

Above the average

Real estate has been blamed for triggering the 2007-2009 crisis. However, Switzerland, notably in commercial and office real estate, remains unaffected. Markus Graf, CEO of Swiss Prime Site, gives a few reasons

BY CYRIL DEMARIA

Swiss Prime Site is a listed company focusing on real estate (business and commercial). How are financial markets dealing with stocks in real estate at the moment?

>**Markus Graf:** Over the course of the 11 years following Swiss Prime Site's initial public offering (IPO) in April 2000, real estate stocks have established a foothold in Switzerland. In 2000, only about one-eighth of Swiss pension fund assets were allocated to real estate investments, while today estimates are close to one-fifth. In the same period, the share of real estate stocks and funds rose from 15% of real estate investments to 40%. Listed real estate shares are increasingly integrated into portfolios: together, Swiss Prime Site, PSP Swiss Property and Allreal have currently a free float market weight of 80% of all Swiss real estate shares. On a monthly basis since 2000, correlation of the SXI Real Estate Shares with the Swiss Performance Index has been 0.53 – a much lower correlation than in other countries – due to their relatively low correlation to other asset classes, such as bonds or commodities. Real estate investment companies generate steady, attractive cash flows and promise significant stability in value. As the leading listed real estate investment company in Switzerland, we think that we are particularly well positioned to benefit from this trend. Swiss Prime Site (SIX: SPSN) is probably the most liquid real estate stock in Switzerland.

Switzerland has been spared most of the crisis related to real estate worldwide (admittedly this crisis was largely related to the housing market, where Swiss Prime Site is not active). How do you explain this? Do you think that the real



Markus Graf, CEO of Swiss Prime Site

estate bubble still has room to further deflate, as is the case with Spain or France? The situation in Switzerland is not comparable with that in Spain or France. There are no signs of an overall real estate crisis in Switzerland because the local market has generally been spared from excesses. Most of the banks and investors learned lessons from the real estate crisis of the 1990s, and have acted sensibly ever since in Switzerland. Take Spain, for example: construction groups produced gigantic residential building complexes – and often entire neighbourhoods – in alliance with local government officials with the

hope that these units would find a buyer. In 2006, roughly 600,000 residential units were built. With the financial and economic crisis, however, property sales suffered a severe decrease. Construction companies were left with a vast number of unsold real estate units. Speculative production does not exist in Switzerland: new residential units are easily absorbed by the market. The Swiss residential housing segment is supported by low interest rates. Net migration inflows, as well as the growing need for floor space and comfort, also fuel the demand. The commercial real estate sector benefits from the

fact that Switzerland suffered far less than other countries from the last global economic crisis. The sector has found its way back to growth more rapidly too.

The Prime Tower and other buildings have been criticised for their architecture and visual impact. Increasingly, the population is reluctantly accepting transparency and cold materials. In a nutshell, the public is tired of the concrete/glass dictate. What is your response to this feedback?

On the contrary, we have experienced just the opposite with the Prime Tower. Some people took a sceptical stance toward the project at the very outset. Today, we are receiving compliments from all sides just a few months ahead of the opening. The unique aesthetic is being noticed, as explicitly conveyed by the distinctive octagon-shaped layout that expands as it extends upward, in contrast to common architectural standards and static norms. The greenish façade – which seems to change colour, depending on the perspective and time of day – does not leave the impression of being cold or repelling at all. Incidentally, the building is constructed with a triple layer of insulated glass and fulfills the criteria for LEED certification, which Prime Tower is proud to have received.

The oldest buildings in Zurich date back to the end of the fifteenth century and look almost new. Comparatively, concrete buildings of the 1960s and 1970s are not only looking old but age fast. What will remain of the buildings of today in 100 years, according to you? How do you deal with an architectural culture that is no longer 'built to last'?

Indeed, mistakes were actually made in the 1960s and 1970s, when concrete buildings first emerged. Builders paid too little attention to structural physics, which led to problems with insulation and soundproofing, as well as moisture-related damage and signs of premature aging. Today, the use of concrete has been improved. Its static, plastic, atmospheric and aesthetic characteristics have become indispensable in contemporary architecture. Given proper maintenance, most of the buildings constructed today should still be standing in 100 years.

A few industries – such as fine art dealing,

gems and jewellery trading, retailing and construction – have been subject to criticism as potential sources of money laundering and corruption. How does your company address these issues?

We have no information regarding any misuse of our stock in money-laundering activities. As a Swiss publicly listed corporation, we rigorously comply with all the relevant laws and regulations that such companies are subject to. Moreover, we know the names of all of our shareholders because we have registered shares.

Can you give more details about how specifically and in your day-to-day activities SPS is using procedures and guarding against corruption and anti-money laundering activities?

The Swiss real estate market is, in fact, small and manageable by international comparison. We know our business partners, especially the buyers and sellers of properties. Profound market know-how and transparency are the most significant and effective elements to steer clear of possible illegal business practices. Furthermore, our Audit Committee has the responsibility of supervising the management with respect to financial reporting, compliance with legislation, requirements, internal rules and guidelines, as well as risk management and monitoring external corporate activities. Swiss Prime Site also boasts an internal control system that regulates the management of various risks. Among the risks to be avoided are reputation-related risks, in particular, which would arise when conducting business activities with dubious partners.

Switzerland offers few sites to establish major buildings. How do you address this scarcity of locations? What are your next projects? Where is the most pressing need (geographically and business-wise)?

We counter the lack of appropriate properties and locations by investing increasingly in the project development business – an area where we have many years of extensive experience. We can mention a few examples: the construction of the Meseturm in Basel, the commercial building complex Opus in Zug, Prime Tower and annex buildings situated on the Maag site in Zurich West, or the recent development project of the SkyKey commercial

building in Zurich North. We continue to anticipate the greatest momentum in the major economic regions of Switzerland, primarily in Zurich, Basel and Geneva. These regions are the focal points of our real estate investments. The Zurich region accounts for roughly 40% of the Swiss Prime Site portfolio, on a fair-value basis. Geneva and Basel make up around 20%, respectively. In terms of utilisation, we believe that we are well positioned with a 40% share of retail properties and approximately 36% share of office properties.

Equity Office Properties was one of the largest ever Leveraged Buyouts (LBOs) in the US undertaken by Blackstone. How do you see these operations? Is there a consolidation expected in the real estate sector in Switzerland as well?

Such a transaction is inconceivable in Switzerland: first, due to the size – amounting to US\$ 39 billion at that time, if I recall correctly. By comparison, our portfolio amounts to CHF8 billion. Another reason this is inconceivable in Switzerland is because Swiss banks would not participate in an operation with such financial leverage. The cautious stance taken by Swiss banks in lending activities has had an impact on leverage buyers in the past: they tried their luck and then exited the market. Investors can always expect to realise a net return of just roughly 5% on the Swiss real estate market, which seems to be much too little in the eyes of many. Such investors were lured by the high returns in the US, Great Britain or Spain – and they lost a lot of money. +

MARKUS GRAF

Function: CEO Swiss Prime Site and Head of Real Estate Asset Management Switzerland at Credit Suisse

Age: 61

Domicile: Feldbrunnen/SO

Family: Married, three children

Education: Dipl. Architect HTL/STV

Professional background: After holding management positions at several construction and real estate companies, Markus Graf assumed his managing role (Managing Director) at Credit Suisse AG, Real Estate Asset Management, Zurich, in 1995. Since 1 December 2000, he has held the position of Chief Executive Officer of Swiss Prime Site.