



INSIGHT

#2

June 2018

INITIATIVE  
UNTERNEHMENS  
IMMOBILIEN



# GERMANY IN THE FOCUS OF FOREIGN INVESTORS

Unternehmensimmobilien  
Assets Increasingly Popular  
as Investment Objectives  
for International Capital

# „We accept that yields go up and down“

Why is Germany such an interesting light industrial investment market for international market players? What is their opinion of the German market and its participants?

Alistair Marks, Chief Financial Officer of Sirius, speaks about the potential of the asset class Unternehmensimmobilien for local and foreign investors.



**A**t Sirius, we have always been strong believers in the Unternehmensimmobilien sector for many reasons and it has been pleasing for us to see over the last five years that many other local and foreign investors are also recognising the major benefits of investing into this high yielding asset class.

We believe that the fundamentals remain strong for investing into the Unternehmensimmobilien asset class in Germany and that the demand will remain strong for the foreseeable future. The key reason behind this is the high cash flow that can be generated from these assets, especially if you have an effective asset management

platform in place to deal with the key aspects of Unternehmensimmobilien that can be enhanced from intensive management, namely:

- lettings and renewals,
- service charge recovery,
- further capital investment into development and refurbishment.



Sirius Business Park Mannheim  
(Photo: Sirius Real Estate)



We are convinced that the returns of this asset class in German yields are overall higher and more sustainable than abroad - that's why we are comfortable with them, even if they fluctuate slightly. The reasons for the positive situation in Germany lie in the following reasons:

- the vast amount of large industrial assets that exist in Germany,
- the fact that assets can be purchased at such significant discounts to replacement costs,
- the strong occupational demand from both large blue-chip organisations and the incredibly strong SME (small and medium-sized enterprises) sector in Germany,
- the higher yields in comparison to foreign markets or other asset classes like office or retail that Unternehmens-

immobilien, even in core locations, can be purchased for,

- the value-add opportunities available on these assets which can be realised through effective asset management and investment,
- the sustainability of the transactional and occupier demand in both good and bad times because of the size and strength of the German economy,
- the availability of financing at very attractive interest rates.

Sirius historically has invested into the larger, older, mixed-use industrial and commercial business parks and because of the above-mentioned reasons we have more recently been acquiring the more modern, post-unification warehouse, service and office parks. Additionally, we have been purchasing pure office buildings in

secondary locations around the big seven cities in Germany in order to increase the diversity of our portfolio. Our focus is to continue to invest in the secondary and tertiary locations around the „big 7“ major cities in Germany because the demand and pricing for our product offerings is much higher in these locations and we believe tertiary areas around A grade locations offer greater opportunity than secondary areas around B or C grade locations.

We seek to buy a combination of value-add properties along with a mix of core properties because over time we make the highest returns from the opportunistic value add assets and we need the stability of the core assets in order to secure the right banking facilities.

We think the points set out above are just some of the reasons why we are seeing so much competition when it comes to buying light industrial and logistics assets in Germany today and it is also why we believe large foreign investors including Blackstone, Cromwell, China Investment Corporation and Frasers Centrepoint have entered the market in a substantial way along with an increasing number of local players like Palmira and the newly formed Deutsche Industrie. This is undoubtedly leading to a much better understanding and acceptance of Unternehmensimmobilien as a traditional and institutional investment class with German real estate.



Mircopolis Dresden  
(Photo: Sirius Real Estate)

# Putting German Unternehmensimmobilien in Global Context

## High Level Acceptance of Industrial Real Estate in the United States and United Kingdom

Light industrial real estate—this is what commercial properties that combine warehouse/logistics, light manufacturing or research and development facilities with office-related types of use are called in Anglo-American and Anglo-Saxon countries. In Germany, by contrast, the term Unternehmensimmobilien has established itself. In addition, the asset class subsumes so-called converted properties that do not lend themselves to new commercial occupancy until comprehensively revitalised and structurally altered. They tend to come with a historic industrial charm. Quite characteristic for Unternehmensimmobilien is the “flex space” type of accommodation.

On the US and UK real estate markets, light industrial properties are nothing exotic but have been established for a long time and remain a popular investment objective then as now. As a result, selling prices in this real estate segment have historically been considerably higher than prices on the German market. A good way to put the German market for Unternehmensimmobilien into international context

is by looking at the average cap rate for industrial real estate (including large-scale logistics assets) because comparables for these are readily available.

As early as 2013, the UK market experienced a serious yield compression at a time when the average cap rates stood at around 8.2% and thus on more or less the same level as in Germany. In the wake of persistently keen demand, the average cap rate for light-industrial real estate on the British market dipped to 6.0% by year-end 2017. Meanwhile, yield rates on the industrial market in the US have steadily hardened since 2014, though not as quickly as they did in the UK and in Germany. This matches the trend of prior years, when the average cap rate on the US market had remained stable at 7.3% and shown no major spikes. In fact, the US market registered the highest comparative value at the end of the concluded year 2017 with an average cap rate of 6.5%.

The average cap rate in Germany’s industrial real estate segment was defined by volatility between 2012 and 2015 when compared to the US and UK markets. But in 2015, investment demand in Germany began to surge at such a brisk pace that the average cap rate took a more or less steady downward turn, dropping from

8.0% (2015) to 6.3% by the end of 2017, in some places actually undercutting comparables in the US and UK markets.

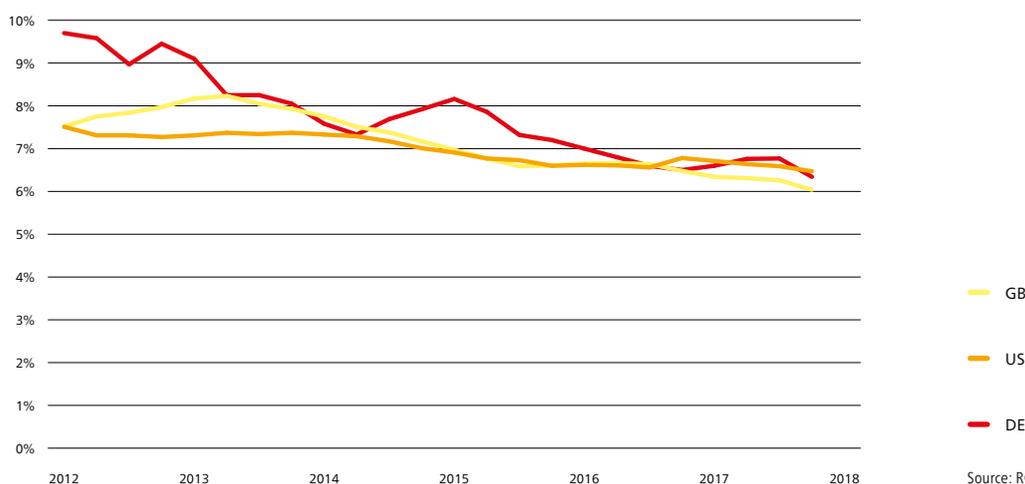
## Prospering German Market

A comparison of cap rates shows clearly that the German market has developed considerable momentum in recent years, despite its volatilities. Although its volume and share of the overall market remain low-level compared to the US and UK markets, it manifests substantial upside, given the total investment potential.

Of course, the sheer size of the commercial real estate market in the US makes its transaction volume in industrial real estate exceed the absolute sums invested in the United Kingdom and in Germany many times over. In the banner year of 2015, investments in the United States came to a total of nearly 56.5 billion euros. But a look at the percentages in the transaction volume of the past two years, 2016 and 2017, shows that percentage-wise the asset class of industrial property (including large-scale logistics) claimed its highest share of the total transaction volume in the United Kingdom. In 2017, it became the first of the three markets analysed to cross the mark of 20% during the period under review (2012 and thereafter).

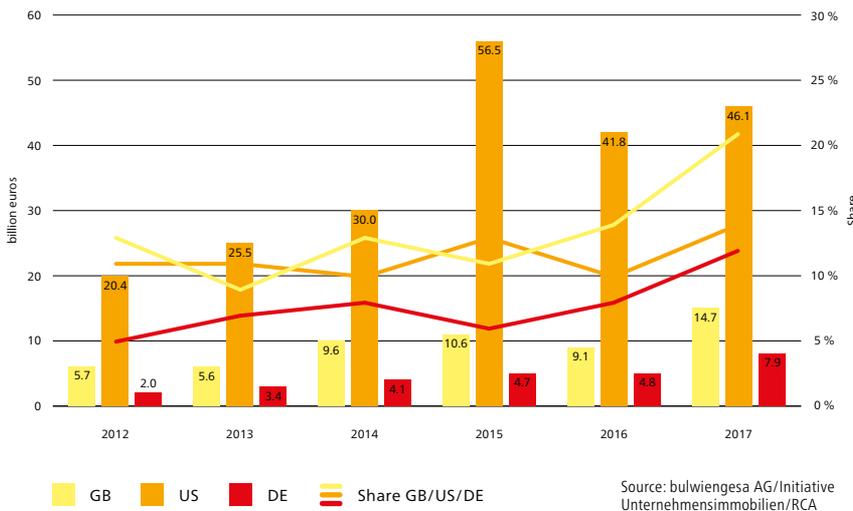
The share that industrial real estate claimed in the commercial transaction total in Germany in 2012 and subsequent years was much lower than on the reference markets. However, the asset class has noticeably gained in significance in Germany: Claiming 12% of the market, it crossed into the two-digit range in 2017 for the

Average cap rates of industrial real estate



Source: RCA, bulwiengesa AG

Market volume and share of industrial real estate in the overall commercial property market



first time, which is twice of what it was in 2015 and which is explained, in addition to investments in Unternehmensimmobilien, by the strong demand from large-scale logistics real estate.

Germany's Market Benefits from Permanently Attractive Parameters

The current interest environment remains as investor-friendly as it has been, and buyer are looking for investment objectives as eagerly as ever. Due to the size of its national economy and its economic structure, Germany is a particularly attrac-

tive investment destination, including for Unternehmensimmobilien investments. Occupiers of Unternehmensimmobilien typically belong in the vast group of small and medium-sized enterprises (SME), which are the driving force behind Germany's robust economic situation. At the same time, the country's polycentric structure has created multiple prospering economic areas. Demand for assets of this type among investors and occupiers is therefore not to be expected in the foreseeable future. Other factors that enhance the appeal of Unternehmensimmobilien include the still comparatively low prices and value-add potential.

International Investors Enter the Market via Portfolio Acquisitions

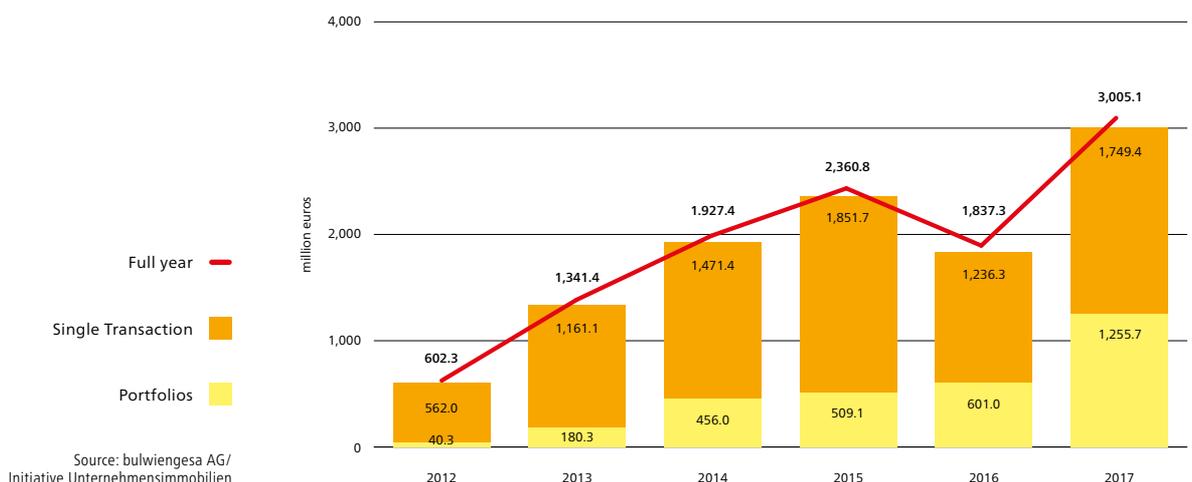
German Unternehmensimmobilien have increasingly whetted the appetite of international players. Market evidence reflecting the fact includes not least the trend in transaction volumes of portfolio acquisitions whose significance has increased steadily during the years since 2013, the year Initiative Unternehmensimmobilien started to monitor the market. Investments in larger portfolios or the acquisition of entire companies permit the instant placement of large sums of capital in a given market and to create a conspicuous footprint in that market at the same time.

During the banner year of 2017, both the transaction total and the roughly 42% market share of package sales climbed to a new high-water mark. Over 1.2 billion euros were invested in portfolio acquisitions, which is more than the year-end totals of 2015 and 2016 combined.

International investors accounted for the bulk of it. Their market entry has cause the sum total that is committed in Unternehmensimmobilien portfolios to multiply. Accordingly, the record-breaking transaction volumes recently seen in the asset class of Unternehmensimmobilien is closely linked to the intense market presence of international investors.



Unternehmensimmobilien investment volumes in Germany by type of transaction





The return potential raised through the active management of Unternehmensimmobilien assets as outlined in the comments made by Alistair Marks has obviously been a compelling reason to invest not just for Sirius. Asset managers and fund managers/private equity investors were by far the strongest buyer group in recent years.

Among the most spectacular deals lately was the one transacted by the US-based private equity partnership Blackstone in a joint venture with the UK property company M7 Real Estate in Q2 2017: The entire company Hansteen Holdings PLC and its real estate assets were taken over. The portfolio included primarily business parks and warehouse properties.

### North American Investors Particularly Eager to Enter the German Market

Historically, the German market for Unternehmensimmobilien used to be dominated by domestic investors. German buyers accounted for roughly 82% of the purchase volume in 2012, while 12% was bought by investors from other countries in Europe. At that time, overseas investors played barely a role on the German market for Unternehmensimmobilien. Things changed once the market became more transparent and the asset class met with growing acceptance. The balance between domestic and foreign buyers began to shift in 2014. The market share of German buyers dropped to 70% that year and has more or less maintained this level ever since.

Up to and including 2015, the first foreign investors claiming a higher share of the German market originated in neighbouring countries in Europe. It was not until 2016 that North American investors began to show more interest in the German market for Unternehmensimmobilien. That year, the contribution of North American buyers to the overall investment volumes more than tripled, rising from 6% to 19%. In 2017, the mentioned acquisition of the Hansteen portfolio caused the share of buyers from this region to jump up again, pushing it up to 27% by year-end. Year on year, the activity of North American investors diminished the significance of foreign buyers from European countries whose share in the transaction volume bottomed out at 3%.

### Unambiguous Preferences of International Investors

The buying pattern of international investors on the German market for Unternehmensimmobilien has so far been defined by two factors:

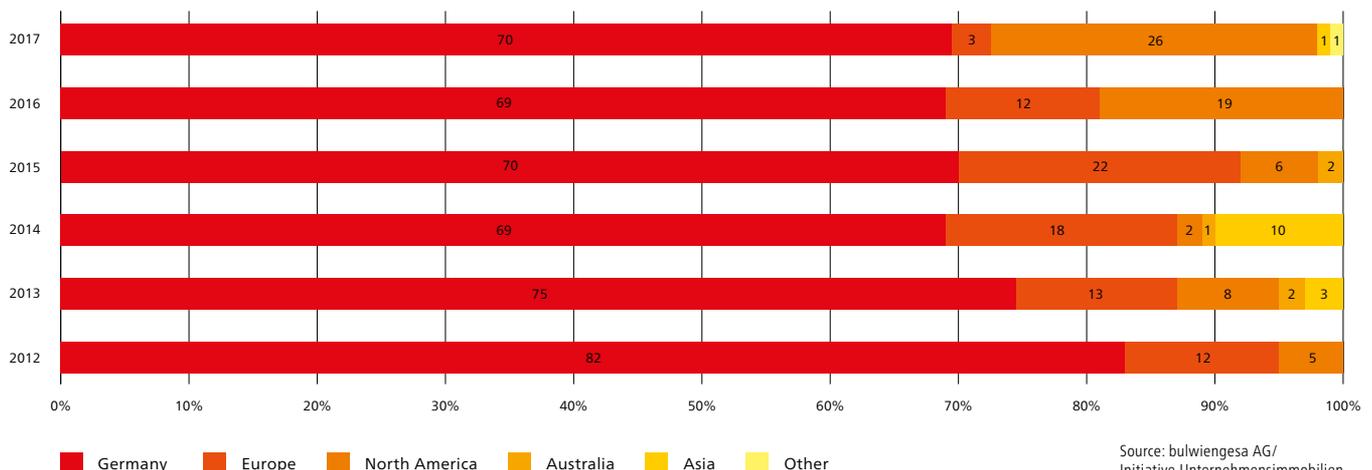
On the one hand, warehouse properties have been the asset type of choice. Large-scale logistics assets, while equally popular among international buyers, are not considered part of the Unternehmensimmobilien category. Although light manufacturing properties, in addition to warehouses, were favoured in the early days of the market survey, business parks have increasingly moved into focus since 2015. They are acquired alongside the still popular, fast-trading warehouse properties. However, the investment volume in each property category is defined by a contracting supply situation.

International investors have previously bought mainly in or near German metro regions. This implies that the Unternehmensimmobilien assets acquired are exposed to relatively low investment risks because of favourable demographic and economic developments in those regions. Conversely, domestic investors with a detailed knowledge of the market will often invest in Unternehmensimmobilien outside the conurbations because they have an easier time appraising a given property over and above its macroeconomic performance indicators.

One needs to remember that, on the one hand, a huge stock of Unternehmensimmobilien exists outside the metro regions in Germany and that, on the other hand, there are countless SMEs—many of them hidden champions—who qualify as tenant leads. Lately though, foreign investors, supported by the competence of experienced and independent advisers, have started to exploit investment opportunities beyond the conurbations.

Now, as then, Unternehmensimmobilien assets are owner-occupied more often than is the case in the United States or the United Kingdom. To ensure that the German market for Unternehmensimmobilien remains a sustainably attractive investment destination, and to prevent a slowdown in investment activity due to short supply, the bulk of the previously owner-occupied stock should be diverted to the investment market. This is particularly true for the floor space stock of major industrial companies that are often no longer required for owner-occupancy in their entirety.

Breakdown of purchases by origin



## Martin Czaja on Doing Business with International Investors



Martin Czaja,  
Speaker of the Board, BEOS AG

### **Generally speaking, are international investors easier or harder to handle than domestic German investors?**

I'm afraid there is no general answer to that. The market operators are simply too different. Principally, no investor is difficult to handle if you maintain an open and fact-based exchange. It is important in this line of business to see eye to eye—regardless of where the other party comes from.

### **Have you observed any specificities in the hands-on dealing with international investors?**

Our experience with international investors has been that they take an unusually strong interest in operative issues. Whenever events come into play that impact the performance, they will be scrutinised—no matter whether the ramifications are positive or negative. The time intervals between personal meetings tend to be slightly longer than they would be with domestic investors. But once you sit down together, the exchanges are decidedly intense.

### **Are there any pitfalls in cross-border business that you habitually overlook if you are not careful?**

Difficulties interpreting German law regularly become an issue. Especially the differences between federal and state-level law in the planning and building codes requires frequent explainers. Germany's federalist structure is rather peculiar, to be sure.

I also noted that liability issues seem to have a much higher significance abroad—even if not everybody here in Germany can comprehend it. But apparently it is easier in some countries to directly enforce liabilities against the capital owners. Accordingly, we need to take this subject very seriously to keep a given transaction from running into trouble.

And finally, when dealing with investors from America or the Far East, the time differences are an issue that should not be underestimated by either side.

### **Where do cultural differences become particularly obvious, especially as far as Anglo-Saxon investors are concerned?**

With investors of this group, the financial engineering aspect tends to be highly developed. By contrast, German investors are more focused on the asset and its use—which I, by the way, find a rather sensible things to do. In addition, market comparisons play a bigger role. This is attributable primarily to the fact that Anglo-Saxon real estate markets are still far ahead of us in terms of transparency.

### **Without international investors, would the breakthrough of the Unternehmensimmobilien asset class have been possible at all?**

The answer is clearly No. In the same sense that international investors have made swifter progress in terms of transparency, they are also more experienced in our asset class. A look at the ownership rates alone suggests as much: While 70 % of the companies in Germany own their real estate outright, the ratio is no more than 40 % in the United Kingdom, only 30 % in the United States, and just 20 % in Asia. Indeed, the German Unternehmensimmobilien market would not have taken off the way it did without international investors.

## Credits

Published and edited by:	
Office of the INITIATIVE UNTERNEHMENSIMMOBILIEN	Andreas Schulten bulwiengesa AG Wallstrasse 61 D-10179 Berlin Phone: +49 30 278768-0
Scientific processing, data handling, and editing:	Project management Tobias Kassner bulwiengesa AG Moorfuhrweg 13 D-22301 Hamburg Phone: +49 40 42 32 22-20 kassner@bulwiengesa.de
Project assistants	Lars Diekmann Marcel Schwerin
Editorial deadline	31 May 2018
Concept & design	elevenfifteen GmbH elevenfifteen.de
Copyright © 2018	

All rights reserved. Excerpts may be used if "INITIATIVE UNTERNEHMENSIMMOBILIEN" is cited as their source.

Extensive reproduction, publication, and disclosure of contents to third parties in any form whatsoever is principally permitted only subject to prior written authorisation by INITIATIVE UNTERNEHMENSIMMOBILIEN, and any of the above must cite the original source.

Exempt is the use of the UI Insight publication or parts thereof for marketing brochures, these being subject without exception to the requirement of prior written consent by INITIATIVE UNTERNEHMENSIMMOBILIEN. The point of contact is the registered office of the Initiative.

### Disclaimer (Exclusion of Liability)

The findings and calculations presented in this survey as well as the research conducted are based on evaluations by bulwiengesa AG, and were 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 adopted from third parties.

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

### Title image

Aerial view on the Sirius Business Park Potsdam, Sirius  
Source: Sirius Facilities GmbH

INITIATIVE UNTERNEHMENSIMMOBILIEN is a joint project by:

