

Intelligent Investment

Modern Living: New Housing Concepts Flourishing in Germany's Metropolises

VIEWPOINT

Modern Living is currently establishing itself in Germany against a backdrop of changing housing requirements. These concepts come in a range of variations, address different target groups and different rental models.

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Foreword

Student Living, Serviced Apartments, Co-Living, Micro Living, Service Living for Senior Citizens, and many other concepts are manifestations of a trend that has determined a range of different niches in the housing segment for some years now. These niches are a supply-driven response to changing requirements and demand in an increasingly tight housing market.

CBRE has set out to capture the plethora of terms and concepts, put them in context, and give them a workable definition. The asset class of **Modern Living** has emerged from these endeavors, a term that serves as a point of reference for developers, operators and investors wanting to classifying specific properties and concepts.

The following report identifies the drivers of the development and considers the target groups of the various concepts. An interview with representatives of Catella's pan-European Modern Living fund shares an insight into investor interest. The law firm GSK Stockmann subsequently provides an overview of the legal framework conditions prevailing in the segment, including rental price models.

Finally, the report provides an analysis of the offers currently observed in the market and the asking prices in Berlin in particular and the Top 7 locations in general. A differentiation is made between the various concepts.

We trust that you will find the report enriching and enjoyable reading, and we look forward to stimulating talks and discussions.



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joined CBRE in 2019 and, as an Associate Director in Residential Investment Germany, is currently responsible in the role of Team Leader for the topic of Modern Living. He holds an IREBS master's degree in real estate and is based in Berlin.

Housing Requirements in a State of Flux in Germany's Metropolises

Germany's metropolises, magnets for young people, are currently characterized by sea changes in demand structures. The pandemic has accelerated this process that has been ongoing for a while now. Students, both in the country and from abroad, weekly commuters and project team members are additionally crowding onto the tight housing market. Lastly, there is a lack of adequate housing supply for senior citizens.

This demand was originally served by special forms of housing and niche offerings. With demand becoming more specific, the concepts have become increasingly differentiated. Along with conventional purpose-built student accommodation, supply has steadily evolved for other target groups, with larger and/or barrier-free apartments, with higher quality fit-out, a more extensive range of services and much greater flexibility in booking arrangements. The concept of micro-apartments replaces Student Living as an overarching concept and is supplemented by concepts for later living with specific service offerings.

Modern Living as a New Asset Class

To do justice to these developments and variations, CBRE has coined the term **Modern Living**. In conclusion, Student Living, Co-Living and Micro Living are all subsumed under this term. As elaborated on in the following, these concepts are similar in terms of their structural features but can be clearly distinguished from other products, also when considering the price level for end customers.



Drivers of the Demand for Modern Living

National and international students

Modern Living displays a heterogeneous demand structure, characterized by the short-term requirements for accommodation. Students constitute the most important target group. Against the backdrop of the tight housing market and the lack of public student housing in university locations and in the metropolises, there is virtually no alternative to the private student hall of residence. Furthermore, the internationalization of Germany's university landscape since the start of the Bologna Process in the 2000s is progressing apace and driving demand. While the number of first-semester students has generally fallen due to demographic change, the number of international new students continues to rise and, at the last count, exceeded the all-time high of almost one quarter of all freshers recorded at the start of the 2018/19 winter semester. An additional boost emanates from high quality of German universities, the growing number of courses held in English, and the relatively low cost of a degree course in an international comparison.

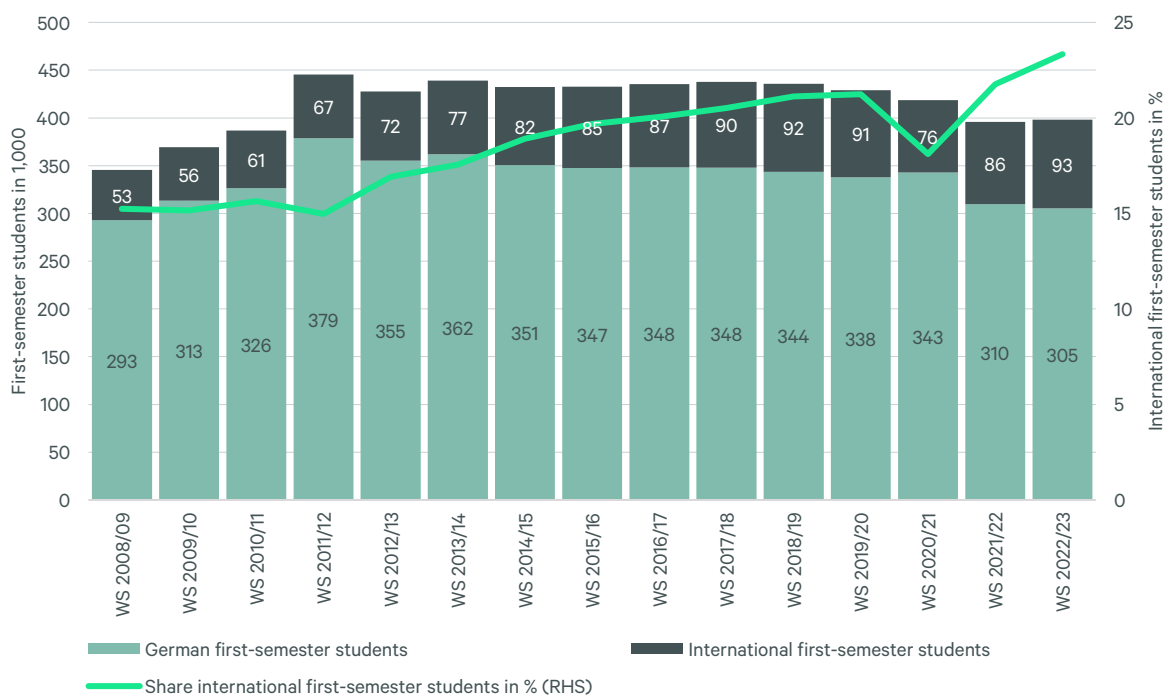
First-semester students in Germany - winter semester 2022/23

398,244

Increase in the number of foreign students since 2008/09

+76%

FIGURE 1: First-semester students in Germany (at the start of the winter semester respectively)



Source: German Federal Statistical Office, 2023.

International employees, young professionals, commuters

Along with the students, the gainfully employed also constitute a target group for Modern Living. The target groups range from young professionals (employees under 35 years of age) through to commuters and on to international employees (expats). The latter come to Germany in the context of temporary employment and therefore require adequate accommodation for a limited space of time, with a package of services combined as a welcome extra. Compared with 2022, the number of foreign academics has risen by more than 100,000 people. In addition, many employees moved into peripheral areas during the pandemic, only come into the cities infrequently, and therefore have a growing need for temporary accommodation. This also applies to project employees whose lives do not center around the current place of work. The number of commuters into the Top 7 cities (Berlin, Cologne, Düsseldorf, Frankfurt/M., Hamburg, Munich and Stuttgart) grew by 14 percent over the period from 2017 to 2022. The common denominator is initially the temporary nature of their activities at the place of work, with the search for accommodation not taking up too much time and ideally being fully furnished and available in the city center. Generally, employees rent accommodation directly, but it is also customary for companies to lease properties on a contingency basis for their employees*.

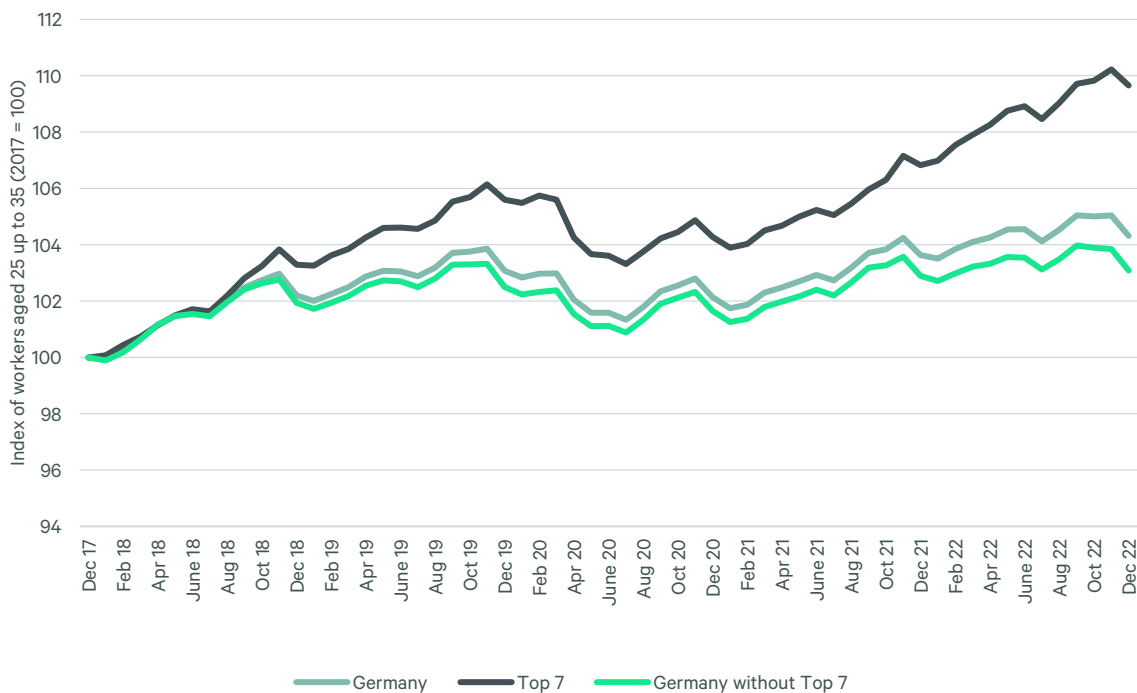
Foreign employees with academic qualifications in Germany in 2022

855,000

Number of commuters to work Top 7, 2017-2022

+14%

FIGURE 2: Index of workers subject to social security contributions aged 25 to 35, 2017-2022



Source: German Federal Employment Agency statistics; German Federal Statistical Office, 2023.

*Corporate Real Estate – Corporate Employee Housing & Accommodation (available in German only), CBRE Research 2022.

Senior Citizens

Serviced Living for Senior Citizens is a concept allied with Modern Living offering a solution beyond nursing, in conjunction with easy access accommodation and relative comfort. Demand is set to grow on the back of the demographic change, particularly as the number of people aged 70 and over in Germany is projected to rise by 36 percent to 18.5 million persons by 2040. The premise of giving precedence to “outpatient rather than inpatient” care underpins the trend toward purpose-built housing for older people. Service Living for Senior Citizens permits a concept to be established that offers an independent lifestyle, flanked by customized support provided in later life as needed.

Share of 65+ households with barrier-free housing

6%

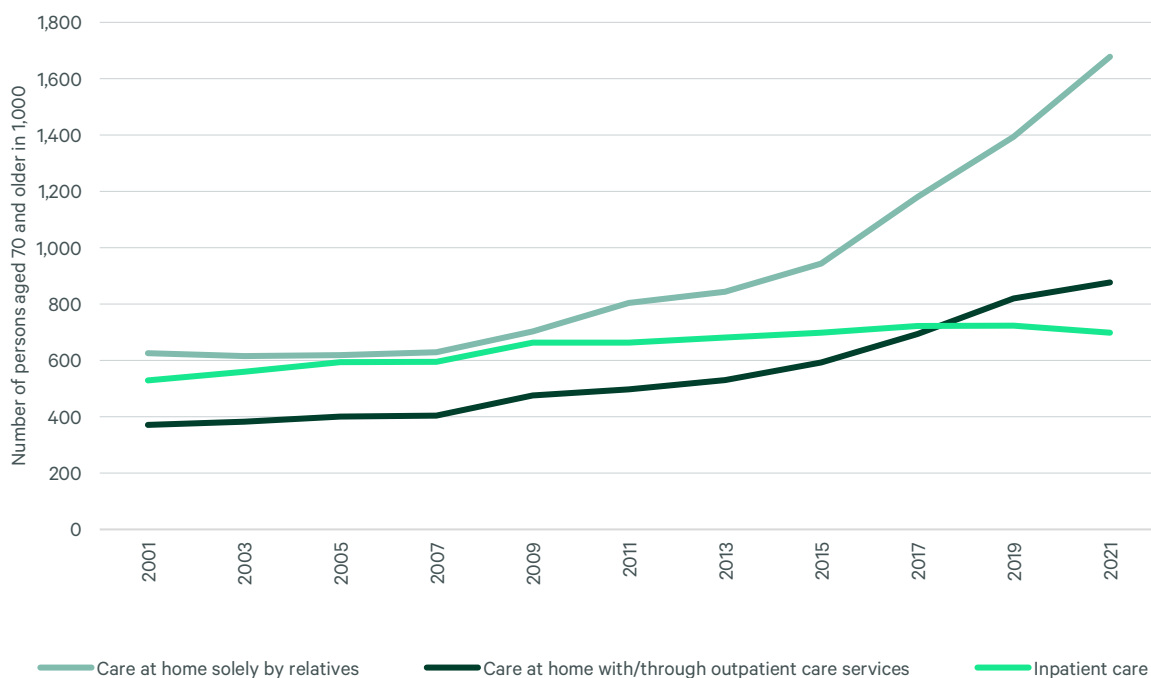
Number of 70+ persons cared for at home – 2011-2021

+96%

Tourism

In addition to students and people commuting to work, tourism also contributes to the demand. The number of overnight stays has almost returned to pre-pandemic levels. The Modern Living solution is attractive, particularly with longer stays, coupled with reduced or flexible need for services. The boundaries between this concept and the hotel sector are blurred here.

FIGURE 3: Persons aged 70 and older in need of care in Germany



Source: German Statistical Federal Office, 2023.

Investment Market

Investor interest in the Modern Living investment market has been on the rise since 2016. Whereas most (German) investors initially purely focused on the segment of student housing, they have expanded their investment strategy in recent years. In addition to purpose-built student accommodation (PBSA), other Modern Living concepts in particular are in decisive and growing demand. The transaction volume was formerly extremely supply driven, meaning that, with demand running steady, investments were only curbed by the lack of fresh supply. In the pandemic year 2020, the volume declined sharply, but concerns that the Modern Living asset class would lose its appeal after the pandemic years and that there would be less occupier demand have proven unfounded. Stable fundamentals are also reflected in the marked recovery in the volume during the years 2021 and 2022, with transaction volumes again exceeding the ten-year average. At the present point in time, as part of the interest rate turnaround and the associated higher financing costs, investment in Modern Living has also declined considerably though the relative proportion in the overall volume has recently been trending up again. Interest in investment opportunities in the Top 7 and in the traditional university cities continues to run at a high level.

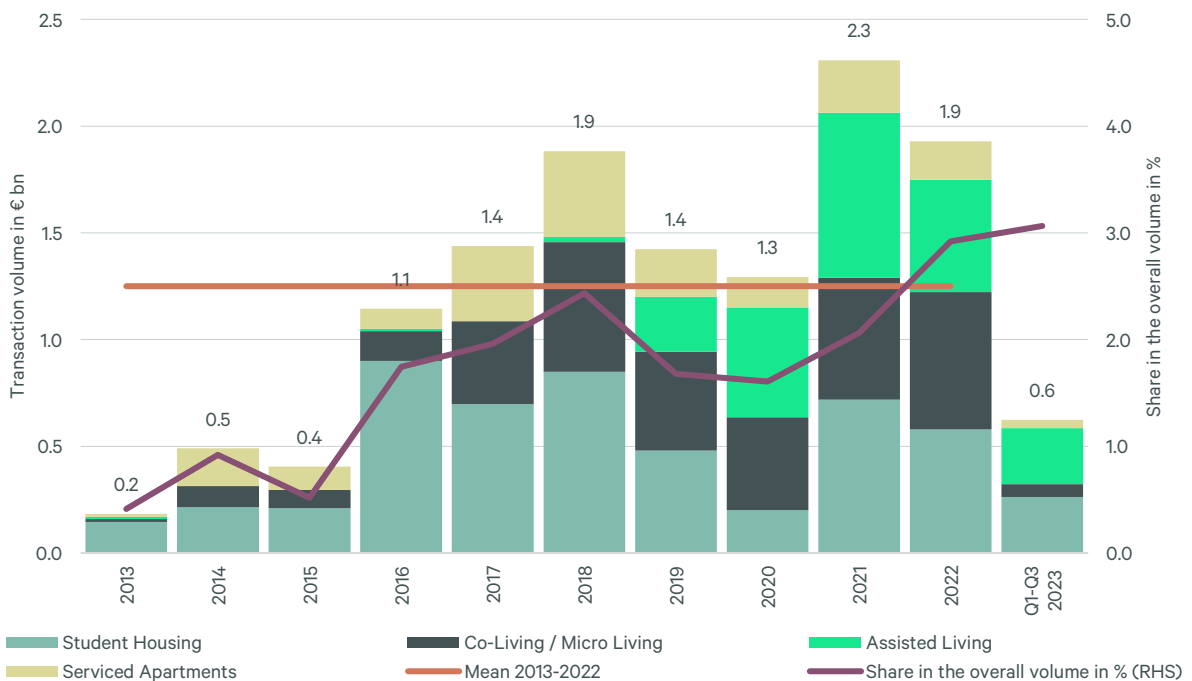
Modern Living transaction volume 2016-Q3 2023 in € billion

12

Share of special funds in the buyers of Modern Living 2016-Q3 2023

40%

FIGURE 4: Modern Living transaction volume



Source: CBRE Research, 2023.

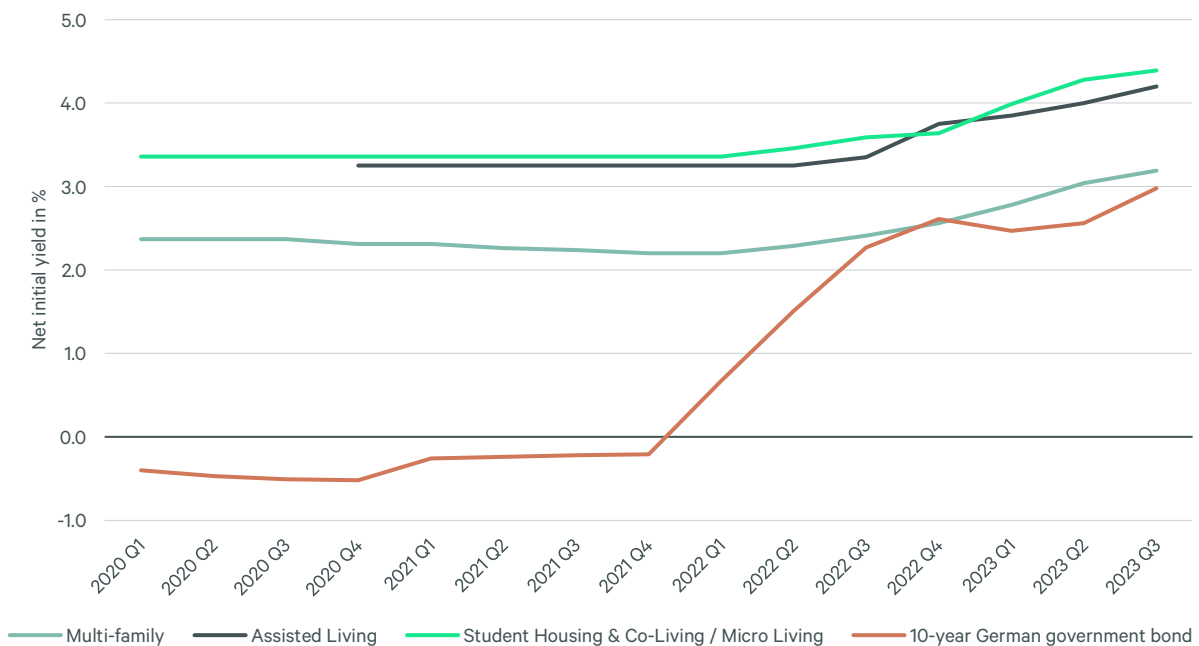
Determinant drivers of the keen interest in the Modern Living asset class consist, on the one hand, of the lack of rental regulation for furnished accommodation in Germany, which enables high and inflation-proof cash flows. On the other, the sub-segments of Modern Living lend themselves as diversification and yield drivers, above all for special funds focused on the residential segment. Pure theme funds are also increasingly being launched in the Modern Living subsegment.

The appetite of domestic and foreign investors remains unabated despite currently subdued market sentiment induced by the interest rates. In this context, investors from North America, the UK and Asia in particular, countries where Modern Living has already established itself as an asset class, are crowding onto the German market. These investors view the current maturing of the German market as an opportunity of securing market shares for themselves at an early stage, albeit with a stronger focus on portfolios or platforms. German investors have so far accounted for more than 60 percent of the buyers, also due to their home advantage. Along with direct investments, participations and takeovers of operator companies by international players have also been observed.

The current process of price finding, along with the lack of supply, are dragging on potential investments. The increase in construction costs and the high interest rate level have caused new build activity to decline significantly. Supply is unlikely to increase to any great extent in the near future, which will result in the ongoing imbalance between supply and demand. Although activities have slowed, only one third of the properties that changed hands in the past year originated from existing stock. The majority of the assets were traded in the form of forward deals, also against the backdrop of the ESG topic.

In response to the current situation on the financial markets, the yield for individual sub-segments has also trended up. Consequently, the average prime yield for Student Living in Germany's Top 7 markets came in at 4.39 percent in the third quarter of 2023, which is around 80 basis points above the level posted in the year-earlier period.

FIGURE 5: Modern Living prime yields 2020-Q3 2023



Source: CBRE Research, 2023.

TABLE 1: Modern Living in the purchasing profiles of 15 investors and investment managers

SIZE / VOLUME	<p>In eight of the 15 purchasing profiles analyzed, the target size of the properties to be acquired was considered a criterion :</p> <ul style="list-style-type: none"> - Minimum (e.g. €10 million and more per property) - Range (5,000 bis 15,000 sq m GFA or 200 to 350 residential units). <p>No restrictions or limitations that would fundamentally not accord with the format of the concepts were cited. From an investor standpoint, it is therefore unusual size or volumes in particular that could result in a decision against an investment.</p>
TARGET GROUPS / FORMATS / CONCEPTS	<p>The majority of investors have a broader investment profile than the subtypes considered here – if a specific focus is mentioned, this often pertains to students.</p> <ul style="list-style-type: none"> - Students (13 from 15 profiles) - Micro-apartments and young professionals (10/15) - Serviced apartments (5/15) - Senior citizens (5/15) <p>No concept in particular was excluded by the investors. Individual players nevertheless further define their investment profile by excluding operator-run properties.</p>
RISKS AND KEY DATA	<p>Information on the investment strategy and on yield expectations is given in 5 out of 15 profiles. In most cases, this information focuses on core and core plus, in one case also on value-add. Two investors specified customary market expectations of gross yield in a range of more than 4% and 4% to 6%. Against the backdrop of the changing market environment with interest rates trending up, these expectations are rising.</p> <p>Of greater relevance for most investors is the assessment after the due diligence has been performed (technical DD, environmental/ESG DD) and internal committee discussions.</p>
MACRO LOCATION	<p>As far as choosing a location is concerned, around half of the profiles investigated placed preference on “growing/established cities” without being more precise. Four out of 15 investors referenced a specific list of university cities, with A and B or C cities mentioned in some cases.</p> <p>It can be assumed that investors have similar ideas about the attractiveness of specific cities for the respective concepts. However, a key criterion for selection ultimately comes down to local demand expected in the long term.</p>
MICRO LOCATION	<p>In five of 15 profiles, proximity to the university and/or the city center is identified, with a further five investors considering infrastructure and transport connections and their crossovers as criteria impacting their decision.</p>
ESG	<p>The topic of ESG is explicitly cited by six of 15 investors in the context of acquisitions and investment. As regards the other investors, ESG is relevant in the context of their general investment strategies and partly addressed as a separate topic on their homepages.</p> <p>Specific aspects include:</p> <ul style="list-style-type: none"> - Energy efficiency (4/15) - Sustainability (3/15) - The availability of ESG documentation (3/15) - KfW standard (1/15) - “ESG takes precedence in investments” formulation (2/15)
ADDITIONAL CRITERIA	<p>In some cases, certain transactions structures such as share or asset deals are included or excluded, as are heritable building rights or part-ownership. In one profile, the desirable occupancy rate is specified at ≥90%.</p>

Source: CBRE Research, 2023.

Modern Living from an Investor Viewpoint

With a Modern Living mutual fund in a volume of around €500 million, Catella is one of the largest of its kind in Europe.

You have been actively engaged in Modern Living for many years. Why does this asset class interest you?

Housing is subject to constant change, especially as what people want from their homes is changing rapidly at present. Nowadays, people are required to relocate more frequently than before, either temporarily or permanently. Furnished accommodation offered on a temporary basis is therefore a response to rising occupier interest. Moreover, the product appeals to investors because of the yields it can deliver. The asset class is currently in the process of establishing itself and offers a yield mark-up compared with traditional housing. Along with furnished space, occupiers are also offered a range of different service packages – a commercially viable income component not to be underestimated.

A further advantage is the possibility of developing offerings on urban pieces of land close to the city center that, from the standpoint of the relevant building laws, are not suited to creating conventional housing. This being the case, Modern Living can contribute to providing accommodation close to the city centers despite competition from commercial usages.

Many decisions on location and concept are already taken during the phase of obtaining planning permission. What KPIs do you consider to be particularly important?

As with all asset classes, site and location are key. With Modern Living, access to public transport is more important than with traditional housing or many office buildings as the target group is younger and more international, values sustainability, and does not use the car as much, especially in urban areas. With housing for the elderly as well, public transport is often more important than private means of transport. Furthermore, the quality of building permit is particularly critical as this has a decisive influence on the feasibility of the specific design of a concept in terms of the length of stay, the potential target groups, and the range of services offered. The extent to which the final realization of a project depends on the local planning authorities and the specific contacts is often comes as a surprise to global players. We therefore view the actual obtaining of planning permission as an important component in risk assessment.



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Dr. Lars Vandrei

is responsible for research at Catella Residential Investment GmbH.

What impact do the aspects have in the context of risk and return?**Is Modern Living suitable for hedging inflation?**

Inflation hedging is an important aspect and can be realized 1:1 on the back of currently rising rents and high fluctuation rates in Modern Living when leasing directly. In the case of operator models, inflation hedging is assured via indexing the lease agreement, albeit even when not at 100%. The more heavily residential a concept is, the lower the yield premium is. Concepts that focus more strongly on services offer higher yields, but also harbor greater risk. At this point, we always investigate vacancy and default risk. Moreover, having the format established in the market is also important. As far as financing is concerned, of relevance is the question of whether a planned property can be allocated to a concept the bank is familiar with – or whether the business model is completely new and has to be explained. This aspect is clearly reflected in the interest rate applicable to financing. For their part, our investors expect the higher risk to be reflected in their payouts. The yield premium compared with conventional housing varies in Modern Living concepts synonymous with residential or close to residential usage between 50 and up to 150 basis points for service-oriented (hotel) concepts.

Let us include the topic of ESG – what impact do the rising requirements have in your opinion?

It is true that the requirements and thus the price of realizing a project are on the rise. Nevertheless, we basically believe that the KfW Efficiency House 40 (energy consumption 40% less compared with a standard building) is feasible. The high price of land in the recent past that has not been fully factored in by many vendors is rather more of current challenge in calculations at the moment. ESG, on the other hand, offers genuine value especially as far as lowering the high ancillary costs in Modern Living is concerned, with the commensurate impact on yield. In addition, lenders are looking for future-proof investments, so we generally only invest in Article 8 and Article 9 products. We also place emphasis on social heterogeneity and affordable rents in the properties which is, by the way, also required by German institutional investors in particular. Although rents in Modern Living appear to be higher when compared with traditional residential – often and then, especially if one includes communal areas and services – many Modern Living concepts create additional living space that was generally not provided for under building regulations. Flexible and unbureaucratic access enables Modern Living (along with other functions) to create an additional fluctuation reserve that improves the allocation of tenants and residential units on the markets, thereby easing the burden.

What in your view are the future drivers of demand for Modern Living?

In many ways Modern Living is a future-oriented project. Against the backdrop of housing shortages in Germany's metropolises, the subsegment of Modern Living offers a solution to target groups whose needs are not, or only partly, met by conventional housing. One of the most important drivers consists of international students who, also in the wake of Brexit, have increasingly discovered Germany as a place to study. Furthermore, people embarking on a career, along with project team members, make up a growing target group. Given demographic change, we ultimately also consider older people as users of Modern Living who, in addition to living close to the city center, also want to make use of services while relinquishing ideas about the size of their accommodation.

Generally speaking, we believe that the change in urban lifestyle away from conventional housing toward more shared economy, a growing number of single households, and flexibility as to time will cause demand for Modern Living to rise further.

Concepts for solutions

On the one hand, Modern Living is distinct from the conventional free housing market through its offering of communal space and services (amenities). On the other, the supply of hotels is to be differentiated from Modern Living as stays of one night only are generally possible. This short length of stay does not fall under the concept of Modern Living. Concepts are generally realized by an operator, but also by leasing directly that is particularly customary in the case of Student Living. The various solutions on offer can be distinguished from one another by the following features: duration of stay, scope of the communal areas and services, and the target groups.

Purpose-Built Student Accommodation (PBSA) and Micro Living

Purpose-Built Student Accommodation (PBSA) is defined as exclusively on offer to students. This concept does not therefore include any rooms in house shares or generally smaller apartments on the free housing market as these are basically available to all tenants. The purpose-built student accommodation investor product has been established for a considerably longer time on the British market so that the name and definition, together with demand for the product on the German market, originates from the English term. PBSA as an asset class in the UK also defines the product in Germany as accommodation specifically built for students. The concept of **Micro Living** has established itself as a synonym for the growing PBSA asset class, as the product is increasingly offered not only to students but also to professionals.

Co-Living, Temporary Living and Serviced Apartments

In tandem with regional distribution, the supply has evolved further to address broader and different target groups. The term **Co-Living** has established itself for this product in the UK and on the European investment market. The characteristic features of this offering include communal space and special events as well as, in the past, a higher proportion of rooms in shared accommodation.

In addressing young professionals, the concept is also designed for weekly commuters and employees working on location for a limited period of time. The concept incorporates furnished apartments that are easy to book at an all-in price without any great emphasis on communal space and events. In this context, the term **Temporary Living** is increasingly used in the marketing phase. An addition to include services customized for shorter stays for the target group of business travelers and tourists is marketed as **Serviced Apartments**.

Service Living for Senior Citizens

Service Living for Senior Citizens is defined by being specifically designed for the target group of senior citizens. As opposed to the other four forms, unfurnished or partly furnished apartments are leased. However, unlike the free housing market, mandatory and optional services are offered. This format, in part also known as **Assisted Living**, is experiencing growing interest from developers and investors specialized in the asset class of Modern Living.

Service Living for Senior Citizens

Demographic change in our society is behind the steady increase in the need for senior citizen housing. The distinguishing features of the concepts with services in the market are increasingly perceived by the target group as a solution distinct from care homes and, as such, demand is stronger. Both the general shortage of barrier-free accommodation (DIN 18040-2*) and security later on in life, guaranteed by the provision of support services individually customizable and scalable, play a role.

Service Living for Senior Citizens provides a solution for a barrier-free supply of accommodation with services especially tailored to older cohorts as the target group. A part-time concierge service or in-patient service located in a neighboring building for the purpose of providing advice and acting as an intermediary for procuring additional services is generally offered as a minimum. By contrast, premium residences for senior citizens offering a versatile range of communal areas, including a wellness area with a pool and a sauna and an exclusive restaurant, are located at the other end of the spectrum, for instance. Similar to a hotel, personnel are also available on site 24/7.

The term Assisted Living designates offers of Service Living for Senior Citizens with a low level of service (basic service) and/or greater care-oriented offers. Apartments for senior citizens, either separate or attached to a care home, are marketed as Assisted Living. With Service Living, emphasis is placed on the aspect of independence, with support in the form of care as an optional safety net that, in the case of this target group, is more relevant for the future.

Rent is partly stated as an all-in price and is often communicated as the sum total of base rent, ancillary and operating costs, as well as a service charge. The broad range in terms of the quality of the offers (similar to hotel classifications on a scale of up to 5 stars) and variations in the components included in the service charge (particularly meals) are to be noted in a direct comparison of pricing.

SITE / LOCATION	Wide range (both urban and peripheral locations)
APARTMENT SIZES	Generally 30-70 sq m, premium offerings also with larger apartments
RENTAL MODEL	"Warm" rent ("Warmmiete" meaning including heating and running costs) and obligatory service charge
PREMISES / SERVICES	Depending on the level of quality, concierge, communal area, counseling services through to wellness area with pool, restaurant
OPERATORS / CONCEPTS	Charitable providers <ul style="list-style-type: none"> - AWO, DRK Ecclesiastical providers <ul style="list-style-type: none"> - Diakonie, Johanniter Private care home operators <ul style="list-style-type: none"> - Alloheim, Victor's Group, Korian Premium providers <ul style="list-style-type: none"> - Augustinum, Rosenhof, Tertianum

Source: CBRE Research, 2023.

*A standard issued by the German Institute for Standardization, providing guidelines on accessibility and usability in the built environment.

Private Purpose-Built Student Accommodation

The offering of student housing operated by the public sector or a university's "Studentenwerk" (publicly funded non-profit organization for student affairs in Germany similar to student unions in the UK) is extremely limited and often associated with long waiting lists. A market for private concepts has therefore established itself over the last decade. Demand is driven, on the one hand, by the rising number of national and especially international students. The latter are accustomed to living in private student halls of residence, as is customary in their own home countries, and factor in these costs when calculating their stay. Furthermore, the tight housing markets in Germany's cities only offer a few options for students to share accommodation. In recent times, international entrants have surged onto the market wanting to transfer their experience from more mature markets to Germany.

Student halls of residence (aka PBSA) offer living space exclusively designed for students. In the new-build segment, self-contained apartments (studios) are standard. The studios offer privacy and an environment in which students can concentrate on their studies. Apartments are generally offered including a bathroom and a kitchen. Some concepts deliberately offer a kitchen for communal use.

Student halls of residence are a residential concept. Rental agreements are concluded for a semester at minimum. Rent is generally all-in. The fit-out of the individual building may vary widely (possibly including a private bathroom/kitchen, communal areas and/or sports facilities). Apartments or rooms for single occupancy are offered in shared accommodation. The combination of privacy and community is aimed at enabling students to integrate quickly.

Private sector solutions are priced above apartments in public "Studentenwerk" halls of residence. They are rarely government funded and are generally realized as new builds or repurposing of existing stock and tend to be equipped to a higher standard. Operators standardize their offers and facilitate digital leasing, above all, with a view to enabling remote renting by international students without the necessity of viewing.

SITE / LOCATION	University cities (proximity/connection to universities and/or city center)
APARTMENT SIZE	Generally, 18-25 sq m, larger apartments as premium offer
RENTAL MODEL	All-in rent
PREMISES / SERVICES	Community, learning rooms and/or gym, terrace or outdoor area, laundry room, cleaning of areas, events
OPERATORS / CONCEPTS	Local "Studentenwerke" German private concepts – SMARTments student, THE FIZZ, Staytoo, Campus Viva, Neon Wood International private concepts – Basecamp (Xior), CAMPO NOVO, YOUNIQ

Source: CBRE Research, 2023.

Co-Living and Micro Living

The Co-Living concept offers private living space, supplemented by communal areas. Offers in the market are partly only distinguished from Student Living by the fact that they address a broader target group. The Co-Living concept places emphasis on the communal areas and regular events offered for the community. Fully furnished and shared housing concepts with fit-outs often of a higher quality are offered as individual residential communities with their own front door.

The Micro Living concept offers small, self-contained furnished apartments. Tenants pay an all-in rent that includes all ancillary costs. In terms of presentation in the market, salient features include flexible booking options as well as private and fully equipped accommodation. Unlike Co-Living, Micro Living does not include events for the community and only offers a low proportion of communal areas.

Target groups also include students, but principally address young professionals, commuters, expats and project team members depending on the concept and the location. Micro Living focuses more on people on business trips in one location and also targets international employees in particular. Apartment contingencies are in some cases leased on a permanent basis by companies.

The concepts offer a diversity of extras. Co-Living concentrates on events and areas for the community. Micro Living focuses more on private amenities and partly offers cleaning of an apartment on a weekly basis, a laundry service for clothing, or an order and delivery shopping service.

Depending on the length of stay, both concepts may incorporate commercial or residential usage. Independent housekeeping in a formal sense is not given in every case – though the main place of residence and registering the address is possible, the contractually agreed term of tenancy is nevertheless partly limited and any stay is therefore not of a permanent nature. Co-Living offers partly open-end rental contracts, particularly with furnishing and shared accommodation arrangements. In the case of Micro-Living, leasing for a period of at least one month is possible, with stays being limited to twelve months.

SITE / LOCATION	Urban locations or locations with good transport connections in the Top 7 and B locations
APARTMENT SIZE	Mainly in the range of 20-50 sq m, average size of around 30 sq m
RENTAL MODEL	All-in rent
PREMISES / SERVICES	Co-Living: communal kitchen, gym, terrace or outdoor areas, events Micro Living: laundry room, customized service
OPERATORS / CONCEPTS	German private concepts – i Live, Cube Life, Urban Base, Tannhaus International private concepts – Habyt, Home & Co, The Social Hub

Source: CBRE Research, 2023.

Serviced Apartments

Strictly speaking, Serviced Apartments are allocable to commercial usage as stays are short term and not intended to be permanent. Accordingly, leasing arrangements pertain to temporary hotel-like accommodation and not to housing as such. The concept is therefore to be differentiated from Modern Living. Its versatile manifestations in the continuum between hotel and Micro Living also serve the needs of Modern Living target groups while attracting the interest of investors and operators active in this asset class.

The concept is defined by the scope of services and the short stay of guests. Service may range from a minimum package such as room cleaning right through to a scope of services similar to that of hotels. Stays are generally less than six months but, clearly distinct from hotels, always more than one day. So-called aparthotels/apartment hotels offer apartments for a period of less than one month with services similar to hotels.

Service apartments' main target group consists of professionals who live and work in a city for a short period of time. The concept also targets tourists. Along with the option of booking periods shorter than one month, the greater scope of services also sets serviced apartments apart from Micro Living. Buildings often offer a bistro, bar and/or restaurant, allowing overnight stays with breakfasts to be optionally booked. Some concepts offer gyms or spa activities, along with co-working space either on site or nearby as part of the package or for an extra fee.

The rents/prices for service apartments are considerably higher than for residential offers and compare more with prices in the hotel industry. This is determined by the short-term lets and consequently virtually unavoidable vacancies in between occupations, as well as the (more or less) extensive service package.

SITE / LOCATION	Urban locations in the Top 7 and B locations
APARTMENT SIZE	Principally in the range of 20-45 sq m, larger apartments as premium offer, average size of around 30 sq m
RENTAL MODEL	All-in rent
PREMISES / SERVICES	Lobby, co-working space, bistro, laundry room, apartment cleaning, bespoke services
OPERATORS / CONCEPTS	<p>German private concepts</p> <ul style="list-style-type: none"> - SMARTments business, JOYN, STAYERY, Brera, ipartment <p>International private concepts</p> <ul style="list-style-type: none"> - The Base, The Flag

Source: CBRE Research, 2023.

Analysis of Supply using the Example of Berlin

Berlin is Germany's largest market for Modern Living. With around 120 properties and approximately 25,000 residential units in total, all standard concepts have been implemented in Berlin. Student Living accounts for 73 properties, 16 of which are privately operated in the city. A low rate of supply of student accommodation, compounded by the general shortage of housing in the city, will boost the ongoing development of these concepts in Berlin.

The distribution of concepts on offer shows a concentration on the city center, demarcated by the Berlin Ring railway line. Student Living properties, along with Co-Living and Micro Living, are predominantly situated in larger university and research locations. Properties therefore cluster in the south-west in the locations of the Free University and in the south-east where parts of the Humboldt University are based. Adlershof, with its technology park and its proximity to the airport, also lends itself to these concepts. Serviced apartments are mainly concentrated in the Mitte district, with its tourist attractions and businesses.

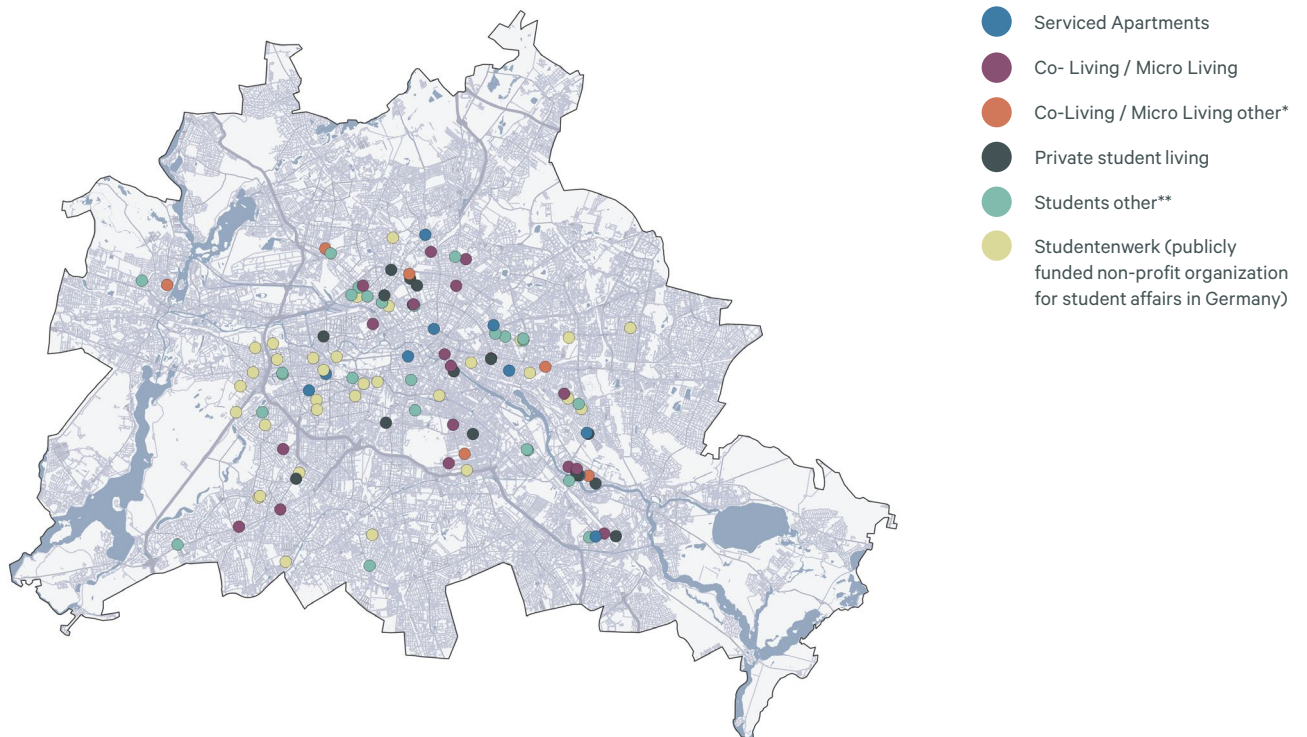
Ratio of rooms in student halls of residence to students in Berlin

1/10

Average year of construction (median) of privately offered accommodation

2017

FIGURE 6: Distribution of Modern Living solutions in Berlin



Source: CBRE Research, Open Street Maps, 2023.

*Offers of state-owned companies and those not fully corresponding to the format.

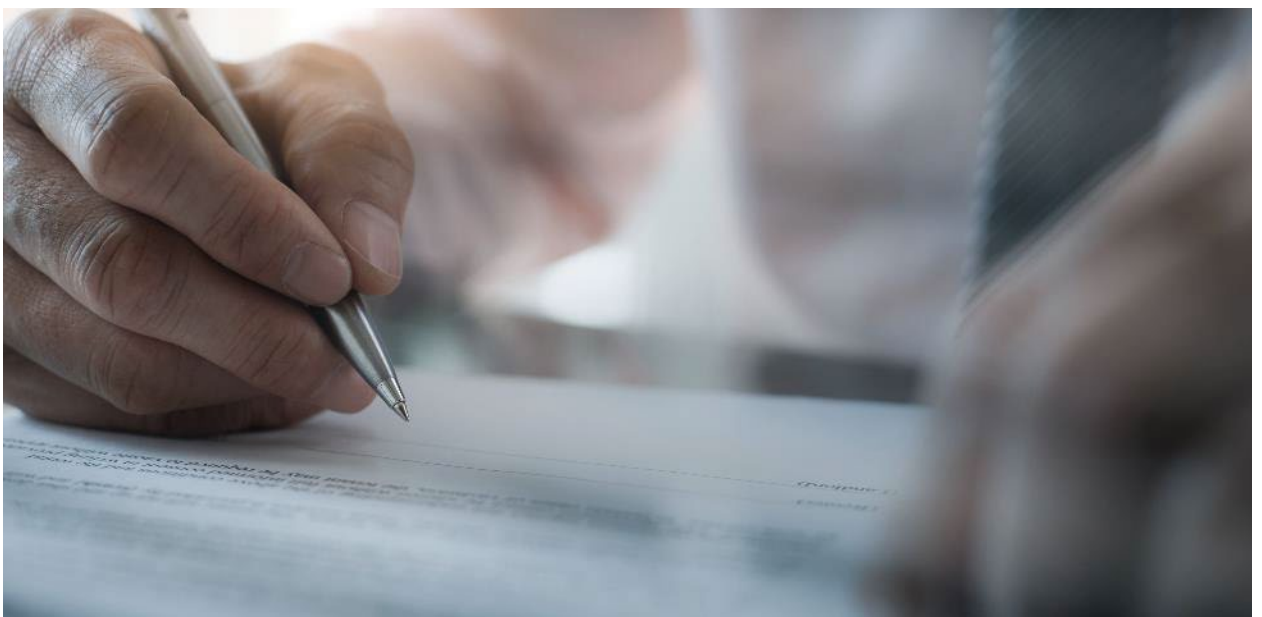
**Ecclesiastical and non-profit operators, student fraternities, associations and state-owned companies.

Legal and Tax Framework for Temporary Forms of Residence

Guest article by GSK Stockmann

Temporary forms of living have many names. The names themselves are often not used precisely. The actual form the concept takes is decisive for legal classification. An evaluation and assessment of the respective operator concept are what count. The relevant laws recognize two classifications above all: residential or hotel. Depending on the concept, temporary forms of accommodation occupy a gray area in terms of civil, construction, misappropriation (“Zweckentfremdung”), tax, and regulatory law, and may be more residential or hotel-like in nature. The concept is based on assumptions that must hold water from a legal perspective. The main levers include:

- Short-term leasing is generally subject to VAT.
- Agreeing an all-in rent is generally permitted but must nevertheless also be viable in terms of tax law.
- Short-term forms of residence and student halls of residence are generally exempt from most provisions governing tenant protection. What is critical is that the concept complies with the statutory requirements.
- The digital conclusion of leasing agreements is attractive but nevertheless often requires setting up a qualified electronic signature.
- Framework conditions prescribed by building regulations determine which usage concept is eligible for approval on which areas earmarked for construction – in consideration of the potential disruption or noise sensitivity. A building permit will only be issued if the concept envisaged satisfies the requirements of the prevailing planning regulations.



Distinction between residential/non-residential (commercial) from a VAT perspective

Leasing can be exempt from or subject to VAT. This will determine a landlord's right to deduct input tax. As far as the landlord is concerned, leasing subject to VAT is desirable as this allows for the possibility of deducting input tax. This being the case, VAT paid on input purchases (goods and services) can be reimbursed to the taxpayer as input tax.

Leasing of residential accommodation

The leasing of residential accommodation is exempt from VAT if the lease is long term. Rent is therefore owed without VAT. If VAT is nevertheless charged without any legal grounds, the landlord will also owe this tax to the tax authority as unauthorized tax, without any right to deduct input tax being conferred. For this reason, care must be taken not to include VAT on an invoice when billing tenants. This tax exemption does not apply to providing short-term accommodation for guests where the landlord has the intention of making the premises available for a period of up to six months. In this instance, leasing is subject to VAT in principle. If the same premises are made available for the option of long- or short-term letting, all letting transactions pertaining to these premises are subject to VAT. If no VAT is applied to a short-term let, the amount due on the agreed rent must be paid to the tax authority. It is therefore particularly important to show VAT separately in the case of short-term leases in order to avoid any damage to commercial interests. Distinguishing between the individual cases can be very difficult especially given the wide range of applicable criteria. Experienced tax experts should therefore be consulted in the assessment process.

Leasing of commercial property

The leasing of commercial premises is also generally exempt from VAT. An option to make the lease subject to VAT is only possible if the tenant is an entrepreneur within the meaning of VAT law, if the lease is for the tenant's business, and if the tenant uses or intends to use the premises exclusively for transactions that do not preclude the deduction of input tax. These conditions are typically not met when renting out residential space. The following therefore applies: rentals intended for the long term are generally exempt from VAT. However, depending on the tenant's services or line of business, the landlord may waive this VAT exemption and opt for VAT.

All-in rent

If there is a high turnover of new occupants, preparing ancillary cost statements at regular intervals and installing meter reading devices are often undesirable. Instead, an all-inclusive rent (meaning rent including heating, hot water, electricity and operating costs) should be agreed upon.

As regards the usual operating costs according to the German Operational Costs Ordinance (Betriebskostenverordnung), a lump sum payment can be concluded. Under the German Heating Costs Ordinance – meaning heating and hot water – this is generally not permissible since at least partial consumption-based billing is prescribed for these utilities. In the case of student residences and similar accommodation, heating and hot water may also be billed on a flat-rate basis, however. There are good arguments for flat-rate billing for heating and hot water being permissible for temporary accommodation concepts. However, charging an all-inclusive rent for electricity is a gray area that needs to be assessed on a case-by-case basis from an energy, tax and regulatory perspective.

In the case of VAT-exempt rentals, the ancillary costs included in the all-in rent should also generally be exempt from VAT (no separate VAT on the costs charged on by the landlord). If VAT is included in the ancillary costs, the landlord may pass on the gross amounts (including VAT). The services in connection with leasing properties that are exempt from VAT also include the customary ancillary services that are directly and economically incurred in this context (including heating, hot water, the use of washing machines, the cleaning of common areas, electricity, if applicable).

Planned special or additional services such as cleaning and laundry services should not be encompassed by the aforementioned VAT exemption, as these are basically independent services within the meaning of VAT law. The statutory standard tax rate of currently 19% applies to such special services. The person liable to pay VAT on these special services is, in principle, the entrepreneur providing the service. If the special services are provided by the landlord, then they are responsible for paying VAT on these services to the tax office. The landlord can avoid an economic burden by simply "charging" VAT to the tenant on a contractual basis. Depending on the type of offer, however, these special services can also be "merged" into a single service with the rental. Consequently, all services, including the rental, would then be subject to VAT.

It is in principle possible for rental companies to achieve full relief from trade tax, for instance by seeking the extended trade tax reduction in the case of commercial rental companies or, if the landlord is an investment fund, by not engaging in active commercial management. In principle, special or additional services that are atypical for rental purposes may only be provided to a certain extent for this purpose. Coordinating trade tax relief at an early stage in the project with tax law experts on a case-by-case basis is essential. This rings especially true as the legal regulations have been subject to regular amendment in recent years and continue to evolve.

Peculiarities under tenancy law pertaining to temporary and student housing

Various regulations under conventional residential tenancy law do not apply to "temporary housing" and "purpose-built student accommodation". Such regulations include in particular caps on the amount of rent increases ("Mietprelsbremse"), along with the possibilities of limiting the term of rental contracts and charging flat rates for operating costs.

Accommodation is only deemed temporary if an apartment or room is rented out for a short period of time and for a temporary purpose (e.g., renting to commuters, guest lecturers, seconded employees, and similar). A short period has so far been defined as one year. A legislative initiative of the Bundesrat to shorten this period to six months is currently under way. Establishments let to students count exclusively as purpose-built student accommodation, and only if they fulfil the so-called rotation principle, meaning that the period of occupancy is limited and changes frequently. This is only a point of reference, however. The more a property is distinguishable from and set apart from conventional student accommodation, the more likely it is that normal residential tenancy law will apply.

It is important that the concept envisaged is also "lived out" in practice. For instance, if an officially approved student hall of residence is rented out to non-students this can be problematic. A specific building permit does not therefore necessarily allow general residential letting.

From a tax perspective, our comments above on distinguishing between residential and commercial usage and all-in rent apply accordingly.

Digital conclusion of contracts

People wanting to rent an apartment at short notice usually only travel to the destination when they are due to move in. Rental agreements therefore need to be concluded as efficiently as possible and via digital means. However, the law stipulates that rental agreements with a term of more than one year must be concluded in writing (with the requirement of a manual signature). Rental agreements with a term of less than one year can also be concluded orally or by mail. Rental agreements with index-linked or graduated rents must always be concluded in writing regardless of the term.

In order to be able to conclude contracts subject to the written form requirement digitally, the option of replacing the written form requirement with a qualified electronic signature (qeS) was created a few years ago. In concrete terms, this means that the entire contract can be created and concluded digitally, provided the respective signatures are in the form of a qeS. The decisive factor is that the qeS requires users to register via a certified provider in order to ensure that the digital signature also originates from the respective party.

General conditions under building law

The classification of usage concepts under building law is necessary for checking their eligibility for approval. This is often difficult because the German Building Regulations (BauNVO) make a primary distinction between the categories of residential property and establishments providing temporary lodging. While obtaining approval for residential use of property tends to be easy in pure and general residential areas and in urban areas and mixed-use areas, operations in the commercial (hotel-like) accommodation business must be located in urban areas, mixed-use areas and core areas, and can also be considered in commercial areas where residential use is generally not permitted.

The Federal Administrative Court (BVerwG) has determined the various usage types. Accordingly, residential use is defined as domestic and intended to be permanent, allowing individuals to organize their own households in the domestic sphere. A feature characteristic of residential use is that it is an integral part of private life, enabling individuals to develop undisturbed and in private, to the exclusion of third parties. In contrast, businesses in the (hotel-like) accommodation sector provide temporary, overnight board and lodging, making premises available to a constant flow of guests in return for payment. Unlike residential use, guests do not set up independent households in establishments of this kind.

Merely how the concept is labeled is therefore not important for classification under building law and the issue of eligibility for approval. Instead, the emphasis is placed more on an examination of the concept to determine whether it is intended for domestic living arrangements.

Along with a toilet and washing facilities, features typical of residential use include a kitchen or cooking facilities in particular, which may also be available for communal use. In addition, the courts often examine the size of residential units, with common areas possibly also being of relevance, especially in new concepts, provided that each resident has the option of private retreat.

Commercial rental concepts are generally not suitable for ensuring long-term domesticity because of the size and configuration of the premises. The concepts are often – though not necessarily – associated with additional services.

In addition, the duration of the planned use usually plays a significant role in distinguishing between concepts. However, this is at best an indication as to whether a domestic living arrangement is possible in the premises or not. As the usage concept is assessed in its entirety, there are no fixed minimums with regard to the planned rental period. Usage entailing residence of two to six months and three to eight months has already been deemed by various courts as sufficient for residential use within the meaning of German planning law. On the other hand, usage concepts in which tenants usually stay in the premises for only "a few weeks" and which provide services typical of temporary hotel-like accommodation, such as breakfast and cleaning services, are to be classified as accommodation businesses according to the Higher Administrative Court of Berlin-Brandenburg.

Finally, the Bavarian courts in particular have also focused on whether the units were rented out subject to VAT. Since the VAT exemption applies to residential rentals lasting more than six months (Section 4, item 12. lit a UStG), a discrepancy between residential accommodation under building regulations and residential accommodation within the meaning of tax law is conceivable, especially in the case of regular rentals of more than three months. However, if the units in a building are predominantly (more than 95%) rented out for a maximum of around three months and are subject to VAT, the Administrative Court of Munich and the Bavarian Administrative Court of Appeal ruled that the building in question was an accommodation business.

Service Living for Senior Citizens

Service Living for Senior Citizens and Assisted Living are making inroads as an alternative to conventional nursing homes for people requiring support in old age but who can and still want to live independently. The salient feature of these concepts is the agreement of a certain level of services to supplement traditional living (accessible units for disabled tenants, emergency call service, housekeeping). Further care and nursing services can be added as required.

Self-determined Service Living for Senior Citizens is not subject to the stringent building regulations applicable to nursing homes, such as minimum sizes for private living space or shared rooms, requirements for access to bathrooms and single room contingencies. A careful and detailed examination must be conducted to establish whether the rental concept actually falls under the regulatory regime in individual cases because the required level of independence and self-determination is not achieved.

In some cases, a residential lease is concluded for letting the apartment and a separate service contract is concluded for cleaning, meals or emergency call services. In the domain of nursing care, compliance with the Residential and Care Contract Act (WBVG) that comprises rules and regulations on entering into contracts, notices of termination, etc., is mandatory. Whether the WBVG is applicable to the concept in question must be examined on a case-by-case basis.

Outlook

An amendment to the law on short-term leases was recently passed by the Bundesrat. Section 549 of the German Civil Code (BGB) that provides for an exception to tenant protection regulations for temporary housing is to be tightened. As a rule, the exception no longer applies to lease terms of six months or more, meaning that residential tenancy law now applies to such contracts. Landlords are thus no longer able to set a time limit or charge whatever amount of rent they want. Furthermore, the "Mietpreisbremse", a cap on rent increases, is applicable unless the property is a new building (first occupation after October 1, 2014).

This bill must now be debated in the Bundestag. Although this will create more clarity around the concept of temporary housing, this will be at the expense of temporary housing concepts, which will be further constricted.

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In legal terms, temporary forms of accommodation occupy a gray area depending on the concept.

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Rent Components and Rental Rates

Modern Living concepts encompass a range of different rental models with different components, some of which are included in the rent or can be additionally booked if required. This needs to be factored into comparative analysis of the range of rents entailed by the various concepts in the Top 7 cities.

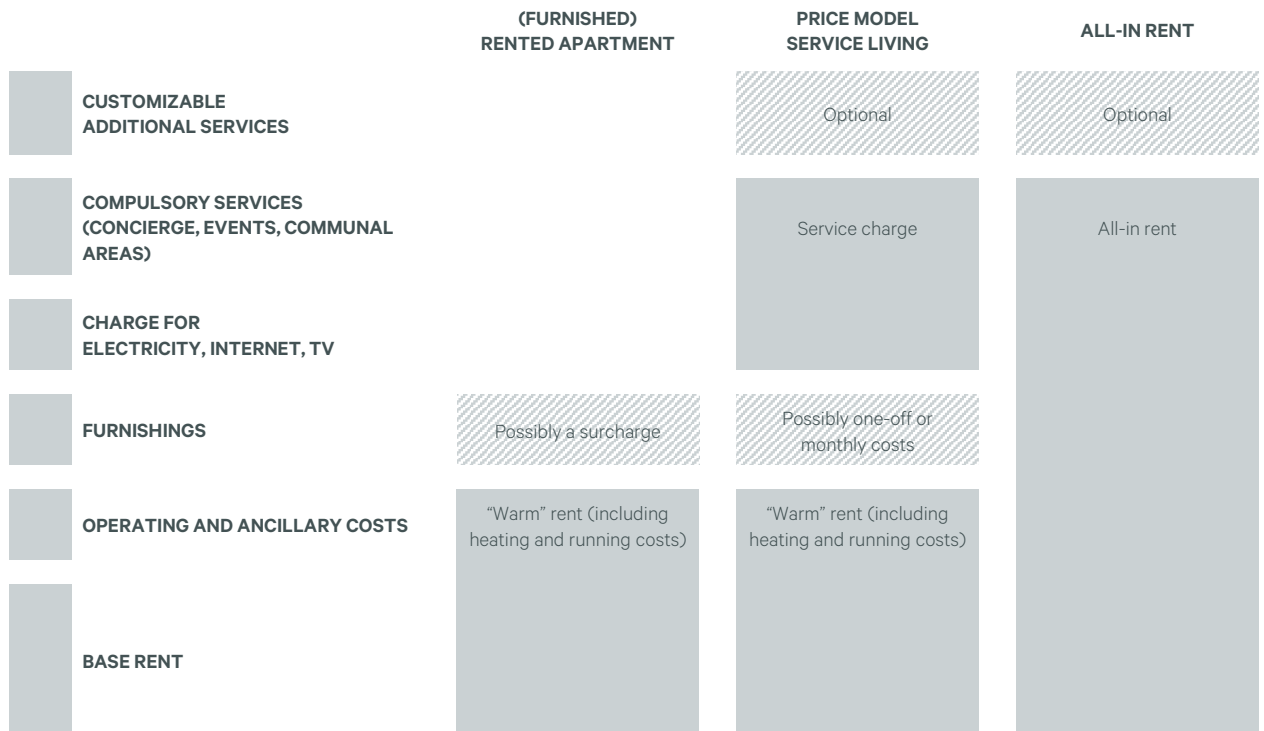
Service charge

A service charge is levied for additional services supplementing the use of the accommodation. An obligatory service charge due monthly is common in Service Living for Senior Citizens. This charge covers the use of communal areas, services provided by the establishment's staff and also partly one or several meals a day. Other concepts include a one-off service charge for taking up residence or when leaving, which covers the costs of any events or final cleaning of the apartment.

All-in rent

To facilitate leasing and billing, a flat-rate all-in rent is customary in Modern Living. This comprises the base rent along with the operating and ancillary costs of other amounts that are usually incurred through the use of the accommodation, such as the cost of electricity, Internet and TV connections and the cost of furnishings. The all-in rent is due as a lump sum on a monthly basis.

FIGURE 7: Rental models for Modern Living (examples)



Source: CBRE Research, 2023.

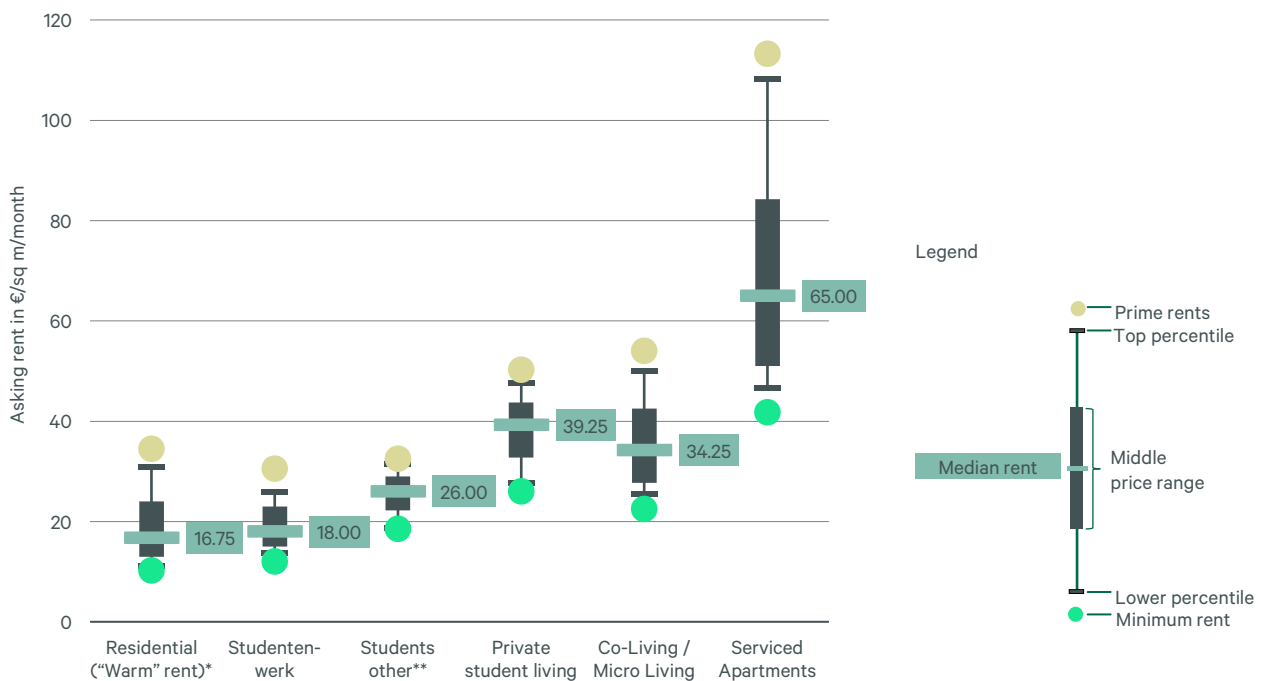
Price Range of the Concepts in Berlin

With its diversity of supply, the market of Berlin provides a very good basis for a cost comparison of the various concepts as well as “warm” rent (“Warmmiete” meaning including heating and running costs) on the free housing market.

The average all-in rent for Studentenwerk apartments is only marginally higher than the average gross rent for smaller apartments on the free housing market. Studentenwerk properties have been partly modernized. Existing stock generally does not include any new buildings, however. Student accommodation provided by ecclesiastical and non-profit operations, student fraternities, associations and state-owned companies is generally more expensive than Studentwerk student housing, also because the buildings offered by state-owned housing companies are younger.

Compared with Studentenwerk apartments, private residential solutions for student accommodation offer higher quality accommodation commanding an average all-in price of almost €40/sq m/month with well-equipped communal areas. Buildings are often new or at least younger than 10 years. The Co-Living and Micro Living price range is comparable with the level of private student accommodation. The average rent at somewhat more than €34/sq m/month is lower compared with private student halls of residence, mainly dictated by larger apartments on average. Communal areas and services are aimed at serving a different target group, but nevertheless range around a similar cost level. Serviced apartments at €65/sq m/month command a significantly higher average rent than all other concepts, while also displaying a wide price range. The range clearly reflects differences in the quality of the apartments and a higher scope of services. The fundamentally higher costs are attributable to greater flexibility for the lease period, thus pricing in potential vacancies.

FIGURE 8: Range of rents for Modern Living in Berlin (all-in rent)



Source: CBRE Research, Value AG, 2023.

*Total rent of rental apartments in sizes of 15-50 sq m in the first half of 2023.

**Ecclesiastical and non-profit operators, student fraternities, associations and state-owned companies.

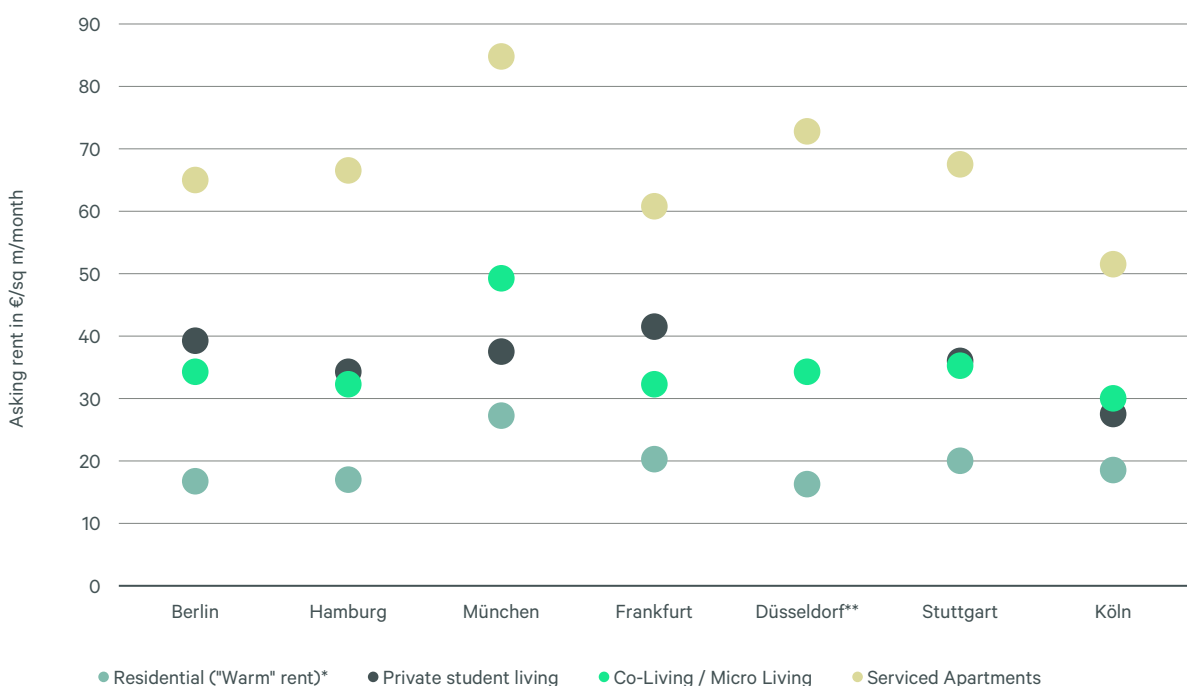
Differences at the Level of the Top 7 Cities

A price comparison of the concepts in the Top 7 cities reveals regional differences, while confirming the price relationships between the various concepts. In this context, sole consideration was given to median prices, factoring out the range of costs.

Privately offered Student Living as well as Co-Living and Micro Living are comparable across all cities. The costs in Student Living are lumped together for smaller apartments on average, with the result that they slightly exceed the price of Co-Living and Micro Living. The findings for the city of Munich run counter to this trend: Here an average rent of around €50/sq m/ month falls due for Co-Living and Micro Living and rent for student housing is almost €38/sq m/month. The different buying power of the target groups plays a significant role in this case. Student Living rents in Munich exhaust students' budgets, leaving virtually no wriggle room. By contrast, other Modern Living concepts fully exploit the higher income potential in Munich, with the effect that the gap compared with Student Living is higher than in other cities. The demand for temporary accommodation is not only generated directly by employees but also by the large corporations based in Munich.

Despite regional differences, the ranking of the concepts basically remains the same. Serviced apartments command significantly higher prices everywhere. Whereas Student Living, along with Co-Living and Micro Living, displays tendencies similar to rental levels on the free housing market, this trend is less pronounced for serviced apartments. Among other reasons, this is attributable to the specific focus of the concepts, for instance when operators are concentrating locally on clients on a budget.

FIGURE 9: Rents for Modern Living in the Top 7



Source: CBRE Research, 2023.

*Total rent of rental apartments in sizes of 15-50 sq m in the first half of 2023.

**Owing to the insufficient supply, the price of student living in Düsseldorf was not ascertainable.

Conclusion and Outlook

The segment of **Modern Living** is an important component of the housing supply in the metropolises and university cities. The concepts are diverse and increasingly complement the supply of traditional housing for the different target groups against the backdrop of society's growing singularization, greater employee mobility, tight housing markets, and ultimately also an ageing population.

The higher returns achievable compared with the rental market and less regulation – for the time being at least – greatly enhance the appeal of Germany's market for Modern Living for many international concepts and investors.

Against the backdrop of regulations on planning, rent and fiscal issues that should not be underestimated, detailed location-related and use-case specific advice, supplemented by evaluations accompanying the expansion, acquisition, as well as concept development and potential analysis are indispensable.

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Modern Living offers an adequate alternative for a range of different target groups to live flexibly with a high standard of living despite strained housing markets.

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