

Research Update:

Swedish Housing Company Uppsalahem 'AA-/A-1+' And 'K-1' Ratings Affirmed; Outlook Stable

June 13, 2019

Overview

- We expect Uppsalahem to uphold its sound operating balance, leading to lower external loan financing needs.
- We continue to believe that the company enjoys a high likelihood of extraordinary government support in the event of financial distress.
- We are affirming our 'AA-/A-1+' global scale and 'K-1' regional scale ratings on Uppsalahem.
- The stable outlook reflects our expectation that Uppsalahem will maintain its strong performance and conservatively manage its debt position.

Rating Action

On June 13, 2019, S&P Global Ratings affirmed its 'AA-' long-term and 'A-1+' short-term issuer credit ratings on Swedish housing provider Uppsalahem AB. The outlook is stable.

At the same time, we affirmed our 'K-1' Nordic regional scale rating on Uppsalahem.

Rationale

Uppsalahem's robust financial performance, continued minimal vacancy rates, and high demand are key strengths for the rating. The rating is somewhat constrained by slightly weak liquidity.

Uppsalahem holds a dominant position in the city of Uppsala's rental market through its 42% market share. Uppsala is experiencing strong population growth and economic development and we view the risk of market disruption as low. Although the pace of housing development (primarily condominiums) in Uppsala has fallen substantially in the past year compared with 2017, we do not expect any change in the demand or strategy for Uppsalahem's rental apartments. We assume that Uppsalahem's vacancies will remain negligible through 2021, attesting to its very predictable operating performance. In addition, we calculate the average price of private homes in Uppsala is 130% of the national average, which, combined with record population growth of about 2% per year, suggests solid local economic fundamentals.

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We assess the financial profile as strong, based on our expectation that Uppsalahem's conservative financial policies will contain its debt burden and maintain its strong margins. We acknowledge that Uppsalahem is in an expansion phase and expect that it will invest close to Swedish krona (SEK) 1 billion per year in 2019-2021 through new development and maintenance.

In our view, these planned investments will add to net new loans, resulting in debt to EBITDA of 12.2x by year-end 2021, down from our previous base-case expectations. At the same time, we believe there is ample room for the company to absorb new financing thanks to a very strong loan-to-value ratio of below 30% in 2018, headroom within its interest-coverage ratios, and the transition of a large percentage of loans to the city's in-house bank. In our base-case scenario, we estimate Uppsalahem's EBITDA interest coverage ratio at a very strong 4.7x on average over 2017-2021. However, we believe Uppsalahem's strategy of pursuing short durations in its loan portfolio, with 54% of loans having fixed interest of less than one year, adds some risk.

In 2019-2021, we forecast that Uppsalahem will post sound operating balances, with a five-year average EBITDA margin of 42.5%, due to increases in negotiated rents and the containment of operating costs. These strong operating margins will help to finance Uppsalahem's investment portfolio. Over 2019-2021, we forecast that Uppsalahem's investments and internal cash generation will create financing needs averaging SEK300 million (about €30 million) annually.

Over the past few years, the city has transferred Uppsalahem's loans into its in-house bank function as debt matures. After the transition to the city treasury, Uppsalahem will have about SEK600 million in commercial paper and the remainder as loans from the city. We expect Uppsalahem to keep backup facilities in place commensurate with a liquidity coverage ratio of about 80%--both during the incorporation in the in-house bank and thereafter.

We consider Uppsalahem to be a government-related entity. We base our view of a high likelihood of timely and sufficient extraordinary government support on our assessment of Uppsalahem's important role for Uppsala in providing affordable housing and area development. The company has a very strong link with the city, which is actively involved in defining its strategy, appoints its board of directors, and intends to maintain its 100% stake. In our view, Uppsalahem's ongoing integration into Uppsala's in-house bank affirms this very strong link.

The 'AA-' rating on Uppsalahem is derived from its stand-alone credit profile, which we assess at 'a+'. In our opinion, there is a high likelihood that the company's government owner, the city of Uppsala (AA+/Stable/A-1+), would provide timely and sufficient extraordinary support to Uppsalahem in the event of financial distress, which gives provides one notch of uplift to the rating.

Liquidity

We consider Uppsalahem's liquidity position to be somewhat weak although mitigated by strong access to external financing.

We calculate that Uppsalahem's liquidity needs over the next 12 months include interest expenses and capital spending of SEK900 million, together with debt maturities of SEK3 billion.

In terms of available liquidity, Uppsalahem committed to facilities with banks totaling SEK2.75 billion and cash and liquid short-term investments of SEK260 million in May 2019. Together with funds from operations (net of interest), we calculate that the company's available liquidity, including bank facilities, covers about 87% of uses of liquidity over the next 12 months.

Outlook

The stable outlook reflects our expectation that Uppsalahem will maintain its strong financial performance. We expect that the company will maintain sufficient financial buffers to support its increasing debt and that its integration into the city treasury will continue. We do not anticipate Uppsalahem's ownership or support structure will change to an extent that it would affect our view of the company's affiliation with Uppsala.

Upside scenario

We could raise the ratings if Uppsalahem's liquidity position strengthened substantially, coupled with the formalization of this strategy in the company's financial policies, and the amortization of its debt. We could also raise the ratings if we considered that Uppsalahem's role for the city had strengthened.

Downside scenario

The ratings could come under pressure if we observed that Uppsalahem's liquidity position relative to short-term debt maturities had deteriorated significantly, its access to external liquidity had decreased, or its role for, or link to, the city had weakened.

Table 1

Uppsalahem AB Selected Financial Indicators

(MIL. SEK)	--Fiscal year ended Dec. 31--				
	2017	2018	2019BC	2020BC	2021BC
Number of units	16,758.0	16,902.0	17,077.0	17,252.0	17,427.0
Vacancy rates (% of net rental income)	0.1	0.1	0.1	0.1	0.1
Revenue	1,334.0	1,386.0	1,416.0	1,459.0	1,503.0
EBITDA§	575.7	601.0	633.2	647.1	661.3
EBITDA/revenue (%)	43.2	43.4	44.7	44.4	44.0
Interest expense	119.1	133.6	124.3	129.8	134.7
Debt/EBITDA (x)	12.4	11.9	11.8	12.1	12.2
EBITDA/interest coverage (x)†	4.8	4.5	5.1	5.0	4.9
Capital expense	960.2	766.4	805.0	825.0	775.0
Debt	7,148.0	7,150.0	7,475.0	7,800.0	8,050.0
Housing properties (according to balance-sheet valuation)	11,735.0	11,974.0	12,556.0	13,124.0	13,603.0
Cash	262.0	9.1	38.0	55.3	56.8

*Current arrears. §Adjusted for capitalized repairs. †Including capitalized interest. BC--base case, reflects S&P Global Ratings' expectations of the most likely scenario. SEK--Swedish krona.

Ratings Score Snapshot

Table 2

Uppsalahem AB Rating Score Snapshot

Industry risk	2
Economic fundamentals and market dependencies	1
Strategy and management	2
Asset quality and operational performance	1
Enterprise profile	2
Financial performance	2
Debt profile	3
Liquidity	4
Financial policies	2
Financial profile	3

S&P Global Ratings' analysis of social housing providers' creditworthiness rests on our scoring of eight key rating factors: (i) industry risk; (ii) economic fundamentals and market dependencies; (iii) strategy and management; (iv) asset quality; (v) financial performance; (vi) debt profile; (vii) liquidity; and (viii) financial policies. Each of the factors is assessed on a continuum spanning from 1 (strongest) to 6 (weakest). S&P Global Ratings' "Methodology For Rating Public And Nonprofit Social Housing Providers," published Dec. 17, 2014, and "Rating Government-Related Entities: Methodology And Assumptions," published March 25, 2015, detail how we derive and combine the scores, and then determine each social housing provider's stand-alone credit profile and the issuer credit rating. In accordance with S&P Global Ratings' public and nonprofit social housing providers methodology, a change in score does not in all cases lead to a change in the rating, nor is a change in the rating necessarily predicated on changes in one or more of the scores. In determining the final rating, the committee can make use of the flexibility afforded by paragraphs 12-17 of "Methodology For Rating Public And Nonprofit Social Housing Providers."

Related Criteria

- General Criteria: Methodology For Linking Long-Term And Short-Term Ratings, April 7, 2017
- General Criteria: Rating Government-Related Entities: Methodology And Assumptions, March 25, 2015
- Criteria | Governments | General: Methodology For Rating Public And Nonprofit Social Housing Providers, Dec. 17, 2014
- General Criteria: Stand-Alone Credit Profiles: One Component Of A Rating, Oct. 1, 2010
- General Criteria: Use Of CreditWatch And Outlooks, Sept. 14, 2009

Related Research

- S&P Global Ratings Definitions, Oct. 31, 2018

Ratings List

Ratings Affirmed

Uppsalahem AB

Issuer Credit Rating AA-/Stable/A-1+

Nordic Regional Scale --/--/K-1

Commercial Paper K-1

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. Complete ratings information is available to subscribers of RatingsDirect at www.capitaliq.com. All ratings affected by this rating action can be found on S&P Global Ratings' public website at www.standardandpoors.com. Use the Ratings search box located in the left column. Alternatively, call one of the following S&P Global Ratings numbers: Client Support Europe (44) 20-7176-7176; London Press Office (44) 20-7176-3605; Paris (33) 1-4420-6708; Frankfurt (49) 69-33-999-225; Stockholm (46) 8-440-5914; or Moscow 7 (495) 783-4009.

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