S&P Global
Ratings

Research

Research Update:

Belgium-Based Property Investment Company Befimmo Affirmed At 'BBB'; Outlook Stable

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Research Update:

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Overview

- Belgian real-estate trust Befimmo has shown resilient performance and stable credit metrics despite still-sluggish conditions in the Brussels office market.
- We are affirming our long- and short-term corporate credit ratings on Befimmo at 'BBB/A-2'.
- The stable outlook reflects our view that Befimmo's predictable rental income should allow it to maintain EBITDA interest coverage above 3x, with debt to debt plus equity staying below 50%.

Rating Action

On May 26, 2016, S&P Global Ratings affirmed its 'BBB/A-2' long- and short-term corporate credit ratings on Belgium-based property investment company Befimmo S.A. The outlook is stable.

At the same time, we affirmed the issue rating on Befimmo's unsecured debt at 'BBB'.

Rationale

The affirmation reflects Befimmo's resilient performance in 2015 and its stable credit metrics. It also reflects our expectation that Befimmo's rental income and cash flows should continue to be supported by its good quality assets, long-term leases to creditworthy tenants, and limited exposure to development activities.

In 2015, Befimmo's performance was robust despite the still-sluggish macroeconomic environment and subdued demand for office space in Brussels. The company maintained its occupancy rate at around 94%, in line with the previous year and above the average in the Brussels market, which remains around 90%. In our view, this is supported by the high share of Befimmo's portfolio (about 58%) located in the center of Brussels. Weighted-average leases remained long at about 8.60 years in 2015 (compared with 8.64 years in 2014), with mostly creditworthy tenants (the Belgian public sector and EU Commission represented about 66% of 2015 total rental income). Most rental income is contracted for the next two years, with only 1%-2% of rent at risk in 2016 and about 6% in 2017. We believe that Befimmo should retain a high degree of rent predictability, although its portfolio continues to show potential negative rent renegotiations that are currently estimated at about -8.6%. We note that this figure has slightly improved from the end of 2014 (-9.7%), although it remains in our view an important downside risk in the medium-to-long term.

We have revised our assessment of Befimmo's business risk profile to satisfactory from strong, in order to better position our view of Befimmo's credit quality among our rated universe of European real estate investment companies, in particular in the office sector. This change reflects two factors in particular: the absolute value of Befimmo's portfolio (€2.4 billion as of March 31, 2016), which is low compared with other European office players whose business risk profiles we assess in the above category (such as Derwent London, Gecina, or SFL) and its high rent concentration mainly in a single regional market, Brussels offices, which is still recovering and is significantly less liquid than the London or Paris office markets. At the same time, we have removed the negative comparable rating analysis, which reflected our previous assessment of Befimmo as being at the low end of the strong category. These two changes in the rating components do not affect the overall 'BBB' rating.

We continue to assess Befimmo's financial risk profile at intermediate, supported by our forecast of S&P Global Ratings-adjusted EBITDA interest coverage of 3x-4x and adjusted debt-to-debt-plus-equity staying below 50% in the next two years. Befimmo's EBITDA interest coverage remained at the upper part of our range for the intermediate category in 2015 (3.8x) supported by the relatively high-yield environment in Befimmo's main markets and by its low cost of debt, which has further improved in 2015 (to 2.66% compared with 3.16% in 2014). We believe that Befimmo will likely maintain adequate hedging and back-up credit lines to limit any interest-rate-related risks in the medium-to-long term.

On the other hand, we forecast that the adjusted ratio of debt-to-debt-plus-equity will remain close to our downgrade threshold of 50% in the next two years (46.5% as of December 2015), as a result of capital expenditure (capex) and dividend payments. We understand that management remains committed to its financial policy of maintaining leverage below 50%.

Lastly, our assessment of the financial risk profile also factors in the resilience and predictability of cash flows from Befimmo's mostly long-term tenancies. We note that the cash flow base remains relatively low, however, as a result of the small size of the asset portfolio.

Our base case assumes:

- 1%-2% like-for-like contraction in rental income in the next two years. We assume that compulsory lease indexation (we forecast consumer price index inflation at 1.2% in 2016 and 1.6% in 2017 for Belgium) will be offset by less-favorable pricing for lease renewals and new rental agreements.
- Occupancy rate to stabilize further at around 93%-94%, assuming a good letting rate of the 2016 project deliveries.
- Portfolio valuation to remain relatively flat in the next two years on a like-for-like basis (following 0.5% growth in 2015), due to stabilizing

vacancy levels and low speculative supply of high quality offices in the Belgian market. Overall portfolio value should modestly increase on an absolute basis as a result of capex.
- Capex of about €50 million-€60 million per year to support the development of upcoming projects, including maintenance capex of existing properties, in line with management's forecasts.
- Our base does not include any asset disposal or acquisition given we understand that nothing is committed at this stage.

Based on these assumptions, we arrive at the following credit measures:
- EBITDA interest coverage between 3x-4x in the next two years.
- Adjusted debt-to-debt-plus-equity on a fair value basis between 47% and 48% over the next two years.

Liquidity

We assess Befimmo's liquidity as adequate as we anticipate that the ratio of liquidity sources to uses will be about 1.4x in the 12 months to March 31, 2017.

As of March 31, 2016, we estimate that liquidity sources over the next 12 months mostly consist of:
- €503 million available under the credit facilities (with a maturity of more than 12 months).
- Forecast funds from operations of €80 million-€85 million.

This compares with our estimate of liquidity uses for the next 12 months of:
- Commercial papers of €288 million maturing within 12 months. These are backed up by long-term bank facilities, which are included as part of the €503 million credit facilities mentioned above.
- Limited other debt repayments of about €8 million.
- Capex of about €50 million-€55 million.
- Dividend payment of €80 million. For the purpose of the liquidity, we assume that the dividend will be paid in cash, although the company has a track record of offering the possibility of dividend distribution in a mixture of cash and shares.

We consider that Befimmo has well-established and solid relationship with banks, with a generally high standing in the credit markets. Our assessment of Befimmo's adequate liquidity also includes our view of its generally very prudent financial risk management and our expectation that Befimmo will maintain adequate headroom under all its maintenance covenants.

Outlook

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. Our stable outlook also anticipates that Befimmo will be able to maintain an EBITDA interest-coverage ratio around 3.5x and an adjusted ratio of debt-to-debt-plus-equity of less than 50% over the next two years.

Upside scenario

An upgrade would depend on Befimmo's ability to improve its adjusted debt-to-debt-plus-equity ratio to less than 40% on a sustainable basis, with EBITDA interest coverage remaining comfortably above 3.5x. An upgrade would also require Befimmo to be able to generate positive rental growth on a like-for-like basis and a step change in the company's earnings base with improved diversification of income streams.

Downside scenario

We could lower the ratings if adjusted debt-to-debt-plus-equity increases persistently above 50%. We believe that this would most likely occur if Befimmo funds more and more projects and acquisitions with debt only. We might also consider lowering the ratings if we see a material shift in the supply and demand characteristics in the Brussels office market or if negative reversions have a greater effect on rental income than anticipated, leading to a significantly lower forecast for cash flows than we currently expect from the leased portfolio in properties.

Ratings Score Snapshot

Corporate 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)
- Liquidity: Adequate (no impact)
- Financial policy: Neutral (no impact)
- Management and governance: Satisfactory (no impact)
- Comparable rating analysis: Neutral (no impact)

Related Criteria And Research

- Methodology And Assumptions: Liquidity Descriptors For Global Corporate Issuers, Dec. 16, 2014
- Corporate Methodology, Nov. 19, 2013

- Corporate Methodology: Ratios And Adjustments, Nov. 19, 2013
- Country Risk Assessment Methodology And Assumptions, Nov. 19, 2013
- Group Rating Methodology, Nov. 19, 2013
- Key Credit Factors For The Real Estate Industry, Nov. 19, 2013
- Methodology: Industry Risk, Nov. 19, 2013
- Methodology: Management And Governance Credit Factors For Corporate Entities And Insurers, Nov. 13, 2012
- Use Of CreditWatch And Outlooks, Sept. 14, 2009

Ratings List

Ratings Affirmed

Befimmo S.A.	
Corporate Credit Rating	BBB/Stable/A-2
Senior Unsecured	BBB

Additional Contact:
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Certain terms used in this report, particularly certain adjectives used to express our view on rating relevant factors, have specific meanings ascribed to them in our criteria, and should therefore be read in conjunction with such criteria. Please see Ratings Criteria at www.standardandpoors.com for further information. Complete ratings information is available to subscribers of RatingsDirect at www.globalcreditportal.com and at spcapitaliq.com. All ratings affected by this rating action can be found on the S&P Global Ratings public website at www.standardandpoors.com. Use the Ratings search box located in the left column. Alternatively, call one of the following S&P Global Ratings numbers: Client Support Europe (44) 20-7176-7176; London Press Office (44) 20-7176-3605; Paris (33) 1-4420-6708; Frankfurt (49) 69-33-999-225; Stockholm (46) 8-440-5914; or Moscow 7 (495) 783-4009.