EDISON

Custodian REIT

Good momentum through Q123

Q123 update and outlook

Real estate

Custodian REIT's (CREI's) Q123 report showed continuing strong performance, with like-for-like rental and capital value growth supporting a three-month total return of 3.2%. Capital growth has been strong in the past year, but it is CREI's income-driven approach that has driven its consistent record of attractive returns. It is optimistic that this will continue, while any weakness in capital values may present opportunities for further income and dividend accretive growth.

Year end	Net rental income (£m)	EPRA earnings* (£m)	EPRA EPS* (p)	NAV/** share (p)	DPS (p)	P/NAV** (x)	Yield (%)
03/21	33.1	23.7	5.6	97.6	5.00	1.09	4.7
03/22	35.6	25.3	5.9	119.7	5.25	0.89	5.0
03/23e	38.8	26.4	6.0	124.7	5.63	0.85	5.3
03/24e	40.0	27.0	6.1	124.9	6.00	0.85	5.7

Note: *Excludes revaluation gains/losses and other exceptional items. **Defined as EPRA net tangible assets (EPRA NTA) per share.

Forecast income growth maintained but costs higher

A strong performance continued through Q123, despite growing market headwinds. NAV grew 2.1% to 122.2p, driven by a 1.7% like-for-like increase in portfolio valuations. ERV increased by 1.4% like-for-like and net capital deployment added 1.5% to annualised rent roll (to £41.1m). The Q123 DPS of 1.375p is in line with Q422 as well as the FY23 target of at least 5.5p. It was fully covered despite EPRA earnings of 1.4p (Q422: 1.6p) being negatively affected by the timing of capital deployment and a reduction in occupancy (88.7% vs 89.9% at end-FY22), with the positive impact of letting offset by the timing of refurbishment and sales. CREI remains positive about the strength of the regional occupier market and its ability to grow income further, while debt is now 74% fixed for an average of around eight years. We nevertheless expect higher interest and administrative costs than previously and have reduced forecast EPRA earnings and DPS by c 7%.

Consistently positive returns built off income growth

CREI's prime strategy for delivering returns is its focus on generating attractive and stable dividend returns, from an actively managed, well-diversified portfolio of UK regional commercial real estate. It is differentiated by a focus on smaller lot-size properties, which typically provide a yield premium over larger assets. This is partly the result of a broader range of potential occupiers, while attracting less competition from larger institutional investors. Combined with moderate gearing and a relatively low-cost base, this yield premium has contributed to consistent and attractive total returns since the 2014 initial public offering (IPO), delivered by dividends paid.

Valuation: Consistent, income-focused returns

The minimum 5.5p per share DPS targeted by CREI for FY23 represents an attractive yield of 5.2%, while our forecast for FY23 DPS growth exceeds CREI's minimum target. The c 13% discount to the unaudited end-Q123 NAV per share compares with an average c 3% premium since IPO.

30 August 2022

Price	**106p**
Market cap	**£467m**

Estimated net debt (£m) at 30 June 2022	150.5
Net LTV as at 30 June 2022	21.5%
Shares in issue	440.9m
Free float	91%
Code	CREI
Primary exchange	LSE
Secondary exchange	N/A

Share price performance

%	1m	3m	12m
Abs	(2.6)	7.3	7.9
Rel (local)	(2.7)	9.7	8.8
52-week high/low		110p	93p

Business description

Custodian REIT is a London Main Market-listed REIT focused on smaller lot-size (<£10m) commercial properties across the UK regions outside London. It is income focused, with a commitment to pay a high but sustainable and covered dividend, with the potential for capital growth.

Next events

AGM	31 August 2022

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Custodian REIT is a research client of Edison Investment Research Limited

Investment summary

In addition to recent financial performance, this report covers CREI's long-term performance and strategy. The strength of the FY22 result may be seen as exceptional, benefiting as it did from a bounce-back in property valuations as pandemic restrictions were progressively eased. However, recurring earnings and dividends also showed good growth, with rent collection back to pre-pandemic levels. A strong performance continued through Q123. Despite growing headwinds from rising inflation, only partly explained by the war in Ukraine, CREI remains positive about the strength of the regional occupier market and its ability to grow income further. It recognises the risk of property valuations being negatively affected on a broad scale by weakening volumes and sentiment in the investment market, thus far restricted to a minority of sub-sectors such as 'big-box' logistics. However, given the company's focus on income driven returns, any falls in the valuation of those assets that CREI targets for acquisition would support reinvestment at higher yields, supporting earnings and enhancing dividend capacity.

The underpinning for CREI's optimism is covered throughout this report, but in summary includes:

- CREI provides diversified exposure to UK commercial real estate, enabling it to spread risks, adapt its portfolio to changing market and economic conditions and seek investment opportunities across a wide pool of assets.
- A focus on properties with smaller individual values differentiates it from most of its peers. Properties of this size typically provide a yield premium over larger assets, in part the result of a broader range of potential occupiers, while attracting less competition from larger institutional investors.
- The company has successfully managed the complexities of a smaller lot-size portfolio through asset and tenant selection, active asset management and well-controlled costs, generating a well-established track record of income-focused returns.
- A significant 69% weighting to industrial logistics and retail warehouse assets, where the investment manager identifies continuing positive fundamentals for rental growth, has been highly beneficial to recent performance.
- Recent acquisitions are yet to fully contribute to earnings and there is significant upside potential from void reduction.
- Gearing is low and 74% of all debt is long term and fixed rate, providing protection against increasing interest rates.
- Commercial real estate has traditionally provided a medium-term hedge against inflation as, at least in part, this is reflected in rental growth and valuations over time. Increasing building costs have a tendency to restrict new construction.

AGM proposals

CREI will hold its annual general meeting (AGM) on 31 August 2022. Within the 'ordinary' business of the AGM we think it worth highlighting three proposals:

- Since 2016 the upper target-lot-size has been £10m at the point of investment, but to reflect significant inflation since then, shareholders will be asked to approve an increase to £15m. This level will continue to be below the general level of institutional demand and CREI does not expect a material difference in the yield premium versus larger assets or in the implementation of its investment strategy.

- Historically, CREI has restricted its investment to completed assets, occasional forward funded development[1] and refurbishment. Shareholders will be asked to approve a broadening of the definition of refurbishment to include the redevelopment of properties already owned to a limit of 10% of gross assets. To be clear, CREI will not acquire land assets or properties with the intention of development or redevelopment. The purpose is to provide additional flexibility to enhance asset quality, including environmental performance, to better meet the demands of tenants and drive income growth.
- To better reflect CREI's focus on income, the board is proposing a change in the company's name from Custodian REIT to Custodian Property Income REIT. This may be especially useful within the retail investment platform space by making the shares more visible to those investors seeking a combination of income and growth.

Consistently positive income-driven returns[2]

Although UK commercial property market returns have historically shown significant cyclicality, the income component has been much less volatile than capital values. CREI's income-focused strategy has consistently generated positive annual total returns. From listing in March 2014 to June 2022 (Q123), it generated an EPRA NAV total return (without assuming reinvestment of dividends paid) of 73.3%, or a compound annual average return of 6.9% pa. Income return has represented the majority of the total return and has been relatively consistent. In the period from IPO to end-FY21, income contributed 100% of total returns, but the strong growth in property values and NAV in FY22 and Q123 has reduced the contribution to c 70%.

Exhibit 1: NAV total return history*

	Annual								Quarterly	Since IPO
	Mar-15	Mar-16	Mar-17	Mar-18	Mar-19	Mar-20	Mar-21	Mar-22	Jun-22	March-14 to Jun-22
	2015	2016	2017	2018	2019	2020	2021	2022	Q123	
Opening EPRA NAV per share (p)	98.2	101.3	101.5	103.8	107.3	107.1	101.6	97.6	119.7	98.2
Closing EPRA NAV per share (p)	101.3	101.5	103.8	107.3	107.1	101.6	97.6	119.7	122.2	122.2
Dividends paid per share (p)	3.750	6.350	6.350	6.425	6.525	6.625	4.913	5.625	1.375	47.9
EPRA NAV total return	7.0%	6.4%	8.5%	9.6%	5.9%	1.0%	0.9%	28.4%	3.2%	73.3%
o/w income returns	3.8%	6.3%	6.3%	6.2%	6.1%	6.2%	4.8%	5.8%	1.1%	48.8%
o/w capital return	3.2%	0.2%	2.2%	3.4%	-0.2%	-5.2%	-4.0%	22.7%	2.1%	24.4%
Compound annual total return										**6.9%**

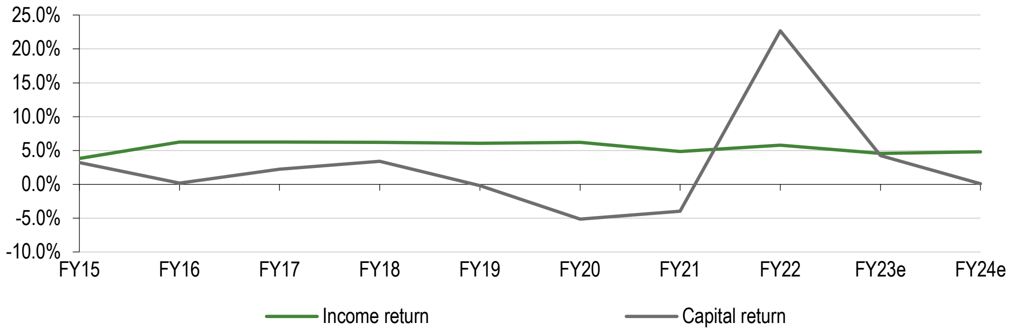
Source: Custodian REIT, Edison Investment Research. Note: *NAV is EPRA NTA per share

The relative consistency of income returns can be seen in the following chart and as interest rates rise, with negative implications for property valuations, we expect this trend to continue.

1 In our view a very low risk activity. CREI typically acquires the land upfront, with planning consent in place, and funds the development of the pre-let asset. During the development phase, it receives a finance coupon equivalent to the net initial yield of the finished asset and at completion acquires the asset at a pre-agreed price.

2 Although the sharp pandemic-related fall in capital values generated a negative total return in Q121 (4.2%), the subsequent quarters each generated positive returns, and total return for the FY21 year was positive.

Exhibit 2: Trend in income return and capital return



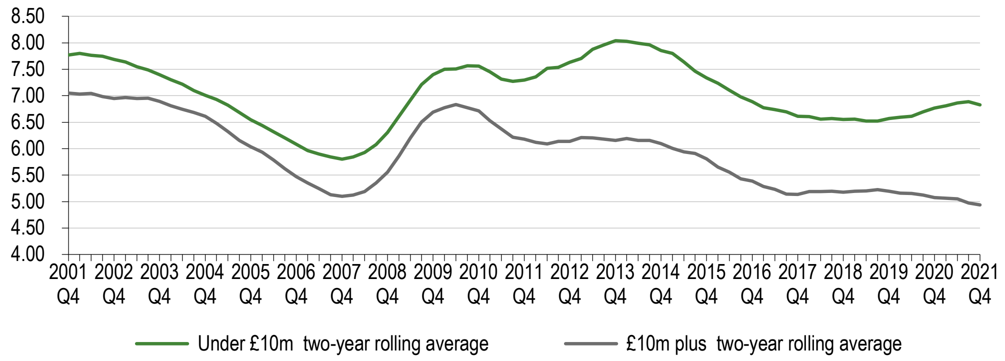
Source: Custodian REIT historical data, Edison Investment Research forecasts

Smaller lot size yield premium supports portfolio income

Reflecting CREI’s focus on higher-yielding, smaller-lot-size properties, the end-Q123 portfolio value of £699.8m reflected an average value per property of c £4.3m. Excluding the DRUM REIT acquisition, during FY22, CREI acquired six assets with an average lot size of £3.6m. The 10 DRUM REIT assets were acquired with an aggregate value of £49m.In FY23 year-to-date CREI has acquired seven assets with an average lot size of £5.9m.

Exhibit 3 compares the transaction net initial yields for properties below £10m versus those above, on a two-year rolling average basis, up to the end of 2021, the most recent available data. On this basis, over a c 20-year period the yield spread of sub-£10m transactions over those of more than £10m has averaged c 1.1%. At end FY21 the spread had widened to c 1.9% compared with c 1.4% immediately before the pandemic. In part, this widening may have reflected investor perceptions of relative risk to the extent that smaller properties may be disproportionately let to smaller tenants, perhaps more exposed to the impacts of the pandemic. Independent data provided to CREI indicate that the spread narrowed a little during Q122. It also indicates that the spread based on lot sizes of less than £15m is a little narrower than for lot sizes of less than £10m but is still clearly positive. As the recent acquisition data show, this does not mean that the intended change to investment policy necessarily indicates a new focus on larger, lower-yielding assets. Rather, the company will have increased flexibility to selectively invest in a wider range of opportunities.

Exhibit 3: Comparison of transaction yields on assets of less than £10m and those greater than £10m*



Source: CREI. Note: *Two-year rolling average basis.

The higher yield on smaller properties is often considered to reflect higher risk and typically a higher cost of management relative to income. However, smaller size does not in itself determine the quality of the property, its appeal to tenants, or the quality of tenant. While there may be less competition for assets from investors, there is an active owner-occupier market which supports vacant possession values and mitigates valuation risk. Asset selection and a long-term approach to investment are key to managing risk and of CREI's strategy for producing an attractive risk-adjusted income return, more than sufficient to offset the additional administrative complexity. Other key elements of CREI's investment strategy for achieving above-average risk-adjusted returns include:

- Diversification by asset, tenant and geographical location, which may be made easier by having a larger number of smaller properties.
- A focus on areas with high residual values.
- Regional locations with strong local economies and favourable demand-supply characteristics.
- No speculative development.

Diversification provides income resilience

Portfolio diversification provides a mitigation to risk in uncertain times such as these and CREI's portfolio is well spread across the main commercial property sectors and by location, tenant and lease term.

Exhibit 4: Portfolio summary

	30-Jun-22	31-Mar-22	31-Mar-21	31-Mar-20
	Q123	FY22	FY21	FY20
Portfolio value	£699.8m	£665.2m	£551.9m	£559.8m
Number of assets	161	160	159	161
Separate tenancies	347	339	265	280
Annualised rent roll	£41.1m	£40.4m	£38.7m	£40.4m
EPRA occupancy rate	88.7%	89.9%	91.6%	95.9%
WAULT	4.7 years	4.7 years	5.0 years	5.3 years
Net initial yield (NIY)	5.5%	5.7%	6.6%	6.8%
Weighted average EPC rating	C (60)	C (61)	C (63)	C (70)

Source: Custodian REIT

At 30 June 2022 (end-Q123) the externally appraised portfolio value of £699.8m reflected a net initial yield of 5.5%, with a rent roll of £41.1m pa. Net transaction activity since has increased the rent roll to £42.4m and the number of properties to 164 from 161. The weighted average unexpired lease term to first break at end-Q123 was 4.7 years.

Of the 347 individual tenancies at end-Q123, the top 10 tenants represented a little more than 20% of overall rent roll, with rents from the largest tenant, Menzies Distribution, spread over eight individual assets. Menzies is one of the UK's leading urban logistics businesses.

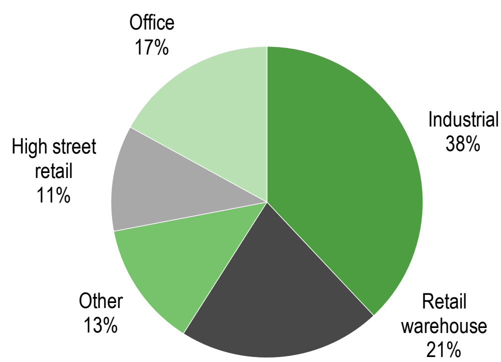
Exhibit 5: Top 10 tenants by share of income at 31 March 2022 (end-FY22)

Menzies Distribution	3.77%	Sainsbury's	1.58%
B&M Retail	3.07%	Homebase	1.56%
B&Q	2.46%	Regus	1.57%
Wickes Building Supplies	2.06%	H&M	1.53%
First Title*	1.59%	Next	1.37%
Top 10 tenants			**20.6%**

Source: Custodian REIT. Note: *Trading as Enact Conveyancing.

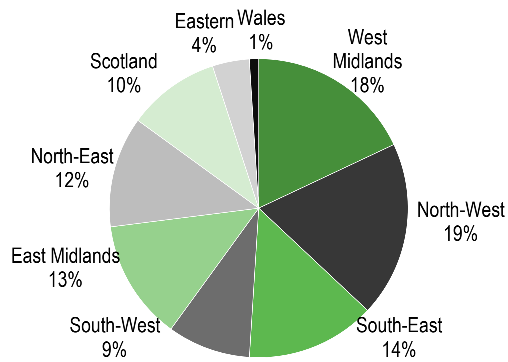
Exhibits 6 and 7 show the sector and geographic spread of the portfolio. Geographically, it has minimal exposure to London, but exposure to every other region. It is split between the main property sectors, in line with the company's objective of maintaining a suitably balanced portfolio, with relatively high exposures to the industrial, retail warehouse and alternative sectors ('other', including drive-through restaurants, car showrooms, trade counters, gymnasiums, restaurants, and leisure units), with relatively low exposure to offices and high street retail. Reflecting yield differences, by value, the industrial weighting is higher (48%) than the income weighting shown in Exhibit 6 and the weightings to offices (12%) and high street retail (8%) are lower. For retail warehouse and 'other', the differences are small.

Exhibit 6: Sector split by income at 31 March 2022 (end-FY22)



Source: Custodian REIT

Exhibit 7: Regional split by income at 31 March 2022 (end-FY22)



Source: Custodian REIT

Diversified but actively managed

Although the portfolio is diversified to manage risk, the investment strategy provides flexibility to adapt to changing market conditions. CREI seeks to position the portfolio to attract the best of occupational market demand through careful stock selection and asset management. This is reflected in active sector positioning and the high weighting currently to industrial and retail warehouse assets, together 69% of the portfolio by value (59% by income).

Asset management has been a key driver of both income and capital growth. This includes lease renewals and re-gears, rent reviews, new lettings, acquisitions and disposals, and investment in asset enhancement, including environmental improvement.

Exhibit 8: Asset management has been a key driver of capital growth

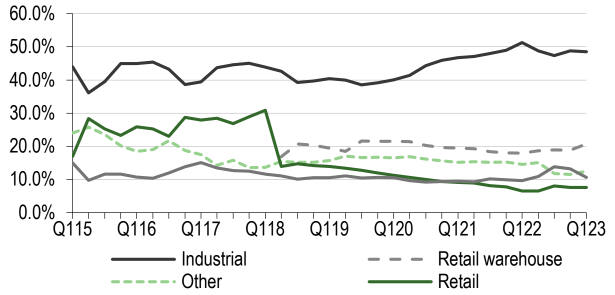
Pence per share	FY18	FY19	FY20	FY21	FY22	5-year
Asset management	2.3	1.6	1.5	2.2	3.0	10.6
General valuation movement	0.8	3.0	(7.7)	(6.9)	16.7	5.9

Source: Custodian REIT

As a long-term investor, changes to the overall portfolio positioning have been evolutionary rather than revolutionary, but we highlight the following:

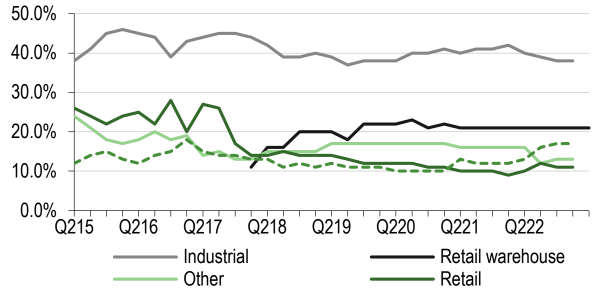
- The significant long-term exposure to industrial/logistical assets that the manager sees as a particularly good fit with CREI's investment strategy, with typically high vacant possession values and relatively low capital expenditure requirements. Growing occupier demand has benefited from the trend towards online purchasing and supply chain disruption, while supply is constrained. The investment manager notes that smaller properties are more expensive to develop, pro-rata, so require higher rents to justify development. With inflation driving build costs higher, it expects continuing rent growth. Strong investment demand has driven yields lower, especially for the 'big box' distribution centres that CREI has no exposure to. More recently, investor sentiment has begun to weaken for these as interest rates increase and, despite the expectation of rent growth, the manager is conscious that this may broaden out across the sector. For CREI's industrial and logistics portfolio, like-for-like rental growth continued in Q123, up 1.7% (FY22: 10.7%), and capital values increased too (+1.8% versus 26.4% in FY22).
- A steadily growing exposure to the out-of-town retail warehouse sub-sector, which benefits from restricted supply, generally free parking and the convenience that is complementary to growth in online sales for both click-and-collect and customer returns. CREI's portfolio is almost exclusively focused on DIY, homewares, discounters and food, all let at affordable rents. Capital values increased by 16.4% in FY22 and 1.5% in Q123. With the occupier profile well matched to current market demand, the investment manager expects rental growth to pick up (down 1.7% in FY22 but up 0.1% in Q123).
- A significant exposure to 'other' sectors, which includes properties with a wide range of tenant exposures that would ordinarily be defensive in terms of the economic cycle, but which in some cases were challenged during the pandemic. These include car showrooms, petrol filling stations, children's day nurseries, restaurants, gyms, hotels, healthcare units, and, more recently, 'drive-thru' restaurants (typically coffee and prepared food) that is in strong demand from an increasing number of tenants. Although rents were down by 2.7% in FY22, the second half of the year saw a recovery (+1.9%), which continued through Q123 (+0.6%).
- A highly selective approach to regional offices, a sector about which the manager has been cautious regarding the potential for ownership costs (through obsolescence and the requirement for capital expenditure, as well as lease incentives) to weigh on net income to a greater extent than is typically the case in other sectors. These factors are more evident in a post-pandemic world where occupiers are focusing on higher-quality space to support business, attract employees back to the office and improve their environmental footprint. To better meet this demand, the company is seeking to reposition its portfolio through suitable acquisitions and identified refurbishment opportunities that it expects will reduce vacancy and drive rental growth. During Q123, rental growth accelerated to 3.4% from 2.7% in the whole of FY22.
- A long-term decline in high street retail exposure, reflecting challenging structural issues that were accelerated by the pandemic. CREI has reorganised its portfolio over the past two years, exiting most of its secondary locations to focus on prime locations where it expects occupier demand to support future rental growth. For CREI's assets, rents and capital values both continued to decline in FY22, each by c 5%, but there are increasing signs of this bottoming out in recent months with good demand for remaining vacant space.

Exhibit 9: Sector positioning (by share of portfolio value) over time



Source: Custodian REIT data, Edison Investment Research

Exhibit 10: Sector positioning (by share of portfolio income) over time



Source: Custodian REIT data, Edison Investment Research

Inflation protection in bricks and mortar

CREI's investment manager expects medium-term rental growth across the market to broadly match inflation, although over shorter periods this relationship is influenced by the incidence of rent reviews (typically on a five-year basis) and the timing of lease maturities. At the end of FY22, 81% of CREI's income was on an open market review basis[3] and the weighted average unexpired lease term to first break across the portfolio was 4.7 years at end of Q123. While recognising the shorter-term visibility of index-linked reviews, the investment manager is cautious of the 'bond-like' characteristics this may create, and the potential for greater emphasis to be placed on the tenant covenant over property fundamentals. It notes that 'at some point in a property's lifecycle, rents will always be re-based to open market values. An over-reliance on index linked rent reviews can lead to disparity between investment values and underlying property values'. For this reason, CREI will continue to target good real estate where open market rent reviews have the capacity to deliver rental growth, aiming to 'provide inflation protection from the bricks and mortar, not the lease contracts'. Although 'under-renting' across the CREI portfolio is relatively modest (c £0.4m), like-for-like ERV continued to grow through Q123.

While lease maturities reflect an element of income risk, they also provide an opportunity to reset rents towards or ahead of ERV. As at end-FY22, c 38% of portfolio rental income was due to mature over the following three years (Exhibit 11), representing a reasonable balance of risk and opportunity in our view.

Exhibit 11: Income expiry profile*

	31-Mar-22	31-Mar-21
	End-FY22	End-FY21
0–1 year	15%	11%
1–3 years	23%	20%
3–5 years	19%	22%
1–10 years	31%	34%
10+ years	12%	13%
Total	100%	100%

Source: Custodian REIT. Note: *To first break or to expiry where no break clause exists.

[3] 81% open market; 8% inflation indexed; 11% fixed uplifts.

Predominantly fixed-rate borrowing provides interest rate protection

CREI operates with moderate gearing and for most of its debt the interest rates are fixed. The end-Q123 net loan to value (LTV) ratio of 21.5% (21.7% including post-Q123 investment activity) remained below the medium-term target of 25%. A Q123 refinancing increased the proportion of agreed debt facilities that are fixed rate to 74% from 61%, providing significant protection against rising interest rates.

In June 2022 CREI arranged a £25m tranche of term debt with existing lender Aviva Real Estate Investors at a fixed 4.10%, using the proceeds to refinance a £25m variable rate revolving credit facility (RCF) with RBS. The RBS facility was acquired with DRUM REIT and was due to expire in September 2022.

Total agreed debt facilities now amount to £190m, of which £140m is fixed-rate debt with a blended cost of c 3.6% and average term to maturity of just under eight years. Including the shorter-term, flexible, floating rate RCF with Lloyds Bank, the total average cost of debt at end-Q123 was 3.2% with an average term to maturity of just over six years. Reflecting the impact of interest rate movements on CREI's floating rate debt, we anticipate an increase to c 3.4% in the average cost of borrowing by end-FY23.

Exhibit 12: Summary of debt facilities at 30 June 2022

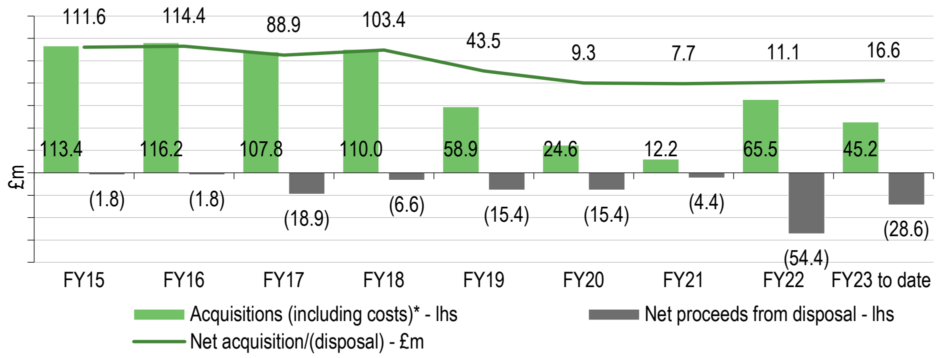
Lender	Facility (£m)	Margin	Term to maturity (years)	Maturity date
Scottish Widows	20.0	3.935%	3.1	13/08/2025
Scottish Widows	45.0	2.987%	5.9	05/06/2028
Aviva tranche 1	35.0	3.020%	9.8	06/04/2032
Aviva tranche 2	15.0	3.260%	10.4	03/11/2032
Aviva tranche 3	25.0	4.100%	10.4	03/11/2032
Total fixed rate	**140.0**	**3.359%**		
Lloyds Bank revolving credit facility	50.0	SONIA +1.5%-1.8%	2.2	17/09/2024
Total debt facilities	**190.0**	**3.2%**	**6.3**	

Source: Custodian REIT data, Edison Investment Research

Seeking further accretive growth

CREI has grown strongly since IPO, increasing an initial seed portfolio of c £95m to an end-Q123 portfolio valuation of c £700m, and it targets further accretive growth. For shareholders, the benefits of growth are for CREI to become a larger, more liquid and further diversified vehicle, appealing to a broad range of investors, that can benefit from scale efficiencies, spreading fixed costs over a wider income-producing asset base and ultimately reducing the marginal rate of asset management charges. With net assets now above £500m, the marginal asset management charge has reduced to 0.65% of average net assets (and the administration fee to 0.05%), and at net assets of more than £750m would fall to 0.55%/0.03%. Initial portfolio growth in the three years to end-FY19 was funded by significant equity raises. Net acquisition activity slowed noticeably in FY20, as attractive opportunities that met CREI's investment criteria were more difficult to identify. Due to high demand for the shares, maintaining a consistent premium to NAV, net acquisitions were funded by share issuance under the company's tap issue facility in addition to capital recycling. During the pandemic, activity slowed further but picked up in FY22, and to a lesser extent net investment, continuing into 2023.

Exhibit 13: Portfolio acquisitions and disposals



Source: Custodian REIT data, Edison Investment Research. Note: *Includes acquisition costs written off.

FY22 was dominated by two main transactions. DRUM REIT was acquired for £43.5m, adding a portfolio of 10 assets with a valuation of £49m. The consideration was settled by the issue of new CREI shares. Also in FY22, a portfolio of nine industrial assets, non-core to CREI over the medium term, was sold for £32.6m, 19% above the start-year valuation.

Including DRUM REIT, during FY22 CREI acquired assets with an aggregate value of £63.5m (before costs) at a blended net initial yield of 6.6%. Properties with an aggregate consideration of £54.5m were sold, £9.6m ahead of the pre-sale valuation, at a blended 6.0% yield for those occupied.

So far in FY23, CREI has acquired properties for an aggregate £41.6m (before costs) at a blended net initial yield of 6.6% and disposed of properties for an aggregate £14.8m, £4.8m ahead of the end-FY22 valuation, at a blended 6.0% yield for those occupied.

Exhibit 14: Summary of recent transactions

Purchases (£m)				Sales (£m)			
Location	Sector	Consideration (£m)	NIY*	Location	Sector	Price	NIY*
Cromer	Retail warehouse	4.5	6.3%	Nottingham & Cheltenham	High street retail	2.9	N/A
Liverpool	Industrial	4.3	5.6%	Day nursery	Other/day nursey	0.6	N/A
Dundee	Industrial	1.9	5.9%	Galashiels	Retail warehouse	4.5	5.7%
Manchester	Office	6.3	6.1%	Portfolio	Industrial (7)	32.6	5.9%
York	Industrial	3.0	5.9%	Stockport	Other/car showroom	9.0	6.7%
DRUM REIT	Portfolio	43.5	6.8%	Stafford	Other/car showroom	4.9	5.8%
FY22 total		**63.5**	**6.6%**			**54.5**	**6.0%**
Grangemouth	Industrial	7.5	5.5%	Derby	Other/car showroom	5.6	5.7%
Winchester	High street retail	3.7	6.4%	Weston-Super-Mare	High street retail	0.7	8.6%
Nottingham	Retail warehouse	15.0	6.2%	Milton Keynes	Industrial	8.5	N/A
York	Retail warehouse	3.0	5.1%				
Measham & Droitwich	Retail warehouse (2)	8.9	9.4%				
Chesterfield	Industrial	3.5	6.1%				
FY23 to-date total		**41.6**	**6.6%**			**14.8**	**6.0%**

Source: Custodian REIT data, Edison Investment Research. Note: *Net initial yield. For purchases includes notional buyers' costs in addition to consideration. Assets that were vacant at the point of sale are shown as N/A.

While CREI's preference is for selective individual property acquisitions, we expect it will also consider further strategic portfolio acquisitions and corporate acquisitions, seeking to benefit from sector consolidation. The company also sees the potential to take market share from struggling open-ended funds. Strategic disposals, particularly of mature assets, may provide capital recycling opportunities, but to significantly grow scale will require additional capital. Maintaining a moderate level of gearing, larger acquisitions will require additional equity and debt capital. Equity issuance for cash, including under the tap issuance facility, is unlikely while the shares trade at a discount to NAV, but given the above-average price to net asset value at which CREI shares trade, vendor placings and equity swaps are possibilities. This was the case with DRUM REIT, which had the added advantage of broadening CREI's shareholder base.

Investing in asset quality and environmental performance

Within its broader ESG strategy, CREI has seen a continuing improvement in the environmental performance of its portfolio. During FY22, the percentage of properties with an EPC rating of C or better increased to 73% from 59% in FY21 and the weighted average EPC score of the portfolio at end-Q123 was C (60) compared with C (61) at end FY22 and C (63) at end-FY21.

The company plans no EPC E-rated properties by 2025 and no D-rated properties by 2027 in line with MEES regulations.[4] Most of the investment required to meet its these targets will form part of the existing rolling programme of asset enhancement and CREI will work with occupiers that share similar environmental performance goals. The company sees such improvements as an opportunity to benefit from improved asset quality, attractive to tenants, with enhanced rents and valuation, generating a positive return on investment. CREI's ESG committee report in the FY22 annual report details its other targets and progress towards achieving these, and a next stage is to publish its net zero carbon pathway.

Exhibit 15: Summary of portfolio EPC ratings by weighted average floor area

	31-Mar-22	31-Mar-21
EPC rating	**End-FY22**	**End-FY21**
A	3%	1%
B	21%	15%
C	49%	43%
A-C total	**73%**	**59%**
D	20%	30%
E	7%	11%
F	0%	0%

Source: Custodian REIT

Recent financial performance: A strong FY22 has continued into Q123

FY22 results were published in June 2022, reflecting CREI's strongest ever year of total returns. On an IFRS basis, earnings increased to £122.3m from £3.7m in FY21, driven by a £117.0m swing in realised and unrealised property gains after acquisition costs (to £97.1m from a loss of £19.9m). Excluding capital gains, EPRA earnings also showed a good level of growth, increasing 6.7% to £25.3m or 5.9p per share (FY21: 5.6p). DPS declared for the year showed a continuing recovery, up 5% to 5.25p and was 110.3% covered by EPRA earnings, while rent collection returned to pre-pandemic levels. Custodian has subsequently published its quarterly update for the three months that ended 30 June 2022 (Q123), which shows further progress with a three-month total return of 3.2%.

Exhibit 15 shows a summary of the FY22 results. We highlight the following:

- Net rental income increased by £2.5m (7.6%) to £35.6m. The increase reflected higher annualised contracted rents and a reduction in rent receivable charges, partly offset by higher non-recoverable property operating costs.
- Administrative expenses increased £0.9m to £5.5m. Within this, management fees increased £0.4m, reflecting the growth in NAV, and other administrative costs by £0.4m, driven by

[4] Minimum Energy Efficiency Standards.

increased staff costs and additional costs relating to the development of the pathway to net zero carbon and other sustainability linked costs.

- With interest costs flat, EPRA earnings increased £1.6m (6.7%) to £25.3m or 5.9p per share (FY21: 5.6p). DPS declared increased by 5% to 5.25p and was 110% covered.
- Including realised and unrealised property gains net of acquisition costs, IFRS earnings were £122.3m, taking NAV per share to 119.7p (FY21: 97.6p; H122: 106.0p). Including DPS paid the total return was 28.4%.

Exhibit 16: Summary of FY22 financial performance

Year end March (£m unless stated otherwise)	FY22	FY21	FY22/FY21	Edison FY22 forecast
Gross rental income	39.0	38.7	1.0%	39.1
Non-rechargeable property costs	(3.3)	(2.0)		(2.9)
Receivables provision/write-off	(0.2)	(3.6)		(0.2)
Net rental income	**35.6**	**33.1**	**7.6%**	**36.0**
Administrative expenses	(5.5)	(4.6)	20.7%	(5.2)
Operating Profit before revaluations	30.1	28.5	5.5%	30.8
Net interest	(4.8)	(4.8)		(4.9)
EPRA earnings	**25.3**	**23.7**	**6.7%**	**25.9**
Revaluation of investment properties	94.0	(19.6)		71.4
Costs of acquisitions	(2.3)	(0.7)		(3.1)
Profit on disposal	5.4	0.4		5.3
IFRS earnings	**122.3**	**3.7**		**99.5**
IFRS EPS (p)	28.5	0.9		23.2
EPRA EPS (p)	5.9	5.6	4.5%	6.0
DPS (declared) (p)	5.25	5.00	5.0%	5.50
EPRA earnings/dividends paid in period (x)	110.3	112.7	99.3%	109.2
IFRS NAV & EPRA NTA per share (p)	119.7	97.6		114.7
Investment portfolio (£000s)	665.2	551.9	20.5%	669.1
NTA total return	28.4%	0.9%		23.5%
Net LTV	19.1%	24.9%		23.3%

Source: Custodian REIT data, Edison Investment Research

Q123 NAV total return 3.2%

Further progress in Q123 included NAV growth of 2.1% to 122.2p, driven by a 1.7% like-for-like increase in portfolio valuations. ERV increased by 1.4% like-for-like and net capital deployment added 1.5% to annualised rent roll of £41.1m (end-FY22: £40.5m). Strong leasing activity saw 13 new leases secured, adding £1.8m of annualised rental income for an average 6.8 years. The positive impact of letting four vacant units was offset by vacancy at two industrial properties earmarked for refurbishment and another that has since been profitably divested, with EPRA occupancy reducing to 88.7% (end-FY22: 89.9%). A Q123 DPS of 1.375p, in line with Q422, is consistent with the FY23 target of at least 5.5p and was covered by EPRA earnings. Quarterly EPRA EPS of 1.4p (Q422: 1.6p) was affected by the timing of capital deployment and the change in occupancy.

Forecast update

The changes in our EPRA earnings forecasts are driven by higher administrative costs and net interest expenses.

Exhibit 17: Forecast revisions

	Net rental income (£m)			EPRA EPS (p)			DPS (p)			EPRA NAV/share (p)			Net LTV		
	Old	New	Change (%)	Old	New	Change (%)	Old	New	Change (%)	Old	New	Change (%)	Old	New	Change (pp)
03/23e	39.4	38.8	-1.7	6.5	6.0	-7.4	6.00	5.63	-6.3	116.7	124.7	6.9	23.2%	23.0%	0.2
03/24e*	40.0	40.0	0.0	6.6	6.1	-6.9	6.50	6.00	-7.7	118.7	124.9	5.2	23.3%	24.0%	-0.7

Source: Edison Investment Research. *Our last published note showed FY24e EPRA EPS of 6.7p due to an incorrect adjustment from IFRS to EPRA earnings for revaluation gains.

The increase in administrative costs is substantially related to higher management fees, reflecting the strong growth in NAV and despite the lower marginal fee reducing with growth. We also expect other administrative costs to be higher than previously, in line with FY22. The increase in our forecast interest charge reflects borrowing costs rather than the level of borrowing.

Exhibit 18: Change in EPRA earnings forecasts

£m	New estimate		Old estimate		Change in estimate	
	FY23e	FY24e	FY23e	FY24e*	FY23e	FY24e
Net rental income	38.8	40.0	39.4	40.0	(0.7)	(0.0)
Administrative expenses	(6.4)	(6.6)	(5.6)	(5.7)	(0.9)	(0.9)
Net interest	(5.9)	(6.4)	(5.3)	(5.3)	(0.6)	(1.1)
EPRA earnings	26.4	27.0	28.5	29.0	(2.1)	(2.0)

Source: Edison Investment Research. *Our last published note showed FY24e EPRA earnings of £29.6m due to an incorrect adjustment from IFRS to EPRA earnings for revaluation gains

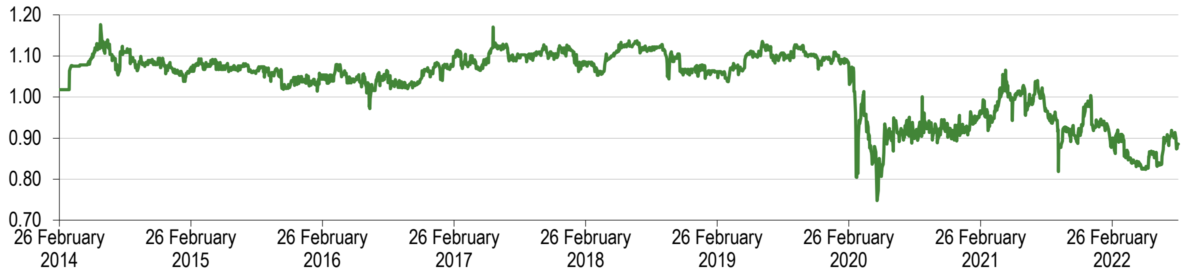
Our gross rental income forecasts are little changed and reflect like-for-like ERV growth of c 2.8% in FY23 (Q123 c 1.4%). This may prove to be conservative given the growth currently being experienced. Similarly, our forecasts imply only a modest increase in occupancy from 88.7% at end-Q123 to c 89.0% at end-FY23 and 89.4% at end-FY24. We have assumed no acquisitions or disposals other than those already announced, although capital recycling is likely.

Following a 1.7%/£11.3m like-for-like valuation increase in Q123, we forecast c 2.6%/£18.7m for the year and flat in FY24. We estimate that a 0.5% increase in the valuation yield (Q123: 5.54%) would reduce NAV per share by c 14p.

Valuation and performance

CREI's target DPS for FY23 of at least 5.5p represents a prospective yield of 5.2%. Based on our forecast DPS of 5.625p, the yield is slightly higher. Meanwhile, the shares trade at a c 13% discount to the Q123 NAV per share of 119.7p, below the average premium of c 3% since IPO.

Exhibit 19: P/NAV history



Source: Refinitiv prices at 29 August 2022, Custodian REIT NAV data, Edison Investment Research

In Exhibit 20, we show a summary performance and valuation comparison of CREI and what we consider to be its closest diversified income-oriented peers. CREI's share price performance is above the peer group average over one and three years. For comparative purposes, the valuation data are shown on a trailing basis. CREI trades on a higher P/NAV than the average of the group, as it has done for most of the period since IPO, and its trailing yield is below average. Factors supporting CREI's valuation include uninterrupted quarterly DPS during the pandemic (albeit at a reduced level), moderate gearing and a focus on smaller lot size properties with a yield premium that has historically supported risk-adjusted income returns.

Exhibit 20: Peer performance and valuation summary

	Price (p)	Market cap (£m)	P/NAV (x)	Trailing yield (%)**	Share price performance			
					1 month	3 months	1 year	3 years
Ediston Property	74	156	0.77	6.8	-6%	-8%	-4%	-33%
BMO Real Estate Investments	88	209	0.66	4.6	8%	-5%	19%	-10%
BMO Commercial Property Trust	107	754	0.72	4.2	-11%	-9%	6%	-27%
Picton	91	498	0.74	3.8	-2%	-8%	-6%	0%
Regional REIT	71	366	0.73	9.2	-4%	-16%	-20%	-25%
Schroder REIT	53	259	0.67	5.9	-3%	-3%	2%	-15%
Standard Life Investment Property	76	292	0.72	5.0	-3%	-5%	7%	-19%
UK Commercial Property REIT	71	921	0.63	7.0	-5%	-16%	-10%	-20%
Average			**0.71**	**5.6**	**-3%**	**-9%**	**-1%**	**-19%**
Custodian	**106**	**467**	**0.87**	**5.1**	**-3%**	**8%**	**8%**	**-12%**
UK property sector index	1,567				-9%	-13%	-20%	-14%
UK equity market index	4,076				-1%	-3%	-1%	-3%

Source: Company data, Refinitiv prices at 29 August 2022. Note: *Based on last reported EPRA NAV/NTA. **Based on trailing 12-month DPS declared.

Additional details on the company and management

Custodian REIT is an externally managed UK real estate investment trust (REIT), listed on the Main Market of the London Stock Exchange. Its portfolio of commercial property assets is managed with the objective of providing long-term, secure income with an attractive target dividend and long-term NAV growth. To this end, CREI looks to maintain a diverse tenant, region and sector mix with properties, outside of London, with high residual values and a lower risk of obsolescence. It is differentiated from most peers by investing in smaller lot-size assets of between £2m and £10m at the point of acquisition, where there is less price competition.

The board

CREI's board of directors typically comprises six members, all of whom are non-executive and responsible for the overall management of the company's activities. The board is chaired by David Hunter, a professional strategic adviser focused principally on UK and international real estate, who sits on the boards of a number of listed and unlisted companies, as well as holding corporate advisory roles.

The independent non-executive directors are Hazel Adam, who joined the board in December 2019, bringing a range of experience including the buy-side and sell-side investment industry, strategies and markets; Elizabeth McMeikan, a former Tesco executive and experienced board member, appointed in March 2021; Chris Ireland, a former CEO of JLL UK and former chair of the Investment Property Forum, who also joined the board in March 2021; Malcolm Cooper, who has extensive board experience and a background in corporate finance, infrastructure and property, and who joined the board in June 2022, replacing Matthew Thorne, who will retire at the AGM in August 2022 after eight years' service. Ian Mattioli, chief executive officer of Mattioli Woods and a board member of the investment manager, is also a non-executive board member but deemed not to be independent. Ed Moore, finance director of Custodian Capital, is company secretary to CREI. Full details of the board can be found at www.custodianreit.com/about-us-2/meet-the-directors/.

The investment manager

The company is externally managed by Custodian Capital (www.custodiancapital.com), a wholly owned subsidiary of Mattioli Woods (www.mattioliwoods.com). Custodian Capital was appointed investment manager at the IPO, an arrangement that is subject to regular board review. Richard Shepherd-Cross is the managing director of Custodian Capital and the fund manager of CREI. He is a former director of Jones Lang LaSalle in London, where he led the portfolio investment team before joining Mattioli Woods in 2009, with responsibility for its syndicated property initiative, the precursor to Custodian. In total, the Custodian Capital team that is dedicated to the management of CREI's assets consists of 18 members, including six property professionals.

Management and administration fees are paid to the manager on a sliding scale that allows shareholders to benefit from growth in NAV. The fees on continued growth in NAV above £500m were reduced during the year.

- **Property management fees** are charged at 0.90% pa on average net assets of up to £200m, 0.75% pa between £200m and £500m, 0.65% between £500m and £750m, and 0.55% above £750m.
- **Administrative fees** are charged at 0.125% pa on average net assets up to £200m, 0.08% pa between £200 and £500m, 0.05% between £500m and £750, and 0.03% above £750m.

Sensitivities

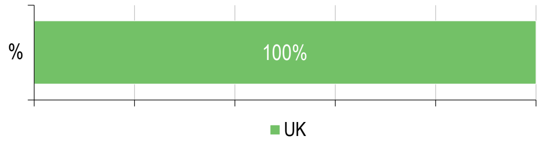
The commercial property market is cyclical, historically exhibiting substantial swings in valuation through cycles. Income returns are significantly more stable, but still fluctuate according to tenant demand and rent terms. From a sector viewpoint, we also highlight the increased risks and uncertainties that attach to development activity, including planning consents, timing, construction risks and the long lead times to completion and eventual occupation. CREI's development exposure is modest and limited to the improvement of existing properties. In this respect it may best be seen as an extension of its refurbishment activity, aimed at enhancing long-term income growth and returns. Forward funded development activity is likewise modest and, in our view, very low risk. More generally we note the sensitivity to:

- **Economic risk:** the war in Ukraine and sharply rising inflation, to a lesser extent reflected in interest rates, are creating a high level of uncertainty regarding the global and UK economic outlook. Although the incidence and impact of the pandemic has substantially eased, there remains some uncertainty about the potential emergence of new strains.
- **Sector risk**: some of the inherent cyclical risk to vacancy in commercial property can be mitigated by portfolio diversification. CREI's portfolio is highly diversified by asset, sector, tenant and geography, with a focus on properties with higher yields and residual values.
- **Energy performance considerations:** a failure to successfully meet regulatory and/or tenant expectations for energy performance enhancement would likely affect CREI's ability to let properties on satisfactory terms and may make properties unlettable.
- **Funding risks:** three-quarters of debt facilities are fixed rate and longer term, mitigating interest rate risk. Increasing long-term rates may be expected to negatively affect market-wide property valuations.
- **Management risk**: as CREI is externally managed, any management risk is indirect. Custodian Capital, the external manager, operates with a relatively small team, and if a senior member of that team were to leave, they would need to be replaced.

Exhibit 21: Financial summary

Year end 31 March, £m	2018	2019	2020	2021	2022	2023e	2024e
	IFRS	IFRS	IFRS	IFRS	IFRS	IFRS	IFRS
PROFIT & LOSS							
Gross rental income	34.1	39.1	40.0	38.7	39.0	41.8	42.7
Non-recoverable property costs	(0.9)	(1.5)	(1.5)	(2.0)	(3.3)	(3.0)	(2.7)
Rent receivables provisions/write	0.0	0.0	(0.3)	(3.6)	(0.2)	0.0	0.0
Net rental income	33.2	37.6	38.1	33.1	35.6	38.8	40.0
Administrative expenses	(4.4)	(4.9)	(4.8)	(4.6)	(5.5)	(6.4)	(6.6)
Operating Profit before revaluations	28.8	32.7	33.4	28.5	30.1	32.3	33.4
Revaluation of investment properties	11.9	(5.5)	(25.9)	(19.6)	94.0	18.7	0.0
Costs of acquisitions	(6.2)	(3.4)	(0.6)	(0.7)	(2.3)	(2.7)	0.0
Profit/(loss) on disposal	1.6	4.3	(0.1)	0.4	5.4	4.6	0.0
Operating Profit	36.1	28.0	6.8	8.6	127.2	53.0	33.4
Net Interest	(3.7)	(4.4)	(4.7)	(4.8)	(4.8)	(5.9)	(6.4)
Profit Before Tax	32.4	23.6	2.1	3.7	122.3	47.1	27.0
Taxation	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Profit After Tax	32.4	23.6	2.1	3.7	122.3	47.1	27.0
Net revaluation of investment property/costs of acquisition	(5.6)	8.9	26.4	20.3	(91.7)	(16.0)	0.0
Gains/(losses) on disposal	(1.6)	(4.3)	0.1	(0.4)	(5.4)	(4.6)	0.0
EPRA earnings	25.2	28.5	28.7	23.7	25.3	26.4	27.0
Average Number of Shares Outstanding (m)	362.4	391.9	409.7	420.1	428.7	440.9	440.9
IFRS EPS (p)	8.9	6.0	0.5	0.9	28.5	10.7	6.1
EPRA EPS (p)	6.9	7.3	7.0	5.6	5.9	6.0	6.1
Dividend per share (p)	6.45	6.55	6.65	5.00	5.25	5.63	6.00
Dividend cover (x)*	1.06	1.10	1.04	1.13	1.10	1.07	1.02
Ongoing charges ratio (excluding property expenses)	1.15%	1.12%	1.12%	1.12%	1.20%	1.19%	1.20%
NAV total return		5.9%	1.1%	0.9%	28.4%	8.8%	4.9%
BALANCE SHEET							
Fixed Assets	528.9	572.7	559.8	551.9	665.2	725.1	735.9
Investment properties	528.9	572.7	559.8	551.9	665.2	725.1	735.9
Other non-current assets	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Current Assets	12.9	6.1	30.7	9.9	16.8	20.0	10.2
Debtors	7.9	3.7	5.3	6.0	5.2	7.6	7.7
Cash	5.1	2.5	25.4	3.9	11.6	12.3	2.5
Current Liabilities	(12.8)	(14.2)	(14.9)	(12.8)	(39.9)	(17.6)	(17.7)
Creditors/Deferred income	(12.8)	(14.2)	(14.9)	(12.8)	(17.2)	(17.6)	(17.7)
Short term borrowings	0.0	0.0	0.0	0.0	(22.7)	0.0	0.0
Long Term Liabilities	(113.9)	(138.1)	(148.9)	(139.2)	(114.5)	(177.6)	(178.0)
Long term borrowings	(113.4)	(137.5)	(148.3)	(138.6)	(113.9)	(177.0)	(177.4)
Other long term liabilities	(0.6)	(0.6)	(0.6)	(0.6)	(0.6)	(0.6)	(0.6)
Net Assets	415.2	426.6	426.8	409.9	527.6	550.0	550.5
NAV/share (p)	107.3	107.1	101.6	97.6	119.7	124.7	124.9
EPRA NAV/share (p)	107.3	107.1	101.6	97.6	119.7	124.7	124.9
NAV total return	9.6%	5.9%	1.1%	0.9%	28.4%	8.8%	4.9%
CASH FLOW							
Operating Cash Flow	28.4	36.0	31.0	23.8	32.6	29.5	32.7
Net Interest	(3.5)	(4.2)	(4.4)	(4.5)	(4.5)	(5.5)	(6.1)
Tax	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Net additions to investment property	(105.9)	(46.2)	(12.2)	(10.1)	26.6	(38.5)	(10.0)
Ordinary dividends paid	(23.0)	(25.5)	(27.0)	(20.6)	(24.2)	(24.7)	(26.5)
Debt drawn/(repaid)	49.4	24.0	10.5	(10.1)	(25.1)	40.0	0.0
Proceeds from shares issued (net of costs)	53.9	13.3	25.0	0.0	0.5	0.0	0.0
Other cash flow from financing activities	0.0	0.0	0.0	0.0	1.7	0.0	0.0
Net Cash Flow	(0.7)	(2.6)	22.9	(21.5)	7.7	0.7	(9.8)
Opening cash	5.8	5.1	2.5	25.4	3.9	11.6	12.3
Closing cash	5.1	2.5	25.4	3.9	11.6	12.3	2.5
Debt as per balance sheet	(113.4)	(137.5)	(148.3)	(138.6)	(136.6)	(177.0)	(177.4)
Unamortised loan arrangement fees	(1.6)	(1.5)	(1.7)	(1.4)	(1.2)	(0.8)	(0.4)
Total debt	(115.0)	(139.0)	(150.0)	(140.0)	(137.8)	(177.8)	(177.8)
Restricted cash	(1.3)	(1.4)	(0.9)	(1.2)	(1.1)	(1.4)	(1.4)
Closing net debt	(111.3)	(137.9)	(125.5)	(137.3)	(127.3)	(166.8)	(176.7)
Net LTV	21.0%	24.1%	22.4%	24.9%	19.1%	23.0%	24.0%

Source: Custodian REIT historical data, Edison Investment Research

Contact details	Revenue by sector
Custodian REIT c/o Custodian Capital 1 New Walk Place, Leicester LE1 6RU UK +44116 240 8740 Company website: www.custdianreit.com Investment adviser website: www.custodiancapital.com	

Leadership team

Independent non-executive chair, Custodian REIT: David Hunter	Senior independent NED, Custodian REIT: Elizabeth McMeikan
David Hunter is an international property consultant, specialising in supporting the creation, operation and liquidation of property funds and companies. He is chairman of a UK-based real estate debt fund manager and has corporate advisory roles in the UK and France. He was managing director of Aberdeen Asset Management's £6.5bn UK and international property fund business from 2001–04. He was president of the British Property Federation in 2004.	Elizabeth McMeikan's substantive executive career was with Tesco, where she was a stores board director before embarking on a non-executive career in 2005. She is currently senior independent director (SID) at Unite, the UK's largest owner, manager and developer of purpose-built student accommodation and non-executive director (NED) of Dalata Hotel Group, the largest hotel group in the Republic of Ireland. Her other board roles include NED at McBride, Europe's leading manufacturer of cleaning and hygiene products, and NED of Fresca Group, a fruit and vegetable import/export company. Previously Elizabeth was SID of JD Wetherspoons and Flybe and chair of Moat Homes.
Managing director of Custodian Capital: Richard Shepherd-Cross	**Finance director, Custodian Capital: Ed Moore**
Richard Shepherd-Cross is the managing director of Custodian Capital and the fund manager of Custodian REIT. He is a chartered surveyor and a former director of Jones Lang LaSalle in London, where he led the portfolio investment team. He joined Mattioli Woods in 2009, where he was responsible for the management and growth of the syndicated property portfolio, which was the precursor to CREI. He was instrumental in establishing CREI and raising £55m at IPO.	Ed Moore qualified as a chartered accountant with Grant Thornton in 2003. He is finance director of Custodian Capital, with responsibility for all day-to-day financial aspects of its operations, and company secretary of Custodian REIT, where his key responsibilities are ongoing regulatory compliance, accurate external and internal financial reporting and maintaining a robust control environment. Since the Custodian REIT IPO in 2014, Ed has overseen it raising over £300m of new equity, arranging or refinancing six loan facilities and completing three corporate acquisitions.

Principal shareholders as at 16 June 2022 (Source: FY22 Annual Report)	(%)
BlackRock	5.3%
Mattioli Woods	4.0%

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