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1798

EQUITY RESEARCH
GERMANY

Deutsche Euroshop

Buy Target Price: € 57.00

Real Estate

Start Coverage

Reuters symbol: DEQGn.DE
ISIN: DE0007480204

Price on 8 February 2006: € 50.50
High/Low 12 month: € 54.41/38.40

Capital	
Market capitalization	€ 867.8 m
Number of shares	17.2 m
Subscribed capital	€ 22.0 m

Ownership structure		
widely spread	ord	80.7%
Otto family	ord	19.3%

Upcoming events	
20 Apr 2006 :	Result 2005
15 May 2006 :	Q1 2006
22 Jun 2006 :	AGM
11 Aug 2006 :	Q2
14 Nov 2006 :	Q3

- **High-quality property investments**

- **Further growth is marked out**

- **Price target of € 57**

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Price / Relative strength to MDAX

Source : JCF M.M.Warburg Investment Research

in €	2005e	2006e	2007e	2008e
EPS (current)	**2.82**	**2.29**	**2.36**	**2.56**
EPS (previous)	---	---	---	---
CFPS	1.01	1.63	1.76	1.97
Dividend	2.00	2.10	2.20	2.30

in € m	2005e	2006e	2007e	2008e
Sales	71.8	90.6	94.2	99.6
EBITDA	58.8	75.2	78.8	84.2
EBIT	58.8	75.2	78.8	84.1
Net income	44.5	39.3	40.5	44.0
Cash flow	16.0	28.0	30.3	33.8
ROCE (EBIT/CE)	4.4%	5.1%	5.0%	5.0%

	2005e	2006e	2007e	2008e
PER	15.5	22.1	21.4	19.7
PCFR	43.2	31.0	28.7	55.0
Div. Yield	4.6%	4.2%	4.4%	4.6%
EV/Sales	17.66	16.89	17.19	27.27
EV/EBITDA	21.6	20.3	20.5	32.3

PUBLISHED 09 FEBRUARY 2006

INVESTMENT RESEARCH

Contents

1 SWOT profile

Strengths

- Deutsche Euroshop (DES) is a pure player in the real estate segment with a clear focus on well managed shopping centres.
- Over the past years a first-class portfolio of shopping centres has been acquired and the diversification in terms of locations and tenant and industry mix gives rise to expectations of solid earnings growth also in the coming years.
- For management the long-term realisation of high surplus funds is a priority besides a continuous and quality oriented investment strategy. These form the basis for a continuous and attractive dividend policy.
- The lean management structures of the DES Holding allow quick decisions and result in low costs. The centres are predominantly managed by the very experienced ECE.

Weaknesses:

- Further investments can only be financed by outside capital, sale of investment properties and capital increases, as the positive operating cash flow is fully distributed as dividends to shareholders.
- The sales and earnings performance of DES is strongly dependent on the particular management of a centre.
- Should the consumer environment in Germany remain weak, negative effects on the investment income of DES cannot be ruled out.

Opportunities:

- DES virtually fulfils the criteria for a REIT already today. The company could be transformed into the new corporate form without restructuring if the overall conditions are created in Germany.
- The real estate prices in Germany are favourable by international comparison and have growth potential. This would have a positive effect on net asset value and thus the share price potential.
- An economic upturn in Germany and Europe should also further improve the consumer climate. The shopping centres of DES could benefit from this more than the average.
- The rental agreements with retailers in the shopping centres have a dynamic format. Higher sales lead to higher rents. Furthermore, rent levels are linked to inflation rates and fixed on the downside. This means a favourable risk/reward profile in terms of the future sales of DES.
- DES and ECE are particularly well positioned in the German market for shopping centres so this should mean further interesting investment options in future.

Threats:

- A significant reduction in rent levels for retail properties or the insolvency of important tenants would have a negative impact on the sales and earnings of DES.
- DES AG currently only consists of the two board members and five employees. This means a certain human resources based risk. As the operating business is managed by the companies invested in, however, we believe this risk is limited.
- Negative effects from changing shopping habits of consumers and a move away from the shopping centres cannot be ruled out even if this is unlikely in our view.

2 Investment recommendation

With this report we start our coverage of the Deutsche Euroshop stock (DES) in our research spectrum. The first recommendation for the stock is "buy", with a price target of € 57. The DES stock is currently valued at around the level of its European peer group, but we grant it a premium in view of its clear and so far very successful strategy. The price target is calculated on the basis of a dividend discount model and a peer group comparison. The DES stock is listed in the DAX and is a member of the EPRA Index and currently has a market capitalisation of € 868 m. The free float is 81%. The key investment arguments are:

- Deutsche Euroshop (DES) pursues a clear and transparent business strategy. It invests solely in well managed shopping centres (focus on Germany) which show solid sales growth despite several years' of consumer sluggishness. Around € 1.4 bn has been invested in 16 centres since 2000. In the past years, the enterprise value has continued to increase through this investment policy.
- DES's concept is a dividend payout model, which allows tax-free payout of its excess liquidity in the form of dividends. The objective is a tax-free return of at least 5% on the capital employed.
- The current property portfolio provides a good basis for further earnings improvements. 99% of the investment properties are rented, the tenant and sector mix in the shopping centres is well diversified. The rental level is also fixed on the downside and rents are linked upwards to the inflation rate and rising sales.
- The centre management is the responsibility of experienced external service providers. In Germany, this is predominantly the market leader in centre management, namely ECE.
- Since 2003 DES has published the NAV of the stock. The basis of the NAV is the current market values of the shopping centres, calculated each year by external experts in accordance with international standards.
- The DES stock is a net asset value stock, whose attraction lies primarily in its stable dividend yields (2006e: 4.2%). The intrinsic value is measurable by the NAV, which was € 45.70 per share at the end of 2005. At the end of 2006 we believe it will be € 46.30, as we expect a positive valuation difference again.

3 Valuation

In our valuation of DES we use two different methods: Firstly, we compare the valuation level with other companies using selected ratios. Furthermore, we calculate a fair value from a discount model based on the expected dividends.

3.1 Peer Group Comparison

In the peer group comparison (*see Fig. 1 and 18 in the Appendix)* we have compared DES to the European companies that are most comparable in our view. These are property companies with a similar business structure from our standpoint.

PE, EV/EBITDA and price/NAV in line with competitors

The PE of 22.1 (2006e) and 21.4 (2007e) for DES is slightly above the level of its peer group of 21.8 (2006e) and 18.7 (2007e), as is the case with EV/EBITA. In our comparison we use consensus data from JCF Quant for the peer group, while the DES figures are based on our own estimates. The price/NAV ratio is roughly in line with the peer group. Like the industry, the DES stock is currently listed at a 10% premium on the NAV, which can also be justified in our view due to the expected further positive performance of the holdings. A look at the expected dividend yields also shows that DES at 4.2% (2006e) is slightly under the average for the peer group. It is also noticeable, however, that there is a relatively large spread between the peer group values. In the case of NAV, for example, significant premiums are being paid for some stocks, while others are being traded at a discount. In view of the very convincing strategy and transparency of DES, we regard the upper end of the valuation range as more justified for the company.

3.2 Discount model

Based on DES's special business model we believe a dividend discount model is more useful for a valuation of the long-term prospects than a discounted cash flow model. The reason for this is, firstly, the company's objective to paying stable dividends from its surplus funds. excess liquidity. Secondly, the operating cash flows are just about enough at present to pay the dividends. New investments in shopping centres will be largely financed through outside capital and fresh equity from capital increases. The free cash flow is therefore negative (and will remain so in the foreseeable future), especially as no regular write-downs can be made on the holdings under IFRS (regular impairment tests instead).

A discounting of the future expected dividends implies a fair value for the DES stock of € 56-57. We have assumed the following parameters:

- We use a two-phase model. For 2006-2008 we orientate ourselves by our detailed estimates. Accordingly, we assume a dividend of € 2.10 for 2006, rising to € 2.30 by 2008. We believe this rise is realistic because additional investment income will be generated by additional shopping centres in the coming years and existing centres should show a positive development.
- For the second phase from 2009 we assume an annual growth in dividends of 1%.
- We set the discounting rate at 5.5%. This rate is derived from the current capital structure as WACC, whereby we have assumed the yield on long-term government bonds (3.5%) as the risk-free interest and a risk premium of 2.0%.
- Based on the above assumptions, the fair enterprise value for DES is nearly € 1 bn or € 56.58 per share.

Fig. 1 : **Dividend discount model**

Year	Dividend in €	discounted in €
2002	1.92	
2003	1.92	
2004	1.92	
2005e	2.00	
2006e	2.10	1.99
2007e	2.20	1.98
2008e	2.30	1.96
Growth 2009 ff	1.0%	50.7
Total		**56.58**

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4 The company

4.1 History and shareholder structure

Deutsche Euroshop AG (DES), Hamburg; commenced its business activity in 2000, starting out from the shopping centre investments of DB Real Estate (Deutsche Bank), which were incorporated into DES at that time. The objective of the new company was to further expand the existing shopping centre portfolio. DES was allocated a capital of € 600 m, on which to achieve a return of at least 5%. The capital was invested relatively swiftly in various investments over the following five years. In 2000 the company was listed on the stock exchange and became more capital market orientated. The story of the company – a clear strategy concentrating on investments in profitable shopping centres and a transparent corporate communication – has been honoured by investors. We expect this course to be continued in future. The locations of the DES holdings are shown in Fig. 3. DES AG acts as a holding company with interests in the operating companies (partnerships). These in turn manage the shopping centres. The milestones of the company's history can be outlined as followed:

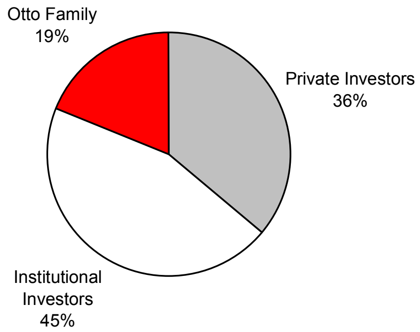
- September 2000: DES commences its business activities. A capital increase is made to € 20 m and funds of € 580 m are put into the capital reserve by the shareholder DB Real Estate. From these funds a shopping-centre investment portfolio of the DB Real Estate with properties in Germany and abroad is acquired.
- November 2001: The Hamburg entrepreneurial family Otto becomes major shareholder.
- July 2003: The DES stock is admitted to the SDAX.
- January 2004: Admission of the DES stock in the EPRA Index.
- September 2004: Admission to the German MDAX.
- November 2005: First successful capital increase by 1.5 million shares to continue the acquisition strategy.

Fig. 2 : **Peer-Group comparison**

Company	Price in € Feb. 08, 2006	Marktetcap. in € m	P/E 2006e	P/E 2007e	EV/EBITDA 2006e	EV/EBITDA 2007e	P/B 2006e	Dividend 2006e (€)	Div. yield 2006e	Price/NAV 2006e
Rodamco Europe	72.20	6,472	17.6	14.1	19.8	18.2	1.2	3.32	4.6%	1.16
Hammerson	15.43	4,394	35.8	30.8	25.5	25.5	1.0	0.30	1.9%	0.96
Klepierre	85.50	3,947	27.7	23.6	16.1	15.3	1.2	2.90	3.4%	1.16
Corio	49.87	3,354	15.4	11.2	19.5	18.2	1.2	2.55	5.1%	1.24
Eurocommercial Prop.	30.46	1,075	18.4	17.0	17.6	11.4	1.0	1.69	5.5%	1.03
Vastned Retail	57.10	965	15.8	15.6	16.5	16.1	1.1	3.62	6.3%	1.11
Average			**21.8**	**18.7**	**19.2**	**17.4**	**1.1**		**4.5%**	**1.1**
DES	**50.50**	**868**	**22.1**	**21.4**	**20.5**	**20.7**	**1.2**	**2.10**	**4.2%**	**1.1**

Source: Factset *M.M.Warburg Investment Research*

Fig. 4 : **Shareholder structure**



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The current shareholder structure is dominated by free float, which is currently nearly 81%. After the complete exit of Deutsche Bank to focus on its core business, members of the Hamburg entrepreneurial family Otto are the only major shareholders today with a 19% stake. We do not expect this holding to be sold because Deutsche Euroshop cooperates closely with ECE in centre management, which is owned by the Otto family. In regional terms, 86% of the shares are currently inland, 14% are held by foreign investors. In the course of the growing interest of foreign investors in the German property market (also with the possible introduction of REIT in Germany) we believe that the share of foreign investors could increase in future. In view of the company's solid assets and its value-oriented growth strategy we believe the company's positioning in the MDAX is secure.

4.2 Management

Many years of real estate experience

The CEO of DES AG since October 2001 has been Claus-Matthias Böge (47). Prior to this position at DES, Mr Böge worked for ECE Projektmanagement G.m.b.H. & Co. KG in Hamburg for a period of eight years and was responsible for conception, financing and current earnings optimisation of real estate investments. ECE is the European market leader in the development, realisation, leasing and long-term management of shopping centres. Besides graduating in business studies, he also has a banking apprenticeship.

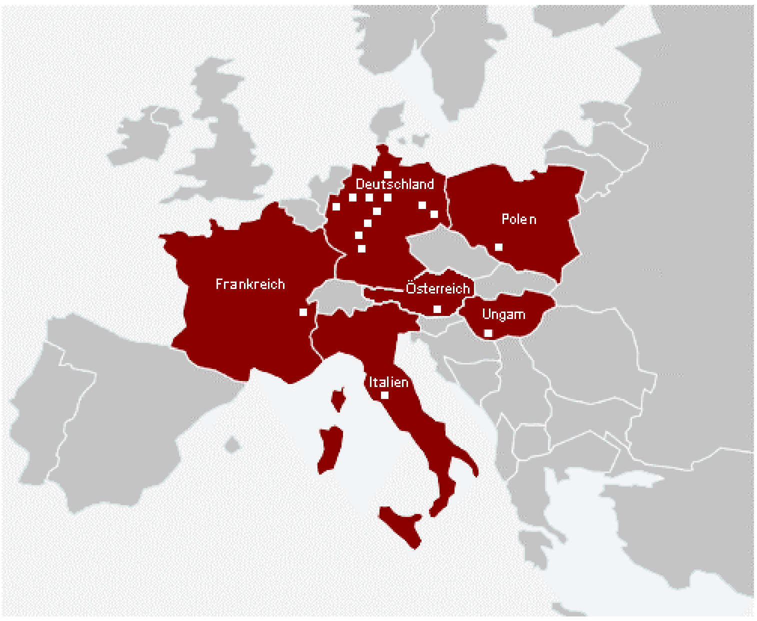
Olaf Borkers (41) has been on the DES board as CFO since October 2005. Before moving to DES Mr Borkers was a member of the board of TAG Tegernsee Immobilien und Beteiligungs-AG, where he was in charge of Finances and Investor Relations for six years up to September 2005. Mr Borkers also gained three years' real estate experience at RSE Grundbesitz und Beteiligungs AG, where he was assistant to the CEO. He is a graduate in business studies and also completed a banking apprenticeship with Deutsche Bank

4.3 Strategy

Focus on shopping centre investments

The DES portfolio consists solely of investments in well managed and profitable shopping centres. DES is the only German stock with which investors can really profit from

Fig. 3 : **Locations of DES shopping centres**



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the changing shopping trends especially among the German population (see also Chapter 5). DES is a pure financial investor and aims with its investments at achieving long-term stable cash flows, which are paid out directly to investors in the form of dividends. The actual operating business, especially active centre management, is handled by external service providers. In the case of the German shopping centres, this is the European market leader in the development and operation of shopping centres, namely ECE. The company's role as a purely financial investor also explains its very lean management structure. Besides the two board members, the company has only five other employees working in Investor Relations, Management and Administration. Besides the two board members, the company has only five other employees working in Investor Relations, Management and Administration. The relatively small workforce naturally implies a certain personnel risk, but this is modified by the fact that the operating business is run by the companies invested in.

Clear corporate targets

The DES management pursues clear corporate targets. This include:

- The long-term increase of the Net Asset Value (NAV). NAV represents the intrinsic value or the economic net worth of the company and is calculated from the market value of the investment properties minus the company's liabilities. The market values are calculated once a year by external experts based on earnings models.
- DES pursues a "Buy & Hold" strategy. Investments are long-term commitments aimed at constant cash flows. The surplus funds are the basis for the permanent payment of attractive dividends. Furthermore, this strategy avoids the payment of trade taxes because DES is classified as a property management holding. Sales from investments are made exclusively for portfolio optimisation purposes.
- The primary focus of investment is Germany. DES currently has interests in 16 shopping centres, 11 of which are in Germany. This German share is likely to grow in future, since the most attractive returns are seen here. In addition, Eastern Europe could offer potential, where some investments have already been made. The interests in France and Italy could be given up accordingly. Overall, the percentage of investments abroad should not exceed 25%.
- DES pursues a controlled growth strategy. Management is striving for an expansion of the portfolio by 10% p.a. This can take the form of an acquisition of a new shopping centre or by increasing investments. In the case of a shortage of investment funds DES also finances attractive new projects by means of capital increases. The group capital ratio should not fall below 45 %.

The current portfolio consists of 16 shopping centres

The current portfolio of DES consists of 16 shopping centres (see Chapter Fig. 5), 11 in Germany and 5 in other European countries. The present investment total is € 1.4 bn (nearly

Fig. 5 : **Portfolio details**

Domestic	Country	Rentable area in sqm	Sales area in sqm	Number of shops	Occupancy rate in %	Coverage Inhabitants (m)	FERI-Rating
Rathaus Center, Dessau	Germany	30,000	25,000	80	98	0.4	in 2006
Rhein-Neckar-Zentrum, Viernheim	Germany	64,000	60,000	100	100	1.4	A
Stadtgalerie, Hameln	Germany	25,500	20,000	90	50	0.4	in 2008
Allee-Center, Hamm	Germany	34,800	21,000	80	100	1.0	A
City-Galerie, Wolfsburg	Germany	30,000	20,000	90	100	0.6	A
City-Arkaden, Wuppertal	Germany	28,100	20,000	90	100	0.7	B+
Forum, Wetzlar	Germany	34,300	23,500	110	100	0.5	in 2005
Altmarkt-Galerie, Dresden	Germany	43,800	26,000	100	99	1.0	A
Phoenix-Center, Hamburg	Germany	39,000	26,500	110	96	0.6	in 2005
City-Point, Kassel	Germany	29,400	20,000	60	100	0.8	A
Main-Taunus-Zentrum, Sulzbach	Germany	102,000	79,000	100	100	2.2	A
Total domestic		**460,900**	**341,000**	**1,010**			
Foreign							
Centro Commerciale Tuscia, Viterbo	Italy	15,200	n.a.	40	100	0.3	A
Shopping Etrembieres, Annemasse	France	16,600	n.a.	50	100	0.8	A
Arkad, Pecs	Hungary	34,200	n.a.	130	100	0.5	A
City Arkaden, Klagenfurt	Austria	30,000	n.a.	120	100	0.4	in 2006
Galeria Dominikanska, Breslau	Poland	32,600	n.a.	100	100	1.0	A
Total foreign		**128,600**		**440**			

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€ 200 m abroad). The interests in the centres currently range from 43% to 99.8% (with the exception of the centre in Breslau (Poland), and are therefore consolidated (full or pro rata consolidation). As a result of an increase in the holding the Main-Taunus centre will be pro rata consolidated from 1 January 2006. Merely the interest in Breslau (33% stake) will be reported under financial assets accordingly in future statements. In general, DES management aims at majority holdings, but imposes restrictions upon itself as to the investment volume per property in order to avoid cluster risks and present a widely diversified portfolio. Ideal investment volumes per property are therefore between € 50 m and € 80 m per property, which means that 1-2 new holdings per year are possible. Human resources would not allow a higher investment frequency in any case.

After stock market flotation, the first task for DES was to invest the liquid funds of € 600 m. This target was met in 2003 with the holdings in the Phoenix Center in Hamburg, the Forum in Wetzlar and the Galeria Dominikanska in Breslau.

The next business phase consisted in developing and further optimising the portfolio. Management has two options for financing further shopping centres. It either has to create liquidity from its own assets by selling a holding. This option was chosen by the company in connection with the acquisition of a stake in Klagenfurt in 2004 (investment volume: € 72 m), when it sold its interest in the Italian Centro Commerciale Friuli in Udine for € 62 m to finance this. The holding in Italy was the least profitable of the group at that time. Even so, DES realised a book profit of € 4.8 m through this transaction.

If there is no suitable divestment property for creating liquidity, DES also has the possibility of procuring new funds through a capital increase. Management made use of this option at the end of 2005 when it placed 1.56 million new shares at an issuing price of € 43 per share. The gross issue proceeds of € 67.2 m are being used partly to finance the new holdings in the Rathaus Center in Dessau (investment volume: € 100 m) and the Stadtgalerie in Hameln (investment volume: € 80 m) and partly to increase the stakes in the Rhein-Neckar and Main-Taunus centres and in Annemasse (investment volume: € 20 m). It is important in this connection to note that capital increases are only made when definite interests have been purchased and are intended to replace bridging finance. DES Management aims at a capital ratio of at least 45% on the group balance sheet. Investors consequently never invest their money “blindly” but know precisely prior to the capital increase in which property the new funds are to be invested. As DES always demands a minimum return on the investments of 6% before investing in accordance with its strict investment criteria (no. 4.4) and the target dividend of 5% is therefore guaranteed, the capital increases do not result in dilution despite the higher number of shares.

DES’s acquisition strategy is solely driven by opportunity. Consequently, it is also quite conceivable that DES will make further shifts in its portfolio. The tendency in our view will be to strengthen the share of investments in Germany and reduce investments abroad. In general, we have the impression that the German shopping centres are easier to control than the foreign investments due to the close relationship to ECE.

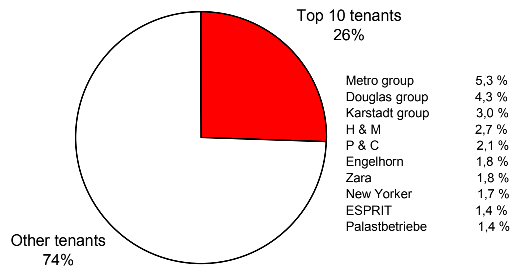
4.4 Success factors

Stringent investment criteria

The first key success factor of DES is, in our view, a profit-oriented investment strategy, which starts with the purchase of the property. Based on strict investment criteria properties are selected that management regards as attractive in terms of lasting value. When deciding on an investment property, DES applies the following criteria:

- DES invests solely in shopping centres.
- Properties are acquired either by direct or indirect equity investments.
- The minimum property size is 5,000 sq m, not more than 15 % of which may be for office or other non-retail purposes.
- Centres under development must have a pre-let rate of at least 50%, centres which are already in operation, at least 80%. Furthermore, for existing centres, at least 25% of the space must have a remaining term in the rental agreement of over five years.
- Purchase decisions are made carefully based on up-to-date, long-term oriented site appraisals, market analyses and extensive due diligence.
- Locations must have a sustainable catchment area of at least 100,000 inhabitants.
- The percentage of investments in Germany must not fall below 50% of the total investment volume in the long term.
- To guarantee sufficient liquidity, 25% of the available liquid funds, but at least € 1 m, must be invested in form of overnight or one-month money. The rentable area must be at least 10,000 sq m.

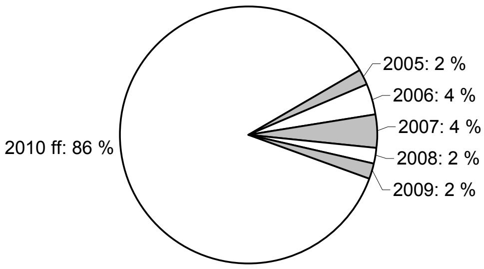
Fig. 6 : **Diversified tenant structure**



Source: DES *M.M.Warburg Investment Research*

All in all, an intensive examination of the so-called micro and macro criteria is made prior to investment. The site and the ground plan of the building are primary factors, which have to guarantee long-term rentability at an attractive level of rent for the company. The ground plan of the building is decisive because retailers' space requirements constantly change and these requirements have to be taken into account. Flexible space use is thus of decisive importance. The examination of the macro location mainly relates to the catchment area of the shopping centre, the regional purchasing power and the competitive environment. DES consults a large of number of external valuators and experts to examine the investment conditions.

Fig. 8 : **Duration of rental agreements**



Source: DES *M.M.Warburg Investment Research*

Diversified tenant and sector structure

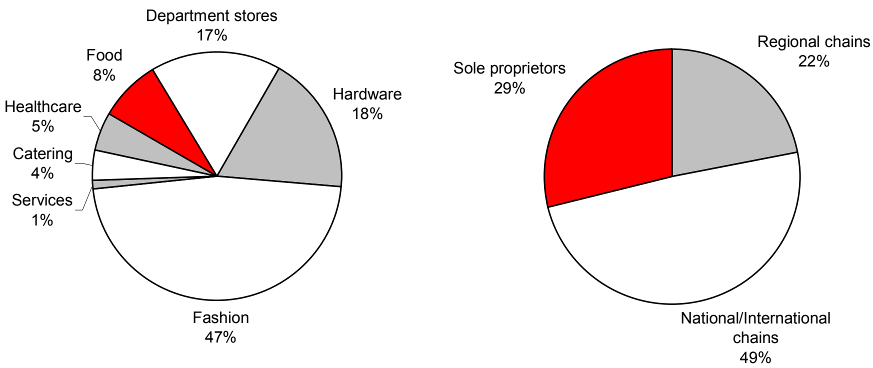
A particularly important factor for the long-term stability of the rental income is a well diversified tenant and sector structure in the shopping centres. We believe DES has an advantageous and balanced mix (see Fig. 6 + 7). The share of top 10 tenants in the total rental income is currently nearly 26%, the largest single tenant is the Metro group with a 5.3% share. Overall, around 29 % of the tenants are sole proprietors, while 22% are regional and 49% are national or international chains. The company generally aims at a strong anchorage of so-called "magnet tenants" in its centres (such as Media Markt or P&C), in order to make the shopping centre attractive for the widest possible range of shoppers, where the other retailers also profit. The scene is also well diversified in terms of sectors. The largest share is represented by clothing companies at 47% (see Fig. 7), which is advantageous in our view, as internet sales for clothing are relatively limited. The second largest share is hardware/electronics at 18%, followed by broad-range department stores at 17%. The remaining 19% is spread across the food, catering, health and services sectors.

Fig. 9 : **Most important tenants**

Source: DES *M.M.Warburg Investment Research*

We believe the structure of the rental agreements is also of decisive importance (see Fig. 8). According to the company, over 88% of its rental agreements are valid beyond 2011. Rental agreements generally have a 10-year term and cannot be terminated during this time. Furthermore, the rental agreements stipulate a basic rent with annual rent adjustments, which are linked to the rise in the cost of living. Consequently, the rental agreements offer at least one form of protection against inflation for the sales of DES.

Fig. 7 : **Diversified sector mix**



Source: DES *M.M.Warburg Investment Research*

Beyond the basic rent, the rents rise in line with tenants' sales so DES also has direct participation in the success of its tenants. Up to now, however, the share of sales induced rental income was only 2-3 % of DES group sales. In general, the tenant structure in the shopping centres is very stable. The company puts the fluctuation rate at currently 3-4% of the shops p.a.

Rents in the investment properties of DES are presently an average of € 20-25 per sq m, although the spread is relatively wide depending on the sector. The sales generated by tenants average around € 4,300 per sq m, which gives a rent/sales ratio of 6.5-8.5%. The rent therefore seems quite acceptable to retailers.

Centre management is predominantly through ECE

Besides the favourable purchase of equity interests, the centre management plays the decisive role in long-term profitability. Already in the planning phase, the centre management company contributes to the long-term success of the DES investments with its competence and experience by optimising the tenant structure and sector mix. In the later operating phase, the centre management is responsible for the maintenance and upkeep of the property and controlling the sustainability of rent payments. This includes close cooperation with tenants and strict monitoring of sales performance. If a negative trend is apparent, which could affect rent payments in the longer term, concepts are developed with the tenants to counteract this. If a tenant has to leave, the centre management ensures that a subsequent tenant is quickly found for the sales area to guarantee the high occupancy rate of 99%.

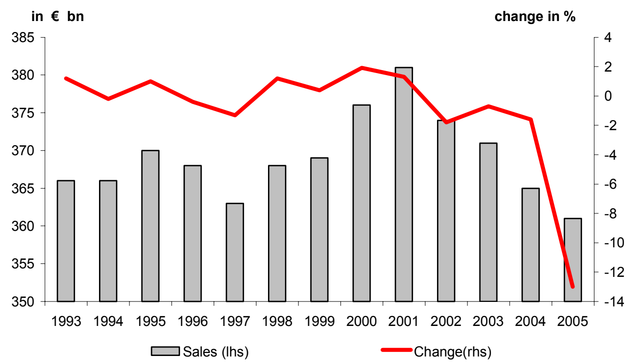
For 12 of the present 14 shopping centres (Stadtgalerie in Hameln and Cityarkaden in Klagenfurt are currently being built), ECE Projektmanagement GmbH und Co. KG is responsible for the centre management while the other two centres are managed by Espansione Commerciale and Unibail. ECE has designed, implemented, leased and managed shopping centres since 1965. With 83 city-centre and district shopping centres under its management, the company is the market leader in Europe. ECE belongs to an investor group around the Hamburg entrepreneurial family Otto. In view of the increasing concentration on ECE as its partner in centre management, DES is clearly dependent on ECE to a certain extent. On the other hand, this is a very strong partner and a major guarantee factor to the lasting business success. ECE is an excellent partner with respect to attractive new acquisitions, especially as the regional focus of the two partners is the same. DES pays 8% of its rental income to ECE for its centre management under a non-gratuitous contract for services, whereby ECE also has a direct participation in the success of the centre management. The success of ECE is shown by a comparison of the sales performance of retail overall with the sales development of ECE tenants over the past ten years (see Fig. 11, p. 11).

5 The market

5.1 Weak consumer climate

The continued weak consumption in Germany has been depressing the performance of the German retail trade for several years. In Fig. 10 we show the sales performance of the past 12 years (source: HDE), where retail sales at € 361 m in 2005 were at its lowest level since 1993. With the exception of 2000 and 2001, we see a continued stagnation of sales. Particularly the years from 2002 to 2005 are weak, when accumulated retail sales slumped by around 5%. A main reason for the permanent sales decline over the past years besides the quantity component is, without doubt, the price trend, as the price levels for goods of the traditional retail segment are under continued pressure. In the textiles business, for example, prices declined by about 1% p.a. in 2003 and 2004 (the figure for 2005 is not yet available). At the same time, the general cost of living rose by 1.1% in 2003 and 1.6% in 2004. The increases are mainly driven by rises in energy and rental costs, however. Whether the propensity to consume in Germany will recover longer term in the coming years essentially depends, in our opinion, on the general economic trend, for the high propensity to save and the resulting weak private consumption is strongly connected with the prevailing uncertainty of the German employment market. According to analyses by the Gesellschaft für Konsumforschung (GfK) the Germans set high hopes on the general economic trend at the start of 2006. Their inclination to make major purchases increased significantly again in December and sales levels picked up again for the first time in four years. On the other hand, consumers are still rather cautious about their future personal income levels.

Fig. 10 : **Declining retail sales**

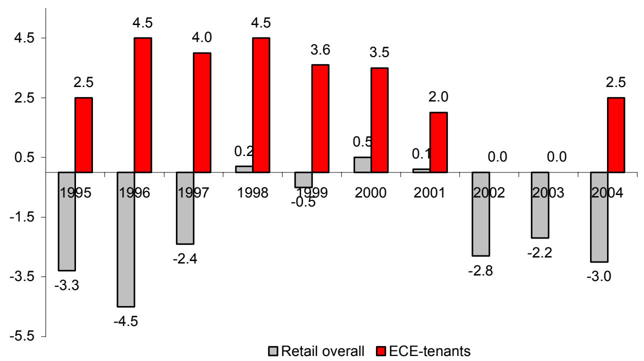


Source: HDE *M.M.Warburg Investment Research*

5.2 Shopping centres with their own special trend

Contrary to the general trend in German retail the situation with shopping centres is much more positive. In our view this is a logical development, as the shopping centre concept has decisive advantages over traditional retail structures. Shopping centres are specifically planned and optimised shopping, services and business centres under one management. Here, the customer finds a wide (and often spatially coordinated) product range, close parking or other transport infrastructure, and consistent opening times. In addition, a positive shopping atmosphere is created by the secure and clean environment offered by the centres.

Fig. 11 : **ECE Shopping-centres with special business**

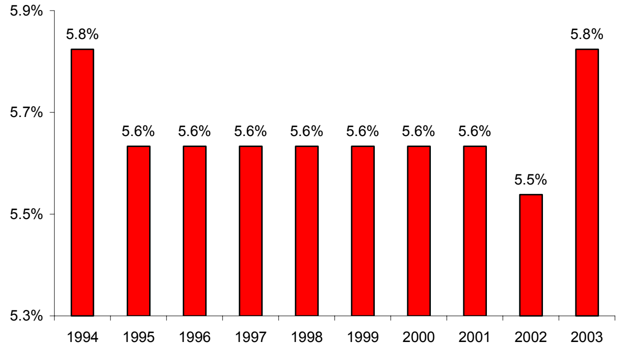


Source: ECE *M.M.Warburg Investment Research*

It is against this background that the number of shopping centres in Germany has significantly growth over the past years. The term shopping centre has no concrete definition, but it can be assumed that there are meanwhile around 370 centres in Germany with an average sales area of 30,000 sqm.

The question is whether this trend will continue in the coming years. There are good reasons to believe so in our opinion. Firstly, we see no reason at present why the trend in favour of shopping centres should break. We think the concept has clear advantages over traditional retail structures. As the consumer climate brightens, shopping centres should draw above-average benefit accordingly. A concentration on city-centre shopping centres is conceivable in our view, however, as this, in combination with pedestrian zones and the like, opens up further shopping and leisure opportunities. The experience with city-centre shopping centres also shows that they do not necessarily threaten the existence of neighbouring stores, who may even benefit in the long-term from the magnetic effect of the centres. Furthermore, a general demographic trend towards city centres can be observed in Germany, especially among younger and moneyed population groups. We do not regard the mail order business as a major threat to shopping

Fig. 12 : **Mailorders: stable market share**



Source: Federal Statistical Office
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centres. According to analyses by the German Federal Statistical Office and the Federal Association of German Mail Order Companies, sales of mail order businesses have been relatively stable at 5.6% of total German retail sales over the past years. We do not expect this to change significantly in the future.

5.3 High-return investments in shopping centres

The decoupling of the shopping centres from the weak sales performance in the retail sector is also having an effect on the value of the properties. While office buildings in particular in Germany show a high vacancy rates and declining rent levels, the situation with well managed retail properties is much better. According to analyses by Deutsche Immobilien Datenbank GmbH, retail properties had above-average total returns (4.2% compared to 3.9% for all property types) and net cash flow returns (5.7% compared to 5.1%) from 2000 to 2004. While the total return at –1.4% is roughly in line with the average for all property types, the sustained level of gross earnings, especially in a nine-year comparison – was better than in the entire real estate segment. We estimate that this trend will continue, although a differentiated trend will also be visible across retail property segments. We expect above-average value growth for specialist stores and properties in good locations in particular, while secondary locations or properties with high vacancy rates will have to accept value depreciations.

Fig. 13 : **Attractive retail properties**

	3 years	5 years	9 years
Total Return %			
Retail	3.9	4.2	4.7
Office	2.6	3.9	4.0
Residential	3.2	4.0	3.6
Mixed	2.0	3.1	3.3
Other	3.3	4.1	4.4
Average property	2.8	3.9	4.1
Cashflow-yield (net) %			
Retail	5.6	5.7	6.0
Office	5.1	5.2	5.2
Residential	4.3	4.3	4.6
Mixed	4.2	4.4	4.6
Other	5.2	5.3	5.3
Average property	5.0	5.1	5.2
Yield total value %			
Retail	-1.6	-1.4	-1.1
Office	-2.3	-1.2	-1.1
Residential	-1.1	-0.3	-1.0
Mixed	-2.1	-1.3	-1.2
Other	-1.8	-1.2	-0.8
Average property	-2.1	-1.1	-1.1
Change of gross revenue %			
Retail	-0.4	-0.2	0.2
Office	-0.9	-0.2	-0.2
Residential	0.8	1.0	0.0
Mixed	-0.7	-0.2	-0.4
Other	-0.2	0.3	0.3
Average property	-0.6	0.0	-0.1

Source: DID *M.M.Warburg Investment Research*

6 Financial discussion

6.1 Operating performance

9-10% internal growth p.a.

In the past three years DES has increased its sales by an average 9.5%. The sales of DES consist of the rent income from the investment properties. Expansion is being driven by the solid growth from the existing shopping centres, resulting from the rises in rents. The rent level is linked to the inflation rate on the one hand but also increases with retailers' growing sales in the shopping centres on the other. Consequently, the organic growth rate in the past two years was 1.5-2.0%, the sales induced rent share was 2.6% in 2004 (around € 1.6 m compared to € 1 m in 2003). This share is likely to have increased again slightly in 2005. Besides the organic sales growth, the rent income from new holdings continually contributes to the sales growth of DES. If we assume an annual investment for new holdings of € 150 m for the coming years and a long-term return of 6-7% on the invested funds, this gives an annual sales growth of around € 9-10 m for the coming years.

On the sales side there will be a special effect in 2006, which will boost sales significantly. Due to the increase of shares in the Main-Taunus-Zentrum (MTZ) from previously 37.4% to 43.1% and the resulting pro rate consolidation of this holding, we estimate additional sales of around € 8-9 m. The MTZ has been reported as a financial investment so far; consequently the investment income under this item will disappear from 2006. Furthermore, the interests were also increased in the Rhein-Neckar-Zentrum (from 92.8% to 99.8%) and in the shopping centre in Annemasse in France (from 92.8% to 99.8%). There will also be sales for the first time from the newly opened shopping centres in Dessau (€ 7.7 m) and Klagenfurt (opening in spring 2006, rent income for nine months: € 3.8 m). Against this background DES group sales should grow by 25% to over € 90 m in the current year 2006. For 2007 and 2008 we expect further increases in sales, which should be in the region of 1.5-2.0% from organic rent growth, in addition to the sales growth from acquisitions. It is already foreseeable that the new acquisition of the Stadtgalerie in Hameln will contribute around € 6 m to group sales with rent income from 2008. Furthermore, the increase in VAT planned by the German federal government will have a twofold effect on DES rent income: Firstly, there should be a notable inflationary push in 2007, driving price indexed rents upwards. Secondly, retailers' sales could increase due to the rising prices, which would have a positive effect on the sales indexed rents. Furthermore, consumers are expected to bring forward purchases of goods in 2006 in order to avoid the rise in VAT from 2007. This likewise implies (one-off) sales growth in 2006.

6.2 Profits before and after taxes

Financial income will be more negative in future

DES's financial income is marked by three different factors:

1. Interest income: As the investments are partly financed by outside capital to achieve an optimum capital structure, DES has a considerable interest expense. This was € 25.3 m in 2004. Long-term financial debt was nearly € 600 m. The average effective interest rate for the long-term debt was relatively high at the end of 2004 at 5.66%. Management sees potential for improvement here. Replacement of these liabilities, for example, by shorter-term liabilities and the use of alternative financing instruments (participation certificates, commercial papers) could reduce the interest burden. Against this background, we expect a lower increase in interest expenses in the coming years (in relation to the growing debt capital). In the medium term, the average interest rates should be below 5%.

2. Income from participations: Until the end of 2005 the holdings in the Main-Taunus-Zentrum and in the Galeria Dominikanska, Breslau, were reported as financial assets. Excess liquidity was entered as investment income accordingly. Due to the increase in the stake in the Main-Taunus-Zentrum from 37.4% to currently 43.1%, this will be allocated to fixed assets in future and rent income will thus be entered as sales rather than investment income as before. Consequently, the only financial investment will be the Galeria Dominikanska in Breslau in future. The income from financial investments should therefore only be € 1 m in 2006 (2005e: € 5 m).

3. Valuation result: As DES reports in accordance with IFRS, the holdings in the shopping centres are evaluated once a year by external experts. The valuation processes are based on discounted cash flow methods. The expected rental income on the one hand and the underlying discount factor on the other play the decisive role here. While the rent income based on the existing rental agreements is relatively stable and predictable, to determine the adequate discount factor is very complicated. To establish the discount factor up to 150 different variables (derived from micro and macro-factors) are applied, with the objective of correctly assessing the risk of investment. As the rent income is indexed and therefore rises at least with the general costs of living, this means (other things being equal) a permanent positive valuation result. However, if the discount factor rises, due to a strongly rising interest level or deterioration in the macro-environment of the shopping centres (high regional unemployment etc.), this can overcompensate the positive effect of the rising rent income and result in negative valuation adjustments. As we are not able to anticipate possible changes in the discount factor due to the complexity of determining this, we have assumed an annual positive valuation result of 1% of the invested capital for the future earnings scenario. As the future inflation rate is more likely to be 1.5-2% p.a., this gives a certain buffer from a possible increase in the discount rate resulting from rising interest rates .

All in all, we expect a financial income for DES in 2005 of € 7.2 m, due to positive valuation adjustments amounting to € 30 m (e.g. first valuation of the Phoenix centre in Hamburg and the Forum in Wetzlar), but we expect € –15 m in 2006 due to the transfer of the holding in MTZ on the balance sheet and a lower valuation result. In the medium term, however, there will be significant potential for improvement here from the optimisation of the financing structures.

Fig. 14 : **Details on DES shopping centres**

Domestic	Cty	Con-sol. *	Share in %	Investment-vol. in € m	Year of purchase	Date of opening	Sales (€ m) 2003	2004	2005e	2006e	2007e	2008e	CAGR %
Rathaus Center, Dessau	G	F	94.9	100	2006	2006	0.0	0.0	0.0	7.7	7.8	8.0	1.9%
Rhein-Neckar-Zentrum, Viernheim	G	F	99.8	274	2000	1972/2003	14.8	15.7	16.1	17.5	18.3	19.0	5.1%
Stadtgalerie, Hameln	G	F	95.0	82	2008	2006	0.0	0.0	0.0	0.0	0.0	6.0	n.m.
Allee-Center, Hamm	G	F	87.7	96	2002	1992/2003	8.8	8.9	9.1	9.3	9.6	10.0	2.6%
City-Galerie, Wolfsburg	G	F	89.0	108	2000	2001	7.7	7.7	7.9	8.1	8.3	8.6	2.2%
City-Arkaden, Wuppertal	G	F	72.0	96	2000	2001/2004	7.7	7.4	7.5	7.6	7.8	8.1	1.0%
Forum, Wetzlar	G	F	65.0	72	2003	2005	0.0	0.0	4.5	5.0	5.1	5.3	5.5%
Altmarkt-Galerie, Dresden	G	F	50.0	96	2000	2002	5.7	6.1	6.2	6.4	6.6	6.8	3.6%
Phoenix-Center, Hamburg	G	P	50.0	80	2003	2004	0.0	1.6	4.9	5.0	5.2	5.4	3.3%
City-Point, Kassel	G	P	40.0	48	2000	2002	2.9	2.9	2.9	3.0	3.1	3.2	2.0%
Main-Taunus-Zentrum, Sulzbach	G	P	43.1	140	2000	1964/2004	18.0	19.0	20.0	20.5	21.0	21.5	3.6%
Total domestic				**1,192**			**65.6**	**69.3**	**79.1**	**90.1**	**92.8**	**101.9**	**9.2%**
Foreign													
Centro Commerciale Tuscia, Viterbo	I	F	100	24	2001	1998/2001	2.6	2.7	3.1	3.2	3.3	3.4	5.5%
Centro Commerciale Friuli , Udine	I	F	0				4.4	2.5	0.0	0.0	0.0	0.0	n.m.
Shopping Etrembieres, Annemasse	F	F	99.8	39	2000	1994	3.3	3.5	3.8	4.0	4.2	4.4	5.9%
Arkad, Pecs	H	P	50	36	2002	2004	0.0	2.6	3.3	3.5	3.8	4.0	6.6%
City Arkaden, Klagenfurt	A	P	50	72	2004	2006	0.0	0.0	0.0	3.8	5.1	5.2	17.0%
Galeria Dominikanska, Breslau	P	P	33.3	24	2003	2001	0.0	0.0	3.3	3.5	3.8	4.0	6.9%
Total foreign				**195**			**10.3**	**11.3**	**13.5**	**18.0**	**20.2**	**21.0**	**15.3%**

** F=full consolidation, P=proportional consolidation*

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Fig. 15 : **Development of EBT and net profit**

in T €	2004	2005e	2006e	2007e	2008e
EBIT	50,678	58,829	75,209	78,782	84,140
Margin (%)	*82.5*	*81.9*	*83.0*	*83.6*	*84.5*
+ Interest income	-25,312	-28,644	-30,200	-31,000	-31,400
+ Inc. from participations	4,799	4,923	1,000	1,043	1,087
+ Valuation differences	8,018	30,873	14,030	13,030	13,030
= EBT	38,183	65,981	60,039	61,855	66,857
- Taxes	-11,756	-19,110	-18,012	-18,556	-20,057
- Minorities	1,309	-2,333	-2,753	-2,771	-2,753
= Net profit	27,736	44,538	39,274	40,527	44,047
EPS (€)	**1.78**	**2.82**	**2.29**	**2.36**	**2.56**

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Tax rate could decrease significantly under transformation into a REIT

DES's reported tax rate is around 30%; the absolute tax burden was € 11.8 m in 2004. € 8.1 m was passive deferred taxes, however. As the investment companies in operation report under HGB standards and therefore have regular write-downs on the property portfolio, the deferred taxes have to be accrued accordingly in the IFRS accounts of DES Holding. The actual tax expense was € 2.7 m in 2004 as income taxes and nearly € 1 m as other taxes (mainly real property tax for the investment properties). DES does not have to pay trade tax as the company is classified as a property management holding and is thus not liable for trade tax.

For the coming years we have likewise assumed a tax rate of 30%. However, should REITs be introduced in Germany and DES become a REIT, the majority of the deferred tax expense would most likely not be accumulated with a positive effect on EPS.

In the case of operating income (EBIT) for DES we expect a rise of about 25% to € 75.2 m for 2006, resulting mainly from the aforesaid transfers of holdings and the new acquisitions. We estimate that group income after taxes and minorities at € 39.3 m could be lower than in 2005, however, because financial income will be much lower, as outlined above. As we initially do not expect any further capital increases with a higher number of shares accordingly, EPS should likewise be € 2.29 in 2006 in order to then rise to € 2.36 in 2007.

6.3 Cash flow and Investments

Stable investment ratio

With regard to investments DES pursues a fundamental "Buy & Hold" strategy. Disposals are made only in a few cases for portfolio optimisation purposes. This strategy also has tax advantages, as it means that the DES is classified as a property management holding and is therefore exempt from trade tax liability. According to management planning, DES also aims at growth in future through the acquisition of further holdings in shopping centres. It has an investment volume target of around € 150 m p.a. However, management emphasises that the investment strategy is strongly driven by opportunity and it only invests in properties that promise a lasting return of 6-7%. Furthermore, it prefers investment projects with a volume of € 150 m in order to avoid cluster risks in the portfolio structure. In general, DES acquires majority holdings in the investment properties and aims at sole ownership for tax optimisation reasons. For larger investment plans, the lower limit for the holding is 50%. Consequently, we expect future investments to be effected solely as tangible fixed assets.

Investments are partly financed by borrowing, while DES also aims at a group capital ratio of at least 45%. Consequently, for this investment policy, if the target balance sheet ratios are not reached, it is necessary to either sell interests (this was the case with the shopping centre in Udine) or alternatively use the capital market in the form of capital increases (like in November 2005). Generally speaking, DES only raises fresh capital when specific projects need financing. A "war chest" is not kept as the available funds would have to be invested in the money and capital market at low interest rates and would dilute the results. Any bridging finance required is provided by banks.

Investments are made either in new holdings or partly to increase existing holdings. At the end of 2005, for example, the holding in the Rhein-Neckar-Zentrum was increased from 92.8% to 99.8%. The strategy of non-sole-ownership acquisition serves tax optimisation purposes.

Scope for higher dividends

The operating cash flow is largely used for paying dividends. As DES is based on the concept of a dividend payment model, a dividend of € 30 m was already paid out in past years (5% of the capital provided by shareholders). In view of the fact that the original € 600 m was only invested last year and therefore generated the planned earnings, dividend payments in the first few years of business activity were also at the cost of the capital reserve (operating cash flow for the group in 2004: € 21.7 m). This is not at all critical, however, as the free cash flow of the holdings already in operation is the decisive factor for DES in the dividend payments. This free cash flow was € 30.7 m in 2004 (compared to € 28.0 m the year before), so the full dividend of € 30 m could be paid from this for the first time in the company's history. Since 2001 the relevant free cash flow has continually risen from € 18.1 m to € 30.7 m in 2004. The figure for 2005 is not yet known but we expect a further increase to around € 33 m.

In view of this growth, the dividends should also continue to increase in future years. DES has an important feature with regards to dividends in that they are distributed to shareholders as tax-free payments. This is based on the income tax law, which stipulates that shareholders resident in Germany are not liable for income and cooperation tax provided the dividend payment is classified as an equity repayment. This is the case for DES and will also apply in the coming years, theoretically, until the total dividends exceed the capital reserve. However, as these reserve will continue to grow through capital increases as a result of the expansion strategy, the tax-free dividend payments will still be possible for a number of years.

6.4 Balance sheet structure

Liabilities

The capital ratio (without the equity of external shareholders) of the DES group was 46.4% in 2004 and fell to 45.2% at the end of September 2005. At the end of 2005, however, the capital share was likely to have been around 50%. This was attributable to the successful capital increase (gross issue proceeds: € 67 m) and the annual net income for the group of € 44.5 m (based on our estimate including a positive valuation adjustment of € 30 m). As already said above, the capital ratio should be at least 45% in the long term. Fluctuations are possible, however, depending on the timing of the investment process.

In September 2005 the DES group had a net debt of € 502 m (due to banks ./. securities and liquid funds). While the short-term and long-term debts totalled € 632 m (secured by the properties), the company had a liquidity of € 130 m. The average interest charge on the long-term due to banks was 5.66% in 2004, whereby 91% of the liabilities have a term of over five years. We expect the average terms to shorten in future, with more favourable financing rates accordingly.

Fig. 16 : **Balance sheet structure**

in € m	2004	2005e	2006e	2007e	2008e
Assets					
Fixed Assets	1,101.6	1,380.0	1,455.6	1,555.6	1,668.7
Financial Assets	101.7	102.0	112.0	112.0	112.0
Receivables	2.0	1.8	2.3	2.4	2.5
Other receivables	14.7	15.7	16.0	16.0	16.0
Cash	150.2	130.7	63.4	74.2	68.8
Other assets	0.0	0.0	0.0	0.0	0.0
Total	1,370.2	1,630.2	1,649.3	1,760.2	1,868.0
Liabilities					
Equity	684.4	754.2	785.9	810.4	816.6
Provisions	18.2	5.0	6.0	7.0	8.0
Financial debt	597.7	698.7	778.7	878.7	978.7
Trade accounts payable	3.7	2.0	2.5	2.6	2.8
Other debt	14.6	8.9	11.2	11.5	11.9
Deferred taxes	51.6	60.0	65.0	50.0	50.0
Total	1,370.2	1,528.8	1,649.3	1,760.2	1,868.0

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Assets

The assets of the DES group balance sheet are shaped by the investments in the present 16 shopping centres. At the end of September, fixed assets at € 1.25 bn accounted for nearly 90% of the balance sheet total. This ratio will barely shift in future, because new investments will be reported under this item. Current assets totalled € 146 m at the end of September 2005, with € 130 m as liquid funds for further investment purposes. There is no goodwill on the balance sheet.

6.5 Net Asset Value

An important factor for the future value of a property company is the Net Asset Value (NAV), which can also be interpreted as the intrinsic value. The basis for determining the NAV is the market values of the properties calculated annually by external experts. Current assets are then added, liabilities and minority interests deducted. We believe it also makes sense to deduct the deferred taxes in order to calculate the so-called Net Net Asset Value (NNAV).

DES published a NAV for the first time in 2004, and the NAV was also calculated retroactively for the end of 2003. The NAV per share at the end of 2003 was € 43.68 and rose to € 43.96 by the end of 2004. According to the preliminary figures, the NAV at the end of 2005 was € 45.70 and therefore 4% higher than the year before. The main reason for the growth in 2004 was the inclusion of the Phoenix centre in Hamburg and the Forum in Wetzlar. Both shopping centres were included in the NAV valuation for the first time in 2005 and were previously reported at the acquisition/production costs. For the coming years we expect a further rise in the NAV per share, firstly because of the inclusion of the shopping centres in Dessau and Hameln in the NAV calculation, which can be expected in 2006 (Dessau) and 2008 (Hameln), and, secondly, because the indexed rents should lead to a continual rise in NAV by 1-2% p.a.

For 2006 we therefore expect a NAV per share of € 46.30, which could rise to € 47.20 per share by 2008 (excluding any further acquisitions).

Fig. 17 : **Net Asset Value**

in € m	2004	2005e	2006e	2007e	2008e
Fixed assets	1,203	1,381	1,568	1,668	1,781
Current assets	167	148	82	93	87
Total assets	1,370	1,529	1,649	1,760	1,868
Long-term debt	598	699	779	879	979
Short-term debt	37	16	20	21	23
Net assets	736	814	851	860	867
Minorities (equity)	49	55	55	55	55
Net Asset Value DES	687	759	796	805	812
NAV per share (in €)	**44.0**	**45.7**	**46.3**	**46.9**	**47.2**
Deferred taxes	52	60	65	50	50
Net Net Asset Value	635	699	731	755	762
NNAV per share (in €)	**40.7**	**44.3**	**42.5**	**44.0**	**44.3**

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7 Special topic of REITs in Germany

Introduction in 2007 is uncertain

The possible establishment of a new asset class, the REIT (Real Estate Investment Trust), is currently the subject of intensive discussion in Germany. In principle, these are entrepreneurial property companies which are exempt from corporation and trade tax at company level provided their earnings are predominantly distributed to their shareholders and other conditions are fulfilled. REITs are a combination of property funds and listed property stock companies. The comparatively high dividends are liable to tax payments by shareholders – as is normal with open property funds. REITs usually have the legal form of a stock corporation. The products are basically suitable for private investors for long-term capital formation and for institutional investors as a further medium for the investment portfolio and diversification. REITs have already existed in the USA for 40 years and have become the standard indirect property investment. More and more countries worldwide are creating the legal and taxation conditions for setting up this class of asset. In Europe, REITs are allowed, for example, in Belgium, the Netherlands, France, Luxembourg, Spain and Italy, although the general legal and taxation conditions are extremely inhomogeneous. The introduction of REITs in the United Kingdom is also planned for 2006.

Relatively wide political consensus has been reached in Germany on the swift introduction of REITs. When the grand coalition was formed after the federal elections in September 2005, hopes were set on a start of the new asset class as of 1 January 2007. Its introduction is subject to several taxation problems being solved beforehand, however. These lie mainly in the fact that foreign investors can collect gains entirely tax free, based on double taxation agreements, as the company is already exempt from taxation liability. Furthermore, increasing criticism has been heard from SPD circles in the past weeks, as they expect rents to rise, especially for residential properties, once REITs are introduced and therefore signal their rejection of the plan. From our perspective, the introduction of REITs in Germany is inevitable in the medium term and we believe the taxation problems can be solved.

Possible effects for DES

DES is virtually a REIT today. The company meets the usual international criteria – in particular with regard to the focus on long-term property investments and a high rate of dividend payouts to shareholders. Furthermore, the dividend is already tax-free today (see 6.3). Consequently, DES could easily become a REIT if the overall conditions for REITs were attractive. Two factors would change, however:

- EPS would rise dramatically, as the company would no longer need to accrue deferred taxes due to the tax exemption. In 2004 deferred taxes totalled € 8.1 m or € 0.52 per share.
- Shareholders currently profit from the tax-free dividends. If REITs were introduced, the “half-income procdcure” would probably be abolished for the dividend payments of the REITs, however, so dividends would have to be fully taxed at the shareholder’s personal income tax rate.

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		2003	2004	2005e	2006e	2007e	2008e
Income statement (in € m)							
Sales		57.9	61.4	71.8	90.6	94.2	99.6
Cost of goods		---	---	---	---	---	---
Gross profit		57.9	61.4	71.8	90.6	94.2	99.6
SG&A expenses		-0.8	-0.8	-0.8	-0.9	-0.9	-0.9
R&D expenses		---	---	---	---	---	---
Other oper. income/expenses		-16.6	-9.9	-12.2	-14.5	-14.5	-14.5
EBITDA		40.5	50.7	58.8	75.2	78.8	84.2
Amortization		0.0	0.0	0.0	0.0	0.0	0.0
Depreciation		0.0	0.0	0.0	0.0	0.0	0.0
EBIT		40.5	50.7	58.8	75.2	78.8	84.1
Financial income		-12.3	-12.5	7.2	-15.2	-16.9	-17.3
Extraordinary income/expenses		0.0	0.0	0.0	0.0	0.0	0.0
Pre-tax profit		28.2	38.2	66.0	60.0	61.9	66.9
Income taxes		-8.5	-11.8	-19.1	-18.0	-18.6	-20.1
(Tax rate in %)		-30.2	-30.8	-29.0	-30.0	-30.0	-30.0
Net income		19.7	26.4	46.9	42.0	43.3	46.8
Net income ex minorities		19.3	27.7	44.5	39.3	40.5	44.0
EPS ord.		1.23	1.78	2.82	2.29	2.36	2.56
Growth (in %)	**CAGR (03/08)**						
Sales	11.5 %	24.5	6.1	16.9	26.1	4.0	5.7
EBITDA	15.7 %	24.8	25.1	16.1	27.8	4.7	6.8
EBIT	15.7 %	272.7	25.1	16.1	27.8	4.8	6.8
Net income excl. minorities	18.0 %	---	43.9	60.6	-11.8	3.2	8.7
Cost ratios (in % of sales)							
Cost of goods / sales		---	---	---	---	---	---
SG&A / sales		1.3	1.3	1.1	0.9	1.0	0.9
R&D / sales		---	---	---	---	---	---
Cash flow (in € m)							
Operating cash flow		20.6	21.7	4.3	32.6	36.1	39.9
Capital expenditure		71.7	75.2	40.0	40.0	30.0	30.0
Change in working capital		0.0	0.1	1.5	-0.1	0.0	0.0
Oper. free cash flow		-51.1	-53.6	-37.2	-7.3	6.1	9.9
Cash flow		13.8	18.4	16.0	28.0	30.3	33.8
Productivity (in € ts.)							
Sales / employee		---	---	---	---	---	---
Personnel expense / employee		---	---	---	---	---	---
EBIT / employee		---	---	---	---	---	---
Returns (in %)							
EBITDA / sales		70.0	82.5	81.9	83.1	83.7	84.5
EBIT / sales		70.0	82.5	81.9	83.0	83.6	84.5
Pre-tax profit / sales		48.7	62.2	91.9	66.3	65.7	67.1
Net income / sales		33.3	45.2	62.0	43.4	43.0	44.2
Return on equity		2.8	4.1	5.9	5.0	5.0	5.4
Return on total capital		1.6	2.0	2.9	2.4	2.3	2.4
ROCE		3.9	4.5	4.4	5.1	5.0	5.0
Balance sheet (in € m)							
Property, plant and equipment		995.1	1,101.6	1,331.6	1,455.6	1,555.6	1,668.7
Goodwill		0.0	0.0	0.0	0.0	0.0	0.0
Working capital		-1.8	-1.7	-0.2	-0.3	-0.3	-0.3
Current assets		145.1	166.9	95.2	81.7	92.5	87.3
Capital employed (CE)		1,034.3	1,114.6	1,347.1	1,471.4	1,571.4	1,684.4
Shareholders' equity		695.3	684.4	754.2	785.9	810.4	816.6
Equity ratio in %		56.1	49.9	49.3	47.7	46.0	43.7
Net debt (+), net liquidity (-)		379.4	454.1	624.1	719.2	808.4	913.8
Gearing in %		54.6	66.4	82.8	91.5	99.8	111.9

Price ord. on 8 February 2006: € 50.50

Valuation						
EPS ord. (€)	1.23	1.78	2.82	2.29	2.36	2.56
CFPS (€)	0.89	1.18	1.01	1.63	1.76	1.97
Number of shares ord., (m)	15.6	15.6	15.8	17.2	17.2	36.8
P/E ord.	25.7	19.8	15.5	22.1	21.4	19.7
P/CF	35.7	29.8	43.2	31.0	28.7	25.7
EV / Sales	14.34	15.49	17.66	16.89	17.19	27.27
EV / EBITDA	20.5	18.8	21.6	20.3	20.5	32.3
EV / EBIT	20.5	18.8	21.6	20.3	20.6	32.3

Appendix I: International comparison

Fig. 18 : **Peer-group Deutsche Euroshop**

	Notes	Reuters code	Price (€) 8 Feb. 2006	Market cap.	PER 2005	2006e	2007e	2008e
Corio	2)	CORN.DE	49.87	3,354	14.7	15.4	11.2	10.2
Deutsche Euroshop	1)	DEQGn.DE	50.50	868	15.5	22.1	21.4	19.7
Eurocommercial Properties	2)	ECMPP.PA	30.46	1,075	19.3	18.4	17.0	16.7
Hammerson Property	2)	HMSO.L	15.43	4,394	31.2	35.8	30.8	27.8
Klepierre	2)	LOIM.PA	85.50	3,947	28.8	27.7	23.6	13.1
Rodamco Europe	2)	RDMB.PA	72.20	6,472	16.8	17.6	14.1	13.9
Vastned Retail	2)	VASN.PA	57.10	965	15.3	15.8	15.6	12.3
Average					20.2	21.8	19.1	16.2
Median					16.8	18.4	17.0	13.9
Total				21,074				

Note : 1) M.M.Warburg Investment Research, 2) JCF consensus estimates

Fig. 19 : **Sales growth/multiples**

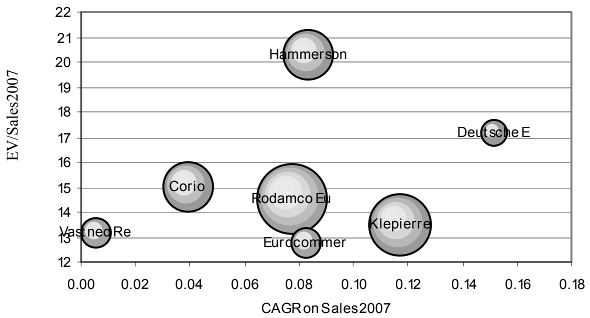

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Fig. 20 : **EBITDA growth/multiples**

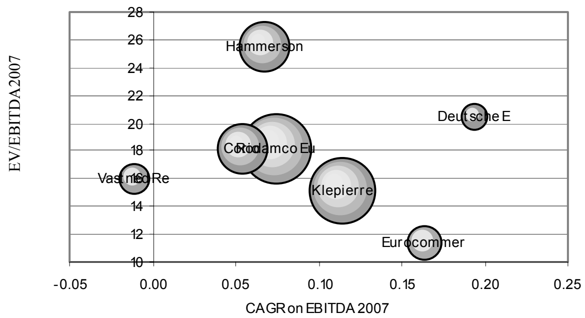

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Fig. 21 : **Net income growth and PER**

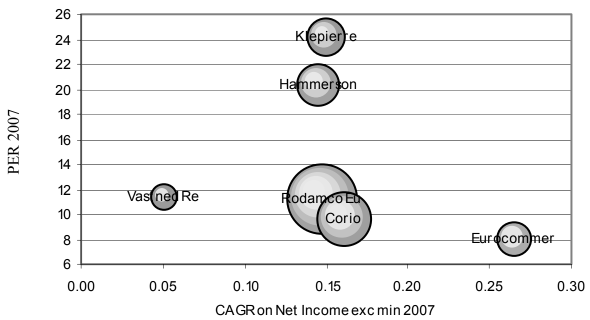

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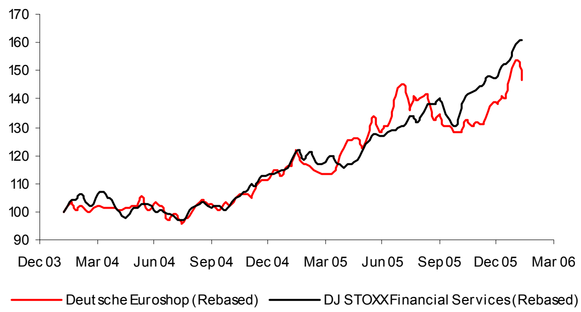
Fig. 22 : **Performance and bench market index**



Source : JCF M.M.Warburg Investment Research

Sector

Fig. 18 : **Peer-group Deutsche Euroshop (continue)**

PEG		EV/Sales				EV/EBITDA				Performance	
2007e	2008e	2005	2006e	2007e	2008e	2005	2006e	2007e	2008e	1 year	1 month
0.75	0.61	15.24	15.86	15.03	12.71	19.0	19.5	18.2	16.7	9.6	9.8
2.16	---	17.66	16.89	17.19	27.27	21.6	20.3	20.5	32.3	26.5	4.1
3.46	3.44	14.80	13.76	12.76	---	19.1	17.6	11.4	---	10.2	5.0
5.09	2.87	23.39	21.56	20.35	19.18	27.0	25.5	25.5	22.6	26.9	5.9
1.29	0.37	15.57	14.00	13.51	14.49	18.0	16.1	15.3	15.8	17.8	5.6
1.12	1.29	16.27	16.27	14.53	15.69	20.2	19.8	18.2	17.0	21.3	2.3
---	1.31	13.34	13.55	13.22	---	16.3	16.5	16.1	---	4.8	6.2
2.31	1.65	16.61	15.98	15.23	17.87	20.2	19.3	17.9	20.9	16.7	5.6
1.72	1.30	15.57	15.86	14.53	15.69	19.1	19.5	18.2	17.0	17.8	5.6

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Fig. 23 : **EBITDA margin 2007e**

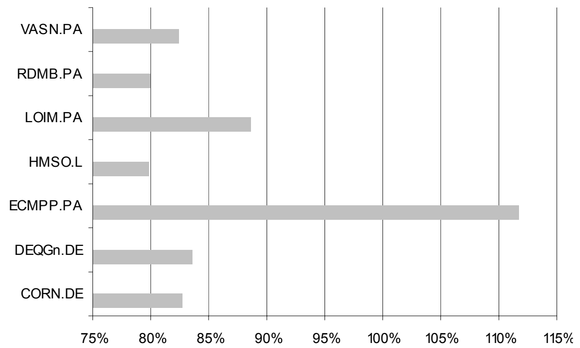

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Fig. 24 : **EBITDA margin 2008e**

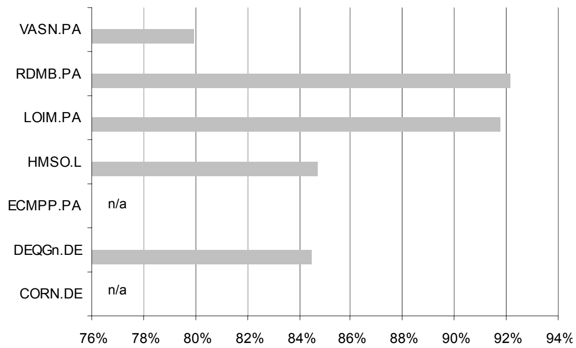

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Fig. 25 : **Sales / net profit 2007e**

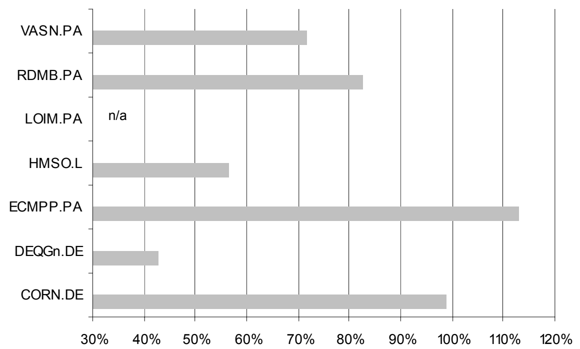

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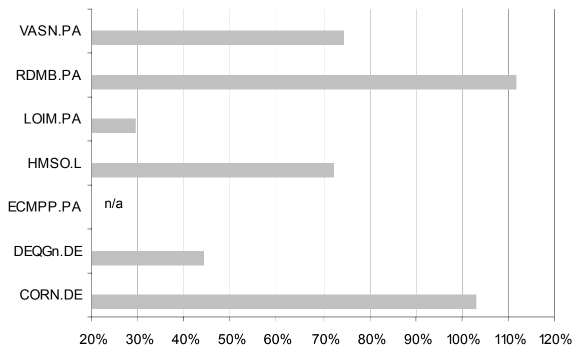
Fig. 26 : **Sales / net profit 2008e**



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Appendix II: Characteristic numbers development

Fig. 27 : **EBIT, EBITDA and net margin**

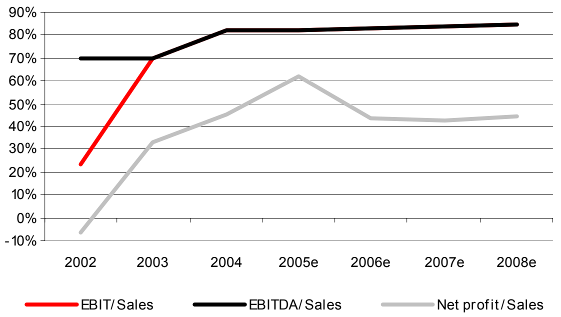

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Fig. 28 : **Productivity development**

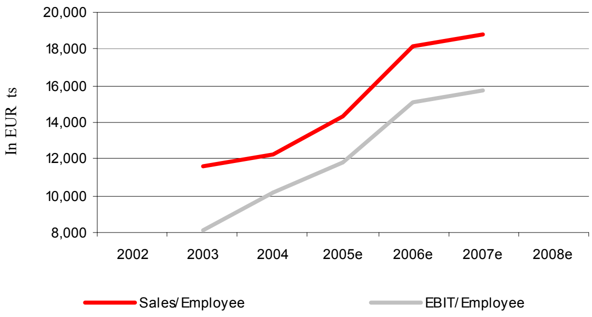

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Fig. 29 : **Capex, working capital and FCF**

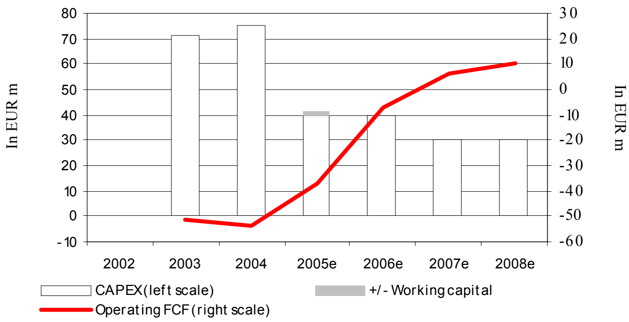

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Fig. 30 : **Capital employed and ROCE**

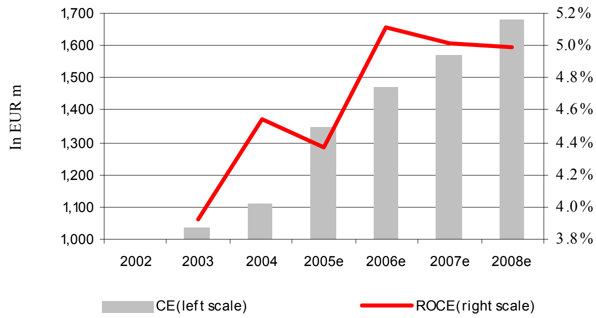

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Fig. 31 : **Shareholder's equity and ROE**

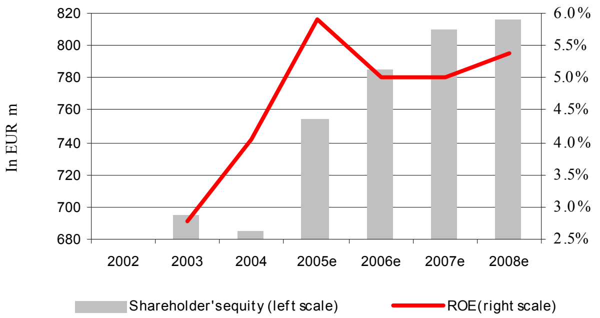

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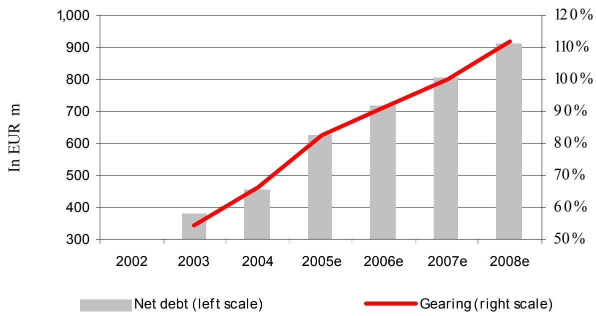
Fig. 32 : **Net debt and gearing**



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Deutsche Euroshop

Fig. 33 : **Balance sheet structure : Assets**

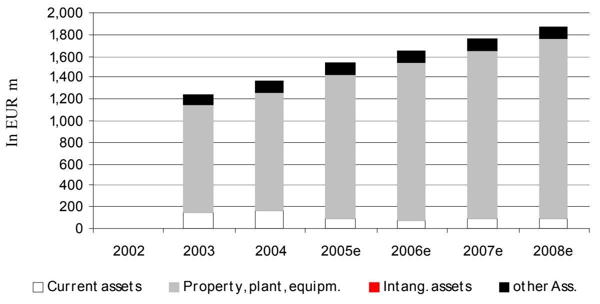

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Fig. 34 : **Balance sheet structure : Liabilities**

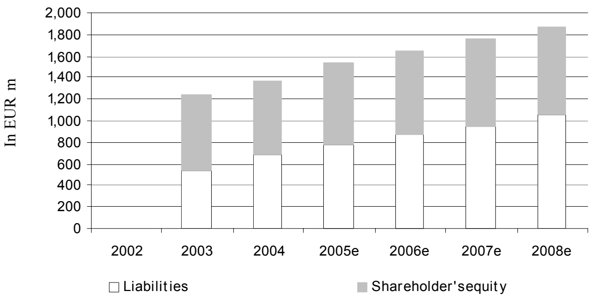

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Fig. 35 : **Free cash flow and financial result**

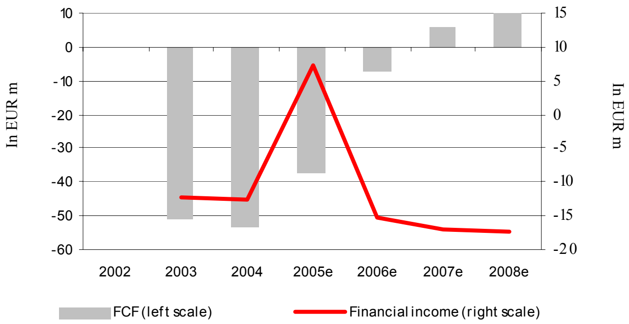

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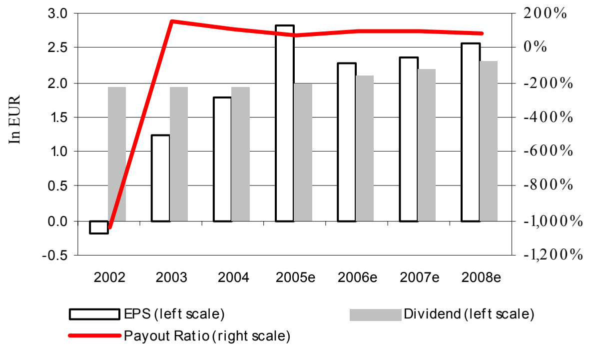
Fig. 36 : **EPS and dividend**



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Price and Rating History

Deutsche Euroshop (DEQGn.DE) as of 8.2.06

Sources: Factset (prices) / M.M.Warburg (ratings)

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Equity Research Report

Kommanditgesellschaft auf Aktien

Completed on February 9, 2006

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