# PERE

# Value Creation & Asset Management

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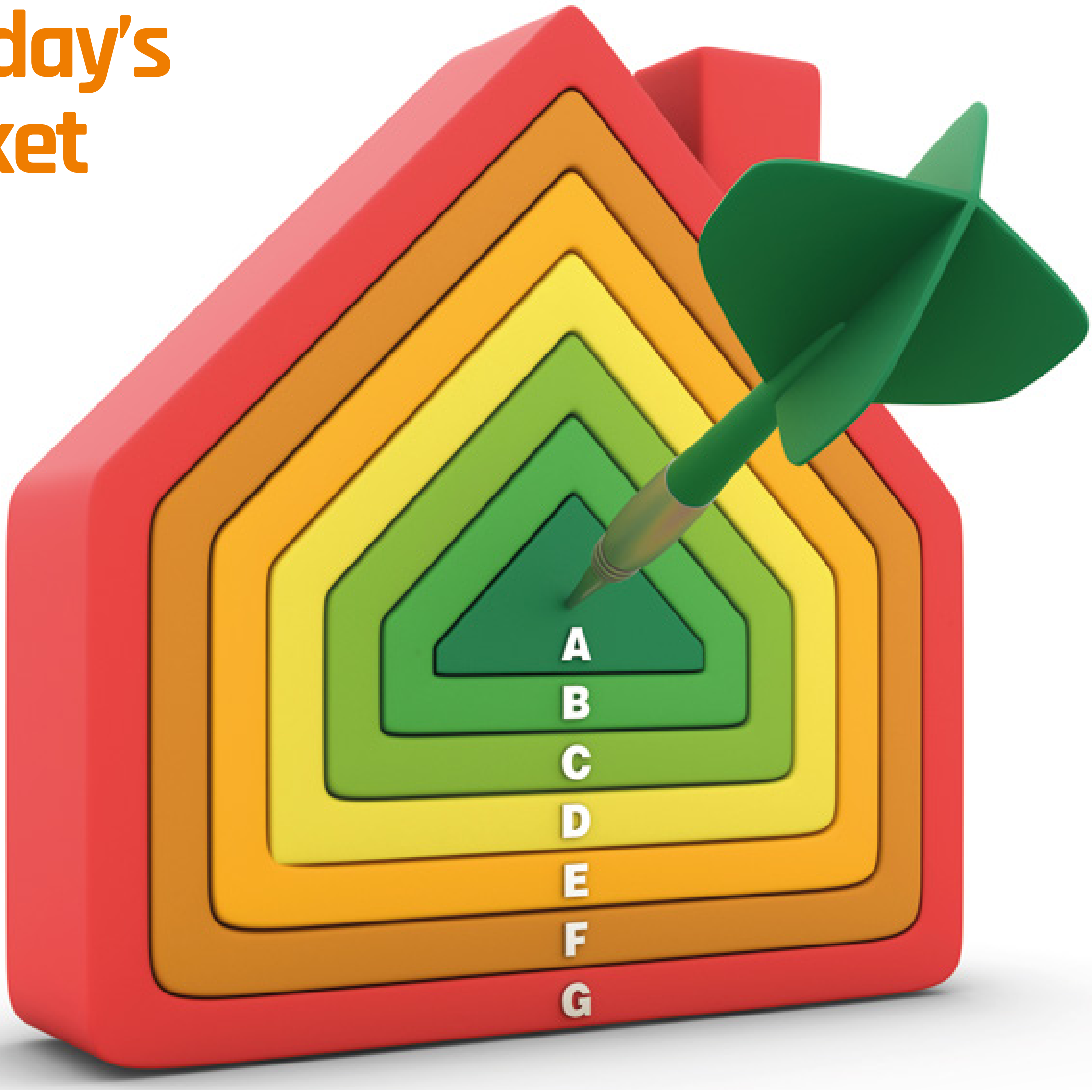
## Creating value in today's market

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KEYNOTE INTERVIEW

# Creating value through active management in Germany

*Current market dynamics offer the opportunity to acquire 'special sits,' assets at attractive yields-on-cost, says Arrow Global's Stefano Giardina*

In the current market environment of limited dealflow and investor appetite, active asset management is widely being seen as a crucial play to enhance returns, particularly within a value-add strategy.

Stefano Giardina, managing director, real estate, and chief investment officer of Arrow Germany, says there are investment opportunities to be found in special situations and high-yielding assets, particularly in Germany. However, he emphasizes that robust underwriting and strategic capex investment are essential to unlocking value in such transactions.

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**Q What is the current investor appetite for value-add strategies?**

Investors like us are seeking special situations where price imbalances or discrepancies create opportunities. Asset managers that have the expertise to understand whether an opportunity exists because they have the full power of the local platforms behind them can build an investment case and achieve risk-adjusted returns for their investors.

For example, we recently acquired a stranded asset in Munich, Germany, where the shell and core of the building had been constructed but never completed as the previous developer went into insolvency. The expertise of Arrow Germany allowed us to confidently execute the transaction.

**Q What investment opportunities are drawing the most attention in Germany today?**

Right now, special situation deals are attracting significant interest in Germany for several reasons. Recently, the country experienced an extended period of cheap debt where the 10-year German Bund recorded negative yields, which led many developers to take on excessive leverage. As interest rates rose, some were unable to service their debt, resulting in many situations of assets being stranded.

We are seeing many such distressed situations, albeit on a granular basis. For example, in June 2024, we acquired the operating platform and assets of a long-standing, family-owned German developer, Interboden, after the company became financially insolvent. We purchased the platform through insolvency proceedings and, with our own team, took over most of the assets.

This allowed us to assist banks in restoring value, repositioning the projects and ultimately unlocking their full potential. With a current GDV exceeding €500 million and a team of more than 60 staff, Interboden strengthens Arrow's ability to source granular opportunities under €50 million directly within the market.

Furthermore, Germany's insolvency process is particularly transparent and efficient, which has created a rare window of opportunity. Many nearly completed projects are now available at steep discounts, sometimes 30-80 percent off capital cost, making them highly attractive for special situation strategies. By moving quickly and leveraging the expertise of our local teams, we can act decisively on these opportunities.

Additionally, while stranded assets remain a key focus, we are also evaluating high-yielding opportunities in sectors such as student housing, logistics and convenience retail. The distress we are seeing is not just in traditional residential or office assets but across multiple asset classes, where liquidity constraints are forcing owners and/or banks to offload properties at significant discounts.

**Q What kind of risk-adjusted returns are investors expecting from a value-add strategy in Europe today? How has this changed given the lack of deals in the current market environment?**

Investors' expectations have changed due to reduced capital availability and fewer active investors pursuing opportunities.

The returns we are expecting are higher than pre-covid levels. Investors now typically seek internal rates of return between 15 and 25 percent, depending on the specific investment opportunities and related risk profile.

**Q What factors should stakeholders consider while underwriting and originating value-add deals in Germany?**

There are several considerations that we look at in our underwriting. ESG is very important – having a clear plan for improving sustainability can significantly enhance value. While Germany is culturally more advanced in topics evolving around green buildings, asset managers can definitely add value by going the extra mile.

For example, buildings can be connected to district heating, upgraded with energy-efficient heating and cooling systems, fitted with photovoltaic panels or transitioned to LED lighting. These enhancements strengthen an ESG case, attract tenants, improve building efficiency and reduce operating costs – ultimately increasing liquidity at exit and making it easier to secure financing.

Beyond ESG, capex investment is key, particularly when dealing with stranded assets or operationally working buildings where previous busted capital structures limited improvements. In such cases, one would have to incur what I call defensive capex and accretive capex.

Defensive capex is what you spend to ensure the asset remains modern and resilient. While it may not generate direct income, it stabilizes the property and can lead to a better exit cap rate by enhancing durability and sustainability.

On the other hand, accretive capex brings additional rental income. For instance, in a shopping center, tenant incentives and fit-out contributions should be strategically balanced against expected rental income to maximize returns.

And, last but not the least, underwriting must ensure that rent levels are sustainable and have growth potential, securing long-term value creation.

**Q What are the leasing dynamics in Germany currently, and how does it differ from other European markets?**

In general, German retail assets previously had standard 10-year leases, but this has become increasingly rare. Today, lease terms are typically around five years, often at more affordable rent levels compared to markets like Italy, for example, where leases tend to have shorter durations.

Another key difference is Germany's strong focus on green aspects of the buildings. Tenants are more attuned to a building's sustainability credentials than in many other European markets, particularly those in Southern Europe. For example, tenants consider very positively if a property has solar panels or if at least 30 percent of its energy comes from renewable sources.

There is also significant potential to convert brown buildings into green buildings in Germany. This transformation is a key focus in our underwriting and due diligence process. Green buildings not only make it easier to secure debt, since banks prioritize ESG compliance, but also enhance liquidity at exit, as investors increasingly factor in energy efficiency and other sustainability metrics.

We also see notable resilience in the retail sector, particularly in convenience-led retail centers that maintained high traffic during covid. Many of these assets have undergone rent resets, making them more attractive to tenants while also creating strong rental growth potential for investors. Given high replacement costs, few competing assets are being developed, further strengthening the sector's fundamentals. This is an area we are actively monitoring as part of our broader strategy.

**Q How can investors balance capex requirements with return expectations when they are underwriting value-add deals?**

The balance between capex and return expectations largely depends on the level of risk involved. Ground-up developments carry higher risks, requiring higher returns to justify the investment.

In contrast, stranded assets that only need, for example, improvements to the roof, facade and interiors involve significantly lower development risk. Since the structural foundation is already in place, investors can focus on optimizing the asset rather than managing full-scale construction uncertainty.

**Q What role does active management play in achieving these returns in a value-add strategy?**

Active asset management is essential. As a rule of thumb, when you make an investment, half of the value is created at acquisition, while the other half comes from asset management and value-add initiatives.

In the residential sector, value-add strategies start from the construction phase. Active management is both a skill and an art – it's about tailoring the property to the right target group through design, marketing and leasing strategies. Ensuring apartments are properly fitted out, marketed through the right channels and handled by the right leasing or sales agents is key to maximizing returns. All of this becomes part of the overall value-add proposition.

For stranded assets, assembling the right team is critical. Having the technology and expertise to reconfigure floorplans and execute a clear construction plan is an integral part of the value-add process.

At Arrow Global, thanks to the full integration between the central team and its platforms on the ground, we create value across the entire investment cycle, from origination and underwriting to business plan execution and hands-on asset management. In the current market, where competition is lower and dealflow is limited, being a first mover and leveraging data-driven decision making can help build a leadership position.

*"When you make an investment, half of the value is created at acquisition, while the other half comes from asset management and value-add initiatives"*

**Q How can investors and managers navigate risk in the current investment landscape?**

While I don't want to reveal all of our strategies, we maintain a clear and disciplined approach to underwriting. Our focus is on achieving an adequate yield on cost while ensuring a sufficient spread between the yield at which we build an asset to and the prevailing market rates.

Drawing on lessons from past cycles, we are currently prioritizing high-yielding assets, where market conditions allow for acquisitions or developments at particularly attractive yield on cost levels.

What sets this cycle apart is the highly localized nature of distress in Germany. Unlike previous downturns, where large portfolio sales dominated the market, today's opportunities are emerging at an individual asset level. Many of these distressed projects, especially in Germany's secondary cities, are being sold by local insolvency practitioners with limited international reach. With our on-the-ground teams and strong local relationships, we are able to identify and execute on these deals before they gain wider market exposure, allowing us to secure compelling risk-adjusted returns for our investors. ■