REFIRE
Real Estate Finance Intelligence Report Europe

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Inside REFIRE

REFIRE is a specialised report focused on providing market intelligence and background analysis to finance professionals in German and continental European real estate investment.

Whatever your particular area of specialisation, we think you'll find timely, incisive information within our pages, helping to inform you of the key deals, the numbers, the markets, the players and the people.

The areas we focus on are:

US Funds in Europe
European REITs
German Real Estate Finance
German Non-Performing Loans (NPLs)
Retail Property Funds
Mortgage Securitisation
CMBS/RMBS
Privatisations
Refinancing
Euro-zone Property Financing

REFIRE has an extensive network of contacts in the field of continental European real-estate finance, which enables us to bring you the latest and most relevant news. However, we always want to know more about what's going on in this dynamic sector, so make sure your company is keeping us informed of your moves. Send your media communications to news@refire-online.com for our consideration.

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Convertible bonds find new favour as refinancing option for German AGs

We report elsewhere in this issue on a number of bond issues from German real estate companies which highlight the increasing role that bonds, and in particular convertible bonds, are playing as a rational alternative source of financing for listed companies. The trend to convertible bonds has been spreading throughout Europe, with transaction volume over the first six months DOUBLING over last year's volume to about €1.5bn. Around 60% of all new European convertible bonds are now issued by the property sector.

So it was timely for REFIRE to sit down recently with a small group of active bond market participants to learn more about why the market for convertible bonds is growing, and in whose hands these bonds are ultimately landing.

Leading French issuer **Société Générale** told us that by the end of May this year, 35 convertible bonds were issued across all sectors in Europe, with a value totalling €9.2bn. Last year saw a total of 20 issues for a record €24bn in capital raised for the whole year.

One of the leading speakers at the gathering was **Ralf Darpe**, Société Générale's head of equity capital markets and co-head of corporate finance for German-speaking Europe. "This year, convertible bonds of property companies continue to play a major role, because, in view of current low interest rates, they represent an attractive financing tool", he said. Listed property companies are issuing bonds not only to diversify their financing, but also to strengthen their investor base.

"Property companies in particular benefit from these attractive conditions, due to the fact that low financing costs with long maturity and without collateralization are of special importance", he said. On average, in recent months investors have granted listed property companies coupons ranging between 0.5% to 2.0% and looked for conversion premiums ranging between 30.0% and 35.0% above the reference price – with an average term of 5 to 7 years.

Deutsche Bank buys remaining Corpus Sireo residential

Deutsche Bank subsidiary Deutsche Asset & Wealth Management (formerly RREEF) showed that it still sees upside value in the German residential real estate sector when it bought the Merkur residential portfolio from asset manager Corpus Sireo. The portfolio... see page 3

France's FdR expands, Icade departs from German market

It was a tale of executing diametrically opposite German strategies for two leading French property companies over the past few weeks, as one leading French REIT took a decisive step to boost its residential holdings in the country and the other made an equally decisive step to exit the German market see page 5

Shareholders happy as Fortress exits Gagfah

It's been all good news for residential housing group Gagfah shareholders in recent years, who are sitting on a six-bagger since the dark days of early 2009. Things were given a fillip last year with the arrival of CEO Thomas Zinnöcker from Berlin housing group GSW.... see page 8

AEW targeting€700m for "manage-to-core" fund

Pan-European real estate manager AEW Europe has brought German and Austrian institutional investors into the first close of its latest European real estate fund, a so-called "Manage-to-Core" fund...Page 13

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The advantages of convertible bonds, argued the issuers in the group, lie in the mixture of shares and loans. Investors not only acquire a fixed-rate debenture but also the option of swapping the bonds for shares.

Because conversion prices are clearly above the market price at the time of issue, a rise in share prices means investors profit in addition to annual interest payments. But even if the share price develops positively and the market price of the convertible bond increases, the issuer is able to secure financing at attractive interest rates. According to Société Générale, a quarter of all issuers are now using convertible bonds as a refinancing option. In Darpe's view, about a quarter of issuers view their convertible bonds purely as a financing option. About 8% issue the bonds to finance acquisition or takeovers.

"Four of the six biggest-ever convertible bonds issued by listed German property companies were placed in the last 6 months, for a total of €1.1bn. The biggest of these was Gagfah's at €375m."

Also sharing his experience was **Gerald Klinck**, chief financial officer at publicly-listed housing group **Gagfah**. In May Gagfah issued a five-year convertible bond of €375m. The fixed-rate coupon was 1.5% p.a. and the initial convertible premium was 30% above the reference price of €11.92 (the share is currently trading at €13.20).

"For us the convertible bond offers an excellent opportunity to optimize our borrowing costs in the current financing environment," said Klinck. "As a result of the successful emission, we were able to refinance a portfolio unsecured at a favourable interest rate. The low interest payments had a positive effect on our income. Further, these unsecured assets gave us additional financial latitude, such as investing in the existing portfolio or in future acquisitions."

We also heard from the management of Austrian company **Convertinvest**, which is an independent asset management company specializing in convertible bonds, and a pioneer in the field of absolute return with convertible bonds. The company is taking the popularity of convertible bonds as an opportunity to issue a global property convertible bond fund, called **Convertinvest Global Convertible Properties.** The fund has a volatility of 5.0% and an expected return of 5.0-7.0%, and invests purely in others' convertible bonds.

Even before launching the fund, said CEO **Gerhard Kratochwil**, institutionals such as insurances, family offices and foundations invested more than €30m in the fund. Issuer ratings on the fund are performed by rating agency **FERI EuroRating**.

According to **Wolfgang Kubatzki,** board member at FERI EuroRating Services who addressed the meeting, "Convertible bonds are complex. When investing in this type of vehicle we recommend investing in professionally and actively-managed funds. As a rating agency we integrate the entire technical know-how of the investment process related to convertible bond funds, so that at the end an attractive product is created."

As with other bonds, the FERI rating includes a detailed determination of site and user type in each individual company's portfolio, based on a quantitative company analysis. FERI says it also analyses the individual properties underpinning the bonds, "so that ultimately the evaluations are based on the attractiveness of the property portfolios", said Kubatzki.

Underlining the current popularity of the bond trend, capital markets researcher **Barkow Consulting** separately notes that four of the six biggest-ever convertible bonds issued by listed German property companies were placed in the last six months, with a total of €1.1bn. The biggest of these was the €375m Gagfah convertible, which is likewise the biggest since the outset of the financial crisis. Only erstwhile market leader **IVG Immobilien AG** has ever issued a bigger bond – a €400m bond in 2007 just before the crash. Meanwhile, all of the larger German listed property company's have issued convertible bonds, with the exception of the biggest company, **Deutsche Annington.**

DEALS ROUNDUP

Germany/Acquisitions

Deutsche Bank buys remaining Corpus Sireo residential

Deutsche Bank subsidiary **Deutsche Asset & Wealth Management** (formerly **RREEF**) showed that it still sees upside value in the German residential real estate sector when it bought the **Merkur** residential portfolio from asset manager **Corpus Sireo**. The portfolio represents the last remaining residential holdings owned by Corpus Sireo. It will now join DAWM's institutional funds division.

The portfolio, held by **Corpus Sireo Investment Residential GmbH**, consists of 3,604 residential units and154 commercial units totalling 260,000 sqm. Following the sale, Corpus Sireo will continue to exclusively asset-manage the 123-building residential portfolio for the next ten years, initially.

The sale price was not disclosed, but we reported recently here in REFIRE that we thought the division was valued at about €300m, and generated annual rental income of more than €20m. This sales price would be based on housing portfolios of equivalent quality normally expecting to fetch a multiple of 15-16 times annual rent, while the market for such portfolios has still been holding up firmly in Germany recently.

Most of the apartments are situated in Berlin, with additional locations in Nuremberg, Braunschweig, Hanover, and Leipzig. The vacancy rate is around 3.2%. The properties dating from 1857 to 2005 were acquired by Corpus successively through 2008, since when the group has largely been operating as a pure real estate service provider and reducing its own owned physical assets.

Corpus Sireo's now-prime business is the property servicing business, known as **Project Venus**, and this segment of the business is up for sale, with a decision on the new owner likely by the end of July.

Corpus Sireo, which is owned by shareholders the **Sparkassen** (savings banks) of **Cologne-Bonn**, **Düsseldorf** and **Frankfurt**, handles real estate interests in Germany for clients including **Deutsche Telekom**, **Deutsche Bank**, and private equity groups **Cerberus** and **Brookfield**, and partners new institutional investors coming into Germany through either its Luxembourg investment management platform or through its international client management