19.11.09

Befimmo (EUR 65 - Hold): Will Frankfurt be this helpful in 2010?

Comment of update:
The net cash flow guidance is lower now than in the original prospectus not the dividend guidance as we mentioned before.

Yesterday after the close Befimmo announced its FY results. The net current result per share was better than expected. Nonetheless, the company lowered its occupancy guidance for the coming 3 years as the office markets are under stress.

Facts

Total rental income increased to EUR 119.1m vs. EUR 109.5m which was mainly thanks to the completed renovation projects of the WTC 2 tower and the Justice Extension which are both let to the Belgian government. This was slightly higher than we expected (EUR 118.5m). The occupancy rate of the portfolio decreased to 93.7% (vs. 94% at 30/06/09 and 97.3% last year), which was inline with our estimate (93.5%). The operating margin increased to 89% compared to 83.5% last year (we expected 86.5%). This was mainly thanks to lower technical and over-head costs. The latter because of lower charges related to research for investment projects. As a result of the company's hedging strategy, which is based on both swaps and caps, the average interest rate decreased to 3.58% vs. 4.78% last year and 4.09% at 30/06/09 (we expected 3.85%). Therefore financing costs decreased to EUR 30m vs. EUR 40m last year. Overall net cash flow increased from EUR 59.8m to EUR 72.4m which was mainly thanks to the lower financing costs. We expected EUR 69.7m. Per share the net cash flow amounted to EUR 5.15 compared to EUR 4.55 last year, we expected EUR 4.95.

As a result of the good results the company will pay out a final dividend of EUR 1.04 per share on top of the interim dividend of EUR 3.36, which was inline with the company's guidance in the prospectus of the capital increase.

As the office market remains difficult and take-up decreased significantly in both Brussels and Luxembourg the company has revised its outlook for next 3 years. As 485.000sqm additional space will come on the market in Brussels next year, of which 75% at risk and not pre-let, the company expects the market vacancy rate could decrease to 13% vs. 11% at the moment and 9% at the beginning of the year. As a result the company expects its occupancy rate for 09/10 to further decrease to 92.6% and 91.5% the year after vs. the their old estimate 94.7% and 94.8%.

Total revaluation amounted to -3.74% or EUR -75m, which was more or less inline with our estimate (-3.5%). Surprisingly, negative revaluation amounted to -0.86% vs. -0.24% during Q2 and -0.43% in Q3. This was mainly due to significant revaluation in the periphery on Brussels which has also seen market rental levels drop and market vacancy increase during the last quarter. As a result the NAV decreased to EUR 58.87, we expected EUR 59.5.

With regard to the capital increase the company said it has not seen any interesting investment opportunities on the Brussels market and we should not expect an investment in the short term. As the company mentioned before it will most probably not invest in Paris and remained focussed on the Brussels market.

Our View

Thanks to their hedging strategy the company was able to report a better than expected net cash flow and thus has no problems to pay the final dividend. Nonetheless, as the Brussels office market is under significant stress and will see supply increase even further next year the company has lowered its occupancy rate expectations. We believe that even though the company has a very opportunistic view on the Euribor for the coming 12 months (0.78%) when forecasting its financing costs for next year, they should be able to pay EUR 3.90 dividend next year, given no large defaults arise. This is mainly because the guided pay-out ratio for next year (88.6%), excluding a EUR 8m expected capital gain next year, is more than enough to protect them in case of a quickly increasing Euribor. Furthermore, for the coming year the company only has to renew 1% of its leases, excluding completed pipeline projects. Furthermore, one should take into account that Befimmo's guidance tends to be rather conservative as the outperformance of the guidance is becoming a recurring item.

Again the company said the Paris market looks attractive but they will most probably stay focuses on its Brussels home market. However, the company said it has not seen any interesting investments opportunities on the Brussels market. Therefore, as there already have been some deals in Befimmo-like assets we do not expect an investment in the short term as the company does not seem to be willing to pay what other funds are paying. Furthermore, during the conference call last night the management again said that the main goal of the capital increase was to reinforce the balance sheet as the debt ratio had increased to +50%.

Conclusion

All in all, this year's results were better than expected thanks to the current low Euribor. Even though we believe the company's expectations for Euribor for the coming 12 months seems opportunistic (0.78%) we believe a sudden increase will not lead to the company not being able to pay EUR 3.90 dividend next year as the pay-out ratio provides a large enough safety net. Furthermore, lease renewals are limited. Therefore even though the Brussels office market is set for a bumpy ride in the coming year we reiterate our Hold recommendation as the company specific outlook looks stable but provides little upside. Target price EUR 62.50

Analyst: Pieter van der Meijden, Phone: +32 2 229 63 40, E-mail: .vandermeijden@petercam.
Sales contact: Pieter van der Meijden, Phone: +32 (2) 229 63 40, E-mail: .vandermeijden@petercam.