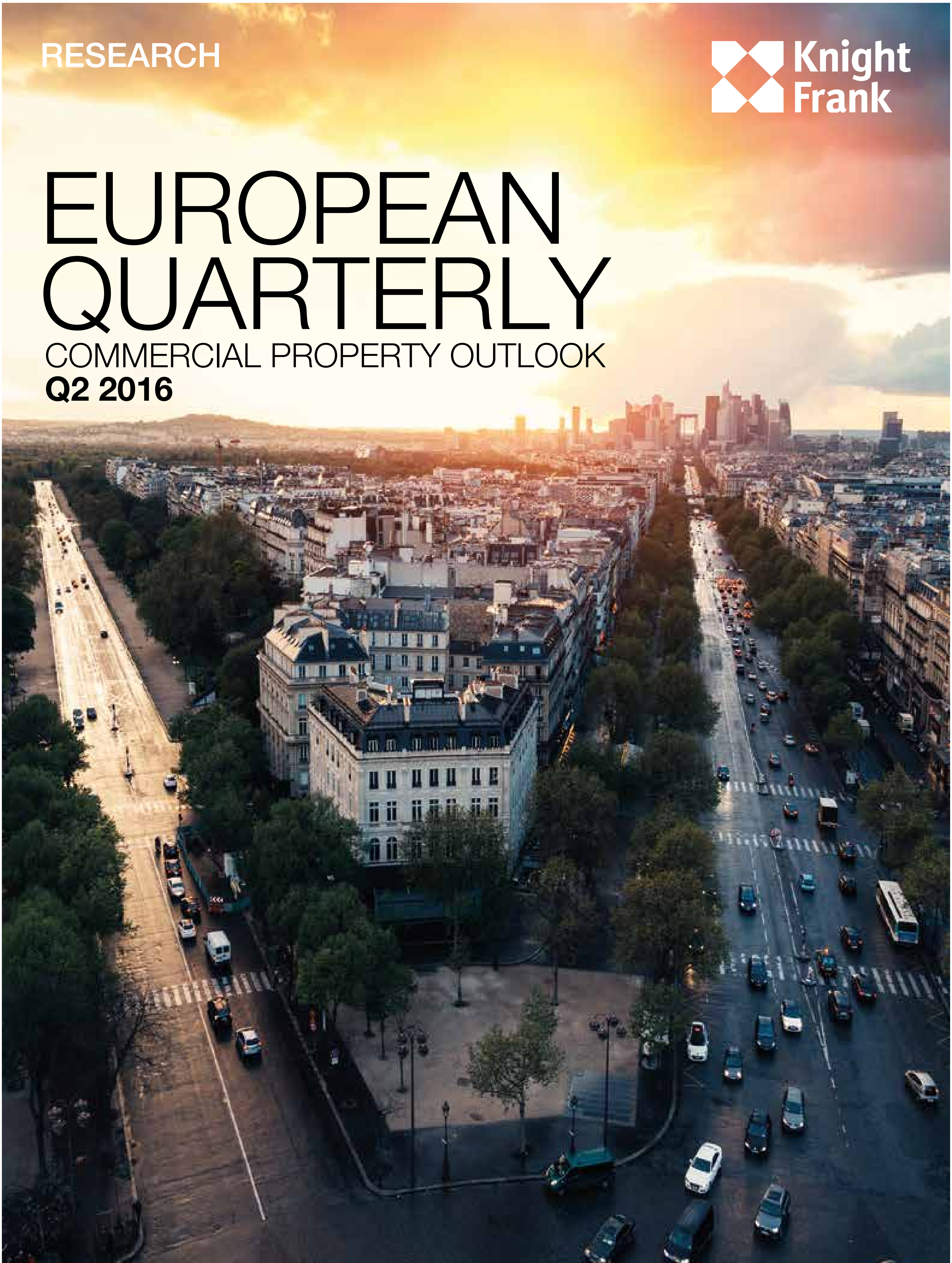
RESEARCH

Knight Frank

EUROPEAN QUARTERLY

COMMERCIAL PROPERTY OUTLOOK

Q2 2016

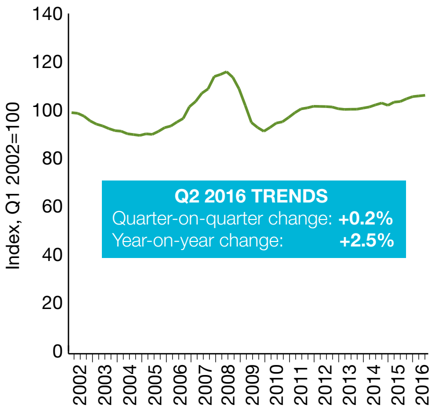


OCCUPIER TRENDS | INVESTMENT TRENDS | MARKET INDICATORS

EUROPEAN OUTLOOK

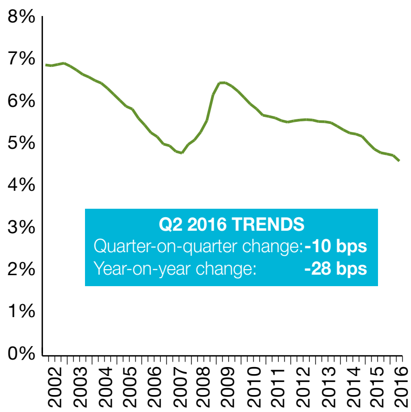
European investment volumes fell in Q2, largely due to slower activity in the UK and Germany.

FIGURE 1
European prime office rental index



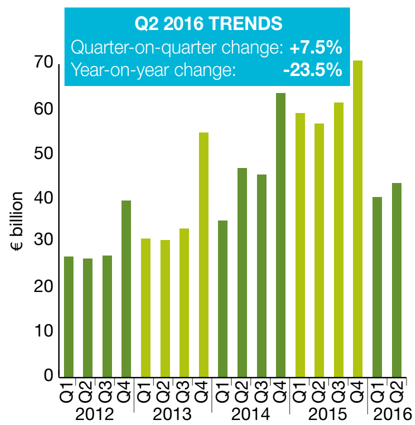
Source: Knight Frank Research

FIGURE 2
European weighted average prime office yield



Source: Knight Frank Research

FIGURE 3
European commercial property investment volumes



Source: Real Capital Analytics / Knight Frank Research

A total of €43.7 billion was invested in European commercial property during Q2 2016. Although this was an improvement on the weak performance of Q1, it was 23.5% down on the corresponding quarter of 2015 and confirmed the more subdued pace of investment activity being set in 2016.

The fall in investment in Q2 was primarily due to decreased activity in Europe's two largest markets; on a year-on-year basis, volumes were down by 50.1% in the UK and by 47.2% in Germany. However, other European markets showed more positive trends and Q2 volumes were up, year-on-year, in countries including France (+18.5%), Italy (+94.6%), Poland (+43.6%), Spain (+51.3%) and Sweden (+83.2%).

The reduced activity in the UK during Q2 reflected investor caution in the run-up to June's referendum on EU membership. The vote to leave has added to an already uncertain outlook and, as investors assess the impact of Brexit, UK investment activity is likely to remain subdued over the remainder of 2016. However, some international investors will see opportunities created by the depreciation of the UK pound and possible outward yield shifts.

Several major transactions have been agreed or completed in continental Europe since the Brexit vote, indicating that there is an ongoing investor appetite for European real estate. In one of the year's largest deals, for example, Amundi has agreed to purchase an €875 million European office portfolio from KanAm.

Investors continue to have large volumes of capital allocated to real estate, and this money may increasingly be targeted at prime assets in core continental European cities, as investors become more risk averse in light of economic and political uncertainties. Low interest rates and bond yields will continue to support property investment activity, with central bank interest rates expected to stay lower for longer in the aftermath of the Brexit decision.

Despite the lower level of overall transaction volumes, prime yields remained under downward pressure in a significant number of European markets in Q2, pushing the Knight Frank European Weighted Average Prime Office Yield to a record low of 4.62%. Prime office yields hardened in markets including Amsterdam, Brussels, Madrid and Paris, but softened by 25 basis points in London (City).

Occupier market activity has remained strong across a range of European cities, with aggregate office take-up in the major markets monitored by Knight Frank up by 5.4% in Q2 2016 compared with the same quarter of 2015. However, only a handful of major markets, including Berlin and Madrid, recorded prime office rental growth in Q2.

There has been considerable press attention on the potential impact of the Brexit decision on European occupier markets, with cities such as Frankfurt, Paris and Dublin touted as possible beneficiaries should companies decide to relocate staff from London. However, for the time being, most occupiers appear to be in "wait and see" mode as they monitor how the UK's withdrawal from the EU plays out. There is no evidence, as yet, of any significant exodus of occupiers from London, but the UK's exit from the EU will be factored into occupiers' decision-making over the longer term.

A more immediate impact to occupier demand could come from any economic slowdown caused by Brexit. Most forecasters have made substantial downward revisions to their UK GDP forecasts, with smaller revisions made to Eurozone forecasts. However, Purchasing Managers Index surveys released since the Brexit vote have provided evidence of a slight strengthening of Eurozone economic activity, indicating that contagion to countries outside the UK may be limited.

MARKET HIGHLIGHTS

1 BRUSSELS

Following a subdued 2015, the Brussels office market was much more active in the first half of 2016, with take-up boosted by several major public sector deals. The largest was the City of Brussels' pre-lease of AG Real Estate's Brucity project, which has a gross floor area of 37,200 sq m.

2 DUBLIN

In one of the biggest single-asset deals ever in Ireland, Blackstone has agreed to the purchase of the Blanchardstown Centre retail complex for a reported €950 million, in a deal expected to close over the summer.

3 FRANKFURT

GEG German Estate Group acquired the International Business Campus (IBC) for €400 million in Q2, in the largest deal of the year to date in Frankfurt.

4 LONDON

Central London office take-up reached just over 221,000 sq m in Q2, making it the weakest quarter since Q3 2012. The vacancy rate shifted upwards from 5.0% to 6.1%.

5 MADRID

Madrid office take-up came to approximately 220,000 sq m in H1 2016, a slight increase on H1 2015, despite an absence of large deals over 10,000 sq m. Prime rents edged upwards by 1.9% in Q2.

6 MOSCOW

The Moscow office vacancy rate fell from 19.1% to 17.6% in Q2, and availability is expected to continue to decrease in light of a much reduced development pipeline for 2016-2017.

7 PARIS

Office take-up in the Île de France market reached approximately 1.16 million sq m in H1 2016, 27% up on the same period of 2015. Five deals of over 20,000 sq m were recorded in H1.

8 WARSAW

A record-breaking 350,000 sq m of new office space was delivered to the Warsaw market in H1 2016, pushing up the vacancy rate to 15.4%.

FIGURE 4
Brexit impact Five cities that could benefit from occupier relocations from London

FRANKFURT

+	−
Established European financial centre Home to the European Central Bank and Deutsche Börse Significant amount of available office space	Relatively small city with limited cultural appeal Shortage of housing for relocated staff

VERDICT: The most likely city to attract any large financial sector occupiers relocating from London, albeit employees may feel it lacks the appeal of larger cultural centres such as London or Paris.

BERLIN

+	−
Growing centre for the creative industries Appealing lifestyle for young professionals Low office rents and housing costs	Less prosperous than other major German cities Relatively high unemployment

VERDICT: Berlin is already London's main rival as Europe's premier tech location, and is in pole position to attract any tech companies and fintech groups looking to relocate.

DUBLIN

+	−
English-speaking city with cultural similarities to London Growing reputation as a tech location Favourable corporate fiscal environment	Small office market with limited available space Rents significantly high and approaching their peak Shortage of housing for relocated staff

VERDICT: As the only remaining English-speaking capital city in the EU, Dublin will be well placed to pick up demand from any UK and US companies seeking to retain an EU presence.

PARIS

+	−
Major global city with huge cultural appeal Established headquarters location for global businesses Largest office market in continental Europe	Relatively high office rents Limited availability of office space in central locations High tax rates for top earners

VERDICT: Paris is the only European city that rivals London's status as a tier-1 global city and is an obvious option for companies looking to relocate.

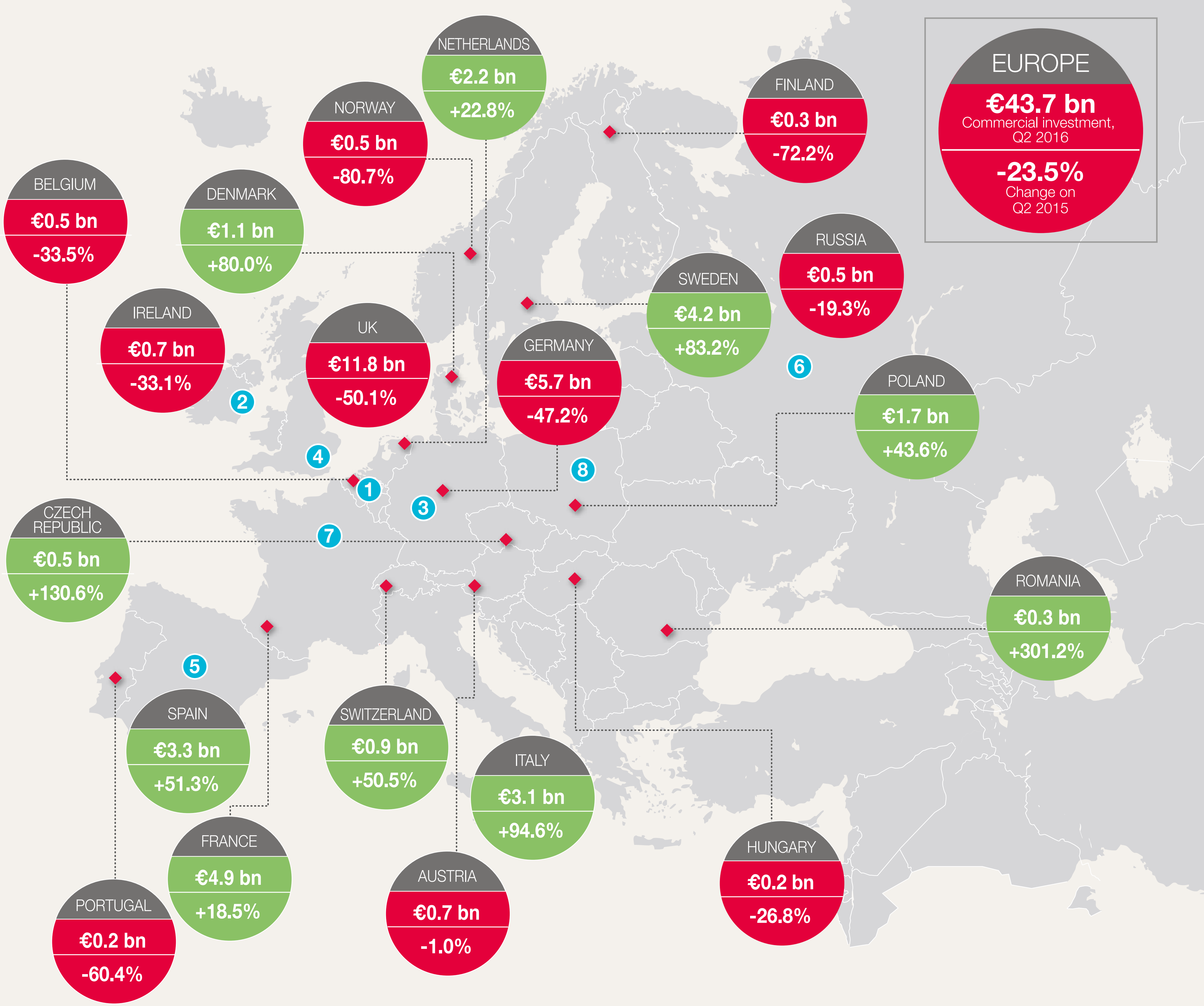
AMSTERDAM

+	−
Well-connected European gateway location Strong digital connectivity Well-educated, largely English-speaking labour force	Relatively small office market Banks may be detered by caps on bonuses

VERDICT: While unlikely to attract big banking and financial occupiers, Amsterdam may have success by targeting niches such as the fintech sector.

Source: Knight Frank Research

FIGURE 5
European commercial property investment volumes, Q2 2016



Source: Real Capital Analytics / Knight Frank Research
Investment volumes comprise office, retail, industrial and hotel transactions

EUROPEAN MARKET INDICATORS

During Q2, prime office yields hardened by 25 basis points in Amsterdam and Paris, and by 50 basis points in Brussels and Warsaw.

Commercial property prime rents and yields

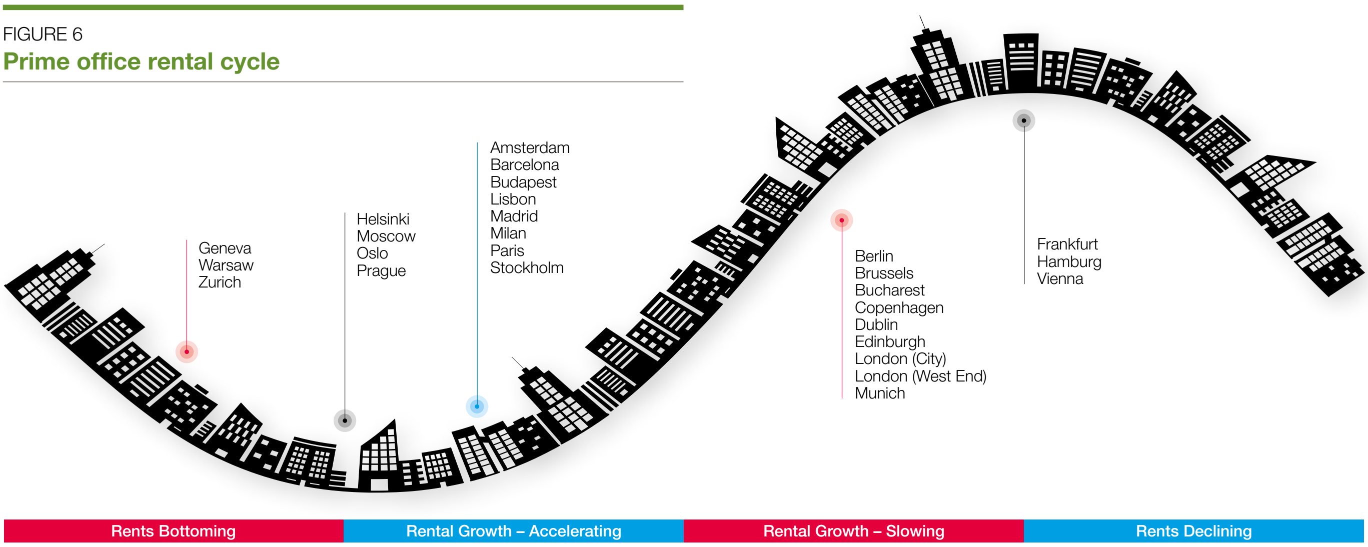
City	Offices Prime rents (€/sq m/yr)	Offices Prime yields (%)	Logistics Prime rents (€/sq m/yr)	Logistics Prime yields (%)	Shopping centres Prime rents (€/sq m/yr)	Shopping centres Prime yields (%)	Retail warehousing Prime rents (€/sq m/yr)	Retail warehousing Prime yields (%)
Amsterdam	340 ▲	4.75 ▼	85 ▶	5.75 ▼	1,000 ▶	5.25 ▶	135 ▶	5.75 ▼
Barcelona	255 ▲	4.50 ▼	59 ▶	6.85 ▼	552 ▶	5.00 ▶	120 ▶	6.00 ▶
Berlin	312 ▲	3.90 ▼	69 ▶	5.50 ▼	1,380 ▶	4.25 ▼	150 ▶	5.50 ▼
Brussels	300 ▶	5.00 ▼	55 ▶	6.50 ▶	1,800 ▶	5.25 ▶	185 ▶	5.75 ▶
Bucharest	216 ▶	7.50 ▶	45 ▶	9.00 ▶	720 ▶	7.75 ▶	120 ▶	9.50 ▶
Budapest	258 ▲	7.00 ▼	42 ▶	8.50 ▼	1,140 ▶	6.75 ▼	90 ▶	7.75 ▼
Copenhagen	241 ▶	4.00 ▼	77 ▶	6.25 ▶	697 ▶	5.00 ▼	164 ▶	6.50 ▶
Dublin	619 ▶	4.50 ▶	75 ▶	5.25 ▼	3,100* ▶	5.00 ▼	290 ▶	5.25 ▼
Edinburgh	429 ▶	5.25 ▶	98 ▲	6.25 ▶	2,732* ▶	5.00 ▶	390 ▲	6.00 ▲
Frankfurt	462 ▶	4.25 ▼	80 ▶	5.25 ▼	1,560 ▶	4.20 ▼	170 ▶	5.50 ▼
Geneva	690 ▼	3.25 ▶	183 ▶	5.75 ▶	1,041 ▶	4.00 ▼	164 ▶	5.25 ▶
Hamburg	300 ▶	3.90 ▼	72 ▶	5.50 ▼	1,650 ▶	4.25 ▼	150 ▶	5.50 ▼
Helsinki	396 ▶	4.25 ▼	120 ▼	6.00 ▶	1,200 ▶	4.75 ▼	120 ▼	6.25 ▶
Lisbon	222 ▲	5.25 ▼	45 ▶	7.00 ▼	1,140 ▶	5.25 ▼	108 ▶	7.25 ▶
London	1,495(WE) ▶ 911 (City) ▶	3.50 (WE) ▶ 4.25 (City) ▲	182 ▲	4.25 ▶	5,789* ▶	4.25 ▶	611 ▶	4.50 ▲
Madrid	330 ▲	3.90 ▼	59 ▶	6.85 ▼	530 ▶	5.00 ▶	132 ▶	6.00 ▶
Milan	500 ▶	4.50 ▶	50 ▶	7.00 ▶	850 ▶	5.50 ▶	300 ▶	6.75 ▶
Moscow	720 ▶	10.00 ▼	65 ▶	12.50 ▶	3,152 ▶	10.75 ▶	N/A	N/A
Munich	414 ▶	3.50 ▼	83 ▲	5.20 ▼	1,900 ▶	3.90 ▼	180 ▶	5.00 ▼
Oslo	452 ▶	4.25 ▶	128 ▶	5.50 ▶	1,262 ▶	4.75 ▶	137 ▶	6.00 ▶
Paris	760 ▲	3.25 ▼	58 ▶	5.75 ▼	2,500 ▲	3.75 ▼	180 ▶	5.00 ▼
Prague	234 ▶	5.50 ▶	48 ▶	6.50 ▼	840 ▶	5.25 ▼	120 ▶	7.50 ▶
Stockholm	590 ▲	3.75 ▼	113 ▶	5.75 ▼	851 ▶	4.50 ▼	225 ▶	5.75 ▼
Vienna	309 ▶	4.40 ▶	72 ▶	7.00 ▶	1,320 ▶	5.10 ▼	168 ▶	6.00 ▶
Warsaw	276 ▶	5.50 ▼	60 ▶	7.00 ▶	1,800 ▲	5.50 ▼	132 ▶	7.50 ▶
Zurich	713 ▼	3.25 ▶	228 ▶	5.50 ▶	1,369 ▶	4.00 ▼	183 ▶	5.00 ▶

Indicative prime yields, as quoted locally, based upon a hypothetical Grade A unit. Office rents are for prime city area Grade A space, 2,000 sq m. Shopping Centre rents are based on prime covered shopping malls, quoted on best position, 100 sq m units. Retail Warehouse rents are for units of 1-5,000 sq m located in purpose built parks. Typical Retail Warehouse schemes vary between countries. Logistics rents are for prime industrial space of units over 5,000 sq m. The data above is provided for general reference purposes only. Local market conditions will vary. *Zoned/weighted figure. Arrows provide a broad indication of recent movements and the short-term outlook for prime rents and yields. London office data is quoted for the West End (WE) and City (C) submarkets.

Source: Knight Frank Research

FIGURE 6

Prime office rental cycle



The above diagram is intended to provide a comparative guide to the current positions of European prime office markets in their rental cycles. Markets will move through their cycles at different speeds and, sometimes, in different directions. The positions indicated in the diagram do not constitute formal forecasts of future rental trends.

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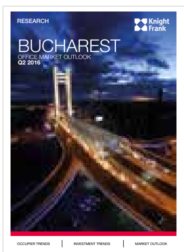
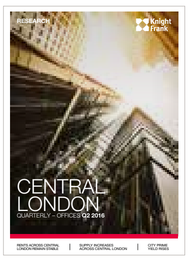
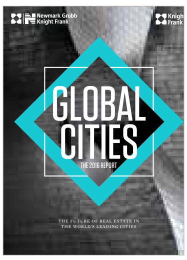


Bucharest Office Market Outlook Q2 2016



Central London Quarterly Q2 2016



Global Cities 2016

Vienna Office Market Outlook Q2 2016

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