

Berlin Residential Investment Market

News Update on Berlin's Rental Housing Market

November 2009



“The Berlin News”

Investment Climate Improves

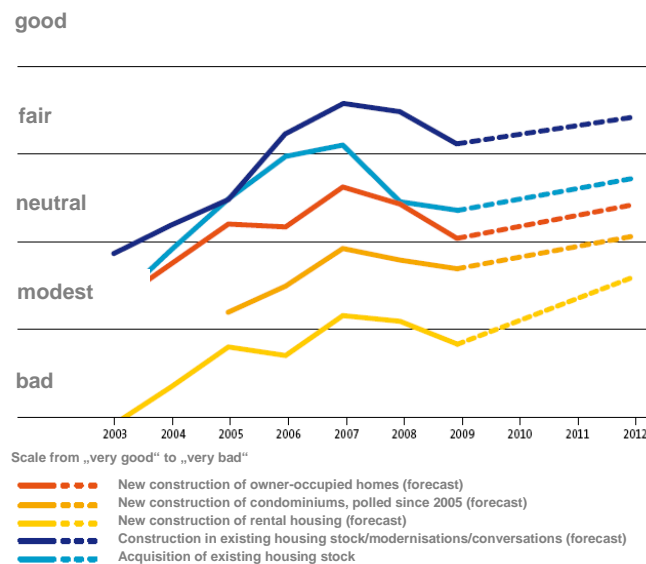
The 2009 IBB Residential Market Barometer for Berlin has diagnosed a particular need for additional housing in Germany's capital that appears to reflect the specific requirements posed by the demographic changes. Accounting for a 70 percent share of the shortage, demand is highest for senior-living and barrier-free apartments – particularly in the mid-price but also in the low-price segment. The situation looks similar in regard to redeveloped rental housing, where 65 percent of the poll respondents see a particularly dire need. The percentage is nearly as high for single-person rental housing, though the demand is higher in the lower than in the medium price segment. Less pressing is the need for additional supply in attic apartments, inner-city terrace housing, and semi-detached houses. For its Housing Market Barometer, Investitionsbank Berlin (IBB) polled housing companies, housing management companies and owners, estate agents, valuers, public sector administrations, tenant unions, lenders, and social institutions.

Berlin's condominium and rental housing markets have developed asynchronously for some years now. This is confirmed by the latest assessments. While the situation for condominiums has relaxed, the rental housing market presents a differentiated picture. Poll respondents painted a particularly bleak picture for the lower price segment, in contrast to the medium and even more so to the upper price segment. Analogously, they predicted the highest demand increases for the lower price segment through 2012. By contrast, forecasts for the upper price segment suggest an unchanged or indeed regressive demand trend, as they do for condominiums, too.

The investment climate projects an upward tendency through 2012, both for newly constructed and existing housing. Estimates regarding the investment climate peak across categories

in 2007, and have since declined before the background of the general economic environment, in some cases substantially so. Then as now, low income levels impact Berlin's housing market like no other factor, or so the interviewees believe. Also, the city's low level of housing construction is deemed problematic by more respondents than in 2008.

Investment climate on Berlin's residential market
Assessment by 232 expert poll respondents



Source: Investitionsbank Berlin “IBB Wohnungsmarktbarometer 2009”

Column

Berlin – Up and Coming Location

By Dr. Rainer Zitelmann



In late September, the HANDELSBLATT published the “Zukunftsatlas Branchen 2009,” a collection of forecasts for a variety of German industries compiled by the Swiss economic research institute Prognos. It identifies

Germany’s 25 top regions with business sectors poised for future growth. Runner-up was the nation’s capital Berlin, second only to Hamburg. This means, it placed ahead of Munich, Frankfurt, Cologne and Stuttgart. The question underlying the survey was: Which of Germany’s regions are economically fit for the future?

In a first stage, the Swiss researchers identified industries with a high long-term growth potential. To this end, they relied on the long-term forecasts of the “Prognos World Report 2009, Industrial Countries 1995 - 2025.” Prognos concluded that seven industries with great prospects will be the key growth drivers of the future: healthcare, information and communication technology, automotive engineering, mechanical engineering, measuring, controlling and automation technology, high-end corporate and research services.

In a second stage, Prognos analysed employment figures to identify the leading German regions in growth areas. The cluster index computed for this purpose integrates the three characteristics of strength, dynamics, and localisation. On the basis of the cluster indices, Germany’s leading regions were determined from among all 413 counties and corporate cities.

Among the top 20 regions, Berlin placed first in Germany’s healthcare sector, second in the area of high-end corporate and research services, fourth in the area of logistics, and sixth in the information and

communications technology segment. With all indicators taken into account, Berlin scored second place overall!

According to the survey, Berlin is the location with most employees in high-end corporate, research and development services. “The proximity to universities, interest groups and government smorgasbords is exerting a magical pull on advisers, attorneys, and head-hunters,” observed Bernd Kreuels of Stifterverband für die Deutsche Wissenschaft, an association of science sponsors.

Prognos found that Berlin is not just the most important location for communication and media but also the biggest research location in Germany. Medical R&D is particularly strong here. In addition to major corporations such as Bayer Schering Pharma and Berlin Chemie, a number of small biotech companies have set up shop in the vicinity of 17 centres operated by the Charité hospital complex centres and diverse other medical research institutes. What does all this imply for real estate investors? The long-term appreciation of a property is above all determined by the economic prospects of the respective location. Real estate values in Munich have substantially increased over the past decades, whereas the value of real estate in Saarbrücken or Bremerhaven, for instance, has declined. The reason is this: Munich has become an established location for pioneering technologies, whereas Saarbrücken and Bremerhaven are dominated by industrial sectors whose time has come and gone.

To be sure, Berlin today is not a major economic location – on the contrary. Yet, what counts for real estate investors with a long-term horizon is not the present situation, but the prospective situation ten or 15 years from now. This makes it all the more important to identify trends and growth potential early on. Those who plan to acquire real estate in Berlin or have already done so will feel vindicated by the findings of the Swiss researchers. For a more detailed look at the survey, please go to www.prognos.com/zukunftsatlas.

Market Performance

What Counts in the Long Run are Stability and Security

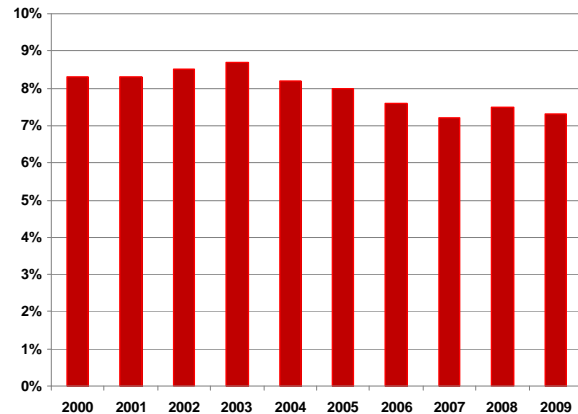
By Jürgen Michael Schick, MRICS

In the past, capital investors used to look for the best interest rates for their financial commitments. More often than not, the most auspicious asset classes proved to be rather volatile as well. Obviously, great opportunities tend to come with corresponding risks. Not always did the scales of the risk/reward ratio tip in favour of the investors. Many investment vehicles have spectacularly failed. If nothing else, enlightened savers should shun any promise of returns well into the two-digit range. Thousands of investors have lost their fortunes to such inflated upside targets in recent years. It is hardly a secret that real estate investments currently show comparatively high or indeed very high interest rates. This, however, is not explained by a sudden surge in real estate performance from what it used to be five or ten years ago. Rather, the other capital investment options have ceased to be viable alternatives in times of low interest levels and stock markets both volatile and unreliable.

When quizzed about the chances of real estate commitments I tend to point at one characteristic above all: stability. Prospective buyers will frequently limit their interest to the development of purchase prices. Have prices perked up lately, they wonder, or have they softened? Does the retreat of international buyers pave the way for re-entering the market, or is the market so overgrazed by private buyers that choice properties in good locations have become hard to find? Yet those who keep their eyes solely on the price performance will lose sight of the most important factor, which is the permanently stable profitability of let property. Given its absence of major dips and major hikes both, no other type of investment offers an interest rate of comparable stability. Average apartment buildings in Berlin have

earned a gross yield of nearly eight percent in recent years. At the start of the decade, the relation of purchase prices and annual net rents equalled 8.3 percent. Prices were lowest in 2003 with a gross yield of 8.7 percent.

Development of yield rates for residential property as capital investment in Berlin

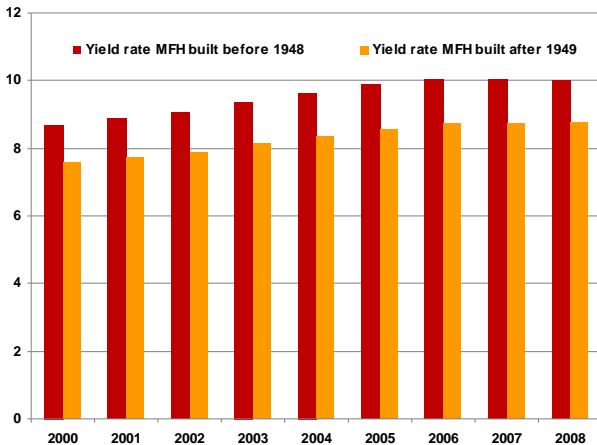


Source: Michael Schick Immobilien

Today, Berlin's market for apartment buildings – meanwhile matured – has stabilised at 7.3 percent. Taking a long-term view, this is a unique characteristic. Rental house owners are well aware that they will realise anywhere between 7.3 and 8.5 percent in gross returns, year after year. Naturally, they need to factor in the non-recoverable management costs and ancillary acquisition expenses to arrive at the net yield figure. But you would be hard pressed to find the same level of stability elsewhere. Its virtually non-existent volatility makes real estate an important anchor in any portfolio. During the banner years of the stock market word from the banks was often that apartment buildings were “overinvested” in the real estate sector and that you were well advised to shift your cash to more lucrative equities. With the benefit of hindsight it is easy to see that property-based portfolios continue to report the highest gains, whereas countless other portfolios have suffered veritable meltdowns. To be sure, the Berlin market is a particularly lively one, making it apt to take a look beyond the city limits. Yet

even when taking a nationwide perspective let multi-family home present an extremely stable form of investment.

Development of yield rates for residential property as capital investment nationwide



Source: IVD

Between 1990 and 2008, the aggregated gross yield rates in 200 German cities moved in a range between well over eight and just short of ten percent. In fact, even institutional portfolio managers should expand their real estate quota substantially to raise

the stability of the assets under their management. Looking back at the past two decades, though, it is interesting to see that prices nationwide have tended to slip, if anything. This is due to the defensive price performance in structurally weak regions such as northern Hesse, parts of lower Saxony, northern Bavaria and large areas of eastern Germany. Berlin, by contrast, being a city with a considerable catch-up need in terms of prices and rents, has experienced a gradual price increase and along with it a slight decline in initial yield rates. For buyers committing themselves in Berlin today, this opens onto the very real prospects of realising capital growth in addition to their regular rent returns. One can hardly repeat it often enough that the positive development of rent rates and the dwindling housing supply present wonderful opportunities for apartment building buyers in terms of future performance. Ultimately, however, stability – and with it security – strikes me as the one characteristic of the apartment building market that renders it superior to any other form of capital investment.

Portrait of a District

Variety in the North of Berlin

The headline aptly captures the nature of Berlin's borough of Pankow. During the district reform of 2001, the district of Pankow merged with the adjacent districts of Prenzlauer Berg and Weissensee. Its population of 360,000 makes Pankow the most populous borough of Berlin. From the faddish quarters in Prenzlauer Berg, to Weisser See lake, and all the way to the numerous shopping malls and farmer's markets, Pankow is home to a wide variety of options on nearly 1400 hectares.

Historic Roots Dating back to 1230

First mention of the name of Pankow dates back to the year 1230 in the context of transferring a plot to a parish

priest. The village church of field stone masonry, preserved to this day, stands in testimony to that time. The name of Pankow does not appear in official documents until 1311. The land register of Charles IV from 1375 already describes the place, complete with details on settlements and ownership. Yet the population made substantial gains only through the settlement policy of the Prussian Kings Frederic I and II in the 18th century. In 1910, Pankow already counted 45,000 residents. The town did not become a borough of Berlin until 1920, when it was incorporated together with the communities of Niederschönhausen, Rosenthal, Buchholz, Blankenfelde, and Buch.

A Piece of Prussian History

One of Pankow's culturally most precious monuments is Schönhausen Palace. It was built as residence for Countess Sophie Theodore Dohna-Schlobitten who acquired the lands of Pankow and Niederschönhausen in 1662. In 1664, she ordered the construction of a manor that was to become the centre piece of Schönhausen Palace. Over the years, the house experienced a history of shifting fortunes. In the 18th century, the palace changed hands and became the property of the Prussian crown. This era saw a steady expansion of the estate. Queen Elisabeth Christine, wife of Frederic II, had two wings added to the building in 1764, giving the palace its present-day appearance. With the formation of the Communist GDR, the estate became the seat of the President. Through 1960, the premises saw receptions of high-ranking visitors such as Ho Chi Minh or Nikita Khrushchev. In 2005, the palace was transferred into the portfolio of the foundation that manages the formerly Prussian palaces and parklands in Berlin and Brandenburg. Nearly nine million Euros have since been spent on the restoration of the palace, which is scheduled to reopen on December 19, 2009.



Schönhausen Palace

Berlin's Oldest Beer Garden

If you are looking for conviviality and shade beneath the canopy of ancient chestnuts in the summertime, you ought to pay a visit to the Prater. This, Berlin's oldest

beer-garden, owes its name to its location along Kastanienallee. When the Prater opened for business in 1837, the tree-lined street was little more than a dirt road fringed by meadows. The name's etymology suggests as much, pointing to the Latin word for meadow – "pratium."



Berlin's Prater

However, the history of the Prater does not start for good until the acquisition by one Johann Friedrich Adolph Kalbo on 1852. At the time, Berlin was transforming from a residential town into an industrial and labour metropolis. Recreational venues such as the Prater became increasingly important in line with this development. It was for this reason that Kalbo applied to the Chief of the Royal Prussian Police for a license to stage "amusements." With its summertime garden stage, the Prater began to contrast favourably against ordinary beer gardens. Once the buildings had been expanded, the venue also offered amusements during the cold season. Following the reunification of Germany, the Prater was closed down because of structural defects in 1991. Having undergone extensive redevelopment, it celebrated its grand reopening in 1996. Today, the beer garden opens at noon every day between April and September, weather permitting.

Cultural Arena in Central Location

Home to the Max-Schmeling-Halle, one of the largest arenas in the Berlin/Brandenburg region, Pankow is a

magnet for concert goers, The venue is located on the grounds of the Friedrich Ludwig Jahn Sportpark. Max-Schmeling-Halle opened to the public in 1997, having taken four years to build and 100 million Euros in investments. It seats an audience of 11,900 maximum. To satisfy the spatial needs of various kinds of events, the hall can be divided into smaller segments. From seven fitting room for artists and the Albatros restaurant, to the 400 sqm dance hall, all the way to its VIP lounge, Max-Schmeling-Halle provides everything a modern venue is expected to have. Its flexibility makes the hall eligible for any number of events, including sporting events such as handball, boxing, dirt bike trials, as well as concerts, shows or gala events. In addition, Max-Schmeling-Halle hosts trade fairs, product presentations, or conferences. International stars like Madonna, Rod Stewart and Eric Clapton have played this venue. Its great connectivity to the public transportation network makes the arena easily accessible even for non-motorised visitors.



Max Schmeling Halle

Rent Levels Exceeding Berlin's Average

According to the 2009 Housing Market Report compiled by the Berlin-based housing company GSW and real estate service provider Jones Lang LaSalle, Pankow continues to report a growth in rent rates. On the whole, Pankow's average quoted rents of 6.45 Euros per

square metre slightly exceed the mean Berlin square metre rent of 6.35 Euros. Especially the mid segment reports an accelerated rise in rent rates. Less favoured locations, by contrast, show a decline in quoted rent rates. Very popular are inner-city locations, most notably those in the Prenzlauer Berg district around Kollwitzplatz. Attractive suburban locations in immediate vicinity of the Bürger- und Schlosspark in Pankow are equally popular among tenants. At the same time, large contingents of simple housing are found throughout the district.

Comparatively Low Housing Cost Load

While the 2009 *Marktspiegel* market report published by the IVD German Real Estate Federation projects but minimal increases for Pankow's prime locations during the next twelve months, green locations such as Niederschönhausen and Rosenthal will continue to show positive development. Similarly, the quarters around Helmholtzplatz and Arnimplatz as well as the Bötzow quarter keep manifesting a positive tendency. Despite the rent hikes, the rent level in the heart of the borough or in Weissensee still undercuts rent levels in the in-scene locations of Prenzlauer Berg by far. As Pankow has a large stock of affordable apartments, the average housing cost load per household remains substantially lower than in other boroughs. While the average tenant in Pankow spends 28.1 percent of the household purchasing power on housing, the figure in neighbouring Friedrichshain-Kreuzberg is 33.9 percent, for instance.

Rent Rate Potential through Demographic Growth

According to the demographic forecast of the Berlin Senate for Urban Development, the population of Pankow will increase by 12.6 percent before 2030. Compared to the rest of the city, this will make Pankow the fastest-growing borough for years to come. In absolute figures, the expected increase in population equals 40,000 new residents. Before this background, the coming years are very likely to drive up both the demand for housing and the quoted rent rates.

Apartment Buildings of the Month

Historic Stucco Beauty in Popular Kreuzberg Quarter



The property is located in a traffic-reduced side street in Berlin's Kreuzberg district between Kottbusser Damm and Urbanstrasse on the fringe of the Graefequarter. The street is characterised by its high share of historic buildings, and offers plenty of potential for development. The historic four-storey stucco building includes just one front building with altogether eleven rental units. The ground floor houses three small stores, the upper floors eight apartments.

Purchase price: 710,000 € plus 7.14% sales commission, yield rate: 6.7% TARGET

Attractive Residential/Business Estate in Berlin's Southwest



This residential compound is located in the southwest of Berlin in the borough of Steglitz-Zehlendorf. Surrounding residential structures present a well-maintained, quiet, and modern aspect. A ten-minute ride on the S2 and S25 urban mass transit lines will take you downtown to Potsdamer Platz.

The compound includes 14 buildings, six of which are townhouses. The buildings were raised in 1994/95 in three zoned areas on a 17,040 square metre plot subject to a ground lease. The floor space breaks down into 130 residential and 14 commercial units. Out of a total of 105 parking spaces, 93 are located in an underground car park, twelve in above-ground garages. The houses feature attractive floor plans and high-end fit-outs. All apartments come with balcony, patio or loggia, and are equipped with fitted kitchens, gas ranges, and high-quality flooring.

Purchase price: 18,000,000 € plus 7.14% sales commission, yield rate: 7.2% TARGET

Attractive Front Corner Building in Sought Location in Neukölln



The plot is situated in a quite residential neighbourhood near Sonnenallee in Berlin's borough of Neukölln. The retail infrastructure of the immediate vicinity features convenience goods stores. The prestigious corner building consists exclusively of residential rental units with no commercial space.

It includes two front buildings at right angle to each other, and a small side building. The house is accessed via three staircases and has two handsome entranceways with lavish stucco ornaments. The building includes a total of 36 apartments.

Sales price: 1,925,000 €, no sales commission, yield rate: 7.8% TARGET

Imprint

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