S&P Global Ratings

# Research

## Research Update:

# Spain-Based Inmobiliaria Colonial Upgraded To 'BBB+' On Incrementing Controlling Stake In SFL; Outlook Stable


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## Overview

- Colonial has announced that it will acquire a 22.2% stake in Societe Fonciere Lyonnaise (SFL) from Qatar Investment Authority (QIA), increasing its controlling stake from 59.0% to 81.0%.
- The majority of the €718 million transaction will be carried out through a capital increase in Colonial and an equity swap in favor of QIA, and Colonial will cover the remaining one-quarter of the investment through a cash payment of €203 million.
- The transaction will have a minimal impact on Colonial's credit ratios, and the company will benefit from a leaner corporate structure and a meaningful controlling stake in SFL, its core subsidiary.
- We are therefore raising our ratings on Colonial and its senior unsecured debt to 'BBB+' from 'BBB'.
- The stable outlook reflects our view that Colonial's prime, well-located assets should continue to generate stable recurring income and enable the maintenance of an EBITDA interest coverage of around 3x and a debt-to-debt-plus-equity ratio of less than 45% in the next two years.

## Rating Action

On Oct. 18, 2018, S&P Global Ratings raised its long-term issuer credit rating on Spain-based property investment company Inmobiliaria Colonial SOCIMI, S.A. (Colonial) to 'BBB+' from 'BBB'. The outlook is stable.

We also raised our issue rating on Colonial's senior unsecured debt to 'BBB+' from 'BBB'.

At the same time, we affirmed our 'A-2' short-term issuer credit rating on Colonial.

## Rationale

Colonial has announced that it will increase its stake in its French subsidiary SFL from 59% to 81% by acquiring a 22.2% stake from QIA for a total value of €718 million. The transaction will be carried out mainly through a capital increase in Colonial that will be entirely underwritten by QIA, and a cash payment of €203 million. The deal was approved by Colonial's board of directors, which, in the following days, will call a shareholders' meeting to formally approve the transaction and the capital increase. Even though the transaction has yet to close, we see minimal execution risk on the finalizing steps.

The structuring of the transaction is supportive of Colonial's credit quality, with approximately one-quarter of the investment volume coming from a cash payment made by Colonial. We therefore expect a minimal impact on Colonial's credit ratios (S&P Global Ratings-adjusted debt-to-debt-plus-equity ratio of 44.3% as of June 30, 2018), since the weight of the SFL transaction will be somewhat offset by about €350 million the company recently received from asset disposals. Furthermore, we understand that the transaction will markedly simplify the group's shareholding structure. We also note the reasonable terms for Colonial: the acquisition price implies an average discount of 19% to the last reported net asset value per share of SFL, but an average 18% premium over SFL's recent share price.

Colonial will benefit from a substantial controlling stake in SFL, its core subsidiary, which represents about 60% of the total gross asset value on a consolidated basis. Until now, we had factored into our analysis of Colonial a certain degree of insulation for SFL. In our view, the transaction indicates that SFL's previous insulated status no longer applies. Even if there is no change regarding SFL's listing and independent funding strategy, no single minority shareholder will hold more than 15% of SFL's equity, and Colonial's payment of a substantial premium to share price highlights the eminently strategic nature SFL has for the group.

We therefore rate Colonial at 'BBB+', now in line with our long-term issuer credit rating on SFL. We acknowledge that Colonial has higher leverage than SFL, but we weigh in the benefits of Colonial's Spanish portfolio, composed of high-quality assets, mainly located in the central business district of well-performing markets such as Madrid and Barcelona.

Overall, we do not anticipate any significant deviation from the forecast credit metrics, and the company will maintain strong liquidity, in our view. For more details, see "Spain-Based Inmobiliaria Colonial 'BBB' Ratings Affirmed On Robust Credit Metrics After Axiare Takeover; Outlook Stable," published April 27, 2018, on RatingsDirect.

## Outlook

The stable outlook reflects our view that strong market fundamentals, the successful integration of Axiare, and Colonial's high-quality assets should enable the company to maintain adjusted EBITDA interest coverage around 3x and debt-to-debt-plus-equity below 45% over the next two years. Our outlook is supported by the company's prudent financial policy and our belief that Colonial's prime, well-located assets will benefit from low vacancy rates in the central business district of Paris, Madrid, and Barcelona.

### Upside scenario

Considering increased ownership of SFL and the company's existing portfolio, ratings upside would hinge on Colonial's willingness and ability to consistently maintain an adjusted debt-to-debt-plus equity ratio of less than 35% and an adjusted EBITDA interest coverage above 3.8x. An upgrade would also be contingent on Colonial ensuring a disciplined financial policy consistent with these stronger credit measures, and a stronger and more diversified cash flow base.

### Downside scenario

We could consider a downgrade if, in particular, Colonial's EBITDA interest coverage dropped below 2.4x and its debt to debt plus equity increased meaningfully above 45%. This could stem from more debt-financed acquisitions than we currently anticipate, or a substantial drop in Colonial's portfolio value. Historically volatile business confidence in Spain remains an operating risk that could depress the company's interest coverage, among other debt metrics, in our opinion.

## Ratings Score Snapshot

Issuer Credit Rating: BBB+/Stable/A-2

Business risk: Strong
- Country risk: Low
- Industry risk: Low
- Competitive position: Strong

Financial risk: Intermediate
- Cash flow/Leverage: Intermediate

Anchor: bbb+

Modifiers
- Diversification/Portfolio effect: Neutral (no impact)
- Capital structure: Neutral (no impact)
- Liquidity: Strong (no impact)
- Financial policy: Neutral (no impact)
- Management and governance: Satisfactory (no impact)
- Comparable ratings analysis: Neutral (no impact)

## Related Criteria

- 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
- General Criteria: Group Rating Methodology, Nov. 19, 2013
- Criteria - Corporates - General: Corporate Methodology: Ratios And Adjustments, Nov. 19, 2013
- Criteria - Corporates - General: Corporate Methodology, Nov. 19, 2013
- General Criteria: Country Risk Assessment Methodology And Assumptions, Nov. 19, 2013
- General Criteria: Methodology: Industry Risk, Nov. 19, 2013
- General Criteria: Methodology: Management And Governance Credit Factors For Corporate Entities And Insurers, Nov. 13, 2012
- General Criteria: Use Of CreditWatch And Outlooks, Sept. 14, 2009

## Related Research

- Spain-Based Inmobiliaria Colonial 'BBB' Ratings Affirmed On Robust Credit Metrics After Axiare Takeover; Outlook Stable, April 27, 2018

## Ratings List

Upgraded; Ratings Affirmed

| | To | From |
|---|---|---|
| Inmobiliaria Colonial, Socimi, S.A. | | |
| Issuer Credit Rating | BBB+/Stable/A-2 | BBB/Stable/A-2 |
| Senior Unsecured | BBB+ | BBB |

**Additional Contact:**
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Certain terms used in this report, particularly certain adjectives used to express our view on rating relevant factors, have specific meanings ascribed to them in our criteria, and should therefore be read in conjunction with such criteria. Please see Ratings Criteria at www.standardandpoors.com for further information. Complete ratings information is available to subscribers of

RatingsDirect at www.capitaliq.com. All ratings affected by this rating action can be found on S&P Global Ratings' public website at www.standardandpoors.com. Use the Ratings search box located in the left column. Alternatively, call one of the following S&P Global Ratings numbers: Client Support Europe (44) 20-7176-7176; London Press Office (44) 20-7176-3605; Paris (33) 1-4420-6708; Frankfurt (49) 69-33-999-225; Stockholm (46) 8-440-5914; or Moscow 7 (495) 783-4009.