

Research Update:

German Real Estate Company Alstria Outlook Revised To Negative On Tight Credit Metrics; 'BBB-' Ratings Affirmed

May 9, 2023

Rating Action Overview

- The credit metrics of Alstria Office REIT-AG (Alstria), including the holding company's debt, for the first quarter of this year were weaker than our rating thresholds, with S&P Global Ratings-adjusted debt to debt plus equity at 55.3% and EBITDA interest coverage ratio at 1.5x for the 12 months to March 31, 2023.
- Given the current volatile market environment, with expected further interest rate increases, potential property valuation declines, and uncertainty on the refinancing of the holding company's debt, we believe Alstria's credit metrics could deteriorate further and remain inconsistent with our rating thresholds for a longer period.
- Therefore, we revised our rating outlook on Alstria to negative from stable and affirmed our 'BBB-' ratings on the company and its senior unsecured debt.
- The negative outlook indicates that we could lower the ratings if Alstria's credit metrics do not recover within the next 12 months, with our adjusted ratio of debt to debt plus equity exceeding 55% and EBITDA interest coverage remaining continuously below 1.8x.

PRIMARY CREDIT ANALYST

Gabriel Zurita
Frankfurt
+49 6933999193
gabriel.zurita
@spglobal.com

SECONDARY CONTACT

Nicole Reinhardt
Frankfurt
+ 49 693 399 9303
nicole.reinhardt
@spglobal.com

ADDITIONAL CONTACT

Corporate and IFR EMEA
RatingsCorpIFREMEA
@spglobal.com

Rating Action Rationale

Following some negative asset revaluations for 2022 and in the first quarter of 2023, Alstria's credit metrics remained close to our downside thresholds for the current rating. For the fiscal year ended Dec. 31, 2022, Alstria reported a net negative property valuation result of about €174 million, which weakened its ratio of debt to debt plus equity to 55.2% from 54% in Sept. 30, 2022. Its EBITDA interest coverage dropped by 30 basis points to 1.7x from 2.0x over the same period. The company's first-quarter results showed that its leverage remains elevated and close to our downside thresholds for the current rating. the ratio of debt to debt plus equity was 55.3% versus our benchmark of less than 55%, and EBITDA interest coverage for the 12 months to March 31, 2023, was 1.5x compared with our threshold of 1.8x. The decline in EBITDA interest coverage

included a 10 basis-point impact due to a change in accounting for capitalized borrowing costs, which we now include in our interest expense calculation. We understand the company has not performed a quarterly valuation report, but a change in transfer tax in the state of Hamburg has reduced the property portfolio's value by about €29 million. Given the current market environment, rising interest rates, and risk of further real estate valuation corrections, we believe the company may not be able to maintain credit metrics in line with an investment-grade rating. We assume about 5% devaluation of Alstria's portfolio value in 2023 and, as a result, a temporary increase in its ratio of debt to debt plus equity beyond 55%, with stabilization in 2024. Although we assume rental income growth will remain positive, benefiting from the inflationary environment, the rising cost of debt may continue to weigh on the company's debt-servicing capacity. We forecast that EBITDA interest coverage would recover to 1.8x or higher over the next two years, but we see a risk that the ratio will remain below our rating threshold. Furthermore, we expect the ratio of debt to EBITDA to stay high at about 20x-22x. We understand that Alstria's credit metrics would be significantly stronger when excluding the holding company's debt: debt to debt plus equity would be at 44.3% rather than 55.3% and EBITDA interest coverage at 3.7x versus 1.5x as of first-quarter 2023.

Debt at the holding company elevates our adjusted credit metrics and we remain cautious about Brookfield's refinancing plan. Since the takeover of Alstria by Brookfield at the beginning of 2022, we have included the acquisition facility of €1,733 million in our adjusted debt figure for the company. This facility is on the books of the holding company, Alexandrite Lax Lux Holdings S.a.r.l. After the payment of an extraordinary dividend of €750 million in 2022, which was used to partly redeem the acquisition facility, Alstria's adjusted net debt settled at about €3.1 billion, of which €1.1 billion relates to the holding company's debt. We understand Alstria has no contractual obligation or guarantee to repay the holding company's debt. However, we continue to include it in our leverage metrics to reflect the risk of further extraordinary dividend payments or an increase in Alstria's debt to service the debt of the holding company, given the absence of other cash flow sources to the holding company. We understand the acquisition facility is due latest in January 2024 and we remain cautious about the potential refinancing plan, which may further burden Alstria's balance sheet.

We expect Alstria to continuously generate stable operational cash flow, supported by its resilient tenant base and good locations of properties. As of March 31, 2023, Alstria's portfolio yield stood at 4.2%, and like-for-like rental income growth remained positive at an estimated 1%-2%. We assume Alstria's annual like-for-like rental income growth to be 2%-3% in 2023 and 2024, benefiting from its long-term inflation-linked lease contracts and solid demand for office spaces in Germany's key cities. The company benefits from a good weighted average lease term of more than five years and exposure to public tenants, with stable and predictable long-term cash flows. For the first three months of the year, vacancy rates remained stable at 7.2% compared with 7.3% at year-end 2022, and we conservatively assume a slight increase in vacancies due to potentially delayed re-leasing in a challenging commercial real estate market. Nevertheless, Alstria has a long-standing position in Germany's office market and a good track record of attracting and retaining long-term tenants.

Alstria's good relationship with mortgage banks support its access to external funding sources, with its liquidity position remaining comfortable. In April 2023, Alstria secured mortgage financing of about €331 million for a five- to seven-year tenor, at an average margin of 137 basis points. We understand the new funding has been used to repay short-term debt of €362 million, including a €325 million senior unsecured bond that matured in April. We view the company's

access to bank financing as solid, benefiting from long-term relationships with several banks. In addition, we expect the company to generate about €100 million of cash funds from operations over the next 12 months, with no further material debt maturities over that period. As a result, we view Alstria's liquidity as adequate for the next 12 months; we do not include the holding company's debt in our estimate of liquidity uses, since that debt is nonrecourse to Alstria. Pro forma the recent refinancing, Alstria's average debt tenor is four years and the average cost of debt is 2.45% up slightly from 2.1% at year-end 2022. About 80% of Alstria's debt exposure is currently at fixed interest rates or hedged, versus 86.7% at year-end 2022. Alstria's headroom under its financial covenants remained solid as of first-quarter 2023.

Outlook

The negative outlook reflects our view that Alstria's credit metrics could deteriorate more than currently anticipated, and remain weaker than our downside thresholds for the rating. This could occur, if Alstria's property portfolio were to show steeper negative revaluation than currently assumed, if the company made debt-funded shareholder distributions, or a refinancing of the holding company's debt were to erode Alstria's credit metrics.

Downside scenario

We could lower the rating within the next 12 months if, for a prolonged basis:

- Alstria's S&P Global Ratings-adjusted debt to debt plus equity remains above 55%;
- EBITDA interest coverage remains below 1.8x; or
- Debt to annualized EBITDA materially exceeds our base-case projections.

Upside scenario

We could revise our outlook to stable if Alstria's:

- Debt to debt plus equity remains close or below 55% over our forecasted period;
- EBITDA interest coverage ratio increases back to above 1.8x; and
- Debt to annualized EBITDA remains within our base case.

An outlook revision to stable would also depend on more visibility on Brookfield's plan regarding the refinancing of the upcoming debt maturity at the holding company.

Company Description

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, and Stuttgart. Alstria's portfolio combines 107 assets with a market value of about €4.6 billion (as of March 31, 2023). Alstria became the first German REIT in 2007 and is listed on the MDAX. As of May 5, 2023, Brookfield Asset Management remained as largest shareholder with 95% ownership.

Our Base-Case Scenario

Assumptions

- Real GDP in Germany to remain unchanged in 2023, while increasing slightly by 0.9% and 1.8% in 2024 and 2025 respectively. German consumer price index to remain high at 6.3% in 2023 but slow down to 2.9% in 2024. Unemployment rate to remain broadly stable at 3.2% in 2023 and 2024.
- Positive like-for-like growth of 2%-3% over the next 12-24 months, mainly supported by solid inflation rates and stable demand for Alstria's assets, but partly offset by a slight decrease of occupancy rates.
- A potential devaluation of the property portfolio's market value of around 5% for 2023, mainly due to an increase of capitalization and interest rates.
- No significant acquisitions for the coming years.
- Annual capital expenditure (capex) of €150 million-€175 million over 2023-2024.
- €50 million-€100 million of disposals in 2023, and €200 million-€250 million annually the years after. We understand disposal proceeds will fund Alstria's capex pipeline, which may be reduced if disposals do not materialize.
- Annual cash dividends of about €30 million, representing the minimum dividend requirement by Alstria's German status as a real estate investment trust and in line with the company's strategy.
- Average cost of debt remaining at about 2.5% for 2023, including recent refinancing activities.

Key metrics

- Debt to debt plus equity will temporarily increase to 57%-58% in 2023 and to around 55% in 2024, including constant debt levels at the holding company;
- Adjusted debt to EBITDA of 20x-22x in 2023 and 2024; and
- EBITDA interest coverage to settle at 1.8x-2.0x over 2023-2024.

Ratings Score Snapshot

Issuer Credit Rating	BBB-/Negative/--
Business risk:	Satisfactory
Country risk	Very low
Industry risk	Low
Competitive position	Satisfactory
Financial risk:	Significant
Cash flow/leverage	Significant
Anchor	bbb-

Issuer Credit Rating	BBB-/Negative/--
Modifiers:	
Diversification/Portfolio effect	Neutral (no impact)
Capital structure	Neutral (no impact)
Financial policy	Neutral (no impact)
Liquidity	Adequate (no impact)
Management and governance	Fair (no impact)
Comparable rating analysis	Neutral (no impact)

ESG credit indicators: E-2, S-2, G-2

Related Criteria

- General Criteria: Environmental, Social, And Governance Principles In Credit Ratings , Oct. 10, 2021
- 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: Methodology: Industry Risk , Nov. 19, 2013
- General Criteria: Country Risk Assessment Methodology And Assumptions , 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

Ratings List

Ratings Affirmed; Outlook Action

	To	From
Alstria Office REIT-AG		
Issuer Credit Rating	BBB-/Negative/--	BBB-/Stable/--
Senior Unsecured	BBB-	BBB-

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. A description of each of S&P Global Ratings' rating categories is contained in "S&P Global Ratings Definitions" at

https://www.standardandpoors.com/en_US/web/guest/article/-/view/sourceld/504352 Complete ratings information is available to subscribers of RatingsDirect at www.capitaliq.com. All ratings affected by this rating action can be found on 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; or Stockholm (46) 8-440-5914

Copyright © 2023 by Standard & Poor's Financial Services LLC. All rights reserved.

No content (including ratings, credit-related analyses and data, valuations, model, software or other application or output therefrom) or any part thereof (Content) may be modified, reverse engineered, reproduced or distributed in any form by any means, or stored in a database or retrieval system, without the prior written permission of Standard & Poor's Financial Services LLC or its affiliates (collectively, S&P). The Content shall not be used for any unlawful or unauthorized purposes. S&P and any third-party providers, as well as their directors, officers, shareholders, employees or agents (collectively S&P Parties) do not guarantee the accuracy, completeness, timeliness or availability of the Content. S&P Parties are not responsible for any errors or omissions (negligent or otherwise), regardless of the cause, for the results obtained from the use of the Content, or for the security or maintenance of any data input by the user. The Content is provided on an "as is" basis. S&P PARTIES DISCLAIM ANY AND ALL EXPRESS OR IMPLIED WARRANTIES, INCLUDING, BUT NOT LIMITED TO, ANY WARRANTIES OF MERCHANTABILITY OR FITNESS FOR A PARTICULAR PURPOSE OR USE, FREEDOM FROM BUGS, SOFTWARE ERRORS OR DEFECTS, THAT THE CONTENT'S FUNCTIONING WILL BE UNINTERRUPTED OR THAT THE CONTENT WILL OPERATE WITH ANY SOFTWARE OR HARDWARE CONFIGURATION. In no event shall S&P Parties be liable to any party for any direct, indirect, incidental, exemplary, compensatory, punitive, special or consequential damages, costs, expenses, legal fees, or losses (including, without limitation, lost income or lost profits and opportunity costs or losses caused by negligence) in connection with any use of the Content even if advised of the possibility of such damages.

Credit-related and other analyses, including ratings, and statements in the Content are statements of opinion as of the date they are expressed and not statements of fact. S&P's opinions, analyses and rating acknowledgment decisions (described below) are not recommendations to purchase, hold, or sell any securities or to make any investment decisions, and do not address the suitability of any security. S&P assumes no obligation to update the Content following publication in any form or format. The Content should not be relied on and is not a substitute for the skill, judgment and experience of the user, its management, employees, advisors and/or clients when making investment and other business decisions. S&P does not act as a fiduciary or an investment advisor except where registered as such. While S&P has obtained information from sources it believes to be reliable, S&P does not perform an audit and undertakes no duty of due diligence or independent verification of any information it receives. Rating-related publications may be published for a variety of reasons that are not necessarily dependent on action by rating committees, including, but not limited to, the publication of a periodic update on a credit rating and related analyses.

To the extent that regulatory authorities allow a rating agency to acknowledge in one jurisdiction a rating issued in another jurisdiction for certain regulatory purposes, S&P reserves the right to assign, withdraw or suspend such acknowledgment at any time and in its sole discretion. S&P Parties disclaim any duty whatsoever arising out of the assignment, withdrawal or suspension of an acknowledgment as well as any liability for any damage alleged to have been suffered on account thereof.

S&P keeps certain activities of its business units separate from each other in order to preserve the independence and objectivity of their respective activities. As a result, certain business units of S&P may have information that is not available to other S&P business units. S&P has established policies and procedures to maintain the confidentiality of certain non-public information received in connection with each analytical process.

S&P may receive compensation for its ratings and certain analyses, normally from issuers or underwriters of securities or from obligors. S&P reserves the right to disseminate its opinions and analyses. S&P's public ratings and analyses are made available on its Web sites, www.standardandpoors.com (free of charge), and www.ratingsdirect.com (subscription), and may be distributed through other means, including via S&P publications and third-party redistributors. Additional information about our ratings fees is available at www.standardandpoors.com/usratingsfees.

STANDARD & POOR'S, S&P and RATINGSDIRECT are registered trademarks of Standard & Poor's Financial Services LLC.