

**"A long-term, internationally competitive investment"**

*Germany's federal association for investment and asset management, BVI, has put its proposals for the reform of open-end real estate funds on the table – but how is the sector reacting? Places & spaces – the real estate magazine of DIFA Deutsche Immobilien Fonds AG - spoke with DIFA board member Reinhard Kutscher*

**Places & spaces:** What do the reform proposals mean for investors – will open-end real estate funds remain an attractive option?

**Reinhard Kutscher:** Yes. The reform proposals are aimed at keeping open-end real estate funds as a long-term form of investment more competitive internationally. In so doing, investor protection plays an important role. At the heart of the reforms are suggestions that will lead to improved transparency of the product, and create the basis for optimal cash management. It's also important that institutional money be separated from private money. Large-scale institutional investors react more quickly to changes in the funds arena than private investors. Separation of these two client groups creates more security for the private investor.

**Places & spaces:** But why should the minimum liquidity amount be doubled, as has been suggested?

**Kutscher:** This reform proposal also serves to increase the security of the investment. It's supposed to help create greater manoeuvrable reserves for the shifting of funds.

**Places & spaces:** Some funds are restricted to investing only within the EU. Isn't it about time, in the framework of these new regulations, to create a unified legal foundation?

**Kutscher:** As a matter of principle, the same markets should be open for everyone. According to the fund's profile and the investment strategy though, there are funds that deliberately invest only in certain countries, like Germany for example. The important thing is that this is made clear to investors so that when they're making their decisions, they have a clear understanding of the risk profile of the individual fund.

**Places & spaces:** Real estate funds should soon be allowed to also invest in REITs or in real estate stocks. What are the advantages of this?

**Kutscher:** To remain internationally competitive as an asset class, companies are being given a higher degree of flexibility with regard to their investment options. Participation in real estate stocks would allow companies to benefit from promising markets in a way that would be difficult for individual funds. Aside from this, investments in REITs also help build up a sort of liquidity buffer, since they can be sold quickly on the market on a daily basis.

**Places & spaces:** Doesn't this distort the profile of the property fund?

**Kutscher:** It's certainly true that REITs, like stocks, are much more volatile than property funds. Value fluctuations of 20 percent within a short period wouldn't be unusual. But it's the job of fund managers to ensure that overall value stability of their open-end funds is not affected by this. The amount of investment in REITs would therefore be limited according to the individual risk profile of the fund, and could serve simply to add diversity. And within the share allocation, there can also be risk-diversification. An interesting alternative there would be real estate stock funds.

**Places & spaces:** Transactions between the funds of a particular provider is also meant to become possible in Germany in the future.

**Kutscher:** This possibility should only be used in exceptional cases. But a constellation could arise in which a transaction within a company could be interesting for the investors in both the funds involved. For example, if the fund that's selling needs more liquidity, the fund that's purchasing needs to lose liquidity, and the property meets the search criteria but is difficult to find on the market. If legislators follow this suggestion, certain precautions will need to be made. We will push for the best possible checks on such transactions, in order to protect the interests of the investors in both funds.

**Places & spaces:** There are still questions surrounding market-driven valuations. Is this something the reforms will address?

**Kutscher:** The discussion has centred on the valuation process itself, and providing results that are in line with the market. The proposals are aimed at making the objectivity of the valuation process even clearer. Independent appraisers should be able to work for a company for a maximum of five years. In addition to this, the sector is demanding twice yearly check-ups on a property's valuation. That should help keep valuations better in line with the market. Additionally, we've long been aware of the necessity of relying on the expertise of local property experts when it comes to foreign purchases. Every time DIFA buys a property abroad, we safeguard the appraiser's verdict through a third, local valuation. This process is in line with the BVI proposals.

**Places & spaces:** When will the reforms come into effect?

**Kutscher:** It'll happen quite quickly. Everything that doesn't require any legal changes should come into effect on April 1. Things where legislation is needed, for example with investments in REITs or the withdrawal notice for institutional investors, will of course be dependent on the legislative process.

**Places & spaces:** How will you be preparing your own funds?

**Kutscher:** For the DIFA-Fonds Nr. 1, we'll continue with the portfolio regrouping we've already begun, and divest it of smaller, older properties. With DIFA-Global, we're planning to enter markets that are not yet the focus of the big international investors. Those markets could include Turkey, Mexico or South Korea, for example. In 2006, DIFA-GRUND will continue to focus its investments on classic markets in Europe and North America, although here, the strong rise in prices mean that we'll proceed selectively and look for properties that promise especially good returns.

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