

Rating Action: Moody's upgrades Citycon's ratings to Baa1; stable outlook

Global Credit Research - 15 Jan 2016

London, 15 January 2016 -- Moody's Investors Service has today upgraded to Baa1 from Baa2 the senior unsecured long-term issuer ratings of Citycon Oyj ("Citycon") and the instrument rating of its EUR500 million 3.75% notes due 2020 issued by Citycon, the EUR350 million 2.5% senior unsecured notes due 2024 issued and EUR300 million 2.375% unsecured notes due 2022 issued by Citycon Treasury B.V., both irrevocably and unconditionally guaranteed by its Citycon. The outlook on all ratings is stable.

RATINGS RATIONALE

"We have upgraded Citycon's ratings to Baa1 from Baa2 reflecting the company's improved business profile following the acquisition and integration of Sektor", said Roberto Pozzi, Moody's Vice President and lead analyst on the company. "We consider that the company will have greater geographic diversification as well as scale, and reduced tenant concentration risk when compared to its previous business profile".

Citycon's Baa1 long term issuer rating reflects the company's business model focused on the long term ownership and management of a retail property portfolio across the Nordics, the region's strong long term fundamentals and its greater exposure to stable food retail spending compared to other retail property companies. The ratings also reflect the company's greater geographic diversity following the acquisition of Sektor (unrated) in July 2015, which has greatly reduced macro and tenant concentration risks, in our view. The rating also reflects our expectation that Citycon will maintain fixed charge cover of around 3x over the next two years, its conservative interest rate hedging policy, and adequate liquidity underpinned by a mostly unencumbered asset base.

The Sektor transaction has reduced Citycon's exposure to the weak Finnish economy: its geographic exposure has become much more diversified with 35% of its gross asset value located in Finland (Aaa negative, 51% before the acquisition), 29% in Norway (Aaa stable), 28% in Sweden (Aaa stable) and 8% split between Estonia (A1 stable) and Denmark (Aaa stable), according to the figures reported for the third quarter of 2015. The transaction has also considerably increased Citycon's scale and established it as a truly pan-Nordic leader, the largest in Finland and Estonia, the second and third largest in Norway and Sweden, respectively. If Kista was fully consolidated, Sweden would represent a third of the company's GAV and boost its market position.

We expect Citycon's net rental income growth to remain close to flat or slightly (between -1 and -2%) negative on a like-for-like basis (excluding currency effects) over the next 12-18 months reflecting our view of some further pressure on rents given still weak retail sales in Finland and increasing competition in the Baltics which a more resilient performance in Sweden and Norway might not entirely offset. Longer term, however, we remain positive on the company's strategy focused on investing in high quality convenience shopping centres located in growing, urban locations with strong demographics in the Nordics.

Citycon has one of the largest exposures to food/grocery shopping across Europe's retail property companies. We believe that food retail sales tend to be more stable and, everything else being equal, that this also tends to result in a more defensive business profile for retail property companies. Citycon owns 29 shops that are leased to Kesko Corporation. Kesko contributed 13.2% of rental income in 2015 from 15.4% in 2014 and 16.1% in 2013. The next largest tenant is S Group, a Finnish retail cooperative which generated 6% of Citycon's gross rental income in 2014. Following the completion of Citycon's planned sale of several non-core assets, and after the acquisition of Sektor, these exposures will decrease (to approx. 7% for Kesko), which we view as a major improvement in terms of tenant concentration risk and business profile overall.

The company's fixed charge cover and "effective" leverage stood at 3.2x and 43%, respectively, at the same date. Despite expected additional debt over the next two years to fund modest asset growth, we anticipate that Citycon will maintain "effective" leverage (gross debt to total assets, as adjusted by Moody's) between 40%-45% over the next two years, with a fixed charge cover unchanged at approximately 3.0x.

Citycon has adequate liquidity in our view, underpinned by the steady generation of recurring cash flow and ample availability under its sizeable and long-dated revolving credit facilities. The company's immediate liquidity amounted to EUR379 million at the end of September 2015, including EUR44 million of cash on balance sheet, EUR 18 million of account overdraft limits and EUR317 million available under undrawn committed bank lines. We

expect these resources to more than cover the cash outflows anticipated over the next 12-18 months.

RATIONALE FOR THE STABLE OUTLOOK

We expect the company will invest mainly to improving the quality of its shopping centres over the next two years and refrain from major further expansion of its asset base. The stable outlook also reflects our expectation that Citycon will maintain fixed charge cover at approximately 3.0x, a conservative interest-rate hedging policy, and adequate liquidity, including a mostly unencumbered asset base. We also expect that "effective" leverage will remain between 40%-45%.

What Could Change the Rating -- Up/Down

Upward rating pressure could develop if the company further improved its business profile (assets quality, market position, diversification, etc.) whilst maintaining its current financial profile, or if debt metrics improve with the current business profile. Although we anticipate that the company will continue investing and improve the quality of its assets, we also expect such spending to focus mainly on extensions and re-developments of existing shopping centers. Quantitatively, expectations of leverage sustained below 40% and a fixed charge cover sustained above 3.5x could create positive rating pressure.

Downward pressure could develop if we expected a deterioration of the company's business or financial profile, as evidenced by a fixed charge coverage below 2.5x or effective leverage above 45%. Negative rating pressure could also result if a deteriorating trend in the company's covenant headroom or liquidity develops.

Headquartered in Helsinki (Finland), Citycon is a property company that owns and manages urban, grocery-anchored shopping centres in the Nordic and Baltic region with gross rental income of EUR206 million in the first nine months of 2015 and adjusted gross assets of EUR4.7 billion as of 30 September 2015. The company also has a 50% stake in Kista Galleria, a large shopping centre in Stockholm, which is reported using the equity method.

PRINCIPAL METHODOLOGY

The principal methodology used in these ratings was Global Rating Methodology for REITs and Other Commercial Property Firms published in July 2010. Please see the Credit Policy page on www.moodys.com for a copy of this methodology.

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