MOODY'S
INVESTORS SERVICE

Credit Opinion: Granite Real Estate Investment Trust

Global Credit Research - 10 Dec 2015

Toronto, Ontario, Canada

Ratings

Category	**Moody's Rating**
Outlook	Stable
Senior Unsecured Shelf -Dom Curr	(P)Baa2
Granite REIT Holdings Limited Partnership	
Outlook	Stable
Bkd Senior Unsecured -Dom Curr	Baa2
Bkd Subordinate Shelf -Dom Curr	(P)Baa3

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Key Indicators

Granite Real Estate Investment Trust[1]

	[2]**2015**	**2014**	[3]**2013**	**2012**	**2011**
Total Revenue [4][5]	**161**	**218**	**204**	**181**	**450**
Recurring EBITDA [4]	**135**	**183**	**173**	**153**	**133**
Recurring EBITDA %Total Revenue	**83.9%**	**83.9%**	**85.1%**	**84.2%**	**29.6%**
Total Debt / Recurring EBITDA (X)	**3.4x**	**3.2x**	**3.3x**	**1.7x**	**1.9x**
Recurring EBITDA / Fixed Charge (X)	**9.5x**	**7.5x**	**8.2x**	**9.1x**	**8.0x**
Total Assets [3][4]	**2,701**	**2,448**	**2,469**	**2,007**	**1,225**
Secured Debt % Gross Assets	**3.4%**	**2.7%**	**1.7%**	**0.0%**	**0.0%**
Total Debt + Pfd Equity % Gross Assets	**22.4%**	**23.7%**	**23.0%**	**13.1%**	**15.2%**

[1] 2011 figures contain former MEC-racing/gaming operations spun-off in 2011. [2] For the 9-month period ended September 30, 2015 [3] 1/1/13: reporting framework changed to IFRS which reflects investment properties at fair value. [4] 1/1/12: reporting changed to CAD$mil; 2011 and prior:US$mil. [5] Mexican portfolio was disposed in June 2014 and was included in revenue prior to that date.

Opinion

SUMMARY RATING RATIONALE

Granite Real Estate Investment Trust (GRT.UN:TSX; GRP.U:NYSE) is a Canadian-based REIT engaged principally in the ownership and management of predominantly industrial, warehouse and logistics net lease properties in North America and Europe. The portfolio is primarily leased to the automotive operating subsidiaries of Magna International Inc. (rated Baa1 with a positive outlook), from which Granite was spun off in 2003. Since converting to a REIT in 2013, Granite has reduced its Magna exposure from 97% to 81%, while maintaining solid financial metrics and occupancy. On June 12, 2015, Granite's board announced that it was exploring strategic alternatives to best enhance the long term interests of Granite and its stakeholders.

Credit Strengths

- Mostly unencumbered, geographically diversified portfolio with good asset quality, long-term net leases and minimal lease rollover

- Rental revenues primarily come from a strong tenant, Magna (rated Baa1 with a positive outlook) and its affiliates

Credit Challenges

- Acute tenant concentration with Magna; portfolio concentration in manufacturing and assembly plant properties

- Reliance on the health of the auto industry, which can be a cyclical business

Rating Outlook

The stable outlook reflects Moody's expectation that Granite will at least maintain its solid operational performance as a net lease company and liquidity commensurate with the rating, while continuing to acquire properties leased to non-Magna tenants to increase tenant diversification. The stable outlook also reflects Moody's expectation that Granite's management is committed to an unsecured debt capital structure and continued conservative credit metrics, despite the anticipated leverage increase.

What Could Change the Rating - Up

Rating improvement is unlikely in the intermediate term, but would be contingent upon the current management team's ability to successfully execute their strategic plan towards greater tenant diversification with Magna comprising less than 40% of Granite's annualized lease revenues, while maintaining strong credit metrics and showing other avenues of growth.

What Could Change the Rating - Down

A rating downgrade would occur should Granite experience a substantive weakening in its credit metrics likely resulting from a significant deterioration in the automotive industry that forces Magna International to close a large number of its properties leased from Granite, significant changes in growth strategy, or substantially increased leverage beyond Granite's stated range.

DETAILED RATING CONSIDERATIONS

Key factors currently influencing the ratings and outlook include:

Factor 1 - Liquidity & Funding

Trend: Neutral

Granite's debt metrics are well-situated with enough internal liquidity to cover its cash needs over the next few years. Granite's main source of liquidity is cash flows from its real estate operations, which are stable given the net lease structure. The company also has a C$250 million multicurrency revolver (82% available at 3Q15) that is mainly used for acquisitions, which matures February 2018 (with a C$50 million accordion and one-year extension option) and C$139.6 million cash on balance sheet. The next debt maturities are approximately C$18.4 million in 2016 for a construction loan and C$57.7 million in 2017 for a construction loan and mortgage. The majority (93%) of Granite's assets are unencumbered, a plus.

Factor 2 - Leverage & Capital Structure

Trend: Neutral

Granite's leverage (debt/gross assets of 22% at 3Q15) and Net debt/EBITDA (2.6x at 3Q15) are very strong. These subfactors were adjusted down in our methodology scorecard to reflect the potential for an increase in leverage to 40%-50% of total capital, per the company's announced strategic plan. However, Moody's does not expect any imminent increases to leverage unless a significant portfolio acquisition opportunity were to present itself. Granite has a secured debt/gross assets ratio of 3.4% and is expected to maintain a mostly unsecured capital strategy going forward. Granite's revenues on an annualized basis as of September 30, 2015 were approximately 45% Euro, 29% Canadian, and 25% US dollar.

Factor 3 - Market Position & Asset Quality

Trend: Neutral

Granite has a strong franchise in owning and operating over 95 properties located in eight countries. Granite has approximately 30 million square feet of leaseable area in the core real estate business, which is concentrated in terms of property type -- a credit challenge, with approximately 99% (based on square footage) manufacturing plants and warehouses, and 1% office buildings. Another credit challenge is Granite's acute concentration with Magna, as well as its reliance on the health of the auto industry, which is a cyclical business. Approximately 75% of the portfolio is comprised of properties strategically located and used by Magna to provide automotive parts and modules to the world's manufacturers of cars and light trucks for their assembly plants throughout North America and Europe. However, the Magna concentration has decreased to 81% of Granite's annualized lease payments from 97% due to leases with new non-Magna tenants executed over the past two years. On a fair value basis at 3Q15, the properties are distributed in Canada (26%), Austria (29%), USA (28%), Germany (11%), Netherlands (5%), and other countries (1%). The portfolio also includes corporate offices, product development, and engineering centers and test facilities, including the head offices of Magna in Canada, as well as Cardinal Health's Canadian operations. The total amount of development and redevelopment has historically been low and Moody's anticipates it remaining minimal in the intermediate term. The weighted average lease term by square footage was 4.7 years at 3Q15.

Factor 4 - Cash Flow & Earnings

Trend: Neutral

Fixed charge coverage is very strong at 9.5x at 3Q15; this sub-factor has been adjusted to reflect the previously mentioned potential leverage increase. Granite's joint venture partnership with Dermody Properties for the acquisition and development of land and income-producing properties in the U.S. includes Granite's ownership of these assets at 90% or above, so the JV is fully consolidated in the company's financials. The EBITDA/Revenues ratio is a solid 84%, and reflects the consistency of the net lease contract structure.

Key Covenants

The 2013 and 2014 debentures include the following covenants: 1. Consolidated EBITDA (Granite REIT and Granite GP) to Consolidated interest expense ratio not less than 1.65; 2. Consolidated Indebtedness not more than 60%; 3. Unencumbered Aggregate Assets (Granite REIT and Granite GP)/consolidated unsecured debt of 150% or more.

Rating Factors

Granite Real Estate Investment Trust
806939637

Rating Drivers [1]	**Aa**	**A**	**Baa**	**Ba**	**B**	**Caa**	**Ca**	**Implied Score**	**Adjusted Score**	**Trend**
Liquidity & Funding								Low A	Low A	Neutral
Liquidity Coverage			Good							
Upcoming Debt Maturities		18.3%								
FFO Payout			68.3%							
Amount of Unencumbered Assets		92.8%								
Leverage & Capital Structure								Mid A	Mid Baa	Neutral
Debt + Preferred/Gross Assets		22.4%								
Net Debt/EBITDA	2.6x									
Secured Debt/Gross Assets		3.4%								
Access to Capital			Good							
Market Positioning & Asset Quality								Mid Ba	Mid Ba	Neutral
Franchise/ Brand Name			Good							

Gross Assets			$2.7							
Diversity-location/tenant/industry/economic							N/A			
Development % Gross Assets										
Asset Quality			Good							
Cash Flow & Earnings								Mid Aa	Mid A	Neutral
EBITDA/Revenues	83.9%									
EBITDA Margin Volatility		1.67%								
Fixed Charge Coverage	9.5x									
JV/Fund Business % Revenues										
Overall Assessment										
Implied Score								Low A		
Adjusted Score									High Baa	

[1] Data as of September 30, 2015

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