FITCH AFFIRMS PSP'S SENIOR UNSECURED RATING AT 'A-'; OUTLOOK STABLE

Fitch Ratings-Frankfurt/London/Paris-24 March 2016: Fitch Ratings has affirmed PSP Swiss Property AG's (PSP) senior unsecured rating at 'A-' and its Long-term Issuer Default Rating (IDR) at 'BBB+' with a Stable Outlook. The Short-term IDR has been affirmed at 'F2'.

The affirmation reflects Fitch's expectation of PSP's continued strong financial risk profile driven by recurring rental income from a high quality, purely Swiss commercial property portfolio. A conservative balance sheet and management approach towards financing its long-term assets provide ample headroom for the current ratings. The Swiss property market remains stable even despite some weakness in 2015. PSP's business model is underpinned by the positive yield gap between its property income yields and low CHF funding rates.

KEY RATING DRIVERS

Uncertain Environment

PSP, with its purely Swiss portfolio, does not directly suffer from the strengthening of the Swiss Franc. Nonetheless, Fitch will monitor any impact a stronger franc may have on its tenants. Uncertainties from ongoing immigration reform in Switzerland may also undermine the overall appeal of the Swiss real estate market.

Conservative LTV Through-the-cycle

Fitch believes PSP has conservatively managed its loan-to-value ratio (LTV; net debt/portfolio value excluding development) through the cycle and will continue to do so. The LTV, as estimated by Fitch, decreased to 31% in 2015 from 37% in 2009, largely driven by the increased portfolio value. As a result, PSP compares favourably with players which use revaluation gains to further leverage their balance sheet. PSP's 2015 LTV remained roughly unchanged on the previous year.

Strong Debt Serviceability

PSP has a good track record of beating Fitch's estimates and we expect the company to continue to achieve EBITDA net interest cover around 7.0x and an LTV between 25% and 35% over the medium term. This is well within our rating guidelines, despite the shorter lease structures in Switzerland (three to five years versus seven to eight years for offices in the UK).

Signs of Market Overheating

The current low and even negative interest rate environment continues to increase the level of capital flows into prime Swiss commercial property, which is viewed as a safe haven. This has started to stretch fundamentals and Fitch expects yields on PSP's assets to remain low.

Turning Swiss Rental Market

The Swiss rental market is expected to remain somewhat weak in 2016, with pressure on vacancy rates, especially in Zurich, and flat rents. However, the Swiss market should remain reasonably healthy for prime offices. The rental market continues to be supported by a robust Swiss economy, which is attracting international businesses.

Strong Recurring Rental Income

Cash flow generation has proved defensive through the cycle. Vacancy rate decreased to 8.5% in 2015 (10% in 2014). PSP's management remains cautious, citing the oversupply of office space that has been built up over the past years (especially in peripheral areas of Zurich and Geneva). The absorption of this oversupply will take time, which may have a further dampening effect on rental prices. PSP does not have any significant tenant arrears and has not experienced any material tenant defaults.

Measured Development Exposure
PSP's outstanding committed development exposure is moderate at CHF86m in 2016, although the potential programme is around CHF554m until 2022. Fitch expects total development capex for 2016 to remain below 3% of the investment property portfolio value.

Limited Geographic Diversification
The ratings are constrained by the size of the Swiss property market, which is small by European standards. The ratings also incorporate the fairly short-term lease structure in Switzerland (five years with the possibility of extending at the tenant's request for a further five years).

KEY ASSUMPTIONS
Fitch's key assumptions within our rating case for the issuer include:
- Moderate increase in vacancy rate leading to a slight decrease in rental income
- No material change in valuation in 2016
- A small decrease in funding rates

RATING SENSITIVITIES
Negative: Future developments that could lead to negative rating action include:
- An increase in rent arrears, tenant defaults, resulting in EBITDA interest cover falling below 2.5x (2015: 7.9x)
- LTV above 40% and net debt to EBITDA above 9.5x (2015: 8.7x) on a sustained basis
- Material committed development spending rising above 15% of the portfolio value (2% in 2015)

Positive: Future developments that could lead to positive rating actions include:
- Material diversification of existing portfolio geographically or by sector. This transformation would have to be supported by financial metrics being maintained, notably LTV below 40% through the cycle.

LIQUIDITY
PSP has solid liquidity, with CHF650m of undrawn credit facilities that should cover its needs over the next 24 months, and has only limited committed capex. Further, PSP has firm access to both local Swiss banks and bond markets.

Contact:

Principal Analyst
Fredric Liljestrand
Associate Director
+44 20 3530 1285

Supervisory Analyst
Dr. Georgy Kharlamov
Director
+49 69 768 076 263
Fitch Deutschland GmbH
Neue Mainzer Strasse 46-50
60311 Frankfurt am Main

Committee Chairperson
Frederic Gits
Managing Director

+33 144 299 184

Media Relations: Peter Fitzpatrick, London, Tel: +44 20 3530 1103, Email: peter.fitzpatrick@fitchratings.com.

Additional information is available on www.fitchratings.com. For regulatory purposes in various jurisdictions, the supervisory analyst named above is deemed to be the primary analyst for this issuer; the principal analyst is deemed to be the secondary.

Applicable Criteria
Corporate Rating Methodology - Including Short-Term Ratings and Parent and Subsidiary Linkage (pub. 17 Aug 2015)
https://www.fitchratings.com/creditdesk/reports/report_frame.cfm?rpt_id=869362
Recovery Ratings and Notching Criteria for Equity REITs (pub. 03 Dec 2015)
https://www.fitchratings.com/creditdesk/reports/report_frame.cfm?rpt_id=874214