

Research Update:

# Swedish Property Company Akelius Outlook Revised To Negative On Planned Asset Disposal And Uncertainty On Proceeds' Use

September 29, 2021

## Rating Action Overview

- On Sept. 26, 2021, Akelius Residential Property AB has announced that it will sell a portfolio of residential assets to Swedish peer Heimstaden Bostad AB for about €9.1 billion.
- The disposal would significantly decrease Akelius' asset base, and pro forma the transaction, the property portfolio would be worth about €5.4 billion at year-end 2021, compared with €12.9 billion as of second-quarter 2021.
- We understand that Akelius intends to reinvest the proceeds into new residential properties but the final usage of proceeds and the timing and details of the reinvestment strategy are uncertain.
- Consequently, we revised our outlook on Akelius to negative from stable and affirmed our 'BBB/A-2' long- and short-term issuer credit ratings on the company.
- The negative outlook indicates that we could downgrade Akelius if it maintains a significantly smaller asset base without changing its existing capital structure or financial policy, resulting into an EBITDA interest coverage of 1.5x or below.

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## Rating Action Rationale

**The disposal of the German and Scandinavian assets for a book value of €7.5 billion will shrink the overall asset base materially and makes the company's portfolio and cash flow increasingly dependent on unregulated residential markets.** The planned disposal will significantly reduce the company's geographical diversity. Pro forma the transaction, Akelius' portfolio will shrink by about 58% to about €5.4 billion from €12.9 billion currently and 16,253 units from about 45,029 units. The remaining portfolio will focus on the U.S. and Canada (together about 75%), London (about 17%), and Paris (about 8%). The exit from the German and Swedish residential markets will move the company's focus mainly to unregulated rental markets. We believe unregulated rental markets might experience higher operational volatility compared to regulated rental markets in a

downturn market scenario, with rents falling more strongly. Also, occupancy levels in Akelius' remaining markets are much lower compared with that in the disposed markets, so we expect the remaining portfolio occupancy levels at 85%-90% compared with 94% currently. Nevertheless, we maintain our business risk profile assessment at strong, on a still-sizable remaining portfolio that are in prime locations and underpin a high asset and tenant diversity.

**We have no visibility on how Akelius will use the transaction's proceeds.** The company is disposing the assets to a premium of around 20% to fair value as of second-quarter 2021 and that closing is expected before year end. Although Akelius has publicly stated that the proceeds will likely be reinvested in the portfolio, we have limited visibility on the timing and details of this reinvestment. We remain cautious regarding potential distributions to the shareholder. The company is ultimately owned by Akelius Foundation (84% of the votes and 80% of capital), which has a focus on distributing significant amounts to charity and humanitarian projects. Once we have more clarity on the use of proceeds and the respective timing, we will update our analysis accordingly.

**The transaction will lead to a material cash position, supporting net debt--however, EBITDA interest coverage will likely weaken in 2022.** Upon the transaction's closing, the company will have a strong cash position of over €8 billion compared to S&P Global Ratings adjusted net debt of €5.8 billion at second-quarter-end. We understand that about €1 billion of debt related to the disposed assets will be rolled over to the buyer. We believe the lost earnings from the disposed assets will likely result in an overall weaker debt service capacity in 2022, and we anticipate S&P Global Ratings-adjusted EBITDA interest coverage will fall to 1.5x-1.7x for 2022 (compared with 2x at second-quarter-end), close to our downside threshold of 1.5x. The final impact on its debt service capacity will also depend on the timing of reinvestment and therefore restoring the cash flow impact from the disposals. Any adjustments to its debt structure, such as active debt repayments or distribution of dividends, might also affect the ratio.

## Outlook

The negative outlook reflects our view that we could downgrade Akelius in the next 12-24 months if, once the transaction closes, the significant reduction of its asset base is not restored in a timely manner while the company maintains its existing gross debt profile and financial policy. This could happen if Akelius does not reinvest the proceeds of the sale of the portfolio to restore its existing asset base or strengthen its credit profile and mainly distributes them to unitholders.

## Downside scenario

We could lower the rating if the company does not reinvest the proceeds into restoring its existing asset base or strengthen its credit profile and mainly distributes them to unitholders, for example.

## Upside scenario

We could revise the outlook to stable if the transaction does not close, or if the disposals take place and Akelius restores its cash flow levels similar to the existing levels in a timely manner. That would indicate that the company's reinvestments will continue with the prime quality and markets in line with its existing portfolio, with high occupancy levels and attractive yields.

We could also revise our outlook to stable if the company uses part of the proceeds to strengthen

its credit metrics so that its debt-to-debt plus equity ratio remains sustainably close to or below 50%, while EBITDA interest coverage moves more toward 2.4x. We would also expect to see a new financial policy commensurate with these levels.

## Company Description

Sweden-based Akelius is a privately owned real estate company, focusing on residential assets. As of June 30, 2021, the company's portfolio stood at €12.9 billion, with properties in 12 cities across seven countries, including Berlin (25%), Stockholm (15%), Malmö (in Sweden; 9%), and London (8%). The company focuses on long-term ownership of residential properties, particularly in large cities with sound growth prospects and limited new supply.

Akelius Foundation owns 80% of Akelius. The remaining shares are split between Hugo Research Foundation (9%), Grandfather Roger Foundation (5%), and institutional shareholders (6%, through the issuance of D-shares in 2019).

## Ratings Score Snapshot

Issuer Credit Rating: BBB/Negative/A-2

Business risk: Strong

- Country risk: Very low
- Industry risk: Low
- Competitive position: Strong

Financial risk: Significant

- Cash flow/Leverage: Significant

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: Fair (no impact)
- Comparable rating analysis: Neutral (no impact)

## Related Criteria

- General Criteria: Group Rating Methodology, July 1, 2019
- General Criteria: Hybrid Capital: Methodology And Assumptions, July 1, 2019
- Criteria | Corporates | General: Corporate Methodology: Ratios And Adjustments, April 1, 2019
- General Criteria: Methodology For National And Regional Scale Credit Ratings, June 25, 2018

- Criteria | Corporates | Industrials: Key Credit Factors For The Real Estate Industry, Feb. 26, 2018
- General Criteria: Methodology For Linking Long-Term And Short-Term Ratings, April 7, 2017
- Criteria | Corporates | General: Methodology And Assumptions: Liquidity Descriptors For Global Corporate Issuers, Dec. 16, 2014
- Criteria | Corporates | General: The Treatment Of Non-Common Equity Financing In Nonfinancial Corporate Entities, April 29, 2014
- General Criteria: Country Risk Assessment Methodology And Assumptions, Nov. 19, 2013
- General Criteria: Methodology: Industry Risk, 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

## Related Research

- Akelius Residential Property AB, April 12, 2021

## Ratings List

### Ratings Affirmed; Outlook Action

	To	From
<b>Akelius Residential Property AB</b>		
Issuer Credit Rating	BBB/Negative/A-2	BBB/Stable/A-2
Nordic Regional Scale	--/--/K-2	--/--/K-2
<b>Akelius Residential Property Financing B.V.</b>		
Senior Unsecured	BBB	
Subordinated	BB+	

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