RESEARCH

Knight Frank

GERMANY

OFFICE MARKET OUTLOOK

Q1 2015

OCCUPIER TRENDS | INVESTMENT TRENDS | MARKET OUTLOOK

KEY FINDINGS

Prime office rents generally remained constant in Germany's main cities during 2014

A lack of prime CBD space in major cities is forcing occupiers and investors to move further out-of-town

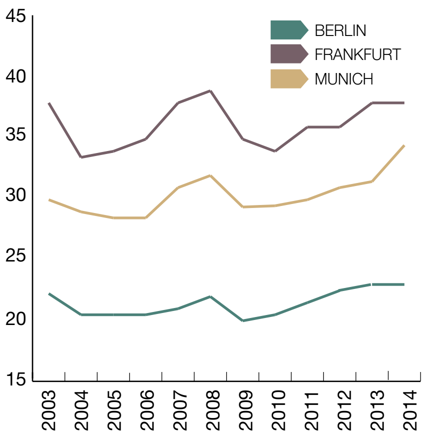
Vacancy rates are falling mainly because offices are being withdrawn from the market for change of use to residential or hotel purposes

In Germany's top five cities, offices accounted for around 30% of commercial investment volumes in 2014

FIGURE 1

Prime office rents

€ per sq m per month



Source: Knight Frank Research

OCCUPIER MARKET

While growth has slowed, relative economic stability has supported a strong level of occupier activity around the country, although trends have varied between the major cities.

The continued demand for office space in Munich has meant that rents have risen again by €3 to €34.50 per sq m per month – the highest annual increase of the top five cities. Munich has outperformed largely because of the diversity of its occupier base compared with other cities such as Frankfurt, where the banking and financial services sector accounts for over 30% of the market.

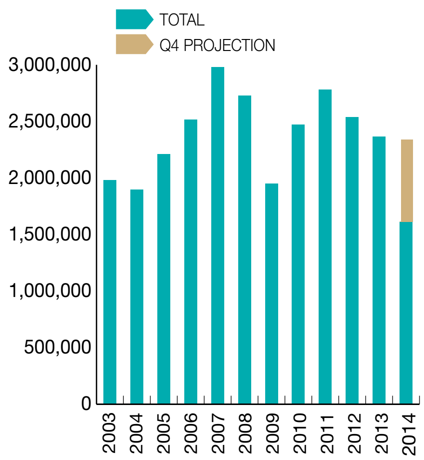
In 2014, office rents saw minimal change in Hamburg and no movement in Berlin, Düsseldorf and Frankfurt, despite a decline in market sentiment earlier in the year. A number of offices with change of use potential were removed from the Berlin market, reducing the vacancy rate by 40 bps to 8.4% in the final quarter. With demand for office space relatively high in the capital, buildings are unlikely to stay vacant for long. Frankfurt experienced the largest fall in the vacancy rate (from 11.4% in Q4 2013 to 10.7% in Q4 2014), although the rate is still highest (in relative and absolute terms) of the major German cities.

As at Q3, overall office take-up in the top five was down by 1.2% on twelve months earlier, with individual markets showing significant changes. Frankfurt experienced the biggest fall, with take-up in Q1-Q3 totalling 263,800 sq m, down 19.3% on the same period in 2013. This is mostly due to a fall in the number of large units available – most of the space available to rent is below 1,000 sq m. Despite this, take-up is forecast to be in the region of 450,000 sq m for the whole year. Berlin, meanwhile, saw take-up increase by 24.4% for the first nine months of the year, owing to a number of large (10,000 sq m+) leasing transactions, enabling the city to achieve take-up levels close to the highs of 2011 and 2012. Despite a 9.6% fall in take-up, Munich continues to be the market leader, with take-up for the first nine months of the year close to 400,000 sq m, which should mean a full year total of approximately 600,000 sq m.

FIGURE 2

Top five cities total office take-up

sq m



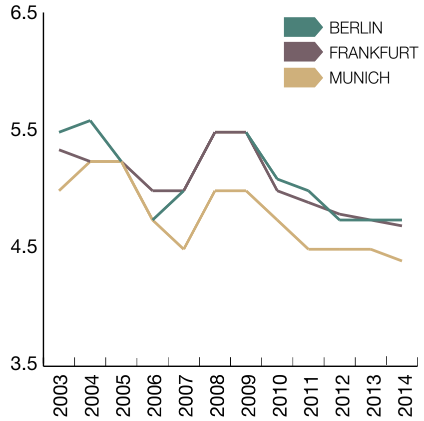
Source: Knight Frank Research

Key office leasing transactions in 2014

Quarter	Property	Tenant	Size (sq m)
Q2	Hamburg	Deutsche Telekom AG	32,200
Q1	Frankfurt	DWS - Deutsche Asset & Wealth Management	32,000
Q1	Munich	Brainlab	21,300
Q1	Berlin	Idealo Internet GmbH	10,500
Q3	Düsseldorf	MFI Management fur Immobilien AG	5,000

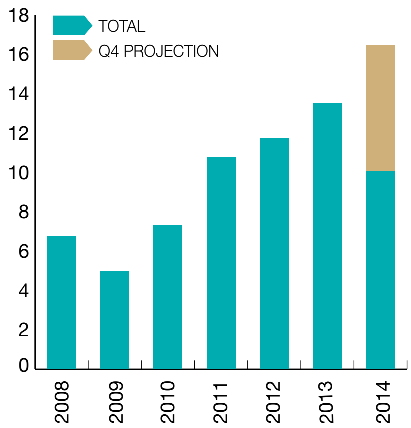
Source: Knight Frank Research

FIGURE 3
Prime office yields
%



Source: Knight Frank Research

FIGURE 4
Germany office investment volumes
€ billion



Source: Knight Frank Research / Real Capital Analytics

The Theresie building bought by Deka Immobilien for €257m in Q3 2014

INVESTMENT MARKET

During the first nine months of the year, offices accounted for approximately half of all commercial investment in Germany, followed by retail and logistics, which had market shares of 25% and 10% respectively. Office investment volumes for Germany totalled €10.1bn, with the CBDs in the top five cities accounting for €7.8bn. With the split between the sectors remaining unchanged, year-end transaction figures for German offices are expected to be in the region of €16.5bn, with deals in the top five cities projected to reach €11.8bn.

General trends in 2014 were similar to 2013, although actual transaction volumes for the top five cities are expected to be approximately €1.1bn higher once the data is finalised. A large number of portfolio deals contributed to this, notably the purchase of the mixed use PalaisQuartier portfolio in Frankfurt in Q4 by Deutsche Bank, where the office element was valued at an estimated €350m. Other portfolio deals in 2014 included the acquisition of the An den Brucken portfolio for €155m by DekaBank in Munich in Q1. Such transactions helped Munich and Frankfurt to retain their positions as Germany's largest investment markets.

However, while the bulk of investment activity takes place in CBD locations, domestic and foreign demand has risen for higher yielding assets in secondary and out-of-town locations across the five major cities. In fact, yield differentials between in and out-of-town locations can be as much as 150 bps. Prime yields have shown little to no movement in the last twelve months. The largest shift occurred in Düsseldorf, where yields hardened by 20 bps to 4.7%, to reach the same level as Frankfurt.

Key office investment transactions in 2014

Quarter	City	Property name	Seller	Buyer	Confirmed price (€)
Q3	Munich	Theresie	Ivanhoe Cambridge	Deka Immobilien	257,000,000
Q2	Düsseldorf	Metro Group HQ	Metro	IVG Funds	200,000,000
Q3	Hamburg	Tanzende Turme	Zueblin Development	Hansainvest	165,000,000
Q2	Berlin	Mosse Zentrum	DPGP	Real I.S. AG	91,500,000
Q1	Frankfurt	Europa Arkaden I	UBS	Schroders Prop Investment	16,200,000

Source: Knight Frank Research

KNIGHT FRANK VIEW

Together with the scarcity of good office space, continuing occupier demand is likely to put upward pressure on rents over the coming year, particularly in Frankfurt and Munich. As a result, these cities are expected to outperform in the short-term. Outside the top cities, however, rents are expected to remain relatively stable, which may encourage occupiers to look more closely at these locations.

While the short-term economic outlook is more uncertain, Germany will continue to remain a "power house" as Europe's second largest investment market. The market is considered a safe haven for buyers with its stable yields, steady rental growth and falling vacancy rates.

With many Q4 transactions awaiting confirmation, full year investment volumes for 2014 for the top five cities are expected to increase by as much as 10% on 2013. The recent acquisition of the IBC buildings in Frankfurt by US firm RFR Holding will contribute a reported €300m to the final total. German investors accounted for about half of all office transactions in the five cities in 2014, although Berlin is seeing more international interest. However, over the coming months, we expect international investors to focus increasingly on second and third tier cities where rental growth has yet to re-emerge.

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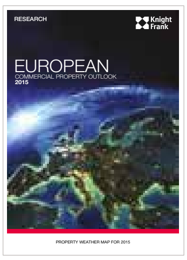

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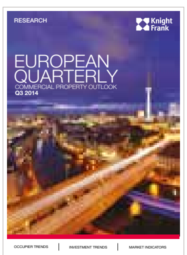

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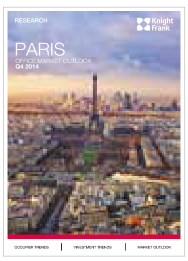
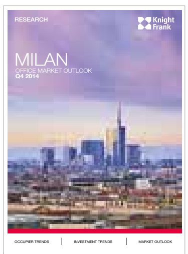


Paris Office Market Outlook Q4 2014



Milan Office Market Outlook Q4 2014

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