

19 Jul 2019 | Affirmation

Fitch Affirms NEPI Rockcastle at 'BBB'; Outlook Stable

Fitch Ratings-Stockholm-19 July 2019:

Fitch Ratings has affirmed real estate company NEPI Rockcastle plc's Long-Term Issuer Default Rating (IDR) and senior unsecured rating at 'BBB' with a Stable Outlook. Fitch has also affirmed the senior unsecured 'BBB' rating of bonds issued by NE Property B.V. which are guaranteed by NEPI Rockcastle plc.

The ratings reflect the group's large portfolio of regionally dominant shopping centres across central and eastern Europe (CEE) financed with low leverage. Assets are primarily located in Romania (36% by market value at end-2018) and Poland (24%). NEPI's core countries provide potential for higher retail sales (therefore rental) growth as countries converge towards Western Europe, but also exposure to higher country risk as they are lower rated. Geographical, asset concentration and tenant diversification help spread some of these risks.

The Stable Outlook reflects our expectations that NEPI will continue to conservatively finance its expansion through a combination of debt and equity.

Key Rating Drivers

Regionally Dominant Assets: With a EUR5.8 billion portfolio (including JV at share), NEPI has reached a size that benefits from efficient asset, property and leasing management. The majority of NEPI's assets are dominant shopping centres in large and medium-sized urban conurbations across CEE. Asset concentration is moderate, with the top 10 assets constituting 44% of the income-producing portfolio. NEPI aims to fully concentrate on retail assets and has put its small Romanian office portfolio up for sale.

Growth at Reduced Pace: We expect NEPI to continue to grow its portfolio through acquisitions and developments, in existing territories, although at a slower pace than in recent years. NEPI is pursuing a development pipeline of eight extension and refurbishment projects with estimated costs totaling EUR381 million. Additionally, EUR317million of greenfield developments are at different stages. Costs to complete the committed projects are around EUR200 million. To help reduce risk of the programme, management requires significant pre-lets as well as procurement of internal funding sources before committing to the spend.

Wide Geographical Footprint: NEPI's portfolio is spread across nine countries in CEE, which is a high number compared with most Fitch-rated property companies. However, the majority of assets are concentrated in Romania and Poland (totaling 60% of the portfolio) with a further 28% evenly spread across Hungary, Bulgaria and Slovakia. NEPI's growing portfolio is reducing its concentration to Romania (one of the lower rated countries in its portfolio). NEPI's exposure to low investment grade countries (or lower in the case of Serbia) highlights a higher risk profile than other Fitch-rated peers.

Strong Financial Profile: NEPI's financial policy is prudent with a target LTV of 35%. Management has adhered to its target despite the portfolio expansion and used equity issuance and scrip dividends to preserve the group's metrics. Net debt to EBITDA is expected to increase slightly in 2019 to 6.5x due to acquisition and capex. However, Fitch forecasts this leverage ratio will return to 6.2x in 2020. The average debt maturity is shorter than investment grade peers at around four years after its recent bond issuance. The Fitch-defined LTV was 35% at end-2018 (Fitch's calculation includes only investment property).

Maintained Access to Capital Markets: NEPI has maintained its capital market access despite earlier market turbulence around its share and bond pricing. South Africa's financial regulator FSCA completed its investigations in May 2019 and found the allegations made by Viceroy Research regarding NEPI's accounting to be without substance. NEPI subsequently issued EUR500 million of bonds with a four-year maturity.

Robust Operational Metrics: The rapid expansion in recent years has not impacted NEPI's operational performance. The shopping centre portfolio exhibits low vacancy (EPRA: 2.8%), increasing sales per sq. m (5.7% like-for-like growth in 2018) and low occupancy costs (11.9%). The tenant mix is granular with the top 10 tenants (22% of total rents) well-known global or regional brands skewed towards fashion retailers. The weighted average lease length is stable at around four years, which is comparable with other CEE peers, and affords both the landlord and tenant some flexibility, given the very dynamic retail environment.

Retail Transformation Underway: As a retail landlord the group is potentially exposed to negative trends already seen in some Western European retail markets, especially in the UK. CEE e-commerce penetration is increasing, albeit from a low base and significantly below the penetration in UK or other Western European countries. Robust retail sales growth helps limit the impact of an increasing proportion of online sales. These factors give CEE landlords time to learn from the experience of their western counterparts in how to deal with the new retail landscape. NEPI's strategy is to create dominant destination centres that embrace the customer experience in preparation for likely retail transformation.

Currency Risk: NEPI's leases and debt are euro-denominated, while in the majority of NEPI's jurisdictions tenants generate revenue in local currency. This type of setup is standard in CEE real estate markets. Nevertheless, a sharp substantial depreciation of the local currency can weaken tenants' profitability and their ability to meet euro-denominated rent obligations. The negative effect from NEPI's perspective could be amplified as currency markets in the region share some element of contagion risk. However, the various currencies in the portfolio have been stable against the euro for some time

Derivation Summary

NEPI's portfolio of EUR5.8 billion spread across nine countries in CEE is larger and more geographically diversified than fellow CEE peers such as Atrium European Real Estate Limited's (BBB/Stable) EUR2.8 billion portfolio and the EUR2.4 billion office-focused portfolio held by Globalworth (BBB-/Stable).

NEPI's conservative financial profile is demonstrated by its low (Fitch-calculated) LTV of 35%. Its end-2018 net debt to EBITDA at 6.3x is also a reflection of owning higher income-yielding assets. The resultant financial profile is stronger than Atrium's and Globalworth's. However, the majority of Atrium's assets are located in countries rated 'A-' and above, whereas the lower average country risk rating of NEPI's exposure more resembles that of Globalworth.

Western European peers like Hammerson (BBB/Stable) or British Land plc (A-/Stable) have assets located in the more mature Western European markets where income yields are tighter, thus their resultant financial metrics are not directly comparable with CEE entities.

Key Assumptions

Fitch's Key Assumptions Within Our Rating Case for the Issuer

- New rental income coming on-stream through developments and acquisitions is accounted on a 12-month basis in given year
- Aggregated acquisitions and capex of around EUR1.2 billion over the next four years
- Divestment of the Romanian office portfolio to be completed in 2019
- Listed securities portfolio sold down by the end of 2020
- No equity issuance during the forecast period

RATING SENSITIVITIES

Developments That May, Individually or Collectively, Lead to Positive Rating Action

- Continuing the expansion and positive geographical diversification of the portfolio, while maintaining similar occupancy rates, current conservative financial profile, and like-for-like rental growth
- Proportional increase to higher-rated countries in the portfolio, either through expansion or through upgrades
- Net debt to EBITDA below 7.0x on a sustained basis
- Average debt maturity no shorter than five years

Developments That May, Individually or Collectively, Lead to Negative Rating Action

- Material expansion into new or existing non-investment-grade countries
- Significant deterioration of operating metrics on a sustained basis, such as higher vacancies
- Increase in leverage with such metrics as LTV (adjusted net debt/investment properties) consistently exceeding 45% or net debt to EBITDA surpassing 8.0x on a sustained basis
- A liquidity score below 1.25x on a sustained basis

Liquidity and Debt Structure

Adequate Liquidity, Active Debt Management: At end-2018 NEPI had EUR90 million readily available cash and EUR236 million of available revolving credit facilities (RCF) with three banks compared with EUR265 million maturities in 2019. During 1H19 NEPI refinanced short-term bank loans and issued a EUR500 million bond with a 2023 maturity. NEPI's resultant liquidity score is now comfortably above 1x pro forma for the refinancing (end-2018: 0.8x)

Sources of Information

Public Ratings with Credit Linkage to other ratings

NEPI Rockcastle plc; Long Term Issuer Default Rating; Affirmed; BBB; RO:Sta
----senior unsecured; Long Term Rating; Affirmed; BBB
NE Property B.V.
----senior unsecured; Long Term Rating; Affirmed; BBB

Contacts:

Primary Rating Analyst

Fredric Liljestränd,

Director

+46 85510 9441

Fitch Ratings Espana S.A.U. (Spain) Nordic Region Filial

Kungsgatan 8

Stockholm 111 43

Secondary Rating Analyst

Pawel Jagiello,

Associate Director

+48 22 330 6707

Fitch Polska SA

Krolewska 16, 00-103

Warsaw

Committee Chairperson

John Hatton,

Managing Director

+44 20 3530 1061

Media Relations: Adrian Simpson, London, Tel: +44 20 3530 1010, Email:
adrian.simpson@thefitchgroup.com

Additional information is available on www.fitchratings.com

Applicable Criteria

[Corporate Rating Criteria \(pub. 19 Feb 2019\)](#)

[Corporates Notching and Recovery Ratings Criteria \(pub. 23 Mar 2018\)](#)

Additional Disclosures

[Dodd-Frank Rating Information Disclosure Form](#)

[Solicitation Status](#)

[Endorsement Policy](#)

ALL FITCH CREDIT RATINGS ARE SUBJECT TO CERTAIN LIMITATIONS AND DISCLAIMERS. PLEASE READ THESE LIMITATIONS AND DISCLAIMERS BY FOLLOWING THIS LINK:

[HTTPS://WWW.FITCHRATINGS.COM/UNDERSTANDINGCREDITRATINGS](https://www.fitchratings.com/understandingcreditratings). IN ADDITION, RATING DEFINITIONS AND THE TERMS OF USE OF SUCH RATINGS ARE AVAILABLE ON THE AGENCY'S PUBLIC WEB SITE AT WWW.FITCHRATINGS.COM. PUBLISHED RATINGS, CRITERIA, AND METHODOLOGIES ARE AVAILABLE FROM THIS SITE AT ALL TIMES. FITCH'S CODE OF CONDUCT, CONFIDENTIALITY, CONFLICTS OF INTEREST, AFFILIATE FIREWALL, COMPLIANCE, AND OTHER RELEVANT POLICIES AND PROCEDURES ARE ALSO AVAILABLE FROM THE CODE OF CONDUCT SECTION OF THIS SITE. DIRECTORS AND SHAREHOLDERS RELEVANT INTERESTS ARE AVAILABLE AT [HTTPS://WWW.FITCHRATINGS.COM/SITE/REGULATORY](https://www.fitchratings.com/site/regulatory). FITCH MAY HAVE PROVIDED ANOTHER PERMISSIBLE SERVICE TO THE RATED ENTITY OR ITS RELATED THIRD PARTIES. DETAILS OF THIS SERVICE FOR RATINGS FOR WHICH THE LEAD ANALYST IS BASED IN AN EU-REGISTERED ENTITY CAN BE FOUND ON THE ENTITY SUMMARY PAGE FOR THIS ISSUER ON THE FITCH WEBSITE.

Copyright © 2019 by Fitch Ratings, Inc., Fitch Ratings Ltd. and its subsidiaries. 33 Whitehall Street, NY, NY 10004. Telephone: 1-800-753-4824, (212) 908-0500. Fax: (212) 480-4435. Reproduction or retransmission in whole or in part is prohibited except by permission. All rights reserved. In issuing and maintaining its ratings and in making other reports (including forecast information), Fitch relies on factual information it receives from issuers and underwriters and from other sources Fitch believes to be credible. Fitch conducts a reasonable investigation of the factual information relied upon by it in accordance with its ratings methodology, and obtains reasonable verification of that information from independent sources, to the extent such sources are available for a given security or in a given jurisdiction. The manner of Fitch's factual investigation and the scope of the third-party verification it obtains will vary depending on the nature of the rated security and its issuer, the requirements and practices in the jurisdiction in which the rated security is offered and sold and/or the issuer is located, the availability and nature of relevant public information, access to the management of the issuer and its advisers, the availability of pre-existing third-party verifications such as audit reports, agreed-upon procedures letters, appraisals, actuarial reports, engineering reports, legal opinions and other reports provided by third parties, the availability of

independent and competent third- party verification sources with respect to the particular security or in the particular jurisdiction of the issuer, and a variety of other factors. Users of Fitch's ratings and reports should understand that neither an enhanced factual investigation nor any third-party verification can ensure that all of the information Fitch relies on in connection with a rating or a report will be accurate and complete. Ultimately, the issuer and its advisers are responsible for the accuracy of the information they provide to Fitch and to the market in offering documents and other reports. In issuing its ratings and its reports, Fitch must rely on the work of experts, including independent auditors with respect to financial statements and attorneys with respect to legal and tax matters. Further, ratings and forecasts of financial and other information are inherently forward-looking and embody assumptions and predictions about future events that by their nature cannot be verified as facts. As a result, despite any verification of current facts, ratings and forecasts can be affected by future events or conditions that were not anticipated at the time a rating or forecast was issued or affirmed.

The information in this report is provided "as is" without any representation or warranty of any kind, and Fitch does not represent or warrant that the report or any of its contents will meet any of the requirements of a recipient of the report. A Fitch rating is an opinion as to the creditworthiness of a security. This opinion and reports made by Fitch are based on established criteria and methodologies that Fitch is continuously evaluating and updating. Therefore, ratings and reports are the collective work product of Fitch and no individual, or group of individuals, is solely responsible for a rating or a report. The rating does not address the risk of loss due to risks other than credit risk, unless such risk is specifically mentioned. Fitch is not engaged in the offer or sale of any security. All Fitch reports have shared authorship. Individuals identified in a Fitch report were involved in, but are not solely responsible for, the opinions stated therein. The individuals are named for contact purposes only. A report providing a Fitch rating is neither a prospectus nor a substitute for the information assembled, verified and presented to investors by the issuer and its agents in connection with the sale of the securities. Ratings may be changed or withdrawn at any time for any reason in the sole discretion of Fitch. Fitch does not provide investment advice of any sort. Ratings are not a recommendation to buy, sell, or hold any security. Ratings do not comment on the adequacy of market price, the suitability of any security for a particular investor, or the tax-exempt nature or taxability of payments made in respect to any security. Fitch receives fees from issuers, insurers, guarantors, other obligors, and underwriters for rating securities. Such fees generally vary from US\$1,000 to US\$750,000 (or the applicable currency equivalent) per issue. In certain cases, Fitch will rate all or a number of issues issued by a particular issuer, or insured or guaranteed by a particular insurer or guarantor, for a single annual fee. Such fees are expected to vary from US\$10,000 to US\$1,500,000 (or the applicable currency equivalent). The assignment, publication, or dissemination of a rating by Fitch shall not constitute a consent by Fitch to use its name as an expert in connection with any registration statement filed under the United States securities laws, the Financial Services and Markets Act of 2000 of the United Kingdom, or the

securities laws of any particular jurisdiction. Due to the relative efficiency of electronic publishing and distribution, Fitch research may be available to electronic subscribers up to three days earlier than to print subscribers.

For Australia, New Zealand, Taiwan and South Korea only: Fitch Australia Pty Ltd holds an Australian financial services license (AFS license no. 337123) which authorizes it to provide credit ratings to wholesale clients only. Credit ratings information published by Fitch is not intended to be used by persons who are retail clients within the meaning of the Corporations Act 2001. Fitch Ratings, Inc. is registered with the U.S. Securities and Exchange Commission as a Nationally Recognized Statistical Rating Organization (the "NRSRO"). While certain of the NRSRO's credit rating subsidiaries are listed on Item 3 of Form NRSRO and as such are authorized to issue credit ratings on behalf of the NRSRO (see <https://www.fitchratings.com/site/regulatory>), other credit rating subsidiaries are not listed on Form NRSRO (the "non-NRSROs") and therefore credit ratings issued by those subsidiaries are not issued on behalf of the NRSRO. However, non-NRSRO personnel may participate in determining credit ratings issued by or on behalf of the NRSRO.

ENDORSEMENT POLICY - Fitch's approach to ratings endorsement so that ratings produced outside the EU may be used by regulated entities within the EU for regulatory purposes, pursuant to the terms of the EU Regulation with respect to credit rating agencies, can be found on the [EU Regulatory Disclosures](#) page. The endorsement status of all International ratings is provided within the entity summary page for each rated entity and in the transaction detail pages for all structured finance transactions on the Fitch website. These disclosures are updated on a daily basis.