 by Rainer Apel

Berlin—from boom to doom?

Real estate and banking problems are threatening Germany's capital with a financial crash.

When the next big banking crash hits Germany, where will it hit hardest? In Frankfurt, the center of banking? Maybe. But, the worst damage could be in Berlin, the capital and, with 3.5 million inhabitants, Germany's biggest city. Berlin has made headlines in recent weeks because the municipal government imposed a total budget freeze until the end of this year, to cover a shortfall in tax revenues of more than half a billion deutschemarks. This marks the end for new public sector projects and for many construction firms, and many more construction workers will join the 44,000 in this industry who are already officially unemployed.

This is a dramatic development for a city that, after the reunification of Germany in October 1990, hoped it would become the "boomtown" not only of Germany, but of Europe, because of the envisioned return of the government from the provisional capital of Bonn to Berlin, and the many construction and restoration projects that would accompany it. There was a time, in 1991-92, when Berlin was portrayed as the biggest market for real estate development in the world, next to Hongkong, with a potential for several tens of billions of dollars in projects. But it was already clear at the time, that a lot of those projects were not sound, because they were based on real estate speculation and shadowy designs for huge shopping malls with integrated office buildings, with an investment volume of $1.5-2 billion each. Murky investors, such as Mark Palmers, with his over-ambitious Checkpoint Charlie project, or the U.S.-Canadian Tishman Speyer group, came on the scene, proclaiming plans for turning Berlin into a "supermodern" city.

For the construction union, which saw more and more of its members losing their jobs and being replaced by cheap labor from other parts of Europe (east and west) on these huge new construction sites, it soon became clear that there was a foul game being played. Also, the huge discrepancy between housing projects and office-building projects caused many observers to ask where all those people who were going to work in those brand-new offices would come from, when the government in Bonn, because of austerity, had slowed down its move to Berlin, and the creation of new jobs in the service sector was not keeping up with the new office space. A disaster seemed programmed in five years ago, and now, it is here.

"The Most Risky Real Estate Market in Europe," the daily *Süddeutsche Zeitung* headlined its May 16 feature on the Berlin real estate crisis. Many investors are facing a situation, it reported, in which their office buildings are turning into "money-destruction facilities." A manager of a Berlin real estate company was quoted saying that "so far, there hasn't been a spectacular bankruptcy" among the investors or their creditors. But, "behind closed doors, there is massive activity of all sorts" to try to prevent exactly this from happening, while "many profitability calculations are not worth the paper they are printed on."

About 1.4 million square meters of unused office space already exist in Berlin, a giant castle in the sand. And, according to a recent survey by the local chamber of trade and commerce, this figure will soon increase to 2.2 million square meters. For example, in Berlin's famous Friedrichstrasse, one of the showcase streets of the city, only 20-50% of office space has been rented. And, the paper revealed, tenants privately admit that for the first year they don't have to pay any rent at all—which determined their decision to move there in the first place. How they will survive the second year, when they will have to pay rent, is a mystery.

The first week of May also brought news of another, related disaster: It was "a black week for the Berlin banking sector," *Handelsblatt,* Germany's leading business daily, reported on May 7. As a consequence of plunging real estate prices and the overall economic depression in the region, the Grundkreditbank received an emergency injection of DM 80 million from the deposit insurance of the Federal Association of Cooperative and Agricultural Banks, to escape the immediate threat of bankruptcy. The head of the bank was replaced, and it will be merged with Berliner Volksbank.

In addition, a brand-new banking crisis erupted during the first days of May, when Bankhaus Loebbecke, a bank that has 60% of its operations in the real estate sector, received an emergency loan of DM 650 million from its main stockholder, the Milan-based Cassa di Risparmio delle Province SpA (Cariplo), Italy's third biggest bank—which itself will be forced to report a net loss of the same dimension in its Berlin branch. "The German capital is right now a dangerous area for the banking sector," *Handelsblatt* said. "The crisis is hitting almost every bank in the capital."