MOODY'S INVESTORS SERVICE

Rating Action: Moody's assigns P-3 short-term issuer rating to TAG Immobilien AG

01 Oct 2018

London, 01 October 2018 -- Moody's Investors Service (Moody's) has today assigned a first-time Prime-3 (P-3) short-term issuer rating to TAG Immobilien AG ("TAG"), a residential real estate company that owns and manages around 82,400 multi-family residential units across Germany. TAG's Baa3 long-term issuer rating and the Stable outlook are unchanged.

RATINGS RATIONALE

TAG's liquidity is supported by positive operating cash flow generation, substantial cash balances and undrawn credit facilities and long dated debt maturities. These strengths are partly offset by limited unencumbered assets, the level of which, as at 30 June 2018, remain well below our expectations for the Baa3.

We anticipate positive operating free cash flow generation after dividends and broadly balanced net acquisitions and divestments over the next two years. As at 18 September 2018 TAG has €133 million cash on balance sheet after refinancing transactions completed in August 2018. Additionally, TAG has available credit lines totaling €121 million at the same date, all undrawn and available for general corporate purposes, with financial covenants and MAC clauses in line with the typical language used in bilateral loans with German banks.

Following the repayment of a €310 million bond in August 2018 (€191 million was left to be repaid), the company's near term debt maturities over the next 12-18 months are limited, with only €65 million in 2019. TAG has a very long dated average debt maturity of 8.8 years as of August 2018, which is slightly above its German residential peers and well above other European rated landlords.

Negatively, only 16% of TAG's assets are unencumbered as of 30 June 2018 (or pro-forma 12% for the repayment of the bond in August 2018), the lowest ratio across the rated residential peer group. Although we acknowledge that the company has limited refinancing needs for secured debt and will therefore only gradually be able to increase its unencumbered assets, the rating assigned factors in expectations of a gradual increase in unencumbered assets. Recent refinancing actions will result in this ratio recovering towards 20% by year end, a level that we however believe is still low compared to peers and in the context of the group's leverage.

TAG's Baa3 long-term issuer rating mainly reflects i) its focus on regulated affordable housing activities which result in stable rental income, ii) the broad tenant diversification derived from a sizeable portfolio of around 82,400 residential units valued at around €4.5 billion (total assets of €4.9 billion) across a number of regions in Germany, which we believe is one of the most stable European real estate markets, iii) a good coverage of fixed charges of 3.2x as at 30 June 2018 (YTD, 2.9x LTM), and iv) long dated debt maturities averaging 8.8 years.

These credit positives are partly offset by i) the secondary locations of the property portfolio in economically weaker regions in Eastern and Northern Germany, ii) improving but still relatively high vacancy rates especially if compared to other rated residential peers and iii) more limited financial flexibility compared to some peers, with unencumbered assets representing a low 12% of total assets as at 30 June 2018 pro-forma for the repayment of unsecured debt completed in August 2018.

TAG's leverage, measured as Moody's adjusted gross debt to total assets, stood at 53.0% as at 30 June 2018 and 56.8% at the end of 2016. We expect this ratio to further improve to around 51.0% before the end of 2018 driven by the repayment of debt already completed in August 2018. Whilst not factored in our 12-18 forward view, further leverage reduction could materialize through revaluation gains. The valuation of the property portfolio was performed annually until 2016, but since 2017 the valuation is conducted every six months. The last portfolio valuation was carried out by CBRE at 30 June 2018, resulting in a valuation gain of €230.0 million driven by yield compression (€194.8 million) and operational performance (€35.2 million). The next valuation will follow at 31 December 2018.

RATIONALE FOR THE OUTLOOK

The stable outlook reflects our expectations that TAG will improve its unencumbered assets ratio to around one third of total or its Moody's adjusted gross debt to assets ratio will improve well below 50% over the next 6-12 months.

WHAT COULD CHANGE THE RATING -- DOWN

» The short term rating could be revised downward if the long term issuer rating was downgraded to Ba1 or below, or if its liquidity deteriorated. Weakening liquidity and, in particular, drawings under a planned commercial paper program exceeding available committed liquidity could also put pressure on both the long term and short term ratings.

» Failure to improve the level of unencumbered assets to around a third of total would require the debt to assets ratio to be well below 50% for the assigned rating

» Fixed charges coverage below 2.25x

» Failure to maintain adequate liquidity

» A deterioration of market conditions for the German residential property sector, acquisitions of assets diluting the quality of the company's current portfolio could also generate negative rating pressure.

WHAT COULD CHANGE THE RATING - UP

» Unencumbered assets well above a third of total assets

» Gross debt to Total Assets sustained towards 45% (or well below 45% if unencumbered assets remain below one-third of total assets)

» Fixed charge coverage maintained above 3.0x

» An upgrade would also be conditional to the company maintaining stronger liquidity and improving market fundamentals.

The principal methodology used in this rating was REITs and Other Commercial Real Estate Firms published in September 2018. Please see the Rating Methodologies page on www.moodys.com for a copy of this methodology.

Headquartered in Hamburg, TAG is listed on the MDAX Frankfurt Stock Exchange with a market capitalisation of €3.0 billion as of 26 September 2018 (a 33.5% premium to reported NAV as of 30 June 2018).

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