S&P Global
Ratings

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Alstria Office REIT-AG

Primary Credit Analyst:
Yilin Li, Frankfurt + 49 693 399 9107; yilin.li@spglobal.com

Secondary Contact:
Nicole Reinhardt, Frankfurt + 49 693 399 9303; nicole.reinhardt@spglobal.com

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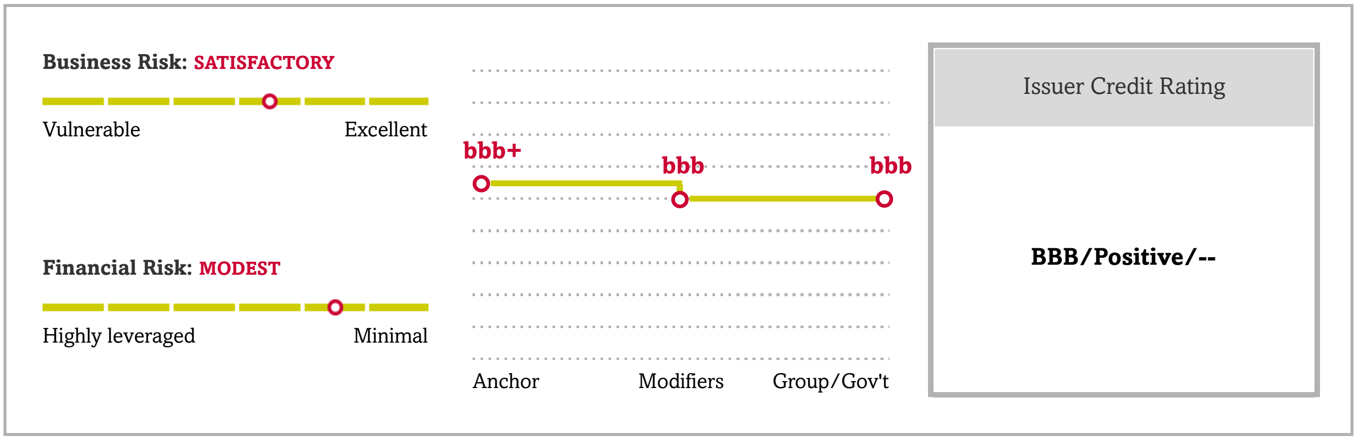
Alstria Office REIT-AG



Credit Highlights

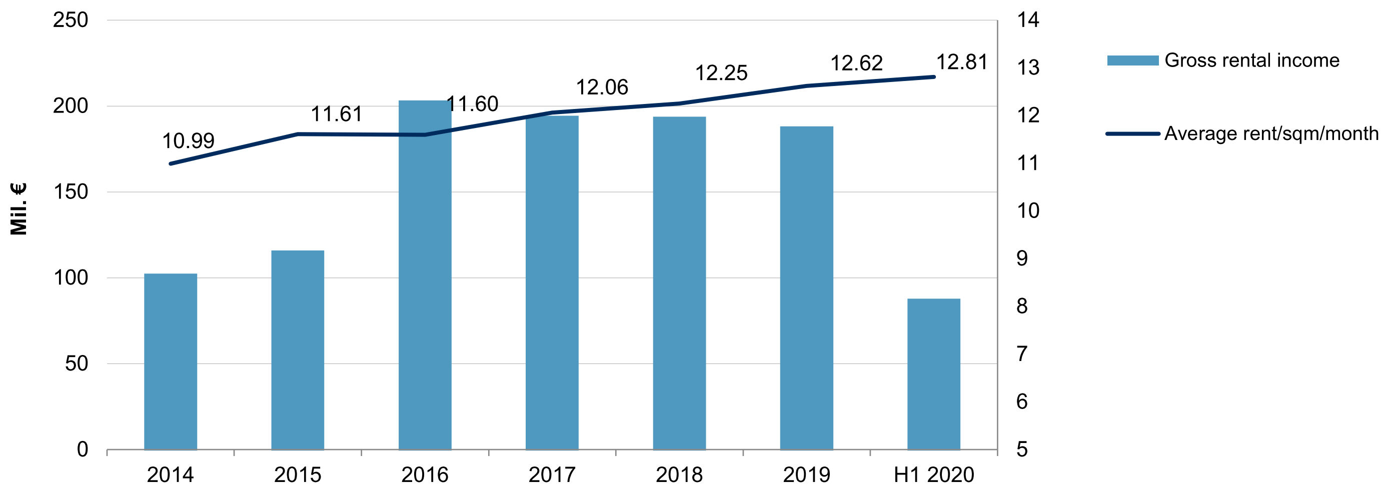
Overview

Key strengths	Key risks
Strong portfolio, with about €4.4 billion of office assets mainly in German metropolitan cities with good macroeconomic fundamentals.	100% exposure to the office segment, which we view as more volatile and cyclical than the residential sector, and where medium-to-long term demand trends remain uncertain considering the COVID-19 pandemic.
Consistent strategy of long-term property holding with average lease maturities of around six years, in line with industry standards.	Relatively high vacancy rate (about 8%) compared with that of other rated investment-grade peers, excluding buildings vacant for renovation needs.
Relatively low leverage, with expected S&P Global Ratings-adjusted debt to debt plus equity of 30%-33% for the next 12-24 months.	Some tenant concentration to the City of Hamburg and Daimler AG, although tenant contracts are spread across several lease agreements.
Robust EBITDA interest coverage ratio of 4.5x rolling last 12 months as of June 30, 2020, which we expect will remain at similar levels.	

S&P Global Ratings expects the COVID-19 pandemic will have only a limited impact on Alstria Office REIT-AG's (Alstria's) rental income in 2020, although the future of office demand is unclear. Alstria's operational performance in 2020 should remain stable overall, despite headwinds from the COVID-19 pandemic. We understand Alstria was able to collect about 90% of its monthly rent during the second quarter, and payments since July are now broadly back at pre-pandemic levels. Nonetheless, we anticipate an up to 3% decline of like-for-like rental income for the year, mainly because we assume some rent deferrals will not be collected, and new leases and lease-ups will not fully compensate lease expirations. Overall, we remain cautious about the medium-to-long-term demand and market rent growth for office properties in Germany as a result of increased remote working capacities for many tenants, as well as a weakening macroeconomic environment, particularly in the auto and manufacturing sectors. However, Germany has proved more resilient than other European countries.

Chart 1

Alstria Office REIT AG: Rental Income



Source: S&P Global Ratings.

We believe Alstria will continue to keep its leverage low, supporting our positive outlook on the company. Alstria has maintained its reported loan-to-value (LTV) ratio below 35% since end-2018, translating into S&P Global Ratings-adjusted debt to debt plus equity of below 35%-36%. Including a reported negative portfolio revaluation of €88 million for the first six months of 2020, reflecting generally prudent assumptions compared with the transaction market and peers, the company's S&P Global Ratings-adjusted debt to debt plus equity remained low at 26.8% as of June 30, 2020. Although Alstria's financial policy does not state any specific LTV target, we expect the LTV ratio will remain below 35%. Our positive outlook on the company reflects our belief that Alstria should withstand any further pressure from the COVID-19 pandemic and maintain its strong credit metrics. However, in the light of current market uncertainties, we remain cautious about the re-leasing of properties for which lease maturities are upcoming, as well as rent levels for new lettings and further valuation impacts.

Alstria demonstrated solid access to debt capital markets during the peak of the pandemic, further strengthening its liquidity profile. In June 2020, Alstria issued €350 million of senior unsecured notes at a coupon rate of 1.5%, maturing in 2025. The proceeds will serve for general corporate purposes, mainly acquisitions of real estate, and/or refinancing of existing debt. We understand demand was very strong, with order books reaching about €1.7 billion, showing the company's access to debt capital markets at attractive pricing in the middle of the pandemic. Including this issuance, the company's cost of debt remains stable at 1.5% as of June 30, 2020, with an average debt maturity of 4.6 years.

Outlook: Positive

The positive outlook reflects the possibility that Alstria will maintain strengthened credit ratios over the next few quarters, assuming a disciplined financial policy and a well-balanced asset rotation strategy. This includes an EBITDA interest coverage ratio of over 4x, and a debt-to-debt-plus-equity ratio sustainably well below 35%.

We expect the company's property portfolio will continue to generate stable cash flow thanks to its improved occupancy rate and lease maturity length, and its focused investment strategy on centrally located offices within German metropolitan cities.

Downside scenario

We could revise the outlook to stable if Alstria's leverage increases to previous levels, most likely following larger-than-anticipated debt-funded acquisitions or higher-than-anticipated renovation projects. We would also revise the outlook to stable if debt to debt plus equity rose to 35% or above.

Upside scenario

We could raise the issuer credit rating if Alstria maintains its debt-to-debt-plus-equity ratio well below 35% on a permanent basis, with EBITDA interest coverage remaining well above 4.0x. An upgrade would also be contingent on the company's ability to demonstrate healthy organic rental income growth and stable-or-improving occupancy rates in its office portfolio throughout the next quarters, demonstrating resilience to the impact from the COVID-19 pandemic

Our Base-Case Scenario

Assumptions

- GDP decline in Germany of 5.4% in 2020 in light of the pandemic, before rebounding to growth of 4.7% in 2021, with unemployment rising to about 4.5% over the next year.
- Flat consumer price index growth in Germany in 2020, before rebounding to positive 1.1% in 2021.
- Overall like-for-like rental income decrease of close to 3%, with stable occupancy rates in 2020, incorporating potential rent concessions to tenants affected by the coronavirus pandemic. We expect the company will generate flat to slightly positive like-for-like rental income growth in the following years.
- Acquisition of up to €350 million in the next 12 months, financed mainly by the company's recent bond issuance.
- Annual capital expenditure (capex) investments of €150 million-€200 million in the next couple of years.
- Marginal dip in like-for-like revaluation for Alstria's properties for full-year 2020, following its first-half results, and flat valuation result the following year.
- Stable cost of debt at about 1.5%.

Key metrics

Alstria Office REIT-AG Key Metrics*

	--Fiscal year end Dec. 31--				
(Mil. €)	**2018a**	**2019a**	**2020e**	**2021f**	**2022f**
Net rental income	169.1	162.9	153-156	170-173	185-188
EBITDA	143.7	139.1	130-133	144-147	157-160
EBITDA interest coverage (x)	4.8	5.2	4.5-4.8	5.5-6.0	5.5-6.0
Debt to Debt plus Equity (%)	31.2	27.7	28.0-30.0	30.0-34.0	30.0-33.0
Debt to EBITDA (x)	8.5	8.8	9.0-10.0	10.0-11.0	9.5-10.5

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

New acquisitions could push the company's leverage up to 34%. After a record-low reported LTV of 26.3%, corresponding to S&P Global Ratings-adjusted ratio of debt to debt plus equity of 26.8%, we anticipate that it is likely to approach 30% by year-end 2020. Our forecast incorporates the expected dividend payment and capex investment for the second half of the year, as well as our assumption that revaluation of Alstria's portfolio would fall slightly. In 2021, we believe leverage could rise further, cautiously assuming that Alstria uses the €350 million bond proceeds mainly for acquisitions.

EBITDA is likely to dip this year compared with 2019, with future growth depending on transaction activities. For 2020, we assume EBITDA will decline 5%-7% compared with 2019, mainly due to Alstria's continued disposals of noncore assets throughout 2019 and the beginning of this year. While we forecast that re-lettings and new leases will be renegotiated at less favorable conditions to pre-COVID-19 levels, we believe the company's absolute EBITDA base may expand on the back of portfolio growth, which will be reflected in 2021 financial results at the earliest. In addition, the expected early repayment of the 2021 bond by end 2020 (due in March 2021 with a coupon of 2.25%), will likely benefit the company's EBITDA interest coverage in following years.

Company Description

Table 1

Alstria Office REIT AG Portfolio Summary

Segment Focus	**Office**
Total Portfolio Value (€ Bn)	4.4
Total Number of Assets	111
Current Average EPRA Vacancy (%)	7.9
Average Lease Maturity (Yrs.)	6.4
Current Valuation Yield (%)	4.6

Source: Company's report as of June 30, 2020.

Alstria is one of the largest listed office real estate companies in Germany. The company is focused on the acquisition and management of office properties across Germany, with locations mainly in or close to metropolitan areas such as Hamburg, Frankfurt, Düsseldorf, Berlin, or Stuttgart. Alstria's portfolio combines 111 assets at about €4.4 billion (as of June 30, 2020).

Alstria became the first German REIT in 2007 and is listed on the MDAX. The company's free float is 100% according to the definition of Deutsche Börse AG.

Peer Comparison

Table 2

Alstria Office REIT-AG--Peer Comparison

Industry sector: Real estate investment trust or company

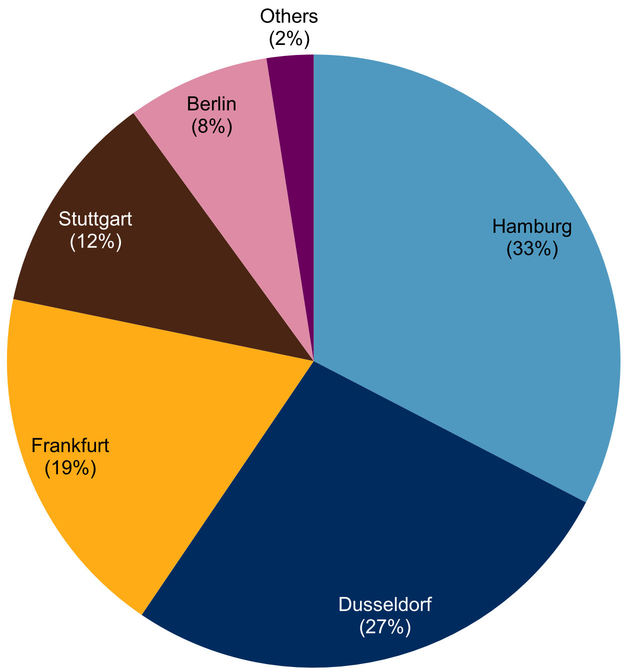
	Alstria Office REIT-AG	Aroundtown S.A.	Societe Fonciere Lyonnaise S.A.	CPI Property Group SA	Immofinanz AG
Ratings as of Oct. 27, 2020	BBB/Positive/--	BBB+/Stable/A-2	BBB+/Stable/A-2	BBB/Negative/--	BBB-/Stable/--
	--Rolling 12 months ended June 30, 2020--				
(Mil. €)					
Revenue	158.6	1,278.4	192.0	466.8	209.2
EBITDA	130.2	837.5	168.4	292.0	155.2
Funds from operations (FFO)	105.3	460.8	123.7	198.3	93.9
Interest expense	28.9	227.9	29.2	93.8	70.4
Cash flow from operations	121.6	483.6	118.7	215.1	112.6
Capital expenditure	142.1	287.3	92.0	330.8	235.5
Dividends paid	0.0	209.5	124.3	18.8	0.0
Cash and short-term investments	619.6	2,709.9	270.0	310.5	339.5
Debt	1,149.8	12,838.0	1,937.2	4,801.5	2,536.6
Equity	3,143.4	15,280.0	5,009.4	4,785.7	2,781.7
Debt and equity	4,293.2	28,117.9	6,946.6	9,587.2	5,318.3
Valuation of investment property	4,363.6	26,697.6	7,124.7	9,656.8	5,174.6
Adjusted ratios					
Annual revenue growth (%)	(4.6)	23.5	(1.7)	(0.1)	16.0
EBITDA margin (%)	82.1	65.5	87.7	62.6	74.2
Return on capital (%)	2.9	3.7	2.4	2.7	3.7
EBITDA interest coverage (x)	4.5	3.7	5.8	3.1	2.2
Debt/EBITDA (x)	8.8	15.3	11.5	16.4	16.3
FFO/debt (%)	9.2	3.6	6.4	4.1	3.7
Debt/debt and equity (%)	26.8	45.7	27.9	50.1	47.7

Business Risk: Satisfactory

The rating reflects the company's market standing as one of the largest-listed office players in Germany, as well as its solid scale and scope. Its portfolio comprises 111 properties, valued at about €4.4 billion as of June 30, 2020. The buildings are mainly office assets in metropolitan areas in Germany, such as Hamburg (32.6% of the portfolio value), Düsseldorf (26.8%), Frankfurt am Main (18.8%), Stuttgart (11.8%), and Berlin (7.5%).

Chart 2

Alstria Office REIT AG: Geographic Diversity
% of Portfolio value: June 2020



Source: S&P Global Ratings.

Most of Alstria's assets are in or near city centers, where demand for office space tends to be stronger. They have access to good infrastructure and positive rental growth prospects due to low unemployment and solid tenant demand. Although Alstria is one of the largest listed office players in Germany, its market share remains limited because the German real estate market is highly fragmented. We assess the asset quality of the company's office building as average and in line with the overall German office market. The properties require some renovation and refurbishment measures, with annual capex estimated at approximately €100 million.

The portfolio is characterized by its relatively long average lease length of close to 6.4 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.

Alstria's tenant base is somewhat concentrated on the City of Hamburg and Daimler AG (BBB+/Negative/A-2), which each account for approximately 11.5% of total annual rental income. That said,we view the exposure to the City of Hamburg as public sector tenant as favorable, and understand that leases with Daimler are spread over eight lease agreements, limiting the risk of cash flow volatility. In addition, the 10-largest tenants represent a concentration of 42% of annual rental income.

The company reported an EPRA (European Public Real Estate Association) vacancy ratio of 7.9% as of June 30, 2020 (excluding surface under renovation), which is somewhat above that reported by most rated investment-grade peers in the European office market, but is in line with the company's asset-recycling strategy. We note, however, slightly improved occupancy levels in first-half 2020, despite the challenges due to the lockdown in second-quarter 2020. Alstria has higher geographic, segment, and tenant concentration compared with those of peers rated a notch above. However, we believe it enjoys exposure to top metropolitan cities of Germany, and good growth prospects and its position among the top players in the German office market partially mitigate the risk.

Although the hit from temporary office closures and rent concessions due to fallout from the COVID-19 pandemic has been moderate so far, we believe office players may face difficulty in addressing their next lease maturities because of softening office demand in some markets. We note that Alstria has a moderate amount of lease maturities in the next 12-24 months, accounting for about 10% of annualized contractual rental income. We remain cautious about the re-leasing of properties for which lease maturities are upcoming, as well as rent levels for new lettings.

Moreover, occupiers may need less space as remote working increases, companies take cost-saving measures, and if economies only rebound slowly. These factors could weigh not only on occupancy, but also on market rents--the extent of which remains unknown in the absence of a significant number of leasing transactions. We believe Alstria's exposure to public tenants, representing 26% of total annual rental income, may to some extent offset some of those risks, given their long-term lease contracts and somewhat limited remote working capabilities, at least for the short term.

Financial Risk: Modest

Our assessment of Alstria's financial risk profile reflects significant improvement in the company's credit metrics in recent years. We expect they will stay strong over the next two-to-three years, likely as a result of the company's following a disciplined financial policy and a well-balanced asset rotation strategy over the next 24 months.

The company's S&P Global Ratings-adjusted ratio of debt to debt plus equity has remained low, at 26.8% as of June 30, 2020, compared with 29.6% on the same date in 2019. This mainly reflects the sale of noncore assets, partly mitigated by some negative portfolio revaluations. Following the €350 million bond issuance in June 2020, the average cost of debt has remained stable at 1.5%, with an average debt maturity of about 4.6 years. Alstria has proven solid access to debt capital markets during the peak of the pandemic in second-quarter 2020 at an attractive yield. The low interest cost will sustain the company's capacity to cover its interest charges, with EBITDA interest coverage expected to remain well above 4x.

While leverage is still strong thanks to the successful liability management in the recent years, our assessment incorporates potential debt-funded acquisitions and renovation projects that would push leverage closer to 35%. However, we believe that, at current levels, the company has headroom under the rating to sustain strong ratios.

Although Alstria's management financial policy does not include any LTV target, we expect debt to debt plus equity will stay at 30%-35% over the next 12-24 months. Our forecast captures the company's pipeline of renovation projects and anticipated asset rotation activity, including the possible use of the €350 million bond proceeds for acquisitions in

2021, mixed with some additional equity. We would, however, revise the outlook to stable if any larger-than-anticipated debt-funded acquisitions or higher-than-expected capex investment lead to an LTV ratio of 35% or above.

We believe Alstria's leverage is slightly higher than those of peers that we assess in the modest financial risk category such as Prologis European Logistics Fund (A-/Stable/A-2), and reflect this in the ratings. We think Alstria's leverage could remain at the weaker end of its financial category, meaning close to 35%. In addition, compared with other 'BBB+' rated companies, the company has a relatively small portfolio.

Financial summary

Table 3

Alstria Office REIT-AG -- Financial Summary Quarterly

Industry sector: Real estate investment trust or company

	June 2020	March 2020	December 2019	September 2019	June 2019
(Mil. €)					
Revenue	38.3	37.8	40.0	42.5	40.6
EBITDA	34.5	31.6	34.1	30.0	31.8
Funds from operations (FFO)	24.2	23.5	28.3	29.3	21.7
Interest expense	7.6	7.4	6.7	7.3	6.6
Cash flow from operations	24.6	25.6	36.4	34.9	28.5
Capital expenditure	36.2	34.3	44.2	27.6	22.1
Dividends paid	0.0	0.0	(1.9)	1.9	92.3
Cash and short-term investments	619.6	349.7	298.2	297.7	107.2
Debt	1,149.8	1,161.6	1,219.3	1,217.7	1,209.5
Equity	3,143.4	3,204.4	3,175.6	2,896.5	2,872.1
Debt and equity	4,293.2	4,366.0	4,394.9	4,114.2	4,081.6
Valuation of investment property	4,363.6	4,436.6	4,458.2	4,172.1	4,134.8
Adjusted ratios					
Revenue growth, past 12 months (%)	(4.6)	(3.8)	(3.6)	(3.4)	(3.6)
EBITDA margin (%)	82.1	79.2	85.4	81.5	86.3
Return on capital (%)	2.9	2.9	3.2	3.2	3.6
EBITDA interest coverage (x)	4.5	4.6	5.2	4.9	5.3
Debt/EBITDA (x)	8.8	9.1	8.8	9.1	8.4
FFO/debt (%)	9.2	8.8	9.4	10.0	9.7
Debt/debt and equity (%)	26.8	26.6	27.7	29.6	29.6

Reconciliation

Table 4

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

	--Rolling 12 months ended June 30, 2020--									
Alstria Office REIT-AG reported amounts										
	Debt	**Shareholders' equity**	**Revenue**	**EBITDA**	**Operating income**	**Interest expense**	**S&P Global Ratings' adjusted EBITDA**	**Cash flow from operations**	**Dividends**	**Capital expenditure**
Reported	2,013.5	3,143.4	158.6	131.7	297.5	28.9	130.2	121.6	--	142.1
S&P Global Ratings' adjustments										
Cash interest paid	--	--	--	--	--	--	(24.9)	--	--	--
Reported lease liabilities	5.6	--	--	--	--	--	--	--	--	--
Accessible cash and liquid investments	(869.3)	--	--	--	--	--	--	--	--	--
Share-based compensation expense	--	--	--	2.2	--	--	--	--	--	--
Nonoperating income (expense)	--	--	--	--	0.7	--	--	--	--	--
EBITDA: Gain/(loss) on disposals of PP&E	--	--	--	(3.7)	(3.7)	--	--	--	--	--
Depreciation and amortization: Asset valuation gains/(losses)	--	--	--	--	(167.0)	--	--	--	--	--
Interest expense: Other	--	--	--	--	--	0.1	--	--	--	--
Total adjustments	(863.6)	0.0	0.0	(1.5)	(170.0)	0.1	(24.9)	0.0	0.0	0.0
S&P Global Ratings' adjusted amounts										
	Debt	**Equity**	**Revenue**	**EBITDA**	**EBIT**	**Interest expense**	**Funds from operations**	**Cash flow from operations**	**Dividends**	**Capital expenditure**
Adjusted	1,149.8	3,143.4	158.6	130.2	127.5	28.9	105.3	121.6	--	142.1

Liquidity: Strong

We continue to view Alstria's liquidity as strong, based on the company's ratio of liquidity sources to uses of above 1.5x over the next 12 months as of June 30, 2020. The strong liquidity is supported by Alstria's cash balance, its reserved bond proceeds from the issuance of €350 million in June 2020, and available undrawn committed revolving credit lines.

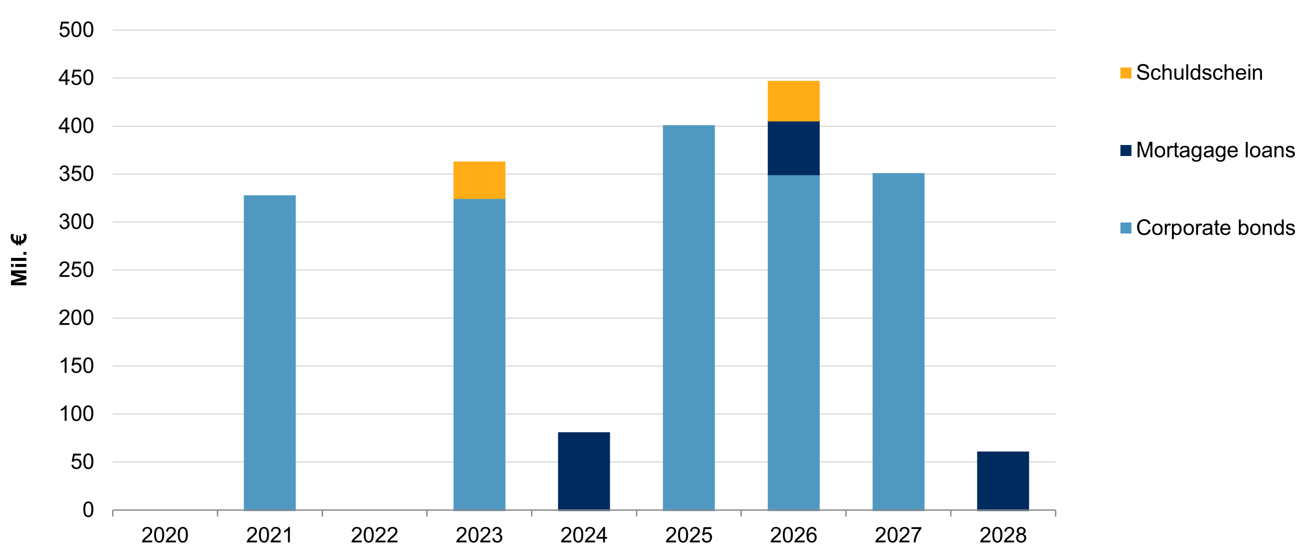
Principal Liquidity Sources	Principal Liquidity Uses
• Unrestricted cash balances of about €620 million; • About €250 million of cash deposits reported as financial assets, which we understand would be released to cash; • Undrawn committed revolving credit facility of €100 million, maturing in more than 12 months; • Our forecast of cash funds from operations of €110 million-€120 million; and • Proceeds from committed asset sales of about €44 million.	• Short-term debt maturities of about €335 million; • Annual committed capex of €100 million-€120 million for renovation and refurbishment; and • Estimated cash dividend payment of about €92 million in third-quarter 2020.

Debt maturities

The average remaining debt maturity was 4.6 years as of June 30, 2020.

Chart 3

Alstria Office REIT AG: Debt Maturities
As of June 30, 2020



Source: S&P Global Ratings.

Covenant Analysis

We understand that Alstria has financial covenants for its existing debt. We estimate that the headroom under these covenants is adequate (more than 15%).

Issue Ratings - Subordination Risk Analysis

Capital structure

As of June 30, 2020, Alstria's capital structure comprised about 11% secured debt, mainly mortgaged bank loans; and 89% unsecured debt, including mainly senior unsecured bonds and promissory notes.

Analytical conclusions

The issue ratings on the company's senior unsecured bonds are '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%).

Ratings Score Snapshot

Issuer Credit Rating

BBB/Positive/--

Business risk: Satisfactory

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

Financial risk: Modest

- **Cash flow/leverage:** Modest

Anchor: bbb+

Modifiers

- **Diversification/portfolio effect:** Neutral (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:** Negative (-1 notch)

Related Criteria

- General Criteria: Group Rating Methodology, July 1, 2019
- 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
- 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: 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, Nov. 13, 2012
- General Criteria: Principles Of Credit Ratings, Feb. 16, 2011

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-

Ratings Detail (As Of October 27, 2020)*

Alstria Office REIT-AG	
Issuer Credit Rating	BBB/Positive/--
Senior Unsecured	BBB
Issuer Credit Ratings History	
02-Sep-2019	BBB/Positive/--
24-Nov-2015	BBB/Stable/--

*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.

Additional Contact:
Industrial Ratings Europe; Corporate_Admin_London@spglobal.com