MOODY'S

Rating Action: Moody's downgrades DEMIRE's CFR to Caa1; outlook remains negative

07 Jul 2023

Frankfurt am Main, July 07, 2023 -- Moody's Investors Service (Moody's) has today downgraded DEMIRE Deutsche Mittelstand Real Estate AG's ("DEMIRE" or "the company") long term corporate family rating ("CFR") to Caa1 from B3. At the same time the senior unsecured rating of its €600 million note issuance maturing in October 2024 was downgraded to Caa2 from Caa1. The outlook remains negative.

A full list of affected ratings can be found at the end of this press release.

RATINGS RATIONALE

The downgrade to Caa1 reflects increased refinancing risk following the withdrawal of the buyer of DEMIRE's LogPark logistics property from the purchase agreement. The disposal of LogPark is a key component of DEMIRE's effort to increase liquidity sufficiently to address the roughly €500 million remaining senior unsecured bond maturity in October 2024 and around €150 million secured debt maturing during 2024. The downgrade also reflects a continued weak business environment for real estate landlords in Germany that makes disposals more difficult and getting new secured debt more costly and difficult, combined with less time available to generate sufficient liquidity to facilitate a bond repayment.

Moody's expected the disposal of LogPark to generate around €80 million of net liquidity next to addressing the refinancing of more than €35 million of secured debt attached to the asset that matures in Q3 2024. Moody's still expects LogPark to be a key and marketable asset for disposal to meet refinancing requirements, even if uncertainty of timing and proceeds has increased. Hence the cancelled disposal adds to the execution risk for asset disposals and asset encumbrance sufficient to address the 2024 senior unsecured bond and loan maturities.

One of the complexities in refinancing the bond maturity are the limitations in crystallising the asset values at Fair Value REIT AG that has a lower LTV than DEMIRE on a standalone basis. Hence reported consolidated financial metrics d not fully reflect the financial position of DEMIRE on a standalone basis that is subject to refinancing. As of March 2023, Moody's adjusted gross debt/total assets was 56.2% on a consolidated basis, while separating DEMIRE (excluding Fair Value REIT AG's asset and liabilities) would increase this ratio to around 65% before giving equity value for the stake in Fair Value REIT AG.

Our credit metrics expectations have weakened moderately given slightly higher uncertainties about disposal proceeds and property values and tightening availability of financing rising prices of debt. Moody's estimates Moody's-adjusted consolidated debt/total assets to be around 50-55% in 2024 on a consolidated basis. This includes an assumption of up to 15% further fall in property values.

The interest cover post repayment/refinancing of the bond is not very predictable at this point. Our forward view looks at 2024 more than 2023, as fixed charge coverage pre refinancing of the bond maturity is sufficient to cover interest expense. Both EBITDA as well as interest rates payable depend strongly on disposal success, as much as on interest rates on new debt that is required for refinancing. Moody's expects interest cover to drop to 1.1-1.5x from 2.5x as of March 2023 because lower debt amounts will cost significantly more than the current 1.7% reported interest cost.

The notching of the senior unsecured notes below the CFR reflects the anticipated change of the capital structure towards a largely secured one. Recoveries on the secured debt that currently have very moderate LTVs will be substantially higher than for the unsecured debt that faces the risk of restructuring or a distressed exchange.

RATIONALE FOR THE OUTLOOK

The negative outlook reflects increasing uncertainty around property lending and less time remaining to refinance the bond. We expect further disposal activity as well as proceeds from secured financing in the next six months to be key for DEMIRE's refinancing efforts. The inability of a timely refinancing and a potential debt restructuring or distressed exchange could result in further negative rating pressure over the next months.

LIQUIDITY

Liquidity remains the key credit drivers for DEMIRE. The company faces a significant debt maturity wall, as €668 million out of €781 million outstanding debt is due in 2024. The company had €73 million of cash available as of Q1 2023 (including cash at Fair Value REIT AG level which Moody's considers not to be available for bond refinancing). DEMIRE has since concluded the disposal of the Ulm asset for an undisclosed amount, closed a second discounted bond buy-back that reduced the maturity wall in 2024 by around €51 million, and continues to actively pursue additional secured debt refinancing. The unexpected withdrawal of the purchase agreement for the LogPark logistics property exerts a critical liquidity pressure on the timely execution and refinancing risk the company is facing to honor its debt maturities by October 2024. With no public announcement of key shareholders has been made, no shareholder support is visible at this point.

Moody's perceives the refinancing risk of the secured debt maturities on existing encumbered assets to be lower, eve if some assets may require asset management activities to facilitate a refinancing or re-leveraging.

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

Factors that could lead to an upgrade:

A rating upgrade is less likely to occur given the negative outlook, but it can occur if

• DEMIRE succeeds in disposing material asset volumes with moderate discounts and thereby secures repayment of the majority of the 2024 senior unsecured bond maturity

• The company succeeds in raising sufficient alternative debt financing to enable a bond refinancing at a sustainable interest cover

Factors that could lead to a downgrade:

• Failure to raise material further proceeds to address the refinancing of the upcoming debt maturity through disposal proceeds, as well as through encumbering existing assets

• A deterioration in the lending appetite for secondary German real estate assets making both disposals and refinancing from secured banks less likely

• Weaker operational performance of the asset portfolio

• Expected recovery rates in case of a default or distressed exchange to be lower than anticipated

LIST OF AFFECTED RATINGS

Downgrades:

..Issuer: DEMIRE Deutsche Mittelstand Real Estate AG

.... LT Corporate Family Rating, Downgraded to Caa1 from B3

....Senior Unsecured Regular Bond/Debenture, Downgraded to Caa2 from Caa1

Outlook Action:

..Issuer: DEMIRE Deutsche Mittelstand Real Estate AG

....Outlook, Remains Negative

PRINCIPAL METHODOLOGY

The principal methodology used in these ratings was REITs and Other Commercial Real Estate Firms published in September 2022 and available at https://ratings.moodys.com/rmc-documents/393395. Alternatively, please see the Rating Methodologies page on https://ratings.moodys.com for a copy of this methodology.

COMPANY PROFILE

DEMIRE Deutsche Mittelstand Real Estate AG (DEMIRE) is a publicly listed commercial real estate company with a focus on offices in secondary locations across Germany. The company's portfolio has an aggregate portfolio value of around €1.3 billion with an annualised contracted rent of €84.1 million as of 31 March 2023.

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 on https://ratings.moodys.com/rating-definitions.

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 issuer/deal page for the respective issuer on https://ratings.moodys.com.

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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://ratings.moodys.com/documents/PBC_1288235.

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 https://ratings.moodys.com.

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