November 28, 2022

Raghsa

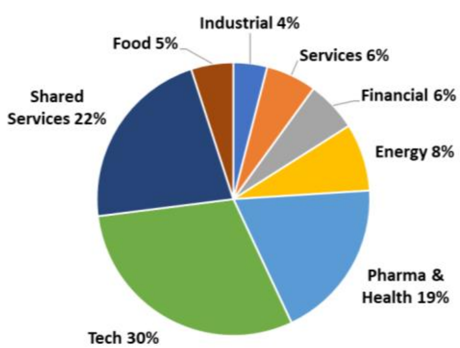
Raghsa is a company founded in 1969 dedicated to the development, construction, sale, and rental of high-quality office buildings and residential towers. The Company leads Argentina's class A offices market and is one of the major companies focused on the development of luxury residential towers.

The company's operating income comes from the sales of real estate and the rental and administration of the Property Owners Association. Among its already-built and sold residential towers are the well-known Le Park Puerto Madero and Le Park Figueroa Alcorta in Argentina and Le Park Punta del Este I, II, III in Uruguay.

The Company is currently embarking on a new project, Centro Empresarial Nuñez, in order to expand its high-end offices portfolio. Moreover, Raghsa owns the One Union Square South building in New York City, which allows the company to diversify market risks.

Raghsa's local clients are a mix of highly renowned local and international corporations. Current clients include Chevron, Facebook, Navent, HP, TGN, L'Oréal, DOW, PedidosYa, Quilmes, Glaxo, JPMorgan, Amazon, Itaú, Lenovo, Loma Negra, and Raizen, among others.

% Revenue by customer's sector



Source: Sekoia Research based on Raghsa presentation Oct-22.

Results

The square meter in Argentina's premium office market is priced in US dollars. Income from rentals is tied to the official FX rate. Furthermore, Raghsa's assets located abroad provide the company with the possibility of obtaining hard dollars. As it will be shown, in line with its business, Raghsa's assets and liabilities are also denominated in hard currency. For this reason, we will analyze Raghsa's results reported in Argentine pesos at the average official FX rate or the closing FX rate as appropriate for each balance sheet period.

Raghsa presented its latest results at the end of the second quarter of the 2023 fiscal year, dated August 31, 2022. It should be noted that the company closes each fiscal year in February.

During the last quarter, the company sold two of its office buildings in order to focus its operations on the northern corridor of the city of Buenos Aires. The company sold Madero Riverside, a tower of 16,024 rentable square meters for USD 70 million, and completed the sale of Edificio Plaza San Martin by selling the remaining functional units and parking lots of 9,375 rentable square meters for USD 27 million.

The current portfolio of corporate office buildings is composed of the Madero Office Tower (13,146 m²), the 955 Belgrano Office Tower (30,499 m²), and the Centro Empresarial Libertador (60,220 m²). The total rentable area is 103,865 square meters with an average occupation rate that reached 85% at the end of August. The sale of the Edificio Plaza San Martin, which had a low occupancy rate, allowed an improvement of this indicator compared to the previous quarter. Raghsa keeps almost total occupancy in its newer and highest quality properties: Belgrano office with 93% occupancy and Centro Empresarial Libertador with 92%. Both buildings are Gold certified by the U.S. Green Building Council (USBGC) and represent 87% of the company's total rentable square meters. Centro Empresarial Libertador was inaugurated in January 2020 and it's the largest Class AAA office building in Argentina.

Occupation (%)	Edificio Plaza San Martín	Madero Office	Belgrano Office	Madero Riverside	Ctro. Emp. Libertador	Total
rentable m2	-	13.146	30.499	-	60.220	**103.865**
2Q2023	-	35%	93%	-	92%	**85%**
1Q2023	36%	35%	93%	64%	94%	**80%**
Var (bps)	-	*0*	*0*	-	*-200*	***524***
2Q2022	68%	55%	93%	96%	92%	**86%**
Var (bps)	-	*-2000*	*0*	-	*0*	***-69***
2T2021	88%	75%	97%	100%	74%	**83%**
Var (bps)	-	*-4000*	*-400*	-	*1800*	***171***

Source: Sekoia Research based on Raghsa's financial statements.

At the end of the first semester, Raghsa reported revenues of USD 27.1 million from office rentals, an increase of 14% versus the same period of the previous year and a rise of 63% with respect to the same period of the 2021 fiscal year. As stated in previous reports (see here) the increase in revenues was mainly explained by the incorporation of the Centro Empresarial Libertador, a property that today represents 58% of the company's rentable square meters. It should be noted that income from rentals may correspond mostly to the office occupancy of previous periods. In the second quarter of the 2022 fiscal year, Raghsa reached a record occupancy of more than 116,000 m² in five buildings.

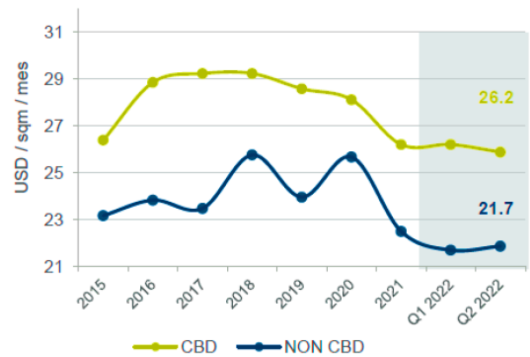
On the other hand, while revenues from rental contracts showed growth, the cost of revenues and administrative and commercial expenses have been growing at a faster pace. Rental costs represented 14% of the rent while they used to represent only 5% in the previous fiscal year. Likewise, expenditures totaled USD 13 million, which is 94% higher than the previous fiscal year. This effect was due to a combination of higher expenditures in fees, taxes, and contributions along with the increase of local costs in dollars. The macroeconomic imbalances of the Argentinean economy alter corporate balance sheets. August 2022 closed with a depreciation of the peso at 42% y/y, while inflation reached 71% y/y.

Revenues (US millions)	6M2023	6M2022	Var (%)	6M2021	Var (%)
Rental revenues	27,1	23,7	14%	16,6	63%
Cost of rental revenues	3,8	4,0	-5%	0,8	395%
Cost/Rental revenues (%)	14%	17%	-300bps	5%	900bps
Consortium revenues	0,5	0,4	37%	0,3	77%
Adm. & comm. expenses	13,0	6,7	94%	3,4	283%
Expenses/rental rev. (%)	48%	28%	2000bps	20%	2800bps

Source: Sekoia Research based on Raghsa's financial statements.

We could project upcoming revenues taking the average price of USD 26.2 per rentable square meter estimated by the company and the current office portfolio. With maximum occupation, Raghsa has the capacity of an annual revenue of USD 32.6 million. At the current level of occupancy, the company would be able to achieve an annual flow of USD 27.8 million. These estimates do not consider either the potential sale of units or the acquisition/start of new projects.

Rental price per square meter (CBD, certified)



Source: Raghsa presentation Oct-22.

Office Rentals	2Q2023
Rentable m2	103.865
Price per m2	26,17
Max. monthly flow (millions)	2,72
Max. annual flow (millions)	32,6
Ocuppation %	85%
Rented m2	88.367
Monthly flow (millions)	2,31
Annual flow (millions)	27,8

Source: Sekoia Research based on Raghsa's financial statements.

Moreover, as it was mentioned, the company owns an important residential property in the United States. The building was acquired by Raghsa Real Estate LLC, a subsidiary of Raghsa, during the pandemic at the end of 2020. The One Union Square South was built in 1998, is located in the heart of New York, and has 239 residential units for rent. Its total rentable area is 16,165 m².

After a grace period for the tenants, the projection of revenues from One Union Square South is estimated at USD 14.7 million per year. Considering annual costs at USD 8.3 million, the property could generate an operating net income (before interests and amortization) of USD 6.4 million per year.

Investments and projects

Raghsa is currently focused on expanding its office portfolio constructing a new premium building, the Centro Empresarial Nuñez. The project will incorporate 24,000 rentable square meters in a new class A tower. Raghsa will seek to certify this property under the USGBC's Gold classification. At the average rent prices previously mentioned and in a full occupancy scenario, the building would have a potential revenue of USD 7.5 million per year.

Regarding the development progress, the excavation was finished during the last semester, the installation of the reinforced concrete structure was initiated, as well as the masonry and other complementary works. Preventively and using only the flows coming from its business, the company already stockpiled 90% of the concrete and consumed 40% of the steel needed for the project. Also, 90% of the necessary contracts were agreed upon to complete the project and 50% of the total cost of construction has been paid.

As to the other investments, Raghsa has a renowned investing tradition in the luxury housing market of Punta del Este. With a new subsidiary in Uruguay, the company will build a new residential tower called Le Park Torre IV. The tower will have 96 residential units and 60 have been sold already.

Lastly, Raghsa stated in the last financial statement its interest in investing in other real estate opportunities in New York City, either alone or in association with third parties.

Debt Profile

At the closing of the second quarter, Raghsa's net debt was USD 283.8 million. The amount is similar to the one reached in the same period of the previous year. The company continued with its prudent financial policy and funded its expansion projects with its own cash flow.

The financial debt is composed of 54.6% of international corporate bonds, 40% mortgage debt linked to the New York building, 4.6% debt guaranteed by shares of the LLC subsidiary, and 0.9% on guaranteed deposits.

Issued corporate bonds are Class 3 and 4. Class 3 matures in 2024 with a 7.25% coupon for a total amount of USD 94.9 million. Class 4 matures in 2027 and has an 8.5% coupon for a total amount of USD 60 million. Both bonds are bullets and jurisdiction is under New York law.

Furthermore, the amount of the One Union Square mortgage is USD 113.4 million. The debt has a 2.65% interest rate during the first ten years, after which it switches to a Libor-based scheme. The sink schedule payment starts on November 2023. This loan was taken in 2020, during a context of very low-interest rates, a great opportunity from which the company took advantage. It is expected that the rental cash flow from the property net of costs pay the interest of this mortgage and leave a profit margin between 2.5% and 3.5% on this asset.

The Company's cash and equivalents totaled USD 16.3 million at the last closing period. If we take into account that 58% of the cash is denominated in US dollars and the rest corresponds to peso assets, the cash and equivalents at blue-chip swap FX rate would be reduced to USD 12.6 million. The reduction would be a result of the 116% exchange rate gap between the official exchange rate and the blue-chip swap FX rate. The cash and equivalents fell by 20% in respect of the previous quarter.

Either way, during the same period, Raghsa increased considerably their financial assets. The company has USD 134.8 million invested in financial instruments, which represents a 159% increase with respect to the previous quarter and almost a triple versus the previous year. 94% of these investments are denominated in hard currency, Among the most noteworthy securities were U.S. Treasury Bonds for USD 50.9 million and USD 72.1 million in corporate bonds under NY law.

Since the mortgage is secured by the property, the lender cannot claim Raghsa's assets. For this reason, we will focus on the debt ratios without taking into account both the mortgage debt and the income flows corresponding to the NYC building.

Therefore, the total debt is USD 157.4 million, which implies USD 11.6 million in annual interest. At the same time, net financial debt is reduced to USD 10.1 million. In a moderate scenario in which Raghsa generates an annual cash flow of USD 27.8 million, it would be enough for the company to receive rents for 5 months to cover the net debt payment. This flow is also able to cover annual interests at a 2.4x ratio. Financial ratios reflect the strong financial position of the Company. Raghsa accumulated financial assets thanks to the sales of properties.

On the other hand, if we consider the mortgage debt and the estimated net cash flows from the New York units, the net debt would a total USD 136.4 million, revenues would increase to USD 34.2 million, and annual interest would increase to USD 15 million This level of net debt generates leverage of 4 times, i.e. it would take 4 years of operations to service the debt. The level of leverage is not high considering that the mortgage loan will be paid in equal annual installments from 2023 to 2050.

Argentina operations only

Debt ratios (US millions)	2Q2023	1Q2023	Var (%)	2Q2022	Var (%)
Financial Debt	157,4	152,7	3%	155,3	1%
Cash & Equivalents	12,6	15,7	-20%	15,6	-19%
Financial Assets	134,8	52,0	159%	45,3	197%
Net Debt	10,1	85,1	-88%	94,4	-89%
Annual Rentals	27,8				
Net Debt/Annual Rentals	0,4				
Annual Interest	11,6				
Annual Rentals/Interests	2,4				

Argentina and USA operations

Debt ratios (US millions)	2Q2023	1Q2023	Var (%)	2Q2022	Var (%)
Financial Debt	283,8	281,8	1%	283,1	0%
Cash & Equivalents	12,6	15,7	-20%	15,6	-19%
Financial Assets	134,8	52,0	159%	45,3	197%
Net Debt	136,4	214,2	-36%	222,2	-39%
Annual Rentals	34,2				
Net Debt/Annual Rentals	4,0				
Annual Interest	14,8				
Annual Rentals/Interests	2,3				

Source: Sekoia Research based on Raghsa's financial statements.

From a second perspective, we could compare the total market value of Raghsa's office's portfolio against the net debt, without taking into account the mortgage. In August 2022, the company reported a market value of all of its properties of USD 512.4 million, which means an average sell price of USD 4,000 per square meter.

This means that the value of the buildings represents three times the financial debt, and more than fifty times the net financial debt. In conclusion, the sale of some of the units even at a lower price would be enough to cover future debt payments.

Fixed Income

Corporate bonds trade around a 94-96% parity, with a 9.5% yield for the 2027 maturity and a 10.5% yield in the 2024 maturity. Their performance during the last year was stellar. In line with most Argentine corporate bonds, parities have not suffered the effect of the increase in the risk premium caused by the Fed's interest rate hikes. Bonds remained stable throughout 2022.

Raghsa 7,25% 2024

Source: Bloomberg

Raghsa 8,5% 2027

Source: Bloomberg

Briefly, the company manages its debt very carefully to achieve a solid financial position while investing in new developments and diversifying not only the currency but also the quality and origin of its future clients. The performance of its bonds worked as a safeguard for investors, even with capital appreciation during a volatile high-interest rate global context.

We believe Raghsa is one of the best risk/return relationships of the local hard currency issuers. In bond funds, it is one of the main issuers of our portfolios. Though like the rest of the Argentine curve, Raghsa bonds have been losing attractiveness during the last months given that other emerging markets with stronger economies have been offering nice yields. This being said, as a local issuer, it has been one of our favorites for a long time.

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