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Talking Point

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No longer “poor, but sexy“

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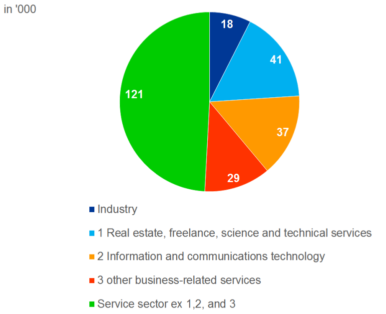
Berlin found it difficult to adapt to the market economy after Germany’s re-unification. Both parts of the divided city, the eastern and the western, had to cope with fundamental changes – the eastern for obvious reasons, the western because it had benefited from generous subsidies until then. Berlin has therefore been lagging behind the rest of western Germany for decades. By now, however, it is not only catching up with western German metropolitan areas, but even beginning to overtake them. Employment growth in cutting-edge industries suggests that Berlin is truly becoming an innovation hub. And this development serves as an excellent basis for the residential market. While we mainly focus on developments in 2018 in this article, the house price trends are likely to remain in place for some time to come.

In 2018, prices for existing terraced houses in Berlin rose by 14% yoy and climbed to a new all-time high, at considerably above EUR 300,000. Despite this jump, which considerably exceeded the uptrend in most other major metropolitan areas in Germany, house prices in Berlin are still relatively low. In fact, terraced houses in major cities (“A cities”) in western Germany currently cost c. 50% more than in Berlin. Back in 2009, the difference was only 30%, and in the 1990s, prices were still largely similar. Prices for new terraced houses rose considerably as well, namely by more than 10% yoy, whereas prices for single-family homes were up by “only” 5%. Single-family homes in Berlin are just about half as expensive as in western German metropolitan areas. Apartment prices underwent a similar development. Prices for existing apartments rose by more than 15% and those for new apartments by more than 10%. According to bulwiengesa, Berlin is currently the 11th most expensive German city in terms of apartment prices (up from rank 15), and according to Numbeo, it is the twentieth most expensive city in Europe, with square metre prices outside the city centre amounting to EUR 3,600.

In Berlin, too, the price increases are caused by a significant shortage of available housing. Many observers believe that the lack of available construction plots is one of the main reasons for this. However, qualified labour is in short supply as well, not only in Berlin, but also in other cities. According to the Berlin statistical office, the number of workers in the construction sector declined slightly in year-on-year terms between January and September 2018. At the same time, the number of hours worked rose by almost 5%. In 2017 (latest available figures), only 15,700 residential units were completed, i.e. 0.8% of the total number of existing homes. Bearing in mind the increase in hours worked, the number of completions probably rose to more than 16,000 residential units or 0.9% of existing homes in 2018. However, this is only a fraction of what is required as the population grows.

Between 2011 and 2017 (latest available figures), Berlin's population increased by nearly 290,000 and the number of households by almost 200,000. Robust demand is not least due to the favourable labour market development. Employment growth amounted to c. 4% in both 2016 and 2017 and probably continued at that pace in 2018. Since 2009, employment has increased by more than 30% in accumulated terms. In line with this, unemployment has been declining for years and fell to 7.6% in November 2018. Berlin's labour market is normalising in comparison to that in other German cities. A look at the historical figures shows just how impressive the development is. In 2003, the unemployment rate was still above 20%.

2013-2018: More than +200.000 jobs added in the service sector



Sources: Federal Labour Office, Deutsche Bank Research

A sector analysis yields additional, interesting insights into Berlin's labour market. Manufacturing traditionally is an important sector in Germany, with one out of four jobs that are subject to social security contributions being found in this industry. However, it plays only a subordinated role in Berlin, where only one out of eight employees with a job that is subject to social security contributions works in manufacturing. Employment growth mainly took place in the services sector, where more than 200,000 jobs were newly created between 2013 and 2018. This figure is above the total number of manufacturing jobs subject to social security contributions. Almost half of these new jobs were created in three services sectors only (WZ2008): first, professional, scientific and technical services, which include real-estate services; second, other business services; and third, the information and communications sector, which has registered the strongest growth rate since 2013 (more than 50%). Berlin has clearly positioned itself as a start-up hub. According to figures prepared by the city of Berlin, more than 500 digital companies were newly established in 2017, i.e. more than in Hamburg, Munich and Frankfurt taken together. In addition, one out of ten digital companies is founded in Berlin.[1] As a result, the share of university graduates among those who hold a job that is subject to social security contributions has increased by more than 5 pp between 2013 and 2018, to more than 26%. Employment growth in knowledge-based and future-oriented sectors points to sustainable growth. It would therefore not come as a surprise if the Berlin labour market not only caught up with the labour markets in western German large cities, but even overtook them.

This trend has already had a favourable effect on Berlin's budget. Between 2014 and 2018, public-sector spending increased by c. EUR 5 bn, to EUR 28.6 bn. At the same time, social security expenditure (i.e. spending by social and youth services) declined by EUR 1.5 bn, and their share in total expenditure was down from 28% to 24%. Investment and public-sector construction spending increased by almost EUR 1 bn during this period. Moreover, Berlin reduced its public-sector debt from more than EUR 60 bn in 2012 to less than EUR 55 bn in 2018. Further structural debt and fiscal improvements are likely as the real estate and economic boom continues, particularly as the population continues to rise. More than 260,000 people are expected to move to Berlin until 2030. For years to come, a steady rise in demand for housing will meet with relatively inelastic supply. As the ownership rate is particularly low in Berlin (15.6% according to the census of 2011, compared to more than 20% in other metropolitan areas and 45.9% in Germany as a whole), many tenants may want to acquire their own homes, even though rent growth has slowed significantly, at least for existing apartments. The annual rate of increase dropped from 7% in 2016 and a peak at 11% in 2017 to only 3% in 2018. Apart from the slowdown in rent growth, numerous factors point to a super-cycle in Berlin, which might continue far beyond 2020. Housing in Berlin might thus contribute to a trend which will make Berlin one of the most expensive German and European cities, just as the city is becoming one of the most innovative, too. Berlin is no longer "poor, but sexy", as its former mayor Wowereit famously said in 2003. Rather, it might soon be "rich and innovative".

[1] "Gründungsdynamik in der Berliner Digitalwirtschaft nimmt weiter zu", press release by the city of Berlin, 12 December 2018.

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