STANDARD & POOR'S RATINGS SERVICES
McGRAW HILL FINANCIAL

RatingsDirect®

Research Update:

Prologis European Properties Fund II Outlook Revised To Positive On Improved Credit Metrics; 'BBB' Ratings Affirmed

Primary Credit Analyst:
Marie-Aude Vialle, London (44) 20-7176-3655; marie-aude.vialle@standardandpoors.com

Secondary Contact:
Franck Delage, Paris (33) 1-4420-6778; franck.delage@standardandpoors.com

Table Of Contents

1347261 | 301701763

Research Update:

Prologis European Properties Fund II Outlook Revised To Positive On Improved Credit Metrics; 'BBB' Ratings Affirmed

Overview

- Luxembourg-registered property fund Prologis European Properties Fund II FCP-FIS (PEPF II) has further expanded its portfolio amid improved market conditions in the European logistics sector, and its credit metrics have improved more than we had expected.
- We are therefore revising our outlook on PEPF II to positive from stable, and affirming our 'BBB/A-2' long- and short-term corporate credit ratings on the fund.
- We are also affirming our 'BBB' issue rating on PEPF II's senior unsecured debt, issued by Prologis International Funding II S.A.
- The positive outlook reflects our view that we could raise the rating on PEPF II if the fund sustains its improved credit metrics and maintains organic growth.

Rating Action

On July 17, 2014, Standard & Poor's Ratings Services revised its outlook on Luxembourg-registered property fund Prologis European Properties Fund II FCP-FIS (PEPF II) to positive from stable.

At the same time, we affirmed our 'BBB/A-2' long- and short-term corporate credit ratings on PEPF II and our 'BBB' issue rating on PEPF II's senior unsecured debt, issued by Prologis International Funding II S.A.

Rationale

The outlook revision reflects our view that PEPF II's credit metrics have strengthened amid improving conditions in the European logistics markets. The positive outlook is supported by the recent growth in PEPF II's asset portfolio, following the significant acquisitions completed in 2013 and 2014, and our expectation of further growth due to additional acquisitions this year and in 2015.

The market valuation of PEPF II's portfolio increased to €3.5 billion in December 2013 from €2.9 billion in December 2012, and we forecast this figure to surpass €4 billion over the next two years. PEPF II funded its acquisitions with a mix of debt and equity, following two successful equity raises in 2013 and early 2014 as well as debt issuances in the bond capital markets. As a

1347261 | 301701763

result, credit metrics have improved faster than we anticipated, and we now forecast EBITDA interest coverage to stay at about 4x and debt to debt plus equity at about 40% in 2014 and 2015.

Our rating on PEPF II reflects our "satisfactory" business risk and "intermediate" financial risk profile assessments for the company. Rating modifiers do not have any impact on the rating outcome. In our view, the portfolio growth has reinforced PEPF II's business risk profile, which we now assess at the stronger end of the "satisfactory" category. PEPF II's scale, scope, and diversity benefit from a relatively large pan-European portfolio of premium logistics assets. In addition, we believe that market conditions in the European logistics sector are currently more favorable to PEPF II, as indicated by the compression of yields, notably in the U.K. logistics market, and the still-limited supply of new modern warehouses in Europe.

Our base case assumes:

- Overall revenue growth of 10%-12% in 2014, reflecting the material acquisitions that PEPF II completed in 2013 and early 2014.
- Like-for-like growth in rental income of 1%-2% in 2014 and 2015, supported by our assumption of a stable or slightly improving occupancy rate and modest rent increases. We consider GDP growth, unemployment rates, and consumer price index (CPI) inflation to be the most relevant macroeconomic indicators of market conditions in real estate, and we forecast these as stable or slightly improving for PEPF II's core markets. We also consider corporate sentiment and the supply of new projects as among the most important influences on rent for logistics property investors. In our view, slowly improving sentiment should support an increase in demand in the sector in the next two years.
- PEPF II's EBITDA margin staying firmly at about 88% over the next two years.
- Ongoing asset acquisitions from both third-party transactions and the Prologis pipeline in 2014. This should continue to boost PEPF II's revenue and EBITDA base. Our base case does not factor in any material disposals.

Based on these assumptions, we arrive at the following credit measures:

- We forecast EBITDA interest coverage of about 4.0x in the next two years, comfortably above our previous target of 3.5x.
- We expect the Standard & Poor's-adjusted ratio of debt to debt plus equity to reduce to 40% over the next two years, in line with management's intention to maintain reported leverage below 40%.

Liquidity

We classify PEPF II's liquidity as "adequate" under our criteria, as we believe funding sources will exceed uses by more than 1.2x over the next 12 months.

As of March 31, 2014, we estimate that liquidity sources over the next 12 months will mostly consist of:

- €39 million in cash and short-term investments;

- €150 million availability under committed revolving credit lines;
- About €150 million-€160 million of annual funds from operations (FFO);
- €300 million of unsecured notes raised in April 2014 and about €150 million of new secured debt that we expect to be raised during the year to refinance existing secured debt facilities; and
- About €225 million from a follow-on equity raise completed in April 2014.

This compares with our estimate of liquidity uses over the same period:
- About €300 million of debt maturities;
- 90%-95% disbursement of distributable earnings to the unit holders;
- About €10 million of maximum maintenance capital expenditure; and
- In addition, we forecast significant acquisitions over the next 12 months. We understand that as of July 2014, about €140 million of acquisition spending has already been committed for the year and we anticipate further acquisitions in 2014 and 2015.

Outlook

The positive outlook reflects our view that PEPF II's credit metrics should further strengthen over the next 12-24 months, supported by the material pipeline of acquisitions and improved market conditions.

The outlook also reflects our assumption that the governance and financial policy of PEPF II's largest shareholder--U.S.-based international owner, developer, and manager of industrial properties Prologis Inc.--will remain constant. We believe PEPF II should be able to maintain high occupancy rates and long-term leases to generate stable operating cash flows over the medium term. We also believe that the fund will maintain "adequate" liquidity, an EBITDA-to-interest ratio above 3.5x, and an adjusted ratio of debt to debt plus equity of about 40%.

Upside scenario

An upgrade would likely depend on PEPF II's ability to sustain its recently improved credit metrics and reduce its ratio of debt to debt plus equity to firmly below 40%, while maintaining positive organic growth.

Downside scenario

Conversely, we could revise the outlook back to stable if PEPF II is unable to maintain EBITDA interest coverage above 3.5x and if its debt to debt plus equity remains materially above 40%. We could also revise the outlook back to stable if organic growth turns negative.

Ratings Score Snapshot

Corporate Credit Rating: BBB/Positive/A-2

Business risk: Satisfactory

- Country risk: Low
- Industry risk: Low
- Competitive position: Satisfactory

Financial risk: Intermediate
- Cash flow/Leverage: Intermediate

Anchor: bbb

Modifiers
- Diversification/portfolio effect: Neutral (no impact)
- Capital structure: Neutral (no impact)
- Liquidity: Adequate (no impact)
- Financial policy: Neutral (no impact)
- Management and governance: Satisfactory (no impact)
- Comparable rating analysis: Neutral (no impact)

Related Criteria And Research

Related Criteria
- Methodology And Assumptions: Liquidity Descriptors For Global Corporate Issuers, Jan. 2, 2014
- Corporate Methodology, Nov. 19, 2013
- Corporate Methodology: Ratios And Adjustments, Nov. 19, 2013
- Key Credit Factors For The Real Estate Industry, Nov. 19, 2013
- Methodology: Management And Governance Credit Factors For Corporate Entities And Insurers, Nov. 13, 2012

Related Research
- Prologis European Properties Fund II FCP – FIS, May 2, 2014

Ratings List

Ratings Affirmed; Outlook Action

	To	From
Prologis European Properties Fund II FCP-FIS		
Corporate Credit Rating	BBB/Positive/A-2	BBB/Stable/A-2

Ratings Affirmed

Prologis International Funding II S.A	
Senior Unsecured*	BBB

*Guaranteed by Prologis European Properties Fund II FCP-FIS.

Additional Contact:
Industrial Ratings Europe; Corporate_Admin_London@standardandpoors.com

Complete ratings information is available to subscribers of RatingsDirect at www.globalcreditportal.com and at spcapitaliq.com. All ratings affected by this rating action can be found on Standard & Poor's public Web site at www.standardandpoors.com. Use the Ratings search box located in the left column. Alternatively, call one of the following Standard & Poor's numbers: Client Support Europe (44) 20-7176-7176; London Press Office (44) 20-7176-3605; Paris (33) 1-4420-6708; Frankfurt (49) 69-33-999-225; Stockholm (46) 8-440-5914; or Moscow 7 (495) 783-4009.

Copyright © 2014 Standard & Poor's Financial Services LLC, a part of McGraw Hill Financial. All rights reserved.

No content (including ratings, credit-related analyses and data, valuations, model, software or other application or output therefrom) or any part thereof (Content) may be modified, reverse engineered, reproduced or distributed in any form by any means, or stored in a database or retrieval system, without the prior written permission of Standard & Poor's Financial Services LLC or its affiliates (collectively, S&P). The Content shall not be used for any unlawful or unauthorized purposes. S&P and any third-party providers, as well as their directors, officers, shareholders, employees or agents (collectively S&P Parties) do not guarantee the accuracy, completeness, timeliness or availability of the Content. S&P Parties are not responsible for any errors or omissions (negligent or otherwise), regardless of the cause, for the results obtained from the use of the Content, or for the security or maintenance of any data input by the user. The Content is provided on an "as is" basis. S&P PARTIES DISCLAIM ANY AND ALL EXPRESS OR IMPLIED WARRANTIES, INCLUDING, BUT NOT LIMITED TO, ANY WARRANTIES OF MERCHANTABILITY OR FITNESS FOR A PARTICULAR PURPOSE OR USE, FREEDOM FROM BUGS, SOFTWARE ERRORS OR DEFECTS, THAT THE CONTENT'S FUNCTIONING WILL BE UNINTERRUPTED, OR THAT THE CONTENT WILL OPERATE WITH ANY SOFTWARE OR HARDWARE CONFIGURATION. In no event shall S&P Parties be liable to any party for any direct, indirect, incidental, exemplary, compensatory, punitive, special or consequential damages, costs, expenses, legal fees, or losses (including, without limitation, lost income or lost profits and opportunity costs or losses caused by negligence) in connection with any use of the Content even if advised of the possibility of such damages.

Credit-related and other analyses, including ratings, and statements in the Content are statements of opinion as of the date they are expressed and not statements of fact. S&P's opinions, analyses, and rating acknowledgment decisions (described below) are not recommendations to purchase, hold, or sell any securities or to make any investment decisions, and do not address the suitability of any security. S&P assumes no obligation to update the Content following publication in any form or format. The Content should not be relied on and is not a substitute for the skill, judgment and experience of the user, its management, employees, advisors and/or clients when making investment and other business decisions. S&P does not act as a fiduciary or an investment advisor except where registered as such. While S&P has obtained information from sources it believes to be reliable, S&P does not perform an audit and undertakes no duty of due diligence or independent verification of any information it receives.

To the extent that regulatory authorities allow a rating agency to acknowledge in one jurisdiction a rating issued in another jurisdiction for certain regulatory purposes, S&P reserves the right to assign, withdraw, or suspend such acknowledgement at any time and in its sole discretion. S&P Parties disclaim any duty whatsoever arising out of the assignment, withdrawal, or suspension of an acknowledgment as well as any liability for any damage alleged to have been suffered on account thereof.

S&P keeps certain activities of its business units separate from each other in order to preserve the independence and objectivity of their respective activities. As a result, certain business units of S&P may have information that is not available to other S&P business units. S&P has established policies and procedures to maintain the confidentiality of certain nonpublic information received in connection with each analytical process.

S&P may receive compensation for its ratings and certain analyses, normally from issuers or underwriters of securities or from obligors. S&P reserves the right to disseminate its opinions and analyses. S&P's public ratings and analyses are made available on its Web sites, www.standardandpoors.com (free of charge), and www.ratingsdirect.com and www.globalcreditportal.com (subscription) and www.spcapitaliq.com (subscription) and may be distributed through other means, including via S&P publications and third-party redistributors. Additional information about our ratings fees is available at www.standardandpoors.com/usratingsfees.