DEFAMA

Retail - Property / Germany

Baader Europe

DEFAMA continues on its way up

Earnings/sales releases - 24/11/2023

Against a generally deteriorating market backdrop, DEFAMA continues to make progress, notably through a major and profitable acquisition. We remain positive.

Fact

- Acquisition of a property complex generating €1.2m in additional rental income. Price not disclosed.
- Thanks to acquisitions and indexation, rental income approached €6m in Q3 23 vs. €5.2m in Q3 22. The contribution of indexation and organic growth were not disclosed.
- FFO continued to rise in Q3 23 on a sequential basis to €2.5m vs. €2.3m in Q2 23, reflecting the increase in EBITDA over the period. It rose by 15% over 9M 23 (+16% yoy in H1 23).
- The LTV ratio remains at 58%.
- DEFAMA has achieved its annual targets, in particular an annualised FFO in excess of €11m. It is continuing to explore profitable acquisition opportunities to develop its portfolio towards the 2025 target of €350m of assets under management (€285m today).

Analysis

Acquisition in Baden-Württemberg and sectoral considerations

The 10,000 sqm Reutter-Center is DEFAMA's largest-ever acquisition. It generates €1.2m in rental income. The target was converted in 2001 and modernised in 2016, and does not require any major work. It is mainly let to REWE, AWG Mode and Schuh Mann. The price is above €10m but probably reflects an EV/net rents multiple at the lower end of the historical range (i.e. a rental yield of above 10%), of we believe in the difference of €12m between the GAV at September 2023 (€273m) and the GAV to date (€285m at 24 November, both figures from the 9M 23 company's presentation).

Compared with DEFAMA's historical assets, the price of €1,200/sqm seems high (usually more like €700-800) but this is offset by a monthly rent/sqm that is also much higher: €10 vs. usually more like less than €7 on the portfolio as a whole. This of course also reflects the high quality of the asset, which will generate a net yield in excess of 10% (our estimate) for a cost of debt that we estimate at less than 5%.

The main tenants are already known to DEFAMA, which already leases space to them at other sites. The average remaining lease term (WALT) has not been disclosed but is likely to be favourable.

In our opinion, this good-quality acquisition reflects a change in market practice, with a decline in the creditworthiness of potential buyers as a result of rising interest rates. There are beginning to be bargains to be had in this buyer's market. DEFAMA's balance sheet is solid enough to enable it to seize a couple of opportunities of this type in the coming quarters, as long as the market prices do not contaminate balance sheet valuations, via the GAV appraised by external valuers. The slowdown in inflation is expected to result in a pause in rent increases (indexation) by 2025 at the latest. The rent impact, which will have been positive in

Add	**Upside: 30.6%**
Target Price (6 months)	€ 27.3
Share Price	€ 20.9
Market Cap. €M	100
Price Momentum	**UNFAVORABLE**
Extremes 12Months	20.3 ▶ 24.8
Sustainability score	2.7 /10
Credit Risk	B
Fundamental Strength	3 /10
Bloomberg	DEF GY Equity
Reuters	DEF.MU

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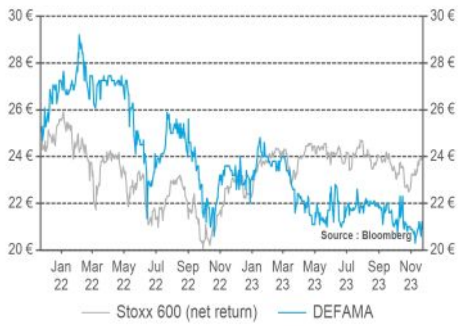


Analyst : Christian AUZANNEAU

Equity Sales EquitySales@baaderbank.de
Frankfurt +49 69 1388 1355
London +44 20 7054 7100
Munich +49 89 5150 1850
Zurich +41 43 388 9200
New York +1 212 935 5150

PERF	1w	1m	3m	12m
DEFAMA	-1.42%	0.00%	-5.43%	-10.7%
Real Estate	1.37%	13.7%	10.3%	5.09%
STOXX 600	1.60%	5.37%	1.11%	4.48%

Sector Opinion	**Underweight**
Strongest upside	DEMIRE
Worst potential	Hammerson

Complete Sector Analysis

Last updated: 17/05/2023	12/22A	12/23E	12/24E	12/25E
Adjusted P/E (x)	21.6	23.9	21.0	19.1
Dividend yield (%)	2.14	2.68	2.78	2.87
EV/EBITDA(R) (x)	21.4	17.8	16.7	15.8
Adjusted EPS (€)	1.17	0.87	0.99	1.10
Growth in EPS (%)	2.73	-25.3	13.7	10.4
Dividend (€)	0.54	0.56	0.58	0.60
Sales (€M)	20.2	24.7	27.4	29.9
EBITDA/R margin (%)	62.8	60.1	61.3	61.5
Attributable net profit (€M)	5.40	4.20	4.77	5.27
ROE (after tax) (%)	15.5	9.96	10.8	11.4
Gearing (%)	331	366	382	389

Company Valuation - Company Financials

2022-23, will then cease to offset the risk of a further rise in interest rates (yield impact), or simply of interest rates not falling rapidly, or the consequences of a stronger-than-expected recession.

The ECB has continued to alert the market and banks to the risks hanging over commercial property in Europe. We feel that the cycle has not yet bottomed out and that there are undoubtedly still significant adjustments to be made. In this context, DEFAMA's financing method (long mortgages at fixed interest rates) can be considered resilient. FFO will rise from €10.5m (annualised) at 30 June 2023 to €11.1m today. With this transaction, DEFAMA has improved its consolidated risk profile.

In the sector, we are awaiting publication of the results of the bond issue by FCR Immobilien (listed, not covered), which sought to place an 09/2028 bond yielding 7.25%. This transaction reflects the rising cost of liquidity for small players, but DEFAMA is not exposed to the bond market. As regards the banks, which are the company's usual lenders, the first write-downs are beginning to appear (see PBB), although they are not yet cause for concern. However, we do not rule out a sharp acceleration in risk over the next few quarters.

With classical mortgages, DEFAMA is not at immediate risk in the event of more pronounced restrictions on bank lending (reduced liquidity, repricing of mortgages, etc.). From our point of view, the best deals are still ahead of us. We will continue to monitor the speed of saturation of DEFAMA's balance sheet, which remains satisfactory for the time being.

Back to 9M 23

The building occupancy rates were little changed over the quarter, in line with Q1 and Q2 23, at around 94%. The announced acquisition should bring the consolidated vacancy rate down to around 5%, suggesting a high occupancy rate for this asset, coupled with improved occupancy in most recent delivered extensions. For the time being, the economic crisis has not yet led to a significant rise in vacancy rates in our portfolio of companies under coverage, but we will be keeping a close eye on the consequences of the slowdown that is set to spread over the coming months.

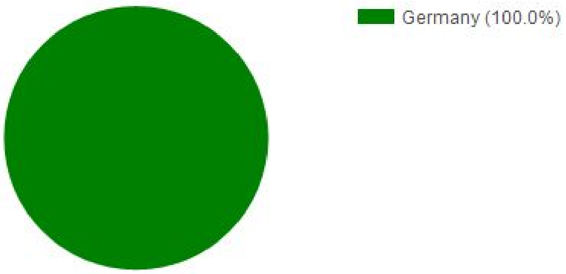
The company's performance therefore continued to improve sequentially in Q3 23, whether in terms of rents, EBITDA or FFO. The absence of any GAV revisions this quarter meant that the LTV ratio remained at 58% (before financing the acquisition of the Reutter-Center). The rise in operating indicators (rental revenue, EBITDA) did not translate into strong leverage on Earnings Before Taxes in Q3 23 due, in our view, to a gradual rise in financial costs (average cost of debt from 2.32% in September 2022, 2.45% in June 2023 and 2.58% in September 2023). Given DEFAMA's debt profile, this impact should be very gradual and smoothed out over time. It will also be offset by the contribution of highly profitable acquisitions. The FY 23 and, to a certain extent, FY 24 operational reports can therefore be considered as safe.

Impact

Given the structure of its debt, DEFAMA is one of the few players able to withstand a sharp fall in market values, as it will not have to refinance any bond tranches at potentially high interest rates over the next few years. In our view, it can therefore get through the crisis with LTV ratios at above 75%, which will not be the case for everyone. We therefore see DEFAMA as a resilient player, like some of the rare low LTV ratio players (using bonds financing) on the market.

Our positive recommendation on DEFAMA is confirmed, even though we do not expect the share price to soar over the next few quarters. Its story continues to be built brick by brick, in a sector where negative news flow could accelerate further over the next few months. It is at the end of the cycle that the market will best recognise the quality of DEFAMA's strategy. More than some other peers, DEFAMA has time to react to any major crisis that may lie ahead. Time is precious.

Sales by Geography



Valuation Summary

Benchmarks	Value	Weight
NAV/SOTP per share	€ 29.6	55%
Dividend Yield	€ 20.9	20%
DCF	€ 27.5	10%
PE based	n/a	10%
P/book based	n/a	5%
TARGET PRICE	€ 27.3	100%

NAV/SOTP Calculation

Largest comparables

Consolidated P&L Accounts

		12/22A	12/23E	12/24E
Sales	€M	20.2	24.7	27.4
Change in sales	%	18.1	21.9	11.2
Change in staff costs	%	5.59	10.0	6.00
EBITDA	€M	12.7	14.8	16.8
EBITDA(R) margin	**%**	**62.8**	**60.1**	**61.3**
Depreciation	€M	-5.10	-6.08	-6.72
Underlying operating profit	€M	7.60	8.74	10.1
Operating profit (EBIT)	**€M**	**7.60**	**8.74**	**10.1**
Net financial expense	€M	-2.90	-3.74	-4.40
of which related to pensions	€M	0.00	0.00	0.00
Exceptional items & other	€M	2.48	0.00	0.00
Corporate tax	€M	-1.78	-0.80	-0.91
Equity associates	€M			
Minority interests	€M			
Adjusted attributable net profit	**€M**	**5.40**	**4.20**	**4.77**
NOPAT	€M	5.70	6.55	7.56

Cashflow Statement

EBITDA	€M	12.7	14.8	16.8
Change in WCR	€M	-1.18	0.00	0.00
Actual div. received from equity holdi...	€M	0.00	0.00	0.00
Paid taxes	€M	-1.78	-0.80	-0.91
Exceptional items	€M	2.09	4.00	0.00
Other operating cash flows	€M			
Total operating cash flows	€M	11.8	18.0	15.9
Capital expenditure	€M	-45.2	-25.0	-25.0
Total investment flows	€M	-45.2	-25.0	-25.0
Net interest expense	€M	-2.90	-3.74	-4.40
Dividends (parent company)	€M	-2.45	-2.59	-2.69
Dividends to minorities interests	€M	0.00	0.00	0.00
New shareholders' equity	€M	10.3	0.00	0.00
Total financial flows	€M	34.8	6.99	9.11
Change in cash position	€M	1.50	0.00	0.00
Free cash flow (pre div.)	**€M**	**-36.2**	**-10.7**	**-13.5**

Per Share Data

No. of shares net of treas. stock (year...	Mio	4.80	4.80	4.80
Number of diluted shares (average)	Mio	4.61	4.80	4.80
Benchmark EPS	**€**	**1.17**	**0.87**	**0.99**
Restated NAV per share	€	20.2	21.9	23.2
Net dividend per share	**€**	**0.54**	**0.56**	**0.58**

Balance Sheet

		12/22A	12/23E	12/24E
Goodwill	€M			
Total intangible	€M	0.00	0.00	0.00
Tangible fixed assets	€M	186	200	219
Financial fixed assets	€M			
WCR	€M	6.17	6.17	6.17
Other assets	€M			
Total assets (net of short term liab.)	€M	192	207	225
Ordinary shareholders' equity	**€M**	**41.3**	**42.9**	**45.0**
Quasi Equity & Preferred	€M			
Minority interests	€M	0.00	0.00	0.00
Provisions for pensions	€M	0.00	0.00	0.00
Other provisions for risks and liabilities	€M			
Total provisions for risks and liabilities	€M	0.00	0.00	0.00
Tax liabilities	€M			
Other liabilities	€M			
Net debt (cash)	**€M**	**150**	**164**	**180**
Total liab. and shareholders' equity	€M	192	207	225

Capital Employed

Capital employed after depreciation	€M	192	207	225

Profits & Risks Ratios

ROE (after tax)	**%**	**15.5**	**9.96**	**10.8**
ROCE	%	2.97	3.17	3.36
Gearing (at book value)	**%**	**331**	**366**	**382**
Adj. Net debt/EBITDA(R)	x	11.8	11.1	10.7
Interest cover (x)	x	2.62	2.34	2.29

Valuation Ratios

Reference P/E (benchmark)	**x**	**21.6**	**23.9**	**21.0**
Free cash flow yield	%	-29.9	-10.7	-13.5
P/Book	x	2.93	2.34	2.23
Dividend yield	**%**	**2.14**	**2.68**	**2.78**

EV Calculation

Market cap	€M	121	100	100
+ Provisions	€M	0.00	0.00	0.00
+ Unrecognised acturial losses/(gains)	€M	0.00	0.00	0.00
+ Net debt at year end	€M	150	164	180
+ Leases debt equivalent	€M	0.00	0.00	0.00
- Financial fixed assets (fair value)	€M			
+ Minority interests (fair value)	€M	0.00	0.00	0.00
= EV	€M	271	264	280
EV/EBITDA(R)	**x**	**21.4**	**17.8**	**16.7**
EV/Sales	x	13.4	10.7	10.2

Analyst : Christian Auzanneau, Changes to Forecasts : 17/05/2023.

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