

RESEARCH



MADRID

PRIME RESIDENTIAL 2016

MACROECONOMIC BACKDROP

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| DEMAND

| PRICES

Prime residential assets: safe haven for investors

“Macro data suggests a positive trend, but the uncertainty brought on by the lack of government cannot be ignored. The economy continues to chug along, but stability would create exponential growth”.

ERNESTO TARAZONA
Partner, Director Residential & Land

The performance of the world’s prime residential market is shaped by several factors. This is clearly demonstrated in the latest Prime International Residential Index (PIRI) figures published in The Wealth Report. Whilst some prime second-home markets such as France and Italy were still recovering from the economic crisis, other markets such as London have hit all-time highs. The good news is that very few markets included in the PIRI saw price falls.

All the Spanish destinations included in the index (Madrid, Barcelona, Ibiza, Marbella and Mallorca) registered price increases.

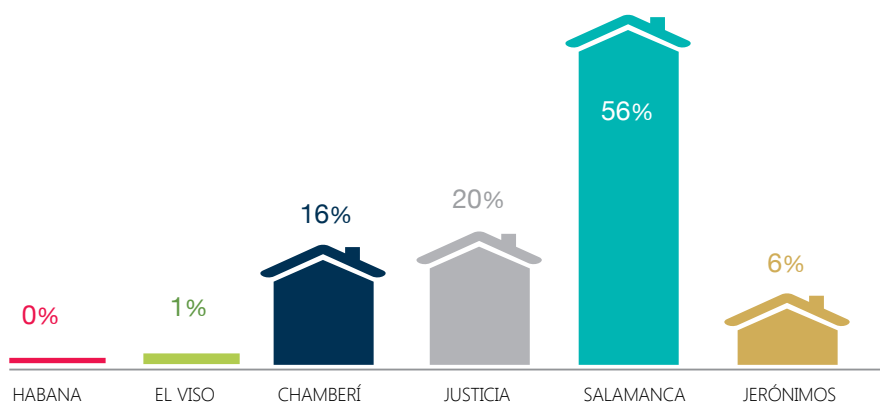
Prices in the prime areas of Madrid analysed by Knight Frank rose 3% y-o-y, testament to the sector’s modest and stable growth. Furthermore, in line with our forecasts published in our last report, Madrid’s prime residential sector has changed significantly. The growth potential in several areas of the city has now clearly materialised, with prices now on a continued upward curve.

Prime residential assets have once again become a safe haven for investors. At a time when the economy is marked by market volatility and negative interest rates, the real estate sector – especially luxury residential - has become the safest bet for investors.

Whilst some real estate sectors may be affected by Brexit, Madrid’s prime residential market will not only not be affected, but may in fact benefit in some cases if investors decide to invest in Madrid instead of London.

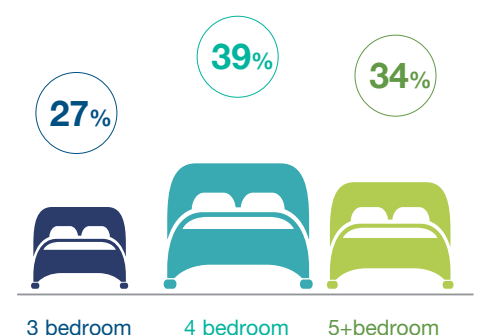
Although Macro data continues to outline a positive trend (record-breaking tourist figures, excellent infrastructure and upbeat forecasts for job creation), the fact remains that political uncertainty has been hanging over Spain for 10 months now. Over this period, the prime residential sector has benefited from robust activity, largely because the economy continues to chug along out of inertia. However, at Knight Frank we believe that with a stable government, the sector’s growth would turn exponential.

FIGURE 1
Distribution of available stock by district (%)



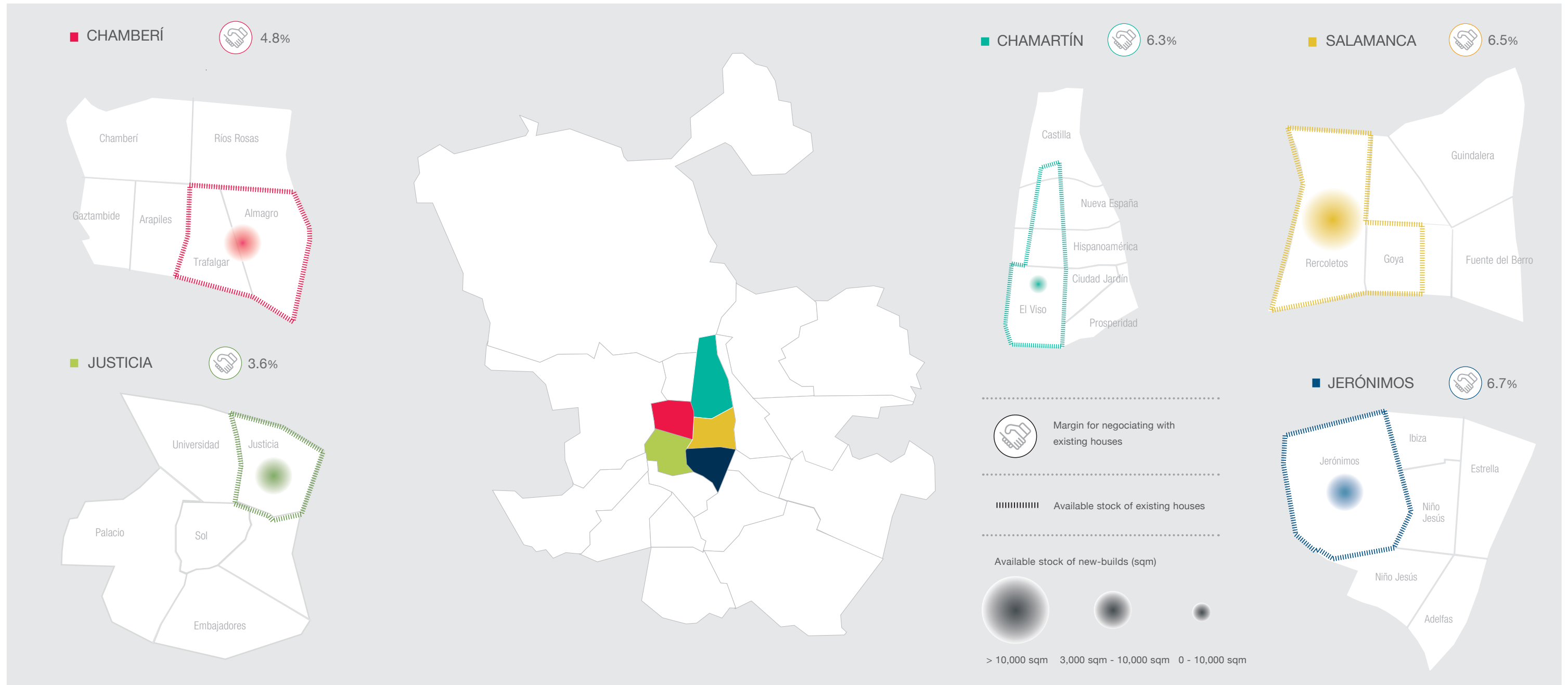
Source: Knight Frank

FIGURE 2
Distribution of available stock by type (%)



Source: Knight Frank

FIGURE 3
Location of available stock in Madrid's prime area



Source: Knight Frank

Prime new-build supply in Madrid has increased for the first time on record

The major change in terms of prime product supply is the considerable upturn in the amount of new-build stock compared to last year. Luxury new-builds

accounted for just 30% of total supply in 2014, whereas this figure jumped to 60% in 2015. Consequently, the size of this market has also increased, with available supply totalling €820 million, 17% up y-o-y.

All aspects of the sales marketing process continue to gradually improve. Take-up came in at 31%, in line with the figure booked last year. We would also

highlight that prime product buyers are increasingly opting for new-builds, with take-up in this segment reaching almost 40%. Whereas in previous years, this figure was in the region of 30%.

With 56%, the Salamanca district accounts for the lion's share of supply (both new-builds and existing housing) and is the undisputed leader in new-build projects.

The fact that some new-build projects going on the market feature a higher than average number of units is also particularly noteworthy. Due to the exclusive nature of luxury projects, especially given their architectural and technical specifications, only a limited number of units go on sale, in most cases no more than 15 or 20. However, complexes such as Lagasca

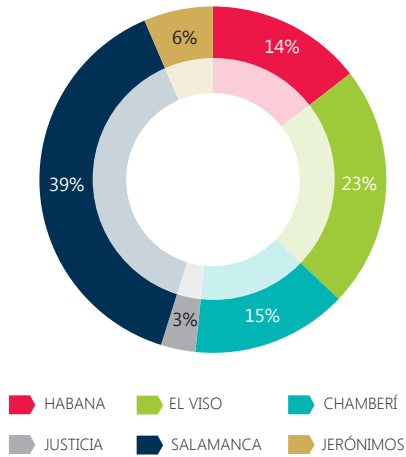
99 have gone against the norm for luxury developments and gone on the market with over 40 units.

In terms of number of bedrooms, four and five-bed homes account for the largest share of supply, representing just shy of 80% of total supply. This is a change in trend versus previous years, when 3-bedroom homes held more weighting.

El Viso: one of the most sought-after areas

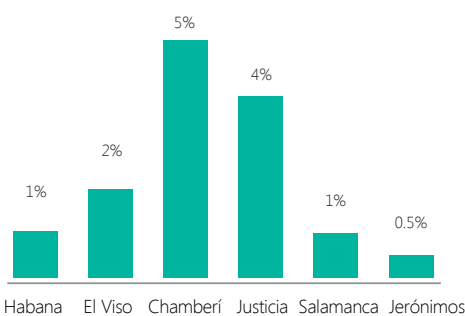
As the number of buyers continues to climb, so too does the number of transactions. In fact, in Q1 2016, the number of transactions involving prime residential properties (both new-builds and existing housing) rose 30% y-o-y.

FIGURE 4
Preference by area (%)



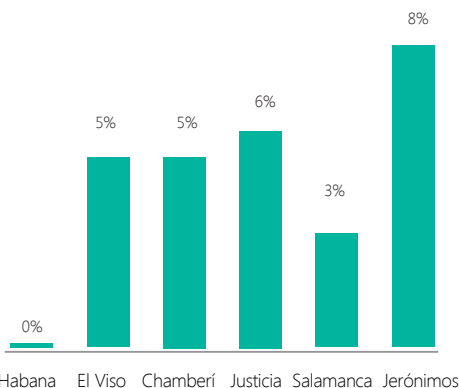
Source: Knight Frank

FIGURE 5
Existing housing 2015 vs. 2016 (€/sqm)



Source: Knight Frank

FIGURE 6
New-builds 2015 vs. 2016 (€/sqm)



Source: Knight Frank

The confidence of those who invest in prime products continues to grow and negotiating margins between asking and closing prices, which on average barely exceed 5.5%, are testament to this.

The Salamanca district remains the most sought-after area (39%), however interest has notably increased in the El Viso district. In our previous report we highlighted that the profile of this area was set to rise, and we can now confirm that El Viso is indeed now the preferred choice for an increasing number of buyers, with its market share rising from 8% to 23%.

Over 56% of buyers opt for homes that require refurbishing, with many preferring to personalise their homes with the quality materials and finishes of their choice, and improve the property's energy efficiency in the process.

In line with the trend seen last year, local buyers still hold more weighting (70%) than international buyers (30%). Latin Americans (Venezuelans and Mexicans) and Europeans are the most active buyers.

Prices

Prices in prime areas of Madrid continue to tick steadily upwards.

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We would particularly note that prices have not fallen in any of the city's districts, rising on average by 3%. Furthermore, in districts such as Jerónimos, the y-o-y increase in new-builds has reached 8%. As far as existing homes are concerned, Chamberí and Justicia have registered the sharpest price increases, rising 5% and 4% respectively.

Salamanca and Jerónimos remain the most expensive areas, with average prices standing at €7,800 per sqm and €8,200 per sqm respectively.

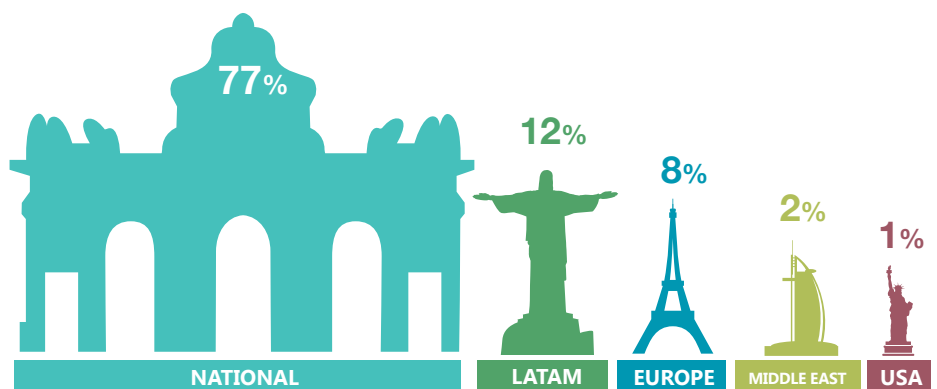
According to our forecasts, El Viso and Jerónimos are the areas with the greatest upside potential in terms of prices, as not only has demand increased in these areas, but they have a sizeable pipeline that will come to light in the coming months.

Madrid will continue to appeal

Madrid will continue to climb up the ranking of European cities. However, even if prices in the luxury residential market carry on rising, they will still be modest and a far cry from those reached in European cities such as Paris, London and Milan.

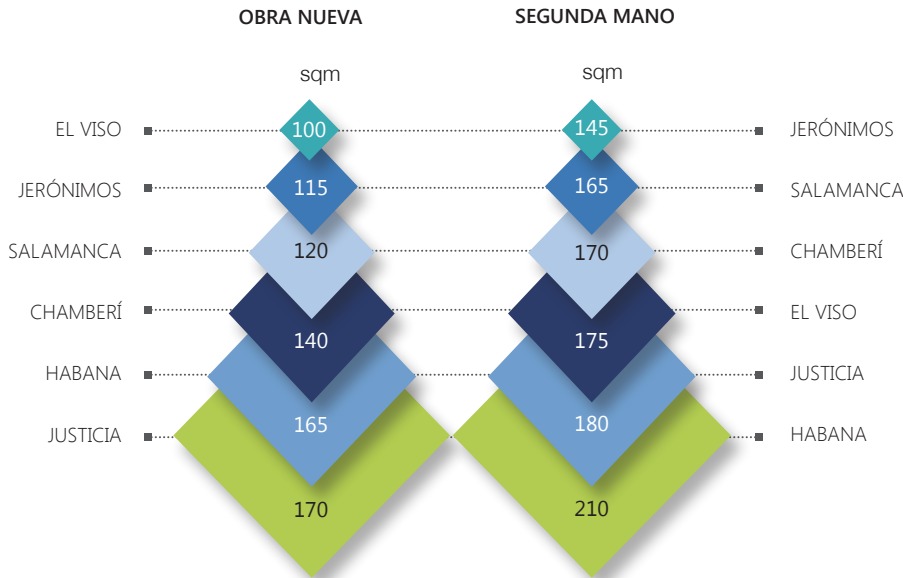
The number of deals closed looks set to continue to increase, reaffirming the

FIGURE 7
Demand by nationality



Source: Knight Frank

FIGURE 8
How many prime sqm do you get for €1 million?



upbeat performance of the prime residential sector.

The already slim negotiating margin between buyers and sellers will continue to tighten over the coming months.

Whilst domestic demand will remain stable, we are likely to see heightened demand from international investors over

the coming months, especially Latin Americans and Europeans, partly thanks to Madrid's competitiveness with other European markets.

Prime product buyers will remain a key and strategic target for banks that want to remain active in the luxury residential real estate business.



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RESEARCH

Ernesto Tarazona
Partner, Director Residential & Land
Ernesto.Tarazona@es.knightfrank.com
+34 600 919 065

Nuria Serranos
Deputy Director Residential & Land
Nuria.Serranos@es.knightfrank.com
+34 600 919 056

José Gregorio Faría
Director Prime Residential
JoseGregorio.Faria@es.knightfrank.com
+34 600 919 116

Marta González
Deputy Director Prime Residential
Marta.Gonzalez@es.knightfrank.com
+34 600 919 119

Davinia Benito
Research Residential & Land
Davinia.Benito@es.knightfrank.com
+34 600 919 087

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