COVID-19 Impact on Real Estate

Weekly PwC Expert Session via WebCast
6th May 2020, 10:00-11:00 am

- Scenarios Real Estate – The way back into business
- Deep Dive – Hotel market and hotel properties
- Outlook – Travel behavior and consequences
- Valuation – Investor behavior
- Contracts - Rental / Lease / Management
- Laws - Meetings, events & Co.
- Tax Update – Value added tax in the hotel industry
- Q&A Session

Questions to the PwC experts via e-mail to: de_covid19_pwc_real_estate@pwc.com
Updates and further information on https://blogs.pwc.de/real-estate/
Scenarios Real Estate
The way back into... "normal" life

Infection rates are falling

Pandemic - under control?

• Cautiously, positive news is making its way and at the same time leading to calls for easing restrictions.

• But the curves in the US, UK and SWE still show the struggle to ease the pandemic.

• Social distancing helps, but no herd immunity, no vaccine, drugs in the testing process.

• The fear of a second wave resonates as the sword of Damocles in opening scenarios.

• The "new normal" begins...
Fiscal policy - CORONA shock successfully mitigated!

- In the first phase of the pandemic, liquidity was provided on an exceptional scale to bridge liquidity shortages through no fault of one’s own.
- In Germany amounting to 17.4% of the GDP - top of the list!
- Economic stimulus packages will follow.
Scenarios Real Estate ... recovery will take time

**After the lockdown it goes only slowly upwards**

Monetary policy - bazooka for the real and financial economy!

- Monetary policy has reacted very quickly and supports the real and financial economy.
- Global central banks have drastically lowered key interest rates, ECB already well into negative territory, QE programs have expanded considerably. Refinancing of companies is secured.

Recovery China - already visible?

- A look at China shows: After the "lockdown" the Chinese domestic market is slowly regaining momentum.
- Estimates on the impact of COVID-19 on growth see significant losses in 2020, catch-up effects are expected in 2021.

Recovery Europe - first estimates today!

- Economic forecasts for the euro zone by the EU Commission - gloomy figures and a sharp rise in unemployment are expected.

Economic growth - when will it return to normal levels?

- **V-Shape**: Deep but temporary recession, 2nd half-year with first catch-up effects
- **U-Shape**: Prolonged recession with structural change, economic restrictions until 2021
- **L-Shape**: Deep, long-lasting recession with structural change, no foreseeable return to pre-crisis levels

Quelle: WeBank (2020)
Scenarios Real Estate: Direct and indirect trends will change the industry

Trends are crisis-induced and crisis-catalyzed

**Macroeconomics and economy**
- Lower growth rates (“90% economy) and even more rising sovereign debt levels
- Fiscal crisis response fostering ultra-low interest rates
- Liquidity in the market as underlying force for future price developments

**Economic sectors and enterprises**
- Reduced supply chain integration and focus on resilience
- Future way of working (“more digital”) and travel (“less”)
- ESG pressure remains and might be kick-started

**Private & Social**
- Back to social life, but more distanced
- (Way of) consumption/fostering online but also less intensive sharing
- Changed perception of travel and renewed relevance of “local” and sustainable practices
Scenarios Real Estate
Deep Dive hotel market

COVID-19 and the hotel industry

- What has happened since early 2020?
- Key figures and direct effects?
- Effects on hotel operations?

European hotel market

- What are the implications in Europe?
- What impact does this have on the individual European metropolises?

Outlook

- Development of the hotel industry in Germany and Europe?
- How are investments in hotel properties influenced by COVID-19?

Markus Hauk
Manager, PwC VMA Germany
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Crash of the hotel industry from mid-March 2020 - only 20% open with a room occupancy rate of 4 to 9% in April

**Data & Facts**

**German hotel market**
- Annual turnover in 2019: 29.0 bn. €
- Transaction volume 2019: 5.0 bn. €
- Rent/lease brand hotels p.a.: 3.5 bn. €

**11 March 2020**
WHO declares COVID-19 a pandemic

**Since 22 March 2020**
Extensive border and hotel closures by decisions of the German government

>80% of German hotels closed

**Until mid-June 2020:**
Worldwide travel warning by the Federal Foreign Office

**Until 31 August 2020:**
Ban on major events

Sources: PwC Research, STR, Auswärtiges Amt

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**RevPAR 03/2019 vs. 03/2020**

<table>
<thead>
<tr>
<th>Country</th>
<th>03/2019</th>
<th>03/2020</th>
</tr>
</thead>
<tbody>
<tr>
<td>Germany</td>
<td>72</td>
<td>29</td>
</tr>
<tr>
<td>Germany 3*</td>
<td>60</td>
<td>25</td>
</tr>
<tr>
<td>Germany 4*</td>
<td>72</td>
<td>28</td>
</tr>
<tr>
<td>Germany 5*</td>
<td>121</td>
<td>48</td>
</tr>
</tbody>
</table>

**Direct impacts**

By February 2020, the RevPAR was only 3.1% below the level of the previous year.

March 2020 there were about **90% fewer bookings** than in the previous year.

RevPAR slumped by 30%.

At the quarterly level (Q1 2020 vs. 2019), the impairment of RevPAR was **-23%**.

In April 2020, **room occupancy in the TOP 7 markets was approx. 6%**, compared with 75% previously.

By the end of April, the **loss in revenues** is estimated to be up to € 10 billion.

*Congress and cultural cities* are particularly affected.

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**Capacity utilisation April 2020**

- Berlin: 7%
- Hamburg: 7%
- Düsseldorf: 4%
- Cologne: 9%
- Frankfurt: 6%
- Stuttgart: 7%
- Munich: 7%

- 13.-19. April 2020 without closed hotels
Serious effects of the COVID-19 crisis also on the European hotel markets

### European hotel market

<table>
<thead>
<tr>
<th>City</th>
<th>January 2020</th>
<th>February 2020</th>
<th>March 2020</th>
</tr>
</thead>
<tbody>
<tr>
<td>Amsterdam</td>
<td>-1%</td>
<td>-6%</td>
<td>-72%</td>
</tr>
<tr>
<td>Berlin</td>
<td>0%</td>
<td>-3%</td>
<td>-67%</td>
</tr>
<tr>
<td>London</td>
<td>1%</td>
<td>-2%</td>
<td>-60%</td>
</tr>
<tr>
<td>Madrid</td>
<td>6%</td>
<td>5%</td>
<td>-76%</td>
</tr>
<tr>
<td>Paris</td>
<td>15%</td>
<td>8%</td>
<td>-69%</td>
</tr>
<tr>
<td>Prague</td>
<td>-2%</td>
<td>-14%</td>
<td>-78%</td>
</tr>
<tr>
<td>Rom</td>
<td>7%</td>
<td>-11%</td>
<td>-86%</td>
</tr>
<tr>
<td>Warsaw</td>
<td>3%</td>
<td>-5%</td>
<td>-69%</td>
</tr>
<tr>
<td>Vienna</td>
<td>14%</td>
<td>0%</td>
<td>-69%</td>
</tr>
<tr>
<td>Zurich</td>
<td>0%</td>
<td>-1%</td>
<td>-72%</td>
</tr>
</tbody>
</table>

Quellen: PwC Research, STR

All European cities have suffered severe declines in RevPAR since February / March 2020.

### Paris without and with COVID-19

<table>
<thead>
<tr>
<th>City</th>
<th>RevPAR</th>
<th>Finance crisis 2009</th>
<th>COVID-19 crisis 2020</th>
</tr>
</thead>
<tbody>
<tr>
<td>Europe</td>
<td>(April) -28,0%</td>
<td>(April) -89,4%</td>
<td></td>
</tr>
<tr>
<td>China</td>
<td>(August) -59,1%</td>
<td>(March) -85,3%</td>
<td></td>
</tr>
</tbody>
</table>

RevPAR (% change on previous year)

Extensive closures Sales losses and short-time working

Measures taken by operators

1. **Closure of the hotels**

2. **Reduction of fixed costs** (wages and salaries, lease/rent, financing and investments for FF&E and capex)

3. **Postponement of FF&E and Capex investments**

4. **Government/insurance support** (payment of salaries, business interruption insurance)
Market recovery will take time - impact depends on economic recovery scenario and operator focus

Mixed recovery in hotel performance

**Best Case – V Shape**
*False Alarm*

Conceivable for holiday hotels with domestic guests

**Base Case – U Shape**
*Measured Recovery*

- The more exhibition and event business,
- the higher the proportion of international guests,
- the more danger einer längeren Recovery.

**Worst Case – L Shape**
*Prolonged Event*
Guest segments are affected differently - business guests return late

<table>
<thead>
<tr>
<th>Type of demand</th>
<th>Factors for forecasting performance</th>
</tr>
</thead>
<tbody>
<tr>
<td>Leisure</td>
<td>• Backlog demand drives demand in summer</td>
</tr>
<tr>
<td></td>
<td>• Domestic tourism as driver</td>
</tr>
<tr>
<td></td>
<td>• Dependence on the course of the pandemic, provided that infection is avoided</td>
</tr>
<tr>
<td>Individual business trips (Corporate Transient)</td>
<td>• When the economy restarts, business travel will resume</td>
</tr>
<tr>
<td></td>
<td>• Personal contact remains important</td>
</tr>
<tr>
<td></td>
<td>• But in part also increased use of digital solutions</td>
</tr>
<tr>
<td>Business Guests Events (Corporate Group)</td>
<td>• Postponed events end 2020 at the earliest</td>
</tr>
<tr>
<td></td>
<td>• 2021 may become a catch-up year</td>
</tr>
<tr>
<td></td>
<td>• Introduction of the vaccine important for this segment</td>
</tr>
</tbody>
</table>

Source: PwC Research
France, Spain & Italy much more affected due to high number of foreign guests

Forecast of international tourist arrivals in Europe (million)

- Spain, UK, Italy and France have the largest number of international guests.

Share of international tourists in total national market in % (2017)

- 2020 for forecast
-290 to -440 million tourists
-20% to -30%

Source: PwC Research, STR, Statista

Source: PwC Research, Eurostat 2017
German hotel market at an advantage - high proportion of domestic guests likely to lead to faster recovery

- There are indications that the German hotel market will have a shorter recovery phase compared to the rest of Europe.
- Germany has a pronounced demand for holidays and a significant proportion of domestic business travelers.
- During the SARS crisis in 2003, the German hotel market recovered faster than in other countries. The recovery period was 3-6 months, while the European average was 9-12 months.
Behavior Change
“Less Travel” as a trend?

Travel behavior

• An average recovery period of 10 months is assumed (WTTC).

• Possible trend: "Revenge Travel" - as soon as you get the opportunity to travel, it will be used.

• Survey STR: Twice as many people are not planning to travel internationally in the next two years (early March versus late March 2020).

• Possible reduction of personal meetings in the business sector.
Changed travel behavior and additional new hotel offers intensify the market development

What do we see in China?

- Most **hotels** in China **reopen after about two months**. In the first phase, the number of **domestic leisure guests, business travelers** in industrial park zones and quarantined guests **near airports** rose in particular.

- The rest of the world is about **two months behind China**.

Hotel occupancy rate in %

Hotel room offer

- In Germany, **additional rooms** will come onto the market **within the next 2 years**.

- In **Frankfurt** there are **over 5,500 rooms** in the **pipeline**, in **Berlin** there are **more than 3,450 rooms** and in **Munich** more than **3,900 rooms**.

- The **majority** of these **hotels** are in the **3-4 star segment** and are causing **further pressure on occupancy rates** in the hotel industry.

<table>
<thead>
<tr>
<th>New hotel rooms</th>
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<th>New hotel rooms</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Frankfurt</strong></td>
<td><strong>München</strong></td>
<td><strong>Berlin</strong></td>
</tr>
<tr>
<td>2020</td>
<td>&gt; 4.300</td>
<td>2020</td>
</tr>
<tr>
<td>2021</td>
<td>&gt; 1.200</td>
<td>2021</td>
</tr>
<tr>
<td>2020</td>
<td>&gt; 2.000</td>
<td>2021</td>
</tr>
<tr>
<td>2021</td>
<td>&gt; 1.900</td>
<td></td>
</tr>
</tbody>
</table>

Sources: PwC Research, STR, Bulwiengesa
Key cost item: Lease

- Landlords and financing partners bear approximately €300 million rental risk per month in Germany (20-30% of turnover).
- Extension of the lease agreements as a negotiation option.
- 70,000 hotels and restaurants before insolvency.
- 250,000 employees in short-time work or threatened with dismissal.
- 10 billion € loss of sales by the end of April 2020 in Germany.
- Every third business reports that its liquidity is sufficient for less than 20 days.
- Owner/operator structures under greater pressure.
Market participants' expectations subdued

Investment behavior and price changes

Expected change in purchase prices

- 8% increase
- 77% equal
- 15% lower
- Incalculable

Expected changes in hotel rents

- 13% increase
- 75% equal
- 12% lower
- Incalculable

Source: PwC Research, Colliers, Savills
Market values and investments - negative temporary catch-up effects expected

**Expected market attractiveness after Covid-19**

- 16% stable
- 16% falls
- 68% falls heavily

**Hotel Investment market**

- Q1/2020 - Hotel investment market still relatively stable.
- Negative catch-up effects are expected from Q2/2020 onwards.
- Uncertainties in the rental and investment market:
  - Duration of sales shortfalls
  - Duration of the loss of rent
  - Availability of debt capital and general liquidity
- Temporary effects due to a reduction in demand possible:
  - Increase of the risk return
  - Reduction in the turnover of space
  - Reduction of the transaction volume

**Opinion Investors with AuM > € 500 million €**

- 77% “Purchase prices will fall”
- 75% “Hotel rents will fall”
- 84% “Market attractiveness falls”
Obligation to protect guests and staff

Public law requirements

- Accommodation offers for private holiday purposes still prohibited in all federal states
  - Partially allows business travelers and guests for non-private tourist purposes (depending on federal state);
  - In case of violation fine, sometimes even criminal prosecution (depending on the federal state);
  - Legal basis: Country-specific COVID-19 decrees ("patchwork carpet").
- No special hygiene and/or distance regulations for hotels in country dispositions

Operator responsibility

- Duty of conduct under tort law to prevent and avert danger;
- Duty to protect guests and personnel in the hands of operators/leaseholders;
- Violation can lead to compensation claim;
- No uniform standards: DTV plans orientation guide Protection and hygiene concepts for hotels and restaurants
- Planning and design of the hotel equipment (security lock, fever scanner, UV light column in the lobby area, cleaning of the rooms according to clinic standards, etc.)
Measures and aids

Complex contract structures / many parties involved

- In case of delay in lease payments for the months April to June 2020 no termination by lessor possible;
- Regulation does not apply to management and other contracts: More complex contractual situation than e.g. with office tenants, loss of operator contract can make operation impossible;
- Operating obligation in lease agreements continues to apply;
- Recommendation: Agreement with owners and operators, e.g.:
  - Suspension or limitation of the obligation to operate;
  - Sharing the economic risk with owners, for example by agreeing sales-based rents or deferrals;
  - early renewal of leases as a concession;
  - agreeing to more extensive waivers of termination in lease agreements;
  - waiver of termination of operating agreements in order to ensure operation.
- Adjustment of operations, e.g. use of hotel room as home office space.

State aid

- Decisions Coalition Committee
  - Reduction of value added tax for meals to 7 % from 7 July 2020;
  - Flat-rate reduction in advance tax payments for SMEs already made for 2019;
  - Temporary increase in short-time working allowance.
- KfW Special Programme to bridge Financial Shortages.
Meetings, events & Co.
Different degrees of affectedness

Laws & Regulations

- Bans on major events
  - Berlin: > 1.000 p. until 31.08.2020, > 5.000 p. until 24.10.2020
  - No standard rules for Germany
- Closure arrangements for gastronomy and the hotel industry
  - Relaxation initiatives especially in MV, HH, Berlin, SH ...
  - Procedure inconsistent - wait for effects
- Mitigating Act in Event Contract Law
  - Law expected this week (07.05. 2.+3. reading)
  - leisure events and facilities - not: professional events such as congresses etc.
  - Voucher - redemption or refund as per 31.12.2021=> claim for payment remains
  - Reference date: Sale by 8 March 2020
- Cultural aid from Federal States
- UPDATE Trade: 800 sqm limit falls
Tax changes in the hotel industry

Business Model & Tax Issues

- Tax practice for COVID-19 measures
- Change in value added tax on catering services (7%)

Sven Behrends
Partner, PwC Real Assets, Germany
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The tax authorities are satisfied with plausible information from the taxpayer that the Corona crisis has **serious negative effects** on his economic situation.

*BMF, FAQ „Corona“ (taxes), 30th April 2020, p. 2.*

**Practice:**
The critical situation of the industry is almost automatically recognised. This applies not only to operating companies, but also to investors.

### Impact on operators

- **Deferral**
- Refund of the special VAT prepayment and adjustment of current VAT payments
- Reduction of advance payments
Tax changes for catering services

Reduced VAT rate for catering services (7%) from 1 July 2020 - 30 June 2021

"Mövenpick Law"

- Overnight stay (19%)
- Additional benefits (19%)

1st January 2010

Judgment of the European Court of Justice (ECJ) of 18th January 2018 (Case C-463/16 - Amsterdam Stadium) (different sentences not justified)

- Overnight stay (7%)
- Additional benefits (19%, even if only part of the standard benefit)

Finance Court Berlin-Brandenburg, judgment of 28th November 2018 - 7 K 7314/16 - various sentences justified

7% also for gastronomy (without drinks)

1st July 2020

30th June 2021
Your questions to the PwC experts

Scenarios

Impact on hotels

Impact on the valuation of hotels

Legal Update

Tax Update

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PwC information on COVID-19 and its impact on the real estate industry can be found here:

Current information about Real Estate and also COVID-19
https://blogs.pwc.de/real-estate/

Central email address for questions to PwC experts on de_covid19_pwc_real_estate@pwc.com

PwC Plus - All the information about real assets with push message function
https://pwcplus.de/

Weekly expert session via WebCast on current topics always Wednesday 10:00 to 11:00
PwC COVID-19 Services

Operations
• Management of the tenant and service portfolio
• Support in daily business
• Crisis Management

Liquidity/Financing
• Monitoring the liquidity status
• Review of the loan portfolio
• Support review grants and loan options
• Dealing with tax deferrals

Scenario Analysis
• Development of scenarios for dealing with the COVID-19 crisis
• Changes in the business model to ensure sustainable cash flows

Strategic Impact
• Expansion of IT systems & digitization
• Further development of the value chain, business model & assets
• ESG implementation

PwC COVID-19 Real Estate Taskforce
• Experienced, interdisciplinary team (Legal, Tax, Operations, Financials)
• Pragmatic and efficient project approach
• Possibility of short-term support and ‘Ready-to-Go’ support with a proven IT communication platform

COVID-19 Expert Contact:
de_covid19_pwc_real_estate@pwc.com
COVID-19 Impact on Real Estate

Weekly PwC Expert Session via WebCast

13th May 2020 from 10:00-11:00 am

Registration via Link or via E-Mail: