PRIME CAPITAL

European Real Estate Debt

Newsletter Q3 2022

Summary

> With EUR 157bn, H1 2022 was the strongest ever for European real estate investments. This was driven in particular by a very strong first quarter. In Q2 2022, transaction volume declined to EUR 71bn (YoY: -9%).

> Risk-return profile for Whole Loans and Mezzanine has improved in the last quarter with on average more conservative LTVs and higher returns.

> Due to shifting economic fundamentals and rising interest rates, banks are reluctant with new business which creates more bankable financing options for alternative lenders.

> As uncertainty and volatility increase, it is of paramount importance to work with established specialized players who can demonstrate long-standing and local expertise.

Real Estate Market Europe

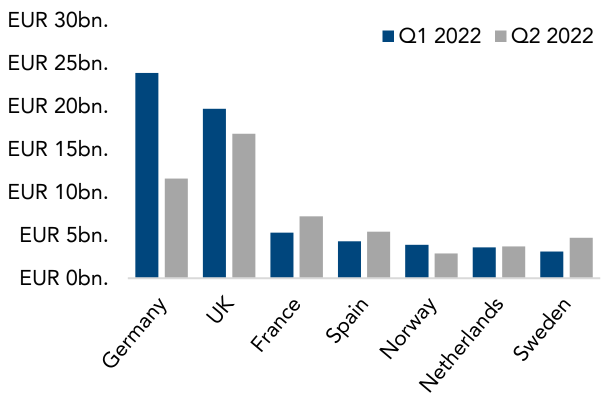

Figure 1: Transaction Volume by Quarter (Western Europe).

European real estate transaction volumes reached EUR 71 bn in Q2 2022, making it the strongest first half ever at EUR 157 bn, mainly due to strong transaction volumes in Q1 2022[1]. On a rolling twelve-month basis, investment volume reached EUR 387 bn, the second-highest level recorded over such a period. However, transaction volumes were down in Q2 2022 compared to Q2 2021 (-9%), reflecting market uncertainty and increased borrowing costs.

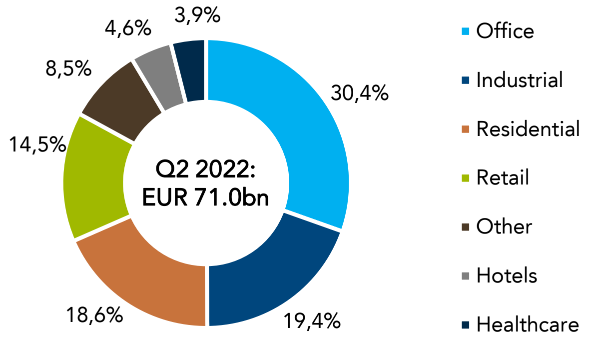

Figure 2: Transaction Volume by Asset Class (Western Europe).

The sector breakdown shows a strong positive trend in the industrial sector (H1: +18%) even though the transaction volume in this sector declined by 8% in Q2 2022.

[1] Source: CBRE - European Real Estate Investment Volumes Q1 2022.

PRIME CAPITAL

Transaction volumes in the office market were 19% lower in Q2 2022 (YoY) at EUR 21.6 bn, however H1 2022 shows a significant recovery vs. H1 2021 (+20%). On a year-on-year basis, European office rents are up 3.6% which is above the average of the past five years (+3.3%). Even though construction activity has decreased to 1.1m sqm in Q2 (-12% YoY, -21% QoQ), the largest shares of completed office space in Europe fall to three German cities: Berlin (167.000sqm), Hamburg (129.000 sqm), and Munich (118.000 sqm) followed by Paris (99.000 sqm). Investors in this segment show a growing preference for high-quality sustainable properties, which means that competition and demand for these assets remain high. By contrast, lower-quality assets are attracting less interest as investors consider the capex investments that are required to bring these assets up to sustainable and marketable standards.

The retail market has also recovered and recorded an increase of 52% in H1 2022. This brings the overall transaction volume back to pre-pandemic levels. However, the strong increase in transaction volume in H1 2022 is mainly due to the sale of a EUR 2bn portfolio in Spain.

Looking at the residential, hotel and healthcare sectors, all sectors have lower transaction volumes in Q2 2022 (-20%, -26% and -26% respectively), and transaction volumes in H1 2022 have also decreased compared to the same period last year (-7%, -13%, and -13%).

Mezzanine and Whole Loan Financing Market Overview[2]

In the second quarter of 2022 we observed changing financing conditions in the alternative finance space. Average IRRs increased for financings against existing assets, both for Whole Loans (+50 bps to 600 bps - Figure 3) and Mezzanine (+170 bps to 11,5% - Figure 4). Simultaneously, average LTVs decreased slightly compared to Q1 2022, down to 72% (-3 percentage points) for Whole Loans and to 74% (-2 percentage points) for Mezzanine. Returns increased due to rising base interest rates and funding tightening with banks further withdrawing from the sector.

Therefore, despite lower transaction volumes, the deals that were closed by alternative financiers are more "bankable" than before, i.e., risk-return-profiles are evolving favorably to the benefit of end investors who have decided to include Real Estate Debt in their strategic asset allocation. We expect this situation to continue and alternative lenders to gain further market share.

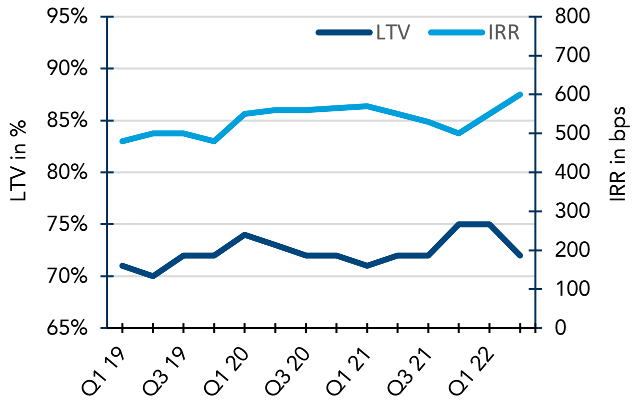

Figure 3: LTV and returns for existing properties Whole Loan financing in Europe.

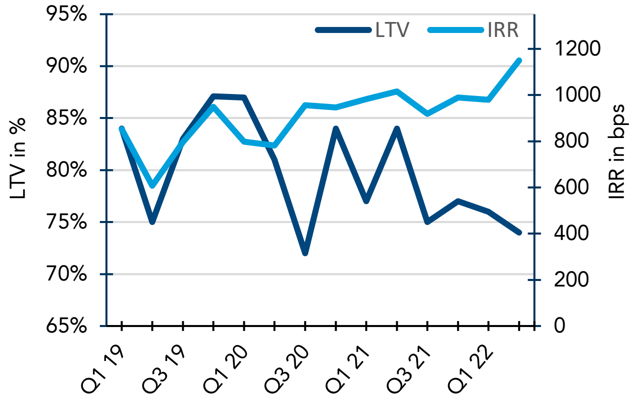

Figure 4: LTV and returns for existing properties Mezzanine financing in Germany.

A similar situation could be observed in the development financing sphere. Whole Loan project development financings in Q2 2022 offered higher average IRRs (+75 bps to 725 bps) with stable LTC levels around 71% (Figure 5). Mezzanine development financings showed a small reduction in LTC levels to 80% (-2 percentage points) with increased IRRs of +50 bps to ~12% (Figure 6). Overall, we observe improved conditions from lender's perspective, at the same time rising inflation and higher interest rates have slowed down project development activity. But we continue to see institutional investors to invest in project developments, because the interest rate is still risk-adequate. What is important is a selective approach. A prerequisite for commitment: a high-quality project, contractually fixed costs and a solid business case.

[2] The aggregated data in this section is based on the transactions conducted by Prime Capital (closed-, pipeline- and rejected-deals).

PRIME CAPITAL

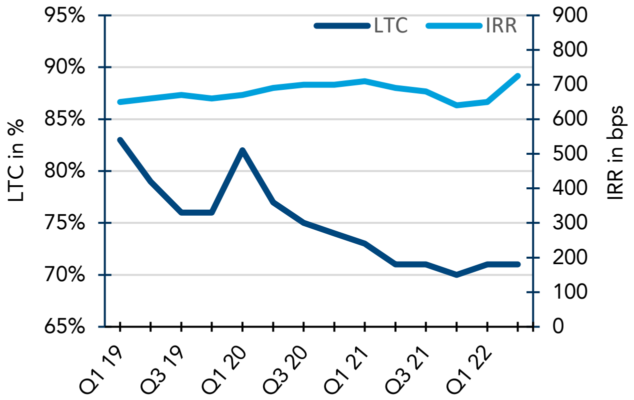

Figure 5: LTC and margins for Whole Loan project development financing in Europe.

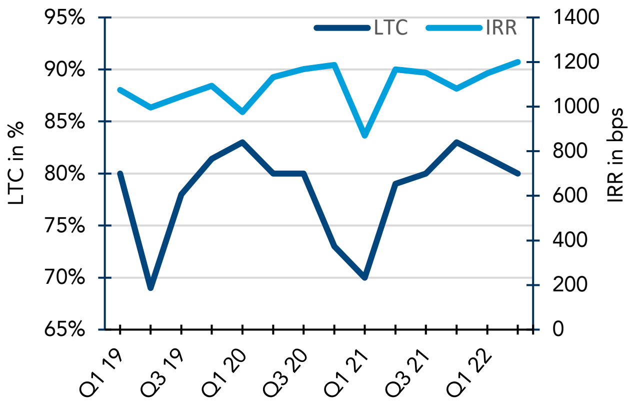

Figure 6: LTC and margins in Mezzanine project development financings in Germany.

Dealing with current market challenges

The real estate market is facing a challenging period: rising interest rates, higher ESG requirements, increasing construction costs etc. are leading to increasing uncertainty in the market and a divergence between buyers' and sellers' price expectations, resulting in an overall decrease in transaction volumes.

We opt for a differentiated approach as part of our lending strategy. For example, with regards to high inflation, we provide financing currently only for projects where construction costs either represent only a minor part of total costs or where construction costs are largely contractually fixed. In addition, we enforce more and more structural elements, such as construction cost contingencies, cost overrun guarantees and additional equity injection provisions. When selecting properties and locations to be financed, we stress the ability of the intended buyer to finance / acquire the property and deliver on their business case: can they continue to carry out their strategy despite the higher interest rates, so that the exit of our financing is highly likely? To manoeuvre in such a rising interest rate environment, financing should be provided where the overall exposure is reduced over the term (amortization, up-front payments, ongoing interest). Floating rate loans or loans with interest rate step up are also options to keep margins constant.

When analysing financing opportunities, we increasingly take into account the quality of the sponsor and its financial resources (creditworthiness), as well as - to the extent relevant and possible - the quality of the other parties involved in the project, in order to be able to compensate for a delay in the project or increased costs. The possibility of a macroeconomic downturn should also be increasingly considered in the underwriting of financing opportunities. We include differentiated stress tests, additional collateral, lower loan-to-value ratios, more extensive reserves and higher equity commitment.

Overall, despite the declining transaction volume in the market and the current challenges due to the current developments in connection with the very restrictive lending policies of banks, we are seeing more transactions that were "bankable" a few months ago. This further increases the quality of the assets submitted to us for financing. Furthermore, this enables us to be even more selective in origination and to source transactions with lower risk and higher-return profiles for our investors.

Sample Q3 2022 Pipeline

Despite the current market challenges, our pipeline is well filled. What is noticeable is that we are receiving more and more funding requests from sponsors who previously relied on pure bank financing.

Sample Q3 2022 transaction opportunities (pipeline)

Location	Sector	Asset Type	Financing Type	LTV	IRR	Size
Germany Top 7	Mixed Use	Develop-ment	Mezzanine	67.5%	11.0%	20.0m
Germany (Portfolio)	Resi-dential	Existing	Whole Loan	75.0%	6.0%	42.0m
Germany (Top 7)	Office	Existing	Mezzanine	68.1%	12.1%	20.5m
France (south)	Mixed Use	Develop-ment	Mezzanine	70.0%	12.0%	20.0m
Netherlands (central)	Resi-dential	Develop-ment	Whole Loan	65.0%	6.25%	60.0m
Germany (Top 7)	Office	Existing	Whole Loan	80.0%	6.5%	78.0m

About Prime Capital's Private Debt Team

Our team has been active in the Real Estate Debt market for many years, with a particular expertise in Mezzanine and Whole-Loan transactions and has already carried out transactions of more than EUR 700m. In addition, our wider Private Debt Team invests into Transport Debt, Infrastructure Debt and Corporate Lending. We expect significant further growth in these areas, which provide attractive risk-adjusted returns to our investors.

Prime Capital's Private Debt Team manages assets in excess of EUR 2bn across private debt segments on behalf of institutional investors.
Further information about Prime Capital AG can be found on our website www.primecapital-ag.com.

Contact:

Dennis Davidoff
Director
Real Estate Debt

Prime Capital – Portfolio Management Private Debt
impd@primecapital-ag.com

PRIME CAPITAL

Disclaimer:

*The information and opinion contained in this document (hereinafter "**Information**") is provided only for advertising purposes, and is not construed as a solicitation or an offer to buy or to sell any securities or financial instruments in any jurisdiction whatsoever. It does not constitute an official confirmation, invitation, solicitation or offer to subscribe for or purchase or sell any of the products or services of Prime Capital AG, Frankfurt am Main. No investment decision should be made on the basis of this document. The Information contained herein may not be complete and may not contain all relevant material information related to any (financial) instrument presented. No representation or warranty is made or implied concerning, and Prime Capital AG assumes no responsibility for, the accuracy, completeness, reliability or comparability of the information contained herein relating to third parties.*

The Information contained in this document was obtained in good faith from sources considered to be reliable, but its accuracy, completeness, reliability, or comparability is not guaranteed or otherwise warranted or represented by Prime Capital AG. Specifically, the Information contained herein has been obtained from third party sources, which is based solely on publicly available information. Prime Capital AG makes no representation, express or implied, as to the accuracy, correctness, suitability or timeliness of such data. In particular, Prime Capital AG is not obligated to update information provided in this document or to delete obsolete information from this document. The information provided in this document may change at any time without prior notification. As a result, information once published in this document may not be understood to mean that matters have remained the same since publication or that the information is still up-to-date following its publication. The validity of the information is limited to the point in time of their being issued and may change based on market developments.

This document and the Information contained herein is confidential and intended only for the person to whom it has been provided and under no circumstance may a copy be shown, copied, transmitted, or otherwise given to any person other than the authorized recipient without the prior written consent of Prime Capital AG.

The content of this document is protected by intellectual property rights owned by Prime Capital AG. The reproduction, transmission (electronically or by other means), linking, alteration, storage, archiving or other uses for public or private use of information or data, in whole or in parts, in particular, the use of texts, portions of texts or images requires the prior consent of Prime Capital AG. In particular, you are prohibited from:

- *i. copying this document in whole or in parts (whether by printing them on paper, saving them to a file or otherwise);*
- *ii. removing, changing or otherwise making the content of this document incomprehensible or using the material contained on this document in a manner other than intended in these legal notices and terms of use;*
- *iii. using this document or the information it contains for unlawful purposes.*

The Information provided herein is not taking into account any particular person's objectives, financial situation or needs. Investors should before acting on the information provided in this document, consider the appropriateness of the information having regard to their individual objectives, financial situation or needs.

Please bear in mind, that any forward looking statements re targets and achieving such targets is subject to unexpected risk and uncertainties and can not be guaranteed in any way.

Privacy:

Prime Capital AG is committed to protecting your privacy. The types of personal information we collect about you depends on the relationship with us. They include (i) your personal contact details such as name, title, postal addresses, email addresses and telephone numbers, (ii) the company you work for and your position, (iii) identification and background information we may collect about you as part of our business acceptance procedures, (iv) technical information such as information from your visits to our website or relating to the event invitations, updates, marketing material, and other communication we send to you electronically, (v) your communication preferences regarding marketing materials or (vi) any other personal information you provide to us during your relationship with us, such as dietary requirements, any physical disability and your views and comments.
They ways in which we collect personal information about you may include the following: (i) in the course of our business acceptance procedures, (ii) through your general use of our website . In particular, we collect personal information about you if you complete forms on our website and if you send emails to firm personnel, (iii) through your responses to our emails asking that you confirm and update information we maintain about you, or that you provide your consent for us to communicate with you, or (iv) through information you may provide to representatives of our firm at conferences or similar events.