INVESTMENT MARKET UPDATE

Record investment set to continue

Europe Q4 2015

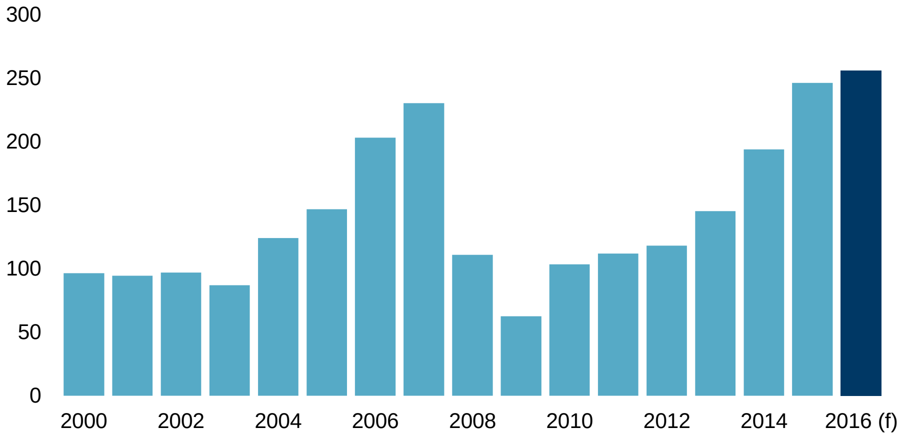
03/02/2016

Contents

- European commercial real estate investment reached EUR70.4bn in Q4 2015, pushing full year investment volumes to a new record high of EUR246.3bn.
- Majority of markets recorded growth in activity in 2016, with the balance shifting from the UK to the continent. Of the major markets Germany led the way with 40% growth in activity. Strong growth continued in the Periphery and across the rest of Europe. The UK and France posted below average growth.
- Domestic investors increased their activity in the second half of the year, but remained net sellers in 2015. Non-European investors continue to grow their holdings driven by strong investment from North American, Asian and Middle Eastern capital.
- Investment into retail sector continues to grow with record volumes of capital invested, supported by strong shopping centre sales. Other sectors, including leisure continue to see strong inflows. Offices remain the most desirable asset class.
- Funds, institutions, including sovereign capital and listed companies were the main net buyers into European commercial real estate. The trend by listed companies reverses their position of net sales in previous years.
- Commercial real estate is expected to remain attractive with the lower for longer interest rate environment maintaining the weight of capital flowing in. Further growth in investment activity should result in over EUR260bn of acquisitions in 2016.

Figure 1

European investment activity, EUR bn



Source: Cushman & Wakefield Research

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Investment Volume

Full year volumes surpass 2007 levels

The fourth quarter of 2015 saw an upsurge of investment into commercial real estate investment in Europe totalling EUR70.4bn. This took full year volumes for 2015 to EUR246.3bn, surpassing the previous record of EUR230.5bn in 2007. The volume of activity in the final quarter came in marginally lower than anticipated and broadly on a par with activity in Q4 2014. As a result the rolling annual total flat lined in the final quarter (Figure 2).

Strongest growth in Germany and outer Europe

The UK commercial real estate market saw EUR20.9bn invested in Q4, a 21% increase on Q3. This pushed full year volumes to EUR84.8bn, substantially surpassing last year's record of EUR73.4bn. Despite the overall positive trend, the rate of growth is starting to slow with rolling annual volumes now 8% lower than their peak in Q2 2015. The UK has led the recovery compared to the rest of Europe, thus the rate of growth remains below the European average (Figure 3). Despite an increase in investment activity in Q4 to EUR10.1bn, it was still not enough to spark a recovery in the French market with growth remaining below average. We expect the trend to reverse.

Of the three core markets, Germany stands out with the strongest performance. Full year volumes of EUR50.9bn were over 40% up on 2014 levels and highlight the growing investor interest in this market. It is also the only of the three core markets to see its share grow. Despite this, volumes are still below their 2007 peak of EUR58bn.

Elsewhere in Europe, strong growth remained a theme. Double digit year on year growth was recorded in the Benelux and the Nordic regions at 28% and 27% respectively. The rate of growth slowed slightly in the periphery markets of Ireland, Italy and Spain, although remained robust at 43%. The capital targeting Spain had spread wider across the Iberian Peninsula, with Portugal seeing a substantial growth in investment during 2015. Very strong growth in capital inflow in both Switzerland and Turkey also contribute growth of over 200% across the Rest of Europe.

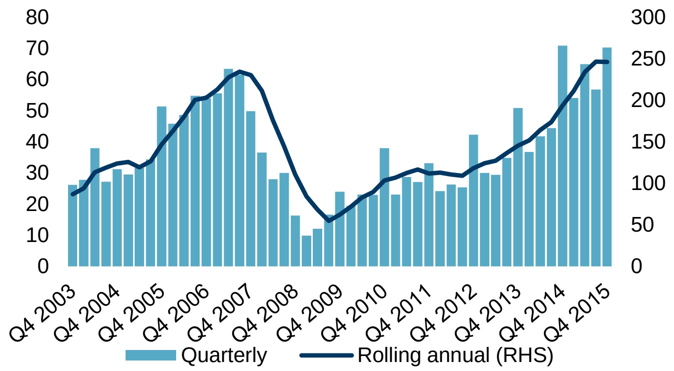
Increase in EUR500m+ deals boosts average lot size

The average lot size for deals in Europe rose in Q4 2015 following a dip in the previous quarter (Figure 4). Entity level deals returned with Merlin Properties completing the purchase of Testa Inmuebles En Renta Sa from Sacyr SA. This contributed to the upturn in average lot size. There were also a number of large portfolio deals including the Blackstone purchase of the Kensington portfolio in France and the Oslo Areal portfolio purchase by Swedish institution AMF.

Deals ranging between EUR100m and EUR500m continued to be the most active accounting for 40% of total volume.

Figure 2

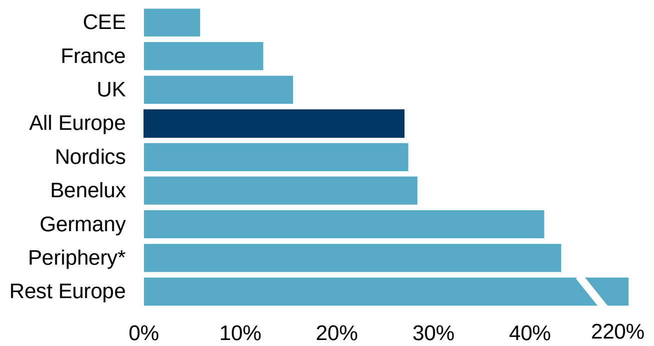
European Investment activity, EUR bn



Source: Cushman & Wakefield Research

Figure 3

Change in investment activity 2015v2014, %

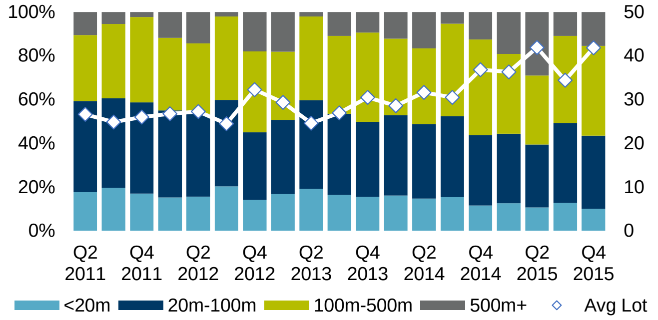


** Ireland, Italy and Spain*

Source: Cushman & Wakefield Research

Figure 4

Investment activity by lot size and average lot size, EUR m



Source: Cushman & Wakefield Research

Source of Capital

Non-European investors remain net investors

Domestic investors were increasingly active in 2015, with over EUR38bn invested in the final quarter and following over EUR31bn in Q3. This took full year investment to near EUR125bn, a 19% increase on 2014. Despite showing the weakest growth (Figure 5), domestic players deployed EUR20bn more this year, more in absolute terms than other cross border players.

Cross border investment has remained strong throughout the year. European cross border investment has continued to grow and has seen the highest year on year growth at 42% (Figure 5), albeit this is at lesser volumes than those invested by Non-European and domestic investors. Here we have seen strong inflows into Germany, as well as increased flows within the Nordic region. Flows from outside of the region remained strong and grew 32% to over EUR76bn, although the rate of growth slowed in the final quarter.

Despite a slight loss in the market share from Non-European investors in Q4, they continue to increase their exposure to the European real estate market adding a net EUR27bn in 2015. In line with previous trends, both European cross border and domestic investors continued to be net sellers over the year (Figure 6).

North Americans dominant

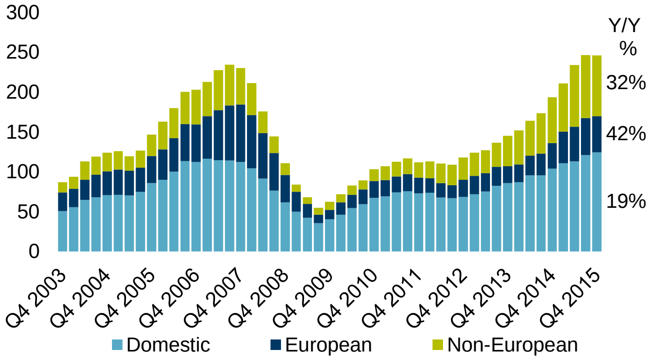
2015 was a record year for Non-European investment into European real estate with EUR76.3bn invested, 66% up on the volumes invested from overseas in 2007. This included some high profile entity level transactions, notably North America's Brookfield. Even excluding these transactions the flow of capital from North America was strong with US investors deploying EUR16.4bn in 2015, adding to a strong 2014 where EUR19bn was deployed. A further EUR5bn flowed into Europe from Canada (Figure 7). However a similar EUR5bn was also repatriated through sales.

Despite volatility in equity markets in China and lower economic growth, the flow of capital from China continues unabated. They yet again led the Asian charge into Europe with EUR3.4bn invested. With few sales, they were the largest net investor for a single nationality. Several listed Singaporean companies have been active in the European real estate market and their investment total closely follows that of the Chinese.

Middle Eastern capital targeting Europe has primarily come from Qatar and the United Arab Emirates. Even excluding entity transactions the volume was strong and included a mix of both sovereign and private capital.

Figure 5

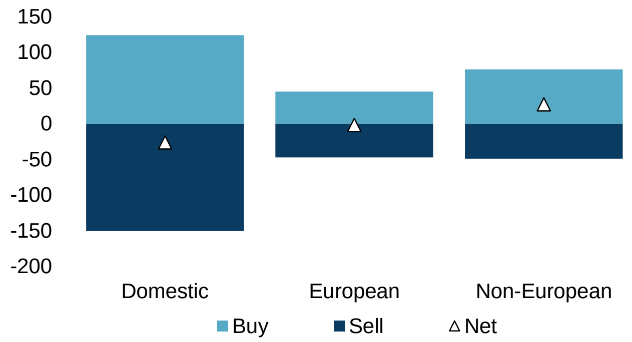
European investment by capital source, rolling annual, EUR bn



Source: Cushman & Wakefield Research

Figure 6

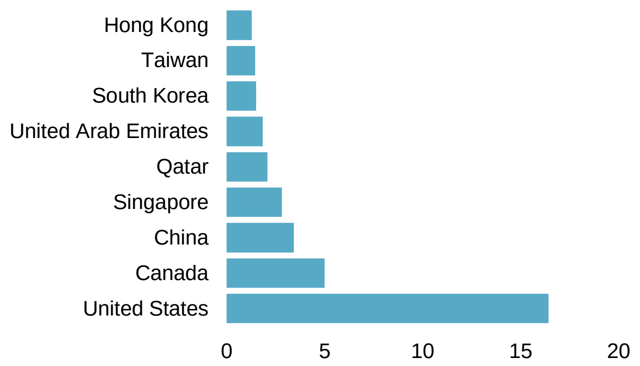
Net investment by capital source, 2015, EUR bn



Source: Cushman & Wakefield Research

Figure 7

Top investors into Europe*, 2015, EUR bn



** Excludes entity level deals and capital from international sources*

Source: Cushman & Wakefield Research

Balance shifting away from UK

In absolute volume terms, investment from overseas is up in most markets in Europe, exemplifying the growing non-European presence in the European real estate market. Not only has Non-European investment grown in recent years, but 2015 was a year in which these investors continued to move away from the safe haven of the UK and broaden their horizons and diversify into a wider set of markets (Figure 8). Many overseas investors prefer to establish themselves in the UK before moving out to other geographies, and the trend has been clear to see when paying close attention to inter-regional investment activity. Non-European investment into the UK in 2015 was EUR33.4bn, and whilst this was the highest volume of investment from a non-European source for a full year, it represented 44% of the total, compared to 53% in 2013.

Germany has been the main beneficiary of this shift as investment has almost trebled since 2013 to over EUR15bn in 2015. Its share increased from 15% to 20% over this period.

Other than the Benelux region, overseas investment grew year on year in all European regions in 2015. In particular the countries making up Rest of Europe saw a spike in investment from overseas, taking their share of non-European investment to 6%. This however includes some pan-European portfolios deals.

Investor Type

Funds dominate, listed companies remain biggest net buyers

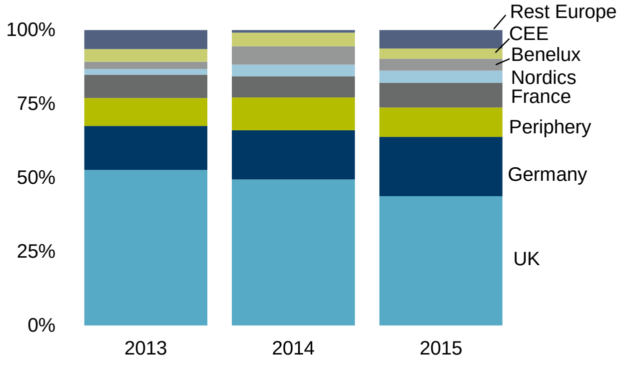
Throughout the year, unlisted funds have dominated activity in the market. With funds now clearly focussed on deploying their raised capital, the volume and share of activity rose in Q4 after a strong Q3 (Figure 9). The latter half of the year saw unlisted funds increase their market share and account for over EUR62bn of capital flowing into European real estate. With little change in the volume of sales activity, unlisted funds became net investors for the year overall, reversing the trend earlier in the year.

With a net investment of EUR14.2bn, listed companies remained the biggest net investors into Europe in 2015 despite being slight net sellers in Q4. The net position of listed companies reflects strong activity early in the year, notably from overseas companies (Figure 10). Institutions, both domestic and overseas, remained net investors in 2015 at near EUR7bn, following a year of consistently strong investment activity. Sovereign wealth funds were also very active buyers, and similarly invested close to a net EUR7bn in 2015. This total was their second highest total for a full year in the past decade.

Private companies and investors yet again sit at the opposite end of the spectrum and are the biggest net sellers in the European real estate market. Corporate investors, as well as investors of other classifications, were the other net sellers in 2015.

Figure 8

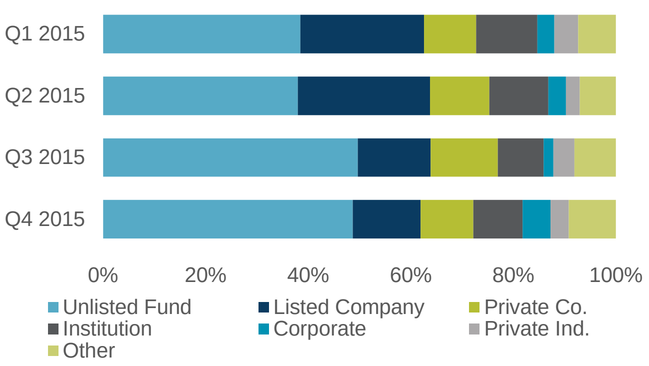
Destination of non-European investors



Source: Cushman & Wakefield Research

Figure 9

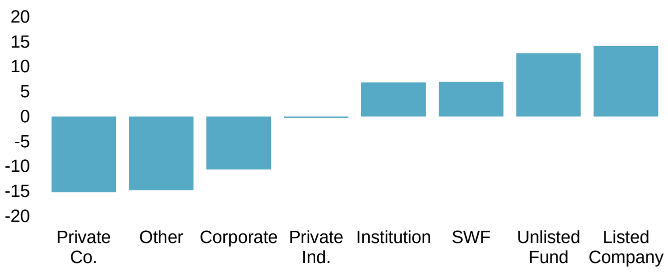
Investment activity by investor type



Source: Cushman & Wakefield Research

Figure 10

Net investment by investor type, 2015, EUR bn



Source: Cushman & Wakefield Research

Property type

Offices dominate, but market share weakens

Historically the office sector attracts the greater share of volume invested into Europe. Despite prime office assets in a number of the markets approaching record prices, and the sector generating strong competition amongst investors, 2015 was no different. Over EUR100bn was invested into the office sector, a 20% increase on 2014. As such, investment into the office sector accounted for 42% of total capital flow into European real estate in 2015. However, as a share of total investment, this continues to decline as investors invest more into other sectors (Figure 11).

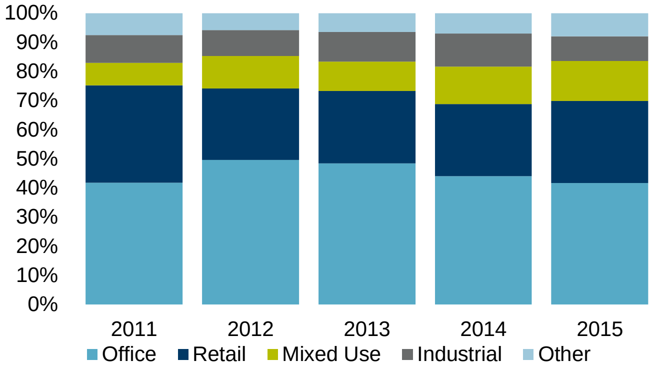
Rebound in retail and other sectors

One of the beneficiaries has been the retail sector, in particular, investment into shopping centres. Nearly EUR70bn was invested into the retail sector in Europe throughout 2015, with several substantial shopping centre portfolio sales driving the record total. During the fourth quarter this included the sale of the Oslo city shopping centre portfolio to a joint venture between Steen & Strøm and Entra. With over EUR34bn invested into shopping centres in 2015, this was the highest volume on record.

The mixed use sector has seen year on year growth in investment volumes in recent years and now accounts for 14% of total investment into Europe. Industrial volumes also remained strong at over EUR20bn in 2015, though marginally lower than 2014 leading to a reduction in market share. Other asset types continue to attract investor interest, where volumes doubled to over EUR6.5bn in 2015.

Figure 11

Investment activity by property type



Source: Cushman & Wakefield Research

Outlook

Demand will continue to drive volumes higher

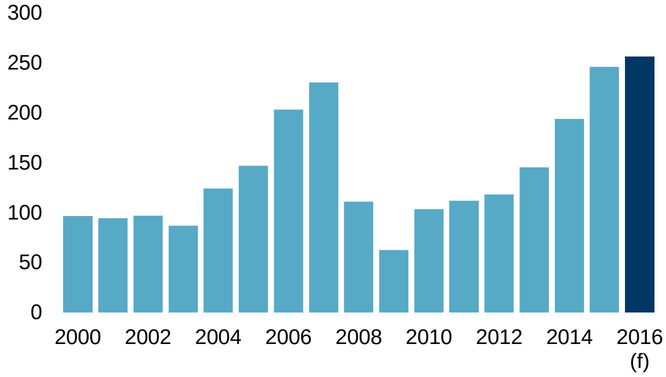
2015 was a record year for investment into Europe, and even with investment towards the end of the year being slightly below expectations, investor sentiment remains positive and a number of deals are expected to spill over into the first quarter of 2016. As such, the core markets continue to see strong inflows of capital and investors have been more susceptible to exploring opportunities elsewhere in Europe.

Despite volatility in equity markets, the lower for longer interest rates and continued quantitative easing in Continental Europe will maintain investor demand for real estate. At the same time the economy also appears to be recovering, with GDP forecasted to grow to 1.8% in 2016. This supports both the leasing markets and rental growth.

With a strong weight of capital remaining and investors diversifying more into the growth markets on the continent, we expect volumes to grow by between 5-10% in 2016 to over EUR260bn (Figure 12).

Figure 12

European investment activity, EUR bn



Source: Cushman & Wakefield Research

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