pbbIX
Office Property Market Germany
2024 | Q3

DEUTSCHE PFANDBRIEFBANK

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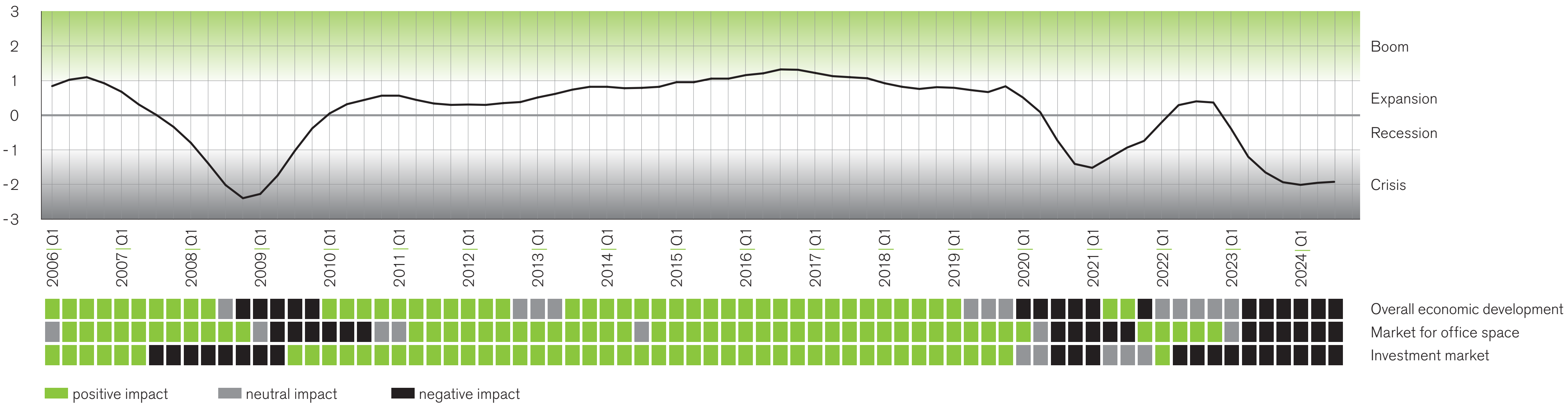
Overview

Having arrested the decline prevailing since the end of 2022, the pbbIX **continued its tentative recovery in the third quarter of 2024, reaching an index value of -1.92.** Germany's office real estate markets remain in a **bottoming-out** phase. Economic output declined in the second quarter but staged a surprising recovery in the quarter under review. General economic weakness and ongoing structural changes as to how office space is used meant that **demand for office space remained below average**, while **investment market turnover further declined quarter-on-quarter,** remaining on a very low level. Initial yields remained stable during the year to date; capital values only rose marginally on account of continued rent increases. Despite the initial round of interest rate cuts between June and October 2024, market participants are still uncertain as to how economic and inflationary developments will pan out. This means that overall activity on the office markets is going to remain muted.

The **German economy grew slightly – by 0.2 %** – in the third quarter. According to ifo research institute's autumn 2024 economic forecast, GDP for the full year is still expected to stagnate. Growth prospects for the coming months are likely to be rather subdued. Overall, the lack of orders in manufacturing industry remains a key issue: capacity utilisation has continued to decline in recent weeks and business expectations in the general construction sector have deteriorated. The plain fact is that Germany's economy is stuck in a slump: in these circumstances it is no surprise that demand for office space remains depressed.

pbbIX BIG 7 | Index



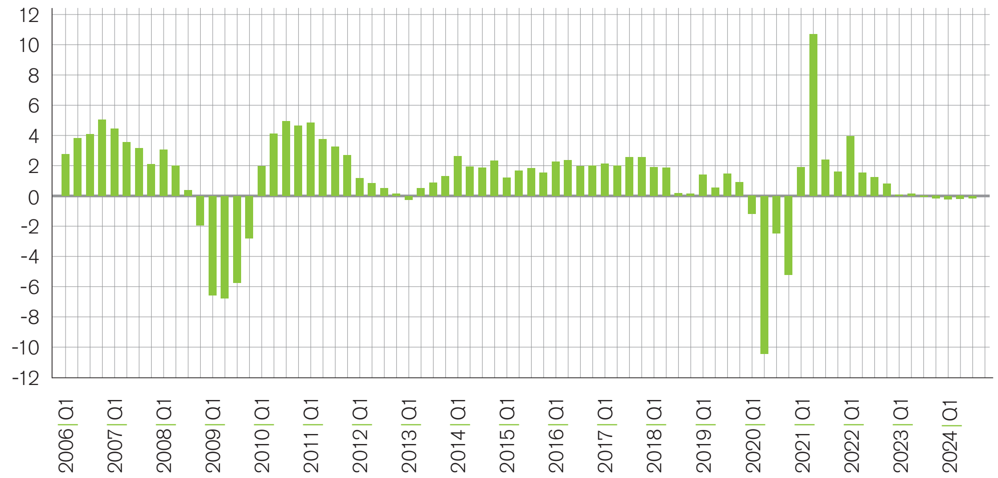
Overall economic outlook

Germany's **economy remains mired: real economic output** which was still showing q/q **growth** of 0.2% in the first quarter of the year, shrank by 0.3% in the second quarter. According to preliminary figures , **GDP rose by 0.2% in the third quarter**. Figures from the German Federal Statistical Office indicate that the increase was mainly attributable to government spending and private consumption.

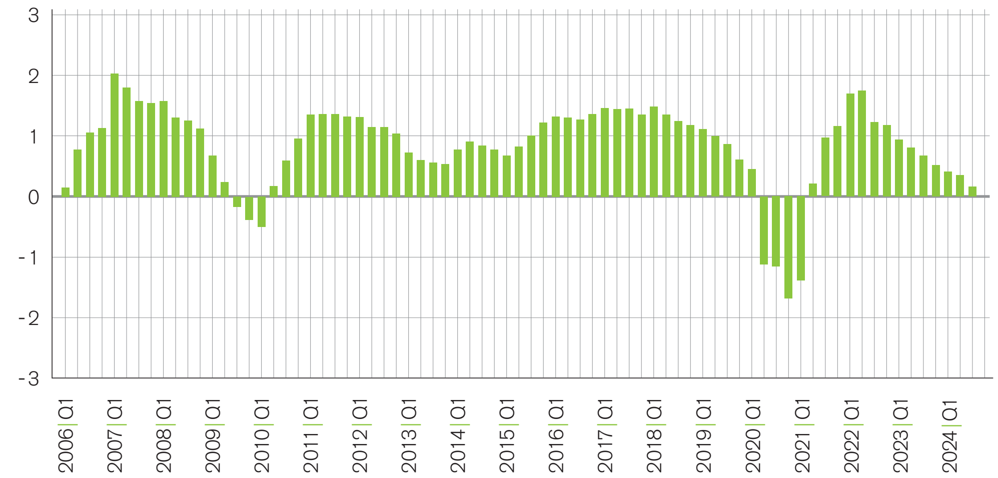
Inflation was below the ECB's target in August and September, at **1.9% and 1.6%**, respectively; preliminary figures for **October** indicate that it regained the **2.0% level**. An inflation rate in line with the ECB's target and a labour market that remains stable should bode well for recovery, but the **sluggish economic development** is now **burdening the labour market**: despite the number of people employed increasing by 75,000 year-on-year in the third quarter of 2024, the positive momentum is clearly slowing. At **6.0%, the current unemployment rate** remains modest.

The macroeconomic **outlook** for Germany **has deteriorated in the third quarter**. Business sentiment has improved overall: following four consecutive declines, the Ifo business climate index rose again for the first time in October. It was only in the general construction sector that the mood remained subdued. Business expectations for the next six months brightened somewhat in October, yet scepticism remains.

Real gross domestic product | year-on-year change in %



Working population | year-on-year change in %



Market for office space

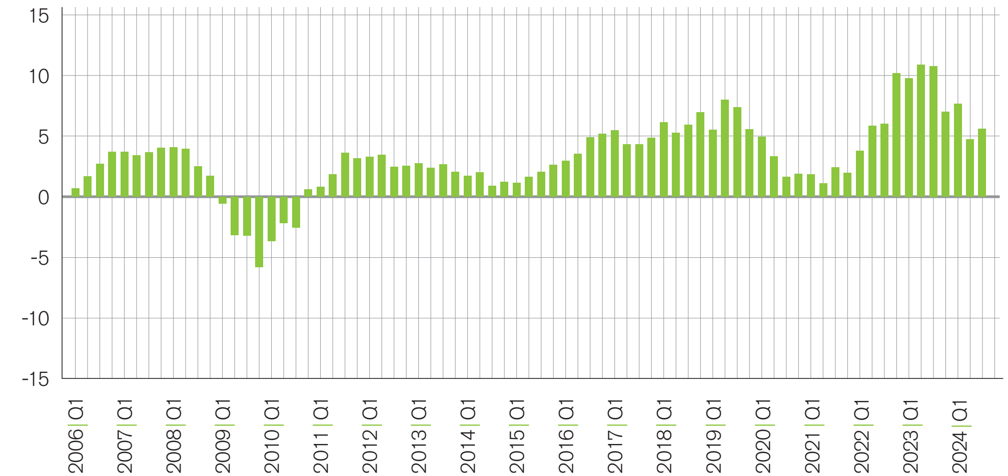
As with the German economy overall, the big 7 **markets for office space continue to suffer from sluggish demand**, evidenced by rental development. Despite rising slightly in the third quarter compared to the weak previous quarter, take-up remained low at 730,000 sqm. All in all, only 2.0 million sqm office space was let in the first three quarters of the current year. While this exceeded the 1.8 million sqm recorded in the same period of the previous year, the figure still undershot the 10-year average by 20%. Performance in the cities showed a very mixed picture: Hamburg and Dusseldorf saw year-to-date rental performance decline by 7% and 5%, respectively, while Stuttgart and Munich posted increases of 36% and 34%.

Against the background of below-average demand and a high completion rate, **average vacancy rates across all markets rose** by 40 basis points against the previous quarter, to reach 6.6%. Figures for the individual markets ranged from 4% in Cologne up to 9% in Frankfurt and even in excess of 10% in Dusseldorf. New construction activity in the first nine months of the year led to the completion of approx. 1.2 million sqm of office space, which is 40% more than in the previous year.

In line with the demand for high-quality space, rents for first-class properties in prime locations continued to trend upwards. Top rents in the third quarter of 2024 exceeded the previous year's figure by 5.5%. Competition for prime space in central locations with good accessibility remains strong and will once again drive rental growth upwards in the prime segment between now and the end of the year.

Office space vacancies (BIG 7) | in % of the portfolio

Top rents (BIG 7) | year-on-year change in %



Investment market

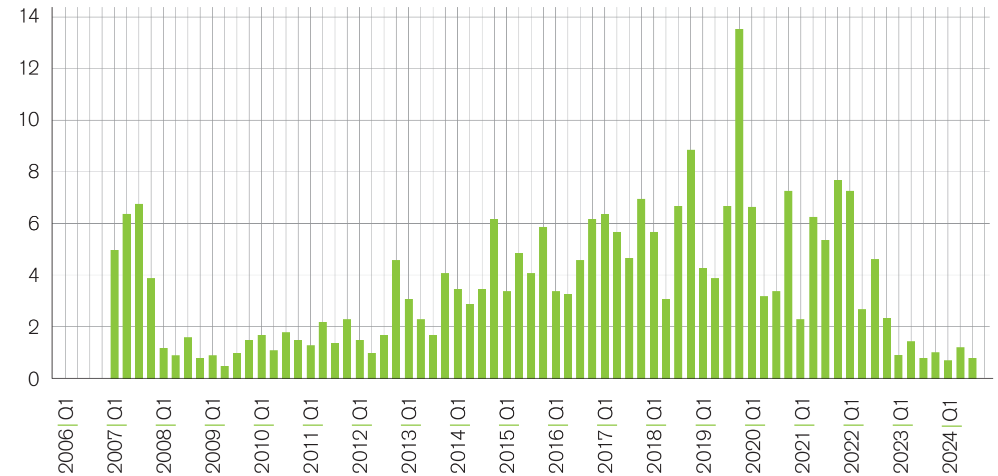
The recessionary development on the office investment markets persisted during the third quarter. Cash inflows remained low, posting a **significant 40% decrease from the previous quarter**. Aggregate investment volumes of approximately €2.7 billion for the first nine months were down by around 12% year-on-year. To put this into perspective: nine-month volumes in the years 2017 to 2022 ranged between €13 billion and €17 billion. Inflow levels as low as in the current year have not been seen since 2009. Interest rate cuts have started in Europe and the US, signalling a market recovery. However, investment markets are still in decline, labouring under the ongoing process of finding price equilibrium, high borrowing rates, steep construction costs, the persistently weak performance of office markets and a stagnant economy.

Yields for first-class properties have been **trending sideways since the beginning of 2024**: it now looks as though they have peaked in the current cycle. The average across all big 7 markets stands at 4.28%, i.e. it has not moved since the beginning of the year. The yield spread against the current yield for 10-year German government bonds stood at 200 basis points at the end of the third quarter, compared to around 150 basis points twelve months ago.

Structural problems on the office markets are compounded by **uncertainty regarding economic developments**. Any recovery of investment markets is likely to be moderate over the coming quarters, and very vulnerable to crises.

Net initial yield (BIG 7) | in %

Investment volume (BIG 7) | in € billion

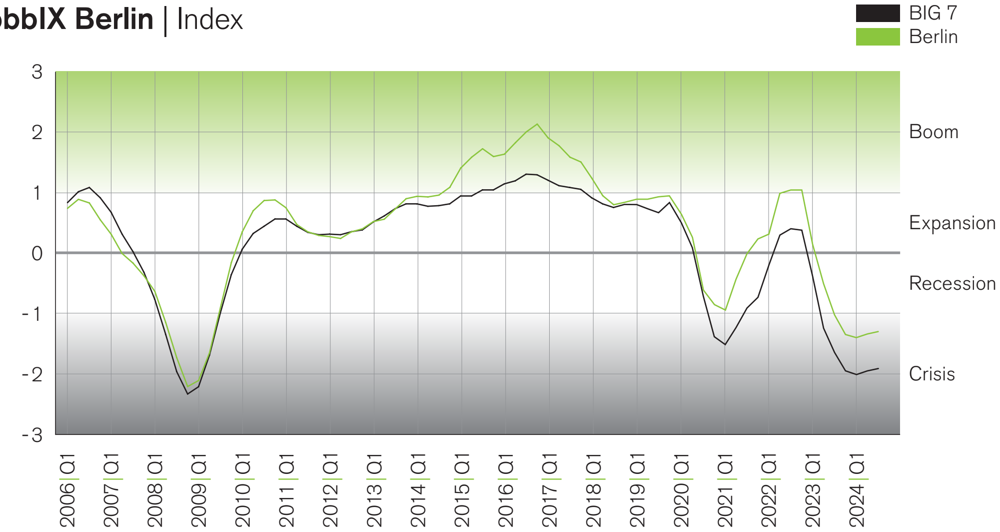


BIG 7

BERLIN

Third-quarter office space take-up in Berlin stood at 147,000 sqm and was in line with the previous two quarters. The year-to-date figure of approximately 440,000 sqm exceeded the previous year's figure by some 10 %, but the persistent difficulty of office space marketing is driving up the vacancy rate – which rose by 70 basis points in the third quarter, to reach 6.3 %. The top rent rose quarter-on-quarter to €45 per sqm. Investment market inflows continued to decline: transaction volumes year-to-date of approximately €480 million only amount to half the previous year's level. At 4.2 %, the net initial yield for first-class properties has remained stable so far this year.

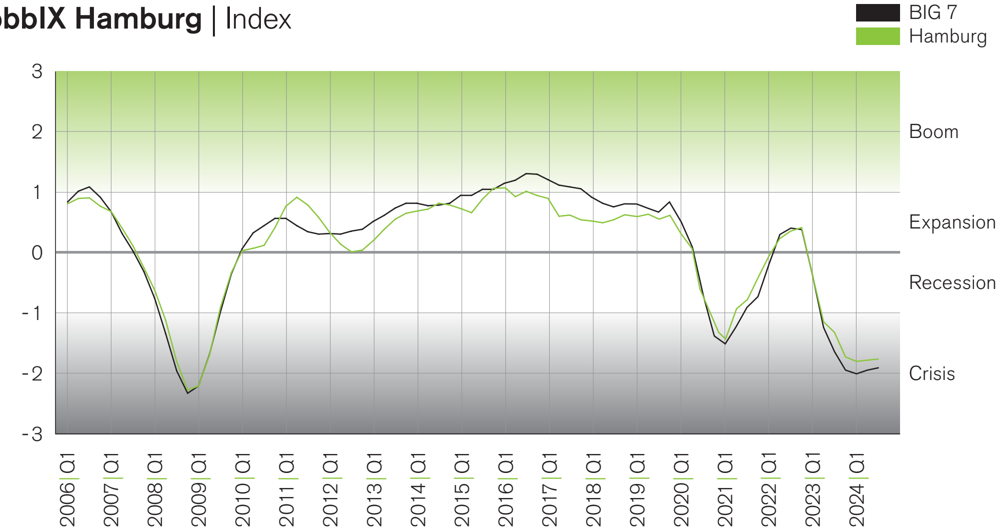
pbbIX Berlin | Index



HAMBURG

Letting performance in the Hamburg office market improved moderately in the third quarter, leading to year-to-date take-up of 305,000 sqm – a figure that fell short of the first nine months of 2023 by some 7 %. Take-up in the current year has been largely generated by the public sector, which accounted for around 20%. The vacancy rate rose to 5.2% despite a decline in new construction activity, a year-on-year increase of 60 basis points. The top rent rose by €1 quarter-on-quarter, to €36 per sqm. Investment market participants remained on the sidelines: at €480 million in the first three quarters, cash inflows increased by 7% compared to the very weak prior-year period. The net initial yield for first-class properties remained unchanged at 4.25 % in the third quarter.

pbbIX Hamburg | Index

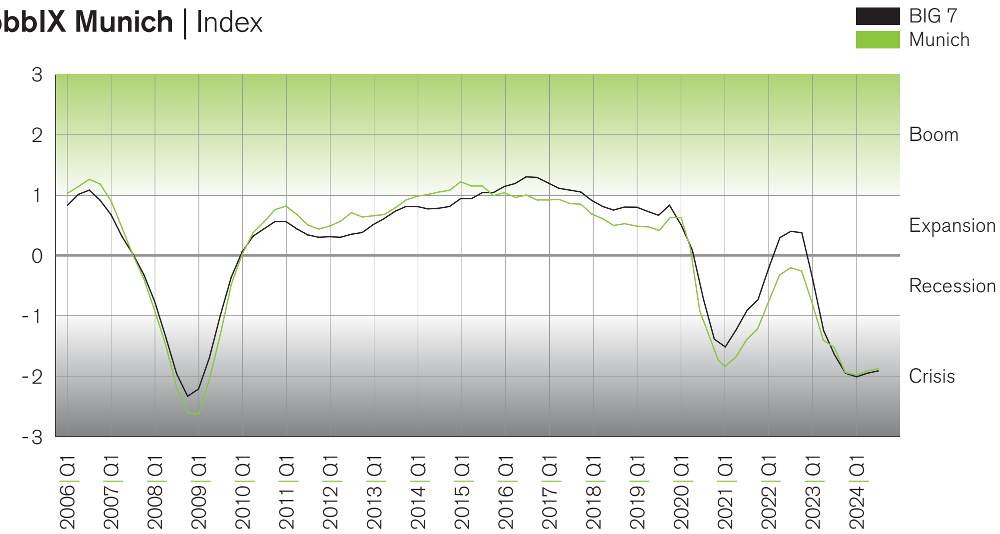


BIG 7

MUNICH

Demand for office space in Munich was up strongly, with take-up for the first three quarters of 2024 totalling around 450,000 sqm, up by about one third year-on-year.The strongest sectors were industry administrative departments, professional services and IT, together accounting for just under 50 %. The vacancy rate rose by 20 basis points in the third quarter, to reach 6.4 %. Demand for high-quality space in prime locations propelled the top rent to €53.50 per sqm (up 9 % over the past 12 months), the highest level across Germany. The investment market remained very weak, with inflows of around €350 million for the first three quarters, about 40 % lower year-on-year. At 4.15 %, yields for first-class properties have remained stable since the end of 2023.

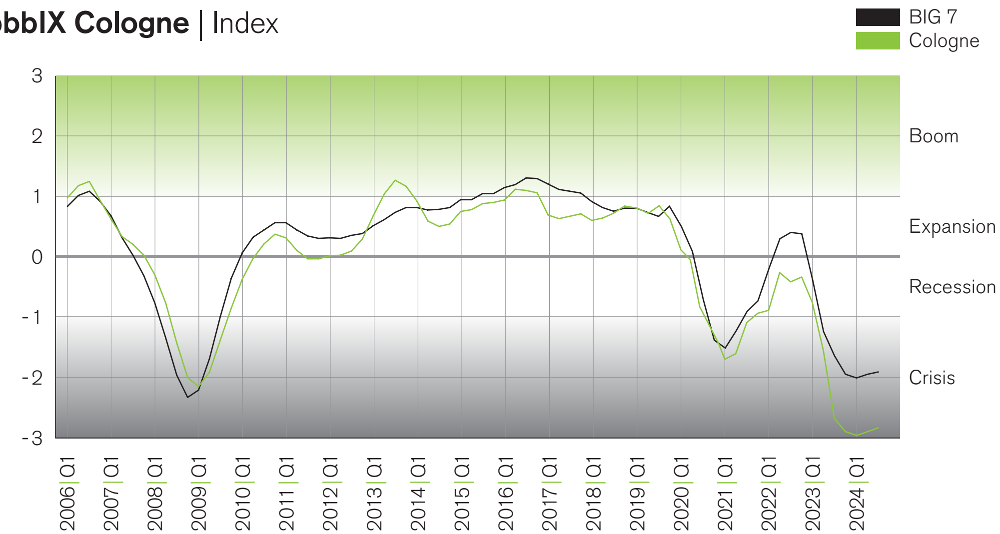
pbbIX Munich | Index



COLOGNE

Demand for office space was above average in the third quarter at around 108,000 sqm. Take-up for the first three quarters rose to approximately 180,000 sqm, up 30 % year-on-year. The vacancy rate of 3.9 % rose by around 70 basis points compared to the previous quarter. Cologne retains the lowest vacancy rate among the top 7 cities. The top rent has remained at a constant €32.50 per sqm for 12 months now. Year-to-date inflows on Cologne's investment market were markedly higher than in the previous year, reaching €380 million compared to around €220 million the year before, but nonetheless underperformed the five-year average by 40 %. During the third quarter the net initial yield for first-class properties remained unchanged at 4.55 %.

pbbIX Cologne | Index

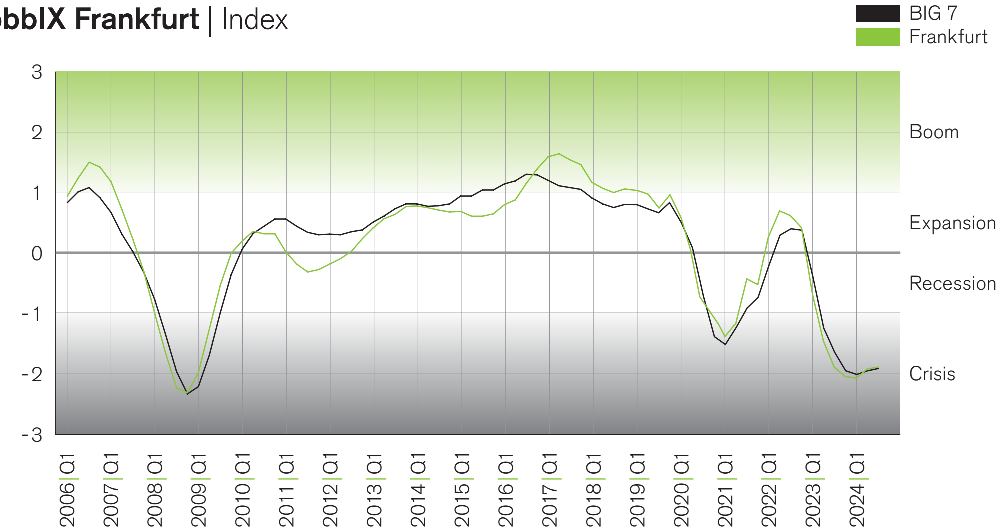


BIG 7

FRANKFURT

Transaction volumes on the Frankfurt office space market remained weak in the third quarter: year-to-date take-up was approximately 280,000 sqm – up 4% year-on-year but around 20% below the ten-year average. Here, the strongest sectors were banks/financial services, construction, professional services and manufacturing industry, together generating approximately 60% of aggregate take-up. Vacancy rates – which were already high – rose further in the third quarter to reach 9.2%, up 60 basis points from the previous quarter. The top rent currently stands at €48.00 per sqm. Investment inflows increased significantly in the first three quarters of 2024, up 86% year-on-year, reaching around €570 million. The net initial yield for first-class properties in top locations remained stable in the third quarter, at 4.6%.

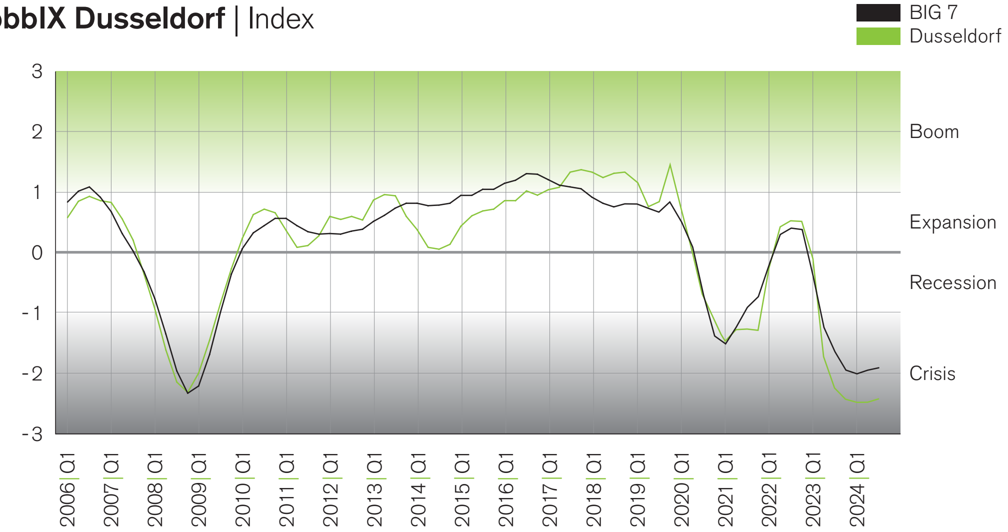
pbbIX Frankfurt | Index



DUSSELDORF

Q3 rental performance remained stable compared to the previous quarter with take-up of around 60,000 sqm, producing a year-to-date take-up figure of 190,000 sqm – down 5% on the same period of the previous year. The vacancy rate rose from 9.4% to 10.6% over the last 12 months, reaching the highest level since 2014. The top rent rose by €1.50 during the first nine months of the year, to reach €43.50 per sqm. Investment market inflows remained very low: at around €280 million, the year-to-date figure was some 15% higher than the same period in 2023 but still fell short of the five-year average by approximately 75%. The net initial yield for first-class properties in Dusseldorf was also unchanged since the beginning of the year, at 4.55%.

pbbIX Dusseldorf | Index

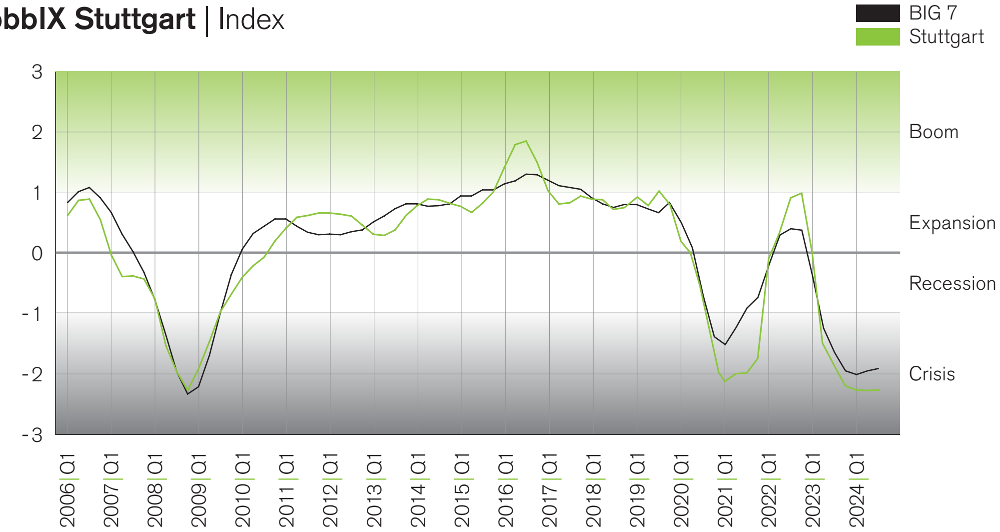


BIG 7

STUTTGART

Q3 rental performance on Stuttgart's office space market rose in the third quarter, giving a total of 145,000 sqm taken up in the first nine months of the year. While this represents an increase of 36% over the same period last year, it fell short of the ten-year average by 24%. Whilst the vacancy rate remained unchanged compared to the previous quarter, it picked up by 120 basis points to 5.0% compared to the previous year. The top rent remained stable at €36 per sqm during the course of the year. Inflows of around €180 million were registered on Stuttgart's office investment market in the first nine months of the year, which not only undershot the previous year's figure by around one-third but was also substantially below the five-year average of around €400 million. At 4.25%, the net initial yield for first-class properties remained unchanged quarter-on-quarter.

pbbIX Stuttgart | Index



About the pbbIX real estate index

SCOPE AND METHODOLOGY

As the last two decades have shown very clearly, the development of real estate markets is not a continuous trend that is free of disruption – instead, these markets are characterised by significant cyclical fluctuations. The pbbIX index family tracks economic developments on Germany's key office property markets. The index family comprises a total of eight indices: seven individual indices for the office real estate markets in Berlin, Cologne, Dusseldorf, Frankfurt, Hamburg, Munich and Stuttgart, plus a composite index which tracks overall economic development of the BIG 7 markets.

The indices are based on the results of a dynamic factor model, which brings together eleven variables, using time series to extract the key driving forces for economic trends of office property markets. Specifically, these variables relate to macroeconomic developments, the rental market, and the investment market across the seven office property markets covered. As a preparatory step for the factor analysis, the various market-related indicators are aggregated to form a single market indicator that measures overall development (for example, vacancies or new construction activity). The data list shown below sets out the indicators which were used for the dynamic factor analysis.

Over and above the office real estate market index, the presentation contains assessments regarding the components of 'macroeconomic developments', 'market for office space', and 'market for office investments'. The directional impact of these components on the composite indicator is colour-coded: GREEN indicates a positive, BLACK a negative and GREY a neutral impact.

DATA LIST OF THE DYNAMIC FACTOR MODEL

Overall economic development

- Real gross domestic product (YOY change in %)
- Workforce in the BIG 7 markets (YOY change in %)
- Consumer prices (YOY change in %)
- Current yield (Umlaufrendite) for public-sector bonds with a minimum remaining term of 10 years (in %)

Rental market

- Completed office and administration buildings (in sqm of usable space in the BIG 7 markets)
- Marketing volume (in sqm of rental space in the BIG 7 markets)
- Vacancies (in % of gross available area in the BIG 7 markets)
- Top rent (in € per sqm for the BIG 7 markets)
- Average rent (in € per sqm for the BIG 7 markets)

Investment market

- Initial net yield (in % for the BIG 7 markets)
- Inflow of funds (€ million)