Ecnomic Factor Real Estate 2017

– Report on the Macro-Economic Aspect of Germany's Real Estate Market

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Content

Summary

- The real estate industry plays a key role for Germany's economy, with real-estate-related business activities accounting for around 18 percent of the gross value added. Activities of this type are pursued by more than 815,000 German companies, nearly 3.9 million private landlords, and around 16 million owner-occupiers.
- Rather than standing out just because of its sheer size, the real estate industry is moreover characterised by its stability and therefore the way in which it contributes to the resilience of Germany's national economy. Especially during the financial crisis after the real estate bubble in the United States burst in 2006/2007, the German real estate industry had demonstrated its stability.

- Real estate is the most important real asset class in Germany. Out of a gross fixed assets total (at market prices) of 17.3 trillion euros by year-end 2016, built-up structures of one sort or another accounted for 80.3 percent or 13.9 trillion euros thereof. With accumulated depreciation deducted, the sum total of German net fixed assets in built-up structures is close to 8 trillion euros, which breaks down into c. 4.8 trillion euros in residential buildings and 3.2 trillion euros in non-residential buildings. The total asset value tied up in real estate is more than three times as high as Germany's net national income in 2015.

- At year-end 2015, roughly 82.2 million people lived in Germany in well over 41.4 million flats and 19.4 million buildings with a combined residential floor area of around 3.79 billion square metres. At the same time, workplaces occupied, for instance, around 426 million square metres of office space, 2.8 billion square metres of industrial and logistics space and 123.7 million square meters of sales area in the retail sector (estimates as of early 2015). However, these figures are fraught with uncertainty because the commercial real estate stock in particular is inadequately covered by official statistics.

- The average German household owns 125,000 euros worth of real estate, which is a relatively modest figure. In the last few years, the value of real estate stocks has been rising significantly, though. There are now 90 billion euros tied up in German real estate using this investment format. Open end and closed-end real estate funds have also rebounded in recent years, the focus being increasingly on institutional investors.

- Of fundamental significance for all investment formats is the brisk growth in real estate prices since 2010, which has been most conspicuous with residential real estate prices in major German cities. The threat of a speculative bubble remains nonetheless elusive because there are plausible reasons for the price trend, and because the financing behaviour remains virtually unchanged. However, it needs to be remembered that interest rates, employment figures and demographic growth combine into extraordinary favourable parameters for the time being, and that the coming years are likely to bring market adjustments for one or several of these factors.

- Driven by a fast-paced expansion of new lending business, the loan volume increased by nearly 4 percent in 2016 and thus substantially faster than in previous years. In the years since 2003, the annual growth rate had moved in a range of -1 to +2 percent. But even the most recent surge falls short of the long-term average since 1982, which is 4.7 percent. Similarly, the current boom is rather modest compared to other countries in Europe. Between 2004 and 2008, the rates of change in Germany's private housing loan volume remained substantially below the European average.

- At the same time, the challenges that banks face have intensified due to four simultaneous trends: The number of more complex loans (e.g. more project financing and more funding for secondary locations and in secondary cities) has grown. Moreover, the regulatory cost of equity has increased, and so has the bank levy. In addition, the organisational overhead for meeting the regulatory requirements has gone up. These trends suggest higher margin requirements. The fact that these have proven unattainable lately could be seen as a sign for fierce competition among German banks.

- Meanwhile, bank refinancing is on solid ground: Investors are buying up bonds as covered debentures, and their volume has noticeably increased in the most recent past

*Assets plus 10 billion euros in cultivated assets. *Miscellaneous areas mining land and areas used for other purposes, not including cemeteries. Source: Federal Statistical Office (2016a, b). Proprietary chart.*

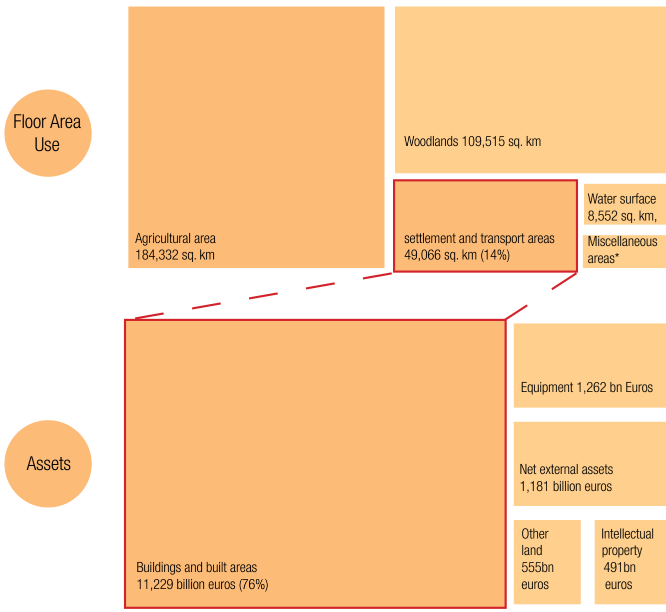

Figure 0: Ratio of floor space utilisation (environmental accounting) to asset value (national accounting) of the each real estate industry share in Germany's macro-economy of in 2015

Chapter 1
Specificities of theReal Estate Industry

Chapter edited by:
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EXECUTIVE SUMMARY

At first glance, real estate represents a class of "normal" goods. But this is valid only if you apply a narrow economic interpretation. According to the latter, the normality of the demand for goods implies that demand will positively respond to changes in income.

If you take a broader view, real estate represents in many ways a special type of good: They are large-scale, durable, fixed in place, therefore specific, and require a large number of different market operators for their development and management. They also satisfy a demand that in many ways cannot be covered by other goods, while simultaneously involving basic needs. Real estate therefore plays not just an economically important role, but is important in a cultural and often in an emotional sense, too.

As a result of these specificities, real estate market processes move at a comparatively slow pace and involve relatively high transaction costs.

Moreover, real estate markets are interconnected. Changes on the occupier market, for instance, will have effects for the investment and new-build markets, with the corresponding changes in the building stock affecting the occupier market again.

In addition, there are many relations between regional and sectoral real estate markets. Changes on the housing markets will impact the markets for commercial real estate and vice versa, while rising prices in the core cities will also put pressure on the prices in the suburbs, and vice versa.

The sheer number of these connections and the inertia of the market processes can trigger drastic real estate cycles. That being said, the cycles in Germany tend to be comparatively less intense.

The regulation of real estate markets needs to take the specificities of these markets into account in order to make the regulatory effort both efficient and effective.

1.1 Specificities of Real Estate

Economists talk of "normal" goods if demand for the goods in question responds positively to income growth. This appears to be the case with the demand for housing. Most people will look for larger or nicer accommodation when their income rises. According to this view, real estate (in this case, housing) would qualify as normal goods. But this sort of textbook terminology is at odds with the day-to-day experience of most occupiers of residential and commercial real estate, not least because it reduces the complexity of the markets to a single aspect. Fact is that real properties are, in several ways, a special kind of goods. Residential real estate serves truly basic needs, namely the need for shelter and warmth; commercial real estate is similarly essential for businesses as a means of production. For either asset class, it is fair to say that there is virtually no substitute for them. An office building in Hamburg is no substitute for an apartment you need in Bayreuth. Nor will a shopping centre in Bayreuth work as substitute. This means that people and companies depend in their consumption and production activity on availability of real estate in sufficient quality and quantity at the right place or alternatively that they could be raised there.

This actually defines the most conspicuous feature of real estate: It is fixed in place. A regional change in demand cannot be balanced by using existing supply (assuming all other conditions remain as they are). This contrasts with many non-discretionary goods and even many investment products: Textiles and furniture you can pack up when moving from Bonn to Weimar, to say nothing of stocks and bonds, but you cannot pack up a terraced house.

It is a specificity that presents a challenge insofar as another two characteristics of real estate make it difficult to customise: On the one hand, real estate is defined by its large investment volumes, while, on the other hand and in sync with the aforesaid aspect, it is marked by long market effectiveness, meaning life cycle length. Real property is built to last for decades, in some cases even centuries, and for most private households, it generally implies the single biggest investment of a lifetime. By analogy, the same applies to corporates, for whom investments in real estate represent very long-term and capital-intensive decisions, especially because they will define the business activity for years or even decades to come.

This explains why, in economic terms, the financing volumes and the access to funding are highly important for this sector. Chapter 5, below (see specifically Figure 5-2), will discuss the subject in depth.

Another specificity of real estate is that economies of scale play less of a role than is the case with industrial products: The adage "each property is one of a kind," which suggests that there are no economies of scale at all involved in the production and operation of real estate, would be an unacceptable oversimplification, because economies of scale do factor in the production of real estate and even more so in its operation. However, the potential in economies of scale is limited when compared to the industrial manufacturing of consumer goods or simple industrial goods, and by definition they are hardly open to the group of small-scale landlords, which happens to be an important group (see specifically Figure 2-5 in this context). One location is different from the next, the stakeholders involved differ in their respective goals and experiences while occupiers and the regulatory environment vary as well, so that there are very different requirements a given building needs to fulfil. Accordingly, a developer for retail real estate cannot simply change tack to become a hotel developer or employ the experiences he gathered in Germany to become active in the same line of business in France. These peculiarities, the capital intensity, the length of the Sound planning is of the essence, not least because errors are very hard to correct once construction is under way – and the options to control the costs are dwindling rapidly as a project progresses. This is true both for decisions in the public sector, e.g. in regard to the development of new building land, and for private decision makers, e.g. in regard to the concrete design.

It necessitates an advanced and professional division of labour in the construction and real estate industry. The latter requires the professional expertise of engineers, architects, town planners, attorneys, geographers, business administrators and economists who work for a wide variety of companies, including architectural firms, financial services providers, facility managers or project managers. To coordinate all of these players requires time and money, and this is aggravated not least by radical differences between the various groups of owners (or their agents), which range from owner-occupiers and private small-scale landlords, to municipal and cooperative housing associations, and all the way to major listed real estate companies (for a visualisation of provider structures, see specifically Figure 3-15). Hence the usual estimates of the direct transaction costs, meaning the costs of the market process, 10 to 12 percent of which are commonly broken down into estate agent fees, notarial charges and real estate transfer tax, are ultimately but a fraction of the total transaction costs in the management and production of real estate.

The price of any transaction is increased by high transaction costs. They delay or even hamper market adjustments. Indeed, they cause friction losses that filter through to other markets, e.g. the labour market. If the working population has a hard time finding affordable housing (transaction costs included), it can keep them from changing jobs even if it is otherwise the sensible thing to do. There are few exceptional cases where inflated transaction costs would be welcome, for instance whenever lower transaction costs would stimulate the market at an inopportune time. However, this scenario would presuppose extensive and purely speculative or exaggerated transactions that are not backed by proportionate occupier demand.

Of course, the rich diversity of players also implies that estimates as to the size of the real estate industry have to be sourced from the statistical data for highly different economic sectors, and implies above all that the real estate industry generates the second highest gross value added of any sector of the German economy (this being best illustrated by Figure 2-3).

Finally, there is one other peculiarity typical of real estate that slows its regulation and market analysis. Real property lend themselves to the pursuit of both consumption goals and investment targets. The consumption goals are best illustrated by the nature of private homes. If housing was all about accommodation and shelter, flats would need neither gardens nor balconies, and the size of the rooms would be largely as irrelevant as the southern orientation of the windows. But as it so happens, most people are willing to spend good money for such amenities simply because they associate them with a certain consumption purpose. By the same argument, the location of a given flat relative to transportation infrastructure, local supply facilities or attractive green spaces can be valuable for private households because they save commuting costs, open up appealing lines of sight or enhance the quality of leisure options. This suggests in turn that strongly external effects may be associated with some of these consumption purposes. Positive external effects may include, for instance, the appreciation of a given property after a large number of other properties in the same neighbourhood have been refurbished. Conversely, negative external effects could be precipitated by the deterioration of a neighbourhood or if contamination by third parties is discovered. Such compound aspects are highly important for the real estate market and with it for the real estate performance. Occasionally, they even justify state intervention when external factors become too massive to be corrected by private transactions.

This aspect is also important for the second objective that property buyers may be pursuing: The investment target, when real estate is used to generate returns. Home buyers will save on rent, yet they pay interest on their financing arrangements instead. As the saved rent payments add up over time, the property experiences appreciation, so that real estate returns always consist of two components: rental yield and capital growth. Since real estate comes with a lower risk than equities but clearly higher ones compared to gilt-edge government bonds because of the aforesaid uncertainties, the total return for real estate is generally somewhere between that of equities and that of bonds. Accordingly, real estate investments are often a sensible long-term private investment, although they need not take the form of a direct investment (see Chapter 4.2). That owner-occupied residential real estate thus serves two purposes, achieving consumption goals on the one hand and generating returns on the other, is generally understood. But that the same is true for many commercial properties is often overlooked. An office scheme is of course not just a productive resource to provide services. It is also a place where office staff spend a large part of their lives. Since additional factors beyond the sheer existence of a workplace plays a role for high-skilled employees, aspects quite similar to those that qualify residential real estate come into play: comfort, safety, inspiration and location – of course always in correspondence with comparable places in the neighbourhood.

These specificities ensure that real estate markets do follow the fundamental logic of markets, meaning that the quantity structures respond to price changes and that supply responds to demand. However, it is important to highlight, not least with a view to the governing hand of the public sector, that real estate markets in some way work along different lines than stock markets or indeed most markets for consumer goods.

1.2 Specificities of Real Estate Markets

It hardly needs mention that real estate markets are connected to the macroeconomic ups and downs, because the same is true for most markets for consumer goods and investment goods. Chapter 4 of this study discusses the significance of real estate as production factor (see specifically Figure 4-1 in this context).

The demand for real estate (in general) is ultimately influenced by three central economic factors: First: The trend in incomes is important, and with it the trend on the labour markets. Even and especially because real estate qualify as "normal" goods for the purposes of the aforementioned micro-economic nomenclature, demand rises in boom periods, and will drop during a recession. This goes for virtually all real estate investment categories, albeit subject to temporal delays and to differences in degree. The demand for residential real estate is more stable than the demand for office or logistics space because the latter are far more directly related to the economy's production cycle. Secondly: Since real estate, given its sheer dimension, is rarely financed with equity capital alone, and since it represents a commodity of long-term use, demand for it depends on the level of interest rates. Thirdly: Demographic growth makes the creation of additional residential and commercial space mandatory, which explains why sudden hikes in migration flows will trigger drastic shifts in demand on the affected real estate markets.

Important to note here, however, is that the specificities of a given property should be used to make inferences about regional and factual sub-markets. Surging demand in Hamburg cannot be balanced by excess supply in Munich, and expanding the office stock will do nothing to slow down the boost of housing rents. This also implies that the very fixation of real estate in its location can create several different kinds of imbalance. If people were to start moving from Chemnitz to Munich, it would intensify short-term vacancies in Chemnitz and the housing shortage in Munich. Both trends may emerge within the same unified macroeconomic climate, yet they require very different responses by the respective market players and the policy makers. Concrete forecasts for the regional demographics in Germany will be discussed in Chapter 3 (see specifically Figure 3-12 in this context).

Market transparency is compromised by the sheer number and diversity of the many submarkets. The very coarse-grained data that is supplied by the official statistics suggests as much.

To be sure, with regards to market transparency there have been notable improvements in recent years, but for the commercial real estate markets in particular there is still a conspicuous lack of even the most basic market intelligence, such as real estate stock, rental growth, or the trend in vacancy rates. While private providers may be able to fill many of the data gaps, their data tends to be available only to a small number of market players. Asymmetrical distribution of information of this sort can actually precipitate market distortions.

Moreover, the lack of market transparency forces all players to undertake extensive and time-consuming due diligence investigations to review markets and properties. Due diligences are per se a very useful thing to do, but the processes could be sped up by a boost in transparency, and so could the response to imbalances. Instead, the current state of affairs causes development and/or marketing processes to be needlessly protracted. The market's low elasticity of adjustment, meaning the slow response speed in face of emergent market changes, can result in rash cycles on real estate markets. The term "pork cycle," borrowed from agricultural economics, has been used to describe them. If the real estate supply fails to respond in time to changes in demand because of a number of market delays, there is a chance that new supply might actually come too late. For instance, if fresh housing units raised in answer to a rise in demand hit the market of a given city with a delay of several years, the initial surge in rents and prices during the boom phase will be followed by a plunge if demand has declined due to the down-cycle in the meantime.

To cope with this sort of trend, you need to understand that several different real estate markets come into play here. The public debate admittedly simplifies things by talking about the real estate market as if it were a homogeneous whole, but in the context of this adjustment, it makes sense to differentiate between three submarkets: the occupier market, the investment market and the construction market. The occupier market takes centre stage. After all, the value of a property is established by its use. A permanently vacant flat will eventually lose its value.

The same goes for unoccupied offices regardless of location and building quality. The only way for a property to regain its value after a lengthy vacancy is often by putting it to alternative use. The interaction between the supply in space to let and the corresponding demand establishes the so-called headline rent. Prices on the investment markets are closely tied to this rent. Higher rents will legitimise higher prices. But inversely, it is also safe to say that elevated prices are not necessarily backed by a high rent level. Markets are interconnected in a network, but that does not mean they are congruent. Still, whenever prices go up on the investment markets, it will attract property developers and thus cause the construction market to gain momentum, so that, once the reduction of property has been deducted, the supply on the occupier market will increase. In this way, all three markets are closely synchronised. Intervening on the occupier market will influence both the investments in the existing stock and new construction, and vice versa. In this sense, even investment market speculators can be good news for the occupier markets.

But the interconnectedness of real estate markets does not end there. There are close reciprocal effects even between the regional and functional sub-markets. If rents increase in the town core of a city, flat hunters will expand their search into the suburbs or to other cities altogether. This goes for housing markets as much as for commercial real estate markets. Equally safe to say is that enlarging the housing supply in a given region is sensible only if the regional job supply and the concomitant commercial floor area are sufficiently sustainable. Assuming the demand for labour in a region goes up, you need to build not only new offices and manufacturing plants, but also new housing and amenities. If the financial crisis has taught market participants one thing it is that the interconnectedness of real estate markets does not stop at national boundaries anymore. Upheavals on foreign real estate markets can impact domestic markets through interdependencies between them, and by the same logic, migration flows driven by depressed foreign markets can boost demand on the domestic market. In the wake of the financial and economic crisis, unemployment rates in Spain, Portugal, Ireland and many Eastern European countries skyrocketed. People emigrated to Germany by the hundreds of thousands, as the country's budget policy as well as its real estate markets and real estate financing markets proved more stable and facilitated a very quick recovery from the crisis (on the subject of the stability of German real estate financing, see specifically Figure 5-12).

1.3 Implications for the Body Politic

This report provides an overview of the macroeconomic significance of the real estate industry while including no concrete recommendations regarding housing and town-planning policies. However, general messages derived from six different aspects are suggested for consideration by the policymakers:

Real estate represents not just an investment class of very large assets, but the assets are in several ways unique. This is true both for the assets and for the markets. It also presupposes specific know-how and dexterity on the part of the political players.

Real estate markets are slow to respond. Rushed measures are rarely helpful, because their effects may come too late to have the desired effect on the market (see Figure 2-4 for illustration).

Political intervention in real estate markets can have a variety of effects: For one thing, it can have a direct impact on the real estate markets as intended. However, it frequently triggers unintended effects on (other) real estate markets as well, and it is quite common, given the size and the economic significance of the real estate industry, for the effects to spill over into other industries or factor markets. The complexity of the reciprocal effects make them very hard to estimate ahead of time. Accordingly, measures aimed solely at a certain sector – while ignoring potential effects on other areas of activity – should therefore be avoided.

Rather, it makes more sense to enhance the adjustment flexibility. This can be facilitated by lowering transaction costs.

The geographic heterogeneity of real estate markets rarely ever justifies the use of standard measures on a national level.

Increasing the market transparency is needed. It benefits smaller market operators in particular. Expanding the data material that is publicly accessible is therefore of the essence. This goes in particular for commercial real estate.

Chapter 2

Core Data of the Real Estate Industry

Chapter edited by:
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EXECUTIVE SUMMARY

- The real estate industry is one of the largest and most important sectors of Germany's national economy. With a gross value added of more than 500 billion euros, the real estate industry accounts for 18.2 percent of the country's total value added. This makes the real estate industry a far bigger sector than the frequently quoted automotive industry or the retail trade, for instance.

- At the same time, the real estate industry is an extremely small-scale sector with more than 815,000 companies and another 3.9 million private landlords.

- One of the most distinct characteristics of the German real estate industry is its stability. Despite the turbulent macroeconomic parameters created by the crisis of the new economy, the financial crisis and the sovereign debt crisis, the real estate sector has shown a steady performance.

- Compared to other countries, the German real estate industry is more or less average, measured by its share of the gross value added.

- The real estate industry can be delineated in narrow and broad terms. A narrow definition of the sector would include owner-occupiers, landlords, real estate agents, property managers and real estate traders (including property developers), whereas a broader definition would moreover include any company involved in the planning, building, financing and management of real estate during its life cycle.

- The German real estate industry in a narrow sense covers around 300,000 companies which together generated a turnover of 145 billion euros in 2015. This means that the sector accounted for 9.3 percent of all companies and 2.3 percent of all revenues, the companies in the sector being smaller than the macroeconomic average. Its gross value added equalled 302.9 billion euros at the last count or 10.9 percent of the entire German economy.

- Job growth in the real estate industry in a narrow sense has continued since the turn of the century. In 2016, it accounted for a total of 252,000 employees liable for social security while the total number of jobs was 467,000 in the sector.

- Private small-scale landlords earned 55 billion euros in gross revenues in 2015. Since 2011, the number of small-scale landlords has grown by 330,000 to a total of 3.9 million.make it difficult to customise: On the one hand, real estate is defined by its large investment volumes, while, on the other hand and in sync with the aforesaid aspect, it is marked by long market effectiveness, meaning life cycle length.

Chapter 3
Real Estate Stock and Structure

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EXECUTIVE SUMMARY

The purpose of this chapter is to analyse the real estate assets and real estate stock of Germany's national economy.

- Real estate is the most important tangible asset class in Germany. Out of the totality of gross fixed assets (at market prices) in the amount of 17.3 trillion euros at the end of 2016, built-up structures of every kind accounted for 80.3 percent or 13.9 trillion euros thereof.

- With depreciation taken out of the equation, the total net fixed assets of German built-up structures adds up to nearly 8 trillion euros, which breaks down into 4.8 trillion euros in residential buildings and 3.2 trillion euros in non-residential buildings.

- The total asset value tied up in real estate is more than three times as high as Germany's net national income in 2015.

- In absolute figures, Germany thus has the highest value in real estate assets in Europe. But relative to its population total or its total income, Germany only ranks somewhere in the middle among the European countries.

- By the end of 2015, roughly 82.2 million people lived in Germany in well over 41.4 million flats and 19.4 million buildings with a combined residential floor area of around 3.79 billion square metres. At the same time, the working population occupied around 426 million square metres of office space, for instance, 2.8 billion square metres of industrial and logistics space and 123.7 million square meters of sales area in the retail sector (estimates from early 2015). However, these figures are fraught with uncertainty because the commercial real estate stock in particular is inadequately covered by official statistics.

- Home-owning households in the same income group tend to be wealthier on average than tenant households.

- Germany's homeownership rate has made modest gains in recent years. Still, it remains in the bottom segment of the list of European nations with roughly 45.5 percent. In fact, the rate has levelled out or even declined for the younger age groups of less than 45 years since 2013. In terms of capital-building, this could imply a disadvantage for German households.

- A major share of the final energy consumption in the building sector is attributable to activities in properties or relating to them. The efficient use of real estate therefore plays a key role in the effort to bring down Germany's energy consumption. The final energy consumption in German buildings totalled 3,069 petajoules in 2015, a reduction by 11 percent since 2008 that highlights the modernisation efforts of the real estate industry. But further investments will be required to reach the goal of 2,761 petajoules (which would mean 20 percent less than 2008 and 11 percent less than 2015) by 2020.

Chapter 4
Real Estate as Production Factor and investment good

Chapter edited by:
IW Cologne Institute for Economic Research

- Commercial real estate constitutes an essential basis for all sorts of economic activity. Its significance is reflected in 150 million euros in revenues that the real estate industry generated through its dealings with other businesses.

- Property rents and prices serve as key indicators for the appeal of a given city. After all, the willingness to pay high rents or prices rises with the quality of a property's location and of the local infrastructure. In addition, prices also mirror the economic prosperity of a city. The score of a city, understood as a potential model to illustrate the principle, measures the economic performance of a given city. For instance, Munich outperforms Frankfurt and Hamburg in a per-capita comparison. But a city's score may also rise when the floor space supply is actively limited. In which case it would become an indicator of a restricting zoning practice that hampers the economic growth of the city.

- The average household in Germany owns 125,000 euros worth of net fixed assets. Although this tops the average in Greece and Portugal, it falls short of the figures reported from France, Italy or Belgium. The definitive factor to explain the ranking is the low homeownership rate in Germany.

- In addition to directly owned property, however, the property stock market has gained considerably in significance over the past years. There are now 90 billion euros tied up in German real estate using this investment format. Especially the going public of major private housing companies helped to stimulate the market.

- Meanwhile, open-ended and closed-end property funds were busy coping with the regulatory challenges posed by the new national adaption of the Alternative Funds Managers Directive (AIFMD). But both formats registered growth in the wake of the reform, especially with specialised vehicles for institutional investor.

- Of fundamental significance for all investment vehicles has been the strong growth in real estate prices since 2010, most conspicuously so with residential real estate prices in major cities. The threat of a speculative bubble remains nonetheless elusive because there are plausible reasons for the price trend, and because the financing behaviour remains virtually unchanged. However, it needs to be remembered that interest rates, economic situation and demand combine into highly favourable parameters at the moment, and the coming years are likely to bring market adjustments for one or several of these factors.

Chapter 5
Specificities of German Real Estate Financing

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EXECUTIVE SUMMARY

- Driven by a fast-paced expansion of new lending business, the private housing loan volume of 2016 increased by nearly four percent and thus substantially faster than in previous years. In the years since 2003, the annual growth rate had moved in a range of -1 to +2 percent. But even the most recent rise lies still below the long-term average since 1982, which is 4.7 percent.

- Similarly, the current boom is rather modest compared to other countries in Europe. Between 2004 and 2008, the rates of change in Germany's private housing loan volume remained substantially below the European average. The situation in the years thereafter does not lend itself to qualified comparisons because it is distorted by bursting home price bubbles in other countries.

- There is some evidence suggesting that the recent increase in private housing loan volumes in Germany could be due to catch-up effects in the real economy: Rising residential rent rates point to a very real demand for new residential accommodation.

- The favourable economic trend has increased incomes and enabled them to develop in line with the expansion of housing loans. The low level of interest rates has kept the financing of owner-occupied property affordable, which means that borrowers are able to cover their debt service (interest and repayment) out of their income.

- Substantially higher interest rates not to be expected until the European economy as a whole is back up to speed or unless capital drains from Europe; for the time being, an interest rate hike is therefore not to be expected (see elaborations in Chapter 4).

- The spread (margin of the banks) has been under noticeable downward pressure since 2014. As recently as the years 2011 through 2013, the margins in commercial real estate financing had continued to push up. But in 2014 and 2015, margins began to soften, and they remained under pressure in 2016.

- At the same time, the challenges that banks face have intensified due to four different trends: The share of demanding loans has increased (e.g. more project financing, a higher proportion of financing arrangements in Grade B locations and Class B cities, more loans handed out to finance managed properties, etc.). Moreover, the regulatory cost of equity has gone up, and so has the bank levy. In addition, the organisational overhead for meeting the regulatory requirements has increased. These trends suggest higher margin requirements. The fact that these have proven unattainable can be read as a sign for intense competition.

- Meanwhile, bank refinancing remains on sound footing: Investors are buying up covered bonds as ”Pfandbriefe”, and their volume has noticeably increased in the most recent past.

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