PRESS RELEASE

FAP Real Estate Private Debt Report Germany 2024

Alternative finance providers now concentrating on whole loans

- **Stretched senior loans also continuing to grow in importance**
- **Mezzanine financing playing less of a role**
- **Growing interest from British and North American investors**
- **Residential and mixed-use remain most popular asset classes**

To celebrate the tenth year of publication, FAP Group is expanding the scope of its previous FAP Mezzanine Report to encompass the entire range of alternative finance products, along with guest contributions from selected financing experts to provide additional insights.

Berlin, 14 October 2024 – The prevailing market environment for alternative financiers remains challenging, even as the first glimmers of hope appear on the horizon. Despite the ECB's two interest rate cuts, a turnaround in commercial real estate finance is not yet in sight. Banks continue to act with extreme caution, many institutional investors are sitting out the market for now, and various loan funds are also no longer active in the market. This reluctance is being reflected not only in lower lending ratios and more exhaustive deal review processes but also in more stringent requirements for pre-leasing and pre-selling or for securing construction costs. Because subordinated financing is currently no longer an option for most projects, whole loans and stretched senior loans have been gaining in importance.

The reluctance of banks and their lengthy and unpredictable approval timeframes have been playing into the hands of alternative financiers who are active in the market. In the current environment, those with sufficient capital and resources can cherry-pick the best projects. Most of these alternative lenders are focusing on existing properties in good locations with regular cash flows. Residential and mixed-use remain the most popular asset classes.

"We have been seeing a growing number of enquiries, especially since the second quarter of 2024. Despite the higher interest rates, alternative lenders are at a significant advantage with their fast deal approval times compared to banks," explains Hanno Kowalski, Managing Partner at FAP Invest. "We are now landing projects that would previously have ended up with a bank as a traditional loan financing. This situation is also attracting international investors."

These are the some of the key findings of this year's FAP Real Estate Private Debt Report Germany 2024, formerly the FAP Mezzanine Report. In addition to taking its annual in-depth look at the German market environment, this year's study examines not only the market for subordinated capital but also for alternative real estate finance in its entirety. FAP conducted interviews with 73 domestic and international investors who provide commercial real estate financing in Germany. Of those surveyed, 59 stated that they were still active in the debt sector. In other words, 20 per cent of study participants have exited the real estate lending business, at least for the time being, while 11 per cent are concentrating solely on whole loans and are no longer involved in subordinated financing.

Lower lending ratios with whole loans than with mezzanine financings

While the difference between lending ratios for mezzanine deals and whole loans was barely observable in last year's report, this year there is at least a small difference: the average loan-to-value (LTV) for whole loan financings of existing properties was approx. 74 per cent, compared to approx. 77 per cent for mezzanine financings.

In practice, senior secured financings are, in contrast, generally being offered only up to a maximum LTV of 70 per cent. In fact, many senior secured deals are well below this mark and therefore barely distinguishable from the traditional bank financing route. In the case of development projects, the picture is similar, with the study finding an average loan-to-cost (LTC) of 76.7 per cent for whole loan financings and 80.2 per cent with subordinated capital.

Looking at the market as a whole, the tightness of liquidity among many alternative lenders has led to a significant reduction in overall lending, as well as smaller ticket sizes for individual deals. International capital providers, on the other hand, are still looking for big-ticket deals, particularly for whole loans. With only a limited number of German participants willing to consider financings upwards of EUR 100 million, there is less competition for these larger deals.

"It's clear that whole loans have been increasing in popularity. Although the ticket sizes have likewise fallen here, these are now at a level comparable to traditional bank financing in the past. Moreover, financing costs with whole loans are no longer so far apart from the traditional bank financing route," explains Kim Jana Hesse, Head of Capital Partners at FAP Finance.

Residential and mixed use remain the most popular asset classes, with hotels gaining ground

Although the majority of financiers surveyed still prefer existing properties in good locations with stable cash flows, 86 per cent of respondents said they were also willing to selectively consider financing development projects. In practice, however, only projects with extremely solid economics are being financed.

Residential and mixed-use remain the most popular asset classes, followed by logistics. 81 per cent of respondents expressed interested in office properties, compared to 94 per cent last year. Despite the "back to the office" trend, the uncertainty surrounding office real estate has not fundamentally changed. Office properties are only of interest to alternative financiers if they are in prime locations, meet strict ESG requirements, and are largely leased out. It is expected that demand for ESG-compliant office space will continue to grow as companies strive to meet their sustainability commitments. The hotel asset class is becoming significantly more popular, with an increase of 15 percentage points over the previous year.

When asked about their willingness to finance in specific locations, all participants said they would finance in Germany's Class A cities, and 91 per cent also in Class B cities. In contrast, only 67 per cent are active in Class C cities, and only 53 per cent in Class D cities. International investors, in particular, prefer Germany's largest and best-known cities. For the first time, lenders were asked about their willingness to finance abroad: 81 per cent said they finance projects outside Germany, mainly in Western and Northern Europe.

We will gladly send a copy of the complete report upon enquiry.

About FAP

The FAP Group is an independent advisory company that specialises in raising and structuring capital for real estate investments and project developments. The Group comprises FAP Invest, a leading real estate investment platform for institutional investors with a focus on debt products, FAP Finance, which provides advice on all capital and financing issues to borrowers, and FAP Syndication & Capital Markets, an independent syndication desk which brings single lenders and groups of lenders together and offers access to raising debt capital on the capital market. FAP structures conventional debt finance as well as mezzanine, equity and capital market products. These services secure the overall financing from debt capital and – if necessary – equity substitutes. FAP, headquartered in Berlin, was founded in 2005 by Curth-C. Flatow. The group has since advised and structured capital with a volume of over €18 billion.

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