Credit Benchmark®

Credit Risk Case Study: REITS vs Tenants

June 2021

Introduction

As part of the credit risk assessment of a commercial real estate investment trust (REIT), one can consider the credit risk of the REIT itself as well as the credit risk of its tenants. But what does it mean when a REIT's credit quality doesn't reflect that of its tenants? This case study presents Credit Benchmark consensus credit data on Boston Properties and its top 20 tenants per its 2020 annual report.

Analysis

Boston Properties is one of the largest publicly traded office REITs in the United States that invests in office buildings in Boston, Los Angeles, New York City, San Francisco, and Washington, D.C. As of December 2020, they owned or had joint venture interests in a portfolio of 196 commercial real estate properties, aggregating approximately 51.2 million net rentable square feet.

Over the last two years, credit risk of Boston Properties was rather stable. It was downgraded by S&P from A- to BBB+ in August 2020, while it kept a Credit Consensus Rating (CCR) of a until April 2021, when it was downgraded to a- as shown in Exhibit 1.

Aggregate data on United States Industrial and Office REITs also demonstrates stability over the last two years, particularly as compared to Retail REITs, which have seen a dramatic drop in in credit quality with no signs of recovery.

Exhibit 1 Boston Properties Credit Risk

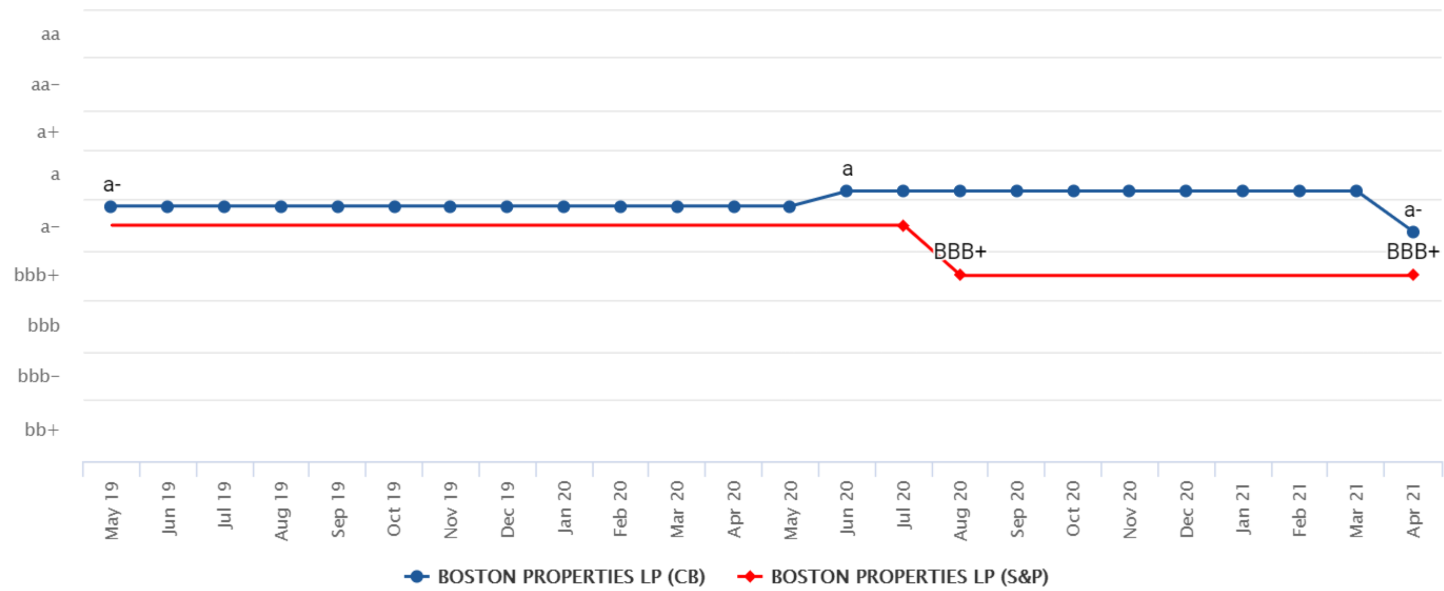


Exhibit 2, overpage, uses consensus credit data to demonstrate the credit risk of Boston Properties' top 20 tenants and reports information available on the Bloomberg Terminal. The last column compares tenants' current credit risk states to their pre-crisis (February 2020) credit risk states.

The analysis of the creditworthiness of the REIT's tenants shows a slightly different story than suggested by the REIT's credit rating.

Credit Benchmark covers 14 of the 20 tenants. Most of the portfolio is rated as investment grade (IG) with two exceptions – SAIC and WeWork. The analysis reveals that credit quality of six of the tenants was negatively impacted since the start of the crisis. However, recent months see more pronounced improvements, including for Microsoft and Mass Financial Services. The credit quality of tenants might significantly impact the credit risk of the REIT in the future. Analysing the credit risk of tenants at both the company level and portfolio level can provide valuable insights on REITs.

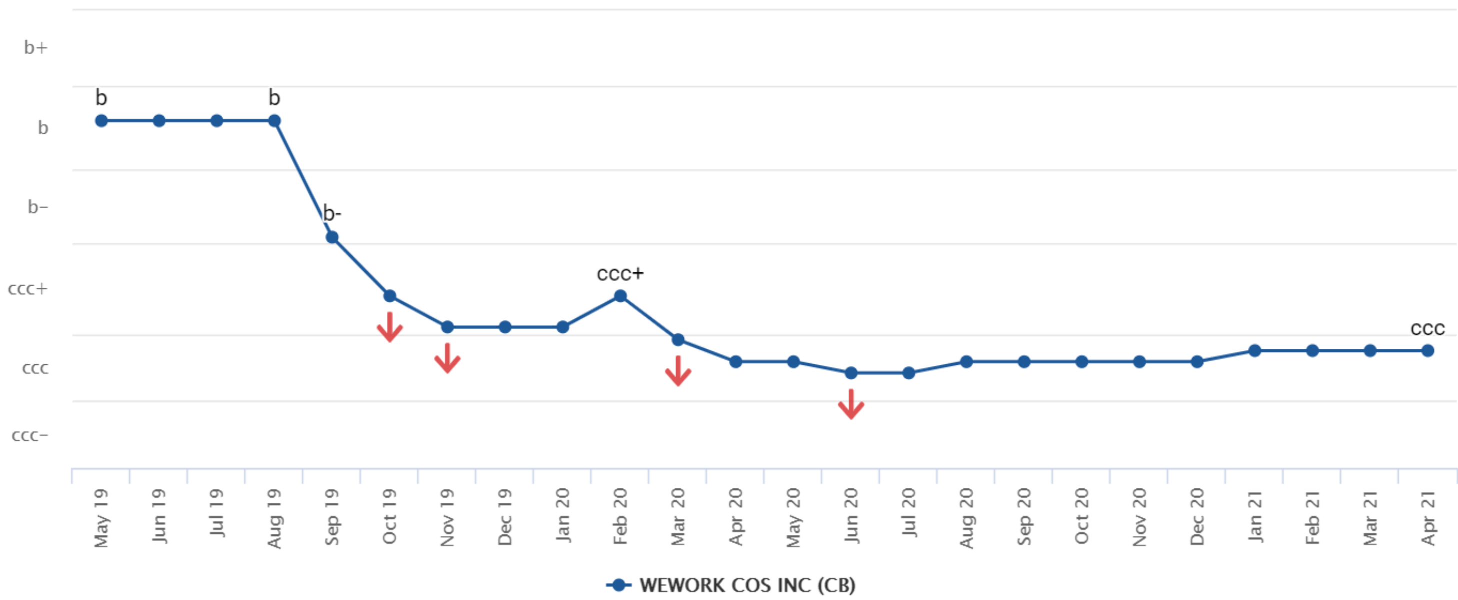
Exhibit 2 Credit Risk of Top 20 Tenants

Top 20 Tenants	% of Portfolio	Credit Risk Indicator	1M Change	6M Change	Feb-20 to Apr-21 Change
salesforce.com	2.30%	IG1	Stable	Stable	Stable
Arnold & Porter Kaye Scholer	2.07%				
U.S. Government	2.06%	IG1	Stable	Stable	Downgraded
Biogen	1.96%	IG1	Stable	Deteriorating	Stable
Akamai Technologies	1.67%	IG2	Stable	Stable	Stable
Ropes & Gray	1.37%				
Microsoft	1.32%	IG1	Upgraded	Upgraded	Stable
Google	1.27%	IG1	Stable	Stable	Stable
Shearman & Sterling	1.27%				
WeWork	1.12%	HY2	Stable	Improving	Downgraded
Kirkland & Ellis	1.01%	IG2	Stable	Stable	Deteriorating
Wellington Management	0.89%	IG1	Stable	Stable	Deteriorating
Blue Cross Blue Shield	0.88%				
Bank of America	0.85%	IG1	Stable	Stable	Stable
Mass Financial Services	0.80%	IG1	Improving		Improving
Leidos	0.77%	IG2	Deteriorating	Deteriorating	Upgraded
Weil Gotshal & Manges	0.69%				
Bain Capital	0.68%				
Bechtel Corporation	0.68%	IG2	Stable	Stable	Downgraded
SAIC	0.66%	HY1	Stable	Stable	Stable

Premium data from Credit Benchmark on the Bloomberg Terminal can provide even further details at the company level, including the Credit Consensus Rating with 100 scale granularity and consensus opinion change analytics, as shown in Exhibit 3 for WeWork. The data coverage spans 1,600 entities in the real estate investment trusts and services space, 80% of which are unrated.

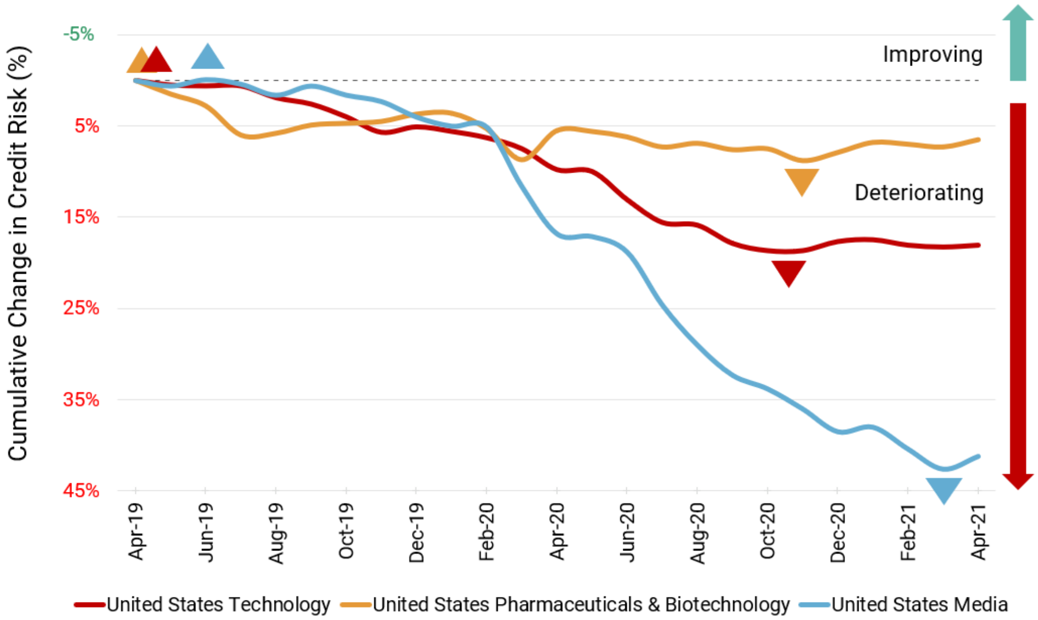
Exhibit 3 shows WeWork at the bottom of the HY2 category with a ccc rating.

Exhibit 3 Credit Risk of WeWork – Premium Data



Credit Benchmark data at the Aggregate level allows for sectoral analysis. Boston Properties report that 30% of their portfolio are within technology, media and life-sciences. Exhibit 4 shows the credit performance of these sectors, revealing stark differences. Media were strongly impacted by the crisis with almost 40% increase in credit risk and a continuing downwards trend, with just recent signs of stabilisation. On the contrary, Pharmaceuticals & Biotechnology were hardly impacted.

Exhibit 4 Sector Analysis



Source: Credit Benchmark

Conclusion

Credit Benchmark offers broad consensus credit risk data coverage not only on REITs, but also on REITs' underlying properties. Using the data to investigate the individual creditworthiness of the underlying tenants can help provide a stronger understanding of where there may be weakness in a REIT's portfolio of properties, and how the REIT's credit rating may be impacted in the future. Further, Aggregate Analytics can help reveal exposures and trends within risky sectors.

Credit Benchmark data is now available on the Bloomberg Terminal. Visit CRDT<GO> or get in touch with us for your free trial of Premium Data and Analytics on the Bloomberg Terminal.

About Credit Benchmark

Credit Benchmark brings together internal credit risk views from 40+ of the world's leading financial institutions. The contributions are anonymized, aggregated, and published in the form of entity-level consensus ratings and aggregate analytics to provide an independent, real-world perspective of risk. Consensus ratings are available for 57,000+ financials, corporate, funds, and sovereign entities globally across emerging and developed markets, and 90% of the entities covered are otherwise unrated.

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