S&P Global
Ratings

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Nassauische Heimstaette Wohnungs- und Entwicklungsgesellschaft mbH

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This report does not constitute a rating action.

Credit Highlights

Overview

Enterprise profile	Financial profile
Nassauische Heimstaette Wohnungs- und Entwicklungsgesellschaft mbH (NH) benefits from the robustness of its core business of letting affordable housing units and an increasing focus on the dynamic Rhine-Main region.	NH's financial indicators will remain under pressure from higher operating costs but only limited leeway to increase rents, and from the increase in debt required to finance the ongoing portfolio expansion and upgrades.
--Letting its units with a discount to market rent, NH should enjoy strong demand for its product, particularly in the undersupplied area around Frankfurt.	--No longer boosted by asset sales and operating under an agreement with its key owner that restricts rental increases, margins have already fallen in response to cost inflation.
--Despite likely peaking in 2025, when the bulk of units from two ongoing development projects complete, we anticipate that sales revenue will play only a minor role for NH going forward.	--About one-third of all borrowing is sourced as subsidized loans from state promotional lender WI Bank, which mitigates the impact of additional debt and higher market interest rates.
--A self-imposed ceiling for leverage and scaled-back development plans will, in our view, support management's efforts to mitigate the impact of the currently challenging operating environment.	--Liquidity remains strong, backed by a combination of liquid financial assets held, available facilities, and contracted long-term loans that can be drawn in line with construction progress.

S&P Global Ratings expects NH's adjusted EBITDA margin to remain broadly stable in the mid-to-upper 20% range. Having fallen below the 30% threshold in 2022, the combination of portfolio growth and rent increases, albeit limited, should help to mitigate the impact of continuing cost inflation.

Indebtedness will quickly exceed 15x nonsales adjusted EBITDA, but we anticipate nonsales adjusted interest coverage will remain very strong. Next to competitively priced borrowing in the open market, NH has access to subsidized promotional lending, which we expect to soften the growth in interest expense.

NH's liquidity position should remain stable. We observe NH as very pro-active in securing sufficient funding from key partners under a forward-looking approach.

Outlook

The stable outlook reflects our view that NH will be able to mitigate the impact of sector headwinds such that the weakening of the group's credit metrics will be contained.

Downside scenario

We could lower our ratings if operating costs or capital expenditure (capex) increase materially above our base-case expectations. This could materialize, for example, from higher-than-anticipated inflation or a ramp-up of NH's development program. The impact of such developments could lead to materially weaker liquidity or debt metrics, and might also reflect weaker management.

In addition, we could downgrade the company if we consider that the likelihood of support from Hesse has diminished.

Upside scenario

An upgrade would depend on NH's financial indicators strengthening significantly, which could additionally result in a more positive view on management.

An upgrade could also follow a similar action on the majority owner of NH, Hesse, or if we assess a higher likelihood of extraordinary support from the state in case of financial distress.

Rationale

The ratings on public housing provider NH reflect our view on the robustness of its underlying core business of letting affordable units, and our view that there is a high likelihood that NH, in case of financial distress, would receive extraordinary support from its 61% owner, the German State of Hesse. That said, we observe a challenging operating environment for NH, with pressure on EBITDA margins. In its lettings business, it is facing increased operating cost but limits on rent growth. Due to the current state of the German real estate market, we expect no significant boost to profitability from NH’s two large ongoing development-for-sale projects, scheduled to complete from 2025, and revenue from asset disposals will now be minimal. Rising debt--caused by material borrowing needs for ongoing construction and refurbishments--and recently risen interest rates will pressure NH's debt metrics compared with the stronger financial indicators of previous years.

Including consolidated group companies, NH owns and operates almost 61,000 housing units across Hesse, but with an increasing focus on the prosperous Rhine-Main metropolitan area around Frankfurt. In our view, the group benefits from generating most of its earnings in the predictable and noncyclical affordable housing sector, supported by a solid market position in its segment and a generally cautious approach to sales risk. We estimate that the development-for-sale business, which boosted performance until 2021 and is expected to peak again in 2025/2026--when numerous units in Frankfurt's new Schönhof quarter are scheduled for delivery--will, on average, only contribute slightly more than 5% to adjusted operating revenue over 2021-2025.

Market dependencies remain balanced for NH. In the wider Rhine-Main area, now the focus of almost all its capex, the company benefits from the region's very tight housing market and, according to our estimates, offers its units at a discount to market rent. For example, we calculate that the average in-place rent of the units owned by NH in the city of Frankfurt itself amounts to below 76% of the city's official rent index. For the wider NH portfolio, we estimate an average rent-to-market-rent ratio of about 84%, albeit based on not very granular market reference data in some areas. Given NH's operations across the entire State of Hesse--which also comprises areas with less strong dynamics--and usual delays between completing new units and tenants moving in, we consider its stated overall portfolio vacancy rate of 2.7% per the end of first-half 2023 as aligned with that of peers in its area of operations.

We assess the regulatory framework under which German public housing providers such as NH 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).

Going into 2023, NH's experienced management has, in the face of higher construction costs and interest rates, scaled back new developments of affordable rental homes. We understand that NH has set itself a limit on gearing and adjusts construction plans accordingly, thereby containing the planned increase in debt. In our view, NH's leadership has opted to reduce risks and clearly prioritize the financial stability of the company rather than accommodate noncommercial housing policy goals. We generally perceive NH's management team as highly experienced, note the long tenure of the company's executives, and believe that they will keep NH conservatively run.

NH's group financial performance, as measured by its adjusted EBITDA margin, has softened to below 30% in 2022, and we predict it will remain clearly below this threshold over our 2023-2026 forecast horizon. This reflects ongoing cost increases in categories that the company cannot apportion to tenants, particularly for maintenance, compliance with tighter energy efficiency and other regulation, and staff compensation. It also incorporates our assumption that an agreement between NH and the government of Hesse that sets ceilings for rent increases, among other things, will be extended on broadly unchanged terms upon expiry at year-end 2023. This should result in only subdued rent growth relative to rising expenditure. In 2025, and to a lesser extent in 2026, EBITDA will be supported by the delivery of, in total, more than 400 development-for-sale units from the Schönhof quarter project in central Frankfurt. However, after reducing our assumptions on achievable sales prices, we expect no materially positive margin effect from this. Our view considers a recently much weaker market for real estate sales, where we understand that tighter funding conditions and discussions about more intrusive energy efficiency legislation have had a negative impact.

NH's consolidated indebtedness will increase, and its interest coverage will likely decline over our 2023-2025 forecast period, despite the recent scale back in construction plans. Projects that are already under construction or in the advanced planning stages should still add more than 1,500 letting units to NH's portfolio over the next three years. Together with about €80 million of planned spending on energy-efficient modernization per year, we calculate annual borrowing needs of, on average, about €300 million for these years at NH. With subdued EBITDA growth and higher interest rates, NH's ratio of debt to nonsales adjusted EBITDA will therefore quickly exceed 15x, up from 13.5x as of year-end 2022, and its nonsales adjusted interest coverage ratio will fall gradually to 2.7x by 2026, down from 5.1x for 2022, according to our view. NH’s interest coverage ratio is supported by its access to substantially subsidized funding from Hesse’s promotional lending arm WI Bank, currently--and in our view, also in the future--representing about one-third of total borrowing. The remaining, essentially all fixed rate debt has been sourced via traditional mortgage loans next to funds raised in the form of senior unsecured "Schuldschein" loan certificates placed in the German private capital market.

Based on a calculated coverage of liquidity uses by liquidity sources of almost 1.5x over the next 12 months, we assess NH's liquidity position as strong. Our calculation considers liquidity sources of €647 million, consisting of cash generated from operations, bank deposits, and other liquid financial instruments held, undrawn and available revolving credit facilities, and agreed long-term loans not yet disbursed. Estimated liquidity uses of €432 million mainly consist of anticipated capex and debt service. Reflecting its established presence in the German "Schuldschein" market, relationships with several mortgage loan lenders from the banking and insurance sector, and the ability to source funding from WI Bank, we evaluate NH's access to external liquidity as satisfactory. Notably, NH has concluded framework agreements with various key partners on future funding that currently still fall outside our 12-month horizon but should provide liquidity in future years.

Government-related entity analysis

Our rating incorporates a two-notch uplift to our 'a-' stand-alone credit profile (SACP) on NH, which we consider a government-related entity. We believe there is a high likelihood that the company would receive timely and sufficient extraordinary support from its 61% owner, the **State of Hesse** (AA+/Stable/A-1+), in case of financial stress, even if the 26 other share-owning Hessian municipalities and related holding vehicles remain passive. We assess the link between NH and Hesse as very strong. This reflects a track record of two €200 million capital injections exclusively provided by the state in the past seven years, Hesse's minister of economic affairs chairing a supervisory board where state appointees dominate, and very close monitoring of NH through a dedicated division in Hesse's finance ministry. Furthermore, we consider NH's role important, given the weight that housing availability and affordability has on the regional political agenda, and that NH is Hesse's only tool to directly intervene in the housing market.

Environmental, Social, And Governance

We think that Germany-based public housing providers are exposed to elevated environmental and social risks that relate to affordability of services and increased investment in existing homes.

These include inflationary pressures, the need to enhance the energy efficiency of the housing stock and eventually phase out carbon-based heating systems, as well as the government's environmental agenda to achieve net-zero carbon emissions.

We think these risks apply to NH in line with the sector and we assess the group's respective current asset quality to be on a par with its peers.

Key Statistics

Nassauische Heimstaette Wohnungs- und Entwicklungsgesellschaft mbH--Key Statistics

	--Year ended Dec. 31--					
Mil. €	**2021a**	**2022a**	**2023e**	**2024bc**	**2025bc**	**2026bc**
Number of units owned*	59,649	60,252	60,937	61,634	62,309	62,575
Adjusted operating revenue	432	426	443	467	646	568
Adjusted EBITDA	138	123	125	130	153	142
Non-sales adjusted EBITDA	130	126	125	130	136	137
Capital expense	275	222	332	300	287	300

	--Year ended Dec. 31--					
Mil. €	2021a	2022a	2023e	2024bc	2025bc	2026bc
Debt	1,550	1,698	1,963	2,170	2,338	2,540
Interest expense	25	25	29	37	44	50
Adjusted EBITDA/Adjusted operating revenue (%)	32.1	28.9	28.2	27.9	23.6	25.0
Debt/Non-sales adjusted EBITDA (x)	12.0	13.5	15.7	16.7	17.2	18.5
Non-sales adjusted EBITDA/interest coverage(x)	5.2	5.1	4.4	3.6	3.1	2.7

*Residential, commercial, and other units, regardless of size differences, at end of period. Parking spaces/garages not included. a--Actual. e--Estimate. bc--Base case reflects S&P Global Ratings' expectations of the most likely scenario. Figures are based on German GAAP data.

Rating Component Scores

Nassauische Heimstaette Wohnungs- und Entwicklungsgesellschaft mbH --Ratings Score Snapshot

	Assessment
Enterprise risk profile	3
Industry risk	2
Regulatory framework	3
Market dependencies	3
Management and Governance	3
Financial risk profile	3
Financial performance	4
Debt profile	3
Liquidity	3
Stand-alone credit profile	a-
Issuer credit rating	A+

S&P Global Ratings bases its ratings on non-profit social housing providers on the seven main rating factors listed in the table above. S&P Global Ratings' "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
- General Criteria: Stand-Alone Credit Profiles: One Component Of A Rating, Oct. 1, 2010

Related Research

- State of Hesse, Oct. 16, 2023
- Regulatory Framework Assessment: German Public Housing Providers Face Increasing Political Demands But Benefit From Strong Institutions, Oct. 3, 2023
- Economic Outlook Eurozone Q4 2023: Slower Growth, Faster Tightening, Sept. 25, 2023
- European Housing Markets: Sustained Correction Ahead, July 20, 2023
- Non-U.S. Social Housing Providers Ratings History: March 2023, March 27, 2023
- Non-U.S. Social Housing Providers Ratings Score Snapshot: March 2023, March 27, 2023
- Non-U.S. Social Housing Providers Ratings Risk Indicators: March 2023, March 27, 2023

Ratings Detail (as of November 17, 2023)*

Nassauische Heimstaette	
Issuer Credit Rating	A+/Stable/A-1
Issuer Credit Ratings History	
24-Mar-2023	A+/Stable/A-1

*Unless otherwise noted, all ratings in this report are global scale ratings. S&P Global Ratings credit ratings on the global scale are comparable across countries. S&P Global Ratings credit ratings on a national scale are relative to obligors or obligations within that specific country. Issue and debt ratings could include debt guaranteed by another entity, and rated debt that an entity guarantees.