MOODY'S INVESTORS SERVICE

CREDIT OPINION

23 July 2020

Update

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RATINGS

TAG Immobilien AG

Domicile	Hamburg, Germany
Long Term Rating	Baa3
Type	LT Issuer Rating - Dom Curr
Outlook	Stable

Please see the ratings section at the end of this report for more information. The ratings and outlook shown reflect information as of the publication date.

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TAG Immobilien AG

Update to credit analysis

Summary

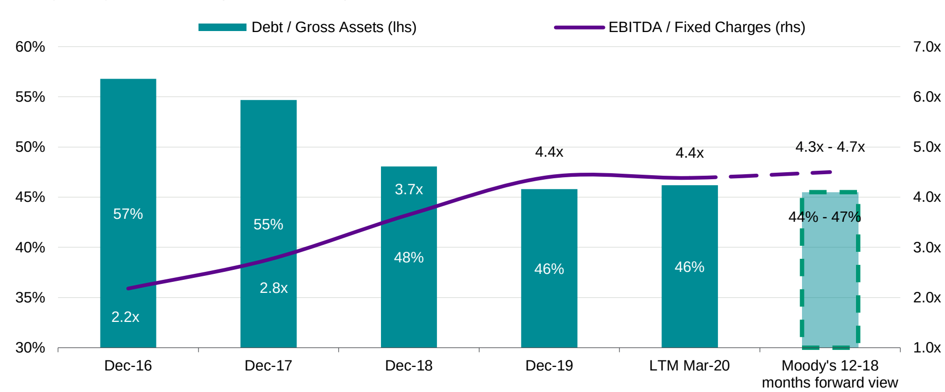
TAG Immobilien AG's (TAG) Baa3 long-term issuer rating reflects the company's focus on regulated affordable housing activities that generate stable rental income; broad tenant diversification in a portfolio of around 84,900 units, valued at around €5.3 billion (€5.5 billion including Poland) across a number of regions in Germany (Aaa stable), one of the most stable European real estate markets; strong debt/gross assets, fixed-charge coverage ratios for the rating category and stable net debt/EBITDA, all of which we expect to remain broadly stable; and long-dated debt maturities with an average of 7.3 years. The rating reflects our continued positive view on the regulated residential rental sector in Germany, which we believe is one of the most stable European real estate asset classes. Although rental growth has declined in the sector, we still expect further rent increases above inflation. The ongoing coronavirus pandemic has not impaired demand or rents for residential affordable housing, and the implication of rent deferrals are currently moderate for TAG. Overall, the development of credit metrics positions the rating well in the Baa3 category.

These positives are partly offset by a larger share of the company's assets in weaker economic regions of Germany, with higher vacancy rates in TAG's portfolio compared with peers; its entry into the unregulated residential market in Poland with development exposure, albeit with limited volume at this stage; its high reliance on secured funding, resulting in a low ratio of unencumbered assets and a high secured debt ratio; and a higher sensitivity of the German residential sector to social and political considerations, which may lead to tightening regulations.

Exhibit 1

We expect TAG's leverage and coverage to remain broadly stable

Moody's-adjusted leverage and coverage metrics



Sources: Moody's Financial Metrics™ and Moody's Investors Service estimates

Credit strengths

» Focus on stable and regulated rental housing activities in Germany, generating stable cash flow from a portfolio diversified across several German regions

» Improving debt/gross assets and fixed-charge coverage, and stable net debt/EBITDA

» Long-dated debt funding structure and access to inexpensive German long-term bank debt

» Rental growth in the portfolio, without substantial capital spending

Credit challenges

» A large share of the company's assets in the weaker economic regions of Germany

» Market entry into the unregulated market in Poland with development exposure, albeit with limited volume at this stage

» High reliance on secured funding, resulting in a low ratio of unencumbered assets and a high secured debt ratio

» Still higher vacancy rates compared with those of most peers

» Sensitivity of the residential sector to social and political considerations, which may lead to tightening regulations

Rating outlook

The stable outlook reflects our expectation that TAG's leverage, measured as Moody's-adjusted debt/gross assets, will remain around 45% in the next 12-18 months, the ramp-up of the Polish activities perform as expected, and the company's unencumbered asset ratio will remain broadly stable.

Factors that could lead to an upgrade

» Gross debt/total assets below 45% on a sustained basis, supported by the company's financial policy, and net debt/EBITDA that exhibits a stable to declining trend

» Fixed-charge coverage is maintained above 3.0x

» Reduced reliance on secured funding, resulting in lower secured debt/assets and a higher unencumbered asset base

Factors that could lead to a downgrade

» Gross debt/total assets above 55% — failure to improve the level of unencumbered assets within Germany would require debt/assets to be below 50% for the assigned rating

» Fixed-charge coverage below 2.25x

» Change in our positive fundamental view of the German residential sector, potentially driven by tightening regulations

» Failure to maintain adequate liquidity

Key indicators

Exhibit 2

TAG Immobilien AG

USD Millions	Dec-15	Dec-16	Dec-17	Dec-18	Dec-19	LTM (Mar-20)	Moody's 12-18 month forward view
Real Estate Gross Assets	4,134.5	4,248.9	5,578.3	5,767.6	6,338.7	6,419.9	6,750 - 7,150
Amount of Unencumbered Assets	9.7%	6.3%	15.7%	14.0%	12.3%	13.6%	15% - 20%
Debt / Real Estate Gross Assets	62.2%	56.8%	54.7%	48.1%	45.8%	46.2%	44% - 47%
Net Debt / EBITDA	14.1x	12.3x	11.2x	10.9x	11.3x	11.3x	11x - 12x
Secured Debt / Real Estate Gross Assets	48.2%	45.3%	41.7%	36.8%	33.7%	34.2%	32% - 35%
EBITDA / Fixed Charges	1.7x	2.2x	2.8x	3.7x	4.4x	4.4x	4.3x - 4.7x

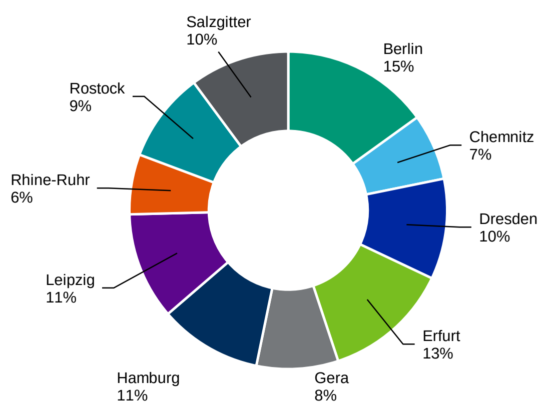
All figures and ratios are calculated using Moody's estimates and standard adjustments. Moody's 12-18-month forward view is Moody's opinion and does not represent the views of the issuer. Periods are financial year-end unless indicated. LTM = Last 12 months.
Sources: Moody's Financial Metrics™ and Moody's Investors Service estimate

Profile

TAG Immobilien AG (TAG) owns and manages a large and diversified multifamily residential rental portfolio of about 84,900 units, mainly located in the east and north of Germany. The company recently entered the Polish market via the acquisition of the developer Vantage Development SA. As of 31 March 2020, TAG's total assets amounted to around €5.9 billion. Headquartered in Hamburg, TAG is listed in the MDAX at the Frankfurt Stock Exchange, with a market capitalisation of €3.3 billion as of 21 July 2020, which is at around 10% premium to its reported net asset value.

Exhibit 3

TAG's portfolio is mostly located in Eastern and Northern Germany
Property fair value split by geography



As of March 2020.
Source: Company

Detailed credit considerations

Supportive operating environment through a focus on stable and regulated market

The German residential sector is one of the most stable asset classes in the European real estate industry, with high demand and limited supply supporting rents and values. While the potential for tighter regulations is a threat to property values and cash flow growth, it will also probably intensify the supply and demand imbalance.

The German rental market is highly regulated — reletting rents and rent increases for existing tenants are capped with reference to a local index (Mietspiegel) calculated by local authorities, reflecting the location and quality of the units. Rent increases are mostly capped to 15% over a period of three years (5% a year; allowance made for modernisation, the cap on which is 8% per year). From a longer-term perspective, prices and rents for residential properties have been more stable in Germany than in any other large developed economy even after taking into account recent increases. Since 1970, German house prices have increased broadly in line with inflation, but have never declined more than 3% in any given year.

Average rents remain affordable despite recent rent and value increases. Nevertheless, affordability fluctuates in tandem with the absolute amount of household income, which exposes lower-income households in particular to higher rental cost-to-income ratios. Affordability has clearly declined in the past five years in Germany as a whole, with rental growth exceeding income growth, resulting in political and regulatory activity aiming to reduce rental growth.

Diversified portfolio with stable growth prospects and improving vacancies, partially located in weaker regions of Germany

TAG has a very diversified portfolio of around 84,900 units, of which 83,153 are residential units, concentrated outside the largest cities. TAG focuses on affordable housing, which is mainly reflected in its relatively moderate rents in a portfolio that generates a higher yield on value than those of some of its residential peers.

Around two-thirds of TAG's residential units are located in 30 cities with more than 20,000 inhabitants, although some are suburbs of larger urban areas. Only about 10% of the portfolio is located in cities with smaller populations. Therefore, overall, the portfolio will benefit to some extent from the urbanisation trend in Germany.

Exhibit 4

TAG's portfolio as of 31 March 2020

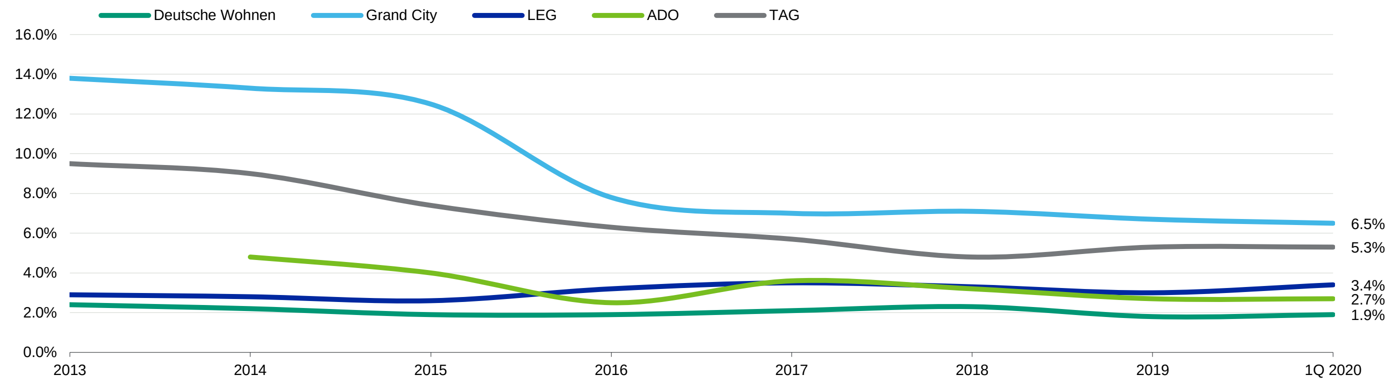
Region	Fair Value in EURm	FV in % total	Units	Renatable area (sqm)	Fair value per sqm (EUR)	Gross yield	Vacancy March 2020	Actual net cold rent (EUR/sqm)	Reletting rent (EUR sqm)	Maintenance (EUR sqm)	Capex (EUR sqm)
Berlin	784	14.7%	10,409.0	596,927	1,313.4	5.1%	4.2%	5.8	6.3	1.2	7.3
Chemnitz	351.6	6.6%	7,523	439,837	799.4	6.8%	7.9%	4.9	4.9	1.8	8.4
Dresden	533.2	10.0%	6,298	409,025	1,303.6	5.2%	2.5%	5.8	6.3	0.8	1.4
Erfurt	670.6	12.6%	10,861	611,134	1,097.3	5.5%	3.3%	5.3	5.6	1.7	3.1
Gera	432.9	8.1%	9,652	561,321	771.2	7.3%	7.3%	5.0	5.3	1.2	3.2
Hamburg	544.3	10.2%	7,049	433,541	1,255.5	5.3%	4.0%	5.8	6.1	2.6	5.6
Leipzig	568.4	10.6%	10,014	589,918	963.5	6.2%	6.2%	5.3	5.8	1.3	1.6
Rhine-Ruhr	318.4	6.0%	4,187	266,405	1,195.2	5.4%	2.3%	5.5	5.6	2.7	1.5
Rostock	477.4	8.9%	7,980	452,371	1,055.3	6.0%	4.4%	5.5	6.0	2.9	5.1
Salzgitter	527.5	9.9%	9,180	563,122	936.7	6.5%	5.3%	5.4	5.6	1.6	4.2
Total residential	**5,208.3**		**83,153**	**4,923,601**	**1,057.8**	**5.8%**	**4.9%**	**5.4**	**5.7**	**1.7**	**4.2**
Acquisitions	16.7	0.3%	429	23,573	708.4	7.4%	7.4%	4.7			
Others	117.4	2.2%	161	20,421	5,749.0	5.9%	6.2%	15.0			
Commercial units			1,147	148,440			16.4%	8.1			
Total	**5,342.4**		**84,890**	**5,116,035**	**1,044.2**	**6.1%**	**5.3%**	**5.5**			

Source: Company

About 70% of TAG's properties are located across six federal states in Eastern Germany (Berlin, Brandenburg, Mecklenburg-Vorpommern, Sachsen, Sachsen-Anhalt and Thüringen), which are economically weaker regions in terms of purchasing power.

Nevertheless, there are a number of positive macroeconomic trends in TAG's target markets. The GDP growth in many larger and medium-sized Eastern German cities has been in line with or even above the national average, and unemployment rates have improved in recent years, increasing rent affordability. Combined with a relatively good rent affordability on a portfolio level, TAG's ability to pick the right assets and locations will be a key driver of further rental growth and vacancy rate reduction. TAG's vacancy rate has started to stabilise as further vacancy reductions are more difficult to achieve or require more capital spending, and TAG's acquisitions typically come with higher vacancy rates, which increase the average rate slightly.

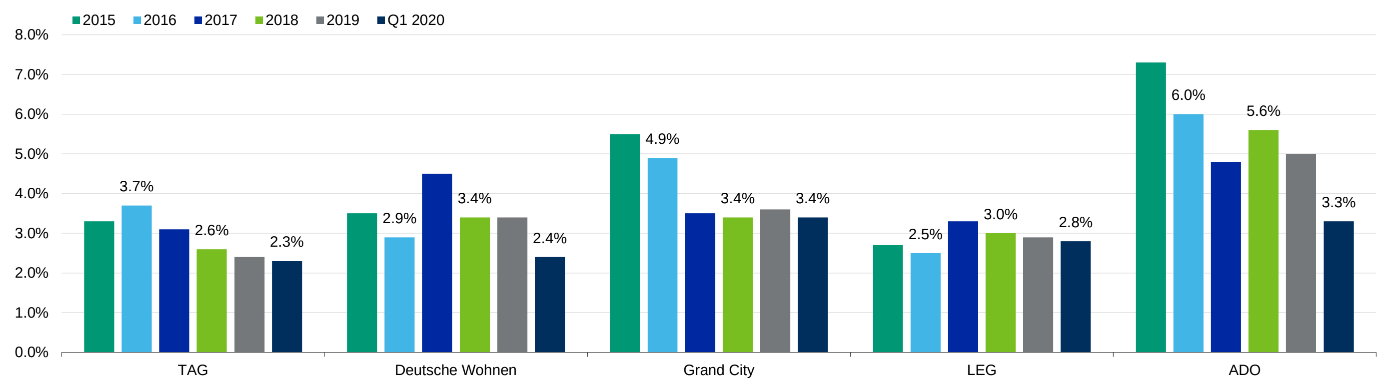
Exhibit 5
Development vacancy rates
TAG compared with its peers



Source: Company reports

TAG's rental growth has been steady in recent years without substantial capital spending. Its rents are lower than those of its peers, but remain affordable compared with average household incomes. We expect sustained rental income growth of 2%-2.5% during the next two years, driven by targeted investments, rent increases for standing tenants and moderate occupancy gains. We expect this income growth, combined with further moderate improvements in its operating margin, to drive EBITDA growth over the next 12-18 months.

Exhibit 6
Like-for-like rental growth
TAG and its peers



Source: Company reports

Moderate effect from the coronavirus pandemic

The overall effect of the coronavirus pandemic will be moderate for TAG. We expect some rent deferrals, ultimately driving the risk of increased bad debt, but in negligible amounts. In line with peers, the effect of the coronavirus pandemic will rather be a moderation in growth. Nevertheless, a medium-term increase in unemployment will translate into lower growth potential even for affordable housing providers, such as TAG.

Market entry into Poland adds development risk in an unregulated residential market

In November 2019, TAG announced the acquisition of Vantage Development S.A., a listed Polish residential real estate developer. The rational behind the acquisition was to enter the Polish residential rental market via an established platform that can create a portfolio of a sufficient size with local expertise.

The Polish residential market is structurally different compared with that in Germany because most people live in their own premises rather than as tenants. We positively view the fact that Poland's (A2 stable) economic development has been relatively good in the last few years, leading to increasing disposable incomes. As of June 2020, we also expect Poland's GDP to suffer less from the coronavirus pandemic than Germany's GDP, with a real GDP decline of 3.8% in 2020 and a subsequent increase of 4% in 2021. TAG will also serve a different client base and segment in Poland compared with its German operations, with younger renters at higher rents for newly constructed flats in larger cities outside Warsaw.

The Polish rental market is relatively unregulated, which we expect to result in higher volatility in rents than that in Germany. Unregulated markets tend to attract a higher amount of supply in good years and mark up existing rents to market rents quicker, which also increase the downside potential during periods of economic decline. In this context, TAG's decision to focus on growth regions is much more relevant as we expect the population trends in those cities to be better.

The residential market does not yet have a track record of institutional investments through economic cycles. While some funds (mostly private) have started to accumulate larger portfolios, we expect lower price stability because of lower liquidity and the historical evidence of portfolio performance through economic cycles.

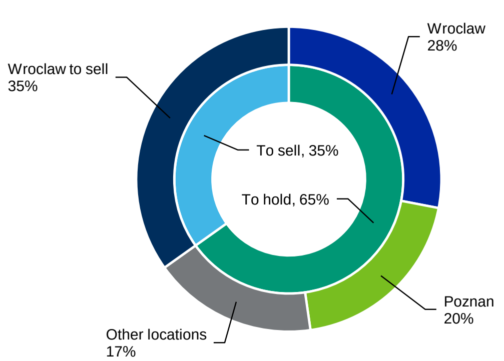
TAG's exposure to Poland and development risk will be limited in 2020 and 2021 and will not substantially affect our credit metrics estimations. Considering the development pipeline over the next five years that the company has indicated, TAG's exposure towards the Polish market will likely remain below 10% of its asset base. TAG's acquired and planned development pipeline consists of around 13,200 units, of which currently 8,600 units are earmarked as build-to-hold projects, while 4,600 units are classified as build-to-sell units. These developments will positively reflect on the companies' average portfolio quality over time.

The company's overall investment costs in the next three to five years are expected to be between €875 million and €975 million, which we expect it to fund with debt and equity.

Exhibit 7

Most of the portfolio comprises developments to hold in metropolitan areas

Based on the number of units

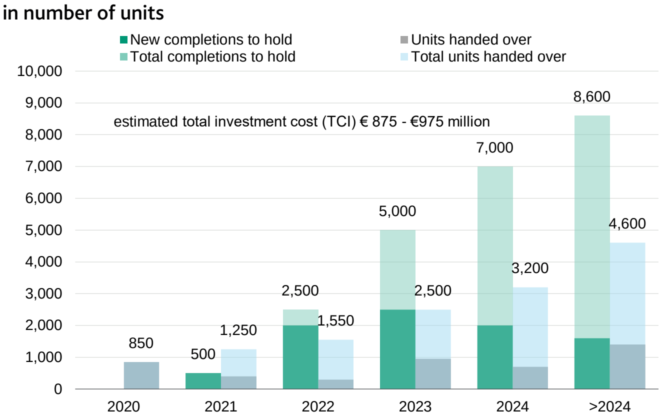


Source: Company

Exhibit 8

The Polish development pipeline is likely to add 8,600 units to TAG's portfolio over the next five years

in number of units



Source: Company

Residential sector sensitive to social and political considerations, which may lead to tightening regulations

There is continued social pressure for German policymakers to address housing supply and affordability, which increases the risk of tightened regulations, with negative credit implications for residential real estate companies. The recent Berlin rental cap is an extreme example that we do not expect to be replicated on a national basis. Historically, regulations have helped to keep rental growth as well as supply low, and hence provided stability to the residential market as an asset class. The overboarding regulation impairs landlords' ability to at least moderately grow income and makes the asset class a less-attractive investment, with a respective effect on property values.

Key financial ratios improved over the last years and will likely remain stable on a better level

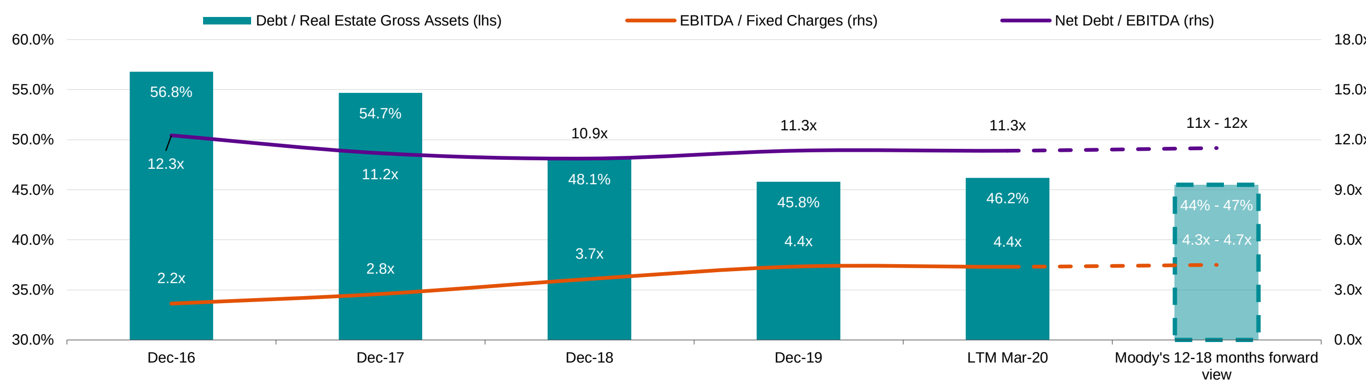
We expect an overall stable debt-to-asset ratio around or below 45%, driven by a prudent capital spending approach, some revaluation gains, largely debt-funded net acquisitions and a moderate cash need to ramp up its Polish built-to-hold portfolio. Debt/assets declined constantly in the last years since we assigned the rating, and the company has amended its financial policy down to 45%, effectively neutralising the yield compression that drove up property values. TAG's debt/assets positions it strongly compared with similarly rated peers.

The company's fixed-charge cover has steadily improved since 2014, at 4.4x as of the 12 months ended March 2020. Without shocks to fixed-term residential loan pricing, TAG will likely achieve some further reduction in its weighted-average interest cost, which was 1.7% as of March 2020. Given our expectation of overall higher absolute debt and some refinancing at lower cost, we expect the fixed-charge cover to be stable in the next 12-18 months.

We expect net debt/EBITDA to be stable or slightly increase, potentially as a result of the funding of acquisitions, capital spending in Germany and the moderate funding of its Polish build-to-hold operations (currently non-yielding).

Exhibit 9

Leverage and coverage are likely to remain broadly stable



Sources: Moody's Financial Metrics™ and Moody's Investors Service estimate

The company pays a relatively high dividend of 75% of funds from operations (FFO) compared with that of its peers. However, the company can cover parts of its capital spending programme with free cash flow because of its higher portfolio yield.

High reliance on secured funding, resulting in a low ratio of unencumbered assets and a high secured debt ratio

TAG's unencumbered asset ratio of 13.6% is the lowest in the European real estate peer group, stemming from its bank debt-funded model. The bank debt provides a very long average debt maturity and low cost of funding, but reduces flexibility and subordinates unsecured creditors, and also increases the secured debt ratio. We see some potential for an increased unencumbered asset ratio, depending on the funding structure of the Polish developments.

TAG's access to equity capital is supported by its granular shareholder base with cornerstone investors. As of 31 March 2020, the company's largest shareholders were MFS Investment Management with a 9.9% share, Capital Group with a 9.6% share and Blackrock with 6.2%. TAG has a dividend payout ratio target of 75% of FFO before capital spending and capital gains.

Liquidity analysis

Long-dated debt maturities result in good liquidity

TAG's good liquidity is based on the following:

» the company's €196.8 million cash and cash equivalents as of 31 March 2020

» the stable cash flow generation from the portfolio

» committed undrawn revolving facilities of €120 million

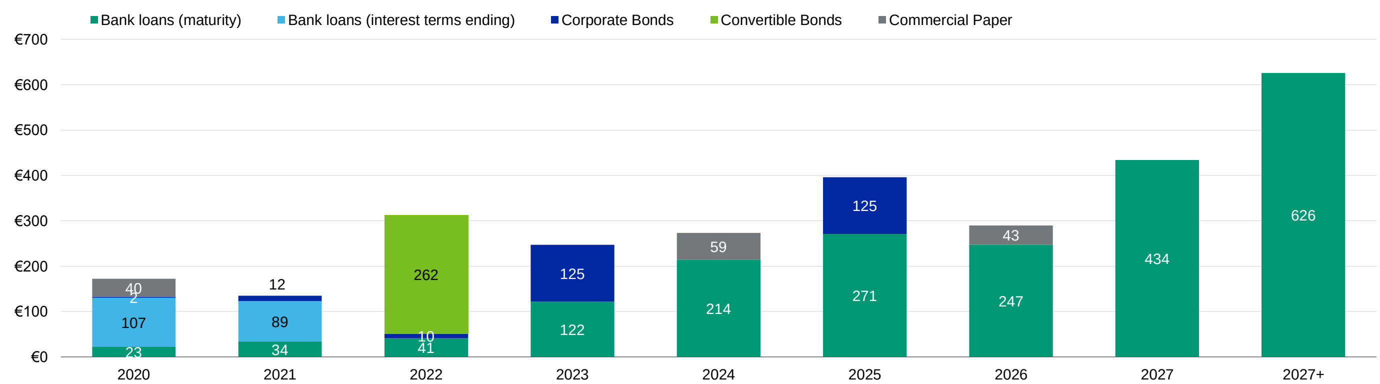
» very long-dated, well-staggered maturity profile, with a 7.3-year weighted average term, which is largely on fixed or hedged rates

TAG has also set up a €500 million commercial paper programme, to which we have assigned a P-3 rating. The notes issued under this programme will rank pari passu with all other unsecured and unsubordinated obligations of the company. There were no drawings under the programme as of 31 March 2020.

Exhibit 10

Debt maturities as of 31 March 2020

In € millions



Source: Company

TAG's cash generation is stronger than that of its peers, driven by its portfolio's yield and its moderate use of modernisation capital spending to drive rental income. As a result, we expect TAG to cover most of its maintenance and capital spending with rental cash flow, even though more capital spending resulted in slightly less FFO-based capital spending compared to we expect increasing capital spending to require relatively more debt funding.

The company's weighted-average interest rate is 1.7%. This is broadly in line with the range of 1.3%-1.8% for other residential peers we rate.

ESG considerations

We take into account the impact of environmental, social and governance (ESG) factors when assessing companies' credit quality. In the case of TAG, the following are the main ESG-related drivers:

» Environmental: Environmental performance of the properties have an effect on the marketability of properties and the asset quality. The company has committed to further invest in its portfolio to increase energy efficiency, and an increasing share of its portfolio is supplied with energy and heating by a subsidiary of TAG, ultimately based on lower carbon-intense sources.

» Social: The social dimension of the housing situation in Germany has gained importance on the political agenda, although the recent coronavirus pandemic may have shifted the attention towards other matters. The company introduced various measures, such as no terminations or evictions, rent deferral arrangements and an increase in engagement with nonprofit organisations.

» Governance: TAG recently amended its financial policy to a reduced reported LTV target of around 45%. The company is currently in line with its own financial policy and has a history of adhering to its leverage targets. We do not consider other governance topics to weigh on the rating.

Structural considerations

Most group assets and debt are held by subsidiaries of the holding company, TAG, which is a pure holding company, and the issuer of two unsecured bonds of €125 million each and a convertible bond of €262 million. In most cases, each mortgage loan is only guaranteed by the property held by the relevant subsidiary.

Methodology and scorecard

The principal methodology used in this rating was our REITs and Other Commercial Property Firms rating methodology, published in September 2018. TAG's assigned rating of Baa3 is above the scorecard-indicated outcome under both our current view and forward view. This reflects our stable view of the German residential sector from a demand and supply perspective. It also reflects the German banking markets' provision of very long-term debt funding to residential companies, which lowers the scorecard-indicated outcome because of weak unencumbered assets and secured debt ratios.

Exhibit 11

Rating factors

TAG Immobilien AG

Real Estate / REIT Industry Grid [1][2]	Current LTM 3/31/2020		Moody's 12-18 Month Forward View As of 6/29/2020 [3]	
Factor 1 : Scale (5%)	**Measure**	**Score**	**Measure**	**Score**
a) Gross Assets (USD Billion)	$6.4	Baa	$6.7 - $7.2	Baa
Factor 2 : Business Profile (25%)				
a) Market Positioning and Asset Quality	Ba	Ba	Ba	Ba
b) Operating Environment	Aa	Aa	Aa	Aa
Factor 3 : Liquidity and Access To Capital (25%)				
a) Liquidity and Access to Capital	Ba	Ba	Ba	Ba
b) Unencumbered Assets / Gross Assets	13.6%	Caa	15% - 20%	Caa
Factor 4 : Leverage and Coverage (45%)				
a) Total Debt + Preferred Stock / Gross Assets	46.2%	Baa	44% - 47%	Baa
b) Net Debt / EBITDA	11.3x	Caa	11x - 12x	Caa
c) Secured Debt / Gross Assets	34.2%	B	32% - 35%	B
d) Fixed Charge Coverage	4.4x	Baa	4.3x - 4.7x	Baa/A
Rating:				
a) Indicated Outcome from Scorecard		Ba2		Ba1
b) Actual Rating Assigned				Baa3

[1] All ratios are based on adjusted financial data and incorporate Moody's Global Standard Adjustments for Non-Financial Corporations.
[2] As of 31 March 2020 (L).
[3] This represents a Moody's forward view, not the view of the issuer, and unless noted in the text, does not incorporate significant acquisitions and divestitures.
Source: Moody's Financial Metrics™

APPENDIX

Exhibit 12

Peer comparison

TAG Immobilien AG

	TAG Immobilien AG Baa3 Stable			Deutsche Wohnen SE A3 Negative			Grand City Properties S.A. Baa1 Stable			LEG Immobilien AG Baa1 Stable			ADO Properties S.A. Ba1 Negative		
(in USD millions)	FYE Dec-18	FYE Dec-19	LTM Mar-20	FYE Dec-18	FYE Dec-19	LTM Mar-20	FYE Dec-18	FYE Dec-19	LTM Mar-20	FYE Dec-18	FYE Dec-19	LTM Mar-20	FYE Dec-18	FYE Dec-19	LTM Mar-20
Gross Assets	$5,768	$6,339	$6,420	$28,676	$31,263	$30,431	$10,129	$11,058	$10,908	$12,854	$14,502	$14,221	$4,772	$4,935	$4,923
Unencumbered Assets / Gross Assets	14.0%	12.3%	13.6%	25.0%	29.8%	28.6%	70.7%	82.7%	81.4%	19.2%	25.3%	25.5%	29.3%	41.0%	40.2%
Total Debt + Preferred Stock / Gross Assets	48.1%	45.8%	46.2%	36.8%	37.3%	37.6%	43.4%	44.0%	44.7%	42.7%	40.4%	39.9%	39.8%	31.5%	33.7%
Net Debt / EBITDA	10.9x	11.3x	11.3x	13.5x	13.9x	15.0x	11.8x	11.6x	12.2x	11.6x	12.1x	12.1x	17.4x	11.6x	13.8x
Secured Debt / Gross Assets	36.8%	33.7%	34.2%	24.7%	22.7%	22.7%	9.7%	5.4%	6.4%	27.1%	22.0%	22.0%	24.2%	16.6%	20.1%
Fixed Charge Coverage	3.7x	4.4x	4.4x	6.0x	5.1x	4.9x	4.5x	4.8x	4.9x	4.3x	4.3x	4.4x	3.6x	2.9x	2.8x

Source: Moody's Financial Metrics™

Exhibit 13

Moody's-adjusted debt breakdown

TAG Immobilien AG

(in EUR millions)	FYE Dec-15	FYE Dec-16	FYE Dec-17	FYE Dec-18	FYE Dec-19	LTM Ending Mar-20
As Reported Debt	**2,349.6**	**2,270.2**	**2,513.8**	**2,398.8**	**2,577.1**	**2,679.5**
Pensions	6.0	6.1	5.9	5.5	5.8	5.8
Operating Leases	11.8	11.6	11.0	12.1	0.0	0.0
Non-Standard Adjustments	0.0	0.0	9.2	9.0	3.1	17.4
Moody's-Adjusted Debt	**2,367.4**	**2,287.9**	**2,539.9**	**2,425.4**	**2,586.0**	**2,702.7**

All figures are calculated using Moody's Investors Service estimates and standard adjustments.
Source: Moody's Financial Metrics™

Ratings

Exhibit 14

Category	Moody's Rating
TAG IMMOBILIEN AG	
Outlook	Stable
Issuer Rating -Dom Curr	Baa3
Commercial Paper -Dom Curr	P-3
ST Issuer Rating -Dom Curr	P-3

Source: Moody's Investors Service

REPORT NUMBER 1236473

CLIENT SERVICES

Americas	1-212-553-1653
Asia Pacific	852-3551-3077
Japan	81-3-5408-4100
EMEA	44-20-7772-5454