Transcription
H1 2018 Earnings Call
August 31, 2018

Rene Hoffmann

Thank you Kai and welcome everybody to our H1 2018 earnings call. Your hosts today are CEO, Rolf Buch, and CFO, Helene von Roeder. They will lead through the results presentation first and then be happy to take your questions. I assume you have all had a chance to download the presentation, just to be sure; the H1 earnings presentation is available on our IR website in the section "Latest Publications". So without further delay, let us kick it off and I am handing over to Rolf Buch.

Rolf Buch

Thank you Rene, welcome to our half year 2018 earnings call. I am very pleased to have our new CFO, Helene von Roeder, joining us for the first time. So welcome Helene, again. Today we want to report our H1 results; we want to give you a general update on our business. We share with you our revised guidance and, of course, we are ready to answer your questions after the presentation.

As always, I start with the highlights. Organic rental growth is up by 4.1 % on a year-to-year basis. Operating expenses are reduced by 16.8 % ,mainly due to the synergy effect of conwert but also some additional efficiency gains. This leads, for the first time in our existence, to an adjusted EBITDA operation margin of more than 90 %, close to 91 %; this is 290 bps better on a year-on-year basis. FFO 1 accordingly increased by 11.5 % on a year-on-year basis, mainly driven by EBITDA operations improvement but also lower interest and for a less important part, less income taxes.

As you know, we are doing an H1 revaluation on only two thirds of our portfolio for efficiency reasons; these are the 20 largest German locations plus some additional German locations and Vienna. We have seen in this revaluation a 6.9 like-for-like value growth on the revaluated portfolio, which is a 5.7 like-for-like revaluation uplift based on performance and yield compression. Total value growth is € 1.7 billion which represents for the total overall portfolio 5.3 %

growth. Adjusted NAV grew by 10.5 % and on a per share base, due to the ABB we have done in May, it is of course only 3.5 %.

The new guidance now includes BUWOG and Victoria Park. The FFO guidance is € 1,050m or up to € 1,070m which leads with the new number of shares to € 2.03 to € 2.07 per share.

Of course, keep in mind that we raised the number of issued shares in May and we only have a half years elements of FFO from BUWOG and only one quarter from Victoria Park. If you do a so-called pro forma FFO per share including the full year BUWOG and full year Victoria Park, the FFO per share would be € 2.08 to € 2.12. Keep in mind that in 2018 we will not show any synergies from BUWOG, so this is the starting point for discussion for the guidance for 2019.

As you know, my most favorite slide is page four which actually shows that we are able to deliver more than the top line down to the bottom line in this quarter and this half year it is a relatively positive effect. As you can see we have a 3 % smaller portfolio in the first half year of 2018 in comparison to 2017 due to the effect that we have sold a significant part of our portfolio in 2017 at the beginning of this year, this is mostly non-core. But even with this smaller portfolio the top line is a little bit bigger because rental growth overcompensated the smaller portfolio. We have 5.6 million more topline.

Operating expenses were down almost 17 % driven by, as I mentioned, conwert synergies and ongoing internal improvements. In addition to this, also value-add business developed properly, so in the end the EBITDA operation is up by 25 million. So only 5.6 million topline, 25 million more EBITDA operation and then you can see that by better financing in the end the FFO 1 is up by 52.6 million. So 5.6 million topline, 52 million FFO 1.

Keep in mind that at the end of the year 2018 we will stop disposing. That is why we will see a higher top line in the future so this will also give you an indication how the development of the bottom line will develop in the future. And with this I hand over to you Helene.

Helene von Roeder

Thank you very much, Rolf. So as a short intro since some of you have not met me yet, my name is Helene von Roeder. I joined Vonovia on the 9th of May as the CFO following a long career as a banker and, believe me, it is great to be here. So with that, let us carry on with the numbers.

Now, you may have noticed that Rene kindly included a small grey box at the top of the page. To explain these boxes a little bit: You already saw on the highlights page Rolf showed to you that BUWOG and Victoria Park are fully consolidated in our IFRS accounts, balance sheets, P&L and so on. However, our performance KPI's such as EBITDA or FFO are reported excluding any contribution from BUWOG and Victoria Park.

With BUWOG closing at the end of Q1 and Victoria Park at the end of Q2, it would have been only one quarter of BUWOG anyway and we felt it would be more useful to allow for a clean Vonovia stand-alone comparison. This applies to a few pages in this presentation and we have included these small boxes as an indicator on the upper hand left corner where this is the case. So please follow the grey boxes to know what is included and what not.

So this page is without BUWOG and Victoria Park, so stand-alone Vonovia. So absolutely no surprises also on the rent growth part of the business. We are overall 40 basis points stronger than in the prior year and that is driven predominantly by our increased investments. I would not over-interpret the 20 basis points lower contribution from the market rent growth, that is the third line, because we should not forget that last year included a very strong 'Mietspiegel' in our two largest locations, Berlin and Dresden. And second, more and more of the rent growth from re-lettings you see in the line item modernizations, as the new lettings line only includes those re-lettings where we make no substantial investments, so as the tenant moves out and we simply let the apartment straight away. And the re-lettings without material investments are getting fewer and fewer.

So that brings me to a critical point about which we believe there has been a bit of confusion in the market. There has been a lot of discussion about the so called reversionary potential and what the real reversionary potential of the different players is. In quite a few analyses that we have seen, there is a big gap between the reversionary potential of different companies. So we would love to put that a bit into context: In most markets, and certainly the ones where demand is bigger than supply, you do not see many lettings without new investments, because the investments allow you to capture a substantially higher uplift in the rent. So the growth in market rents is to a large extent driven by investments and not simply a market move on its own. And to capture this very reversionary potential, you need to make these investments. Again, absolutely nothing wrong with investments as it leads to superior returns but, quite frankly, we believe this is a bit misleading to suggest that there are markets where re-letting rents come for free and give you a 20 % or 30 % value uplift in rent.

As you know, in Germany we have a law with the rental cap of 10 %. This is in place in many places, especially the big ones, and it obviously makes it impossible for anyone playing by the rules to re-let above that 10 %.

So you are very familiar with our rent growth column in the regional markets overview, you will find it in the appendix on page 30. What that shows is the average rental uplift per regional market that we actually achieved following the so called optimized apartment investment over the last twelve months. So we believe that this is our reversionary potential.

Next slide. So as Rolf already mentioned, in terms of EBITDA margins, we continue to see very healthy growth. I personally believe that the margin excluding maintenance is the better metric, because spending less or more on maintenance is certainly not a sign of efficiency, just as spending less on maintenance is also not a sign of inefficiency.

So let me focus on the EBITDA margin excluding maintenance. Year-on-year that is up 290 basis points to now 90.9 %. As was said earlier, one of the drivers is a) the integration of conwert but this is also the result of continuous improvements across the company in different areas. So coming from the outside, to me this is the actual alpha that Vonovia has. Scale certainly works and it is in the DNA of the people here in Bochum and in the regions to continuously and relentlessly optimize processes. These improvements alone should enable us to at least balance the impact of cost and wage inflation for the foreseeable future.

So more of a technical page, we have already covered the FFO. Look at the grey thing at the top, this is Vonovia only. Again, on a per share basis the numbers look different, so if you look at the end of period vs. average, but that is largely timing. As Rolf already mentioned, we did a rough pro forma calculation again, assuming full contribution of BUWOG and Victoria Park in H1, the FFO per share would have been € 1.05 per share.

Looking at the like-for-like value uplift, the first thing you need to remember is that, as Rolf said, our approach has been very pragmatic. We did the same thing that we did in Q2 last year, where we simply said we will capture the valuation movements of the 27 largest cities, which is approximately two thirds of our overall portfolio. On this valuation portfolio we saw a like-for-like growth of 6.9 %, of which 1.2 % was from investments and 5.7 % from valuation uplift. So hence, performance and yield compression.

Now, as a side note, you will have seen what our peers have reported so this number is certainly an extremely strong number, in our opinion at least. In terms of the overall German portfolio, a few data points, € 1,561 per square meter, an in-place multiple on average of 20.5 and a gross yield of 4.9 %. The point on this page is to show the current in-place valuation in terms of multiple or fair value per square meter against the like-for-like value uplift for the first six months.

So some of the locations may certainly surprise you, when you look at the value uplift in H1 vs. their in-place valuation. It was certainly not the usual suspects that drove our values in H1 and I am not sure whether you have been to Augsburg, but it is certainly part of our current hit list.

Let us look at the investment clusters. As you know, we cluster our German portfolio not only by Geography but also by action, what are we going to do with it, what is our plan? And based on the latest clustering there are a few points we would like to highlight. The investment portfolio still holds a lot of potential. It is more than 50 % of the total portfolio so we are absolutely not worried about running out of ammunition anytime soon. There are many flats which we can still - and need to – still modernize.

Secondly, our sell portfolio is down to 10,000 units, or 1 % of the total portfolio. Most of this should be gone by the end of the year. So that is good news as we will no longer need to shrink our portfolio in exchange for a better quality portfolio, but operate on a stable portfolio basis instead of having to make up for top-line shrinkage before the rent growth starts to make a positive contribution.

And third, in terms of fair value, we now have approximately 90 % of our portfolio value in Germany and 10 % combined in Austria and Sweden.

Net Asset Value growth – so the adjusted NAV increased by 10.5 % at the end of Q2 in absolute terms and 3.5 % on a per share basis. Again, this is now including BUWOG and Victoria Park. We have talked about this in the past, but please allow me to reiterate our view on NAV and to what extent it is the right metric to use as a pure proxy for the share price of Vonovia and/or the value of our company.

To remind ourselves of the definition of the adjusted NAV: It reflects a brick and mortar the value of the building and it applies to market terms and assumes the properties are owned by anyone, any third party. Obviously this approach ignores, in terms of the business, the fact that we have the value-add business which, Rolf already mentioned, contributes strong margins overall to our business, and it also ignores the cost advantage and operating platform we have as a professional owner.

Now in addition for Vonovia, it also ignores the fact that we have a development business and it ignores the fact that we have cash flow coming from privatization.

A few words on LTV. Our LTV at the end of June 30th was at 43.9 %. Now clearly, as we settled the second tender offer for BUWOG about a week later, after the end of Q2, and also issued a € 500 million bond at the time, it probably makes sense to look at the LTV taking that into account. And then you are at about 45 %, which is clearly the upper end of what we think is the right range for German residential and for our business.

Obviously different market participants have different LTV comfort zones but we would continue to argue that even after the yield compression we have seen the in-place value of our portfolio remains conservative and we really do not see a scenario in which these values would come under pressure. On the contrary, pretty much every indicator we look at suggests that there is more to come.

So we believe our target range of 40-45 % gives investors enough of a security buffer, while at the same time not putting undue burden on our equity. Looking at our own internal projections for the year end and even before any yield compression, we should be at the upper end but inside our target range. So depending on the amount of yield compression still to come we will be moving south from the top end and further into the range.

Just as a broad rule of thumb: €500 million of yield compression result in approximately 50 basis points of LTV reduction. So here is another familiar page and to me it is a Stefan Kirsten testimonial. It is the perfectly spaced benchmark bond. The maturity profile here now also includes Victoria Park, which does not change the overall picture that much. We are very happy with this profile, we like the diversification of debt sources and we continue to see its opportunities especially in the near term to still benefit from upcoming refinancings. And to be honest, it is a great starting point for me as the CFO and with that, over to Rolf.

Rolf Buch

Thank you Helene, so I continue with the value-add page. As you know, value-add business is a long-term business, so a very steady process. Do not exchange material news from quarter to quarter. As we have said for one year now, we expect for this year 120 million of adjusted EBITDA from this business. And I want to mention that all contributors of this business are directly related or directly linked to the rental contracts.

So stability and risk profile of this business is at least the same as the stability of the underlying rental contract. There is probably one exemption, which is not a big part of the 120 million, which can be the energy services because due to regularity reasons you cannot link the energy contract to the rental contract directly. All the others are directly linked. I know some of you have followed a lot of discussions about multiples of this business. We have the clear opinion that this business has the same underlying stabilities than the rental contract and that is why it should deserve the same multiple on the EBITDA.

We continue to believe that value-add services are the material growth driver and will be increasingly relevant in our business for the next years.

On the next page we report on sales. It is not much to report, I think it is only good news, but this sales slide also gives you a flavor, as Helene already pointed out, that the trend in value development in Germany is still completely intact.

As you can see, we have privatized in the first half around 1,000 units and despite the significant value uplift we have seen at the end of the year 2017 we still achieve a 30 % value uplift, so this means also the value uplift in the valuation is reflected in the market price of the units we have sold.

Very positive is our uplift in the portfolio which we have formerly called non-core, today we call it sell. You know, this is a portfolio which we think is not the best and here we have now achieved a 15.4 % margin based on fair market values, this is, I think, one of the highest margins we ever have shown. This is also a key indication that market prices are turning to the upward.

Coming to our investments: On our investment program we are fully on track with the execution. €361 million are already accounted for in H1. This is a little bit lower than we expected, this was due to some difficult weather conditions at the beginning of the year. The good news is that the remaining 640 are kicked off and are at various stages of completion. So we will deliver this year the one billion investment program.

We are a little bit proud of this because this is roughly 20,000 apartments which will get an energetic modernization and an additional 13,000 apartments which will get a modernization from the inside. We will get to this point again in the guidance and Helene will talk about it but let me please explain in a bit more in detail how this program works. The main part of the physical work has to be done in spring and summer and early autumn, because to realize the rental growth at the end of the year we have to send out the rental growth notifications in September.

So only a slight shift of the execution, probably done by a lack of subcontractors or some delay, would actually lead to a later rental increase which is probably not coming in December, but in January. So on the point in the like- for-like, it would lead to a lower rental growth; in reality it has no impact because the rental comes up in January. So please keep this in mind when we are talking about the guidance later.

Coming to new construction: The short version of this slide is: we would like to do more but we simply can’t because it takes too long to get the building permission. This is not a specific Vonovia problem, this is a general problem in Germany. It might sound ironic to most of you given the supply and demand imbalance in urban areas, but this is unfortunately Germany in 2018. And this is really the only reason why the volume of completion is not higher. It is not lack of opportunities, it is not lack of financing, it is not lack of production capacity in the space creation program, because we are able to produce it in the factory, it is simply the lack of building permits. And it takes me a lot of time at the moment, to explain to politicians that they have to change something. But this will be a long journey.

On the other side of the coin, of course, this is very good news, because this means that the structural imbalance between supply and demand in Germany will not go away in the near or medium term.

In terms of the overall business, you will see this in higher value uplifts because of shortage in the big cities and, of course, this is good news for investors, it is not good news for our company.

So this year we expect around 500 completions and for the next year we think we will see around 1,000. If you add the current BUWOG estimates, the Vonovia 2019 number will be around 2,800 completions over the next year.

Only one very short slide about the BUWOG development projects. You know, the development business of BUWOG is now part of Vonovia since roughly three months. I do not want to spend too much time on page 18, but I think this page shows you that we have in only three months approved a magnitude of more than € 200 million of new development projects, so I think you can see here that the development business of BUWOG will grow and is loved inside the Vonovia family.

Giving you a short update on BUWOG, Victoria Park and our European activities in general: As you can see on page 19, BUWOG, we have achieved 90.7 % voting rights; we have started to integrate the business in Q2 of this year. The operational integration of the German operating business is fully on track and will be expected to be finished in the end of 2018, so you will see the positive effect during the year 2019. The next step, the BUWOG EGM on the 2nd of October, where we will decide the squeeze-out, the cash component for the minority shareholders will be the same than the offer price of € 29.05 per share.

In Victoria Park, at the moment we have 61.4 % of the voting rights. We consolidate the company fully, the activities have started at the beginning of Q3. The Victoria management team stays in place, we believe that they are doing a very good job. We believe also that we will realize with them good synergies in purchasing of construction material and also helping them to execute the Vonovia business model also in Sweden. It is very positive and we think it will be a great achievement, because Sweden is a very attractive market. You know, in Sweden they have the 1 million housing program, so a lot of the houses built in the 70's now need modernization, which is exactly our modernization program. So we will bring this and use Victoria Park to do this modernization in addition to it, because so many apartments need modernization, a lot of companies are ready to sell smaller portfolios and Victoria Park is ideally positioned to buy these smaller portfolios.

So we believe that the European activities enhance our accretive acquisition opportunities. Similar to Germany, we closely monitor these opportunities in the respective regions. In Austria we also continue to build further development while we are also selling because of the very low exit yields, so it is a very effective business. In Sweden, I have already said, we will continue to acquire and to install the Vonovia business model.

We believe that France is the long-term biggest opportunity in Europe, but it is not ready yet, we have to wait for legislational changes. My expectation is not that we will do massive acquisitions in France at the moment, we are there to look on this market, to test the market, to get experience and to prepare ourselves for the moment of the legislation – which from my point of view will happen, if it happens to be there, because Vonovia will be the only company who can combine operational experience and knowledge out of Germany, together with capital. I think that we will be well positioned, but we have to be patient. So do not put it in your business models at the moment.

The Netherlands might also be an attractive market but we have decided to concentrate on Austria and Sweden first. All other countries in Europe we have put lower on our priority list, so this is not where we are spending time at the moment. And with this I hand over to Helene.

Helene von Roeder

So guidance, our updated guidance for 2018 now includes the contributions of nine months of BUWOG and 6 months of Victoria Park. It does not include any synergies for these deals. The only exception to that inclusion is obviously the organic rent growth which by definition looks 12 months back so this is Vonovia only without BUWOG and Victoria Park.

So let me start with the organic rent growth: We are a bit more conservative for the financial year 2018 and we have revised the guidance to around 4.4 %. This 4.4 % compares the total one month's rental income for December 2018 to that of December 2017. And as Rolf just pointed out, it is a timing point. If you were maybe to compare January to January, that number will already look different. This is not at all, hence the result of us becoming more pessimistic on the business or on the market, but purely driven by those two reasons, which are timing related.

The first one is the lower space creation volume, which is the result of those building permits since they are not coming through and the other reason is that the poor weather conditions earlier in the year and combined with the bottleneck of craftsmen to actually get the work done, have slightly delayed some of the projects. The rent growth will come for sure, but it may be shifted a bit on the timeline and we may not be able to capture it in 18, but only in 19.

The way this works in Germany is that you need to finish the work, have all of it accounted for and then you can send out the letters to the tenants to ask for the rent increase. And because there is a mandatory announcement period of three months, you need to send out these letters no later than the end of September, in order to book the rent growth still in 2018. This will not be possible for a small share of the investment project. It is not lost. It will simply come in 2019.

So, all said, this is not a cash-flow or FFO issue, because we are simply talking a shift in months. Either way, even as we are on 4.4 %, our rent growths will be higher than last year and that is something that not many players in this space can say.

So, going on to the other line items of the new guidance, we expect 1,900 million of rental income at the midpoint and then FFO between 1,050 and 1,070. On a per share basis, because of the increased share counts this equals to € 2.05 at the midpoint, which will be an 8 % increase year-on-year.

Assuming a pro forma 12 months contribution from BUWOG and Victoria Park, the FFO per share for the 2018 guidance would be between € 2.08 and € 2.12. Maintenance will be higher and that is basically volume-driven as we now also include BUWOG and Victoria Park in this number.

We also increased the guidance on privatization volumes and margins which is due to including BUWOG. As many of you are familiar with the special Austrian business model which has an ongoing privatization included in the normal course of business.

So, finally we think we can sell up to 14,000 non-core units, which would reduce that part of the overall portfolio to almost zero. Given the strong appetite in the market, we raise our expectations for the fair value step up to 10 to 15 %. And now over to Rolf for the closing remarks.

Rolf Buch

Thank you, Helene. So, I just have to wrap up. I think you have seen a very strong operational performance that continues margin extensions.

Market conditions remain very supportive and one evidence for this is the H1 valuation.

Guidance 2018 is compelling, but does not reflect the full potential of BUWOG and Victoria Park acquisitions. This will materialize significantly in the year 2019.

The outlook of the nine months reporting on December 2006, and in this outlook we will have the indicators reporting format in addition to and beyond the traditional FFO1 logic to properly account for the different earnings contributors. So, the nine months reporting will be very interesting. With this I hand back over back to Rene. Thank you very much.

Rene Hoffmann

Yes, thank you Rolf and I will hand right back to the operator to kindly open up the Q&A.

QUESTION AND ANSWER SECTION

Operator

First question is from Thomas Neuhold, Kepler Cheuvreux. Your line is now open, Sir.

Thomas Neuhold

Thank you very much for taking my questions. I have several ones and I would like to start with a couple of questions on the slightly reduced organic rent growth guidance. If I understood you correctly you sound quite optimistic that these are just timing issues and no structural issues, but if you look at the explanations, like delays in building permits, it obviously takes longer to get building permits. Will the recent experience lead to any shift in your strategy in terms of how you are handling your construction activities that you maybe put more projects in the pipeline or is it an issue that you have a reasonable amount of projects you can carry out?

And also, on the second issue that you have mentioned, the availability of craftsmen. Can you give us an update what the situation currently is in the market or what you plan to work out? Or you could give an indication of what kind of cost inflation you are currently facing with these kind of services?

And then related to the new guidance, I also have a clarification question; for modernization investment, guidance of 1 billion is unchanged. On slide 20 that includes BUWOG and Victoria Park. I just wanted to make sure that the figure also includes the BUWOG and Victoria Park modernizations and what is future for Vonovia only on a temporary basis? And I have some of other questions.

Rolf Buch

So, Thomas probably the last question first. We have said around 1 billion for the Victoria Park modernization, which is not meaningful enough to change the business method. For the BUWOG, you know our process, we are sorting the portfolio in this year to build it up in the next year. So, by definition BUWOG will not see in their portfolio any modernization investment in 2018.

For the concept of lack in craftsmen and lack in building permissions: Through the lack in craftsmen we are comfortable, we are sure that we will deliver the 1 billion also in the next years, because of our own craftsmen organization. The shortage is mainly in the availability of sub-contractors to compensate short-term delays which we had this year, in the beginning of the year. So we thought we can catch up with some more sub-contractors and this actually showed up to be very difficult, because there is a significant shortage in Germany of building construction. But due to our own craftsmen organization and due to our long-term lasting cooperation with existing craftsmen, we believe we will deliver the 1 billion in the next years. So, there is no reason to be nervous about it.

The second reason is the construction permission. The construction permission is a real issue. We are spending a lot of time. Actually we are doing two things: The first is what you are saying, we are trying to get more and more construction permissions in the pipeline, to get more and more. So, we have enough projects, it is not a question of people capacity but the construction departments all over Germany are completely overbooked. The second is, that we are in concrete discussions with the politicians to change the system. It is too complex, it is too long, it is too expensive, and it is not concrete enough. But this is something which I believe will happen in the next five years. This is not something that will change the situation shortly. We want to increase to the 2,000 units, but this will take unfortunately longer than we have expected.

But again, as I said this is a very quiet indicator, because the only way how to solve the imbalance between supply and demand, is more supply and with these systems we will not deliver enough supply and the gap will become bigger and bigger, year by year. You can see this also in Germany, you know the construction is going down and not up. And the political will is that construction figures will increase, but they are obviously not capable to make this happen.

Thomas Neuhold

Okay, a follow up on that 1 billion CAPEX guidance, if I may? At Vonovia you are including the space creation in this 1 billion and then BUWOG also has a development portion of its portfolio. Will you in the future also put this build portfolio in your CAPEX guidance or will you keep that separate like you do now?

Rolf Buch

To be very clear, in the 1 billion that we have now in this presentation there is nothing from the BUWOG development business in it. This will come on top and as Helene has told you, we will give you the complete figures and the complete guidance in the Q3 reporting on the 6th of December. But definitely for the next year this will come on top of the 1 billion. The 1 billion is for the existing Vonovia portfolio, which we intend to do the next year.

Thomas Neuhold

Thanks for the clarification.

Rolf Buch

And also, to be clear we have less new construction, we will do more traditional modernization.

Thomas Neuhold

Okay, and then the next question is on BUWOG itself, I was wondering if you had already time to strategically review this business. Are there any plans to further roll out the development business of BUWOG to other German big cities apart from Hamburg and Berlin, that BUWOG currently is active in? Do you consider that the build-to-sell business, as a long term strategic part of your business, or do you think it is better to switch the focus rather on build-to-hold strategy going with a portfolio of standing assets.

Rolf Buch

So, actually BUWOG is active in three cities - in Vienna, in Hamburg and in Berlin. I would not exclude that BUWOG will go in other cities but the priority is to build the development projects in these three big cities and as you have seen on the list, we have approved already a lot of new projects. So, there is a lot of new projects available so there is no immediate need to expand to different cities.

The development-to-sell business is a very attractive business in terms of IRR and it actually fits together with our development-to-hold because, you know, in Germany normally you have to have a mixed combination. You have a part which is to hold, by definition because it is social housing and there is a part to sell. So, I would say that BUWOG will continue their ways of what they are doing today. They will do development-for-sell, which is a very attractive business, but they will also do development-to-hold and there will be some synergies with Vonovia. For example, we want to use BUWOG's model of constructive technique, also in the development business. So there are synergies and the detailed plans we will present to you on the 6th of December.

Thomas Neuhold

Thank you. And my last question is a short one on Victoria Park. I was wondering if you could give us an update on the potential Swedish acquisition pipeline?

Rolf Buch

No, I cannot and I will not because you know we are again always opportunistic. What you have to keep in mind is the mechanics of the market. In Sweden, you see a lot of small portfolios. So, this is not doubling Victoria Park, but pick up smaller portfolios which have come up regularly to the market, with 500/600,000 units, mainly sold by local companies, because they need a lot of investment in these buildings which were built in the 70s. They are forced to sell. And this is a typical way how Victoria Park will grow, but we are optimistic, we do not exclude anything, but this depends on price and our acquisition criteria. So, it is the same rule to what you have seen us operating in the last six years in Germany.

Thomas Neuhold

Okay. Thank you very much.

Operator

Thank you. Next question is from Sander Bunck, Barclays. Your line is now open, Sir.

Sander Bunck

Hi. Good afternoon to you. Two questions from me. I will start with the first one. Just looking at slide 30 and just how the portfolio has been performing and I noticed that Berlin at the moment has the highest multiple, but is actually producing lower than average rental growth. How are you looking in terms of capital allocation here? Is it a good time to dispose perhaps a couple more Berlin assets and would you in that case be looking to rotate that for example into Sweden? Or is it something you believe structurally has a lot more upside?

Rolf Buch

I would say we are not ready to dispose more Berlin assets. I think it is too early, but what we are definitely not doing is to buy for the prices we see at the moment in Berlin, new Berlin assets. So, I think Berlin is okay, Berlin has, by the way, the second biggest multiple. Munich is higher. But Berlin has a relatively high multiple and it is a stable market. It is not the best and not the worst in our portfolio.

Sander Bunck

Okay. So, there is no additional idea to dispose further assets there for now?

Rolf Buch

Nothing meaningful which has to be mentioned here.

Sander Bunck

And also, say that a further acquisition in Sweden may come along, would you be thinking rather than for example coming back to the equity market, would you be thinking about disposing more units for example in Berlin?

Rolf Buch

I would not, I think we have different units which we have to dispose before we are disposing Berlin units. So, Berlin is not the worst portfolio, but I think the discussion is not there at the moment because we need an opportunity in Sweden first.

Sander Bunck

Okay, sure. And then the other one is around regulation. It is actually consisting of two parts. The first one is, you mentioned in your statement that the limitation of modernization allocation is going from 11 % to 8 %, but given that you are at 7 % at the moment, the impact is going to be quite light. Can you just confirm that if that regulation were to be implemented that it would have no impact on your rental growth?

Rolf Buch

I would point out, it is very light, like I said before, but in the end it is close to zero, so you will not see it in our figures.

Sander Bunck

Excellent. And then kind of a follow up on that, is there any other update on any of the other potential regulations that we should be aware of? Or are those discussions kind of starting after the summer and we will have updates on those after?

Rolf Buch

No, there is nothing new. The probability that they will pass the law is close to 99 %, so this we will see after the summer. After discussions we have to wait and in general, I have to mention, that at the moment housing is getting a hotter topic in Germany, due to the fact that actually the big cities are completely empty with empty flats. So, this is a high political point besides immigration. This is the most important political issue in Germany, so that is why you will see also the German newspaper and the German political discussion is every day, today a report of housing and why there is a shortage and a lot of discussion what would happen and including getting it back to the senate of Berlin. So, there are also a lot of crazy things also going on, so this is at the moment a little bit of a hotter environment than we were used to.

Sander Bunck

Okay. And would you think that any of that could have a more material impact on your operations?

Rolf Buch

I cannot see it at the moment. I am just mentioning to give you the full picture because some of you are also reading German newspapers.

Sander Bunck

Excellent. Thank very much.

Operator

Next question is from Christopher Fremantle, Morgan Stanley. Your line is now open, Sir.

Christopher Fremantle

I just wanted to ask a follow up on the valuation. You said very clearly only two thirds of the portfolio was revalued. Can you just a give a bit more clarity on how the two thirds were selected? Is that driven simply by the size of the locations or is it by taking those parts of the portfolio whose valuation is likely to have changed the most? In other words, should we expect the growth in other parts of the portfolio to be broadly comparable with what you have revalued? Or should we expect it to be lower or higher? Any comments that you can give on this, or, you know, any guidance you have received from your valuers would be helpful? Thank you.

Helene von Roeder

Thank you. So, what we did we took the 25 cities and then we added those where we have seen the biggest value increase to the valuation. So, hence as a result, your assumption is broadly right that overall we should see a similar development.

Christopher Fremantle

Okay. Thank you.

Operator

Next question is from Kai Klose, Berenberg Bank. The line is now open, Sir.

Kai Klose

Hello, good afternoon. I have got two quick questions: The first one on page 13, where you show the global ICR of 6.0 times. As of March you showed a global ICR including BUWOG of 4.9. Now you show it excluding BUWOG and Victoria Park of 6.0? Would we have the comparable numbers comparing Q1 with Q2?

Helene Von Roeder

I think we need to find these numbers and deliver them to you separately. I would not have them off the cuff here now.

Kai Klose

Okay, no problem. And the second question, we had in the first half about 50.5 million of non-recurring items. Could you indicate what would be the number of the second half, just as an indication?

Helene Von Roeder

So, we have done a quick look around. It sounds like we would be safer also to deliver you a more exact number later on, rather than have a guestimate at this point. We know where it is, but let's be safe.

Kai Klose

Perfect. Not to hurry. Thanks a lot.

Operator

Next question is from Manuel Martin, ODDO BHF. Your line is now open.

Manuel Martin

Yes. Hello, ladies and gentlemen. Two questions please. Question number one: Could you give some color on Victoria Park, because you said that you will not integrate Victoria Park for the time being. It will be used as a platform in Sweden. Maybe you could give some color on that and does Starwood have something to do with that? Because I think they still hold 30 %. That would be the first question. The second question would be regarding your FFO1 guidance for 2018. Do you see some more room for some improvement there for the rest of the year? Because it seems to be rather conservative. Thank you.

Rolf Buch

You first question I take for Starwood. You have seen that we have now a new supervisory board in Victoria Park, so you can see that we have achieved full control of the company. To be very clear Starwood for us is a big RETT blocker. They have no influence in the politics of the company, so we control it. Of course, it will be accounting-wise completely integrated into Vonovia. I am just saying we will not change the management teams, they are Swedish people, they know the market. They have a very clear knowledge about potential acquisitions and as you know the Starwood business, as a Victoria Park business, is relatively simple today. They are doing actually optimized apartments, what we are doing, they are doing it on a much more bigger scale than we are doing it, because they have access to more apartment blocks which need modernization and are empty.

Manuel Martin

Okay.

Helene von Roeder

FFO - obviously we are always working to be better, but at the moment, as you know, FFO guidance is our own best estimate. So, I think we should all be working with what we have right now, but with our constant aim to improve. And I have another number: 60 million, is the number for this year for one-offs. In case you wanted to include that, plus or minus approximately.

Manuel Martin

Okay. Thank you.

Operator

Next question from Valerie Guezi, Exane BNPP. Your line is now open, Madam.

Valerie Guezi

Yes, good afternoon. I just have a couple of questions. My first question is on your FFO1 per share. So it is being downgraded now that you integrated Victoria Park and BUWOG. And I was just wondering if you could comment on, you know, what part comes from the downgrading organic growth and what part comes from the Victoria Park and BUWOG? And maybe if you can tell me how you think about that? And I know there are some other businesses, within BUWOG to contribute to value creation.

My second question is on disposals, I just wanted some clarification, because you said there is only one percent of the portfolio left to be sold. But I assume you are still going to make disposals in future years, so maybe if you can sort of tell us how you decide on a yearly or monthly basis, what apartments you are going to sell and keep? Thank you.

Rolf Buch

I will take the second question and later Helene will take the first one, because the second is a very easy. You know we have a process once a year where we sort all our 400,000 apartments in different brackets. So, of course you are right, there might be a few apartments that end up in the sales portfolio… or the privatization portfolio. Actually it is the same size always, because they do not need independent land registers, which we are not doing new ones at the moment because we still have enough privatize. But for the sales business, you know, historically we had a significant not strategic part, and this will be sold. So, I think you can see in the guidance that we were selling 14,000 units and we are planning to sell 14,000 units this year. If this will be around 1,000 next year, this is probably a rough figure. So, the huge amount of selling of units which we are thinking does not fit with us, will be over in this year because then we think that we have a clean portfolio.

It was a long journey for us, it took us five years to clean our portfolio, to concentrate our portfolio on the big cities and the surrounding of the big cities, but this job will be done and I repeat again, this will have a massive impact on our figures in the next year, because we reduce our topline by disposing assets and this will stop in the next year.

Helene von Roeder

Okay, let's do FFO1. I think you must be looking at page 20 and then let's go on the FFO1 line-by-line. Because we look at 2017, actually, so it is 1.90 per share, then we sort of move on into November '17 where we have an old guidance of 1.98 to 2.02. Now I presume the reason why you are saying that there has been a downgrade – which by the way we do not agree with – is like if you then move on to the next column, which is the May 18 column, we are suddenly seeing a slight drop. And the reason we are seeing that slight drop from that column to the next because we have actually increased the number of shares. So you have the dilutive effect of the ABB in there, which basically means that optically you will consider this as a downgrade. It is not and if you look on page seven you will actually also see in the bottom two lines the exact effect of dilution versus not dilution. So, I think basically that must be a little bit of a misreading.

Rolf Buch

To make it very clear, we have more FFO, but we have more shares, we have more shares actually for the full year, but you do not see the results of BUWOG and Victoria Park for the full year. So, this is the technical effect. In the next year, and I think we have given you guidance in the presentation, you will have a full year of BUWOG, you are going to have a full level of Victoria Park with the same number of shares and that's why I think this is a technical effect. It is not a downgrade.

Valerie Guezi

Yes, but no, I mean if I speak to what you said in the past, you said that when you acquire a business and you fund it with equity, it should be accretive to FFO and you funded this acquisition with equity and it is not accretive to FFO. So, I am just a little bit confused, I understand that there is equity into it. But maybe if I want to see that otherwise, would you be, in the past to do more acquisition funded by equity that will be dilutive to FFO?

Rolf Buch

No, the acquisition is not dilutive to FFO, because this is just a fact of shares on a specific date and the figures on the whole year. If you would calculate with average number of shares the picture would look completely different. So, indeed our criteria is to be accretive in the first year. If you do the performance figures, so if you take the new numbers of shares including the FFO from Victoria full year and BUWOG full year, then the FFO per share will increase even to the last guidance. It will be two cents more, and this is then without synergies which will come in 2019.

Valerie Guezi

Okay, that’s very clear now. Thank you.

Operator

Next question is from Marios Pastou, Credit Suisse. Your line is now open, Sir.

Marios Pastou

Oh, hi good afternoon. A very quick question from me on the BUWOG development business. I am interested in the levels of building cost inflation we are seeing in the development, mainly within Germany and if there is any measures you are currently considering to apply to try and stabilize these to protect the return, especially from the development-to-sell business? Thank you.

Rolf Buch

Very good, certainly because inflation also gets on the selling price. So, at the moment you normally build with a fixed term and then if inflation is higher, then actually your selling price gets up, so your margin gets up. This is why development business is so attractive at the moment in Germany. But you are mentioning a point which is important for us overall. You have seen globally that the last labor agreement for the construction industry foresees a labor cost increase of 5.7 % for the construction companies, which of course will be transferred into the price list, so you will see a significant inflation. For Vonovia, our inflation of labor is less, because our craftsmen will get around a 2.5 % salary increase this year. So, we are protected by this effect by our own craftsmen organization. I know you have asked the question about the development, but I just wanted to complete it here. For the development inflation is good news, because you get a higher selling price for the apartments.

Marios Pastou

Okay, very useful. Thank you. So, you were able to pass on pretty much all of the cost inflation through inflated prices, is that correct?

Rolf Buch

Actually, to be very clear, normally the cost is already agreed with the general constructor for the construction, so you have no cost increase in two or three years, but you have a selling price increase, so the margins are getting up.

Marios Pastou

All right, that makes sense. Thank you very much.

Operator

As a reminder if you would like to ask a question, please press zero one on your telephone keypad now. As far as there are no further questions, I hand back to Rene.

Rene Hoffmann

Thank you Kai and thanks everyone for joining. As a reminder, our nine months results will come out on December the 6th, but I hope we will speak on one occasion or the other before then. As always feel to reach out to me or the team with any questions or comments you may have. That is it from us today. Have a great weekend everybody. Thank you so much for your participation.