

publity

Back on track

In FY18, publity managed to post a rebound from the weak FY17, with an almost 50% y-o-y increase in revenues, PBT and net income (close to record-high FY16 figures). The company has also been moving closer to resolving its dispute with convertible bondholders, with a new share issue and partial bond repurchase that will continue in FY19. As the covenant limiting the increase in financial liabilities beyond €5m was recently waived, publity continues to review options for a potential new bond issue, which would support further business development, including further property purchases by publity Investor GmbH.

High transaction activity supporting earnings

Even though AUM in FY18 remained flat at €4.6bn, publity recorded a 46.7% y-o-y increase in sales to €34.6m. This was driven by both recurring revenue and finder's fees from asset acquisitions and participation in disposal gains. It translated into similar improvements in PBT (up 48.4% y-o-y) and net income (up 47.8%). However, as the company issued 3.78m new shares last year, the dilutive effect outweighed the increase in profits, resulting in a 9.1% y-o-y EPS decline. Management also expects that AUM in FY19 will remain stable, which should result in only a slight EBIT increase according to the company.

Office demand in Germany remains solid

The imbalance between demand and supply for office space persists in the big seven German cities, which drives vacancy rates down and rents up. The unleased area in the attractive locations is almost exhausted, which limits further increase in take-up. Robust market conditions coupled with high liquidity from foreign investors supported growth in investment volumes by 18% in 2018. Due to limited capacity and increase in development and construction costs, there is a possibility that this trend will not be reversed in the near future, limiting further development in prime locations in the big seven cities and opening up opportunities class B locations.

Valuation: Trading close to peers

The company's shares are trading at a 16.4% premium and a 1.4% discount to the peer group on FY19e and FY20e P/E consensus estimates, respectively. The company has announced that it intends to pay a dividend from FY18 income at €1.5 per share, which translates into a dividend yield of c 6.0%.

Consensus estimates						
Year end	Revenue (€m)	PBT (€m)	EPS (€)	DPS (€)	P/E (x)	Yield (%)
12/17	23.6	14.6	1.67	0.0	16.9	N/A
12/18	34.6	21.6	1.52	1.5	18.6	5.3
12/19e	38.5	N/A	2.04	0.0	13.8	N/A
12/20e	44.3	N/A	2.45	0.0	11.5	N/A

Source: publity accounts, Refinitiv consensus as at 16 April 2019, based on forecasts of one analyst

Real estate asset management

18 April 2019

Price €28.2
Market cap €277m

Share price graph



Share details

Code	PBY
Listing	Deutsche Börse Scale
Shares in issue	9.8m
Last reported net debt at 31 December 2018	€21m

Business description

publity is an asset manager with a focus on German office buildings. It has an 18-year track record as an investor in commercial real estate in larger German cities and manages a portfolio worth €4.6bn.

Bull

- Experienced player with a focus on one segment of the property market.
- New asset management mandates with institutional investors.
- Strong demand in the German office market.

Bear

- Limited AUM growth potential.
- Dependent on banks for property sourcing.
- Funding risk associated with convertible bonds.

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Financials: Lower EPS despite rebound in net income

In FY18, pubilty recorded a c 50% increase in revenues, PBT and net income, reaching €34.6m, €21.6m and €14.9m respectively, which was achieved despite assets under management (AUM) remaining flat compared to FY17 at €4.6bn. The top-line increase was driven by recurring revenue, but also transaction-related income, including finder's fees in conjunction with asset acquisitions and participation in disposal gains of properties within the asset management mandates. An example of the large transactions finalised last year is the sale of four office properties to Demire Deutsche Mittelstand Real Estate concluded in November 2018, as well as two other sizeable disposals completed earlier in 2018. Revenues in the asset management segment almost doubled in FY18 as they reached €29.8m compared with €15.5m in the preceding period.

The published figures stand close to the lower end of the latest management guidance published in December 2018. The company's expectations were for a 50–70% annual growth rate across sales, EBIT and net income, which would imply a net income in the range of €15–17m. Despite the above-mentioned earnings improvement, pubilty's EPS decreased by 9.1% y-o-y to €1.52. This was due to the issue of 3.8m new shares completed in October 2018 (see our detailed comment below). As per management guidance, the company's results are expected to record only a slight increase in 2019 based on the assumption that AUM will remain stable throughout the period.

Exhibit 1: Financial highlights

€000s, unless otherwise stated	FY18	FY17	y-o-y change
Revenue	34,583	23,571	46.7%
Cost of materials	(5,804)	(3,314)	75.1%
Personnel expenses	(1,670)	(1,974)	-15.4%
Other operating expenses	(6,911)	(7,160)	-3.5%
D&A	(166)	(196)	-15.3%
Income from profit transfer	1,005	1,160	-13.4%
EBIT	21,037	12,087	74.0%
<i>EBIT margin (%)</i>	<i>60.8%</i>	<i>51.3%</i>	<i>955bp</i>
PBT	21,624	14,576	48.4%
Income tax and other taxes	(6,721)	(4,490)	49.7%
Net income	14,902	10,086	47.8%
<i>Net margin (%)</i>	<i>43.1%</i>	<i>42.8%</i>	<i>30bp</i>
EPS (€)	1.52	1.67	-9.1%

Source: pubilty accounts, Edison Investment Research

Balance sheet

The main changes in the company's balance sheet reflect the strategic decision to develop pubilty Investor GmbH (pubilty's fully owned subsidiary) as its own investment vehicle acquiring attractive office real estate located in the largest German cities. Last year, pubilty invested €20m in the entity, which increased its investments in subsidiaries to €20.8m (compared with €0.9m in FY17). This position also includes pubilty AG's stake in pubilty Performance GmbH and pubilty Emissionshaus GmbH.

Another important development in FY18 was the capital increase concluded in October, with gross proceeds amounting to €40.5m. The purpose of the issue was to strengthen the capital base to fund future growth. However, the offering was also associated with ongoing discussions with the convertible bonds holders related to an alleged covenant breach in relation to the dividend payout ratio (see our previous [update notes](#) for a detailed discussion). During the negotiations, one of the conditions highlighted by some bondholders was that pubilty should raise additional equity. Thomas Olek, the CEO and sole shareholder of TO-Holding GmbH, committed to subscribe to all new shares not subscribed to by other investors and, as a result, he acquired the majority of shares offered (more than 80%, according to our estimate). In conjunction with the subsequent (and still ongoing) high-volume director's dealing activity, his stake in the company stands at c 70%.

Meanwhile, the company has repurchased some of the convertible bonds and, as a result, the balance declined to €46.95m at the end of FY18 compared with €50.0m in FY17. According to management, an additional €10.0m may be redeemed before 1 July 2019 based on agreement with one of the bondholders. As a consequence of all the above, publity's cash position improved from €8.0m in FY17 to €26.0m at end-2018.

Following the strengthening of the capital base, publity has initiated some 'market sounding' initiatives in conjunction with the potential placement of a new bond. In this context, in March 2019, publity was able to obtain the approval of convertible bondholders to waive one of the bond's covenants, according to which publity cannot increase its financial liabilities by more than €5m. In return, the bondholders were granted the right to redeem part or all of their bonds, plus any accrued interest, in the case of an increase in liabilities by more than €5m. With the right to take up new financial liabilities, the company will continue its ongoing review of options for a potential new financing in the debt markets, announced on 28 January 2019.

Nevertheless, it is important to note the possibility that another dispute with bondholders may emerge, as some consider the significant increase in stake owned by Thomas Olek as a result of last year's share issue a breach of the covenant related to a change of control in the company.

Vacancy rates exhausting any downward potential

Corporate demand for office space in Germany remains solid in a still favourable macroeconomic environment despite signs of slowdown seen recently. Transaction volumes in the real estate market increased by 5.2% in 2018 to reach €61.1bn, 63% of which were generated in the big seven cities. However, Zentraler Immobilien Ausschuss (ZIA) expects this amount to fall slightly in 2019. The office segment still dominates the real estate investments spectrum with a share of 47.1% in 2018, ahead of the five-year average of 45.2%. Office investment volumes in Germany recorded an above average improvement of 18% y-o-y. Even though the office take-up decreased by 6.5% in Q418, it still remains at high levels and is fully attributable to the scarce supply of new office space. According to JLL, total office take-up, in the big seven cities only, fell just short of 4m sqm, which constitutes the second-best all-time result (behind 2017). Following a decrease by 1.1pp since end-2017, the vacancy rate in the big seven cities at end-2018 stood at 3.6%, including 2% in Berlin, 2.2% in Stuttgart and less than 3% in Munich.

Importantly, the robust office real estate market is not accompanied by a sufficient volume of newbuild space. Even though office completions in 2018 increased by almost 8% y-o-y to 927k sqm, this number is below the previous market forecasts due to significant delays, caused by limited capacity, and increase in development and construction costs. JLL expects that only 1.68m sqm of new office space will be completed in 2019, instead of the 1.8m sqm planned by developers. Similarly, in 2020 completions should reach 2.1m sqm instead of the previously projected 2.3m sqm. Consequently, the vacancy rate is expected to fall even further to reach 3.5% on aggregate in the big seven cities according to JLL forecasts.

As a result of the persistent imbalance between the demand and supply of space, all of the big seven cities recorded significant increases in rental prices, which reached 6.4% on aggregate in 2018. The highest rate was recorded in Berlin, where the y-o-y rent improvement stood at 13.3%. In six of the seven largest markets (except Cologne), the upward trend is expected to prevail but with the projected aggregate annual rate falling to 3.5% in 2019. Interestingly, it may result in Munich replacing Frankfurt as the most expensive office market in terms of rents, according to JLL.

Valuation: Trading close to peers

In our view, P/E and EV/EBITDA multiples are the most appropriate measures to value publity, as it is an asset manager rather than a property fund, so it focuses on generating earnings rather than NAV growth. The company's shares are trading at a 16.4% premium changing to a c 1.4% discount to the peer group on 2019e and 2020e P/E consensus. Given that consensus estimates for publity's EBITDA are no longer available, we have not included this ratio in our analysis. The company has also announced that it intends to pay a dividend for FY18 amounting to €1.5 per share, subject to approval at the Annual General Meeting (24 May 2019). Total disbursement should reach €14.8m, 49% of which would come from FY18 net income and the remainder being derived from the previous years' results. This translates into a dividend yield of c 5.3%.

Exhibit 2: Peer group comparison

Company's name	Market cap (€)	P/E (x)		Yield (%)
		2019	2020	2019
Corestate Capital	836.0	6.0	5.6	6.4%
Patrizia Immobilien	1,729.6	18.2	16.8	1.4%
VIB Vermögen	700.1	11.3	10.8	2.6%
TLG Immobilien	2,736.1	11.8	13.4	4.9%
Peer group average		11.8	11.6	3.8%
Publity	276.6	13.8	11.5	5.3%
Premium/(discount) to peer group		16.4%	(1.4%)	150bp

Source: Refinitiv consensus as at 16 April 2019, company accounts, Edison Investment Research

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