



22 | March | 2019

■ **Price (Euro)** **4.90**
52 weeks range 5.06 / 3.75

■ **Key Data**

ISIN DE000A0XFSF0
Bloomberg DMRE:GR
Reporting standard IFRS
Market Cap (Euro million) 528
Number of shares (million) 107.8
Free Float 11.4%
Free Float Market Cap (Euro million) 60
CAGR EBT ('17-'20e) 30.7%

■ Multiples	2018	2019e	2020e	2021e
Market Cap/ Total revenues	7.2	6.6	5.4	4.5
PE-Ratio	8.6	8.9	11.6	10.4
Dividend Yield	0.0%	0.0%	0.0%	0.0%
Price-to-Book-Ratio	0.98	0.87	0.80	0.73
P/ NAV-ratio	0.89	0.81	0.75	0.68

■ Key Data per share (Euro)	2018	2019e	2020e	2021e
Earnings per share (EPS)	0.57	0.55	0.42	0.47
Dividend per share (DPS)	0.00	0.00	0.00	0.00
Book Value per Share (BVPS)	4.99	5.65	6.15	6.74
EPRA NAV per share	5.50	6.07	6.55	7.16

■ Financial Data (Euro '000)	2018	2019e	2020e	2021e
Rental income	73,709	80,147	98,142	116,287
Net revaluation result	93,059	65,214	46,823	43,589
Operating profit (EBIT)	127,065	108,215	101,935	111,571
Net financial result	-38,308	-37,177	-40,244	-43,311
Pre-tax profit (EBT)	88,757	71,038	61,691	68,260
Taxation	-19,704	-1,018	-1,254	-1,490
Net profit after minorities	61,575	67,603	58,262	64,837
FFO I after tax	23,359	30,426	37,673	44,920
Shareholders' equity (Euro million)	582	727	887	966
Property portfolio (Euro million)	1,130	1,525	1,813	2,079
RoE (after tax)	13.7%	10.3%	7.2%	7.0%
Equity ratio (incl. equity minorities)	42.2%	42.2%	40.2%	39.1%

■ **Main Shareholders**

Apollo 64.1%
Wecken-Group 24.5%

■ **Financial calendar**

1Q 2019 report 15 May 2019
AGM 29 May 2019
1H 2019 report 14 August 2019

■ **Analysts**

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FFO doubled and bottom line up 4.5 times – Portfolio value lifted following high revaluation result – we expect significant portfolio growth to come – new rating Accumulate

On Wednesday, the company released the 2018 annual report and invited to a conference call. The numbers showed some significant hikes. Rental income came in at almost Euro 74m, remaining stable compared to last year, at the top end of the firm's guidance. The lowered rental income from the sale of non-strategic properties was therefore made up by a 2.9% like-for-like rental growth driven by a successful letting performance. The valuation result was at more than Euro 93m in 2018, of which about 50% come from improved portfolio KPI's and the other half results from yield compression. This led to an EBIT of more than Euro 127m, up 50% compared to last year's number of Euro 85m. The financial result significantly improved due to the refinancing activities in 2017 and come down from Euro -57m to Euro -38m. The firm's pre-tax profit thus was at almost Euro 89m more than threefold the amount of the previous year's result of almost Euro 28m. The bottom line after minorities was at almost Euro 62m 4.5 times last year's result of almost Euro 14m. This translates into earnings per share of 85 cents. The FFO result doubled as well and was up from almost Euro 12m last year to more than Euro 23m. This significant increase was driven by the already mentioned lower interest expenses, by the operational performance and by lower than expected capex spending.

The value of the portfolio stands at Euro 1.13bn at year end 2018 (FY 2017: Euro 1.03bn) with a gross rental income of more than Euro 73m and WALT of 4.5 years. Not included are the four newly acquired objects with an investment volume of Euro 167m, as these have not been closed yet. The EPRA vacancy rate came down from 9.4% to 7.5%. The firm's financial debt came down from Euro 695m to Euro 637m, mainly following the conversion of the convertible bond and the first time application of IFRS 9. Along with the increase in the portfolio value and the capital increase, this resulted in a significant reduction of the net LTV from 60% to 39%. The diluted EPRA NAV per share is at Euro 5.50 at year-end, up more than 11% year over year.

For 2019 the company expects rental income in a range of Euro 77m to Euro 79m and an FFO between Euro 27m and Euro 29m. As these numbers do not consider any new additions to the portfolio in 2019, our estimates are on top of the firm's guidance at a rental income of more than Euro 80m and a FFO of more than Euro 30m. The company has Euro 74m of cash at year-end 2018 and thus should be able to further extend the portfolio in 2019, following the strategic goal to significantly lift the portfolio to Euro 2bn in the medium term. **At the moment the portfolio growth is lagging a bit behind our expectations, but we believe the company will compensate in 2019. Until then, we confirm our target price of Euro 5.40. As the share has already gained about 14% YTD and is getting closer to our target price, we reduce our rating from Buy to Accumulate.**

DEMIRE Deutsche Mittelstand Real Estate AG

Industry:	Real Estate	Management Board of DEMIRE AG:
Sub-segment:	Office / Retail / Logistics	Ingo Hartlief FRICS (CEO)
Region:	Germany	Tim Brückner (CFO)
Headquarter:	Frankfurt am Main	
Foundation	2006	
Employees: (31.12.2018)	75	Supervisory Board of DEMIRE AG:
		Prof. Dr. Alexander Goepfert (Chairman)
IR Contact:		Frank Hölzle (Vice Chairman)
Peer Schlinkmann		Dr. Thomas Wetzel
schlinkmann@demire.ag		

DEMIRE Deutsche Mittelstand Real Estate AG acquires and manages high quality commercial real estate properties. The firm was originally founded in April 2006 as MAGNAT Real Estate Opportunities, focusing their business activities on real estate markets in Eastern Europe and the Black Sea region. In 2013 however, the company changed their strategic alignment and further changed their name to DEMIRE Deutsche Mittelstand Real Estate AG. Since then, the focus has been shifted on office, retail and logistics properties in secondary locations across Germany, such as mid-sized cities and boardering areas to metropolitan cities. The company follows a strategy that combines a stable income creating Core+ portfolio (55%) with value-add properties (40%) to create rental growth opportunities due to a "manage-to-core" strategy, and redevelopments (5%) due to extensions, refurbishments and selective developments.

The company currently holds a diversified portfolio with a total rental space of more than 900,000 sqm and a portfolio value of Euro 1.13bn as of FY 2018. The portfolio is diversified within the commercial segment. Currently, about 68% of the portfolio in terms of Gross Asset Value is concentrated in 68 % offices, 23% in retail properties, 6% in the logistics segment and about 3% in others. The largest share of the portfolio is located in the state of North Rhine-Westphalia, where almost 19% of the portfolio is held. During 2017, the company further followed its transformation strategy and sold some of the non-core assets from the old portfolio. For 2019 we expect significant additions to the portfolio and some minor disposals as currently Euro 12m of properties are held for sale.

The average maturity of rental contracts amounts to c. 4.5 years with a vacancy rate of 7.5 as of year-end 2018. Among tenants are various well-known and successful brands like Telekom, Sparkasse, Comdirect Bank, and Zapf. Except the 30.4% share of GMG (Telekom), the remaining tenants from the top 10 list make up for not more than 3% each. This represents a well diversified income structure. Average gross rental yield is at 6.5%. Office properties have a yield of 6.4% as compared to retail at 6.6% and logistics at 6.7%.

INVESTMENT STRATEGIES in % of portfolio market value

- 54.6 Core plus
- 40.6 Value-added
- 4.8 Redevelopment



(Status: 31/12/2018)

Since 15 July 2016, DEMIRE is trading in the Prime Standard segment in Frankfurt. That segment requires the highest level of transparency of all segments at the Frankfurt Stock Exchange and even in Europe.

Source: Company Data, SRC Research

An eventful FY 2018 is in the books with many organizational changes

In February 2018 the company announced a 10% equity capital hike by the issue of more than 5.4m new shares. The capital increase was fully subscribed by the new strategic investor, Apollo Managed Funds, and was completed in April. The issue price was set at Euro 4.35 per share for gross proceeds of almost Euro 24m. Apollo furthermore entered into a cooperation agreement with Wecken & Cie. Together, the two investors have acquire control of the company and accordingly had announced a mandatory tender offer to all shareholder of DEMIRE for a price of Euro 4.35.

On 13 November 2018, DEMIRE reported on the successful completion of an equity capital hike. About 55% of the subscription rights were exercised, the remaining shares were picked up by Apollo, who now holds more than 64%. The capital hike resulted in gross proceeds of Euro 150m, which are to be used to expand the portfolio by about Euro 350m.

On 20 December 2018, the company announced the expansion of the firm's Executive Board with the appointment of Mr. Ingo Hartlief, FRICS, as the new CEO. His former positions include Vice CEO & COO of CORPUS SIREO Real Estate, CEO of Swiss Life KVG and Managing Director of Union Investment Real Estate.

On 17 January 2019, the firm's Supervisory Board appointed Tim Brückner as new CFO of the company. His former positions include corporate finance and M&A positions at ING BHF-Bank and HSBC Bank, an executive role at Rothschild International investment bank and most recently as Managing Director at CORPUS SIREO Real Estate.

We believe the two experienced and knowledgeable managers should provide the company with the required skills and a strong network to further grow the company and to reach the targeted strategic goals. Along with the support of Apollo and the capital, the company should be able to deliver some strong portfolio growth in 2019.

Overview of Top 20 Assets

Top 20 Properties as of 31/12/2018

	City	Asset Class	Cluster	GAV (€ m)	Share (%)	Space ('000 sqm)	EPRA Vacancy ⁽¹⁾ (%)	GAV/sqm (€)	GRI p.a. ⁽²⁾ (€ m)	GRI Yield (%)	WALT (Years)
1	Bonn	Office	Core+	87.9	7.9%	38,353	-	2,339	5.6	6.3%	6.2
2	Ulm	Office	Core+	77.6	7.1%	47,527	0.8%	1,690	4.3	5.4%	5.9
3	Rostock	Retail	Core+	68.9	6.2%	19,306	3.0%	3,657	4.4	6.2%	3.8
4	Leipzig	Logistic	Value-Add	64.5	5.8%	178,283 ⁽³⁾	12.9%	367	4.4	6.7%	1.6
5	Kassel	Retail	Core+	59.0	5.4%	21,508	5.8%	2,841	3.5	5.7%	7.4
6	Freiburg	Office	Redevelopment	39.4	3.7%	22,674	-	1,821	2.7	6.6%	2.2
7	Regensburg	Office	Value-Add	34.8	3.2%	29,219	-	1,256	2.6	7.0%	2.2
8	Düsseldorf	Office	Value-Add	34.2	3.0%	24,307	23.0%	1,415	2.0	5.8%	4.1
9	Leipzig	Office	Value-Add	32.7	2.9%	23,260	5.0%	1,406	1.8	5.4%	3.4
10	Eschborn	Office	Core+	31.0	2.7%	18,889	-	1,641	2.0	6.5%	6.0
Top 10 Properties				543.3	48.1%	423,326	4.9%	1,283	33.3	6.1%	4.4
11	Eisenhüttenstadt	Retail	Value-Add	28.5	2.5%	29,169	23.9%	977	2.3	8.1%	5.9
12	Lutherstadt Wittenberg	Retail	Core+	23.7	2.1%	14,710	4.5%	1,611	1.7	7.1%	5.2
13	Unterschleißheim	Office	Value-Add	23.2	2.1%	15,663	31.5%	1,481	1.0	4.5%	2.7
14	Flensburg	Office	Value-Add	21.4	1.9%	23,800	-	899	1.7	8.0%	2.2
15	Zittau	Retail	Core+	21.3	1.9%	17,421	4.3%	1,223	1.3	6.2%	10.5
16	Köln	Office	Core+	17.6	1.6%	9,108	-	1,932	1.0	5.6%	1.0
17	Quickborn	Office	Core+	17.3	1.5%	10,570	0.5%	1,637	1.2	7.1%	3.4
28	Stahnsdorf	Office	Value-Add	17.3	1.5%	17,110	-	1,011	1.9	11.2%	2.2
19	Neumünster	Office	Value-Add	16.9	1.5%	11,808	1.5%	1,431	1.1	6.3%	6.9
20	Langen	Office	Value-Add	16.5	1.5%	13,681	31.5%	1,206	1.0	6.1%	3.1
Top 20 Properties				747.0	66.1%	586,367	7.2%	1,274	47.6	6.4%	4.4
Other Properties				383.4	33.9%	340,094	8.0%	1,127	25.6	6.7%	4.6
Total Properties				1,130.4	100.0%	926,461	7.5%	1,220	73.2	6.5%	4.5

Source: Results presentation FY 2018

Even though the growth of the portfolio in terms of new acquisitions remained behind our expectations for 2018, many objects in the portfolio showed some clear improvements. Some significant vacancy reductions were achieved e.g. in the logistics object in Leipzig from 33.5% to 12.9%, in Düsseldorf from 29% to 23% and in Unterschleißheim from 36.9% to 31.5%. This also corresponded to some significant value uplifts such as a 23% value increase in Unterschleißheim near Munich, a 19% hike in the Gutenberggalerie Leipzig and a 13% increase in Ulm.

In terms of valuation we still see a lot of upside potential in the current portfolio. The average value per sqm is at Euro 1,220 still very low and offers further upside. With the high liquidity and further capital hikes to come, we believe that DEMIRE will report some significant acquisitions in 2019. The first step in that direction was already done by the acquisition of the four office buildings with a total investment volume of Euro 167m that were reported in November and will be closed in 2Q 2019.



Total investment volume of € 167m

Closing expected in Q2 2019



Funding via Capital Increase in November 2018

Attractive indicative financing terms, well below current average cost of debt



Initial rental income: c. € 8m

Initial FFO contribution: c. € 3m



Source: results presentation FY 2018

SWOT Analysis

Strengths

- The Management is highly senior, experienced and well-known in the German real estate sector.
- The transformation of the company has well proceeded since the change in strategy in 2013 and now has a clear focus and targets for the coming years.
- The current portfolio is well diversified between asset classes and regions and therefore has no cluster risks in that regard.

Weaknesses

- The firm's current free float of the share is at about 11% very low, which limits the tradability and liquidity of the share. The free float should be increased with possible upcoming capital hikes in 2019 and following years, however.
- DEMIRE still lacks reputation in the market, which leads to a discount in their share price. As the firm gains more popularity and awareness with investors we see this current weakness turning into an opportunity to close the current gap to NAV.

Opportunities

- DEMIRE currently follows the strategic plan "DEMIRE 2.0". Thereby the company aims to double the size of the portfolio, reduce their financing costs and make use of economies of scales in the portfolio. The strategic plan sounds very promising and, if accomplished, could lead to lucrative earnings in the midterm future. DEMIRE is on a very good way to deliver on the goals.
- DEMIRE could reach better financing conditions as they reach a better standing and they grow their portfolio and strengthen their balance sheet. The firm has already significantly lowered its cost of debt to currently 3%, but still has room to improve. A rating upgrade to investment grade, which is targeted by the firm, should significantly help that cause.
- The firm still has a lot of upside potential in their current portfolio due to revaluation gains. There are many objects that are still significantly below the potential value. The company can help realize that potential by improving their portfolio e.g. by reducing vacancy rates and other measures.
- The focus on secondary cities still offer lucrative yields compared to the Top7 locations and good opportunities to find lucrative deals with value add potential that will drive the company's operations and thus the share.

Threats

- The largest tenant in the portfolio, Deutsche Telekom, currently makes up for about 30% of gross rental income, which could lead to a significant reduction in rental income if problems were to arise. However, Deutsche Telekom is a large company with a long history and therefore a good tenant to have. Furthermore, the exposure is split over 28 different lease contracts and over 18 properties with lease maturities spreading until 2025 and a high WALT of more than 4 years.
- The company follows a "manage-to-core" strategy in their Value-Add portfolio and further has some redevelopment objects in their portfolio. Problems regarding the improvements of the objects could lead to higher than expected costs.
- A change in European monetary policy by the ECB regarding the termination of the currently all-time low-interest period could result in a relatively high increase of interest expenses and might also lead to higher expenses for DEMIRE. We currently do not see any drastic changes in the near future however and the company has also already locked in some long term financing at good rates.

DEMIRE Deutsche Mittelstand Real Estate AG 31/12 IFRS ('000)	2016	2017	2018	2019e	2020e	2021e	CAGR '18 - '21e
Rental income	76,371	73,716	73,709	80,147	98,142	116,287	16.4%
Income from utility and service charges	15,746	14,624	15,101	16,029	19,628	23,257	
Operating and ancillary costs	-33,547	-32,708	-30,310	-32,860	-40,238	-47,678	
Profit/loss from the rental of real estate	58,570	55,632	58,500	63,316	77,532	91,867	16.2%
Revenue from the sale of real estate companies	7,471	0	0	0	0	0	
Net assets from real estate companies sold	-3,510	0	0	0	0	0	
Profit/loss from the sale of real estate companies	3,961	0	0	0	0	0	
Revenues from the sale of real estate	21,966	28,389	1,052	7,514	3,264	1,245	
Expenses relating to the real estate sales	-21,003	-27,445	-1,002	-7,125	-3,147	-963	
Profit/loss from the sale of real estate	963	944	50	389	117	282	
Profits from investments accounted for using the equity method	0	73	0	0	0	0	
Losses from investments accounted for using the equity method	-359	0	0	0	0	0	
Unrealised fair value adjustments in equity investments	0	0	0	0	0	0	
Profit/loss from investments accounted for using the equity method	-359	73	0	0	0	0	
Profit/loss from fair value adjustments in investment properties	38,414	48,560	93,059	65,214	46,823	43,589	
Impairment of receivables	-2,058	-2,763	-1,874	-214	-547	-314	
Profits originating from a purchase below market value	0	0	0	0	0	0	
Other operating income	5,550	5,052	2,513	3,147	3,748	2,981	
Other operating income and other effects	41,906	50,849	93,698	68,147	50,024	46,256	-21.0%
General and administrative expenses	-14,505	-15,304	-19,007	-16,796	-17,145	-18,358	
Other operating expenses	-7,367	-7,523	-6,176	-6,841	-8,593	-8,476	
Earnings before interest and taxes (EBIT)	83,169	84,671	127,065	108,215	101,935	111,571	-4.2%
Financial income	1,153	940	480	1,269	1,341	1,413	
Finance expenses	-39,134	-49,703	-26,415	-32,475	-36,258	-40,041	
Interest of minority shareholders	-5,226	-8,279	-12,373	-5,971	-5,327	-4,683	
Financial result	-43,207	-57,042	-38,308	-37,177	-40,244	-43,311	
Profit/loss before taxes (EBT)	39,962	27,629	88,757	71,038	61,691	68,260	-8.4%
Income taxes	-12,313	-8,197	-19,704	-1,018	-1,254	-1,490	
Tax rate	31%	30%	22%	1%	2%	2%	
Net profit/loss	27,649	19,432	69,053	70,020	60,437	66,770	
Minorities	-2,979	-5,649	-7,478	-2,417	-2,175	-1,933	
Net profit/loss after minorities	24,670	13,783	61,575	67,603	58,262	64,837	
FFO I after tax	13,019	11,738	23,359	30,426	37,673	44,920	24.4%
FFO per share	0.24	0.22	0.32	0.25	0.27	0.33	
Number of shares ('000)	54,247	54,271	107,777	122,589	138,174	138,174	
Earnings per share (EPS)	0.39	0.25	0.57	0.55	0.42	0.47	
Dividend per share (DPS)	0.00	0.00	0.00	0.00	0.00	0.00	
in % of FFO result	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	
Shareholders' Equity (without minorities)	271,945	285,417	537,913	692,147	849,476	930,805	43.8%
Shareholders' Equity (including minorities)	308,637	319,101	582,338	727,147	887,372	965,586	
EPRA NAV	300,459	323,572	595,225	744,569	904,634	988,947	40.9%
Balance Sheet sum	1,094,006	1,147,116	1,378,692	1,722,547	2,205,318	2,469,269	
Equity Ratio	28.2%	27.8%	42.2%	42.2%	40.2%	39.1%	
RoE (after tax)	8.6%	4.4%	13.7%	10.3%	7.2%	7.0%	18.0%
Property portfolio	981,274	1,034,100	1,130,400	1,524,783	1,812,589	2,079,025	
Book Value per share (Euro)	5.01	5.26	4.99	5.65	6.15	6.74	5.3%
EPRA NAV per share (Euro)	4.60	4.94	5.50	6.07	6.55	7.16	9.8%

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Rating chronicle:

Company	Date	Rating	former share price	former target
DEMIRE	18 January 2019	Buy	4.54 €	5.40 €
DEMIRE	20 December 2018	Buy	4.27 €	5.40 €
DEMIRE	15 November 2018	Buy	4.30 €	5.40 €
DEMIRE	2 November 2018	Buy	4.18 €	5.10 €
DEMIRE	16 August 2018	Buy	4.17 €	5.10 €
DEMIRE	1 June 2018	Buy	4.38 €	5.10 €
DEMIRE	3 May 2018	Buy	4.36 €	5.10 €
DEMIRE	27 February 2018	Buy	3.91 €	5.10 €
DEMIRE	1 February 2018	Buy	3.74 €	5.10 €

Please note:

The share price mentioned in this report is from 21 March 2019. DEMIRE Deutsche Mittelstand Real Estate AG mandated SRC Research for covering the share.

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