MG RE Invest S.A.
Kingdom of Belgium, Real Estate

BB STABLE

Key metrics

			Scope estimates	
Scope credit ratios	2021	2022	2023E	2024E
Scope-adjusted EBITDA/interest cover	10.3x	10.1x	5.2x	6.4x
Scope-adjusted debt/EBITDA	3.2x	3.9x	4.5x	3.7x
Scope-adjusted loan/value ratio	53%	52%	52%	45%

Rating rationale

The rating is supported by MG RE Invest S.A.'s strong credit metrics and the successful and prudent execution of its development pipeline. Its pipeline benefits from a predominant exposure to the logistics segment with favourable long-running market drivers.

Main rating constraints include MG RE's relatively small size and lack of diversification within its development pipeline and revenue streams, which hinder its ability to mitigate potential cash flow volatility given the cyclical nature of development activities and shifting market conditions.

Outlook and rating-change drivers

The Outlook is Stable and reflects our expectation that the company will successfully execute its development pipeline amid favourable market drivers for the logistics segment and maintain a careful approach towards development risks. Moreover, the Stable Outlook reflects our expectation that the company will keep leverage under control, with Scope-adjusted debt/EBITDA below 6x.

A negative rating action could be warranted if Scope-adjusted debt/EBITDA exceeded 6x or Scope-adjusted EBITDA/interest cover dropped below 4x on a sustained basis. This could be triggered by lower exit values due to widening yields, cost overruns or prolonged disposal periods.

A positive rating action might be warranted if the company increased its size and improved its development pipeline diversification while keeping credit metrics within our rating guidance.

Rating history

Date	Rating action/monitoring review	Issuer rating & Outlook
13 April 2023	Affirmation	BB/Stable
07 April 2022	New	BB/Stable

Ratings & Outlook

Issuer	BB/Stable
Senior unsecured debt	BB

Analyst

Fayçal Abdellouche
+49 30 27891 026
f.abdellouche@scoperatings.com

Related Methodologies and Research

General Corporate Rating Methodology; July 2022

European Real Estate Rating Methodology; January 2023

ESG considerations for the credit ratings of real estate corporates; April 2021

European Real Estate sector Outlook; October 2022

Scope Ratings GmbH

Lennéstraße 5
10785 Berlin

Phone +49 30 27891 0
Fax +49 30 27891 100

info@scoperatings.com
www.scoperatings.com

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Rating and rating-change drivers

Positive rating drivers	Negative rating drivers
• Sizeable development pipeline with a potential of 1.3 million sq m of gross leasable area, ensuring positive growth prospects • High pre-sale/pre-letting rates reducing disposal risks and providing good visibility on future revenue • Good standing in the industrial/logistics development segment, which benefits from robust underlying fundamentals • High quality projects translating into high pre-letting rate and long-dated weighted average unexpired lease term (above 10 years), ultimately supporting the saleability of properties	• Relatively small company in the European logistics real estate market, albeit a sizeable player in its domestic market of Belgium • High exposure to volatility induced by the cyclical nature of real estate development • Exit values/margins constrained by yields movements and inflationary pressure • Debt protection constrained by exposure to floating rate debt (indexed to Euribor)

Positive rating-change drivers	Negative rating-change drivers
• Increased size and improved diversification of the pipeline while keeping credit metrics within our rating guidance	• Scope-adjusted debt/EBITDA of above 6x or Scope-adjusted EBITDA/interest cover sustained below 4x

Corporate profile

MG RE Invest S.A. is a private real estate developer that focuses on large-scale logistics projects such as storage and distribution facilities across several European countries, as well as residential real estate in Belgium. The company was founded in 2001 by its owner and president, Ignace De Paepe. As of end-2022, the company had a headcount of 53 (up 18 full-time equivalents YoY) and reported total assets of EUR 529m and EBITDA of EUR 68m.

Financial overview

				Scope estimates	
Scope credit ratios	**2020**	**2021**	**2022**	**2023E**	**2024E**
Scope-adjusted EBITDA/interest cover	5.7x	10.3x	10.1x	5.2x	6.4x
Scope-adjusted debt/EBITDA	7.3x	3.2x	3.9x	4.5x	3.7x
Scope-adjusted loan/value ratio	43%	53%	52%	52%	45%
Scope-adjusted EBITDA in EUR '000s					
EBITDA	17,341	64,321	68,007	65,193	82,864
Operating lease payments	0	0	0	0	0
Other items	0	0	0	0	0
Scope-adjusted EBITDA	**17,341**	**64,321**	**68,007**	**65,193**	**82,864**
Funds from operations in EUR '000s					
Scope-adjusted EBITDA	17,341	64,321	68,007	65,193	82,864
less: (net) cash interest paid	-3,051	-6,259	-6,708	-12,522	-12,992
less: cash tax paid per cash flow statement	-3,995	-2,471	-2,185	-5,453	-7,657
add: dividends from associates	0	0	0	0	0
Change in provisions	0	0	0	0	0
Funds from operations (FFO)	**10,295**	**55,591**	**59,114**	**47,217**	**62,216**
Net cash interest paid in EUR '000s					
Net cash interest per cash flow statement	-3,051	-6,259	-6,708	-12,522	-12,992
Change in other items	0	0	0	0	0
Net cash interest paid	-3,051	-6,259	-6,708	-12,522	-12,992
Scope-adjusted total assets in EUR '000s					
Total assets (reported)	291,341	390,949	529,073	601,917	703,275
less: cash and cash equivalents	-20,782	-35,195	-36,406	-32,746	-23,829
IFRS fair value adjustments	24,700	24,700	24,700	0	0
Scope-adjusted total assets	**295,259**	**380,454**	**517,367**	**569,172**	**679,446**
Scope-adjusted debt in EUR '000s					
Reported gross financial debt	148,200	218,283	292,494	326,448	331,448
less: subordinated (hybrid) debt	0	0	0	0	0
less: cash and cash equivalents	-20,782	-35,195	-36,406	-32,746	-23,829
add: non-accessible cash	0	0	0	0	0
add: pension adjustment	0	0	0	0	0
add: operating lease obligations	0	0	0	0	0
Other items[1]	0	19,800	12,400	0	0
Scope-adjusted debt	**127,418**	**202,888**	**268,487**	**293,702**	**307,619**

[1] Include financial guarantees.

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Environmental, social and governance (ESG) profile[2]

Environment	Social	Governance
Resource management (e.g. raw materials consumption, carbon emissions, fuel efficiency)	Labour management	Management and supervision (supervisory boards and key person risk)
Efficiencies (e.g. in production)	Health and safety (e.g. staff and customers)	Clarity and transparency (clarity, quality and timeliness of financial disclosures, ability to communicate)
Product innovation (e.g. transition costs, substitution of products and services, green buildings, clean technology, renewables)	Clients and supply chain (geographical/product diversification)	Corporate structure (complexity)
Physical risks (e.g. business/asset vulnerability, diversification)	Regulatory and reputational risks	Stakeholder management (shareholder payouts and respect for creditor interests)

Legend

Green leaf (ESG factor: credit positive)

Red leaf (ESG factor: credit negative)

Grey leaf (ESG factor: credit neutral)

Key person risk

The company is wholly owned by Ignace De Paepe (founder & president of the board), who is involved in the operational decision-making process. The sole-shareholder structure suggests a key person risk, which is partially mitigated by the experienced management team in place and the succession plan underway.

MG RE promotes the application of best sustainability practices at each project stage (site preparation, design) and seeks to optimise the management of resources (water, energy and waste). This allows the company to comply with increasing investor requirements for sustainable properties such as building certifications, the use of solar panels or on-site electric vehicle charging stations, which are becoming the norm for new developments. MG Park De Hulst (developed in 2021) is a great showcase of the company's standing, being the first carbon-neutral logistics building in Belgium. The company targets a minimum BREEAM certification 'very good' for all its projects.

Despite the positive factors mentioned so far, the company does not report on extra-financial performance and does not have defined ESG targets.

[2] These evaluations are not mutually exclusive or exhaustive as ESG factors may overlap and evolve over time. We only consider ESG factors that are credit-relevant, i.e. those that have a discernible, material impact on the rated entity's cash flow and, by extension, its credit quality.

Business risk profile: BB-

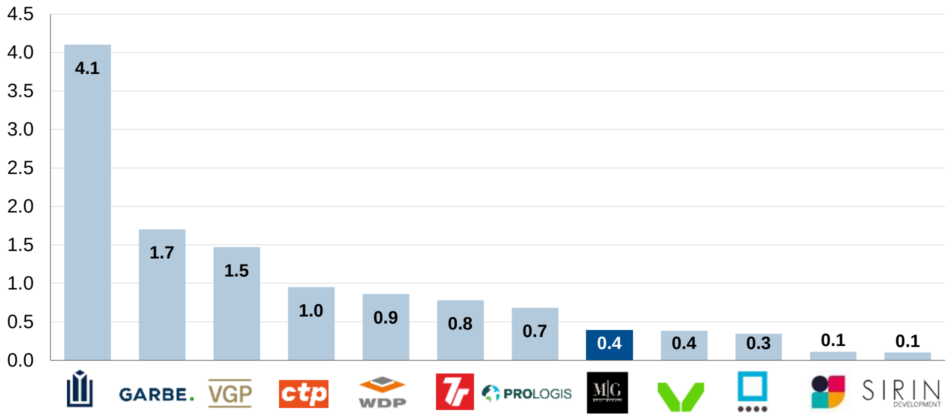
Industry risk profile: B+

MG RE's industry risk profile is primarily driven by its exposure to commercial development activities (industry risk: B) and to a lesser extent to residential property development/homebuilding (BB). We acknowledge the modest contribution of commercial rental activities (BB), which represented less than 3% of total revenue in 2022. Taking into consideration the pipeline breakdown, we assign a blended industry risk assessment of B+.

Small developer in the European commercial development market

MG RE is one of the largest developers of industrial and logistics space in its home-market of Belgium, but it is still comparatively small in a European context. With Scope-adjusted total assets of EUR 517m as of end-2022 (up 36% YoY), the company has grown organically over the years, following a gradual scaling approach and safeguarding capital resources. Since 2019, it has completed over 560,000 sq m of gross leasable area (GLA).

Figure 1: Logistics space under construction in Europe from selected developers (million sq m) as at end-2022



Sources: MG RE Invest S.A, Public information, PropertyEU, Scope

Solid market shares in its home market of Belgium

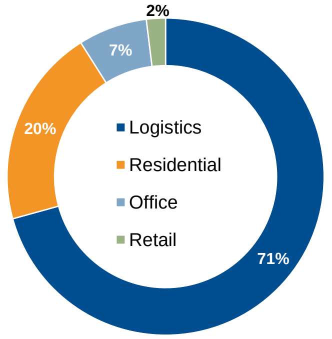
Although the company has a sizeable development pipeline (over 1.3 million sq m of GLA potential), it does not figure among the largest developers of industrial & logistics space in Europe. However, it ranks among the top-five in its home-market (alongside WDP and other European developers active in Belgium). Out of the volume of new logistics space delivered in the Belgium market in 2022 (around 700,000 sq m), at least 10% is attributable to MG RE and we expect the company to retain similar shares of completed volumes in 2023. This will be supported by planned projects such as MG Malinas (69,406 sq m), MG New Docks 1 (76,925 sq m) or MG Park Isnois (40,681 sq m), although some of these projects could run over into Q1 2024.

Moderate geographical concentration

The company's development activities are predominantly located in Belgium (70% of the project pipeline by GLA), whose market benefits from a sustained demand for industrial and logistics space (take-up exceeding 1.8 million sq m in 2022), a low vacancy rate (1.5% as of Q4 2022) and a limited availability of modern properties.

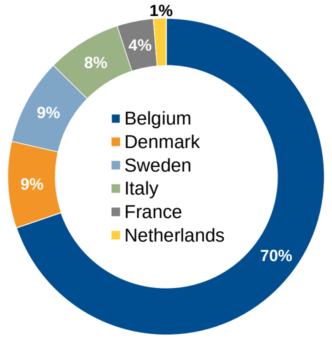
MG RE gradually expanded its geographical reach, starting in 2015 with a built-to-suit project for FedEx in Denmark. The company then executed projects in other European countries, whilst setting footholds in these locations for future opportunities. The company pursued a stepwise geographical expansion by establishing itself in markets with favourable growth prospects for industrial and logistics properties (i.e. strong demand from occupiers, low vacancy, limited space available).

Figure 2: Pipeline segment diversification (by planned GLA)



Sources: MG RE Invest S.A., Scope

Figure 3: Pipeline geographical diversification (by planned GLA)



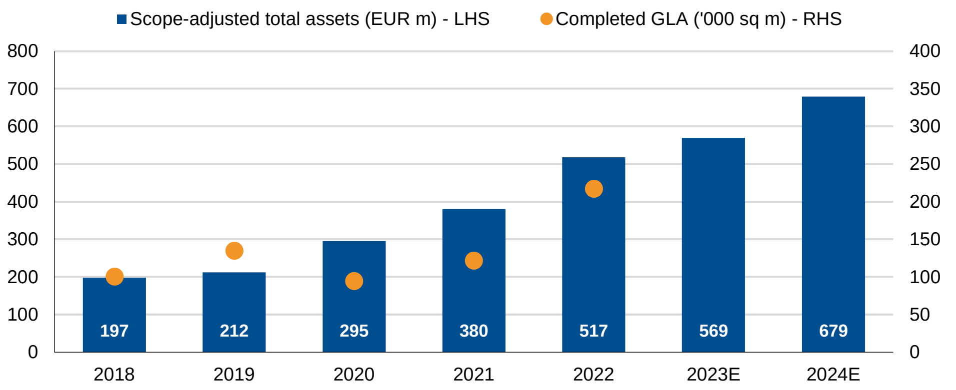
Sources: MG RE Invest S.A., Scope

While we do not expect it to occur in the short term, MG RE could seek to expand its geographical reach across other European countries such as Germany, Poland or the Czech Republic.

Pipeline largely skewed towards logistics projects

The company's project portfolio remains largely centred around industrial and logistics developments, which accounted for 71% of the pipeline by GLA as of end-2022, although it has been gradually complemented by other real estate segments (i.e. office, retail, residential). The diversification across segments has been largely promoted by the introduction of mixed-use projects and a focus on urban residential developments. The company's acquired exposure to other property types is positive, as these benefit from slightly different demand patterns and market dynamics.

Figure 4: Scope-adjusted total assets and completed gross leasable area



Sources: MG RE Invest S.A, Scope estimates

Development risks mitigated by favourable long-term market drivers for logistics…

The industrial/logistics segment benefits from long-running positive market drivers, mainly provided by the rapid growth of e-commerce and the occupiers' willingness to optimise supply chains. These strong underlying fundamentals ultimately favour developers, as they capitalise on the sustained demand for modern logistics properties (especially last-mile facilities), which are scarce in the markets where MG RE operates. However, the industrial/logistics segment is not immune from the pronounced repricing of real estate properties, with industrial prime yields expanding to 4.8% as of Q4 2022 (up 0.9 pp YoY), although it has been partly absorbed by continued and strong rental growth.

…and well-balanced project pipeline

With an average project investment size of EUR 35m, the development pipeline is well distributed across 27 projects (of which 13 were under construction as of end-2022), thus limiting concentration risks and the need to deploy substantial resources, as only a handful of projects exceed EUR 75m in investment.

MG RE has a good standing in the logistics development market, as evidenced by the trust received from top-quality investors and occupiers (investors include CBRE, Patrizia, Belfius; tenants include FedEx, DHL, Carrefour, Eutraco). Having developed a cumulative GLA of about 1.2 million sq m as of end-2022, the company has established a strong reputation and gained solid expertise in the execution of large-scale projects.

High-quality projects support attractiveness and liquidity

MG RE focuses on delivering modern and high-end properties, also aligned with high sustainability standards. The majority of logistics projects are located outside mid-to-large metropolitan areas (e.g. Brussel, Ghent, Malmö), which are particularly relevant for their end-use (i.e. proximity with ports and main E-road network). The quality positioning of MG RE properties is also reflected in achieved rental values, above or in line with logistics prime rental values in most locations, as well as long-dated lease term of above 10 years on average. Altogether, these factors support the attractiveness and liquidity of MG RE's properties, as they remain well-positioned to capture investment flows, largely directed towards high-quality assets with minimised tenant risk and high cash flow visibility. Potential investors are particularly cautious at the moment due to difficulties in accessing financing and elevated interest rates, as they wait for the right deals to come along.

High pre-sale/pre-letting rates support cash flow visibility

The company essentially focuses on forward development projects (no speculative projects) and seeks to reach an adequate lease rate before starting construction. The company has been able to enter pre-sale agreements at the early stage of a projects, thus limiting inherent development risks, ensuring shorter disposal periods and good cash flow visibility. The company has historically sold 95% of its projects before completion and 67% of the 2023 pipeline was secured through sale or promissory agreements as of Q1 2023. As for residential development, construction of the Emerald Garden project is expected to start in summer 2023 and was 29% pre-sold as of Q1 2023 (100% for adjoining retail spaces).

The high pre-letting rate achieved (projects under commercialisation are 52% pre-leased) coupled with long initial lease contracts (WAULT of between 10 and 15 years) largely support the saleability of properties while providing a cash flow buffer should disposals lag after completion. More than three quarters of logistics projects that are under construction were fully-lease as of Q1 2023. Lastly, MG RE's exposure to tenant risks is marginal, as properties are transferred immediately or soon after completion. Some properties can be held longer while waiting for better market conditions and long-term value appreciation.

Relatively high profitability, although vulnerable to volatility

In view of the company's reliance on development sales without recurring income streams (less than 3% of total revenue in 2022), volatility in earnings has been somehow moderate, although affected by the fluctuation of projects and share deal transactions. Profitability as measured by the Scope-adjusted EBITDA margin stood at 41% as at end-2022 (down 1.5 pp YoY), driven by the sharp increase in share deals booked (mostly concluded under the company's joint-venture arrangement). MG RE normally achieves margins between 20% and 35% on logistics projects (min/max of 10%/39%), which translates into a weighted average internal rate of return of around 25%. Residential projects' margins sit at around 12% on average.

We anticipate profitability at around 35% in 2023, supported by the company's lean organisational setup and its ability to partially pass on higher costs to end-buyers. We expect profitability to drop back to 30% or below after 2023, on the back of potential lower exit values due to yield movements, inflationary tension on construction costs and high land acquisition costs. We expect MG RE to maintain strong cost-discipline and to limit potential cost overruns to face these conditions.

Contained impacts from rising development costs

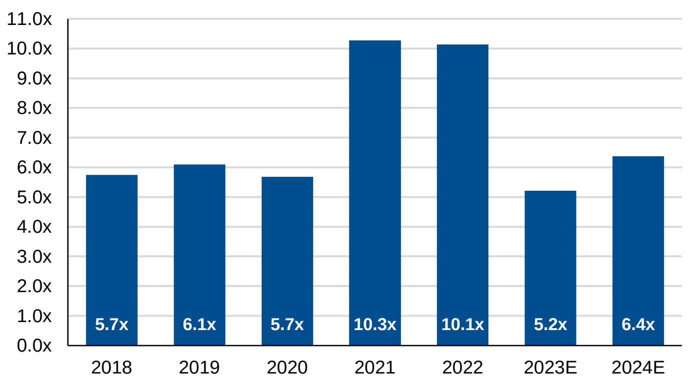
MG RE works with a small set of trusted contractors with whom it has built longstanding and sound relationships. Contracting works are awarded on a fixed price basis, thus limiting the impacts from rising construction and building material costs. However, contractors inevitably adjust their costs on future projects to factor in price volatility, which will ultimately reduce MG RE's margins. Further pressure on margins could arise from increased land prices, as demand and supply imbalances remain.

Financial risk profile: BBB-

Adequate debt protection, sufficient to serve interest payments…

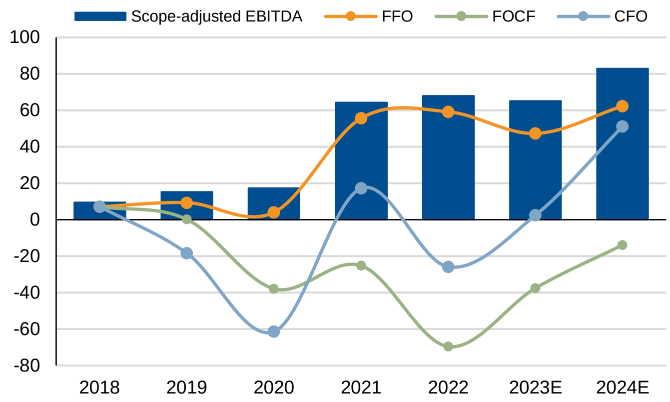
MG RE's debt protection is adequate, with Scope-adjusted EBITDA interest cover standing at 10.1x in 2022 (2021: 10.3x), largely supported by robust sales and improved profitability. Interest cover is sufficient to serve current and future interest payments, while providing some headroom against potential cash flow volatility, which commonly affects real estate development.

Figure 5: Scope-adjusted EBITDA/interest cover



Sources: MG RE Invest S.A, Scope estimates

Figure 6: Cash flow (EUR m)



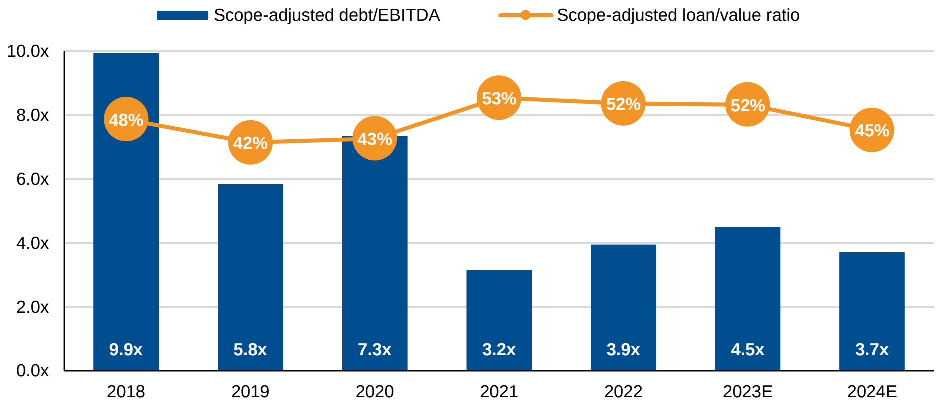
FOCF: free operating cash flow;
CFO: cash from operations
Sources: MG RE Invest S.A, Scope estimates

…although potential constrains remain

MG RE remains moderately exposed to interest risks, two-thirds of its debt having floating rates (indexed to Euribor), but exempt from foreign exchanges risks as all debt is denominated in euro. Given the changed interest rate environment, the company's average weighted cost of debt climbed to 4.5% as of Q1 2023. An interest rate swap, i.e. a 2% cap up to EUR 80m of debt, partially mitigates the impacts of rising interest rates. We expect cash flow generation to remain stretched, leading to additional short-term financing needs to fund investments and working capital gaps.

We expect interest cover to remain above 4x, taking into consideration a higher interest burden from project loans drawdowns, development spendings unmatched by cash flow and potential earnings volatility. Our view is further comforted by the company's prudent liquidity management, which aims to sustain a minimum cash position of EUR 20m.

Figure 7: Leverage



Sources: MG RE Invest S.A, Scope estimates

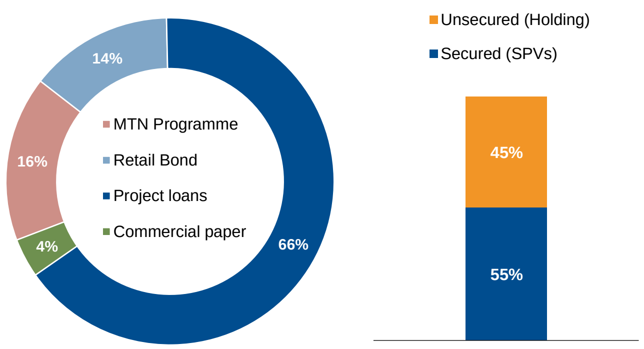
Moderate leverage, expected to remain below 6x

Leverage, as measured by Scope-adjusted debt/EBITDA, stood at 3.9x as at end-2022 (end-2021: 3.2x), although it remains well below its 2018-2020 peaks. Leverage remains satisfactory for a real estate developer, as it provides some headroom against potential volatility in earnings, a decline in property values or a decrease in demand.

Indebtedness has been rising since 2020, with Scope-adjusted debt reaching EUR 268m at end-2022 (up by EUR 141m from end-2020). As most ongoing developments are already financed through project loans, we do not anticipate any major debt issuance in the foreseeable future, but rather a recourse to short-term instruments that will be rolled over (i.e. commercial papers, revolving credit lines) to fund working capital.

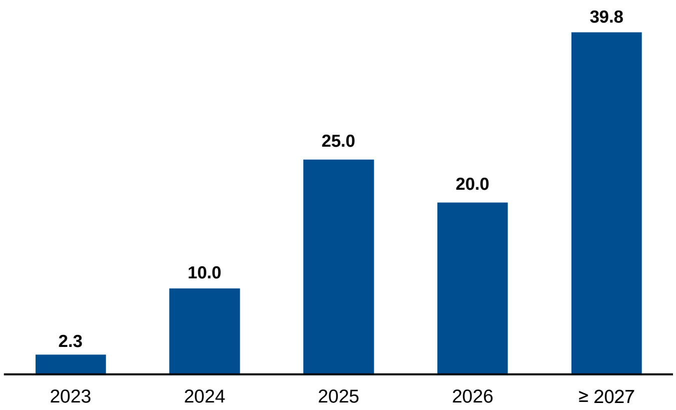
We expect leverage to remain below 6x, noting that the company still has some leeway under its development spending, having full discretion to postpone or cancel projects to preserve capital.

Figure 8: Debt composition and secured financing as of end-2022



Sources: MG RE Invest S.A, Scope estimates

Figure 9: Bond maturity schedule as of end-2022 (EUR m)



Sources: MG RE Invest S.A, Scope estimates

Adequate liquidity

Liquidity is adequate despite being below par for the 12 months to end-December 2023, with an anticipated shortfall of EUR 55m. This view is comforted by MG RE's consistent record of debt refinancing, its access to committed credit facilities and prudent liquidity management policy that aims to maintain a minimum cash position of EUR 20m. Besides, most developments are financed via non-recourse project loans (loan-to-cost ranging from 50% to 90%), which are immediately repaid upon disposal.

Balance in EUR '000s	2022	2023E	2024E
Unrestricted cash (t-1)	35,195	36,406	32,746
Open committed credit lines (t-1)	37,500	42,500	45,000
Free operating cash flow	-69,658	-37,615	-13,917
Short-term debt (t-1)	-60,537	-96,045	-60,000
Coverage	**5%**	**43%**	**106%**

In view of the issuer's good relationships with a diversified banking pool and its record in capital markets, liquidity and refinancing risks are manageable, especially given the absence of major upcoming debt maturities in the short-term.

Long-term debt rating

Senior unsecured debt rating: BB

Our recovery analysis is based on a hypothetical default scenario in 2024 and MG RE's liquidation value (subject to haircuts on inventories and finished properties and a 10% liquidation cost). On that basis, we have assessed an 'average' recovery for the company's senior unsecured debt, resulting in a BB rating for this debt category.

Appendix: Peer comparison

	MG RE Invest S.A	Futureal Holding B.V.	CORDIA International Zrt.	Infogroup Holding Kft.	Euroboden GmbH
	BB/Stable	BB/Negative	BB/Negative	BB-/Stable	B+/Negative
Last reporting date	31 December 2022	31 December 2021	31 December 2021	31 December 2021	30 March 2022
Business risk profile					
Scope-adjusted total assets (EUR m)	517	762	660	115	600
Gross lettable area (thousand sq m)	na	318	845	163	na
Countries active in	6	3	5	1	2
Top 3 tenants (%)	na	18%	na	39%	na
Top 10 tenants (%)	na	40%	na	75%	na
Property location	‘A’ and ‘B’	‘B’	‘B’	‘B’ and ‘C’	‘A’
EPRA occupancy rate	na	na	na	na	na
WAULT (years)	na	6.0	na	3.1	na
Scope-adjusted EBITDA margin	41%	19%	17%	51%	21%
Financial risk profile					
Scope-adjusted EBITDA/interest cover	10.1x	1.1x	3.6x	6.3x	1.4x
Scope-adjusted debt/EBITDA	3.9x	61.2x	4.8x	8.6x	20.8x
Scope-adjusted loan/value ratio	52%	43%	30%	46%	50%
Weighted average cost of debt	na	2.7%	na	3.4%	2.1%
Unencumbered asset ratio	>100%	>100%	>100%	>100%	>100%

Scope Ratings GmbH

Headquarters Berlin

Lennéstraße 5
D-10785 Berlin

Phone +49 30 27891 0

Frankfurt am Main

Neue Mainzer Straße 66-68
D-60311 Frankfurt am Main

Phone +49 69 66 77 389 0

Paris

10 avenue de Messine
FR-75008 Paris

Phone +33 6 6289 3512

Oslo

Karenslyst allé 53
N-0279 Oslo

Phone +47 21 09 38 35

Madrid

Paseo de la Castellana 141
E-28046 Madrid

Phone +34 91 572 67 11

Milan

Via Nino Bixio, 31
20129 Milano MI

Phone +39 02 30315 814

Scope Ratings UK Limited

London

52 Grosvenor Gardens
London SW1W 0AU

Phone +44 20 7824 5180

info@scoperatings.com
www.scoperatings.com

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