Research & Debt Advisory Deutschland

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DIFI-Report

Assessment of the Real Estate Financing Market

Biggest drop in DIFI since the beginning of the Covid crisis

Significant deterioration in sentiment in the refinancing markets

Current LTVs and margins: financing conditions for residential real estate worsen once again

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.

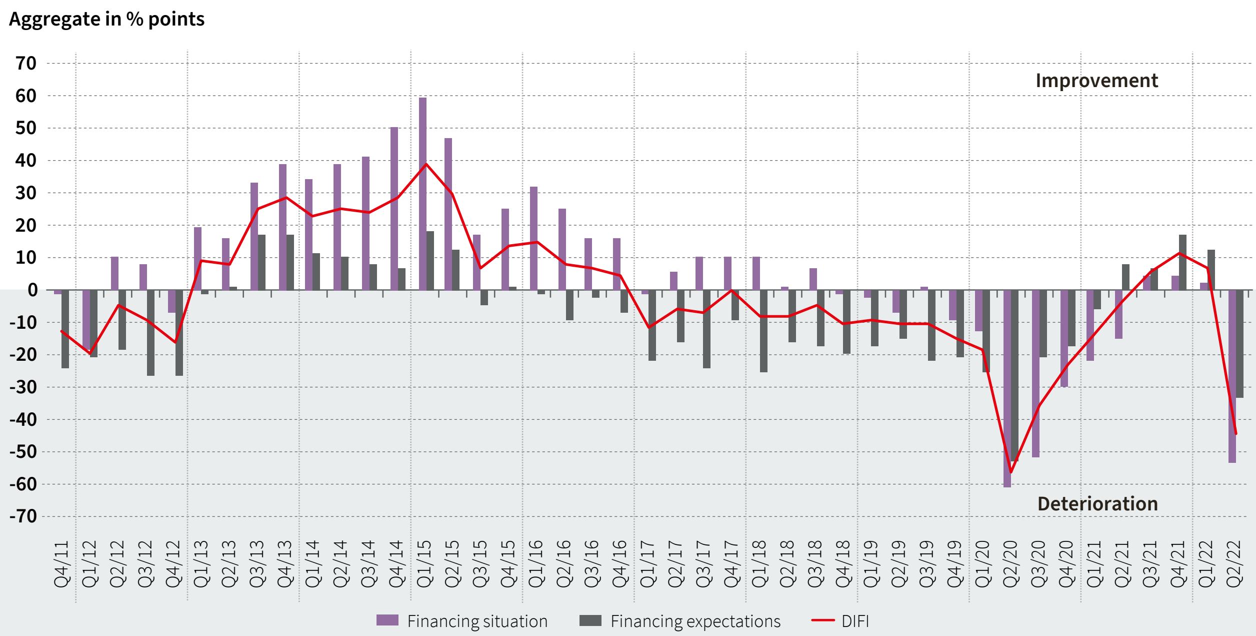
Biggest drop in DIFI since the beginning of the Covid crisis

Assessments of current situation and outlook for financing deteriorate significantly
There was a significant downturn in the **German Real Estate Finance Index (DIFI)** in the second quarter of 2022. At **-44.5 points**, the indicator is 51.7 points lower than in the previous quarter. The survey participants' assessments of both the financing situation in the past six months and the outlook for the financing situation in the coming six months have deteriorated significantly. The 55.0-point fall in the current situation indicator compared to the first quarter of 2022 was greater than the downturn in the expectations indicator, which fell by 48.3 points to -35.5 points.

Pessimism affects all use types
The assessments by the respondents of the current situation and outlook for financing for all use types under consideration significantly worsened between the first and second quarters of the year.

According to the survey participants, the financing situation deteriorated significantly across all use types in the second quarter. The aggregates of the positive and negative responses ranged from -66.7 points for residential to -44.0 points for logistics uses. All use types suffered significant losses, regardless of whether they still had a positive balance in the first quarter (such as office and logistics uses).

German Real Estate Finance Index (DIFI)



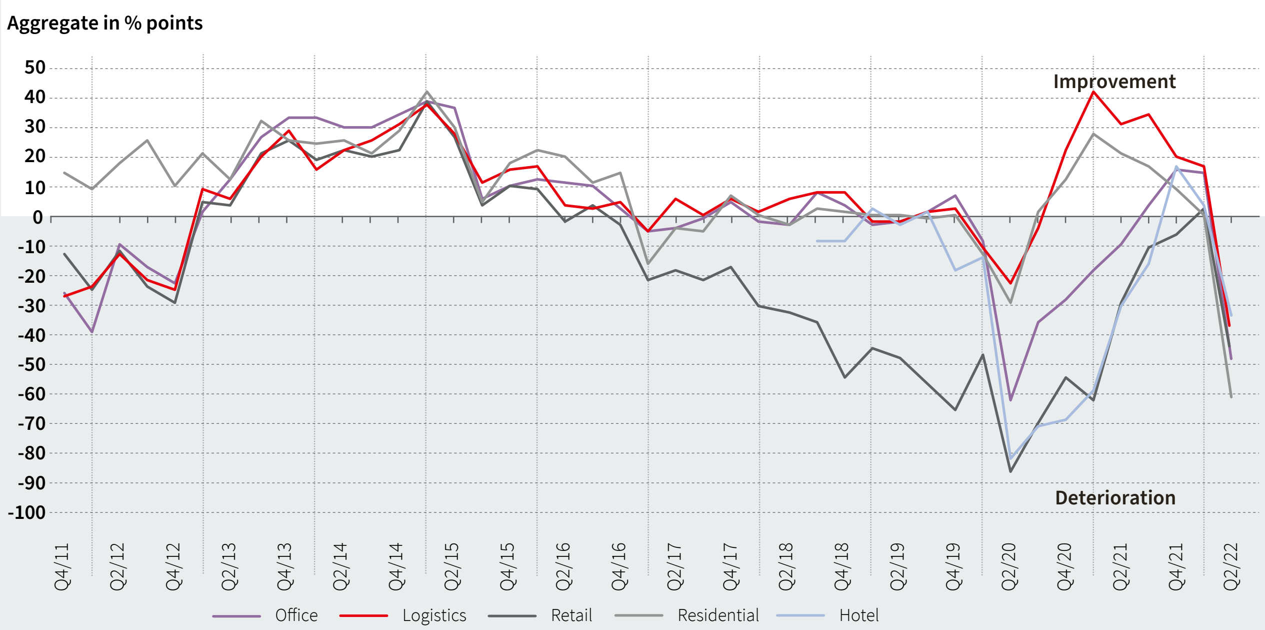
Average assessment of the current situation in and expectations for the five real estate market segments (Office, Retail, Logistics, Residential, Hotel).
Source: JLL and ZEW

The aggregate of financing expectations for all use types is also in negative territory. The changes since the first quarter of 2022 are stark, with the most marked decrease in the office use type. The corresponding indicator lost 60.8 points compared to the first quarter and now stands at -45.8 points, ten percentage points lower than the average value across all use types, while the decline for hotel use appears more moderate than the other use types, at 38.7 points.

Because of the declines, all DIFI sub-indicators, which represent the average values of the current situation and expectations indicators, were in negative territory in the second quarter. At -32.9 points, the DIFI sub-indicator for the hotel use type reached the highest level of all the use types considered. Nevertheless, the financing of hotel properties is currently particularly challenging. In terms of the index, this use type has been steadily losing ground since shifting into negative territory at the beginning of 2020 and has now reached a very low level. This contrasts with the situation with residential properties where, at -60.5 points, the corresponding indicator is by far at its lowest level. According to the survey participants, this use type has therefore experienced a very abrupt deterioration in financing conditions. Nonetheless, lenders and borrowers are still sounding each other out in this market segment and so a somewhat higher level can be attributed to the financing market for residential properties. The emergence of this trend was evident from the positive DIFI levels over the course of 2021.

The current survey is the first to be undertaken since the outbreak of the war in Ukraine. The negative assessments

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

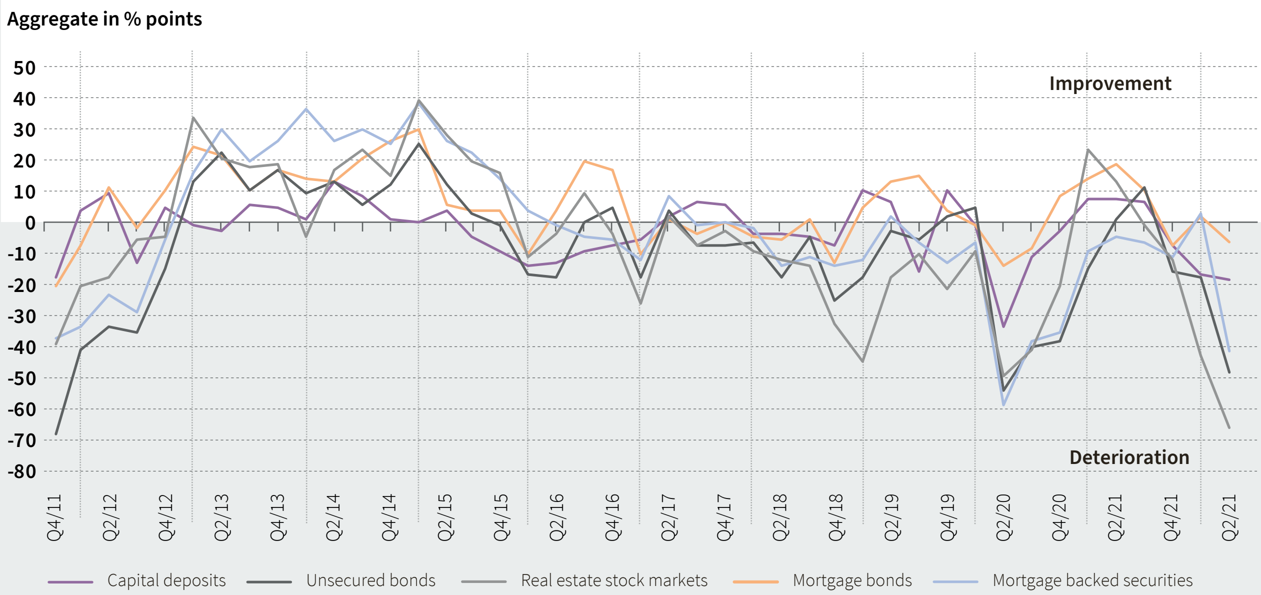
of the survey participants show their concern about the overall economic development in Germany which could also have an impact on the development of the real estate markets. Lending is also being burdened by the continued high price rises and the higher interest rate level. This particularly applies to high-risk exposures such as project developments.

Significant deterioration in sentiment in the refinancing markets

The assessments of the market for new real estate financing as well as the current situation and outlook in the refinancing markets were generally negative in the second quarter of 2022. With the exception of the expectations indicator for the capital deposits refinancing instrument, the current situation and expectations indicators of all refinancing instruments have deteriorated. The declines in the situation indicators range from 7.5 points (capital deposits) to 57.6 points (mortgage-backed securities). The situation for refinancing in the real estate equity markets is assessed as the worst of all the refinancing instruments considered in the second quarter. The corresponding current situation indicator has reached a new all-time low of -76.5 points, falling below its last all-time low of -65.2 points which it reached in the second quarter of 2020. At -10.6 points, the situation in the refinancing market for Pfandbrief mortgage bonds is currently the most optimistic in terms of the assessments.

The declines in the expectations indicators range from 11.3 points (Pfandbrief mortgage bonds) to 47.4 points

Development of the refinancing markets



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

(unsecured bonds). At 2.2 points, the market for capital deposits was the only market to experience an improvement in outlook between the first and second quarters of 2022. Looking at the next six months, the issuance of new shares as a refinancing instrument is rated the worst of all instruments considered. The corresponding indicator has fallen by 32.2 points to -75.1 points to reach an all-time low, even falling below its last all-time low of -44.5 points which it reached in the fourth quarter of 2018.

Overall, the refinancing market for Pfandbrief mortgage bonds is rated the highest and real estate stocks and shares are rated the worst. At -75.9 points, the average value of current situation and expectations indicators for real estate stocks and shares has reached a new all-time low. The corresponding figure for Pfandbrief mortgage bonds is -7.9 points.

Further deterioration in financing conditions for residential real estate

To gain a complete overview, since 2014 survey participants have been regularly asked to provide their assessments of typical margins and Loan-to-Value ratios (LTVs, leverage ratios based on market values) achieved in the market for real estate financing in the 'Core' and 'Value-Add' risk categories. They choose the most likely (in their opinion) from a predefined range of values.

In the second quarter of 2022, the assessment of typical market LTVs in the Core and Value-Add categories showed a very similar development compared to the final quarter of 2021, when the survey participants were last asked about typical market LTVs and margins: while the average LTVs for residential properties in the Core and Value-Add categories are lower, they increase for properties from the other segments compared to the final quarter of 2021. In the Core category, average LTVs are currently between around 60% (residential) and around 73% (logistics) and in the Value-Add category, between around 59% (residential) and around 69% (logistics). While average LTVs for logistic properties since data collection began in the second quarter of 2014 have never been higher than in the second quarter of 2022, they are currently at a new all-time low for residential properties.

According to the respondents' assessments, the typical market margins for the commercial financing of properties of various use types in the Core and Value-Add categories increased in the second quarter of 2022, with the exception of logistic properties in the Core category. The average margin for logistic properties in the Core category is unchanged compared to the fourth quarter of 2021. At around 18 bps, the highest increase in the average value in the Core category was in the residential use type. In the Value-Add category, the average increases range from around 3 bps (hotel) to around 30 bps (residential). Across both categories, the lowest margins are currently found in residential properties (around 112 bps and 162 bps in the Core and Value-Add categories, respectively), and the highest margins are in hotel properties (around 213 bps and 271 bps in the Core and Value-Add categories, respectively).

DIFI-Report: Results of Responses, 2nd Quarter 2022

	Improved	Δ Q1	Unchanged	Δ Q1	Deteriorated	Δ Q1	Aggregate	Δ Q1
German Real Estate Financing Index (DIFI)	5.3	(-18.7)	45.1	(-14.2)	49.7	(+32.9)	-44.5	(-51.7)
Financing situation	**Improved**	**Δ Q1**	**Unchanged**	**Δ Q1**	**Deteriorated**	**Δ Q1**	**Aggregate**	**Δ Q1**
Office	4.0	(-18,7)	40.0	(-28,2)	56.0	(+46,9)	-52.0	(-65,6)
Retail	0.0	(-20,0)	47.8	(- 7,2)	52.2	(+27,2)	-52.2	(-47,2)
Logistics	4.0	(-18,8)	48.0	(-24,7)	48.0	(+43,5)	-44.0	(-62,3)
Residential	0.0	(-15,0)	33.3	(-36,7)	66.7	(+51,7)	-66.7	(-66,7)
Hotel	13.1	(- 1,2)	21.7	(-30,7)	65.2	(+31,9)	-52.1	(-33,1)
All use types	4.2	(-14,8)	38.2	(-25,5)	57.6	(+40,2)	-53.4	(-55,0)
Financing expectations	**Will improve**	**Δ Q1**	**Will not change**	**Δ Q1**	**Will deteriorate**	**Δ Q1**	**Aggregate**	**Δ Q1**
Büro	0.0	(-25,0)	54.2	(-10,8)	45.8	(+35,8)	-45.8	(-60,8)
Einzelhandel	4.4	(-25,6)	56.5	(+ 6,5)	39.1	(+19,1)	-34.7	(-44,7)
Logistik	4.2	(-19,6)	62.5	(- 4,2)	33.3	(+23,8)	-29.1	(-43,4)
Wohnen	0.0	(-21,0)	45.8	(-12,1)	54.2	(+33,1)	-54.2	(-54,1)
Hotel	22.7	(-22,3)	40.9	(+ 5,9)	36.4	(+16,4)	-13.7	(-38,7)
All use types	6.3	(-22,7)	52.0	(- 2,9)	41.8	(+25,7)	-35.5	(-48,3)
Situation in the refinancing markets	**Improved**	**Δ Q1**	**Unchanged**	**Δ Q1**	**Deteriorated**	**Δ Q1**	**Aggregate**	**Δ Q1**
Capital deposits	5.2	(+ 5,3)	63.2	(-18,1)	31.6	(+12,8)	-26.4	(- 7,5)
Pfandbrief mortgage bonds	10.5	(+ 4,6)	68.4	(-19,8)	21.1	(+15,2)	-10.6	(-10,6)
Unsecured bonds	0.0	(- 6,7)	50.0	(- 3,3)	50.0	(+10,0)	-50.0	(-16,7)
Mortgage-backed securities	7.2	(-15,9)	35.7	(-25,8)	57.1	(+41,7)	-49.9	(-57,6)
Real estate stocks and shares	0.0	(- 6,6)	23.5	(-23,2)	76.5	(+29,8)	-76.5	(-36,4)
Expectations in the refinancing markets	**Will improve**	**Δ Q1**	**Will not change**	**Δ Q1**	**Will deteriorate**	**Δ Q1**	**Aggregate**	**Δ Q1**
Capital deposits	16.6	(+ 3,3)	55.6	(- 4,4)	27.8	(+ 1,1)	-11.2	(+ 2,2)
Pfandbrief mortgage bonds	5.3	(- 7,1)	84.2	(+ 2,9)	10.5	(+ 4,2)	-5.2	(-11,3)
Unsecured bonds	5.3	(- 1,9)	42.1	(-43,6)	52.6	(+45,5)	-47.3	(-47,4)
Mortgage-backed securities	8.3	(- 8,3)	50.0	(-16,7)	41.7	(+25,0)	-33.4	(-33,3)
Real estate stocks and shares	6.2	(- 0,9)	12.5	(-30,4)	81.3	(+31,3)	-75.1	(-32,2)
Spreads compared to German Government Bonds	**Will increase**	**Δ Q1**	**Will not change**	**Δ Q1**	**Will reduce**	**Δ Q1**	**Aggregate**	**Δ Q1**
Pfandbrief mortgage bonds	55.0	(- 1,2)	35.0	(- 8,8)	10.0	(+10,0)	45.0	(-11,2)
Unsecured bonds	90.4	(+ 9,2)	4.8	(- 7,7)	4.8	(- 1,5)	85.6	(+10,7)
Development of segments	**Will increase**	**Δ Q1**	**Will not change**	**Δ Q1**	**Will reduce**	**Δ Q1**	**Aggregate**	**Δ Q1**
Syndication business (volume)	36.3	(-18,7)	27.3	(-12,7)	36.4	(+31,4)	-0.1	(-50,1)
Underwriting (volume)	9.1	(-25,9)	27.3	(-27,7)	63.6	(+53,6)	-54.5	(-79,5)

Comment: The German Real Estate Finance Index survey was carried out between 09.5.2022 - 20.5.2022 and involved 23 experts. hese 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

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