

Deutsche Euroshop

Internet version of our Flash Note dated 10 November 2005;
for domestic institutional clients only

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Deutsche Euroshop

Germany

Capital increase and acquisition announced following Q3 figures; we remain Overweight

- ▶ Q3 in line with HSBC and consensus figures; company FY 2005 guidance increased
- ▶ 10% capital increase placed @EUR43 per share
- ▶ Acquisition of a new shopping centre for EUR108m announced
- ▶ We remain Overweight and lower our notional target price to EUR50.6 from EUR51.4 per share

 Equity
Flash note

Q3 in line with consensus – guidance increased

Deutsche Euroshop's Q3 2005 figures were in line with Q3 2005 consensus and HSBC forecasts. Sales stood at EUR18.1m, EBIT at EUR14.5m and net profit after minorities at EUR4.7m (EPS EUR0.30). The 9m like for like sales grew by 2% y-o-y, the 9m net income adjusted for disposal gains and currency effects grew by 41% y-o-y. On quarter to quarter basis top and bottom line grew by 0-2%.

Management raises full year guidance by 2% at the sales level and by 7% on the PBT level. In the conference call 10 November at 10am CET the CEO Claus-Matthias Böge did not give guidance for 2006. We expect (mostly external) double digit growth in sales and earnings. This is not a surprise as long-term Euroshop aims to invest EUR100-150m in new centres annually.

Dividend is intended to be increased from EUR1.92 to EUR2.00 for 2005, in line with our forecast. The FCF in 2005 is expected by management to be EUR32.9m while dividend payment would need EUR31.25m.

Capital increase

Deutsche Euroshop has placed new shares in the market. The shares have been placed at EUR43.00 with European and US investors. According to the CEO the capital increase was oversubscribed. The gross cash proceeds were cEUR67.2m. This capital is needed to finance the new shopping centre acquisition and a possible further acquisition in the future, according to the company. At the moment, there is no information whether another capital increase will be necessary in 2006 if new investments are made.

Shopping centre acquisition

After an increase in stakes in three shopping centres for EUR20m, Euroshop announced that it would acquire a shopping centre in Dessau (East Germany) for EUR108m. Furthermore, it plans to buy another shopping centre in 2005 for EUR80m. This would mean an investment

Stock data

Current price	Reuters	Bloomberg equity	Bloomberg debt	Valuation range
(EUR) 45.10	DEQGn.DE	DEQ GR		EUR45.6-55.7

Source: HSBC

Research team*

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volume of cEUR210m in total in 2005 which is above the company's annual target.

Since Euroshop will acquire 94.9% of the Dessau centre effective from 2006, it appears that this shopping centre will not be in the books in 2005. The centre has 25,000 square meters retail space and 5,000 office space with 80 stores. The vacancy rate is at 2% which is above Deutsche Euroshop's occupancy rate of 1%. The annual rent income of this centre is EUR7.7m which results in an initial yield at >7%. (On average Euroshop's shopping centres are valued at cap rates of 6.53% as of FY 2004). Management expects rents in Dessau to grow 1-2% pa in this centre.

Despite a difficult German retail market, retailers in Deutsche Euroshop's shopping centres experience continuous growth in sales. According to the CEO there is a yield compression in Eastern European countries. According to Jones Lang Lasalle prime yields in German shopping centres declined by c0.5% in 2005 compared to 2004.

NAV adjustment

We adjust the NAV per share following the capital increase. The dilution is small and the adjusted NAV is EUR43.79 per share. This is because the stock trades close to its NAV.

Capital increase calculation

In EUR	FY 2004 NAV	Price	Clean price after 2% transaction costs	NAV (in EURm)
Number of old shares (million)	15.63	43.96		686.9
Number of new shares in (million)	1.56	43.0	42.14	65.8
Total number of shares	17.19			752.7
New NAV per share	43.79			
Dilution	-0.4%			

Source: Company data, HSBC Trinkaus & Burkhardt

Deutsche Euroshop trades at a premium of c1% to its adjusted NAV of EUR43.79 per share. However, European retail peers are trading at a premium of 22% which indicates a relative undervaluation of the stock. In August 2005 the peer group was valued at a premium of c30%. We expect NAV per share of EUR44.74 for 2005e, EUR45.63 for 2006e and EUR46.67 for 2007e.

We derive our target price from the average of estimated NAV in 2006, the P/NAV multiple of the retail European peer group (1.22x) and a DCF value. This methodology yields a range of EUR45.6-55.7 with a midpoint at cEUR50.6 per share. We do not apply a discount to this number as we think that sales growth in Deutsche Euroshop's domestic shopping centres will be higher than in the difficult German retail market in general. We stick to our Overweight rating and lower our notional target price to EUR50.6 (previously EUR51.4) in a range of EUR45.6-55.7 (previously EUR44.7-58.1) per share.

Valuation in EUR per share

Valued at HSBC 2006e NAV	45.6
Valued at 22% premium to NAV	55.7
Valued at DCF	51.0
Midpoint (45.6-55.7) per share	50.6

Source: HSBC Trinkaus & Burkhardt

Deutsche Euroshop FY2004 figures

Q3 2005 (EURm)	Q3 2004a	Q2 2005a	Q3 2005 Consensus**	HSBC Q3 2005e	Q3 2005a	q-o-q	y-o-y	a/e	HSBC 9m 2005e	9m 2005a	HSBC FY 2005e	Old FY 2005 company guidance*	New FY 2005 company guidance*
Revenues	14.6	17.8	18.0	18.0	18.1	2%	24%	1%	53.2	53.3	71.8	68-72	71-72
EBITDA	15.4	14.6	14.3	14.2	14.5	0%	-6%	2%	42.6	42.9	57.7	53-56	56-58
EBIT	15.4	14.5	14.3	14.2	14.5	0%	-6%	2%	42.6	42.9	57.7	53-56	56-58
Pretax profit	9.9	7.5	na	7.6	7.6	1%	-24%	-1%	22.1	22.1	53.6***	28-30	30-32
Net income (after minorities)	6.6	4.6	4.7	4.7	4.7	2%	-29%	-1%	13.7	13.7	36.2	n.a.	n.a.
EPS (EUR)	0.42	0.29	0.30	0.30	0.30	2%	-29%	-1%	0.88	0.87	2.19	n.a.	n.a.

Note: *before shopping centre revaluations, ** Reuters consensus, ***including EUR22.2m revaluation gains

Source: Company data, HSBC Trinkaus & Burkhardt

The main risk to our rating is a worsening of the economic situation, especially in Germany. This could put pressure on the occupancy rate in Euroshop's centres, although rental contracts are long term. A further risk would be a halt in further acquisition efforts of the management which are the main driver of sales and profit growth.

Disclosure appendix

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This report addresses only the long-term investment opportunities of the companies referred to in the report. As and when HSBC publishes a short-term trading idea the stocks to which these relate are identified on the website. Details of these short-term investment opportunities can be found under the Reports section of this website.

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Rating definitions for long-term investment opportunities

Stock (vs Local universe)

- ▶ Overweight (Buy)
- ▶ Neutral (Hold)
- ▶ Underweight (Sell)

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For companies covered on a sector basis, we apply a ratings structure which ranks the stocks according to their notional target price vs current market price and then categorises (approximately) the top 40% as Overweight, the next 40% as Neutral and the last 20% as Underweight. The performance horizon is 2 years. The notional target price is defined as the mid-point of the analysts' valuation for a stock.

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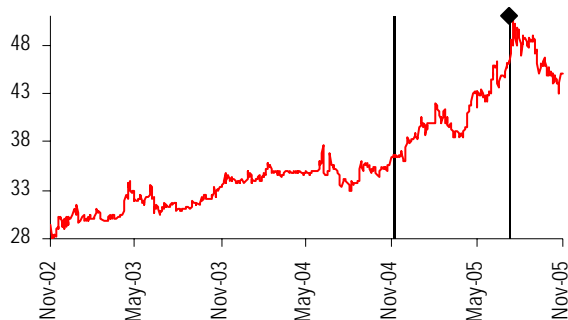
Rating distribution for long-term investment opportunities

As of 10 November 2005, the distribution of all ratings published is as follows:

Overweight/Buy	43%	(38% of these provided with Investment Banking Services)
Neutral/Hold	40%	(38% of these provided with Investment Banking Services)
Underweight/Sell	17%	(39% of these provided with Investment Banking Services)

Share price and rating changes for long-term investment opportunities

Deutsche Euroshop share price performance EUR vs
HSBC rating history



Source: HSBC

Rating & price target history

From	To	Date
N/A	N/R	15 November 2004
N/R	Overweight	19 July 2005

Target price	Value	Date
Price 1	N/A	15 November 2004
Price 2	51.00	19 July 2005

Source: HSBC

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