EMEA REAL ESTATE

MARKET OUTLOOK 2020

MIDYEAR REVIEW

CBRE RESEARCH | EMEA

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INTRODUCTION

Considering the extent of COVID-19's impact on the global economy, let alone the European property market, it was imperative that we update our Market Outlook report which launched at the end of 2019.

The previous cycle, marked by record investment and development, has ended abruptly due to this black swan event. The occupier side in particular has been severely impacted by a decline in economic activity. Nonetheless, the continued low-interest rate environment coupled with ample unallocated capital means the market is well-positioned for a bounce-back.

The commercial real estate industry now faces unprecedented questions. For example, with occupier market performance slowing, will this mean lower returns and investors subsequently turning to sectors better placed to withstand short-to medium term pressures?

What COVID-19 has highlighted is that change is coming quickly. We are here to guide you through these times of uncertainty and point you towards opportunities that these changes will bring. Enjoy your summer.

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Head of Research, Continental Europe;
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ECONOMICS

ECONOMIC OUTLOOK
SEVERE DIP BUT REBOUND IN SIGHT

The pandemic impacted the euro area harder than was expected earlier in the year when the virus first made the global headlines. The euro area suffered a collapse in business activity in Q1 2020, largely because of measures taken in China to contain the spread of the virus. The pandemic and local measures taken to contain the spread mainly impacted European economies in Q2 2020, with the hit to GDP likely to be the deepest decline in its history.

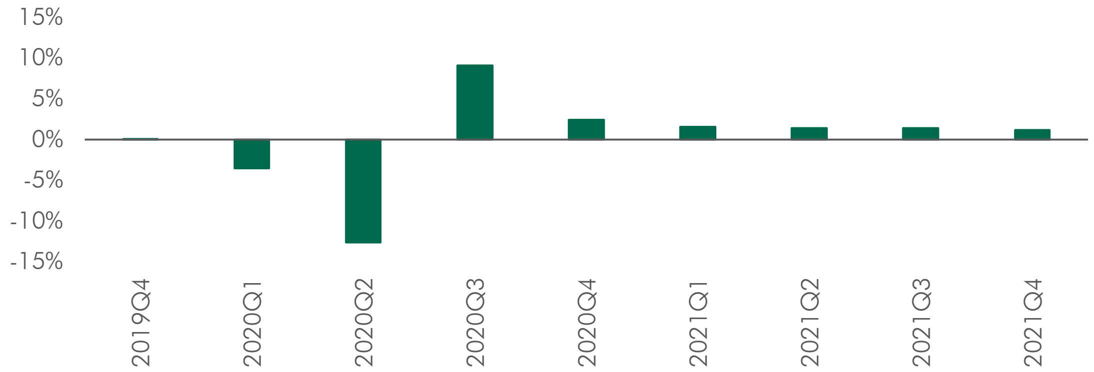
Forward-looking indicators, however, point to a recovery late in Q2 2020 and support CBRE's base case of a lopsided V or check-mark recovery in the euro area. The Purchasing Managers Index (PMI) – although difficult to interpret – rose strongly in May and June, suggesting that business activity reached a trough in April and is now returning to more normal levels. Retail sales volumes in May also support this view, with the European Union as a whole seeing an increase in sales volumes in May (excluding motor vehicles and fuels) of over 15%. The bounce-back was particularly strong in those countries, such as Germany, that moved swiftly to contain the spread of the virus and were able to remove lockdown restrictions earlier.

As economies have relaxed restrictions, Google mobility data in the euro area has rapidly improved. In June, on average, euro area mobility was only 10% below normal or pre-crisis levels, a sharp rise on the 50% in late March.

As such, we do expect a bounce-back in economic activity in H2 2020. However, the hit to activity was so strong in H1 2020 that a partial rebound will be insufficient to prevent a fall in annual growth. The CBRE House View is that euro area GDP will contract by 8.3% in 2020, before rebounding strongly by 6.4% in 2021. On this basis, it will take some time for euro area GDP to recover to the levels seen in Q4 2019.

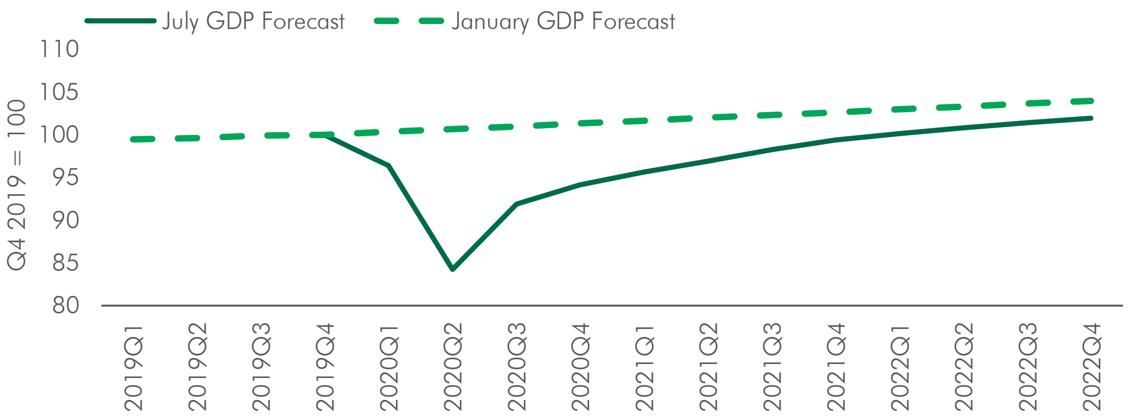
There is a higher degree of uncertainty than usual in our forecasts and several sources of downside risk. Firstly, any sustained increase in infections, and the possible need for further lockdowns, would hinder the recovery. Secondly, the labour market may fare worse than assumed as short-time working schemes are unwound. Thirdly, we are assuming that we avoid any severe second and third round income and spending effects, the result of corporate defaults, bankruptcies and mass layoffs. Finally, we highlight the efforts of the ECB, which so far look to be sufficient to maintain stability in the financial markets.

FIGURE 1: EURO AREA REAL GDP FORECAST (Q-O-Q)



Source: Oxford Economics and CBRE Research, 2020

FIGURE 2: EURO AREA REAL GDP (2019 = 100)



Source: Oxford Economics and CBRE Research, 2020

UNEMPLOYMENT AND INFLATION: SHORT-TERM TURBULENCE THEN STABILISATION

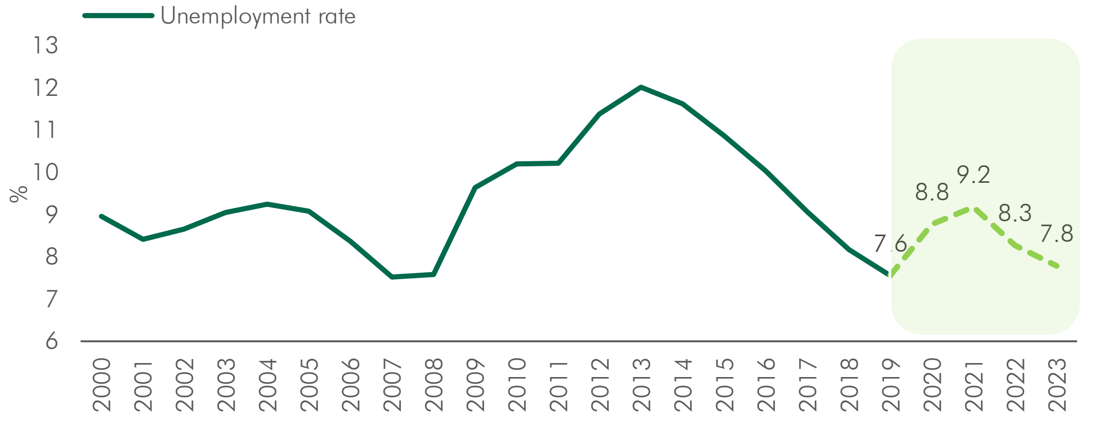
The pandemic has significantly disrupted European labour markets. In H1 2020, euro area labour markets deteriorated, which translated into a large decline in the number of hours worked. In comparison to the decline in economic output, the rise in unemployment in the euro area has been relatively muted to date. This is in stark contrast to the U.S., where layoffs occurred immediately and in large numbers. Differences in national statistics account for some, but not all, of these differences.

Government policy measures such as short-time working schemes, wage subsidies, and liquidity to firms have played an important role in avoiding large job losses in the euro area. Assuming that these policy measures are effective and can be unwound smoothly, we expect the rise in unemployment this year to be far more moderate than the decline in output. Unemployment in 2021 is expected to be 1.6 percentage points above that recorded in late 2019.

Inflation in the euro area remains subdued and annual rates have now fallen below 0.5%, driven by the fall in energy prices. A weakening labour market, lower demand, falling energy prices and temporary cuts to VAT mean that the inflation outlook will remain very low in 2020.

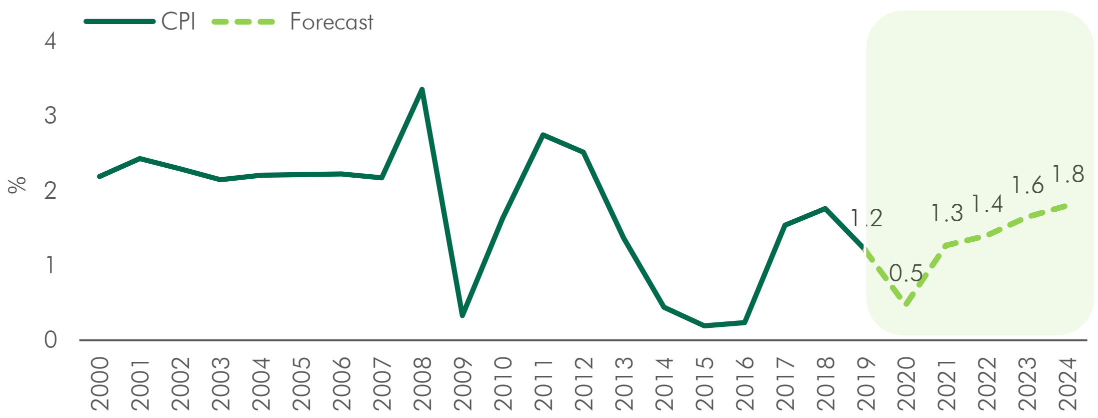
As we move into 2021, the reversal of temporary tax cuts and higher oil prices against a backdrop of stronger demand will mean that inflation will increase in 2021. Overall, euro area headline CPI inflation is expected to average 0.5% in 2020, increasing to 1.3% in 2021.

FIGURE 3: EURO AREA UNEMPLOYMENT RATE, %



Source: Oxford Economics and CBRE Research, 2020

FIGURE 4: EURO AREA CPI INFLATION (Y-O-Y), %



Source: Oxford Economics and CBRE Research, 2020

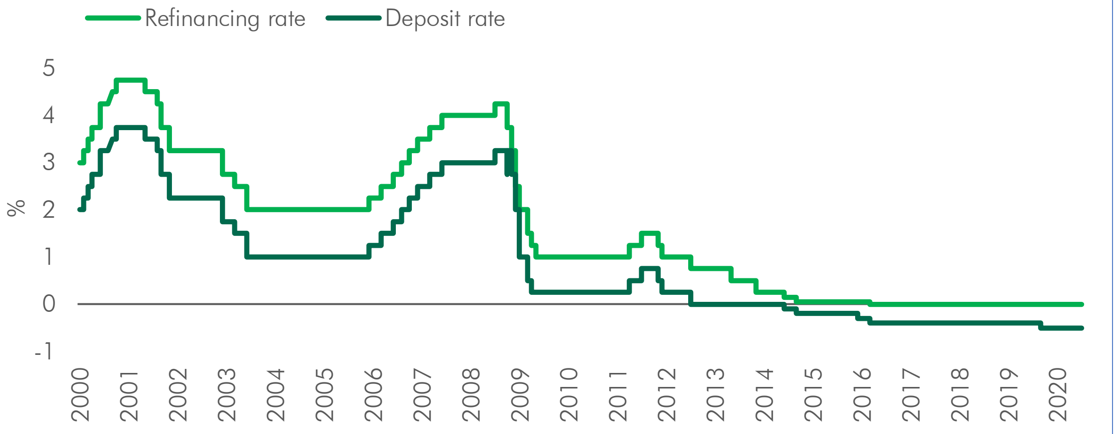
INTEREST RATES: LOWER FOR EVEN LONGER

The ECB remains committed to ensuring that financial conditions remain supportive in the euro area. The deposit rate remains negative and the ECB has increased the size and pace of the Pandemic Asset Purchase Programme (PEPP), and has now committed to purchasing €1.35 trillion of bonds until June 2021. With such a large and committed asset purchase programme, the ECB has created room for Member States to increase debt issuance substantially without borrowing costs rising significantly. The move appears to have stabilised financial markets, with long-term interest rates now at historically low levels and risk spreads between member states narrowing to pre-crisis levels.

Looking further ahead, the weak economic growth and inflation outlook means that CBRE expects monetary policy to remain ultra-accommodative for at least the next 18 months, if not longer. In fact we do not expect short-term interest rates to rise until 2023.

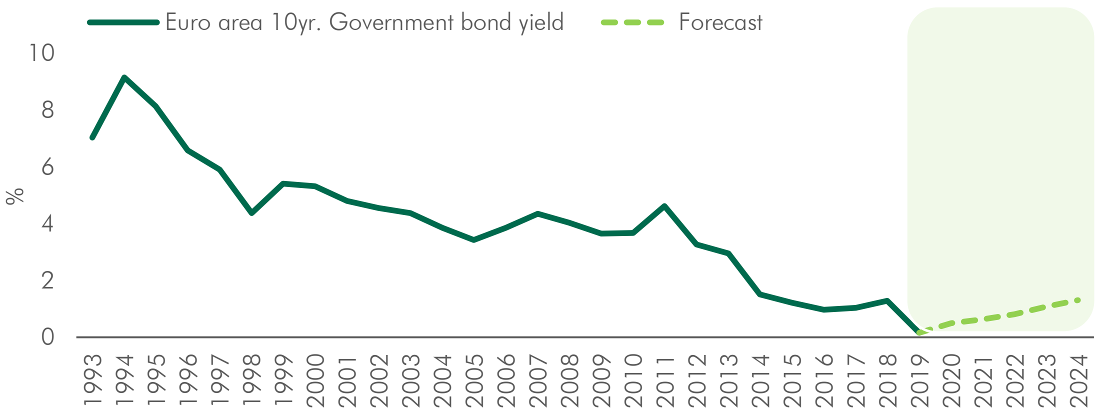
Lower-for-longer interest rates, weaker inflation and significant asset purchases mean long-term interest rates will remain at historically low levels, which is good news for real estate. As the ECB continues to distort prices in liquid financial markets, and with the property spread remaining attractive, there is likely to be an increased interest in real assets such as property.

FIGURE 5: EURO AREA POLICY RATES



Source: Oxford Economics and CBRE Research, 2020

FIGURE 6: EURO AREA 10YR. GOVERNMENT BOND YIELD



Source: Oxford Economics and CBRE Research, 2020

CAPITAL MARKETS

FUNDAMENTALS REMAIN STRONG IN BOTH PUBLIC AND PRIVATE EQUITY MARKETS

PRIVATE EQUITY

Despite a slowdown in EMEA commercial real estate transaction volume in Q2 2020, the private equity market remained robust, with ample dry powder. Preqin data show that fund raising targeting EU real estate investment neared €17 billion in H1 2020, on par with 2019's annual total of €34.5 billion. The period from March-May 2020 saw significant flight to value-add and opportunistic funds, resulting in a 27% y-o-y increase in aggregate funds raised. Activity was led by Blackstone's closing of its sixth European Opportunistic fund, with an eventual US$9.8 billion in potential capital allocation.

Although the volume of funds raised would have been less impressive had this particular close not been reached, such activity by large institutional investors is now the market norm, and remains the optimal route for individuals seeking exposure to commercial real estate, especially during periods of economic uncertainty. In the medium-term, CBRE expects to see the continued raising of funds, led by a few large market players and characterised by heavier portfolio allotment to value-add and opportunistic strategies.

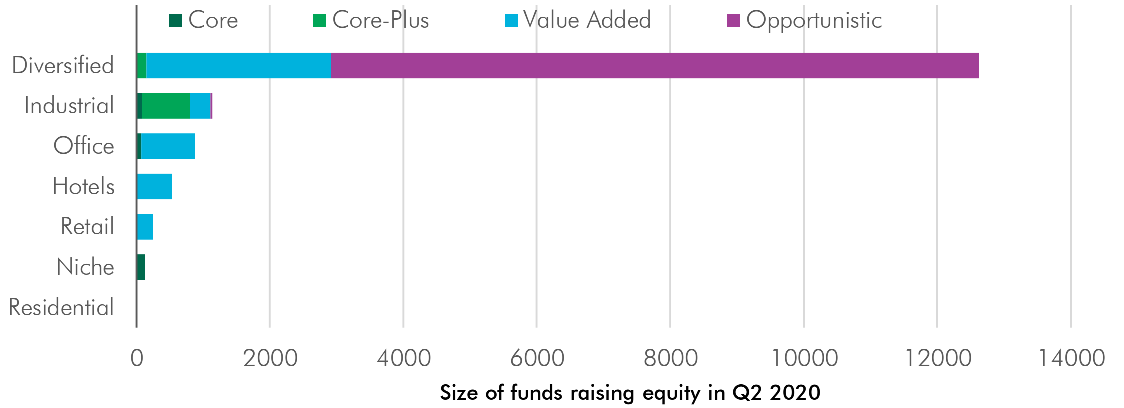
PUBLIC EQUITY

The public equity real estate market closely paralleled wider global benchmarks, registering massive corrections heading into Q2 2020. The subsequent recovery across major global stock indices has yet to be fully observed in the publicly traded real estate market. EPRA indices revealed gains of around 5.5% during Q2 2020 and slight losses so far in Q3 2020, trailing behind the 17.7% climb in the DJI average.

CBRE therefore has a nuanced outlook for publicly traded real estate. On the one hand, as REITS have lagged major global indices, investors may flock to open ended funds as they seek opportunities during the economic downturn. On the other hand, calls for redemptions may force funds to sell at a discount.

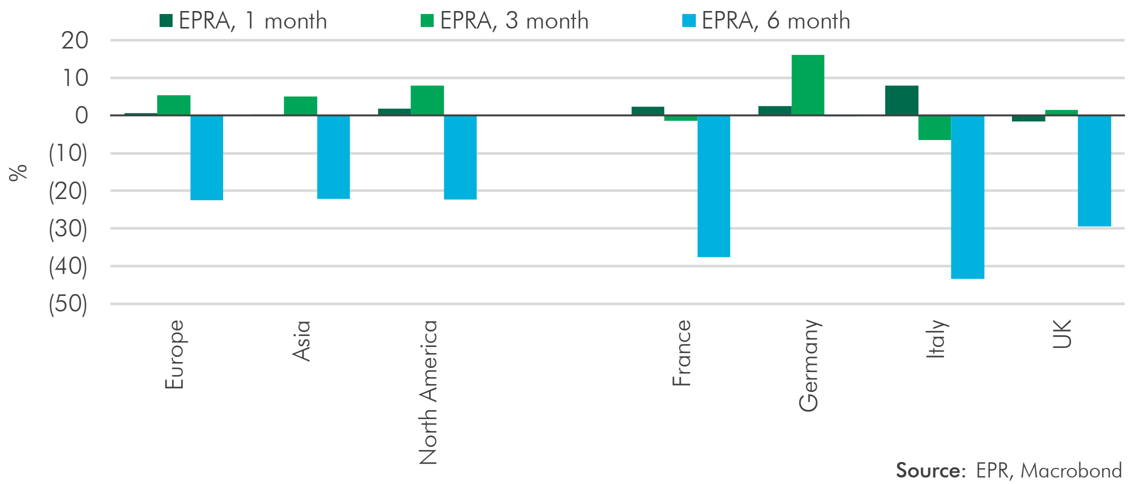
Intensification of NAV discounts for European REITS, the six largest of which had already been trading at a discount of -22% going into Q2 2020, could have implications for distressed selling. In the short- to medium-term, value in public equity markets will be impacted by future developments related to the pandemic, such as the likelihood of a second wave or the successful development of a vaccine.

FIGURE 7: FUND RAISING BY EUROPEAN FOCUSED FUNDS, Q2 2020



Source: Preqin

FIGURE 8: REAL ESTATE VERSUS WIDER EQUITY MARKET PERFORMANCE, H1 2020



Source: EPR, Macrobond

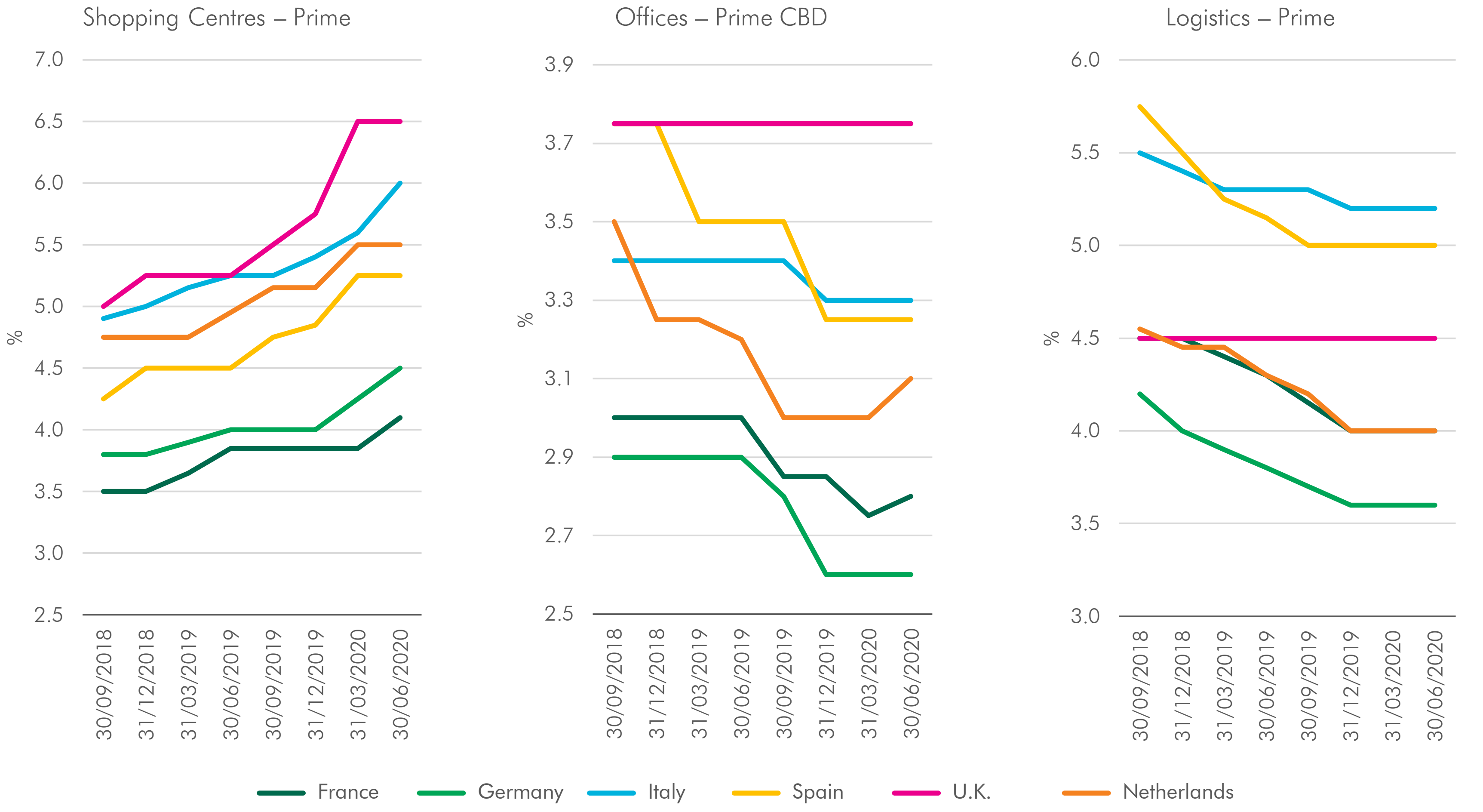
RETAIL AND HOTEL YIELDS MOST AFFECTED

YIELD OUTLOOK

The pandemic continued to weigh on European commercial real estate yields in Q2 2020.
The retail and hotel sectors have been the most affected, with yields for prime shopping centres and hotels (leased) softening in the region of 25 – 75 bps across several locations since Q4 2019. In certain categories, such as secondary retail in the U.K., the variation has been much more pronounced. In the office sector, prime yields, which were compressing in the quarters leading up to the onset of the pandemic, have slightly altered course, either by remaining stable or marginally softening.

Multifamily and logistics yields have been stable and are well positioned to recover. CBRE expects investor appetite for commercial real estate to strengthen in the coming quarters as investors are lured by the spread on the risk-free rate and low long-term interest rates. Yields for most sectors, aside from retail, specifically shopping centres and high streets, will harden. This could happen as early as H2 2020 for logistics, core offices and multifamily. Hospitality will likely take longer to recover due to the profound impact of the pandemic on business travel and tourism.

FIGURE 9: PRIME YIELDS SECTOR COMPARISON



Source: CBRE Research 2020

EUROPEAN COMMERCIAL REAL ESTATE INVESTMENT VOLUME LIKELY TO APPROACH PRE-PANDEMIC LEVELS BY 2022

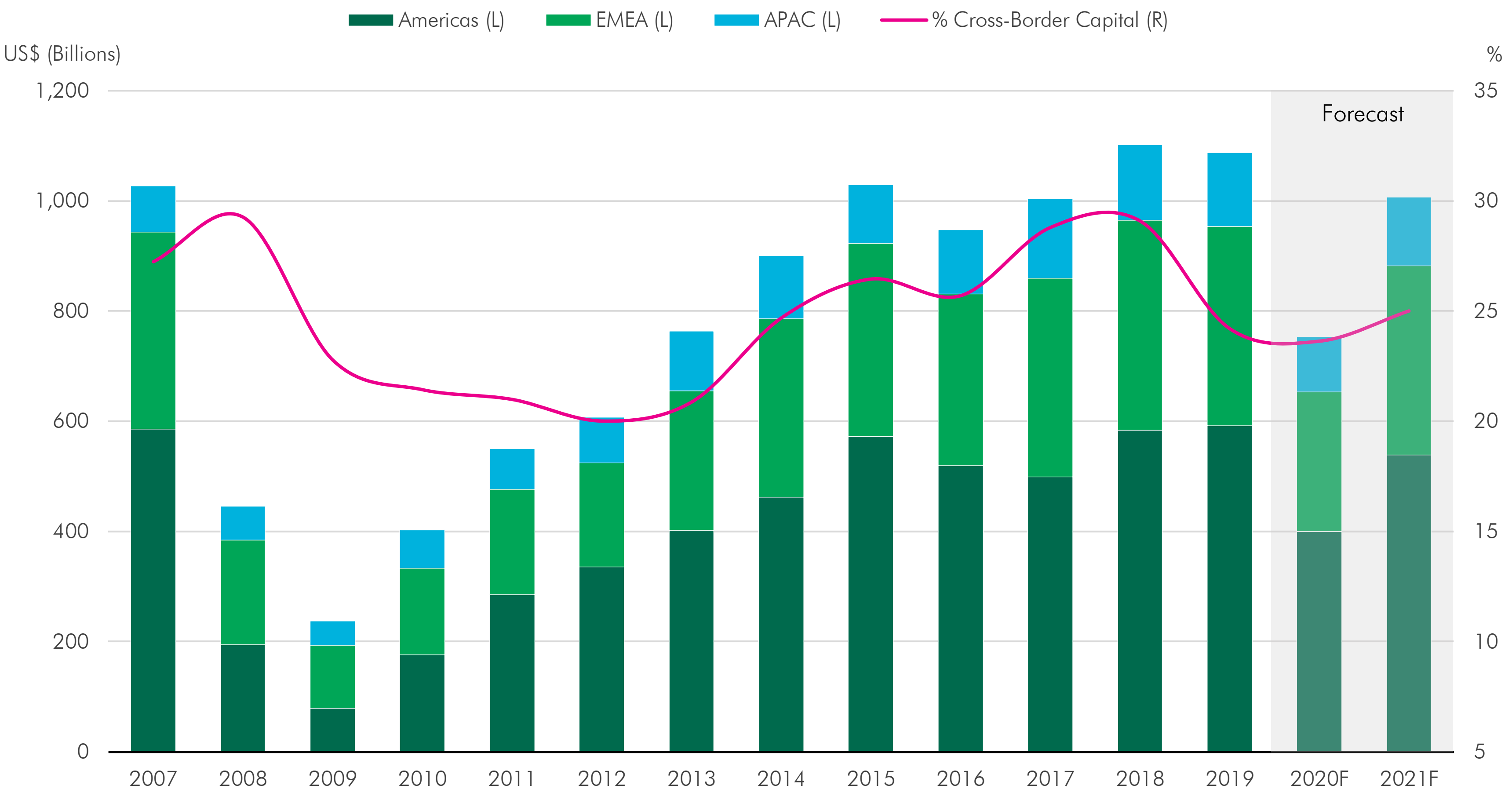
INVESTMENT OUTLOOK

Following the best first quarter on record in terms of investment volume, activity in Q2 2020 was significantly reduced by the pandemic. CBRE transaction data indicates a –39% y-o-y drop in European investment volume over the quarter. However, this figure nevertheless exceeded CBRE's initial estimates of a two-thirds drop, thanks to deal activity picking up in June.

Countries that emerged relatively quickly from lockdowns, including Austria, Germany, and the Netherlands, outperformed other markets in terms of investment volume, and are poised to lead the recovery. However, most deals sized over EUR100 million completed in Q2 2020 were initiated well before the onset of the pandemic, and the weak pipeline may drag on investment volume in the coming quarter. Other concerns include a slowdown in foreign capital inflows into Europe, particularly those from Asia, which typically represent 5% of aggregate investment.

CBRE expects aggregate European commercial real estate investment to fall by between 30-40% y-o-y in 2020. Provided occupier markets do not worsen further, investment activity will return to pre-pandemic levels by 2022.

FIGURE 10: GLOBAL INVESTMENT VOLUME FORECAST



Source: CBRE Research, Real Capital Analytics (Americas), Q2 2020

INVESTORS FOCUS ON VALUE-ADD AND ALTERNATIVE STRATEGIES

VALUATION OUTLOOK

Downward pressure on rental income is expected to weigh on capital values in the short- to medium-term. Cap rates should therefore expand over the same timeframe, a trend that to some extent is already supported by market evidence. Repricing of around -25% has been observed in value-add secondary office locations as well as value-add investments in traditional sectors. However, cap rates in core markets, especially those for logistics and office assets, have generally remained stable.

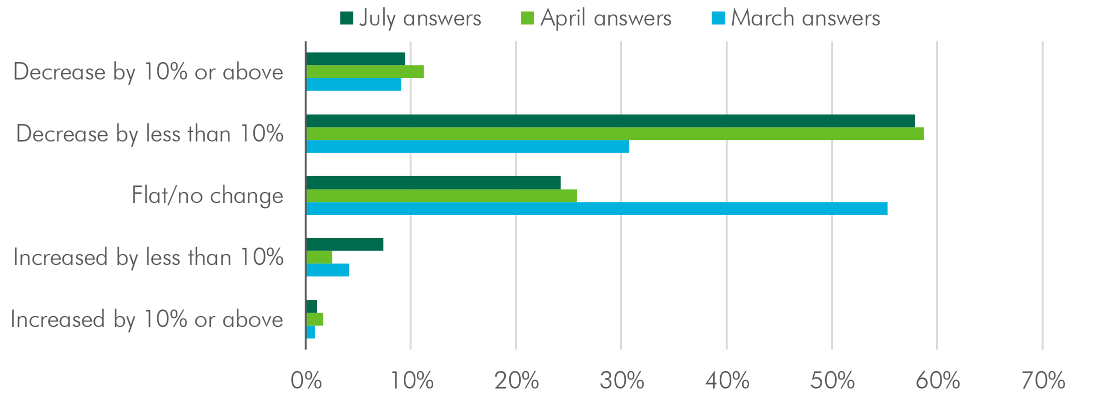
While an abundance of capital is ready to be deployed through private equity channels, transactions in the near term are contingent upon repricing. The pause in private debt markets in Q2 2020 has led to an increased cost of borrowing, estimated at around 50 bps in Europe. This development, coupled with lenders implementing lower LTVs, will continue to affect underwriting in the short- to medium-term – a trend that will benefit equity firms and investors. Repricing across the retail, hotel and selected alternative sectors, as well as value-add strategies across traditional sectors, may intensify in the short-term.

INVESTMENT STRATEGY OUTLOOK

Rapid ecommerce growth and a drive to shore up domestic supply chains will provide a solid foundation for logistics markets. Multifamily investment, also defensive in nature, offers reliable income streams and stable capital values. Those seeking exposure to this sector, which many currently consider to be trading at a premium, may wish to pursue opportunities in specialised sub-sectors, such as student housing. Therefore, investment in REITs, particularly those with selective alternative investments, may have strong growth potential, especially considering their attractive discounts.

Positive sentiment in continental European occupier markets, reflected by the gradual return of office-based employees to their workplaces and increased footfall in retail, is also likely to support core investment in the coming quarters. Investors seeking higher yields and possessing a greater risk appetite may wish to consider heavier portfolio allocation to alternatives, core retail and value-add strategies in traditional sectors, all of which are in the midst of repricing.

FIGURE 11: EMEA CAP RATE SURVEY – Q1: 'What was the change in asking prices/asset valuation this month compared to that immediately prior to the COVID-19 outbreak?'



Source: CBRE Research 2020. Survey sent to CBRE EMEA Capital Market Professionals

KEY TAKEAWAYS

- While investment volumes dipped by 39% in Q2 2020, there remains ample unallocated capital and pent up demand for European prime property.
- Public real estate markets will remain volatile in the short-term but may ultimately make up ground with global stock indices. Given current levels of market liquidity, the future course of the pandemic will be a major factor in returns.
- Yields and pricing for core logistics and office assets should remain stable in the near term.
- Although contingent on repricing, investors are displaying renewed appetite for value-add and core plus investments.
- Other opportunities include multifamily, logistics and selective investment in REITS with exposure to alternatives.

OFFICES

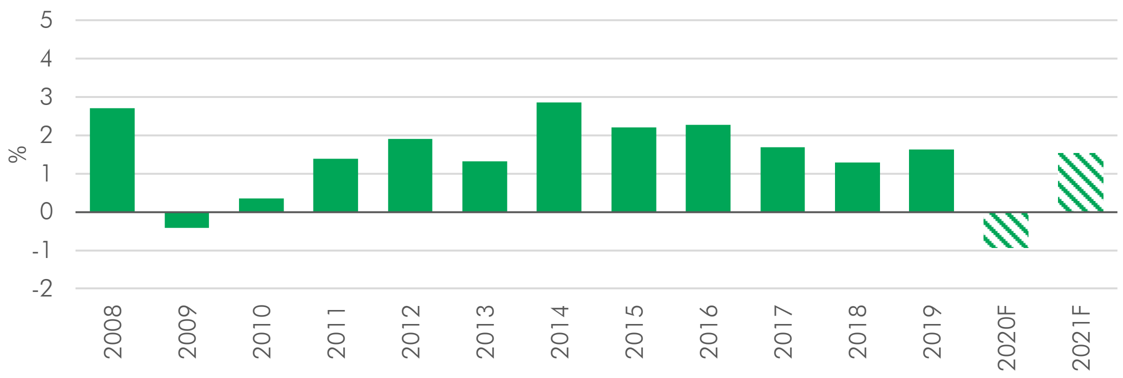
USER DEMAND: SHORT-TERM NEGATIVE BUT SIGNS OF RESILIENCE

- Early indications point to some degree of resilience for many office-using sectors. Office-based employment (OBE) for the EMEA region as a whole has been stable up to mid-year, with some cities including Berlin, Amsterdam and Madrid retaining some positive momentum.

- However, labour markets are clearly weakening and reductions in headcount will temper demand in the short-term, particularly as employment and wage support schemes taper. CBRE expects OBE to fall by about 1% over full-year 2020 before growth returns across most major markets in 2021. This will result in an overall rebound of around 1.5%, roughly in line with the 2017-19 annual rate of growth.

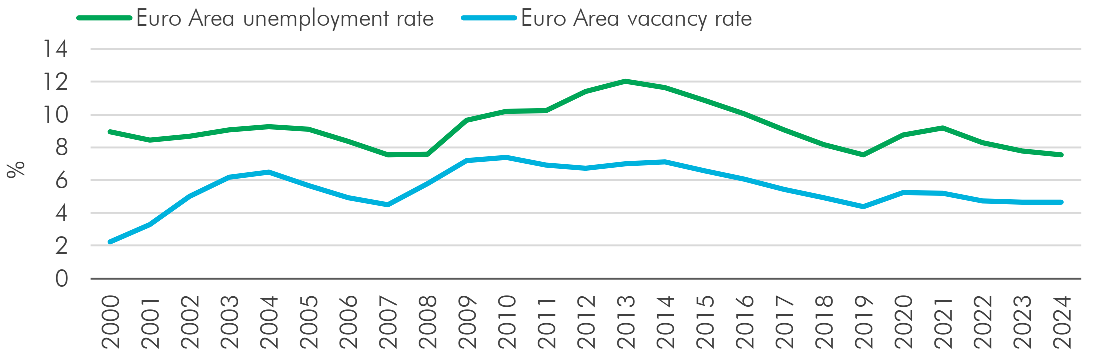
- Technology and knowledge-based sectors have tended to dominate take-up in many markets, and remain somewhat better-positioned in terms of short-term revenue prospects. Over the medium-term, a rather more balanced demand profile looks likely.

FIGURE 12: OFFICE-BASED EMPLOYMENT GROWTH (EUROPE MAJOR MARKETS % Y-ON-Y), 2008-21



Source: Oxford Economics and CBRE Research, 2020

FIGURE 13: UNEMPLOYMENT RATE (%) VS OFFICE VACANCY RATE (%), EURO AREA, 2000-2024



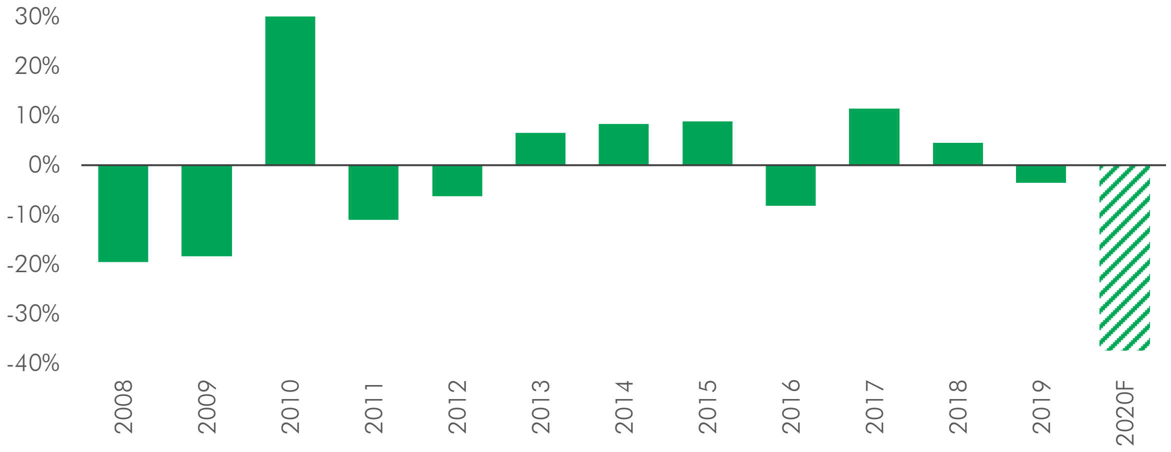
Source: Oxford Economics and CBRE Research, 2020

LEASING VOLUME: SHARP BUT SHORT-LIVED SLUMP

- With the effects of lockdown measures on office demand slow to become apparent, leasing volumes initially fell gradually, with tight supply conditions still a constraint in many markets. Q2 2020 data have started to reveal the extent of the lockdown-induced downturn more fully, with gross leasing levels across the main European markets falling by 49% y-o-y to the lowest quarterly total in over 20 years. Take-up in H1 2020 was 35% lower than H1 2019. Smaller requirements have been particularly impaired but demand for larger units is also becoming patchy.

- For the main European office markets, CBRE expects take-up to decline by up to 40% this year, a steeper single-year fall than anything seen in the aftermath of the Global Financial Crisis.

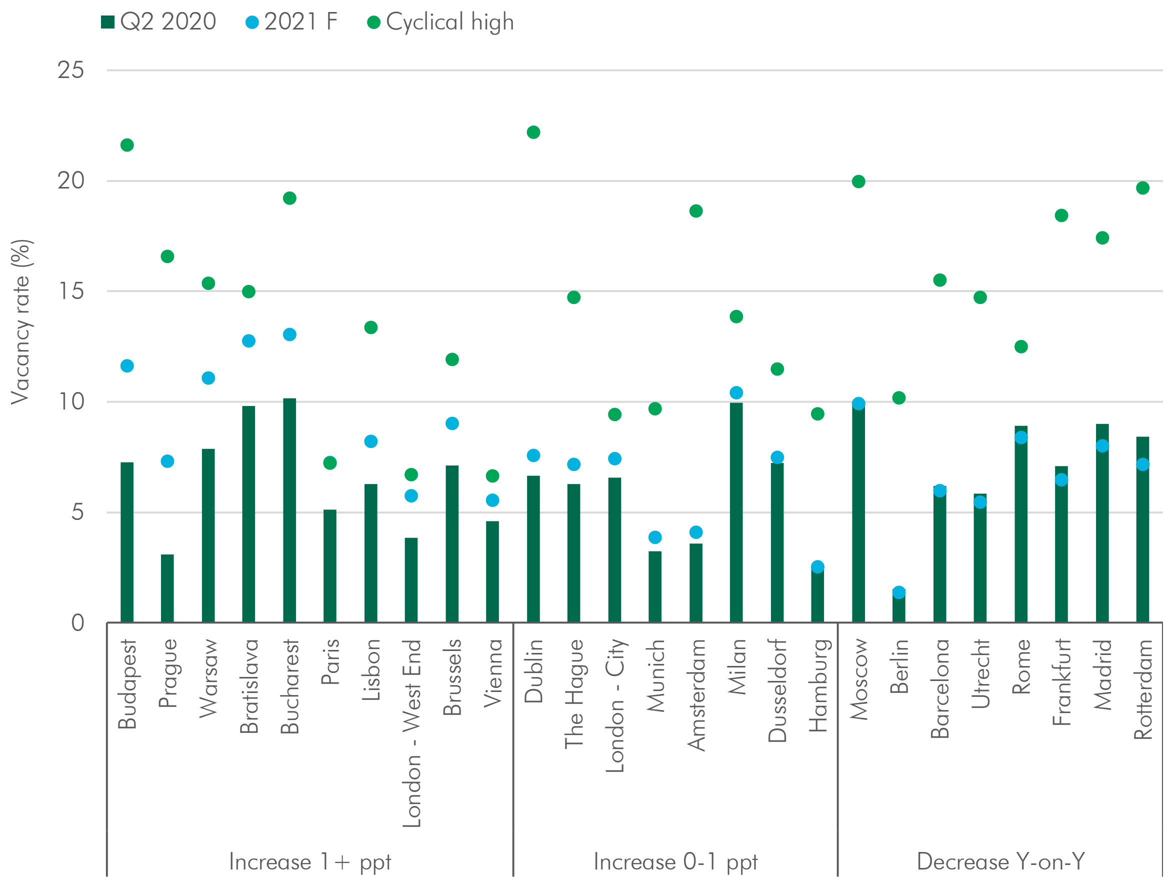
FIGURE 14: EUROPEAN OFFICE LEASING, 2009-20 (% P.A.)



Source: CBRE Research, 2020

VACANCY: STEADY RISE FROM RECENT TROUGHS BUT CAPPED BY SLOWER DEVELOPMENT

FIGURE 15: CURRENT AND FORECAST VACANCY RATES RELATIVE TO CYCLICAL PEAKS



Source: CBRE Research, 2020

- 2020 will represent a watershed in new office supply. Vacancy rates in most major markets had been trending down for most of the past five years, to a point where leasing levels were being stifled by a lack of options. The expected rise in vacancy this year therefore signifies a clear turning point.
- Most major cities are likely to see an increase in vacancy of 1-2 percentage points to levels that are still mostly lower than previous highs.
- Curtailed development will limit the rise in vacancy. Even though the effect may not be immediate, with new completions running well above 2019 levels, this could still produce shortages of prime space in the medium-term, particularly since over 55% of expected new supply in major cities from now until end-2021 is already pre-let. This is truer for western European markets where expected vacancy growth is more muted, than for parts of CEE where development-fuelled supply growth appears far more likely. Major markets including Bucharest, Moscow and Budapest look particularly exposed.
- While lockdowns have stifled deployment, the amount of available capital remains high and should give confidence heading into H2 2020. With the pandemic necessitating changes to layouts and specifications, well-located properties or refurbishment of good secondary assets may provide opportunities for developers, particularly in some of the larger Western European markets such as Amsterdam.

RENTAL OUTLOOK: SHORT-TERM NEGATIVE BUT GOOD PROSPECTS FOR A REBOUND

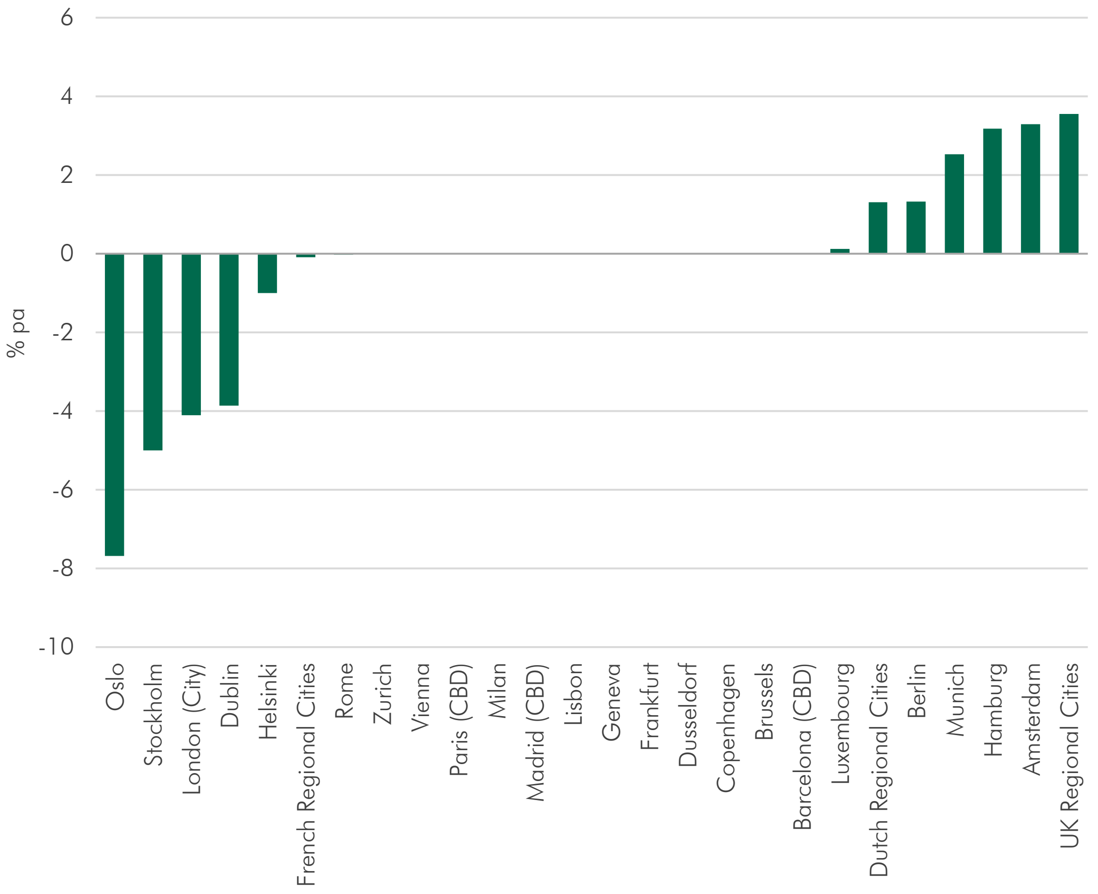
- Rental growth in the major European cities was already starting to ease in the early part of this year. The downturn will accelerate this process and pitch several markets into negative territory before year-end. These markets include London, Dublin and Stockholm, where we expect falls of 3-5%.

- Markets that might buck the trend and see rent increases in 2020 are mainly located in Germany and the Netherlands, where the impact of lockdowns has been less severe and where vacancy was very tight going into the pandemic. This generally reflects the impact of growth in Q1 2020, with H2 2020 likely much weaker. Most of the other larger markets look flat.

- While there are some markets – notably Paris and parts of CEE – where downward rental pressure looks set to persist or be delayed into 2021, in general a demand recovery will be sufficient to cause a rental rebound next year. Occupier incentives will naturally expand in the meantime.

- With the short-term outlook volatile, investors and occupiers should where possible seek to ascertain optimal times to deploy capital or to re-gear leases. On a five-year view, London, Paris, the Nordics and Spain look like strong rental plays.

FIGURE 16: PRIME RENTAL FORECAST (%), FULL YEAR 2020



Source: CBRE Research, 2020

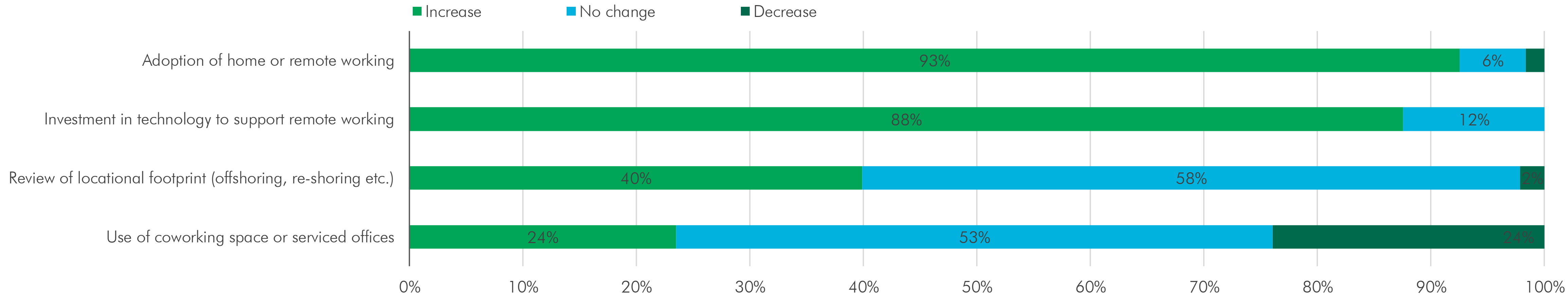
ACCELERATED AGILITY: THE SHIFTING ROLE OF THE OFFICE

- As well as introducing massive short-term volatility, the pandemic is also accelerating a number of structural processes leading towards more fluid, multi-format real estate portfolios.
- Expanded employee choice will likely include more remote working, including in satellite or suburban locations that do not require extensive commuting.
- Technology investment in buildings will be crucial both for the existing motive of enhanced user experience but increasingly also for health management and wellbeing. Expect a widening value gradient between prime, tech-enabled buildings and poorer stock.

KEY TAKEAWAYS

- Short-term rental volatility offers opportunities for astute timing of capital deployment and lese audits. Expect turning points in many markets in late 2020 or early 2021. Occupiers should seek to maximise short-term incentives even where headline rents are stable.
- Occupier demand shifting increasingly towards tech-enabled 'smart' space, offering development or refurbishment opportunities.
- Health, wellbeing and sustainability becoming the touchstones of occupier choice. Early mover investors should target assets accordingly.

FIGURE 17: KEY STRATEGIC CHANGES ANTICIPATED BY OCCUPIERS



Source: CBRE Research, 2020

OCCUPIER TRENDS

SENTIMENT AND REALITY: NAVIGATING A COMPLEX AGENDA

Corporate occupiers are currently engaged in a delicate balancing act, transitioning from crisis-mode to preparing, and executing, plans for the future of work. Organisations are having to get this balance right across Europe as countries come out of local lockdowns at varying speeds; offices in Germany and the Netherlands have been open much earlier than the UK, for example.

Grounded in making the best decisions possible for the safety and productivity of employees in an environment where revenues, headcount and a vaccine are uncertain, occupier sentiment can be characterised across three key areas. Each of these areas have complex, intertwining and nuanced business realities, that will manifest themselves differently across geographies and businesses over the next 12 months and beyond.

FOCUS OF OCCUPIER SENTIMENT DURING COVID-19 CRISIS

REMOTE WORKING	DE-DENSIFICATION	PORTFOLIO STRATEGY
THE FLUID WORKPLACE	WELLNESS AND EXPERIENCE	FLEXIBLE OFFICE AND AGILITY

BUSINESS REALITY IN THE POST-COVID-19 ERA

TOWARDS AN INCREASINGLY FLUID WORKPLACE

NOT A QUESTION OF 'ON OR OFF?' BUT A QUESTION OF 'WHERE AND WHEN?' FOR THE FUTURE OF THE OFFICE

Speculation abounds on the future of the office, with a handful of corporate announcements on the permanency of home-working strategies being misconstrued by many as implying a long-term shift from the office to the home as the permanent place of work. The reality for multi-service and multi-location businesses is not a binary choice of the office or the home, but one of fluid working requiring fluid workplace options.

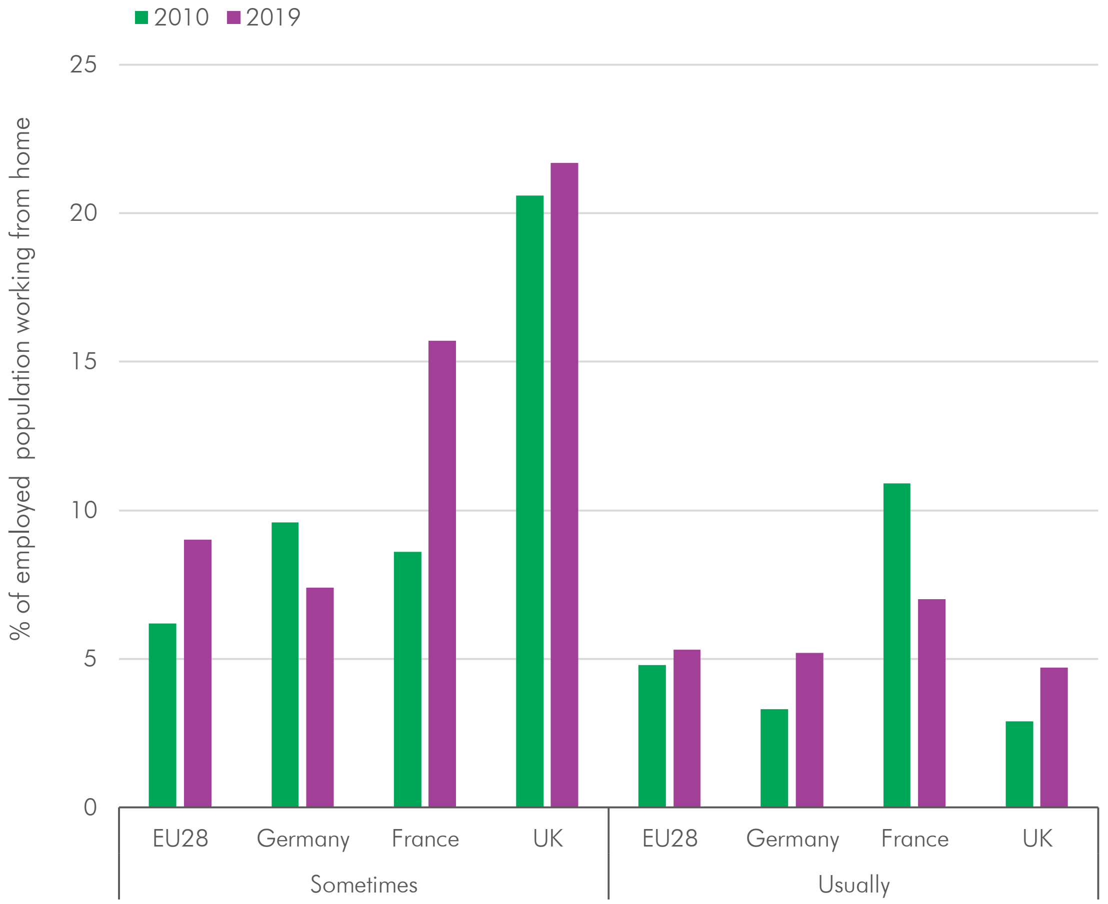
While 93% of occupiers in CBRE's recent European Occupier Survey indicated that remote working will increase in the coming years, this will not necessarily be as a replacement for office space. Fluidity will come in the form of working from a variety of locations (from home, to headquarters, to flex office to coffee shop) reflecting the diversity of tasks and the preferences of employees.

In the next 12 months we will see differing transition speeds to fluid working across geographies depending on national work culture and the trajectory out of lockdown.

For example, at aggregate European level, the proportion of the workforce working from home 'sometimes' has risen from 6% to 9% over a 10-year period. This is not a uniform trend; in Germany this proportion has declined with workers shifting from working from home 'sometimes' to 'usually' in increasing numbers, the opposite to what we have seen in France. The UK has been the most fluid of these countries, with over a fifth of employees working from home 'sometimes' over the decade.

Both working from home 'sometimes' and 'usually' mean that most employees go to an office much of the time. The outlook for at least the next 12 months would therefore suggest that the temporary forced mass remote working pilot will help accelerate the trend of fluid working, rather than lead to a wholesale structural shift in such a short-period of time. Fixed elements of culture and urban structure are critical factors in understanding this underlying trend.

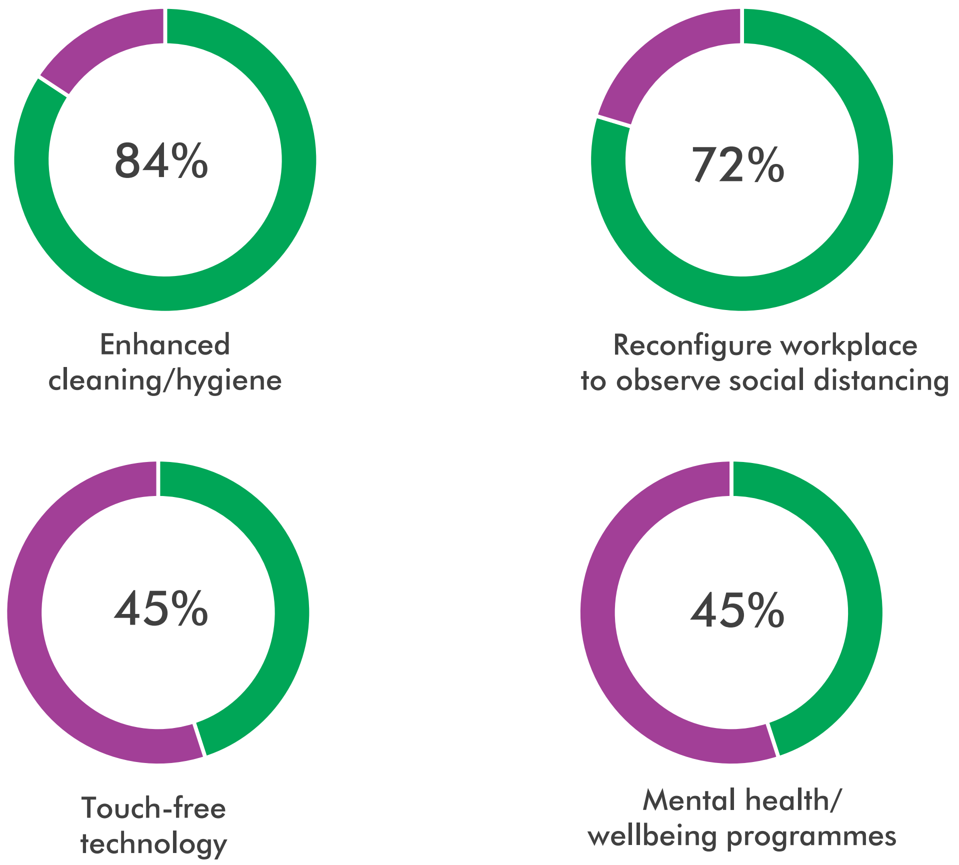
FIGURE 18: WORKING FROM HOME PROPENSITY, SELECTED COUNTRIES



Source: Eurostat, CBRE Research, 2020

WELLNESS & EXPERIENCE: ENCOURAGING A FLIGHT TO QUALITY

FIGURE 19: PERCENTAGE OF OCCUPIERS EXPECTING TO ADOPT WELLBEING MEASURES POST-COVID-19



Source: CBRE Research, 2020

There will be a subtle acceleration of the trend towards greater provision and focus of wellbeing measures in the workplace over the next 12 months.

This will begin with a review of workplace density, cited by 46% of European occupiers in CBRE's survey, but will extend beyond this, including the continuation of health and safety elements enforced by the pandemic (e.g. enhanced cleaning and observation of social distancing) as well as investments in touch-free technology and mental health and wellbeing programmes.

What the pandemic catalyses is the trend of occupiers looking for and trying to create great workplaces that attract, retain and engage the best talent across markets.

Even pre-pandemic, among the fastest growing building selection factors cited by occupiers were brand image (from 22% to 55%), smart building technology (18% to 33%) and wellness capability (17% to 25%). These are all factors which are more explicitly aimed at talent rather than building operations, and are all factors which occupiers will be looking for more in the near-future.

This will renew the attractiveness of prime trophy headquarters space, particularly in core office markets, which may lead to greater divergence in performance of prime and secondary office stock. As we come to the end of the current real estate cycle which in general has seen limited development of new space, competition for the best new space may increase.

LESS DENSE BUT BETTER-QUALITY SPACE WHICH IS MORE SUPPORTIVE OF EMPLOYEE WELLBEING AND BRAND

FLEXIBLE OFFICE & AGILITY: A GROWING RANGE OF SOLUTIONS

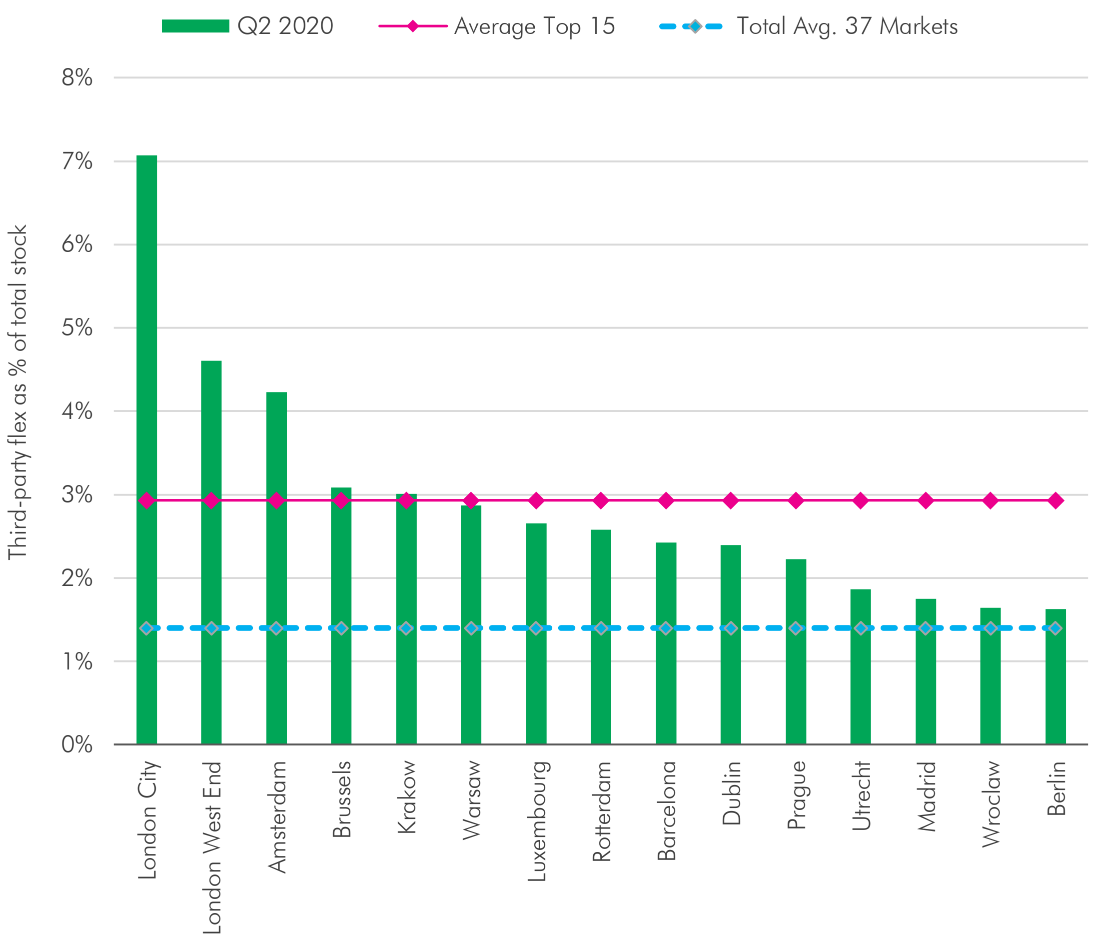
With the outlook for fluid working set to increase and heightened pandemic and economic uncertainty to continue, occupiers of all sizes will increasingly look to create more agility within their portfolios, alongside high-quality, long-term core space. Agility will be provided to employees in a number of ways depending on the organisation.
It will cover:

- Increased tech investment to enable home and remote working.
- Increased availability of satellite suburban/local/peripheral serviced office space.
- Increased availability of drop-in touchdown space via memberships.
- Development and refinement of 'Hub & Spoke' strategy.

The provision of flexible office space in Europe's cities has been growing at an average of 30% per annum since 2014, but has not produced uniform levels of flex stock levels across the continent. The main contributor to that growth has been third-party operators leasing space from landlords, which we expect to slow down or even contract in H2 2020 in some markets. With only five markets having third-party flex penetration above 3% (which will dwindle) it raises the question of whether Europe has enough flex space to fulfil potential demand.

We expect landlords to make-up for this under-provision through providing more tenant-ready, managed and flexible office space, not just to meet occupier demand but to alleviate vacancy and monetise space as overall demand begins to weaken in an uncertain environment.

FIGURE 20: TOP 15 FLEX MARKETS BY THIRD-PARTY MARKET PENETRATION



Source: CBRE Research, 2020

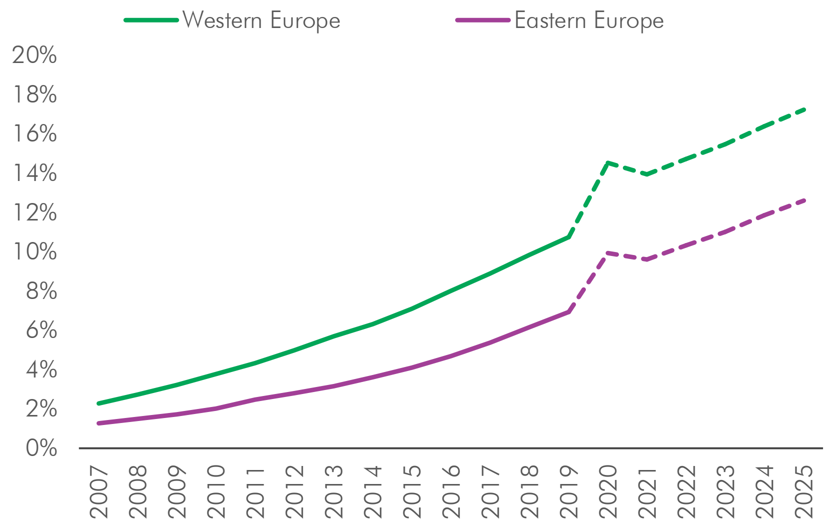
LOGISTICS

LOGISTICS DEMAND EXPECTED TO HOLD UP

Despite being much better positioned than most other sectors, logistics has not been immune to the impact of the pandemic. The main sources of demand have been affected, with both positive and negative lasting consequences for logistics property. Ecommerce sales, the main demand driver over the last few years, have seen a spike in activity due to lockdowns and will emerge from the crisis at a significantly higher level, leading to a further uptick in logistics requirements from this sector.

While global trade was already threatened by protectionist disputes and Brexit heading into 2020, the pandemic has worsened conditions, as evidenced by the increase in idle capacity reported by ocean freight companies. Although the manufacturing sector has been hit hard, the reopening of production plants has increased the focus on how to improve supply chain resilience to avoid future shortages. This trend could potentially benefit logistics property via increased demand for space to increase safety inventories and re-shore suppliers in Europe.

FIGURE 21: ECOMMERCE PENETRATION FORECAST WESTERN AND EASTERN EUROPE



Source: Euromonitor, Forrester and CBRE, July 2020

FIGURE 22: GLOBAL TRADE EXPORTS GROWTH FORECAST: SINGLE AND DOUBLE HIT SCENARIOS (2007 = 100)

Source: OECD, July 2020

LOGISTICS DEMAND DRIVERS

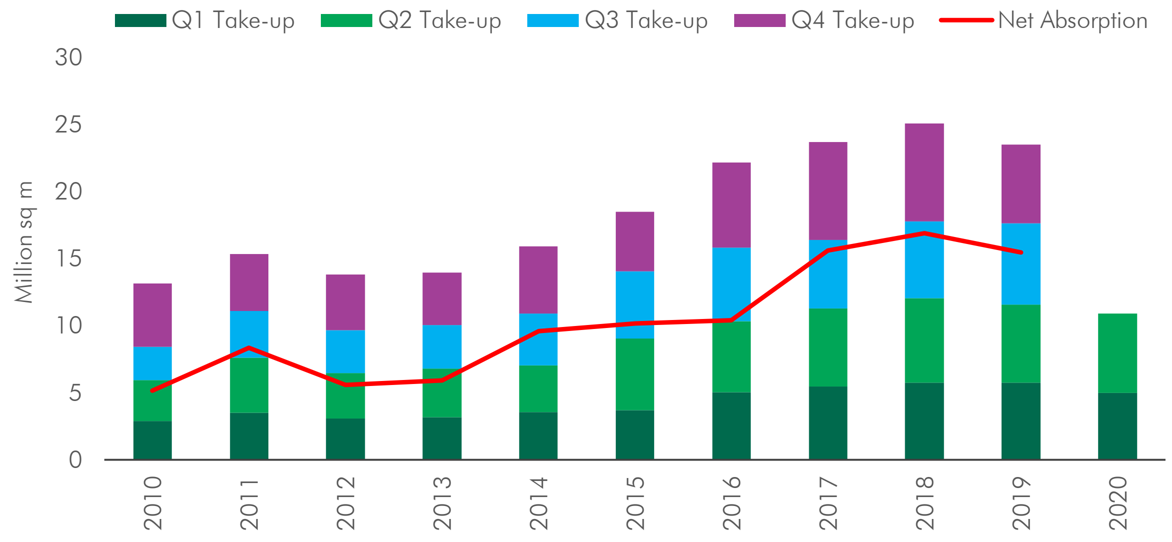
	SHORT TERM DEMAND	MID-TERM DEMAND
ECOMMERCE	INCREASED	INCREASED
GLOBAL TRADE	REDUCED	SLOW RECOVERY
MANUFACTURING	REDUCED	INCREASED AS SAFETY INVENTORIES INCREASE

SUPPLY IS TIGHTENING

Take-up in tier 1 markets in Europe was stronger than expected in Q2 2020 considering the challenging conditions, particularly in the UK, where take-up registered an all-time high. This provided further proof of the overall resilience of logistics demand. Demand came in the form of new pre-let units but also ready-to-occupy facilities, further tightening the already scarce supply of new warehouses. Additionally, approximately 70% of the development pipeline for 2020 was already committed via pre-lets and built-to-suit units, meaning that there will be stiff competition among occupiers for space in speculative developments due to be completed this year.

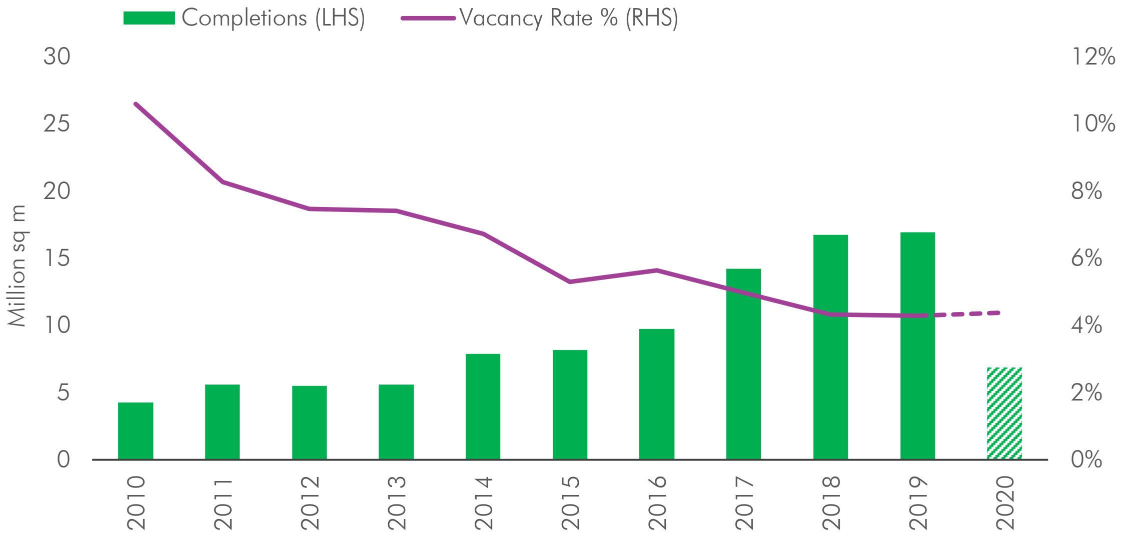
*Tier-1 European Logistics markets are Germany, France, the United Kingdom, the Netherlands, Italy, Poland, Spain, Belgium and the Czech Republic.

FIGURE 23: TAKE-UP AND NET ABSORPTION TIER-1 EUROPEAN LOGISTICS MARKETS* (M SQ M)



Source: CBRE Research, 2020

FIGURE 24: COMPLETIONS AND VACANCY RATE TIER-1 EUROPEAN LOGISTICS MARKETS* (M SQ M)



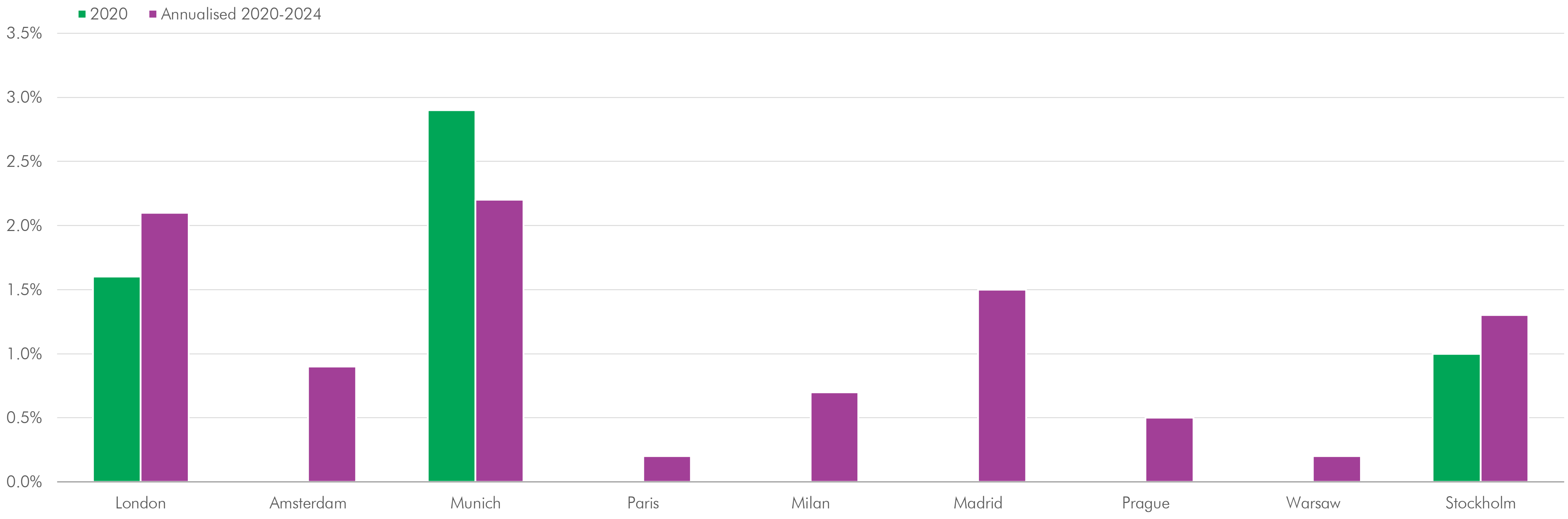
Source: CBRE Research, 2020

PRIME RENTS EXPECTED TO RISE

The strength of the logistics sector is also evident in CBRE's headline prime rental forecast for the main submarkets. Most locations are expected to show no change during 2020, in contrast with most other property sectors.

In the long-term, the annualised growth forecast remains positive for all locations, with further upward pressure in those markets with severe restrictions on land and stock availability, such as London and Munich.

FIGURE 25: LOGISTICS HEADLINE PRIME RENTS FORECAST



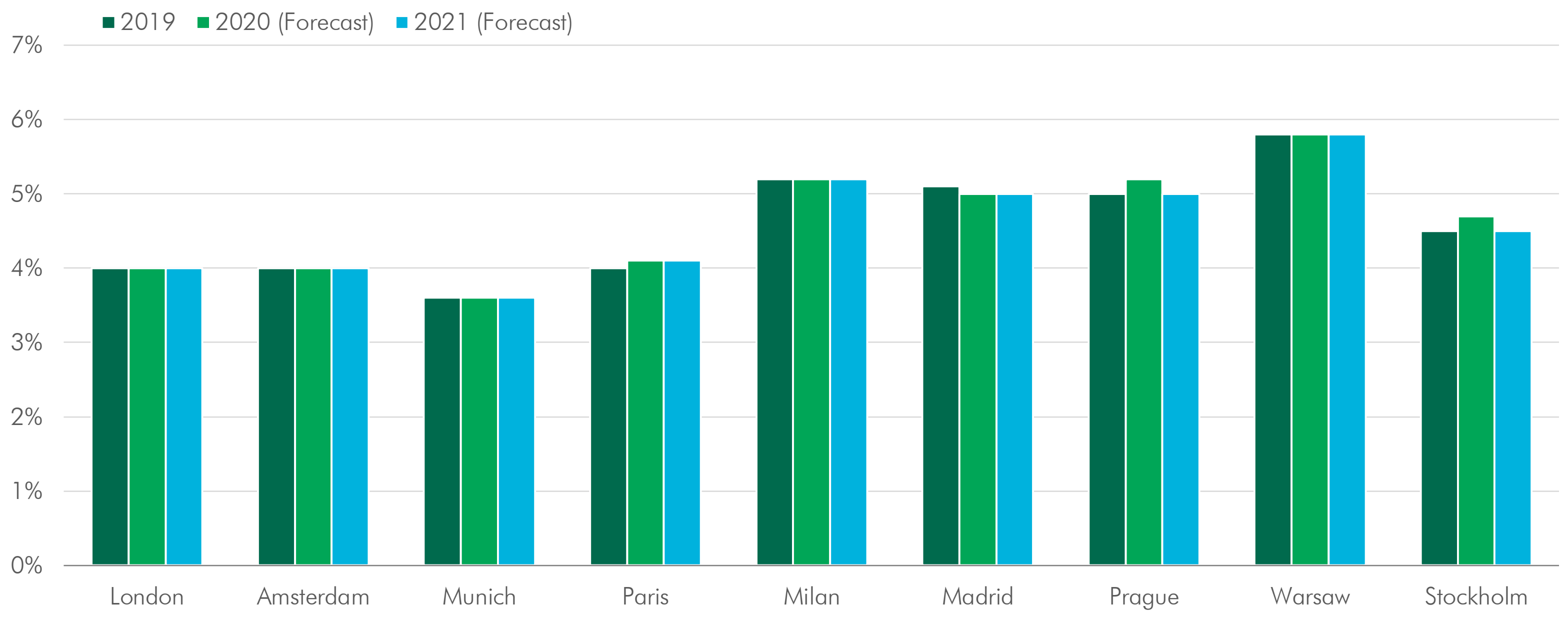
Source: CBRE Forecast, June 2020

INVESTMENT MARKET SET TO BOUNCE BACK STRONGLY

Prime logistics yields are expected to be stable and, in most cases, remain at historical lows. Strong occupier demand is generating robust investor interest, with some groups looking to increase their exposure and others seeking to enter the sector for the first time. Many investment opportunities will be derived from anticipating occupier needs and understanding customer strategy, especially around desired improvements in supply chain resilience.

Logistics is well positioned to continue to outperform most other sectors, supported by strong fundamentals and reinforced occupier demand. Developers looking to capture forthcoming demand are expected to accelerate the construction of new projects. Other opportunities lie in repurposing well connected retail parks close to cities and refurbishing units to accommodate on-demand warehousing.

FIGURE 26: LOGISTICS PRIME YIELDS FORECAST



Source: CBRE Forecast, June 2020

KEY TAKEAWAYS

Opportunities in the logistics sector emerge from the resilience of the occupier demand and the needs to:

- Be closer to customers
  - ✓ Growth of satellite distribution hubs near major urban locations
  - ✓ Food retailers
  - ✓ Repurposing of well connected retail parks
  - ✓ Increased attention on cold storage
- Improve supply chain resilience
  - ✓ Increased safety inventories
  - ✓ Diversification of suppliers
  - ✓ Efforts to accelerate automation

RETAIL

THE ERA OF TACTICAL SHOPPING

Due to the prolonged closure of non-essential retailers for as long as one to three months and social distancing measures, consumers have readjusted their shopping behaviours. Key trends include:

- Queuing and booking appointments online/in app
- Increased levels of online shopping
- Preference for local shops

A shift in shopping behaviours was also observed after lockdowns were lifted. Changes include:

- Reduced dwell times combined with a shift to more focused shopping
- Higher spending per person compared to the pre-pandemic period
- Increase in ticket value by up to 10 to 15% in some markets

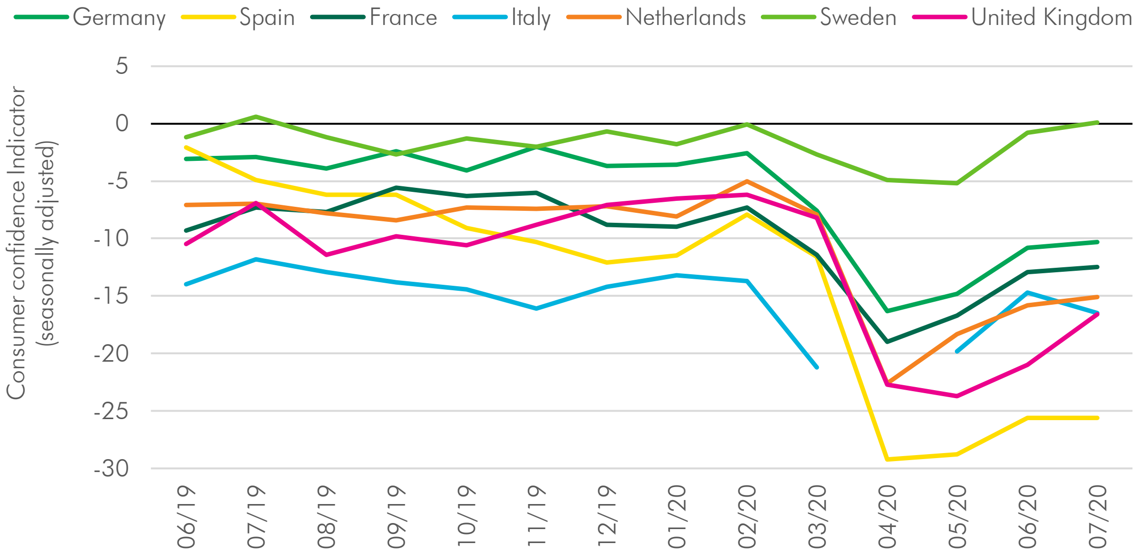
SELECTIVE SPENDING IN UNCERTAIN TIMES

While consumer confidence rebounded in all markets as non-essential retail reopened, this has been counterbalanced with concerns over the global economy and job uncertainty, which are likely to lead consumers to continue to spend cautiously.

STEADY RECOVERY OF FOOTFALL

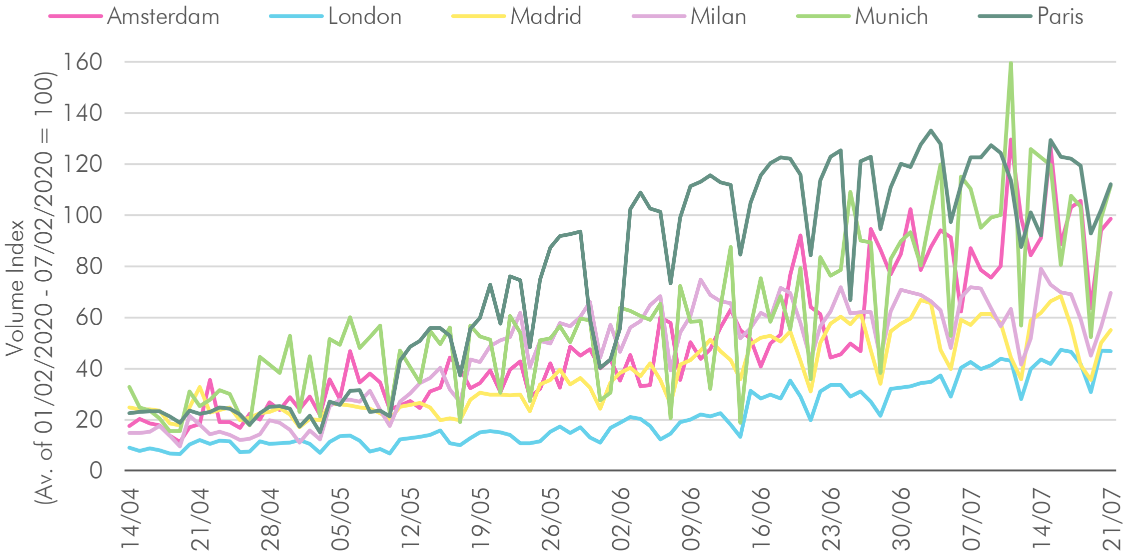
Despite the absence of tourism – especially in Spanish, Greek, Italian, French, German and British cities – and lack of events attracting consumers to shopping centres and high streets, footfall recovered steadily after lockdown in most countries. CBRE expects the rebound to continue in all markets, provided there is no second wave of COVID-19 cases leading to large-scale nationwide lockdowns.

FIGURE 27: REBOUNDING CONSUMER CONFIDENCE



Source: Eurostat. No data for Italy for April 2020 available

FIGURE 28: HIGH STREET FOOTFALL POST-LOCKDOWN



Source: CBRE Supply Chain & Consumer Advisory, data as of 21 July 2020

THE RETAILER RESPONSE

The abrupt nature of (re)lockdown and reopening, shifting consumer preferences and continuously changing government policies have created uncharted market conditions, making it hard to predict retail sales and operations in the coming months, let alone 2021.

Accelerating structural changes will lead to continued administrations and rental recalibrations over the next six months. Rent concessions are part of the strategy to safeguard cashflow. The strength of asset and performance figures will dictate retailers' response to individual negotiations.

Retailers have also responded by refocusing on consumers and online sales and rationalising portfolios. Examples of practices include:

RENEWED FOCUS

- Stronger focus on omnichannel online sales but brick-and-mortar stores remain key to generating profit
- Steering consumers towards click-and-collect
- Expansion of home delivery slots
- Direct sales to consumers
- Digital campaigns focusing on brand experience

RATIONALISATION

- Acceleration of store portfolio consolidation
- Medium sized retail spaces vacated
- Expansion strategies and strategic frameworks rethought (e.g. Inditex)
- Sale and leaseback of headquarters (Ted Baker), warehouses (Next) and factories (Wolford)

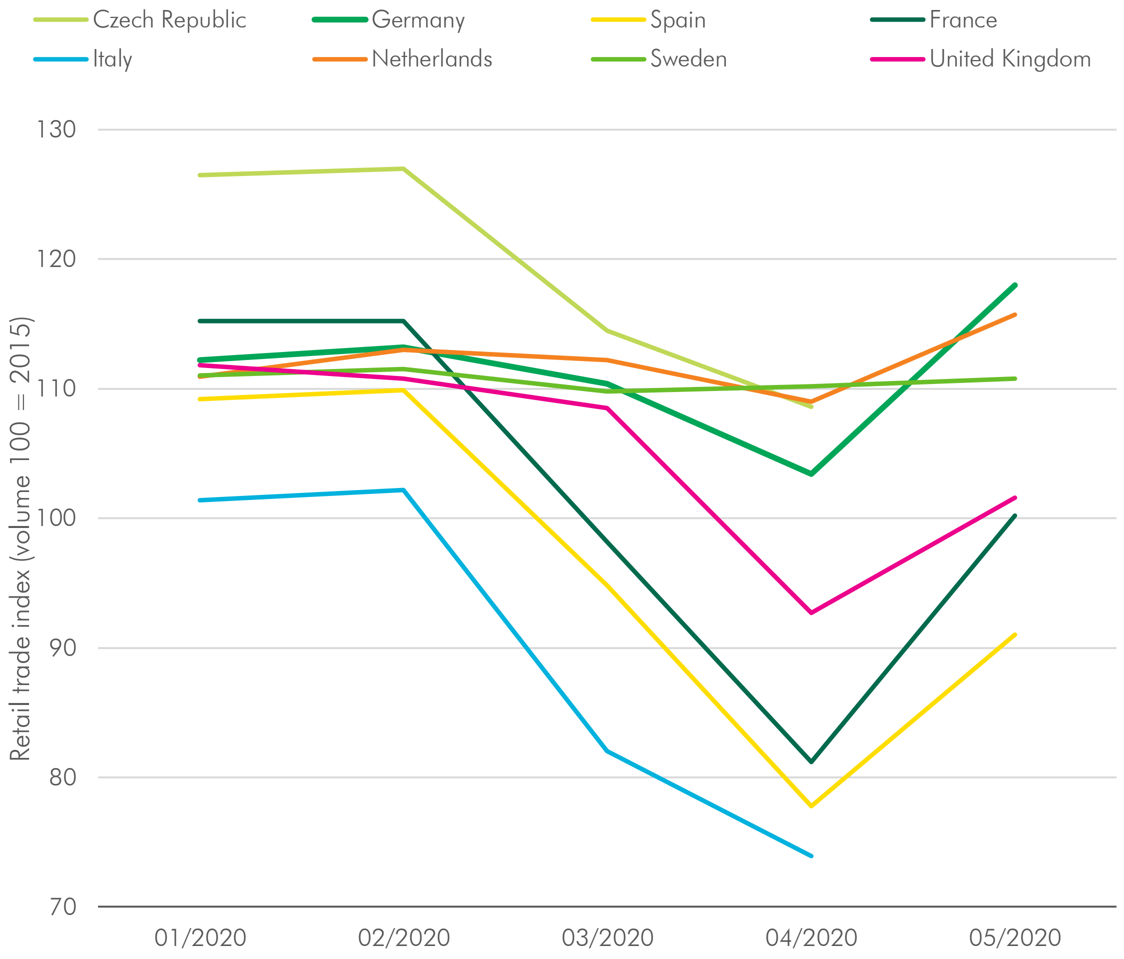
RESILIENT RETAIL

- Retailers with a strong online presence and strong inventory management
- Grocery sector, albeit at low margins
- Leisure apparel
- Click and collect
- German and Dutch retail markets: sales surpassed pre-pandemic levels in May 2020

CHALLENGED RETAIL

- Apparel, clothing and footwear
- Luxury due to decline in tourism
- Food & beverage
- Leisure sector
- Department stores

FIGURE 29: RETAIL SALES EVOLUTION, SELECTED MARKETS



Source: Eurostat

SHIFT TO FLEXIBLE LEASES

With cashflow severely impacted due to lockdowns and the gradual pace of recovery, and challenging market conditions ahead, retailers are asking landlords to provide them with lease and rent concessions in the short-term.

- Rent negotiations accelerated just before summer, but these discussions only concern rents until the end of 2020
- Retailers are reticent to consider long term solutions beyond 2021 because of uncertainty
- As a result, headline rents are falling in most EMEA markets

In nearly all European countries, governments have announced policy measures to support retailers, including several steps related to rent support.

GOVERNMENTAL RETAIL RENT PROTECTION IN KEY MARKETS

UK	Moratorium on evictions for commercial tenants until the end of September 2020
Netherlands	N/A
Germany	Moratorium on rent evictions between 1 April and 30 June 2020. Tenants have the option of settling arrears (plus default interest) as a result of the impact of COVID-19 until 30th of June 2022, otherwise termination is possible
France	Moratorium on evictions for commercial tenants until end of June 2020
Italy	Retailers can deduct 60% of the rent paid in March and April from taxes, but only for retailers in high streets, not shopping centre or factory outlet tenants
Spain	Moratorium on rent payments, deferments of rents accrued from 14 March 2020 to 14 July 2020 for a maximum of 2 years
Portugal	Moratorium on rent payments for commercials tenants and turnover rent until 31 December 2020 for shopping centre contracts

In the long-term, the move towards more flexible lease terms might include:

- Turnover rents
- Including online sales as part of turnover rents
- Shorter lease terms
- Different break options
- Shift from quarterly to monthly payments
- Insertion of pandemic clauses

Retailers will look at the full package of costs related to a location. This will involve:

- A change to the definition of prime and secondary retail
- Different measurement of what constitutes a successful retail destination

Landlords will require a holistic understanding of a retailer's organisation and need to focus on managing their existing portfolios

RETAIL ASSETS ON THE MOVE

In the short-term, CBRE expects:

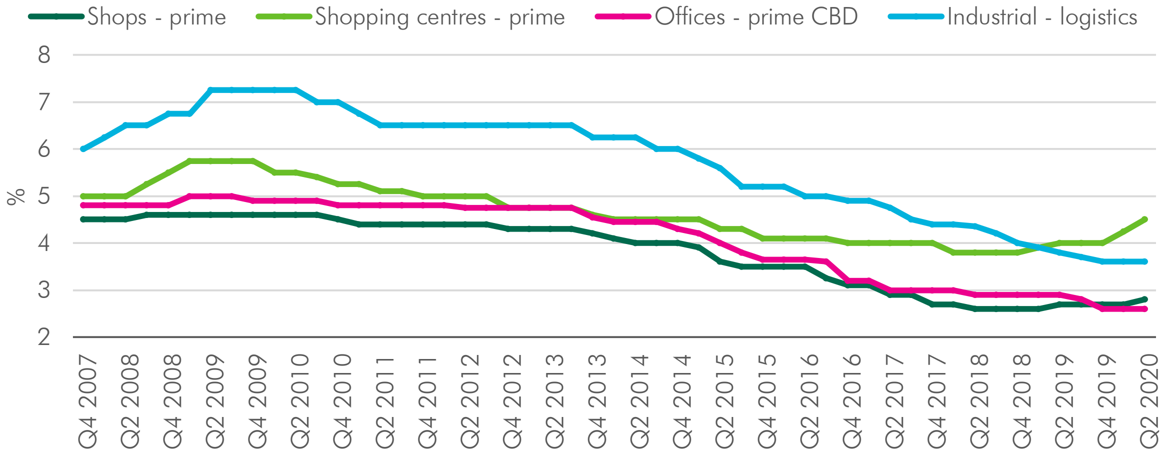
- Lease modifications, including declines in headline and net effective rents
- Higher vacancy levels
- Retail yields to continue expanding, surpassing these in other sectors
- Significantly reduced liquidity

PRESENTING…

… RARE INVESTMENT OPPORTUNITIES

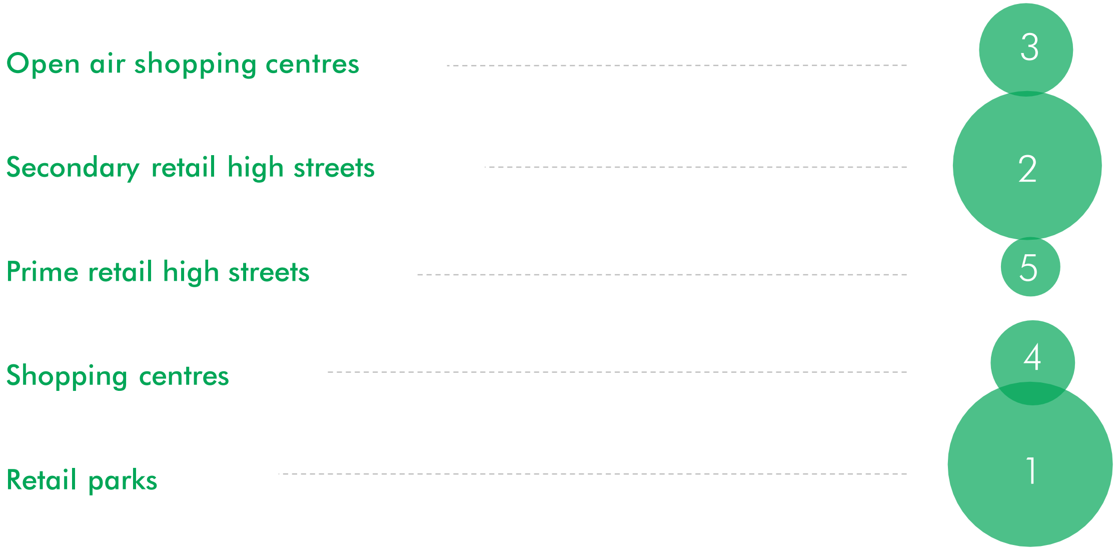
- Retail parks
- Opportunity to repurpose obsolete retail incorporating redevelopment to mixed use schemes
- Exceptional prime assets
- Stable long-term income, e.g. supermarkets with long lease terms

FIGURE 30: PRIME YIELD MOVEMENTS IN GERMANY



Source: CBRE 2020

FIGURE 31: PERFORMANCE OF RETAIL CATEGORIES IN THE COVID-19 ERA



Source: CBRE 2020. Note: performance reflects quantitative and qualitative data on footfall, conversion rates and sales.

KEY TAKEAWAYS

- The pandemic has accelerated the already existing structural trends in retail.
- Customers and retailers are adapting the way in which they organise themselves: while omnichannel is the way forward, brick-and-mortar remains an indispensable element of the equation.
- In the short-term, exceptional prime retail assets are still investment-worthy across different retail categories.
- Retail remains a versatile sector and is capable of evolving in myriad ways.

HOTELS

CBRE RESEARCH | EMEA

UNPRECEDENTED TIMES BUT DEMAND ALWAYS COMES BACK

The COVID-19 pandemic presents unusually severe challenges to the European hotels sector, reflected in current very low customer demand.

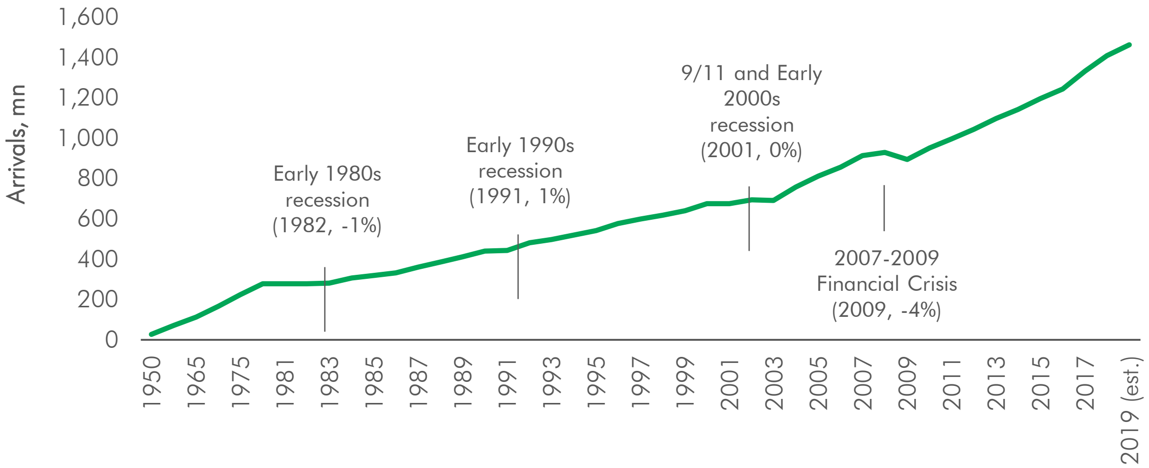
Many hotels across the EMEA region remain closed and those which are open are achieving very low occupancy relative to pre-pandemic levels.

A decline between 58% and 78% in global cross-border tourism numbers is expected for 2020. Europe, which typically captures over half of the world's annual international arrivals, has therefore been severely impacted.

However, the European tourism industry has overcome downturns in the past, with annual average growth of 5.6% in tourism arrivals since 1950. On average, it took just one year for European tourism demand to recover following periods of extended crisis.

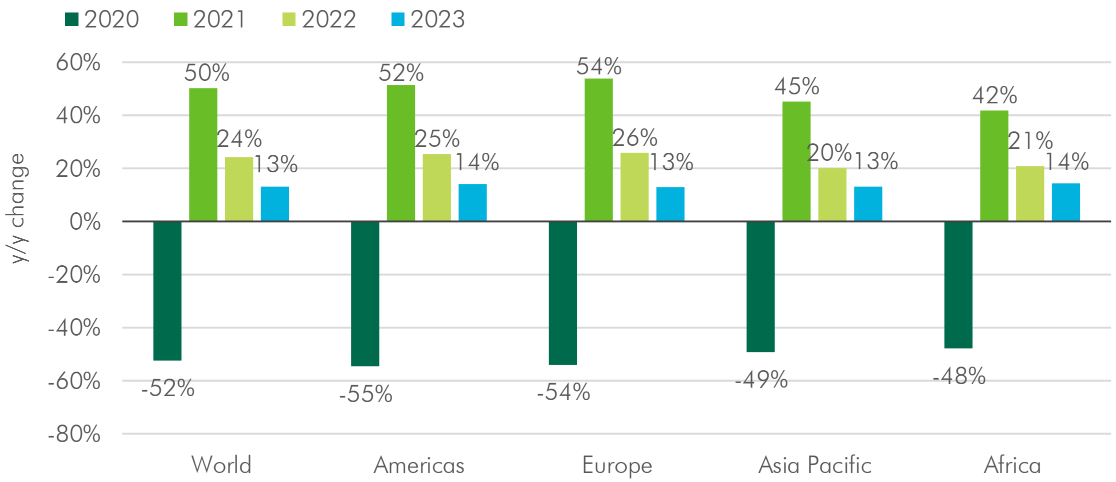
Travel numbers will recover, but the high operational gearing of hotel assets is a particular challenge for owners and operators, many of which are experiencing significant financial pressure through this period of low demand and curtailed revenue generation.

FIGURE 32: GLOBAL INTERNATIONAL TOURIST ARRIVALS, 1950-2019



Source: UNWTO, 2020

FIGURE 33: INBOUND VISITOR GROWTH FORECAST



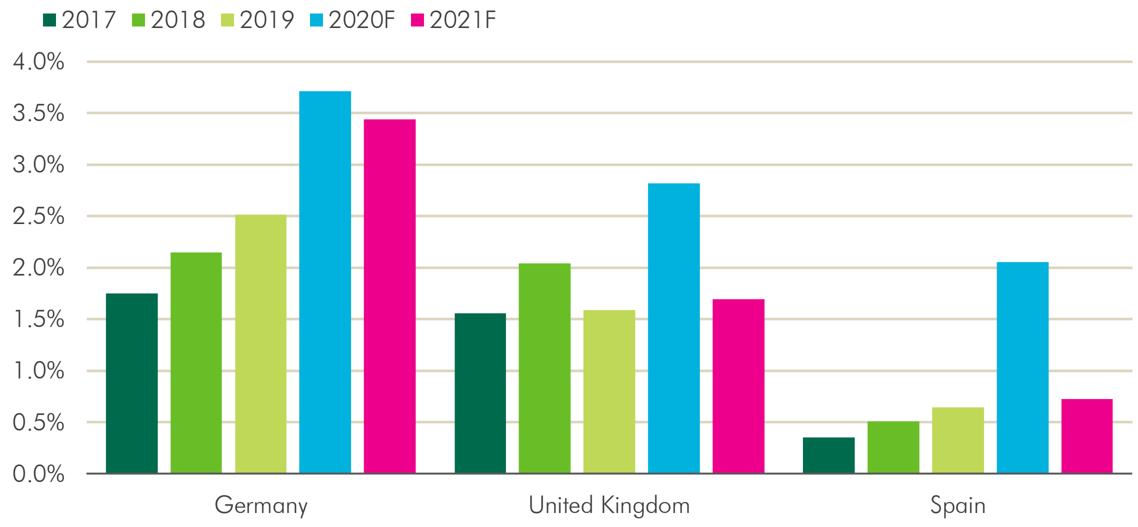
Source: Tourism Economics, 2020

NEW SUPPLY PIPELINE REMAINS SUBSTANTIAL

Buoyant hotel performance in recent years has led to high development activity in 2020. Whilst many projects will be deferred or abandoned, those which are already under construction and therefore committed to will most likely materialise, albeit with a delay in some cases.

Most of these projects are concentrated in gateway cities, which are most exposed to the longer recovery expected for corporate and international travel demand.

FIGURE 34: NET BEDROOMS SUPPLY GROWTH FORECAST



Source: CBRE, STR, 2020

STATE SUPPORT: SHIELDING THE HOTEL SECTOR

State-backed support such as loans, grants and tax breaks have so far shielded many European hoteliers from the full-force of COVID-19. Nevertheless, the abrupt slowdown in guests has forced many hotel owners and operators to close their properties temporarily.

Furlough schemes have enabled operators to reduce their staff costs, which generally account for the largest share of a hotel's operational expenses.

As the hospitality sector could be one of the last business sectors to recover, some government programmes are being extended. However, these measures will likely end before hotel revenues have fully recovered, indicating the potential for further financial liquidity challenges.

In past downturns, CBRE has observed hotels competing for limited demand by lowering rates. However, it takes considerably longer for pricing to recover relative to occupancy. That said, the cost of a closed hotel is not insignificant, and despite hoteliers reducing their operating expenses, fixed costs have weighed heavily on the bottom line.

Therefore, despite governments giving the green light for hotels to reopen, some owners and operators have decided to remain closed until a greater degree of demand returns.

A COMPETITION RESET?

Some market observers initially predicted a material and structural decline in demand for private rental accommodation, such as Airbnb, expecting that most travellers would default to traditional chain hotels and their enhanced hygiene protocols.

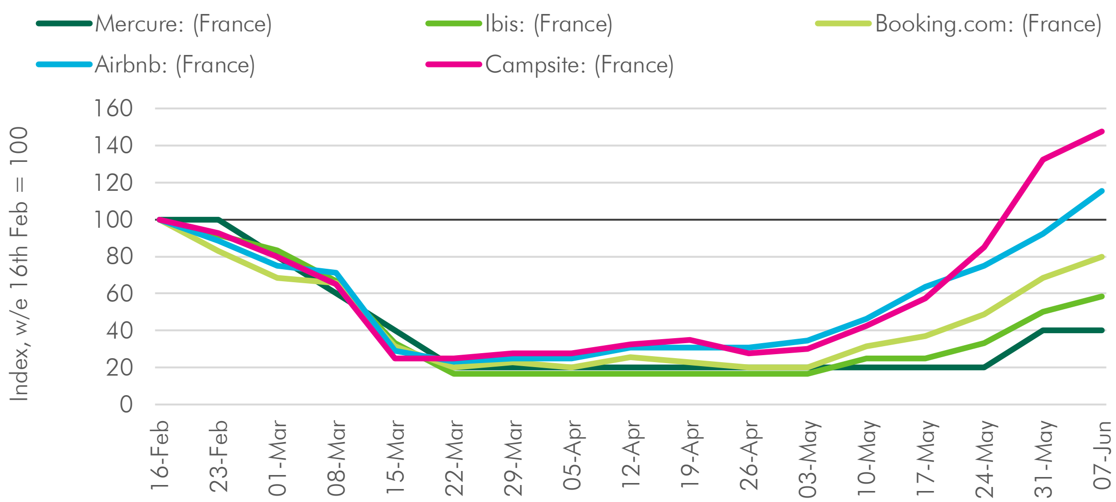
However, since the easing of lockdown measures, demand for Airbnb remains robust, while there has also been a surge in interest in other alternatives to hotel accommodation, such as campsites. This suggests that the ability to limit contact with others is currently a priority for travellers.

Serviced apartments have performed particularly well through the pandemic. Despite declining occupancy, those seeking accommodation have been willing to pay a significant premium to stay in serviced apartments over traditional hotels.

Whilst long stays commencing pre-COVID-19 may have partly supported serviced apartment ADR since the onset of the pandemic, the chart below shows that the rate premium achieved by serviced apartments in London relative to traditional hotels has increased significantly in recent months. As a result of this resilience, CBRE expects investor interest in the extended stay subsector to strengthen further in the months ahead.

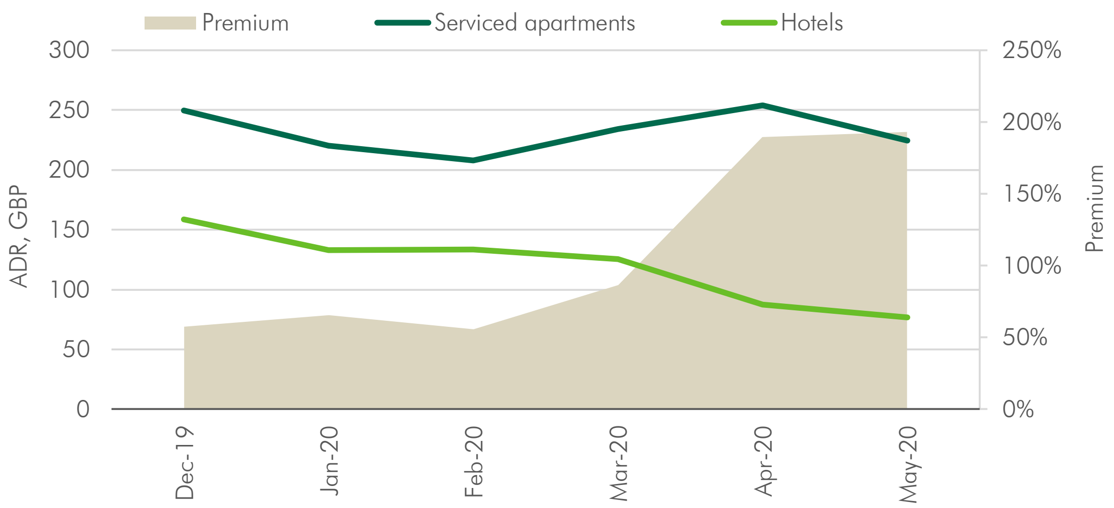
However, travellers will continue to express some apprehension about staying in transient accommodation and coming into contact with others, at least in the short-to-medium term.

FIGURE 35: GOOGLE TRENDS SEARCH POPULARITY



Source: Google Trends, 2020

FIGURE 36: MONTHLY LONDON ADR, SERVICED APARTMENTS VS HOTELS, DEC-19 TO MAY-20



Source:CBRE, HotStats, STR, 2020

DEAL ACTIVITY TO INCREASE

Some secondary hotels are likely to remain permanently closed and will eventually be repurposed. An inability to access additional credit and the cost of reopening will be further drains on the availability of working capital for owners and operators.

Investors continue to show interest in the sector, looking for large discounts and predominantly focused on core cities and leisure markets. There is currently a delta between owner and investor expectations around pricing, but as the pressure on working capital heightens and the trajectory of recovery becomes clearer, it is likely that the bid-ask gap will narrow, and deal flow will increase.

KEY TAKEAWAYS

- Demand recovery will initially be driven by domestic travellers. International travel will take longer to recover due to travel restrictions, flight availability and quarantine regulations.
- Ability to limit contact between customers and hygiene protocols will be the core of the 'new normal' standards for accommodation providers.
- There will be a competition reset between European major actors – Interest in serviced apartments is strengthening across Europe.
- The high number of pipeline projects currently under construction will extend the recovery period in some markets.
- Financial pressure on non-diversified or small owners could induce forced sales.

MULTIFAMILY

MULTIFAMILY TRANSACTION MARKET REMAINS STRONG

The onset of the pandemic failed to dent demand for multifamily assets in H1 2020. However, some investors are reticent to invest during the current economic climate, whilst those actively looking to deploy capital have been somewhat inhibited from doing so by a lack of opportunities. Transaction volume in H1 2020 was supported by acquisitions of core and core plus properties through larger deals and mergers. Among the most active players were equity driven investors with insurance and pension fund backgrounds as well as those seeking to diversify their portfolios. Investment in the European multifamily market has traditionally been driven by domestic buyers, but recent developments have indicated that cross-border activity is starting to pick up strongly.

The stable rent profile of the sector has been the main reason behind the rising volume of investor enquiries. This is the case not only for mature multifamily markets in central and northern Europe, but also for emerging multifamily markets in southern Europe. Recent months have seen rent collection rates stabilise at a level only slightly lower than before the pandemic. Due to a further increase in urbanisation and a rise in apartment prices, it is expected that young households will be increasingly opting to rent instead of buying.

Investment prices and prime yields have not changed significantly compared to the end of 2019, with the market situation potentially set to improve heading into the next few quarters.

FIGURE 37: RESIDENTIAL TRANSACTION VOLUME EUROPE

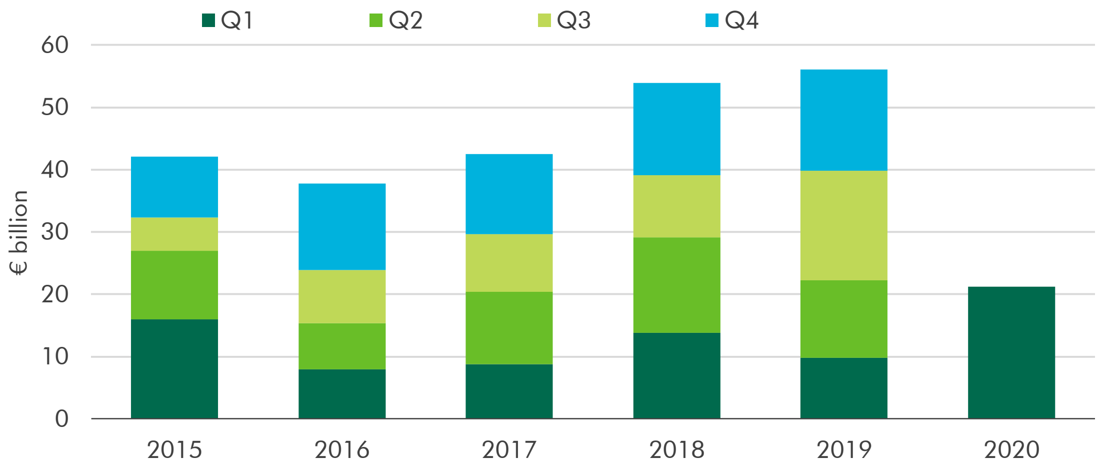
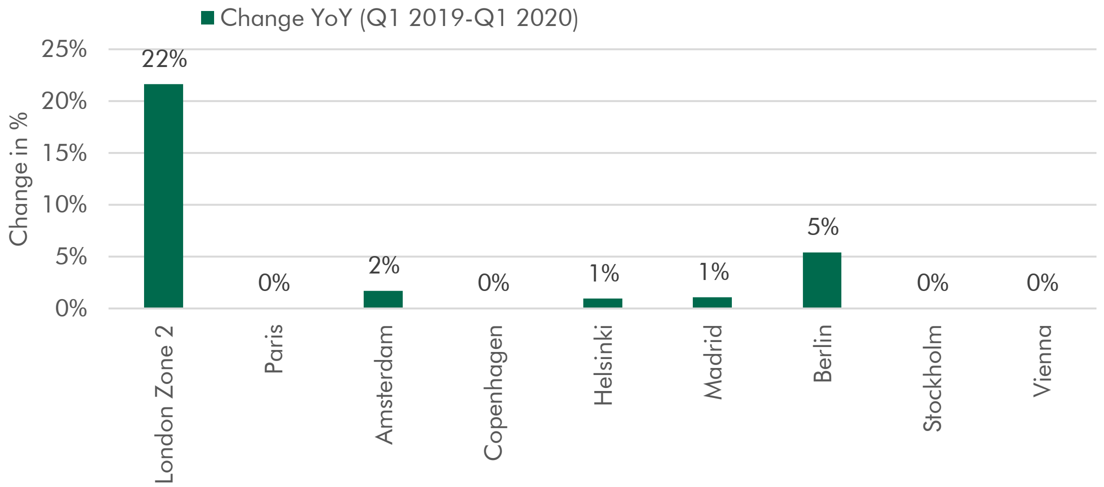


FIGURE 38: MULTIFAMILY PRIME RENTS CHANGE



Source: CBRE, 2020

EVOLUTION OF MULTIFAMILY INVESTMENT STRATEGIES

Major European private housing companies and some fund managers are currently looking for ways to increase their market shares while expanding in different or new market segments. Key strategies include:

Internationalisation: While most housing companies are still active in their domestic markets, some have purchased larger portfolios or made acquisitions of foreign competitors for the purposes of international expansion.

Market entry through project development and forward deals: Due to a scarcity of available properties, multifamily investors cannot satisfy their appetite for core income-producing properties, leaving them to seek forward deals and/or funding.

Direct purchasing and investment in developers: Some larger residential corporations have started to augment their own development capacity by acquiring or purchasing stakes in developer companies or increasing their land banking activity.

Filling-the-gap strategies and geographical diversification. Market players are looking to pursue strategic investments in multifamily portfolios outside core and capital regions with sociodemographic development potential, such as University cities or geographical locations in between major economic districts.

Institutional investors are increasingly turning towards the multifamily sector, attracted by a generally stable cashflow even in times of uncertainty.

Trends in household spending during the pandemic have demonstrated that, out of necessity, tenants generally prioritise the payment of rent. In addition, European governments have introduced a wide range of fiscal packages, including regulations and wage subsidies, to support rent payment. As a result, rent collection rates in the sector have remained quite high. Because of the defensive characteristics of the sector as shown through stable cashflows, the European multifamily sector is likely to see increased activity from global capital over the coming months.

FIGURE 39: MULTIFAMILY INVESTMENT ADVANTAGES

BETTER LONG-TERM RETURNS

STABILITY OF INCOME STREAMS

DIVERSIFICATION OPPORTUNITIES

COUNTER-CYCLICAL CHARACTERISTICS SUPPORTED BY LONG TERM SOCIO-DEMOGRAPHIC TRENDS

Source: CBRE, 2020

This report was written by CBRE's multi-national cross border EMEA research team comprised of commercial real estate professionals located across Europe. If you have any questions regarding the content of the report, the contributors listed below are ready to assist you.

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EMEA REAL ESTATE MARKET OUTLOOK 2020: MIDYEAR REVIEW

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This report was prepared by the CBRE EMEA Research Team, which forms part of CBRE Research – a network of preeminent researchers who collaborate to provide real estate market research and econometric forecasting to real estate investors and occupiers around the globe.

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