European Outlook 2020

European investment trends • 2020 Outlook • Rental growth and yield projections
Germany was the largest market last year with a total volume of €70.8bn, followed by the UK at €61.3bn and France at €40.1bn.

**European investment activity in 2019 increased by 1.3% yoy**

<table>
<thead>
<tr>
<th>Year</th>
<th>European Commercial Investment (€bn)</th>
<th>10Y German Bond Yield (%)</th>
</tr>
</thead>
<tbody>
<tr>
<td>2012</td>
<td>0</td>
<td>-0.5%</td>
</tr>
<tr>
<td>2013</td>
<td>0</td>
<td>0.0%</td>
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<tr>
<td>2014</td>
<td>0</td>
<td>0.5%</td>
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<tr>
<td>2015</td>
<td>0</td>
<td>1.0%</td>
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<tr>
<td>2016</td>
<td>0</td>
<td>1.5%</td>
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<tr>
<td>2017</td>
<td>0</td>
<td>2.0%</td>
</tr>
<tr>
<td>2018</td>
<td>0</td>
<td>1.5%</td>
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<tr>
<td>2019</td>
<td>0</td>
<td>1.0%</td>
</tr>
<tr>
<td>2020</td>
<td>0</td>
<td>0.5%</td>
</tr>
<tr>
<td>2021</td>
<td>0</td>
<td>0.0%</td>
</tr>
</tbody>
</table>

Source: Savills Research

**Different strategies for different risk profiles**

- However, late cycle signs and external threats to the economy, such as political uncertainty, trade tensions and the impact of coronavirus call for vigilance. Investment strategies vary: flight to safety, diversification of sectors or geographies, focus on countercyclical sectors or sectors that benefit from structural changes, moving up the risk curve.
- Investors remained loyal to offices last year, which accounted for 40% of the investment activity, up from 38% the year before. We expect another strong year of offices, as we believe that core strategies will prevail. Some new developments that will be delivered in the market will offer investable stock.
- Student housing investment registered the highest increase last year, by over 250% reflecting the shift towards alternative sectors, although in absolute terms the volume was just about €2.8bn.
- There is certainly a rising investor demand for residential sectors that should offer income stability even at a cyclical downturn, but...
The share of investment into the office sector in 2019. We expect another strong year for offices as new developments will come as investable product on to the market.

The average prime multifamily yield in the 10 markets that we monitor was at 3.2% at the end of last year.

We forecast an average annual yield compression of 12 bps for prime offices by the end of the year.

We forecast that prime office rents will grow fastest in Lisbon (11.4%), Munich (9.6%) and Luxembourg (6.4%).

40%

In 2020 we predict that prime office rents will grow fastest in Lisbon (11.4%), Munich (9.6%) and Luxembourg (6.4%).

We predict that the UK transaction volume will recover by 12% in 2020.

We observed the drop of retail investment (-13% yoy) and the rise of logistics investment (6% yoy). Five years ago, the total retail investment volume was at €67.3bn and the total industrial was at €23.3bn. Last year the gap narrowed with €40.9bn invested into retail and €36.6 into logistics and they are likely to converge even further in 2020.

The widening gap of buyer and seller expectations around pricing in the retail sector will be restricting deal making, however price corrections are expected to emerge, creating an opportunity for value-add investments. Several retail properties in good locations, with strong catchment areas have the potential to be redeveloped, repositioned or completely converted into other uses. We expect the UK market to lead the trend.

A number of investors have been looking in secondary cities for core plus and value-add opportunities. Last year the average share of investment into capital cities dropped to 36% from 54% the year before. The UK, France and Spain were amongst the larger markets where we noted a shift towards the regions, in the UK they captured 64% of the activity last year, in Spain 61% and in France 31%.

Transaction activity will be driven by “flight to quality”

• Investor intentions remain positive for European real estate, supported by strong fundamentals, cheap debt and comparatively attractive yields. With the accommodative monetary policy lasting for at least another year, record low yields remain acceptable to investors. In fact, the prime office yield spread with the 10 year sovereign bond yield has been widening over the past two years (by 37bps) on average, making property look even more attractively priced.

• Already the first month of the year saw record high investment volumes in the German market. With a transaction volume of almost €3.7bn, January 2020 was the strongest January for investment on record. The rolling twelve-month transaction volume stands at approx. €90.8bn, which is around 2% higher than December’s figure.

Some €2.7bn were invested in France in January 2020 against €1.8bn last year. Although it is too soon to say this sets the trend for the year. We expect a strong investment activity in 2020, fuelled by both domestic and cross border interest.

• It is still early to witness the impact of coronavirus on real estate, which is typically an asset

European investment 2018-2019 changes highest in peripheral markets

Source: Savills Research
type that reacts with a lag to shocks. Nevertheless we expect the immediate impact to be on the one hand a delay in some transactions, especially cross border ones, due to travel limitations and on the other hand a “flight to quality” towards prime markets and assets, due to the risks that the spread of the coronavirus may pose on businesses and the economy. The most vulnerable segments are tourism, leisure and retail ie hotels, restaurants/cafes, malls. However, for now we have not revised our projections on pricing, as we expect activity to bounce back in the second half of the year, if the outbreak is successfully contained by summer.

• In that case we could witness another strong year of investment turnover, driven by the recovery in UK volumes and strong investor demand for the core markets.

Another year of hardening yields ahead
• The average prime CBD office yield in our survey area was at 3.9% at the end of 2019, 27.2 bps compared to 12 months before. We forecast that despite concerns about the strength of economic growth outlook. According to Capital Economics positive
• The main question for the coming years is to identify the markets with positive rental growth prospects for investors.

Prime rental growth outlook is positive for investors
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