Guidelines for Compiling Commercial Property Investment Market Reports

Gesellschaft für Immobilienwirtschaftliche Forschung e.V.
Society of Property Researchers, Germany

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Working group: property market research

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Society of Property Researchers, Germany

Mosbacher Strasse 9
65187 Wiesbaden
Internet: www.gif-ev.de

Telefon (0611) 236810-70
Telefax (0611) 236810-75
E-Mail: ak-research@gif-ev.de

Head of the Working group: Olaf Janssen, Inga Schwarz

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Contents

1. Preamble

There is considerable demand for information about the size and structure of the German commercial property investment market, while the expected standards of completeness and the level of detail in the information are continually increasing. However, the market lacks a consensus regarding terms, definitions and demarcations. With these present Guidelines, gif e.V., the Society of Property Researchers Germany, aims to assist the sector by providing a common structure for the description and analysis of events in this transaction market.

The Guidelines are intended to appeal in particular to all undertakings that record and analyse commercial property transactions and that publish corresponding market reports. At the same time, the Guidelines will assist the readers of such market reports in putting the matters described into perspective.

The recording of transaction events in the commercial property market serves to:

- further increase the transparency of the German investment market
- provide an assessment of the volume of money that flowed into a particular commercial property market during a particular period. In the following, this volume of money will be referred to as the Transaction Volume.
- differentiate the capital invested, for example by property type, classes of investment, types of vendor and purchaser, property quality and other features.
- gather comparables for advisory and valuation purposes.

The Guidelines intentionally concentrate on investments in commercial properties. The suggested definitions and characteristics are therefore of only limited applicability to residential property transactions.

2. Recording property transactions

2.1 Definition of a property transaction

A property transaction must fulfil all the following conditions:

- change of owner
- notarised contract of sale
- payment of a purchase price
- acquisition of property as the purpose of the transaction

Within the meaning of these Guidelines, property is:

- Existing property: Purchase of a developed site or the buildings situated on a site (ground leasehold)
- Development projects: Purchase of buildings that are yet to be developed or are in course of construction (both newbuild and full refurbishments)
- Development sites: Undeveloped properties, on which commercial development is planned

Not to be regarded as property transactions within the meaning of these Guidelines are, inter alia:

- strategic company takeovers (i.e. in which property is not the centre of the transaction)
- trading in debt portfolios
- Initial public offerings (IPOs), increases of capital and everyday stock exchange dealings
- transactions between companies associated under company law, not involving payment of an arm's-length purchase price

Should operations that are not defined herein as property transactions nevertheless be registered and published in the market report, they are not to be included in the transaction volume (see section 3.1) but must be identified as separate items (e.g. "Market volume IPOs").

2.2 Recommendations for recording property transactions

2.2.1 Relevant transaction data

In the registration of transactions, the following elements will normally be compiled as standard:

- Date of transaction (see section 2.2.2)
- Type of transaction: asset or share deal and/or individual property or portfolio transaction (see section 2.2.3)
- Purpose of investment (see section 2.2.4)
- Address(es) of the property/ies
- Type(s) of use (see section 2.2.5)
- Lettable area gif (in this respect refer to “Guidelines for Assessing the Lettable Area of Commercial Accommodation (MF/G)", if possible differentiated by types of use
- for development sites: Site area
- Names of the vendor and purchaser
- Types of vendor/purchaser (see section 2.2.6)
- Origin of vendor/purchaser (see section 2.2.7)
- Purchase price (see section 2.2.9)
- Yield / rental multiplier (see section 2.2.10)

Other elements could include:

- Origin of the capital (see section 2.2.8)
- Risk classification of the property transaction
- Lease length(s)
- Vacancy
- Submarket
- Sustainability certification

2.2.2 Date of registering a transaction

For the registration of a transaction, the date of conclusion of the sale contract (“signing”) is to be adopted. Where there are clearly defined rights of rescission or if board approval is still pending, the effective date should be rechecked in order to determine whether the contract was actually finalised ("closing"). If not, the data must be corrected accordingly.

The date of signing the contract is also the decisive date for recording a transaction, even if this does not become known until a later reporting period. The initial data (even if it has already been published) must then be appropriately corrected retrospectively.

2.2.3 Types of property transaction

Firstly, property transactions should be differentiated between direct and indirect investments (Asset vs. Share Deal).

- A direct investment (Asset Deal) is an investment in a separable property on the basis of a notarised contract of sale, with entry in the land register (*Grundbuch*).
- An indirect investment (Share Deal) involves the acquisition of shares (greater than 0 to 100%) in a property holding company or a property company (including stock-market listed companies)("corporate acquisition").

Distinction can also be made between transactions in individual properties and portfolio transactions.

- An individual property transaction involves the acquisition of a commercial property or a development site.
- A portfolio transaction involves the acquisition of at least two spatially-separated properties.

2.2.4 Purpose of a property transaction (purchaser's view)

The following purposes of investment by the purchaser in a property transaction may be differentiated:

- Owner-occupation
- Investment (as capital investment; including so-called "forward deals")
- Development or revitalisation (construction or revitalisation of a property with the aim of reselling it within a short period of time)

2.2.5 Differentiating the transaction volume by types of use

Each transaction must be assigned to a type of use. As information regarding rental income is often not available in the German market, for pragmatic reasons gif recommends assigning the type of use to the dominant proportion of the floorspace, i.e. a property with several types of use will be assigned to the type of use that occupies at least 75% of its floor area. In a completely transparent market, however, classification on the basis of rental income would be preferable, i.e. a property with several types of use would be assigned to the type of use that generates at least 75% of its rental income.

The following classifications are recommended for **existing properties and developments**.

- **Office buildings:** Buildings with at least 75% office space. An office building situated in a shopping location, provided that there is retail occupancy at least on the ground floor, should be classified as a commercial building (see Retail properties).
- **Retail properties:** Properties with at least 75% retail space. This includes, inter alia, shopping centres, stand-alone retail warehouses, retail warehouse centres, stand-alone supermarkets, discounters, department stores and Cash & Carry stores. This category also includes so-called commercial buildings, which are properties with mixed use, including retail or similar services oriented to the public in the lower floors and office and/or residential accommodation on the upper floors, in town- or city-centre shopping locations or district shopping locations. The retail portion of such properties may be less than 75%.
- **Logistics and warehouse properties:** Properties with at least 75% storage and/or logistics space
- **Hotels:** Properties with at least 75% hotel occupation.
- **Mixed-use:** Mixed-use properties, in which no use type occupies a proportion of at least 75% and which are not commercial buildings or commercial parks.
- **Other** (residual category), e.g.:
    - Health and social properties (inter alia care homes, hospitals, schools and kindergartens)
    - Production buildings (inter alia factories, workshops)
    - Buildings for research, training, trade fairs
    - Leisure properties (inter alia stand-alone sports/fitness centres, cinemas, events centres/arenas)
    - Commercial parks (mixed-use office/"service"/storage space, with more than 25% of "service"/storage space)
    - Car park buildings

The decisive factor for the use type classification is the use at the date of purchase, irrespective of whether the purchaser plans to change the use.

Development sites will not be assigned to a type of use but listed in an independent category.

The above recommendations apply in equal measure to individual property and portfolio transactions. If, at a later stage, the individual properties in a portfolio are assigned to different geographical areas, the use classification at individual property level must also be carried out at the latest by that time.

Transport and infrastructure properties (e.g. solar and wind energy parks, bridges, underground storage facilities), which have increasingly attracted interest by institutional investors in recent years, are not included in property for the purposes of these Guidelines. Should they nevertheless be registered, they should be shown separately in the market report and identified as infrastructure properties.

2.2.6 Differentiation of the transaction volume by types of vendor and purchaser

Typically, the following types of vendor and purchaser can be distinguished:

- Private investors (individuals, Family Offices, asset administrators)
- Insurance companies
- Pension providers
- Pension funds

- Sovereign wealth funds
- Open-ended mutual property funds
- Open-ended special real estate funds
- Closed-end real estate funds
- Private equity funds / opportunity funds
- Other funds
- Fund managers (serves as a residual category if the type of fund is not definitively known)
- Stock-market listed property investment AG / Real Estate Investment Trusts
- Non-quoted property companies (e.g. property management and holding companies)
- Banks
- The public sector
- Developers
- Corporates
- Charitable institutions
- Other
- Not known

Some of these types of vendors and purchasers, e.g. open-ended special property funds and REITs, function as financial intermediaries, i.e. they gather funds from other parties and invest them in property. When such financial intermediaries appear as vendor or purchaser, the corresponding vehicle rather than the source of the funds should be registered (e.g. if a special fund purchases for a pension fund, the special fund should be recorded as purchaser).

2.2.7 Differentiation of the transaction volume by origin of the parties concerned

The countries of origin of the parties should be registered. The classification should be oriented to the head office of the party appearing as vendor / purchaser (e.g. the open-ended retail fund (headquarters of the financial investment management company) and not the issuing bank; the fund manager and not the pension provider providing the capital).

2.2.8 Differentiation of the transaction volume by origin of the capital

As well as the origin of the parties, the origin of the funds can also be registered. For direct investments the origin of the funds corresponds to the origin of the purchaser. For financial intermediaries, the decisive factor is the origin of whoever made the funds available. For example, if an Austrian pension provider makes an acquisition via a German special fund, the country of origin should be registered as Austria and the type of investor as “pension fund”.

2.2.9 Purchase prices

When registering the purchase price, the net purchase price should be adopted. According to the commentary by the “Real Estate Investment Management“ working group, the net purchase price represents the consideration payable by the purchaser, including any liabilities taken on, in accordance with the purchase contract or other binding document.

The net purchase price is exclusive of ancillary costs of purchase related to the property (typically these include Grunderwerbsteuer (transfer tax), notary’s and legal fees and, if appropriate, agents’ fees).

2.2.10 Statements/definitions of Yield

For each transaction the initial yield, based on the rent currently payable, should be registered. A distinction may be made between:

Gross initial yield (GIY):

$$\frac{(\text{initial monthly contractual rent x 12})}{\text{net purchase price}}$$

Net initial yield (NIY):

$$\frac{(\text{initial monthly contractual rent less non-transferable costs) x 12}}{\text{net purchase price+purchaser's costs}}$$

N.B.
The gif Real Estate Investment Management working group has produced detailed definitions of the various yield terms and yield calculations, to which your attention is expressly drawn: gif Guidelines “Yield Definitions”, www.gif-ev.de

3. Recommendations for compiling market reports

3.1 Fundamentals of reporting

A (market) report at aggregated level can only be produced if the elements stated in Chapter 2 have been registered at transaction level. Information normally provided at aggregated level includes:

- Total transaction volume, i.e. the sum of the purchase prices of all registered transactions
- Transaction volume distinguishing between e.g.: Types of use, locations, types of vendor/purchaser, origin of vendor/purchaser, type of transaction (e.g. transaction volumes in individual properties and portfolios)

The following indicators are also often identified:

- (prime) yields or rental multipliers (100/(prime) yield: see Section 3.3)
- Capital value in Euro per square metre (the product of the annual rental value and the market rental multiplier)

3.2 Area covered and period for assessing the transaction volume

Market reports concerning commercial property transactions should relate to a clearly defined market area. As, depending on the compiler of the report, market areas having similar names may be differently defined (e.g. the Berlin market area may or may not include nearby municipalities such as Potsdam or Schönefeld), the transaction volume should be reported not only for the whole market area but also separately for each eponymous town or city in its administrative boundary. This makes it easier for the reader to compare the volume of transactions stated in different market reports with dissimilarly-defined market areas.

N.B. For transactions involving property portfolios, in which the properties are distributed over a number of locations, each individual property could be ascribed to a particular location or a defined region - provided that the information is available and it is feasible to do so. In determining the individual values estimates are allowable, however this must be made clear in the report.

gif recommends that the period of coverage for market reports and purposes of comparison should be based on a calendar year, and/or one or more quarters.

3.3 Yield statements in market reports

For consideration of the market (aggregation level) the concept of prime yield is of particular importance, as it enables comparison between periods and between regions. On the basis of the gross and/or net initial yields referred to in the section "Yield" above, the following definitions apply:

The achievable prime yield, in accordance with the normal international methodology, constitutes the standard definition. This is defined as the lowest yield that can be expected to be achieved at a particular date for a property of top quality, fit-out and location that is let (to good covenants as tenants) in line with normal market conditions. It reflects assessment of the market on the basis of up-to-date knowledge of supply and demand, as well as transactions that have been concluded. gif recommends that net initial yields should be stated. As an alternative, rental multipliers (as a reciprocal of the gross initial yield) may be stated.

The market report should state which of the definitions of yield in the section “Yield” have been applied.

4. Appendix: Example transactions (with annotations)

Example 1:

In 2011 CBRE Investors acquired the ING Group's real estate division.

This is not a property transaction within the meaning of these Guidelines, as it is a strategic company takeover. The properties still belong to the fund companies and therefore to the fund investors.

Example 2:

In 2012 Unibail-Rodamco acquired shares in mfi and therefore also in the shopping centres and developments held by mfi.

This is a property transaction, because Unibail-Rodamco wished to gain entry to the German retail property market via its participation in mfi. The properties were therefore the main purpose of the transaction.

Example 3:

As part of a credit restructuring, Arminius has acquired the controlling majority in two funds in a Eurocastle German portfolio (the so-called Mars Portfolio: 28 properties worth around 1 bn Euro). 75% of the shares were acquired in 2011, the remaining 25% in 2012.

This example is not to be regarded as a property transaction: it is a purely credit deal, which is not focussed on the properties.

Example 4:

In 2012 IVG AG sold two office properties in Unterföhring to IVG Private Funds, for a closed-end fund. At the end of 2011 the properties had been transferred from the IVG Immobilien Management Holding to the two property holding companies.

The transfer of the properties from the holding (company) to the two property holding companies was only carried out in preparation for sale: it was therefore not a property transaction.

In contrast, the sale of the properties from IVG AG to the fund is to be treated as a property transaction, even though the properties were transferred between two associated companies. In this case it can be assumed that the vendor and purchaser had opposing interests, particularly as a purchase price in line with the market was paid.

Example 5:

In 2011 Union Investment acquired 25% of the shares in the Limbecker Platz shopping centre in Essen from Karstadt, adding to its previous 60% holding.

This case is representative of proportionate acquisitions of property holding companies. Regardless of the size of the share acquired and irrespective of whether or not the purchaser already owned any shares, such share acquisitions are property transactions for the purposes of these guidelines. In such cases the transaction volume to be adopted is the purchase price paid for the shares acquired (not the resulting value derived for the whole property!). The lettable area will also be applied in accordance with the proportion acquired - in the subject case 25% of the total lettable area.

Examples of origin of the parties / origin of the capital

a) Prime Portfolio: A Luxembourg special fund, launched by IVG, the investor in which is a single German pension fund, acquires several properties in Frankfurt and Berlin. IVG has a 5% share as co-investor and undertakes the asset and property management of the properties.

   At the level of the parties:
   The type of purchaser is a special fund; the origin is Germany (headquarters of the IVG)

   At the level of the capital:
   Type of purchaser 1 (95%) is a pension fund and pension provider; Origin 1 is Germany

   Purchaser type 2 (5%) is a listed property investment AG; Origin 2 is Germany

b) A German special fund, launched by IVG, acquires the Galileo office tower in Frankfurt. The capital for the special fund comes from several institutional investors from South Korea.

   At the level of the parties:
   The type of purchaser is a special fund; the origin is Germany (headquarters of the IVG)

   At the level of the capital:
   The type of purchaser is a pension fund; the origin is South Korea

c) Art-Invest Real Estate Funds purchases the Kö-Bogen in Dusseldorf for two German pension providers.

   At the level of the parties:
   The type of purchaser is a special fund; the origin is Germany

   At the level of the capital:

   Type of purchaser is a pension fund and pension provider; Origin is Germany