Press release

2019 Irebs German Debt Project study:

“Margins finally rising but by far not everywhere”

- The volume of new business has stabilised at last year’s value; the volume of loans has risen slightly against a downward trend in non-scheduled repayments.
- Loan-to-value ratios (LTV) have stabilised at last year‘s comparatively low level (63%). Although there has been a drop in loan-to-value ratios in low-risk financing in particular, with commercial property prices rising steeply, the ratios have risen in price-adjusted terms.
- Commercial property financing margins have bottomed out; residential property financing margins are currently in decline. At the same time, the competition has shifted into the sphere of non-monetary contract terms (in particular covenants and maturities). More investors are demanding the extensive waiver of covenants.
- Banks are increasingly pursuing more sophisticated financing (e.g. niches, operator-run properties, foreign investments, value-add investments and project developments), in order to avoid margin pressure.
- The market climate, with a marked rise in land and construction costs and intensive competition between banks, is raising the pressure to consolidate both among project developers and financial service providers.
- Syndications for risk-diversification are on the rise.

Eltville, 19 September 2019. The German Debt Project study of the International Real Estate Business School (Irebs) will be presented for the seventh time on Tuesday 24.9.2019 in Frankfurt by Prof Dr Tobias Just, (FRICS), Academic director of Irebs Immobilienakademie and professor for real estate at University of Regensburg, supported by the Association of German Pfandbrief Banks (Verband deutscher Pfandbriefbanken, vdp) together with distinguished representatives of the real estate sector.

The study provides detailed information on the commercial real estate financing market in Germany.

New business declined in 2017 and 2018 after six very expansive years. At 8%, the overall rate of decline in 2018 was similar to that in 2017. However, savings banks and cooperative banks are under-represented in the portfolio analysed. As competition for market share among these banks is fierce, particularly outside the metropolitan regions where conditions are aggressive, some of the banks taking part in this GDP study are no longer able to hold their own in these segments of the market. Therefore it can be assumed that the decline in new business for Germany overall is lower than indicated here.

In 2019, the volume of new business in our analysed portfolio is stable at last year's level. With a decline in unscheduled repayments, the overall credit volume for 2018 grew by approximately 3.5% and is also set to increase in 2019, although somewhat more slowly. In the face of the price level achieved on most real estate markets – measured as multiples of attainable annual rent – stakeholders in the real estate market are increasingly struggling to turn over properties quickly.

In a persistently low interest-rate environment, many banks continue to attempt to keep their real estate business stable and in some cases even to expand it. The pressure of competition, in particular in the case of investments in existing properties, remains high. Although margins have at least stabilised for the majority of banks, a third of all institutions surveyed continue to report declining margins in 2019. Since 2013, net margins have fallen by more than 30 basis points (bp), on average. This decline however is calculated across all categories of property. Shifts between risk classes are therefore not mapped. For project developments, the pressure on margins has markedly reduced; a growing number of banks are reporting a moderate increase in margins, in particular for more complex financing.

As the margin level, in particular for low-risk transactions, is already very low at 50 to 70 bp, the competition is increasingly taking place in the context of non-monetary terms in particular in maturities and covenants. At the same time, the banks continue to seek reasonable margins by agreeing financing beyond purely core strategies. This might include financing for niche products and operator-run properties, project developments or undertakings abroad. Real estate with appreciation potential too, i.e. vacant properties or properties in need of refurbishment, as well as properties in peripheral locations, are being financed more frequently, as in 2018, in order to circumvent the very low margins in plain vanilla business. In this light, the stabilisation of margins is no all-clear of relieving pressure.

At the same time, it remains true that the favourable market position has helped to improve ratings for bank portfolios by and large, and risk provision is declining once more. The market in non-performing loans therefore remains flat. The cautiousness of the banks is also expressed in a starker differentiation between individual asset classes: over the past 18 months, office property has made some of the strongest gains; residential property continues to be regarded as a safer haven. Willingness to finance logistics premises also remains high; although personal interviews have revealed some initial doubts as to whether the massive drop in rental income from logistics property can be justified in view of the economic slow-down. Overall, retail properties are perceived to be the most critical; yet two pronounced distinctions can be drawn here. Firstly, retail parks and prime inner-city locations are valued significantly more highly than urban district locations and simple shopping malls and, secondly, some bank representatives have expressed an assumption that the punishment of the retail asset class might have already gone too far. In addition to the more pronounced distinction between asset classes and deliberate risk-taking in niche markets, most banks have developed a syndication strategy in order to reduce specific property risks by associated opportunities for diversification.

None of the banks participating in the survey currently hold on to the concerns expressed in recent years that, in a phase of increasing interest rates, significant upheavals may occur on the real estate market and therefore also on the real estate financing market. Continuous rises in interest rates are not expected in the coming years. However, the drastic decline in rental income implies that financing with very low repayments in the core segment is increasingly forcing shareholder equity to ensure that debt servicing remains manageable. Accordingly, concerns surrounding economic downturn have superseded the fear of interest rate rises, especially as the geopolitical situation is assessed as fragile, and overestimations are being openly addressed in the markets. Simon Mallinson of Real Capital Analytics remarks in this regard, “The volume of transactions in Europe fell in the first half of 2019. The German market however is in a relatively good position with a decline of (only) 12% and is currently the strongest market in Europe. Good properties are still in demand as international investors continue to want to strengthen their allocation in Germany.”

As the other regulatory steps require somewhat higher margins, the pressure to consolidate among the banks – especially in standard business – is only set to increase. The majority of the banks surveyed consider the risks that have been identified on the real estate markets so far to be manageable in principle. They do not expect any serious collapses in demand, but they are conscious of a sustained level of uncertainty. According to Prof Dr Tobias Just, “In this context it would be appropriate not to unsettle the real estate market stakeholders by regulatory actionism as, with the rental incomes being achieved, even slight changes in stakeholders’ expectations may lead to severe effects on prices“.

About the German Debt Project study

The German Debt Project study was initiated by the market research and consultancy company Real Capital Analytics, and has been supported from the start by the Association of German Pfandbrief Banks (Verband deutscher Pfandbriefbanken). Twenty-four German financial institutions have taken part in the survey. The credit volume analysed in the context of the study is € 93 billion. The objective of the study is to increase transparency in the German commercial real estate financing market and to enable meaningful comparisons, in particular in risk analysis. The study was carried out for the first time in 2013.

The sponsors of the study, in alphabetical order, are bulwiengesa, Commercial Real Estate Finance Council Europe (CREFC), Greenberg Traurig, JLL and the Central Real Estate Committee (Zentrale Immobilien Ausschuss, ZIA). The project manager with academic responsibility is Prof Dr Tobias Just of Irebs. The study’s co-author is Simon Wiersma of the Real Estate Faculty of the University of Regensburg. The Association of German Pfandbrief Banks (Verband deutscher Pfandbriefbanken, vdp) has supported the study.

The German Debt Project website

The study can be purchased for € 450 exclusive of VAT on the www.irebs-immobilienakademie.de/shop/publikationen/studie-german-debt-report-2019 website. Older studies can be found at www.german-debt-project.de.

About the Irebs Real Estate Academy

The Irebs Real Estate Academy is the further training academy of the Irebs International Real Estate Business School, and part of the Faculty of Economics of the University of Regensburg. The International Real Estate Business School comprises the Irebs Institute of Real Estate Economics and the Irebs Real Estate Academy. The Irebs Real Estate Academy offers professional development courses for management, junior management and specialist staff. In addition to real estate, construction and financial management companies, the study is designed for use by industrial, commercial and service companies as well as the public sector.

The Irebs Real Estate Academy has been certified by TÜV Hesse to ISO 29990 as a provider of education and further education. The seal guarantees students that the services of the Irebs Real Estate Academy are designed on the basis of employment market requirements and are continuously being developed.

The contact course on Real Estate Economics and the excellence course for the Executive MBA Real Estate at the Irebs Real Estate Academy have been accredited by the prestigious Royal Institution of Chartered Surveyors (RICS). Further information is available at www.irebs-immobilienakademie.de/en.

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