Research & Debt Advisory Germany
Q2 | June 2021

# DIFI-Report

## Assessment of the Real Estate Financing Market

Fourth successive rise in DIFI

Mixed outlook for the real estate refinancing markets

Special question: lenders remain cautious in terms of hotel and retail properties

*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.*

# Fourth successive rise in DIFI

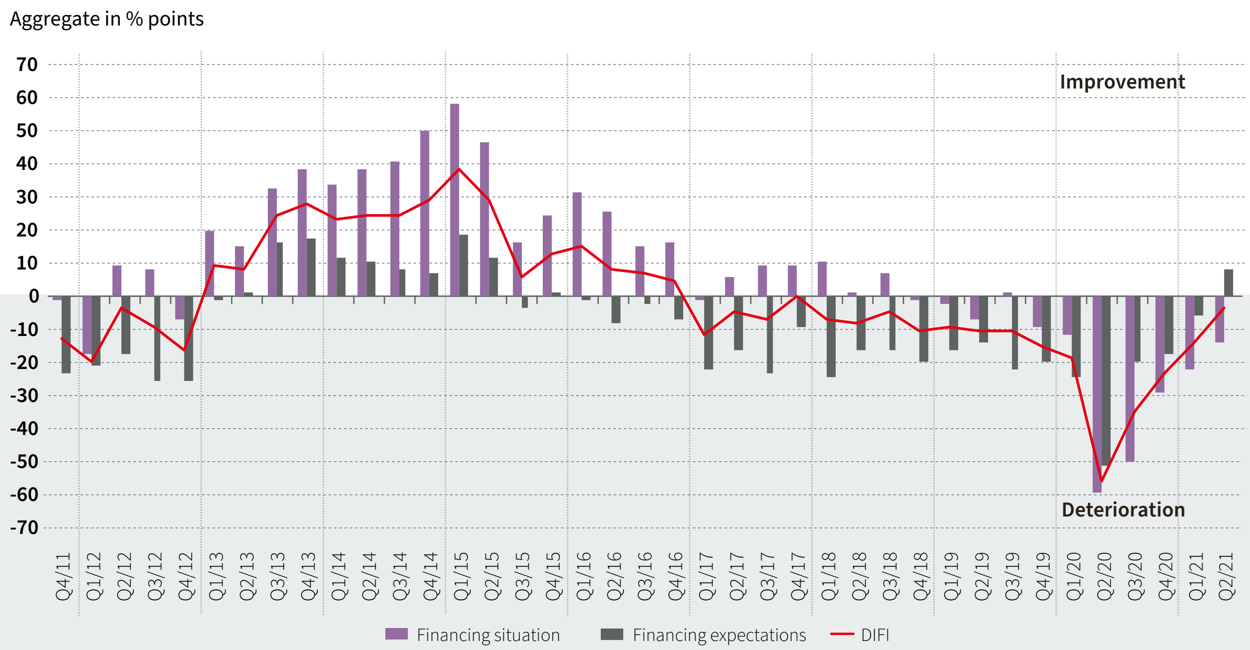
**Financing indicator back in positive territory**

The **German Real Estate Financing Index (DIFI)** rose by 10.7 points in the 2nd quarter of 2021 to its current level of **-3.3 points**. This is the fourth successive rise. Both the experts' assessments of the current financing situation over the last six months and their expectations for the financing situation over the next six months are more positive than they were in the 1st quarter of 2021. Whilst the situation indicator remains in the negative range at -14.8 points despite a rise of 7.4 points, the expectation indicator rose by 13.9 and is now in positive territory. The expectation indicator score of 8.2 points is its highest level since the 4th quarter of 2015 and is considerably above the level of before the onset of the COVID-19 crisis.

**Strong recovery amongst pandemic losers**

In the 2nd quarter of 2021, the experts are again more optimistic about the office, retail and hotel real estate segments, which is likely to be down to the good progress with the vaccination programme. The respondents' assessments for the three segments have improved significantly since the last survey in terms of the current financing situation, but particularly in terms of the financing expectations. The respective current situation indicators rose by 10.9 points (office), 19.0 points

**German Real Estate Finance Index (DIFI)**

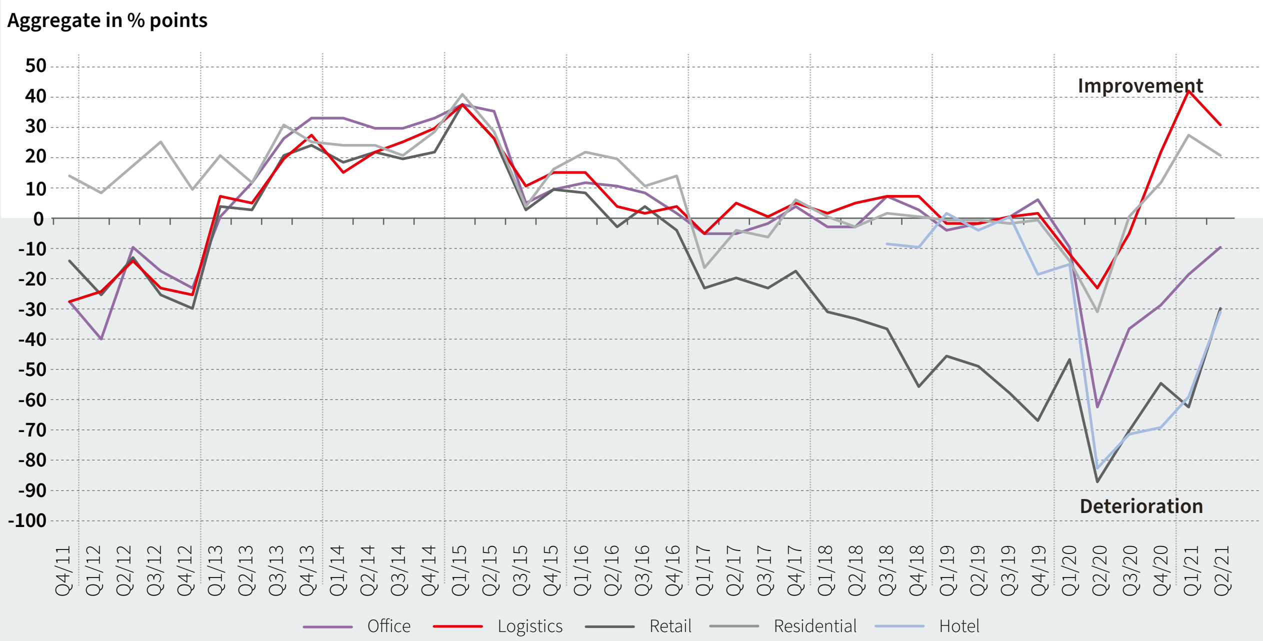



Average assessment of the current situation in and expectations for the five real estate market segments (Office, Retail, Logistics, Residential, Hotel).
Source: JLL and ZEW

(retail) and 15.8 points (hotel), whereby the assessment of the financing situation for the office segment (-26.2 points) is currently the most optimistic of the three use types. The expectation indicators for the retail and hotel segments showed significant improvements compared to the last survey, with rises of 45.8 points and 41.8 points, respectively. Looking at both the current situation and outlook together, the real estate financing market for offices in the 2nd quarter of 2021 is viewed in a similar way to the last survey prior to the onset of the COVID-19 crisis (Q1 2020), whilst the retail and hotel segments are assessed as better and worse, respectively.

The experts' assessments show that, compared to the last few quarters, the logistics and residential segments are no longer benefiting to the same extent from the current circumstances. After three successive hikes, the current situation indicator (-9.7 points) and the expectation indicator (-12.5 points) for the logistics segment in the 2nd quarter fell compared to the previous quarter. Whilst the current situation indicator for residential was almost unchanged, the expectation indicator fell from 21.9 points (Q1 2021) to 8.5 points (Q2 2021). Despite the downturns, the real estate financing markets for both real estate segments remained very attractive according to the respondents. The DIFI sub-indicators for the logistics and residential segments (31.1 points and 21.4 points, respectively) were the only segments well into the positive range.

**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

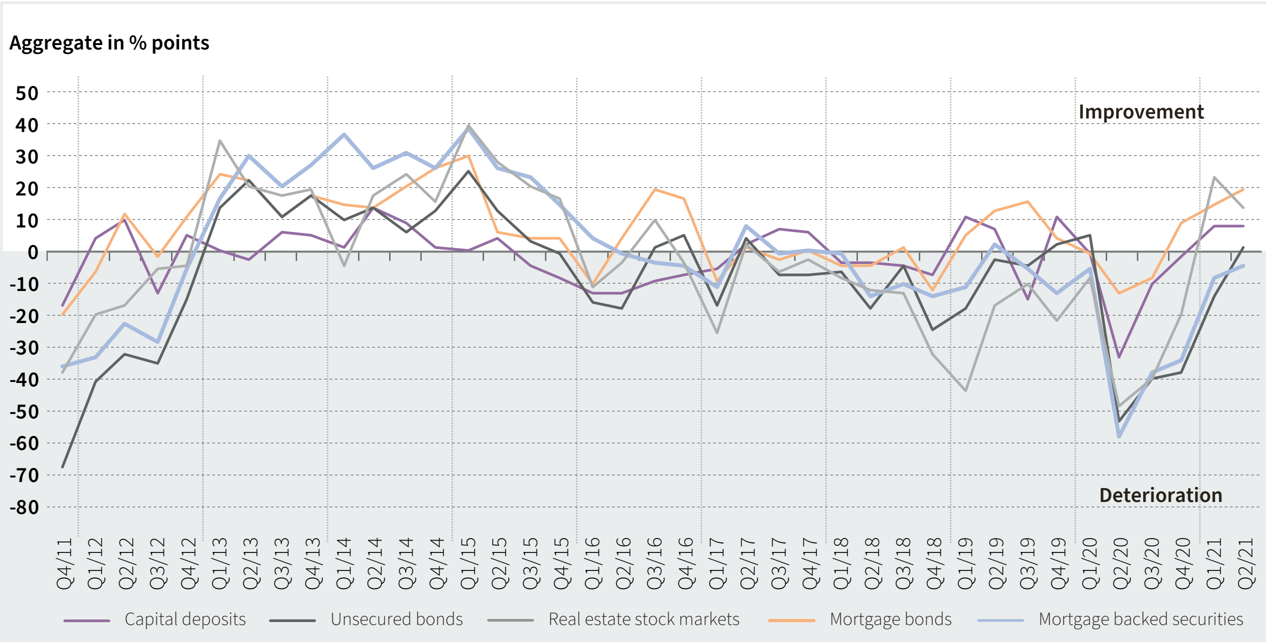
In our opinion, this downward movement could well be driven by the continued high price level for both use categories.

**Mixed outlook for the real estate refinancing markets**

Over the 2nd quarter of 2021, the overall situation in the refinancing markets is viewed more optimistically. With the exception of the indicator for real estate stocks, all other current situation indicators rose compared to the previous quarter. The biggest hike was for the mortgage bonds refinancing instrument (+13.8 points) and the weakest was for mortgage-backed securities (+1.4 points). With the exception of the indicator for mortgage-backed securities, all other situation indicators were in the positive range. The experts' most optimistic situation assessment is for the refinancing market for mortgage bonds. The indicator rose to 32.3 points over the 2nd quarter, which is its highest level since the 1st quarter of 2015.

The outlook for the real estate refinancing markets is again mixed over the 2nd quarter of 2021. Whilst the expectation indicators for capital deposits (-0.1 points) and mortgage-backed securities (-4.3 points) showed slightly negative balances, mortgage bonds (6.7 points), unsecured bonds (0.1 points) and real estate stocks (12 points) were slightly positive. With a rise of 28.1 points, the most significant change compared to the previous quarter was in the expectation indicator for unsecured bonds. Even the indicator for mort-

**Development of the refinancing markets**




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

gage-backed securities had improved since the last quarter. The outlook for the other refinancing instruments was more pessimistic in the 2nd quarter of 2021 than in the previous quarter. Looking at the current situation and expectations together, the experts are most optimistic about the development of the market for mortgage bonds over the 2nd quarter of 2021 and are least positive about the market for mortgage-backed securities.

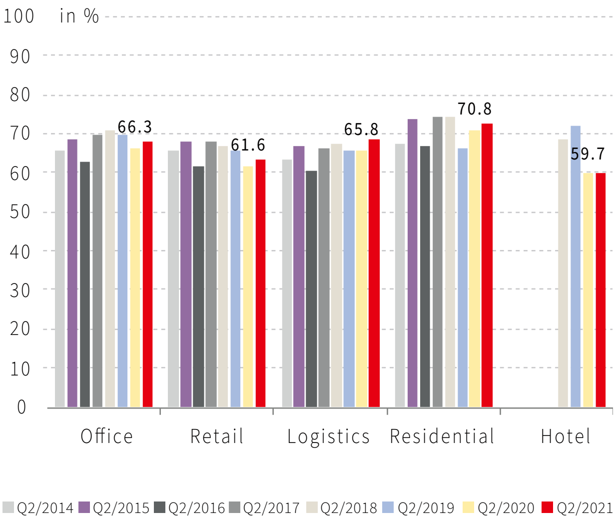
**Lenders remain cautious in terms of hotel and retail properties**

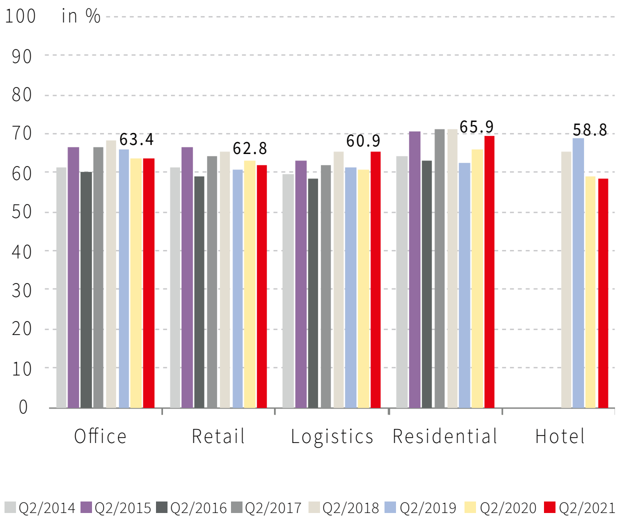
In order to paint a continuous picture, in the second quarter of the year the experts have been asked for their opinions on typical market margins and loan to value ratios (LTVs, debt financing based on market values) for property financing in the Core and Value-Add risk categories since 2014. The participants are able to select their most likely scenario from a prescribed set of ranges.

In terms of the typical market LTVs, there have been some divergent developments in both the Core and Value-Add risk categories over the 2nd quarter of 2021. Whilst the average LTVs for existing properties in the Core category have risen over the quarter for all real estate sectors in the survey, this is not the case in the retail and hotel segments in the Value-Add category. The relevant LTVs fell to 61.9% (retail) and 58.6% (hotel), which equate to 0.8% points and 0.2% points less than in the 2nd quarter of 2020, respectively. Given the highly positive developments in the real estate financing markets for logistics and residential properties, the LTVs for these use types in both risk categories registered their greatest increases compared to the same quarter of the previous year. The lenders are therefore financing the increased prices at disproportionate levels. The lowest average LTVs over the 2nd quarter of 2021, of under 60% in both risk categories, are in the hotel segment.

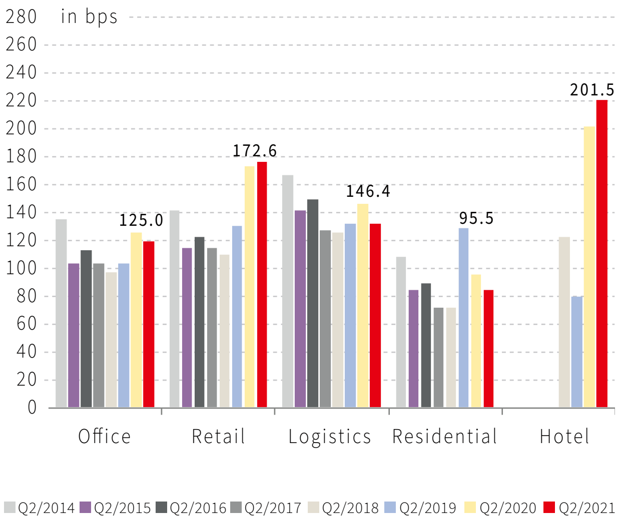
The investigation into the typical market margins for commercial real estate financing across the various real estate segments shows a mixed result. The average margins for office, logistics and residential properties fell in both risk categories (Core and Value-Add) compared to the same quarter of the previous year. This has been driven by the level of competition between the lenders. The average margins for hotel real estate financing rose across both categories in the current survey compared to the same quarter of the previous year, in part because market participants have temporarily withdrawn from the hotel segment. The development of the retail segment is different for the two risk categories, Core and Value-Add. Whilst the average assessment by the respondents in terms of the typical market margin in the Core category was higher compared to the same quarter of the previous year at 177 bps, this fell in the Value-Add category to just under 245 bps. The fall in margins in the Value-Add category appears unusual at first glance. We think that this may have something to do with both the foreseeable end of the COVID-19 pandemic and the pressure on lenders to invest. The overall view is that despite good progress with the vaccination programme, lenders remain cautious in terms of financing retail and hotel properties and are pricing the risk accordingly. The logistics and residential segments have actually benefited from the COVID-19 crisis, which is shown in the higher average LTVs and lower average margins compared to the same quarter of the previous year.

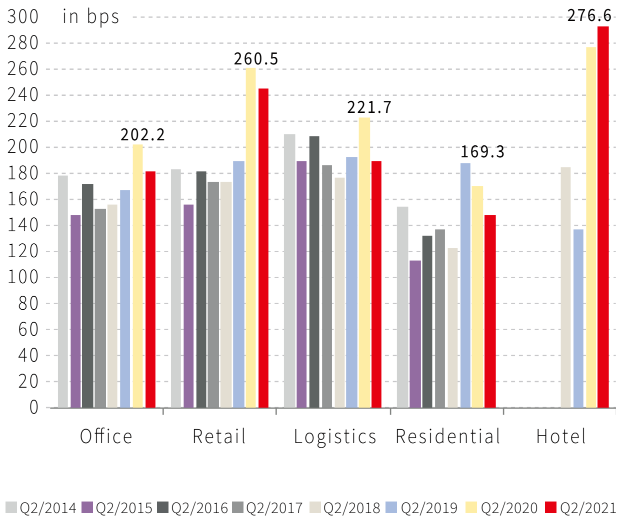
**Estimates of the average LTVs for commercial real estate financing of existing properties in the Core (left) and the Value-Add risk categories (right)**




**Estimates of the average margins for commercial real estate financing of existing properties in the Core (left) and the Value-Add risk categories (right)**




Source: JLL und ZEW

## DIFI-Report: Belegung der Antwortkategorien, 2. Quartal 2021

| | improved | Δ Q1 | unchanged | Δ Q1 | deteriorated | Δ Q1 | aggregate | Δ Q1 |
|---|---|---|---|---|---|---|---|---|
| **German Real Estate Finance Index** | 19.0 | (+ 2.0) | 58.7 | (+ 6.6) | 22.3 | (- 8.6) | -3.3 | (+ 10.7) |
| **Financing situation** | **improved** | **Δ Q1** | **unchanged** | **Δ Q1** | **deteriorated** | **Δ Q1** | **aggregate** | **Δ Q1** |
| Office | 2.7 | (- 0,2) | 68.4 | (+11,3) | 28.9 | (-11,1) | -26.2 | (+10,9) |
| Retail | 2.7 | (+ 2,7) | 37.8 | (+13,6) | 59.5 | (-16,3) | -56.8 | (+19,0) |
| Logistics | 45.9 | (- 7,0) | 51.4 | (+ 4,3) | 2.7 | (+ 2,7) | 43.2 | (- 9,7) |
| Residential | 34.3 | (+ 1,0) | 65.7 | (- 1,0) | 0.0 | (+/- 0,0) | 34.3 | (+ 1,0) |
| Hotel | 0.0 | (+/- 0,0) | 31.4 | (+15,8) | 68.6 | (-15,8) | -68.6 | (+15,8) |
| All real estate segments | 17.1 | (- 0,7) | 50.9 | (+ 8,8) | 31.9 | (- 8,1) | -14.8 | (+ 7,4) |
| **Financing expectations** | **improve** | **Δ Q1** | **remain unchanged** | **Δ Q1** | **deteriorate** | **Δ Q1** | **aggregate** | **Δ Q1** |
| Office | 21.0 | (+ 2,8) | 65.8 | (+ 2,2) | 13.2 | (- 5,0) | 7.8 | (+ 7,8) |
| Retail | 18.9 | (+18,9) | 59.5 | (+ 8,0) | 21.6 | (-26,9) | -2.7 | (+45,8) |
| Logistics | 21.6 | (- 9,8) | 75.7 | (+ 7,1) | 2.7 | (+ 2,7) | 18.9 | (-12,5) |
| Residential | 11.4 | (-10,5) | 85.7 | (+ 7,6) | 2.9 | (+ 2,9) | 8.5 | (-13,4) |
| Hotel | 31.4 | (+22,3) | 45.7 | (- 2,8) | 22.9 | (-19,5) | 8.5 | (+41,8) |
| All real estate segments | 20.9 | (+ 4,8) | 66.5 | (+ 4,4) | 12.7 | (- 9,1) | 8.2 | (+13,9) |
| **Refinance market situation** | **improved** | **Δ Q1** | **unchanged** | **Δ Q1** | **deteriorated** | **Δ Q1** | **aggregate** | **Δ Q1** |
| Capital deposits | 24.1 | (+11,6) | 69.0 | (-18,5) | 6.9 | (+ 6,9) | 17.2 | (+ 4,7) |
| Mortgage bonds | 32.3 | (+10,1) | 67.7 | (- 6,4) | 0.0 | (- 3,7) | 32.3 | (+13,8) |
| Unsecured bonds | 23.1 | (- 2,9) | 57.7 | (+ 9,6) | 19.2 | (- 6,7) | 3.9 | (+ 3,8) |
| Mortgage backed securities | 12.5 | (+ 1,4) | 70.8 | (- 1,4) | 16.7 | (+/- 0,0) | -4.2 | (+ 1,4) |
| Real estate stock markets | 23.1 | (-15,0) | 69.2 | (+16,8) | 7.7 | (- 1,8) | 15.4 | (-13,2) |
| **Refinance market expectations** | **improve** | **Δ Q1** | **remain unchanged** | **Δ Q1** | **deteriorate** | **Δ Q1** | **aggregate** | **Δ Q1** |
| Capital deposits | 3.5 | (- 0,7) | 92.9 | (- 2,9) | 3.6 | (+ 3,6) | -0.1 | (- 4,3) |
| Mortgage bonds | 6.7 | (- 4,4) | 93.3 | (+ 4,4) | 0.0 | (+/- 0,0) | 6.7 | (- 4,4) |
| Unsecured bonds | 11.6 | (+ 7,6) | 76.9 | (+12,9) | 11.5 | (-20,5) | 0.1 | (+28,1) |
| Mortgage backed securities | 0.0 | (-10,5) | 95.7 | (+27,3) | 4.3 | (-16,8) | -4.3 | (+ 6,3) |
| Real estate stock markets | 20.0 | (- 3,8) | 72.0 | (+ 0,6) | 8.0 | (+ 3,2) | 12.0 | (- 7,0) |
| **Segment development** | **increase** | **Δ Q1** | **remain unchanged** | **Δ Q1** | **decrease** | **Δ Q1** | **aggregate** | **Δ Q1** |
| Mortgage bonds | 15.1 | (+ 2,2) | 78.8 | (- 8,3) | 6.1 | (+ 6,1) | 9.0 | (- 3,9) |
| Unsecured bank bonds | 43.7 | (- 3,2) | 46.9 | (- 3,1) | 9.4 | (+ 6,3) | 34.3 | (- 9,5) |
| **Segment development** | **increase** | **Δ Q1** | **remain unchanged** | **Δ Q1** | **decrease** | **Δ Q1** | **aggregate** | **Δ Q1** |
| Syndication business (volume) | 61.1 | (+ 9,5) | 36.1 | (- 5,8) | 2.8 | (- 3,7) | 58.3 | (+13,2) |
| Underwriting (volume) | 27.8 | (+ 7,1) | 61.1 | (+ 9,4) | 11.1 | (-16,5) | 16.7 | (+23,6) |

Comment: The German Real Estate Finance Index survey was carried out between 03.05.2021 – 17.05.2021 and involved 38 experts. These experts were asked for their as-sess-ments of the market situation (preceding six months) and market expectations (coming six months). The results shown are the percentages of the response catego-ries 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 nega-tive 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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