Research Update:

Logistics Company P3 Group S.a.r.l. Assigned 'BBB' Rating; Outlook Stable

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Rating Action Overview

- Luxembourg-registered P3 Group S.a.r.l. (P3) is the third-largest rated logistics property company in Continental Europe, with a gross asset value of about €6.7 billion as of June 30, 2021. The company owns and manages high-quality logistics assets across 11 European countries.
- P3 intends to diversify its capital structure with capital market instruments and it has issued €1.0 billion of senior unsecured bonds. We understand that the proceeds would be largely used to repay existing unsecured bank term loans.
- We assigned our 'BBB' long-term issuer credit rating to P3 and our 'BBB' issue rating to its senior unsecured notes.
- The stable outlook reflects our view of the company's good asset quality and high geographic diversity, which will likely enable it to continue generating stable and predictable income. Our base-case scenario also factors in P3's continuing expansion of its portfolio while maintaining financial discipline in line with our current ratings.

Rating Action Rationale

P3 is the third-largest rated logistics property company in Continental Europe, with a gross asset value of about €6.7 billion as of June 30, 2021, and plans to grow the portfolio considerably by 2023. The company's strategy is to acquire modern logistics assets in its key markets, with a focus on Western European cities, and to expand its portfolio to about €9.0 billion over the next two years. The company's portfolio mainly comprises relatively large assets--about 93% of the total portfolio is larger than 10,000 square meters (sq. m.), with an average age of about 11 years. We believe that P3's asset type and quality compare well with the logistics assets of other rated players in Europe, such as Blackstone Property Partners Europe Holdings S.a.r.l. (BPPEH; BBB/Stable/--) and CTP N.V. (BBB-/Stable/--), which have an average asset size of between 21,000 sq. m. and 26,000 sq. m. and a similar average age of about 10 years. Of P3's assets, 75% are in urban locations in logistics corridors (a one-hour drive from the population catchment of two million people), ensuring easy accessibility and to some extent supporting

distribution deliveries. We understand that the company plans to certify 75% of the existing portfolio by the end of 2022, and aims to have a large amount of its portfolio rated at the BREEAM level of "Very Good". This is in line with other rated peers in the logistics property segment.

P3's pan-European presence and strong operating performance should support stable income and cash flow generation. P3's portfolio is well-diversified geographically because its assets are located across 11 European countries (Germany 33%; Czech Republic 21%; Poland 10%; Spain 11%; Italy 8%; Slovakia 6%; France 5%; the Netherlands 3%; and Romania 3%). We view positively the markets in which P3 is present, especially Germany, Czech Republic, France, the Netherlands, and Spain, which in our view are historically more resilient to economic difficulties and have recently benefited from positive e-commerce tailwinds as demand outpaces new supply. The assets exhibit high physical average occupancy (95% as of June 30, 2021) and high rent-collection rates (above 99%), which we believe should support stable cash flow generation over the next two years. This compares well with other rated players in Europe, such as BPPEH and CTP, which own good-quality logistics real estate portfolios in urban locations in the main European corridors. P3 has a healthy tenant base with a high retention rate of about 80%, and a good average lease duration (about seven years of weighted-average lease terms), which highlight the company's strong competitive advantage and relationship with tenants. Its largest tenant is Metro Inc. (BBB/Stable/--), representing about 14% of total gross rental income as of June 30, 2021. We see limited development exposure (representing about 5% of the total gross asset value as of June 2021) and most of the developments are pre-let. P3 aims to maintain at least 70% pre-let levels for its future developments. That said, our assessment of P3 also considers its smaller asset base (portfolio of €6.7 billion) than that of higher rated peers', such as Prologis European Logistics Fund (A-/Stable/A-2), which owns a real estate portfolio worth €15.3 billion as of June 30, 2021. In addition, there is some concentration among the top 20 tenants, which account for 42% of rental income as of June 30, 2021, but we understand that most are large, creditworthy tenants.

We treat P3's shareholder loans as equity in our leverage calculations. The company's capital structure includes over €900 million of shareholder loans as of Oct. 31, 2021, from Euro Vitus Private Ltd., which owns 100% of P3 shares. We exclude these instruments in our leverage calculations because they exhibit equitylike characteristics, as laid out in our criteria (see "The Treatment Of Non-Common Equity Financing In Nonfinancial Corporate Entities," published April 30, 2018, on RatingsDirect). The non-common equity (NCE) effective financing maturity date is beyond that of the other existing debt and are structurally and contractually subordinated to other debt in the capital structure. While the NCE documentation includes an early redemption option (prepayment) that could be theoretically exercised at any time by the borrower, the prepayment flexibility is substantially mitigated by the company's inter creditor agreement, which restricts any early repayment of the shareholder loan subject to prior written consent of each senior debt creditor representative. Furthermore, we understand that the company's intention is to maintain this instrument outstanding in the capital structure. Therefore, we believe that there are strong contractual provisions that ensure this instrument will act as loss-absorbing capital in the future and as such exclude the NCE from our leverage calculations. The payment of interest on shareholder loans is permitted in certain circumstances; however, we understand that in the normal course of business, the company expects interest on shareholder loans to accrue and be capitalized. Should any of the terms and conditions mitigating early prepayment alter in the future, we may change the treatment of the NCE, which in turn may significantly affect our key credit metrics.

We expect P3's leverage ratios to remain at current levels, in line with its financial policy of a loan-to-value (LTV) ratio of up to 47.5%. Our assessment of P3's financial risk profile is supported by the sizable and stable recurring cash flow base, thanks to the relatively long contracts and stable occupancy. The company has a prudent financial policy with a net LTV of up to 47.5% (which translates to S&P Global Ratings-adjusted debt to debt plus equity of about 50%). We understand that the company aims to expand its portfolio base, mainly through developments and some acquisitions, while maintaining its current leverage. We assume €500 million-€600 million of net asset growth each year and therefore expect P3's debt to debt plus equity to increase toward 51%-52% in the next 12-24 months (49.7% as of Dec. 31, 2020). We expect debt to EBITDA to remain slightly high at about 14x-15x (16.9x as of Dec. 31, 2020), where full EBITDA contribution may not be achieved in the same year, and part of growth expenses are not capitalized like some of P3's peers but are expensed and in line with the company's accounting standards. The company assumes a mix of debt and equity to fund its future portfolio growth. P3 demonstrates a solid capacity to cover its interest burden, with EBITDA interest coverage that we expect to remain well above 5x in the next two years, and a low average cost of debt including the recent bond issuance. The company intends to refinance its current unsecured bank loans mainly toward an unsecured capital market debt structure. Including the recent bond issuance, the company has very limited refinancing needs over the next two years.

P3's strong shareholder, prudent financial policy, and well-positioned credit metrics under its current assessment support the rating. Our rating on P3 incorporates a one-notch upward adjustment based on our comparable ratings analysis. We consider the ultimate shareholder, Singapore sovereign fund GIC (Realty) Private Ltd., as a very strong strategic owner. We understand that GIC has a long-term investment horizon for P3 and supports P3's capital structure by providing guarantees to the existing unsecured bank loans. This allows P3 to benefit from unsecured bank funding at extremely low interest costs, versus the traditional secured bank financing that most peers have as part of their capital structure. We understand that no guarantees will be given for future issuances or refinanced debt; however, we expect that GIC will continue to support P3 with additional equity contributions in the future, which may be used for acquisitions and new project capital expenditure (capex) requirements. This should help the company to grow its portfolio while maintaining financial discipline in line with our current ratings. In addition, the company's overall credit metrics are better positioned than those of other real estate companies with the same financial risk profile assessment.

Outlook

The stable outlook reflects our view of P3's strong asset quality and high geographic diversity, which will likely enable it to continue generating stable and predictable income. Our base-case scenario also factors in P3's continuing expansion of its portfolio and increasing exposure to high-quality logistic assets, while maintaining its credit metrics. Under our base-case scenario, we anticipate that P3 should maintain adjusted EBITDA interest coverage ratio above 5x and a debt-to-debt-plus-equity ratio of about 51%-52% in the next 12-18 months.

Downside scenario

We could lower the rating if financial ratios weaken such that:

- Debt to debt plus equity moves toward 55% or above on a sustained basis;

- EBITDA interest coverage moves toward 2.4x or below; and
- A change in its current ownership structure that we view as less favorable or a change in existing or future shareholder loans leads us to review the equity treatment.

We would also take a negative view if P3 acquired properties with weaker characteristics--for example, properties in less fundamentally solid locations--or if the company were to increase its exposure to underperforming assets.

Upside scenario

We see a rating upside as limited, unless P3 significantly expands its portfolio scale and scope beyond our base case, while maintaining positive like-for-like rental growth and stable occupancy levels. In addition, the company would need:

- A maintained EBITDA interest coverage as per our base case;
- Debt to debt plus equity below 40% over a sustained period; and
- Debt-to-annualized EBITDA ratio well below 13.0x on a sustainable basis.

Company Description

P3 is a limited liability company incorporated in Luxembourg and a real estate owner of industrial properties. The company was established in 2001 and owns a gross portfolio value of about €6.7 billion (6.6 million sq. m. of gross leasable area) as of June 30, 2021. The total portfolio includes about 300 logistics properties spread across 11 European countries.

P3 is 100% owned by Euro Vitus Private Ltd., which is ultimately controlled by the sovereign wealth fund GIC.

Our Base-Case Scenario

Assumptions

- Real GDP in the eurozone to grow by 4.5%-5.0% in 2022 and 2023. We expect unemployment in the eurozone to remain at about 7.0%-7.5% in 2022, with moderate inflation of about 3%-3.5% in the next 12-24 months.
- Annual like-for-like rental growth of about 1.5%-2.0% over the next two years, mostly benefiting from consumer price index inflation, and limited growth from rent reversion, given the company's low level of leases that will expire in the next two years.
- Occupancy levels to remain at about 95% in the next 12-24 months, mainly supported by high occupancy in Germany, Czech Republic, and the Netherlands.
- Positive portfolio revaluation of 7%-8% in 2021, mainly supported by revaluation gains of about €475 million-€500 million already achieved as of June 30, 2021. We expect an annual 2%-3% revaluation from 2022.
- Acquisitions of about €400 million in 2021 and about €500 million-€550 million annually in the coming years, as per management's intention to increase the company's scale and presence in

European markets.

- About €350 million-€400 million development capex in 2021 and about €300 million-€350 million per year in 2022 and future years.
- Disposals of about €250 million in 2021. We also forecast disposals of €150 million-€200 million in 2022 and future years as per management's intention to dispose certain noncore assets.
- Steady EBITDA margins of close to 77%-78% in the next few years.

Key metrics*

- A debt-to-debt-plus-equity ratio of about 51%-52% over the next 24 months.
- Adjusted debt to EBITDA of about 14x-15x over the next 24 months; however, as a result of the portfolio expansion plan, this does not reflect the full annualized EBITDA contribution from the investments made during the year. Hence, we expect this to decrease over time; and
- Adjusted EBITDA interest coverage of above 5.0x in the next two years.

*Including its shareholder loans as equity for our credit metrics calculations.

Liquidity

We anticipate P3's liquidity sources will likely cover liquidity uses by more than 1.2x in the 12 months started Oct. 1, 2021. Therefore, we assess liquidity as adequate.

We estimate principal liquidity sources for the 12 months from Oct. 1, 2021, as follows:

- €278.6 million in available unrestricted cash;
- Undrawn revolving credit facility (RCF) of €750 million, maturing in over 12 months;
- Our estimate of funds from operations of about €200 million-€220 million; and
- Unsecured bonds of €1.0 billion.

We estimate the following principal liquidity uses for the same period as follows:

- About €1.0 billion of unsecured bank loan repayment;
- About €400 million-€450 million of committed development capex; and
- Committed acquisitions of €200 million-€210 million, mainly to acquire assets for future growth.

Covenants

The company has no financial covenants on its unsecured bank term loans. We understand that the new RCF has ongoing maintenance financial covenants. We also understand that the bonds have financial covenants that restrict the ability to raise additional debt related to a maximum net loan-to-value ratio of 60%, a minimum interest coverage ratio of 1.5x, and unencumbered assets to net unsecured debt greater than 150%, and priority debt would be greater than 40% of the property value. We forecast that the company will keep sufficient headroom (greater than 15%)

under all its covenants of the capital structure, including the recently issued bonds.

Environmental, Social, And Governance

ESG credit indicators: E-2 S-2 G-2

ESG factors have no material influence on our credit rating analysis of P3. We understand that the company plans to certify 75% of the total portfolio by the end of 2022 with a target to achieve large portfolio at BREEAM very good plus. This is in line with other rated peers in the logistics property segment. We believe customer (tenant) demand for sustainable buildings has been increasing across Europe in the past couple of years.

Issue Ratings - Subordination Risk Analysis

Capital structure

The group's capital structure comprises about 100% of unsecured debt. The company has existing bank term loans, but those are unsecured, because GIC (the ultimate shareholder) provides guarantees to the existing unsecured bank term loans. The company expects to partially replace the existing bank term loans with the recent bond issuance and new RCF and the remainder of the existing bank term loans to be refinanced in the coming years.

Analytical conclusions

We expect P3's group exposure to secured debt to remain below 40% of total fair market value of the assets in the next 12-24 months. Although unsecured debt issuance is structurally subordinated to other debt obligations, the subordination does not affect the rating on the unsecured debt. Therefore, our issue rating is the same level as the issuer credit rating.

Ratings Score Snapshot

Issuer credit rating: BBB/Stable/--

Business risk: Satisfactory

- Country risk: Low
- Industry risk: Low
- Competitive position: Satisfactory

Financial risk: Significant

- Cash flow/Leverage: Significant

Anchor: bbb-

Modifiers:

- Diversification/Portfolio effect: Neutral (no impact)

- Capital structure: Neutral (no impact)
- Liquidity: Adequate (no impact)
- Financial policy: Neutral (no impact)
- Management and governance: Fair (no impact)
- Comparable rating analysis: Positive (+ one notch)

Related Criteria

- 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
- Criteria | Corporates | Industrials: Key Credit Factors For The Real Estate Industry, Feb. 26, 2018
- Criteria | Corporates | General: Methodology And Assumptions: Liquidity Descriptors For Global Corporate Issuers, Dec. 16, 2014
- Criteria | Corporates | General: The Treatment Of Non-Common Equity Financing In Nonfinancial Corporate Entities, April 29, 2014
- General Criteria: Methodology: Industry Risk, Nov. 19, 2013
- Criteria | Corporates | General: Corporate Methodology, Nov. 19, 2013
- General Criteria: Country Risk Assessment Methodology And Assumptions, 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

Related Research

- Logistics Company P3 Group S.a.r.l. Assigned Preliminary 'BBB' Rating; Outlook Stable, Jan. 17, 2022

Ratings List

New Rating	
P3 Group S.a.r.l.	
Issuer Credit Rating	BBB/Stable/--
Senior Unsecured	BBB

Certain terms used in this report, particularly certain adjectives used to express our view on rating relevant factors, have specific meanings ascribed to them in our criteria, and should therefore be read in conjunction with such criteria. Please see Ratings Criteria at www.standardandpoors.com for further information. A description of each of

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