

The Children's Day Care Real Estate Market in Germany

An Introduction

2020



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FOREWORD

In recent years, children's daycare facilities have attracted increasing interest among institutional real estate investors. In this report, Cushman & Wakefield would like to present a niche market that has thus far received far too little attention.

Due to the fact that there is a legal right to childcare in Germany but the supply landscape does not provide appropriate coverage to adequately meet demand, childcare in Germany is a socially and politically hot topic! The everyday life of about 11.4 million families with children is dependent on a professional childcare service in Germany. And the need for children's day care facilities is growing. According to a study by the German Economic Institute in 2018, there was a deficit of over 300,000 daycare slots for the under-3 age group alone. In addition, the Bertelsmann Foundation prognosticated that, as many as 583,000 new trained child care workers will be required by 2025.

We are also pleased to present two expert

interviews; one with Mr Daniel Wolf, Head of Asset Management at E&G, and the second with Ms Sascia Hauke, Head of Transaction Management and Ms Anahita Afzalkhani, Senior Transaction Manager, at AviaRent Invest AG, and thus with two real estate investors active in the field of social real estate.

In this sense we wish you an exciting read of our new Children's Day Care Real Estate report and hope we provide some interesting findings along the way as well as some transparency in what is still a very under-explored market.





01

**GERMANY'S SOCIO-
DEMOGRAPHIC AND
SOCIO-ECONOMIC
STRUCTURE**

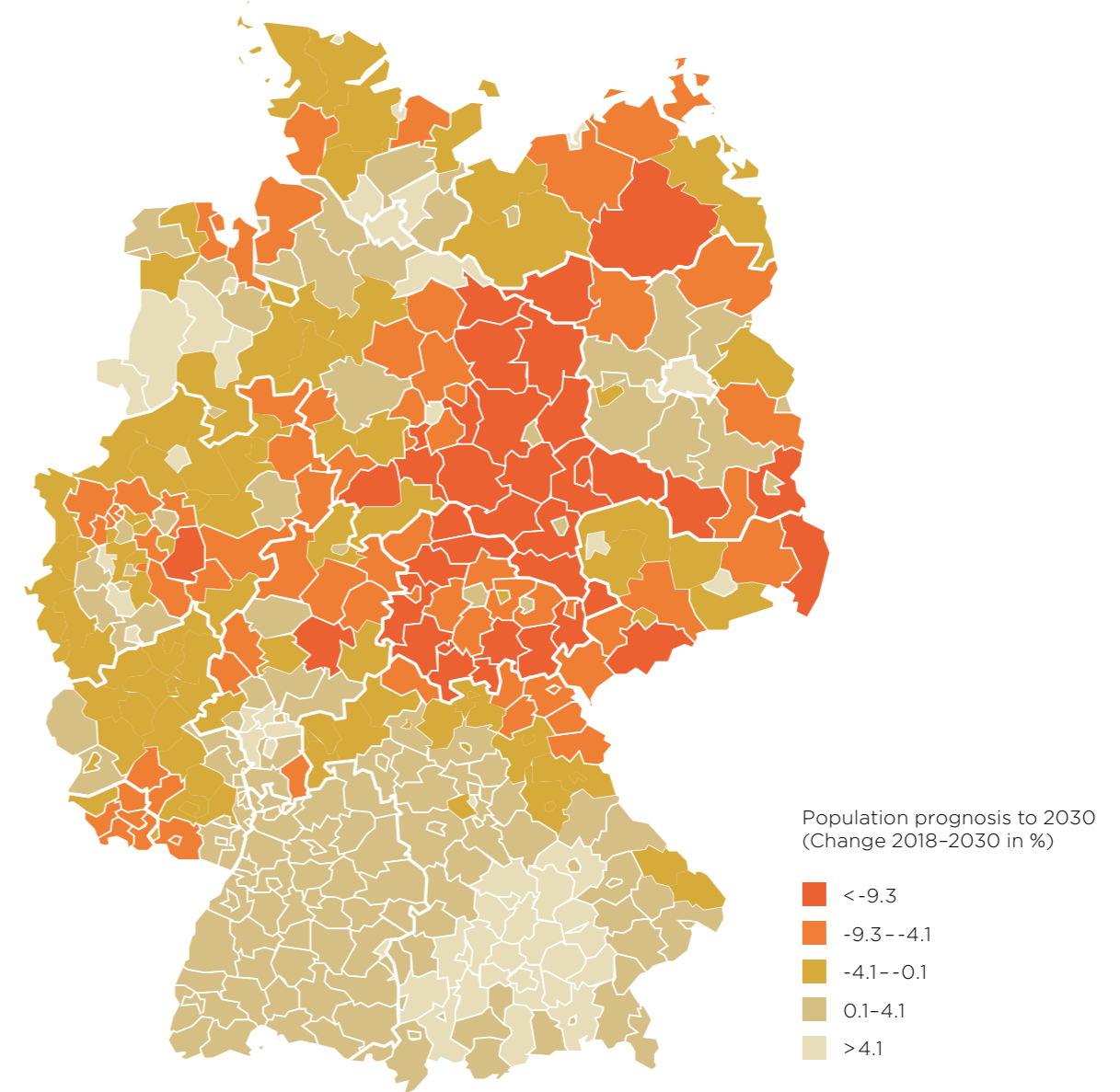
Germany is in a better economic position than ever before and is by far the largest economy in Europe. In 2019, GDP will have grown for the tenth year in succession. This is the longest period of economic growth in the history of modern Germany. A weakening of the economy due to the Coronavirus crisis, at least in 2020, appears inevitable, but the extent of this is still unclear. Within the European Union, Germany remains the "Powerhouse" and is still considered worldwide as the "safe haven" of Europe. The unemployment rate has continuously fallen for the last ten years and was below five percent as of 2019.

Despite Germany's leading economic position, another social issue is currently dominating the public debate and, along with the acute management of the Coronavirus pandemic, is probably the most important national structural challenge of the coming decades: Germany is in the midst of demographic change. On the one hand, the population is aging, and on the other hand there are regional differences in population development. Population growth is predicted to be focused mainly in conurbations and metropolitan regions. Moreover, from a demographic point of view, there is not only an east-west but also a north-south divide in Germany. While in southern Germany and in the conurbations, population growth is, predicted for the period up to 2030, the trend is predicted to be largely negative in parts of the Ruhr region, for example, as well as in many rural and peripheral regions and in the "new federal states" formerly comprising East Germany. This is due to the fact that young and highly qualified inhabitants in particular are drawn to the economically stronger regions.

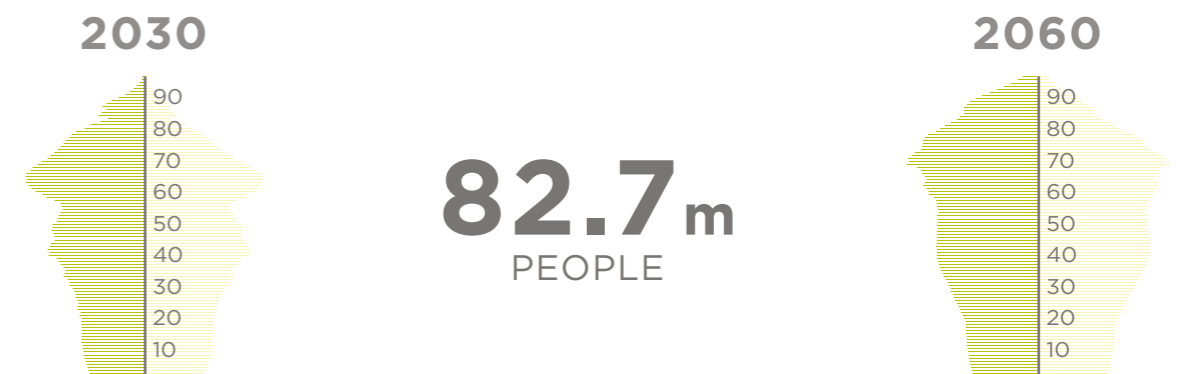
While the proportion of old people in Germany is rising continuously, the proportion of young people is stagnating. Although the birth rate is not falling continuously, life expectancy is rising, contributing further to the increasing proportion of older people in the total population. As a result of this trend, the public focus in this country tends to be on the ageing society, both politically and socio-economically. While nursing care for the elderly is increasingly on the political and social agenda and has become established as the number one campaign topic, the structure of the younger population and its development as well as childcare, at least in public, often takes a back seat.

The proportion of the younger population in Germany is highest in western and southern regions in particular, as well as in urban areas. The trend towards one- or two-person households results in an increasing dependence on third parties, including with regard to childcare. An additional factor is the increasing flexibility in the choice of professional location. Young people in particular are increasingly moving away from their original home to other cities. Therefore, the proportion of parents with relatives nearby who can provide or help with childcare is falling.

German Population Development by District

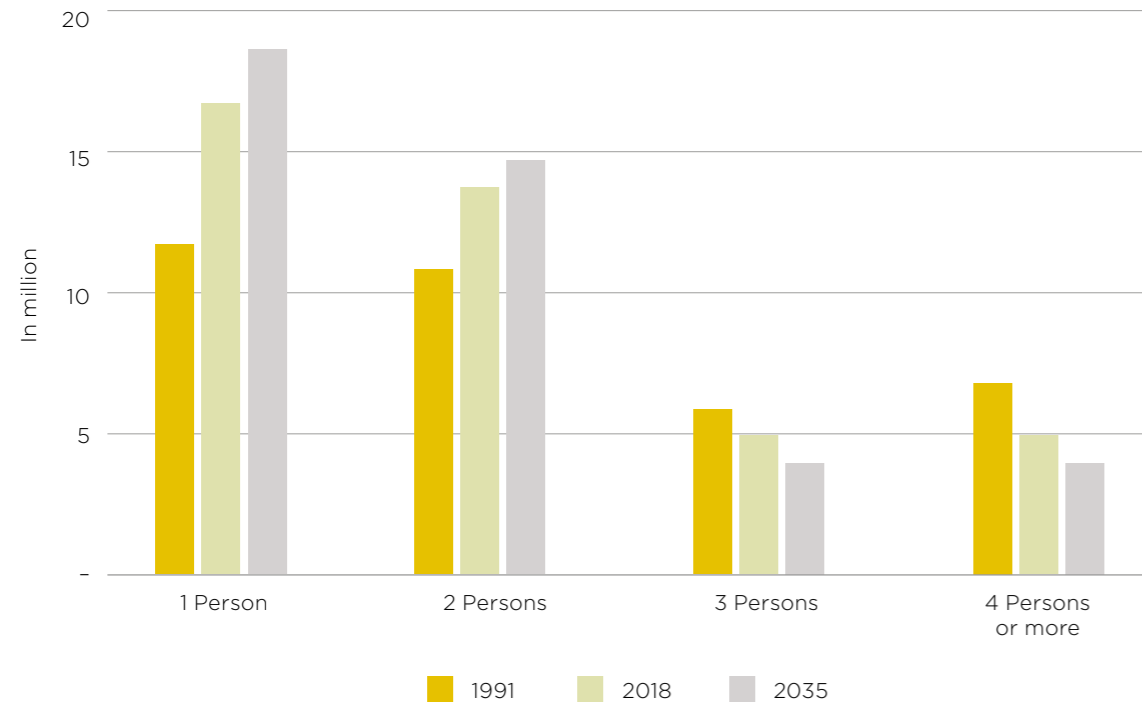


Riwis, Cushman & Wakefield 2020



Statistisches Bundesamt, Cushman & Wakefield 2020

Development in number of households by size 1991 to 2035

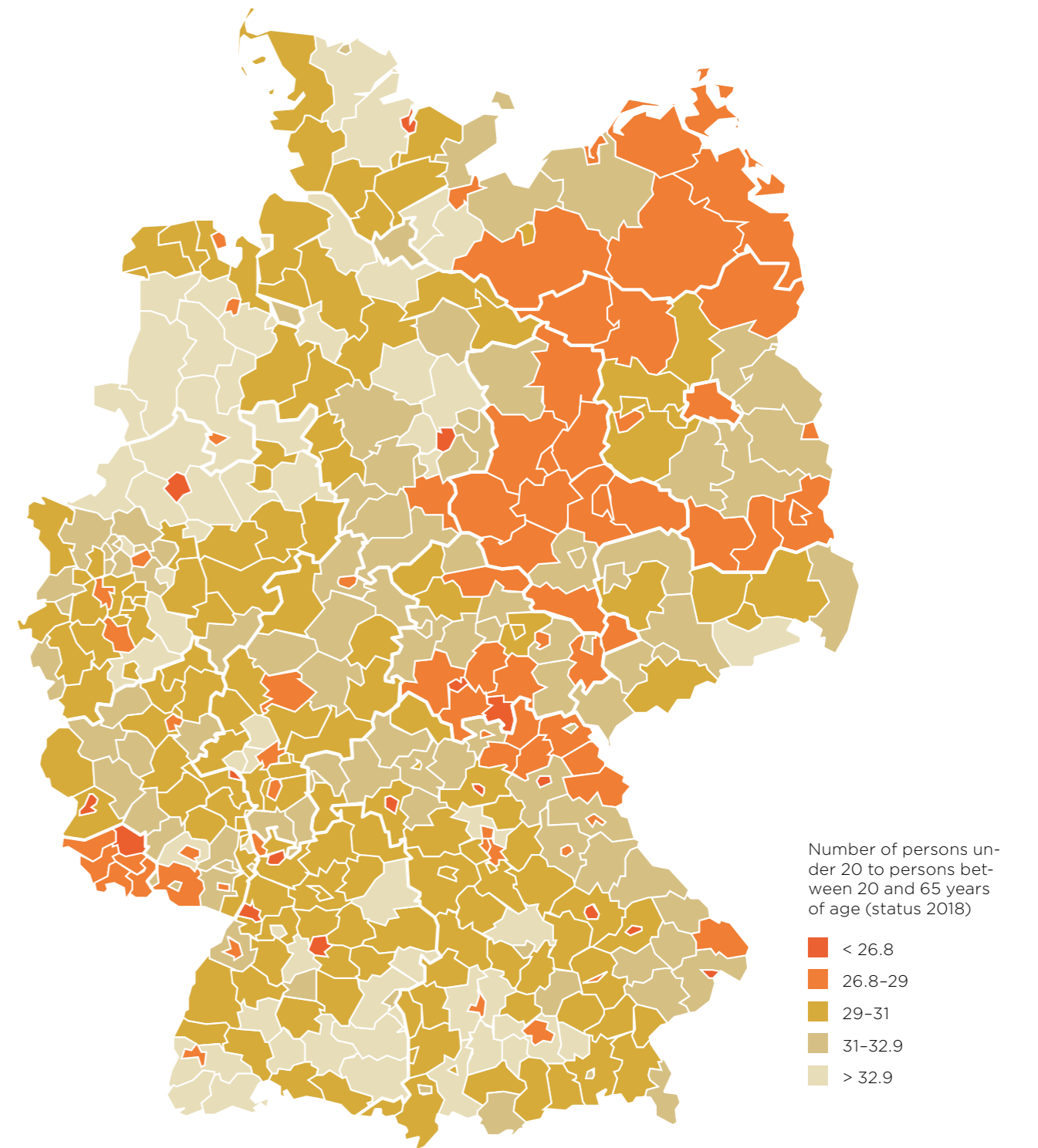


Statistisches Bundesamt, Cushman & Wakefield 2020



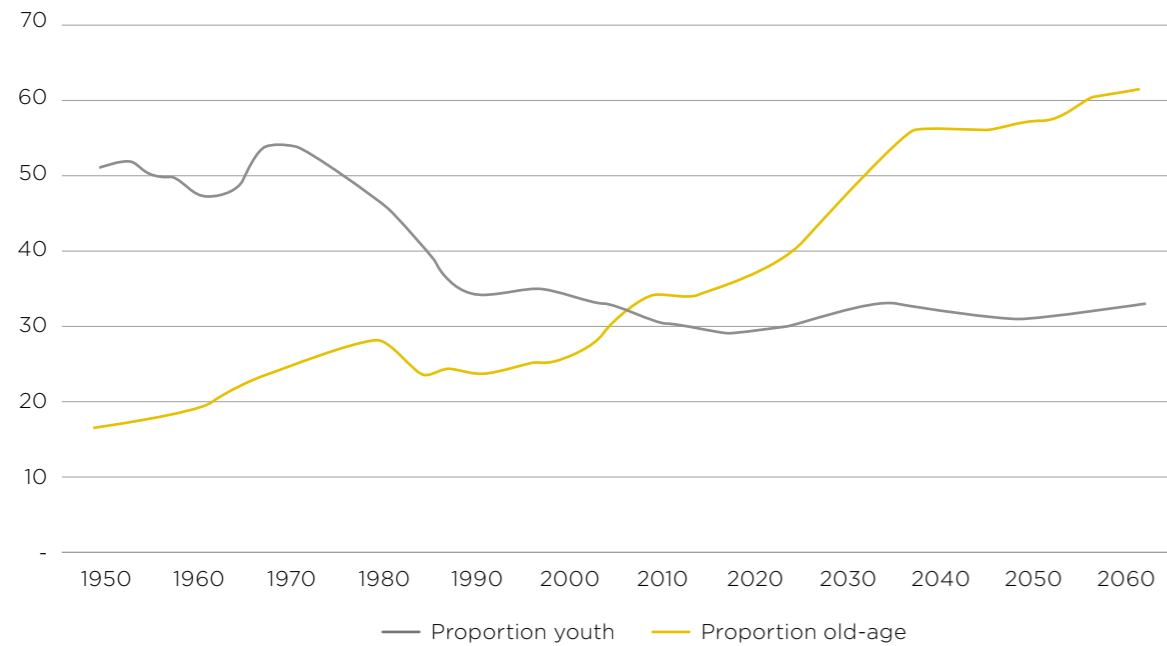
KEY FACTS - PROPORTION OF YOUNGER PERSONS, FERTILITY & LIFESTYLE

Proportion of youth 2018



Riwis, Cushman & Wakefield 2020

Comparison of development youth and old-age cohorts



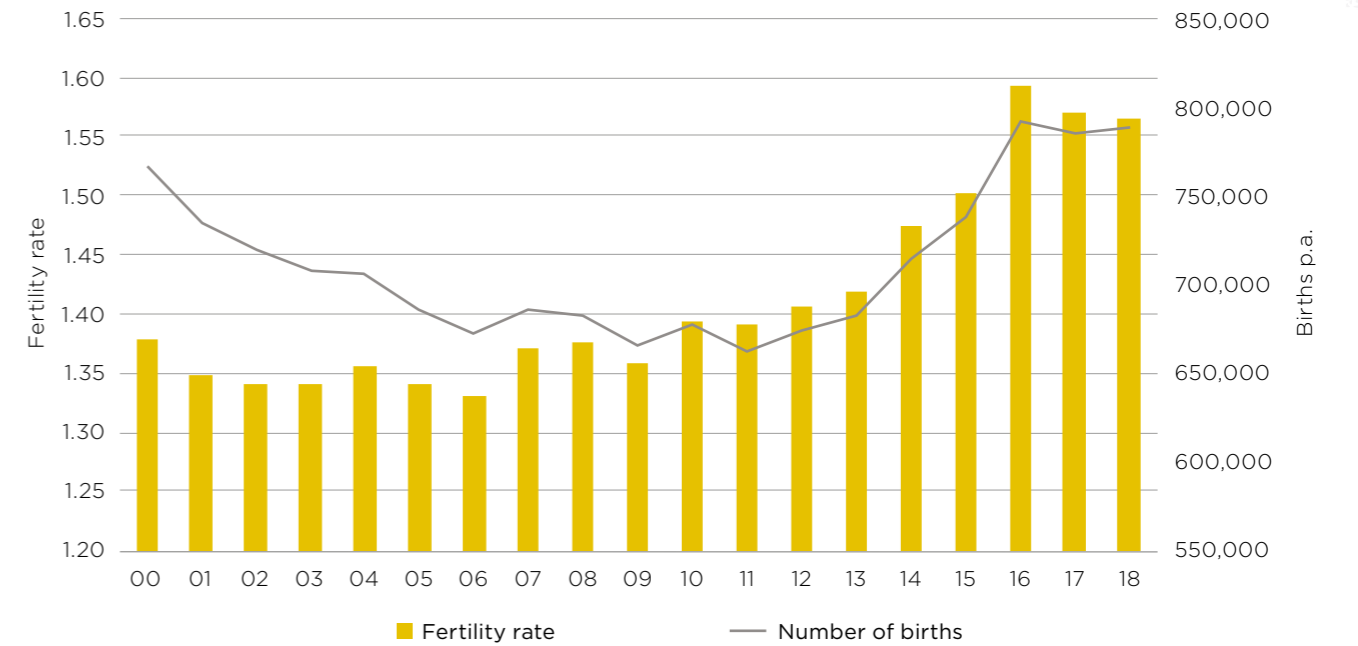
Statistisches Bundesamt, Cushman & Wakefield 2020

The number of births per woman (fertility rate) has remained at a relatively stable level over the past almost 20 years. The fertility rate of a calendar year shows how many children on average per woman were born. It defines both the behaviour of women in the respective calendar year and also the average number of children that a woman has in the course of her life. For about two years it has stagnated at roughly 1.57 births per woman. Over the last ten years both the fertility rate as well as the number of live births have increased significantly. The average age of a first-time mother in Germany is approximately 30 years. An increasing number of women in Germany are having their first child in the fourth decade of life. In 2018, 48% of mothers of the total of 366,000 first-born children were between 30 and 39 years old. About 3% were older than 39 years.

According to the Federal Statistical Office, about one fifth of all women in a particular year's cohort remain without a biological child on reaching the end of the fertile age range, considered to be between 15 and 49 years.

A total of 787,500 live births were recorded in Germany in 2018 and more people die in Germany each year than are born. Although it is not possible to make an exact forecast of the resulting decrease in the total population in Germany excluding migration according to forecasts by the Federal Statistical Office, a decline in the population from 2030 appears a realistic prospect.

Development of fertility rate and number of births (2000 to 2018)



Statistisches Bundesamt, Cushman & Wakefield 2020

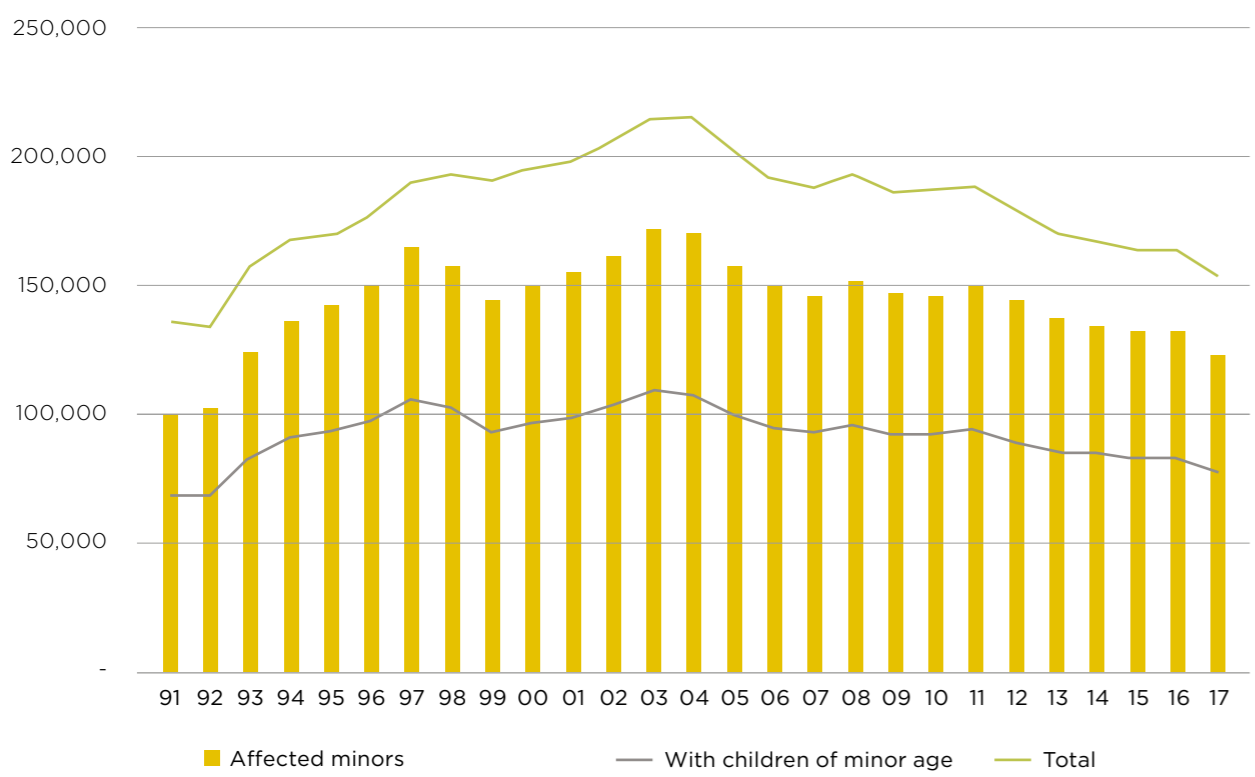


Although the number of divorces fell from 191,948 in 2008 to 148,066 in 2018, the number of divorces has in principle remained at a relatively stable level over the last 20 years. The number of children affected by a divorce has also remained relatively stable.

The number of single mothers has fallen slightly, from 2.74 million in 2015 to 2.58 million in 2018. At the same time, the number of working women has risen continuously over the past few years - this not only demonstrates progressive emancipation, but also a social change that is taking place and is of decisive relevance, especially in the area of childcare: The employment of parents is increasing, and as a result, the demand for high-quality childcare facilities is growing throughout Germany.

Ever more mothers are taking maternity leave, but are also returning to their old jobs much earlier. This development is due to Elterngeld parental benefit payments and the increasing employment of women. For example, in 2010 only 31.5% of mothers of children under 3 years of age were employed. By 2017, this figure had risen to 32.3%. Of the mothers of 3 to 5-year olds, 60.5% had a job in 2010 and 63.6% in 2017. This trend has continued in recent years.

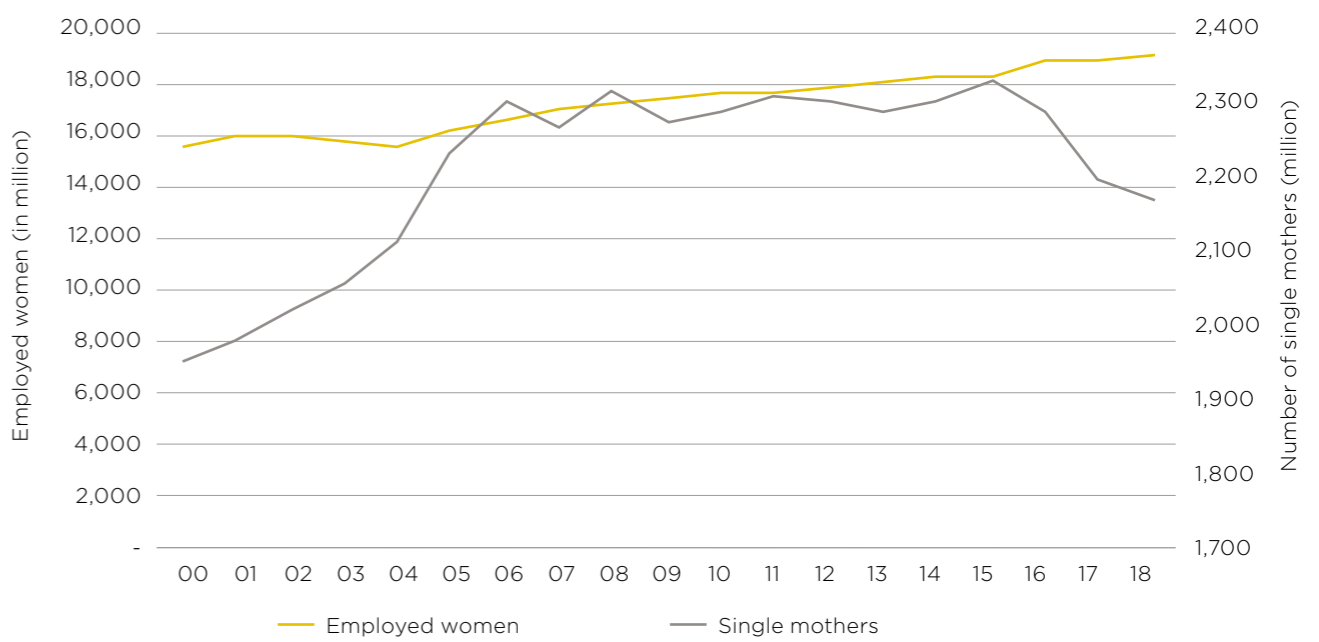
Development in number of divorces



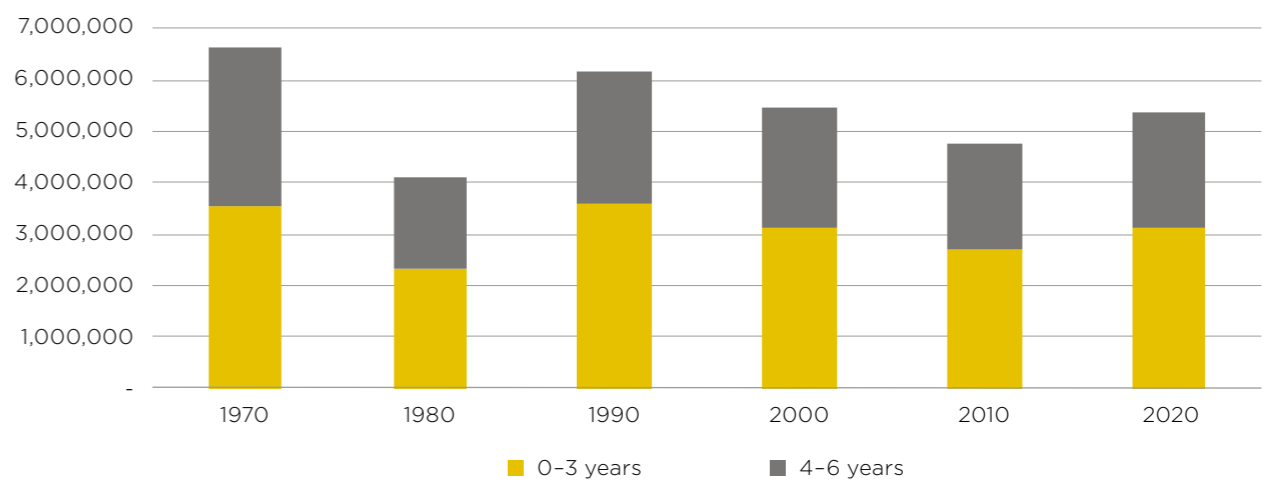
Statistisches Bundesamt, Cushman & Wakefield 2020



Development in women's employment and the number of single mothers



German population growth by age cohort (1970-2018)



Statistisches Bundesamt, Cushman & Wakefield, 2020

Childcare is generally considered in a differentiated manner by age cohort - in particular, the "up to 3 year olds" and the "4 to 6 year olds" are the relevant population groups for daycare. The number of small children had been declining in Germany since 1970 but increased again slightly between 2010 and 2018. Between 2010 and 2018, both the number of children aged up to 3 years and the number of 4 to 6 year-olds in Germany

increased. The number of small children is generally highly dependent on exogenous, partly social and partly economic factors. A valid forecast of these is therefore relatively difficult. However, the Federal Statistical Office provides prognoses under various scenarios.



A bright, colorful children's playroom. In the foreground, there's a wooden table with three small, colorful stools (yellow, pink, and floral). A large yellow circle is overlaid on the right side of the image, containing the number '02' and the title 'CHILDCARE IN GERMANY IN INTERNATIONAL COMPARISON'. The background features a wooden easel, a storage unit with colorful bins, a basketball, a cactus decoration, and a blue wall with yellow light bulbs. The floor is made of light-colored wood planks.

02

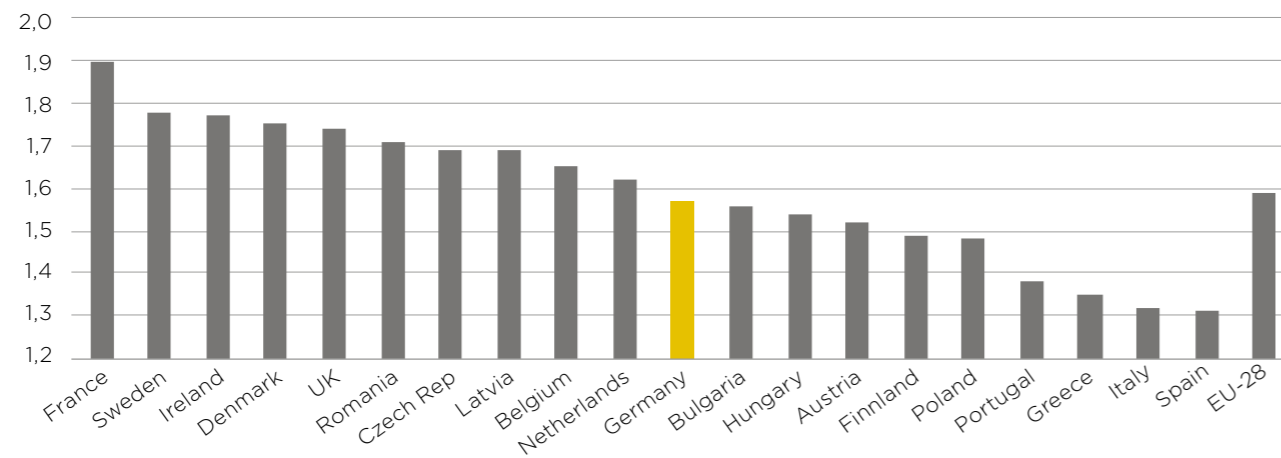
CHILDCARE IN
GERMANY IN
INTERNATIONAL
COMPARISON

CHILDCARE IN GERMANY IN INTERNATIONAL COMPARISON

Across Europe there are major differences in childcare. These are not limited to childcare as such, but also in the level of expenditure as well as in the sociodemographic basis of the different countries. While the fertility rate is highest in France, Germany is in midfield, at 1.57. The Southern European countries, such as Portugal, Greece, Italy and Spain exhibit the lowest fertility rates.



Fertility in European comparison

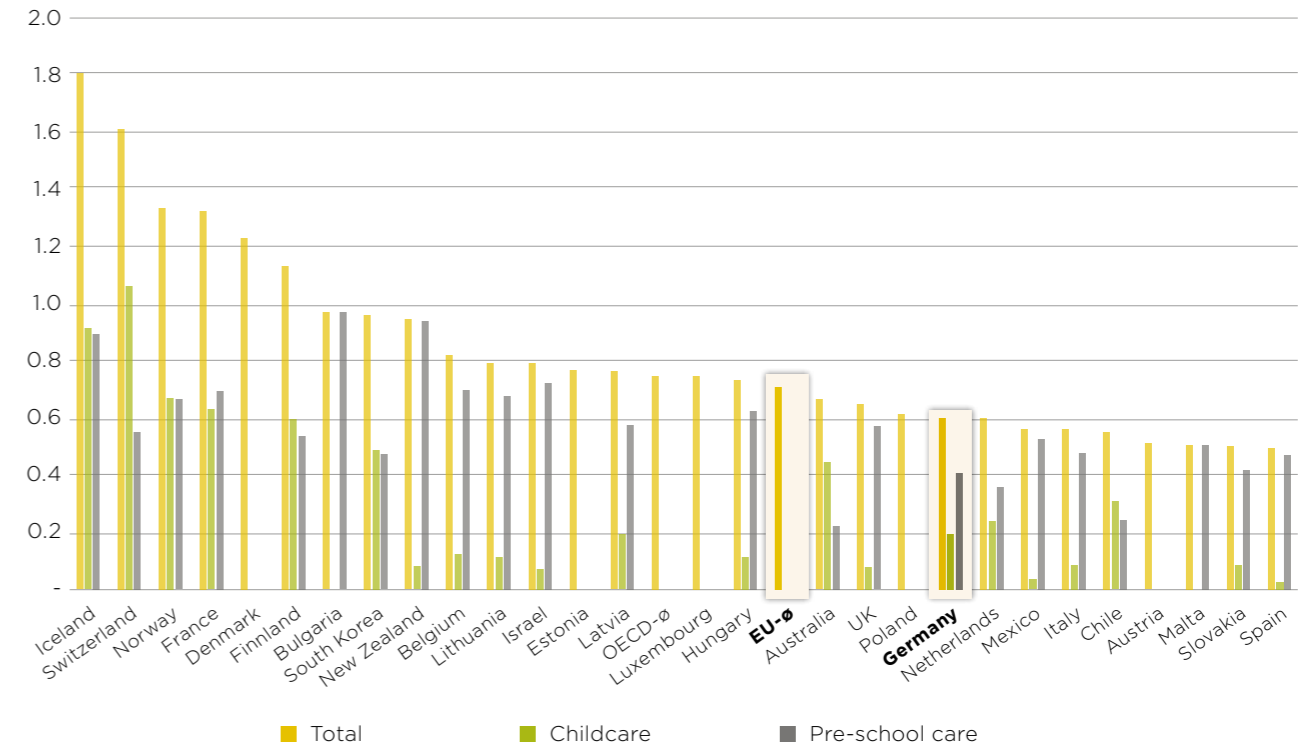


Eurostat, Cushman & Wakefield 2020

European countries also differ considerably in terms of support and financing from national budgets. The Scandinavian countries and France invest the highest percentage of

their GDP in childcare. Germany is in midfield with just 0.6% of GDP. With 1.8% of GDP, Iceland spends the highest proportion on childcare in Europe.

Expenditure on childcare, percentage of GDP in international comparison



Eurostat, Cushman & Wakefield 2020

In general, there are great differences in childcare in Europe. While in countries such as Denmark, Sweden, Ireland and France a large proportion of children are looked after in day-care centres or by childminders, in Eastern Europe the majority of children are looked after by their mothers. Moreover, in countries with a higher female employment rate, childcare is better organised and there is a better supply.

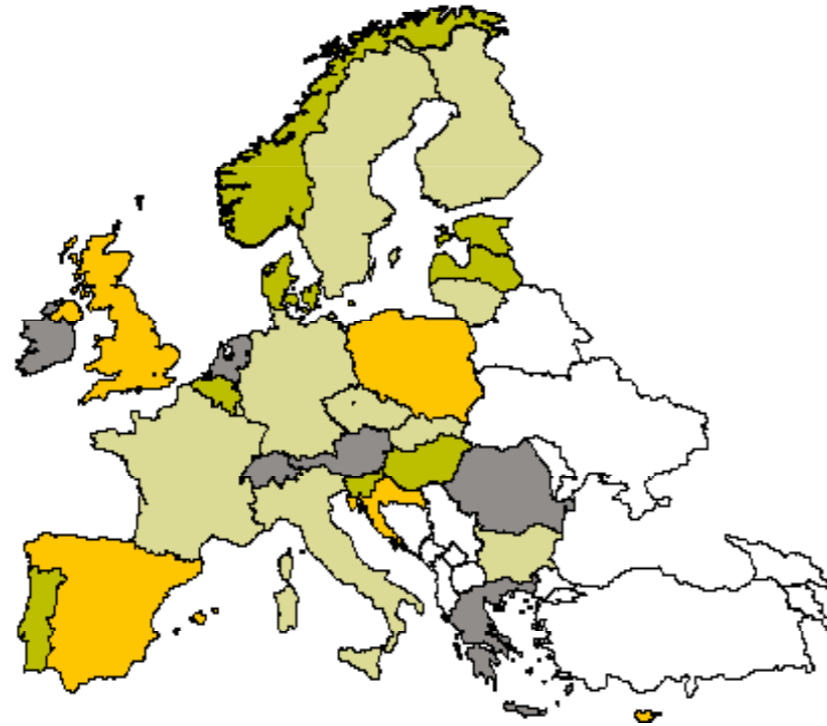
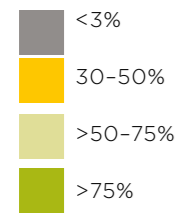
Other reasons why so many children go to day-care centres in Denmark, for example, are the wide range of facilities on offer and the state subsidy, as the fees are financed by taxes and there is no parental contribution. Moreover, the rate of female employment in Denmark is 72%. In Germany there are more childcare places now than a few years ago. This is due to the high level of state

investment in recent years and was triggered by increased demand for daycare places. An observation here is that European countries which invest more money in childcare have a higher birth rate and lower child poverty. Germany is again midfield, in a comparison of day-care centres across Europe.

According to a study by the German Economic Institute, there was an estimated shortfall of over 300,000 daycare places (for under 3-year-olds) in Germany in 2018.

Due to the increase in female employment, the topic of childcare is becoming ever more important generally and is also gaining in importance in Germany. In recent years, this topic has increasingly moved into political focus.

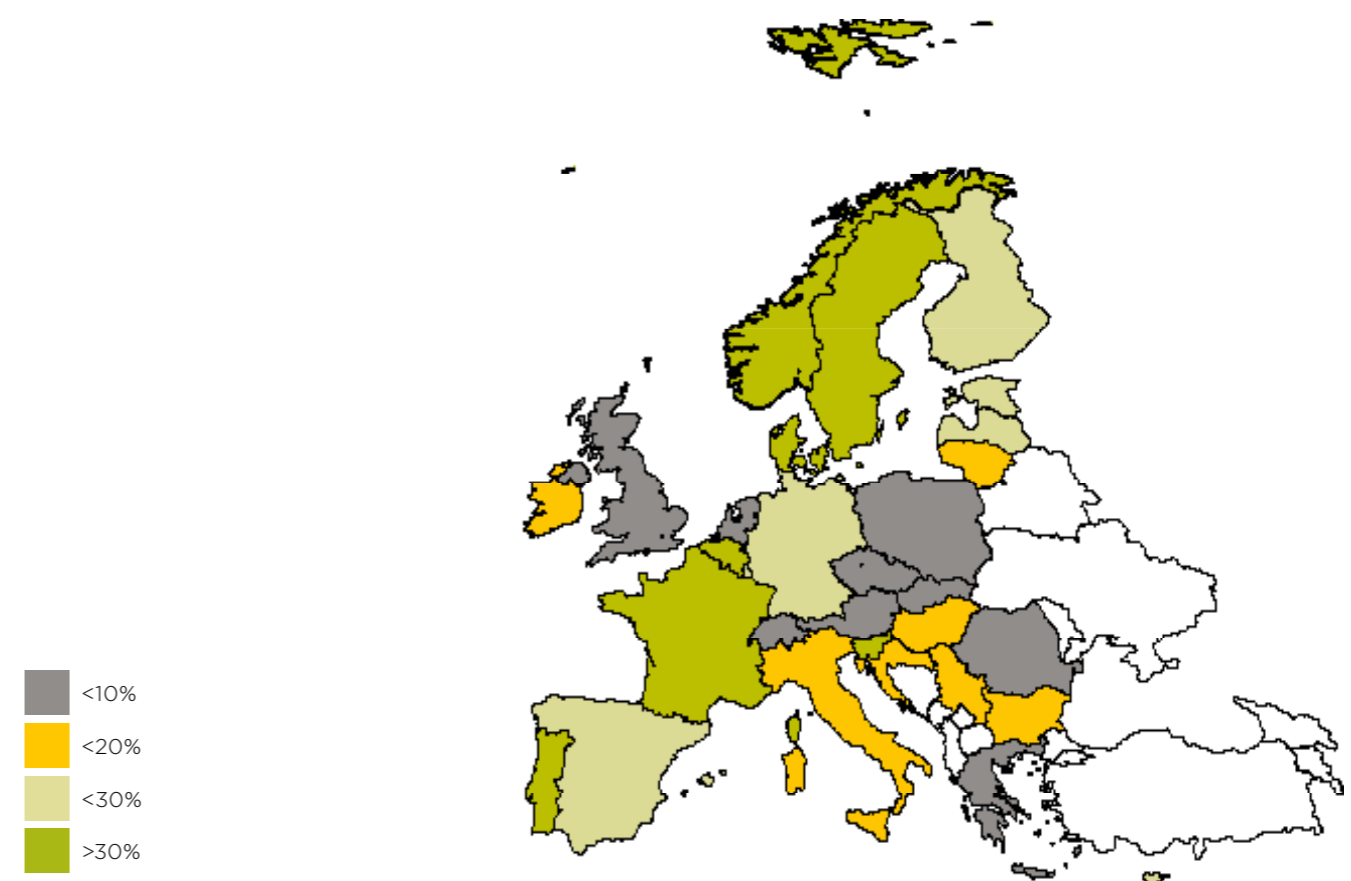
**Childcare in Europe:
3 years until school age,
30 hours or more**



Childcare by age cohort and length of care (%)

Country	0-3 years		3-6 years	
	LESS THAN 30 HRS CARE (2018)	MORE THAN 30 HRS CARE (2018)	LESS THAN 30 HRS CARE (2018)	MORE THAN 30 HRS CARE (2018)
Germany	7.7	22.1	30.0	59.5
France	19.6	30.4	34.8	59.9
UK	31.7	7.0	37.9	31.7
Italy	9.6	16.1	21.8	69.2
Spain	30.2	20.3	52.5	42.4
Portugal	1.4	48.8	5.5	88.4
Sweden	15.1	34.3	25.5	69.6
Finnland	12.3	24.9	21.4	63.8
Denmark	8.7	54.5	15.3	79.8
Norway	5.2	50.4	7.5	80.9
Belgium	20.0	34.0	19.6	79.1
Bulgaria	0.9	15.3	4.9	72.9
Czech Republic	5.2	3.8	25.8	53.6
Ireland	26.1	11.6	69.2	25.9
Poland	2.1	8.8	15.3	44.1
Netherlands	50.5	6.3	69.4	15.3

Childcare in Europe: 0-3 years 30 hours or more per week



A young girl with long, wavy red hair is seen from behind, painting a colorful picture on an easel. She is wearing a white t-shirt. The painting depicts a landscape with a green hill, a yellow sun, and a blue sky. In the background, other children are visible, some playing with a ball. A large yellow circle is overlaid on the right side of the image, containing the number 03 and the title of the document.

03

**INTRODUCTION TO
CHILDREN'S DAY CARE AND
ITS LEGAL FRAMEWORK**

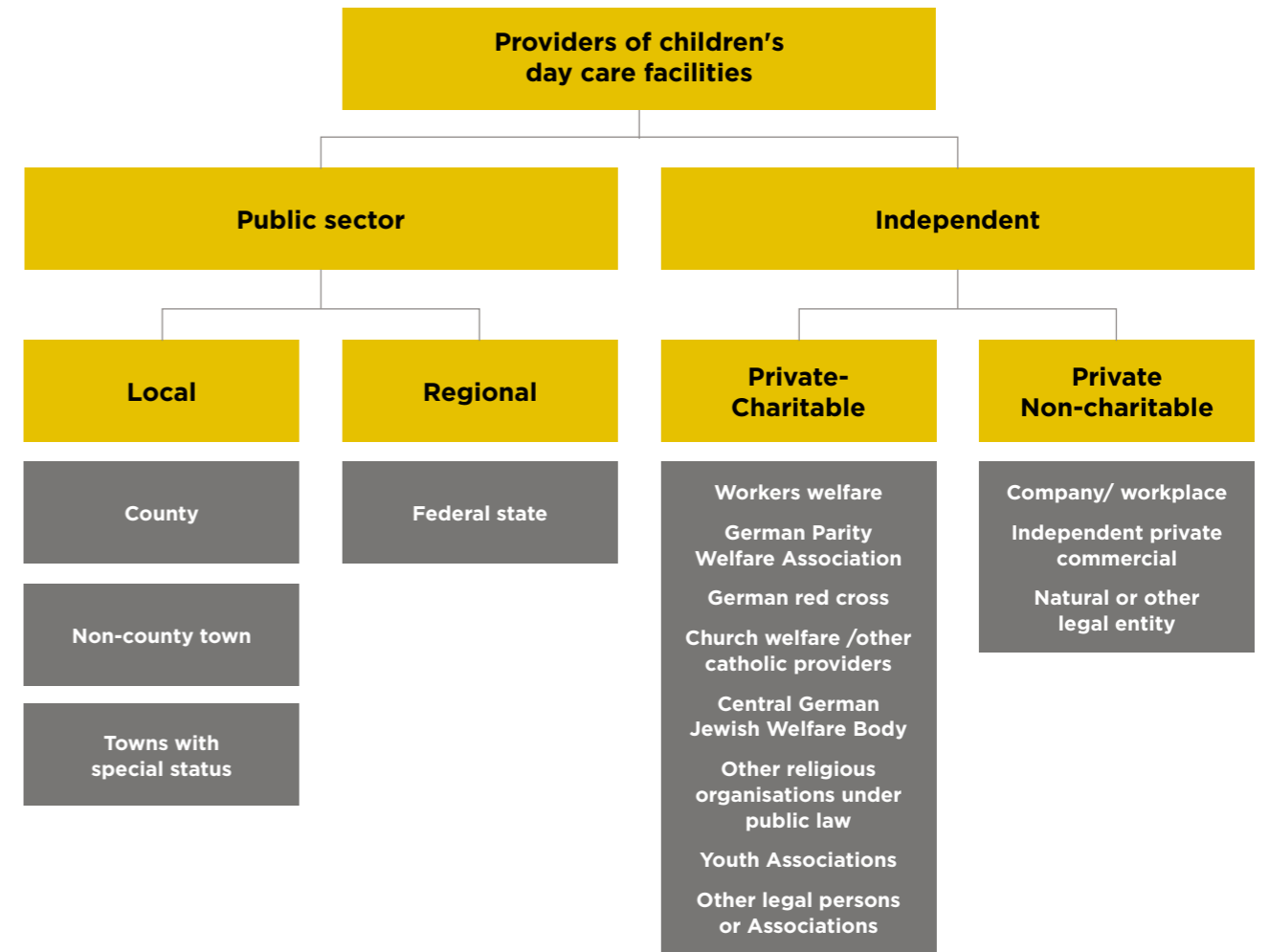


INTRODUCTION TO CHILDREN'S DAY CARE AND ITS LEGAL FRAMEWORK

Providing childcare in day-care centres is one of the most important social and political tasks in Germany. Since 1996 there has been a general legal entitlement to care in Germany - therefore providing care in line with demand throughout the country is an essential task of the legislation. Since 1 August 2013, children who have reached the age of one have a right to a place in a day care facility or in a publicly-funded day care centre. The legal foundation for this in Germany is SGB VIII (Social Security Code, Book Eight), in accordance with which operating licences for day care centres are issued. Various other federal and state laws as well as ordinances and guidelines regulate the framework for the care of children. In principle, the federal states have legislative competence, unless the national Government exercises its legislative competence.

Childcare in Germany is provided by a variety of organisations. A distinction is generally made between public and independent institutions. Who can act as a public provider is determined by state law. These regional or even local institutions are mostly administrative districts (counties), non-county towns, cities with special status or even supra-regional institutions (the respective federal state). The independent institutions are differentiated as private non-profit and private commercial. Examples of private non-profit organisations are the German Red Cross, Arbeiterwohlfahrt, Caritas and other such bodies under civil law as well as associations and federations. Private non-profit institutions are, for example, either part of a company (company childcare facilities) or are independent private-commercial institutions.

Providers of children's day care facilities



In the context of childcare, a distinction is made between daycare facilities and domestic day care. Daycare facilities are general facilities in which children spend a certain amount of time during the day. Domestic day care takes place, in contrast, in the household of a child carer.

With regard to the deployment of personnel in daycare facilities, the minimum qualification required, which varies per federal state, is decisive. The management of a daycare centre is normally obliged to provide only one trained teaching specialist. The staff requirements calculated for such a facility is as follows: Qualified personnel ratio x mean duration of care plus 15.00% downtime (Example federal state of Hesse).

Example Hesse

Qualified personnel ratio	Average care
0.2 (Children 0 to 3 years)	22.5 Hours per week (up to 25 hours care)
0.07 (Children 3 years to school age)	30 Hours per week (25 to 35 hours of care)
0.06 (Schoolchildren)	42.5/50.0 hours per week (35 to 45/45+ hours of care)



04

FINANCING STRUCTURE
OF CHILDREN'S
DAYCARE FACILITIES

The (re-)financing structure of a children's daycare centre is in line with federal regulations, which are usually implemented at municipal level. Daycare centres can apply for subsidies for construction and equipment costs as well as operational personnel and material costs. All levels of local authority in Germany are responsible for these grants: federal, state, district, city/municipality. The prerequisite for a subsidy is of course a valid operating licence.

In addition to subsidies, there are also parental contributions/parental fees that complement the income side of a daycare centre. As the financing structure differs not only from state to state, but also from municipality to municipality, the following calculation is a sample calculation for the state of Hesse. This cannot be transferred one-to-one to other federal states, but it does show the typical general characteristics of the financing framework for daycare centres:

Building and fit-out support: €10,000 to €50,000

Operation costs: annual grants

A. State grants (from public funds):

1. Basic grant:

0-3 years (per child)	
up to 25 Hrs/Week	€2,070
25-35 Hrs/Week	€3,100
> 35 Hrs/Week	€4,130

3 years to school age (per child)	
Bis 25 Hrs/Week	€500
25-35 Hrs/Week	€660
> 35 Hrs/Week	€880

2. Quality grant (applies when operating to certain standards (in Hesse: Hessian education and childrearing plan): €300 p.a. per child)

3. Focused daycare grant (22% of children from families who are not German speakers): €390 p.a. per child

4. Integration-place grant (Integration of children with disabilities): up to €2,340 p.a. per child plus a fixed sum per degree of disability (€1,200 to €2,160 per child)

5. Small daycare centre grant (with only a single group): up to €5.500 p.a.

B. Parental contribution: to be paid privately; individual participation and cost contribution depending on the duration of care and age of the child and is regulated by the municipality and stepped locally depending on the parents income.



A child's playroom with a chalkboard, toys, and a yellow overlay. The chalkboard shows a drawing of a sun and a house. The room is filled with various toys, including a rocking horse, blocks, a ball, and a toy truck. A yellow circle is overlaid on the right side of the image, containing the number 05 and the title of the document.

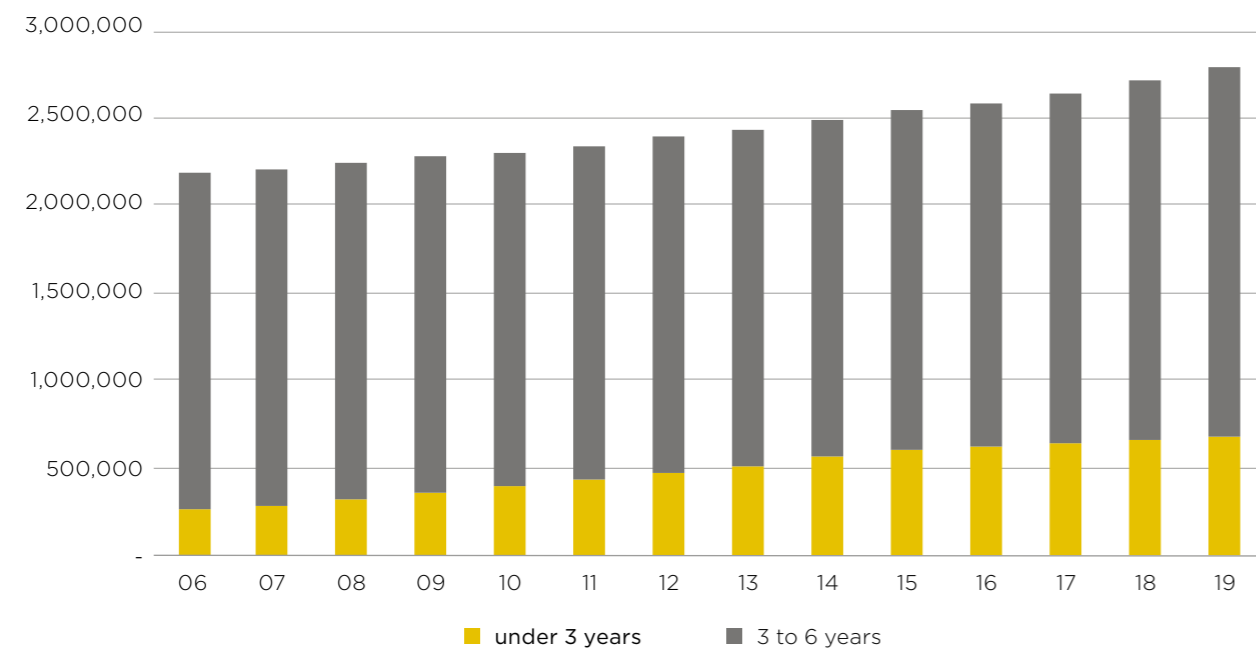
05

CHILD CARE
IN GERMANY - FACTS
AND FIGURES

Child day care and early childhood education are the foundation for equal opportunities for children and have long been the focus of political and public debate. In addition, good childcare is a prerequisite for many families to be able to combine work and family life. In recent years, the number of children between 0 and 6 years of age in day care has risen

continuously, and recorded an increase of 27% between 2006 and 2019. The number of children under 3 years of age in day care increased massively, by more than 170%, in the same period, while the number of children between 3 and 6 years of age rose by a modest 8.5%.

Development in the number of children in daycare

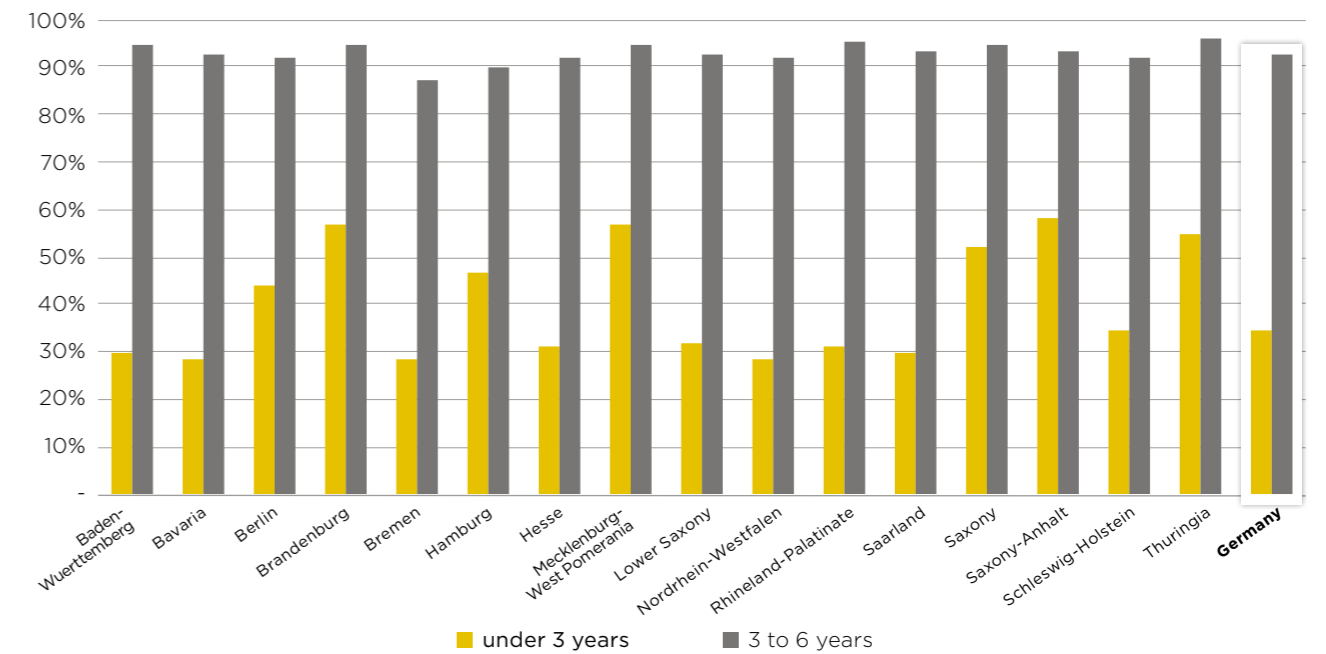


Statistisches Bundesamt, Cushman & Wakefield, 2020

The care rate has increased in recent years, rising by a further 6.8% percentage points between 2006 and 2018 and reaching around 93% by the end of 2019. Despite a strong convergence in recent years, regional differences between the eastern and western federal states are still evident. For example, the childcare rate for children between 3

and 6 years of age is similar in the eastern and western states, with 94.2% in the eastern states and 92.7% in the western states. Whereas a greater difference can be seen in the care of children between 0 and 3 years of age. The childcare rate in the east is 52.1%, and in the west is only 30.3%.

Proportion of children in daycare by age cohort and federal state 2019



Statistisches Bundesamt, Cushman & Wakefield, 2020



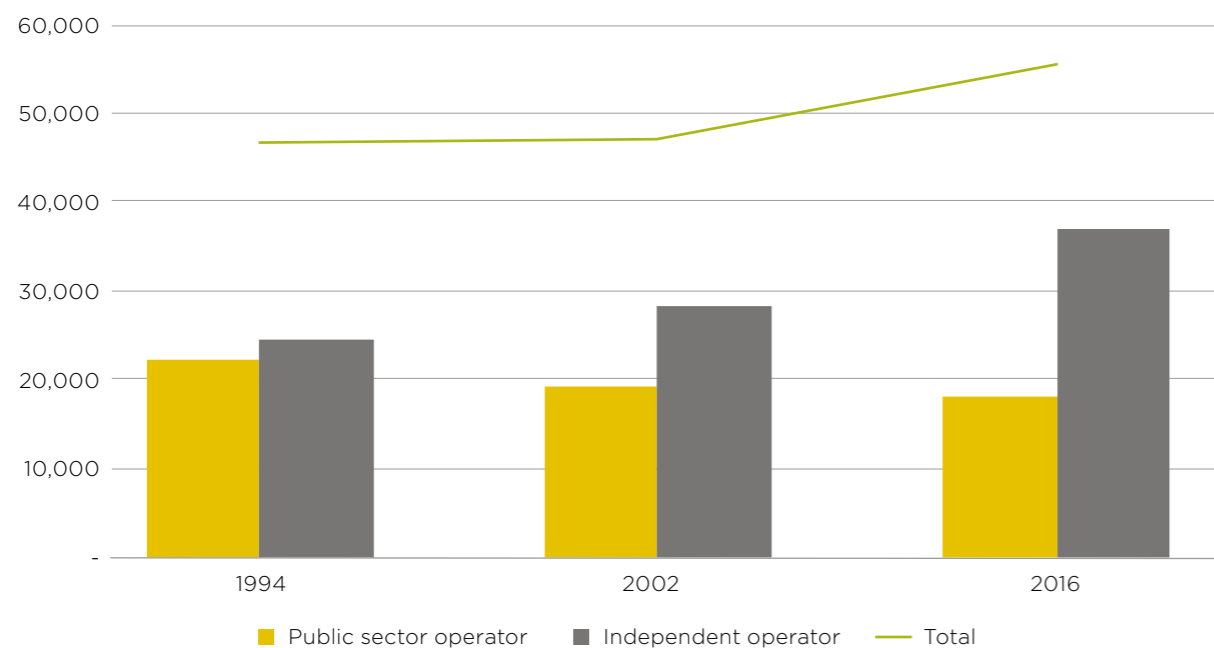
06

CHILD CARE
OPERATOR MARKET

Over the past 25 years, the number of childcare facilities has developed extremely positively - an increase that can be traced back to the Childcare Act of 2006. For example, the number of day-care centres in Germany has risen by almost 22% from around 46,600 in 1994 to around 56,700 in

2019. There was a particularly strong increase in the number of day-care centres run by independent organisations, which increased by 52% to approx. 37,000 in 2016, while the number of facilities run by public authorities declined by approx. 18%.

Number of children's daycare facilities

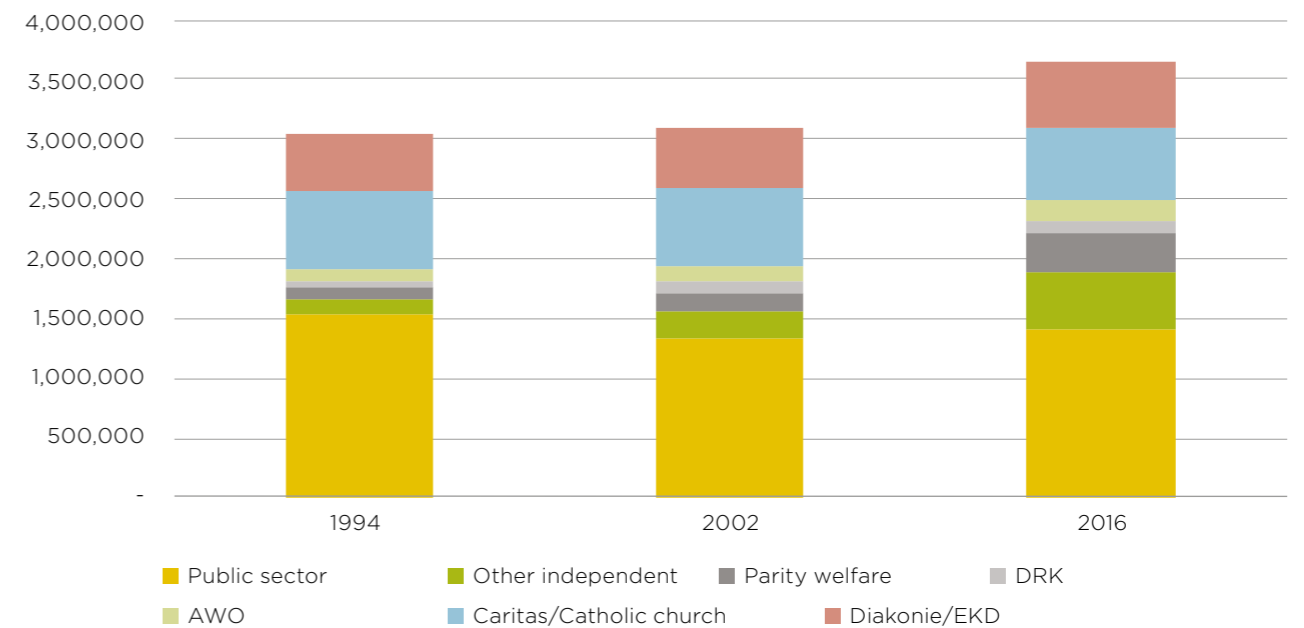


fowid, Cushman & Wakefield 2018

The largest independent operators include, for example, the Protestant Diakonie and the Catholic Caritas organisations, each with around 9,000 facilities. Both church institutions are still much more strongly represented in the old federal states of western Germany than in the new ones. Meanwhile, in 2018 almost 4,000 facilities were accounted for by the German Paritätische Wohlfahrtsverband, about 2,500 by the AWO and over 1,500 by the DRK. Other independent operators ran about 5,600 additional facilities. The rapid expansion of daycare facilities also includes to other independent institutions, most of which are organized as non-profit associations or as non-profit limited liability companies. Their share of the daycare provision rose

from around 122,000 places in 1994 to over 470,000 places in 2016. Without them, the growth in the number of daycare places in recent years would not have been possible. The private non-profit, non-mutual providers play a subordinate role, as they operate fewer than 1,700 day-care facilities and only have a market share of just under 5% among the independent providers. In 2019, just under 654,000 people were employed in day-care facilities, of which the public providers accounted for just under 220,000 and the independent providers for just under 434,000. This resulted in a considerably better care rate among the independent institutions than among the public institutions.

Number of places in children's daycare by operator



fowid, Cushman & Wakefield 2018

A child is sitting on a light-colored, textured carpet, playing with several wooden alphabet blocks. The child is wearing a white shirt with a small pattern and blue pants. The blocks are arranged in a row, with some letters visible like 'A', 'O', 'S', 'L', 'E', 'W', 'G', 'M'. A yellow circular graphic is overlaid on the right side of the image, containing the number '07' and the text 'CHILDREN'S DAYCARE FACILITIES AS REAL ESTATE'.

07

CHILDREN'S
DAYCARE FACILITIES
AS REAL ESTATE



As previously stated, childcare in a day care centre is provided by an independent or public institution as the operating company. From a property management point of view, it is usually this same operator who signs a general lease with the property owner. Such a lease is, in most cases, in line with the market, often indexed on the basis of the CPI, and structures the maintenance and repair costs as double or triple net. Due to the long-term planning horizon, long-term leases are also typical. This usually results in a relatively secure and long-term cash

flow for the property owner. Often day-care facilities for children are planned and built as part of a neighbourhood development. Complementary uses, such as residential, care facilities for the elderly and/or those in need of care due to illness, as well as conventional commercial and office uses, often come together with a children's daycare centre, to form an integrated neighbourhood for living, residing and working together.

With regard to the fit-out and structuring of such a facility, coordination with the

state-specific "Recommendations programme for rooms" is indispensable, as the granting of an operating licence is a prerequisite for opening a childcare facility. This applies in particular with regard to the room sizes. In addition to group rooms, a day care facility for children is usually characterised by retreat areas for children, kitchen and dining areas, cloakrooms, extensive corridors and separate personnel areas. Due to the high safety requirements for children, the use of special building materials (e.g. shatterproof glass) is just as important as child-friendly furniture, secured sockets and secured doors. Certification measures and TÜV technical standards agency tests are an essential component

and foundation for obtaining an operating licence. Fire safety is also one of the decisive factors in such a facility. Detailed regulations can be found in the state-specific building regulations and obtained from some accident insurance companies. The outdoor area is also of great importance due to the large number of outdoor activities. The size of the group with regard to the children depends on the respective age groups and is also regulated by the individual states (for example, in Hesse not more than 25 children). The opening hours are also regulated by the states.



08

INVESTMENT IN
CHILDREN'S DAYCARE
FACILITIES



On the real estate investment side, the market for day care centres is in its infancy. The daycare centres is an absolute niche asset class. Due to the fact that the public sector, despite regional demand and in particular due the legal right to care, is not building sufficient daycare facilities, parts of Germany have high new-build requirements. Due to the fact that the leases typically have a duration of 20 to 30 years, with financing mostly from the public sector or solvent independent bodies, the cash flow of this asset class is generally considered comparatively safe. The municipal or federal benefit obligations entail a relatively low risk of default by daycare centre operators making it an attractive investment product class for cash flow-driven investors.

Childcare facilities are increasingly developing into core investment products for institutional property investors. In principle, however, investment opportunities in day-care centres are relatively rare and investment volumes are also limited at property level. Purchase prices for day care centres are usually in the range of €750,000 to €5,000,000. Due to this granularity, it is not easy for investors to build a portfolio with an attractive lot size.

Net initial yields for this type of operator property are highly dependent on the locations of the individual properties, the creditworthiness of the operators and the structure of the general leases, and the sustainability of use as a daycare centre. And for core product, those yields range between 4.0% and 5.0%. Due to the significant intransparency of the fragmented operator market and limited investment market, there are however few meaningful figures on the annual Investment volume.



A bright, colorful children's playroom. The room features orange and yellow furniture, including a large cabinet and a table with chairs. There are various toys on shelves and the floor, such as dolls, books, and toy trucks. A yellow circular graphic overlay is positioned in the upper right corner, containing the number '09' and the text 'EXPERT INTERVIEWS'.

09

EXPERT INTERVIEWS



E&G Funds & Asset Management GmbH

Daniel Wolf

Head of Asset Management

Since when have you been involved with children's daycare centre as an asset class?

We already encountered the first children's daycare facility investments several years ago in the course of purchases of social real estate. We have been intensively involved in this asset class since 2017 and launched our first investment fund focusing on daycare facilities in 2018.

As a real-estate investor, what do you think is special about this type of property and what makes it attractive from your perspective?

The original idea of investing in daycare facilities arose from the desire to counteract the lack of supply of places. This is still the driving force behind every purchase. This class of property is particularly attractive for institutional investors with an increasing interest in the topic of "ESG".

The current market environment is correspondingly positive due to the high demand resulting from the legally established right

to a daycare place in conjunction with rising birth rates and an increasing need for support for investors. At the same time, the market has so far been tapped by very few professional market participants compared to other property asset classes. From an investor's point of view, daycare facilities are operator properties with particularly good refinancability of the rent, in some cases secured by the public sector. This attractive risk/return profile speaks for investments in this market.

In your opinion, has the perception of daycare centres as an investment opportunity changed in recent years?

Children's daycare centres are becoming increasingly important as a real estate class and are perceived by ever more market participants as an investment opportunity. Cities are also becoming increasingly aware that daycare centres represent a new asset class for investors, although much educational work still needs to be done in this area.

What is the biggest challenge in building a real estate portfolio in this asset class?

Currently, the small size of this asset class in combination with the few existing properties on the market represents one of the biggest hurdles. Possible investments are made more difficult by differences in refinancing of the owners and rising construction costs.

What does a "picture book" day care centre look like for you from an investor's point of view - in terms of the lease, operator, concept and the property from a structural point of view?

Sustainable demand at the location, experienced and renowned operator (municipal, independent or church institutions), long-term lease (double-net if possible), at least 4 groups, large outdoor facilities, spacious group rooms.

Do you see consolidation tendencies in the operator market?

So far only a few consolidations are visible. However, we expect increasing consolidation.

What are special features of this type of investment and how do you deal with the plethora of different municipal and federal different refinancing mechanisms?

The special feature of this asset class lies in finding a suitable property/project and to take all interests into account. For most transactions, a large number of municipal contacts need to be convinced (whether new building project planning or even takeover of an existing building); this can lead to very drawn-out decision-making. The various refinancing mechanisms make it generally difficult to penetrate the market, as the legal situation in the respective market always has to be analysed anew. We are always expanding our database in this respect and

have thereby gained good insight into the legislation. Also the ever increasing experience helps here.

What do you consider to be the greatest challenges/risks and opportunities which this segment will present in the future?

Challenges/ Risks:

- Lack of market transparency
- The small scale and fragmentation of the daycare centre real estate market
- Different local and federal refinancing mechanisms
- Further price increases due to rising construction costs with capped rent
- (e.g. NRW)
- In the long term, shortages of skilled workers could also become a problem from a real estate perspective

Opportunities:

- Consolidation of operators and professionalisation of the market
- Cooperation between real estate investors and cities/ municipalities
- Continued good market environment with regard to demand for daycare places
- Low default risk due to public refinancing of childcare facilities
- Low administrative costs with correct contractual terms

Where do you see a need for regulatory catch-up and adjustment?

With regard to refinancing, individual federal states and cities differ greatly, so that certain regions are scarcely competitive in comparison and have a lot of catching up to do.



AviaRent Invest AG

Sascia Hauke

Head of Transaction Management

Since when have you been involved with children's daycare centre as an asset class?

AviaRent entered the market at a very early stage and has been at the forefront of launching funds with a social and sustainable investment approach. The first funds with themes such as kindergartens, schools and care facilities were launched before other private investors had even discovered daycare centres as an asset class.

As a real-estate investor, what do you think is special about this type of property and what makes it attractive from your perspective?

On the one hand, a children's daycare centre usually has a long-term lease (20 to 30 years). In addition, it is usually based on a kind of "public sector rental cash flow". The rent is paid to the landlord either directly by the municipality or through an operator. Depending on the federal state or municipality, there are also various safeguarding mechanisms such as guarantee or warranty structures in the unlikely event that an



AviaRent Invest AG

Anahita Afzalkhani

Senior Transaction Manager

operator becomes insolvent. In addition to the cash flow, it is equally important for us as an investor to always consider the ethical and moral aspects of our investments. The education of children represents the future of the country and we would like to make a contribution by investing in safe facilities and create an appropriate space for this. By investing in day-care centres we support the modern family concept. Families are given the opportunity to provide optimal care for their children during working hours, which makes it much easier for them to return to working life.

In your opinion, has the perception of daycare centres as an investment opportunity changed in recent years?

Following the renewal of the Child Education Acts, the associated legal entitlement to a place in a day care centre and the targeted promotion of the expansion of day care centres by the federal government, daycare centre property has continued to develop as a new asset class. The expansion of the

daycare network was supported by the municipalities with the help of financial support and in many cases also by way of a model involving private investors. Over the last few years, the asset class has ever increasingly gained in popularity due to the secure and stable cash flows as well as a lack of comparable alternative properties. As a result, purchase price factors have risen steadily. This effect has been further enhanced by steadily increasing construction and land prices. We have seen purchases of new-build daycare centre real estate where, depending on the location and the terms of the lease, the multiples has exceeded 25 times the annual net rent in some instances. In our view a partly "unhealthy" development, as the risk/reward ratio is generally no longer correctly reflected. After all, even with this asset class, individual risks, such as future, demographic development have to be taken into account. It remains to be seen whether and how "Corona effects" influence the real estate market medium-term and possibly lead to minor price corrections.

What is the biggest challenge in building a real estate portfolio in this asset class?

Due to the high demand in the asset class and the already mentioned high purchase price factors, it is becoming increasingly difficult to find daycare centre properties that have an acceptable purchase price and at the same time fulfil the other important conditions regarding the quality of the property and the operator. However, AviaRent benefit here from our long-standing market presence and we are known to many sellers as a reliable and quick-to-act investor: Purchasing processes are completed in 4-6 weeks due to well-established processes with experienced consultants such as Taylor Wessing, GSK Stockmann, L+P Immobilienbewertungs GmbH, Soleo GmbH and Apertus Capital Partners.

What does a "picture book" day care centre look like for you from an investor's point of view - in terms of the lease, operator, concept and the property from a structural point of view?

A property with a 25- to 30-year lease, either with a medium-sized operator with a good educational concept and local establishment or a larger operator from the well-known charities, both municipal and city-based, with a solid classical structure without any expected excessive maintenance requirements, at best located in an established residential environment. A good interior design is also important, with beautiful wooden play and climbing structures, good kitchen and bathroom equipment, atmospherically pleasant sleeping places and a generous outdoor area.

Do you see consolidation tendencies in the operator market?

In addition to the classic, well-known charities, there are also private operators who already have numerous daycare centres in operation. In our view, however, local players with some facilities are also serious partners, who can make a difference through good educational concepts and good local networking with the Youth Welfare Office and local businesses.

What are special features of this type of investment and how do you deal with the plethora of different municipal and federal different refinancing mechanisms?

The regulations of the federal states differ with regard to rent levels and subsidies for the construction and expansion of daycare centres. With all the different models in the individual federal states, it ultimately depends on which rental cash model is acceptable to our fund as the lessor of the properties. The annual net rent should be almost completely covered by the subsidy rates of the federal states and any rent subsidies from individual municipalities. This results in a kind of "inner cycle of rent payments", even if the municipality is not itself the tenant of the property. In addition, some type of guarantee or guarantor liability by the municipality in the event that the operators, contrary to expectations, cannot pass on the rental payments.

What do you consider to be the greatest challenges/risks and opportunities which this segment will present in the future?

Sharp increases in construction and land costs have led to purchase prices at multiples on the annual net rent in some cases as high as the remaining term of the lease. Taking into account risks such as demographic development and the properties' suitability for use by third parties, it must be weighed up whether the asking prices do justice to the risk/opportunity ratio and then invest there. Even with the Coronavirus crisis, AviaRent is very solidly positioned to continue to act as a reliable and fast investor in concluding transactions, regardless of whether they involve an existing children's daycare centre or a new construction project.

Where do you see a need for regulatory catch-up and adjustment?

The previously-mentioned increase in construction and land costs are, in the main, not yet reflected in the level of state subsidies and thus nor in the rent levels. A corresponding increase in subsidies and rents would benefit the risk/opportunity ratio. Over the past few years many new daycare centres have been established in Germany. On the real estate side, a lot has been done. Reports from the operators indicate it is still very challenging, as we have repeatedly stated, to find sufficient good educators and other care staff for the facilities. The state should create, through good education and good staff pay levels, create the prerequisite for a functioning market in this area. In these investments we take on a responsibility for German education and the care for the smallest members of society.

About AviaRent:

AviaRent Invest AG, with its headquarters in Frankfurt am Main, Germany, is a subsidiary of AviaRent Capital Management S.à r.l., a Luxembourg-based fund management company. Together with its French partner Primonial, one of the leading European asset management platforms, with more than €23 billion in assets under management, AviaRent has a combined fund volume of more than €5.5 billion in the care, education and micro-living sectors. As a specialised asset manager, AviaRent invests exclusively in social infrastructure. AviaRent's portfolio consists of care properties with more than 5,200 care beds, 1,400 units of assisted living, day care centres with 2,000 places and 2,300 micro apartment units.

Further information can be found at: www.aviarent.lu



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CONTACT DETAILS & DISCLAIMER

Simon Jeschioro

International Partner

Head of Investment Advisory

+49 (0) 69 50 60 73 260

simon.jeschioro@cushwake.com

Jan-Bastian Knod

Associate

Investment Advisory

+49 (0) 69 50 60 73 261

jan-bastian.knod@cushwake.com



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