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# Befimmo S.C.A.

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## Table Of Contents

Major Rating Factors

Rationale

Outlook

Business Description

Business Risk Profile: Low Exposure To Development, Solid Occupancy Rate, And High Average Lease Duration

Financial Risk Profile: Small Operating Cash Flows And Steady Debt

Financial Statistics/Adjustments

Related Criteria And Research

# Befimmo S.C.A.

## Major Rating Factors

| Corporate Credit Rating |
| --- |
| BBB/Stable/A-2 |

**Strengths:**

- Good quality portfolio that generates stable cash flows, albeit constrained.
- Occupancy rates well above market average, mainly with long-term leases mostly to public sector tenants with strong credit standing.
- Relatively low exposure to development activities.
- Lower financing costs and better debt service capacity than other European real estate companies.

**Weaknesses:**

- Large exposure to the cyclical office segment and the oversupplied Brussels market, and to a lesser extent, even tougher Brussels suburbs.
- Decrease in fair value of investment properties portfolio in 2011 and limited near-term potential for rent growth.
- Cash flow metrics unlikely to strengthen over the short-term given stunted rental growth in the Brussels market and rising debt costs in the real estate sector.
- Relatively low revenue base owing to the company's small size and limited organic growth opportunities.

## Rationale

The ratings on Belgium-based real estate company Befimmo S.C.A. reflect Standard & Poor's Ratings Services' view of the company's good-quality assets; its long-term leases to creditworthy tenants; and its limited exposure to development activities. These strengths are tempered by Befimmo's high exposure to the oversupplied Brussels office market, which continues to face high vacancy rates overall. In addition, the company is exposed to concentration risk owing to its focus on the Belgium federal and regional entities and the European institutions, whose leases represent 66.6% of gross revenues.

We view Befimmo's business risk profile as "strong" according to our criteria. Befimmo's strategy mainly focuses on the long-term holding and renting of real estate assets, which, from a credit standpoint, is associated with passive low-risk property ownership and rent collection. The portfolio is of average size compared with its peers' (€1,971 million on Dec. 31, 2011). It is composed of offices mainly situated in Brussels with a long average lease maturity of 9.04 years and a tenant base that has a strong credit quality. Some 8.6% of rental income comes from peripheral districts of Brussels, which carry higher vacancy rates than the centre. We view this as a risk factor, together with Befimmo's strong focus on the Brussels property market and public tenants (namely Belgium federals states and European institutions), which represent 66.9% of the company's gross revenues. That said, concentration risk is partly offset by the long-term nature of their tenancies.

Befimmo's development strategy is relatively cautious in our opinion. Large renovation projects are backed by long-term lease commitments from strong tenants, which offset redevelopment and renting risks.

Our assessment of Befimmo's financial risk profile as "significant" is based on the company's somewhat high loan-to-value (LTV) internal limit set at around 50% and the relatively low cash flows metrics, although we understand they are standard for the real estate industry. Mitigating factors are the resilience and the predictability of cash flows from Befimmo's mostly long-term tenancies and its good access to capital markets, which remain key rating drivers given the sector's capital intensive characteristics. The ratings also capture the company's ability to service its debt with an EBITDA interest coverage ratio higher than 3x. Befimmo's tax-exempt status as a SICAFI (a Belgian tax-transparent vehicle) currently imposes maximum gearing of 65%.

### S&P base-case operating scenario:

Over the next two years, we anticipate that Befimmo will continue to record slightly negative rental income growth on a like-for-like basis, as rental demand in Belgium remains subdued. For the current portfolio, we believe the decline in revenues should be mitigated by the full year's rent contribution from the "Pavilion" building acquired in February 2011. In addition, new assets coming into operation should offset the loss of income from the disposals of the "Empress Court" and "Kattendijkdok" buildings in 2010 and 2011.

We forecast flat market valuations for Befimmo's properties owing to our view that Brussels property market yields may not compress until the end of 2013. This forecast is sensitive to the potential supply of new projects in Brussels in 2013.

### S&P base-case cash flow and capital-structure scenario:

We anticipate that Befimmo should post a Standard & Poor's-adjusted ratio of EBITDA to interest above 3x over the next two years, despite gradually increasing cost of debt in the sector. Still, funds from operations (FFO) to debt should remain in the 8%-10% range as cash flow generation remains solid and the company monitors its debt leverage prudently.

We forecast an adjusted LTV ratio between 45% and 48% over the next couple of years, which we believe remains adequate for the current ratings.

We believe the company will likely refinance its upcoming debt maturities to fund its renovation works. As a result, the LTV ratio will very much depend on the share of stock dividend in the overall dividend payment.

We factored into our analysis a slight depreciation of the assets portfolio value until 2013 to reflect the negative effect of a slowdown of real estate activity on the appraisal values.

### Liquidity

The short-term rating is 'A-2'. We assess Befimmo's liquidity as "adequate" as our criteria define the term, because we anticipate that its liquidity sources will be sufficient to meet its funding needs over the next 12 months.

On Dec. 31, 2011, Befimmo's liquidity uses for the next 12 months included:

- Short-term debt maturities of €392 million, including a €130 million syndicated loan expiring on March 30, 2012, and €262 million outstanding under a €400 million commercial paper program;
- Committed investment costs of about €50 million; and
- Our forecast of about €30 million of cash dividends.

Against these short-term cash calls, we anticipate:

- €411 million of available committed credit facilities excluding the commercial paper back-up lines;
- €4 million of unrestricted cash; and
- About €80 million of FFO.

Because Befimmo distributes free cash flows to its shareholders under its SICAFI status, we think the company is likely to refinance rather than repay existing and future debt. The company's maintenance of adequate backup liquidity resources is therefore important.

Supporting liquidity are the company's good access to capital market as evidenced by the successful closing of its €162 million bond in April 2011 and €110 million bond in December 2011, the extended average debt maturity of 4.5 years (from 2.9 years as of Sept. 30, 2010), and the headroom under the covenants, which we estimated was adequate on Dec. 31, 2011.

Befimmo has what we view as a satisfactory hedging strategy, consisting of a combination of caps and swaps. Overall, Befimmo's interest rate policy is to hedge a decreasing portion of borrowings, over a period of five to 10 years. That said, the company has indicated that 83% of total debt was hedged on Dec. 31, 2011.

## Outlook

The stable outlook reflects our view of Befimmo's good-quality office property portfolio and long-term leases, which will likely enable it to continue generating stable and predictable income.

We anticipate that Befimmo will maintain an EBITDA interest-coverage ratio of more than 2.5x and a maximum LTV ratio of about 50% over the short to medium term. In addition, we believe that Befimmo will likely maintain adequate hedging and backup credit lines to limit any interest rate-related risks in the medium to long term. We forecast that Befimmo should retain a high degree of rent predictability, which should help mitigate the risks stemming from the rent concentration in a single regional market and a concentration of its tenants in the Belgian public sector and the EU Commission.

Ratings upside depends, in our view, on the company's nominal cash flow increasing to a more resilient level, resulting in a full-year FFO of more than €200 million, an adjusted LTV ratio of less than 40%, and an average debt duration remaining above 3.5 years.

Conversely, we could take a negative rating action in the event of an unexpected and significant downward revaluation of the company's real estate portfolio, combined with an absence of deleveraging actions to maintain the LTV ratio below 50%, or if Befimmo makes material debt-financed acquisitions.

## Business Description

Befimmo is Belgium's second-largest property investment company after Cofinimmo S.A./N.V. (BBB/Stable/A-2), with about €1.9 billion of property assets, principally comprising offices in the Brussels area. Befimmo is listed on the Brussels stock exchange. Its main shareholder is AG Insurance and associated companies, which holds 17.4% of Befimmo's shares, according to Befimmo.

## Business Risk Profile: Low Exposure To Development, Solid Occupancy Rate, And High Average Lease Duration

The major supports for Befimmo's business risk profile, which we consider "strong," are its:

- Stable and predictable cash flows stemming from the long average lease duration of 9.02 years, as of Dec. 31, 2011, that is significantly more than peers'. The high proportion of public sector tenants, which generally have longer leases than corporations, underpins the long duration.
- Low exposure to development, representing less than 5% of the portfolio's total fair value, generally backed by long-term lease commitments from tenants that offset redevelopment and renting risks.
- High and resilient occupancy rate, despite the strong oversupply in the market, which is supported by long-term leases and the high quality of its assets. Befimmo's occupancy also remains substantially higher than the market rate in most geographic areas, which enables it to provide better visibility on revenues and stable cash flows.

These supports are partially offset by Befimmo's:

- Concentration of assets in the cyclical office segment, which faces a challenging economic environment, notably in the oversupplied Brussels market.
- Asset revaluation (negative 0.93% over the last 12 months) and rental yield (6.61%), which are still in the stabilizing phase as of Dec. 31, 2011. However, we observed a positive change in fair value during the preceding three months mirroring trends in the sluggish Brussels market.
- Some tenant concentration--mainly the EU institutions and Belgian state administrative offices--although they benefit from strong credit quality and long-term, secured leases.

## Financial Risk Profile: Small Operating Cash Flows And Steady Debt

Befimmo's financial risk profile is "significant," in our view, owing to the following weaknesses:

- Befimmo's low revenues relative to peers', with an EBITDA of about €100 million. That said, the company's income is sufficient to absorb about €2 million of rental income subject to a break option over the coming year.
- The company's relatively highly leveraged capital structure, with ratios of Debt to EBITDA at around 8.5x, Loan-To-Value (LTV) at 44.5% and a maximum LTV target at around 50% on Dec. 31, 2011. We do not forecast a decline in debt leverage because Befimmo's investments are generally debt-funded. This may be mitigated by the use of equity, such as stock dividend distribution.
- Constrained cash flow metrics compared with peers, owing to some vacancy on properties under renovation (about 117,000 squareare meters subject to refurbishment in 2011), the rising cost of debt (to 3.55% on Dec. 31, 2011, from 3% on March 31, 2011), and debt-funded investments resulting in FFO to debt of less than 10%.

These weaknesses are mitigated by:

- The low, albeit increasing, cost of debt at 3.55% at year-end 2011, with no refinancing maturities in 2012 that are not backed by available sources of funding.
- High visibility on and stability of cash flows from Befimmo's property portfolio. We expect the company to maintain high debt service, with an EBITDA interest coverage ratio of more than 3x.

## Financial Statistics/Adjustments

Befimmo prepares its financial statements under International Financial Reporting Standards (IFRS).

As the company changed its fiscal period this year, we used the 12-months data as of Dec. 31 for 2011 and as of

Sept. 31 for the preceding years. The purpose was to better compare Befimmo's performance over similar periods of time although we did not include the last calendar quarter of 2010 as a result.

We adjust Befimmo's reported EBITDA and EBIT by excluding revaluation gains and losses from disposals, which are noncash in nature.

**Table 1**

**Reconciliation Of Befimmo S.C.A. Reported Amounts With Standard & Poor's Adjusted Amounts (Mil. €)**

| | --Fiscal year ended Dec. 31, 2011-- | | | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|---|
| **Befimmo S.C.A. reported amounts** | | | | | | | | | | |
| | **Debt** | **Shareholders' equity** | **Revenues** | **EBITDA** | **Operating income** | **Interest expense** | **Cash flow from operations** | **Cash flow from operations** | **Dividends paid** | **Capital expenditures** |
| Reported | 877.2 | 1,002.6 | 124.8 | 117.2 | 98.2 | 25.8 | -- | -- | -- | -- |
| **Standard & Poor's adjustments** | | | | | | | | | | |
| Postretirement benefit obligations | -- | 0.2 | -- | 0.3 | 0.3 | -- | 0.2 | 0.2 | -- | -- |
| Reclassification of nonoperating income (expenses) | -- | -- | -- | -- | 0.3 | -- | -- | -- | -- | -- |
| Minority interests | -- | 67.8 | -- | -- | -- | -- | -- | -- | -- | -- |
| EBITDA--disposals of investment properties (gains)/losses | -- | -- | -- | (14.6) | (14.6) | -- | -- | -- | -- | -- |
| D&A--asset valuation (gains)/losses | -- | -- | -- | -- | 19.0 | -- | -- | -- | -- | -- |
| Total adjustments | 0.0 | 68.0 | 0.0 | (14.3) | 5.0 | 0.0 | 0.2 | 0.2 | 0.0 | 0.0 |
| **Standard & Poor's adjusted amounts** | | | | | | | | | | |
| | **Debt** | **Equity** | **Revenues** | **EBITDA** | **EBIT** | **Interest expense** | **Cash flow from operations** | **Funds from operations** | **Dividends paid** | **Capital expenditures** |
| Adjusted | 877.2 | 1,070.6 | 124.8 | 102.9 | 103.2 | 25.8 | 0.2 | 0.2 | 0.0 | 0.0 |

D&A--Depreciation and amortization.

**Table 2**

**Befimmo S.C.A. Peer Comparison**

| | **Befimmo S.C.A.** | **Cofinimmo S.A./N.V.** | **Gecina** | **Derwent London PLC** | **Societe Fonciere Lyonnaise S.A.** |
|---|---|---|---|---|---|
| Corporate credit rating as of March 13, 2012 | BBB/Stable/A-2 | BBB/Stable/A-2 | BBB-/Stable/A-3 | BBB/Stable/A-2 | BBB-/Stable/A-3 |
| **(Mil. mixed currencies)** | --Average of past three fiscal years-- | | | | |
| Currency | € | € | € | £ | € |
| Revenues | 122.6 | 197.0 | 633.7 | 124.6 | 180.1 |
| EBITDA | 107.2 | 179.1 | 497.8 | 97.3 | 154.3 |
| Interest expense | 27.0 | 73.6 | 181.8 | 39.3 | 57.9 |
| Net income from continuing operations | 24.7 | 76.8 | (216.9) | 182.6 | (160.2) |

**Table 2**

| Befimmo S.C.A. Peer Comparison (cont.) | | | | | |
|---|---|---|---|---|---|
| Working capital | (0.4) | (3.7) | 13.7 | 6.5 | 0.7 |
| Capital expenditures | 17.9 | 21.4 | 389.3 | 145.1 | 100.7 |
| Dividends paid | 41.1 | 60.8 | 301.7 | 26.0 | 109.6 |
| Cash and short-term investments | 4.6 | 5.3 | 55.9 | 9.9 | 15.8 |
| Debt | 820.6 | 1,666.7 | 5,016.0 | 839.5 | 1,243.2 |
| Equity | 1,067.6 | 1,417.7 | 5,926.5 | 1,457.9 | 2,030.3 |
| Debt and equity | 1,888.2 | 3,084.4 | 10,942.5 | 2,297.4 | 3,273.5 |
| **Adjusted ratios** | | | | | |
| EBITDA margin (%) | 87.4 | 90.9 | 78.6 | 78.1 | 85.7 |
| EBITDA interest coverage (x) | 4.0 | 2.4 | 2.7 | 2.5 | 2.7 |
| Debt/EBITDA (x) | 7.7 | 9.3 | 10.1 | 8.6 | 8.1 |
| Total debt/debt plus equity (%) | 43.5 | 54.0 | 45.8 | 36.5 | 38.0 |

**Table 3**

**Befimmo S.C.A. Financial Summary**

| | 2011 | 2010 | 2009 | 2008 | 2007 |
|---|---|---|---|---|---|
| Rating history | BBB/Stable/A-2 | BBB/Stable/A-2 | BBB/Stable/A-2 | BBB/Stable/A-2 | BBB/Stable/A-2 |
| **(Mil. €)** | | | | | |
| Revenues | 124.8 | 124.0 | 119.1 | 109.5 | 104.9 |
| EBITDA | 102.9 | 112.5 | 106.4 | 91.4 | 88.1 |
| Operating income | 102.9 | 112.5 | 106.4 | 91.4 | 88.1 |
| EBIT | 103.2 | 112.8 | 109.0 | 100.3 | 87.2 |
| Interest expense | 25.8 | 23.2 | 31.9 | 37.2 | 32.6 |
| Net income from continuing operations | 62.0 | 46.7 | (34.5) | 58.2 | 89.1 |
| Funds from operations (FFO) | N/A | 94.0 | 83.0 | 66.2 | 56.8 |
| Capital expenditures | N/A | 23.7 | 29.8 | 48.3 | 0.0 |
| Dividends paid | 66.2 | 62.7 | 60.6 | 49.8 | 48.2 |
| Cash and short-term investments | 4.2 | 3.5 | 6.1 | 4.6 | 6.0 |
| Debt | 877.2 | 792.1 | 792.4 | 872.4 | 845.1 |
| Equity | 1,070.6 | 1,082.1 | 1,050.2 | 1,028.5 | 996.8 |
| Debt and equity | 1,947.9 | 1,874.2 | 1,842.7 | 1,900.9 | 1,841.9 |
| Valuation of Investment Property | 1,971.3 | 1,922.6 | 1,922.9 | 1,886.5 | 1,812.9 |
| **Adjusted ratios** | | | | | |
| Annual revenue growth (%) | 0.7 | 4.1 | 8.7 | 4.4 | 37.6 |
| EBITDA margin (%) | 82.4 | 90.7 | 89.3 | 83.5 | 84.0 |
| EBITDA interest coverage (x) | 4.0 | 4.9 | 3.3 | 2.5 | 2.7 |
| Return on capital (%) | 5.4 | 6.1 | 5.8 | 5.4 | 6.0 |
| FFO/debt (%) | N/A | 11.9 | 10.5 | 7.6 | 6.7 |
| Debt/EBITDA (x) | 8.5 | 7.0 | 7.4 | 9.5 | 9.6 |
| Debt/debt and equity (%) | 45.0 | 42.3 | 43.0 | 45.9 | 45.9 |
| Rental yield (%) | 6.4 | 6.4 | 6.3 | 5.9 | 7.3 |
| Rental income coverage (x) | 4.8 | 5.4 | 3.7 | 2.9 | 3.2 |

**Table 3**

| Befimmo S.C.A. Financial Summary (cont.) | | | | | |
|---|---|---|---|---|---|
| Loan to value (%) | 44.5 | 41.2 | 41.2 | 46.2 | 46.6 |

## Related Criteria And Research

- Criteria Methodology: Business Risk/Financial Risk Matrix Expanded, May 27, 2009
- Methodology And Assumptions: Liquidity Descriptors For Global Corporate Issuers, Sept. 28, 2011
- Key Credit Factors: Global Criteria For Rating Real Estate Companies, June 21, 2011

| **Ratings Detail** (As Of March 30, 2012) | |
|---|---|
| **Befimmo S.C.A.** | |
| Corporate Credit Rating | BBB/Stable/A-2 |
| Senior Unsecured (3 Issues) | BBB |
| Short-Term Debt (1 Issue) | A-2 |
| **Corporate Credit Ratings History** | |
| 18-Jun-2007 | BBB/Stable/A-2 |
| 27-Dec-2006 | BBB/Watch Neg/A-2 |
| 25-Feb-2004 | BBB/Positive/A-2 |
| **Business Risk Profile** | Strong |
| **Financial Risk Profile** | Significant |
| **Debt Maturities** | |
| On Dec. 31, 2011:<br>2012: €137 mil.<br>2013: €527 mil.<br>2014: €7 mil.<br>2015: €118 mil.<br>2016 and thereafter: €8 mil. | |

*Unless otherwise noted, all ratings in this report are global scale ratings. Standard & Poor's credit ratings on the global scale are comparable across countries. Standard & Poor's credit ratings on a national scale are relative to obligors or obligations within that specific country.

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