Real Estate BEYOND COVID-19

Weekly PwC Expert Session via WebCast
10. Juni 2020, 10:00-11:00

Real Estate Market DACH & Italy
Economic stimulus package - Special

- Real Estate scenarios - today:
- Austria
- Switzerland
- Italy
- Tax implications
- Legal and other implications

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/
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Real Estate
BEYOND COVID-19

Repair. Rethink. Reconfigure.

- It is time to think about the future!
- **Repair** – Crisis-induced losses will have to be dealt with and will also leave their mark in the second half of the year. The underlying conditions are clear: the real economy will only slowly regain a foothold. The real estate sector will suffer in part.
- **Rethink** – Individual asset classes will have to redefine their resilience. Some business models will have to be adapted. The stability of portfolios will have to be reviewed, not only because of the pandemic, but also because of new ESG requirements. Investment and country allocations will have to be reconsidered.
- **Reconfigure** – Structures, platforms, organizations, processes, technology and systems as well as data management and digitization will change. A good reason to look ahead.

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The economic stimulus package - what is the outcome for real estate?

Economic injection & future package

• **Reduction of the value added tax:** From 1 July to 31 December 2020, the VAT rate will be reduced from 19% to 16% and for the reduced rate from 7% to 5%.

• **Child bonus for families:** Parents receive a one-off payment of 300 euros per child. For single parents the allowances are doubled.

• **Strengthening of local authorities:** The federal government is increasing its share of the cost of housing for the needy, is offsetting half of the municipalities' trade tax losses and is strengthening local public transport and the health sector.

• **Relief in electricity costs:** The EEG levy is to be reduced from 2021 through subsidies from the federal budget.

• **Future package:** Around 50 billion euros are flowing into future areas such as the hydrogen economy, quantum technologies and artificial intelligence.
Real estate industry profits!

Thoughts. Expectations. Reality.

- Boosting private consumption - city centres and retail properties can benefit
- Bridging assistance - retail, hospitality, real estate owners
- 25 billion for small and medium-sized companies in the form of operating grants (including fixed operating costs, rent payments)
- Construction industry benefits from the Municipal Solidarity Pact 2020, as the willingness of the public sector to invest is strengthened
- CO2 building refurbishment programme with an additional €1 billion for 2020 and 2021
- Expansion of federal funding programmes for the energy-efficient renovation of municipal buildings
- Promotion of climate adaptation measures in social institutions
- Investment plan for sports facilities, extensions, conversions and new buildings of day-care centres
- Relief for the housing costs of Hartz IV recipients
- Service charge settlements benefit from the agreed cost cap for the EEG levy
Swiss speciality - Legal remission of rents

Restriction of contractual security

Business tenants owe 40% of the rent during the lock-down. Landlord pays the remaining 60%. Rent ceiling is CHF 20k p.m.

If the rent is between CHF 15k and CHF 20k, tenant and landlord can do without this solution.

Any rental agreements already made between tenants and landlords remain valid.

Federal Council provides for a hardship fund of CHF 20 million for landlords.

www.pwc.ch/immospektive


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Economy remains uncertain

Current state of the Swiss economy

- Since the beginning approx. 31,000 cases of infection and 1,660 deaths (as of 09.06.) - now only <10 new infections per day
- Extensive relaxation measures - 06.06. Meetings up to 300 participants - 15.06. Opening of borders to all EU & EFTA countries
- Demand and supply shock will probably trigger a recession
- Q1 GDP forecast for 2020 at 1.4% already below the current potential growth
- Q2 GDP forecast for 2020: -3.4%; economic catch-up effect expected in 2021
- Short-time work prevents a rapid rise in unemployment. A downstream increase in unemployment is to be expected. This consequence will continue into 2021.
Weak transaction volume for commercial real estate

Current developments on the transaction market

- Transaction volume reduced since 2016

- The slow start in Q1-2020 was extended by COVID-19 until April 2020. In May, transaction volumes increased again.

- Many investors still reluctant to invest. They wait and see and observe the current developments.

- In 2020, approximately 60% was invested in sales properties and approximately 20% in office properties.

- In terms of volume, almost 90% was invested in Zurich in 2020.
Declining demand for office space - not only COVID-19 impact!

Developments on the office market

• Even before Covid-19, office rents in Q1-2020 were declining 1.2% on the previous quarter

• All in all, Covid-19 led to a halt in the expansion of space. Instead, companies increasingly invested in IT and home office systems

• Home office solutions are establishing themselves, shorter & more flexible rental contracts are in demand

• Yields in top urban locations have fallen in Q1-2020 (before Covid-19). Currently more stable to slightly rising yields expected. In back-office locations, yields are expected to rise more markedly in the short term, not only by Covid-19.

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Retail and hotels most affected - but also positive effects from local focus!

Retail space - High Street remains stable

- Existing structural difficulties **further exacerbated** by Covid-19, but no shopping tourism and rising sales in May due to catch-up effect
- **Net yields for sales properties remained stable** in Q1 (before Covid-19) in **urban locations**. **After** Covid-19 we expect a **noticeable increase**.

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Hotel industry - anticipation of a lively summer

- **Occupancy** has fallen by 70% since March.
- ADR fell from CHF 250 before Covid-19 to CHF 150 in April
- **Stronger holiday** hotel industry - **businesses report high booking rates for summer 2020**.
- A gradual recovery to 2019 levels is expected for the city hotel industry by **the end of 2022**.
COVID-19 in Austria
Current situation

Perspectives – COVID-19 in Austria

- The COVID 19 pandemic has also completely reached Austria since mid-March 2020
- The Austrian Federal Republic reacted quickly and decisively - socially and economically, measures were taken and adapted according to the situation
- Abolition of exit restrictions as of 1 May, with a minimum distance of one metre within public areas still in force or the use of a mouth/nose guard
- Reopening of retail and service businesses since 2 May - Gastronomy since 15 May - Hotels since 29 May - General construction activities since 26 March
- Since Thursday 4 June, all checks on neighbouring countries on entry into Austria - with the exception of Italy - have been lifted

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COVID-19 Impact in Austria with significant economic consequences

COVID-19 – Economic Impact

- By the end of April alone, a total state Corona aid package of around EUR 40 bn in support of the economy (around 9.5% of GDP) was promised
- Projected increase in government debt from 70% to about 75% of GDP
- The OeNB expects real GDP to decline by 7.2% in 2020 and to catch up in 2021 and 2022 with growth of 4.9% and 2.7%, respectively
- HICP inflation will fall to 0.8% in 2020, remain at that level in 2021 and accelerate to 1.5% only in 2022
- The unemployment rate according to the Eurostat definition will rise to 6.8% in 2020; in 2022 it will drop to 5.3%
- A new short-time working model is designed to keep as many employees as possible in employment - core system of 80-90% of net income comes from AMS

GDP LOSS DUE TO THE CORONA CRISIS IN AUSTRIA (VS. PREVIOUS YEAR, 2020)
EUR -35,7 bn.

CHANGE IN THE NUMBER OF UNEMPLOYED IN AUSTRIA (COMPARED TO THE PREVIOUS YEAR’S MONTH, MAY 2020)
69,7%

CONSUMPTION RESTRAINT DUE TO THE CORONA CRISIS IN AUSTRIA (YTD MAY 2020)
28%
Retail and logistics market

Covid-19 hits retail market hard (short & long term)

- Complete closure of the stationary trade including gastronomy from 16 March with the exception of the food trade, pharmacies and petrol stations
- Daily sales loss of approx. 46% or EUR 117 million - up to EUR 700 million per week
- Rent losses of around EUR 200 million p.m. from the shutdown
- Protection against dismissal through pandemic law
- Re-opening gradually from 14 April (shops up to 400m²), from 02 May (shops over 400m²), gastronomy from 15 May with restrictions
- Insolvency applications are to be expected, especially for small tenants and catering and entertainment businesses
- Concerns that the Covid-19 crisis will accelerate the pressure on stationary trade
- Prime Yields 3.30% ↑ (limited database due to deferred transactions)

Logistics market: demand remains strong

- Demand still driven by booming online trade
- Rental processes for logistics space are only marginally influenced by Covid-19
- Decline in industrial production could slow down growth
- Logistics sector is resilient and will recover faster than other commercial asset classes

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10 June 2020
Austrian hotel market sustainably affected

Opening of the accommodation facilities since 29 May

- Complete closure of all hotels over the period from 03 April to 29 May,
- Hotels, hostels and serviced apartments recorded drastic declines in bookings and sales
- Vienna March 2020: RevPAR -69% (year-on-year change), driven by occupancy rate, price level stable
- Record year 2019 with EUR 1.26 billion transaction volume in the hotel segment (approx. 80% in Vienna)
- Record increase in the number of unemployed in this segment
- Collapse in demand expected in the short to medium term
- Loss of overnight stays between 24% - 31% for 2020
- Recovery through domestic and German tourism (2019: around 50%)
- Long-term trend reversal possible for work-related travel

RevPAR

WIEN -69%

ROM -86%

LOSSES OF OVERNIGHT STAYS 2020

24% - 31%

TOURISMUS FROM DE ~50%
Office market only affected in the long term - also applies to Austria

Moderate impact on office investments

- **Current leases** will be **continued**
- **Demand for space lower** since mid-March due to uncertain economic prospects
- Based on the moderate level of rents, **no significant falls in market rents are expected**
- The current spread of **home office is a strong impulse to work from home**
- **Flexible office use concepts** such as **desk sharing** increasingly attractive
Residential market not affected

The residential sector - the most resistant

- Residential market is more crisis-resistant than commercial property markets
- High number of housing market completions in 2020
- Concerns about future rent payments due to continuing problems in the labour market
- Delay due to current curfew - Rules for handing over, renting and selling apartments
Italy - first affected!

**Current situation of Covid-19 in Italy**

- Italian GDP is forecasted to drop by -9.5%, compared to a drop of -6.5% in Germany and -7.7% overall in the Euro Area (19 member states).

- **Extended coverage** and **relaxed eligibility** criteria for wage supplementation schemes (Cassa integrazione guadagni) should **support labor incomes** and reduce the risk of dismissals and unemployment.

- **Lockdown measures decreased private consumption**, but consumer spending is forecast to **bounce back** in the second **half of 2020** – due to income support measures and low inflation.

- **Decree of 16 May** started **easing lockdown** measures for economical stimulation. Re-opening of offices, factories, construction sites, restaurants and bars, high street retail shops, shopping centers, entertainment, parks, etc.

- However, there are **additional costs necessary** to **clean and adapt commercial spaces** (owners and tenants) which could increase prices for consumers: **direct costs** (cleaning) and **indirect** (loss of usable space in offices, restaurants).

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Limited impact of Covid-19 can be observed within the Italian RE Market so far

Current situation on transactions

- First quarter of 2020 was +7% higher than the same period of 2019 – not yet really impacted by Covid-19

- Investment market in 1Q 2020 was driven by retail, and office sectors:
  - Retail: Supermarkets (deal Esselunga and Unicredit – €435 mln), and high street retail
  - Office: 70% Milan city center (core and value add)

- In 2Q 2020 investors mainly adopted “wait and see” approach with multiple deals put on hold.

- Some operations closed which were already in advanced negotiations (Vittoria Assicurazioni and York Capital for over €500 mn. - office asset class; InvestiRE and Reale Immobili for over €200 mn. - residential).
Smart working is currently the norm in the beyond Covid-19 situation right now

### Market observations

#### Office

- Impact of the measures **aimed at containing** Covid-19 has caused a **progressive postponement** of the transactions in progress.
- **Rents** are expected to **remain stable** in the short term.
- **Slow opening of offices** due to the need to make safety updates and that not all employees can re-enter at the same time. **Smart working continues** to be the norm for companies that have the technological capabilities.
- **Potential Threat:** So far no objective data to confirm the impact of smart working on office space demand in the short term, but demand shifts could be expected as companies become comfortable working remotely.

#### Hotel

- **After a record 2019**, with € 3.3 billion investments, and a very **promising start to the year**, the tourism sector has had a significant impact, first with the **postponement** and **cancellation** of numerous events, then with travel bans and movements.
- In March 2020, **loss** in terms of RevPAR of around **93%**, **compared** to the previous year from a freefall in occupancy as ADR, however, remained stable.
- As **lockdown measures ease**, **domestic tourism** (car based) is expected to **grow faster**, while **international demand** will have a **slower recovery**, certainly dictated by the evolution of the emergency situation in the rest of the world.
Rise in e-commerce affecting brick and mortar – no impacts on logistic so far!

Market observations

Retail

- Certainly among the sectors most affected by the lockdown with the exception of supermarkets, pharmacies and shops selling essential products. Non-essential retail stores were closed (e.g. clothing).
- Renegotiation of rents and the probability that variable rent payments will be eliminated for retail due to lockdown measures.

Industrial/logistics

- Currently, no change has yet been highlighted regarding the demand for logistics spaces, which is confirmed as strong and is supplemented by the demand for structures by the pharmaceutical sectors and large-scale retail trade (supermarkets).

E-commerce retail and industrial/logistics relationship

- Current situation has given a strong push to the use of online shopping, strongly linked to primary needs, increasing the structural penetration of e-commerce. Retailers will increasingly have to integrate their online and offline platforms into an omni-channel in order to respond to consumer needs once the emergency phase is over.
- This will be an important accelerator for the processes of spreading e-commerce in the medium-long term, leading to a change in consumption habits, in particular in sectors currently minorly involved in e-commerce, such as food, which had already shown significant growth in online sales during the first days of the crisis.
Residential transaction volume possibly decrease by 25%

**Observations for Residential & Nursing homes**

- For *residential use*, market conditions are expected to **deteriorate** in the **short term** and could be sharper than during the 2012 crisis; **residential transactions** could possibly **decrease** by 20-25% compared to last year.

- Over a **longer time horizon**, cyclical conditions will depend on the impact of the pandemic on **household incomes**.

- **Elderly population is growing** due to the age composition and the improvement of living standards that lead to a higher life expectancy.

- **Elderly market** is **resilient** and predictable, even during financial crisis periods.

- **Demand** for this asset class expected to **remain strong** even during the crisis.
Temporary reduction of VAT rates from 1 July to 31 December 2020

Overview of the measures from a tax perspective

- General rate of value added tax falls from 19% to 16%
- Reduced changes in value-added tax from 7% to 5%
- BMF letter in preparation for transitional and implementing measures - draft expected shortly
- Many open questions
- Very ambitious timetable
Changes affect many operational details - attention effort!

Effects

- Change of ERP systems and invoice templates to account for new VAT rates (twice!)
- Ensure the correct application of the VAT rate:
  - The time of performance is decisive (rent payment = monthly partial performance)
  - Service charge settlements (partial service 16% or 19% depending on the month?)
  - Construction services = partial services or not?
- Check contracts and price lists
- Incorrect value added tax in invoices, contracts, permanent rental invoices: VAT obligation for the exhibitor, no deduction for the recipient!
- Possible cost savings with non-deductible value added tax (e.g. housing, partially exempt tenants)
Economic stimulus package - Legal innovations in “Marshall Plan 2.0”

Rethink.Reconfigure. – legal implications

- Pre-insolvency restructuring proceedings
  - Implementation EU Directive 2019/1023 required anyway
  - Distinction from the protective shielding method
  - Moratorium - Creditor protection as a challenge

- Public procurement law - use of scope for design
  - Shortening of award deadlines - leeway questionable
  - Adaptation of "threshold values" for flexible procedures - especially in the area of VOB/A - Take up CoPa 2009 II?

- "Covert" legal issues
  - Charging point infrastructure:
    - Publicly accessible charging infrastructure - need for coordination for operators; antitrust, public procurement and road law
    - Uniform payment system
  - Allocation of financial income from wind power

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Economic stimulus package - from "Bazooka" to “Marshall Plan 2.0”

Thoughts.Expectations.Reality.

• Operating grants €25 billion for SMEs
  – Operating grants: including fixed BK, rent payments
  – valid for 06-08/2020
  – Corona-related decline in sales compared to the same months of the previous year (04-05/2020 by 60%; 06-08/2020 by 50%)
  – Refund depending on decline in sales - max. T€ 150 for 3 months, T€ 9 for ≤ 5 employees, T€ 15 for ≤ 10 employees
  – Examination/confirmation by StB/WP
  – ATTENTION: Application by the end of 08/2020
• Further measures:
  – Support measures, etc.
    • Kindergarten and day-care centre construction; municipal infrastructure
    • € 500 million in GRW funding
    • Increase of CO2 building refurbishment programme
  – Increase does not solve bottlenecks of the administration (positions)
Your questions to the PwC experts

Scenarios Real Estate

RE Market Switzerland

RE Market Austria

RE market Italy

Recovery package - fiscal dimension

Recovery package - legal dimension

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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/](https://blogs.pwc.de/real-estate/)

- Central email address for questions to PwC experts on [de_covid19_pwc_real_estate@pwc.com](mailto:de_covid19_pwc_real_estate@pwc.com)

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

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**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

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Weekly PwC Expert Session
via WebCast

17th June 2020 from 10:00-11:00 am

Registration via Link or via E-Mail: