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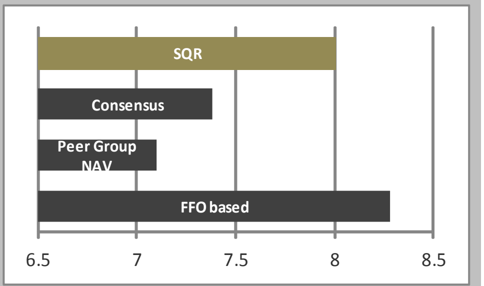
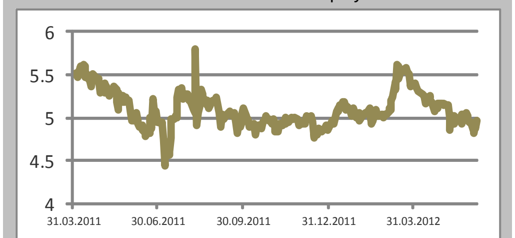
KWG Kommunale Wohnen AG Buy, TP EUR8.00

Target price decomposition



Stock data/Rating			BUY
Last price	**EUR**	**5.01**	**±**
SQR target	**EUR**	**8.00**	**59.7%**
Consensus target	**EUR**	7.39	
52 week high/low	EUR	5.80	4.39
All-time high/low	EUR	13.99	0.49
Performance	-1month	-3months	ytd
%	-0.4%	-4.2%	2.4%
Current market cap	EUR	71.43	m
Shares out (average)		14.38	m
Free float		14.38	%
P&L	**2011**	**2012e**	**2013e**
Sales EURm	34.0	57.7	43.1
EBIT margin %	72.51	137.05	75.97
Net margin %	38.29	87.88	38.89
ROA %	7.71	12.54	7.62
ROE %	10.61	17.64	8.20
Dividend yield %	-	-	-
Balance Sheet EURm	**2011**	**2012e**	**2013e**
Balance Sheet	241	318	329
Real estate assets	228.9	306.2	316.7
Cash	3.6	3.0	4.1
Equity	92.6	144.2	157.1
Net debt	132.1	153.2	149.7
Enterprise value	204	225	221
NAVPS	7.25	9.08	8.69
Valuation	**2011**	**2012e**	**2013e**
EV/EBIT	11.11	5.70	8.93
P/E	7.27	2.81	5.55
P/S	1.54	1.11	1.49
P/E at SQR target	8.9	5.1	10.2
ROE/ROA	1.38	1.41	1.08
FFO/NAV%	0.49	3.35	5.78
Market data			
Bollinger up/low	EUR	5.09	4.84
MAV 100/200 days	EUR	5.13	5.05
Beta (6 months)		0.51	
Code	BIW GR Equity		



Source: Bloomberg

Growth investment at rock-bottom value stock prices.

KWG acquired Barmer AG for a rock bottom price and increased capital by €19m. Investing the funds boosts value

KWG Kommunale Wohnen (KWG) completed in June a groundbreaking deal for the company: the BWAG acquisition. It increases its asset base by 30%, its FFO by around 30% (CAGR until 2014), its NAV by more than 20% and its platform for further growth. The silently conducted deal shows the management's excellence in creating shareholder value - more upside to come.

KWG exceeded initial 2011 results. Net profits of EUR9.8m came in EUR1m ahead of initial expectations on revenues of EUR21.6m. KWG currently owns 5,419 residential units, BWAG additional 1,391 units. KWG succeeded in cutting vacancies and producing FFO of around EUR2.7m, we assume. Net cold rent was about EUR14.6m, 20% of current market capitalization.

KWG's announced transaction is - we believe - the starting point for entering a more profound growth path. The platform - laid out in North Rhine Westphalia - enables KWG to swiftly integrate this and further acquisitions. Essentially, new assets on the platform can be operated with a fraction of inherited operating costs, boosting KWG's FFO and asset values.

* **Asset growth is KWG's prime goal**
Following a phase of consolidation at a 5,000 unit level, KWG set up an impressive asset growth path by adding 30% in assets through BWAG

* **Operating results improved already**
While in the past KWG used each available euro to turn its 'investment portfolio' into a 'core portfolio', the current size creates positive FFO (SQR calculation)already. This should at least double in the next three years

* **Acquisition offers massive NAV upside**
BWAG is under-geared and its value under-estimated. Based on market valuations, the acquired assets bear 100% value upside bases on market cap

KWG is expected to achieve net profits after the successful integration of BWAG (2013e) of EUR25m and an EBIT of EUR10.5m. We understand that the company's LTV will decrease initially (BWAG LTV ~20%), before refinancing. This suggests that KWG sees significant re-financing potential in the acquired portfolio, we believe of up to EUR25-30m in the next two years.

We do not share the view that **KWG** needs to trade at a discount to its peers due to lower market capitalization. While this might have been justified during the period, in which KWG did not yield positive FFO this would no longer be the case. The solidity of the business model should now outweigh the current market capitalization issue, meaning potential peer group out-performance.

KWG's shares trade in cheap 'crisis scenario' Europe while its activities are truly in the 'non crisis' world. KWG has no re-financing issues in the next years. The BWAG deal lowers its LTV anyway. The discount to new NAV of around 45% is in line with that of GAGFAH, which still sees re-financing issues of around 80% of its current market cap. The gap should close, hence we lift our target price to EUR8.00.

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Please inform yourself of important disclosures and disclaimers in the appendix

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Executive Summary

KWG's acquisition boosts FFO 2-fold.

NAVPS upside 50% in three years

KWG Kommunale Wohnen AG has turned into a positive cash flow producing residential real estate company in 2011. The intelligent acquisition of Barmer Wohnungsbau AG is a blueprint of KWG's expansion strategy: buying cheaply a top product in Tier2/3 cities, within the proximity of existing portfolios in order to slash operating costs and boost rent levels and operating income. This transaction catapults KWG into a new league, adding 30% of units instantly, trebling FFO and boosting NAVPS by 15% in the next three years (SQR).

KWG posted a successful financial year 2011: Total revenues increased 8.5% to EUR21.5m, helped by a 13% increase in net cold rent to EUR14.6m. Together with a further value appreciation of its assets, KWG posted a 10% increase in pre-tax profits to EUR11.9m. Net profits reached EUR9.8m (+15%), leading to EPS of 90EURcts. Operationally, we assume that KWG had achieved a positive FFO of around EUR2.7m (SQR estimate). Operational performance was helped by the 442 units purchased in Delmenhorst in July 2011 and the cut in the 'core portfolio' vacancy rate to 2.7% (down from 6.4%).

Q4 2011 with strong rental performance: KWG benefits from the two effects, namely a) the increase in demand for attractively priced and newly refurbished living space due to record employment levels across Germany and b) its unique business model which is based on cheap sourcing of space and renovation work. Both effects led in Q4 2011 to rental income of EUR4.1m, implying an annual rental income of more than EUR16.3m on an annual basis (no rent increase included). This alone warrants an 8.6% NRI growth in 2012, outpacing its peers in Germany.

KWG invested massively in the past years – there will be less going forward

Modernization expenditures set to fall in 2012: Following a boost to EUR28/sqm investment in 2011 (up from EUR20/sqm in 2010 and EUR8 in 2009), most of KWG's assets are converted into 'core assets'. The core asset proportion rose from 64% by the end of 2010 to 75% by the end of 2011, leaving some 1,300 units in the 'investment portfolio'. As the acquired BWAG portfolio is all 'core' the investment portfolio proportion drops to 20% from 25%. At an assumed modernization rate of 450 units annually, the rate would drop to EUR21/sqm in 2012 and towards ~EUR15/sqm in 2013. Based on past experience, ROI yield should be around 35%, or EUR4.8m annually after 2014.

BWAG acquisition is a 'lucky buy' – boosts KWG's local reach

BARMER Wohnungsbau AG is a leading landlord in Wuppertal, a Tier2 city in the southern part of the 'Ruhrgebiet', the most densely populated region in Germany with 16m inhabitants (~20% of Germany's population). Barmer owns 1,391 residential units, which are mostly energetically renovated and has almost no vacancy (11 units on their website). The company is socially active in Wuppertal, supporting living oriented projects. BWAG's average 2010 rent is 25% below average market rent. KWG is able to raise rents 'organically', but can push towards market rent only from 2014 onwards. KWG owns 77.3% of BWAG at this stage (16% free float, 6.6% City of Wuppertal)

However, BWAG offers significant upside. Based on available data, BWAG's rental income stagnated around EUR6m for the past 4 years, while net income (cash earnings, German GAAP) were around EUR0.5m. This is due to very high maintenance fees, which accounted for EUR19/sqm/year in 2010 – against ~EUR4.75/sqm/year with KWG. The difference alone would be worth EUR1.4m (= 21% of BWAG's stated rental income). In addition BWAG's assets are valued at purchase prices (German GAAP), implying significant valuation upside under IFRS. We assume that the entire valuation upside is close to EUR40m (based on current sqm prices and rent potential)

KWG is cheap – too cheap after this deal. Market cap set to reach EUR>100m soon

History weighs on the stock price: KWG in the past invested voluntarily into its assets – part of the business model. As such, comparable FFO development trailed that of its peers. However, this time is over: we expect KWG to show FFO of EUR6.2m by 2013, assuming an additional acquisition of 2,000 units. Here, we have not altered KWG's cost base significantly, although we assume a massive reduction in maintenance costs at BWAG (see above).
We believe that the uncertainty in this earnings estimate is low, given KWG's track record on creating value in its assets., KWG's share prices appear to have more than incorporated the risks of the past, but no realistic chances: the stock trades at 55% NAV (2012e) (market average ~75% of NAV), and at 21x EV/cashEBIT (2012e, 5% yield). On 2014e estimates, the company trades at only 14x EV/cashEBIT (7.2% yield). These are cash yields, as we do not include IFRS valuation gains into our EBIT calculation.

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The BWAG deal

BWAG acquisition is a 'lucky buy' – boosts KWG's local reach

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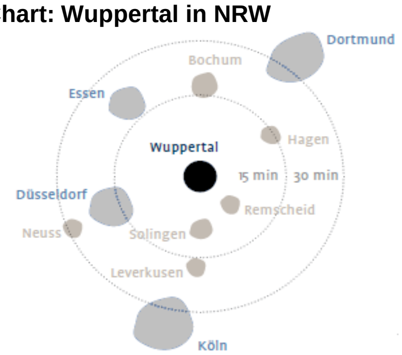
City of Wuppertal

Wuppertal is a regional center of the 'Bergische Städtedreieck' (Wuppertal, Remscheid, Solingen – 'Berg. Triangle', 30 minutes commuting time). The city is economically healthy, allowing employees to earn on average 4% more than in the other cities of the triangle. As a result, office space is more expensive, luring higher income groups into the city. However, with a rather high manufacturing proportion of GDP (34%), the overall income level is slightly below that of NRW, while employment levels are higher than in NRW.

Chart: Wuppertal in NRW



Source: City of Wuppertal

Table: Economic data for Wuppertal

	Wuppertal	Berg.Triangle	North Rhine Westphalia
Inhabitants	349.713	630.828	17.933.064
Employed	113.766	202.314	5.798.724
% ratio	32,5%	32,1%	32,3%
GDP total (2010, €bn)	10,17	17,61	541,10
GDP per capita (€)	29.080,99	27.915,69	30.173,32

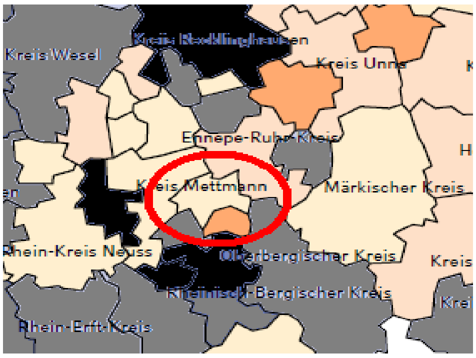
Source: City of Wuppertal, 2011

Wuppertal is located neatly between three international and national airports (distance to Duesseldorf International Airport 25mls, to Cologne/Bonn International Airport 35mls and to Dortmund Airport 30mls).

As with other Tier2 cities, the number of households in the coming years depends on a) demographics and b) economic attractiveness. In case of Wuppertal, the city is (see above) within the vicinity of larger cities. Hence, there will be most likely a drift away from Wuppertal into these cities, namely Duesseldorf and Cologne. However, the price development in these cities is currently far more aggressive than in Wuppertal, suggesting that the decline in households would be lesser than currently estimated, which is about 7%

Wuppertal is a solid city with little risk of massive decline in household numbers

Chart: development of households in the area around Wuppertal until 2030



Source: NRW Bank 2011, grey: rising numbers, gold: falling numbers

The housing market is typical for a Tier2 city: there is little price variance for semi-detached houses and terraced houses, as space in the surrounding of the –relatively small – city is sufficient, meaning that the price for ground is less important (average land price: EUR250/sqm). Here, prices range from EUR235,000 to EUR270,000 on average (2010/2011 data).

For owner occupied apartments, the local price range is between EUR2,050/sqm and EUR2,500/sqm (Source: Wohnungsmarktreport Wuppertal 2010). These prices are calculated for the 1st time use (newly built apartments). Renovated and used building typically fletch prices around 25-35% below the stated prices for newly built ones. This relation is based on the difference of rent levels (for average quality).

BWAG's portfolio is under-rented, even on low Wuppertal comparison

Table: Rent levels in Wuppertal

Average area average fittings Building year	low level €/sqm	high level €/sqm	€/sqm	BWAG average €/sqm
before 1948	3,80	5,80		
1948 - 1960	3,95	5,95		
1961 - 1969	4,05	6,15	5,10	
1970 - 1982	4,25	6,45	5,35	} 4,07
1983 - 1990	4,95	7,45	6,20	
1991 - 2000	5,50	8,20		
Mietspiegel 2010			**5,10**	
Wuppertal average	**4,42**	**6,67**		

Source: City of Wuppertal, 2011, BWAG, KWG

The table above shows the current average rent levels for apartments in Wuppertal, based on average rents in 2010/2011. The table links the average rent level to the age of the buildings. We understand that BWAG's assets are mostly built in the 60ties through the 80ties. The current average rent per sqm is EUR4.07/month.
This level is well below the average level for flats in building of the same age, which is typical for BWAG's assets. It is therefore clear that BWAG'S assets are not over-rented.

BWAG transaction

KWG acquired 77.3% of BWAG's shares. The company is a joint stock company, but its shares are not listed. KWG is the key shareholder now, with some 16% of shares described as 'free float' and 6.6% is held by the City of Wuppertal. The latter would not dispose of its shares, allowing KWG to keep the transaction free of transfer tax (5%) payment.

We understand that KWG is in concrete negotiations to acquire further shares in BWAG from other shareholders, increasing its stake and lowering the minority interest in the company. KWG has indicated that the parties decided to keep the purchase price secret. Based on the available information, we assume the following parameters for the transaction:

BWAG purchase price is attractive for KWG – helped by using own shares

Table: BWAG purchase price estimates

Instrument	number (m)	value €/unit	value €m
KWG shares	1,50	7,54	11,31
debt (BWAG)			13,30
additional payment			20,69
units	1.391		
sqm	90.600	500,00	**45,30**
sqm/unit	65,13		
rent/sqm/year (€)	48,84		
rent/unit/month (€)	265,09		
est value		750,00	**67,95**

Source: KWG, SQR estimates

Based on available data, BWAG's rental income stagnated around EUR6m for the past 4 years, while net income (cash earnings, German GAAP) were around EUR0.5m.

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This is due to very high maintenance fees, which accounted for EUR19/sqm/year in 2010 – against ~EUR4.75/sqm/year with KWG. The difference alone – i.e. the shift of BWAG cost structure to KWG cost structure - would be worth EUR1.4m (= 21% of BWAG's stated rental income). In addition, renovation and modernization costs could be trimmed. The KWG platform allows integrating additional assets at marginal costs well below inherited costs. This advantage grows with size.

In addition BWAG's assets are valued at purchase prices (German GAAP), implying significant valuation upside under IFRS. We assume that the entire valuation potential is close to EUR55m (based on current sqm prices and rent potential)

BWAG deal: other conditions

BWAG Social Charta is no issue for KWG. Rents start increasing by 2014 to market level

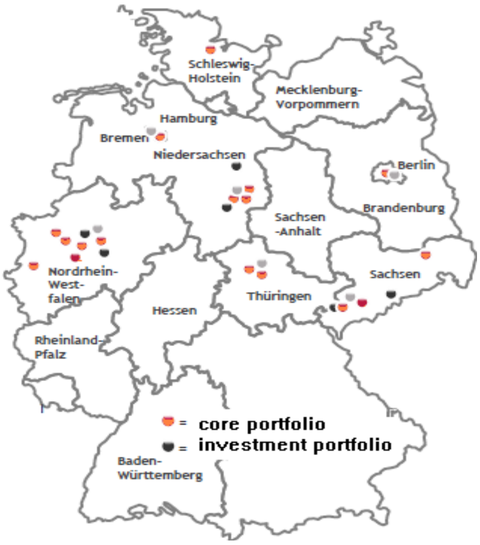
Following other recent transactions between local city-linked asset holders and private companies (Gagfah – City of Dresden, Patrizia – LBBW/City of Stuttgart), KWG also had to agree to some 'Social Charta'-like conditions. These include, we understand:

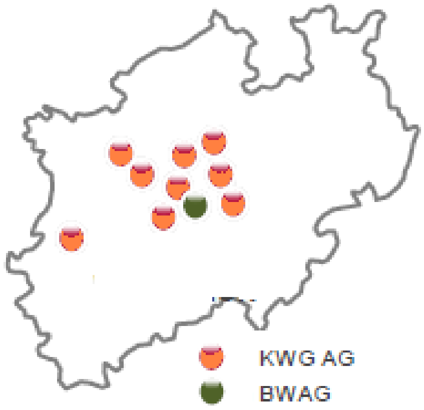
- No significant increase in rents, continuation of the rent price model of BWAG until the end of 2013
- Thereafter, gradual increase in rents toward Wuppertal average rent level (Mietspiegel)
- Maintain the current personnel (6 persons) for the next 5 years
- Pre-emptive rights for tenants in case of disposal. However, different to the Gagfah condition in Dresden, tenants would not get preferential prices

While the fact that KWG would keep the current personnel for the next years would not be a burden for KWG, as the company plans to expand in the region anyway. We understand that KWG is in negotiations for further 2,000-5,000 units in NRW. This would boost KWG asset holdings in the region to about 50% of the total – enlarged – assets base.

BWAG and KWG portfolios are close and easy to manage – room for cost efficiency and growth

Chart: current locations of KWG assets in Germany and BWAG and KWG in NRW





Source: KWG 2012

We assume that KWG would need to pay additional EUR10m for the acquisition of 77.3% of BWAG, implying that the remainder would cost another EUR7-10m. In any case, the average price/sqm would be well below the average price for portfolio transactions (EUR750/sqm), implying a value appreciation of around EUR23m (based on full consolidation).

This amount is equal to 40% of KWG's current market capitalization. Assuming the privatization levels prevailing the Wuppertal housing market (see above) and assuming that 50% of the assets are suitable for privatization, the appropriate value would be EUR102m, implying EUR55m of appreciation, equal to 100% of KWG's current market capitalization.

We also believe that KWG would use a different LTV formula than BWAG. In essence, the increase in IFRS value would be sufficient to refinance (i.e. leverage) the BWAG portfolio towards the level of KWG average LTV. In this case, the increase in typically non-cash IFRS valuations would lead to a cash inflow to the same tune.

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Site visit: first hand impressions

NRW and Lower Saxony sites visit confirms the values inherent in KWG

We visited the asset sites of BWAG and KWG in North Rhine Westphalia and in Lower Saxony. The site visit confirmed our view that KWG's assets mostly are the best assets within the micro-environment. This simply means that tenant move into the sites, when possible. This explains, why KWG is successful in filling its assets with tenants quickly after renovation efforts have been terminated.

We visited sites in Duesseldorf (KWG), Wuppertal (BWAG), Gelsenkirchen (KWG), Braunschweig (KWG) and Wolfsburg (KWG).

BWAG portfolio visit

Key assets are in Barmen and Elberfeld, the only 'interesting' areas in Wuppertal. BWAG assets are in excellent condition

- Barmen newly renovated area (>150 units). Basically, all flats are renovated to the highest standard. Additional floors have been added (wooden construction, less than 6 months to finish) and increase rental revenues. All capex has been don and budgeted already, went through P&L. Valuation upside through shift to IFRS significant, but not through aggressive valuation, but through capitalization of investments. Ongoing maintenance capex would, we believe, fall to less than EUR3/sqm/year in the coming 5 years.
- Nursing home: 36 newly built units (look like the renovated ones from Barmen) in a serviced home. Fully occupied and subsidized financed with 0.5% annual interest costs. Over 15% ROI.
- Elberfeld single house compound. Within the BWAG, there are approx 60 stand alone houses (each approx. 100sqm plus approx 150sqm of garden and separate parking space), built in the 70s, within a park-like surrounding. Fully let and in top condition. In case of privatization, this could easily fletch EUR1,750/sqm.
- Elberfeld (2), end of the town housing complex, fully let, on the street going to Bochum. All 2 room apartments with balcony. Rent increases easier to be pushed through, as turnover is a touch above the 10% average turnover.

BWAG: new (2011) building (nursing home)

BWAG: renovated (1968) multi-family house

Source: SQR photos

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BWAG: single houses and semi-detached houses ensemble

Source: SQR photos

Gelsenkirchen portfolio visit

- Registered ensemble with large inner park, which is very well maintained by the local church, resulting in no extra costs for KWG. Top location within the micro-area of Gelsenkirchen. Works like a magnet, with all possible flats being easily re-rented. We were impressed by the quality of the assets and the tenant structure (hardly any Hartz IV)

Gelsenkirchen: registered landmark building

Source: SQR photos

Braunschweig portfolio visit

- We visited several assets in Braunschweig. KWG acquired buildings for renovation, which has now been finished. We visited a flat, which was occupied by a new tenant. He moved into the KWG assets, as the quality was superior and the he was willing to pay a higher rent.
- Other buildings are located near the university and are home to many students, which pay superior rents. KWG will add balconies in the back in the coming year, boosting rent levels, as it will also increase insulation.

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Braunschweig: single house at the end of street with 8 KWG multi-family houses

Source: SQR photos

Wolfsburg portfolio visit

- We saw the excellently refurbished ensemble, which is fully let. The proximity to the city hospital increases turnover, which allows for rising rents at all times. Waiting lists exist for new tenants. The asset looks like new, the surrounding is very well maintained.
- KWG is likely to sell the assets for EUR970/sqm, after acquisition costs of EUR470/sqm and renovation of approx. EUR200/sqm. This would represent the full IFRS value, i.e. showing that the valuation is not excessive.

Wolfsburg ensemble

Source: SQR photos

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Valuation Discussion

KWG looks very attractive at the current price level. The discount to NAV (stand-alone basis, 2011e) is already high at 35%. This discount implies high operating risks, which would eventually translate into asset value destruction.
The opposite has been the case and is seen continuing. In 2011, KWG lowered the proportion of its 'investment portfolio' from 36% of total units to less than 25%. With the BWAG acquisition, this proportion would fall further, we believe to 20%. In fact, the acquisition improves KWG's risk profile in terms of safer cash flow generation and asset value improvement.

Operating cash flow valuation

Looking at KWG's accounts, we would assume the following development (**Note: this calculation is based on EPRA standards. SQR excludes in its accounts IFRS impairments from top line revenues, which is different to EPRA)**.

Table: KWG accounts

KWG (€ '000) **(EPRA accounting)**	**2.009**	**2.010**	**2.011**	**2012e**	**2013e**	**2014e**
Total revenues	18.924	20.628	25.276	28.776	32.614	35.776
IFRS impairments	6.300	11.896	8.753	28.962	10.453	10.453
Reported sales	25.224	32.524	34.029	57.739	43.067	46.228
EBITDA	9.817	16.223	18.545	39.690	25.064	27.124
EBIT	9.753	16.153	18.328	39.438	24.776	26.808
Pre tax profits	4.833	10.727	11.940	32.847	17.394	20.181
Reported net profits	3.898	8.577	9.826	25.472	12.948	15.178
FFO	- 2.196	- 1.951	918	3.933	5.864	7.322
NAVPS	6,11	8,04	8,24	9,08	9,66	10,60
EBIT margin	52%	78%	73%	137%	76%	75%
FFO margin	-9%	-6%	3%	7%	14%	16%
Price/sales	1,40	1,51	1,54	1,11	1,49	1,38
Imp. market value				7,73	8,21	9,01
Implied shareprice (15%dic)				**7,73**	**8,21**	**9,01**
average implied price					**8,32**	

Source: KWG, Bloomberg, SQR estimates

The table above includes the BWAG acquisition with the following assumptions:

- 6/12 consolidation of the newly acquired assets, assuming a full consolidation of 6,069 units in 2012 and 6,764 thereafter
- Increase in rent levels by 2.5% annually until 2014, thereafter 10%
- Value appreciation of EUR28m in 2012 and EUR10m in 2013 as a result of the a) the consolidation of BWAG in 2012 and b) higher FFO contribution in 2013
- Initial increase in debt in 2012 by EUR36m, declining thereafter
- Shift in maintenance costs towards KWG level, improving the cost ratio on gross rental income from 31% in 2011e to 25% by 2014e

As a result, reported EBIT margins are set to rise by 10% from 60% to 72%, while the FFO margin jumps by to 14%. The average EBIT margin in the past 5 years was 53%, leading to an average price/sales multiplier of 1.49 times.

This leads to implied market valuation of EUR>120m by the end of 2012 latest. We therefore adjust our price target to EUR8.00/share (based on 16.2m shares outstanding, the result from the increase in capital through the acquisition structure, which includes 1.5m new shares).

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NAV based peer group valuation

KWG will see its NAV rising significantly as a result of the BWAG transaction and as a result of the ongoing shift from ‘investment portfolio’ (which basically has purchase price valuation, i.e. close to zero) into ‘core portfolio’ (which is almost completely rented out, i.e. commands full market valuation).

We believe that KWG’S NAVPS is set to reach EUR10.60 by the end of 2014e (based on 16.2m shares), and EUR9.08 by the end of 2012e. Based on this assumption, the following comparison to the company’s German peer group applies:

Table: Peer group comparison (NAVPS base)

Name	last price	last NAVPS	% discount	next NAVPS	% discount
GAGFAH SA	7,23	12,84	44%	12,80	44%
DEUTSCHE WOHNEN AG-BR	11,24	12,27	8%	12,50	10%
TAG IMMOBILIEN AG	7,78	8,33	7%	9,94	22%
FRANCONOFURT AG	7,48	9,00	17%	9,25	19%
PATRIZIA IMMOBILIEN AG	4,72	5,98	21%	6,25	24%
CONWERT IMMOBILIEN INVEST SE	8,04	18,35	56%	18,80	57%
GSW IMMOBILIEN AG	26,84	29,96	10%	30,20	11%
average			**23%**		**27%**
KWG KOMMUNALE WOHNEN AG	4,86	8,23	41%	9,32	48%

Source: Bloomberg, company data, SQR estimates

Currently (NAVPS, mostly using 2011 audited data) the average discount to NAV is 23%, while the figure for KWG stands more at 41%, i.e. 78% higher). The average data is distorted by the high discounts of Gagfah and Conwert, two companies with special, specific issues.

In the case of Gagfah, re-financing issues remain a burden, even after the Dresden case settlement. It should be noted that Gagfah initially entered the market as a safe dividend paying company (starting with quarterly payments). These have been omitted in order to allow Gagfah building up a cash pile to move itself into a better position, when refinancing issues emerge in late 2012 and in 2013.

In the case of Conwert, the company is still struggling in managing the conversion from a low yielding Austrian asset base towards a high yielding German asset base. In addition, values attached to some non-residential assets – namely the ECO Buisiness portfolio – are seen difficult to assess by outside analysts. Finally, Conwert carries a triple-digit euro amount of goodwill on its balance sheet. While we would regard this amount as justified, the NAV quality is mostly seen to be inferior to that of pure real estate assets.

The discount to NAV increases in 2012e to 48%, based on our estimates and the inclusion of the BWAG acquisition. We regard this level as conservative, assuming a shift towards market valuation latest in 2013. It should also be taken into account that KWG would be able to increase rents (i.e. cash flow from rental operations) at BWAG more aggressively after 2013.

Excluding Gagfah and Conwert from the peer group (for the moment, until these companies have solved their internal issues), the average discount to NAV would be 12% in 2012e, leaving a 36 percentage points gap towards KWG. On an average valuation, KWG’s shares should trade close to EUR7.00 on this basis. However, this price would not reflect the underlying – almost certain – further increase in NAVPS towards EUR10.00 in 2013e. Anticipating this move, KWG’s shares should trade north of EUR8.00 within the next 12 months.

SWOT Analysis

Strengths

- Leading investors provide full support to KWG management and its strategy
- Platform structure is safe and allows for further fast and cost efficient expansion
- Proven track record of turning assets around in presumably more challenging areas
- Proven network to provide further value and cash enhancing acquisitions

Weaknesses

- Still too low market capitalization to attract shorter-term orientated investors
- Low trading volume in KWG shares
- Still too small to participate in large auctions

Opportunities

- Boosting market capitalization above the EUR100m bracket for the 1st time in history
- Proving integrative capabilities with the BWAG deal, attracting more assets
- With higher market cap, shift into Prime Standard possible and value accretive, as possibilities for an index membership increase
- Further asset growth in NRW would come and hardly more operating costs, boosting FFO to gain sustainable dividend paying capability.

Threats

- Abrupt change in financing abilities of banks, KWG relies on. Requirement of higher equity participation in acquisitions
- Change in real estate taxation without possibilities to pass on additional costs
- More aggressive move of large asset holders towards smaller deals, basically squeezing out KWG from attractive acquisitions

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Financials

Profit and Loss Accounts

P&L Accounts	2010	2011	2012e	2013e	2014e
Rental income gross	19.775,44	21.658,71	25.068,45	28.627,93	31.490,73
Rental income gross	-	-	-	-	-
Rental income gross	-	-	-	-	-
Trade income gross	-	-	-	-	-
other income	852,58	3.617,39	3.707,82	3.985,91	4.284,85
Group Performance	**20.628,02**	**25.276,10**	**28.776,27**	**32.613,84**	**35.775,58**
Group Performance (stated)	**32.523,82**	**34.029,28**	**57.738,65**	**43.066,59**	**46.228,33**
Costs of goods sold	4.596,89	3.350,59	3.546,23	3.746,04	3.902,54
Costs of goods sold	7.073,18	7.013,31	7.516,09	7.938,52	8.636,71
Costs of goods sold	-	-	-	-	-
Administrative costs	1.590,38	2.331,97	2.690,27	2.757,53	2.826,46
- thereof personnel	1.590,38	2.331,97	2.690,27	2.757,53	2.826,46
other	3.040,83	2.788,08	4.295,70	3.560,48	3.738,50
Operating Costs	**16.301,28**	**15.483,95**	**18.048,29**	**18.002,57**	**19.104,22**
Cost margin	*50,1%*	*45,5%*	*31,3%*	*41,8%*	*41,3%*
EBITDA	**4.326,74**	**9.792,16**	**10.727,98**	**14.611,27**	**16.671,36**
Margin	*13,3%*	*28,8%*	*18,6%*	*33,9%*	*36,1%*
Margin rental	*64,2%*	*67,6%*	*70,0%*	*72,3%*	*72,6%*
Depreciation	70,03	217,70	251,97	287,75	316,53
Goodwill Amortisation	-	-	-	-	-
Amortisation (other)	-	-	-	-	-
EBIT	**4.256,71**	**9.574,46**	**10.476,01**	**14.323,52**	**16.354,83**
Non-Recurring Items	-	-	-	-	-
EBIT After Non-Recurring Items)	**4.256,71**	**9.574,46**	**10.476,01**	**14.323,52**	**16.354,83**
Margin	*13,1%*	*28,1%*	*18,1%*	*33,3%*	*35,4%*
Share of Net Profits	74,62	8,15	8,56	8,99	9,43
Interest Expense	5.855,06	6.413,89	6.738,00	7.531,42	6.778,28
Other Financial Income/(Expense)	-	- 6,61	- 12,00	- 12,00	- 12,00
Investment & Interest Income	355,25	25,20	150,00	152,25	154,53
Net Interest Expense	**- 5.425,20**	**- 6.387,15**	**- 6.591,44**	**- 7.382,19**	**- 6.626,31**
IFRS 40 adjustment (assets)	11.895,80	8.753,17	28.962,38	10.452,75	10.452,75
IFRS adj.(participations)	-	-	-	-	-
Deferred taxes (calculated)	3.390,30	1.095,31	5.792,48	2.090,55	2.090,55
Pre Tax Income	**10.727,31**	**11.940,48**	**32.846,95**	**17.394,08**	**20.181,27**
Taxes	1.800,00	1.494,15	6.569,39	3.478,82	4.036,25
other taxes	350,00	619,90	805,87	967,04	967,04
Tax Rate	*28,5%*	*12,5%*	*20,0%*	*20,0%*	*20,0%*
Net Income	**8.577,31**	**9.826,43**	**25.471,69**	**12.948,22**	**15.177,97**
Minority Interest	-	-	-	-	-
as % of Net	*0,0%*	*0,0%*	*0,0%*	*0,0%*	*0,0%*
booked as capital		149,42	150,00	200,00	200,00
Net Income to Common Shareholders	**8.577,31**	**9.677,01**	**25.321,69**	**12.748,22**	**14.977,97**
margin	*41,58%*	*38,29%*	*88,00%*	*39,09%*	*41,87%*
stated margin	*26,37%*	*28,44%*	*43,86%*	*29,60%*	*32,40%*
Shares Outstanding (m)	10.804,70	10.804,70	16.104,70	16.104,70	16.104,70
EPS (RG)	**0,79**	**0,90**	**1,57**	**0,79**	**0,93**
EPS (reported, incl.IFRS adjustments)					
Diluted number of shares	9.862,95	10.804,70	13.454,70	16.104,70	16.104,70
EPS (SQR, fully diluted)	**0,87**	**0,90**	**1,88**	**0,79**	**0,93**

Source: KWG, SQR estimates

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Balance Sheet Accounts

	2010	2011	2012e	2013e	2014e
Balance Sheet					
Assets					
Balance sheet total (assets)	**198.089,0**	**241.355,5**	**317.597,5**	**329.346,5**	**339.298,4**
Property/Financial assets	200.194,1	228.915,1	306.224,2	316.676,9	327.129,7
Property/Subsidiaries					
intangible assets	234,7	324,9	357,4	393,1	432,4
Investments	0,0	0,0	0,0		
Goodwill	279,2	125,0	156,2	195,3	244,1
deferred tax assets	2.807,8	3.915,3	3.915,3	3.915,3	3.915,3
other long term assets	0,0	0,0	0,0	0,0	0,0
Capital assets	**203.515,7**	**233.280,3**	**310.653,1**	**321.180,7**	**331.721,6**
percent of total B/S					
percentage change	15,1%	14,6%	33,2%	3,4%	3,3%
Properaty held for sale/inventories	75,0	107,1	100,0	100,0	100,0
Receivables (long term)	652,8	1.245,7	1.603,4	1.621,5	1.633,2
Receivables (current, for rents, leases)	0,0	0,0	0,0	0,0	0,0
Receivables (current, from sales, comms)	559,0	1.675,0	2.240,7	2.317,2	2.393,6
Total receivables	**1.286,8**	**3.027,8**	**3.944,1**	**4.038,7**	**4.126,8**
other assets	0,0	1.464,0	0,0	0,0	0,0
Current assets (excl. cash)	**1.286,8**	**4.491,8**	**3.944,1**	**4.038,7**	**4.126,8**
Cash and equivalents	9.866,1	3.583,4	3.000,3	4.127,2	3.450,0
Total current assets	**11.152,9**	**8.075,2**	**6.944,4**	**8.165,9**	**7.576,8**
Equity => manual input					
Liabilities					
Balance Sheet Total (EQ & debt)	**198.089,0**	**241.355,8**	**317.597,5**	**329.346,5**	**339.298,4**
base capital	10.804,7	10.804,7	16.104,7	16.104,7	16.104,7
capital reserves	48.993,9	40.887,2	63.412,2	63.412,2	63.412,2
retained eranings	22.380,2	39.215,1	64.653,4	77.535,4	92.653,8
minorities&others	0,0	1.673,2	0,0	0,0	0,0
Shareholders Equity	**82.178,8**	**92.580,2**	**144.170,3**	**157.052,3**	**172.170,7**
bank loans (long term)	102.184,2	104.732,9	140.223,6	135.433,6	132.725,3
convertible loans	0,0	0,0	0,0	0,0	0,0
deferred tax liabilities	7.479,5	7.021,0	12.813,5	14.904,0	14.735,6
other long term liabilities	0,0	1.068,8	0,0	0,0	0,0
Long term debt	**109.663,7**	**112.822,7**	**153.037,1**	**150.337,6**	**147.460,9**
bank loans (short term)	1.000,0	30.985,4	16.020,1	18.410,4	17.489,9
other short term loans	-	-	-	-	
Accounts payable (short term, trade)	4.218,6	2.070,0	2.277,0	1.079,8	-584,5
Advances (received cash)	0,0	98,2	0,0	0,0	0,0
tax provisions	0,0	0,0	0,0	0,0	0,0
other liabilities	1.027,9	2.799,3	2.093,0	2.466,4	2.761,4
Short term debt	**6.246,5**	**35.952,9**	**20.390,1**	**21.956,6**	**19.666,8**

Source: KWG, SQR estimates

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Author of the present financial analysis: Ralf GRoenemeyer, Head of Research and Strategy.

2.2. Sources of information and summary of the basis of valuation and the valuation methods applied during the preparation

2.2.1. Sources of information:

Essential sources of information for the preparation of this document are publications in interior and foreign media like information services (e.g., Reuters, VWD, Bloomberg, dpa-AFX, among others), business press (e.g., “Börsenzeitung” (financial paper), “Handelsblatt”, “Frankfurter Allgemeine Zeitung”, Financial Times, among others), specialized press, published statistics, rating agencies as well as publications of the analysed issuers.

All information refers to the date of the publication: [Date, time, refer to the date at the end of the disclaimer]

2.2.2. Summary of the basis of valuation and the valuation methods used during the preparation:

Within the scope of the evaluation of enterprises the following valuation methods are applied: multiplier models (stock exchange value / profit, stock exchange value / cash flow, stock exchange value / book value, Enterprise Value (EV) / turnover, EV / EBIT, EV / EBITA, EV / EBITDA), Peer Group comparisons, historic valuation methods, discounting models (DCF, DDM, EVA, RIM), Break-up-Value- and Sum-of-the-Parts-approaches, substance-valuation methods or a combination of different methods. The valuation models are dependent on economic parameters like interest rates, currencies, resources and on economic assumptions. Moreover, market moods influence the valuations of enterprises. Also, the approaches are based on expectations that may change rapidly and without advance warning according to developments specific for the respective branch. Therefore, the valuation results and fair values derived from the models may also change accordingly. The results of the evaluation basically refer to a period of 12 months. Nevertheless, they are also subjected to market conditions and constitute merely a snapshot. They may be reached faster or slower or may be scaled up or down.

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NEUTRAL: The expected yield, based on the determined target price, incl. dividend payment within the suitable time frame amounts to between -10% and <+10%.

AVOID: The expected yield, based on the determined target price, incl. dividend payment within the suitable time frame amounts to <= - 10%.

2.3. Update

A specific update of the present analysis at a firm time has currently not yet been determined. The analysis and the opinions and assessments contained therein merely reflect the perspective taken at the date stated on the first page of the analysis. Silvia Quandt Research GmbH reserves the right to make an update of the analysis or the opinions and assessments contained therein without prior notice. The decision whether and when an update is made lies solely in the discretion of Silvia Quandt Research GmbH.

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3. In their trading portfolio the aforementioned Persons and/or enterprises regularly hold financial instruments which or the issuer of which are subjected to the financial analysis.

4. The aforementioned persons and/or enterprises hold in respect of the financial instruments, which or the issuer of which are subjected to the financial analysis, a net short (short position) of at least 1 percent of the share capital of the issuer.

5. The aforementioned persons and/or enterprises supervise financial instruments, which or the issuer of which are subjected to the financial analysis, in a market by placing purchase or selling orders (Market Making/ Designated Sponsoring).

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7. The aforementioned persons and/or enterprises acted as an issuing bank or a selling agent within the scope of the listing on the stock exchange of the issuer, who or whose financial instruments are subjected to the financial analysis.

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9. The aforementioned persons and/or enterprises expect from the issuer, who or whose financial instruments are subjected to the financial analysis, during the next three months remunerations for services in connection with investment banking transactions or seek at such remunerations.

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11. This financial analysis had been made accessible for the issuer, who or whose financial instruments are subjected to the financial analysis, before publication and was modified subsequently.

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13. The aforementioned persons and/or enterprises have other important financial interests relating to the issuer, who or whose financial instruments are subjected to the financial analysis.

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2.5. Quarterly overview according to section 5 subsection 4 No. 3 FinAnV

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3.1. Issuer and notice according to section 4 subsection 4 No. 4 FinAnV about preceding publications during the last twelve months about the security or the issuer

Issuer of the analyzed finance instrument is KWG Kommunale Wohnen AG.

	1st publication	Price €	Recommendation	Target €
KWG Kommunale Wohnen AG	20.10.2009	4,25 €	Buy	7,48 €

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Company	Date of issue	Price at issue	Recommendation	Target price
KWG Kommunale Wohnen AG	14.04.2010	4,12 €	Buy	7,48 €
KWG Kommunale Wohnen AG	05.11.2010	4,58 €	Buy	7,48 €
KWG Kommunale Wohnen AG	17.02.2011	5,95 €	Buy	7,25 €
KWG Kommunale Wohnen AG	06.03.2012	5,04 €	Buy	8,00 €
KWG Kommunale Wohnen AG	07.03.2012	5,18 €	Buy	8,00 €
KWG Kommunale Wohnen AG	26.03.2012	5,53 €	Buy	8,00 €
KWG Kommunale Wohnen AG	18.04.2012	5,25 €	Buy	8,00 €
KWG Kommunale Wohnen AG	10.05.2012	5,03 €	Buy	8,00 €
KWG Kommunale Wohnen AG	23.05.2012	5,00 €	Buy	8,00 €
KWG Kommunale Wohnen AG	29.05.2012	5,17 €	Buy	8,00 €

3.4. Information about possible conflicts of interest

3.4.1. Conflict of interests of Silvia Quandt Research GmbH

2.4.1.1. Bet: >5%	2.4.1.2. Comp.	2.4.1.3. Trade	2.4.1.4. Short >1%	2.4.1.5. DS	2.4.1.6. ECM act.	2.4.1.7. IPO	2.4.1.8. Comp.Res.	2.4.1.9. Comp.ECM	2.4.1.10. Contract	2.4.1.11. Inform.	2.4.1.12. Mandate	2.4.1.13. Holding
					x							

3.4.2. Conflicts of interest biw bank für Investments und Wertpapiere AG when transmitting the financial analysis

2.4.2.1. Bet: >5%	2.4.2.2. Comp.	2.4.2.3. Trade	2.4.2.4. Short >1%	2.4.2.5. DS	2.4.2.6. ECM act.	2.4.2.7. IPO	2.4.2.8. Comp.Res.	2.4.2.9. Comp.ECM	2.4.2.10. Contract	2.4.2.11. Inform.	2.4.2.12. Mandate	2.4.2.13. Holding
		x		x	x			x				

3.5. Publication according to article 5 (4) no. 3 of the German Regulation concerning the analysis of financial instruments (Finanzanalyseverordnung):

Number of recommendations from Silvia Quandt Research GmbH in 2012	Thereof recommendations for issuers to which investment banking services were provided during the preceding twelve months
Buys: 97	35
Neutral: 50	6
Avoid: 11	0

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Frankfurt am Main, 12.06.2012

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