Globe Trade Centre S.A.
Republic of Poland, Real Estate

SCOPE BBB- NEGATIVE

Key metrics

			Scope estimates	
Scope credit ratios	**2022**	**2023**	**2024E**	**2025E**
Scope-adjusted EBITDA interest cover	3.7x	3.6x	3.2x	2.8x
Scope-adjusted debt/EBITDA	11.5x	11.2x	12.4x	11.7x
Scope-adjusted loan/value ratio	46%	48%	51%	53%

Key rating drivers

GTC's business risk profile is driven by its unchanged position as one of the most important commercial real estate players in CEE and SEE (Scope-adjusted total assets of EUR 2.6bn at end-March 2024, up EUR 0.1bn YoY), which shows and is expected to show above-average profitability despite weakening asset quality with increasing obsolescence risk in parts of its office portfolio.

GTC's financial risk profile is driven by sustained high levels of capital expenditure, pressure on achievable rental levels, rising borrowing costs and further, but limited, yield widening, all of which are putting pressure on credit metrics that are seen to be on the verge of deteriorating to levels that are not commensurate with the rating.

Liquidity is considered adequate but close to being stretched. While short-term debt maturities are fully covered by cash sources, a longer-term view shows the company's reliance on external financing especially to refinance the EUR 500m bond in June 2026.

Outlook and rating sensitivities

The Outlook has been revised to Negative due to the risk of the Scope-adjusted loan/value ratio rising to around 55% as a result of continued pressure on capitalisation rates and ERVs, as well as the increased risk of inadequate liquidity, coupled with GTC's limited ability to reduce its debt burden over the next 18 months through cash generation from its standing portfolio, leaving it reliant on (i) the successful execution of asset sales to free up the required capital or (ii) the extension and increase of secured financing. The Outlook is based on the assumption of annual like-for-like rental growth of 3-5% between 2024 and 2026, capital expenditure of EUR 237m and dividend payments of EUR 90m, both over the same period. Proceeds from the asset sales programme are only included to the extent that they have been executed.

The upside scenarios for the ratings and Outlooks are collectively: (1) Successful and swift execution of the deleveraging plan, resulting in continued adequate liquidity as perceived by us, (2) Scope-adjusted loan/value ratio not increasing to around 55%, (3) Scope-adjusted EBITDA interest cover of above 2.2x.

The downside scenarios for the ratings and Outlooks are (individually or collectively): (1) Further, perceived liquidity deterioration, i.e. if significant debt maturities in 2026 are not addressed well in advance, (2) Scope-adjusted loan/value ratio of around 55% if continued pressure on portfolio value does not abate and GTC is unable to reduce indebtedness, (3) Scope-adjusted EBITDA interest coverage of less than 2.2x if GTC is unable to significantly reduce indebtedness or achieve strong Scope-adjusted EBITDA growth.

Rating history

Date	Rating action/monitoring review	Issuer rating & Outlook
10 Jun 2024	Outlook change	BBB-/Negative
11 Sep 2023	Affirmation	BBB-/Stable
22 Dec 2022	Affirmation	BBB-/Stable

Ratings & Outlook

Issuer	BBB-/Negative
Senior unsecured debt	BBB-

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Related Methodologies/ Research

General Corporate Rating Methodology; October 2023

European Real Estate Rating Methodology; March 2024

ESG considerations for the credit ratings of real estate corporates; April 2021

Real Estate Outlook 2024, February 2024

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Bloomberg: RESP SCOP

Rating and rating-change drivers

Positive rating drivers	Negative rating drivers
• Medium-sized real estate company; size supports visibility on investment and letting markets across CEE and SEE • Portfolio well distributed across CEE and SEE, although this also entails exposure to more volatile economies • Strong profitability: Scope-adjusted EBITDA margin of around 75% driven by economies of scale • Capital recycling and deleveraging programme to address future funding needs • New strategy foresees investments in sectors with higher sustainable growth incl. hospitality, living sector and renewable energy	• Focus on second-tier investment markets • Relatively low WAULT leads to ongoing re-letting risk especially with tenant demand likely to change • Declining demand for office space and portfolio rents above market rents limit organic rental growth potential • Risk of increasing leverage with Scope-adjusted loan/value ratio expected to reach around 55% in the next 18-24 months • Scope-adjusted EBITDA interest cover anticipated to dip to below 2.2x when EUR 500m bond needs to be refinanced in 2026

Positive rating-change drivers	Negative rating-change drivers
• Continued adequate liquidity as perceived by us • Scope-adjusted loan/value ratio not increasing to around 55% • Scope-adjusted EBITDA interest cover of above 2.2x	• Further, perceived liquidity deterioration, i.e. if significant debt maturities in 2026 are not addressed well in advance. • Scope-adjusted loan/value ratio of around 55% • Scope-adjusted EBITDA interest coverage of less than 2.2x

Corporate profile

Globe Trade Centre (GTC) is a real estate investor and developer focusing on Poland and capital cities in Central and Eastern Europe. GTC actively manages the real estate portfolio of 46 commercial buildings providing 755,200 sq m of office and retail space. In addition, GTC has a development pipeline (under construction) of approx. 84,000 sq m office properties in capital cities of Central and Eastern Europe, most of it under construction. The company is listed on the Warsaw Stock Exchange, included in the mWIG40 index and is inward listed on the JSE.

Financial overview

				Scope estimates		
Scope credit ratios	**2022**	**2023**	**Q1 2024[1]**	**2024E**	**2025E**	**2026E**
Scope-adjusted EBITDA interest cover	3.7x	3.6x	3.5x	3.2x	2.8x	2.0x
Scope-adjusted debt/EBITDA	11.5x	11.2x	11.2x	12.4x	11.7x	11.4x
Scope-adjusted LTV ratio	46%	48%	48%	51%	53%	53%
Scope-adjusted EBITDA in EUR m						
EBITDA	101	103	105	105	116	121
Other items[2]	0	5	5	0	0	0
Scope-adjusted EBITDA	**101**	**107**	**110**	**105**	**116**	**121**
Funds from operations in EUR m						
Scope-adjusted EBITDA	101	107	110	105	116	121
less: (net) cash interest paid	-28	-30	-31	-33	-42	-60
less: cash tax paid per cash flow statement	-11	-7	-7	-8	-11	-9
Change in provisions	-1	-1	0	-1	-1	-1
Funds from operations	**62**	**69**	**71**	**63**	**63**	**51**
Net cash interest paid in EUR m						
Net cash interest per cash flow statement	-28	-30	-31	-33	-42	-60
Change in other items	0	0	0	0	0	0
Net cash interest paid	**-28**	**-30**	**-31**	**-33**	**-42**	**-60**
Scope-adjusted total assets in EUR m						
Total assets	2,670	2,657	2,740	2,669	2,664	2,689
less: guarantee deposits	-12	-13	-13	-13	-13	-13
less: cash and equivalents	-140	-120	-166	-104	-104	-91
less: derivatives (assets)	-25	-14	-13	-13	-13	-13
Scope-adjusted total assets	**2,493**	**2,509**	**2,547**	**2,539**	**2,533**	**2,572**
Scope-adjusted debt in EUR m						
Reported gross financial debt	1,280	1,318	1,384	1,389	1,445	1,455
add: derivatives	24	5	15	15	15	15
less: non-interest-bearing liabilities held for sale	0	0	0	0	0	0
less: available cash and cash equivalents	-140	-91	-153	-91	-91	-91
add: pension adjustments	0	0	0	0	0	0
Scope-adjusted debt (SaD)	**1,164**	**1,231**	**1,245**	**1,313**	**1,369**	**1,379**

[1] 12 months ending March 2024 for cash flow-related metrics
[2] Includes non-recurring items like severance payments

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Environmental, social and governance (ESG) profile[3]

Environment		Social		Governance	
Resource management (e.g. raw materials consumption, carbon emissions, fuel efficiency)		Labour management		Management and supervision (supervisory boards and key person risk)	
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)	
Product innovation (e.g. transition costs, substitution of products and services, green buildings, clean technology, renewables)		Clients and supply chain (geographical/product diversification)		Corporate structure (complexity)	
Physical risks (e.g. business/asset vulnerability, diversification)		Regulatory and reputational risks		Stakeholder management (shareholder payouts and respect for creditor interests)	

Legend
Green leaf (ESG factor: credit-positive)
Red leaf (ESG factor: credit-negative)
Grey leaf (ESG factor: credit-neutral)

Credit-neutral ESG profile

We believe GTC has pursued a transparent governance policy over the years. We base this belief on the quality and quantity of publicly available information as well as on future strategies.

88% of GTC's assets are LEED- or BREEAM-certified (as at end September 2022). The company committed itself to 10 UN Sustainable Development Goals and introduced a green bond framework in 2020. Funds issued under this framework are used to finance and refinance the acquisition, construction or refurbishment of buildings that meet recognised standards, such as BREEAM (very good and above) and LEED (gold and above). GTC has made a commitment that all its future investments will meet criteria for sustainable construction certificates and ensure tenant safety. We see all these initiatives as positive but not as impacting the company's credit profile.

[3] 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: BBB-

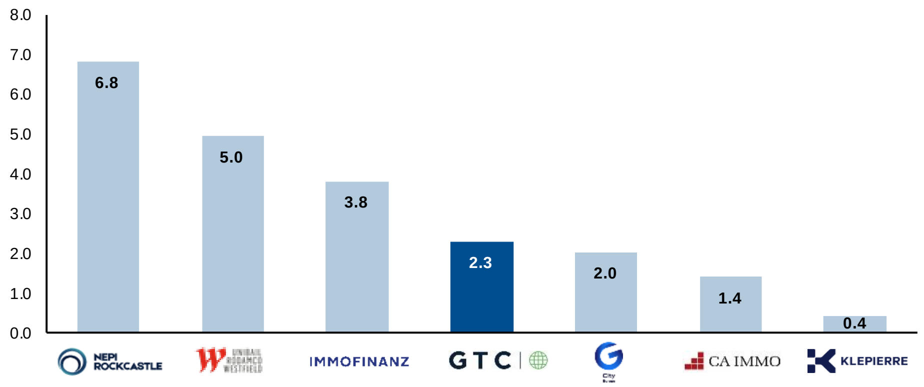
Industry risk profile: BB

GTC is a real estate investor and developer, so it is exposed to two sub-segments of the real estate sector: commercial buy-and-hold (industry risk of BB) and commercial development (industry risk B). We only consider its commercial exposure based on the relatively low share of development under construction (3% as at end-March 2024), which in turn is based on the company's gross asset value, including developments to be delivered and landbanks.

Medium size supports visibility on investment and letting markets across CEE and SEE

GTC is a medium-sized real estate company focused on CEE and SEE with Scope-adjusted total assets of EUR 2.6bn as at end-March 2024 (EUR 2.4bn in gross asset value) broadly unchanged from EUR 2.5bn in March 2023 as EUR 59m in negative fair value adjustments (12 months to end-March 2024) have been offset by further investments into the company's development pipeline including the completion of Matrix C in Q4 2023. The company is among the larger peers in the region and benefits from some visibility on capital markets (listed on the Warsaw Stock Exchange and inward listed on the Johannesburg Stock Exchange). Moderate visibility will support GTC's operations going forward as it provides access to external financing and thus the firepower to buy or develop revenue-generating assets. These, in turn, will support the company's strategy to expand its portfolio in Poland and in the capital cities of selected CEE and SEE countries.

Figure 1: GTC and competitors by gross asset value (EUR bn) in CEE as at YE 2023



Sources: Public information, Scope

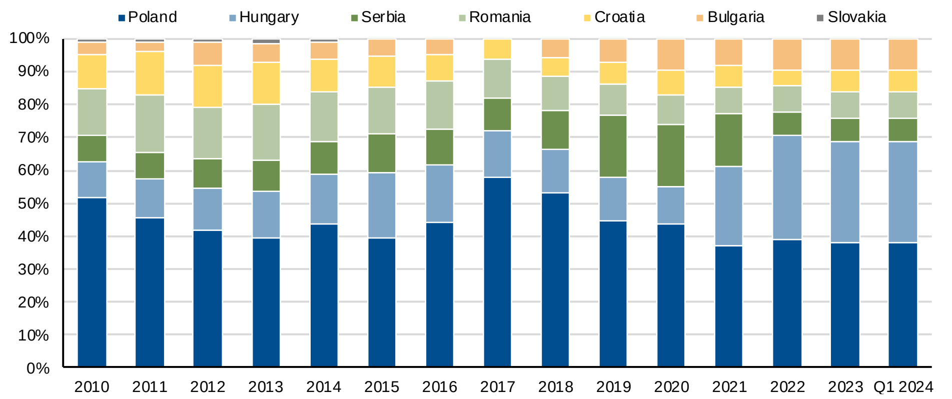
As at end-March 2024, GTC manages completed commercial properties with a combined gross leasable area of approximately 755,200 sq m, including 40 office buildings and 6 shopping malls. With its focus on capital cities in CEE and SEE, GTC benefits from decent visibility on these markets, especially as its portfolio predominately comprises relatively new properties (weighted economic age of eight years).

As at end-December 2023, GTC Hungary has a gross asset value of EUR 1.4bn (unchanged YoY) and operates a portfolio of 9 office properties with a gross leasable area of 199,000 sqm. We believe the market visibility of GTC Hungary will continue to improve going forward based on its focus on Budapest, namely the Váci Corridor – where it is one of the main players – and following execution on its development pipeline by 2025 (Center Point 3, 36,000 sq m, Andrassy, 3,600 sq m and Rose Hill Business Campus, 1,574 sq m). The first property 'The Pillar' was delivered in Q4 2021.

Portfolio distribution across CEE and SEE entails exposure to more volatile economies

GTC's portfolio is well distributed across CEE (69% of gross asset value – income producing assets – as at end-March 2024) and SEE (31%) with a focus on Poland (38%) the company's domestic market. Thus, performance will hinge on Poland's macroeconomic environment. Macroeconomic factors will drive consumer spending on, for instance, leisure and non-essential retail, affecting GTC's two shopping malls as well as tenant demand for its 16 office properties. The rest of the portfolio is distributed across five other countries: Hungary (31%), Bulgaria (10%), Romania (8%), Croatia (6%) and Serbia (7%). As such, GTC benefits from different demand patterns in the countries to which it is exposed. However, the volatility of economic development in GTC's markets is higher than in EU-28 markets (except Poland). On the one hand, these markets benefit from faster growing economies, outpacing more mature markets in Europe. On the other hand, they experience larger downswings e.g. during the global financial crisis. Nonetheless, GTC's relatively good foothold in the capital cities of SEE and CEE countries enables it to attract high-profile, blue-chip tenants.

Figure 2: Geographical distribution by gross asset value



Sources: GTC, Scope

New strategy foresees investments in sectors with higher sustainable growth

In August 2022, GTC signed an agreement to enter in a joint venture investment in Kildare Innovation Campus, an innovation hub located outside of Dublin. The site will be converted into a Life Science and Technology campus extended over 135,000 sqm lettable space. GTC acquired a minority stake of 25% through notes (debt instruments) issued by a Luxembourg securitisation vehicle. While the transaction reduced the geographical dependency from CEE and SEE, it was aimed also at diversifying customer segments and focus on high demand tenants. According to GTC, Dublin currently hosts 25% of technology and innovation centres in Europe, thus representing an attractive hub for companies seeking real estate spaces.

However, the stake in Kildare is likely to be sold and the capital recycled to invest in either new developments or acquisitions within the defined core asset classes of green office buildings, green shopping centres, residential for sale and rent (new), hospitality (new) and renewable energy (new). GTC is also looking to expand into the German (senior living) and UK markets, highly rated countries with some growth potential in the asset class focussed on.

However, these investments are subject to execution risk due to GTC's limited experience in these additional core asset classes and market.

Investment-grade tenants on average, but slightly reduced diversification

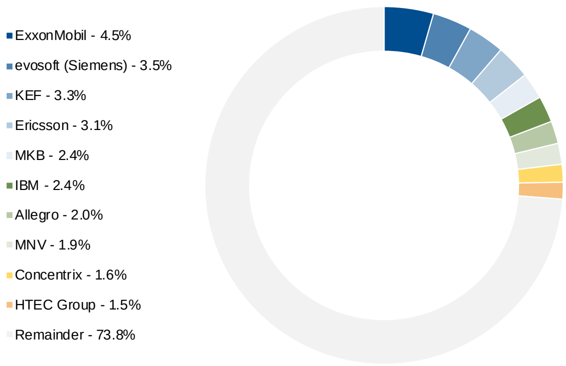
With its top three tenants accounting to 11% of total rent as at end-March 2024, diversification remained stable (unchanged compared to March 2023): top 10 tenants account to 26% of total rent (26% at end March 2023). We consider the diversification still adequate and don't see a risk of significant increase in concentration. Furthermore, tenants, including names as Ericsson, Exxon Mobil, IBM, have good credit quality (80% of the top 10 tenants and around one quarter of overall tenants are investment grade rated, blue-chip and government/supra-national tenants). This limits the impact of single tenant defaults on the company's cash flows, as illustrated by bad debt impairments of below 30bp of gross rental income for the last couple of years.

Change in tenant demand

GTC has significant exposure to retail tenants (35% of annualised in-place rent as at end-March 2024 / unchanged since June 2022) leaving cash flows vulnerable to the ongoing transformation of the European retail industry (see also Adapt or Disappear: E-commerce Transforms European Retail). However, the retail performance appeared to have recovered following the pandemic, as turnover in 2023 exceeded pre-covid levels and the occupancy rate is 96%, stable compared to March 2023. The footfall and tenant's turnover increased in GTC's malls in 2023 by 7.1% and 10.9%, respectively. Moreover, GTC benefits from exposure to CEE and SEE where online shopping habits grows at lower pace compared to western Europe and consumer purchasing power is forecast to remain resilient in 2024 thanks to a strong improvement in real disposable income since H2 2023.

The annualised rental income from the office segment improved to EUR 98m as at end-March 2024 from EUR 90m in March 2023. This is due to a high share of CPI-linked lease contracts, which have balanced the continuous decline in occupancy rate since its peak at 95% in 2019 and remained at 83% as at end-March 2024 (down 1 pp, YoY). In general, we also expect employers' behaviour to change as the biggest ever remote-working experiment – prompted by the Covid-19 pandemic – proves largely successful. Companies may consequently adjust their real estate needs downwards in the medium term. Having that said, we note that vacancy has increased in many of the CEE office markets, reflecting lower space requirements as many tenants switch to hybrid working, as well as some new supply, although construction activity has already declined in some of GTC's core markets.

Figure 3: Top tenants by net rental income as at March 2024



Sources: GTC, Scope

Occupancy is lowest in GTC's office properties in Poland (73% as at end-March 2024) and Romania (83%). The majority of vacancies are driven by properties in regional Polish cities with a high market vacancy, due to the strong "work from home" trend, or properties with small floor plates with imperfect structure and fitting. These weaknesses have been addressed by reorganization of GTC's office leasing department in Poland (2023) and Hungary (Q1 2024) as well as increased community management addressed at employees of tenants to encourage back to office policies of tenants. In some cases, GTC also provides more flexibility regards lease terms (length, incentives, local currencies) to support leasing activity. While we see these efforts to have been well chosen, to get a return for the least monetary expense it still needs to be seen whether these action bear fruit or some of GTC's assets do become stranded requiring big investments to convert and benefit from demand for other uses or to be sold at a discount to nowadays value.

Tenant concentration is much more pronounced for GTC Hungary, for which the top three tenants account for 38% of rental revenue as of March 2024. However, GTC Hungary's tenant portfolio is almost entirely of investment grade quality, sharply decreasing the likelihood of single tenant defaults. Furthermore, the company aims to reduce tenant concentration as evidenced by the strong weight of Hungarian developments within the company's pipeline under construction (100% of gross leasable area).

Development pipeline remains marginal in value

Following the cut by 50% in 2021, GTC has again accelerated its development activity in 2023 (GDV of EUR 337m as at end-March 2024 for projects under construction and ready to be launched in the next 24 months), although the value remains relatively low compared to the income producing assets value. The relatively low exposure to development activity (EUR 176m under construction) is considered positive, as it leaves the company less exposed to risk associated including cost overruns, delays in delivery as well as sufficient up letting to enable positive returns. We note current pre-letting rates of 48% based on estimated rental values. There are currently four office projects under development (including the large-scale refurbishment of the former ExxonMobil headquarters in Budapest).

The under-construction pipeline includes Center Point 3, a 36,000 sqm office property, as well as Rose Hill Business Campus and Andrassy, all in Budapest. In addition, Centre Point 1 & 2, a 42,500 sqm office property in Budapest, is under renovation that is expected to be completed in Q4 2024.

Among the projects ready to be launched, the largest project is Napred - Phase 1, Belgrade (24,900 sqm office space) with a total development cost of EUR 69m expected to be delivered beyond 2026. Furthermore, GTC added to the pipeline two residential projects, (8,600 sq m) in Budapest (total development cost EUR 50m). The new residential project introduces a degree of diversification which we see as positive, as residential developments meet increasing demand in CEE for higher quality living and is less exposed to economic downturn and substitution risk (homebuilders address a basic human need).

However, GTC highlighted that further execution on the company's development pipeline is subject to high pre-letting rates (above 30%) that allow for built-to-suit projects, thus limiting associated development risk.

Focus on second-tier investment markets

GTC's properties are predominately located in second and third-tier investment markets, excluding Warsaw (12% of GLA as at end-March 2024), which is considered first tier. Even if the capital city markets (Zagreb, Sofia, Budapest, Bucharest, Belgrade) have gained more momentum over the last few years, investment volume has not reached EUR 1bn for most of them (excluding Budapest where annual investment hit EUR 1.7bn in 2019). Thus, the liquidity of GTC's portfolio is relatively limited. In the current scenario of prevailing higher interest rates, 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 (excluding Warsaw), an increase in leverage, the reduced availability of external financing, and limited recovery expectations for debt investors. For the time being, however, GTC benefits from predominantly euro-denominated leases on a comparably young portfolio (economic age of 8 years at end-March 2024) trading at a yield of 7.5% on its annualised gross rental income (estimated at 6.8% on net rental income), which represents a premium for limited market liquidity and protects values to some extent. However, the greatest threat to GTC's portfolio values is related to the limited rental growth expectations due to (i) the significantly lower ERVs, which are 6.4% below GTC's gross rental income as at end-March 2024, (ii) the limited visibility of achieving improved occupancy for the office portfolio in the short term, and (iii) the threat of declining demand for the retail portfolio in the medium to long term.

GTC shows a weakening but still adequate tenant demand with an occupancy rate of 83% in March 2024 (down 1pp YoY) for the office segment and 96% (unchanged YoY) for the retail segment. The office segment has suffered from declining occupancy especially for the aged share of the portfolio (economic age of at least 10 years) and its partial exposure to Polish regional cities (21% of GAV as at end-March 2024) as well as the ongoing refurbishment of Center Point 1 & 2. We expect this trend to continue given the completed (Matrix A and B and Forrest Office Debrecen) and planned sales of higher quality properties with above-average occupancy rates of 95-100% and the lack of demand for some properties due to their location or structure.

While the retail segment has shown to be resilient with strong recovery in uptake, sales and footfall after restrictions during the Covid-19 pandemic have been lifted and despite the current macroeconomic environment, pressure will increase on the office segment given the growing trend of hybrid work which might lead companies to reduce their office space.

Relatively low WAULT leads to ongoing re-letting risk

Nonetheless, risk regarding future occupancy levels is amplified by the relatively short WAULT of 3.4 years as at end-March 2024, which exposes GTC to ongoing re-letting risk, especially in light of muted demand as expressed by portfolio ERV being about 6% below actual market rents. Going forward we expect GTC to be in need to increase spendings on the aged share of the portfolio to be able to successfully re-let vacant space but see the majority of GTC's portfolio relatively well protected thanks to supporting features including properties that have been either: i) recently built (economic age of around eight years) and are mostly located in the central business district (offices) or ii) benefitting from relatively little competition (retail, excluding Warsaw) and mostly located in residential areas.

Strong profitability with Scope-adjusted EBITDA margin of around 75%

Profitability has improved greatly, with the discontinuation of residential development activity (finalised in 2018) leading to a Scope-adjusted EBITDA margin above 75% since 2016 (last twelve months to end-March 2024: 78%; down 4pp YoY). After a strong increase in profitability to close to 90% in between 2019 to 2021 was driven by cost optimisation measures also in response to Covid-19 lockdowns, including a reduction in non-critical operating expenses and a decrease in provisions for share-based payments. The sharp reduction in operating expenditures was less pronounced in 2022, with the Scope-adjusted EBITDA margin normalising closer to 80% and further declining in 2023 to around 78% - a level we view as sustainable. However, decreasing occupancy combined with inflation-driven increases in property operating expenses will put further pressure on profitability which will be partially mitigated by the company's efforts to cut SG&A expenses.

Financial risk profile: BB+

Below-par discretionary cash flow

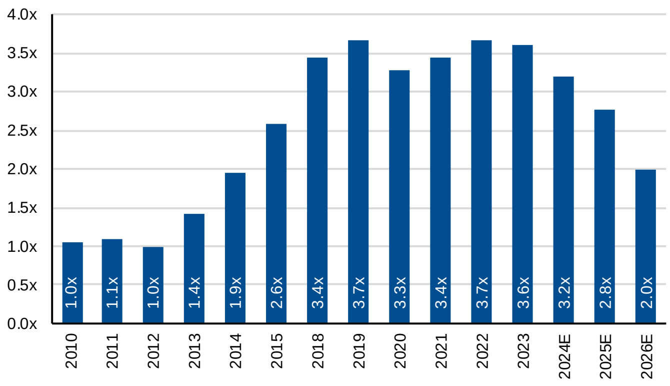
Cash flow from operations has followed a positive trend since 2016. Improvements have been driven by: i) the end of residential development activity in 2018; and ii) portfolio growth achieved via execution on the company's commercial development pipeline (develop-to-hold) and property acquisitions. The former has led to negative FOCF between 2016 and 2021, which was financed externally pushing Scope-adjusted debt to EUR 1,404m as at YE 2021. Acquisitions have been mainly financed by capital recycling or equity issuances which we expect to remain main financing sources going forward.

Capital expenditure of EUR 237m in between 2024 and 2026 are not expected to be covered by operational cash flow limiting room to deleverage to compensate for pressure on achievable rent levels, rising interest rates and yield widening. Deleveraging capacity is further constrained by the fact that dividend payments are expected to continue at the lower of EUR 30m per annum or 50% of funds from operations, resulting in negative discretionary cash flow in the coming years. Therefore, any deleveraging will depend on the successful implementation of the company's deleveraging plan, which consists of asset sales with net proceeds of approximately EUR 400m over the next 24 months (EUR 12m signed to date). Exit proceeds will be used in priority to (i) deleverage and (ii) execute the company's development/acquisition pipeline.

We acknowledge that further execution of the company's development pipeline is subject to high pre-letting rates of at least 30%, enabling build-to-suit projects and thus limiting the associated development risk. However, we note that the company is seeking external funding to either fund construction up to a level of 70% loan/cost or to release capital for delivered developments up to a level of 50% loan/value. We expect the corresponding increase in Scope-adjusted debt to be well offset by the additional earnings contribution from delivered developments.

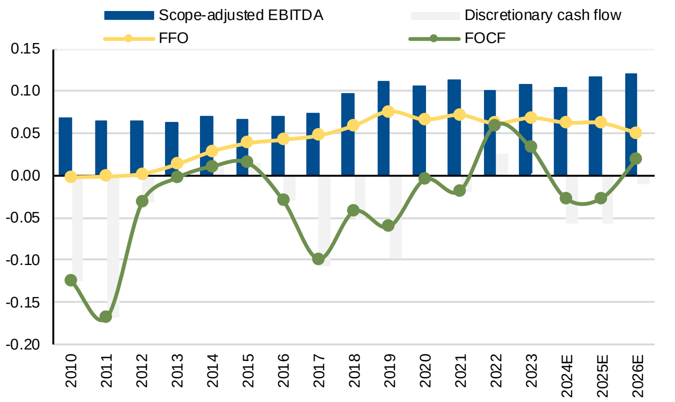
We see the benefit of the company's ESG focus with a portfolio that had a carbon intensity of 24.9 kg CO_2e/sqm at the end of 2022, which is reasonably good and minimises the investment required to become carbon neutral by 2050 in line with EU targets. However, part of the office portfolio is facing weak tenant demand, which will either lead to significant investment needs or to write-downs, which are not part of our rating scenario but are qualitatively captured in the leverage assessment.

Figure 4: Scope-adjusted EBITDA interest cover (x)



Sources: GTC, Scope estimates

Figure 5: Cash flows (EUR bn)



Sources: GTC, Scope estimates

Scope-adjusted EBITDA interest cover anticipated to dip to below 2.2x when EUR 500m bond needs to be refinanced in 2026

Scope-adjusted EBITDA interest cover has been above 3x since 2018 (3.5x in the last 12 months ending March 2024). This is due to a low weighted average cost of debt (2.58% as at end-March 2024). We do not expect GTC will be significantly impacted by changing interest rate environment in the short term as the company has 100% of debt fixed or hedged.

However, new debt will bear notably higher interest rates and shares of debt show caps that allow the pass through of a significant share of rate increases that happened since Q1 2022. Thus, we expect the weighted average cost of debt to increase to close to 3% by YE 2024 and around 4% by YE 2026.

As a result, we forecast a decline in Scope-adjusted EBITDA interest cover to between 2.0 and 2.5x in 2026, when EUR 770m of debt (including the EUR 500m bond) will need to be refinanced at significantly higher borrowing costs. Rising financing costs are only partially offset by existing interest rate hedges and expected rental growth given the challenging economic environment as well as the limited demand for some of GTC’s office portfolio.

Rising leverage due to rising yields and negative discretionary cash flow

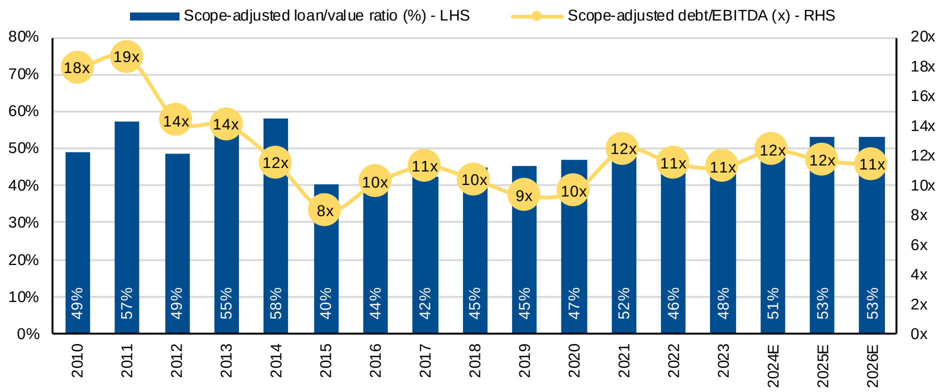
GTC's leverage, measured by the Scope-adjusted loan/value has ranged between 45% and 50% since 2016 (following the successful debt restructuring in 2015), with a peak in 2021 to 52%. At end-March 2024 the ratio stood at 48%. We expect the loan/value ratio to rise above 50% and approach 55% in the coming years. Our view is driven by:

- additional pressure on Scope-adjusted total assets, with further, but limited, yield widening not offset by rental growth as portfolio rents will slowly return to lower market rents (ERVs[4]), driven by around 15% of leases coming up for renewal each year, and limited visibility on incremental rental income from developments under construction, coupled with relatively weak pre-letting; and
- an increase in Scope-adjusted debt of around EUR 150-175m over the next three years, given continued negative discretionary cash flow.

Pressure on leverage could also unfold because of delays in projects' execution and a consequent extension of the funding period; however, as the development activity is expected to remain marginal, we do not anticipate the Scope-adjusted loan/value ratio to increase substantially above 55%.

Still the company's strategy is to maintain the level of leverage or even reduce it, given the current unfavourable cost of funding, and to fund the future expansion through own liquidity and capital recycling. Maintaining leverage below 50% could be achieved if GTC successfully implements its deleveraging plan. While we acknowledge the clear deleveraging path to which the company has committed, it remains subject to execution risk and is therefore not reflected in the rating case.

Figure 6: Leverage



Sources: GTC, Scope estimates

Cash flows from commercial real estate are partially linked to changes in general demand. Therefore, our financial risk assessment of companies active in this segment also includes leverage, as measured by Scope-adjusted debt/EBITDA, which provides good visibility on leverage independent of changes in market value driven by shifts in capitalisation rates. As such, we view positively GTC's past ability to keep Scope-adjusted debt/EBITDA stable at around 11x, which indicates that the fair value growth of its properties in the past was well balanced between yield compression and rent increases. Furthermore, it provides confidence that the company can absorb increased funding costs with a debt yield of around 10%.

Adequate liquidity

Liquidity is considered adequate but close to being stretched. While short-term debt maturities are fully covered by cash sources, a longer-term view shows the company's

[4] around 6% lower at end-March 2024

reliance on external financing, with debt maturities in the 24 months to end-March 2026 (EUR 212m) and a negative FOCF forecast for the same period of EUR 61m, which is not expected to be fully covered by cash sources, including available cash and cash in construction escrow accounts of EUR 166m (as at end-March 2024). Liquidity is further constrained by around EUR 680m of debt repayments due in Q2 2026, including a EUR 500m bond. Thus, even if we see some likelihood that GTC will be able to cover its EUR 500m in unsecured debt maturities until the end of 2026 with existing cash and by using its secured lending headroom[5], it will only be able to do so by a narrow margin. These 2026 debt maturities could have a significant impact on GTC's liquidity profile if the company does not manage to address the related funding requirements - through asset sales and/or new (bank) debt - well in advance, in line with its refinancing plan. We will closely monitor the implementation of this plan to assess whether the liquidity risk is well managed or whether further rating pressure will arise.

Balance in EUR mEUR m	2023	2024E	2025E
Unrestricted cash (t-1)	140	110[6]	91
Open committed credit lines (t-1)	94	0	0
FOCF	33	-27	-27
Short-term debt (t-1)	48	45	133
Coverage	**>200%**	**184%**	**48%**

Financial covenants are the following (as at Q1 2024):

- Adj. EBITDA/ net cash interest ≥ 1.5x (3.3x)
- Unencumbered assets/ unsecured financial debt ≥ 125% (181%)
- Net financial debt/ total assets ≤ 60% (50%)
- Secured financial debt/ total assets ≤ 40% (25%)
- DSCR covenants on individual bank loans at different levels

All of these covenants have been complied with ample headroom.

A breach of any covenant would constitute an Event of Default if such breach continues for 30 days, the Fiscal Agent may, if so requested in writing by the holders of not less than 25% in aggregate principal amount of the Notes then outstanding, give notice in writing to the relevant Issuer and the Guarantor that each Note is declared due and payable, whereupon such Note shall immediately become due and payable at their principal amount together (if applicable) with accrued interest without further action or formality.

Supplementary rating drivers: +/- 0 notches

Financial policy: neutral

The company follows no publicly communicated financial policy except a strategic LTV target of below 50%.

Issuer rating for GTC Hungary Zrt.

The issuer rating for GTC Real Estate Development Hungary Zrt. is driven by the issuer rating of its parent, Globe Trade Centre S.A., based on our assessment of a strong link between GTC S.A. and GTC Hungary Pltd. Our view is supported by the following:

[5] Secured lending headroom represents the headroom a company has to issue asset-backed/secured loans against its unencumbered asset base. This headroom may be subject to financial covenants, including a maximum secured loan/value ratio and/or a minimum unsecured asset ratio. In general, we believe that asset-backed/secured financing is possible up to a maximum loan/value ratio of 60%.
[6] Includes EUR 19m of cash on escrow accounts for development projects under construction.

- Explicit guarantee: The senior unsecured bonds as well as all future debt (excluding non-recourse secured bank debt) of GTC Real Estate Development Hungary Zrt. (GTC Hungary Pltd.) is irrevocably and unconditionally guaranteed by GTC S.A.
- Majority owner: As of today, GTC holds 100% of GTC Hungary Pltd.
- Name equality: GTC Hungary is clearly identifiable as part of GTC S.A.
- Strategic importance: GTC Hungary forms part of GTC Group and represents group operations in Hungary. There is no intention to change the group's structure in the medium term.
- Centralised treasury: GTC S.A. is expected to continue to finance GTC Hungary Pltd.'s operations (excluding non-recourse bank loans for property SPVs) via intercompany loans under GTC's centralised treasury, which handles the group's financing.
- Strong integration in GTC S.A.: GTC Hungary Pltd. is strongly integrated in GTC's operations, with all decisions approved and made by the management board of GTC S.A. (note: the management board of GTC Hungary Pltd. is comprised of two members of GTC S.A.'s board).

Long-term debt ratings

Senior unsecured debt rating: BBB-

GTC has EUR 653m in capital market debt outstanding as at end-March 2024. All issuances are irrevocably and unconditionally guaranteed by Globe Trade Centre S.A.

The issuer's unencumbered asset ratio stands at above 200% as at end-March 2024 providing sufficient collateral to bondholders, thus, justifying the senior unsecured debt rating of BBB-.

Appendix: Peer comparison

	Globe Trade Centre S.A.	Fastpartner AB	Inmobiliaria Colonial SOCIMI S.A.	Norwegian Property ASA	Corem Property Group AB
	BBB-/Negative	BB/Negative	--/--*	BBB-/Negative	BBB-/Negative
Last reporting date	31 Mar 2024	30 Jun 2023	31 Dec 2023	30 Dec 2023	30 Sep 2023
Business risk profile					
Scope-adjusted total assets (EUR m)	2,560	3,100	13,310	2,500	6,400
Portfolio yield (NIY)	6.8%	6.2%	2.7%	na	6.7%
Gross lettable area (‘000s sq m)	755	1,563	1,688	619	2.602
Number of residential units	na	na	na	na	na
Countries active in	6	1	2	1	3
Top three tenants (%)	11%	9%	10%	34%	10%
Top 10 tenants (%)	26%	19%	26%	49%	17%
Office (share net rental income)	65%	46%	93%	69%	49%
Retail (share NRI)	35%	12%	6%	7%	9%
Residential (share NRI)	0%	0%	0%	0%	0%
Hotel (share NRI)	0%	4%	0%	0%	0%
Logistics (share NRI)	0%	24%	0%	5%	25%
Others (share NRI)	0%	14%	1%	18%	16%
Property location	Mainly 'B'	‘A’ and ‘B’	Mainly ‘A’	Mainly 'A'	‘A’ and 'B'
EPRA occupancy rate (%)	86%	93%	97%	94%	89%
WAULT (years)	3.4	4.5	5.0	6.0	3.6
Tenant sales growth (%)	na	na	na	na	na
Like-for-like growth rents (%)	7.0%	13.0%	7.0%	na	na
Occupancy cost ratio (%)	na	na	na	na	na
Scope-adjusted EBITDA margin	78%	68%	77%	90%	70%
EPRA cost ratio (incl. vacancy)	na	na	21.9%	na	na
EPRA cost ratio (excl. vacancy)	na	na	20.1%	na	na
Financial risk profile					
Scope-adjusted EBITDA interest cover	3.5x	1.9x	3.1x	2.6x	2.0x
Scope-adjusted LTV ratio	48%	48%	38%	53%	55%
Scope-adjusted debt/EBITDA	11.2x	12.0x	17.9x	13.7x	14.6x
Weighted average cost of debt	2.6%	4.5%	1.7%	4.4%	4.6%
Unencumbered asset ratio	>200%	>200%	>200%	na	na
Weighted average maturity (years)	3.6	3.4	na	2.8	na

* Subscription ratings available on ScopeOne

Sources: Public information, Scope

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