S&P Global
Ratings

Research

Tear Sheet:

Vonovia SE

September 5, 2023

Vonovia's rent growth should remain solid, partly offsetting poor performance in its other segments. The company reported 3.5% like-for-like growth in rental income for first-half 2023 (3.3% in 2022), at the high end of our conservative 2.5%-3.5% assumption for 2023-2024, thanks to strong uplifts in rent renewals, slowly growing indexation, stable and low vacancy rates (2.2%), and a record high collection rate (99.9%) despite inflation biting German households' purchasing power. Still, the company's ability to capture rental growth is limited by lower investments in modernization (which would otherwise allow it to increase rents beyond indexation levels) and very low tenant churn (less than 8% as of June 30, 2023).

As we expected, Vonovia's other segments--value-add, development, and recurring sales--were materially depressed in the first half of 2023 given the fall in market transactions amid increased interest rates. We do not expect a strong recovery before 2024, though these segments' contribution to EBITDA is moderate (10.5% in first-half 2023, 21% in first-half 2022).

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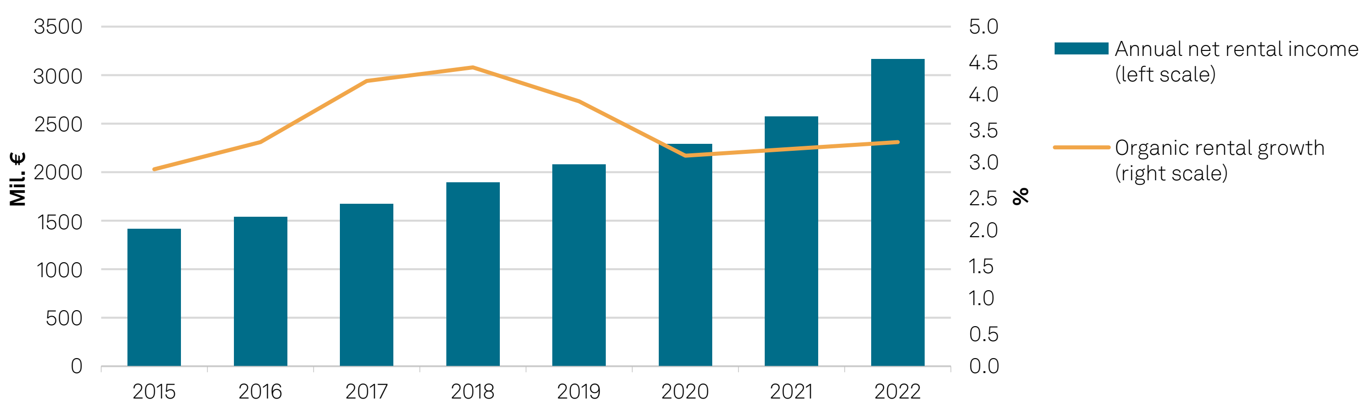
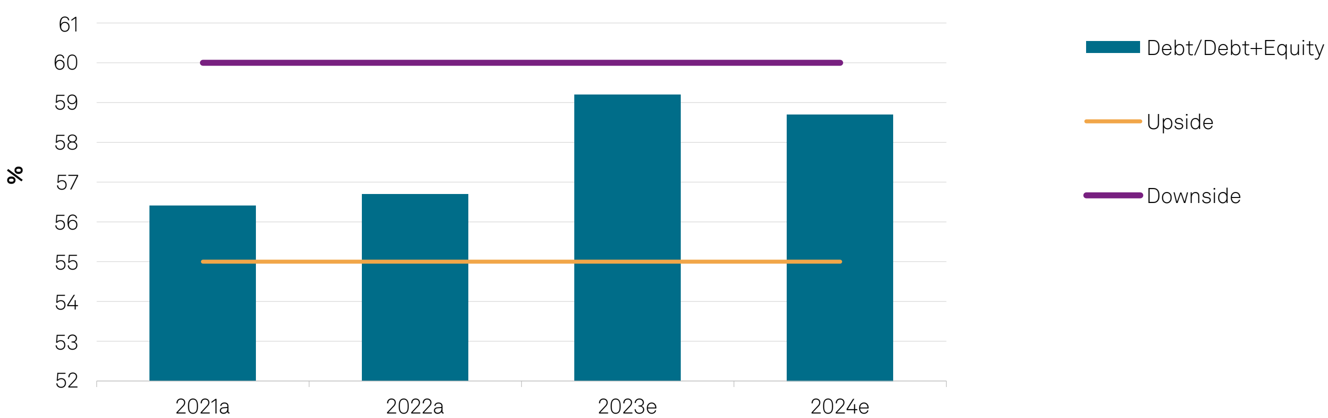
Vonovia SE's Annual Rental Income And Like-For-Like Annual Rental Growth



Source: S&P Global Ratings and company reports.

Devaluation is weighing on Vonovia's high debt to debt plus equity ratio, while disposals and lower dividends should keep it below our rating downside threshold. The ratio increased to 58.8% as of June 30, 2023 (47.2% on a reported basis), from 56.7% on Dec. 31, 2022, due to a 6.6% portfolio devaluation in first-half 2023 (following a 3.4% decline in second-half 2022), partly offset by the €1 billion sale of its stake in Südewo. We expect the proceeds of the assets disposed to CBRE (€560 million) and the €1 billion recent bond buy-back at 11% discount to ease the ratio in second-half 2023, absent devaluation. While Vonovia and some market research recently reported early signs of value stabilization, we conservatively assume a further 3%-4% downward valuation leading to a 13% peak-to-through decline and lower-than-expected asset disposals, despite the company's strong commitment to reducing debt by selling properties. On that basis, we think debt to debt plus equity should remain 58%-59% through to 2025.

Vonovia SE's Outlook Threshold For Adjusted Ratio Of Debt To Debt Plus Equity

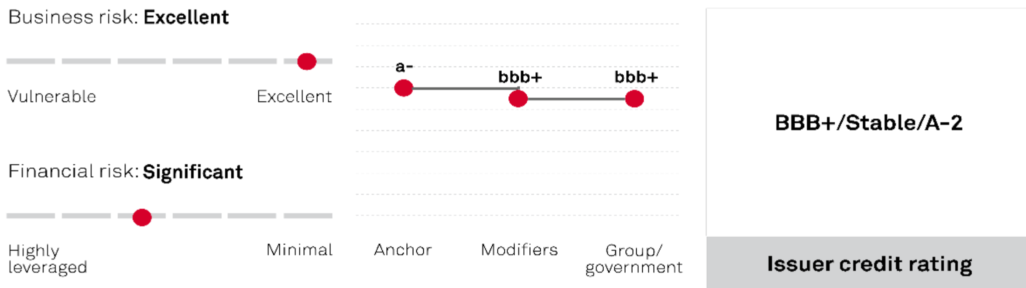


a--Actual. e--Estimate. Source: S&P Global Ratings.

S&P Global Ratings-adjusted interest coverage has weakened closer to 3x as refinancing has become more expensive, though deleveraging, rental growth, and cheaper bank lending have softened the impact of higher rates. Amid more-expensive debt refinancing, Vonovia's EBITDA interest coverage (excluding revenue from recurring sales and developments) declined to 3.1x in first-half 2023 on an RTM basis, from 3.7x in 2022. By repaying bond maturities (€1.5 billion-€2 billion per fiscal year; €3.2 billion in 2025) with proceeds from asset disposals and free cash flows, Vonovia will likely lessen the impact from higher rates. Although the company is refinancing or extending its bank loans at terms that are currently more attractive than bond yields, we assume a conservative 5.50% coupon on all refinancings. We therefore forecast EBITDA interest coverage (excluding revenue from recurring sales and developments) to remain around 3.0x in 2023-2024 and 2.5x-3.0x in 2025, well above our 1.8x downside rating threshold.

Vonovia should preserve an adequate liquidity cushion thanks to well staggered debt maturities, flexibility regarding dividends and capex, high disposal targets, and relatively good access to debt funding. Vonovia's short-term debt maturities (€3.7 billion in the 12 months from June 30, 2023) are staggered and moderate in relation to the company's size (€88.2 billion). Total refinancing needs for the next 12 months are €4.6 billion if we include the early repayment of €900 million bonds maturing after June 30, 2024. This is more than covered by about €7.4 billion of short-term liquidity sources, comprising €3.7 billion of undrawn bank lines (out of which €3.0 billion RCF likely to be extended by two years), €1.5 billion cash position, €560 million expected cash proceeds from the CBRE transaction, and our expectation of €1.6 billion funds from operations.

Ratings Score Snapshot



Recent Research

- Industry top trends Midyear Update: Real Estate (REITs), Refinancing risks increase, asset corrections materialize, July 18, 2023
- European REITs The Great Repricing Continues, July 18, 2023
- Vonovia SE's €1 Billion Stake Sale Will Cushion Credit Ratios And Fuel Liquidity, April 28, 2023
- Credit FAQ: Spotlight On Refinancing Risks In European Commercial Real Estate, April 24, 2023
- Rising Rents, Stable Leverage, And Dividend Cut Support Vonovia's Credit Profile, March 21, 2023
- German Residential REITs Face A Mixed Outlook In 2023, Feb. 20, 2023

Company Description

Vonovia is the leading listed residential real estate holding company in Germany, and largest listed real estate landlord by portfolio size in Europe. Its portfolio was worth about €88.2 billion as of June 30, 2023. At the same date, the company owned about 548,080 residential units in Germany, Austria, and Sweden and managed about another 71,200 units for third parties.

The company is listed on the German stock index (DAX) with an average market cap of about €16.4 billion on Aug. 4, 2023. The largest shareholders are Norges Bank (14.6%), BlackRock (6.9%), APG (4%), and DWS Investments (3%), with 71.5% in free float.

Outlook

The stable outlook on Vonovia reflects our view that group will continue generating robust rental growth, supported by the undersupply of housing in Germany, increasing rent indexation, and low tenant defaults. This should enable the group's EBITDA interest coverage and debt to debt plus equity to remain above 1.8x and below 60%, respectively, for at least the next two years.

We expect Vonovia to preserve a sound liquidity cushion and adjust its capital-allocation strategy to fast-evolving financial market conditions. We also assume that management will take the necessary steps to decrease leverage and comply with its publicly stated financial policy, centered on a maximum reported LTV of 45% (comparable to S&P Global Ratings-adjusted debt to debt plus equity of 55%).

Downside scenario

We could consider a negative rating action if:

- Debt to debt plus equity increases to 60% or above for a prolonged period, because of higher revaluation losses or lower asset sales than expected;
- The liquidity cushion significantly decreases, for example because of a late refinancing of upcoming maturities or the issuance of debt with shorter maturities;
- EBITDA to interest moves toward 1.8x; or
- Outstanding secured debt exceeds 40% of the company's asset value, which may lead us to notching down our ratings on its unsecured debt.

Upside scenario

We could raise our ratings by one notch if:

- The group is able to dispose substantial assets or development projects or raise enough equity such that its debt to debt plus equity would sustainably stay below 55% while maintaining EBITDA interest coverage at 3x or above; and
- Vonovia increases its payback capacity via internal cash flow generation, so that its debt-to-EBITDA ratio (excluding revenue from sales) sustainably returns to historical levels (mid-teens or below).

Key Metrics

Vonovia SE--Forecast summary

Period ending	Dec-31-2019	Dec-31-2020	Dec-31-2021	Dec-31-2022	Dec-31-2023	Dec-31-2024	Dec-31-2025
(Mil. EUR)	2019a	2020a	2021a	2022a	2023e	2024f	2025f
Revenue	2,148	2,366	2,731	3,595	3,726	3,777	3,835
EBITDA	1,422	1,614	1,850	2,274	2,422	2,455	2,531
Funds from operations (FFO)	1,057	1,096	1,315	1,542	1,716	1,671	1,436
Interest expense	406	444	490	609	713	791	964
Cash flow from operations (CFO)	1,150	999	1,394	1,574	1,686	1,657	1,435
Capital expenditure (capex)	1,662	1,614	1,731	1,855	998	998	1,048
Cash Dividends	442	531	1,516	714	343	585	1,005
Debt	24,784	25,706	47,186	45,179	42,206	40,158	39,804
Equity	20,570	23,832	36,545	34,439	29,037	28,222	27,966
Adjusted ratios							
EBITDA margin (%)	66.2	68.2	67.8	63.3	65.0	65.0	66.0

Vonovia SE--Forecast summary

EBITDA interest coverage (x)	3.5	3.6	3.8	3.7	3.4	3.1	2.6
Debt/EBITDA (x)	17.4	15.9	25.5	19.9	17.4	16.4	15.7
Debt/debt and equity (%)	54.6	51.9	56.4	56.7	59.2	58.7	58.7

EFinancial Summary

Vonovia SE--Financial Summary

Period ending	Mar-31-2022	Jun-30-2022	Sep-30-2022	Dec-31-2022	Mar-31-2023	Jun-30-2023
Reporting period	RTM	RTM	RTM	RTM	RTM	RTM
Display currency (mil.)	EUR	EUR	EUR	EUR	EUR	EUR
Revenues	3,010	3,497	3,926	3,595	3,634	3,455
EBITDA	2,022	2,265	2,364	2,274	2,248	2,190
Funds from operations (FFO)	1,483	1,578	1,621	1,542	1,484	1,436
Interest expense	502	493	532	609	664	699
Operating cash flow (OCF)	1,569	1,642	1,731	1,574	1,583	1,392
Capital expenditure	1,898	1,901	2,248	1,855	1,667	1,569
Dividends paid	1,526	1,723	1,726	714	714	415
Cash and short-term investments	3,451	1,495	1,245	1,198	1,195	1,572
Debt	45,070	45,656	45,859	45,179	44,897	44,224
Common equity	36,490	37,523	37,425	34,439	32,254	30,953
Valuation of investment property	95,436	98,265	98,664	94,527	89,111	85,683
Adjusted ratios						
EBITDA margin (%)	67.2	64.8	60.2	63.3	61.9	63.4
EBITDA interest coverage (x)	4.0	4.6	4.4	3.7	3.4	3.1
Debt/EBITDA (x)	22.3	20.2	19.4	19.9	20.0	20.2
Debt/debt and equity (%)	55.3	54.9	55.1	56.7	58.2	58.8

Peer Comparison

Vonovia SE--Peer Comparisons

	Vonovia SE	Vesteda Residential Fund FGR	Deutsche Wohnen SE	Grand City Properties S.A.	Heimstaden Bostad AB
Foreign currency issuer credit rating	BBB+/Stable/A-2	A-/Stable/A-2	BBB+/Stable/A-2	BBB+/Negative/A-2	BBB/Negative/--

Vonovia SE--Peer Comparisons

Local currency issuer credit rating	BBB+/Stable/A-2	A-/Stable/A-2	BBB+/Stable/A-2	BBB+/Negative/A-2	BBB/Negative/--
Period	RTM	RTM	RTM	RTM	Annual
Period ending	2023-06-30	2023-06-30	2023-06-30	2023-06-30	2022-12-31
Revenue	3,455	1,089	620	1,374	1,249
EBITDA	2,190	668	316	845	729
Funds from operations (FFO)	1,436	460	217	434	444
Interest expense	699	187	72	393	275.5
Operating cash flow (OCF)	1,392	390	158	332	415
Capital expenditure	1,569	746	77	775	859
Dividends paid	415	23	46	382	333
Cash and short-term investments	1,572	218	709	700	842
Debt	44,224	8,520	3,824	16,841	16,775
Equity	30,953	15,361	4,793	12,937	15,142
Valuation of investment property	85,683	25,986	8,990	28,887	30,955
Adjusted Ratios					
EBITDA margin (%)	63.4	61.4	50.9	61.5	58.4
EBITDA interest coverage (x)	3.1	3.6	4.4	2.2	2.6
Debt/EBITDA (x)	20.2	12.8	12.1	19.9	23.0
Debt/debt and equity (%)	58.8	35.7	44.4	56.6	52.6

Environmental, Social, And Governance

ESG factors are a neutral consideration in our credit rating analysis of Vonovia. We consider Vonovia's exposure to social and environmental factors as on par with the German residential industry. That said, social and political debates on rent affordability in Germany's metropolitan areas may increase regulation and reputation risk for the largest German residential real estate company. Vonovia, together with its peers, has become a target for social protests, blaming the company for rising rents in German metropolitan cities as well as non-transparent utility costs (Vonovia in particular) charged to tenants. We believe additional rent regulation could hinder like-for-like rental growth for Vonovia. We note that the company refurbishes and renovates approximately 3%-4% of its portfolio per year to meet latest standards in terms of thermal insulation and energy efficiency. We note the German government's published climate package, which targets reducing carbon dioxide emissions for buildings by 66% (compared to 1990) by 2030.

Rating Component Scores

Foreign currency issuer credit rating	BBB+/Stable/A-2
Local currency issuer credit rating	BBB+/Stable/A-2
Business risk	Excellent
Country risk	Very Low
Industry risk	Low
Competitive position	Excellent
Financial risk	Significant
Cash flow/leverage	Significant
Anchor	a-
Diversification/portfolio effect	Neutral (no impact)
Capital structure	Neutral (no impact)
Financial policy	Neutral (no impact)
Liquidity	Adequate (no impact)
Management and governance	Satisfactory (no impact)
Comparable rating analysis	Negative (-1 notch)
Stand-alone credit profile	bbb+

Related Criteria

- General Criteria: Hybrid Capital: Methodology And Assumptions, March 2, 2022
- General Criteria: Environmental, Social, And Governance Principles In Credit Ratings, Oct. 10, 2021
- General Criteria: Group Rating Methodology, July 1, 2019
- Criteria | Corporates | General: Corporate Methodology: Ratios And Adjustments, April 1, 2019
- General Criteria: Methodology For Linking Long-Term And Short-Term Ratings, April 7, 2017
- Criteria | Corporates | General: Methodology And Assumptions: Liquidity Descriptors For Global Corporate Issuers, Dec. 16, 2014
- Criteria | Corporates | General: Corporate Methodology, Nov. 19, 2013
- General Criteria: Country Risk Assessment Methodology And Assumptions, Nov. 19, 2013
- General Criteria: Methodology: Industry Risk, Nov. 19, 2013
- General Criteria: Methodology: Management And Governance Credit Factors For Corporate Entities, Nov. 13, 2012
- General Criteria: Principles Of Credit Ratings, Feb. 16, 2011