Hammerson

CLUCASGRAY

13	9	17	1 m	180 m
Destinations	Premium outlets	Cities	sq m of lettable area	Shopper visits per year

Hammerson has had three near death experiences since 2015…

- 2015 saw the start of the online shopping craze in the UK where free delivery and free collection spelt the end of shopping centres for some critics who predicted tumble weeds rolling through shopping centres. Fast forward to 2022 and we have seen the peak of online shopping as the free delivery and collection has severely dented margins to the point where £8 of online sales is needed to achieve the same profit margins as £5 of instore sales. Online-only retailers, such as Amazon, are now renting space in destination centers owned by Hammerson.

  The table below highlights retailers thinking on brick-and-mortar stores…

Flight to quality - best-in-class retailers value the importance of physical space

next	Our stores play an important role in supporting our Online customers; nearly half of our UK Online orders are collected instore and the majority of returns are through our stores (85%). *Next Annual Report 2022*
JD	The Group is committed to showcasing brands in a premium environment and stores remain a core part of our strategy *JD Sports Annual Report 2022*
NIKE	"Our smaller format concept stores allow us to design insight-driven journeys to personally engage with our customers, all with the purpose to inform, inspire and engage." *Lucy Ramseyer, senior retail director UK&IRE at NIKE 2022*
M&S EST. 1884	The investment in M&S' accelerated store rotation programme aims to create an estate of 180 Full Line stores and 420 owned food stores by FY25/26, creating over 3,400 new jobs *M&S Press Release 2022*
Apple	Certain stores have been designed and built to serve as high-profile venues to promote brand awareness *Apple Annual Report 2021*
PRIMARK®	"You've got to start to question the maturity now of online in the United Kingdom" *John Bason, finance director of Associated British Foods 2023*

- Online shopping was followed by the CVA (company voluntary arrangement) phase which started in 2018. Much like our Business Rescue methodology, CVA's allowed indebted retailers to renegotiate, or in some cases not pay rent at all during the process. This wave of CVA's is now over, leaving a strengthened group of UK retailing companies wanting to expand.
- Covid then hit in early 2020 forcing the closure of discretionary retail, forcing consumers into online shopping and allowing retailers not to pay rent as they could not be closed down due to UK emergency Covid rules. Thankfully this is now behind us!

These three issues left the UK shopping centre valuations down 65%, France down 30% and Ireland down 31%. Valuations are not scientific and very much rely on human sentiment which, as markets prove, swing wildly from euphoria to depression. This left Hammerson's iconic destination UK shopping centres with yields of 7.2% to 9.5%.

But it gets better…Hammerson trades at a c.50% discount to this published valuation with hidden value in one key asset, inappropriately called "Value Retail".

Value Retail has 9 villages in 9 European countries selling extremely expensive luxury goods (it's the extreme opposite of value centers in South Africa) and is valued at £1.9bn. Hammerson charges no rent but rather 20% of turnover, providing a cheap entry to the luxury good market. Richemont trades at 29x PE, LVMH 31x, Kering 19x, Hermes 61x, Prada 27x and Christian Dior 26x as the rich get richer and demand for luxury goods grows significantly faster than global GDP growth. On the 25th of April 2023 Hammerson announced in its pre-AGM trading update that Value Retail footfall was up 14% with Q1 sales up 17% on Q1 2022 sales. This is an astonishing figure compared to European retail sales which are down over 2%.

Hammerson has a market cap of £1.33bn with Value retail valued at £1.887bn (less the debt it amounts to £1.189bn).

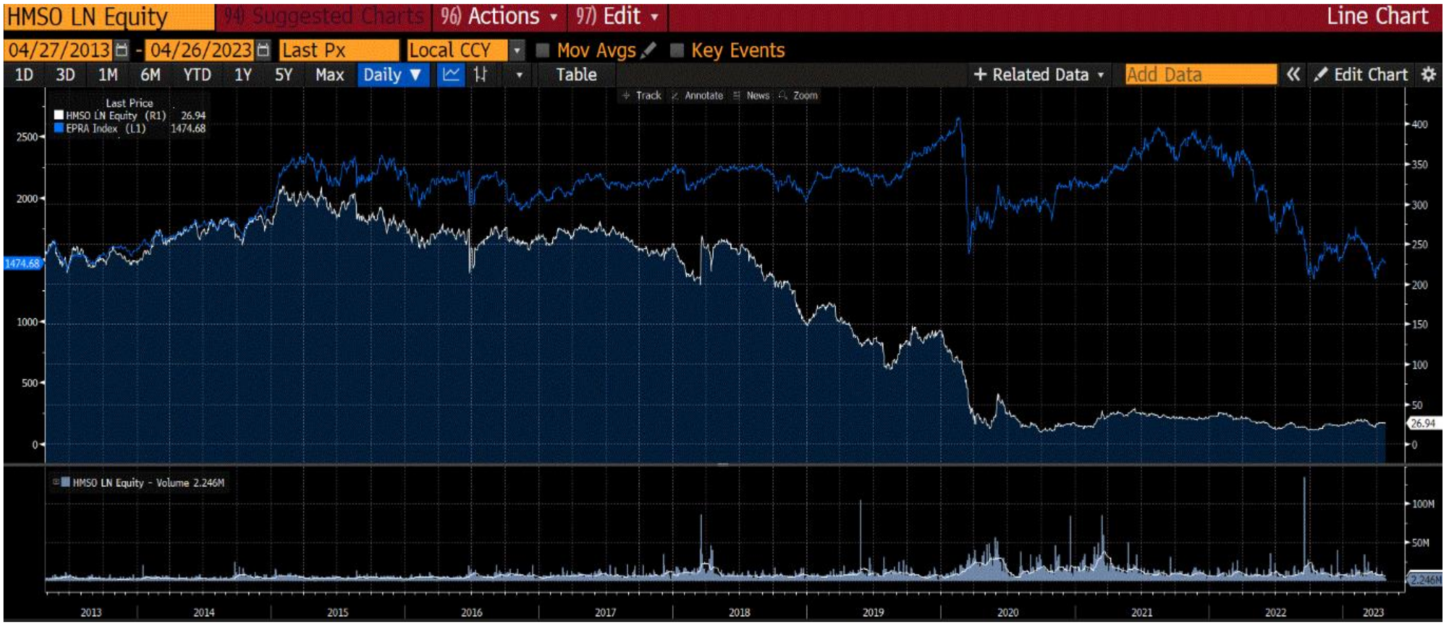
But there's more…The core business of 13 destination shopping centers, defined as the "managed portfolio" is valued at c.£2.8bn (post some recent disposals) and includes iconic centers such as Brent Cross in London, Bullring in Birmingham, Dundrum in Ireland and O'Parinor in Paris. The full list of destinations can be found here at https://www.hammerson.com/destinations

We have avoided UK property retailers in the past as they have been under tenant pressure to cut rents for the past 7 years. Now, however, with online retail concerns easing, CVA's over and Covid behind us, we are seeing rental tension building as retailers seek to expand and services and entertainment becomes a larger user of retail space. The recent 2022 results confirm leasing tension growing which allows for rental increases - this is reiterated in the Q1 2023 trading update with headline rent renewals 18% ahead of previous passing rent and 5% ahead of ERV (the valuers assessment of what the rent should be for a new tenant). Q1 footfall in the UK and France was up 6% and Ireland up 13%, with retail sales up 6% in the UK, 11% in France and 7% in Ireland.

Occupancy is up to 95% and the LTV (Loan to value) continues to fall from mid-40's to 35% (which is a very good low gearing ratio).

Hammerson's Westquay Centre in the UK.

WHAT'S IT WORTH?



The Bloomberg graph above is Hammerson (white line) over a 10-year period indexed to 100 against the EPRA index blue line (European Property Index). The graph highlights the three death defying events, online retailing starting in 2015, CVA's staring in 2018 and Covid in 2020. Important to note is how stable Hammerson has been while the index fell in 2022 due to rising interest rates. This is due to the already high cap rates applied to the properties and the expectation of interest rates rolling over in 2024.

Management indicated on their recent roadshow through Johannesburg that Value Retail was potentially for sale (values referred to above) as well as having £432m of development assets. This could potentially result in £1.62bn (after settling the Value Retail debt of £675m) of asset sales on a £1.33bn market cap.

NAV is 53p (R12.15) and FFO yield (the equivalent of distributable earnings in South Africa) is 7.8%.

With these positive tailwinds it's not difficult to see Hammerson trade up to NAV of 53p. Hammerson last traded at a premium to NAV in early 2015 before the online retailing concerns started to worry investors. At the very least the 10-year average discount to NAV would imply a 32% return to 35.5p (R8.14 @ R22.94/£)

Brendon Hubbard

26 April 2023