European Commercial – February 2021

SPOTLIGHT

Savills Research

European Logistics Outlook

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• Occupational • Investment • Outlook

Economy to recover losses in 2021

Economic overview

International lockdowns and curfews imposed across Europe as a result of the coronavirus continue to disrupt the economic recovery and boost European consumers' digital adoption and online spending.

The Eurozone economy contracted by 7.6% during 2020 and is expected to rebound by 4.6% in 2021, although not to recover fully until end 2022 (Chart 1). Part of the drag on economic growth has been Europe's export market, falling by 9.9% last year, although Focus Economics anticipates a 7.6% rebound in 2021.

Unemployment has remained relatively stable, rising from 7.4% to 8.4% over the course of 2020, although Eurozone government debt continues to rise as a result of furlough schemes, and now exceeds 100% of the economy.

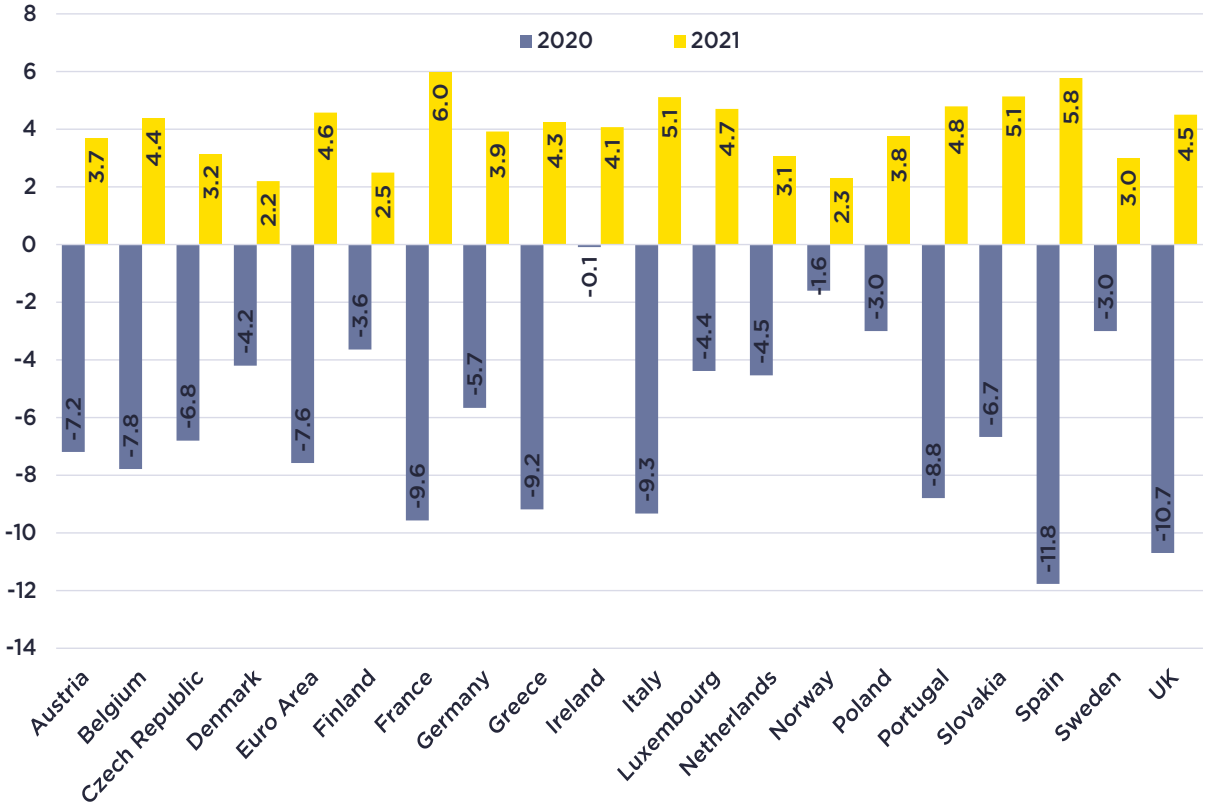
Eurozone inflation rose to 0.9% in January 2021 following five consecutive months of deflation. This was largely down to a rise in non-energy industrial goods inflation rising and energy prices decreasing at a slower rate. Inflation is expected to reach 2% by end 2021, before falling again in 2022.

Ecommerce

The UK's ecommerce penetration rate reached 27.9% during 2020, up from 19.2% in 2019. Although comparable data is not yet available for the European markets, latest forecasts from the Centre for Retail Research (CRR) indicates a rise in average European ecommerce penetration rates from 12.0% to 16.2% over the course of 2020, although we anticipate this level could be exceeded due to the extent of the lockdowns towards the end of the year.

The next big question is at what rate the ecommerce levels will normalise, which will be heavily dependent on the duration of national lockdowns. The CRR's most recent forecasts indicate that the average online retail sales penetration rate will drop to 15.3% in 2021, although into early February 2021, all but essential retail remains closed in Germany and the UK, whilst curfews imposed in Netherlands and France continue to redirect shoppers online.

Chart 1: European GDP growth rate by country, (%)



Source: Focus Economics, Oxford Economics

Record year of occupier demand

Occupational

European logistics take up reached 26 million sq m during 2020, marking a record year of demand - up 12% on the level observed during 2019 and 19% above the five year average (Chart 2).

Germany accounted for 6.8 million sq m of demand, up 3% on the five year average, and accounting for 26% of Europe's total take up. While e-commerce benefitted disproportionately, the situation remains more difficult in parts of the export economy and manufacturing sectors.

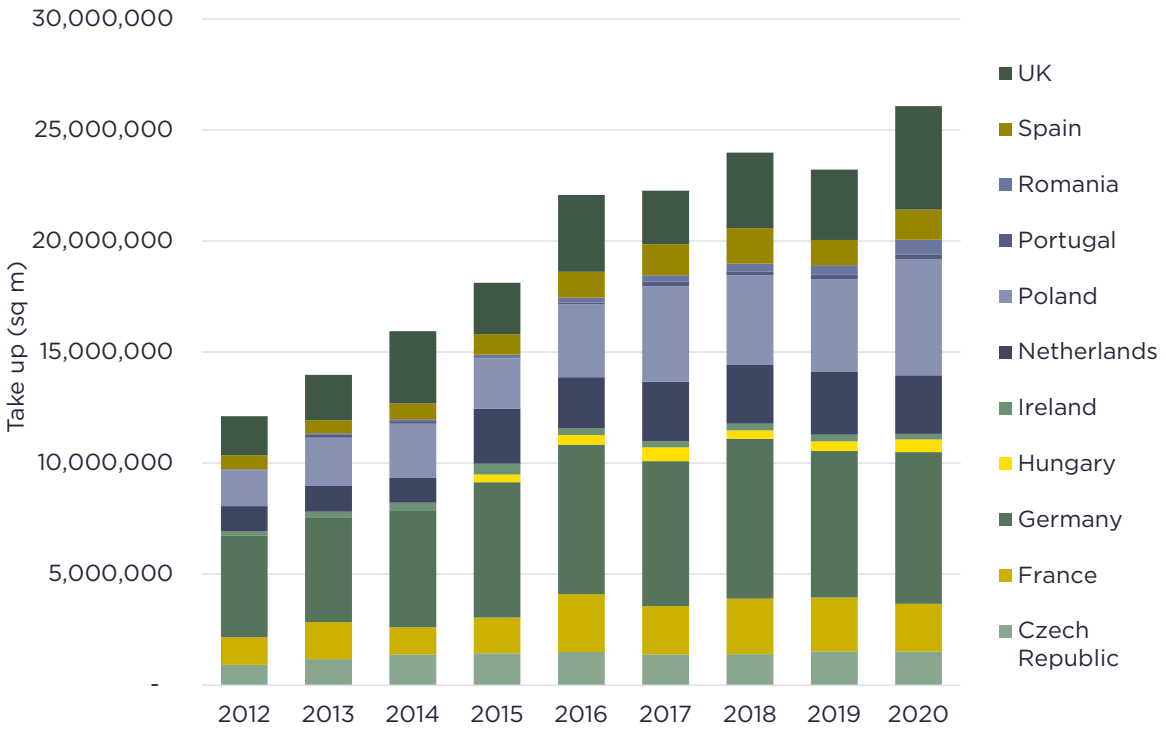
The Netherlands recorded 2.6 million sq m of take up, 0.3% up on the five year average. We are closely analysing the impact that newly-imposed Brexit tariffs are having on occupational demand in mainland Europe from British companies and we anticipate that we could see more inventory stored closer to where goods will be used/consumed as a result. We anticipate Dutch logistics take up will increase further in 2021.

Poland recorded yet another record year of logistics take up, totalling 5.2m sq m, 45% above the five year average. The UK (4.7 m sq m, +58%), Czech Republic (1.5m sq m, +4%), Spain (1.4m sq m, +9%), Romania (662,000 sq m, +135%), Hungary (+569,000 sq m, +29%) and Portugal (227,000 sq m, +58%) also all recorded increases on their respective five year averages.

France reached 2.2m sq m of take up, down 4% on the five year average whilst Ireland recorded 254,000 sq m, down 24% on the five year average, which was particularly affected by the severe lockdown restrictions adding delays to development completions. Throughout H1 2021, we may see new requirements arising across Ireland from retailers looking to avoid paying new tariffs in the UK.

We are also observing more demand from cross-border Chinese ecommerce operators who operate through their own distribution centres and sell through established ecommerce marketplaces to the European markets. China's One Belt One Road (OBOR) continues to expand across Europe, with rail freight now extending as far as Duisburg, where Europe's largest inland port terminal is set to be developed by end 2022 and we expect Chinese ecommerce giants to expand across European markets in the coming years.

Chart 2: European logistics take up



Source: Savills

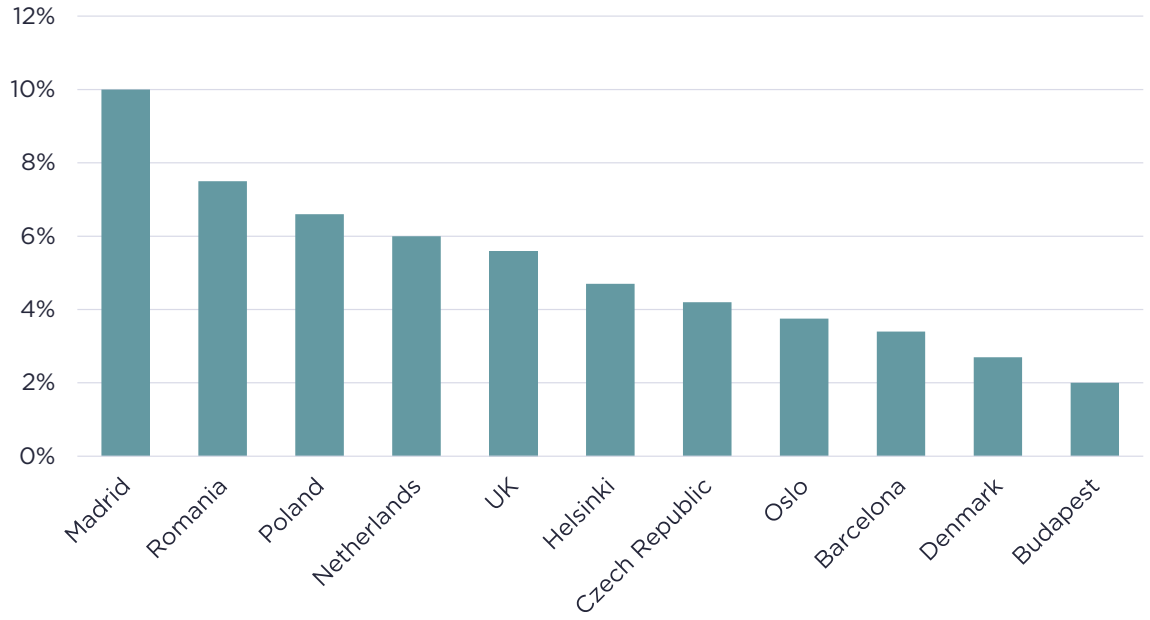
Vacancy remains low and stable

Vacancy rates remain at record lows across the European markets, hovering at 5.3% at end Q4 2020 (Chart 3). Whilst Madrid observed a significant level of new speculative development during 2020, the majority of markets observed declines in availability as a result of Covid-related new requirements. Romania (7.5%), Poland (6.6%), Netherlands (6.0%), UK (5.6%), Helsinki (4.7%), Czech Republic (4.2%), Oslo (3.8%), Barcelona (3.4%), Denmark (2.7%) and Budapest (2.0%) vacancy rates all remain below their respective long term averages. We have not yet observed any real impact of retailer liquidations increasing vacancy rates whilst urban facilities remain undersupplied across dense conurbations and it is here that we are observing some of the strongest rental growth.

Lockdowns are still hampering movement of raw materials and we anticipate further delays to development completions into H2 2021. A shortage of labour availability in the construction sector will further add to these delays.

Prime logistics rents rose by an average of 1% over the last 12 months, with Stockholm (+6%), Venlo (+5%) and London (+4%) observing the largest increases. We anticipate rental growth to resume again this year, with potential for secondary rental growth in core markets, driven by the undersupply of existing and future stock.

Chart 3: European logistics vacancy rate



Source: Savills

Prime yields compress further in Q4 2020

Investment

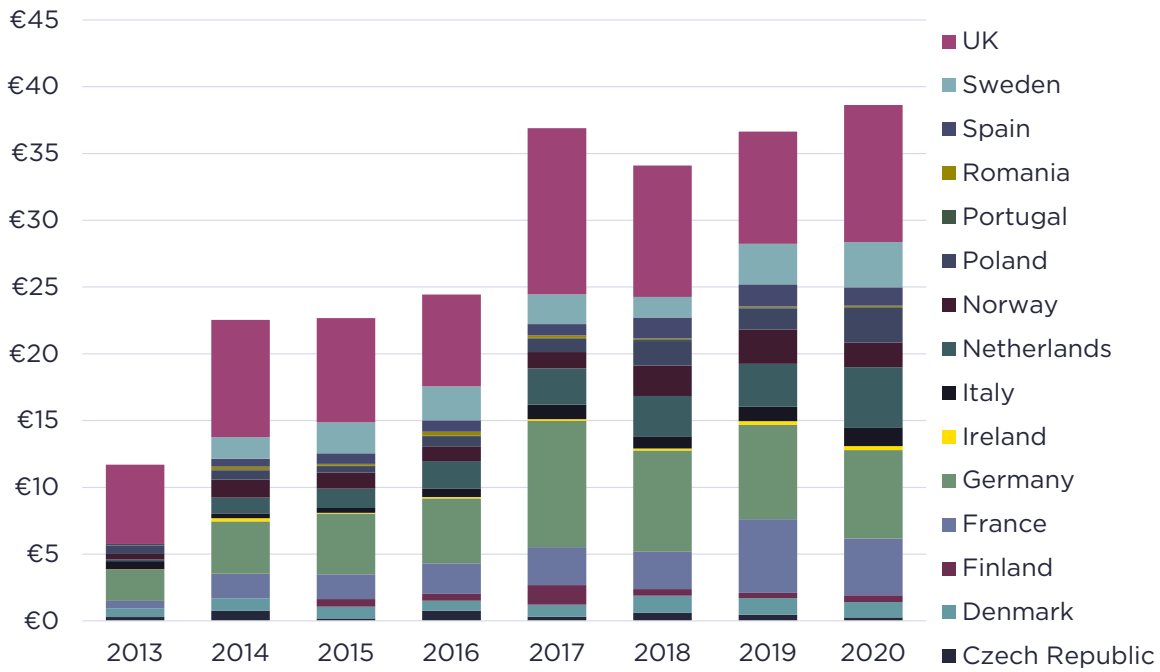
European logistics investment soared to €39bn during 2020, marking a record year of transaction volumes, up 5% yoy and 24% above the previous five year average (Chart 4). Despite demand continuing to outstrip supply, a large number of portfolio deals were transacted, achieving premiums of circa 10-15% in core markets.

The UK (€10.27bn, +13% vs 5yr average), Germany (€6.6bn, +16%) and France (€4.2bn, -23%) accounted for the majority of investment transactions as both domestic and cross border buyers opted for core markets. However, Poland (€2.6bn, +131%) and Sweden (€3.4bn, +45%) stood out as the markets which outperformed most significantly against the five year average.

The Netherlands (€4.5bn, +81%) can also be categorised in this group, with a flurry of Q4 2020 deals completing before the transfer tax rose at the turn of the year. Nevertheless, the impact of the tax increase has been relatively small, with new product being brought to market and more institutions are looking to launch last mile funds in search of rental growth. We are also noting more developers building to hold and offer more flexible lease terms to tenants to deal with short term uncertainty in exchange for higher rents.

Given the favourable fundamentals of the sector, institutional investors are looking outside core locations in

Chart 4: European logistics investment (€bn)



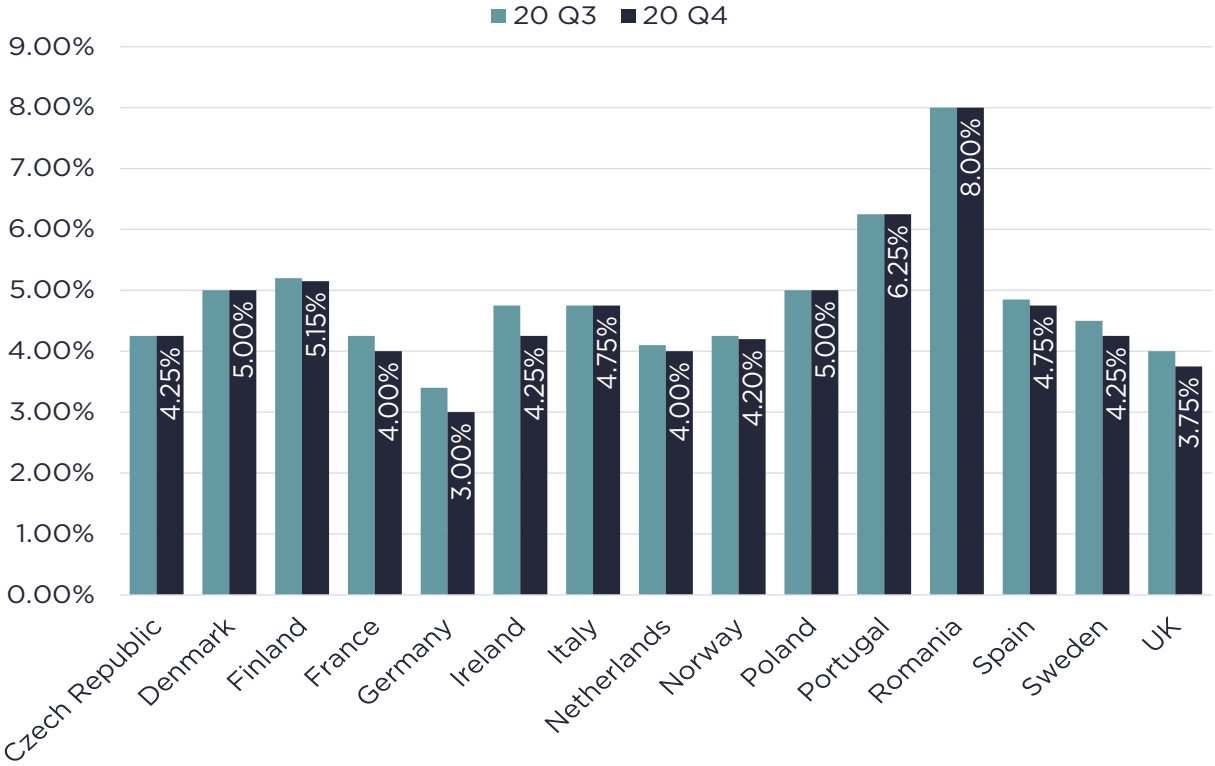
Source: Savills

search of more attractive yields across southern Europe.

Resilient demand for core product observed downwards pressure on prime yields in the final quarter of 2020, compressing by an average of 13 bps. Ireland (-50 bps to 4.25%), Germany (-40 bps to 3.00%) and France (-25 bps to 4.00%) compressed the most in the final quarter of 2020 (Chart 5). It should be noted that Berlin prime logistics yields have traded in the 3% region, although the rest of the German prime markets are trading in the 3.6 to 3.7% range. Given the allocation of real estate capital targeting the logistics sector, we anticipate further yield compression as buyers are increasingly willing to take on additional risk.

More landlords are now trying to boost their logistics exposure by developing speculatively. Development funding remains available across most core markets and more examples of UK funds are now open to speculative funding.

Chart 5: European logistics prime yields



Source: Savills

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