PRIMONIAL REIM GERMANY

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PRIMONIAL REIM GERMANY CONVICTIONS

Investor´s view on the German Real Estate Market

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The Research & Strategy Departments´s role is to formalize Primonial REIM´s real estate investment strategies, based on continuous monitoring of the European markets. By nature, real estate is at the crossroads of financial (interest rates), economics (tenants), demographic and social factors. This is why a broad analysis is needed, which is also long term and therefore matches the horizon of most real estate investors.

Primonial REIM relies on its local teams to provide on-the-ground research on the German markets. As Germany is a polycentric market, with specific real estate features, standards of valuation, demographic challenges and industrial forces, we want to provide a regular analysis of Germany´s real estate markets, from the investor´s viewpoint. This is the purpose of our quarterly *Real Estate Convictions Germany study.*

FIGURES 2022

FORECAST ECONOMIC GROWTH (GDP)

+1.3%

FORECAST INFLATION

+8.3%

10-YEAR GOVERNMENT BOND YIELDS

+2.1%

Source: Oxford Economics

ECONOMY

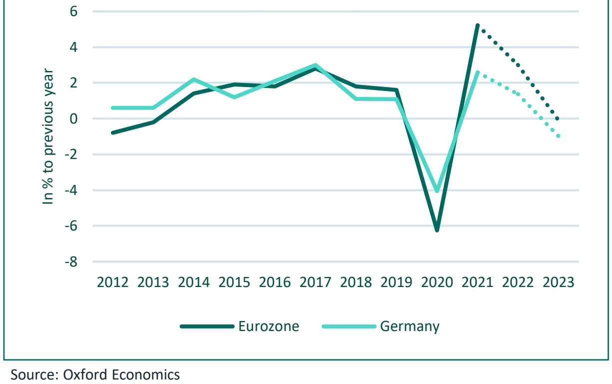
Autumn has begun in Germany and with it the worries about real energy shortages. Both industry and private households are currently facing major challenges. The forecasts for economic growth are accordingly associated with many uncertainties. At present, a moderate GDP increase of 1.3% is expected for the full year 2022. For the coming year, the German economy is currently expected to shrink slightly. The yield on 10-year German government bonds has now risen to over 2%. The risk premium for real estate is therefore melting down further. In conjunction with significantly higher construction interest rates, (further) rising real estate yields can therefore be expected in the medium term.

INFLATION

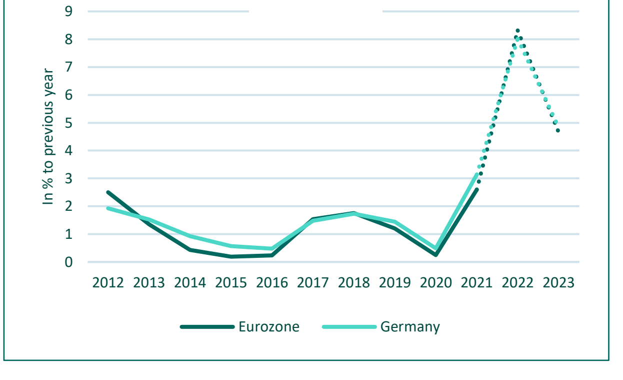
The monthly inflation rate in Germany reached record levels of over 11% in October. While the first signs of an easing in the inflation rate were still visible in the summer, prices rose again significantly at the start of the fall. For the year as a whole, inflation in Germany is expected to be aorund 8.3%. In the coming year, inflation is expected to recover slightly to around 5%, partly due to the base effect.

The ECB has already announced further interest rate hikes to curb inflation. In addition to the ECB decisions, the energy sector and the stability of global supply chains will be decisive factors in the medium-term development of inflation.

GDP



Inflation

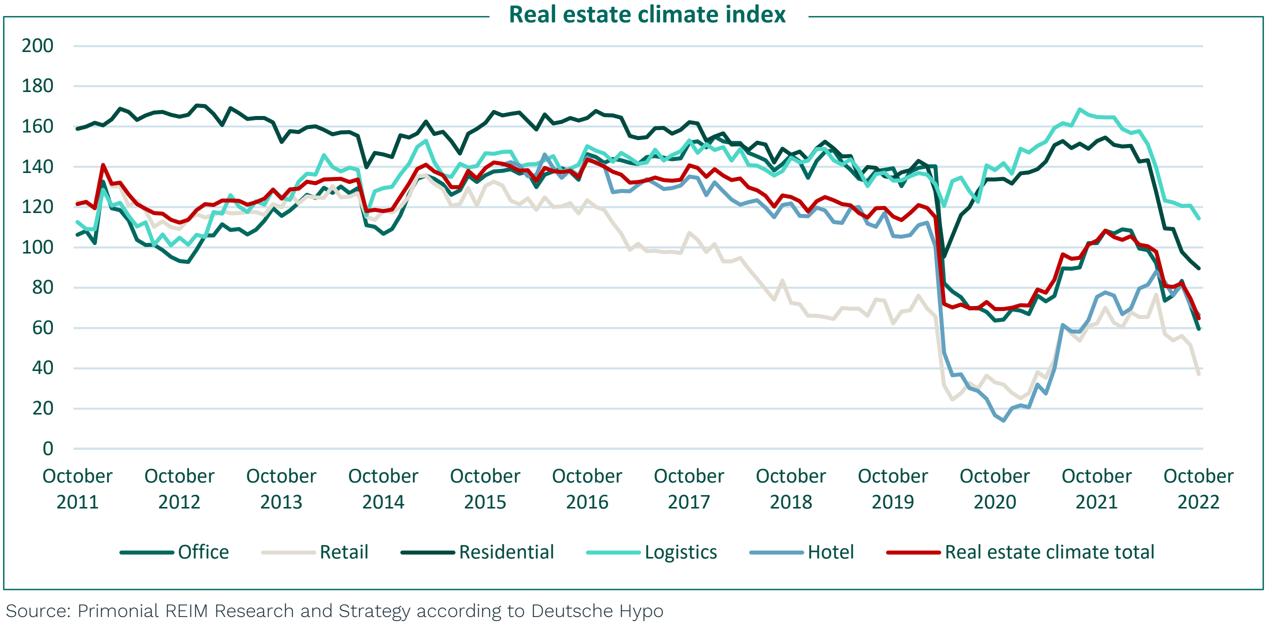


Source: Oxford Economics

GERMAN REAL ESTATE CLIMATE

The real estate climate had already plummeted dramatically by the middle of the year. This trend is continuing. The sentiment barometer for the overall real estate climate is at its lowest level since 2009 following the outbreak of the financial crisis. Even in the first shock phase of the corona pandemic in March 2020, a somewhat higher value was measured. In addition to inflation and interest rate developments, the real estate sector is primarily concerned with the issue of energy security. In the individual asset classes, the mood is somewhat less pessimistic than in the overall picture. The only asset class where sentiment remains positive is logistics (healthcare is not part of the real estate climate index). For all other asset classes, the mood is becoming increasingly pessimistic.

Furthermore, there is a certain imbalance between interest rates, yields on federal bonds and real estate yields, which means that many investors expect real estate prices to fall and remain in a wait-and-see mode. Provided that energy supplies can be guaranteed over the winter, a recovery in the real estate climate in early 2023 appears realistic. Nevertheless, falling real estate prices can still be expected in this scenario.



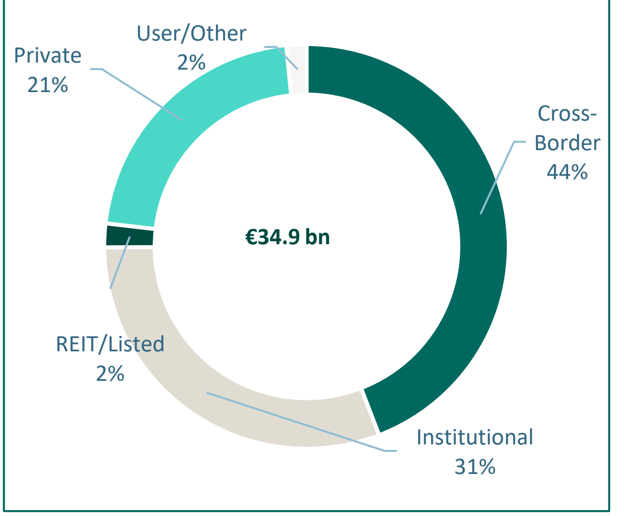
Source: Primonial REIM Research and Strategy according to Deutsche Hypo

TRANSACTION VOLUME

The great uncertainty in the market is reflected in the transaction volumes of the last three months. Many market players are currently adopting a wait-and-see approach, as a further downturn and price decline are expected. Potential sellers would in some cases have to accept significant discounts on their properties compared with their book values at the beginning of the year, with the result that there is little transaction activity overall. At the same time, the low number of transactions is making pricing more difficult for both buyers and sellers and reinforcing investor restraint.

In the first three quarters of 2022, the transaction volume was around EUR 35 billion and thus below the prior-year figure. While the major asset classes of office and residential are seeing significant declines in transaction volumes, healthcare remains one of the bright spots on the investment market as a niche asset class. At around EUR 1.3 billion in the first three quarters, the previous year's figure was exceeded. The challenging economic environment, in particular the sharp rise in construction interest rates, has led to increased yields in all asset classes.

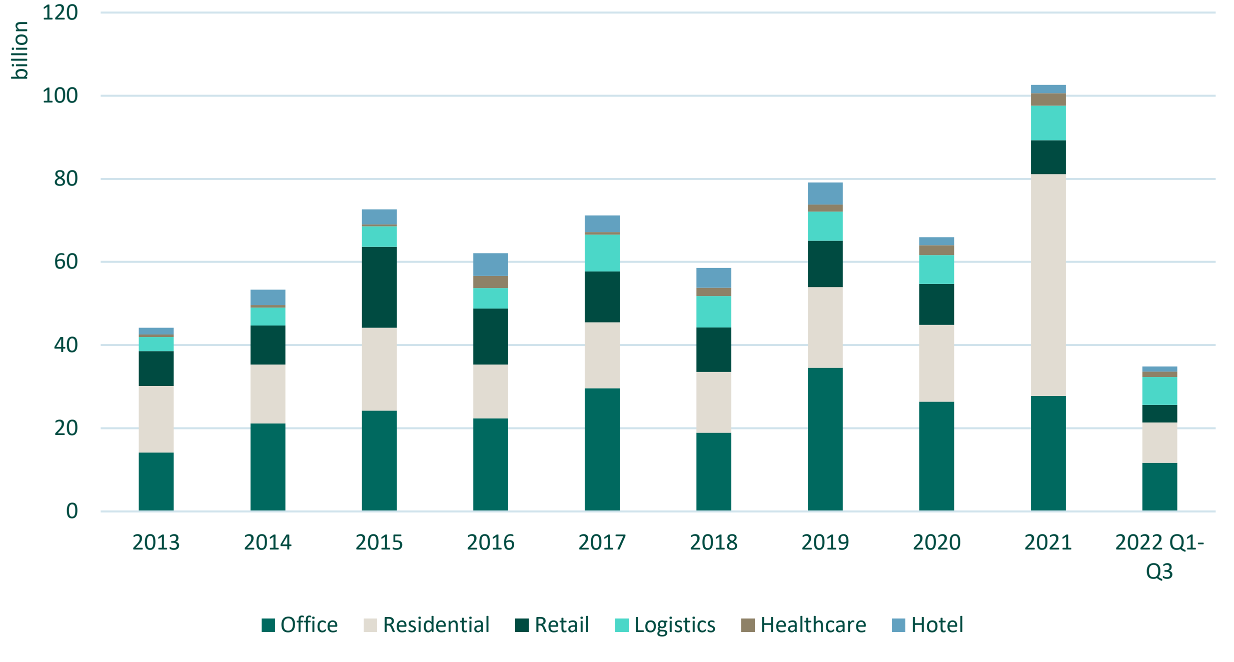
Investors composition Q1-Q3 2022



OUTLOOK

At present, there is little to suggest a genuine year-end rally on the German real estate market. The general conditions with high interest rates, falling prices and economic uncertainty appear to be too great for this to happen for many players. For some investors and project developers, however, the pressure to sell could increase further in the next six months due to liquidity bottlenecks and denominator effect, thus stimulating transaction activity.

Transaction volume per asset class



Source: Primonial REIM Research and Strategy according to RCA

SUMMARY ASSET CLASSES

Asset Class	Transaction Volume Q1-Q3 2022	Transaction Volume 5-year-average Q1-Q3	Cross-Border Volume Q1-Q3 2022	Prime Yields Q3/2022	Trend Transaction Volume Q1-Q3 2022
Office	€11.7 bn	€16.2 bn	€4.7 bn (40 %)	2.9 %	↘
Residential	€9.7 bn	€12.1 bn	€4.4 bn (46 %)	2.3 %	↘
Retail	€4.2 bn	€5.8 bn	€1.0 bn (25 %)	3.0 % (High-Street-Shops)	↘
Healthcare	€1.3 bn	€1.3 bn	€0.6 bn (49 %)	4.0 %	↗
Hotel	€1.3 bn	€2.0 bn	€0.3 bn (26 %)	4.5 %	↘
Logistics	€6.6 bn	€5.3 bn	€4.2 bn (63 %)	3.4 %	↘

Source: Primonial REIM Research and Strategy according to CBRE, RCA

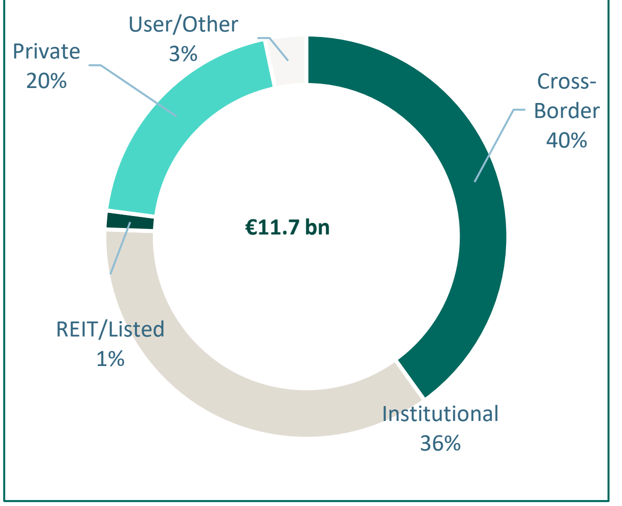
OFFICE

OFFICE TRANSACTION VOLUME Q1-Q3 2022	€11.7 bn
THEREOF CROSS-BORDER TRANSACTION VOLUME Q1-Q3 2022	€4.7 bn
PRIME YIELDS OFFICE A-CITIES Q3/2022	2.9 %
PRIME YIELDS OFFICE SECONDARY-CITIES Q3/2022	3.5 %
TRANSACTION VOLUME TREND COMPARED TO Q1-Q3/2021	↘

The office market continues to be divided between the investment and rental markets. On the one hand, there has been great restraint on the investment market since the outbreak of the Ukraine war and the recessionary concerns indirectly associated with it. In the first three quarters, a total of EUR 11.7 billion was invested in office properties - the lowest level for ten years. In addition to recession fears, the significant rise in interest rates and construction costs played a decisive role. This is reflected in the rise in prime office yields since the beginning of the year (+40 bp). Prime yields for office properties in A-cities are currently 2.9%, in secondary cities 3.5%.

Even though there are clear signs of restraint on the part of investors, the rental market remains stable. Prime and average rents in the top markets have risen slightly. At the same time, the top seven markets have seen a slight increase in vacancy rates and lower office take-up. The polarization with vacancy increases in peripheral locations and higher demand for central, modern office spaces is continuing.

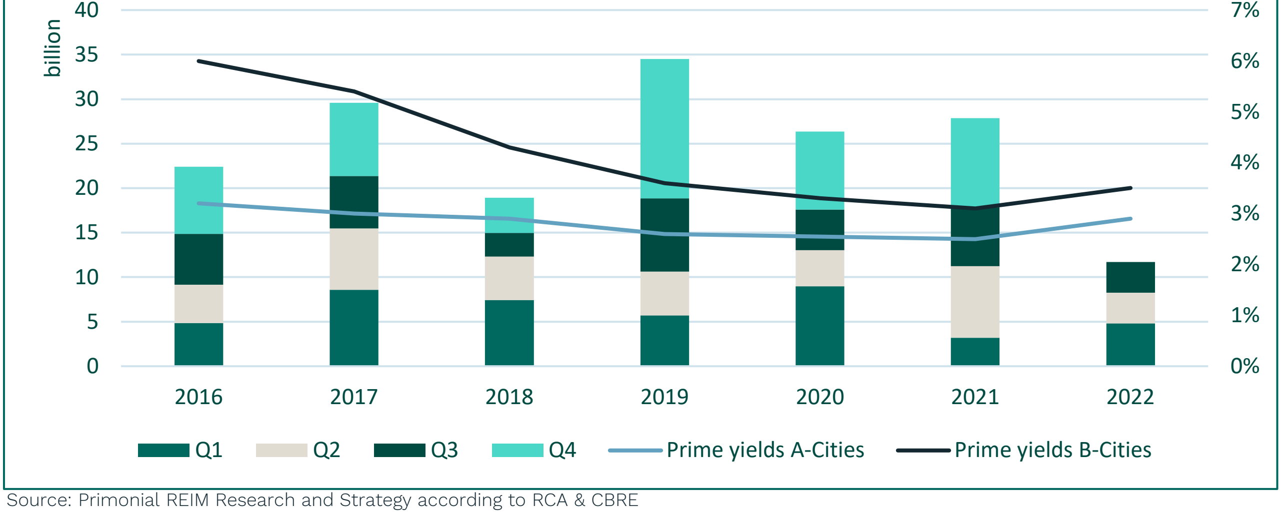
Investors composition office Q1-Q3 2022



OUTLOOK

As an asset class that tends to be cyclical, the office market is comparatively strongly affected by the economic uncertainties. So far, however, this has mainly been reflected on the investment side. It can be assumed that modern, centrally located and energy-efficient office spaces will continue to experience stable demand.

Office transaction volume and yields



Source: Primonial REIM Research and Strategy according to RCA & CBRE

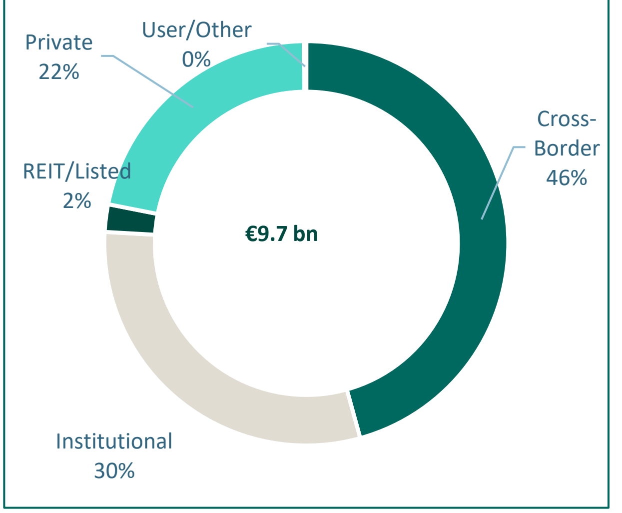
RESIDENTIAL

TRANSACTION VOLUME RESIDENTIAL Q1-Q3 2022	€9.7 bn
THEREOF CROSS-BORDER TRANSACTION VOLUME Q1-Q3 2022	€4.4 bn
PRIME YIELDS RESIDENTIAL Q3/2022	2.3 %
TRANSACTION VOLUME TREND COMPARED TO Q1-Q3 2021	↘

In the first three quarters of 2022, around EUR 9.7 billion was invested in residential real estate. This represents the lowest investment volume in four years. The main reasons are the sharp rise in interest rates. In addition, investors are showing restraint with regard to project developments. The virtually skyrocketing increases in construction costs are making it difficult for project developers to find investors at an early stage who would like to secure residential construction projects via forward deals. At the same time, investors are also taking a closer look at existing portfolios. The energy condition of residential buildings may have a significant impact on the prices of residential portfolios in the future.

In the meantime, the rough concept of the government relief packages to combat the high energy costs are known. Even if these measures can alleviate some of the high burdens, especially for threshold households, high inflation and energy costs will increasingly affect housing demand. Thus, investors should calculate with conservative assumptions regarding future rent increases.

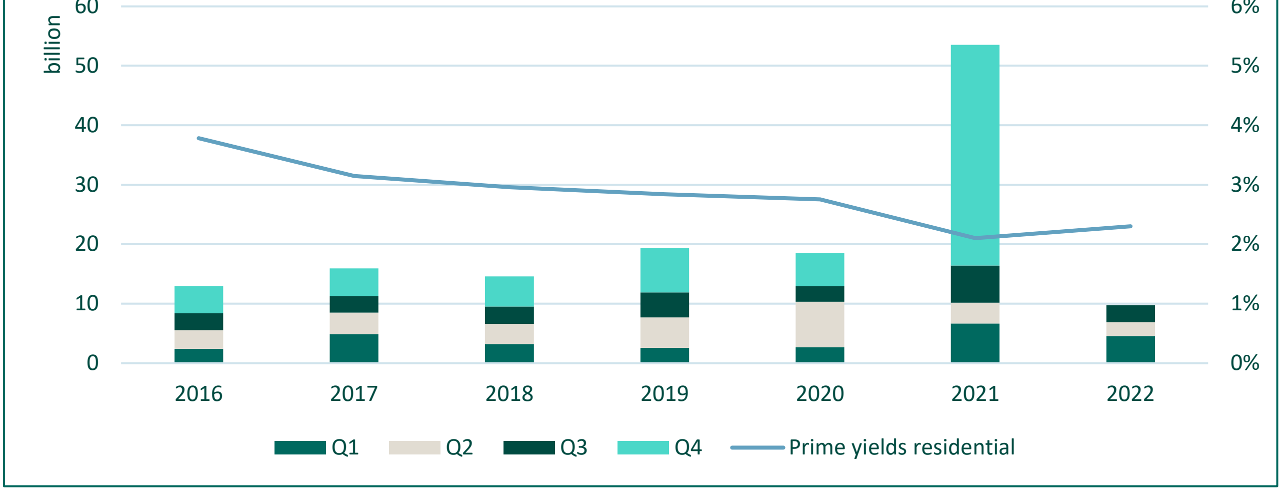
Investors composition residential Q1-Q3 2022



OUTLOOK

The housing market is directly affected by the explosion in energy costs, high inflation and the turnaround in interest rates. In this mixed situation, further declines in residential property prices are to be expected. Nevertheless, demand for energy-efficient existing buildings is expected to be high, both from investors and tenants.

Residential transaction volume and yields



Source: Primonial REIM Research and Strategy according to RCA & CBRE

RETAIL

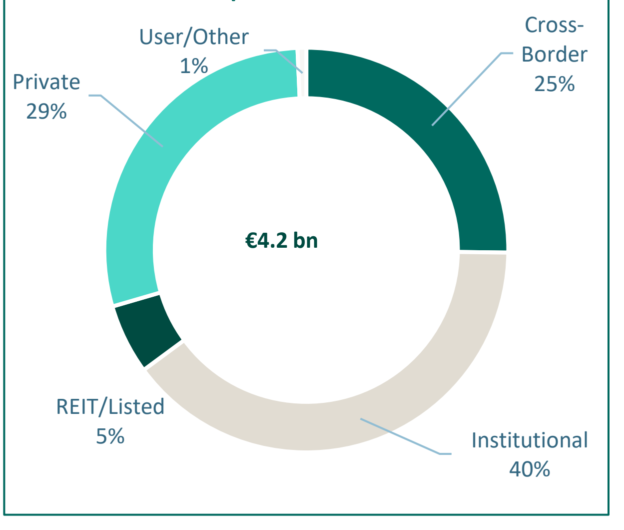
TRANSACTION VOLUME RETAIL Q1-Q3 2022	€4.2 bn
THEREOF CROSS-BORDER TRANSACTION VOLUME Q1-Q3 2022	€1.0 bn
PRIME YIELDS HIGH-STREET-SHOPS Q3/2022	3.0 %
PRIME YIELDS SUPERMARKETS Q3/2022	3.9 %
PRIME YIELDS SHOPPING-CENTER Q3/2022	4.9 %
TRANSACTION VOLUME TREND COMPARED TO Q1-Q3 2021	↘

In the first three quarters, EUR 4.2 billion was invested in German retail real estate. This figure is significantly lower than the transaction volumes of previous years in the same period. In addition, there is little to suggest that there will be a year-end rally this year against the backdrop of the macroeconomic conditions.

Prime yields for retail properties continue to rise gradually. They currently range from 3.0% for high-street stores to just under 4.9% for shopping centers.

Retail sales were better than expected in the first three quarters. Despite high inflation rates and thus real losses in purchasing power among private households, most sectors recorded slight sales growth. However, the outlook for the Christmas season is less optimistic. High energy prices and persistently high inflation rates are having a considerable impact on the consumer mood of Germans, as revealed by the barometer of the German Retail Association.

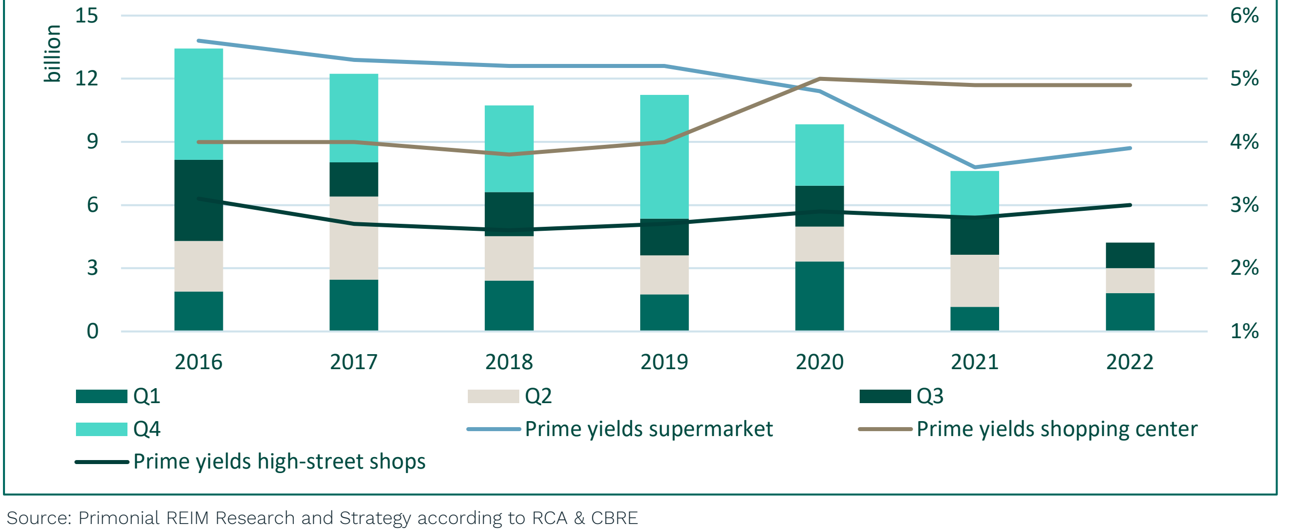
Investors composition retail Q1-Q3 2022



OUTLOOK

The retail sector continues to face major structural challenges. Added to this are high inflation and energy prices, which are dampening the consumer mood of private households and reducing retailers' sales expectations. Retail real estate will therefore remain something for opportunistic investors in the near future.

Retail transaction volume and yields



Source: Primonial REIM Research and Strategy according to RCA & CBRE

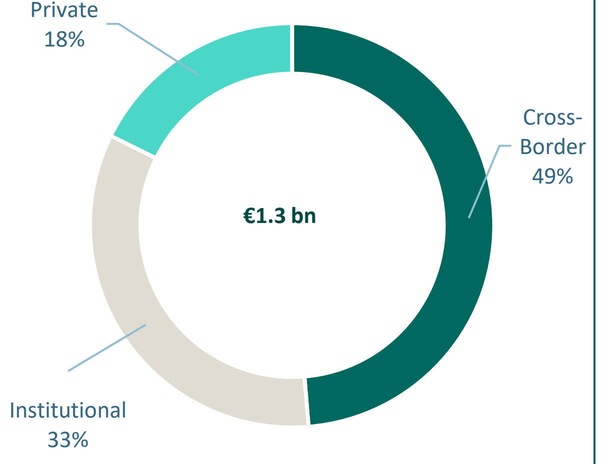
HEALTHCARE

HEALTHCARE TRANSACTION VOLUME Q1-Q3 2022	**€1.3 bn**
THEREOF CROSS-BORDER INVESTMENT VOLUME Q1-Q3 2022	**€0.6 bn**
PRIME YIELDS HEALTHCARE Q3/2022 (GROSS)	**4.0 %**
TRANSACTION VOLUME TREND COMPARED TO H1/2021	↗

The healthcare investment market continues to be robust. At around EUR 1.3 billion, the transaction volume is higher than in previous years in the same period. As an asset class that tends to be less dependent on the economic cycle, healthcare real estate enjoys a high level of popularity even in times of impending recession. The scarcity of healthcare real estate opportunities is today the greatest limit to investment. Nevertheless, the healthcare sector is also affected by inflation, interest rate developments and the energy crisis. Especially for operators of nursing homes, the increased personnel and energy costs pose major challenges. In addition, long-term leases usually contain inflation-linked rent adjustments, which can present operators with problems in the current market phase. For investors, this can mean in individual cases having to forego a rent increase or not taking advantage of the contractually possible rent adjustment leeway so as not to jeopardize the operator's solvency. Although operators can in principle pass on the costs of the real estate to the residents, a renegotiation with the nursing care insurance funds cannot usually be implemented in the short term. Possibly a trade-off implying lower indexation but longer leases can reconcile investors, operators and residents.

The fact that healthcare properties are also affected by the change in the macro environment is shown by a look at the development in yields in the third quarter of 2022, with prime yields for nursing homes rising by 10 basis points to 4%. .

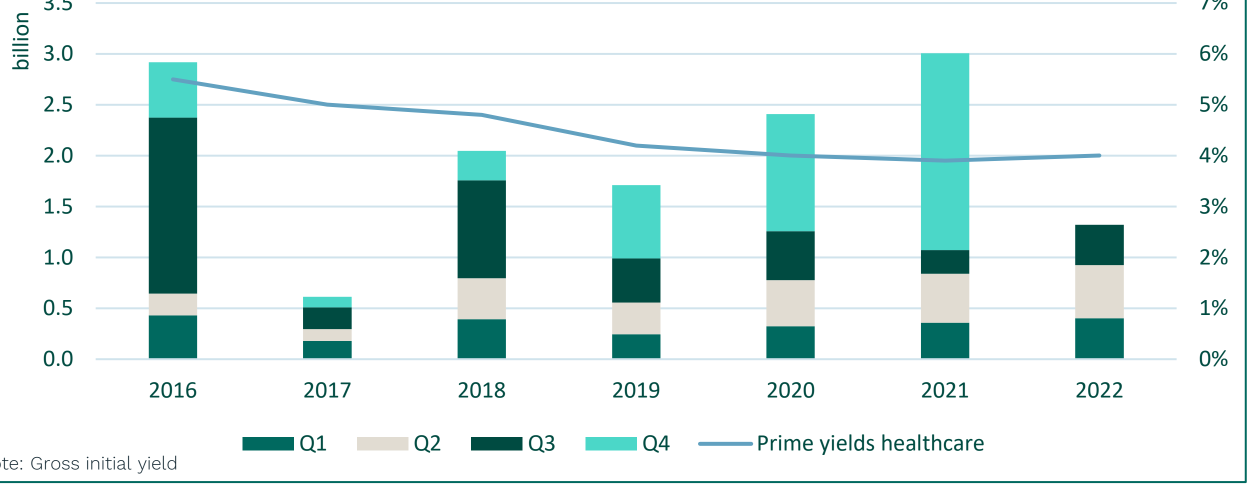
Investors composition healthcare Q1-Q3 2022



OUTLOOK

Investor demand for healthcare real estate has so far proved very resistant to the crisis. Nevertheless, the effects of the changed interest rate environment, high inflation and the energy price explosion are also being felt in the healthcare real estate market. Operators in particular can expect to face major challenges in the coming months due to the high cost burdens.

Healthcare transaction volume and yields



Note: Gross initial yield

Source: Primonial REIM Research and Strategy according to RCA & CBRE

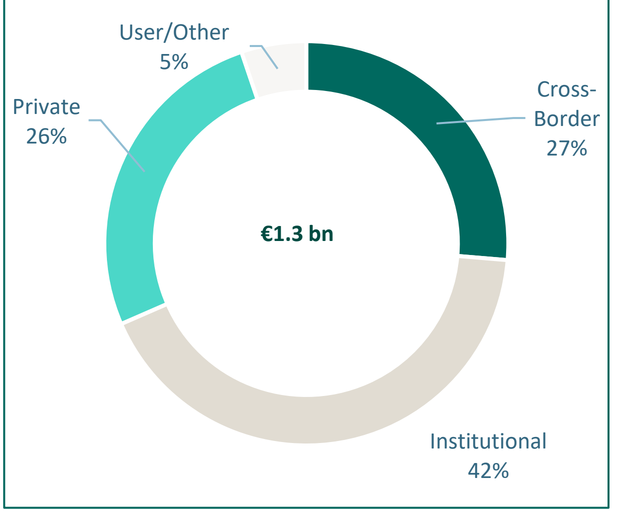
HOTEL

HOTEL TRANSACTION VOLUME Q1-Q3 2022	**€1.3 bn**
THEREOF CROSS-BORDER INVESTMENT VOLUME Q1-Q3 2022	**€0.3 bn**
PRIME YIELDS HOTEL Q3/2022	**4.5 %**
TRANSACTION VOLUME TREND COMPARED TO Q1-Q3 2021	↘

The summer and the main travel season of the Germans is over and also the hotel investment market can look back on a comparatively good third quarter. Although far from the investment volumes of the pre-Corona years, around EUR 1.3 billion was invested in German hotels in the first three quarters. Foreign investors in particular are skeptical about German hotel investments. This is reflected in transaction volumes of only EUR 300 million in the first three quarters.

Prime yields are currently at 4.5%. Further increases in yields are expected in the coming months due to interest rate developments and uncertainties in the hotel sector. The issue of energy will also become more important in the coming years due to the explosion in energy costs. Since hotel properties generally have high energy consumption, the issue of energy efficiency in hotel buildings will increasingly come into focus. Modern buildings with low energy consumption and high shares of renewable energies (e.g. via photovoltaics) will thus become more attractive. In addition, operator concepts that focus on sustainability, e.g., in food, heat supply, or resource consumption in operations, could also be in greater demand in the future.

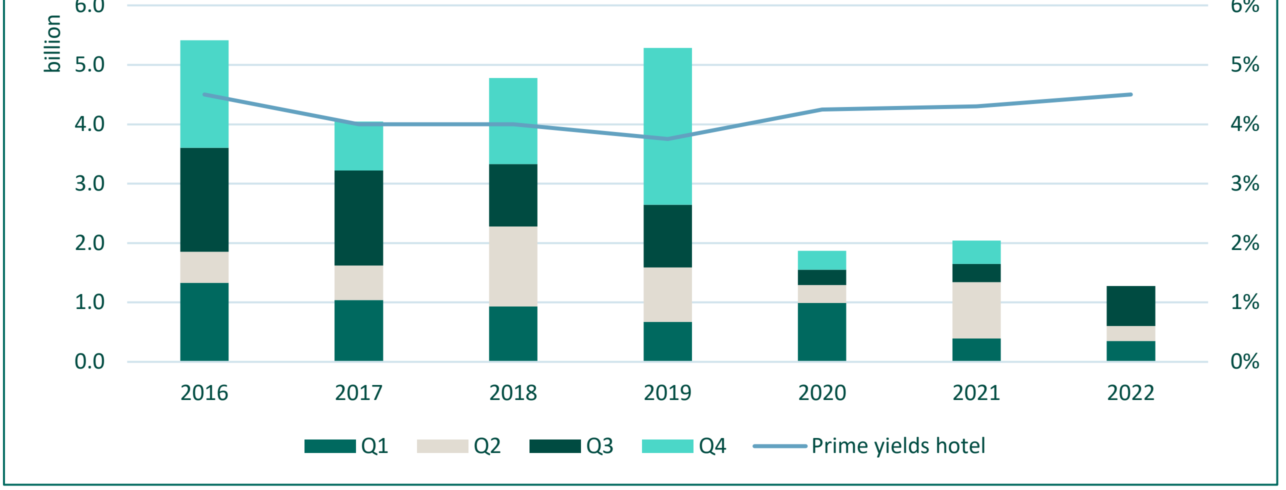
Investors composition hotel Q1-Q3 2022



OUTLOOK

Foreign investors remain critical of hotel investments. Due to the macroeconomic environment, the hotel industry will continue to face major challenges in the coming months. A quick recovery to the pre-Corona level of the hotel investment market therefore seems unlikely.

Hotel transaction volume and yields



Source: Primonial REIM Research and Strategy according to RCA & CBRE

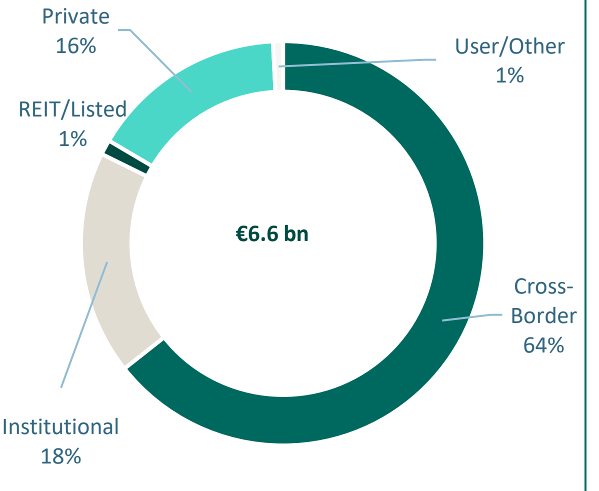
LOGISTICS

LOGISTICS TRANSACTION VOLUME Q1-Q3 2022	€6.6 bn
THEREOF CROSS-BORDER INVESTMENT VOLUME Q1-Q3 2022	€4.2 bn
PRIME YIELDS LOGISTICS Q3/2022	3.4 %
TRANSACTION VOLUME TREND COMPARED TO Q1-Q3 2021	↗

The boom in the German logistics market continues unabated. At EUR 6.6 billion, a new peak value was achieved in the first three quarters. German logistics properties continue to enjoy great popularity, particularly among foreign investors. However, it remains to be seen whether, despite the interest rate trend, there will be a year-end rally as in previous years. It seems more likely that investor restraint will also make itself felt on the logistics market in the final quarter of the year.

Prime yields for logistics properties currently stand at 3.4%, 30 basis points above the year-end value in 2021. Despite high demand, the macroeconomic environment is therefore also causing prices for logistics properties to drop.

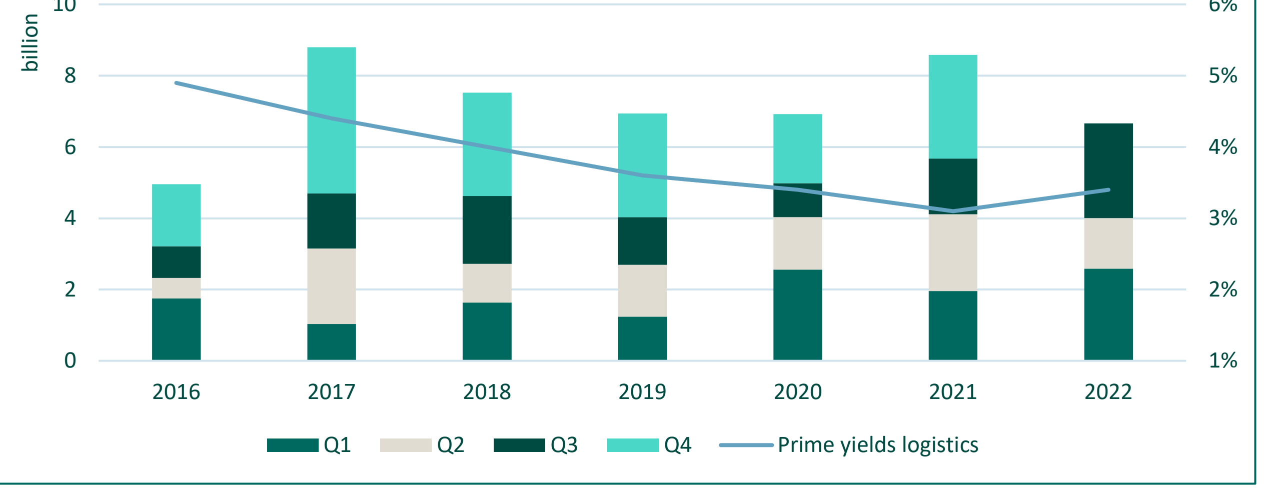
Investors composition logistics Q1-Q3 2022



OUTLOOK

The problems in global supply chains and increasing political uncertainty with regard to non-European production and storage facilities continues to be one of the drivers of logistics demand. High demand coupled with a shortage of supply is also expected in the coming months. However, due to the development of interest rates, prices are expected to fall slightly.

Logistics transaction volume and yields



Source: Primonial REIM Research and Strategy according to RCA & CBRE

DEFINITIONS

10-year government bonds: debt securities issued by a state for a period of ten years, generally acknowledged to be a risk-free investment.

Investment volume/transaction volume: total volume of premises acquired in the offices, residential, retail, business premises and warehouses segments by an investor.

Take-up offices: all leases or sales to the occupant (as opposed to sales to investors) for premises to be used as offices. It is expressed as square meters of usable space.

Yield: ratio between the net revenues from the building and the capital committed by the buyer (acquisition price + fees and transfer taxes). All yields quoted follow this definition unless otherwise stated.

High-Street-Shops: traditional ground-floor retail premises located in town-center high streets.

Shopping center: a building containing at least 20 retail outlets housed in indoor centers around a large food store that drives customer traffic.

RevPAR: abbreviation for Revenue Per Available Room. It corresponds to the turnover on accommodation of an establishment divided by the total number of rooms RevPAR also corresponds to Occupancy Rate multiplied by ADR.

Hotel Occupancy Rate (OR): ratio of the number of occupied rooms to the total number of rooms in a hotel.

About **Primonial REIM**

Primonial REIM has a workforce of 400 employees in France, Germany, Luxembourg, Italy, the UK and Singapore. Its values of conviction and commitment as well as its expertise on a European scale are used to design and manage real estate funds for its national and international clients, whether they are individuals or institutions.
Primonial REIM currently has €33.5 billion of assets under management. Its conviction-based allocation breaks down into:

- 45 % offices,
- 34 % healthcare/education,
- 10 % residential,
- 8 % retaill,
- 4 % hotels.

Its pan-European platform manages 61 funds and has more than 80.000 investor clients, 53% of which are individual investors and 47% institutional. Its real estate portfolio consists of more than 1.400 properties (offices, health/education, retail, residential, hotels) located in eleven European countries.

www.primonialreim.com

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The Research & Strategy Department's role is to formalize Primonial REIM's real estate investment strategies, based on continuous monitoring of the French and European markets. Although collective real estate accounts for a growing share of institutional portfolios and household savings, it is at the crossroads of financial (hierarchy of rates), economic (tenants' business models), demographic (the metropolisation phenomenon) and societal (changes in usage) factors. This is why a cross-cutting analysis is needed, which is also long term and therefore in keeping with the horizon of most real estate investors.

Real Estate Convictions Germany offers Primonial REIM's quarterly view of the most important asset classes: offices, retail, residential, healthcare, hotel and logistics.

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