Press release

FAP Mezzanine Report: more capital, more risk, more optimism

- **Growing volumes and increasing flexibility in investment**
- **High interest from institutional investors in hybrid financing structures with returns decreasing**
- **Family offices active, international capital providers reticent**

Munich/Berlin, 4 October 2018. The FAP Mezzanine Report 2018 details a rapidly growing and dynamic market for subordinate financing. The analysis of the sector in the 4th edition of the report from FAP Group, a leading independent consultancy in the procurement and structuring of capital for real estate investments and development projects in Germany, reports a significant increase in the provision of subordinated capital over the last twelve months, a greater appetite for risk, modestly declining returns and a noteworthy shift in preferred property sectors and locations for investment.

Curth-C. Flatow, founder and Managing Director of FAP Group: “The market for mezzanine forms of financing is evolving rapidly. In view of the sustained historically low interest rate landscape, capital volumes and pressure to invest remain high. This year’s report reflects the views of 59 of the 136 capital providers active in the segment. These market participants alone have provided EUR 3.9 billion of mezzanine capital over the last twelve months compared with EUR 2.6 billion in the previous reporting period. The total for 2018 is expected to reached up to EUR 6 billion. It is noteworthy that the market's appetite for risk is increasing with equity contributions falling by up to 25 per cent year on year, capital providers becoming more flexible and capital tranches becoming larger.”

Higher volumes, declining returns, greater appetite for risk

Interest rates / returns on subordinated loans are also falling modestly on average. This is attributable to the significant competition for suitable investments in the segment at present. Interest rates achieved in 2018 average 7.5 per cent (last year: 8 per cent) p. a. on financing of existing property and 10.5 per cent (last year: 11 per cent) on development projects.

More than 80 per cent of providers (last year: 56 per cent) now offer capital for existing property up to an LTV of 90 per cent or more. In general, more capital providers than last year are willing to honour such high lending ratios. On developments, 81 per cent of providers finance projects at between 90% and 95% of total investment cost.

Old and new players

Against a background of constant capital inflows from pension contributions, institutional investors are directing their policyholders into the market. However, they are increasingly conservative in their provision of capital and are investing directly to a lesser extent in favour of increasing allocations to appropriate specialist funds. While approx. 27 per cent of this group of lenders focused exclusively on the Top 7 cities in 2017, this has risen to 37 per cent in 2018 owing to security-oriented investment guidelines.

Hanno Kowalski, Managing Director of FAP Invest GmbH: “Family offices (multi-family offices) represent a stable constant in the market as a financially strong and entrepreneurial backbone in the development segment in particular. Funds fed with institutional capital are increasingly focusing on this segment. It is striking once again this year that international capital providers continue to play a scarcely discernible role in this market in Germany. The strength of international loan funds lies in the provision of large volumes with conservative LTVs and is primarily benefiting European and/or global real estate financing structures.”

Various crowdfunding platforms now represent established subordinate financing providers. Besides the traditional crowd capital, these players are increasingly providing volumes above the crowd ceiling of EUR 2.5m.

Potential for returns in the regions

Capital providers are deploying their available capital more flexibly and are investing in both existing property and development projects in increasing numbers. 54 per cent (last year: 52 per cent) are now active in both segments. Providers are increasingly recognising the potential for returns in smaller cities. More than half of providers (55 per cent) now provide capital throughout Germany, including B and C-cities (last year: 49 per cent), with C locations alone witnessing an increase of 14% compared with last year.

Capital is also increasingly being provided for special or “difficult” situations where traditional bank financing is frequently unavailable or difficult to obtain, e.g. re-positioning of property, value-add scenarios or bridging phases.

Residential investment has gained significant ground

Offices remain the preferred sector for investment this year both in terms of financing existing property and development projects. The remaining sectors have witnessed significant shifts compared with 2017 in favour of the entire residential sector (residential, hotels, micro-apartments, etc.) as well as retail and shopping projects.

When it comes to financing existing property, the residential sector ranks second with 95 per cent (last year: 100 per cent), followed by retail with 90 per cent (last year: 75 per cent) and micro-apartments with 87 per cent (last year: 47 per cent). Financing of development projects shows a similar picture: 96 per cent (last year: 100 per cent) of all providers finance residential construction, 90 per cent (last year: 63 per cent) finance micro-apartments and 88 per cent (last year: 77 per cent) are active in the retail sector.

Market participants are optimistic about the market over the next 12 to 18 months, expecting activity to remain at a consistently high level or to show positive growth.

About FAP Group

FAP Group is one of the leading independent consultancies in the procurement and structuring of capital for real estate investments and development projects in Germany. In 2016, FAP was crowned "Property Debt Advisor of the Year" at the renowned Europe Property Finance Awards of Property Investor Europe (PIE) magazine.

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 and has since advised on and structured capital with a total volume in excess of €14bn.

Contact FAP
Hanno Kowalski
Managing Director FAP Invest GmbH
Marburger Str. 17
10789 Berlin, Germany
Tel.: +49 30 8441594-90
www.fap-group.de

Press contact
Sascha Monath
Ummen Communications GmbH
Tel.: +49 30 46006-180
E-mail: monath@ummen.com