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Dear Reader,

More than a quarter of a century ago, East and West Germany were reunified. For Eastern Germany's states in particular, the intervening 26 years have been a period of rapid change: new infrastructure, programmes to support regional economies, and the modernisation of housing stock. Measures implemented under the banner "Aufbau Ost" (Rebuild the East) were wide-ranging, designed to prevent mass outward migration to Western Germany. In the first few years after reunification, these measures were only moderately successful.



The situation is very different today. Eastern Germany has long since reversed the post-reunification trend. And not just in the region's major cities, Dresden, Leipzig and Jena, which stepped into the limelight in the mid-1990s and have been there ever since. We've now reached the point where people from Western Germany are happily moving to the East. They come to study in the regions' large universities and smaller technical colleges – in Mecklenburg's Greifswald, for example, or Saxony's Freiberg. The previous (western) German was the first to fully appreciate the region's medium-sized cities, valuing their rich cultural heritages and overall quality of life. And let's not forget the large number of modernised Wilhelminian apartments in the central districts of Eastern Germany's most beautiful towns and cities, absolute pearls found in places like Weimar and Görlitz, and available for a fraction of the rent in Western Germany's major cities. Quite a few people from Cologne or Hamburg have found a new home in the East – and now have more money in their pockets as a result.

It is cheaper to live in Eastern Germany than it is to live in the West, even today, and despite double-digit rental and property price increases in many Eastern regions. And it is not just the small, commuter-belt towns around Berlin or Dresden that have seen their populations expand as housing has become more expensive and ever scarcer – the desire to live in an urban environment has also led to population growth in towns such as Merseburg and Dessau.

As a housing company with a defined focus on Eastern Germany, we have a particular interest in developments across the region. What opportunities are there for landlords and investors in Eastern Germany's medium-sized and major cities? What risks and challenges need to be recognised and accepted if previously neglected locations are to develop positively?

In order to provide you, and ourselves, with the answers to these questions, we asked the real estate services company Wüest & Partner to compile and analyse a full range of relevant housing market parameters in selected cities in Eastern Germany. Their comparison of rents, property prices, price-to-rent ratios, yields and micro-economic data for each of the cities has revealed some very exciting developments. Our report begins by providing details on a range of geographically differentiated developments that every investor should know. At this juncture, we can already reveal one of the report's most important findings. In the past, people often referred to an "Eastern German property market". Our analysis makes it abundantly clear – there is not one property market, there are various distinct markets. Prepare to be surprised ...

We hope you enjoy reading this report.

Claudia Hoyer
Executive Board (COO)

Martin Thiel
Executive Board (CFO)

Dr. Harboe Vaagt
Executive Board (CLO)

Executive Summary

One look at Eastern Germany's housing markets reveals that there has been a trend reversal. Outward migration from Germany's Eastern states has come to an end. But, as in many other regions, the markets are heterogeneous and the development of rents and property prices is shaped by a combination of different factors. Urban or rural locations plays just as much of a role as regional affiliation, transport infrastructure and economic or population growth. Although double-digit price rises have been registered in some areas, it is still comparatively cheap to live in Eastern Germany – and in an environment that is just as attractive and comfortable as the West. This is a major plus for the region's cities, and has attracted more and more residents, many of whom have moved from Western Germany. As a result, countless opportunities are opening up for investors.

Strong demand for housing in large cities

Rapid urbanisation is also having a positive impact on Eastern Germany. Major cities, including Berlin, Leipzig, Jena and Dresden, have seen their populations surge over the last few years. The same applies to a number of state capitals, such as Potsdam, Erfurt and Magdeburg. Smaller university towns like Freiberg and Greifswald are attracting growing numbers of young people, especially those who want an urban lifestyle but can't afford the cost of living in a big city. All of these cities have profited from above-average growth in demand for housing.

The smaller, commuter-belt towns around Berlin that are included in this report are also doing well – above all, those that have the most convenient road and rail links to Germany's capital. The higher the cost of living in Berlin (and Potsdam), the better the prospects of growth are for smaller, more peripheral localities. For example, Strausberg, which is 54 kilometres from Berlin and has a population of 26,000, has seen residential investment properties change hands at prices of up to 25 times annual net rental income – a higher price-to-rent ratio than in any other town or city in Brandenburg. Such high prices are only possible because of the town's commuter rail line that runs to the heart of Berlin. A significant proportion of Strausbergers are commuters, and they can travel to Berlin's central train station in less than 45 minutes.

Significant reductions in vacancy rates

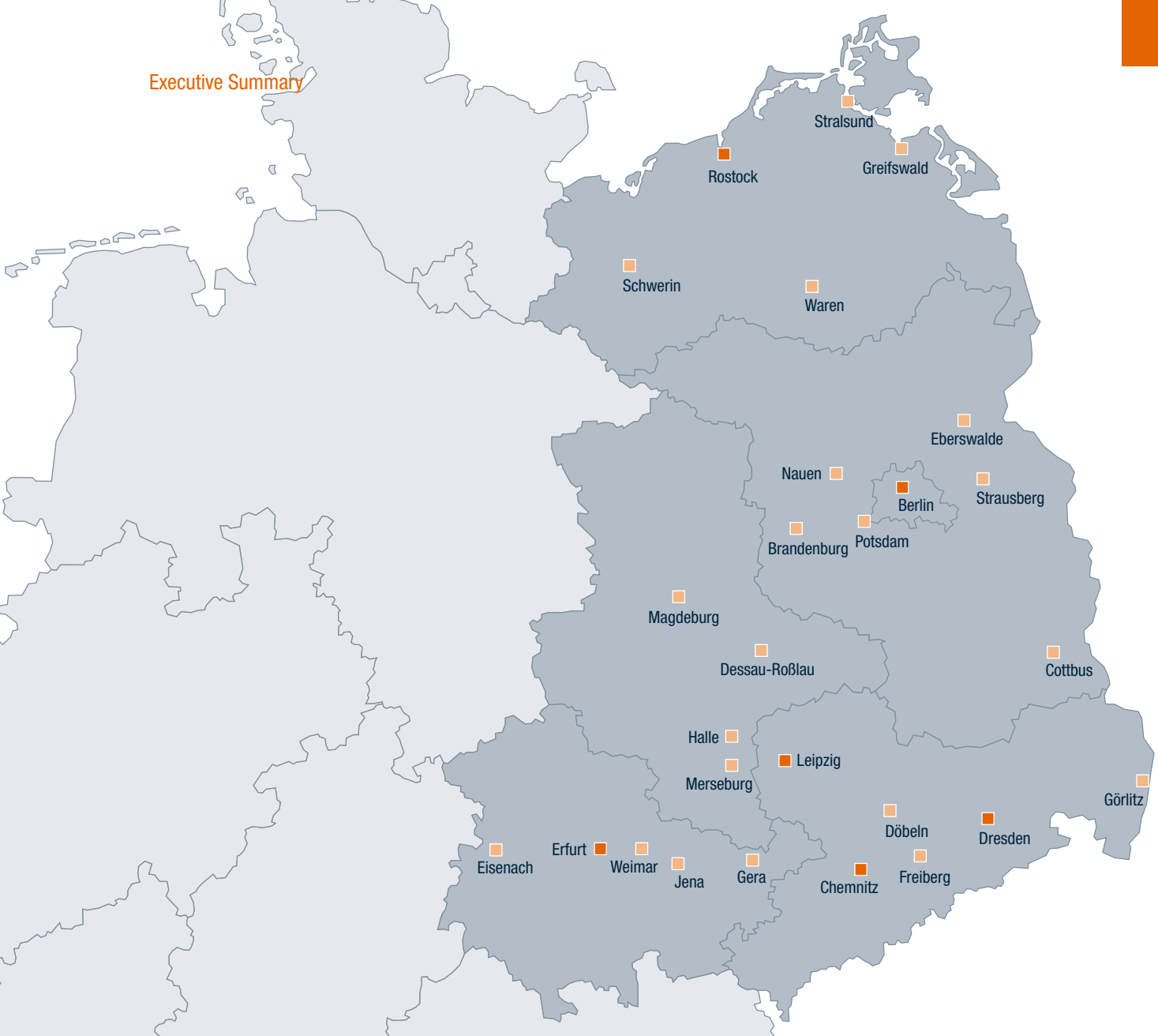
The towns and cities along Germany's Baltic coast are in a league of their own – and this is equally true as far as the relationship between rental and property prices is concerned. In parts of Greifswald, Stralsund and Rostock, house and apartment prices have risen dramatically. In just ten years, the square-metre price in Rostock has surged by an average of almost 60%, and in Greifswald by around 35%. The town's average rent, at EUR 8.00/sqm, is also by far the highest in all of Mecklenburg-West Pomerania. In contrast, tenants in Schwerin, Stralsund, Rostock and Waren an der Müritz pay an average of between EUR 5.00 and just over EUR 6.00/sqm. Rental prices have already clearly reached a peak in Rostock, whereas property prices seem set to rise further.

In the vast majority of Eastern Germany's towns and cities, rental prices have developed largely in parallel to property prices. In the "somewhat weaker" towns and cities, such as Chemnitz, Eisenach, Gera or Dessau-Roßlau, where rental and property prices are more moderate, prices have actually fallen substantially over the last decade – despite their low starting position, prices in some locations have dropped below the EUR 1,000/sqm threshold. Rental prices, however, have gained some ground over the same ten-year period. This is largely due to the fact that relatively few new rental apartments have been built in many locations, while much of the region's older, and often quite dilapidated, housing stock has been demolished. As a result, the double-digit vacancy rates of the 1990s have since been cut to below 10 %.

Chemnitz and Freiberg are among the new magnet cities

Another interesting phenomenon is the current rate of population growth in places that previously suffered from massive population decline. The reason – on the one hand, refugees from crisis regions in the Middle East have boosted population figures. On the other hand, senior citizens are increasingly abandoning their village homes and moving to the nearest town in search of better infrastructure and housing tailored more to their specific needs. Both of these factors have combined to return towns such as Merseburg and Dessau to positive population growth.





Chemnitz can once again report real population growth. Within a single year (2014-15), the city added 3,560 new residents. A similar development has also been observed in the much smaller town of Freiberg, which has seen its population rise to more than 40,000. Both are now classed as “Schwarmstädte” (literally, “swarm cities”), as are Leipzig and Dresden. This group of towns and cities are defined by their ability to deliver rapid population growth on their own, without having to rely on the lure of a neighbouring major city.

Medium-sized cities offer yields of between 5% and 8%

A significant portion of our study is also devoted to an analysis of where it still makes sense to invest in Eastern Germany’s housing. The towns, cities and regions we have considered in this report present a differentiated picture. Strongly divergent yields and price-to-rent ratios clearly reflect regional variations in risk (loss of earnings due to population decrease) and potential (population growth and reduced household sizes).

The better prepared a location is for the challenges of the future, the higher the price-to-rent ratios and the lower the yields. This is why Berlin and Potsdam register price-to-rent ratios of between 25 and 30 for multi-family apartment buildings, and why yields are so meagre at between 4.5% and 5%.

In Erfurt, Weimar, Rostock and Jena, price-to-rent ratios tend to average 15 to 16, which results in yields of around 6.5%. And in Eisenach, Cottbus, Schwerin or Stralsund, investors have to budget for average price-to-rent ratios of 12 (8% yields). Double-digit gross yields can be expected in Görlitz, Gera and Nauen.

At the moment, few investors focus on Eastern Germany – with the exception of Berlin. In particular, it is the region’s medium-sized towns and cities that offer enormous development potential, because they are already on a path to further growth, have positive outlooks for the future and still have relatively low rental and property prices. From this point of view, Eastern Germany’s pearls are not just Leipzig, Dresden and Jena, but also towns like Greifswald, Freiberg and Strausberg.

“New opportunities for Eastern Germany’s medium-sized cities”

Mr Slupina, Eastern Germany has lost around 14% of its population over the last 25 years. We often have the image of the “depopulated” East. But there are definitely regions that have experienced positive population growth. Do we need to redefine our image of the East?

We certainly do. You’re absolutely correct when you point out that Eastern Germany’s five states have lost approximately 2 million people since 1990 as a result of outward migration and mortality figures exceeding birth rates. But these developments have not been uniform. Above all, the greatest population losses have been seen in rural areas, away from the region’s major towns and cities – for example, in large sections of Mecklenburg-West Pomerania, and in the Altmark, Oberlausitz or Prignitz regions. And there are no indications that this trend will reverse anytime soon.

Have all rural regions suffered the biggest losses?

Famously, there are always exceptions to the rule. In earlier studies we saw that there are a number of very small, fairly isolated places that have bucked the general rural exodus trend and have enjoyed population stability. In many cases, it is the well-established structures and unusually high number of clubs and associations in these villages that make a crucial contribution to such positive, localised developments. Unfortunately, it’s not possible to offer a more detailed explanation. But, in general terms, the further a village is from a sizeable town or city, the more limited its prospects for the future.

What role does proximity to Berlin play?

A huge one. The closer a locality is to Berlin, the better its prospects. With established infrastructure and rail or commuter rail lines, communities around the German capital can definitely profit from the growth of Berlin, and from the higher rental and property prices there. But Berlin is not representative of the entire Eastern region. If we put Berlin to one side for a moment, Leipzig and Jena are attracting the greatest numbers of young people. But there are a host of other cities, including Magdeburg, Rostock and Erfurt, that have experienced positive growth over the last few years and have seen their populations expand.

And what makes these cities attractive to migrants?

Eastern Germany’s largest cities have also experienced tough times, and their populations declined continuous-

ly over a number of years. Numerous development programmes were launched under the umbrella “Stadtumbau Ost” (“Urban Redevelopment in Eastern Germany”), and were largely successful in reversing the trend. The run-down – but often very attractive – historic centres of numerous cities were refurbished, and the stock of prefabricated housing was either demolished or modernised. There was also a great deal of new housing built. The redevelopment programme even stretched as far as more rural exurbs, where former East German citizens fulfilled their dreams of owning a house with a garden. Whereas the 1990s were an era of outward migration, as people deserted derelict towns and cities, the new millennium saw a flood of people return. And not just returnees, but new migrants, too.

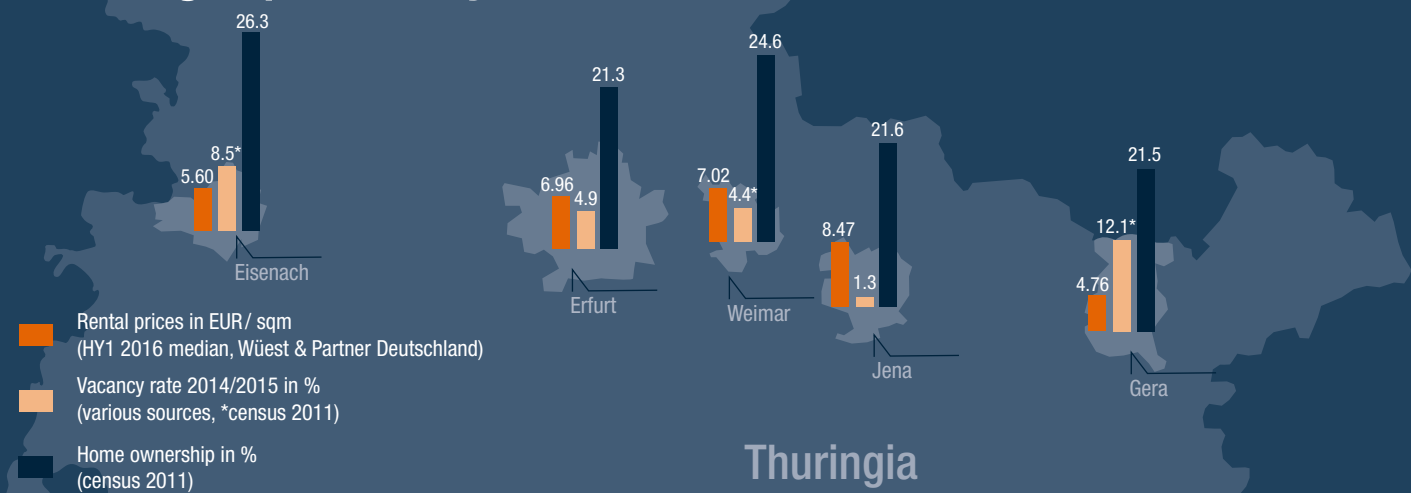
Even people from Western Germany are moving to the East. Who are they and why are they migrating?

It’s impossible to say in detail. But in 2013 the first East-West comparison was made that registered a positive population balance in favour of Eastern Germany. The first to make the move were senior citizens over the age of 65. Nowadays, there are also significant numbers of young people and young families moving from Western Germany to one of the region’s larger cities, such as Leipzig or Jena. These are attractive cities to live in, and the cities in Eastern Germany have nothing to be afraid of in comparison to the West. Still, we haven’t yet examined migrants’ specific motives.

But you have looked at population movements within Eastern Germany itself. Who is moving, and where are they settling?

We have identified several groups who exhibit different patterns of behaviour. What we call “student migrants” tend to be drawn to larger cities, such as Leipzig, Dresden and Jena. The “job migrants” go wherever they find a suitable job – so mostly also the larger cities. The “family migrants” are really the only group still interested, at least to some extent, in moving to rural communities, where they hope to raise their children in a more tranquil environment beyond the hustle and bustle of a big city. But even this group is more likely to stay in an urban centre today, where they can find work and the infrastructure they need for their children, such as daycare nurseries and schools. One of the most interesting groups is the “retiree migrants”. These are people above the age of 65 who are leaving their villag-

Economic and Demographic Key Data



Demographics

City	Population 2015	Population development Δ 2012-2014	Households 2016	Household development Δ 2014-2016
Erfurt	210,118	1.3%	107,569	2.6%
Jena	109,527	1.2%	61,300	4.3%
Gera	96,011	-0.9%	54,084	2.4%
Weimar	64,131	0.4%	34,660	1.3%
Eisenach	42,417	0.3%	22,840	0.2%

Sources: State statistical offices and cities' websites; Federal Office of Statistics; BBSR; GfK

Purchasing Power

City	Household purchasing power 2015 (D = 100)	Household purchasing power Δ 2010-2015	Retail centrality 2016 Index (D = 100)
Erfurt	86.1	22.5%	112.8
Jena	80.1	9.2%	106.4
Gera	75.1	10.3%	118.1
Weimar	78.2	14.6%	83.9
Eisenach	79.3	11.6%	127.2

Source: GfK Geomarketing

Labour Market

City	Unemployment rate 2015	Unemployment rate Δ 2010-2015	Employment subject to social security contributions Δ 2010-2015	Net commuter flow 2015 (inward minus outward commuters)
Erfurt	7.7	-22.3%	6.2%	26,199
Jena	6.4	-8.4%	11.4%	15,028
Gera	10.2	-23.5%	0.2%	2,278
Weimar	7.7	-25.1%	4.2%	1,845
Eisenach	7.3	-23.6%	8.5%	7,286

Source: Federal Employment Agency statistics

Building may resume

Thuringia is well equipped for the future. Because so little has been built in many of the region's cities, rental and housing prices continue to increase. Real estate markets are now being energised by the growing number of inhabitants.

Good news for the real estate markets in Erfurt, Eisenach and Weimar: Cologne's Institute for the German Economy (IW) sees further need for apartments in all three cities. The people of Thuringia have to play catch up, because so little has been built in recent years. Between 2008 and 2014, on average only 1.4 new apartments were added per 1,000 inhabitants (national average: 2.1); in Weimar it was 0.9 and in Eisenach only 0.8.

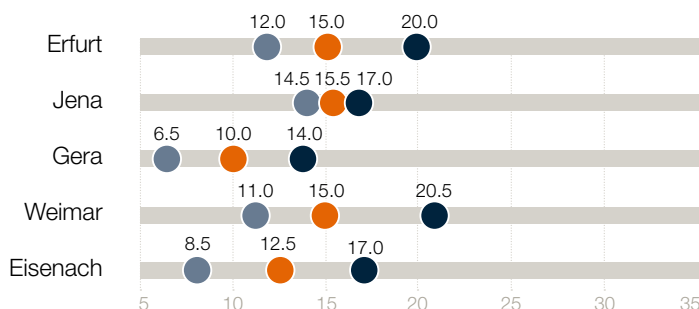
Renovation and new construction instead of demolition

Therefore the state capital, Erfurt, has announced that it wants to build about 4,000 new apartments by 2022 – spread out over 60 residential building projects. The plan is supported by European funding of EUR 36 million. Because the population is starting to grow again and Erfurt is hoping to reach the population it had before reunification, the city does not want to demolish the old prefabricated concrete apartment blocks, but instead have them renovated. Young people, in particular, are attracted to these affordable apartments. This year was the first in which more prefabricated units were renovated than demolished. Although 2,000 residents moved out, 3,700 new residents moved in.

Jena has also stopped demolishing old apartment buildings, choosing instead to renovate them. Even old administrative buildings in the inner city have been rezoned for housing, as the real estate market has become tight, in spite of many new buildings. Although more housing has been built in this university and research city than anywhere else in Thuringia – yearly 3.1 apartments per 1,000 residents – it is still not enough. Jena is on a growth trajectory. In recent years (2008-14), 4.7% more people moved there. The average rental price is EUR 8.47/sqm (H1 2016) the highest in

Multipliers

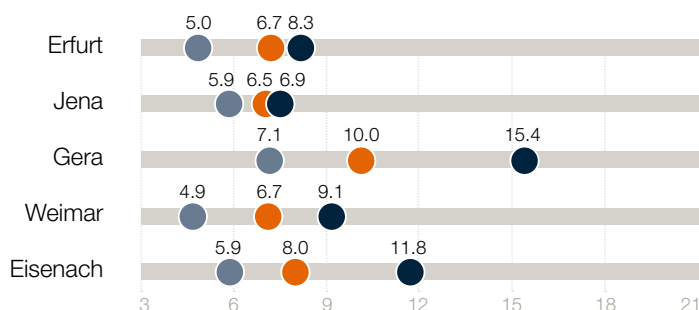
● = minimum ● = average ● = maximum



Source: Property market reports, Wüest & Partner Deutschland

Gross Yields

in % ● = minimum ● = average ● = maximum



Source: Property market reports, Wüest & Partner Deutschland

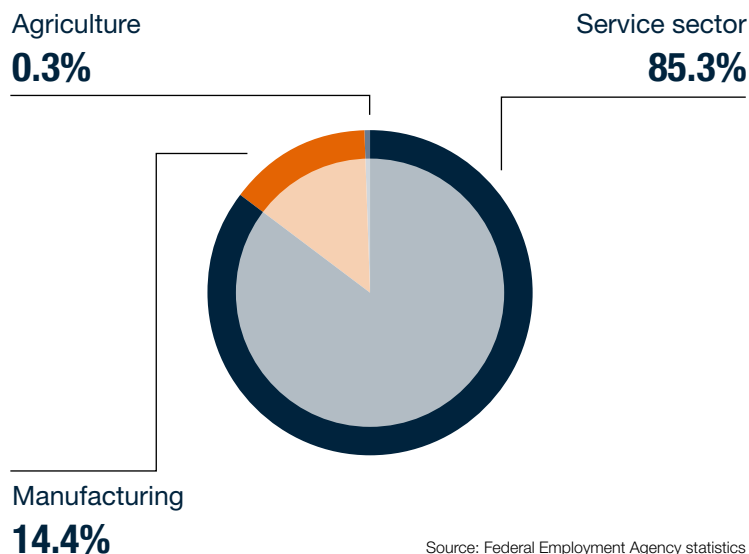
Transaction Market

City	Housing 2015 in € millions
Erfurt	463
Jena	173
Gera	78
Weimar	106
Eisenach	52

Source: Property market reports

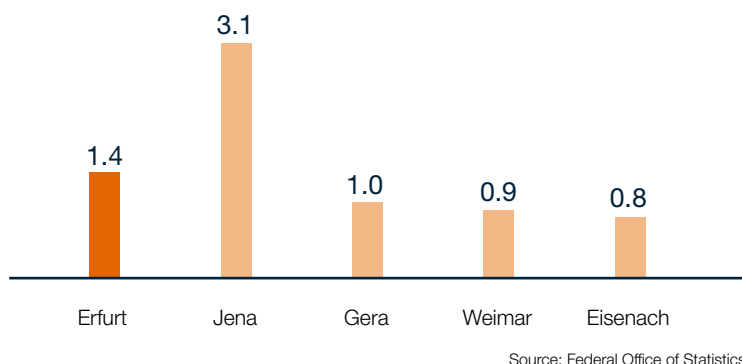
The transaction volume covers developed land, undeveloped land and well as residential property and apartments.

Economic Structure in Erfurt



Constructions

Completed construction per 1,000 population Ø 2008-2014 p. a.



Gera, market

Eastern Germany (with the exception of Berlin and Potsdam). Within ten years, rental prices have risen by almost 28%. In the meantime, the state has also enacted rent controls. And social building projects are always being discussed, because not everyone can afford such high rents. Meanwhile, the government is considering construction cost subsidies for investors, to enable them to build affordable apartments. In 2017, EUR 14 million was made available.






The city of Gera, only 35 kilometres away, is also once again receiving investment. The private equity investor, Benson Elliot, has made purchases from the local housing association (GWB), and is now the majority owner of housing stock amounting to 6,700 apartments. British investors want to renovate and modernise many apartment units in the coming years and are preparing for an upswing in what used to be the second-largest city in the state. Although Gera has lost about 6% of its population in the last years. But in terms of purchasing power, the Otto Dix city has almost caught up with Jena. The unemployment rate has sunk by almost 24% to 10% (2010-15). Another positive trend – since 2014, young people from the surrounding areas are once again moving to Gera and have raised the city's population for the first time in 27 years. This will also contribute to lowering the vacancy rate which was at 12% five years ago.

Solid property market A few years ago, Eisenach and Weimar had to accept population losses (2008-11). Now their numbers are starting to increase again. The populations of Eisenach and Erfurt have returned to growth. The loss of population in the previous years didn't have a negative impact on real estate prices. On the contrary, according to a current State real estate market report in 2016 "Thuringia, despite its demographic change, had a stable property market". And apartments have never been more expensive. The average price for detached and semi-detached homes rose by 7% (2015-16), and has now reached almost EUR 102,000.








Gera, Lasurstraße

Property Prices

City	Property purchase price EUR/sqm			% change
	2011	2015	H1 2016	Δ 2011–2016
Erfurt	1,376	1,759	1,808	31.4 % 
Jena	1,716	2,108	2,092	22.0 % 
Gera	759	651	650	-14.3 % 
Weimar	1,173	1,660	1,676	42.8 % 
Eisenach	915	1,079	1,167	27.4 % 

Source: Wüest & Partner Deutschland; median price

Rental Prices

City	Apartment rent EUR/sqm/month			% change
	2011	2015	H1 2016	Δ 2011–2016
Erfurt	6.00	6.77	6.96	16.0 % 
Jena	8.00	8.60	8.47	5.8 % 
Gera	4.65	4.74	4.76	2.4 % 
Weimar	6.15	6.97	7.02	14.2 % 
Eisenach	5.05	5.56	5.60	10.9 % 

Source: Wüest & Partner Deutschland; median price



Eisenach, An der Tongrube

Rising rents and prices Rental prices have also risen. In a ten-year comparison, rental prices in Erfurt rose by 22.5% to EUR 6.70/sqm (rent controls have recently been enacted here); in Weimar by 26,6% to EUR 6.95/sqm, in Eisenach by 10.9% to EUR 5.55/sqm (average for 2014–16) and in Gera by 7% to EUR 4.72/sqm. On average over the last two years, apartments in Thuringia's capital have cost EUR 1,745/sqm (+ 33% in ten years), in Weimar they cost EUR 1,664/sqm (+18,8%). During this time, prices in the Lutherstadt Eisenach have become 11% cheaper. However, the square metre price in Eisenach was EUR 1,071 (2014–16), but advertised prices in Q1 of this year alone have risen by more than 8% – to EUR 1,159/sqm and to EUR 1,167/sqm in Q2. The historic city is one of the candidates with the best future prospects in Thuringia. The Cologne-based IW even ranked Eisenach, due to its socio-economic position and

its economic development, among the best 100 of 402 examined cities and regions in its national regional ranking. In contrast, Jena is playing in a completely different league – more on par with Dresden and Rostock. The square metre price for property is EUR 2,122 (average for 2014–16), which shows an increase of almost 34% over the last ten years. Investment property, here and in Erfurt and Weimar, sells for an average of 15 times annual net rental income and generates returns of 6.5%.

Outlook: Property in Thuringia has never been more expensive than today. On the one hand, this is due to minimal building activity, on the other, due to the growing number of residents in a stable economic environment. We expect positive impulses for the property markets in future. ■