

Studentbostäder i Norden AB (publ)

Rating Action Report

Studentbostäder i Norden AB (publ) long-term issuer rating lowered to 'CC'; Rating on Watch Negative

LONG-TERM RATING

CC

Watch Negative

SHORT-TERM RATING

N6

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Nordic Credit Rating (NCR) said today that it had lowered its long-term issuer rating on Sweden-based residential property manager [Studentbostäder i Norden AB \(publ\)](#) to 'CC' from 'CCC'. At the same time, the short-term rating was affirmed at 'N6'. Given the increasing likelihood of a covenant breach and distressed exchange on the company's outstanding bond, as well as the company's weak liquidity, we have extended our Watch Negative placement on the ratings reflecting a material risk for a distressed exchange over the next three to four months.

Rating rationale

The downgrade of the long-term rating reflects the decreasing likelihood that Studentbostäder will avoid a covenant breach on its outstanding SEK 564m senior unsecured bond, maturing on 14 May 2024, as well as doubts over the company's ability to repay the bond at maturity. While there are ways for the company to avoid a default on the bond, we believe the most likely resolution is through a distressed exchange in the near term, accelerated by the imminent covenant breach. In addition, the company remains under significant liquidity pressure.

By our definition, a 'CC' issuer rating represents a high likelihood of a conventional default or a distressed exchange within the next 12 months. A change of terms qualifies as a distressed exchange when the amended terms result in lower value to bondholders than the original terms and is carried out to avoid a near-term default. Although we do not specifically rate Studentbostäder's senior unsecured bonds, a default on the bond would result in a long-term issuer rating of 'SD' to reflect a selective default on the bond, as long as the company fulfils its other commitments. NCR would not consider a covenant breach or a covenant waiver, on their own, as a default on the bond.

The maintenance covenant on Studentbostäder's outstanding bond stipulates an interest coverage ratio (ICR) above 1.5x. At 30 Jun. 2023 the covenant-defined ICR was 1.52x, compared with our adjusted calculation of 1.3x (rolling 12 months), or 1.21x in the quarter. In addition, Studentbostäder has an equity ratio covenant of 20% on the outstanding bond. At 30 Jun. 2023, the equity ratio was 25.4%. While there is some headroom under the covenant, we believe it could be at risk if property valuations continue to fall in line with our expectations (-16% for the full year 2023). We consider the risk of breaching the ICR covenant is imminent, however, as recent interest rate hikes take effect. According to the bond terms, a covenant breach is cause for immediate repayment. Given the low likelihood of interest coverage and repayment risk improving in the near term, in our view, negotiations with bond investors are likely to result in a distressed exchange. Consequently, failure to negotiate a distressed exchange would imply not only a default on the bond but also a very serious situation for the company.

We note that the company recently announced a letter of intent to divest its Danish portfolio (SEK 1.5bn on the balance sheet) and an impending relatively small equity issue (SEK 100m), SEK 50m of which will be paid out in the near term, improving short-term liquidity. The equity issue is contingent on the outcome of an extraordinary general meeting on 20 Jul. 2023, which we believe is likely to give its approval. However, given the small volume of the planned equity issue and Studentbostäder's other liquidity and refinancing needs, we believe the equity issue is unlikely to be of material help in avoiding a distressed exchange on the outstanding bond. In addition, we believe significant uncertainty remains over the potential divestment in Denmark. Based on our estimates of on-balance portfolio value in Denmark, and the SEK 1.2bn in Danish mortgage credit (*realkredit*) loans per 30 Jun. 2023, we note that the high leverage in the Danish portfolio imply that net cash proceeds from the divestment are not sufficient to cover the outstanding bond volume. Although there are measures the company could take to avoid a distressed exchange, such as further equity issues or divestments, we believe they are unlikely to be successfully executed to such an extent and with such timing as to fully pay off the bond before a distressed exchange becomes necessary. While

the company has repurchased a small portion of its outstanding bond, we do not believe it is likely to succeed in voluntary repurchases of the full volume.

Both the long-term issuer rating and the extension of the Watch Negative also reflect concerns about the overall liquidity position, notwithstanding the bond maturity. As of 30 Jun. 2023, the company had SEK 22m in cash, with a net SEK -42m cashflow in the quarter. In addition to the bond, which has an outstanding volume of SEK 564m, the company has SEK 204m in maturing debt, plus SEK 42m in amortisations. While Studentbostäder has demonstrated a good relationship with its banks for project financing, we believe they are unwilling to provide additional loans necessary to repay the bond before maturity.

Watch Negative

The extension of the Watch Negative reflects the increasing likelihood of a covenant breach and distressed exchange, as well as general uncertainty over whether the company's actions to improve its liquidity position will be sufficient. We believe that Studentbostäder is likely to trigger the interest coverage covenant on its bond, and that negotiations with bond investors will result in a distressed exchange. The Watch Negative placement also reflects our belief that material divestments, and possibly further equity injections, are necessary to repay the bond, which matures on 14 May 2024, and our general concern over Studentbostäder's liquidity.

We could lower the rating to 'C' to reflect the announcement of an imminent distressed exchange or default that has not yet materialised. At the time of a default or distressed exchange on the bond or other outstanding debt, we would lower the issuer rating to 'SD', as long as the company fulfils its other commitments, until the future capital structure is defined. We could lower the issuer rating to 'D' if the company files for bankruptcy or in the event of similar action that would likely cause it to miss or delay future contractually required debt service payments.

We could raise the long-term issuer rating back to the 'B' category to reflect a fully resolved situation regarding the outstanding bond, with no immediate concerns of a covenant breach or distressed exchange, and a stabilised capital structure with more moderate concerns about liquidity in the following 12 months.

We expect to resolve the Watch Negative placement no later than in the days following the publication of Studentbostäder's results for the third quarter of 2023, currently scheduled for 9 Nov. 2023.

Related publications:

- i) [Corporate Rating Methodology](#), 8 May 2023
- ii) [Rating principles](#), 24 May 2022
- iii) [Studentbostäder i Norden AB \(publ\) long-term issuer rating lowered to 'CCC'; Rating on Watch Negative](#), 24 May 2024
- iv) [Studentbostäder i Norden AB \(publ\) long-term issuer rating lowered to 'B+'; Outlook negative](#), 19 Jan. 2023

Rating list	To	From
Long-term issuer credit rating:	CC	CCC
Watch:	Watch Negative	Watch Negative
Short-term issuer credit rating:	N6	N6

Figure 1. Studentbostäder rating scorecard

Subfactors	Impact	To	From
Operating environment	20.0%	bbb+	bbb+
Market position, size and diversification	12.5%	b+	b+
Portfolio assessment	12.5%	bb+	bb+
Operating efficiency	5.0%	bb+	bb+
Business risk assessment	50.0%	bb+	bb+
Ratio analysis		b-	b-
Risk appetite		b-	b-
Financial risk assessment	50.0%	b-	b-
Indicative credit assessment		bb-	bb-
Liquidity		Negative	Negative
ESG		Adequate	Adequate
Peer calibration		Neutral	Neutral
Stand-alone credit assessment		b-	b-
Support analysis		Neutral	Neutral
Issuer rating		CC	CCC
Watch		Watch Negative	Watch Negative
Short-term rating		N6	N6

Type of credit rating:	Long-term issuer credit rating Short-term issuer credit rating
Publication date:	The rating was first published on 13 Jan. 2022.
Office responsible for the credit rating:	Nordic Credit Rating AS (NCR), Oslo, Norway. NCR is a registered credit rating agency under Regulation (EC) No 1060/2009.
Primary analyst:	Ylva Forsberg, +46768806742, ylva.forsberg@nordiccreditrating.com
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Were ESG factors a key driver behind the change to the credit rating or rating outlook?	No.
Methodology used when determining the credit rating:	<p>NCR's Corporate Rating Methodology published on 8 May 2023 NCR's Rating Principles published on 24 May 2022 NCR's Group and Government Support Rating Methodology published on 18 Feb. 2022</p> <p>The methodology and principles documents provide analytical guidance to NCR's rating activities including but not limited to, assumptions, parameters, cash flow analysis, and stress-testing. NCR's methodologies and principles can be found on our website nordiccreditrating.com/governance/policies. The historical default rates of entities and securities rated by NCR will be viewed on the central platform (CEREP) of the European Securities and Markets Authority (ESMA).</p>
Materials used when determining the credit rating:	Annual- and quarterly reports of the rated entity, Bond prospectuses, Company presentations, Data provided by external data providers, External market reports, Meetings with management of the rated entity, Non-public information, Press reports/public information, Website of rated entity.
Potential conflicts of interest:	The rating is NCR's independent opinion of the rated entity's relative creditworthiness. The rating is solicited, i.e. it is prepared for a fee paid by the rated entity. At the time of analysis and publication neither NCR nor any of the analysts or persons involved in the rating process held any interest, ownership interest or securities in the rated entity. NCR does not have any direct or indirect shareholder with a holding of more than 5% of NCR's shares and votes. For further information, please refer to NCR's conflict of interest policy which is available on: https://nordiccreditrating.com/governance/policies
Additional information:	Prior to publication, the rating was disclosed to the rated entity. The issuer was given 24 hours (of which 8 business hours) to remark on factual errors and/or the inadvertent inclusion of confidential information, if applicable. The rating was not amended after the review by the issuer. No stress test was performed. Standard cash flow forecasting was performed. NCR's rating is an opinion regarding the relative creditworthiness of an entity or an instrument. It is not a prediction, guarantee or recommendation to buy, hold or sell securities. NCR assigns outlooks to issuer ratings to indicate where they could move in the near term, normally 12–18 months. Further information on the rating process, rating definitions and limitations is available on our website: nordiccreditrating.com/governance/policies .
Ancillary services provided:	No ancillary services were provided.
Regulations:	This rating was issued and disclosed under Regulation (EC) No 1060/2009.
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