S&P Global
Ratings

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Summary:
Alstria Office REIT-AG

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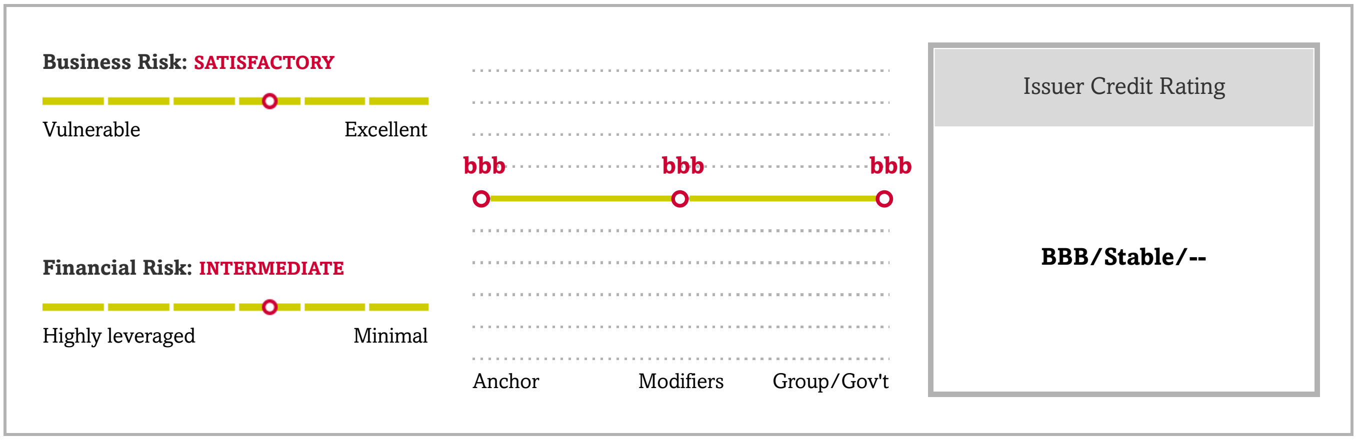

Rationale

Business Risk	Financial Risk
• Solid portfolio size, with about €3.5 billion of office assets in mainly German metropolitan cities with good macroeconomic fundamentals. • Consistent strategy of long-term property holding with average lease maturities of around five years, in line with industry standard. • Some tenant concentration in the City of Hamburg, although tenants are spread across several lease agreements. • Relatively high vacancy rate of about 11%, excluding buildings vacant for renovation needs.	• Moderate leverage, with S&P Global Ratings-adjusted debt to debt plus equity of around 35%. • Robust EBITDA interest coverage ratio of around 4.5x. • Strong liquidity, supported by the solid cash position, absence of short-term debt maturities, and undrawn committed credit lines.

Outlook

S&P Global Ratings' stable outlook on Alstria Office REIT-AG reflects that the company's property portfolio will generate steady cash flows over the next 24 months. Our view is based on the resilient operating performance of Alstria's office buildings, which are mostly in metropolitan areas across Germany and enjoy good economic growth prospects. The outlook also captures our assumption of stable occupancy levels over our 2018-2020 forecast period.

We forecast EBITDA interest coverage will remain strong at close to 4.5x over the next two years and debt to debt plus equity of about 35%-37%, in line with the company's strategy. We also expect the company to maintain a stable debt maturity profile.

Downside scenario

We could consider lowering the rating if Alstria's vacancy rate increased further to above 11%, excluding vacant buildings for renovation needs, on a sustainable basis, or if the company experienced further concentration to single tenants.

We would also view negatively if the Alstria deviates from its stated leverage policy, with EBITDA interest coverage decreasing below 2.5x and debt to debt plus equity higher than 50%.

Upside scenario

We could raise the rating if Alstria's leverage dropped, with the ratio of debt to debt plus equity falling below 35%, while EBITDA interest coverage remained comfortably at 3x or higher. Such an improvement could come from a material debt reduction or significant portfolio revaluation.

A positive action may also stem from an increase in overall portfolio size and a marked reduction in the portfolio vacancy to 5% or below.

Our Base-Case Scenario

Assumptions

- Approximately 1.5%-2.0% like-for-like rental income growth over the next 12-24 months, stemming from positive GDP growth of about 2.4% in 2018 and 1.9% in 2019, low growth in the consumer price index of 1.7% in 2018 and 1.8% in 2019, while occupancy levels are assumed to remain stable with EPRA (European Public Real Estate Association) occupancy of around 90% (excluding vacant premises for renovation and refurbishment needs);
- Annual net rental income of about €165 million for 2018, reflecting some rental losses from departing tenants in 2018, partly offset by new leases signed during the year
- Overall stable portfolio size with limited asset rotation;
- 0%-3% like-for-like portfolio revaluation in next 12 months; and
- Cost of debt to remain stable at around 2% with limited refinancing needs until 2021.

Key Metrics

	2017A	2018E	2019E
EBITDA margin (%)	86.5	About 85.0	About 85.0
EBITDA/interest (x)	4.2	4.2-4.4	4.2-4.4
Debt to debt plus equity (%)	41.5	35.0-37.0	35.0-37.0

A--Actual. E--Estimate

Company Description

Alstria Office REIT-AG is one of the largest listed office real estate company in Germany. The company is focused on the acquisition and management of office properties across Germany with locations in mainly metropolitan areas such as Hamburg, Frankfurt, Düsseldorf, Berlin, or Stuttgart. Alstria's portfolio combines 116 assets at about €3.5 billion (as of June 2018).

Alstria became the first German REIT in 2007 and is listed in the SDAX.

Business Risk

Alstria's business risk profile reflects the company's market standing as one of the largest-listed office player in Germany, as well as its solid scale and scope with portfolio value as of June 30, 2018, of about €3.5 billion, comprising 116 properties. The buildings are mainly office assets located around metropolitan areas in Germany, such as Hamburg (30% of the portfolio value), the Rhine-Ruhr region (29%), the Rhine-Main region (20%), Stuttgart (13%), and Berlin (5%).

Most of Alstria's assets are in or near city centers where demand for office assets tends to be stronger. They have access to good infrastructure and positive rental growth prospects thanks to low unemployment and solid tenant demand for office spaces. Although Alstria is one of the largest-listed office player in Germany, its market share remains limited because the German real estate market is highly fragmented. We assess Alstria's office buildings as being of average quality. The properties require some renovation and refurbishment of approximately €40 million-€60 million annually.

The portfolio is characterized by its relatively firm average lease length of close to five years, supported by its exposure to tenants from the public sector. Our assessment of Alstria's business risk is further supported by the absence of speculative development activities in the company's portfolio, which limits the risk of revenue volatility. We anticipate limited asset rotation for Alstria in the next few years, due to the absence of well-priced office buildings in the market.

Alstria's tenant base is somewhat concentrated on the City of Hamburg and Daimler AG (A/Stable/A-1), which account for approximately 12% each of total annual rental income. We understand that leases with the City of Hamburg are spread over 20 lease agreements, limiting the risk of cash flow volatility. It's third-largest tenant GMG Generalmietgesellschaft mbH (part of Deutsche Telekom AG; BBB+/Watch Neg/A-2) accounts for 8% of total annual rental income, making it to a concentration to the top-three tenants of 32% of total annual rental income.

Compared with most European office players in a stronger business risk category, Alstria remains small in size. The company reported an EPRA occupancy ratio of 89.0% as of June 30, 2018 (excluding surface under renovation), which is somewhat below that reported by most rated peers in the European office market.

Alstria's like-for-like property value growth will remain flat in the next 12-24 months, in our view. Although office property prices are rising in some major cities in Germany, we still foresee some oversupply in cities like Frankfurt and in the Rhine-Ruhr area.

Peer comparison

Table 1

Alstria Office REIT-AG -- Peer Comparison

Industry Sector: Real Estate Investment Trust or Company

	Alstria Office REIT-AG	Derwent London PLC	Covivio	Aroundtown S.A.	Befimmo S.A.
Rating as of Sept. 20, 2018	BBB/Stable/--	BBB+/Stable/A-2	BBB/Positive/A-2	BBB+/Stable/A-2	BBB/Stable/A-2
	--Fiscal year ended Dec. 31, 2017--				
(Mil. €)					
Revenues	172.3	196.9	588.9	713.5	143.2
EBITDA	150.4	156.0	493.2	462.0	117.7
Funds from operations (FFO)	115.1	111.1	323.8	304.3	97.2
Interest Expense	36.2	41.0	162.0	103.8	19.5
Net income from cont. oper.	297.0	353.8	914.1	1,282.6	136.1
Capital expenditures	59.4	180.9	627.9	110.2	40.5
Dividends paid	79.7	136.2	324.7	154.6	89.3
Cash and short-term investments	102.1	98.0	1,089.0	841.6	0.3
Debt	1,385.7	765.4	5,849.3	6,048.8	995.8
Equity	1,954.7	4,724.1	6,363.0	6,914.0	1,448.5
Debt and equity	3,340.4	5,489.5	12,212.3	12,962.8	2,444.3
Valuation of Investment Property	3,392.1	5,464.3	12,784.0	12,275.5	2,494.4
Adjusted ratios					
EBITDA margin (%)	87.3	79.2	83.8	64.7	82.2
Return on capital (%)	5.6	2.9	4.3	4.2	4.8
EBITDA interest coverage (x)	4.2	3.8	3.0	4.5	6.0
Debt/EBITDA (x)	9.2	4.9	11.9	13.1	8.5
Total debt/debt plus equity (%)	41.5	13.9	47.9	46.7	40.7

Financial Risk

Our assessment of Alstria's financial risk profile remains unchanged despite its recent larger-than-expected reduction in leverage, with S&P Global Ratings-adjusted ratio of debt to debt plus equity at 35% as of June 30, 2018. In the first half of 2018, the company successfully executed a capital increase with gross proceeds of about €193 million and, as expected, the conversion of its 2013/2018 convertible bond of €73.5 million into shares. The average cost of debt remained stable at 1.8%.

We expect the S&P Global Ratings-adjusted ratio of EBITDA interest coverage to remain strong at above 4x in the next 12-24 months, supported by the low average cost of debt and that over 90% of interest cost are fixed or hedged.

In addition, Alstria's ratio of debt to debt plus equity will likely remain conservatively at approximately 35%-37% for the next 12-24 months, in line with the company's strategy.

Financial summary

Table 2

Alstria Office REIT-AG--Rolling 12 Months Data					
Industry Sector: Real Estate Investment Trust or Company					
(Mil. €)	**June 2018**	**March 2018**	**December 2017**	**September 2017**	**June 2017**
Revenues	172.4	173.7	172.3	170.9	172.2
EBITDA	149.1	152.8	150.4	161.4	158.2
Funds from operations (FFO)	116.0	117.4	115.1	125.9	121.8
Interest Expense	34.0	36.2	36.2	36.2	37.2
Net income from continuing operations	280.9	298.4	297.0	210.0	202.2
Capital expenditures	60.7	60.1	59.4	31.9	31.7
Dividends paid	92.2	79.7	79.7	79.7	79.7
Cash and short-term investments	178.1	265.6	102.1	59.6	51.8
Debt	1,212.8	1,129.5	1,385.7	1,442.4	1,442.8
Equity	2,218.4	2,278.2	1,954.7	1,761.5	1,728.1
Debt and equity	3,431.3	3,407.7	3,340.4	3,203.9	3,170.8
Valuation of Investment Property	3,481.8	3,459.2	3,392.1	3,169.7	3,210.8
Adjusted ratios					
EBITDA margin (%)	86.5	87.9	87.3	94.4	91.9
Return on capital (%)	4.6	5.7	5.6	5.9	5.8
EBITDA interest coverage (x)	4.4	4.2	4.2	4.5	4.3
Debt/EBITDA (x)	8.1	7.4	9.2	8.9	9.1
Debt/debt and equity (%)	35.3	33.1	41.5	45.0	45.5

Liquidity

We continue to view Alstria's liquidity as strong. This is based on its ratio of liquidity sources to uses of well above 1.5x over the next 12 months as of June 30, 2018. The strong liquidity is supported by the absence of large debt maturities for the next two to three years, and the company's solid cash balance and available undrawn committed revolving credit lines.

We expect Alstria will maintain ample headroom (greater than 15%) under the financial covenants in its debt agreements.

Listed below, our forecast for Alstria's liquidity sources and uses for the 12 months as of June 30, 2018.

Principal Liquidity Sources

- Unrestricted cash balances of about €178 million and undrawn committed revolving credit facility of €100 million, maturing in more than 12 months;

- Our forecast of cash funds from operations of approximately €120 million-€140 million; and
- Proceeds from committed asset sales of around €26 million for the properties sold in Eschborn and Hamburg earlier this year.

Principal Liquidity Uses

- Annual capital expenditures of about €50 million-€60 million for renovation and refurbishment, of which we understand most of it is not committed;
- Committed acquisitions of approximately €33 million, relating to a property in Frankfurt and Wiesbaden; and
- Estimated cash dividend payment of around €95 million in second-quarter 2019.

Ratings Score Snapshot

Issuer Credit Rating

BBB/Stable/--

Business risk: Satisfactory

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

Financial risk: Intermediate

- **Cash flow/Leverage:** Intermediate

Anchor: bbb

Modifiers

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

Reconciliation

Table 3

Reconciliation Of Alstria Office REIT-AG Reported Amounts With S&P Global Ratings' Adjusted Amounts (Mil. €)

	--Fiscal year ended Dec. 31, 2017--			
Alstria Office REIT-AG reported amounts				
	Debt	**EBITDA**	**Operating income**	**EBITDA**
Reported	1,468.4	167.0	348.0	167.0
S&P Global Ratings' adjustments				
Interest expense (reported)	--	--	--	(36.2)
Interest income (reported)	--	--	--	0.8
Current tax expense (reported)	--	--	--	--
Surplus cash	(102.1)	--	--	--
Share-based compensation expense	--	1.1	--	1.1
Non-operating income (expense)	--	--	28.9	--
Debt - Equity component of convertible debt	7.2	--	--	--
Debt - Issuance cost	12.2	--	--	--
EBITDA - Gain/(Loss) on disposals of PP&E	--	(19.7)	(19.7)	(19.7)
EBITDA - Other	--	2.0	2.0	2.0
D&A - Asset Valuation gains/(losses)	--	--	(181.5)	--
Total adjustments	(82.7)	(16.6)	(170.3)	(52.0)
S&P Global Ratings' adjusted amounts				
	Debt	**EBITDA**	**EBIT**	**Funds from operations**
Adjusted	1,385.7	150.4	177.7	115.1

Issue Ratings--Subordination Risk Analysis

Capital structure

As of June 30, 2018, Alstria's capital structure comprises about 17% secured debt, mainly mortgaged bank loans and 83% unsecured debt, including mainly senior unsecured bonds and promissory notes.

Unsecured bonds are issued under Alstria Office REIT-AG.

Analytical conclusions

We assess the issue ratings on the company's senior unsecured bonds at 'BBB', in line with the issuer credit rating. This is because the company's exposure to secured debt is limited (secured debt to total fair value assets is below 10%).

Related Criteria

- Criteria - Corporates - General: Methodology And Assumptions: Liquidity Descriptors For Global Corporate Issuers, Dec. 16, 2014
- Criteria - Corporates - General: Corporate Methodology: Ratios And Adjustments, Nov. 19, 2013

- Criteria - Corporates - Industrials: Key Credit Factors For The Real Estate Industry, Nov. 19, 2013
- General Criteria: Group Rating Methodology, Nov. 19, 2013
- Criteria - Corporates - General: Corporate Methodology, Nov. 19, 2013
- General Criteria: Use Of CreditWatch And Outlooks, Sept. 14, 2009

Business And Financial Risk Matrix

	Financial Risk Profile					
Business 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-

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