Research & Debt Advisory Germany
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DIFI-Report

Assessment of the Real Estate Financing Market

DIFI shows a slight fall

Considerable dynamism across the individual use types

Special question: The role ESG criteria are playing in the German real estate market

The German Real Estate Finance Index (DIFI) reflects survey participants' assessments of the current situation (the last six months) and expectations (the coming six months) for the German real estate financing market. DIFI is produced quarterly and is calculated on the basis of an average of the results for the real estate market segments office, retail, logistics, residential and hotel. 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 (Zentrum für Europäische Wirtschaftsforschung – Centre for European Economic Research) in Mannheim.

DIFI shows a slight fall

Slight falls in the situation and expectations indicators

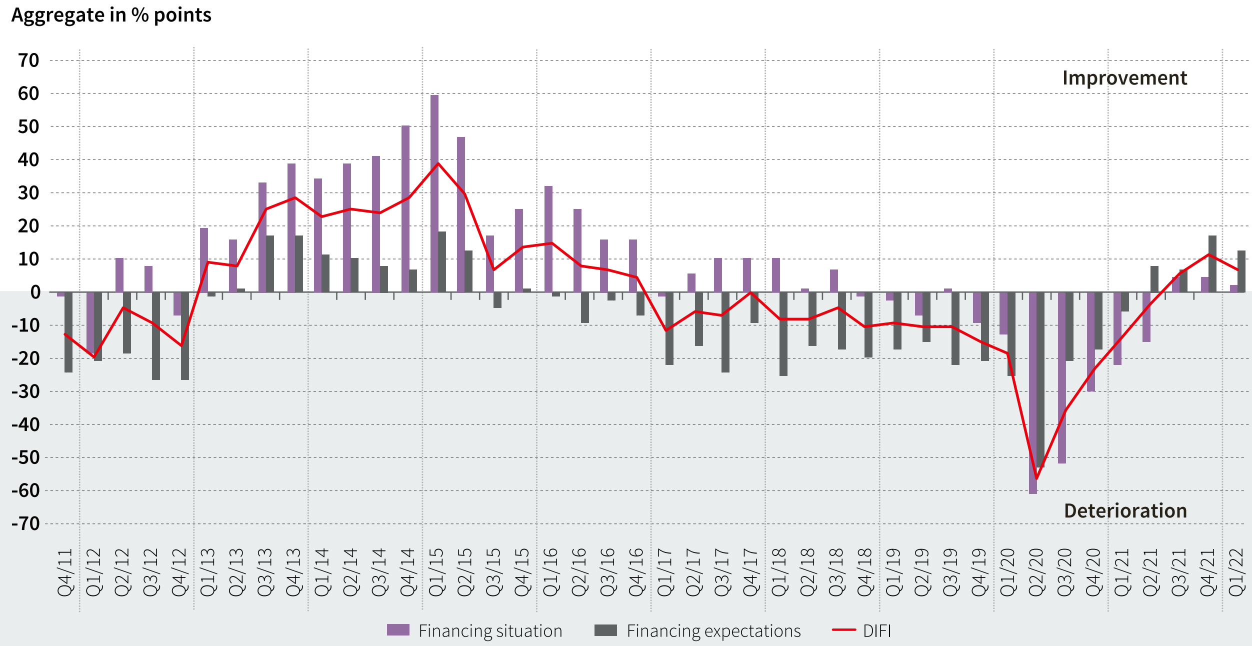
After six successive rises, the **German Real Estate Financing Index (DIFI)** fell slightly in the first quarter of 2022. At **7.2 points,** the indicator was 3.5 points lower than in the previous quarter; however, compared to the same quarter last year, the DIFI increased by 21.2 points. Both the experts' assessments of the financing situation over the last six months and the outlook for the financing situation over the next six months have deteriorated slightly. With a decline of 2.4 points compared to the final quarter of 2021, the situation indicator remained in positive territory at 1.6 points, while the expectations indicator fell by 4.6 points to 12.8 points.

Considerable dynamism across the individual use types

In the first quarter of 2022, the experts' assessments painted a picture of a very dynamic real estate financing market. The situation and expectations indicators within the individual use types showed different and partly contradictory changes compared to the previous quarter. Only the situation and expectations indicators for the office use type remained almost unchanged.

While the financing situation in the market for logistics real estate was assessed as worse overall than in the previous quarter, its outlook for the coming six months is improving. The corresponding situation and expectations indicators fell and rose by 20.8 and 14.2 points,

German Real Estate Finance Index (DIFI)



Average assessment of the current situation in and expectations for the five real estate market segments (Office, Retail, Logistics, Residential, Hotel).
Source: JLL and ZEW

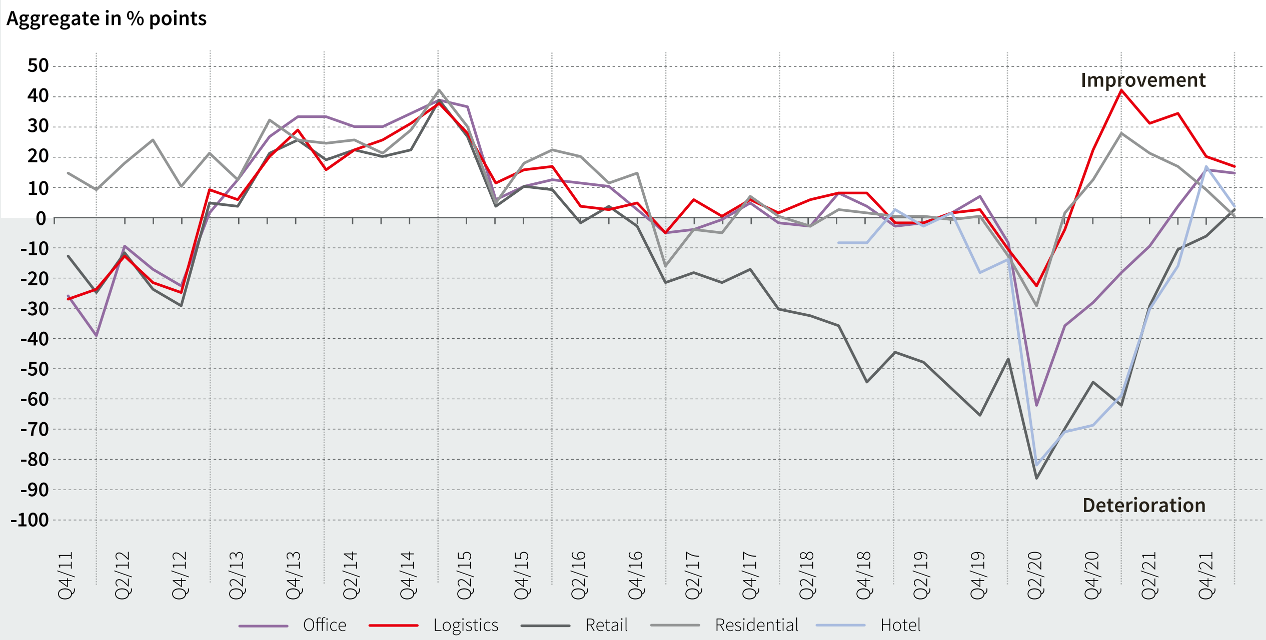
respectively. The reverse was true for the retail sector. While the corresponding situation indicator rose by 26.8 points to -5.0 points, the corresponding expectations indicator fell by 8.3 points to 10.0 points.

For the residential use type, the situation in the real estate financing markets in the first quarter of 2022 was assessed as significantly worse than in the previous quarter. The corresponding situation indicator fell by 18.2 points to a new aggregate of 0.0 points. Looking ahead to the next six months, the assessment of the residential use type is unchanged since the fourth quarter of 2021. The corresponding expectations indicator remained slightly negative at -0.1 points.

The situation indicators for the office (-3.8 points) and hotel (+3.8 points) use types were almost unchanged since the previous quarter. While in the case of office properties this also applied to the corresponding expectations indicator (+1.4 points), the outlook for the hotel use type was assessed as significantly worse than in the final quarter of 2021. The corresponding expectations indicator fell by 30.0 points to reach 25.0 points; despite this significant decline, the expectations indicator was at its second highest level since the third quarter of 2018.

Apart from the residential use type, all DIFI sub-indicators, which are formed as the arithmetic mean of situation and expectations indicators, were in positive territory in the first quarter of 2022. At 16.3 points, the DIFI sub-indi-

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

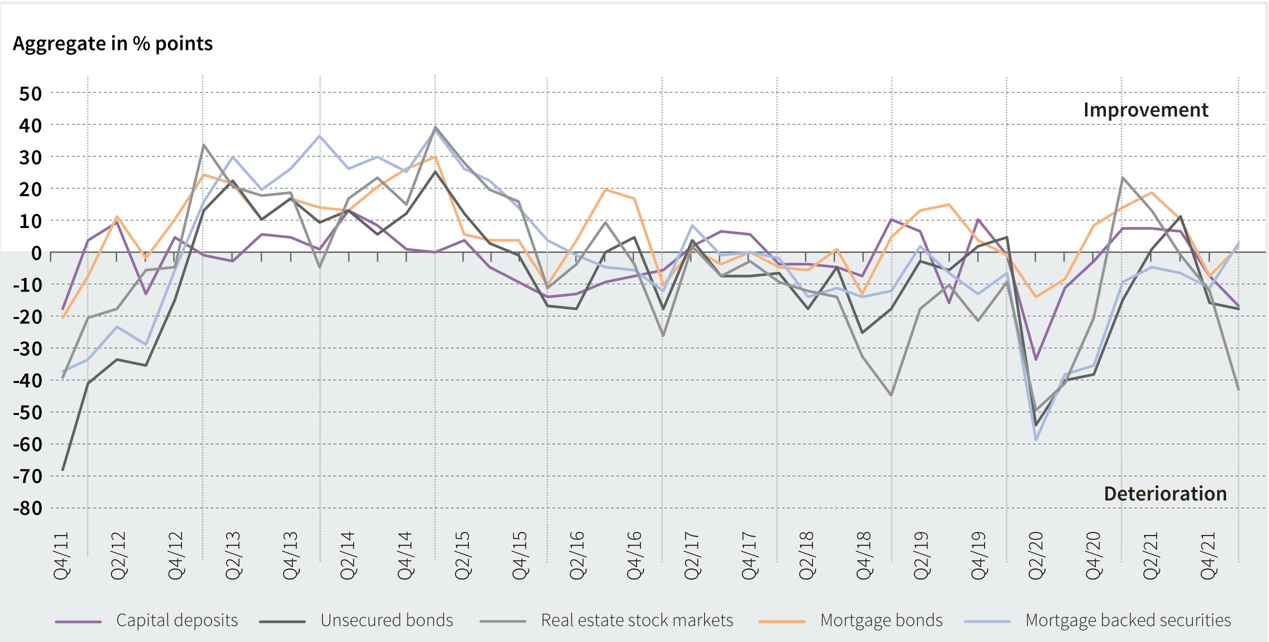
cator for the logistics use type remained the highest of all the use types considered. It is important to emphasise here that the survey was conducted well before the escalation of the Ukraine conflict. In the wake of the massive sanctions against Russia, it remains to be seen as to what extent these will also affect the business activities of the financing experts surveyed.

Situation and outlook in the refinancing markets mixed

In the first quarter of 2022, the situation and outlook in the refinancing markets was assessed as mixed overall. While capital deposits and real estate stocks and shares were assessed worse overall than in the previous quarter, Pfandbrief mortgage bonds and mortgage-backed securities were assessed better overall. Unsecured bonds were the only refinancing instrument for which the assessment of the situation and the outlook differed.

The situation for capital deposits and real estate stocks and shares in the refinancing markets deteriorated in the first quarter of 2022. The corresponding situation indicators fell by 5.6 points and 25.9 points to -18.9 points and -40.1 points, respectively. The corresponding expectations indicators were also lower than in the previous quarter. For capital deposits, the decline was 13.4 points, while for real estate stocks and shares, the decline was as high as 35.2 points. Following these declines, the respective expectations indicators stood at -13.4 points (capital deposits) and -42.9 points (real estate stocks and shares).

Development of the refinancing markets



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

The situation for Pfandbrief mortgage bonds and mortgage-backed securities improved relative to the previous quarter. The corresponding situation indicators rose by 12.5 points and 18.8 points to 0.0 points and 7.7 points, respectively, while the respective expectations indicators were also higher than in the final quarter of 2021, reaching 6.1 points (+6.1 points) and -0.1 points (+9.9 points), respectively.

While the situation in the refinancing market for unsecured bonds deteriorated since the previous quarter, its outlook improved. The corresponding situation indicator fell by 10.1 points to -33.3 points, while the corresponding expectations indicator rose by 7.8 points to lie in slightly positive territory at 0.1 points.

Overall, the refinancing market for mortgage-backed securities was rated best in the first quarter, while that for real estate shares was rated worst. At -42.9 points, the arithmetic mean of the situation and expectations indicators for real estate stocks and shares reached a similar level to the third quarter of 2020. Unlike in that quarter, however, the poor assessment for real estate stocks and shares is likely to be due to the inflation and interest rate outlooks for Germany.

The role ESG criteria are playing in the German real estate market

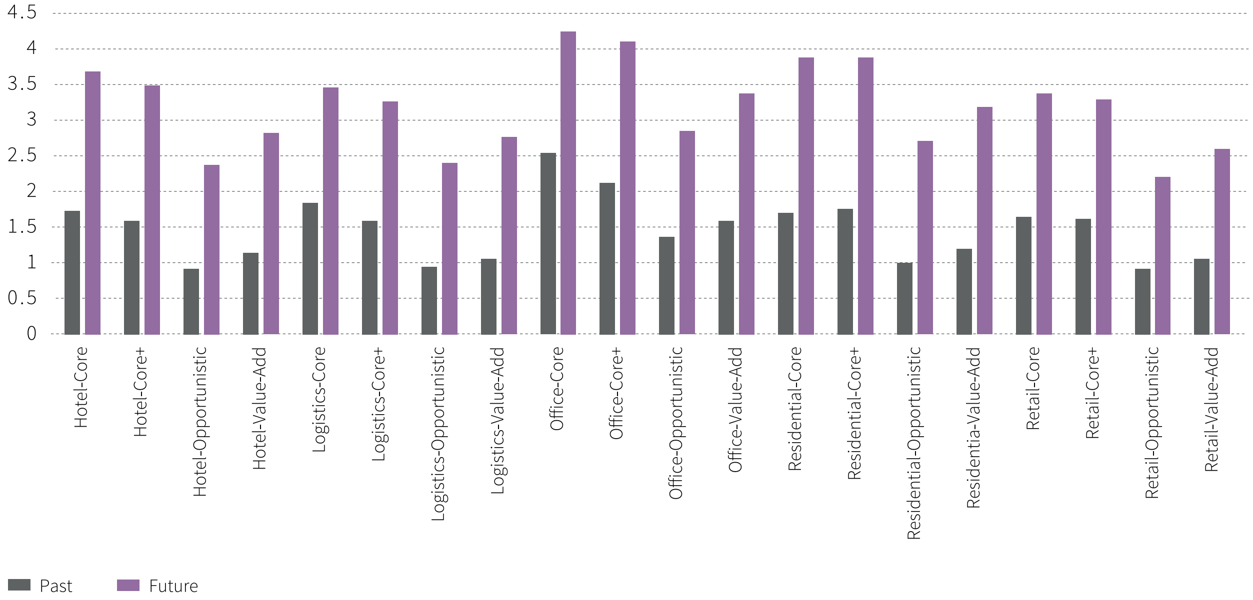
Sustainability is playing an increasingly important role in the financial markets. With a series of special questions in the first quarter of 2022, we wanted to take a closer look at the importance of sustainability in the German real estate market and how this may affect financing structures and their pricing. We therefore asked our experts for their assessments of ESG (sustainability) certifications.

While ESG certifications have played a very minor to minor role in the German real estate market in the past, according to the respondents' assessments, their importance is expected to increase across all use types and segments in the future. Previously, ESG certifications played the greatest role for office properties, especially in the Core and Core+ segments, and the most insignificant role for the retail use type. ESG certifications are also expected to continue to play the greatest role for office properties and the most insignificant role for retail properties in the future. The strongest increases in importance are expected in the residential and hotel use types. The respondents see the most significant increase in the importance of ESG certifications in the residential opportunistic segment. The S (Social) in ESG is also gaining in importance in certifications, which will manifest itself primarily in residential real estate.

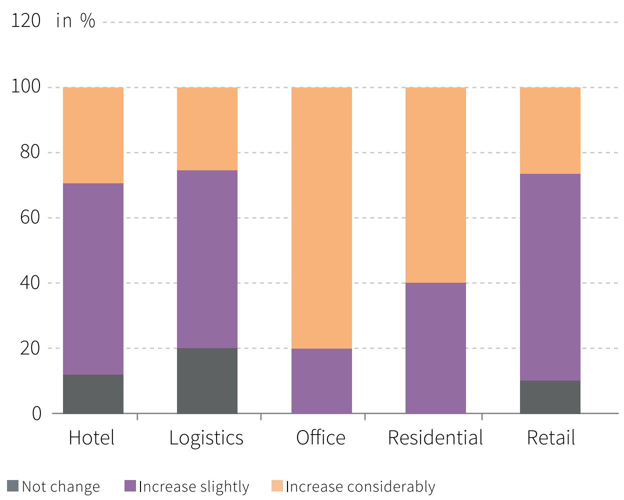
In line with the substantial role that respondents see ESG certifications playing in office properties, a considerable majority (80%) also expect investments that raise the sustainability standards of office properties to increase strongly in the future. The remaining 20% expect a slight increase. In the case of residential real estate, too, all experts assume that such investments will increase, with a clear majority expecting a strong increase here as well. For hotel, logistics and retail properties, the majority of experts also anticipate increases, although most believe that investments will increase only slightly.

In the previous special question, the experts were asked for their assessment of the BREEAM, DGNB, ECORE and LEED sustainability standards. All four standards were rated either positively or very positively by the majority of respondents. BREEAM received the best overall assessment (38% very positive and 62% positive), closely followed by DGNB (36% very positive and 64% positive). There was less consensus amongst the experts in the case of ECORE and LEED. While 46% and 43% (respectively) rated ECORE and LEED very positively, more than was the case with BREEAM and DGNB, 31% and 7% (respectively) rated them as only neutral. The remaining 23% and 50% (respectively) delivered a slightly positive assessment.

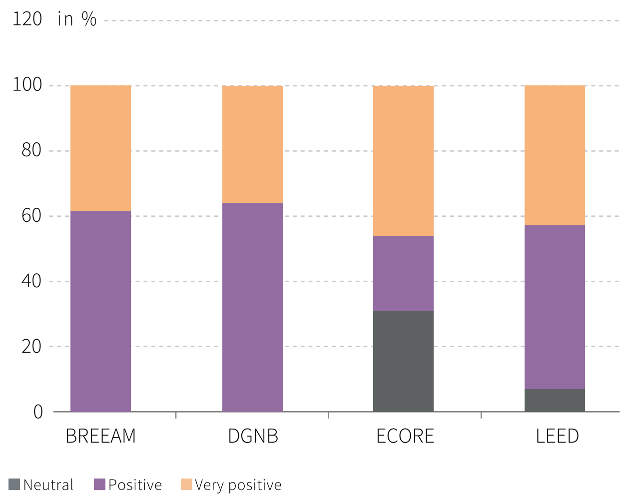
The importance of ESG certification in the German real estate market



In future, the importance of investments in existing properties that raise the sustainability standards of the property will ...



Assessment of ESG criteria



Source: JLL and ZEW

DIFI-Report: Results of Responses, 1st Quarter 2022

	Improved	Δ Q4	Unchanged	Δ Q4	Deteriorated	Δ Q4	Aggregate	Δ Q4
German Real Estate Finance Index	24.0	(+ 1.3)	59.3	(- 6.2)	16.8	(+ 4.8)	7.2	(- 3.5)
Financing situation	**Improved**	**Δ Q4**	**Unchanged**	**Δ Q4**	**Deteriorated**	**Δ Q4**	**Aggregate**	**Δ Q4**
Office	22.7	(+ 5,3)	68.2	(-14,4)	9.1	(+ 9,1)	13.6	(- 3,8)
Retail	20.0	(+10,9)	55.0	(+ 5,0)	25.0	(-15,9)	-5.0	(+26,8)
Logistics	22.8	(-16,3)	72.7	(+11,8)	4.5	(+ 4,5)	18.3	(-20,8)
Residential	15.0	(- 3,2)	70.0	(-11,8)	15.0	(+15,0)	0.0	(-18,2)
Hotel	14.3	(+ 0,7)	52.4	(+ 2,4)	33.3	(- 3,1)	-19.0	(+ 3,8)
All real estate segments	19.0	(- 0,5)	63.7	(- 1,4)	17.4	(+ 1,9)	1.6	(- 2,4)
Financing expectations	**Will improve**	**Δ Q4**	**Will not change**	**Δ Q4**	**Will deteriorate**	**Δ Q4**	**Aggregate**	**Δ Q4**
Office	25.0	(+ 2,3)	65.0	(- 3,2)	10.0	(+ 0,9)	15.0	(+ 1,4)
Retail	30.0	(- 1,9)	50.0	(- 4,5)	20.0	(+ 6,4)	10.0	(- 8,3)
Logistics	23.8	(+19,2)	66.7	(-24,2)	9.5	(+ 5,0)	14.3	(+14,2)
Residential	21.0	(+16,3)	57.9	(-32,6)	21.1	(+16,3)	-0.1	(+/- 0,0)
Hotel	45.0	(-20,0)	35.0	(+10,0)	20.0	(+10,0)	25.0	(-30,0)
All real estate segments	29.0	(+ 3,2)	54.9	(-10,9)	16.1	(+ 7,7)	12.8	(- 4,6)
Situation in the refinancing markets	**Improved**	**Δ Q4**	**Unchanged**	**Δ Q4**	**Deteriorated**	**Δ Q4**	**Aggregate**	**Δ Q4**
Capital deposits	-0.1	(- 0,1)	81.3	(- 5,4)	18.8	(+ 5,5)	-18.9	(- 5,6)
Pfandbrief mortgage bonds	5.9	(+ 5,9)	88.2	(+ 0,7)	5.9	(- 6,6)	0.0	(+12,5)
Unsecured bonds	6.7	(- 8,6)	53.3	(+ 7,1)	40.0	(+ 1,5)	-33.3	(-10,1)
Mortgage-backed securities	23.1	(+23,1)	61.5	(-27,4)	15.4	(+ 4,3)	7.7	(+18,8)
Real estate stocks and shares	6.6	(- 0,6)	46.7	(-24,7)	46.7	(+25,3)	-40.1	(-25,9)
Expectations in the refinancing markets	**Will improve**	**Δ Q4**	**Will not change**	**Δ Q4**	**Will deteriorate**	**Δ Q4**	**Aggregate**	**Δ Q4**
Capital deposits	13.3	(+13,3)	60.0	(-40,0)	26.7	(+26,7)	-13.4	(-13,4)
Pfandbrief mortgage bonds	12.4	(+12,4)	81.3	(-18,7)	6.3	(+ 6,3)	6.1	(+ 6,1)
Unsecured bonds	7.2	(- 0,5)	85.7	(+ 8,8)	7.1	(- 8,3)	0.1	(+ 7,8)
Mortgage-backed securities	16.6	(+ 6,6)	66.7	(- 3,3)	16.7	(- 3,3)	-0.1	(+ 9,9)
Real estate stocks and shares	7.1	(+ 7,1)	42.9	(-49,4)	50.0	(+42,3)	-42.9	(-35,2)
Spreads compared to German Government bonds	**Will increase**	**Δ Q4**	**Will not change**	**Δ Q4**	**Will reduce**	**Δ Q4**	**Aggregate**	**Δ Q4**
Pfandbrief mortgage bonds	56.2	(+37,2)	43.8	(-32,4)	0.0	(- 4,8)	56.2	(+42,0)
Unsecured bank bonds	81.2	(+43,1)	12.5	(-49,4)	6.3	(+ 6,3)	74.9	(+36,8)
Development of segments	**Will increase**	**Δ Q4**	**Will not change**	**Δ Q4**	**Will reduce**	**Δ Q4**	**Aggregate**	**Δ Q4**
Syndication business (volume)	55.0	(+ 5,0)	40.0	(+/- 0,0)	5.0	(- 5,0)	50.0	(+10,0)
Underwriting (volume)	35.0	(+10,0)	55.0	(-10,0)	10.0	(+/- 0,0)	25.0	(+10,0)

Comment: The German Real Estate Finance Index survey was carried out between 07.02.2022 – 14.02.2022 and involved 23 experts. These experts were asked for their assess-ments 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

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