**LIGHTHOUSE** INSTITUTO ESPAÑOL DE ANALISTAS

# Inmobiliaria del Sur

**EQUITY - SPAIN**
Sector: Real Estate

Closing price: EUR 7.30 (21 Dec 2022)
Report distribution: 22 dec 2022 (11:00h)

**Initiation of Coverage**
Independent Equity Research

**Inmobiliaria del Sur (ISUR),** is a property company with headquarters in Seville and a presence in Andalusia and Madrid, whose business model combines a development activity (residential and tertiary) with a property management business, that has a portfolio of rental assets (mainly offices), both activities having a significant weighting in terms of GAV. The board directly and indirectly controls c. 64% of capital.

**David López Sánchez** – david.lopez@lighthouse-ieaf.com
+34 915 904 226

**Market Data**

| | | |
|---|---|---|
| Market Cap (Mn EUR and USD) | 136.3 | 144.7 |
| EV (Mn EUR and USD) (1) | 397.7 | 422.1 |
| Shares Outstanding (Mn) | 18.7 | |
| -12m (Max/Med/Mín EUR) | 8.48 / 7.85 / 7.24 | |
| Daily Avg volume (-12m Mn EUR) | 0.07 | |
| Rotation(2) | 12.7 | |
| Factset / Bloomberg | ISUR-ES / ISUR SM | |
| Close fiscal year | 31-Dec | |

**Shareholders Structure (%)**

| | |
|---|---|
| Board of Directors | 64.4 |
| Free Float | 35.6 |

| **Financials (Mn EUR)** | **2021** | **2022e** | **2023e** | **2024e** |
|---|---|---|---|---|
| Adj. nº shares (Mn) | 17.8 | 18.7 | 18.7 | 18.7 |
| Total Revenues | 125.2 | 127.1 | 161.9 | 182.8 |
| Rec. EBITDA | 22.5 | 22.9 | 28.3 | 31.5 |
| *% growth* | *-8.5* | *1.8* | *24.0* | *11.3* |
| *% Rec. EBITDA/Rev.* | *17.9* | *18.0* | *17.5* | *17.3* |
| *% Inc. EBITDA sector(3)* | *11.0* | *17.6* | *3.1* | *7.5* |
| Net Profit | 12.0 | 15.0 | 9.7 | 11.8 |
| EPS (EUR) | 0.68 | 0.80 | 0.52 | 0.63 |
| *% growth* | *-40.8* | *18.5* | *-35.2* | *21.3* |
| Ord. EPS (EUR) | 0.52 | 0.48 | 0.52 | 0.63 |
| *% growth* | *9.2* | *-7.7* | *8.1* | *21.3* |
| Rec. Free Cash Flow(4) | 9.7 | -16.2 | -20.6 | -0.4 |
| *Pay-out (%)* | *46.6* | *45.5* | *45.5* | *45.5* |
| DPS (EUR) | 0.32 | 0.36 | 0.24 | 0.29 |
| Net financial debt | 198.0 | 241.9 | 269.3 | 274.1 |
| ND/Rec. EBITDA (x) | 8.8 | 10.6 | 9.5 | 8.7 |
| *ROE (%)* | *9.5* | *11.0* | *6.8* | *8.0* |
| *ROCE (%)(4)* | *4.9* | *4.1* | *4.4* | *4.7* |

| **Ratios & Multiples (x)(5)** | | | | |
|---|---|---|---|---|
| P/E | 10.8 | 9.1 | 14.1 | 11.6 |
| Ord. P/E | 14.0 | 15.2 | 14.1 | 11.6 |
| P/BV | 1.0 | 1.0 | 0.9 | 0.9 |
| *Dividend Yield (%)* | *4.3* | *5.0* | *3.2* | *3.9* |
| EV/Sales | 3.18 | 3.13 | 2.46 | 2.18 |
| EV/Rec. EBITDA | 17.7 | 17.4 | 14.0 | 12.6 |
| EV/EBIT | 18.1 | 20.4 | 17.0 | 14.9 |
| *FCF Yield (%)(4)* | *7.1* | *n.a.* | *n.a.* | *n.a.* |

(1) Please refer to Appendix 3.
(2) Rotation is the % of the capitalisation traded - 12m.
(3) Sector: Stoxx Europe 600 Real State.
(4) Please see Appendix 2 for the theoretical tax rate (ROCE) and rec. FCF calculation.
(5) Multiples and ratios calculated over prices at the date of this report.

# A developer with a "safety net"

**A UNIQUE PROPERTY COMPANY, COMBINING PROPERTY DEVELOPMENT AND MANAGEMENT BUSINESSES.** ISUR is a small property company whose business model combines the development activity (residential and tertiary) with the property management business, with a portfolio of rental assets (office buildings, hotels, commercial premises and parking spaces), both with a significant weighting in terms of GAV (40% development – 60% property management).

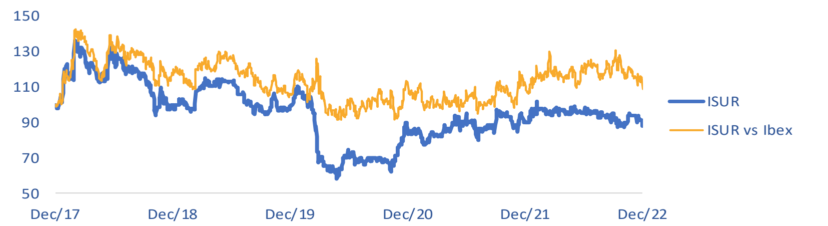
**THE CURRENT LAND BANK ENSURES A SIGNIFICANT INCREASE IN ACTIVITY.** ISUR has a land bank that should allow for the construction of +4,000 homes, of which 1,700 are already being marketed (47% sold) that provides visibility: presales represent c. 55% of the deliveries envisaged until 2024e.

**IN 2024E WE ESTIMATE REVENUE OF EUR 180MN AND EBITDA OF EUR 30MN.** Based on a conservative scenario, we estimate deliveries of, at least, 450 homes in 2023e and 2024e (vs c. 380 in 2021 and 2022e). So in 2024e the company should have sales of EUR 180Mn (+13.5% CAGR 21-24e) and EBITDA of c. EUR 30Mn (+12% CAGR 21-24e).

**A SAFER WAY TO PLAY THE DEVELOPMENT SECTOR.** The property management business (c. 45% of EBITDA) provides a recurrent source of revenue and cash that gives greater resilience and the ability to self-fund growth, allowing the company to "be more patient" with the development business. This is especially interesting in the current market context. The LTV is c. 40%, a result of the weighting of the property management business in the GAV (c. 60%).

**TRADING AT A DISCOUNT OF 60% VS THE VALUE OF ITS ASSETS.** At the date of this report, ISUR is trading at a discount of 60% to its 9m22 NAV vs an average of 50% for the listed property developer sector in Spain and the large Spanish REITs. Although, obviously, with higher bond yields there is a risk of reductions to asset values, the current discount would seem excessive especially when it comes to a developer with a "safety net". The acceleration of activity (and revenue) guaranteed by the current land bank should be a strong catalyst for the share price.

**Relative performance (Base 100)**




| **Stock performance (%)** | **-1m** | **-3m** | **-12m** | **YTD** | **-3Y** | **-5Y** |
|---|---|---|---|---|---|---|
| Absolute | -6.4 | -7.8 | -2.3 | -2.3 | -11.5 | -12.2 |
| vs Ibex 35 | -7.7 | -12.6 | -1.3 | 2.5 | 3.2 | 8.9 |
| vs Ibex Small Cap Index | -5.5 | -9.6 | 6.8 | 11.2 | -19.0 | -20.0 |
| vs Eurostoxx 50 | -5.5 | -16.9 | 5.3 | 8.4 | -13.7 | -19.1 |
| vs Sector benchmark(3) | -2.3 | -5.0 | 57.1 | 62.6 | 43.1 | 33.4 |

(*) Unless otherwise indicated, all the information contained in this report is based on: The Company, Factset and Lighthouse.

# A vertically integrated property company (a rarity in the listed sector in Spain) with credible arguments for long-term growth

ISUR is a small property company with a unique business model that combines a development activity (mainly residential and tertiary) with a property management business that has a portfolio of rental assets (office buildings, hotels, commercial premises and parking spaces). Both activities have a significant weighting in terms of GAV (40% development, 60% property management). It also has a construction company, 100% owned and serving the development business (that allows for greater control of costs, quality and execution times).

Founded in 1945 and listed since 1984, ISUR is run by a management team with significant sector experience (especially important in the current context of the cycle).

## A) The macro is the most important variable for the property sector and the most recent indicators show signs of weakening. This will have a negative impact in the s/t …

The recession is approaching and rate hikes will slow demand for housing in the s/t

**Growth expectations are lower now than those expected a few months ago** and interest rates have risen more than initially expected. The threat of recession is rearing its ugly head and the increase in mortgage rates (the 12-month Euribor rate, the main benchmark for Spanish mortgage financing, is already at highs of 2009).

Additionally, the impact of inflation on disposable household income suggests that in coming quarters we will see a decline both in house prices and in housing transactions. Something that is already visible analysing the data for the third quarter of 2022 in isolation: the appraisal price for private housing remained flat (0.0% qoq), that means this has decelerated very sharply in yoy terms throughout 2022, from +6.7% in 1Q, to 5.5% in 2Q and 4.7% in 3Q.

## B) … but the imbalance between housing supply and demand is, in itself, a driver of long-term growth

**Residential market: since 2014 there has been a sustained recovery in demand (reaching highs already in 2021 not seen since 2007)…** according to government data, in 1H22 there were 373,145 housing transactions (+10% vs 2021 and +37% vs 2019). So 2022 could end with a volume of transactions of over 700,000 (exceeding 2021, the best year since 2007).

Although housing supply continues (and will continue) to be limited (c. 100,000 units a year)

**… with an offer that is still limited (private housing starts remain around 100,000 units p.a.)** In 2021 the number of private housing starts was c. 100,000 (+4.4% vs 2019). This level remains well below the highs reached in 2006 (650,000) and below expected growth in demand: in 2021 the average number of households grew by c. 172,000 (+0.9% vs 2020). In fact, over 2008-2021 the increase in new households exceeded (in cumulative terms) the number of housing completions by c. 300,000.

Compared to growth in the number of households of c. 180,000/year

**Which explains that now the problem is a lack of stock and not excess supply (as occurred in 2008).** As regards growth in households (one of the main variables used to extrapolate demand for housing), the National Statistics Office predicts a CAGR of 0.9% for the next 15 years (implying the creation of 180,000 new households a year). What's more, supply-side limitations such as the lack of building sector capacity (due to the difficulties in finding labour), the lack of building land and uncertainty regarding the new housing law, will continue to have a negative effect in the short and mid term.

Supply-demand imbalance: a long-term growth driver for the Spanish residential sector

**An imbalance that, in itself, will be a driver of long-term growth (once the current situation is over).** In the short term a weakening of demand would seem inevitable (rising interest rates, worsening of the economic situation) and the result of this is as yet unknown. However, the sector is facing the current situation in good conditions (both families and developers are in a more solvent position than in the past). Looking to the longer term, supply will continue to be scarce (and lower than demand) and, in our view, this will in itself be a growth driver for the Spanish residential sector.

### C) ISUR has a unique business model that combines development and property management businesses: a rarity in the listed sector in Spain

ISUR operates via two main businesses; i) residential and tertiary development (67% of 2021 revenue) and ii) property management (12% of revenue), in addition to two complementary business serving the development business (both for proprietary developments and for those developed with third parties through joint ventures): i) construction (18% of 2021 revenue) and ii) administration and marketing (3% of 2021 revenue). Specifically, from a business model point of view, we would highlight:

A business model that combines residential and tertiary development and the property management business

- **A business model that is unique thanks to its combination of housing development and property management...** ISUR combines a development business (capable of delivering > 350 homes/year and with a land bank that should allow for the construction of +4,000 homes, 40% of which are already on sale today), with a property management business, with a portfolio of rental assets of 130,000 m2 of offices (71% of the total), hotels (21%) and commercial premises (8%) offering a gross yield of 4.9%. The rental assets have an occupancy rate of 88% (and a large part of the vacant space is being reformed).

  In our view, the recurrent generation of rents of the property management business (c. 45% of EBITDA in 2021) allows for "greater patience" in the development business, acquiring land during the downward stages of the cycle (as demonstrated in 2008-2012) and maximising shareholder returns.

9m22 GAV: EUR 600Mn (+ 15% vs 2021). 40% development-60% property management

- **... both with a significant weighting in terms of GAV (38% development – 62% property management).** At the 2015 close, ISUR's GAV was EUR 600Mn (+15% vs 2021), of which 62% corresponded to the property management business and 38% to the developer. By geographies, 80% is located in Andalusia, where the company has a leading and consolidated position in office rentals (mainly in Seville), and 20% in Madrid.

- **Vertical integration.** With a construction company, 100% owned and serving the development business, that allows for greater control of costs, quality and execution times. In addition, the development of the property assets from their construction, allows the added value of the entire process to be captured.

- **A significant part of the development business is carried out through joint ventures,** with three objectives: (i) to take on larger projects, (ii) to improve the profitability of the investment (by providing the joint ventures with construction and administration and marketing services) and (iii) to diversify risk.

With a very local nature (Andalusia), where it has significant experience

- **A local focus, in markets where it has significant experience.** Many investors use property companies to invest in a certain country or city. In this respect, ISUR combines: 1) a strong position in Andalusia, where it has been operating since its creation in 1945, being a leading player in both development and office rental, with 2) growth in Madrid (the most dynamic market in the Spanish property sector, where ISUR expects to generate c. 40% of its residential development activity from 2025e).

The refinancing of debt in 2019 delayed 60% of maturities to 2026e

- **A reasonable level of debt (LTV < 40%).** Higher gearing than the average for listed developers in Spain (LTV < 20%) explained by the weighting of the property management business in the value of its assets (c. 60% of the GAV). The refinancing of debt in 2019 (with more favourable conditions) delayed 60% of maturities to 2026e.

The management team has been with the company for a long time...

- **Alignment of interests between the owners and management.** Controlling shareholders have not changed in practice throughout the history of the company and have a presence both on the Board of Directors and the management team. This implies an alignment of interests between the owners and management (the Board of Directors controls c. 60% of the capital).

...something we think could reduce the risks inherent to the cycle itself.

**In conclusion, a rarity in the listed sector in Spain.** All the previous points (combination of development and property management, vertical integration, carrying out the business via joint ventures, local focus…) are mainly strategic and differential compared to property companies with businesses based exclusively on development. This makes ISUR an option to play the Spanish development business in a safer way, reducing the risk inherent to the residential property cycle.

### D) The current land bank ensures a very significant increase in activity....but the benefits will not be felt until 2025e

Having reached this point, the question now is what can we expect from a company like ISUR in a situation such as the present one. Our projections for 2022e-2024e can be summarised as follows:

ISUR's development business looks set for a very significant increase in activity (but not until 2025e)

- **The land bank and level of presales point to an acceleration of growth in the development business (development revenue: +12.8% CAGR 21-24e).** Assuming a conservative scenario (the current context invites prudence), we estimate levels of deliveries of, at least, c. 450 homes in 2024e (the company has 1,700 homes for sale), with revenue of c. EUR 120Mn (+12% CAGR 21-24e). Although from 2024e visibility is lower, in 2025e we estimate deliveries close to 800 homes (2025e development revenue: EUR 190Mn). This represents a genuine step-up in size bearing in mind that in 2021 and 2022 approximately 380 homes were delivered.

Without forgetting the large contribution of the property management area to EBITDA (EBITDA margin >70%).

- **The property management business (highly recurrent) provides high visibility both in terms of revenue and margins (property management revenue: + 6.5% CAGR 21-24e).** The scenario we envisage for ISUR's property management business includes the continuation of mid single-digit non-organic growth to rental revenue of EUR 18.6Mn in 2024e (+6.5% CAGR 2021-2024e) as a result of: i) the updating of rents in line with inflation (mainly in 2022, visible in 9m22 results) and ii) a slight improvement in the occupancy rate of the asset portfolio to levels of c. 90% in 2024e (vs 88% in 2021) without forgetting the large contribution of the property management area to the generation of EBITDA and cash flow (with an EBITDA margin of c.75%).

- **Accessory services (construction; administration and marketing): growth in line with that of the development activity.** The revenue generated by the construction (12.5% of 2022e revenue) and administration and marketing (3% of 2022e revenue) businesses corresponds to the services provided for developments carried out as joint ventures. So their growth depends on: i) the evolution of the company's development activity, ii) the mix of deliveries corresponding to joint ventures (with more revenue from these services the greater the level of activity carried out through joint ventures) and iii) the percentage stake that ISUR holds in each of the joint ventures (normally between 50% and 70%).

In 2024e we estimate revenue of EUR 180Mn and EBITDA of EUR 30Mn

- **At the consolidated level, revenue growth (+13.5% CAGR 21-24e) will translate to similar growth in EBITDA to c. EUR 30Mn in 2024e (+12% CAGR 21-24e).** As a result of all the above, 2024e should see a company with consolidated revenue of EUR 180Mn (+13.5% CAGR 2021-2024e) and EBITDA of c. EUR 30Mn (+12% CAGR 21-24e), maintaining an EBITDA margin of 17.5% (similar to that seen in 2021; Table 1). Looking ahead to 2025e, the sharp increase in activity expected for the development business should drive 2025e revenue to > EUR 250Mn and EBITDA to c. EUR 50Mn (EBITDA margin 18.5%).

Despite the rebound in working capital investment, leverage will remain reasonable

- **And despite the rebound in investment, leverage will remain reasonable.** The high level of investment estimated for coming years will increase net debt to EUR 275Mn in 2024e (+38% vs 2021). Despite this, gearing will remain at reasonable levels with an average LTV for 2022e-2024e of < 45%, and EBITDA always higher than 3x interest (despite the estimated 250bp increase in the cost of debt).

***Table 1. Summary of sales and EBITDA margin***

| EUR Mn | 2020 | 2021 | 2022e | 2023e | 2024e | 2025e |
|---|---|---|---|---|---|---|
| Property development business | 98.0 | 83.6 | 90.3 | 115.3 | 117.3 | 193.0 |
| Rental Revenue | 13.3 | 15.4 | 17.3 | 18.1 | 18.7 | 19.2 |
| Construction | 18.5 | 22.7 | 15.8 | 23.7 | 41.9 | 46.3 |
| Administration and marketing | 2.9 | 3.5 | 3.7 | 4.8 | 4.9 | 8.0 |
| **Total sales** | **132.7** | **125.2** | **127.1** | **161.9** | **182.8** | **266.5** |
| COGS | (73.2) | (63.8) | (70.4) | (89.9) | (89.1) | (145.7) |
| **Gross margin** | **59.6** | **61.3** | **56.6** | **72.0** | **93.7** | **120.8** |
| *% over total sales* | *44.9%* | *49.0%* | *44.6%* | *44.5%* | *51.2%* | *45.3%* |
| **EBITDA** | **24.5** | **22.5** | **22.9** | **28.3** | **31.5** | **49.3** |
| *EBITDA margin (%)* | *18.5%* | *17.9%* | *18.0%* | *17.5%* | *17.3%* | *18.5%* |

Note: The large revenue growth in 2025e is basically explained by the larger number of deliveries of homes expected (c. 800 units vs 450 in 2023e and 2024e).

### E) In conclusion: a combination of businesses (development and property management) that allows ISUR to aspire to a significant increase in activity, limiting levels of risk

The snapshot that ISUR leaves us with is that of a resilient company that aspires to a significant increase in activity. However, in our view, what is really interesting are the factors that make this growth credible and attainable with less exposure to the residential property cycle. These factors are:

A company that aspires to a significant increase in activity…

- **A land bank that provides significant visibility and makes the step-up in size of the development business credible.** The current land bank will allow for the construction of +4,000 homes (of which 1,700 are already being marketed; 47% sold). In other words, the homes to be delivered during the estimated period will, in the majority, be on land in the land bank.

- **Vertical integration (with a construction company at the service of the development business).** Unlike other developers, ISUR has a 100% owned construction company (that only builds for ISUR and its developments via JVs), that should allow greater control of costs, quality and execution times (essential in the current context).

- **A property management business, with quality assets (with occupancy rates of c. 90%),** that provides a recurrent source of cash (with very high margins; > 70% in EBITDA). This reduces the company's risk profile. In addition, the value of the property assets provides greater comfort from a financial point of view as, if needed, ISUR could sell assets.

… with a resilient business model that provides a greater degree of visibility

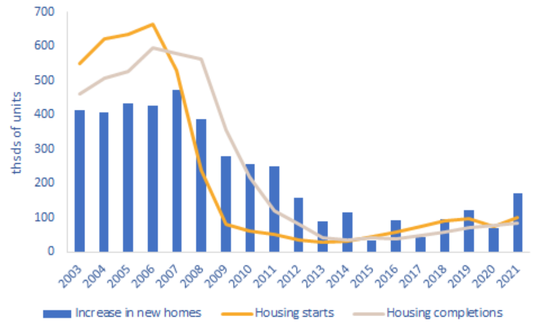
**In conclusion, an option to invest in the Spanish property sector with a combination of businesses that allows ISUR to aspire to a significant increase in activity, limiting levels of risk.** All the above are factors unique to ISUR that allow the company to weather periods of uncertainty (such as the present one) with a greater degree of visibility (both in terms of revenue and margins) and even take advantage of the low part of the property-development cycle to buy land at more attractive prices (that should improve the long-term return for shareholders vs traditional developers).

Trading at a discount of 60% vs the NAV (the largest of the listed developer sector)

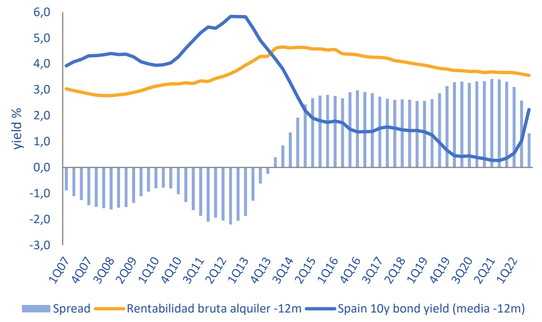
**Trading at a discount of 60% vs the NAV at September 2022e.** Obviously there is a risk of decreases in asset values against a backdrop of higher bond yields, but at the date of this report, ISUR is trading at a discount of 60% to its 9m22 NAV vs an average of 50% for the listed property developer sector in Spain and the large Spanish REITs. An apparently excessive discount that makes visible the opportunity that ISUR represents today in the Spanish property sector. A developer with a "safety net".

## The company in 8 charts

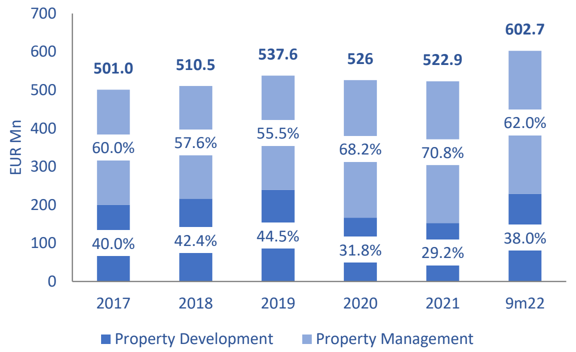
***Supply-demand imbalance: a long-term growth driver for the Spanish residential sector***



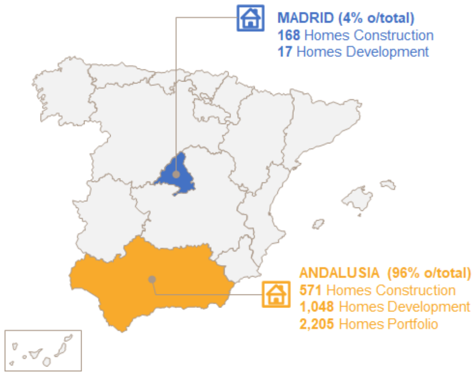

***Although the macro and interest rates will weigh heavy in the short term for the property sector***



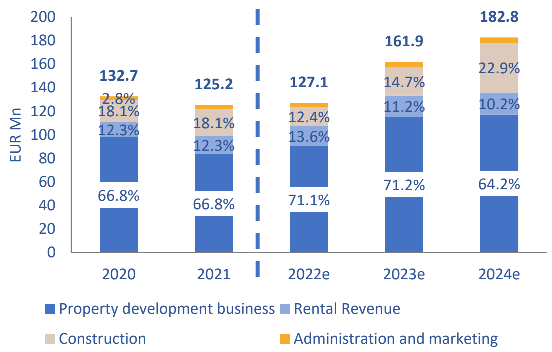

***ISUR: A unique property company, combining development and management businesses (both with significant weighting in GAV)***



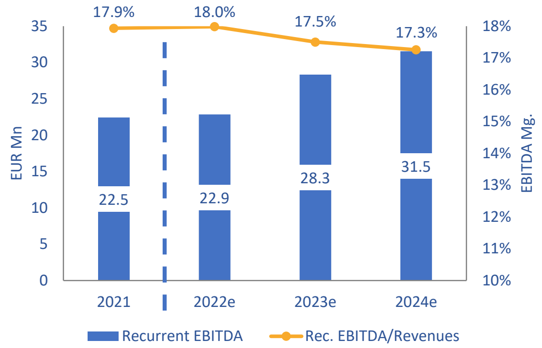

***With a land bank for building 4,000 homes (40% being marketed), maintaining unique exposure in Andalusia***



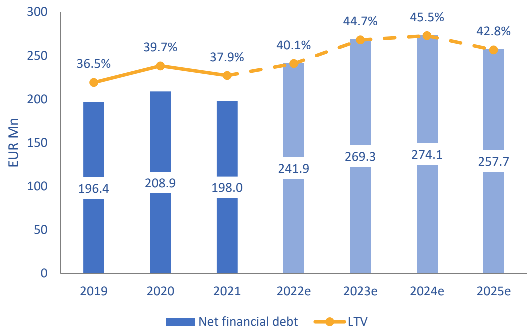

***2024e should see a company with revenue of EUR 180Mn…***



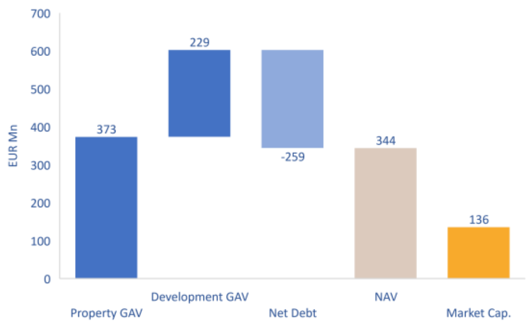

***… and EBITDA of c. EUR 30Mn (+12% CAGR 2021-2024e)***




***despite the rebound in investment, leverage will remain reasonable (LTV < 45%)***




***Trading at a discount of 60% vs the NAV at September 2022e***



## Business description

# A unique property company, combining development and management businesses thereby reducing risk

Inmobiliaria del Sur, Insur (ISUR), is a property group with headquarters in Seville, and a presence in Andalusia (where it has a leading position) and Madrid. It combines development activity (mainly residential) and property management, with a portfolio of rental assets (shops, office buildings and parking spaces; but no residential). It also has a construction company (100% owned) serving the development business, both for the development of proprietary developments and for those developed with third parties via joint ventures (allowing for greater control of costs, quality and deadlines). Founded in 1945, it has been traded since 1984 (since 2007 on the continuous market).

### The company's strategy involves carrying out a significant company the development business through alliances with third parties

So as to increase turnover and reduce risk, a large part of the development business is carried out through companies in which ISUR has a significant shareholding (usually c. 50%; Chart 1), considered joint ventures.

However, and as ISUR does not have control according to article 42 of the code of commerce of these joint ventures, they are consolidated by the equity method (according to the stipulations of IFRS 11). At the same time, and in order to reflect the true volume of the assets managed, ISUR carries out a quarterly conciliation between the financial statements under IFRS and the proportional consolidation method, **the method we use throughout this report (unless indicated otherwise)** as it enables a better analysis of the real size and performance of the activities carried out through JVs (increasingly important in the development business, and something that would be totally obscured by an equity method consolidation).

### At September 2022 it had a GAV of EUR 603Mn of which >60% corresponded to the property management business

ISUR operates via two main businesses; i) residential and tertiary development (67% of 2021 revenue; Chart 2) and ii) property management (12% of 2021 revenue), in addition to two complementary business serving the development business (both for proprietary developments and for those developed with third parties through joint ventures): i) construction (18% of 2021 revenue) and ii) administration and marketing (3% of 2021 revenue).

At September 2022 the appraisal of the asset portfolio (GAV) by the proportional consolidation method resulted in a total value of EUR 602.7Mn (+15% vs 2021; Chart 3), of which 62% corresponds to the property management business (shops, office buildings and parking spaces) and 38% to the development business. The 9m22 GAV was boosted by the acquisition of the 50% that ISUR did not own of Desarrollos Metropolitanos del Sur (a JV owned 50/50 with BBVA, acquired in June for EUR 18.2Mn).

ISUR closed September with a NAV of €18.4/share (+5.8% vs 2021), that means that at the date of this report, it is trading at a discount of 60% to its 9m22 NAV (Chart 5) vs an average of 50% for the listed property developer sector in Spain and the large Spanish REITs.

*Chart 1. Corporate structure*

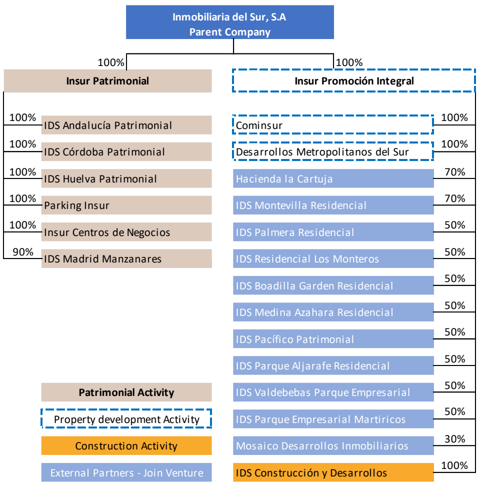



*Chart 2. Revenue mix by business (2021, proportional consolidation)*

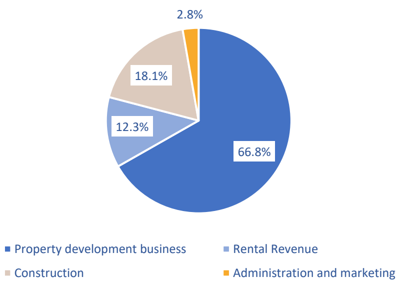



*Chart 3. GAV by business (2017-2021)*

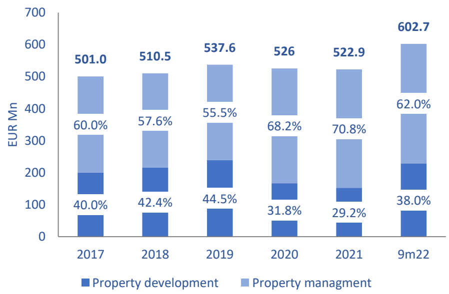



*Chart 4. NAV (2017-2021)*

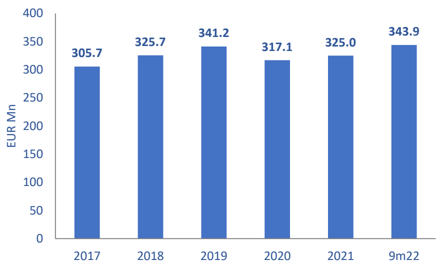



*Chart 5. Share discount vs NAV*

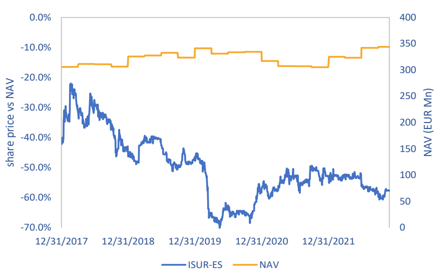
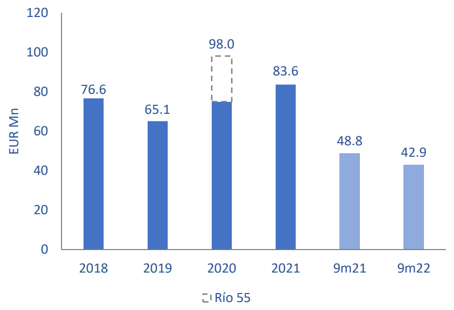


*Chart 6. Revenues of the property development business*




Note: 2020 development revenue includes the sale of the South building of the Río 55 business park (Madrid) for EUR 23Mn. Excluding this sale, development business revenue grew by 15.2% in 2021.

*Chart 7. Revenue from the construction business and the provision of services*

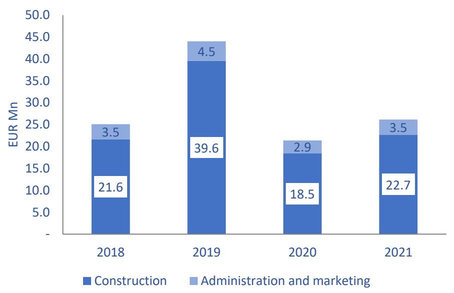
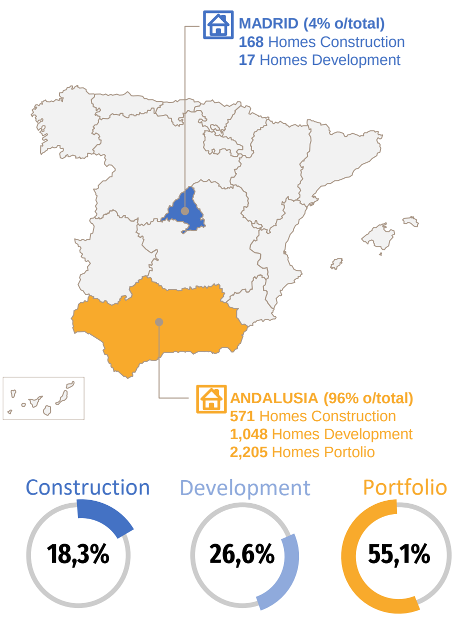



*Chart 8. Geographical mix of the development business*




## Development (67% of 2021 revenue; 38% of the GAV): a vertically integrated business, fundamentally residential, and with capacity for growth

The development activity, that represents the company's origins, has a scalable and flexible business model based (since 2016) on the company standardisation of processes and the execution of a significant number of its developments through joint ventures. This increases turnover (with larger projects) while at the same time diversifying risk. Also, in order to reduce development risk, ISUR buys land during downward stages of the cycle (as in 2008-2012), acquiring land that is shovel-ready or with no urban planning risk (treating land as a raw material rather than as a commodity).

In 2021 ISUR delivered 380 homes (71 of its own and 309 through JVs) with an average sale price (ASP) of EUR 320,000, resulting in revenue adjusted by the percentage in joint ventures of EUR 83.6Mn (+11.5% vs 2020; excluding the impact of the sale of the South building office block of the Río 55 business park in Madrid; Chart 6). At 9m22, ISUR had delivered 189 homes with an ASP of EUR 309,000.

Over 2019-9m22, the gross margin of the development business was between 27.5% in 2019 and 22% at 9m22 (vs a gross margin target of between 24.5% and 26%).

## In addition to the development business, the company has two complementary businesses: construction (18% of revenue) and the provision of services (2% of revenue)

ISUR has a construction company (100% owned) serving the development business (as a special purpose vehicle), both for the development of proprietary developments and for those developed with third parties via joint ventures, allowing for greater control of costs, quality and execution times (that should reduce gestation periods, in line with company strategy).

The revenue generated by the construction and administration and marketing businesses corresponds to the services provided by ISUR for developments carried out with third parties as joint ventures.

Specifically, in 2021 the construction business provided revenue via fees of EUR 22.7Mn (+22.6% vs 2020, reflecting the start of construction of new developments), with a margin of c. 2% that, together with fees received for providing administration and marketing services (EUR 3.5Mn in 2021; 2.8% of revenue) improved the profitability of the development business (with a +4p.p. increase in the EBITDA margin, estimated by Lighthouse).

## With a land bank for building 4,000 homes (40% being marketed), maintaining unique exposure in Andalusia

At September 2022, the development business had a GAV of EUR 229.3Mn (38% of the total), with a land bank for building 4,000 homes (Chart 8) of which 1,671 are already on sale (including those in finished developments pending delivery) with 47% having already been sold.

As regards the geographical mix of the land bank, after delivery in 2022 of a development of 80 homes in Extremadura (Caceres), at present ISUR's developments are located mainly in Andalusia (96% of the total; mainly in Seville and Malaga, although also in Granada, Cordoba and Cadiz; Chart 8), while Madrid still only accounts for 4% of the total land (10% if we include homes under construction and development). Company strategy is to increase the residential development activity in Madrid until this accounts for 40% of the total.

At September 2022, ISUR had 11 developments under construction, equivalent to 733 homes (18% of the total; Chart 8), of which 62% are in Andalusia and the other 23% in Madrid, and another 11 under development, equivalent to 1,065 homes. This provides enormous visibility, as sales for the next 6 years will come from the developments of the current land bank. In addition, ISUR has a land bank on the balance sheet that should allow for the construction of a further 2,205 homes (1,941 of its own and 264 via JVs).

***Chart 9. Annual presales (proportional consolidation)***

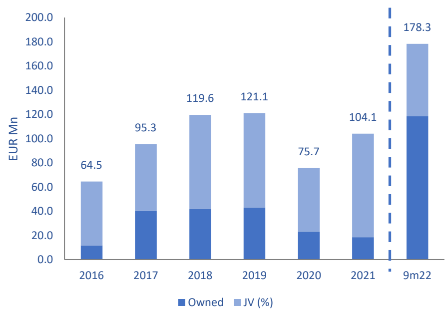



***Chart 10. Annual deliveries***

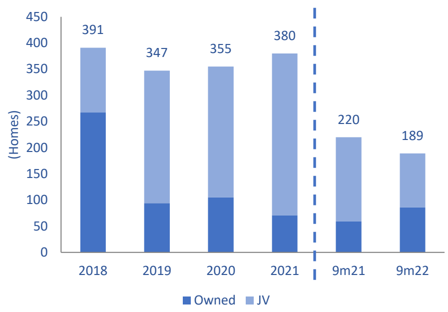



***Chart 11. Tertiary development***

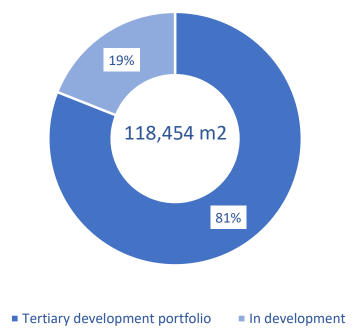
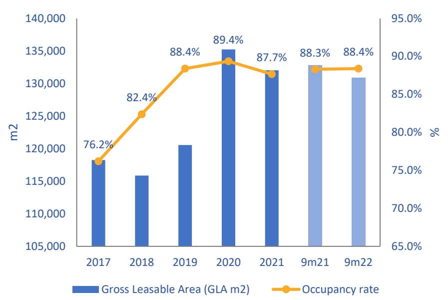



***Chart 12. Occupancy and gross lettable area of the property assets***




## Analysing developments in progress, most of the product is aimed at current demand (with more square metres, communal areas…)

With 22 developments in progress (of which 11 are already under construction), we analyse their location, sale prices, level of presales, etc. to give a realistic and illuminating vision of ISUR's development product.

By type of product, ISUR has both single- and multi-family housing developments. These are mainly projects aimed at the middle and high middle classes of the residential segment, of good quality, with communal areas and an average sale price of between €300,000 and €400,000/unit. In other words, the type of home currently in demand by the Spanish population (that due to the impact of the pandemic seeks larger homes with communal garden areas). In addition, the second home projects (c. 11-12% of the total) are located in areas such as Marbella, Estepona (Malaga) or the tropical coast of Granada, that have always attracted a large number of tourists.

As regards presales, at September ISUR had a portfolio of presales of 779 units for EUR 218Mn (EUR 178Mn proportionally; Chart 9), equivalent to 47% of the homes for sale. This represents 55% of the deliveries envisaged until 2024e. In fact, for 2023e 86% of deliveries have been pre-sold and for 2024e close to 40%, and 10% of homes to be delivered in 2025e have already been pre-sold.

Finally, the acquisition in 2022 of the 50% that ISUR did not control of Desarrollos Metropolitanos del Sur (a JV previously held 50/50 with BBVA) caused a significant change in the presales mix: now 70% of the developments are proprietary.

## In addition, the development of assets for tertiary use will drive business growth and diversification. Although not before 2024e

In addition to its current residential developments, ISUR has five large tertiary developments in progress (118,454 m2) that will represent a significant driver for the development business, both in terms of volume (Chart 11) and mix, as they will increase its exposure to Madrid that accounts for c. 40% of the square metres in development; although not before 2024e. These projects are:

- **Ágora (Malaga city),** 9,500 m2 of office space and slated investment of EUR 31Mn. Permit already obtained in 3Q22.
- **Martiricos (Malaga city),** 10,900 m2 of office space and slated investment of EUR 31Mn.
- **A hotel project in Atlanterra (Tarifa, Cadiz),** 30,000 m2 of building space and slated investment of EUR 66Mn.
- **A project in Las Tablas (Madrid),** 9,000 m2 of office space and slated investment of EUR 39Mn.
- **A business campus in Valdebebas (Madrid),** 36,500 m2 of office space and slated investment of EUR 100Mn.

## The property management business (12% of revenue; 62% of the GAV): a recurrent business with high margins (offices). Gross yield 4.9%

In September, the GAV of ISUR's rental asset portfolio was EUR 373.4Mn (62% of the total) including 130,900 m2 of offices, commercial premises and over 3,000 parking spaces (Chart 12), mainly in Andalusia, where it is the leader of the offices market in prime locations in Seville.

Also, in recent years ISUR has significantly increased the presence of the business in Madrid (that at the date of this report already accounts for c. 20% of the total rental assets portfolio), including the development and subsequent management of the Rio 55 project, located inside the M-30 ring road in calle Virgen del Puerto (comprised of two buildings with a surface area of 27,500 m2 and 400 parking spaces all surrounding a large green area; in 2020 one of the buildings was sold (EUR 46Mn; EUR 23Mn in proportional consolidation) with the North building currently being let to BNP).

***Chart 13. Revenues of the property management activity (2018-9m22)***

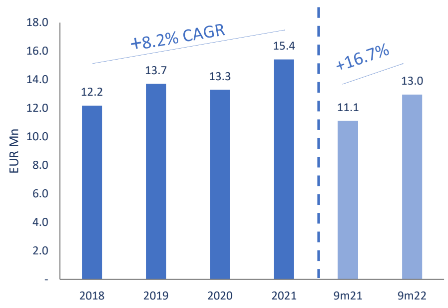
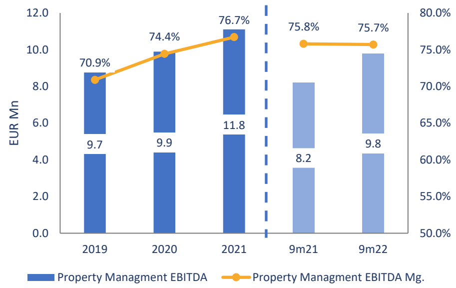



***Chart 14. EBITDA and EBITDA Margin of the property management activity (2018-9m22)***




The rental assets portfolio is comprised of complete buildings (ISUR owning 100% of these except for IDS Manzanares, where it owns 90%), that enables greater control and more effective administration. In this business EBITDA generation depends mainly on: (i) rental prices, ii) occupancy levels and iii) the management of direct costs associated with renting and indirect expenses (administration and structure).

In 2018-2021, ISUR's property management business saw revenue increase to EUR 15.4Mn (+8.2% CAGR 2018-2021) mainly due to: i) the increase in the occupancy rate to close to 90% in 2021 (vs 82% in 2018) and ii) the increase in the gross lettable area to 130,000 m2 (+12.9% vs 2018) mainly due to commencement of the letting of the north building of the Río 55 project (c. 14,000 m2 of office space). At September 2022, occupancy improved to 88.4% (+0.7p.p. vs 2021) and the annualised rent from ongoing leases was EUR 18.6Mn (+6% vs 2021; a gross yield of 4.9%).

In terms of EBITDA (stripping out the impact of the sale of property investments), the property management business recorded very high margins (> 70% over 2019-9m22; Chart 14).

Finally, we would point up that ISUR's property investments are carried at cost (not fair value) with unrealised capital gains of EUR 153Mn at the 2021 close (EUR 114Mn net of tax). The company's strategy involves increasing the size of the property management business, developing assets from their construction (and so capturing the added value of the entire process), and increasing the weighting of the business in Madrid, accelerating the asset rotation program to grow in this market.

## The combination of the development and property management businesses generates high margins (2021 EBITDA margin, c. 18%)

As a result of all the above, in 2021 the company generated consolidated revenue of EUR 125.2Mn (Chart 15), of which 67% corresponded to the development business, 21% to revenue from construction and the provision of services (serving the development business) and 12% to the property management business.

Procurements correspond to the cost of sales of the development business (gross margin of the development business c. 24%). Operating costs are largely associated with the company's own construction activity (57%); and this item plus the marketing and structural costs of each development represents c. 80% of the overheads of the business. The other large component of costs is the operating and structural costs of the property management business (9% of operating costs) and structural costs at the corporate level (very stable over time: c. EUR 4.5Mn/year, 11% of operating costs).

Over 2019-2021 ISUR generated a Recurrent EBITDA margin of c.18% (Chart 16). This EBITDA margin is in line with those of the main listed Spanish property developers (17.5% and 17.3% for AEDAS Homes and Neinor Homes, respectively), although achieved with a lower level of volatility/risk (due to the recurrence and stability provided by the property management business).

***Chart 15. Revenue mix (2018-2021)***

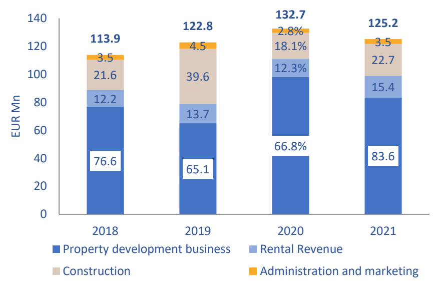
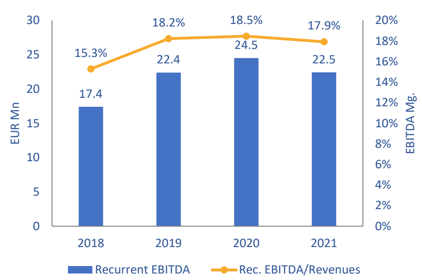
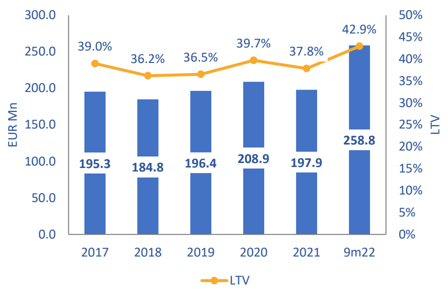



***Chart 16. EBITDA and EBITDA Mg. (2018-2021)***

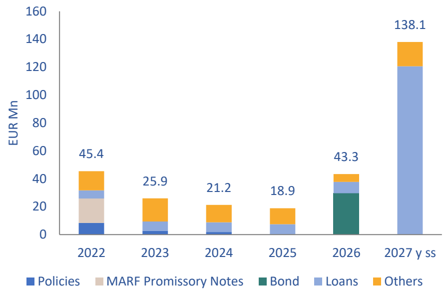



Note: 2020 recurrent EBITDA adjusted to strip out the non-recurrent impact of impairments (EUR 5.1Mn).

### Chart 17. Net Debt and LTV

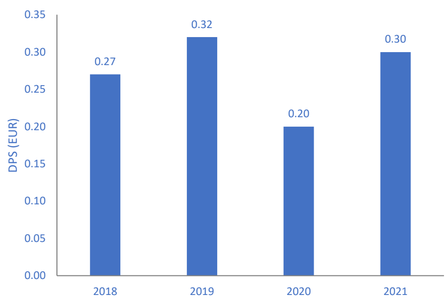



### Chart 18. Debt maturities (2021)

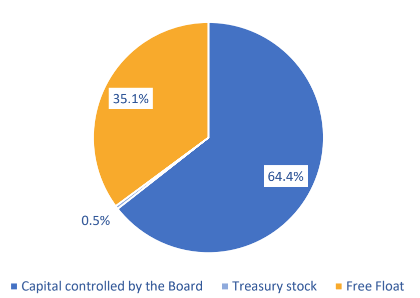



Note: Others includes financed payments, subrogatable mortgage loans, land loans, other loans, financial leases and accrued interest payable.

### Chart 19. Dividend per share (2018-2021)




### Chart 20. Shareholder structure




## At the 9m22 close ISUR's gearing was 43% of the GAV

ISUR has maintained a healthy balance sheet structure in all stages of the cycle (including the big property crisis of 2008), always keeping its gearing within prudent limits (LTV < 40%), with 2021 EBITDA that was over 4x interest (vs 2.5x in 2018).

The large investments made in 9m22 on buying plots of land (EUR 34.5Mn) and the acquisition of 50% of DMS (EUR 23.4Mn net of debt and cash) increased 9m22 net debt to EUR 258Mn (+30.8% vs 2021), a level of debt that implies a LTV of 42.9% (vs 37.8% in 2021; Chart 17) and that should decrease slightly in the last quarter of the year due to the deliveries of developments programmed.

The company's gearing is higher than the average for listed developers in Spain (LTV < 20%) explained by the large weighting of the property management business in the value of its assets (c. 60% of the GAV), a more recurrent business that admits higher levels of debt than those borne by an exclusively development business.

As regards the composition of the debt, in 2019 a syndicated loan was executed for EUR 110Mn with a maturity of 10 years aimed at strengthening the financial structure of the property management business and reducing its costs. In addition, in December 2021 the company issued a MARF bond for EUR 30Mn with an annual coupon of 4% and maturity in 2026 (BBB- rating by Axesor) to boost the development business. In the issue's schedule of maturities, c. 60% of these are from 2026 (Chart 18). In addition, ISUR's strategic plan envisages a capital increase of up to c. EUR 60Mn to boost the growth of its businesses.

## ISUR has paid a dividend for the last 30 years (payout c. 45-50%)

Apart from 2012, ISUR has paid a dividend each year for the last 30 years. The current dividend policy is to pay out between 45% and 50% of consolidated profit after tax. In 2021 ISUR paid out a total dividend of 0.30 euros per share (EUR 5.6Mn; payout c. 45%, dividend yield of 3.8%).

In addition, ISUR has approved a treasury stock buyback programme for a maximum amount of EUR 5Mn to satisfy the variable remuneration of the management team and as a complement to shareholder remuneration. The maximum number of shares to be acquired is 375,000 (2% of the share capital), c. 25% of which will be allocated to the variable remuneration plan and the rest to reducing capital via the redemption of treasury stock to complement shareholder remuneration.

## Alignment of interests between the owners and management: the Board of Directors controls c. 64% of the capital

The board directly and indirectly represents c. 64% of capital. Specifically, board members control 23% of the capital, while other shareholders linked to this (in general relatives) control a further 41%. The controlling shareholders have not changed in practice throughout the history of the company and seem to be in it for the long run so changes to the shareholder structure are not, a priori, a factor to take into account.

A significant shareholding is held by the Pumar family (one of the company's founding families with a c. 30% shareholding) who have a presence both on the Board of Directors and the management team, holding, among others, the positions of Chair of the Board and Managing Director.

The free float is 35.1% (Chart 20). Although not including small shareholdings (< 3%) associated with the Board, the free float would increase to c. 51%.

## In conclusion, a property company with a unique business model that offers the possibility of playing the development business in a safer way

Having reached this point, we would ask: What is ISUR today? How does it generate Cash Flow?

- **A unique business model,** combining development activities (with the capacity to deliver c. 350 homes/year) and a property management business (130,000 m2 of office space, hotels and commercial premises), both with a significant weighting in terms of GAV (38% development – 62% property management).

In our view, the stable generation of rents by the property management business (c. 45% of EBITDA in 2021) allows for greater patience in the development business, acquiring land during the downward stages of the cycle (as demonstrated in 2008-2012).

- **Vertically integrated,** with a construction company, 100% owned and serving the development business, that allows for greater control of costs, quality and execution times. In addition, ISUR develops its property assets from their construction, capturing the added value of the entire process.

- **A significant part of the development business is carried out through joint ventures,** with three objectives: (i) to take on larger projects, (ii) to improve the profitability of the investment (by providing the joint ventures with construction and administration and marketing services) and (iii) to diversify risk.

- **A local focus, in markets where the company has significant experience:** combining a strong position in Andalusia (mainly in Seville and the city of Malaga), where it is a leading player in both development and office rental, with growth in Madrid (the most dynamic property market in Spain).

- **A reasonable level of debt (LTV < 40%).** Gearing is higher than the average for listed developers in Spain (LTV < 20%) explained by the weighting of the property management business in the value of its assets (c. 60% of the GAV). The refinancing of debt in 2019 (under more favourable conditions) has delayed 60% of maturities to 2026.

- **Alignment of interests between the owners and management.** Controlling shareholders have not changed in practice throughout the history of the company and have a presence both on the Board of Directors and the management team.

In our opinion, ISUR is an option to play the Spanish development business, with very local exposure (concentrated in Andalusia and Madrid), in a safer way: due to the combination of the development and property management businesses. This is a combination that provides a recurrent source of revenue and cash that gives the business greater resilience and the ability to self-fund growth, maintaining a level of debt that is proportional to the payment capacity of the rents generated by the property management business although obviously this strategy also reduces, mathematically, the potential that could be generated by an acceleration of the Spanish residential cycle (compared to a business that is 100% development).

# Property: the macro will weigh heavy in the s/t. But in the l/t the imbalance between supply and demand is a growth driver

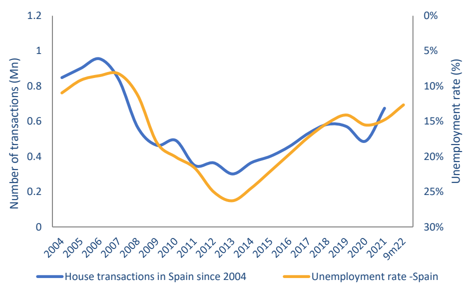
Investors usually view a country's property sector (offices, shopping centres, residential…) as a proxy of its economy, so, if the macro is doing well the property sector also does well (P/L, stock market) and vice versa. This is a totally logical correlation as demand dynamics are quicker and pre-empt supply ones (that are very rigid). This correlation is also applicable to the residential property market (where it is, in fact, even greater).

## The macro is (and will be) the most important variable for the property sector

We won't go into detail regarding the future of Spain's macro but the most recent indicators show clear signs of weakening. Although for 2022e as a whole GDP growth is expected to be 4.5%, negative growth is already expected for 4Q. For 2023e, most of the research services compiled by Funcas have downgraded their estimates for GDP growth, the consensus forecast being 1.1%. The consensus estimate for inflation, however, has been upgraded to 8.7% for 2022 and 4.1% for 2023.

As regards employment in Spain, after recording a maximum unemployment rate of c. 27% in 1Q13, the good progress of the economy since 2014 has reduced this to 12.7% in September 2022 (which will have stimulated the Spanish property sector in recent years; Chart 21). According to consensus estimates compiled by Funcas, the annual average unemployment rate in 2022e will fall to 13% (three tenths of a point less than in September) and will remain at this level in 2023 indicating a stagnation of the decline in unemployment.

*Chart 21. Housing transactions vs unemployment rate (2005-3Q22)*




Note: Unemployment rate (rh scale, inverted).

*Chart 22. Spain GDP (% var QoQ)*

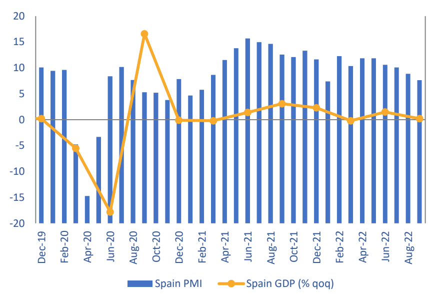
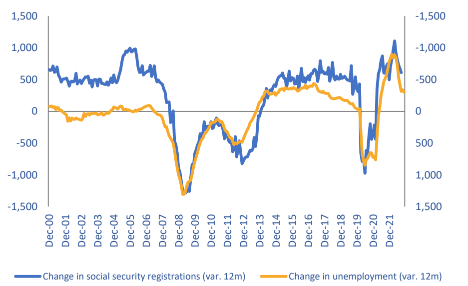



*Chart 23. Change in unemployment*




## Also of great importance are interest rates, that have never before risen so quickly and decisively (up by 2.5% in just five months)

Monetary policy directly impacts the property market due to the effects of fluctuations in interest rates on demand and of this on property prices. While for commercial property the fixed income market and the yield on the 10-yr bond are much more important for asset values, for the housing market the most important variable are short-term rates, with most Spanish mortgages being indexed to the 12-month Euribor rate.

The current toughening of monetary policy is causing a sharp increase in interest rates, making borrowing more expensive for families and companies. At the last ECB meeting (December 2022), a 50bp increase was agreed for the three interest rate indicators. There has never been such a quick and decisive increase in interest rates since the euro came into existence (Chart 24), with rates rising in just five months from zero to 2.5% (their highest level since 2009) and everything suggests rate hikes are set to continue.

The 10-year bond yield is 3.4% (vs 0.56% at the end of 2021) and the 12-month Euribor rate has risen to 3.2% (vs -0.5% at the end of 2021), narrowing the spread between the return on rental housing and the average fixed income yield in the last 12 months to 1.8% (Chart 25; the spread to the bond at the date of this report is 0.2%).

*Chart 24. ECB key interest rates vs 12-month Euribor*

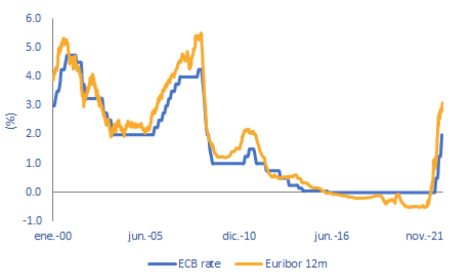



*Chart 25. 10-yr Spanish bond yield (12m average) vs rental yield*

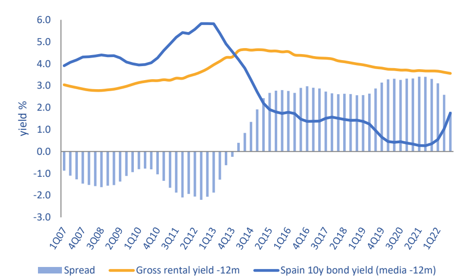
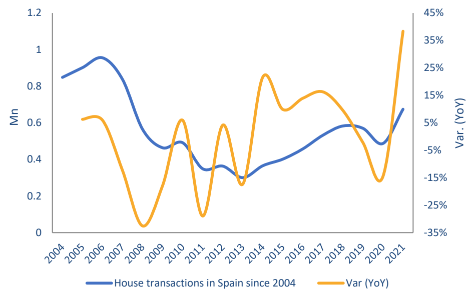


***Chart 26. Number of housing transactions in Spain (2005-2021)***



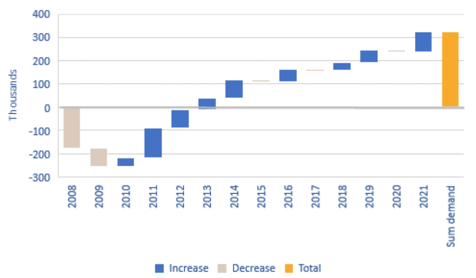

## Residential market: since 2014 there has been a sustained recovery in demand (reaching highs in 2021 not seen since 2007)…

The economic crisis of 2008 caused demand in the residential segment to slump, falling from nigh on a million transactions a year (including new and used housing; Chart 26) to c. 300,000 transactions a year in 2013. The recovery began in 2014, with the improvement in employment, easier access to credit, the recovery of confidence in the economy and clearly unsatisfied demand after so many years of crisis.

Specifically, according to government data, there were 373,145 housing transactions in 1H22 (+10% vs 2021 and +37% vs 2019). So we could end 2022 with a volume of transactions of over 700,000 (exceeding 2021, the best year since 2007). However, persistently high inflation continues to cloud prospects for 2023e, a year for which the forecasts are not so optimistic. In fact, demand is already showing signs of weakness (the number of transactions grew 6.9% yoy in September vs rates of > 30% at the beginning of the year).

By markets, in recent years Andalusia and Madrid (where ISUR operates) have accounted for 20% and 18% of new private housing transactions in Spain, respectively, and an average of 19% (Andalusia) and 13% (Madrid) of used housing transactions.

***Chart 27. Supply and demand (growth in the number of households vs housing completions)***




Source: Lighthouse from Mitma data (2022). An increase in the chart above implies higher growth in the number of households vs housing completions.

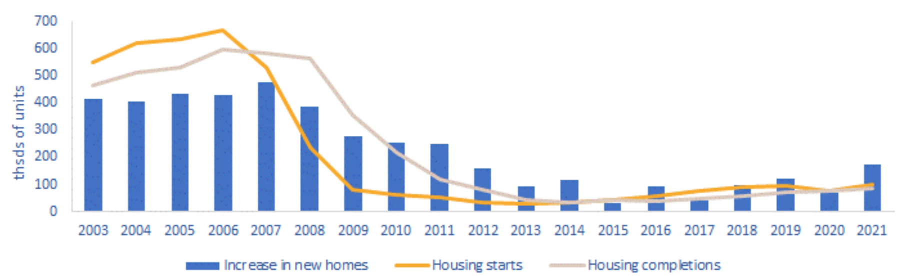
.

## … with a supply that is still limited (private housing starts remain around 100,000 units p.a.)

As is well known, the slump in demand in 2008 led to a severe crisis in the Spanish property sector, with a sharp contraction in the number of housing starts (-85% 2009 vs. 2006), bottoming out in 2013 (<30,000 units).

In 2021 the number of private housing starts increased to c. 100,000 (+32% vs 2020, due to the impact of the pandemic and +4.4% vs 2019). This level remains well below the highs reached pre-2008 crisis (c. 650,000 in 2006; Chart 28) and below expected growth in demand: in 2021 the average number of households grew by c. 172,000 (+0.9% vs 2020). Over 2008-2021 the increase in new households exceeded (in cumulative terms) the number of private housing completions by c. 300,000 (Chart 27).

***Chart 28. New households vs housing starts and housing completions in Spain***

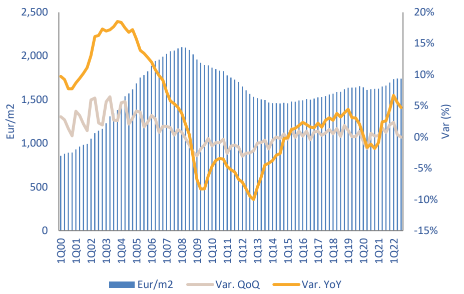



Source: INE (2022)

As regards growth in households (one of the main variables used to extrapolate demand for housing), the National Statistics Office predicts a CAGR of 0.9% for the next 15 years (implying the creation of 180,000 new households a year). This growth is set to be led by the Balearics, Murcia and Madrid (with CAGRs of 1.3%-1.6%) and with an expected increase for Andalusia of a 0.9% CAGR (fully in line with that expected for the national market average). This means that if the current number of housing starts is maintained (c. 100,000), supply will continue to be lower than demand. In fact, the number of new building permits (109,000 homes in the last 12m to August) is smaller than the net creation of households (206,000 -12m to September 2022).

What's more, supply-side limitations such as the lack of building sector capacity (due to the difficulties in finding labour), the lack of building land and uncertainty regarding the new housing law, will continue to have a negative effect in the short and mid term. This explains why now the problem is a lack of stock and not excess supply (as occurred in 2008).

***Chart 29. Price per m2 of housing in Spain***




Fuente: MITMA

## Driving house prices upwards, by 4.7% in 3Q22, although these are still c. 20% below the previous peak

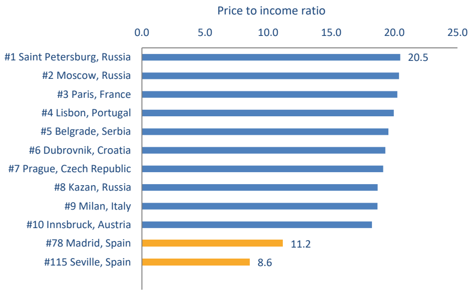
From lows of 2014, house prices rose 19.2% to September 2022 although despite the recovery of prices, these are still a long way from the historical highs reached in the previous cycle. In general, the price per m2 of residential property in Spain is on average 20% below the prices of the previous peak (March 2008; Chart 29).

According to Spanish government data, at the September 2022 close, house prices in Spain had risen 4.7% yoy, already exceeding levels of September 2019 by 6.2%, and although these continue to increase at high rates, as the year advances the slowdown in yoy terms is clear: +6.7% in 1Q, +5.5% in 2Q and +4.7% in 3Q22. A deceleration of house prices that, in qoq terms, could already be anticipating a cooling of the property market (in 3Q22 the appraisal price for private housing remained flat at +0.0% qoq, Chart 29); a trend that should continue in 2023e due to the sharp rise in interest rates.

By regions, both the Balearics (+7.3% yoy) and the Madrid region (+7.0%) saw high growth. In Andalusia, house prices grew by 4.6% yoy in 3Q (with growth in Seville, Malaga and Granada, where the bulk of ISUR's portfolio is concentrated, of +2.9%, +7.4% and +5.9%, respectively). However, it is important to stress that given the large number of nuances in the housing market (no two property assets are the same) and that supply and demand dynamics are local, average prices only offer a partial view.

## And the housing purchase affordability rate has been growing continuously since 2013

***Chart 30. Price of housing over household income (net of tax)***




Source: Numbeo

The increase in house prices by more than the increase in salaries in recent years, plus more expensive financing since 2022, is eating into families' purchasing power, making the relationship between house prices and household income worse.

The housing purchase affordability rate for Spanish households (calculated as the ratio in years between the average house price and the estimated gross income per household) has been growing continuously since 2013. According to Bank of Spain data, at the September 2022 close, the housing purchase affordability rate for Spanish households was equivalent to 8.2 years of gross income per household. Although this figure is still well below the high of 9.4 years reached in 3Q07, it already exceeds the average for the period between 2005 and 2Q22 (average of 7.7 years; Chart 32) and will continue to increase in coming months.

***Chart 31. Income spent on house purchasing (1T05-2T22)***

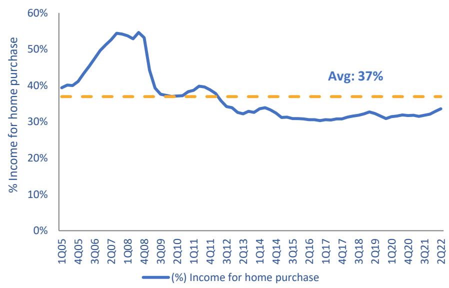
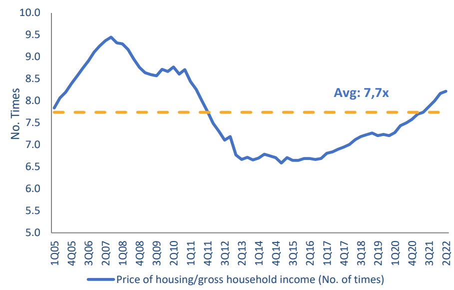



***Chart 32. House prices over gross household income***




Source: Bank of Spain.

Despite the increase in the percentage of income spent on buying a house to 33.6% in September 2022, this remains at levels close to historical averages (c. 37% since 2005), unlike the situation prior to the crisis of 2008 when a family would spend c. 50% of its income on its monthly mortgage instalment (Chart 31).

Finally, comparing prices over income for a sample of 150 cities in Europe, we see that both Madrid and Seville are clearly lagging in terms of prices (Chart 30).

## Rate hikes suggest a correction for the property sector although the sector is facing the current uncertainty in good conditions

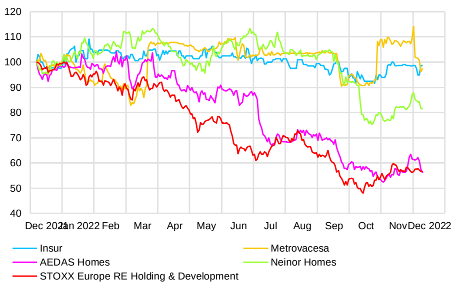
The macro remains the most important variable for the property sector. Growth expectations are lower now than those expected a few months ago and interest rates have risen more than initially expected. The threat of recession is rearing its ugly head and the increase in mortgage rates plus the impact of inflation on disposable household income suggests that in coming quarters we will see a decline both in house prices and in housing transactions.

However, since 2014 the Spanish market (one of those most affected by the bubble) has seen moderate organic growth in line with growth in the economy. Unlike the crisis of 2008 (caused by surplus supply and hyper-indebtedness in the sector, leading to the bankruptcy of many developers), the current situation finds the Spanish property sector in a healthy position. In fact, the credit crunch after the financial crisis has led to a more solvent profile both for families and developers, leaving them in a better position than in the past. What's more, the surplus of savings accumulated by households during the pandemic, plus a supply that will remain limited (and weaker than relatively strong demand), should help to underpin consumption and investment.

We would point up a risk to monitor in coming quarters: the continuation of rate hikes could result in an even bigger worsening of the housing purchase affordability rate (now at slightly higher levels than the average since 2005), that would weaken the market restricting demand (and causing an increased slowdown in prices).

## And the stock market performance of the main listed Spanish property developers has been very disparate: why?

*Chart 33. Main listed developers in Spain vs sector in Europe*




Source: Facset

Now there is only one question: What impact will this situation have on the market value of property developers? In the last year the market performance of the main listed Spanish property developers has been very disparate (Chart 33). On the one hand there is AEDAS Homes and Neinor Homes (more exposed to the property development cycle) with cumulative losses in the last 12m of -44% and -21%, respectively. And on the other, Metrovacesa (the listed property developer with lowest gearing: LTV c. 6.5x) and Insur (with a property management business that accounts for c. 60% of the GAV and provides more recurrent and stable cash generation; enhancing its risk perception) with losses of -10% and -5.5%, respectively. In addition, ISUR is currently trading at a 60% discount to its NAV, the largest among listed property developers in Spain (average of c. 50%) vs a discount of 50% for the REITs, that could explain its outperformance vs the sector.

Obviously, the worsening of the Spanish macro together with rising interest rates (that have a direct impact on the housing purchase affordability rate and will mean higher discount rates for property assets) will impact the property sector's performance. And in the short term the risk of revision is on the downside for the following reasons: i) a higher cost of mortgage financing, (ii) a lower household savings rate and (iii) a loss of attraction of investment in rental housing (vs alternatives such as government bonds).

In conclusion, in the short term a weakening of demand would seem inevitable (due to rising interest rates and a worsening of the economic situation) and the result of this is as yet unknown. However, the sector is facing the current uncertainty in good conditions (both families and property developers are in a more solvent position than in the past). Looking to the longer term, supply will continue to be scarce (and lower than demand) and, in our view, this will in itself be a growth driver for the property development sector (once the current uncertainty has receded).

As we have said on other occasions, you don't have to be a financial analyst to know that the current weakness of the property sector is not going away until the macro uncertainty begins to lift. So, whilst the current situation continues, the sector is unlikely to recover the losses of the last year although all the negative impact the macro can have, as it is well-known (and even obvious), should already be priced in.

### Offices: available supply has been and will continue to be the main factor shaping rental prices (and the dynamics in Malaga at present seem especially attractive)…

ISUR has exposure to the office market (mainly in Seville, but also in Malaga and Madrid, where its main projects under development are located). ISUR's property management business (mainly offices and commercial premises) represents c. 60% of its GAV and its rental leases generate c. 50% of EBITDA (providing recurrence and acting as a safety net for the company's cash generation capacity).

Our analysis focuses on the supply of available space as this has been and will continue to be the main factor shaping rental prices. By geographies, according to CBRE data, the office market in Seville has very high availability (c. 25%), although this is only 5% for prime buildings. The CBD and Cartuja (where a large part of ISUR's office portfolio is located) are still the areas with the highest rents in the city, with prime rents (an average rent of c. 12 eur/m2 that can reach close to 17 eur/m2 depending on the quality of the building).

In Malaga, where c. 25% of ISUR's office projects under development are located with 20,400 m2, the availability of space is very limited (c. 4%) as a result of the lack of development of office buildings and the growing interest being shown in the city by tech companies. Availability declines to 1.5% in the most central areas of the city, the CBD being the most in demand (with similar rents to Seville, although the lack of supply should continue to push these upwards).

In Madrid (where ISUR has developments in Las Tablas and Valdebebas, both outside the M-30 ring road), the supply of office space remains high, with the average vacancy rate still at 11.6% at the 3Q22 close (-50 bp vs 2Q22). As regards rental prices, the average rent in Madrid is c. 20.2 EUR/m2 (+9.6% yoy) and the prime, the highest in Spain, is c. 36.7 EUR/m2 (+3.5% yoy), still below levels of 2008 (in La Castellana office rents at one time reached 46-48 EUR/m2).

### … although the current macro situation will make it difficult for rents to rise so investors need to be picky (quality assets have the best prospects)

Although we do not expect the current cooling of the economy to allow a generalised increase in rents in the office market in Spain, this doesn't mean that in certain areas there won't be increases in rents. Remember that not everything in the CBD is good or everything in the periphery is bad (making generalisations in the property sector always leads to errors). Accordingly, we think that at this stage of the cycle buildings of a certain quality where there could be problems of supply are those that have the best prospects (location, including Business District areas considered premium; energy certificates B+ and A; sustainability…). According to research carried out by CBRE, certified buildings have an average rental premium at five years of between 13% and 29%.

The contraction of yields finally seems to have bottomed out. In October the yield on premium office assets in the Madrid CBD was 3.75% (vs 3.25% previously, the lowest of the historical series) although this is still below levels seen during the boom of 2007 (3.9%). And after the strong rebound in sovereign bond yields in 2022 (Spanish 10y bond: 3.4%), the spread to fixed income has narrowed significantly. This should lead to investors demanding higher returns on assets (pushing valuations downwards). In other words, it does not seem logical to invest in property now expecting further declines in yields, reaffirming our opinion that in this context investors need to be especially selective regarding the type of asset/company they invest in

# The current land bank guarantees a significant increase in activity... but not before 2025e

ISUR is a small property company whose management team has significant experience in the sector, with a unique business model that combines housing development with a property management business (both with a significant weighting in terms of GAV; something that is unusual in the sector at present).

There is no doubt that in the last year the scenario for the residential segment has become more difficult. Competition has intensified both in land buying and in the marketing of homes (with more developments for sale) and the fast and decisive increase in interest rates could cause demand to slow down in the short term. In this context, there is only one question: What can we expect from a property company like ISUR in terms of operating results and cash generation?

## 2021-2024e: the land bank and level of presales point to an acceleration of growth in the development business (development revenue: +12% CAGR 21-24e)

According to 9m22 results, ISUR has a land bank that should allow for the construction of 4,000 homes, of which 1,700 are already being marketed (47% sold; including finished developments pending sale). A portfolio of presales (779 homes) that, at the September close, was worth EUR 218Mn (EUR 178Mn in proportional consolidation) and that represents a coverage of approximately 50% of our estimate for deliveries until 2025e, increasing the visibility of the business for the next three years. The main assumptions behind our estimate for revenues from the property development business are:

- **Delivery of 2,450 homes in 2021-25e:** Although in 2022e we estimate a similar level of presales to 2021 (370-380 units), the 11 developments in progress (1,100 homes) and the portfolio of presales suggest an acceleration of growth from 2023e; although we will have to wait until 2025e to see levels of deliveries close to 800 homes/year (Table 1; that will represent a genuine step-up in scale for the company). A conservative assumption that implies the delivery of 2,450 homes in 2021-2025e (vs the target of c. 2,900 included in the company's strategic plan).

- **Change in the ownership mix of developments (with an increased weighting of proprietary developments vs those executed via JVs).** The acquisition of DMS caused a significant change in the 9m22 portfolio of presales, increasing the weighting of proprietary developments to 65% (vs 20% at the 2021 close). This is something that will impact the mix of future deliveries. We estimate a 60%/40% mix of proprietary developments/JVs in 2022e and 2023e, changing to c. 40%/60% from 2024e (Table 1).

- **With an average sale price of 320,000 euros.** The average sale price of homes delivered in the period 9m22 was 309,000 euros. We estimate an increase in sale prices from 2023e to close to 340,000 euros/unit mainly due to the higher percentage of deliveries of homes in Madrid from 2023e (prices c. 25% higher).

*Chart 34. Deliveries and mix of deliveries*

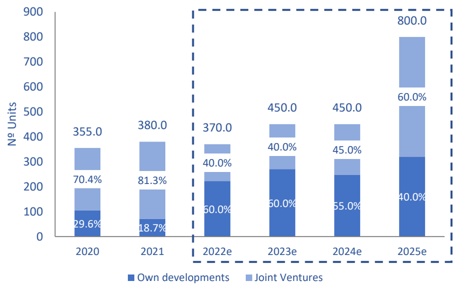



*Chart 35. Revenues of the property development business*

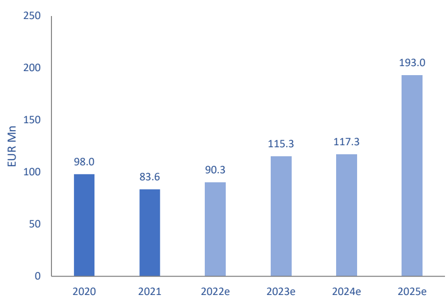



*Table 1. Estimates for the development business (2020-2025e)*

| EUR Mn | 2020 | 2021 | 2022e | 2023e | 2024e | 2025e |
|---|---|---|---|---|---|---|
| Nº Units | 355.0 | 380.0 | 370.0 | 450.0 | 450.0 | 800.0 |
| *Own units (%)* | *29.6%* | *18.7%* | *60.0%* | *60.0%* | *55.0%* | *40.0%* |
| *Joint venture units (1) (%)* | *70.4%* | *81.3%* | *40.0%* | *40.0%* | *45.0%* | *60.0%* |
| Selling price (thousand euro unit) | 342,656 | 320,113 | 305,000 | 320,250 | 336,263 | 344,669 |
| *% change* | *-2.3%* | *-6.6%* | *-4.7%* | *5.0%* | *5.0%* | *2.5%* |
| **Total sales** | **98.0** | **83.6** | **90.3** | **115.3** | **117.3** | **193.0** |
| | | | | | | |
| **Gross margin** | **24.8** | **19.8** | **19.9** | **25.4** | **28.1** | **47.3** |
| *% over sales* | *25.3%* | *23.6%* | *22.0%* | *22.0%* | *24.0%* | *24.5%* |

Note 1: ISUR has stakes of between 50% and 70% in its joint ventures.

***Chart 36. Gross margin of the property development business***

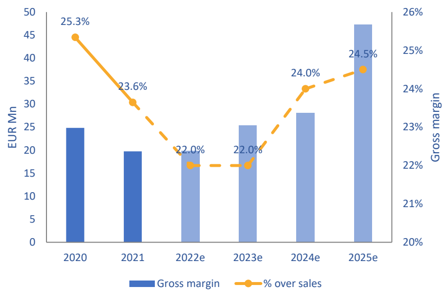
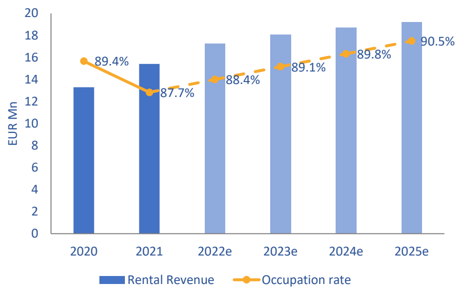



***Chart 37. Revenue from the property management business and occupancy rate***




- **Although the current context will squeeze margins in 2023e.** Margins are coming under pressure from the prices of shovel-ready land and of building materials. And, although ISUR's business has certain peculiarities that should protect its margins (vertically integrated business with a 100% owned construction company and a land bank that should allow for the construction of +4,000 homes), the truth is that margins suffered in 9m22 results: 9m22 gross margin of 21.7% (vs 24.7% in 9m21).

  Although we do not expect this pressure on margins to grow moving forward, we think it will continue in 2023e leading us to estimate a gross margin for the property development business of c. 22% in 2022e and 2023e (Table 1). However, the increase in the mix of deliveries of developments via JVs (with higher margins) and the normalisation of building materials prices will allow the gross margin of the property development business to return to c. 24% by 2024e.

All the above can be summarised in a development business that, assuming a conservative scenario (the current context invites prudence), should aspire to levels of deliveries of, at least, c. 450 homes in 2024e, with revenue of c. EUR 120Mn (+12% CAGR 21-24e). And, looking further ahead, should exceed 600 deliveries of homes from 2025e (2025e revenue > EUR 145Mn). A significant step-up in size bearing in mind that in 2021 and 2022 approximately 380 homes were delivered.

Moreover, the development of tertiary-office projects (96,000 m2 under development and 22,500 m2 in the pipeline; for more details about the projects see the business description section) will represent an important additional growth lever (although not before 2025e, so their sales have not been included in our financial projections).

## The property management business (highly recurrent) provides high visibility both in terms of revenue and margins (revenue: + 6.7% CAGR 21-24e)

ISUR has a portfolio of high quality assets (occupancy of 88% and a large part of the vacant space in the process of being reformed) with 130,000 m2 of offices (71%), hotels (21%) and commercial premises (8%) with a presence in Andalusia (80%) and Madrid (20%). A particularity that enables the company to weather the current situation with a unique visibility compared to a property company with a 100% development business.

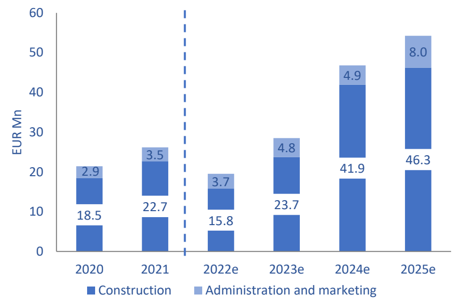
In fact, the scenario we envisage for ISUR's property management business includes the continuation of mid-single-digit non-organic growth up to rental revenue of EUR 18.6Mn in 2024e (Table 2; +6.7% CAGR 2021-2024e; in line with growth in 2018-2021) as a result of: i) the updating of rents in line with inflation (mainly in 2022e, already visible in 9m22 results) and the renegotiation of leases and ii) a slight improvement in the occupancy of the asset portfolio to average levels of c. 90% (vs 87.7% in 2021).

***Table 2. Estimates for the property management business (2020-2025e)***

| EUR Mn | 2020 | 2021 | 2022e | 2023e | 2024e | 2025e |
|---|---|---|---|---|---|---|
| Gross Lettable Area (GLA m2) | 135,243 | 132,026 | 130,882 | 130,882 | 130,882 | 130,882 |
| M2 Marketed | 6,434 | 10,173 | 10,173 | 10,173 | 10,173 | 10,173 |
| Commercialisation s/GLA | *4,76%* | *7,71%* | *7,71%* | *7,71%* | *7,71%* | *7,71%* |
| Occupation rate | 89.4% | 87.7% | 88.4% | 89.1% | 89.8% | 90.5% |
| Rented area | 120,907 | 115,787 | 115,700 | 116,616 | 117,532 | 118,448 |
| *Change (%)* | *12.2%* | *-2.4%* | *-0.9%* | *0.0%* | *0.0%* | *0.0%* |
| EUR m2 | 9.2 | 11.1 | 12.4 | 12.9 | 13.3 | 13.5 |
| *EUR m2 change (%)* | *-14.5%* | *21.1%* | *12.0%* | *4.1%* | *2.5%* | *2.0%* |
| **Total sales** | **13.3** | **15.4** | **17.3** | **18.1** | **18.7** | **19.2** |
| *Total sales chg (%)* | -3.0% | 16.0% | *11.9%* | 4.9% | 3.3% | 2.8% |
| **EBITDA rental business** | **9.9** | **11.8** | **13.2** | **13.9** | **14.4** | **14.8** |
| *EBITDA Mg.* | 74.4% | 76.7% | *76.7%* | 76.8% | 76.8% | 76.9% |

Not forgetting the large contribution of the property management area to the generation of EBITDA and free cash flow, as we are talking about a business with an EBITDA margin of c. 77% (Table 2), with a very high capacity to convert EBITDA into cash. This factor sets ISUR apart from other property companies with businesses that depend 100% on development, as it allows the company to weather periods of uncertainty (such as the present one) with a greater degree of visibility (both in terms of revenue and margins) and even take advantage of the low part of the property-development cycle to buy land at more attractive prices.

*Chart 38. Revenue from construction and administration and marketing*



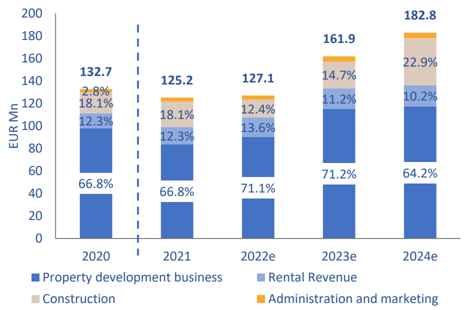

## Accessory services (construction; administration and marketing): growth in line with that of the development activity

The revenues generated by construction (12.5% of 2022e revenue) and administration and marketing (3% of 2022e revenue) correspond exclusively to the services provided by ISUR for developments carried out with third parties as joint ventures and so their capacity for growth depends on: i) the evolution of the company's development activity, ii) the mix of deliveries corresponding to joint ventures (with more revenue from these services the greater the level of activity carried out through joint ventures) and iii) the percentage stake that ISUR holds in each of the joint ventures (normally between 50% and 70%).

On the one hand, our estimates envisage the continuation of the fees generated by the provision of administration and marketing services for developments with third parties (c. 4.5% of development revenue) to levels of c. EUR 5Mn in 2024e (+12% CAGR 2021-2024e; fully in line with growth in the development activity).

And, on the other, we estimate the acceleration of revenue generated by the construction company to levels of c. EUR 40Mn from 2024e (vs EUR 23Mn in 2021), the result of: i) the start (in 4Q22) of the building of a larger volume of units (in 2025e >800 homes should be delivered vs 380 in 2021, that, mathematically, will imply a higher volume of construction revenues) and ii) the beginning of the building of tertiary development projects (that we estimate will provide revenue of c. EUR 15Mn/year in 2024e and 2025e, that explains the step-up in the business in 2024e; Chart 38).

*Chart 39. Revenue mix (2021-2024e)*




## At the consolidated level, revenue growth (+13.5% CAGR 21-24e) will translate to similar growth in EBITDA (+12% CAGR 21-24e) to c. EUR 30Mn in 2024e

With all this we expect ISUR to attain consolidated revenue of c. EUR 180Mn (Chart 39), with 65% coming from the development business, 24% from the construction of and provision of services to developments executed through joint ventures and the other 11% from the property management business. Revenue that in 2025e should approach EUR 250Mn, although evidently visibility is lower (Table 2).

Procurements correspond to the cost of sales of the development business, and as the vast majority of the developments to be delivered correspond to land already acquired, we expect the gross margin of the development business to return to levels of c. 24% from 2024e (gross margin of the development business c. 24%).

Operating costs are largely associated with the company's own construction activity that, together with the marketing and structural costs of each development, represent an average of 80% of the overheads of the business (Table 2). The other large component of costs is the operating and structural costs of the property management business (9% of operating costs) and structural costs at the corporate level (very stable over time: c. EUR 4.5Mn/year, 10% of operating costs).

The above translates to 2022e EBITDA of EUR 23Mn (in line with 2021) that should increase to c. EUR 30Mn in 2024e. The vertical integration of the business will allow an EBITDA margin of c. 18% to be maintained (despite the estimated smaller gross margin of the development business). Levels of EBITDA that should be achieved with little downside risk (given the large contribution of the property management business to EBITDA; c. 50%).

*Chart 40. EBITDA and consolidated EBITDA margin (2021-2024e)*

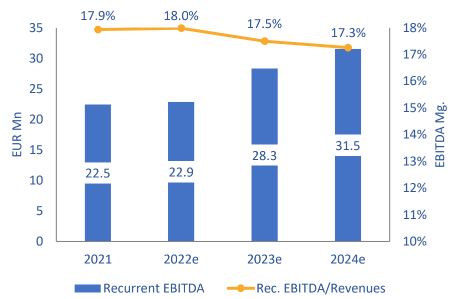
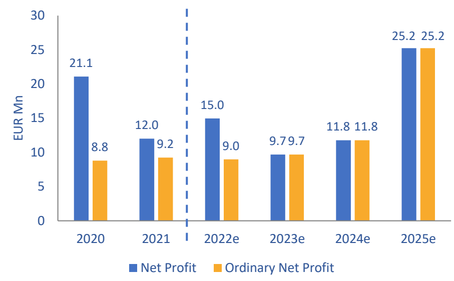



*Table 3. Summary of sales and EBITDA margin*

| EUR Mn | 2020 | 2021 | 2022e | 2023e | 2024e | 2025e |
|---|---|---|---|---|---|---|
| Property development business | 98.0 | 83.6 | 90.3 | 115.3 | 117.3 | 193.0 |
| Rental Revenue | 13.3 | 15.4 | 17.3 | 18.1 | 18.7 | 19.2 |
| Construction | 18.5 | 22.7 | 15.8 | 23.7 | 41.9 | 46.3 |
| Administration and marketing | 2.9 | 3.5 | 3.7 | 4.8 | 4.9 | 8.0 |
| **Total sales** | **132.7** | **125.2** | **127.1** | **161.9** | **182.8** | **266.5** |
| Cost of development sales | (73.2) | (63.8) | (70.4) | (89.9) | (89.1) | (145.7) |
| **Gross margin** | **59.6** | **61.3** | **56.6** | **72.0** | **93.7** | **120.8** |
| *% over total sales* | *44.9%* | *49.0%* | *44.6%* | *44.5%* | *51.2%* | *45.3%* |
| Construction activity costs | (18.3) | (22.3) | (15.6) | (23.4) | (41.4) | (45.7) |
| Marketing and delivery costs | (5.6) | (5.4) | (5.8) | (7.4) | (7.5) | (12.4) |
| Operating expenses (assets) | (2.3) | (2.6) | (2.9) | (3.0) | (3.1) | (3.2) |
| Structural costs (property) | (1.1) | (1.0) | (1.1) | (1.2) | (1.2) | (1.3) |
| Structural costs (promotion) | (4.0) | (3.6) | (3.8) | (3.8) | (3.9) | (4.0) |
| Structural expenses (corporate) | (3.7) | (4.1) | (4.6) | (4.7) | (4.9) | (4.9) |
| **EBITDA** | **24.5** | **22.5** | **22.9** | **28.3** | **31.5** | **49.3** |
| *EBITDA margin (%)* | *18.5%* | *17.9%* | *18.0%* | *17.5%* | *17.3%* | *18.5%* |

*Chart 41. Net profit and Ordinary Net Profit*




## The increase in financial expenses will reduce the capacity to convert EBITDA in net profit, although this will remain close to 40%

Over 2018-2021, ISUR converted c. 40% of the Rec. EBITDA generated into Ordinary Net Profit (calculated as net profit not including income from the sale of property investments, extraordinary and other non-recurrent items). And in 2022e-2024e, the main items between EBITDA and ordinary NP are:

- **The increase in financial expenses.** Our estimates envisage an increase of 250 bp in the effective cost of debt to c. 4.5% in 2023e that, including the capitalisation of interest costs directly assignable to developments in progress (c. 30-40% of estimated total financial expenses in 2023e), would translate to an average cost of debt in 2023e of c. 3.5% (vs c. 2% in 2021). This, plus estimated growth in debt, will imply financial expenses of c. EUR 10.5Mn from 2023e (vs c. EUR 6Mn in 2022e and 2021).

- **Tax rate (25%).** We assume the tax rate seen in 2021 will continue in 2022e-2024e (25%).

In addition, in 2022e it is important to take into account the following (due to their impact on net profit):

- **Income from the sale of property investments.** Our 2022e estimates include income of EUR 1.3Mn from the sale of property investments (visible in 9m22 results). Our estimates do not envisage additional capital gains from asset rotations that could be an additional lever of value generation.

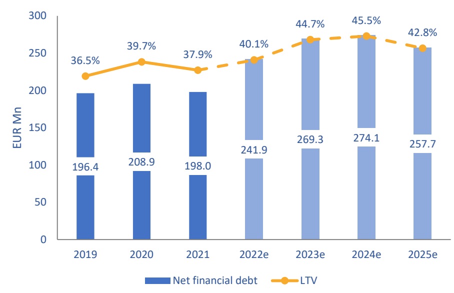
- **Result of the taking control of Desarrollos Metropolitanos del Sur (DMS).** We estimate an accounting impact of c. EUR 6.5Mn in 2022e for the recording at fair value of DMS after its acquisition in June 2022.

All the above leads us to estimate 2022e net profit of EUR 15Mn that, excluding income from the sale of property investments (EUR 1.3Mn) and the extraordinary amount arising from the consolidation of DMS (EUR 6.7Mn) translates to 2022e ordinary net profit of EUR 9Mn (c. 40% of Rec. EBITDA) that, despite the increase in financial expenses, should increase to levels of EUR 12Mn in 2024e (+8.4% CAGR 2021-2024e).

## ISUR will need heavy investment in working capital to be a big generator of cash from 2025e

The large growth in the number of deliveries expected for 2025e (c. 800 vs 380 in 2021 and 2022e) and the execution of tertiary development projects will imply an increase in working capital requirements in order to: 1) buy land (in 9m22 ISUR invested EUR 34.5Mn on purchasing plots of land) and 2) execute developments in progress. From 2025e, once deliveries of homes have accelerated, ISUR will begin to generate large amounts of cash (we estimate a Rec. FCF of c. EUR 20Mn in 2025e; Rec. FCF yield 2025e of c. 15%).

*Chart 42. Net debt and LTV (2020-2024e)*




## And despite the increase in net debt, gearing will remain reasonable (LTV < 45%)

The high level of investment estimated for coming years will increase net debt to c. EUR 275Mn in 2024e (+38% vs 2021; Chart 42). Despite this, gearing will remain at reasonable levels with an average LTV for the period of < 45%, with EBITDA always higher than 3x interest (despite the increase in financial expenses to c. EUR 10.5Mn from 2023e).

Our estimates envisage the continuation of a dividend policy similar to that seen in 2021, with a payout of 45%-50% of net profit that, on 2022e profits, will imply a dividend of EUR 5.5Mn (dividend yield 4%), gradually increasing to c. EUR 12Mn in 2025e (2025e yield c. 9%).

## A combination of businesses (development and property management) that allows ISUR to aspire to a significant increase in activity, limiting levels of risk

There is no doubt that in the last year the scenario for the residential segment has become more difficult. The worsening of the Spanish macro is a fact and downgrades to growth estimates plus the quick and decisive increase in interest rates could slow down housing demand in the short term.

Despite this, the snapshot of ISUR is that of a company that aspires to a significant increase in activity, with a development business that should reach levels of deliveries of over 450 homes in 2024e (and 800 in 2025e). This is a genuine change of scale bearing in mind that in 2021 some 380 homes were delivered. However, in our view, what is really interesting are the factors that make this growth credible and attainable with less exposure to the residential property cycle (compared to companies with a 100% development business). These factors are:

- **A land bank that provides significant visibility and makes the step-up in size of the development business credible.** The current land bank will allow for the construction of 4,000 homes (of which 1,700 are already being marketed; 47% sold). In other words, the homes to be delivered during the estimated period will, in the majority, be on land in the land bank.

- **Vertical integration (with a construction company at the service of the development business).** Unlike other developers, ISUR has a 100%-owned construction company (that only builds for ISUR and its developments via JVs), that should allow greater control of costs, quality and execution times (essential in the current context).

- **A property management business, with quality assets (with occupancy rates of c. 90%),** that provides a recurrent source of cash (with very high margins; >70% in EBITDA). This reduces the company's risk profile. In addition, the value of the property assets provides greater comfort from a financial point of view as, if needed, ISUR could sell assets.

All the above are factors unique to ISUR that allow the company to weather periods of uncertainty (such as the present one) with a greater degree of visibility (both in terms of revenue and margins) and even take advantage of the bottom of the property-development cycle to buy land at more attractive prices (that should improve the long-term return for shareholders vs traditional developers).

## Valuation inputs

### *Inputs for the DCF Valuation Approach*

| | 2022e | 2023e | 2024e | Terminal Value (1) | | |
|---|---|---|---|---|---|---|
| **Free Cash Flow "To the Firm"** | **(31.9)** | **(12.7)** | **7.8** | **n.a.** | | |
| | | | | | | |
| **Market Cap** | **136.3** | At the date of this report | | | | |
| **Net financial debt** | **258.7** | Debt net of Cash (9m Results 2022) | | | | |
| | | | | | Best Case | Worst Case |
| Cost of Debt | 4.5% | Net debt cost | | | 4.3% | 4.8% |
| Tax rate (T) | 20.0% | T (Normalised tax rate) | | | = | = |
| **Net debt cost** | **3.6%** | **Kd = Cost of Net Debt * (1-T)** | | | **3.4%** | **3.8%** |
| Risk free rate (rf) | 3.4% | Rf (10y Spanish bond yield) | | | = | = |
| Equity risk premium | 6.0% | R (own estimate) | | | 5.5% | 6.5% |
| Beta (B) | 1.1 | B (own estimate) | | | 1.0 | 1.2 |
| **Cost of Equity** | **10.0%** | **Ke = Rf + (R * B)** | | | **8.9%** | **11.2%** |
| Equity / (Equity + Net Debt) | 34.5% | E (Market Cap as equity value) | | | = | = |
| Net Debt / (Equity + Net Debt) | 65.5% | D | | | = | = |
| **WACC** | **5.8%** | **WACC = Kd * D + Ke * E** | | | **5.3%** | **6.3%** |
| **G "Fair"** | **2.0%** | | | | **2.0%** | **1.5%** |

(1) The terminal value calculated beyond the last FCF estimate does not reflect the company's growth potential (positive/negative) at the date of publication of this report.

### *Inputs for the Multiples Valuation Approach*

| Compañía | Ticker Factset | Mkt. Cap | PER 22e | BPA 22e-24e | EV/EBITDA 22e | EBITDA 22e-24e | EV/Vtas. 22e | Ingresos 22e-24e | EBITDA/Vtas. 22e | FCF Yield 22e | FCF 22e-24e |
|---|---|---|---|---|---|---|---|---|---|---|---|
| Metrovacesa | MVC-ES | 961.6 | 30.4 | -6.4% | 19.4 | 1.0% | 1.8 | 3.4% | 9.3% | 13.5% | 6.5% |
| Aedas Homes | AEDAS-ES | 616.9 | 5.7 | -5.7% | 6.3 | -3.2% | 1.1 | -1.0% | 17.8% | 11.9% | 3.2% |
| Neinor Homes | HOME-ES | 659.9 | 6.7 | -12.0% | 3.7 | -8.5% | 0.6 | -12.5% | 16.9% | 16.8% | -62.8% |
| **Inmobiliarias** | | | **14.3** | **-8.0%** | **9.8** | **-3.6%** | **1.2** | **-3.4%** | **14.7%** | **14.1%** | **-17.7%** |
| **ISUR** | **ISUR-ES** | **136.3** | **9.1** | **-11.4%** | **17.4** | **17.5%** | **3.1** | **19.9%** | **18.0%** | **n.a.** | **89.3%** |

### *Free Cash Flow sensitivity analysis (2023e)*

#### Rec. EBITDA and EV/EBITDA sensitivity to changes in EBITDA/Sales

| Scenario | EBITDA/Sales 23e | EBITDA 23e | EV/EBITDA 23e |
|---|---|---|---|
| **Max** | **19.3%** | **31.3** | **12.7x** |
| **Central** | **17.5%** | **28.3** | **14.0x** |
| **Min** | **15.7%** | **25.4** | **15.6x** |

## What can go wrong?

We consider risks to be those that could have a significant negative impact on our projections, mainly those for operating profit and free cash flow:

- **Slowdown in demand for housing.** Buying land and building houses is the industrial (easy?) part of the development business. The difficulty and risk lie in the marketing of the completed developments (as seen in the 2008 property crisis). The current interest rate context (with Euribor at its highest since 2008) significantly increases the cost of mortgage financing. This could result in a slowdown in demand for housing that would inevitably impact ISUR's development business (c. 64% of 2023e revenue), delaying estimated deliveries of developments (and also implying greater consumption of cash and lower margins and ROCEs).

  Specifically, a 10% reduction in the estimated number of deliveries in 2023e would cause a reduction of c. 8% in consolidated revenue and of c. 10% in terms of EBITDA.

- **The current macro situation and its impact on the property management business (offices): both regarding the ability to raise rents...** The current scenario (rocketing inflation, rising interest rates, a credit squeeze, less liquidity…) is fully impacting growth, and its effect is already being reflected in downgrades to GDP and job creation estimates (that according to the latest consensus data will be zero in 2023e). This could result in a slower than expected increase in rents on rental assets (especially in the office segment, where the company has most of its rental assets).

  A 10% contraction in rents in 2023e (vs estimated growth of 5%) would result in a 7% decline in 2023e EBITDA.

- **… and occupancy levels:** ISUR has continuously increased its occupancy rate from 70% in 2016 to 88.5% in 9m22. Our estimates envisage further improvement in occupancy levels with an annual increase of 0.5p.p. (similar to that seen in 2022) to 90% in 2024e.

  A reduction in the current high rate of occupancy to 80% in 2023e would negatively impact the company's results (-5% EBITDA vs our central scenario).

- **Increase in construction costs and impact on the margins of the development business.** Although ISUR has a vertically integrated property business (with a 100%-owned construction company, not common in the sector), continuous increases in the cost of both land purchases and building materials could have a negative impact on our estimates for margins and EBITDA generation. This was clear from ISUR's 9m22 results (the gross margin of the development business fell to 22% vs 25% previously).

  Although our estimates do not envisage an improvement of margins in 2023e (we estimate a similar gross margin to that seen in 9m22), an additional 1.5p.p contraction to 20.5% would result in a decrease in 2023e EBITDA of 6.5%.

- **Level of debt and the evolution of interest rates.** At September 2022, ISUR had net debt of EUR 259Mn (LTV 43%), with c. 60% of the maturities from 2026, with an interest rate mainly indexed to the one-year Euribor rate (80% of the total).

  Our estimates envisage an increase of 250 bp in the effective cost of debt to c. 4.5% in 2023e that, including the capitalisation of interest costs directly assignable to developments in progress (c. 30-40% of estimated total financial expenses in 2023e), would decrease to an average cost of c. 3.5% (vs c. 2% in 2021). An additional 100 bp increase in interest rates would imply a c. 15% increase in estimated net financial expenses for 2023e.

- **Rebound in discount rates and the impact on asset values.** The rebound in the yield on the 10-yr Spanish bond (now c. 3.4% vs 0.5% at the beginning of the year) makes property less attractive as an investment asset.

Under equal conditions, an increase in the yields demanded of the office segment (3.75% for premium assets in the Madrid CBD vs c. 6% at 2012 highs) and of the residential segment (now close to 3.6% vs c. 5% in 2014) would inevitably reduce asset values that are currently close to highs. Logically, any change in asset values would impact on the business itself (sale prices, margins, gearing levels…) and on its capacity for cash flow generation.

# A large Board comprised mainly of proprietary directors (64% of capital)

From a governance point of view, ISUR can be seen as a family company with a large board (comprised of 15 members; relatively stable in the last 10 years) that directly and indirectly represents 64% of the shareholder structure. There are no purely executive directors (without significant shareholdings). We highlight:

- **A board controlled by core shareholders...** With 11 of the 15 members being proprietary directors accounting for c. 64% of capital, logical given the family origins of the company. Specifically, the members of the board directly control 23% of the capital, while other shareholders linked to this (in general relatives) control a further 41%. However, of the 11 proprietary board members, 6 represent shareholdings of between 3% and 9% (with no family ties among them).

  With a significant shareholding in the hands of the Pumar family (one of the company's founding families; shareholding of c. 30%) and a presence both on the Board of Directors (with 6 of the 15 seats on the board) and the management team, holding, among others, the positions of Chair of the Board and Managing Director.

- **... with significant experience in the property sector (a crucial factor in the current context).** Most of the board have significant experience in the property sector. To put it in context, 8 of its 15 members (Table 1) were appointed to the board over 10 years ago and so had to navigate the bottom of the cycle in 2008-2013.

  In addition, the management team have also been with the company a long time (9 of its 12 members joined the group over 15 years ago). Given the current context of the property cycle, we think the sector experience of both the board of directors and the management team could reduce the risks inherent to the cycle itself.

- **Few independent board members.** Independent directors account for 20% of the total (vs a recommendation of 33.3% in the CNMV's Code of Good Governance for companies with low capitalisation). This makes it difficult for its committees to maintain their independence (although both the Audit Committee and the Appointments and Remuneration Committee have a majority of independent board members).

***Table 4. Composition of the Board of Directors***

| Member of the Board | Date of first appointment | Status of Board Member | % Capital |
|---|---|---|---|
| Ricardo Pumar López | 12/2/2005 | Executive | 0.9% |
| Esteban Jiménez Planas | 1/28/2005 | Proprietary | 5.1% |
| Andrés Claudio Fernández Romero | 6/19/2004 | Proprietary | 0.3% |
| Fernando Pumar López | 4/9/2021 | Proprietary | 3.0% |
| Antonio Román Lozano | 3/31/2022 | Proprietary | 5.0% |
| Jose Manuel Pumar López | 6/26/2010 | Proprietary | 0.6% |
| Ignacio Ybarra Osborne | 1/25/2002 | Proprietary | 0.0% |
| Augusto Sequeiros Pumar | 3/27/2002 | Proprietary | 0.6% |
| Salvador Granell Balén | 6/26/2010 | Proprietary | 0.7% |
| Candelas Arranz Pumar | 4/5/2019 | Proprietary | 1.1% |
| Luis Alarcón de Francisco | 3/31/2022 | Proprietary | 5.1% |
| Alberto Hoyos-Limón Pumar | 12/30/2021 | Proprietary | 0.0% |
| Jorge Segura Rodríguez | 11/15/2012 | Independent | 0.1% |
| Jose Luis Galán González | 6/7/2014 | Independent | 0.0% |
| Brita Hektoen Wergeland | 4/28/2018 | Independent | 0.0% |
| | | **Total** | **22.6%** |

Esteban Jimenez Planas is a board member in representation of Menezpla, S.L.
Ignacio Ybarra is a board member in representation of Increcisa, S.L.

***Table 5. Key corporate governance indicators***

| KPI | 2019 | 2020 | 2021 |
|---|---|---|---|
| % of independent directors | 20.0% | 20.0% | 20.0% |
| % of proprietary directors | 80.0% | 80.0% | 80.0% |
| % of executive directors | 6.7% | 6.7% | 6.7% |
| % of women on the board of directors | 13.3% | 13.3% | 13.3% |
| % Remuneration of the board/personnel costs (1) | 8.7% | 8.6% | 10.8% |

Note 1: The remuneration of the Executive Chair in 2021 included the delivery of shares corresponding to the variable remuneration scheme for 2016-2020. This explains the one-off increase in the percentage remuneration of the board in 2021.

- **Board remuneration has remained stable in the last 3 years.** In 2019 and 2020 the remuneration of the Board remained relatively stable (c. 9% of personnel expenses).

  In 2021 the remuneration of the Board increased to EUR 990k (+28% vs 2020; 10.8% of personnel expenses) as a result of the delivery of shares corresponding to the variable remuneration of the Chair of the Board for 2016-2020.

  In the policy for the remuneration of board members for 2022/2024, a new long-term system of variable remuneration has been approved for the Chair and 12 directors (maximum annual cost of 400,000 euros). This remuneration is linked to permanence in the company and compliance with the objectives included in the 2021/2025 Strategic Plan.

- **Without an explicit diversity policy for appointing board members.** Although there is no explicit diversity policy for appointing board members, board regulations stipulate that the board must ensure the procedures for selecting board members favour professional, knowledge and gender diversity (avoiding, in all cases, any type of bias hindering the selection of board members).

  The percentage of women board members has been stable in the last 3 years (13.3% of the total), as has the percentage of women in the workforce at c. 32% (33.2%, 2019; 31.6%, 2020; 32.1%, 2021).

- **Without a sustainability and environment committee.** Oversight of compliance with policies and regulations in respect of environmental matters is the responsibility of the Appointments and Remuneration committee and the Audit committee (CSR committee).

- **Contribution to society:** In 2021 ISUR set aside 130,000 euros (+14.5% vs 2020; 0.6% of EBITDA) for cooperation with non-profit entities working to help people with disability and the vulnerable.

- **Stable shareholder remuneration (payout c. 45-50%), including share buyback.** Apart from 2012, ISUR has paid a dividend each year for the last 30 years. The current dividend policy is to pay out between 45% and 50% of consolidated profit after tax. In 2021 ISUR paid out a total dividend of 0.30 euros per share (EUR 5.6Mn; payout c. 45%, dividend yield of 4%).

  In addition, ISUR has approved a share buyback programme for a maximum amount of EUR 5Mn to satisfy the variable remuneration of the management team and as a complement to shareholder remuneration. The maximum number of shares to be acquired is 375,000 (2% of the share capital), c. 25% of which will be allocated to the variable remuneration plan and the rest to reducing capital via the redemption of treasury stock to complement shareholder remuneration.

# Appendix 1. Financial Projections (proportional consolidation)

| Balance Sheet (EUR Mn) | 2017 | 2018 | 2019 | 2020 | 2021 | 2022e | 2023e | 2024e |
|---|---|---|---|---|---|---|---|---|
| Intangible assets | | - | - | - | - | - | - | - |
| Fixed assets | | 139.1 | 146.7 | 216.0 | 216.9 | 244.9 | 243.3 | 242.0 |
| Other Non Current Assets | | - | - | - | - | - | - | - |
| Financial Investments | | 2.1 | 1.8 | 1.2 | 0.5 | 0.5 | 0.5 | 0.5 |
| Goodwill & Other Intangilbles | | - | - | - | - | - | - | - |
| Current assets | | 226.4 | 263.5 | 196.9 | 185.2 | 211.0 | 253.3 | 273.0 |
| **Total assets** | | **367.7** | **412.1** | **414.1** | **402.6** | **456.4** | **497.1** | **515.5** |
| Equity | | 103.8 | 107.2 | 122.3 | 131.5 | 140.9 | 143.8 | 151.1 |
| Minority Interests | | - | - | 3.2 | 3.2 | 3.2 | 3.2 | 3.2 |
| Provisions & Other L/T Liabilities | | - | - | - | - | - | - | - |
| Other Non Current Liabilities | | - | - | - | - | - | - | - |
| Net financial debt | | 184.8 | 196.4 | 208.9 | 198.0 | 241.9 | 269.3 | 274.1 |
| Current Liabilities | | 79.0 | 108.4 | 79.7 | 69.9 | 70.5 | 80.9 | 87.1 |
| **Equity & Total Liabilities** | | **367.7** | **412.1** | **414.1** | **402.6** | **456.4** | **497.1** | **515.5** |

| | | | | | | | | | CAGR | |
|---|---|---|---|---|---|---|---|---|---|---|
| **P&L (EUR Mn)** | **2017** | **2018** | **2019** | **2020** | **2021** | **2022e** | **2023e** | **2024e** | **18-21** | **21-24e** |
| **Total Revenues** | | **113.9** | **122.8** | **132.7** | **125.2** | **127.1** | **161.9** | **182.8** | ***3.2%*** | ***13.5%*** |
| *Total Revenues growth* | | *n.a.* | *7.8%* | *8.1%* | *-5.7%* | *1.5%* | *27.4%* | *12.9%* | | |
| COGS | | (51.5) | (47.2) | (73.2) | (63.8) | (70.4) | (89.9) | (89.1) | | |
| **Gross Margin** | | **62.4** | **75.6** | **59.6** | **61.3** | **56.6** | **72.0** | **93.7** | ***-0.6%*** | ***15.1%*** |
| *Gross Margin/Revenues* | | *54.8%* | *61.6%* | *44.9%* | *49.0%* | *44.6%* | *44.5%* | *51.2%* | | |
| Personnel Expenses | | (9.0) | (9.7) | (9.0) | (9.1) | (10.3) | (10.6) | (10.7) | | |
| Other Operating Expenses | | (36.0) | (43.5) | (26.0) | (29.8) | (23.5) | (33.1) | (51.4) | | |
| **Recurrent EBITDA** | | **17.4** | **22.4** | **24.5** | **22.5** | **22.9** | **28.3** | **31.5** | ***8.8%*** | ***12.0%*** |
| *Recurrent EBITDA growth* | | *n.a.* | *28.6%* | *9.5%* | *-8.5%* | *1.8%* | *24.0%* | *11.3%* | | |
| *Rec. EBITDA/Revenues* | | *15.3%* | *18.2%* | *18.5%* | *17.9%* | *18.0%* | *17.5%* | *17.3%* | | |
| Restructuring Expense & Other non-rec. | | - | - | (5.1) | - | - | - | - | | |
| **EBITDA** | | **17.4** | **22.4** | **19.4** | **22.5** | **22.9** | **28.3** | **31.5** | ***8.8%*** | ***12.0%*** |
| Depreciation & Provisions | | (3.6) | (2.5) | (6.3) | (4.3) | (4.6) | (4.9) | (4.9) | | |
| Capitalized Expense | | - | - | - | - | - | - | - | | |
| Income from the sale of property investments | | 6.1 | 4.1 | 0.3 | 3.8 | 1.3 | - | - | | |
| **EBIT** | | **19.9** | **24.0** | **13.3** | **21.9** | **19.5** | **23.4** | **26.7** | ***3.3%*** | ***6.8%*** |
| *EBIT growth* | | *n.a.* | *20.6%* | *-44.4%* | *64.2%* | *-10.9%* | *20.1%* | *13.8%* | | |
| *EBIT/Revenues* | | *17.5%* | *19.5%* | *10.1%* | *17.5%* | *15.4%* | *14.5%* | *14.6%* | | |
| Impact of Goodwill & Others | | - | - | - | - | - | - | - | | |
| Net Financial Result | | (6.6) | (6.6) | (5.9) | (5.6) | (6.3) | (10.5) | (11.0) | | |
| Income by the Equity Method | | - | - | - | - | - | - | - | | |
| **Ordinary Profit** | | **13.3** | **17.4** | **7.4** | **16.4** | **13.3** | **12.9** | **15.7** | ***7.2%*** | ***-1.4%*** |
| *Ordinary Profit Growth* | | *n.a.* | *31.1%* | *-57.2%* | *120.1%* | *-19.0%* | *-2.5%* | *21.3%* | | |
| Extraordinary Results | | - | (4.4) | 21.9 | - | 6.7 | - | - | | |
| **Profit Before Tax** | | **13.3** | **13.0** | **29.4** | **16.4** | **20.0** | **12.9** | **15.7** | ***7.2%*** | ***-1.4%*** |
| Tax Expense | | (3.2) | (4.1) | (8.3) | (4.3) | (5.0) | (3.2) | (3.9) | | |
| *Effective Tax Rate* | | *24.1%* | *31.9%* | *28.2%* | *26.0%* | *25.0%* | *25.0%* | *25.0%* | | |
| Minority Interests | | - | - | (0.0) | (0.1) | - | - | - | | |
| Discontinued Activities | | - | - | - | - | - | - | - | | |
| **Net Profit** | | **10.1** | **8.8** | **21.1** | **12.0** | **15.0** | **9.7** | **11.8** | ***6.1%*** | ***-0.7%*** |
| *Net Profit growth* | | *n.a.* | *-12.2%* | *138.4%* | *-43.0%* | *24.6%* | *-35.2%* | *21.3%* | | |
| **Ordinary Net Profit** | | **5.5** | **9.3** | **8.8** | **9.2** | **9.0** | **9.7** | **11.8** | ***19.1%*** | ***8.4%*** |
| *Ordinary Net Profit growth* | | *n.a.* | *69.9%* | *-5.3%* | *5.0%* | *-2.9%* | *8.1%* | *21.3%* | | |

| | | | | | | | | | CAGR | |
|---|---|---|---|---|---|---|---|---|---|---|
| **Cash Flow (EUR Mn)** | **2017** | **2018** | **2019** | **2020** | **2021** | **2022e** | **2023e** | **2024e** | **18-21** | **21-24e** |
| **Recurrent EBITDA** | | | | | | **22.9** | **28.3** | **31.5** | ***8.8%*** | ***12.0%*** |
| Rentals (IFRS 16 impact) | | | | | | - | - | - | | |
| Working Capital Increase | | | | | | (25.2) | (31.9) | (13.4) | | |
| **Recurrent Operating Cash Flow** | | | | | | **-2.4** | **-3.6** | **18.1** | ***29.8%*** | ***-9.4%*** |
| CAPEX | | | | | | (2.5) | (3.2) | (3.7) | | |
| Net Financial Result affecting the Cash Flow | | | | | | (6.3) | (10.5) | (11.0) | | |
| Tax Expense | | | | | | (5.0) | (3.2) | (3.9) | | |
| **Recurrent Free Cash Flow** | | | | | | **(16.2)** | **(20.6)** | **(0.4)** | ***27.5%*** | ***-26.9%*** |
| Restructuring Expense & Other non-rec. | | | | | | - | - | - | | |
| - Acquisitions / + Divestures of assets | | | | | | (22.1) | - | - | | |
| Extraordinary Inc./Exp. Affecting Cash Flow | | | | | | - | - | - | | |
| **Free Cash Flow** | | | | | | **(38.3)** | **(20.6)** | **(0.4)** | ***28.3%*** | ***-26.6%*** |
| Capital Increase | | | | | | - | - | - | | |
| Dividends | | | | | | (5.6) | (6.8) | (4.4) | | |
| **Net Debt Variation** | | | | | | **43.9** | **27.4** | **4.9** | | |

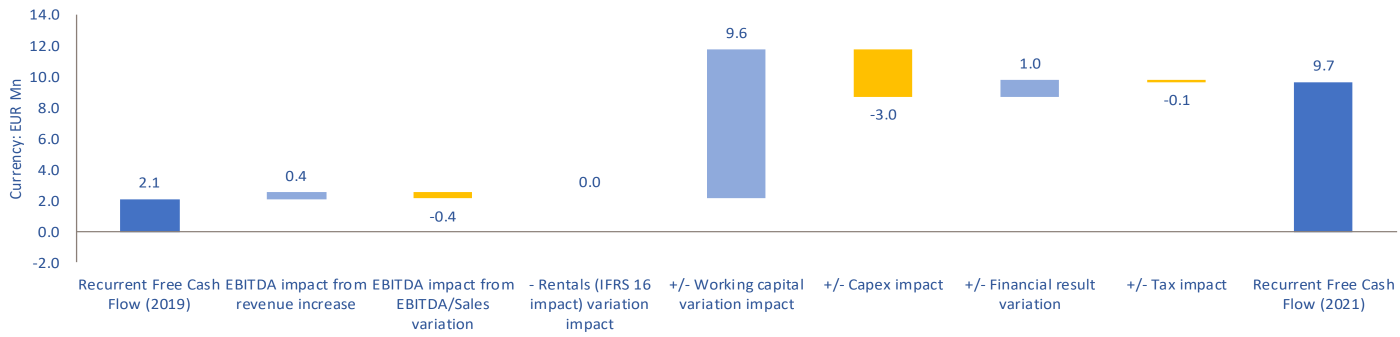
# Appendix 2. Free Cash Flow (proportional consolidation)

| A) Cash Flow Analysis (EUR Mn) | 2018 | 2019 | 2020 | 2021 | 2022e | 2023e | 2024e | CAGR 19-21 | CAGR 21-24e |
|---|---|---|---|---|---|---|---|---|---|
| **Recurrent EBITDA** | | **22.4** | **24.5** | **22.5** | **22.9** | **28.3** | **31.5** | *0.1%* | *12.0%* |
| *Recurrent EBITDA growth* | | *28.6%* | *9.5%* | *-8.5%* | *1.8%* | *24.0%* | *11.3%* | | |
| *Rec. EBITDA/Revenues* | | *18.2%* | *18.5%* | *17.9%* | *18.0%* | *17.5%* | *17.3%* | | |
| - Rentals (IFRS 16 impact) | | - | - | - | - | - | - | | |
| +/- Working Capital increase | | (7.7) | 37.9 | 1.9 | (25.2) | (31.9) | (13.4) | | |
| **= Recurrent Operating Cash Flow** | | **14.7** | **62.4** | **24.4** | **(2.4)** | **(3.6)** | **18.1** | *28.6%* | *-9.4%* |
| *Rec. Operating Cash Flow growth* | | *111.3%* | *324.1%* | *-61.0%* | *-109.8%* | *-50.8%* | *605.9%* | | |
| *Rec. Operating Cash Flow / Sales* | | *12.0%* | *47.0%* | *19.5%* | *n.a.* | *n.a.* | *9.9%* | | |
| - CAPEX | | (1.9) | (5.9) | (4.9) | (2.5) | (3.2) | (3.7) | | |
| - Net Financial Result affecting Cash Flow | | (6.6) | (5.9) | (5.6) | (6.3) | (10.5) | (11.0) | | |
| - Taxes | | (4.1) | (8.3) | (4.3) | (5.0) | (3.2) | (3.9) | | |
| **= Recurrent Free Cash Flow** | | **2.1** | **42.3** | **9.7** | **(16.2)** | **(20.6)** | **(0.4)** | *n.a.* | *-26.9%* |
| *Rec. Free Cash Flow growth* | | *101.6%* | *n.a.* | *-77.1%* | *-267.2%* | *-27.2%* | *97.9%* | | |
| *Rec. Free Cash Flow / Revenues* | | *1.7%* | *31.9%* | *7.7%* | *n.a.* | *n.a.* | *n.a.* | | |
| - Restructuring expenses & others | | - | - | - | - | - | - | | |
| - Acquisitions / + Divestments | | (3.9) | (51.9) | 4.0 | (22.1) | - | - | | |
| +/- Extraordinary Inc./Exp. affecting Cash Flow | | (5.2) | 2.6 | 0.6 | - | - | - | | |
| **= Free Cash Flow** | | **(7.0)** | **(7.0)** | **14.3** | **(38.3)** | **(20.6)** | **(0.4)** | *n.a.* | *-26.6%* |
| *Free Cash Flow growth* | | *94.6%* | *0.2%* | *303.3%* | *-367.8%* | *46.3%* | *97.9%* | | |
| | | | | | | | | | |
| *Recurrent Free Cash Flow - Yield (s/Mkt Cap)* | | *1.6%* | *31.0%* | *7.1%* | *n.a.* | *n.a.* | *n.a.* | | |
| *Free Cash Flow Yield (s/Mkt Cap)* | | *n.a.* | *n.a.* | *10.5%* | *n.a.* | *n.a.* | *n.a.* | | |

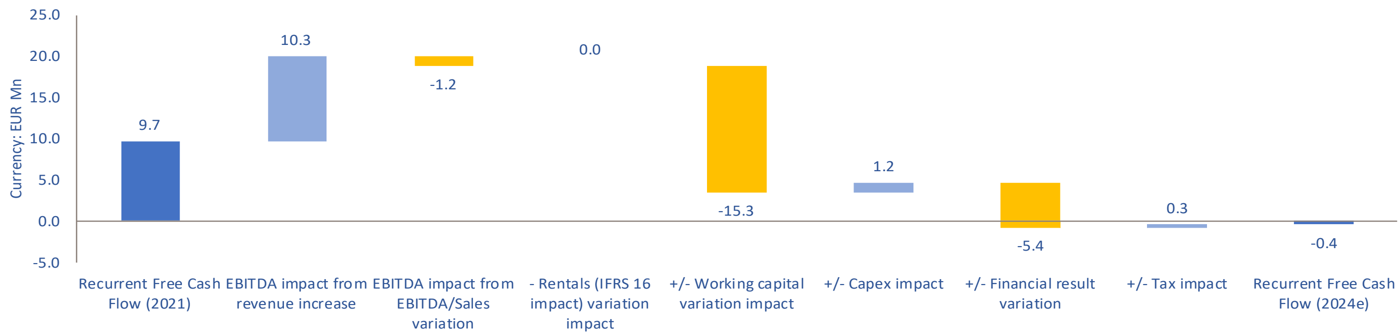
| B) Analytical Review of Annual Recurrent Free Cash Flow Performance (Eur Mn) | 2018 | 2019 | 2020 | 2021 | 2022e | 2023e | 2024e |
|---|---|---|---|---|---|---|---|
| **Recurrent FCF(FY - 1)** | | | **2.1** | **42.3** | **9.7** | **(16.2)** | **(20.6)** |
| EBITDA impact from revenue increase | | | 1.8 | (1.4) | 0.3 | 6.3 | 3.7 |
| EBITDA impact from EBITDA/Sales variation | | | 0.3 | (0.7) | 0.1 | (0.8) | (0.4) |
| **= Recurrent EBITDA variation** | | | **2.1** | **(2.1)** | **0.4** | **5.5** | **3.2** |
| - Rentals (IFRS 16 impact) variation impact | | | - | - | - | - | - |
| +/- Working capital variation impact | | | 45.6 | (36.0) | (27.1) | (6.7) | 18.5 |
| **= Recurrent Operating Cash Flow variation** | | | **47.7** | **(38.1)** | **(26.7)** | **(1.2)** | **21.7** |
| +/- CAPEX impact | | | (4.1) | 1.1 | 2.3 | (0.7) | (0.4) |
| +/- Financial result variation | | | 0.7 | 0.4 | (0.7) | (4.2) | (0.5) |
| +/- Tax impact | | | (4.1) | 4.0 | (0.7) | 1.8 | (0.7) |
| **= Recurrent Free Cash Flow variation** | | | **40.2** | **(32.6)** | **(25.8)** | **(4.4)** | **20.1** |
| | | | | | | | |
| **Recurrent Free Cash Flow** | | | **42.3** | **9.7** | **(16.2)** | **(20.6)** | **(0.4)** |

| C) "FCF to the Firm" (pre debt service) (EUR Mn) | 2018 | 2019 | 2020 | 2021 | 2022e | 2023e | 2024e | CAGR 19-21 | CAGR 21-24e |
|---|---|---|---|---|---|---|---|---|---|
| **EBIT** | | **24.0** | **13.3** | **21.9** | **19.5** | **23.4** | **26.7** | *-4.4%* | *6.8%* |
| ** Theoretical Tax rate* | | *30.0%* | *28.2%* | *26.0%* | *25.0%* | *25.0%* | *25.0%* | | |
| = Taxes (pre- Net Financial Result) | | (7.2) | (3.8) | (5.7) | (4.9) | (5.9) | (6.7) | | |
| | | | | | | | | | |
| **Recurrent EBITDA** | | **22.4** | **24.5** | **22.5** | **22.9** | **28.3** | **31.5** | *0.1%* | *12.0%* |
| - Rentals (IFRS 16 impact) | | - | - | - | - | - | - | | |
| +/- Working Capital increase | | (7.7) | 37.9 | 1.9 | (25.2) | (31.9) | (13.4) | | |
| **= Recurrent Operating Cash Flow** | | **14.7** | **62.4** | **24.4** | **(2.4)** | **(3.6)** | **18.1** | *28.6%* | *-9.4%* |
| - CAPEX | | (1.9) | (5.9) | (4.9) | (2.5) | (3.2) | (3.7) | | |
| - Taxes (pre- Financial Result) | | (7.2) | (3.8) | (5.7) | (4.9) | (5.9) | (6.7) | | |
| **= Recurrent Free Cash Flow (To the Firm)** | | **5.7** | **52.7** | **13.8** | **(9.8)** | **(12.7)** | **7.8** | *56.0%* | *-17.3%* |
| *Rec. Free Cash Flow (To the Firm) growth* | | *104.2%* | *830.7%* | *-73.9%* | *-171.1%* | *-29.4%* | *161.6%* | | |
| Rec. Free Cash Flow (To the Firm) / Revenues | | 4.6% | 39.7% | 11.0% | n.a. | n.a. | 4.3% | | |
| - Acquisitions / + Divestments | | (3.9) | (51.9) | 4.0 | (22.1) | - | - | | |
| +/- Extraordinary Inc./Exp. affecting Cash Flow | | (5.2) | 2.6 | 0.6 | - | - | - | | |
| **= Free Cash Flow "To the Firm"** | | **(3.5)** | **3.4** | **18.4** | **(31.9)** | **(12.7)** | **7.8** | *n.a.* | *-24.9%* |
| *Free Cash Flow (To the Firm) growth* | | *97.4%* | *196.7%* | *441.6%* | *-273.4%* | *60.2%* | *161.6%* | | |
| | | | | | | | | | |
| *Rec. Free Cash Flow To the Firm Yield (o/EV)* | | *1.4%* | *13.3%* | *3.5%* | *n.a.* | *n.a.* | *2.0%* | | |
| *Free Cash Flow "To the Firm" - Yield (o/EV)* | | *n.a.* | *0.9%* | *4.6%* | *n.a.* | *n.a.* | *2.0%* | | |

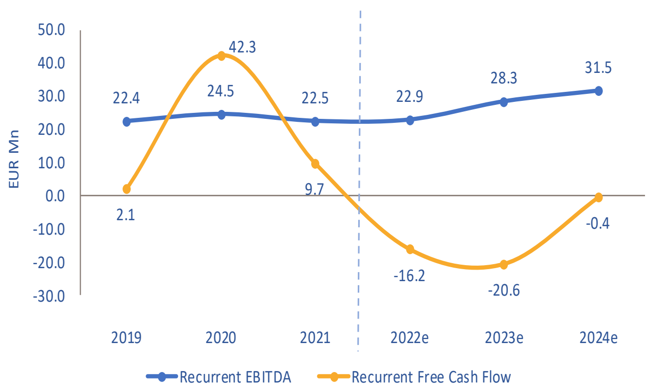
### Recurrent Free Cash Flow accumulated variation analysis (2017 - 2021)



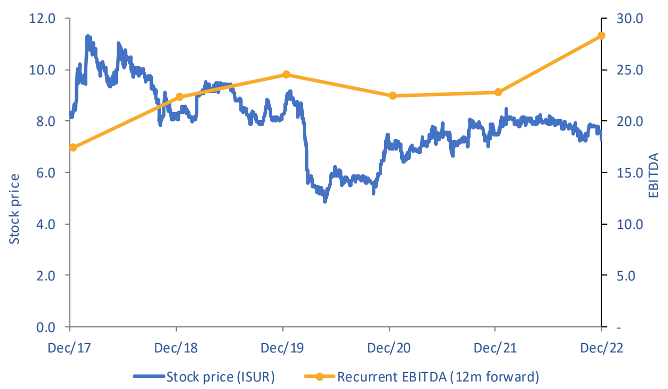

### Recurrent Free Cash Flow accumulated variation analysis (2021 - 2024e)




### Recurrent EBITDA vs Recurrent Free Cash Flow




### Stock performance vs EBITDA 12m forward




# Appendix 3. EV breakdown at the date of this report

| | EUR Mn | Source |
|---|---|---|
| Market Cap | 136.3 | |
| + Minority Interests | 3.1 | 9m Results 2022 |
| + Provisions & Other L/T Liabilities | - | 9m Results 2022 |
| + Net financial debt | 258.7 | 9m Results 2022 |
| - Financial Investments | 0.4 | 9m Results 2022 |
| +/- Others | | |
| **Enterprise Value (EV)** | **397.7** | |

# Appendix 4. Main peers 2022e

| | | Real estate | | | | |
|---|---|---|---|---|---|---|
| | EUR Mn | Metrovacesa | Aedas Homes | Neinor Homes | Average | ISUR |
| Market data | Ticker (Factset) | MVC-ES | AEDAS-ES | HOME-ES | | ISUR-ES |
| | Country | Spain | Spain | Spain | | Spain |
| | Market cap | 961.6 | 616.9 | 659.9 | | 136.3 |
| | Enterprise value (EV) | 1,024.1 | 1,015.9 | 521.4 | | 397.7 |
| Basic financial information | Total Revenues | 566.7 | 902.4 | 830.2 | | 127.1 |
| | Total Revenues growth | *10.9%* | *17.9%* | *-9.5%* | *6.4%* | *1.5%* |
| | 2y CAGR (2022e - 2024e) | *3.4%* | *-1.0%* | *-12.5%* | *-3.4%* | *19.9%* |
| | EBITDA | 52.8 | 160.2 | 140.6 | | 22.9 |
| | EBITDA growth | *92.7%* | *9.4%* | *7.0%* | *36.3%* | *1.8%* |
| | 2y CAGR (2022e - 2024e) | *1.0%* | *-3.2%* | *-8.5%* | *-3.6%* | *17.5%* |
| | EBITDA/Revenues | *9.3%* | *17.8%* | *16.9%* | *14.7%* | *18.0%* |
| | EBIT | 53.2 | 157.7 | 135.5 | | 19.5 |
| | EBIT growth | *62.6%* | *10.1%* | *7.1%* | *26.6%* | *-10.9%* |
| | 2y CAGR (2022e - 2024e) | *0.7%* | *-3.4%* | *-6.9%* | *-3.2%* | *16.9%* |
| | EBIT/Revenues | *9.4%* | *17.5%* | *16.3%* | *14.4%* | *15.4%* |
| | Net Profit | 29.7 | 103.8 | 96.7 | | 15.0 |
| | Net Profit growth | *61.1%* | *11.5%* | *-6.1%* | *22.2%* | *24.6%* |
| | 2y CAGR (2022e - 2024e) | *2.9%* | *0.3%* | *-10.8%* | *-2.6%* | *-11.4%* |
| | CAPEX/Sales % | *15.0%* | *0.4%* | *16.8%* | *10.7%* | *2.0%* |
| | Free Cash Flow | 129.7 | 73.4 | 110.7 | | (38.3) |
| | Net financial debt | 243.7 | 297.2 | 320.6 | | 241.9 |
| | ND/EBITDA (x) | 4.6 | 1.9 | 2.3 | 2.9 | 10.6 |
| | Pay-out | *616.0%* | *87.4%* | *57.4%* | *253.6%* | *45.5%* |
| Multiples and Ratios | P/E (x) | 30.4 | 5.7 | 6.7 | 14.3 | 9.1 |
| | P/BV (x) | 0.5 | 0.6 | 0.6 | 0.6 | 1.0 |
| | EV/Revenues (x) | 1.8 | 1.1 | 0.6 | 1.2 | 3.1 |
| | EV/EBITDA (x) | 19.4 | 6.3 | 3.7 | 9.8 | 17.4 |
| | EV/EBIT (x) | 19.2 | 6.4 | 3.8 | 9.8 | 20.4 |
| | ROE | *1.6* | *10.5* | *9.1* | *7.1* | *11.0* |
| | FCF Yield (%) | *13.5* | *11.9* | *16.8* | *14.1* | *n.a.* |
| | DPS | *1.21* | *2.01* | *0.72* | *1.31* | *0.36* |
| | Dvd Yield | *19.1%* | *15.2%* | *8.8%* | *14.4%* | *5.0%* |

Note 1: Financial data, multiples and ratios based on market consensus (Factset). In the case of the company analyzed, own estimates (Lighthouse).
Note 2: All ratios and multiples on EBITDA refer to total EBITDA (not to recurrent EBITDA).

LIGHTHOUSE

Calle Basílica, 17, 1ª Planta, Oficinas
28020 Madrid
T: +34 915 904 226
www.ieaf.es/lighthouse

Alfredo Echevarría Otegui
Head of research
alfredo.echevarria@lighthouse-ieaf.com

David López Sánchez
Equity research
david.lopez@lighthouse-ieaf.com

Luis Esteban Arribas
Equity research
luis.esteban@lighthouse-ieaf.com

Enrique Andrés Abad
Equity research
enrique.andres@lighthouse-ieaf.com

Jesús López Gómez
ESG Analyst & Data analytics
jesus.lopez@lighthouse-ieaf.com

*All Lighthouse research documents are available simultaneously on the Lighthouse website (www.ieaf.es/lighthouse) and via third-party aggregators such as Bloomberg, Factset, Capital IQ and Refinitiv.*

# IMPORTANT LEGAL INFORMATION REGARDING THIS REPORT

### LIGHTHOUSE

Lighthouse is a project of IEAF Servicios de Análisis S.L.U. Lighthouse is a research project funded by Bolsas y Mercados Españoles S.A. Lighthouse aims to improve the research coverage of the "orphan stocks" of the Spanish market: those which lack real and continuous research coverage. Lighthouse reports will not include valuation and target price. Lighthouse does not seek to provide investment advice to any natural or legal person. For this reason, Lighthouse will not provide a valuation, target price or investment recommendation for any of the securities analysed.

IEAF Servicios de Análisis S.L.U. is a Spanish company whose corporate purpose is:

1º) To provide information and financial analysis regarding securities issued by any class of legal person traded or not on official secondary markets, and especially (but not exclusively) those securities which are not the object of the recurrent provision of information and analysis by financial analysts who participate in the markets.

2º) To publicise and update the aforementioned financial reports and analysis, in addition to the monitoring and following of the securities on which the information and analysis is provided.

3º) To prepare studies and projects aimed at proposing and implementing measures to improve the information and financial analysis of securities traded on official secondary markets.

IEAF Servicios de Análisis S.L.U. is a company whose sole shareholder is the Instituto Español de Analistas Financieros, a professional, not for profit association.

### DISCLAIMER

The Instituto Español de Analistas Financieros hereby certifies that the analyst of IEAF Servicios de Análisis S.L.U. whose name figures as the author of this report, expresses views that reflect their personal and independent opinion of the company analysed without these implying, either directly or indirectly, a personalised recommendation of the company analysed for purposes of providing investment advice. This report is based on the preparation of detailed financial projections from information available to the public and following traditional fundamental research methodology (i.e. it is not a technical or quantitative analysis report). For the analysis methodology used in the preparation of this report, please contact the analyst directly; contact details are included on the front page of this report.

The report includes basic information regarding the main parameters to be used by an investor when making their own valuation (whether by discounted cash flows or multiples). These parameters are the personal opinion or estimate of the analyst. The person receiving this report should use their own judgement when using these parameters and should consider them as another element in their decision-making process in respect of investment. These parameters do not represent a personalised investment recommendation.

### Rules governing confidentiality and conflicts of interest

None of the following rules governing confidentiality and conflicts of interest (12) is applicable to this report:

1. This report is non-independent research as it has been commissioned by the company analysed (issuer).

2. In the last 12 months, the Instituto Español de Analistas Financieros or its subsidiary, IEAF Servicios de Análisis S.L.U., has had Investment Banking mandates or has managed or co-managed a public offering of the securities of the issuer, or has received compensation from said issuer for Investment Banking services, that exclude brokerage services for prepaid fees.

3. In the next 6 months, the Instituto Español de Analistas Financieros or its subsidiary, IEAF Servicios de Análisis S.L.U., expects to receive or intends to obtain compensation for Investment Banking services provided to this company that exclude brokerage services for prepaid fees.

4. The Investment Analyst or a member of the Research Department or a member of their household has a long position in the shares or derivatives of the corresponding issuer.

5. The Investment Analyst or a member of the Research Department or a member of their household has a short position in the shares or derivatives of the corresponding issuer.

6. At the date of publication, the Instituto Español de Analistas Financieros or its subsidiary, IEAF Servicios de Análisis S.L.U. held a long position of over 0.5% of the issuer's capital.

7. At the date of publication, the Instituto Español de Analistas Financieros or its subsidiary, IEAF Servicios de Análisis S.L.U. held a short position of over 0.5% of the issuer's capital.

8. At the end of the month immediately prior to the publication of this report, or of the previous month if the report is published in the ten days following the end of the month, the company analysed (the issuer) or any of its subsidiaries held 5% or more of any class of equity security of the Instituto Español de Analistas Financieros or its subsidiary, IEAF Servicios de Análisis S.L.U.

9. A senior director or officer of the Instituto Español de Analistas Financieros or its subsidiary, IEAF Servicios de Análisis S.L.U., or a member of their department is a director, officer, advisor or member of the Board of Directors of the issuer and/or one of its subsidiaries.

10. The Instituto Español de Analistas Financieros or its subsidiary, IEAF Servicios de Análisis S.L.U., acts as broker for the Issuer for the corresponding prepaid fees.

11. The contents of this report related to the financial analysis, financial projections, valuation, investment summary and opinion of the analyst have been reviewed by the issuer prior to its publication.

12. The issuer has made changes to the contents of this report prior to its distribution.

The Investment Analysts who have prepared this Investment Analysis are employees of IEAF Servicios de Análisis S.L.U. These analysts have received (or will receive) compensation according to the general earnings of IEAF Servicios de Análisis S.L.U. To obtain a copy of the Code of Conduct of IEAF Servicios de Análisis S.L.U. (in respect of the Management of Conflicts of Interest in the research department), please use the e-mail address secretaria@ieaf.es or consult the contents of this Code at www.ieaf.es.

IEAF Servicios de Análisis S.L.U. is compensated by Bolsas y Mercados Españoles, S.A. for the preparation of this report. This report should be considered as just another element in the taking of investment decisions.

### A report issued by IEAF servicios de análisis S.L.U.

 This document has been prepared and distributed, according to the provisions of the MiFID II by IEAF Servicios de Análisis S.L.U. Its corporate activity is regulated by the CNMV (the Spanish Securities Exchange Commission). The information and opinions expressed in this document do not represent nor are they intended to represent an offer or a solicitation to buy or sell the securities (in other words, the securities mentioned in this report and related warrants, options, rights or interests). The information and opinions contained in this document are based upon information available to the public and have been obtained from sources believed to be reliable by IEAF Servicios de Análisis S.L.U., but no guarantee is given regarding their accuracy or completeness. All comments and estimates reflect solely the opinion of IEAF Servicios de Análisis S.L.U. and do not offer any implicit or explicit guarantee. All the opinions expressed are subject to change without prior warning. This document does not take into account the specific investment objectives, financial position, risk profile or other specific aspects of the person who receives this document, and accordingly they should exercise their own judgement in this respect. Neither the Instituto Español de Analistas Financieros nor its subsidiary, IEAF Servicios de Análisis S.L.U., assumes any responsibility for direct or indirect losses arising from the use of the published research, except in the event of negligent conduct by IEAF Servicios de Análisis S.L.U. The information contained in this report is approved for distribution to professional clients, eligible counterparties and professional advisers, but not for distribution to private individuals or retail clients. Its reproduction, distribution or publication for any purpose without the written authorisation of IEAF Servicios de Análisis S.L.U. is prohibited. The Instituto Español de Analistas Financieros and/or its subsidiary IEAF

Servicios de Análisis S.L.U., their employees and directors, may hold a position (long or short) in an investment knowing that this issuer will be the object of analysis and that this analysis will be distributed to institutional investors. Any further information regarding the contents of this report will be provided upon request. IEAF Servicios de Análisis S.L.U. intends to publish (at least) one quarterly report or note updating the information on the company analysed.

**United States**. IEAF Servicios de Análisis S.L.U. is not registered in the United States and, consequently, is not subject to the regulations of that country governing the preparation of research and the independence of analysts. This report is distributed solely to major US institutional investors, in reliance on the exemption from registration provided by Rule 15a-6 of the US Securities Exchange Act of 1934, as amended (the "Exchange Act"), and interpretations of this made by the US Securities Exchange Commission.

**Major US Institutional Investors**. This report will be distributed to "major US institutional investors", as defined by Rule 15a-6 of the US Securities Exchange Commission and of the US Securities Exchange Act of 1934.

### Notes and Reports History

| Date of report | Recommendation | Price (EUR) | Target price (EUR) | Period of validity | Reason for report | Analyst |
|---|---|---|---|---|---|---|
| 22-Dec-2022 | n.a. | 7.30 | n.a. | n.a. | Initiation of Coverage | David López Sánchez |

European Commission
LIGHTHOUSE WINNER 2020 Special Mention
European Small & Mid-Cap Awards
FESE
EuropeanIssuers