

GRAND CITY Properties S.A.

Luxembourg / Real Estate
 Frankfurt
 Bloomberg: GYC GR
 ISIN: LU0775917882

Q2 2019
 Results

RATING
BUY

PRICE TARGET
€ 28.00

Return Potential 36.9%
 Risk Rating Medium

OPERATIONS CONTINUE TO HUM IN Q2

Second quarter reporting featured a solid operational performance with all headline figures showing mid single digit growth. Net rent climbed 3.4% Y/Y, thanks to the reversionary potential of the portfolio, which resulted in 3.8% like-for-like (LFL) total net rent growth. GCP acquired some €300m in new properties in H1 offsetting disposals of €187m in non-core and mature assets as part of cash recycling. Management confirmed full year guidance (FFOPS 1: €1.26 - €1.27). Good portfolio diversification also helps insulate GCP against the regulatory headwinds in Berlin. We look for the good operational trajectory to continue to deliver solid results in the coming quarters as the company optimises its German properties and its growing London portfolio. Our rating remains Buy with a €28 price target.

Berlin rent freeze priced into stock Management addressed the rent freeze and expropriation topics at length on today's conference call. Although the picture remains unclear with a looming feud between state and federal regulators over the legality of Berlin setting rent legislation, management assured investors that good portfolio diversification—Berlin accounts for 9% of total units and <13% of rental income—means that overall LFL performance has < 1% exposure to a Berlin rent freeze outcome. Our sensitivity analysis confirms this assumption. The rent freeze draft will be finalised at the end of August with the Senate set to vote in October. Since Bundestag lawyers have already declared the rent freeze unconstitutional, we expect the federal government to challenge a successful vote. We have written a number of times this year that Berlin should focus on clearing up regulatory bottlenecks that gate new construction to increase supply rather than implement artificial measures that only temporarily help existing renters. In our view, the matter is far from being settled. But we think the rent-freeze-risk is priced into the stock so investors can return their attention back to operations until the regulatory dust up has been settled. (p.t.o.)

FINANCIAL HISTORY & PROJECTIONS

	2015	2016	2017	2018	2019E	2020E
Rental income (€m)	333.50	435.67	494.89	544.98	596.96	633.62
Y/Y growth	53.8%	30.6%	13.6%	10.1%	9.5%	6.1%
Adj. EBITDA (€m)	177.27	224.73	247.98	275.53	298.18	315.86
Net income ² (€m)	343.9	542.5	534.6	488.6	396.1	415.6
EPS (diluted) (€)	2.35	3.25	3.06	2.76	2.23	2.32
EPRA NAV ¹ (€m)	2402.09	3208.45	3993.06	4783.07	5151.76	5513.73
DPS (€)	0.25	0.68	0.73	0.77	0.82	0.88
FFO 1 (€m)	128.04	160.12	178.01	197.85	211.86	226.02
FFOPS 1 (€)	1.01	1.05	1.12	1.19	1.27	1.35
Liquid assets (€m)	388.93	630.27	401.48	765.04	1,095.80	993.01

RISKS

Risks include, but are not limited to, unfavourable interest rate developments, unfavourable macroeconomic developments, and departure of key personnel.

COMPANY PROFILE

Grand City Properties is a specialist real estate company focused on investing in and managing value-add opportunities in the German real estate market. The overarching strategy is to improve the portfolio through targeted modernisation and intensive tenant management and thus create value by subsequently raising occupancy and rental levels.

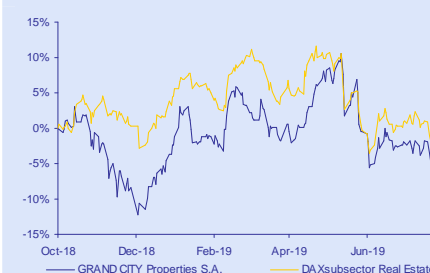
MARKET DATA

As of 19 Aug 2019

Closing Price	€ 20.46
Shares outstanding	166.72m
Market Capitalisation	€ 3411.09m
52-week Range	€ 18.62 / 24.16
Avg. Volume (12 Months)	233,194

Multiples	2018	2019E	2020E
P/FFO 1	17.1	16.1	15.1
P/EPRA NAV	0.7	0.7	0.6
FFO 1 Yield	5.9%	6.2%	6.6%
Div. Yield	3.8%	4.0%	4.3%

STOCK OVERVIEW



COMPANY DATA

As of 30 Jun 2019

Liquid Assets	€ 769.00m
Current Assets	€ 1,401.12m
Intangible Assets	€ 4,879.30m
Total Assets	€ 9,277.66m
Current Liabilities	€ 469.00m
Shareholders' Equity	€ 4,722.05m

SHAREHOLDERS

Edolaxia Ltd.	38.9%
Free Float	61.1%



ANOTHER GOOD QUARTER

Both the top line and earnings showed solid performances led by a 7% Y/Y rise in adjusted EBITDA and FFO 1. This was spurred by a continued strong like-for-like (LFL) performance. As of H1, GCP realised total LFL net rental growth of 3.8% comprising 0.3% occupancy increases and 3.5% in-place rent. The latter contains 1.0% indexation, 2.2% re-letting and 0.3% modernisation increases.

Table 1: Q2 results vs forecasts

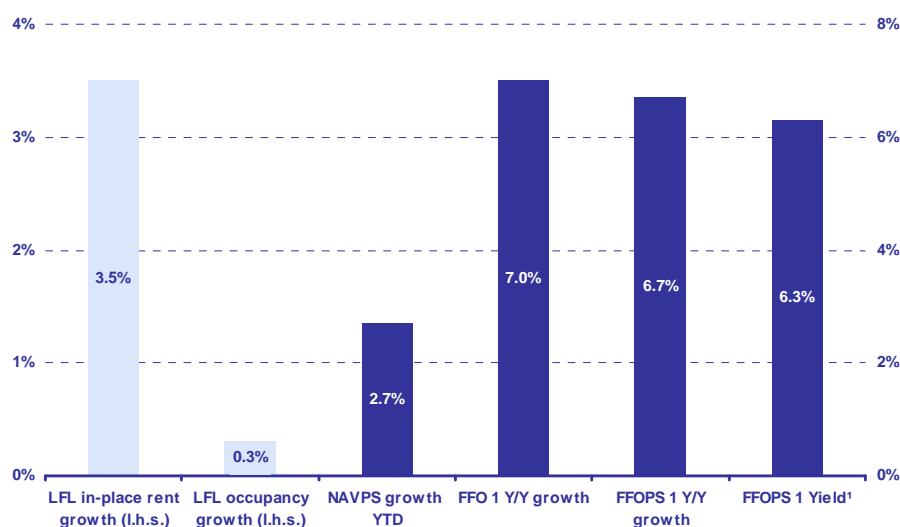
in €m	Q2/19	Q2/19E	Variance	Q2/18	Variance	H1/19	H1/18	Variance
Rental income	139	138	0.8%	136	2.4%	278	269	3.6%
Net rent	95	94	1.2%	92	3.4%	189	182	4.0%
Adjusted EBITDA	74	73	1.0%	69	6.8%	146	137	7.0%
margin	53%	53%	-	51%	-	53%	51%	-
FFO 1	53	53	1.5%	50	6.8%	106	99	7.1%
FFOPS 1 (€)	0.32	0.32	1.5%	0.30	6.7%	0.64	0.60	6.7%

Source: First Berlin Equity Research estimates

FFO 1 was close to our estimate and climbed 7% Y/Y to €53m in Q2/19 equating to FFOPS 1 of €0.32 (+7%). The capital gains, property revaluations and other income line item totalled €91m for the quarter (Q2/18: €132m) but lagged behind the strong pace set last year and in Q1 (€120m) This was due to more conservative market developments Y/Y and a lower volume of properties assessed in Q2 vs Q1. Roughly half of the portfolio was evaluated in H1. Adjusted EBITDA, which reflects recurring operational profit excluding capital gains and revaluation effects, rose 7% Y/Y to €74m. On a half-year basis, adjusted EBITDA and FFO 1 climbed 7% Y/Y. The company is thus tracking well towards guidance (table 4 overleaf).

FFO 2 amounted to €191m in H1 (H1/18: €187m). GCP disposed of €187m in non-core and mature assets during the first six months as part of its cash recycling strategy. Properties sold in Berlin, Halle, and Merseburg generated some €85m in disposals gains over total costs including CapEx.

Figure 1: Operating performance as of 30 June



¹ based on share price of EUR20.4

Source: First Berlin Equity Research, Grand City Properties



As of 30 June, EPRA NAV totalled €3.9bn (€23.1 / share) compared to €3.8bn at year end 2018 (€22.5 / share, +2.7%). NAV growth owes predominantly to the strong net profit of €250m recorded for the six month period. Including the perpetual notes, which are classified as equity under IFRS, this KPI stood at €4.9bn or €295 / share (+1.7%).

Table 2: Portfolio overview as of 30 June 2019

	Investment properties (€m)	Rentable area ('000 m ²)	EPRA vacancy	Annualised net rent (€m)	In-place rent (€/m ²)	Number of units	Value (€/m ²)	Rental yield
NRW	2,010	1,842	8.0%	118	5.7	27,592	1,091	5.8%
Berlin	1,477	539	5.9%	47	7.6	7,188	2,739	3.2%
Dresden / Leipzig / Halle	990	947	9.2%	53	5.2	16,350	1,046	5.3%
Mannheim / KL / Frankfurt / Mainz	414	267	4.7%	22	7.1	4,441	1,547	5.4%
Nuremberg / Fürth / Munich	223	102	3.6%	10	8.1	1,471	2,180	4.5%
Hamburg / Bremen	368	297	5.0%	20	6.0	4,272	1,236	5.5%
London	501	61	9.7%	20	30.8	1,213	8,226	4.0%
Others	1,006	1,086	7.1%	66	5.7	18,513	928	6.6%
Development rights & new build*	604	-	-	-	-	-	-	-
Total	7,593	5,141	7.3%	356	6.25	81,040	1,359	5.1%

* land for development, building rights on existing buildings (€278m) and premarketed new buildings in London (€326m)

Source: First Berlin Equity Research; Grand City Properties

Portfolio gross asset value (GAV) totalled €7.6bn at the end of Q2 vs €7.5bn end of Q1 and €7.2bn YE18. The company has been active in buying well located assets in London, which now accounts for 11% of GAV. Management noted an overall €400m acquisition pipeline that contains a ~€100m London component on the conference call. GAV / m² edged higher to €1,359 vs €1,314 in Q1 with all cities and regions except London improving. The latter dipped mainly on currency exchange effects while the actual value remained stable.

Table 3: Financial highlights

in €m	H1/19	2018	Variance
Cash & liquid assets	769	760	1%
Investment property ¹	7,593	7,244	5%
Total equity	4,722	4,667	1%
EPRA NAV incl. hybrid notes	4,879	4,783	2%
EPRA NAV	3,857	3,753	3%
Interest bearing debt	649	871	-25%
Straight bonds	2,473	2,177	14%
Convertible bond	273	272	0%
Loan-to-Value (LTV)	34%	34%	-
Equity ratio	51%	53%	-

¹ including inventories-trading property

Source: First Berlin Equity Research, Grand City Properties

Financial mix includes higher corporate debt component Grand City has issued some €700m in corporate debt YTD and retired around €200m in bank debt. The swap helped compress cost for debt (CoD) to €1.4% (YE18: 1.6%) and lengthen the debt maturity to 8.4 years (YE18: 8.2). Corporate debt now constitutes 31% of the overall financing mix vs 27% YE18, while bank debt was dialled back to 8% (2018: 11%).

The company reported cash and liquid assets of €769m for the period ended 30 June compared to €760m at the end of Q4/18, while net debt stood at €2.6bn vs €2.6bn at YE18. The debt structure continues to feature an LTV of 34%, which remains well below the 45% internal limit set by the Management Board. Coverage ratios were solid with a debt service coverage ratio (DSCR) and an interest coverage ratio (ICR) of 5.3x and 6.4x respectively at the end of Q2.

**Table 4: Full year guidance confirmed and in line with forecasts**

	Unit	H1 annualised	2019 Guidance	2019E
FFO 1	€m	212	211 - 213	212
FFOPS 1	€	1.28	1.26 - 1.27	1.27
DPS	€	0.83	0.82 - 0.83	0.82
LFL net rent growth	%	3.8	> 3.5	3.5
LTV	%	34	< 45	34

Source: First Berlin Equity Research, Grand City Properties

Sticking to Buy rating and €28 price target Second quarter performance matched our expectations. Operational performance continues to deliver upper single digit annualised growth as management corrals embedded portfolio reversionary upside (+28%). We look for operations to continue their current positive trajectory as the company balances external growth with disposal of mature and non-core assets. We believe the Berlin rent-freeze-risk is now priced into the stock, which is still trading ~13% off its yearly highs.

VALUATION MODEL

in €m	2019E	2020E	2021E	2022E	TV
EBITDA	298	316	333	350	354
(+) Revaluations	342	322	312	260	50
(+) Investment income	2	2	2	2	2
(-) Tax expense	96	96	97	92	61
NOPAT	546	543	550	520	345
Total assets	9,513	9,962	10,233	10,975	10,975
(-) Current liabilities	307	327	339	355	355
(+) Current financial debt	22	22	22	22	22
(-) Cash	615	513	253	480	480
(+) Deferred taxes	541	588	635	681	681
Capital employed (CE)	9,153	9,732	10,298	10,842	10,842
Average CE	8,806	9,443	10,015	10,570	10,842
ROCE	6.2%	5.8%	5.5%	4.9%	3.2%
WACC	3.1%	3.1%	3.1%	3.1%	3.1%
ROCE-WACC	3.1%	2.7%	2.4%	1.8%	0.1%
Economic Profit	274	252	241	194	10
NPV	274	242	224	175	449
Fair value calculation					
Total return	1,364				
(+) EPRA NAV (2018)	3,753				
(-) Dividend to be paid	129				
Equity value	4,988				
Diluted SO ('000)	179				
Fair value per share (€)	28.00				



INCOME STATEMENT

All figures in EURm	2015	2016	2017	2018	2019E	2020E
Net rent	220	285	328	364	388	412
Rental and operating income	333	436	495	545	597	634
Revenue from sale of buildings	0	7	2	0	0	0
Revenue	333	443	497	545	597	634
Capital gains, property revaluations & other	311	598	616	507	342	322
Result from equity-accounted investees	0	1	6	1	2	2
Property expenses	-152	-204	-239	-263	-288	-305
Cost of buildings sold	0	-5	-1	0	0	0
Administration expenses	-7	-10	-11	-11	-13	-14
Operating income (EBIT)	486	823	868	780	639	637
Finance expenses	-26	-36	-40	-46	-52	-54
Other financial results	0	-11	-43	-36	-21	0
Pre-tax income (EBT)	460	775	786	698	567	584
Tax and deferred tax expenses	-66	-122	-146	-115	-90	-86
Minority interests	-35	-88	-80	-64	-48	-50
Hybrid note investors	-15	-23	-24	-30	-33	-33
Net income	344	542	535	489	396	416
Basic EPS (€)	2.71	3.56	3.35	2.95	2.37	2.48
Diluted EPS (€)	2.35	3.25	3.06	2.76	2.23	2.32
Adjusted EBITDA	177	225	248	276	298	316
Ratios						
Adjusted EBITDA margin	53.2%	51.6%	50.1%	50.6%	50.0%	49.9%
Tax rate	12.8%	11.9%	-11.3%	-10.8%	10.8%	10.8%
Expenses as % of revenues						
Property expenses	45.4%	46.8%	48.3%	48.2%	48.2%	48.2%
Administration expenses	2.1%	2.2%	2.2%	1.9%	2.3%	2.3%
Y-Y Growth						
Rental and operating income	53.8%	30.6%	13.6%	10.1%	9.5%	6.1%
Total revenues	44.1%	32.7%	12.2%	9.7%	9.5%	6.1%
Operating income	41.9%	69.3%	5.5%	-10.2%	-18.0%	-0.4%
Adjusted EBITDA	58.3%	26.8%	10.3%	11.1%	8.2%	5.9%
Net income/ loss	67.3%	57.7%	-1.5%	-8.6%	-18.9%	4.9%
Funds from Operations (FFO)						
Operating profit	486	823	868	780	639	637
Depreciation and amortisation	2	2	2	3	2	2
EBITDA	488	825	871	782	642	639
Capital gains, property revaluations and other	-311	-598	-616	-507	-342	-322
Result from disposal of trading properties	0	-2	0	0	0	0
Others	1	0	-6	0	-2	-2
Adjusted EBITDA	177	225	248	276	298	316
Financial expense	-26	-36	-40	-46	-52	-54
Tax	-23	-27	-28	-30	-32	-34
Minorities	-1	-1	-2	-2	-2	-2
FFO 1	128	160	178	198	212	226
CapEx	-34	-56	-67	-75	-83	-89
AFFO	94	104	111	122	129	137



BALANCE SHEET

All figures in EURm	2015	2016	2017	2018	2019E	2020E
Assets						
Current assets, total	627	1,028	796	1,238	1,608	1,528
Cash and cash equivalents	236	449	312	603	934	831
Traded securities at fair value though P&L	153	181	89	162	162	162
Trade and other receivables	226	220	260	319	360	382
Inventories - Trading property	12	27	12	17	16	17
Assets held for sale	0	150	123	136	136	136
Non-current assets, total	4,062	5,126	6,712	7,623	8,224	8,752
Equipment and intangible assets	9	16	20	24	26	29
Investment property	3,846	4,823	6,414	7,282	7,861	8,364
Equity accounted investees	0	118	37	26	28	29
Other LT assets	195	155	214	254	269	285
Deferred tax assets	11	15	28	37	40	44
Total assets	4,689	6,154	7,508	8,861	9,832	10,280
Shareholders' equity & debt						
Current liabilities, total	277	338	371	306	342	362
Short-term debt	55	29	62	22	22	22
Trade and other payables	190	252	267	242	276	293
Other current liabilities	32	58	42	42	45	47
Long-term liabilities, total	2,239	2,750	3,288	3,887	4,475	4,543
Long-term debt	792	897	919	846	634	634
Convertible and straight bonds	1,168	1,478	1,810	2,450	3,188	3,202
Deferred taxes	239	326	500	523	581	633
Other LT liabilities	40	50	59	69	72	75
Minority interests	142	197	364	409	457	507
Shareholders' equity	2,030	2,868	3,485	4,258	4,558	4,868
Total consolidated equity and debt	4,689	6,154	7,508	8,861	9,832	10,280
Ratios						
Current ratio (x)	2.26	3.04	2.15	4.04	4.70	4.22
Equity ratio	46.3%	49.8%	51.3%	52.7%	51.0%	52.3%
EPRA NAV ¹ (€m)	2,402	3,208	3,993	4,783	5,152	5,514
Net debt (€m)	1,626	1,783	2,393	2,560	2,748	2,864
Net debt / equity	0.8	0.6	0.7	0.6	0.6	0.6
Net debt / EBITDA (x)	9.2	7.9	9.7	9.3	9.2	9.1
Interest cover (x)	6.9	6.2	6.2	6.0	5.7	5.9
Loan-to-value (LTV)	41.9%	34.9%	36.4%	34.3%	34.2%	33.6%
Return on equity (ROE)	18.1%	21.3%	16.6%	12.5%	9.5%	9.3%

¹ including perpetual notes



CASH FLOW STATEMENT

All figures in EURm	2015	2016	2017	2018	2019E	2020E
Net income	394	653	639	583	476	498
Depreciation and amortisation	2	2	2	3	2	2
Profit from equity accounted investees	0	-1	-6	-1	-2	-2
Change in fair value of investment properties	-311	-598	-616	-507	-342	-322
Net finance expenses	26	47	83	82	73	54
Tax result	66	122	146	115	90	86
Others	1	1	1	1	0	0
Operating cash flow	177	227	248	276	298	316
Inventories - trading properties	-1	2	-6	-6	1	-1
Trade & other receivables	-25	-6	-39	-38	-40	-22
Trade & other payables	20	3	19	18	34	17
Provisions for other liabilities	5	-6	3	3	2	2
Tax paid	-19	-19	-23	-28	-32	-34
Net cash flow from operating activities	157	201	202	225	262	277
Investment in fixed/intangible assets	-4	-3	-6	-6	-5	-5
Investments & acquisitions of investment property	-406	-476	-374	-501	-236	-182
Acquisition of subsidiaries	-446	-111	-324	-112	0	0
Proceeds from investments in financial assets	-359	33	95	-100	-15	-16
Cash flow from investing	-1,215	-557	-608	-718	-256	-202
Debt financing, net	440	487	597	916	527	14
Equity financing, net	640	171	176	312	0	0
Other financing activities	-24	-44	-457	-385	-149	-138
Net paid financing expenses	-33	-46	-47	-56	-52	-54
Cash flow from financing	1,023	569	269	786	325	-178
Net cash flows	-34	213	-137	291	331	-103
Cash, start of the year	270	236	449	312	603	934
Cash, end of the year	236	449	312	603	934	831
Adjusted EBITDA / share (€)	1.27	1.46	1.50	1.65	1.78	1.88
FFO I	128	160	178	198	212	226
FFOPS I (€)	1.01	1.05	1.12	1.19	1.27	1.35
Y-Y Growth						
Operating cash flow	38.3%	27.8%	0.5%	11.0%	16.6%	5.9%
Adjusted EBITDA / share	34.5%	15.0%	3.0%	9.8%	7.5%	5.9%
FFO I	68.2%	25.1%	11.2%	11.1%	7.1%	6.7%
FFOPS I	52.8%	3.9%	6.5%	7.1%	6.0%	6.3%

FIRST BERLIN RECOMMENDATION & PRICE TARGET HISTORY

Report No.:	Date of publication	Previous day closing price	Recommendation	Price target
Initial Report	21 January 2013	€4.37	Buy	€14.30
2...30	↓	↓	↓	↓
31	7 May 2019	€21.22	Buy	€28.00
32	21 May 2019	€22.64	Buy	€28.00
33	6 June 2019	€23.44	Buy	€28.00
34	Today	€20.46	Buy	€28.00

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First Berlin Equity Research GmbH (hereinafter referred to as: "First Berlin") prepares financial analyses while taking the relevant regulatory provisions, in particular the German Securities Trading Act [WpHG], Regulation (EU) No 596/2014 of the European Parliament and of the Council of April 16, 2014, on market abuse (market abuse regulation) and the German Ordinance on the Analysis of Financial Instruments [FinAnV] into consideration. In the following First Berlin provides investors with information about the statutory provisions that are to be observed in the preparation of financial analyses.

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PRICE TARGET DATES

Unless otherwise indicated, current prices refer to the closing prices of the previous trading day.

AGREEMENT WITH THE ANALYSED COMPANY AND MAINTENANCE OF OBJECTIVITY

The present financial analysis is based on the author's own knowledge and research. The author prepared this study without any direct or indirect influence exerted on the part of the analysed company. Parts of the financial analysis were possibly provided to the analysed company prior to publication in order to avoid inaccuracies in the representation of facts. However, no substantial changes were made at the request of the analysed company following any such provision.

ASSET VALUATION SYSTEM

First Berlin's system for asset valuation is divided into an asset recommendation and a risk assessment.

ASSET RECOMMENDATION

The recommendations determined in accordance with the share price trend anticipated by First Berlin in the respectively indicated investment period are as follows:

Category		1	2
Current market capitalisation (in €)		0 - 2 billion	> 2 billion
Strong Buy ¹	An expected favourable price trend of:	> 50%	> 30%
Buy	An expected favourable price trend of:	> 25%	> 15%
Add	An expected favourable price trend of:	0% to 25%	0% to 15%
Reduce	An expected negative price trend of:	0% to -15%	0% to -10%
Sell	An expected negative price trend of:	< -15%	< -10%

¹ The expected price trend is in combination with sizable confidence in the quality and forecast security of management.

Our recommendation system places each company into one of two market capitalisation categories. Category 1 companies have a market capitalisation of €0 – €2 billion, and Category 2 companies have a market capitalisation of > €2 billion. The expected return thresholds underlying our recommendation system are lower for Category 2 companies than for Category 1 companies. This reflects the generally lower level of risk associated with higher market capitalisation companies.

RISK ASSESSMENT

The First Berlin categories for risk assessment are low, average, high and speculative. They are determined by ten factors: Corporate governance, quality of earnings, management strength, balance sheet and financial risk, competitive position, standard of financial disclosure, regulatory and political uncertainty, strength of brandname, market capitalisation and free float. These risk factors are incorporated into the First Berlin valuation models and are thus included in the target prices. First Berlin customers may request the models.

INVESTMENT HORIZON

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Legally required information regarding

- key sources of information in the preparation of this research report
- valuation methods and principles
- sensitivity of valuation parameters

can be accessed through the following internet link: <http://firstberlin.com/disclaimer-english-link/>

SUPERVISORY AUTHORITY: Bundesanstalt für Finanzdienstleistungsaufsicht (German Federal Financial Supervisory Authority) [BaFin], Graurheindorferstraße 108, 53117 Bonn and Lurgiallee 12, 60439 Frankfurt

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