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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Refinancing
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German brokers braced for slump after introduction of new 'agency principle' law

The law on rental commissions in Germany changed fundamentally on June 1st with the introduction of the "Bestellerprinzip", or agency principle – in other words, he who orders, pays. The new measure came into effect, along with what has been seen as a 'sister' measure to protect potential tenants in affordable housing - the 'Mietpreisbremse', or rental cap, designed to limit rent rises in areas where demand significantly exceeds supply in the most popular German cities

Prospective tenants in Germany have traditionally paid 2.38 months 'cold' rent in the form of commission to a property broker to secure an apartment, although the broker was mandated by the landlord, at neither risk nor cost to the landlord. In this, Germany has long been out of kilter with other markets, where the normal practice is for the commission is paid by the landlord.

According to **Jürgen Michael Schick,** the vice president of the national property association **IVD**, competition among servicers is bound to increase, and not all brokers are going to survive the heightened pressure – closures and layoffs are inevitable, he believes.

"The introduction of the agency principle will fundamentally change residential brokerage in Germany," says Schick. "But it has nothing to do with the quality of brokerage and is not the right tool to eliminate the 'black sheep' from the market. As many landlords will now forego brokerage services altogether, competition among servicers will increase."

Germany has about 38,000 registered property brokers, who collectively earn €17.1bn in commissions annually. The lawmakers expect a fall in this turnover of €310m, or an average loss across all brokers of €8,200 each.

A survey carried out by market research group **Talocasa** among 300 German property brokers showed that 84% of brokers expect the new law to lead to less instructions from landlords to rent a property. 59% believe the law will lead

Helaba heads list of German banks' new property lending

A new report issued by property advisors JLL shows that German banks boosted their commercial real estate lending in 2014 by 11% to 37bn last year, and are anticipating about the same or slightly higher volumes this year. . . see page 5

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Deutsche Wohnen AG raises €900m in new rights issue

Germany's second-biggest residential housing company Deutsche Wohnen raised gross proceeds of €907m this week in a rights issue. Shareholders were offered one new share for every seven they hold, at a price of €21.50 (the current traded price is about €22.15) see page 6

Project developments in big German cities rise 12%

Investment in project developments planned between 2012-2019 in the top seven German cities has grown by 12% from last year to €112bn buoyed by rising rents, prices and larger space volumes, says Berlin-based research firm BulwienGesa. see page 18

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to lower commissions for themselves, with 21% saying they fear for their very existence. Most accept that the changes are likely, however, to lead to a better image for their frequently maligned profession.

The responses differ markedly between independent freelance brokers and those who work for the bigger franchise chains such as **Engel & Voelkers** or **Re/Max**, with the latter group much more optimistic about their chances (69%) and a more positive image for their industry than the independents (43%). Similar trends for further training and education are also highlighted by the study, with 29% of the franchise brokers planning further study and training, as against 13% of the independents.

Both groups are united on one thing – that conditions for tenants will worsen as a result of the new law, with 76% believing that landlords will find a way to claw the money back from their tenants

Both groups are united on one thing – 71% are convinced that conditions for tenants will worsen as a result of the new law, with 76% believing that landlords will somehow find a way to claw the money back from their tenants if they have had to pay the commission to the broker themselves.

Another survey, by property portal Immowelt, showed that 86% of property brokers said they expect many landlords to take charge of rentals themselves. With the new regulation, landlords will weigh different brokerage options which will lead to increased competition against a shrinking market.

A survey by the **Center for Real Estate Studies** at Berlin's **Steinbeis University** showed that landlords are willing to pay €245-€560 per brokered flat, while other surveys indicated 1x net cold rent, well below current commission rates. It will take some months for the effects of the law to make themselves felt, but it is a mini-revolution for Germany all the same.

DEALS ROUNDUP

Germany/Banking

Aareal completes takeover of profitable WestImmo

Wiesbaden-based property lender **Aareal Bank** has finalised the acquisition of all the shares in **Westdeutsche Immobilienbank (WestImmo)** from **EEA**, the workout bank of former owner **WestLB** for €350m, in the process gaining a €4.3bn performing European commercial property loan book. Aareal funded the takeover out of its own cash reserves.

In February of this year, Aareal succeeded in a long drawn-out bidding process, that had been halted at several stages due to the "inadequacy of the bids", and "severe market deterioration", according to WestLB. Among many underbidders along the way were **Lone Star**, **Apollo Global Management** (with whom exclusive talks were ultimately broken off), **ING Real Estate** and fund management group **PIMCO**, whose parent **Allianz** itself has a burgeoning German property loan book.

Despite being forbidden to generate new business while the sales process for itself was ongoing, WestImmo delivered 2014 net profits of a record €64m. the Mainz-based bank owns total assets of around €8.1 bn. Its €4.3bn commercial property portfolio is widely diversified - both geographically and in terms of the type of financed properties. Germany accounts for one-third of the assets, while Western Europe represents another 38% and North America takes a 9% share. It has been hiving off its non-strategic assets to refocus on its core business for the past three years.

In a press statement, Aareal said: "The acquisition of WestImmo is a targeted investment into Aareal Bank's

core business segment of Structured Property Financing. This transaction creates added value for Aareal Bank from the very beginning, partly with the negative goodwill of approximately € 150 million recorded upon closing the deal; in addition to this one-off effect, the transaction will make a positive contribution to Aareal Bank Group's consolidated operating profit.

"Aareal Bank aims to integrate WestImmo swiftly into the group. The technical integration is intended to take place by the end of the year. Discussions will shortly take place with the competent bodies about the future strategic focus of the new subsidiary, which apart from renewals is no longer active on the market itself on account of EU requirements since 2012.

"These discussions will for instance cover the possible inclusion of WestImmo in Aareal Bank's new business activities and the settlement of existing overlaps in the location network. Operations in Mainz will be maintained for at least three years. Strategic options are being examined for the private customer business of WestImmo concentrated in Münster, which is not part of Aareal Bank Group's core business.

"Overall, Aareal Bank assumes that a significant number of jobs at WestImmo will be kept at least in the medium term, regardless of the extensive integration planned. A control and profit transfer agreement will be concluded in the near future as part of the forthcoming integration of WestImmo."

Separately the bank said at its AGM during the month that it had raised first quarter new business to €1.8bn from €1.6bn, confirming its full-year profit guidance of €400m-€430m, including the negative goodwill from the WestImmo acquisition. During the first quarter, Aareal said it raised fresh long-term funds of €900m, including €700m of mortgage Pfandbriefe and €200m of unsecured financing. At the meeting shareholders approved the payment of a dividend of €1.20 per share for the 2014 full year, up from €0.75 the previous year.

EDITORIAL

The path to German retail success is paved with the graves of fallen heroes

Two further German companies are scrambling to make themselves fit for a public flotation, shunning their hitherto modest self-containment, and now suiting and booting themselves for a new life under the scrutiny of the analysts and the number crunchers.

Ado Properties, a Berlin residential specialist, and Aurelis Real Estate, a project developer and nationwide owner of valuable urban landbanks as a legacy of its old Deutsche Bahn railway holdings, are prepping themselves for IPOs this year. Australian group BGP is also thought to be pondering a public listing of its remaining German housing interests.

With the cost of refinancing so low, and Germany riding so high in popular perception, it's understandable why these companies, all of whom have majority foreign shareholders, want to make hay while the sun is still shining. There is - still - good mileage in their equity stories.

There are now twelve German real estate companies in the leading MDax and SDax listed segments, with the 800-pound gorilla Deutsche Annington vying for a coveted place in the Dax, representing Germany's top 30 industrial companies. This could happen within a few months. Most of the listed companies have seen spectacular share price rises over the past eighteen months, with the average for the sub-sector All Real Estate up 60% since the beginning of 2014, compared to the 20% rise enjoyed by the Dax and MDax in that time. Several companies have seen their share prices multiply.

Never has so much money been raised by the listed sector, with new share sales reaching a record €4.8bn last year, 29% more than in 2013. Just last week Deutsche Wohnen raised €907m in a seven-for-one rights issue, by a margin the highest cash capital increase ever in the German real estate industry – and nearly twice as much as the next highest, by Deutsche Wohnen itself, back in 2012.

It would be easy to conclude that all this easy money is providing fodder for a further rash of takeovers, mergers and acquisitions, in a heady dash to fuel investor fantasies with visions of the next great mega-merger with its boundless synergies and lucrative scale effects. But it was Deutsche Wohnen itself which pulled the plug on its own takeover bid for troubled Austrian group conwert Immobilien recently, in a clear statement that the sky was not the limit as to what it would pay to bulk up.

It would also be comforting to believe that German institutional investors have finally fallen in love with the stock market, and are tucking away large blocks of their own property industry as a long-term hold, part of their widely-heralded commitment to increase their allocation to real estate.

Not so, unfortunately. German listed property shares are held 95% - repeat, 95% - by foreign investors. The traditional German aversion to stock market volatility helps ensure that domestic insurers and pension funds give the stock market a wide berth – to the benefit of the rejuvenated funds industry, particularly *Spezialfonds*. These have added tax benefits for German-domiciled businesses, as well as being easier to justify to disgruntled shareholders, if necessary, since losses are never crystallised quite so clearly.

Apart from investing in REITs, institutional investing in stock market listed companies does NOT count for allocation purposes – and with the REITs industry in Germany effectively stillborn, no help will come from that quarter. So, for the foreseeable, it looks like it's up to the foreigners to keep the indirect investment flag flying in Germany. With the rest of Europe grappling in recovery mode, it's Germany's game to lose.

Now, indirect is one thing, direct investing is another. No matter how favourable the climate, share prices don't rise forever, as trees don't grow to the sky. When they cease to rise, they fall. By contrast, investing *directly* in German real estate always demands a greater degree of involvement – invariably more than anticipated at the outset, as investors always learn.

And sometimes learn painfully, as even retail giant Wal-Mart had to concede when it quit the German market in 2006. The retail behemoth, still the world's largest private employer, met its Waterloo after a nine-year, €1 billion disastrous engagement with the German market, in what is still discussed in business schools as a classic case of cross-cultural antipathy and corporate mis-management.

No matter. It doesn't seem to be putting off Richard Baker, owner and chairman of Canada's venerable Hudson's Bay Company, from tabling a bid for troubled German retailer Kaufhof, by some accounts topping an alternative bid from René Benko's Karstadt group. Baker has achieved wonders at HBC since buying up the bits of the company he didn't own seven years ago, and turned it into a retailing powerhouse with nearly 350 stores under brands including the flagship Hudson's Bay, Lord & Taylor, and Saks Fifth Avenue.

It's hard to know how serious he is about Germany, although his retail moves to date have clearly been more about the real estate than the pure peddling of textiles. In the event of success, however, he is less likely to aggravate his staff by compelling them to smile, greet customers warmly, or help them pack their shopping bags at the till – all of which clearly speeded Wal-Mart's downfall, in a retail market where any signs of humanity other than a rock-bottom price are treated with grave suspicion and mistrust.

The more Canadians in Germany the better, we say. Toronto's DREAM Property REIT and, more recently, the mighty Canada Pension Plan have been wading in with open arms. But a major retailer, intent on improving Kaufhof…? Certainly, but only after visiting the graves of Intermarché, Castorama, Prénatal, Oviesse, Marks & Spencers…

Charles Kingston, Editor

Germany/Banking

Helaba heads list of German banks' new property lending

A new report issued by property advisors **JLL** shows that German banks boosted their commercial real estate lending in 2014 by 11% to 37bn last year, and are anticipating about the same or slightly higher volumes this year.

The JLL study, which surveyed 15 banks active in commercial real estate financing and who made up 70% of all new business lending last year, highlights how the low interest rate climate means that new borrowing and refinancing options remain plentiful for the time being. Competition among lenders is keeping margins low, and are likely to remain low for a while.

Leading the list of active lenders last year was Frankfurt-based **Helaba** with €5.5bn in new business, or 15% of the volume generated by the banks surveyed. Next was **DG Hyp** with €4.7bn (13%) and **HSH Nordbank** with €4.2bn, 50% more than in the previous year. **pbb Deutsche Pfandbriefbank**, **HypoVereinsbank** and **Berlin Hyp** each took an 11% share of the total volume.

Of the big lenders, only DG Hyp and **Aareal Bank** saw a decrease in new business last year, by 12% and 13%, respectively. The latter was impacted by the takeover of **Corealcredit,** JLL said. With the takeover of **WestImmo**, Aareal expects another fall in new business volume to €6bn- €7bn in Germany and abroad in 2015

Despite new business growth in Germany, total loan portfolios (in Germany and abroad) fell by 6% to €226.4bn. The reduction is primarily driven by the two banks that are attempting to reduce their portfolio, which are **Hypothekenbank Frankfurt** (the former **Eurohypo**) and WestImmo, which registered a reduction of 42% and 28%, respectively.

HSH Nordbank lost 20% of its portfolio, despite strong new business growth, **BayernLB** 11%. Aareal's loan book grew

by 15% due to the Corealcredit takeover and is expected to increase with the WestImmo acquisition (see article elsewhere in this issue). Following 9% growth, Helaba replaced Hypothekenbank as the bank with largest portfolio, now managing €34.3bn in its loan book.

Germany/Acquisitions

Orion clinches €600m Odin portfolio deal from Credit Suisse

Two open-ended funds from **Credit Suisse** have sold the much speculated-upon **Odin** office portfolio to London-based private equity firm **Orion Capital Partners**, for a sum thought to be just north of €600m. The portfolio consists of 19 separate assets, mainly located in Berlin and Hamburg, and will be allocated to Orion's **European Real Estate Fund IV.**

Frankfurt-based property lender **Helaba** said it was providing €347m in financing for 11 of the properties, spread over six German cities with a concentration in Hamburg and Berlin, with 178,000 sqm of which 81% is currently let. The top 10 tenants with strong covenants - such as the **Federal Institute for Real Estate Issues**, **Philips**, or **Reemtsma** - account for 72% of the rental income and 57% of the lettable area. Dutch electronic concern Philips' German headquarters in Hamburg is among the assets is included in the sale. The terms were thought to be for five-years, at a margin of less than 200 bps above Euribor.

16 of the properties are being sold from Credit Suisse's **CS Euroreal** public mutual fund, while the remaining three are from the institutional open-ended fund **CS Property Dynami**c. Both the funds are in the process of being wound up with liquidation deadlines of April 2017 and December 2016 respectively. The portfolio was put on the market through **Brookfield Financial** last summer.

According to **Aref Lahham**, one of the three founding partners of Orion (along with **Van Stults** and **Bruce Bossom**), "Orion assessed the quality of the portfolio to be superior compared to other German office portfolios that are currently being marketed. Many of the assets are located in the big seven cities and the portfolio is anchored by strong credit tenants. Orion's business plan is to drive rental income by investing in the premises in order to increase occupancy levels and further institutionalise the assets."

Credit Suisse will continue to manage the assets after the sale to Orion. The fund manager has been selling off assets since closing down the fund in 2011, but CS Euroreal, which had previously been one of the biggest open-ended funds with €5.1bn under management, still had 67 properties in 38 locations across 11 European countries at the end of April. In December 2014 CS Euroreal sold a package of six assets in Sweden, France, Germany and the UK for €315m, or about 6.5% below their last assessed value, and this deal looks to have been sold at a similar discount to the book value of just under €700m.

The deal underlines a strong return to the German market for Orion, which has been absent from the market for several years. In December the group came back to Germany by buying the *Lilien-Carré* shopping centre in Wiesbaden out of insolvency (reported on in these pages). Orion has over €3bn of European office properties under management.

Germany/M&A

Whither the current M&A wave in Germany's listed sector?

We wrote on the front page of last month's REFIRE that we believed there was plenty of scope for futher consolidation in Germany's listed real estate sector, despite the – at the time – recent rejection by Austrian **conwert Immobilien** of the embrace of German housing giant **Deutsche Wohnen AG.**

Within days we found ourselves sitting, among a handful of journalists, together with a small group of hardened property experts in Frankfurt who represented a dichotomy of views as to whether this further consolidation is likely or not – and if so, in what form.

Veteran property analyst at **Berenberg Bank**, **Kai Klose**, was decidedly of the opinion that the recent wave of mergers (**Deutsche Annington/Gagfah**, **Oaktree/Prime Office**, **Adler Real Estate/ Estavis** and **Westgrund**, the proposed **Deutsche Wohnen/conwert** alliance) had now run its course, and this year will see the recently-merged firms bedding down as they try to integrate their activities. Investors are now looking for targeted specialist companies rather than large generalists, he believes.

"These specialists will remain, by definition, smaller here in Germany than in the UK or France, for example, where investment activity is largely concentrated on one big city respectively, London or Paris. After our M&A wave here in Germany, which all made sense in the short term, we'll now have to see if this leads to actually improved company performance."

However, **Arwed Fischer,** CFO at the increasingly pan-European **Patrizia Immobilien AG**, argued that the increasingly complicated regulatory framework being faced by real estate companies is driving further consolidation. "With the costs of conforming to regulatory requirements having risen significantly, economies of scale have taken on even greater importance." So far most of Patrizia's investors are still German, and the company is expanding across Europe to match local expertise with German investor mandates, while at the same time international investors are looking for more exposure to Germany.

Ralf Dibbern, CFO at Germany's first and largest REIT, the Hamburg-headquartered **Alstria Office REIT,** said he believed investors were still attracted by

larger players. "Compared to other European countries, the German commercial listed sector is still very small and it can only gain more visibility through growth." Given the low level of interest rates, the drive to merge may not be so acute right now since everybody can borrow cheaply, but this could change, he believes. With such cheap money, sale-and-lease-bank deals have also lost their attraction, but with a turn-up in interest rates, we could yet again see a trend for corporates and insurers to spin off their real estate interests as REITs.

Klose thinks that the industry has been preparing itself well for higher rates, and has been lowering leverage and focusing on operations in anticipation of rate rises.

Fischer, Dibbern and Klose were all agreed that the proportion of foreign investors in German listed property stocks is still too high, at a whopping 95%. Despite German institutionals' drive to increase their allocation to real estate, a historic aversion to the volatility of the stock market has kept them out of the sector in droves, trusting more in the traditional fund models.

As Fischer noted, investment into listed companies by institutionals does NOT count against their real estate quota. Investing in REITs **does** count – but with only three companies qualifying, and only one (Alstria) of any real size, the options for domestic institutionals remain limited.

Germany/Retail real estate

Germany still lagging behind in market for factory outlet centres

The retail market for factory outlet centres in Germany has long trailed its European neighbours, and the segment is likely to remain a niche offering, despite the arrival of a number of new centres in and just outside Germany, according to a new report published by property advisers **CBRE**.

Eight factory outlets (FOC) with gross lettable space of nearly 120,000 sqm are in the pipeline, while two are currently being built – Montabaur (between Frankfurt and Cologne), and Brehna near Leipzig. Germany and its immediate border areas have 16 factory outlet centres, of which 11 are in Germany itself – at a rate of 1.8 sqm of sales space per 1,000 inhabitants.

This compares to 8.7 sqm per 1,000 inhabitants in the UK, 7.7 sqm per 1,000 inhabitants in Italy, and 9.6 sqm per 1,000 in Switzerland. The USA has about 20 sqm per 1,000 inhabitants. The European market has seen two large transactions in the FOC sector this year, the *Alpenheim Outlet Village* in Switzerland, and *Roppenheim The Style Outlets* in France, where US investor **TIAA Henderson Real Estate** teamed up with outlet specialist **Neinver** as asset manager to spearhead its European move into the sector.

The opening of the Montabaur FOC is scheduled for the coming autumn. The centre is being developed by Dutch project developer **Stable International**, and will have 76 shops with 13,900 sqm. Stable International is also the developer and operator of the FOC in Brehna near Leipzig in Saxony-Anhalt. The centre is being built on the old site of the *PEP – Prima Einkaufs Park* – and will have 19,000 sqm when it opens in early-2016.

Lagging behind, but also in the pipeline, are further FOCs in Remscheid and Duisburg, with restricted planning permission granted for Grafschaft, Königswinter (near Bonn) and Werl. The CBRE study highlights how Germany's highly restrictive planning and zoning policies for large-area retail developments outside of town centres, backed up by heavy resistance from local retail interests.

According to **Jan Linsin**, head of research at CBRE in Germany, "It can take up to ten years to realise an FOC project, and the entire process is ridden with uncertainties as to the likelihood of the project going ahead." Hence it's highly improbable that Germany can make up much ground on the UK, for example, which has 39 such centres.

Linsin's colleague **Jan Dirk Poppinga,** the head of retail investment at CBRE Deutschland, emphasises the attractive yields in the FOC segment for investors, which are well above other returns on retail categories such as shopping centres or "*Fachmarktzentren*", specialist neighbourhood malls. Recent yields on transacted FOC deals in Europe are put at between 6.5% and 10%, depending on location and perceived quality.

The attractions of the German market are that, where planning permission IS granted, restrictive German zoning laws will ensure that another such centre is unlikely to appear as a nearby competitor, thus heightening the attractiveness for investors of those centres that ARE approved.

Just this week the Düsseldforf-based project developer **Clees Unternehmungsgruppe** presented plans for what will be Germany's biggest factory outlet in Wuppertal, in Germany's most populous state of North Rhine-Westphalia.

The FOC Wuppertal, with an initial project investment of €120m, is expected to open its first 10,000 sqm sales area in 2017, with at first 65 shops. A further 13,000 sqm of lettable space is to follow, and by 2019 the centre should have 30,000 sqm with 150 outlets, making it Germany's largest FOC. The entire centre is planned for the downtown Döppersberg district, connecting the old local **Bundesbahn** headquarters with the old central **post office** building under a new bridged and roof design. **ROS Retail Outlet Shopping** will be the centre manager.

...see page 12

Guest Column:

Strong economic data disguise increasing problems

Prof. Dr. Tobias Just, Regensburg University and IREBS Real Estate Academy

The German economy has recently been sending some positive signals despite the weak economy in Southern Europe. The ifo Business Climate Index has improved continuously from October 2014 to April – and remained more or less stable in May 2015.

In particular, the business situation was positively assessed by respondent companies. Even the companies' outlook for the near future has improved irrespective of the continued uncertainties surrounding Greece. In May this year, the Federal Government as well as the EU Commission set their growth forecast at almost 2% for 2015 and 2016.

The German Council of Economic Experts, sometimes referred to as the "five wise men" – together with leading economic research institutes - have produced similar estimates for the current year and part of next year.

Real estate demand is of course dependent on the performance of the economy overall and it could be concluded that the upswing in the German real estate market will continue for at least two years. Critics may point out that caution is advised when there is consensus among economic researchers, as forecasting cycles exist in addition to economic cycles.

These critics could also argue that demand for real estate boomed, particularly on the investment side and in the years of great uncertainty, as risk-adverse investors sought a safe haven in real estate. Considering this positive perception of the economic climate, shouldn't investment be moving towards more opportunistic vehicles?

Firstly, the question arises: what exactly is a more opportunistic type of investment? Stocks soared from one historical peak to the next. The DAX still stands at 50% above its highest value in 2006, despite a decline of 1,000 points. This certainly promises a more opportunistic style of investment, even when one considers that the increasing dividends partly explain this rally. Simultaneously, debate surrounding a possible real estate bubble in Germany continues.

Indeed, the decline in yields on German apartments is considerable: since 2009 rental yields for new-build apartments in German cities fell by almost 50 basis points (0.5% points), in some cities such as Munich or Mainz by even more than 80 basis points.

During the same period, however, German 10-year government bond yields fell temporarily by 400 basis points to almost zero per cent. Even if bond yields have recently recovered slightly, long-term German government bond yields remain only marginally above zero per cent.

This makes prime yields for Munich apartments appear a very reasonable deal, doesn't it? In short: share prices have lost substantial ground, but remain at almost 50% of their peak value during the last cycle. The yields for long-term government bonds saw gains of almost 40 basis points in a few days and are now reaching an implicit multiple of 200.

For short-term government bonds investors still accept negative yields. And yet, we are primarily concerned about a real estate bubble, which seems a little strange.

To avoid any misunderstanding: the pricing for many real estate investments is alarmingly aggressive. Sooner or later there will be losers. In the end real estate cycles always follow the same pattern: demand increases and as a consequence so do rents and prices, which prompts developers into action and then due to the time-lag supply reaches the markets too late, namely when demand has passed its cyclical peak. Then rents and prices begin to sink again.

This can be expected for the near future again and absolutely no bubble needs to burst; it would be a 'very normal' real estate cycle. Rising interest rates could accelerate this process.

However, the most concerning fact is that many conservative real estate investors are not driven by a desire to gamble, but rather a lack of investment alternatives. The search for a satisfying yield is leading more investors towards increasingly opportunistic real estate investments (including developments), which, according to the real estate cycle model outlined above, is not favourable in the mid-term.

What is more, as the government has restricted residential rent increases, the options for conservative investors have been eroded further and unnecessarily.

Following the positive growth forecasts, two further challenges need to be digested this year, which have so far not been sufficiently considered in the real estate sector:

1) On the one hand, the yields for Greek government bonds have recently doubled. They previously were at the level of a secondary residential location in a prime city and are now again two-digit. Whoever believed that in 2014 the investment risk for Greek bonds was similar to a residential investment in Frankfurt, would have been seriously disappointed.

We have now become accustomed to the fluctuations of Greek government bonds. It is truly remarkable that negative financial news from Greece exerted almost no impact on Spanish, Italian and Portuguese bonds, as had occurred two or three years previously. Portuguese government bonds were most recently listed at 2.4% i.e. around half the level of German 10-year bonds in 2008. The capital markets evidently regard the contagion risk factor as negligible.

This is exactly what makes a Grexit or a Graccident far more likely today than in 2012 as the Minimax strategy – the minimisation of maximum risk – in Europe might now lie in the management of a Grexit. Previously, this had been almost impossible due to the contagion risk factor.

Then, the upward pressure on the euro would increase (indeed the euro did appreciate again moderately) and this would reduce the growth momentum as well as the scope for rising commercial real estate rents. However, this development is less a result of an expected Grexit than the second, additional risk factor.

2) On the other hand, the latest economic news for China and the US does not suggest sustained growth. A delay in the interest rate turnaround is being discussed again in the US although this matter was previously considered to be settled.

At the same time, the Chinese government has relaxed the laws for acquiring second and third homes, evidently as a measure to stimulate the construction and real estate sector. A measure that was unlikely to have been taken as a result of strong domestic economic sentiment.

When the locomotives of the two most important global economies are not moving full steam ahead, this is not good news for Germany, a train wagon dependent on exports.

In conclusion, three aspects are important for the next 18 months: firstly, the benign economic growth forecast for Germany is far from a guarantee. Significant uncertainties remain, bad news for those that have based their purchase considerations on aggressive rental growth in the future.

Secondly, a Grexit is more likely today than two years ago; a 'Grapocalypse' has certainly become less likely than in 2012 as other Southern European countries are currently considered less of a contagion risk than three years previously.

At second glance, this good news is not necessarily positive for real estate investors as the argument for secure investment has been somewhat eroded compared to other asset classes. Moreover, the question arises whether the investment risk in Portugal or Italy really is as small as government bond prices suggest.

Thirdly, there are arguably excesses in European real estate markets, however, compared to the excess in bond markets this is a 'lesser evil' for investors. At present, real estate investors must give careful consideration and certainly need to be more patient than three or four years previously.

Still, subsequent quarters should prove positive for real estate markets. However, the better they perform, the stronger the downward correction could later prove to be.

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Germany/Listed Companies

Patrizia absorbs new 14,000-unit residential fund

The listed Augsburg-based **Patrizia Immobilien AG** has swooped again to pick up a major residential portfolio, this time persuading a group of Swedish and Norwegian investors in an off-market transaction to accept its offer for a 14,000-unit portfolio, with 13,500 of the units in Germany and the rest in Sweden. The value of the portfolio is put at €900m.

Patrizia submitted a takeover bid on April 15th to the nearly 8,400 fund owners from Norway and Sweden. By 18th May, at least 83.1% of the Norwegian and 52.5% of the Swedish fund owners had accepted the offer.

The apartment portfolio was previously held by the Swedish fund **Hyresbostäder i Sverige III Gul AB**. The fund is owned 67.4% by Norwegian group **Boligutleie Holding III AS**, while 32.6% is still owned by the Swedish Hyresfastigheter Holding III Gul AB. The Scandinavian real estate fund was established in 2005 and was most recently managed by the Oslo-based **Obligo Investment Management AS** company.

According to **Wolfgang Egger**, CEO and founder of Patrizia, "There was great willingness among the fund owners to part with their units. We submitted an extremely fair offer for them… This off-market transaction demonstrates that, with its pan-European positioning, Patrizia is capable of seeking out attractive real estate investments not only through established channels."

On the basis of 100% of equity, the gross asset value is about €900 million. Once the fund has been completely taken over and dissolved, Patrizia said it plans to offer the residential portfolio to its customers and third parties as a potential investment.

In addition to Berlin, where alone more than 5,000 apartments are located, the portfolio holdings cover Munich, Stuttgart, Frankfurt, Cologne, Dusseldorf and Hamburg, as well as several regional capitals and urban areas across western Germany. The portfolio also includes holdings of 500 residential units in Umea, in Sweden.. The residential portfolio is described as being "in good technical condition", with a vacancy rate of less than 4%.

Launch of €600m domestic fund

Separately, Patrizia has also raised €300m in equity commitments for a new domestic commercial property fund with target investment of €600m, and also said it aims to raise full-year operating earnings by 10% from the €50m generated in 2014.

In first quarter, Patrizia collected €300m equity for the **Patrizia Gewerbeimmobilien Deutschland II** fund with target volume of €600m, and also set up the **Patrizia Nordic Cities** fund for two investors, which will hold 10 commercial assets in Denmark as seed assets.

The company has come a long way from the dark days of the credit crisis, when it struggle to refinance the long term lending on its much simpler business model, of being essentially a regional opportunistic trader of residential housing, mainly in its Bavarian heartland.

"Patrizia today is in the position to seek out attractive investment opportunities in the individual European real estate markets for its investors," said CEO Egger in a release. "That applies to the various types of use across all stages of the value chain in all phases of the real estate life cycle."

In an interim release Patrizia said it has raised total assets under management by €900m to €15.5bn and started with a solid first quarter, even though operating earnings fell to €7.5m from €16m in 1Q14 - which included the €1bn Leo I portfolio of mainly government and municipal buildings acquired from the State of Hesse. "We are continuing to view the future with the utmost confidence - and not just for the current year," said Egger. "Even without the tailwind of low interest rates, real estate con- tinues to be an essential

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component of institutional investors' portfolios." He confirmed the full-year forecast of raising earnings by 10%.

Through its diversification strategy, 28% of Patrizia's managed real estate is now located outside Germany. The firm's recently-established subsidiary in Madrid to explore opportunities mainly in residential in Iberia, followed local offices set up in the last two years in Scandinavia, France, UK and the Netherlands. It also co-invested in Ireland for the first time, and was further in the news last week when it partnered as asset manager with Taiwanese insurance company **Fubon Life** to buy the popular tourist attraction **Madame Tussauds** for £332.5m sterling.

Germany/Listed Companies

Deutsche Wohnen AG raises €900m in new rights issue

Germany's second-biggest residential housing company **Deutsche Wohnen** raised gross proceeds of €907m this week in a new rights issue. Shareholders were offered one new share for every seven they hold, at a price of €21.50 (the current traded price is about €22.15). The cash capital increase was the largest ever in the German real estate industry.

The proceeds are expected to be used to buy a further 6,500 residential units, mostly in the Marzahn district of Berlin, Deutsche Wohnen said recently. The new portfolio generates an annual net rent roll of €25.6m, and currently has a vacancy rate of 2.6%. It is expected to make an annual EBITDA contribution of more than €20m. Buying it will require about €500m, and will bring the company's residential holdings up to more than 155,000 units.

The company is trying to bring its overall leverage ratio down to below 45% from its current 50.4%, largely by turning over bank loans and possibly issuing new 10-year bonds, and needs to refinance €1.2bn of loans due in 2018 and 2019, while bringing its average interest rate down below 2%, as against the 3.4% being paid now. A further €0.3bn with likewise higher interest costs are to be repaid from the company's cash holdings.

According to Deutsche Wohnen's board member and finance director **Andreas Segal**, the plan is for further buying of residential portfolios in Berlin, which along with the Rhine-Main area around Frankfurt, represents the company's major heartland, particularly after the acquisition of Berlin group **GSW Immobilien** with its 60,000 units some years ago. "In addition, we see attractive opportunities in the market to continue our growth strategy .. and will use a part of the proceeds from the capital increase for value enhancing growth. In addition, we will further optimise our capi- tal structure with the capital increase and envisaged refinancing, and at the same time strengthen our FFO and cash-flow profile from 2015 onwards."

Deutsche Wohnen saw its FFO rise in the first quarter by 21% to €71m, and its EPRA net asset value rise to €18.83 per share, up from €18.61 the previous quarter, thanks to higher rental income and lower vacancies, along with selected disposals. Just last month the company allowed its €1.2bn takeover bid for Austrian rival **conwert Immobilien** to lapse at €11.50 offered per share, when insufficient conwert shareholders agreed to the bid price.

Germany/IPOs

Berlin specialist Ado Properties in €400m IPO this year

The Berlin-based **Ado Properties SA**, a value-add residential real estate investor focused on the German capital, plans to raise at least €400m in an initial public offering this year.

Ado, whose parent company **Ado Group Ltd**. is already traded in Tel Aviv, will sell shares on the Prime Standard of the Frankfurt exchange, Ado said, pitching itself as a pure-play Berlin specialist. The company owns about 13,700 homes and 700 commercial properties in Berlin valued at €1.2bn, following a recent major buy of 5,750 further residential units from **Deutsche Wohnen** for €375m.

Demand for German property stocks is rising as investors seek to take advantage of increasing home values in Europe's largest economy. Berlin apartment prices have climbed almost 50% in three years, while rents have gained more than 30%, according to data from property advisers **JLL**.

According to **Shlomo Zohar**, executive vice chairman of the parent group in Israel, Ado Group and its major shareholder **Shikun & Binui** remain "committed as long-term strategic investors" in Ado Properties after supporting the Berlin entity over the past decade. "Markets are

very supportive," he said. "It's a good opportunity to raise funds to support and expand the business."

The IPO will be managed by **Kempen & Co. NV** and **UBS Group**, with **Barclays** and **Commerzbank** mandated as additional joint bookrunners, along with **Arbireo Capital** as process manager and sole financial adviser in the transaction. The flotation will include the sale of existing Ado Group shares and the issuing of new stock. Proceeds will be targeted at further properties in Berlin and to upgrade existing homes.

Ado Properties, which was previously known as **Swallowbird Trading**, said it has a conservative balance sheet consisting mainly of mortgage backed loans with an average cost of debt of 2.6%, no major maturities until 2018 and a weighted average maturity of six years.

Rabin Savion, Ado Properties CEO, said the company strategy was to create value through targeted investment in its portfolio, privatisations and accretive acquisitions. "We aim to approximately double the number of units over the next few years to generate value for our shareholders, capitalize on our existing platform and further enhance the efficiency of our operations."

At the end of March this year Ado Properties had an overall loan-to-value ratio of 57%, which it targets reducing to below 50% after the IPO. Savion commented that "Our conservative capital structure allows for predictable growth, supporting attractive and continuous dividends whilst ensuring that our indebtedness does not restrict our business or strategy."

Germany/Residential real estate

LEG buys 700 units from Benson Elliot's Speymill stock

Benson Elliot, the UK-based private equity real estate fund manager, said it sold 700 units from its German residential portfolio to German listed investor **LEG Immobilien**, at a rental yield of 6.8%.

The properties sold to LEG are all located in North-Rhine Westphalia, as are all the properties owned by the former municipally-owned LEG prior to its successful flotation threee years ago.

The properties make up part of the Tor portfolio of the now defunct **Speymill Deutsche Immobilien plc**, which originally encompassed more than 3,000 residential and commercial units across 80 multi-family properties throughout Germany, but mainly in Berlin, Frankfurt, Munich, Hamburg and Cologne.

The Speymill portfolio, which secured a €187m loan, was bought by Benson Elliot out of an Isle-of-Man receivership in 2012, in a process directed by special servicer **Hatfield Philips International** and receiver **Ernst & Young**, in conjunction with the borrower.

Benson Elliot's purchase of the Tor portfolio represented one of the first defaulted CMBS portfolio loans to be resolved in the aftermath of the global financial crisis.

Since acquisition, Benson Elliot and joint venture partner **Wertgrund Immo-**

bilien have undertaken a number of asset management initiatives including the implementation of a capex programme, raising the occupancy rate across the portfolio from 90% to 97% and signing more than 1,000 new leases.

Following this latest disposal, Benson Elliot said it has realised well over €200m of disposal proceeds from the Tor investment, exiting 69 of the original 80 assets and distributing investors more than 150% of invested capital.

'We have seen strong income and capital growth across the Tor portfolio since we acquired it some three years ago,' said **Georg Strassner**, principal and co-head of Germany at Benson Elliot. 'We were confident at the time of purchase that quality residential assets like these – once stabilised – would prove attractive to buyers seeking reliable income in a low interest rate environment. We'll look to wind down the remaining assets in the near term, crystallising the remaining value.'

Meanwhle, the listed LEG Immobilien raised first quarter FFO by 25% to €51m mainly due to rental and portfolio growth. It expects €195m-€200m FFO for 2015 without taking into account further acquisitions.

The company boosted rental income by 13.8% to €107m in the first three months, due to a larger portfolio as well as like-for-like rental growth of 2.5% per sqm. Its **EPRA** vacancy remained stable at 3.2% but it aims to raise occupancy to at least 97.2% by year-end. So far this year, the firm has bought 800 residential units and is close to signing on another 2,500 - on track to achieving its stated acquisitions target of at least 5,000 units this year.

According to CEO **Thomas Hegel,** "The organic rental growth proves our operating strength and the value-oriented expansion of our portfolio is progressing. We intend to consistently pursue this value-generating growth strategy in the future." LEG now holds about 110,000 apartments across North Rhine-Westphalia.

Germany/Research

2015 to see further strong year in resi portfolio sales

Some 304,000 German apartments were traded in portfolio transactions of over 800 units last year, the same strong level as in 2013, says the **BBSR** specialist federal institute. It expects another strong year for 2015.

In a new report, BBSR **(Bundesinstitut für Bau-, Stadt- und Raumforschung)** said German residential market activity should continue strong, driven by M&A activity in first half. The largest deal was **Deutsche Annington** taking over listed peer, the Essen-based **Gagfah** for €3.9bn, creating the largest European listed housing firm, with 350,000 residential units.

Adler Real Estate, managing 31,000 flats, has also issued a takeover bid for 20,000-unit **Westgrund**, valuing the latter at €350m. It noted that a significant overlap in the shareholder structure is facilitating the transactions.

In last year's first half, their German housing market activity was characterised by financial investors exiting holdings via the stock exchange; the US private equity group **Fortress Investment** sold 28% of **Gagfah**, while UK private equity group T**erra Firma** shed 13% of Deutsche Annington. The largest deal in the second half was Westgrund buying 13,300-unit **berlinovo** for €390m from the Berlin city-state.

Property consultancy **Dr Lübke & Kelber** in Frankfurt expects turnover of residential deals this year to "probably surpass the 2007 record with approximately €15bn". The prediction is based on a "strong start to the year with €10.6bn invested in the first quarter alone into the German multi-family market" – 80% more than in Q1 2014.

The forecast does not include the planned takeover of Berliner Westgrund by Adler Real Estate. **Ulrich Jacke**, (*pictured, below*),managing partner of Dr Lübke & Kelber, says this further consolidation, together with high prices and ongoing low interest rates, "supports his opinion" on the new record transaction level.

Overall, BBSR registered 48 large portfolio sales last year in total, down from 51 in 2013. Private companies were responsible for 87% of sales and 96% of acquisitions. Communal housing firms remain net sellers, though some are now back on an expansion course, especially in Berlin.

REFIRE: *The BBSR's conclusions about likely residential market activity in Germany have been underpinned by a fundamental shift in perception about the nature of residential portfolio investment. If ten years ago investors avoided residential, in favour of office or retail real estate, it was largely because yields were seen as too low and management costs too high and too troublesome.*

But with office yields having fallen by about 100 basis points over the last ten years to about 4.5% in Frankfurt, the contrast between residential and commercial is no longer as stark, while with large-scale migration into Germany's employment-offering big cities, investors' understanding of the risk profile of residential investments has changed.

Hundreds more institutional products are now available on the market to enable investors take advantage of the more 'bond-like' character of residential, including the spreading of risk and avoidance of exposure to the loss of one significant tenant. Such 'lumpen-risk' is a common feature of office investment, with its sudden unwanted vacancies.

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In most of Germany's big cities, new construction is still lagging demand for residential housing – Frankfurt and Berlin by at least 8,500 apartments a year, with Munich at 5,400 a year and Hamburg a 2,100 units, according to research from Aberdeen Investments. The shortage of affordable rented mult-family housing in the towns and cities where people want to live is not going to disappear overnight.

Germany/Project Development

Project developments in big German cities rise 12%

Investment in project developments planned between 2012-2019 in the top seven German cities has grown by 12% from last year to €112bn buoyed by rising rents, prices and larger space volumes, says Berlin-based research firm **BulwienGesa**. (The research group produce an annual rolling study covering a seven year period – last year's study covered 2011-2018).

Total development space rose by 7% to 25.54 million sqm., bulwiengesa found in its analysis of the 3,440 property projects currently in planning and building stages in the seven largest cities (Berlin, Munich, Hamburg, Düsseldorf, Cologne, Frankfurt and Stuttgart.

The total volume of new project development has increased continually over the past three years and now reached a record 11 million sqm. According to BulwienGesa board member **Andreas Schulten**, (*pictured, next page*) "Due to the consistently low interest rates in the Eurozone, more private and institutional capital in the billions is flooding into the German property market, which has been has been fuelling price growth in the past years. The market is stretched, with high demand, rising competition and plot prices rising exponentially."

Guest Column:
Matthias Domke, Project Director, VALTEQ Gesellschaft mbH

Potential for energy savings – Lost in the Bermuda triangle of non-accountability

www.valteq.de

The following situation frequently crops up in my advisory practice: Buildings and technical installations are "state of the art"; operating expenses however are anything but ideal in terms of energy use. Potential energy savings of 10% of the overall operating expenses and more are not uncommon to be identified. This does not involve any high-cost measures, but rather performance optimisation and "quick wins": system running periods, demand-orientated air-flow volumes, simultaneous heating and cooling. These issues apply to pretty much every commercial property – the higher the standard of equipment, the greater potential savings.

So, that's the good news – what is the problem?
All too often, exploitation of these potential energy savings falls by the wayside – lost in a Bermuda triangle of responsibilities: The owner is not expected to show any passion in this regard; he simply passes the energy costs onto his tenants as part of the service charges. The tenant, on the other hand, has no access to the energy-related technical systems, as their operation (on behalf of the owner) was awarded to an FM provider. And the FM provider? Although it sits at the decisive set-screws, it only has limited motivation to optimise any settings, because it is just on top and not paid.

What is to be done then?
The **contract design for building management** offers starting points. The project experience gained by VALTEQ shows that FM contract models with performance-based components and appropriate incentive systems are indeed possible. The service provider's participation in the savings achieved – as part of a gain sharing model – creates the conditions required for raising potential energy savings in the first place.
In doing so, all parties must change their attitudes. The owner benefits from an improved image and introduces a readiness to actively tackle the issue of energy use. The tenant enjoys the benefit of reduced energy costs, on condition that a part of the generated saving is shared with the FM provider. The FM provider is given an incentive to establish an ongoing process of improving systems operation.

The key issue is **energy audits**: By obligating larger companies (non-SMEs) to execute energy audits by the end of the year, the legislator – tardily, by the way – has implemented EU energy efficiency directive into national law. In fact, within the framework of energy audits, VALTEQ has already identified potential savings of up to 0.70 EUR/m²/month. In this regard, the issues that always prove to be significant are those at the aforementioned intersection of the user, owner and FM provider. So, why not then take the forthcoming energy audits as a cue to look beyond the scope of one's own responsibility, work together with the other parties and together implement the identified savings – to the mutual benefit of the owner, tenant and service provider?

He added, “Although we have a very overheated market, but we don’t see any danger of any bubble bursting in the A-cities”. Or at least not as developer do not forget that the key drivers of their industry is not the investment market, but new leases. “Every successful project needs to have a real chance of finding a good tenant. Yield isn’t produced on completion, but through a lease agreement.”

And that preferably in the residential sector. Most growth was seen occurring in residential, which was responsible for 80% of total space volume. Berlin headed the list for the most activity. “The city’s lead will not be challenged in the future,” said project head **Ellen Heinrich**.

In the office segment, Frankfurt and Düsseldorf registered the highest space growth by 16%, followed by 11% in Berlin. Stuttgart and Hamburg lost 6% and 8% volume compared to last year, with Stuttgart continuing a three-year fall, while completion of a large project in Hamburg was postponed to after 2019.

The ranking list of Germany’s top developers also has a new Number 1 – The Bremen-headquartered **Zech Group** has displaced long-time leader **Hochtief** from the top spot. Zech and its subsidiaries including the Cologne-based **Art-Invest**, **Die Developer** and **Die Wohnkompanie** booked a turnover of 725,000 sqm, up 31% on last year. In second place is Hochtief with 589,000 sqm, followed by pure residential developer **NCC** with 536,000 sqm.

Zech Group leads the table also for office developments with 368,000 sqm, followed by Hochtief (317,000 sqm), and then **CA Immo** (232,000 sqm). In the much more granular retail development sector, the leader is Berlin’s **High Gain House Investment** (196,000), followed by the Zech Group with 66,000 sqm and **Bayerische Hausbau** (58,000 sqm).

Germany’s Top 10 Project Developers:

1. **Zech Group**
2. **Hochtief**
3. **NCC**
4. **CA Immo**
5. **CG Gruppe**
6. **Bayerische Hausbau**
7. **Wilma Wohnbau**
8. **Baywobau**
9. **Strabag**
10. **BPD**

CORPUS SIREO
ASSET MANAGEMENT RETAIL

FROM SPECIALIST STORE TO SHOWROOM FOR ONLINE TRADING

Author:

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Online must enter the High Street

Stores do not have it easy nowadays. They try to present their products to customers in an attractive manner, provide extensive advice, only for the customers to go home and sit in front of the computer in order to by a product cheaper online, after previously clicking through various comparison sites. This could be the death knell for specialist retailers in the nearby shopping centre if they do not adapt to meet the challenges posed by the new customer behaviour.

At present it is assumed that only seven percent of all purchases are handled online, but the trend is rising. Because customers are becoming increasingly connected instore, mobile and online, stores will also have to become multi-channel. This is still a vision of the future, although a pilot project initiated by ebay has shown the direction which might be taken: In the Westfield San Francisco Centre, the visitors were confronted with „digital store fronts“ instead of conventional display windows; these fronts functioned as giant touch-screens on which visitors were able to tap and slide their way through a range of 100 products and the related product information. Without entering the store, they were able to place orders by means of text messages. The products were then delivered to their home. This is an idea with a promising future which extends the analogue process of purchasing in a shopping centre to include a digital and also diversified component.

Buying or shopping?

The buying process focuses on specific demand for a specific product. Most of us are under time pressure. On the other hand, shopping is a leisure pursuit which, if the wishes of retailers are met, ends in impulse buying. Also in purchases of products which shoppers probably originally did not even intend to consider. The trend of simply meandering for fun through shopping centres is not new; however, it is becoming more and more prevalent. Retailers will have to come to terms with this aspect by creating diversified purchasing worlds which communicate the idea of an event. This also includes glamorous presentation of the products. Some retailers have already started to present their store as a showroom or a gallery rather than a place in which the primary function is to sell something. In the store, the customer is able to inspect, touch and try on the product. This haptic experience cannot be provided by the internet, and is the major added value of analogue retailing. The profane remainder, namely paying for and transporting

the products home, is outsourced.

Not only a retailer, but also a service provider
In addition to the normal service, retailers nowadays have to consider various ideas in order to retain their customers. This is because customers are nowadays more informed and because internet searches mean that they now have knowledge which previously was the exclusive preserve of the retailer.

One opportunity for the retailer is to focus on the individual needs of each customer and to surprise the customer by the fact that his wishes and preferences are already known. Good hotels have already been working with this customer loyalty instrument for a long time. How does this work? The main criteria are still the discussion with the customer - as well as a good memory and increasingly in-store analysis. But be careful, data protection and privacy are extremely important, and negligence must be avoided at all cost.

One final word: Customising, i.e. the process of individually adapting a product from mass production to the specific needs of each individual customer, is constantly becoming easier as a result of new production methods. And this is where the retailer can become a service provider who is in demand, who provides advice and who can be engaged to provide products and services which precisely meet the customer‘s own needs.

A requiem for analogue trading is thus not appropriate. Shopping centres in particular have an excellent opportunity if they expand their strengths and skilfully integrate new purchasing habits.

For further informations please go to **www.corpussireo.com**

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Germany/Legislation

Milestone change at Germany's BaFin on debt funds

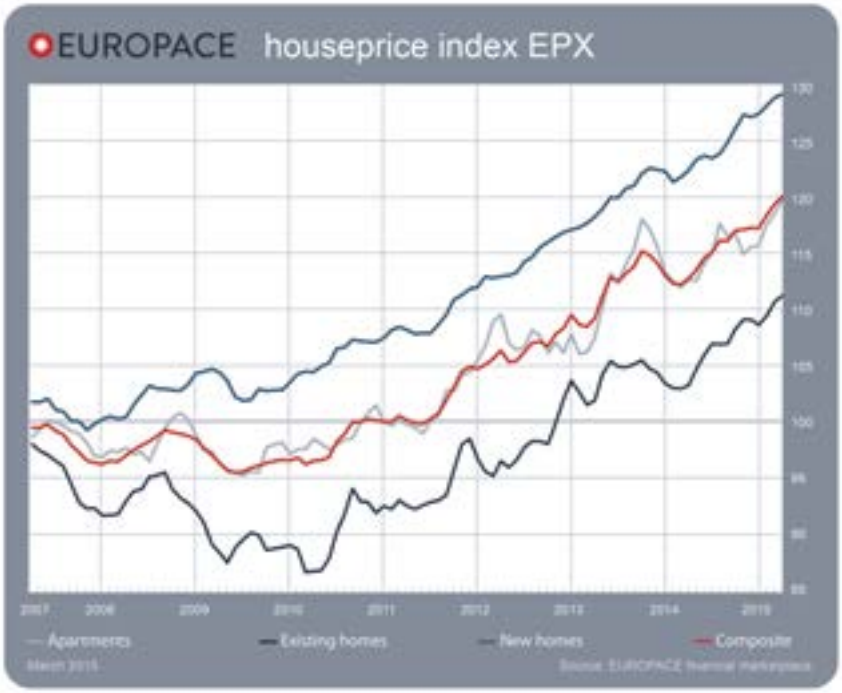
Germany's financial watchdog **BaFin** announced an important change to its treatment of investment funds and lending in Germany, particularly in relation to debt funds, and for EU and third country investment funds looking to originate, acquire or restructure German loans.

On May 12th the BaFin decided to allow loans, loan restructuring and prolongations by alternative investment funds (AIF). Lending by AIFs had been completely forbidden because of its association with the shadow banking system, and because it was considered a banking activity within the meaning of the **German Banking Act (KWG**).

Now, taking their guidance from recent statements issue by the **European Securities and Markets Authority (ESMA**), BaFin has made it clear that, according to the Investment Code (KAGB), certain – closed-ended – AIFs can grant loans directly.

Germany's **Bundesverband (Association) Alternative Investments (BAI)** called this a "paradigm change" and sees this as a solution to "hugely important problem areas" in the sector. Although investment funds have long been allowed to acquire uncertified loan receivables, the regulatory limits were quickly reached in managing them, leading to disadvantages and even losses for investors.

The new guidelines are expected to apply also to non-German AIFs wishing to originate loans to Germany entities, given the EU ban on discrimination, as long as they are subject to similar supervision and EU-AIF regulatory requirements. BaFin has issued a long list of 'recommendations' in advance of the enactment of its revised supervisory laws. The move has been widely welcomed in Germany among debt fund providers as clearing up an area of legal uncertainty that has been seen as a grey area for years.



Germany house price development

Germany/Retail real estate

Tank & Rast still up for sale, but IPO ruled out

The German autobahn service area chain **Tank & Rast**, which is jointly owned by British private equity group **Terra Firma** and Germany's **RREEF Infrastructure Funds**, is now officially up for sale for a reported €3.5bn. However, contrary to what we reported in these pages some months ago, the proposed stock market flotation as an exit for its owners is now thought to be off the table.

A report in German business daily *Handelsblatt* said the two joint owners were looking for a trade sale as early as this summer for the Bonn-headquartered service station and sanitary facilities chain, after a long and chequered history of ownership.

Up for sale is the Tank & Rast chain with 390 autobahn service areas, 350 petrol stations and 50 hotels, making it the largest service provider of its type in Germany. The group employs 600 directly, including 300 in its Bonn headquarters, and over 12,000 through its numerous franchise partners, in generating more than €3bn in annual revenues.

The **Guy Hands**-led Terra Firma bought Tank & Rast in 2004 for €1.1bn from **Lufthansa** and two funds belonging to **Apax** and **Allianz**, six years after being privatised by the German government. In 2007 the private equity group attempted to sell the chain, and ended up selling just below 50% to **Deutsche Bank**'s alternative investments subsidiary RREEF.

The group was forced to take on hefty debt during the financial crisis, and ended up issuing very high-priced bonds to service its €2.1bn debt, including some which are committed to paying interest of up to 6.75%. The sticky nature of these commitments have made the consortium's financial prospects more difficult, so much so that the mooted IPO is no longer feasible, according to **JP Morgan** and **Deutsche Bank**, who are advising on the deal.

According to the report, other potential suitors have also been turned of by the group's liabilities. However, four bidding groups are said to be negotiating with the group – a consortium of insurer **Allianz**, Canadian infrastructure group **Borealis**, the **Abu Dhabi Investment Authority**, and **MEAG**, an investment subsidiary of insurer **Munich Re**. Also in the frame are two groups assembled by Australian banking group **Macquarie**, along with the Singapore wealth fund **GIC**, and the **Ontario Teachers Pension Fund**.

All bids so far are thought to have come in at under €3bn, while the owners are looking for €3.5bn. Although Tank & Rast is expecting to boost operating profit from €235m to €405m this year, it looks as if they may have to make concessions on their target price.

Germany/Study

German prices rise 5%, but commercial loses momentum

German commercial and residential property prices continue on their upward path in the first quarter, rising 5% year-on-year as a whole, with particular strength coming from the housing market, according to the German Association of Pfandbrief-issuing banks **vdp**.

The vdp property price index has now reached another all-time high, using calculations based on actual transaction data.

According to the vdp's CEO **Jens Tolckmitt**, "Once again, the driver of growth is the housing market. We saw the strongest price increase, of 6.8%, in the segment for multi-family houses, which resulted from the consistently brisk demand by investors in search of suitable properties. However, prices for single-family and semi-detached houses likewise continued to advance strongly, by 5.8%, in the first quarter of 2015, whereas the price hike for condominiums was again more moderate at 2.8%.

"It appears that demand for residential property is experiencing a growing shift away from the expensive urban locations to the more affordable surrounding area, where construction is typically characterized by single-family and semi-detached houses."

The latest vdp figures show, however, that the commercial property market continues to lose momentum. The vdp commercial property sub-index rose by 2.3% year-on-year, but "investors in office and retail properties are becoming increasingly cautious in their acquisitions, and are no longer willing to pay just any price for a property, all the more as rents on commercial premises are now only showing very little growth."

The vdp figures show that, for the second quarter in succession, office rents rose only minimally (+0.2%) while the cap rate index dropped further (-1.8%), leading to a 2.0% increase in the capital value index for office properties. Nor did prices for retail premises rise as strongly as in previous quarters. The capital value index went up by 2.9%. New lease rentals in this market segment gained 0.7%, and the cap rate index shed 2.3%.

Germany/Acquisitions

More 'core' exposure for M&G in Germany after recent euro deals

M&G Real Estate fund management group, which acts as the asset manager in Europe for the giant **Prudential** insurance combine, is continuing to roll out what it calls its 'core' European property strategy by buying a major retail park just south of Frankfurt, following recent similar deals in Italy and Denmark.

The 23,000 sqm property is the well-known *Dreieich Nordpark* about 10km south of Frankfurt, positioned at the centre of a wide catchment area stretching as far down as Darmstadt. Anchor tenants are the Metro hypermarket subsidiary **REAL** and **Decathlon**, which now claims to be the world's largest sports retailer. The centre attracts more than 2.5 million shoppers a year.

The seller was **TIAA Henderson**, which had held the property in its **HERALD Henderson European Retail Property Fund**, and the price paid was €51.9m. The centre underwent a major re-branding and repositioning exercise in 2011-12.

Simon Ellis, strategy manager at M&G said, "With economic growth gaining momentum and the **European Central Bank's** quantitative easing programme lending further support to the economy and the real estate markets, we see a very positive environment for continued investment. Prime assets and prices are likely to continue to strengthen, given the limited supply. Investor appetite remains strong for core, well-leased assets of this nature."

M&G recently released a report suggesting that the European Central Bank's pump-priming policy should lead to significantly higher inflows into real estate. The ECB's quantitative easing programme to date has already helped to weaken the euro, driving it to a 12-year low against the dollar and a 7-year low against the pound sterling, with 10-year Bunds at record lows.

M&G's head of real estate research **Richard Gwilliam** draws parallels with QE phases in the US and the UK, which led to increased output, higher employment and higher private consumption, and suggests we're seeing the same thing happen in continental Europe. The weaker currency and positive structural changes to European export industries are particularly good news for rental growth in ecommerce-related real estate such as logistics and distribution hubs,

especially in economies such as Germany. "Already cheap European property is likely to be even cheaper for both non-Eurozone European countries and non-European overseas investors."

The lower yields on government bonds have added to the attractions of property, while investors are more comfortable with lower yields against a backdrop of growth in the economy and expected rental growth, said Gwilliam.

Germany/Asset Management

Prelios weighing up hive-off of €300m investment arm

The Italian-listed **Prelios** said it was looking to hive off the remainder of its investment activities as part of its strategy to reposition itself as a pure asset management group. The company (known in a previous incarnation as **Pirelli Real Estate**) has been disposing of its real estate holdings, including the €917m sale of its 18,000-unit **DGAG** German residential portfolio, jointly held with **Deutsche Asset & Wealth Management (ex-RREEF)** to listed **Buwog** last year.

In a statement, the Milan-based Prelios said, "Activities aimed at verifying the feasibility of a transaction for the spin-off of the investment activities and the service activities are continuing,"

Prelios has held several meetings about the operation, which is "progressing successfully", it added during the first-quarter result announced in mid-May. "Subject to the approval of the company's lending banks, Prelios is confident of finalising the agreements in a reasonable time, to be followed by… technical activities and operations, also including the transfer of business relating to the investment activity of a separate special purpose vehicle," the company said.

The company halved its net losses in the first quarter of the year, reporting a loss of €6.1m versus a loss of €13.4m in the same period a year before.

Revenues from the management platform – now Prelios's core business - fell to €13m from €16.9m in 2014, largely as a result of disposals and a fall in assets under management. EBIT from the management platform came in at a negative €3m compared to a loss of €1.6m in the same period a year earlier.

As part of the group's new corporate strategy, Prelios concentrates in Germany on development, transaction and management services for retail and commercial property, Prelios recently presented its plans for a new 12,000 sqm shopping centre in the northern German coastal city of Husum. The inner-city centre is built around a previous **Hertie** department store, and managing director **Martin Mörl** *(pictured)* said recently that Prelios is looking for similar-sized German towns that could profit from creative solutions with fresh impetus and contemporary tenant mixes that integrate traditional local retailers (such as **C.J. Schmidt** in Husum) at the heart of newer downtown retail developments.

Prelios manages other centres for regional investors in Hamburg Altona, Constance on the Swiss border, and Marburg in northern Hesse, along with a number of department stores in Berlin.

Germany/Acquisitions

Tristan, Freo joint venture buy landmark Cologne estate for €110m

The **EPISO 3 Opportunity Fund** managed by London-based real estate manager **Tristan Capital Partners** has bought the landmark *Barthonia Forum* mixed-use estate in Cologne for €110m in a joint venture with Luxembourg-based developer and manager **Freo**. **HSH Nordbank** is providing senior financing of €91m on the deal.

The previous owner was **Terra Heimbau**, a company associated with Tel-Aviv listed investor **Arazim Investments**, for which **Deutsche Immobilien Wirtschafts Gesellschaft (DIWG)** had been managing the asset, including renovations and new leases.

The Barthonia Forum urban quarter, in the city's Ehrenfeld district, consists of 12 buildings with 70,000 sqm of gross lettable area, including a shopping centre anchored by the **Kaufland** supermarket chain, an office tower, the former factory of the famous **4711** *eau de cologne,* partly converted into offices, and 200 residential apartments.

"Barthonia Forum presents an opportunity to transform an inner-city square, a short walk from the centre of Cologne, into a vibrant quarter with an attractive retail, office and residential offer thanks to great tenant demand," said Tristan managing director **Ali Otmar**. The investment gives EPISO 3 a mixture of cash-flow and value-add opportunity in retail, residential and office repositioning.

Apart from co-investing, Freo will advise the joint venture on asset management and other repositioning activities. Tristan pan- European real estate funds include core-plus and value-added/opportunistic strategies with a total of €5bn of assets under management.

Germany/Listed Companies

Shareholder merry-go-round at Austria's conwert

It's been a turbulent few months at Vienna-listed residential investor **conwert Immobilien**, and recent changes at the company are unlikely to be the last after this week's annual general meeting. The company only recently rejected an

offer by **Deutsche Wohnen** to be taken over, at a price of€11.50 per share, on the grounds that the offer price did not reflect the company's true value.

The conwert share price has risen above that level since then, currently trading at about €12.35, but this will have as much to do with a new shareholding structure since the majority of shareholders rejected the Deutsche Wohnen offer. Major shareholder **Hans Peter Haselsteiner**, who was in favour of the merger with Deutsche Wohnen, has now sold his family's stake of 24.79% to **Mountain Peak Trading Ltd**, a company whose beneficial owner is London-based Israeli billionaire **Teddy Sagi**.

Former **Strabag** boss Haselsteiner's 21.2 million shares would have had a market value of €240m based on the company's market cap of €973m, and Sagi now becomes the company's largest single shareholder. Sagi is the founder of gambling company **Playtech**, owner of London's **Camden Market**, which he floated in 2006. **Camden Market Holdings**, which owns Camden Market, **Stables Market** and **Camden Lock Developments**, was bought by Sagi in March 2014 for $664m. He has continued to buy property in the surrounding area.

Conwert's administrative board also sacked previous CEO **Clemens Schneider,** who had opposed the Deutsche Wohnen takeover, with CFO Thomas Doll taking over the top job on an interim basis.

New shareholder Sagi has wasted no time in issuing diktats for conwert's future strategy. In a statement he urged more "value creation from its higher valued residential buildings through unit sales" and "resolute lease-up and reconstitution of conwert's commercial to create a more valuable commercial portfolio." Sagi said the company "has to capture value uplift through targeting higher gains on sales over current market value, rather than increasing arithmetic NAV calculations through manipulation of valuations."

Reports suggest that Sagi is keen to place **Ben Lehrecke** in as the new CEO of conwert, to replace Schneider. Lehrecke is the CEO of **Vitus-Gruppe**, which was absorbed last year by **Deutsche Annington** (now known as **Vonovia**). Sagi is also thought to want to replace supervisory board chair **Kerstin Gelbermann** and board member **Alexander Tavakol** with UK-based real estate veterans **Barry Gilbertson** and **Maureen Harris**.

...from page 25

Germany/Acquisitions

Hansteen buy further 13 industrial properties for €22m

UK-based REIT Hansteen Holdings plc has exchanged contracts on the acquisition of 13 multi-let and single-let industrial properties located in established commercial zones across Germany. The seller was the Internos-managed fund Benelux Industrial Partners, with Hansteen paying a total of €21.65 million, inclusive of costs. The deal is expected to close this month.

The properties include a total lettable area of 99,355 sqm, of which 18,172 sqm (18.29%) is currently vacant. The properties generate a combined passing rent roll of €2.78m per annum from 66 tenants, reflecting an initial yield of 12.86%, with an unexpired weighted average lease term of 1.13 years. At full occupancy the portfolio is expected to produce a rent roll of more than €3.46 million per annum. Ten of the properties are in North Rhine-Westphalia with three others in Eichenzell, Bingen and Hann Muenden.

Commenting on the deal, Ian Watson, Hansteen's joint CEO, said, "This is exactly the sort of purchase Hansteen loves. It will be hard work and require some capital expenditure but the portfolio has a high yield and real capital upside." Hansteen's normal modus operandi is to invest in properties with high yields, low capital costs and upside asset management potential. Main markets are Germany, the UK, the Netherlands, Belgium and France, where it owns properties worth €1.6bn.

The deal comes two weeks after Hansteen sold its Hansteen UK Industrial Property Unit Trust II, comprising 76 assets across England, Wales and Scotland, for £192m pounds (€268m). The FTSE 250-listed Hansteen was founded ten years ago on the AIM market by joint CEOs Ian Watson and Morgan Jones, and moved to the main market when it became a REIT in 2009.

Germany/Listed companies

New London listing for Phoenix Spree Deutschland

UK-based investment company **Phoenix Spree Deutschland Ltd** plans to take advantage of ongoing investor enthusiasm for the Berlin residential market by

floating on the main market of the London Stock Exchange, with its initial listing scheduled for June 9th.

Phoenix Spree Deutschland is part of **PMM Partners**, founded in 2006 by a group of ex-**UBS** bankers who raised about €90m at the time to invest in – mainly- Berlin. The price of the float, which is being sole sponsored by **Liberum Capital**, will be based on the company's net asset value, which was €144m at 31st December 2014.

The Jersey-incorporated closed-ended fund currently holds 114 assets in Berlin, along with Hannover, Bremen and Nüremberg with a gross value of €245.3m and yielding 4.1%. the bulk of the portfolio (82%) is residential, with the rest being garages, parking lots and commercial properties. Borrowings are currently 39%.

According to Phoenix Spree founding partner **Mike Hilton**, no new money is being raised in the IPO as none is required. The float will enable several early investors to exit, said Hilton, adding "There is quite a lot of corporate activity around the German residential property market, and from our perspective, the timing is very good to look to institutional investors to fund further growth."

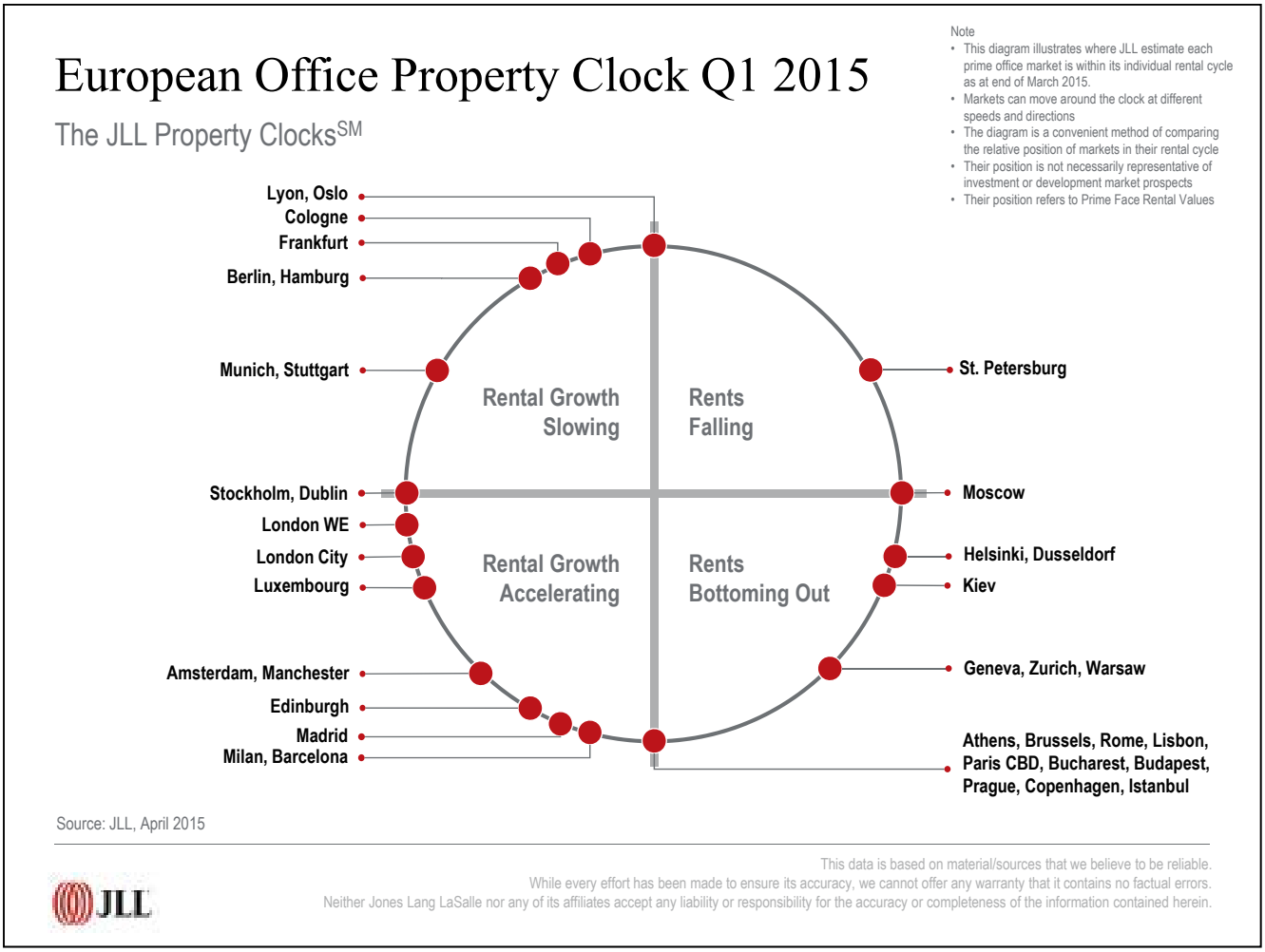
Hilton says he remains bullish on Berlin because of constrained supply. "Although new-build property is coming on, there isn't anything like enough of it. Last year, 4,000 properties were built in Berlin. The demand is for 20,000."

"I can look at the buildings that the Phoenix Spree fund owns and can say they cost less than the bricks and mortar," says Hilton. "That is key. London is about momentum; it's touch and feel. Berlin is value." The fund aims to deliver annual shareholder return of 8-10%, including a 2.5% dividend yield.

Europe/Study

Best performance by non-listed property funds since 2006 - INREV

European non-listed real estate funds last year earned a record 8% total return, the best since 2006 and more than dou-



ble the 3.2% in 2013, the recently-published **INREV Annual Index** shows.

Most of the improved performance was capital growth at 4.5%, after a 0.3% decline in 2013. Income returns remained stable at 3.5%. The UK was the big outperformer with a total return of 16.7%, nearly twice its previous year's 8.6%. INREV said the index revealed a marked general uplift across continental Europe at 3.7% against 0.7% in 2013. Western Europe funds returned 11.2% while southern Europe improved to -1.1% against -6.7% the previous year.

Investors' increased appetite for risk was reflected in performance figures for value added fujnd, which reached 8.9% in 2014 as against 7.9% for core funds. The best performing sector was industrial/logistics, which returned 17.9% for the period against 9.6% for retial, 7.5% for offices and 4.6% for residential.

According to INREV's director of research **Henri Vuong**, "The mood is clearly upbeat. But while there's no sign of a bubble, the consistent rise in capital values and dwindling supply of quality real

estate assets across core markets in Europe may yet raise questions about the prospects for sustained outperformance over the longer term."

The INREV Annual Index 2015 covers the performance of European non-listed real estate funds for the full year 2014 and captures data from 303 participating funds., with performance measured by INREV's proprietary NAV calculation methodology.

Germany/Funds

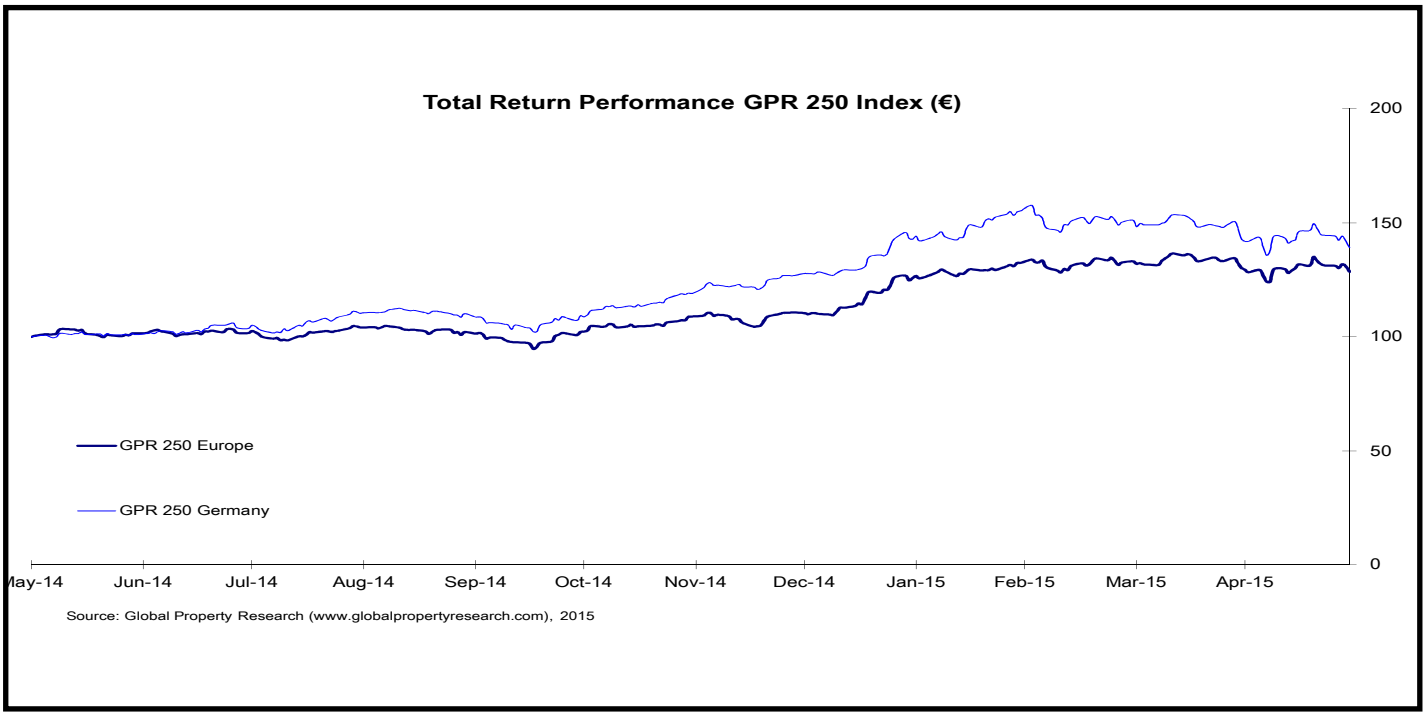
Catella launches €150m Southern Germany special fund

Catella Real Estate, the Munich-based investment manager of the Swedish financial group, has launched a new Special Fund focused on commercial real estate in southern Germany, targeting equity of €150m and a yield of 4%-5%.

The **IWS II–Wirtschaftsregionen Süddeutschland** will focus on A and B cities in Bavaria and Baden-Württemberg, with 40%-60% destined for office, 20%-40% for retail and 20%-40% for logistics assets, Catella said.. It sees good prospects for the region as the population continues to grow, economic forecasts are positive, and unemployment as well as public and private debt remain low.

The new fund follows **IWS I**, which has built a net volume of €155m since inception in December 2011. It holds 13 assets in cities such as Nuremberg, Stuttgart, Regensburg, Augsburg and Munich, which have an average 98% occupancy. The initially planned equity has been raised twice as investors raised commitments. "Thanks to the positive development of IWS I, we are confident of meeting our forecasts for the successor fund IWS II," said Catella board member **Henrik Fillibeck**. "The high demand from investors shows how popular property as an investment product currently is."

Catella Real Estate, founded in 2007, manages property worth over €2bn. Stockholm-based listed Catella Group



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

Charts courtesy of GPR Global Property Research

specialises in real estate investment banking, financial services and asset management across 12 European countries.

Germany/Retail real estate

Israeli group Optibase buys €29m German supermarket portfolio

A new arrival onto the German market is the Israeli group **Optibase**, an unlikely-sounding real estate company that was previously engaged in the field of digital technologies until selling out its core business five years ago. Since then it has been investing in fixed-income real estate, primarily in Switzerland and the USA.

The NASDAQ and Tel Aviv-listed company is now dipping its toe into the German market, and its wholly-owned German subsidiary **Optibase Bavaria GmbH** has just closed on the purchases of 25 supermarkets in Bavaria from an unnamed seller for €24m. The deal was first flagged in December of last year.

Optibase said it financed the deal partly with a loan from German bank **DG Hyp** of €15.25m for a five-year term. The company has contracted to buy a further two supermarkets to complete the portfolio for a further €5.75m, also to be partly financed by DG Hyp.

According to Optibase's CEO **Amir Philips**, "The acquisition is well spread across various locations in Bavaria which is considered to be the strongest economical region in Germany. We will continue looking for additional opportunities in this market."

Germany/Acquisitions

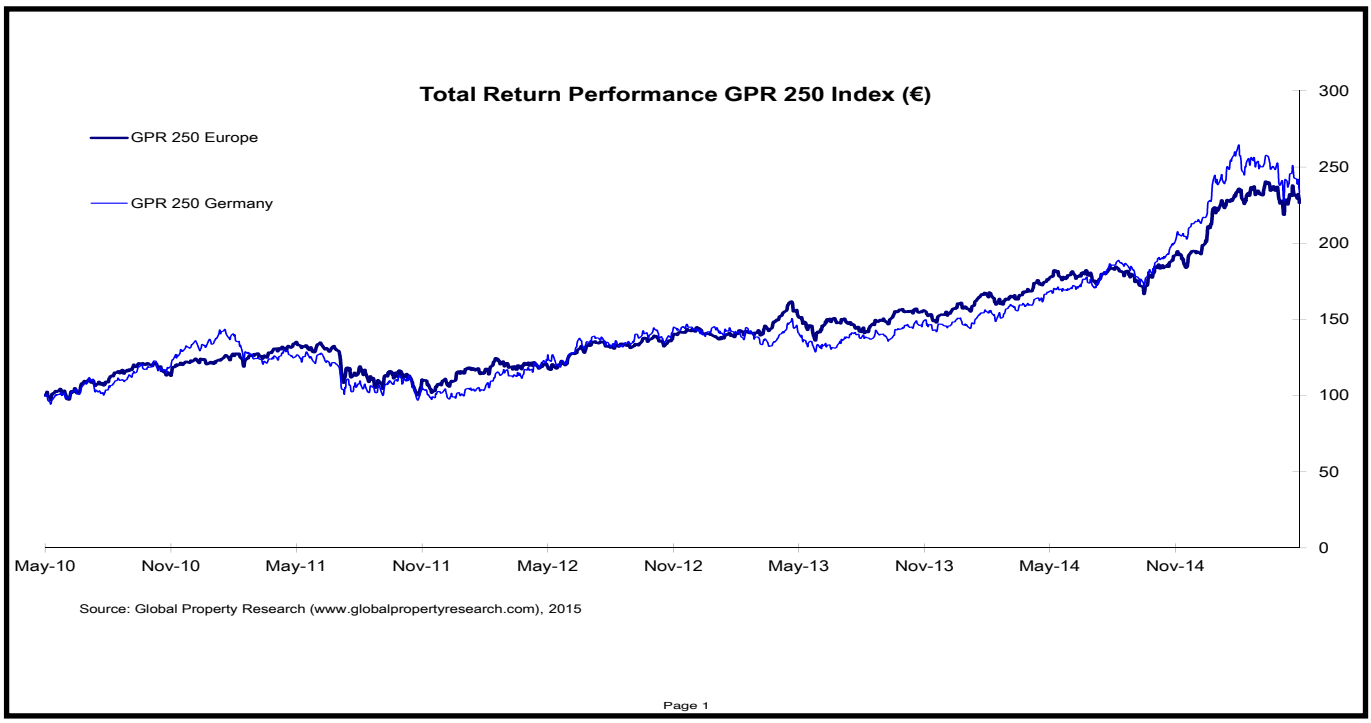
Brack Capital buys further German residential units

The Netherlands-headquartered **Brack Capital** has bought a further 430 residential units in northern Germany for €24.5m and said it was in advanced stages of negotiation with an unnamed German bank for a £17.6m non-recourse loan.

The total leasable area of the portfolio is about 29,000 sqm and the units are let to a number of tenants. The occupancy rate is 97% and the annual gross rental income is €1.7 million.

The Tel Aviv-listed **Brack Capital Properties N.V.** has been active in Germany since 2004, concentrating mainly in the multifamily and retail sectors throughout the country, as well as the condominium development market in Düsseldorf (Grafental). The Germany portfolio, which Brack Capital manages itself, has more than 1.1 million sqm of lettable space.

The commercial assets include shopping centres, power centres, retail parks and DYI centres, with major tenants including **Kaufland** and **OBI**. Residential holdings include about 9,200 apartments with 520,000 sqm in Leipzig, Hanover, Bremen, Essen, Dortmund and other mid-sized cities in North Rhine-Westphalia. Occupancy rates are over 95%.



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

Germany/Residential real estate

Accentro buys from Westgrund at 21 times net income

Berlin housing privatisation specialist **Accentro Real Estate AG** has also been among active buyers on the Berlin residential markets in recent week. It has just acquired a further 419 centrally located residential units with a total residential area of 22,186 sqm, and a combined annual net rent of €1.5m. The seller was listed company **Westgrund**, now about to become part of **Adler Real Estate AG**.

Just last month the Frankfurt-listed **Accentro** bought a further 364 apartments for €27.4m. The portfolio has 22,000 sqm of lettable space, and are located in Neukölln, Spandau, Friedenau, Zehlendorf, Reinickendorf and Alt-Tegel districts of the city. Accentro described them as 'reasonably-priced housing, affordable for existing tenants as owner-occupied properties. The company also recently sold a residential portfolio in the Hohenschönhausen district for €51.5m, which generated "a high profit", according to CEO **Jacopo Mingazzini**.

Mingazzini said the funds would be re-invested in residential properties. "The new acquisitions are a good example of our investment strategy. We are looking for properties in the medium price segment in established locations in major German cities. One of our unique strengths lies in the socially responsible sale of properties to tenants and tenant-focused buyers." He is still very bullish on Berlin, saying "The parameters are extremely auspicious in the German capital. In addition to the very favourable demographics, the city's macro-economy presents a bright picture. There is steady job growth. In addition, Berlin keeps attracting new companies."

The seller of the 419 units to privatiser Accentro is Westgrund AG, about to be absorbed in a takeover by high-flying listed company Adler Real Estate, which will give the combined new company more than 50,000 residential units.

Westgrund said it had made a profit of more than €6m on the 419 units, with the purchase price at 20% above the IFRS fair book value as of end-2014. Westgrund's board member and financial director **Sascha Giest** commented, "For our shareholders this is a favorable transaction as it also increases the NAV per share by 8 eurocents". He added that the transaction will increase liquid funds by slightly more than €16m net before tax payments, and will improve the financial results for the second quarter of the current business year.

His fellow board member **Arndt Krienen** added the pointed comment, "With this divestment we take advantage of the favourable market environment for residential real estate in Berlin and the corresponding preparedness of investors to offer purchasing prices equating to 21 times multiples of yearly net rental income."

Germany/Financing

New crowdfunding platform in Germany launches first mixed project

After a slow start in Germany, crowdfunding for real estate investments is now starting to take off, and the last six months have seen the steady arrival of new entrants into the field.

As REFIRE can attest from several recent conferences where the subject of crowdufnding was on the agenda, the investment form is always one that will attract the attentions of the German financial watchdog, ever-anxious to protect German investors from doing themselves harm with strange and untested financial instruments.

With the launch of Munich-based **Michael Ullman's Immobilienfreunde** nearly three years ago, the first platform was launched with an experienced real estate man at the helm. Since then several new crowdfunding platforms have sprung up, not all of which have the same understanding of the bricks-and-mortar industry, but no shortage of enthusiasm for the digital world and social marketing.

Now a new crowdfunding platform called **Mezzany** has just been launched, which brings together experienced housing privatisiation specialist **Jürgen Kelber** (*pictured, right*) with entrepreneur **Jens-Uwe Sauer,** founder of two green funding start-ups. Mezzany aims to enable private individuals to invest alongside professionals in project funding.

According to Sauer, "We are not just a crowdfunding platform which only offers property emissions or a property company that is discovering the internet as an additional distribution channel," said Sauer. "We are perfectly combining expertise from both worlds." Sauer's experience includes being founder and managing director of **Seedmatch** and **Econeers**, crowdfunding platforms for green start-ups and projects which have processed investments of more than €25m since 2011.

The first crowdfunding project is a residential redevelopment of listed bell

foundry *Franz Weeren* in Berlin's Neukölln district. Kelber plans to create 20 apartments and some commercial space in the old foundry and develop an adjacent building with 54 flats. Minimum investment required is €1,000, while target bond volume is €3m. If the amount is not reached, the project developer will put up the remainder to assure financing. Investors will receive 4.5% interest p.a. plus a project surplus at maturity, resulting in an IRR of over 13% in total, according to Mezzany's website.

Kelber said, "In contrast to usual project development financing, investors are entering via Mezzany at a late project stage. That reduces risk in so far as planning and financing risks are mostly tackled." Kelber is managing partner at **Dr. Lübke & Kelber** in Frankfurt, which has nationwide expertise in residential housing, and comes from 30 years of experience as a residential specialist at the Heilbronn-based **Alt & Kelber**, and later as a board member at listed Austrian group **conwert Immobilien**, which bought out Alt & Kelber.

Also joining in the crowdfunding fray in Germany and Austria is "**Home Rocket**", a Graz-based start-up founded by the very youthful **Wolfgang Deutschemann** and **Peter Garber** along with Steiermark project developer **C&P**, who is providing the first two developments to be funded, in Graz and Vienna. Minimum investment is €250 up to a maximum of €50,000.

Germany/Acquisitions

UK group InfraRed betting on Munich office market

UK asset manager **InfraRed Capital** has acquired a half-vacant office in Munich from German fund manager **Deka Immobilien** for €40m, backing its belief in an upsurge of demand in the eastern part of the city.

The London-headquartered InfraRed, a value-add property and infrastructure spin-out from British bank **HSBC**, has bought a 25,000 sqm office scheme including 400 underground car parking spaces in the east of the of the Bavarian capital, close to the Ostbahnhof railway station. Built in 1982, the building is only 50% occupied with a short weighted average lease term of 1.5 years.

The deal, earmarked for the **Active Fund III**, follows InfraRed's previous purchase of the *Leitwerk* building in the same Munich district in November 2013, which the firm said had been successfully repositioned and re-let to tenants including the Bavarian **Ministry of Health and Care**, and the **German Patent Office**.

'Applying our proven value-add expertise, we will seek to achieve the same with this investment undertaking an extensive refurbishment, modernisation and letting programme,' said **Joram Szerkowski**, in charge of German real

estate investments at InfraRed.

InfraRed said it will seek further investments in Munich. "Making repeat investments in select target markets has been a very effective way for us to source attractive opportunities. The Munich office sector is one of these markets," InfraRed's **Andreas Katsaros** said.

Just last November InfraRed completed fundraising for its third European value-add fund after attracting €475m of capital from investors worldwide, including Malaysia, Australia and Qatar. In a recent transaction the company sold the landmark *Cologne Tower*, which it had bought in 2011, to acquisitive Canadian listed group **DREAM Global REIT** for €110m, while also selling an adjoining hotel to fund manager **Internos** for just under €30m.

Germany/Industrial

Sirius to raise further €50m, buy 5 new business parks

London-listed **Sirius Real Estate**, which owns and operates business parks, offices and light industrial complexes throughout Germany, seems to be making steady progress in its recovery while building out its asset base among small and medium-sized German manufacturing businesses. In the year to March it grew its net asset value per share by 13%, and has seen its share price recover strongly over the past nine months.

According to CEO **Andrew Coombs**, "Demand for Sirius's workspace continues to be high, with gross annualised rent roll from the pre-acquisitions portfolio at €43.6m as at the end of March, compared with €41.3m at the end of March last year. This represented a like-for-like 5.6% increase. Including acquisitions, the rent roll has increased to a gross annualised €50m."

The company raised fresh capital and took a secondary listing on South Africa's **JSE AltX** in Johannesburg last December, which enabled it buy a further four business parks earlier this year (*as we reported in REFIRE*).

The group now plans to raise a further €50m by a private placement of new shares to fund the proposed purchase of a further five mixed-use business parks costing €58.2m, and yielding an initial 8.1%. Sirius says the share placement will help fund the acquisition, while the balance of the purchase will be initially funded by an €18m bank facility currently under negotiation, at an expected interest rate of 2.5%.

The surplus will be used to help the early repayment of two **Macquarie** loans totalling €56m. Sirius also intend to take out a new ten-year loan of €56m, at a rate of 135 bps over 3-month Euribor, and help reduce the group's overall LTV to 46%.

Guest Column: George Salden (7)

SERIES: The German Property Market: Increasing Values is the Key to Rate of Return

So far so good: we know the value of our real estate. In determining this we have not relied on the traditional methods therefor. Instead, we have used the "dynamic method" to determine and interrelate the microcycle and the macrocycle while at the same time being attentive to factors that could lead to possible rejections. What now? Now the focus must be on identifying whether or not value can be increased and realised during the investment cycle. It is only in this manner that real estate can generate the desired rate of return. Therefore we will now devote ourselves to the second step of the dynamic method: increasing value.

Here, too, a very important paradigm shift is involved: the processes for increasing value must focus on the tenant, because the tenant pays the rent and the rent generates the profit. It is the only factor that raises the value of the real estate and that realises the potential for increase, in that it is the basis therefor. Initially, in the context of increasing value, it is unimportant whether one is dealing with current or new tenants. The rental unit must be designed so that the tenant can maximise its use. Only in this fashion can tenant turnover be prevented or minimised and a sustainable cash flow guaranteed. Since the law dictates that the tenant must agree to every increase in rent, it is all the more important to undertake renovation and refurbishment operations that address the needs of the tenant. A sustainable increase in value that is free of conflict can only be attained by harmonising the individual interests of the tenant with those of the investor.

Active value increase takes place on two levels: first the value of the real estate is increased through construction measures. Second, the revenue of the real estate is increased by raising the rent and through the elimination of vacancies. Both measures not only have a direct effect on the value of the real estate but are also mutually dependent on one another. This is because construction measures should only be undertaken if there is a potential for increasing the rent and the rent can only be increased if the construction measures raise the rental unit to a corresponding level of quality.

And here one must be sure to bear in mind that all measures undertaken to increase value must be coordinated with the micro- and macrocycles. It is only when the construction measures and the rent increases take place in accordance with the cycles that the value of the real estate can be increased and optimal revenue generated. It is not only the entire real estate that must be measured against the cycles but an individual strategy based on the cyclical circumstances must be drafted for each separate rental unit. In practice this insight is not always fully acted upon. In business plans, renovation costs are time and again itemised in a manner that is simply based on the area of the rental unit; sometimes flat rate contributions are simply assigned to each rental unit.

There are basically two possibilities available for increasing the value of real estate: on the one hand elimination of vacancies, rent increases upon change of tenants, rent increases for existing tenants, as well as structural alterations, and on the other hand an increase in the surface area of the real estate itself. The quickest and most effective solution for increasing the annual net rent is the elimination of vacancies. The worst case scenario is that the real estate is completely vacant and the investor must cover all the costs associated therewith without generating any revenue. Such an investment is by all means to be avoided, because it violates the golden rule for increasing the value of real estate: cash on cash! With cash-on-cash management all on-going expenses can be covered by on-going income.

If the vacancies in the real estate are eliminated, then rental increases in the case of changes in tenants can be carried out as a second step in increasing value. Increasing rent for existing tenants is subject to a clearly defined legal process because the investor must operate within a statutory framework. A statutory change undertaken on 1st March, 2013 established that communities could even reduce the capping limit by 15 %, in order to counteract too rapid an increase in rent.

In considering whether or not to undertake construction measures, it is important to take into account analyses of the micro- and macromarkets. They establish the conditions for determining the real net output ratio: the classification of real estate investments provide a starting point in order to ascertain the real net output ratio of renovation work. Through the microcycle the investment costs can be determined, which then serve as a decisive indicator for establishing the investment class and, moreover, for ascribing a certain chance/risk profile to real estate. In order to also actually realise the chances, the value of real estate must be raised to its corresponding potential. Increase of real estate value is often associated with a high level of expense. It is

therefore even more important to keep the expenses in their proper relationship to the development potential of real estate and to the desired target revenue.

Since both the potential of real estate and the target revenue are determined by the macrocycle, the cycle plays a special role in connection with increasing value: it establishes what renovation work has a positive value on the real estate and for which property no such positive effect can be attained. Many investors would think that an unrenovated rental unit from the 1970s with an old backsplash and wall-to-wall carpeting would in any case have to be renovated - regardless of the strength of the macrocycle. Yet if the rent in this rental unit is already at the level of the market rent because there is a high demand due to exclusive location, then no potential for increase exists. The rent can no longer be increased - how then are the expenses for renovation to be compensated for?

From the revenue. Expenditures that do not increase value are paid out of the profits of the investor and thereby reduce revenue. On the other hand, it would make good sense to completely renovate the same rental unit, if its current rental price was far below the local market rent because of its poor condition. The increase of the rent would justify the renovation costs. Measures to increase value must therefore always be undertaken in a fashion so they make sense in relation to the potential of the real estate and the prognosis of future market rent.

However, before undertaking measures to increase value, the investor must look into the investment cycle. At what point in the investment cycle does the real estate find itself at the beginning of the process of increasing value and where will it be at the end thereof? In this regard it is to be assumed that a piece of real estate passes through various investment classes during the course of its life cycle. Each piece of real estate - either after it has first been built or after being completely renovated from the ground up - begins as a super core, core or core plus piece of real estate, based upon the location of the property. Super core property is a classification that would be restricted to property in truly exclusive locations experiencing extraordinarily strong macrocycles. In order for property to be assigned a core classification, a good location is necessary. Property that is located in intermediate or ordinary locations merely begins its lifecycle in the core plus class.

Starting with the initial investment classification, the real estate, in a prototypical market cycle, passes through the value-added, opportunistic and development classifications: an increasingly worsening structure, rental units with substantial need of repair, and rejections based on considerations of the macrocycle are the major reasons for a continuing downgrading of the property. The processes that were carried out in the context of a value increase now take place in reverse order for the real estate. By attending to accumulated repairs through renovation as well as by undertaking active tenant management, it is possible to raise the investment classification of a property.

Just how much the value of a property can be increased and what investment classification it reaches at the end of the investment cycle depends greatly on investment strategy, which once again is determined by the cycle itself. One must assume that a long course of value increase through the investment classifications signifies a significant real net output ratio. A great deal more expense for renovation is involved in transforming a development class property into super core real estate than for increasing the value of property in the core plus classification.

In this regard the gross revenue plays an important role in terms of the investment cycle: it provides information concerning the available real net output ratio for value increase measures. The gross revenue provides the ratio that the renovation costs must bear to the value increase. In the case of gross revenues of 10 per cent a sustainable increase of rental income per year of 1,000.00 Euros must therefore not incur costs of more than 10,000.00 Euros.

The money that is available for renovation of a rental unit is always ascertained directly from the market for which the potential increase in value of the individual rental unit is being considered. The starting point for such considerations is the difference between the current effective rent and the previously ascertained target rent. This difference is then projected for the year in order to determine the effect of a rent increase on the annual net earnings. The maximum investment of capital is easy to calculate: the return on investment is to be divided by the rate of return on investment.

In our next column we will turn to that which is our actual goal: how to realise value!

George Salden is the author of the book "Die Dynamische Methode" [The Dynamic Method] based on his 19 years of experience as an expert and manager in property and transaction management which highlights the way towards a whole new method of determining the profitability of properties. He was previously a director at alt+kelber Immobilienmanagement, a subsidiary of conwert Immobilien Invest SE, where he was responsible for major international transactions. He then took over as International Head of M&A at AK Holding GmbH & Co. KG. He is now Head of Transaction/ Executive Board Member at Dr. Lübke & Kelber / Arbireo.

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