Impact Healthcare REIT

Q123 results

Making hay in all weathers

Real estate

In Q123, Impact Healthcare REIT built on its strong FY22 underlying income performance. It also benefited from a stabilisation of the portfolio valuation yield, allowing indexed rental growth to feed through to property values and NAV. In this note we focus on the drivers of Impact's consistently positive financial and operational performance.

Year end	Net rental income (£m)	EPRA earnings* (£m)	EPRA EPS* (p)	EPRA NTA/ share (p)	DPS (p)	P/NAV (x)**	Yield (%)**
12/21	36.5	27.4	8.1	112.4	6.41	0.86	6.6
12/22	45.4	32.6	8.4	110.1	6.54	0.88	6.7
12/23e	53.1	35.2	8.5	111.5	6.77	0.87	7.0
12/24e	55.5	36.5	8.8	114.6	6.96	0.85	7.2

Note: *EPRA earnings exclude fair value movements on properties and interest rate derivatives. **P/NAV and yield are based on the current share price.

Strong financial and operational performance

Rental income and cash flow are growing strongly, supporting dividend growth and a high level of cover (128% on an EPRA basis and 109% on an adjusted 'cash' basis in FY22). We forecast that the FY23 targeted DPS of 6.77p (+3.5%) will be similarly well covered. With yields stabilising, in Q123 the portfolio value increased c £9m on a like-for-like basis versus a c £21m decline in Q423. Q1 NAV increased 2.2% to 112.6p and the NAV total return was 3.7%. For tenants, fee growth and improved occupancy are an offset to inflationary pressures, and rent cover remains strong at c 1.8x. For the first time, rent collection dipped in Q123 (to 98%), but we do not believe that the single tenant in arrears is indicative of wider tenant stress. Taking account of the FY22 results and the Q123 update, we have made only modest, positive changes to our adjusted earnings and NAV forecasts.

Building on a structurally supported market

Impact's DPS has increased each year since listing in 2017, driving consistently positive accounting returns, averaging 7.1% pa. Providing a strong tailwind, it operates in a structurally supported market, where care demand is driven by the demographics of a growing elderly population rather than the economy. Homes with the quality to meet this demand sustainably are in short supply. That said, the sector is not without challenges for operators (eg the pandemic, strongly rising inflation) and in this context Impact's strong financial and operational performance is no accident but reflects the robustness of its strategy. As we discuss in detail, at the core of its strategy is the identification of suitable assets that can be let to selected tenant partners, at sustainable rents, consistent with their maintaining a high level of care while providing a good level of rent cover and meeting Impact's financial investment criteria. This has consistently delivered gross acquisition yields of c 7%.

Valuation: Income-driven, long-term returns

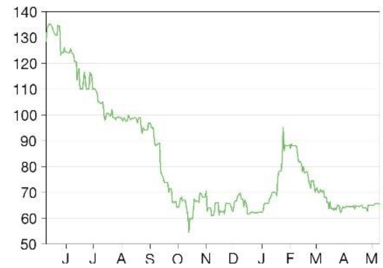
The FY23 DPS target represents an attractive yield of 7.0%, which we expect to again be fully covered by adjusted 'cash' earnings. Meanwhile, the shares trade at a 13% discount to Q123 NAV per share.

10 May 2023

Price	**97p**
Market cap	**£402m**

Gross debt at 31 March 2023	£187.3m
Gross LTV at 31 March 2023	28.3%
Shares in issue	414.4m
Free float	90%
Code	IHR
Primary exchange	LSE
Secondary exchange	N/A

Share price performance



%	1m	3m	12m
Abs	0.7	(5.3)	(21.3)
Rel (local)	0.1	(3.0)	(25.9)
52-week high/low		127p	90p

Business description

Impact Healthcare REIT, traded on the Main Market of the London Stock Exchange, invests in a diversified portfolio of UK healthcare assets, primarily residential and nursing care homes, let on long leases to high-quality operators. It aims to provide shareholders with attractive and sustainable returns, primarily in the form of dividends, underpinned by structural growth in demand for care.

Next events

H123-end	30 June 2023

Analyst

Martyn King +44 (0)20 3077 5700

financials@edisongroup.com

Edison profile page

Making hay in all weathers

The healthcare real estate sector has historically proved resilient in challenging environments, and continues to benefit from a strong demographic tailwind, largely independent of the wider economy. Within this, the care home market is large and fragmented, with a strong growth outlook. The UK population is ageing rapidly, and those aged 85 or over are the fastest growing group, forecast to increase 60% by 2036. The sector provides a substantially non-discretionary, essential service, yet the number of beds has shown no material growth over the past 10 years, with newly developed and refurbished stock offset by the withdrawal of older, obsolete homes. That said, the sector is not without challenges for operators, Impact's tenants. Most recently, the pandemic significantly reduced occupancy levels, and this was followed by the sharp acceleration of inflation in the second half of 2022. In this context, Impact's strong financial performance and its ability to deliver progressive, fully covered dividends is no accident but reflects the robustness of the particular strategy that it has adopted and successfully implemented. We cover the recent financial performance later in this note but first focus on its foundations, reviewing the key elements of that strategy and how it is reflected in tenant performance.

Exhibit 1: Progressive dividends and consistently positive NAV total return since listing in March 2017

Pence per share unless stated otherwise	2017*	2018	2019	2020	2021	2022	Q123	FY17–Q123
Opening NAV	97.9	100.6	103.2	106.8	109.6	112.4	110.2	97.9
Closing NAV	100.6	103.2	106.8	109.6	112.4	110.2	112.6	112.6
Dividends paid	3.0	6.0	6.1	6.3	6.4	6.5	1.6	35.9
NAV total return	**7.2%**	**8.5%**	**9.5%**	**8.5%**	**8.4%**	**3.8%**	**3.7%**	**51.7%**
Of which dividends	3.1%	6.0%	5.9%	5.9%	5.8%	5.8%	1.5%	36.7%
Of which capital growth	2.8%	2.5%	3.5%	2.6%	2.6%	-2.0%	2.2%	15.0%
Average annualised return								**7.1%**

Source: Impact healthcare data, Edison Investment Research. Note: *Annualised returns from listing in March 2017.

The strategic foundations to performance

At the core of strategy has been a disciplined approach to acquisitions and careful tenant selection. The portfolio has been built by acquisition, typically of portfolios of assets, at consistently high gross yields of c 7%, providing a strong level of cash flow. Acquisition yields have been maintained despite a general tightening across the sector over the same period. However, the investment manager is keen to stress that while yield is an important factor, it is an 'output' from the asset selection process rather than the 'input' from which decisions flow. The selection process starts with an identification of suitable assets to be let to selected tenants, typically mid-sized operators, with an established track record of financial and operational performance. It is then necessary to establish whether rents can be set at a level that is sustainable to tenants, consistent with their maintaining a high level of care while providing a good level of rent cover[1] and meeting Impact's financial investment criteria. Typically, Impact has acquired assets with the following characteristics:

- Standing assets with a consistently positive trading history and a good reputation in the local markets in which they operate.
- Rent cover at acquisition of around 2x.

[1] Rent cover is a key metric used by Impact in monitoring and assessing the ability of individual homes and operators to support the rents that it expects from its portfolio sustainably. The ratio tracks home-level earnings before interest, tax, depreciation, amortisation, rent and group management overheads (EBITDARM), or operational cash earnings, on a rolling 12-month basis divided by rents over the same period. It excludes 'turnaround' and 'immature' homes. Immature homes are defined as homes that are newly opened or are undergoing major capital improvement requiring partial closure. The rent cover calculation excludes eight properties that are defined as turnaround or immature.

- Portfolios, which provide a two-fold pricing advantage. The first is a straightforward reduction in acquisition costs if structured as a 'corporate acquisition' rather than an 'asset transaction' (to c 1.5% rather than c 6.5%). More importantly, it can be possible to agree a more attractive acquisition price in return for providing the vendor with a clean exit.
- Acquisitions that provide asset management opportunities, working in partnership with tenants to enhance homes, making them more operationally and environmentally efficient, more attractive to current and prospective residents, and generating an attractive unlevered yield on costs (of at least 8%).
- Selected forward funding opportunities, in partnership with existing, established tenant operators, providing access to high-quality homes on a low-risk, pre-let, fixed-cost basis.

The following examples reflect this process:

- **Corporate acquisition of a six-home portfolio with attractive rent cover and high initial yield.** In January 2023, Impact invested in six care homes in Shropshire and Cheshire where the family owner/operator (Morris Care) was seeking to exit and retire. Each of the homes has an established track record of delivering strong operational performance and strong environmental credentials (four are EPC rated B and two are rated C, with outline strategies in place for achieving an EPC rating of B). Morris Care enjoys a strong local reputation for delivering high acuity care and has established good working relationships with the local NHS clinical commissioning groups. The vendors have granted a licence for the homes to continue to trade under the Morris Care brand for three years and the operational management team of Morris Care has transferred to Welford Healthcare, an existing Impact tenant, which will operate the homes.[2] It has initially been funded by way of a loan to Welford, allowing it to take immediate operational control of the homes, avoiding a potentially lengthy transition period while regulatory approvals are sought to register the operation of the homes in new legal entities. Once this is received, Impact has the option to acquire the company that owns the properties from Welford[3] and meanwhile receives loan interest of 8.4% pa. When either option is exercised, new 35-year leases on Impact's standard terms, which have been pre-agreed with Welford, will come into effect. As a corporate transaction, costs are low. The rent under the new leases has initially been set at £3.9m, representing rent cover of more than 2x and reflecting a gross initial yield of 7.0%.
- **The enhancement and repositioning of Fairview demonstrates the benefits of asset management for tenants, residents and staff.** In 2018, Impact acquired two adjacent homes (Fairview Court and Fairview House) at Fairview in Bristol. Fairview Court was built by the vendors in 2006 with 49 single bedrooms, all of which are ensuite, providing nursing with dementia care. Fairview House is a 22-bed unit in a period building, providing residential care. Although planning permission was in place to extend Fairview House and to link the homes, Impact believed the plans were sub-optimal and decided on revisions. Work commenced in 2022, completing the construction of the new-build 'link block' bringing the two homes together. A second phase of the project is now underway and expected to be completed by the end of 2023. This involves a comprehensive upgrade of Fairview House, adding ensuites to bedrooms, improving the residents' day spaces and increasing energy efficiency, so the new combined building will have an EPC rating of A. The homes were acquired for £4.9m, with the £356k of annual rent reflecting a gross initial yield of 7.3%. The developments represent a further investment of £3.5m, bringing the total to £8.4m. Including rent increases since acquisition and rentalisation of the capex at 8.6%, contracted rent at completion will be c £700k. In combination with the enhanced quality of the asset, this indicates strong potential

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2 This allows Impact to expand its relationship with Welford, which now operates 18 of its homes.

3 Welford also has the option to sell the entire issued share capital of the company to Impact to repay the loan.

for valuation uplift. The investment manager anticipates this may be reflected in an independent valuation some 30–40% above the investment cost, or a gross yield of 6.0–6.5%. Even at the portfolio average yield, a conservative and unlikely outcome, an uplift of c 20% is indicated.

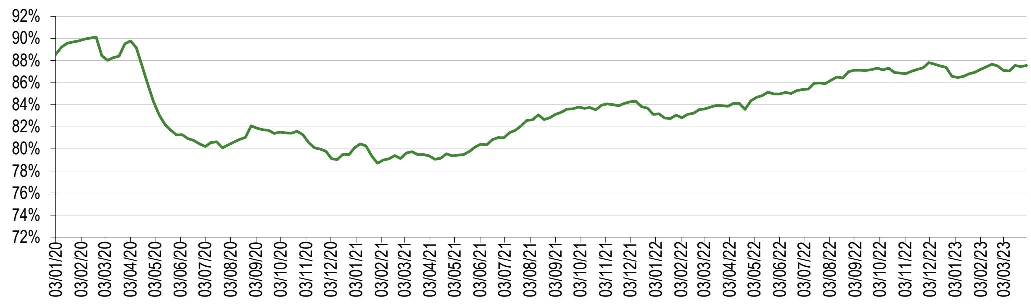
Notable previously completed projects were at Diamond House, Leicester and Freeland House, Oxfordshire. At both, new specialist dementia care facilities were developed within the footprint of the existing homes, offering specialist care and support to existing residents of the homes who may develop dementia symptoms and providing places for 76 new residents with dementia needs.

- **Developments.** During H122, Impact reached practical completion of its first forward-funded development scheme, a high-quality, 94-bed home in Hartlepool, which is being run by existing tenant Prestige. The home is now in the occupancy build-up phase, which Impact says is proceeding in line with the tenant's plan. Impact provided £6.1m to fund the development, achieving a yield on cost of 7.8%. A £1.9m valuation uplift at completion represented a 30% profit on cost. The company has also committed to fund a new development and 80-bed home in Norwich, which it believes will be the best home of its type in the area, to be operated by existing tenant Carlton Hall. The home will form part of a care village, along the same lines as another successful development undertaken by Carlton Hall in Lowestoft. We expect Impact to provide c £10.5m in funding with an initial gross yield on cost of 7.1%. Deferred payments of up to £4m may become payable based on the trading performance of the new home at maturity in exchange for an annual rent increase of up to £246k (6.2%), so long as rent cover remains in excess of 2x.

Tenant resilience

Despite a significant reduction in occupancy through the pandemic, from a typical c 90% to a low of 79% in early 2021, tenant performance remained robust. A good level of rent cover was maintained and rents were collected in full without contract variation, as had been the case since Impact listed in 2017. In part, this robust performance through the pandemic was assisted by government grant funding for what was recognised as a critically important sector, but also significantly reflected tenant operational efficiency, Impact's close relationship with, and monitoring, of them and, perhaps most importantly, affordable rents.

Exhibit 2: Average adjusted tenant occupancy {model/charts & tables/line 578}

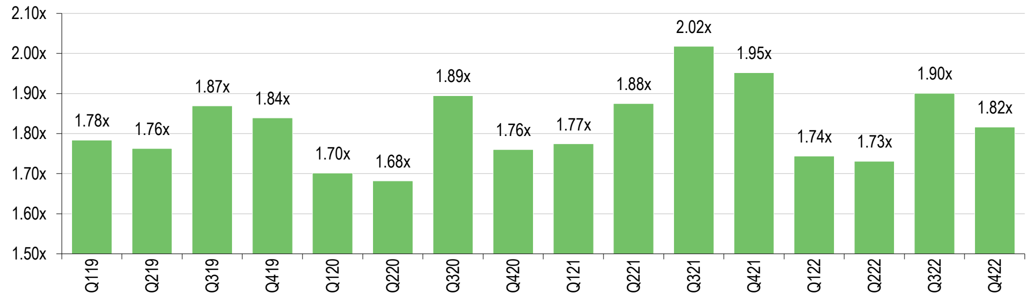


Source: Impact Healthcare REIT

As occupancy began to rebuild, home-level profitability and rent cover both returned to 'normal' levels, despite the phased withdrawal of government pandemic support at the end of Q122.

As the pandemic became more manageable, the very rapid acceleration of inflation in the second half of 2022 provided a new challenge to the sector. With profitability having recovered from the pandemic, Impact's tenants entered this inflationary environment in a generally strong financial position. Strong fee growth and a continued increase in occupancy have thus far offset staffing and other cost pressures and rent cover has remained stable (1.8x at end-FY22).

Exhibit 3: Impact 2-month trailing rent cover {model/charts & tables/line 555}



Source: Impact Healthcare REIT

The key factors that contribute to the inflation resilience of tenants include:

- Occupancy increased to 86.6% at end FY22 and, after a pause during the winter months, increased to 87.6% at end Q123. The demand for care home places is effectively non-discretionary, at least for anything other than short periods, and is still a little below the pre-pandemic level of c 90%.
- Operators continue to pass through cost pressures in fee increases. UK care operators have a track record of being able to pass through inflationary pressures in fee increases. Between 1998 and 2020, weekly fees grew by an average of 3.8% pa for nursing care and 3.6% for residential care, a premium of c 1% pa over average annual growth in RPI of 2.8%.[4] Based on the detailed home-level reporting that Impact receives from its tenant operators, the average increase in weekly fees charged by operators of Impact homes in FY22 was 12.6%. Despite the high level of fee increases, operators report widespread acceptance by or on behalf of residents that this is necessary to maintain the level of care. For the current year, the company expects an acceleration in local authority fee growth,[5] c 60% of tenant income (with the balance split c 32% private pay and 8% NHS).
- For Impact, all rents are linked to inflation[6] (98% to RPI and 2% to CPI) – although rent uplifts are typically capped at c 4% with a floor of c 2%[7] – and although this means that while RPI inflation is above 4%, rental growth will lag in real terms, it contributes towards rents remaining affordable for tenant operators and enhances the security of Impact's income.
- Staffing is the key cost across the sector (an average c 60–65% of revenues for Impact's tenants). Although typically milder, the Omicron wave continued to affect staff availability during 2022, exacerbated by some leaving the sector. Staffing pressures resulted in a spike in the use of more expensive agency cover, which is now showing signs of improvement. Impact notes the positive effect of the government's temporary relaxation of the immigration rules in respect of skilled labour.
- Other cost increases are manageable. Based on tenant data, despite very strong increases, food costs as a percentage of home revenues have remained at c 4%, similar to the relatively stable five-year average. Utility costs rose sharply in Q422, increasing the share of revenues to around one percentage point above the five-year average of 2.3%, but are now reducing.

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4 Impact Healthcare REIT.

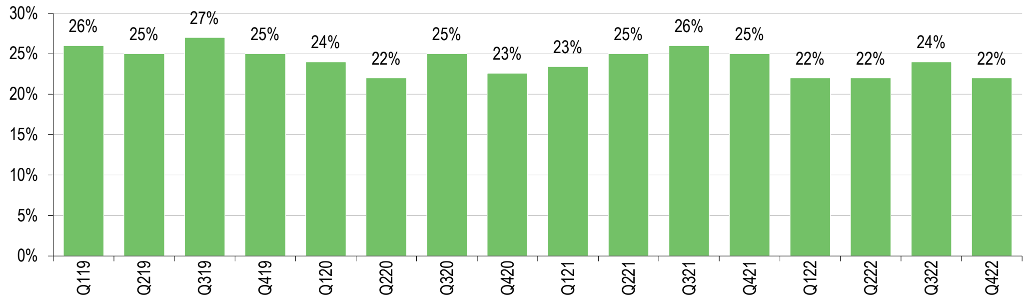
5 Local authority fees are reviewed in April and, at the time of reporting FY22 results, Impact was in receipt of around one-third of settlements.

6 As measured by the Retail Price Index (RPI) and Consumer Price Index (CPI).

7 90% of leases are RPI linked with an annual floor at 2% and cap at 4%; 8% are RPI-linked with an annual floor at 1% and cap at 5%; 2% increase in line with CPI.

Exhibit 4 shows the trend in average home-level EBITDARM margins, which remain healthy and show only a mild weakening since before the pandemic. It is worth noting the element of seasonality driven mainly by annual pay increases falling in January/April, while local authority fee increases in April have a more material impact in Q3.

Exhibit 4: Home-level tenant average EBITDARM margin*



Source: Impact Healthcare REIT. Note: *Earnings before interest, tax, depreciation, amortisation, rent and group management charges.

One tenant is under-performing in early FY23

During 2022, Impact's strong track record of collecting 100% of rents due with contract variation continued. However, one of the 13 care home tenants[8] failed to pay the quarter's rent that was due in advance on 1 January 2023. The core problem relates to a small number of homes, operated by the tenant, which were acquired by Impact in the first quarter of 2020 as a turnaround project, atypical of Impact's acquisition policy. The turnaround was significantly delayed by the pandemic that ensued and this remains the case. Impact says it remains confident in the quality of the buildings and their ability to deliver good-quality care and believes that the rents are set at a level that is affordable. The average rent per bed charged by Impact for these homes is c £4,000 pa, compared with a portfolio average that is c 50% higher and is supported by the average rent cover of 1.8x.

For Q123, Impact has received 98% of all rents due (£9.6m). Rent collection includes a £0.2m utilisation of rent deposits, offsetting half the £0.4m quarterly rent due from the under-performing tenant. Within the quarterly update we understand that the outstanding £0.2m has been provided to ensure that earnings are not overstated, while the investment manager remains in active discussions with the tenant and is hopeful of reaching a resolution by the middle of the year.

No material changes in forecasts for fully covered DPS growth

Taking account of the FY22 results and the Q123 update, we have made only modest changes to our forecasts, with slight increases in adjusted earnings, dividend cover and NAV per share.

[8] Impact has 14 tenants including the NHS, which leases two health facilities.

Exhibit 5: Forecast summary

£m unless stated otherwise	Reported	New forecast		Previous forecast			FY22 forecast vs actual	Forecast change			
	FY22	FY23e	FY24e	FY22e	FY23e	FY24e	FY22	FY23e	FY24e	FY23e	FY24e
Cash rental income	35.9	39.8	41.4	35.8	39.4	40.3	0.0	0.5	1.1		
Interest from loan investments	3.2	6.1	6.5	3.2	6.1	6.5	0.0	0.0	0.0		
Net revenue	39.1	45.9	47.9	39.0	45.4	46.8	0.0	0.5	1.1	1%	2%
Net finance costs	(4.6)	(8.7)	(9.5)	(4.5)	(8.5)	(8.3)	(0.1)	(0.1)	(1.2)		
Administrative costs	(7.0)	(8.1)	(8.3)	(7.1)	(8.1)	(8.4)	0.1	0.1	0.1		
Other	0.2	0.0	0.0	0.2	0.0	0.0	0.1	0.0	0.0		
Adjusted earnings	27.7	29.1	30.1	27.7	28.7	30.2	0.1	0.4	(0.0)	1%	0%
IFRS adjustments	6.5	7.3	7.6	6.6	7.4	7.7	(0.2)	(0.2)	(0.1)		
Loan fee amortisation	(1.2)	(1.2)	(1.2)	(1.3)	(1.2)	(1.2)	0.1	0.0	0.0		
Other	(0.4)	0.0	0.0	(0.1)	0.0	0.0	(0.3)	0.0	0.0		
EPRA earnings	32.6	35.2	36.5	32.8	35.0	36.7	(0.3)	0.2	(0.1)	1%	0%
EPRA EPS (p)	8.4	8.5	8.8	8.4	8.4	8.8	(0.0)	0.1	(0.0)	1%	0%
Adjusted EPS (p)	7.1	7.0	7.3	7.1	6.9	7.3	0.0	0.1	(0.0)	1%	0%
DPS declared (p)	6.5	6.8	7.0	6.5	6.8	7.0	0.0	0.0	0.0	0%	0%
EPRA DPS cover	128%	126%	127%	128%	125%	127%					
Adjusted DPS cover	109%	104%	105%	108%	103%	105%					
EPRA NTA per share ('NAV') (p)	110.1	111.5	114.6	110.1	109.5	113.0		2.0	1.6	2%	1%
NAV total return	3.8%	7.6%	8.7%	3.7%	5.7%	9.3%					

Source: Edison Investment Research

We have not assumed any additional transaction activity although, as the portfolio acquisition in January demonstrated, despite the increased cost of capital, selective, accretive transactions remain possible (see below).

Well positioned to manage the impact of rising interest rates and resources available for selective acquisitions

End-Q123 debt drawn was £187.3m and the gross LTV was 28.3% (end FY22: £142.3m and 23.9%). LTV is a little above the company's medium-term target of 25% but well below the 35% maximum specified by its gearing policy. Impact's policy is to have at least 75% of the cost of drawn debt fixed or hedged and, including additional hedging undertaken during the period, the proportion was 80% at end Q123, with a blended cost of 4.3%. A £25m interest rate swap at 1%[9] will mature in June and we expect Impact to take further measures to increase the hedging rate, from an adjusted c 67%, in line with policy.

Allowing for the January transaction and all other capital commitments, at the end of FY22 Impact had available liquidity of c £63m. However, given the continuing volatility in debt markets, we expect the company to remain cautious and highly selective in pursuing acquisitions. Funding of the January transaction was innovative, combining attractively priced new equity with new borrowing at a hedged cost. We estimate an immediate positive earnings impact and for this contribution to increase with RPI-linked rental growth (capped at 4.0%). Of the £56m consideration, £44.8m (or 80%) was in cash, funded by newly drawn debt, with the balance in new shares issued to the vendors and priced at 116.62p per share, the Q322 NAV, a significant premium to the current price. The debt drawn has been hedged through a new £50m interest rate cap at a cost of £1.5m, which caps SONIA at 3.0% for two years.

9 The SONIA rate paid is limited to 1%.

Exhibit 6: Available cash resources (end FY22, adjusted for January portfolio investment)

	£m
Cash at end FY22	22.5
Available debt	98.7
January 2023 acquisition	(44.8)
Capital commitments	(9.2)
Deferred payments	(4.6)
Liquidity headroom	62.6

Source: Impact Healthcare REIT

Capital values appear to be stabilising

Healthcare property has not been immune to property yield widening (valuation decline) across the UK commercial property sector, particularly in the final quarter of 2022. Likewise, Impact's portfolio has demonstrated resilience, confirmed by the Q123 update.

For FY22, the valuation loss was £9.9m, with the positive impact of rent uplifts (£22.1m) more than offset by the negative impact of yield widening (£32.0m). The EPRA-topped up net initial yields increased from 6.71% to 6.98%. In Q422 alone, there was a negative net valuation movement of £21.6m with a 6.98% yield increasing from 6.68%.

Q123 showed significant stabilisation, with EPRA-topped up net initial yield showing no material change (6.99%) and c £9.1m in positive revaluation movements, driven by like-for-like rent growth.

With inflation remaining stubbornly high and debt markets remaining volatile, it may be too early to call a turning point in valuations, but we expect the resilience of sector valuations to continue. Our valuation forecast is increased slightly but continues to reflect yield widening for the year of c 10bp.

Valuation

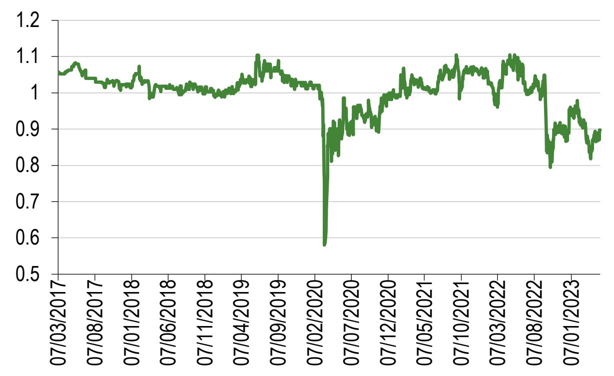
For FY23, Impact is targeting a DPS of 6.77p (+3.5%), fully covered by adjusted 'cash' earnings. This represents an attractive yield of 7.0%. Meanwhile the shares trade at c 0.9x Q323 EPRA NTA (NAV) per share of 112.6p. The discount to NAV appears to anticipate some modest further weakening of property valuations, although this was not evident during Q123.

Leaving aside the pandemic period, Impact's share price has not fully kept pace with dividend growth and its dividend yield has trended upwards. It is at the upper end of its historical range (excluding the peak of pandemic uncertainty) and above the average c 5.7% since listing. While rising interest rates will have contributed to a widening dividend yield, we would argue that the maturing of the care home investment sector and Impact's robust performance through the pandemic are both positive offsetting factors.

Exhibit 7: Dividend yield since listing

Source: Company DPS data, Refinitiv prices

Exhibit 8: P/NAV since listing



Source: Company NAV data, Refinitiv prices

Exhibit 9 shows a summary of the performance and valuation of a group of real estate investment trusts (REITs) that we consider to be Impact's closest peers within the broad and diverse commercial property sector. The group is invested in the primary healthcare, supported housing and care home sectors, all targeting stable, long-term income growth derived from long lease exposures. For consistency, NAV and DPS data are presented on a trailing basis[10] and do not reflect Impact's increased FY23 DPS target.

Exhibit 9: Peer group comparison

	WAULT* (years)	Price (p)	Market cap (£m)	P/NTA** (x)	Yield*** (%)	Share price performance			
						1 month	3 months	1 year	3 years
Assura	12	50	1488	0.83	6.1	-2%	-6%	-22%	-36%
Civitas Social Housing	22	80	486	0.72	7.1	43%	30%	-4%	-18%
Primary Health Properties	12	104	1393	0.93	6.3	0%	-6%	-25%	-34%
Target Healthcare****	27	76	468	0.73	8.7	0%	-6%	-31%	-27%
Triple Point Social Housing	26	53	212	0.49	10.3	8%	-2%	-41%	-44%
Average	20			0.74	7.7	10%	2%	-25%	-32%
Impact Healthcare	20	97	400	0.87	6.8	1%	-5%	-21%	3%
UK property index		1,314				0%	-8%	-22%	-8%
UK All-Share Index		4,231				1%	-2%	6%	29%

Source: Historical company data, Refinitiv. Note: *Weighted average unexpired lease term. **Based on last published EPRA NTA/NAV per share. ***Based on trailing 12-month DPS declared (except for Target). ****Based on the H223 target yield, annualised. Refinitiv price data at 9 May 2023.

Impact's shares have outperformed the peer group and tracked the broader UK property sector over the past year and have substantially outperformed the peer group over three years, and have tracked the broad UK property sector. As a result, Impact's trailing yield is now below the average of the peer group but remains above that of the primary healthcare REITs. Although the latter have the benefit of government-backed rents (c 90% paid directly by government or indirectly through GPs), they have significant exposure to open market rent reviews. Although these are accelerating, we do not expect rent growth to reach 4% in the near term (the average level at which Impact's indexed rents are capped).

Details of FY22 financial performance

We have referred to Q123 financial performance throughout this note, which built on the strong FY22 underlying income performance and benefited from the stabilisation of the portfolio valuation yield, in contrast to the c 40bp widening in Q422. In Exhibit 10, we present the results on an adjusted earnings basis with a reconciliation to EPRA earnings and IFRS earnings.

[10] Target Healthcare's yield reflects its quarterly dividend rebasing, effective Q323, to 1.4p per share or 5.6p on an annualised basis.

Exhibit 10: Summary of FY22 financial performance

£m unless stated otherwise	FY22	FY21	FY22/FY21
Cash rental income	35.9	30.5	18%
Interest income from loaned portfolio investments	3.2	0.1	
Total adjusted income	**39.1**	**30.5**	**28%**
Administrative and other expenses	(6.9)	(5.8)	20%
Gain on disposal	0.1	0.3	
Net finance expense	(4.6)	(2.4)	92%
Adjusted earnings	**27.7**	**22.7**	22%
IFRS rent smoothing & lease incentive adjustments	6.4	5.9	
Gain on disposal	(0.1)	(0.3)	
Amortisation of loan arrangement fees	(1.2)	(1.0)	
Non-recurring due diligence costs	(0.1)	0.0	
EPRA earnings	**32.6**	**27.4**	19%
Change in fair value of investment properties	(14.3)	4.5	
Change in fair value of call option	(1.8)	0.0	
Change in fair value of interest rate derivative	0.4	0.1	
IFRS earnings	**16.9**	**32.0**	-47%
Closing number of shares in issue (m)	404.8	350.6	15%
Average number of shares (m)	390.1	339.8	15%
IFRS EPS (p)	4.33	9.41	
EPRA EPS (p)	8.37	8.05	4%
Adjusted EPS (p)	**7.11**	**6.68**	6%
DPS declared (p)	**6.54**	**6.41**	2%
DPS cover (EPRA earnings)	128%	126%	
DPS cover (adjusted earnings)	**109%**	**104%**	
EPRA cost ratio	16.6%	15.8%	
Gross debt	142.3	114.5	
Gross LTV	23.8%	22.3%	
EPRA NTA per share	110.1	112.4	-2%
EPRA NTA total return	3.8%	8.4%	

Source: Impact Healthcare REIT data

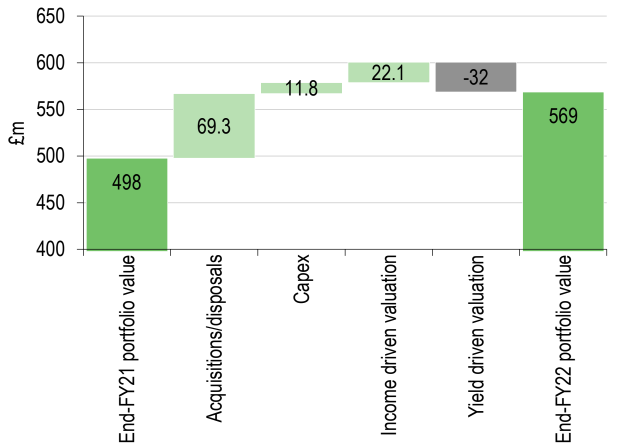
In particular we note:

- An increase in annualised contracted rent roll to £43.1m pa at end FY22, up 14% or £5.2m versus end-FY21. Growth continues to be driven by acquisitions and indexed rent growth. During Q123, rent roll increased by a further 11% to £47.9m pa with the £56m investment in six care homes via a loan adding £3.9m, and completed rent reviews at an average uplift of 4.0% adding £0.8m.
- Cash rental income increased 18% to £35.9m and, including £3.2m of interest income earned on loan investments, total adjusted income (excluding IFRS smoothing adjustments) increased by 28%.
- During the year, rents were collected in full, without contract variation. In Q123, one tenant failed to pay rent due, as discussed above.
- Recurring administrative expenses increased by 20% to £6.9m, reflecting the growth of the business and inflationary effects. Within this, management fees, directly linked to NAV, increased by 19% to £4.6m.
- Adjusted to include interest received on investments via loans, in our view providing a clearer view of economic performance, the FY22 cost ratio was 15.4% versus 15.8% in FY21. On an EPRA basis (which excludes loan interest), the cost ratio was 16.6% versus 15.8%.
- The increase in net finance expense from £2.4m to £4.6m reflected higher average borrowings, drawn to fund portfolio growth, and an increase in the average cost of drawn debt to 3.6% from 2.9%.
- Adjusted ‘cash’ earnings (before non-cash IFRS accounting and the amortisation of loan arrangement fees) increased by 22% to £27.7m and, allowing for a higher average number of shares in issue, adjusted EPS increased 6% to 7.11p. Including the non-cash IFRS rental

adjustments and loan fee amortisation, EPRA EPS earnings increased 19% to £32.6m and EPRA EPS by 4% to 8.37p.

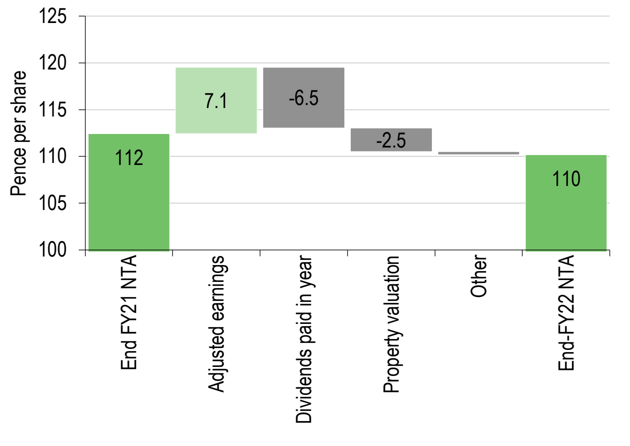
- Aggregate quarterly DPS of 6.54p was 109% covered by adjusted earnings and 128% covered by EPRA earnings.
- During the period, the portfolio value increased to £569m from £498m, driven by acquisitions. On a like-for-like basis, the valuation decreased by 5.5% (2.5p per share), with yield widening of 7.3% (40bp or 8.2p per share) partly offset by indexed rent uplifts (5.7p per share).
- End-FY22 EPRA NTA per share of 110.1p was 2% lower (FY21: 112.4p) and, adjusting for DPS paid (but not reinvested), NAV/accounting total return was a positive 3.8%.

Exhibit 11: FY22 change in portfolio value (£m)



Source: Impact Healthcare REIT data

Exhibit 12: FY22 change in NTA* (pence per share)



Source: Impact Healthcare REIT data. Note: *Net tangible assets.

Exhibit 13: Financial summary

Year to 31 December (£m)	2019	2020	2021	2022	2023e	2024e
Cash rental income	19.1	25.9	30.5	35.9	39.8	41.4
Interest income from loaned portfolio investments	0.0	0.0	0.1	3.2	6.1	6.5
Rental income arising from recognising rental premiums, fixed rent uplifts & lease incentives	4.9	4.9	5.9	6.4	7.3	7.6
Net rental income	24.0	30.8	36.5	45.4	53.1	55.5
Administrative & other expenses	(4.6)	(5.3)	(5.8)	(7.0)	(8.1)	(8.3)
Realised gain on disposal	0.0	0.2	0.3	0.1	0.0	0.0
Operating profit before change in fair value of investment properties	19.4	25.7	31.0	38.6	45.1	47.2
Unrealised change in fair value of investment properties	9.1	5.6	4.2	(14.5)	(0.5)	4.7
Change in fair value of loan asset call option				(1.8)	0.0	0.0
Operating profit	28.5	31.3	35.2	22.3	44.6	51.9
Net finance cost	(2.1)	(2.5)	(3.3)	(5.4)	(10.6)	(11.5)
Profit before taxation	26.3	28.8	32.0	16.9	33.9	40.5
Tax	0.0	0.0	0.0	0.0	0.0	0.0
Profit for the year (IFRS)	26.3	28.8	32.0	16.9	33.9	40.5
Adjust for:						
Change in fair value of investment properties Including loan assets)	(9.1)	(5.6)	(4.2)	16.3	0.5	(4.7)
Gain on disposal	0.0	(0.2)	(0.3)	(0.1)	0.0	0.0
Change in fair value of interest rate derivatives	0.4	0.1	(0.1)	(0.4)	0.8	0.8
EPRA earnings	17.6	23.1	27.4	32.6	35.2	36.5
Rental income arising from recognising rental premiums & fixed rent uplifts	(4.9)	(4.9)	(6.0)	(6.5)	(7.3)	(7.6)
Amortisation of loan arrangement fees	0.4	0.7	1.0	1.2	1.2	1.2
Amortisation of lease incentive			0.1	0.1	0.0	0.0
Non-recurring costs	0.2	0.0	0.0	0.1	0.0	0.0
Gain on disposal	0.0	0.2	0.3	0.1	0.0	0.0
Adjusted earnings	13.4	19.1	22.7	27.7	29.1	30.1
Average number of shares in issue (m)	254.0	319.0	339.8	390.1	414.1	414.4
Basic & diluted IFRS EPS (p)	10.37	9.02	9.41	4.33	8.20	9.76
EPRA EPS (p)	6.95	7.25	8.05	8.37	8.50	8.81
Adjusted EPS (p)	5.26	5.98	6.68	7.11	7.04	7.28
Dividend per share (declared)	6.17	6.29	6.41	6.54	6.77	6.96
EPRA earnings dividend cover	113%	115%	126%	128%	126%	127%
Adjusted earnings dividend cover	85%	95%	104%	109%	104%	105%
NAV total return	9.5%	8.5%	8.4%	3.8%	7.6%	8.7%
EPRA cost ratio		17.1%	15.8%	16.6%	17.2%	16.9%
BALANCE SHEET						
Investment properties	310.5	405.7	437.6	504.3	517.8	534.0
Other non-current assets	10.1	15.9	62.0	68.1	132.5	139.3
Non-current assets	320.7	421.6	499.7	572.4	650.3	673.3
Cash and equivalents	47.8	8.0	13.3	22.5	10.3	10.7
Other current assets	0.6	0.1	1.6	1.5	1.2	1.2
Current assets	48.3	8.1	14.8	24.1	11.5	11.9
Borrowings	(23.5)	(74.2)	(110.9)	(122.4)	(183.4)	(194.6)
Other non-current liabilities	(1.8)	(2.8)	(2.6)	(4.3)	(4.3)	(4.3)
Non-current liabilities	(25.2)	(77.0)	(113.5)	(126.7)	(187.7)	(198.9)
Borrowings	0.0	0.0	0.0	(14.8)	0.0	0.0
Other current liabilities	(3.1)	(3.1)	(6.7)	(9.1)	(10.8)	(11.2)
Current Liabilities	(3.1)	(3.1)	(6.7)	(23.9)	(10.8)	(11.2)
Net assets	340.7	349.5	394.2	445.9	463.3	475.1
Adjust for derivative financial liability/(asset)	(0.1)	(0.0)	(0.1)	(0.4)	(1.1)	(0.4)
EPRA net tangible assets (NTA)	340.6	349.5	394.2	445.6	462.2	474.8
Period end shares (m)	319.0	319.0	350.6	404.8	414.4	414.4
IFRS NAV per ordinary share	106.8	109.6	112.4	110.2	111.8	114.7
EPRA net tangible assets (NTA) per share	106.8	109.6	112.4	110.1	111.5	114.6
CASH FLOW						
Net cash flow from operating activities	14.9	21.0	(13.9)	29.5	(22.6)	33.6
Purchase of investment properties (including acquisition costs)	(73.4)	(88.5)	(28.1)	(71.9)	(4.5)	(3.5)
Capital improvements	(8.2)	(1.7)	(1.1)	(11.2)	(9.5)	(8.0)
Other cash flow from investing activities	0.1	0.9	1.6	5.3	6.1	6.5
Net cash flow from investing activities	(81.5)	(89.3)	(27.6)	(77.7)	(7.9)	(5.0)
Issue of ordinary share capital (net of expenses)	132.2	0.0	34.6	60.5	11.2	0.0
(Repayment)/drawdown of loans	(0.9)	51.2	38.2	27.7	45.0	10.0
Dividends paid	(16.1)	(20.0)	(21.9)	(25.7)	(27.7)	(28.6)
Other cash flow from financing activities	(2.2)	(2.8)	(4.1)	(5.1)	(10.2)	(9.5)
Net cash flow from financing activities	112.9	28.5	46.8	57.4	18.4	(28.2)
Net change in cash and equivalents	46.3	(39.8)	5.3	9.2	(12.1)	0.4
Opening cash and equivalents	1.5	47.8	8.0	13.3	22.5	10.3
Closing cash and equivalents	47.8	8.0	13.3	22.5	10.3	10.7
Balance sheet debt	(23.5)	(74.2)	(110.9)	(137.2)	(183.4)	(194.6)
Unamortised loan arrangement costs	(1.7)	(2.2)	(3.6)	(5.1)	(3.9)	(2.7)
Net cash/(debt)	22.7	(68.4)	(101.3)	(119.8)	(176.9)	(186.5)
Gross LTV (net debt as % gross assets)	6.8%	17.8%	22.3%	23.8%	28.3%	28.8%

Source: Impact Healthcare REIT historical data, Edison Investment Research

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