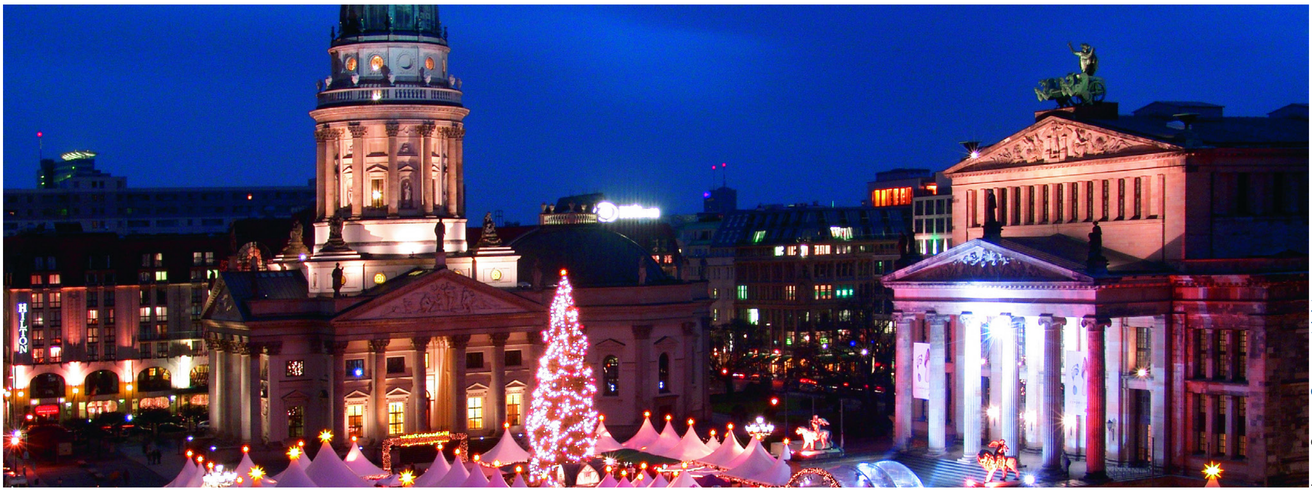

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What to Expect from Berlin´s Economy and Property Markets in 2018

The end of year is approaching and it is good to see that Germany and Berlin in particular have had a strong 2017. The economy grew faster than expected and the forecast figures for 2018 have been upped from previous forecasts. Berlins population is growing fast and the business landscape is expanding rapidly, very much in favour of the real estate markets making 2017 another successful year. In this newsletter we have looked into whether or not the conditions are set for a prosperous 2018.

The Berlin Economy 2018

The German economy is flourishing benefiting from record-high employment, extremely low interest rates and buoyant export dynamics. The gross domestic product (GDP) growth for 2017 is estimated between +1.9 and 2.0%. Taking into account that there is a significant calendar effect in 2017 as the figures are not adjusted for workdays, that would translate the foreacast figure into a rate of +2.3 percent. The forecast for 2018 looks just as good with +1.8 to 2.2 % (depending on sources).

Berlin´s economic dynamics are extraordinary promising. The economy grew particularly well in the second half of 2017, by 2.8% and the growth forecast for the total year is 2.5%. According to a report by *Berliner Sparkasse*, a growth of 2.7% can be expected for the first quarter of 2018 (calendar adjusted).

Berlin´s economic base is keeping up well with its fast population growth. Employment grew by 4.6% this year (as of July 2017), especially in higher paid segments. With that, it seems the purchasing power is set to grow further.

Main growth drivers are business services, media and technology sectors. The information and communication technology sector grew by more than 11.1% in 2017.

Experts in an article by *PropertyEU* forecast employment growth above the national average, mainly fueled by the technology sector and with that, Berlin is believed to become the fastest-growing city in the next five years.

According to *Bulwiengesa*, one of the largest independent analysts in the real estate industry in continental Europe, the number of office employees grew by more than 24% between 2005 and 2015. To compare with, Paris had a 7% and London 23% growth in office employees in the same period. This highlights how dynamic the expansion of the business landscape in the capital is, which is set to continue further.

The financial situation of the Berlin government is looking healthy as well with the new budget for the years 2018/19 allowing an additional investment volume of 500 million a year. Public spending, especially in infrastructure, will additionally boost the city´s attractivity and create additional jobs (see our November 2017 newsletter).

The Commercial Property Market 2017 and 2018

A look at this year´s commercial investment activity reveals a remarkably positive picture for the Berlin property markets while the overall German market is also doing well.

Commercial transaction volume in the German capital reached €6 billion (in the first three quarters), which is 79% more than in the same period last year and more than the ten-year-average of €3.9 billion. This result puts Berlin ahead of all other cities in Germany, followed by Munich with €3.8 billion transaction volume.

Grossmann & Berger forecasts that € 7 billion could be realistic as a result for the total year 2017, which would get Berlin close to its record year 2015, where it saw €7.8 billion in transaction volume.

The office segment is currently the obvious favourite of investors taking the share of ca. 77% of overall commercial activity — an increase of 20% year on year, while hotel and retail accounted for only 9% and 8%, respectively.

Berlin´s commercial investment prospects for 2018 are regarded as highly beneficial. The German capital ranks first in terms of overall investment and development prospects across Europe in the annual survey *Emerging Trends in Real Estate Europe 2018* by *PwC* and *Urban Land Institute*.

According to investors surveyed by *PwC* and *ULI*, Berlin is so attractive because it offers sustainable property values due to its fast growing population and expanding businesses. Investors primarily rely on rental growth, as the capacity for further capital growth is limited due to compressing yields. However, there are no signs of overheating as demand from tenants is set to grow further.

The forecast for the office letting market looks quite compelling for 2018 and beyond.

According to the rating agency *Scope*, office rents will continue to grow with an annual rate of ca. 4.4% until 2021 (1% up from the last year´s forecast). This would represent the highest growth rate in Europe.

Top office rents in Berlin could grow by as much as 12% by the end of 2018 and are expected to surpass the 30 Euro mark, as the report by the research association *gif (Gesellschaft für Immobilienwirtschaftliche Forschung)* suggests. This places Berlin at the top of the German Big-5 cities, where growths between 2 and 7% are expected.

The vacancy rate is currently at ca. 3% and experts expect prime rental growth to go up by ca. 4% in 2018. Lack of space is expected at least until 2019.

It also looks like the strong investment activity is going to continue in the next years boosted by foreign investors, who clearly dominated the buying activity with a share of ca. 72% and the selling activity with a share of ca. 50% in Berlin this year. There are actual indicators that this trend might continue.

According to *REFIRE* (*German Real Estate Finance)*, the Canadian investor *Oxford Properties* who invested in the Sony Center in Berlin this year, has the goal to invest further in continental European assets within the next five years, with the primary focus on Berlin and Paris.

And different real estate and China experts suggest that especially Chinese investors become increasingly aware of Berlin as international investment destination, while in the past they were primarily focusing on destinations in the UK, US, Canada and Australia. Within Germany, Berlin and Frankfurt are the most favoured cities.

Housing Market Trends

Positive developments can also be expected in the Berlin housing market albeit accompanied by a slow down of price growths.

On the supply side, building activity is growing. The increased number of building permits by ca. 18% in the first three quarters of 2017 indicates a high level of construction activity in 2018 and the following years. The building industry is seeing high price increases.

On the demand side, conditions remain beneficial for further price and rent increases (unless regulations will tighten). Continued urbanisation will further fuel demand widening the gap between required and supplied housings, despite the growing building activity.

According to *Dr. Klein* financial consulting, property prices in Berlin increased by 18% in the second quarter 2017 compared to the same period last year.

However, these price surges are not just due to the wide gap between demand and supply. Low borrowing rates and lack of alternative investment options play a significant role.

While it is not yet clear, when a reversal of the interest rate policy can be expected and how it will affect the market activity, it seems that the peak for price growth has been reached Berlin property, as *Dr. Klein* experts suggest. Only moderate price increases are expected in 2018.

However, there are no signs for a bubble, in general, only certain market segments could be affected (e.g. luxury segment).

Conclusion

Real estate experts firmly believe that Germany is going to have a strong 2018, despite the political uncertainties about the next coalition. Berlin´s significance as Germany´s largest property market combined with its booming economical and employment development seem to provide very favourable conditions for at least another year.

Low interest rates facilitate these dynamics. The European Central Bank is expected to keep the key rate near zero also in the next year meaning that real estate will likely remain an attractive investment option.

Nonetheless, it is unforeseeable how long this upturn will continue and what sort of challenges investors might face when it is over. It is advisable to look at opportunities very carefully and consult experts with solid market experience.

Please note that the contents of this newsletter have been researched and written according to the best of our knowledge; however they are in no way to be accepted as a legal advice or suggestion. Therefore we exclude any liability.

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