Real Estate House View
Germany

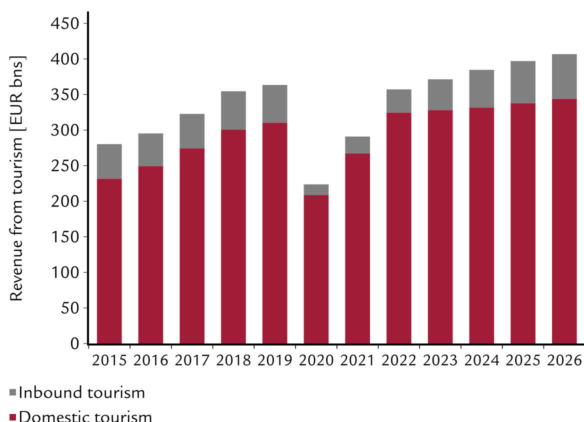
SwissLife
Asset Managers

First half of 2022

Key takeaways

– **Real estate remains an attractive asset class:** Interest rates for German government bonds are low, the money supply is high, (temporary) inflation is devaluing money and penalty interest remains in force. It therefore comes as no surprise that real estate investments remain a sound option (perhaps even the only one?) for investing capital.
– **Germany remains the most attractive investment market:** Due to its size and stability, Germany represents one of the most attractive real estate markets. As a result, more than a third of the European investment volume was placed in German real estate in 2021; 2022 is likely to continue on a similar note.
– **Safety first:** As the markets are still shaped by economic uncertainty despite signs of recovery, investors will in future continue to seek safe havens such as residential and logistics. Core properties are in demand at less safe havens – as has been the case since the start of the pandemic.
– **Looking beyond the immediate environment is advisable:** Polarisation is leading to a herd effect. Particularly in the office market it might be wise for investors to look beyond their immediate environment, while attention should also be paid to property quality in logistics/industrial.
– **Sustainability is increasingly being implemented:** The topic of sustainability is being backed more and more in both the rental and investment market – at present particularly in the office sector. ESG is also gaining importance and being taken into account for other types of use.

Chart in focus



No sector has been affected so much by the pandemic and the lockdowns as the hotel industry. Initial tentative signs of recovery already emerged in 2021: tourism revenue was 30% up on 2020. According to McKinsey, domestic tourism should already reach its pre-crisis level again in 2022. Inbound tourism is likely to take a year longer. Altogether the German tourism sector can be expected to recover somewhat more rapidly than the European average, with the decisive factor set to be the very high share of domestic tourism of over 80% that countries such as Spain and Italy are unable to draw on.

According to the high frequency indicators of the German Bundesbank on economic activity and data from the automotive industry, the economy grew again at the end of 2021. Germany is displaying the greatest catch-up potential here among the leading economies. So far, the domestic economy has recovered less quickly from the slump than that of the USA and the neighbouring countries of Switzerland and France, as supply bottlenecks for primary products have put car manufacturers under pressure. There have recently been signs of an improvement in the supply of semiconductors. As a result, industrial production should recover further in the coming quarters and support German growth in 2022. Inflation rates above 5% are expected only to be a temporary phenomenon. They will already fall again in the next few months. The annual inflation rate is set to fall below 2% by mid-2022. In the medium term we expect inflation to level out near the ECB target of "close to but below 2%".

Everyone loves Berlin...

... and Munich and Frankfurt. Around 66% of the nationwide volume of office transactions was accounted for by these cities in 2021. The top seven even achieved a share of 88%. The reason is – allegedly – the lack of any alternative to a flight to the core markets, the prime rents of which were stable to rising in 2021. The prime yields in the top seven are accordingly falling further and now lie below 3%. That there are alternatives can be seen from a glance at the distribution of office workers, 78% of whom work outside the top seven. That prime rents are also rising and achieving acceptable levels in B and C cities is illustrated clearly by cities such as Bonn and Potsdam, where prime yields are still above the magic 3% threshold. A selective look beyond the immediate environment (of investors) could pay off.

People will always need somewhere to live!

The cliché continues to hold true. The only thing that is lacking is affordability, at least in the large cities. The new Federal Government has therefore decided to address the issue: the newly created Ministry of Construction is to create 400 000 additional apartments each year, and initial regulations are also entering into force. The rent cap is being extended until 2029, and rents in strained housing markets may not rise by more than 11% within three years, down from 15% previously. Investors are nevertheless expected to remain well-disposed to the German housing investment market, as German residential properties continue to offer a sound investment despite potential regulation: rents are stable to increasing and rising property prices are forcing households to rent.

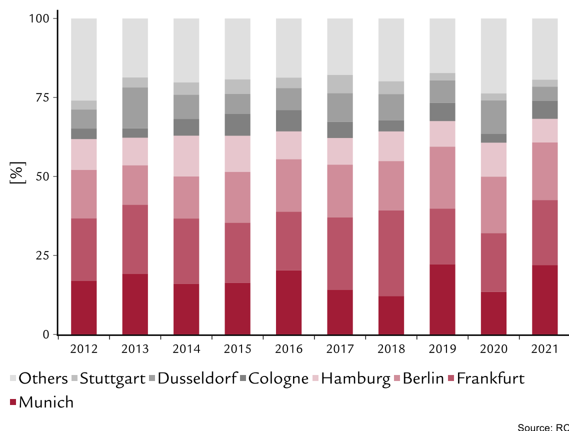
People will also always need to eat!

This truism explains why investors in retail favour supermarkets, speciality shopping malls and local suppliers, as these segments offer stable cash flows and are suffering less – at least at the moment – from the competition of e-commerce that is weighing down on high streets and shopping centres. Prices for speciality shopping malls therefore increased slightly in 2021, while those for prime locations in the top seven once again fell. However, the prime locations should recover in the long term. It can be seen from initial developments of new ground floor concepts that the tenant market is adjusting to the new reality. And on the subject of concepts: food retailers will find themselves obliged to offer online groceries, with the big players set to develop their own concepts.

And people are ordering more and more!

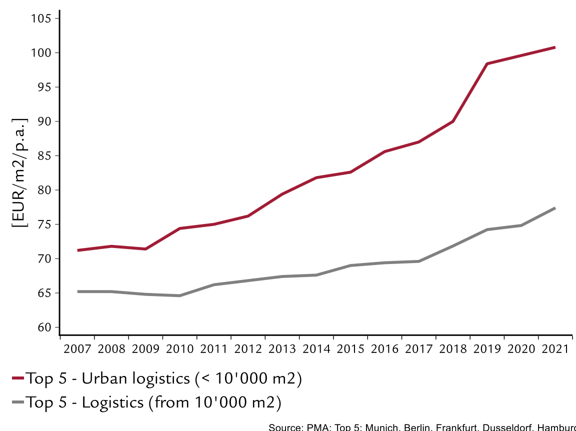
Revenues in e-commerce continued to increase further even after the reopening of shops: they were 8.8% higher than in the prior-year period from May to September 2021. The ongoing trend towards e-commerce is increasing demand for corresponding space. On top of this, supply chains are being restructured and storage/production capacities transferred into the country from abroad. As a result, space take-up reached a new record in 2021 (Q1-Q3: approx. 6 million m^2). Rents are also only pointing in one direction – upwards, especially for urban logistics space. Investors remain attracted by the fundamentally intact tenant market and are accordingly pushing down net prime yields towards 3%. Further compression is to be expected as the drivers are unbroken. Despite, or even because of the momentum, investors should pay attention to quality.

Figure 1: Share in volume of office transactions by market



Source: RCA

Figure 2: Prime yields for logistics and urban logistics space



Source: PMA; Top 5: Munich, Berlin, Frankfurt, Dusseldorf, Hamburg

Authors

Swiss Life Asset Managers, Germany

Andri Eglitis
Head Research
andri.eglitis@swisslife-am.com

Gudrun Rolle
Research Analyst Real Estate
gudrun.rolle@swisslife-am.com

Swiss Life Asset Managers

Francesca Boucard
Head Real Estate Research & Strategy
francesca.boucard@swisslife-am.com

Marc Brütsch
Chief Economist
marc.bruetsch@swisslife-am.com

Do you have any questions or would you like to subscribe to this publication?
Please send an email to info@swisslife-am.com.
For more information, please visit our website at www.swisslife-am.com/research.

Released and approved by the Economics Department, Swiss Life Asset Management Ltd, Zurich
Swiss Life Asset Managers may have acted upon or used research recommendations before they were published. The contents of this document are based upon sources of information believed to be reliable but no guarantee is given as to their accuracy or completeness. This document includes forward-looking statements which are based on our current opinions, expectations and projections. We undertake no obligation to update or revise any forward-looking statements. Actual results could differ materially from those anticipated in the forward-looking statements.
France: This publication is distributed in France by Swiss Life Asset Managers France, 153 rue Saint-Honoré, F-75001 Paris to its clients and prospects. **Germany**: This publication is distributed in Germany by Swiss Life Asset Managers Deutschland GmbH, Aachener Strasse 186, D-50931 Köln, Swiss Life Asset Managers Luxembourg, Niederlassung Deutschland, Hochstrasse 53, D-60313 Frankfurt am Main and BEOS AG, Kurfürstendamm 188, D-10707 Berlin. **UK**: This publication is distributed by Mayfair Capital Investment Management Ltd., 55 Wells Street, London W1T 3PT. **Switzerland**: This publication is distributed by Swiss Life Asset Management Ltd., General-Guisan-Quai 40, CH-8022 Zurich. **Norway**: Swiss Life Asset Managers Holding AS, Haakon VIIs gt 1, NO-0161 Oslo.