7 April 2022

Corporates

MG RE Invest S.A.
Luxembourg, Real Estate

STABLE

BB

Corporate profile

MG RE Invest S.A. (MG Real Estate) is a private real estate developer registered in Luxembourg. The company focuses on large-scale logistics real estate across several European countries, but with more than half of assets, as well as residential real estate, in Belgium. MG Real Estate was founded in 2001 by its owner and President, Mr. Ignace De Paepe. In 2021, the company had 34 employees and reported total assets (including 16 projects under development) and EBITDA of EUR 391m and EUR 64m respectively.

Key metrics

				Scope estimates	
Scope credit ratios	**2019**	**2020**	**2021**	**2022E**	**2023E**
Scope-adjusted EBITDA/interest cover	6.1x	5.7x	10.3x	7.5x	8.7x
Scope-adjusted debt (SaD)/ Scope-adjusted EBITDA	5.8x	7.3x	2.8x	3.1x	3.2x
Scope-adjusted loan/value ratio	42%	43%	48%	40%	41%

Rating rationale

Scope Ratings has today assigned a first-time issuer rating of BB/Stable to Luxembourg registered real estate developer MG RE Invest S.A. (MG Real Estate). Senior unsecured debt has also been rated BB.

MG Real Estate's business risk profile (assessed at BB-) is driven by the high industry risk for commercial real estate developers and the company's relatively small size, balanced by a strong developer track record, a conservative approach to development risk, high asset quality and a large pipeline.

With an active development pipeline of EUR 500-600m (500-600k sqm of gross lettable area 'GLA') for 2022 and 2023 combined, the company has a sizeable market position in logistics real estate development in its home market of Belgium (68% of pipeline), but it is relatively small in a European context, compared to for example Panattoni with over 4m sqm under construction. MG Real Estate also has significant developments underway in Denmark (16% of development pipeline) and Sweden (9%). Its relatively small size has resulted in high cash flow volatility in the past. However, this is partially mitigated by the fact that the development pipeline is diverse for a company of its size, with 16 assets under construction, largely pre-let or pre-sold to tenants and investors with a good credit standing. The developments are generally of a high quality, commanding above-average rent, benefitting from very long (15+ year) leases and BREEAM assessments of at least "very good".

MG Real Estate's financial risk profile (assessed at BBB-) reflects moderate financial leverage with Scope-adjusted debt (SaD)/Scope-adjusted EBITDA of 2.8x at YE 2021 and Scope-adjusted EBITDA interest coverage of 10.3x. Although the company has operated with much higher leverage in the past and experienced significant cash flow volatility, we expect leverage and interest coverage metrics to remain around these levels for the next two years as MG Real Estate executes its pipeline of largely pre-let and pre-sold properties and no M&A or shareholder distributions are expected.

Ratings & Outlook

Corporate rating[1]	BB/Stable
Senior unsecured debt rating	BB

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Related Methodologies

Corporate Rating Methodology
6 Jul 2021

European Real Estate Rating Methodology
25 Jan 2022

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Bloomberg: RESP SCOP

[1] Editor's note: The text was amended on 7 April 2022 after the initial publication. The original text read 'Corporate debt rating'

The timing of development handovers, rapidly rising inflation and working capital fluctuations could still cause volatility, however, and with about half of debt floating, the company is exposed to interest rate risk.

Liquidity is adequate. It is supported by the company policy of maintaining at least EUR 20m of cash balances (EUR 35m at YE 2021) as well as EUR 35m of long-term committed credit lines (of which EUR 7.5m were utilised at YE 2021), compared to short-term debt of EUR 61m.

One or more key drivers of the credit rating action are considered an ESG factor.

Outlook and rating-change drivers

The Stable Outlook is based on robust market conditions for logistics property in Europe and residential property in Belgium, as well as MG Real Estate's strong backlog, robust level of pre-lets and pre-sales for 2022 and 2023, with execution risk partially mitigated by strong developer track record. We expect SaD/Scope-adjusted EBITDA to remain around 3x and Scope-adjusted EBITDA/interest cover above 6x over the next two years.

A negative rating action might occur if the Scope-adjusted EBITDA/interest cover ratio drops to significantly below 4x or SaD/Scope-adjusted EBITDA significantly exceeds 6x on a sustained basis. This could result from, for example, cost overruns or delays in the company's existing development projects, or the inability to sustain the delivery of new developments at the current pace.

A positive rating action might be warranted if MG Real Estate continues to grow in size and geographic diversification, and maintains credit metrics in line with the above guidelines

Rating drivers

Positive rating drivers	Negative rating drivers
• 76 projects and over 1.2m sqm delivered over the past 20 years; no project has been sold at a loss • Large backlog of around 1.4m sqm (incl. 1.0m sqm of logistics) with an estimated exit value of EUR 2.6bn • Strong demand for logistics real estate in Europe fuelled by e-commerce and efforts to optimise supply chains • 70%-75% of projects under active development pre-let or pre-sold to counterparts of good credit standing • High asset quality reflected in long average lease tenor of over 15 years • Adequate liquidity with EUR 20-30m of cash at all times, in addition to back-up credit lines	• High industry risk for commercial real estate development • Relatively small company in the European logistics real estate market, but a sizeable player Belgium • High historic financial leverage • Negative discretionary cash flow in the past two years because of build-up in inventories and a one-off dividend payment • Around half of debt at floating interest rate, exposing the company to rising interest rates • Active developments encumbered in favour of secured lenders • Key person risk [ESG factor: credit negative]

Rating-change drivers

Positive rating-change drivers	Negative rating-change drivers
• Greater size and geographic diversification, whilst maintaining credit metrics in line with the guidelines for the rating	• SaD/Scope-adjusted EBITDA of significantly above 6x or Scope-adjusted EBITDA interest cover significantly below 4x on a sustained basis

Financial overview

				Scope estimates	
Scope credit ratios	**2019**	**2020**	**2021**	**2022E**	**2023E**
Scope-adjusted EBITDA/interest cover	6.1x	5.7x	10.3x	7.5x	8.7x
Scope-adjusted debt (SaD)/ Scope-adjusted EBITDA	5.8x	7.3x	2.8x	3.1x	3.2x
Scope-adjusted loan/value ratio	42%	43%	48%	40%	41%
Scope-adjusted EBITDA (EUR '000s)	**2019**	**2020**	**2021**	**2022E**	**2023E**
EBITDA	15,274	17,341	64,321	51,188	70,621
Scope-adjusted EBITDA	**15,274**	**17,341**	**64,321**	**51,188**	**70,621**
Scope-adjusted net cash interest (EUR '000s)	**2019**	**2020**	**2021**	**2022E**	**2023E**
Interest paid	-3,144	-3,381	-6,373	-6,816	-8,129
Interest received	638	330	114	0	0
Scope-adjusted net cash interest	**-2,506**	**-3,051**	**-6,259**	**-6,816**	**-8,129**
Scope-adjusted total assets (EUR '000s)	**2019**	**2020**	**2021**	**2022E**	**2023E**
Total assets	232,563	291,341	390,949	423,660	549,999
IFRS fair value adjustment	0	24,700	24,700	24,700	24,700
Cash and equivalents	-20,933	-20,782	-35,195	-49,446	-31,959
Scope-adjusted total assets	**211,630**	**295,259**	**380,454**	**398,914**	**542,741**
Scope-adjusted debt (EUR '000s)	**2019**	**2020**	**2021**	**2022E**	**2023E**
Reported gross debt	110,114	148,200	218,283	207,746	256,746
Cash and equivalents	-20,933	-20,782	-35,195	-49,446	-31,959
Scope-adjusted debt (SaD)	**89,181**	**127,418**	**183,088**	**158,300**	**224,787**

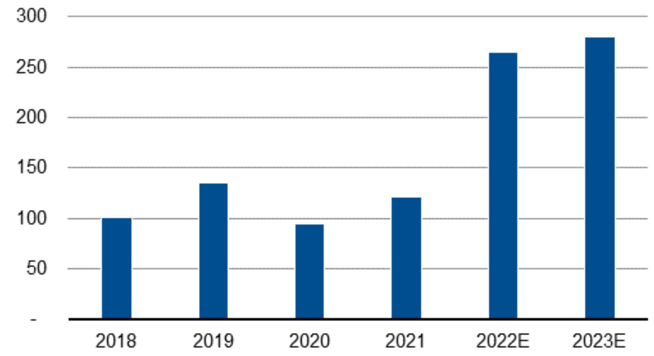
Business risk profile: BB-

Industry risk of B+ reflects exposure to volatile commercial development activity

82% of MG Real Estate's development pipeline is devoted to commercial real estate development (industry risk: B) and 18% to residential development (industry risk: BB). We therefore assign the company a blended industry risk score of B+. Commercial real estate development is characterised by high cyclicality, whereas residential development is medium. Entry barriers are medium and substitution risk is low for both sectors.

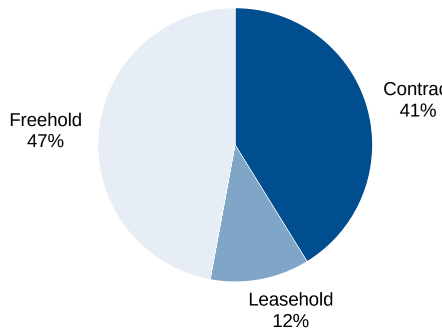
MG Real Estate's business risk profile assessment therefore reflects the high industry risk for real estate development as well as the company's relatively small size, balanced by a strong developer track record, a conservative approach to development risk, high asset quality and a large, secured pipeline.

Figure 1: GLA delivered (sqm thousand)



Sources: MG Real Estate, Scope estimates

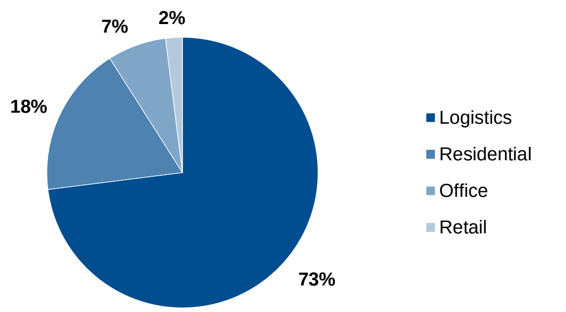
Figure 2: EUR 2.6bn development pipeline



Sources: MG Real Estate, Scope

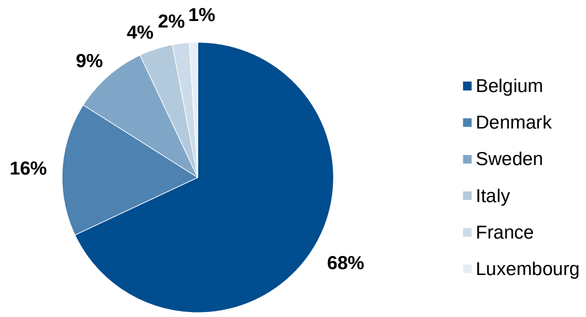
MG Real Estate is one of the top logistics real estate developers in its home market of Belgium (68% of development pipeline). Since 2015 it has also expanded into other European countries, notably Denmark (16%) and Sweden (9%) (see Figure 4). We see this geographic expansion as credit positive, since it has been carried out in a measured way and without excessive risk taking. The company also develops residential real estate in Belgium (18% of development pipeline), which adds some diversification and stability (see Figure 3).

Figure 3: Development pipeline by category (GLA), 2021



Sources: MG Real Estate, Scope

Figure 4: Development pipeline by country (GLA), 2021



Sources: MG Real Estate, Scope

Development risk mitigated by pre-lets and pre-sales

MG Real Estate's relatively small size results in high cash flow volatility and concentration risk. However, this is partially mitigated by the fact that the development pipeline is diverse for a company of its size, with 16 assets currently under construction, largely pre-let or pre-sold to tenants and investors with a good credit standing. Around 75% of developments scheduled for completion in 2022 and 70% of those scheduled for completion in 2023 are either pre-let or pre-sold, significantly mitigating development risk.

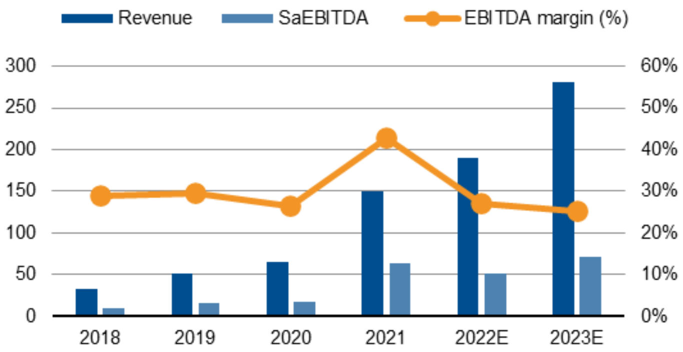
Strong demand for logistics real estate in Europe reflected in revenue and earnings growth

This reflects the very strong demand and shortage of supply for logistics real estate in Europe, fuelled by the rise in e-commerce and supply chain optimization. MG Real Estate is well positioned to benefit from this with a pipeline of around 1.0m sqm of logistics real estate secured by a land bank (freehold, leasehold and contract). Approximately 70% of the EUR 2.6bn pipeline (estimated exit value) is subject to planning permission.

High asset quality reflected in above-average rent and very long leases

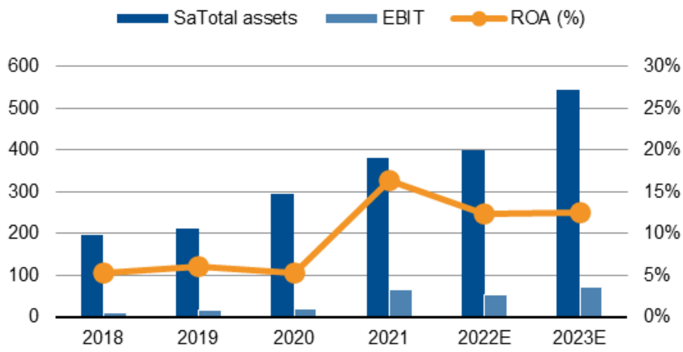
MG Real Estate's developments are generally of a high quality, commanding above-average rent and benefitting from very long (15+ year) leases. The company is a pioneer in the field of developing sustainable logistics buildings, an important competitive strength, having developed Belgium's first carbon neutral logistics building in 2021.

Figure 5: Scope-adjusted revenue (EUR m) and Scope-adjusted EBITDA margin (%)



Sa = Scope-adjusted; Sources: MG Real Estate, Scope estimates

Figure 6: Scope-adjusted total assets (EUR m) and return on assets (%)



Sa = Scope-adjusted; Sources: MG Real Estate, Scope estimates

The company grew rapidly in 2021 with revenues up by 129% to EUR 150m (see Figure 5) and the Scope-adjusted EBITDA margin rising to 42.9% (2020: 26.5%). We expect revenue growth to continue in 2022 and 2023 based on the company's large development pipeline, which indicates that completed GLA will rise to a level of over 250,000 sqm p.a. from 2022.

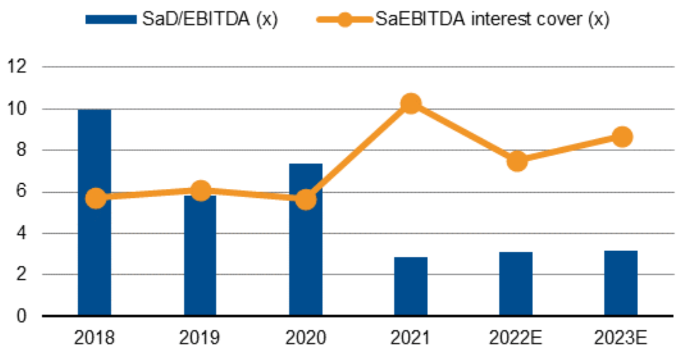
We have made more conservative assumptions for margins in 2022 and 2023, since rent increases and yield contractions may slow down going forward, and rising inflation may dent profitability.

Financial risk profile: BBB-

Leverage expected to remain moderate at around 3x in 2022 and 2023

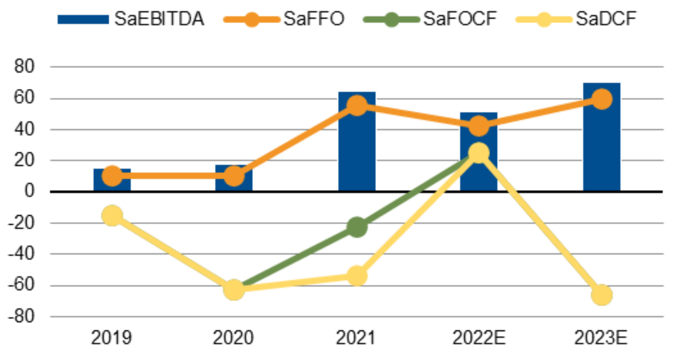
MG Real Estate's financial risk profile reflects moderate financial leverage with SaD/Scope-adjusted EBITDA of 2.8x at YE 2021 and Scope-adjusted EBITDA interest coverage of 10.3x (see Figure 7). Although the company has operated with much higher leverage in the past and experienced significant cash flow volatility, we expect leverage and debt service coverage metrics to remain around these levels for the next two years as MG Real Estate executes its pipeline of largely pre-let and pre-sold properties. The timing of development handovers, rapidly rising inflation and working capital fluctuations could still cause volatility, however (see Figure 8).

Figure 7: Scope-adjusted leverage and interest cover



Sa = Scope-adjusted; Sources: MG Real Estate, Scope estimates

Figure 8: Scope-adjusted EBITDA and cash flow (EUR m)

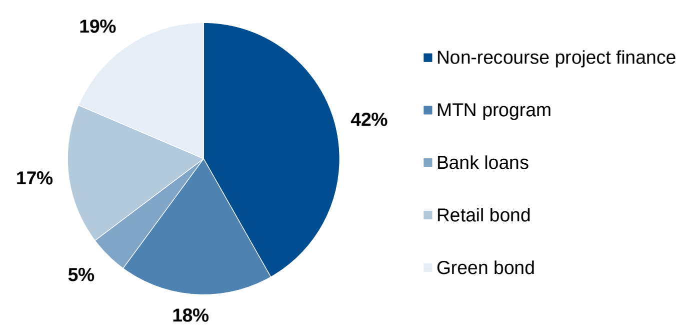


Sa = Scope-adjusted; Sources: MG Real Estate, Scope estimates

We do not expect any M&A or shareholder distributions for the foreseeable future, after a one-off dividend payment in 2021. However, we do expect MG Real Estate to continue to invest in its land bank to maintain production at the current level and to facilitate geographic expansion. This will likely result in higher absolute debt levels, but we do not expect higher leverage metrics.

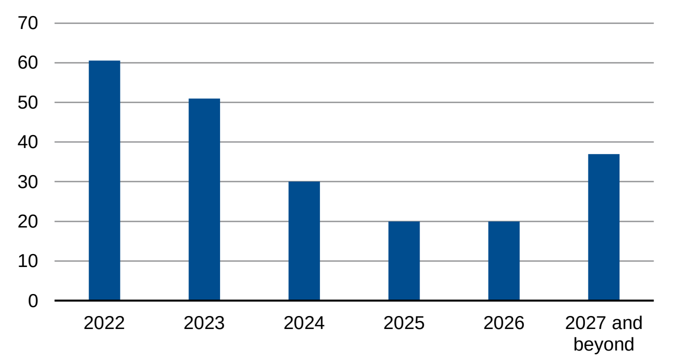
About half of debt is floating (bank loans), exposing the company to interest rate risk (see Figure 9). MG Real Estate is a frequent bond issuer and plans to issue its first green bond of EUR 50m in 2022. The bond should help to reduce interest rate risk and term out the debt maturity profile further (see Figure 10).

Figure 9: Sources of capital, pro forma of green bond



Sources: MG Real Estate, Scope

Figure 10: Debt maturity profile, YE 2021 (EUR m)



Sources: MG Real Estate, Scope

Liquidity is adequate. It is supported by the company policy of maintaining at least EUR 20m of cash balances (EUR 35m at YE 2021) as well as EUR 35m of long-term committed credit lines (of which EUR 7.5m were utilised at YE 2021), compared to short-term debt of EUR 61m. MG Real Estate also had EUR 147m of unencumbered real estate (land and projects under development) at YE 2021 that can be used as collateral for external financing. Development expenditures are 60%-80% financed by secured bank loans at the SPV level, largely covering associated cash outflow.

Figure 11: Liquidity

in EUR '000s	2022E	2023E
Short-term debt (t-1)	60,537	51,000
Unrestricted cash (t-1)	35,195	49,446
Committed credit lines (t-1)	27,500	25,000
Scope-adjusted free operating cash flow (t)	24,788	-66,488
Coverage	1.5x	0.2x

Sources: MG Real Estate, Scope estimates

Supplementary rating drivers

Supplementary rating drivers have a neutral impact on the ratings. As a private company owned and directed by a single individual, MG Real Estate is subject to key man risk [ESG factor: credit negative], reflected in our assessment of the company's business risk profile. This risk is partially mitigated by a competent senior management team.

Long-term debt rating

Bank lenders have a priority claim on active developments

About half of debt is accounted for by secured development loans at SPV level. The other half comprises unsecured bonds and bank loans at the holding company level (MG RE Invest S.A.). The company plans to issue a EUR 50m senior unsecured corporate green bond in 2022.

Senior unsecured debt rating: BB

Our recovery analysis is based on a hypothetical default scenario at year-end 2023 and assumes a liquidation of the business. This scenario results in an average (30%-50%) recovery rate for senior unsecured debt, which is legally and structurally subordinated to the development loans. Unencumbered assets covered unsecured debt by about 1.7x at YE2021. This assessment translates into a BB rating for senior unsecured debt, at the same level as the issuer rating.

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