



**Independent Research**

Unabhängige Finanzmarktanalyse GmbH

# Investment Research

## ADLER Real Estate AG



**Market segment: Official Market  
Sector: Real Estate**

**Initial Coverage**

**04/02/2007  
(Revised version)**

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## Table of Contents

1. Summary	3
2. SWOT-Analysis	4
3. Equity Story	5
4. German Real Estate Market	8
5. Business development and projections	11
6. Valuation	14
7. Conclusion	16

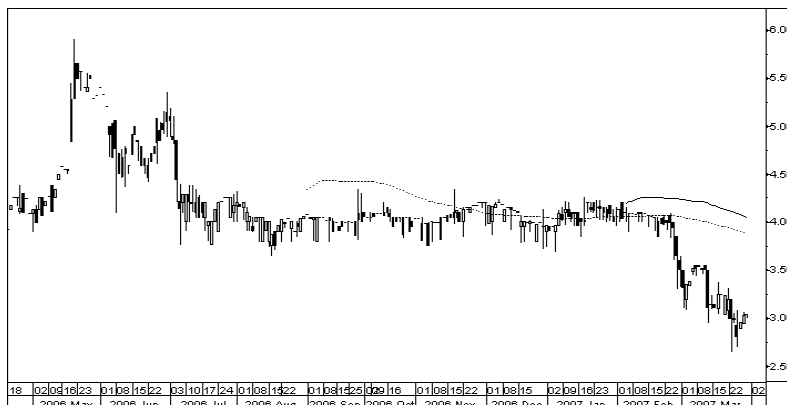
**ADLER REAL ESTATE AG** <sup>4)</sup>Buy  
before: -**Event:**

Initial Coverage

**Recommendation:**

Buy

<b>IR</b>	<b>2</b>	-	-
Rating	Growth	Investor Relations	Dependability

**Author: Manuel Martin (analyst)**

- ⇒ **ADLER Real Estate AG has been successfully restructured and is on the way to expand their development business and to enter more strongly into the business fields of Portfolio Management, Asset Management and Closed-end Funds (mid term target)**
- ⇒ **The shareholder structure gives a stable picture with the majority shareholder Mezzanine IX Investors (60%)**
- ⇒ **We see ADLER as an interesting opportunity to invest in the rising German real estate market**
- ⇒ **According to our peer group valuation we derive a fair value of EUR4.06 per share. Our recommendation is Buy with a price target of EUR4.--**

<b>ADLER Real Estate</b>		<b>Real Estate</b>		<b>Performance (in %)</b>				
Country	GE	Fiscal year	Dec. 31	Rel. 1 Month	-19.5			
Shares (m)	15.0	www.adler-ag.de		Rel. 3 Months	-27.1			
∅ Trading Volume	6,137	Last dividend (Euro)	-	Rel. 6 Months	-35.6			
ISIN	DE0005008007	Payable day	-	Rel. 12 Months	10.3			
Curr. Price (Xetra)	3.02 EUR	Market cap. (EURm)	45.3	Beta	0.57			
03/30/07 3:33 PM		Currency	EUR	Volatility (60 days)	47.1			
52W High	5.90	Date	05/22/06	CDAX	0.002%			
52W Low	2.65	Date	03/23/07					
Shareholders:	Mezzanine IX Investors, L.P. 60%; Freefloat 40%							
Investments:								
FY	Total revenue	EBIT	EBT	EAT	EPS	P/E	EV/Sales 07e:	2.9
2005	8.3	4.4	4.4	4.1	0.41	2.3	EV/EBIT 07e:	7.5
2006(e)	13.2	8.9	8.6*	8.6	0.69*	5.3	Dividend yield 06e:	-
2007e	16.2	6.3	6.1	6.1	0.41	7.4	CAGR Tot. revenue 05-07e:	39.8%
							CAGR EAT 05-07e:	22.6%
Figures in EURm except EPS (in EUR). Historical P/Es based on yearly average share prices							AS:	IFRS
* Estimate Independent Research								

<sup>1)2)3)4)</sup> Please notice the advice regarding possible conflicts of interests as well as the disclaimer at the end of this document

## STRENGTHS AND OPPORTUNITIES

- **Successfully restructured company**
- **Management has long standing and profound experience in the real estate business**
- **Excellent network and relationships with banks and property companies**
- **Strong balance sheet**
- **Profitable on net income basis**
- **Existing potential in the development pipeline**
- **Entering new business fields (Portfolio Management, Asset Management and Closed-end Funds) with promising potential and synergy potential**
- **Stable shareholder structure with long-term strategic interest in ADLER**

## WEAKNESSES AND THREATS

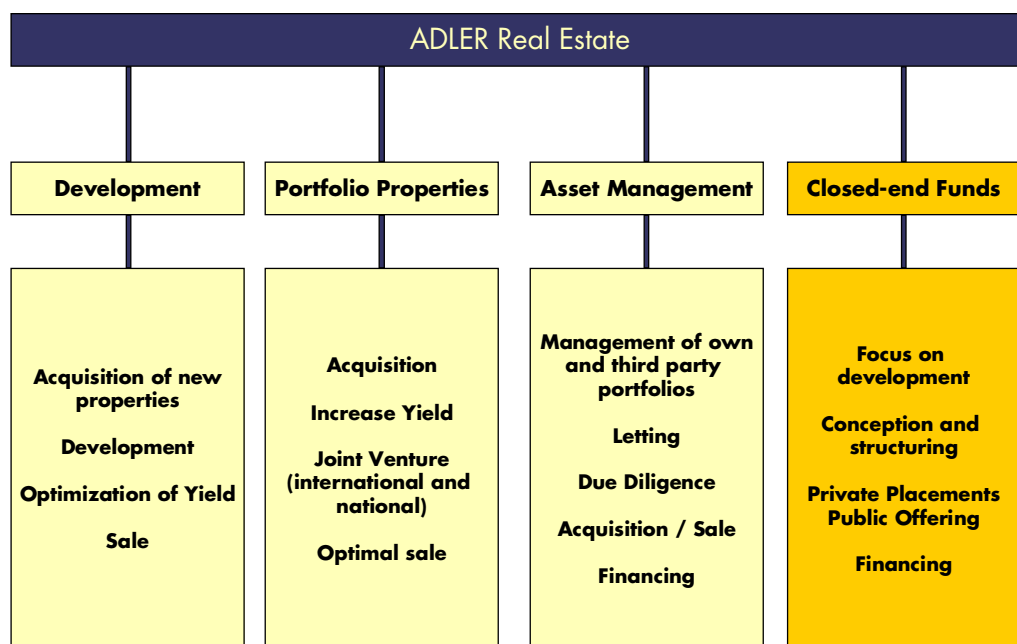
- **Possible significant fluctuations in earnings due to still relatively small size of the pipeline**
- **Success in entering the new business fields must be proven in the future**
- **Toughening competition in the German real estate market**
- **Possible bottlenecks in finding suitable properties for investment**
- **Cost pressure and squeeze on margins due to possible increase in building costs**
- **Rising interest rates could lead to lower margins**

## Equity Story

### Company profile

After being bought out from insolvent AGIV in 2005 with the help of U.S. investor Mezzanine IX, L.P. (acquired 88%) ADLER Real Estate has been in the process of restructuring and actually started operations in September 2005. In 2006, a capital increase, a debt restructuring and in 2007 the acquisition of Mübau Real Estate (residential development) were carried out. Therefore ADLER nowadays is not comparable with the former company.

ADLER mainly focuses on the development of commercial properties and to a minor extent on the development of residential properties through the recently acquired Mübau. The near term target is to expand the development business. They have already made co-Investments with AIG. Also, ADLER wants to increase its presence in the business fields of portfolio management (Portfolio Properties) with a return on equity expectation of 15 to 25%, Asset Management and as a mid-term target to enter the business field Closed-end Funds.



Source: ADLER Real Estate

The company is active on a countrywide basis in Germany with the biggest part of the activities located in Berlin.

### Portfolio investments

- ➔ **Berlin**, Hellersdorfer Strasse
- ➔ **Guetersloh**, Verler Strasse
- ➔ **Frankfurt/Main**, Herriotstrasse
- ➔ **Gruenstadt**, Hauptstrasse

Source: ADLER Real Estate

### Financial investments

- ➔ **Amsterdam**, Schiphol/NL, development of a realty at Amsterdam Airport (7.5%)
- ➔ **Luxembourg**, AirportCenter / LUX (10%)

Source: ADLER Real Estate

### Project overview development

- ➔ **Berlin**, Fanny-Zobel-Strasse
- ➔ **Berlin**, Grossbeeren, Trebbiner Strasse
- ➔ **Berlin**, Spaethstrasse
- ➔ **Berlin**, Dallgow-Doeberitz, Triftstrasse
- ➔ **Duisburg**, Hamborner Strasse
- ➔ **Dresden**, Alt Trachau
- ➔ **Frankfurt**, Herriotstrasse
- ➔ **Offenbach**, Strahlenbergerstrasse
- ➔ **Saarbrücken**, Hafenstrasse
- ➔ **Homburg/Saar**, Am Forum
- ➔ **Munich**, Einsteinring

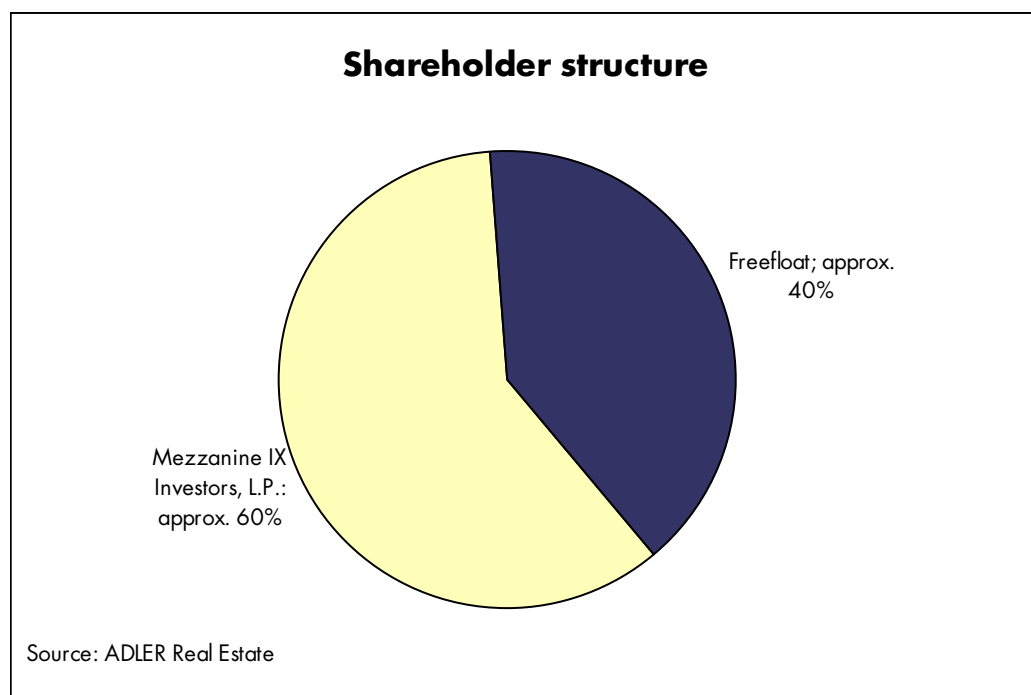
Source: ADLER Real Estate

### Management

Mr. **Axel Harloff** (48) has been Executive Board Member since 2003. Before joining ADLER he was Head of Asset Management at HBAG Real Estate AG (1998-2003) and Head of Asset Management at Transatlantica Real Estate AG (1997-1998). Mr. Harloff has more than 23 years of experience in the real estate business.

Ms **Barbara Yaltrak** (50) has been Executive Board Member since 2005. Before she joined ADLER she was Project Manager of commercial real estate at Bau-Verein zu Hamburg AG (2004-2005) and Authorized Officer at Transatlantica Real Estate AG (2000-2004). Ms Yaltrak advised funds of more than EUR1bn.

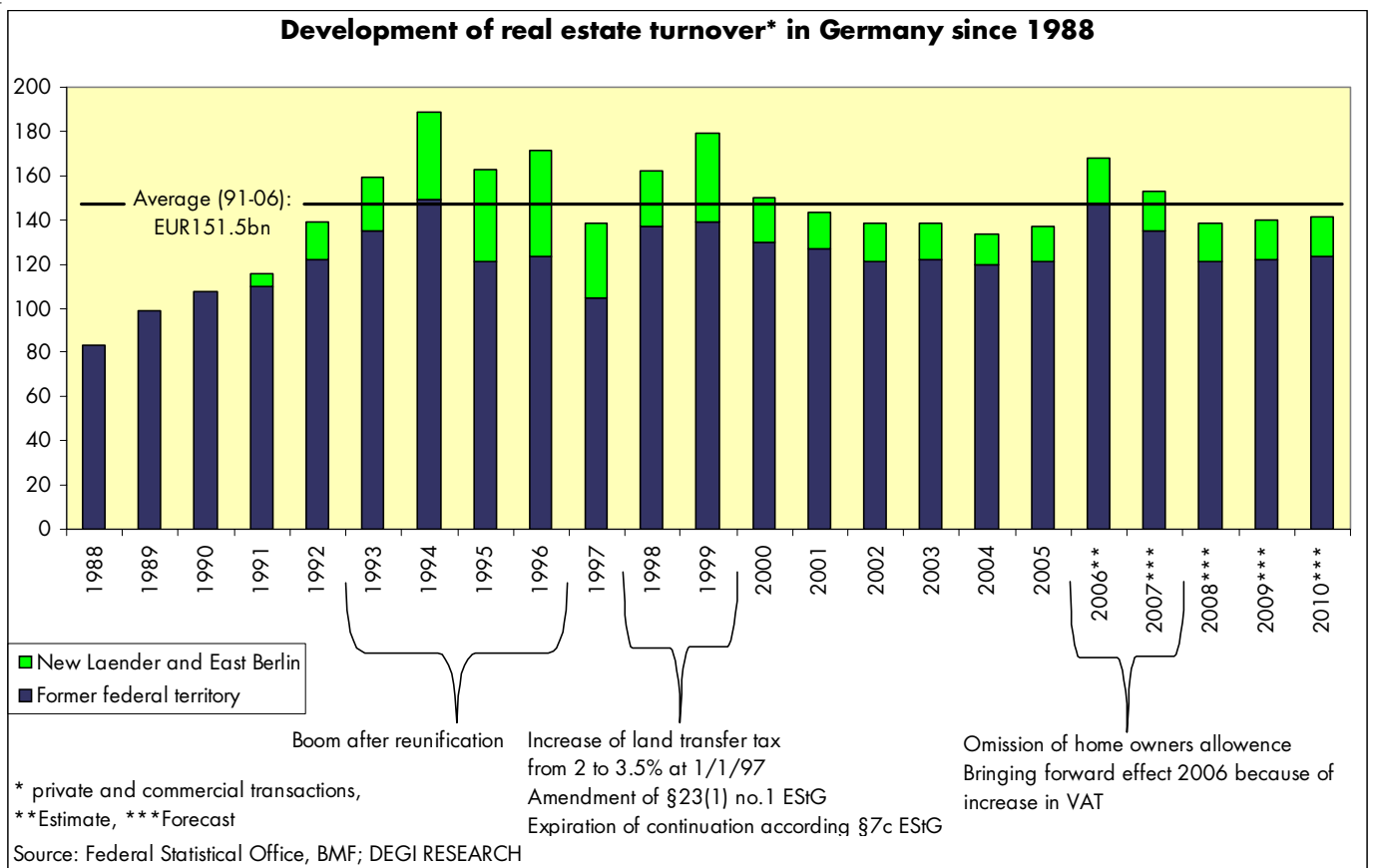
The Supervisory Board consists of Mr. Peter Pahlke (Chairman), Mr. Andreas Helwig and Mr. John D. Heikenfeld (owner of the majority shareholder Mezzanine IX Investors).



The majority shareholder is U.S. investor Mezzanine IX Investors (a company of the Supervisory Board Member John D. Heikenfeld), which has a long-term strategic interest in ADLER. The majority of the free float is held by international institutional investors.

### German Real Estate Market

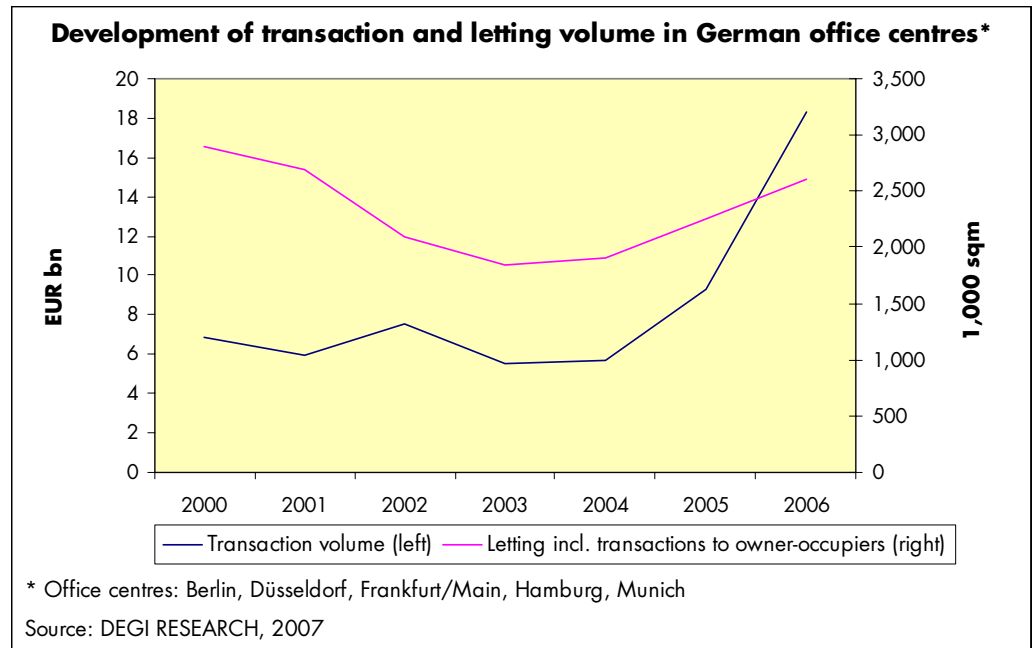
The economic upswing last year has influenced the german real estate market in an impressive way. Above all the low interest rates and the expiring governmental subsidies in residential construction led to an increase of 22.5% in real estate turnover vs. 2005. DEGI expects for the overall real estate turnover in 2007e a more calm development but splitting up the overall real estate turnover DEGI expects that commercial real estate will stay in the focus of institutional investors because german real estate is seen as undervalued and the market cycle is in the recovery phase.



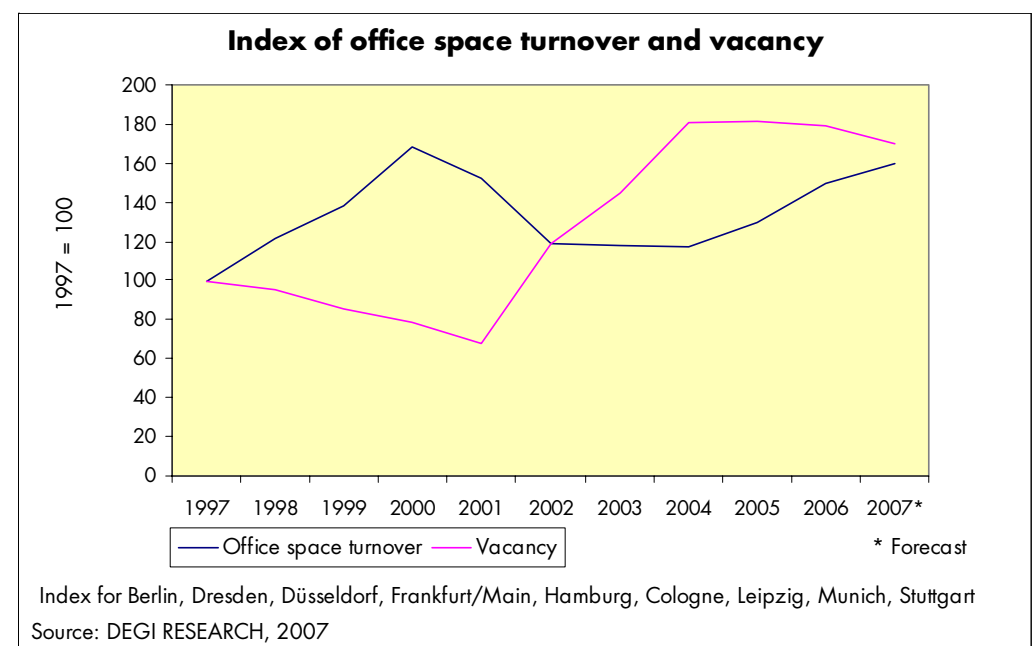
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**Office Real Estate**

The transaction volume in commercial real estate has increased to a new record high of EUR46bn (plus 12% vs 2005) because of foreign investors and big portfolio transactions. The main focus was on office real estate. Looking to the five important office centres in Germany (Berlin, Düsseldorf, Frankfurt/M, Hamburg and Munich) there was a transaction volume of EUR18.5bn in 2006. This is an increase of 105% y/y after an increase of 70% in 2005 y/y.



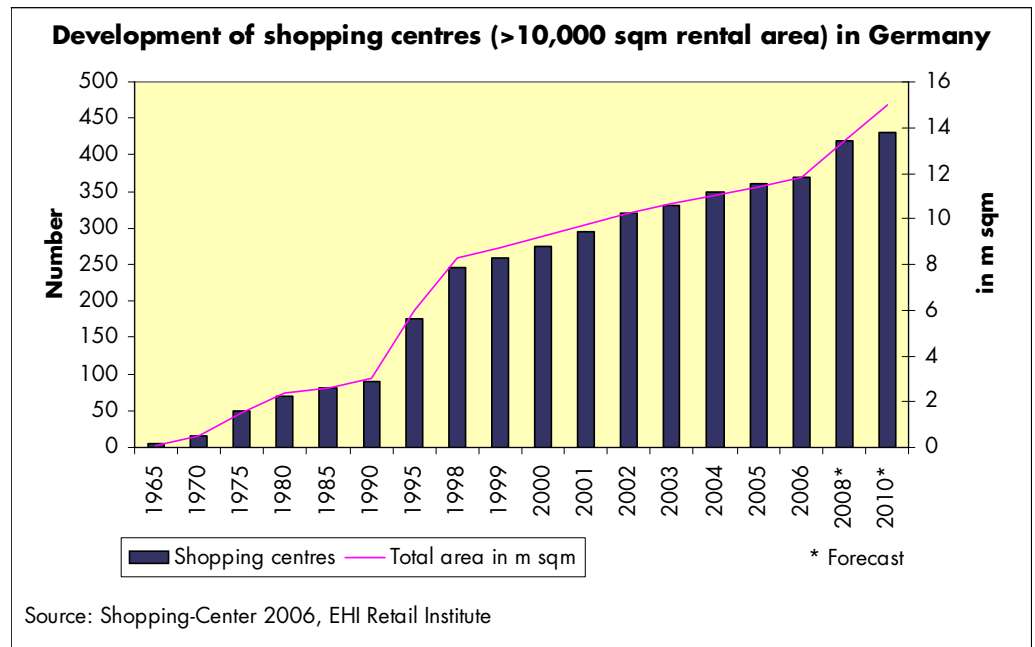
The positive development in German office real estate is due to a strong demand for office real estate, the reduction of space offered and rising rents. DEGI expects the rising trend in office space turnover and the falling trend in vacancy to be continued in 2007.



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**Shopping Centres**

Talking about commercial real estate we are going to mention also the good development of shopping centre real estate that was positively influenced by the booming German economy 2006. Exports of the German industry and investments in Germany undertaken in 2006 led to an improvement of the labour market. As a consequence of the improved labour market, for the first time since six years private consumption was able to support the economic growth in the second half of 2006. The demand for shopping centre real estate is strongly driven by foreign investors, in particular by british investors. Due to the positive interest rate spread and the cheap purchase prices for the properties, from the perspective of british or U.S. investors, the segment of shopping centres continues to be in focus. DEGI expects the rising trend of number of shopping centres and total area to be continued.



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## Business development and projections

### Fiscal years 2005 and 2006(e)

After being bought out from the insolvent AGIV in 2005 with the help of U.S. investor Mezzanine IX, L.P. (acquired 88%) ADLER Real Estate has been in the process of restructuring and actually started to operations in September 2005. In 2006, a capital increase, a debt restructuring and in 2007 the acquisition of Mübau Real Estate (residential development) were carried out. Therefore ADLER nowadays is not comparable with the former company.

Total revenue in 2006e went up to EUR13.20m from EUR8.29m in 2005. The biggest part of the increase stems from IAS 40 fair value valuation of investment properties (approximately EUR7m) and from operating business picking up. We estimate that there were almost no material expenses in 2006(e) as no purchases took place in that year in contrast to 2005 where material expenses were EUR2.91m. Based on the risen total revenue in 2006(e), EBIT climbed to EUR8.90m (EUR4.37m in 2005), EBT to EUR8.9m (own estimate, EUR4.37m in 2005) and net income to EUR8.60m (EUR4.06m in 2005).

### Forecast 2007e

As ADLER has been recently restructured and is a relatively small development company it is difficult to make accurate predictions of future revenue. Therefore we have limited the forecast horizon to 2007e.

Keeping in mind the Duisburg project (warehouse, 126,000 sqm) where part of it should lead to revenues in 2007e, the realties of the acquired Mübau (development land 300,000 sqm) and possible earnings from fair value valuation of investment properties, we estimate total revenue of EUR16.22m. As the screening of target properties should lead to purchases in 2007e we expect material expenses of EUR4.12m which, together with SG&A and depreciation, should result in EBIT of EUR6.3m. Due to a loss carry forward in 2006(e) we expect no tax payments and estimate net income of EUR6.1m (EPS EURO.41).

<b>ADLER Real Estate AG</b>				
<b>Profit and loss statement</b>				
Unit:	EUR (k)			
End of fiscal year:	Dec. 31	<b>2005</b>	<b>2006(e)</b>	<b>2007e</b>
Accounting standards	IFRS			
<b>Total revenue</b>		<b>8,298</b>	<b>13,200</b>	<b>16,220</b>
% YoY		0.00%	0.00%	0.00%
Material expenses		-2,914	0	-4,124
% YoY		395.02%	-100.00%	-
% total revenue		35.12%	0.00%	25.42%
<b>Gross profit</b>		<b>5,384</b>	<b>13,200 *</b>	<b>12,096</b>
% YoY		-56.43%	145.19%	-8.36%
% total revenue		64.88%	100.00%	74.58%
SG&A and depreciation		-2,081	-4,300 *	-5,770
% YoY		547.70%	106.63%	34.20%
% total revenue		25.08%	32.58%	35.58%
Revenues from disposals		1,067	0 *	0
% total revenue		12.86%	0.00%	0.00%
<b>EBIT</b>		<b>4,370</b>	<b>8,900</b>	<b>6,326</b>
% YoY		495.71%	103.68%	-28.92%
% total revenue		52.66%	67.42%	39.00%
Financial result		4	-300 *	-225
<b>EBT</b>		<b>4,373</b>	<b>8,600 *</b>	<b>6,101</b>
% YoY		361.68%	96.65%	-29.06%
% total revenue		52.70%	65.15%	37.61%
Taxes		-317	0 *	0
% EBT		-7.25%	0.00%	0.00%
<b>Net income</b>		<b>4,056</b>	<b>8,600</b>	<b>6,101</b>
% YoY		355.33%	112.02%	-29.06%
% total revenue		48.88%	65.15%	37.61%
Number of shares (k)		9,893	12,500 *	15,000
<b>EPS (EUR)</b>		<b>0.41</b>	<b>0.69 *</b>	<b>0.41</b>

\* Estimate Independent Research  
Source: Independent Research, ADLER Real Estate AG

The development of the balance sheet total from 2005 to 9M 2006 is mainly influenced by the capital increase that took place in 2006, which raised cash and cash equivalents from EUR1.36m (2005) to EUR7.79m (9M 2006). According to the company cash and cash equivalents rose to EUR10.4m at the end of 2006(e) with total assets of EUR37m. Financial liabilities should amount to about EUR8m at the end of 2006(e) and the equity ratio should be at an attractive level of 74.9%.

<b>ADLER Real Estate AG</b>			
<b>Balance sheet</b>			
Unit:	EUR (k)		
End of fiscal year:	Dez 31	<b>2005</b>	<b>9M 2006</b>
Accounting standard:	IFRS		
<b>Assets</b>			
<b>Non-current assets</b>			
Intangible assets		7	7
Tangible assets		40	60
Other financial assets		150	150
Accounts receivable		415	483
<b>Sum</b>		<b>612</b>	<b>700</b>
<b>Current assets</b>			
Inventories		12,345	10,568
Accounts receivable		1,976	1,247
Other receivables		24	24
Other current assets		5,662	7,946
Cash and cash equivalents		1,363	7,796
Assets held for sale		0	0
<b>Sum</b>		<b>21,369</b>	<b>27,580</b>
<b>Total assets</b>		<b>21,982</b>	<b>28,280</b>
<b>Equity and Liabilities</b>			
<b>Equity</b>			
Share capital		10,000	15,000
Retained earnings		421	7,872
Loss carry forward		0	-4,165
Net income for the year		-4,165	2,064
<b>Sum</b>		<b>6,256</b>	<b>20,771</b>
<b>Non-current liabilities</b>			
Pension liabilities		809	809
Other liabilities		294	352
Financial liabilities		11,388	3,572
<b>Sum</b>		<b>12,492</b>	<b>4,733</b>
<b>Current liabilities</b>			
Other provisions		1,138	1,492
Tax liabilities		275	0
Financial liabilities		0	0
Accounts payable		857	637
Other liabilities		964	647
<b>Sum</b>		<b>3,234</b>	<b>2,776</b>
<b>Total equity and liabilities</b>		<b>21,982</b>	<b>28,280</b>
Source: ADLER Real Estate AG			

<sup>1)2)3)4)</sup> Please notice the advice regarding possible conflicts of interests as well as the disclaimer at the end of this document

## Valuation

### Peer Group Valuation

We have estimated the value of ADLER by means of a peer group comparison. The group comprises 7 publicly-listed companies from the German real estate sector with business activities as comparable as possible. The geographic focus of all the companies is Germany.

**ALTA FIDES AG** focuses on project development as well as the trading in and holding of high-value and predominantly listed residential properties in best locations. The investment focus is currently on the federal states of Saxony (especially Leipzig), Baden-Württemberg and Bavaria. Through its subsidiary PROPECTO AG the company deals in the purchase and realisation of non-performing real estate loans.

**Design Bau AG** operates in the acquisition, parceling and development of lots in the so-called 'fat-belts' of large cities (such as Berlin and Hamburg). Thanks to their platform strategy the company provides individualised and cost-efficient construction of single-family homes and duplexes. The company's customers are mainly young families who are also supported by the company with respect to financing.

**Franconofurt AG** acquires apartment portfolios and individual apartment homes with the goal of the successive sale of the apartments. Regionally the company is limited to the Rhine-Main region, especially in the Frankfurt districts of Westend, Nordend, Bornheim, Sachsenhausen and Bockenheim. An issuing platform for regional apartment portfolios is being developed and is to serve as a second business area.

**GWB Immobilien AG** is a group that specialises in the development, realisation, letting and management of retail, shopping and specialized discount store centres as well as commercial properties in Germany. Together with its subsidiaries, GWB covers the complete value chain and special expertise needed for the realisation of the so-called "large-scale retail" (trading space of more than 1,200m<sup>2</sup>). Retail properties projects are realised both for the issuer (as general contractor) and on behalf of third parties (as general contractor) against a service fee. Within the asset management segment, both objects sold from the company's own portfolio and objects sold from third parties to investors are managed.

**HII Hanseatische Immobilien Invest AG** deals in the building and administration of lucrative investment properties, the dividing of apartment houses, the trading of individual properties and property packages, the takeover of real estate companies, and also acts as an agency for high-value investment properties starting from a volume of roughly EUR 1m. The company's geographic focus is on Greater Hamburg and German cities with more than roughly 100,000 inhabitants.

**Primag AG** is a holding company that focuses on the refurbishment of old buildings and package development. The company focuses almost exclusively on Oberkassel, one of Dusseldorf's prime neighbourhoods. The regional orientation for package development extends to Greater Dusseldorf.

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**InCity Immobilien AG** specialises in the conception and realisation of high-quality real estate properties in the centres of large German cities and in growth regions (Cologne/Bonn, Berlin, Weimar/Erfurt, Rhine Main area). The company covers the entire value creation chain, from property search over redevelopment or new building to sale. Merely construction work is carried out by external contractors. The business model does not include long-term holdings of existing properties; the properties acquired are intended exclusively for resale. InCity's business includes partial and total redevelopment of listed and non-listed old buildings, new building and space optimisation, i.e. the creation of additional living space in existing objects with the help of extension and expansion.

<b>Peer-Group:</b>											
Companies	Currency	Price 03/29/07	Market cap		EV/EBIT			P / E ratio			Application IAS 40
			in EURm	EV	2005	2006(e)	2007e	2005	2006(e)	2007e	
<b>ALTA FIDES AG</b>	EUR	17.70	124.8	140.8	14.9	12.4	6.3	17.7	23.3	9.5	Yes
<b>Design Bau AG</b>	EUR	9.49	45.6	36.5	31.8	8.3	5.1	14.4	17.6	12.7	Yes
<b>Franconofurt AG</b>	EUR	12.46	109.6	112.1	60.2	11.1	9.4	51.9	11.6	12.4	Yes
<b>GWB Immobilien AG</b>	EUR	13.10	64.2	92.1	57.8	28.8	7.5	38.5	16.4	11.8	No
<b>Hil Hanseatische Immobilien Invest AG</b>	EUR	12.85	35.3	60.7	-	25.8	6.5	-	15.9	11.3	Yes
<b>InCity Immobilien AG</b>	EUR	8.84	22.1	32.6	18.4	9.2	4.5	17.7	8.3	6.1	No
<b>Primag AG</b>	EUR	3.57	15.6	20.4	68.1	6.2	5.8	35.7	8.1	5.8	No
<b>Mean</b>			59.6	70.7	41.8	14.5	6.5	29.3	14.5	9.9	
<b>Median</b>			45.6	60.7	44.8	11.1	6.3	26.7	15.9	11.3	
<b>ADLER Real Estate AG*</b>	<b>EUR</b>	<b>2.98</b>	<b>45.3</b>	<b>47.7</b>	<b>5.4</b>	<b>7.5</b>	<b>7.5</b>	<b>11.2</b>	<b>5.3</b>	<b>7.4</b>	<b>Yes</b>

Source: Independent Research; Bloomberg consensus overview

We have determined the P/E ratio for the peer group for 2005, 2006(e) and 2007e according to mean and median. For the valuation we have taken the mean value for 2007e into consideration.

<b>Fair value according to peer group valuation</b>		
<b>ADLER Real Estate AG</b>	according to median	according to mean
EPS 2007e	0.41	0.41
Peer Group P/E 2007e	11.3	9.9
<b>Fair value in EUR per share</b>	<b>4.63</b>	<b>4.06</b>
Source: Independent Research		

Based on an EPS estimate of EURO.41 in 2007e and a peer group P/E of 9.9 (mean) for 2007e we calculate a fair value per share of EUR4.06.

<sup>1)2)3)4)</sup> Please notice the advice regarding possible conflicts of interests as well as the disclaimer at the end of this document

## Conclusion

The successfully restructured ADLER Real Estate AG is on the way to expand their development business and to enter more strongly into the business fields of Portfolio Management (Portfolio Properties) with a return on equity expectation of 15 to 25%, Asset Management and as a mid term target to enter the business field Closed-end Funds.

Within the above mentioned targets their goal is to build up an attractive portfolio and to become more transparent. In order to improve the tradability of their shares ADLER wants to expand the free float and to enter the Prime Standard in the future.

The shareholder structure gives a stable picture with the majority shareholder (60%) Mezzanine IX Investors (a company of Supervisory Board Member John D. Heikenfeld) as it has a long-term strategic interest in ADLER.

It should be kept in mind that the earnings of the company can fluctuate significantly due to the still relatively small size of its pipeline, which is to grow strongly. Nevertheless, in our opinion ADLER is an interesting opportunity to invest in the rising German real estate market. With their strong balance sheet (equity ratio of 74,9%) the company should be able to purchase interesting properties and to execute their expansion program

Based on our forecast we expect a net income of EUR6.1m in 2007e which represents an EPS of EURO.41. According to our peer group valuation we derive a fair value of EUR4.06 per share. Our recommendation is Buy with a price target of EUR4.-.

## Disclaimer

### Recommendation shares - Single Issuer -:

Buy:	According to our assessment, the stock should register an absolute profit of at least 15% within a 6-month period.
Accumulate:	According to our assessment, the stock should register an absolute profit between 0% and 15% within a 6-month period.
Reduce:	According to our assessment, the stock should register an absolute loss between 0% and 15% within a 6-month period.
Sell:	According to our assessment, the stock should register an absolute loss of at least 15% within a 6-month period.

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### Key sources of information

Key sources of information used in the preparation of this document are publications in foreign and domestic media such as information services (e.g. Reuters, VWD, Bloomberg, DPA-AFX etc.), the financial press (e.g. Börsen-Zeitung, Handelsblatt, FAZ, FTD, Wall Street Journal, Financial Times etc.), specialised journals, published statistics, rating agencies and publications of the issuers analysed.

<sup>1)2)3)4)</sup> **Please notice the advice regarding possible conflicts of interests as well as the disclaimer at the end of this document**

## Summary of the evaluation principles used:

### Analyses of shares:

In valuing companies standard and accepted valuation methods (amongst others the Discounted Cash Flow Method (DCF Method), Peer Group Analysis) are applied. Under the DCF Method the capitalised value of the issuers is calculated which shows the sum of the discounted company results, i.e. the current value of the issuer's future net distributions. The capitalised value is therefore determined with reference to the anticipated future company results and the capitalisation yield applied. Under the Peer Group Analysis Method issuers quoted on the Stock Exchange are valued with reference to the comparison of ratio indices (e.g. price earnings ratio, price to book ratio, enterprise value / sales, enterprise value / EBITDA, enterprise value / EBIT). The comparability of the ratio indices is determined above all by business activity and commercial prospects.

### Technical analyses:

Technical analyses are based on historic share price and sales developments which are analysed by mathematical-statistical tools (chart techniques, indicator technology, the Elliott wave theory, sentiment observations as well as relative strength approaches) and on forecasts of future developments.

### Sensitivity of the evaluation parameters:

The figures taken from the statement of income, the cash flow statement and the balance sheet upon which the evaluation of companies is based are estimates referring to given dates and therefore subject to risks. These may change at any time without prior notice.

Regardless of the evaluation method applied, there exists a very real risk that the price target may not be reached in the anticipated period of time. These risks include unforeseen changes in competitive pressure or in the demand for the issuer's products. Such fluctuations in demand may arise as a result of changes of a technological nature, the overall level of economic activity or in some cases as a result of changes in moral standards. Changes in tax law, in currency exchange rates and, in certain industries, in regulations are further factors which can influence evaluations. This discussion of evaluation methods and risk factors makes no claim to be exhaustive.

### Timing conditions of planned updates:

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**As of: - 04/02/2007 -**

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