Intelligent Investment

German offices: new cycle, new opportunities

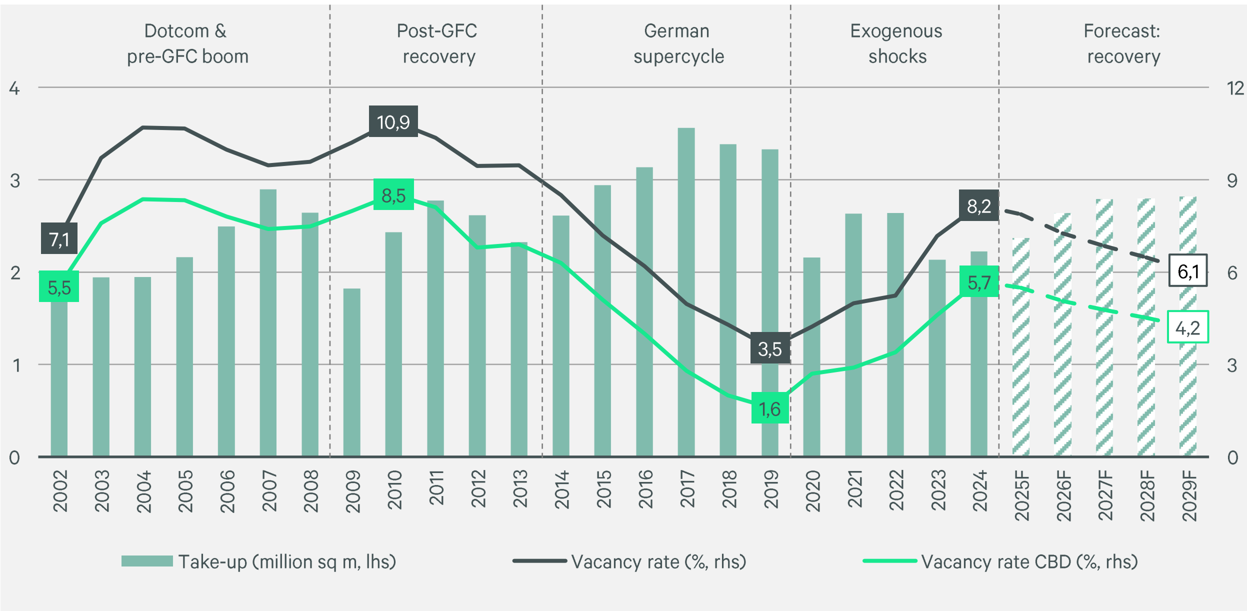
Matthias Düsing and Dr. Jan Linsin
April 2025

Germany's office market is at the brink of a new market cycle. Forward-looking guidance for market fundamentals turned positive and investor sentiment is easing. The case for German offices is gradually improving, opening a growing opportunity set along the risk curve.

After a decade of 'anything-goes' during the 'German Supercycle', the historical interest rate hike following 2022 sparked almost a full stop to the investment market. However, liquidity, valuations and returns bottomed out. Occupier markets reached their cyclical turning point in 2024 after a phase of economic weakness with a supply overhang weighing on.

However, silver linings are emerging in 2025 as forecasts on long-term demand and supply dynamics improve. The recovery phase until the end of the decade will be bumpy, but steady, characterized by increasing demand for modern Grade A offices, decreased construction activities and structural challenges (see Figure 1).

FIGURE 1: Long-term demand and supply German Top-5 office markets (in million sq m and percent)*



* German: Top-5 office markets: Berlin, Düsseldorf, Frankfurt, Hamburg, Munich; including sub-letting spaces
Source: CBRE Research, April 2025

The office is anything but dead!

The asset class office has lost some of its allure. German offices were among the most expensive in terms of net initial yields and capital values in Europe during the last market cycle. The hit on values during the 2022/2023 correction was sharp. Domestic institutional capital sources are traditionally highly exposed to and in some cases even overallocated to German offices. The risk perception towards structural themes and the overall return profile has increased. Hence, repositioning the asset class for the next cycle is challenging[1].

Investors are trying to adequately price in risks emerging from the recessionary economy, effects of return-to-office and A.I. on long-term occupancy rates, technical and regulatory obsolescence risks. At the same time, companies are changing the way they utilize the office. It is no longer merely a necessity or cost factor. Instead, the office is becoming a competitive asset in most industries for attracting and retaining talent, as well as adding value to productivity and innovativeness. The times of 'one-size-fits-all' layouts are a thing of the past: workplaces need a sophisticated and strategic management approach more than ever[2].

With changing occupier demand, the importance of location quality, amenities, fit-out and re-lettability for asset managers and investors has become increasingly significant. Given the size of investable stock, there is no doubt, that this asset class will remain a cornerstone of commercial real estate portfolios, but with different underwriting assumptions as part of a broader repricing. As risks evolve, new opportunities are emerging: for asset managers and investors, understanding underlying long-term occupier demand trends and local market patterns is again key to identifying the best opportunities (see Figure 2).

FIGURE 2: Structural challenges, adaptation strategies and opportunities in the German office market

	Employees/Companies	Portfolio/Asset Manager	Investor/Lender
Risks	• Dysfunctional offices, outdated workplace strategies • Higher occupation costs at negative cost-benefit • Low availability of adequate grade A offices	• Elevated letting, re-financing and exit risks • Failure to meet target returns and portfolio risk requirements • Higher CapEx requirements for underperforming assets	• Repricing, mispricing and distressed assets • Elevated letting, financing and exit risks • Opportunity costs and failure to meet return targets
Adaptation	• Employee-focused workplace strategies • Right-sizing and flight-to-quality with lower floor sizes but higher quality requirements	• Active asset management to attract and retain occupiers • Dedicated CapEx and ESG initiatives to lift attractiveness of underperforming assets	• Core for stable income, diversification, inflation-hedge and long-term value retention • Value-add and income-growth strategies to unlock higher risk-adjusted returns
Opportunities	• Aligning office workplaces with strategic business goals • Efficient and effective office solutions at positive cost-benefit	• De-leveraging, diversification and portfolio transformation • Attracting and retaining tenants, lifting ERV reversion potential in existing portfolio	• Letting market recovery and rental growth for grade A offices in CBD locations • Cyclical entry opportunities for capitalizing on repricing at improving underwriting criteria and stronger bargaining power

Source: CBRE Research, April 2025

[1] CBRE Investor Intentions Survey 2025, INREV Investment Intentions Survey 2025
[2] CBRE Return to Office: Germany, CBRE Global Workplace & Occupancy Insights, CBRE C-Suite Perspectives

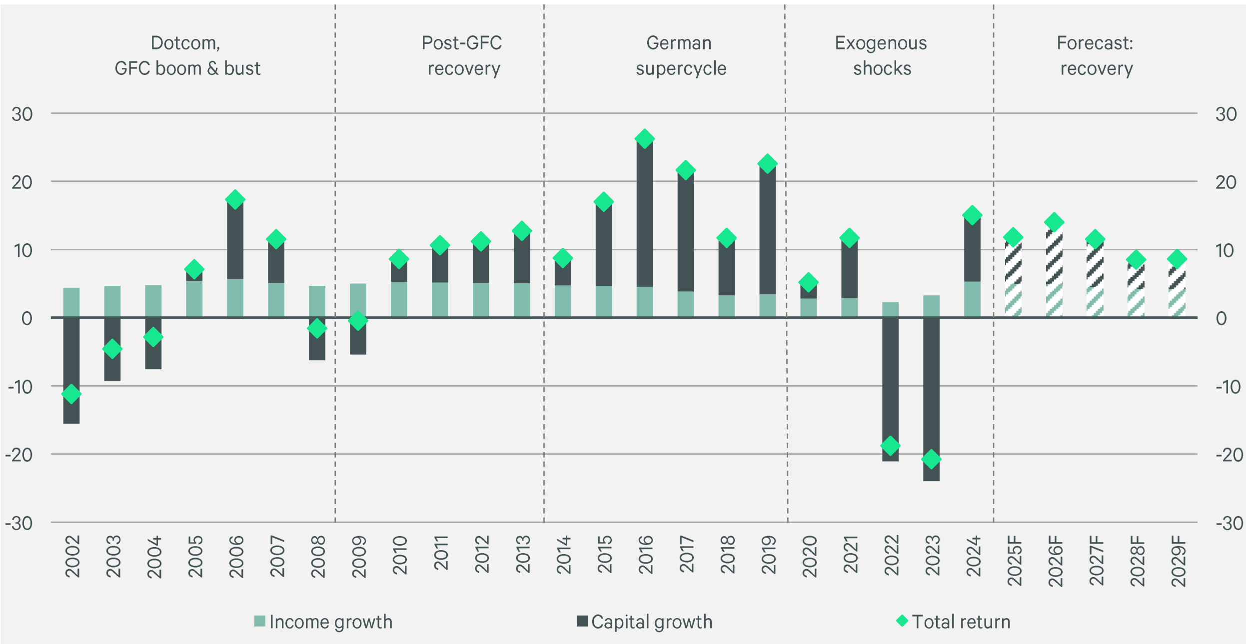
Capital values to rebound - focus on income growth

The broader repricing creates recapitalization opportunities to provide fresh debt and equity to reposition underperforming or stranded assets, offering attractive entry points. A distinct 'barbell strategy' can be identified with a core strategy on one hand and value-add on the other to align with the current capital and leasing market environment.

The anticipated average capital value growth until 2029 is projected at 27% recovering from the cyclical through of 2023. Given the muted outlook for yield compression, the relative importance of income growth to total return during this recovery cycle is increasing with a higher relative impact on capital value growth and valuations. The anticipated capital market and interest rate environment indicates higher volatility, elevated downside risks and only potential for a slight yield compression (see Figure 3).

Core strategies continue to evolve around a conventional buy-and-hold approach, focusing on long and stable income. Opportunities herein are emerging from mispricing and dislocation situations. Value-add investors are increasingly able to capitalize on income growth in specific segments of the market. Rental growth is supported by undersupply on the leasing market and construction cost inflation. Investors with market access can achieve income growth through re-leasing and ERV reversion. It is unlocked via CapEx, where requirements have intensified to enhance underperforming assets and have been associated with higher risk-adjusted returns. Core-Plus strategies remain challenging as ERV reversion potential from light refurbishment, financing costs and asset availability often do not offset the associated risks (see Figure 5).

FIGURE 3: Synthetic total returns German offices Top-5 (in percent p.a.)



Source: CBRE Research, April 2025

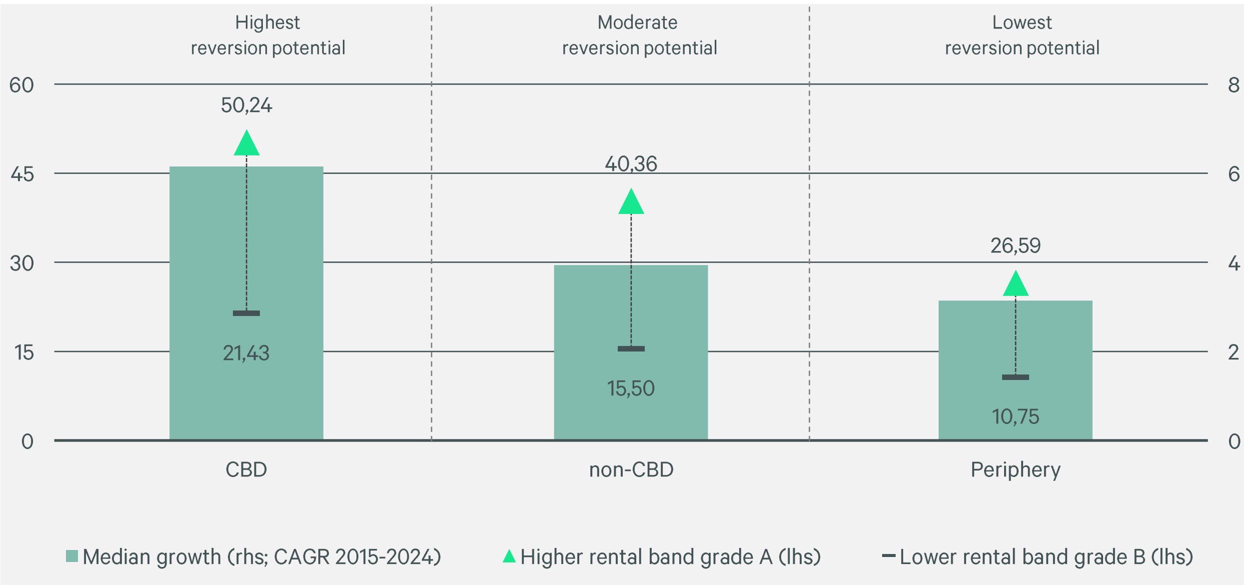
Reversion potential – but not in all segments

Understanding occupier demand is key for portfolio managers and investors to retain existing tenants, attract new ones, and transform their portfolios into the next cycle. Recent letting market activities and new inquiries from the German Top-5 are pointing toward a demand-driven consolidation and further polarization of leasing markets. Lease terms are becoming more flexible and occupier requirements for locations, fit-outs and amenities have increased. Hence, active asset management is mandatory again.

Against the backdrop of the ongoing low supply of adequate offices, some market segments will benefit from these structural shifts, whilst others are exposed to higher risks, underperformance or even obsolescence. Leasing evidence suggests a clear trend: the closer to a public transport station the younger the building age, the better the office fit-out, and the higher the lettability, rental growth and performance.

Driven by occupiers right-sizing and flight-to-quality, CBD Grade A offices have seen the highest rental growth during the past ten years indicating the underlying supply shortage. Vacancy rates in the German CBDs hovered below 5.0 % even during the recession and are forecast to 4.2% in 2029. Asking rents for newly built offices have increased in the double-digit territory, driven by construction price inflation and despite an increase in overall market vacancy rates. The CBD is poised for outperformance again and ERV reversion potential is the highest. Followed by non-CBD locations and less so in the peripheral submarkets, where vacancy rates are at their cyclical highs. Here, occupiers are offered multiple letting alternatives and from a developer's perspective, construction costs are barely been realized with achievable rents (see Figure 4).

FIGURE 4: Rental growth and stylized rent reversion potential by market segment in Top-5 (in €/sq m/month and percent)*



* Based on aggregated analysis of more than 29,000 letting transactions with 28.3 million sq m between 2015-2024
Higher Band: 75% percentile; Lower band: 25% percentile, Median: 50% percentile
Source: CBRE Research, April 2025

A growing opportunity set

The German office market is at an attractive entry point. 2025 and 2026 have the potential to become good vintage years for core as well as value-add strategies. This is mostly driven by the resilience and anticipated recovery of the German office letting markets. Demand-supply dynamics remain healthy in CBD and selected non-CBD submarkets supporting strong real rental growth and inherent upside potential.

Forward-looking return expectations are positive giving cause for improved underwriting assumptions, with a focus on income growth. Not all geographies and segments will perform equally though. Aside from the overall yield environment and return requirements, understanding letting fundamentals and deploying rigorous market due diligence on an asset-by-asset basis is key to identifying new opportunities along the risk curve.

FIGURE 5: Current stylized office investment strategies in the German market environment

	Core	Core-Plus	Value-add	Opportunistic
Approach	Buy-to-Hold	Manage-to-Core, Asset Management	Built-to-Core, Recapitalization	Development, Distressed
Income return	Stable	Moderate	High	High
Capital return	Low	Moderate	High	High
Segments	Stabilized grade A, CBD and selective non-CBD	Underrent grade A and B CBD, selective non-CBD	Dysfunctional grade C and B CBD, selective non-CBD	Distressed projects, Demand-driven submarkets
Challenge	Access to market and suitable assets	Access to market and suitable assets, financing	CapEx, mitigating project, ESG and reletting risks	CapEx, mitigating construction risks, financing
Appetite	High	Low	High	Selective
Target returns (Key metric)	4-6% (CoC)	6-8% (IRR)	12-18% (IRR)	> 20% (IRR)

Source: CBRE Research, April 2025

Contacts

Matthias Düsing
Associate Director
Research
matthias.duesing@cbre.com

Dr. Jan Linsin
Managing Director
Head of Research
jan.linsin@cbre.com

Marc Rohrer
Managing Director
Capital Markets
marc.rohrer@cbre.com

Sebastian Tiemann
Senior Director
Valuation Advisory Services
sebastian.tiemann@cbre.com

Matthias Mohr
Director
Valuation Advisory Services
matthias.mohr@cbre.com