ING WHOLESALE BANKING

Company update

Real estate

Belgium

Maintained

# Befimmo

## Sharpening the focus

# Buy

| | |
|---|---|
| | 20/02/08 |
| **Reuters: BEFB.BR** | Price: €74.63 |

Previously: €84

12-mth target: €85.00

- The rationale behind the disposal of several office premises in the Brussels periphery is not indisputable in strategic terms, but is still consistent with the low risk profile of Befimmo and its inability to re-let empty assets in this difficult area. BUY.
- As assets sold are partially vacant, there is no negative impact on recurrent EPS. In addition, sizeable capital gains will be booked.

**Disposal of non-strategic assets.** Befimmo announced it will sell several assets deemed as non-strategic. Assets include two office buildings in the Brussels Periphery and all semi-industrial (logistic) sites. The rationale is an increased focus towards offices in city centres vs peripheric locations and unrelated property. The latter makes sense given the marginal weight of semi-industrial property in the portfolio (2% of FY07 group rents). The case for the former is more questionable as offices in the Brussels Peripherey do not look more 'exotic' than office premises in second-tier cities (Fedimmo assets). Befimmo's holdings in the beleaguered Brussels Periphery are affected by important vacancies. The timing might not be optimal, but the company reckons long-term prospects of the area are mixed, at best, possibly on the basis of the important potential supply vs more *intra muros* locations. The office buildings sold are partially (Woluwe Garden B) or completely (Woluwe Garden D) vacant. Befimmo retains several other offices sites in the Brussels Periphery (valued at c.€160-170m).

**Positive financial impact.** We have assumed that the disposal is completed on 1 July 2008. Given the lower resulting indebtedness and the higher property yields vs financial costs, one might expect this disposal to weigh on recurrent results, at least in the short run. However, given the important vacancies plaguing several assets sold, rents lost are actually more than compensated by lower financial expenses in 2008 (fiscal year closing on 30 September 2008); earnings estimates for FY09 and FY10 are only marginally down (12-months impact of lost rents). Our new 2008-10 net current EPS estimates stand at €3.84, €4.23 and €4.34, respectively, vs €3.75, €4.25 and €4.37. In addition, in 2008 Befimmo will book capital gains worth c.€0.40 per share.

**Reinvestment issues.** The indebtedness of the company as of end-September 2008 is expected to fall slightly below 45% (LTV), triggering the reinvestment issue. While we are slightly disappointed by the inability of Befimmo to fill its Brussels Periphery assets (Woluwe Garden D has been fully empty since January 2007), we believe it is still better to sell than keep empty assets.

**Investment case unchanged.** We raise our DCF-based target price slightly from €84 to €85/share. At these levels we believe the share remains very attractive given its fundamental upside potential and its ultra-low risk profile (moderate indebtedness, two-thirds of rents generated by public bodies, weight of the Brussels Periphery now below 10% of total portfolio value).

**12-month forecast returns (%)**

| | |
|---|---|
| Share price | 13.9 |
| Dividend | 6.0 |
| **12m f'cast total return** | **19.9** |

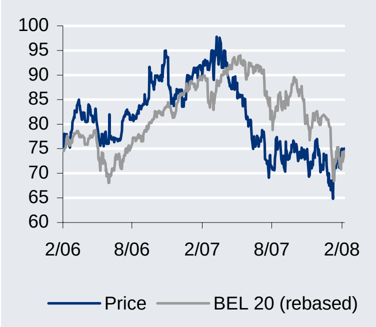
**Forecasts and ratios**

| Yr to Sep (€m) | 2007 | 2008F |
|---|---|---|
| Turnover | 104.9 | 108.9 |
| EBITDA | 88.3 | 90.3 |
| Net profit | 129.0 | 83.0 |
| Adj EPS (€) | 4.55 | 3.84 |
| Adj PER (x) | 16.4 | 19.4 |
| Dividend yield (%) | 6.0 | 6.0 |
| EV/EBITDA (x) | 20.5 | 19.9 |
| Price/NAV (x) | 1.0 | 1.0 |
| ROE (%) | 11.2 | 7.1 |

**Share data**

| | |
|---|---|
| No. of shares (m) | 13.1 |
| Daily turnover (shares) | 7,643.0 |
| Free float (%) | 83.8 |
| Enterprise value (€m) | 1,791.9 |
| Market cap (€m) | 974.6 |

**Share price performance**




Source: ING

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**21 February 2008**

**SEE THE DISCLOSURES APPENDIX FOR IMPORTANT DISCLOSURES AND ANALYST CERTIFICATION**

Fig 1 Properties sold

| | location | FY06/07 rents (€000) | Occupancy as of Sept. 2007 |
|---|---|---|---|
| Woluwe Garden B | Brussels Periphery | 1,288 | 91.4% |
| Woluwe Garden D | Brussels Periphery | 421 | 32.8% |
| Anderlecht I | Brussels Decentralized | 345 | 100.0% |
| Anderlecht II | Brussels Decentralized | 592 | 100.0% |
| Green Hill | Brussels Periphery | 155 | 89.4% |
| Kontich I | Antwerp | 623 | 98.8% |
| Kontich II | Antwerp | 382 | 93.7% |

Source: Company data

## Company profile

### Company profile

Listed in 1995, Befimmo was the first closed-end property investment company established under the SICAFI/V-BEVAK legislation (ex-ServiceFlats). Assets consisted mainly of properties formerly held by Bernheim-Comofi (now part of Fortis), which, as statutory manager, retains managing control of Befimmo despite the dilution of its stake.

In 2001, Befimmo merged with Cibix, resulting in further marginalisation of non-office assets and a higher weight of offices in central Brussels versus the Brussels periphery, not a bad thing as the latter continues to suffer in the current economic context. Since the acquisition of the Poelaert building (December 2003), a 14,000m2 office building fully leased to the Belgian state for 18 years, no new acquisitions have taken place, reflecting the lack of investment opportunities. However, Befimmo has not been idle; several important issues were addressed recently such as the disposal of non-strategic assets (Charleroi), the sale of the huge Borschette conference centre and an agreement on the allegedly asbestos-plagued WTC building (the state took over the Belgian Post's lease and extended it until end-2018). With a vacancy rate above 25%, the Shell building remains the main challenge in the short term.

### Strategy

As a registered SICAFI, Befimmo's sole activity is the active management of a property portfolio. Its assets consist mainly of office premises located in/around Brussels. A main feature of the portfolio is its low risk profile, epitomised by the high weight of government-like tenants (64% of rental income), the relatively low contribution of decentralised and periphery Brussels locations and the high rental duration (total duration of nine years). It also holds hi-tech and semi-industrial buildings in Brussels and other attractive areas (Brussels-Antwerp axis). Given the lack of suitable investment opportunities, the company recently hinted it might expand abroad, albeit only for a small portion of its portfolio.

### Risks

Market risk: Befimmo is mainly exposed to the Brussels office market, but this risk is mitigated by long-term leases and top tenants.

Interest rate risk: most of the financial debt is at floating rates, but a sizeable part is hedged.

## Financials

| Yr to Sep (€m) | 2007 | 2008F | 2009F | 2010F |
|---|---|---|---|---|
| **Income statement** | | | | |
| Turnover | 104.9 | 108.9 | 115.1 | 122.1 |
| EBITDA | 88.3 | 90.3 | 96.3 | 101.5 |
| Net financial charges | (35.7) | (36.0) | (36.9) | (40.5) |
| Operating exceptionals | 38.6 | 11.2 | 11.4 | 11.3 |
| Adj pre-tax profit | 52.4 | 54.1 | 59.3 | 60.8 |
| Corporate exceptionals | | | | |
| Profit/loss on sale of tangible fixed assets | 1.3 | 5.2 | 0.0 | 0.0 |
| Amortisation of goodwill | 0.0 | 0.0 | 0.0 | 0.0 |
| Pre-tax profit | 92.3 | 70.5 | 70.7 | 72.1 |
| Taxes | (0.6) | (0.7) | (0.7) | (0.7) |
| Extraordinary items (net) | 39.9 | 16.4 | 11.4 | 11.3 |
| Minorities | (2.6) | (3.3) | (3.3) | (3.4) |
| Preference dividend | 0.0 | 0.0 | 0.0 | 0.0 |
| Net profit | 129.0 | 83.0 | 78.0 | 79.3 |
| **Balance sheet** | | | | |
| Investment Properties | 1,815.1 | 1,796.0 | 1,960.8 | 1,987.4 |
| Working capital | 24.0 | 15.8 | 16.7 | 17.7 |
| L/T non-interest-bearing liabilities | 88.6 | 61.1 | 63.5 | 66.3 |
| Enterprise net assets | (48.5) | (29.1) | (30.7) | (32.5) |
| Group equity | 996.8 | 1,017.8 | 1,028.9 | 1,040.2 |
| Net debt | 806.0 | 785.3 | 937.4 | 950.9 |
| Capital employed | 1,802.8 | 1,803.1 | 1,966.3 | 1,991.1 |
| **Cash flow** | | | | |
| Operating cash flow | 97.4 | 106.2 | 97.9 | 103.3 |
| Cash taxes | (0.6) | (0.7) | (0.7) | (0.7) |
| Net financial charges (CF) | (35.7) | (36.0) | (36.9) | (40.5) |
| Gross cash flow | 61.1 | 69.5 | 60.3 | 62.1 |
| Capital expenditures (net of disposals) | (716.5) | 30.7 | (157.4) | (16.0) |
| Free cash flow | (655.5) | 100.2 | (97.1) | 46.1 |
| **Ratios (%)** | | | | |
| EBITDA margin | 84.1 | 82.8 | 83.7 | 83.1 |
| Operating margin | 84.0 | 82.7 | 83.6 | 83.0 |
| Net debt/equity | 80.9 | 77.2 | 91.1 | 91.4 |
| ROACE | 8.6 | 5.6 | 5.7 | 5.7 |
| ROE | 11.2 | 7.1 | 7.0 | 7.1 |
| **Growth (%)** | | | | |
| Turnover | 37.6 | 3.9 | 5.6 | 6.1 |
| EBITDA | 40.9 | 2.3 | 6.7 | 5.3 |
| Net profit | 35.0 | (25.3) | 0.1 | 2.0 |
| **Valuation** | | | | |
| EV/EBITDA (x) | 20.5 | 19.9 | 20.2 | 19.4 |
| Adj EPS (€) | 4.55 | 3.84 | 4.23 | 4.34 |
| Adj PER (x) | 16.4 | 19.4 | 17.6 | 17.2 |
| Price/NAV (x) | 1.0 | 1.0 | 1.0 | 1.0 |
| DPS (€) | 4.51 | 4.51 | 4.60 | 4.65 |
| Dividend yield (%) | 6.0 | 6.0 | 6.2 | 6.2 |

Source: Company data, ING estimates

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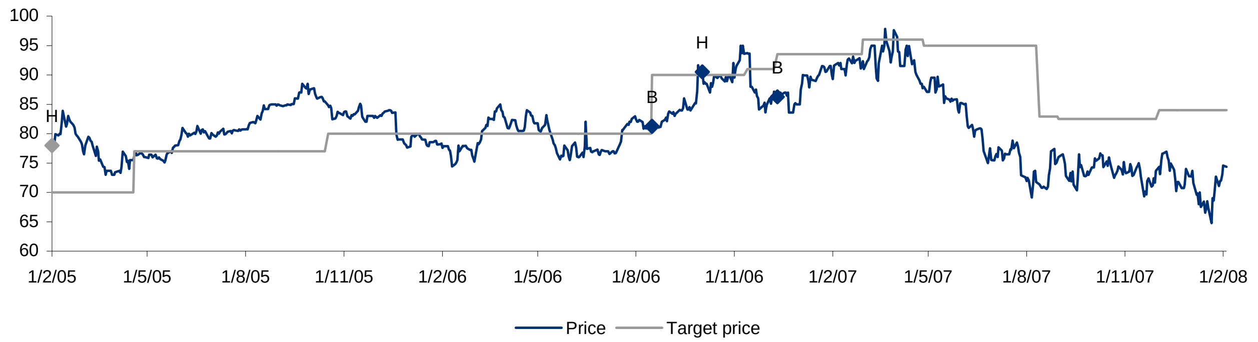


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Source: ING

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