Press release

FAP capital markets commentary
Conditions in the real estate financing markets remain ideal

By Curth-C. Flatow

We live in turbulent times. Whether the slowdown in the global economy, Brexit, Syria and the refugee crisis – risks are piling up all around to such an extent that it is difficult to maintain an overview. The capital markets are accordingly nervous. If we look at official indicators, such as the Ifo Business Climate Index or the Immobilienkonjunktur-Index (Real Estate Economy Index), the signs are negative.

The situation is being further exacerbated by a self-fulfilling prophecy effect. In addition to the real risks in the financial markets, often only a rumour is sufficient to precipitate the next crash. As is known, psychology is an influencing factor. That is why everything possible is currently being done to stabilise the markets as far as possible.

This also includes governments around the world attempting to create a secure position for their national economies among the global competition. Central banks are supporting economies with cheap money and currency devaluations.

For that reason alone, we believe interest rates will remain very low for some time. The spiral of insanity in monetary policy has not yet been broken, even if the Fed has taken the first step in the right direction.

As an asset class, commercial real estate investments will continue to benefit. While yields have hardened owing to the strong demand, the basic conditions remain ideal. Firstly, unlike in other asset classes, yields are still actually attractive. Secondly, financing rates have been trending even further downwards.

The banks' refinancing costs have also fallen to remarkably low levels. By way of example, Berlin Hyp recently issued the first Pfandbrief with a negative yield. The €500m bond has a term of three years and a coupon of 0%. The issue yield was -0.162%. According to Berlin Hyp, banks were the largest investor group, accounting for 53% of investment. FAP does not expect this to prove an exception and anticipates negative issue yields across an increasing range of maturities going forward. When discussing the bank's reduced margins, therefore, any objective analysis should also add the lower refinancing costs into the equation. Thus, the earning capacity of real estate finance providers is not so bleak.

FAP sees a similar trend when it comes to interest rate expectations of mezzanine capital providers. Expected returns are falling slowly but nonetheless further downwards. In an overall context, this trend is only logical since the spread between senior and subordinated capital cannot drift apart further. Returns on mezzanine finance are also being driven by the entry of additional capital providers, who are completely new to this asset class or are returning to the market. The broader base of providers and increasing competition for suitable deals is also acting in favour of borrowers.

About Flatow AdvisoryPartners (FAP)

Flatow AdvisoryPartners GmbH (FAP) is the leading independent consultancy for the procurement and structuring of capital for real estate investments and development projects in Germany. As a one-stop agency, FAP secures overall financing comprising debt capital and, where necessary, equity replacement funds. FAP's involvement in transactions and projects means that our services are called upon by purchasers, vendors, agents, lenders and those seeking to raise capital. FAP, with its head office in Berlin, was founded in 2005 by Curth-C. Flatow, who heads the company as Managing Partner alongside Managing Director Jörg Scheidler. Co-operation partners include Savills, BNP and Engel & Völkers.

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