Italian Spotlight - 2022

SPOTLIGHT
Savills Research

Italian Investment Market

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Highlights

- In terms of investment volumes, 2022 represented a record year in the Italian CRE market despite the expected slowdown in the fourth quarter
- Offices came back as the investors' main target, followed by logistics
- Hospitality has proved to be resilient; ADR and Revpar are increasing
- If triggering factors will soften in 2023, the recession will be shorter and shallower in comparison to previous GFC
- The lack of grade A products and the healthy occupational market will sustain rent and investment volume in sectors characterised by demand constraints
- Investment activity is slowing as yields adjust in the actual challenging scenario
- Price adjustment in H1 2023 will be followed by a stabilisation in the second part of the year, which will bring a recovery in investment volumes
- Like interest rates, yields will remain higher compared to data registered in recent years of expansionary policy

"Record year, despite slowing activity in Q4."

Investment volumes

Total **11.8** bn €

▲ **+20%** YoY

256 deals



OFFICE

4.8 bn €

▲ **+134%** YoY

41% weight



LOGISTICS

2.9 bn €

▲ **+4%** YoY

24% weight



HOSPITALITY

1.6 bn €

▼ **-19%** YoY

13% weight



LIVING & HEALTHCARE

1.3 bn €

▲ **+41%** YoY

11% weight



RETAIL

0.9 bn €

▲ **-37%** YoY

7% weight



MIXED & OTHER

0.3 bn €

▼ **-50%** YoY

4% weight

Macro-economic Outlook

The global scenario is currently dominated by uncertainty: the war in Ukraine continues as well as USA and China tensions; China is also experiencing a further resurgence of the Covid pandemic due to the consequence of the zero-Covid policy; a faster-than-expected monetary tightening may delay the exit from an impending recession. If triggering factors will soften in 2023, the recession will be shorter and shallower in comparison to previous GFC. Italy economic trend remains positive although gradually slowing down. Growth in services continued mainly thanks to retail trade, transport and tourism; although the employment trend continues to remain in positive territory, real incomes decreased (-1% YoY).

In December, Italian inflation slowed down slightly (+11.6%). Average 2022 figure marks the largest increase since 1985 mainly due to the trend of energy goods price (+50.9% 2022 yearly average). Net of energy, 2022 CPI was +4.1%. The core component accelerated to 3.8% while the so-called 'shopping trolley' to 8.4%.

Propensity to save rapidly compressed below pre-Covid levels (7.1% Q3 2022), close to values recorded only in 2012. Some of the savings accumulated during the pandemic already seem to have flowed into household consumption, and a large part of that has been accumulated by high-income households. On the other hand, the uncertainty originated from the deteriorating economic outlook may induce households to make further 'precautionary' savings in the next months. Moreover, persistently high energy prices could absorb further savings, reducing the positive impulse on consumption and accelerating stagnation.

PNRR remains fundamental for the economic growth and market confidence. As of December 2022, the planned 55 targets were achieved. The disbursement of the third tranche of € 19 bln is expected in the next months, following the EC evaluation process.

In December, the Bank of England increased its base rate to 3% while the FED raised the benchmark rate by 50 bps to 4.25-4.50%. With the headline and core inflation well above expectations, the ECB is expected to raise the interest rates by 100bps in 2023, in order to bring inflation timely back to 2%. At its last meeting, the ECB appeared more hawkish that expected. Keeping interest rates at restrictive levels is seen as the way to reduce inflation by dampening demand and will also help prevent the risk of a persistent upward shift in inflation expectations. Demand dampening will have an obvious recessionary effect.

The inevitable rise in interest rates is impacting government bond yields, making government debt and commercial loans more expensive. In addition, borrowing money has become more difficult.

In December, the consumer confidence index improved significantly, while business sentiment also increased, although still at a level below the annual average. The increase in the index is mainly driven by both the service and construction sectors. In winter, fears of a recession are increasing, and this, together with expectations of high inflation for a longer period, is weighing heavily on industrial production (October -1.6% y/y) and manufacturing. Consumers reported an improvement of the general situation and of unemployment expectations.

According to Consensus Economics, after a growth of 6.7% in 2021, Italian GDP registered a provisional increase of 3.6% in 2022, thanks to EU funds, the recovery of the tourism industry and accumulated savings. In 2023, growth will sharply stop on tighter financing conditions, higher interest rates and a slowdown in consumption and export.

CPI
+11.6% YoY
(December 2022, provisional)

GOVERNMENT BOND YIELDS 10 YEARS
4.24% (**+323** bps YoY)
(November 2022)

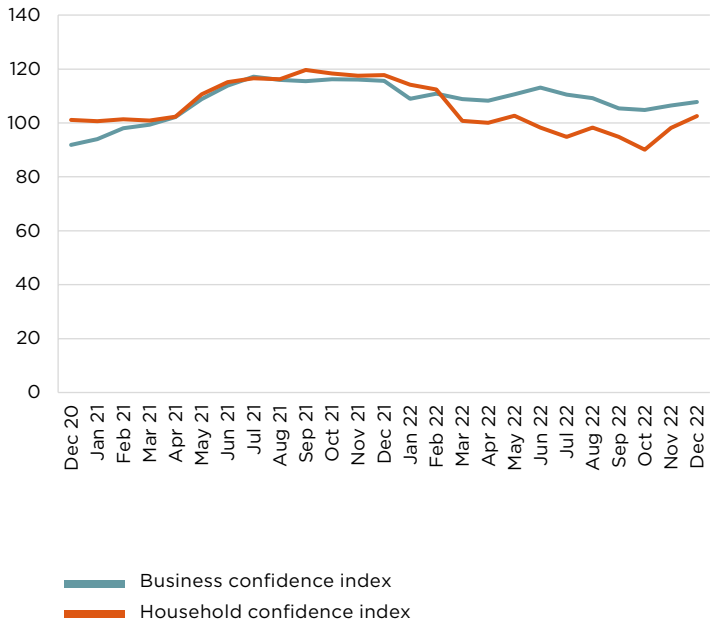
CONSTRUCTION COSTS' INDEX
+8.2% YoY
(November 2022)

INTEREST RATE – LOANS FOR HOUSE PURCHASE
2.75% (**+131** bps YoY)
(October 2022)

Macro-economics KPIs

Italy (% YoY)	2013-19 average	2020	2021	2022 (F)	2023 (F)
GDP	0.50	-9.10	6.70	3.60	0.00
Consumer spending	0.50	-10.40	5.10	3.90	0.50
Unemployment	11.50	9.40	9.50	8.20	8.40
CPI inflation	0.70	-0.10	2.00	8.50	6.80
ECB Refinancing rate	0.05	0.00	0.00	2.50	3.05
Government bond yields 10 years	2.21	0.55	1.17	4.35	4.16

Confidence index



Source: Consensus Economics, Oxford Economics, ISTAT, Banca d'Italia

Commercial Real Estate Investment Market

In 2022, around € 11.8 bln was invested in the Italian commercial real estate market, registering a 20% increase compared to the previous year. 2022 represented the second better result in the last 10 years, despite a slowdown in the fourth quarter. 2022 investments' volume surpassed the last 5 years' average by 18%.

Mega deals' (> €100 mln) weight increased (49% of total investments) compared to 2021 including the sale of a €842 million portfolio from Enpam to Apollo. Portfolio deals decreased, reaching 33% of the volumes transacted in the period.

Foreign capital continued to be predominant, accounting for the 76% of the total volumes; Global and European capitals represented the biggest share.

In terms of geographies, Milan confirmed to be the preferred destination, registering 46% of the investment volume, followed by Rome (12%) which is gaining market share compared to 2021. Thanks to the positive trend of logistics and hospitality sectors, the other Italian cities accounted for 42%; among these, Verona (logistics), Siena (hospitality) and Bologna (logistics and office) stood out.

With € 4.8 bn, offices returned to be the main sector in terms of investment volumes, followed by logistics. Rome and mainly Milan remained central, as well as grade A assets.

Logistics confirmed its relevance in the Italian panorama, representing around 24% of total investments. International investors confirmed to be the most active actors in the segment.

Following the great rebound of 2021, hospitality continued to register a significant volume of investments, thanks to the positive trend in ADR and RevPar. Key leisure destinations, like Rome, Siena and Venezia, have seen a rebound in investment volumes. Although improving on a year-on year basis, the number of tourists in the first ten months of the year remained below YTD October 2019.

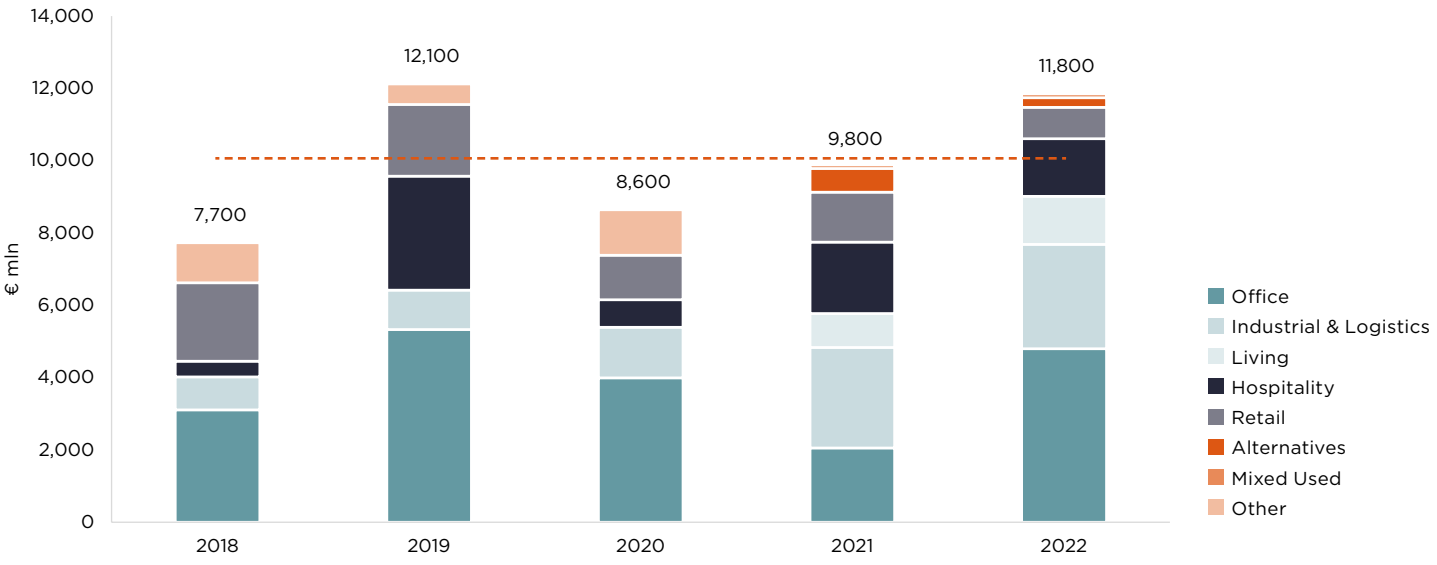
The resilient characteristics of the living & healthcare sectors sustained volumes. The 2022 level was mainly driven by the residential segment; among the 40 deals of the period, several transactions involved lands and developments, while investors remained focused on Milan. As regards as healthcare, care homes and clinics drove volumes.

Since the beginning of the year, rental levels remained stable for high streets while the shopping centre rents started to incorporate the inflation trend; offices and logistics registered an increase sustained by high demand for grade A assets and low vacancy rate. Although the high competition for prime assets resulted in a further yield compression in office and logistics in Q1, raising interest rates caused a decompression in the second part of the year.

Investment activity is slowing as yields adjust in the actual challenging scenario. Price adjustment in H1 2023 will be followed by a stabilisation in the second part of the year, which will bring a recovery in investment volumes. The stabilisation of interest rates and costs and the easing of inflation during 2023 will lead to a more favourable market in 2024. Today and in the next 6 months, price correction will reflect the impact of higher bond yields and borrowing costs. Like interest rates, yields will remain higher compared to data registered in recent years of expansionary policy. In sectors characterised by demand constraints, rental growth is expected to offset yield decompression.

> 2022 exceeded expectations despite the slowdown in the fourth quarter of the year. The last few months have confirmed a general wait-and-see approach. In 2023, the market will be more selective focused on sustainability.

Investment volume by sector



Office

In 2022, the office sector came back to take the lion's share, reaching around € 4.8 bln, a figure up both on 2021 (+129%) and on the last five years average (+24%). Q4 volumes remained positive and amounted to € 850 mln (+30% YoY).

2022 was characterized by the presence of several deals of large volume: thirteen operations above € 100 mln were recorded, 3 of which in the last quarter. Mega deals counted for 47% of annual volumes.

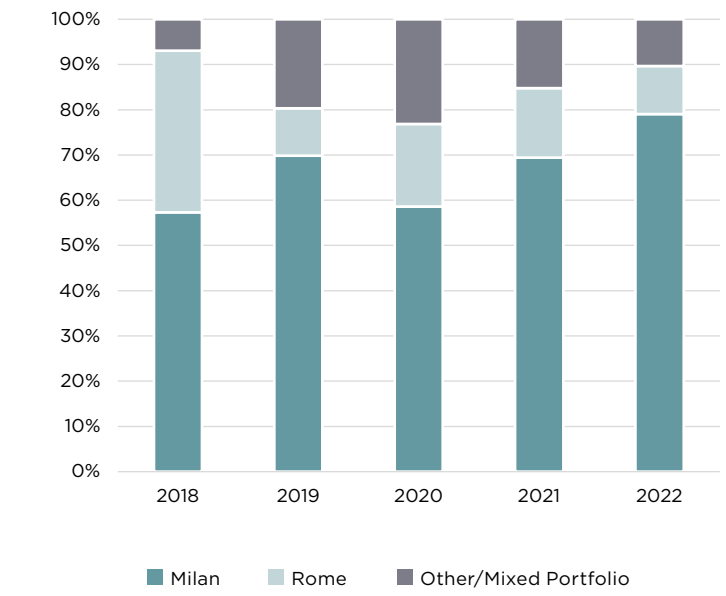
Milan continued to be the investors' first target: 79% of the total volumes were transacted in the city across the acquisitions of 74 assets. Deals were mainly related to assets located in the CBD as well as in the peripherical areas of the city and presenting core or value add profile. The city of Rome reached instead € 510 mln across the closing of 8 deals.

International investors remained prevalent, representing 62% of annual volumes and 7 mega deals. On the other side, domestic investors were involved in 40 operations, 6 of which of large volume.

In terms of typology, 5 transactions were related to flexible spaces, one of which is located in Rome.

Leasing activity registered record take-up volume in Milan and a positive trend in Rome. Leasing activity has been sustained by demand for flexibility and the need for a workplace that enables health and wellbeing. Prime rents grew from the beginning of the year both in Milan (675 €/sqm/year) and Rome (500 €/sqm/year), but remained stable compared to the previous quarter.

Investment volumes by geographies



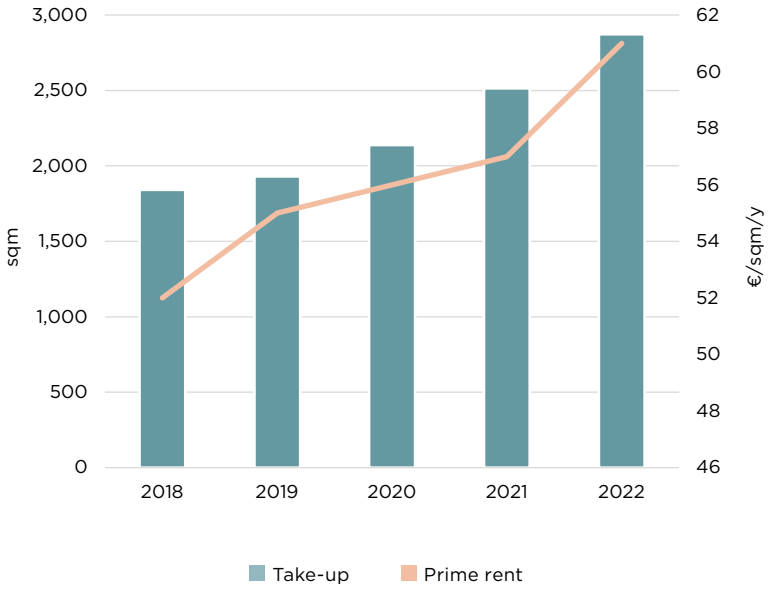
Logistics

The logistics sector has become a top priority over the last years, in fact a new record high has been reached in 2022, with volumes closing at € 2.9 bln. The sector was the second most sought-after following office sector in the Italian landscape, attracting 24% of volumes and representing a well-established asset class in investors' strategies. Moreover, the sector was the most dynamic, recording 68 operations, 13 of which are portfolios.

Looking at geographical areas, the north of the country continues to be the first destination: here more than 75% of volumes were transacted. From the beginning of the year, Verona and Milan represented the top destinations, where more than half of volumes (without considering assets in mixed portfolios) have been transacted across the acquisition of 35 assets. In line with the historical trend, the market continues to be dominated by foreign capitals, which represented 97% of total yearly volumes.

After reaching the lowest level in the first part of 2022, prime net yields started to decompress in the second semester, following rising financing costs. In the last quarter of 2022, prime net yields in Milan reached 4.75% (+75 bps on Q4 2021), coming back at 2020 levels. Another upsurge could occur in the next months. Great attention to capital value has to be paid during underwriting processes.

Take-up (LHS) and prime rent evolution (RHS)



Hospitality

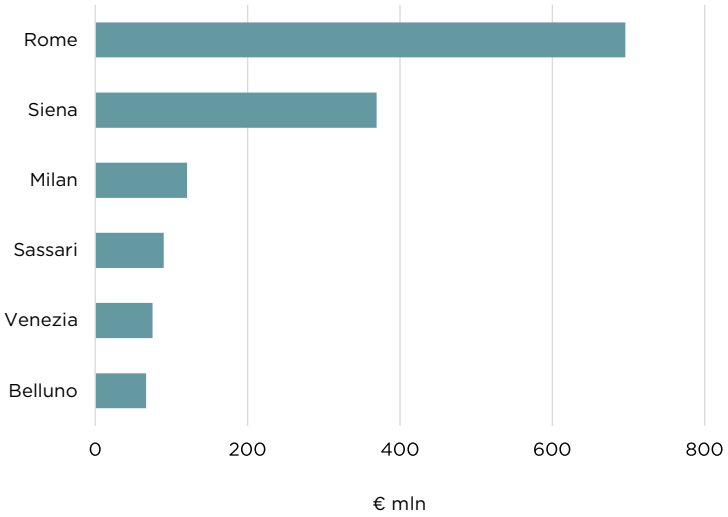
Since spring, the easing of Covid restrictions in Italy has translated into a rebound for the hospitality sector and provisional figures for 2022 are positive. In the first 10 months of 2022, the number of tourists grew by 41% compared to the same period of the previous year, but are still below 2019 data (-17%). International travellers' spending were slightly (-6%) below pre-pandemic level in YTD October 2022. ADR and RevPar are increasing.

The investment volumes transacted in 2022 amounted to around € 1.6 bln, a figure 19% lower on the same period of the previous year but in line with the last 5 year average (+3%). Investments in the fourth quarter amounted to € 560 mln.

The assets acquired included estates, resorts and 5 stars category hotels as well as hotels to be totally renovated. A total of 29 hotels were acquired, mainly located in Rome and Milan. The Capital affected most of the volumes (44%) across eleven operations, part of which involved conversions of use.

International capitals drove the demand, affecting 84% of the total and coming mainly from Qatar, USA and Canada.

2022 Top 6 province by investment volume



Retail

Retail investment volumes continued to be limited: around € 300 mln were recorded in the fourth quarter of 2022 totalling € 900 mln from the beginning of the year. Investments are still below both the last 5 year average (-42%) and 2021 data (-36%). In terms of number of deals, the sector was more dynamic than in 2021 with a total of 25 deals, 5 more compared to the previous year.

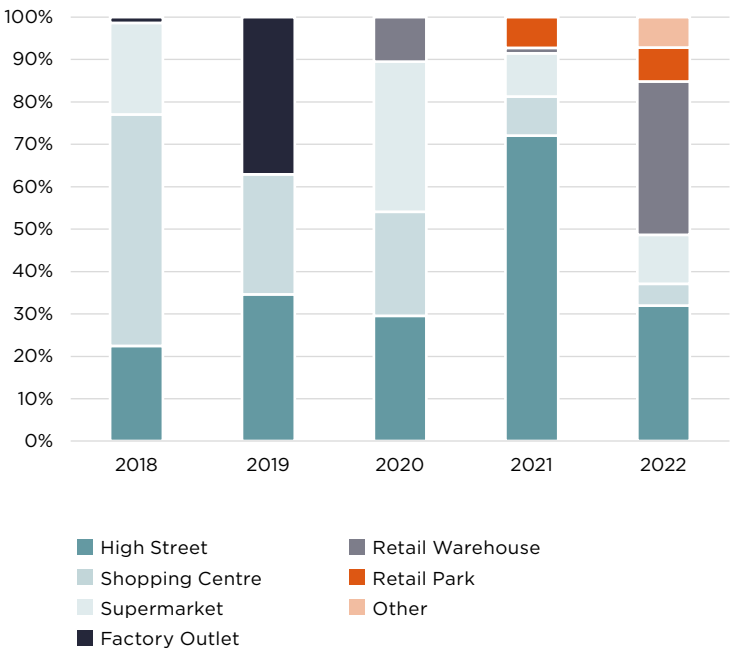
As for the general trend, this sector was characterized by a predominance of international buyers, but at a lower extent (68%).

High street attracted 32% of the investments across the closing of 11 deals. The city of Milan was the most sought after location (28%) mainly thanks to the sale of Eataly store acquired by COIMA; a great attention was nevertheless paid to Rome, Bologna and to the South of the Country. On the other side, the out of town segment recorded 14 deals for € 590 mln. Among the subsectors, retail warehouses and grocery stood out, characterizing together more than 70% of the total out of town activity.

Prime net yields started to decompress in the second semester both for high street (+25 bps), shopping centres (+35 bps) and retail parks (+50 bps), due to the shortage of liquidity in the sector and the imbalance in price between supply and demand.

Regarding prime rents, high streets continued to show stability in Milan and Rome, while prime shopping centres showed an increase due to inflation upsurge and the high demand in prime centres. More incentives are anticipated to be granted as raising costs are impacting expansion strategies.

Investment volume by segment



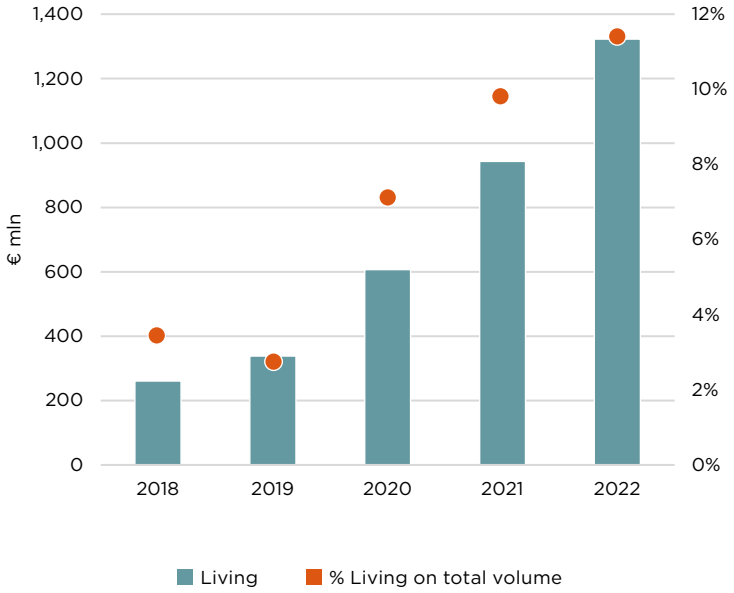
Living & Healthcare

In 2022 the sector hit a new record high with around € 1.3 bn of volumes. This result has been achieved especially thanks to the residential segment which counted for 62% of the yearly volumes. The living sector is now becoming well-established: it has grown consistently in recent years and is now one of the first sectors that investors are targeting.

The demographic fundamentals are sustaining the demand in urban cities where new development schemes are expected to be developed despite the costs increase. Many investors are looking to increase allocation to counter-cyclical assets, such as BTR and PBSA. In 2022 we recorded the highest amount of build to rent project transacted (9): the preferred location remains the city of Milan, but also other cities such as Rome and Firenze stood out. This product will remain at the top of investors' agenda and in the next months we will assist to the first transactions related to properties nearing completion and to already up-and-running ones.

In 2022 the healthcare segment recorded a great volume of transactions with around € 390 mln across 12 deals. The assets mainly refer to care home structures located in the North, Centre and South of the Country. Capitals allocated to this subsector are international, coming mainly from France. This segment is sustained by ageing populations and a low level of beds per inhabitant. The consolidation of owners and operators will continue, alongside with redevelopment opportunities.

Living investment volumes (LHS) and % on total volumes (RHS)



> A lower supply than the demand and tenants willing to pay higher rents will sustain rental growth for PRS sector.

Milan, new development projects



Student housing continues to attract interest: it performed well during the year, reaching more than € 100 mln of volume across 5 transactions in Milan, Padova, Torino and Bologna. The increasing number of mobile students wishing to live away from home will sustain the market and contribute to push rental growth further.

The number of development projects in Milan related to student housing and build to rent typologies testifies the high appealing for this kind of products.

Typology
- Build to rent
- Student housing

N° of Dwellings (Build to Rent)
N° of Beds (Student housing)
- > 1200
- 900
- 600
- 300
- < 14



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