

Grand City Properties S.A.

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

Q2/23 results

RATING
BUY

PRICE TARGET
€ 12.80

Return Potential 75.0%
 Risk Rating Medium

GUIDANCE RAISED; REVALUATIONS IN LINE

Spearheaded by 2.7% LFL rental growth, good operational performance continued in Q2 prompting management to up FFO 1 guidance to €175m - €185m (old: €170m -€180m) underpinned by LFL net rent of >2% (old: 1% - 2%). As anticipated, FFO 1 took a small hit in Q2 (-3.3%) due to higher financing costs and perpetual note attribution. The entire portfolio was revalued in Q2 resulting in a 5.4% decrease in valuation excluding CapEx. This is in line with expectations and should cheer investors concerned that much sharper declines were lurking. Cash and liquid assets (€0.7bn) now cover debt maturities until Q2/26. Meanwhile, there are signs that we are approaching the peak in interest rates, which should help end investor ennui. We remain Buy-rated on GCP with a €12.8 target price.

Valuations did not fall off a cliff Q2 was an encouraging sign that the residential portfolio will continue to perform well and help absorb rising financing costs. Property valuations were in focus with the entire portfolio assessed by external auditors to capture the most up-to-date market conditions. Higher discount and cap rates on the back of higher interest rates led to decrease in property valuations of some €532m, which is consistent with prior messaging. But the landlord gave no view on expectations for H2 and will continue to monitor the market. Deleveraging continued and helped offset portfolio devaluations to keep the LTV stable at 36%. GCP has secured €430m in bank debt YTD at a €1.3% margin over Euribor and has a €7.7bn pool of unencumbered assets in its debt management toolbox. The landlord has also repurchased ~€90m in bonds at an 8% discount but communicated that bond holders are largely content to keep their positions.

Other conference call takeaways The German and London residential markets are still characterised by acute low supply, and new construction has ground to a halt with financing at eye-watering levels. GCP's portfolio vacancy marked another record low (3.9%) with more and more renters staying put in Germany and the British capital. Meanwhile, upticks. . . (p.t.o.)

FINANCIAL HISTORY & PROJECTIONS

	2019	2020	2021	2022	2023E	2024E
Rental income (€m)	560.3	535.4	524.6	582.5	622.3	626.3
Y/Y growth	2.8%	-4.4%	-2.0%	11.0%	6.8%	0.6%
Adj. EBITDA (€m)	297.7	299.8	298.6	308.1	311.4	319.0
Net income (€m)	406.9	362.2	523.5	129.2	-297.0	109.0
EPRA NTA* (€m)	4,357.7	4,566.4	5,020.2	4,655.6	4,304.3	4,278.9
EPRA NTAPS* (€)	25.9	26.5	30.4	27.0	25.0	24.8
DPS (€)	0.82	0.82	0.83	0.00	0.76	0.73
FFO 1 (€m)	179.0	182.2	186.3	192.2	175.1	167.2
FFOPS 1 (€)	1.07	1.07	1.11	1.14	1.02	0.97
Liquid assets (€m)	1,069.5	1,697.9	1,113.5	436.8	939.0	717.5

*Updated to exclude RETT

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 16 Aug 2023

Closing Price	€ 7.32
Shares outstanding	176.18m
Market Capitalisation	€ 1,288.76m
52-week Range	€ 6.09 / 13.74
Avg. Volume (12 Months)	224,172

Multiples	2022	2023E	2024E
P/FFO 1	6.4	7.2	7.5
P/NTA	0.3	0.3	0.3
FFO 1 Yield	15.6%	13.9%	13.3%
Div. Yield	0.0%	10.4%	9.9%

STOCK OVERVIEW



COMPANY DATA

As of 30 Jun 2023

Liquid Assets	€ 709.0m
Investment Properties	€ 8,990.0m
EPRA NTA	€ 4,267.0m
Total Assets	€ 10,847.0m
Current Liabilities	€ 658.0m
Total Equity	€ 5,518.0m

SHAREHOLDERS

Edolaxia Ltd.	60.0%
Treasury	2.0%
Free float	38.0%



. . . in the *Mietspiegel* by German lawmakers to compensate for inflation effects have unlocked upside for further rent increases, although management noted that they have no sense as to how future policies will be shaped.

Q2 RESULT HIGHLIGHTS

GCP realised total LFL net rental growth of 2.7% comprising 0.3% occupancy increases and 2.4% in-place rent. In-place LFL rent contains 1.1% re-letting and 1.3% indexation. The strong performance owes to the aforementioned resilience of the German and London rental markets.

Table 1: Second quarter vs prior year and FBe

in €m	Q2/23	Q2/23E	Variance	Q2/22	Variance	H1/23	H1/22	Variance
Rental income	159	156	2.2%	139	15.1%	309	272	13.8%
Net rent	103	101	1.7%	98	4.9%	204	195	4.6%
Adjusted EBITDA	81	79	1.9%	76	6.5%	160	152	5.3%
margin	78%	78%	-	77%	-	78%	78%	-
FFO 1 (after perpetuals)	47	46	2.2%	49	-3.3%	94	97	-3.1%
FFOPS 1 (€) (after perpetuals)	0.27	0.26	2.2%	0.30	-10.0%	0.54	0.59	-8.5%

Source: First Berlin Equity Research; Grand City Properties

AEBITDA rose 6.5% Y/Y in the April-to-June period, driven chiefly by the rise in rental income. FFO 1, the key industry indicator for recurring operational cash flow, was close to our estimate at €46m in Q2/23 but fell short of the prior year result by 3.3%, mainly due to higher financing costs from new and existing debt plus perpetual note attribution. FFOPS 1 of €0.27 was ~10% lower Y/Y on the higher share count stemming from the scrip dividend.

On a six month basis, the headline KPIs performed on par with Q2 figures. FFO 1 took a 3.1% hit during the January-to-June period, owing to higher financing costs that offset the increases in NRI and AEBITDA in H1/23. FFO 2 was up 23% in H1 on the €250m in disposals executed at ~3% below book value. These allowed GCP to crystallise gains of ~€34m and boost liquidity. This is an encouraging development in a headwind year with many investors bracing for the worst.

So far portfolio devaluations close to expectations For the first time, management decided to have the entire portfolio revalued in one go in order to fully capture the latest state of the residential market. GCP brass had been calling for potential valuation downside of around 5% over the coming 12 months.

Table 2: Valuation parameter developments

	Unit	H1/23	YE22
Rent multiple	x	22.1	23.6
Value per m ²	€	2,183	2,282
Average discount rate	%	5.1	4.8
Average cap rate	%	3.9	3.8

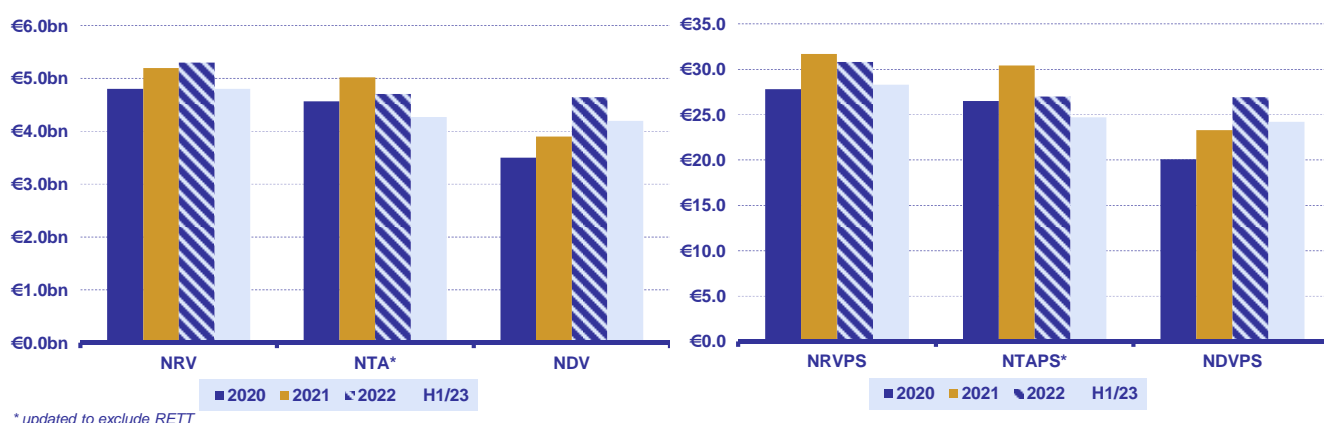
Source: First Berlin Equity Research; Grand City Properties

The reported €539m reduction in property valuations and capital gains for the period was equal to -5.4%, excluding CapEx. Adding back the CapEx invested for the period, the KPI stood at minus 4.8%. The negative result stems from the higher discount and cap rate used by external assessors (table 2).



Portfolio value dips to €2,183 / m² (Q1/23: €2,273 / m²) The company made no material acquisitions in H1/23. In-place rent stood at €8.4 / m² at the end of Q2 vs €8.2 / m² at YE22, while the portfolio vacancy rate remained at a record low of 3.9%. Annualised net rent tallied €398m at the end of the reporting period. The portfolio currently has rent reversionary potential to €465m (~17%) to be captured over the mid- to long-term.

Figure 1: EPRA BPR reporting



Source: First Berlin Equity Research; Grand City Properties

Deleveraging measures offset negative valuations Despite the portfolio write-downs, the balance sheet featured a stable LTV of 36% (YE22: 36%), or 47% assuming perpetual notes are counted as debt. The net debt / EBITDA and interest coverage (ICR) ratios stood at 10.4x and 5.8x respectively at the end of Q2.

Table 3: Financial highlights

in €m	Q2/23	2022	Variance
Cash & liquid assets	709	429	65.3%
Investment property	8,990	9,530	-5.7%
Unencumbered assets	7,663	8,665	-11.6%
Unencumbered assets ratio	83%	88%	-
Total equity	5,518	5,914	-6.7%
EPRA NTA*	4,267	4,656	-8.4%
Loans and borrowings	507	323	57.0%
Straight & convertible bonds	3,526	3,612	-2.4%
Loan-to-Value (LTV)	36%	36%	-
Equity ratio	51%	53%	-

* updated to exclude RETT

Source: First Berlin Equity Research; Grand City Properties

**Table 4: Overview of perpetual notes**

Currency	Outstanding Volume (m)	Current Coupon (%)	Reset Rate (%)	Call Date
EUR	200	6.332	3.887 + 5Y mid-Sw ap	22-Jan-2028
EUR	350	2.500	2.432 + 5Y mid-Sw ap	24-Oct-2023
EUR	700	1.500	2.184 + 5Y mid-Sw ap	09-Jun-2026

Source: First Berlin Equity Research; Grand City

The hybrid dilemma Grand City has roughly €1.25bn in hybrid notes on the balance sheet with another call date looming in October. In January, GCP brass let the coupon on the hybrid reprice at a sharply higher level of 6.332% (old: 2.75%). Given still unfavourable refinancing terms, we have already factored a reset of the October notes into our model. The full effect of the two resets will be a nearly €19m increase in coupon payments on an annualised basis.

Table 5: Updated guidance vs FBe

	Unit	Guidance		FBe 2023	2022A
		old	new		
FFO 1	€m	170 -180	175 -185	175	192
FFOPS 1	€	0.99 - 1.04	1.01 - 1.07	1.02	1.14
DPS *	€	0.74 - 0.78	0.76 - 0.80	0.76	0.00
LFL net rent growth	%	1.0 - 2.0	> 2.0	2.0	2.9
LTV	%	< 45	< 45	36	36

*subject to market conditions and AGM approval

Source: First Berlin Equity Research; Grand City

We have updated our 2023 forecasts to reflect the YTD operational performance and bring the numbers in line with the lower end of new guidance (table 5). Slightly higher rental income is mostly offset by greater property operating expenses.

Table 6: Changes to FBe and target price

	old	new	revision	upside	dividend yield	total upside
Price target (€)	12.8	12.8	0.0%	75.0%	10.4%	85.4%
	2023E			2024E		
in €m	Old	New	Variance	Old	New	Variance
Net rent (NRI)	404	408	0.9%	413	413	0.1%
AEBITDA	309	311	0.7%	320	319	-0.3%
margin (NRI)	77%	76%	-	-	77%	-
FFO 1	174	175	0.8%	168	167	-0.5%
Margin	43%	43%	-	-	40%	-
FFOPS 1 (€)	1.01	1.02	0.6%	0.97	0.97	-0.2%

Source: First Berlin Equity Research estimates



VALUATION MODEL

While operational upside cannot fully compensate for the higher financing costs, we think Grand City has found the formula to cope with the headwind year(s). After a series of rapid-fire rate hikes, we also think we may be finally approaching peak rates, which could spark new interest from investors. We stay Buy-rated on GCP with a €12.8 target price.

	Unit	2023E	2024E	2025E	2026E	2027E	2028E	2029E	2030E	TV
FFOPS 1	€	1.02	0.97	1.02	1.03	0.99	0.95	0.94	1.00	1.01
Payout ratio	%	75	75	75	75	75	75	75	75	75
Dividend (DPS)	€	0.76	0.73	0.76	0.77	0.74	0.72	0.70	0.75	0.76
Y/Y	%	n.a.	-0.05	0.05	0.01	-0.04	-0.03	-0.02	0.07	n.a.
NPV	€	0.74	0.66	0.65	0.62	0.56	0.50	0.46	0.46	8.1
Terminal growth rate	%	1.0								
Discount rate	%	6.8								
NPV of dividends	€	4.7								
NPV of TV	€	8.1								
Fair value per share	€	12.8								

		Terminal growth						
		-0.5%	0.0%	0.5%	1.0%	1.5%	2.0%	2.5%
Discount rate	6.2%	11.9	12.5	13.3	14.2	15.3	16.7	18.4
	6.4%	11.5	12.1	12.9	13.7	14.7	16.0	17.5
	6.6%	11.2	11.8	12.5	13.2	14.2	15.3	16.7
	6.8%	10.9	11.5	12.1	12.8	13.6	14.7	16.0
	7.0%	10.6	11.1	11.7	12.4	13.2	14.1	15.3
	7.2%	10.4	10.8	11.4	12.0	12.7	13.6	14.7
	7.4%	10.1	10.6	11.1	11.6	12.3	13.1	14.1

		Cost of debt						
		2.25%	2.50%	2.75%	3.00%	3.25%	3.50%	3.75%
Discount rate	6.2%	16.5	15.7	15.0	14.2	13.4	12.7	11.9
	6.4%	15.9	15.2	14.4	13.7	13.0	12.2	11.5
	6.6%	15.3	14.6	13.9	13.2	12.5	11.8	11.1
	6.8%	14.8	14.1	13.5	12.8	12.1	11.4	10.8
	7.0%	14.3	13.7	13.0	12.4	11.7	11.1	10.4
	7.2%	13.9	13.2	12.6	12.0	11.4	10.8	10.1
	7.4%	13.4	12.8	12.2	11.6	11.0	10.4	9.9



INCOME STATEMENT

All figures in EURm	2019	2020	2021	2022	2023E	2024E
Net rent	383	372	375	396	408	413
Rental and operating income	560	535	525	583	622	626
Property revaluations & capital gains	401	343	695	118	-540	-37
Result from equity-accounted investees	0	4	4	0	0	0
Property expenses	-253	-226	-218	-266	-300	-296
Cost of buildings sold	0	0	0	0	0	0
Administration expenses	-11	-11	-11	-11	-11	-11
Depreciation & amortisation	-4	-5	-8	-10	-9	-9
Operating income (EBIT)	693	640	986	413	-238	273
Finance expenses	-45	-53	-46	-47	-57	-61
Other financial results	-33	-46	-149	-137	-40	0
Pre-tax income (EBT)	615	542	791	229	-335	212
Current tax	-37	-31	-39	-39	-40	-41
Deferred tax	-84	-61	-135	-11	70	4
Tax result	-121	-93	-174	-50	31	-37
Minority interests	-53	-54	-69	-25	43	-21
Hybrid note investors	-33	-33	-25	-25	-35	-45
Net income	407	362	524	129	-297	109
Basic EPS (€)	2.43	2.13	3.12	0.77	-1.72	0.63
AEBITDA	298	300	299	308	311	319
Ratios						
AEBITDA margin (% of net rent)	77.8%	80.5%	79.7%	77.8%	76.4%	77.2%
Tax rate	12.5%	10.5%	13.1%	12.7%	12.7%	12.7%
Expenses (% of net rent)						
Property expenses	66.2%	60.8%	58.2%	67.2%	73.5%	71.6%
Administration expenses	3.0%	2.9%	3.0%	2.7%	2.7%	2.7%
Y-Y Growth						
Rental and operating income	2.8%	-4.4%	-2.0%	11.0%	6.8%	0.6%
Total revenues	2.8%	-4.4%	-2.0%	11.0%	6.8%	0.6%
Operating income	-11.1%	-7.6%	54.0%	-58.1%	n.m.	n.m.
Adjusted EBITDA	8.0%	0.7%	-0.4%	3.2%	1.1%	2.5%
Net income/ loss	-16.7%	-11.0%	44.5%	-75.3%	n.m.	n.m.
Funds from Operations (FFO)						
Operating profit	693	640	986	413	-238	273
Depreciation and amortisation	4	5	8	10	9	9
EBITDA	697	645	994	423	-229	282
Property revaluations & capital gains	-401	-343	-695	-118	540	37
Others	2	-2	-1	3	0	0
Adjusted EBITDA	298	300	299	308	311	319
Financial expense	-45	-53	-46	-47	-57	-61
Tax	-37	-31	-39	-39	-40	-41
Minority & JV contributions	-4	-1	-2	-5	-5	-5
FFO 1 (before perpetuals)	212	215	211	217	210	212
Perpetual note adjustment	-33	-33	-25	-25	-35	-45
FFO 1	179	182	186	192	175	167



BALANCE SHEET

All figures in EURm	2019	2020	2021	2022	2023E	2024E
Current assets, total	1,629	2,264	1,679	1,134	1,479	1,160
Cash and cash equivalents	914	1,412	895	325	827	606
Traded securities at fair value though P&L	155	286	218	112	112	112
Trade and other receivables	342	395	452	353	426	429
Inventories - Trading property	16	16	0	0	0	0
Assets held for sale	201	155	114	344	113	13
Non-current assets, total	8,223	8,602	9,883	9,997	9,426	9,728
Equipment and intangible assets	27	27	70	77	79	87
Investment property	7,981	8,043	9,364	9,550	8,960	9,234
Equity accounted investees	21	108	0	0	0	0
Other LT assets	151	373	397	316	329	342
Deferred tax assets	42	51	51	54	59	65
Total assets	9,851	10,866	11,562	11,131	10,905	10,887
Current liabilities, total	454	427	773	309	367	369
Short-term debt	33	147	455	5	5	5
Trade and other payables	288	209	216	225	279	276
Other current liabilities	133	71	103	79	84	89
Long-term liabilities, total	4,431	4,884	4,986	4,908	4,953	4,925
Long-term debt	521	427	353	319	500	750
Convertible and straight bonds	3,195	3,639	3,642	3,612	3,538	3,256
Deferred taxes	592	634	760	789	718	715
Other LT liabilities	122	183	231	189	197	205
Minority interests	444	535	615	666	623	644
Shareholders' equity	4,523	5,020	5,188	5,249	4,962	4,949
Total consolidated equity and debt	9,851	10,866	11,562	11,131	10,905	10,887
Ratios						
EPRA NTA* (€m)	4,358	4,566	5,020	4,656	4,304	4,279
EPRA NTAPS* (€)	25.9	26.5	30.4	27.0	25.0	24.8
Net debt (€m)	2,690	2,521	3,342	3,506	3,104	3,293
Net debt / equity (x)	0.6	0.5	0.6	0.7	0.6	0.7
Net debt / EBITDA (x)	9.0	8.4	11.2	11.4	10.0	10.3
Interest cover (x)	6.6	5.7	6.4	6.6	5.5	5.2
Loan-to-value (LTV)	33%	31%	36%	36%	36%	36%
Equity ratio	50%	51%	50%	53%	51%	51%
Return on equity (ROE)	9.9%	8.1%	10.6%	3.0%	-5.5%	3.1%

* updated to exclude RETT



CASH FLOW STATEMENT

All figures in EURm	2019	2020	2021	2022	2023E	2024E
Net income	493	449	617	179	-305	175
Depreciation and amortisation	4	5	8	10	9	9
Profit from equity accounted investees	0	-4	-4	0	0	0
Change in fair value of investment properties	-401	-343	-695	-118	540	37
Net finance expenses	78	98	195	184	97	61
Tax result	121	93	174	50	-31	37
Others	2	2	3	3	0	0
Operating cash flow	298	300	299	308	311	319
Change in working capital	-20	-29	-45	-61	-12	1
Tax paid	-28	-28	-37	-31	-40	-41
Net cash flow from operating activities	249	242	217	216	260	280
Investment in fixed/intangible assets	-7	-7	-8	-5	-11	-17
Net property investments / disposals	-194	-492	-465	-242	281	-211
Acquisition of subsidiaries	31	547	333	-4	0	0
Proceeds from investments in financial assets	117	-439	-58	82	-13	-13
Cash flow from investing	-53	-392	-198	-168	257	-241
Debt financing, net	360	559	-71	-486	107	-32
Equity financing, net	-33	207	-91	-25	-25	-35
Share buyback	0	0	-272	0	0	0
Dividend paid	-107	-71	-54	-56	0	-131
Other financing activities	-55	7	0	-2	-40	0
Net paid financing expenses	-50	-51	-50	-47	-57	-61
Cash flow from financing	115	651	-537	-617	-15	-260
Fx effects	0	-3	2	-1	0	0
Net cash flows	311	498	-517	-571	502	-222
Cash, start of the year	603	914	1,412	895	325	827
Cash, end of the year	914	1,412	895	325	827	606
AEBITDA / share (€)	1.77	1.74	1.69	1.75	1.77	1.81
FFO 1	179	182	186	192	175	167
FFOPS 1 (€)	1.07	1.07	1.11	1.14	1.02	0.97
Y-Y Growth						
Operating cash flow	11.1%	-2.9%	-10.4%	-0.4%	20.1%	7.7%
Adjusted EBITDA / share	7.3%	-1.6%	-2.8%	3.2%	1.1%	2.5%
FFO 1	6.8%	1.8%	2.3%	3.2%	-8.9%	-4.5%
FFOPS 1	5.8%	0.3%	3.6%	2.8%	-11.1%	-4.5%

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Ggf. Inhaltlich Verantwortlicher gem. § 6 MDStV

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The production of this recommendation was completed on 17 August 2023 at 15:20

Person responsible for forwarding or distributing this financial analysis: Martin Bailey

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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.

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...47	↓	↓	↓	↓
48	18 March 2022	€19.92	Buy	€28.00
49	18 May 2022	€16.43	Buy	€24.50
50	16 August 2022	€13.86	Buy	€24.00
51	12 October 2022	€9.29	Buy	€19.00
52	17 November 2022	€10.51	Buy	€16.80
53	21 March 2023	€7.32	Buy	€12.80
54	21 May 2023	€7.18	Buy	€12.80
55	17 May 2023	€7.41	Buy	€12.80
56	Today	€7.32	Buy	€12.80

INVESTMENT HORIZON

Unless otherwise stated in the financial analysis, the ratings refer to an investment period of twelve months.

UPDATES

At the time of publication of this financial analysis it is not certain whether, when and on what occasion an update will be provided. In general First Berlin strives to review the financial analysis for its topicality and, if required, to update it in a very timely manner in connection with the reporting obligations of the analysed company or on the occasion of ad hoc notifications.

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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: <https://firstberlin.com/disclaimer-english-link/>

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