REFIRE
Real Estate Finance Intelligence Report Europe

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Inside REFIRE

REFIRE is a specialised report focused on providing market intelligence and background analysis to finance professionals in German and continental European real estate investment.

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The areas we focus on are:

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Retail Property Funds
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CMBS/RMBS
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Euro-zone Property Financing

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Property investors showing appetite for bigger risks, lower yields in 2014

Large investors in German real estate are showing an increasing appetite for taking on bigger risks for smaller yield, according to Ernst & Young's annual real estate barometer. The researchers also expect to see a rise in cross-border transactions this year, with deal volume as a whole expected to rise. The results were presented at a recent press briefing in Frankfurt.

Ernst & Young (or **EY**, as the group is now called) carried out a series of comprehensive surveys, among which was a survey of investor intentions in relation to 15 European countries, in which 500 responses were analysed.

While in Central and Eastern Europe investors are focused mainly on residential properties, in Western and Southern Europe the pendulum is swinging back in favour of investment in office properties, with investors showing a willingness to look beyond 'core' properties, in contrast to earlier years.

99% of respondents described Germany as an "attractive" investment destination, while 72% of respondents expect the overall transaction volume in 2014 to rise from €44bn last year to about €47bn this year. Last year's figure was itself an increase of 23% on the previous year. 65% of respondents said they expect a further renaissance in the previously moribund CMBS market, which sprang back into life for a number of German deals last year.

While the position of Germany as a 'safe haven' was the main attraction in previous years, investors now rate the attractive financing environment as Germany's most persuasive draw. According to Ernst & Young real estate partner **Christian Schulz-Wulkow**, whom we've often quoted in these pages, . "Banks are willing to finance beyond core, even looking at speculative project developments, which were a total no-go in recent years... Equity requirements are still higher than in the boom years, posing a good market corrective. Expectations

LEG Immobilien goes on acquisition trail, Goldman's Whitehall Funds exit

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continue to be good for real estate, with stable to rising rents and prices in the cities – a trend that could only be changed by strongly rising interest rates, which we view as very unlikely in the immediate future."

Top of investors' preferences are still residential and office properties in A1 locations. In residential, Berlin still offers the best prospects, ahead of Cologne and Munich, while in the office sector Munich, Hamburg and Frankfurt all vie for the top position. However, although indications are that many investors feel the residential market is topping out, almost none expect price falls – rather, prices are expected to stabilise.

"Germany is evidently still strongly in the focus of investors, but there are indications that some big investors are taking the benign climate in Germany as an opportunity to exit the market and look elsewhere"

Investors are also perceiving secondary cities such as Bremen, Leipzig and Mönchengladbach as offering the same risks as cities such as Frankfurt, but with yields of more than 7-8% rather than the 5-6% typical of Frankfurt. There are also notably more transactions in some of the industrially weaker areas of eastern Germany, where yields are also attractive.

As a testimony to the desirability of German property generally, 81% of respondents said they see the proportion of non-core acquisitions rising firmly. "In contrast to past years, more risky investments are not seen per se as negative. The willingness to take on more risk seems particularly prevalent in the residential sector, where we've seen large transactions in B- and C-locations, a trend we expect to see continuing", said Schulz-Wulkow.

In the commercial and industrial sector, the majority of recent deals have largely been within the 'core' segment, and for activity to spill out beyond this, the gap in price expectations between buyer and seller still has to narrow a lot to significantly boost transaction volumes, according to 91% of respondents. There are increasing signs, however, that risk acceptance is rising in this segment too, despite ongoing high vacancy rates and frequently short remaining lease periods, while 58% of respondents said they expect to shortly see the re-emergence of speculative commercial property project developments.

Respondents also expected (71%) that this year will see more portfolio deals, while 65% expect heightened activity in the CMBS sector. With residual Eurozone fears still lurking, Germany's attractions for office investment still give cause for 53% of respondents to expect top German office prices to rise in the coming year, as against only 35% last year.

The survey also showed that for the logistics sector, price are expected to rise by 46% of respondents (25% last year). while most investors believe in stable prices for prime retail (65%) and hotels (62%). Those likely to be the most active sellers this year are opportunistic, private equity and open-ended funds, while the most active buyers will be private investors, family offices, insurance companies and pension funds.

Underpinning the relative German property boom is the low level of interest rates, which has continued to help push up residential prices. Buyers are making the simple calculation that what they're saving in interest payments they're paying in the form of higher prices. It looks increasingly likely, though, that these interest rates have irreversibly come off their lows. According to the Bundesbank, if borrowers were paying 2.6% last June for a loan fixed for between five and ten years, that rate would now be 2.9%, and rising. A recent study by consultants Feri warns that it expects rates to rise again from this summer, with the same loan

more likely to cost 4%.

The low interest rate climate is undoubtedly encouraging Germany's banks to hold on to their distressed and sub-perfoming loans longer on their own balance sheets, with survey respondents seeing joint restructuring efforts (91%) and prolongations (85%) as likely to be to the fore, rather than enforcements or the sell-off of loans at deep discounts.

Germany is evidently still strongly in the focus of investors, but there are indications that some big investors are taking the benign climate in Germany as an opportunity to exit the market and look elsewhere. The Ernst & Young study also points to investors' wandering eyes. This year 49% of the survey respondents consider Spain a "very attractive" real estate market, compared to 32% who gave Germany the same rating.

According to Schulz-Wulkow, "Germany is no longer so conspicuous – the investment climate has generally improved across Europe. In the eurozone crisis countries of Spain and Italy prospects have noticeably improved." While for many investors the safety of their capital will continue to keep Germany attractive, private equity investors looking for much higher yields may be finding it increasingly hard to pinpoint opportunities here, and are rooting around in Spain, Ireland, and other markets.

Still bullish on the prospects for German real estate (not surprisingly) is **Ulrich Höller**, CEO of listed **DIC Asset AG.** Speaking at a company event in Frankfurt earlier this month, Höller predicted a further two good years for the industry in Germany, with the recent obsession with top-quality 'core' commercial properties giving way to more traditional investment into more 'normal' assets, such as those that listed companies **Alstria Office REIT**, **IVG** and DIC Asset itself deal in.

Höller suggested that the recent problems experienced by IVG Immobilien's involvement with *The Squaire* at Frankfurt Airport had affected investor perceptions of DIC Asset's huge *MainTor* development in downtown Frankfurt, which will see the central business district in the city now extend all the way down to the banks of the river Main. Despite this scepticism, investor appetite for new, pre-let top-quality office properties is nonetheless still so strong that "the recent sale of one of the MainTor buildings for €155m went almost unremarked, so many other large deals were taking place at the same time", commented Höller wryly.

Höller believes the winners this year will be those listed companies (Alstria, **Prime Office**, DIC Asset, among others) that are holding maybe less prestigious, but commercial assets capable of generating generous payouts, through specialised management and a strong cash-flow profile. He sees a shift underway from the residential sector back to the commercial sector, "as they have always done in the past". In particular he sees an imminent narrowing of the gap between the market capitalisations and the NAVs of the listed companies, citing in the case of DIC Asset, a market cap of under €500m and a net asset value of €850m.

EDITORIAL

There may be life in that old residential market yet

There's a fair measure of truth in that old chestnut beloved of smart money men, that when everyone's thinking the same, then nobody's thinking. Right now it seems as if almost everyone is thinking that the German residential circus has played out, it's time to take profits, the caravans are moving on. Institutional money is switching tack, back into the commercial segment, and its beloved office properties.

Hardened investors smirk when they see Germany's mass-market newspaper Bild-Zeitung explaining to its readers on the front page – as it did in November - how they can clamber aboard the housing bandwagon with NO MONEY DOWN! The power of low interest rates will do it for them, advise the paper's crack team of financial advisors. Cue the sound of experienced hands rushing for the exit, reminded of Baron Rothschild's advice that when your shoe-shine boy starts giving you stock tips, the game is up.

Not so fast, say the researchers at property analyst BulwienGesa. Board member Andreas Schulten points out in the market researcher's latest study how the actual level of new residential building is still trailing the level of building permits issued – and by a long measure, at least in the 20 to 30 most dynamic urban areas in Germany. Schulten sees rents rising a further 5% this year – about the same as the last two years – while purchase prices should rise by 6%, his team believes. This represents a slight slowing down, to be sure, compared to the nearly 8% price rises of the last two years. But such returns are not to be sniffed at.

There is still too little housing being built and refurbished in the right places in Germany, as the flight from the countryside and the provinces into the cities gathers pace. Potential investors are digesting the implications of the pending 'rental brake' or *Mietpreisbremse*, and a number will be encouraged to invest in a different asset class. But for those committed to property, the prospect of two to three more years of minimal interest rates will keep them from wandering too far from the industry they know.

Add to that potent mix a wave of immigrants entering the housing market at the lower end – again, in the bigger cities - and housing analysts like BulwienGesa and the DIW Deutsches Institut für Wirtschaftsforschung are understandably loth, then, to sound the death knell on the residential sector just yet.

And what of the German market for commercial investment? More than €30bn in capital flooded into German commercial property last year, half of it into offices. Brokers and other advisers point to the cheery prospect of a wave of sovereign fund and Asian money flowing in to a market where domestic investors might fear to tread. Many had reason to be grateful to Korean and other Asian investors in helping them to make their numbers last year.

Indeed, what's not to like about the recent tie-up between 'Old Europe Hand' Europa Capital and Beijing-based Ilex Partners, which is helping China's leading institutional investors to find their feet in Europe's (and increasingly Germany's) real estate markets. Chinese insurance companies have only recently been unshackled from cumbersome legislation previously preventing them from investing in overseas property, and thery're raring to go. Such a partnership is a two-way street, of course, and provides reciprocal arrangements for Europa Capital in booming Asia – but as a business model it looks to us like a harbinger of things to come.

Take Union Investment, Germany's most active real estate investment manager. Last year its real estate funds under management surged 12% to €24bn, nearly all of it invested in mutual funds for private savers. As Dr. Frank Billand, the chief investment officer for the group, confirmed recently, the US is looming increasingly large on his group's investment plans, as there simply aren't enough assets in Germany that meet his stringent criteria. A further $2bn has been earmarked for the US over the next three years, as much again as it holds there now after fully 30 years of investing in the American market.

Union Investment, as a blue-chip investor burdened with a mandate to protect investors' money at all costs, is obviously limited in the type of core property it can invest in, home or abroad. Overly-adventurous opportunistic investing would rapidly incur the wrath of its investors, who didn't sign up for any buccaneering strategies with their precious pension pots.

Likewise at fellow co-operative investor Deka Immobilien, the second largest German investor and the largest domestic player, the mood of caution pervading the top management corridors is real. It will invest a net €2.3bn this year, but group CFO Matthias Danne sees the company facing peak prices and flat rents in its major markets, with little prospect of significant rent rises ahead, despite climbing capital values. Many current prices are purely driven by low interest rate levels, he believes, rather than fundamentals.

Looking for richer pickings, opportunists such as private equity investor Blackstone, whose investing nose has served it well in Germany, has been a net seller of German residential and a net buyer of commercial property since 2012 – and it isn't queueing up to invest in Frankfurt office at 4%. It needs more, or it'll look elsewhere. Blackstone and a raft of other investors are targeting assets that were bought at the height of the boom, and where their lenders or their cash-strapped owners are now running out of road. These include the seven stricken open-ended funds, whose offerings are withering in value each day they remain unsold, on their way to a sell-by date of 2017. For the opportunistic buyer, this is a specialist business, indeed.

When Union Investment and Deka, who have no effective limitations on the amount of money they can raise from their distribution networks, are exercising such caution in Germany, others need to double-check and then stress-test their own value-added assumptions. New entrants notwithstanding, the Chinese didn't get to where they are today by leaving lots of money on the table for the foreigner.

Charles Kingston, Editor

Germany/Listed Companies

LEG Immobilien goes on acquisition trail, Goldman's Whitehall Funds exit

The **Whitehall Funds** of **Goldman Sachs** took the opportunity earlier this month to dispose of practically its entire holding of 15.2m shares or nearly 29% in **LEG Immobilien AG**, Germany's fourth-largest property company by market value.

The accelerated book build was 1.5 times oversubscribed, suggesting there was strong demand for the stock. The sale raised €646m for Goldman. In October last year Goldman sold a further 7m LEG shares at a price of €41.25, raising 290m.

Goldman sold all but 0.5% of its holding in the listed, Düsseldorf-based LEG at a price of €42.50 per share through its **Saturea BV** fund. After a minor dip, the stock has recovered to over €44.00, suggesting that the market essentially approved of the sale, glad that there is no further big overhang of shares held by private-equity investors in such a sizeable company. Analysts have long being eyeing such private equity holdings in competitors **Deutsche Annington** and **Gagfah AG** with a certain caution, fearful of a major block being dumped on the market at an inopportune time. Private equity groups **Terra Firma** and **Fortress** are still prominent shareholders in these two listed companies.

LEG owns and manages about 95,000 apartments in North Rhine-Westphalia, Germany's most popular state, with about 260,000 tenants. It generated rental income last year of more than €500m. Average rental growth has been 2.3% since 2008, with LEG's average price at €4.94 per sqm/month, below the regional average in North Rhine-Westphalia of €6.44.

LEG was floated last year by owner Goldman Sachs and minority partner **Perry Capital** in an IPO which raised €1.3bn. Goldman and Perry had bought LEG in 2008 for about €3.5bn including assuming the housing company's debt.

One analyst commented that the sale will have been widely noted by LEG competitors, looking for their own exit. The success of the Goldman disposal right now "bodes well for the giant overhang that Deutsche Annington is facing, roughly five times as big as the stake that Whitehall just sold", a reference to the manner in which Annington only just managed to get its IPO away last year after an initial stumble.

That left owner Terra Firma with a larger stake in its subsidiary than it had anticipated before the hiccup. Terra Firma's own lockout period prohibiting it from selling stock after last July's IPO has also now expired, so the market will be expecting further sales by the private

equity group fairly soon, so long as the listed housing sector is still enjoying investors' favour.

LEG has been on the acquisition trail, recently signing for 537 new apartments and negotiating on a further 2,000 units throughout North Rhine-Westphalia. The apartments bought are generating an initial FFO yield of more than 8%. The company bought 6,700 apartments last year and is targeting 3,300 further units this year.

Speaking at a conference recently, LEG's CEO **Eckhard Schultz** *(pictured, below*) said the company was in direct dialogue with alternative debt providers, particularly large domestic insurers, to explore new forms of financing LEG's planned acquisitions. Many such large insurers, particularly Allianz which has a war-chest of €5bn to invest in European real estate, are looking for ways to increase their exposure to property debt markets.

Financing acquisitions via these insurers could help to lower LEG's current average cost of financing of 3.3%, commentd Schultz. More highly leveraged acquisitions of 60-65% could also help LEG boost its LTV ratio to about 55% from its current 49%, he said.

Meanwhile, fellow listed residential investor Deutsche Annington, Germany's largest private landlord, says it has 4bn available for acquisitions, and says it plans to leave no available portfolio unexamined in its quest for growth. This may be just a demonstration of intent by new boss **Rolf Buch**, recently arrived in the top job from media concern **Bertelsmann**, designed to put down a marker for rivals from the industry heavyweight – and tempered somewhat by his more risk-averse statement that, "We won't risk our rating with just any acquisition." Annington was rated "BBB" by **Standard & Poor's** at the time of the IPO last year.

Buch says his priorities as Annington's CEO are paying a first dividend (a possible €0.70 has been mentioned) to new shareholders, growth for the company, and satisfied tenants.

Germany/Legislation

Further rises in German property transfer tax ahead

Investors in German real estate in the northern federal states of Berlin, Schleswig-Holstein, Bremen and Lower Saxony will have to brace themselves for a further increase in the *Grunderwerbsteuer*, or property transfer tax, a sort of stamp duty imposed on property purchases.

Heading the upward surge is Schleswig-Holstein which has raised its rate to 6.5%. Berlin has raised its rate to 6% after a raise to 5% as recently as April last year. Lower Saxony is raising its rate from 4.5% to 5%, while even the state of Hesse, which hiked its rate last year from 3.5% to 5%, is set to vault up to 6% in 2015.

The issue of the property transfer tax has become a hot potato in German state politics. Until the federal reforms of 2006 the rate was a uniform 3.5% nationwide, (and a mere 2% until 1996) since when the setting of the rate was decentralised and left up to the discretion of the sixteen state parliaments. With such a lucrative source of taxation in their gift, politicians have been unable to resist what is now becoming an upwards spiral to raise as much from this source as possible. Only Bavaria and Saxony in the east have maintained their rate at 3.5%, although Green politicians in Dresden in Saxony have been pushing – so far unsuccessfully – for a increase in the rate.

The €7.4bn raised in property transfer tax in 2012 made up fully half of all the pure *Länder* taxes raised that year, up from €5.3bn two years before. Along with federal subsidies, the nation's municipalities benefited to the tune of €10.3bn in 2012 from the property tax alone.

An anomaly in Germany's *Länderfinanzausgleich*, the system of financial equalisation between the Federal Government in Berlin and the Länder, seems in a perverse way to be actually encouraging the Länder to raise their rates. Lowering the rates would require the Länder to top up their own deficits, while the extra revenue raised from higher rates remains in the kitty without negatively affecting the state's obligations to pay back in to the community pot. Those states not raising their rates have their tax take assessed as if the rate were higher – with the net effect being that states are tempted to join the upward race.

Jens-Ulrich Kiessling, the president of the German Property Association **IVD (Immobilienverband Deutschland**) has been a vocal critic of the existing system, saying it is socially and economically unacceptable and highly detrimental to the official German goal of raising the home ownership rate across the nation. "Instead of competing to offer lower tax rates, we've got a race to see who can raise them higher, faster." The IVD is seeking to have the rate-setting returned to the federal government or at least to have a cap imposed on the Länder by federal decree. Investors would be scared away, and the higher taxes raise the cost of housing, which in turn feed through to higher rents.

Germany has also long been battling with notions of how to reform another basic tax – that of the plain vanilla property tax. This tax, levied on 35m properties in Germany and which every property owner is obliged to pay, is assessed and charged in a myriad of different ways, depending on factors such as location, size of property, current valuation, type

of use, or other criteria. Revenues from the tax flow to the municipalities and the Länder, rather than the federal government, hence the ongoing inability to find common ground for a more uniform taxation policy.

For example, properties in the east are assessed using different valuation criteria to those in the west for legacy reasons, leading among other differences to skewed valuations in the larger cities. As landlords typically pass the quarterly tax on to tenants, the higher valuations of properties in the larger cities will translate into higher rents – again hindering the efforts of local politicians to keep a lid on private rent levels. Germany's **Supreme Tax Court** (**Bundesfinanzhof**) has been pushing for urgent reform of the basic property tax, warning that any further delays would be in breach of the country's very constitution. Dealing with the issue is likely to become much more pressing in Berlin over the coming months.

Germany/Legislation

Germany braced for 'Mietpreisbremse' introduction this summer

Now that the political squabbling over the coalition agreement between the SPD and **Angela Merkel**'s CDU/CSU alliance has been settled (for now), the responsible ministers are now tackling the legislation for introducing the *Mietpreisbremse*, or 'rental brake' which puts an effective cap on the maximum permissible level of rent increase. It looks increasingly likely that the new law will be in place by this coming summer.

Federal housing & environment minister **Barbara Hendricks** (SPD) and justice minister **Heiko Maas** (also SPD) have both seemingly made it a priority within their departments to get the legal framework up and running as soon as possible, "hopefully by this summer", Hendricks said to the newspaper *Tagesspiegel am Sonntag*. The sixteen federal states would then have until 2015 to decide which of their localities would be affected by the regulations, which aim to keep rental increases in line with a local rent table, and to limit the amount of charges for energy-saving improvements which can be loaded on to tenants's rents.

Germany's tenants associations have been quick to welcome the politicians' commitment to quickly enact laws which they see as overdue for the protection of tenants' rights, and the provision of sustainably affordable housing. The **Deutsche Mieterbund (German Tenants Association)** commented that "the planned changes are overdue and urgently necessary".

Independent of the imminent 'Mietpreisbremse' for new lease agreements, Germany's individual federal states have also been granted the right in 2013 legislation to prevent existing lease agreements from rising above 15% over a three-year period, in contrast to the normally prevailing 20%. A number of states, including Bavaria, Hamburg and Berlin have already started imposing this law, with North Rhine-Westphalia set to follow suit in 59 identified municipalities across the state which have recognisable housing shortages.

Germany/Commercial

Auction.com makes sudden withdrawal from German market

Fifteen months ago, when **Auction.com** set up shop in Germany, the company heralded its arrival at the **ExpoReal** commercial real estate trade fair in Munich with the biggest splash that had been seen in the industry for many years.

No expense was initially spared to trumpet the success of the company in its home market of the United States, where it is a powerhouse in real estate auctions, and how, given time, Germany would overcome its own traditions and learn to love the auction model for the buying and selling of real estate portfolios as well.

That might yet turn out to be so, in the course of time, despite the chorus of skepticism that greeted the arrival of the Americans with a business model that most Germans have traditionally associated with the final stages of a foreclosure procedure that sees beaten-up, washed out properties being sold for rock-bottom prices.

Whether it does or not, it will happen without Auction.com, who summarily announced their withdrawal from the German market last week, and the immediate closure of their Frankfurt office. The announcement – or, indeed lack of it initially, as apparently staff and business partners had yet to be informed before the news leaked out – came as a surprise nonetheless. The company had only recently moved to bigger offices in Frankfurt's central business district and made a number of significant hires from within the industry.

All told, the company ran four auctions in Germany, with the third and fourth running in December last year. From REFIRE's discussions with Auction.com's top management, the second auction last summer had shown the company making progress in establishing a viable platform, although the results of the third and fourth auctions late last year (for commercial property, and then residential property) have not yet been officially publicised. Now, it looks like, we'll never know.

The company finally issued the following statement last week about its decision to withdraw from the market:

"The senior management team at Auction.com has been analyzing all of the company's business operations, and has identified several businesses that were unprofitable and/or deemed non-core to our overall corporate objectives. As part of this initiative, the company has decided to suspend operations related to Germany, effective immediately", ac-

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cording to **Rick Sharga**, Executive Vice President of Auction.com.

"This has been a difficult decision, as we're proud of what we've accomplished in Germany over the past year. We broke new ground by successfully auctioning commercial property online in one of Europe's most traditional markets, further proving the power of our online platform. Despite these achievements, however, our German business unit has been operating at a loss, and was not expected to achieve profitability requirements in the foreseeable future. In addition, significant time and attention of senior management has been required for the German effort, and we feel that these resources are better applied to business units where growth and profitability potential are higher", he comments.

Germany/Financing

New debt provider Tyndaris closes €64m German mezzanine deal

Alternative commercial real estate lending specialist **Tyndaris Real Estate** said earlier this month that it had closed its third debt investment, a €64m mezzanine loan secured against a portfolio of three German offices. Overall, the company said it has now closed deals worth €90m of debt capital since last summer, secured by €420m of office, retail and residential real estate assets, making it a notable new entrant to the alternative new lending sector.

On its latest deal, two of the office properties are in Frankfurt and the third is in Berlin in an unidentified portfolio valued at €330m. Annual rent on the fully-let portfolio is said to be €29m, with average unexpired lease terms of more than 10 years.

The company, which has only been actively lending and investing since last July, is the real estate arm of UK-based Tyndaris LLP, an advisory business founded by **Raffaele Costa**, a former partner at hedge fund GLG. The real estate division is led by former **Deutsche Bank** executives **Clark Coffee** and **Heath Forusz**, and focuses on originating senior, mezzanine and preferred equity investments backed by performing assets – initially in the UK and Germany.

Describing the business, Forusz said the company had the flexibility to invest across capital structures, asset classes and jurisdictions in Europe. "We provide capital where, for the most part,

the banks cannot due to regulatory and balance sheet constraints. We continue to find attractive debt investments and have maintained a robust pipeline of opportunities despite increased liquidity in the sector. Given the size and diversity of the European market opportunity, we believe this will continue to be the case."

"The Tyndaris Real Estate team has completed three excellent deals that demonstrate their ability to source and execute on opportunities that meet the investment criteria for our capital, all within a short timeframe," said Raffaele Costa, CEO of parent company Tyndaris. "The structural imbalances that exist in the European commercial real estate market, combined with the resilience of real estate as an asset class, make this a particularly attractive opportunity both on an absolute and relative basis in comparison to other alternative investment products."

Last year, as more new entrants started to emerge to address the funding gap in commercial real estate across Europe, along with the return of some traditional lenders – albeit at much reduced levels – Tyndaris Real Estate founder Coffee said, "This increased liquidity is a positive development for the market, but it remains a drop in the bucket compared to pre-crisis lending levels. When I speak with many of my clients who are looking for leverage, they continue to struggle to find credible financing solutions for all but the most prime assets or markets."

While many of the new entrants providing debt liquidity are focused on senior lending, this is having the effect of increasing overall lending volumes, lowering the pricing of senior debt as more competitors enter the field, and more transactions. Coffee said this is where his business comes in: "You need to get the senior debt right in a deal before the rest of the capital structure can make sense. If borrowers have greater access to senior debt at lower pricing, this facilitates greater use of mezzanine and other forms of subordinate capital in their deals."

Coffee cited (at the time) the company's first deal last year as evidence of this. "We recently closed an investment related to an acquisition of good quality Berlin multi-family residential assets. We are earning about a 15% annualised return for 62% to 78% LTV risk, on one of the most stable asset classes anywhere."

Germany/Financing

Top Stuttgart retail property refinanced by Evans Randall

The UK-based investment banking and private equity group **Evans Randall** said this week that it had completed a full refinancing of its senior debt position on one of its major German assets, the *Königsbau Passagen* in Stuttgart.

The property, once the home of the **Stuttgart Stock Exchange**, is probably the most prominent commercial building in Stuttgart, located alongside the historic *Königsbau* building in the very centre of Stuttgart's shopping and business district.

Evans Randall said the refinancing replaces the existing maturing facility from **HSH Nordbank** which was put in place when Evans Randall bought the centre for €220m in 2006. The new loan includes a senior facility from insurer **Allianz** for €145 million at a fixed rate of 3.5% per annum and with no amortisation for the first two years, while **European Real Estate Debt II S.à.r.l**, advised by **DRC Capital** also provided a mezzanine facility of €37.5 million.

Both facilities are for a seven-year term, which Evans Randall said was a core element of its strategy, "being to take advantage of historically low interest rates and pursue longer term value-enhancing asset management initiatives." Allianz already has a loan book of €1.3bn and has made it clear it intends to boost its senior debt exposure over the coming years; late last year it hired **Roland Fuchs** from **Helaba** in France to spearhead its European real estate finance drive.

The centre, (*pictured, below*) which is managed by specialist shopping centre manager ECE, is the largest shopping mall in Stuttgart. It comprises 26,000 sqm of prime retail space in more than 70 shops, 18,000 sqm of prime office space and car parking below the centre with 415 spaces. It features a range of more than 70 upmarket retail, dining and leisure outlets across five floors, and has recently undergone a major revamping including the creation of a new top-quality food lounge on the second floor, which has added about €14m to its capital value, based on new income generated of more than €700,000 per annum.

Evans Randall's CEO **Kent Gardner** commented: "The successful completion of the recent redevelopment works was a key step in our strategy to create additional value through increasing occupier and consumer appeal. Combined with a robust refinancing deal with leading lenders, this has added to the investment appeal of this prime international asset, providing the means to further drive increases in rental income and capital growth. "

Evans Randall invests in large-scale and normally prestigious commercial and retail assets for both itself and investor clients, and holds a range of high profile assets in its portfolio, including 50% of the Gherkin in London, the HBOS headquarters in London, the ING Bank building in the Hague, and the European Commission's new headquarters building in Brussels, among others. It normally targets real estate returns of 20% upwards annually.

Germany/Listed Companies

Gagfah starts disposal programme, plans dividend resumption

It may be just a question of perception, but it certainly feels as if there are fresh winds blowing through listed German residential investor **Gagfah AG** since the arrival last spring of **Thomas Zinnöcker** as CEO from Berlin's **GSW Immobilien AG**. In any event, investors seem to have rediscovered their faith in the Essen-based company after the previous troubled years which were overshadowed by lawsuits, accusations of insider trading, and negative publicity associated with the treatment of tenants under the old – now largely replaced – regime.

Major shareholder, the US private equity group **Fortress**, has also been steadily decreasing its stake in the business, which seems to be coinciding with the group's return to favour. Gagfah owns and manages about 145,000 residential units throughout Germany.

Gagfah recently published its provisional full-year figures for 2013, and clarified its goals for 2014. The group plans to increase its operating results (FFO) by 35% this year and 10% the year after in preparation of a return to a dividend payout of €0.20-€0.25 in early 2015. There will be no dividend payout this year, due mainly to the nearly €200m extra costs incurred in pushing through the company's 4bn refinancing package last year – at a new average financing cost of 3.1% p.a. on loans now mainly due in 2017-2019. (The company reckons the overall saving on the refinancing to be over €40m).The company last paid a dividend in the fourth quarter of 2010.

Zinnöcker commented on the year just past in a statement accompanying the results: "2013 was a very good year for GAGFAH and its stakeholders. We have successfully laid the groundwork for an improved operational performance and for strong FFO growth this year, and we are very confident about our targets for 2014 and beyond." The results show FFO of €0.60 per share, while rental growth was above 1% and the average vacancy rate held at under 4.5%.

Gagfah is now focused on shedding apartment units in non-core geographic areas, such as Saarland and Saxony-Anhalt, where it manages small amounts of apartments but nonetheless needs to maintain a strong administrative presence. All in all 17,000 apartments are scheduled for disposal, including 4,200 in North Rhine-Westfalia, 3,300 in Lower Saxony, and 2,200 in Schleswig-Holstein. These regions, outside Gagfah's core regions of Dresden, Leipzig and the eastern part of the country, have had a vacancy rate of up to 8.5% at average rents of €4.92 per sqm/month, and Gagfah will be looking to sell off the holdings as portfolio deals.

The rest of Gagfah's holdings have an average vacancy rate of 3.5%, and generate rents of €5.26 per sqm. The company plans to pump in €70m this year for upgrade and maintenance, lowering the overall vacancy rate to below 4%, and which should be reflected in an improved NAV.

Germany/Listed Companies

Newly-merged Prime Office starts life with fresh €130m capital

The newly-created **Prime Office AG** is starting out on its new life with a planned €130m capital increase with which to strengthen its capital structure, following final approval by Germany's financial supervisor **BaFin** of any remaining outstanding hurdles. A supplement to its main offering prospective to investors was due to have been submitted by January 28th.

The company, created out of the merger between listed **Prime Office REIT AG** and **OCM Real Estate**, a unit of US private equity firm **Oaktree**, expects to issue 50.2m new shares in a cash-raising exercise offering pre-emptive rights to existing shareholders, reducing the new group's overall leverage to about 58%.

Oaktree funds are expected to participate with at least a €65m investment in the new capital, while a separate investor has also indicated his intention to invest up to €20m. The Oaktree funds will become the largest shareholder in the new entity with around 60% of the equity.

Prime Office REIT's existing shareholders will enter into OCM's share capital at an exchange rate of 1-to-1 for existing shares held.

The new business, operating without Prime Office's previous REIT status, will have gross real estate assets of about 1.9bn, with 920,000 sqm of mainly high-quality offices in Germany's bigger cities, with the goal of growing its assets to 3bn in the medium term.

To boost its equity ratio and lower its debt to comply with the merger agreement, Prime office REIT has been engaged in a selling spree of a number of its previous assets. Its most recent sale, to a foreign investment group and which raised €34m, was an office building in Fellbach near Stuttgart. The property with nearly 20,000 sqm of lettable space, is leased to the State of Baden-Württtemberg's **Office for Salaries and Benefits** until the end of 2020.

According to **Jürgen Overath,** the CEO of OCM German Real Estate Holding and a future board member of Prime Office, "We are delighted that the merger of the two companies is now on the finishing straight and that we can in due course implement our joint plan of creating a leading, listed office property platform with a conservative financing structure."

AlexandervonCramm, CEO of Prime Office REIT (*pictured, above*) added, "With the planned capital increase, we will lay the foundation for attractive cash flows as well as a sustainable growth strategy that should translate into dividends of about 40 to 45% of our funds from operations for our shareholders."

Germany/Acquisitions

Morgan Stanley/Redos in major eastern German retail acquisition

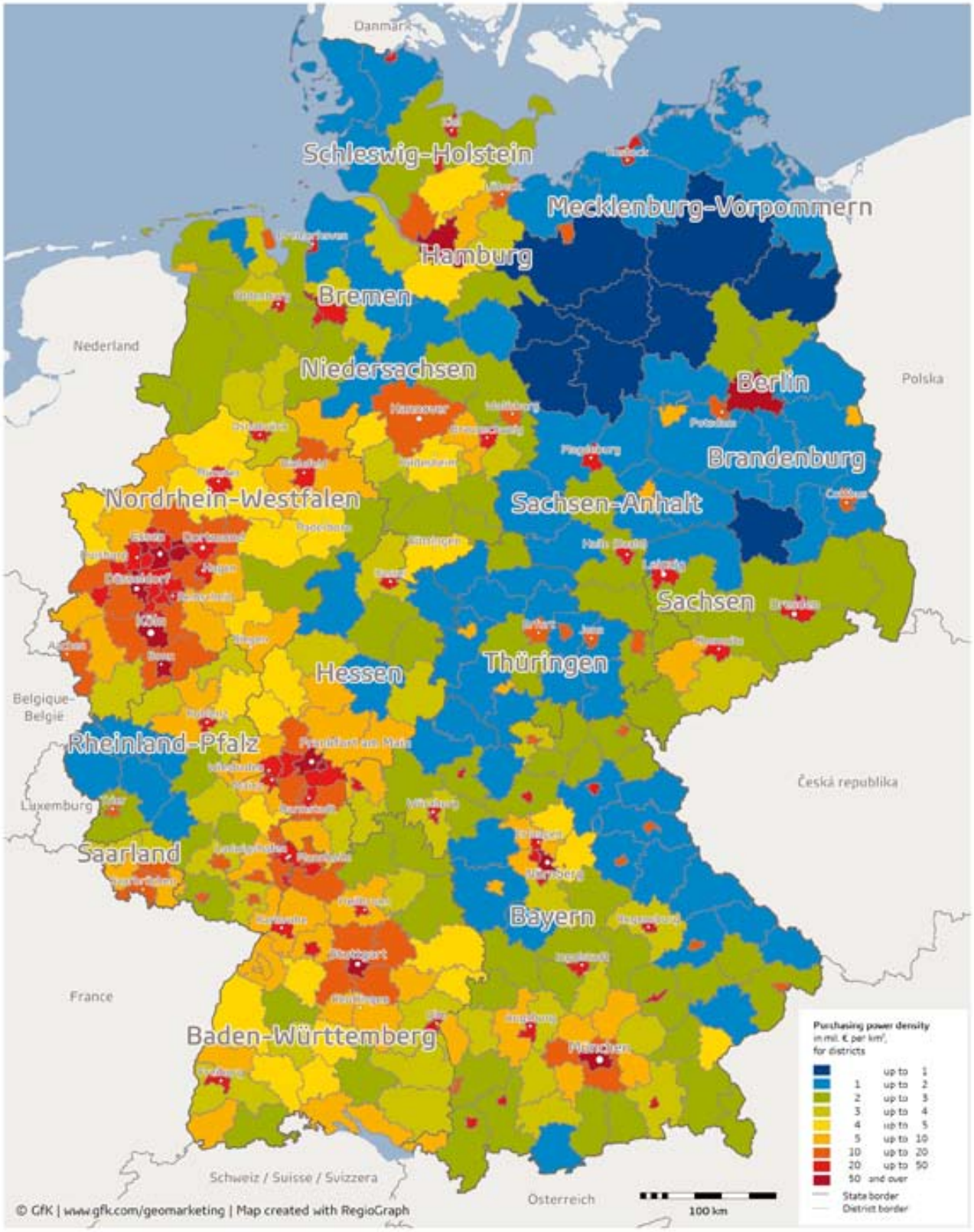
In a significant German retail transaction, a consortium led by a fund from **Morgan Stanley Real Estate Investing (MSREI)** and Hamburg-based asset manager **Redos Real Estate** has acquired four shopping centres in eastern Germany and Berlin from **M&G**, the real estate manager of UK insurer **Prudential**. This is the fourth German retail deal the two partners have done together .

The centres changing owner are *Eiche Shopping Park (Kaufpark Eiche)* and *Havel-Park* in Dallgow near Berlin, *Dresden Shopping Park (Kaufpark Dresden)* and the *Wust* mall in Brandenburg just west of Berlin. All are anchored by the general store chain **Kaufland**, and together make up the so-called Christie portfolio put together between 1993 and 1995 by **Lidl & Schwarz**, the parent company of discount grocery chain **Lidl** and Kaufland.

The properties, which are managed by shopping centre manager **Mfi**, are almost fully occupied, but given their advanced age are now in need of modernisation – particularly the centres in Dallgow, Dresden and Eiche. Specialist Münster-based developer **HLG** has been hired to pump in 'high double-digit millions' to renovate the centres over the next three years. They will then be primed for re-sale, say the new buyers.

The deal represents one of the largest seen in the eastern part of Germany. MSREI, which acquired the 214,000 sqm. gross lettable area portfolio in a share deal, will place it initially in its **Real Estate Fund VII**. Although the purchase price was not named, analysts estimate the buyers paid between 14 and 16 times annual rent, or around €400m. Notably, the Kaufland stores are among the largest Kaufland properties in all of Germany. The portfolio was financed by Hamburg-

GfK purchasing power density 2014



...see page 13

based Landesbank **HSH**.

MSREI executive director **Patrick Lindemann** commented that the portfolio met with the firm's strategy of finding assets needing repositioning but with good cash-flow, while Redos CEO **Oliver Herrmann** added that the portfolio offered attractive upward capital value potential.

Germany/Residential

Researchers see rate of residential price increases slowing in 2014

As we report else where in this issue, most of our research brethren in Germany are expecting a slower rate of increase in the prices for residential real estate throughout 2014. **DB Research** expects new apartments to rise by 5% nationwide, although up to 7.5% in the larger cities – after increases of up to 7% last year. Last year twelve German cities recorded price increases of more than 10%, up from seven cities the year before, one in 2011 and none at all in 2010 and 2009.

The DB researchers said that average residential rents increased by 3% last year, which puts their figure well ahead of the figure of 1.2% estimated by **Destatis**, the federal statistics office (the figure for 2012 was +4.8% on new leases).

The highest rental increases in 2013 were in Berlin, up 2.5% on the year, according to Destatis. However, apart from the larger cities and university towns, rents nationwide remained static. The eastern states of Mecklenburg-Vorpommern (+0.3%), and Brandeburg and Saxony-Anhalt (+0.9%) are cited as examples. The overall rate of rental increase between 2005 and 2013 for 'cold' rents i.e. without utility charges was 9.8%, while the consumer price index rose by 14.3% over the period.

Meanwhile Destatis also released figures from November showing that the price-adjusted value of new orders in the construction industry increased by 12.3% over the same period in 2012. Construction industry revenues at €10.1bn in November were 4.8% above the figure for November 2012. Between January and November, overall revenues rose by 1.9% to €87.0bn, says Destatis, although the figure is below the full-year estimates issued by industry associations HDB and ZDB. They see full-year revenues up 2.5% in 2013 to €95.3bn, and expect growth of 3.5% for 2014.

Germany/Acquisitions

Swedish groups Akelius, Cityhold make fresh German investments

News from Swedish investors in Germany highlight how the Nordic country's leading investors are expanding their footprint across both the residential and the commercial sectors. Residential investor **Akelius** invested over €270m last year in residential real estate – mainly in Berlin at over €130m – and sees that level topping a further €300m this year.

Akelius says it is increasingly focused on portfolios with a volume of €50m upwards, while this year it's extending its reach into secondary cities beyond its usual beat. Last year the group bought apartments in Berlin and Hamburg (€55m), as well as in Munich, Cologne, Düsseldorf, Frankfurt, Mainz and Wiesbaden. Akelisus has now bought over 16,000 residential units since 2006.

Meanwhile **Cityhold Property,** a wholly-owned subsidiary of Sweden's **AP Funds I and II**, has dipped its toe into the German market for the first time with the purchase of a centrally-located freehold office building in Munich with15,000 sqm of lettable space. The seller was a Spezialfonds of **IVG Institutional Funds**. The property in the Nymphenburger Strasse was built in 2003, and is multi-let to a mix of blue-chip tenants, with average unexpired leases of seven years. The annual yield is 5%, which is the whole fund's overall average target return.

Cityhold was established in 2011 with the specific mandate of investing in core European office buildings worth about €50m and above, to add diversification to its parent's real estate allocation, now worth €48bn in total. The UK was the group's first priority, and having invested half its current allocation of €1.2bn in three London properties in 2012, Cityhold said it is now looking to diversify geographically by using the other €600m to buy buildings in Munich, Hamburg and Paris.

According to **Per Sjoberg**, Cityhold Property's CEO, Germany is now looking very attractive to his group, notably because of its stability and lower levels of debt. "Munich – and Germany as a whole – is a very stable and low-risk real estate investment because of the low volatility, which fits in perfectly with our investment criteria… Moreover, finance costs in Germany are much lower than elsewhere – for example, the UK."

As to its future investment pipeline, Sjoberg said there was no rigidly-fixed timetable for Cityhold's acquisition programme because they were looking for the right opportunities and strategies. "We are looking primarily for offices in markets that are transparent and liquid, with modern buildings in good locations with good transportation links," he said. "And we are looking for high-calibre tenants."

Germany/Financing

PIMCO, ING named as potential buyers of WestImmo

Westdeutsche Immobilienbank (WestiImmo), the previous real estate lending division of the mothballed **WestLB** is said to be in talks with at least two possible buyers to sell its lending business out of the clutches of the German state, which absorbed the bank as part of the dissolution of landesbank WestLB two years ago.

WestLB was compelled by the European Commission to divest itself of its lending subsidiary under the terms of its original €5.4bn state bailout package at the height of the financial crisis.

According to the usually well-informed **James Wallace** over at **CoStar Finance**, among those evaluating a bid are **PIMCO**, itself part of German insurer **Allianz**, and **ING Real Estate Finance**. Westimmo had been the object of a protracted bidding process in 2014 with prices then being quoted of about €400m, in which **Apollo Global Management** ultimately withdrew after WestLB complained of "severe market deterioration" leading to unacceptable price offers.

There were also unclarified liability risks at the time for WestLB and its shareholders which led to them scuppering the sale, which was all taking place against the background of the sovereign debt crisis and fears about the break-up of the Eurozone.

A further potential suitor, Wiesbaden-based **Aareal Bank**, has now withdrawn from the bidding after it itself bought **Corealcredit Bank** from US private equity investor **Lone Star** just before Christmas.

WestImmo, which was spun into WestLB's bad bank **Erste Abwicklungsanstalt (EAA)**, is only interested in selling itself as a whole business, much as **Commerzbank** is and has been selling its UK and Spanish loan portfolios. Likely buyers, therefore, will have to be those with access to affordable long-term money markets, such as the big banks and insurers, rather than private equity funds which are more tuned in to the shorter-term sources of funding.

EEA absorbed WestImmo's then €15.9bn property loan book in September 2012, and after a succession of loan sales, maturities and enforcements, had €11.9bn on its books a year later. Under its restricted trading conditions, WestImmo may still renew loans with existing customers and make further minimal top-ups in line with its restructuring plans. It posted revenue of €72m in the year to June 2013, for a pre-tax return on equity of 4.5%.

Guest Column:
Dr. Thomas Herr, Managing Director of VALTEQ

Six technical risks you should take into account in German commercial real estate

www.valteq.de

In November 2013, we were guests at Charles Kingston's London REFIRE Conference. There, we had an opportunity to familiarise the public with our experience in technical due diligence and the most common technical problems in German commercial real estate, which we would like to summarise once more.

Fire protection is and remains the main issue. In this regard, matters as diverse as the fire-resistance of existing building elements, the lack of component approvals or installation defects, for example in ventilation systems, are all weighty (price) factors. As an investor, one can – in the truest sense of the word – end up burning a lot of money. A second issue, and one that is constantly growing in importance, is energy-related refurbishment. The Energy Savings Ordinance (EnEV) passed by the German legislature in 2013 comes into effect in April 2014. This will have an impact in a wide variety of areas: whether it is the arrangement of façade insulation, energy-related optimisation in the event of established repair requirements or retroactive insulation of heating and hot water pipes. Increased costs can also be brought about by the insulation of top floor ceilings or the replacement of low-efficiency heating boilers. A third and often underestimated focal point in the technical review of buildings is the subject of water. More stringent statutory regulations force us to look more closely to see whether, e.g. the drainage network on one's own site is watertight, whether fire-fighting water is separated from drinking water or whether lead pipework is still present. As the fourth aspect in technical appraisals, we must remain vigilant with respect to concrete damage, especially in underground car parks, where the remediation costs can run into the millions. The same applies for the replacement of obsolete building management systems dating back to the 80s or 90s of the last millennium. Finally, allowances must be made for the disposal of hazardous building substances, such as asbestos and man-made mineral fibres – an aspect which is easily overlooked, yet intrinsically linked with high cost risks (around 3 to 5 percent of the refurbishment costs).

We have the impression that investors tend to concentrate on the achievable income and opportunities when making their acquisition decisions, preferring to blank out any risks and the forecast repair costs. We are convinced, though, that long-term success is only enjoyed by those who are competent and thorough in their dealings with real estate and who are prepared to portray the risks in their business plans. VALTEQ is happy to be at your side as an experienced partner for technical due diligence and in the practical implementation of your reinstatement strategy.

Germany/Listed Companies

Fast-growing Adler Real Estate tops up with further 1,900 units

Listed German residential investor **Adler Real Estate** moved this month to boost its holding in a company holding three residential real estate portfolios to take over complete ownership, giving it more than 1,900 new housing units. The deal follows on from a further acquisition of a majority stake in December of 2,400 units in Lower Saxony. From almost a standing start a year ago, Adler has now invested nearly €530m to build up a housing stock of 10,000 units.

Adler's latest deal sees it taking over complete control of the three portfolios, from its previous 52.8% stake in the company. The portfolios consist of 1,769 apartment and 137 commercial units with living and usable space of 114,000 sqm, located across the states of Schleswig-Holstein, Mecklenburg-Western Pomerania, Vorpommern, Saxony, Thuringia, North Rhine-Westphalia and Rhineland Palatinate. Most of the apartments are in Rostock, Düsseldorf, Dresden, Leipzig, Kiel, Hagen and Lübeck.

Investors have taken a shine to the small but growing real estate investor, in sympathy with their general enthusiasm for the German residential sector, with the Adler share price more than doubling over the last twelve months.

Europe/Research

Include listed property to magnify portfolio returns, urges EPRA

Defined contribution pension funds that combine private and listed property in investments consistently generate superior returnscompared with portfolios without a blended approach, according to new research sponsored by the **European Public Real Estate Association EPRA**.

In its annual Insight presentation in Amsterdam on 14 January, EPRA executives showed figures that showed that a UK pension fund portfolio that combines a 30% international property shares with non-listed funds delivered an annualised total return of 7.5% p.a., or 0.9pts better than more than a portfolio with no real estate stocks. The data were based on 15 years of performance data compiled by consultants **Consilia Capital** and **The Townsend Group**.

"No matter what period we looked at and irrespective of the property cycle, we found that an allocation to the listed sector enhanced the returns of the real estate portfolios of defined contribution pension funds, Consilia Capital MD **Alex Moss** told the event.

"A compelling body of research shows that by sticking to

traditional non-listed strategy investing institutions miss out on superior returns, as well as the benefits of liquidity and efficient pricing that come from integrating listed property into real estate allocations."

Nicholas Cooper, principal with The Townsend Group, added: "It is well understood that private real estate can be a beneficial component of a multi-asset portfolio, primarily due to the diversification that it provides. Real estate solutions within Defined Contribution schemes often require an enhanced level of liquidity. This study finds a blended portfolio, with a majority of direct real estate exposure through private real estate funds, can provide attractive risk-adjusted performance. The diversification potential is also largely retained, especially when considering typical institutional allocations to the asset class."

The study, which covers June 1998 to June 2013, showed that a 70/30 blended portfolio generated a 13.6% outperformance in returns compared with non-listed funds. **Fraser Hughes**, research director at EPRA commented: "The results of the research are clearly in line with the findings of the **Maastricht University** report on global pension fund performance issued in 2012 – that investors who ignore the listed real estate market seriously risk underperforming those that embrace it. It only goes to bolster our opinion that listed real estate should form a material portion of all investors' allocation to property."

The liquidity that stocks provide, lower transaction costs and ease of diversification by sector, regionally and globally are among the reasons DC pension funds are warming to the listed real estate sector, according to a separate EPRA survey (**Pension Fund Real Estate Investments**) released in September and prepared by Consilia and **Andrew Baum** of **Property Funds Research**.

The UK's **National Employment Savings Trust** indicated last year that it will earmark one-fifth of total investment to **Legal & General's Hybrid Property Fund,** which invests 30% of its assets in a global real estate equities. NEST, established under reforms introducing automatic enrolment to the UK workplace DC pension schemes, expects assets to rise to as much as £150bn by 2030.

Austria/Listed Companies

Austria's CA Immo targeting up to €200m on new German projects

Listed Austrian investor and developer **CA Immo** said that its recent spate of heavy disposals, primarily in Germany, have helped it to improve its equity ratio from 31% in 2012 to 40% at the beginning of 2014. Last year the group sold a quarter of all its real estate assets, currently totalling €5.4bn, at what it said was above book value. However, investments of between €150m and €200m are still planned for German in 2014.

For this year the plan is to re-weight its portfolio equally between Germany and the group's traditional hinterland of eastern Europe, primarily by continuing divestments, developing more of its existing land reserves, and by further reducing financing costs. Proceeds will be used to further pay down debt and to buy out minority partners in eastern European projects.

CEO **Bruno Ettenauer** said in a recent statement, "It is our specialist development expertise that guarantees organic growth, generates regular contributions to earnings and stands as the main driver of valuation increases. We are not reliant on costly acquisitions: instead, we utilise centrally located land reserves and build high quality, high-yielding office properties in high-demand markets."

However, the group is still planning to invest €150-200m in project developments, particularly in Berlin. Other projects include the *Kontorhaus* in Munich, the *Belmundo* in Düsseldorf, the *John F. Kennedy Haus* in Berlin and the *Monnet 4* project near Berlin's main train station.

According to **Florian Nowotny**, the group's finance director, "Having come through some difficult years for financing, we are now seeing excellent credit availability in Germany under attractive conditions – a situation from which we can benefit enormously while drawing

attention to our development activities in the country."

In 2013 CA Immo was primarily in the headlines for its high-profile disposals, selling the "**Leo II**" portfolio in the state of **Hesse** for €800m to a consortium led by Augsburg-based **Patrizia Immobilien**, and 67% of Frankfurt high rise **Tower 185** to two pension funds, including that of **PwC** - which occupies around 60% of the tower's space – for about €330m.

The disposal programme continued through December, with the sale of carmaker **Mercedes-Benz'**s German headquarters in the *Mediaspree* area of Berlin to giant real estate fund manager Union Investment for €88m. The fund manager is transferring the building into one of its major open-ended property funds **Uni-Immo:Deutschland**, and leasing the entire property back to Mercedes Benz on a ten-year lease.

Meanwhile, CA Immo has bought back a financing portfolio from fellow Austrian **Volksbanken AG** with a nominal valuation of €480m. The amount is made up of equal parts of both secured real estate loans in eastern Europe and unsecured financing at the holding company level. The actual price paid was not disclosed. Florian Nowotny merely said the deal would strengthen the structure of its balance sheet and allow the group to rapidly utilise funds from its property sales over the past weeks.

Europe/Research

INREV survey sees shift in risk appetite for European investors

Glancing over **INREV's** notes before its recent presentations in London, Amsterdam and Frankfurt for its global **Investment Intentions Survey**, we noted the headline, "Investors Bullish about Real Estate in 2014". Where, we wondered, had we seen that before? In fact, it occurred to us, don't investors tell INREV every year at this time that they're planning to increase their real estate allocations for the coming year? We think EPRA is told the same thing as well every January by its members. This year, not surprisingly, the INREV respondents are bullish again.

Presenting the latest findings at the Villa Kennedy in Frankfurt earlier this month, INREV's CEO **Dr. Matthias Thomas** and head of research **Casper Hesp** had an optimistic message to deliver, based on the results of INREV's annual Investment Intentions Survey, which INREV has been carrying out since 2007. This time INREV could draw on supplementary research from sister organisations **ANREV** and **PREA** in Asia and America to provide a more global perspective.

What does the survey conclude? This year the 142 participating institutional investors in the survey expect to increase their allocations to real estate from 9.5% to 10.3% of their overall portfolios, or upping their investment to about €35bn. The biggest growth is seen in Asia Pacific, with 53.8% of those surveyed planning to increase their allocations to the region over the next two years.

The report shows European investors also have an optimistic outlook on the market, with 48.9% of respondents saying they expect to increase their allocations. There is more caution amongst North American investors as only 26.9% plan to do the same while the majority (61.5%) do not expect allocations to change. More stable economic conditions and a weak correlation with bond and equity markets mean that real estate remains a popular choice for investors looking to diversify their portfolios. This was borne out in the survey findings, with diversification benefits cited by investors and fund of funds managers as the top reason to invest in real estate, scoring an average importance rating of 4.2 (out of 5), up from 3.9 last year.

For Europe, the survey results suggest that interest in joint ventures and club deals, which remains high, may now have passed its peak. Over a third (36.6%) of respondents expect to increase their allocations to these products, which is more than ten percentage points lower than a year ago.

Debt will be a popular investment target over the next two years. Overall, 25.2% of investors expect to increase their allocations to real estate and mortgage debt, with large investors in particular looking to increase their exposure to debt markets. And fund managers of all sizes continue to launch real estate debt products.

"These results show a stabilisation of confidence amongst investors with increased allocations to real estate, which is good news for the sector," said head of research Casper Hesp. "There are also signs of a potential change in emphasis with investors searching for the optimum way to structure their portfolios to achieve the ideal investment mix."

There was good news for the non-listed real estate sector as the percentage of investors saying they expect to reduce their allocation to non-listed has fallen significantly, from 30.5% in 2013 to 18.5%. With the proportion of investors wishing to increase their allocation to non-listed real estate funds remaining almost unchanged from last year, the result is a higher net balance in favour of non-listed funds - notably from smaller investors - bucking the downward trend of the previous three years.

Germany, France and the UK will remain the top priority markets for 2014. Buoyed by strong support from domestic investors, Germany remains the top European country, with 58.3% of investors and 70.5% of fund managers expecting to invest there this year. However, the UK is the preferred location for cross-border investment.

from page 18

UK offices is the most popular country and sector combination preferred by 45% of investors. Then comes the French offices sector (favoured by 44% of investors), followed by Germany offices (preferred by 43% of investors).

Retail was the most popular sector overall for investors and fund managers, while there was a noticeable increase in interest in residential, suggesting that this sector is proving its viability.

Outside of the core markets, Spain, recognised as the most popular of the 'Club Med' economies, looks set to be on the comeback trail in 2014. According to the Survey, 41.7% of fund of funds managers, 31.3% of fund managers and 22.6% of investors expect to invest there this year.

"The global Investment Intentions Survey reflects a generally positive sentiment across the industry as we enter 2014. And while we see some familiar anticipated behaviours - such as European investors adopting a mostly defensive strategy and their US and Asian counterparts being more opportunistic - in Europe there are also interesting shifts in attitude with a growing appetite for risk. These results suggest an industry in the midst of change," concluded CEO Matthias Thomas (*pictured, above*).

Germany(Open-ended Funds

SEB Investment now pure real estate, looks at starting closed-end funds

SEB Investment, the German investment division of parent Swedish bank **SEB**, said earlier this month that it plans in future to focus solely on real estate, and said it is looking at making its first venture into closed-end funds. The company is one of several German former managers of open-ended property funds that are now in the process of being wound up due to liquidity problems in the fallout from the financial crisis.

Despite being committed to selling off its assets from its ImmoInvest fund, the company said the environment is now actually conducive to generating new institutional business. In particular, demand for core properties has actually played into the company's hands, it says, as it can provide top-quality assets for hungry buyers.

This is a much more preferable situation than 2-3 years ago, when there was little demand, said **Christian Hanke**, the head of institutional real estate clients at SEB Investment. Among other plans, his group was now looking to sell off assets from formerly open-ended funds in "themed packages" – such as 'European core', 'US retail' or 'European logistics' – and other assets to investors, possibly in club deals.

Another area SEB Investment is looking at is the closed-end fund business, which has been restructured in Germany through new KAGB regulations. SEB Investment confirmed that it had specifically included the possibility of entering the segment when applying recently for a KVG license, an obligatory step in the application to German regulator **Bafin** as part of the new regulations, by which the country implemented the Alternative Investment Fund Managers Directive (AIFMD).

Meanwhile, the Berlin-based **Scope** rating agency reported that the amount of new closed-end funds in all asset classes set up in Gemany last year was €1.5bn, only half of the amount raised in the sector in 2012. Across all categories, the hardest hit was renewable energy, while the only class of funds not down on the previous year were leasing funds, particularly aviation.

As in the previous year, real estate funds made up 65% of all closed-end funds. Their biggest difficulty was in finding suitable property assets in which to invest against stiff competition, a situation made more difficult by the introduction of the new KAGB legislation in July, which effectively paralysed the industry through the second half of the year. Scope expects fund emission to pick up again in 2014 as initiators adapt to the new rules of the AIFs (Alternative Investment Fonds), with numerous fund initiators ready to launch new products.

Germany/Study

35% more German residential portfolio deals in 2013

Although figures for residential portfolio transactions in Germany were skewed heavily in the last quarter of 2013 due to the takeover of **GSW Immobilien** by **Deutsche Wohnen AG**, the year proved to be a remarkable one for the German residential investment market, and one we are unlikely to see repeated in a hurry. Overall residential portfolio turnover for the year reached €13.8bn, up 35% on the previous year's €10.23bn – itself a boom year in the sector.

Figures published by property advisor **Savills** show that the number of transacted portfolios rose by 17% to 193, against 165 in 2012, and the number of units transacted increased by 14% to over 221,000, compared with approximately 193,000 in 2012, based on Savills' own data.

Karsten Nemecek, managing director corporate finance – valuation at Savills Germany, commentsed, ‚2013 was a remarkable year for residential investment. No other property type in Germany attracted higher amounts of money from institutional investors than residential portfolios.'

The firm's research reveals that public real estate companies and REITs were by far the largest group of buyers in 2013, accounting for a share of 54% of investment

(approximately €6.9bn). Insurance firms and pension funds are next on the list, accounting for a share of almost 9% (€1.2 bn). Domestic buyers dominated, accounting for 75% of the transaction volume, followed by investors from Luxembourg (approximately 6%) and Austria (5%).

Of the sellers, German investors also dominated accounting for 61% of sales, followed by US (13%) and Swiss vendors (11%), according to Savills. These figures do not include the GSW acquisition for which its shareholders were paid by means of Deutsche Wohnen shares and consequently did not sell residential properties. In terms of investor types, banks were the most active sellers accounting for 32% of sales, followed by private equity funds (17%) and public real estate companies and REITs (11%).

Despite the ongoing strong interest in German residential real estate Savills suggests the market for residential portfolios is likely to have reached its cyclical high in 2013 with the transaction volume expected to slow down this year. This is partly due to a lack of suitable properties for sale, but also due to fears of the possible effects of the new Mietpreisbremse ("rental brake") and other legal impositions being championed by the government coalition.

Matthias Pink, responsible for research at Savills Germany, is still optimistic: "There is much to suggest that even in 2014 an above-average transaction volume will be achieved. With a decreasing supply of available stock for sale a lot will happen on the capital market in the form of IPOs, which are not reflected in the statistics, as well as mergers and acquisitions of companies."

Germany/Research

Study highlights fragmentation of Germany's residential sector

A new study on Germany's residential housing market shows how fragmented the market is and how the lack of scale efficiencies have led to inflated cost structures, despite robust growth among listed residential property firms.

The study, produced by two partner consultancies **Akselrod Consulting** and **Barkow Consulting**, is the latest in a series of useful research prepared by **Jesse Freitag-Akselrod** and **Peter Barkow** on Germany's listed real estate companies and the role of the capital markets as a source of finance for the sector. For this study the researchers analysed ownership data from more than 300 German

UPCOMING EVENTS AND CONFERENCES

EVENTS/ CONFERENCES Feb-March 2014

February 4th-5th, Tues-Wednesday
ULI Europe Annual Conference 2014, Westin Hotel, Paris, France
The 18th ULI Europe Annual Conference will be themed 'Rethinking, Reinvention and Recovery', reflecting the continued improvement in sentiment towards Europe's real estate markets. The conference is being chaired by Giancarlo Scotti, CEO of Generali Real Estate.i
More at www.parisconference.uli.org

February 11th-12th, Tues-Wednesday
24th Quo Vadis, Adlon Kempinski Hotel, Berlin
The 24th edition of the Heuer-Dialog managed early-year conference for the Gemran real estate industry, the German-language event normally attracts about 300 visitors from the top ranks of German real estate. Will Germany remain the focus for leading institutional investors?.
More at www.heuer-dialog.de

March 11th-14th, Tues-Friday
MIPIM, Cannes
The 25th staging of the annual world's commercial property fair. Last year with 19,000 sqm of exhibitors on 40,000 sqm of space, 2,000 exhibinting companies from 80 countries, 20,000 individual participants, 3,000 CEOs and chairmen, 4,300 investors, 460 journalists, and more. Firmly established as one of the key events of the real estate calendar.
.More at www.heuer-dialog.de

May 7th-8th, Tuesday-Wednesday
10th annual Deutsche GRI, Frankfurt
The leading international players and national decision-makers driving the real estate business in Germany today. In keeping with the GRI formula, no speakers, no panelists, just informal discussions in small groups, where everyone participates
More at www.globalrealestate.org

residential landlords.

The study shows that the biggest ten listed German residential property firms added over 300,000 units to their portfolios in 2013 to bring their totals up to more than 1.1m units, up from 900,000 units in 2011.

Nonetheless, says the study, even if the Top 10 German housing investors now own marginally more units than the next largest 40 companies, their combined portfolios still only represent about 5% of the total market for rental accomodation.

Over the last 24 months, the Top 10 has seen three new entrants: Berlin-based **Deutsche Wohnen**, with the largest absolute increase in housing units at 96,000 and now merged with fellow Berlin company **GSW Immobilien AG**, Hamburg's **TAG Immobilien** with the largest rise in the Top 10 over a two-year period, and **Vivawest**, the group established by the merger of **Evonik Wohnen** and **THS**. Vivawest has an unusual ownership structure, encompassing a foundation, a pension fund, a union and the publicly-listed energy conglomerate Evonik.

The researchers highlight how half of the Top 10 residential owners are stock-exchange listed, with three largest being **Deutsche Annington**, Deutsche Wohnen and **GAGFAH**. Two other listed players, LEG and TAG, are respectively the sixth and seventh largest. Public housing companies **SAGA GWG**, **Degewo**, **Nassauische Heimstätte**, and **GEWOBAG** account for the remaining four.

"The above results highlight a high degree of fragmentation in the German residential market and suggest the lack of scale efficiencies and inflated cost structures in large parts of the residential universe," the consultants say.

The 16 publicly listed companies included in their research own a combined 770,000 German housing units, or about 26% of the sample. Of this, 80,000 units are owned by four foreign listed companies. In 2013 the listed sector grew by around 310,000 units, largely driven by the IPOs of Annington and **LEG**, but also benefiting from ongoing company acquisitions and consolidation.

"The listed space is thus the most dynamic player in terms of residential market share gains," the report said, but added: "Such gains come largely at the expense of privately-held companies."

Germany/Conferences

BIIS Conference focused on changes in German market

The question of how Germany's troubled open-ended and closed-ended funds would fare this year was at the centre of this year's gathering of the Association of German Real Estate Valuers **BIIS,** against a global background where 10% more institutional money is expected to flow into real estate worldwide.

The 200 assembled delegates heard from **Hela Hinrichs**, researcher at **Jones Lang LaSalle**, how more than €600bn additional funds would be invested in real estate this year, and how "for every dollar of real estate there are seven investment dollars waiting". However, she warned, nothing can be taken for granted. In particular, Germany is grappling with the whole issue of how much office space is really required for all these employees. Long with the most generous amount of space per employee of any market, Germany is undergoing steady change.

Daniel Tochtermann, head of real estate investment at **Credit Suisse**, advised delegates (somewhat tongue-in-cheek?) to invest in new buildings if they could, since there is so little bank finance available for project developments. Preferably assets between core and value-added, he said enigmatically, „If you have a competitive building in a competitive location, then you can certainly accept a two-to-three year lease contract, as long as its's not rented out too expensively."

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CORPUS SIREO
REAL ESTATE

A BOOMING MARKET SEGMENT: 100 NEW MEDICAL SERVICE CENTRES CREATED ANNUALLY

Guest essay by:

Douglas Edwards, Managing Director, CORPUS SIREO Investment Management S. à r.l.

CORPUS SIREO expects rapid growth in this market segment of healthcare real estate, creating challenges for both project developers and asset managers alike.

Medical Office Buildings (MOBs), the properties housing the new medical centres, represent a growth driven segment in Germany's real estate market, assisted by the emergence of a new and dynamic tenant base – the "Medizinische Versorgungszentren" (MVZ). Between 2006 and 2011, the development and growth of MVZs, assisted by proactive legislation, tripled in number, climbing to around 1,800, whilst the number of physicians employed in these facilities doubled to an average of six per MVZ during the same period of time. CORPUS SIREO expects a long-term annual completion rate of circa 100 new MVZs, which will continue to drive demand for the development of new MOBs.

Recent publications by the German National Association of Statutory Health Insurance Physicians (KBV) substantiated the sustained growth of the MVZ segment. Totaling around 1,800 facilities by the end of 2011, their number increased several fold since the introduction of the 2004 legislation which allowed for their creation. This growth trend is expected to continue in the wake of the 2012 Supply Structure Act (VStG). There is also a defined upward trend in the scale and networking intensity within the existing MVZ segment, in particular when they are co-sponsored by a hospital organization.

MVZ: A growing tenant base

What sets MVZs apart from the traditional medical centers ("Ärztehäuser") and medical service centres ("Gesundheitszentren") is mainly their organizational and legal form. In the former two types, physicians rent out office space in their own right. Resident physicians operating within an MVZ, are by contrast, jointly organized in a private limited company (GmbH) or a private partnership (GbR). An MVZ is able to be a multi-disciplined organization having

within its operating structure a variety of healthcare professionals, other than just physicians, all of whom seek are able to offer patients with their ambulatory care needs. MVZs are frequently operated by hospitals, the idea being to expand their service spectrum. These cooperative business models generate organizational and financial synergistic benefits, whilst patients benefit from direct contact to an array of specialist physicians and healthcare professionals within a single entity.

MOBs: Continued rise in demand

The properties housing MVZs are referred to as "medical office buildings" (MOB). The current rise in demand for these assets, which is forecast to continue to expand given Germany's demographic trend, represents a real challenge for project developers and asset managers alike, due to the specials requirements associated with purpose-built properties of this type.

An MOB typically accommodates 10 – 25 tenants on a net lettable area of 3,000 to 5,000 square meters. The investment volume for this type of property can range from €5 – €30mn, which creates a need to aggregate and manage the assets on a regional, sub regional basis, ensuring economies of scale and ability to attract institutional capital into the sector. The current project developers constructing MOBs still tend to be regional or city focused, meaning an investor has to be able to reach across a number of markets to facilitate a wider investment strategy in the sector. The fact that the MVZs are rooted in their local communities, and the MOBs housing them tend to let space to them on leases as long as 15, or even 20 years, makes investment in this real estate segment highly interesting for safety-conscious, income driven, investors. The US market has seen the strongest development by far in this field of healthcare real estate, with numerous listed REITs and institutions operating within the MoB sector.

Having been active in the "healthcare real estate" segment for many years with its own institutional funds, CORPUS SIREO now intends to step up its commitment in this market.

For more informations, please go to: www.corpussireo.com
Follow us on Twitter: @corpussireo

THE REAL ESTATE PEOPLE®

Sponsored Statement

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Jörg Kramer, chief economist at **Commerzbank**, painted an economic picture for Europe with the inflation rate in the Eurozone likely to remain at 1% for the next 12-24 months. However, he sees trouble in Belgium, the Netherlands, France and Finland due to too high wage levels, too much credit, and looming price bubbles in housing – with prices now at least falling in the Netherlands, but with the others soon to follow, he forecast.

Germany/Financing

Strong demand for Berlin Hyp €500m bond

Kicking off the unsecured benchmark bond market this year was German lender **Berlin Hyp** which placed a €500m five-year senior facility.

Due to the strong demand, the volume was increased to €750 mln, the bank said. The bond was issued with an initial spread at mid-swap + high 50s, and the order book opened in the mid-swap +55 region. The bank received orders for as much as €2.1bn at this level, Berlin Hyp said. The order book was closed by the underwriting banks after less than an hour and the price was set at mid-swap +53 basis points. The bond's coupon rate is 1.625%.

The order book included about 200 individual orders, the majority of which came from Germany (80%). More than half of the bond went to savings banks, which are traditionally the main buyers for Berlin Hyp's bonds. The share of subscriptions by foreign investors was dominated by orders from Scandinavia. The unsecured bond was placed on the market by a consortium consisting of **Commerzbank**, **DekaBank**, **DZ Bank**, **HSBC** and **Landesbank Baden-Württemberg**.

Parent company Landesbank Berlin has been going through major restructuring, and said it was important to issue the new bond to an even broader investment

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base. Board member Gero Bergmann said "The high participation rate of savings banks shows that Berlin Hyp has an excellent reputation as an issuer in its own sector. At the same time, we were also able to place a significant portion of the bond with other German and international investors…. Particularly in light of the restructuring measures in the Landesbank Berlin Group and Berlin Hyp's progression to a savings banks' partner for commercial real estate financing, we are convinced that the path we have taken is the correct one."

Austria/Research

Austrian Central bank downplays fears of property bubble

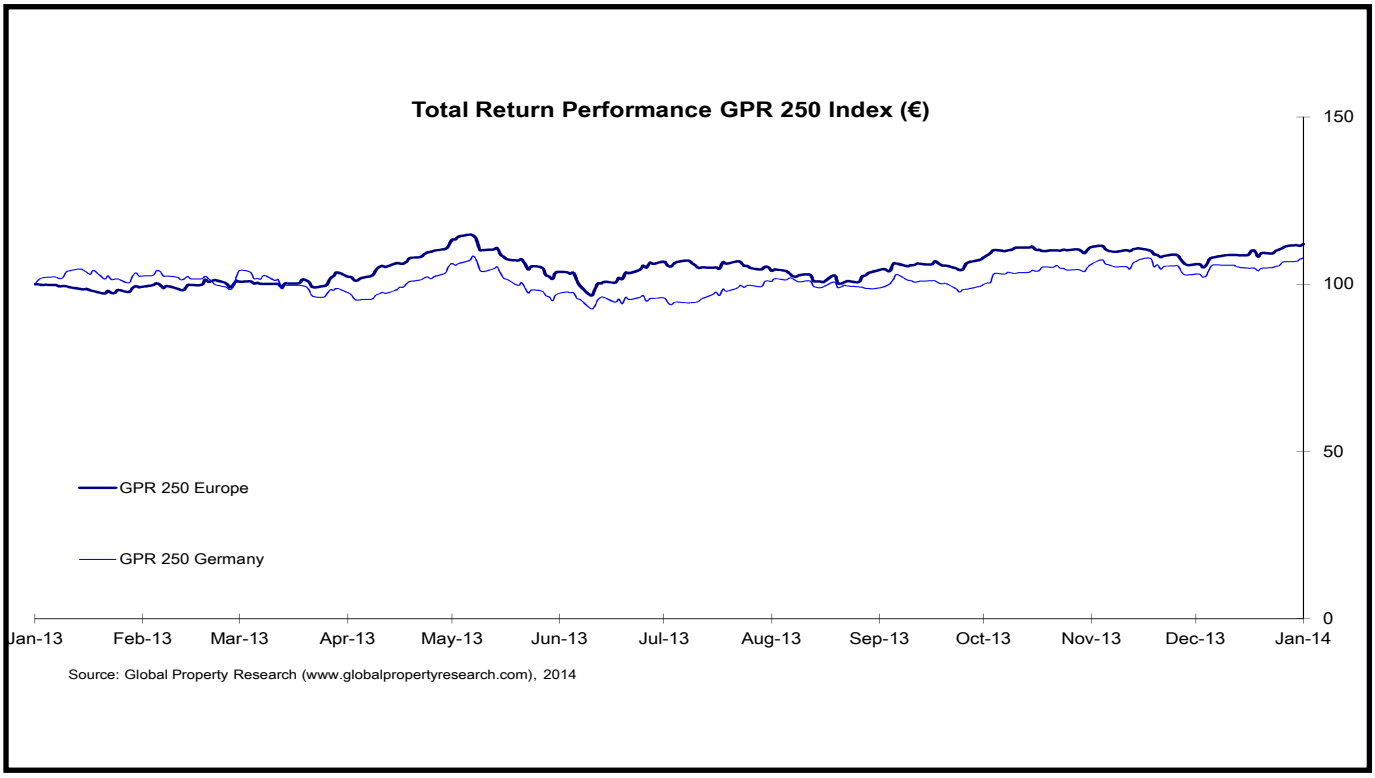
Following on the heels of several statements from German's **Bundesbank** downplaying any real estate bubble fears here in Germany, Austria's central bank has also taken pains to allay concerns that

there is any emerging real estate bubble in Vienna and throughout the rest of the country. It said it was monitoring the situation closely and was introducing a new fundamental price indicator.

Residential real estate in Austria has increased 39% between 2007 and 2013, the highest increase seen in the eurozone. Vienna saw particular price hikes with the top-end of the market attracting foreign buyers looking for second homes. Across Austria second-hand apartments saw the largest price increases, but single family homes and new apartment also saw substantial price rises. Low interest rates holding mortgages down, as well as demographic factors, and the lack of alternatives offering equivalent yields, are given as the main reasons for the price surge.

In a statement last week, the Austrian central bank commented, "The risk to financial stability from increasing real estate prices is gauged to be low." At the same time the bank said that Vienna real estate is overvalued by 21%, while residential real estate for the country as a whole is undervalued by 8%.

According to **Georg Fichtinger**, **CBRE**'s head of capital markets in Austria, the bulk of buyers have been investors who are looking for "insurance for the future" and are "looking to park a certain amount of money," While Vienna's top-end apartment market has been dominated by buyers from outside of the country looking to invest, the market for small apartments–seen as investments for retirement or to be rented out–has been dominated almost 100% by local investors, Fichtinger said.



Graph of Total Return Performance of Europe and Germany in € currency over the past twelve months

Charts courtesy of GPR Global Property Research

Germany/Logistics

Logistics yields remain under pressure as buyers swarm in

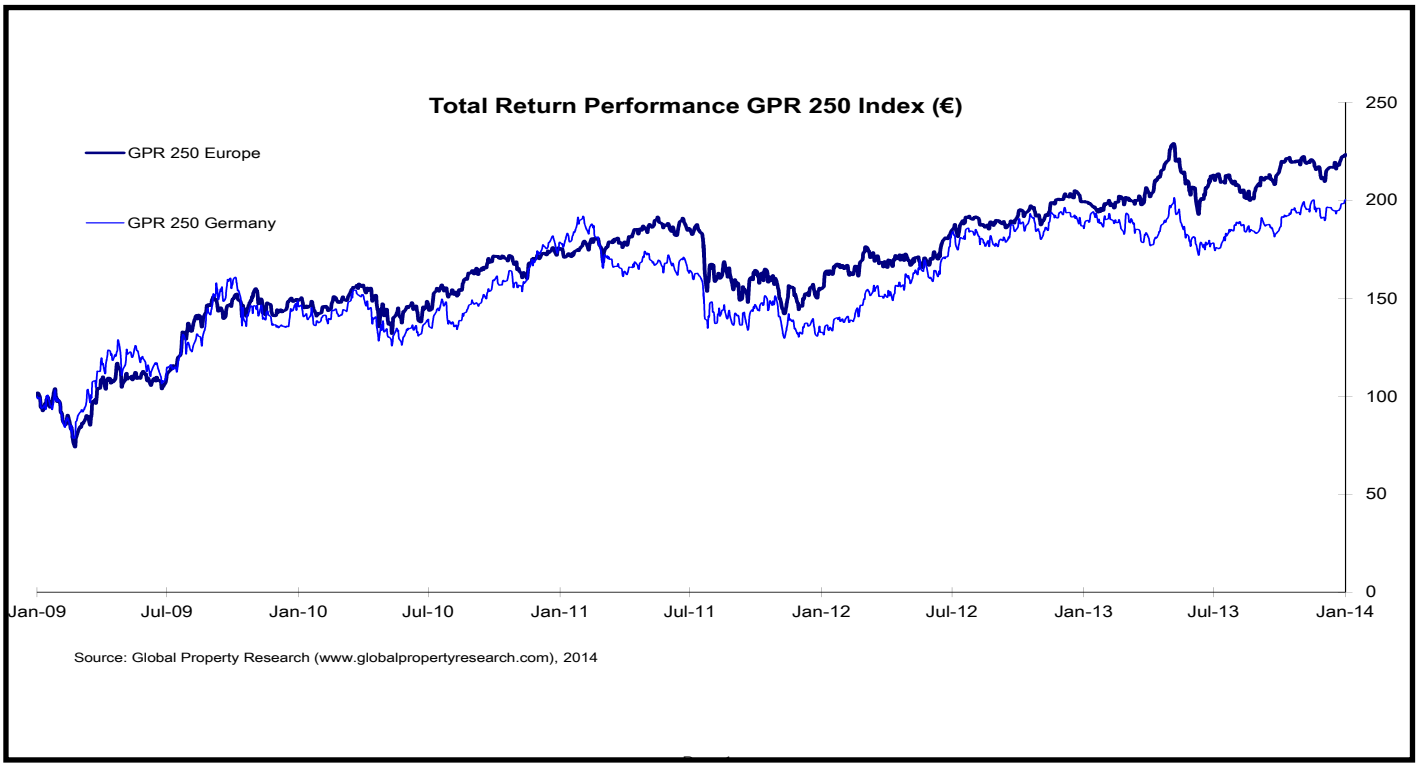
The German for logistics real estate investment had it s best year last year since 2007, with nearly €2.3bn of transaction volume, up 40% on the year before, with 75% being invested in existing logistic assets. About €1.2bn or 52% came from institutional funds, while foreign investors were responsible for nearly half (46%) of all investment, the latest figures from property advisor **Colliers International** show.

This makes for the fourth year in a row that German logistics volume has exceeded the previous years, with increasing pressure on yields as prices rise. Of the six major metropolitan areas examined in the study – Berlin, Düsseldorf, Frankfurt, Hamburg, Munich and Stuttgart – the average top yield was 6.90%, or 22 basis points lower than twelve months previously. The most expensive was Frankfurt with yields of 6.7%, followed by Düsseldorf and Munich at 6.75%, Berlin at 6.8%, while Hamburg and Stuttgart remained unchanged at 7.2%.

CBRE also issued figures on the logistics market for the year, which differed slightly from Colliers, but agreed on the main points. The investment volume now makes logistics property the third-largest real estate asset category behind office and retail, with 7.1% of total investment. Almost 70% of the investment volume went to the Class A new generation distribution facilities including cross docks, about 25% to standard warehouses and the remaining portion to production facilities, say the CBRE figures.

All the big brokerage groups are predicting further strong demand through 2014, as global capital pools re-position to take advantage of the surge in online shopping, which is transforming the industry. Over the last eighteen months big new investor names piling into European logistics real estate include **Norges REIM** managing Norway's giant pension fund, **Prologis**, **Blackstone-Logicor, Canada Pension-SEGRO**, **Brookfield-Gazeley, HOOPP-Verdion**, **Point Park-TPG Ivanhoe Cambridge**, **TIAA-CREF-Henderson**, while Australian-owned **Goodman Europe** is boosting its **GELF** fund, and teeing up a partnership with a Malaysian joint venture, to name just a few.

The rise in the market share by foreign investors (of 6% to 49% last year), and overall demand for exposure to the sector is likely to continue this year. According to **Peter Kunz**, (*pictured, left*) head of industrial and logistics at Colliers International, „If the positive forecasts for the German economy kick in over the



Graph of the total return performance of Europe and Germany in Euro currency over the past five years

REFIRE charts courtesy of GPR, Global Property Research

next couple of months then the overall prospects for the logistics investment market in Germany could improve even further. The domestic economy could grow noticeably if the USA and China are strong, in which case the willingness to invest and demand for new storage, logistics and light industrial space could all rise. We are confident we will again see more than 2bn of investment in the sector this year“, he said.

Germany/Funds

Internos teams up with French investor for German retail fund

UK-based **Internos Global Investors** is teaming up with French fund manager **PAREF Gestion** to launch the first French SCPI retail real estate fund investing exclusively in Germany. The specially constructed fund, called **Novapierre Allemagne**, is designed to offer solid returns and a favourable tax regime for French investors. The initiators say the fund will be a unique product in the French market.

Novapierre Allemagne will focus on “German retail property assets on the outskirts of medium-sized German cities which will offer secure and durable revenue streams“. The fund is aiming to raise €20m capital from both institutional and private investors by the end of this year, has a target capitalisation of €100m, and is targeting a return of 6%.

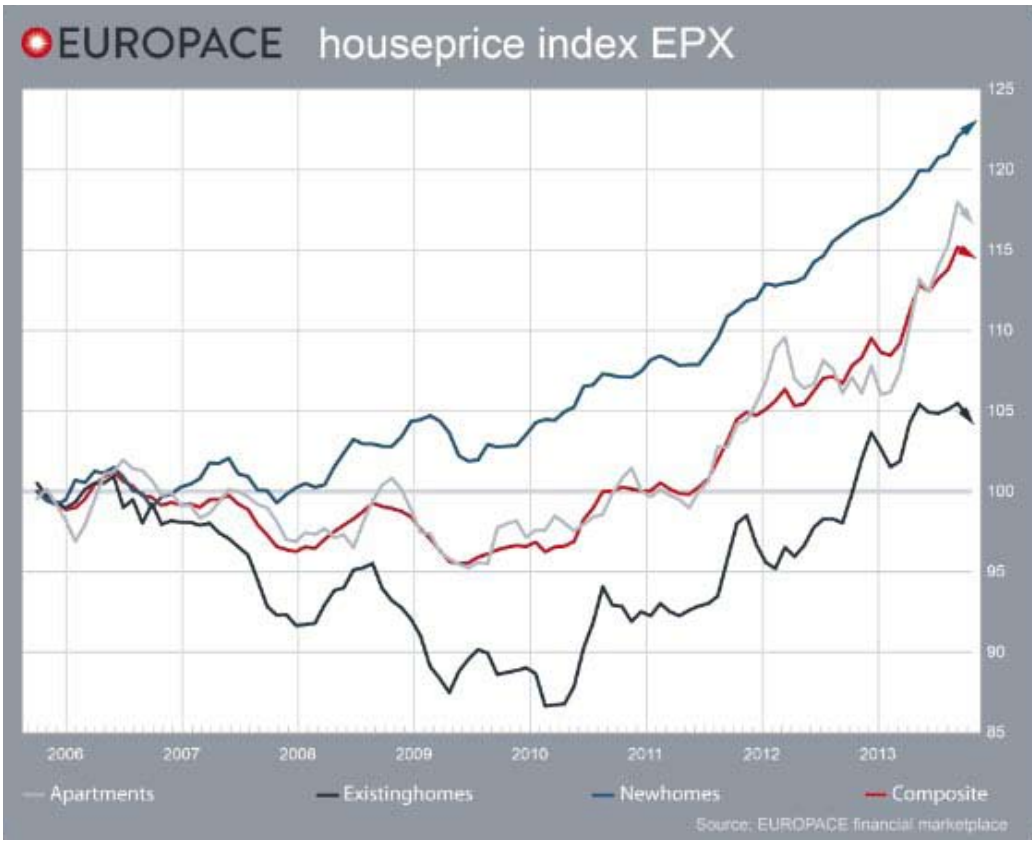
While PAREF Gestion is handling the marketing and administration as well as investor relations, Internos will deal with asset selection, management, tenant relationships, and generally optimising the returns from the fund.

Parent company **PAREF**, Internos and French insurer **APICIL Assurances** have provided initial capital for the fund, with APICIL including an offer to invest in the fund through its life insurance products.

Internos already manages six funds in Germany with 116 retail property assets, ranging from stand-alone discount stores to shopping centres, valued at about €813m. All in all, it manages €1.5bn of German assets, and a total of €4.1bn across Europe (which it recently said, as reported in REFIRE, it aims to expand to €5bn over the next two years).

A 55-year old Franco-German tax treaty means that Novapierre Allemagne’s rental income and capital gains will be subject to German corporation tax of 15.825% and exempt from French income tax and social charges, according to PAREF Gestion.

PAREF Gestion is a 100% subsidiary of the listed PAREF Group and had €800m of property assets under management at end-June2013. It specialises in the management of SCPI and OPCI unlisted real estate funds (special structures under French investment law). In addition to this latest fund Novapierre Allemagne, it offers four other SCPIs to institutional investors



Germany/Retail

UK‘s Tristan Fund buys German, Austrian centres for €110m

UK-based **Tristan Capital Partners‘ EPISO3** opportunity fund signed off on three separate property deals in Austria and Germany, valued at €110 million.

European Property Investors Special Opportunities 3 (EPISO3) bought two neighbourhood shopping centres: one in Vienna immediately northeast of the city centre for €75m, and the other one close to the centre of the German city of Bremen for

Guest Opinion

Property – the Better Investment
by Jochen Schenk, Member of the Board, Real I.S. AG

The gap between the total returns of office real estate in European top locations and the returns of comparatively safe government bonds is wider than ever.

Indeed, property returns can be up to 3.5 percent higher, give or take. The fact has investors and market analysts wonder whether office investments truly represent an attractive long-term commitment. Their concern is that such assets may be too costly to qualify as attractive investment anymore. Declining rents or rising yields – in tandem with eroding property prices – could translate into losses by the time you sell.

Even on the basis of a detailed risk assessment, I personally still consider property investments attractive and comparatively profitable – provided the properties are professionally selected and managed.

Let me use a simplified example to show that property prices would actually have to plummet in order to push the total returns of, say, office property below those of government bonds. Certain bonds count among the few large-volume investment alternatives left for safety-oriented investors today – but they have to content themselves with extremely low returns.

Returns on ten-year German "Bunds," for instance, registered a downtrend in recent years, lately hovering around 1.5 percent, which means: If you invest in a ten-year Bund today, you will be paid around 115 percent at maturity.

For the sake of comparison: The average prime yield for office property in Germany's "Big Seven" cities is currently around five percent p.a. The annual distribution results in a net income of 50 percent over a ten-year lifetime – and this from the property's cash flow alone. Not included are the proceeds from the property's eventual disposal. So assuming the asset sells for the same net price at which it was bought, the investor will realise a total return of 150 percent. Taking risk aspects into account, this means: Even if the property was to sell at a 35-percent discount on the purchase price, you would still have the equivalent of a 115-percent return on a bond investment.

A look at initial rates of return shows just how unlikely an impairment of this magnitude is: If a given property sold for a mere 65 percent of its former purchase price, this would imply an increase in acquisition yield for prime property from currently around five percent to 6.6 percent – a rate that has no historic precedent in high-end property sales and that we are unlikely to see in the future.

Moreover, worries over such drastic drops in rent seem unfounded – at least as long as investors stick to the right locations. In fact, market observers assume that prime rents in top locations will keep rising in the years to come. This goes not just for a number of German cities like Berlin, Munich, Hamburg or Düsseldorf, but also for many metropolises elsewhere in Europe, such as Paris and Amsterdam. The rental growth is driven by low completion volumes.

Modern office accommodation of the sort most sought by corporates is particularly hard to find. This is not about to change anytime soon and rents will keep pushing up in response to high demand and low supply. Owner of existing schemes stand to benefit from this trend, assuming they have an active asset management in place to match current market developments, for example by customising units to meet actual tenant needs.

While this may be a simplifying account, it does highlight one thing, I believe: When you compare the asset classes of gilts and real estate, the latter clearly comes out on top, even if you take the lower degree of liquidity into account. The spectre of price drops, which many investors fear, is not very worrisome.

Even if sales proceeds were to fall radically short of purchase prices, property investors would still run circles around bond holders. That being said, the profitability of property is hardly a foregone conclusion but the result of close scrutiny and a sober weighing of threats and opportunities.

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€32m. The third transaction involved the sale of an office building in East Berlin acquired for the fund nine months ago from a commercial mortgage backed securities (CMBS) vehicle.

The 36,000 sqm *Shopping Centre Nord* in Floridsdorf, a suburb 11 km northeast of central Vienna, is 85% occupied, with supermarket chain **Merkur** as the anchor tenant. The two-storey shopping centre has 83 national and international retailers including **H&M**, **McDonald's**, **Benetton** and **Marc O'Polo**. The centre's leisure facilities include a multiplex cinema and a paintball complex, while an adjacent multi-story car park provides space for 1,500 vehicles.

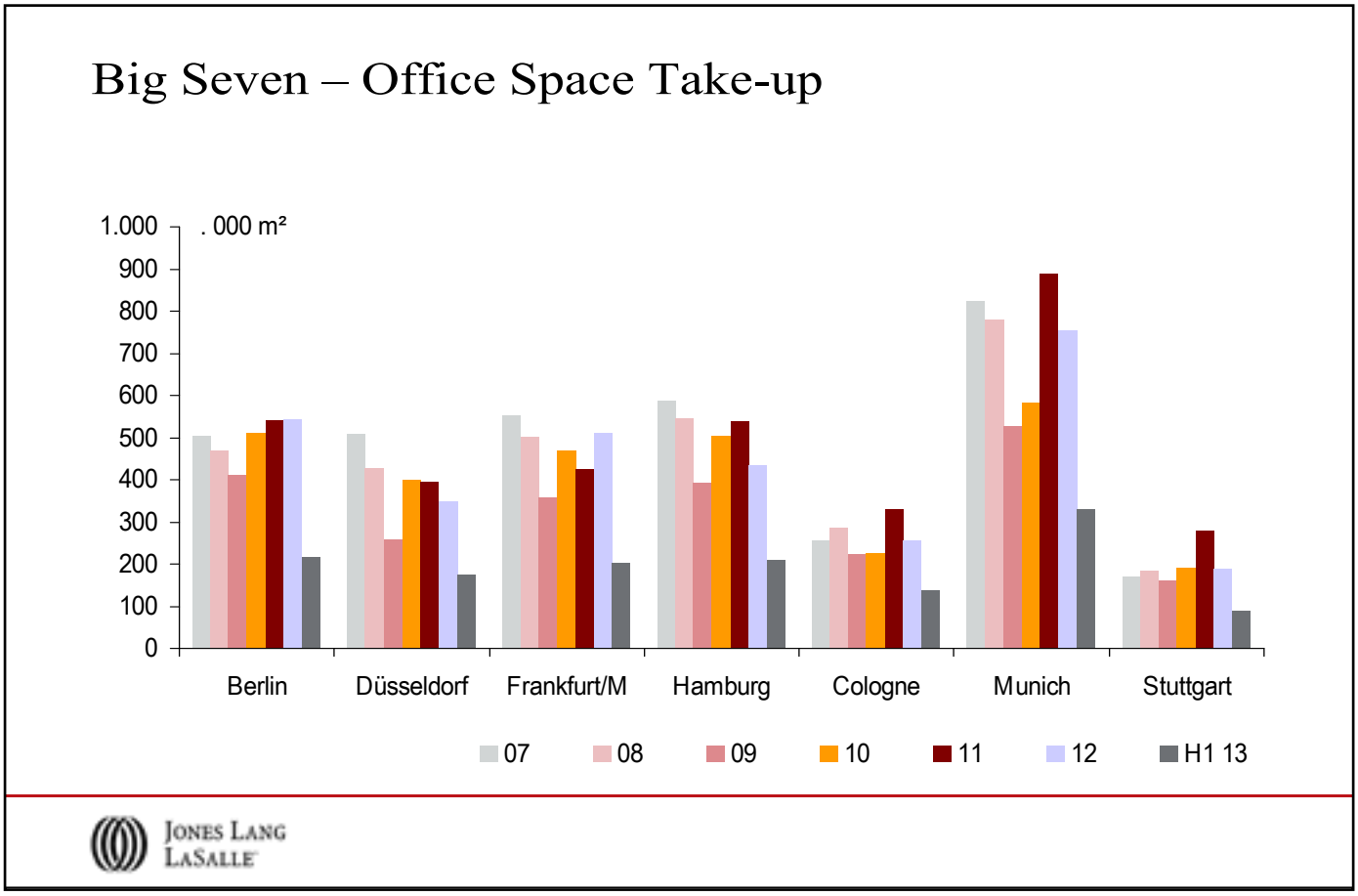
EPISO3 partnered with **Blue Asset Management**, which is responsible for asset management on the ground as well as tenant relationships and execution of the planned extensive refurbishment initiatives for the centre.

In Bremen, the fund bought the 24,400 sqm *Walle-Centre* in a residential district of the German city from a closed-end fund in liquidation. The building opened in 1999 and has supermarket chain **EDEKA** as its anchor tenant, which has agreed to a lease extension subsequent to signing. Among the other 55 tenants are nationwide convenience retailers, such as **Aldi**, **Rossmann**, **Tchibo** and fast food chain **McDonald's**. In addition, the center features a small business office section let to the Bremen police department.

Frankfurt-based **Kintyre Investments,** which sourced the transaction and is a minority co-investor, will be the local operating partner responsible for asset management of the center as well as tenant relationships.

According to **Ali Otmar**,Tristan's managing director for investments, "Although both assets have been well-established and entrenched in their locations, they display a backlog of asset management. Once they have been repositioned, we anticipate they will appeal strongly to institutional investors, given their appetite for defensive retail-related properties,"

The third deal saw EPISO3 selling the 14,900 sqm *Die Welle* office building in the Lichtenberg district of east Berlin to private investors for €4.5 million. The sale of the property represents a profitable exit at a 35% gross profit only eight months after acquisition by the Fund in April 2013 along with the *Jannowitz Center* in Berlin Mitte, in a sale administered on behalf of a **Cornerstone Titan Europe** CMBS vehicle.



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