Press release

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A temporary break… before the great end-of-year rush

Knight Frank analyses the French corporate real estate market at the end of Q3 2018

Following a first half of the year that was close to record levels, investment activity stalled during Q3 2018. "*3.6 billion euros was invested in France over the last three months, equating to decreases of 54% compared to the previous quarter and 33% compared to Q3 2017.* ***Even so, investment volumes since January have reached 15.4 billion euros, 3% above investment levels recorded over the same period last year****"* announces Vincent Bollaert, Head of Investment at Knight Frank France.

In spite of a less favourable economic context, and investment activity that was sometimes limited by lack of supply, the French market remained dynamic due to the combination of favourable factors (abundance of cash to be invested, increasing popularity of certain asset types, significant interest for areas subject to the Grand Paris project, etc.). **The strength of lettings activity also worked in favour of the investment market.** "*Almost 2 million sq m of offices have already been let in the Greater Paris Region since January, whilst the vacancy rate in Paris is around 2%; these figures illustrate the solidity of Europe's leading office market and enable investors to anticipate further rent increases"* continues Vincent Bollaert.

More than 11 billion euros invested in the Greater Paris Region

Large transactions were few in number in Q3 2018 but nevertheless played a key role. There have been 44 deals over 100 million euros since the start of 2018, all asset types included, totalling 9 billion euros and 59% of all investment volumes. As usual, these deals primarily took place in the Greater Paris Region where the market showed strong results. Since January, **investment volumes in the Greater Paris Region thus reached 11.4 billion euros** (+ 7 % year-on-year), of which 85% was for office deals.

Offices: a temporary slowdown

Despite a significant slowdown during the 3rd quarter, offices still account for the majority of French investment volumes (71 %). This market sector has seen investment volumes of **almost 11 billion euros since the start of 2018, an increase of 9% year-on-year and 42% compared to the ten-year average.** Whilst transactions over 100 million euros have been few in number during the 3rd quarter (8, compared to 27 during the 1st quarter), they remain the driving force behind investment activity. With a cumulative volume of 7 billion euros, this size of deal accounts for 64% of investment volume in the French office market since January.

Paris itself still comprises a significant proportion of deals, accounting for 52% of the 9.7 billion euros invested in offices in the Greater Paris Region since the beginning of 2018. Investment activity is primarily concentrated in the CBD, where a deal was recently completed for more 400 million euros. Other areas have also been targeted by investors, as illustrated by the sale of "Atrium Bercy" (Paris 12th district) to GENERALI. Outside of Paris, large deals were few in number during the 3rd quarter, but nevertheless confirmed the **increasing appetite of investors for certain areas subject to developments in the north and south of the Greater Paris Region** ("Network I" in Bagneux, bought by LBO FRANCE, etc.). The most established office hubs to the West of Paris still account for a good proportion of investment activity. Since January, Neuilly-Levallois and the Southern Loop thus total 37% of office investment volumes outside of the capital. This relatively high share contrasts with the low level of sums invested in La Défense, where the summer period was primarily driven by the purchase of "Curve" in Puteaux by MONCEAU ASSURANCES. That being said, several large or very large deals are ongoing, and their completion will mark the business district's return to the forefront.

Office investment volumes in the regions since January totalled 1.2 billion euros, a decrease of 23% year-on-year. Investment activity took place in a limited number of geographical sectors. **The Rhône-Alpes region thus comprised 39% of regional office investment volumes.** Following the sale of the CASINO headquarters in Saint-Etienne during the 2nd quarter, Lyon reaffirmed its domination during the 3rd quarter with several large deals of between 20 and 50 million euros. It is a French investor that will take centre stage during the 4th quarter, with the expected completion of the sale of two of GECINA'S regional office portfolios, thus implementing the property company's strategy of refocusing their portfolio in the main Greater Paris Region office hubs.

Retail: the year of the high street

Almost 600 million euros were invested in French retail during Q3 2018, taking the **2018 total to date to 2.2 billion euros**. This total equates to 14% of French corporate real estate investment activity and reflects an increase of 11% compared to the same period last year. "*Whilst volumes have increased, it is due to the completion of the sale of the future Apple Store on the Champs Elysées to Hines during the 2nd quarter. The concentration of activity in a few major transactions is moreover one of the main characteristics of 2018,* ***with five transactions of more than 100 million euros which alone account for 48% of retail investment volumes****"* notes Antoine Grignon, Head of Retail at Knight Frank France.

During the 3rd quarter, the sale of "65 Croisette" in Cannes by THOR EQUITIES was added to the four large deals of the first half of the year, confirming the domination of high streets. "*High street assets remain sought-after by investors. Over the first nine months of 2018, investment volumes in this asset class totalled 1.25 billion euros, which is 58% of all French retail investment"* continues Antoine Grignon. Investors continue to particularly target the most renowned retail pitches. Besides La Croisette in Cannes, rue Saint-Honoré in Paris also stands out. Following the acquisition of the new MOSHINO shop by GENERALI, several other large deals are ongoing on this ever more upmarket street, where almost 30% of all luxury retail openings in Paris in 2018 and 2019 are to be found.

Retail parks account for 26 % of French retail investment volumes since the start of 2018, equating to a total of 560 million euros, a decrease of 17 % year-on-year. This performance, however, is still respectable and was driven by the completion of brands and big boxes portfolio sales of varying sizes. Retail park acquisitions remain few in number due to a limited structural supply of latest generation assets that struggles to satisfy the large appetite of investors. Finally, the shopping centre market has been almost flat, with investment volumes of close to 350 million euros which is 16% of French retail investment volumes. Since the sale of "Grand Vitrolles" to CARMILA at the beginning of the year, deals can almost be counted on one hand; a tightening of the market which illustrates the lack of flagship shopping centres available for sale, and the **lack of investors' visibility as to the future of less prime assets.**

Upcoming sales of Parisian flagships, the expected completion of a MONOPRIX portfolio sale by CASINO and a few other large ongoing deals lead us to anticipate a much more active 4th quarter.

However, 2018 performance levels will probably not reach those seen in the last 5 years (5.4 billion euros invested on average between 2014 and 2017 in the retail market).

Industrial: an exceptional year

Following a record 2017, 2018 is set to be another exceptional year for the industrial sector. Last year, 4.5 billion euros were invested in France in this market sector, including 1.6 billion for an exceptional deal: the sale to CIC of the LOGICOR portfolio. **At the end of the 3rd quarter 2018, investment volumes have already reached 2.3 billion euros,** which is 15% of all investment activity in the French market. This high proportion is due to strong investor appetite for logistics assets. Warehouses in fact account for 91% of investment volumes in the industrial sector, due notably to the acquisition of various portfolios by foreign investors. Besides DWS, BLACKSTONE and GRAMERCY, GREENOAK has also recently been active in the market. Market activity has also benefitted from the completion of several individual asset sales; assets that are predominantly located within the large hubs on the North-South axis, but whose geographic breakdown also confirms the growing popularity of more remote sectors.

Foreign investors: Americans are in the lead

The French market remains primarily driven by French investors. However, their market share continues to decrease: all asset types included, **they "only" account for 53% of investment volumes since the beginning of 2018, compared to an average of 60 % over the last five years.** Foreign investors, who are active across all asset types, are behind some of the largest deals of the year. Americans account for the highest proportion of foreign investors and are particularly fond of logistics and Parisian office and retail assets, targeting both core and more opportunistic market sectors: since January they account for 17% of investment volumes, ahead of investors from the Euro zone. The latter account for 13 % of investment volumes and are primarily Germans who, having signed the largest deal of the year in Q2 (the sale to HINES for BVK of the future Apple Store on the Champs Elysées), have more recently positioned themselves on more modest sized and less core deals in Lyon and the Greater Paris Region (the sale of "New" in Asnières-sur-Seine to DEKA, etc.). Investors from outside of the Euro zone take third place (8 %): this group is primarily comprised of British investors who have notably signed a few medium sized deals in Q3.

Accounting for 44 % of investment volumes, investment funds continue to dominate the market, well ahead of SCPI/OPCIs (21 %), whose net collection is down 46% year-on-year as at the end of the 1st half 2018 but is still above the 10-year average. Finally, the share of insurance companies remains stable (20 %), driven by a few deals undertaken by GENERALI, as well as the completion of deal for more than 400 million euros in Paris.

Yields: limited decreases or increases

Prime yields remain stable for offices (between 3.00 and 3.25% in Paris CBD), even if **a decrease is still possible in certain sectors of the Greater Paris Region**. Yields for shopping centres (4.25%) and retail parks (5.00%) haven't seen significant changes over the last three months, and it is worth highlighting the very limited number of prime asset sales. Prime yields for Paris high street assets have been at their lower limit since 2016 but have recently seen slight upward pressure and currently stand at 2.90% (excluding exceptional deals or those on assets with reversionary potential). Finally, logistics yields until now were comprised between 4.75 and 5.00% but could soon reach the threshold of 4.50% in light of ongoing negotiations, confirming the popularity of this asset class.

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What can we expect in the coming months?

A general increase in yields is not expected in the short term due to high investor demand. Furthermore, Mario Draghi, President of the ECB, recently indicated that the bank would keep key interest rates at their current level until at least summer 2019. The spread thus remains favourable to the real estate sector which, combined with several other factors (anticipation of the new Franco-Luxembourg treaty, etc.), helps to explain the strength of the French market. Indeed, following a relatively calm 3rd quarter 2018, investment volumes should bounce back significantly during the 4th quarter, even if they don't necessarily reach the record level seen at the end of 2017 (13 billion euros). "*Deals over 200 million euros that are today subject to sales agreements or are under exclusive negotiations with an investor total almost seven billion euros. Given the dynamism of large deals,* ***investment volumes could thus reach at least 10 billion euros during the 4th quarter, and probably surpass 25 billion euros for the whole of 2018****" concludes* Vincent Bollaert.