PRESS RELEASE

Hamburg/Münster, 2 October 2019

German Real Estate Market 2019/2020: Top locations remain attractive

- **DZ HYP publishes study on the commercial real estate markets of seven German metropolitan areas**
- **Positive labour market data is driving demand for the office property market**
- **Number of completed residential properties is growing**

The German commercial real estate market has maintained its uptrend. So far, the subdued economic outlook has had no real impact on the market – in fact, retail, office and residential segments are being influenced by other factors. High demand for office properties – in conjunction with a scarce supply of space – leads to persistent rent increases. In the residential asset class, increasing completion figures have slowed down price momentum. The retail sector in Germany's top locations is expected to buck the trend of falling top rents until the end of 2020. These are the results of the latest research report published by DZ HYP, covering developments on the commercial real estate markets of Germany's top locations: Hamburg, Berlin, Dusseldorf, Cologne, Frankfurt, Stuttgart and Munich.

"Demand for office and residential space remains strong in the metropolitan areas. Therefore, increasing new construction activity is encouraging and provide some relief in certain areas. At the same time, it is impossible to close the gap created by strong demand within a short space of time. We are observing sustained rent increases - albeit with abating momentum", says Georg Reutter, Chairman of the Management Board of DZ HYP, and adds with regard to investors: "The yield gap has developed in favour of commercial real estate. Investors continue to focus on this asset class, which continues to gain attractiveness relative to bonds."

Large office spaces barely available at short notice

Employment growth which has lasted for several years has led to increasing demand for office space, which markedly exceeded supply in the recent past. As a consequence, vacancies in the metropolitan regions decreased from more than 10 per cent in 2010 to an average of around 3 per cent by mid-2019. Currently, almost the half of approximately 2.5 million square metres of unlet office space are attributable to Dusseldorf and Frankfurt. With vacancy rates of just under 7 per cent, both cities still have a comparatively good supply of space. However, vacancies in Berlin, Cologne, Munich and Stuttgart have already fallen to around 2 per cent. This means that approximately 300,000 square metres are unlet in Berlin – less than 200,000 sqm in each of the other three cities.

Given the scarce supply, a significant part of completed rental contracts concerns new construction projects. Businesses can move into these offices only after completion – after a certain waiting period. Larger connected spaces are practically no longer available at short notice, which is why a growing number of companies switch to co-working environments. The segment of flexibly-rented office space continues to grow strongly, whilst aggregate space on offer remains manageable.

On average, prime rents in the lop locations have increased by 40 per cent since 2010. The extent of the rental growth can be largely attributed to the dynamic market in Berlin, where the top rent rose by 80 per cent during the observation period. With 20 per cent, Cologne recorded the lowest growth rate. For the coming months, slight changes to the market situation are on the horizon. Given that the supply of space is growing this year, and will continue to rise especially in the next year, vacancy rates may have seen their lowest levels. ‚As demand is expected to adjust to the economic slowdown. rental momentum is expected to ease until the end of 2020.

Increasing housing construction slows down the rise in rents

The combination of continuous population growth and insufficient new construction activity has impacted the residential real estate markets across all top locations over recent years. As a consequence, average first-occupancy rent levels increased between 35 per cent in Cologne and 65 per cent in Berlin since 2008. With rental prices ranging from €13 per square metre in Dusseldorf to just under €20 in Munich, the construction of multi-family houses has become more attractive for investors, as evidenced by the number of new completions. In 2018, more than 50,000 residential units were built in the seven metropolitan areas. This corresponds to a 150 per cent increase compared to the average for the period from 2001 to 2011 (20,000 units).

Given the enhanced offering, rental momentum for newly-built units has decreased. In 2018, the prices for apartments in the top locations increased by an average of around 4,5 per cent; this year, the figure is expected to be around 3 per cent. Developments in Berlin are more dynamic: after an increase of approximately 8 per cent of initial rents in the previous year, we expect 5 per cent by the end of 2019. We may see the slowdown in rental growth continue into the coming year, with expected growth rates of just over 2 per cent. Growth is likely to be even somewhat lower in the top market segment.

Metropolitan areas remain attractive

In comparison to the rest of Germany, the retail sector at the seven top locations benefits in particular from rising visitor numbers and population growth. The mostly above-average purchasing power also plays a role. The growing customer potential helps to mitigate the consequences of the booming e-commerce sector. At the same time, clothing retailers in particular respond to the growing online competition, adapting their bricks-and-mortar concepts by cutting back on selling space. Demand is shifting in favour of supermarkets, drugstores and especially gastronomy providers. In the first half of the current year, the latter replaced fashion retailers as the biggest source of demand for space in the inner cities.

Top rents in the retail sector almost reached an average of €300 in the top locations in 2016, following around ten years of growth. As a consequence of the changed consumer behaviour, rental levels have stagnated on this high level since then. As of mid-year 2019, top rents ranged from €245 per square metre in Stuttgart up to €345 in Munich. With €310 per square metre, the up-and-coming Berlin represents Germany's second most expensive retail location, ahead of Frankfurt and Hamburg. At 44 per cent, the Federal capital has seen the biggest ten-year rent increase. During the forecast period until the end of 2020, top rents are likely to remain stable at the current levels.

DZ HYP regularly analyses developments on the real estate markets in its target business areas. The current study report "The German Real Estate Market 2019|2020" is available for download from our website (https://www.dzhyp.de/en/about-us/market-research/); alternatively, we can send you a copy upon request. The charts are also available upon request.

About DZ HYP AG
DZ HYP is a leading provider of real estate finance in Germany as well as a centre of competence for public-sector clients within the Cooperative Financial Network. DZ HYP services its clients and business partners with a comprehensive range of products and services from its four business divisions of Commercial Real Estate Investors, Housing Sector, Public-Sector Clients, and Retail Customers/Private Investors. The Bank's nationwide presence comprises two Head Offices (Hamburg and Münster), plus Regional Centres in Germany's economic centres and Regional Offices across Germany. Please visit www.dzhyp.de for more information.

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