Brack Capital Properties N.V.

March 15, 2016

Research Update

Rating Raised to ‘ilAA-‘ On Lower Leverage And Change In Financial Policy; Outlook Stable

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Summary

- The company's book leverage ratio improved in recent months and is expected to drop below 60% in its 2015 financial statements.
- In addition, the company recently published quantitative objectives derived from its business plan which we believe support long-term maintenance of ratios commensurate with the rating upgrade.
- Operating performance remains stable on the company's income-producing asset portfolio, both residential and commercial, with high occupancy rates and rent growth, due in part to the strong German economy and real estate market.
- We are upgrading Brack Capital Properties N.V., a real estate investment company with residential and commercial rental assets in Germany, to 'ilAA-' from 'ilA+'.
- The stable outlook reflects our assessment that the company's asset portfolio and development project will continue to show stable performance. This assessment is underpinned, among other things, by the positive growth forecast and the favorable real estate market in Germany. The outlook is also supported by long-term maintenance of a debt-to-debt-and-equity ratio below 60% and an EBITDA interest coverage ratio of about 3x, based on the company's financial policy and our base case scenario.

Rating Action

On March 15, 2016, Standard & Poor's raised its corporate credit rating on Brack Capital Properties N.V., a real estate investment company with residential and commercial rental assets in Germany, to 'ilAA-' from 'ilA+'. The outlook is stable.

Rationale

The upgrade on Brack Capital Properties N.V. reflects the improvement in its financial risk profile reflected in an improved adjusted debt-to-debt-and-equity ratio as of September 30, 2015, and our assessment that this ratio will drop below 60% in the upcoming annual financial statement. We view this ratio as commensurate with the current rating. The upgrade is also supported by our evaluation of the management's commitment to a financial policy supportive of the current rating.

We expect the company's adjusted debt-to-debt-and-equity ratio to drop below 60% in its 2015 financial statements. This drop is mainly due to an increase in rent income (both due to rent growth on existing assets and to new asset acquisitions), to recognition of revenues from the residential development project, to the betterment of land in Düsseldorf the use of which was changed from commercial to residential, and to lower financing costs. In addition, in February 2016 the company announced quantitative objectives derived from its business plan, which include, among other things, the maintenance of debt-to-debt-and-equity below 60% and an EBITDA interest coverage of 2.5x or higher.

The company's income-producing asset portfolio maintained stable operating performance, as reflected in high occupancy rates of 96%. In our base case scenario we forecast a 4% increase in like-for-like NOI (net operating income) in 2015.

There is still some dependence on two major lessees generating together about 25% of the company's rental income. Nevertheless, all commercial assets have long-term leases, and leases with the two major lessees have a duration of 10-15 years (in February 2015, leases on 17 assets with one of the major lessees were extended until 2030). Revenues recognized from apartments delivered in the Düsseldorf development project reflect meeting profitability and delivery objectives, and presale of the apartments is progressing adequately (almost all residential units in phases A, B1 and B2 have been sold, as well as 62% of phase B3 residential units).

Our base case scenario assumes the following:

- Gross revenues of about € 90-95 million from rent and property management in 2015, based on recent acquisitions and growth in like-for-like rental income due to higher rents;
- Continued growth in revenues in 2016 and 2017, mostly due to new acquisitions and 3% growth in like-for-like rent in the residential portfolio;
- Recognition of revenues from the development project of about € 70 million in 2015 and at least € 115 million in 2016-2017;
- Increase of about € 20 million in value of current assets in the next two years, due to favorable market conditions and positive demand trends;
- Increase in debt due to additional acquisitions of income-producing assets of about € 50-100 million per year.

In our base case scenario, we expect the company's metrics to be as follows:

- Debt to debt and equity of about 58%-59% in the next two years;
- EBITDA interest coverage of about 2.7x;
- Debt to EBITDA of about 11x.

Liquidity

We estimate Brack Capital Properties' liquidity as "adequate", according to our criteria. This estimate is largely based on the current cash balance, the company's ability to generate high operating cash flows, a low maturity burden, and good access to the local capital market and to the German banking system. However, the fact that all of the company's assets are encumbered adversely affects its financial flexibility, in our opinion, but we believe that the fact that most of the loans on its assets are non-recourse and with no cross default mitigates this issue. Our base case scenario does not include unsecured debt refinancing and bond issuances, and nor does it include future asset acquisitions.

In our base-case scenario we estimate that the sources at the company's disposal as of January 1, 2016, and until December 31, 2017, are:

- About € 51 million in cash and tradable financial assets;
- About € 25 in accounts receivable from banks;
- About € 40 million in operating cash flow;
- Bank loan refinancing of about € 57.5 million (completed).

Our assumptions regarding the company's uses as of January 1, 2016, and until December 31, 2017, are:

- About € 17 million in bond maturities and about € 69 million in bank loan maturities;
- Dividends paid to non-controlling interest owners of about € 11 million;
- About € 8 million in capital expenditure;

- Acquisition of 430 residential units (completed in March 2016) at about € 7 million (after financing).

Outlook

The stable outlook reflects our assessment that the company's property portfolio and development project continue to show stable performance, This is supported, among other things, by the positive growth forecast and the favorable real estate market in Germany. The outlook is also supported by long-term maintenance of a debt-to-debt-and-equity ratio below 60% and an EBITDA interest coverage of about 3x, based on the company's financial policy and our base case scenario.

Downside Scenario

We may consider a downgrade if the company's debt-to-debt-and-equity ratio enduringly rises above 60%, or if the company significantly increases the share of its development business out of its total activity. We believe this could happen if the company makes large leverage acquisitions of income-producing properties or development land.

Upside Scenario

We may consider a positive rating action if the company expands its income-producing asset portfolio in the next two years and significantly decrease its dependence on major lessees, simultaneously deleveraging to the effect that its debt-to-debt-and-equity ratio drops below 50% and its EBITDA interest coverage is about 4x.

Modifiers

- **Diversification/Portfolio effect:** Neutral
- **Capital structure:** Neutral
- **Liquidity:** Neutral
- **Financial policy:** Neutral
- **Management and governance:** Neutral
- **Comparable rating analysis:** Neutral

Related Criteria And Research

- Criteria For Rating Non-Financial Corporate Issuances On Standard & Poor's Maalot's Local Rating Scale, September 22, 2014.
- National And Regional Scale Credit Ratings, September 22, 2014
- Standard & Poor's National And Regional Scale Mapping Tables, January 19, 2016
- Standard & Poor's Ratings Definitions, February 1, 2016
- Methodology: Timeliness Of Payments: Grace Periods, Guarantees, And Use Of 'D' And 'SD' Ratings, October 24, 2013
- Corporate Methodology, November 19, 2013
- Methodology And Assumptions: Liquidity Descriptors For Global Corporate Issuers, December 16, 2014
- Corporate Methodology: Ratios And Adjustments, November 19, 2013
- Group Rating Methodology, November 19, 2013
- Key Credit Factors For The Real Estate Industry, November 19, 2013

Rating Details (As of 15-March-2016)	
Brack Capital Properties N.V.	
Issuer rating	ilAA-/Stable
Senior Unsecured Debt	
Series A, B, C	ilAA-
Issuer Rating history	
15-March-2016	ilAA-/Stable
02-April-2013	ilA+/Stable
01-April-2012	ilA/Stable