The German housing market:

Supply and demand – today and tomorrow
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Structure of the housing market
Why this topic is so sensitive

- There are about 40 m housing units (and households) in Germany
- Residential buildings make up 48% of total German gross fixed assets of EUR 11.7 tr (2007)
- 42% of private households' gross assets are tied in real estate
- Per capita living space in west Germany amounts to 42.2 m² in 2006 (compared with 37 m² in 1990). In east Germany it is 38.9 m² today, up from 28 m² in 1990
- 70% of all housing units were built after WWII (in west Germany the share of older buildings is smaller than in east Germany)
- Almost 50% of all dwellings are in buildings with 1 or 2 units – no more than 10.5% are in buildings with more than 13 units
- At around 45% in west and 35% in east Germany, the home ownership ratio is clearly below the European average
Structure of housing stock in 2003

Housing stock in Germany (2003)
38,690,000 dwellings

Profesional suppliers
9,769,000 dwellings

- Municipal housing association
  2,744,000 dwellings

- Private-sector housing companies
  2,597,000 dwellings

- Cooperatives
  2,288,000 dwellings

- Public housing associations
  390,000 dwellings

- Churches
  137,000 dwellings

- Other suppliers*
  1,613,000 dwellings

Small private suppliers
13,791,000 dwellings

- Private small landlords
  10,386,000 dwellings

- Lodgers with owner-occupiers
  3,405,000 dwellings

Owner-occupiers
15,130,000 dwellings

- One- and two-family houses
  12,249,000 dwellings

- Multi-family dwellings
  2,881,000 dwellings

* Banks, insurance companies, real estate funds, other companies and non-profit organisations

Sources: GDW, Stat. BA
Since 2003 the housing market has undergone big changes
- Big transactions of housing portfolios, HU in ´000 -

- 2004 and 2005 were exceptional years
- The volumes of newly traded portfolios has been falling since 2004. In 2006 every second portfolio was a resale
- Overall, about 1.3 million housing units (HU) in approx. 150 transactions – in first and resales since 1999

Portfolios with at least 800 housing units only.
Who sold the units?
- HU in ´000 -

- 470,000 HU until 2003
- 810,000 HU from 2004 until 2006
- Municipalities are selling more (special effect WOBA Dresden)
- Federal/state level portfolios already relatively small GAGFAH transaction in 2004 (82,000 HU)
- Thyssen Krupp (48,000) and Viterra (138,000) portfolios explain more than half of the development in 2004

Portfolios with at least 800 housing units only

Note: estimate for H1 2006
Source: ifs Institut für Stadtforschung und Strukturpolitik
Anglo-Saxon investors dominate as buyer

- HU in ‘000 -

Since 1999 Anglo-Saxon investors have bought approx. 650,000 HU

These have often been big portfolios

It is interesting that public authorities do not only act on the sell side

Misc. are, for example, investors from Scandinavia or Middle East

Portfolios with at least 800 housing units only

Note: estimate for H1 2006
Source: ifs Institut für Stadtforschung und Strukturpolitik

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Structural changes since 1999
- Difference between purchases and sales, HU in ´000 -

- Anglo-Saxon corporations win at the expense of public authorities
- But this has to be put in perspective: the whole German housing market amounts to 40 m HU!
- It is important to note that public authorities still possess about 2.5 m HU – and municipalities more than 2 m HU

Portfolios with at least 800 housing units only

Source: ifs Institut für Stadtforschung und Strukturpolitik
Resales growing significantly

- Portfolio sales will continue. But there are additional structural changes
  - Resales will become more important. BulwienGesa estimates that in the next few years only every third traded housing portfolio will be a new portfolio
  - The WOBA franchise in Dresden marked a break: First, the local authority paid off its debt in full. Second, political sensibility rose (see transaction failure in Freiburg and the compromise in the REIT bill)
  - There will still be first sales in the future, as the municipalities' financial worries will ease only in the short term, and the laws of economics won't change

- Amongst buyers the asset manager with a long investment horizon will dominate. Interest rate hikes will reduce the leverage effect. Opportunistic investors will rather retreat
Buyer’s view: What does this indistinct market offer?

- Prices for condominiums have been falling for years.
- Rents for existing stock stagnating currently after falling in the second half of the 1990’s.

Average for 50 and more than 100 German cities in east and west Germany, respectively.

Sources: BulwienGesa, Stat. BA DB R h.
Condo prices in 2006
- Existing stock -

- Hypoport (HPX) offers monthly data
- Prices do not rise for end-consumers
- How can portfolio investors achieve value gains?

Source: Hypoport, BulwienGesa
The buyer’s view: Condos are very “cheap” today
- Affordability index, all of Germany -

The affordability index measures mortgage rates for an approx. 80 m² unit and a 25-year mortgage in relation to disposable income per capita in Germany.

Sources: BulwienGesa, Bundesbank, OECD, DB Research
The affordability index measures mortgage rates for an approx. 80 m² unit and a 25-year mortgage in relation to disposable income per capita in Germany.
Population decline and ageing of society inevitable

Population decline about 10% till 2050

Big changes in the age structure

Source: Stat. BA, 11. koordinierte Vorausberechnung 2006
Tenant privatisation works, but success is limited
- Privatisation ratios in %, until early 2006 -

- Housing privatisation is an important business model
- Not all units can be privatised to the tenants
- Asset management has (almost) always to be considered

Note: bigger portfolios: 3,000 - 5,000 HU
smaller portfolios: under 3,000 HU

Source: BulwienGesa
Housing markets remain in motion

- In 2007 housing prices and rents will grow moderately. In many places stagnation is expected
- Hartz IV has already triggered a shift in housing demand. Small units are more sought-after
- Generally, for private persons it is a good time to buy a property. Prices are rising more slowly than incomes. Interest rates are still low, and supply is growing slowly
- The demographic trends are already casting a shadow on today's real estate markets
- Tenant privatisation is only one of many business models
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Housing is also a political good

- The sale of any public housing portfolio is going to be a political issue
  - The successful transaction in Dresden and the failure in Freiburg mark the cornerpoints in the discussion
  - Fundamentally, it is necessary to start the discussion
  - But it is amazing how simple arguments can ostensibly convince parts of the media and many politicians

Introduction to Real Estate Investment Trusts
- The bill does not allow German REITs unlimited investment in the residential sector (only new buildings or in mixed-use units with predominantly commercial use)
- This regulation, however, does not make sense either economically or for the tenants
- Nevertheless, it is a success that a compromise on REITs has been reached
A few words on German REITs

- REITs are not opportunistic investors. In the USA they are only moderately leveraged and are focusing on management and optimising of their portfolios.

- REITs provide an opportunity to public investors. They can keep their influence, for municipalities, too, may invest in REITs.

- REITs are not the answer to all questions in the German property market. This is a new product, which combines elements of existing products. Something new and dynamic is emerging.

- The biggest advantage of REITs is increased competition between investment products.

- Investors can also exit via the exchange without a German housing REIT; either as a conventional real estate corporation or via exchanges in other countries. Is this more desirable?
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Concluding Remarks

- Thinking in alternatives is necessary
  - The world has changed dramatically. Alleged public goods are frequently put to the test. This requires an important decision: which goods should be supplied in which quality by the government (direct implication: which goods should not!)

- Cautious argumentation with so-called positive externality
  - Here, these externalities are called “social or city return“
  - The social mix of tenants is always an implicit financial transfer from the BOTTOM to the TOP
  - The colourful mix we are (still) seeing in Germany partly stems from earlier shortages and from old transfer systems
Recommended reading (section) www.dbresearch.de

1) Bubble Trouble in the housing market (2003)
2) Demography sends tremor through German property market (2003)
3) Demography will not spare the public infrastructure (2004)
4) UK house prices: end of the rally in sight (2004)
5) Berlin property market: Heavily mortgaging the future (2005)
6) Housing portfolios in Germany: Scene set for further divestment (2005)
7) Retail warehousing prospects (2005)
8) Building up India: Outlook for India's property markets (2006)
9) German retail property: Opportunities despite oversupply (2006)