S&P Global Ratings

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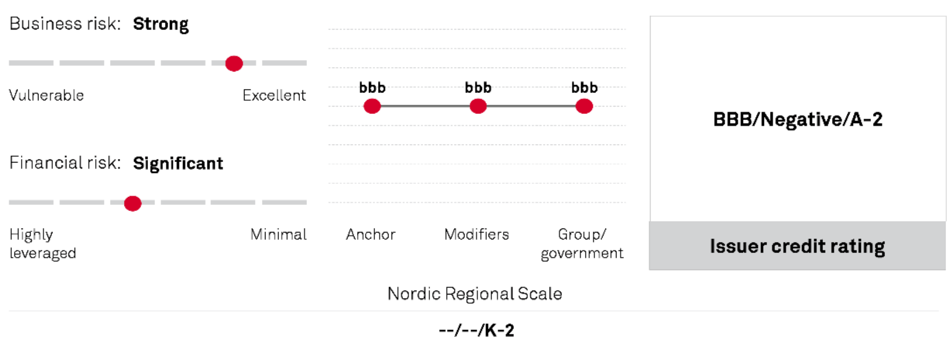
Akelius Residential Properties AB

April 28, 2022

Ratings Score Snapshot



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Credit Highlights

Overview

Key strengths	Key risks
Diversified income-producing portfolio, with residential real estate in large metropolitan cities where demand remains solid and supply limited.	Lower-than-peers' EBITDA interest coverage close to 2x predisposals, which will take some time to recover as portfolio base regrows.
Moderate asset portfolio valued at approximately €6.0 billion at end-2021, spread across 17,770 apartments with a large tenant base.	Weak debt to EBITDA of above 20x, although distorted by asset rotation.
Good operational track record, with a high occupancy rate of 97.4% (excluding units for refurbishment), supporting recurring cash flow generation.	Uncertainties on high inflation and rising interest rates, which could burden EBITDA margin and funding costs needed to execute growth strategy.
Good access to diversified funding sources, including capital markets.	

Following the significant amount of disposals in 2021, we expect Akelius Residential Properties AB (Akelius) to expand its portfolio in the coming years, in line with its public target to restore its portfolio to previous levels and its revised business strategy, including a focus on cost efficiency and acquisition of higher-yielding rental properties. Akelius is likely to expand its portfolio over the next 12-24 months, and aspires to restore its portfolio to the previous level of 50,000 apartments. At this stage, we have limited visibility on the timing and details of the reinvestment strategy. But, we expect Akelius to expand into existing markets with favorable demand and supply characteristics, primarily in North America where yields are higher on average compared with regulated European markets (for more information, see "Swedish Property Company Akelius Outlook Revised To Negative On Planned Asset Disposal And Uncertainty On Proceeds' Use, Sept. 29, 2021", published on RatingsDirect). Akelius is shifting its business model to focus on acquiring higher-yield rental properties with strong cash flow generation capabilities and high occupancy levels, from acquiring properties with appreciation potential through expensive upgrading. We believe that the adjusted strategy could benefit the company's cash flow generation and debt service capacity, which historically have been weaker relative to peers.

We believe that there are some integration risks in Akelius reinvesting its portfolio. In December 2021, Akelius acquired 861 apartments in Austin, Texas for €192 million. Austin is a metropolitan city, and we note its favorable population and job growth in the area. However, expanding to new cities increases integration risks, and can put pressure on margins in the short term before a sufficient scale is reached to be profitable in the market.

We anticipate that higher inflation and interest rates could negatively affect Akelius' operating performance, as well as its reinvestment strategy. We anticipate margins to increase from current levels, due to the geographic mix and cost saving programs initiated in late 2020, with an overall cost reduction of €42 million by end-2022, when the program is fully implemented. Yet, in our view, increasing inflation could be a challenge for Akelius, as we understand most of its U.S. business has a lease structure where utility costs cannot be transferred to tenants, but heating is already included in the fixed rent. We consider that this could negatively affect margins, which are already lower compared with peers (40.1% as per fourth-quarter 2021). Although, strong locations could act as a mitigant and facilitator for the company to compensate higher operating costs. For 2022, we assume a slightly positive, but still conservative, asset valuation growth of 1%-2% in 2022-2023, despite current trends in the credit market. Although, we consider that higher interest rates may slow Akelius' reinvestment strategy as asset funding becomes more difficult due to a negative effect on the risk premium in the wake of higher interest rates.

Over the medium term, we expect Akelius' leverage to increase, in line with its financial policy of a reported net loan-to-value (LTV) of a maximum of 45%. As of fourth quarter 2021, Akelius' reported cash position exceeded its gross debt by €2.05 billion. We understand that the company plans to use the proceeds from the recent disposal for a net cash dividend payout of €2.0 billion as well as repayment of several debt positions, including a partial redemption of its hybrid bonds. Throughout 2022, we expect a further €800 million repayment of senior debt. We forecast that Akelius will continue to restore its portfolio in line with public targets, as well as the financial policy that allows for a maximum LTV of 45%, translating into our adjusted ratio of debt-to-debt plus equity of about 55% (within our downside thresholds for the current rating). We believe that the company will reach its target within the next 24 months. That said, its ratio of debt to EBITDA will likely remain weak at above 20x, distorted by its acquisition pipeline. EBITDA interest coverage should be restored to close to 2x within the next 12 months, still relatively weak compared with other investment-grade rated residential real estate peers.

Outlook

The negative outlook reflects our view that we could downgrade Akelius in the next 12-24 months if its significantly reduced 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 portfolio sale to restore its existing asset base or strengthen its credit profile and instead mainly distributes the proceeds to unitholders.

Downside scenario

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

Upside scenario

We could revise the outlook to stable if Akelius restores its cash flow similar to previous levels, in a timely manner. This would indicate that the company's reinvestments will continue with 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 toward 2.4x. We would also expect to see a new financial policy commensurate with these levels.

Our Base-Case Scenario

Assumptions

- Positive annual like-for-like rental income growth of 3% to 5% over the next two years, on the back of expected inflation in operating economies as well as some positive rent renegotiations and increase in in-place rents.
- Indexation in North America of about 2.0%-4.0% over the next 12 months, with GDP growth of about 3.2% and 2.3% for the U.S. and Canada in 2022 and expected inflation rates of 6.0% and 3.4% respectively over the same period.
- Like-for-like portfolio revaluation to remain positive of 1%-2% in 2022 and 2023.
- Stable capital expenditure (capex) of €300 million-€400 million annually, in line with Akelius' operating strategy.
- Akelius will be a net buyer and expand its portfolio in the coming years with limited asset disposals.
- Net cash dividend of about €2 billion in 2022, in line with company's recent announcement.
- Average cost of debt to remain below 2%.

Key metrics

Akelius Residential Property AB--Key Metrics*

Mil. €	2020a	2021a	2022e	2023f	2024f
EBITDA	201	85	110-120	140-150	165-175
EBITDA margin (%)	42.7	40.1	44-45	44-45	44-45
Capital expenditure	392	367	200-400	200-400	200-400
Debt	5,306	N/A	1800-2000	3500-3700	4400-4500
Debt to EBITDA (x)	26.4	N/A	16-18	25-27	25-27
EBITDA interest coverage (x)	2.0	1	1.5-2.0	2.0-2.5	2.0-2.5
Debt to debt plus equity (%)	47.5	N/A	26-28	41-43	44-46

*All figures adjusted by S&P Global Ratings. a--Actual. e--Estimate. f--Forecast. N/A--Not applicable.

Company Description

Sweden-based Akelius is a privately owned real estate company, focusing on residential assets. As of Dec. 31, 2021, the company's portfolio stood at €6.0 billion, with properties in eight cities across four countries, including Toronto (18%), Montreal (17%), London (16%), and Washington D.C. (15%). The company focuses on the 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).

Akelius Residential Property AB--Portfolio Summary

Segment focus	Residential
Total portfolio value (Bil. €)	6.02
Total units owned	17,770
Portfolio occupancy* (%)	97.4

Exposure to number of countries	4
Exposure to number of cities	8
Proportion of upgraded apartments (%)	57.8
Proportion of apartments, rented out below market rent (%)	30
Capitalization rate (%)	3.99

All data as of Dec. 31, 2021. *Excluding apartments vacant due to renovation or planned sales.

Peer Comparison

Akelius Residential Property AB--Peer Comparison--Financial Metrics

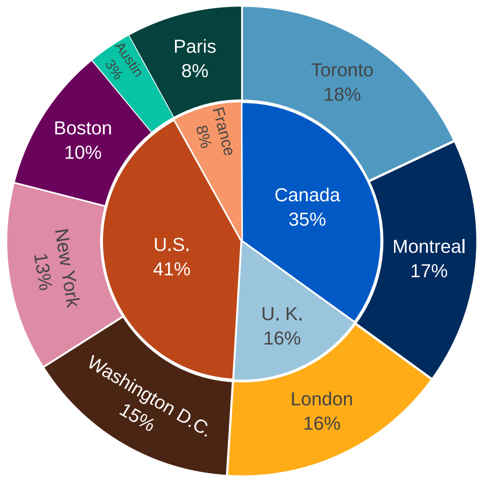
	Akelius Residential Property AB	Vonovia SE	Fastighets AB Balder	Heimstaden Bostad AB	Samhallsbyggnadsbolaget i Norden AB (publ)
Foreign currency issuer credit rating	BBB/Negative/A-2	BBB+/Positive/A-2	BBB/Stable/--	BBB/Stable/--	BBB-/Positive/A-3
Local currency issuer credit rating	BBB/Negative/A-2	BBB+/Positive/A-2	BBB/Stable/--	BBB/Stable/--	BBB-/Positive/A-3
Period	Annual	Annual	Annual	Annual	Annual
Period ending	2021-12-31	2021-12-31	2021-12-31	2021-12-31	2021-12-31
Mil.	EUR	EUR	EUR	EUR	EUR
Revenue	212.0	2,730.8	870.9	899.2	577
EBITDA	85.0	1,850.3	631.8	462.7	370
Funds from operations (FFO)	3.3	1,315.4	444.8	190.6	204
Interest expense	87.7	489.8	149.0	168.1	124
Cash flow from operations	124.3	1,394.1	212.0	319.4	378
Capital expenditure	367.0	1,730.1	728.4	522.8	383
Free operating cash flow (FOCF)	(242.7)	(336.0)	(516.3)	(203.3)	(5)
Dividends paid	987.3	1,516.2	19.5	464.3	162
Cash and short-term investments	1,193.0	1,315.2	245.0	1,897.0	957
Debt	0.0	47,185.7	10,967.6	15,212.6	8,506
Equity	7,534.5	36,545.1	9,035.2	13,954.9	7,309
Debt and equity	7,534.5	83,730.8	20,002.8	29,167.5	15,815
Valuation of investment property	6,020.0	95,073.9	18,392.3	300,854	14,522
Adjusted ratios					
Annual revenue growth (%)	(55.0)	15.4	10.1	37.6	16
EBITDA margin (%)	40.1	67.8	72.5	51.5	64
Return on capital (%)	0.9	2.8	5.5	2.4	5
EBITDA interest coverage (x)	1.0	3.8	4.2	2.8	3
Debt/EBITDA (x)	0.0	25.5	17.4	32.9	23
FFO/debt (%)	NM	2.8	4.1	1.3	2
Debt/debt and equity (%)	0.0	56.4	54.8	52.2	54

Business Risk

The disposals of Akelius' German and Scandinavian assets, which accounted for a book value of €7.5 billion (sold for a price of €9.1 billion) reduced Akelius' property portfolio value to €6.0 billion at end-2021. Despite the reduction in portfolio value, our assessment of Akelius' business risk profile continues to reflect our view of its solidly sized and stable residential property portfolio, with exposure to real estate markets where demand-supply trends remain favorable. The current portfolio is tilted toward North America with 76% of portfolio value located across Toronto, Montreal, Washington D.C., New York, Boston, and Austin, and the remaining 24% in Europe, mainly London and Paris. Akelius is in the process of regrowing its portfolio and has publicly communicated that it will speed up its acquisitions pace in 2022 in the U.S., Canada, France, and the U.K.

Akelius--Geographical Portfolio Spread

% of total portfolio value

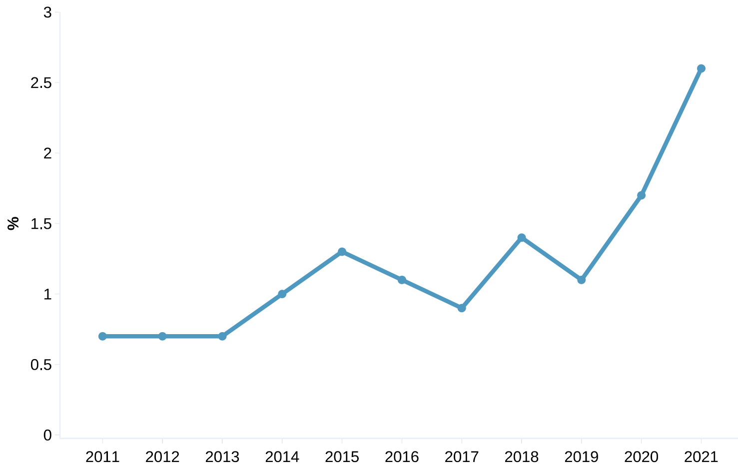


Source: S&P Global Ratings based on company report as of Dec. 31, 2021.

Akelius has broad asset and tenant diversity of nearly 18,000 units. Asset quality ranges from average to good, with 58% of properties modernized during recent years. In our view, the company's strategy of long-term ownership of residential properties in A and B locations with no development activities supports its business risk assessment. The average apartment size is 30 square meters-80 square meters, with smaller apartments in Paris and London compared with larger apartments in Washington D.C. and Austin, in line with what we observe for other rated residential players in Akelius' markets.

In our view, the company has a positive operational track record. Like-for-like rental income grew by 1.5% in 2021, a year characterized by portfolio transformation and some minor effects from the pandemic, mainly in markets like London or New York. Vacancy has remained low at 2.6% in 2021 (excluding vacant premises for renovation).

Akelius--Real Vacancy Rate*



Source: S&P Global Ratings based on company report as of Dec. 31, 2021.
*The total number of vacant apartments less the number of apartments vacant due to renovation work or planned sales, in relation to the total number of apartments.

In England and France (about 24% of the portfolio), Akelius is mostly able to transfer its rising utility costs to the tenant. However, in the U.S. and Canada, rising utility costs may not be fully covered by tenants and could negatively affect margins. In the light of current rising energy costs and inflation, we anticipate that a potential negative effect on profitability will be partially offset in some regions, where rent contracts are linked to the Consumer Price Index. We expect like-for-like rental income growth to remain positive but low over the forecasted period.

Akelius benefits from both country and city diversification. However, we believe that the company can achieve only limited economies of scale in some of its markets compared with its rated peers in the residential segment, particularly those which focus more on domestic markets. Given Akelius' new strategic direction, expanding to higher yielding assets while reducing renovation and refurbishment needs, we expect lower capex and an increased focus on cost efficiency.

Financial Risk

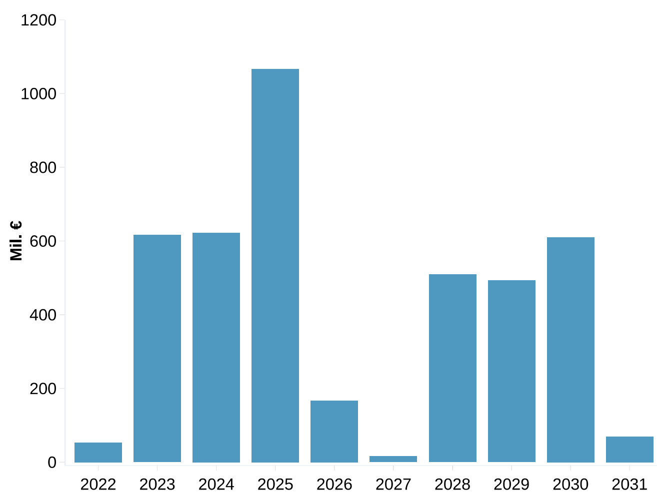
As of Dec. 31, 2021, Akelius has no net debt, due to a large amount of about €6.2 billion of liquid available investments including cash versus a gross debt position of €4.7 billion. We expect Akelius to reposition its capital structure during 2022 and 2023, and align its net debt position with its financial policy target of a reported LTV of maximum 45% and an EBITDA interest coverage of 2x. The company has also issued common equity of about €4.1 billion in mid-April and paid a special dividend of €6.1 billion, leading to a cash out of a net dividend of approximately €2 billion. Additionally, the company has announced a tender offer to buy back hybrid bonds for a maximum amount of €350 million and we expect Akelius to redeem a further €800 million of senior debt with most of it occurring within the second quarter of 2022.

Over the next 12-24 months, we expect the company's leverage to increase to an adjusted ratio of debt to debt plus equity ratio of around 45%, given the company's strategy to restore its portfolio size similar to predisposal levels. The adjusted EBITDA interest coverage ratio stood at only 1.0x as of Dec. 31, 2021, however, excluding the EBITDA contribution of its discontinued operations. Over the medium term, we expect its EBITDA interest coverage ratio to steadily improve toward 2x, due to the company's plan to acquire higher yielding assets. That said, we forecast the company's ratio of debt to EBITDA to remain elevated and distorted by its growth pipeline, well above 20x. The company's current cost of debt is relatively low at 1.51% but we remain cautious on short-to-near term refinancing needs, as a result of the current rising interest rate environment. For the next 12 to 24 months, we forecast its cost of debt will remain below 2%.

Debt maturities

As of Dec. 31, 2021, the average length of Akelius' debt maturities was 4.5 years. The company has some refinancing needs in the next three years, especially in 2025 where more than €1 billion of its debt matures. We understand that Akelius will address the upcoming maturities well ahead of due dates, partially with the proceeds of the recent disposals.

Akelius--Debt Maturity Profile



Source: S&P Global Ratings based on company report as of Dec. 31, 2021.

EMEA REIT Financial Summary

Akelius Residential Property AB--Financial Summary

Period ending	Dec-31-2016	Dec-31-2017	Dec-31-2018	Dec-31-2019	Dec-31-2020	Dec-31-2021
Reporting period	2016a	2017a	2018a	2019a	2020a	2021a
Display currency (mil.)	EUR	EUR	EUR	EUR	EUR	EUR
Revenues	4,109	469	482	496	471	212
EBITDA	2,217	231	236	244	201	85
Funds from operations (FFO)	736	111	83	83	92	3
Interest expense	1,485	136	154	141	102	88
Operating cash flow (OCF)	551	92	95	43	123	124
Capital expenditure	2,989	288	349	478	392	367

Akelius Residential Property AB--Financial Summary

Dividends paid	5,233	857	832	34	124	987
Cash and short-term investments	137	16	13	19	250	1,193
Debt	42,875	5,035	6,048	5,103	5,307	0
Common equity	36,004	4,595	5,327	5,776	5,874	7,535
Valuation of investment property	84,634	10,589	12,340	11,891	12,021	6,020
Adjusted ratios						
EBITDA margin (%)	54.0	49.3	49.0	49.2	42.7	40.1
EBITDA interest coverage (x)	1.5	1.7	1.5	1.7	2.0	1.0
Debt/EBITDA (x)	19.3	21.8	25.6	20.9	26.4	0.0
Debt/debt and equity (%)	54.4	52.3	53.2	46.9	47.5	0.0

Liquidity

We assess Akelius' liquidity as adequate. This is based on our forecast that the company's liquidity sources will exceed its funding needs by about 1.6x over the next 12 months.

Our liquidity assessment is also supported by Akelius' positive track record of accessing capital markets, and its good relationships with banks in its operating countries.

Principal liquidity sources

- Unrestricted cash and cash equivalents of about €6.4 billion as of Dec. 31, 2021, of which about €5 billion relate to financial assets which can be liquidated immediately;
- About €136 million of undrawn and committed credit lines maturing in more than 12 months; and
- Our forecast of positive cash funds from operations of about €45 million-€50 million for the next 12 months.

Principal liquidity uses

- About €53 million of short-term debt maturities, including amortization from Akelius' bank loans;
- About €50 million of committed capex for the next 12 months; and
- Approximately €2.1 billion of net cash dividends, including that related to hybrid bondholders (postequity issuance).

Covenant Analysis

Compliance expectations

We understand that Akelius has some covenants for its existing bond issuances and credit lines. Most relate to a maximum LTV ratio and a minimum EBITDA interest coverage threshold. We estimate that the headroom for these covenants is adequate (at more than 10%) and that the company will maintain sufficient headroom.

Requirements

Akelius has to comply with the following incurrences across its bond issues under the euro medium term note program:

- Net interest-bearing debt to total assets of no more than 60%; 39% as of 2021.
- Adjusted profit before taxes to total interest expenses of at least 1.5x; 2.5x as of 2021.
- Unencumbered assets to unsecured debt greater than 125%; 189% as of 2021.

- Secured debt to total assets of no more than 45% (incurrence based); 9% as of 2021.

Environmental, Social, And Governance

ESG Credit Indicators

E-1	**E-2**	E-3	E-4	E-5	S-1	**S-2**	S-3	S-4	S-5	G-1	**G-2**	G-3	G-4	G-5

ESG credit indicators provide additional disclosure and transparency at the entity level and reflect S&P Global Ratings' opinion of the influence that environmental, social, and governance factors have on our credit rating analysis. They are not a sustainability rating or an S&P Global Ratings ESG Evaluation. The extent of the influence of these factors is reflected on an alphanumerical 1-5 scale where 1 = positive, 2 = neutral, 3 = moderately negative, 4 = negative, and 5 = very negative. For more information, see our commentary "ESG Credit Indicators: Definition And Applications," published Oct. 13, 2021.

ESG factors are an overall neutral consideration in our credit rating analysis of Akelius Residential Property. The company currently doesn't have green certified buildings in the portfolio, but we understand that it aims to reduce its carbon emissions by 50% in 2025 versus 2018.

Issue Ratings--Subordination Risk Analysis

Capital structure

As of Dec. 31, 2021, the company's debt capital structure comprised 5% of secured debt and 95% of unsecured debt. Unsecured bonds are issued under Akelius Residential Property AB and its financing vehicle Akelius Residential Property Financing B.V.

Analytical conclusions

We assess the issue ratings on Akelius' senior unsecured bonds at 'BBB', in line with the issuer credit rating. This is because the company's exposure to secured debt is limited and its secured debt to total assets ratio is less than 5%, which is well below our 40% threshold for notching down issue ratings on debt.

Regarding the outstanding subordinated hybrid bond, we lower the issue rating by two notches to 'BB+', one notch for subordination and one for deferability.

Rating Component Scores

Foreign currency issuer credit rating	**BBB/Negative/A-2**
Local currency 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**
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)
Stand-alone credit profile	**bbb**

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: Methodology: Industry Risk, Nov. 19, 2013
- General Criteria: Country Risk Assessment Methodology And Assumptions, 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

Ratings Detail (as of April 28, 2022)*

Akelius Residential Property AB	
Issuer Credit Rating	BBB/Negative/A-2
Nordic Regional Scale	--/--/K-2

Ratings Detail (as of April 28, 2022)*

Senior Unsecured		BBB
Subordinated		BB+
Issuer Credit Ratings History		
29-Sep-2021		BBB/Negative/A-2
03-Nov-2017		BBB/Stable/A-2
03-Mar-2017		BBB-/Positive/A-3
03-Nov-2017	*Nordic Regional Scale*	--/--/K-2
24-Aug-2015		--/--/K-3

*Unless otherwise noted, all ratings in this report are global scale ratings. S&P Global Ratings credit ratings on the global scale are comparable across countries. S&P Global Ratings credit ratings on a national scale are relative to obligors or obligations within that specific country. Issue and debt ratings could include debt guaranteed by another entity, and rated debt that an entity guarantees.