Summus Capital OÜ
Estonia, Real Estate

BB STABLE

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 currently holds a portfolio with a total market value of about EUR 300m.

Key metrics

			Scope estimates	
Scope credit ratios	**2019**	**2020**	**2021E**	**2022E**
Scope-adjusted EBITDA/interest cover (x)	4.9x	3.4x	2.4x	2.2x
Scope-adjusted debt (SaD)/EBITDA	7.2x	15.5x	11.2x	11.1x
Scope-adjusted loan/value (%)	45%	53%	55%	57%

Rating rationale

Scope Ratings GmbH (Scope) has assigned a first-time issuer rating of BB to Summus Capital OÜ.

Summus' business risk profile (assessed at BB) is driven by the quality of its commercial real estate portfolio, with assets located in Baltic capital cities, second-tier investment markets with stable tenant demand. This is evidenced by the portfolio's high and stable occupancy rate (96% as of December 2020). The rating is underpinned by its 'buy-and-hold' investment approach, which results in stable rental cash flow generation. Although over 50% of its rental income is derived from retail tenants, Summus' properties proved resilient during the Covid-19 pandemic, with no significative impact on rent collections (around 3.6% of the portfolio's annual rent cash flow). Profitability, as measured by the Scope-adjusted EBITDA margin, remained stable and above 60% in the last few years. We expect occupancy to remain at above 95% based on healthy demand in the tenant market and the Summus demonstrated ability to keep high occupancy in the buildings.

The rating is mainly constrained by the company's small size and market shares, with Scope-adjusted total assets of around EUR 350m as of June 2020. Given its limited size, Summus does not have substantial market power and is highly exposed to unforeseen shocks and volatile cash flows, although this is partially mitigated by the portfolio's weighted average unexpired lease term (WAULT) of 5.4 years. Summus plans to expand its income-generating portfolio of properties and aims to invest about EUR 150m in the period to 2023. Despite this, we expect Summus to remain relatively small in the European context and exposed to the retail segment. Tenant diversification is modest, with the top 10 contributing 45% of total rental income. Although some major tenants also have strong credit quality, a large, unexpected vacancy could still have a material impact.

Summus' financial risk profile (assessed at BB) is driven by its moderate credit metrics. Debt protection, as measured by Scope-adjusted EBITDA interest cover of 3.4x as at December 2020, benefits from a relatively low average cost of debt (2.8% on average). Although we anticipate further increase in the company's indebtedness, we expect debt protection will remain above 2x, driven by the positive cash flow contribution from planned acquisitions (estimated additional uplift of EUR 10m in gross rental income by 2023).

Ratings & Outlook

Corporate ratings	BB/Stable
Senior unsecured rating	BB

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Related Methodology

Corporate Rating Methodology: July 2021

Rating Methodology: European Real Estate Corporates January 2021

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Bloomberg: RESP SCOP

Leverage, as measured by the Scope-adjusted loan/value ratio, stood at 53% as at December 2020, not considering outstanding majority shareholder loans of EUR 98.6m, of which about 80% was converted into equity in April 2021. We forecast that the Scope-adjusted loan/value ratio will increase towards 60% in the coming years. This is based on the most recent EUR 10m bond issuance, approx. EUR 100m in additional loans needed to finance the company's business plan and the assumption of a 65% loan/value ratio financing structure for the intended acquisitions.

Outlook and rating change drivers

The Outlook is Stable and incorporates: i) the successful execution of Summus' business plan including intended acquisitions in the next few years; ii) the extension of Riga Plaza, currently pre-let on a long-term lease basis; and iii) the portfolio's average occupancy rate to remain above 95%. Our rating case assumes that the Scope-adjusted loan/value ratio will increase towards 60%.

A positive action is possible if the Scope-adjusted loan/value ratio (leverage) decreases to around 50% while the company grows in size, thereby decreasing portfolio concentration. This could be achieved by new acquisitions financed with a higher share of equity relative to debt.

A negative rating action is possible if Scope-adjusted EBITDA interest cover decreases below 2.0x and/or leverage increases, indicated by a Scope-adjusted loan/value ratio above 60%. Leverage could rise if property values in the portfolio drop considerably due to a sudden 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 our rating base case.

Rating 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 95% in the last years • Stable EBITDA margin of above 60% • Moderate WAULT of 5.4 years to first-break option • Moderate Scope-adjusted EBITDA/interest cover of 3.4x in 2020 and expected to remain above 2x	• Small player in the European context, with relatively small market shares an increasingly competitive environment • Significant exposure to retail (54%), segment that has been facing increasing pressure from e-commerce for some years, particularly the retail fashion industry • Modest tenant diversification (main tenant represents 9% of total rental income, while top 10 represent 45%) • High leverage, with Scope-adjusted loan/value ratio of 53% in 2020 expected to increase towards 60% in the next few years • Negative discretionary cash flow due to portfolio expansion in the next few years

Rating-change drivers

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

Financial overview

			Scope estimates		
Scope credit ratios	**2019**	**2020**	**2021E**	**2022E**	**2023E**
Scope-adjusted EBITDA/interest cover (x)	4.9x	3.4x	2.4x	2.2x	2.1x
Scope-adjusted debt (SaD)/EBITDA	7.2x	15.5x	11.5x	11.3x	11.9x
Scope-adjusted loan/value ratio (%)	45%	53%	55%	57%	59%
Scope-adjusted loan/value ratio (%) - incl. SHL*	80%	83%	60%	62%	64%
Scope-adjusted EBITDA in EUR m	**2019**	**2020**	**2021E**	**2022E**	**2023E**
EBITDA	10.9	11.4	18.6	21.7	24.0
Operating lease payment in respective year	0.0	0.0	0.0	0.0	0.0
Other	0.0	0.0	0.0	0.0	0.0
Scope-adjusted EBITDA	10.9	11.4	18.6	21.7	24.0
Scope-adjusted funds from operations in EUR m	**2019**	**2020**	**2021E**	**2022E**	**2023E**
Scope-adjusted EBITDA	10.9	11.4	18.6	21.7	24.0
less: (net) cash interest as per cash flow statement	-2.2	-3.4	-10.3	-11.3	-12.8
less: cash tax paid as per cash flow statement	0.0	0.0	-1.5	-2.0	-2.2
Others (provisions, impairments)	0.0	0.0	0.0	0.0	0.0
Scope-adjusted funds from operations	8.6	8.1	6.9	8.4	9.0
Scope-adjusted debt in EUR m	**2019**	**2020**	**2021E**	**2022E**	**2023E**
Reported gross financial debt	149.5	274.4	227.9	270.9	307.6
SHL – equity credit	-60.0	-98.6	-20.8	-20.8	-20.8
Other financial loans	10.2	13.6	13.6	2.4	2.4
less: cash, cash equivalents	-21.7	-11.5	-11.3	-11.1	-8.5
Scope-adjusted debt	77.9	177.9	209.4	241.5	280.7

* Calculation including majority shareholder loan

Business risk profile: BB

Industry risk: BB

Summus' activities encompass the acquisition and management of commercial assets, mainly including offices, shopping centres and logistics buildings in the Baltic region.

Small property company exposed to sudden shocks and the real estate cycle

Summus is a relatively small property company in the European context, with Scope-adjusted total assets of about EUR 350m as of June 2021. 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 being weaker than its larger peers. The company is targeting some growth in the next few years, including the acquisition of new assets for approx. EUR 150m and the investment of EUR 3.6m to expand the recently acquired Riga Plaza. However, despite these investments, we expect Summus to remain relatively small in a European context.

Small market shares with some visibility through its shopping centres

Summus' market shares are modest in the fragmented Baltic commercial real estate markets. Since the company's portfolio is split across multiple asset classes and locations (mainly Vilnius, Tallin and Riga) it does not have substantial market power or visibility in the markets in which it operates. This makes it vulnerable to pressure from other players in an increasingly competitive environment. Such is the case of the office segment, where Scope estimates Summus market shares to be around 2.5% in Vilnius and 2% in Tallin[1]. In addition, demand for modern space in Vilnius has led to a very dynamic development pipeline: in 2021, the largest amount of new office space (about 135,000 sq m) in the city's history will open. Likewise, 60,000 sq m will be completed in Tallin in 2021.

As regards retail (more than 50% of the portfolio's net leasable area), the company has increased visibility through its ownership of two large shopping centres: i) Riga Plaza, the fourth largest in the city, at around 51,000 sq m (6% of total leasable space in Riga); and ii) Nordika with 31,000 sq m (8% of the total leasable area in Vilnius). Some large projects are under construction: around 90,000 sq m in Vilnius and 50,000 sq m in Riga. Summus' assets have also proven resilient, shown by the high occupancy rates in the last few years.

Portfolio diversified across the Baltic region

Summus' portfolio is diversified across the Baltic region: Estonia (25% of the total property value), Lithuania (47%) and Latvia (28%). 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. This was evidenced in 2020 when Lithuania's GDP dropped by just 0.8%, the least among the Baltic countries (and one of the lowest in the EU), while Estonia's decreased by 2.9%. As such Summus can benefit from slightly different demand patterns, influenced by the different industries in its markets.

Modest tenant diversification, partially mitigated by moderate tenant quality

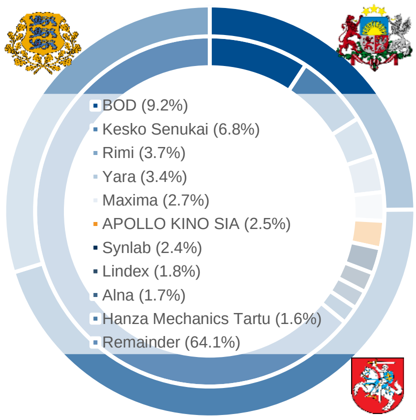
Although having a fairly diversified tenant base structure, with more than 320 tenants on its portfolio of assets, Summus is exposed to tenant concentration. The top three and top 10 tenants represent 20% and 45% of total rental income, respectively; thus any large, unexpected vacancy could have a material impact. The largest tenant, BOD Group (main industrially recorded CD, DVD and Blue-Ray manufacturer in the Baltic States) provides 9% of rental income as of June 2021. Tenants mostly come from retail (around 40% of NRI), followed by medical services (14%) and manufacturing (12%).

Whilst the assets in the portfolio have benefited from stable demand, worsening macroeconomic conditions and unforeseen shocks are expected to directly translate into softer demand, and the possible closure of some branches, particularly in the segment retail, which is going through major changes, including: rise in e-commerce and shift in

[1] Considering a total office stock of 887k sqm in Vilnius and 1m sqm in Tallin. Real Estate Market report 2021. Ober-Haus Real Estate Advisors.

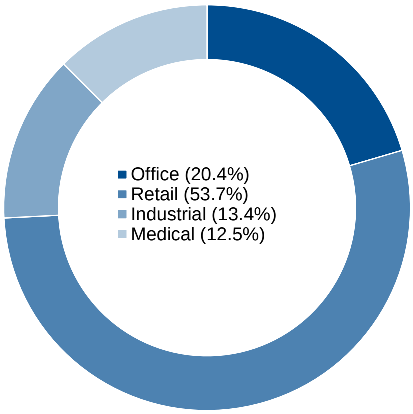
consumer habits exacerbated by the pandemic. This is partially mitigated by i) many traders and service providers preferring to locate their sales or service outlets directly in shopping centres; ii) tenant mix including largest retail chains, like Rimi and Maxima, that have continued their expansion even during the pandemic; and iii) the presence of bank guarantees or cash deposits that partially mitigates the risk of a single tenant default, which could impair rental cash flow.

Figure 1: Geographical (outer ribbon) and tenant diversification (inner ribbon) by NRI[2]



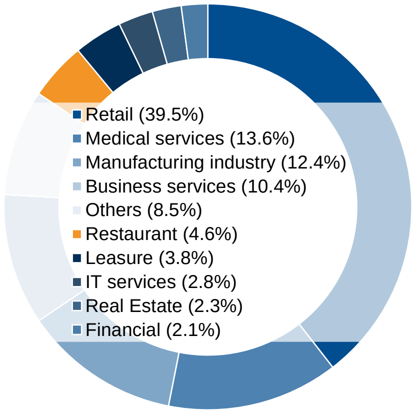
Sources: Summus, Scope

Figure 2: Property type diversification by NRI



Sources: Summus, Scope

Figure 3: Tenants by industry



Sources: Summus, Scope

Baltics, second-tier investment markets in Europe

The whole portfolio consists of eleven properties, including shopping centres (54% of total gross asset value), office buildings (20%), medical services premises (12%) and industrial buildings (13%). All of the properties are located in Latvia, Lithuania and Estonia, i.e. in second-tier investment markets in terms of size and demand from international investors. If the economy cools and/or interest rates rise, investors are likely to focus on tier-one markets and safe havens like London, Paris or the seven major German cities. This could eventually lead to substantial downward pressure on property values, an increase in leverage, the reduced availability of external financing, and limited recovery expectations for debt investors.

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

The high occupancy rate of the company's property portfolio in the last few years (96% as of December 2020) has helped to keep net rental income generation stable. Rental increases were mainly due to additions to the portfolio (Park Town East Hill and Riga Plaza added in 2020). Average occupancy benefits from the office assets, which are fully let, but is also influenced by the shopping centres, which have some vacant areas. The largest asset in the portfolio, Riga Plaza, has a 12% vacancy rate. New leases are being negotiated, with about 25% already signed. In 2022, the company plans to add 3,000 sq m of leasable area, already pre-let to a long-term tenant.

We expect the portfolio's average occupancy to remain above 95% based on healthy demand in the tenant market and the Summus demonstrated ability to keep high occupancy in the buildings.

The company's estimated medium-term WAULT to first break of 5.4 years as of June 2021 provides some visibility on future cash flows. There is only re-letting risk in the short term (about 10% of lease agreements due until 2022). This mostly concerns the retail

[2] NRI = net rental income

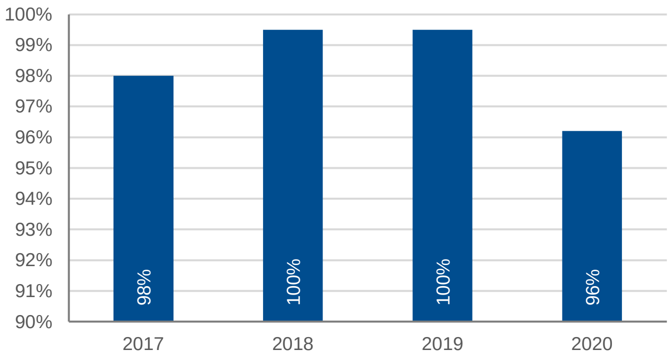
properties, which are particularly jeopardised by the rise of e-commerce (see also *Real Estate Outlook 2021*).

Good quality property portfolio

Asset quality is balanced, including new properties such as two medical centres (Veerenni 1 in operation since 2017 and Veerenni 2 in 2020) and older ones (e.g. De la Garde, built in 2000). The largest office buildings are BREEAM-certified (22% of the portfolio) enhancing portfolio attractiveness and company profitability. Altogether, the portfolio benefits from either a central location, a resilient neighbourhood catchment or strategic locations to tenants.

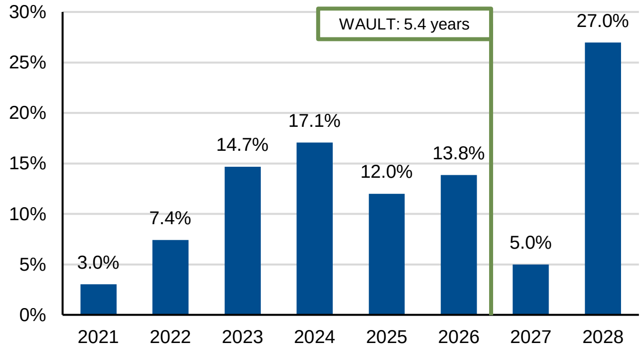
Summus budgets about 2-3% of revenue for regular maintenance. For Riga Plaza, the company has budgeted around EUR 2m for large investments in 2021 and 2022.

Figure 4: Historical occupancy rate



Sources: Summus, Scope

Figure 5: Lease maturities



Sources: Summus, Scope

Stable profitability ratios

Summus' profitability, as measured by its EBITDA margin, stood at 65% in 2020. This is lower than other buy-and-hold peers, some of which have margins above 80%. The company has managed to keep its asset occupancy rate high and estimates the impact of Covid-19 on total cash flows to be EUR 757,000 (in share value), which is around 3.6% of the portfolio's annual rent cash flow. We expect Summus' EBITDA margin to remain at levels above 65%. Profitability is supported by: i) the company's stable anchor tenant base; ii) the moderate WAULT; and iii) the recovery in the retail assets' footfall, which will enhance the demand for the centres' products and services, despite the increase in online sales during the lockdown.

Financial risk profile: BB

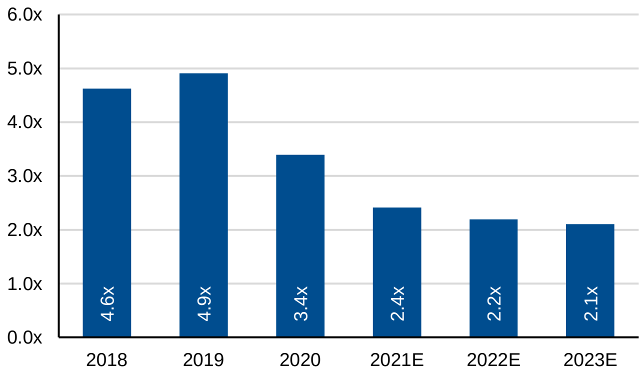
Adequate debt protection supported by positive operating cash flows

The company's debt protection, measured by its EBITDA interest cover, stood at 3.4x as at December 2020. We anticipate some pressure on debt protection as a result of the higher leverage component in the company's balance sheet after the acquisition of two large assets in 2020 (Park Town East Hill and Riga Plaza) and the bond placement in June 2021. However, we forecast that EBITDA interest cover will remain above 2x in the next few years, mainly benefiting from: i) the addition of income-producing assets, which will provide more certainty on recurring cash flows, with an estimated rental revenue uplift of about EUR 10m; and ii) the relatively low cost of bank financing (2.8% as at end of 2020).

Targeted portfolio expansion will squeeze free operating cash flows

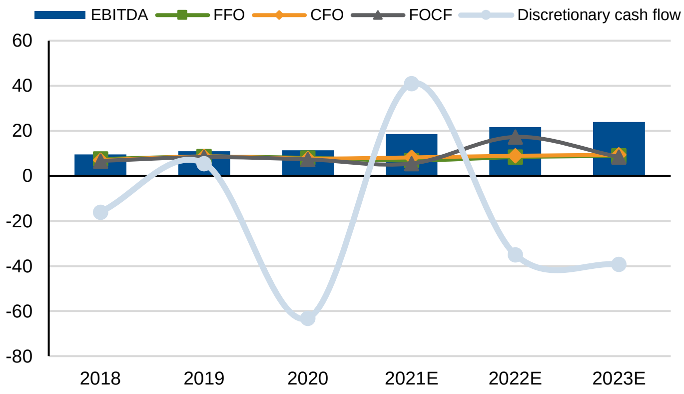
Summus has had positive Scope-adjusted free operating cash flow in the past few years. This cash flow has been mainly absorbed by the acquisition of investment properties. For the next few years, we anticipate positive internal cash flow (Scope-adjusted EBITDA, Scope-adjusted funds from operations and Scope-adjusted free operating cash flow). This is based on Summus' solid recurring rental income and the further acquisition of income-generating assets. Discretionary cash flow has been more volatile, influenced by the in-kind contribution via the conversion of the EUR 78.m shareholder loan into equity and the EUR 1.2m equity increase in the first semester of 2021. We expect it to turn negative from 2022 on, driven by the portfolio expansion planned for the 2021-2023 period, which involves intended acquisitions for about EUR 150m. These acquisitions will be partly financed by external bank debt, subsequently leading to higher leverage on the company's balance sheet.

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



Sources: Summus, Scope estimates

Figure 7: Cash flows (EUR m)



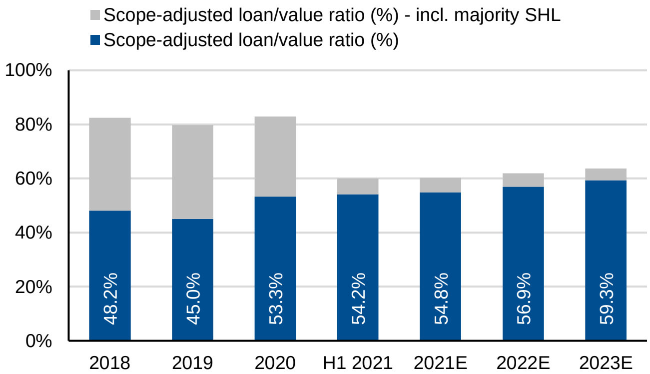
Sources: Summus, Scope estimates

Increasing leverage as measured by the company's loan/value ratio

Leverage, as measured by the Scope-adjusted loan/value ratio, stood at 53% as at December 2020, not considering outstanding majority shareholder loans of EUR 98.6m as at December 2020. In previous years, the company has financed its property acquisitions via a combination of bank loans and shareholder loans (including fully subordinated shareholder loans from majority interests and shareholder loans from minority parties). In April 2021, about 80% from majority shareholder loans (EUR 78.1m) were converted into equity, while the remainder remains fully subordinated to all other financial obligations, including secured bank loans, issued bonds (and all future issuances). In June 2021, Summus issued a EUR 10m senior unsecured bond to enhance its funding structure.

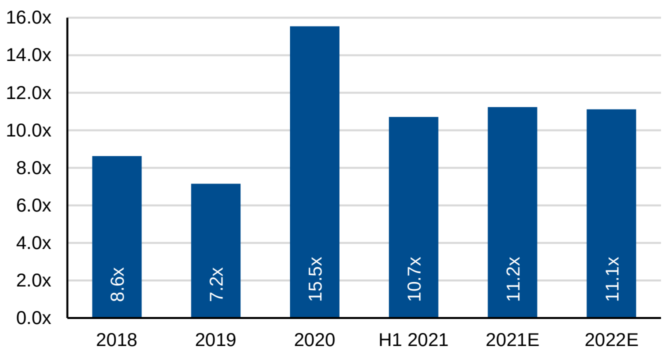
We forecast that the Scope-adjusted loan/value ratio will increase towards 60% in the coming years. This is based on the most recent EUR 10m bond issuance, approx. EUR 100m in additional loans needed to finance the company's business plan and the assumption of a 65% loan/value ratio financing structure for the intended acquisitions.

Figure 8: Scope-adjusted LTV ratio



Sources: Summus, Scope estimates

Figure 9: SaD/EBITDA



Sources: Summus, Scope estimates

Adequate liquidity

Summus' liquidity is adequate, supported by unrestricted cash (EUR 18m as at June 2021) and positive operational cash flow that covers short-term debt of about EUR 5m, due in the next twelve months. 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 a combination of available internal resources and financial debt, including the bond issuance and bank loans.

in EUR m	2020	2021E	2022E
Short-term debt (t-1)	-5.6	-8.9	-8.9
Unrestricted cash (t-1)	21.7	11.5	11.3
Open committed credit lines (t-1)	0.0	0.0	0.0
Free operating cash flow (t)[3]	7.3	5.4	17.3
Coverage	**5.1x**	**1.9x**	**3.2x**

Long-term and short-term debt ratings

Senior unsecured debt: BB

Summus issued a EUR 10m senior unsecured corporate bond in June 2021. The bond's tenor is three years with a fixed coupon of 6.75% and payments made four times per year. Proceeds are earmarked for the acquisition of revenue-generating properties.

Our recovery analysis is based on a hypothetical default scenario in FY 2022 with a company liquidation value of EUR 288m. This value is based on a haircut of 25% to reflect liquidation costs and reasonable discounts to the company's asset base as well as 10% for insolvency proceedings. This compares to secured financing of a forecasted EUR 230m and senior unsecured debt of EUR 10m.

We expect an 'above average' recovery for Summus' senior unsecured debt (EUR 10m) but note the high sensibility the sensibility analysis regarding the portfolio of property's advance rate and therefore assigns the debt class a rating of BB, in line with the issuer rating.

[3] We exclude discretionary expansion capex from our liquidity calculation, as such investments are only made if external financing is available.

Appendix I: Peer comparison

	Summus Capital OÜ	NEPI Rockcastle Plc	Fastpartner AB	Globe Trade Centre S.A.	Budapesti Ingatlan Nyrt.
	BB/Stable/--	-- / --	BBB-/Stable	BBB-/Stable/--	B+/Stable/--
Last reporting date	31.12.2020	31/12/2020	31/12/2020	31/12/2020	30/12/2020
Business risk profile					
Scope-adjusted total assets (EUR m)	330	6,028	3,018	2,198	161
Portfolio yield	7.0%	6.7%	4.6%	6.9%	7.3%
GLA (thousand sq m)	182	2,030	1,535	753	89
No. of residential units	0	na	na	na	0
Countries active in	3	9	1	6	1
Top 3 tenants (%)	20%	11%	9%	14%	53%
Top 10 tenants (%)	45%	24%	19%	26%	69%
Office (share NRI)	20%	2%	49%	65%	49%
Retail (share NRI)	54%	97%	12%	35%	0%
Residential (share NRI)	0%	na	1%	na	0%
Hotel (share NRI)	0%	na	2%	na	7%
Logistics (share NRI)	13%	na	16%	na	0%
Others (share NRI)	12%	1%	20%	na	44%
Property location	B	B	A	B	B
EPRA occupancy rate (%)	96%	96%	91%	91%	87%
WAULT (years)	5.4	4.1	4.7	2.9	2.5
Tenant sales growth (%)	na	-32%	na	na	na
Like-for-like rent growth (%)	na	-21%	na	-16%	na
Occupancy cost ratio (%)	na	15%	na	na	na
Scope-adjusted EBITDA margin	65%	80%	68%	87%	35%
EPRA cost ratio (incl. vacancy)	na	11%	na	na	na
EPRA cost ratio (excl. vacancy)	na	10%	na	na	na
Financial risk profile					
Scope-adjusted EBITDA interest cover (x)	3.4	6.1x	3.7x	3.3x	8.4x
Scope-adjusted loan/value ratio (%)	53%	31%	49%	48%	17%
SaD/Scope-adjusted EBITDA (x)	16x	6.2x	12.4x	10.0x	5.7x
Weighted average cost of debt (%)	2.8%	2.3%	2.0%	2.3%	na
Unencumbered asset ratio (%)	159%	278%	190%	364%	177%
Weighted average maturity (years)	3.9	4.1	3.2	4.2	13

Sources: Public information, Scope

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