Paradigm shift in Germany:
The future for open ended, closed ended funds and REITs

Bernhard Funk

ERES Industry Seminar

Frankfurt on March 23, 2012
Foreword: Phrases for the year 2012

“The closed open-ended fund.”

“Discount on NAV for open-ended fund shares.”

“Diversified closed-ended funds for institutional investors.”

“The abolition of the German REIT.”
Hypothesis: Paradigm Shift

The German market for indirect real estate vehicles:

1st: “There is a profound shake-up in the market, changing the rules of the game.“

2nd: “Reorganization for funds and sponsors is imminent.“

3rd: “We failed to introduce a regulatory framework that offers viable alternatives to existing regimes in the indirect market.“
Is this the first paradigm shift in the German fund industry?

NO!

Previous industry reorganizations occurred, just naming one …

Abolishment of tax incentives for German real estate by the end of the 90s …

TRIGGERING

Meltdown of fund structures designed to help High Net Worth Individuals receiving benefits from accelerated depreciation for properties in East Germany.
Where do we stand, and where do we go?

2012 market environment for German …

A) Open-ended funds

B) REITs

C) Closed-ended funds

D) “Specialfunds“ for institutional clients
Unlike one would think, there is considerable inflow into German open-ended funds …

Figures show that German open-ended funds maintain to attract capital from private clients, but why?

- Interest rates
- Euro crisis
- Diversification benefits

And perhaps …

“Selective retention”

Source: BVI, January 2012

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Considerate share of open-ended funds “froze” capital of investors …

Customers considered open-ended funds to provide immediate liquidity by providing daily redemption rights … but now …

Almost 30% of the market is “locked“ …

“The promise of providing liquidity by investing into illiquid real estate assets has been broken …“

Note: Shares calculated by fund size (AuM)
Examples for funds hoping to reopen in 2012 …

<table>
<thead>
<tr>
<th>&quot;Frozen&quot; are...</th>
<th>Assets in million Euro</th>
<th>&quot;Last call&quot; for re-opening or closing until...</th>
</tr>
</thead>
<tbody>
<tr>
<td>SEB ImmolInvest</td>
<td>6,336</td>
<td>May 5, 2012</td>
</tr>
<tr>
<td>CS EUROREAL A</td>
<td>6,000</td>
<td>May 18, 2012</td>
</tr>
<tr>
<td>KanAm SPEZIAL grundinvest Fonds</td>
<td>359</td>
<td>May 2, 2012</td>
</tr>
<tr>
<td>AXA Immosolutions</td>
<td>353</td>
<td>May 25, 2012</td>
</tr>
<tr>
<td>UBS (D) 3 Sector Real Estate Europe</td>
<td>345</td>
<td>October 6, 2012</td>
</tr>
<tr>
<td>SEB Global Property Fund</td>
<td>293</td>
<td>March 7, 2012</td>
</tr>
<tr>
<td>DEGI GERMAN BUSINESS</td>
<td>238</td>
<td>November 29, 2012</td>
</tr>
</tbody>
</table>

**Total** 13,925

Source: BVI, January 2012
Examples for funds that eventually will sell their assets and quit the market …

<table>
<thead>
<tr>
<th>Dissolved will be…</th>
<th>Assets in million Euro</th>
<th>Closing until…</th>
</tr>
</thead>
<tbody>
<tr>
<td>KanAm grundinvest Fonds</td>
<td>3,925</td>
<td>December 31, 2016</td>
</tr>
<tr>
<td>AXA IMMOSELECT</td>
<td>2,463</td>
<td>October 20, 2014</td>
</tr>
<tr>
<td>DEGI INTERNATIONAL</td>
<td>1,562</td>
<td>October 15, 2014</td>
</tr>
<tr>
<td>DEGI EUROPA</td>
<td>845</td>
<td>September 30, 2013</td>
</tr>
<tr>
<td>TMW Immobilien Weltfonds P</td>
<td>673</td>
<td>May 31, 2014</td>
</tr>
<tr>
<td>DEGI GLOBAL BUSINESS</td>
<td>234</td>
<td>June 30, 2014</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>9,702</strong></td>
<td></td>
</tr>
</tbody>
</table>

Will the selling spree impact the investment markets for German commercial properties in the coming years?

Source: BVI, January 2012

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Markets can provide liquidity, and stock exchanges are the institutionalized format to organize this …

There is a secondary market for fund shares „locked“ by closed open-ended funds …

Shares trade at discounts on NAV.

The discounts for “frozen“ open-ended funds range from 25% through 50% .
The current market sentiment: Open-ended funds supported by a strong retail banking distribution network will survive

But what happens if further closures in 2012 hamper the image of the product ....

... and cause retail customers of banks to redeem their shares in open-ended funds even further?

„Is there WISDOM OF CROWDS amongst the retail investors?“
Why does Germany lack a significant market for REITs?

A significant listed sector would solve the liquidity issues.

In Switzerland and in the US, the listed sector works well.

Why not in Germany? The “TRIANGLE OF PREVENTION“:

- German politicians do not support the evolvement of a viable REIT regime in Germany. The regulatory framework is unsatisfactory.
- Typical German retail clients avoid the volatility of public markets.
- Institutional investors such as German insurance companies would prefer a PRIVATE REIT - not allowed by the German regulatory framework.

“CASE CLOSED … BUT HOPING FOR CHANGE“:

Germany would clearly benefit from a significant listed sector, but the regulatory framework is not supportive for the listed sector!
Market for closed-ended funds contracted in the last decade

Todays market accounts for less than 50% from what the sector had close to millennium.

Why?

Abolishment of tax incentives

Some sponsors with poor performance

Banks hesitant to take-on legal risk in distribution chains

Source: VGF 2012
German laws and directives governing funds are manifold

AIFM directive and associated German laws and directives:

- InvG
- KWG
- WpHG
- WpÜG
- InvStG
- WpPG
- VerkProspG
- UBGG
- WKBG
- AnlIV

Indirect vehicles face more regulation

AIFM directive implementation will benefit the big players …

AIFM and associated regulation will lead to complete reorganization of closed-ended funds:

Stricter regulation and re-design of organizational process …

Risk- and Liquidity Management

Depository

Prospectus and Marketing

Top 10 Sponsors for closed-ended funds – Sorted by equity million EUR

Source: VGF, 2012
German Specialfund is filling the gap of non-existent Private REITs vehicle …

Market Share of German Specialfunds – Top 5

<table>
<thead>
<tr>
<th>Company</th>
<th>AuM (million EUR)</th>
<th>Market Share (per cent)</th>
</tr>
</thead>
<tbody>
<tr>
<td>IVG Institutional Funds</td>
<td>7,281.9</td>
<td>23.41</td>
</tr>
<tr>
<td>Internationales Immobilien-Institut (iii-investment)</td>
<td>3,160.2</td>
<td>10.16</td>
</tr>
<tr>
<td>RREEF Spezial Invest</td>
<td>1,762.6</td>
<td>5.67</td>
</tr>
<tr>
<td>Warburg-Henderson KAG für Immobilien</td>
<td>1,734.3</td>
<td>5.58</td>
</tr>
<tr>
<td>Hansainvest Hanseatische Investment</td>
<td>1,700.7</td>
<td>5.47</td>
</tr>
</tbody>
</table>

Specialfunds is a sector with organic growth. But competition will increase fiercely as …

Former open-ended fund sponsors

Closed-ended fund sponsors

enter the market for German Specialfunds.

Total market volume ~ EUR 30bn +


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REITs will not substitute other indirect vehicles, unless the regulatory framework and the retail clients’ sentiment towards the listed sector improve.

Retail clients’ demand for a well-diversified risk-averse real estate investment is strong.

The classical segmentation between the markets for open-ended funds and closed-ended funds is historical. “Just imagine AIFM required diversified portfolios for closed-ended funds!”

Fund organizations will look very similar in the future due to stronger regulation.

If the market for open-ended and closed-ended funds contracts, who will fill the gap?
Your contact

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