Fitch Ratings

19 MAY 2021

Fitch Assigns Akropolis Group, UAB First-Time 'BB+' IDR; Outlook Stable

Fitch Ratings - Stockholm - 19 May 2021: Fitch Ratings has assigned Baltics-focused retail property company Akropolis Group, UAB a first-time Long-Term Issuer Default Rating (IDR) of 'BB+' with a Stable Outlook. Fitch has also assigned Akropolis' planned EUR300 million bond an expected 'BB+(EXP)' senior unsecured rating.

Akropolis' ratings are constrained by concentration on a limited number of assets, restricting asset and geographical diversification. The largest asset comprises above 40% of the group's portfolio. This asset concentration is expected to improve as assets are acquired and an ongoing development project completes in 2024.

The ratings also reflect a portfolio of four regionally dominant shopping centres in Lithuania (75% of market value) and Latvia (25%) and a conservative financial profile. Akropolis' shopping centres are anchored by Maxima Group, a Baltic leading grocery chain, and other tenants with a range of fashion and entertainment retail offers. The portfolio was valued at EUR0.8 billion at end-2020.

The assignment of the final rating is contingent on final documentation conforming to information already received.

Key Rating Drivers

Concentrated Portfolio: Akropolis' portfolio comprises four regional shopping centres. The largest one with 89,000 sqm of retail gross lettable area (GLA) and at 40% of the total portfolio market value (MV) is located in Vilnius (Lithuania). The second-largest centre (61,000 sqm, 25% MV) in Riga (Latvia) and two in Klaipeda (61,000 sqm, 25%) and Siaulai (36,000 sqm, 10%) which are the third- and fourth-most populous cities in Lithuania. Akropolis is negotiating the acquisition of another shopping centre in the the Baltic states and plans development of an over-136,000 sq m GLA mixed-use scheme in Vilnius.

Even including these two additions Akropolis will be one of the most concentrated property companies among EMEA Fitch-rated peers.

Strong Market Position: Akropolis' shopping centres benefit from high brand recognition as a result of a first-mover advantage of investing in shopping centres in Lithuania. Its conveniently-located shopping centres dominate their respective catchment areas, providing a wide retail offering. The centres are anchored by the largest food retailer in Baltics, Maxima Group (owned by Akropolis' parent company, UAB Vilniaus prekyba (VP Group)). Fashion sales are represented by a range of well-known international or regional brands. The fashion offering is complemented by food & beverage and entertainment segments encompassing cinemas and indoor ice-skating rinks.

High Tenant Concentration: The top-10 tenant groups generate over 40% of Akropolis' income, including 17% by VP Group-owned tenants. This is higher than Fitch-rated CEE peers' 20%. The comparatively small scale of local retail markets and demographic trends have not attracted many international retailers to enter the Baltics. This results in the retail market being dominated by a small number of regional companies operating own and/or franchised international brands.

Low E-commerce Penetration: Online sales penetration in the Baltics is lower than in other CEE and western European countries. It has allowed bricks-and-mortar retail to capture more of the region's consumption growth. In Lithuania and Latvia penetration ranged between 3.5% and 5% (in 2019) versus Romania's over 5%, Poland's 7%, and the Czech Republic's 15%. While e-commerce is gaining market share, accelerated by the pandemic-related social-distancing measures, each country's low population density is less conducive to exponential growth in this retail channel.

Manageable Coronavirus Impact: Non-essential stores in Latvia have remained closed since December 2020. In Lithuania they opened in April 2021. Akropolis reports that 74% of its GLA was fully operational in April. Even during 2020, Akropolis' operational performance remained solid with 91% rental collection (including granted discounts), high occupancy above 99% and a healthy occupancy cost ratio (OCR) at 12%.

Tenancy Contracts' Features: A distinctive feature of a substantial part (over 78% of rental income) of Akropolis' tenancy contracts is an annual inflation-linked rent indexation of a minimum 1%-3%. The assets' OCR and occupancy illustrate a sustainable profile. Even after past years of like-for-like average 3% annual rent increases, rent affordability is aided by tenants' sales growth reflecting strong local consumption that has been converging towards western European levels. As the Baltics are eurozone members tenant rents and Akropolis' cost base are denominated in euros, resulting in no exposure to currency risk.

Development Pipeline: Akropolis' Vingis development project will be located next to a popular city park in Vilnius, providing a natural entry point for park visitors. The first stage of the scheme is expected to be completed in 2024 with full rental income achieved in 2026 when the second phase is completed. Capex totals around EUR300 million. To reduce development risk management requires pre-lets and procurement of a fixed-price construction contract with a third-party general contractor.

Moderate Leverage: Akropolis' net debt/EBITDA of 4.4x at end-2020 reflects the company's high-yielding Baltics-located retail assets and a conservative 31% Fitch-adjusted loan-to-value (LTV). Cash flow leverage is expected to moderately increase to 6.3x in 2021 when management's potential property acquisition is completed (using annualised rents) and remain around this level until its development project is completed in 2024 when the ratio will settle at 5.6x. Interest cover remains over 6x due to strong cash flows and low interest rates.

Governance Structure Limitations: As part of the VP Group, Akropolis has benefitted from cooperation with VP Group-owned retailers who create a comprehensive retail proposition and coordinate retail offerings in its shopping centres. However, concentrated ownership by a privately-held group means financial disclosure and corporate governance are not comparable to listed companies'. Indirect 77% ownership by dominant shareholder Nerijus Numa, together with the lack of independent directors on Akropolis' board, means that the arm's length nature of related-party transactions (with Maxima Group and sister tenants) does not have independent oversight.

Derivation Summary

Akropolis' EUR0.8 billion portfolio, comprising four shopping centres located in Lithuania (A/Stable) and Latvia (A-/Stable), is smaller and materially more concentrated than the EUR5.8 billion CEE retail portfolio owned by NEPI Rockcastle plc (BBB/Stable). Atrium European Real Estate Limited's (BBB/Stable) has a CEE retail portfolio of EUR2.5 billion, which is similar in size to the EUR2.4 billion office portfolio of Globalworth Real Estate Limited (BBB-/Stable).

Akropolis' country risk exposure is comparable to that of Atrium where assets are in 'A-' or above-rated countries except for 10% of the portfolio (by value), which is located in Russia (BBB/Stable). NEPI has the highest diversification with a presence in nine CEE countries but the average country risk is lower and similar to that exhibited by Globalworth, whose office assets are almost equally split between Poland (A-/Stable) and Romania (BBB-/Negative).

Akropolis' end-2020 net debt/EBITDA at 4.4x was the lowest among all CEE Fitch-rated peers. This is partly because Akropolis has the highest income-yielding assets with a net initial yield estimated at around 7.5% (adjusted for rent lost to Covid 19-related rent discounts) and the lowest LTV at 31%. This net debt/EBITDA is most comparable to NEPI's around 6x. NEPI's financial profile is stronger than Atrium's and Globalworth's.

Key Assumptions

Fitch's Key Assumptions Within Our Rating Case for the Issuer

- Given the extended effect of the pandemic and related tightening of social-distancing measures including essential shops closures, for 2021 rents we assume (i) two months of lost rent (adjusted to reflect Akropolis' share of essential stores) and (i) a 5% decrease in rents on scheduled lease renewals

- Increasing vacancy rate to 4% in 2024

- Sizable property acquisition completed in 2021 based on details provided by management

- Over EUR250 million of capex (including Vingis' development spend) during forecast horizon until 2024

- No dividends paid for the next four years

RATING SENSITIVITIES

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

- Expansion of the portfolio in less correlated markets while maintaining portfolio quality

- Unencumbered asset/unsecured debt cover above 2.0x

- Net debt/EBITDA below 8.5x

- Consistent interest-rate hedging policy

- Improved corporate governance

- Under Fitch's Parent and Subsidiary Rating Linkage Criteria, assuming a moderate to strong linkage, VP Group's credit profile would need to be investment-grade for an upgrade of Akropolis to investment-grade.

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

- Net debt/EBITDA above 9.0x and LTV trending above 55%

- Unencumbered asset/unsecured debt cover below 1.75x

- Failure to complete the Vingis development as per schedule and/or materially outside the assumed budget

- Liquidity score below 1.0x

- Transactions with related-parties that are detrimental to Akropolis' interest.

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

Adequate Liquidity: Pro-forma for the planned EUR300 million bond, partial repayment of bank loans and completion of the potential property acquisition, Akropolis's cash is sufficient to cover an EUR5 million loan amortisation in 2021. Akropolis does not use committed revolving credit facilities as a contingent source of liquidity.

Using the bond proceeds to partially prepay secured bank loans, three Akropolis' assets will become unencumbered. Assuming successful closing of the potential property acquisition, Fitch calculates that the total value of unencumbered assets/unsecured debt will be 2.5x.

Akropolis is not a REIT so it is not constrained by dividend distribution requirements. Fitch interprets its internal dividend policy to mean no dividends when material outlays related to the development programme or acquisitions are expected, or would cause the company's reported LTV to be above 45%. No dividends during the rating horizon (until 2024) will allow Akropolis to retain free cashflow to finance the development of Vingis shopping centre.

ESG Considerations

Akropolis has an ESG Relevance Score of '4' for Governance Structure reflecting the lack of corporate governance attributes that would both mitigate key person risk from the dominant shareholder Nerijus Numa and assure independent oversight of related-party transactions. This has a negative impact on the credit profile, and is relevant to the ratings in conjunction with other factors.

Unless stated otherwise above the highest level of ESG credit relevance is a score of 3 - 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 company. For more information on Fitch's ESG Relevance Scores, visit www.fitchratings.com/esg.

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.

Fitch Ratings Analysts

Fredric Liljestrand
Director
Primary Rating Analyst
+46 85510 9441
Fitch Ratings Ireland Nordic Region Filial Kungsgatan 8 Stockholm 111 43

Pawel Jagiello
Associate Director
Secondary Rating Analyst
+48 22 330 6707

John Hatton
Managing Director

Committee Chairperson
+44 20 3530 1061

Media Contacts

Adrian Simpson
London
+44 20 3530 1010
adrian.simpson@thefitchgroup.com

Rating Actions

ENTITY/DEBT	RATING			RECOVERY	PRIOR
AKROPOLIS GROUP, UAB	LT IDR	BB+ (Stable)	New Rating		
• senior unsecured	LT	BB+(EXP)	Expected Rating		

RATINGS KEY	OUTLOOK	WATCH
POSITIVE	⊕	⬘
NEGATIVE	⊖	⬙
EVOLVING	⦿	◆
STABLE	⊙	

Applicable Criteria

Corporate Rating Criteria (pub.21 Dec 2020) (including rating assumption sensitivity)

Corporates Recovery Ratings and Instrument Ratings Criteria (pub.09 Apr 2021) (including rating assumption sensitivity)

Parent and Subsidiary Linkage Rating Criteria (pub.26 Aug 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

Solicitation Status

Endorsement Status

Disclaimer

Copyright

jurisdiction. The manner of Fitch's factual investigation and the scope of the third-party verification it obtains will vary depending on the nature of the rated security and its issuer, the requirements and practices in the jurisdiction in which the rated security is offered and sold and/or the issuer is located, the availability and nature of relevant public information, access to the management of the issuer and its advisers, the availability of pre-existing third-party verifications such as audit reports, agreed-upon procedures letters, appraisals, actuarial reports, engineering reports, legal opinions and other reports provided by third parties, the availability of independent and competent third- party verification sources with respect to the particular security or in the particular jurisdiction of the issuer, and a variety of other factors. Users of Fitch's ratings and reports should understand that neither an enhanced factual investigation nor any third-party verification can ensure that all of the information Fitch relies on in connection with a rating or a report will be accurate and complete. Ultimately, the issuer and its advisers are responsible for the accuracy of the information they provide to Fitch and to the market in offering documents and other reports. In issuing its ratings and its reports, Fitch must rely on the work of experts, including independent auditors with respect to financial statements and attorneys with respect to legal and tax matters. Further, ratings and forecasts of financial and other information are inherently forward-looking and embody assumptions and predictions about future events that by their nature cannot be verified as facts. As a result, despite any verification of current facts, ratings and forecasts can be affected by future events or conditions that were not anticipated at the time a rating or forecast was issued or affirmed.

The information in this report is provided "as is" without any representation or warranty of any kind, and Fitch does not represent or warrant that the report or any of its contents will meet any of the requirements of a recipient of the report. A Fitch rating is an opinion as to the creditworthiness of a security. This opinion and reports made by Fitch are based on established criteria and methodologies that Fitch is continuously evaluating and updating. Therefore, ratings and reports are the collective work product of Fitch and no individual, or group of individuals, is solely responsible for a rating or a report. The rating does not address the risk of loss due to risks other than credit risk, unless such risk is specifically mentioned. Fitch is not engaged in the offer or sale of any security. All Fitch reports have shared authorship. Individuals identified in a Fitch report were involved in, but are not solely responsible for, the opinions stated therein. The individuals are named for contact purposes only. A report providing a Fitch rating is neither a prospectus nor a substitute for the information assembled, verified and presented to investors by the issuer and its agents in connection with the sale of the securities. Ratings may be changed or withdrawn at any time for any reason in the sole discretion of Fitch. Fitch does not provide investment advice of any sort. Ratings are not a recommendation to buy, sell, or hold any security. Ratings do not comment on the adequacy of market price, the suitability of any security for a particular investor, or the tax-exempt nature or taxability of payments made in respect to any security. Fitch receives fees from issuers, insurers, guarantors, other obligors, and underwriters for rating securities. Such fees generally vary from US$1,000 to US$750,000 (or the applicable currency equivalent) per issue. In certain cases, Fitch will rate all or a number of issues issued by a particular issuer, or insured or guaranteed by a particular insurer or guarantor, for a single annual fee. Such fees are expected to vary from US$10,000 to US$1,500,000 (or the applicable currency equivalent). The assignment, publication, or dissemination of a rating by Fitch shall not constitute a consent by Fitch to use its name as an expert in connection with any registration statement filed under the United States securities laws, the Financial Services and Markets Act of 2000 of the United

Kingdom, or the securities laws of any particular jurisdiction. Due to the relative efficiency of electronic publishing and distribution, Fitch research may be available to electronic subscribers up to three days earlier than to print subscribers.
For Australia, New Zealand, Taiwan and South Korea only: Fitch Australia Pty Ltd holds an Australian financial services license (AFS license no. 337123) which authorizes it to provide credit ratings to wholesale clients only. Credit ratings information published by Fitch is not intended to be used by persons who are retail clients within the meaning of the Corporations Act 2001
Fitch Ratings, Inc. is registered with the U.S. Securities and Exchange Commission as a Nationally Recognized Statistical Rating Organization (the "NRSRO"). While certain of the NRSRO's credit rating subsidiaries are listed on Item 3 of Form NRSRO and as such are authorized to issue credit ratings on behalf of the NRSRO (see https://www.fitchratings.com/site/regulatory), other credit rating subsidiaries are not listed on Form NRSRO (the "non-NRSROs") and therefore credit ratings issued by those subsidiaries are not issued on behalf of the NRSRO. However, non-NRSRO personnel may participate in determining credit ratings issued by or on behalf of the NRSRO.

Endorsement policy

Fitch's international credit ratings produced outside the EU or the UK, as the case may be, are endorsed for use by regulated entities within the EU or the UK, respectively, for regulatory purposes, pursuant to the terms of the EU CRA Regulation or the UK Credit Rating Agencies (Amendment etc.) (EU Exit) Regulations 2019, as the case may be. Fitch's approach to endorsement in the EU and the UK can be found on Fitch's Regulatory Affairs page on Fitch's website. The endorsement status of international credit ratings is provided within the entity summary page for each rated entity and in the transaction detail pages for structured finance transactions on the Fitch website. These disclosures are updated on a daily basis.