RESEARCH

EUROPEAN QUARTERLY

COMMERCIAL PROPERTY OUTLOOK

Q3 2015

OCCUPIER TRENDS | INVESTMENT TRENDS | MARKET INDICATORS

EUROPEAN OUTLOOK

European investment activity moderated slightly in Q3, but occupier markets gained momentum.

Eurozone GDP growth slowed to 0.3% in Q3 2015, which was below expectations and followed an increase of 0.4% in Q2. France returned to growth in Q3 after a stagnant second quarter, but the Italian and German economies both slowed. The European Commission forecasts that annual Eurozone GDP growth for 2015 will be 1.6%, increasing moderately to 1.8% in 2016.

The European Central Bank (ECB) appears to be preparing to extend its current programme of quantitative easing (QE), in response to the single currency area's stuttering economic growth and persistently low inflation. ECB policies may prolong the environment of low interest rates and bond yields, which have helped to enhance the attractiveness of European property investments.

During Q3, a total of €50.7 billion was invested in European commercial property. This was a 14% increase compared with the same quarter of 2014, but represented a mild slowdown from the volumes seen during the first two quarters of 2015. However, a final quarter surge in investment is anticipated, repeating the pattern of recent years. With numerous large deals expected to be completed by the year-end, Knight Frank maintains its forecast that annual European commercial property investment volumes for 2015 will reach €230 billion.

Among the larger European markets, Germany performed most strongly in Q3, with commercial investment reaching €12.0 billion, a 76% increase on the corresponding quarter of 2014. Activity in Germany was boosted by several large portfolio deals, most notably HBS Global Properties' acquisition of 41 Galeria Kaufhof department stores in a transaction valued at €2.6 billion.

There remains a large volume of capital targeting European commercial property, and prime yields continue to come under downward pressure in many markets. During Q3, prime office yields hardened in markets such as Amsterdam, Barcelona, Milan, Munich, Prague and Vienna. As a result, Knight Frank's European Weighted Average Prime Office Yield moved down by eight basis points to 4.82%, almost exactly the level that it reached at the previous market peak of Q3 2007.

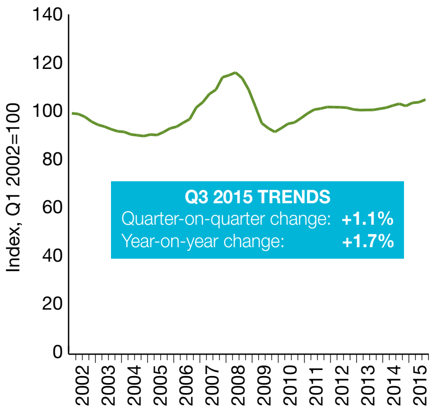
While the momentum of the investment market eased slightly in Q3, there were signs that the occupier market recovery is gaining traction. Strong leasing volumes were recorded in a number of major markets including Berlin, Madrid, Paris and Warsaw. At an aggregate level, European office take-up in the key markets monitored by Knight Frank has increased by 11% year on year, over the first three quarters of 2015.

A significant number of large-scale occupational transactions were completed across Europe in Q3, notably WPP's acquisition of the former Telefónica headquarters in Madrid. There is evidence that corporate tenants are increasingly prepared to make major occupational decisions and to take advantage of rents that are still well below their previous peaks in many markets.

Despite the increased office demand, rental growth has remained moderate across most of Europe. During Q3, prime office rents rose in Dublin, Lisbon, London (City), Madrid and Stockholm, but remained stable in other major European markets. Knight Frank's European Prime Office Rental Index rose by a modest 1.1% over the quarter.

FIGURE 1

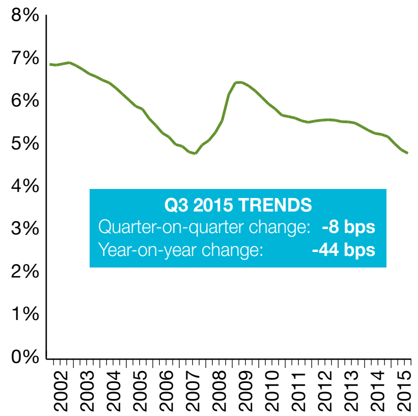
European prime office rental index



Source: Knight Frank Research

FIGURE 2

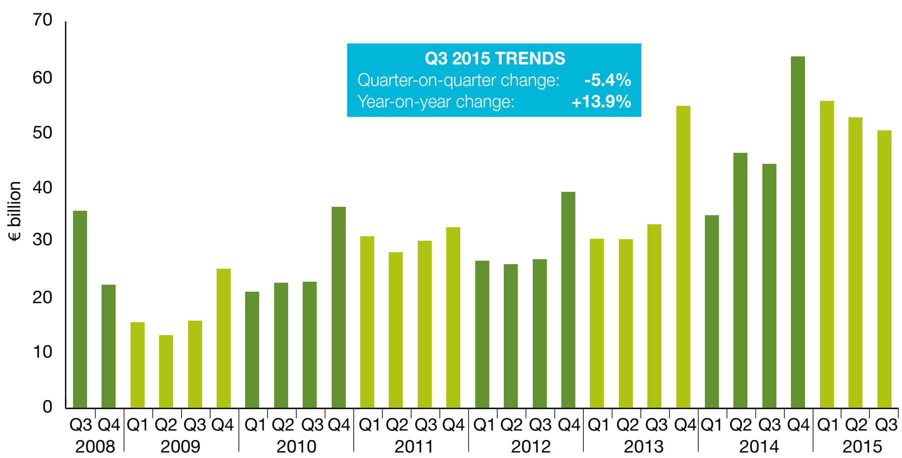
European weighted average prime office yield



Source: Knight Frank Research

FIGURE 3

European commercial property investment volumes



Source: Real Capital Analytics / Knight Frank Research

MARKET HIGHLIGHTS

1 AMSTERDAM
Booking.com, the Dutch travel website, continues to expand its presence in Amsterdam. In Q3, it signed a long lease agreement for 13,500 sq m in the Piet Hein Buildings complex.

2 BRUSSELS
In the biggest occupier deal in Q3, KPMG preleased 13,000 sq m in the PassPort office complex, which is under development at Brussels Airport. Office take-up in Q4 is expected to be boosted by the completion of several large deals involving European institutions.

3 DUBLIN
Dublin office rents continue to rise, driven by the limited availability of centrally located space. In Q3, prime office rents reached €55 per sq ft (€592 per sq m) per annum, a 22% increase year-on-year.

4 FRANKFURT
Frankfurt office take-up reached 110,300 sq m in Q3, making it the strongest quarter of the year. However, large-scale transactions have remained scarce and Deutsche Vermögensberatung's owner occupier deal for c. 32,000 sq m in Q1 remains the only transaction over 10,000 sq m this year.

5 LONDON
Underlining the continuing importance of the technology, media and telecommunications sector as a source of office demand in London, Facebook preleased more than 20,000 sq m in Great Portland Estates' Rathbone Square development in Q3.

6 MADRID
WPP has completed the purchase and subsequent sale and leaseback to M&G Real Estate of Calle de Ríos Rosas, 26. The 36,000 sq m property will be refurbished and WPP plans to occupy it in 2018.

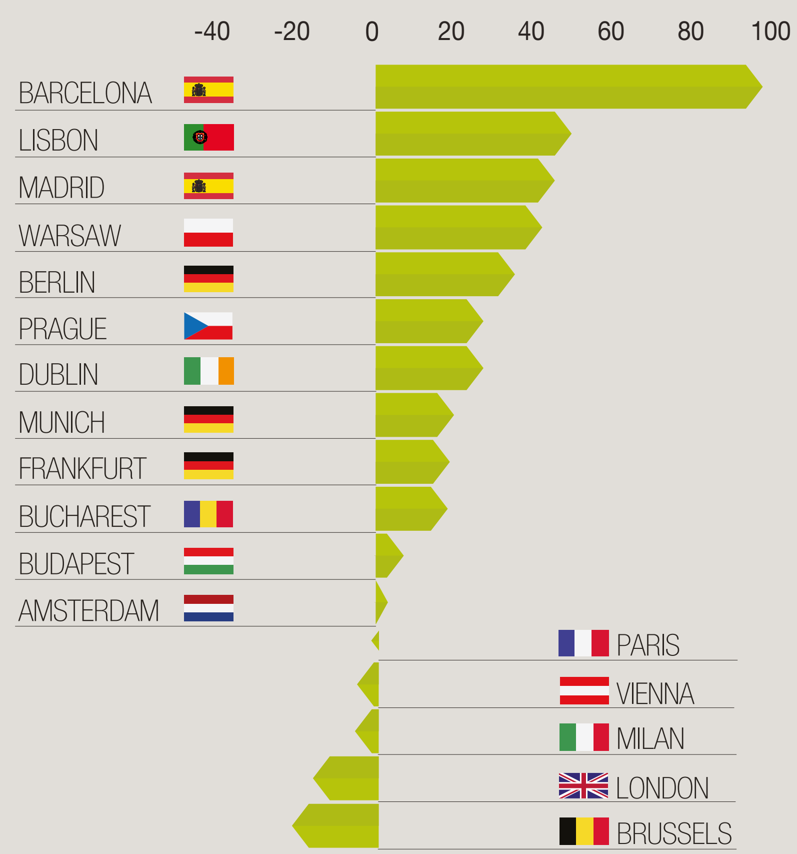
7 MILAN
Over €3 billion of commercial property was transacted in Milan during the first nine months of 2015, more than three times the level of the same period of 2014. Overseas investors have driven this increase, with buyers from China, Qatar and the USA being among the most active.

8 MOSCOW
With office demand remaining weak, average Class A asking rents in Moscow have fallen by 14% since the start of 2015. However, the rate of rental decline slowed in Q3, and rents may bottom out over the coming quarters.

9 PARIS
Following a slow first half of 2015, the Paris office market recovered in Q3, with Île de France take-up reaching 609,000 sq m. This brought total take-up for the first three quarters to 1.5 million sq m, a very similar level to the same period of 2014.

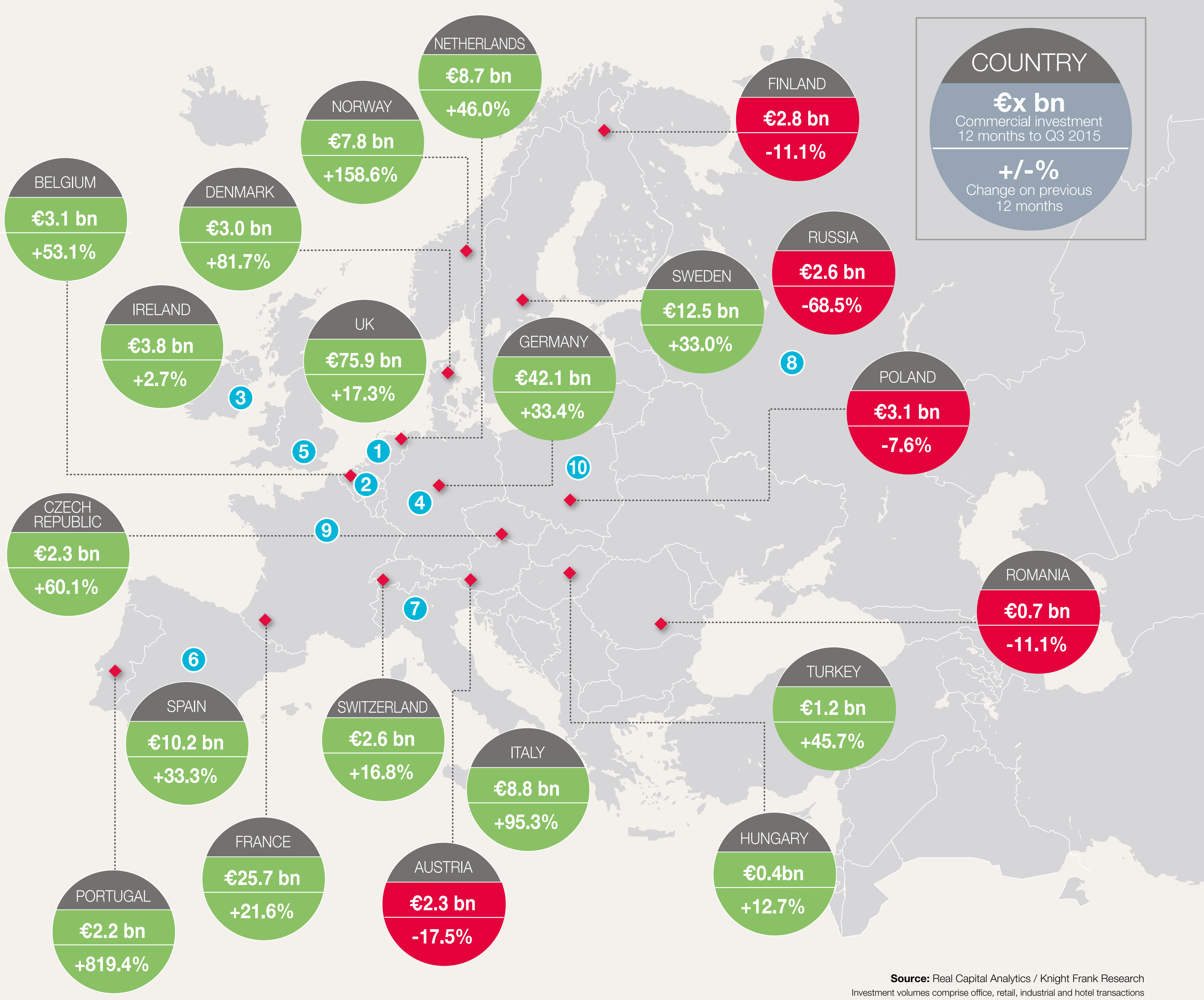
10 WARSAW
The Warsaw office market is on course to see new deliveries reach a record total of c. 340,000 sq m in 2015. However, developers have become more cautious and construction has commenced on only 60,000 sq m of new space over the first three quarters of 2015.

FIGURE 4
Office take-up, Q1-Q3 2015 vs Q1-Q3 2014, % change



Source: Knight Frank Research

FIGURE 5
European commercial property investment volumes, 12 months to Q3 2015



Source: Real Capital Analytics / Knight Frank Research
Investment volumes comprise office, retail, industrial and hotel transactions

EUROPEAN MARKET INDICATORS

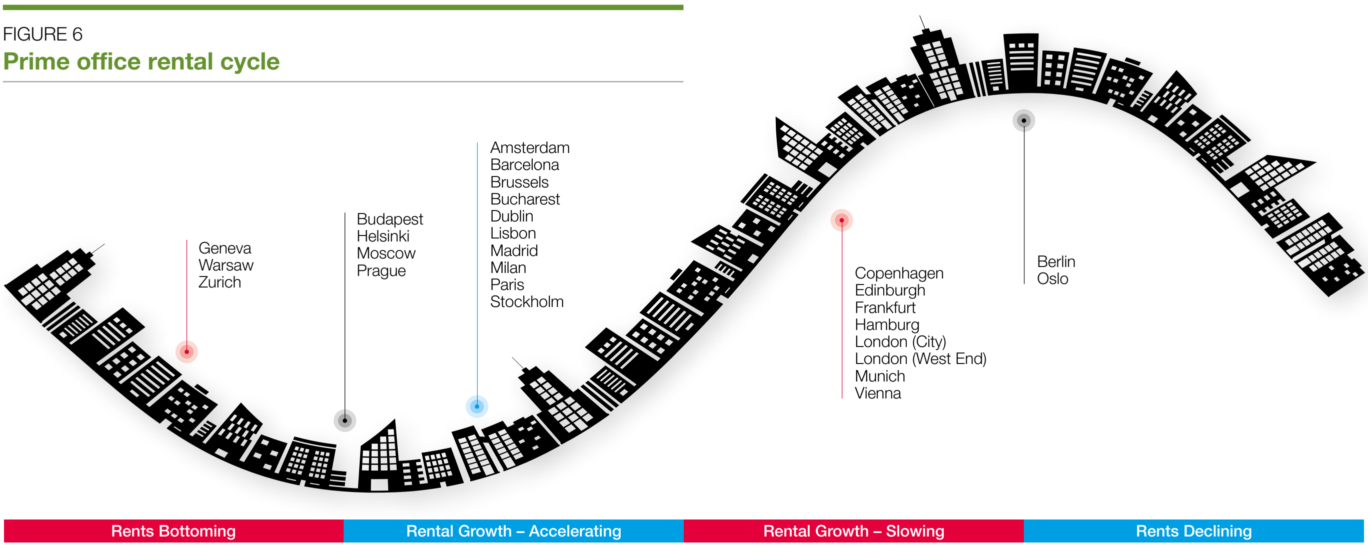
In Q3, the strongest increases in prime office rents were in Stockholm (+7.5%), Dublin (+7.3%) and Lisbon (+2.3%).

Commercial property prime rents and yields

City	Offices Prime rents (€/sq m/yr)	Offices Prime yields (%)	Logistics Prime rents (€/sq m/yr)	Logistics Prime yields (%)	Shopping centres Prime rents (€/sq m/yr)	Shopping centres Prime yields (%)	Retail warehousing Prime rents (€/sq m/yr)	Retail warehousing Prime yields (%)
Amsterdam	340 ▶	5.25 ▼	85 ▶	6.25 ▼	1,000 ▶	5.25 ▶	135 ▶	6.50 ▶
Barcelona	234 ▲	4.75 ▼	57 ▶	7.00 ▼	552 ▶	5.25 ▶	120 ▶	6.20 ▶
Berlin	282 ▲	4.25 ▼	69 ▶	6.00 ▼	1,380 ▶	4.25 ▼	150 ▶	5.75 ▼
Brussels	300 ▶	5.75 ▼	45 ▶	6.50 ▼	1,800 ▶	5.35 ▶	170 ▶	6.00 ▶
Bucharest	216 ▶	7.50 ▼	45 ▶	9.00 ▼	720 ▶	7.75 ▼	120 ▶	9.50 ▼
Budapest	240 ▶	7.25 ▶	42 ▶	9.00 ▶	1,080 ▶	7.00 ▶	90 ▶	8.00 ▶
Copenhagen	241 ▶	4.50 ▼	77 ▶	6.50 ▶	697 ▶	5.50 ▶	164 ▶	6.50 ▶
Dublin	592 ▲	4.50 ▶	75 ▲	6.25 ▼	3,000* ▲	5.75 ▼	280 ▲	6.25 ▼
Edinburgh	414 ▶	5.50 ▶	94 ▲	6.25 ▶	3,048* ▶	4.75 ▼	400 ▶	6.00 ▶
Frankfurt	459 ▶	4.40 ▼	80 ▶	5.75 ▼	1,560 ▶	4.20 ▼	169 ▶	5.75 ▼
Geneva	777 ▶	3.75 ▶	183 ▶	6.00 ▶	1,043 ▶	4.25 ▶	165 ▶	5.25 ▶
Hamburg	300 ▶	4.25 ▼	72 ▲	5.75 ▼	1,650 ▶	4.25 ▼	150 ▶	5.75 ▼
Helsinki	396 ▲	4.75 ▼	120 ▶	7.00 ▼	1,200 ▶	5.25 ▶	145 ▶	6.50 ▶
Lisbon	222 ▲	6.00 ▼	45 ▲	7.25 ▼	1,080 ▲	6.00 ▼	108 ▲	8.00 ▼
London	1,669 (WE) ▶ 965 (City) ▲	3.50 (WE) ▶ 4.00 (City) ▶	200 ▶	4.25 ▶	6,460* ▶	4.00 ▼	682 ▶	4.25 ▶
Madrid	318 ▲	4.00 ▼	57 ▶	7.00 ▼	530 ▶	5.25 ▶	120 ▶	6.20 ▶
Milan	500 ▶	4.50 ▼	50 ▶	7.25 ▼	850 ▶	5.75 ▼	300 ▶	7.00 ▼
Moscow	692 ▼	10.00 ▲	77 ▶	12.50 ▲	3,264 ▼	11.00 ▲	N/A	N/A
Munich	414 ▲	3.75 ▼	84 ▲	5.75 ▼	1,900 ▶	4.00 ▼	180 ▶	5.50 ▼
Oslo	449 ▶	4.25 ▼	128 ▶	5.75 ▶	1,254 ▶	5.25 ▶	136 ▶	6.25 ▶
Paris	750 ▶	3.50 ▼	55 ▶	6.00 ▼	2,400 ▲	4.00 ▼	180 ▶	5.25 ▼
Prague	234 ▶	5.50 ▼	46 ▶	6.75 ▼	840 ▶	5.50 ▶	120 ▶	7.75 ▶
Stockholm	528 ▲	4.00 ▼	111 ▶	6.00 ▼	836 ▶	4.75 ▼	225 ▶	6.00 ▼
Vienna	309 ▶	4.60 ▼	78 ▲	7.15 ▼	1,320 ▶	5.25 ▶	168 ▶	6.00 ▶
Warsaw	276 ▶	6.00 ▶	66 ▶	7.00 ▼	1,200 ▶	5.50 ▼	132 ▶	7.50 ▶
Zurich	732 ▶	3.25 ▼	229 ▶	5.75 ▼	1,372 ▶	4.00 ▶	183 ▶	5.00 ▶

Indicative prime yields, as quoted locally, based upon a hypothetical Grade A unit. Office rents are for prime city area Grade A space, 2,000 sq m. Shopping Centre rents are based on prime covered shopping malls, quoted on best position, 100 sq m units. Retail Warehouse rents are for units of 1-5,000 sq m located in purpose built parks. Typical Retail Warehouse schemes vary between countries. Logistics rents are for prime industrial space of units over 5,000 sq m. The data above is provided for general reference purposes only. Local market conditions will vary. *Zoned/weighted figure. Arrows provide a broad indication of recent movements and the short-term outlook for prime rents and yields. London office data is quoted for the West End (WE) and City (C) submarkets.

FIGURE 6
Prime office rental cycle



The above diagram is intended to provide a comparative guide to the current positions of European prime office markets in their rental cycles. Markets will move through their cycles at different speeds and, sometimes, in different directions. The positions indicated in the diagram do not constitute formal forecasts of future rental trends.

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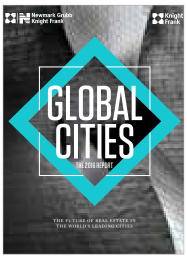

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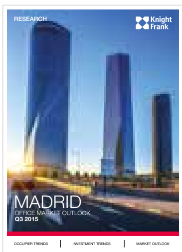

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