

Research Update:

Swedish Housing Company Stockholms Kooperativa Bostadsforening 'AA-/A-1+' And 'K-1' Ratings Affirmed; Outlook Stable

May 20, 2019

Overview

- In our view, Stockholms Kooperativa Bostadsforening's (SKB's) enterprise profile remains supported by the strength of Stockholm's economy and high demand for property in the region.
- In the coming years, we expect SKB's debt, which it amortized in 2018, will rise as investments increase.
- We are affirming our 'AA-/A-1+' and 'K-1' ratings on SKB.
- The stable outlook reflects our expectation that SKB will maintain its budgetary performance and liquidity position, despite higher debt to fund increasing investments.

Rating Action

On May 20, 2019, S&P Global Ratings affirmed its 'AA-' long-term and 'A-1+' short-term issuer credit ratings on Swedish public-sector housing company Stockholms Kooperativa Bostadsforening (SKB). The outlook is stable.

At the same time, we affirmed our 'K-1' Nordic regional scale rating on SKB.

Rationale

We view SKB as a public housing entity, based on its not-for-profit mission, guidelines and principles for setting rent, and targeted tenant clientele. SKB has a strong market position, with well-maintained and attractive properties mainly located in Stockholm, which has a wealthy economy. Strong population growth in the city continues to fuel housing demand, with scarce supply supporting demand for SKB's housing units. SKB has no vacancies. SKB's plan to expand into the neighboring Uppsala region does not change our view of the company's enterprise risk. If the plan is successful, it might open up further opportunities for SKB to widen its regional scope. Furthermore, SKB's market position is enhanced by its solid strategy and prudent management, in

PRIMARY CREDIT ANALYST

Dennis Nilsson
Stockholm
(46) 8-440-5354
dennis.nilsson
@spglobal.com

SECONDARY CONTACT

Carl Nynerod
Stockholm
(46) 8-440-5919
carl.nynerod
@spglobal.com

ADDITIONAL CONTACT

EMEA Sovereign and IPF
SovereignIPF
@spglobal.com

our view.

SKB's financial profile benefits from its strong debt position and robust financial performance, with no legal limits on rent-setting allowing for greater flexibility than peers to adjust revenues. In addition, capital from members' deposits and compulsory member savings provide predictable cash flow. Nevertheless, we consider that SKB's creditworthiness is constrained by its management's policy of maintaining moderate liquidity.

SKB currently has 90,000 members, including existing tenants and those on a waiting list. SKB had 8,000 rental apartments at year-end 2018, implying that about 82,000 members are on the waiting list. Although a high share of people on the list are not actively seeking housing, active members on the waiting list are supporting high demand. SKB benefits from low competition and low cyclicalities, features of Sweden's public housing sector. Although SKB's members are free to leave the association and withdraw their savings at any time, we see no material risk of this happening in the foreseeable future, given the ongoing high demand for rental apartments in and around Stockholm and historical patterns during SKB's long history.

We assess SKB's management and governance as very strong, with a focused strategy, prudent planning, and comprehensive risk-management practices, showcased through a conservative and consistent approach to risks in the debt portfolio and development of new properties. SKB has taken steps to potentially acquire leasehold land from the city of Stockholm, which could be positive for the company over the long term. This step supports SKB's long-term planning and strategy, but could weaken its financial ratios in the short term depending on whether the transaction goes ahead and the costs associated with it.

SKB has a strong balance sheet, enhanced by its ability to raise rent and delay maintenance if needed, and sound access to funding from multilateral lending institutions, banks, and the capital market. In our base-case scenario for 2019-2021, we forecast the association's EBITDA-to-revenue margin at a sound 37%. Since we also consider SKB's properties to be well maintained, we believe the association could delay a good portion of its yearly maintenance costs if necessary without affecting rental demand. In addition, we regard as positive that SKB operates under special legislation allowing it the right to increase rents above the benchmark rates for public- and private-sector landlords.

Operating cash flows comfortably service SKB's debt. We forecast EBITDA interest coverage at a strong 5x in our base-case scenario for 2019-2021. In contrast to our previous base case, we now think SKB will ramp up investment levels and therefore need to increase its debt by a total Swedish krona (SEK) 500 million (\$52 million) until year-end 2021. Importantly, SKB reports properties on its balance sheet at historical cost less depreciation, which implies significant surplus values in its property portfolio. An internal property appraisal places SKB's loan-to-value ratio at a robust 13% at year-end 2018, suggesting substantial additional debt capacity and liquidity potential through unencumbered assets. In our view, risk tolerances and financial policies regarding the share of fixed-rate debt, have a minimal impact on the association's credit standing, considering its very low leverage.

Liquidity

The short-term rating is 'A-1+'. We still regard SKB's liquidity position as adequate, owing to its moderate internal cash flow generation, committed bank facilities that mitigate refinancing risk, and demonstrated strong market access.

We estimate that SKB will refinance approximately SEK2.0 billion in loans over the next 12 months. In addition, we estimate SKB's yearly capital expenditure (capex) at about SEK520 million

on average over 2019-2021. We include SEK90 million of expected capital revenues from compulsory member savings and deposits as an extraordinary source of financing for capex over the coming 12 months.

SKB currently has committed liquidity facilities totaling SEK2 billion to mitigate refinancing risks associated with short-term debt maturities. Together with a checking account containing SEK50 million and our base-case assumption of funds from operations of SEK274 million, we calculate that the association has available liquidity, including committed bank facilities, amounting to 108% of debt service and committed capital spending over the next 12 months.

Outlook

The outlook is stable because we expect strong demand and financial flexibility will help SKB fund its development and mitigate risks associated with its moderate liquidity position. We do not foresee any material changes in Sweden's legal framework governing cooperative housing.

We could raise the ratings if SKB's financial risk profile strengthened, for example, owing to improved profitability and liquidity metrics, reflected in a liquidity coverage ratio sustainably higher than 1.25x.

Conversely, the ratings could come under pressure if SKB's financial management led to a surge in leverage materially beyond our base-case projections and also constrained liquidity.

Key Statistics

Table 1

Stockholms Kooperativa Bostadsforening Selected Indicators

	2017	2018	2019bc	2020bc	2021bc
Vacancy rates (% of net rental income)	0.1	0.1	0.1	0.1	0.1
Revenue	747.4	765.1	780.0	796.3	837.8
EBITDA	290.3	296.4	267.0	282.3	313.8
EBITDA/revenue (%)	38.8	38.7	34.2	35.5	37.5
Interest expense	64.4	54.1	50.0	51.7	55.9
Debt/EBITDA (x)	10.3	9.9	11.0	11.1	10.9
EBITDA/interest coverage (x)	4.5	5.5	5.3	5.5	5.6
Capital expense	282	232	217	231	258
Debt	2,993	2,942	2,939	3,143	3,433
Housing properties (according to balance-sheet valuation)	6,129	6,256	6,360	6,681	7,112
Cash and liquid assets	56.2	74.2	67.7	80.6	84.1

The data and ratios above result in part from S&P Global Ratings' own calculations. The main sources are the financial statements and budgets, as provided by the issuer. SEK--Swedish krona. bc--Base case, reflects S&P Global Ratings' expectations of the most likely scenario.

Ratings Score Snapshot

Table 2

Stockholms Kooperativa Bostadsforening Ratings Score Snapshot

Key rating factors	Score
Industry risk	2
Economic fundamentals and market dependencies	1
Strategy and management	1
Asset quality and operational performance	1
Enterprise profile	2
Financial performance	2
Debt profile	2
Liquidity	3
Financial policies	1
Financial profile	2

S&P Global Ratings' analysis of social housing providers' creditworthiness rests on our scoring of eight key rating factors: (i) industry risk; (ii) economic fundamentals and market dependencies; (iii) strategy and management; (iv) asset quality; (v) financial performance; (vi) debt profile; (vii) liquidity; and (viii) financial policies. Each of the factors is assessed on a continuum spanning from 1 (strongest) to 6 (weakest). S&P Global Ratings' "Methodology For Rating Public And Nonprofit Social Housing Providers," published Dec. 17, 2014, and "Rating Government-Related Entities: Methodology And Assumptions," published March 25, 2015, detail how we derive and combine the scores, and then determine each social housing provider's stand-alone credit profile and the issuer credit rating. In accordance with S&P Global Ratings' public and nonprofit social housing providers methodology, a change in score does not in all cases lead to a change in the rating, nor is a change in the rating necessarily predicated on changes in one or more of the scores. In determining the final rating, the committee can make use of the flexibility afforded by paragraphs 12-17 of "Methodology For Rating Public And Nonprofit Social Housing Providers."

Related Criteria

- General Criteria: Methodology For Linking Long-Term And Short-Term Ratings, April 7, 2017
- Criteria | Governments | General: Methodology For Rating Public And Nonprofit Social Housing Providers, Dec. 17, 2014
- General Criteria: Stand-Alone Credit Profiles: One Component Of A Rating, Oct. 1, 2010
- General Criteria: Use Of CreditWatch And Outlooks, Sept. 14, 2009

Ratings List

Ratings Affirmed

Stockholms Kooperativa Bostadsforening

Issuer Credit Rating AA-/Stable/A-1+

Nordic Regional Scale --/--/K-1

Certain terms used in this report, particularly certain adjectives used to express our view on rating relevant factors, have specific meanings ascribed to them in our criteria, and should therefore be read in conjunction with such criteria. Please see Ratings Criteria at www.standardandpoors.com for further information. Complete ratings

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