MOODY'S
INVESTORS SERVICE

Rating Action: Moody's upgrades PEPF II's ratings to Baa2; stable outlook

Global Credit Research - 20 Mar 2014

London, 20 March 2014 -- Moody's Investors Service has today upgraded to Baa2 from Baa3 the senior unsecured long-term issuer rating of Prologis European Properties Fund II (PEPF II) and the instrument ratings of its backed senior unsecured bonds, issued by Prologis International Funding II S.A. (Funding II), a wholly owned subsidiary of and guaranteed by Prologis Management II S.a.r.l. (Management II) acting in its own name and on behalf of PEPF II. Concurrently, Moody's has upgraded to (P)Baa2 from (P)Baa3 the provisional backed long-term rating of PEPFII's EUR5.0 billion medium-term note (MTN) programme with notes to be issued by Funding II and guaranteed by Management II, acting in its own name and on behalf of PEPF II. The outlook on all ratings is stable.

RATINGS RATIONALE

"The upgrade of PEPF II's issuer rating to Baa2 reflects the fund's continuing strong operating performance, the improved outlook for the logistics property sector and our belief that Europe is on the road to a gradual, albeit uneven, economic recovery", said Lynn Valkenaar, Moody's Vice President and lead analyst on the fund. "In addition, PEPF II has achieved a significant reduction in its secured debt/gross assets ratio over the past two years to just over 20% at year-end 2013 and we expect that this will decline further in the near term", added Ms. Valkenaar.

PEPF II's issuer rating is underpinned by the fund's (1) strong brand name, which attracts high quality tenants; (2) broadly diversified presence in the European distribution warehousing market, with a high-quality portfolio of assets that occupy prime locations; (3) lower business risk profile than many similarly rated peers as the fund bears no development risk; (4) solid credit metrics as of year-end 2013, which include effective leverage, as measured by adjusted total debt/gross assets at 39.5% and fixed charge coverage, as measured by adjusted EBITDA/fixed charges, of 3.4x; (5) further reduction in secured debt/gross assets below its current level of 20.4% in the near term; and (6) improving trend in tenant demand across European trade routes for distribution warehousing facilities. All financial metrics are as adjusted by Moody's.

PEPF II's rating is constrained by its (1) exposure to the cyclicality of the distribution warehouse property sector; and (2) sizable exposure to the Central and Eastern Europe region -- estimated at 27% by value and 29% of annual rental income as at year-end 2013 -- which presents higher growth opportunities but with higher volatility than the more established western European regions in which the fund operates. While the fund has reduced secured debt and increased unencumbered assets, Moody's expects that management will fulfil its intention to move to a largely unsecured financing structure over time.

PEPF II's liquidity profile is adequate. Its steady cash flow generation, EUR150 million long-term committed revolving credit facility (RCF), maturing in 2016, and an equity draw, cover its committed cash outflows for more than a year. In addition, the fund's pool of unencumbered assets provides a source of alternative liquidity and there is ample headroom for its financial covenants.

PEPF II is not a listed entity and, notwithstanding the quality of PEPF II's unitholders, access to capital is dependent on the unitholders' ability and willingness to continue as investors and, from time to time, to provide additional funds. This is a factor that could restrict PEPF II's access to capital compared with publicly listed REITs. However, PEPF II reports that it has only had limited redemption requests over the past seven years of operation, representing cumulatively less than 4% of total units.

In addition, management is overseen by the fund's Advisory Council, which is composed of representatives of the five largest unaffiliated unitholders and has approval rights on all major PEPF II decisions. The largest unitholders' participation in the fund's investment-making decisions reduces the likelihood that the fund would face redemption requests owing to dissatisfaction with investment policies.

RATIONALE FOR THE STABLE OUTLOOK

The stable rating outlook reflects PEPF II's steady financial performance as the fund executes on its strategy as well as Moody's assumption that the underlying factors that support tenant demand in the European logistics property sector will continue to improve along with the economic climate.

WHAT COULD CHANGE THE RATING UP/DOWN

Upward pressure on the ratings could arise if (1) PEPF II's effective leverage remains below 40%; (2) its fixed charge cover rises towards 4.0x; (3) its liquidity continues to improve as the fund extends its average debt maturity such that (a) committed cash inflows exceed outflows for 12 to 18 months on a sustainable basis; and (b) unencumbered assets/total assets trends towards 70%.

Conversely, negative pressure on the rating could occur if (1) PEPF II's earnings deteriorate such that its fixed charge coverage trends below 2.75x; or (2) effective leverage rises above 45% for a sustained period. Negative pressure on the rating could also arise if any liquidity challenges develop or are not adequately addressed or if PEPF II's ratio of unencumbered/total assets does not remain sustainably above 50%.

PRINCIPAL METHODOLOGY

The principal methodology used in these ratings was the Global Rating Methodology for REITs and Other Commercial Property Firms published in July 2010. Please see the Credit Policy page on www.moodys.com for a copy of this methodology.

Prologis European Properties Fund II FCP-FIS was established in Luxembourg in 2007 as a fond commun de placement (FCP-FIS) that invests solely in prime distribution warehousing facilities. It reported total assets of EUR3.62 billion at 31 December 2013. The large US REIT, Prologis, L.P. (Baa2, stable) is the fund's external manager and held 32.48% of the fund's units at 31 December 2013.

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