

The German office and residential developer's cautious approach to project management and funding have helped it to survive the downturn

Hochtief

The Marco Polo Tower at HafenCity Hamburg, a residential project developed by Hochtief Projektentwicklung (HTP) and DC Residential, won this year's MIPIM Award 2010. Though it was not surprising to find a Hochtief project among the winners, the company is more famous for its office developments than its residential schemes.

"Residential is not a new business area for HTP," explains Rainer Eichholz, chairman of Hochtief's real estate division and chairman of HTP. "But in 2009, we decided to increase the proportion of residential in our development portfolio. So today it is 22% of the total investment volume. One year ago it was only 12%."

This change in strategy, says Eichholz, is "a consequence of the changed demand by institutional investors, who are increasingly interested in blocks of flats as stable investments. In general, we develop classic blocks of flats or owner-occupied dwellings. With the Marco Polo Tower we entered the luxury sector."

The company's main focus, however, is on commercial property, and office buildings are its core business. "Some 55% of our investment is directed at office projects. Retail is another segment, but here we prefer inner-city locations or districts with mixed-use property assets. And two years ago, we started to develop health care properties, especially nursing homes," explains Eichholz.

The change in strategy is partly the result of HTP's expansion, but also the result of the changed investment climate since 2008. Developers and construction companies have found it more difficult to operate profitably. Hochtief Real Estate's construction pipeline has been decreasing steadily – from €1.04bn in 2007 to €744.1m in 2008 and to €642m in 2009.

Hochtief, known as a leading international construction corporation, was established by Balthasar and Philip Helfmann in

Frankfurt in 1873. One of its first large projects was the construction of the University of Gießen, a provincial city north of Frankfurt.

It was Philip Helfmann who converted the provincial company Helfmann Brothers into a joint stock company under the name Aktiengesellschaft für Hoch- und Tiefbauten (since 1923 its name has been Hochtief Aktiengesellschaft) and started to expand the business outside the Frankfurt region.

Home office in Essen

In 1922 the company's head office was transferred to Essen, where it remains today. In the 137 years since its inception, Hochtief has become a global provider of construction and construction-related services and offers development and construction services as well as specialist real estate, such as PPP projects. In 2009 the firm's consolidated net profit was €195.2m, up from 2008's profit of €156.8m.

With the enlargement of its range of services, Hochtief's structure has become increasingly sophisticated. Today it has six corporate divisions: three geographical divisions, Hochtief Americas, Hochtief Asia Pacific and Hochtief Europe, which are mainly responsible for construction and engineering; and Hochtief Concessions, Hochtief Real Estate and Hochtief Services.

Hochtief Services comprises Hochtief Facility Management and Hochtief Energy Management. Hochtief Concessions' business areas include airports, roads, social infrastructure and public-private partnership projects.

The company's portfolio, which has a total value of around €1.6bn (2008: €1.47bn) comprises six airport holdings, seven roads, 92 schools, two town halls, a community centre, a military base, two geothermal energy projects and two investment partnerships.

Catella

Parent company Ikea is to sell off Stockholm-based Catella, which has reported positive first-quarter results

Hochtief Real Estate is the division that focuses on property issues. It is divided into Hochtief Projektentwicklung (Hochtief Project Development, HTP) and Hochtief Property Management, as well as a 50% share in Aurelis Real Estate. Hochtief Real Estate develops and markets real estate projects and also offers general support and management services for these properties.

Hochtief Property Management, founded in 2007, manages around 42m m², of which around 10m m² are managed buildings.

In 2009, the Hochtief Real Estate division's profit before taxes totalled €27m (2008: €31.6m). Operating earnings were €53.2m (2008: €59.2m). During last year, Hochtief generated around €880m from planned sales in the Hochtief Real Estate division.

Because the investment market in the first half of 2009 was nearly dead and started to recover only slowly in the second half, this is a creditable result.

For Eichholz, however, it is the result of "a traditionally conservative strategy that did not favour highly leveraged development clients". Today, it is to HTP's advantage that it "did not neglect the traditional investors with high equity", he says. And he is proud when he states that more than a third of HTP's investors have worked with it on more than one occasion.

An international scope

Although most of the firm's properties, projects and land are in Germany, Hochtief Project Development is also internationally active. About 20% of the total investment volume is allotted to projects in central and eastern European countries, mainly in the capitals of Hungary, the Czech Republic and Poland. "All projects that HTP has already started in the CEE region, when the financial crisis became virulent, had already found an investor," says Eichholz.

In this context, Hochtief's more conservative approach to project development has helped it to avoid being hit by falling values. But Hochtief itself is also conservative when it comes to financing its project development. "HTP's principles have always included an

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Rainer Eichholz, Hochtief Real Estate

insistence on a reasonable debt-to-equity ratio and a quite high level of prelets. These principles have proved their worth over the past few years, especially during the financial crisis," says Eichholz.

"Given the changed conditions in the financial market today, we assume a debt-to-equity ratio of 40% and an average preletting rate of 50% before we start the development process," he explains. The company also aims, he says, to "co-operate with institutional investors and to involve them more as strategic partners".

Although the company's development pipeline is shrinking, this could be the result of the company's conservative principles, Eichholz says. "HTP is a classic trade-developer. We buy land plots, we take care of the planning and building permissions, we choose the architectural design and after we find the future user we start with the physical realisation of the project. At the same time, we offer the project on the investment market and try to sell it at a very early stage."

"In this way we regulate the order inflow. We are not dependent on orders from third parties," explains Eichholz. "What is shown as orders on the balance sheet are projects we have already logged in. What we have in the pipeline is much more. We keep the number of orders deliberately

lower than they were during the past few years. Thus we avoid the predicament of other market participants, who have to fear devaluations of their highly valued assets in their balance sheets."

Another of Hochtief's principles has proved its value: its focus on sustainability. It was not until 2005-06 that the theme finally arrived on the Continent and was the talk of the market. But way back in 2000, Hochtief committed itself to the principle. An example is the WestendDuo in Frankfurt, two office towers totalling 32,700 m² that HTP completed in 2006 and a year later were purchased by ING Real Estate.

Although the focus was always on the fact that WestendDuo is a low-energy building, Eichholz explains that "sustainability is more than energy saving".

"Developing a sustainable building starts with the first concept of a project and has to take into consideration the whole life cycle of a project – from the first idea or plan and financing, through to construction and later operation and possible refurbishment and redevelopment," he explains.

So perhaps it was to be expected that in 2007 Hochtief was one of the founding board members of the German Council for Sustainable Building (DGNB).

The real estate business always presents challenges – especially today, as the market emerges from a severe slump. "With the successful disposals at the end of last year and the high rate of prelets of our projects, we feel well prepared for a difficult market environment. We assume a continuing recovery of the investment markets, but we are well aware that the office rental markets will remain stagnant," says Eichholz.

"However, office real estate will still be our core business because markets need sustainable buildings of high quality. We are confident that the demand for services such as tenant services and asset management will increase. So we expect property management to gain in importance."

Consolidated earnings (€, '000)		
Item	2009	2008
Sales	18,166,081	18,703,135
Changes in inventories	32,203	399,417
Other operating income	225,107	375,889
Materials	-12,562,542	-14,273,373
Personnel costs	-3,501,085	-3,265,768
Depreciation/amortization	-501,370	-392,306
Other operating expenses	-1,333,123	-1,259,676
Operating profit	525,271	287,318
Profit after taxes	408,169	323,882
Of which consolidated net profit	195,222	156,744

Source: Hochtief