



RATING ACTION COMMENTARY

Fitch Affirms Nordic's SBB at 'BBB-' on Bid for Entra; Outlook Positive

Wed 25 Nov, 2020 - 5:10 AM ET

Fitch Ratings - Stockholm - 25 Nov 2020: Fitch Ratings has affirmed Swedish property company Samhallsbyggnadsbolaget i Norden's AB (SBB) Long-Term Issuer Default (IDR) with a Positive Outlook. A full list of ratings is provided below.

The rating actions follow the announcement that SBB has bid for 100% of the outstanding shares in the Norwegian property company Entra ASA. Entra's NOK51.8 billion (SEK49.5 billion at end-3Q20) portfolio is focused on community service and office properties across Norway in Oslo, Bergen and Stavanger. SBB is offering to pay NOK30 billion (SEK28.8 billion) for the equity in Entra. The bid is funded by NOK9 billion (SEK8.5 billion) of new SBB equity to Entra's shareholders, planned issue of hybrid bonds, and SBB's cash resources. Entra had net debt of NOK20.4 billion (SEK19.6 billion) at end-September 2020.

The Positive Outlook reflects expected step-change improvements in SBB's business profile resulting from a successful bid. This, combined with deleveraging as SBB continues its disposal of non-core assets, would warrant a higher rating. The resultant business profile would have greater diversification across government-linked tenants mainly in two countries rated 'AAA', together with improved profitability and scale. Fitch views the greater stability of the combined group's community service and regulated residential rental income (90%/10%) would allow higher leverage than for commercial office asset peers.

KEY RATING DRIVERS

Large Community Service Portfolio: The acquisition of Entra's portfolio, which complements SBB's existing community service portfolio, will materially increase SBB's scale and diversification. The combined portfolio will be broadly equally split between Norway and Sweden with some properties in Finland and Denmark after the completion of its disposal programme. SBB's portfolio will total SEK131billion (EUR12.8 billion) pro-forma for the acquisition at end-3Q20.

Niche Community Service Assets: The combined portfolio of SBB and Entra will be 90% community service and prime office properties and around 10% on regional residential. The community service properties have an indirect and direct government tenant base including government departments, municipalities, education, judicial, elderly care, and LSS (disabled) group housing. The passing rent for the combined group would be SEK7 billion pro-forma at end-3Q20. Fitch views the stability of SBB's government-linked rental income, backed by long lease lengths, as allowing higher leverage than for commercial retail, office and industrial asset classes.

Deal Funding: The offer for Entra's shares, which represents a 26% premium to the volume-weighted share price during the last three months, will be funded by a 30% equity and 70% cash mix. SBB plans to fund the cash portion by tapping the capital markets and issuing SEK6.5 billion hybrid and senior unsecured bonds. The bid includes a back-up SEK20 billion unsecured bridge facility with Goldman Sachs.

Leverage to Temporarily Increase: Fitch forecasts SBB's net debt to EBITDA to increase to around 12x at end-2021 pro forma for the disposal of non-core assets before improving towards 11.5x in 2022 and 10.4x in 2023, driven by rental growth, monetisation of building rights and planned asset recycling. Based on these forecasts the 2023 leverage will be commensurate with an upgrade to 'BBB'. Deleveraging is also aided by the scheduled conversion to equity of SBB's mandatory convertible in July 2023. Interest cover is more than sufficient and forecast to improve to 3.5x-4.0x including the cash coupons on its existing and planned hybrids.

Limited COVID19 Impact: Fitch expects the economic effects of the coronavirus pandemic to have a limited impact on rental income from SBB's portfolio of community service and residential properties. This provides stability to SBB's cash flows compared with peers who are exposed to retail store closures or tenants with weaker tenant quality. SBB's collection

rates in 2Q20 and 3Q20, which have been above 99% of contractual rents, reflect this quality.

Unsecured Capital Structure: Fitch understands from management that SBB will maintain its primarily unsecured capital structure by issuing senior unsecured bonds and hybrids to fund the acquisition. This leaves a large pool of unencumbered assets. Fitch expects the enlarged group's unencumbered asset cover to be above 2x relative to its senior unsecured debt.

DERIVATION SUMMARY

With the lower-yielding nature of SBB's residential rental portfolio and longer lease length than peers' (from both community service assets and average tenure of residential assets), and portfolio mix, Fitch has allowed SBB more leverage headroom and lower interest cover than for (i) commercial property-orientated Swedish peers, and (ii) EMEA peers with commercial property companies that underpin our EMEA REIT Navigator mid-point guidelines.

Fitch views SBB's portfolio as more stable due to the strength of Swedish residential properties with regulated below-open market rents and the community service properties' stable tenant base with longer term leases. This is tempered by the regional location of assets within SBB's portfolio. Its portfolio fundamentals are less sensitive to economic cycles than commercial office property companies that are reliant on open market conditions with multiple participants affecting respective market fundamentals.

Assura plc (A-/Stable) builds and owns modern general practitioners' (doctors') facilities in the UK, with state NHS-approved (National Health Service) rent and indirect NHS rent payment covenant. Its end-2019 portfolio was much smaller than SBB's at GBP2.1 billion. Reflecting Assura's community service activities, a 4.7% net initial yield (SBB: 4.5%), longer 11.7 year weighted average lease length, 99% occupancy rate, and specific-use assets, the company's downgrade rating sensitivity to 'BBB+' includes net debt/EBITDA more than 9x, compared with SBB's upgrade metric to 'BBB' below 11x net debt/EBITDA. In part, this acknowledges the wider diversity of SBB's larger portfolio, including residential rental exposure. Net Interest cover (NIC) is more difficult to compare, as the companies have different interest-rate environments. Assura's NIC is similar to the enlarged SBB's at 4x.

KEY ASSUMPTIONS

Fitch's Key Assumptions Within Our Rating Case for the Issuer

- Bid equivalent to SEK28.8 billion for Entra equity funded by SEK8.5 billion new equity issue and planned hybrids.
- Realising operational synergies and further improvements in the EBITDA margin of the combined group.
- Continued disposal of non-core assets during 2020 and 2021.
- Around SEK3 billion of capex p.a. over the next four years with a 10-to-15 year payback period.
- Organic rental growth of 2%-2.5% per year including indexation until 2024.
- SEK3 billion of cash inflow from mainly SBB building right disposals during 2021-2023.

RATING SENSITIVITIES

Factors that could, individually or collectively, lead to positive rating action/upgrade:

- Net debt to EBITDA of less than 11x (2021 pro forma: around 12x)
- Fixed charge cover (FCC) greater than 3.0x
- Unencumbered asset cover above 2.0x
- Continued improvement in corporate governance standards including reduced key man risk in SBB's processes

Factors that could, individually or collectively, lead to negative rating action/downgrade:

- Net debt to EBITDA greater than 12x
- Portfolio acquisitions that decrease FCC below 2.0x
- 12-month liquidity score below 1.0x

BEST/WORST CASE RATING SCENARIO

International scale credit ratings of Non-Financial Corporate issuers have a best-case rating upgrade scenario (defined as the 99th percentile of rating transitions, measured in a positive direction) of three notches over a three-year rating horizon; and a worst-case rating downgrade scenario (defined as the 99th percentile of rating transitions, measured in a negative direction) of four notches over three years. The complete span of best- and worst-case scenario credit ratings for all rating categories ranges from 'AAA' to 'D'. Best- and worst-case scenario credit ratings are based on historical performance. For more information about the methodology used to determine sector-specific best- and worst-case scenario credit ratings, visit <https://www.fitchratings.com/site/re/10111579>.

LIQUIDITY AND DEBT STRUCTURE

Healthy Liquidity: At end-3Q20, SBB had healthy liquidity consisting of SEK6 billion in cash on balance sheet and SEK9.1 billion of undrawn committed credit facilities compared with SEK2.5 billion (including commercial paper) of debt maturing within one year and another SEK4.1 billion within 24 months. To fund the bid for Entra SBB has signed a SEK20 billion bridge facility covering these funding needs.

During 2020, SBB has actively managed its funding by redeeming older bonds with higher coupons and replacing new (mainly senior unsecured) bonds with lower coupons. The average debt maturity was 4.7 years at end-3Q20 and the average interest cost declined to 1.41% (1.76% at end-2019).

REFERENCES FOR SUBSTANTIALLY MATERIAL SOURCE CITED AS KEY DRIVER OF RATING

The principal sources of information used in the analysis are described in the Applicable Criteria.

ESG CONSIDERATIONS

SBB: ESG Relevance Score of '4' for Governance Structure

Fitch has assigned an ESG credit relevance score of 4 for Governance Structure to reflect the key person risk in SBB compared with companies with longer track records and more established governance. Fitch acknowledges SBB's expanding management team, a property transaction team, and an experienced board behind the CEO. These have a negative impact on the credit profile, and are relevant to the ratings in conjunction with other factors.

Unless stated otherwise above the highest level of ESG credit relevance is a score of 3 - ESG issues are credit neutral or have only a minimal credit impact on the entity, either due to their nature or the way in which they are being managed by SBB. For more information on Fitch's ESG Relevance Scores, visit www.fitchratings.com/esg.

RATING ACTIONS

ENTITY/DEBT	RATING		PRIOR	
SBB - Samhallsbyggnadsbolaget i Norden AB	LT IDR	BBB- Rating Outlook Positive	Affirmed	BBB- Rating Outlook Stable
	ST IDR	F3	Affirmed	F3
● subordinated	LT	BB	Affirmed	BB
● senior unsecured	LT	BBB-	Affirmed	BBB-
● senior unsecured	ST	F3	Affirmed	F3

[VIEW ADDITIONAL RATING DETAILS](#)

FITCH RATINGS ANALYSTS

Fredric Liljestrand

Director

Primary Rating Analyst

+46 85510 9441

Fitch Ratings Espana S.A.U. (Spain) Nordic Region Filial
Kungsgatan 8 Stockholm 111 43

John Hatton

Managing Director
Secondary Rating Analyst
+44 20 3530 1061

Bram Cartmell

Senior Director
Committee Chairperson
+44 20 3530 1874

MEDIA CONTACTS**Adrian Simpson**

London
+44 20 3530 1010
adrian.simpson@thefitchgroup.com

Additional information is available on www.fitchratings.com

APPLICABLE CRITERIA

[Corporates Notching and Recovery Ratings Criteria \(pub. 14 Oct 2019\) \(including rating assumption sensitivity\)](#)

[Short-Term Ratings Criteria \(pub. 06 Mar 2020\)](#)

[Corporate Rating Criteria \(pub. 01 May 2020\) \(including rating assumption sensitivity\)](#)

[Sector Navigators - Addendum to the Corporate Rating Criteria \(pub. 26 Jun 2020\)](#)

[Corporate Hybrids Treatment and Notching Criteria \(pub. 12 Nov 2020\)](#)

APPLICABLE MODELS

Numbers in parentheses accompanying applicable model(s) contain hyperlinks to criteria providing description of model(s).

Corporate Monitoring & Forecasting Model (COMFORT Model), v7.9.0 ([1](#))

ADDITIONAL DISCLOSURES

[Dodd-Frank Rating Information Disclosure Form](#)

[Solicitation Status](#)

[Endorsement Policy](#)

ENDORSEMENT STATUS

SBB - Samhallsbyggnadsbolaget i Norden AB

EU Issued

DISCLAIMER

ALL FITCH CREDIT RATINGS ARE SUBJECT TO CERTAIN LIMITATIONS AND DISCLAIMERS. PLEASE READ THESE LIMITATIONS AND DISCLAIMERS BY FOLLOWING THIS LINK: [HTTPS://WWW.FITCHRATINGS.COM/UNDERSTANDINGCREDITRATINGS](https://www.fitchratings.com/understandingcreditratings). IN ADDITION, THE FOLLOWING [HTTPS://WWW.FITCHRATINGS.COM/RATING-DEFINITIONS-DOCUMENT](https://www.fitchratings.com/rating-definitions-document) DETAILS FITCH'S RATING DEFINITIONS FOR EACH RATING SCALE AND RATING CATEGORIES, INCLUDING DEFINITIONS RELATING TO DEFAULT. PUBLISHED RATINGS, CRITERIA, AND METHODOLOGIES ARE AVAILABLE FROM THIS SITE AT ALL TIMES. FITCH'S CODE OF CONDUCT, CONFIDENTIALITY, CONFLICTS OF INTEREST, AFFILIATE FIREWALL, COMPLIANCE, AND OTHER RELEVANT POLICIES AND PROCEDURES ARE ALSO AVAILABLE FROM THE CODE OF CONDUCT SECTION OF THIS SITE. DIRECTORS AND SHAREHOLDERS RELEVANT INTERESTS ARE AVAILABLE AT [HTTPS://WWW.FITCHRATINGS.COM/SITE/REGULATORY](https://www.fitchratings.com/site/regulatory). FITCH MAY HAVE PROVIDED ANOTHER PERMISSIBLE SERVICE TO THE RATED ENTITY OR ITS RELATED THIRD PARTIES. DETAILS OF THIS SERVICE FOR RATINGS FOR WHICH THE LEAD ANALYST IS BASED IN AN EU-REGISTERED ENTITY CAN BE FOUND ON THE ENTITY SUMMARY PAGE FOR THIS ISSUER ON THE FITCH RATINGS WEBSITE.

[READ LESS](#)

COPYRIGHT

Copyright © 2020 by Fitch Ratings, Inc., Fitch Ratings Ltd. and its subsidiaries. 33 Whitehall Street, NY, NY 10004. Telephone: 1-800-753-4824, (212) 908-0500. Fax: (212) 480-4435. Reproduction or retransmission in whole or in part is prohibited except by permission. All rights reserved. In issuing and maintaining its ratings and in making other reports (including forecast information), Fitch relies on factual information it receives from issuers and underwriters and from other sources Fitch believes to be credible. Fitch conducts a reasonable investigation of the factual information relied upon by it in accordance with its ratings methodology, and obtains reasonable verification of that information from independent sources, to the extent such sources are available for a given security or in a

given jurisdiction. The manner of Fitch's factual investigation and the scope of the third-party verification it obtains will vary depending on the nature of the rated security and its issuer, the requirements and practices in the jurisdiction in which the rated security is offered and sold and/or the issuer is located, the availability and nature of relevant public information, access to the management of the issuer and its advisers, the availability of pre-existing third-party verifications such as audit reports, agreed-upon procedures letters, appraisals, actuarial reports, engineering reports, legal opinions and other reports provided by third parties, the availability of independent and competent third-party verification sources with respect to the particular security or in the particular jurisdiction of the issuer, and a variety of other factors. Users of Fitch's ratings and reports should understand that neither an enhanced factual investigation nor any third-party verification can ensure that all of the information Fitch relies on in connection with a rating or a report will be accurate and complete. Ultimately, the issuer and its advisers are responsible for the accuracy of the information they provide to Fitch and to the market in offering documents and other reports. In issuing its ratings and its reports, Fitch must rely on the work of experts, including independent auditors with respect to financial statements and attorneys with respect to legal and tax matters. Further, ratings and forecasts of financial and other information are inherently forward-looking and embody assumptions and predictions about future events that by their nature cannot be verified as facts. As a result, despite any verification of current facts, ratings and forecasts can be affected by future events or conditions that were not anticipated at the time a rating or forecast was issued or affirmed. The information in this report is provided "as is" without any representation or warranty of any kind, and Fitch does not represent or warrant that the report or any of its contents will meet any of the requirements of a recipient of the report. A Fitch rating is an opinion as to the creditworthiness of a security. This opinion and reports made by Fitch are based on established criteria and methodologies that Fitch is continuously evaluating and updating. Therefore, ratings and reports are the collective work product of Fitch and no individual, or group of individuals, is solely responsible for a rating or a report. The rating does not address the risk of loss due to risks other than credit risk, unless such risk is specifically mentioned. Fitch is not engaged in the offer or sale of any security. All Fitch reports have shared authorship. Individuals identified in a Fitch report were involved in, but are not solely responsible for, the opinions stated therein. The individuals are named for contact purposes only. A report providing a Fitch rating is neither a prospectus nor a substitute for the information assembled, verified and presented to investors by the issuer and its agents in connection with the sale of the securities. Ratings may be changed or withdrawn at any time for any reason in the sole discretion of Fitch. Fitch does not provide investment advice of any sort. Ratings are not a recommendation to buy, sell, or hold any security. Ratings do not comment on the adequacy of market price, the suitability of any security for a particular investor, or the tax-exempt nature or taxability of payments made in respect to any

security. Fitch receives fees from issuers, insurers, guarantors, other obligors, and underwriters for rating securities. Such fees generally vary from US\$1,000 to US\$750,000 (or the applicable currency equivalent) per issue. In certain cases, Fitch will rate all or a number of issues issued by a particular issuer, or insured or guaranteed by a particular insurer or guarantor, for a single annual fee. Such fees are expected to vary from US\$10,000 to US\$1,500,000 (or the applicable currency equivalent). The assignment, publication, or dissemination of a rating by Fitch shall not constitute a consent by Fitch to use its name as an expert in connection with any registration statement filed under the United States securities laws, the Financial Services and Markets Act of 2000 of the United Kingdom, or the securities laws of any particular jurisdiction. Due to the relative efficiency of electronic publishing and distribution, Fitch research may be available to electronic subscribers up to three days earlier than to print subscribers.

For Australia, New Zealand, Taiwan and South Korea only: Fitch Australia Pty Ltd holds an Australian financial services license (AFS license no. 337123) which authorizes it to provide credit ratings to wholesale clients only. Credit ratings information published by Fitch is not intended to be used by persons who are retail clients within the meaning of the Corporations Act 2001

Fitch Ratings, Inc. is registered with the U.S. Securities and Exchange Commission as a Nationally Recognized Statistical Rating Organization (the "NRSRO"). While certain of the NRSRO's credit rating subsidiaries are listed on Item 3 of Form NRSRO and as such are authorized to issue credit ratings on behalf of the NRSRO (see <https://www.fitchratings.com/site/regulatory>), other credit rating subsidiaries are not listed on Form NRSRO (the "non-NRSROs") and therefore credit ratings issued by those subsidiaries are not issued on behalf of the NRSRO. However, non-NRSRO personnel may participate in determining credit ratings issued by or on behalf of the NRSRO.

[READ LESS](#)

SOLICITATION STATUS

The ratings above were solicited and assigned or maintained at the request of the rated entity/issuer or a related third party. Any exceptions follow below.

ENDORSEMENT POLICY

Fitch's approach to ratings endorsement so that ratings produced outside the EU may be used by regulated entities within the EU for regulatory purposes, pursuant to the terms of the EU Regulation with respect to credit rating agencies, can be found on the [EU Regulatory Disclosures](#) page. The endorsement status of all International ratings is provided within the entity summary page for each rated entity and in the transaction detail

pages for all structured finance transactions on the Fitch website. These disclosures are updated on a daily basis.

Real Estate and Homebuilding Corporate Finance Europe Sweden
