Germany Industrial - October 2022

MARKET IN MINUTES
Savills Research

Industrial property market Germany

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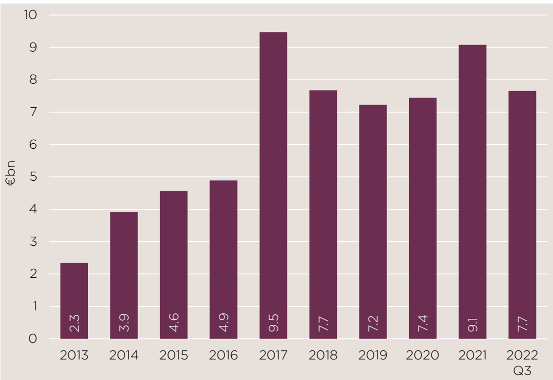
Long-term growth prospects remain intact

Despite increasing economic headwinds, the industrial space market remains characterised by scarcity and many investors want to continue to increase the logistics share in their portfolios. In the 3rd quarter of the current year, however, activity on the investment market remained subdued against the backdrop of the turbulence on the financial markets and, above all, due to the sharp rise in interest rates. The transaction volume in these three months amounted to €1.7bn. This corresponds to the value of the previous quarter and is only slightly below the quarterly average of the last five years (approx. €2.0bn), but is less than half as much as in the 1st quarter of this year. Rental markets continue to benefit from the tailwinds that have underpinned the sector over the past decade and which have been exacerbated by the pandemic. These drivers continue to operate, but at the same time the short-term outlook is deteriorating due to the impending recession. Together with the massively increased and recently further rising interest rates, this is such a challenging and also uncertain environment for investors that many of them are taking a wait-and-see approach for the time being. However, due to the still favourable rental growth prospects of the sector, they are likely to return as soon as the interest rate level has stabilised.

Price discovery remains difficult in a rising interest rate environment

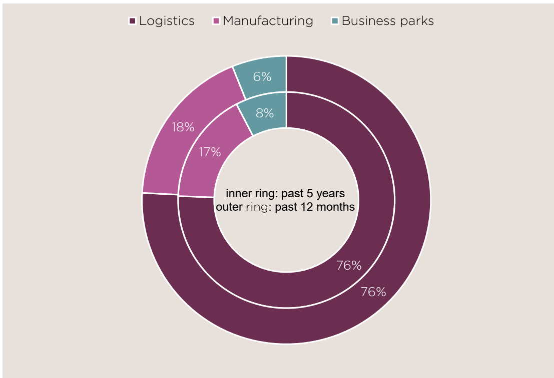
Due to the exceptionally high volatility of interest rates, price formation continues to be difficult and in recent months numerous sales processes were aborted because buyer and seller sides could not bridge their price expectation gap. However, the price correction that had already begun in spring has continued. The prime yield for logistics properties rose from 3.0 % to 3.2 % before to now 3.3 % to 3.7 %. We continue to show spreads to reflect the unusually large difference between buyers' willingness to pay and sellers' price expectations. If the current interest rate level consolidates or even rises further, the price

Graph 1: Transaction volume



Source Savills

Graph 2: Transaction volume by type of use



Source Savills

Focus on selected figures

19%
Almost one fifth of the total transaction volume achieved with commercial real estate this year was accounted for by industrial properties. If it remained at that level until the end of the year, it would be a new record.

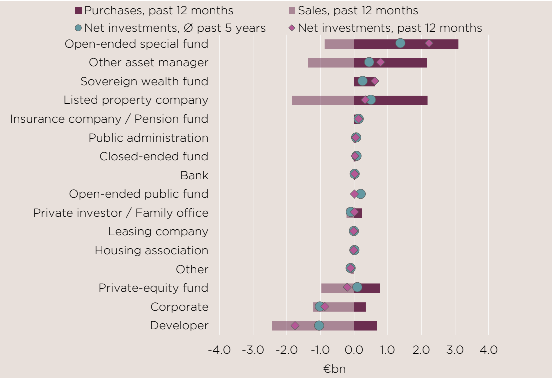
40%
More than 40 % of the users surveyed by us in the 'European Real Estate Logistics Census' assume that they will need more warehouse space in the next three years.

Table 1: Transaction volume at a glance

	Q1 - Q3 2022	y-o-y change	past 12 months	y-o-y change
Logistics	5,721	+18%	8,163	+18%
Industrial	1,423	+56%	1,950	+65%
Business parks	509	+159%	657	+66%
Total	7,653	+28%	10,770	+27%

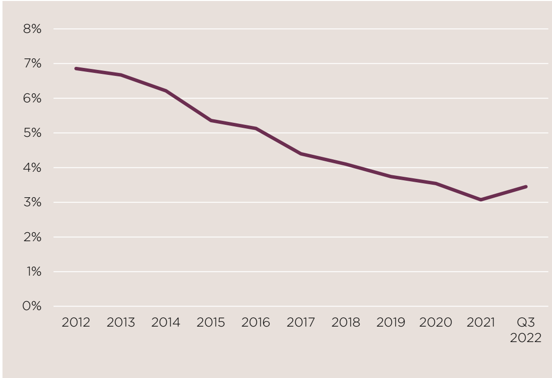
Source Savills / Transaction volume in million Euro

Graph 3: Transaction volume by type of investor



Source Savills

Graph 4: Net initial yields logistics properties



Source Savills / Note: The yield shown for Q3-2022 reflects the midpoint of the spread we have observed between offered and demanded prices. This is between 3.3% and 3.7%.

correction is likely to continue in the coming months. Only properties without any scratches will achieve top prices. Bidders use even small flaws in the quality of the property, location or the letting situation as a justification for comparatively high price reductions. This was not the case in the past and leads to correspondingly long and sometimes unsuccessful price negotiations between buyer and seller. Who is in the stronger position in the end remains to be seen.

Industrial real estate establishes itself as the second-largest asset class after offices

Although investment activity has cooled considerably, the industrial property market has been less affected than many other commercial property segments. Consequently, the share of industrial real estate in the total investment turnover generated with commercial real estate has increased. In the first three months of the current year, it was 19%. If this remains the case until the end of the year, it would be the highest value ever achieved. Moreover, industrial property would then be the type of use with the second-highest share after office property for the second year in a row. The short-term turbulence does not change the fact that industrial real estate in general and logistics real estate in particular have gained in importance in the portfolios of many investors and will probably continue to do so. Almost one third of the investors we surveyed in the summer in the 'European Real Estate Logistics Census' stated that they were still under-allocated in the logistics property segment.

Demand for space could fall in the short term

In the short term, however, other issues are likely to take centre stage. One of the main occupiers of logistics space, the retail sector, is in deep crisis and parts of manufacturing sector are also experiencing difficulties, not least because of high energy costs. This is likely to reduce demand for space in the coming months. However, this will be countered by demand-increasing effects, especially the conversion of supply chains from just-in-time to just-in-case models. In the short term, the negative effects may outweigh the positive ones in the medium to long term. For many companies, the easiest way to move towards more resilient supply chains is to increase their inventory levels. About 40% of all European logistics occupiers intend to do just that. The same number of users expect to need more warehouse space in the next three years, and only just over a tenth expect to get by with less space. This is likely to exacerbate the already existing shortage of space, especially since development sites suitable for logistics properties are likely to remain a bottleneck. Against this background, rents, which have already risen sharply recently, will continue to grow in the coming months and years.

Download the charts and raw data here

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