

8 May 2012

BEFIMMO

Cloudy weather ahead

REAL ESTATE INVESTMENT TRUSTS
BELGIUM

CURRENT PRICE €45.96
TARGET PRICE €50.00

HOLD
RATING DOWNGRADED

Performance over	1M	3M	12M
Absolute	-5%	-14%	-26%
Rel. BEL20	-2%	-10%	-9%
12m Hi/Lo	€64.40/45.40		
Bloomberg	BEFB.BB		
Reuters	BEFB.BR		
Market Cap	€772m		
Next corporate event			
Results 1Q12: 14 May 2012			
www.befimmo.be			

FY/e 31.12	2011*	2012E	2013E	2014E
Current Result (€m)	90.0	67.8	66.9	70.7
Portfolio Result (€m)	-6.6	-23.7	-16.1	0.0
Net Profit (€m)	81.9	44.2	50.8	70.7
Diluted adj. EPS (€)	5.35	3.87	3.77	3.94
NAV per share	57.4	56.7	56.5	56.4
P/E	10.85	11.88	12.19	11.66
EV / EBITDA	15.01	16.86	17.42	16.61
DPS	4.93	3.50	3.50	3.63
Dividend Yield	8.5%	7.6%	7.6%	7.9%

Source: KBC Securities * 15 quarters

The 1Q12 update of the Brussels' office market confirms the current malaise. Low take-up figures prevent both rental prices from rising and the availability ratio from dropping. Although Befimmo is known for its defensive business profile, the company seems to be struggling to resist the current pressure. Management expects only a slight increase in rental income over the coming three years. We see no immediate changes or growth opportunities for the company and assume fresh capex in order to keep the portfolio attractive. These challenges have prompted us to lower our estimates. We lower our TP to €50 and revise our rating from Accumulate to Hold.

MARKET PRESSURE SLOWS INCOME STREAM

- Affecting impeccability.** We appreciate Befimmo's solid profile as a pure player with long-term indexed lease contracts (>9y), a stable and high-quality tenant base and a strong balance sheet. However, the current challenging conditions on the office market seem to be slowing the rental income stream. The company has 14.8% exposure to the low-performing decentralized zone and periphery, where 3/6/9 contracts reduce income visibility. In the annual report management guides for weak results in the coming three years and for a dividend cut to €3.45. Despite the low number of expected developments in the coming years, this situation seems to be structural and we expect it to continue weighing on the results in the next two years.
- 1Q12 results preview.** We do not expect any material elements in the 1Q12 interim statement: net rental income of €32m vs. €30m in 2Q10-11 on the back of the Froissart and Pavilion building, an operating result before result on portfolio of €26.9m vs. €25.1m in 2Q10-11. Bottom line we expect an EPRA result of €17.5m vs. €18.6m in 2Q10-11.
- Valuation & share rating.** We adapted our model to reflect current market conditions and the guidance. Following these changes, we attain a theoretical fair value of €50.5 using an Economic Value Added model and an explicit 5-year forecasting period. We set our Target Price at €50, which corresponds to a P/NAV of 0.88x and a dividend yield of 7%, and downgrade our rating from Accumulate to Hold.

ANALYSTS

Koen Overlaet-Michiels

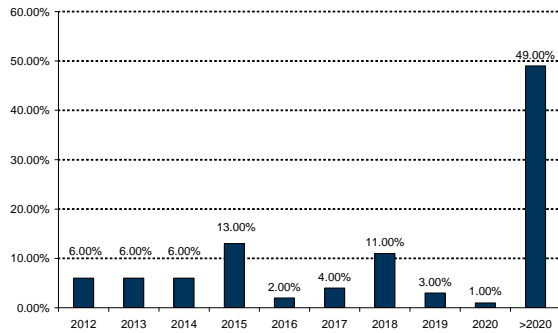
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EXPIRY DATE LEASE CONTRACTS (FIRST BREAK)



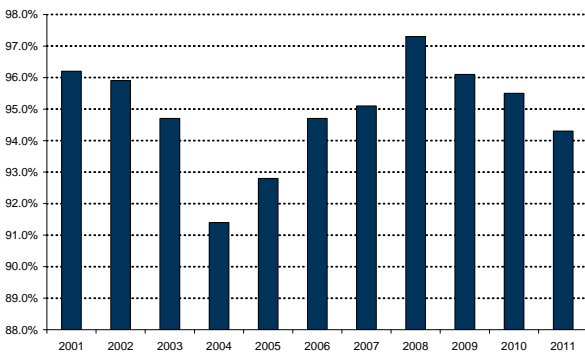
Source: Befimmo

GEOGRAPHIC IMPORTANCE

	Proportion of rents (%)	Weighted avg duration (y)
Brussels Centre	56.40%	10.2
Brussels Decentralized	6.20%	3.9
Brussels Periphery	8.60%	2.7
Wallonia	8.90%	6
Flanders	16.50%	13
Luxembourg	3.40%	3.5

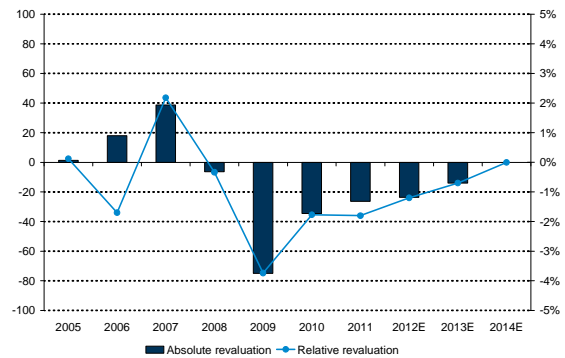
Source: Befimmo

PORTFOLIO OCCUPANCY RATE



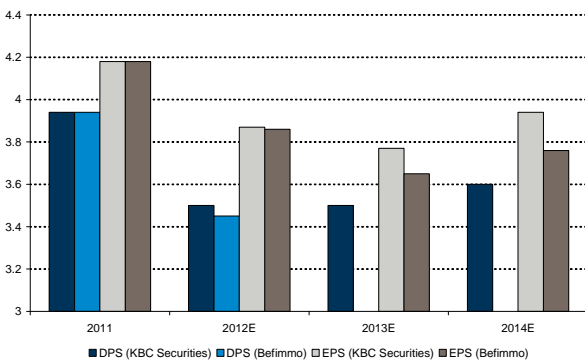
Source: Befimmo

PORTFOLIO REVALUATION



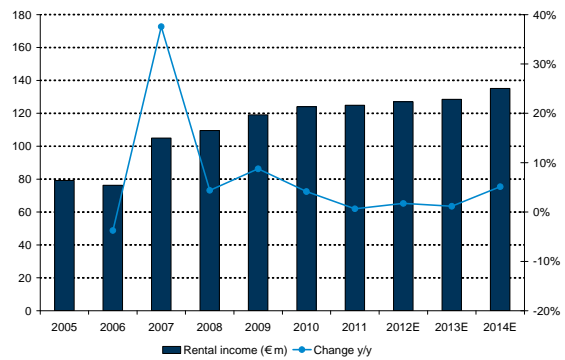
Source: Befimmo, KBC Securities

DPS – EPS EVOLUTION



Source: Befimmo, KBC Securities

RENTAL INCOME EVOLUTION



Source: Befimmo, KBC Securities

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PRO FORMA FY11 RESULTS

On February 16, Befimmo reported its annual results, which were above management’s own estimates, but broadly in-line with consensus figures. In order to have a better comparison base, we only focus on the pro forma figures. Net rental result increased from €123.7m to €124.6m, while the operating margin decreased for the second year in a row to 84%. The financial result (excl. IAS 39 impact) rose from €-22.5m to €-28.8m due to the increase in short-term interest rates, the higher debt and the higher fixed interest rate payable on the new financing. As such, these higher financial charges are to a large extent expected to persist. EPRA earnings came in at only €70m vs. €85m in FY10. This lower bottom line was mainly caused by the increased financial charges and the absence of a one-off payment of €6.5m for a contract termination in FY10.

Next to this slight decrease in EPRA EPS (from €5.09 to €5.03 on a pro forma basis), the company’s net asset value also dropped sharply as a consequence of the negative portfolio revaluations, from €61.7 to €57.4 per share. These were however good results given the current challenging market. Management confirmed the final dividend of €0.99 per share.

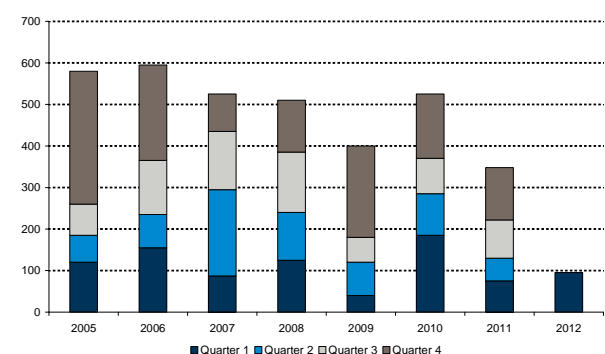
OUTLOOK

However, Befimmo’s outlook was less promising. Management only expects limited growth in rental income in the coming years due to the malaise in the office market and a further increase in net financial charges. Management estimates weak EPRA earnings of €67.7m in 2012, €64.8m in 2013 and €67.5m in 2014. Therefore, the company guides for a dividend cut from €3.94 on an annual basis to €3.45 in FY12.

Office market movements

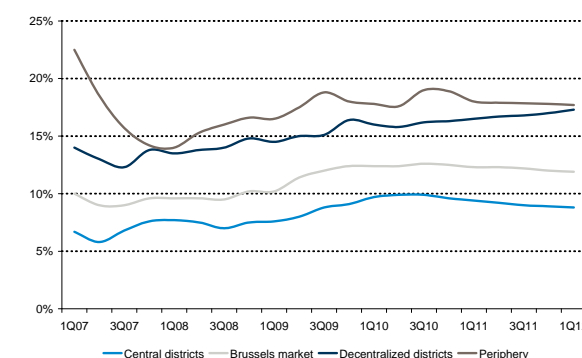
Recent research suggests that Befimmo’s predictions might prove accurate. The Brussels office market is still under pressure in 2012, after a 2011 that was the worst year of the decade in terms of take-up. The availability ratio in Brussels dropped slightly however in 1Q12 vs. 1Q11. This trend is mainly detected in recent buildings and supported by the low number of new development projects. In the prime segment we detect a slight increase in prime rents and an increase of effective rents. Older buildings and non-prime locations seem to suffer more in this challenging environment, with vacancy levels in the decentralized zone and periphery at respectively 17.3% and 17.7%.

BRUSSELS – OFFICE TAKE-UP ('000 M²)



Source: DTZ Research

AVAILABILITY RATE



Source: DTZ Research

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Befimmo's profile

We appreciate Befimmo's sharp focus as a pure player in the office market. This means that management has a clear strategic focus and that the shareholder has more freedom to diversify. With a weighted average portfolio maturity of 9 years, the company is largely resistant to the current challenges in the office market. Moreover, the majority of its portfolio is leased to the Belgian state, which creates a secure income stream. In our view the largest challenges are in the decentralized zone and the periphery, where Befimmo's portfolio maturity averages 3 to 4 years. This requires Befimmo to renew rental contracts more frequently, with a resulting negative impact on rents. The impact on Befimmo's current result is therefore not insignificant either. Another issue in the current market is the predominant interest in recently-built offices. As a consequence, Befimmo is increasingly obliged to carry out constant renovation of its buildings in order to keep them attractive.

These challenges together with the limited growth opportunities have made us adjust our estimates downwards. We forecast no growth in the upcoming two years. The increase in rental income will only come from a positive indexation of the rents and the contribution of the current projects. Given the current challenging office market, we believe a slight indexation of the existing rents will be Befimmo's main target. We estimate a net current result (EPRA) of €67.8m in 2012, €66.9m in 2013 and €70.7m in 2014.

P&L ANALYSIS

€ m	2009	2010	2011*	2012E	2013E	2014E	2015E
Gross rental income	119.1	124.0	156.0	127.0	128.5	135.1	137.4
Property operating expenses	(3.1)	0.7	(9.3)	(6.4)	(7.8)	(8.9)	(9.1)
Property operating result	116.0	124.7	146.7	120.6	120.6	126.2	128.3
Administrative expenses	(9.8)	(12.5)	(17.7)	(15.0)	(15.3)	(15.6)	(15.9)
EBITDA	106.1	112.2	129.0	105.6	105.4	110.6	112.4
Net financing expenses	(30.0)	(20.7)	(34.5)	(32.4)	(33.1)	(34.2)	(35.0)
Corporate income tax	(0.5)	(0.7)	(0.8)	(0.8)	(0.8)	(0.8)	(0.8)
Minorities	(3.3)	(3.9)	(5.2)	(4.6)	(4.6)	(5.0)	(5.2)
Net current result - group	72.4	86.9	90.0	67.8	66.9	70.7	71.4
Profit (loss) on disposals	0.2	0.2	14.8	-	-	-	-
Portfolio revaluations	(75.0)	(34.6)	(26.4)	(23.7)	(16.1)	-	14.8
Revaluation of financial instruments	(34.3)	(5.9)	5.0	-	-	-	-
Minorities	2.2	0.1	-	-	-	-	-
Portfolio result - group	(106.9)	(40.1)	(6.6)	(23.7)	(16.1)	-	14.8
Net profit - group	(34.5)	46.7	81.9	44.2	52.8	70.7	86.1
Number of shares	16.8	16.8	17.5	17.5	17.7	17.9	17.9
EPS - direct	4.31	5.17	5.35	3.87	3.77	3.94	3.98
DPS	4.4	3.9	4.9	3.5	3.5	3.6	3.8
Pay out ratio	102%	75%	92%	91%	93%	92%	95%

Source: KBC Securities

* 15 quarters

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PREVIEW 1Q12 RESULTS

We do not expect Befimmo to publish new material elements in its 1Q12 update. Therefore, our 1Q12 estimates reflect the expected trend for the full year. We use the period from 1 January to 31 March 2011 (or 2Q10-11) to compare our 1Q12 estimates. We estimate a net rental income of €32m vs. €30m last year, supported by the contributions of the Froissart and Pavilion building. Corporate overhead costs will be slightly higher leading to an operating result before result on portfolio (EBITDA) of €26.9m vs. €25.1m. Befimmo did not report any investments or divestments in 1Q12, so capital gains are expected to be zero. The financial charges are assumed to be significantly higher, thereby lowering the net current result (group share) to €17.5m vs. €18.6 in 2Q10-11.

The net result is expected to drop to €11.5m, impacted by the estimated portfolio revaluation of €-5.9m. The changes in fair value of the financial instruments (IAS 39) are expected to be negative as long-term interest rates decreased in 1Q12 vs. 5Q10-11. This corresponds to an expected EPRA result per share of €1.00 vs. €1.09 in 2Q10-11 and a net result per share of €0.66 vs. €2.20 in 2Q10-11.

1Q12 PREVIEW

€ th	1Q10-11	2Q10-11	2011*	1Q12E
Net rental income	31,200	29,799	155,752	32,136
Property operating result	n.a.	59,013**	146,764	30,473
Corporate management costs	n.a.	-7,530**	-17,695	-3,742
Operating result before result on portfolio	26,360	25,123	128,997	26,919
Gains or losses on disposals of invest. properties	n.a.	14,746**	14,769	0
Changes in FV of investment parties	-7,400	-5,670	-26,403	-5,914
Net interest charges	n.a.	-11,763**	-30,948	-8,094
NET RESULT - GROUP SHARE	11,585	45,094	81,855	11,555
EPRA RESULT (RECURRING GROUP SHARE)	19,477	18,559	90,022	17,468

Source: KBC Securities

** Cumulative Q1+Q2 of FY10-11 * 15 quarters

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VALUATION

We prefer to value Befimmo using an Economic Value Added model as this captures both direct and indirect returns. We use an explicit 5-year forecasting period and expect no value creation or destruction afterwards. The new NOPLAT figures result from the net result changes mentioned above. The portfolio result mainly comes from Befimmo's portfolio revaluation. Using Befimmo's predictions, we lowered our negative portfolio revaluation in 2012, 2013 and 2014 to respectively -1.2%, -0.8% and 0%. We use a WACC based on the following parameters:

- A cost of equity of 7.75% based on a risk free rate of 4% and a market risk premium of 5%.
- A long-term credit spread of 200 bps.
- A long-term debt/equity ratio of 50/50.

We set our target price at €50, which corresponds to a P/NAV of 0.88x and a dividend yield of 7%. Simultaneously, we revise our Accumulate rating to Hold, as the office market is in a structural malaise and growth opportunities are limited. We expect this situation to continue weighing on the results in the coming two years.

EVA VALUATION

€ m	2011	2012E	2013E	2014E	2015E	2016E
NOPLAT	128.1	104.9	104.7	109.9	111.7	113.7
Portfolio result	(6.6)	(23.7)	(16.1)	-	14.8	21.3
Total return	121.5	81.3	88.6	109.9	126.5	135.0
Shareholders' equity	1,003	1,006	1,024	1,068	1,127	1,156
Minorities	68	68	68	68	68	68
Provisions & deferred taxes	2.4	2.4	2.4	2.4	2.4	1.4
Net debt	874	907	953	946	913	911
Other long-term liabilities	10	10	10	10	10	10
Minus: financial assets	(10)	(10)	(10)	(10)	(10)	(10)
Capital invested	1,947	1,983	2,047	2,084	2,110	2,136
ROIC		4.1%	4.4%	5.3%	6.0%	6.4%
WACC		6.8%	6.8%	6.8%	6.8%	6.8%
Value creation spread		-2.7%	-2.4%	-1.5%	-0.8%	-0.5%
EVA		(53.7)	(50.1)	(31.7)	(17.2)	(10.3)
Discount period		-	1.00	2.00	3.00	4.00
Discounting factor		1.00	0.94	0.88	0.82	0.77
Number of shares (m)		17.5	17.7	17.9	17.9	17.9
NPV of EVA per share		(3.1)	(2.5)	(1.6)	(0.8)	(0.4)
NAV adj.	56.8					
Minus 50% deferred taxes	-					
NPV of EVA	(8.4)					
1/2 y forward base rate	2.2					
Fair value per share	50.5					
Upside (downside)	9.9%					

Source: KBC Securities

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FINANCIAL DATA

Income statement (€m)	2009	2010	2011	2012E	2013E	2014E
Gross Rental Income (GRI)	119.1	124.0	156.0	127.0	128.5	135.1
Other Income	-	-	-	-	-	-
Property & Development Costs	-3.1	0.7	-9.3	-6.4	-7.8	-8.9
Other Costs	-9.8	-12.5	-17.7	-15.0	-15.3	-15.6
EBITDA	106.1	112.2	129.0	105.6	105.4	110.6
Depreciation & Amortization	0.0	0.0	0.0	0.0	0.0	0.0
EBIT	106.1	112.2	129.0	105.6	105.4	110.6
Financial Result	-30.0	-20.7	-34.5	-32.4	-33.1	-34.2
Taxes	-0.5	-0.7	-0.8	-0.8	-0.8	-0.8
Associates	0.0	0.0	0.0	0.0	0.0	0.0
Discontinued / Other	0.0	0.0	0.0	0.0	0.0	0.0
Minorities	-3.3	-3.9	-5.2	-4.6	-4.6	-5.0
Net current result (Group's share)	72.4	86.9	90.0	67.8	66.9	70.7
Changes in FV of investment properties	-75.0	-34.6	-26.4	-23.7	-16.1	0.0
Gains/losses on real estate divestments	0.2	0.2	14.8	0.0	0.0	0.0
Minorities	2.2	0.1	0.0	0.0	0.0	0.0
Portfolio Result	-106.9	-40.1	-6.6	-23.7	-16.1	0.0
Net Profit (Group's share)	-34.5	46.7	81.9	44.2	50.8	70.7
Adjusted Net Profit (Group's share)	73.1	86.9	90.0	67.8	66.9	70.7
Cash flow statement (€m)	2009	2010	2011	2012E	2013E	2014E
Cash Flow from Operations	82.8	93.8	93.9	72.5	71.5	75.7
Change in Working Capital	4.8	-6.1	75.2	-0.4	-0.4	-0.5
Cash Flow from Operating Activities	87.6	87.7	169.1	72.0	71.1	75.2
Cash Flow from Investments	-29.4	-26.0	-115.5	-58.7	-79.6	-37.2
Free Cash Flow	58.2	61.7	53.6	13.3	-8.5	38.0
Dividend Payments	-60.6	-62.7	-91.9	-45.6	-37.7	-31.4
Share issues	159.5	0.0	0.0	0.0	0.0	0.0
New borrowings / reimbursements	-155.5	-1.7	86.5	30.0	45.0	10.0
Other cash flow from financing	-	-	-	-	-	-
Cash Flow from Financing	-56.7	-64.3	-5.5	-15.6	7.3	-21.4
Fx and changes in consolidation scope	-	-	-	-	-	-
Change in Cash & Equivalents	1.5	-2.6	48.1	-2.2	-1.2	16.6
Balance sheet (€m)	2009	2010	2011	2012E	2013E	2014E
Investment Properties	1,918.3	1,885.0	1,971.3	2,006.3	2,069.9	2,107.1
Development Projects	-	-	-	-	-	-
Other Fixed Assets	21.4	20.8	27.0	27.0	27.0	27.0
Total Fixed Assets	1,939.7	1,905.7	1,998.3	2,033.3	2,096.9	2,134.1
Assets held for Sale	4.6	37.6	0.0	0.0	0.0	0.0
Receivables	23.5	19.5	15.7	16.3	16.9	17.6
Other current assets	15.5	18.7	18.5	18.3	18.1	17.9
Cash and Cash Equivalents	6.1	3.5	4.2	2.0	0.8	17.4
Total Current Assets	49.7	79.4	29.6	27.8	27.1	44.2
TOTAL ASSETS	1,989.4	1,985.1	2,027.8	2,061.1	2,123.9	2,178.2
Shareholders' Equity	988.4	1,017.4	1,002.6	1,005.9	1,023.7	1,068.0
Minority Interest	61.6	64.4	67.8	67.8	67.8	67.8
Total Equity	1,050.0	1,081.9	1,070.5	1,073.7	1,091.5	1,135.8
LT Financial Debt	745.4	584.8	855.8	885.8	930.8	940.8
Other LT Liabilities	18.9	20.1	10.4	10.4	10.4	10.4
Total LT Liabilities	764.3	604.9	866.2	896.2	941.2	951.2
ST Financial Debt	1.9	206.0	21.4	21.4	21.4	21.4
Other Current Liabilities	173.3	92.3	69.7	69.7	69.7	69.7
Total ST Liabilities	175.1	298.3	91.1	91.1	91.1	91.1
TOTAL LIABILITIES	1,989.4	1,985.1	2,027.8	2,061.1	2,123.9	2,178.2
Per share data (€)	2009	2010	2011	2012E	2013E	2014E
Basic EPS (€)	-3.97	2.66	4.98	2.52	2.87	3.94
Adjusted EPS (€)	2.40	5.05	5.35	3.87	3.77	3.94
Diluted EPS (€)	-3.97	2.66	4.98	2.52	2.87	3.94
Diluted Adjusted EPS (€)	2.40	5.05	5.35	3.87	3.77	3.94
Net Current Result Per Share (€)	2.40	5.05	5.35	3.87	3.77	3.94
Portfolio Result Per Share (€)	-6.36	-2.39	-0.38	-1.35	-0.90	0.00
DPS (€)	4.40	3.90	4.93	3.50	3.50	3.63
NAV Per Share (€)	59.85	61.68	57.37	56.72	56.49	56.41

Source: KBC Securities

*Historic valuation data are based on historic prices

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DISCLOSURE & DISCLAIMER SECTION

The company disclosures can also be consulted on our website <http://www.kbcsecurities.be/disclosures>.

KBC Securities uses an absolute rating system including terms such as Buy, Accumulate, Hold, Reduce and Sell (see definitions below).

	Definition
BUY	Expected total return (including dividends) of 10% or more over a 6-month period
ACCUMULATE	Expected total return (including dividends) between 0% and 15% over a 6-month period
HOLD	Expected total return (including dividends) between -5% and 5% over a 6-month period
REDUCE	Expected total return (including dividends) between -15% and 0% over a 6-month period
SELL	Expected total return (including dividends) of -10% or worse over a 6-month period

Due to external factors and in exceptional cases, KBC Securities allows the use of ratings such as Accept the Offer, Black Out, No Recommendation or Suspended.

Our analysts assign one of those ratings based on their investment outlook and valuation for the concerned stock. The valuation can be based on different methodologies such as DCF (discounted cash flow), absolute multiples, peer group multiples, sum-of-parts or NAV (Net Asset Value). The valuation is reflected in a 6-month target price. Occasionally, the expected total return may fall outside of these ranges because of price movement and/or volatility. Such deviations will be permitted but will be closely monitored. Investors should carefully read the definitions of all ratings used in each research report. In addition, since the report contains more complete information concerning the analyst's view, investors should carefully read the entire report and not infer its contents from the rating alone. KBC Securities discloses the recommendations of its reports to the issuers before their dissemination. In case the recommendation has been amended following this disclosure, such amendments will be indicated in the concerned report.

Stock rating	% of covered universe	% of covered universe with investment banking relationship during last year
BUY	26.80%	20.00%
ACCUMULATE	39.80%	40.00%
HOLD	31.70%	40.00%
REDUCE	0.80%	0.00%
SELL	0.80%	0.00%

Befimmo is an office REIT focussing on prime assets let on long-term to public entities.

The price target for Befimmo is based on following parameters: Absolute Multiples, Peer Group Multiples, Estimated Equity Value (NAV), Dividend Discount Model (DDM)

The risks which may impede the achievement of our price target are: Access to capital (debt & equity), evolution of interest rates and credit spreads, real estate investment market, impact real economy on portfolio vacancy and rental values

Below is an overview of the stock ratings and target price history in the last 12 months for the stock described in this report.

Date	Rating	Target price
08-MAY-12	Hold	€ 50.00
17-FEB-12	Accumulate	€ 54.00
13-JAN-12	Accumulate	€ 56.50

KBC Securities will provide periodic updates on companies/industries based on company-specific developments or announcements, market conditions or any other publicly available information.

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