Befimmo

ADD (+)

02 February 2007

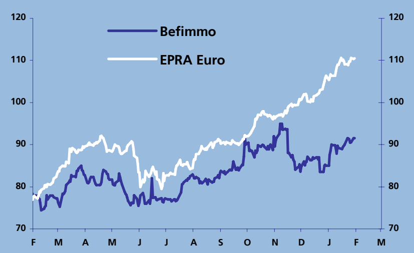
Belgium
Real Estate

Price	**€ 89.0**
Price target	**€ 92.0 (+)**

Market cap (€ m)	891.3
N° of shares (m)	9.794
Daily volume	12,197
Free float	84%
Reuters	BEFIt.BR
Bloomberg	BEFB BB

Performance Befimmo

- 1M	6.53%	- 3M	-1.58%	YTD	6.53%



Back in business!

While Befimmo has wrong-footed investors with regard to its dividend policy, we believe this will be downplayed by recent substantial deal flow after three years of inactivity on the investment front. The Fedimmo deal will most likely change investors' perception towards the stock as it will considerably improve the company's visibility and overall risk profile besides growing cash flows by 5-6% p.a. Our updated DCF-model echoes a fair value of €92 per share (from €82) which is where we set our new target price. As this leaves us with 8.4% total return potential we increase our rating to Add from Reduce.

€	2006A	2007E	2008E	2009E
EPS (recurring)	4.85	4.58	4.28	4.45
CFPS	4.87	4.60	4.29	4.47
NAV	67.4	72.8	74.3	75.9
Dividend	4.92	4.45	4.50	4.55
Net income (m)	47.5	47.5	51.7	53.9
P/E	18.5	19.4	20.8	20.0
CF yield	5.4%	5.2%	4.8%	5.0%
EV/EBITDA	20.4	21.7	20.4	20.3
P/NAV	1.34	1.22	1.20	1.17
Div. Yield	5.5%	5.0%	5.1%	5.1%

- **Fedimmo transaction.** Befimmo has acquired a 90% stake in this special purpose vehicle which owns a portfolio of office buildings let to Belgian government bodies with an average lease length of 17 years. Assuming a €200m capital increase in order to bring post-deal gearing back to an acceptable level, we estimate impact on cash flows should amount to 5-6% p.a.

- **Solid and defensive.** We believe the Fedimmo acquisition perfectly fits within Befimmo's strategy of securing quality long-term cash flows and will strengthen its visibility and overall risk profile. Its excellent earnings quality (53% CBD exposure, 66% public tenants, superb maturity profile) should allow the stock to trade at a higher multiple.

- **Investment case revisited.** In our view investors should take a longer-term view on the stock as the announced refurbishments both at Befimmo and Fedimmo level might weigh on results in the first years but will ultimately create strong shareholder value. We upgrade our rating to Add from Reduce and set our new DCF-based target price at €92, implying an estimated total return of 8.4%. From a relative valuation perspective, we point to its appealing 2007E 5.2% cash flow yield (vs. EPRA Euro: 4.6%) and would recommend investors to switch from Cofinimmo (Reduce, PT of € 138, 4.8% div yield) into Befimmo (5.0% div yield).

- **Further triggers.** Fedimmo earnings upgrades, the tender for Fedimmo II (€300m) which is scheduled to take place before the elections in June or additional investments in Luxembourg could trigger a higher valuation.

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Equity Research
Focus

DEXIA

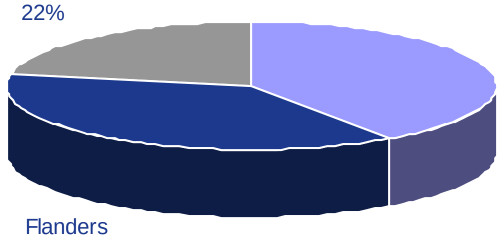
I. FEDIMMO: VENI, VIDI, VICI…

I.1. Fedimmo: quid?

Fedimmo will strengthen Befimmo's business profile and visibility

Late December 2006, Befimmo announced it had won the Fedimmo auction. The latter is a special purpose vehicle set up by the Belgian State that owns 62 office buildings let to Belgian government bodies with an average lease length of 17 years. The total GLA amounts to 382,000m² (vs. Befimmo: 523,000m²) of which 40% in Brussels (9 buildings), 38% in Flanders (34) and 22% in Wallonia (19). The portfolio also includes the right to build on the WTC 4 plot (39,000m²). Spot occupancy stands at 100% but we understand that in the first three years about 13% is about to be vacated and these premises will need to be redeveloped in order to bring them back to market standards. Note that the deal also includes a contractual obligation to cope with €50m refurbishments in the Fedimmo portfolio within the first three years of its existence.

Graph 1: Fedimmo portfolio breakdown by GLA (m²)



Source(s): Befimmo

I.2. Nice deal…

At a 5.5% entry yield this acquisition is not a bargain…

Befimmo will acquire a 90% stake in Fedimmo for an amount of €576m whilst the Belgian government will hold the remainder of the shares. While it was originally foreseen in the State Sicafi deal that the Belgian government would hold a blocking minority, this won't be the case for Fedimmo as we understand that one share equals one vote. The Belgian State will however be entitled to appoint two out of the six Board members of Fedimmo.

Fedimmo is structured as a limited liability company and according to a fiscal ruling it will have to keep this status for a minimum of three years. As a result Fedimmo won't be eligible to reside under the Sicafi regime and should thus normally pay taxes until it will be absorbed by Befimmo after this lock-up period. However, as the buildings will be depreciated at Fedimmo level (not at a consolidated level) and due to the notional interest tax deduction scheme, there won't be any tax leakage. Befimmo will keep the gearing low in its Fedimmo subsidiary, pushing most of the debt at the parent company and the equity at Fedimmo level, in order to prevent tax outgoings. Consequently, Befimmo will fully consolidate Fedimmo into its accounts. This structure is in our view more transparent and cost-efficient than the original plans for the State Sicafi operation, which took into account a separate listing and this would also have diluted Befimmo's stake due to the minimum 30% free float requirement for Belgian REITs.

…but is in line with prevailing market yields for LT office leases

The balance sheet impact will be enormous as the overall portfolio value will take a giant 68% leap to €1.8bn. This is nearly equal to the €2bn portfolio of closest peer Cofinimmo after the latter disposed 10% of its asset base last month. Since the portfolio will increase by € 730m and Befimmo will pay €576m for its 90% stake, this implies €64m of minorities and €90m of debt related to a financial lease obligation at Fedimmo. Befimmo will in a first instance finance the acquisition with a bridge loan but has already hinted towards a capital increase in the next months as its gearing will jump to 60% (see table below) or 62% based on Q1'06/07 when the balance sheet equity is lowered through the dividend payment.

Table 1: Befimmo – balance sheet impact assuming full debt financing

	Befimmo 2006A	+ Fedimmo	Befimmo consolidated	+ Axento + renovations + revaluations	Befimmo consolidated
Buildings	1,078	730	1,808	312	2,120
Goodwill	-		-		-
Other non-current assets	2		2		2
Other current assets	13		13		13
Cash	15		15		15
Total assets	**1,109**	**730**	**1,839**	**312**	**2,151**
Equity	660	-	660	81	742
Minorities	-	64	64		64
Financial debt	409	576	985	230	1,215
Other liabilities	37	90	127		127
Accrued liabilities	3		3		3
Total liabilities	**1,109**	**730**	**1,839**	**312**	**2,151**
Debt ratio	40.2%		60.4%		62.4%

Source(s): Dexia estimates

Befimmo will tap the equity markets to finance the acquisition

While still below the 65% legal threshold this level of indebtedness is too high for a REIT with such a defensive profile. Moreover, in the next three years the company also has to deal with its own renovation programme (€63m), refurbishments in Fedimmo buildings (€72m, of which €50m committed) and the Axento project in Luxembourg (€95m). We have assumed a capital increase of €200m which would bring back the gearing to a realistic 50% by the end of 2007. Taking into account the above mentioned investments its debt ratio would by 2010 still be acceptable at 53% (see table below). Note that this figure arguably assumes a 2% annual value uplift for the existing portfolio, which should in our view be taken into account as well. Alternatively Befimmo could also dispose some of its assets but has up till now not made any insinuations in this direction.

Table 2: Befimmo – balance sheet impact assuming € 200m capital increase

	Befimmo 2006A	+ Fedimmo	Befimmo consolidated	+ Axento + renovations + revaluations	Befimmo consolidated
Buildings	1,078	730	1,808	312	2,120
Goodwill	-		-		-
Other non-current assets	2		2		2
Other current assets	13		13		13
Cash	15		15		15
Total assets	**1,109**	**730**	**1,839**	**312**	**2,151**
Equity	660	200	860	81	942
Minorities	-	64	64		64
Financial debt	409	376	785	230	1,015
Other liabilities	37	90	127		127
Accrued liabilities	3		3		3
Total liabilities	**1,109**	**730**	**1,839**	**312**	**2,151**
Debt ratio	40.2%		49.6%		53.1%

Source(s): Dexia estimates

I.3. …but some issues remain

The portfolio will require intense management…

- **Litigation risk.** After the State Sicafi debacle one could fear legal objections from the other bidders (Axa and Cofinimmo). However, as the Fedimmo tender was organized as a straightforward auction process with the price being the sole criterium it would be difficult to make a strong case to fight the outcome. Moreover, Cofinimmo has already renounced to file any complaints.

- **Need for funding.** Fedimmo is a big transaction for Befimmo to digest. While its balance sheet capacity would in fact allow it to absorb such a large asset, but in order not to jeopardize its financial profile Befimmo will have to tap the equity markets to partially fund the acquisition.

- **Renovation programme.** In the first three years refurbishments will need to be carried out for an amount of €52m but these will be compensated by higher rents. We estimate this should bring an additional €3.5m in revenues.

- **Vacancy risk.** About 50,000m² (13% of Fedimmo portfolio) is about to be vacated by their occupants in the first three years and these will need to be redeveloped. This implies that at Fedimmo level the company will incur higher direct property costs due to vacancy (5% p.a. assumed) and higher financing charges as a result of additional capex required to re-let the premises which we assess at €22m.

…but hard work will only unlock further value

- **Arbitrage.** We believe the buildings in the Fedimmo portfolio do not all fit in Befimmo's strategy of securing office buildings at prime locations that can be let on long-term leasing contracts. While some of these assets could be re-developed into residential, this does not fit within the company's strategy. Most likely Befimmo will make an analysis on an asset-per-asset base and start disposing peripheral assets in the medium-term. Concerning the WTC 4 plot, we would not expect any building plans to unfold in the near term given the vast amount of development projects in the North district. Perhaps Befimmo could sell the plot of land to a developer like Atenor (Buy, PT of €37.5).

- **No absorption possible before 2010.** While there won't be any tax leakage on Fedimmo level, one should beware that as a plain public limited company instead of a REIT, it will have to write down the buildings. This has two direct consequences. Firstly, this will depress the book value and increase the taxable base for the calculation of the exit tax (16.995%) which we estimate at €13m when the SPV will be absorbed by Befimmo in 2010. Secondly, the depreciations will also lower the distributable result at Fedimmo and we wonder if this won't cause any conflicts with regard to the dividend Befimmo pays on a consolidated level.

- **Quid valuation?** While we believe the 5.5% entry yield is quite expensive, we have to acknowledge that this price is market conform especially when taking into account recently reported transactions. In our view the price paid is fair when taking into account the average lease length of 17 years and the triple-A tenant, but we believe this is not the case when taking into account the average quality and location of the buildings. We also point out that the expert appointed by the Belgian State (DTZ) originally valued the buildings at 6.9%, so one could wonder if the expert appointed by Befimmo won't be reluctant to push valuation towards these high levels. Nevertheless, Befimmo management confirmed that JLL will value the Fedimmo portfolio at 5.5% so there will neither be any recognition of goodwill on its balance sheet nor any negative revaluations.

I.4. Financial impact

Initial financial impact is modest…

According to Befimmo, the transaction should increase its cash flow per share by €0.20 to 0.30 (+4.5 to +6.5% vs. pre-deal) as from the current fiscal year. This is quite low in our view especially in the light of the impressive effect on its portfolio size (+68%) and the efforts that it will take to manage this transaction. One could also look at this another way: investing at a 5.50% entry yield and assuming 50bps costs nearly equals a 75bps spread over 5-year SWAP rates (4.25%), which is not attractive in our view. In addition, we also have some sympathy with the view that EPS accretion may not necessarily imply value accretion. But contrary to this, we do believe this transaction will add shareholder value for the following reasons:

- The initial impact on cash flows does not take into account the renovation programme which will be compensated for through higher rents. We calculate this would increase the entry yield by 15-30 bps.
- One should not forget the leveraged impact on cash flows of CPI indexation (3.0-3.5% p.a.).

…but does not take into account the longer-term value creation

- The assets will appreciate slowly but steadily over time ensuring sound long-term NAV growth.
- The Fedimmo transaction will further lower Befimmo's risk profile (triple-A tenant, superb maturity profile) under the assumption that leverage is kept under control. This should bring down the WACC through a lower beta and should ultimately translate into a higher trading multiple.

With the limited data available we have tried to sketch an overall portrait of how Befimmo's P&L would look like post-deal. We also want to add that we have addressed management with the issue of limited guidance on the operation and they reassured us that they are in the middle of preparing a detailed overview of the transaction which will be presented in the next months.

Below we have tried to gauge the impact on Befimmo's financials taking into account the following assumptions for Fedimmo:

- Annualized rental level in 2007: €40m
- A stable 5% vacancy as from 2008 which we consider as quite cautious. Assuming an occupancy of 100% would feed the bottom line by another 3-4%.
- Indexation at 2% p.a.
- €72m refurbishments spread over 2007-09 compensated for by higher rents
- Direct property costs equal to 5% of net rents
- Annual overhead cost of 0.50% of the portfolio value based on the valuation by DTZ. This percentage is in line with the historical level at Befimmo.
- A capital increase of €200m leading to the creation of 2,299k new ordinary shares. This implies an issue price or €87, i.e. 3.3% discount on the average share price of €90 YTD.
- 3M-Euribor gradually rising to 4.0% by 2009 and an 18bps spread on CP.
- €13m exit tax in 2010 which we have included in the capex line
- No portfolio revaluations which is extremely cautious but first we want to learn more about the quality of the buildings and their expected terminal value. We do however not expect any negative revaluations when interest rates move up further as indexation and higher rents from refurbishments will automatically cause yield expansion which should act as a buffer.
- Annual tax outgoings of €200k.

Table 3: Combined P&L Befimmo-Fedimmo assuming € 200m capital increase

Fedimmo stand-alone - Pro forma P&L (€ m)

	2007E	2008E	2009E	2010E
Rents	30.2	41.8	40.5	43.7
real estate charges	(1.5)	(2.1)	(2.0)	(2.2)
corporate cost	(2.2)	(3.0)	(3.0)	(3.1)
EBIT	26.5	36.7	35.4	38.4

Befimmo stand-alone - Pro forma P&L (€ m)

	2007E	2008E	2009E	2010E
Rents	76.2	75.1	80.8	88.5
real estate charges	(7.9)	(9.2)	(6.8)	(9.1)
corporate cost	(8.0)	(7.6)	(7.6)	(8.0)
EBIT	60.2	58.4	66.4	71.4

Befimmo consolidated - Pro forma P&L (€ m)

	2007E	2008E	2009E	2010E
Rents	106.4	116.9	121.3	132.2
real estate charges	(9.4)	(11.3)	(8.9)	(11.2)
corporate cost	(10.2)	(10.6)	(10.6)	(11.1)
EBIT	86.8	95.1	101.8	109.8
- net financial (*)	(20.8)	(24.1)	(28.4)	(31.7)
- financing Fedimmo stake (**)	(15.2)	(15.2)	(15.7)	(15.7)
EBT	50.7	55.9	57.7	62.4
- taxes	(0.8)	(0.8)	(0.8)	(0.8)
- minorities	(2.4)	(3.3)	(3.0)	(3.2)
net direct result	47.5	51.7	53.9	58.3
existing # shares	9.794	9.794	9.794	9.794
additional # shares	2.299	2.299	2.299	2.299
pro-rata # shares	10.369	12.093	12.093	12.093
EPS new	4.58	4.28	4.45	4.82
chg yoy	-5.5%	-6.7%	4.1%	8.3%
EPS pre-Fedimmo	4.35	4.03	4.35	4.63
chg abs	0.23	0.25	0.11	0.19
chg rel	5.3%	6.1%	2.5%	4.2%

(*) Includes interest payments on existing Befimmo debt, Axento project, all renovation spending at Befimmo and Fedimmo and the financial lease obligation at Fedimmo level
(**) €200m capital increase takes place at the end of Q3'06/07

Source(s): Dexia estimates

In the table below we have tried to measure the impact of the capital increase on the EPS accretion. As Befimmo and most publicly traded real estate companies are trading at record premiums to NAV we have also inserted a column in which we have computed the new premium to spot NAV. Taking into account our core scenario of a €200m capital increase the premium to spot NAV should drop from 32% to 25%. We also stress that we believe investors should not attach a great significance to the premiums to published NAVs, especially those of Belgian REITs, as the experts are extremely cautious. Moreover, as the latter have a backward looking approach, it takes some time to catch up with reality so we strongly wonder if the published NAV provides us with a true valuation yardstick.

Table 4: Scenario analysis – impact capital increase on EPS & premium to spot NAV

Capital increase (€ m)	2007E	2008E	2009E	2010E	NAV premium
-	6.8%	10.7%	7.1%	10.7%	32%
50	6.4%	9.4%	5.8%	8.8%	30%
100	6.0%	8.1%	4.6%	7.1%	28%
150	5.6%	7.1%	3.5%	5.6%	27%
200	5.3%	6.1%	2.5%	4.2%	25%
250	4.9%	5.2%	1.6%	2.9%	24%

Source(s): Dexia estimates

II. PORTFOLIO DEVELOPMENT

News flow has been substantial in recent months with the announcement of an acquisition in Luxembourg and the refurbishment programme in a number of its existing Brussels CBD assets. We have discussed these topics here below.

❒ Axento – €95.4m investment

We might see some additional investments in Luxembourg

…as management indicated it wants to create a strong foothold in its second home market

In December Befimmo announced it had closed a deal to acquire a 12,100m² mixed project Axento (10,500m² offices/1,600m² retail) for €95.4m which will be developed by CIP Luxembourg. Befimmo will forward fund 15% as from 2007 and will pay the remainder at delivery. Construction works should start end 2007 after permits have been obtained and delivery is scheduled for H1'09. Taking into account an 18-month rental guarantee the transaction should impact yearly cash flows by 3.4% (pre-Fedimmo). Despite the fact that the impact won't be fully visible until FY'09/10 we are bullish on the operation as we believe Befimmo has closed this deal at attractive conditions. No capitalization rate was disclosed (Dexia est.: 5.7%), but a 3.4% impact on cash flows (€1.5m) is equivalent to 150bps spread over financing, which is attractive taking into account the prime quality and location of the project. Note that Befimmo will still need some fiscal creativity to prevent tax leakage as is can not benefit from its Belgian REIT status in Luxembourg, but we believe this should pose no problem.

❒ Extension Justice - €19.9m renovation

The Ministry of Justice will vacate the premises after the lease matures in March 2008. Befimmo will then start a full renovation of the building, for which the necessary permits have already been obtained. This will lead to a 2-year loss in rents, but afterwards we expect Befimmo to increase rents to €/m² 210 vs. €/m² 165 as of today.

❒ Brederode II - €3.3m refurbishment

Renovation works will start in Q2'06/07 when the current tenants have left the building and will last about 1 year. Currently the surfaces are already rented at about €/m² 230 so we do not expect a dramatic increase after refurbishments.

❒ WTC - €19.6m renovation

Previously Befimmo already announced that the The Post will transfer its lease to the Belgian State Buildings Agency. The Post will gradually move out of Tower II from June 2007 till December 2008 and during this vacant period Befimmo will carry out refurbishments. This will impact the P&L through a temporary loss in rents, higher real estate costs borne by Befimmo and an increase in financial expenses due to funding requirements. Afterwards, the rental level will be adjusted to market rates while the initial lease was also extended by two years till 2018. Note that the loss in cash flow will be offset by an increase in value of the building.

❒ Central Gate - €20.0m renovation

Renovation works are required to bring the premises back to market standards and will be scheduled from 2008 till 2010. Befimmo will phase the works in function of tenant movements in order to minimize temporary vacancies. We are banking on a strong rise in rental levels afterwards to at least €/m² 180 vs. the current low €/m² 140 and expect the occupancy rate (spot rate: 75%) to improve.

III. VALUATION

❒ DCF value - € 92 per share

Our DCF model is built upon on the following conservative assumptions:

- The cost of equity is based on our assumptions for the European risk free rate (which we expect to climb gradually to 5% by 2010), a stable risk premium of 4.0% and a levered beta of 0.5.
- We calculate a dynamic WACC in function of the company's gearing evolution, which is expected to remain stable over time (D/E = 90%)
- Our TY cost of equity and WACC work out at 6.8% and 6.2% respectively.
- A growth to infinity of 2.0%
- Our assumptions with regard to capex are detailed above. We use a normalized capex of €2.5m from 2011 onwards.
- A capital increase of €200m leading to the creation of 2,299k new ordinary shares. This implies an issue price or €87, i.e. 3.3% discount on the average share price of €90 YTD.

Table 1: DCF valuation

DCF Valuation model (k EUR)	**2006A**	**2007E**	**2008E**	**2009E**	**2010E**	**2011E**	**20012E**	**2013E**	**2014E**	**2015E**
EBIT	62,504	86,763	95,098	101,830	109,846	114,611	116,923	119,281	121,687	124,141
% chg	*-5.5%*	*38.8%*	*9.6%*	*7.1%*	*7.9%*	*4.3%*	*2.0%*	*2.0%*	*2.0%*	*2.0%*
Taxes	(715)	(800)	(800)	(800)	(800)	(800)	(800)	(800)	(800)	(800)
Normative tax rate %	*1.5%*	*1.6%*	*1.4%*	*1.4%*	*1.3%*	*1.2%*	*1.2%*	*1.1%*	*1.1%*	*1.0%*
NOPLAT	61,789	85,963	94,298	101,030	109,046	113,811	116,123	118,481	120,887	123,341
+ depreciations & provisions	200	200	200	200	200	200	200	200	200	200
- investments / + disposals	5,640	(617,680)	(53,450)	(125,070)	(23,000)	(2,500)	(2,500)	(2,500)	(2,500)	(2,500)
- chg in working capital	(953)	(1,061)	(583)	(605)	(659)	(685)	(699)	(713)	(727)	(742)
Unlevered FCF	66,676	(532,578)	40,465	(24,444)	85,587	110,825	113,124	115,468	117,860	120,299
WACC		5.3%	5.6%	6.0%	6.2%	6.2%	6.2%	6.2%	6.2%	6.2%
Discount factor		1.00	0.95	0.89	0.84	0.79	0.74	0.70	0.66	0.62
Actualized FCF		**(532,578)**	**38,305**	**(21,775)**	**71,551**	**87,284**	**83,933**	**80,710**	**77,611**	**74,631**

NPV forecast period 2007-2015	(40,328)
NPV residual	1,694,770
Total DCF value	**1,654,442**
- Net debt	393,803
- Minorities	64,000
- Pension provisions	-
- Financial lease obligation	90,000
+ Net deferred tax assets	-
+ own shares	-
Fair equity value	**1,106,639**
no shares (m)	12.093
Per share	**92**

Source(s): Dexia

IV. INVESTMENT CASE

Drastic dividend guidance…

At the announcement of the 2006 annual results in November Befimmo management made a drastic U-turn with regard to its dividend guidance. While it had always indicated that the yearly 2.5% dividend growth was secured by capital gains on the sale of the Borschette building, the 2007 dividend forecast was cut by 12% to €4.45 from €5.04 in order to bring the dividends in line with recurring cash flows. The underlying reason, besides having been unable to reinvest the proceeds from asset disposals and the newly announced refurbishment programme, were rising short-term interest rates. As we were already anticipating this in our forecasts, we hope management will not make the same mistake twice as a closer look to its annual report shows that the updated guidance takes into account an average level for 3M-Euribor for 2007-2009 of 3.70% vs. a spot rate of 3.78% and a forward curve pointing towards 4.0%+.

…but positive news flow will change investors' sentiment towards the stock

While Befimmo has wrong-footed investors with regard to its dividend policy, we believe this will be downplayed by recent substantial deal flow. After three years of inactivity on the investment front, latest acquisitions will most likely change investors' perception towards the stock. We believe the Fedimmo acquisition perfectly fits within Befimmo's strategy of securing quality long-term cash flows and will strengthen its overall risk profile which should allow its stock to trade at a higher multiple. In addition, in our view investors should take a longer-term view on the stock as the announced refurbishments both at Befimmo and Fedimmo level might depress the P&L in the first years but will ultimately create strong shareholder value. We upgrade our rating to Add from Reduce and set our new DCF-based target price at €92, implying an estimated total return of 8.4%. From a relative valuation perspective, we point out its appealing 2007E 5.2% cash flow yield (vs. EPRA Euro: 4.6%) and would recommend investors to switch from Cofinimmo (Reduce, PT of € 138, 4.8% div yield) into Befimmo (5.0% div yield).

V. SWOT

Strengths

- **Attractive regulatory framework** with the legal and fiscal advantages offered by the SICAFI status.
- **Well-leased and medium-to-high quality portfolio** with high exposure (53%) to the a-cyclical Brussels CBD zone and a high proportion of triple-A tenants (66% public sector).
- **Superb maturity profile,** with an average period till first break standing at 10.1 years.
- **Reliable real bond proxy**, offering steady dividend growth of 2-3% p.a.

Weaknesses

- **Debt is nearly entirely floating (85%)** with little protection from hedging instruments (cap at 5%), although improved recently (twin caps at 3.5-5.0% for €200m).
- **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 triple-A tenants.
- **Management needs to restore credibility** after the unexpected drastic cut in its dividend guidance (-12%) although this might be overshadowed by recent substantial deal flow.

Opportunities

- **Upside risk to the occupancy** in a Brussels rental market which is modestly recovering.
- **Taking on commercial risks** by acquiring quality buildings at risk or by making off-plan purchases.
- **Further development of the presence in Luxembourg or entering other segments** (e.g. senior homes).
- **Renovation programme** for the existing portfolio is underestimated.

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.
- **Capital market risk:** need for equity issuance in order to finance the Fedimmo acquisition.

Consolidated P&L (€ m)	2005A	2006A	2007E	2008E	2009E
Rental income	79.2	76.3	106.4	116.9	121.3
Other income	-	-	-	-	-
Operating costs	(7.3)	(6.8)	(9.4)	(11.3)	(8.9)
Corporate cost	(5.8)	(7.0)	(10.2)	(10.6)	(10.6)
EBITDA	66.1	62.5	86.8	95.1	101.8
Depreciation & amortization	-	-	-	-	-
EBIT	66.1	62.5	86.8	95.1	101.8
Net Financial	(15.5)	(14.3)	(36.0)	(39.2)	(44.2)
Revaluation of financial instruments	-	-	-	-	-
EBT	50.7	48.1	50.7	55.9	57.7
Taxes	(0.7)	(0.6)	(0.8)	(0.8)	(0.8)
Equity method	-	-	-	-	-
Minorities	-	-	(2.4)	(3.3)	(3.0)
Dividend on preference shares	-	-	-	-	-
Direct investment result	50.0	47.5	47.5	51.7	53.9
Revaluation of property assets	1.3	18.0	20.2	20.3	20.4
Book profits on asset disposals	12.7	0.5	-	-	-
Portfolio result	14.0	18.5	20.2	20.3	20.4
Net profit - group share	64.0	66.0	67.7	72.0	74.3

Cash Flow (€ m)	2005A	2006A	2007E	2008E	2009E
Cash flow from operations	50.0	47.7	50.1	55.3	57.1
Change in working capital	1.9	-	(1.1)	(0.6)	(0.6)
Cash from operating activities	51.9	47.7	49.1	54.7	56.5
Net (investments) / disposals	50.9	5.6	(617.7)	(53.5)	(125.1)
Free cash flow before financing	102.8	53.4	(568.6)	1.3	(68.6)
Dividends	(45.2)	(47.0)	(48.2)	(53.8)	(54.4)
Equity issuance / (share buy back)	-	-	200.0	-	-
Change in interest bearing debt	(55.7)	-	417.7	53.5	125.1
Cash from financing activities	(100.9)	(47.0)	569.5	(0.4)	70.7
Change in cash	1.9	6.3	0.9	0.9	2.1

Balance sheet (€ m)	2005A	2006A	2007E	2008E	2009E
Market value of property assets	1,063.2	1,078.4	1,870.2	1,944.0	2,089.5
Revaluation of property assets	1.3	18.0	20.2	20.3	20.4
as a % of the portfolio	*0.1%*	*1.7%*	*1.9%*	*1.1%*	*1.0%*
Sh. Equity	641.3	660.2	879.8	898.0	917.9
Minority interest	0.0	0.0	66.4	69.7	72.8
Provisions & deferred taxes	0.0	0.0	0.0	0.0	0.0
Net financial debt	400.9	393.8	810.6	863.2	986.2
Investment capacity (50% threshold)	199.4	218.0	(3.7)	(35.6)	(137.8)
Investment capacity (65% threshold)	753.2	786.8	810.1	796.8	714.2

Per share data	2005A	2006A	2007E	2008E	2009E
Number of shares (m)	9.79	9.79	12.09	12.09	12.09
EPS (recurring)	5.11	4.85	4.58	4.28	4.45
CFPS	6.40	4.87	4.60	4.29	4.47
NAVPS (before profit distribution)	65.5	67.4	72.8	74.3	75.9
DPS	4.80	4.92	4.45	4.50	4.55
Payout %	94%	101%	97%	105%	102%

Financial ratios	2005A	2006A	2007E	2008E	2009E
Total debt-to-total assets	41%	40%	50%	51%	53%
Net debt/Equity	63%	60%	92%	96%	107%
Net debt/EBITDA	6.1	6.3	9.3	9.1	9.7
Interest cover (EBIT/int. exp.)	4.3	4.4	4.2	4.0	3.6
ROE %	10.4%	10.4%	7.9%	8.3%	8.3%

Valuation ratios	2005A	2006A	2007E	2008E	2009E
Market cap	857	881	1,076	1,076	1,076
EV	1,258	1,275	1,887	1,939	2,062
EV/EBITDA	19.0	20.4	21.7	20.4	20.3
P/E	17.1	18.5	19.4	20.8	20.0
CF yield (recurring)	5.83%	5.41%	5.17%	4.83%	5.02%
P/NAV	133.6%	133.5%	122.3%	119.9%	117.3%
Dividend yield %	5.49%	5.47%	5.00%	5.06%	5.11%

COVERAGE BY PRIMARY ANALYST

Mickael Van den Hauwe: Real Estate
Companies covered: Aedifica, Atenor, Befi mmo, Cofinimmo, Kaufman & Broad, Leasinvest, Nexity, Retail Estates, WDP

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I, Mickael Van den Hauwe, hereby certify that the views expressed in this research report accurately refl ect my personal opinion about the companies and the securities discussed herein. 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 refl ect 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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Rating category	Buy	Add	Neutral	Reduce
Rating distribution	29.7%	27.0%	18.9%	24.3%
Investment banking relationship	25.0%	12.5%	37.5%	25.0%

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12-MONTH PRICE TARGET CHARTS

Source: Bloomberg

Date	Target price
02-Feb-07	92
12-Dec-06	82
31-May-06	76

HISTORY OF RECOMMENDATIONS

Befimmo's stock has been covered by Mickael Van den Hauwe as from May 31, 2007.

Date	Recommendation
02-Feb-07	Add
18-Sep-06	Reduce
31-May-06	Neutral

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