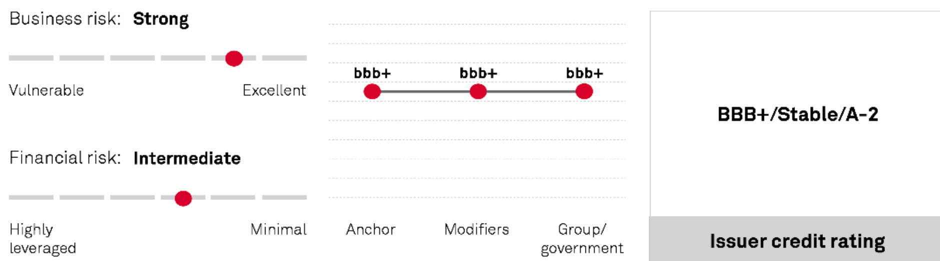
Grand City Properties S.A.

December 9, 2021

Ratings Score Snapshot



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Credit Highlights

Overview

Key strengths	Key risks
Exposure to the regulated German residential segment, which continues to benefit from strong market fundamentals.	Exposure to the non-regulated London market (currently 20% of total gross asset value) where occupancy and market rents could be more volatile than in Germany.
Large portfolio of average-quality residential assets mainly located in or close to metropolitan German cities and in London, valued at €8.9 billion at Sept. 30, 2021.	Social and political debates on rent affordability in Germany could lead to further regulation and tighter rent controls that could affect operational profitability.
Strong track record of positive like-for-like rental income growth, supported by a highly diversified asset and tenant base and long tenant stays.	Although occupancy has improved consistently in recent quarters to 94.7%, it is still weaker than similar rated peers, with average rent at €8 per square meter.
Moderate leverage and financial policy, with debt to debt plus equity expected to remain below 45%, and a strong liquidity position.	Relatively high ratio of debt to EBITDA, expected at 12x-13x in the coming years, compared with peers operating in a higher yield environment.

GCP's operating performance remains resilient to the COVID-19 pandemic, although additional regulation and the exposure to London could bring some instability to its operations. Most of the residential landlords we cover continue to report sustained positive rental growth and occupancy levels. This shows the stability of residential portfolios and it is why we continue to consider this property segment, especially in regulated markets such as Germany, among the most resilient. GCP reported like-for-like net rent growth of 2.1% as of Sept. 30, 2021 with vacancy levels reaching the lowest levels over the past few years (5.3% at end-September 2021 from 7.1% at end-December 2018). That said, we think social and political debates on rent affordability in Germany could lead to further regulation and tighter rent controls that could affect GCP's operational profitability. We also think potential future needs for higher investments due to requirements to meet national climate targets could put pressure on the cost basis for residential real estate players, including GCP. At the same time, we think the exposure to the non-regulated London market could bring certain volatility to GCP's operations. The pandemic's impact on the U.K. residential real estate market was greater than on the residential property markets in other European countries such as Sweden, the Netherlands, and Germany. We also note that Brexit could affect the market further. These factors translated into a significant increase in GCP's London vacancy rate raising to 8.4% at the end of March 2021 compared to 4% at year-end 2019. We note that vacancy in London has reduced to 6% as of Sept. 30, 2021 but we still view this market as more volatile and challenging than Germany. That said, the exposure to London remains limited, although it has increased in recent years and now represents 20% of GCP's total gross asset value (up from 13% at year-end 2019). We do not expect it to increase materially from current levels, in line with the company's strategy.

In line with its moderate financial policy, we expect GCP's credit metrics to remain relatively stable in the coming years. GCP's net acquirer position and share buyback program (€215 million completed as of Sept. 30, 2021) have translated into a slight increase in leverage compared to year-end 2020. At the end of September 2021, the company's debt to debt plus equity was 44.6% (up from 39.6% at end-2020) and its debt to EBITDA was about 13x (10.7x at end-2020). These levels remain commensurate with our existing ratings, but we note the reduced headroom in credit metrics compared to previous periods. We assume GCP will continue to fund capital expenditure (capex) and acquisitions through cash flow generation and a mix of funding in line with GCP's financial policy. Therefore, we forecast that the company's debt to debt plus equity will remain below 45%, at about 43%-44% in the coming years, supported by sustained asset revaluations. The company's long average debt maturity profile of more than six years, and low cost of debt (1% as of September 2021) with 97% being at fixed rates or hedged, will continue to support its healthy EBITDA interest coverage ratio about 4.5x-5.5x (4.3x at year end 2020). We expect GCP's debt to EBITDA will remain at 12x-13x, slightly higher than in previous periods where it was about 11x.

We continue to view GCP as a highly strategic subsidiary of Aroundtown S.A. (Aroundtown; BBB+/Stable/A-2). Aroundtown continued to increase its stake in GCP to 45% at the end of September (from 42% at the end of June). We think Aroundtown's stake in the company, combined with the absence of a strong minority shareholder and the presence of several of Aroundtown's leadership in GCP's management bodies, gives Aroundtown the ability to influence GCP's strategy and disposition of cash flow. Therefore, we continue to apply our group rating methodology in our assessment of GCP's creditworthiness and we regard the company as a highly strategic subsidiary of Aroundtown. This is because we think GCP is almost integral to the group's identity and future strategy (GCP represented 17% of Aroundtown's gross asset value, proportionally consolidating GCP, at end-September 2021). We think Aroundtown is likely to support GCP under almost all foreseeable circumstances. That said, we note the significant stake still owned by other shareholders and the independence of GCP's funding strategy, with no cross-default clauses in the existing debt instruments. Our assessment of the group does not currently have a positive or negative influence on the final rating of the company given that we view the credit quality of Aroundtown as comparable to GCP's.

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Outlook

The stable outlook on GCP reflects that on Aroundtown. We expect Aroundtown's diversification to mitigate the pandemic's effect on the hotel portfolio. At the same time, we expect GCP's portfolio to sustain steady demand and occupancy levels. Our outlook is supported by Aroundtown's and GCP's relatively prudent financial policy.

Downside scenario

We could downgrade GCP if:

- We were to lower the rating on Aroundtown while the composition of GCP's shareholding structure and management bodies remained broadly as they are now.

- GCP's stand-alone operating performance deteriorated significantly, with higher vacancy in its portfolio, and credit metrics deviated significantly from our base case--specifically, if debt to debt plus equity did not stay below 45% on a sustainable basis.

Upside scenario

Ratings upside for GCP is linked to Aroundtown achieving a higher rating, and the shareholder structure and composition of GCP's management bodies.

Although it would not result in an upgrade, we could revise upward GCP's stand-alone credit profile to 'a-' from 'bbb+' if:

- Debt to debt plus equity improved to about 35% as part as a more conservative financial policy and debt to EBITDA improved from current levels, while EBITDA interest coverage stayed comfortably above 3.5x; or
- The portfolio showed strong growth, significantly exceeding €10 billion without raising existing leverage. We would expect the new assets to be of at least the same quality as the existing ones, and that such growth would dilute GCP's exposure to assets with renovation potential that generally exhibit higher vacancy rates, allowing the group's average vacancy rate to fall below 5%.

Our Base-Case Scenario

Assumptions

- Real GDP growth of 3.1% in Germany in 2021, followed by a 5.0% in 2022 and 2.1% in 2023. We forecast the consumer price index in Germany at 2.9%, 1.7%, and 1.6% in those years.
- Like-for-like rental income growth of about 2.0%-3.0% in 2021 and then about 2.0% in the coming years.
- Stable occupancy levels of 94%-95% in the coming 12-24 months.
- Positive like-for-like increase in the overall portfolio's market valuation up to 5.0% in 2021 and 2.0%-3.0% per year in 2022-2023, on the back of rental growth and solid investor demand for German residential assets.
- Total capex of €100 million-€110 million a year, mainly linked to repositioning activities and modernization projects in existing assets. We expect maintenance capex to remain stable at about €40 million per year.
- Steady gross EBITDA margins of 55%-56% in the next few years, due to a stable cost base.
- Portfolio value to reach about €9 billion by year-end 2021. We then assume an overall balanced asset rotation.
- Potential additional share buy backs, to be funded in line with GCP's financial policy and our existing ratings.
- Stable dividend policy, with cash distributions to shareholders following a payout policy of 75% of reported funds from operations. This should translate into dividends of about €150 million per year.
- Average cost of debt to remain stable at about 1%.

Key metrics

Company Name--Key Metrics*

Mil. €	2019a	2020a	2021e	2022f	2023f
EBITDA	297.7	299.8	300-310	310-320	320-330
EBITDA margin (%)§	53.1	56.0	55-56	55-56	55-56
Dividends	105.0	70.2	53.7	~150	~150
Debt	3,272.5	3,216.9	~3,900	~4,000	~4,000

Debt to EBITDA (x)	11.0	10.7	~13	12-13	12-13
EBITDA interest coverage (x)	4.8	4.3	4.5-5.0	5.0-5.5	5.0-5.5
Debt to debt plus equity (%)	42.4	39.6	~44	~44	43-44

*All figures adjusted by S&P Global Ratings. §Margin is based on gross revenue. a--Actual. e--Estimate. f--Forecast.

GCP decided to offer a scrip dividend again this year. As a result, the company issued new shares for a total value of €82.7 million. GCP paid the remainder of the dividend, €53.7 million, in cash in July 2021. This explains the lower amount of cash dividend distributed in 2020 and 2021 compared with other years. We conservatively assume full cash dividend distributions in subsequent years.

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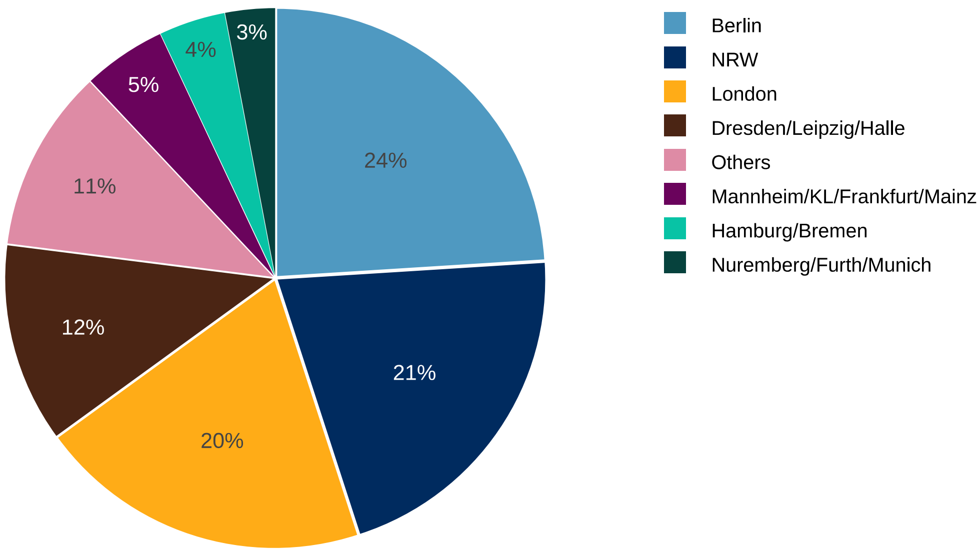
Company Description

GCP is a Luxembourg-incorporated property investment company, focusing on owning and managing properties, mainly in the German residential real estate market. As of Sept. 30, 2021, its total portfolio value amounted to about €8.9 billion, comprising 64,939 owned units located in densely populated areas, with a focus on Berlin (24% of portfolio value), North Rhine-Westphalia (21%), and the cities of Dresden, Leipzig, and Halle (together 12%). The company has expanded its footprint to London, which now represents 20% of its portfolio value.

Grand City Properties S.A.-- Geographic Diversity

Distribution by value; as of September 2021



Source: Company report.

The company is listed on the MDAX on the Frankfurt stock exchange. At the end of September 2021, the shareholder structure comprised a free float of 50%; Aroundtown SA, through its subsidiary Edolaxia Group, owned a 45% stake; and treasury shares accounted for 5%.

Peer Comparison

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Grand City Properties S.A. -- Peer Comparison -- Operating Metrics

	Grand City Properties S.A.	Vesteda Residential Fund FGR*	Vonovia SE	Heimstaden Bostad AB$
Issuer credit rating as of Nov. 29, 2021	BBB+/Stable/A-2	A-/Stable/A-2	BBB+/Stable/A-2	BBB/Stable/--
Business Risk Profile	Strong	Strong	Excellent	Strong
Financial Risk Profile	Intermediate	Intermediate	Significant	Significant
Portfolio Value (bil. €)	8.90	8.20	95.40	27.16/ SEK 274.8
Asset Diversity	100% residential	100% Residential	100% residential	100% residential.

Geographic Diversity	80% Germany 20% London	100% Netherlands	90% Germany 7% Austria 3%Sweden	31% Sweden 25% Germany 22% Denmark 9% Netherlands 7% Norway 6% Czech Republic
Occupancy (%)	94.7	97.5	97.3	97.0

All data as of Sept. 30, 2021. *Data as of Dec. 31, 2020. $Figures as of Q2 2021 adjusted for estimated pro forma fair value of newly acquired portfolio.

Grand City Properties S.A. -- Peer Comparison -- Financial Metrics

Mil. €	**Grand City Properties S.A.**	**Vesteda Residential Fund FGR**	**Vonovia SE**	**Heimstaden Bostad AB**
Foreign currency issuer credit rating	BBB+/Stable/A-2	A-/Stable/A-2	BBB+/Stable/A-2	BBB/Stable/--
Local currency issuer credit rating	BBB+/Stable/A-2	A-/Stable/A-2	BBB+/Stable/A-2	BBB/Stable/--
Period	RTM	Annual	RTM	RTM
Period ending	2020-09-30	2020-12-31	2020-09-30	2020-09-30
Revenue	523.7	335.0	2,425.7	818.3
EBITDA	298.7	229.0	1,660.2	439.2
Funds from operations (FFO)	193.2	196.0	1,115.4	200.7
Interest expense	62.5	41.0	490.5	145.3
Cash flow from operations	165.1	168.0	995.1	154.3
Capital expenditure	72.5	138.0	1,554.1	504.3
Dividends paid	52.8	195.0	507.1	472.3
Cash and short-term investments	1,263.9	2.0	2,097.6	1,408.0
Debt	3,954.7	2,062.0	46,286.5	9,963.9
Equity	4,911.4	6,294.0	27,726.4	9,911.4
Valuation of investment property	8,894.3	8,387.0	92,039.3	19,581.3
Adjusted ratios				
EBITDA margin (%)	57.0*	68.4	68.4	53.7
EBITDA interest coverage (x)	4.8	5.6	3.4	3.0
Debt/EBITDA (x)	13.2	9.0	27.9	22.7
Debt/debt and equity (%)	44.6	24.7	62.5	50.1

*Margin is based on gross revenue

Business Risk

GCP's business risk profile is underpinned by its large income-producing asset portfolio of about €8.9 billion as of Sept. 30, 2021, generating stable and recurring cash flows across Germany. The company benefits from a broad geographic spread across densely populated regions, with good growth prospects in Germany. It focuses mainly on metropolitan areas with favorable macroeconomic fundamentals and solid demand for residential premises.

GCP is present in regions with healthy rental growth prospects, such as North Rhine-Westphalia--which includes cities such as Cologne, Duisburg, and Dortmund--as well as Berlin, and the cities of Dresden and Leipzig. Demand continues to outpace supply of new property developments in GCP's core regions, further facilitating improvements in occupancy rates (overall vacancy reduced to 5.3% in September 2021, from 6.2% on Dec. 31, 2020).

The company has expanded its operations to London, which now represents 20% of the total gross asset value as of Sept. 30, 2021 (from 13% at year-end 2019). Although the exposure is small compared with the overall portfolio size, we note that Brexit and the pandemic could affect rent and valuation. We view this market as more volatile and challenging compared to regulated markets like Germany. Although vacancy has improved in the London portfolio to 6% as of Sept. 30, 2021, we note the increase suffered during the pandemic last year. GCP's London vacancy increased to 8.6 % as of Dec. 31, 2020 from 4% at year-end 2019. This surpassed the overall average vacancy rate in GCP's portfolio. We expect GCP will remain mainly a player in Germany but note that the exposure to London could bring some instability to its operations. That said, we do not forecast U.K. exposure to increase beyond 20%-25% in the long term, in line with the company's strategy.

We see the asset quality of most apartments in GCP's portfolio as in line with the German average, reflecting that the company still has some exposure to lower-quality premises, which points to GCP's previous acquisition strategy. Vacancy rates remain high compared with levels at other residential real estate companies we rate, such as Vonovia SE (BBB+/Stable/A-2) and Deutsche Wohnen SE (BBB+/Stable/A-2). We acknowledge that this is related to GCP's acquisitive profile and value-added strategy in the past, which saw it constantly add above-average-vacancy assets to its portfolio. That said, we note GCP's improvements on vacancy, which stands now at the end of September at 5.3% compared to 7.1% at the end of 2018.

GCP has limited exposure to development activities. Investments relate mainly to the maintenance and renovation of acquired premises. GCP's property portfolio now comprises about 64,939 owned units and, like its residential property peers, has broad asset and tenant diversity. In addition, GCP's assets are rented at 10%-20% below the market average rates, providing them headroom in a market downturn scenario, where rents would start declining. We think the residential asset class, especially in Germany, is more resilient than commercial properties, which are more cyclical and vulnerable to economic downturns.

Financial Risk

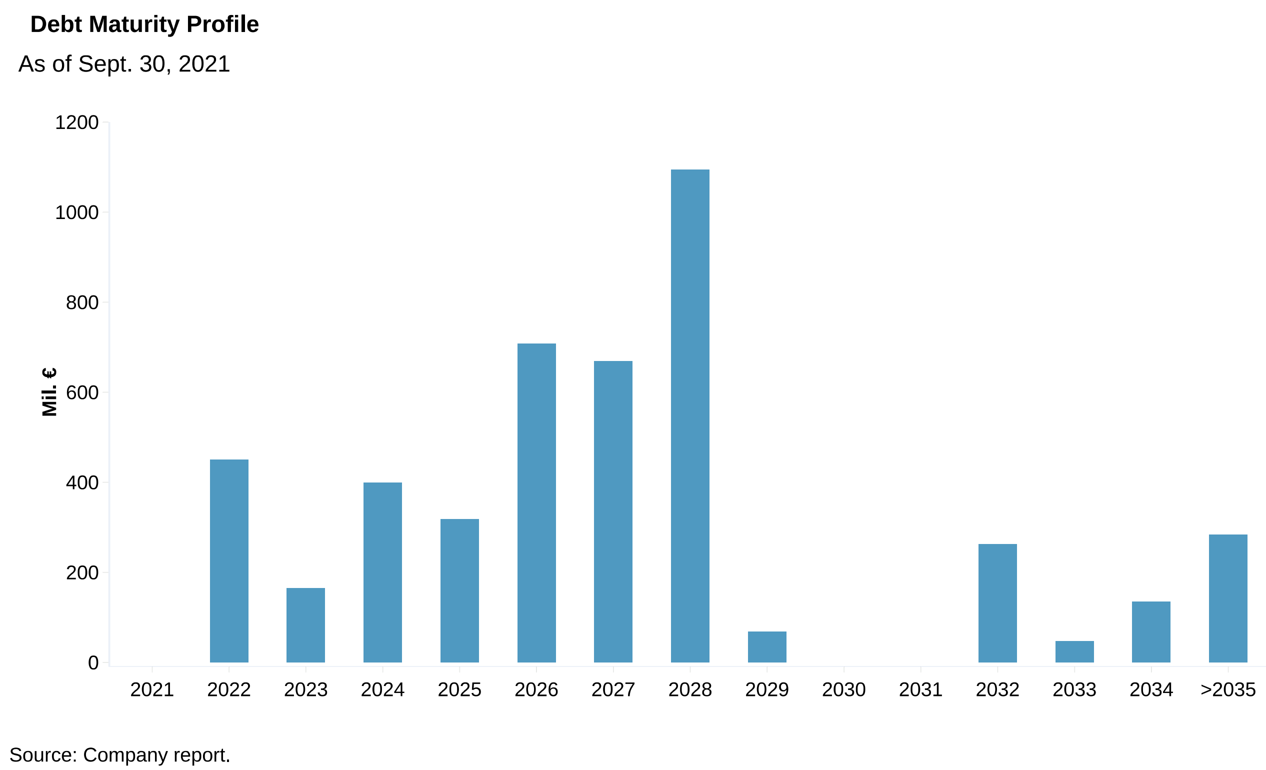
Our assessment of GCP's financial risk profile reflects the company's moderate financial policy of maintaining its debt-to-debt-plus-equity ratio at or below 45% on a sustainable basis.

We expect GCP's credit metrics to remain relatively stable in the coming years, in line with its moderate financial policy, but we note reduced headroom in credit metrics compared to previous periods. We forecast that the company's debt to debt plus equity will remain below 45%, at about 43%-44% in the coming years, supported by sustained asset revaluations. The company's long average debt maturity profile and low cost of debt will continue to support its healthy EBITDA interest coverage ratio about 4.5x-5.5x. We expect GCP's debt to EBITDA will remain at 12x-13x, slightly higher than in previous periods when it was about 11x.

GCP has a solid capital structure with no significant debt maturities until 2024 (average debt maturity of 6.2 years) and a low cost of debt on Sept. 30, 2021, of 1% (improved from 1.3% for the same period last year). GCP's proportion of unencumbered assets is relatively high at about 88% (about €8 billion) of the total portfolio value. The company has well-diversified funding sources, which include mortgage debt, convertible and straight bonds, perpetual notes, and straight common equity. GCP has also demonstrated a very good track record of accessing both equity and debt capital markets in the last few years.

Partly offsetting these strengths is the company's somewhat weaker cash flow generation, mainly due to the low yield profile of its assets compared with those of other residential peers operating in a higher yielding environment (such as the U.S.) or other commercial landlords.

Debt maturities



Financial Summary

Quarter ending	September 2020	December 2020	March 2021	June 2021	September 2021
Revenue	133.5	134.2	128.3	131.1	130.1
EBITDA	76.0	76.7	72.6	74.8	74.6
Funds from operations (FFO)	52.0	51.5	39.7	53.3	48.7
Interest expense	18.2	18.8	15.0	14.1	14.6
Cash flow from operations	41.7	56.3	29.5	39.3	40.0
Capital expenditure	18.7	16.0	16.0	16.8	23.8

Cash and short-term investments	1,336.1	1,691.9	1,666.8	1,354.7	1,263.9
Debt	3,553.2	3,216.9	3,397.8	3,539.4	3,954.7
Equity	4,687.0	4,914.4	4,798.8	4,772.9	4,911.4
Valuation of investment property	7,842.4	8,005.9	8,144.9	8,387.0	8,894.3
Adjusted ratios					
EBITDA margin (%)*	55.4	56.0	56.5	56.9	57.0
EBITDA interest coverage (x)	4.6	4.3	4.3	4.5	4.8
Debt/EBITDA (x)	11.8	10.7	11.4	11.8	13.2
Debt/debt and equity (%)	43.1	39.6	41.5	42.6	44.6

*Margin is based on gross revenue.

Reconciliation Of Grand City Properties S.A. Reported Amounts With S&P Global Adjusted Amounts (Mil. EUR)

	Debt	Shareholder equity	Revenue	EBITDA	Operating income	Interest expense	S&PGR adjusted EBITDA	Operating cash flow	Dividends	Capital expenditure
Financial year	Dec-31-2020									
Company reported amounts	4,213	5,020	535	355	640	53	300	242	71	70
Cash taxes paid	-	-	-	-	-	-	(28)	-	-	-
Cash interest paid	-	-	-	-	-	-	(51)	-	-	-
Lease liabilities	55	-	-	-	-	-	-	-	-	-
Debt-like hybrids	31	(31)	-	-	-	1	(1)	(1)	(1)	-
Intermediate hybrids (equity)	610	(610)	-	-	-	16	(16)	(16)	(16)	-
Accessible cash and liquid investments	(1,692)	-	-	-	-	-	-	-	-	-
Share-based compensation expense	-	-	-	2	-	-	-	-	-	-
Income (expense) of unconsolid. cos.	-	-	-	(4)	-	-	-	-	-	-
Reclassification of interest and dividend cash flows	-	-	-	-	-	-	-	(51)	-	-
Noncontrolling/ minority interest	-	535	-	-	-	-	-	-	-	-
EBITDA - Gain/(loss) on disposals of PP&E	-	-	-	(54)	(54)	-	-	-	-	-

Reconciliation Of Grand City Properties S.A. Reported Amounts With S&P Global Adjusted Amounts (Mil. EUR)

	Debt	Shareholder equity	Revenue	EBITDA	Operating income	Interest expense	S&PGR adjusted EBITDA	Operating cash flow	Dividends	Capital expenditure
D&A: Asset valuation gains/(losses)	-	-	-	-	(290)	-	-	-	-	-
Dividends: other	-	-	-	-	-	-	-	-	16	-
Total adjustments	(996)	(106)	0	(56)	(343)	17	(96)	(68)	(1)	0
S&P Global Ratings adjusted	**Debt**	**Equity**	**Revenue**	**EBITDA**	**EBIT**	**Interest expense**	**Funds from Operations**	**Operating cash flow**	**Dividends**	**Capital expenditure**
	3,217	4,914	535	300	297	70	203	174	70	70

Liquidity

We assess GCP's liquidity as strong because we forecast that the fund's liquidity sources will exceed its funding needs by at least 1.5x over the next 12 months, and by more than 1x over the subsequent 12 months.

The company benefits from the absence of large debt maturities in the short term. Aside from its convertible bond maturing in March 2022, there are no significant maturities until 2024. In addition, GCP has very high cash balances.

Principal liquidity sources

- About €1,263.9 million of unrestricted cash and liquid market investments and €50 million undrawn under its back-up facilities.
- Our forecast of about €200 million in cash funds from operations for the next 12 months.

Principal liquidity uses

- About €452.9 million of short-term debt maturities, including regular debt amortization.
- Our forecast of €100 million-€110 million of capex for property, plant, and equipment, and property investment, most of which is not committed.
- About €57 million pending on its existing share buyback program.
- About €150 million of dividend distribution (including perpetual notes) assuming full cash payment.

Covenant Analysis

Compliance expectations

GCP complied with all its covenants as of Sept. 30, 2021. We expect GCP will maintain significant headroom (more than 30%) under the financial maintenance covenants in its various debt agreements.

Requirements

GCP has several covenants under its bond and bank loan documentation. The straight bonds and convertible bonds are unsecured and have the following covenants:

- Limitation of debt: Total debt/assets of less than or equal to 60%.
- Limitation on secured debt: Secured debt/total assets of less than or equal to 45%.
- Interest coverage ratio: Adjusted EBITDA/net cash interest of greater than or equal to 2.0x.
- Maintenance of unencumbered assets: Unencumbered assets/unsecured net debt of greater than or equal to 125%.

Group Influence

Aroundtown's stake in GCP was 45% at the end of September 2021 (42% at the end of June). We think Aroundtown's stake in the company, combined with the absence of a strong minority shareholder and the presence of several of Aroundtown's leadership in GCP's management bodies, gives Aroundtown the ability to influence GCP's strategy and disposition of cash flow. Therefore, we continue to apply our group rating methodology in our assessment of GCP's creditworthiness and we regard the company as a highly strategic subsidiary of Aroundtown. This is because we think GCP is almost integral to the group's identity and future strategy. We think Aroundtown is likely to support GCP under almost all foreseeable circumstances. That said, we note the significant stake still owned by other shareholders and the independence of GCP's funding strategy, with no cross-default clauses in the existing debt instruments. Our assessment of the group does currently not have a positive or negative influence on the final rating of the company given that we view the credit quality of Aroundtown as comparable to GCP's.

Issue Ratings--Subordination Risk Analysis

Capital structure

GCP's proportion of secured debt remains limited and its ratio of secured debt to total assets is well below 40% as of Sept. 30, 2021.

Analytical conclusions

We continue to align the ratings on the senior unsecured debt with our 'BBB+' issuer credit rating.

We assign intermediate equity content to GCP's outstanding subordinated hybrid instruments. The issue rating of 'BBB-' is two notches below our issuer credit rating, one notch for subordination and one for deferability.

Rating Component Scores

Foreign currency issuer credit rating	**BBB+/Stable/A-2**
Local currency issuer credit rating	**BBB+/Stable/A-2**
Business risk	**Strong**
Country risk	Very Low
Industry risk	Low
Competitive position	Strong
Financial risk	**Intermediate**
Cash flow/leverage	Intermediate
Anchor	**bbb+**
Diversification/portfolio effect	Neutral (no impact)
Capital structure	Neutral (no impact)
Financial policy	Neutral (no impact)
Liquidity	Strong (no impact)
Management and governance	Satisfactory (no impact)
Comparable rating analysis	Neutral (no impact)
Stand-alone credit profile	**bbb+**

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
- 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
- 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