

Research Update:

Shopping Center Owner NEPI Rockcastle Outlook Revised To Stable On Anticipated Operational Recovery; 'BBB' Rtg Affirmed

August 23, 2021

Rating Action Overview

- NEPI Rockcastle's (NEPI) results for first-half 2021 indicate stable occupancy levels of 95.6%, improved rent collection (94% as of mid-August), and slightly increasing footfall (+2.2% versus first-half 2020).
- We understand that NEPI's property portfolio has been fully operational since June 2021, and anticipate that occupancy levels and rent collection rates will remain high (well above 90%) in the next 12-18 months.
- In addition, NEPI's S&P Global Ratings-adjusted debt-to-debt-plus-equity ratio of 33.7% and debt to EBITDA of 6.3x (rolling 12 months as of June 30, 2021) remained below our rating downside thresholds of 35% and 7.5x, respectively.
- Therefore, we revised our outlook on NEPI to stable from negative, and affirmed our 'BBB' long-term issuer credit rating and senior unsecured debt ratings on the company.
- The stable outlook reflects our view that operating performance will continue to stabilize, thanks to improving footfall and tenants' sales as economic activity recovers in Central and Eastern Europe (CEE), with a debt-to-debt-plus-equity ratio below 35%, debt to EBITDA at about 6.0x-6.5x, and EBITDA interest coverage above 4.0x over the next two years.

PRIMARY CREDIT ANALYST

Manish Kejriwal
Dublin
+ 353 (0)1 568 0609
manish.kejriwal
@spglobal.com

SECONDARY CONTACT

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

Rating Action Rationale

Despite a continuously challenging operational environment, NEPI reported a stable occupancy level and slightly increasing footfall in the first half of 2021. NEPI continued to face operating pressures in the first six month of 2021, due to closure of nonessential stores and adoption of social-distancing measures. The company reported a decline in net rental operating income of 3.0% versus first-half 2020 (and -22.5% versus first-half 2019), mainly due to the impact of government regulated concessions in Poland and Slovakia and the full periodic rental impact from the disposal of its office assets, completed in August 2020. That said, we recognize the company's

stable and high occupancy levels at 95.6% and slightly increasing footfall (+2.2% versus first-half of 2020, but -34.3% versus first-half 2019). We understand that only 2.1% of leases expire in 2021, whereas 81% are already agreed and 72% are already signed. We believe the likelihood of further rent renegotiations or unpaid rents is limited for this year, assuming no further lockdown in the company's operating regions. We also view positively the company's high number of fixed-rent contracts (above 94% as of June 30, 2021), which should limit losses linked to variable rent contracts. In our revised base-case forecast, we now assume like-for-like rental income growth of just about 1%-2% for 2021, following its first-half 2021 results. This encompasses some expected rent discounts/loss or some negative renegotiation, even after the lockdown measures end. In our base-case scenario for 2022, we now forecast about 10%-12% growth in rental income compared with 2021 figures.

Given that NEPI's property portfolio by gross leasable area is now 100% operational, we anticipate continued high and stable occupancy levels and high rent collection rates in the next 12-18 months. As a result of decreasing COVID-19 infection rates, trading restrictions were eased in all CEE countries at the end of first-quarter 2021. Since June, NEPI's shopping centers (which represent 99% of its overall portfolio) became fully operational, including all stores, cinemas, and indoor food services. In 2020, NEPI collected about 99% of reported revenue (adjusted for rent concessions granted to tenants). We understand that collection rates declined to 88% in the first six month of the year, but recovered back to 94% as of mid-August 2021. We believe acceleration of vaccinations could lead to further reopening of CEE economies, leading to higher footfalls and retailers' sales. We anticipate that NEPI will be able to sustain high occupancy rates and rent collections in next 12-18 months (well above 90%). We expect that its stores will remain open, supported by a lower number of new COVID-19 cases and increasing vaccination rates, however, we remain cautious as different virus variants could disrupt the market in the short term.

NEPI's credit metrics remained below our downside thresholds in the past 12 months, and we now believe that improving macroeconomic fundamentals should help the company maintain stable leverage in the next 12-24 months. NEPI's adjusted ratio of debt to debt plus equity stood at 33.7% as of June 30, 2021 (versus 37.9% as of June 2020) with debt to EBITDA (rolling 12 months) at 6.3x (versus 6.8x as of June 2020). We forecast that the company will be able to maintain a ratio of debt to debt plus equity at 34%-35% and debt to EBITDA below 7x over the next 12-24 months. Our new base case incorporates a flat valuation in 2021 versus our previous assumptions of a 5% decline, given that we note some signs of value stabilization for NEPI's assets. The company reported a revaluation increase of €25.5 million (+0.4% of total portfolio value) during the first half of 2021. NEPI's good-quality assets should also be supportive for an anticipated improving operational performance. NEPI has also taken measures to support its conservative capital structure with the sale of the Romanian office portfolio (net cash proceeds of €294 million) in August 2020 and a capitalization issue in 2020.

We believe NEPI's liquidity and funding profiles should remain solid over the next 12-24 months. The company enjoys a solid liquidity buffer with the ratio of uses over sources well above 1.2x as of June 30, 2021. The company's debt repayments for the next 12 months total only about €7.7 million. NEPI had about €380 million of cash and cash equivalents and €570 million available under its committed undrawn backup facility as of second-quarter 2021. We understand covenant headroom is also adequate (more than 15%).

Outlook

The stable outlook on NEPI reflects our view that the company's operating performance will continue to stabilize with improving footfall numbers and tenants' sales as economic activity recovers in the CEE, particularly in Romania and Poland, thanks to the quality of their assets and limited new competition. We also believe that its debt to debt plus equity will be about 34%-35% and EBITDA interest coverage will remain higher than 4.0x over the next two years, supported by the company's resilient cash flows and conservative financial policy. We expect NEPI will maintain a large liquidity buffer.

Downside scenario

We could consider taking a negative rating action if :

- Debt to debt plus equity increased significantly above 35% on a prolonged basis, for instance as a result of unexpected asset devaluations;
- Debt to EBITDA moved above 7.5x; or
- EBITDA interest coverage falls below 3.8x on a prolonged basis due to weaker operating performance.

We could also take a negative rating action on NEPI if Romania experienced an economic slowdown and monetary policy flexibility weakened, leading to a sovereign downgrade.

Upside scenario

An upgrade would hinge on NEPI materially improving its portfolio in terms of size, as well as geographic and segment diversification, making it more comparable with that of peers with stronger business risk profiles. Necessary conditions for an upgrade are the ability to continue generating positive like-for-like rental income growth and showing positive portfolio revaluations.

In addition, a positive rating action on NEPI would be contingent on an improvement in Romania's credit quality or a significant dilution of the company's exposure to Romania to less than 25% of its assets and maintaining its debt to debt plus equity below 35%.

Company Description

NEPI Rockcastle is a property and development company operating in the CEE region. It was established in 2017 by the merger of New Europe Property Investments PLC and Rockcastle Global Real Estate Co. Ltd. The company has a portfolio valued at €5.8 billion, and a strong focus on retail, with some additional activities in offices and industrial. It operates in nine countries in CEE, particularly the Romanian and Polish markets.

Issue Ratings – Subordination Risk Analysis

Capital structure

As of June 30, 2021, NEPI's capital structure comprised 11% secured debt and 89% unsecured

debt, spread across bond and bank debt.

Analytical conclusions

We expect that NEPI's secured debt will remain lower than 40% of total assets (less than 10% as of June 30, 2021). As a result, although unsecured debt issuance is structurally subordinated to other debt obligations, the subordination does not affect the rating on the unsecured debt. We align our issue ratings on its senior unsecured debt with the 'BBB' issuer credit rating.

Ratings Score Snapshot

Issuer Credit Rating: BBB/Stable/--

Business risk: Satisfactory

- Country risk: Moderately high
- 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: Adequate (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
- General Criteria: Ratings Above The Sovereign--Corporate And Government Ratings: Methodology And Assumptions, Nov. 20, 2013
- General Criteria: Methodology: Industry Risk, Nov. 19, 2013
- General Criteria: Country Risk Assessment Methodology And Assumptions, Nov. 19, 2013

- Criteria | Corporates | General: Corporate Methodology, 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
NEPI Rockcastle PLC		
Issuer Credit Rating	BBB/Stable/--	BBB/Negative/--
NEPI Rockcastle PLC		
NE Property B.V.		
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; Stockholm (46) 8-440-5914; or Moscow 7 (495) 783-4009.

Copyright © 2021 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.