S&P Global
Ratings

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Befimmo S.A.

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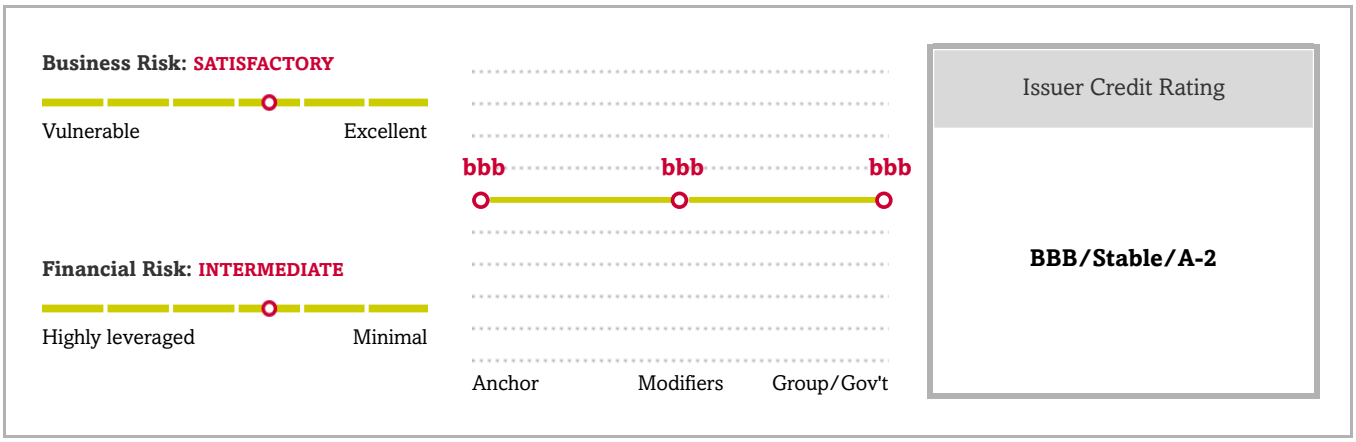


Credit Highlights

Overview

Key strengths	Key risks
Well located office assets, with over 50% of portfolio gross value-added (GAV) in the Brussels central business district (CBD), where supply and demand dynamics remain supportive.	Uncertainty on how COVID-19-related trends and the increase in working from home could affect the office sector in the long term, with macroeconomic forecasts showing a moderate recovery in the eurozone.
Solid tenant base of large public sector organizations (62.6% of rental income) and long-term leases (7.2 years on average), supporting rental income stability and predictability.	Large redevelopment pipeline (15% of GAV), which will lead to a temporary increase in leverage.
Strong preletting activity, with 83% of current committed ongoing projects already prelet, mitigating vacancy risk inherent in redevelopment	Single market and segment exposure (94.5% of portfolio value is Belgian offices), with higher volatility and susceptibility to economic cycles than other asset classes in Europe, such as residential markets.
Modest debt leverage, with adjusted debt to debt plus equity of 39.8% at year-end 2020, which should be sufficient to finance the committed development pipeline and absorb potential asset devaluations.	Temporarily shrinking EBITDA base, on the back of asset disposals and the large redevelopment pipeline, will likely result in deteriorating debt to EBITDA, which is already relatively high (10.8x at year-end 2020)

Economic uncertainty and an increase in working from home could reduce demand for office space and subdue rent levels. S&P Global Ratings expects fragile business confidence and heightened economic uncertainty resulting from the COVID-19 pandemic will temporarily result in subdued demand for office space. Similarly, the pandemic-led increase in remote working and pressure on companies to control costs may reduce demand for office space as tenants reorganize their workforces and operations. We therefore expect flattish performance on average for office real estate investment trusts (REITs) in 2021-2022, with rental and valuation declines limited to 5% per year.

We forecast Befimmo S.A.'s net rental income will be flat to slightly negative in the coming two years. Befimmo posted a 0.2% like-for-like decrease in net rental income and a flat portfolio revaluation in 2020, with occupancy remaining high at 95.2% compared with 94.4% at Dec. 31, 2019. Going forward, the long lease maturity profile, with a limited portion of leases coming to maturity in 2021--about 10% of total rental income and about 6% in 2022--reduces the risk of increasing vacancies from tenant departures or lower rents from renegotiations amid unfavorable market dynamics. Therefore, we expect flat or only slightly negative like-for-like rental growth for Befimmo in the coming two years.

Large asset disposals in 2020 built headroom for a debt increase to fund the large redevelopment pipeline, but debt to EBITDA continues to weaken. Following the large disposals completed in 2020, with over €250 million in sales proceeds and flat portfolio revaluation, the company reduced its S&P Global Ratings-adjusted debt to debt plus equity

to 39.8% at year-end 2020, from 41.1% a year earlier. This improvement provides the company with more headroom to maintain its debt to debt plus equity below 45% in the coming years, and therefore within our rating threshold. We forecast this ratio will deteriorate as Befimmo continues to fund its upcoming development pipeline (15% of the portfolio) partially with debt. However, we expect metrics will remain commensurate with our current rating assessment given Befimmo's long track record of successful asset rotations and maintaining headroom under its own financial policy, with a maximum loan-to-value (LTV) target of 45%. That said, we expect a temporary deterioration in debt to EBITDA to 14x-16x over the next 12 months, on the back of asset disposals and redevelopment activities. We believe this ratio should start improving from 2023, when EBITDA from most project deliveries kick in.

Outlook: Stable

The stable outlook continues to reflect Befimmo's stable and predictable rental income from its good-quality office property portfolio and long-term leases with trustworthy tenants. The outlook also reflects our expectation that Befimmo will maintain EBITDA interest coverage of at least 3.5x and an adjusted debt to debt plus equity of less than 45% over the next two years.

Downside scenario

We could lower our ratings on Befimmo in the next 24 months if the company's credit metrics deteriorate more than we anticipate, with S&P Global Ratings-adjusted debt to debt plus equity sustainably exceeding 45%. This could result from lower-than-anticipated asset disposals, higher-than-expected development capital expenditure (capex), or an unexpected decline in valuations.

At the same time, a negative rating action could follow an extended deterioration of Befimmo's portfolio quality and size, which could result in EBITDA interest coverage decreasing close to 3.5x. This could happen if Befimmo sells off more prime assets than anticipated.

We might also consider lowering the rating if the company's business model becomes riskier with, for example, a substantial proportion of revenue coming from co-working space management, or if more redevelopment activities drain liquidity.

Credit stress could also come from lower-than-anticipated sources to cover upcoming debt maturities, dividends, and large redevelopment capex in the next 12 months that could deteriorate liquidity.

Upside scenario

An upgrade would depend on Befimmo's ability to improve its adjusted debt to debt plus equity to near 35% on a sustainable basis, with EBITDA interest coverage remaining comfortably above 3.5x.

An upgrade would also require Befimmo to build a track record of rental growth on a like-for-like basis and a marked change in the company's earnings base, with improved diversification of income streams.

Our Base-Case Scenario

Assumptions

- GDP in Belgium to recover to 4.3% growth in 2021, following a 6.3% contraction in 2020. The sharp decrease in economic output last year will result in an increase in unemployment to 6.0% in 2021 from 5.6% in 2020. We estimate consumer price inflation growth of 1.8% in 2021 and 1.4% in 2022.
- Flat to slightly negative gross rental income on a like-for-like basis for Befimmo in 2021 and 2022, affected by our assumptions of lower business confidence and subdued demand for office space.
- Stable occupancy, at 94%-95% in 2021 and 2022, since few leases expire this year and next year (about 10% and 6% of gross rental income respectively) and the average lease duration is long at 7.2 years.
- Conservatively, a slightly negative like-for-like asset revaluation in 2021 of a maximum of 5%, and flat in 2022.
- Deteriorating EBITDA margins to about 60%-65%, resulting from a lower EBITDA base, stable fixed costs, and higher costs related to redevelopment activities.
- Redevelopment capex of about €180 million-€200 million per year during 2021-2022 as the main projects are currently underway and approaching delivery (Paradis express: About €30 million, delivery 2021; Quatuor: About €50 million, delivery 2022; and ZIN: About €320 million, delivery 2023.)
- Some opportunistic acquisitions of about €80 million in 2021, of which it has already completed €57 million in the first quarter with the Cubus building in Luxembourg and the Esprit Courbevoie development in Belgium.
- Asset disposals of about €150 million in 2021 and €130 million in 2022, in line with Befimmo's asset rotation strategy, including mainly divestments of mature assets.
- Dividends of about €50 million in 2021, corresponding to the minimum legal distribution requirement of regulated Belgian REIT (B-REIT) companies.

Key metrics

Befimmo S.A.--Key Metrics*

	--Fiscal year ended Dec. 31--				
	2019a	**2020a**	**2021e**	**2022f**	**2023f**
(Mil. €)					
EBITDA	108.0	97.1	70-80	75-85	80-90
EBITDA margin (%)	75.8	70.6	60-65	60-65	60-65
Dividends	88.2	68.7	40-50	40-50	40-50
Debt	1,120.0	1,052.9	1,100-1,200	1,200-1,300	1,400-1,450
EBITDA interest coverage (x)	5.6	5.1	3.5-4.5	3.5-4.5	3.5-4.5
Debt to EBITDA (x)	10.4	10.8	14-16	14-16	14-16
Debt to debt plus equity (%)	41.1	39.8	44-45	44-46	45-48

*All figures adjusted by S&P Global Ratings. a--Actual. e--Estimate. f--Forecast.

Company Description

Befimmo operates in the office real estate segment, with a focus on Belgium (94.5% of portfolio value with 68% located in Brussels) and, to a lesser extent, Luxembourg (5.5%). The company's portfolio consists of more than 100 buildings, with a total value of €2.7 billion at year-end 2020. It is listed on Euronext Brussels with a market capitalization of about €966 million (as of May 31, 2021). Befimmo has B-REIT status.

Befimmo's largest shareholders are insurers AXA Belgium SA and Ageas, which respectively owned 9.6% and 9.3% of the company on Dec. 31, 2020. In addition, BlackRock owned 3%, Befimmo owned 5.0% of its own shares, and 73.1% were split among investors each holding less than 3% of the company.

Peer Comparison

Table 1

Befimmo S.A.--Portfolio Summary (As of Dec. 31, 2020)

Segment focus	**Office**
Total portfolio value (bil. €)	2.7
Total GLA (square meters)	975,946
Occupancy (%)	95.2
Average lease maturity (years to next break)	7.2
Overall portfolio quality	Good quality portfolio with around 55% of the portfolio located in Brussels CBD (gross yield: offices 5.3%)
Market capitalization (mil. €)*	About 966

*As of May 31, 2021. GLA--Gross leasable area. CBD--Centra business district.

Table 2

Befimmo S.A.--Peer Comparison

Industry sector: Real estate investment trust or company

Companies	**Befimmo S.A.**	**Alstria Office REIT-AG**	**Cofinimmo S.A./N.V.**	**Merlin Properties Socimi S.A.**	**CPI Property Group S.A.**
Ratings*	BBB/Stable/A-2	BBB+/Stable/--	BBB/Stable/A-2	BBB/Stable/--	BBB/Watch Negative/--
Business risk profile*	Satisfactory	Satisfactory	Strong	Satisfactory	Satisfactory
Financial risk profile*	Intermediate	Modest	Intermediate	Intermediate	Intermediate
Portfolio value (bil. €)	2.7	4.6	4.9	12.8	10.3
Assets diversity	Offices 100%	Offices 100%	Health care 59%, Offices 30%, Distribution networks 11%	Offices 50%, Shopping centers 18%, Net leases 14%, Logistics 12%, Other 6%	Offices 52%, Retail 22%, Residential 9% , Hotel 7%, Other 10%
Occupancy (%)	95.2	92.4	97.4	94.2	93.7
WAULT (years)	7.2	6.1	12.0	5.4	3.6
Top 10 tenants as a % of GRI	81.1§	42.0	62.0	17.6	11.5

Table 2

Befimmo S.A.--Peer Comparison (cont.)

Industry sector: Real estate investment trust or company

Companies	Befimmo S.A.	Alstria Office REIT-AG	Cofinimmo S.A./N.V.	Merlin Properties Socimi S.A.	CPI Property Group S.A.
Geography diversity	Belgium 94.5% and Luxembourg 5.5%	Germany 100%	Belgium 66%, Germany 12%, France 10%, Netherlands 10%, Spain 2%, Finland <1%	Spain ~91%, Portugal ~9%	Czech Republic 41%, Germany 25%, Poland 15%, Hungary 6%, Other CEE 6% and Other Western Europe 6%
% development	~15%	3.1	6.8	N/A	2.1
EBITDA interest coverage (x)	5.1	4.2	6.5	2.7	2.8
Debt/EBITDA (x)	10.8	9.3	12.9	15.1	16.0
Debt/debt and equity (%)	39.8	27.6	47.0	44.9	49.1

*As of June 21, 2021. Source: Latest Company Reports. §Including 62.6% of public tenants N/A--Not applicable. WAULT--Weighted average unexpired lease term. GRI--Gross rental income. CEE--Central and Eastern Europe.

Business Risk: Satisfactory

Our business risk assessment reflects Befimmo's predictable and stable cash flow. Befimmo collected 99.7% of rents due in 2020, despite the COVID-19 pandemic's impact on economic activity. This compares positively with other rated peers in the office real estate segment and is reflective of Befimmo's high-quality tenant base and large exposure to creditworthy public-sector tenants, which represented 62.6% of total rent in 2020. These tenants include the Belgian public sector (53.9% of rent) and the European public sector (8.8%). The share of public tenants has slightly reduced from historical levels (about 70%), but we note that Befimmo recently signed new leases with public organizations such as the Flemish authorities for the ZIN project. Moreover, the dilution comes mainly from the regular disposal of small buildings in Belgium's provinces at the end of the lease. We also take a positive view of the company's long lease terms, at 7.2 years until the next break option, which provide cash flow stability and predictability and mitigate the inherent short-term volatility of the office market.

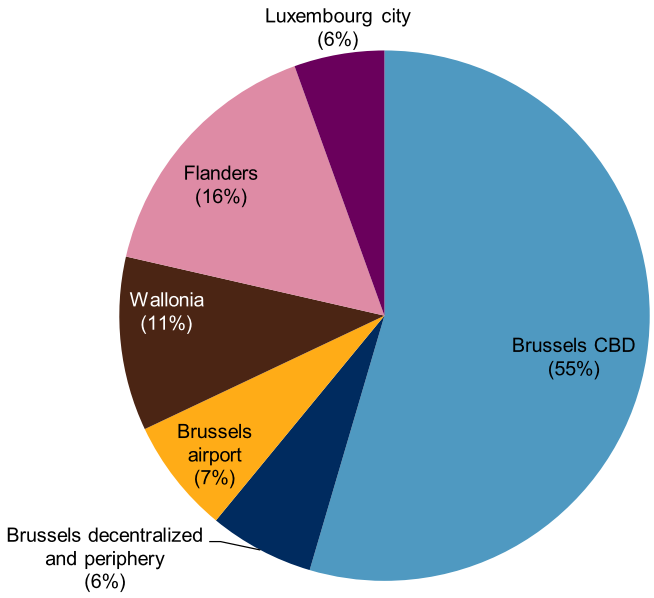
Befimmo's redevelopment activities are part of its asset rotation and value-creation strategy, partially funded by core asset disposals. The company received about €250 million from asset disposals in 2020 to fund its capex program. The total committed redevelopment pipeline represents about 15% of portfolio value. This is higher than the company's long-term average and that of most rated real estate peers, which generally limit their exposure to more risky redevelopment activities to 5%-10% of portfolio value. We believe redevelopment activities typically carry risks such as cost overruns, vacancies at completion, or unexpected drops in rental market rates during the construction cycle. However, to mitigate these risks Befimmo has prelet 83% of its committed pipeline as of today, including the full office preleasing of 70,000 square meters (sqm) to Flemish authorities with an 18-year lease, starting 2023, at the ZIN tower. The Quatuor project also has a 56% prelease rate thanks to contracts with a large financial institution and a major corporate client. Befimmo has now completed the demolition phase of the ZIN redevelopment project and is currently starting the rebuilding phase, re-using part of the materials obtained from the demolition for a total investment of €411

million. The Quatuor project is also advancing well, with delivery expected in 2022.

To fund this development pipeline, Befimmo will be selling off mature noncore assets from the Fedimmo portfolio located in Belgian provinces and will look for a partner for its ZIN building. This will complement the already completed sales of the Media, Guimard, Froissart, Schuman 3, Schuman 11, and more recent Wiertz building asset disposals in 2020 and 2021, and capitalizes on investor appetite for the Brussels office market. As a result, the company's share of rents generated by assets in the Brussels CBD will temporarily shrink to about 45% in 2021 from about 52% currently. However, the deterioration in portfolio size and quality should be only temporary because the majority of the projects under redevelopment are large buildings in Brussels CBD.

Chart 1

Befimmo S.A.--Gross Asset Value Breakdown (2020)



Source: Company report. CBD--Central business district.

The business risk profile also reflects Befimmo's relatively limited portfolio size of about €2.7 billion at Dec. 31, 2020, which is smaller than those of similarly rated peers such as Merlin Properties (€12.8 billion), CPI Property Group (€10.3 billion), or Alstria Office REIT-AG (€4.6 billion) on the same date. We believe a small-scale portfolio exposes holding companies to the risk of revenue volatility in the case of asset or tenant rotation. In addition, Befimmo has high rent concentration, with a single-market exposure to Brussels, which we consider as less liquid than other Western European office markets such as Paris and Berlin.

Financial Risk: Intermediate

We base Befimmo's financial risk profile on relatively prudent leverage, with our adjusted debt to debt plus equity at 39.8% on Dec. 31, 2020 (41.1% at year-end 2019), and a solid EBITDA interest coverage of about 5.1x at year-end 2020. The strong coverage ratio is supported by the relatively high-yield environment in Befimmo's main markets (European Public Real Estate Association [EPRA] net initial yield of 5.0% at year-end 2020 versus 2.7% for Societe Foncière Lyonnaise in Paris, for example). This ratio also reflects the company's low cost of debt, which remained stable at 2.0% in 2020 (2.0% in 2019). We believe that Befimmo will maintain an average hedging rate of about 90%-95% of financial obligations and backup credit lines to limit any significant interest-rate-related risks in the medium to long term.

Befimmo's credit metrics are burdened by a relatively high debt to EBITDA of about 10.4x, highlighting the capital-intensive nature of its business. This is particularly due to its significant redevelopment pipeline; and lower yields than some other riskier asset classes or geographical exposures. We also forecast a slight deterioration in EBITDA margins going forward as the rental income base shrinks due to disposals and there is a lag in EBITDA contribution from buildings under construction.

We expect Befimmo to dispose of €200 million-€300 million of assets during 2021-2023, of which €75 million already completed via the Wiertz building disposal, to partially fund its redevelopment pipeline. We view positively Befimmo's long track record of successful asset disposals, even in uncertain market conditions. This was proven in 2020 when Befimmo sold assets for over €250 million at or above book value, which will help maintain headroom under our current downside trigger of 45% S&P Global Ratings-adjusted debt to debt plus equity. Our assessment also takes into account the company's financial policy, targeting a maximum LTV ratio of 45%.

Overall, we expect our adjusted debt to debt plus equity to deteriorate toward 45% in 2021 and 2022, close to our downside rating threshold. However, we expect this to be only temporary as redevelopment works ramp up. We expect future disposals to result in debt to debt plus equity stabilizing below 45%. We conservatively do not assume equity issuances, although we factor in Befimmo's positive track record of equity market access and its large amount of treasury stock. It currently holds 5.0% of total shares outstanding, which could be used to partially fund the redevelopment pipeline. Similarly, our adjusted debt to EBITDA will also increase to 14x-16x. However, we believe the deterioration is only temporary, with the company's disposal proceeds and development project deliveries likely to restore its credit metrics back to our requirements for the current rating level.

We expect the company's ability to cover interest payments to remain solid, with EBITDA interest coverage consistently above 3.5x.

Financial summary

Table 3

Befimmo S.A.--Financial Summary

Industry sector: Real estate investment trust or company

	--Fiscal year ended Dec. 31--			
	2020	**2019**	**2018**	**2017**
(Mil. €)				
Revenue	137.7	142.4	144.1	143.2
EBITDA	97.1	108.0	116.6	117.7
Funds from operations (FFO)	72.5	83.0	95.3	94.6
Interest expense	19.1	19.1	18.9	19.5
Cash flow from operations	86.4	65.2	90.9	105.4
Capital expenditure	162.3	68.5	51.0	40.5
Free operating cash flow (FOCF)	(75.9)	(3.3)	39.9	64.8
Dividends paid	68.7	88.2	88.2	89.3
Discretionary cash flow (DCF)	(144.6)	(92.6)	(48.3)	(24.4)
Cash and short-term investments	2.4	2.9	0.6	0.3
Debt	1,052.9	1,120.0	1,160.6	990.2
Equity	1,591.4	1,603.9	1,443.2	1,448.5
Adjusted ratios				
Annual revenue growth (%)	(3.4)	(1.1)	0.6	3.9
EBITDA margin (%)	70.6	75.8	81.0	82.2
Return on capital (%)	3.6	4.0	4.6	4.8
EBITDA interest coverage (x)	5.1	5.6	6.2	6.0
Debt/EBITDA (x)	10.8	10.4	10.0	8.4
FFO/debt (%)	6.9	7.4	8.2	9.6
Debt/debt and equity (%)	39.8	41.1	44.6	40.6

Reconciliation

Table 4

Befimmo S.A.--Reconciliation Of Reported Amounts With S&P Global Ratings' Adjusted Amounts (Mil. €)

	--Fiscal year ended Dec. 31, 2020--				
Befimmo S.A. reported amounts					
	Debt	**EBITDA**	**Operating income**	**Interest expense**	**S&P Global Ratings' adjusted EBITDA**
Reported	1,005.5	97.4	96.3	19.1	97.1
S&P Global Ratings' adjustments					
Cash taxes paid	--	--	--	--	(1.0)
Cash interest paid	--	--	--	--	(23.5)
Reported lease liabilities	47.8	--	--	--	--
Postretirement benefit obligations/deferred compensation	2.0	--	--	0.0	--
Accessible cash and liquid investments	(2.4)	--	--	--	--
Nonoperating income (expense)	--	--	0.7	--	--

Table 4

Befimmo S.A.--Reconciliation Of Reported Amounts With S&P Global Ratings' Adjusted Amounts (Mil. €) (cont.)					
EBITDA: Gain/(loss) on disposals of PP&E	--	(0.3)	(0.3)	--	--
Depreciation and amortization: Asset valuation gains/(losses)	--	--	(1.4)	--	--
Total adjustments	47.4	(0.3)	(0.9)	0.0	(24.6)
S&P Global Ratings' adjusted amounts					
	Debt	**EBITDA**	**EBIT**	**Interest expense**	**Funds from operations**
Adjusted	1,052.9	97.1	95.4	19.1	72.5

Liquidity: Adequate

We view Befimmo's liquidity as adequate over the coming 12 months, with a ratio of sources to uses above 1.4x as of March 31, 2021.

Principal liquidity sources	Principal liquidity uses
• Unrestricted cash balance of €2.5 million; • About €820 million available under committed undrawn credit facilities, maturing in more than 12 months; and • Our forecast of cash funds from operations of €55 million-€60 million in the next 12 months.	• Short-term debt maturities of about €370 million, including drawn commercial paper of €363 million. We understand that the commercial paper is backed by long-term bank facilities, which are included in the €820 million credit facilities mentioned in the sources; • Redevelopment capex of about €190 million, although we understand not all of it is committed; and • Dividend payments of about €50 million.

Covenant Analysis

Befimmo maintained substantial headroom under its financial covenants at Dec. 31, 2020. We expect the company will maintain adequate headroom (more than 10%) under all maintenance covenants over the next 12-24 months.

Ratings Score Snapshot

Issuer Credit Rating

BBB/Stable/A-2

Business risk: Satisfactory

- **Country risk:** Low
- **Industry risk:** Low
- **Competitive position:** Satisfactory

Financial risk: Intermediate

- **Cash flow/leverage:** Intermediate

Anchor: bbb

Modifiers

- **Diversification/portfolio effect:** Neutral (no impact)
- **Capital structure:** Neutral (no impact)
- **Financial policy:** Neutral (no impact)
- **Liquidity:** Adequate (no impact)
- **Management and governance:** Satisfactory (no impact)
- **Comparable rating analysis:** Neutral (no impact)

Related Criteria

- Criteria | Corporates | General: Corporate Methodology: Ratios And Adjustments, April 1, 2019
- Criteria | Corporates | Industrials: Key Credit Factors For The Real Estate Industry, Feb. 26, 2018
- General Criteria: Methodology For Linking Long-Term And Short-Term Ratings, April 7, 2017
- Criteria | Corporates | General: Methodology And Assumptions: Liquidity Descriptors For Global Corporate Issuers, Dec. 16, 2014
- Criteria | Corporates | General: Corporate Methodology, Nov. 19, 2013
- General Criteria: Group Rating Methodology, Nov. 19, 2013
- General Criteria: Country Risk Assessment Methodology And Assumptions, Nov. 19, 2013
- General Criteria: Methodology: Industry Risk, Nov. 19, 2013
- General Criteria: Methodology: Management And Governance Credit Factors For Corporate Entities And Insurers, Nov. 13, 2012
- General Criteria: Use Of CreditWatch And Outlooks, Sept. 14, 2009

Business And Financial Risk Matrix

Business Risk Profile	Financial Risk Profile					
	Minimal	Modest	**Intermediate**	Significant	Aggressive	Highly leveraged
Excellent	aaa/aa+	aa	a+/a	a-	bbb	bbb-/bb+
Strong	aa/aa-	a+/a	a-/bbb+	bbb	bb+	bb
Satisfactory	a/a-	bbb+	**bbb/bbb-**	bbb-/bb+	bb	b+
Fair	bbb/bbb-	bbb-	bb+	bb	bb-	b
Weak	bb+	bb+	bb	bb-	b+	b/b-
Vulnerable	bb-	bb-	bb-/b+	b+	b	b-

Ratings Detail (As Of June 21, 2021)*

Befimmo S.A.	
Issuer Credit Rating	BBB/Stable/A-2
Senior Unsecured	BBB
Short-Term Debt	A-2
Issuer 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

*Unless otherwise noted, all ratings in this report are global scale ratings. S&P Global Ratings' credit ratings on the global scale are comparable across countries. S&P Global Ratings' credit ratings on a national scale are relative to obligors or obligations within that specific country. Issue and debt ratings could include debt guaranteed by another entity, and rated debt that an entity guarantees.

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