
APG Asset Management	8.69
BlackRock Inc	5.38
CCLA Investment Management	4.71

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