

Things remain interesting

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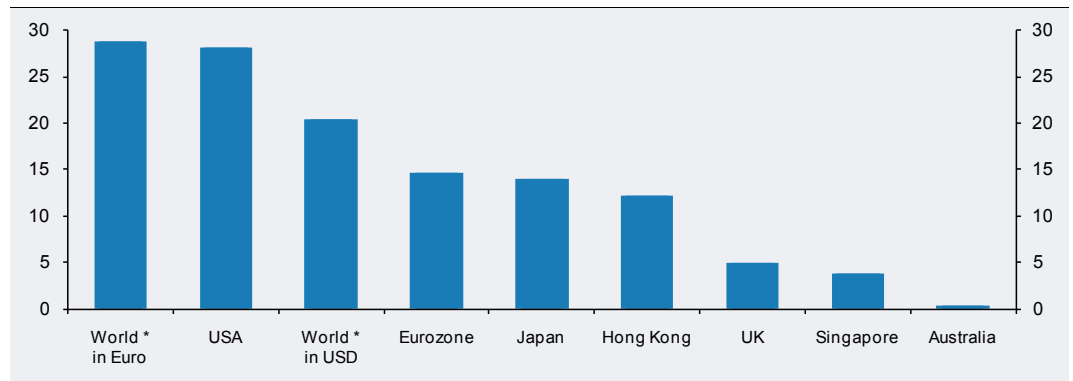
A continued recovery and the further unwinding of the consequences of the financial crisis will shape the international real estate markets in the new year (p. 2). Important decisions are pending for the open-ended real estate funds in Germany, since a regulatory change will take effect shortly (p. 3). Within the German construction sector, housing construction should develop best in 2011 (p. 4).

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1 At a glance

Good yearly performance of real estate stocks

FTSE EPRA/NAREIT real estate stock indexes in local currency, total return 2010 in %



Sources: Datastream, Helaba Research

* Developed World

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Real estate stocks posted a respectable performance last year. With a total return of nearly 29 %, the global real estate stock index of FTSE EPRA/NAREIT, calculated in euro, nearly equalled the good performance in the previous year (+34 %). However, the regional real estate stock markets showed highly divergent developments. In local currency, the US was at the top, the eurozone and Japan in the middle field. Hong Kong and Singapore were not able to follow up the very positive performance in the previous year. The British market, the largest within Europe and the one that has progressed the farthest in fundamental terms, disappointed with a total return of only 5 %. As the year before, Australian real estate stocks were at the bottom.

2 Selected Real Estate Analyses

Dr. Stefan Mitropoulos

2.1 Outlook 2011: a good year for real estate?

Last year brought a palpable recovery in the European real estate markets. The positive trends should continue in the new year, though without constituting a return to past boom times. Rather, dealing with the aftermath of the great financial crisis continues to be a dominant theme.

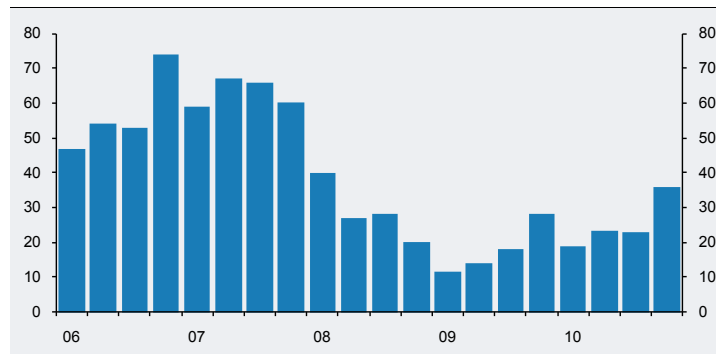
The sales figures for commercial real estate rose noticeably in Europe in 2010. A robust increase was recorded especially in the final quarter, thanks to a number of large transactions. Crucial were high liquidity and the great interest by investors in core real estate objects, but also the selling pressure of various market participants. The need for liquidity on the part of few open-ended real estate funds and a continued rise in the volume of refinancing reveal, however, that the processing of the financial crisis in the real estate sector is still ongoing. Even if the outstanding final quarter must not be projected forward, rising transaction volumes are likely for 2011. However, they remain a long way from those in the boom years 2006/2007.

Real estate markets
reflect fundamental
divergences

A continued positive trend can also be expected in the rental markets. However, great divergences in the economic fundamentals within the European real estate markets persist. Germany remains an economic engine with above-average economic growth, continued improvement in the job market, and a corresponding rise in demand for space in the office market. The outlook remains less favourable in Europe's problem countries, in which some drastic cuts in the public budgets and rising taxes are putting the brakes on overall economic growth and thus also on the recovery of the real estate market there.

Energetic close of the year in the European investment market

Transaction volumes of commercial real estate in Europe, billion Euro



Sources: CBRE, Helaba Research

The crucial question this year will be whether the gap between prime objects and less attractive property can be closed. In the wake of the financial crisis investors still have a strong need for security, as a result of which their focus is on the highest-quality real estate objects. However, now that the initial yields in this segment have already declined, investors should slowly engage also in riskier investments. Many institutional investors are planning to increase their real estate ratio in their portfolios this year – but that is only realistic if the fixation on core real estate is given up. At least compared to the main investment alternatives, real estate as an asset class is not unattractive at this time: the prospects of further rises in stock prices are low, and in the bond market, as well, there are by now significant risks.

2.2 Setting the course for open-ended real estate funds

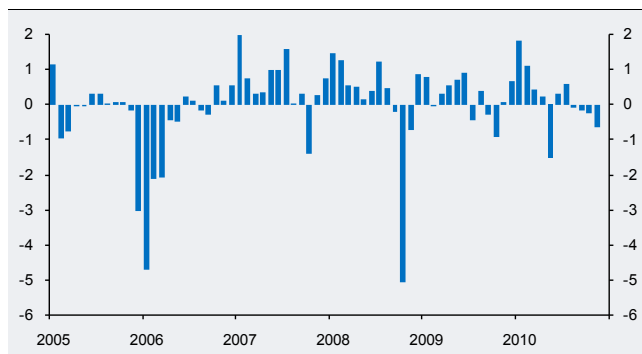
For open-ended real estate funds in Germany, 2011 could prove a fateful year. For the first time since this investment vehicle came into being, several problem funds are being liquidated. At the same time a regulatory change is coming, which will set the course for how attractive this real estate investment category will be to investors in the future.

2010 a bad year for open-ended real estate funds

Last year was not a good one for the open-ended real estate funds, which still play an important role in the German investment market with investment assets of more than 86 billion euros. Not only did a number of the more than 40 funds suspend the redemption of shares, three even decided to close down after the expiration of the two-year period. Further, in part substantial depreciations of the real estate portfolios led to a pronounced negative performance by some of the investment products. The result was that the average (not capital weighted) annual performance reported by the investment association BVI for the open-ended real estate funds of its member companies will show a negative value for the first time in 2010 – as of the end of November, average performance was down by 1.2 %. The outflow of capital from funds that are still redeeming shares has risen again slightly in the second half of 2010.

Rise in outflow of funds most recently

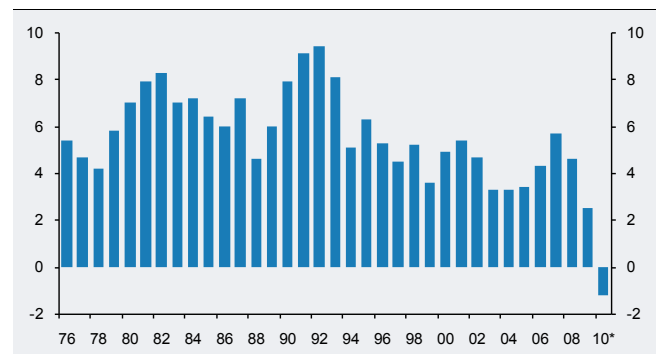
Monthly net inflow in billion euros



Sources: Datastream, Helaba Research

Yearly performance negative for the first time

% yoy



Sources: BVI, Helaba Research

* Yearly performance 2010 refers to November

Impending regulatory change

How will things unfold in the new year? Even though performance will presumably continue to remain low this year, the problems of various funds, who are confronted with depreciations – sometimes substantial – in their real estate portfolios, must not be transferred to all products in this asset class. The impending passage of the Investor Protection Act will finally bring clarity about the modalities of future redemptions and will make it easier to manage liquidity in the open-ended real estate funds. According to the most recent reports an agreement has now been reached within the governing coalition, one that is less restrictive compared to the original plans. Thus, the law now calls for only a one-year notice for the redemption of large sums for existing investors, and a minimum holding period of two years for new investors. However, private investors are to be given the right to withdraw up to 30,000 euro per half year from the funds. After the expiration of these periods, which will take effect in 2013, no redemption deductions are planned any longer. The funds can implement the regulations already in 2012. In addition, the share of debt financing is to be limited to a maximum of 30 % (previously: 50 %) beginning in 2014. The new regulations would strengthen the character of the open-ended real estate funds as a fairly stable and long-term real estate investment. We therefore assume that the fund category will remain in place as an important real estate investment in for private investors.

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2.3 German housing construction in an updraft

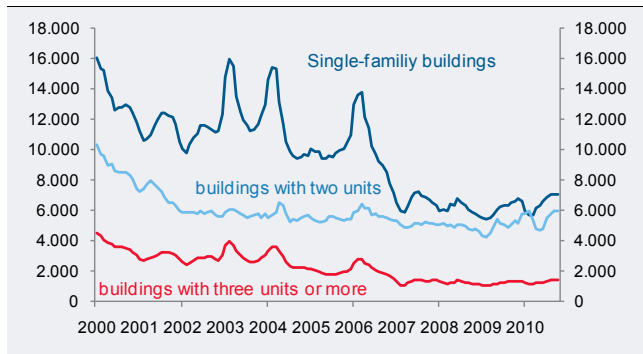
German housing construction posted above-average growth last year. A need for new, affordable housing exists especially in the important metropolitan areas. However, the biggest impulses are coming from renovation and expansion, especially for improvements in energy efficiency. Housing construction should expand moderately over the next few years.

Completions: rise from low level

German housing construction made a strong return in 2010 after three weak years. Investments in this sector rose by 4.4 % and thus more strongly than construction investments as a whole (2.8 %). The impulses came from both new constructions and renovations. Thus, building permits rose by an estimated 7 % to more than 190,000 units. Completions are also likely to have increased. However, at 170,000 units, the level is still extremely low. In fact, the West German lows from the eighties were undershot in 2009 with 159,000 units. And the current number of new constructions should also be barely enough to meet the demand. The number of households is still on the rise in Germany. Migrations from structurally weak regions demand new constructions in the mostly urban target regions. In addition, higher demands on energy efficiency are likely to lead in part to the demolition and rebuilding of structures if that proves to be the most economical solution. With that, the number of completions over the next few years should approach the level of 200,000. However, the structure of the new constructions will presumably change. The smaller household size is leading to a greater demand for condominiums and rental housing. The growth in the construction of single-family homes should lag behind. Thus, already last year the permits for residential buildings with three or more units showed the strongest growth at around 12 %.

Permits in Germany are increasing

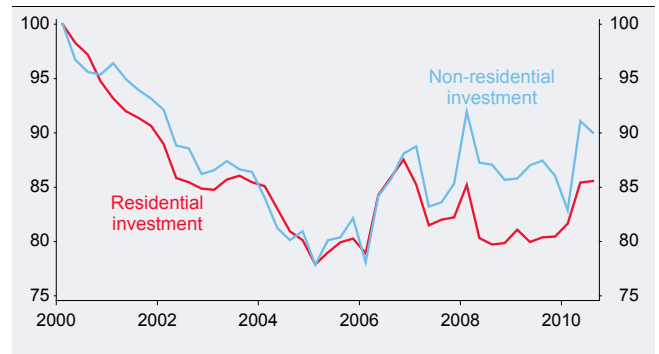
Thousands per month, seasonal adjusted



Sources: Feri, Helaba Research

Construction on the rise

Index: Q1 2000 = 100



Sources: EcoWin, Helaba Research

Renovation dominant

Most buildings, however, are capable of being renovated. The segment that benefits especially from this are companies in the renovation business, and their share of overall construction activity since 2000 has risen by 20 percentage points to now just under 80 %. Apart from high energy prices, governmental incentive programs are the driver behind this trend. Added to this are rising incomes and mortgage interest rates that were at historic lows until recently. Also, the uncertainty that increased with the financial crisis should have contributed to a more positive assessment of investments in real estate. Incoming orders in residential construction rose an estimated 9 % in 2010, much more robustly than in the construction industry as a whole (2.5 %). The chances for a positive trend this year in housing construction are therefore favourable. Investments in this most important sub-sector (57 % of overall construction investment), should grow at a rate of 2 % above the industry as a whole (1.5 %). The pent-up demand in the renovations sector and in part in new construction will continue to ensure moderate growth in residential construction also over the medium term. ■