

Real estate market Germany

A Research Publication by DG HYP

Office and retail real estate still downward – residential real estate stable

Office real estate

- Office rents in Germany are likely to decline by around 5 per cent this year, with the pace of the downward movement slowing only marginally next year. We expect rents in Berlin, Munich and Frankfurt to show the steepest fall. However, the current downward trend is nowhere near as severe as eight years ago.
- Rents are likely to show an above-average decline this year in Berlin and Frankfurt, and in Munich. An increasing number of tenants in the already favourably priced Berlin office market are vacating prime locations for cheaper non-central properties, but peak rents are also coming under severe pressure in the other large locations

Retail real estate

- We expect the decline in retail rents in Germany to be very moderate at 2 to 3 per cent this year, and 1 per cent next year. Despite the downward trend, an index of retail rents based on the locations covered here should still be well above the 2007 level next year.
- We expect a slightly above-average decline in Frankfurt given the high level of per capita space there, while the downward trend in rents in Munich should be below-average because of the fairly low volume of space on offer.

Residential real estate

- Throughout Germany, rents for new apartments are likely to increase by a maximum of 1 per cent this year; we do not anticipate any scope for a sharper rise in residential rents. We also expect only a slight increase in rents in 2010, mainly affecting the major cities.
- We expect prices of residential properties in Munich, Frankfurt and Hamburg to increase slightly up to next year, with only stagnation in Berlin.

September 2009

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Real estate market Germany

Following the severe economic downturn at the beginning of this year, in recent weeks there have been increasing signs of stabilisation. The economy was already growing slightly by 0.3 per cent in the second quarter, although this was partly attributable to a number of extraordinary factors: firstly, the scrappage premium boosted private consumption, and secondly some construction projects were only completed in the second quarter because of the cold winter half-year. As a result of the rise in a number of leading indicators, the chances of levels flattening out in the second half have clearly improved. Nevertheless, we expect GDP to decline by 5.1 per cent in 2009. With only a slight acceleration in economic growth, we anticipate economic growth of 1.2 per cent next year. Investment will then benefit from fiscal policy measures and exports will increase slightly.

German economy likely to contract by 5.1 per cent in 2009

Only weak economic growth next year

Economic forecast Germany

<i>as % compared to previous year</i>	2007	2008	2009	2010
GDP	2.5	1.3	-5.1	1.2
Private consumption	-0.4	0.4	1.0	0.7
Public consumption	2.2	2.2	2.7	2.2
Investments	4.3	2.9	-9.1	1.8
Exports	7.5	2.8	-16.1	5.4
Imports	5.0	4.3	-8.9	5.5
Inflation rate (HICP)	2.3	2.8	0.3	1.1
Unemployment rate (ILO)	8.4	7.3	7.9	9.7
Budget balance <i>as % of GDP</i>	-0.2	0.0	-3.8	-5.2

As a result of the sharp hike in energy prices, the inflation rate of 2.8 per cent in 2008 was higher than at any time in the European Monetary Union's existence. As a consequence of the sharp decline in the oil price, a barrel of Brent oil was only half as expensive in July this year as in the same month last year, and the inflation rate has therefore slipped into the negative sector as a result of a strong basis effect: on average, inflation should reach only around 0.1 per cent in Germany in 2009. As a result of the severe economic downturn, the number of people unemployed (ILO) in Germany has increased by 300,000 since the end of last year. Unemployment has consequently increased from 7.1 to 7.7 per cent, and we expect an average figure of 9.7 per cent next year.

Unemployment could rise further

Office

Office rents in Germany have scarcely risen in the period from 1998 to 2008, increasing only weakly by an average of 0.2 per cent p.a. Compared to office markets in the neighbouring countries of France and the UK, the German market is therefore showing only a very moderate performance, since office rents in these countries have increased by an average of 2.2 and 2.7 per cent in the corresponding period (see graph below). Rents in France and the UK surged in the years 2000 and 2006 and 2007, with rates of increase up by 15 and 35 per cent on the previous year at times. German office rents showed their strongest growth of 5 per cent in 2000. However, Germany was also affected by the Europe-wide downturn in the markets in the years 2000 to 2004 with a decline of around 16 per cent.

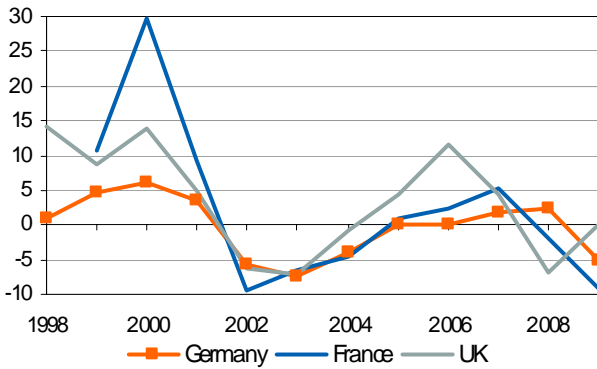
Office rents have hardly risen in Germany since 1998

Situation in France and the UK quite different

The situation is different with regard to vacancy rates, with Germany at the upper end of the range compared to France and the UK at around 8 per cent (see graph). This is attributable to the comparatively high level of vacancy in German office centres, while rates in Paris and London are well below the country-wide average.

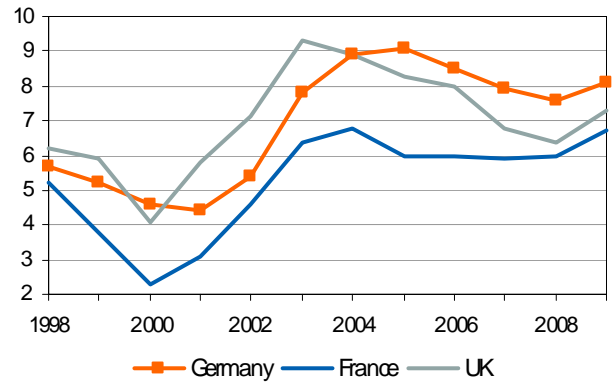
However comparatively high vacancy area in Germany

Subdued trend in office rents in Germany



Source: Feri, rent per sq m office space as % yoy

High vacancy rate on an international comparison



Source: Feri, vacancy rate relating to office space in average location

Situation and trends

As a result of the macroeconomic recession, demand for office space in Germany declined sharply in autumn 2008. However, last year on average there was still no sign of a decline in rents for office space in prime locations. On the contrary, in most locations rents were still clearly rising: the highest level was in Frankfurt (+6.2%), followed by Hamburg (+4.8%), Munich (+4.2%), Düsseldorf (+4.1%) and Berlin (+3.3%). In contrast, rents in Stuttgart were already stagnating last year.

We estimate that rents for prime locations in the main office centres are declining by about 5 per cent in 2009. This would be a similarly sharp decline as last reported in 2004. Rents are likely to show an above-average decline this year in Berlin and Frankfurt, and in Munich. An increasing number of tenants in the already favourably priced Berlin office market are vacating prime locations for cheaper non-central properties, but peak rents are also coming under severe pressure in the other large locations. In the first quarter, rents were already declining in the six main office centres, with the downward trend accelerating further in the second quarter in Frankfurt (-3%) and Munich (-4%).

Demand for office space down sharply in 2008

...but rents have mainly increased

Rents down by about 5 per cent in 2009

Figures and forecast for office markets

	rent top location			vacancy rate		
	2008	2009e	2010e	2008	2009e	2010e
Berlin	22.10	20.30	19.70	8.6	8.9	9.3
Hamburg	24.00	23.60	22.50	7.0	7.9	9.3
Frankfurt	38.50	36.40	34.80	14.4	15.5	15.8
Munich	31.40	29.50	28.60	9.2	10.3	12.0
Düsseldorf	22.90	22.00	20.60	10.1	10.9	12.0
Stuttgart	17.50	16.70	16.20	5.2	6.0	6.3

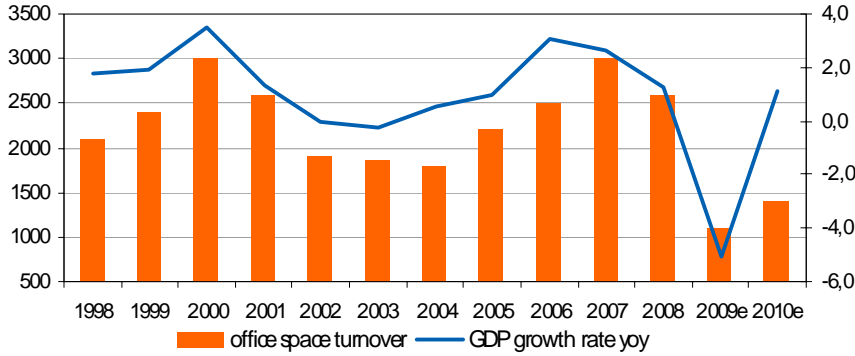
Source: Feri, DZ BANK Research, rent in EUR monthly per sq m, vacancy rate as % of inventories

Potential tenants in the German office markets are currently being offered numerous incentives – for example rent-free utilisation at the beginning of a rental contract or the temporary cost-free use of parking spaces – in order to prevent a steeper decline in rental prices. However, since job shedding in the office sector has only begun over the course of

Office rents likely to decline further in 2010

this year, we expect rents to continue to fall in 2010. However, the rate of decline should be slightly less marked than this year at around 4 per cent.

Office space turnover in 1,000 sq m (rentals and sales)



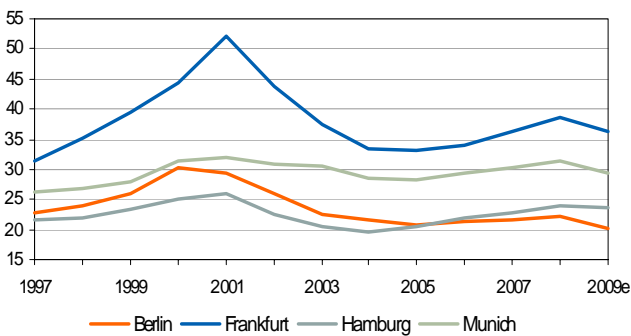
Source: DZ BANK Research

Turnover of office space (rental and sales) declined sharply again in the first half after an already weak second half of 2008. Three quarters of all sales have been in the six main office centres, with virtually no foreign buyers involved. Since no visible recovery is expected over the year, we expect transaction volume of only just over one million square meters this year. Following the economic recovery we expect the number of transactions for office properties to increase at the earliest from mid-2010, and sales of office space next year are therefore likely to be only slightly higher than this year.

Turnover restricted to main centres in first quarter

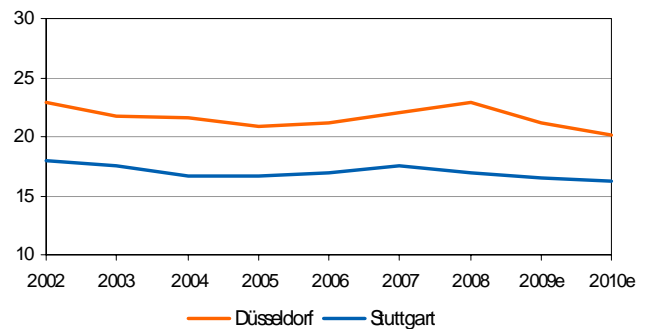
Turnover likely to remain weak

Office rents for top locations in Frankfurt affected by international comparison (in EUR per sq m)



Source: Feri, forecast DZ BANK Research

...resulting in some wide divergence from other national markets



Source: Feri, forecast DZ BANK Research

Frankfurt

Rents for prime office space increased again significantly by 6.2 per cent in 2008 – the sharpest increase amongst the main centres of office accommodation in Germany. However, the only rent increases in the banking capital were at the beginning of the year, subsequently office rents stagnated on account of the sharp decline in demand for space. On an international comparison, the level of rents in Frankfurt at around EUR 36 per sq m is in line with the French capital. However, rents in Paris are likely to have fallen much more sharply this year than in Frankfurt, where a number of incentives are being offered in an

Frankfurt: rent level similar to Paris

attempt to halt the decline in rents. Based on the more rigid downward rent level, we expect a sharp increase in empty office space in Frankfurt – the vacancy rate is likely to reach around 16 per cent next year.

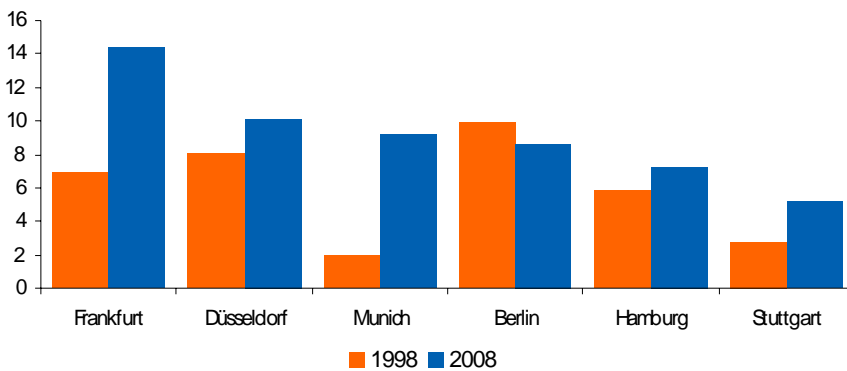
...but decline in rents likely to be weaker

Munich

In contrast to Frankfurt, rents in Munich continued to rise until the third quarter of 2008, although remaining well below the Frankfurt level at just over EUR 30. Overall, rents in Munich have increased by 17.5 per cent since 1998 and thus more strongly than in Frankfurt. However, as a result of strong construction activity, the supply of space also increased significantly in this period, and the vacancy rate has thus increased more than fourfold from 2 to 9.2 per cent in the last ten years (see graph). As in Frankfurt, rents in Munich fell sharply in the first half of this year, and the rate of decline even accelerated in the second quarter. Since more new space is being completed this year and the supply of office space is growing more strongly than in Frankfurt, we expect rents to decrease by about 6 per cent this year.

Munich: rents fell sharply in the first half of this year

Vacancy rate up sharply in Munich since 1998



Source: FERI, DZ BANK Research, vacancy as % of available office space

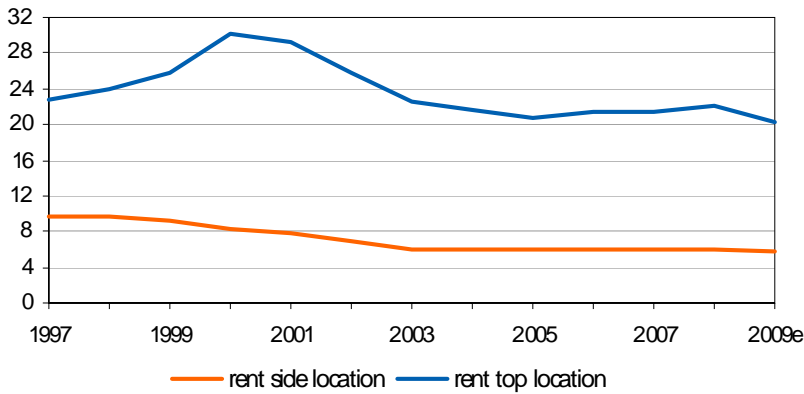
Berlin

The Federal capital has the newest supply of office space as a result of the construction boom triggered by reunification. A quarter of the available 17.3m sq m has been created since 1995. This comparatively modern supply of office space also in non-central locations is clearly depressing top Berlin locations in the current downturn for office markets. Since many large companies still only have a branch in Berlin, while their headquarters is situated elsewhere in West Germany, the decision to move to a much cheaper non-central location with modern facilities is easily taken. Rents in prime locations should therefore show an above-average decline of about 8 per cent this year compared to the rest of the country. Since we expect the downward trend to continue until the middle of next year, a decline of around 3 per cent is likely in 2010.

Berlin: large supply of modern office space in side locations...

...therefore top rents down by 8% in 2009

Berlin: office rents in EUR per sq m



Source: Feri, DZ BANK Research

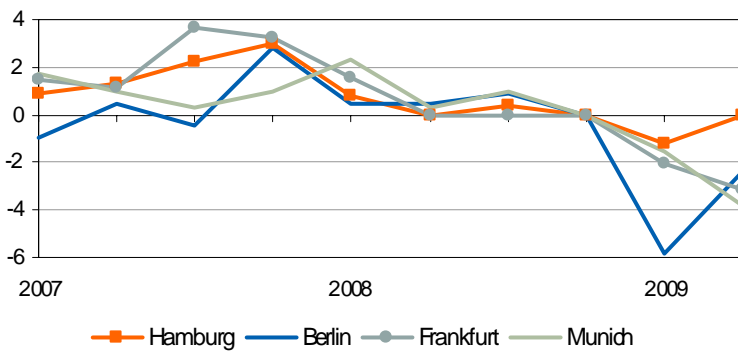
Hamburg

Compared to Berlin, Frankfurt and Munich, office rents in Hamburg have proved very robust in the first half of this year, stagnating in the second quarter after falling by “only” 1.2 per cent in the first quarter qoq (see graph). In the months ahead we expect rents in the North German metropolis to decline further, however rents for prime locations are only likely to decline by an average of about 2 per cent on the previous year’s level this year. However, the collapse of world trade in the winter months is having a very marked negative effect on demand for office space, a situation which is likely to persist until well into next year, and we expect more jobs to be shed in the winter months. The supply of office space will also be visibly increased in 2010, for example as a result of the completion of new buildings in the port city. The fairly subdued economic outlook and the growth in office space will considerably strengthen the negotiating power of potential tenants, and we therefore anticipate a steeper decline in office rents next year than this year. This year the vacancy rate is already likely to increase to just over 8 per cent, and in 2010 we expect a figure in excess of 9 per cent – the highest level since 1992.

So far very robust growth in office rents in Hamburg

Hamburg: rents down more sharply in 2010 than this year

Hamburg: very robust trend in office rents so far (prime locations)



Source: Feri, DZ BANK Research

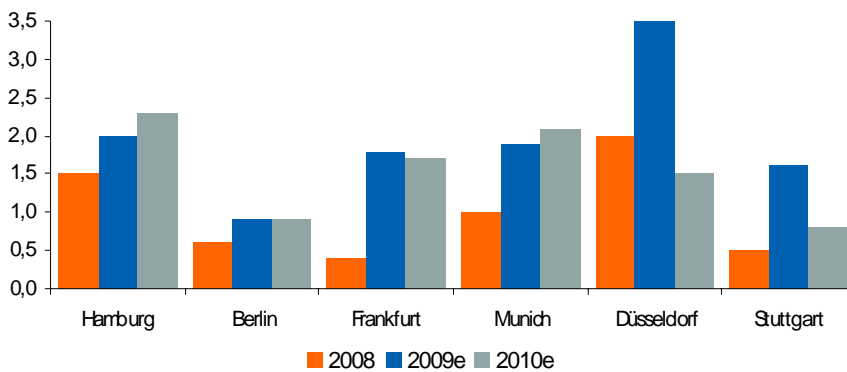
Düsseldorf

We expect rents for prime locations in the capital of North Rhine-Westfalia to remain slightly higher than those in Berlin for the time being. However, the downside is a double-digit vacancy rate which is likely to exceed the 11 per cent level this year. Although, according to estate agents, rents have not fallen in the first half, we currently expect rent levels in Düsseldorf to decline sharply. The opportunities for concessions from landlords such as cost-free renovations and rent-free periods are likely to come to an end, and we therefore anticipate a rent level in 2009 which is four percent below the previous year. Since a large number of new building projects will be completed in the final months of the year (see graph), we expect the downward trend in office rents in Düsseldorf to accelerate at year-end: in 2010 we anticipate a rent figure of close to EUR 20 per sq m, representing a decline of around 6 per cent.

Vacancy rate in Düsseldorf increasing sharply

Decline in rents expected to accelerate at year-end

Düsseldorf: largest growth in office space as % yoy



Source: Feri, DZ BANK Research forecast

Stuttgart

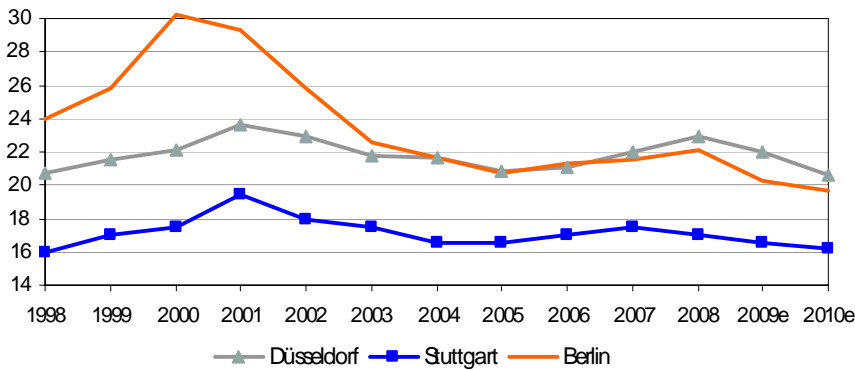
Since the supply of office space in Stuttgart is slightly smaller than in Düsseldorf, the office market in the Swabian capital is the smallest of the markets covered here at 6.9m sq m. Rents for prime locations had already been stagnating since mid-2007, and then fell by around 3 per cent in the first quarter of this year. Despite by far the lowest vacancy rate of the six main office centres in Germany, we do not believe that rents have bottomed out as yet.

Stuttgart: rents down by 3 per cent in first half...

The industrial companies mainly based in Stuttgart have been particularly badly affected by the sharp decline in the global economy. Irrespective of the first signs of economic recovery, the companies are likely to continue with their cost-saving measures and also scale back their requirements for office space accordingly. Overall, in 2009 we expect a level of rent probably about 5 per cent below last year, while next year rents are likely to decline again slightly by 3 per cent.

...decline continuing

Stuttgart: office rents in prime locations in EUR per sq m



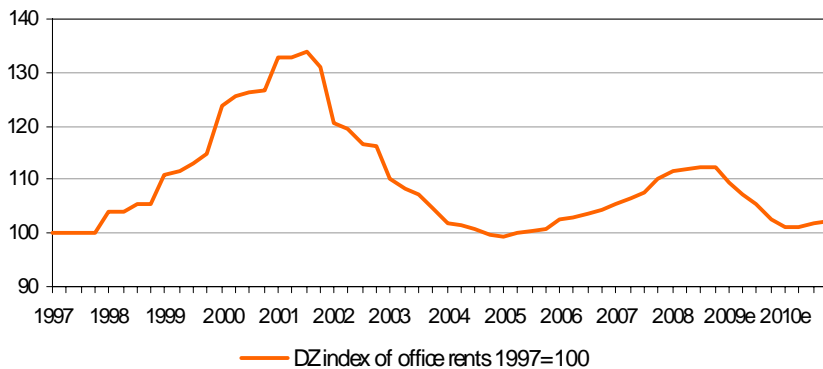
Source: Feri, DZ BANK Research forecast

Outlook

Office rents in Germany are likely to fall by about 5 per cent this year, with the pace of decline only expected to weaken slightly in the year ahead. We expect rents in Berlin, Munich and Frankfurt to show the steepest declines. Although the current downward movement is nowhere near as severe as eight years ago, an index of office rents we have calculated based on the property centres examined where 1997=100 is approaching the 1997 level.

Decline in rents not as marked as eight years ago

Rent index unlikely to fall below the 1997 level



Source: DZ BANK Research, Index office rents in top locations

Retail

Rents for retail space in top locations have risen by only eleven per cent in Germany since 1998, while much steeper rent rises have been implemented in other European countries (see graph). Fairly surprisingly, no German city therefore ranks amongst the ten most expensive locations in Europe. Although Munich tops the list within Germany for rent levels in prime locations, on a European comparison it ranks only twelfth. In contrast, in the largest neighbouring country, France, rents have soared by around 40 per cent. However, retailers there have also enjoyed similarly strong growth in their sales in the same period, while in Germany sales have virtually stagnated with growth of only 0.4 per cent.

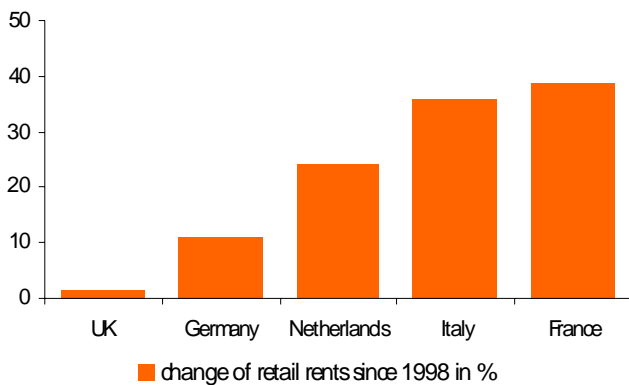
Only weak growth in retail rents since 1998...

...retail sales stagnated in this period

However, the last economic upturn provided visible momentum for German retail rents, albeit after a certain time delay; in 2007 rents rose by 2.2 per cent and in 2008 by 5.2 per cent. However, this positive trend was mainly restricted to very good locations, while in most non-central locations vacancy continued to increase and is still having an adverse impact on rent levels in modest locations.

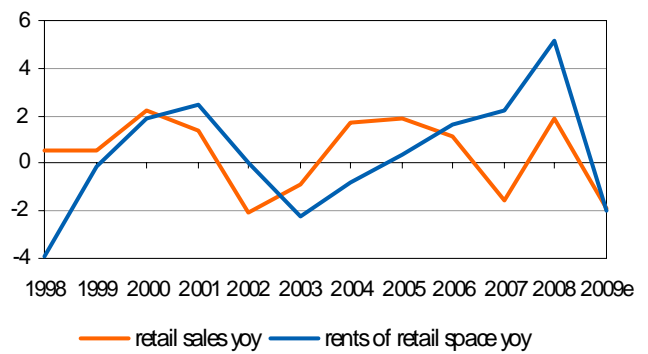
Top locations benefited in the last economic upturn

Retail rents up only slightly in Germany since 1998



Source: Feri

...however 2008 retail rents rose sharply



Source: Feri, DZ BANK Research forecast

Situation and trends

The range of rental prices in the property centres examined here extends from only EUR 70 in Hamburg to EUR 209 in Munich, and a good retail location in Munich therefore costs three times as much as in Hamburg. Second and third position are occupied by Frankfurt and Düsseldorf, more or less level-pegging at monthly rents of around EUR 170 per sq m. Berlin has by far the largest supply of retail space in Germany, at around 5.8 sq m in 2009. However, in terms of the rent level, the capital city ranks only second last (see table below).

Wide range of rent levels

In 2008, retail rents in Germany were still showing an average annual increase of around 5 per cent. However, growth in Stuttgart was already very low at only one per cent, while Hamburg, Berlin and Düsseldorf reported above-average growth.

Figures and market forecasts for retail properties

	2008	Rents in prime locations 2009e	2010e	2008	Retail space per capita 2009e	2010e
Berlin	112.80	110.00	109.00	1.65	1.70	1.75
Hamburg	80.70	79.20	78.80	1.49	1.51	1.52
Frankfurt	176.40	170.00	165.00	1.97	2.06	2.10
Munich	213.30	209.90	207.80	1.33	1.35	1.38
Düsseldorf	170.90	166.00	163.00	1.60	1.60	1.62
Stuttgart	147.90	145.00	142.80	1.58	1.61	1.62

Source: Feri, DZ BANK Research, rent in EUR per sq monthly, vacancy rate as % of available retail space

As a result of space becoming available in stores and the completion of building projects, the construction of which had started during the last economic boom, the supply of retail space in Germany will continue to increase clearly until the year 2011. However, we also expect demand for retail space to fall slightly. Like many other sectors of the economy, many retail companies are also undergoing a phase of consolidation, and willingness to close down unprofitable sites is therefore at a very high level. On the other hand, there are still some international chains which do not yet have a presence in Germany and which are still considering what is admittedly not a high-growth, but still a solid market. However, since this is only likely to provide very limited support for demand for retail space, we expect rents in the property centres referred to above to decline by 2 to 3 per cent this year. In 2010 the decline is likely to initially continue, and rent levels will also then fall slightly.

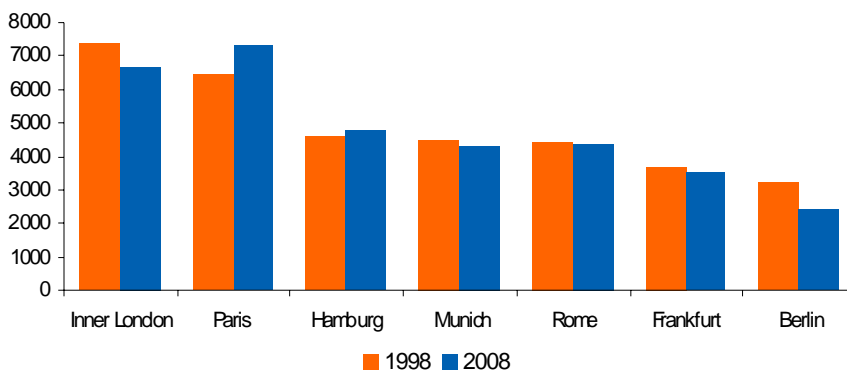
However, we anticipate a generally more negative trend in B-locations, since customer flows are likely to focus more strongly in future on attractive shopping centres and city centres – the buzzword being “event shopping”. The departure of an anchor tenant is increasingly laying waste to smaller town centres.

Many construction projects completed in 2009 and 2010

Rents should also decline slightly in 2010

B-locations facing steeper rent decline

Low retail space productivity compared to London and Paris



Source: Feri, DZ BANK Research forecast, annual retail sales per sq m in EUR

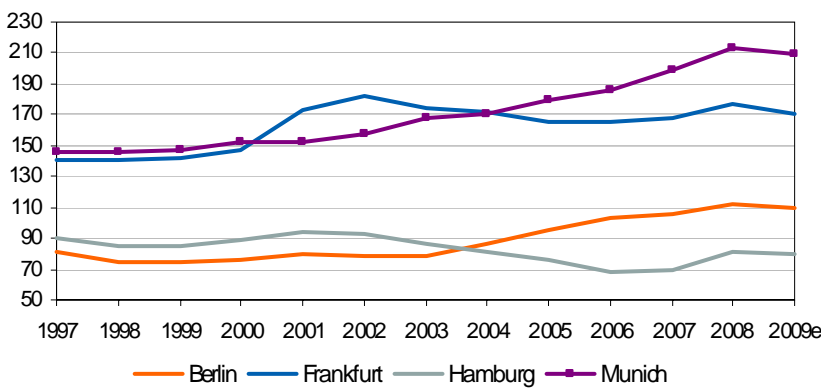
Frankfurt

With around 2 sq m of per capita sales space, of the cities observed Frankfurt has by far the largest volume of retail space. By comparison: the average throughout Germany is around 1.5 sq m and the average in property centres is about 1.6 sq m. Next year a large number of new retail properties will also be completed in Frankfurt, and the supply of sales space will then show an above-average increase to 2.1 sq m. However, retailers in the banking capital are viewing the future with some concern since unemployment is likely to rise sharply, which will in turn depress retail sales. On account of the strong expansion of retail space in the recent past and the forthcoming growth, we expect the decline in rents in Frankfurt to be above-average compared to other centres, with an anticipated decline of 4 per cent this year and 3 per cent next year.

Frankfurt: large supply of per capita sales space

...therefore above-average decline in rents

Retail rents in top locations in EUR sq m



Source: Feri, DZ BANK Research forecast

Munich

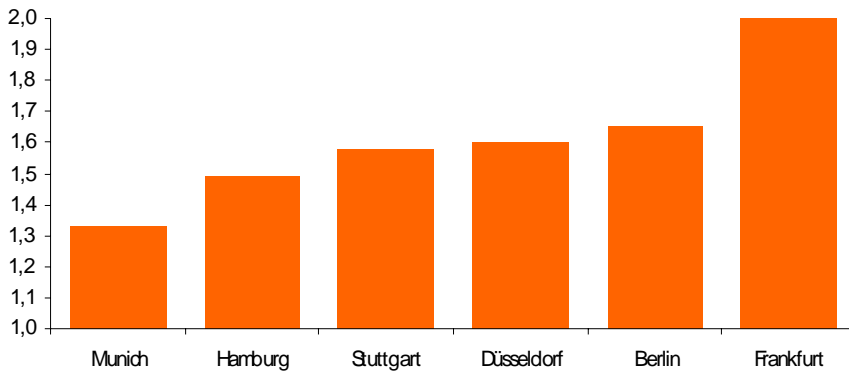
In contrast to the city on the river Main, the lowest supply of per capita retail space is to be found on the river Isar: at only 1.3 sq m in 2008 the figure was well below the German average and only two thirds of the level in Frankfurt. Since the image of Munich as an attractive shopping city with many tourist attractions has not suffered in recent years and the population continues to grow steadily, landlords of retail properties have also benefited from continuous growth in rents in the last ten years. At EUR 212.50 per sq m, rents were 45 per cent higher in 2008 than in 1998. By comparison: consumer prices have increased by almost 20 per cent in Bavaria in the same period.

Munich: retail rents have risen by 45 per cent since 1998

Although Munich continues to act as a magnet for the surrounding area, we still expect unemployment there and in the surrounding area to increase visibly next year. We also expect a slight decline in the disposable incomes of private households. As a result of the global economic crisis, the number of foreign tourists has also fallen. This has dampened the expectations of retailers, and no sales growth is likely for the time being. What are very high rents in Munich compared to the rest of Germany are therefore increasingly difficult to justify, however the decline is likely to be only below-average at around 2 per cent. In 2010 we anticipate a weaker decline of only one percent. The main reason for the below-average decline is the comparative shortage of available space.

Decline in rent likely to be below-average

Munich: Lowest supply of per capita retail space (in sq m) 2008



Source: FERl, DZ BANK Research

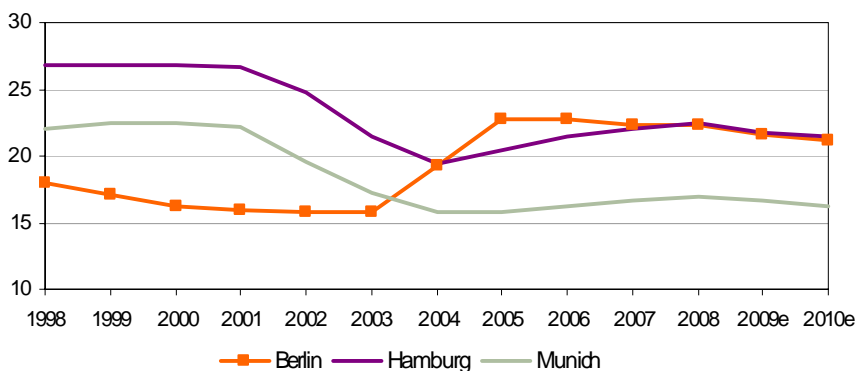
Berlin

Rents for prime retail locations in the German capital have risen slightly higher than in Munich in the last ten years with an increase of around 50 per cent. However, renting a shop in Berlin costs only half as much as in the Bavarian city (see table). In contrast, it is comparatively expensive to rent a shop in a side location in the biggest shopping city in the East of Germany, as can be seen in the graph below. While Berlin is level-pegging with Hamburg in this segment, Munich brings up the rear amongst all the locations covered here at only EUR 17 per sq m. Since retail space productivity in Berlin is likely to have fallen to a new record low as a result of declining retail sales, we expect rents in both prime and side locations to decline by 2 to 3 per cent. Rents in Berlin are also likely to fall slightly next year on account of sluggish consumer sales.

A shop is half as expensive in Berlin as in Munich

Retail rents will fall again slightly in 2010

Berlin: retail rents in side locations in EUR per sq m



Source: Feri, DZ BANK Research forecast

Hamburg

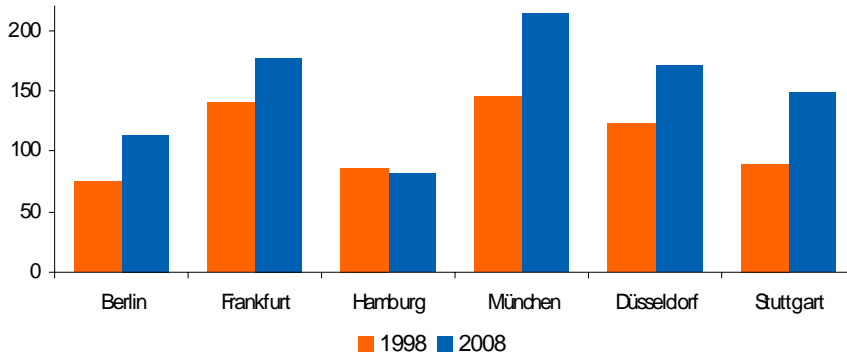
While retail rents in other locations have increased visibly since 1998, the level in the North German port city has fallen slightly. This is all the more remarkable since retailers in Hamburg generate the highest sales per sq m of retail space ahead of Munich. Nevertheless, rents for prime locations were still growing strongly at the beginning of 2008 as a result of the last economic boom, and the average annual increase was therefore a

Hamburg: sharp increase in rents in 2008 was a response to pent-up demand...

substantial 15 per cent. However, this strong growth also has to be regarded as a reaction to pent-up demand following below-average growth in previous years. Rents are now moving downwards again slightly. Based on the comparatively favourable rent level and the slightly below-average supply of per capita space, we anticipate only a very weak decline in rents this year and next year. However, since annual growth in retail space will increase from 2010 partly due to the completion of buildings in the port city, we expect only very limited scope for rent increases in the medium term.

...however, we anticipate retail rents are down by only 2% in 2009

Hamburg: retail rents down slightly on 1998 levels



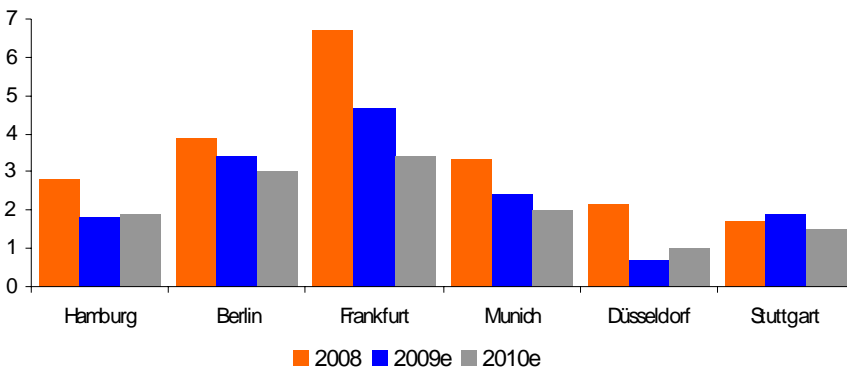
Source: DZ BANK Research

Düsseldorf

In Düsseldorf a retailer has to pay roughly the same level of rent as in Frankfurt at around EUR 170 per sq m, however higher retail sales in the city on the Rhine mean that retail space productivity and thus profits are slightly higher. Available per capita space is exactly average for property centres at 1.6 sq m. Since the supply of space is growing only slightly this year and next year, we do not expect the supply level to depress growth. Nevertheless, demand for retail properties in Düsseldorf is also suffering as a result of weak consumption in Germany, and rents are therefore likely to fall slightly in 2009 and 2010.

Düsseldorf: here too demand for space is suffering from weak consumption

Düsseldorf: comparatively weak growth in retail space in % Y/Y



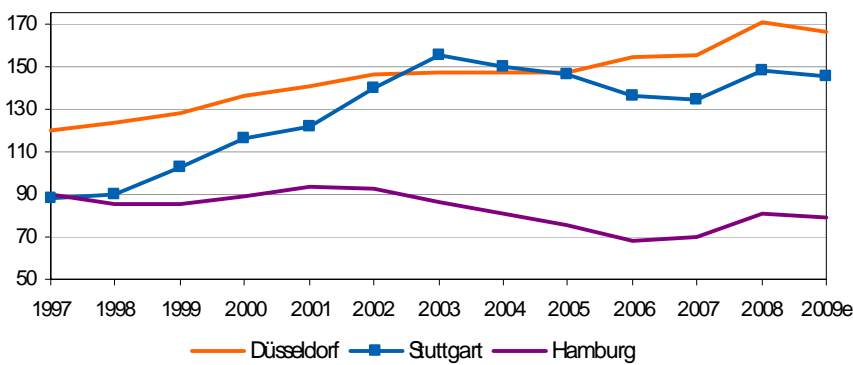
Source: Feri, DZ BANK Research forecast

Stuttgart

Along with Düsseldorf, Stuttgart has the smallest supply of space of the centres reviewed here at around 950,000 sq m. Retail rents surged around the new millennium but after a slight decline since 2006, are now around EUR 136 per sq m. Despite the fairly weak trend in recent years, rents in Stuttgart are still twice as high as in Hamburg and are also clearly above the level in Berlin. In terms of retail space productivity, the South German provincial capital is at the average level for property centres and even reported a slight increase in 2008. Given the severe economic downturn of the last 12 months, and the subdued economic outlook for next year, we also expect rents in Stuttgart to fall slightly until the middle of next year.

Stuttgart: top rents are twice as high as in Hamburg

Stuttgart: retail rents in prime locations in EUR per sq m



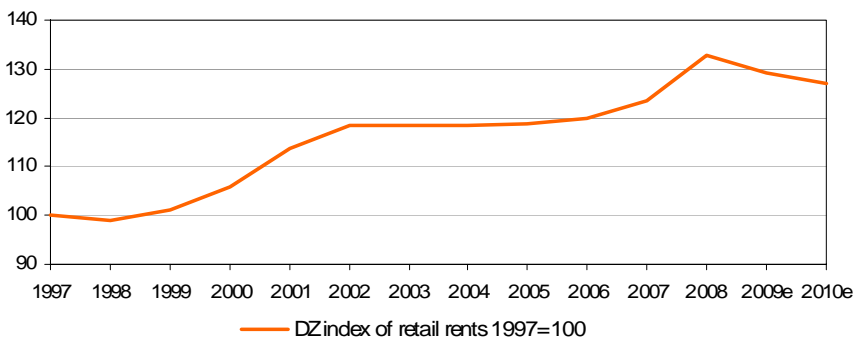
Source: Feri, DZ BANK Research forecast

Outlook

We estimate that retail rents in Germany will fall by a very moderate 2 to 3 per cent this year and by 1 per cent next year. An index of retail rents calculated on the basis of the locations covered here is likely to remain well above the 2007 level next year despite the downward trend. We expect a slightly above-average decline in Frankfurt on account

Moderate decline in retail rents in Germany

Rent index for top retail space in the large centres down only slightly



Source: DZ BANK Research, index retail rents in top locations (1997=100)

of the high level of per capita space available, while rents in Munich should show a below-average decline due to the very low level of supply.

Residential

The stock of housing units in Germany was nearly 39.8m in 2008. Of this, just over half are apartments in multi-family houses, while the rest are single-family houses, semi-detached and terrace houses. Since most private households in Germany (around 57 per cent) live in rented apartments, this category still represents around 23m housing units.

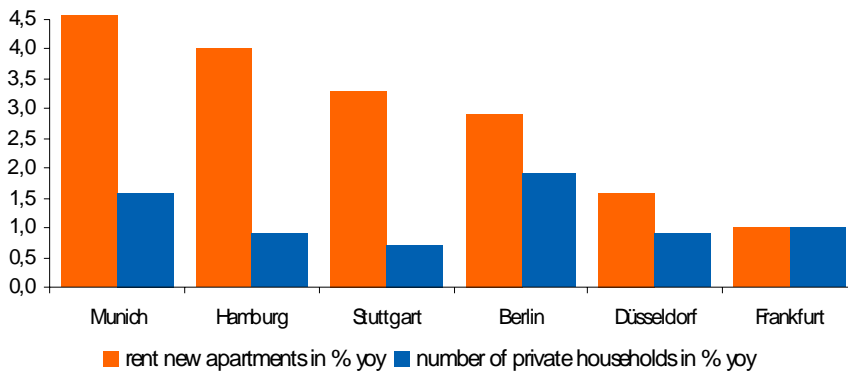
Situation and trends

The number of private households in Germany just about matched the 2006 level in 2008 as a result of the further growth in the number of single-person households. Given that the population has already been shrinking for several years, without this trend the number of private households would have fallen last year and in previous years. The number of private households is likely to remain virtually constant this year and next year, and demand for rented living space should also remain almost unchanged.

57 % of private households live in rented properties

Number of private households stagnating

Housing rents and number of private households in 2008 as % yoy



Source: Feri

However, the number of private households in the large business centres is continuing to show above-average growth: in 2008, the growth was between 0.7 per cent in Stuttgart and 1.9 per cent in Frankfurt (see graph). The process of migration from the country to the city has gained pace slightly in Germany in recent years. Consequently, trends in rents in large and small towns have diverged further, and this is likely to continue in the years ahead.

...but migration to business centres

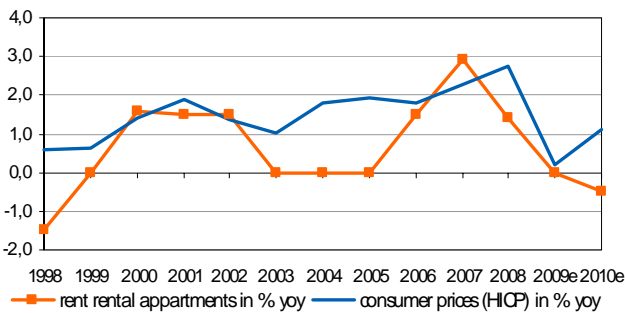
According to the Institute for Urban Development and Housing in Berlin (ifs), the average size of a rental apartment in West Germany is 73 sq m and 64 sq m in East Germany. According to the ifs, in 2008 rents per sq m in the West were around EUR 6.03 and in the East around EUR 5.66 – for the average household, this represents a monthly rent of EUR 440 and EUR 362 respectively. Throughout Germany, “cold rents” for housing increased by 1.3 per cent in 2008, whereas, as in previous years, rents for old apartments (+1.5%) increased more strongly than for new builds (+1.2%).

Stronger growth in rents for old apartments

In 2008 Munich once again showed the biggest increase in rents for new residential housing in good locations (+4.6%). Growth in Düsseldorf was only slightly weaker at 4 per cent. In contrast, rent increases in Hamburg and Berlin remained below the 2 per cent level (see graph). However, Hamburg still ranks third within Germany after Munich and Frankfurt with a rent level of EUR 10.60. Residential rents in the capital Berlin are still at the provincial level at only EUR 7 per sq m.

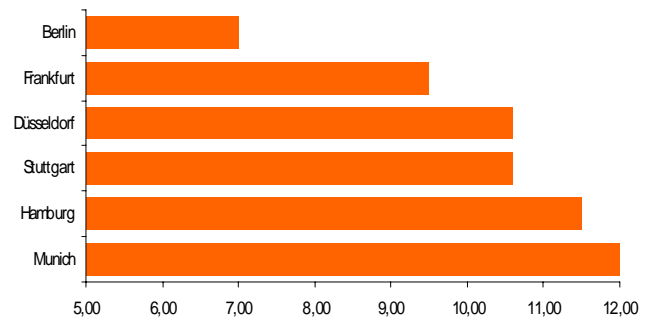
Only weak growth in rents in Berlin and Hamburg in 2008

Growth in rents much lower than inflation rate



Source: Feri, DZ BANK Research forecast

Residential rents in prime locations in Munich the highest of the major cities

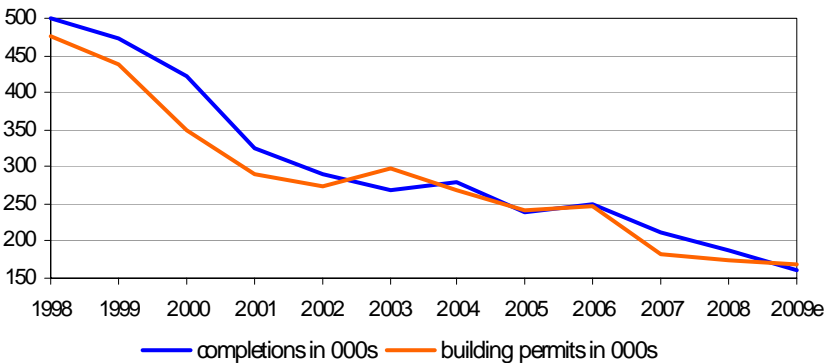


Source: Feri, rents per sq m in EUR for new residential properties

The number of new residential properties being completed has shown an almost unbroken decline in recent years reaching only 186,000 units in 2008, a new record low. The construction of apartment complexes has been particularly severely affected by the downward trend in recent years. Consequently, supply has become fairly tight in some parts of the German rental apartment market, particularly in the financial centres. Although the number of residential units does roughly correspond to the number of private households, a certain proportion of older residential properties are probably no longer suitable for letting due to technical deficiencies or completely unsatisfactory facilities.

Supply shortage due to weak construction activity

Steep downward trend in building completions not over yet



Source: Feri, forecast DZ BANK Research

However, we do not see any scope for a sharp increase in residential rents given the unfavourable macroeconomic situation which is likely to continue to depress the labour market in the months ahead. Next year too we expect only modest increases in rents, with residential properties in the major cities probably feeling the greatest impact. Rents for newly built apartments throughout Germany are likely to increase by a maximum of 1 per cent this year.

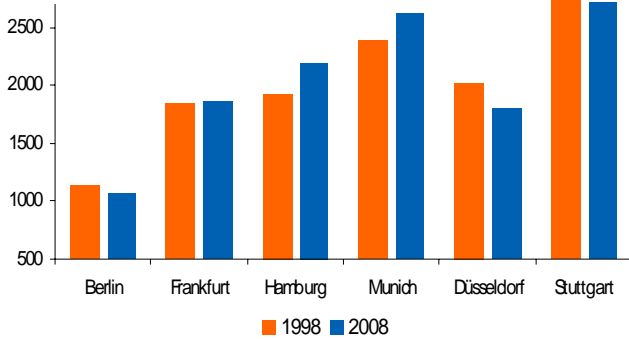
Residential rents likely to increase only slightly in 2009 and 2010

As with residential rents, Berlin is at the lower end of the range for the major cities examined here in terms of the level of purchase prices for apartments (see graph). In both the Southern Germany cities of Munich and Stuttgart, purchase prices are two and a half times

Very low price level in Berlin

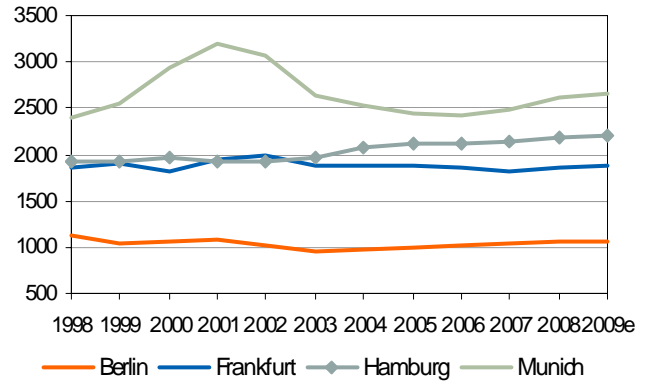
as high, and in Hamburg they are twice the level of the capital. Furthermore, prices in Berlin have fallen by 5.5 per cent since 1998, while they have increased by almost 10 per cent in Munich.

Prices of rental apartments in Germany virtually unchanged in some areas since 1998



Source: Feri, price for new rental apartments in EUR per sq m (average location)

Prices of rental apartments in Berlin the lowest



Source: Feri, price for new rental apartments in EUR per sq m (average location)

In 2008, prices of rental houses increased by 2.4 per cent throughout Germany; of the financial centres, Hamburg and Stuttgart reported growth of this level, while in Berlin, Frankfurt and Düsseldorf the upward movement was slightly smaller. As in previous years, the steepest price increase (+5.2%) was reported in the Bavarian capital. This year we expect prices of rented residential properties to stagnate throughout Germany as a result of the tougher financial conditions and the absence of foreign investors. While we anticipate only a slight increase of 1 to 2 per cent in Munich, Frankfurt and Hamburg, prices in Berlin are likely to stagnate or fall slightly. By our estimates, this trend will continue in 2010 with Munich continuing to benefit most from the increase in the number of private households, while weak construction activity will continue to support the price trend in Frankfurt.

Outlook

Rents and prices of residential properties are continuing to benefit in the business centres from the increasing number of private households. However, rents of new build residential apartments should increase by at most 1 per cent this year, and we do not anticipate stronger growth in residential rents because of the strained conditions in the labour market. We also anticipate only modest rent increases in 2010, mainly affecting the major cities. We expect prices of residential properties to increase slightly up to next year in Munich, Frankfurt and Hamburg, with only stagnation in Berlin.

Prices also likely to increase only slightly

Only weak growth in rents and prices of residential properties

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