FitchRatings

RATING ACTION COMMENTARY

Fitch Assigns LondonMetric First-Time 'BBB+' IDR; Senior Unsecured Debt 'A-'; Outlook Stable

Thu 20 Mar, 2025 - 13:37 ET

Fitch Ratings - London - 20 Mar 2025: Fitch Ratings has assigned LondonMetric Property plc a first-time Long-Term Issuer Default Rating (IDR) of 'BBB+' with Stable Outlook and senior unsecured rating of 'A-'.

The ratings reflect an all-UK core "distribution" logistics property portfolio of GBP2.8 billion at end-September 2024, weighted towards urban logistics, with proven rent reversion, high occupancy, and long leases. These types of assets are core to a retailer's or distributor's logistics network, as shown by this portfolio's high 90% tenant retention rate.

The group's "long income" portfolio of GBP3.2 billion shares similar traits of contractual rent increases, high occupancy and longer leases. These specialist assets include Merlin Entertainment's theme parks, Ramsay's private hospitals, and Travelodge's budget hotels.

LondonMetric continues to be conservatively financed, aided by recent equity-funded M&A activity. Fitch projects a pro-forma net debt/EBITDA at around 7x and interest cover at a comfortable 3x.

KEY RATING DRIVERS

Rental Income-Focussed: The combination of the group's long weighted average lease length to earliest break (WALB, 17.7 years), high occupancy (99%), and contractual CPI/RPI or fixed rent uplifts (78% of the portfolio), some with minimum annual cash rent increases, results in rent visibility and stability. This is underpinned by the fundamentals of LondonMetric's core UK 'distribution' portfolio, which includes mega and regional distribution and urban logistics. Their embedded rent reversionary potential reflects quality asset selection, location, the size of these assets, and their underlying demand.

Mission-Critical Assets: LondonMetric has targeted key units that are "mission-critical" to retailers' and logistics' established distribution networks. In assessing these properties, the group calculates their rent potential relative to operators' larger transport, labour and other operating costs. Such properties offer an enduring service, including supporting the UK's growth in ecommerce. This approach is also consistent with LondonMetric's smaller portfolios of drive-thru and convenience service assets (quick restaurants and local Co-op type stores).

Long-Dated WALB and Purpose: The long WALB provides the landlord with long-term income and the tenant with the security of an extended tenure. Indications of a tenant's intention to stay long-term include their investment in operational automation and the building's ESG credentials, and the unit's strategic importance within its national and regional distribution network. In the distribution and convenience portfolios, LondonMetric actively seeks to re-gear and extend a lease as its WALB shortens towards five to seven years, thereby maintaining the portfolios' WALB at 11 and 12.3 years, respectively.

Specialist Long-Term Income Portfolio: The very long leases for the former LXi portfolio's Merlin Entertainments sites (53 years to expiry), Ramsay private hospitals (12.6 years) and Travelodge budget hotels (25 years) share the same investment strategy of long-stay and specialist properties with dedicated operators. The portfolios' properties also benefit from established locations, some with sites of critical mass.

Capturing Cash Rent Increases: Within the core distribution portfolio, LondonMetric has posted significant five-yearly rent increases above previous passing rent from lease lettings and re-gearing (FY24: 37%, FY23: 26%, year-end March). Rent reviews have also resulted in material increases (FY24: 21%, FY23: 16%, on a five-yearly equivalent basis). On a group basis, LondonMetric receives annual cash rent uplifts on 42% of the portfolio, while 50% of the portfolio has rent increases at five-year intervals.

Post-M&A Portfolio: The acquisitions of LXi's GBP2.9 billion of investment properties in March 2024 and CT Property Trust's (CTPT) GBP0.3 billion in May 2023 - both through all-shares transactions - have expanded LondonMetric's portfolio. They complement the long-income portfolio and industrial assets. As part of its strategy to refine the portfolio, LondonMetric has sold GBP231 million of these acquired non-core properties. Management targets a portfolio mix of at least 50% 'distribution' assets by value (end-September 2024: 45%).

Tenant Concentrations: Management's disciplined approach seeks to reduce high tenant concentrations, where its top 10 tenants currently contribute 37% of total income. This includes Ramsay Health Care at 11%, followed by Merlin Entertainments at

9% and Travelodge at 6%. The remaining tenants are each below 2% and include typical retailers such as Primark, Tesco and Sainsbury/Argos with their distribution centres and some superstores; logistics companies like Great Bear Distribution and Amazon; and industrial units.

Specialist Assets' Rental Evidence: The contractual rent uplifts for some of the specialist buildings, such as private hospitals and entertainment sites, partly mitigate the lack of readily available open market rent review evidence for some of these assets. These rents therefore rely on a tenant's covenant, rent affordability, assessments of the asset's alternative use, and the enduring viability of the asset's purpose. Due to their higher net income yield, Fitch has applied a lower debt capacity to these asset types when setting rating sensitivities, relative to the profiles of commercial property peers.

Pro-forma Profile: Fitch forecasts LondonMetric's net debt/EBITDA at around 7x for FY25, and comfortable interest coverage above 3x, after including the full-year effects of LXi and CTPT. Fitch uses cash rents, reflecting actual payments received, rather than using IFRS rental income, which straight-lines future years' fixed rent uplifts and tenant incentives over the lease term. Fitch uses 1HFY25 annualised net contractual rent of GBP345.6 million (net of Merlin's income strip). Consistent with the group's historical profile, Fitch-calculated loan-to-value (LTV) forecast is 34% at FYE25.

Senior Unsecured Debt Uplift: Historically, LondonMetric has used unsecured debt. The enlarged group inherited LXi asset-specific secured debt, some of which has been prepaid with new unsecured funding at the LondonMetric level, and others are planned for repayment. Nevertheless, the Fitch-calculated unencumbered investment properties/unsecured debt ratio is expected to remain above 2.0x (even after excluding the specialist properties) and warrants the senior unsecured rating uplift to 'A-'.

PEER ANALYSIS

LondonMetric's closest peer is SEGRO PLC (IDR: BBB+/Stable, GBP15.1 billion portfolio end-2024). SEGRO has greater exposure to property development, which entails planning permission, construction, completion, valuation and pre-let risks. In contrast, LondonMetric has minimal exposure to forward-funded units, so it benefits less from a premium yield-on-cost or a valuation uplift resulting from well-managed development risk.

SEGRO's net initial yields (UK only: 4.1%, group: 4.4% end-2024) and LondonMetric (distribution: 4.7%, group: 5.3% end-September 2024) reflect the latter's more regional portfolio without the self-managed critical-mass campuses that SEGRO has. LondonMetric's end-September 2024 stable occupancy of 98% for its "distribution" assets compares with SEGRO's variable 94% at end-2024. LondonMetric 90% five-year tenant retention rate is higher than SEGRO's 80% equivalent.

Both companies quote significant rent reversion but Fitch calculates that SEGRO has captured higher rent increases (2024: 43%, 2023: 40%, and 2022: 28%) than LondonMetric (1HFY25: 18%, FY24: 21%, FY23: 16%, excluding re-gearing). Figures for both companies are five-year equivalents.

Fitch believes this is because:

-- SEGRO's five-year reviews are at open market rent values whereas LondonMetric has a greater proportion (60% of the portfolio) of annual fixed or CPI/RPI uplifts, some capped;

-- SEGRO's UK WALB is 8.5 years versus 11 years for LondonMetric's "distribution" portfolio. Thus SEGRO has shorter leases and more frequent breaks or re-leasing to capture estimated rental values; and

-- SEGRO's portfolio also includes its core London-weighted campuses where rents will be higher.

When, if, the UK logistics market no longer has significant ERVs, LondonMetric will be protected by its fixed and minimal, some CPI/RPI, contractual rent uplifts, whereas SEGRO will be negotiating more (albeit upward-only) rent reviews and lease expiries.

LondonMetric has a very low European Public Real Estate Association (EPRA) cost ratio (property and admin expenses including vacant property costs/gross rents, 1HFY25: 7.6%) compared to European peers of about 10%-12%. The acquisition of LXi REIT Plc in 2024 has not adversely affected this ratio. The group's lower cost ratio is attributed to a lean head-office and the portfolio's assets' triple-net-lease structure. Conversely, SEGRO's EPRA cost ratio was a high 24% reflecting unrecovered property outgoings, some of which are due to property development activities.

Although SEGRO and LondonMetric have the same IDR, Fitch's rating sensitivities differentiate their financial profiles. SEGRO's net debt/EBITDA negative rating sensitivity to a 'BBB' IDR is above 9.5x, whereas LondonMetric's is above 8.5x (blending the lower debt capacity of the specialist portfolios). LondonMetric's financial profile, LTV, and equity-raising, have been steadier than SEGRO's over the recent years.

KEY ASSUMPTIONS

Key Assumptions Within Our Rating Case for the Issuer

- Fitch's forecasts use annualised cash rents so that all assets acquired or leased part-way during the year make a full-year contribution to rents relative to year-end debt

- Fitch uses actual contractual rental uplifts for the Merlin assets, as well as Travelodge and Ramsay portfolios. For the rest of the portfolio, RPI/CPI rental uplifts are calculated using Fitch's UK inflation forecasts under its December 2024 Global Economic Outlook. Open market reviews are assumed to achieve at least rent increases that match inflation. Fixed uplifts are forecast at around 2% per year

- Acquisition spend of about GBP300 million in FY25 with yield income at 6% (in line with completed 1HFY25 acquisitions) followed by GBP160 million in FY26 and around GBP100 million per year thereafter

- Disposals of GBP353 million and GBP24 million in FY25 and FY26, respectively, mostly comprising non-core assets from the acquired LXi portfolio

- Development spend (mostly forward-funded) of about GBP450 million during FY25-FY28

- Average cost of debt at 4.5%-5%, reflecting the embedded high cost (some floating rate) on the inherited LXi REIT secured debt. Fitch's UK interest rate assumptions under its December 2024 Global Economic Outlook are used for variable debt costs

- Dividends at 90% of Fitch's cash rents-based funds from operations. This does not include the benefit of LondonMetric's five-year history of scrip dividends averaging 7.4% of total dividends

- No additional equity

RATING SENSITIVITIES

Factors that Could, Individually or Collectively, Lead to Negative Rating Action/Downgrade

-- Net debt/EBITDA, based on the current portfolio mix, above 8.5x

-- Net interest cover below 2.5x

-- Affecting the senior unsecured rating: secured debt/total debt above 20% (Fitch FYE25 forecast: 38%)

Factors that Could, Individually or Collectively, Lead to Positive Rating Action/Upgrade

-- Completion of planned, management-preferred, portfolio mix after the LXi merger

-- Reduction in significant tenant concentrations

-- Net debt/EBITDA, adjusted for the portfolio mix, below 7.5x

-- Net interest cover above 3.0x

LIQUIDITY AND DEBT STRUCTURE

LondonMetric's end-1HFY25 liquidity included cash of GBP85 million and GBP748 million availability under its revolving credit facilities, reducing to about GBP540 million with April 2026 expiries. These cover GBP350 million of debt maturing in September/October 2025. At end-1HFY25, the group's average loan tenor was about 4.8 years with a weighted average cost of debt of about 4%. Despite end-1HFY25 cost of debt being burdened by LXi's legacy high fixed coupon secured debt, group EBITDA net interest cover is forecast at above 3.5x for FY25.

LondonMetric's debt is fully hedged until September 2026, when some of the interest hedges expire. Fitch assumes an increase in cost of debt as these existing hedges, with weighted average caps/swaps of 2.42%, expire and are replaced by market-rate instruments. Even then, Fitch forecasts net interest cover to remain above 3.0x.

Much of the unsecured debt is held at the parent level. Secured creditors (at former LXi entities, A&J Mucklow or CT Property Trust) only have recourse to the property company owning the pledged asset, and not to the wider group. Although Fitch expects the secured debt/total debt ratio to be 38% at FYE25, this will decrease as the group reduces secured funding, as liability management opportunities arise.

DATE OF RELEVANT COMMITTEE

25 February 2025

REFERENCES FOR SUBSTANTIALLY MATERIAL SOURCE CITED AS KEY DRIVER OF RATING

The principal sources of information used in the analysis are described in the Applicable Criteria.

MACROECONOMIC ASSUMPTIONS AND SECTOR FORECASTS

Click here to access Fitch's latest quarterly Global Corporates Macro and Sector Forecasts data file which aggregates key data points used in our credit analysis. Fitch's macroeconomic forecasts, commodity price assumptions, default rate forecasts, sector key performance indicators and sector-level forecasts are among the data items included.

ESG CONSIDERATIONS

The highest level of ESG credit relevance is a score of '3', unless otherwise disclosed in this section. A score of '3' means ESG issues are credit-neutral or have only a minimal credit impact on the entity, either due to their nature or the way in which they are being managed by the entity. Fitch's ESG Relevance Scores are not inputs in the rating process; they are an observation on the relevance and materiality of ESG factors in the rating decision. For more information on Fitch's ESG Relevance Scores, visit https://www.fitchratings.com/topics/esg/products#esg-relevance-scores.

RATING ACTIONS

ENTITY / DEBT	RATING		
LondonMetric Property Plc	LT IDR	BBB+	New Rating
senior unsecured	LT	A-	New Rating

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VIEW ADDITIONAL RATING DETAILS

Additional information is available on www.fitchratings.com

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APPLICABLE CRITERIA

Corporate Recovery Ratings and Instrument Ratings Criteria (pub. 02 Aug 2024) (including rating assumption sensitivity)

Corporate Rating Criteria (pub. 06 Dec 2024) (including rating assumption sensitivity)

Sector Navigators – Addendum to the Corporate Rating Criteria (pub. 06 Dec 2024)

APPLICABLE MODELS

Numbers in parentheses accompanying applicable model(s) contain hyperlinks to criteria providing description of model(s).

Corporate Monitoring & Forecasting Model (COMFORT Model), v8.1.0 (1)

ADDITIONAL DISCLOSURES

Solicitation Status

Endorsement Policy

ENDORSEMENT STATUS

LondonMetric Property Plc	UK Issued, EU Endorsed

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