MOODY'S
INVESTORS SERVICE

Rating Action: Moody's downgraded DEMIRE's ratings to Ba3. Outlook is stable

06 Apr 2021

Frankfurt am Main, April 06, 2021 -- Moody's Investors Service ("Moody's") has today downgraded DEMIRE Deutsche Mittelstand Real Estate AG ("DEMIRE") corporate family rating to Ba3 from Ba2. Consequently, Moody's downgraded the senior unsecured rating of its €600 million notes maturing in 2024 to Ba3 from Ba2. The outlook on the ratings remains stable.

RATINGS RATIONALE

After a first dividend distribution of EUR 57m in Q3 2020, DEMIRE announced another request from majority shareholders Apollo and Wecken Group (together holding 90.7%) to distribute a second dividend amounting to EUR 65m by Q2 2021. Pro-forma for this second dividend distribution and including signed disposals as well as the recent acquisition of a 50% stake in the CIELO office property in Frankfurt, the company's loan-to-value (LTV) will be at around 54% and net debt to EBITDA will increase to around 15x.

A second significant dividend distribution within a very short timeframe appears aggressive in the context of a still uncertain economic backdrop. Moreover, it will position the company's leverage outside of its publicly communicated financial policy of a maximum loan-to-value ("LTV") of 50% and with limited headroom vs. max 60% LTV covenant for incurring additional financial indebtedness under the senior unsecured notes' documentation.

We expect Moody's adjusted debt to assets to reach 55% per year-end 2021 and net debt to EBITDA to be around 15.7x. Those credit ratios leave the company with very limited financial flexibility to withstand challenging operating conditions ahead including increased business insolvencies, reduced leasing activity, weaker rental growth prospects and downside pressure on capital values. Accordingly, we expect the company's credit ratios to further weaken and thus to be more commensurate with a Ba3 rating.

The rating remains supported by (i) the company's well-diversified portfolio of commercial real estate assets in secondary locations in Germany, focused on office properties but also including retail and logistics properties; (ii) DEMIRE's solid operating performance, notwithstanding coronavirus-driven business disruptions, backed by integrated business model and active portfolio management, which have resulted in a higher occupancy rate per year-end 2020 and (iii) adequate liquidity following the refinancing activities of 2019, with no debt maturities until 2024 and a large unencumbered asset base.

The Ba3 corporate family rating also reflects the company's main credit challenges arising from (i) its private-equity dominated ownership structure and its demonstrated more aggressive financial approach to shareholder distributions than we had previously factored into the rating (ii) the economic fallout in 2020, rising unemployment in Germany and a fragile economic recovery in 2021 which will continue putting pressure on the rental cycle and investment sentiment; and (iii) a small and lower-quality asset portfolio, compared with higher-rated peers.

RATIONALE FOR STABLE OUTLOOK

The stable outlook reflects our expectation that despite the tough economic climate, DEMIRE's operating results are likely to remain solid, resulting in a financial leverage that is in line with our Ba3 rating guidance. We expect Moody's adjusted debt to assets to remain between 54% to 56% and net debt to EBITDA to be between 15.5x -14.5x over the next 12 to 18 months. Fixed- charge coverage ratio will likely remain at a solid level of around 3x.

If contrary to our expectations, the company would make further shareholder distributions or aggressively financed acquisitions resulting in company's LTV creeping up towards 60%, this would lead to a negative rating action.

FACTORS THAT COULD LEAD TO AN UPGRADE OR DOWNGRADE OF THE RATINGS

FACTORS THAT COULD LEAD TO A DOWNGRADE

DEMIRE's rating could come under pressure if sustained coronavirus-driven business disruptions translate into greater stress for its retail tenants and thus weaker rental income or occupancy than currently anticipated in our base case. Other factors that could lead to a downgrade include:

- Additional shareholder distributions or debt-funded acquisitions resulting in DEMIRE further departing from or relaxing its current financial policy

- Deterioration of the asset quality within the portfolio or increasing vacancy rate

- Moody's-adjusted gross debt to total assets increases to above 60%, accompanied by an increasing trend in net debt to EBITDA from current level

- Moody's-adjusted fixed charge coverage falls below 2.25x

- The company fails to maintain good liquidity or refinance debt maturities well in advance

FACTORS THAT COULD LEAD TO AN UPGRADE

A rating upgrade could result from:

- Track record of sustaining leverage in line with its financial policy

- Moody's-adjusted debt to total assets sustained below 55%, in combination with net debt to EBITDA reverting to pre covid-19 level

- Sustained solid operating performance, reflected by growing and higher quality property portfolio, with at least a stable occupancy ratio

- Sustained strong Moody's-adjusted fixed charge coverage at above 2.75x

ENVIRONMENTAL, SOCIAL AND GOVERNANCE CONSIDERATIONS

DEMIRE's rating considers its private-equity dominated ownership structure and the associated aggressive financial policy to that, which is tolerant of higher leverage, debt-funded M&A and recapitalisation measures. As such the envisaged dividend distribution is credit negative, weakening the company's debt metrics in a challenging economic environment.

PRINCIPAL METHODOLOGY

The principal methodology used in these ratings was REITs and Other Commercial Real Estate Firms published in September 2018 and available at https://www.moodys.com/researchdocumentcontentpage.aspx?docid=PBC_1095505. Alternatively, please see the Rating Methodologies page on www.moodys.com for a copy of this methodology.

COMPANY PROFILE

Headquartered in Langen, Germany, DEMIRE Deutsche Mittelstand Real Estate AG (DEMIRE) is a public listed commercial real estate company with focus on offices in secondary locations across Germany. The company's portfolio value stands at circa €1.4 billion. The company's contracted rental income amounts to around €86 million over a 4.8 year weighted average lease term (WALT). DEMIRE is listed on the Frankfurt stock exchange and had a market capitalization around €501 million as of 30 March 2021. Apollo-managed funds and Wecken Group together hold 90.7% of DEMIRE's shares.

REGULATORY DISCLOSURES

For further specification of Moody's key rating assumptions and sensitivity analysis, see the sections Methodology Assumptions and Sensitivity to Assumptions in the disclosure form. Moody's Rating Symbols and Definitions can be found at: https://www.moodys.com/researchdocumentcontentpage.aspx?docid=PBC_79004.

For ratings issued on a program, series, category/class of debt or security this announcement provides certain regulatory disclosures in relation to each rating of a subsequently issued bond or note of the same series, category/class of debt, security or pursuant to a program for which the ratings are derived exclusively from existing ratings in accordance with Moody's rating practices. For ratings issued on a support provider, this announcement provides certain regulatory disclosures in relation to the credit rating action on the support provider and in relation to each particular credit rating action for securities that derive their credit ratings from the support provider's credit rating. For provisional ratings, this announcement provides certain regulatory disclosures in relation to the provisional rating assigned, and in relation to a definitive rating that may be assigned subsequent to the final issuance of the debt, in each case where the transaction structure and terms have not changed prior to the assignment of the definitive rating in a manner that would have affected the rating. For further information please see the ratings tab on the issuer/entity page for the respective issuer on www.moodys.com.

For any affected securities or rated entities receiving direct credit support from the primary entity(ies) of this credit rating action, and whose ratings may change as a result of this credit rating action, the associated regulatory disclosures will be those of the guarantor entity. Exceptions to this approach exist for the following disclosures, if applicable to jurisdiction: Ancillary Services, Disclosure to rated entity, Disclosure from rated entity.

The ratings have been disclosed to the rated entity or its designated agent(s) and issued with no amendment resulting from that disclosure.

These ratings are solicited. Please refer to Moody's Policy for Designating and Assigning Unsolicited Credit Ratings available on its website www.moodys.com.

Regulatory disclosures contained in this press release apply to the credit rating and, if applicable, the related rating outlook or rating review.

Moody's general principles for assessing environmental, social and governance (ESG) risks in our credit analysis can be found at https://www.moodys.com/researchdocumentcontentpage.aspx?docid=PBC_1243406 .

At least one ESG consideration was material to the credit rating action(s) announced and described above.

The Global Scale Credit Rating on this Credit Rating Announcement was issued by one of Moody's affiliates outside the UK and is endorsed by Moody's Investors Service Limited, One Canada Square, Canary Wharf, London E14 5FA under the law applicable to credit rating agencies in the UK. Further information on the UK endorsement status and on the Moody's office that issued the credit rating is available on www.moodys.com.

Please see www.moodys.com for any updates on changes to the lead rating analyst and to the Moody's legal entity that has issued the rating.

Please see the ratings tab on the issuer/entity page on www.moodys.com for additional regulatory disclosures for each credit rating.

Ana Luz Silva Robles
Asst Vice President - Analyst
Corporate Finance Group
Moody's Deutschland GmbH
An der Welle 5
Frankfurt am Main 60322
Germany
JOURNALISTS: 44 20 7772 5456
Client Service: 44 20 7772 5454

Anke Rindermann
Associate Managing Director
Corporate Finance Group
JOURNALISTS: 44 20 7772 5456
Client Service: 44 20 7772 5454

Releasing Office:
Moody's Deutschland GmbH
An der Welle 5
Frankfurt am Main 60322
Germany
JOURNALISTS: 44 20 7772 5456
Client Service: 44 20 7772 5454

MJKK and MSFJ also maintain policies and procedures to address Japanese regulatory requirements.