

German economy

Slower pace of development

The German upturn has slowed significantly over the course of 2011. Gross domestic product was up only 0.1% in the last quarter. Forecasts for both this year and 2012 point to considerably reduced economic output.

Consumers in cautious mood

Reasons for this development include growing uncertainty among consumers vis-à-vis the crisis in the eurozone and the associated fall in consumer spending. In addition, higher energy prices – particularly for oil – are having an adverse effect on the German economy. Even exports have weakened massively due to the economic difficulties facing the country's trading partners. The debt crisis in Europe and the US is leading to a significant fall in demand around the world. The expectation is that exports will not show high rates of growth in future either because the global economic situation is under too much strain.

The sovereign debt crisis also poses new challenges for Europe as criticism of the various bail-out funds becomes increasingly vocal. The core of the problem – highly indebted countries – is not being solved, and instead the problems are being kicked into the long grass.

Debt crisis squeezes German exports

This is compounded by the fact there has been a slowdown in economic growth in the emerging-market countries – and this will also affect the development of German exports.

Germany: Key indicators and change from last year

Population (2011, Q2)	81,600,000	↘
GDP growth (2011, Q2)	+0.1%	
GDP growth (2010)	+3.6%	
GDP forecast (2012)	+2.3%	↘
GDP per capita (2010, EUR)	30,554	↗
Unemployment rate (08/2011)	7.00%	↘
Total employment (06/2011)	28,394,600	↗
Share of service employment (08/2011)	71.87%	↗
Disposable household income (2011, EUR)	40,537	↗
Inflation (07/2011)	2.60%	↗
Average mortgage interest > 5 years (06/2011)	4.58%	↘
10-year federal bond yield (08/2011)	2.30%	↘
3-month Euribor (08/2011)	1.55 %	↗
5-year euro swap rate (09/2011)	1.99%–2.03%	↘
10-year euro swap rate (09/2011)	2.66%–2.70%	↘
Change in consumer sentiment index (08/2011)	-0.1	
Change in Ifo Business Climate Index (08/2011)	-2.6%	
Change in retail turnover, real (07/ 2011)	-0.40%	

Office market

Significant rise in turnover

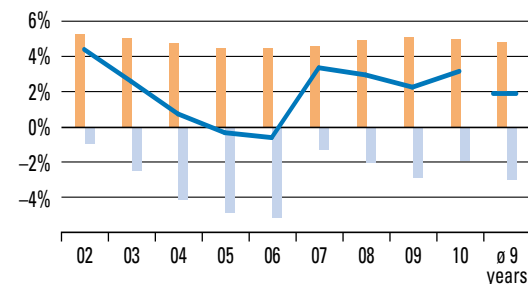
The German office market continued to gain momentum in the first half of 2011, with turnover in key office centres rising nearly 20% from the previous quarter's level.

Good prospects for 2011

The positive economic developments seen in the first half of 2011 were also reflected in the behaviour of office-space users. They are now more prepared to pay significantly higher prices for good to very good locations. Analysis of prime rents in the top seven markets shows clear growth in the first six months of the year. On the other hand, average rents remained stable. Vacancies fell significantly in some cases in parallel with the upward movement in prime rents in the individual office markets.

It should also be noted that the office market continued to become more attractive from an investment perspective. In the cities of Munich, Frankfurt, Stuttgart and Hamburg, office space was the most important type of property for investors in the first half of the year. This trend is also reflected in the continued fall in prime yields.

Returns: office market



— Total return
 ■ Income return
 ■ Capital growth
 Source: IPD

	Office Stock (m ² , 2011, Q2)	Employment (2010, Q4)	Vacancy rate (2011, Q2)	Average rent (EUR/m ² , 2011, Q2)	Prime rent (EUR/m ² , 2011, Q2)	Prime yield (2011, Q2)
Berlin	17,640,000	1,142,302	8.2%	12.2	21.0	5.1%
Munich	19,750,000	698,572	8.8%	14.5	30.0	4.8%
Hamburg	13,550,000	832,716	8.7%	13.6	23.0	4.9%
Cologne	7,430,000	473,261	9.0%	14.5	21.1	5.5%
Frankfurt	11,730,000	495,366	15.3%	19.4	34.8	5.1%
Dusseldorf	8,050,000	364,788	11.9%	13.9	23.2	5.2%
Stuttgart	7,910,000	347,390	6.6%	11.8	18.1	5.3%

Retail market

Positive development

Germany's positive economic performance also had a clearly positive effect on the retail market.

In the first half of the year, nearly EUR 6.2 billion (55%) of the investment volume went to the retail asset class. As well as shopping centres, investors focused on retail warehouses and retail parks in the first half of the year.

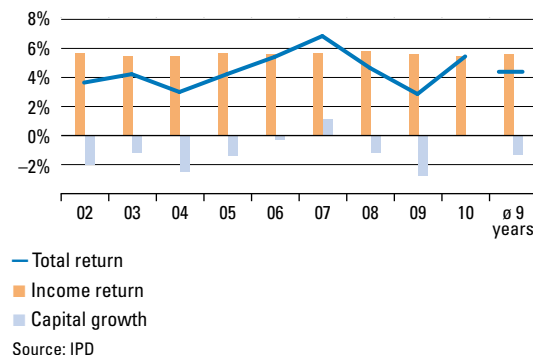
Mainly foreign investors

Given the stable economic situation thus far, foreign investors became increasingly interested in German retail properties (portfolios and individual properties). German investors also preferred commercial property with retail use, though their share is significantly lower.

Further fall in prime yields

Prime yields for shopping centres continue to harden due to very high demand from investors. As this demand continues unabated, many investors have been prompted to consider investments in large and even medium-sized towns alongside purchases in the main cities.

Returns: retail market



	Retail Stock (m ² , 2010)	Purchasing Power Index (2010)	Retail Centrality Index (2010)	Average rent (EUR/m ² , 2011, Q2)	Prime rent (EUR/m ² , 2011, Q2)	Prime yield (2011, Q2)
Berlin	4,560,000	93.9	108.6	109.0 ↗	240.0 ↗	4.7% ↘
Munich	1,570,000	126.3	119.9	137.0 ↗	320.0 ↗	4.1% ↘
Hamburg	2,500,000	105.4	115.4	154.0 ↗	240.0 ↗	4.4% ↘
Cologne	1,550,000	108.1	125.9	113.0 ↘	240.0 ↗	4.5% ↘
Frankfurt	1,290,000	111.7	111.9	119.0 ↘	270.0 →	4.4% ↘
Dusseldorf	840,000	115.6	125.4	132.0 ↗	240.0 ↗	4.5% →
Stuttgart	880,000	109.6	125.9	127.0 ↘	250.0 ↗	4.6% ↘

Residential rental properties

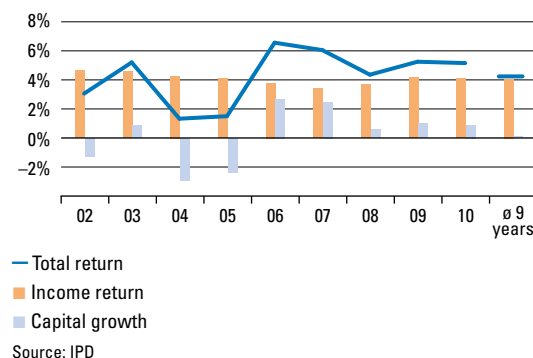
High demand for residential investments

Demand for residential investments continued unabated in the second half of the year. As it is difficult for supply to keep pace with demand, purchase prices for residential investments have continued to rise and prime yields are still falling.

New rented housing set to increase

Due to rising rent levels, investment in the construction of new rented housing is also becoming increasingly attractive. The appeal of building new housing is growing, particularly in light of the expected future cost burden associated with older residential properties and essential refurbishment to improve energy efficiency, as well as with creating flexible, barrier-free living space. It is virtually impossible for most existing properties to be adapted to these twin requirements – even with substantial investment. In overall terms, new residential buildings consequently – on a long-term view – now achieve yields that the sustainability assessment shows to be close to the initial yields on older properties.

Returns: residential market



	Stock (2010)	Residents (2010)	Population growth (2010)	Building activity (2010)	Average rent (EUR/m ² , 2011, Q2)	Prime rent (EUR/m ² , 2011, Q2)	Prime yield (2011, Q2)
Berlin	1,898,807	3,460,725	0.13%	0.23%	6.6 ↗	12.7 ↗	4.8% ↘
Munich	750,512	1,382,273	3.75%	0.34%	12.0 ↗	18.9 ↗	4.2% ↘
Hamburg	893,495	1,786,278	0.13%	0.34%	9.8 ↗	17.1 ↘	4.4% ↘
Cologne	539,730	1,027,504	2.86%	0.51%	8.5 ↗	13.5 ↗	4.8% ↘
Frankfurt	360,234	688,249	2.37%	0.75%	10.8 ↘	18.0 →	4.4% ↘
Dusseldorf	332,271	588,169	0.33%	0.29%	8.2 ↗	14.6 ↗	4.5% ↘
Stuttgart	298,307	577,353	-4.21%*	0.52%	9.2 ↗	14.4 ↗	4.6% ↘

* Due to the introduction of a secondary home tax at the beginning of 2011, currently a major cleanup of the civil registry of the residents with secondary homes in Stuttgart is in place. This led to a statistical decrease of the number of residents.

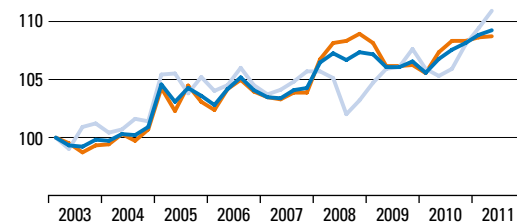
Owner-occupied housing

Increased demand

Demand for residential property continued to rise in the first half of 2011, resulting in further price growth and increased newbuild activity. The owner occupied market in Berlin in particular remains on a growth trajectory and in terms of prices is slowly catching up with other global cities.

There are essentially two reasons for this: first, newbuild was neglected for a period of several years; this is now reflected in supply being too limited in the desirable locations. Second, real estate is seen as one of the last safe investments. Increasing uncertainty among consumers with respect to future European and global economic developments on the financial markets is resulting in a veritable run on residential property. For many private individuals, there is growing anxiety about a decrease in the value of money and the purchase of property is seen as a secure investment.

Price indices for property purchased as own residence



— Owner-occupied housing
— Single-family houses
— Condominiums

Source: Verband deutscher Pfandbriefbanken (vdp)

	Average price (EUR/m ² , 2011, Q2)	Prime price (EUR/m ² , 2011, Q2)	Percentage owner-occupied (2010)	Single-/two-family houses (prime, EUR/m ² , 2011, Q2)
Berlin	1,818 ↗	5,600 →	14%	6,100 ↗
Munich	3,536 ↗	9,600 ↗	24%	10,700 ↗
Hamburg	2,614 ↗	8,000 →	22%	7,900 ↗
Cologne	1,800 →	5,300 →	25%	5,100 →
Frankfurt	2,547 ↗	7,800 ↗	16%	7,100 ↗
Dusseldorf	1,969 →	6,200 ↗	21%	8,300 ↗
Stuttgart	2,094 →	5,700 →	30%	9,300 →

Logistics properties

Further increase in turnover

Turnover was up again year-on-year in the first half of 2011 and is expected to exceed the 5-million-square-metre mark this year.

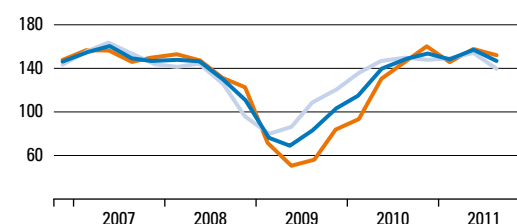
The rise in turnover is primarily attributable to the 5,000m²-plus category, which was up 37% compared annually.

Foreign investors are particularly attracted by the persistently favourable economic climate in Germany and the stability that investing in Germany has to offer. Unlike German investors, they are not focused solely on the premium newbuild segment.

Investors remain cautious

Despite strong manufacturing output, German investors remain cautious and are concentrating on high-quality investments with secure income flows at traditional locations. Yields have nevertheless hardened across the board.

Logistic indicator



— Climate
— Current situation
— Expectations

Source: Dr. Stefan Kooths, Prognose-Zentrum

	Stock (m ² , 2010)	Land price (EUR/m ² , 2011, Q2)	Average rent (EUR/m ² , 2011, Q2)	Prime rent (EUR/m ² , 2011, Q2)	Prime yield (2011, Q2)
Hamburg	2,650,000	250 ↗	4.5 →	5.9 →	7.1% ↘
Frankfurt	2,300,000	225 →	4.3 →	6.3 ↗	7.0% ↘
Rhein/Ruhr	2,700,000	85 →	3.4 →	7.5 →	7.4% ↗
Berlin	2,150,000	110 →	4.0 ↗	5.3 ↗	7.5% →
Munich	1,400,000	250 →	5.5 →	6.5 →	7.1% ↘
Dusseldorf	970,000	140 ↗	4.1 →	5.7 ↘	7.4% →

Focus on the hotel market

Hotel investments attractive again

The onset of the financial and economic crisis was accompanied by a significant decline in the hotel investment sector. Hotel performance was significantly weakened by the crisis, resulting in falling hotel property values. Hotel performance has since improved thanks to the economic upturn, and an increase in investment activity was recorded in 2010.

Distressed sales continued to fall in 2010 from the levels seen in 2008 and 2009. This development was primarily attributable to the hotel industry's rapid recovery from the crisis, mainly thanks to a reduction in value added tax from 19% to 7%.

The biggest share of transaction volume in 2010 was in mid-range hotels, in the three and four-star sector. Totaling around EUR 500 million at the year-end, they exceeded the one and two-star hotels in the budget sector (EUR 280 million). Turnover in the 5-star luxury hotels segment in 2010 amounted to approximately EUR 130 million. The bulk of the transaction volume in 2010 flowed into the top seven locations: Berlin, Dusseldorf, Frankfurt, Hamburg, Cologne, Munich, and Stuttgart.

Trends in the hotel market

According to the German Hotels Association (DEHOGA), the following trends can be observed in the German hotel sector at the moment:

Cut-throat competition at the expense of mid-range hotels and non-branded, imageless hotels continues with the construction of new capacity. Clear positioning is therefore more important than ever.

City tourism – which includes conferences and conventions as well as cultural and sporting highlights – has major growth potential. According to DEHOGA, Berlin – along with Hamburg and Munich – is among the top three city destinations in Germany. In terms of overnight stays, Berlin now ranks fourth in Europe (after London, Paris and Rome) at 20.8 million.

As a future megatrend, health and wellness is likely to be the biggest winner in terms of market significance and influence over the next few years.

In view of demographic change, it is important to increasingly develop offers for keen travellers who are over the age of 60 but young-at-heart.

Selected transactions 2011

	Rooms	Price (\$)	Price/Room (\$)	Hotel	Location
January	128	26,781,000	209,227	Citadines Apart Hotel	Hamburg
January	322	79,673,475	247,433	Steigenberger Airport Hotel	Berlin
April	165	39,652	240,316	Citadines at Europaviertel	Frankfurt a. Main
May	142	37,009,999	260,634	Hotel Pestena	Berlin
June	177	98,047,729	553,942	Grand Spa Resort A-Rosa	Sylt
July	436	144,907,323	332,356	Radisson SAS Blue Heaven	Frankfurt a. Main

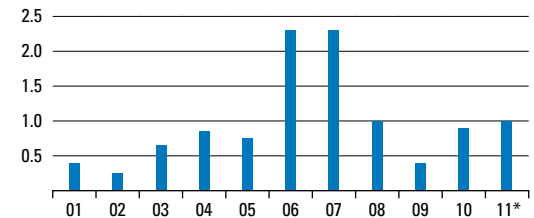
Low point seems to have been overcome

Distressed sales continue to fall

Transactions mainly at the top seven locations

Branding development increasingly important

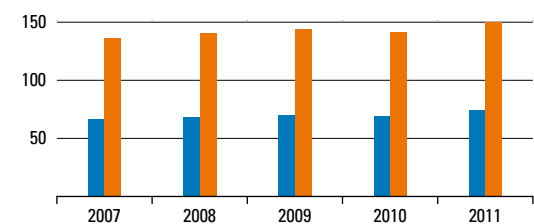
Hotel investment in Germany (in Bn. EUR)



* 1st half-year

Source: JLL Hotels

Tourist arrivals and overnight stays in Germany (in Mio.)



■ Arrivals

■ Overnight stays

Source: Bundesamt für Statistik

An important sector **Accommodation services in Germany**
 The overall accommodation services sector in Germany is an important economic factor with a total 54,822 businesses and 509,627 employees. Within accommodation services, there is a huge spectrum of business types such as hotels, guest houses, youth hostels, holiday homes, campsites, preventive clinics and rehabilitation centres. In Germany, nearly one quarter of all businesses in the accommodation services industry (24%) are categorized as hotels.

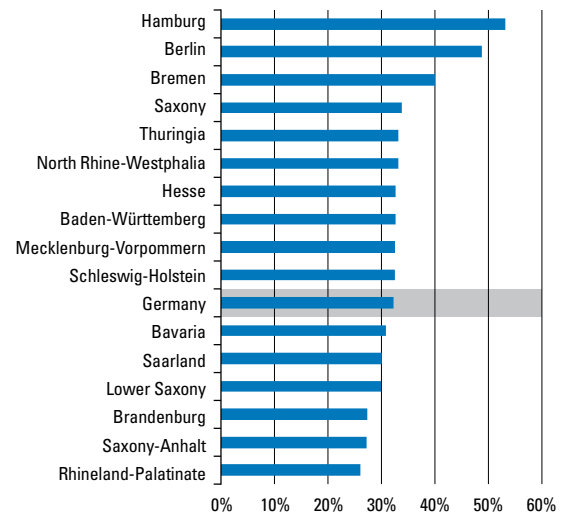
Slight rise in occupancy rates
 Average occupancy rates in the hotel sector have risen from 37% in 2004 to stand at nearly 38% currently; on the other hand, average occupancy rates in all accommodation service businesses fell by around 4% in the same period. In addition, higher occupancy rates are generally achieved in hotels compared with other types of accommodation.

The demand situation has developed positively in recent years, with growth in the number of overnight stays in hotels rising by around 10% in the last five years. The average length of stay was almost unchanged during this period at 2.0 days.

Positive demand trend **Development of demand and turnover**
 Following a sharp decline in demand in 2002 and 2003 as a result of September 11, 2001, net turnover in the German hotel sector began to develop positively. However, the hotel trade is highly cyclical and was therefore badly affected by the financial and economic crisis in 2009. The German hotel industry recovered again in 2010, however, and was almost back to its pre-crisis level of 2008.

Room rates higher in all regions
 According to the German Hotels Association, average room rates in the German hotel market rose 12.6% last year to EUR 90. Significant price increases for hotel rooms were recorded again in all regions in 2010. Room rates increased most significantly in small German cities, where there was a rise of 14%. The revenue situation also developed positively again last year. Figures from the German Hotels Association show clearly that average revenue per room in the German hotel market rose 19% to EUR 57 per room, thus taking it back to the level of 2008.

Average occupancy rate by state (2009)



Source: Statistisches Bundesamt

Average room rate (2010)

	Room rate (EUR)	Change (2009-2010)
Germany	90	13%
Major cities	97	12%
Medium sized towns	79	13%
Small towns	76	14%
Airport hotels	87	13%
5 star	138	12%
4 star	82	12%
3 star	61	12%
1-2 stars	59	10%

Source: IHA

**Investment volume in 2011:
EUR 1 billion**

Outlook

The volume of investment is expected to be higher in 2011 than in 2010. The figure for 2011 is likely to return to the level of 2008, meaning an investment volume of EUR 1 billion. The increasing number of projects that have already found a buyer prior to completion is a clearly positive sign and an indication of growing confidence in the hotel asset class.

At EUR 335 million for a total of eight transactions, the investment volume for individual deals in the first half of 2011 was around three times higher than the figure for the first six months of 2010. The three largest individual transactions accounted for around two-thirds of the volume.

**Luxury segment
more attractive again**

The share of the 5-star luxury segment in total transaction volume in the first half of 2011 was also significantly above the overall figure for the previous year at around EUR 175 million.

Broad spectrum of investors

While the hotel investment market continued to be dominated by international investors in the first quarter, domestic investors raised their share of the volume of transactions from less than 20% in the first quarter to a figure of nearly one third in the first half of the year as a whole. A German closed-end real estate fund paid nearly EUR 71 million for the 177-room Grand SPA Resort A-Rosa Sylt in List. Together with the sale of the Radisson SAS Blue Heaven, this represented one of the biggest individual transactions so far this year.

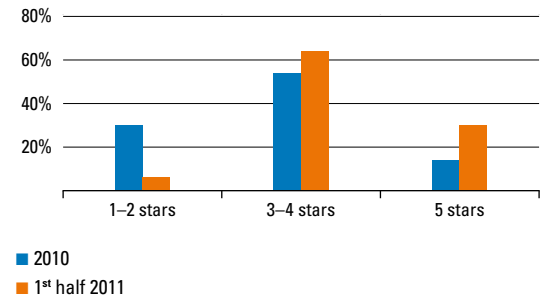
The buyer mix is once again characterized by a broader spectrum of investors, though the majority continue to comprise institutional investors seeking to generate stable yields. These investors are complemented by wealthy private individuals interested in exceptional hotel properties. Despite the stable market situation and positive economic trend, the lease agreement remains the priority from a buyer's perspective, as it offers greater security compared with a management contract. In addition, lease agreements provide tax advantages for investors.

Due to the rise in demand and fairly limited supply in the safe core segment, a further hardening of yields and rise in property values is expected in 2011.

Falling yield expectations

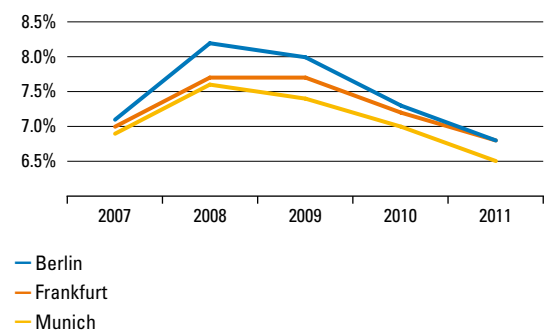
Having averaged around 7% in 2007, the net initial yield increased significantly during the years of the financial crisis. The decline in revenues described above had a clear impact on the development of yields. In both 2010 and 2011, net initial yields have hardened significantly and now stand between 6.5% and 6.8%. It remains to be seen how current developments on the financial markets will affect the hotel trade.

Hotel investment in Germany 2010 and 2011 by segment



Source: Colliers Hotels

Net initial yield for mid-class hotels in Germany



Source: W&P Immobilienberatung GmbH

International prime rents

		Office (Local currency / m ² p. a.)	Office (EUR / m ² p. a.)	Retail (Local currency / m ² p. a.)	Retail (EUR / m ² p. a.)	Exchange rates (EUR, March 2011)
Europe	Amsterdam	350 EUR →	350 →	2,800 EUR ↗	2,800 ↗	1.00
	* Budapest	240 EUR →	240 →	1,200 EUR →	1,200 →	1.00
	Brussels	300 EUR →	300 →	1,630 EUR →	1,630 →	1.00
	Copenhagen	1,770 DKK →	240 ↗	16,460 DKK →	2,200 ↗	0.13
	Frankfurt	460 EUR ↗	460 ↗	3,240 EUR →	3,240 →	1.00
	Helsinki	315 EUR ↗	315 ↗	1,920 EUR ↘	1,920 ↘	1.00
	London	1,040 GBP →	1,200 ↘	6,500 GBP →	7,490 ↘	1.15
	Madrid	320 EUR ↘	320 ↘	2,400 EUR →	2,400 →	1.00
	* Moscow	840 EUR ↗	840 ↗	3,340 EUR ↗	3,340 ↗	1.00
	Oslo	3,580 NOK ↗	460 ↗	16,000 NOK ↗	2,040 →	0.13
	Paris	780 EUR ↗	780 ↗	9,200 EUR ↘	9,200 ↘	1.00
	* Prague	250 EUR →	250 →	2,040 EUR ↗	2,040 →	1.00
	Rome	450 EUR →	450 →	3,500 EUR →	3,500 →	1.00
	Stockholm	4,350 SEK ↗	470 ↘	14,300 SEK →	1,550 ↘	0.11
	Vienna	280 EUR ↗	280 ↗	3,000 EUR →	3,000 →	1.00
	* Warsaw	310 EUR ↗	310 ↗	1,000 EUR →	1,000 →	1.00
	Zurich	1,100 CHF ↗	900 ↗	8,500 CHF →	7,080 ↗	0.82
America	** Buenos Aires	380 USD ↘	280 ↘	1,010 USD →	750 →	0.74
	** Mexico City	280 USD ↘	210 ↘	540 USD →	400 →	0.74
	New York	660 USD →	490 ↘	22,340 USD →	16,610 →	0.74
	São Paulo	1,440 BRL ↗	580 ↘	2,050 BRL →	830 ↘	0.41
	Toronto	280 CAD →	200 ↘	3,500 CAD ↗	2,520 →	0.72
Asia	Hong Kong	13,800 HKD ↗	1,320 →	139,960 HKD ↗	13,350 ↗	0.10
	Mumbai	44,400 INR ↗	730 ↗	59,500 INR →	890 ↗	0.02
	Seoul	558,100 KRW ↗	350 ↘	4,750,000 KRW →	2,960 ↘	0.001
	Shanghai	4,200 CNY ↗	490 ↗	21,360 CHN →	2,480 ↘	0.12
	Singapore	1,090 SGD ↗	620 ↗	4,910 SGD →	2,920 ↗	0.57
Tokyo	103,670 JPY ↘	1,010 →	791,970 JPY →	7,700 →	0.01	
Australia	Sydney	720 AUD ↗	520 ↗	10,180 AUD ↗	7,380 ↗	0.73
Africa	Johannesburg	1,440 ZAR ↗	130 ↘	5,070 ZAR →	460 ↘	0.09

* Many rental agreements denominated in EUR.

** Many rental agreements denominated in USD.

Sources This market survey is based on a broad internal data pool. It also draws on data provided by the following public and private sources: Federal Statistical Office, Federal Office for Transport, Building and Urban Development, GFK, and the market reports of various brokers (CB Richard Ellis, Jones Lang LaSalle and Cushman & Wakefield). All data on returns is supplied by IPD.

Notes Rents: EUR per square metre and month for the German data; in local currency per square metre and year for the international data.
Yields: net initial yield per year (cash flow before capex/price).
Building activity: new-build residential properties (last 12 months) as a share of total stock.
The arrows in the property market summaries show changes over the previous half year.

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