5 September 2023

Corporates

Summus Capital OÜ
Estonia, Real Estate

BB STABLE

Key metrics

			Scope estimates	
Scope credit ratios	**2021**	**2022**	**2023E**	**2024E**
Scope-adjusted EBITDA/interest cover	2.8x	2.6x	2.0x	2.4x
Scope-adjusted debt/EBITDA	9.7x	8.8x	9.1x	8.4x
Scope-adjusted loan/value ratio	51%	51%	50%	51%

Rating rationale

The rating affirmation reflects the issuer's high-quality portfolio of assets in Baltic capital cities, which are second-tier investment markets with stable tenant demand. Summus buy-and-hold investment approach provides stable rental cash flows. The assets' quality is evidenced by the high and stable occupancy rate, at 97% as of June 2023. Although over 50% of rental income is derived from retail tenants, properties proved resilient during the Covid-19 pandemic, with no significant impact on rent collections. The rating remains constrained by the company's limited size and market shares, as Summus remains small in the European context and exposed to the retail segment.

Summus' financial risk profile is driven by its moderate credit metrics. The Scope-adjusted loan/value ratio stabilised in the range of 50%-55%. Debt protection, as measured by Scope-adjusted EBITDA interest cover, stood at 2.6x in December 2022. It benefits from a relatively low average cost of debt (3.8% on average excluding Euribor). However, we note Summus' exposure to interest rate risk as its bank loans pay variable interest rates, which is partially mitigated by the policy to have interest rate swaps on at least 50% of its loans (54% to Q2 2023).

Outlook and rating-change drivers

The Outlook remains Stable and incorporates our expectation that rental growth will strengthen cash generation, supported by the occupancy rate remaining above 97% on average and the high share of inflation-linked leases. The rating case assumes the Scope-adjusted loan/value ratio will stay below 55%.

A positive rating action is possible if the Scope-adjusted loan/value ratio decreased to around 50% while the company significantly grew in size, thereby decreasing portfolio concentration. This could be achieved through new acquisitions financed with a high share of equity relative to debt.

A negative rating action is possible if Scope-adjusted EBITDA interest cover decreased below 2.0x and/or leverage increased, indicated by a Scope-adjusted loan/value ratio towards 60% on a sustained basis. Leverage could rise if property values in the portfolio dropped considerably due to a shock in the Baltic real estate market, particularly regarding shopping centres, or if new properties are acquired via external financing with higher leverage than in the rating base case.

Rating history

Date	Rating action/monitoring review	Issuer rating & Outlook
5 September 2023	Affirmation	BB/Stable
5 September 2022	Affirmation	BB/Stable
3 September 2021	Initial	BB/Stable

Ratings & Outlook

Issuer	BB/Stable
Senior unsecured debt	BB

Analyst

Rigel Patricia Scheller
+49 30 27891 319
r.scheller@scoperatings.com

Related Methodologies and Related Research

General Corporate Rating Methodology; July 2022

European Real Estate Corporates Rating Methodology January 2023

Scope Ratings GmbH

Lennéstraße 5
10785 Berlin

Phone +49 30 27891 0
Fax +49 30 27891 100

info@scoperatings.com
www.scoperatings.com

Bloomberg: RESP SCOP

Rating and rating-change drivers

Positive rating drivers	Negative rating drivers
• Good diversification across the Baltic countries, with exposure to second-tier investment markets with healthy demand from tenants • High and stable occupancy rate of above 97% as at end-June 2023 • Stable EBITDA margin of above 80% in the last few years • Moderate WAULT of about five years to first break option • Moderate Scope-adjusted EBITDA/interest cover of 2.3x in 12 months to end-June 2023; expected to remain slightly above 2x	• Small player in the European context, with small market shares amid increasing competition • Significant exposure to retail (about 50%), a segment under increasing pressure from e-commerce, particularly fashion • Modest tenant diversification (main tenant represents 7.6% of total rental income; top 10, 36%) • High leverage, with Scope-adjusted loan/value ratio of 52% as of end-June 2023 • Negative discretionary cash flow due to portfolio expansion in the next few years

Positive rating-change drivers	Negative rating-change drivers
• Decrease in Scope-adjusted loan/value ratio to below 50% while company significantly grows in size	• Decrease in debt protection to below 2x and/or increase in Scope-adjusted loan/value ratio to above 60% • Worsened liquidity

Corporate profile

Summus Capital OÜ, headquartered in Estonia, is a family-owned real estate investment holding company active in the Baltic countries. The company pursues a buy-and-hold investment strategy and its income-generating portfolio includes commercial properties (retail, offices, logistics and medical premises). Summus was founded in 2013 and holds a portfolio with a total market value of about EUR 400m.

Financial overview

				Scope estimates	
Scope credit ratios	**2021**	**2022**	**LTM 2023[1]**	**2023E**	**2024E**
Scope-adjusted EBITDA/interest cover	2.8x	2.6x	2.3x	2.0x	2.4x
Scope-adjusted debt/EBITDA	9.7x	8.8x	8.4x	9.1x	8.4x
Scope-adjusted loan/value ratio (%)	51%	51%	52%	50%	51%
Scope-adjusted EBITDA in EUR m					
EBITDA	20.7	23.9	25.6	23.5	26.4
Operating lease payments	0.0	0.0	0.0	0.0	0.0
Other items	0.0	0.0	0.0	0.0	0.0
Scope-adjusted EBITDA	20.7	23.9	25.6	23.5	26.4
Scope-adjusted funds from operations in EUR m					
Scope-adjusted EBITDA	20.7	23.9	25.6	23.5	26.4
less: (net) cash interest as per cash flow statement	-7.4	-11.9	-13.1	-13.0	-12.1
less: cash tax paid as per cash flow statement	0.0	-0.3	-0.3	-0.8	-0.5
Others (provisions, impairments)	-3.0	5.9	8.9	3.0	0.0
Scope-adjusted funds from operations	10.3	17.6	21.1	12.7	13.8
Free operating cash flow in EUR m					
Funds from operations	10.3	17.6	21.1	12.7	13.8
Change in working capital change	1.8	5.6	14.5	1.0	-0.3
Non-operating cash flow	0.0	0.0	0.0	0.0	0.0
less: capital expenditure (net)	-0.2	0.9	1.4	-0.4	-0.4
Free operating cash flow	11.9	24.1	37.0	13.3	13.1
Net cash interest paid in EUR m					
Net cash interest as per cash flow statement	-7.4	-11.9	-13.1	-13.0	-12.1
add: interest component, operating leases	0.0x	0.0x	0.0x	0.0x	0.0x
Net cash interest paid	-7.4	-11.9	-13.1	-13.0	-12.1
Scope-adjusted debt in EUR m					
Reported gross financial debt	236.1	249.9	241.0	238.1	242.3
Shareholder loan – equity credit	-27.6	-24.0	-17.3	-17.2	-17.2
Other financial loans	4.7	0.0	0.0	0.0	0.0
Leasing	2.6	2.3	2.2	2.3	2.3
less: cash, cash equivalents	-15.1	-16.4	-10.7	-10.3	-5.2
Scope-adjusted debt	200.7	211.8	215.3	212.8	222.2

[1] Last 12 months to end-June 2023 for cash flow-related metrics

Table of contents

Environmental, social and governance (ESG) profile[2]

Environment		Social		Governance	
Resource management (e.g. raw materials consumption, carbon emissions, fuel efficiency)	Grey leaf	Labour management		Management and supervision (supervisory boards and key person risk)	Grey leaf
Efficiencies (e.g. in production)		Health and safety (e.g. staff and customers)		Clarity and transparency (clarity, quality and timeliness of financial disclosures, ability to communicate)	Grey leaf
Product innovation (e.g. transition costs, substitution of products and services, green buildings, clean technology, renewables)	Grey leaf	Clients and supply chain (geographical/product diversification)		Corporate structure (complexity)	Grey leaf
Physical risks (e.g. business/asset vulnerability, diversification)		Regulatory and reputational risks		Stakeholder management (shareholder payouts and respect for creditor interests)	Grey leaf

Legend

Green leaf (ESG factor: credit-positive)

Red leaf (ESG factor: credit-negative)

Grey leaf (ESG factor: credit-neutral)

ESG considerations

As at June 2023, about 77.5% of the portfolio's gross asset value is BREEAM-certified. The company aims to increase the proportion of environmentally certified properties in its portfolio and is in the process of certifying three further assets . Summus' medium-term goal is to have 95% of the portfolio BREAAM/LEED-certified. Summus also aims to optimise energy consumption in its buildings and to generate 69% of energy from renewables.

This initiative is expected to enhance the portfolio's attractiveness and company profitability as: i) work to attain certification improves energy efficiency and increases portfolio efficiency; and ii) environmentally friendly landlords are attractive since high-quality prospective tenants are increasingly concerned with sustainability.

[2] These evaluations are not mutually exclusive or exhaustive as ESG factors may overlap and evolve over time. We only consider ESG factors that are credit-relevant, i.e. those that have a discernible, material impact on the rated entity's cash flow and, by extension, its credit quality.

Business risk profile: BB

Industry risk profile: BB

Summus' activities encompass the acquisition and management of commercial real estate, mainly offices, shopping centres and logistics buildings in the Baltic region. The portfolio consists of 14 properties, including shopping centres (about 62% of total rental income), office buildings (17%), medical services premises (9%) and industrial buildings (11%).

Stable performance in 12 months to end-June 2023

Summus buy-and-hold investment approach provides stable rental cash flows. The portfolio generated EUR 28m in net annual rental income in 2022, up 29% YoY. Scope-adjusted total assets grew slightly by 5% YoY to EUR 412m at end-2022. The addition of two properties (Depo DIY and Damme shopping centre) compensated for the disposal of a small production and warehouse building in Tartu.

Small in a European context

Nonetheless, Summus is still a small property company in the European context. This relatively small scale implies a greater sensitivity to unforeseen shocks, greater cash flow volatility and higher key person risk. In this light, we view Summus' competitive position as weaker than its larger peers.

Small market shares with some visibility through its shopping centres

Summus' market shares are modest in the fragmented Baltic commercial real estate market. Since the company's portfolio is split across multiple asset classes and locations (mainly Vilnius, Tallin and Riga) it does not have substantial power or visibility in its markets.

As regards retail (about 60% of the portfolio's net lettable area), the company has increased its presence in Latvia via the acquisition of two new assets: i) Damme Riga, a leading shopping centre in Riga (16,000 sq m); and ii) Depo DIY (19,400 sq m).

Good geographical diversification, with assets spread across the Baltic region

Summus' portfolio is well diversified but remains focused on the Baltic region: Estonia (18% of total property value), Lithuania (42%) and Latvia (40%), second-tier investment markets in terms of size and demand from international investors. While the Baltic countries form a closely integrated economic area, there are still asymmetries among them. Estonia is the most exposed to international fluctuations, whereas Lithuania (the most populated of the three) is more resilient. Summus benefits from the slightly different demand patterns, influenced by the different industries in its markets.

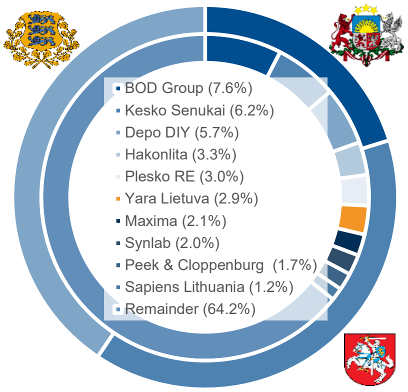
The company intends to continue to expand the portfolio in the next years and is constantly seeking new investment opportunities in the Baltics and neighbouring countries. However, rising interest rates will slow its growth pace due to the higher cost of capital and fewer opportunities in core markets as shifting monetary policies in Europe, including several rate hikes by the ECB, have increased borrowing costs and thereby slowed commercial real estate trade. We therefore expect Summus' geographical foothold to remain predominantly in the Baltic countries but with an increased presence in Latvia (40% of total rental income).

Modest tenant diversification, partially mitigated by moderate tenant quality

Tenant diversification is still modest despite more than 400 tenants in the portfolio, with the top 10 accounting for about 36% of rental income. The tenant mix includes medium and small tenants, mainly in the retail segment (more than 50% of net rental income), exposing the company to major changes in consumer habits accelerated by the pandemic such as the shift to e-commerce. BOD Group, the largest tenant, provides 7.6% of rental income as of June 2023.

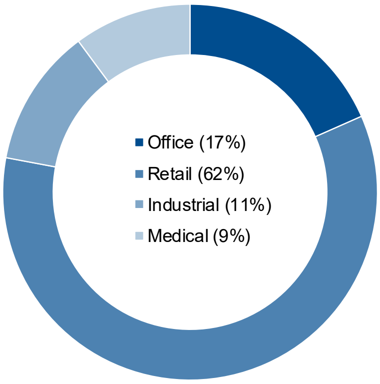
Of the top 10 tenants, only two have a credit rating, one being investment grade. Even so, the tenant mix has had negligible bad-debt rates since 2016 of below 0.5%. The presence of bank guarantees or cash deposits as well as the high and stable occupancy of the portfolio partially mitigates the risk of a single tenant default and its effect rental cash flow.

Figure 1: Geographical (outer ribbon) and tenant diversification (inner ribbon) by net rental income



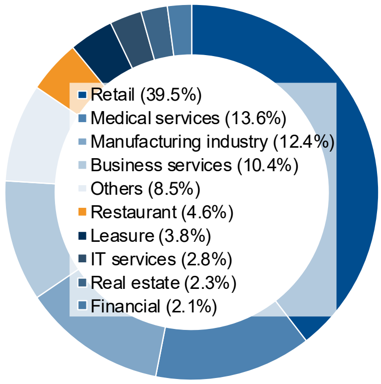
Sources: Summus, Scope

Figure 2: Property type diversification by net rental income



Sources: Summus, Scope

Figure 3: Tenants by industry



Sources: Summus, Scope

High and stable occupancy rate and medium-term WAULT provide cash visibility

The portfolio's high occupancy rate in the last few years (97% as of June 2023) has helped to keep net rental income stable. Average occupancy benefits from the office and industrial assets, which are fully let, but is also influenced by the shopping centres, which have some vacancies. The largest asset in the portfolio, Riga Plaza, has still an 8% vacancy rate as of June 2022 (12% in the prior year). We expect occupancy to remain above 95% based on healthy demand among tenants and Summus' ability to keep occupancy high.

Although demand for the assets is stable, worsening macroeconomic conditions and unforeseen shocks remain a risk. A slowdown in the economy could directly translate into softer demand and the closure of some branches, particularly in the retail segment.

High quality assets with 77.5% BREEM or LEED-certified

As at June 2023, about 77.5% of the portfolio's gross asset value is LEED or BREEAM-certified, including office buildings Park Town West and Park Town East and shopping centre Nordika; a further 8.9% is in the process of certification. Summus' medium-term goal is 95%. Although demand for office space is uncertain as some tenants are holding off on operational decisions, we expect Summus' office portfolio to continue to enjoy robust demand due to tenants' preference towards best-in-class, energy-efficient space in prime locations, and all of Summus' office buildings have LEED or BREEAM certifications. Regarding the retail portfolio (over 50% of rental income) Summus' properties proved resilient during the Covid-19 pandemic with no significant impact on rent collections and footfall continues to recover.

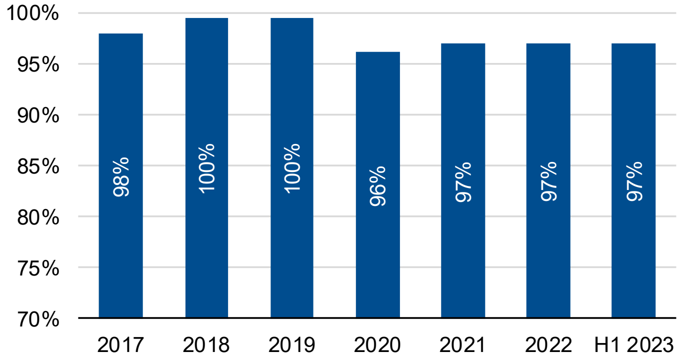
The company's estimated medium-term WAULT to first break of around four years as of June 2023 provides some visibility on future cash flows. Re-letting risk in the short term mostly concerns the retail properties, which are particularly under threat from the rise of e-commerce and fluctuating demand.

Relatively modern property portfolio

The average portfolio age is 7.9 years. The portfolio ranges from newer properties such as the two medical centres (Veerenni 1, in operation since 2017; Veerenni 2, since 2020) and Depo DIY (since 2021) and older ones such as De la Garde (2000). The assets benefit from either a central location, a resilient neighbourhood catchment or strategic locations to tenants.

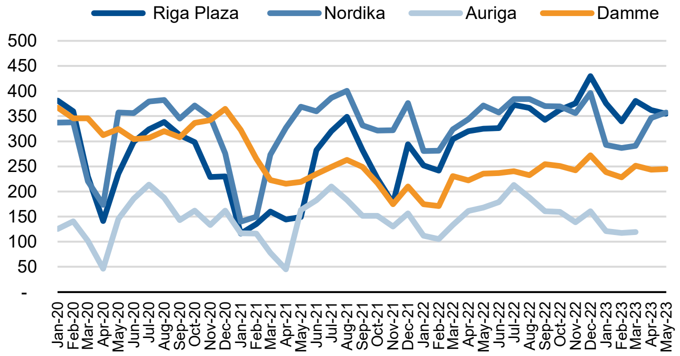
The recovery in retail asset footfall following the easing of pandemic restrictions will enhance demand for the shopping centres' products and services. Summus budgets yearly about EUR 0.3m to EUR 0.4m for regular property maintenance. More recently, it started energy audits for all Estonian properties to map current energy consumption (technical systems, sensors, lights, ventilation, heating, cooling, outside lights, BMS etc.) and define improvement areas.

Figure 4: Historical occupancy rate



Sources: Summus, Scope

Figure 5: Retail assets footfall (thousands)



Sources: Summus, Scope

Stable profitability ratios

Profitability, as measured by the Scope-adjusted EBITDA margin, was stable and above 80% as at end-June 2023. We foresee the EBITDA margin to remain stable in the next few years. In 2022, increasing energy costs put pressure on operations, but this has eased in the last months. Summus can pass on around 62% of utilities costs through lease agreements and most tenants with fixed-rate agreements pay for electricity consumption as measured by counters. In addition, we expect the inflation-driven rise in costs to be balanced out by corresponding rental growth as around 95% of lease contracts have an indexation clause.

Financial risk profile: BB

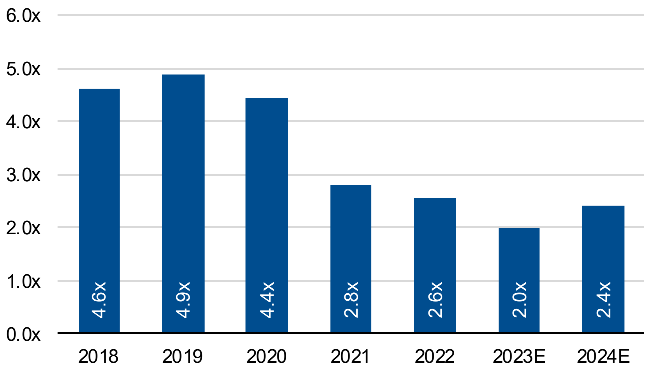
Increasing debt costs to impact debt protection

Debt protection, as measured by Scope-adjusted EBITDA interest cover, stood at 2.6x in December 2022 (2.3x for the 12 months to June 2023). We expect debt protection to remain above 2x on the back of stable operating cash flow and a relatively low average cost of bank financing (3.8% excluding Euribor). Summus is exposed to interest rate risk as its bank loans pay variable interest rates (2.3%-2.9% + Euribor). This risk is partially mitigated by the company's policy to have interest rate swaps on at least 50% of its loans (54% to Q2 2023) and its intention to partially increase the portion of fixed-rate debt. However, any new debt will bear higher interest rates, and the unhedged share of debt allows the pass-through of rate increases observed in the last months. Still, interest cover should remain above 2x, supported by the issuer's inflation-linked revenue base.

Portfolio expansion at a slower pace

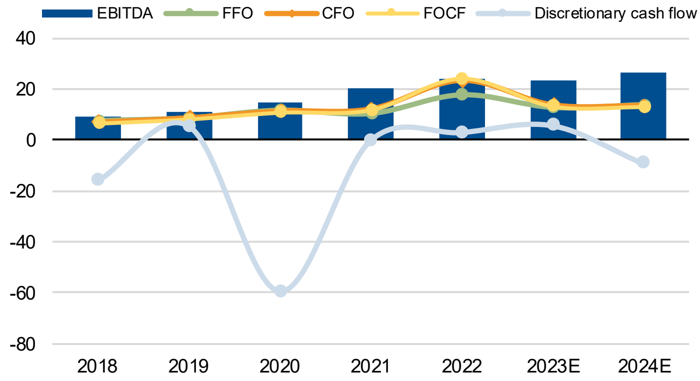
Scope-adjusted free operating cash flow has been positive in the past years, which was mainly used for acquiring properties. For the next few years, we expect positive internal cash flow (Scope-adjusted EBITDA, Scope-adjusted funds from operations and Scope-adjusted free operating cash flows) thanks to solid recurring rental income and further acquisitions of income-generating assets. Discretionary cash flow might turn negative, driven by potential acquisitions in 2023-24, though assumed to be done at a slower pace.

Figure 6: Scope-adjusted EBITDA interest cover (x)



Sources: Summus, Scope estimates

Figure 7: Cash flows (EUR m)

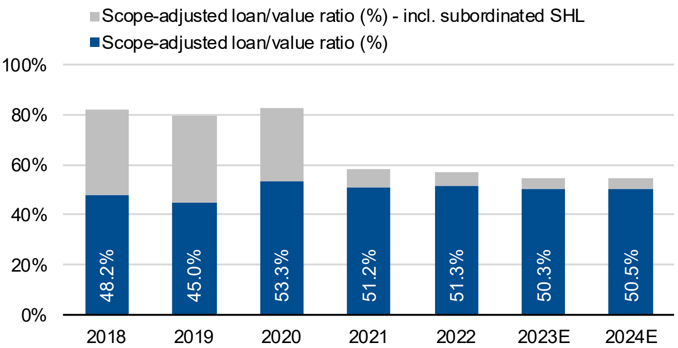


Sources: Summus, Scope estimates

Adequate leverage, but vulnerable to downside market-related volatility

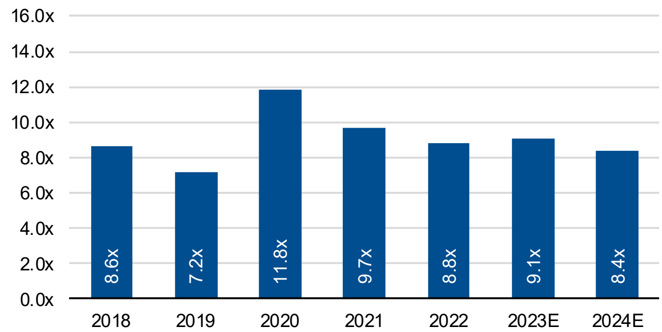
Leverage, as measured by the Scope-adjusted loan/value ratio, stabilised as expected in a range of 50%-55% (end-June 2023: 52%), not considering outstanding subordinated loans from the shareholder (EUR 17.2m as at June 2023). Summus' portfolio is exposed to market pressure that could lead to yield expansion, as the rising interest rates has led to uncertainty regarding property values (negative fair value of EUR 5.4m in 2022). We expect the portfolio value to remain resilient but foresee minor adjustments of about 1%-2% by end-2024, driven by further yield widenings because of the potential lag of 12-24 months between a change in interest rates and its full reflection in property yields. Like-for-like rental growth in the next years – as the market will remain supportive – will likely compensate expected yield expansion. With indebtedness to remain broadly stable, Scope-adjusted loan/value ratio will remain at around 50% in the rating case.

Figure 8: Scope-adjusted loan/value ratio



Sources: Summus, Scope estimates

Figure 9: Scope-adjusted debt/EBITDA



Sources: Summus, Scope estimates

Adequate liquidity

Summus' liquidity is adequate, supported by unrestricted cash (EUR 11.2m as at end-June 2023) and positive operating cash flow that covers short-term debt of about EUR 7m. Even if free operating cash flow turns negative due to investments in the next few years, capex is mostly discretionary and will be financed by available internal resources and financial debt.

Balance in EUR	2022	2023E	2024E
Unrestricted cash (t-1)	15.1	16.4	10.3
Open committed credit lines (t-1)	0.0	0.0	0.0
Free operating cash flow	24.1	13.3	13.1
Short-term debt (t-1)	-42.4	-8.5	-8.9
Coverage	**0.9x**	**3.5x**	**2.6x**

Long-term and short-term debt ratings

Senior unsecured debt rating: BB

Summus has a EUR 10m senior unsecured corporate bond in terms of capital market debt as at end-June 2023. The bond's tenor is three years with a fixed coupon of 6.75% and payments made four times a year.

The recovery analysis is based on a hypothetical default scenario in FY 2024 with a company liquidation value based on a haircut of 25% to reflect liquidation costs, reasonable discounts to assets and 10% for insolvency proceedings. We expect an 'above average' recovery for Summus' senior unsecured debt (EUR 10m) but note the high sensitivity of the portfolio to property advance rates. We have therefore affirmed the debt class a rating of BB, in line with the issuer rating.

Appendix: Peer comparison (as at last reporting date)

	Summus Capital OÜ	NEPI Rockcastle Plc	Globe Trade Centre S.A.	Deutsche Konsum REIT AG
	BB/Stable	--/--*	BBB-/Stable	--/--*
Last reporting date	31 June 2023	31 Dec 2022	30 Dec 2022	31 Dec 2022
Business risk profile				
Scope-adjusted total assets (EUR m)	412	6,900	2,518	50,476
Portfolio yield	7.4%	6.8%	6.8%	4.5%
GLA (thousand sq m)[3]	212	2,149	762	8,332
Number of residential units	na	na	na	na
Countries active in	3	9	6	12
Top 3 tenants (%)	20%	12%	11%	na
Top 10 tenants (%)	36%	25%	25%	na
Office (share NRI)	17%	1%	69%	3%
Retail (share NRI)	62%	99%	31%	91%
Residential (share NRI)	0%	na	na	na
Hotel (share NRI)	0%	na	na	na
Logistics (share NRI)	11%	na	na	na
Others (share NRI)	9%	0%	na	6%
Property location	'B'	'B'	'B'	'A' to 'B'
EPRA occupancy rate (%)	97.1%	97.3%	88.0%	93.5%
WAULT (years)	4.0	3.1	3.7	3.6
Tenant sales growth (%)	na	31.4%	na	127.0%
Like-for-like growth rents (%)	na	5.7%	na	27.4%
Occupancy cost ratio (%)	na	12.1%	na	15.0%
Scope-adjusted EBITDA margin	87%	89%	82%	76%
EPRA cost ratio (incl. vacancy)	na	11.7%	10.8%	20.8%
EPRA cost ratio (excl. vacancy)	na	11.6%	25.4%	17.4%
Financial risk profile				
Scope-adjusted EBITDA/interest cover	2.3x	8.0x	3.7x	3.7x
Scope-adjusted loan/value ratio	52%	34%	46%	49%
Scope-adjusted debt/EBITDA	8.4x	6.3x	11.5x	10.2x
Weighted average cost of debt	3.8%	2.3%	2.2%	2.0%
Unencumbered asset ratio	> 200%	> 200%	> 200%	>200%

* Subscription ratings available on ScopeOne

Sources: Public information, Scope

[3] Unweighted GLA

Scope Ratings GmbH

Headquarters Berlin

Lennéstraße 5
D-10785 Berlin

Phone +49 30 27891-0

Frankfurt am Main

Neue Mainzer Straße 66-68
D-60311 Frankfurt am Main

Phone +49 69 66 77 389 0

Paris

10 avenue de Messine
FR-75008 Paris

Phone +33 6 62 89 35 12

Oslo

Karenslyst allé 53
N-0279 Oslo

Phone +47 21 09 38 35

Madrid

Paseo de la Castellana 141
E-28046 Madrid

Phone +34 91 572 67 11

Milan

Via Nino Bixio, 31
20129 Milano MI

Phone +39 02 30315 814

Scope Ratings UK Limited

London

52 Grosvenor Gardens
London SW1W 0AU

Phone +44 20 7824 5180

info@scoperatings.com
www.scoperatings.com

Disclaimer