# Construction of Rental Housing in Berlin

## Is It Coming Back to Life?

### Political Mandate to Build Rental Housing

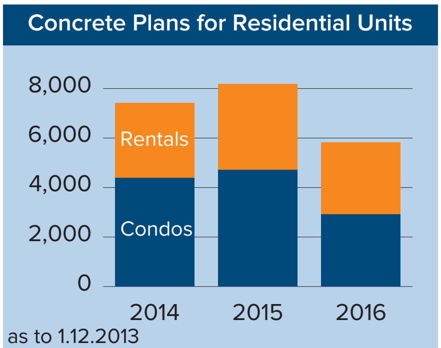
While investors still remember the adverse market developments of the 1990s and early years of this century, the positive employment figures, the economic upturn, and especially the high rate of in-migration from within and outside of Germany have generated increased interest in the city, and is reflected in rising local rents and prices.

The coalition agreement for Berlin's city government from 2011 includes first responses to these developments in the form of a political commitment and mandate to promote housing construction. Especially the municipal housing companies were advised to step up their building activities in order to address what many perceived as a looming housing shortage.

### Increasing Significance of Rental Housing Construction

Berlin needs more rental flats, and needs them fast. Current plans project the creation of 21,400 rental flats and condominiums in multi-family residential buildings over the next three years. Around 7,500 units will be realised in 2014, thereof 60 % as condominiums.

Concrete plans for 2015 envision the completion of around 8,200 residential units. Developments yet to be announced are likely to boost this volume even further.




From the present point of view, even the development pipeline for 2016 is very well endowed, with more than 5,800 residential units planned. Judging by segments, the completion rates suggest that a stalemate could be reached by 2016. So far, bulwiengesa registered a share of 49.7 % planned units are rental flats.

The intended construction of rental flats, with roughly 9,400 units in the pipeline today, has clearly gathered momentum, and could soon outpace the condominium segment. Private investors, who realise 75 % of the total development volume, predictably play a highly important

**TOPICS:**



Dear Readers,

one could say a rather normal year is drawing to a close. Aside from the distress experienced by certain real estate companies, steady price growth on the core markets, and the bankruptcies of some major retailers, not much has happened. Even the real estate bubble failed to form, leaving doomsday prophets high and dry. Which is just as well. After years of serious turmoil, we could do with a bit of peace and quiet. Smart market players have used the breather to prepare for tomorrow, and so they should. In this sense, we wish all of our friends, acquaintances, and clients a wonderful holiday season and every success in the coming year 2014!

Sincerely Yours,

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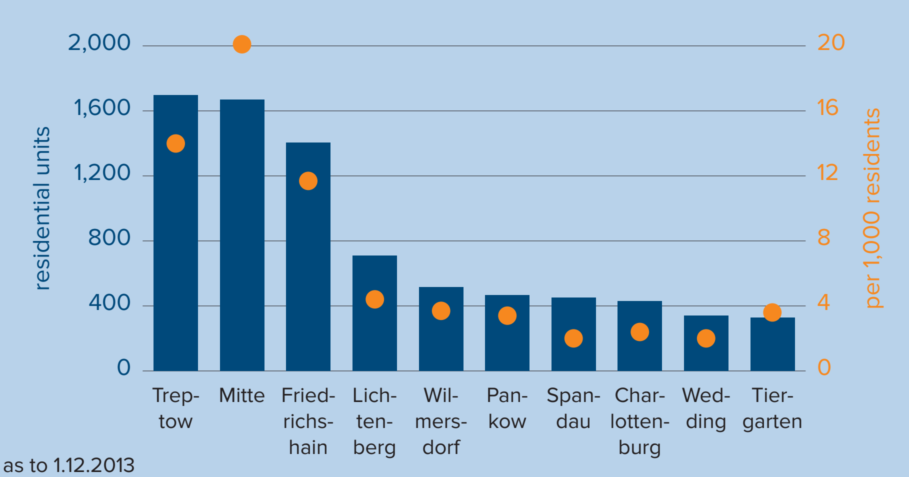
**Construction/Planning Volume for New Rental Flats through 2016 – Top 10 Districts**




as to 1.12.2013

role for Berlin's rental housing market. Anything but negligible is the share of municipal and cooperative market players, who account for the rest of the planned housing units with a share of 12.5 % each.

### Rental Flats in the Suburbs Only?

If you think that rental housing construction in Berlin is more or less confined to the urban periphery due to skyrocketing land prices and the competition of the condominium segment, think again.
Although the peripheral district of Treptow reports the single biggest construction volume of nearly 1,700 residential units, the inner-city districts of Mitte and Friedrichshain are trailing just closely behind.

In the ten districts with the highest development volumes, nearly 60 % of the rental flats planned will be raised in highly coveted downtown locations. That said, the market is dominated by private providers. Municipal housing companies do indeed concentrate their development activities in suburban districts such as Treptow, Lichtenberg, Pankow, and Neukölln.

### Keen Demand for Investment Opportunities in Rental Housing Construction

The massive demand for rental flats generated by private households has ramifications for the investment market, too. Pension funds and institutional funds have lately (re)discovered Berlin as an attractive investment destination. Purchase prices and multipliers are rising. Top assets may by all means sell for 18 to 22 times the net annual rent.

Even municipal companies acquire properties directly from developers, a recent case in point being the acquisition of more than 100 flats in Rudow, a sub-district of Neukölln, by the city-owned degewo AG. It is a strategy that helps them to fulfill their planned housing construction quota sooner.

### Demand for Rental Flats Will Play an Even Bigger Role in the Future

Despite the high development activity in the condominium segment, the housing market demand across the city will be subject to an intensifying focus on the rental segment. The task at hand will be the creation of a broad-based housing supply that serves specific target groups in the majority of districts.

It remains to be seen, however, what sort of ramifications the political parameters will have on the willingness of investors to commit themselves. The key word being "Mietpreisbremse" (rental price cap).

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# Where Do Retail Warehouse Multiples Rent?

## An Analysis of around 15,900 Retail Warehouse and Concessionaire Units

As 2013 is drawing to a close, retail warehouses remained the centre of attention in the retail property segment even in the concluding quarter as the wind-up of the Max Bahr DIY chain made headlines. While the issue of the potential reutilisation of large-scale retail warehouse formats present itself quite graphically from a real estate industry perspective, the bankruptcy demonstrates, just as dramatically, the microeconomic cost pressure that retail warehouse multiples are subject to.
The case of these big box venues exemplifies the different perspectives of market players in the retail warehouse sector. On the one hand, there are investors, who associate managed retail warehouse parks with the hope for rental growth upside, whereas retail warehouse multiples, on the other hand, judge potential in terms of market and location, the degree to which a given retail destination is established, and favourable planning law.

Both sides place a premium on the terms "retail warehouse park" and "sustainability". Yet these terms quite obviously signify different things for investors and retailers, respectively. While investors have the Anglo-Saxon model of managed large-scale centres with 10,000 sqm GLA or more in mind, retail multiples will also use the term for non-managed, smaller-scale integrated locations or agglomerations. And while "sustainable" means an investment with rental upside potential for one party, it connotes a micro-economically viable location from a market and location perspective. What the two angles have in common, though, is that the cost to income ratio is the measure of all things, be it for an investment or for a retail operation.

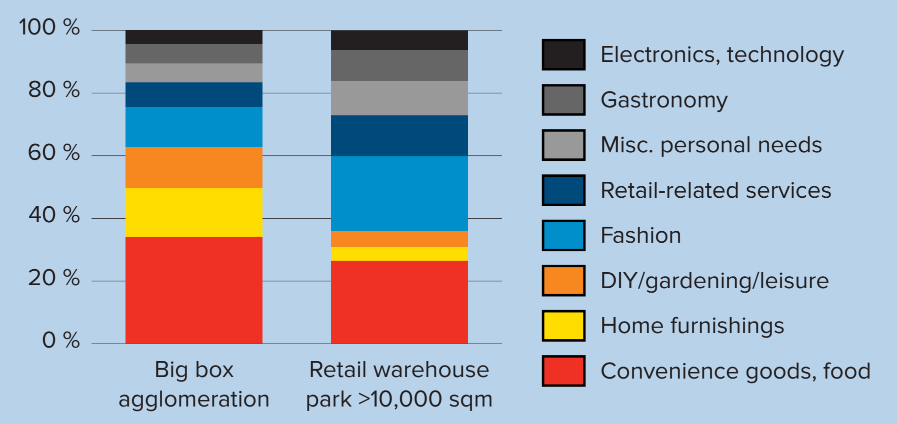
However, investors look for long lease terms, high-net-worth multiples, and strong, footfall-generating brands in order to ensure a sustainable investment, whereas retail warehouse multiples have the choice of genuine alternatives to the managed retail warehouse park. The aforementioned as operating type will have to brace itself for serious competition with existing, well-established retail warehouse agglomerations and other integrated locations in its efforts to attract tenant leads.

In quantitative terms, the predominant share of retail warehouse space is located in retail warehouse agglomerations, some of which feature a highly differentiated sector diversification in established retail locations, and are hardly inferior to managed modern retail warehouse parks. Operators of managed retail warehouse parks will thus be hard pressed to convince prospective tenants of the added value of the location, and of the merits of cost-generating measures that tend to be lower or non-existent in retail warehouse agglomerations, and which therefore do not impact the overhead.

So the respective locational advantages could be summarised as "centre benefits" versus "cost benefits".

The juxtaposition will have a limiting effect on the potential tenant mix and the sector line-up of managed retail warehouse parks, because those who may

**Comparing Sector Diversifications**
(Tenants by main commodity groups, N = 15,914 retail units)




not be available as tenants might well be the ones that shoppers expect to find in a given venue and are badly needed to compete.

This brings us to the critical question what exactly will drive the much-touted rental growth, due to investment and revitalisation measures, at managed retail warehouse parks if the retail warehouse multiples themselves are unwilling to shoulder their share of the costs.

The likely thing to happen is that classic high-street multiples and shopping centre tenants with concepts eligible for the retail warehouse market will try to secure a share of that market, motivated by the benefits of rents markedly lower than high-street and shopping centre rates.
International retail warehouse multiples seeking to enter the German market may see the advantage of moving into managed schemes because it saves them start-up costs and a lot of red tape by not having to deal with planning authorities.

Looking at the tenant line-up, one gets a latent feeling that managed retail warehouse parks increasingly resemble regular shopping centres – to the extent permitted by their zoning parameters.

Initial verifiable information on sector diversification at retail warehouse locations of various types will be delivered by a data sample of currently around 15.900 retail units (around 23.8 million sqm of retail area) that bulwiengesa collected through field research.
In the coming days, bulwiengesa AG will complete its nationwide survey of German retail warehouse locations of 10,000 sqm or more, covering both the main tenants and their concession catering operations in retail warehouse agglomerations, retail warehouse parks, and stand-alone locations. The fact that concession catering operations are also considered, permits the analysis of tenant and sector diversification even of complex integrated locations.

Around 33 % of the occupiers and concessionaires captured are located in retail warehouse parks, more than 62 % in retail agglomerations, whereas stand-alone retail warehouses account for only a marginal share of 5 %. When comparing the type of sites by industry affiliation, the following picture presents itself:

- Home furnishing/DIY retailers are traditionally more prone to operate in agglomerations than in managed retail warehouse parks.

- Food and convenience goods retailers, accounting for 34 % of the tenants, are found to a greater extent in retail warehouse agglomerations than in managed retail parks. Therefore the food and beverage segment shows a similar breakup of 25 % in agglomerations and 16 % in retail parks.

- Predictably, fashion retailers favour managed centres over agglomerations. At 13 %, the tenants of this sector have the same pro-rata presence in retail warehouse agglomerations as the DIY sector.
- Retail-related services (13 %) and gastronomy (8 %) have higher shares in retail warehouse parks, but represent no less than 6 to 8 % of the tenants in retail warehouse agglomerations. Concessions areas of bakeries and delicatessen complete with seating areas were disregarded for the purposes of this survey, but nonetheless play a relevant role for the quality of stay in retail agglomerations.

It becomes rather obvious that, while sector diversification still more or less manifests traditional characteristics depending on the location, the gap between retail warehouse agglomerations and managed retail warehouse parks is closing in regard to service share and quality of stay.

The Top 10 group of tenants most frequently identified includes, in addition to discount food stores, four fashion multiples, one drugstore chain, as well as a restaurant chain (McDonald's). However, this group accounts only for around 13 % of the surveyed rental units, and for only around 5 % of the retail areas surveyed, the average retail area per unit being 590 sqm.

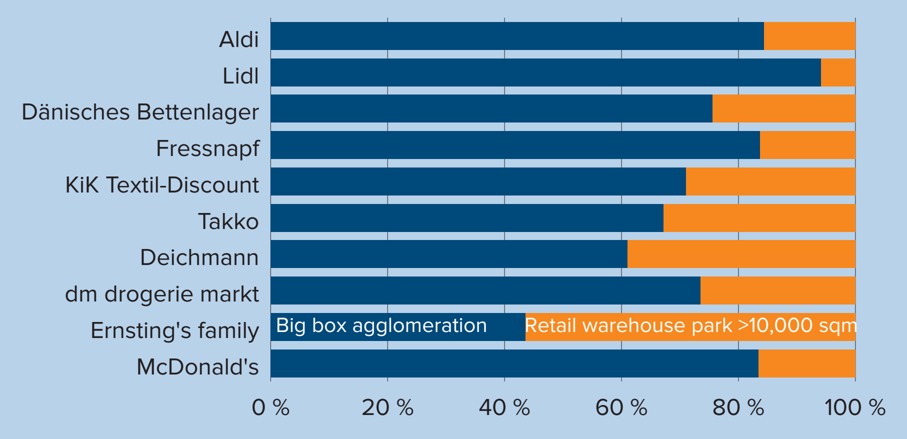
Strategically oriented to this kind of unit size, these tenants may do with relatively flexible floor space options in any type of retail park pitch, as well as in shopping centres or high-street locations, as long as the microeconomic parameters are right.

The chart shows that multiples of this part still rent predominantly in retail warehouse agglomerations, with Ernsting's Family the only retailer in this group to operate roughly the same number of small-scale units (about 54 %) in retail warehouse parks of 10,000 sqm or more as in retail agglomerations. The presence of McDonald's shows that they have long developed ways to accommodate retail warehouse locations of any format.

Overall, the survey found few multiples with a substantially higher number of branches in retail warehouse parks than in agglomerations, cases in point being Mister*Lady Jeans, Jeans Fritz, C&A, Bonita, and Depot, among others.

A pinpoint analysis of classic high-street and shopping centre tenants covered by the available data, by contrast, revealed that only a few of them, e.g. s.Oliver, Esprit, H&M, Street One, New Yorker, or Bijou Brigitte, chose to open branches in retail warehouse locations. This type of multiple accounted for less than 1 % of the surveyed floor area, and for only around 0.2 % of the total retail area covered.

**Top 10 – The Most Common Multiples in Retail Warehouse Locations**
(by frequency and split, N = 15,914 retail units)




**Frequency of High-Street Multiples in Retail Park Pitches >10,000 sqm**

| Multiples | Number of units | Average retail area per unit |
|---|---|---|
| s.Oliver | 24 | 210 qm |
| New Yorker | 20 | 490 qm |
| Bijou Brigitte | 18 | 60 qm |
| Street One | 18 | 150 qm |
| ESPRIT | 15 | 350 qm |
| Cecil | 12 | 110 qm |
| H&M | 8 | 1,600 qm |
| Orsay | 8 | 140 qm |
| Gesamt | 123 | 320 qm |
| Share in the overall survey (N = 15,914, 23.6m sqm) | 0.8 % | 0.2 % |

Coming back to the opening remarks, it is safe to say:

- Retail warehouse agglomeration hardly take the back seat to retail warehouse parks in terms of sector diversification. Concessions areas represent a good way for retail warehouse agglomerations to offset functional shortcomings concerning quality of stay and the service spectrum.
- Indeed, the most important retail warehouse multiples, including those in the fashion segment, currently operate in non-managed, agglomerated retail warehouse locations.
- Few of the classic high-street multiples have so far chosen to open branches in retail warehouse sites.

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