



Uncovering hidden success – the unheralded locations beyond prime?

In times of continuous yield compression, investors are forced to reconsider their risk profile. Investments outside the top locations or in niche segments are traditionally used for diversification. Traditional 2nd tier locations and, to a lesser extent, 3rd tier locations typically get the nod. It is true to say that this decision involves considerable uncertainty in light of the low level of transparency and limited exit opportunities during market crises. To date, investors have been barely to move into unknown regional domains or beyond the traditional nomenclature. However, the long-term nature of investment suggests that they are incorrect to do so. Small and medium-sized German companies – the Mittelstand – are manufacturing and investing here with impressive success, so why not also take look at these areas from a real estate perspective?

The German Mittelstand: a widely unappreciated factor

The metropolises of the globalised world are undoubtedly the centres of value creation, and hence the focal point of real estate investment activity. However, zooming in more closely reveals another dimension of Germany’s economic structure that is probably unique within Europe in its form. A large number of highly specialised small and medium-sized enterprises – the companies that make up the “German Mittelstand” – in supposedly peripheral locations are the leaders in their respective industries.

Hidden Champions

Simon (1990) defines Hidden Champions as mostly relatively small, owner-operated companies that are leaders in their global, or at least domestic, markets. These companies, which typically have a family tradition, tend to have strong links to their region of origin and use it as a base for global expansion. Satisfying the cliché of German engineering expertise, they operate mostly in technical and electronic industries such as mechanical engineering and electrical engineering, specialising in production machinery and vehicles. Catella has recorded and mapped Germany’s Hidden Champions. This makes it possible to identify the hotspots within and outside the conurbations in western and, in particular, south-western Germany that boast substantial positive value creation at the level of the local economy in the areas of retail, consumer goods and residential real estate.

THE INDUSTRIES OF GERMANY’S HIDDEN CHAMPIONS

Industry	Share	Average distance to nearest office market	Ratio of production space to administrative space (office + lab)
Mechanical & plant engineering	22 %	High	80 : 20
Electrical engineering & IT	19 %	Low	60 : 40
Vehicle manufacturing, esp. automotive	11 %	Medium	70 : 30
Medical technology & life Science	6 %	Low	30 : 70
Other	42 %	Low	60 : 40

Source: Catella Research 2016

DEFINITION OF HIDDEN CHAMPIONS (according to Simon)

- They are the number one, two, or three on the global market – or number one on their home continent.
- Their annual revenue is generally below €3 billion.
- Being mostly owner-operated and unlisted, they have a low level of public awareness.

Source: Catella Research 2016

Hidden Champions offer value added for the real estate industry

Many of the Hidden Champions can still be found in their historical locations, meaning that they own a lot of the buildings they occupy. Although most Hidden Champions are clustered around the major cities in the conurbations, very few of them actually have their production facilities and administrative offices there. The typical Hidden champion is based in a small or medium-sized city in the surrounding area with a commercial property market volume that is usually well under a million square metres, meaning that it can serve as an indicator of local economic activity.

HIDDEN CHAMPIONS AS AN INVESTMENT INDICATOR

Pro	Con
Indicator of an innovative economic structure	Limited transparency / exit difficulties
Evidence of positive long-term regional development in the past	Cyclical production relocations
Growth industries and specialisation	Leaders in markets with little competition (oligopoly), meaning almost no price transparency

Source: Catella Research 2016

THE REAL ESTATE DNA OF HIDDEN CHAMPIONS

- Properties often owned and owner-occupied
- Single-use architecture with a focus on individual usage
- Triad of production space with connected office space, low proportion of traffic/logistics space
- Located in real estate markets with a volume of <1 million sqm – property is often “the” market

Source: Catella Research 2016

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GERMANY'S HIDDEN CHAMPIONS – LOCATION STRUCTURE

- Office stock > 1 million sqm volume ●
- Number of company headquarters in the industries investigated
 - 1
 - 3.5
 - 6
 - 10

