European Investment – December 2019

SPOTLIGHT
Savills Research

Alternatives Investment

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● Alternative investment trends ● 2020 Outlook ● Multifamily hotspots

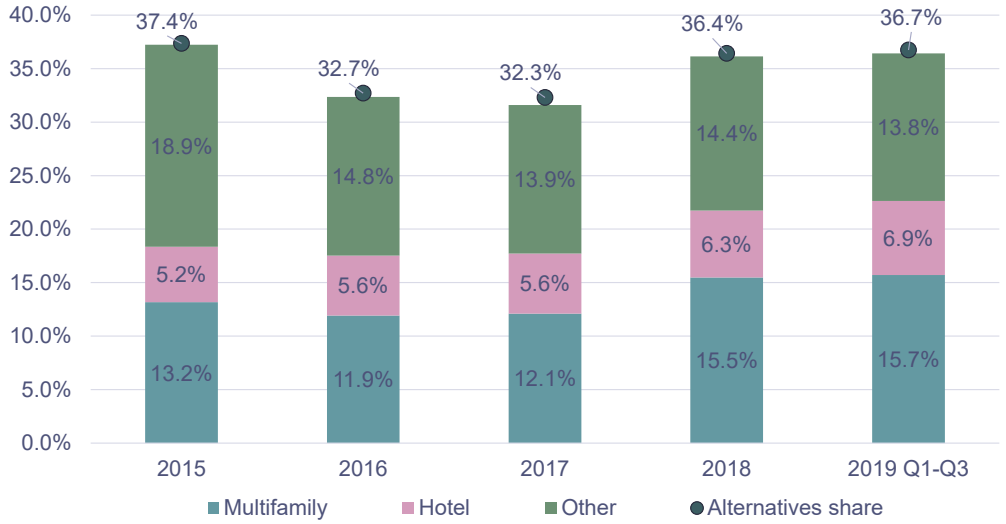
> "Rising allocations in real estate and the search for stable long-term income will continue to fuel demand for "alternatives""

"Alternatives" for better returns and long term stability

Investment into "alternative" property sectors is not something new. There have always been investors looking beyond the traditional commercial property sector trio of office/retail/industrial and buying other types of assets from hotels and residential to hospitals, petrol stations, pubs and prisons!

The discussion, the interest and the competition for the non-traditional property sectors has intensified the past five years along with the scarcity of prime product and the rising prices in the traditional trio. Investors have been looking for alternative opportunities to allocate capital, improve returns and secure long terms income streams. Investment into alternatives achieved its highest share in 2015 (39.4%), followed by 2018 (36.3%) and we project that it will stabilise at this level this year too.

"Alternatives" investment activity should stabilise at about one third of total



Source: Savills Research

European "alternatives"

Investors are increasingly spending outside the traditional commercial "trio" and some of the alternative segments have become large enough to be considered mainstream.

The "big" established alternative sectors

Hotels and multifamily have been the more established and sizeable segments, which have benefited from expanding tourist numbers and urbanisation. Arguably these sectors should not be considered as "alternatives" as they are well established for years and in some markets their share may exceed even the share of the traditional sectors, such as retail. Therefore in this report we will briefly review the trends in hotels and multifamily but mainly focus on the "small" alternatives sectors.

Investment in hotels has been rising by 6% pa on average since 2015 and its share has grown from 5.2% to 6.3% in 2018 and to 6.9% in Q1-Q3 2019 across the 13 countries we cover in this report. Investment in hotels has risen significantly in Czech Republic (100% 2015-2018), Poland (138%), and Spain (185%) since 2015, along with new hotels openings in the most visited destinations.

Multifamily investment has been growing overall by 2% pa over the same period. Residential sector has always been quite sizeable in a number of markets, especially the Nordics and more recently increased in other jurisdictions driven by corporate activity or public sector restructuring. In 2015 it captured 15.2% of the total investment activity, underpinned by high corporate activity in the German market, which accounted for half of all the countries. Since then transaction volumes in Germany have normalised but have grown elsewhere, such as the Netherlands (36% pa on average) where housing corporations had to sell large parts of their portfolios and France (590%) where the public sector has tested the waters by putting on the market and selling successfully to private investors social housing portfolios. Up to Q3 2019 multifamily accounted for 14% of the total activity, about €25bn and less than 60% of last year's total, due to lack of supply of stabilised assets on the market.

The "small" and growing alternative sectors

Investment into the "smaller" sectors of the alternatives has been quite dynamic. It has been growing by an average of 17% pa since 2015. In this category we include any other type of property investment such as student housing, senior housing, healthcare, leisure, mixed use and others, but we exclude land/development/redevelopment. These segments captured 10% of the total activity last year and 11% up to Q3 this year. This corresponds to €19.2bn of investment transactions, about 72% of last year's total, so anticipated to reach or even exceed last year's levels.

The top sectors since 2015 have been student housing (23%), healthcare (23%) and mixed use (30%), accounting altogether for

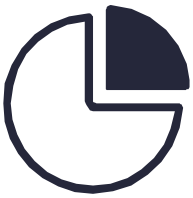
37% The share of investment in the non-traditional commercial sectors in Q1-Q3 2019

The top "small" sectors since 2015 have been student housing (23%), healthcare (23%) and mixed use (30%)

The "small" sectors with the highest rise in investment since 2015 have been Leisure, Sports and Wellness

Investment in hotels has been rising by 6% pa on average since 2015

Up to Q3 2019 multifamily accounted for 14% of the total activity, restricted by lack of product



The "small" alternative segments captured 10% of the total activity last year and 11% up to Q3 this year

over two thirds of total investment into alternatives. The UK continues to dominate the student housing investment market accounting for 84% of the transactions (2019 Q1-Q3), followed by Germany (9%) and Spain (4%). Interestingly the Dutch market has been quiet in 2019 with regards to student housing investment after four active years. Since 2015 about €28bn have been invested in student housing of which €21.6bn in the UK, €2.6bn in Germany, €1.4bn in the Netherlands, €1.3bn in Spain and €0.7bn in France.

The sectors which have seen the most significant increases in investment and stock supply have been Leisure/Sports/Wellness (140% pa on average 2015-2019) and Healthcare/Education/Community/Public buildings (41%).

The first group includes cinemas, theme parks, arenas, swimming pools, fitness centres etc and the most active markets have been Germany, Netherlands and the UK. However the total size of the sector remains small, with the total volume of just below €1bn in 2018 and only close to €0.2m up to Q3 2019.

The second group on the other hand includes hospitals, care homes nurseries/kindergartens and schools and the total turnover has evolved from €3.2bn in 2015 to €6.9bn in 2018 and €3.9bn up to Q3 2019. Several community assets have been sold in Germany, Netherlands and the UK, however the largest transactions were in the healthcare sector namely care homes in Germany, Netherlands and the UK and hospital/clinic portfolios in Spain, France and Italy. These are sectors that are compatible with ESG policies and could see further growth in the future..

Outlook: further expansion

Rising allocations in real estate and the search for stable long-term income in a zero interest rate environment will continue to fuel demand for alternatives. Record high prices in office and logistics sectors and uncertainty in the retail sector have forced investors to search for higher returns elsewhere and to diversify.

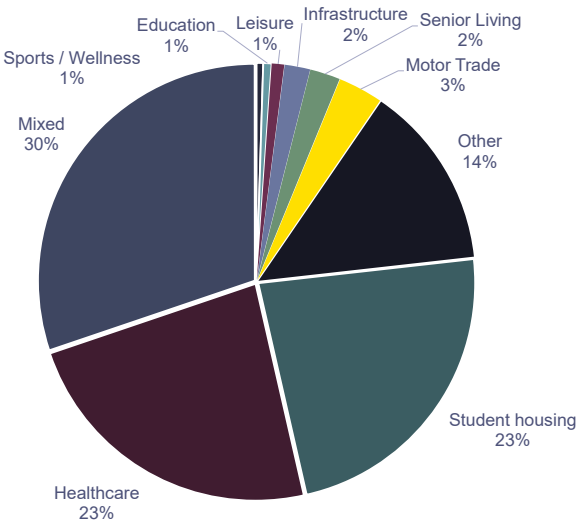
In a lower economic growth environment the somewhat defensive character of many of the alternatives will be seen as an advantage. The focus will remain for the best assets in class and competition will bring further yield compression in these segments in 2020.

We expect demand and investment in the hotels sector to remain robust in 2020, driven by cross border investors. The most attractive markets will be the ones that have posed restrictions to future developments, such as Amsterdam and Barcelona, higher yielding growth markets such as Prague, Lisbon, Oslo, Bucharest and Athens and established tourist destinations such as Italy.

Overall, we predict demand for other alternatives also to further increase. Healthcare, particularly care homes, will become more specialised and separated from mainstream residential and it will be considered a stable investment for the long-term, due to the ageing of the population. Germany, Norway, Sweden, Netherlands, Spain and Italy are seeing the expansion of specialist players in this segment as well rising institutional interest.

We expect to see more investment in student housing in the coming years, especially in less developed and undersupplied markets such as Italy, Portugal, Greece and further developments in Spain and Denmark. Other age restricted formats, such as senior housing, are also predicted to grow in most markets with the larger ones such as UK, France and Germany offering most potential, but new, often small scale, projects are emerging across most European markets..

The "small" alternatives Mixed, Student Housing and Healthcare top sectors



Source: Savills Research

> "The launches of new residential funds across Europe will create further competition for the available product in the multifamily segment, but also opprtunities for new developments"

Multifamily investment hotspots

Too big to be "alternative"?

Competition will intensify in the multifamily sector driven by the launches of new residential funds across Europe. The mismatch between the volumes of capital that will be targeting this segment and the available product, should lead to more forward funding deals and development initiatives. Rising construction costs and rental regulations can restrict returns but residential will still offer secure, long term, inflation hedged income streams. Given the urgent need for more housing in the big cities a balanced approach through the collaboration of public and private sector is required. The markets where we expect to see further activity are:

The Netherlands, especially Randstad due to rapid urbanisation and continuing critical housing shortage. Supply will marginally cover demand.

Czech Republic, because increasing residential prices and CNB (Czech National Bank) restrictions on mortgages create demand for flat/apartment rentals. This is coupled by the younger generation shift from ownership to rental living.

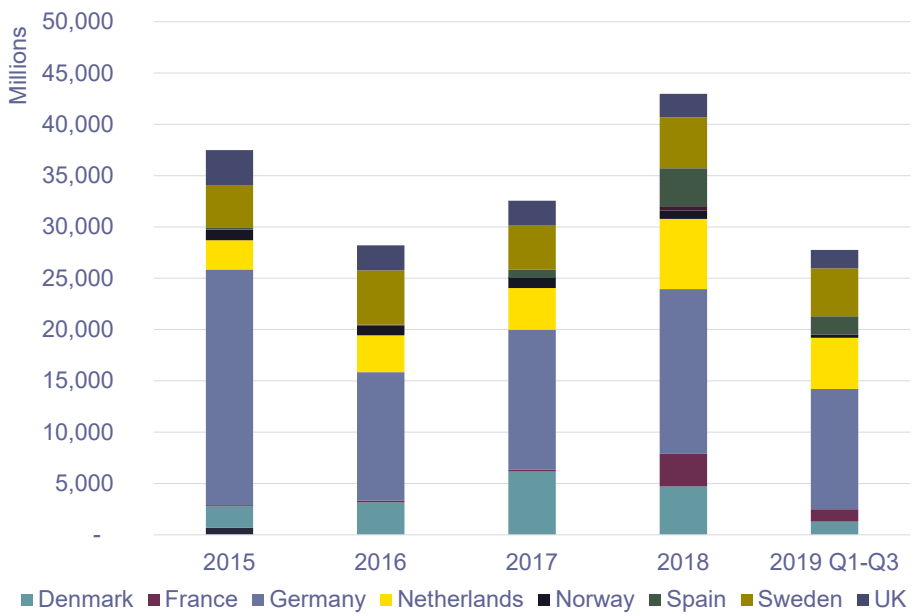
Housing affordability has become an issue in the major cities of Spain too. Traditional "build-to-sell" developers are entering the "build-to-rent" model, providing at the same time the platforms for institutional investors to enter the market through forward funding agreements.

In Germany we anticipate solid interest in the sector, as well as a shift to subsidised housing, in response to the need for affordable housing and as a way to meet ESG requirements.

In Sweden investment in multifamily is already at record levels and interest is expected to be sustained as it is perceived low-risk segment, especially in a weaker economy. Yields are still favourable compared to offices.

In the UK demand and supply imbalances are fuelling development activity. As institutions have become more confident in "Build to Rent" as a long-term asset the number of units being delivered at any one time has grown.

Multifamily investment by country (€): activity expanding in more markets across Europe



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