

Rise Case 2022

Jeudan's Business Model of Bredgade 40-42



jeudan

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Introduction to Jeudan

Jeudan is Denmark's largest listed real estate company with more than 200 properties worth 29 billion DKK in total. The properties are primarily rented out as offices, but also housing and retail stores. Every day, 100,000 people live, visit, work, or shop at one of Jeudan's properties. Jeudan is built on a lasting interest in Copenhagen and annually invests hundreds of millions into maintaining and improving the historical buildings in the city.

Jeudan contributes to the development of Copenhagen, which includes investments in Copenhagen's urban spaces. Notable projects are the construction and ownership of Torvehallerne KBH, participation in the development of Ofelia Beach, Sankt Annæ Square and the Enigma Museum at Østerbro. Overall, Jeudan's vision is to contribute to the sustainable development of Copenhagen while preserving the cultural heritage of its historical buildings.

Jeudan is a long-term investor and primarily finances their real estate investments with long-term, fixed interest bonds¹. As for short-term bonds, Jeudan hedges risk with 10-year interest rate swaps.

¹ Jeudan's Annual Report 2020

Bredgade 40-42

Jeudan owns the building Bredgade 40-42 consisting of 13,226 m² in the inner city of Copenhagen. In the basement of the building, there are 150 parking spaces. Jeudan is considering either renting Bredgade 40-42 out as offices or renting it out as a cultural event center. The business model of the cultural event center is to rent out the building to event organizers for 6-12 months. The intended events are various exhibits and shows, ranging from art exhibitions to theatre plays.

Your job

You have been hired as consultants to help Jeudan decide whether to rent out Bredgade 40-42 as an office building or a cultural event center. You have 6 hours to come up with your solution consisting of a maximum of 7 PowerPoint slides with 1 being a front page. This gives you 6 PowerPoint slides to present your findings and final recommendation.

To succeed in the case competition, you must:

- Present your findings with a clear storyline. It should not necessarily follow the order of the questions. Present your answers top-down, by starting with your recommendation and subsequently supporting this with your analysis and rationale.
- Ensure that your slides are readable, well-structured, and to the point. The judges will choose semifinalists purely from the handed-in PowerPoint slides.

Your solution will be judged on three criteria which are:

- I. There is a clear and well-structured storyline.
- II. Choices are made with concise and convincing arguments.
- III. Choices and conclusions are backed up by high-quality analysis.



Business Model of Bredgade 40-42

1 The Valuation

To decide between renting out the building as offices or the cultural event center, Jeudan would like you to carry out a valuation of Bredgade 40-42 as both an office space and a cultural event center.

How Jeudan Values Buildings

I. Calculate the Net Operating Income (NOI)

First, calculate the Net Operating Income (NOI) for the building. The NOI is the net income from the primary activities of a building and does thereby not contain other costs such as financing costs.

$$\text{Net Operating Income} = \text{Operating Revenue} - \text{Operating Expenses}$$

II. Calculate the Value with the Required Rate of Return (RRR)

Second, calculate the value of the building by dividing the Net Operating Income (NOI) by the Required Rate of Return (RRR). The required rate of return is the minimum amount of return Jeudan would expect for taking on the risk of a given investment. The required rate of return is thus an expression for the return that similar investments with similar risk profiles generate.

$$\text{Value of Building} = \frac{\text{NOI}}{\text{RRR}}$$

Note: The RRR that Jeudan uses and is provided in this case takes the expected growth of NOI into account and you do thereby not need to change the formula to account for this.

For central Copenhagen, Jeudan knows the following statistics about rental income, operating costs, and the required rate of return.

Table 1.1: Rent and Operating Costs. Source: Jeudan and Collier's PULS 2021Q4.

Purpose	Rent in Inner Copenhagen	Maintenance Costs	Property Taxes & Insurance Costs	Required Rate of Return 2021 Q4
Offices	2,150 DKK/m ² /year	60-90 DKK/m ² /year	1.8-2.2 mio. DKK/year	3.00%
Event Center	2,600 DKK/m ² /year	100-150 DKK/m ² /year	2.7-3.3 mio. DKK/year	5.25%

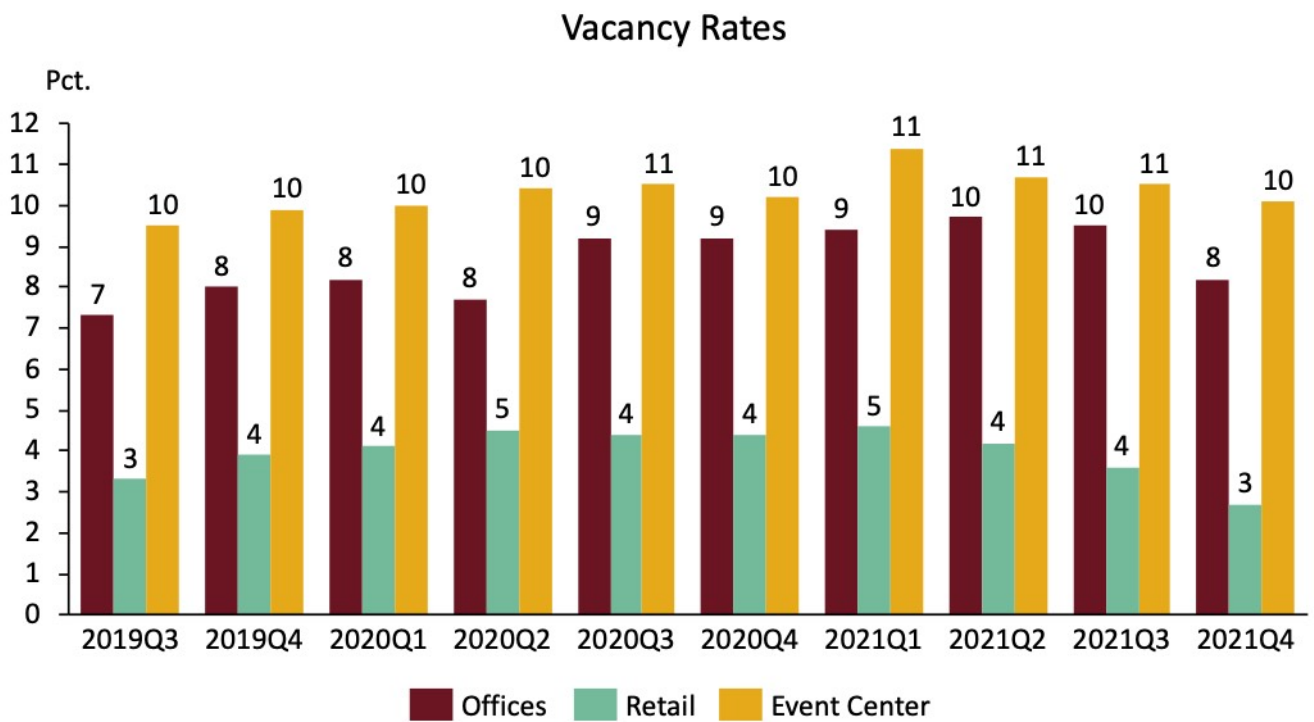
If the building is rented out as offices, the 150 parking spaces would be rented for a flat fee of 2,500 DKK per month per parking space. If the building is rented out as an event center, the parking spaces would be private rentable parking spaces open to the public including visitors and customers of the event center. From similar rentable private parking spaces in the nearby area, Jeudan has the following information.

Table 1.2: Private Parking Statistics. Source: Jeudan.

Location	# Parking spaces	Time period	Price DKK/hour	The average share of occupied parking spaces
Sankt Annæ Plads	500	08.00 - 18.00	40	62%
		18.00 - 08.00	25	21%
Dronningens Tværgade	300	08.00 - 20.00	50	71%
		20.00 - 08.00	28	23%

The vacancy rate is the share of properties that are not currently being rented. The vacancy rate in inner Copenhagen is as follows:

Figure 1.3: Vacancy Rates. Source: Collier's PULS 2021Q4.



**What do you estimate the value of Bredgade 40-42 is if the building is rented out as offices?
 What is the value of the building if it is rented out as a cultural event center?**



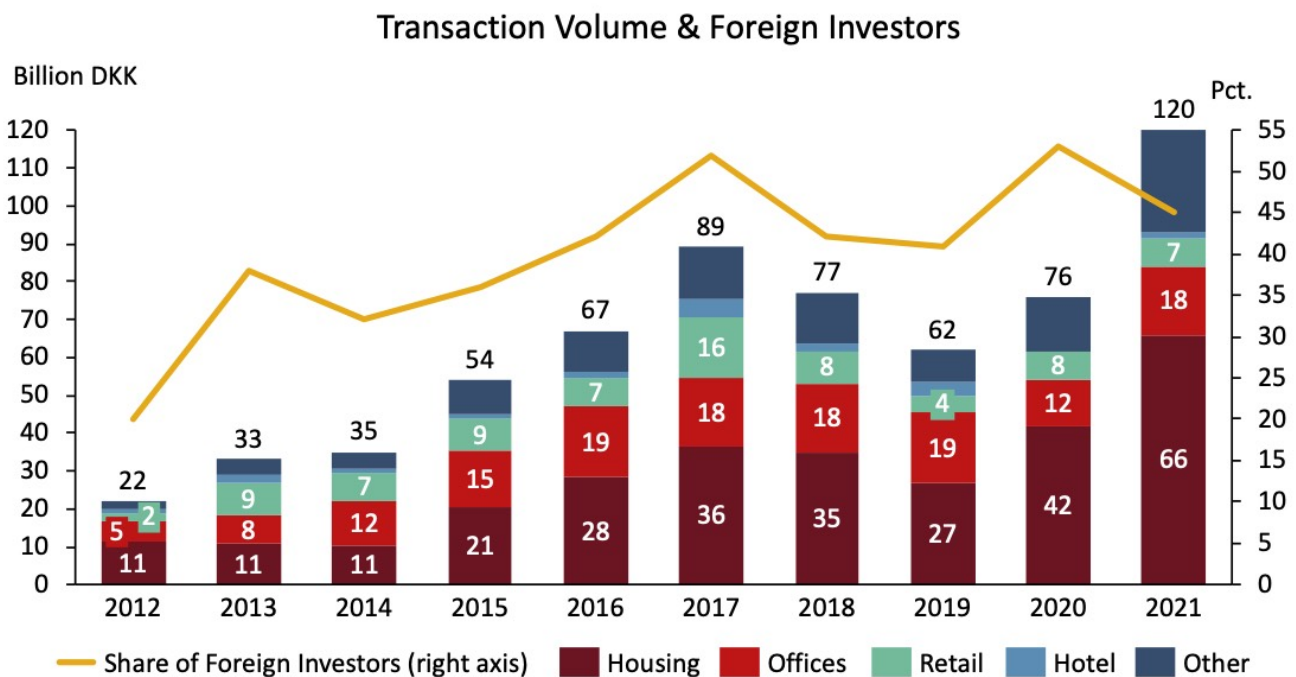
2 The Risks

To help decide upon the business model of the building, Jeudan wants you to examine the possibility and impact of three future risk factors on renting out Bredgade 40-42, both as offices and as an event center. Specifically, analyze how the required rate of return and the valuation of the building could be impacted. The risks are detailed below.

I. Increased demand for investments into Copenhagen real estate

There is an increasingly high level of demand for investments in Copenhagen real estate. In Collier's 2021 Q4 Report, they estimate that Danish pension funds have 50 billion DKK allocated to the real estate market that has yet to be invested. Foreign investors also increasingly look to invest in the real estate market of Copenhagen. The transaction volume is the annual value of all executed real estate deals which shows this trend.

Figure 2.1: Transaction Volume for Danish Real Estate. Source: RED



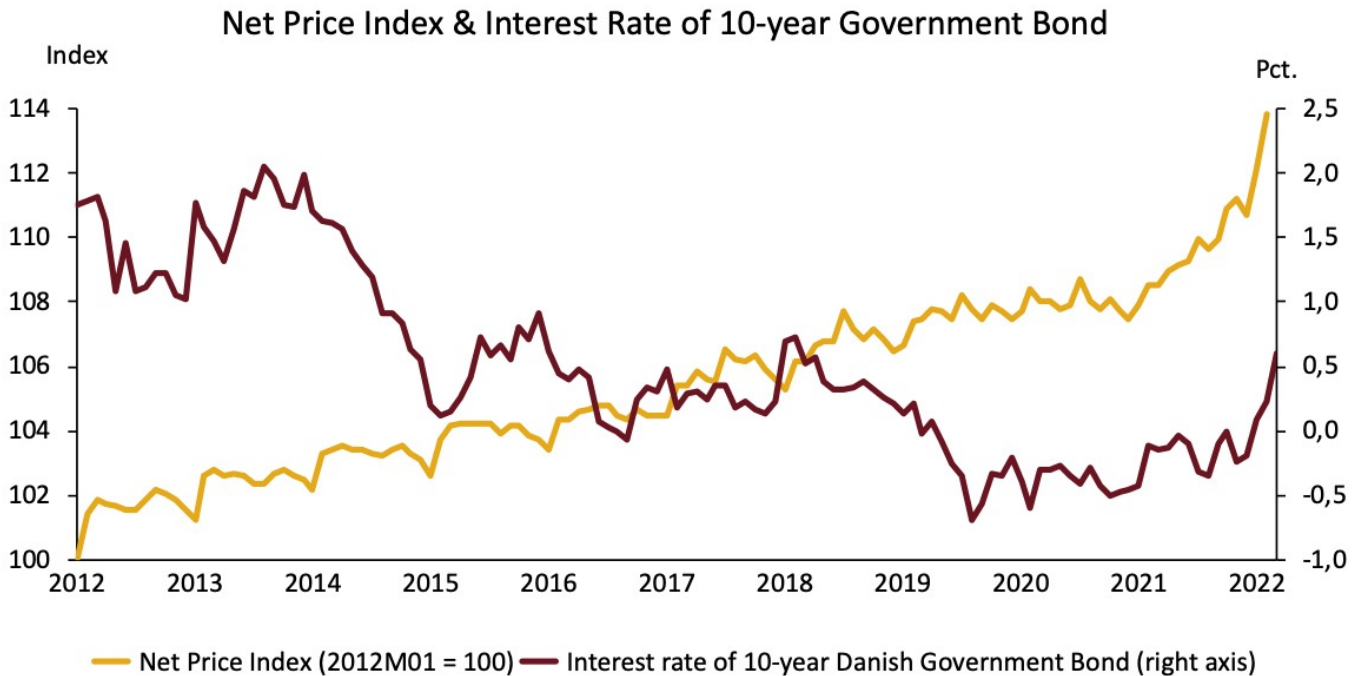
There is no data for the transaction volume of event centers as the market is very small. However, if you find it appropriate, you can consider another category as a proxy for event spaces. The "other" category primarily includes logistics and warehouses. Analyze how increasing demand for real estate investments may affect Bredgade 40-42.

II. Increased inflation and interest rates

While the annual increase in the Net Price Index (Danish: nettoprisindekset) for 2021 was modest with 1.5 %, there has appeared significant increases in inflation at the beginning of 2022. The annual increase in the Net Price Index in Denmark from January of 2021 to January of 2022 was almost 4 %. Rising inflation is likely followed by higher interest rates as a reaction by central banks to control inflation. Since the beginning of 2022, the interest rate of a 10-year Danish government bond has risen almost 0.6 %-points.

The rent in Jeudan’s longer leases such as office leases are annually regulated with the net price index. In contrast, Jeudan would negotiate new leases for each new renter of the event center.

Figure 2.2: The Net Price Index and the interest rate of the 10-year Danish government bond



Analyze how changes in inflation and interest rates are a source of risk for Bredgade 40-42. You might consider the forecast below for evaluating the risks related to these factors. Here “L” is a low forecast, “M” a middle forecast, and “H” a high forecast of increases in the Net Price Index and the interest rate of a 10-year Danish government bond.

Table 2.3: Forecast of Macroeconomic Indicators

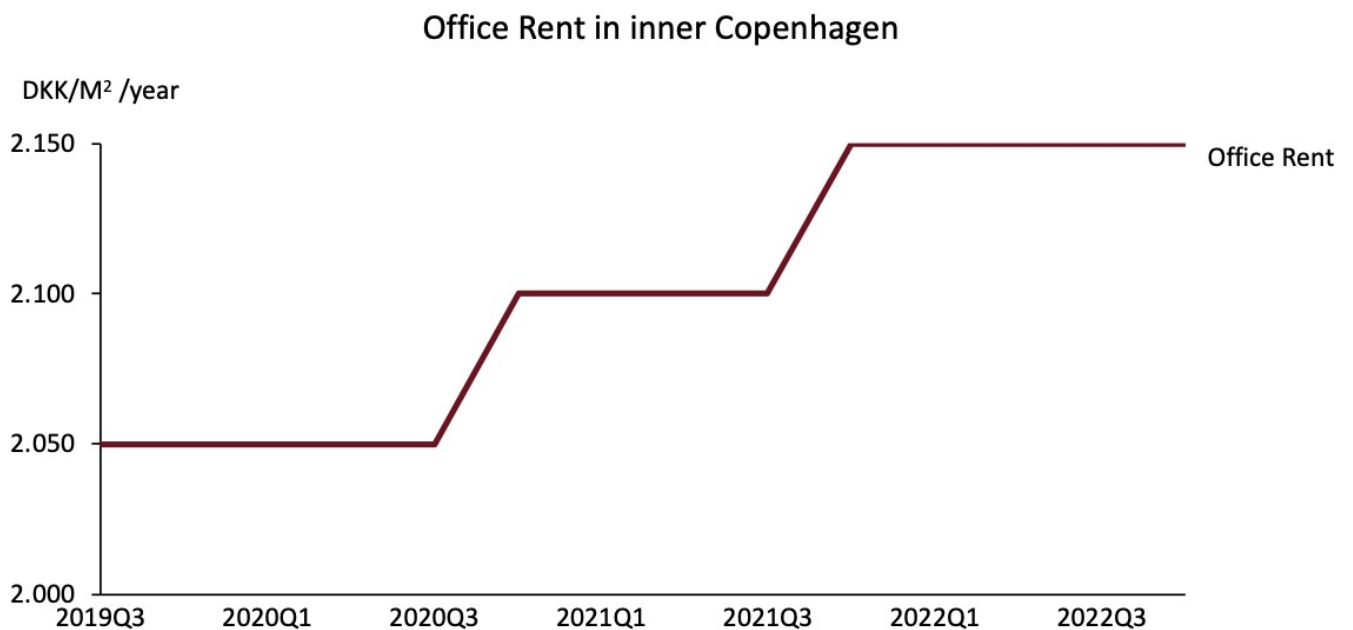
Macroeconomic indicators, pct.	2021	2022			2023		
		L	M	H	L	M	H
The annual increase in the Net Price Index	1.50	2.00	2.50	3.00	1.75	2.50	3.25
The interest rate of a 10-year Danish government bond	-0.10	0.50	0.75	1.00	0.75	1.25	1.75

III. Cultural Changes connected to Covid-19

During Covid-19, working from home has increased immensely. This has spurred a cultural shift in which there is increased importance on offering an attractive work environment in the office space, with larger offices and improved quality of the facilities to encourage employees to work on-site rather than from home. Meanwhile, large gatherings, and by extension cultural events, have been mostly banned in Denmark since March of 2020. However, all public restrictions have been removed as of the 1st of February 2022.

Analyze how cultural changes could impact the demand for office and event spaces. You can include the rent level for offices below and the vacancy rates from figure 1.3 in your assessment.

Figure 2.4: Rent Levels in Copenhagen. Source: Colliers PULS 2021Q4 and 2020Q4



How do you assess the possibility and impact of the three risks on the value of Bredgade 40-42 both with the building being rented out as offices and as an event center?

3 The Strategy and Conclusion

An important aspect of Jeudan's business choices is to consider them in the context of their overall strategy. Jeudan's strategy is to contribute to the development of Copenhagen and its recreational spaces while preserving the cultural history and heritage of Copenhagen's buildings. Specifically, this means Jeudan wishes to preserve historical buildings in a sustainable manner with minimal resource consumption. Jeudan believes this will secure the long-term success of both themselves and Copenhagen.

In the choice between the business models, Jeudan wants you to consider:

- The annual electricity consumption.
- The annual water consumption.

11 SUSTAINABLE CITIES AND COMMUNITIES



From other offices, Jeudan knows the annual electricity consumption of renting the building out as offices will likely be in the range of 25-30 kWh/m²/year. For the water consumption, Jeudan knows the range is around 30-35-liter water per employee per working day.

For the cultural event center, the electricity consumption of the building for a two-hour event is between 500-1,000 kWh. Here, a theater play is at the lower end of the range and a concert at the higher end. For more quiet art exhibitions, the building has a consumption of electricity of ca. 75 kWh/hour, but naturally such exhibits last longer. While it is unclear how much water the culture center would use, the building has room for 1,000 people for shows and 300-400 for art exhibits.

Estimate the annual consumption of electricity and water of the offices and the event center. The estimation will naturally be connected to large uncertainty but specify reasonable assumptions to make a plausible estimation.

What is your estimation of the electricity and water consumption of the offices and the event center? How do the offices and the event center fit into Jeudan's strategy? Give your recommendation on the optimal business model for the building.



Summary of Questions

Question 1: The Valuation

A natural first step in making the choice between offices and a cultural event center is to give a valuation of the building for both cases. To achieve this, you must calculate the expected net operating income and divide it by the appropriate required rate of return.

What do you estimate the value of Bredgade 40-42 is if the building is rented out as offices? What is the value of the building if it is rented out as a cultural event center?

Question 2: The Risks

Any business decision involves taking on risk, and different risk factors may have an asymmetric impact depending on your choice of business model. Jeudan wants you to examine the risks related to increased market demand for investment into Copenhagen real estate, increased inflation and interest rates, and cultural changes connected to COVID-19.

How do you assess the possibility and impact of the three risks on the value of Bredgade 40-42 both with the building being rented out as offices and as an event center?

Question 3: The Strategy

Jeudan's strategy is to contribute to the development of Copenhagen and its recreational spaces while preserving the cultural history and heritage of Copenhagen's buildings in a sustainable manner with minimal resource consumption. Jeudan wants you to consider how both business models support their overall vision, taking into account the electricity and water consumption for both offices and an event center.

What is your estimation of the electricity and water consumption of the offices and the event center? How do the offices and the event center fit into Jeudan's strategy? Give your recommendation on the optimal business model for the building.





Formalities

Final Remarks

- Hand-in is Sunday, March 13th, at 18.00 at the latest. Each team must submit a presentation in PDF (16:9 format) on Innoflow. No other formats will be accepted. Your pdf must be named by your team name.
- The presentation must have a maximum of 7 slides where the first is your front page.
- Your slides must be in English and readable on their own. The judges' initial screening of solutions are based on your slides only.
- Based on the slides, nine teams are selected in a semifinal to present their solution to representatives from Jeudan. The semifinal takes place Thursday, March 17th from 16.15-18.00 at Bredgade 30, 1260 København K. The presentation must be in English and lasts approximately 15 minutes. This includes an 8-minute prepared presentation by you and 7 minutes Q&A.
- The nine teams will be contacted Monday, March 14th.
- Three of the semifinalist teams are chosen to present in a final taking place immediately after the semifinals. Prepare well! There will be an audience. The presentation must be in English and lasts approximately 20 minutes. This includes an 8-minute presentation by you and 12 minutes Q&A. The finals take place from 18.00-21.00, which includes time for dinner, drinks, and networking.

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