Investing in Swiss Commercial Properties

Low-risk assets are in high demand. Also assets such as real estate – they offer return potential and protection against inflation. However, not every property is suited as an investment. Luciano Gabriel, CEO of PSP Swiss Property, favours top commercial properties in Switzerland's economic centres.

Interview with Luciano Gabriel
CEO PSP Swiss Property

Private: Mr. Gabriel, the financial markets just won't settle down. How has business been for PSP Swiss Property in 2011 and in the first half of 2012?
Gabriel: More than satisfying, particularly against the backdrop of a persistently difficult economic environment. With a net income of 149 million francs excl. net changes in fair values, we achieved the best result in our Company's history in 2011; our property portfolio's value has reached 6 billion francs and the share price continues on a strong course. In the first half of 2012, nothing out of the ordinary occurred, which is good news in our line of business.

Private: Were you able to lower your overall vacancy rate?
Gabriel: Yes. At the end of March 2012, the overall vacancy rate was down to 7.4% after 8.3% at the end of 2011. A significant part of the vacancies is due to ongoing renovations and improvements on various properties; this inevitably leads to vacancies and diminished rental income. Of course we could lower the vacancy rate relatively fast, but that would not be our goal. We aim at optimising the vacancy rate in the long run, not reducing it at any cost. We will not "buy" additional short-term rental income by compromising on the properties' or the tenants' quality; we want sustainable growth with top tenants in premium properties.

Private: PSP Swiss Property has a solid balance sheet, a good liquidity ratio and access to the capital market. Why aren't you more active in purchasing additional properties?
Gabriel: We have, indeed, been very reluctant with regard to purchases in recent years. On the other hand, we again sold a number of smaller properties last year to further streamline and optimise our portfolio. In any case, substantial credit lines from various banks offer us the option to react quickly, if special purchasing opportunities would arise. They are also proof of the trust PSP Swiss Property enjoys on the capital market. However, in the current environment we prefer developing our sites and renovating and improving our properties.

Private: As a real estate company, PSP Swiss Property has been benefiting from record-low interest rates for quite some time. What would happen, if or when interest rates rise again?
Gabriel: We are well prepared: First, because we have always pursued a conservative financing policy; our debt ratio is a low 32% of total assets. Second, because we hedge our liabilities against rising interest rates by means of interest rate swaps which, increasingly, include forward starting interest rate swaps, i.e. swaps, which start in a year or two and fix interest rates from that point in time for several years.

Private: How important is sustainability for PSP Swiss Property?
Gabriel: Sustainability has always been a major topic, although we never made a lot of noise about it. Today, however, sustainability is an integral part of our reporting. In our sustainability report inside the annual report, we deal with both ecological sustainability, i.e. the way we take the environment into account at all stages of our business activities, as well as economic and social sustainability. We intend to implement energetic optimisation measures in most of our buildings, if technically feasible, by 2015. Finally, we created a special new position of an environmental officer who is specifically responsible for sustainability at our properties.

Private: Let's focus on environmental sustainability: PSP Swiss Property owns more than 160 properties throughout Switzerland. How can you be sure that your efforts with regard to sustainability are implemented in all of them?
Gabriel: We surveyed and analysed virtually all of our properties with a view to their sustainability in the past two years. The result was that all major environmental key figures – i.e. energy consumption, water consumption and CO_2 output – were excellent, in 2011 even better than in 2010. To keep track of our sustainability efforts overall, we began installing a central monitoring system with data recording devices last year. This allows us to monitor operations respectively energy and water consumption over the Internet and to

PSP Swiss Property: Facts and Figures

PSP Swiss Property is one of Switzerland's leading real estate companies. Throughout the country, the Company owned 167 office and other commercial properties with a carrying value of 5.7 billion francs at the end of March 2012. The properties are mainly in top locations in Zurich, Geneva, Basel, Bern and Lausanne. In addition, PSP Swiss Property has 10 development sites and individual properties for conversions and new constructions valued at 278 million francs. With shareholders' equity totalling 3.3 billion francs – corresponding to an equity ratio of 55% – PSP Swiss Property has an extraordinarily strong equity base. Interest-bearing debt amounts to 1.9 billion francs, which is a mere 32% of total assets. The difference consists primarily of deferred taxes which do not activate any interest charges. Further proof of the Company's capital strength are its open credit lines of 820 million francs from various banks.

A core investment for the Swiss commercial property market

The PSP shares have been listed on the SIX Swiss Exchange since the Company's initial public offering (IPO) in March 2000. The shares' liquidity is high: In 2011, an average of 109,124 shares worth 8.3 million francs were traded each day; the total trading volume of the PSP shares reached 2.1 billion francs. In the same period (January to December 2011), the shares gained 4.8% despite a distribution of 3.7% on the year-end share price 2010; the cash payment to the shareholders was made in June 2011 in the form of a nominal value reduction. (In April 2012, the Company made a cash payment to its shareholders out of the capital contribution reserves corresponding to 3.8% of the year-end share price 2011.) PSP Swiss Property thus confirmed its shareholder-friendly distribution policy. The Company's shares are known as a predictable and stable core investment for the Swiss commercial property market. From 7 March 2000 (the day of its IPO) until 19 June 2012, the PSP share delivered a performance of 122%.

act immediately in the case of irregularities or malfunctions. By the end of 2012, the facility managers at all our properties should be able to regularly record consumption and enter the data into the central database over the Internet. The control system will then verify the data with regard to its plausibility and signal any deviations from the norm.

PRIVATE: How exactly did the environmental key figures improve from 2010 to 2011?

Gabriel: We were able to further reduce energy consumption and, consequently, CO_2 output overall. This was mainly possible due to our targeted renovation and optimisation measures – e.g. by installing new heating systems or improvements in building engineering. Furthermore our efforts to sensitise our staff and tenants to use energy more economically probably also contributed to the positive development. And another interesting piece of information: How successful we are in our efforts with regard to ecological sustainability can also be seen in the fact that, over the portfolio as a whole, our energy savings more than compensated the higher market prices for energy – which also proves that ecological sustainability can directly and positively impact the bottom line.

PRIVATE: To which extent do you take sustainability into account in new constructions and conversions?

Gabriel: In new constructions and conversions energy efficiency is crucial. Basically, we follow the "Minergie" standard to be able to build as environmentally friendly and, consequently, as cost efficiently as possible in the long run. The planning for our new construction project Grosspeter Tower in Basel even goes so far that there should be zero greenhouse gas emissions after completion.

PRIVATE: Do you worry about the new buildings which will come on the market in the near future, particularly in and around Zurich?

Gabriel: No. You are right that substantial new office and retail spaces will come on the market in the next year or two. However, part of this new space will likely be absorbed by the expansion of existing firms and the arrival of new foreign companies. Furthermore, most of the new office and retail space is developed in peripheral areas, which hardly affects our locations in the city centres. If you want to have an office or a shop in the city centre – even if it's just for prestige –, you don't move to the outskirts of town just to save a few francs.

PRIVATE: What is your outlook for Switzerland's commercial property market in general and PSP Swiss Property in particular?

Gabriel: We are not in a booming market, in which every property can be let just like that, particularly with regard to badly located or poorly maintained buildings. On the other hand, demand for properties in good locations in economic centres – and those are the ones PSP Swiss Property is interested in – remains brisk. All in all, I am guardedly optimistic about 2012. Even if Switzerland has been able to avoid the bigger problems of many Eurozone countries so far, the international sovereign debt crisis and the strong franc will probably continue to affect the country's economy in the coming months. Therefore it is all the more important that we keep to our prudent acquisition strategy and our conservative financing policy. PSP Swiss Property has a well-established market position, a strong capital base and a high-quality property portfolio. With all these facts in mind, I am confident about the medium- and long-term prospects for both the Swiss commercial real estate market as a whole and for PSP Swiss Property in particular.

luciano.gabriel@psp.info
www.psp.info