

RESEARCH

A nighttime photograph of a city skyline reflected in water. A large, illuminated skyscraper with a unique, curved facade is the central focus on the right. To the left, a bridge with a dark, arched structure spans across the water. The city lights are reflected in the calm water, creating a shimmering effect. The sky is a deep blue with some clouds.

# EUROPEAN QUARTERLY

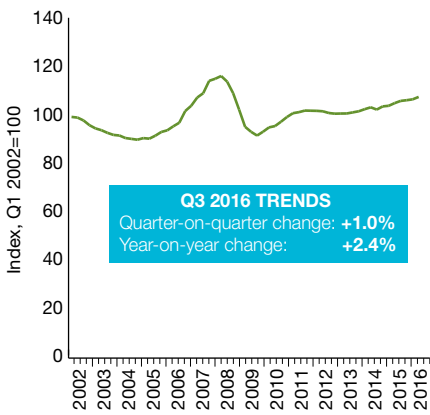
COMMERCIAL PROPERTY OUTLOOK  
**Q3 2016**

OCCUPIER TRENDS

INVESTMENT TRENDS

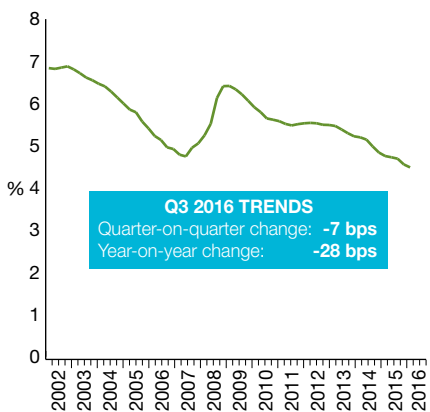
MARKET INDICATORS

FIGURE 1  
European prime office rental index



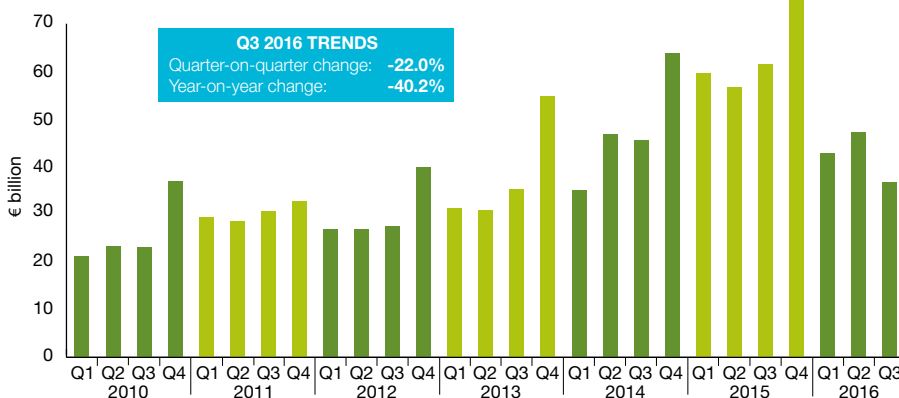
Source: Knight Frank Research

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

# EUROPEAN OUTLOOK

European investment activity slowed further in Q3, although volumes held up more strongly outside the core markets.

A total of €37.1 billion was invested in European commercial property in Q3 2016, making it the weakest quarter since Q1 2014, and 40.2% down year-on-year. Investment volumes for the first three quarters of 2016 reached €128.0 billion, 28.7% below Q1-Q3 2015.

The fall in European investment in 2016 has been largely a result of decreased activity in Europe's three biggest markets, with transaction volumes for the first three quarters down substantially in the UK, Germany and France. While the decline in UK volumes can be partly attributed to investors' uncertainties over the impact of Brexit, the falls in German and French volumes are indicative of wider investor caution and the increased difficulty of sourcing attractive stock in core markets.

Excluding the "big three" markets, investment volumes in the first three quarters were down by a more modest 11.3% in the rest of Europe. Pockets of investment growth were seen in countries such as Finland, Poland and Spain.

Initial indications suggest that investment volumes will surge in Q4, with several large portfolio deals due to be concluded by the year-end. Nonetheless, full-year European investment volumes for 2016

will clearly be some way below the high-water mark set in 2015.

The current year should not, however, necessarily be seen as the start of a longer downturn in volumes. Sentiment towards the sector remains broadly positive, and a recent Knight Frank survey found that 68% of the polled investors expect European investment demand to either stabilise or increase in 2017.

Pricing levels remain robust despite the lower transactional activity seen in 2016. During Q3, the Knight Frank Weighted Average Prime Office Yield hardened by a further 7 basis points to a record low of 4.55%. The most significant inward yield shifts came in regions such as the Benelux and CEE, where yield compression has lagged core markets. However, prime office yields also came down by 25 basis points in Paris, to a new low of 3.00%. Sub-4% yields in core European markets remain attractive to many investors in the current low interest rate environment.

Occupier market activity slowed a little in Q3, with aggregate office take-up in the European markets monitored by Knight Frank decreasing by 5% year-on-year. This was partly due to relatively slow leasing activity in London and Madrid. However, total European take-up for the first three quarters of 2016 remained 4% above 2015 levels and cities including Berlin, Brussels, Dublin, Paris and Vienna are all on course to out-perform 2015.

Q3 proved to be a strong quarter for office rental growth, reflecting both the robust occupier demand and diminishing supply levels in European CBDs. The Knight Frank European Prime Office Rental Index rose by 1.0% during Q3, driven by quarterly increases in markets such as Berlin (+7.7%), Stockholm (+7.3%), Dublin (+4.3%) and Paris (+1.3%). Conversely, prime rents decreased by 4.3% in London (West End), reflecting hesitant demand at the very top end of the UK market following the Brexit vote.

## MARKET HIGHLIGHTS

<p><b>AMSTERDAM</b> 1</p> <p>Finnish pension fund Ilmarinen has made its debut in the Dutch investment market by acquiring a 50% share in the Piet Hein Buildings in central Amsterdam.</p>	<p><b>MADRID</b> 6</p> <p>In one of the biggest single-asset office deals in Europe this year, the Torre Cepsa building has been purchased by Pontegadea Inmobiliaria, the property arm of Zara founder Amancio Ortega, for a reported €490 million.</p>
<p><b>BRUSSELS</b> 2</p> <p>The outstanding deal of a relatively quiet Q3 saw Allianz acquire for its own occupation a 26,600 sq m office tower, which will be developed as part of ImmoBel's Möbius project in north Brussels.</p>	<p><b>MILAN</b> 7</p> <p>Cross-border capital continues to target Milan, with the largest investment transaction of Q3 being AXA's purchase of the Via Monterosa 91 office building for approximately €220 million.</p>
<p><b>DUBLIN</b> 3</p> <p>Following a very active Q3 for the Dublin office market, prime rents have reached the benchmark of €60 per sq ft per annum for the first time since 2008.</p>	<p><b>MOSCOW</b> 8</p> <p>Office market activity remains subdued in Moscow. There was a slight increase in the already-high Class A vacancy rate in Q3, as cost-saving companies made space available for subleasing.</p>
<p><b>FRANKFURT</b> 4</p> <p>In potentially the biggest investment deal of the year in Frankfurt, Patrizia has confirmed that it is acquiring the Commerzbank Tower on behalf of South Korea's Samsung Group, for a price reportedly in the region of €730 million.</p>	<p><b>PARIS</b> 9</p> <p>Prime office rents edged upwards to €770 per sq m per annum in Q3, as limited development activity continued to create a supply squeeze, particularly in the CBD where the vacancy rate dropped to 3.8%.</p>
<p><b>LONDON</b> 5</p> <p>Central London office take-up remained below the long-term average in Q3, with Brexit impacting activity. However, the market received a major boost from Apple's decision to pre-lease more than 46,000 sq m for a new UK headquarters at Battersea Power Station.</p>	<p><b>WARSAW</b> 10</p> <p>The developer HB Reavis has agreed the €186 million sale of Gdanski Business Center in Warsaw to Savills Investment Management, which is reported to be acting on behalf of the Malaysian pension fund EPF.</p>

FIGURE 4  
European investor sentiment

Knight Frank recently took a snapshot of investor sentiment, polling 150 European-focused clients at its annual European Breakfast event. The results showed that sentiment towards the sector remains largely positive and that logistics is increasingly a sector of choice.

**INVESTORS' PREFERRED LOCATIONS**

**INVESTORS' PREFERRED SECTORS**

- 34% LOGISTICS & INDUSTRIAL
- 28% OFFICE
- 19% SPECIALIST (Automotive/Student/Healthcare)
- 15% RETAIL
- 5% HOTEL

**INVESTORS' EXPECTATIONS FOR EUROPEAN PROPERTY DEMAND IN 2017**

68% expect demand for European property to either stay the same or increase in 2017

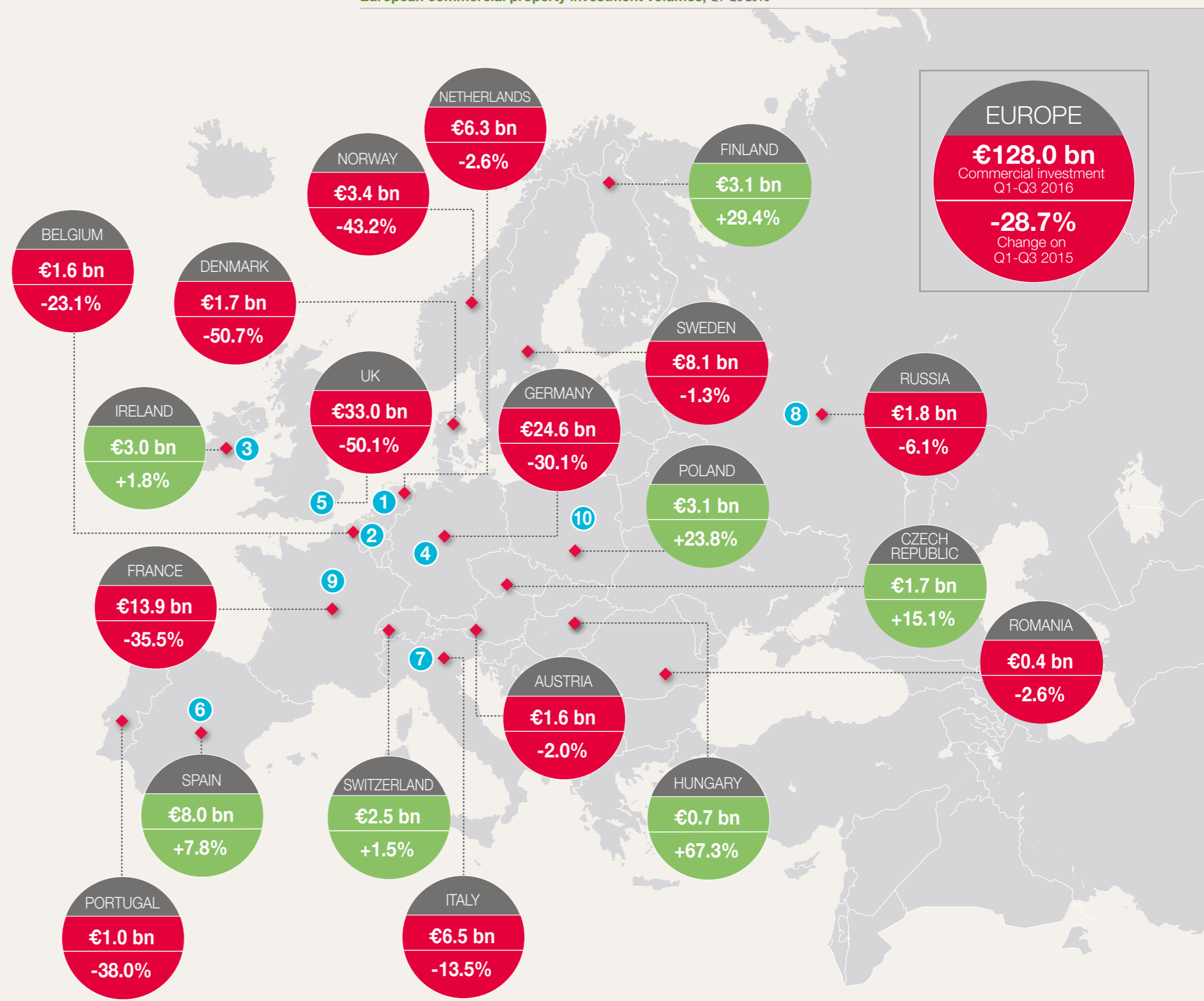
- 29% NO CHANGE
- 32% WEAKER DEMAND
- 39% STRONGER DEMAND

**INVESTORS' EXPECTATIONS FOR EUROPEAN PRIME OFFICE YIELDS IN 2017**

81% expect European prime yields to either stabilise or harden in 2017

- 19% YIELDS TO SOFTEN
- 40% YIELDS TO REMAIN STABLE
- 41% YIELDS TO HARDEN

FIGURE 5  
European commercial property investment volumes, Q1-Q3 2016



Source: Knight Frank European Breakfast Poll. Sector and location results assume a 3-5 year hold period

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



# EUROPEAN MARKET INDICATORS

Berlin has been Europe’s rental growth hotspot over the last 12 months, with prime office rents rising 19.1% year-on-year.

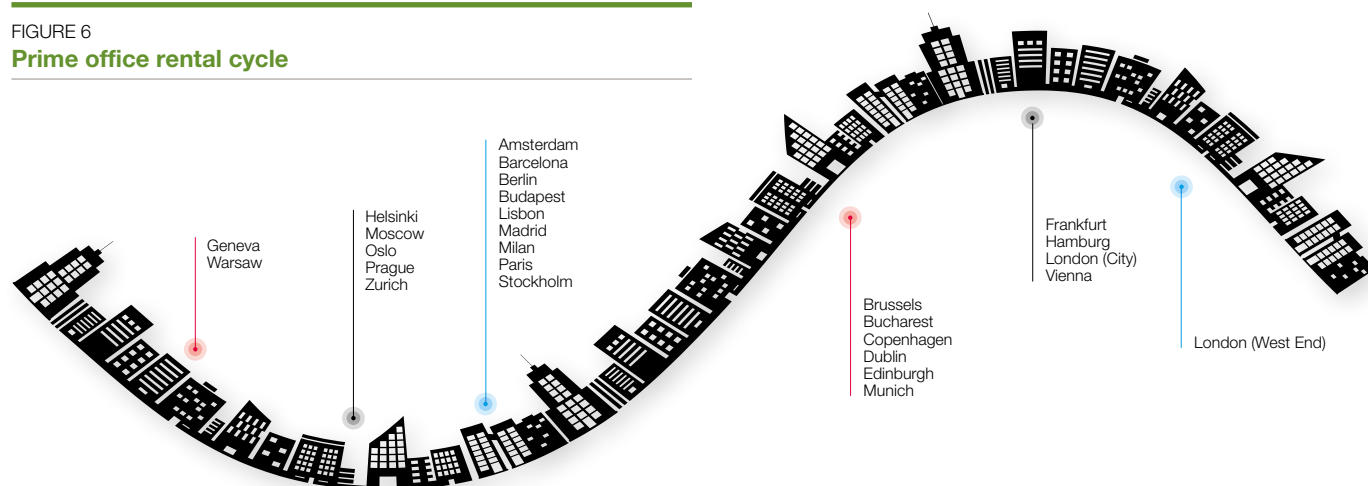
## Commercial property prime rents and yields

City	Offices		Logistics		Shopping centres		Retail warehousing	
	Prime rents (€/sq m/yr)	Prime yields (%)	Prime rents (€/sq m/yr)	Prime yields (%)	Prime rents (€/sq m/yr)	Prime yields (%)	Prime rents (€/sq m/yr)	Prime yields (%)
Amsterdam	365 ▲	4.50 ▼	85 ▶	5.75 ▶	1,000 ▶	5.25 ▶	135 ▶	5.75 ▶
Barcelona	255 ▲	4.50 ▼	66 ▲	6.50 ▼	552 ▶	4.75 ▼	129 ▲	6.00 ▶
Berlin	336 ▲	3.75 ▼	69 ▶	5.50 ▼	1,380 ▶	4.00 ▼	150 ▶	5.50 ▶
Brussels	300 ▶	5.00 ▶	55 ▶	6.25 ▼	1,800 ▶	5.25 ▶	185 ▶	5.75 ▶
Bucharest	216 ▶	7.50 ▶	48 ▲	8.75 ▼	720 ▶	7.50 ▼	120 ▶	9.50 ▶
Budapest	258 ▲	6.75 ▼	42 ▶	8.25 ▼	1,140 ▶	6.50 ▼	90 ▶	7.75 ▶
Copenhagen	242 ▶	4.00 ▶	77 ▶	6.25 ▶	698 ▶	5.00 ▶	164 ▶	6.25 ▶
Dublin	646 ▲	4.50 ▶	75 ▶	5.25 ▶	3,100* ▲	5.00 ▶	290 ▲	5.25 ▶
Edinburgh	450 ▲	5.25 ▲	101 ▶	6.50 ▲	2,960* ▶	5.00 ▲	404 ▲	6.00 ▲
Frankfurt	462 ▶	4.25 ▼	80 ▶	5.25 ▼	1,560 ▶	4.00 ▼	170 ▶	5.50 ▶
Geneva	577 ▶	3.25 ▶	154 ▶	5.75 ▶	876 ▶	4.00 ▶	138 ▶	5.25 ▶
Hamburg	300 ▶	3.75 ▼	72 ▶	5.25 ▼	1,650 ▶	4.00 ▼	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 ▶	7.00 ▼
London	1,480 (WE) ▼ 940 (City) ▶	3.50 (WE) ▶ 4.25 (City) ▶	188 ▶	4.50 ▲	5,987* ▶	4.25 ▶	632 ▶	4.50 ▲
Madrid	333 ▲	3.90 ▼	59 ▶	6.50 ▼	556 ▶	4.75 ▼	156 ▶	5.80 ▼
Milan	500 ▶	4.50 ▶	50 ▶	7.00 ▶	850 ▶	5.50 ▶	300 ▶	7.00 ▶
Moscow	613 ▶	10.00 ▶	55 ▶	12.50 ▶	2,682 ▶	10.50 ▶	N/A	N/A
Munich	420 ▲	3.50 ▼	85 ▲	5.20 ▼	1,900 ▶	3.90 ▼	180 ▶	5.00 ▶
Oslo	524 ▶	4.00 ▼	149 ▶	5.50 ▶	1,463 ▶	4.75 ▶	158 ▶	6.00 ▶
Paris	770 ▲	3.00 ▼	58 ▶	5.75 ▼	2,500 ▶	4.00 ▶	180 ▶	5.00 ▶
Prague	234 ▶	5.25 ▼	48 ▶	6.50 ▶	1,380 ▶	5.25 ▶	120 ▶	7.50 ▶
Stockholm	635 ▲	3.75 ▼	113 ▶	5.75 ▼	854 ▶	4.50 ▼	226 ▶	5.75 ▼
Vienna	309 ▶	4.25 ▼	72 ▶	7.00 ▶	1,320 ▶	4.95 ▼	168 ▶	5.85 ▼
Warsaw	288 ▶	5.25 ▼	60 ▶	7.00 ▶	1,800 ▶	5.50 ▶	132 ▶	7.50 ▶
Zurich	615 ▶	3.00 ▼	192 ▶	5.50 ▶	1,153 ▶	4.00 ▶	154 ▶	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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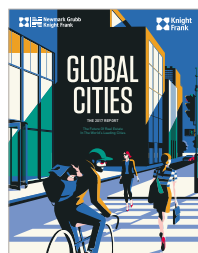
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