RESEARCH

Summary: Befimmo S.C.A.

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Credit Rating: BBB/Positive/A-2

Rationale

The ratings on Belgium-based real estate company Befimmo S.C.A. reflect Befimmo's portfolio of commercial real estate, which produces resilient cash flow streams. This is the result of the good quality of the company's assets, which are leased on long contracts to strong tenants; overall positive indexation in its lease portfolio; and limited exposure to speculative developments over the cycle. This is offset by Befimmo's relatively small portfolio with a narrow focus in terms of geography and asset type, and its exposure to more volatile areas outside the Brussels central business district (CBD) area. Gross financial debt was €413 million at Sept. 30, 2005.

The ongoing downturn in the Brussels office space market has had an adverse effect on rent and vacancy levels, which will negatively impact Befimmo's near- to medium-term cash flows. Befimmo's vacancy level decreased to 7.2% at Sept. 30, 2005, from 8.6% at the end of September 2004. Although still relatively high, this is lower than the market average of about 11%. Newly signed and extended lease contracts are at lower levels, however, which will negatively impact future cash flows. Nevertheless, Befimmo's average lease duration for its 20 largest clients (about 71% of total rents) in the portfolio was about 7.6 years at the end of September 2005, which limits the yearly amounts exposed to rent renewal at lower levels. Furthermore, the company's existing lease portfolio allows for positive indexation, which mitigates the lost margin in rents.

Befimmo's financial profile is strong for the ratings. The LTV ratio was a low 37% at the end of September 2005, which is a reduction from 40% at Sept. 30, 2004. For the current ratings, this ratio is expected to remain below 50%. The company's tax-exempt status as a SICAFI--Société d' Investissement à Capital Fixe--imposes a 50% maximum gearing level; gearing was 44% according to the SICAFI definition at Sept. 30, 2005. EBITDA net interest coverage remained very strong at 4.3x for the fiscal year ended Sept. 30, 2005, mainly as a result of very low average debt cost (3.3%). The ratio of funds from operations (FFO) to net debt stood at a solid 12% for fiscal year 2005; this is expected to remain above 8% over the cycle for the current ratings.

Short-term credit factors

The short-term rating is 'A-2'. Lower rent levels for new or extended lease contracts, combined with the sale of the Borschette building and increasing expenses for new leasing activity (in the form of tenant improvements, incentives, and commissions) are expected to lead to a slight reduction in the operating margin and cash flows in 2006. Furthermore, the company is expected to continue to invest in new assets (within the limits of the SICAFI gearing target). If any new assets are not met by matching asset disposals, however, this could lead to increased debt levels, as most of Befimmo's operating cash flows are required to be distributed as dividends.

Liquidity is adequate, consisting primarily of a €350 million syndicated bank facility due in 2009. Part of this syndicated facility is expected to remain permanently undrawn and used as a back-up line (€295 million was undrawn at Sept. 30, 2005) for the company's heavy commercial paper drawings (€278 million was outstanding at Sept. 30, 2005). Short-term debt maturities were €298 million at Sept. 30, 2005, adequately covered by undrawn committed facilities. Overall exposure to interest rate (EURIBOR-based) hikes is substantially capped (at 5%) until year-end 2008.

Outlook

The positive outlook reflects the company's strong credit ratios, which, if expected to be sustainable on a permanent basis, could lead to a one-notch upgrade. The outlook could be revised back to stable in the event of a further weakening of the Brussels office market, or if there is a material rise in interest rates.

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