

GRAND CITY Properties S.A.

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

Q2/20
 Results

RATING
BUY

PRICE TARGET
€ 27.50

Return Potential 32.7%
 Risk Rating Medium

STEADY RESULTS CONTINUE IN Q2

GCP showed continued stable operating performance in Q2 with pandemic headwinds having little effect. FFO 1 led H1/20 headline figures with 2% annualised growth, despite a 4% decline in rental income. The latter owes to net disposals during H1 as management continue to cull the portfolio of mature properties in non-core locations. GCP confirmed 2020 guidance (FFOPS 1: €1.27 to €1.31), and €1.5bn in liquid assets provides good flexibility to react to fast changing markets. We remain Buy-rated on Grand City with an unchanged price target of €27.5.

Second quarter conference call takeaways Grand City has emerged from the pandemic lockdowns with operations largely unscathed. Only the London portfolio showed any noticeable covid-19 effects with a temporary uptick in vacancy to 8% (YE19: 4%). This owes to the stop in re-letting activities during the lockdown, which was far stricter than in Germany. However, lettings have already picked up in Q3 as the British capital comes back online. London rent deferment rates were around 3% vs ~1% for GCP's German properties, but management stated that collections are back to pre-virus levels and expect to collect postponed rents soon.

What else has changed? The first six months also saw net disposals of €200m. These mainly included mature properties in secondary cities of North Rhine-Westphalia (NRW), while acquisitions were largely shutdown in Q2. Management noted little change in pricing so far during the crisis but cautioned that covid-19 effects have probably not fully played out yet. Acquisitions restarted end of H1 with ~€150m signed deals post-reporting, and the pipeline remains around €500m with London remaining an attractive target, despite the capital's pandemic troubles. Management continue to target a 20% to 25% British capital portfolio footprint. Meanwhile, the Berlin rent cap days appear numbered. Management continue to expect this to be overturned by the federal court. We also note that Bavaria recently struck down a proposed rent cap. (p.t.o.)

FINANCIAL HISTORY & PROJECTIONS

	2016	2017	2018	2019	2020E	2021E
Rental income (€m)	435.67	494.89	544.98	560.30	567.80	577.46
Y/Y growth	30.6%	13.6%	10.1%	2.8%	1.3%	1.7%
Adj. EBITDA (€m)	224.73	247.98	275.53	297.66	308.03	313.27
Net income ² (€m)	542.5	534.6	488.6	406.9	460.7	381.0
EPS (diluted) (€)	3.25	3.06	2.76	2.29	2.57	2.13
EPRA NAV ¹ (€m)	3208.45	3993.06	4783.07	5150.48	5520.51	5810.95
DPS (€)	0.68	0.73	0.64	0.82	0.83	0.84
FFO 1 (€m)	160.12	178.01	197.85	211.97	214.51	216.77
FFOPS 1 (€)	1.05	1.12	1.19	1.27	1.28	1.29
Liquid assets (€m)	630.27	401.48	765.04	1,069.46	1,858.62	1,491.50

¹ including perpetual notes ² after minority interests and hybrid investors

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.

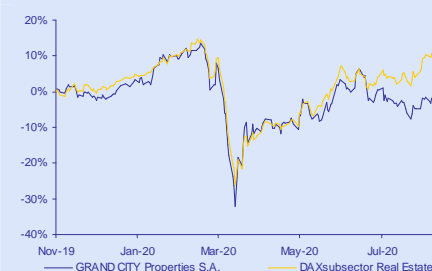
MARKET DATA

As of 17 Aug 2020

Closing Price	€ 20.72
Shares outstanding	168.01m
Market Capitalisation	€ 3481.17m
52-week Range	€ 14.28 / 23.94
Avg. Volume (12 Months)	277,127

Multiples	2019	2020E	2021E
P/FFO 1	16.4	16.2	16.1
P/EPRA NAV	0.7	0.6	0.6
FFO 1 Yield	6.1%	6.2%	6.2%
Div. Yield	4.0%	4.0%	4.0%

STOCK OVERVIEW



COMPANY DATA

As of 30 Jun 2020

Liquid Assets	€ 1,524.00m
Investment properties	€ 7,961.00m
EPRA NAV ¹	€ 5,200.00m
Total Assets	€ 10,749.00m
Current Liabilities	€ 584.00m
Total Equity	€ 5,008.00m

¹ including perpetual notes

SHAREHOLDERS

Edolaxia Ltd.	40.0%
Free float	60.0%



ANOTHER STEADY QUARTER

Revenue and net rent were marginally lower Y/Y due to the YTD net disposals. But adjusted EBITDA and FFO 1 narrowly missed last year's marks (~1%). Thanks to operational efficiencies, property operating expenses were ~10% lower on an annualised basis and helped offset an uptick in financing expenses.

Figure 1: Second quarter results vs FBe and prior year

in €m	Q2/20	Q2/20E	Variance	Q2/19	Variance	H1/20	H1/19	Variance
Rental income	132	136	-2.6%	139	-4.8%	268	278	-3.8%
Net rent	92	92	-0.6%	95	-3.4%	186	189	-1.5%
Adjusted EBITDA	73	74	-1.2%	74	-0.8%	147	146	0.5%
margin	55%	54%	-	53%	-	55%	53%	-
FFO 1	53	51	3.1%	53	-1.1%	108	106	1.9%
FFOPS 1 (€)	0.31	0.30	3.1%	0.32	-0.6%	0.64	0.64	1.1%

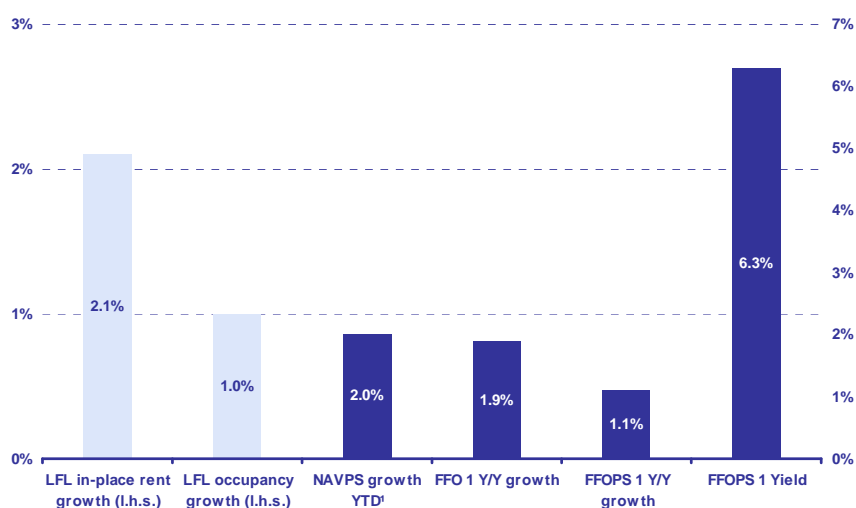
Source: First Berlin Equity Research; Grand City Properties

On a six month basis, net rent dipped some 4% on the aforementioned net disposals. Acquisition activities were shut down during the peak of the covid-19 crisis but resumed towards the end of the reporting period. Adjusted EBITDA matched the prior year figure and helped propel and a 1.9% gain in FFO 1 to €108m.

The results were spurred by another good like-for-like (LFL) performance. As of Q2, GCP realised total LFL net rental growth of 3.1% comprising 1.0% occupancy increases and 2.1% in-place rent. The latter contains 1.2% indexation and 0.9% re-letting.

The company reported Q2 property revaluations and capital gains of €151m vs €91m in the prior year (+65%), thanks to a 3% LFL increase led by Berlin, London, Mannheim, and North Rhine-Westphalia. Roughly two thirds of the portfolio has been re-valued thus far.

Figure 2: Operating performance as of 30 June



¹ 5% factoring in the dividend

Source: First Berlin Equity Research, Grand City Properties

FFO 2 amounted to €216m in H1 (H1/19: €191m). Grand City disposed of €350m in non-core and mature assets at a multiple of 15x rental income during the first six months as part of its cash recycling strategy. Sold properties encompassed around 7k flats with a 15%



vacancy rate in secondary locations of NRW. The management team also noted post-reporting disposals of ~€400m expected to close by YE20 against acquisitions of €150m. We have adjusted our targets to account for the updated figures.

Table 1: Portfolio overview June 2020

	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	1,613	1,262	6.5%	88	6.0	18,414	1,278	5.4%
Berlin	1,784	559	5.0%	55	8.5	7,599	3,191	3.0%
Dresden / Leipzig / Halle	1,038	925	8.6%	53	5.3	15,921	1,122	5.1%
Mannheim / KL / Frankfurt / Mainz	433	226	2.8%	21	7.8	3,821	1,914	4.8%
Nuremberg / Fürth / Munich	311	116	3.4%	13	9.4	1,802	2,682	4.3%
Hamburg / Bremen	377	297	5.4%	20	6.1	4,265	1,270	5.4%
London	918	113	8.2%	36	29.5	2,174	8,144	4.0%
Others	1,021	985	7.0%	66	6.2	16,650	1,039	6.4%
Development rights & new build	482	-	-	-	-	-	-	-
Total	7,977	4,483	6.5%	352	7.0	70,646	1,672	4.7%

Source: First Berlin Equity Research; Grand City Properties

As of Q2, EPRA NAV totalled €4.2bn (€24.9 / share) compared to €4.1bn at year end 2019 (€24.5 / share, +2%). The increase stems from net profits during H1/20 and includes a provision for the dividend distribution. Adjusted for the dividend, NAVPS growth is 5%. Including the perpetual notes, which are classified as equity under IFRS, this KPI stood at €5.2bn or €30.9 / share.

Table 2: Financial highlights

in €m	Q2/20	2019	Variance
Cash & liquid assets	1,525	1,063	43%
Investment property ¹	7,977	7,972	0%
Total equity	5,008	4,967	1%
EPRA NAV incl. hybrid notes	5,200	5,150	1%
EPRA NAV	4,188	4,120	2%
Interest bearing debt	661	559	18%
Straight bonds	3,511	2,920	20%
Convertible bond	276	275	0%
Loan-to-Value (LTV)	36%	33%	-
Equity ratio	47%	50%	-

¹ including inventories-trading property

Source: First Berlin Equity Research; Grand City Properties

Balance sheet flush with cash Grand City exited the six month period with cash & liquid assets of >€1.5bn giving management good financial flexibility to pursue acquisition opportunities, optimise the debt portfolio, and buffer against a resurgence in covid-19. Net debt stood at €2.9bn vs €2.7bn at YE19, and the debt structure features an LTV of 36%, 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 4.8x and 6.1x respectively at the end of Q2. The latter is comfortably above the >=2.0x covenant. The capital structure also includes €6.2bn in unencumbered assets or 77% of portfolio value.



ONLY MINOR CHANGES TO FB TARGETS ON CONFIRMED GUIDANCE

Table 3: 2020 guidance vs FBe

	Unit	2020 Guidance	FBe 2020
FFO 1	€m	213 - 220	215
FFOPS 1	€	1.27 - 1.31	1.28
DPS	€	0.82 - 0.85	0.83
LFL net rent growth	%	1.5 - 2.0	1.8
LTV	%	<45	30

Source: First Berlin Equity Research; Grand City Properties

We now expect disposals to outpace acquisitions in 2020 after the latter were temporarily suspended due to the pandemic. However, the impact on rental income is marginal, given that the bulk of deals will close late in the year.

Table 4: Changes to forecasts and price target

	old	new	revision	upside	dividend yield	total upside
Price target (€)	27.5	27.5	0.0%	32.5%	4.0%	36.4%
in €m	Old	2020E New	Variance	Old	2021E New	Variance
Net rent (NRI)	386	383	-0.7%	400	390	-2.6%
Adj. EBITDA	310	308	-0.6%	322	313	-2.7%
margin (NRI)	80%	80%	-	81%	80%	-
FFO 1	213	215	0.7%	221	217	-1.9%
Margin	55%	56%	-	55%	56%	-
FFOPS 1 (€)	1.27	1.28	0.7%	1.32	1.29	-1.9%

Source: First Berlin Equity Research estimates

We have recalibrated forecasts to: (1) reflect the impact of net disposals on 2020 net rent; (2) account for the improved property operating expense ratio; and (3) factor in the better than expected revaluation gains in Q2.



ECONOMIC PROFIT MODEL

With external growth largely idling, we expect upside to be driven chiefly by the embedded portfolio upside reported at 20%, or 28% assuming no Berlin rent cap. Our price target remains unchanged at €27.5, and we stick to our Buy rating. In our view, Grand City is an attractive investment with good upside potential during unstable times.

in €m	2020E	2021E	2022E	2023E	TV
EBITDA	308	313	331	350	353
(+) Revaluations	401	296	287	285	51
(+) Investment income	2	0	0	0	0
(-) Tax expense	107	91	93	95	61
NOPAT	604	518	526	539	344
Total assets	10,850	11,034	11,619	12,116	12,116
(-) Current liabilities	414	427	450	473	473
(+) Current financial debt	33	33	33	33	33
(-) Cash	1,703	1,336	1,369	1,321	1,321
(+) Deferred taxes	610	654	696	738	738
Capital employed (CE)	9,376	9,958	10,530	11,092	11,092
ROCE	6.6%	5.4%	5.1%	5.0%	3.1%
WACC	3.1%	3.1%	3.1%	3.1%	3.1%
ROCE-WACC	3.5%	2.3%	2.0%	1.9%	0.0%
Economic Profit	320	220	210	206	2
NPV	316	211	195	186	70
Fair value calculation					
Total return	979				
(+) EPRA NAV (2019)	4,120				
(-) Dividend to be paid	138				
Equity value	4,961				
Diluted SO (m)	181				
Fair value per share (€)	27.5				
Valuation metrics					
Price target (€)	27.50	27.50	27.50	27.50	
Share price (€)	20.76	20.76	20.76	20.76	
Return potential	32.5%	32.5%	32.5%	32.5%	
Dividend yield	4.0%	4.0%	4.2%	4.2%	
Total return potential	36.5%	36.5%	36.6%	36.7%	
FFOPS 1 yield	6.2%	6.2%	6.4%	6.6%	
DPS (€)	0.83	0.84	0.84	0.89	



INCOME STATEMENT

All figures in EURm	2016	2017	2018	2019	2020E	2021E
Net rent	285	328	364	383	383	390
Rental and operating income	436	495	545	560	568	577
Revenue from sale of buildings	7	2	0	0	0	0
Revenue	443	497	545	560	568	577
Property revaluations & capital gains	598	616	507	401	401	296
Result from equity-accounted investees	1	6	1	0	2	0
Property expenses	-204	-239	-263	-256	-250	-254
Cost of buildings sold	-5	-1	0	0	0	0
Administration expenses	-10	-11	-11	-13	-13	-13
Operating income (EBIT)	823	868	780	693	708	607
Finance expenses	-36	-40	-46	-45	-57	-60
Other financial results	-11	-43	-36	-33	0	0
Pre-tax income (EBT)	775	786	698	615	651	547
Tax and deferred tax expenses	-122	-146	-115	-121	-100	-85
Minority interests	-88	-80	-64	-53	-58	-49
Hybrid note investors	-23	-24	-30	-33	-33	-33
Net income	542	535	489	407	461	381
Basic EPS (€)	3.56	3.35	2.95	2.43	2.74	2.27
Diluted EPS (€)	3.25	3.06	2.76	2.29	2.57	2.13
Adjusted EBITDA	225	248	276	298	308	313
Ratios						
Adjusted EBITDA margin	51.6%	50.1%	50.6%	53.1%	54.3%	54.3%
Tax rate	11.9%	-11.3%	-10.8%	-12.5%	11.5%	11.5%
Expenses as % of revenues						
Property expenses	46.8%	48.3%	48.2%	45.6%	44.0%	44.0%
Administration expenses	2.2%	2.2%	1.9%	2.3%	2.3%	2.3%
Y-Y Growth						
Rental and operating income	30.6%	13.6%	10.1%	2.8%	1.3%	1.7%
Total revenues	32.7%	12.2%	9.7%	2.8%	1.3%	1.7%
Operating income	69.3%	5.5%	-10.2%	-11.1%	2.2%	-14.3%
Adjusted EBITDA	26.8%	10.3%	11.1%	8.0%	3.5%	1.7%
Net income/ loss	57.7%	-1.5%	-8.6%	-16.7%	13.2%	-17.3%
Funds from Operations (FFO)						
Operating profit	823	868	780	693	708	607
Depreciation and amortisation	2	2	3	4	3	3
EBITDA	825	871	782	697	711	610
Capital gains, property revaluations and other	-598	-616	-507	-401	-401	-296
Result from disposal of trading properties	-2	0	0	0	0	0
Others	0	-6	0	2	-2	0
Adjusted EBITDA	225	248	276	298	308	313
Financial expense	-36	-40	-46	-45	-57	-60
Tax	-27	-28	-30	-37	-35	-36
Minorities	-1	-2	-2	-4	-1	-1
FFO 1	160	178	198	212	215	217
CapEx	-56	-67	-75	-76	-72	-75
AFFO	104	111	122	136	142	142



BALANCE SHEET

All figures in EURm	2016	2017	2018	2019	2020E	2021E
Assets						
Current assets, total	1,028	796	1,238	1,629	2,463	2,102
Cash and cash equivalents	449	312	603	914	1,703	1,336
Traded securities at fair value though P&L	181	89	162	155	155	155
Trade and other receivables	220	260	319	342	389	396
Inventories - Trading property	27	12	17	16	14	14
Assets held for sale	150	123	136	201	201	201
Non-current assets, total	5,126	6,712	7,623	8,223	8,387	8,931
Equipment and intangible assets	16	20	24	27	30	33
Investment property	4,823	6,414	7,282	7,981	8,088	8,612
Equity accounted investees	118	37	26	21	23	23
Other LT assets	155	214	254	151	200	212
Deferred tax assets	15	28	37	42	47	51
Total assets	6,154	7,508	8,861	9,851	10,850	11,034
Shareholders' equity & debt						
Current liabilities, total	338	371	306	454	414	427
Short-term debt	29	62	22	33	33	33
Trade and other payables	252	267	242	288	240	244
Other current liabilities	58	42	42	133	141	150
Long-term liabilities, total	2,750	3,288	3,887	4,431	5,088	4,969
Long-term debt	897	919	846	521	500	450
Convertible and straight bonds	1,478	1,810	2,450	3,195	3,805	3,681
Deferred taxes	326	500	523	592	656	705
Other LT liabilities	50	59	69	122	127	133
Minority interests	197	364	409	444	502	550
Shareholders' equity	2,868	3,485	4,258	4,523	4,846	5,087
Total consolidated equity and debt	6,154	7,508	8,861	9,851	10,850	11,034
Ratios						
Current ratio (x)	3.04	2.15	4.04	3.59	5.95	4.93
Equity ratio	50%	51%	53%	50%	49%	51%
EPRA NAV ¹ (€m)	3,208	3,993	4,783	5,150	5,521	5,811
Net debt (€m)	1,783	2,393	2,560	2,690	2,479	2,673
Net debt / equity (x)	0.6	0.7	0.6	0.6	0.5	0.5
Net debt / EBITDA (x)	7.9	9.7	9.3	9.0	8.0	8.5
Interest cover (x)	6.2	6.2	6.0	6.6	5.4	5.2
Loan-to-value (LTV)	35%	36%	34%	33%	30%	30%
Return on equity (ROE)	21.3%	16.6%	12.5%	9.9%	10.3%	8.2%



CASH FLOW STATEMENT

All figures in EURm	2016	2017	2018	2019	2020E	2021E
Net income	653	639	583	493	551	462
Depreciation and amortisation	2	2	3	4	3	3
Profit from equity accounted investees	-1	-6	-1	0	-2	0
Change in fair value of investment properties	-598	-616	-507	-401	-401	-296
Net finance expenses	47	83	82	78	57	60
Tax result	122	146	115	121	100	85
Others	1	1	1	2	0	0
Operating cash flow	227	248	276	298	308	313
Change in working capital	-7	-24	-23	-20	-84	6
Tax paid	-19	-23	-28	-28	-35	-36
Net cash flow from operating activities	201	202	225	249	189	284
Investment in fixed/intangible assets	-3	-6	-6	-7	-6	-6
Net property investments / disposals	-476	-374	-501	-194	294	-228
Acquisition of subsidiaries	-111	-324	-112	31	0	0
Proceeds from investments in financial assets	33	95	-100	117	-49	-12
Cash flow from investing	-557	-608	-718	-53	240	-246
Debt financing, net	487	597	916	360	588	-173
Equity financing, net	171	176	312	-33	-33	-33
Dividend paid	-38	-112	-79	-107	-138	-139
Other financing activities	-5	-345	-306	-55	0	0
Net paid financing expenses	-46	-47	-56	-50	-57	-60
Cash flow from financing	569	269	786	115	361	-405
Net cash flows	213	-137	291	311	789	-367
Cash, start of the year	236	449	312	603	914	1,703
Cash, end of the year	449	312	603	914	1,703	1,336
Adjusted EBITDA / share (€)	1.46	1.50	1.65	1.77	1.83	1.87
FFO I	160	178	198	212	215	217
FFOPS I (€)	1.05	1.12	1.19	1.27	1.28	1.29
Y-Y Growth						
Operating cash flow	27.8%	0.5%	11.0%	11.1%	-24.3%	50.2%
Adjusted EBITDA / share	15.0%	3.0%	9.8%	7.3%	3.5%	1.7%
FFO 1	25.1%	11.2%	11.1%	7.1%	1.2%	1.1%
FFOPS 1	3.9%	6.5%	7.1%	6.1%	0.8%	1.0%

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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...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	20 August 2019	€20.46	Buy	€28.00
35	20 November 2019	€21.44	Buy	€28.00
36	10 March 2020	€20.66	Buy	€28.00
37	20 March 2020	€16.04	Buy	€28.00
38	19 May 2020	€19.78	Buy	€27.50
39	Today	€20.72	Buy	€27.50

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/>

SUPERVISORY AUTHORITY: Bundesanstalt für Finanzdienstleistungsaufsicht (German Federal Financial Supervisory Authority) [BaFin], Graurheindorferstraße 108, 53117 Bonn and Marie-Curie-Straße 24-28, 60439 Frankfurt am Main

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