SKJERVEN GROUP - *Monthly Newsletter*

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Building Code: Many exceptions to the conversion ban

The Building Land Mobilization Act has come into force and includes amendments to both the German Building Code (BauGB) and the German Land Use Ordinance (BauNVO). It is primarily intended to expand the scope for action of municipalities in tight housing markets.

The so-called conversion ban, which has long been controversial but does not rule out conversions, has been newly inserted into the Building Code as Section 250. Accordingly, in tight housing markets, municipalities can prohibit the conversion of rental apartments into owner-occupied apartments until the end of 2025. However, there are several exceptions. According to the amendment to the building code, conversion can take place if a residential building has no more than five apartments. The states are allowed to set a different number, ranging from three to 15 apartments. Municipalities must also approve a division if at least two-thirds of the apartments are sold to tenants, if apartments are sold to members of the owner's family for owner-occupancy, or if residential or partial ownership is to be created for the benefit of heirs in the event of inheritance. Moreover, economic emergencies are considered an exception.

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Prerequisite: Tight housing markets

As with the conversion ban, the prerequisite for other innovations is that a housing market is tight. Tight markets can be defined by state governments by statutory order under §201. This ordinance is valid until the end of 2026 at the latest.

Other Innovations

In order for more apartments to be built, it should also be possible to deviate from the development plan in tight markets - taking into account neighboring interests. In the BauNVO, a higher building density and a new area category "village residential area" are planned.

Section 13b of the BauGB is to be extended until December 31, 2022, making it easier for municipalities to designate building areas in outdoor areas.

In addition, municipalities will be able to exercise their right of first refusal in the case of undeveloped and fallow land if the land is to be used primarily for housing. It will also be easier for them to issue building bans. However, owners must be able to justify the construction measure from an economic point of view.

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Residential Real Estate prices increased by 9.4 percent

According to the German Federal Statistical Office, residential property prices have risen in both major cities and rural areas.

The house price index compiled by the Federal Statistical Office (Destatis), which includes residential property prices, rose by 9.4% from the first quarter of 2020 to the first quarter of 2021. Houses and apartments became more expensive both in rural areas and in cities. The largest price jumps had been observed with 11.3% for single-family and two-family houses in sparsely populated rural counties and also with 11.3% for apartments in large cities over 100,000 inhabitants. Dwellings in the seven largest metropolises rank however not far behind. In these, the price jump amounts to 11.1%.

The house price index also includes ancillary acquisition costs. These had fallen by 0.3% compared with the same quarter of the previous year due to the "Act on the Distribution of Brokerage Costs in the Brokerage of Purchase Agreements for Apartments and Single-Family Houses", which came into force at the end of 2020, according to Destatis.

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Office rents lag behind construction prices

Normally, the development of office rents follows the rise in construction prices. However, according to JLL, a significant gap opened up between the two values in the first quarter of 2021.

Since 1987, construction prices in Germany have risen by 124%, while office rents have increased by 106%, as calculated by the analysts at JLL. The relative gap is normally not only closed by the value increases of the properties, but partly overcompensated, emphasizes Helge Scheunemann, Head of Research at JLL Germany.

At the end of this long time series, however, there is now a deviation, because here a gap seems to open in favor of the construction prices. JLL has calculated a plus of almost 4% in construction prices in the first quarter of 2021, while office rents stagnated at the same time. JLL researcher Scheunemann fears that high construction prices could have a negative impact on the office pipeline. This, in turn, could lead to a relative shortage of supply and thus to an upward price trend for existing properties.

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Rents to rise in the long term due to construction costs

However, JLL's head of research expects the recent divergence to remain the exception to the rule. Construction prices would continue to act as a driver for rising rents. Their upward trend could even intensify in the event of a recovery in demand for office space.

The price increases in the construction sector are largely due to higher raw material costs. On the commodity exchanges, steel products, copper, insulation materials, plastics, gypsum and wood have recently recorded peak values. The reasons for this include worldwide logistics problems, as the pandemic had disrupted global supply chains.

Analyst presents scenarios for office space demand

How will the trend toward home offices affect demand for office real estate in the coming years? IMMOBILIEN ZEITUNG reports on a webinar in which DB Research presents two scenarios.

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At the end of June, the government's home office requirement in Germany will be eliminated. Still, not all employees are likely to return to the office to the same extent as before the pandemic. Two possible scenarios for the development of the corresponding demand for space in 126 A,B,C and D cities were presented by Jochen Möbert of Deutsche Bank Research at the webinar.

It was important for the macroeconomic analyst to emphasize that the report did not represent a forecast with regard to the statements derived from his research. He said the situation was too uncertain for that in view of the pandemic. The scenarios are based on three variables in addition to the number of office employees and the space required per employee. These are the home office quota, i.e. the proportion of office employees who work from home, the home office intensity, i.e. the proportion of weekdays they spend there, and the corresponding distribution over the weekdays.

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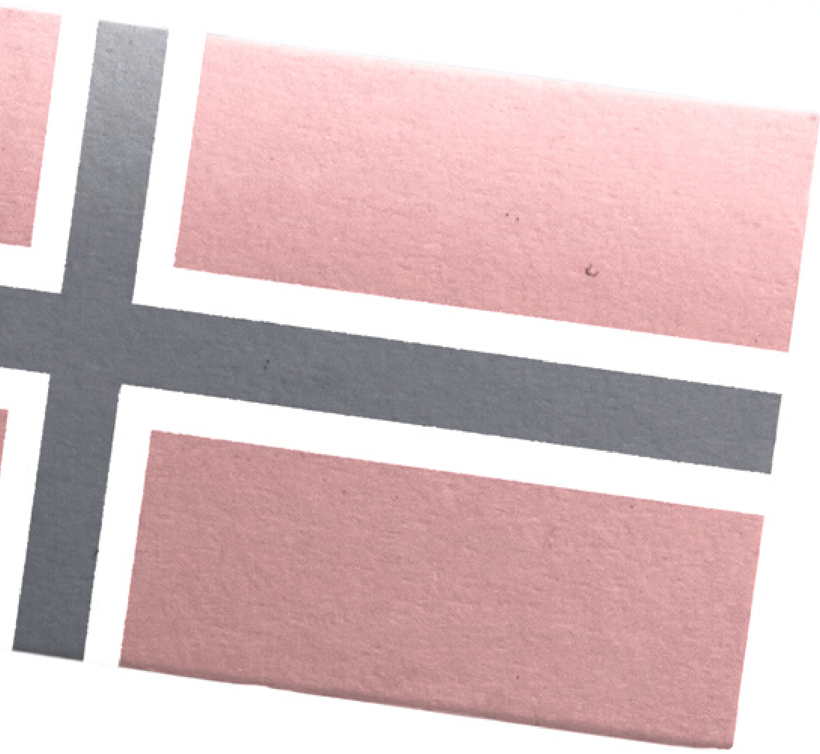
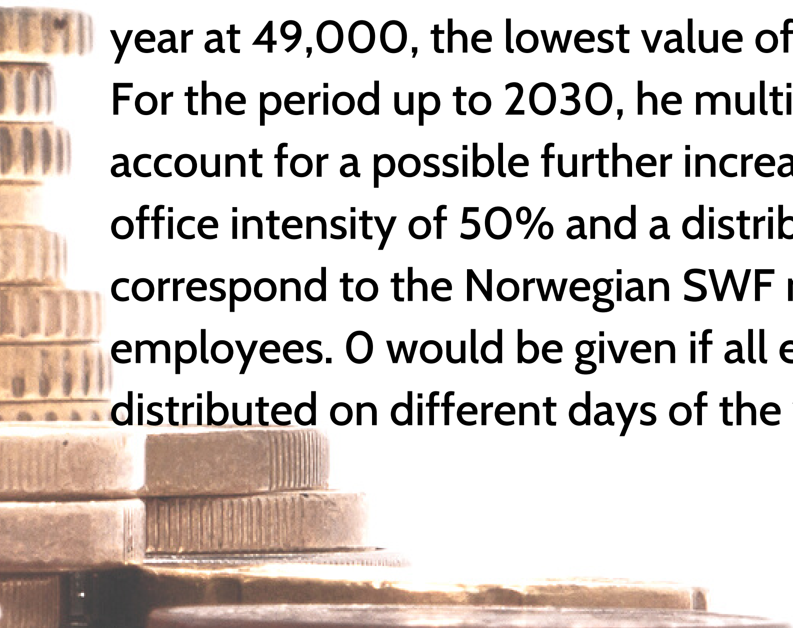
Norwegian sovereign wealth fund as a model



Möbert used the example of the Norwegian sovereign wealth fund to illustrate the impact of this last aspect. There, office employees would still be allowed to work in their home offices in the future. However, they would all have to come to the office on the same day of the week. So at least the same space is needed as before Corona.

Möbert assumes there are currently 7.8 million office workers in the 126 cities he studied. By 2021 and 2022, he expects the average home office ratio to be 29%. By the end of the decade, it could even be as high as 35%. He also expects office space requirements to reach 23.3 square meters per employee.

In his first scenario, Möbert sets the increase in office employees per year at 49,000, the lowest value of the ten years up to 2019 from 2010. For the period up to 2030, he multiplies the home office ratio by 1.2 to account for a possible further increase. Möbert also assumes a home office intensity of 50% and a distribution indicator of 0.6. Here, 1 would correspond to the Norwegian SWF model with a fixed day for all employees. 0 would be given if all employees came to the office evenly distributed on different days of the week.



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Second scenario more likely

In 2019, office space demand in the 126 cities surveyed was 180.6 million sqm. In the first scenario, after a corona-induced slump in 2020 and 2021 and a subsequent partial recovery, it rises again only very slowly. Thus, it only reaches a value just above 170 million sqm by 2030. In the second scenario, demand would rise to 197.3 million sqm by 2030.

There are also major differences between the two possible developments in terms of rental growth, based on the expected vacancy rate. It is true that peak and average rents are almost identical in each case.
In the first scenario, however, growth would remain negative until 2028. In the second scenario, the value would be positive again as early as 2022, but would only be around 2.4%. By way of comparison, rental growth in 2019 was around 8%, according to Möbert.

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Market for hotel investments remains subdued for the meanwhile

Investors and banks will remain cautious about hotel real estate for the foreseeable future. This is due to the fact that the development of the industry is difficult to predict. After all, no one knows yet when the state aid will have to be repaid, how solvent the operators are and how valuable the current lease agreements are.

According to an analysis by the consulting firm mrp Hotels, the first half of 2021 was an extremely quiet one in terms of large-volume transactions in the hotel sector. Just two notable sales were recorded in Germany, Austria and Switzerland: In Stuttgart, the Turm am Mailänder Platz project, operated by Adina Hotels and Premier Inn, was sold for around 137 million euros, and in Frankfurt, the Villa Kennedy of operator Rocco Forte was sold for an amount in the upper double-digit millions.

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mrp Hotels does not expect to see a rapid increase in transactions or portfolio adjustments in the second half of the year. On the one hand, government aid continues to be paid out and on the other hand, the quality and financial strength of the operator remains difficult to assess.

Banks remain cautious about financing

The global economy is currently characterized by skyrocketing prices for raw materials and thus also for construction materials. This is significantly delaying projects that were already being implemented before the pandemic, as the cost buffers on the construction side, which are usually planned anyway, have been exhausted or are not infinitely scalable. Financing also raises many question marks at present. The difficult assessment of the recovery phase as well as the non-existing limited assessment criteria of the recoverability of leases often make it impossible for banks to finance projects.

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MOVIKHEIA

Contemporary Cottages on Picturesque Island in South-Norway

For Sale

On the Norwegian southcoast, facing the Skagerrak and inbetween Raet national park, lies the enchanting island Borøya. On this idyllic island in Tvedestrand, sixteen intriguing contemporary cottages are being built. Relaxed and open cabins with vast windows that frame the spectacular sea views.

With 66 sqm of living space over two floors, they are built from high quality and maintenance free natural materials. The cottages will be placed about 130 metres from the shoreline on an untouched plot of land of 14-acre with sea view.

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Access to the cottages is via car-free footpaths. The parking spaces are located on the neighbouring plot to the east. Hagefjorden Brygge is about a 10-minute walk from the cabins. There you will find the the island's main marina, a restaurant, kiosk and ferry terminal to the neighbouring island.

In the summer season, the costal gems Tvedestrand, Borøya, Sandøya and Lyngør offer a wide assortment of cultural activities; music and bookfestivals, concerts etc. At your cottage you can enjoy "simple luxury" and reading a book on the terrace or active recreation. The cottages, including parking space are sold at fixed prices from 4,350,000 Norwegian kroner (about 427,000 euros).