CUSTODIAN REIT
(LON:CREI)

9 October 2019

Real Estate Investment Trusts

52-WEEK HIGH	**121.80p**
52-WEEK LOW	**111.00p**
PRICE	**117.00p**
MARKET CAP MLN	£480.47
NET DEBT (MLN)	£135.00

Share Price

Major Shareholders

Mattioli Woods 6.0%	
Blackrock 3.4%	
Shares in issue	398,203,332
Primary Index	FTSE AS
Next Key Announcement	June 2019

Company Information

Address: 1 New Walk Place, Leicester LE1 6RU
Website: www.custodianreit.com

Analyst Details

Ed Stacey
ed.stacey@proactiveinvestors.com

Custodian REIT - sustained income to investors

Recent activity

Custodian REIT (LON:CREI) is a strong dividend paying UK REIT (real estate investment trust), managing a diverse portfolio of non-residential properties. The company continues to pursue a low-churn buy-and-hold rental income focused strategy. We summarise some recent developments.

In October 2019, Custodian announced the acquisition of a portfolio of eight distribution warehouses under a sale and leaseback deal with Menzies Distribution Limited. Key points:

- **Net initial yield (NIY) of 6.4%, broadly in line with Custodian's existing portfolio. NIY is an industry standard measure of rental yield.**
- **Natural fit with Custodian's existing industrial portfolio (industrial = 40% of the overall portfolio by value).**
- **Weighted average unexpired lease time (WAULT) of 8.8 years, above the average for the existing portfolio. WAULT is an industry standard measure of lease longevity.**
- **The acquisition is a "corporate" acquisition, meaning Custodian is acquiring a subsidiary of Menzies that holds the assets. This type of deal tends to be efficient in terms of acquisition costs.**

In September 2019 Custodian agreed with Lloyds Bank to increase the total funds available under the company's revolving credit facility from £35 million to £50 million for a term of three years, with an option to extend the term by a further two years subject to Lloyds Bank's agreement, and a reduction in the rate of annual interest to between 1.5% and 1.8% (from 2.45%) above three-month LIBOR - the London inter-bank offer rate. This agreement provides visibility on further funding for Custodian, as well as the reduced interest cost.

On p2 we present a reminder of some of the portfolio metrics that support Custodian's ability to maintain its progressive dividend policy, and we argue that recent developments align well with this objective.

Consistent strategy - prioritise dividends

The Menzies acquisition has been the only property acquisition that Custodian has undertaken in the current calendar year. The company stated in its 31 July update that there is strong buyer demand for properties with low-risk tenants and long leases, and this demand is leading to unattractive prices and therefore low available rental yields. Custodian requires high and secure rental yields to continue to sustain and grow its dividend. We believe that investors should welcome the company's conservatism in refraining from acquisitions this year – income to shareholders is the top priority, not portfolio expansion.

We also note that the acquisition takes balance sheet gearing up to 23.1%, which is still within the company's target level of 25%. On p2 we present an update of one of our favoured measures of risk-reward in the REIT space – dividend yield compared with balance sheet gearing. We argue that Custodian offers investors a premium level of dividend compared to its risk profile.

Year end Mar 31	2018	2019	Current	2021
Value of investment properties	528.9	572.7	595.7	615.7
Revenue from property (£M)	34.8	40.0	41.6	43.8
EPRA EPS (GBp)	6.9	7.3	7.3	7.6
DPS (GBp)	6.5	6.6	6.7	6.8
Dividend yield	5.5%	5.6%	5.7%	5.7%

Richard Shepherd-Cross, fund manager. Shepherd-Cross is a chartered surveyor. He joined Mattioli Woods in 2009, and established Custodian Capital as a property fund management subsidiary to the group. In 2014 he led the business through its flotation as Custodian REIT PLC.

Alex Nix, assistant fund manager. Nix joined Custodian Capital in 2012, having spent eight years with Lambert Smith Hampton. He holds a degree in real estate management, and qualified as a chartered surveyor in 2006.

Risk/reward analysis

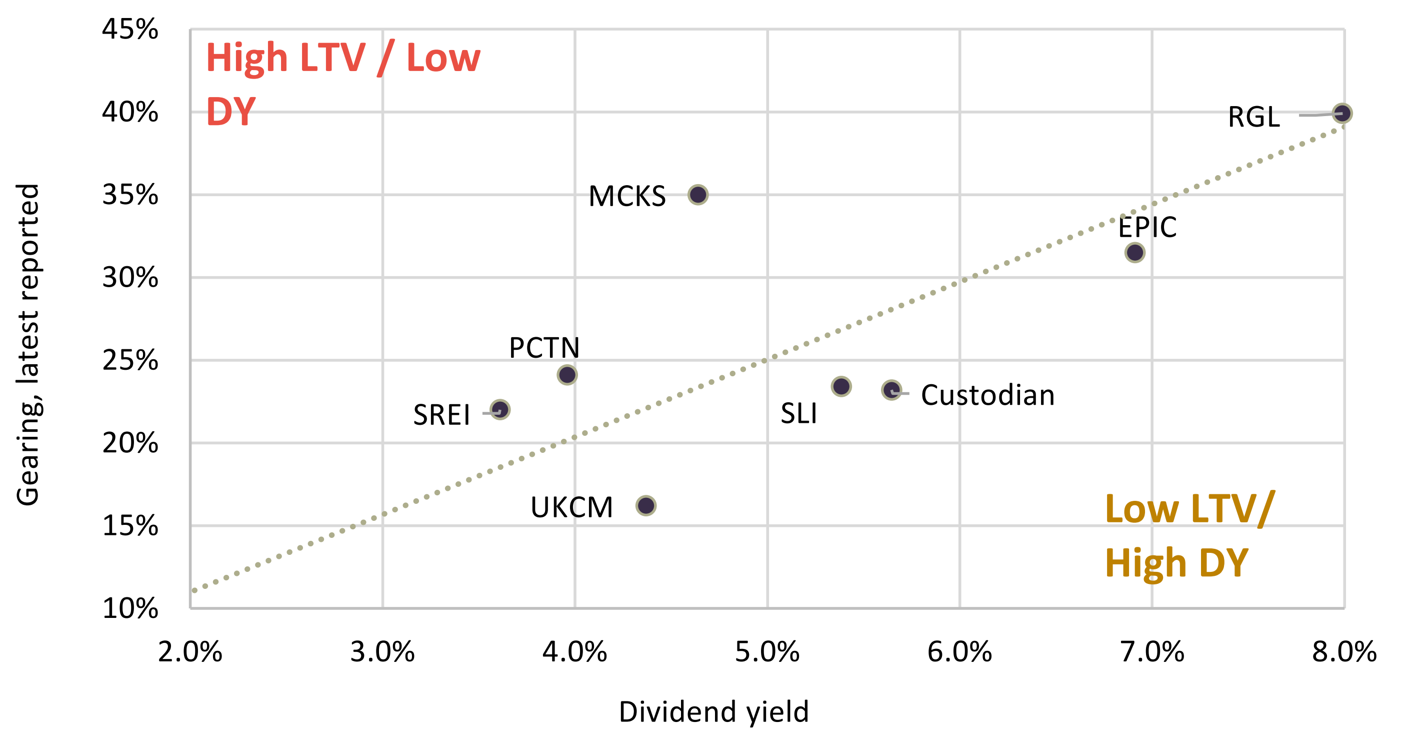
We regard Custodian REIT as one of the safest dividend plays in the UK REIT space. Some of the metrics that support this view are summarised:

- Total shareholder return (dividends plus share price appreciation) of 21.1% over the last three years, compared with 14.4% for the REIT sector (as measured by the FTSE EPRA Nareit UK index).
- Gearing of 23.1% represents a low level of financial risk.
- Weighted average unexpired lease term of 5.6 years and EPRA defined (European Public Real Estate Association) occupancy rate of 95.9%. Both compare favourably with comparable REITs.
- A dividend yield of 5.6%, with a dividend that is fully covered by EPRA-defined earnings per share.

One of our preferred measures of relative risk/reward in the REIT space is a comparison of dividend yield (reward) with balance sheet gearing (risk). The following chart shows Custodian's dividend yield compared with balance sheet gearing, as measured by the loan-to-value (LTV) ratio.

The peers we have used are UK focused, diversified non-residential REITs – Schroders Real Estate Investment Trust (LON:SREI), Picton Property Income (LON:PCTN), UK Commercial Property REIT (LON:UKCM), McKay Securities (LON:MCKS), Standard Life Investments Property Income Trust (LON:SLI), Ediston Property Investment Company (LON:EPIC), and Regional REIT (LON:RGL).

Dividend yield versus LTV ratio



Source: Proactive Research

The chart shows that on this measure, Custodian is among the best (bottom right direction) in class. We note that we could also have included some of the very large UK listed property names – British Land, Shaftesbury, Great Portland Estates, etc. We leave it to the reader to verify that Custodian screens even better if we expand the peer group to include the very large caps.

General Disclaimer and copyright

LEGAL NOTICE – IMPORTANT – PLEASE READ

Proactive Research is a trading name of Proactive Investors Limited which is regulated and authorised by the Financial Conduct Authority (FCA) under firm registration number 559082. This document is published by Proactive Research and its contents have not been approved as a financial promotion by Proactive Investors Limited or any other FCA authorised person. This communication is made on the basis of the 'journalist exemption' provide for in Article 20 of The Financial Services and Markets Act 2000 (Financial Promotion) Order 2005 and having regard to the FCA Rules, and in particular PERG 8.12.

This communication has been commissioned and paid for by the company and prepared and issued by Proactive Research for publication. All information used in the preparation of this communication has been compiled from publicly available sources that we believe to be reliable, however, we cannot, and do not, guarantee the accuracy or completeness of this communication.

The information and opinions expressed in this communication were produced by Proactive Research as at the date of writing and are subject to change without notice. This communication is intended for information purposes only and does not constitute an offer, recommendation, solicitation, inducement or an invitation by, or on behalf of, Proactive Research to make any investments whatsoever. Opinions of and commentary by the authors reflect their current views, but not necessarily of other affiliates of Proactive Research or any other third party. Services and/or products mentioned in this communication may not be suitable for all recipients and may not be available in all countries.

This communication has been prepared without taking account of the objectives, financial situation or needs of any particular investor. Before entering into any transaction, investors should consider the suitability of the transaction to their individual circumstance and objectives. Any investment or other decision should only be made by an investor after a thorough reading of the relevant product term sheet, subscription agreement, information memorandum, prospectus or other offering document relating to the issue of securities or other financial instruments.

Nothing in this communication constitutes investment, legal accounting or tax advice, or a representation that any investment or strategy is suitable or appropriate for individual circumstances or otherwise constitutes a personal recommendation for any specific investor. Proactive Research recommends that investors independently assess with an appropriately qualified professional adviser, the specific financial risks as well as legal, regulatory, credit, tax and accounting consequences.

Past performance is not a reliable indicator of future results. Performance forecasts are not a reliable indicator of future performance. The investor may not get back the amount invested or may be required to pay more.

Although the information and date in this communication are obtained from sources believed to be reliable, no representation is made that such information is accurate or complete. Proactive Research, its affiliates and subsidiaries do not accept liability for loss arising from the use of this communication. This communication is not directed to any person in any jurisdiction where, by reason of that person's nationality, residence or otherwise, such communications are prohibited.

This communication may contain information obtained from third parties, including ratings from rating agencies such as Standard & Poor's, Moody's, Fitch and other similar rating agencies. Reproduction and distribution of third-party content in any form is prohibited except with the prior written consent of the related third-party. Credit ratings are statements of opinion and are not statements of fact or recommendations to purchase, hold or sell securities. Such credit ratings do not address the market value of securities or the suitability of securities for investment purposes, and should not be relied upon as investment advice.

Persons dealing with Proactive Research or members of the Proactive Investors Limited group outside the UK are not covered by the rules and regulations made for the protection of investors in the UK.

Notwithstanding the foregoing, where this communication constitutes a financial promotion issued in the UK that is not exempt under the Financial Services and Markets Act 2000 or the Orders made thereunder or the rules of the FCA, it is issued or approved for distribution in the UK by Proactive Investors Limited.

London
+44 207 989 0813
The Business Centre
6 Wool House
74 Back Church Lane
London E1 1AF

New York
+1 347 449 0879
767 Third Avenue
Floor 17
New York
NY 10017

Vancouver
+1 604-688-8158
Suite 965
1055 West Georgia Street
Vancouver, B.C. Canada
V6E 3P3

Sydney
+61 (0) 2 9280 0700
Suite 102
55 Mountain Street
Ultimo, NSW 2007