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.

Whatever your particular area of specialisation, we think you'll find timely, incisive information within our pages, helping to inform you of the key deals, the numbers, the markets, the players and the people.

The areas we focus on are:

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European REITs
German Real Estate Finance
German Non-Performing Loans (NPLs)
Retail Property Funds
Mortgage Securitisation
CMBS/RMBS
Privatisations
Refinancing
Euro-zone Property Financing

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Lack of investor enthusiasm sees Deutsche Annington cancel IPO

In a last-minute decision, taken on the evening before the company was due to make its long-awaited stock market debut, Germany's largest residential landlord Deutsche Annington cancelled its July 3rd IPO after it became clear that there was insufficient demand for its new shares. Late on Tuesday evening the company issued a statement saying it had postponed the IPO due to "persistent adverse market conditions".

At the price range at which the stock had been offered, the company would have been valued at about €4bn. In its initial statements, a spokesperson for Annington said it would continue to evaluate the market environment regarding a future listing, but it was too early to say when that might be.

It had become increasingly clear over the past week from the company's book-building exercise that the Deutsche Annington flotation was in trouble. Investor response to the price range of €18.00 to €21.00 had been weak in the run-up to the sale, and it was thought that only about 80% of the shares had been taken up, at prices at the very lower end of the spectrum.

On Tuesday evening, the night before the flotation, a number of sources reported that there had been a late surge of buying orders, but it was clearly not enough. In a last throw of the dice, Annington's owners and its banker consortium headed by **JP Morgan** and **Morgan Stanley** slashed the issue volume from more than €1 billion to €650m in a bid to make the offer more attractive, but even that failed to tip the scales in their favour.

Annington' management immediately went into damage-limitation mode to prop up the fundamentals of its business and give itself time to consider the ramifications of its failure to launch itself as a public company. Board chairman **Rolf Buch** said in a statement, "The decision to cancel the flotation has no effect on Deutsche Annington's strategy. We have

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strong financial foundations and will be driving ahead with our operating business, including our planned programme of investment."

The company's plan sees €800m being invested in upgrading and refurbishing a large part of its housing stock next year, and it had earmarked €400m from the proposed proceeds from the listing for this programme and the urgent paying-down of part of its huge debt burden.

"The LEG flotation managed to place product that it might otherwise have been difficult to sell... In my view, pricing needs to below net asset value and offer dividends of about 6% to be attractive"

Over the past week Annington executives had consistently ruled out lowering the issue price, despite audible criticism from analysts that the price was too ambitious. As a general rule, a public flotation like Annington's needs to be well oversubscribed, so that the accompanying bankers can mix-and-match among both longer-term oriented investors and shorter-term traders, to ensure a lively market in the stock. This manifestly failed to happen. Despite all the last-minute efforts to awaken investor appetite, Annington and its owners had no choice in the end but to cancel.

Annington is owned 85% by UK private equity investor **Terra Firma**, with the rest owned by **Apollo Global Management**. Had the stock listed at €18.00, the owners were looking at raising €1bn, rather than the €1.1bn or €1.2bn at the upper end of the price range, had that been feasible. However, even at €18.00 the price represented only small discount to net asset value, and several German analysts had commented over the past few days how institutional investors were keeping their distance, with mutterings to be heard that €17.00 or €16.50 would probably need to be offered by Annington to lure the buyers out in sufficient numbers.

Investors are all too cognisant of the mood in the immediate aftermath of the giant LEG flotation in February, which saw the stock launched against a background of general optimism for the residential sector. However, trading on the opening day was tepid, and the share price has since been trading mainly at about 10% below its €44.00 opening price.

A successful debut had been seen as critical for the Bochum-based Deutsche Annington as it seeks to refinance its debt on a more sustainable basis than it had with its expensive 2006 CMBS. To succeed in issuing more favourably-priced bonds to investors, stamped with the minimum acceptable rating from **Standard & Poor's** and the rating agencies which it will need to satisfy investors, Annington said it needed to raise sufficient money from its public listing to rapidly reduce the debt level on its 180,000 housing units (the company also manages another 40,000 units for third parties).

Certainly there has been a cooling in demand since even the heady days of the LEG flotation a mere six months ago. Investors since then have been questioning whether they paid slightly too high a price for the stock, despite the mantle of enthusiasm surrounding everything to do with German residential for the past three years.

Since Annington's announcing of the date of its IPO on June 10th, the **DAX** has lost 7%. Most listed German property companies have seen their share prices fall over the past three weeks. Bond yields, for so long scorned for their minimal returns, are now creeping back up. The US Fed's 'tapering off' of its quantitative easing and China's monetary policy are also cited as further sources of nervousness in investor circles.

Last week, delegates (*including REFIRE*) at a workshop at the **ULI Urban Leader Summit** in Frankfurt (*for a further*

report, see elsewhere in this issue) heard **Ralph Winter**, the CEO of Switzerland-based opportunistic residential investor **Corestate Capital** express severe doubts about investor warmth for the Annington issue, and whether the listing would go ahead or not.. "The LEG transaction might have proved a milestone for the German market in that it managed to place product that would otherwise have been very difficult to sell. In my view, pricing needs to below net asset value and offer dividends of about 6% to be attractive, but this is not really possible", he suggested.

Winter added that, given the perception in investor circles that the risk in the eurozone may now be abating, the attraction of German housing as a safe haven come what may, may now be paling as a compelling argument for international investors. "German housing may not be such a hot sector any more", he said.

Although perhaps less significant as a factor for dampening enthusiasm in the sector, the so-called *Mietpreisbremse*, or cap on rental increases, has been taxing minds of all political persuasion, particularly in the run-up to parliamentary elections in September, where housing is shaping up to be one of the key electoral issues. Investors are probably aware that such posturing is part of the political landscape, but they are weary of what they see as further political interference in the housing market, several participants observed..

Germany/Legislation

Berlin raises property transfer tax to 6%

We reported some weeks ago in REFIRE that the German authorities were shocked to discover that they had miscalculated when processing the results of the 2011 census, which led to overstating the human population of the country by 1.5m residents and understating the amount of buildings and housing available by 500,000. This led to a lot of head-scratching and analysis as to where things went wrong – which was largely attributed to the amount of foreigners who didn't de-register when they ceased living in Germany, according to the statisticians.

Whether that is the full story or not, the miscalculation has had immediate consequences in Berlin. From the 1st January next year the property acquisition tax in Berlin is being raised from 5% to 6% to compensate for the 180,000 citizens in Berlin who it has now transpired don't exist. The population of the city was overestimated – it's now less than we thought it was. The city will now have €470m less in tax income than it thought it would get – and what's worse, 970m of tax money distributed to Berlin as part of Germany's equalisation payments scheme from wealthier Länder to the poorer ones, now has to be repaid.

As a sop to angry investors, the Berlin senate is considering introducing a law that would lower the agency commission payable to property brokers from 7% to 6%.

EDITORIAL

As one lot tries to exit, the other lot is trying to fight its way in

There may have been an element of bad luck in the aborted IPO of Deutsche Annington, which denied UK private equity investor Terra Firma and its ebullient leader Guy Hands the opportunity to recoup some money after a series of financial disasters, and return something to his long-suffering investors. Hands has been looking for an exit from Deutsche Annington for some time, and this was the golden opportunity.

Possibly this was always going to be a close call, given the internal juggling that Annington has had to engage in over the past eighteen months, from re-financing its massive debt burden, to losing one and then finding another CEO capable of performing miracles with both the company's housing offering and with the financial community.

However, from the beginning of the year it was clear that the company was in a race against time. The Masters of the Universe over at Goldman Sachs' Whitehall Funds got their timing just about right in scrambling over the line in February and leaving the risk of ownership of Düsseldorf's LEG in the hands of thousands of new shareholders, having trousered many hundreds of millions for their brief period of stewardship.

It may have been bad luck that even more uncertainty has been swirling around the markets since June 10th, when Annington announced its IPO schedule. But it's been evident for over a week that there was serious resistance among investors to Annington's issue price, which even at the low end of the price band was pitching the company at the same discount to net asset value as LEG in rosier times.

The lucky LEG shareholders are down only 10% on their investment since then, still faring somewhat better than at a number of their listed German property peers, some of whom have tumbled up to 20% since May.

From what we understand, the banks managing Annington's flotation opted – finally, in the last hours - to cut the issue volume in half, but remained stubborn on the price of the stock. Some previously committed investors sensed the issue was now balancing on a knife-edge, and pulled large orders, scuppering any last hopes of the promoters getting the issue away.

Doubtless there will be extensive post-match analysis as to what might have been done, but it certainly looks as if that window of opportunity is closed for the rest of the year - at the very least - for Annington and Terra Firma.

While the company puts a stoic face on things, and says it's back to business as usual, there will be consequences. The money from the IPO was badly needed for a big backlog of maintenance and refurbishment in the company's enormous housing stock, and this will now have to be found from elsewhere – or not. Although Annington's business fundamentals are solid, it will prove hard to increase its rental income, with the political tide turning against any suggestion of buccaneering landlords.

We have, of course, been reporting in these pages on the cooling in sentiment – particularly among foreign investors – towards the German residential market for months. Given its low vacancy rates, stable rental returns, and new-found enthusiasm for Germans to become owner-occupiers, the sector has enjoyed nearly three years of investor attention – most of it warranted, we have to say.

But the sands are shifting, and the caravan is becoming restless. Gold has plummeted, shares are shaky, bond yields are creeping back up, core assets in real estate markets are looking pricey, and investors are wondering if it's not time to do something else.

Paradoxically, the very owners of capital getting weary of earning only 4% in Germany are vacating the field to a new class of property investor, for whom 4% in a safe currency sounds like something well worth pursuing. Asian investors, particularly groups from China and South Korea, are coming to represent a new force in the market, and after visiting London, are increasingly coming over to look at opportunities in Germany.

They won't be buying tatty 10-storey apartment blocks on the outskirts of Wanne-Eickel any time soon, nor are they interested in the grinding mathematics of how to make such an investment work – the very bread-and-butter of the whizz-kids who toil over the spreadsheets at the private equity groups. No sirree, they don't need to come to Europe for that, with more than half the world's population scrambling to find similar dwellings on their own Asian doorstep.

But they ARE under pressure to diversify risk in their national pension funds, and from Asia, Germany looks more and more like a model of propriety and fiscal rectitude. South Korean cross-border real estate investment grew nine-fold in this year's first quarter, compared to last year's first full six months. That's a big number, and a certain amount of it is headed this way.

That's why we're busy here boning up on the investment strategies of Suhyup Bank, Hanwha AMC, LIG Fire & Marine Insurance, and the National Credit Union Federation of Korea. And this group's just the tip of the iceberg. And so, as one group tries to exit, another tries to fight its way in. 'Twas ever thus.

Charles Kingston, Editor

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Angela Merkel's party the **CDU** had originally opposed the measure, originally proposed by finance minister **Ulrich Nussbaum** (Independent) as a means of helping to balance the budget by 2015 by bringing in a further €100m annually on top of the existing €700m generated by the tax. However, last week the CDU quickly capitulated, conceding that without some form of extra taxation the dream of erasing the deficit was unfeasible – and countering with the proposal of reducing brokers' commissions by law.

Berlin has the lowest level of owner-occupiership of any Germany city, with only about 10% of the population owning their own homes. About half of all Berlin housing transactions – for renting or buying – involve a broker, but (it goes without saying) that all property purchases will now be affected by the new tax. The tax has risen from 2% in 1996 through successive steps (after the German state handed over the setting of the tax to the federal states' own discretion), to where it was raised only last year from 4.5% to 5%. Berlin has always been the first to raise the property tax, and where Berlin goes, the other federal states invariably follow, with nearly all of them raising their own rates over the past few years. This is the first time the 6% barrier has been reached, but others can be expected to do likewise.

Real estate industry lobbying group **ZIA** were quick to comment on the new move, with CEO **Andreas Mattner** saying, "The Berlin senate is obviously trying to make capital out of the housing shortage. Clearly the federal states are taking the view that maximising their income is more important than solving the affordable housing problem."

Also openly criticising the Berlin decision, **Dr. Wulff Aengevelt** of Düsseldorf-based brokers **Aengevelt Immobilien** said the decision would hit the 'little people' hardest, in particular young families trying to build wealth and some security by buying their own home. "When this long phase of low interest rates is over and interest rates start rising, then the broader effects on society of these successive rises in the property transfer tax will become even more apparent", he said.

Aengevelt also criticised what he said was the "easy option" of hitting on property brokers as service providers to claw back some of the extra expense burden on buyers, rather than any of the countless other professionals working in the real estate industry, such as architects, lawyers, valuers, finance providers, and others. "Exclusion and polarisation do nothing but divide up our society, and that can't be the goal of balanced politics", he said.

Germany/Listed Companies

German company bosses sacked as boards clamp down

We would hesitate to herald a new dawn of shareholder activism in Germany on the strength of recent board turbulence, but it might be true to suggest that institutional investors will have taken note of the manner of the sacking of the chief executives of two leading German listed property companies in the past couple of weeks. It's a departure from the normally indulgent approach institutional shareholders have taken to senior board members of public real estate companies – a few more examples, and it might be considered a trend.

At Berlin residential property owner and developer **GSW Immobilien AG**, the brewing shareholder distrust over the appointment of its new CEO led to both he and the supervisory board chairman being deposed in a highly-publicised boardroom wrangle. Just last week the supervisory board at **Prime Office REIT-AG** decided to dispense with the services of CEO **Claus Hermuth**, at a time when the company is involved in merger talks with a larger rival, with key decisions to be taken before the upcoming August AGM.

But first, to GSW. The CEO **Bernd Kottmann** and long-time supervisory board chairman **Eckart John von Freyend** both resigned in the face of sustained pressure from shareholders which made their positions untenable. The opposition was led by 3% shareholder, the giant Dutch pension fund **PGGM**, who claimed that Kottmann had been appointed with undue haste to the top job by von Freyend, with whom he had served on the ill-fated **IVG Immobilien AG** board some years ago. PGGM, in essence, was laying charges of crony capitalism at the board and accusing them of hiring a candidate without the prerequisite experience of the residential housing markets.

At the mid-June annual general meeting, the dissident shareholder groups just narrowly failed to reach the required majorities to depose both men, but the writing was on the wall. The continued free-fall into penny-stock territory for IVG Immobilien, where both men served in the mid-nineties (with von Freyend as chairman and Kottmann as CFO), and at whose door the foundation of many of the company's current problems are being laid, won't have helped.

A specially-convened meeting after the agm, however, put the final nails into both mens' involvement with the company, and both are parting with immediate effect. The company's stock price, previously a strong performer since GSW's successful market flotation in 2011, rebounded after falling by more than 10% since the onset of the dispute nearly two months ago. GSW owns and manages 60,000 apartments in Berlin, and until the new CEO is hired, will be led in the interim by COO **Jörg Schwagenscheidt** and CFO **Andreas Segal.**

Meanwhile, over at Munich-based Prime Office REIT-AG, a decision taken last week by the supervisory board will see the immediate departure of CEO Claus Hermuth. A company spokesman said Hermuth was being held responsible for not achieving operative goals

and slow progress in letting or selling key office assets. The company will be managed by CFO **Alexander von Cramm** while a successor is found.

Prime Office REIT-AG is a very focused owner and manager of prestigious and often unusual office properties in Germany's larger cities, but has struggled with its exposure to re-letting or selling some of its larger assets. Big office properties in Stuttgart and Frankfurt, for example, have had high vacancy rates and crushing cost overheads, leading to Prime Office reporting funds from operations of a mere €1.3m in the first quarter, down from €6.5m year-on-year.

With nearly 1bn of office property under management, the company has been in talks since early spring with the German subsidiary of US private equity group **Oak Tree Capital** to merge and create a group with €2.3bn of assets under management.

According to a company statement, these talks are still on track. "The current talks on a merger with OCM German Real Estate Holding AG, Cologne, will be continued. At the moment, the companies are in the process of calculating the corporate values required to determine the exchange ratio. However, the necessary draft merger agreement and the extensive supporting documentation cannot be finalised until the regular annual general meeting on 21 August 2013."

Also on the agenda for that day is the probable striking out of the proposed dividend of €0.18 per share for 2012 to bolster the company's capital structure. Another reason for institutionals to give voice to their disgruntlement.

Germany/Funds

Commerz Real Spezialfonds division offers logical fit for expanding Internos

Commerzbank is wasting little time in implementing its strategy to divest itself of poorly-performing or low margin businesses, shedding staff, consolidating offices, and refocusing on private clients and 'Mittelstand' companies.

The radical slimming diet includes dumping much of the legacy real estate business it inherited with its ill-fated venture into global real estate financing with **Eurohypo**. The bank has been actively negotiating with interested parties looking to pick up the remnants of Eurohypo's loan book at the right price, and we do expect new loan book sales to be announced shortly.

But this time the bank is selling its real estate Spezialfonds business **Commerz Real Spezialfondsgesellschaft mbH (CRS)**, and the buyer is British fund group **Internos**, which established its own German Spezialfonds platform in mid-2012. CRS manages a portfolio of nine separate funds, holding real estate valued at €1.6bn, including 68 European office, retail, hotel and logistics properties.

Essentially the division is the complete institutional (rather than the retail) real estate business of Commerz Real, although Commerz Real will continue to manage institutional investment vehicles in the infrastructure sector, such as electricity grid operator **Amprion**, which it bought in 2011 from utility **RWE**. The bank said this would play to its strengths in the area of club deals and asset management.

Commerzbank said the real estate Spezialfonds division was low-margin and barely profitable. Just a couple of months ago Commerz Real boss **Andreas Muschter** bemoaned the "lack of efficiency" in the bank's Spezialfonds division, while at the same time announcing the launch of two further European-based Spezialfonds.

Commerz Real, a fully-owned subsidiary of Commerzbank, has €35bn of assets under management and manages several German open-ended property funds. These include the biggest open-ended fund in Germany, **Commerz Real HausInvest,** which, among other assets, controls French REIT/SIIC **Cegereal**. It also has equity investments in aircraft,

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renewable energy, and shipping.

Jos Short, the CEO and co-founder of Internos (*pictured, previous page*), was in Frankfurt last week at a real estate gathering attended by REFIRE, and talked about his expansion plans for the company's German platform, although there were no specific details about the terms or the price of the Commerz Real deal. However, the bulk of Internos's 1.9bn assets under management are in Germany, so there should be a certain natural fit. Internos's German platform is headed by **Paul Muno**, himself a former MD of Commerz Real Spezialfonds.

Commerzbank is gearing up to cut 5,200 jobs by the end of 2016, including 1,400 at its Frankfurt headquarters. This is likely to mean several Commerzbank properties in the Rhine-Main area around Frankfurt coming on the market. Excluded from this will be the *Lateral Towers* in Hausen in Frankfurt, previous home of stock exchange operator **Deutsche Börse**, and the *Gallileo* high-rise in Frankurt's central business district, which was sold to an IVG Immobilien group of South Korean fund investors earlier this month. Helping to boost its price prior to the sale was the signature by Commerzbank itself for a ten-year lease on 40,000 sqm of floor space.

Germany/Financing

Germany experiencing shrinking funding gap, but lower bank margins

Never far from the forefront in the debate about the commercial property funding gap in Europe is property advisory group **DTZ**, whose barometer attempts to measure the pulse of supply and demand for financing in the sector. DTZ's most recent readings indicate that the gap has shrunk by 42% fro $86bn to $50bn over the past six months, while the total volume of property requiring refinancing has fallen by 14% over the period – all of which sounds like very good news.

In fact, says DTZ, the core European commercial property markets of Germany, the UK, France and Sweden will see supply actually surpassing demand over the next two years. This is due to the fresh funding being made available by pension funds and insurance companies, who plan to raise their market share in the medium term from 2% to 7% in the continental European markets, and from 7% to 15% in the UK market. Overall the financing situation has eased considerably, DTZ believes.

These sentiments were echoed in one of the livelier discussions at last week's real estate gathering in Frankfurt under the auspices of the **Urban Land Institute**, attended by REFIRE. The round table discussion concerned the ubiquitous real estate funding gap, and participants agreed that whether there was a funding gap at all or not depended on which market you were in. Germany was good, eastern Europe (except for Poland and the Czech Republic) was not, they agreed. Core is good, but non-core and secondary is bad.

Professor Sven Bienert of the **IREBS** real estate academy pooh-poohed the notion of a wall of uncovered refinancing in Germany. While this was unrealistic, he said, the bigger danger is that the increasing readiness to finance deals might lead banks to not pricing in adequate risk. "Again, we can clearly see that there are two pictures here", said Bienert, a former managing director of **Probus Real Estate** in Austria.

His view was seconded by **Marcus Lemli**, the boss of **Savills Germany**, who said the picture had been transformed over the past six months. "The funding gap of 90m looked dramatic then, but that's given way to a different scenario. We're seeing more balance in the market, the capital markets are responsive, the listed companies are issuing corporate bonds, there's even new life in the CMBS market (a reference to **Gagfah's** recent 2bn refinancing). Certainly there are new sources of financing, but with the new debt funds from the pension funds and insurers looking for yields north of 8%, these are not going to be easy to find when the market is fixated on low-risk core property deals.

Helaba board member **Jürgen Fenk** (*pictured, left)* was also sceptical that there was a big funding gap out there, suggesting that he didn't know of any big project that wasn't getting funding in Germany. The CMBS deal for Gagfah recently was encouraging, but the financing would have been raised anyway – just not as cheaply as with the securitisation, he said.

Jürgen Helm, head of structured finance at **SEB AG**, the German division of the Swedish banking group, agreed that CMBS will return, but "it will have to be a much more transparent product", he said. Germany is still helped by bank funding sources underpinned by *Pfandbriefe* as covered bonds, and the robust nationwide system of *Sparkassen*, with their regional autonomy and specialised local knowledge. Other countries remain hampered by the lack of more debt products, and despite some good news stories, the banks are still very nervous, he added.

Germany/Research

German residential prices rising faster than rents

Studies from two of Germany's leading internet portals **Immowelt** and **ImmobilienScout24** provide strong evidence that the rate of price increases for residential housing in Germany's larger cities is rising now much faster than the rate of

rental increases – often a harbinger of a bubble building.

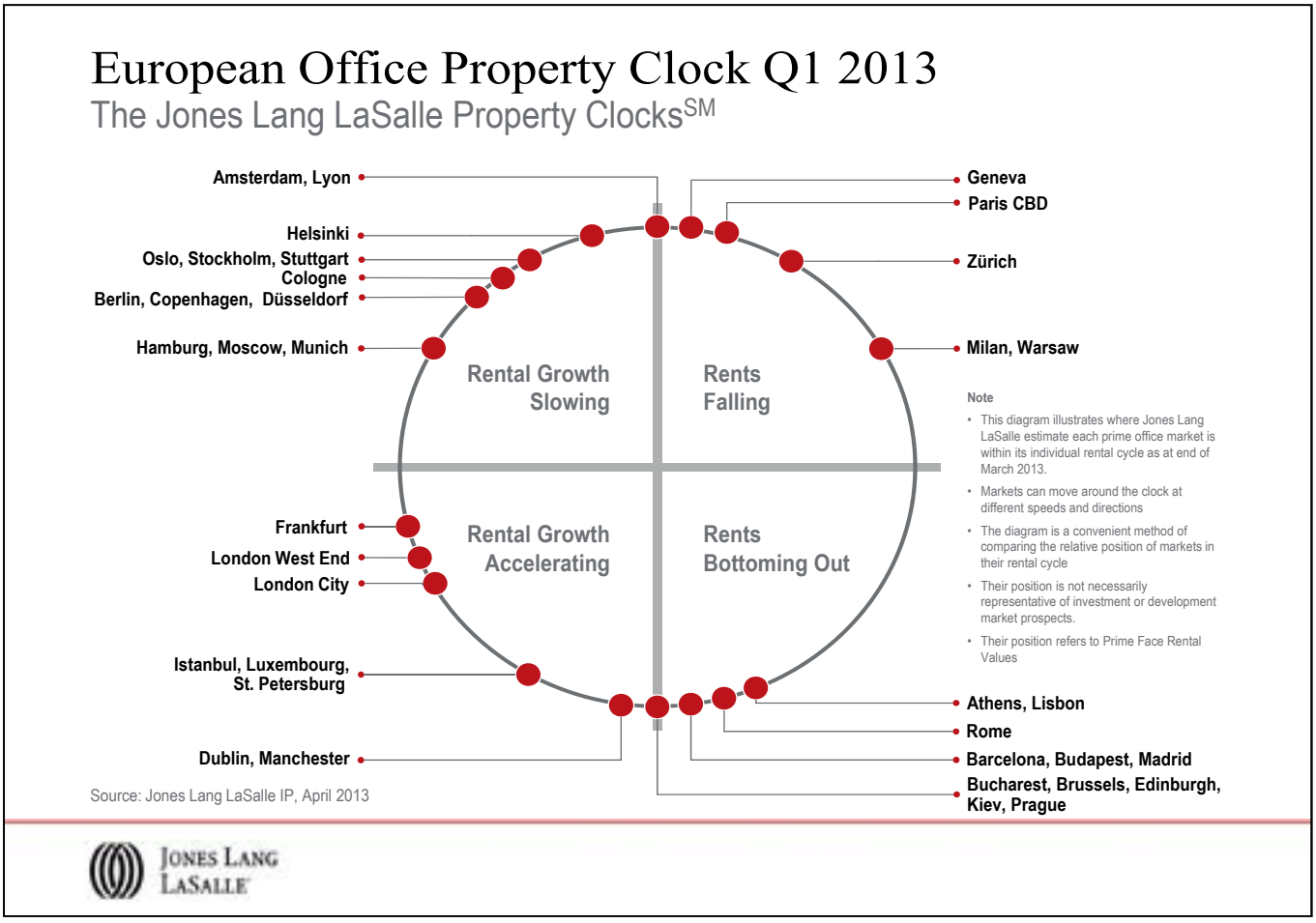
The Immowelt barometer compares the online broker's quoted rent rates in the major German urban markets, with the Nüremberg-based online platform logging nearly 1.2m rental and sales offers per month, making it fairly representative of the market as a whole. Immowelt's data suggests that housing rents largely stabilised in the largest German cities over the first quarter, following a year of strong growth in 2012, with Berlin posting the strongest growth year on year of nearly 11%.

Munich remains the city with highest rents in Germany at an average of €14.20 per sqm per month for new leases, up 7% on 1Q12 and more than double the nation's average of €6.60. It is followed by Frankfurt at €12.80 (+4%), Hamburg (€10.90) and Stuttgart (€10.70; +2%). While rents rose significantly in Frankfurt, Hamburg and Stuttgart last year, prices have stabilised in the first quarter, with Hamburg even seeing a 1% decrease on 1Q12. Berlin comes in at 7th place, after Düsseldorf and Cologne, at €8.40, following 11% rental growth due to a supply bottleneck and continued high demand.

Immowelt and rival ImmobilienScout24 both show similar figures for the rise in purchase prices of residential property over the past year, with the big cities of Berlin, Düsseldorf, Frankfurt am Main, Hamburg, Cologne, Munich and Stuttgart seeing price rises of up to 20%. These prices are still rising steadily, with Munich and Berlin jumping by 1.7% and 1.6% in the month of May alone, compared to April of this year.

Purchase prices in Munich have risen by 15% over the last 12 months, while rents rose by only 7%. In Düsseldorf prices have risen by 14% in the period, while rents have stagnated. Hamburg has seen price rises of 7%, while rents have actually dropped by 1%. These figures correspond to a rental yield of 3.5%-4.5% for investors, or more likely less than 2% after deducting brokers' fees, property purchase tax, and lawyers' fees as well as basic maintenance charges.

We reported in a recent REFIRE issue on the findings of the **AWI Aengevelt Residential Index**, managed by the **Aengevelt** brokerage house, whose latest readings suggested that this is where the professionals start leaving the field to



Source: Jones Lang LaSalle

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the latest wave of amateurs desperate to enter into the fray. Aengevelt's head of research **Markus Schmidt** strongly suggested that investors consider an imminent exit from some of their holdings.

Despite strong demand in most markets, the pace of new building is also acting as a force to dampen both rental and purchase prices – a factor not present a couple of years ago. Last year 211,215 building permits were issued, compared to the 148,340 issued in 2008 – a rise of 42%. Visitors to cities such as Frankfurt can see the enormous amount of new building of residential housing going on to cater for the undoubted demand, but this is likely to ease pressure on prices over the coming years. With bond yields creeping back up (10-year Bunds have risen from 1.31% to 1.78%), interest rates will be rising slowly to match, which will also act to put a damper on super-cheap financing deals.

Meanwhile, a new report issued by the research team under **Marcus Cieleback** at Augsburg-based **Patrizia Immobilien** warns that the pace of growth in residential rents is set to slow, although Germany's largest cities will see continued growth through 2017. Rents for existing homes are likely to rise faster than those for new-built homes, they believe.

In fact, the researchers draw a strong distinction between existing assets and new developments in their latest Residential Property Investment Compass. "Rents on new constructions will not increase as much as existing apartments," says head of research Marcus Cieleback in the report. Investors should distinguish between the existing property market and newly built property market depending on the location in order to ensure a good investment strategy for their portfolio."

Cieleback *(pictured, right)* explains why he sees this as being particularly important: Rental growth for apartments in Germany's Big 7 cities remained below the annual inflation rate of 2% in all the years between 1992 and 2007, before catching up significantly and making up for much lost ground. He explains that, before 2007, rents for newly built properties rose by 0.5% a year on average and existing apartments by 1.5%. "Contrary to the widely-held opinion in Germany that rents would explode, the increases seen were still weaker than actual inflation," says Cieleback. "In particular, increases in the newly built property segment were weaker than originally thought, with an average growth rate of 0.5% a year."

This is where Cieleback sees risk for investors – specifically, where rents deviate greatly from overall market trends.

Frankfurt, for example, is the most volatile market with the largest deviations from the average rental price trend for new-build; Berlin is the city with the greatest risk for existing properties. By contrast, rents in Düsseldorf deviate only slightly from average rents for new-build; the same is true for existing assets in Hamburg. "Depending on the submarket, Germany's individual cities also differ in the potential risk they pose for investors", he cautions.

Germany/Legislation

Sector remains cautious after watchdog BaFin ruling on German REITs status

Experienced real estate investors in Germany are still scratching their heads as they try to second-guess financial watchdog **BaFin's** interpretation of what constitutes an 'operational' business.

Much may depend on the outcome, as the German real estate industry attempts to assess the effectiveness of months of lobbying work devoted to clarifying the status of German REITS in light of the pending new laws under the EU's **AIFM** directives. The new German *Kapitalanlagegesetzbuch (KAGB)* legislation is due to take effect on July 22nd.

The issue has been hinging on whether REITs or other listed real estate companies would fall under the new legal framework. In what seems to be a reversal of its earlier stance, BaFin has now declared that REITs will have to be judged on a case-by-case basis when

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applying the new law. Specifically, it said in a statement that any real estate company operating in the sector without accumulating money from investors into a so-called Investmentvermögen with a view to investing it "along a specified strategy" will not be required to adhere to the new regulations.

BaFin said in an interpretative statement that property management, project development – including the sale of a property the company has developed itself – facility management and consulting on sales and financing would be defined as "operational activities". It added, "The question of whether a REIT qualifies as Investmentvermögen cannot be answered in general but – similar to the case of listed real estate companies – can only be decided according to the specific situation in any single case."

Attempting further clarification, the statement said: "Listed property companies, whose main business is project development (conception, acquisition, property development and subsequent sale of the self-developed property) or facility management, realtor and valuation activity or finance advisory in connection with the purchase or sale of a property, are operationally active and thus not investment wealth. The same is true for listed property companies that operate their properties themselves (e.g. operation of a hotel or nursing facility)." Companies that work with third-party operators are also unaffected as long as operative decisions remain within the company.

Since the beginning of the year, BaFin has received over 300 submissions from the **European Public Real Estate Association**, German property association and lobbying group **ZIA** and major listed property investors, expressing concern that REITs should be subject to this law.

ZIA's president **Andreas Mattner** described the decision by the BaFin as "practical", although he envisages some difficulty pinpointing the difference between an investment and a business strategy. Nonetheless, he said, "We are glad that we could convince BaFin to find a distinction between funds and property companies that is more practical. This is the right way; but further clarifications still need to be made."

Philip Charls (*pictured, above right*), the CEO at European Public Real Estate Association EPRA, also welcomed the revised BaFin stance, saying that it reflected the recent guidance provided by the **European Securities and Markets Authority (ESMA)** and supports EPRA's view that Germany's REITs should be judged against the criteria for identifying funds in the same ways as any other real estate company.

"The position that the BaFin has adopted on REITs reflects the updated ESMA guidance and aligns Germany closely with France and the UK by adopting a 'case-by-case' approach on whether

REITs or property companies fall under AIFMD. Other EU countries will take note as they examine their own implementation of the directive", he said.

However, EPRA too said it remained concerned about BaFin's view that developing property for sale is an 'operational' business (outside the scope of the AIFMD), whereas the business of managing property for long-term leasing activity is not.

Olivier Elamine, CEO of Hamburg-based **Alstria Office REIT** and an EPRA board member, said: "Putting aside the huge contribution that listed property companies make to the real economy through their development and refurbishment programmes, the business of managing and leasing property for the long-term is an intensive operational business.

"The ongoing management of increasingly shorter and more flexible leases and active engagement with occupiers to reduce the operational energy use of buildings during the property lifecycle are just two examples of the important role that property companies perform in servicing the accommodation needs of Europe's business and citizens. We struggle to understand why this business would not be recognised as an 'operational' business."

Germany/Financing

Gagfah gains plaudits after new €2.1bn CMBS refinancing

There has been much talk and speculation in German real estate circles as to whether a revival of the moribund CMBS market is imminent, following the refinancing during the month by listed housing investor **Gagfah** of one of its largest portfolios.

So far most observers are adopting a 'wait and see' attitude, as are investors in the company's stock after an initial thumbs-up when the deal was announced.

Gagfah, which is still 66% majority-owned by US private equity group Fortress, signed a refinancing deal for its €2.06bn securitised *German Residential Funding (GRF)* portfolio in a 5-year (plus one-year extension option) CMBS financing structure at 2.76%. Capital repayment of 0.5% annually is included. The loan on the portfolio, which covers more than 61,000 apartments and 470 commercial properties, had been scheduled for repayment in August, and was seen as a key hurdle for the group to overcome in its overall battle to refinance its debt burden.

In earlier talks, Gagfah had targeted €600m for refinancing the GRF portfolio with the help of a bank consortium, then €700m, then €1bn – so the step to refinancing the whole package through a CMBS at an overall lower interest rate is being seen as somewhat of a coup.

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Earlier this year Gagfah managed to refinance €1.1bn of its loans on its Dresden *Woba* portfolio with **Bank of America Merrill Lynch**, having earlier reversed its decision to sell off the portfolio to external bidders. Gagfah ended up paying 3.34% for the new loan. Bank of America Merrill Lynch subsequently sold bonds backed by that loan in the first public CMBS deal in Europe this year. Gagfah still has to refinance a further €150m of debt due in October this year, but these two big refinancings will make a major difference to its overall financing position.

Gagfah has 145,000 of its own apartment units valued at €8.1bn, and manages a further 40,000 for third parties, making it the second-largest German residential property owner after **Deutsche Annington**.

The original GRF portfolio with its €2.06bn loan was paying 4.32% annually, so the new rate of 2.76% is a sizeable step. New CEO **Thomas Zinnöcker** commented on the latest CMBS agreement, "The refinancing at such attractive terms puts us in a great position and enables us to shift focus on our core business."

Several analysts liked the deal so much they hastily issued revised ratings for the stock. The new lower interest rate surpassed even the company's own expectations of 3.0-3.5% in their assumed best case, and could well help the company to return to its previously active policy of dividend payouts to shareholders, they suggested.

Germany/Debt Funds

iii-Investments launches new €300m debt fund, first deal done

Reinhard Mattern (pictured, right), the head of **iii-Investments**, the Munich-based funds subsidiary of **HypoVereinsbank** and ultimately **Unicredit**, took time out recently to explain his company's philosophy to the **Immpresseclub e.V**, Germany's inofficial association of real estate journalists, at a gathering in Frankfurt.

The Immpresseclub meets twice a year in different German cities, and – in addition to offering staff and freelance journalists a forum for discussing common interests - provides a useful opportunity for company bosses to highlight aspects of their business that might not normally merit headlines, in a fairly relaxed and convivial environment.

We reported some months ago in REFIRE on iii-Investments' first debt fund, a German *Spezialfonds* into which a single large institutional investor committed €200m. Mattern said the company has now raised a further €100m in equity for its second debt fund from insurance companies and pension funds, and is targeting a full volume of €300m. He added that iii-investments has now made its first loan purchase, marking the first time that a pure debt fund has taken a sizeable share in a large German property transaction.

The deal is a €30m syndicated loan for the acquisition of a residential portfolio in North Rhine-Westphalia. The loan was arranged by **Deutsche Bank**, and iii purchased the junior tranche with a term of 10 years. The purchased loan will be spread equally over the two debt funds. "With this contribution to the financing of a widely diversified residential portfolio we have succeeded in making our first debt purchase on attractive terms," said Mattern. "As we have received a number of further interesting enquiries from different banks, we are optimistic about being able to place our investors' capital swiftly."

The second fund is a pool fund, and like the first, is investing in debt backed by low-risk properties mainly in Germany (with some in other eurozone countries), with a little medium-risk thrown in to spice up returns. Loan sizes will be typically €10m to €40m.

iii-Investments' move aims to profit from two key trends. Firstly, banks facing stricter regulations are looking for buyers for their long-term real estate loans to ease pressure on their capital requirements; and secondly, insurers and pension funds are looking for higher yields (Mattern's fund is offering 4%) than they can currently get on low-return bonds in a low interest rate environment. Nonetheless, Mattern said his funds' approach was much more risk-averse than comparable Anglo-Saxon debt funds. iii-Investments already manages €4bn for institutions in 10 German Spezialfonds and two Luxembourg vehicles.

Germany/Acquisitions

CEE specialist Magnat refocuses onto German commercial market

The Frankfurt-listed **Magnat Real Estate AG**, primarily known for its opportunistic investing in eastern European property markets, said earlier this month that it was significantly shifting its business focus away from Austria and further east, in favour of the German commercial sector.

Magnat, which has strong personal and managerial connections with Austria, said it sold the last residential units and its asset management interests in its building schemes in Vienna, and said it was not planning to make further new investment in the country. Traditionally, Magnat has had a 'develop and sell' trading approach, supplemented by portfolio trading, frequently 'anti-cyclical investing' in markets such as the Ukraine, Turkey, Georgia and Romania.. The new focus will be on Germany and commercial properties for German small and medium-sized enterprises. The company is also to be renamed **DEMIRE Deutsche Mittelstand Real Estate AG** to reflect its new interests.

The company has liabilities of about €22.3m (31st December 2013), less the reduction of liabilities of €2.8m following the Viennese sale. Commenting on the move to what looks likely to be a less complex corporate structure, Magnat's CEO **Andreas Steyer** said, "We have now sold off all of our business activities in Austria at a good profit, and are now focusing squarely on German SMEs. This also entails significantly lower costs and a clear company structure."

Europe/Non-listed funds

Capital into Europe's non-listed sector again on the rise

The volume of capital raised for non-listed indirect real estate, funds and similar combinations, has risen substantially over the past year, reaching the highest level since 2008, as investors increasingly believe the market may have bottomed out, says European property fund association **INREV**.

In its 2012 *Capital Raising Survey*, INREV said growing investor confidence should also result in more non-core investments, despite challenging economic conditions. Total equity raised in the segment last year reached €29.5bn, of which €11.5bn was dedicated to non-listed real estate funds alone.

"These are encouraging data," said INREV's research director **Casper Hesp**. "They indicate that investors believe the market has reached its lowest point and are committing capital once again. There is also clearly an appetite for non-listed real estate funds which, to some degree, counters suggestions of a move away from funds towards alternatives such as

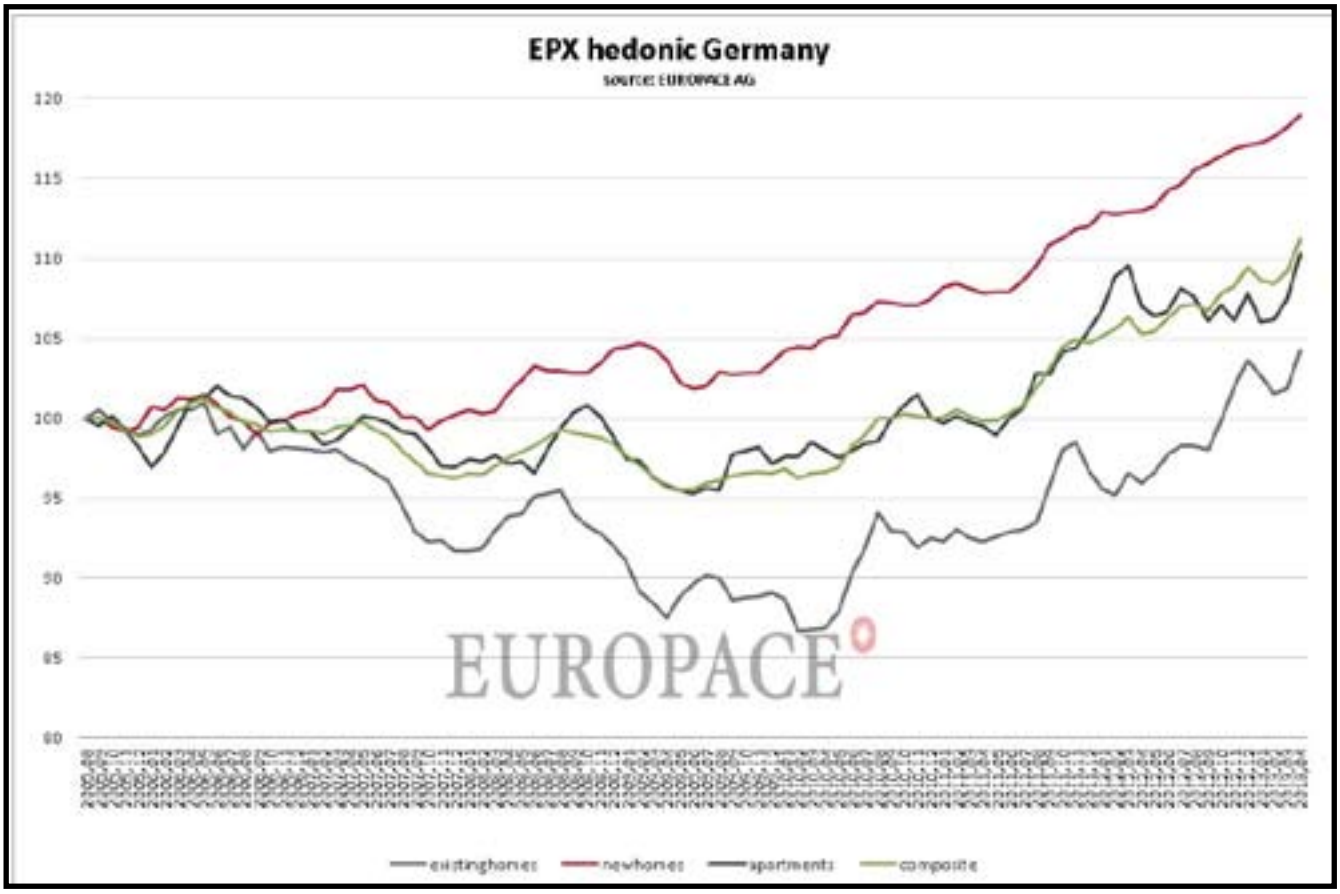

Chart courtesy of Europace

club deals, JVs and real estate debt."

However, there does remain strong investor interest in alternative investment vehicles, with €9.5bn raised for separate accounts and €4bn for joint ventures and club deals.

The survey also revealed a move towards higher-risk fund styles. While 63.1% of equity capital raised was for core funds, 28% was attributable to opportunity and 8.9% to value-add funds. The combined non-core 36.9% was an increase of 23% on 2011. At the same time, 52.9% of capital committed to closed-end funds was raised by opportunity and value-add vehicles. "Driven by the desire for better yields than are currently available in the oversubscribed core market, investors appear to be searching for options further up the risk curve," said Hesp.

The survey also shows that as a group, pension funds were the largest investors across all products. The majority of capital raised for closed-end funds came from European investors (75.4%), followed by those from Asia Pacific (10.4%) and North America (4.3%). Some 41.7% of all capital was raised by new funds with a 2012/2013 vintage.

Among all investors, the Germans were the largest source of European equity in closed-end funds, followed by Nordic and Swiss investors.

Globally, French, German, Italian and Swiss investors were the most risk-averse and assigned on average 92.4% of their capital to core funds, while the UK and Benelux investors committed the majority of their capital to value-added and opportunity funds.

Germany/Non-performing loans

Albulus, UKI team up to invest €100m in German NPLs

Hardened veterans of the German non-performing loans sector have long since learned to treat excessive exuberance about forthcoming waves of bank loan sell-offs with a certain disdain. However, a new tie-up between two experienced veterans may prove more fruitful in actually sourcing new deals than emerged from much of the misplaced hype of the past few years.

The London-based **UK & European Investments (UKI)** and German non-performing loan specialist **Albulus Advisors** have joined forces to invest up to €100m in German NPLs. The partners will focus on single loans or NPL baskets. In Germany, Albulus is headed up by founder **Ruprecht Hellauer** (*pictured, right*), a veteran of the NPL market from his earlier days at **Lohnbach Property Advisors**.

Outlining the terms of the partnership, UKI, a property investor and developer, said it intends to allocate €100m in equity to Albulus for non-performing and sub-performing loan investments. Albulus will originate, underwrite and execute the investments, targeting loans with collateral in major German metropolitan areas. Investment focus is on less liquid single loan transactions or NPL baskets at 10m-50m in equity. The partners will consider loans backed by collateral such as commercial properties, hotels and other operating assets.

"Germany is one of the most attractive markets for non-performing loans in Europe with strong creditor protection and a liquid real estate market," said Hellauer. "This is an exciting time for us as we are seeing an increased deal flow." Added UKI Acquisitions Director **Adam Golebiowski**: "Investing with Albulus is a significant step to capitalise on the European NPL opportunity. We see Germany as one of our core markets in Europe and we intend to increase our asset allocation to the market over the next few years."

The two companies already have experience of doing joint deals. UKI and Albulus completed a first joint transaction last November, acquiring a loan collateralised by the five-star *InterContinental Hotel* in Hamburg. It was revolved via an asset sale to **Kühne Immobilia**, held by **Klaus-Michael Kühne**, majority shareholder in logistics servicer **Kühne + Nagel,** who bought the 200-room hotel on the Alster lake in May. A further three transactions are under due diligence and are expected to close in the second half.

Founded in 1980, UK & European is a privately owned property development and investment company with a portfolio across all sectors and developments around Europe, the US and Asia.

Frankfurt-based Albulus is an independent manager founded by Hellauer in 2011, focusing exclusively on originating, underwriting and executing German NPL investments. The company spends a lot of time scrutinising German actual and potential NPL deals, last year looking at €1.4bn worth and providing indicative offers on about half of them.

In earlier commentaries, Hellauer has proved insightful on why German banks have rejected so many of his company's indicative offers, primarily ostensibly for price reasons. Of those deals rejected, he has commented, "We note that all of these loans ended up in restructuring instead of being sold. Banks seem to prefer keeping restructured and potentially sub-performing loans on their books instead of disposing of them. Insufficient write-downs at many banks, political pressure, the desire by bankers to protect their own jobs and the support provided by internal and external bad bank schemes all contribute to this behaviour."

In further commentary, Hellauer says: "The rationale for the trading of higher volumes of NPLs rose in 2012. From the banks' viewpoint, the complexity of managing assets – capex, lease-up, fire protection issues – and the loan workout challenges increased the longer

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they held on to non-performing loans. This year's themes are operating assets, uncooperative borrowers, asset management challenges and the seasoning of the loans allowing for higher write-downs. A pipeline of deals has emerged due to these factors."

"However, this pipeline is still largely blocked by these constraints, and our biggest competitor might not be other bidders, but the banks themselves, which continue to keep on restructuring. This defers – not resolves – the problem."

"The result is that a fragmented market is becoming even more fragmented. It is substantially different from the last NPL cycle of 2003 to early-2008, which was all about volume. The current cycle requires considerably more effort to identify and gain access to deal-flow. This makes the market less attractive for larger scale investors, but more attractive for specialised investors targeting smaller portfolios or single lines – which frankly suits us down to the ground."

Germany/Acquisitions

Israeli group Euro Globe forced to liquidate German assets

Israeli real estate investment group **Euro Globe Company** has agreed to liquidate its German real estate assets as part of an out-of-court settlement with its major bondholders. The company, which is controlled by Tel-Aviv listed **A. Levy Investments and Construction Ltd,** breached its agreement in April this year to repay bondholders, who subsequently sued the majority shareholder in the Israeli courts.

The company was originally set up in 2006 to invest in European real estate, and currently holds five assets in Germany for which it originally paid €90m. The assets, bought between 2006 and 2008, were 70% financed by foreign banks (mainly **RBS**), with a further 26% financed by the issuance of bonds, and the remaining mere 4% provided by the company's own equity. It is these bonds that the company is now unable to repay.

The nub of the bondholders claim is that Euro Globe owes them NIS 34m (about €7m) and is refusing to execute a deal in which it could liquidate its equity in its German properties, despite the fact that RBS is in the process of retreating back out of the German market, including its €26m mortgage lendings on Euro Globe assets. The bondholders have been arguing that the assets must be sold in order to protect even a fraction of their rights in the assets, and that at least €1.8m is already due on previous asset sales.

Europe/Research

European listed companies sharply narrow gap to NAV

Two recent sets of figures released by **EPRA**, the European Public Real Estate Association, highlight notable developments among Europe's listed property companies. Firstly, how they are scheduling their long-term debt obligations, and secondly, the continued narrowing of the gap between stated NAV and quoted share prices across the sector.

With the due date trend showing yet further lowering, Europe's listed property firms have an average of 15.87% outstanding debt maturing over the next 12 months, the EPRA figures show. Loan-to-value data for constituent firms in the *EPRA/FTSE European Index* for June showed that maturing short-term debt fell slightly from 16.03% in May. The majority, 52.56%, reaches maturity in 1-5 years. The weighted average LTV of the European Index is 41.44%, also down fractionally from 42.18%.

The figures also show that, among the index's constituents, 15 firms have made capital raisings so far this year in Europe. Listed real estate companies in Europe raised €4.77bn in debt in 2013 to date, more than in all of 2011 and about half of all that raised in 2012.

In a separate study, EPRA's NAV calculations for May showed improvements generally across the 12 markets it measures in Europe. Average discount to NAV in Europe is 3.6%, down slightly from April. UK listed property shares moved to a premium for the first time in recent years to join France, Finland, Belgium and Switzerland. All others remained at average discount to NAV, with Italy lowest at 54.9%, followed by Austria at 45.1% discount. But Greece, in third place, sprang higher to an average discount of under 38% from 43.8% in April, and Nordic listed firms' shares were all improved. Norway proved to be a star performer, bounding ahead to an 18% discount after fully 30% in April.

Germany/Retail real estate

Mondial invests €150m in neighbourhood store portfolio

The recently-established **Mondial KAG** has been busy bundling together a €150m portfolio of convenience stores and local discount grocer/retailers, and says it is planning further investment of the same amount for its first retail *Spezialfonds*.

The portfolio of the *Spezialfonds* **mondial retail funds DI (mondial nahversorgungsfonds DI**) holds 20 assets in what the firm terms "robust" B-locations in Hamburg, Kiel, Flensburg, Hanau, Geltendorf and Altötting, the latter two near Munich.

The biggest asset is a neighbourhood shopping centre that evolved from a conversion from an ex-US military base

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in Hanau near Frankfurt am Main, called *Argonner Markt*. Seven of the assets in northern Germany were sold to the fund from the Itzehoe-based **May Gruppe**. All assets are leased long-term to retail tenants such as **Rewe**, **Edeka**, **Co-op** and **Lidl** with an average remaining lease term of 13 years, and have an occupancy rate of 99%. (The existence of a food retailer as anchor tenant is a key investment criterion). The current annual pre-tax dividend for investors is well above 6.5%, says the Munich-based Mondial.

"Via our German-wide network and the long-term experience of all colleagues, we were able to carry out many deals a lot faster than other competitors that have just entered the market," said CEO **Michael Vogt** (*pictured, right*) who founded Mondial at the beginning of this year. "So far we've made all our acquisitions with our own equity capital, and are successively financing the assets."

The company does not participate in expensive bidding processes for larger portfolios, with costs for due diligence frequently topping several hundred thousand euros. "The whole costs of participating in such auction processes are a write-off for everybody except the final buyer", said Vogt.

Vogt, who was head of Augsburg-based special fund manager **Patrizia Wohninvest** until mid-2011, has obviously learned a lot from how Patrizia has expanded out well beyond its traditional strength of residential property trading. He plans to invest a further up to €500m over this year and next, not confined just to the retail sector. "We also see strong investment potential across several asset classes, including student accommodation, corporate real estate or office properties", he says.

The seven assets sold in to the fund from May Gruppe were all based in northern Germany and are let long-term to Edeka, REWE and COOP. The 25m deal was brokered by the Osnabrück-based **JenAcon**, headed up by **Joachim Arenth**, who have become something of a specialist in bundling and selling warehouse retailing portfolios, and this was their second deal for the May Gruppe this year. May Gruppe itself is a developer of local shopping centres and is currently developing assets at eight separate locations across northern Germany, valued at €49m. The total of 30,000 sqm of retail space is due for occupation by retailers such as Edeka, COOP, **Aldi** and **DM** from July this year onwards.

Germany/Acquisitions

German insurers act on intentions, boost real estate allocations

After several years of threatening to do so, it now really appears as if German insurance companies have put their money where their mouths are and have noticeably increased the allocation to real estate in their asset portfolios since the beginning of 2012. Over the period the average share of real estate has risen from 6.3% to 7.0%, primarily due to investment via the indirect or funds route, according to the latest (6th) *Trendbarometer for Real Estate Investments* published by consultants **Ernst & Young**.

If the surveyed insurance companies carry through on their stated intentions, that proportion is set to rise to 7.6% by the end of 2013, with the favoured destinations for all this largesse being Germany and - perhaps a little surprisingly – North America. (insurance companies are allowed by law to allocate up to 25% of their assets to real estate, so theoretically there is plenty of upward scope).

First, some figures. German insurers currently have about 90bn invested in real estate, while the entire amount invested by German insurers in all asset classes was about €1.3 trillion at the end of 2012. On average, every big German insurance company holds €2.6bn of real estate assets, of which €1.8bn are held directly and €0.8bn are held indirectly, according to the Ernst & Young Trendbarometer.

The study found that company board members surveyed claimed yield expectations of between 4.9% (for direct) and 5.5% (for indirect), although **Dietmar Fischer**, partner at Ernst & Young in Germany conceded at a recent press briefing in Frankfurt that these figures were at the 'optimistic' end (i.e. rarely achieved…).

Still at the top of the preferred shopping list for insurers are (German) retail, offices and then residential, while offices is the category most would consider selling. The preferred category in all segments is – inevitably – core. However, the lack of core product and the need for higher returns means they are forced to move up the risk curve. Some 77% of those surveyed said they are planning to invest in core-plus, up from 65% in 2012, and 45% in value-add, up from 35%.

Respondents said that inflation was not a core issue for them (not one of their top five concerns). "Insurers are not worried about it any more, in stark contrast to private wealth investors, for which inflation is still the main driver for real estate investments," said Fischer.

German insurers are particularly focused on direct investments and open-ended Spezialfonds and more are looking at developments and international open-ended funds again. In terms of regions, Germany still remains top of the charts, with 91% planning investment in their home market, followed by Europe ex-Germany at 57%, down from 70%. North America is named by 52% of respondees, up from 20% last year, with most believing that the US has now put the worst behind it.

Germany/Managed Care

Research group Pestel warns on subsidies for elderly care

The Hanover-based market research institute **Pestel** has just published a new study highlighting a massive shortfall in the number of homes suitable for elderly people across Germany over the coming years, and is calling on the government to provide new funding to cover the widening gap.

According to Pestel, Germany will need to build or adapt 2.5m further homes accessible to old people over the coming year, which the researchers believe will cost nearly €40bn. They conclude that the government will need to provide additional funding of €540m annually over the next eight years – or €4.3bn by 2021 – to provide the right incentives for investors to convert enough existing homes to meet the demand. The alternative, they say, is a huge wave of old people with no alternative but to move into a much more expensive care home, whether they can afford to or not.

Researcher **Matthias Günther** of Pestel-Institut, who carried out the study on behalf of **Verbändebündnis Wohnen65plus,** (a lobbying group consisting of several influential industry associations and trade unions), said that elderly people in need of care are being increasingly forced to go into nursing homes if they don't have the adaptation to their own homes as a minimum for their own care needs.

Talking to trade publication *Immobilien Zeitung*, Günther said the difference in annual costs between outside care and adaptation of the old person's existing home was €7,200 a year, while the one-off adaptation costs to make an existing home elderly-friendly is an average of €15,600. The economic justification for making the necessary changes is clear, he says. Without funding for such improvements, he says, home care for the elderly will be €25bn higher in 2035 than they are now, and health insurance

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

Don‘t regurgitate – reflect

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We are all familiar with the wisdom: „Do not trust statistics you haven‘t falsified yourself.“ Conversely, we should occupy ourselves with the details before bothering with statistics. We are frequently all the more astounded, when politicians, journalists, and even industry figures, gullibly quote from statistics and studies, without ever having subjected them to closer scrutiny. Understandable enough – after all, such supposedly cast-iron figures imply a degree of competence and make statements appear bulletproof. A handy example of this is the current, election-campaign-driven debate surrounding the new housing need in our Republic‘s conurbations. Here, for example, in a postulated scenario, Berlin‘s Senate anticipates that the capital city could see net population growth of around 400,000 over next ten years. In the words of the responsible undersecretary to the Senator for Urban Development, the consequence of this would be that „we‘d need to build until breaking point“.

However, this „breaking point“ recently took a knock when the German Federal Office of Statistics published the results of the 2011 census, which showed there were 1.5 million fewer people living in Germany than had been assumed to date. And now the interesting part: Which are the cities with the lowest vacancy rates according to the German Federal Office of Statistics? One would presume they are Munich, Hamburg, Frankfurt and Berlin. In reality, however, only Hamburg appears in the Top 3, sharing the top spot with Oldenburg: 1. Oldenburg (1.5% vacancy)/Hamburg (1.5%), 2. Münster (1.6%), 3. Jena (1.9%).

One other intriguing fact revealed by the census is that Germany‘s two largest cities – Berlin and Hamburg – have 5.2% and, respectively, 4.6% fewer inhabitants than was previously supposed. In a similar vein, nationwide, there are also 500,000 more apartments than assumed.

So, what do all these figures tell us? In order to understand them, one must immerse oneself in them – for it is beyond denial that there are problems with affordable housing in Berlin, Hamburg and Munich. However, this does not mean all of Berlin, all of Hamburg or all of Munich. The old real estate wisdom that location is decisive also applies here. Expressed in exaggerated terms: If everyone wanted to live in Berlin-Mitte, in Munich-Bogenhausen or on the shores of Hamburg‘s Binnenalster, then it would also be reflected in the price. At the same time, there is affordable housing available in Berlin-Marzahn, Munich-Hasenbergl or Hamburg-Langenbek.

What do we learn from this? One wisdom that we, as VALTEQ, also apply in all business activity: The details are decisive! In order to arrive at a good solution, one must get to grips with the project and the seemingly incontrovertible facts and figures. Or, to put it in a nutshell: Don‘t regurgitate – reflect!

to pay for it all will have to rise by 50% above today's levels.

The Pestel report makes the case for direct building subsidies and tax incentives in addition to the KfW loans at favourable rates available to house-owners for energy and other home improvements, to stave off what it sees as a pending housing crisis for the elderly. Loans alone won't solve the problem, the researchers believe. "For most seventy year-olds, taking out a twenty-year loan isn't a compelling option", says Günther.

Günther also believes that part of what the report is calling for in terms of financial assistance is also offering suitably-equipped smaller apartments at very modest rents to old people, a factor looming ever larger against the increasing poverty of many of Germany's elderly. His research suggests that in 20 years time more than 25% of Germany's elderly will be dependent on the state for basic subsistence, up from the mere 3% who are in that situation today.

While affordable housing is gearing up to be the single key issue of the coming national parliamentary elections in September, the Verbändebündnis lobby group says the issue of housing for the elderly is not receiving nearly enough attention, and certainly not the cost-saving measures critical now to avoid much heavier expenditure later. In a statement the association said, "The current government has effectively wiped its hands of the issue of adequate construction and adaptation of housing for the elderly, and the original pot of €100m in **KfW** subsidised funding has been whittled down to zero."

Meanwhile, a study produced on the market for housing for the elderly by **Patrizia Immobilien** pinpoints good investment opportunities - particularly in German provincial regions, such as Mecklenburg-Vorpommern and Saxony in the east, and North Rhine-Westphalia in the west. Managed care homes in these states are already operating at close to full capacity, at more than 90%.. **Karin Siebels**, the author of the Patrizia study, says that, "In the individual urban and rural districts of these regions, the number of home residents will rise by between 2,000 and 20,000 by 2030." In particular, she says, cities such as Cologne, Recklinghausen, Dortmund, Aachen, Esslingen, Ludwigsburg and Karlsruhe, extensive parts of Mecklenburg-Vorpommern in the north-east, as well as south-eastern Saxony, are all ripe for investments.

By contrast, regions such as southern Rhineland-Palatinate, northern Hesse and Lower Franconia are barely utilising 70% of existing nursing home capacity, the study shows, highlighting the strong regional differences.

Patrizia uses a proprietary scoring system for identifying investment opportunities. Key criteria are the level of utilisation, projected population growth and demand for easy access housing, all influenced by the number of over 80-year-olds. By 2030, their share of the total German population will almost double to 9%.

"There are wide variations from region to region as to how rapidly the population is aging," said Siebels. In some areas of Thuringia and Saxony, every eighth resident will be over 80 in 2030, as opposed to a maximum of 6% of residents in the university cities. The larger cities will also see rising numbers of elderly people, especially in and around Hamburg, Hanover and Munich. "In Berlin, for example, the number of elderly in need of nursing home care will rise by more than 20,000 in the next 15 years," she said.

Germany/Asset Management

Corpus Sireo launches new asset manager for retail sector

With German retail real estate making up 36% of all commercial investment in the country last year, it was probably only a question of time until Cologne-based **Corpus Sireo** fixed its gaze upon the sector and set up its own asset management division focused exclusively on retail. Not surprisingly, therefore, it recently announced it was doing just that.

Corpus Sireo Asset Management Retail, also to be based out of Cologne, immediately set its sights on becoming one of the top three providers for asset management services, a position it holds in both the commercial and residential segments.

The core team of the new retail division will be headed by **Thorsten Prior** and made up of an experienced group transferring from **MFI Management für Immobilien AG**, a shopping centre specialist, where it built up a portfolio including six shopping centres valued at €1.7bn and brought in substantial third-party business.

Prior commented on the new division, "With the recently acquired **Treveria** mandate and the retail properties that Corpus Sireo manages within the framework of other mandates, we are off to a fresh start, now working with the asset management market leader in the retail market. There is enormous interest in German retail real estate."

Corpus Sireo is already the largest asset manager in the country, with €16.2bn in assets under management, and a staff of 560 at eleven locations throughout Germany. It also acts as a broker and developer for owner-occupiers and investors.

Prior's comment on Treveria refers to the decision by listed British specialist retail investor Treveria to throw in the towel on its German operations following renewed losses for 2012 of €135m. Tre-

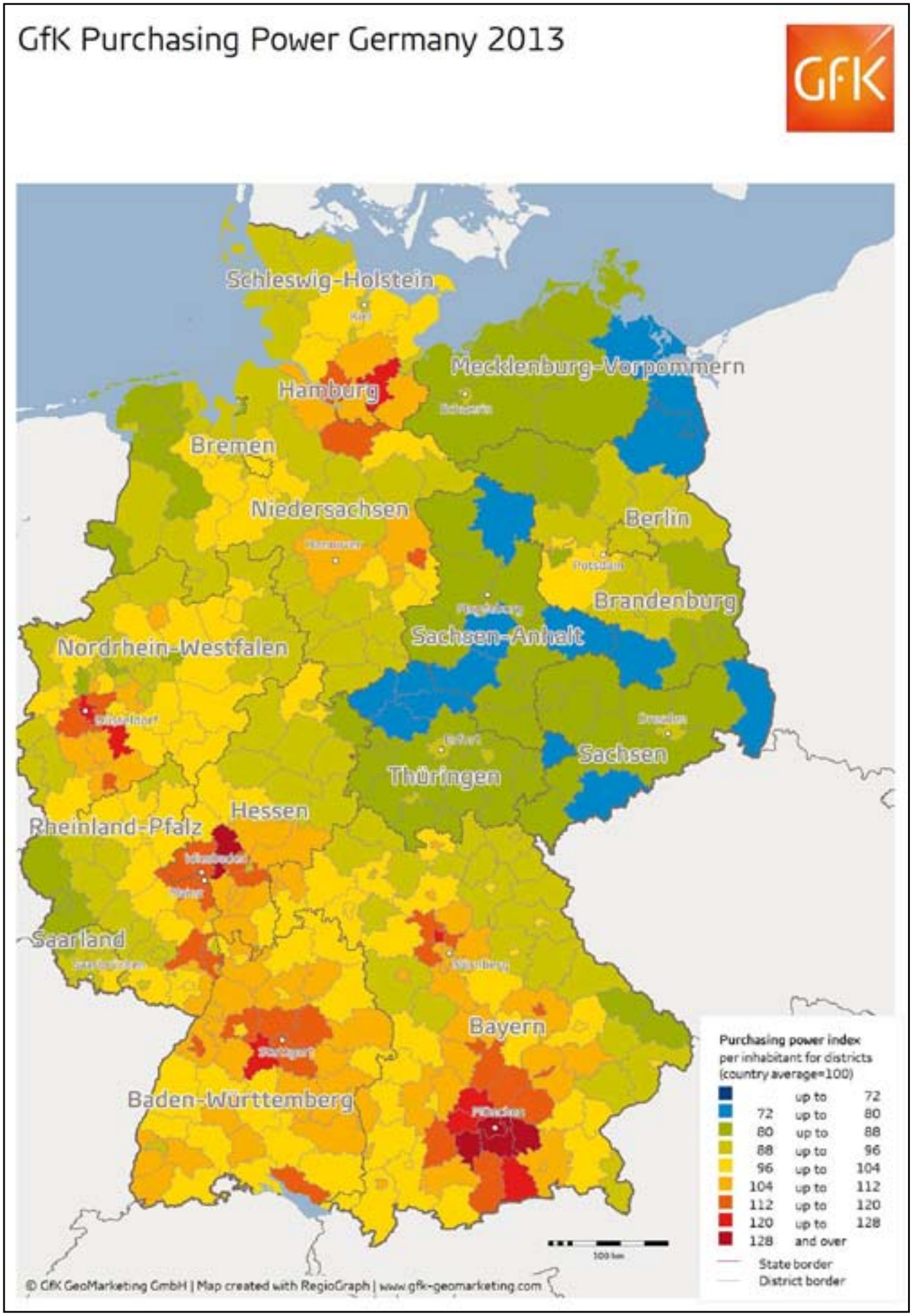


Illustration: GfK GeoMarketing

...from page 23

veria's wind-down is currently being led primarily by board member **David Malpica** and his own separate company **Kewbrige Capital Ltd**. The bulk of Treveria's German assets have for some time been managed by external managers such as Corpus Sireo and **CR Investment Management**.

Germany/Residential

Luxembourg's Grand City targets €200m German residential

The Luxembourg company **Grand City Properties** plans a further investment spree of €200m to add to its German residential holdings. From its German headquarters in Berlin, the group manages about 16,200 residential units with a gross lettable area of more than 1.2m sqm, primarily in Berlin itself and in North Rhine-Westphalia. The next wave of acquisitions will target properties in Nüremberg, Dresden, Leipzig, Mannheim and Bremen – with at least 5,000 units in the immediate pipeline, says the company.

Board member **Christian Windfuhr** says the short-term goal is to head past the 20,000-unit mark over the next six to nine months, and the group has a war-chest of €200m for the right assets, partly funded by a recent private capital placement and a €90m convertible bond. The group is targeting portfolio sizes of between 300 and 2,000 units, with upside potential on both the vacancy rate and the rent levels.

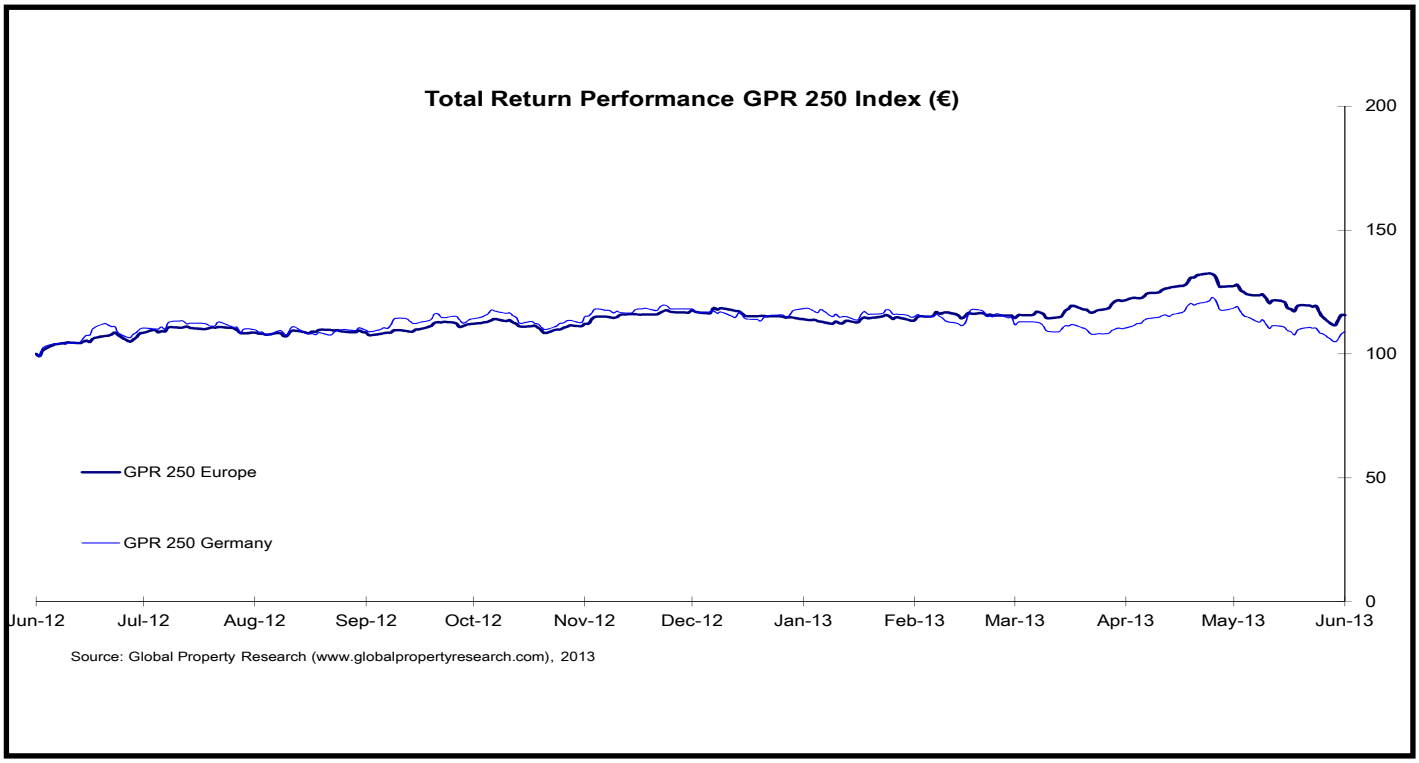
Germany/Open-ended Funds

Fund volumes, returns grow despite heavy open-ended fund sell-offs,

New investments into the German open-ended funds sector are now offsetting the liquidation effect of the funds forced into liquidation, and are generating solid returns for investors of between 2% and 3% for investors, the latest figures from the **IPD** monthly **OFIX** index show.

Compared to May 2012, index volume has decreased by €2.6bn. or 3.4%, as a result of fund liquidations. Ten out of 22 OFIX funds have entered liquidation, and their fund volumes have decreased by 4.9bn compared to last year. These vehicles are now worth €18.1bn. and account for 24.7% of the OFIX index. The OFIX index covers 22 funds targeting retail investors, with a total value (NAV) of €73.4bn.

Despite their high level of coverage by the media, liquidating funds actually account for less than a quarter of the market, and for the bulk of the market fund volumes grew. In terms of returns, those ten funds in the OFIX index that have entered liquidation returned -3.9% over the last twelve months and -4.1% over the last three years on an annual basis, while the twelve funds that are open for new investment returned 2.2% in the last year and 2.3% per annum annualised over



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

the last three years. "The market remains split between active funds and funds in liquidation, but new investments now offset the liquidation effect," said IPD Germany's **Daniel Piazolo** *(pictured, right)*. "Active funds return between 2% and 3% p.a., and investors appreciate this."

Losses for liquidating funds

So, how are the liquidating funds faring as they move towards their five-year goals of selling off all their assets?

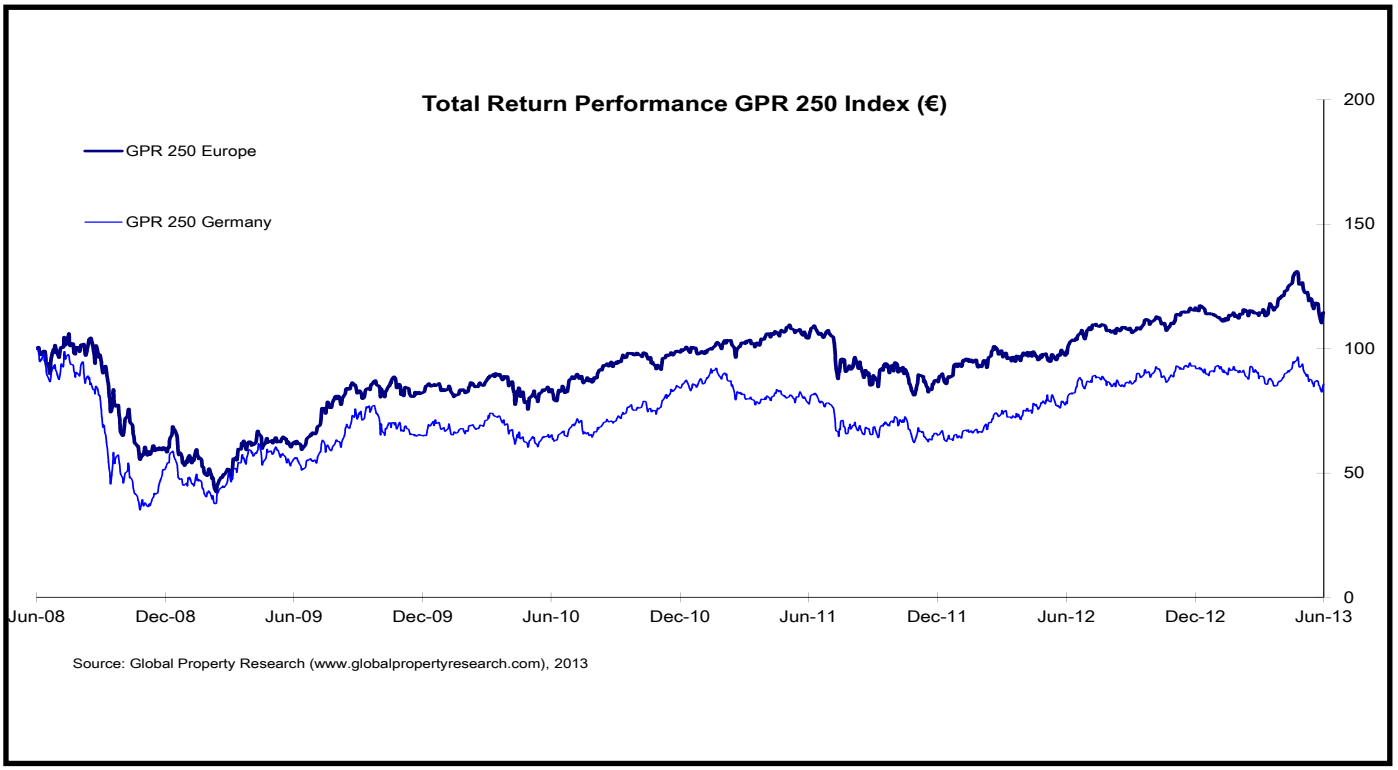
SEB Immoinvest has just made its latest payment to shareholders, distributing another €368m and bringing total payouts to €1.7bn or 30% of its assets. The fund only started liquidation in May 2012. The latest payout came from proceeds of sales including the disposal of a Berlin portfolio to Canadian REIT **Dundee International**, two Berlin hotels to the **ARTIC** subsidiary of Qatari group **Al Faisal Holding**, and a further two individual properties in Berlin and Prague.

AXA Immoselect, which is also in the process of unwinding its holdings, has been aggressively discounting its assets in the interests of a speedy sale. It has recently sold most of its asssets in the Netherlands, an office in France and an office in Germany for about €300m, accepting discounts of up to 48% on their most recent (German accounting) valuations.

Its French office in Colombes near Paris was marked down 21% to 126m, "to reflect the challenging leasing situation of the asset", the company said, given 2.2 years left of lease life and plenty of new competition in the vicinity. Also selling for a 21% discount on book value at €31m was AXA's *Grafenberger Höfe* dual office complex in Düsseldorf, which is facing the departure of its anchor tenant in December 2018.

In the Netherlands the €2.1bn fund sold most of its Dutch portfolio to an unnamed private investor for €140m, a hefty 48% discount on its most recent book valuation, due to the troubled nature of the Dutch office property market. The portfolio consists of six office buildings in what were considered B-locations in Amsterdam, Den Haag, Arnhem, Rijswijk and Rotterdam and one 14,000 sqm retail asset in Dronten with an average lease term of six years and a vacancy rate of 20%. Property advisor **Cushman & Wakefield** organised the structured sales process for the portfolio, which went to the highest bidder. At the price paid by the buyer, the gross initial yield is 12%.

AXA is under time pressure to liquidate the fund completely by October 2014, and said it took the view that in the Netherlands with its hefty office space overhang, the situation was unlikely to improve substantially in the short- to medium-term.



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/Financing

Alstria, DIC Asset tap bond markets for fresh funds

Two of Germany's top listed real estate companies have opted this month to tap the bond markets as a source of fresh finance, as an alternative to their more traditional route of raising capital through a scrip issue to existing shareholders.

Hamburg-based **Alstria Office REIT** said its issue of a five-year senior unsecured convertible bond was well oversubscribed and it had raised €79.4m through the placement. The issue was priced at a coupon of 2.75% and at a conversion premium of 15% above the reference share price of €8.76. The bonds, each with a denomination of €100,000, will be convertible into 7.89m ordinary shares of Alstria, or about 10% of outstanding equity.

The deal should be good for Alstria, whose overall financing costs are still about 3.9% and whose net loan-to-value ratio is 46.8%, as it will lower its overall cost of finance and help it raise its equity level. Shareholders were less than enthusiastic at the dilution of their stake and have been marketing the stock down since the issue. **Bank of America Merrill Lynch** and **JP Morgan** acted as joint bookrunners with **UniCredit Bank** as co-bookrunner.

Meanwhile, also tapping the bond markets for an alternative to bank debt or mezzanine loans is Frankfurt-based commercial property investor **DIC Asset AG**, which is issuing a new unsecured bond, tradable in Frankfurt from July 9th. The company's second five-year corporate bond will have a volume of at least €100m and will be listed in the *Prime Standard* for corporate bonds on the Frankfurt stock exchange. The proceeds are "to refinance existing bank debt on the portfolio as well as for general corporate purposes", its prospectus says.

The bond is being issued through a public offering in Germany, Luxembourg and Austria as well as through a private placement with select international investors. Joint bookrunners are **Bankhaus Lampe KG** and **Baader Bank AG**. It is paying a coupon of 5.75%, just slightly lower than the 5.85% payable on its earlier likewise €100m bond. CEO **Ulrich Höller** (*pictured, below*) commented on the new issue: "The planned issue will help us to base our debt financing on an even broader basis and to expand our financial leeway. We're taking advantage of the high degree of flexibility and the proven cost effectiveness of this financing instrument in line with our mid- and long-term corporate objectives."

Höller said that the issuing of the bond will permit further optimisation of the DIC Asset's financing conditions by reducing its bank debt on the portfolio and property level. On this level, the issue proceeds can be used as equity, and therefore serve as an attractive alternative to classic junior or mezzanine loans. That way, the overall debt level and the net debt equity ratio of the company remain unchanged.

Germany/Managed Care

Belgian REIT Aedifica enters German senior housing market

We report elsewhere in this issue on new studies focused on the market for managed- and elderly care homes in Germany, and looming shortages in Germany's regions. This month saw the first move into the German market by Belgian REIT **Aedifica**, who in addition to furnished and unfurnished residential housing and hotels, also specialises in senior housing in its home market, where it is the second-largest investor.

Brussels-based Aedifica paid about 8m for a recently-completed property, *Seniorenzentrum AGO Herkenrath*, located in Bergisch-Gladbach, near Cologne in North Rhine-Westphalia. The facility is operated by AFO and has 80 beds. The initial gross rental yield was 7.25%.

Commenting on the deal, Aedifica's CEO **Stefaan Gielens** said, "Investing in German rest homes is the logical next step in Aedifica's effort to diversify its assets within its main strategic segment, collective senior housing. Germany presents a significant investment opportunity in this segment: it offers the largest European market,and an even stronger demographic trend toward an ageing population than in Belgium.

"Care operators continue to grow and consolidate and, as in all western European countries, the need for financing solutions for real estate infrastructure in the healthcare sector will inevitably grow. Finally, Germany offers the best risk profile of any country in the Eurozone."

Aedifica in Belgium has a total of €620m of assets under management, including development projects valued at €20m. In the senior housing sector, it traditionally operates through sale-and-leaseback agreements or by investing in new projects. It negotiates long-term indexed and irrevocable contracts, normally a minimum of 27 years, with specialised operators. Belgium's laws have just recently been amended to permit residential REITS to buy assets in other European countries.

Germany/Banking

Fitch sees German 2013 commercial property bank profits in line with last year

Ratings agency **Fitch** produced one of its regular reports earlier this month on the German real estate banking sector, and seemed to have a slightly sharper tone than usual in REFIRE's view, highlighting several banks' lack of a retail base in

pointing to financing bottlenecks ahead.

Fitch says in its report that specialised German commercial real estate (CRE) banks will continue to benefit from benign market fundamentals in their home market and stronger neighbouring markets, although exposure to Spain and Italy will likely lead to higher loan impairment charges.

"Their lack of stable deposits will make it difficult for some banks, especially independent ones, to meet the net stable funding ratio requirements under Basel III, although the rules are still in flux," says **Markus Schmitt**, associate director in Fitch's Financial Institutions group, in the report. Some banks, including Munich-based **Hypo Real Estate**, have now started to take retail deposits, although the level of intakes is still very modest.

The drivers of the 'benign' real estate climate are identified as a low interest rate environment, low domestic unemployment, increasing private consumption, attractive yields, and inflation fears, which cannot yet be seen, resulting in value-preserving property investments. In addition, low, albeit increasing, construction activity, net migration to metropolitan areas and an increasing number of households are fuelling demand for living space, while foreign investors are showing substantial interest in buying German property.

Furthermore, say the researchers, German commercial real estate lenders have been able to realise increasing gross margins in new business due to less competition and a re-pricing of credit risk in the past few years, although further increases will be difficult to achieve as new and old players are attracted by margins which reflect a multiple of pre-2008 lending conditions.

The study's conclusion, phrased in the same somewhat soulless language of the rest of the report, is that Germany's specialised CRE lenders should achieve 2013 profits in line with last year's. The Fitch view is that "current underwriting standards are sound as loan to value ratios for new business have decreased and have ranged between 55% and 65% in recent quarters, resulting in attractive returns on risk-adjusted capital. In addition, refinancing pressure from high CRE loans outstanding or accelerated liquidation/restructuring of assets from the resolution of German open-ended funds or German CMBS is currently no material threat for domestic property prices.

Germany/Legislation

Real estate bodies condemn German political plans to cap residential rents

There has been widespread real estate industry condemnation of the plans to cap German residential rents (known as the *Mietpreisbremse*), now being subscribed to in the pre-election run-up by all the major parties except for the liberal **FDP**, currently coalition partners with Angel Merkel's **CDU/CSU** alliance.

In Germany the employer-friendly **Institut der deutschen Wirtschaft** in Cologne (IW Köln) described the measure as "unfit for purpose" and "barely justifiable", and more likely to "scare off investors and magnify the housing shortage in the larger cities", they say.

The **Royal Institute of Chartered Surveyors RICS** also entered into the debate, saying in a study carried out by its Professional Group (PG) Residential Property that negative effects of the proposed rental cap legislation would certainly outweigh the positive aspects.

Only very few market participants will profit from the planned legislation, said PG head Oliver Moll, these being some tenants in the biggest cities, where the housing problem is the most acute. "But the measure may have a long-term detrimental effect on Germany's entire property market and would lead to market distortions achieving the exact opposite of what the politicians are aiming for. "

UPCOMING EVENTS AND CONFERENCES

EVENTS/ CONFERENCES Summer 2013

July 3rd-6th, Wednesday - Friday
ERES, Vienna, Austria,
Bringing together top level decision-makers along with researchers and educators in real estate and closely allied areas, the European Real Estate Society ERES, founded in 1994, encourages the exchange of information and promotes development in Europe and around the world
More at www.immobilien-forum.com

September 12th-13th, Thur-Friday
Die Industrie-Immobilie, Cologne, Germany
Organised by IIR Conferences, the inaugural edition of the event examines the role of industrial property- a new asset class? Third-party usage, energy, efficiency concepts, new developments, market data, and more. First-class line-up of top German players, attendance includes optional visit of Carlswerk Industrial Park. German language conference.
More at www.iir.de/industrieimmobilie

September 18th, Wednesday
Real Estate Private Equity Summit, Waldorf Hilton, London
Organised by iGlobal Forum, the summit will offer an ind-depth understanding of the structural changes in European real estate. Alternative finance, prime markets, long-term structural trends, and more.
More at www.iglobalforum.com

October 14th-15th, Monday-Tuesday
IMN's European Real Estate Opportunity & Private Fund Investing Forum, London
Now in its 14th edition, the event is annually attended by 400-500 delegates, this year running at One Great George Street concurrently with the European edition of IMN's Real estate CFO Forum.
More at www.imn.org

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Our readers are global investors in real estate, asset managers, REITs and other real estate investing vehicles, lawyers, private investors, public sector authorities – in short, anybody who is interested in staying up-to-date with and learning more about real estate finance in continental Europe.

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