DIFI-Report

Assessment of the Real Estate Financing Market

Germany | 1st Quarter 2019
Published in February 2019

New version of DIFI remains in negative territory

Bricks-and-mortar retail: recovery in sight?

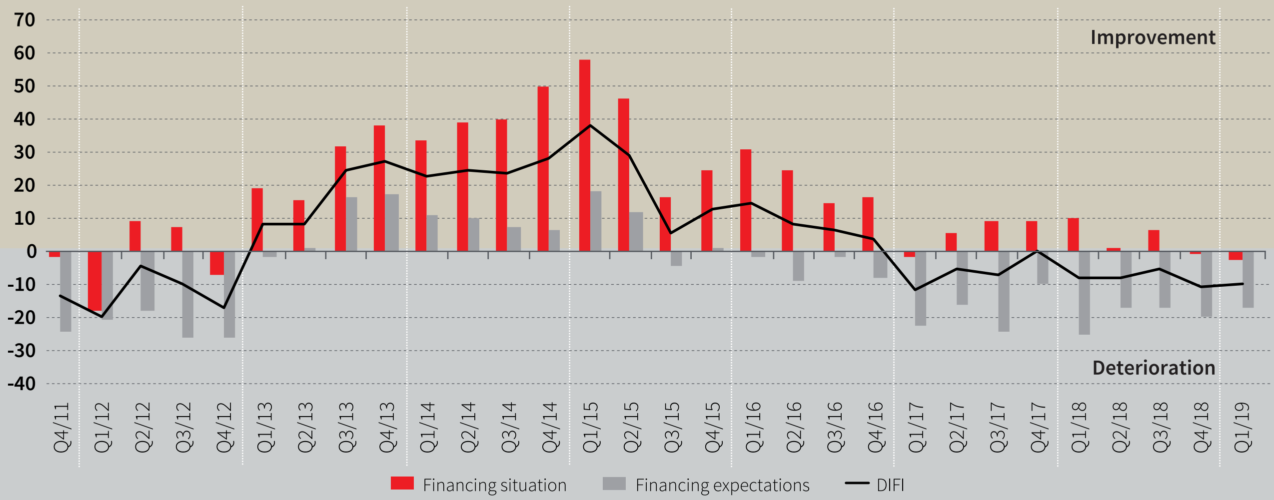
Special question: German property remains in high demand

The German Real Estate Finance Index (DIFI) reflects survey participants' assessments of the current situation in (past six months) and expectations for (coming six months) the German real estate financing market. It is produced quarterly and is calculated on the basis of an average of the results for the office, retail, logistics and residential real estate market segments. These figures reflect the percentage of positive and negative responses received from survey participants relating to the current situation in and financing expectations for the German real estate market. DIFI is produced and published in cooperation with JLL and ZEW – Leibniz-Zentrum für Europäische Wirtschaftsforschung (Centre for European Economic Research).

Pessimistic view continues

German Real Estate Finance Index (DIFI)

Aggregate in % points



Average assessment of the current situation in and expectations for the five real estate market segments (Office, Retail, Logistics, Residential, Hotel).
The time series presented in the report have also included estimates for the hotel real estate segment since Q3/2018.

Source: JLL and ZEW

DIFI still below zero

The **German Real Estate Finance Index (DIFI)** starts 2019 with a new innovation: since the 3rd quarter of 2018, in addition to collecting the experts' opinions on the office, retail, logistics and residential real estate segments, we have also asked them for their assessments of the hotel segment. From this issue of the DIFI report, we will also present the aggregate including this real estate segment, thus including retrospective figures. This reflects the fact that the hotel segment has firmly established itself as a growth sector within the financing market. We have shown the point at which this is included in the time series data in the relevant chart.

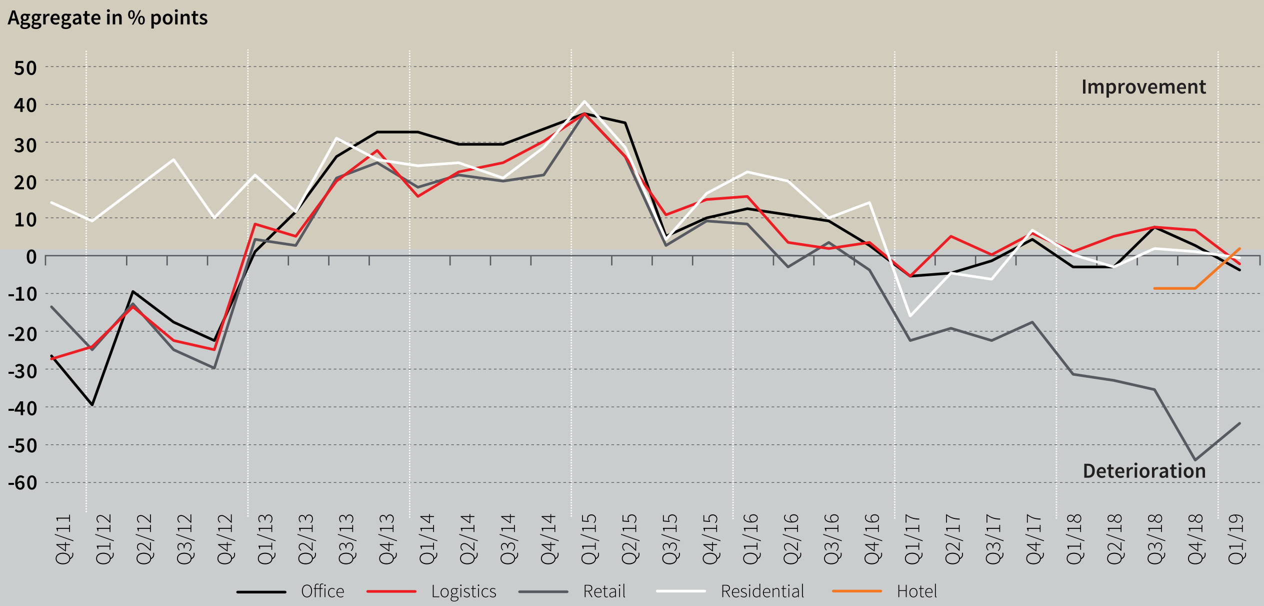
Despite the rather positive assessment of the newly included use class, the "new" DIFI is almost unchanged and again below zero at -9.7 points in the 1st quarter of 2019.

In the previous quarter, the DIFI – comprising expert assessments of the financing situation in the previous 6 months and their expectations for the next 6 months – was at -10.4 points including hotels (-10.8 excluding hotels). This means that the DIFI has been at a consistently sub-zero position for almost 2 years, which reflects the prevailing subdued economic situation that has been cooling down since 2018.

Is the retail segment on course for recovery?

It is perhaps surprising that this quarter has seen a slight trend reversal in the experts' assessments relating to the retail sector. With a current aggregate of -39.4 points, the assessment of the current real estate financing situation is some 10 points higher that it was at the end of last year (-51.5 points). The gloomy future prospects indicated by the experts, including a majority who expected a further

Assessment of the real estate financing market by real estate market segment



Average assessment of the current situation and expectations by defined real estate market segment.
Source: JLL and ZEW

downturn in the last survey, did not turn out to be correct. Also, the financing expectations for the next half year have improved from the previous sub-aggregate of -57.6 points to -50 points. The experts' assessments of the overall situation in the retail sector have slightly improved since the last quarter, but this still does not necessarily suggest a sustainable trend reversal.

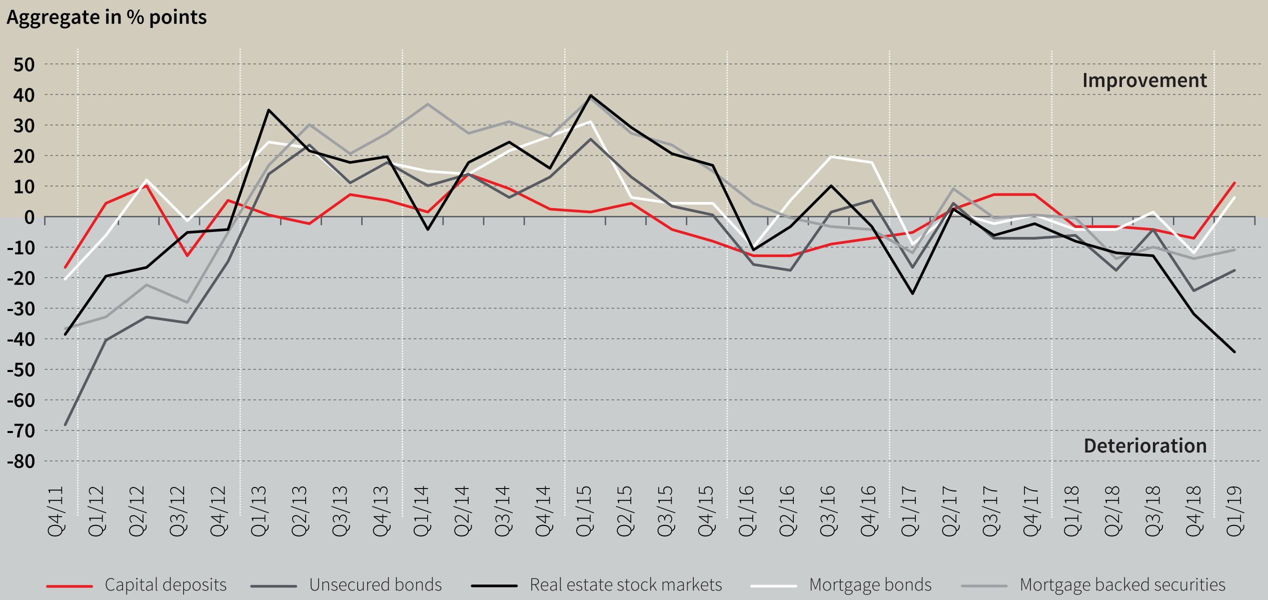
The experts are also similarly in agreement regarding the current situation in the logistics property sector: both the current financing situation and the financing expectations are around 10 points lower in the current quarter. For the first time since 2017, the sub-aggregate for logistics properties is negative. By contrast, there is a slight upswing in the new hotel real estate segment which is the only use type showing a positive aggregate over the New Year (1.9 points). The main reasons for this are the more optimistic financing expectations, which have risen by 20 points from the -23.6 points in the previous survey.

The office and residential use types have continued their zig-zag trajectory around the zero line since 2017. While the financing situation in the office sector fell marginally from 11.7 points to 10.4 points, the residential aggregate slid from 8.8 points to -0.1 point. The expectations in the office property sector fell most strongly of all use types, while residential fell only slightly. As in the previous surveys, the future expectations are significantly more pessimistic than the current situation across all use types, due to the uncertainties resulting from the possibility of a no-deal Brexit with all its negative connotations for German companies and the downturn in the global economy.

Refinancing conditions expected to worsen

The experts view capital deposits and Pfandbrief mortgage bonds as the winners amongst the various refinancing instruments, largely due to positive future expectations: with an increase in expectations of around 25 points in all categories and around 12 points in the assessment of the

Development of the refinancing markets



Average assessment of the current situation and expectations by refinancing instrument.
Source: JLL and ZEW

current situation, these are the only two instruments showing a positive aggregate. The assessment of the current situation and future expectations relating to unsecured bonds each showed a slight improvement of 6.6 points, which is somewhat surprising in view of the expected increased spreads compared to German government bonds.

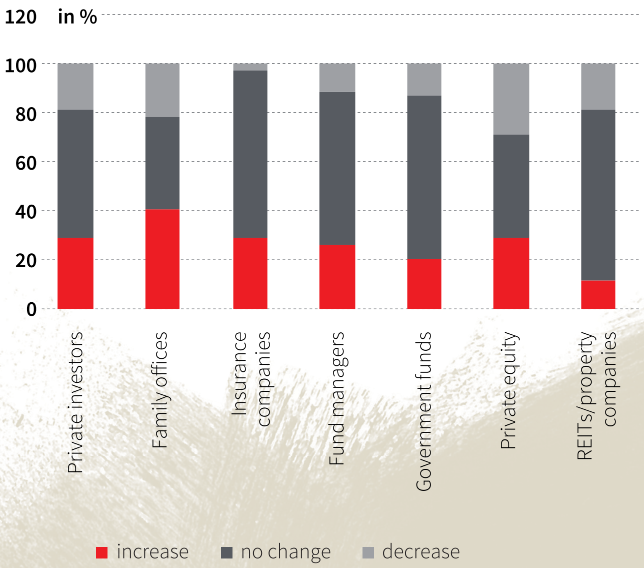
The assessment of the refinancing situation relating to real estate stocks fell by around 30 points. This downturn was not offset by the slight increase in the even more pessimistic expectations. The negative position in terms of expectations has only been apparent since the 4th quarter of 2016, in other words since the Brexit referendum. In hindsight, the actual situation has tended to be significantly more positive than expected. However, this is no longer the case since the 4th quarter of 2018 (-19.3 points) due to the imminent exit of the UK from the EU and the resulting uncertainties. The expectations relating to the real estate stock market sub-aggregate of -47.6 points in the current survey is almost a new record low (-50 points from the 4th quarter of 2011).

German property remains in high demand

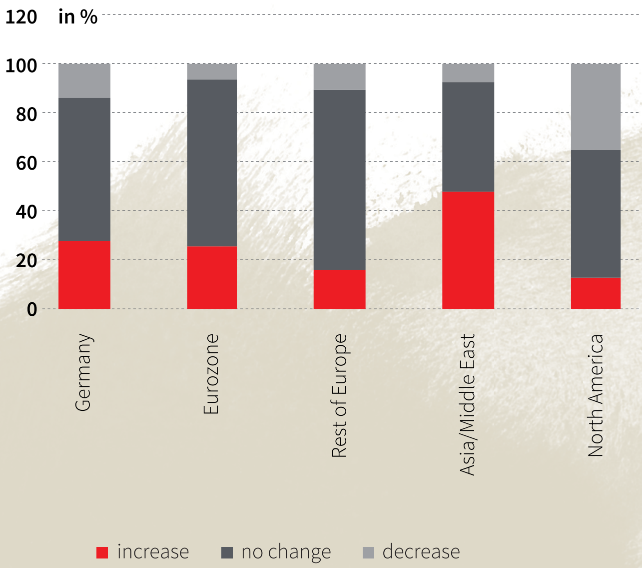
There will be increased demand for German properties from family offices and Asian and Middle Eastern investors over the next 12 months. This is the principal conclusion of the special question which we asked our expert panel in the current quarter. With scores of between 37% and 69%, the respondents expected no change in demand amongst the various investor groups; nonetheless, the overall view is that demand is expected to increase rather than decrease. 41% of the respondents expected a further increase in demand from family offices in the German real estate market. There is a totally different picture when it comes to REITs and property companies: here, experts anticipate that there is more likely to be decreased demand (19%) rather than increased demand (12%) over the next 12 months.

German real estate is particularly popular with investors from Asia and the Middle East: almost half (48%) of respondents expected increased investment activity in the German property market from these regions, and just 8% expect investment to decrease. The reverse is true of North American investors. 36% of respondents expected demand to fall from this group, while almost half expected no change. The experts' forecasts are highly convergent when it comes to German, Eurozone and other European investors: 23% expected increased demand from these regions, 67% expected demand to remain the same and 11% expected demand to fall. Overall, German real estate will remain in high demand as an investment over the next 12 months.

How will demand in the German real estate market develop amongst the following investor groups over the next 12 months?



How will demand in the German real estate market develop amongst investors from the following regions over the next 12 months?



Source: JLL and ZEW

DIFI-Report: Results of Responses, 1st Quarter 2019

	improved	Δ Q4	unchanged	Δ Q4	deteriorated	Δ Q4	aggregate	Δ Q4
German Real Estate Finance Index	**5.7**	**(- 4.7)**	**79.1**	**(+10.2)**	**15.3**	**(- 5.5)**	**-9.7**	**(+ 0.7)**
Financing situation	**improved**	**Δ Q4**	**unchanged**	**Δ Q4**	**deteriorated**	**Δ Q4**	**aggregate**	**Δ Q4**
Office	13.8	(- 3.8)	82.8	(+ 6.3)	3.4	(- 2.5)	10.4	(- 1.3)
Retail	3.5	(+ 3.5)	53.6	(+ 5.1)	42.9	(- 8.6)	-39.4	(+12.1)
Logistics	13.8	(-12.7)	82.8	(+15.2)	3.4	(- 2.5)	10.4	(-10.2)
Residential	3.5	(-11.2)	92.9	(+13.5)	3.6	(- 2.3)	-0.1	(- 8.9)
Hotel	11.1	(-10.1)	85.2	(+21.6)	3.7	(-11.5)	7.4	(+ 1.4)
All real estate segments	**9.1**	**(- 1.4)**	**79.5**	**(- 4.7)**	**11.4**	**(+ 6.1)**	**-2.3**	**(- 7.5)**
Financing expectations	**improve**	**Δ Q4**	**remain unchanged**	**Δ Q4**	**deteriorate**	**Δ Q4**	**aggregate**	**Δ Q4**
Office	0.0	(- 3.0)	82.8	(- 5.4)	17.2	(+ 8.4)	-17.2	(-11.4)
Retail	0.0	(+/- 0.0)	50.0	(+ 7.6)	50.0	(- 7.6)	-50.0	(+ 7.6)
Logistics	0.0	(- 8.8)	86.2	(+ 9.7)	13.8	(- 0.9)	-13.8	(- 7.9)
Residential	3.5	(- 5.5)	92.9	(+17.1)	3.6	(-11.6)	-0.1	(+ 6.1)
Hotel	7.4	(+ 4.5)	81.5	(+10.9)	11.1	(-15.4)	-3.7	(+19.9)
All real estate segments	**2.2**	**(- 0.1)**	**78.7**	**(- 2.7)**	**19.1**	**(+ 2.8)**	**-17.0**	**(- 2.8)**

Refinance market situation	improved	Δ Q4	unchanged	Δ Q4	deteriorated	Δ Q4	aggregate	Δ Q4
Capital deposits	12.5	(+ 5.6)	83.3	(+ 0.5)	4.2	(- 6.1)	8.3	(+11.7)
Mortgage bonds	26.9	(+16.9)	57.7	(-22.3)	15.4	(+ 5.4)	11.5	(+11.5)
Unsecured bonds	12.5	(+ 5.4)	70.8	(- 4.2)	16.7	(- 1.2)	-4.2	(+ 6.6)
Mortgage backed securities	5.2	(- 6.8)	89.5	(+13.5)	5.3	(- 6.7)	-0.1	(- 0.1)
Real estate stock markets	0.0	(-11.5)	52.4	(- 5.3)	47.6	(+16.8)	-47.6	(-28.3)
Refinance market expectations	**improve**	**Δ Q4**	**remain unchanged**	**Δ Q4**	**deteriorate**	**Δ Q4**	**aggregate**	**Δ Q4**
Capital deposits	19.0	(+11.9)	76.2	(+ 1.2)	4.8	(-13.1)	14.2	(+25.0)
Mortgage bonds	12.0	(+ 5.1)	76.0	(+13.9)	12.0	(-19.0)	0.0	(+24.1)
Unsecured bonds	0.0	(- 3.7)	69.6	(+14.0)	30.4	(-10.3)	-30.4	(+ 6.6)
Mortgage backed securities	5.5	(- 6.0)	66.7	(+16.7)	27.8	(-10.7)	-22.3	(+ 4.7)
Real estate stock markets	0.0	(- 7.4)	60.0	(+19.3)	40.0	(-11.9)	-40.0	(+ 4.5)
Spreads compared to German government bonds	**increase**	**Δ Q4**	**remain unchanged**	**Δ Q4**	**decrease**	**Δ Q4**	**aggregate**	**Δ Q4**
Mortgage bonds	48.0	(+ 6.8)	44.0	(- 8.9)	8.0	(+ 2.1)	40.0	(+ 4.7)
Unsecured bank bonds	66.7	(+14.9)	33.3	(-11.5)	0.0	(- 3.4)	66.7	(+18.3)
Segment development	**increase**	**Δ Q4**	**remain unchanged**	**Δ Q4**	**decrease**	**Δ Q4**	**aggregate**	**Δ Q4**
Syndication business (volume)	48.2	(+ 5.3)	44.4	(- 2.0)	7.4	(- 3.3)	40.8	(+ 8.6)
Underwriting (volume)	29.7	(+ 5.5)	44.4	(-14.2)	25.9	(+ 8.7)	3.8	(- 3.2)

Comment: The German Real Estate Finance Index survey was carried out between 21.01.2019 – 05.02.2019 and involved 29 experts. These experts were asked for their assessments of the market situation (preceding six months) and market expectations (coming six months). The results shown are the percentages of the response categories and the changes in per cent compared to the previous quarter (Δ previous quarter). The aggregates are calculated from the difference between the positive and negative response categories (such as 'improved' and 'deteriorated'). DIFI is calculated as an unweighted average from the aggregates of the financing situation and financing expectations for all use types.

Source: JLL and ZEW

Contacts JLL

Anke Herz
Team Leader Debt Advisory Germany
Frankfurt
+49 (0) 69 2003 1943
anke.herz@eu.jll.com
jll.de

Helge Scheunemann
Head of Research Germany
Hamburg
+49 (0) 40 350011 225
helge.scheunemann@eu.jll.com
jll.de

Contact ZEW

Dr. Carolin Schmidt
Department International Finance
and Financial Management
tel +49 (0) 621 1235 287
carolin.schmidt@zew.de
zew.de | zew.eu

Copyright © ZEW – LEIBNIZ-ZENTRUM FÜR EUROPÄISCHE WIRTSCHAFTSFORSCHUNG GmbH MANNHEIM and JONES LANG LASALLE SE, 2019.

No part of this publication may be reproduced or transmitted in any form or by any means without prior written consent of Jones Lang LaSalle SE and Zentrum für Europäische Wirtschaftsforschung. It is based on material that we believe to be reliable. Whilst every effort has been made to ensure its accuracy, we cannot offer any warranty that it contains no factual errors. We would like to be told of any such errors in order to correct them.