

KWG Kommunale Wohnen

Buy (unchanged) **Target: Euro 8.00** (unchanged)



17 | July | 12

Price (Euro)	5.05			
52 weeks range	5.80 / 4.64			
Key Data				
Country	Germany			
Industry	Real Estate			
Segment	Open Market (Entry Standard)			
ISIN	DE0005227342			
WKN	522734			
Reuters	BIWG.DE			
Bloomberg	BIW GY			
Internet	www.kwg-ag.de			
Reporting Standard	IFRS			
Fiscal Year	31/12			
Ø Daily Turnover in € (3M)	49,489			
Market Cap (EUR million)	72.7			
Number of shares (million)	14.4			
Free Float	35%			
Free Float MCap (million)	25.5			
CAGR pre tax profits 11-14e	26.4%			
Multiples				
	2011	2012e	2013e	2014e
MarketCap/ Sales	2.9	2.6	2.4	2.1
PE-Ratio	5.7	5.6	4.5	3.6
Dynamic PE-Ratio	0.21	0.21	0.17	0.14
Dividend Yield	0.0%	3.0%	4.0%	5.0%
Price-to-Book ratio	60.6%	56.7%	53.2%	50.2%
Key Data per Share (Euro)				
	2011	2012e	2013e	2014e
Earnings per Share (EPS)	0.89	0.90	1.13	1.39
Dividends per Share (DPS)	0.00	0.15	0.20	0.25
NAV per share	8.33	8.90	9.50	10.05
Financial Data (Euro '000)				
	2011	2012e	2013e	2014e
Revenues (rental income)	21,659	27,750	30,525	35,104
Net Revaluation Gains	8,535	12,060	10,080	9,590
Total operating income	25,265	28,090	30,875	35,469
Operating profit (EBITDA)	9,824	10,970	16,475	21,119
Operating Profit (EBIT)	18,359	23,030	26,556	30,709
Pre-tax profit (EBT)	11,940	16,316	19,886	24,109
Net profit (after minorities)	9,819	14,286	17,936	22,034
Adjusted Shareholders' Equity	91,494	112,780	123,716	145,750
RoE after tax	11.6%	14.0%	15.2%	16.4%
Financial Calendar				
AGM		31 Jul 2012		
1H 2012		9 Aug 2012		
SRC Forum Financials & Real Estate		12 Sep 2012		
Main Shareholders				
Group of core shareholders		65%		
Analysts				
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KWG with positive newsflow regarding expansion and refinancing conditions – Buy!

Last Wednesday, 11 July, KWG announced the signing of a Term Sheet regarding the acquisition of a 2,900-unit residential portfolio. The units are located in Berlin (approx. 600 units) and North Rhine Westphalia (approx. 2,300 units), already two of KWG's key locations and thus allowing for synergies. At an acquisition price of Euro 93m, KWG would only pay a 9.5 multiple on the current annual Net Cold Rent of the portfolio, translating into a price per sqm of Euro 460. Lettable space of the portfolio amounts to approx. 203,000 sqm and FFO-contribution is expected at about Euro 1.7m for 2013e and may increase significantly in the mid-term to about Euro 3m, according to the management. This sharp increase in rental income should be achieved via the reduction of vacancies (23%), refurbishments and adjustments to current market rents (approx. +10%). Financing for both, the purchase price and the planned refurbishments, is already secured with a German Landesbank. KWG will be able to provide the equity component from the proceeds of the last capital increase as well as from the re-leveraging of BWAG, an option that we discussed in our recent updates. We would welcome the deal at the reported conditions as it fits KWG's strategy to acquire at very low prices and lift the earnings potential via refurbishments and active asset management. As the current vacancies are concentrated at certain locations, we assume that a large portion of the portfolio could be recognized in the core portfolio immediately. Moreover, the company announced the successful refinancing of a Euro 22m loan at an average interest rate of 3.3%, more than 200bps below the replaced loans. This will lower annual interest expenses by about Euro 0.5m. Furthermore, the new interest rate will be secured for 10 years, which we also applaud due to the improved planning reliability.

As we forecasted in recent updates, KWG used its favourable cash position to quickly expand the portfolio. If the 2,900 units will be acquired at the published conditions, KWG would have achieved the desired doubling of its portfolio within the last 18 months. The most recent refinancing underlines the sound development of the firm. We confirm both our Buy rating and our Target Price of €8.00!

Strengths

SWOT – Analysis

- Management and core investors (in particular the Ehlerding family) have a broad and long-term experience in the German real estate arena.
- Excellent network and relationships combined with a proven track record will enhance further deal flow with municipalities. The BWAG deal confirmed the group's capabilities to source and close attractive deals on an ongoing basis.
- High yielding residential portfolio in fundamentally solid regions with a proven track record for active asset management and attractive acquisitions.
- Strong equity ratio of about 38% as of 1Q 2012.
- Successful expansion to the strategic goal of 10,000 units within the last 18 months if the 2,900-unit-deal will be closed within 3Q.
- Buy discipline, proven in several deals, showed the ability to buy at very attractive prices and to pay with own shares near to NAV values to avoid dilution of existing shareholders.

Weaknesses

- Small market cap of the company leads to lower visibility at investors with high investment volume. But market cap already increased with a rising portfolio size and a higher number of shares of now 14.4m shares after the successful capital increase.
- Relatively low liquidity in the KWG share due to market cap and free float.

Opportunities

- Rising cash earnings with further upside as KWG already achieved significant improvements regarding both rents and occupancy rates via comprehensive refurbishment measures within the last two years.
- Proven track record makes municipalities confident for further deals with KWG as reliable partner. This gives the chance for off-market transactions.
- The market for deals with municipalities has some future potential, due to the weak financial conditions of most municipalities. This should increase the willingness to sell municipal housing companies.
- Significant cash flow potential from the announced portfolio acquisition in Berlin and North Rhine Westphalia.
- Market recognition should increase after the announced acquisitions in Berlin and North Rhine Westphalia and the successful consolidation of BWAG in 1H.

Threats

- Funding of acquisitions and refurbishment projects could become problematic when economic conditions worsen significantly.
- Typical risks of property deals such as refurbishment costs getting out of hand. For the new acquisition, however, Capex-costs would also be financed by the lending bank.

Key facts regarding the 11 July news

As of 11 July 2012, the KWG management announced the signing of the Term Sheet regarding the planned acquisition of a 2,900-unit portfolio. Those are the key facts related to the deal that were disclosed.

- **2,910 units in total, located in Berlin (609 units) and North Rhine Westphalia (2301 units)**
- **203,000sqm of lettable space**
- **Euro 9.8m yearly Net Cold Rents**
- **9.5x multiple, resulting in a purchase price of Euro 93m**
- **460€/sqm purchase price on average**
- **Vacancy of about 23%**
- **Financing secured with a German Landesbank at undisclosed conditions including future Capex-needs**
- **FFO-contribution of Euro 1.7m expected for 2013 already**
- **NAV expected to increase by about 1€/share at initial consolidation of the portfolio.**
- **Closing announced for 3Q 2012**

Perfect match in terms of KWG's strategic focus to acquire at low prices and generate long-term value via active asset management and refurbishments.

With a large portion of the targeted portfolio located in North Rhine Westphalia, we expect significant synergies with KWG's existing portfolio properties in the region.

Medium-term goal of 10,000 units would be almost achieved with this deal. Significant cash flow impact projected upon closing.

We would applaud the closing of the deal as it offers great potential for KWG to benefit from its core competencies in active asset management and turnaround strategies for undermanaged residential portfolio.

Both the current vacancy of 23% as well as the underrent-situation of many properties in the portfolio (approx. +10% potential) allow for significant upside. Vacancy is concentrated in some objects in North Rhine Westphalia, whereas the vast majority of Berlin-based properties will be recognized in the core-portfolio immediately.

Moreover, the deal would bring KWG much closer to its strategic medium-term goal of owning about 10,000 units. This should also help to gain more attention within the listed German real estate arena and create upside momentum in the share, which still trades at a very attractive discount of about 40% to NAV.

The equity portion of the purchase price will predominantly stem from the last capital increase in 1Q as well as the successful re-leveraging of the acquired BWAG-portfolio. We hinted on the option to free up significant amounts of cash via an increase in leverage on the BWAG-portfolio in our last research updates and welcome KWG's strategy to promptly use these funds in the further expansion of the portfolio.

As the deal is not confirmed yet, we confirm our current projections excluding the impact of this significant deal. However, the deal offers great upside potential both in terms of immediate cash flow impact as well as from a long term perspective, due to its attractive conditions and the strategic match. We will adjust our projections once the deal is closed.

P&L KWG Kommunale Wohnen AG

31/12 IFRS (Euro '000)	2008	2009	2010	2011	2012e	2013e	2014e	CAGR '11 - '14e
Revenues	13,706	19,759	19,765	21,659	27,750	30,525	35,104	17.5%
↳ thereof rental income from properties	8,711	19,759	19,765	18,053	27,280	30,220	34,753	
↳ thereof rental income without costs of material	3,716	12,423	13,529	11,040	19,660	23,720	28,353	
Other oper. Income	4,211	224	263	3,606	340	350	365	
Total operating income	17,917	19,983	20,028	25,265	28,090	30,875	35,469	
Expenses for investment properties	-3,856	-3,653	-2,999	-3,351	-4,550	-3,300	-3,200	
Cost of material	-4,995	-7,336	-6,236	-7,013	-7,620	-6,500	-6,400	
Net operating income (NOI)	4,855	8,770	10,530	11,295	15,580	20,725	25,504	
NOI-margin	35.4%	44.4%	53.3%	52.1%	56.1%	67.9%	72.7%	
Personnel expenses	-1,377	-1,488	-1,773	-2,323	-2,450	-2,500	-2,650	
Other operating expenses	-5,284	-2,334	-1,866	-2,754	-2,500	-2,100	-2,100	
Operating profit (EBITDA)	2,405	5,172	7,154	9,824	10,970	16,475	21,119	29.1%
EBITDA margin	17.5%	26.2%	36.2%	45.4%	39.5%	54.0%	60.2%	
Amortization of intangible assets and depreciation of property, plant and equipment and investment properties	-49	-103	-173	-218	-190	-220	-260	
Revaluation gains	3,015	3,961	9,602	8,753	12,250	10,300	9,850	
Operating profit (EBIT)	5,372	9,030	16,583	18,359	23,030	26,556	30,709	18.7%
EBIT margin	30.0%	45.2%	82.8%	72.7%	82.0%	86.0%	86.6%	
Income from securities in financial assets	68	0	0	8	50	50	50	
Other interest and similar income	432	72	26	25	300	450	600	
Interest and similar expenditure	-4,897	-5,865	-5,861	-6,445	-7,010	-7,120	-7,250	
Minority interests of other shareholders	-6	-2	-6	-7	-55	-50	0	
Pre-tax Profit (EBT)	969	3,235	10,742	11,940	16,316	19,886	24,109	26.4%
EBT margin	7.1%	16.4%	54.4%	55.1%	58.8%	65.1%	68.7%	
tax expenses and other expenses	-197	87	-2,158	-2,114	-2,005	-1,915	-2,030	
Tax rate	20.3%	15.8%	7.5%	17.7%	12.3%	9.6%	8.4%	
Minorities	0	0	-1	-7	-25	-35	-45	
Net Profit after minorities	772	3,322	8,583	9,819	14,286	17,936	22,034	30.9%
Return on sales	5.6%	16.8%	43.4%	45.3%	51.5%	58.8%	62.8%	
Number of shares (at year-end, '000)	7,490	8,627	10,805	10,805	15,881	15,881	15,881	
Earnings per share (Euro)	0.10	0.39	0.87*	0.89	0.90	1.13	1.39	
EPS above CoE (8.0%)	-0.41	-0.18	0.29	0.28	0.39	0.53	0.71	
Dividends per Share (DPS) in Euro	0.00	0.00	0.00	0.00	0.15	0.20	0.25	
NAV per share in Euro	6.53	6.59	7.23	8.33	8.90	9.50	10.05	
Adjusted Shareholders' Equity without minorities	56,143	64,735	78,099	91,494	112,780	123,716	145,750	16.8%
RoE after Tax	1.6%	5.5%	12.0%	11.6%	14.0%	15.2%	16.4%	
Key ratios & figures	2008	2009	2010	2011	2012e	2013e	2014e	
Growth rates in %								
Revenues	354.0%	44.2%	0.0%	9.6%	28.1%	10.0%	15.0%	
EBITDA	-29.8%	115.0%	38.3%	37.3%	11.7%	50.2%	28.2%	
EBIT	58.3%	68.1%	83.6%	10.7%	25.4%	15.3%	15.6%	
EBT	-63.3%	234.0%	232.0%	11.2%	36.6%	21.9%	21.2%	
Net profit after minorities	-75.1%	330.5%	158.4%	14.4%	45.5%	25.5%	22.9%	
Margins in %								
Gross								
EBITDA	13.4%	25.9%	35.7%	38.9%	39.1%	53.4%	59.5%	
EBIT	30.0%	45.2%	82.8%	72.7%	82.0%	86.0%	86.6%	
EBT	7.1%	16.4%	54.4%	55.1%	58.8%	65.1%	68.7%	
Expense ratios in %								
Personnel costs quote	7.7%	7.4%	8.9%	9.2%	8.7%	8.1%	7.5%	
Cost of material to sales	27.9%	36.7%	31.1%	27.8%	27.1%	21.1%	18.0%	
Depreciation to sales	0.3%	0.5%	0.9%	0.9%	0.7%	0.7%	0.7%	
Tax rate	20.3%	15.8%	7.5%	17.7%	12.3%	9.6%	8.4%	
Profitability in %								
Net profit to sales ratio	5.6%	16.8%	43.4%	45.3%	51.5%	58.8%	62.8%	
Return on equity (ROE) after tax	1.6%	5.5%	12.0%	11.6%	14.0%	15.2%	16.4%	
Valuation								
PE-ratio	49.01	13.11	5.80	5.67	5.61	4.47	3.64	
Price/BVpS	6.53	6.59	7.23	8.33	8.90	9.50	10.05	
Dividend yield in %	0.0%	0.0%	0.0%	0.0%	3.0%	4.0%	5.0%	
EV/ Sales	4.06	3.64	3.63	2.88	2.59	2.36	2.05	
EV/ EBITDA	30.23	14.06	10.16	7.40	6.63	4.41	3.44	
Data per share								
Number of shares in k	7,490	8,627	10,805	10,805	15,881	15,881	15,881	
EpS	0.10	0.39	0.87*	0.89	0.90	1.13	1.39	
DpS	0.00	0.00	0.00	0.00	0.15	0.20	0.25	
BVpS	6.53	6.59	7.23	8.33	8.90	9.50	10.05	

* EPS with average number of shares of 9.857 million shares

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Rating Chronicle	Date	Rating	Former Price	Former Target
KWG	15-May-12	Buy	5.00 €	8.00 €
KWG	18-Apr-12	Buy	5.24 €	8.00 €
KWG	7-Mar-12	Buy	5.18 €	8.00 €
KWG	1-Mar-12	Buy	5.05 €	7.50 €
KWG	9-Nov-11	Buy	4.99 €	7.50 €
KWG	25-Aug-11	Buy	5.16 €	7.50 €
KWG	12-Jul-11	Buy	4.61 €	7.50 €

Please note:

The KWG share price mentioned in this report is from closing of 16 July 2012.
KWG mandated SRC Research for mentoring the KWG share.

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