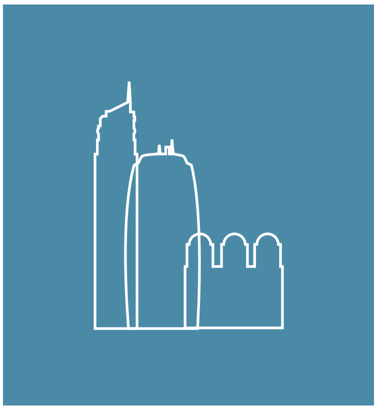

TPN Lockdown Edition Commercial Rental Monitor

In This Edition:

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Commercial tenant payment performance dips sharply through lockdown... Having already been under pressure prior to the COVID-19 crisis

- The COVID-19 Crisis "Lockdown Period's" impact on commercial property tenant payment performance to date has been severe, and was possibly exacerbated by the fact that the tenant population had already been experiencing pressure from a multi-year economic stagnation in the run up to the crisis. The percentage of commercial tenants in good standing declined further in the 1st quarter of 2020, which was largely prior to the late-March start of the national business "lockdown".

- Preliminary tenant payment performance data for the 2nd quarter 2020 months to date then showed a sharp drop in the percentage of tenants in good standing during April and May in all 3 major sectors, i.e. Retail, Office and Industrial Property, with Retail Property being by far the worst affected.

- "Full recovery" in tenant payment performance can be a lengthy process following a sharp recession, and 2020 is indeed expected to yield a very deep recession. If the aftermath of the 2008/9 Global Financial Crisis-related recession is a benchmark, the peak in the recovery percentage of tenants in good standing could lag an economic growth recovery by 1 to 2 years.

The build-up to COVID-19 Crisis... a multi-year economic stagnation already exerting pressure on the tenant population

In the 1st Quarter of 2020, the quarter largely preceding the COVID-19 Crisis-related "lockdown" of a large part of the economy, Commercial Property tenant payment performance continued to weaken gradually.

The percentage of tenants in good standing with their rental payments to landlords was 77.85%, slightly lower than the 78.32% recorded in the previous quarter, and more noticeably down from the 83.11% multi-year high recorded back in the final quarter of 2016.

The percentage as at the 1st quarter remained perhaps surprisingly good, given that the economy had already been in mild recession during the latter half of 2019, and had been broadly stagnating for some years.

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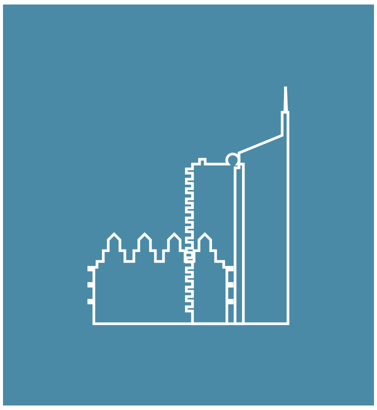
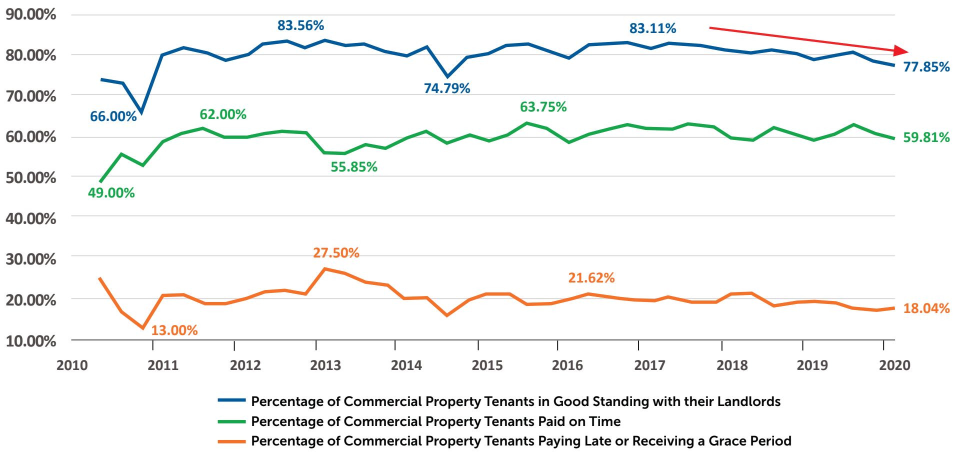


Nevertheless, from 2016 the gradually weakening tenant payment performance had begun to reflect the deteriorating economic fundamentals, and would likely have continued to weaken through 2020 even had there not been a COVID-19 Crisis at all. South Africa's well-documented myriad of structural economic problems had been gradually dragging the economy weaker since as far back as 2012.

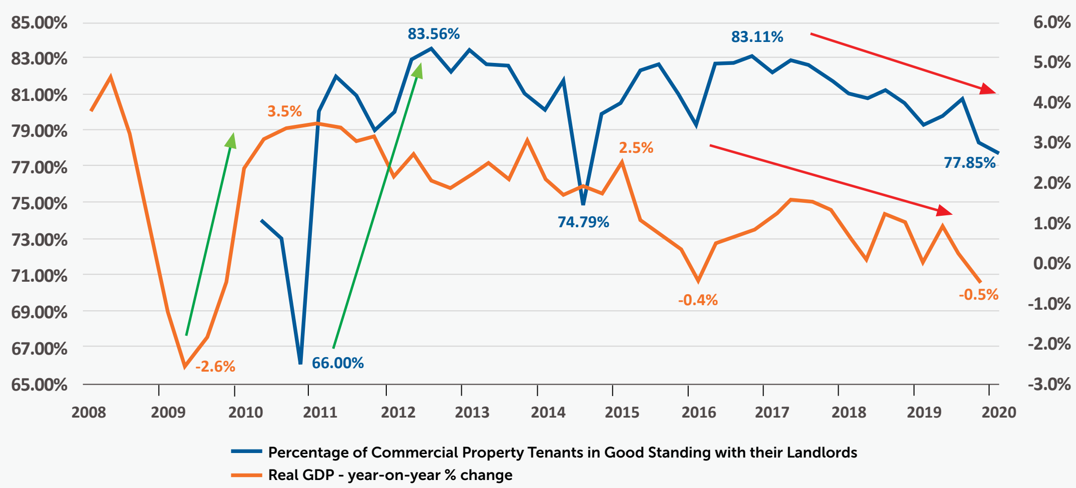
PERCENTAGE OF COMMERCIAL TENANTS IN GOOD STANDING WITH LANDLORDS

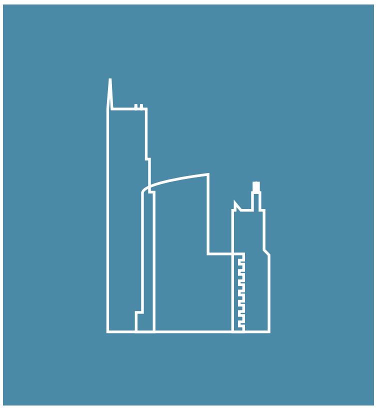


The economic recovery following the 2008/9 Global Financial Crisis (GFC) Recession saw Real GDP (Gross Domestic Product) recover to peak at 3.5% in the 1st quarter of 2011. In lagged response to the economic recovery, the percentage of tenants recovered to a post-recession high of 83.56% as at the 3rd quarter of 2012.

Thereafter, after a 2nd dip towards 2013/14, the tenants in good standing percentage managed to creep back up into the 80s to record a 2nd post-GFC high of 83.11% late in 2016. This "clawback" was perhaps in lagged response to GDP growth retaining some semblance of respectability to still record above 2% (2.5%) year-on-year as recently as early-2015.

PERCENTAGE OF COMMERCIAL TENANTS IN GOOD STANDING WITH LANDLORDS vs GDP GROWTH

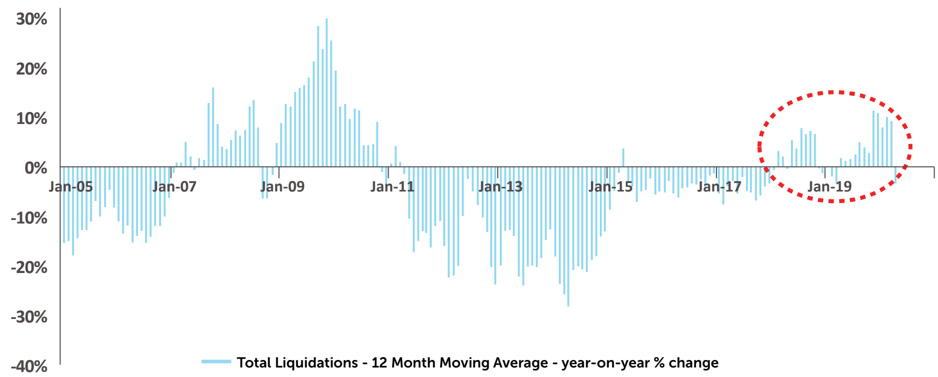




But from 2015, economic growth began to slide more noticeably to levels near 1% and below, moving in and out of contraction territory more frequently. This more severe economic growth weakness since 2015 appears to largely explain the gradual slide in tenant payment performance from 2017 onward.

And through 2018 and 2019, StatsSA liquidations data began to show a general rise in the number of liquidations, after a prior lengthy period of general decline from 2011 to 2017, also confirming the weak economy's mounting impact on businesses.

TOTAL LIQUIDATIONS GROWTH

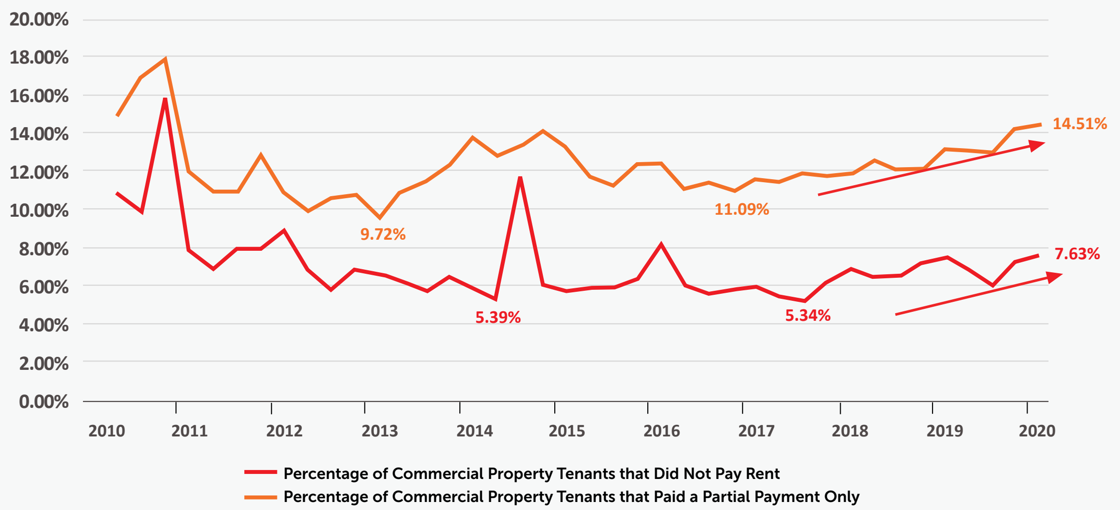


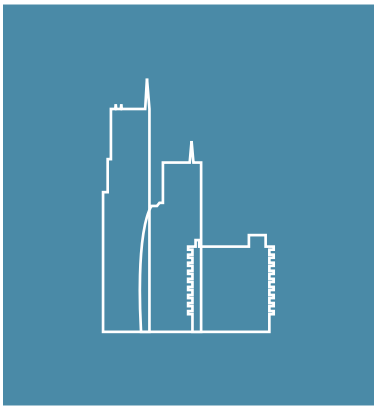
Source: StatsSA

Not surprisingly, therefore, from 11.09% as at the end of 2016, the percentage of tenants that paid a only partial rental payment rose to 14.51% as at the 1st quarter of 2020, while the percentage that did not pay at all rose from a 5.34% low as at the 3rd quarter of 2017 to 7.63% by the 1st quarter of 2020.

Therefore, the tenant payment performance statistics showed 2017 to be the year in which tenant financial pressure began to mount to the extent that it pushed rental payment performance noticeably weaker.

PERCENTAGE OF COMMERCIAL TENANTS THAT DID NOT PAY RENT OR ONLY PAID IN PART





Enter the COVID-19 Lockdown

Then, late in the 1st quarter, the economic environment changed radically with the announcement of COVID-19-related lockdowns of major parts of the economy. This would negatively affect the revenues of a large part of the economy's business population, and thus its commercial property tenant population, which in turn would hamper their ability to make rental payments in many cases.

In order to monitor this unique lockdown impact on tenant performance, TPN has done a special month-by-month data extract of commercial property tenant payment performance.

These are preliminary estimates and may be adjusted in the near future. However, it is believed that they provide a good indication of the severe pressure exerted by the lockdowns.

From 73.59% in March, April's percentage of tenants in good standing slumped sharply to 50.89%, and May's to 44.96%, April and May being the 2 months of the most severe lockdown levels with June so far closely tracking the May rental collection percentage.

55.76% REMAINS A VERY WEAK PERCENTAGE

"Full Recovery", back to pre-COVID-19 levels and beyond, is likely to take a significant time, possibly only happening beyond 2021, as the lagged impacts of the lockdown period linger in the economy for some time to come.

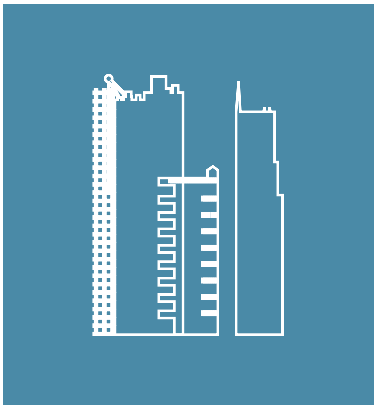
Retail Property has been the hardest hit during Lockdown

During the lockdown period, TPN has also started some new high frequency tenant performance data extracts aimed at examining the relative performances of the tenant population in the 3 major Commercial Property Sub-Sectors, i.e. the Retail, Office and Industrial Property Sectors.

From this data, the Retail Property Sector's tenants appear to have been impacted the hardest, with this sub-sector's percentage of tenants in good standing with landlords having fallen sharply from 73% in March to a lowly 34% by May 2020.

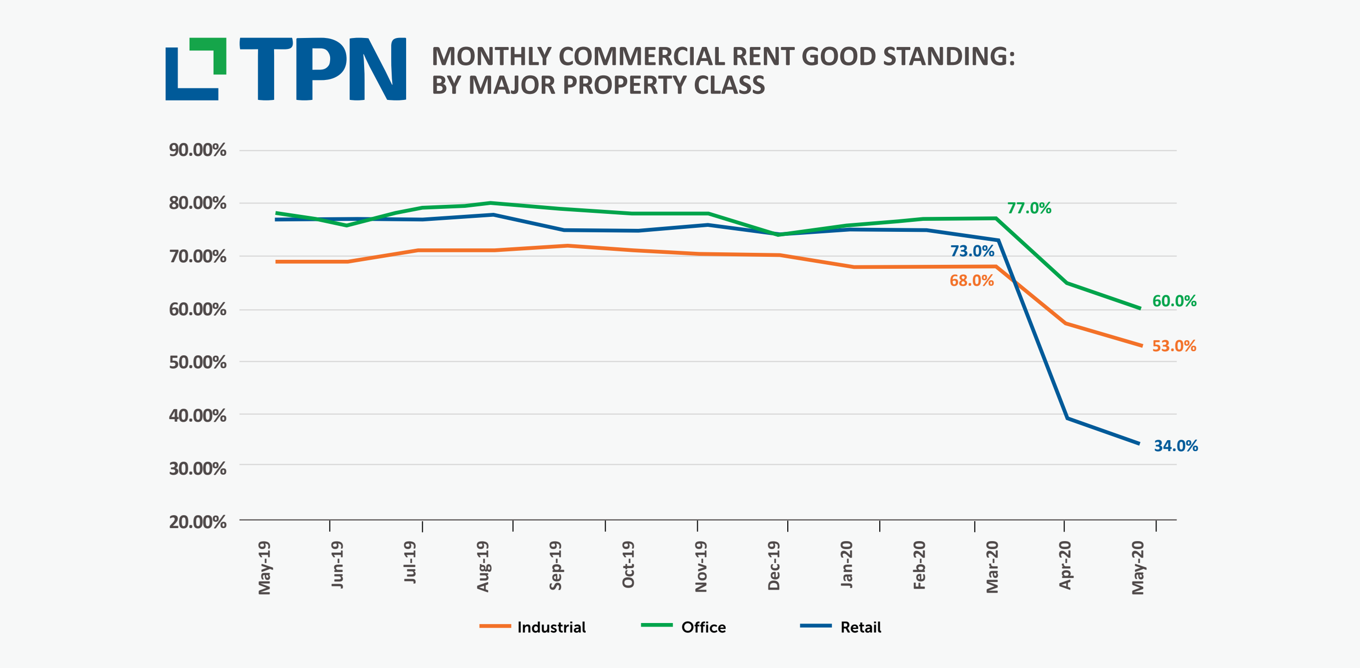
By comparison, the Industrial Property Sector's percentage of tenants in good standing has fallen less sharply, from 68% in March to 53% by May 2020.

To date, the least affected sector is Office Space, its tenants in good standing percentage falling from 77% to 60% from March to May.



All 3 sectors' declines, however, are severe, despite the latter 2 sectors almost being made to look good by the severity of the Retail Tenant performance weakening.

These relative performances are interesting. The Industrial Property Sector is strongly tied to trends in Manufacturing as well as in economy-wide inventory levels (the latter tied to general economy-wide demand), both of which are likely to have dropped sharply due to compulsory lockdowns.



During recessions, Manufacturing production typically contracts far more severely than Real retail Sales. This begs the question as to why Retail tenants have seen their payment performance drop far more sharply than tenants in Industrial Property where both have suffered heavily at the hands of lockdowns? We would believe that this reflects on retail property tenants, on average, being more financially fragile than, for instance, Manufacturing tenants. In addition, rentals on industrial properties are on average far more affordable, not having inflated as sharply as retail property rentals over the past few decades. Retail Property has the most significant affordability challenge for its tenant population, and this may in part be showing up more significantly in that sector's tenant payment performance.

However, it is essential that we don't judge sector performances too early. The post-lockdown period is likely to be one of severe economic weakness for quite some time, and during this period more tenant financial strain and closures are a strong possibility. Many companies occupying office space continued to work remotely through the lockdown period, possibly keeping office-bound companies in a better position for the time being. But this is not to say that they won't feel the financial pain later on, potentially impacted by the economic weakness that could linger for a while.

In short, the severe drop in tenant performance in April, May and June is seen as a direct impact of lockdown on tenant revenues and their ability to pay rent. Ongoing post-lockdown economic weakness can cause further significant tenant financial pressure, and it is less clear which sector would be affected the most during the post-lockdown phase.

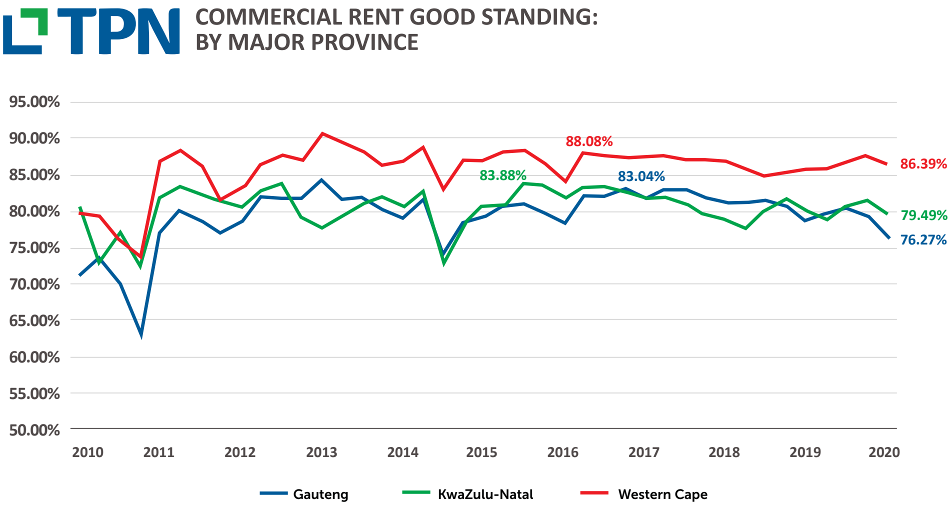
Major Provinces' Tenant Performance

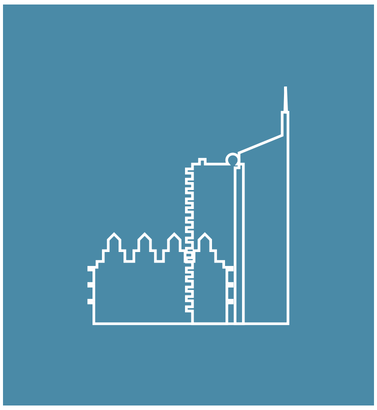
The Western Cape remains the province with the highest percentage of commercial tenants in good standing, to the tune of 86.39%, slightly down on the prior quarter and marginally lower than the 88.08% decade high reached in 2016.

This continues to underscore that province's status as the country's prime property province. Since the Commercial tenant data history started in 2010, the Western Cape has had the highest percentage of tenants in good standing of the Big 3 Provinces for most of the time.

Gauteng, with 76.27% of tenants in good standing, as at the 1st quarter of 2020, has seen the most significant decline in recent times. This is an almost 7 percentage point decline from the 83.04% high recorded in 2016.

In the lagged response to the 2008/9 recession, Gauteng saw its tenants in good standing percentage record the weakest performance in 2010 of the 3 major provinces. Judging by recent quarters' data, it appears that the province is on track to being the weakest major region during the current downturn too.



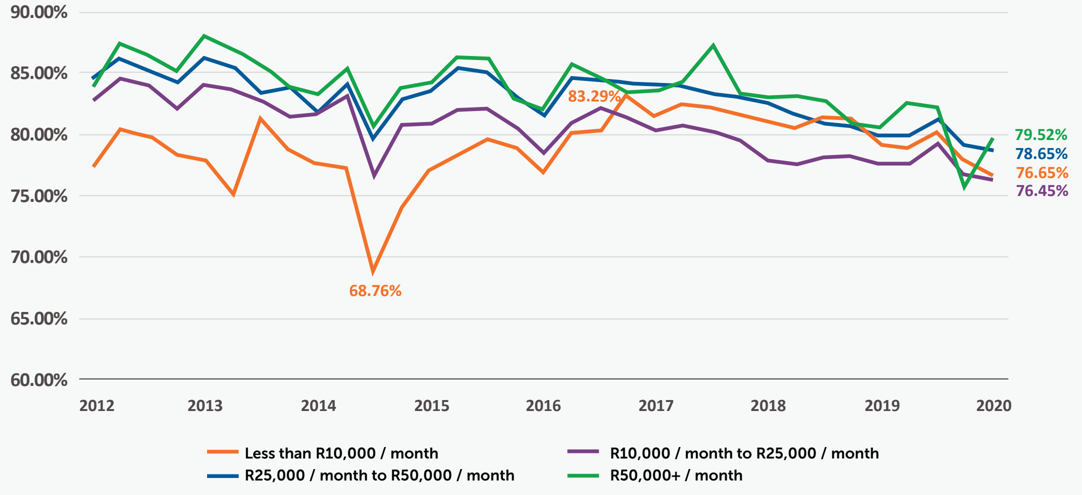


Rental Value Payment Performance

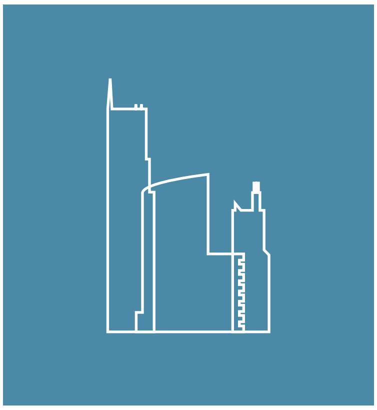
It is believed that smaller tenants in the lower rental/month value bands are most vulnerable on average to the deep recession, and similar to the 2008/9 Global Financial Crisis Recession will be the weakest performers in terms of rental payment performance.

In the run-up to the COVID-19 Crisis, things appeared to be slowly heading in this direction. All 4 rental value segments have seen weakening in their tenants in good standing percentage. However, the lowest value band, i.e. Below R10,000/month rental payment, has seen a slightly more pronounced decline of late. At a stage of 2018, at 81% this segment's tenants in good standing percentage had been by a small margin the highest (albeit short lived) of the 4 segments. But a decline to 76.65% by the 1st quarter of 2020 has meant that it is now near to being the weakest performing segment, with the 2nd lowest value band, i.e. R10,000-R20,000/month, being still only marginally lower at 76.45%. The 2 lowest rental segments have the lowest percentages of tenants in good standing, the higher 2 segments, i.e. R25,000-R50,000/month and R50,000+/month recording 78.65% and 79.52% levels respectively.

TPN COMMERCIAL RENT GOOD STANDING: BY RENTAL VALUE BAND



Our expectation for the weakest performance to be in the lowest rental value band is based on the recorded history. Back in the earlier years of these data series', around 2012 to 2015, in the aftermath of the Global Financial Crisis, this segment's percentage of tenants in good standing was noticeably lower than the higher 3 segments. It narrowed the gap by 2016, but the expectation of deep recession in 2020 is expected to once again widen the gap between the performance of this segment and the higher 3 value bands.



The Post-lockdown Phase

As Government gradually allows the economy to reopen, we would expect an immediately noticeable improvement in tenant payment performance compared with the April/May/June dip, reflected in an increase in the percentage of tenants in good standing with their landlords. However, the projected economic recession for 2020 as a whole is a deep one according to most economists' forecasts, and we would expect the weak economic conditions to linger for a while post-lockdown, as the lagged impacts of the local and global lockdowns filter through to our economy in their entirety.

We would expect it to take significantly longer to return to pre-COVID-19 levels near to 80% or beyond. In addition, the future percentage of tenants in good standing may not reflect the full impact of COVID-19 on the economy, because a portion of the tenant population can be expected to go entirely out of business and cease to exist. This would likely be reflected in rising property sector vacancy rates.

The Retail Property Sector may continue to have the weakest tenant performance of the 3 major property sectors in the near term, given that the restaurants and food component of this sector is still battling in partial lockdown.

As appeared to be the case in the aftermath of the 2008/9 Global Financial Crisis, we would expect the lowest of the rental value bands to be financially the most fragile, and to suffer the weakest tenant payment performance.

Finally, regarding the major provinces, the Western Cape's tenant population appeared to approach the COVID-19 Crisis in the best financial health of the 3 regions (Gauteng and KZN being the 2 others), Gauteng looking to be the weakest performer of the 3. However, the Western Cape has become the epicentre of the COVID-19 pandemic. The risk is thus that the Western Cape is forced at some future stage to be locked down at a higher level than the other provinces, which could hamper its superior tenant performance. For the time being, however, it looks to be in the best position through what appears to be a currently deep recession.