

Befimmo

Real Estate • Belgium

Overly defensive: time to invest

NEUTRAL

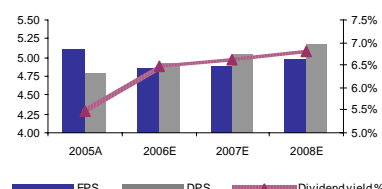
Price: € 76.0

Price Target: € 76.0

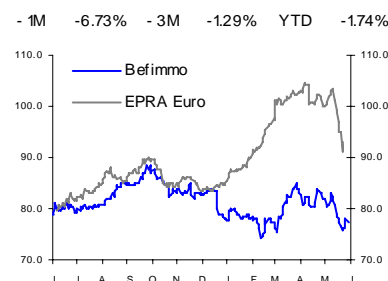
Befimmo operates a quality office portfolio almost entirely located in the capital of Europe with strong exposure to the a-cyclical CBD zone accompanied by an excellent contract maturity profile. Consequently, its stock is a safe haven for investors who are looking for an attractive 2006E 6.5% dividend yield. However, after its change in perimeter due to disposals, the company is confronted with the challenge of reinvesting the proceeds to normalize its payout ratio and offset rising financing costs. We regard the stock as fairly valued and initiate coverage with a Neutral rating.

€	2005A	2006E	2007E	2008E
EPS (recurring)	5.11	4.76	4.88	4.98
CFPS	6.40	4.83	4.90	5.00
NAVPS	65.5	66.9	68.0	68.8
Dividend	4.80	4.92	5.04	5.17
Net income (m)	50.0	47.5	47.8	48.8
P/E	17.1	16.0	15.6	15.3
P/CF	13.7	15.7	15.5	15.2
EV/EBITDA	19.0	18.2	17.5	17.2
P/NAV	1.34	1.14	1.12	1.10
Div. Yield	5.49%	6.47%	6.63%	6.80%

EPS and DPS evolution



Performance Befimmo



- Pure play, low beta.** Befimmo, Belgium's second-largest listed property company operating a €1.1bn portfolio, offers a pure play on the Brussels office market (97% of assets). Its excellent earnings quality translate into a low beta due to i) a stable high quality tenant base (48% public tenants), ii) high exposure (62%) to the a-cyclical CBD zone and iii) a superior maturity profile with 72% of rents expiring after 7 years.
- Attractive and safe 6.5% dividend yield.** We expect recurring cash flow per share to slide by 6% to € 4.78 due to a change in perimeter (sale of Borschette & Charleroi) after which we believe it will recover by a mild 2% p.a. in 2007-08 on the back of indexation but hampered by rising financing costs. Therefore, in absence of any new investments, payout will temporarily exceed cash flow. Nevertheless, the yearly 2.5% growth in the dividend is secured by the capital gains realized in recent disposals (€ 13.8m).
- Fairly valued, initiate coverage with a Neutral rating.** Our DCF and EVA analyses reveal valuations of around € 76, which is where the shares are trading right now. In terms of relative valuation, the stock is trading at a reasonable 2006E 18x EV/EBITDA, in line with its European peers. However, due to the limited growth perspectives in the standing portfolio and its prudent track record with regard to investments, we believe the stock is fairly valued, despite its attractive 6.5% dividend yield.
- Triggers.** Debt financed acquisitions and/or stronger than expected revaluation results could trigger a higher valuation. In particular, if Befimmo were to win the tender for the State Sicafi, this could add up to € 9 per share (+12%).

Price target (€)	76.0
Date	31-May-06
Stock price (€)	76.0
Market cap (€)	744
No. Shares (m)	9.794
Daily volume 3m avg	12,401
Free float	84%
Reuters	BEFIt.BR
Bloomberg	BEFB BB

Analyst:

Mickael Van den Hauwe
 mickael.vandenhouwe@dexia.be
 +32 2 222 33 95

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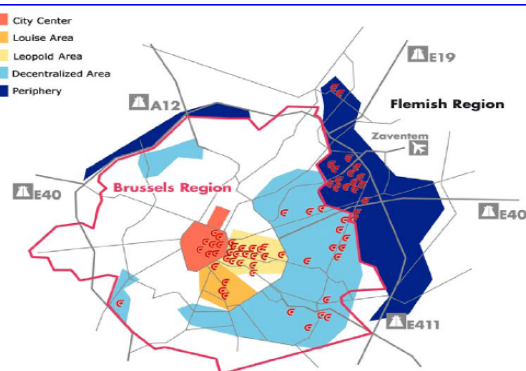
Low-beta play in the capital of Europe

II. PROFILE: RISK AVERSE REIT

II.1. Conservative player on the Brussels office market

With a market cap of € 744m, Befimmo is Belgium's second largest SICAFI after its closest peer Cofinimmo (€ 1.2bn). It operates a medium-size property portfolio of € 1.1bn, which predominantly consists of offices located in and around Brussels (97%). As the company has a very selective approach towards acquisitions, it is not as often mentioned in news headlines as its competitor Cofinimmo, which has a more entrepreneurial approach. Befimmo has a portfolio which is comparable to Cofinimmo's, although it has a more defensive profile as it has a higher exposure towards the CBD (62% vs. 45%) and a superior maturity profile. The company is structured as a Belgian REIT, i.e. a SICAFI (Société d'investissement à capital fixe), offering an attractive legal and fiscal framework.

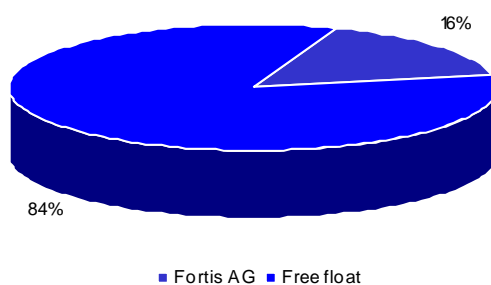
Graph. 1: Breakdown of the Brussels market



Source(s): Dexia

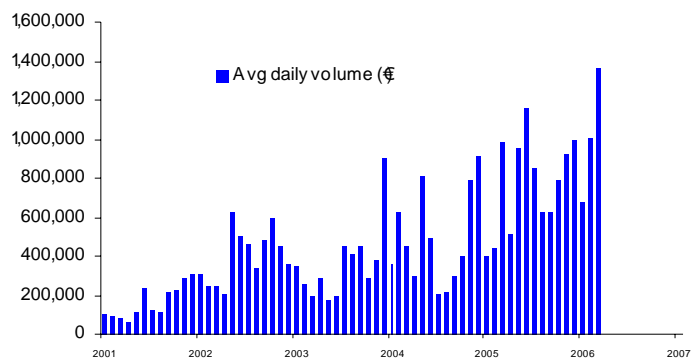
Since 1995, coincident with the emergence of the SICAFI status, the company has been listed on Euronext Brussels. Its stock is included in the EPRA Europe index. The free float stands at 84% as Fortis AG is the only major shareholder with a 16% stake.

Graph. 2: Shareholder's structure



Source(s): Befimmo

Liquidity has hampered in recent years, but has in the last six months strongly improved with an average daily turnover to reach ca € 1m so far in 2006, but thereby still lagging Cofinimmo (€ 2.3m)

Graph. 3: Stock market liquidity

Source(s): Befimmo

Tax-exempt vehicle with a compulsory payout of 80% of net cash income

II.2. Tax-efficient SICAFI status

A SICAFI, a closed-end real estate investment company, is an investment vehicle equivalent to the REIT in the US, the FBI (Fiscale Beleggingsinstelling) in the Netherlands and the SIIC (Société d'Investissement Immobiliers Cotée) in France. Having this tax-efficient status, Befimmo pays no corporate income tax on result and capital gains. In addition, a SICAFI is subject to a compulsory distribution of at least 80% of net income, resulting in an attractive dividend yield.

Table 1: SICAFI – Main characteristics

- Investment and management of a property portfolio
- Activity limited to investment in real estate
- Not permitted to engage in real estate development for third parties
- Closed-end fund listed on the stock exchange
- No more than 20% of total assets invested in a single property
- Gearing limited to 50% of debt-to-total assets
- Assets booked at their estimated market value
- Quarterly appraisal of assets by an independent expert
- No corporate income tax
- Minimum free float of 30%
- A minimum compulsory distribution of 80% of net income
- Withholding tax of 15%, giving relief for private investors residing in Belgium. No withholding tax is deducted for foreign non-profit investors (e.g. pension funds)
- Annual real estate tax has to be paid on the buildings in portfolio, but is usually passed on to the tenants.

Source(s): Dexia

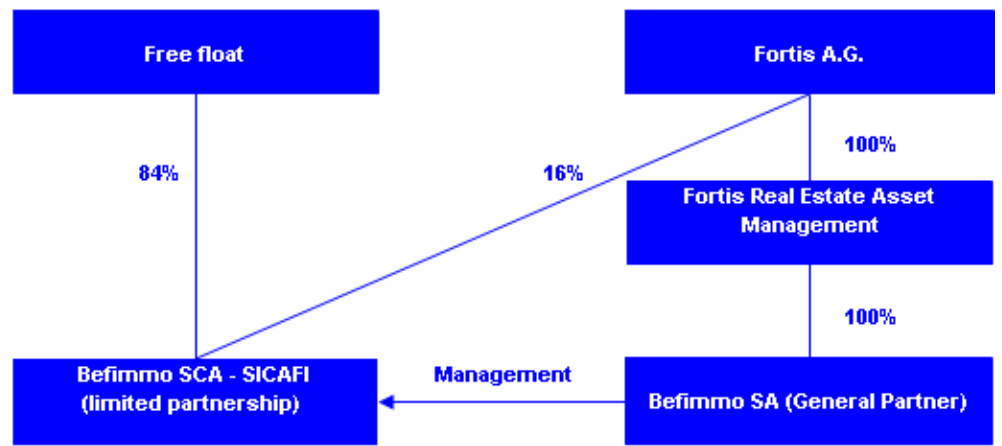
External property management

II.3. Structure

Like many other Belgian listed real estate companies, Befimmo is structured as a limited partnership (Befimmo SCA) (in contrast to Cofinimmo which was founded as a limited liability company). It is managed by its general partner Befimmo SA, which has unlimited liability vis-à-vis the commitments made by Befimmo and is capable to exercise veto right on all crucial decisions. For this unlimited liability, the former receives an annual management fee of 2% of pre-tax profit.

Befimmo SA's only asset is its Board of Directors, which is statutory empowered to carry out all acts that are necessary to achieve the corporate targets at Befimmo SCA. The Board delegates the day-to-day management to Befimmo SCA, under the supervision of CEO Mr Benoît de Blicq, who proposes investments, disposals and finance operations to the Board of Befimmo SA. Befimmo SCA has, besides its CEO, 18 FTE's on its payroll (6 finance, 3 projects, 5 commercial, 4 administrative) who are responsible for the asset management. All other activities are considered as non-core and are outsourced to third parties.

Graph. 4: Befimmo management and ownership structure



Source(s): Befimmo

Strong ties with Fortis, but corporate governance puts strong constraints

The last phrasing could be an unfortunate choice of words as the property management (comprised of technical maintenance and tenant management) is outsourced to Fortis Real Estate Property Management, subsidiary of Fortis Real Estate. In FY'04-05, the latter received a fee of € 403k for its services, which are based on a non-exclusive contract that can be terminated at a one year's notice. Nevertheless, one should put the link with Fortis into the right perspective as only 2 seats out of 11 in the Board of Befimmo SA are taken up by Fortis and the majority is composed of independent directors (6 out of 11), in accordance with proper corporate governance rules. Consequently this does not a priori rule out any M&A activity, but the structure does not facilitate any important decision-making and most of all, in the end the controlling power won't be equally divided among all shareholders.

III. STRATEGY: OLD SCHOOL INVESTOR

III.1. Investment in CBD offices remains core business

Buy and hold

Befimmo's strategy lies in targeting office premises on the Brussels market (97% of portfolio value), with a strong focus towards structures located in the Brussels CBD zone (62%) and minor exposure to the Periphery and Decentralized zones (35%) which offer higher yields but tend to be more cyclical. Apart from location, the company also tries to screen the market for buildings that are fully let on a long-term basis to public sector bodies or high quality covenants with the goal of maximizing its long-term cash flows. The company is not active in property development for own account, except for the occasional refurbishments or small redevelopments of existing properties.

Studying expansion abroad, but will opportunities arise?

Although one could easily make a case for diversification into other real estate types, the company clearly indicates that it sticks to its core business, the real estate management of office premises. On the contrary, geographical expansion is on the agenda as management indicates that it is currently considering expanding abroad, e.g. by buying an office portfolio with an appropriate critical mass in another European capital which would then represent about 10-15% of the portfolio. For example, the Dexia Immo Lux portfolio (€ 148m) which was recently acquired by Leasinvest Real Estate could have well fit into this strategy. Despite the fact that we would welcome such a move, we remark that installing a local management team could prove to be inefficient (read: expensive) and that it will need some fiscal creativity to prevent tax leakage as it is not the company's immediate goal to apply for the local REIT status if it expands abroad. Even more, we wonder if the company will succeed in this objective as suitable investment products have become scarce and given its prudent approach with regard to acquisitions. Also note that if Befimmo seeks for a market which can offer rental growth, the company is taking a directional move by exposing itself to a rental cycle, which can conflict with its desire to sign long-term contracts.

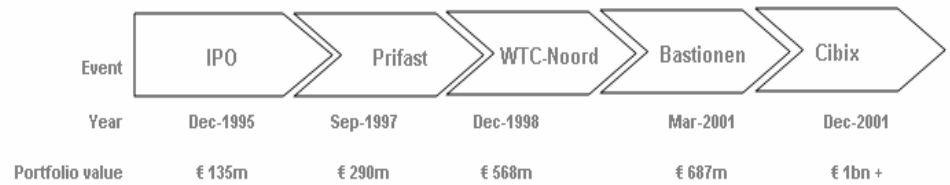
III.2. Management opted for a pure play

When it was founded ten years ago, a strategy originated of investing in three types of properties: i) office buildings in Brussels, ii) semi-industrial premises on the Brussels-Antwerp axis and iii) retail buildings in Belgium. A decade later, the portfolio is almost completely focused on office premises (97.5%) in the Brussels market (97.5%) and therefore lacks diversification. The company indicates that this is a direct consequence of the fact that it could not source any attractive investments in the other real estate classes. This should not be seen as a major negative though, as the bulk of its quality portfolio consists of low risk/low yield a-cyclical CBD assets (62%) in the European capital. Furthermore, one could even argue that diversification in the different types of real estate should be a choice for the investor.

III.3. Selective approach with regard to acquisitions/disposals

Last acquisition was made in 2003

Befimmo takes a very prudent stance with regard to acquisitions. Apart from four large transactions (summarized in graph 4) which ultimately brought the marketable portfolio value in excess of € 1bn, the company has never been very active on the investment front. Befimmo indicates that the main culprit for this is the fierce competition for quality investment products. Indeed, Belgian Sifaci's have been reported as less active on the Brussels investment market in 2005. According to Catella Codemer, they only accounted for 5% of the investment volumes, with 74% of all transactions made in the CBD. Volumes are mainly driven by the presence of German, Irish and Middle Eastern investors whose liquidities put strong pressure on yields (some major transactions were even executed at a yield below the 6% threshold).

Graph. 5: Milestones in Befimmo's history

Source(s): Befimmo

Nevertheless, last year its competitor Cofinimmo was able to source some attractive deals for a total amount of € 278m, mainly by diversifying geographically (Charleroi, Mechelen) and by investing in a new segment (nursing homes and senior residences). Befimmo's last acquisition dates from 2003, when it acquired the 14,000 m² Poelaert 2/3/4 office block for € 52m based on a 5.5% initial yield. The company has made a due diligence for several projects in the last two years, but none of them materialized mainly on competition grounds as mentioned earlier. Currently the company is in the running (as are Cofinimmo, IVG and Axa) to buy a de facto controlling stake in the Sicafi of the Belgian State (see further in this report).

Slightly changing its investment criteria would not harm the company's risk profile

We think would Befimmo have the intention of growing its portfolio, it will have to re-consider other investment options. The rationale behind this is that assets let to government bodies will be extremely scarce as ii) the Belgian State is grouping its real estate patrimony into a real estate holding and ii) the demand for prime assets let to the European Union or representations is extremely strong. In our view Befimmo could loosen its investment criteria without harming an investor's perception of the company's risk profile. Below we have summarized a few possibilities:

- The company could adopt a more pro-active approach and search for office markets abroad which can offer growth (e.g. Paris).
- It could buy exposure to the Luxembourg market by acquiring the projects developer Atenor has in its pipeline.
- A diversification into nursing homes and senior residences like Cofinimmo would match Befimmo's profile (long-term indexed contracts and steady value growth). However, it would have to find a solution to neutralize the default risk of the operator.
- Taking on commercial risks by acquiring quality buildings at risk or by making off-plan purchases.
- The likelihood of taking over a smaller Belgian listed property company seems limited as most of them are trading at a substantial premium to NAV (15-25%) and their legal structure (limited partnership) often prevents M&A activity.
- Taking a more active approach with regard to capital recycling by rotating its asset base more frequently could add more NAV growth. This should not be prohibited by the astronomic transfer tax rate (12.5% in Brussels and the Walloon Region, 10% in the Flemish Region) as most deals are structured in a tax efficient way.

Table 2: How to evade the astronomic transfer tax rate...

- 27-year lease agreement – 0.2%
- Sale to public bodies – tax exempt
- Sale of shares of a real estate company – tax exempt
- Sale of real estate under the rules governing real estate agents – 5.0 to 8.0%
- Contribution of real estate against the issue of new shares – tax exempt
- Merger, division and other forms of company reorganization – tax exempt

Source(s): BEAMA – non-exhaustive list

III.4. Dividend policy

Target set at growing DPS by 2-3% per annum, without taking into account possible investments

Befimmo has in the past been able to offer a healthy dividend growth as it was able to grow its recurring cash flows by 3-4% per annum. Befimmo will grow the dividend by 2.5% p.a. in the next three years, even if this dividend would exceed the net cash flow as a result of a change in perimeter (sale of Borschette) and rising financing costs. This dividend growth is secured by the capital gains realized on the sale of Borschette and Charleroi totalling € 13.8m which therefore can act as a buffer. We also point out to the fact that if Befimmo does not have to address these savings, it will be obliged under the Sicafi rulings to fully distribute the aforementioned cap gains (€ 1.35 per share) after 4 years if it has by then not reinvested the proceeds in new real estate projects.

Table 3: Track record NAV and DPS growth

	1996	1997	1998	1999	2000	2001	2002	2003	2004	2005	2006E	2007E	2008E
NAV	53.96	55.31	56.74	58.62	61.20	64.55	66.11	65.84	66.27	65.48	66.93	67.98	68.79
<i>chg %</i>		2.5%	2.6%	3.3%	4.4%	5.5%	2.4%	-0.4%	0.7%	-1.2%(*)	2.2%	1.6%	1.2%
DPS	3.24	3.62	3.74	3.84	4.00	4.12	4.28	4.45	4.62	4.80	4.92	5.04	5.17
<i>chg %</i>		11.7%	3.3%	2.7%	4.2%	3.0%	3.9%	4.0%	3.8%	3.9%	2.5%	2.4%	2.6%

Source(s): Dexia (*) Decline due to the one-off stemming from the application of IAS 40 (valuation of properties at fair value)

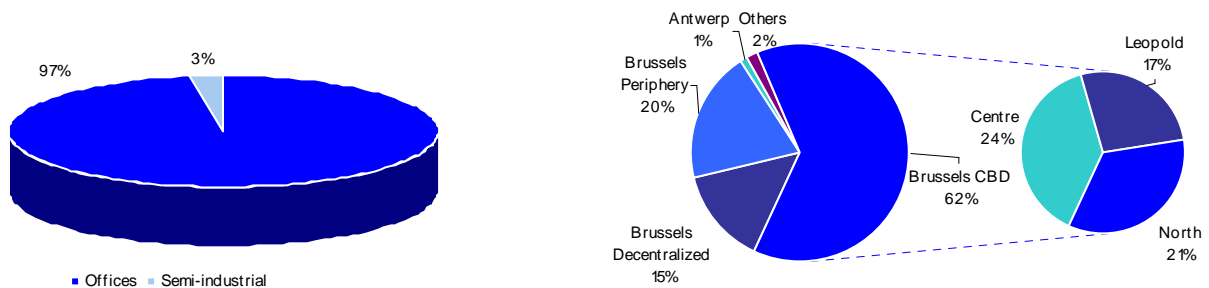
IV. PORTFOLIO

IV.1. Medium-to-high quality portfolio

Single type, single market portfolio

Befimmo manages a portfolio of € 1.1bn (corrected for transfer taxes) that almost entirely consists of medium-to-high quality office premises of about 14,000 m² on average. The vast majority (97%) of the properties is located in Brussels. Being focussed on a single property type in a single market, the portfolio lacks diversification. However this needs to be put into the right perspective, as 58% of the portfolio is let on long term contracts (+9y) and 62% of the buildings is located in the Central Business District (CBD) (vs. 46% for Cofinimmo). This area is made up of the Leopold, Centre and North districts, which benefit from the presence of the European institutions, the Belgian public sector and large financial institutions. It is crystal clear that in this zone rents and occupancy rates are less dependent on the economic cycle. Other areas like the Brussels Decentralized area (15% exposure) and the Periphery (20%) tend to be more vulnerable to the overall economy because they depend on the needs of the private sector. With regard to quality, most of the buildings (60%) are new or had refurbishments less than 10 years ago.

Graph. 6: Portfolio breakdown by type and geography



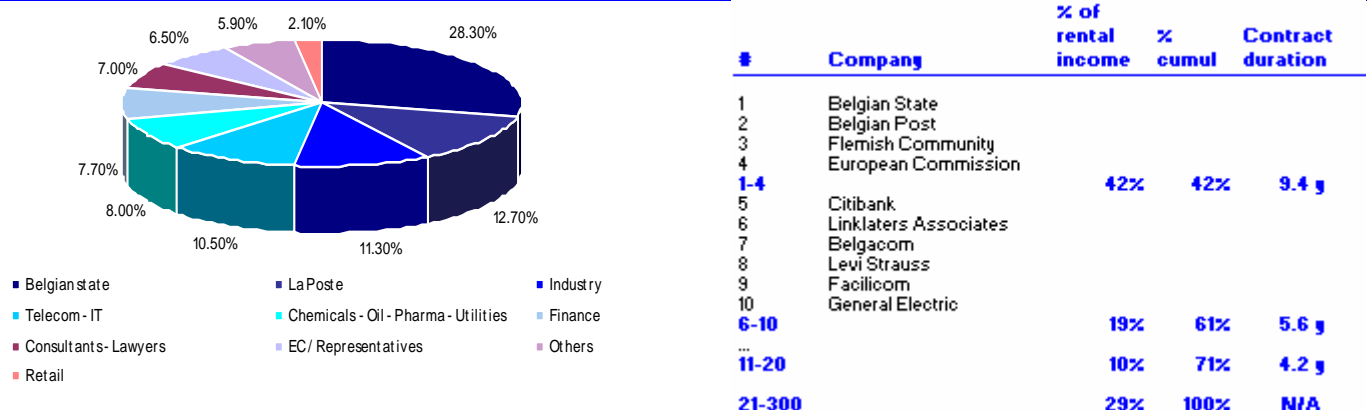
Source(s): Befimmo 30.09.2005

IV.2. Stable high quality tenant base

Concentrated, but low-risk tenant structure

Befimmo's distribution of rental income is quite concentrated towards four tenants who account for 42% of rental income, that is to say the Belgian Government, the Belgian Post, the Flemish community and the European Commission. This does not reveal any material risk though, as these are AAA-tenants whose contracts have an average residual duration of 9.4 years. Consequently, Befimmo can rely on a stable high quality tenant base with little risk of insolvency. Other important tenants include large multinationals in the IT, industrial and chemicals/oil/pharma sector which account for ca 30% of rental income.

Graph. 7: Breakdown of rental income by type of tenant and top-10 tenants



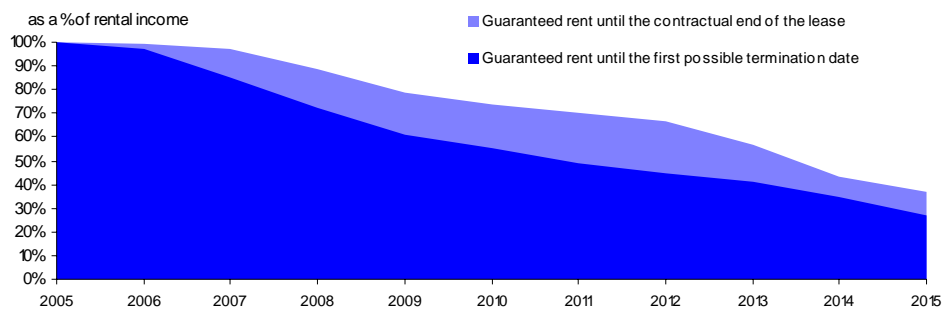
Source(s): Befimmo 30.09.2005

Excellent contract duration thanks to strong CBD exposure...

IV.3. Safe maturity profile

A minimum of 50% of rental income is guaranteed until 2010, or 70% in case no termination option is exercised (equal to Cofinimmo). This forward lock-up appears to be a stable percentage over the last 5 years. The average period till first break stands at 6.4 years, which is quite defensive given the fact that a typical leasing contract is structured as a 3/6/9. This is of course the positive impact from long term leases concluded with its top-10 tenants, which are first class covenants mainly located in the CBD and Decentralized zone and represent 61% of rental income with an average maturity of 8.2 years. For 2006 and 2007 Befimmo is faced with a yearly 10% contract reconciliation, predominantly for smaller surfaces in the weak periphery zone, where we can detect some reversionary potential.

Graph. 8: Lease expiration scheme



Source(s): Befimmo 30.09.2005

...but lease expiries in the suburbs carry negative reversionary potential

Below we have compared Befimmo's contracted rents with market rents. Although we acknowledge that top quartile rents are currently some 15-25% higher (€/ m² 164 in the Decentralized and €/ m² 154 for the Periphery according to JLL), we prefer to base our sample on an average of all transactions that were concluded in the recent quarter (€/ m² 143 and €/ m² 122 respectively). We can identify that lease contracts in the Decentralized and Periphery zones carry some negative reversionary potential of -15% and -18% respectively. We do not think that these figures are distorted by the inclusion of lettings of older buildings, as real estate brokers are reporting an increasing amount of grade A space occupied at the expense of grade C stock (King Sturge). We also want to stress that in the suburbs incentives of 20-30% under the form of rental-free periods are not exceptional and need to be added to the negative reversionary potential. Nevertheless, the latter is mitigated by the positive reversionary potential (+22%) in the Centre, which can be explained by the fact that Befimmo still has a number of contracts concluded at rental levels of around €/ m² 140-160. Nevertheless, it will need some time for this upside to surface as it mainly concerns long-term contracts. We regard the -13% reversionary potential for the Leopold zone based on recent transaction samples as non-existent, as most of Befimmo's Leopold buildings are prime assets. Therefore, we estimate the total reversionary potential of the portfolio to be close to zero.

Typical rent free periods (months)

- 3-6 (3/6/9y lease)
- 3-9 (6/9y lease)
- 6-12 (9y lease)

Source(s): Dexia

Table 4: Reversionary potential

Zone	Contractual rents (€m)	Contractual rents (€/ m ²)	Transaction avg Q1'06 (€/ m ²)	Implied market rent (€m)	Reversionary potential
Centre	17,853	160	195	21,801	22.1%
Leopold	11,514	241	211	10,068	-12.6%
North	19,367	178	180	19,551	0.9%
Decentralized	9,986	168	143	8,483	-15.1%
Periphery	14,648	149	122	12,033	-17.9%
Other	3,865	n/r	n/r	3,865	n/r
Brussels	77,233			75,801	-1.9%

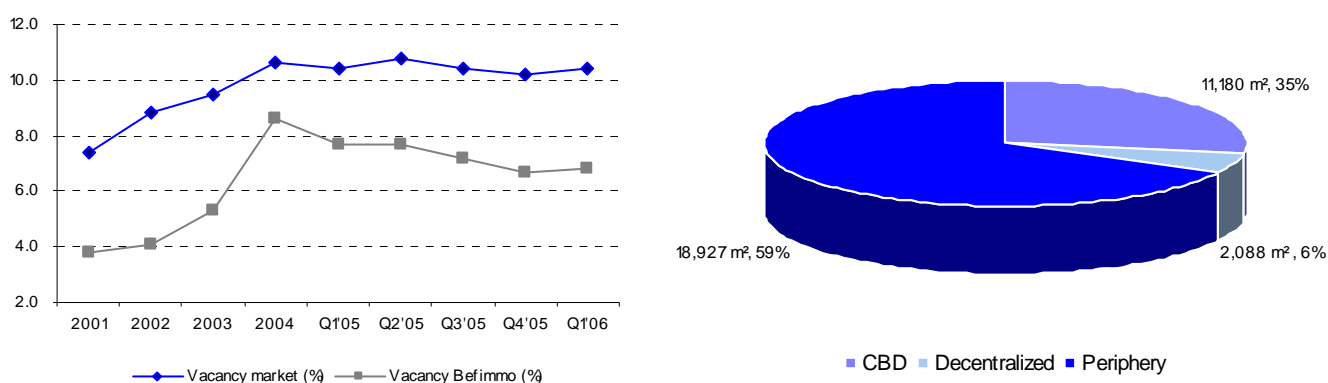
Source(s): Befimmo 30.09.2005, CBRE, Dexia calculations

Upside risk to the vacancy

IV.4. Vacancy

Befimmo's vacancy has in recent years always been slightly better than the market, with an average spread of around 2%. Last year Befimmo was able to decrease its vacancy by 1.4% to 6.7% vs. 10.2% for the Brussels market. This was achieved by strongly reducing the vacancy in the decentralized zone down to a mere 3.3% from 16% in 2004 and 17% for the market. This however did not fuel rental income because at the same time a number of 6/9 contracts which were concluded on the top of the IT-boom in 1999-2000 saw their rental levels strongly revised downward. The bulk of the current vacancy is due to the troubled Periphery zone, although we see some upside risk as the market is bottoming out and corporates could start to arbitrate the attractive rental level and tax differential compared to Brussels city.

Graph. 9: Vacancy rate Befimmo vs. market and distribution of vacancy in Brussels per district (in m²)



Source(s): Befimmo 31.03.2006, JLL, Dexia

CBD assets deserve a higher appraisal

IV.5. Conservative valuation

We feel that Befimmo's portfolio is conservatively valued, especially when compared with prevailing market conditions. For example, the company's CBD assets are currently valued at 7.5% whereas prime yields for standard 3/6/9 years stand at 6% in this zone and brokers even quote prime yields of lower than 6% for assets rented on long term. We think that demand for such assets will persist and we would like to see a more aggressive valuation for these assets. With regard to the non-CBD assets, we follow the conservative approach for three reasons. Firstly, these are of course not all prime assets. Secondly, the market is still tough in this zone. Lastly, one should beware that rising interest rates could eat into the capital values such that a certain safety margin is at its place.

Table 5: Cap rates for Befimmo vs. prime rents

District	Value (€m)	Implied yield	Potential yield (*)	Prime market yield	△
CBD	683	7.1%	7.5%	6.0%	1.5%
Decentralized	148	6.8%	7.0%	6.5%	0.5%
Periphery	210	7.0%	8.1%	7.0%	1.1%
Total portfolio	1,090	7.1%	7.7%		

Source(s): Befimmo 30.09.2005, CBRE, Dexia calculations (*) Corrected for vacancy

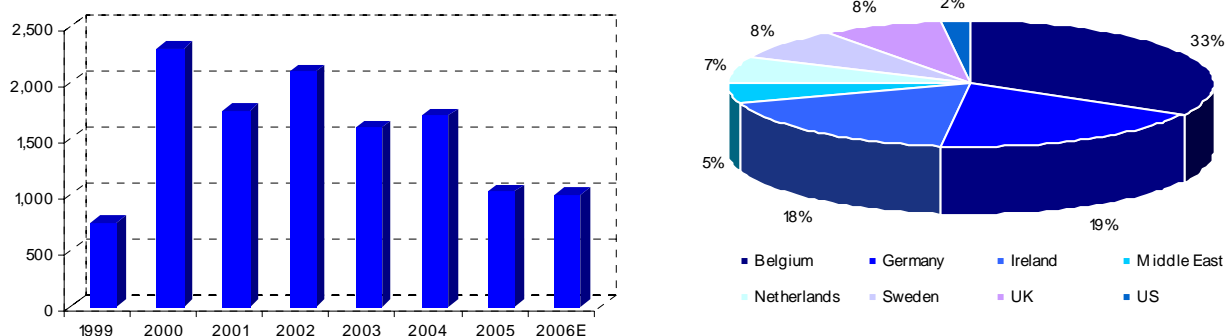
V. BRUSSELS OFFICE MARKET

V.1. Buoyant investment market

Scarcity of prime products in CBD...

The Brussels office market is well-known for its stability and a-cyclical character due to the long-term commitment by the European Union which attracts a lot of international organizations and representation bodies. Consequently, there is a strong appetite for the Brussels market, mainly from international investors which accounted for 67% of the investment volume in 2005 (€ 1.03bn according to CBRE). The most important cross-border investors are of German, Middle Eastern and Irish origin. Investment volume in 2005 was significantly lower than in 2004 (€ 1.55bn), but we believe this is the result of a lack of suitable investment products as there is a divergence between the strong demand from debt driven investors and supply, because of the reluctance of owners to sell. Fierce competition from highly leveraged players is also one of the reasons why the Sicafi's were reported to be less active, with only a 5% contribution to the investment volume (Catella Codemer).

Graph. 10: Investment volume in Brussels & distribution in terms of buyer origin

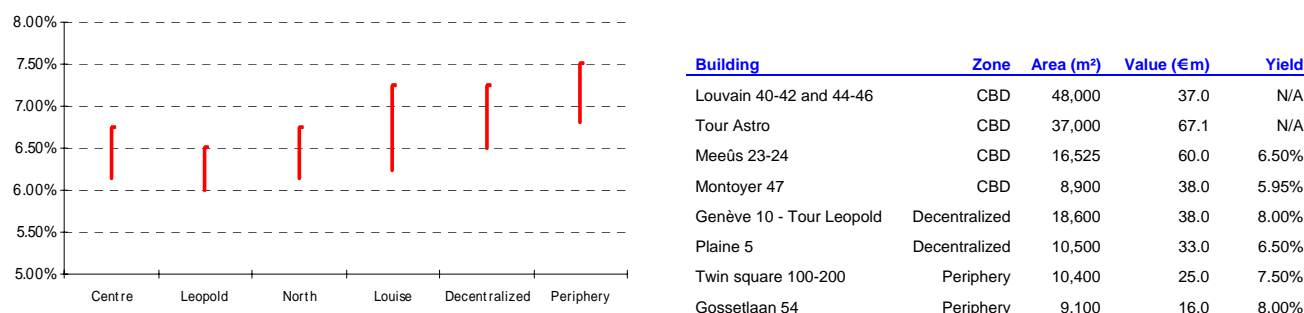


Source(s): CBRE

...causing a renewed interest in the suburbs

Prime yields for standard 3/6/9 contracts are stable at 6% in the Leopold zone, but some major transactions were executed at a yield below the 6% threshold for longer-term contracts (Axa-deal with Flemish Government at 5.5%). The most important trend was the hardening of yields in the suburbs to below 7% (for well-let properties) due to the scarcity of products in the CBD and some large enterprises starting to arbitrate the cost differential vs. the inner-city (lower taxes and more flexible buildings). With a 190 bps spread between prime yields and long term bond yields and an improved take-up situation, the Brussels market will continue to attract a lot of money flow. However, given the rise in bond yields we do not expect a further yield compression and believe yields are generally close to the bottom. The recent increase in bond yields might ease the distortion between supply and demand as it will prompt a number of investors to take profit. 2006 investment volume should be around € 1bn, fuelled by some major transactions in the pipeline with an increased importance from Spanish and UK investors.

Graph. 11: Brussels office market: prime yield range per district & reference transactions in 2005



Source(s): CBRE, JLL

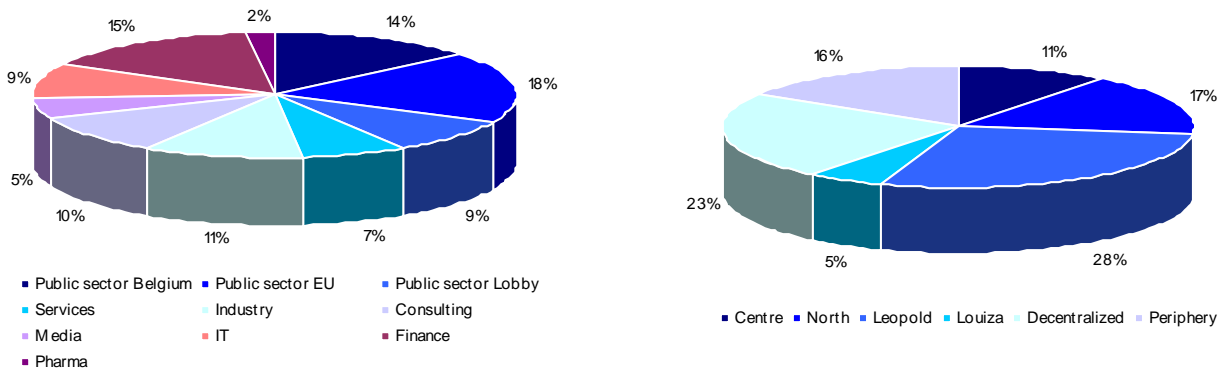
V.2. Rental market: risk to supply/demand equation?

- Office demand – increased activity from corporates

Decentralized and Periphery stabilizing

With a take-up in 2005 of 633,000 m², an increase of 40% yoy, the Brussels office letting market was marked by strong recovery. Nevertheless, the data contain some noise as they were affected by a few large exceptional transactions in both the private (finance) and the European public sector, which accounted for 15% and 18% of take-up respectively. Among the large letting deals were the 80,000 m² - Dexia Tower (Dexia) and the 41,500 m² - Madou Plaza (European Commission). Nevertheless, Q3 and Q4 data showed a very active corporate sector although this activity was predominantly related to relocations than expansion in the light of rationalization of office space needed and M&A activity. 28% of the take-up was related to the Leopold zone, 23% in the Decentralized area and 17% in the North district. Overall vacancy decreased to 10.4% (end 2005) from 10.8% (end 2004). Most important trend was the bottoming out in the Decentralized and Periphery zone, where vacancy rates stabilized and downward pressure on rents eased.

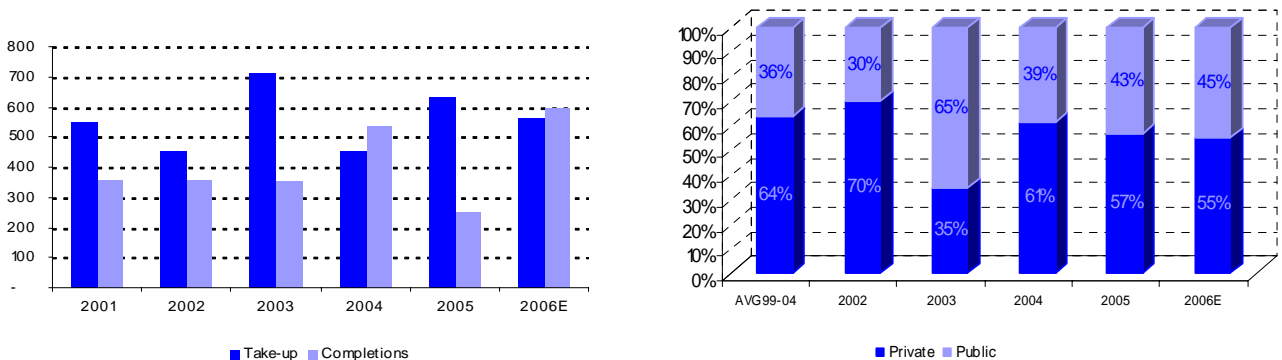
Graph. 12: 2005 take-up per origin and per district



Source(s): CBRE

In 2006 the letting market should continue to stage its recovery on the back of GDP growth (2.3% 2006E, Dexia estimate) which will be higher than the Euro zone average and higher employment in the services sector. This should fuel demand from the private sector for premises in the Periphery and Decentralized zones which have a more cyclical character than the CBD. Therefore, we expect rents to bottom out in these zones but given the high starting point for the vacancy, we do not expect rents to increase in the near term. An important activity from the EU institutions and accompanying lobby groups is also expected due to the planned entry of Bulgaria and Romania to the EU in 2007. Take-up should reach 564,000 m² (CBRE), 10% lower than last year but due to a few exceptional items as mentioned earlier. Certain companies could indeed profit from a recovery of the Brussels market, but an increase in occupancy will be muted by strong incentives and negative rental reversions.

Graph. 13: 2005 take-up per origin and per district

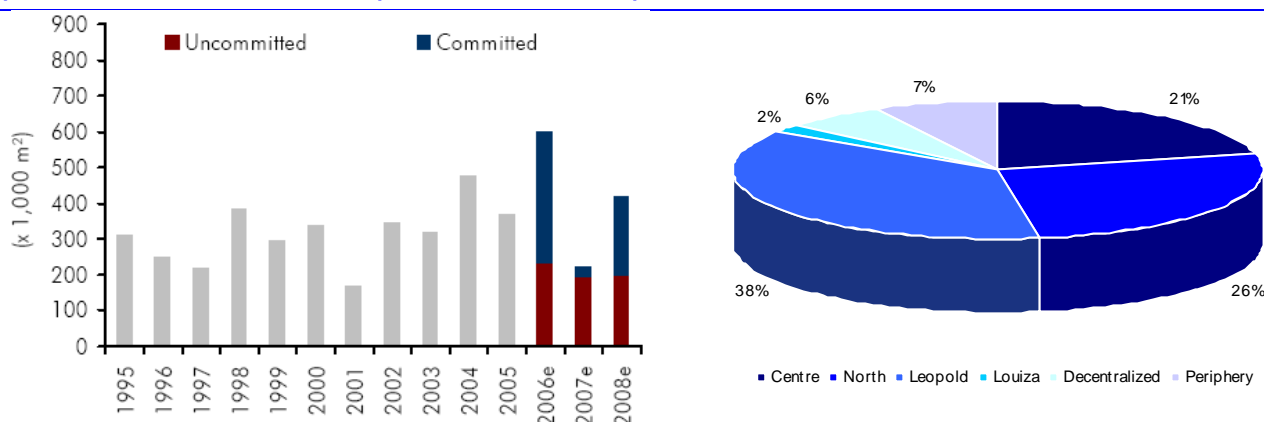


Source(s): CBRE, Catella Codemer

Office supply – development completions could hurt CBD

As the Brussels office rental market is bottoming out, one should closely monitor if the recovery is sustainable by looking at how the supply side is responding. In 2006, 600,000 m² of projects should be completed (5% of total stock), predominantly in the Leopold (32%), the North (23%) and the Centre districts (17%). Although speculation ratios are well managed (62% has been pre-committed for a forward 12-month delivery period), this supply could hurt vacancy levels in the CBD and cause prime rents to go down. This will be exacerbated by i) the increasing bargaining power from the EU as a tenant and ii) the fact that certain corporates could opt for a move from the CBD to the Periphery to arbitrate the rent and tax differential without having to deliver on the quality of the building. Nevertheless, the impact could be of a temporary nature, as 2007 should be marked by a steep drop in construction activity (to 200,000 m²). With regard to the suburbs, development schemes are almost non-existent and this is also the prerequisite for rents to bottom out in these zones. However, possible development sites are abundant so it will remain a question if developers remember a lesson from the previous speculative development boom at the end of the 90s.

Graph. 14: 2006-2008E office completions and distribution per district



Source(s): CBRE

Table 6: Major project completions in 2006

Project	Submarket	Surface (m ²)	Committed
Dexia Tower	North	82,000	100%
Covent Garden	North	68,000	0%
Lex 2000	Leopold	58,000	100%
Ellipse Building	North	50,313	70%
D4 - D5	Leopold	40,000	100%
Paladium	Centre	27,000	100%
Central Plaza	Centre	19,600	0%
Tesaurus	Leopold	18,000	100%
Evere Square	Decentralized	17,000	100%
Lex 65	Leopold	15,360	100%
Subtotal		395,273	74%

Source(s): CBRE

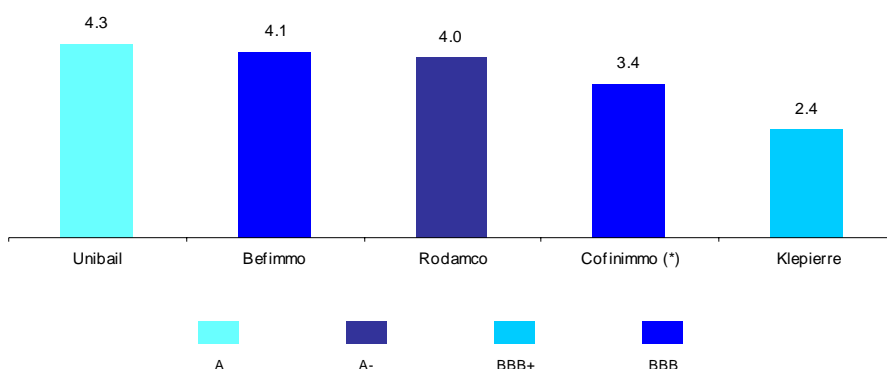
VI. BALANCE SHEET: NIHIL SUB SOLE NOVUM

VI.1. Stable credit rating

Despite a positive outlook by S&P, a credit rating upgrade seems less likely in a rising interest rate climate

Befimmo's BBB credit rating by S&P has been stable over recent years and is more or less in line with other real estate companies that have been awarded a credit rating and equivalent to its closest peer Cofinimmo. However, we must note that Befimmo is more solidly financed than the latter when looking at interest coverage (EBIT/net interest expense) (4.1x vs. 3.4x for Cofinimmo). In a European context, a multiple of 2.5-3.0 seems to be the standard. Befimmo's interest cover is higher and even in line with its larger European peers which have a slightly higher credit rating. This strong ratio is reflected into a "positive outlook" by S&P which, if expected to be sustainable on a permanent basis, could lead to a one-notch upgrade. However, this seems less likely to materialize in the near term in the light of the rising interest climate and the company's weak hedging policy.

Graph. 15: Interest coverage 2006E



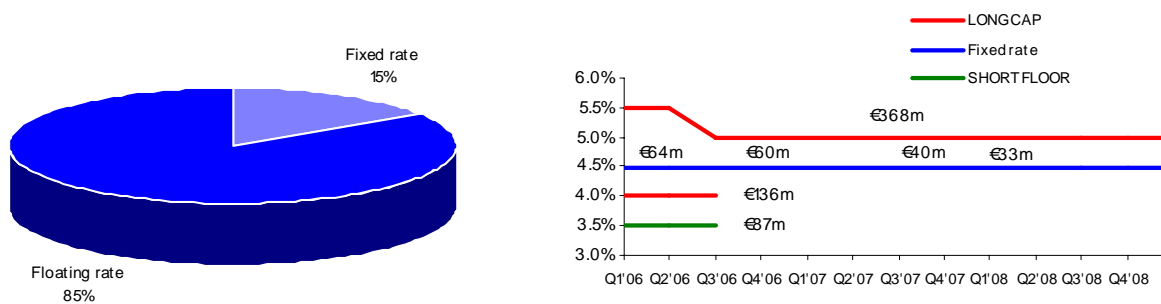
Source(s): Dexia estimates, JCF, (*) Financial income corrected for financial leases

VI.2. Debt structure

85% of debt at floating rate, only capped at 5%...

At FY'05 end, 85% of the group's gross financial debt of € 414m (vs. 99% for Cofinimmo) was structured as short-term floating rate debt, thereby taking advantage of the prevailing low levels of short-term interest rates. In 2005, the average cost of debt (including banking margins and the cost of interest rate hedging instruments) worked out at 3.25%, subsidized by the large exposure towards cheap commercial paper (72% of debt - € 300m). The CP programme is backed by a € 350m syndicated facility maturing in 2011. Consequently, the average duration of Befimmo's debt stands at 4.9 years, of which only 13% is repayable beyond the 5-year horizon. To protect itself against rising interest rates, the company currently has a two long positions in caps at 4% (€ 136m) and 5.5% (€ 87m) partially financed by a short position in a floor at 3.5% (€ 87m), which all mature at the end of Q2'06. Thereafter, it has a cap running at a strike of 5% until end-2008 covering 85% of its floating rate debt.

Graph. 16: Debt structure



Source(s): Befimmo

...not our preferred approach

Indeed, taking advantage of low interest rates has worked quite well in recent years, but the large portion of debt at floating rate makes the company vulnerable to a rise in interest rates. As our macroeconomic model suggests a further rise in interest rates, we estimate the financial expense to increase in the coming years. Since the interest payable is the most important cost for a property company, we would like to see a more adequate hedging programme. Note that Cofinimmo carries out a similar hedging policy, albeit that its hedge is more solidly structured with 80% of its floating rate debt capped at 4%. By way of illustration, and assuming that the structure and level of debt remain constant and given the hedging instruments put in place, an average increase in interest rates of 50 bps over our projected average 2006 Euribor 3M of 2.9% would lead to a rise in financial charges of about € 1.76m (+11.6%).

Table 7: Sensitivity of net financial 2006E vs. Euribor 3M

Euribor 3M	2.63%	2.88%	3.13%	3.38%	3.63%	3.88%
<i>bps chg</i>	-0.25%	0.00%	0.25%	0.50%	0.75%	1.00%
Net financial	(14,287)	(15,168)	(16,049)	(16,930)	(17,810)	(18,691)
<i>chg absolute</i>	881	-	(881)	(1,762)	(2,642)	(3,523)
<i>chg relative</i>	-5.8%	0.0%	5.8%	11.6%	17.4%	23.2%

Source(s): Dexia estimates

VI.3. Gearing to loosen soon?

**Approximately € 105m
gunpowder left for
acquisitions**

As the company is close to its legal ceiling of 50% debt-to-total assets (45%), there is little gunpowder left to aim for acquisitions. We estimate the amount left for investments, assuming gearing would rise to 50%, currently stands at € 105m (equivalent to 10% of the portfolio). However, the Belgian real estate market is warming up for a loosening of the maximum allowed gearing to 60 or 75% as a compensation for the downward correction of the NAV (application of IAS 40 – portfolio valued at fair value, i.e. excluding transfer taxes). This should be beneficial for real estate companies which want to grow but are flirting with the 50% threshold. However, we see a Sicafi with a profile equivalent to that of Cofinimmo or Befimmo able to leverage up to 60%, but draw some serious question marks if it were to gear up any higher in the case of enlarged freedom, as we think it would be penalized by lower credit worthiness and consequently, a higher cost of debt. Also note that growth is not entirely restrained because of a limited debt capacity, as we think the company could easily tap into the equity markets to partly finance acquisitions.

Table 8: Sensitivity of investment capacity vs. gearing threshold

Situation at 30.09.2005			
Debt (*)	495,068		
Portfolio value (**)	1,063,217		
Total assets	1,092,814		
Gearing % (*)	45%		
Gearing threshold	50%	60%	75%
Investment capacity	105,379	404,928	1,303,573
<i>as a % of the portfolio</i>	9.9%	38.1%	122.6%

Source(s): Befimmo, Dexia estimates (*) In accordance with the Royal Decree of April 10, 1995, (**) Excluding transfer taxes

VII. OUTLOOK 2006-2008

VII.1. Direct investment result

Table 9: Financial forecasts 2006-2008

(€m)	2005A	2006E	2007E	2008E	05-08E
Rental income	79.2	76.4	78.1	79.6	0.2%
Operating costs	(6.8)	(7.7)	(6.4)	(6.5)	-1.5%
Corporate cost	(6.3)	(6.2)	(6.4)	(6.6)	1.8%
EBIT	66.1	62.5	65.3	66.5	0.2%
Net Financial	(15.5)	(15.2)	(16.7)	(17.0)	3.2%
EBT	50.7	48.2	48.5	49.5	-0.8%
Taxes	(0.7)	(0.7)	(0.7)	(0.7)	1.9%
Direct investment result	50.0	47.5	47.8	48.8	-0.8%
FCF	51.9	45.7	47.0	48.4	-2.3%
Net debt	400.9	396.1	397.2	398.2	-0.2%
Shareholders' equity	641.3	655.5	665.8	673.7	1.7%

Source(s): Dexia estimates

Key assumptions

	2006E	2007E	2008E
Occupancy rate	92.8%	93.6%	94.3%
CPI indexation	2.0%	2.0%	2.0%
Euribor 3M avg	2.9%	3.3%	3.4%

Source(s): Dexia Bank

- In 2006 we expect the group's rental income to slide 3.5% to € 76.4m due to a change in perimeter. The disposal of Borschette and Charleroi will cause a loss in rental income of € 4.1m and as a result, CPI indexation will only act as a cushion. Although we expect the occupancy to increase by ca 75 bps p.a. the next 3 years, we think this will be mostly offset by reversions and incentives on the renewal of existing contracts.
- Due to higher technical costs because of some large buildings that need refurbishment, the change in perimeter will be more pronounced at the EBIT level in 2006E (-5.3%). For 2007-08 we expect a growth in EBIT of 4% and 2% respectively on the back of maintenance costs reverting to a more normal level and lower charges on unlet property owing to an increase in occupancy.
- Our economist team projects a further rise in interest rates. Therefore, as Befimmo's debt is almost entirely floating and in absence of any adequate hedging instruments, the financial expense will be marked by a sharp rise, especially in 2007 (+10%). Note that the rise in financing cost will not yet be visible in 2006 in absolute terms due to a debt reduction in 2005 and the fact that H1'05/06 figures included a € 0.9m revaluation of financial instruments (non-cash!).
- Consequently, we think that Befimmo's guidance for having restored the direct investment result back to the 2005 level after the change in perimeter by 2007 will not be attained. We expect it to slide by 6.7% this year to € 47.5m after which it will recover by 2% p.a.

VII.2. Indirect result

Capital growth assumptions

	2006E	2007E	2008E
Total portfolio	1.2%	1.0%	0.8%
CBD	2.5%	2.0%	1.5%
Decentralized	0.0%	0.0%	0.0%
Periphery	-2.0%	-1.5%	-1.0%

Source(s): Dexia Bank

- We are banking on a sustained positive revaluation for CBD assets mainly based on the annual 2% indexation of passing rents and a mild yield shift. Although there is sufficient market evidence to justify a strong downward yield shift, we think the experts could remain reluctant to book this yield shift.
- Part of the positive revaluation for CBD assets will be partially offset by negative capital growth in the periphery, were most of the premises are over rented.
- Overall, we anticipate a positive revaluation of 1% on average for the next three years (ca € 1.15 per share).

VII.3. NAV and dividend outlook

Table 10: 2006-2008E NAV and dividend evolution

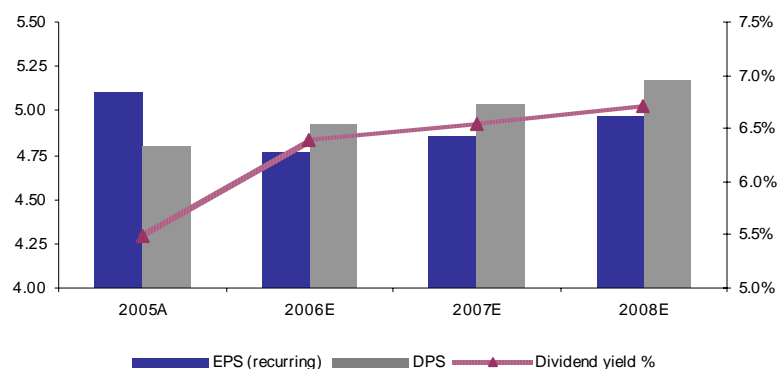
	2005A	2006E	2007E	2008E
Cash direct result	5.11	4.76	4.88	4.98
yoy	-1.3%	-6.8%	2.6%	2.0%
Indirect result	1.43	1.40	1.09	0.86
as a % of portfolio	1.3%	1.3%	1.0%	0.8%
Dividend	4.80	4.92	5.04	5.17
yoy	3.9%	2.5%	2.4%	2.6%
yield	5.5%	6.5%	6.6%	6.8%
NAV	65.48	66.93	67.98	68.79
yoy	3.0%	2.2%	1.6%	1.2%
premium (discount)	34%	14%	12%	10%

Source(s): Dexia estimates

Recent capital gains should secure 2.5% p.a. dividend growth

- In the past Befimmo was able to offer a steady dividend growth as it was capable to grow cash flows by 3-4% p.a. The company is now guiding for a yearly dividend growth of 2.5%.
- As we estimate that the direct (= cash) investment result will not cover for this guided growth in the dividend, the company will have to address the savings money it obtained by selling the Borschette and Charleroi building (€ 13.8m) which will consequently act as a buffer.
- We also point out to the fact that if Befimmo does not have to address these savings, it will be obliged under the Sicafi rulings to fully distribute the aforementioned cap gains (€ 1.35 per share) after 4 years if it has by then not reinvested the proceeds in new real estate projects.
- Sluggish capital growth in the standing portfolio and a payout above 100% will only result in a modest NAV growth of ca 1.5% p.a. such that the NAV premium should gradually decline to 10% in 2008E from 14% in 2006E

Graph. 17: Payout will exceed 100% in the next years



Source(s): Dexia estimates

VII.4. Quid State Sicafi?

One of the projects Befimmo is currently studying is the partial privatization of the buildings owned by the Belgian State. The latter has decided to sell part of its real estate patrimony and bring it in a newly created Sicafi, which will be listed on Euronext Brussels. The goal of this large sale and lease back operation is in fact an artificial trick to reach the 2006 budget equilibrium.

To manage the NewCo, the Belgian State will rely on the expertise of an operational partner which would hold a de facto controlling stake (needed to prevent tax leakage). Befimmo (as are Cofinimmo, IVG and Axa) is one of the candidates to be selected as the operational partner. Recent news flow indicates that the Belgian government would only own 10% in the new vehicle, whereas it was originally foreseen that it would end up with a 25%+1 stake, which would give it a blocking minority. This would be beneficial for the partner, which could then hold 50% without jeopardizing the minimum 30% free float rule. We estimate the transaction to close before year-end as it is foreseen in the 2006 budget (this strengthens the negotiation power of the possible partner). Nevertheless, the IPO will probably not materialize until the beginning of 2007 due to the short time frame and the scale of the transaction.

Below we have tried to get an idea about what could be the impact if Befimmo were to succeed in taking a controlling stake in the upcoming State Sicafi. The total portfolio of the State Sicafi should be around € 1bn, of which the majority should be offices located in Flanders occupied by the ministry of Finance. If we assume the new vehicle to be financed by a 100% debt/equity ratio, the partner would then have to enter the capital for € 250m, of which at least € 100m has to be under the form of assets let to the Belgian government. We would expect the remainder to be financed by debt, which should pose no problem as the legal gearing threshold for Sicafi's would soon be loosened to at least 60%.

Table 11: Impact State Sicafi on Befimmo balance sheet and P&L

State Sicafi - Pro forma balance sheet			Pro forma P&L		Assumptions		
Buildings	1,000,000		Rents	62,500	6.25% gross initial yield		
Total assets	1,000,000		EBIT	53,125	85% margin		
Equity	500,000	100%	Net financial	(20,000)	4% cost of debt		
Befimmo	250,000	50%	Net profit	33,125			
Belgian state	50,000	10%					
Free float	200,000	40%					
Debt	500,000						
Total liabilities	1,000,000						
Befimmo - Balance sheet impact				P&L impact		Assumptions	
	Befimmo 2006E	Sicafi d'état impact	Befimmo consolidated	Net profit 2006E	47,521	Befimmo "as is"	
Buildings	1,070,813	900,000	1,870,813	+ Sicafi d'état	16,563	50% Befimmo share	
Cash	17,628	-	17,628	- € 150m debt financing	(6,750)	4.5% cost of debt	
Other	17,775	-	17,775	- loss in rents on € 100m	(5,000)	5% net yield	
Total assets	1,106,217	900,000	1,906,217	New net profit	52,334		
Equity	655,544		655,544	% chg	10.1%		
Minorities	-	250,000	250,000				
Debt	413,680	650,000	1,063,680				
Other	33,025	-	33,025				
Accrued liabilities	4,779	-	4,779				
Total liabilities	1,107,028	900,000	2,007,028				
Debt ratio	40.4%		54.6%				

Source(s): Dexia estimates – Note that these are more guesstimates than estimates

The key aspect in this exercise is of course at which cap rates the government will sell its assets. We would expect it to be on average in the range of 6%-6.5% as it concerns buildings let on long-term (+15y). However, we have no insight into the quality of the buildings and their location, which have a strong impact on the residual value attached to the premises and their maintenance cost. We apply an EBIT margin of 85%, which is slightly higher than Befimmo and Cofinimmo (both 83%) owing to the fact that the buildings are fully let and need no marketing. Assuming the debt to be financed at a fixed 4% (OLO 10-year), we arrive at a net profit of € 16.6m – Befimmo share. If we subtract financing costs and the loss in rental income on the buildings swapped for shares in the State Sicafi, net profit could be up by € 4.8m (+10%). At first this would seem rather low, but one should not forget the impact of indexation: if rents and operational costs are indexed by 2% p.a. while debt is financed on a long-term basis at fixed rate, net profit of the State Sicafi could rise by 3% p.a.

Table 12: Impact of 2% yearly CPI indexation

	Year t	Year t+1	Year t+2	Year t+3
Rents	62,500	63,750	65,025	66,326
EBIT	53,125	54,188	55,271	56,377
Net financial	(20,000)	(20,000)	(20,000)	(20,000)
Net profit	33,125	34,188	35,271	36,377
<i>Chg % yoy</i>		3.21%	3.17%	3.13%
<i>Chg % cumulative</i>		3.2%	6.5%	9.8%

Source(s): Dexia estimates

VIII. VALUATION

VIII.1. Discounted cash flow

Company	Beta U
Inmobiliaria Colonial	0.58
Unibail	0.43
Silic SA	0.43
Sponda Oyj	0.38
Interinvest Offices	0.35
CA Immobilien Anlagen	0.33
Cofinimmo SA	0.32
Ivg Immobilien AG	0.31
Beni Stabili SpA	0.30
Vastned Offices Industrial	0.28
Nieuwe Steen Investments	0.28
Leasinvest	0.23
Offices avg	0.35

Source(s): Bloomberg, Dexia

- We arrive at a value of €741m, equivalent to 18x EBIT'06, taking into account a WACC of 6.5% based on our forecasted rise in the risk free (and consequently the CoE) and a cost of debt equal to risk free plus a credit spread of 50bps.
- The **cost of equity** is based on our assumptions for the European risk free rate (which we expect to climb to 5% by 2008), as stable long-term risk premium of 4% and a levered company beta which we expect to remain stable over time due to a constant gearing. We calculate an unlevered beta of 0.35 for the office players in the EPRA Euro index. This leads us to a CoE around 7.1%.
- We assume a growth rate of 2% for the next 10 years, after which it falls back to 0.33% for the infinity period, in line with the ROCE converging towards the WACC and in line with the formula: **growth = ROCE x (1- reinvestment rate)**.

Table 13: DCF valuation

Input parameters	2005A	2006E	2007E	2008E	2009E	2010E	2011E	20012E	2013E	2014E	2015E	TY
Risk free	3.30%	4.30%	4.40%	4.90%	5.20%	5.00%	5.00%	5.00%	5.00%	5.00%	5.00%	5.00%
Beta unlevered	0.35	0.35	0.35	0.35	0.35	0.35	0.35	0.35	0.35	0.35	0.35	0.35
Beta levered	0.51	0.53	0.53	0.53	0.53	0.53	0.53	0.53	0.53	0.53	0.53	0.53
D/E	47%	53%	53%	53%	54%	54%	54%	53%	53%	53%	52%	52%
tax	1.5%	1.5%	1.5%	1.5%	1.5%	1.5%	1.5%	1.5%	1.5%	1.5%	1.5%	1.5%
Risk premium	4.0%	4.0%	4.0%	4.0%	4.0%	4.0%	4.0%	4.0%	4.0%	4.0%	4.0%	4.0%
Cost of equity	5.3%	6.4%	6.5%	7.0%	7.3%	7.1%	7.1%	7.1%	7.1%	7.1%	7.1%	7.1%
Cost of debt	3.80%	4.80%	4.90%	5.40%	5.70%	5.50%	5.50%	5.50%	5.50%	5.50%	5.50%	5.50%
WACC	4.8%	5.8%	5.9%	6.4%	6.7%	6.5%	6.5%	6.5%	6.5%	6.5%	6.5%	6.5%
DCF Valuation model (k EUR)	2005A	2006E	2007E	2008E	2009E	2010E	2011E	20012E	2013E	2014E	2015E	TY
EBIT	66,142	62,504	65,270	66,504	68,265	69,630	71,023	72,443	73,892	75,370	76,877	
% chg	-1.5%	-5.5%	4.4%	1.9%	2.6%	2.0%	2.0%	2.0%	2.0%	2.0%	2.0%	
Taxes	(661)	(715)	(700)	(700)	(700)	(700)	(700)	(700)	(700)	(700)	(700)	
Normative tax rate %	1.3%	1.5%	1.4%	1.4%	1.4%	1.3%	1.3%	1.3%	1.2%	1.2%	1.2%	
NOPLAT	65,481	61,789	64,570	65,804	67,565	68,930	70,323	71,743	73,192	74,670	76,177	
+ depreciations & provisions	200	200	200	200	200	200	200	200	200	200	200	
- investments / + disposals	38,278	5,640	-	-	-	-	-	-	-	-	-	
- chg in working capital	1,909	(953)	(778)	(397)	(404)	(413)	(421)	(429)	(438)	(447)	(456)	
Unlevered FCF	105,868	66,676	63,993	65,607	67,360	68,718	70,102	71,514	72,954	74,423	75,922	75,922
WACC		5.8%	5.9%	6.4%	6.7%	6.5%	6.5%	6.5%	6.5%	6.5%	6.5%	6.5%
Discount factor		0.97	0.92	0.86	0.80	0.75	0.71	0.66	0.62	0.58	0.55	0.51
Actualized FCF		64,810	58,686	56,131	53,617	51,676	49,482	47,382	45,372	43,447	41,605	
NPV forecast period 2006-2015	512,209											
NPV residual	629,391											
Total DCF value	1,141,600											
- Net debt year-end 2005A	400,905											
- Minorities 2005A	-											
- Pension provisions	-											
+ Net deferred tax assets	-											
+ own shares	-											
Fair equity value	740,695											
no shares (m)	9.79											
Per share	76											

Source(s): Dexia estimates

Table 14: Sensitivity of DCF value to risk free rate, long-term growth and CoE

Sensitivity analysis	10-years rate from 2010					Sensitivity analysis	CoE TY				
	4.0%	4.5%	5.0%	5.5%	6.5%		6.0%	6.5%	7.1%	7.5%	8.0%
0.25	110	96	84	74	59	0.0%	85	79	73	69	64
0.30	104	91	80	71	56	0.4%	90	83	76	72	67
Beta U	0.35	98	86	76	67	0.5%	92	85	78	73	68
0.40	93	82	72	64	51	1.0%	101	92	84	79	73
0.50	84	74	66	58	47	2.0%	124	112	100	93	85

Source(s): Dexia estimates

State Sicafi could add € 9 to valuation (+12%)

- This valuation is based on our forecasts which do not include any investments. For example, if we were to include the State Sicafi into our valuation model under the conditions we mentioned, we would have a positive effect of € 9 per share (+12%). This is based on the assumptions that this deal would generate an incremental EBIT of € 48m (after accounting for the loss in rental income of the building swapped for shares in the new Sicafi). If we assume the WACC rises to 6.9% from 6.5% due to a higher portion of debt and a growth rate of 2%, the formula $\text{NOPLAT} / (\text{WACC}-g)$ would add € 987m on an EV level, from which would have to subtract minorities and debt totalling € 900m. This gives us ca € 88m, equivalent to € 9 per share.

VIII.2. Economic value added

Identifies at which premium/discount a property company should trade

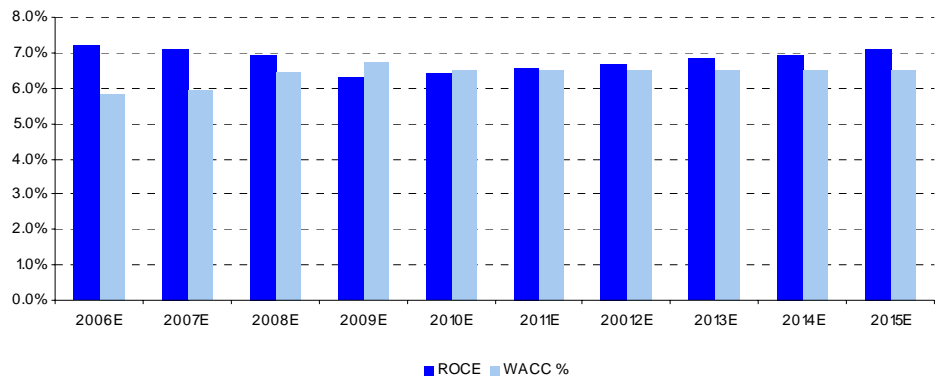
- The starting point for our EVA analysis is the EBIT which is essentially equal to net rental income minus direct operating costs and overhead expenses. Then we subtract taxes to arrive at the NOPLAT. However, we focus on total return so we include the portfolio result as well as we think it is an essential part of the value creation of real estate companies.
- We calculate capital employed as the NAV plus minorities, interest bearing debt and preference shares and subtract cash as the interest income on cash is not included in the EBIT.
- The economic value added is then calculated as the spread between the ROCE and WACC multiplied by capital employed. The terminal value is derived by dividing EVA of the final period by the WACC minus the terminal growth rate (see DCF Valuation).

Table 15: EVA Valuation

EVA Valuation model (k EUR)	2005A	2006E	2007E	2008E	2009E	2010E	2011E	20012E	2013E	2014E	2015E	TY
NOPLAT		61,789	64,570	65,804	67,565	68,930	70,323	71,743	73,192	74,670	76,177	
Capital return		13,725	10,647	8,471	-	-	-	-	-	-	-	
Total Return		75,515	75,217	74,275	67,565	68,930	70,323	71,743	73,192	74,670	76,177	
NAV	641,330											
Minorities	-											
Preference shares	-											
Interest bearing debt	413,680											
Cash	(12,775)											
Capital employed	1,042,235	1,051,595	1,063,020	1,071,887	1,072,292	1,072,705	1,073,125	1,073,555	1,073,992	1,074,439	1,074,895	
ROCE %		7.2%	7.1%	6.9%	6.3%	6.4%	6.6%	6.7%	6.8%	6.9%	7.1%	
WACC %		5.8%	5.9%	6.4%	6.7%	6.5%	6.5%	6.5%	6.5%	6.5%	6.5%	6.5%
EVA %		1.3%	1.1%	0.5%	-0.4%	-0.1%	0.0%	0.1%	0.3%	0.4%	0.6%	
EVA		14,087	12,062	5,259	(4,678)	(1,207)	159	1,555	2,981	4,436	5,921	95,418
Discount factor		0.97	0.92	0.86	0.80	0.75	0.71	0.66	0.62	0.58	0.55	0.51
NPV of EVA's		13,693	11,062	4,500	(3,723)	(908)	112	1,030	1,854	2,590	3,245	49,085
Capital employed	1,051,595											
NPV of EVA's	82,539											
Fair enterprise value	1,134,134											
- Net debt year-end 2005E	400,905											
- Minorities 2005E	-											
- Pension provisions	-											
+ Net deferred tax assets	-											
+ own shares	-											
Fair equity value	733,229											
no shares (m)	9.79											
Per share	75											

Source(s): Dexia estimates

Graph. 18: EVA analysis



Source(s): Dexia estimates

VIII.3. Required dividend yield spread

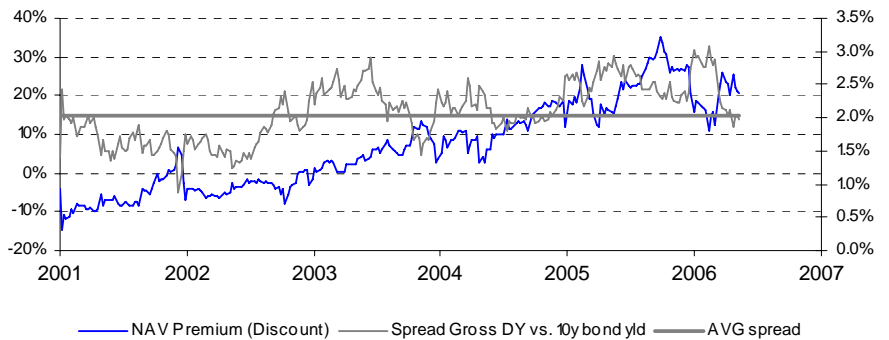
Expected yield spread

	Current	2006E	2007E
10-year bond yield	4.05%	4.30%	4.40%
Befimmo div yield	6.39%	6.39%	6.55%
Implied spread	2.34%	2.09%	2.15%

Source(s): Dexia estimates

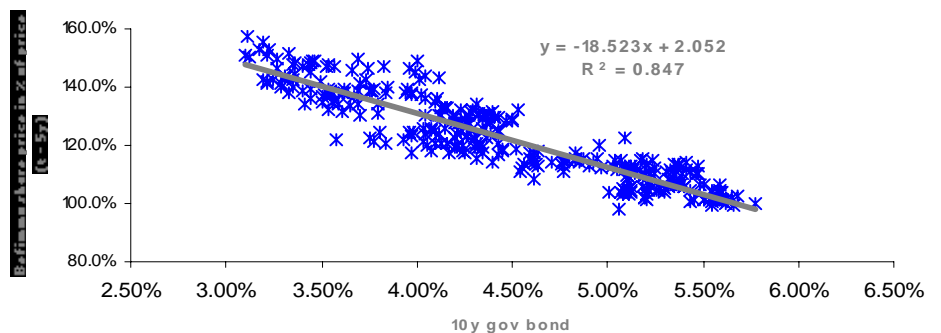
Although we acknowledge that DCF or EVA models are a better tool to determine the intrinsic value of a company, one should bear in mind that REITs with the profile of Befimmo (stable earnings, high payout, limited indirect result) are often treated by investors as a proxy for bonds. Therefore it is obvious that interest rate sensitivity is very high for this kind of stocks. We calculate a 5-year correlation of -0.90 to the 10-year bond yield based on weekly returns. In addition, medium-term history shows an implied yield spread for Befimmo of around 200bps on average (see graph 19). Under current market conditions this would imply a required yield of ca 6.1%, which is below the level where shares are trading right now (6.5%). This should leave some room to cushion the share price in case of further increase in long-term bond yields as is expected by our economist team.

Graph. 19: Market implied yield spread vs. 10-year government bond



Source(s): Dexia estimates, Bloomberg

Graph. 20: Share price sensitivity to 10-year bond yield



Source(s): Dexia estimates, Bloomberg

VIII.4. Relative multiples

Valued in line with its European peers on P/CF and EV/EBITDA

In this section we have put Befimmo in a European perspective using this and next year's forward estimates by comparing it with other office players in the EPRA Euro index. Two of its direct competitors on the Brussels market, Leasinvest RE (Neutral, PT € 65) and Cofinimmo (Neutral, PT € 130) are also included in this shortlist. Trading at 15.8x P/CF'06 and 18.2x EV/EBITDA'06, it appears that Befimmo is valued in line with its peers which are trading at 14.9x P/CF'06 and 18.2x EV/EBITDA'06 respectively. Its attraction lies in its defensive profile and its high payout, which makes it an attractive vehicle for yield investors who are looking for a secure income like for example pension funds.

Table 16: Relative valuation on 2006-2007E

	Market cap (€m)	P/CF		P/NAV		EV/EBITDA		Div yield	
		06E	07E	06E	07E	06E	07E	06E	07E
Befimmo	740	15.8	15.6	1.14	1.12	18.2	17.5	6.5%	6.6%
Beni Stabili SpA	1,393	13.6	13.6	0.77	0.74	18.7	18.1	2.6%	2.5%
Cofinimmo SA	1,454	16.2	15.5	1.19	1.17	21.5	19.5	5.8%	6.1%
Inmobiliaria Colonial SA	2,938	12.0	11.4	2.44	2.23	13.9	12.9	2.5%	2.6%
Intervest Offices	380	13.9	14.2	1.21	1.18	17.1	16.5	6.9%	7.1%
Ivg Immobilien AG	2,491	13.5	12.9	2.47	2.27	13.8	13.3	2.0%	2.1%
Leasinvest	211	19.1	14.5	1.12	1.09	25.1	17.4	5.8%	6.4%
Nieuwe Steen Investments	684	14.0	13.9	1.08	1.00	18.2	16.4	7.1%	7.2%
Silic SA	1,389	15.3	13.1	1.16	1.12	19.8	17.0	4.7%	5.0%
Sponda Oyj	608	12.0	11.7	1.05	0.95	17.3	17.3	5.2%	3.9%
Unibail	5,575	18.8	17.0	1.10	0.95	19.9	18.7	3.6%	4.0%
Vastned Offices Industrial	485	14.3	12.8	1.04	1.02	14.4	13.8	7.0%	8.2%
Offices avg		14.9	13.9	1.31	1.24	18.2	16.5	5.0%	5.1%
EPRA Euro avg		27.1	17.3	1.26	1.19	16.7	16.0	4.0%	4.3%

Source(s): Dexia estimates (Befimmo, Cofinimmo, Leasinvest), JCF Quant

IX. SWOT ANALYSIS

Strengths

- **Attractive regulatory framework** with the legal and fiscal advantages offered by the SICAFI status.
- **Good disclosure/transparency.**
- **Well-leased and medium-to-high quality** portfolio with high exposure (62%) to the a-cyclical CBD zone.
- **Strong maturity profile**, with an average period till first break standing at 6.4 years and 50% of contractual rents guaranteed till 2010.

Weaknesses

- **Debt is nearly entirely floating (85%)** with little protection from hedging instruments.
- **Little diversification** as the portfolio is focused on a single real estate type (offices) in a single market (Brussels).
- **Strong concentration of rental income**, but mainly towards AAA-tenants.

Opportunities

- A new Royal Decree with regard to the **loosening of the gearing threshold** (e.g. to 60% from 50%) could provide the necessary means to finance growth by debt.
- **Upside risk to the occupancy** in a Brussels rental market which is bottoming out.
- **Taking on commercial risks** by acquiring quality buildings at risk or by making off-plan purchases.
- **Expansion abroad (e.g. Luxembourg) or entering other segments** (e.g. senior homes) could diversify the asset base.
- **A more systematic hedging policy** could increase protection against rising interest rates.

Threats

- **Suitable investment opportunities are becoming scarce:** liquidities flooding the market push prices up and thereby create yield compression, making it difficult to source deals at a reasonable price.
 - **Rising interest rates** will cause a rise in net financial expense and could cause erosion of asset values, making the shares vulnerable for interest-rate hikes.
 - In the short-term, the **exposure to the weaker Brussels suburbs reveals some negative reversionary potential.**
-

Consolidated P&L (€m)	2004A	2005A	2006E	2007E	2008E
Rental income	78.6	79.2	76.4	78.1	79.6
Other income	0.0	0.0	0.0	0.0	0.0
Operating costs	-5.6	-6.8	-7.7	-6.4	-6.5
Corporate cost	-6.4	-6.3	-6.2	-6.4	-6.6
EBITDA	66.6	66.1	62.5	65.3	66.5
Depreciation	0.0	0.0	0.0	0.0	0.0
Amortisation	0.0	0.0	0.0	0.0	0.0
EBIT	66.6	66.1	62.5	65.3	66.5
Net Financial	-15.1	-15.5	-15.2	-16.7	-17.0
Revaluation of financial instruments	0.0	0.0	0.9	0.0	0.0
EBT	51.5	50.7	48.2	48.5	49.5
Taxes	-0.7	-0.7	-0.7	-0.7	-0.7
Equity method	0.0	0.0	0.0	0.0	0.0
Minorities	0.0	0.0	0.0	0.0	0.0
Dividend on preference shares	0.0	0.0	0.0	0.0	0.0
Direct investment result	50.8	50.0	47.5	47.8	48.8
Revaluation of property assets	-2.6	1.3	13.2	10.6	8.5
Book profits on asset disposals	2.6	12.7	0.5	0.0	0.0
Portfolio result	0.0	14.0	13.7	10.6	8.5
Net profit - group share	50.8	64.0	61.2	58.5	57.3
Cash Flow (€m)	2004	2005A	2006E	2007E	2008E
Cash flow from operations	50.8	50.0	46.8	48.0	49.0
Change in working capital	-0.4	1.9	-1.0	-0.8	-0.4
Cash from operating activities	50.4	51.9	45.8	47.3	48.6
Cash from investing activities	-69.0	50.9	6.1	0.0	0.0
Free cash flow before financing	-18.6	102.8	52.0	47.3	48.6
Cash from financing activities	2.0	-102.7	-47.0	-48.2	-49.4
Change in interest bearing debt	47.2	-55.7	0.0	0.0	0.0
Change in cash	-16.6	0.1	5.0	-0.9	-0.8
Balance sheet (€m)	2004	2005A	2006E	2007E	2008E
Market value of property assets	1,125.3	1,063.2	1,070.8	1,081.5	1,089.9
Revaluation of property assets	-2.6	1.3	13.2	10.6	8.5
<i>as a % of the portfolio</i>	<i>-0.2%</i>	<i>0.1%</i>	<i>1.2%</i>	<i>1.0%</i>	<i>0.8%</i>
Sh. Equity	603.8	641.3	655.5	665.8	673.7
Minority interest	0.0	0.0	0.0	0.0	0.0
Provisions & deferred taxes	2.4	0.0	0.0	0.0	0.0
Net financial debt	467.3	400.9	395.9	396.8	397.6
Investment capacity (50% threshold)	92.0	105.4	117.2	125.2	130.5
Investment capacity (60% threshold)	401.2	404.9	423.3	435.8	444.5
Per share data	2004	2005A	2006E	2007E	2008E
Number of shares (m)	9.79	9.79	9.79	9.79	9.79
EPS (recurring)	5.18	5.11	4.76	4.88	4.98
CFPS	5.18	6.40	4.83	4.90	5.00
NAVPS (before profit distribution)	63.0	65.5	66.9	68.0	68.8
DPS	4.62	4.80	4.92	5.04	5.17
Payout %	89%	94%	103%	103%	104%
Financial ratios	2004	2005A	2006E	2007E	2008E
Total debt-to-total assets	46%	45%	45%	44%	44%
Net debt/Equity	77%	63%	60%	60%	59%
Net debt/EBITDA	7.0	6.1	6.3	6.1	6.0
Interest cover (EBIT/int. exp.)	4.4	4.3	4.1	3.9	3.9
ROE %	8.4%	10.4%	9.7%	9.1%	8.8%
Valuation ratios	2004	2005A	2006E	2007E	2008E
Market cap	710.7	857	744	744	744
EV	1178.1	1,258	1,140	1,141	1,142
EV/EBITDA	17.9	19.0	18.2	17.5	17.2
P/E	14.0	17.1	16.0	15.6	15.3
P/CF	14.1	13.7	15.7	15.5	15.2
P/NAV	118%	133.6%	113.5%	111.8%	110.5%
Dividend yield %	6.37%	5.49%	6.47%	6.63%	6.80%

COVERAGE BY PRIMARY ANALYST

Mickael Van den Hauwe: Real Estate
Companies covered: Atenor, Befimmo, Cofinimmo, Leasinvest, WDP, Arcelor

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I, Mickael Van den Hauwe, hereby certify that the views expressed in this research report accurately reflect my personal opinion about the companies and the securities discussed herein. This report has been submitted to the issuer of the financial instrument it relates to before its publication. Like all employees of Dexia Bank Belgium, the remuneration can be base in part on the results of Dexia Bank Belgium as a whole, which may include investment banking revenues. I certify that I do not hold, directly or indirectly, any interest in the companies mentioned above. However, no part of my compensation was or is related to any recommendation or opinion expressed in this report.

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RECOMMENDATIONS

We use four stock recommendations which reflect the share's expected absolute performance as follows:

Buy: we expect this stock to generate a return of >15% over the next twelve months

Add: we expect this stock to generate a return of 5-15% over the next twelve months

Neutral: we expect this stock to generate a return of 0-5% over the next twelve months

Reduce: we expect this stock to generate a negative return over the next twelve months

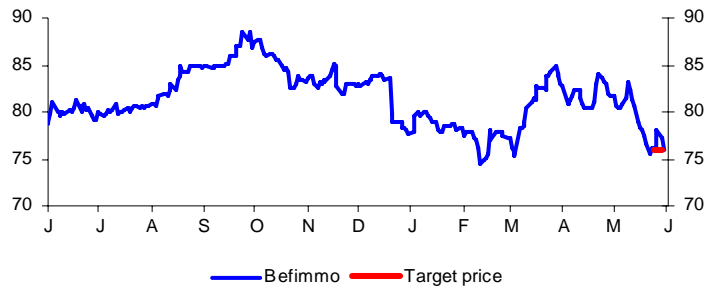
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As of April 1, 2005, the Dexia Bank Belgium equity research has active investment recommendations on [29] securities. Our recommendation on two stocks is currently inactive. We disclose the percentage of rated securities to which we assign a Buy, Add, Neutral and Reduce rating on a quarterly basis. We also include the recommendation composition on securities for which Dexia Bank Belgium has undertaken investment banking actions over the last twelve months.

Rating category	Buy	Add	Neutral	Reduce
Rating distribution	24.1%	37.9%	24.1%	13.8%
Investment banking relationship	28.5%	28.5%	14.2%	28.5%

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12-MONTH PRICE TARGET CHART

Date	Target price
31-May-06	76

Source : Bloomberg

HISTORY OF RECOMMENDATIONS

Befimmo's stock has been covered by Mickael Van den Hauwe as from May 31, 2006.

Date	Recommendation
31-May-06	Neutral

Research & Sales

EQUITY RESEARCH

Head of research

Steven De Proost +32/2/222.02.55

Real estate

Mickael Van den Hauwe +32/2/222.33.95

Utilities

Steven De Proost +32/2/222.02.55

Construction

Pieter Bijlsma +32/2/222.31.67

Healthcare

Koen Wuyts +32/2/222.33.18

Telecom

Rob Goyens +32/2/222.03.47

Small & Mid caps, Belgium

Peter Van Assche +32/2/222.33.16

Maurice Rosenthal +32/2/222.33.12

EQUITY SALES

Manager Sales & Trading

Benjamin Vierendeel +32/2/222.84.24

Head of sales

Guy Noerens +32/2/222.71.73

Equity sales

Guy Noerens +32/2/222.71.73

Olivier Schoevaerdt +32/2/222.70.20

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