

Deutsche EuroShop

Upgrade to Buy

- **We upgrade Deutsche EuroShop from Hold to Buy with an unchanged target price of EUR 26.** Following our downgrade on January 7 at a share price level of EUR 26, the current price offers again a new entry level.
- **Moreover, released preliminary figures for FY 08 came out higher than expected, both on an operating level and with respect to the valuation result.** The announced increase of guidance for FY 09 did not come as a surprise; however, it does demonstrate the steady growth of the company, on one hand, and its conservative assumptions, on the other.
- **Strong valuation result for FY 08.** Most promising is the reported valuation of the portfolio with a valuation yield of 5.65%. A 15 bp yield shift could be more than compensated for by the strong contribution of the new centers in Gdansk and Hameln. Therefore, the overall portfolio valuation increased by 1%. DES's portfolio valuation does not seem to be aggressive, as European competitors have reported yields of 5.3-5.4% in recent days. Overall, this demonstrates the excellent investment policy by management/company in recent years with conservative assumptions.
- **With a current discount of 18% to our 2010e NAV of EUR 26.79 per share, the company is not cheap – but has an attractive risk/reward profile, in our view.** Reliable cash flows, secured financing and a solid balance sheet are still important assets. Based on our three valuation models (DDM, economic profit, peer group), we derive an unchanged target price of EUR 26.

	2006	2007	2008e	2009e	2010e
Gross rental income (EUR mn)	92.9	95.8	115.3	126.2	129.2
EBITDA (EUR mn)	86.3	77.2	98.2	105.9	108.5
Net income (EUR mn)	100.3	94.2	68.7	-0.8	45.1
EPS reported (EUR)	2.92	2.74	2.00	-0.02	1.31
EPS diluted (EPRA) (EUR)	0.76	0.91	1.15	1.23	1.39
NAVPS (EUR)	25.52	26.91	27.44	26.36	26.79
DPS (EUR)	1.05	1.05	1.05	1.15	1.25
ROE (%)	11.9	10.1	6.9	-0.1	4.6
P/E adjusted (EPRA) (x)	35.5	30.0	20.7	18.2	16.1
P/Cash earnings (x)	20.7	25.1	20.5	14.5	13.4
P/FFO diluted (x)	28.1	24.6	16.5	14.5	13.7
P/NAV (x)	1.06	1.01	0.87	0.85	0.84
EV/EBITDA (x)	18.7	22.3	16.9	15.5	15.0
Div. yield (%)	3.9	3.9	4.4	5.1	5.6

Source: Company data, UniCredit Research

Buy (prev. Hold)

Price on 02/09/09	EUR 22.40
Target price (prev. EUR 26.00)	EUR 26.00
Upside to TP	16.1%
Cost of equity	6.7%
High/Low (12M)	28.34/18.55

INVESTMENT HIGHLIGHTS

Pure focus on attractive shopping centers
 Stable generation of cash flows and dividends
 Solid financing and capital structure

STOCK TRIGGERS

Low risk profile as an asset in the sector
 Tax-free dividend with ca. 5% yield

STOCK DATA

Reuters/Bloomberg	DEQn.F/DEQ GR
Average daily volume (tds.)	142.7
Free float (%)	80.5
Market capitalization (EUR bn)	0.8
No. of shares issued (mn)	34.4
Shareholders	Otto family 19.5%, Attfund Ltd 5.3%, free float 75.2%

UPCOMING EVENTS

Annual general meeting	30-Jun-09
BPC, AC	24-Apr-09
Q1	14-May-09



RELATIVE PERFORMANCE (% CHG.)

	1M	3M	6M
DAX	-1.0	14.0	22.9
Euro STOXX 50	2.1	18.2	25.1
ES Financ. S.	6.9	29.4	34.5

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Strong operating and valuation result – increased guidance

Operating result ahead of estimates

Deutsche EuroShop reported preliminary FY 08 figures (full report on April 24), which were ahead of estimates. Both the operating and valuation results came out higher than we expected and led to a net income of EUR 69 mn (UniCredit (E): 34 mn). Rental income increased by 20% to EUR 115.3 mn (UniCredit (E): EUR 114.3 mn) and lower expenses resulted in an EBIT increase by 25% to EUR 98 mn (UniCredit (E): 94 mn), i.e. 5% ahead of our estimate. Also, FFO increased by 30% to EUR 1.46 per share, i.e. 11% above our estimate. All reported figures are above previously given guidance, which already increased during 2008. For example, DES guided for an EBT of EUR 43-45 mn at the beginning of 2008, increased its guidance later to EUR 45-47 mn and reached EUR 50 mn. These results demonstrate that the company successfully integrated new centers like Gdansk, Hameln and Passau into the shopping center portfolio.

GUIDANCE VS. RESULTS

EUR mn	2007		2008			2009e	
	rep.	prelim.	Guidance	UniCredit (E)	Guidance	Guidance (prev.)	UniCredit (E)
Revenues	95.8	115.3	113-115	114.3	125-128	119-121	126.2
EBIT (excl. revaluation)	77.2	98.2	93-95	93.8	105-108	100-102	105.9
EBT (excl. revaluation)	37.7	50.0	45-47	46.5	50-52	49-51	53.2
FFO per share (EUR)	1.11	1.46	n/a	1.32	1.46-1.49	n/a	1.54

Source: Company data, UniCredit Research

Increased guidance, as expected

We are not surprised by the higher guidance for FY 09, as we already made our adjustments following the increased stake in Kassel one month ago. However, it is worth mentioning that the company has never failed to reach its guidance or reduced its guidance so far. New guidance included the contribution of the new investment (stake in Kassel from 40% to 90%) as of 2009. DES expects rental income to increase by 10%, EBIT by 8% and EBT by 2%. In our view, the disproportional earnings increase is a mix of some costs related to the new investment in Kassel and more conservative earnings guidance. Also last year, the company guided for an increase of 17% (sales)/19% (EBT) and reached an increase of 20% (sales)/29% (EBT) for FY 08. Therefore, we stick to our view that the company can reach an EBT of EUR 53 mn vs. guidance of EUR 50-52 mn.

Surprisingly high valuation result

We are surprised by the strong valuation result of EUR 37 mn for FY 08 vs. our estimate of a loss of EUR 6 mn. Despite higher valuation yields by 15 bp to 5.64% on average for the portfolio, DES booked a value increase of ca. 1% for its shopping centers. This is clearly based on a strong contribution of the new centers in Hameln and Gdansk, more than offsetting the overall valuation losses of other centers. Based on our calculation, a 15 bp yield shift resulted in a valuation loss of ca. EUR 50 mn. Additionally, we expect an unrealized currency loss of the Eastern European centers due to the depreciation of HUF and PLN. Besides a value adjustment due to slightly higher rents, the first-time valuation of the centers in Hameln and Gdansk has to be in the direction of EUR 70-80 mn, in our view. With a net valuation yield of 5.64%, DES's portfolio does not seem to be aggressively valued, as Unibail-Rodamco reported a yield of 5.4% and Eurocommercial Prop. of 5.3% in recent days. The reported valuation of the portfolio is relatively resilient compared to the valuations of competitors, which demonstrates the conservative assumptions of the management/company in recent years and its successful investment policy, which regularly led to first-time valuation results for new centers. NAV per share was EUR 27.44 (+2% y-o-y) vs. our estimate of EUR 27.05. Due to the reported NAV basis in 2008, we slightly increase our estimates for 2009 (+3% to EUR 26.36) and 2010 (+4% to EUR 26.79). We still assumed a further yield shift to 5.9% in 2009 and to 6.0% in 2010.

Upgrade from Hold to Buy

We upgrade Deutsche EuroShop from Hold to Buy, which is based on following reasons:

1. Following our downgrade 5 weeks ago at a level of EUR 26, which remains our target price, the current share price of ca. EUR 22 offers an attractive entry level again.
2. The reported valuation of the portfolio is surprisingly resilient compared to the valuations of competitors, which demonstrates the conservative assumptions of the management/company and the successful investment policy.
3. With a discount of ca. 18% to our 2010e NAV, the company is not cheap in comparison to its peers. However, reliable cash flows, secured financing and a solid balance sheet are still important assets.

CONSOLIDATED INCOME STATEMENT

		2006	2007	2008e	2009e	2010e
Total revenues	EUR mn	184.6	147.6	163.1	127.2	130.2
Total expenses	EUR mn	-25.9	-19.6	-18.2	-75.5	-25.0
EBIT	EUR mn	158.6	127.9	144.9	51.7	105.2
Gross rental income	EUR mn	92.9	95.8	115.3	126.2	129.2
Property op./management costs	EUR mn	-16.2	-15.4	-17.2	-18.8	-19.3
as a percentage of rental income	%	17.4	16.1	14.9	14.9	14.9
Net rental income (NOI)	EUR mn	76.7	80.3	98.1	107.4	110.0
as a percentage of rental income	%	82.6	83.9	85.1	85.1	85.1
Profit on disposal of investment properties	EUR mn	14.8	0.0	0.0	0.0	0.0
Other operating income	EUR mn	1.2	1.1	1.1	1.0	1.0
Other operating expenses	EUR mn	-6.3	-4.2	-1.0	-2.5	-2.5
EBITDA (DES defin.: EBIT)	EUR mn	86.3	77.2	98.2	105.9	108.5
as a percentage of total revenues	%	46.8	52.3	60.2	83.3	83.3
Valuation result	EUR mn	72.3	50.8	46.7	-54.2	-3.3
EBIT	EUR mn	158.6	127.9	144.9	51.7	105.2
as a percentage of total revenues	%	86.0	86.7	88.9	40.6	80.8
Income from investments	EUR mn	1.9	1.5	1.6	1.7	1.7
Net financial result	EUR mn	-42.9	-51.6	-59.8	-54.3	-52.6
EBT	EUR mn	117.6	77.8	86.6	-0.9	54.4
as a percentage of total revenues	%	63.7	52.7	53.1	-0.7	41.7
EBT excl. revaluation	EUR mn	45.3	27.1	40.0	53.2	57.6
Taxes	EUR mn	-17.4	16.3	-17.9	0.2	-9.2
Income tax rate	%	14.8	-21.0	20.7	18.0	17.0
Profit for the period	EUR mn	100.3	94.2	68.7	-0.8	45.1
as a percentage of total revenues	%	54.3	63.8	42.1	-0.6	34.6
Minority interests	EUR mn	0.0	0.0	0.0	0.0	0.0
Earnings after minority interests	EUR mn	100.3	94.2	68.7	-0.8	45.1
Adj. net income (direct investment result)	EUR mn	26.1	31.2	39.6	42.2	47.7
Indirect investment result	EUR mn	74.2	63.0	29.1	-43.0	-2.6
Funds from operation (FFO)	EUR mn	33.0	38.2	49.7	52.9	56.2
EPS reported	EUR	2.92	2.74	2.00	-0.02	1.31
EPS reported/diluted	EUR	2.92	2.74	2.00	-0.02	1.31
EPS diluted (EPRA)	EUR	0.76	0.91	1.15	1.23	1.39
FFOPS basic	EUR	0.96	1.11	1.45	1.54	1.63
FFOPS diluted	EUR	0.96	1.11	1.45	1.54	1.63
DPS	EUR	1.05	1.05	1.05	1.15	1.25

Source: Company data, UniCredit Research

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-	-

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Company	Date	Rating	Currency	Target price
Deutsche EuroShop	02/10/2009	BUY	EUR	26.00
Deutsche EuroShop	01/07/2009	HOLD	EUR	26.00
Deutsche EuroShop	10/30/2008	BUY	EUR	25.00
Deutsche EuroShop	08/14/2008	HOLD	EUR	25.00
Deutsche EuroShop	07/10/2008	HOLD	EUR	26.50
Deutsche EuroShop	05/14/2008	HOLD	EUR	30.00
Deutsche EuroShop	04/30/2008	BUY	EUR	30.00
Deutsche EuroShop	02/19/2008	BUY	EUR	29.00

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