Investment Market Update
Europe Q3 2013
Volumes returning to 2005 levels

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- European commercial real estate investment activity reached EUR32.6bn in Q3 2013, posting a 28% increase on Q3 2012. This took total investment volumes in the first three quarters of the year to EUR89.8bn, up by 18% compared with the same period in 2012 (EUR75.9bn).

- This strong increase in volume is a direct consequence of stronger activity in the UK where volumes were close to 50% higher over the quarter at EUR13.7bn. France also saw growth over the quarter but in a smaller proportion (+8%) to EUR4.3bn. Finally, Germany continued to see strong levels of activity at EUR5.7bn, even if the Q3 volume was 4% lower on Q2. Significant increases in volume occurred in Central and Eastern Europe (CEE) as volumes reached EUR3.5bn so far this year, doubling its 2012 performance. Peripheral markets - Ireland, Italy and Spain - continue to attract strong levels of activity as volumes reached over EUR4bn this year, posting a 135% increase on the same period of 2012.

- In contrast to recent trends, the third quarter showed an increase in domestic investment. Overall domestic investment totalled over EUR21bn, representing 67% of activity. It is the highest level in over two years. Cross border investment was just a third of activity, with volumes lower than the second quarter. This was the result of both lower activity within the region, but also capital from outside which totalled just over EUR6bn

- After peaking up in Q2, the industrial sector continued to record strong levels of activity in a range of markets in lot sizes up to EUR50m. However the office sector remained the most favourite asset type with EUR19bn of acquisitions this quarter. Market activity has kept the same pace on the retail segment which accounted for EUR6.5bn in Q3 2013; thanks to big lot size assets acquisitions in the UK, Germany and Poland.

- Becoming less focused on the core segment and less risk adverse, investors are now looking outside the top three markets. In fact, many of them have already been more active in CEE and the peripheral markets, which are still attractively priced. In this context, we have upgraded our forecasts with full year 2013 volumes 15% higher at EUR136bn and a further 10% growth in 2014

Europe Q3 2013

European investment volume

Biggest 3rd quarter volume since 2008

There has been no summer break in the European investment market during the third quarter of 2013 as volumes reached EUR32.6bn a 28% increase on Q3 2012 (Figure 1). This is the biggest figure recorded for a third quarter since 2008. It also pushed volumes in the first three quarters of the year to EUR89.8bn, up 18% from EUR75.9bn recorded over the same period in 2012.

Investor sentiment has improved markedly over the course of the year reflecting gradual economic recovery in Europe and the improving outlook for 2014 and beyond, helping to push volumes higher in many European markets (Map 1).

Focus on core…but CEE and peripheral also grow

The strong increase in volume over the quarter is a direct consequence of much stronger activity in the UK. Here the volume of activity grew by nearly 50% to EUR13.7bn. France also saw growth over the quarter but in a smaller proportion (+8%) to EUR4.3bn. Germany continued to see strong levels of activity at EUR5.7bn, but this was 4% lower on Q2 (Figure 2).

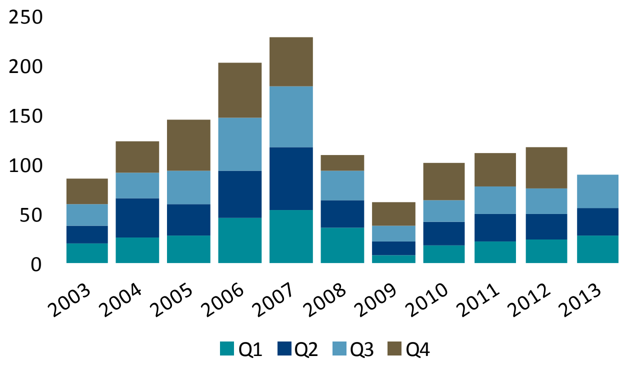
Central and Eastern Europe (CEE) has registered much stronger growth. Volumes so far this year have reached EUR3.5bn, more than double their level in the same period last year. Peripheral markets (Ireland, Italy and Spain) also continue to record strong levels of activity. Volumes in these three markets have already passed EUR4bn this year, posting a 135% increase on the same period in 2012. In CEE, some shopping centres sales in Poland have boosted the volume whist Ireland, Italy and Spain have become increasingly attractive to opportunistic investors. By contrast, Nordics saw volumes dip following recent strong levels of activity. Volumes of EUR10.6bn in the first three quarters of the year were 9% lower than the same period a year ago.

Growth in EUR100m deals drives rise in lot size

The increase in volume has been supported by a growing number of deals over EUR100m. Five deals above EUR500m were recorded in Q3 and focussed on the Germany, Russia, Sweden and the UK. As a consequence, the average lot size in Q3 increased sharply to stand EUR31m compared to EUR26m in Q2 2013 (Figure 3). It still remains below the recent high in Q4 2012.

Figure 1

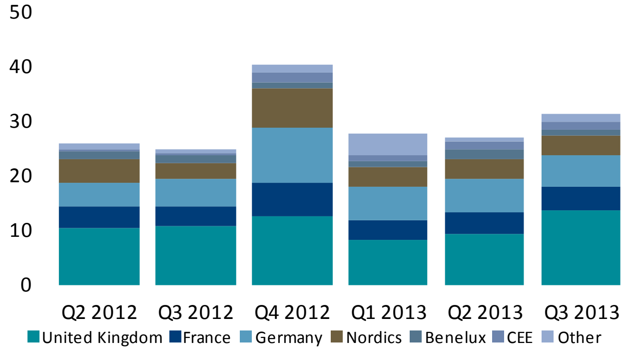
European investment activity by quarter, EUR bn



Source: DTZ Research

Figure 2

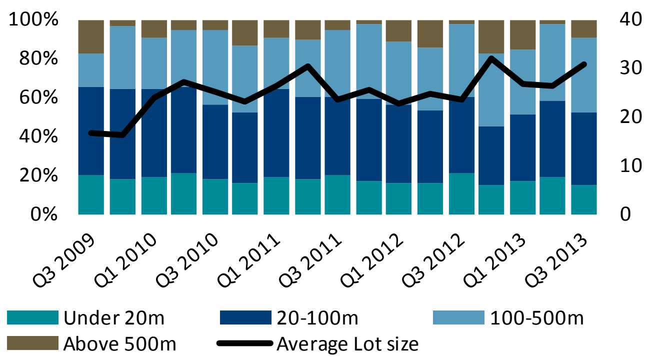
European investment activity by market, EUR bn



Source: DTZ Research

Figure 3

European investment activity by lot size and average lot size, EUR m



Source: DTZ Research

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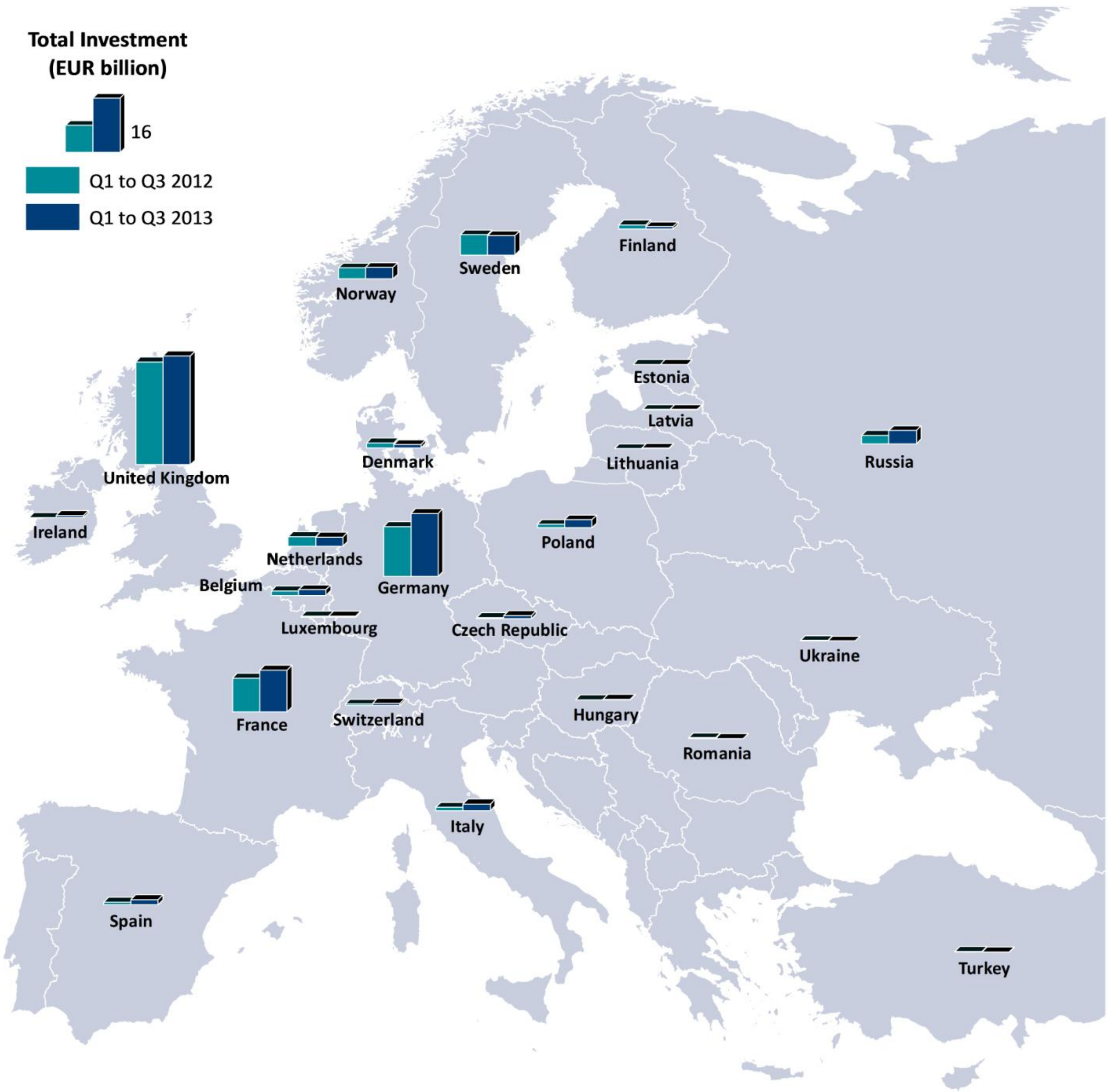
Map 1

Investment volume Q1-Q3 2013 versus Q1-Q3 2012



Source: DTZ Research; ESRI

Europe Q3 2013

Source of capital

Strong rebound of domestic investors in Q3

In contrast to recent trends, the third quarter showed an increase in domestic investment. Overall, domestic investment totalled EUR21bn, representing 67% of Q3 volumes, up from 59% in Q2. This was partly driven by much stronger domestic activity in the UK, notably in Central London.

Cross border investors were less active in the third quarter with volumes from both intra and inter-regional investors lower than in Q2. Although still grabbing the biggest share at 21%, inter-regional volumes fell 13% to EUR6.7bn in Q3. This contrasts with a 3% drop in intra-regional investment. We expect cross border activity to pick-up as recent analysis on capital available (as published in the Great Wall of Money report) suggests that Europe continues to attract the highest share of cross border investment.

Massive market share of inter-regional investors in peripheral

The analysis of cross-border activity by country in Q3 shows some interesting trends amongst the 3 core markets. In the UK the cross-border activity mainly comes from inter-regional investors with EUR3.3bn invested in Q3 2013. In contrast, they have been less active in Germany (EUR0.8bn) and France (EUR0.7bn) (See Figure 5 and Map 2).

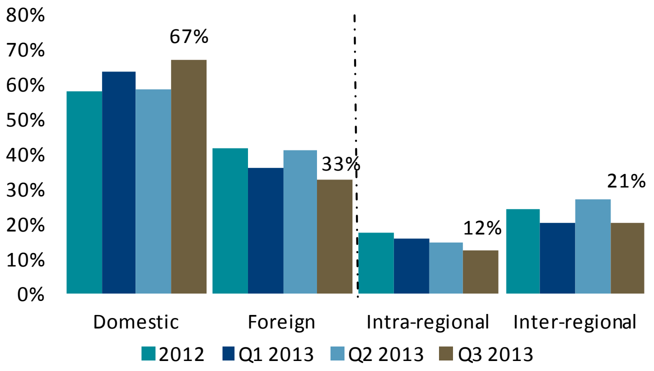
The CEE market, usually favoured by international capital flows, saw strong intra-regional flows with EUR0.75bn of investment, with the majority EUR0.5bn from ECE and ALLIANZ purchase of the Silesia City Centre shopping centre in Poland. The peripheral markets – Ireland, Italy and Spain – have attracted inter-regional investors with opportunistic profiles. Their acquisitions reached EUR0.9bn over the last quarter, mainly in the retail segment (BLACKSTONE in the acquisition of the Francia Corta Outlet Village in Italy and INTU purchasing the Parque Principado in Spain in a joint venture with a Canadian pension fund.

Domestic investors net purchasers for first time since 2002

On a net basis, domestic investors reverse their net seller position for the first time since 2002. Strong investment of over EUR21bn helped generate net investment of EUR1.3bn in Q3. Inter-regional investors continue to increase their holdings in Europe with net purchases over EUR1bn in Q3 and EUR5.0bn since the beginning of the year (Figure 6). North American were the most active purchaser over the quarter with EUR2.7bn of acquisition, mainly in the UK.

Figure 4

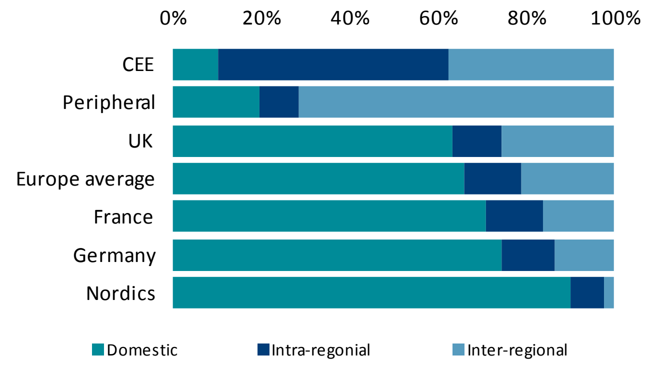
European investment activity by source of capital



Source: DTZ Research

Figure 5

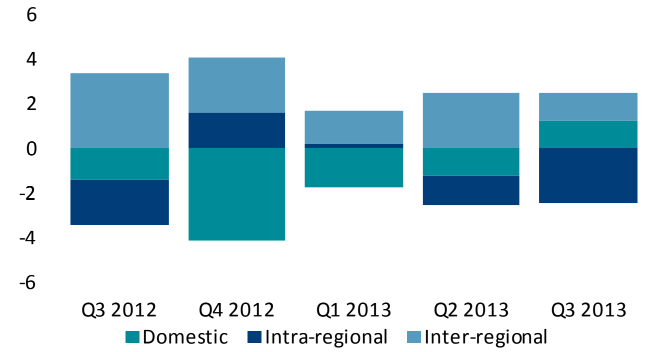
Cross-border investment by country, Q3 2013



Source: DTZ Research

Figure 6

Net investment across Europe by source of capital, EUR bn



Source: DTZ Research

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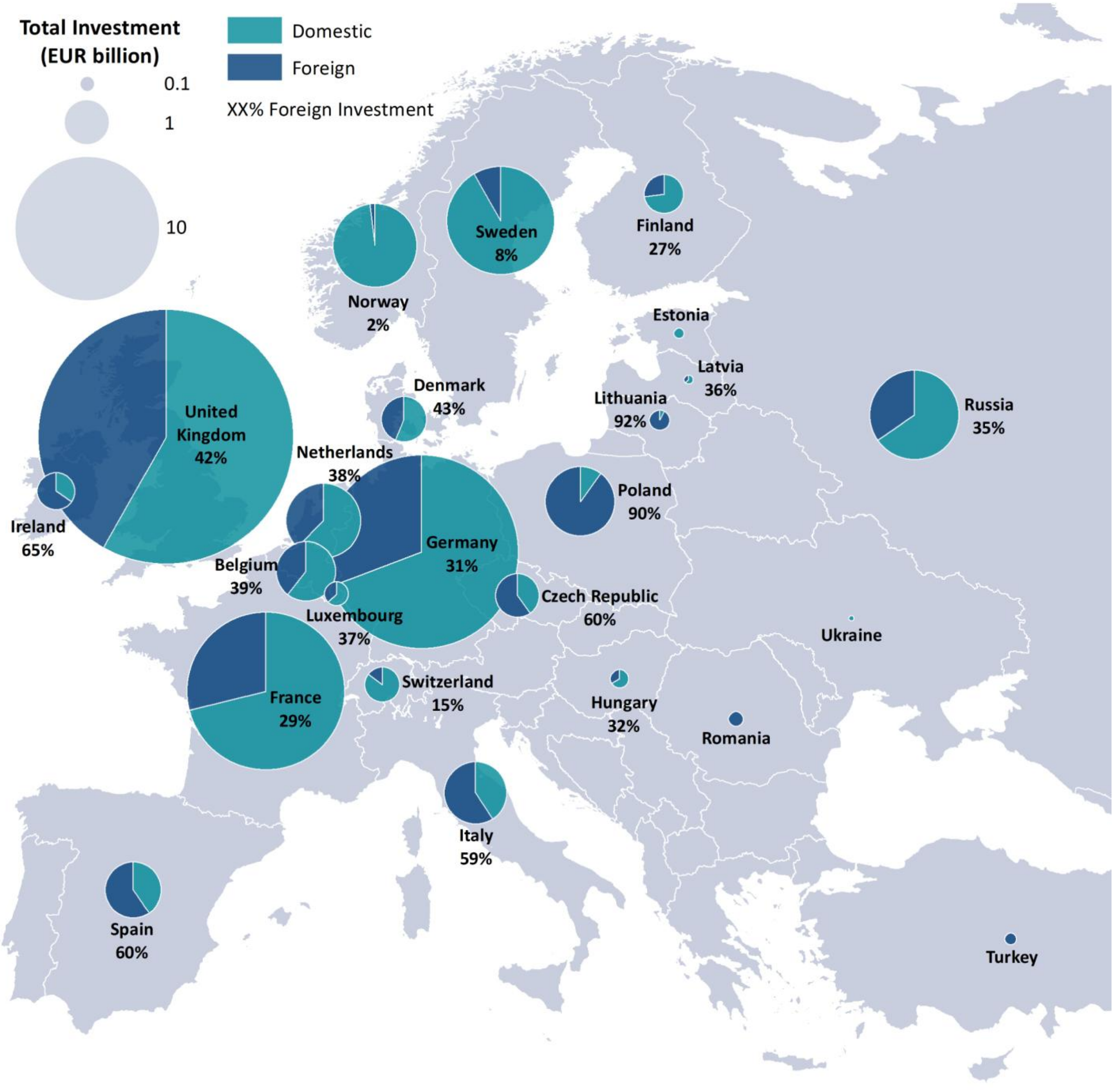
Map 2

Domestic and foreign investment, Q1-Q3 2013



Source: DTZ Research, ESRI

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Investor type

Private property vehicles still dominant in Q3

The third quarter figures confirm the continued domination of private property vehicles. Acquisitions totalled EUR14.5bn reflecting 44% of all European activity (Figure 7). They were followed by the listed sector being more active in Q3 with a total of EUR5bn invested, up from EUR2.7bn in Q2. UK REIT, BRITISH LAND acquired close to EUR0.7bn in the UK after its decision to exit from the Continent. Institutions accounted for a further 11% of the total volume, with acquisitions mainly located in the three core markets (France, Germany and the UK) as well as some activity in Sweden and Poland.

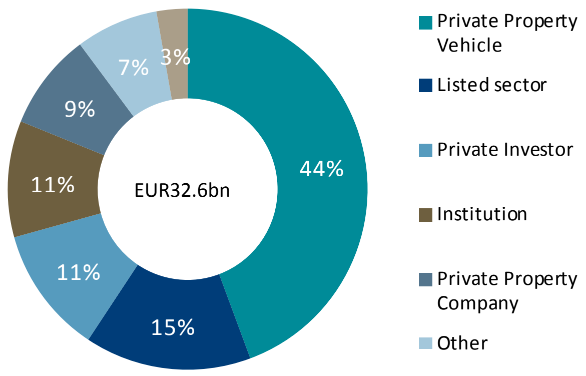
Funds come back to the top, institutions increase their exposure

On a net basis, funds have re-enforced their status as the biggest net buyer with EUR3.6bn of net investment in Q3, significantly up from EUR1.1bn recorded in Q2. They were followed by the institutions with EUR1.4bn of net investment in Q3 (up from EUR1.2bn in Q2). On the other side of the scale, the listed sector continued to deleverage and have reduced their property exposure by EUR650m in Q3 and EUR4.7bn over the last 12 months. However this trend continues to soften, suggesting that they are close to completing their rebalancing.

Private property companies were the second most active vendor this quarter with EUR6bn of sales across the region: they took advantage of the strong investors' appetite for the office sector in the UK and France, and the retail one in Germany.

Figure 7

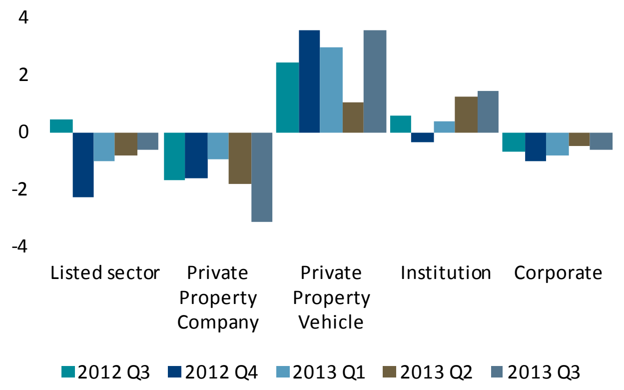
European investment activity by investor type, Q3 2013



Source: DTZ Research

Figure 8

Net investment across Europe by investor type, EUR bn



Source: DTZ Research

Europe Q3 2013

Property type

Office still on the top, industrial volumes remain strong

The industrial sector continued to benefit from strong activity in Q3 2013 with volumes totalling EUR3.3bn, similar to Q2 levels and posting a 30% increase on volume in Q3 2012. Following recent key deals involving PSP partnering with SEGRO and NORGES with PROLOGIS, the market has been active in a wide range of countries including the UK, Germany and Nordics mainly – and typically for lot sizes up to EUR50m.

However, offices remained the most popular asset type with EUR18bn of acquisitions recorded in Q3 2013, up from EUR14bn in Q2 (Figure 9). Market activity has kept the same pace on the retail segment which accounted for a further EUR6.5bn in Q3 2013. Big lot size assets acquisitions in the UK, Germany and Poland as well as in Italy and Spain have boosted quarterly volumes.

Mixed-use assets continued to gain momentum with EUR3.4bn of acquisitions in Q3 2013, up from EUR2.6bn in the previous quarter. The largest part of this volume was invested in the UK (EUR2.2bn) through some acquisitions of schemes combining office and retail spaces. These assets have attracted a wide range of investors but mainly the UK investors e.g. BRITISH LAND and GREAT PORTLAND ESTATES.

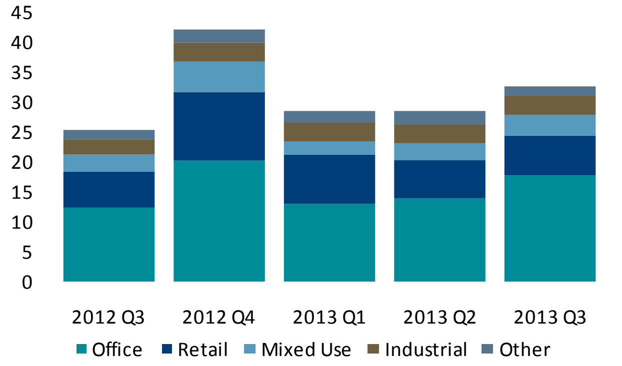
High street volumes recover in Q3

In the retail segment, shopping centre sales has roughly kept its volume of activity with EUR2.8bn or 45% of total retail sales in Q3 (Figure 10), slightly down from EUR3bn recorded in Q2. Beyond the volume, the most significant change over the quarter has been some sales of some shopping centres in the Southern Europe (Francia Corta Outlet Village in Italy sold by ABERDEEN to BLACKSTONE and Parque Principado in Spain acquired by a joint venture between INTU and CPPIB from SONAE SIERRA and CBRE GLOBAL INVESTORS. This first investment by INTU (a UK REIT) on the Continent and reflects some growing confidence from investors towards the Southern European market.

Interestingly Q3 recorded a higher volume of transactions in the high street shops segment. EUR1.4bn of investment was recorded over the quarter, significantly up from EUR0.7bn in Q2. Spain recorded a higher deal volume than the stronger core markets of UK, France and Germany thanks to a portfolio consisting in 278 SABADELL BANK branches sold for an estimated price of EUR300m.

Figure 9

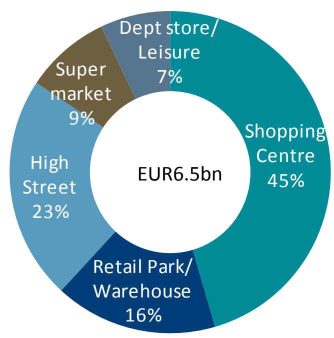
European investment activity by property type, EUR bn



Source: DTZ Research

Figure 10

European retail investment activity by type, Q3 2013



Source: DTZ Research

Europe Q3 2013

Yields trends

New yields compression in Paris and London

The strong competition between investors on the prime segment has placed pricing under downward pressure, especially in London and Paris. Prime office yield sin both these markets compressed a further 25 bps in Q3 to 4% in both markets (Figure 11). By contrast, yields in Milan have increased to 6.75% in Q3, up from 6.50% in Q2. Through this upward adjustment, investors have priced some instability on the political side. Elsewhere, prime office yields have remained roughly stable

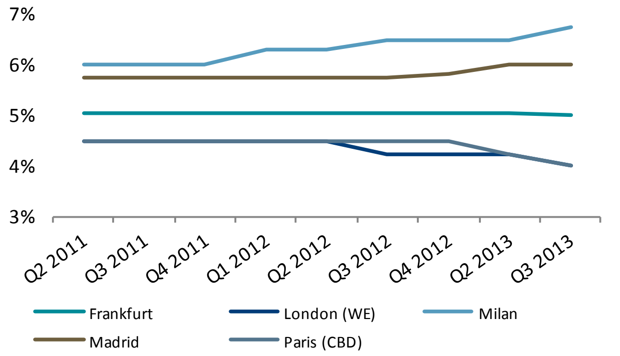
Figure 12 shows the range of yield movements across Europe over the past five years (indicated by the green line) and the current prime office yield at the end of Q3 2013 (indicated by the dark blue dot).

Eight out of the 20 markets covered in our prime office yields analysis have already come back to their pre-crisis level. These include London West-End, Paris CBD, Stockholm, Geneva and Zurich. It means also there is a limited room for further compression going forward.

In contrast, prices are expected to increase in markets where current yields are still far from their peak level. This is the case in markets such as Dublin, Bucharest, Budapest and Madrid where the gap is still over 200 bps. Witnessing a growing interest from investors, these peripheral markets should be the first to see yields compressing.

Figure 11

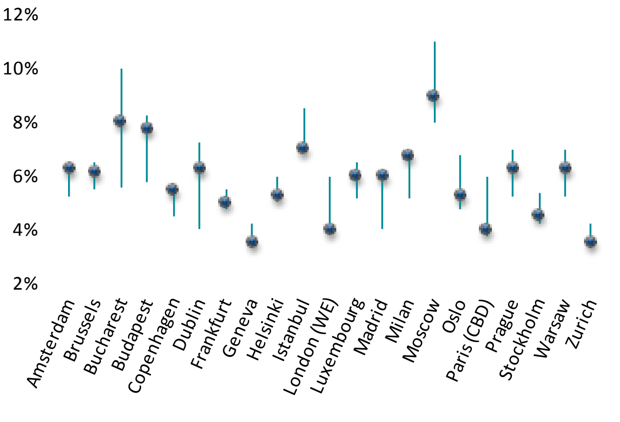
Prime office yields in Europe



Source: DTZ Research

Figure 12

Prime office yields in Q3 2013 – changes 2007-2012



Source: DTZ Research

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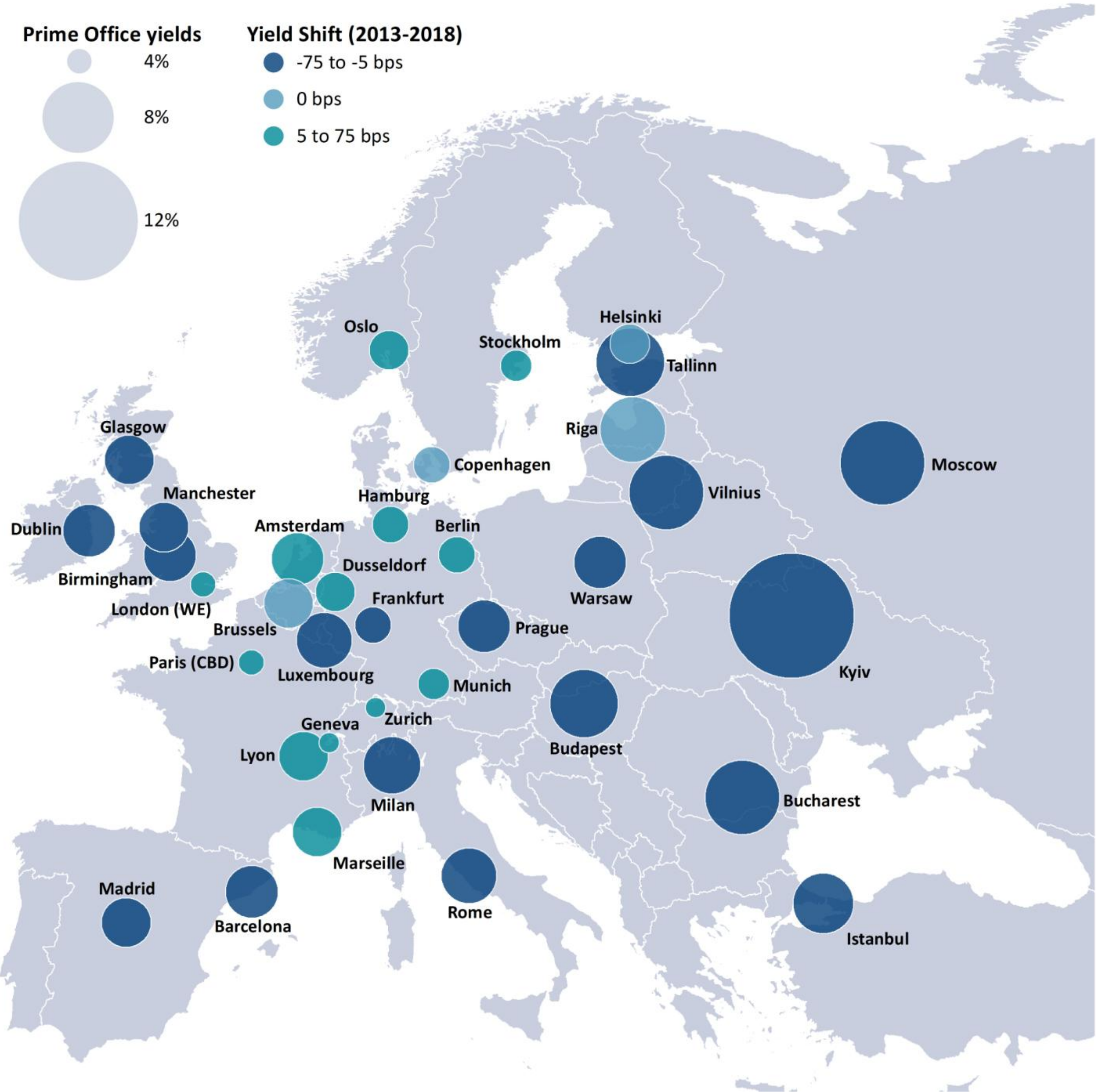
Map 3

Prime office yields, Q3 2013



Source: DTZ Research, ESRI

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Outlook

Close to 15% increase in volume for 2013 and 10% in 2014

The third quarter of 2013 has been the best since 2008 and this welcome rebound of the investment volume is in line with our capital flows analysis (as published in the Great Wall of Money report) with 6% increase for funds targeting Europe over the last 6 months. This upward trend reflects a generally improving economic outlook.

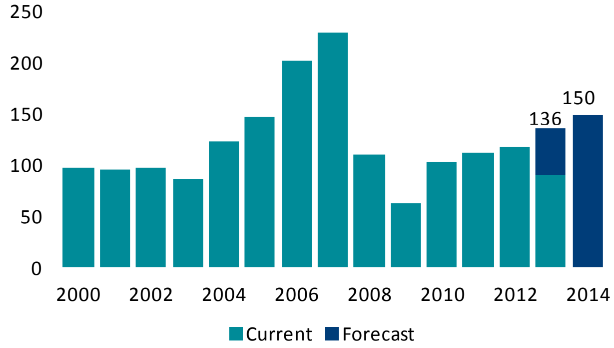
However, the investor demand for prime product is facing a lack of opportunities in some countries reflecting stronger levels of pricing. Thus, we do see increasing evidence of investors' appetite to move up the risk curve in terms of country focus and a shift towards secondary assets. We also see growing interest from new funds to focus more on non-core assets or markets.

Becoming less focused on the core segment and less risk adverse, investors are now looking outside the top three markets in Europe. In fact, many of them have already been more active in CEE and the peripheral markets, which on a comparative basis are attractively priced.

In this context, we have upgraded our forecasts with full year 2013 volumes 15% higher at EUR136bn and we anticipate a further 10% growth in 2014 (Figure 13).

Figure 13

European investment volume forecast, EUR bn



Source: DTZ Research

Europe Q3 2013

Definitions

This report presents data from the DTZ Research Investment Transactions Database (ITD). The ITD is based on commercial property investment deals reported in the press (both property and general), company and fund reports, information supplied by external data providers and by DTZ local offices around the world.

Transactions

Commercial transactions refer only to direct property. However, entity level transactions where real estate is substantial proportion of assets are treated as purchases of direct property. Development transactions are included if the purchase of commercial real estate occurs during the development / construction / comprehensive refurbishment phase and when the completion date is known. Transactions that involve more than one purchaser or vendor are classified as Joint Venture with appropriate weighting allocated to the transaction. Transactions cover European deals in excess of EUR1 million

Prime Yield

Represents the initial yield estimated to be achievable for a notional office property of highest quality and specification in the best location fully let and immediately income producing in a market at the survey date. The yield is derived from the rental income divided by the purchase price.

Property type

DTZ tracks commercial property transactions made primarily in the office, retail, industrial and mixed use sectors. Land sales are not recorded unless the land is purchased in the development phase or is acquired specifically to construct a building or complex of buildings.

Purchaser / vendor type

Classification of purchasers and vendors by type enables us to track trends in transactions and also to assess the type of capital committed to property investments. Purchaser/Vendor Type and subtype definitions are as follows:

- Institution: financial institutions/banks, pension funds and insurance companies.
- Private Property Company: companies and developers, whose principal activities involve the development, buying and selling of commercial real estate but which do not have a stock exchange listing.
- Private Property Vehicle: non-listed investment vehicles whose principal activities involve the development, buying and selling of commercial real estate.
- Private investor: private individuals.
- Quoted property company: companies and developers, whose main activities involve the development, buying and selling of commercial real estate that is listed under Real Estate on a stock exchange.
- Quoted property vehicle: listed real estate vehicles i.e. funds and tax efficient structured vehicles, whose main activities involve the development, buying and selling of commercial real estate
- Corporate: companies whose main activities do not involve development or investment in real estate

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Poland Banking Sector - January 2013
Motorways of the Sea - January 2013
The TMT Sector - October 2012
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Quantitative Easing - UK Regions - September 2013
Singapore Government Land Sales - September 2013
UK lending market -September 2013
Quantitative Easing - August 2013
Property Investment Guide Asia Pacific 2013-2014
Singapore Insight – Residential – July 2013
Net Debt Funding Gap - June 2013
China Insight - The Healthcare Sector - April 2013
City of London occupier demand - April 2013
European Sustainability Guide - April 2013

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- **Investment Transaction Database**
  Aggregated overview of investment activity in Asia Pacific and Europe.
- **Money into Property**
  DTZ's flagship research product for over 35 years providing capital markets data covering capital flows, size, structure, ownership, developments and trends, and findings of annual investor and lender intention surveys.

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