FitchRatings

RATING ACTION COMMENTARY

Fitch Affirms IGD at 'BBB-'; off RWN; Outlook Negative

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Fitch Ratings - Stockholm - 01 Oct 2020:

Fitch Ratings has affirmed IGD SIIQ S.p.A's Long-Term Issuer Default Rating (IDR), and senior unsecured ratings at 'BBB-'. Both the IDR and the instrument ratings have been removed from Rating Watch Negative (RWN). The Outlook on the IDR is Negative.

The rating action reflects higher actual rent collection rates than initially forecast in early April, when IGD was placed on RWN. Since then, shops partially reopened in May and in full during June, limiting the closure to two to three months, while the Italian government has supported the local economy through fiscal incentives (30% to 60% tax credit to those tenants who have paid their March to June rents in full) and government-backed loans. In negotiations with its tenants, IGD favours rent deferrals over rent discounts and waivers. This provides improved visibility on IGD's rental income and contributes to the removal of the RWN.

The Negative Outlook reflects the ongoing uncertain impact on future rental income and the pandemic's effect on consumer spend. Despite cuts to both capex and dividends, we forecast that IGD will exceed our downgrade sensitivity of net debt/EBITDA above 10x in 2020. While we expect rental income to return to 2019's EUR150 million level by 2022 and provide greater financial headroom, a protracted loss of rental income, in the absence of sufficient initiatives to reduce debt, will put pressure on the current ratings.

KEY RATING DRIVERS

Negative Pressure on Retailers: In the three months of strict lockdown in Italy from 13 March 2020, IGD had to shut down all retail galleries within its shopping centres, only allowing hypermarkets, tobacco shops and pharmacies to remain open. This meant that other stores lost two to three months of sales and faced difficulties to pay their rental obligations. IGD is actively engaging with its tenants to reschedule 2Q20 (April to June) rents. As at the beginning of September 2020, around 80% of its tenants have agreed a payment plan.

Increasing Footfall Helps Collection Rates: The payment plans switch to monthly payments for all retailers, with unpaid rents for April, May and June now due at the end of June, September and November respectively. Initial collection figures for April were low at 50% (as at 6 August 2020), although in line with other European shopping centres operators'. This, combined with hypermarket rent paid, represented around 70% of April's rent paid for IGD (May: 65%). Fitch estimates that these figures should have increased in recent weeks, as recovery in footfall (August 2020: -12.6% vs August 2019) and increased average ticket size (August 2020: 19.1% vs August 2019) will help retailers' finances and IGD in its rent negotiations.

4Q20 to Indicate Recovery Pace: The next quarter, 4Q20, will be crucial to assessing the recovery pace of footfall and tenants' sales, as tenants are scheduled to pay two months' worth of rents in September (unpaid May and September) and November (unpaid June and November). An increase in vacancies or further concessions from IGD to its tenants to preserve occupancy versus rental income will be negative for IGD's rating.

Grocery Stores Resilient: Grocery stores across Italy have been increasing their sales since the beginning of March when coronavirus started to spread rapidly there. Restrictions imposed on bars and restaurants have helped to increase grocery shops' sales. Hypermarkets account for around 25% of IGD's gross rents in Italy and represent a defensive source of income. Other essential goods retailers (such as chemists, para-pharmacies and tobacco shops) represent an incremental source of rental income (8%). These stores are regularly paying their rents (collection rate: 100%).

Leverage Increase Detrimental: Fitch estimates net debt/EBITDA at 12.4x for 2020, assuming two months loss of rent from non-essential retailers (representing 67% of total rent roll). We forecast a gradual improvement in IGD's leverage metrics over the following years, assuming tenants will gradually trade as normal, excluding the harmful impact of a second lockdown. We forecast 2021's net debt/EBITDA at 10.6x which is still high for the rating, and 9.6x in 2022. Should tenant defaults materialise or rent arrears and discounts increase, the financial profile of IGD will not be commensurate with the current ratings.

Measures to Preserve Cash: IGD is preserving liquidity and has reduced certain cash outflows, similarly to many Fitch-rated property companies. It has postponed EUR40 million of non-essential capex from 2020 to following years and has reduced its 2020 annual dividend to EUR25 million (2019: EUR55 million), the minimum required by the local REIT regime. Liquidity is further aided by the SACE-guaranteed (the state-controlled entity facilitating access to credit and promoting Italian exports) unsecured loan (EUR36.3 million) that IGD obtained in late September.

DERIVATION SUMMARY

IGD's portfolio of shopping centres is similar in size to that of Atrium European Real Estate Limited (BBB/Stable) and less than a half of that of NEPI Rockcastle plc (BBB/Stable). These two central and eastern European shopping centre operators have stronger financial metrics, partially reflecting higher income-yielding assets that are more comparable with IGD's small Romanian portfolio.

In western Europe, valuation yields for the same asset class are tighter and cash flow leverage for investment-grade REITs trends towards and above 10x. Hammerson plc (BBB/Negative), whose pro forma net debt/recurring EBITDA is around 9x, has a portfolio mainly composed of larger but low-income yield, prime and good secondary assets. UK-based NewRiver REIT plc (BBB/Stable), which also focuses on small and convenience-led shopping centres, has stronger financial metrics reflecting its higher income yield.

KEY ASSUMPTIONS

- Rental income from IGD's retail portfolio excluding hypermarkets to decline by around 20% in 2020. We expect 50% of the rent lost in 2020 to be recovered in 2021 and then fully recovered in 2022.

- Development programme-related capex of around EUR15 million in 2020, of which around EUR5 million-EUR7 million is in 2H20.

- Reduced dividend payments in 2020-2021 (EUR25 million) relative to lower funds from operations (FFO generation). Dividends restored to a level similar to 2019 levels thereafter.

- No property disposals.

RATING SENSITIVITIES

Factors that could, individually or collectively, lead to positive rating action/upgrade:

- Net debt/EBITDA below 9.0x on a sustained basis

- Material diversification of the portfolio by tenant

- Recurring EBITDA interest cover remaining above 1.75x

Factors that could, individually or collectively, lead to negative rating action/downgrade:

- Effect of rental concessions on IGD's future financial profile

- Net debt/EBITDA above 10.0x on a sustained basis

- Recurring EBITDA interest cover falling below 1.5x

- Loan-to-value rising above 50%

- Inability to refinance bonds well in advance of maturities leading to liquidity score falling below 1x

BEST/WORST CASE RATING SCENARIO

International scale credit ratings of Non-Financial Corporate issuers have a best-case rating upgrade scenario (defined as the 99th percentile of rating transitions, measured in a positive direction) of three notches over a three-year rating horizon; and a worst-case rating downgrade scenario (defined as the 99th percentile of rating transitions, measured in a negative direction) of four notches over three years. The complete span of best- and worst-case scenario credit ratings for all rating categories ranges from 'AAA' to 'D'. Best- and worst-case scenario credit ratings are based on historical performance. For more information about the methodology used to determine sector-specific best- and worst-case scenario credit ratings, visit https://www.fitchratings.com/site/re/10111579.

LIQUIDITY AND DEBT STRUCTURE

Sufficient Liquidity: As at June 2020, IGD had EUR103 million of available cash and EUR60 million undrawn committed revolving facilities that were recently extended until 2023. This compares with EUR22 million of bank debt maturing in 2H20. The next large maturity will be in May 2021 when the remaining EUR71 million bond will mature. Fitch does not include uncommitted credit facilities (EUR161 million at end-June 2020) in available liquidity, as they may become more restricted if the operating environment deteriorates although, to date, IGD has been able to regularly renew its bank lines.

In September 2020 IGD obtained an additional EUR36.3 million unsecured loan guaranteed by SACE as part of the Italian government initiative to support businesses during the health emergency.

REFERENCES FOR SUBSTANTIALLY MATERIAL SOURCE CITED AS KEY DRIVER OF RATING

The principal sources of information used in the analysis are described in the Applicable Criteria.

ESG CONSIDERATIONS

Unless otherwise disclosed in this section, the highest level of ESG credit relevance is a score of '3'. This means ESG issues are credit-neutral or have only a minimal credit impact on the entity, either due to their nature or the way in which they are being managed by the entity. For more information on Fitch's ESG Relevance Scores, visit www.fitchratings.com/esg.

RATING ACTIONS

ENTITY/DEBT	RATING			PRIOR
IGD SIIQ S.p.A.	LT IDR	BBB- Rating Outlook Negative	Affirmed	BBB- Rating Watch Negative
• senior unsecured	LT	BBB-	Affirmed	BBB- Rating Watch Negative

VIEW ADDITIONAL RATING DETAILS

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APPLICABLE CRITERIA

Corporates Notching and Recovery Ratings Criteria (pub. 14 Oct 2019) (including rating assumption sensitivity)

Corporate Rating Criteria (pub. 01 May 2020) (including rating assumption sensitivity)

Sector Navigators - Addendum to the Corporate Rating Criteria (pub. 26 Jun 2020)

APPLICABLE MODELS

Numbers in parentheses accompanying applicable model(s) contain hyperlinks to criteria providing description of model(s).

Corporate Monitoring & Forecasting Model (COMFORT Model), v7.9.0 (1)

ADDITIONAL DISCLOSURES

Dodd-Frank Rating Information Disclosure Form

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