PRIMONIAL REIM

REAL ESTATE CONVICTIONS EUROPE

The fund manager's view of real estate markets in Europe

HALF-YEAR
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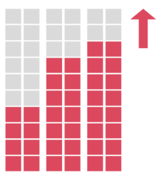
Eurozone growth forecast 2018

2.0 %

Eurozone inflation forecast 2018

1.7 %



Yield on 10-year government bonds in the eurozone 2018 forecast

€

1.1 %

Source: BCE

MSCI Europe index Total performance:

9.2 %

MSCI Real Estate

Source: MSCI

Economic environment

While global growth forecasts for 2018 and 2019 remain strong, the pace of expansion appears to have peaked in some countries. Several sources of uncertainty at the global level have weighed on the growth outlook: rising oil prices, policy rate hikes in the US, trade wars, market pressures on the currencies of countries with weak economic fundamentals and political uncertainties. These factors have added up to de-synchronise growth in the major economic areas.

In the eurozone, forecasters see robust growth of 2% in 2018. However, GDP growth is expected to dip slightly in 2020 with the gradual disappearance of some supportive factors. The inflation rate is forecast to approach 1.7% on an annual basis, much higher than over the period 2009-2016. While energy and food made significant contributions to this growth in 2017, non-volatile components are set to take their place and drive identical inflation out to 2020. A change in the inflation regime, an advanced indicator of interest rate hikes, has therefore materialised.

Even though the euphoria seen at the start of the year has waned on the economic front, real estate indicators remain firm both for users and investors. Yields are stable or have been squeezed slightly in almost all European cities. A general shift by institutional investors into more alternative products (healthcare, logistics and hotels) or those with a higher capital gains component is starting to be felt, a sign that risk-adjusted returns are more than ever a key subject at the European level.

Sources of figures: IMF, ECB, OECD

OFFICES

At 30 June, 2018, the volume of investment in corporate real estate in Europe was € 267bn on an annualised basis (+9% year-on-year). Germany, France and the UK are the three deepest markets in Europe. With more than € 100bn of commitments on average in recent years, investment volumes have been concentrated in the offices segment.

Prime yields are historically low, especially in Berlin, Paris and Munich, at 3.00% or lower. While yields in all large European cities narrowed by 10-80bp in the second quarter of 2018, Central London stabilised at 3.50%.

> Investment volumes are concentrated in offices.

In the European offices segment, new leases have been on an upward trend since 2014. Take-up has been dynamic, with just under 5 million sqm leased in the first half of 2018 in Europe. This fine performance was fuelled by the three largest markets (Paris, London and the four main German cities).

The vacancy rate of the 15 main European markets reached at 6.9% in the first six months of 2018, down 120bp year-on-year. The lowest vacancy rates are in Berlin, Munich, Hamburg, Luxembourg, Central London and Central Paris. In a large majority of European cities, rents are rising or stable. One exception is London, whose prime rent has fallen by 10%. The highest asset values in Europe are seen in the markets of London, Paris and Luxembourg.

Sources of figures: BNP PRE, CBRE

RETAIL

With a stable volume of € 58bn on an annualised basis, the retail investment market is the second biggest investment segment after offices. At the start of this year, the Spanish market was dynamic, with several sales of over € 100m, including the sale to DekaBank of a portfolio of 16 high street retail premises by Inditex. The Spanish fashion group expects the penetration rate of online sales to increase sharply by 2021 on the Iberian Peninsula, hence its strategy to divest non-strategic outlets.

Vacancy rates in the retail sector are polarising. Large city centers have low vacancy rates, whereas shopping centers have recorded a steady increase in their vacancy rates over the past two years (in particular those covering less than 15,000 m2). As a result, the yields of the most attractive retail premises remain under pressure in Europe. In Germany, the prime yield on high-street shops has fallen below the symbolic threshold of 3%, and Italy is nearing this level (3.15%).

> The market is polarising, as is demand.

Only London has experienced a slight decompression recently, but it continues to post the lowest yield (2.00%).

Consumption is forecast to be strong in the eurozone over the next two years, and this should be reflected in retailers' revenues. The battle will be over capturing these additional sales. Retail banners that have opted for an omnichannel strategy (use of the best physical and digital retail practices) appear well placed to adapt to ongoing changes.

Sources of figures: BNP PRE, CBRE, PMA

RESIDENTIAL

The European market of "block" residential investment (generally operated by institutional investors) totalled a volume of € 43bn in 2017. In the eurozone, the most active markets were Germany, the Netherlands, France and Spain. With € 17bn of investment in 2017 (vs. € 13.7bn in 2016), Germany is attracting investors to a country where almost one in two people are tenants. The biggest transaction to date has been made by Vesteda, which bought a real estate portfolio of 6,777 units in the Netherlands from NN Group for around € 1.5bn.

> Investors are staging a marked return into the residential

Residential yields benefited from a positive risk premium relative to ten-year sovereign bonds in 2017, particularly in northern countries, which appears to be a normalisation after the negative levels seen a few years ago.

French, German, Austrian, Belgian and Dutch cities enjoyed strong growth in rent-to-prices ratios over the period 2009-2017. In contrast, other cities are still in catch-up mode (Italian, Spanish, Irish and Portuguese cities). Athens has paid a heavy price for the country's crisis. In a still highly attractive interest-rate environment, Ireland (+12.3% q/q-1), Portugal (+12.2%), the Netherlands (+9.3%), Austria (+5.3%), Germany (+5.3%), France (+3.4%) and Belgium (+2.5%) recorded very solid growth in their national residential price indices in the first quarter of 2018. In contrast, Finland is experiencing a pause and Italy recorded another small decline.

Sources of figures : JLL, national statistics, RCA, Primonial REIM

HEALTHCARE

The volume of investment in healthcare real estate reached at € 4.5bn in 2017. The market is forecast to grow in 2018, with volumes concentrated in Germany and France. The principal transaction was made by Primonial REIM with the acquisition of 50% of a portfolio of 71 clinics in Germany valued at € 1.6bn. Under pressure in recent years, yields are expected to fall further in 2018.

> Germany and France are sought after.

The deepest markets are France and Germany, where investors are pursuing sale & leaseback or portfolio acquisition strategies. Markets are less mature and more fragmented in southern and eastern Europe. The sector's gradual consolidation should therefore continue.

The European elderly care sector has similar characteristics in each country. The market remains characterised by the predominance of public authorities and associations. The private sector remains deeply fragmented. Although it still consists of many independent operators, groups of European scale have been created, such as Korian, Orpea or DomusVi.

The number of beds in nursing homes stands at around 3 million in the eurozone. The five countries with the most important number of beds are Germany, Belgium, Spain, France and Italy. Industry specialists estimate that there will be a shortage around 450,000 beds by 2025/2030 in these five countries and that existing beds will need modernising. These significant needs, in a context of budgetary constraints for public sector players, suggest that the private sector will play a growing rule in creating beds in the years ahead.

Source of figures: Primonial REIM

PRIMONIAL REIM

Primonial Real Estate Investment Management (PREIM) is a portfolio management company approved by the French financial markets authority (AMF) on 16 December, 2011.
It received AIFM accreditation on 10 June, 2014. Its business consists in creating, structuring and managing long-term real estate investments by individual and institutional investors.

Primonial REIM has a comprehensive range of expertise:
> multi-products: SCPI, OPCI, SCI;
> multi-sectors: offices, retail, residential, healthcare and education property;
> multi-national: France, Germany, Spain, Italy, Belgium and Ireland.

At 30 June, 2018, Primonial REIM had:
> € 15.2bn of assets under management;
> 55,138 associates;
> 41 independent real estate advisors;
> a portfolio of 3,552,329 m2 and 7,000 tenants, including a high share of large corporate tenants (Samsung, Korian, Crédit Agricole, SNCF, etc.).

www.primonialreim.com

DEFINITIONS

10-year government bonds: debt securities issued by a state for a period of ten years, generally acknowledged to be a risk-free investment.

Investment volume in corporate real estate: total volume of premises acquired in the offices, retail, business premises and warehouses segments by an investor.

Take-up of offices: all leases or sales to the occupant (as opposed to sales to investors) for premises to be used as offices. It is expressed as square meters of usable space.

Sale Before Completion: sale before completion is the contractual method for selling a building before it is built. The investor becomes the owner as it is built.

Free leases: favourable measures granted to tenants (rent cuts, renovation work, etc.).

Yield: ratio between the gross or net revenues from the building and the capital committed by the buyer (acquisition price + fees and transfer taxes).

Store premises: traditional ground-floor retail premises located in town-center high streets.

Shopping center: a building containing at least 20 retail outlets housed in indoor centers around a large food store that drives customer traffic.

Retail park: an outdoor shopping center built and managed as a single unit. It comprises at least five buildings linked by lanes and located on city peripheries.

Care homes: a health facility that houses dependent elderly people.

Medical, surgery and obstetric clinics: medical facilities for short-term care, with or without lodging, or for severe conditions during their acute phase.

PRIMONIAL REAL ESTATE INVESTMENT MANAGEMENT

A Limited Liability Company with a Board of Directors and Supervisory Board and share capital of € 825,100. Registered under the number 531 231 124 RCS Paris. Approved by the AMF as a portfolio management company on 16 December, 2011 under the number GP 11 000043. AIFM approval dated 10 June, 2014. Professional licences «Transactions in properties and businesses" No. T15813 and "Real estate management" no. G6386 delivered by the Paris Prefecture of Police and guaranteed by CNA Insurance Company Ltd, located at 37 rue de Liège - 75008 Paris.

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