

Befimmo

Buy

Reloading its guns

27/05/08

Previously: €85

Reuters: BEFB.BR

Price: €75.46

12-mth target: €86.00

- Alongside its 1HFY08 results, Befimmo detailed its renovations programme. Most assets due for completion in 2008-09 are now prelet. A second 'wave' of renovations will culminate in 2010-11; their impact on earnings is expected to be much smaller.
- Despite a good relative performance, we believe the share continues to offer good value combined with an ultra-low risk profile.

First-half results in line. Rents rose 12.6% YoY to €54.7m on the back of a higher occupancy rate (96.9% vs 95.1% as of end-September 2007, thanks to new leases and the sale of partially empty buildings). Operating expenses were roughly in line at €13.3m (+50.6%) given the expected enlarged management team but also as a result of several inconclusive due diligence processes. Net financial expenses were slightly better than expected at €17.9m (excluding IAS 39 non-cash adjustments), albeit including realised gains on real estate certificates (€0.9m). Net current profit came in at €26.5m (+4.1%). Absolute figures are not relevant given the enlarged consolidation scope (Fedimmo consolidated for the full six months vs only three months in 1HFY07). At €2.03, the net current EPS result excluding IAS 39 was down 21.9%, reflecting the dilutive effect of the 2007 capital increase (shares outstanding up 33%) and the refurbishment works in progress. Reported results were further helped by realised gains (disposal of non-strategic assets) and a positive revaluation of the portfolio; the appraised yield was 6.38%, flat vs end-September 2007.

More renovations... As a reminder, the FY08 results are likely to be hurt by current renovations (WTC II, Bréderode 2, Extension justice). These assets are all located in the Brussels CBD and are already prelet to first-class tenants on a long-term basis; remaining vacancies are small (Ikaros I, Central Gate). A new wave of renovations will start in September 2009 (Impératrice, Science, part of the Central Gate) as current tenants start leaving. Vacancy risk remains remote (we assume works lasting 18 months), while substantial rent increases are likely once works are completed given very low current rents; we have assumed rents close to €200/m² (implying lower rents for the over-rented Bréderode 2). Commercialisation usually starts well before completion, and long vacancy periods are unlikely given the excellent location.

... should have a positive effect on earnings... Future earnings will be affected by this new wave of renovations, but given the better spread and the positive effect on rents per m², we expect only a modest negative effect in FY10 before earnings rebound in FY11. We have fine-tuned our earnings estimates using new ING rates forecasts. Our DCF-based target price is up €1 at €86.

Attractive valuation. After their recent good relative performance, Befimmo's shares now trade at a premium to those of arch-rival Cofinimmo. However, Befimmo retains an ultra-low risk profile, attractive multiples and positive future newsflow. **BUY** maintained.

12-month forecast returns (%)	
Share price	14.0
Dividend	6.0
12m f'cst total return	19.9

Forecasts and ratios		
Yr to Sep (€m)	2007	2008F
Turnover	104.9	110.6
EBITDA	88.3	91.8
Net profit	129.0	83.5
Adj EPS (€)	4.55	3.87
Adj PER (x)	16.6	19.5
Dividend yield (%)	6.0	6.0
EV/EBITDA (x)	20.6	19.7
Price/NAV (x)	1.1	1.0
ROE (%)	11.2	7.1

Share data	
No. of shares (m)	13.1
Daily turnover (shares)	12,737
Free float (%)	83.8
Enterprise value (€m)	1,805.6
Market cap (€m)	985.4



Source: ING

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Fig 1 Befimmo: 1HFY08 results – main items (€m)

Year to 30 September	2006	1H07	2H07	2007	1H08	%ch YoY
Rents	76.3	48.6	56.3	104.9	54.7	12.6
Other operating income	(0.3)	2.1	(2.4)	(0.3)	5.4	153.5
Operating expenses	(13.5)	(8.8)	(7.7)	(16.5)	(13.3)	50.6
EBIT	62.5	41.9	46.2	88.1	46.8	11.7
Margin (%)	82.2	82.6	85.8	84.2		
Net interest*	(14.3)	(15.9)	(19.9)	(35.7)	(16.1)	1.4
Tax	(0.6)	(0.3)	(0.3)	(0.6)	(0.6)	121.4
Minorities	0.0	(1.0)	(1.6)	(2.6)	(1.8)	79.5
Net current profit*	47.5	24.7	24.5	49.2	28.3	14.4
Extraordinary items	0.0	0.0	0.0	0.0	0.0	N/M
Realised capital gains	0.5	1.2	0.1	1.3	7.5	516.6
Unrealised capital gains	18.0	27.2	11.4	38.6	7.1	-74.0
Portfolio results	18.5	28.4	11.5	39.9	14.5	-48.8
Net reported results	66.0	53.1	35.9	89.1	42.8	-19.4
Per share data (€)						
Adj. EPS	4.85	2.52	2.06	4.55	2.16	-14.2
Adj. EPS excl. IAS 39 adjustments	4.77	2.60	2.13	4.68	2.03	-21.9
Reported EPS	6.74	5.42	3.03	8.23	3.28	-39.6
NAVPS	67.41	68.11		73.66	72.86	7.0

* Including IAS 39

Source: Company data, ING estimates

Fig 2 Befimmo: Financial expenses – main assumptions (€m)

Year to 30 September	2007*	2008F	2009F	2010F
Average financial debt		802.4	867.1	953.2
Assumed 3M Euribor (%)		4.63	3.88	4.04
Margin (bp)	22	40	35	35
IRS 3.73% callable March 2009		200.0	100.0	
IRS 3.90% callable Jan. 2011		75.0	100.0	100.0
Twin caps 3.5-5.0%			300.0	400.0
Unhedged debt		527.4	367.1	453.2
Interest expenses		38.0	35.4	39.5
As a % of average debt		4.74	4.08	4.15

* Actual (fiscal year-end 30 September)

Source: Company data, ING estimates

Fig 3 Befimmo: Main renovations

	Total investments (€000)	Status	Tenant
WTC II	20,500.0	Let to current occupier	La Poste/Belgian state
Extension Justice	22,300.0	Let from 01/03/09	Belgian state
Bréderode Corner (Bréderode 2)	4,000.0	Let from 01/05/08	Sheraton
Central Gate	38,000.0	86.6% let – 20% additional vacancy from February 2009	
Ikaros I		50% let	EFI Vutek
Impératrice	28,300.0	Let until 31/08/09	Belgacom
Science	9,800.0	Let until 30/04/10	Belgian state
WTC III*	22,200.0	Fully let (long-term)	Belgian state
Mons II*	7,500.0	Fully let (long-term)	Belgian state
Fedimmo (excl. WTC III)*	13,900.0	Fully let (long-term)	Belgian state

* Not included in our earnings estimates (timing still undetermined)

Source: Company data, ING estimates

Fig 4 Befimmo: DCF valuation model (€m)

Year to 30 September	2008F	2009F	2010F
Operating cash flow	128.8	-48.9	73.4
Discount factor	0.95	0.90	0.84
Present value of free cash flow	122.8	-43.8	61.8
Cumulative present value of free cash flow	202.3		
+ Present value of terminal value	1,609.0		
+ Other financial assets (e)	34.1		
= Enterprise value	1,845.5		
- Net financial debt (group share)	-788.1		
= Theoretical market capitalisation	1,057.3		
Fair value per share (€)	81.0		
12-month target price (€)	86.2		

Source: ING estimates

Fig 5 Befimmo: Data per share – change of estimates (€)

Year to 30 September	2007*	2008F	2009F	2010F
Befimmo net current EPS guidance (est.)	4.55	3.74	4.47	4.70
ING old net current EPS ests.	4.55	3.89	4.31	4.43
ING new net current EPS ests.		3.87	4.53	4.35
ING old NAVPS before profit appropriation	73.66	72.77	73.45	74.14
ING new NAVPS before profit appropriation		72.76	73.65	74.23
Average shares outstanding (m)	10.8	13.1	13.1	13.1
Total shares outstanding (m)	13.1	13.1	13.1	13.1

* Actual

Source: Company data, ING estimates

Fig 6 Befimmo/Cofinimmo comparison

	Befimmo	Cofinimmo
Price as of 27 May 2008 (€)	75.46	120.23
Gross yield (%)	5.98	6.57
Gross yield (adjusted) (%)	6.12	6.59
Last yearly NAV (€)	73.66	123.22
Next yearly NAV (€)	72.76	127.85
as of	Dec 2008	May 2009
Premium/discount (%)	3.72	-5.96
Premium/discount (adjusted) (%)	1.26	-6.18
Target price (€)	86.0	136.0
12-month upside/downside (%)	19.9	19.7
Current recommendation	BUY	BUY

Source: ING estimates

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 a further marginalisation of non-office assets and a higher weighting of offices in central Brussels versus the Brussels periphery, not a bad thing as the latter continues to suffer in the current economic environment. No new acquisitions were completed between the purchase in December 2003 of the Poelaert building, a 14,000m² office building fully leased to the Belgian state for 18 years, and the end of 2006, reflecting the lack of investment opportunities. The real breakthrough came with the acquisition at end-2006 of the Fedimmo portfolio. Fedimmo consisted of office properties leased on a long-term basis to the Belgian state and spread across Belgium; after years of apparent inactivity, this acquisition dramatically increased Befimmo's size. The subsequent capital increase (summer 2007) brought its market cap above the €1bn threshold. Following the recent pre-lease of the Bréderode 2 building and the disposal of several underperforming assets, no significant vacancies remain.

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 and around Brussels. A main feature of the portfolio is its low risk profile, epitomised by the high weight of government-like tenants (66% of rental income), the relatively low contribution of non-central and peripheral Brussels locations, further reduced by recent disposals of underperforming assets in the Brussels Periphery, and the high rental duration (total duration of nine years). Befimmo's focus on offices was strengthened by the Fedimmo acquisition and the recent disposal of its semi-industrial (warehousing) assets.

Given the lack of suitable investment opportunities, the company recently hinted that it might expand abroad, albeit only for a small portion of its portfolio. The only acquisition abroad so far has been the Axento portfolio (Luxembourg).

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	110.6	116.8	120.8
EBITDA	88.3	91.8	97.9	99.8
Net financial charges	(35.7)	(37.1)	(34.5)	(38.6)
Operating exceptionals	38.6	11.3	11.4	10.9
Adj pre-tax profit	52.4	54.5	63.3	61.0
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	71.0	74.6	71.9
Taxes	(0.6)	(0.7)	(0.7)	(0.7)
Extraordinary items (net)	39.9	16.5	11.4	10.9
Minorities	(2.6)	(3.3)	(3.4)	(3.5)
Preference dividend	0.0	0.0	0.0	0.0
Net profit	129.0	83.5	81.9	78.7
Balance sheet				
Investment Properties	1,815.1	1,799.7	1,963.8	2,000.6
Working capital	24.0	16.0	16.9	17.5
L/T non-interest-bearing liabilities	88.6	61.7	64.2	65.8
Enterprise net assets	(48.5)	(29.5)	(31.1)	(32.2)
Group equity	996.8	1,018.3	1,033.3	1,044.4
Net debt	806.0	788.1	935.6	960.2
Capital employed	1,802.8	1,806.4	1,968.9	2,004.7
Cash flow				
Operating cash flow	97.4	108.1	99.5	100.8
Cash taxes	(0.6)	(0.7)	(0.7)	(0.7)
Net financial charges (CF)	(35.7)	(37.1)	(34.5)	(38.6)
Gross cash flow	61.1	70.3	64.3	61.5
Capital expenditures (net of disposals)	(716.5)	27.0	(156.8)	(26.8)
Free cash flow	(655.5)	97.3	(92.5)	34.7
Ratios (%)				
EBITDA margin	84.1	83.0	83.8	82.6
Operating margin	84.0	82.9	83.7	82.4
Net debt/equity	80.9	77.4	90.5	91.9
ROACE	8.6	5.7	5.7	5.5
ROE	11.2	7.1	7.4	7.0
Growth (%)				
Turnover	37.6	5.4	5.6	3.4
EBITDA	40.9	4.0	6.7	1.9
Net profit	35.0	-24.8	5.2	-4.0
Valuation				
EV/EBITDA (x)	20.6	19.7	20.0	19.9
Adj EPS (€)	4.55	3.87	4.53	4.35
Adj PER (x)	16.6	19.5	16.7	17.3
Price/NAV	1.1	1.0	1.0	1.0
Dividend (€)	4.51	4.51	4.60	4.65
Dividend yield (gross)	6.0	6.0	6.1	6.2

Source: Company data, ING estimates

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PRICE & RATINGS HISTORY TO 05/05/08: BEFIMMO (BEFB.BR)



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