S&P Global Ratings

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Research Update:

German Public Housing Provider Gewoba Aktiengesellschaft Wohnen und Bauen Ratings Affirmed At 'A/A-1'; Outlook Stable

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Overview

- We have slightly lowered our expectations of Gewoba Aktiengesellschaft Wohnen und Bauen's (Gewoba) average investments over the next two years.
- We believe management will maintain a solid investment pipeline averaging around €145 million per year between 2024 and 2026, requiring continued borrowing.
- Gewoba has secured additional funding for construction, which has improved its liquidity position.
- We affirmed our 'A/A-1' long- and short-term issuer credit ratings on Gewoba. The outlook remains stable.

Rating Action

On July 22, 2024, S&P Global Ratings affirmed its 'A/A-1' long- and short-term issuer credit ratings on Gewoba Aktiengesellschaft Wohnen und Bauen (Gewoba). The outlook remains stable.

Outlook

The stable outlook reflects our view that Gewoba's management will continue to mitigate the impact of cost pressure on the company's financial metrics and retain solid margins in its core letting business, underpinned by strong market demand.

Downside scenario

We could lower the ratings if the company accelerates its investment spending resulting in a materially higher debt burden. We could also take this action if margins weaken substantially due to lack of cost control.

Upside scenario

We could raise the ratings if debt to non-sales adjusted EBITDA were to stabilize below 10x. This could result from management continually spreading out its investment spend to contain debt accumulation.

Rationale

We think Gewoba's recent strategic review with its government owner has somewhat eased pressure on the entity's investment spend and reduced our expectation of debt buildup in the near term. Both parties agreed on a more balanced approach between investments on existing properties related to climate goals, and new development spend. We nonetheless expect Gewoba's debt burden will continue to rise and see risks emanating from potential funding needs outside our forecast horizon, once the interest rate environment improves.

Gewoba has been pre-funding for its anticipated investment pipeline, including a new European Investment Bank (EIB) line, which has improved its liquidity position.

In our view, Gewoba's management will be able to protect the company's strong financial performance and balance sheet through adequate cost efficiency measures. Even though solid demand dynamics give room for sound rental increases across the portfolio, we expect margins will continue to weaken as cost pressure and investments related to improving existing properties' energy efficiency persist.

Enterprise profile: Strategic review has reduced uncertainty around Gewaba's investment plan.

Gewoba, which owns almost 43,000 units, is the German city of Bremen's leading public housing provider and benefits from strong demand. It also has sizable activities in the nearby towns of Bremerhaven and Oldenburg. Our ratings on the company are underpinned by its almost exclusive focus on traditional residential letting activities. We assess the inherent industry risk of Gewoba's operations as low. The company pursues a narrowly defined mission--codified in the articles of association--to provide adequate housing to large parts of society. This explicitly includes socially disadvantaged groups. Gewoba's auxiliary activities comprise a small utility subsidiary that provides metering services and small volumes of, mostly self-produced, heat and electricity. It has minimal development for sales activities.

We assess the regulatory framework under which German public housing providers such as Gewoba operate as strong (see "Regulatory Framework Assessment: German Public Housing Providers Face Increasing Political Demands But Benefit From Strong Institutions," published Oct. 3, 2023, on RatingsDirect).

We understand Gewoba's recent strategic review process involving its majority owner, the city-state of Bremen, has not altered the company's overarching strategic direction, while including climate targets and reducing the investment pipeline. In this context, required future climate spending partially replaces spending on new construction but, in our view, refurbished units will generate less additional rental income than new ones. All investments regardless of type have to meet internal affordability requirements, which we think allows management to maintain strong financial metrics. Similarly, the purchase of existing housing stock--while high on the political agenda to increase the number of affordable assets under government control--will only be undertaken if commercially viable. We consider the company's plans are realistic and executed with attention to detail, including formalized risk management and financial policies.

There is strong demand for Gewoba's properties. On average, Gewoba charged €6.64 per square meter at year-end 2023, about 10% below our estimate for the weighted-average in-place market rent in its area of operation. Helped by the housing needs of Ukrainian refugees, vacancies across its entire asset base amount to only 0.5%, somewhat below former levels of around 1%. This compares favorably with a reported market void rate of 2.0%-3.0% across the city-state of Bremen and is in line with German public housing provider peers.

Financial profile: Margin softening expected to continue, while debt accumulation persists at a slower pace.

We expect inflationary cost pressure will weaken Gewoba's financial performance but believe the company can and has the potential to maintain adjusted EBITDA margins above 30%. Elevated prices for construction, repairs, and maintenance represent clear challenges for the company, with personnel spending also rising in 2024 and beyond. We understand that management is proactively addressing these adverse developments, for example by bringing services back inhouse and replacing general contractors with more competitively sourced individual construction services. Furthermore, the company has reduced the budget for large-scale maintenance to reduce cost.

On the revenue side we think Gewoba has sufficient headroom to support healthy margins. Following the publication of the most recent and first-time so-called "qualified" rent index for Bremen, rent levels for Gewoba appear slightly closer to market than previously estimated. We think this does not reduce its scope for rent increase as they are, on average, still below market.

We expect Gewoba's debt will increase modestly from a low base while maintaining very strong interest coverage, despite relatively high interest rates. Debt issuance in 2023 was below our prior expectation on lower capital spend. Capital projects in our forecast comprise new construction projects that are either already started or in an advanced planning stage. We note that Gewoba has resumed further investment planning for the period outside our current forecast horizon following adjustments to the Housing Promotion Act. However, we currently still expect annual average capex of €145 million over the next two to three years. Coupled with spending in existing stock, this implies about €255 million of additional debt by 2026, accumulating slower than previously anticipated. We believe capex could rise again requiring additional borrowing, should interest costs subside.

Gewoba extended the range of its funding instruments in recent years to manage interest costs. It issued a registered bond (Namensschuldverschreibung), agreed on EIB loan facilities, and is negotiating options with another supranational multilateral lender. Gewoba regularly borrows from commercial and promotional banks. The latter are particularly attractive, not least because Gewoba pays close to 0% interest on €60 million of loans currently sourced from Bremer Aufbaubank, Bremen's promotional lender. This, in part, explains the company's very strong non-sales EBITDA interest coverage. Gewoba recently also addressed interest rate reset risks for its commercial loans via forward contracts.

Gewoba displays a very strong liquidity position. The company has over €80 million of committed, yet to be drawn, long-term loans that it agreed mainly with the German federal promotional lender KfW. These loans--combined with roughly €140 million of revolving credit lines and a similar level of cash generated from continuing operations, alongside a recent EIB line of €125 million--resulted in the ratio of liquidity sources to uses increasing to 2x as of June 30, 2024. The main uses of liquidity over the coming 12 months are investments estimated at about €150 million and debt service of €65 million.

We evaluate Gewoba's access to external liquidity as satisfactory. This is based on the company's established presence in the private capital market and its reliable access to a diversified pool of commercial, promotional, and mortgage banks. Sufficient unencumbered assets facilitate borrowing from the latter.

Government-related entity analysis

We believe that there is a moderately high likelihood that Gewoba, as a government-related entity, would receive timely and sufficient extraordinary support from its 75% majority shareholder, the city-state of Bremen. However, the impact of such support is currently neutral on our ratings. We assess the link between Gewoba and Bremen as strong. This is demonstrated, for example, by the fact that the head of the state government's housing and urban development department is usually the chairman of Gewoba's supervisory board. Other government officials and state parliamentarians are ordinary members of the supervisory board. Considering that Gewoba effectively helps Bremen address its constitutional mandate to provide adequate housing, and the high significance this has on the political agenda, we assess the company's role as important.

Selected Indicators

Table 1

Gewoba--Financial statistics

	--Year ended Dec. 31--				
Mil. €	**2022A**	**2023A**	**2024BC**	**2025BC**	**2026BC**
Number of units owned or managed	43,088	43,276	43,402	43,672	43,856
Adjusted operating revenue	303.8	340.8	358.1	382.2	397.3
Adjusted EBITDA	116.8	121.6	119.7	125.6	130.9
Nonsales adjusted EBITDA	116.1	121.6	119.7	125.6	130.9
Capital expense	142.8	138.1	144.9	162.5	139.1
Debt	933	966	1045	1136	1201
Interest expense	10.7	11.6	12.3	16.5	19.8
Adjusted EBITDA/Adjusted operating revenue (%)	38.4	35.7	33.4	32.9	32.9
Debt/Nonsales adjusted EBITDA (x)	8.0	7.9	8.7	9.0	9.2
Nonsales adjusted EBITDA/interest coverage(x)	10.8	10.5	9.7	7.6	6.6

A--Actual. E--Estimate. BC--Base case reflects S&P Global Ratings' expectations of the most likely scenario.

Ratings Score Snapshot

Table 2

Gewoba--Ratings score snapshot

	Assessment
Enterprise risk profile	3
Industry risk	2
Regulatory framework	3
Market dependencies	3
Management and governance	3
Financial risk profile	2
Financial performance	3
Debt profile	2
Liquidity	2
Stand-alone credit profile	a
Issuer credit rating	a

S&P Global Ratings bases its ratings on nonprofit social housing providers on the seven main rating factors listed in the table above. Our "Methodology For Rating Public And Nonprofit Social Housing Providers," published on June 1, 2021, summarizes how the seven factors are combined to derive each social housing provider's stand-alone credit profile and issuer credit rating.

Related Criteria

- General Criteria: Environmental, Social, And Governance Principles In Credit Ratings, Oct. 10, 2021
- Criteria | Governments | General: Methodology For Rating Public And Nonprofit Social Housing Providers, June 1, 2021
- General Criteria: Methodology For Linking Long-Term And Short-Term Ratings, April 7, 2017
- General Criteria: Rating Government-Related Entities: Methodology And Assumptions, March 25, 2015
- General Criteria: Principles Of Credit Ratings, Feb. 16, 2011

Related Research

- Regulatory Framework Assessment: German Public Housing Providers Face Increasing Political Demands But Benefit From Strong Institutions, Oct. 3, 2023
- Non-U.S. Social Housing Sector Outlook 2024: At A Turning Point? Nov. 29, 2023
- Regulatory Framework And Systemic Support Assessments For Nonprofit Social Housing Providers, May 29, 2024
- Non-U.S. Social Housing Providers Ratings Score Snapshot: March 2024, Mar. 11, 2024
- Non-U.S. Social Housing Providers Ratings Risk Indicators: March 2024, Mar. 11, 2024
- Non-U.S. Social Housing Providers Ratings History: March 2024, Mar. 11, 2024

Ratings List

Ratings Affirmed	
Gewoba	
Issuer Credit Rating	A/Stable/A-1