INITIATIVE
UNTERNEHMENS
IMMOBILIEN

bulwiengesa

MARKET REPORT NO. 1

FIRST HALF-YEAR OF 2014

TRANSPARENCY ON GERMANY'S
INDUSTRIAL REAL ESTATE MARKET

CONTENTS

WELCOME TO GERMANY'S INITIATIVE UNTERNEHMENSIMMOBILIEN

What the working spheres of tomorrow and the associable changes in the corporate demand for space will look like is quite predictable today. The introduction of the Internet of Things into the production cycle has initiated the fourth industrial revolution. Going forward, products will be connected with all systems and players involved in the respective manufacturing process across the entire product life cycle via interactive networks. Accordingly, the building corpus for this so-called Industry 4.0 will have to be increasingly flexible and multifunctional.

Industrial real estate offers ample space for meeting the challenges emerging in the German economy. While these represent a rather recent concept for the German real estate industry, they have quickly evolved into an up-and-coming asset class characterised by growing potential. The flexible work environment provided by industrial real estate lends itself to a wide variety of use types: The office, light manufacturing, warehouse, logistics, service and open spaces available on the market, while varying in volume, may generally be combined in modules depending on the intended use type and use period. In other words, users may freely pick the accommodation that is most likely to ensure efficient workflows for them.

In 2010, bulwiengesa became the first research agency that explicitly identified the segment of industrial real estate in a joint survey on the subject of commercial and industrial real estate. In the years since, the segment has undergone a dynamic development, and keeps getting more and more interesting not just for occupiers but for investors as well. Especially against the background of diminishing returns and shortening cycle times in the established real asset classes, industrial real estate is gaining increasingly in significance as investment alternative. So far, the yield upside of industrial real estate remains largely untapped, not least because the available market information continues to lack transparency.

This shortcoming is precisely where the INITIATIVE UNTERNEHMENSIMMOBILIEN comes in. The German Term UNTERNEHMENSIMMOBILIEN can be interpreted as industrial real estate. The stated purpose of the INITIATIVE is to enhance the transparency on the German market for industrial real estate by publishing this Market Report and facilitating access to this asset class in the process. It is the first issue of a semi-annual series that from now on will deliver semi-annual market updates to decision makers, investors, companies, and industry insiders. What makes the report special is its approach: Rather than relying on secondary sources, it uses data that are directly provided by the owners. These are objectively processed and sometimes augmented by data from bulwiengesa's RIWIS database. This enhances the quality and accuracy of the data in mapping the market. The first issue of the market reports takes a close look at the market trend in 2013, and analyses market activities during the first six months of 2014.

The INITIATIVE UNTERNEHMENSIMMOBILIEN currently consists of the eight most important actors on Germany's industrial real estate market as well as Germany's leading independent market research company for industrial real estate.

These are the companies collaborating in the INITIATIVE UNTERNEHMENSIMMOBILIEN:

ATOS | aurelis Real Estate Management | BEOS | Hansteen

GSG BERLIN | SEGRO WHERE BUSINESS WORKS | Sirius facilities | VALAD

WHY "UNTERNEHMENSIMMOBILIEN"?

Companies will have to adapt to the shifting parameters that future innovations are likely to bring. The shift will also have ramifications for the properties they occupy. Innovations in technology and production keep lowering the pollution emitted by manufacturing processes. This in turn clears the way for moving production facilities back closer to downtown or to residential areas. Accelerating shifts in demand that are driven by steady innovation, especially in technical terms, and by increasingly bespoke client requirements result in smaller production runs. In order to prepare for the changed situation, companies require customisable accommodation that is both reversible, i.e. permit quick conversions, and scalable. Owning the occupied property outright tends to be a liability rather than a benefit, as it may hamper quick, cost-effective adjustments. Opting for industrial real estate within a letting solution represents the perfect alternative.

So far, the potential of this property type has hardly been exploited by German companies, and the ownership rate remains very high compared to other countries. Recent analyses show a ratio of about 75% for Germany, whereas the going rates in Asia and North America range from 20% to 30%.[1] Then again, the attitude has begun to shift even in Germany. The supply in high-end industrial real estate is growing steadily, while providers are showing an increasingly professional approach. Clever asset management creates investment assets with stable rental income, making it an attractive proposition for investors, too.

WHAT ARE "UNTERNEHMENSIMMOBILIEN"?

The term industrial real estate refers to mixed-use commercial properties, typically with a mid-market tenant structure. Types of use typically found include office, warehouse, manufacturing, research, service and/or wholesale trade and open space.

Industrial real estate covers four different real estate categories:
· Transformation property
· Business parks
· Light manufacturing
· Warehousing / logistics property

All four of these categories are characterised by alternative use potential, reversibility of use and a principal suitability for multi-tenant structures. This means that the forte of industrial real estate is its flexibility, and this not just in regard to its use but also in regard to its occupiers.

Transformation property:
· converted and revitalised commercial properties
· mostly former production plants or brownfield sites with potential for further densification
· often invested with the special charm of an historic industrial ambience (red-brick character)
· often located relatively close to downtown for historic reasons
· often conveniently accessible by private and public transportation
· often a mix of revitalised period buildings and newly constructed buildings
· all types of floor space available

Business parks:
· usually planned and raised to be let to specific companies
· composed of several distinct buildings forming a cluster
· uniformly organised management and infrastructure
· providing any floor area type (with and office share generally between 20 and 50%)
· usually in suburban locations with easy accessibility

Warehouse / logistics property:
· mainly existing schemes with predominantly simple warehousing options and some general purpose accommodation
· in the industrial real estate context distinguished from modern logistics warehouses by a size limit of 10,000 sqm maximum
· different fit-out and quality standards
· flexible and affordable types of floor space
· usually reversible and eligible for higher-spec occupiers (e.g. by retrofitting ramps and gates)

Light manufacturing property:
· mainly one-off warehouse properties with minor office share
· suitable for a variety of manufacturing types
· warehouse areas principally eligible for other types such as storage, research, and services, as well as for wholesale and retail purposes
· alternative use potential depends essentially on the location

[1] Pfnür, A., 2014: "Volkswirtschaftliche Bedeutung von Corporate Real Estate in Deutschland"

THE VARIOUS CATEGORIES OF INDUSTRIAL REAL ESTATE

ASSET CLASSES

Industrial real estate as alternative asset class	Established asset classes in the real estate sector
Wide variety of occupiers from various industries	Usually just one occupier
Variable mix of use types	Mostly uniform use type
High-level reversibility of use	Low-level reversibility of use

Industrial real estate	Risk of vacancy
Transformation property	
Business parks	
Warehouse / logistics	
Light manufacturing property	

Established asset classes	Risk of vacancy
Retail property	
Office property	
Hotel property	
Special/operator property	

Example for flex space units

Modern "smart office" concept at a business park

EXAMPLES FOR INDUSTRIAL REAL ESTATE

TRANSFORMATION PROPERTY

TIB TECHNOLOGIE- UND INNOVATIONSPARK BERLIN
Address: Gustav-Meyer-Allee 25, D-13355 Berlin
Owner: GSG Berlin
Total area: 109,184 sqm
Types of floor space: office, lab, warehouse, logistics, service and shop space (flex space)
Target group: high-tech companies, software / IT, information and communication companies, manufacturing industry

TRANSFORMATION PROPERTY

SIGMA TECHNOPARK AUGSBURG
Address: Werner-von-Siemens-Strasse 6, D-86161 Augsburg
Owner: ATOS
Total area: 112,670 sqm
Types of floor space: office, lab, warehouse, production area
Target group: high-tech companies, software / IT, information and communications companies, manufacturing industry

BUSINESS PARK

DÜSSELDORF RHEINPARK
Address: Bonner Strasse 317-363, D-40597 Düsseldorf
Owner: SEGRO
Total area: 50,517 sqm
Types of floor space: office, warehouse, production, and service area
Target group: small and medium-sized enterprises, retail, manufacturing industry, logistics

BUSINESS PARK

GLINNKAMP BUSINESS PARK
Address: Wilhelm-Bergner-Strasse 1-9, D-21509 Glinde
Owner: BEOS
Total area: 52,497 sqm
Types of floor space: office, warehouse, production, and service area
Target group: small and medium-sized enterprises, retail, manufacturing industry, logistics

EXAMPLES FOR INDUSTRIAL REAL ESTATE

BUSINESS PARK

SIRIUS BUSINESS PARK BONN-DRANSDORF
Address: Siemensstrasse 36, D-53121 Bonn
Owner: Sirius Facilities
Total area: 20,000 sqm
Types of floor space: office, warehouse, workshop and service areas, flex space
Target group: start-ups, small and medium-sized enterprises, manufacturing industry, logistics

LIGHT MANUFACTURING PROPERTY

SIEMENS MANUFACTURING PROPERTY CONSTANCE
Address: Bücklestrasse 1-5, D-78467 Constance
Owner: Valad
Total area: 60,282 sqm
Types of floor space: office, production, warehouse space
Target group: manufacturing industry

LIGHT MANUFACTURING PROPERTY

LIGHT MANUFACTURING AM NORDRING
Address: Am Nordring 20-30, D-80807 Munich
Owner: aurelis
Total area: 18,723 sqm
Types of floor space: office, production, warehouse space
Target group: manufacturing industry, industrial, production

WAREHOUSE / LOGISTICS PROPERTY

WAREHOUSE / LOGISTICS PROPERTY (HANSEPARK)
Address: Hansestrasse 61-63, D-51149 Cologne
Owner: Hansteen
Total area: 13,479 sqm
Types of floor space: warehouse, logistics, office units
Target group: wholesale trade, automotive and auto suppliers, information and communication companies

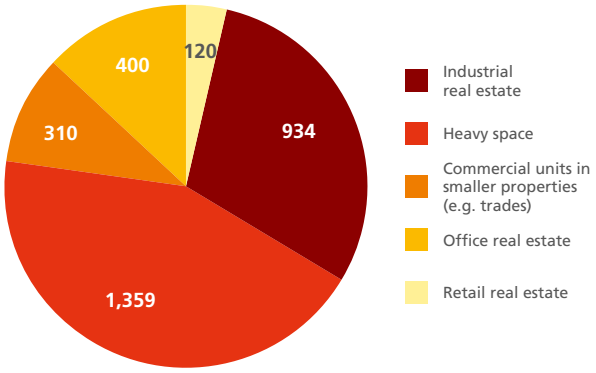
THE MARKET FOR INDUSTRIAL REAL ESTATE IN GERMANY

The stated goal of the INITIATIVE UNTERNEHMENSIMMOBILIEN is to enhance the transparency of the asset class of industrial real estate and to make it more accessible thereby. With this in mind, eight leading market participants that are active as operators, property developers, investors, and asset managers in this class joined forces at the very start of the INITIATIVE. The research end of the market data polling process is handled by bulwiengesa, a leading research agency that has monitored this real estate segments for years. The market data of each market player was matched by bulwiengesa with its extensive data pool, and analysed independently. This Market Report maps the market information of the entire year 2013 and of the first six months of 2014. Going forward, the reports will deliver semi-annual updates on the latest market activity. Upcoming market reports will successively expand its scope and drilldown depth over time. The INITIATIVE encourages queries and analysis requests in order to engage in an open dialogue. So if you are a market player in this field, do get in touch with us.

INDUSTRIAL REAL ESTATE ACCOUNTS FOR 30% OF GERMANY'S COMMERCIAL PROPERTY STOCK

The ongoing market observation by bulwiengesa has determined a current commercial floor space total (not including hotels) of well over 3.1 billion sqm in Germany. At well over 934 million sqm or nearly 30%, industrial real estate represents the second largest group after industrial property.

Fig. 02: Floor space total of commercial property in Germany, not incl. hotels, in million sqm, H1 2014



The market value of industrial real estate equals 543 billion euros or more than 26%, barely less than office real estate, which accounts for 600 billion euros or around 29%. This highlights the high net asset value of this asset class, and thus its potential.

Fig. 03: Market value of commercial property in Germany, not incl. hotels, in billion euros, H1 2014

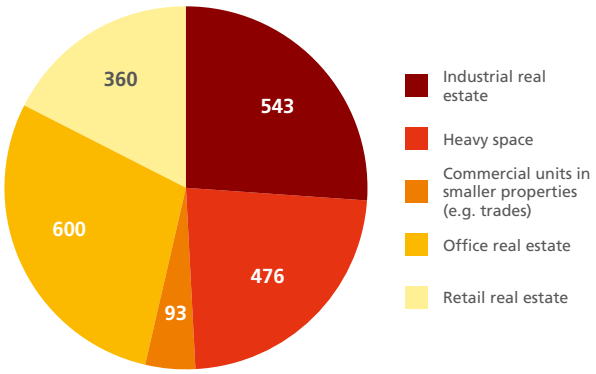
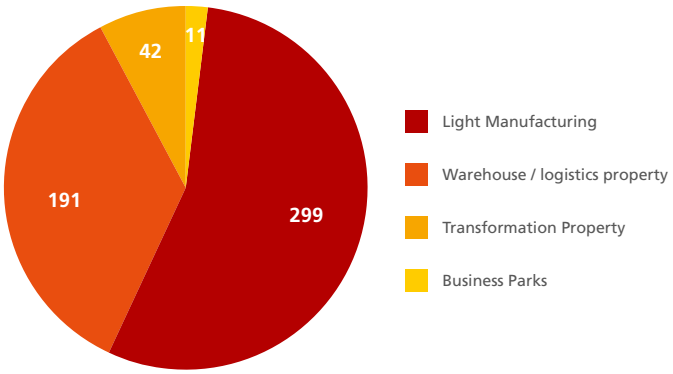


Fig. 04: Market value of the property categories of industrial real estate in H1 2014



[2]The figures are based on the stats published by the IW Economic Institute in Cologne in its publication "Wirtschaftsfaktor Immobilien – Die Immobilienmärkte aus Gesamtwirtschaftlicher Sicht (2010/2013)" and on forward projections for selected property types using the real estate databases of bulwiengesa AG

A breakdown of the different property categories within the industrial real estate segment reveals a striking dominance of light manufacturing properties. The account for 58% of all units and 55% of the total market value of the industrial real estate. That said, only around 40% of the light manufacturing property stock qualifies as investment-grade assets. Since these properties were often built to specification to accommodate a certain manufacturing process, many of them show a low level of reversibility of use or alternative use potential. The category is also defined by owner-occupiers. This explains why such property is rarely put on the market.

Fig. 05: Overview of accommodation and values of German industrial real estate in H1 2014

Property category within the sector of industrial real estate	Floor space in million sqm		Total value		thereof investment-grade	
	H1 2014	in %	in bn euros	in %	in bn euros	in %
Light manufacturing property	542.9	58.1 %	298.6	55.0 %	119.4	40.0 %
Warehousing / logistics property	323.3	34.6 %	191.2	35.2 %	115.5	60.0 %
Transformation property	60.5	6.5 %	42.3	7.8 %	21.2	50.0 %
Business parks	7.8	0.8 %	10.5	1.9 %	9.5	90.0 %
All industrial real estate	934.5	100.0 %	542.6	100.0 %	265.6	49.0 %

At 35% in terms of both floor area and market value, warehousing and logistics property represents the second largest sub-group of industrial real estate. This excludes large-scale new schemes for contract logistics operators. This is because industrial real estate is generally understood to mean existing schemes with a maximum floor area of 10,000 sqm, and designed to meet mainly the needs of regional logistics operators or mid-market manufacturers and traders. Business parks and transformation property are structurally similar because they include diverse floor area types of various sizes within a given ensemble. Yet while business parks tend to take the form of more or less standardised building clusters in site resembling trading estates of uniform identity, transformation property have a decidedly one-off character because of their historic building fabric – in many cases supplemented by more recently built annexes. Business parks admittedly represent a niche category within industrial real estate with their share of just 0.8% of the lettable area and of just 2% of the market value. However, they show the highest investment grade among the sub-segments because they are developed almost exclusively for letting, and thus have a low share of owner-occupiers. Transformation property has a higher share at 6.5% of the floor area and 7.8% of the market value. But their investment-grade share is lower because their previous use and one-off character qualifies their options for redevelopment and continued use to some extent.

INDUSTRIAL REAL ESTATE SHOWS HIGHEST CAPITAL GROWTH

The performance of real estate investments may be measured on the basis of the total return of the German Property Index (GPI), which lists the commercial / industrial segment (GE/GI) along with office and retail. This segment largely reflects the performance of industrial real estate, too. The GPI measures the annual change in total returns on the basis of capital growth and rental yield. As a long-term performance ratio, the GPI is particularly meaningful for property asset holders, though it must not be confused with the initial yield rate.[3] Recently it has clearly shown a trend of real estate cycles to flatten and shorten.

Since total return growth will keep slowing, the differences between the various commercial real estate segments are likely to level out. In this context, the commercial / industrial segment (GE/GI) will outperform others because it is less susceptible to volatility while yielding higher average returns than office or retail properties. The key driver here is the rental yield, which has been stable on a high level year after year.

[3] For a definition both of the GPI and the initial yield rate (GIY = gross initial yield), please see the Glossary

Fig. 06: GPI total return by real estate segments in Germany (YoY) 1995-2018, in %

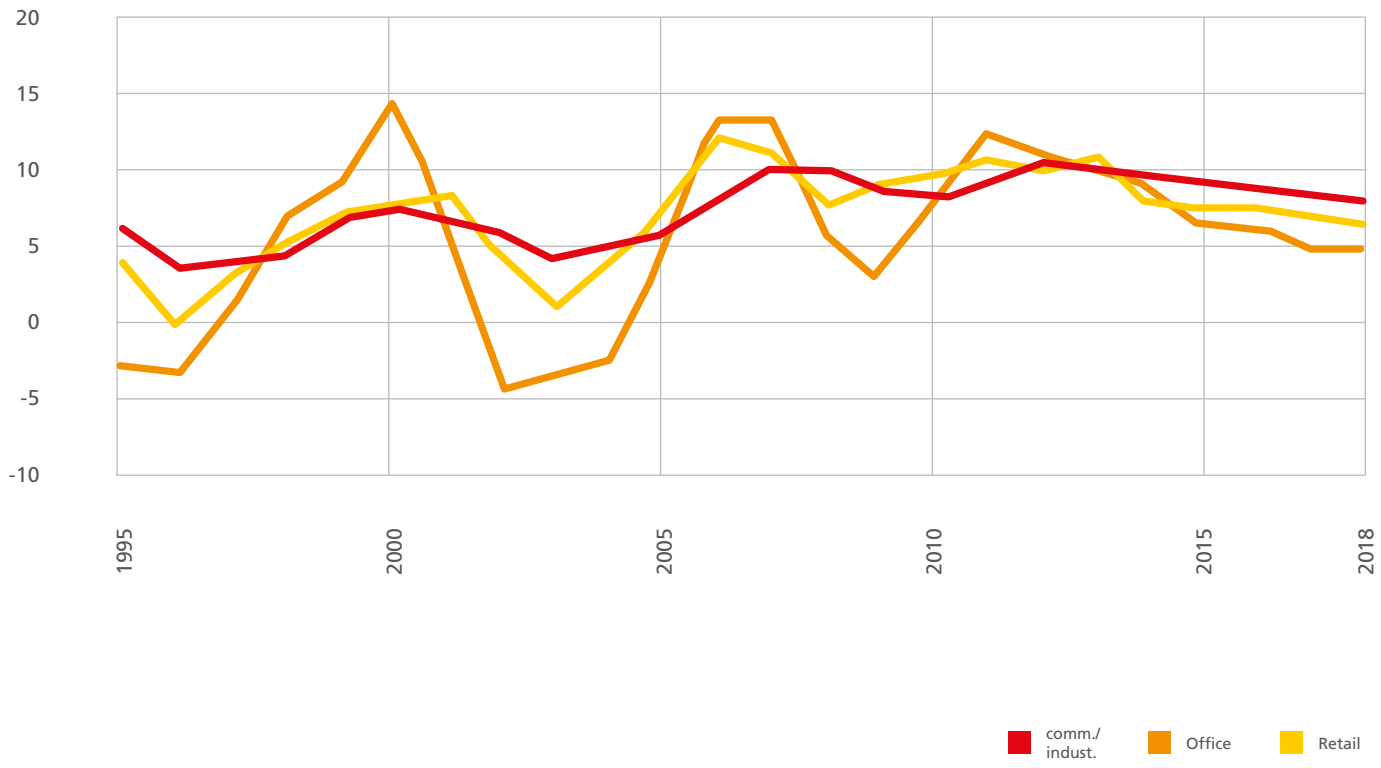
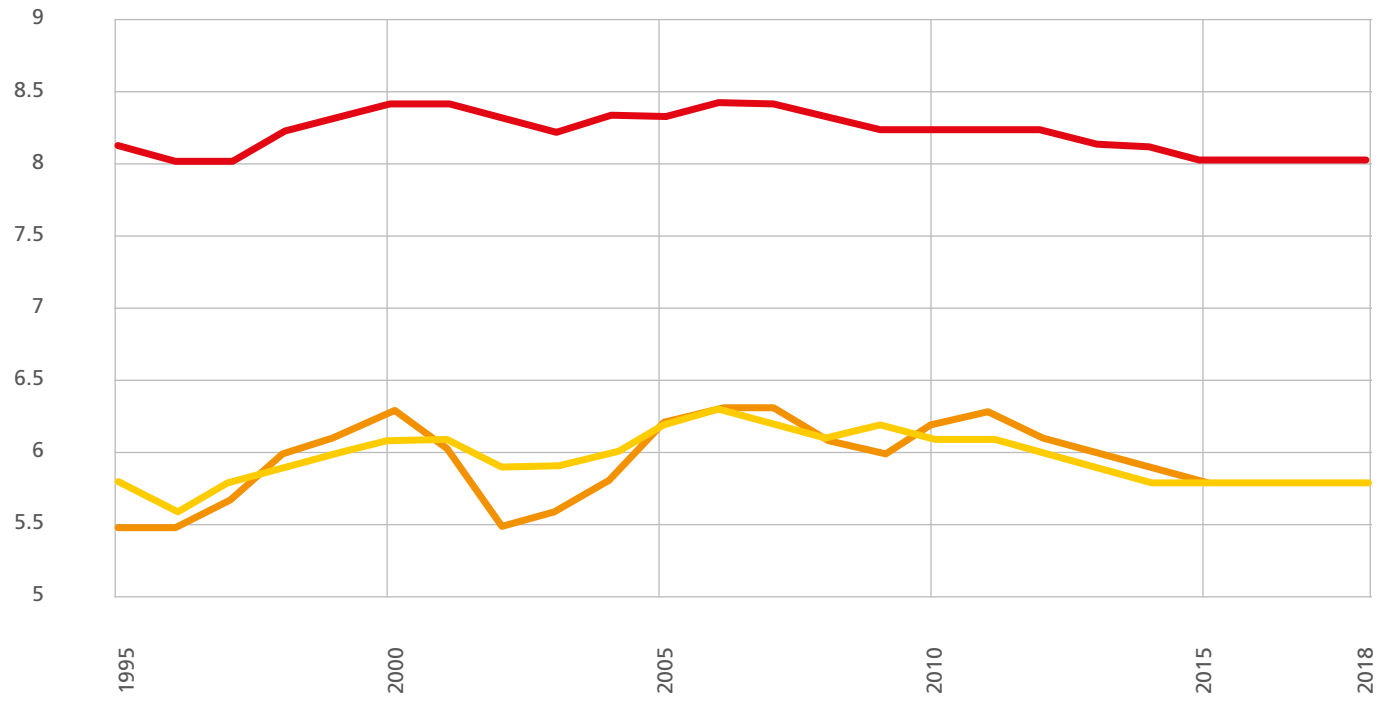


Fig. 07: GPI cash flow return by real estate segments in Germany (YoY) 1995-2018, in %



INVESTMENT MARKET FOR THE YEAR 2013 AND THE FIRST HALF-YEAR OF 2014

BUSINESS PARKS CURRENTLY THE MOST SOUGHT PROPERTY CATEGORY

Approximately 930 million euros were invested in industrial real estate across Germany in 2013. This equals around 3.5% of the entire commercial investment volume in a total amount of 26.7 billion euros (not including residential and hospitality). Investments were more or less evenly distributed among the two semesters (H1: 52.8%, H2: 47.2%). During the first semester of 2014, approximately 381 billion euros worth of industrial real estate changed hands. This compares to a commercial investment total of approximately 15.5 billion euros during the same period, which is one of the largest mid-year transaction volumes on record. Industrial real estate accounted for around 2.5% thereof.

The fastest-selling property category during the first half-year of 2014 were business parks with a transaction volume of approximately 174 million euros, the runner-up being light manufacturing property with a volume of approximately 96 million euros. Third on the turnover list were warehousing / logistics properties (not including big-ticket logistics), which attracted approximately 75 million euros in investments. Trading activities for transformation property were low-key, as the volume dropped to 36 million euros, and thereby declined by 83% year on year. However, the steep decline does not imply that investor interest in this property category has flagged. Rather, it highlights the limited supply in properties currently available and on the market. This results in greater fluctuations in transaction volume.

Fig. 08: Investment volume by category, in million euros

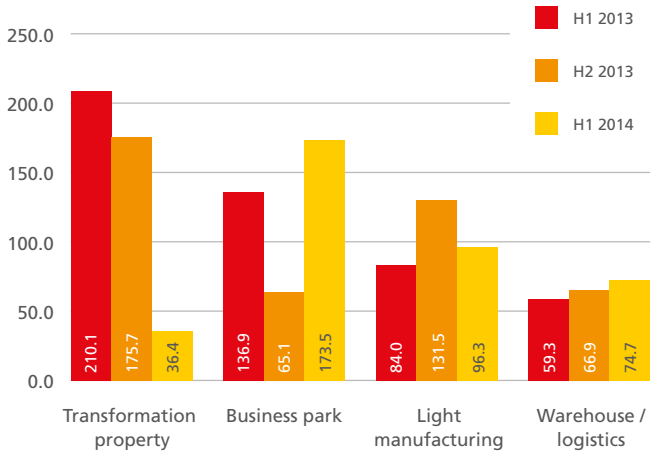
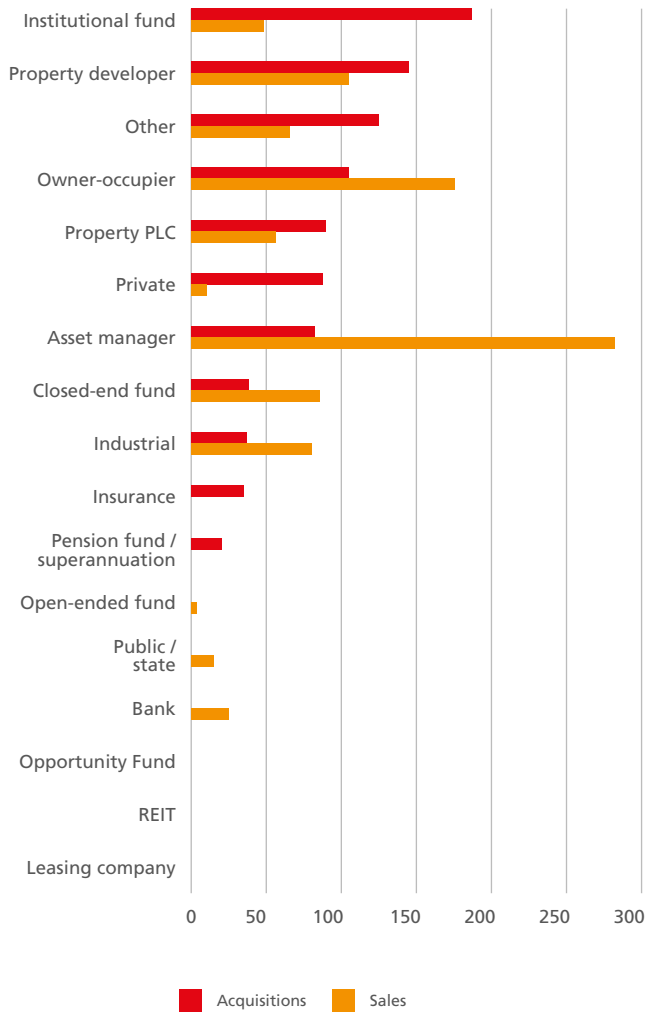


Fig. 09: Acquisitions / sales in 2013 by group of actors in million euros, broken down by largest buyer group

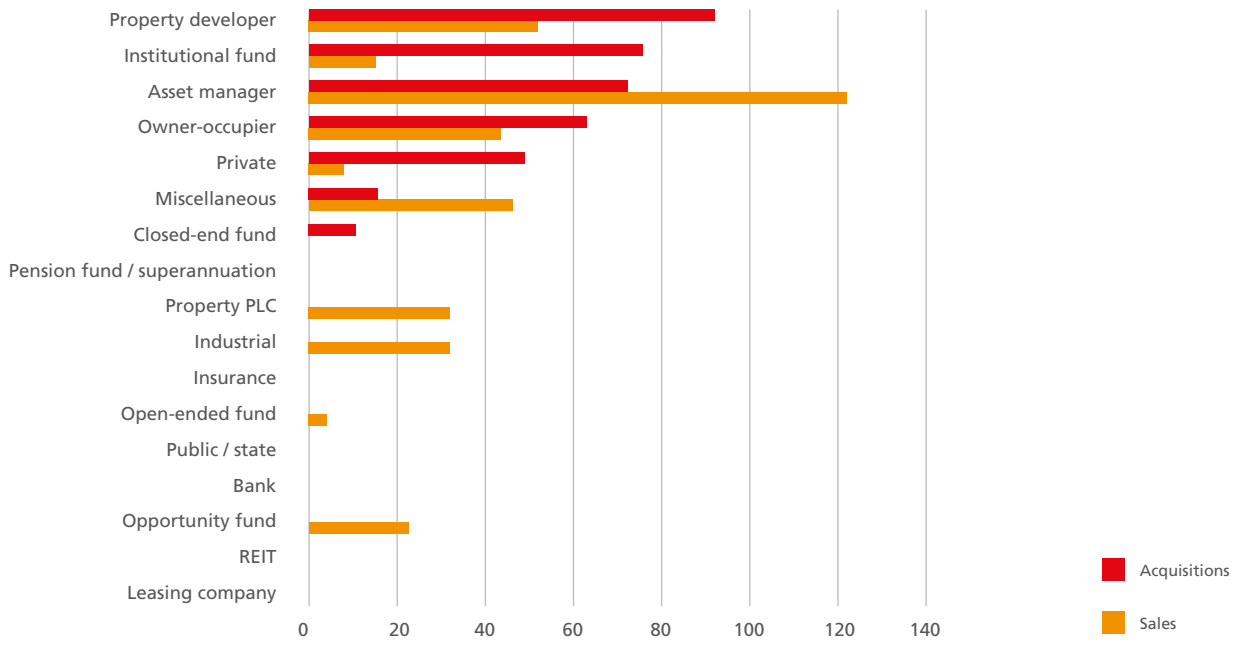


INSTITUTIONAL FUNDS AND PROPERTY DEVELOPERS EAGER TO INVEST

The largest buyer groups throughout 2013 were institutional funds along with property developers / building principals. They invested nearly 186 and 144 million euros, respectively, in industrial real estate in Germany. Another major buyer group were owner-occupiers, which is explained by their role as the largest group of owners in this market segment. For the same reason, they were also highly active on the seller side, disposing of properties worth approximately 174 million euros. Remarkably about this is the fact that companies sold more than they bought. This could indicate a tendency that companies are cutting their ownership rate. The strongest group on the seller side by far were the asset managers. They sold industrial real estate worth approximately 280 million euros, mainly on behalf of international owners.

The situation in H1 2014 was virtually unchanged year on year. Here, too, the largest groups of buyers and sellers were property developers and institutional funds. Asset managers showed the widest gap, as they were once again the largest seller group with approximately 121 million euros in sales but also the third-largest buyer group with well over 72 million euros spent. On the buyer side, owner-occupiers are as active as ever, while the number of private investors is growing steadily.

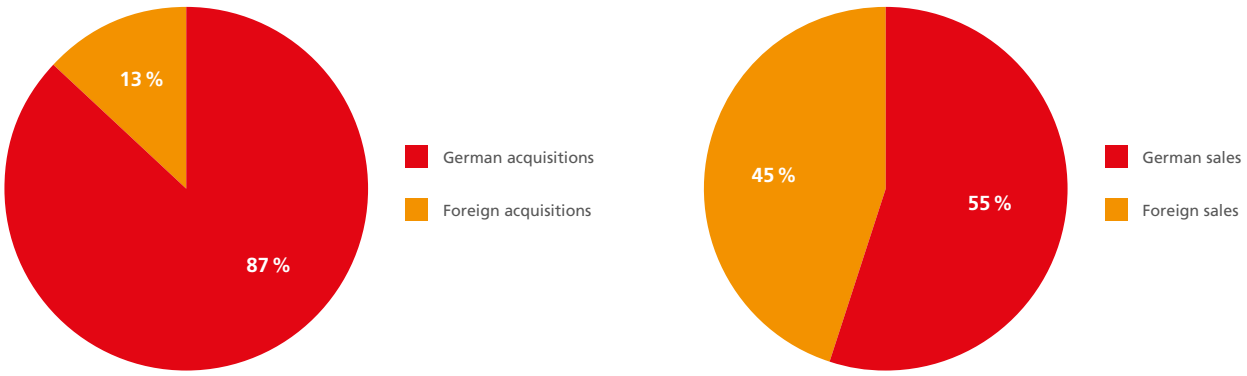
Fig. 10: Acquisitions / sales in H1 2014 by group of actors in million euros, broken down by largest buyer group



FOREIGN INVESTORS ARE BECOMING INCREASINGLY ACTIVE

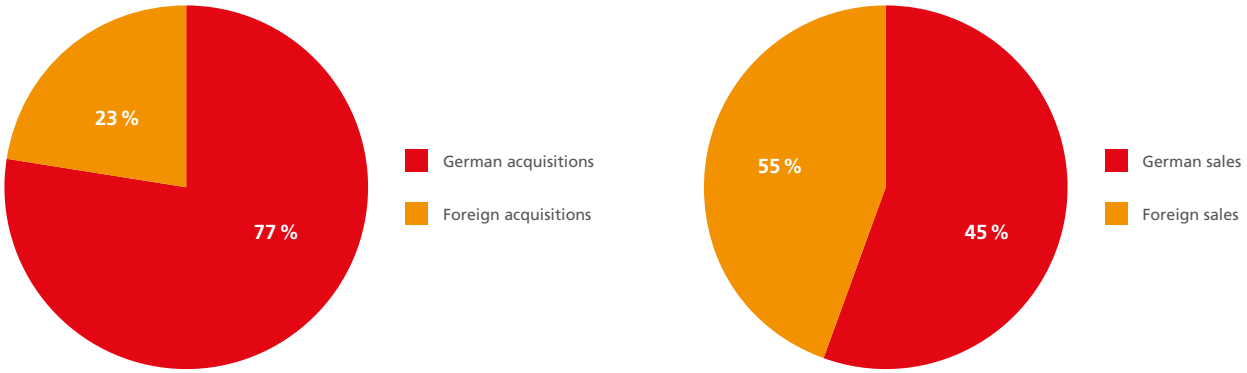
The origin of the market players manifests an unambiguous pattern across the entire reporting period. Most active on the buyer side are German investors, whereas the ratio of German to foreign actors is more or less balanced on the seller side.

Fig. 11/12: Acquisitions and sales in 2013, by origin of actors, in %



What defined the first six months of 2014 more than anything else is that the share of foreign buyers rose from barely 16% during H1 2013 to nearly 23% during H1 2014. The development comes in the wake of a trend that is already well under way on the logistics real estate market. Here, foreign players are setting the pace for the market action. This is explained by the continued increase on market transparency and the growing acceptance of the asset class, among other reasons.

Fig. 13/14: Acquisitions and sales in H1 2014, by origin of actors, in %



LIVELY DEMAND IN WEST GERMANY AND BERLIN

The region with the single-largest transaction volume during the entire period under review was the Rhine-Ruhr conurbation with nearly 205 million euros. Trailing closely behind is the greater Berlin area with an investment volume of nearly 189 million euros. Another market of above-average liquidity is the region west of the Rhine-Ruhr conurbation. The economically strong metro areas of Hamburg and Munich, and the Rhine-Main-Neckar conurbation are following relatively closely behind. All of these registered a transaction volume in excess of 120 million euros over the past year and a half.

The situation shifted during the first half-year of 2014 though. At well over 78 million euros, the region of greater Stuttgart, which had barely figured on the transaction market in 2013, suddenly took the lead. Lagging noticeably behind were the southern and eastern regions and once again Berlin.

Fig. 15: Breakdown of transaction volumes by time period and region, in million euros, descending by transaction volume, in H1 2014

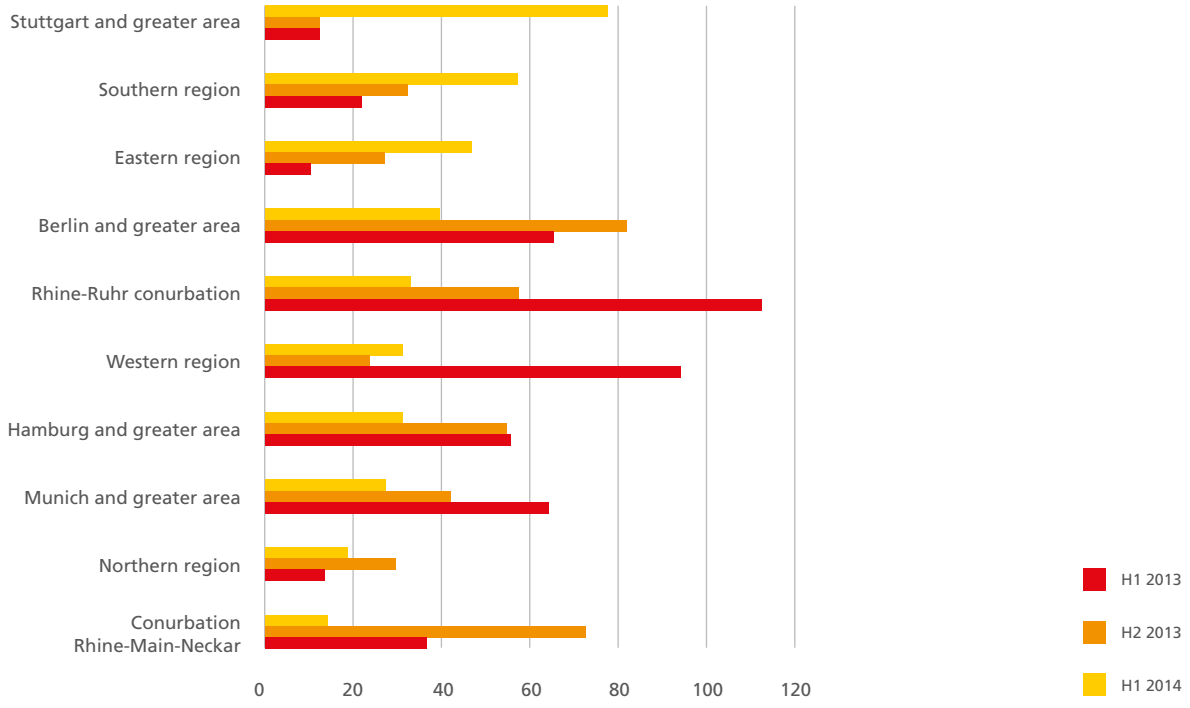
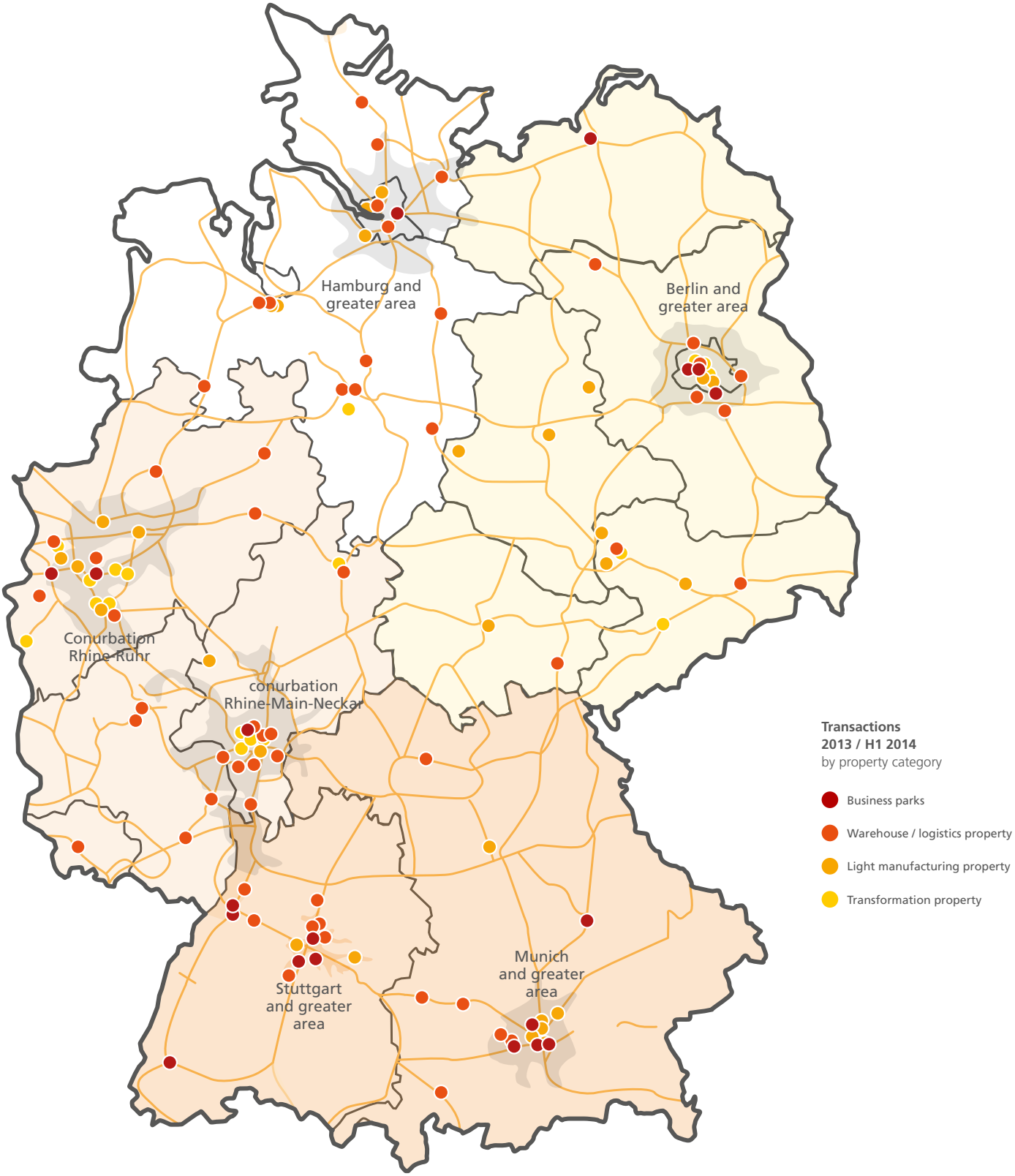


Fig. 16: Geographic spread of investments in Germany during the reporting period 2013 through H1 2014, by property category



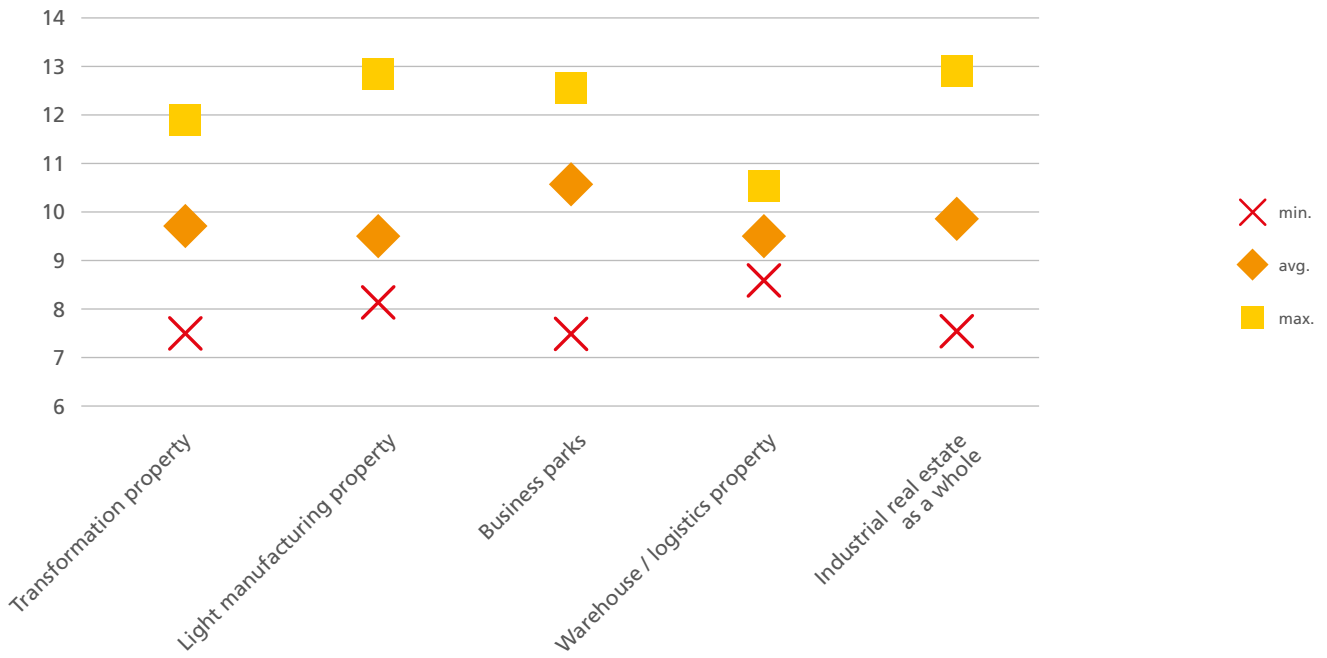
HIGH YIELD LEVELS COMBINED WITH MANAGEABLE THREATS

The achievable yield spread is quoted in terms of gross initial yield (GIY). The GIY represents the ratio of net rental income to net purchase price at the time of the transaction. Accordingly, it simultaneously reflects the profitability and the value of a given property. This sets the ratio apart from a long-term performance ratio like the GPI.[4] The GIY for the period under review suggests that the various property categories of industrial real estate are rather close together, and that they generate an average GIY of 9.8% across categories. The mean rates straddle a bandwidth of 9.5% to 10.7%, with the higher GIY rates being realised by business parks, which exceed the lowest rate of 9.5% (for light manufacturing property) by 120 basis points.

The gap between the minimum average and the maximum average GIY for each property category differs, except for warehousing / logistics properties, which have a narrow spread of 100 to 180 basis points. The deviation to higher GIY (the difference between average and maximum) tends to be more pronounced, and ranges from 4.4 to just over 5 percentage points. The spread at the lower end of the spectrum is much narrower, ranging from 1.4 to barely 2.2 percentage points.

The GIY across all separate categories ranges from 7.5% to 12.8%. The differences from one region or conurbation to the next can be as high as one percentage point.

Fig. 17: Gross initial yield during the period 2013 through H1 2014, by property category, in %



Industrial real estate delivers a comparatively high rate of return. The elevated risk that you would conversely associate with the fact is tempered for industrial real estate by the peculiarities of the asset class, especially by the stable rental yield and the low-level dependence on the capital market. Unlike other asset classes, industrial real estate takes the specific requirements of potential occupiers into account, which noticeably minimises the risk of vacancy, as does the customisable and reversible character of the floor space supply. Very high yield rates are typically achieved with legacy buildings and properties earmarked for redevelopment and in need of revitalisation.

[4] For a definition gross initial yield and the GPI rate, please see the Glossary.

LETTING MARKET FOR THE YEAR 2013 AND THE FIRST HALF-YEAR OF 2014

STABILISING ON HIGH LEVEL

The market for industrial real estate is characterised by lively letting activity. During the three semesters under review, the participants of the INITIATIVE UNTERNEHMENSIMMOBILIEN alone achieved a take-up of around 1.5 million sqm. The second semester of 2013 was particularly robust. Across Germany, around 580,000 sqm were marketed during the same time period. The first six months of 2014 accounted for a take-up of 440,000 sqm, more or less matching the level of the prior-year period.

Fig. 18: Take-up in the regions, in sqm and %, listed by total take-up in descending order

Region	H1 2013	H2 2013	2013	Share	H1 2014	Share	Total	Share of total
Other regions in southern Germany	121,000	176,000	297,000	28.0%	46,000	10.3%	342,000	22.8%
Berlin and greater area	89,000	128,000	217,000	20.5%	72,000	16.3%	289,000	19.2%
Other regions in northern Germany	57,000	77,000	134,000	12.6%	47,000	10.6%	180,000	12.0%
Rhine-Main-Neckar	107,000	37,000	144,000	13.5%	34,000	7.6%	177,000	11.8%
Rhine-Ruhr metro region	51,000	38,000	88,000	8.3%	61,000	13.9%	149,000	9.9%
Stuttgart and greater area	4,000	17,000	21,000	1.9%	121,000	27.5%	142,000	9.4%
Munich and greater area	14,000	66,000	80,000	7.5%	23,000	5.1%	103,000	6.8%
Other regions in western Germany	16,000	30,000	46,000	4.3%	17,000	3.8%	63,000	4.2%
Hamburg and greater area	17,000	11,000	27,000	2.5%	11,000	2.5%	38,000	2.5%
Other regions in eastern Germany	5,000	4,000	9,000	0.8%	11,000	2.5%	20,000	1.3%
Total	479,000	582,000	1,061,000	100.0%	440,000	100.0%	1,501,000	100.0%

STRONGEST MOMENTUM IN THE SOUTH

Industrial real estate lettings are particularly pronounced in Germany's economically strong southern part. Here, a total take-up of 342,000 sqm was reported for the entire period under review. This means, that the region accounts for nearly a quarter of all lettings. When including the two metro areas of Munich and Stuttgart, the region becomes even more dominant. Next in line is Berlin, where not just demand for office floor plate but also the demand for industrial real estate has positively surged. The low level in the greater Hamburg area is striking insofar as it contrasts sharply with the northern German region that surrounds it. It could be attributable to the fact that Hamburg's market is dominated by big-ticket logistics.

Fig. 19: Take-up during the reporting period of 2013 through H1 2014 by region and semester, in sqm, listed by total take-up in descending order

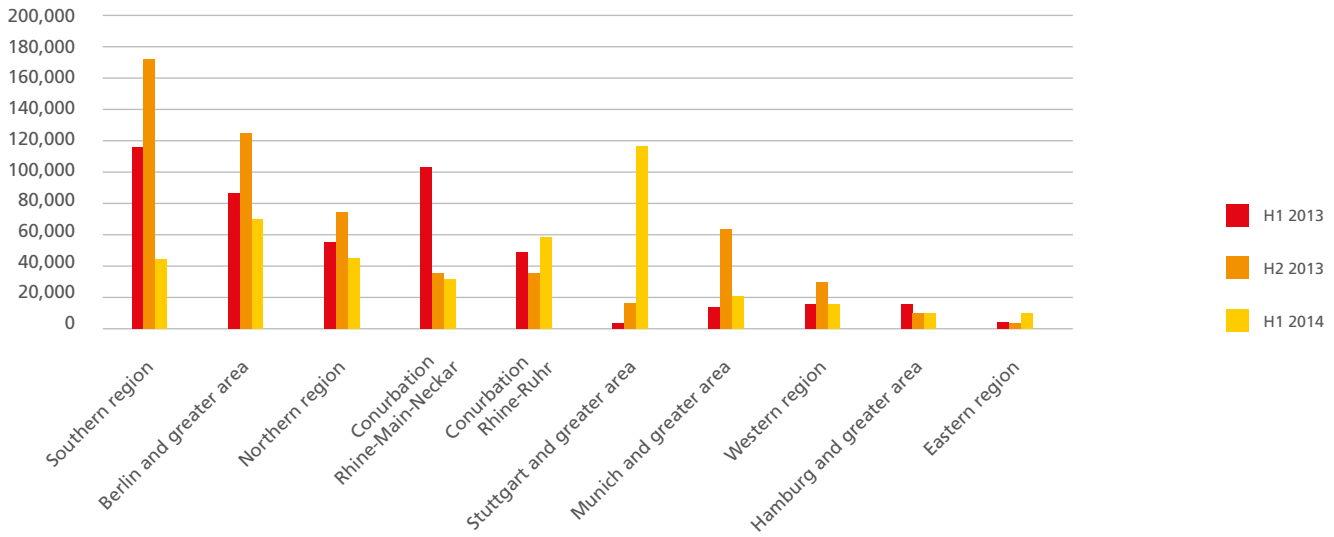
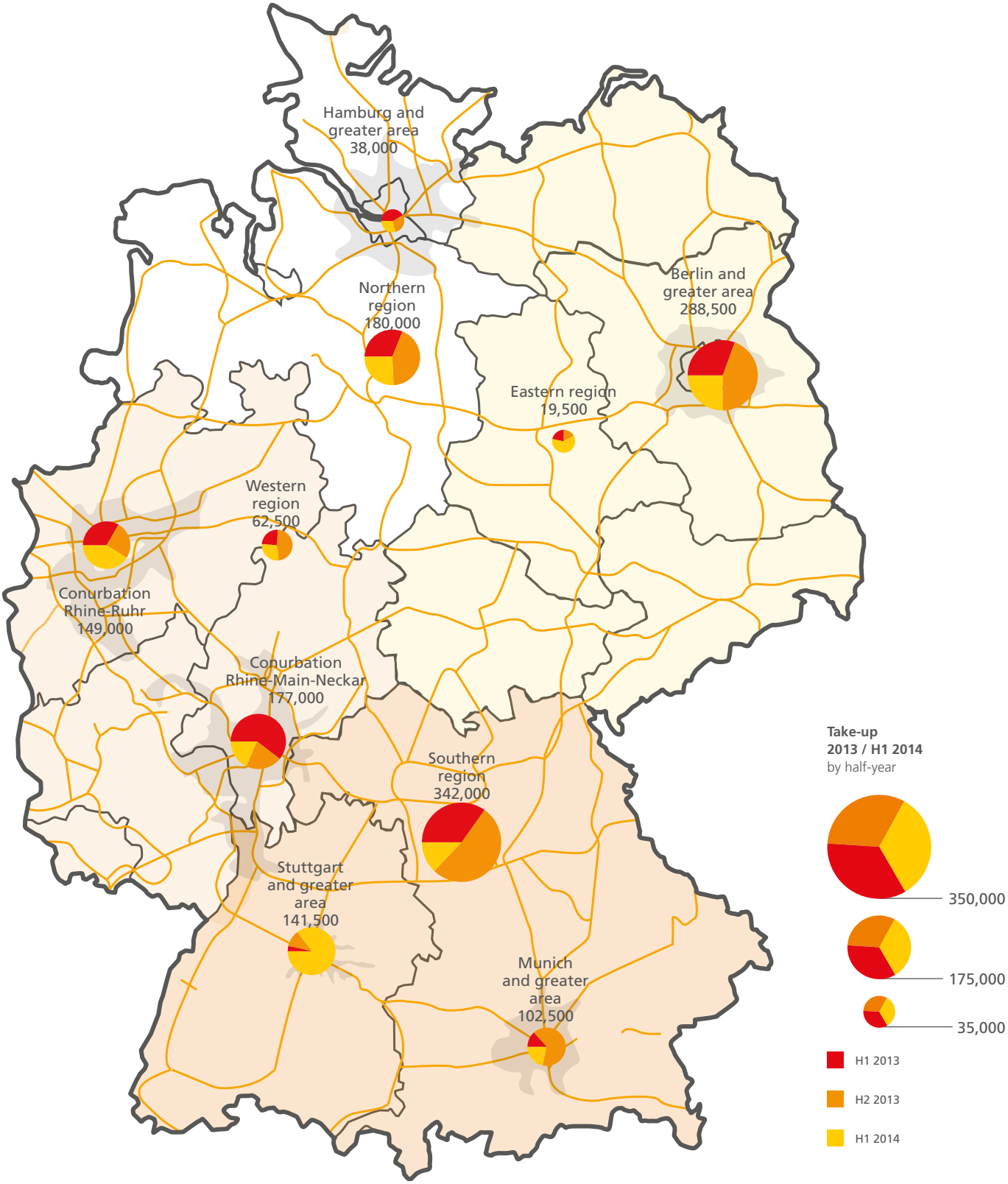


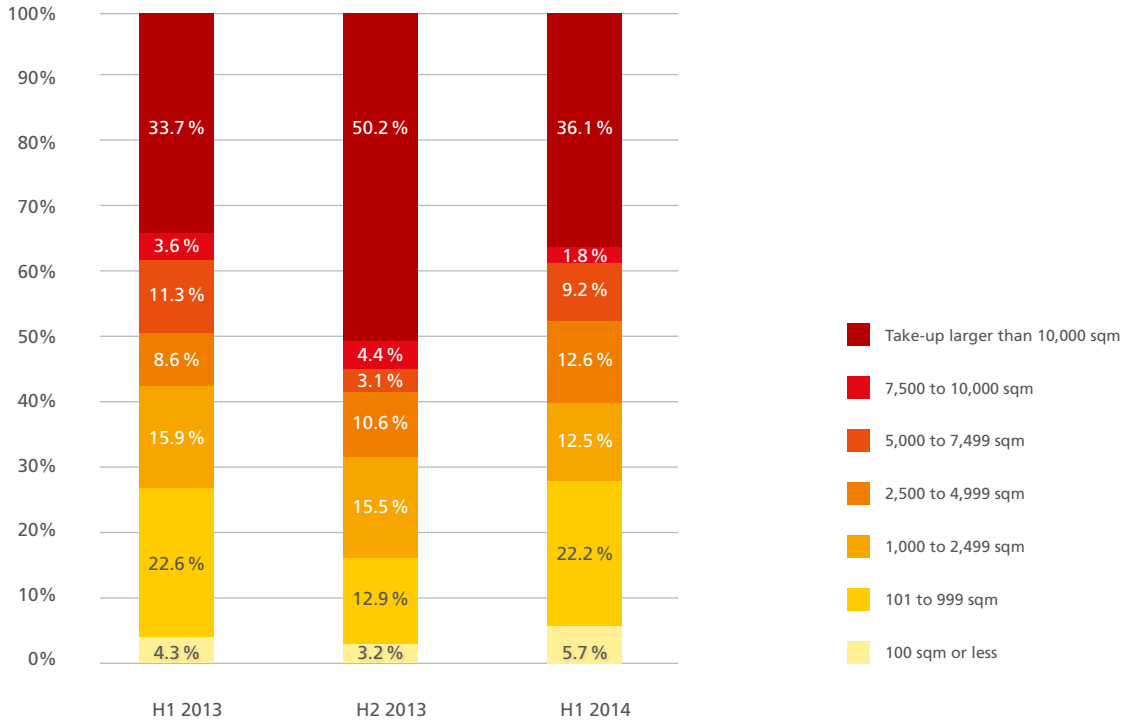
Fig. 20: Absolute take-up during the reporting period of 2013 through H1 2014 by region and half-year



INDUSTRIAL REAL ESTATE IS DEFINED BY A HETEROGENEOUS DEMAND STRUCTURE

The quality that mid-market to large companies appreciate most about industrial real estate is the flexibility of its floor space supply. Corporate demand for this type of accommodation is therefore defined by a very wide size spectrum. The size average in floorplate demand ranges from 400 to 600 sqm across all periods. This highlights the high asset management effort that is required for successful industrial real estate lettings. Then again, the heterogeneous and flexible floor space supply permits an adaptive response to occupier demand depending on the market cycle. No matter whether very small or large units are at issue – industrial real estate lets companies control demand because it represents a modular floor space supply.

Fig. 21: Take-up by area size categories during the periods under review



STABLE LONG-TERM CASHFLOW PAIRED WITH DYNAMIC CAPACITY UTILISATION

Another distinguishing feature of industrial real estate, in addition to its flexible floor space supply, is its stable cash flow. Many tenants are long-term occupiers, and have been in place for years. These faithful incumbents ensure permanently stable rental income, on the one hand. On the other hand, industrial real state is characterised by sufficient supply and reserves to meet peak demand on short notice, too. This explains the comparatively high average capacity utilisation of such properties despite their relatively short lease terms. Short lease terms, which are quickly becoming the standard model in other asset classes as well, meet the companies' need for flexibility half way. This must not be confused with mobility, because companies with a mixed types of use would have very high mobility costs if they decided to relocate.

The desire for flexibility is also expressed in the fact that a comparatively high number of new leases signed during the period under review included no fixed lease term. They are therefore subject to the statutory notice period of just three months. The maximum lease term is 10 years, in some cases even 20 years.

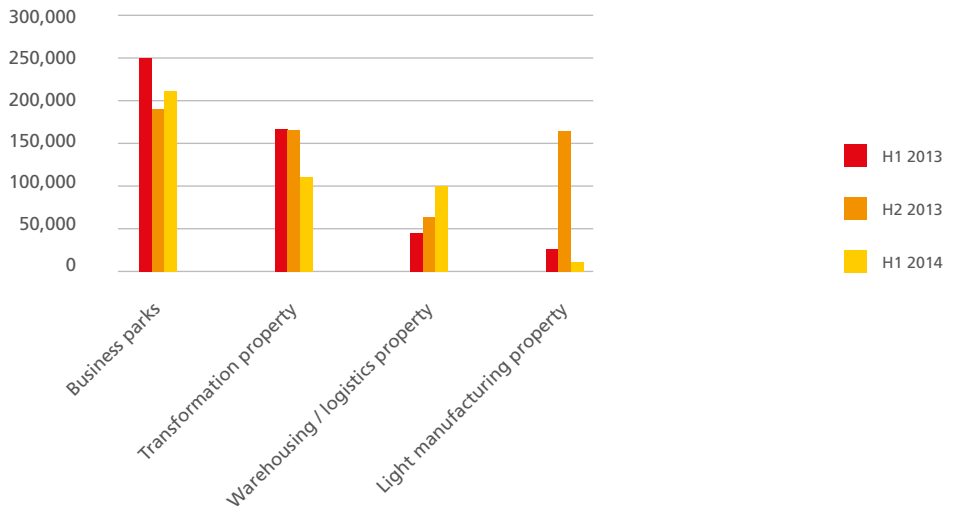
Fig. 22: Average lease term of new rentals during the periods under review

Average lease term for new rentals, 2013 through H1 2014, in years	H1 2013	H2 2013	H1 2014
Avg. lease term	2.5	1.5	1.5
Max. lease term	20.0	10.2	20.0

DEMAND HIGHEST FOR MULTI-TENANT PROPERTIES

As far as new rentals go, units in multi-tenant properties experienced the highest occupier demand. Business parks attracted the strongest demand across all three of the semesters under review, achieving a total take-up of nearly 650,000 sqm. Around 446,000 sqm were let in transformation property during the same period, and nearly 210,000 sqm in warehousing / logistics properties. Several large-scale signings with manufacturing industry tenants were reported in the light manufacturing segment during the second half of 2013, raising the total take-up to around 160,000 sqm. Other than that, light manufacturing property plays a comparatively subordinate role in the industrial real estate lettings because its long-term character and degree of specialisation discourages any shift in demand.

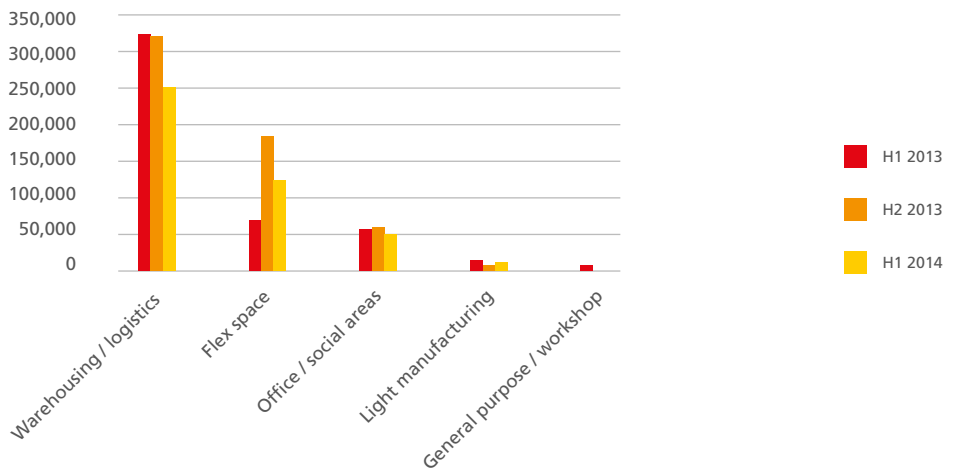
Fig. 23: Take-up by property category and period, in sqm, total take-up in descending order



WAREHOUSES THE FLOOR AREA TYPE MOST IN DEMAND

The type of industrial real estate most in demand during the reporting period was warehousing property. Lagging slightly behind was flex space[5], meaning dynamic floor area types of reversible usage, and office accommodation. While demand for warehousing is often aimed at large rental units, office demand is dominated by a call for small or indeed very small floor plates. Property consisting purely of production area are rarely rented. The top spot of light manufacturing among the property categories is explained by the fact these are flex space units rather than pure production areas. In an economic environment of accelerating cycles, companies feel that properties structured for a single purpose are putting increasing constraints on their activities. The same is true for service and workshop areas, which may also be structured as flex space, principally speaking.

Fig. 24: Take-up across categories in sqm, pro rata by floor area type and semester, total take-up in descending order



[5] For a definition of flex space, please see the Glossary.

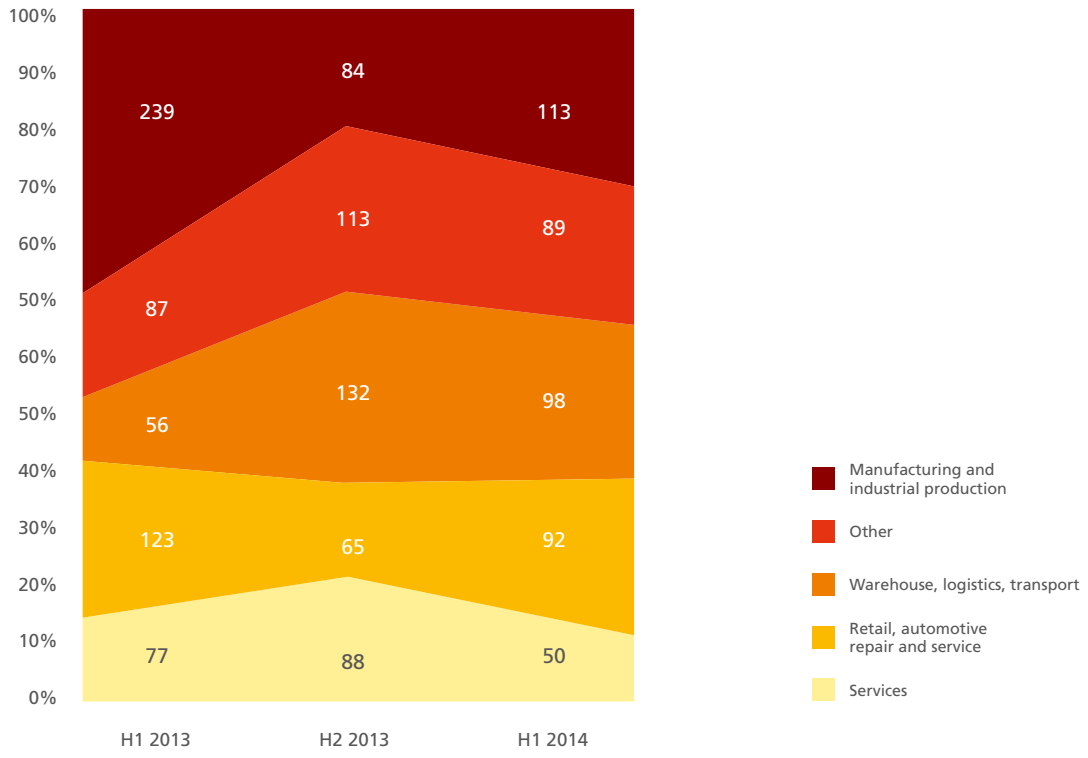
BULK OF THE DEMAND FOR SPACE GENERATED BY THE MANUFACTURING INDUSTRY

The demand for industrial real estate is rather heterogeneously structured in regard to the various groups of occupiers.

The largest demand group for the entire reporting period is the manufacturing and industrial production, with a total take-up of well over 435,000 sqm. The second largest sector with a take-up of around 285,000 sqm is the warehousing, logistics and transportation industry, which accounts for nearly 20% of the floor area demand involving industrial real estate. However, this share is subject to considerable fluctuation, ranging from less than 10% (H1 2013) to nearly 30% (H2 2013). The retail sector, which also includes automotive repairs and services, presents a similar picture. The service sector claims a noticeably smaller share, accounting for an average of around 15% of the floor space rentals.

All things considered, the demand structure is rather broad-based. Inversely, as industrial real estate serves a richly diversified array of target groups, it lends itself to the diversification of economic risks.

Fig. 25: Take-up per semester, by aggregated industry, in 000 sqm, total take-up in descending order



DESPITE THE DIVERSIFIED FLOOR SPACE SUPPLY NO OUTLIERS IN TERMS OF PRIME RENT

The prime rent for industrial real estate approximated 9.70 euros / sqm across floor area types during the first half-year of 2014, down from 10.00 euros / sqm during the prior-year period. The spread extended from 5.50 euros / sqm for pure production areas to 12.30 euros / sqm for office space. Most recently, the average rent across all types of floor plate was approximately 5.40 euros / sqm. The spread extended from 4.50 euros / sqm for pure warehousing space to 6.60 euros / sqm for office space. This implies narrower gaps than is commonly assumed for this asset class because of the sheer variety of its floor space supply with vast differences in dimensions and quality standards.

A floor area-weighted evaluation shows the highest rents for office units, generally speaking, even though these came under pressure during the period under review, dropping successively from 14.00 euros / sqm to 12.30 euros / sqm. This reflects the regressive demand in the office sector.

An often underestimated aspect of industrial real estate is the market rent for warehouse and small-scale logistics space, especially those offered in business parks or transformation properties. Throughout the periods under review and beyond, these rented out for up to 11.00 euros / sqm or indeed more than that. In pure warehousing properties, by contrast, these units tend to be cheaper. Flex space has experienced a much increased demand – with predictable consequences for rent levels. The brisk rental growth therefore pushed rents up from less than 2.00 euros / sqm to around 10.50 euros / sqm during the reporting period alone.

Fig. 26: Performance of prime rents for industrial real estate by floor area type and semester, in euros / sqm / month

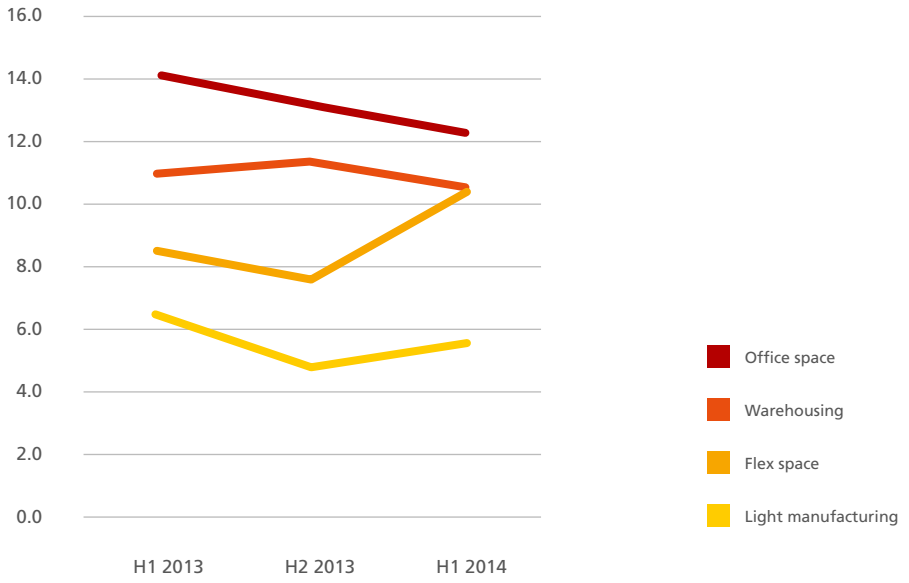
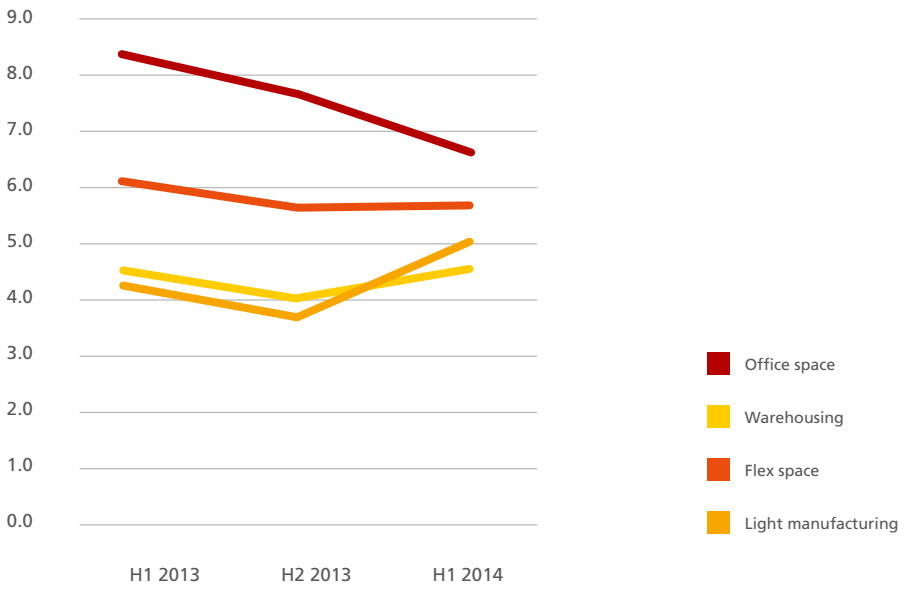


Fig. 27: Performance of average rents for industrial real estate by floor area type and semester, in euros / sqm / month



NOTES ON THE ANALYSIS

A total of 3,121 lease agreements were collected and analysed for the year 2013 and the first six months of 2014. The analysis of the occupier market drew exclusively on primary data sourced from the actual building owners. The evaluation was limited to genuine letting activities to the exclusion of owner-occupier transactions. It also ignored subletting activities undertaken by players other than real estate professionals. Moreover, the analyses failed to differentiate between subsequent rentals and new rentals. We believe that this Market Report covers an estimated third of all lettings transacted in the market. Accordingly, the quoted figures should be read not as a global trend statement but as a random sample. In addition to the data provided by the participants, the investment market analysis took transaction data from the RIWIS database of bulwiengesa into account.

Carlswerk in Cologne

Sirius Park building in Berlin-Tempelhof

Warehouse space in a former production plant

Office space in a former production plant

GLOSSARY

GROSS INITIAL YIELD (GIY):

As a transaction-based ratio, the gross initial yield reflects the actually realised return on a property transaction. The gross initial yield is determined as the reciprocal value of the gross income multiplier, meaning the ratio of net rental income to net purchase price. Compared to the net initial yield, the GIY still includes the non-recoverable service charges in the rental income, as well as the incidental acquisition costs currently accepted as market standard. The GIY ratio is used whenever these variables are unknown in order to make it easier to compare transaction data.

FLEX SPACE:

The floor area type called flex space in the context of industrial real estate combines several types of use (office, warehousing, light manufacturing, among others), and meets a variety of usage requirements. Premises of this type are adapted to an occupier's requirements by the landlord before being handed over or else are converted by the tenant. For instance, a tenant with an unexpired lease for flex space may wish to convert office space into light manufacturing space, or vice versa, without any change to the lease agreement or to the rent level.

GERMAN PROPERTY INDEX (GPI):

The German Property Index (GPI) is a real estate performance index calculated on the basis of available market data. It is compiled for the segments of office, retail, and commercial / logistics. The calculation takes diverse real estate industry market and planning data into account, depending on availability. It also factors in additional assumptions concerning management, maintenance and other non-recoverable operating costs for each market segment that are made on the basis of long-term market know-how.

The national GPI (= total return) of each real estate market sector is derived from the weighted sum of the current (stable) rental income (cash flow return) and the weighted sum of the projected increased in fair market value (capital growth return) of the 127 cities covered by the RIWIS market database. The weightings are differentiated by sector, and are not constant over time. The index and its components are defined as follows in this context:

Total return:
The total return is derived from the weighted sum of the capital growth returns (CG) and the weighted sum of the cash flow returns (CF) of the 127 cities. It represents the total return on the capital employed over a certain period of time, i.e. the year-on-year change, quoted in percent.

Cash flow return:
This term represents the return generated from the current operative use of a property, set in relation to the cash trapped. The cash flow equals the surplus of the periodic rental income after the current operating expenses.

Capital growth return:
This term refers to the capital growth of a real property asset's fair market value over a period of time, set in relation to the capital growth at the end of the prior period. It takes factors influencing the value of a property (modernisations, lettings of vacant premises or renewals of unexpired leases) as well as general changes in property market values into account.

As a benchmark indicator, the GPI is most helpful to long-term property asset holders when gauging the performance of their portfolio. Accordingly, it contrasts with the gross initial yield, which refers solely to the time of a property's acquisition.

LIST OF FIGURES

DISCLAIMER

The findings and calculations presented in this Market Report, as well as the underlying research, are based on evaluations of participant portfolios or letting and selling transactions executed by members of the INITIATIVE UNTERNEHMENSIMMOBILIEN. They are supplemented by other sources either available or accessible during the processing time, and analysed to the best of our knowledge and using due diligence. No warranty is offered regarding the accuracy of the information and data, except for those researched and compiled by ourselves, this guarantee being limited to the standard duty of care. No warranty whatsoever is assumed for the technical accuracy of data or facts and circumstances adopted from third parties.

The findings were interpreted and evaluated against the background of the experience bulwiengesa has gathered through its research and advisory activities in Germany and elsewhere in Europe.

YOUR CONTACT

PUBLISHED BY:
INITIATIVE UNTERNEHMENSIMMOBILIEN

INITIATIVE SPOKESPERSON:
Steffen Uttich
Beos AG
Kurfürstendamm 188
10707 Berlin, Germany
Telephone: +49 30 280099-18
Facsimile: +49 30 280099-66
steffen.uttich@beos.net

SCIENTIFIC PROCESSING, DATA HANDLING, AND EDITING:
bulwiengesa AG
Wallstrasse 61
10179 Berlin, Germany
Telephone: +49 30 278768-0
Facsimile: +49 30 278768-68

PROJECT MANAGER:
Tobias Kassner
+49 30 278768-23
kassner@bulwiengesa.de

PROJECT ASSISTANT
Hauke Prätzel
+49 30 278768-26
praetzel@bulwiengesa.de

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