RESIDENTIAL RESEARCH

Knight Frank

MADRID

LAND **2016**

SUPPLY | PRICES | DEMAND | OUTLOOK

HIGHLIGHTS

Investment in land and buildings exceeded €940 M and increased almost 10% y-o-y

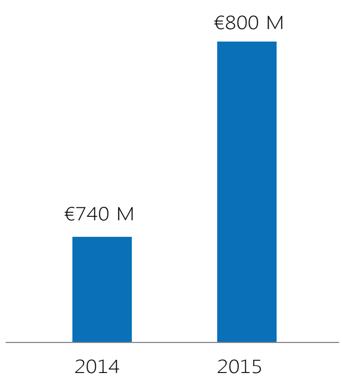
Over 750,000 sqm of serviced development land (suelo finalista) was sold in the metropolitan area of Madrid

Prices per sqm continue to trend upwards, in some specific cases reaching a 12% y-o-y increase

Appetite for development land is increasing amongst international investors who are looking for higher returns on their investments, and are attracted by the high yields currently offered by development land

Finance is gradually returning to the land market, with up to 40% of a scheme being financed, depending on the type of project and the purchaser

GRAPH 1
Land investment, Madrid



Source: Knight Frank

THE LAND MARKET IS BACK ON FORM, DESPITE UNCERTAINTY

The development land market has borne the full brunt of the financial and real estate crisis. The value of development land plummeted in value between 2008 to 2013, and it was in mid-2014 when we started to see things improve. The land market picked up in 2015, and is now back on developers and investors' radars once again. The number of serviced development land transactions has risen, which has pushed average prices per sqm up by as much as 12% in some developments in the north of Madrid.

2015 has been a complicated year in terms of politics. The changes in autonomous-local governments in H2 2015, the General Elections at the end of the year and the consequent political uncertainty which spilled over into the beginning of 2016 is likely to cause a slowdown in activity in the market. Nevertheless, investment in development land and refurbishment projects exceeded €940 million, which is a 5% y-o-y increase . And this increase in investment is even higher if we just focus on Madrid - where investment has risen by almost 10%.

Supply

Around 3.3 million buildable sqm of serviced development land is currently available in Madrid, which equates to approximately 30,000 homes. Nevertheless, within the M-30 ring road, there is just 320,000 sqm of buildable area. This means that 10% of space was taken in 2015 compared to 2014, although we would highlight that this could reach 500,000 sqm if planning consent is granted for additional plots of land over the coming 18 months.

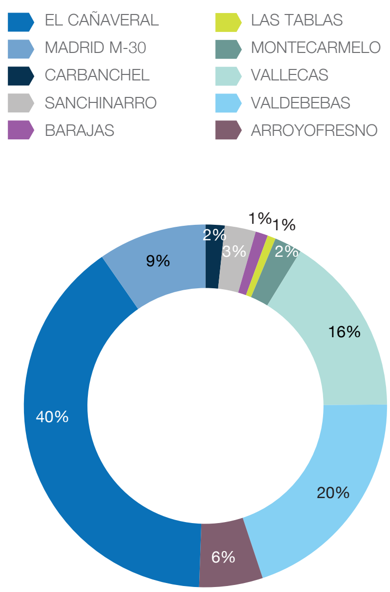
Land is starting to become more scarce in the Urban Development Areas ("PAUs") located in the north of Madrid e.g. Las Tablas, Montecarmelo and Sanchinarro. Supply is gradually falling - just 50% of land is available in Valdebebas and 35% of land in the Vallecas Urban Development Area. 40% of buildable area in Madrid is situated in the El Canaveral. Urban Development Area, which skews the total figure for the city of Madrid.

The lack of supply in some areas of the North of Madrid has pushed demand for land to areas located further south - to areas where land sales have been few and far between in recent years. In 2013 and 2014, the spotlight was firmly focused on Madrid, whereas in 2015, we saw land transactions take place outside of the M-40 ring road.

We would highlight some of the public sector's divestment transactions, such as the Parque Central de Ingenieros de Villaverde (APE 17.02), owned by SEPES, plots owned by Sareb and assets owned by Adif.

We would highlight pre-consented urban extensions including Distrito Norte, Campamento or Operación Mahou (Vicente Calderon). These will undoubtedly contribute to the majority of development land in the pipeline in Madrid, but which the planning authority is currently deliberating.

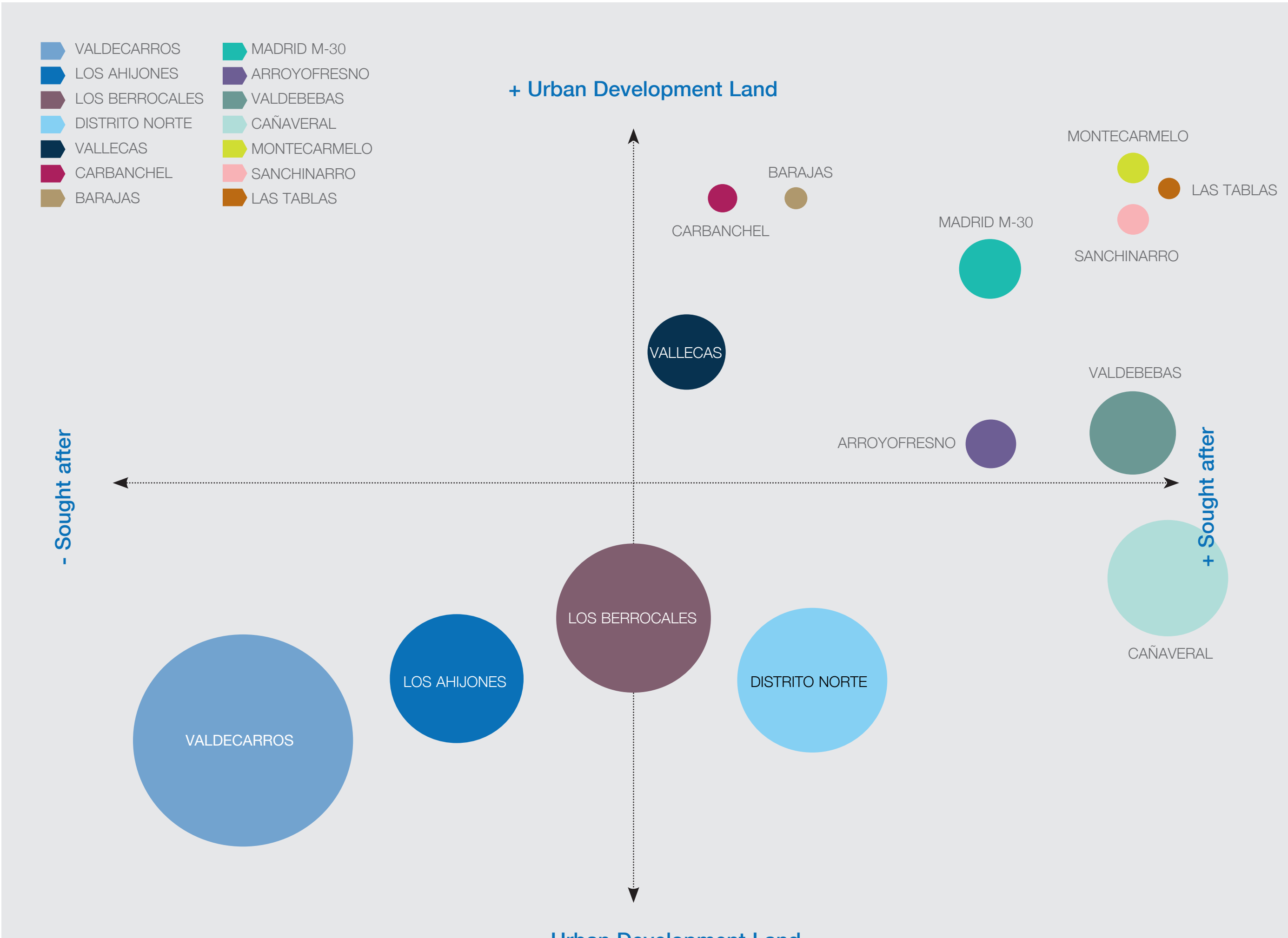
GRAPH 2
Available urban development



Source: Knight Frank

GRAPH 3

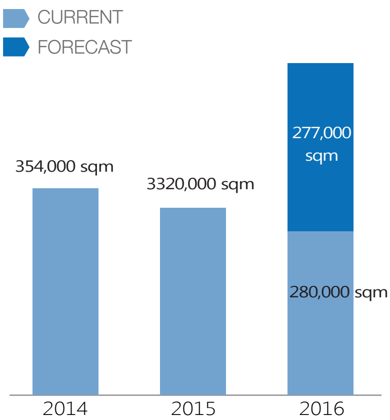
Distribution map: urban land and pre-consented land for the coming 10 years



Source: Knight Frank

GRAPH 4

Forecast for new available supply within the M-30 ring road



Source: Knight Frank

Prices

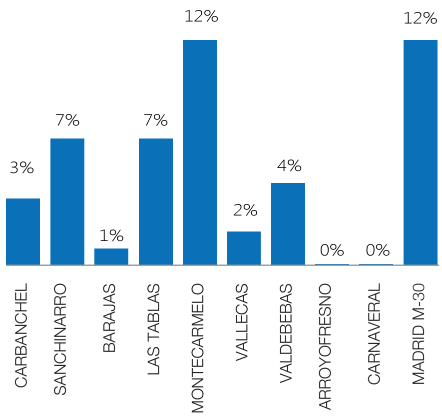
Urban landowners, who managed to stand their ground during the crisis, remain firm when it comes to their sales positions. Competition between purchasers (developers and investors versus cooperative managers) combined with subdued demand have sought to bolster prices.

However, prices per sqm have risen in the most developed areas, with increases of up to 12% y-o-y in the Urban Development Areas (PAUs) in the north of Madrid, such as Montecarmelo for instance.

Within the M-30, we would note that prices per sqm for serviced development land are around €1,800, and prices per sqm for refurbishment projects are around €2,900.

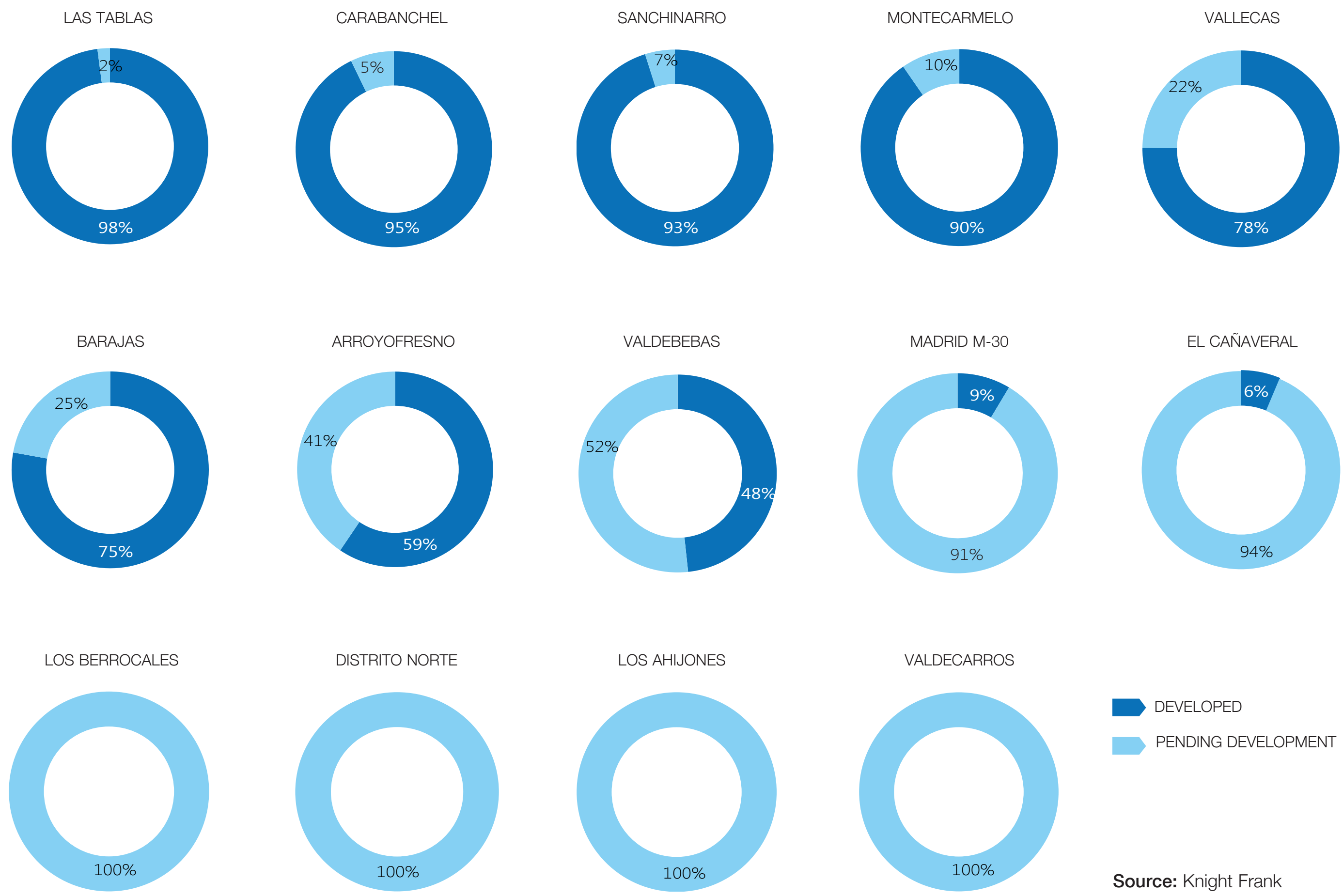
GRAPH 5

Percentage change in prices per sqm by area 2014 vs 2015



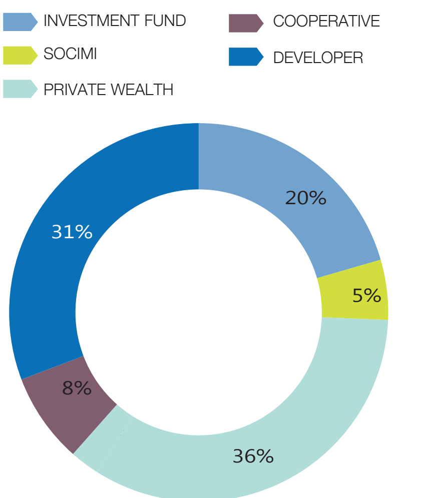
Source: Knight Frank

GRAPH 6
Level of development per area



Source: Knight Frank

GRAPH 7
Type of investor



Source: Knight Frank

Demand

The current state of the market has attracted land buyers who are looking to position themselves in the market as developers and promoters in the short and medium-term.

In this regard, demand has been characterised by the appearance of value-add purchasers who are looking to add value via their transactions.

International investors, who are looking for greater returns on their investments, have an appetite for development land as it an asset that produces more favourable yields.

However, local developers are coming back on to the scene, in some cases via joint ventures with international funds, who are looking for plots of land in developed areas with limited new-build supply, or on schemes that are less developed.

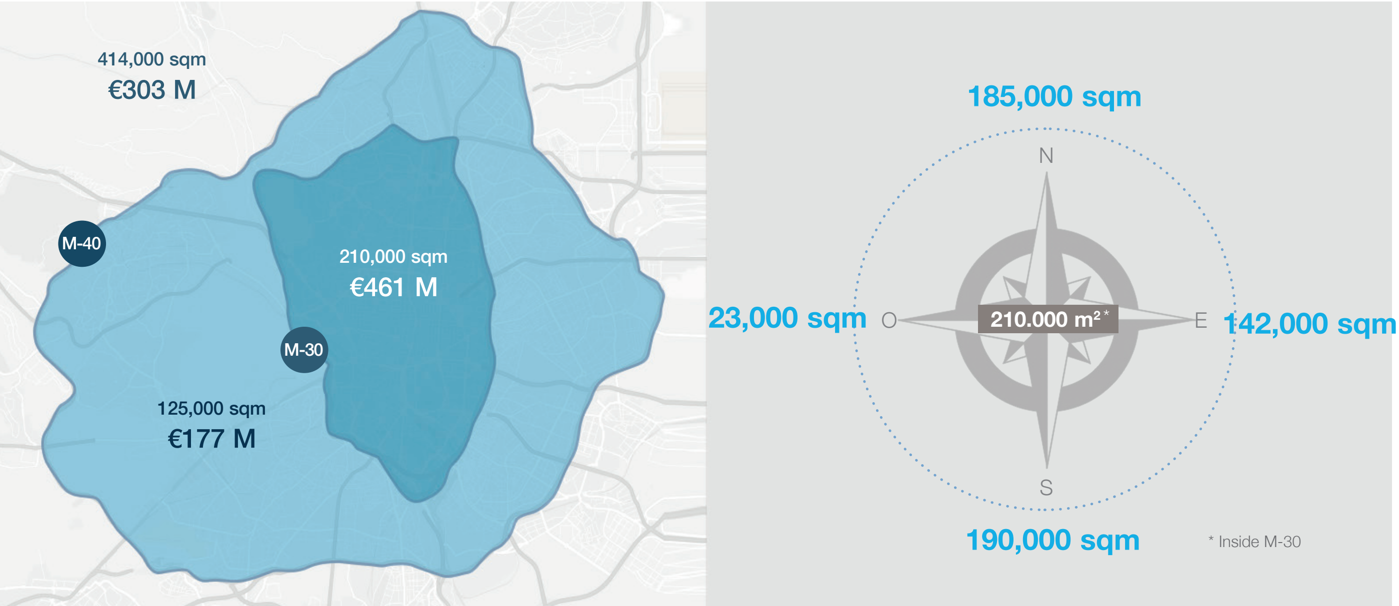
In terms of volume, 36% of transactions in 2015 were via private capital, 31% via developers and 20% via investment funds. Cooperatives and SOCIMIs account for the remaining 13%.

The average investment transaction ranges from €12 million to €15 million for investors and developers and over €25 million on average for cooperatives.

In the refurbishment sector in prime areas, the average size of deals varies between €6 million and €10 million.

In terms of geographical preferences, the North of Madrid remains the most sought after location by developers and investors, with some transactions reaching up to 185,000 sqm of buildable area. 190,000 sqm of space was transacted in the southern area, although we would note that 120,000 sqm of this relates to just one transaction (Parque Central de Ingenieros de Villaverde).

GRAPH 8
Geographical distribution of land investment



Source: Knight Frank

GRAPH 9
Top five land buyers (sqm acquired)

1	Neinor Homes
2	Amenábar
3	Pryconsa
4	Vía Célere
5	Castlelake

142,000 sqm of space was transacted in the eastern area, whilst investment in the western area barely reached 23,000 sqm.

With regard to the type of transaction, in terms of the amount invested and the number of deals, 63% of transactions were for development land and 37% for refurbishment projects.

As we highlighted at the beginning of this report, one of the main changes in the Madrid land market in 2015 has been the fact that transactions have moved out from more central areas towards areas located outside of the M-40. We have seen transactions take place outside of the M-40 for the first time post-crisis, in areas such as Alcobendas and San Sebastian de los Reyes.

Financing

The development land market is inherently linked to the availability of finance. As a result, the development land market has suffered the most as a result of a lack of funding combined with increased scrutiny from organisations such as the BdE and financial institutions.

However, we started to see funding being granted for residential development at the end of 2014, and to a greater extent over 2015. Nevertheless, the majority of developers/investors finance the construction and provide equity to purchase the land. However, some financial entities are looking at schemes in more detail, in terms of their financial viability and the company looking for finance, and as a result developers are able to achieve between 40 and 50% loan to value.

Spreads range between 2% and 2.5%. Although pre-let requirements vary depending on each scheme and purchaser, they are on average between 50% and 60%.

Outlook

The biggest challenge at the moment is the political uncertainty. If this persists, investors will undoubtedly adopt a 'wait and see' approach which will stall the market, both in terms of the number of deals taking place and planning permission being granted for new schemes.

International buyers do still have an appetite for residential development land; however, in order for deals to take place, political and economic stability is required.

With regard to prices, cooperative or self-promotion deals will push up prices per sqm once again to levels that are difficult to justify.

Prices will continue to rise within the inner M-30 area and the northern Urban Development Areas (PAUs), fuelled by strong pent-up demand and a lack of available land. However, we expect new development land to come onto the market, which will push prices per sqm down in the Urban Development Areas of Vallecas and El Canaveral.

2016 is going to be key when it comes to pre-app discussions and negotiations between the Local Authority and large-scale landowners, the outcome of which will undoubtedly affect the outlook for development land in the city of Madrid going forward.

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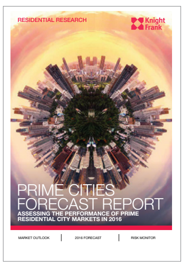

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