

Befimmo (from HOLD to REDUCE - EUR 55.75) Q3 in line with estimates, outlook remains negative

Befimmo reported its Q3 figures yesterday after closing. Overall figures were in line with our expectations. Given the recent price evolution and the negative outlook we change our rating from Hold to Reduce. TP remains EUR 51.70

Facts

- Top line arrived at EUR 92.3m (EUR 92.4m one year ago), while we expected EUR 91.4m. Occupancy rate improved to 94.44% from 93.86% one quarter ago.
- New leases and renewals were signed for 52,600sqm, of which 81% concerns offices. The company did not disclose information on trends of lease reversions. Main renewal is in regard to the Brederode building for 13,400sqm, which will be let to Linklaters for 15 years after the renovation of the building expected in 2013. This historical building, located in Brussels CBD, will be renovated for EUR 25.5m or approx. EUR 1900/sqm. However, the 2 other buildings let to Linklaters (Brederode 9 + Namur 48), sublet for the moment, will be vacated in 2013 (7,000sqm to come to the market).
- FFO/share decreased to EUR 3.31 from EUR 3.96 over the year. We expected EUR 3.39/share (diff A vs. E is -2.27%). Main reason for the higher decrease on FFO level should be a higher cost of debt vs. last year.
- The LfL portfolio value decreased by -1.14% in the first half of 2011 and an additional -0.48% in Q3 (vs. our estimate of -1% for the 3 quarters). The difference is partly explained by the fact that the Brussels CBD LfL value changes by -0.75% in Q3, while during the first 6 months of the year it decreased by only -0.27%. That decline is mainly explained by the Brederode building of Linklaters (lower rent + EUR 25m renovation costs despite the 15-year maturity).
- NAV stands at EUR 60.40, while we banked on EUR 60.1.
- Management quoted that potential investments on the Brussels' market are still there but that it is still waiting for some nicer deals. Obviously the company wishes to divest in the peripheral regions of Brussels, which encounter an vacancy ratio of approx. 20%.
- Regarding the letting market, management quoted that it remains challenging and rather slow. No letting news on the Froissart building, except that the building gained interest from potential tenants aiming to locate themselves close to the EU institutions. No news for the Science Montoyer building.
- Befimmo reiterated guidance on the dividend which offers a 7% dividend yield when looking to yesterday's closing price.

Our view

The weakness of the Brussels office market has its effect on the activity of Befimmo. The company is looking for nicer deals than currently available on the market. The trigger for nicer deals could be: (i) will the (public) letting market pick up shortly and improve rental levels or (ii) will prices further decline? In our opinion, prices will probably decline when the letting market keeps on suffering and a higher risk premium is asked by investors.

Luckily, the probability of rising interest rates has decreased and as this is in favor of Befimmo this might save the case, temporarily. Hence we expect interest rates to pick up on the long run. Secondly the speculative developments came to an end (only 50,000sqm next year).

Conclusion

Q3 Results came in as we expected. We were happy to see quite some lease renewals, however we remain cautious as reversion is still negative. The Brederode building gives an indication of the path forward of Befimmo: negative rental reversions despite heavy renovations and, as a result, lower valuations. Our EVA-model shows a value of EUR 56.55/share, however it looks less attractive when looking to other ratios and the relative upside of the rest of our coverage. We change our rating from Hold to Reduce.

Details

in EUR	2010 Q3a	2011 Q3a	% Ch	2011 Q3e	% Ch
Rental income (m)	92.4	92.3	-0.11%	91.4	1.01%
FFO	65.5	55.59	-15%	56.9	-2.27%
FFO/Share	3.9	3.31	-15%	3.39	-2.27%
NAV/share	59.95	60.4	1%	60.1	0.50%

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