Germany
Market Report

Office and Investment Market
Q1 2016

Accelerating success.

Expected breather of investment volumes, strong take-up in Q1 2016

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Office Letting

The activity in Germany's seven largest office markets again picked up speed in Q1 2016. The strong results we saw in Q1 2015 were topped by 8.3% with 794,000 sqm in take-up.

Dynamic of take-up gained momentum in Q1 2016

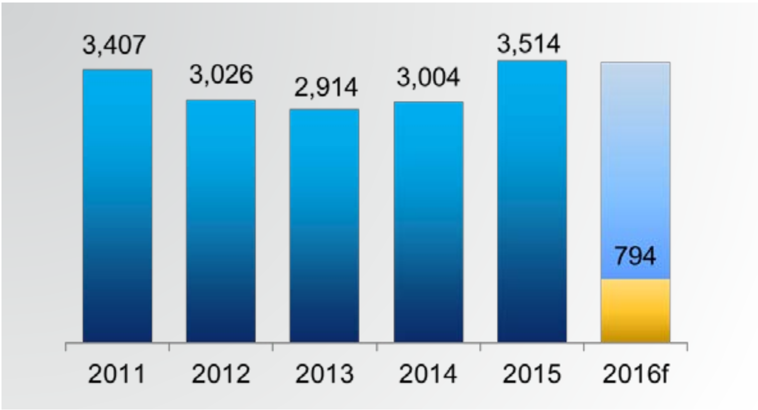
Spurred by the ongoing favorable employment numbers in Germany, net absorption has also been very high over the past 12 months at 1.3 million sqm. In view of the fact that investment activity by German companies is currently relatively sluggish, demand for additional space beyond moving to a new location, which reflects true leasing performance, does not yet appear to have reached its peak.

Berlin still a highly popular office location

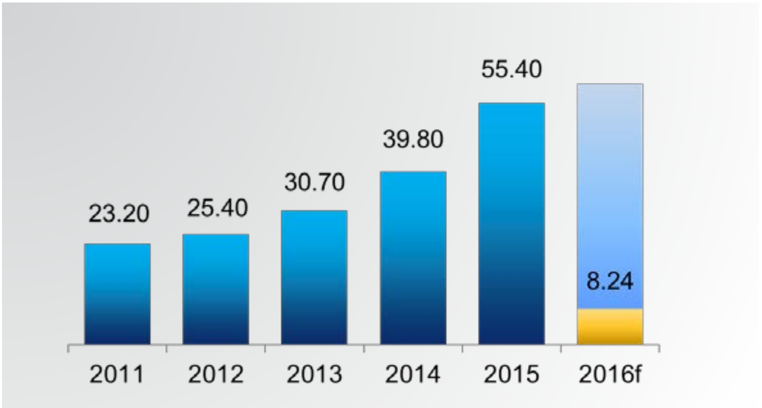
Munich and Berlin posted the highest take-up results in Q1, each with around 180,000 sqm. Berlin saw an increase of around 35% compared to Q1 2015. These results confirm that the German capital, which held the pole position among the Big 7 throughout 2015, continues to be very popular among office tenants.

Munich remained true to 2015's good results. A total of five leases for more than 5,000 sqm each were signed during the first three months of the year, two of which involved owner-occupiers. MorphoSys signed the largest-scale lease, taking up 12,100 sqm at the former Imtech building in Planegg, west of Munich.

Take-up of Office Space in the Top Seven Cities (in 1,000 m²)



Commercial Transaction Volume in Germany (in billions of euros)



The year also got off to a good start in Frankfurt with a considerable 42% yoy increase in take-up to 123,400 sqm. The 19% increase in the number of leases signed can also be attributed to heavy demand across all space segments. With last year only posting one lease signed for more than 10,000 sqm, four leases in this space category have already been signed this year, including the lease signed by the European Central Bank for 17,800 sqm at the Japan Center.

Düsseldorf posted the most favorable yoy results with take-up increasing by almost 50% to roughly 110,000 sqm. These results can be partly attributed to the large-scale lease signed by Uniper for 28,000 sqm at a project development in the Hafen submarket. Even without this large-scale lease being signed at the turn of the year, however, results would still be up 12% yoy. High take-up in all space segments contributed to these results.

Hamburg just missed the 100,000-sqm mark, finishing off Q1 2016 23% behind the strong start to 2015. Low completion volumes struggled to meet high demand for new-build space, creating promising conditions for speculative development.

The Stuttgart office leasing market experienced lively leasing activity at the start of the year with a total of 76 leases signed and take-up of 61,100 sqm, results that are not to be overshadowed by the 12% drop compared to 2015's very strong Q1. Owner-occupiers accounted for a very low share of total take-up. Traditionally, demand has been very high when it comes to smaller units of less than 500 sqm located in downtown submarkets. Large-scale tenants, on the other hand, primarily signed leases for larger-scale units in the city outskirts due to limited availability.

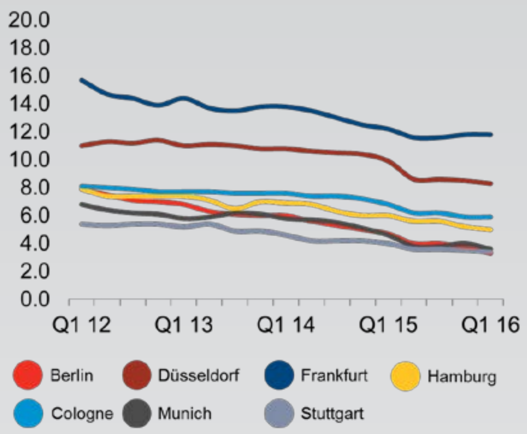
Take-up in Cologne was down by comparison to 44,500 sqm, dropping yoy by around one third.

Space available for immediate tenancy very limited in many locations

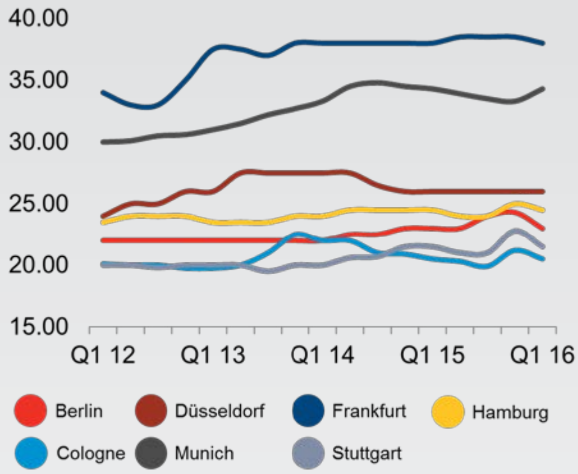
Office vacancy continued to drop in all cities surveyed due to lively demand facing continued moderate new-build activity. Only 4.8 million sqm were vacant at the end of March 2016, reflecting a vacancy rate of 5.4%. This limits the possibility that tenants looking for more than 5,000 sqm in popular locations in numerous office markets will find what they seek. In the Big 7, total space available for immediate tenancy was down 921,000 sqm (16%) yoy.

In Berlin, where the decrease in vacancy yoy was steepest at 30% and the vacancy rate was lowest among the major German office markets at 3.3%, it is becoming increasingly hard to adequately satisfy demand even when it comes to the small-space segment.

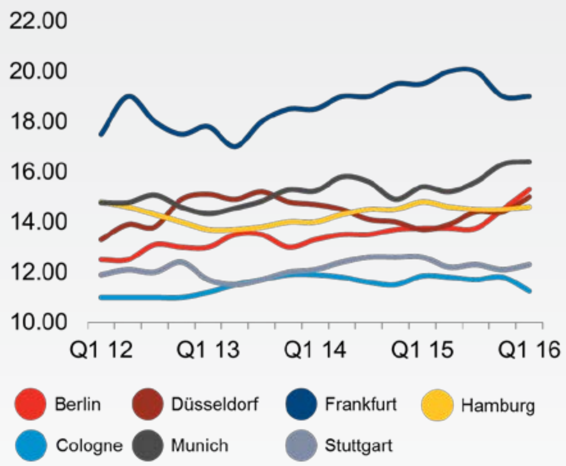
Comparison of Vacancy Rates (in %)



Comparison of Prime Rents (in /m²)



Comparison of Average Rents (in €/m²)



Most other cities are experiencing a similar trend. In Stuttgart and Munich the vacancy rate in Q1 was also below 4%. Vacancy in Stuttgart declined by 60 basis points to 3.4% over the course of the past 12 months; in Munich it fell by 100 basis points to 3.6%. In Hamburg vacancy experienced a similar decrease to 5.0%, dropping below the average calculated for the office hubs surveyed.

In contrast, vacancy in Düsseldorf was above average at 8.3%. However, the vacancy rate here has also dropped significantly. In Cologne, the vacancy rate declined to 5.9%. Frankfurt's vacancy rate remains in the double digits at 11.8%, and the city continues to have more than one million sqm of vacant space available. Nevertheless, vacancy has also dropped here by around 100,000 sqm.

Rise in prime rents has come to a standstill

Following a considerable rise in prime rents in some locations over the course of the second half of 2015, this development has come to a standstill at a high level in most locations. Frankfurt remains at the high end of the price range at €38.50 per sqm, with Cologne at the lower end at €18.20 per sqm. In view of the rise in demand at the beginning of 2016, the stabilization of prime rents can largely be attributed to a lack of supply of new space in the high-price segment.

For what is already the fifth quarter in a row, the situation caused prime rents to stagnate in Düsseldorf and even drop in Munich. Cologne experienced a decrease in prime rent as well.

In contrast, average rent levels varied in the office hubs surveyed. Over the course of the past 12 months, average rents in Berlin, Düsseldorf and Munich increased by 11.3%, 9.5% and 6.5%, respectively. Demand in these locations is shifting in favor of older stock properties in non-central locations due to scarce supply of prime properties. In contrast, average rent fell by 2.6% in Frankfurt, the city with the most potential when it comes to alternative properties. Average rent also fell slightly in Stuttgart and Hamburg by 2.4% and 1.4%, respectively. The steepest drop was recorded in Cologne at 5.1%.

Outlook:

Following the favorable start to the year, all indications point to solid performance on the German office leasing market for the entire year of 2016. The economic upturn, which has so far been consumption-based, could trigger additional demand for office space if companies decide to increase their investment activity. With these developments, take-up could reach stong results already recorded in 2015 at 3.5 million sqm. However, similar to the investment market, supply could be a limiting factor.

Investment

German commercial real estate transaction volume took an expected breather after a remarkable end-of-year rally. At €8.2 bn, transaction volume in Q1 2016 was only half as high as in Q4 2015. A considerably larger number of transactions were successfully brought to a close before year-end than in previous years.

Transaction volume remains at a high €8.2 bn

It is important to also put Q1's 15% decrease in transaction volumes into perspective in a quarterly comparison with the two previous years. There has been a lack of large-volume portfolio and single deals since the beginning of 2016, deals that largely contributed to the exceptional results of €10 bn generated in the comparison periods. A portfolio worth billions changed hands in the first three months of both 2014 and 2015. These transactions included the sale of the Leo I portfolio to Patrizia Immobilien AG and the transfer of a shopping center package to Klépierre. Investors also signed single deals valued at more than €500 m such as the share acquisition of CentrO Oberhausen.

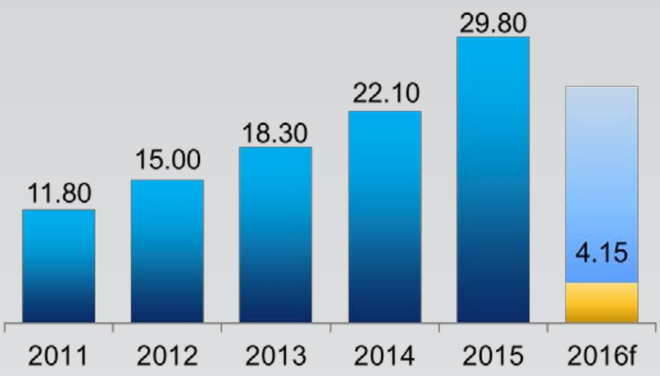
The largest deal signed in Q1 2016 just before the end of the quarter amounted to around €280 m, with WealthCap Management GmbH purchasing BayWa headquarters in Munich for a special real estate fund. The largest portfolio deal changed hands for €250 m: the Victoria portfolio consisting of 21 retail properties sold to Patrizia Immobilien AG. The sale of Forum Hanau, which project developer Hanseatische Betreuungs- und Beteiligungsgesellschaft (HBB) sold to asset and fund manager Hamburg Trust for around €200 m, concludes the list of transactions exceeding €200 m. The total share of transactions exceeding €100 m has decreased from around one third in Q1 2015 to a current one quarter.

Lack of mega deals, drop in portfolio share and moderate foreign investor market presence

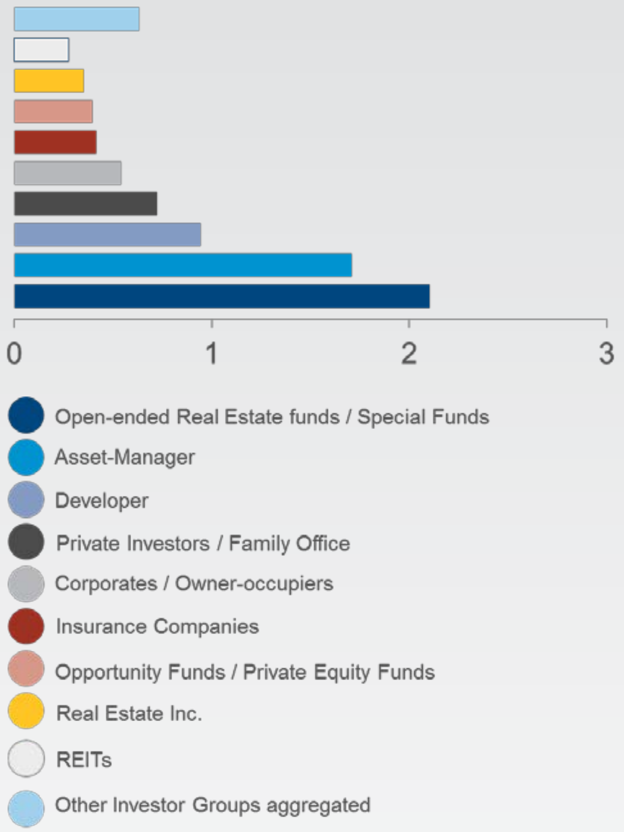
In total, portfolio deals played a considerably lesser role in Q1 than in all of 2015. The decrease in market share from 39% to a current 24% is quite considerable. A close connection can be made between the lack of mega deals, in particular in terms of portfolio deals, and the market presence of foreign investors, which has been decreasing since the beginning of the year.

While international investors accounted for roughly half of transaction volume invested in 2015, their investments made up less than one third of total transaction volume in Q1 2016. Investors from the UK accounted for the bulk of investments made by foreign investors with a total of €860 m. Investors from the other European countries and from outside Europe have been markedly passive in the past three months.

Commercial Transaction Volume in the Top 7 Cities (in billions of euros)



Transaction Volume according to Buyer Groups (in millions of euros) Q1 2016



Development of the Gross Initial Yield

	Office	Retail	Industrial & Logistcs
Berlin	↓	↓	↓
Düsseldorf	↓	↓	↓
Frankfurt/M.	↓	↓	↓
Cologne	↓	–	↓
Hamburg	↓	↓	↓
Munich	↓	↓	↓
Stuttgart	↓	↓	↓

US players invested €420 m in Germany; investors from France only accounted for half of that. As a result, their market shares decreased to 5% and 3%, respectively. German investors took an exceptionally dominant position, generating a volume of €5.7 bn, more than two thirds of total investment volume.

Though, the German commercial real estate market has in no way lost its appeal to foreign investors. On the contrary, Germany's sustained, consumer-driven growth and political and economic security in times of increasing global economic instability will most likely further increase Germany's attractiveness as a safe investment haven. In view of the ECB further loosening its monetary policy, real estate remains a comparatively attractive investment opportunity. With leasing markets growing more popular, i nvestors will accept the expected further increases in purchase prices.

Pressure to invest, particularly on the part of large institutional investors, will increase further as a result. Open-ended real estate funds and special funds as well as asset and fund managers acting on behalf of equity-strong investor groups dominated the market throughout Germany with €2.1 bn (26%) and €1.7 bn (21%), respectively. The strongest seller group was project developers with a market share of 29%. This development can partly be attributed to investors on the lookout for core products, which are becoming harder to find in view of increasingly limited supply.

Hotel and logistics properties strengthen their position as an established asset class

Limited supply of products and an increasing tendency towards taking risks are contributing to a shift in the market shares of some property types. Due to the significance of single deals in this quarter, office properties were able to achieve a 45% share of current investment volume, remaining the strongest segment. In view of the lack of deals involving large shopping centers, however, the retail property market share fell to 18%. At the same time a higher number of retail warehouse, super market and DIY store portfolios changed hands. Looking at package deals alone, the share of retail properties comes to 43%, making this property type the dominant asset class. In turn, the rise in hotel and logistics property transaction volumes that the market has been experiencing continues. Hotels accounted for 9% and logistics properties for 11% of total transaction volume. In addition, a large number of properties used for healthcare and social purposes changed hands, generating a total market share of 5%. Just in terms of portfolio transactions, the numerous care facilities largely sold in the context of package deals accounted for 16%.

Drop in high-volume deals noticeable, particularly in the Big 7

The drop in high-volume deals is also affecting investment volumes in the major German investment hubs. Nevertheless, transaction volume in the Big 7 only decreased yoy by 13% to €4.1 bn. Thanks to the landmark deal involving BayWa headquarters just before the end of the quarter, Munich once again cracked the one-billion-euro mark. This makes the city the market with the highest transaction volume despite a drop of 8%.

Frankfurt posted the strongest drop in transaction volume with 45%, with deals rare especially in the traditionally strong office asset class. The largest transaction of more than €80 m, the Villa Kennedy luxury hotel, boosted total transaction volume to €637 m. In combination with other hotel transfers, this segment achieved a market share of 44%, reflecting the popularity of hotel investments in the city on the Main river.

The top performer of 2015, Berlin, also suffered a yoy drop of 35% in transaction volume to €710 m, falling back to third place among the major German investment hubs behind Munich and Hamburg. Cologne, which recorded the lowest transaction volume among the Big 7, experienced a more moderate decline of 16% to €240 m. In a yoy comparison, performance was highest at the start of the year in Stuttgart, with a 95% increase to €355 m, and Düsseldorf with an increase of 78% to €320 m. Hamburg also again managed to expand the previous year's strong quarterly results by 11% to €830 m.

Prices continued to increase in many locations due to ongoing pressure to invest. Yields once again fell considerably by 25 basis points in Munich, Düsseldorf and Frankfurt. Prime yields for office property are currently recorded at between 3.50% in Munich and 5.00% in Cologne.

Outlook: Supply bottlenecks could put a damper on recent record transaction volumes

The transaction volume posted during the first three months, which was high compared to the long-term average, as well as the favorable general conditions, which are tending to improve rather than worsen in an international context in favor of the German commercial real estate market, are a strong indication that record results similar to 2015 are likely to be reached this year. More high-volume deals are expected to be signed in the coming quarters based on the negotiations that are currently underway. The scarcity of high-volume landmark properties favored by foreign investors could be the greatest obstacle in setting a new transaction volume record.

Office Letting and Investment Market Germany Q1 2016

Key Facts								
	Top 7	BERLIN	DÜSSELDORF	FRANKFURT	HAMBURG	COLOGNE	MUNICH	STUTTGART
Office Leasing Market								
Take-up 2016 in m²	**794,000**	**179,300**	**109,700**	**123,400**	**95,300**	**44,500**	**180,700**	**61,100**
Take-up 2015 in m²	*732,900*	*133,100*	*73,500*	*87,000*	*123,000*	*66,000*	*180,600*	*69,700*
Change y-o-y	+ 8.3 %	34.7 %	49.3 %	41.8 %	-22.5 %	-32.6 %	0.1 %	-12.3 %
Prime rent 2016 in €/m²		**24.30**	**26.00**	**38.50**	**25.00**	**18.20**	**33.00**	**22.80**
Prime rent 2015 in €/m²		*23.00*	*26.00*	*38.00*	*24.50*	*20.50*	*34.30*	*21.50*
Change y-o-y		5.7 %	0.0 %	1.3 %	2.0 %	-11.2 %	-3.5 %	6.0 %
Average rent 2016 in €/m²		**15.30**	**15.00**	**19.00**	**14.60**	**11.25**	**16.40**	**12.30**
Average rent 2015 in €/m²		*13.75*	*13.70*	*19.50*	*14.80*	*11.85*	*15.40*	*12.60*
Change y-o-y		11.3 %	9.5 %	-2.6 %	-1.4 %	-5.1 %	6.5 %	-2.4 %
Vacancy 2016 in m²	**4,770,800**	**610,500**	**635,200**	**1,314,800**	**675,000**	**454,500**	**823,200**	**257,600**
Vacancy 2015 in m²	*5,699,700*	*870,000*	*753,000*	*1,410,000*	*800,100*	*522,000*	*1,040,000*	*304,600*
Vacancy Rate	**16.3%**	**3.3 %**	**8.3 %**	**11.8 %**	**5.0 %**	**5.9 %**	**3.6 %**	**3.4 %**
	Germany	BERLIN	DÜSSELDORF	FRANKFURT	HAMBURG	COLOGNE	MUNICH	STUTTGART
Commercial Investment Market								
Transaction volume in millions of euros 2016	**8,237**	**710**	**320**	**637**	**830**	**240**	**1,056**	**355**
Transaction volume in millions of euros, 2015	*9,742*	*1,100*	*180*	*1.100*	*750*	*286*	*1.143*	*182*
Change y-o-y	-15%	-35%	78%	-42%	11%	-16%	-8%	95%
Largest group of investors	Asset managers / Fund managers 26%	Other investors 38%	Open-ended real estate funds / Special funds 67%	Open-ended real estate funds / Special funds 38%	Asset managers / fund managers 35%	Opportunity Funds / Private equity funds 28%	Open-ended real estate funds / Special funds 34%	Open-ended real estate funds / Special funds 65%
Largest group of sellers	Property developers 29%	Asset managers / Fund managers 26%	Banks 37%	Property developers 46%	Property developers 25%	Corporates / Owner-occupiers 29%	Property developers 41%	Property developers 50%
Most important type of real estate	Office 45%	Office 78%	Office 91%	Office 55%	Office 67%	Office 88%	Office 74%	Offide 43%
Prime yield office		4.00%	4.50%	4.30%	3.90%	5.00%	3.50%	4.30%
Prime yield retail		4.00%	4.10%	3.85%	3.90%	4.20%	3.00%	3.90%
Prime yield industrial		6.00%	5.90%	5.80%	6.20%	6.00%	5.40%	5.80%

Source: Colliers International, Grossmann & Berger (Hamburg, comparison figures from 2015), Larbig & Mortag (Köln)

554 offices in **66** countries on **6** continents

United States: **153**
Canada: **34**
Latin America: **24**
Asia Pacific: **231**
EMEA: **112**

€ 2.3
billion
In annual revenue

€ 103
billion in transaction volume with more than 80,000 investment and leasing deals

186
Million square meter under management

16,000
professionals worldwide

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