European Real SnapShot!

Current developments in the key real estate markets in Europe

Special focus: Digitisation

Autumn 2016

Content

Brexit impacts on the European Transaction Market

Investment in the European real estate market dropped significantly in Q2 2016 compared to the same quarter last year, falling by 26% to EUR55.bn. EUR107.5bn was invested in H1 2016, down by 30% compared to the same period in 2015.

The uncertainty triggered by Britain's vote leave the European Union has reduced investors' appetite for risk. With supply of safe investments extremely limited, this has led to increased competition and further falls in yields in the Core sector, and a drop in the volume of transactions.

The uncertainties associated with the implementation of the Brexit decision have had a particular impact on trends in the United Kingdom, the largest European real estate investment market. At -53%, this was the greatest fall in investment recorded in Q2 2016. London was hit particularly hard, with a fall of 75% compared to the same quarter in 2015.

Significantly less was invested in Germany too, Europe's second largest market. This market attracted 42% less investment than in the same period in 2015.

With Germany and the UK making up over 40% of the European market, the fall in transaction volume in these two countries has led to a reduction in investment activity in the overall European market. However, there were positive trends in seven of the ten largest markets: amongst others, Sweden (+68%), Spain (+51%) and Italy (+76%) experienced notable growth compared to Q2 2015. Spain and Italy in particular appear to be slowly recovering from their longstanding decline. Finland, in tenth place, was the only other top 10 market to record a fall in transaction activity (-6%).

Despite substantial falls in investment volumes in the UK, to date there has been limited negative impact on direct real estate investment prices. To date, Brexit has put pressure mainly on indirect real estate investments. It is not yet clear whether values of direct real estate investments will be hit next, especially as long term economic prospects are perceived to be positive.

Stefan Pfister
CEO KPMG Switzerland
Head of Real Estate Europe / EMA

“Investment in real estate remains very attractive in the current low interest rate environment.”

We anticipate that the uncertainties created by the Brexit vote will accentuate the dichotomy in the UK real estate investment market. Prime assets in key locations with long leases in place will be impacted least because of the strong demand from global investors for investments which can hold their value. It is assumed that non-European investors, particularly from Asia and the Middle East, will be the most active in the London property market. European investors will be more cautious – because of the currency risk and solid fundamental data in their home markets they will once more turn their attention to their domestic markets. This trend has already been seen in some markets such as France, where the largest transactions in the office market in the first half of the year almost exclusively involved domestic buyers. Opportunistic investors meanwhile may be prepared to seize investment opportunities in the event of corrections in values in the United Kingdom market.

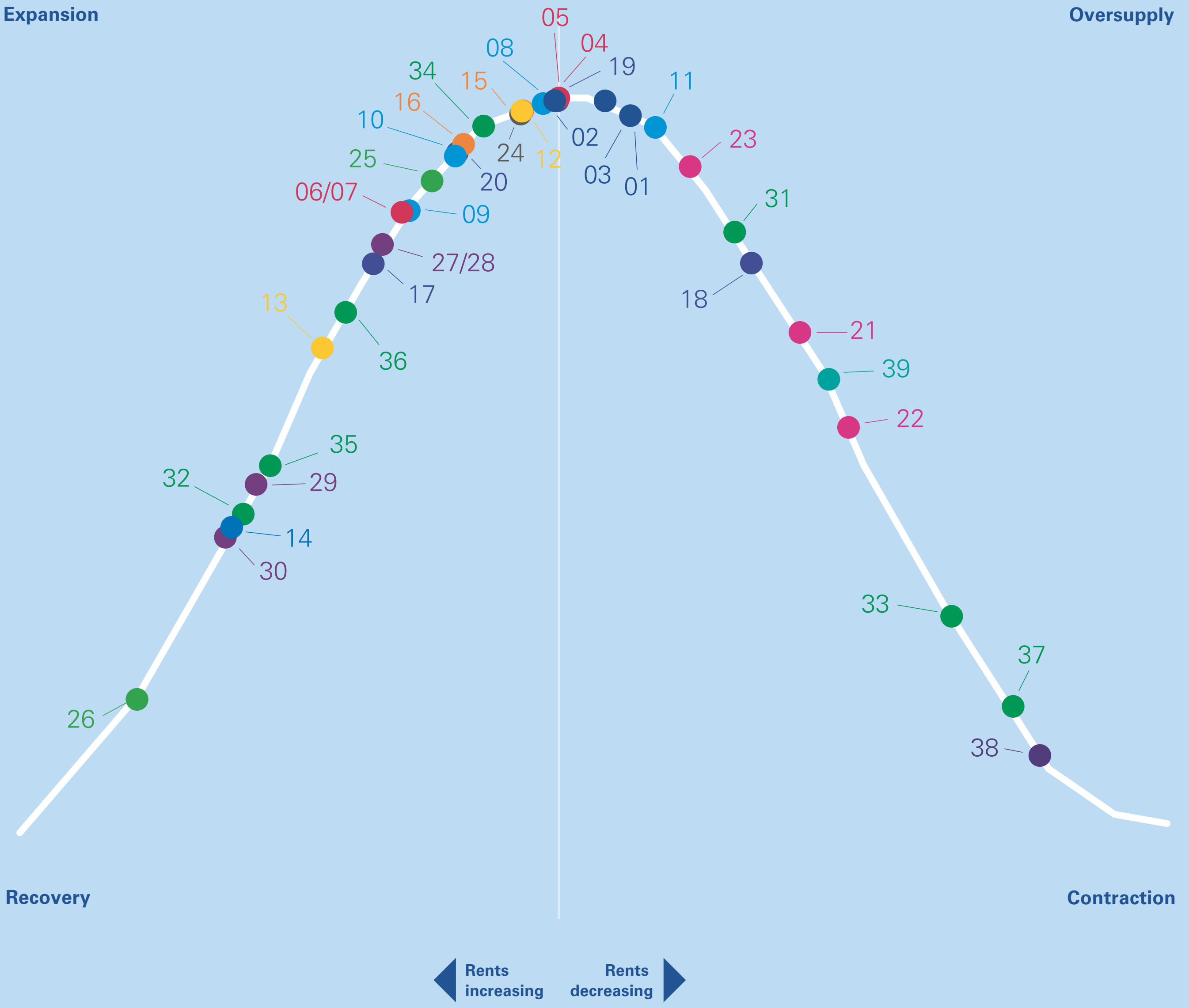
Although there has been a marked drop in investment activity in Europe compared to 2015, an optimistic view of the future can be taken. 2015 was characterised by unusually high transaction volumes. Even without Brexit, achieving a similarly high volume of transactions – the highest since 2007 – would not have been an easy undertaking in view of the lack of suitable assets available.

The basis for European real estate investments remains stable. However, Europe is facing numerous (mostly political) risks. Brexit may not necessarily be an isolated event. In the EU, important political decisions are being taken over the current year and next year: an Italian constitutional referendum in November, elections in Spain likely at the end of 2016, and the French presidential and German federal parliament elections in 2017. Political outcomes with negative impacts on the economy could lead to a downward adjustment of economic forecasts, which have the potential to put the brakes on the real estate investment market.

The current market environment is very different from that in the crisis years of 2008 and 2009. The market is adequately supplied with debt and equity capital. There is no credit crisis in sight. Moreover, most market players are holding real estate investments as long term assets, reducing speculative risk. Despite economic and political uncertainties, investment in real estate remains very attractive in the current low interest rate environment.

Stefan Pfister
CEO KPMG Switzerland, Head of Real Estate Europe/EMA

Market Cycle Office



Source: KPMG Qualitative Market Assessment

Germany
01 Berlin CBD
02 Munich CBD
03 Frankfurt CBD

UK
04 London City
05 London West End
06 Manchester
07 Edinburgh

Nordic Region
08 Stockholm
09 Copenhagen
10 Oslo
11 Helsinki

The Netherlands
12 Amsterdam South Axis
13 Rotterdam, The Hague and Utrecht

Belgium
14 Brussels CBD

Luxembourg
15 Luxembourg's CBD
16 Kirchberg

France
17 Paris CBD
18 Paris La Défense
19 Lyon
20 Marseille

Switzerland
21 Zurich CBD
22 Geneva CBD
23 Basel CBD

Austria
24 Vienna

Italy
25 Milan
26 Rome

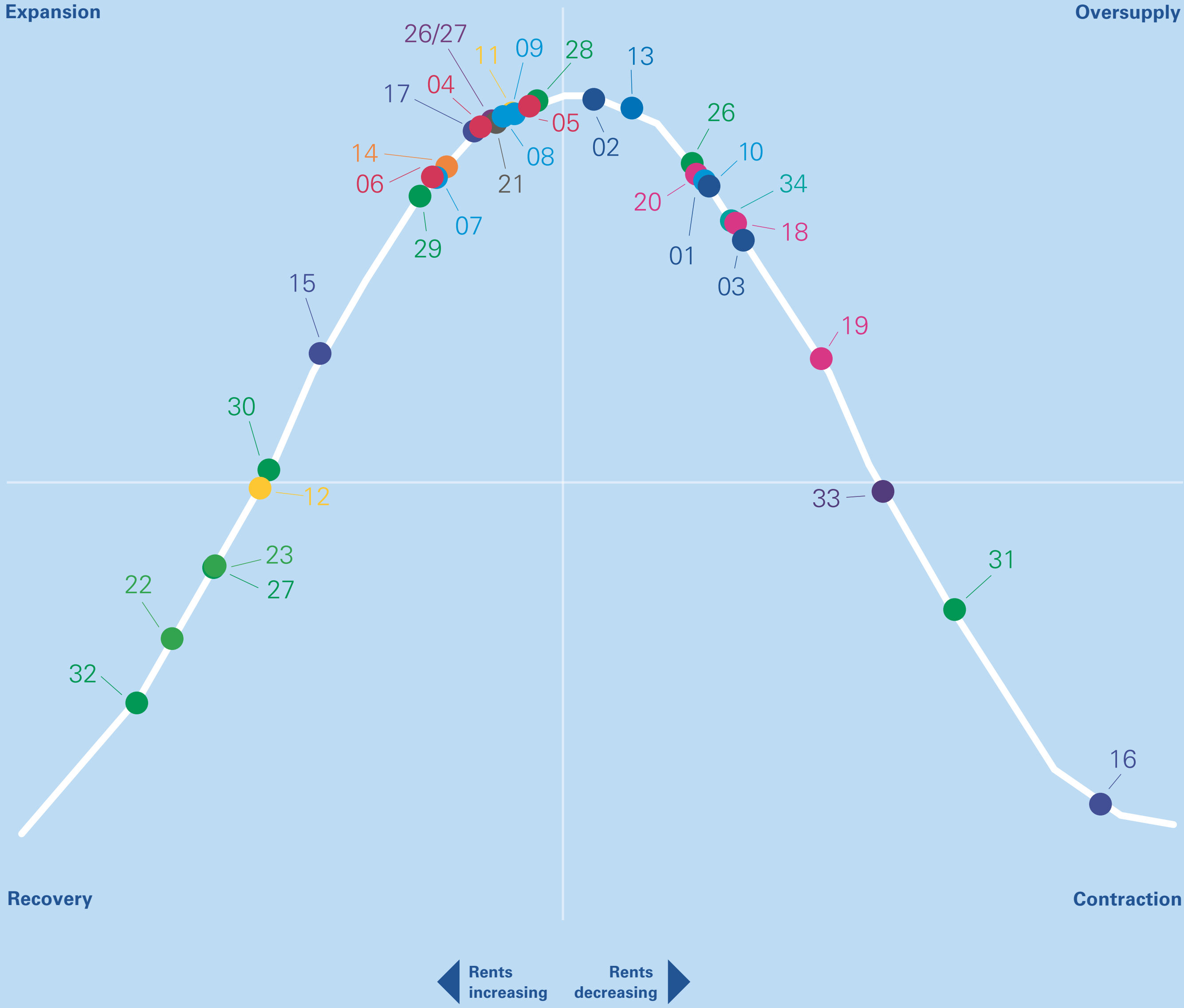
Spain
27 Madrid CBD
28 Barcelona CBD
29 Madrid Decentralised
30 Barcelona Decentralised

CEE
31 Prague
32 Budapest
33 Warsaw
34 Bucharest
35 Belgrade
36 Bratislava
37 Zagreb

Russia
38 Moscow CBD

Turkey
39 Istanbul

Market Cycle Retail High Street



Source: KPMG Qualitative Market Assessment

Germany
01 Berlin
02 Munich
03 Frankfurt

UK
04 London City
05 London West End
06 Edinburgh

Nordic Region
07 Stockholm
08 Copenhagen
09 Oslo
10 Helsinki

The Netherlands
11 Amsterdam
12 Rotterdam, The Hague and Utrecht

Belgium
13 Brussel

Luxembourg
14 Grand-Rue/Rue Philippe II

France
15 Paris
16 Lyon
17 Marseille

Switzerland
18 Zurich
19 Geneva
20 Basel

Austria
21 Vienna

Italy
22 Rome
23 Milan

Spain
24 Madrid
25 Barcelona

CEE
26 Prague
27 Budapest
28 Warsaw
29 Bucharest
30 Belgrade
31 Bratislava
32 Zagreb

Russia
33 Moscow

Turkey
34 Istanbul

Germany

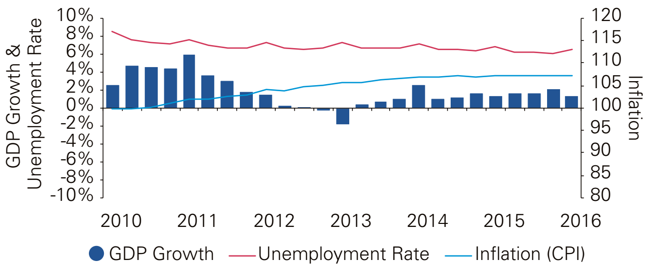
Yield compression continues

Macroeconomic Overview

The economy in Germany has been characterised by steady growth over the last two years. After an increase of 1.6% in 2014, German Gross Domestic Product (GDP) grew by 1.7% in 2015. This growth was mainly driven by private and government consumption, which increased by 1.9% and 2.8% respectively in 2015. The German Institute for Economic Research (IDW) forecasts continued moderate but steady growth of approximately 1.7% for 2016.

However, Brexit could result in a fall in export trade. Germany is a leading exporter; the reduction of growth in exports may lead to a reduction in GDP growth of about 0.1 percentage points in 2016 and 0.5 percentage points in 2017. However, this adjusted forecast takes account only of the direct impact of exports to Great Britain. It is almost impossible to judge indirect effects, such as a decrease in direct investment or impacts on prices. Furthermore, weaker global economic growth, characterised by, amongst other things, a recession in Russia and Brazil and slower growth in China, may also affect German exports, and therefore economic growth.

Economic Indicators



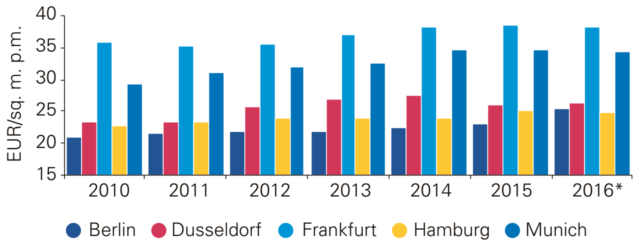
Source: Destatis, 2010 = 100

Germany's real estate market has benefited from both domestic and international demand. In 2015, transaction volumes increased by approximately 40% to EUR56.3bn. Half of this was invested by German buyers and half by international purchasers.

Office Market

Trends in prime office sector rents varied across the top five locations – Berlin, Dusseldorf, Frankfurt, Hamburg and Munich – during H1 2016. Whilst rents in Dusseldorf increased slightly, by 1.2% to EUR26.30/sq. m. p.m., prime rents in Frankfurt decreased by 1.3%, to EUR38.00/sq. m. p.m. Prime rents in Hamburg and Munich also decreased slightly, by 0.8% to EUR24.80/sq. m. p.m. and 0.9% to EUR34.20/sq. m. p.m. respectively. Due to the exceptional level of demand, prime rents in Berlin increased by approximately 10.0%, to EUR25.30/sq. m. p.m., thus surpassing Hamburg for the first time in terms of rental level.

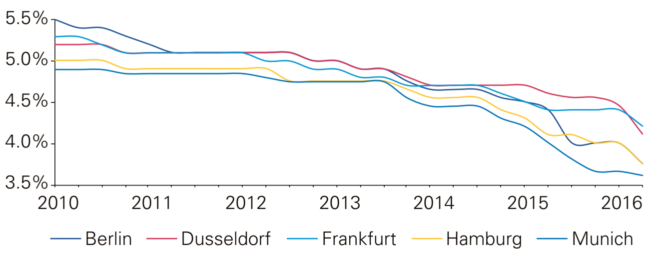
Prime Office Rents



Source: Thomas Daily
Note: * Q2 average

During the first six months of 2016, take-up in the top 5 locations amounted to approximately 1.5m sq. m – an increase of 12.0% compared to H1 2015. The positive trend was driven mainly by lettings in Berlin. Activity here was strongest, at 405,000 sq. m (a 20.9% increase) – Berlin's best ever result in terms of take-up – followed by Munich with 373,000 sq. m (21.5% increase) and Dusseldorf with 228,000 sq. m (11.2% increase). At 225,000 sq. m, take-up in Frankfurt also increased, by approximately 10.8%. Hamburg was the only top 5 city to experience a decrease in take-up, by 9.3% to 233,000 sq. m, due mainly to a lack of large scale lettings.

Prime Office Yields



Source: CBRE

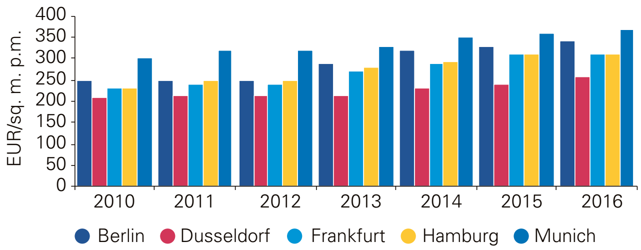
The first half of 2016 was characterised by a further reduction in prime yields Y-o-Y. With a reduction of 65bps to 3.8%, Berlin experienced the strongest yield compression, followed by Dusseldorf, which saw a reduction of 50bps to 4.1%. In the other top 5 locations, prime yields fell by 20bps to 4.2% in Frankfurt, 35bps to 3.8% in Hamburg and to 3.6% in Munich. The continued fall in prime yields is the result of continued strong interest by both domestic and international investors in prime properties in Germany, together with limited availability of investment targets.

During the first six months of 2016, transaction volumes amounted to approximately EUR7.6bn, an 18% decrease compared to H1 2015. The drop is due to insufficient supply, especially of large premises in the Core segment, which cannot keep up with increasing investor demand. Investors are therefore shifting their attention to smaller-volume transactions, so that there were more transactions recorded compared to the same period in 2015.

Retail Market

In the first six months of 2016, prime retail rents in retail remained stable or increased slightly compared to 2015. The most expensive retail location remains Munich with a rent of EUR370/sq. m. p.m., followed by Berlin with EUR340/sq. m. p.m.

Prime Retail Rents

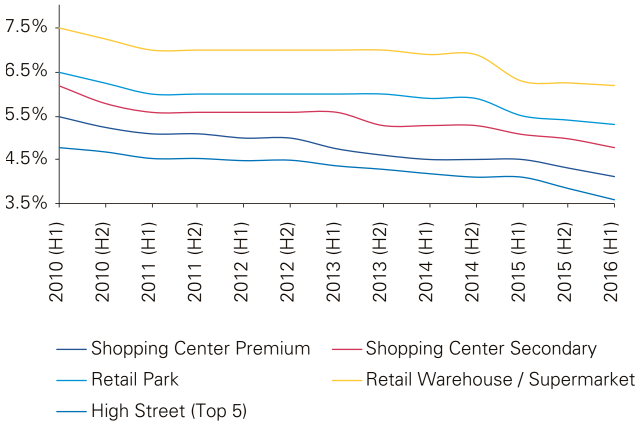


Source: Brockhoff

Due to limited supply and ongoing strong competition amongst investors, prime yields continued to decrease in H1 2016. The biggest fall was recorded in yields for high street retail, which fell by approximately 30bps to 3.6%.

Germany

Prime Retail Yields by Type of Use



Source: CBRE

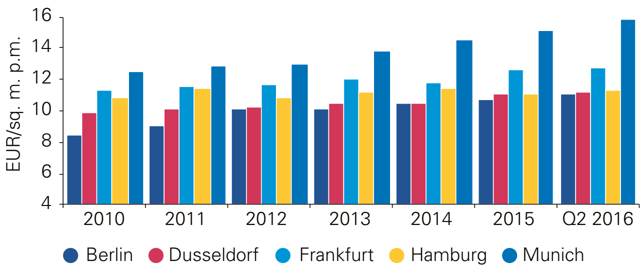
In H1 2016, the volume of transactions in the retail sector amounted to approximately EUR4.1bn. After an exceptional volume of investment in H1 2015, which was the result of the Corio and Kaufhof portfolio transactions, investment volume dropped by approximately 58% in the first six months of 2016. As with the office sector, this is due mainly to insufficient supply of large premises in the Core segment. However, despite the decrease this outcome is in line with average transaction volumes over the last ten years.

As several large portfolios are currently being marketed, market participants expect another good result in terms of investment volume for the second half of the year.

Residential Market

After an exceptional transaction volume in H1 2015, which was notable for, amongst others, the acquisition of GAGFAH and the Südewo portfolio by Deutsche Annington (now Vonovia), the volume of transactions fell by approximately 75% in the first six months of 2016 to EUR4.3bn. However, this result is only about 9% below the ten-year average (excluding the record result registered in 2015). This is again due to a lack of transactions of high volume portfolios (over EUR100m). In contrast, the volume of transactions of up to EUR100m rose by approximately 41% to EUR3.7bn, emphasising the ongoing investor interest in residential assets.

Average Residential Asking Rents



Source: empirica

The highest asking rents per square metre were recorded in Munich, at approximately EUR15.83/sq. m. p.m. (+4.7% compared to 2014), which is again also the strongest increase amongst the top 5 German cities. Munich is followed by Frankfurt, with EUR12.73/sq. m. p.m., an increase of approximately 1.0% Y-o-Y. Hamburg and Dusseldorf experienced increases in rents of 1.4% and 1.1%, to EUR11.25/sq. m. p.m. and EUR11.13/sq. m. p.m. respectively. Rents in Berlin increased by 3.4% to EUR11.09/sq. m. p.m., a cumulative increase in asking rents of approximately 31% between 2010 and 2016.

Focus on Digitisation

There is no doubt that the massive trend towards digitisation will have a huge impact on the economy and society. Trends in the German real estate market are already influenced by the digital economy, which comprises information and communications technologies and internet-related companies.

Due to its strategic location in the centre of Europe and its excellent infrastructure, the logistics sector is one of the main drivers of Germany's economy.
The e-commerce boom which accompanies digitisation has led to increasing demand for logistics space in recent years. At around 6.0m sq. m, take-up increased by approximately 15% between 2014 and 2015, reaching a new record level. Moreover, the amount of newly constructed logistic space is also increasing. From approximately 59% of total take-up in 2015, the share accounted for by new-build space rose in 2016 to 66%.

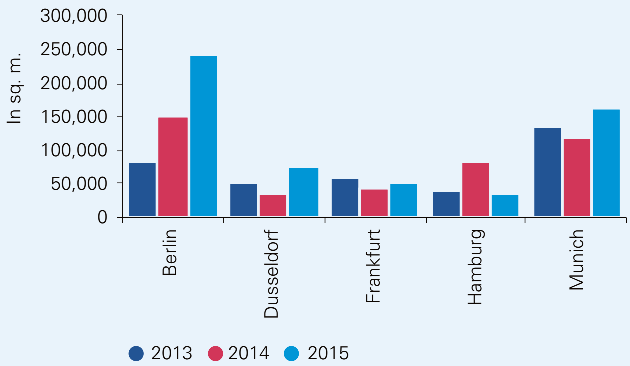
As a consequence, logistic properties are becoming more and more attractive to investors. The record levels for transaction volume (up by around 30% in 2014 and around 40% in 2015) and the yield compression in the German real estate market are proof enough.

The question is: how is the retail sector itself impacted by the e-commerce boom which accompanies the trend towards digitisation. Market participants expect demand for retail space in prime locations to remain stable. This retail space will be converted into showrooms and flagship stores, breaking down the barrier between over-the-counter retail and e-commerce by focussing on customer retention. Customers are inspired and advised in-store so that they buy products online afterwards. However, demand for retail space in B- or C-grade locations is expected to decline.

There is no definitive answer to the question of the impact of digitisation on office buildings and forecast demand for office space. Digitisation brings with it a fear that jobs will be replaced by technology and automation. However, it is evident that the digital economy also creates new employment. According to the Bundesagentur für Arbeit (the Federal Labour Agency), employment in the digital economy increased in four of the top five locations in Germany between 2008 and 2013. The increase ranged from 17.4% in Frankfurt to 44.0% in Berlin. It was only in Munich that employment in the digital economy decreased, by 9.2%.

According to calculations by Investitionsbank Berlin, the digital economy could create around 270,000 additional jobs in Berlin alone.
Digital economy companies are also driving demand for office space. The take-up generated by these companies amounted to approximately 625,000 sq. m in 2015, an increase of about 60% compared to 2013. An exceptional important role is played by Berlin as Germany's "digital hotspot". Whilst digital companies accounted for approximately 21% of take-up in the capital in 2013, their share of office space take-up in Berlin reached around 39% in 2015.

Develpoment of digital Take-up



Source: BNP Paribas Real Estate

Digitisation brings with it other trends that influence the office sector: co-working, remote work and home offices lead to enhanced requirements for flexibility of office space. An up-to-date IT specification is crucial when letting office space in any case.

Beside the impact of digitisation on demand for rental space and investor interest in specific asset classes, digitisation comes along with other benefits such as the simplification of the transaction process and of development projects brought about by storing documents and data and making them available to potential investors or project members on the cloud or in data centres.
Furthermore, digitisation is giving rise to additional financing instruments such as crowdfunding, providing developers and investors with alternative routes to raise equity. Thus, digitisation does not only lead to a fear of vacant office and retail buildings; it also generates demand for alternative asset classes and can actually allow developers and investors to meet (increasing) demand.

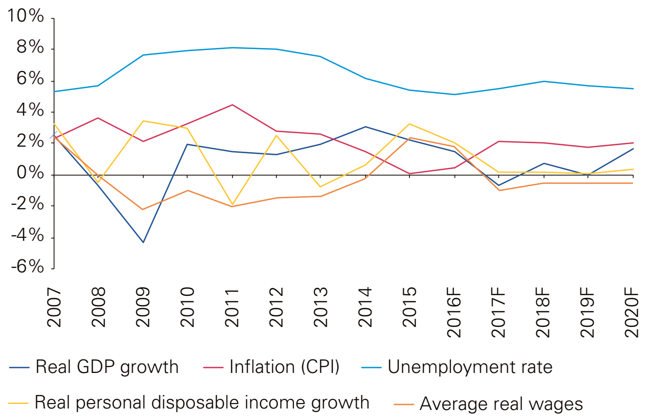
United Kingdom

Life goes on amid Brexit uncertainty

Macroeconomic Overview

The UK's vote on 23 June 2016 to leave the EU is unsurprisingly impacting the economy. While GDP quarter on quarter growth was 0.6% in Q2-16 compared with 0.4% in Q1, there was an immediate post-vote impact on sterling value and financial markets, albeit with some subsequent recovery.[1] It is clear, however, that this is nothing near the scale of 2008. There is a possibility the UK may experience a technical recession within the next few quarters, but most forecasters anticipate a bounce back towards the end of 2017 and the long-term outlook remains largely positive.

Economic Indicators



Source: Economist Intelligence Unit
F – forecast

The Bank of England (BoE) released a package of monetary stimulus measures in August, including cutting the Bank Rate to 0.25%. However the question remains as to whether households will take advantage of the cheaper cost of borrowing amidst the Brexit uncertainty.

Autumn should bring some stability and reassurance for the economy, with the introduction of the new PM's agenda, the conclusion of Labour's leadership contest and the new Chancellor's Autumn Statement. Implications of the Brexit deal are far reaching – from trade barriers, import duties and supply chain management, to hiring of staff, currency fluctuations and consumer confidence – and a firming up of these decisions will be critical to the UK's ability to continue to attract business

Despite uncertainty for occupier markets, the UK is likely to see around €40–50bn invested in commercial real estate (CRE) this year, approximately equal to 2013 and above most annual levels since 2008. After a booming 2014–15, much of

[1] Office for National Statistics, www.ons.gov.uk

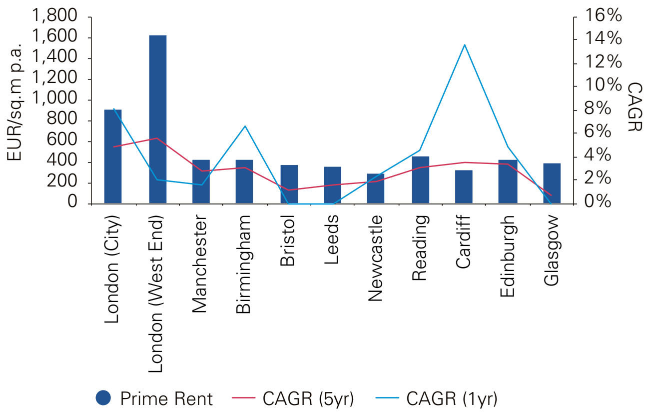
the UK market has peaked in the cycle and investment is expected to return to healthier but more sustainable levels after a dip in the next few quarters. With its strong legal frameworks, political stability and a transparent and liquid market, the UK remains an attractive investment location and should be able to ride the wave of uncertainty.

Office Market

Demand for UK offices peaked in 2015 which, coupled with the Brexit vote impact, has resulted in a fall in investment and leasing volumes in 2016.

London offices are expected to be impacted the most by Brexit with Q2-16 take-up already 56% down Y-o-Y.[2] Both City and West End office rents remained fairly stable in H1-16, however these may come under pressure as leasing slows and some occupiers seek short-term lease extensions while they take stock. This may be felt more strongly in the City given the occupier type, however low vacancy rates for much of the capital should limit the impact.

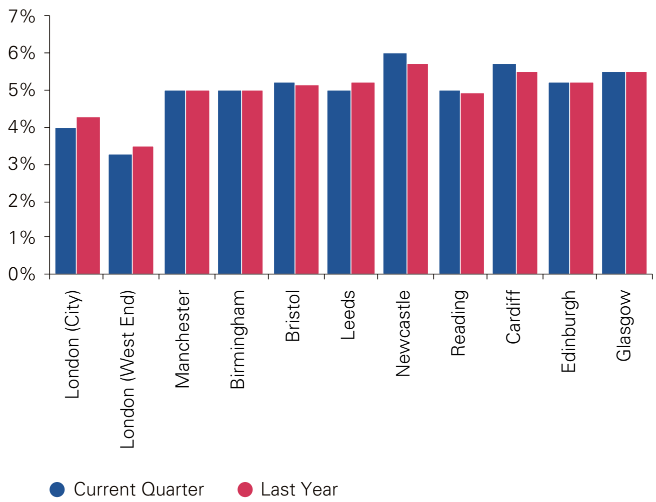
Prime Office Rents – June 2016



Source: Cushman and Wakefield

Investment activity in the City was strong in Q2 at £2.7bn (ahead of the £1.9bn 10 year average) whilst transaction volumes in the West End only reached £819m (well below the 10 year average of £1.4bn).[3] With investment having been at unprecedented levels recently and limited supply driving eye-watering prices, it is unsurprising that the market has slowed. With the high percentage of overseas buyers in the London office market the devalued pound should see opportunistic investors taking interest, however this capital may also be tempted elsewhere.

Prime Office Yields (net) – June 2016



Source: Cushman and Wakefield

Investment activity outside London and the South East remained strong in H1, with approximately £2.2bn transacted.[4] Domestic players have traditionally led the regional markets, but overseas investors may look to take advantage of currency fluctuations and potentially more reasonable prices as some UK funds reassess their real estate allocations. The regional occupier markets mostly continue to perform well, although cities such as Leeds and Manchester fell following a strong couple of years. These markets should continue to benefit from "northshoring" as firms seek ways to cut costs.

Business confidence dipped in light of the Brexit vote and investors will be paying close attention to occupier sentiment. While the banking sector has been highlighted as a particularly vulnerable industry ('passporting' of services across the EU being the key issue), the impact of negotiations about access to the single market will be relevant across UK businesses and investors will be sensitive to any change to London's status as a key global city. Volatility is also expected in the technology sector where European cities are trying to tempt start-ups away from London's Silicon Roundabout.

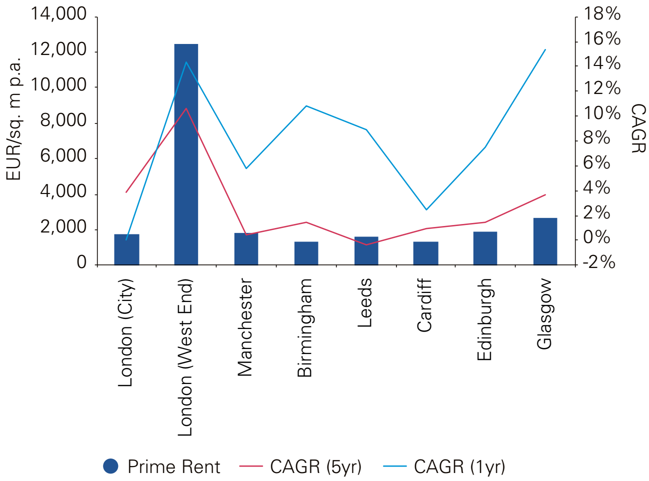
2 Making sense of Brexit – Update III, JLL
3 Central London Office Market Report, Q2 2016, JLL
4 United Kingdom Office – The Property Perspective H1 2016, CBRE

United Kingdom

Retail Market

Despite the Brexit uncertainty, June and July showed retail sales Y-o-Y growth of 0.2% and 1.9% respectively.[5] Better weather and heavy promotions may have given consumers a feel good factor and sense that 'life goes on' following the vote. However the Christmas shopping period will be the real test of the sector's resilience.

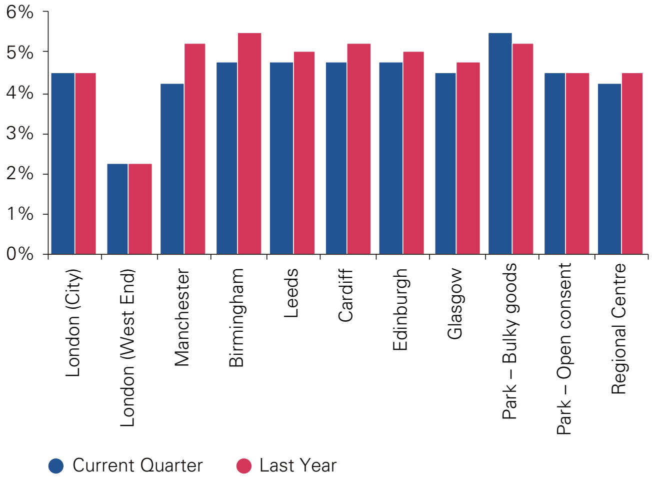
Prime Retail Rents – June 2016



Source: Cushman and Wakefield

The weakening pound may improve retailers' fortunes in the short term if international visitors make previously unplanned trips to the UK and spend a greater amount. Most retailers are expected to have hedged 2016 foreign exchange exposure in anticipation of currency volatility. When these expire in 2017 retailers will need to decide whether to absorb the cost of a weaker pound or pass this onto customers through higher prices, which may curtail the current extra demand.

Prime Retail Yields (net) – June 2016



Source: Cushman and Wakefield

Leasing activity remains buoyant. While there have been high profile collapses of Austin Reed and BHS, the number of retail failures in H1-16 is well below the 2007–2015 average. Key regional cities such as Birmingham continue to benefit from demand from retailers pushed out of London due to limited supply and high rents. With supply generally on the low side across the UK, rents should remain strong and vacancy rates low.

Investment has been relatively healthy this year, although the number of larger deals has reduced as buyers and sellers take stock. After a flurry of deals in recent years, H1–16 shopping centre sales slowed 27% Y-o-Y with £1.46bn transacted.[6] Declining consumer confidence plus limited supply will likely mean a continued slowdown in H2, although some investors may seek to capitalise on the opportunity to enter this otherwise attractive market at more reasonable prices. High streets have performed better, with Savills estimating roughly £1.6bn invested across the UK, although this was mostly made up of smaller deals.[7]

[5] British Retail Consortium and KPMG Sales Monitor, July 2016

[6] UK Shopping Centres Q2 2016, Cushman and Wakefield

[7] UK Shopping Centre and High Street Bulletin, Savills

Residential Market

Brexit may explain some trends in the coming months but there are other key factors at play – notably the raft of stamp duty land tax (SDLT) changes aimed at second home buyers and the prime market and the usual summer slowdown.

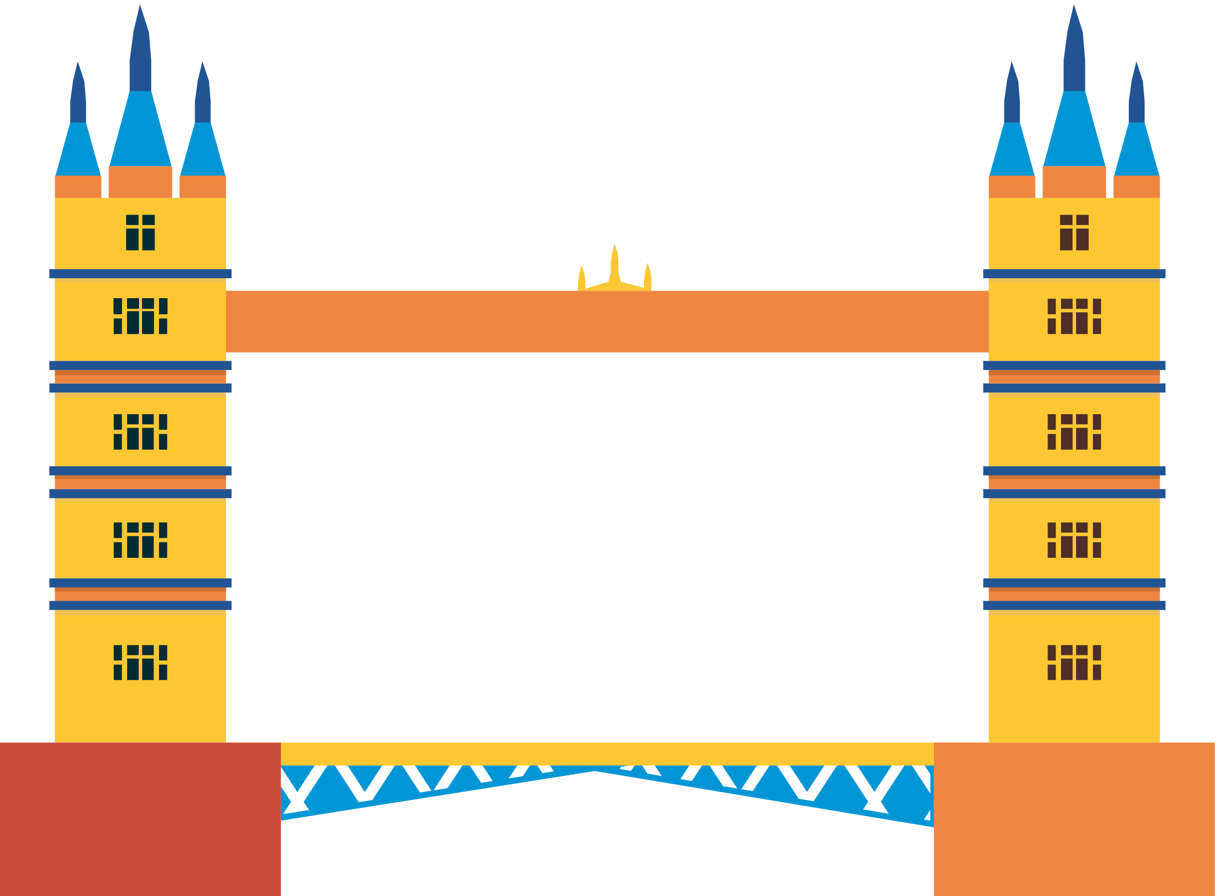
Nationwide estimates annual price growth at 3–6% over the twelve months to June 2016, increasing significantly ahead of market expectations in recent months at 5.1% in June, 5.2% in July and 5.6% in August.[8] However, this is not expected to continue, as the impact of the Brexit vote is only beginning to be seen and BoE data shows a decline in July mortgage approvals to an 18-month low as prices are considered to be falsely high due to limited supply rather than real value. London is most exposed to a price drop, with regional markets expected to be much less impacted. London has been due a price correction and is unlikely to continue to attract previous asking prices in the uncertain environment. However, assuming the economy stabilises in 2017, this period of reduced pricing will likely be fairly short-term. Overall, the residential market is better positioned to weather the storm than in 2008, for example the lower level of debt in housebuilders means they will not need to discount as they did before.

[8] Nationwide House Price Index, August 2016

The pound depreciation may attract foreign investors as London becomes more affordable for overseas capital. However prime real estate has suffered from a less hospitable tax environment recently and will be sensitive to financial sector developments due to Brexit.
Transaction volumes experienced volatility in H1-16 which will continue in H2. With SDLT changes introduced in April there was a clear spike in March activity with a dip in subsequent months. Uncertainty in the run up to the referendum will also have had an impact. The reduced BoE interest rate may stimulate demand if cheaper mortgages make purchases more affordable, however rates were already at a historic low and households will be impacted by anticipated rises in inflation and unemployment and a forecast decline in wage growth. Furthermore, lenders may seek lower LTV ratios to protect themselves.

Supply continues to lag behind demand with a risk that Brexit uncertainty will exacerbate this ongoing issue. Construction output declined by 0.3% in Q1 and 0.7% in Q2, marking the first recession for the sector since 2012.[9] While the Brexit impact will be minimal for this period, it shows an industry vulnerable to uncertainty. With supply already well behind demand, any slowdown in new starts now will be felt for several years given how long it takes to develop sites. Furthermore, with the industry's reliance on EU workers, the future of their right to work in the UK may have drastic implications.

[9] Construction output in Great Britain: June 2016 and Apr to June 2016, ONS



United Kingdom

Focus on Digitisation

Our recently published report on how the UK real estate sector will look in twenty years' time unsurprisingly features much thought around the impact of digitalisation.10 Some key implications are outlined below.

Office occupiers increasingly need a building to act more as a connection hub than a traditional desk-based office

- Physical presence in the office is less important as employees can log in from almost anywhere and utilise virtual meetings
- Focus on informal collaborative spaces rather than formal meeting rooms and siloed desks. KPMG's new London office has more open meeting zones and integrated facilities such as cafes
- Corporates embrace office layouts previously typical of technology start-ups
- Company buildings become a marketing tool to attract clients and employees – tenants seek a cutting edge blank canvas to put their stamp on

New players operating in the real estate sector

- Firms such as WeWork and Workspace have capitalised on needs of start-ups and others for flexible office space they can grow/shrink in as they evolve. The traditional fifteen year lease does not apply
- Co-working spaces such as in London's Silicon Roundabout allow like-minded businesses and employees to share ideas – clustering at a new level
- Community and entertainment focus with the millennial generation's apparent blurring work and play divide
- Traditional real estate firms can take advantage of this model as it becomes more mainstream. While corporates are unlikely to do away with offices they may have a smaller central hub with satellite spaces on flexible leases

Retailers adapting to the rise of e-commerce

- Digital window displays, in-store apps and WIFI attract footfall
- Shopping centres embrace technology – Hammerson's Plus app guides visitors around stores and sends personalised offers based on location
- Opportunity to gather shopper data and use it to improve shopping experience, maximise revenue generation and ensure efficient use of space
- Value of data for others – new income source with permissions to share data

E-commerce changes for the logistics sector

- Increased demand for well-connected high-tech big sheds as logistics firms seek to replicate Amazon's digitalised model
- Smaller urban hubs sought after with delivery time competition
- Previously popular warehouses left deserted – some due for residential conversion, others rendered useless

Property as a service

- Real estate is no longer just about bricks and mortar in the rapidly changing digital world
- Landlords are increasingly likely to consider data analytics, catering and laundry services, integration into other services or parts of the supply chain, advertising and online links. Serviced offices for example are just the start of this trend

Nordic Region

A tale of four countries

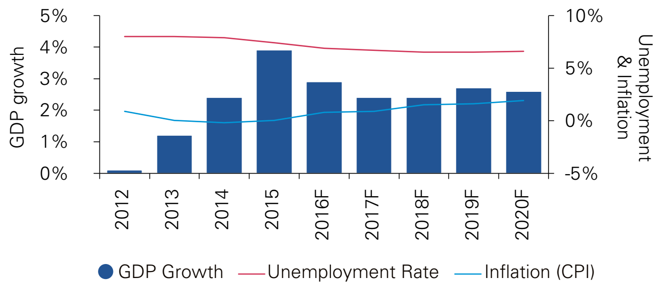
Macroeconomic Overview

Sweden

- GDP: The economy is expected to maintain its strong growth momentum due to strong fundamentals.
- Inflation: Inflation is expected to increase in 2016 and 2017 because of the decreased effect of lower oil prices.
- Employment: Employment is expected to improve as companies plan for expansion.

Growth in the Swedish economy was slow in Q1 2016, at 0.5%. Growth was driven by an increase in private consumption and investment by businesses. During Q1 2016, retail sales increased by 4.6% Y-o-Y and investment by 2.2%. Exports witnessed weak growth during Q1 2016 because of a lack of demand for capital goods and services. The outlook for growth is positive due to strong growth in private consumption and business investment.

Economic Indicators



Source: Economist Intelligence Unit
F – forecast

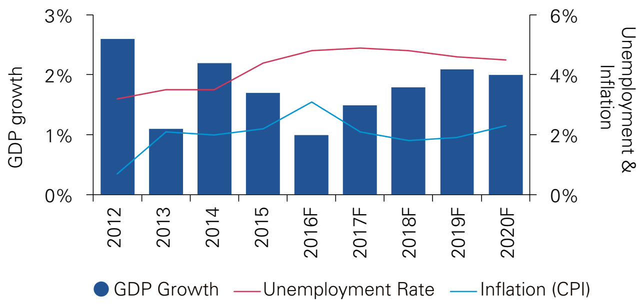
Norway

- GDP: Economic growth is expected to slow down in 2016. However, a favourable monetary and fiscal policy is expected to provide a boost to the economy.
- Inflation: Inflation is expected to increase due to loose monetary policy and weakness in the currency.
- Employment: Low oil prices are expected to place employment under pressure.

The Norwegian economy witnessed a growth of 1% between Q4 2015 and Q1 2016. The economy continued to suffer from low oil prices in early 2016, and this resulted in companies cutting back investment and jobs. Also, weak wage growth and inflation resulted in weak consumer spending. In the long term, growth is expected to improve, based on a recovery in the oil industry and a reduction in inflationary pressure.

Nordic Region

Economic Indicators



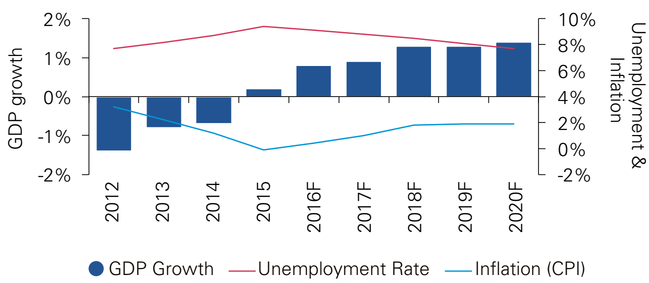
Source: Economist Intelligence Unit
F – forecast

Finland

- GDP: Economic growth is expected to improve but external and internal challenges remain.
- Inflation: Inflation is expected to become positive.
- Employment: Employment is expected to stabilise.

Between Q4 2015 and Q1 2016, the Finnish economy witnessed weak growth of 0.6%. The main driver for growth was private consumption, offset by a decline in exports and public spending. A fall in the unemployment rate, accompanied by low inflation, resulted in an increase in disposable income and private spending. At the start of 2016, the recovery in fixed investment remained weak, and this weakness is expected to continue. Concerns remain over the strength of economic growth, as the country faces structural issues such as weak cost competitiveness, poor labour productivity and declining corporate profitability.

Economic Indicators



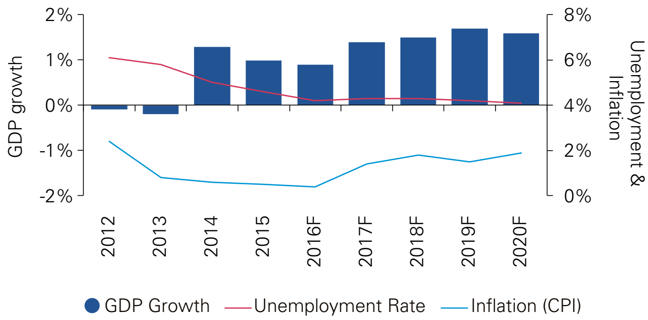
Source: Economist Intelligence Unit
F – forecast

Denmark

- GDP: The Danish economy is expected to improve gradually.
- Inflation: The inflation rate is expected to increase in 2016 and 2017.
- Employment: Employment is expected to improve as companies plan for expansion.

The Danish economy grew by 0.5% between Q4 2015 and Q1 2016. This growth was attributable to a strong increase in domestic demand and improved export performance. The growth of the economy was driven by an increase in fixed investment by firms seeking to expand their operations. This increase in investment is also expected to lead to a lower unemployment rate. In the medium term, economic growth is expected to be driven by a fall in unemployment and increased private consumption.

Economic Indicators



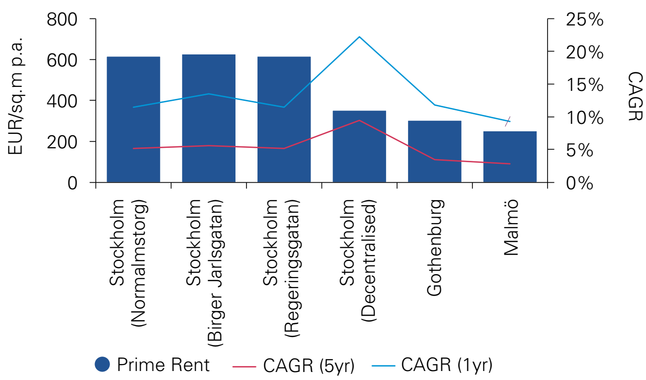
Source: Economist Intelligence Unit
F – forecast

Office Market

Sweden

The growth in the Swedish economy is expected to have a positive effect on the office real estate market. Between the start of 2016 and Q2 2016, healthy growth has been evident in both occupiers of office space and investment in office space. In terms of occupier growth, Stockholm and Gothenburg recorded the highest increase because of growth in employment. During Q2 2016, investment in office space increased by 20% Y-o-Y. This growth in investment was driven by favourable borrowing rates and rental growth. Although demand for office space increased, supply is expected to decline. The outlook for office real estate remains positive due to growth in rents during H2 2016, driven by a shortfall in supply.

Prime Office Rents – June 2016



Source: Cushman and Wakefield

Norway

The Norwegian office market grew during Q2 2016, driven by growth in the Norwegian economy during H1 2016. The occupier market grew in Q2 2016 despite the negative impact of low oil prices. The major drivers of this growth were the consolidation of office space by some occupiers and growth in the central business district (CBD). The impact of lower oil prices continued to weigh down on those areas most exposed to the oil sector. Investment in office space remained strong during Q2 2016 due to favourable financing conditions and low interest rates. Of the various markets, Oslo attracted the majority of the investment. Second-tier markets also witnessed growth in investment. The market outlook remains modest, with stable demand for office space offset by low growth in the economy.

Prime Office Rents - June 2016

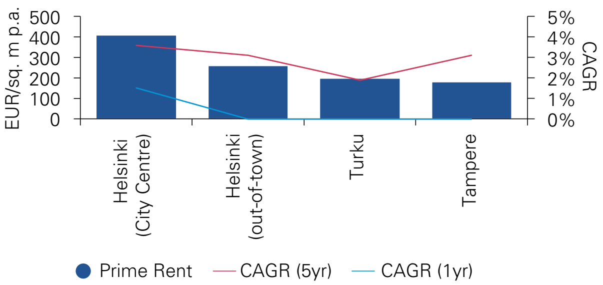
Market (Submarket)	Prime Rent – EUR/sq. m. p.a.	CAGR (5yr)	CAGR (1yr)
Oslo	420.0	2.2%	1.3%

Source: Cushman and Wakefield

Finland

The recovery in the economy is expected to strengthen the office market. The occupier market is expected to improve by the end of 2016. However, during Q2 2016 vacancy rates remained high, at between 13% and 14%. Whilst supply was limited, there was strong demand for modern buildings. In addition, demand for good quality secondary office space also surged during the quarter. Further, the ongoing development of transport infrastructure in Helsinki is expected to reshape the occupier market by enabling occupiers to move into low rental areas. The investment market witnessed demand for office assets in prime properties. However, it is expected that this trend will wane, with the focus shifting towards secondary properties. The outlook for the occupational market appears weak because of the slow growth in the economy, whilst the focus of the investment market is expected to move towards secondary properties.

Prime Office Rents – June 2016

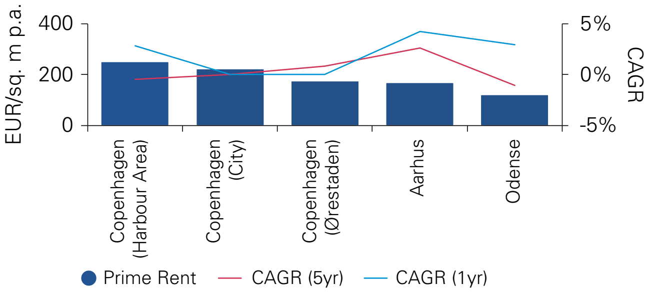


Source: Cushman and Wakefield

Denmark

The positive economic growth drove growth in the office market in the country as a whole. The occupier market is driven mainly by demand for space in central business district areas. In Copenhagen, there are some companies scouting for space in larger office complexes which house multiple tenants with common facilities. Institutional investors are the most active buyers in the market, with a focus primarily on Copenhagen's CBD and Harbour submarkets. In addition, peripheral regions are also increasingly important for investors. The state of the Danish economy is closely linked to overall European demand, and so the impact of the Brexit vote on the country's office market has yet to become clear.

Prime Office Rents – June 2016



Source: Cushman and Wakefield

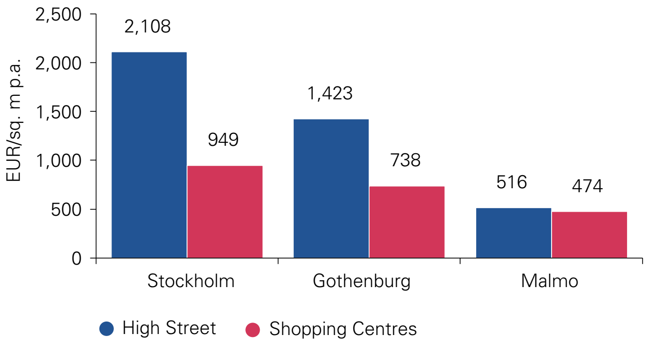
Retail Market

Sweden

Sweden is seeing a strong retail rental market, particularly in locations such as Stockholm. Increased demand for retail space, combined with lack of supply, has pushed retail rents upwards. Markets such as Gothenburg have witnessed a decrease in vacancy rates, whilst new developments have been taking place in Malmö. The outlook for retail space is expected to improve in Sweden's top three cities because of strong demand and growth in prime rents.

Nordic Region

Prime Retail Rent – June 16

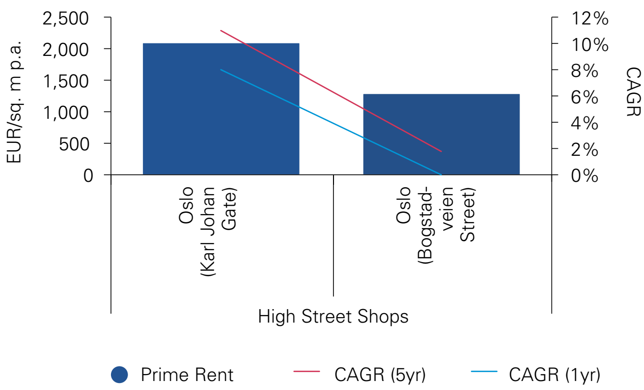


Source: CBRE

Norway

During H1 2016, trends in the retail market were positive, as the Norwegian economy continued to improve. The retail market is expected to grow further, driven by the arrival of international brands in the country's high streets and retailers on the lookout for space in prime locations. The rental level is also expected to spur growth. Retail investment is hampered by a lack of investment product and rising interest rates. The outlook for the retail market is expected to be positive because demand for retail space will remain stable.

Prime Retail Rent – June 16

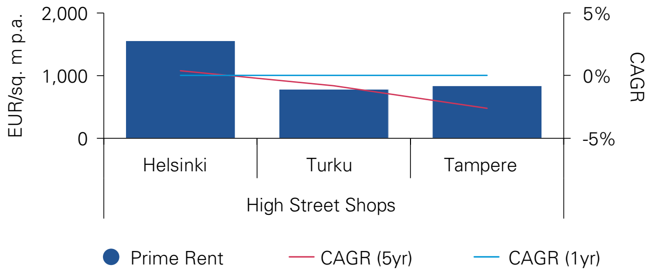


Source: Cushman and Wakefield

Finland

The growth in the Finnish economy during H1 2016 has resulted in positive trends in the retail market. Over the second quarter, consumer confidence increased from 9.8 in April to 14.9 in June. The retail occupier market remained stable, with steady demand for retail space in high streets and shopping malls. Rents remained unchanged, and they are expected to rise during the year due to further demand for both prime and secondary locations. Investment in retail remained stable as acquisitions by investors from the Nordic region continued. The outlook for retail property is expected to be stable, with an overall positive outlook and improved rents and yields.

Prime Retail Rent – June 16

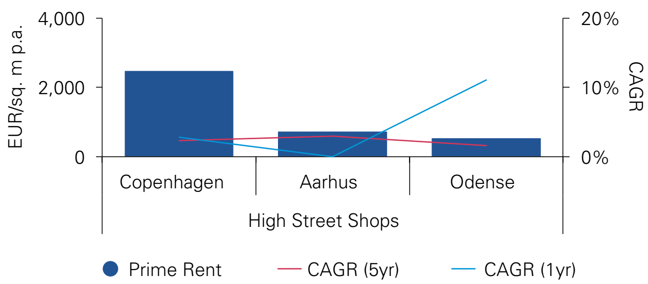


Source: Cushman and Wakefield

Denmark

The continued positive growth in the Danish economy during Q2 2016 has resulted in positive growth in the retail property market. The unemployment rate remained unchanged at 4.3% in May, with consumer confidence improving from 3.2 in April to 4.4 in June. The occupier market witnessed strong demand and limited supply for quality prime retail locations, resulting in upward pressure on rents. The increase in rents in prime locations resulted in increased demand for secondary locations and major regional shopping centres. New entrants in the Danish market are generating demand for retail space. Yields are low because of competition to acquire retail space. This is also pushing investors to seek out acquisitions in suburban locations. The outlook for the retail market remains positive due to strong demand for retail space, and this is expected to push rents upwards and further improve yields for investors.

Prime Retail Rent – June 16



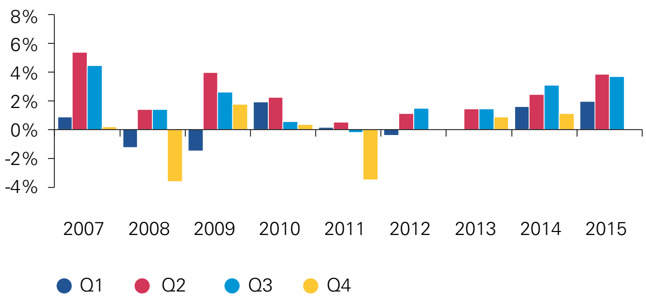
Source: Cushman and Wakefield

Residential Market

Sweden

Between Q1 and Q2 2016, Sweden witnessed an increase in prices. Prices increased in 18 out of the 21 counties in Sweden. The price of detached or semi-detached houses increased by 4%. Prices rose by 14% Y-o-Y in Stockholm and Jämtland County. Across the country, the smallest increase, of 4% Y-o-Y, was registered in Norrbotten County. On an annual basis, an increase of between 9% and 14% was seen in the metropolitan areas of Greater Malmö, Greater Gothenburg and Greater Stockholm. During Q2 2016, the average price in Sweden was SEK 2.8m (approximately EUR295,120).

House Price Change

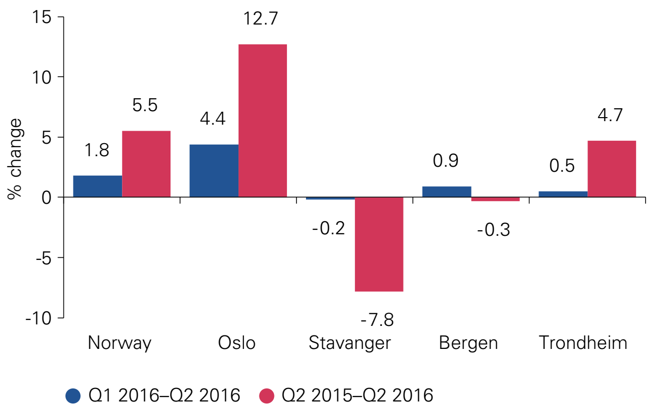


Source: Statistics Sweden

Norway

Between Q1 and Q2 2016, house prices in Norway increased by 1.8%. The highest price increase, of 3.4%, was for apartments in blocks. On a quarter-by-quarter basis, prices for small houses and detached houses increased by 2.5% and 1% respectively. In Oslo and Bærum, house prices increased by 12.7% Y-o-Y. In the Stavanger region, house prices fell by 7.8% Y-o-Y. During the quarter, house prices in Norway increased by an average of 5.5%.

House Price Change

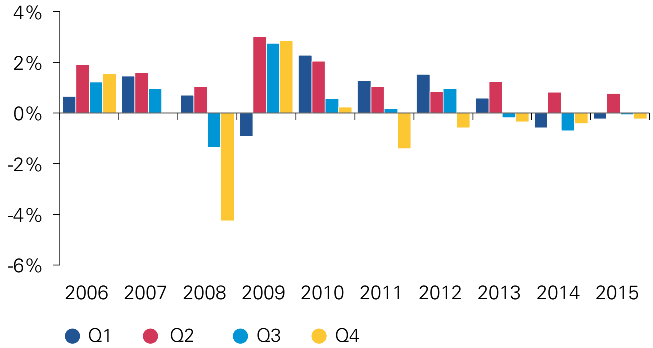


Source: Statistics Norway

Finland

During Q2 2016, non-subsidised residential rents increased by an average of 2.4% Y-o-Y across the country. Nationwide, rents for government-subsidised dwellings increased by 3.1% Y-o-Y. On a quarterly basis, rents for non-subsidised dwellings and government-subsidised dwellings increased by 0.6% and 0.9% respectively.

House Price Change

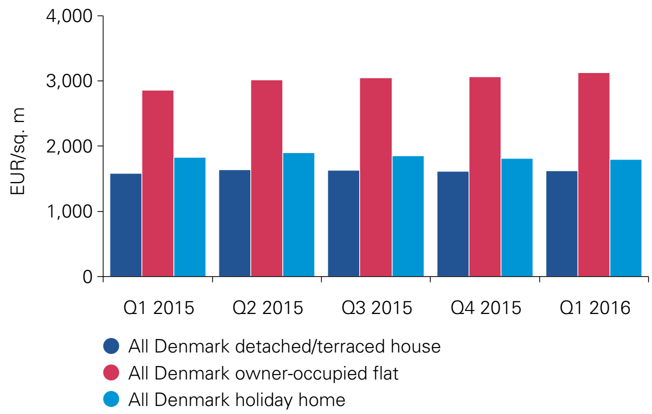


Source: Global Property Guide

Denmark

During Q3 2016, the overall house price index fell by 0.3%, continuing a decreasing trend which started in Q1 2016. During Q1 2016, the house price index recorded an increase of 3.94% Y-o-Y. The highest increase was for owner-occupied apartments, which recorded growth of 9.5% Y-o-Y and 2.1% compared to the previous quarter. Prices for detached/terraced houses increased by 2.6% Y-o-Y and by 0.3% compared to the previous quarter. In contrast, demand for holiday homes decreased by 1.6% Y-o-Y and by 0.7% on a quarterly basis.

Property Prices



Source: Association of Danish Mortgage Banks

The Netherlands

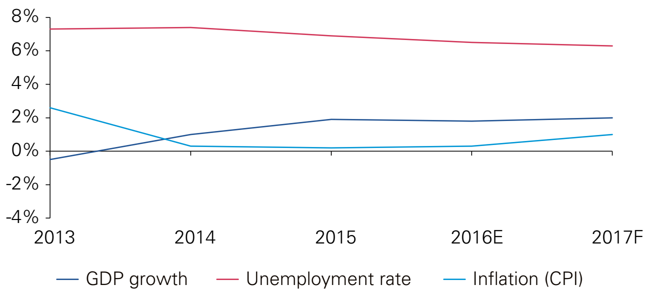
Growth prospects fuel record breaking deal volume

Macroeconomic Overview

The Netherlands economy is experiencing a third consecutive year of GDP growth. Forecasts suggest growth of 1.8% for 2016, similar to 2015, and 2.0% for 2017. This is mainly driven by a strong global economic recovery resulting in global growth of 2.9% this year and anticipated growth of 3.2% next year. Such a recovery typically benefits a trading economy like that of the Netherlands. In 2016, the contribution to GDP growth by the export sector is still relatively low. This is due mainly to the decision to decrease gas production, resulting in higher gas imports and lower exports. The contribution of exports to total GDP growth is expected to increase again following another year of global growth.

Moreover, a persistent decrease in the unemployment rate has been observed since the peak year of 2014, and forecasts are for further decreases of 0.4% and 0.2% in 2016 and 2017 respectively. The fall in unemployment is fuelled by the government's EUR5bn financial relief programme launched at the end of 2015 and by the increase in the pension age from 65 to 67.

Economic Indicators



Source: Centraal Plan Bureau
E – estimate
F – forecast

The ECB's quantitative easing ("QE") programme has put pressure on the inflation figure, something that is still being seen in 2016. Nonetheless, three consecutive years of very low inflation in the Netherlands are expected to come to an end following increases in import and oil prices. An inflation rate of 1.0% is expected for 2017.

The outlook for the economy is promising, mainly based on growth in global trade. GDP figures are outperforming Europe as a whole and unemployment is falling steadily. The unemployment rate is well below the EU average (i.e. 9.3%). Inflation on the other hand is slowly falling behind the ECB target of 1.5%.

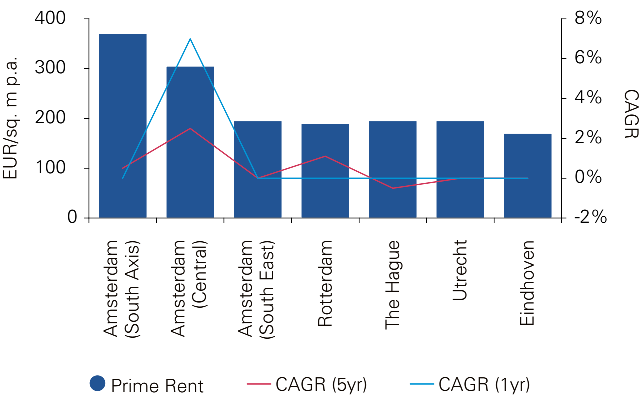
However, the refugee crisis, the result of the Brexit referendum and high volatility on the financial markets have also increased uncertainty, which may impact the overall macro-economic performance in the (near) future.

Office Market

From the end of 2015 to mid-2016, the vacancy rate in the office market has decreased to 5.4%. Prime locations, mainly the South-Axis in Amsterdam, are faced with shortages in the supply needed to meet increased demand, and this is leading to companies being forced to choose another location.

Brexit may have some negative impacts on economic prosperity in the Netherlands. However, it may also present opportunities and increased demand for office real estate, given that UK-based companies may move towards capital cities on the European continent. As a result, prime locations in the Netherlands in particular may benefit in the long run. However, greater supply will also be necessary in order to accommodate this increased demand, particularly in Amsterdam.

Prime Office Rents – June 2016



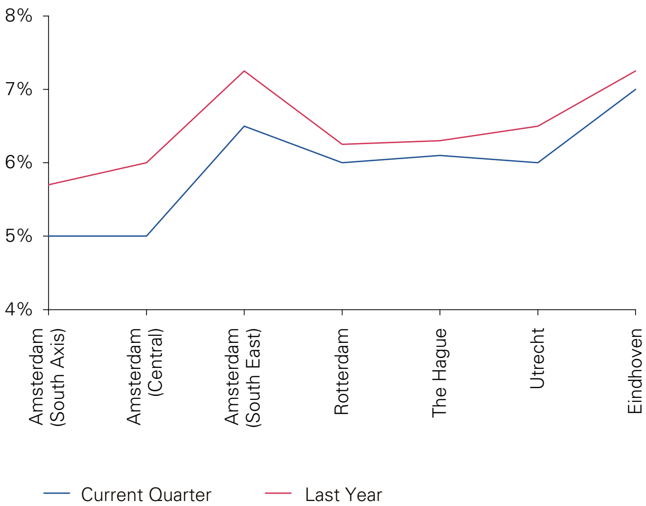
Source: Cushman and Wakefield

In terms of rent per square metre, Amsterdam (South Axis) is still the highest priced office location in the Netherlands, at an average of EUR370/sq. m p.a. Looking at changes in rent, only offices in Central Amsterdam have experienced an increase. Turning to the 5-year growth rate, an increase can be seen for the Amsterdam and Rotterdam areas, whilst The Hague has experienced a slight fall in rents. In contrast, between the end of 2015 and the mid-point of 2016, average office rents across the market as a whole fell by 0.9% to EUR130/sq. m p.a.

Gross yields in the office market show a distinct contraction compared to last year. A fall in yields has been witnessed across all prime locations. The most significant change was in Central Amsterdam, where the yield contracted (Y-o-Y) by a substantial 1.0%, to its current level of 5.0%. This suggests that risks are perceived to be lower in prime office locations.

Office market investment volumes also reveal a reduction in perceived risk. In the first six months of 2016, investors acquired EUR2.3bn of office real estate. Compared to Q1 and Q2 2015, investment volumes grew by 146%. An important example of the increase in investor appetite is the sale of "De Rotterdam" to a consortium of Korean and French investors after a long marketing period.

Prime Office Yields (Gross) – June 2016



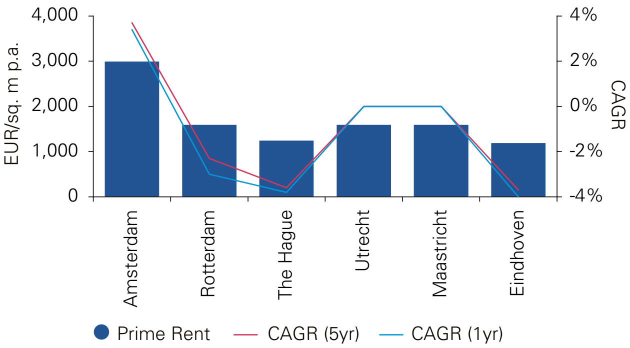
Source: DTZ Zadelhoff, Cushman and Wakefield

Retail Market

The retail market is still under scrutiny due to the global shift towards online shopping and the shake-up of older retail formulas that are not adapting sufficiently to meet current market (and customer) demands. This has contributed to a few large retailers such as the fashion chains MS Mode and McGregor and the food retailer Mitra filing for bankruptcy in the second and third quarters of 2016. The result is that landlords are experiencing difficulties finding new (large) retailers, and this is giving rise to longer vacancy and remarketing periods.

The Netherlands

Prime Retail Rents – June 2016



Source: Cushman and Wakefield

The differences between locations provide a good insight into the retail market. Even though tenants are occasionally lost in major shopping streets in prime locations, demand for these locations is considerably stronger, whilst vacancies are increasing rapidly and rental income is decreasing in the country's secondary locations.

In the past half year, vacancies in the retail market increased by a staggering 7.1%. This increase is due mainly to increased vacancies in secondary retail locations. But rents in prime locations within Rotterdam, The Hague and Eindhoven have also decreased by 3% or more, indicating a significant change in demand for primary retail locations.

Despite the increase in the overall investment volume, the retail market reported a 40% decrease in its investment volume compared to the same period last year. The investment volume for Q1 and Q2 and 2016 amounted to EUR0.8bn, whereas during the same period in 2015, a total of EUR1.3bn was invested in the retail market.

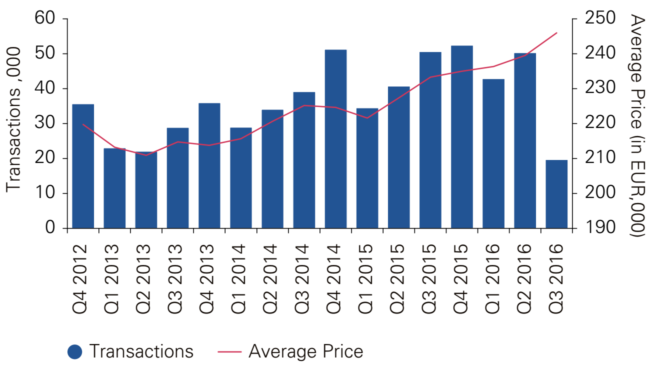
The vacancy and investment volumes do not indicate a positive half year for the retail sector. However, foreign retailers are showing increasing interest in the market, with good examples of this including Hudson Bay and Pull & Bear who have decided to expand their activities to the Netherlands.

Residential Market

The residential market has experienced the most significant increase in housing prices for twelve years. Nationwide, prices per square metre are back to pre-crisis levels. Driven downwards by the European Central Bank's QE programme, mortgage rates in the Netherlands are at a historic low. As a result, the number of mortgages recorded in July this year increased by 8.4% compared to July 2015. In combination with the increase in consumer confidence, the current market suits those in search of a new home.

The number of transactions confirms these developments, as both the second and third quarters of 2016 outperformed the comparable quarters in 2015. The average price per transaction is also following this upward trend, increasing to approximately EUR245,000 per transaction.

Dutch Residential Sales



Source: Kadaster

On the other hand, the increase in house prices means an upsurge in scarcity, especially in prime locations. There is therefore a need to build new homes, otherwise people will no longer be able to afford residential property in these locations. It is also possible that transactions in prime locations could come to a standstill as a result.

Focus on Digitisation

The current growth of digitisation in the form of the Internet of Things ("IoT") and Big Data & Analytics ("BD&A") is permitting the industry to create the buildings of the future. This trend is currently unfolding right across the office, residential and retail real estate sectors.

Trends in digital technology are providing opportunities in real estate at portfolio level by improving performance measurement, value analysis and detailed forecasting. But advanced digitisation can do much more than that. It enables the sector to create smarter and future-proof buildings by improving sustainability, building efficiency and comfort for its users. In the Netherlands, we are experiencing an enormous increase in the use of IoT and BD&A technologies in the real estate sector.

By using advanced digital technologies in the building itself, the world's smartest and most sustainable office building has been created in the Amsterdam region. Housing over a 1,000 shared workstations across fifteen floors, producing more energy than it consumes and boasting more than 28,000 sensors, this innovative building is truly the office building of the future.

A fully automated system allows the building to be completely energy neutral by utilising its solar energy systems, rainwater collection, natural ventilation loop and aquifer thermal energy storage. A digital ceiling tracks users everywhere, so the building knows where and when to shut down lighting and heating/cooling, and reschedule cleaning to save energy and costs. User comfort is increased by informing users where available parking spaces, desks and lockers can be found, and by personalising settings for temperature and lighting for individual workstations, all via their smartphones which users can charge wirelessly on every desk. The building even remembers their favourite coffee machine settings and weekly gym routine.

We see a similar trend in the residential sector where more and more residential developers are aiming at the construction of a digital living environment. Developers are experimenting with future-proof concepts by embedding, for example, "care-concepts", energy-optimised living, smart living and lighting and predictive maintenance into new and existing residential buildings. An increasing number of developers are teaming up with investors, municipalities and even life- and health insurers to prepare for the digital living environment of the future. Residential complexes are being fitted with all kinds of sensors to gather data on the use and quality of homes, all to improve liveability and comfort.

The growth of digitisation can also be seen in retail property where numerous experiments have started with IoT and BD&A technologies. We see our clients monitoring shopper movements within shopping malls and measuring key synergies between different anchor stores within these retail centres. This has led to the introduction of Mall and Tenant Management 2.0, providing portfolio and centre managers with a new and effective toolkit to monitor and analyse real estate performance and value.

As with all technological innovations, success is largely dependent on successfully changing human behaviour. Both owners and users of real estate have to adapt to this new environment in which advanced digitisation provides a multitude of possibilities. Owners need to change and (re) develop their business models to support and use the new digital environment in order to benefit from it fully. Additionally, prerequisites such as data governance, data maturity and privacy protection need to be established as well. Users have to change their habits to enable these technologies to help them. An example of the need for changes in behaviour is the utilisation of the office building we mentioned earlier. Utilisation currently remains a challenge on peak days, as checking in at desks via Quick Response Code scanning is proving to overcharge most users, and desk occupancy remains unknown. The building's owners need to think of ways to incentivise users to change their behaviour and allow digital technologies to increase their comfort and improve usage of the building.

In the Netherlands, IoT and BD&A are quickly becoming a core element of the real estate sector. Although the traditional sector still has a long way to go, there is definitely no turning back.

Belgium

Market conditions remain challenging

Macroeconomic Overview

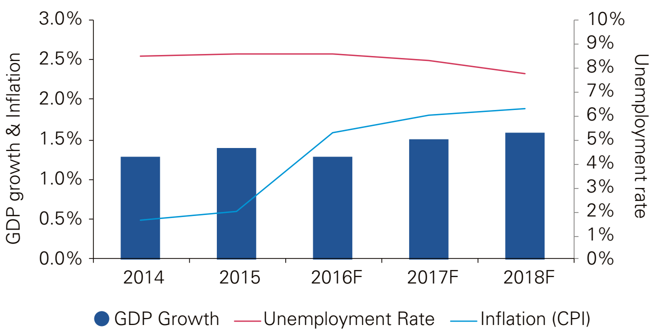
According to the Belgian National Bank, Belgium's GDP grew by 1.4% in 2015. In 2014, GDP growth was 1.3%.

The Belgian economy grew at a rate of 0.2% between Q4 2015 and Q1 2016. This growth was underpinned by an improved climate for the manufacturing industry and business services. The Belgian economy is expected to grow by 1.3% in 2016 and 1.5% in 2017 (less than the Eurozone average). Fiscal cuts are expected to act as a drag on growth in the coming years. There is uncertainty associated with the reform of corporation tax announced by the Minister of Finance.

In H1 2016, concerns surrounding employment have led to a drop in consumer confidence compared to 2015.

In 2015, inflation was low, at 0.6%. It has increased to 1.6% in 2016, mainly driven by an increase in indirect taxes. In the next few years, inflation is expected to increase further, to 1.8% in 2017 and 1.9% in 2018.

Economic Indicators



Source: Economist Intelligence Unit
F - Forecast

Unemployment levels increased slightly in 2015 (to 8.6%); they are expected to remain stable in 2016 and decrease gradually from 2017 onwards.

General and regional elections took place in 2014. This resulted in a centre-right coalition in power, with a French-speaking liberal as prime minister, poised to initiate and push through ambitious reforms. The government is attempting to deliver on its promised tax and pension reforms, although it is facing challenges within the coalition and in parliament. The government is also planning a so-called "tax shift" that aims to shift part of the tax on income to other tax sources such as VAT, capital or the environment. The scope of the government's plan is likely to be curtailed due to tensions within the coalition. These tax measures also include the creation of a specialised real estate investment vehicle. This may become a tax efficient special purpose vehicle to hold Belgian property, as it would benefit from a specifically-determined tax base. The result would be that real estate income would effectively remain virtually tax-exempt.

Office Market

Belgium's economy remains vulnerable and the country's economic growth is expected to weaken in the short-term, impacted by the terrorist attacks in Brussels on 22 March and the UK's decision to leave the European Union (Brexit). Market conditions remain difficult and companies are taking time to make real estate decisions.

Brussels saw an increase in take-up during the second quarter of 2016 to between 174,000 and 190,000 sq. m, the highest quarterly figure since 2009. Total take-up for the year-to-date amounts to between 268,000 and 284,215 sq. m. Brussels' Pentagon district accounted 45% of take-up, compared to 18% a year ago.

Despite the low-vacancy rate for (high quality) office space in Brussels, prime rents are expected to remain stable. In 2016, prime rents in Brussels increased only slightly, to EUR275/sq. m p.a. This figure takes no account of incentives granted by landlords, who are often flexible in negotiations with new potential tenants or when renegotiating existing leases, depending on the quality and location of the building and the duration of the lease.

Prime Office Rents – June 2016

Market (Submarket)	Prime Rent – EUR/sq. m. p.a.	CAGR (5yr)	CAGR (1yr)
Brussels (EU Leopold)	275	0.7%	3.8%
Brussels (Pentagon)	235	3.3%	4.4%
Brussels (Decentralised)	195	2.8%	2.6%
Brussels (Periphery)	175	2.5%	9.4%
Antwerp	140	1.5%	3.7%

Source: Cushman and Wakefield

There was downward pressure on prime yields because of low interest rates, the commodities crash, unstable global equity markets, the slow economic recovery, growing cash reserves chasing returns and the activity of foreign institutional players. Prime office yields in Brussels for Q2 2016 are 5.50% in the EU Leopold district and 6% in the Pentagon district.

No major speculative development activity is expected before 2018. Speculative space totalling 65,000 sq. m. is planned for delivery in 2017.

The activity in 2016 was the result of deals at the start of the year coming to a conclusion, and it should be noted that there were substantially fewer investment deals in H1 2016 than a year ago or than the 5-year average. The quarter's activity consists mainly of deals over 10,000 sq. m.

Despite the terror attacks in Brussels on 22 March, there is strong interest in the Belgian market from international players (especially Asian investors). However, Brexit could potentially reduce investment by UK investors.

Retail Market

The retail property market in Belgium is divided into three sectors: high streets in the major cities, shopping centres and retail warehousing. Retail investment was up significantly in 2015, with investors very interested in prime space. The year-to-date investment volume has decreased by 38% compared to H1 2015.

Prime high street yields compressed further as a result of continued demand, whilst shopping centre yields stabilised. Prime yields are down to 3.50% in the premier high streets of Brussels and 3.75% in Ghent.

Prime Retail Yields – June 2016

		Current Quarter	Last Year
High Street Shops	Brussels	3.50%	4.00%
	Antwerp	3.50%	4.00%
	Liege	4.80%	5.25%
	Ghent	3.75%	4.25%
	Bruges	4.05%	4.60%
	Hasselt	4.65%	4.85%
Shopping Centres	Belgium	4.25%	4.75%

Source: Cushman and Wakefield

The outlook is for prime rents to remain stable in all retail sectors. However, in some areas rents may come under downward pressure as the year progresses, as tenants push for better deals from landlords trying to limit vacancy.

Supply is improving in both occupational and investment markets, but restrictive planning laws remain. About 80,000 sq. m. of new shopping centre space is currently in development (e.g. Docks Brussels). Occupier demand is muted, but investment demand is expected to remain strong.

Belgium

Take-up on the retail market in Belgium in the first semester of 2016 is in line with that in H1 2015, with occupiers still wary and taking longer to reach decisions. Whilst demand is healthy, activity is being hampered by a lack of prime stock.

The relatively modest letting activity and the take-up volume are a clear indicator of the subdued occupier sentiment over the last quarter.

2016 was dominated by mid-size transactions by individual investors, focussing primarily on high street shops and retail warehouse assets. With a number of large retail investment transactions in the pipeline, investment volumes are expected to grow considerably over H2 2016.

With the supply of prime space improving, the retail market is expected to remain tenant-friendly over the coming quarters. With better supply expected in the near future, steady demand is forecast for the prime investment markets.

Residential Market

After a short-lived decline in 2014, the Belgian housing market is on a rise in terms of prices. Prices rose because of low interest rates and increased competition between banks seeking to expand their residential loan portfolio.

Prices of houses increased by 3.9% and apartment prices increased by 1.4% in H1 2016 compared to H1 2015. Villa prices rose by 2.8%.

However, the Belgian residential property price index decreased by 0.6% in Q1 2016 compared to the previous quarter.

Gross rental yields in Brussels have remained steady over the past year. Yields on houses in Brussels ranged from 4.46% to 5.01% in October 2015. Gross rental yields on apartments in Brussels were between 4.87% and 5.06% in October 2015.

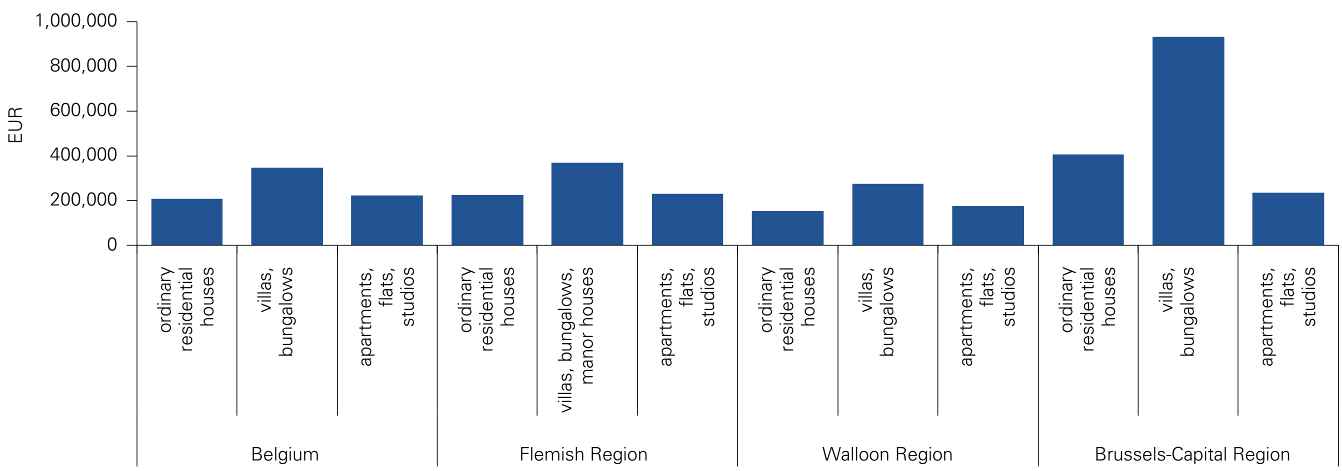
Belgium Residential Market – October 2015

		Price EUR/sq. m.	
Brussels- Apartments	**Yield (p.a.)**	**To Buy**	**Monthly rent**
50 sq. m.	5.06%	3,112	13.13
75 sq. m.	5.37%	2,963	13.27
120 sq. m.	4.87%	3,023	12.26

Source: Global Property Guide

The gap has narrowed between yields on small properties, which tend to be higher, and those on larger properties. The rental market has been subdued for a number of years because of rental controls and the rising number of homeowners. Though the trend is falling, the rental market makes up a significant 30% of housing stock (23% in the private sector, 7% in social housing). The average price per asset for the different categories for H1 2016 increased compared to H1 2015, except for apartments in the Flanders region and villas and bungalows in the Brussels Metropolitan region. The average price per asset in H1 2016 was the highest in the Brussels Metropolitan region, at EUR931,012 for villas and bungalows, still lower than the average 2015 price for villas and bungalows, of EUR1,064,281.

Average Price per Building – first Semester 2016



Source: Statbel Belgium

Luxembourg

A more diverse economy

Macroeconomic Overview

Economic growth decelerated slightly in 2015 compared to 2014; however, for 2016–2017 it is forecast to remain at around 4% per annum. What is more, this is much faster than the Eurozone, which is currently experiencing a period of sluggish growth. Whilst this economic expansion is driven mainly by the robust financial sector, the economy as a whole is becoming more diverse. Luxembourg's substantial exposure to the financial sector is becoming more diversified, as the Grand Duchy continues to attract new companies across the sectors.

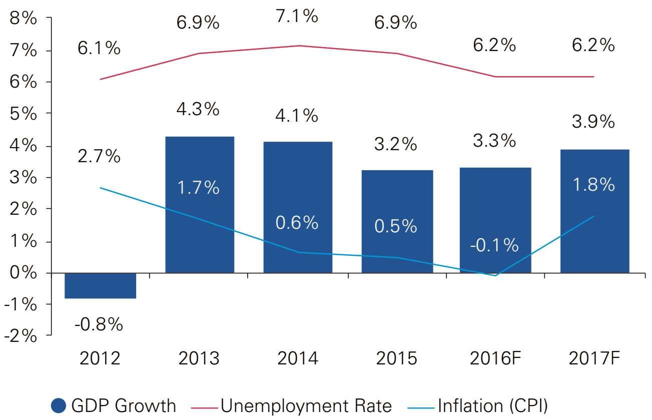
Unemployment is forecast to be around 6.2% in 2016, the same level as in 2015. However, a particular concern is unemployment at both ends of the age spectrum, with both younger (15–24) and older (55–64) workers suffering unemployment levels above the EU average. This implies that there are concerns about growth and fiscal sustainability, however, the trend is reversing.

Luxembourg is seen as a stable, diverse and dynamic economy, adjoining Belgium, Germany and France. Located at the heart of Europe, it benefits from excellent connectivity to markets across the EU and worldwide. Luxembourg exports around 80% of its output (mainly services) and enjoys solid macro economic fundamentals, including a Triple A credit rating from major rating agencies. Historically, the steel industry was the leading activity in its industrial sector.

Nonetheless, a transformation of its economic structure through time saw Luxembourg refocusing on financial services. More recently, the sector has also been complemented by telecommunications and IT services, especially start-up and Fintech companies. At present, the financial sector accounts for approximately 27% of GDP and has more than compensated for the decline in the steel industry.

Luxembourg

Economic Indicators



Source: Statec
F – forecast

Beyond the factors already highlighted, the economy's ongoing growth is based on resilient domestic demand and the dynamism of the financial sector. Being a small country, Luxembourg is substantially influenced by economic developments in the EU, and due to the low interest rate environment these have resulted in a significant boost to the country's funds industry, which is the world's second largest in terms of assets under management.

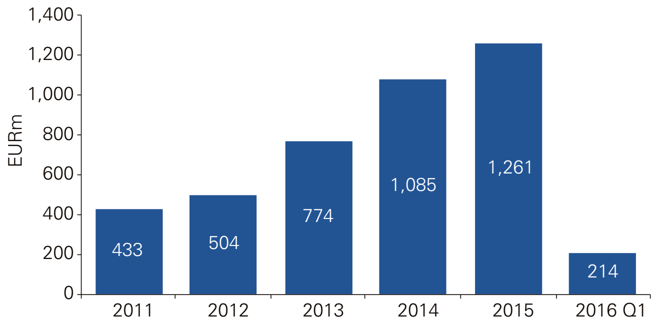
The predominance of financial activity may lead to potential vulnerabilities, but the sector's share of the overall economy may decline in the coming years. Nevertheless, the Grand Duchy has a solid strategy to sustain its future economic growth and fuel other economic sectors with current surpluses.

In common with other European countries, Luxembourg has recorded low inflation levels since 2012, but they are expected to rise closer towards the long term inflation target in 2017.

Office Market

Although, at EUR214m, the volume of investment in the office sector was lower in Q1 2016 than during the same period last year, this outcome is still positive once adjustments are made to allow for the mega deals that took place in 2015. The office market continues to benefit from the country's strong economic growth forecast and the increasing numbers of employees arriving there.

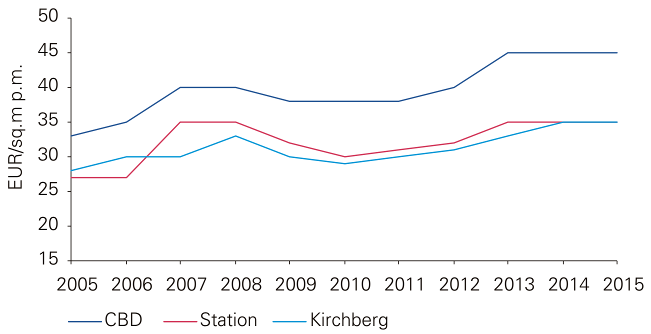
Office Investment Volumes



Source: Inovai

The larger lettings were attributable mainly to financial and legal service providers, such as BDO's new offices in Cloche d'Or (9,400 sq. m), ING's offices near the station (13,500 sq. m) and the BGL BNP Paribas building (>10,000 sq. m).

Prime Rent Evolution – Luxembourg-City



Source: Inovai

Prime rents in the CBD (EUR45.00/sq. m. p.m.) and Station area (EUR35.00/sq. m. p.m.) have remained stable over the twelve months to Q2 2016. In contrast, Kirchberg, which remains the most active in terms of ongoing office developments, has seen prime rental growth of around 6.1% Y-o-Y, and prime rents there currently stand at EUR35.00/sq. m. p.m.

Office Market Overview Q2 2016

Key areas	Vacancy rate	Yield Q3 2015	Rent (EUR/ sq. m. p.m.)	Stock (sq. m.)
Luxembourg City (CBD)	3.48%	5.0%	45.0	825,000
Luxembourg City (Station)	3.87%	5.1%	35.0	383,500
Luxembourg Kirchberg	1.83%	5.4%	35.0	1,026,500

Source: Inowai for Vacancy rate, Rent and Stock; Cushman and Wakefield for Prime yield

Going forward, it is expected that the shortage of supply of quality office space could generate some additional pressure on prime rents. Prime office yields have been close to their lowest levels for ten years. All three areas have recorded a decrease, 10 basis points for CBD and Station, and 40 basis points for Kirchberg.

Vacancy rates have risen to 4.9% in 2016 (compared to 4.3% in 2015), which conceals the fact that vacancy is much lower in the CBD and Kirchberg, whilst vacancy in Periphery is much higher, at up to 20% in some sectors. This is in contrast to the global trend for vacancy, which is one of stabilisation. Despite the increase in available office space resulting from completions of new office buildings in 2016, overall vacancy in Luxembourg's office sector remains amongst the lowest in Europe.

Of new office developments due in 2016, two stand out: Project Lighthouse One and Project Infinity. Lighthouse One, which is expected to open at the end of 2016, is a 14,000 sq. m 15-storey office building located in Kirchberg. Project Infinity is planned as a multipurpose building designed for residential/ retail use with 6,800 sq. m of office space planned for mid-2019, also located in the Kirchberg district.

Overall, prospects for 2016 are very positive. New take-up should reach 200,000 sq. m, with 132,000 sq. m of this expected to be delivered by the end of the year.

Retail Market

Even though the trend for retail sales has been downward in 2016, the retail occupier market was reasonably positive.

Limited supply in prime high street locations has resulted in a low vacancy rate. This has translated directly into Y-o-Y prime rental growth in Q2 2016 of 7.7% in high street and 1.8% in shopping centres. The Retail Market Overview table provides a snapshot of current rental trends in Luxembourg's main retail locations and how they are reflected in growth performance over one and five years.

Retail Market Overview Q2 2016

Key areas	Major retailers	Rent (EUR/ sq. m. p.m.)	Rent (EUR/ sq. m. p.a.)	CAGR 1Y (%)	CAGR 5Y (%)
Grand-Rue	H&M, Zara, Louis Vuitton	210.0	2,520	7.7	11.8
Avenue de la gare	Saturn, Veritas, Okaidi, WE	90.0	1,080	5.9	6.7
Luxembourg City	Various	19.0	228	–	–

Source: Cushman and Wakefield

On the supply side, there is a substantial number of shopping centre developments in the pipeline. These include the Infinity Project, which will provide scarce retail space in Kirchberg. In addition, the 16,000 sq. m Royal Hamilius development, Auchan Ban de Gasperich and the 5,000 sq. m extension of City Concorde are expected to be completed by 2018.

A 75,000 sq. m shopping centre project in Cloche d'Or has also appeared on the investment horizon. Moreover, the government is granting permits for new schemes, with a focus on expanding Luxembourg's retail parks.

Substantial retail investment opportunities remain limited, with only one high street deal concluded in Q2 2016. Yields in the principal high street locations have sharpened by around 15–20 bps since the same period last year. As at Q2 2016, the prime yield in Grand Rue is currently at 4.2%, whereas in Avenue de la Gare, it stands at 5.1%. This yield compression is also expected to continue in the short term, with fierce competition among investors whenever an investment opportunity arises.

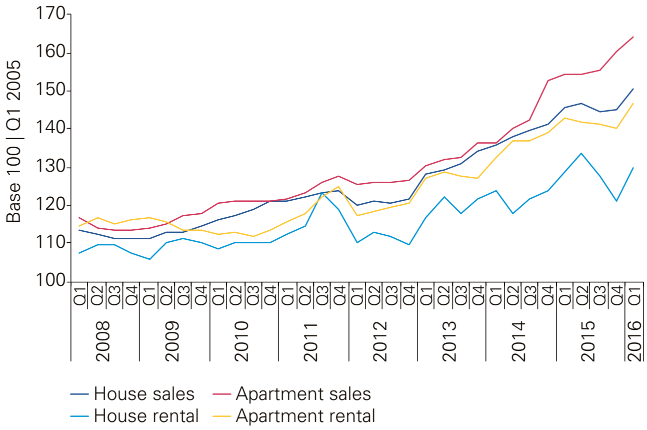
Luxembourg

Residential Market

Investment

In Q1 2016, registered sales transactions for existing accommodation disclosed a price increase of 3.1% Y-o-Y for houses and 6.3% for apartments, in line with previous years.

Prices Evolution of the Residential Market (Announced Prices Base 100 Q1 2005)

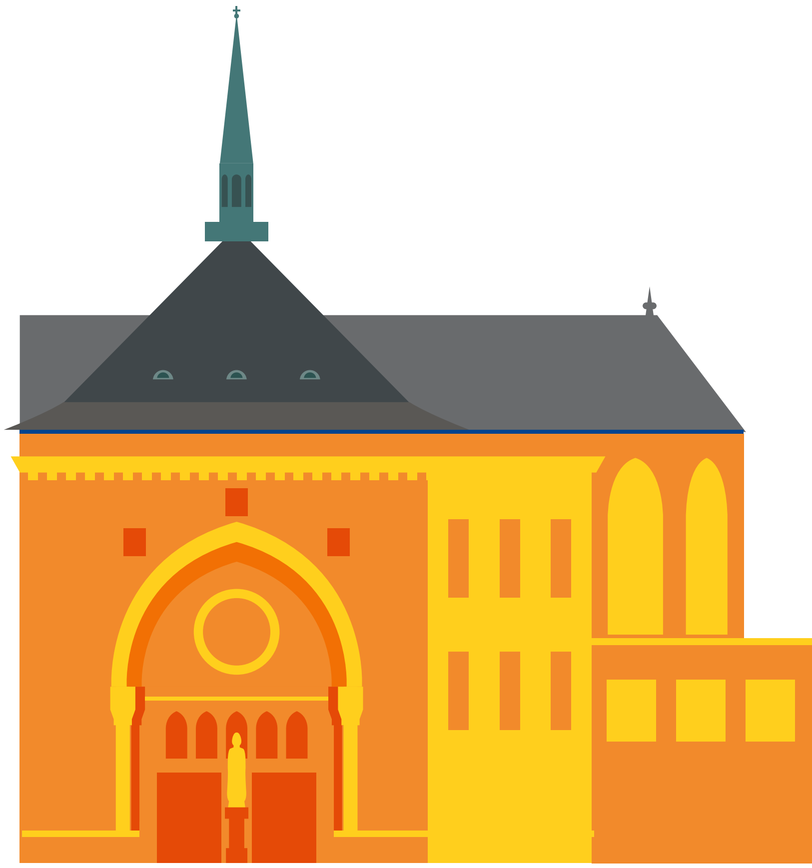


Source: Observatoire de l'habitat

The average price for houses in Luxembourg in Q1 2016 stood at close to EUR4,080/sq. m, whilst the price for apartments averaged EUR5,442/sq. m. When it comes to Luxembourg City, average prices were close to EUR5,405/sq. m for houses and EUR7,496/sq. m for apartments. The Y-o-Y price change for Luxembourg City was -5.1% for houses and 6.8% for apartments respectively.

Rental Market

Average asking rents during Q1 2016 in Luxembourg were EUR2,587 p.m. (EUR13.85/sq. m. p.m.) for houses and EUR1,429 p.m. (EUR20.36/sq. m. p.m.) for apartments. This represents an increase of 0.7% and 2.5% respectively compared to the same period in 2015. In Luxembourg City, rents were approximately EUR3,873 p.m. (EUR19.11/ sq. m. p.m.) for houses and EUR1,739 p.m. (EUR24.22/ sq. m. p.m.) for apartments. This represents an annual increase of 14.6% for houses and 1.6% for apartments. The average sizes of properties on the market were 187 sq. m for houses and 70 sq. m for apartments.



Focus on Digitisation

As mentioned previously, Luxembourg is endeavouring to capitalise on its success as a global financial hub with a view to taking on a leading role in the digitisation of this and other industries, in order to diversify the range of services that it provides. The country is exploiting its expertise as a European and global leader in Information and Communication Technology (ICT), Big Data management, the emergence of FinTech, e-commerce and the Internet of Things (IoT). These initiatives can be summed up in three major trends which affect the real estate sector in different ways.

Growth in FinTech and Start-Up Communities

At the end of 2014, the Luxembourg government set up an initiative to establish the Grand Duchy as the leading European FinTech and start-up hub in fields such as digital wealth advisory services, block-chain, big data, machine learning and smart contracts. Boosted by the favourable environment and governmental support, growth in these start-up communities may add further pressure to existing demand for new office and residential space.

Document Digitisation and Cloud Services

The growing trend towards the digitisation of corporate archives and documents brings opportunities and challenges in its own right. First, it allows for more efficient use of space in existing office buildings by minimizing the use of physical storage facilities for paper archives. Secondly, it brings a challenge in terms of digital data storage, cloud computing and data centre capacity which the country handles with its ICT infrastructure. As at 2016, 27 data centres are in operation in Luxembourg, the majority of which offer Tier III and IV design service levels. This is an increase of 33% since 2013. This number is expected to grow further, in order to meet ongoing demand for accommodation of this type.

Growth of the E-Commerce Sector

The internet, mobility, social networking and the rise of price comparison websites have changed the game over the past decade and have created a new generation of customers who demand simplicity, speed and convenience for their retail and leisure experience. The transparency of offerings and prices enabled by the internet has consequences – more than ever before it is the customer who dictates the trend. In the past three years, e-commerce in Europe has been growing by an average 12–13% per annum, and it is expected to reach EUR500bn in 2016. This industry requires heavy logistical support to handle optimised shopping processes.

According to official statistics, in Luxembourg:

- 93% of people use the Internet;
- 78% of shops have an online presence;
- but only 7% sell online.

In this very competitive environment, the retail industry has begun adapting to allow digital services to be integrated into existing trading formats. It is expected that physical retailers may face challenging times ahead given the speed of the growth of the e-commerce sector. However, as Luxembourg's retail scene is supported by a stable economic environment and steadily growing consumer confidence, it is not expected that physical retailers will be heavily impacted, especially in prime high street locations.

Moreover, Luxembourg is ranked number two in the Global Logistics Performance Index. According to the World Bank, due to the country's strategic geographic location and support through air and rail cargo as well as river freight, the sector is expected to grow further with the help of positive government support. This may allow for yet further developments in the logistics real estate sector on top of the current growth in the presence of Third Party Logistics sector occupiers.

France

Take-up volumes boosted by strong demand from large companies

Macroeconomic Overview

Flat GDP Growth disappoints in Q2

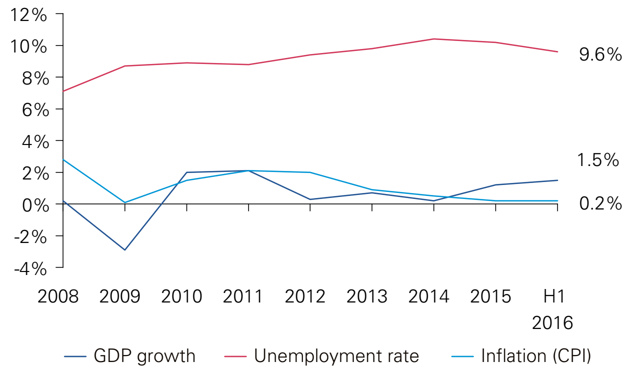
The French economy appeared resilient during Q1 2016, which emerged as a real upturn according to INSEE (revised GDP growth of +0.7%), especially bearing in mind the climate of uncertainty and insecurity resulting from terror attacks in the country since the end of last year and the increased volatility on the financial markets at the start of 2016.

Nevertheless, growth stagnated in the second quarter of the year, a disappointing figure after INSEE had forecast growth of 0.3% for the period. This poor outcome was triggered in part by strikes resulting from unpopular labour market reforms.

French GDP growth is expected to rise to 1.6% in 2016, due mainly to low commodity prices, reduced energy prices, cuts in labour and business taxes and sustained low interest rates.

The unemployment figures are showing a positive trend, with the number of unemployed dropping below 10% of the total population, boosted by lower social security contributions and new subsidies for taking on staff.

Economic Indicators



Source: INSEE

Despite tax cuts, the impact of lower debt servicing costs and spending restraints should be to bring the fiscal deficit down to 3% of GDP in 2017. This will limit further increases in public debt, while minimising risks to the still fragile recovery. To fight high unemployment, the authorities announced new hiring subsidies for small and medium-sized firms and up-scaled training measures for jobseekers. A draft labour market reform clarifies conditions for dismissals for economic reasons and allows more freedom for negotiations at company level, mainly concerning working time.

Borrowing costs continued to fall during the first half of 2016, boosting investment volumes.

The 3M Euribor rate remains negative (at -0.29% as of 1 July 2016) and the 10-year T-Bond ('OAT') hit an all-time low of 0.21% as of 30 June 2016, despite the announcement of the UK's decision to leave the European Union on 23 June 2016; they are both likely to reach 0.1% by the end of the year.

Following the 'Brexit' announcement, the initial forecast for 2017 growth was revised downwards from +1.7% to +1.0%, in view of the uncertainty surrounding the impact of this event.

Investment Market

The Investment Market accelerates in Q2

With the 10-year T-Bond bearing a 0.21% coupon at the end of the first half of the year, real estate has maintained its appeal compared with other investments, confirming the favourable risk-return outlook for this asset type.

During the first half of the year, EUR8.7bn was invested in commercial real estate in France. Office property remains the most important market segment in France, with the Greater Paris area still the most attractive location for investors, representing 72% of overall investment. Retail is the second most preferred asset type, with just over 20% of the total amount invested (+53% compared to the same period in 2015); logistic properties continue to attract more investors, showing a 17% increase in total volume Y-o-Y to around EUR560m, thanks to portfolio acquisitions by players from English-speaking countries.

As in 2015, investment volumes are being driven by large transactions with two transactions in particular: the acquisition by AXA and ACM of the 'First' tower (office building) in La Défense, Paris for a total sum of around EUR800m and the disposal by Meyer Bergman and Thor Equities of 65, avenue des Champs-Élysées (retail including the Tommy Hilfiger shop and offices on the upper floors) for a total price EUR490m. Therefore, although there were fewer large transactions than last year, the total amount invested has remained at a very good level (down slightly at EUR8.7bn compared to EUR10.1bn during the same period in 2015).

With a combination of high liquidity levels and a limited supply of core assets, prime yields are still contracting, reflecting fierce competition for the best assets in the best locations.

Office Market

Offices still the preferred Asset Type

Investment in office assets decreased for a short period during Q1 2016 before picking up in Q2 2016. At the end of H1 2016, they represented 56% of the total amount invested in CRE, compared to 53% in H1 2014 and 2015. It is worth highlighting the number of transactions, which has reached a level close to that of the highly dynamic H1 2007, just before the subprime crisis, when there were 137 transactions (compared to 110 in H1 2015). The two main transactions were the JV purchase of 2-8, rue Ancelle in Neuilly-sur-Seine (in the west of Paris) by Amundi and ACM from French REIT Unibail-Rodamco for EUR272m and the 'First' tower deal mentioned previously. In spite of a sluggish start, volumes are expected to rise to the same level as in previous years, underpinned by transactions in the pipeline (in particular, CBX Tower in La Défense). Overall, 13 transactions for more than EUR100m were recorded in the first half of the year, due almost exclusively to local investors. Office prime yields have compressed by 25 bps in the second quarter of the year and stand at 3.25% as at H1 2016.

The good level of transactions in Paris Centre West district was bolstered by three speculative forward purchases ('ORA', 'Themis' and 'lot N5', 3 projects in or close to the ZAC Clichy-Batignolles in the 17th Arrondissement) and the sale of 17 Matignon in the CBD.

It is worth noting that the La Défense investment market, historically quite volatile, was very active in the first 6 months of the year, with a total volume invested in excess of EUR1bn (five transactions) – the start of a series of disposals of tower blocks which are expected to be transacted this year. As at H1 2016, prime yields here stand at 4.25%.

Prime Office Yields

		Q2 2016	Q1 2016	Q2 2015	10 Year High	10 Year Low
Paris	CBD	3.25%	3.25%	3.75%	5.75%	3.25%
	Rive Gauche	3.75%	3.75%	4.25%	6.25%	3.75%
	La Défense	4.25%	4.75%	5.25%	6.75%	4.50%
Provincial	Lyon	4.80%	4.80%	5.25%	7.00%	4.80%
	Other	5.50%	5.50%	5.50%	7.25%	5.50%

Source: Cushman and Wakefield

Positive trends on the occupier market are also helping to make this asset type attractive to investors. In Greater Paris, following a dynamic Q1 2016 with take-up of more than

France

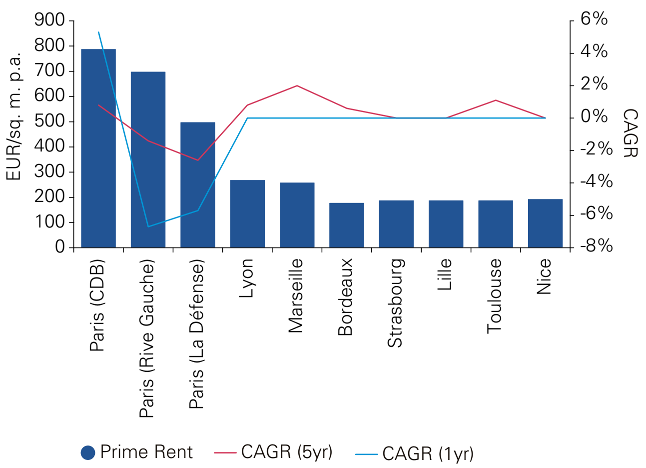
525,000 sq. m, the rising market trend has continued over the second quarter with take-up of almost 615,000 sq. m, a 20% increase compared to the same period last year and equal to the 10-year average.

This performance reflects a sustained level of activity in all size categories. The main point to emphasise is the level of demand from large companies. This market segment recorded some 30 transactions accounting to 380,000 sq. m. Two transactions of more than 25,000 sq. m were recorded during Q2 2016: the pre-letting by Saint-Gobain of 'M2' tower in La Défense (49,000 sq. m) and the acquisition of the 'Qu4drans – East' office building in Paris's 15th Arrondissement by Altice (owner occupier). This was in addition to the letting by Deloitte of 31,000 sq. m in the 'Majunga' tower in La Défense, concluded during Q1 2016.

At EUR750 sq. m p.a., the prime rent in the Paris CBD remains steady compared to H1 2015 and H2 2014. The prime rent in La Défense has decreased slightly over the years, to EUR520/sq. m p.a. (-1.1% over the past five years).

In the regions, prime office rents remained stable in H2 2015, except for Marseille, where the redevelopment of entire districts such as Euroméditerranée is boosting the city's attractiveness.

Prime Office Rents



Source: Cushman and Wakefield

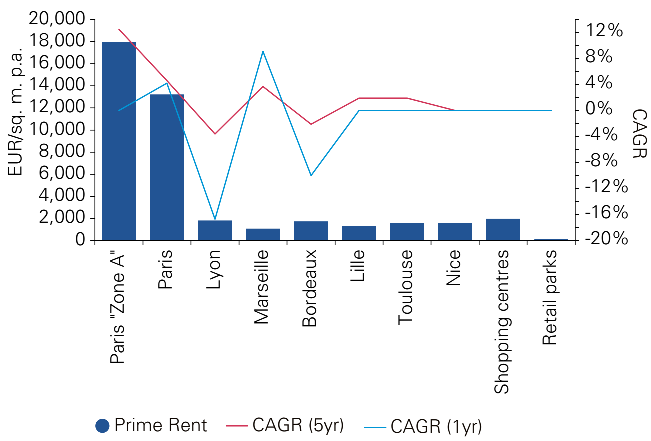
Retail Market

Confidence still high

Despite the impact of terrorist attacks on consumer morale, French consumer spending and household consumption demonstrated their resilience in Q2 2016. Rising purchasing power, strong demand and a steady supply of new developments and redevelopments highlight a comparatively positive mood.

Prime locations continue to be sought after by occupiers, with demand underpinned by new entrants, secondary expansion by recent arrivals and the repositioning of established retailers.

Prime Retail Rents for High Street Shops



Source: Source: Cushman and Wakefield

The French retail market continues to attract positive attention from international brands, with new entrants in food and beverages (Five Guys, Shake Shack, etc.) and fashion (Victoria's Secret, New Balance, Club Monaco etc.) continuing to invigorate letting activity.

We are also currently seeing existing occupiers undertaking expansion projects. These include Primark, Chipotle, Asics, Alexander McQueen and many others.

The vacancy rate is zero on the most prestigious city centre axes. Recently vacated premises in rue Saint-Honoré in Paris were easily let in 2016, with 13 occupiers opening, including Stella McCartney, Brioni and Paul Smith.

In Q2 2016, investment in retail (approx. EUR1.9bn) increased Y-o-Y, accounting for 22% of all property investment in France. At EUR1.1bn (+33% Y-o-Y), transactions in Île-de-France accounted for 58% of total retail investment in France.

Five acquisitions for more than EUR100m were recorded in the second quarter alone, totalling EUR730m (one in the city centre and three in the periphery). Volumes were boosted by the sale of 65-67 avenue des Champs-Élysées to a Middle Eastern investor, confirmation that the Paris region remains the leading market for foreign investors (70% of foreign investment is in the Paris region). Also, retail in the periphery has attracted more than EUR780m in the first half of the year thanks to large portfolio transactions (including the Pearls portfolio of regional outlet stores and the Octave portfolio of retail parks).

Demand for retail assets exceeds supply, maintaining pressure on prime yields. Indeed, prime yields for trophy assets are often falling below 3% in the heart of Paris. The same trend is being witnessed with the best shopping centres, with transactions at around 4.25%, and the best retail parks, at around 5%.

Prime Retail Yields

		Q2 2016	Q1 2016	Q2 2015	10 Year High	10 Year Low
High street retail	Paris	2.75%	2.75%	3.00%	5.00%	2.75%
	Lyon	3.75%	4.00%	4.50%	6.25%	3.75%
	Marseille	5.00%	4.75%	5.00%	6.25%	4.75%
	Bordeaux	4.00%	4.25%	4.75%	6.25%	4.00%
	Lille	4.25%	4.25%	4.75%	6.25%	4.25%
	Toulouse	4.25%	4.25%	4.75%	6.50%	4.25%
	Nice	4.25%	4.25%	4.75%	6.25%	4.25%
Shopping centres	Paris Region	4.00%	4.00%	4.25%	5.50%	4.00%
Retail parks	Paris Region	5.00%	5.00%	5.50%	7.25%	5.00%

Source: Cushman and Wakefield

Residential Market

Revitalised by favourable Financing Conditions

In 2015, strong growth was seen in the granting of new loans for residential property, with a total of EUR202bn (+64% Y-o-Y) of new loans granted to private individuals. Until now, 2016 has seen a continuation of this bullish momentum, with EUR201bn of loans granted over the last 12 months. Interest rates remains attractive, at an average of 2.04%.

According to the banks, demand for credit is still on an upward track. There has been a simultaneous lengthening in the duration of loans: the proportion of loans with 25-year plus terms has jumped from 15% in 2014 to more than 20% at the end of Q2 2016.

New Homes

New construction has increased with 353,000 units under construction over the past 12 months as compared to 350,000 units in 2015.

The number of building permits granted increased by 7% Y-o-Y.

Prices have risen slightly: the average price of a new apartment in France is up, at EUR3,925/sq. m as of H1 2016 (compared with EUR3,887/sq. m at the end of 2015). As with the market for existing homes, there are significant discrepancies in prices between regions: in Bourgogne-Franche-Comté, the average price stands at EUR3,000/sq. m, whilst it is reaching EUR10,710/sq. m in Paris.

Price Variation for Second Hand Homes

	Flats Q1 2016 on Q4 2015	Flats Q1 2016 on Q1 2015	Houses Q1 2016 on Q4 2015	Houses Q1 2016 on Q1 2015
France	0.3%	(0.2%)	1.0%	1.1%
Paris region	(0.1%)	–	0.9%	0.6%
Provincial	0.6%	(0.4%)	1.0%	1.2%

Source: Notaires de France and INSEE

Existing Homes

In 2015, sales of existing homes increased by 16% compared to 2014, with 802,000 units sold; a return to the 2000-2007 average. So far, the trend seems to be confirmed, with 818,000 units sold over the last 12 months. This very good performance is explained mainly by the very low cost of borrowing: these very favourable current financing conditions are increasing the real estate purchasing power of French households (+15% between 2011 and 2016).

A consequence of this good performance of the market is a slight increase in prices: for the first time since the beginning of 2012, prices (apartments and houses) increased by 0.5% during Q2 2016. The cumulative decline of prices between 2011 and 2016 had reached 6.3%.

On the rental market, rents have risen slightly since the start of the year after the fall recorded in 2015. In Paris, the average rent stands at EUR25.00/sq. m. In the big cities, which include Lyon, Marseille, Lille, Toulouse and Bordeaux, rents range from EUR9.10/sq. m (in Limoges) to EUR15.40/sq. m (in Nice).

France

Focus on Digitisation

Real estate has always been about concrete, physical and palpable buildings. Not any more, one could say! Nowadays, it does not seem to be a contradiction to mix it with the abstract and intangible internet.

Real estate does indeed possess two characteristics that can benefit from digitisation: it represents a valuable investment and it involves complex processes. Changes are afoot in the architecture, engineering and construction industry, always information-intensive and formerly document-centred. Owners and occupiers of buildings are adapting their behaviour too. The real world is now making increasing use of the virtual world in order to become more relevant and efficient, and therefore higher-performing and more profitable and competitive.

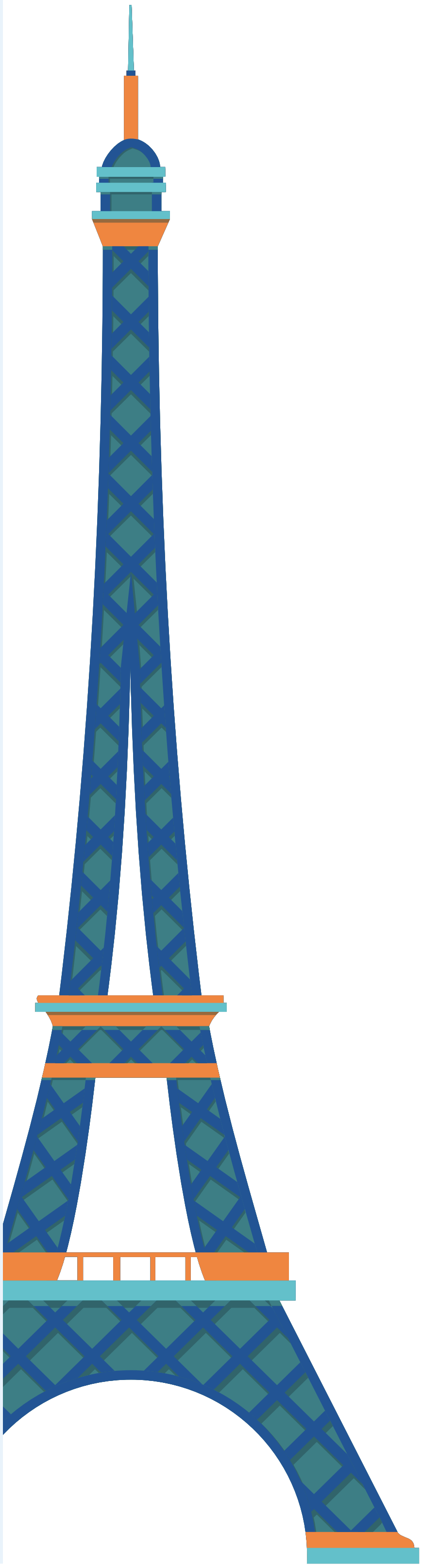
This revolution includes strategic aspects of portfolio planning and investment and also operational aspects of the procurement, provisioning, management and marketing of properties.

- For occupiers, the biggest change will be the 'Uberfication' of commercial real estate: from the way people search for new premises (cartography, 3D asset tour, virtual reality…) to the way buildings are actually used to bring them more into line with the occupier's needs (energy consumption, smart buildings…).
- For owners, it's all about the speed at which they can access the data needed to give commercial real estate players a solid decision-making foundation. The emergence of BIM, combined with the increased use of mobile devices, is placing a new emphasis on data (and more of this is structured data).

In the future, digitisation of the real estate industry will continue to move in innovative directions: smart cities, Big Data, Open Data, crowdfunding, and the shared economy. In fact, this has already started with more and more business incubators putting an emphasis on real estate professionals.

In France, we are seeing many dedicated start-ups aiming at seizing the first-mover advantage, and the largest real estate companies are now integrating this into their overall strategy, clearly aiming at improving transactions and processes, and aggregating and sharing information.

The retail sector has taken the lead as illustrated by initiatives such as the joint project by Unibail Rodamco and NUMA in launching the incubator UR Link, dedicated to start-ups aiming to transform retail. This structure has led the way in this new segment, creating tomorrow's retail.



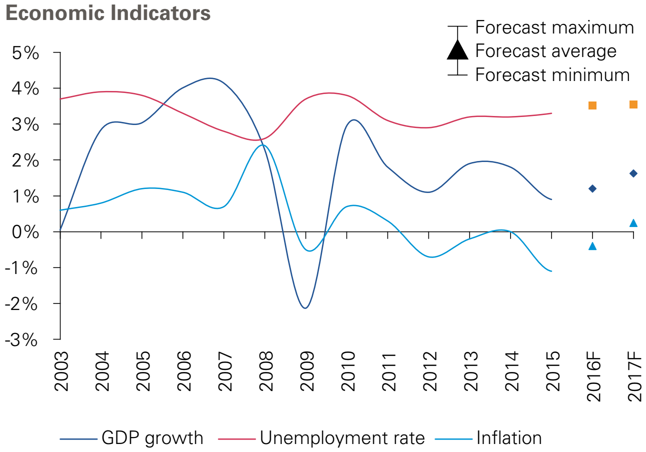
Switzerland

Sustained capital flow driving real estate investment

Macroeconomic Overview

The State Economic Secretariat (SECO) has estimated growth of Swiss Gross Domestic Product in Q2 2016 at 0.6% in real terms. Positive impetus came from foreign trade and government spending. Meanwhile, consumer spending by private households stagnated. There was even a slight fall in investment in construction and equipment. Various economic indicators point towards a sustained positive trend in the world economy this year and next. In this positive but fragile environment, the Swiss economy should grow by 1.2% in 2016; real growth of 1.6% is expected in 2017.

Economic Indicators



Source: BAKBasel, Credit Suisse, KOF, SECO, UBS and KPMG
F – forecast

In view of the somewhat higher oil price and the fading effect of last year's revaluation of the franc on import prices, it should be assumed that the phase of negative price growth will come to an end in the next few months. Average inflation in 2016 should once again be in negative territory, at -0.4%. For 2017, the signs are that inflation will be positive again, at 0.2%.

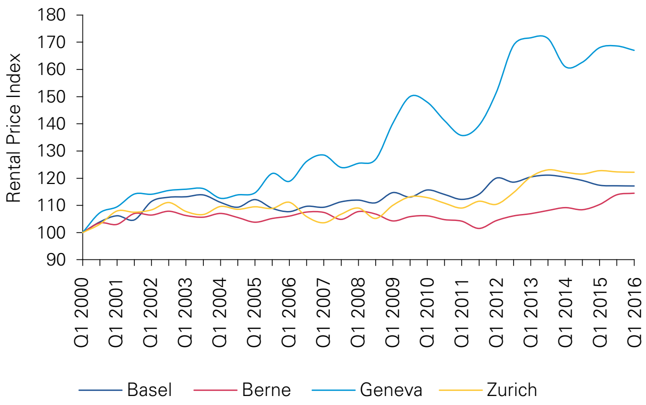
Office Market

Notwithstanding overcapacity in some regions, plenty of capital is once again flowing into the development of new office space. According to Credit Suisse, whilst there has been a reduction in the number of applications and approvals for the construction of new office premises since the highs of 2011 and 2012, it is still above the average for the period since 1995. In April 2016, the total construction cost of office space for which approval had been granted was just about CHF2,100m, whilst that for applications was nearly CHF2,600m. Such high levels of applications have been seen only rarely in recent years.

Switzerland

Asking rents for office space rose by 1.6% between the mid-point of 2015 and the mid-point of 2016. However, the reason for this is mainly improved quality and the numerous upgraded premises on offer. It can be seen that asking rents for office premises have largely moved sideways since the start of 2014.

Asking Rents for Office Space in the Principal Centres



Source: W&P and KPMG

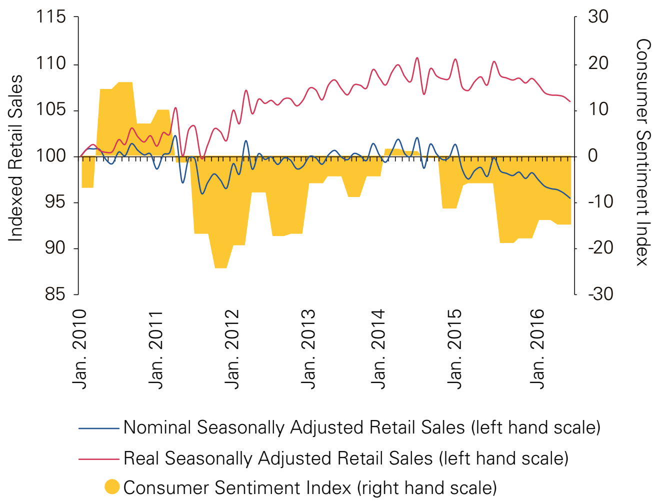
Apart from slow-moving supply, stagnating demand and political uncertainties, the market for office space is facing structural challenges. New workplace concepts, digitisation and co-working space are only some of the issues which are accentuating the already acute competition for space. In such an environment, older premises often no longer meet modern requirements, and increasingly they are feeling the squeeze from qualitatively better space in new buildings. This structural transformation suggests that the higher vacancy rates are not just a temporary phenomenon, but rather that they represent a new paradigm, which the market is going to have to get used to. The previous tight, dense office market is turning into a more open and expansive market, with increased competitive pressure.

Retail Market

Retail sales and consumer sentiment in Switzerland remain low. Whilst consumer sentiment remains relatively stable, at around -15 points, the declining trend in retail sales since the abolition of the euro exchange rate mechanism at the start of 2015 is continuing, albeit in an attenuated form. In the first half of 2016, retail turnover fell by 1.7% and 2.0% respectively in real and nominal terms.[1]

Shopping tourism and ordering abroad is causing headaches for the whole sector. These two factors, amongst others, explain why retail turnover has fallen despite an increase in purchasing power of 1.5% in 2015 (based on real salaries) and stable nominal purchasing power in H1 2016 (BFS estimate: +1.0% compared to H1 2015).

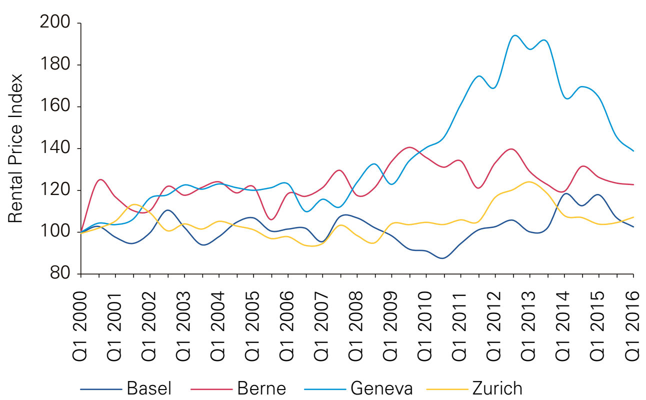
Retail Sales and Consumer Sentiment



Source: BFS, seco and KPMG

Nor has the retail space market escaped the effects of the fall in turnover. Asking rents for retail space in the principal economic centres of Basel, Bern and Geneva have fallen since the start of 2015 (Basel: -12.9%, Bern: -2.8% and Geneva: -4.9%). This trend has also continued in H1 2016 (Basel: -4.2%, Bern: -0.6% and Geneva: -4.9%). It is only in Zurich that asking rents increased slightly in H1 2016, by 3.2%.

Asking Rents for Retail Space in the Principal Centres



Source: W&P and KPMG

[1] The difference between the development of retail turnover in nominal and real terms is calculated from the fall in the prices of everyday products.

Residential Market

With yields at a substantial premium compared to highly rated fixed-interest bonds, investing in real estate remains attractive. The residential sector is viewed by players in the market as particularly attractive. Not even rising vacancies are currently stopping investors from developing numerous residential construction projects. The low interest rate environment and the resulting investment crisis leave them with hardly any alternative. Consequently, a lot of capital is flowing into the residential housing market. According to Credit Suisse, applications for building consents reached a new record between May 2015 and April 2016, at over 30,500 rental units. Meanwhile, consent was granted for at least 26,700 rental homes in the previous 12 months. This further intensifies the emerging risk of oversupply.

The high construction output in the residential sector has already made itself felt in increased levels of vacancy. According to BFS, on 1st June 2016, 56,518, or 1.30% of all homes, including detached houses, were empty. There were 5,436 more homes empty than last year, equivalent to an increase of 11%. The number of vacant homes has reached a level last seen at the turn of the millennium. Since its low point in 2009 (0.90%), the number of vacant homes has been growing continuously year on year, but the trend has accelerated particularly in the past three years.

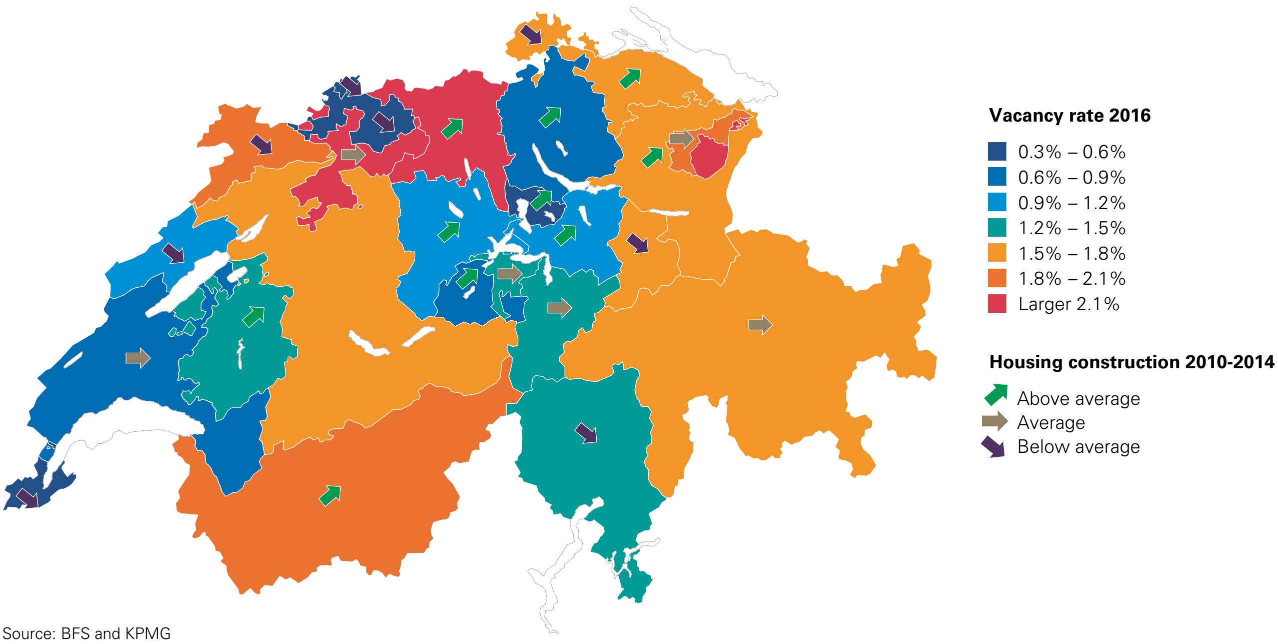
When this is broken down into rental and freehold homes, it can be seen that the increase is particularly high in the case of rental homes. The stock of vacant rental homes has risen by 5,391 units, or 13%, since last year. We estimate that the vacancy rate in this segment stands at around 2% across Switzerland as a whole.

This buoyant construction rate will have a dampening effect on rental growth. Until the mid-point of 2015, quality-adjusted asking rents[2] for rented homes were increasing by around 2% per year. In recent months, this rental growth has come to a complete standstill. The trend towards slower rental growth is affecting just about every region, and geographical differences are becoming smaller. For Switzerland as a whole, in August 2016 the annualised increase in rents was recorded at just 0.1%. Rents even fell in four of the nine regions covered by the index.

Overall, we anticipate that rents will remain stable across Switzerland as a whole. However, negative movements in asking rents can be expected in the expensive regions and for homes with a high fit-out standard.

[2] The Index measures the monthly quality-adjusted change in rents of new homes and homes available for reletting.

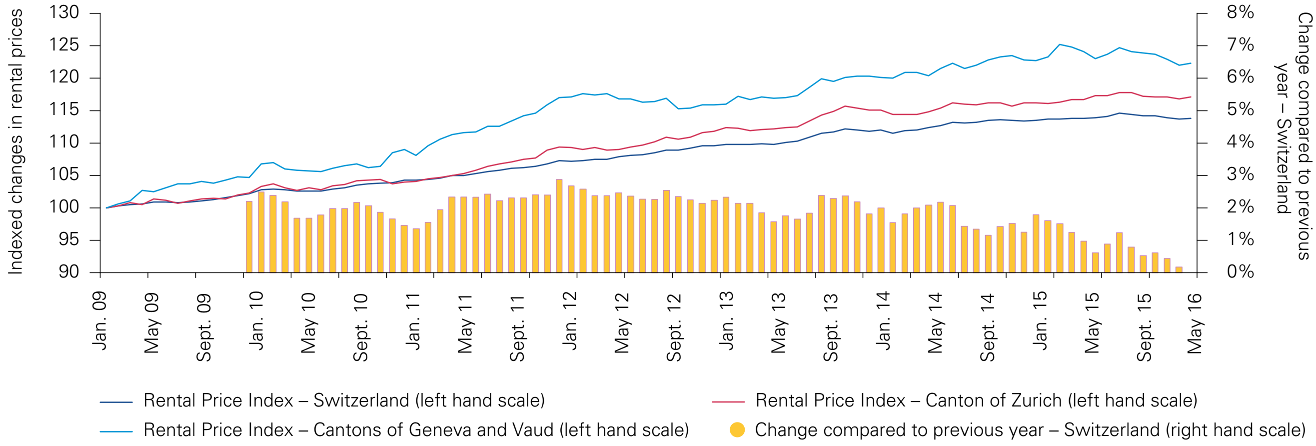
Residential Vacancy Rate and Construction Activity



Source: BFS and KPMG

Switzerland

Asking Rents Index, quality-adjusted



Source: Homegate.ch, ZKB and KPMG

Focus on Digitisation

For about a year, the topic of digitisation has been on everyone's lips in the Swiss property sector. This can be seen clearly in the media's response to digitisation in the sector. Whilst only two articles appeared on the topic in the mainstream press in 2014, in 2015 there were 13 and in the first half of 2016 there were as many as 18. So, the property sector is only at the start of this change. In many places, digitisation is only now being discovered and uncertainty surrounding the effects of technological transformation remains high.

Currently, discussion is largely around the emergence of systems and applications such as the "Internet of Things" (IoT), portal-based building information management (BIM), wearable computing, cloud-based solutions, virtual and augmented reality, 3D printing, big data analytics, intelligent energy networks and storage systems and cognitive technologies. What all these systems have in common is that they are based on technologies which are already available now and that they are being marketed with increasing success. These changes are impacting on demand for space. In industry (robotics systems and 3D printing), retail (online distribution and big data) and even in logistics (intelligent delivery systems and high volume storage facilities), advances in digitisation mean that less space will be required. However, at present the impact on statistical data is partly obscured by the current effects of population growth, increases in space per person and the growing flow of goods.

Austria

Benefiting from favourable economic conditions

Macroeconomic Overview

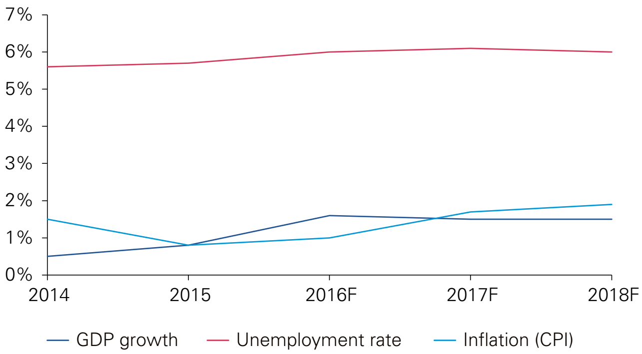
In its current forecast, the Austrian National Bank (OeNB) anticipates moderate growth in the Austrian economy. Whilst economic growth has consistently been less than 1.0% over the past four years, this year the economy is expected to grow by 1.6%. This can be attributed to two specific domestic factors, in particular the tax reform and what is assumed to be deficit-finance expenditure on asylum seekers and recognised refugees.

For the years ahead, a GDP growth rate of around 1.5% is expected.

According to the harmonised consumer prices index, inflation for 2016 is expected to be 1.0%, due mainly to low oil and commodity prices. However, it is expected that inflation will rise to 1.7% in 2017, and 1.9% in 2018.

The unemployment rate is forecast to stand at 6.0% in 2016. As in recent years, trends in the labour market during 2017 and 2018 are expected to be marked by a sharp rise in labour supply. In addition to recognised asylum seekers and other migrants, a growing contribution by older people and women will have a positive effect on labour supply. Despite strong employment growth, the unemployment rate is expected to rise to 6.1% in 2017, and only a slight reduction to 6% is expected in 2018.

Economic Indicators



Source: Austrian National Bank
F – forecast

Austria

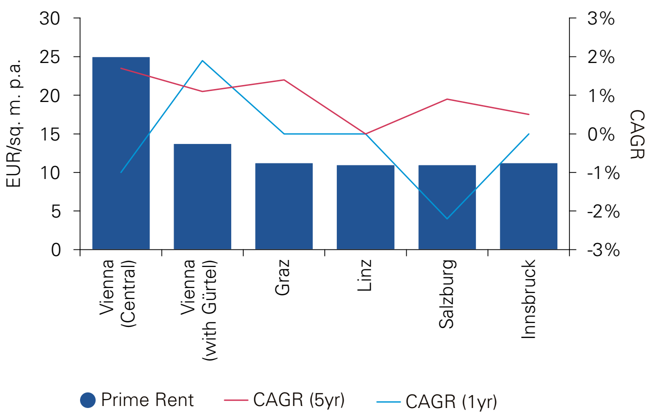
Office Market

The Vienna office market is showing signs of increased activity in 2016. With several new lettings larger than 1,000 sq. m in the first quarter, and concrete negotiations with large potential buyers, positive opportunities are opening up for the Vienna office market.

Another indicator for improvement in the office market is that average rents have increased for the first time in years. In 2016, rents stood at EUR14.00/sq. m. p.m., compared to EUR13.50/sq. m. p.m. in previous years. Average rents are expected to rise further over the medium term because new space coming to the market in 2017 will be offered for between EUR15.00 and EUR20.00/sq. m. p.m.

Completions of new space will fall to a record low in 2016, totalling only 60,000 sq. m, of which approximately 90% are owner-occupied or pre-let. As a result, the vacancy rate has dropped to 6.4% and is expected to decline even further. The highest vacancy rates are seen in older buildings with poor transport connections and a poor location. A large portion of this space is not being modernised but will be converted to residential use (apartments, student residences, hotels, etc.) in the near future.

Prime Office Rents



Source: Cushman and Wakefield

In 2017, approximately 150,000 sq. m of new office space is expected to be constructed, and these will be occupied by many companies planning to relocate.

Retail Market

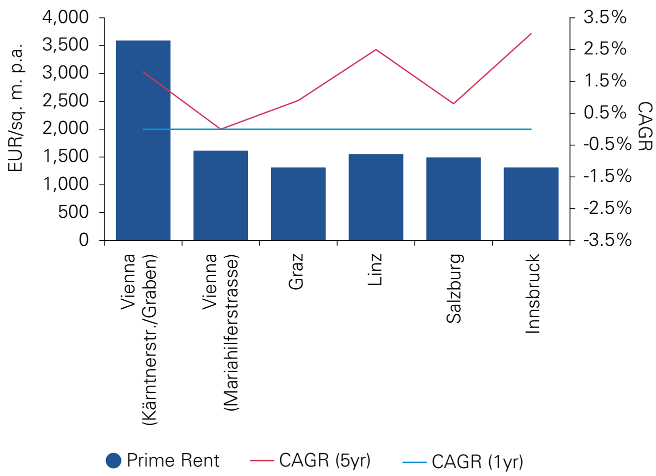
The positive economic trends are benefiting retail sales, which rose by 2.2% Y-o-Y in May 2016. According to a recent survey of retailers from America, Asia and EMEA, Austria ranks in seventh place amongst European countries as a global expansion target.

Whilst the revitalisation of Mariahilfer Strasse was finally completed in 2015, the redevelopment of Herrengasse in Vienna's first district into a low traffic pedestrianised area commenced in May 2016. The expected completion date is set for November this year. Restoration work is also underway in other areas in Vienna, including the area around St. Stephen's Cathedral, Churhausgasse and the links to Schulerstrasse, Rotenturmstrasse and Brandstätte. Prime rents for high street retail premises in Vienna stand at between EUR300.00 and EUR400.00/sq. m. p.m. Prime yields for high street shops are around 3.4%.

The first quarter of 2016 saw the opening of two major shopping centres: the newly constructed "huma eleven" (approx. 30,000 sq. m) in the 11th District of Vienna and the expanded "Traisenpark" in St. Pölten (approx. 13,500 sq. m). Prime shopping centre rents stand at around EUR115.00/sq. m. p.m. Prime shopping centre yields are around 4%.

Turning to retail parks, the level of completions in 2016 is expected to be relatively low. Prime rents for retail parks have remained relatively stable at approximately EUR14.00/sq. m. p.m. Prime yields for retail parks are around 5.9%.

Prime Retail Rents (High Street Shops)



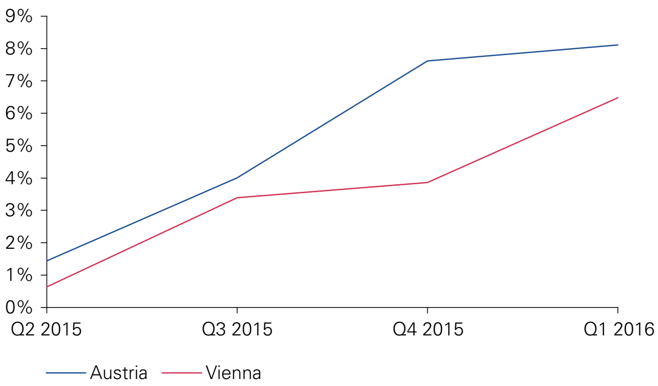
Source: Cushman and Wakefield

Residential Market

The trend of rising prices in Vienna's residential market is continuing. Buyers were very active in the first half of 2016. On the one hand and against a backdrop of low interest rates, many investors are attracted by the stability of the residential sector. On the other, it is possible that a number of institutional investors will take advantage of the current high prices to sell some of their properties, thereby increasing supply on the market. 2015's transaction volume of EUR1.35bn is likely to be surpassed in 2016.

In Q1 2016, prices for detached houses and condominiums in Austria rose by around 8.1% compared to Q4 2015. The comparable figure for Vienna is 6.5%.

Price Change of Single-Family Houses and Condominiums



Source: Austrian National Bank

Compared to Q2 2015, in Q1 2016 rents rose by around 6.0% in Vienna, compared to approximately 5.0% in the rest of Austria.

Focus on Digitisation

Experts agree that digitisation will dominate and revolutionise the real estate market. Digital transformation includes the optimisation of current IT systems and reports, the increased use of mobile applications and the growing use of virtual workspace.

The major benefits of digitisation are:

- Transparency
- Improved data quality
- Time and cost savings in planning, construction, operation and exit
- Risk reduction

IT interconnectivity between property companies and their customers, suppliers, specialist workers and service providers is playing an essential role in harmonising system interfaces and achieving these advantages.

Efficient tools for data analysis and evaluation are playing an important role in coping with the growth in available information, and are helping with further improvements in transparency.

Austria started digitising its land registry as long ago as the 1980s. This meant that land registry extracts were gradually becoming available within seconds. All documents archived since 2006 are available online, including purchase agreements, mortgages, etc. Older deeds such as partition deeds that cannot be scanned, need to be inspected where they are held.

The last amendment to the land registry legislation took place in 2012, and this additional step made provision for the digitisation of partition deeds.

This digitisation process led private companies to create portals which provide convenient user-friendly access to those federal databases via a single platform. For example, digitised purchase contracts can be used as a basis to evaluate all real estate transactions in Austria and can provide a geographic overview of the results. This eases the search for comparable transactions and significantly increases transparency. Additional services include demographic and infrastructure-related data by region, prepared at micro-grid level.

This has been developed to a point where property valuations and reports based on comparable transactions can be created within seconds.

Italy

Confidence continues to strengthen

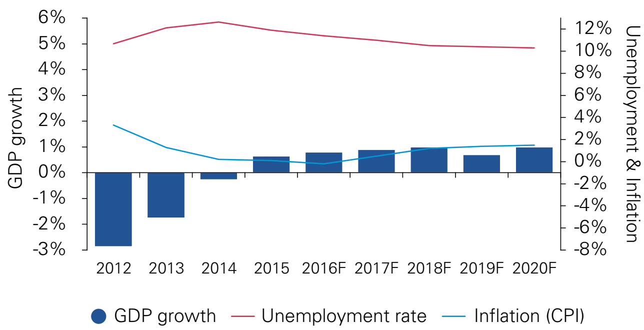
Macroeconomic Overview

After three years of recession, a slow recovery started in 2015 and is expected to strengthen in 2016, with interesting figures expected for 2017. However, there are still downside risks on the horizon.

According to preliminary estimates by ISTAT (National statistics office), Italy's GDP remained flat between Q1 and Q2 2016. However, based on the data for the first half, GDP growth for the full year will come in at 0.8% if activity remains flat in the second half.

The combined effect of low inflation, expansionary fiscal policies and gradual improvements in the labour market are offering some support to consumers in the second half of the year. On the other hand, the short-term outlook for the sector is unclear.

Economic Indicators



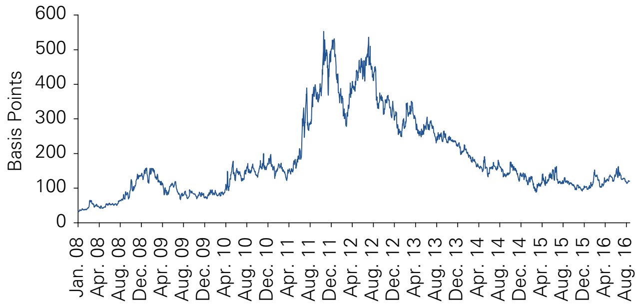
Source: The Economist Intelligence Unit, August 2016
F - forecast

Domestic household consumption spending is expected to grow by 1.4% in 2016. Positive employment trends and an increase in wages, accompanied by a strong reduction in prices, are expected to underpin household purchasing power.

Labour market conditions are expected to improve further in the coming quarters, with employment increasing by 0.8% in 2016. At the same time, the unemployment rate will fall to 11.3% in the current year.

The gap in yields between the Italian government bond and the German government bond has recently stabilised at approximately 120 basis points.

Spread Italian Government Bond/German Government Bond

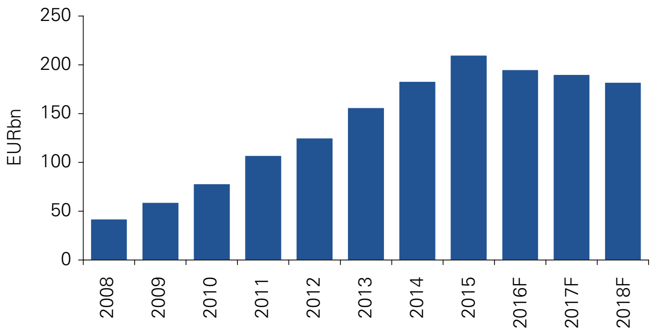


Source: Market data provider

However, the Italian banking sector is still seen as one of the Eurozone's weakest. Specifically, non-performing Loans (NPLs) have increased in Italy, with the solvency of Italian banks attracting investor attention, bearing in mind that the NPL ratio of more than 16% is well above the European average of 5.7%.

Real estate comes in to play because approximately half of corporate and retail NPLs are secured against real estate assets.

Non Performing Loans



Source: Banca d'Italia and Prometeia
F – forecast

The Italian real estate investment market has begun attracting global investors later in the cycle mainly due to limited availability of finance. The sector is still in a deleveraging process and this is impacting heavily on lending conditions (LTV ratios barely go beyond 50%).

In H1 2016, the volume invested in real estate stood at approximately EUR3.4bn, down by 9% compared to the same period in 2015. However, the 2015 figures were boosted by the large Porta Nuova transaction (EUR900m); if this exceptional deal is excluded, the investment market jumped by 20%, representing one of the best first half years ever.

Investor activity in the market remains high, with foreign investors accounting for the majority of first half investment by volume (>70%). Milan and Rome remain the most attractive markets, presenting interesting opportunities for core products in their historic centres.

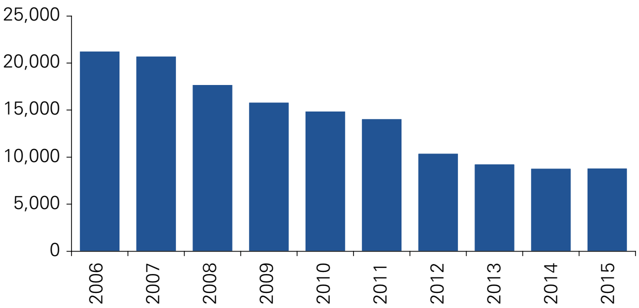
The hotel sector experienced lively growth in H1 2016, with Rome benefiting especially from investor interest; the city enjoys an annual visitor stream of more than 20m tourists.

Office Market

The office sector is still the investor's preferred asset class, although the beginning of 2016 has been marked by increased caution among investors compared to the end of 2015. However, interest in Italian real estate remains solid.

At the 2015 year-end there had been a total of approximately 8,842 deals, a small increase compared to the previous year (+0.4% vs. 2014).

Number of Office Transactions



Source: Agenzia del Territorio

After a turbulent start, confirmation that the ECB would strengthen QE has reassured the markets and injected new confidence, boosting investment activity. Demand remains focused on prime products, and large one-off transactions are expected to impact the year-end figures.

Whilst Milan remains the city preferred by both domestic and international investors, there was increased interest in the Rome office market, with the IT/communications, legal and banking sectors experiencing the liveliest activity.

During Q2 2016, trends in the Milan office market remained positive, with volumes from the first quarter doubling. The most important transaction was the purchase by Axa of Via Monte Rosa 91 for approximately EUR220m.

The low cost of capital continues to encourage the trend for tenants and owner-occupiers to purchase office space. This is driving demand for prime assets in particular and, given the lack of product, prime net initial yields now stand at approximately 4.0% in the CBDs, with prime rents stable at EUR490/sq. m.

Italy

Office Market Highlights – Milan

	Q1 2016	Q1 2015	2015
Investments (EURm)	438	546	2,507
Take-up (sq. m.)	58,500	72,400	370,000
Prime rents (EUR/sq. m. p.a.)	490	490	490
Net prime yields	4.0%	5.0%	4.0%
Vacancy rate	12.0%	13.2%	12.0%

Source: CBRE

In the area around Milan, development remains stable, with 76,000 sq. m in the pipeline for completion by the end of the year. However, developers continue to seek pre-lease agreements before starting construction.

Trends on the Rome market are lively; it accelerated significantly, with a total investment volume of approximately EUR400m, more than double the volume for the whole of 2015.

This level was reached thanks to major deals such as the Great Beauty portfolio transaction of three office assets in the CBD for approximately EUR220m and the Coin in Via Cola di Rienzo for some EUR85m. Both deals recorded aggressive yields.

As the market recovers, investors are considering the redevelopment or change of use of vacant office premises, primarily in the CBD.

By way of an example, the Scarpellini portfolio deal involved two assets in the CBD which will be converted into office space after refurbishment.

In terms of take-up, the public sector is less active and, as a result, the IT and telecommunications sectors have accounted for approximately 75% of the total space taken up.

Prime net yields are stable at 4% (-115 bps compared to Q1 2015) with prime rents at EUR380/sq. m in the CBD and EUR320/sq. m in Eur district.

Office Market Highlights – Rome

	Q1 2016	Q1 2015	2015
Investments (EURm)	397	56	173
Take-up (sq. m.)	72,100	17,500	136,000
Prime rents (EUR/sq. m. p.a.)	380	380	380
Prime yields	4.00%	5.15%	4.00%
Vacancy rate	9.0%	8.2%	9.0%

Source: CBRE

Development activity increased slightly, with almost 163,000 sq. m under construction / refurbishment expected to be completed between 2016 and 2017, of which only 23% related to speculative projects.

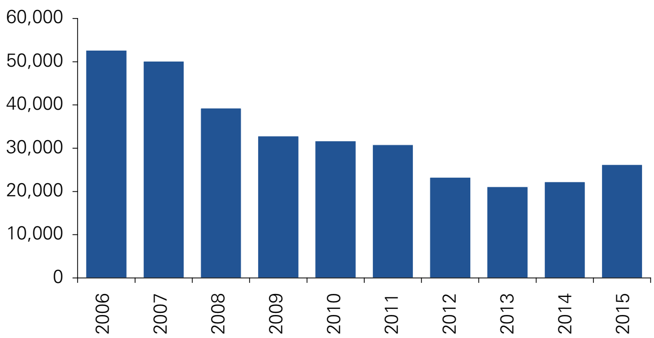
Retail Market

After recording continuous growth for more than 24 months, retail sales in Q2 2016 saw a slowdown, driven mainly by lower consumer confidence due to the macroeconomic situation in Italy and Europe.

However, there is still interest in the retail real estate market, particularly from institutional investors, which have also started looking out for interesting opportunities in southern Italy.

In 2015, the year-end transaction volume totalled 26,234 deals, an increase of 18% from 2014, emphasising the sustained activity on the market (there were approximately 22,271 transactions recorded in 2014).

Number of Retail Transactions



Source: Agenzia del Territorio

Total investment for H1 2016 reached EUR700m, and the pipeline remains strong, with approximately EUR2bn of assets on the market.

As with other sectors, transaction activity continues to be dominated by foreign investors. In particular, Primark and Wagamama restaurants opened their first outlets in Italy with associated major real estate investments.

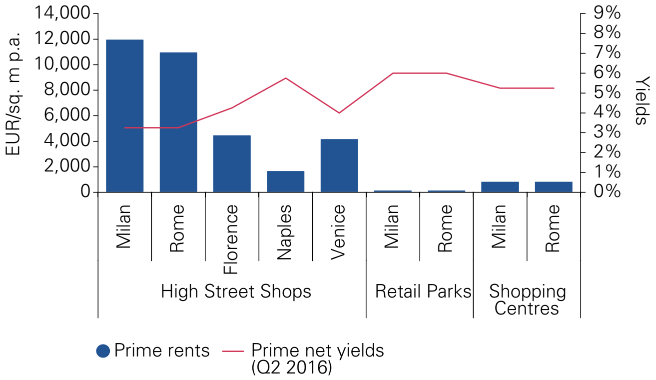
Single-asset deals remain dominant, however H1 2016 saw a major transaction in relation to Grandi Stazioni Retail, which involves various commercial areas associated with Italy's main railway stations (Milan, Rome, Florence, Turin, etc.).

For this deal, the joint venture between the Italian Borletti Group, the French Antin Infrastructure fund and the asset manager Icamap signed a preliminary agreement for around EUR1bn.

In terms of single-asset deals, a major transaction was recorded in relation to the Meraville retail park in Bologna, purchased by TH Real Estate for approximately EUR105m.

Prime net yields across both high street and shopping centre segments, particularly in the Via Montenapoleone area in Milan and the Via Condotti area in Rome, are reaching a low (approximately 3.5%), with secondary cities becoming more and more attractive to investors looking for interesting returns.

Prime Retail Rents and Yields – Q2 2016



Source: Cushman and Wakefield

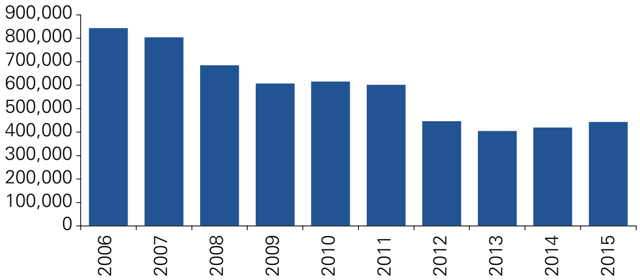
As well as displaying growing interest in northern Italy's secondary cities (Florence, Turin, etc.), investors, driven by compressed yields, are opening up to deals in southern Italy in areas characterised by good fundamentals and interesting yields.

Residential Market

The early months of 2016 have confirmed the positive trend seen in the residential sector throughout 2015.

Comparing Q1 2016 with the same period in 2015, there was a significant increase in the number of transactions (+20.6%), from 95,455 to 115,135.

Number of Residential Transactions



Source: Agenzia del Territorio

As usual, Rome and Milan were the most active cities with approximately 6,340 and 4,108 transactions in Q1 2016 respectively.

The increase in sales in the residential sector is directly linked to a significant improvement in the mortgage market, which recorded an increase of 19.5% in residential loans compared to 2015.

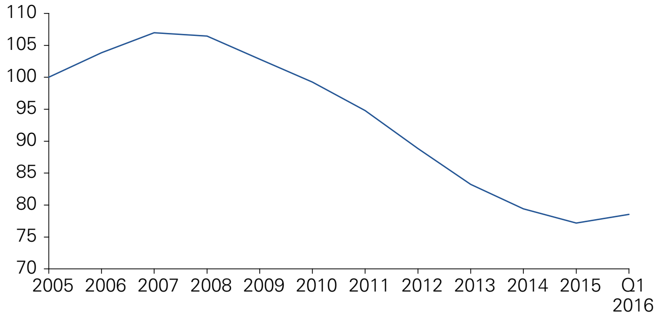
After a declining trend in house prices in the final months of 2015 and the first months of 2016, the market seems to be in a stable phase.

Analysing the situation in the main Italian cities in greater depth, the average house price fell by 7.5% in Rome in 2015 but remained stable in Milan and Naples, with small increases of 0.7% and 0.1% respectively.

The average discount proposed by purchasers on the initial asking price is around 14.5%.

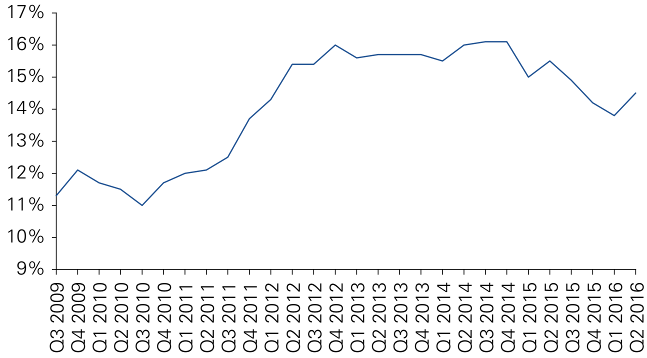
Italy

Average Price of Houses (Price in Real Terms – Price 2005=100)



Source: Globalization and Monetary Policy Institute
Average of 13 main Italian cities

Average Discount to initial Price proposed by Sellers



Source: Bank of Italy, Tecnoborsa, Agenzia del Territorio

Focus on Digitisation

The Italian property market is tempting for foreign investors, with over 75% of investment in the Italian real estate sector dominated by cross-border investors. However, to be competitive in this market, it is essential that their investment operations are supported by digital services.

If Italian real estate is to continue on the path to recovery that has already started, it needs to enhance the available techniques and tools to meet international demand.

Nowadays, various solutions have already been proposed in order to support customers in organising the disposal process. These solutions facilitate the collection of the documents necessary for the sale, as well as preparing the data room for the transaction.

The market has sensed increased interest from customers and a growing focus on the most advanced professional and digitised services on offer from service providers. Thanks to the recovery of the sector and the growing maturity of the market, this is expected to be essential for a high-quality offer.

Digitised services in the real estate sector are expected to bring benefits to the organisation of the asset sale process in Italy. An increasing number of banks and investors are choosing this kind of service, with the aim of ensuring greater transparency for buyers who benefit from the availability of comprehensive and reliable data in relation to the target asset.

This ensures that they have a deep knowledge of the characteristics of the target asset and provides them with a high level of protection in the whole acquisition process. In due course, all of this could also have a positive effect on the purchase price.

Spain

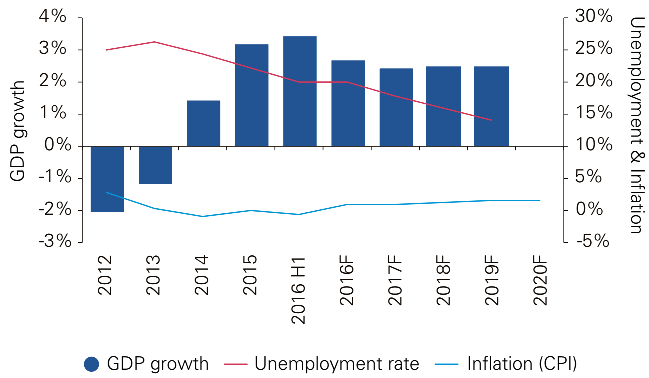
Favourable economic conditions

Macroeconomic Overview

- GDP: In line with government estimates.
- Inflation: Prices falling more slowly.
- Employment: Improvement in services and tourism.

The Spanish economy grew by 0.7% in Q2 2016, slowing slightly from the 0.8% increase in the previous three periods but in line with market expectations. This was the 12th quarter of consecutive growth. Spain's unemployment rate fell to 20% in the three months to June 2016 from 21% in the previous period, beating market expectations of 20.4%. It was the lowest figure since Q2 2010, boosted by jobs in services and tourism. Consumer prices in Spain fell 0.6% in the year to July 2016, following a 0.8% drop in June. This was the 12th consecutive month with no growth in consumer prices although July's decrease was the lowest in six months.

Economic Indicators



Source: INE and ministry of economics
F – forecast

Office Market

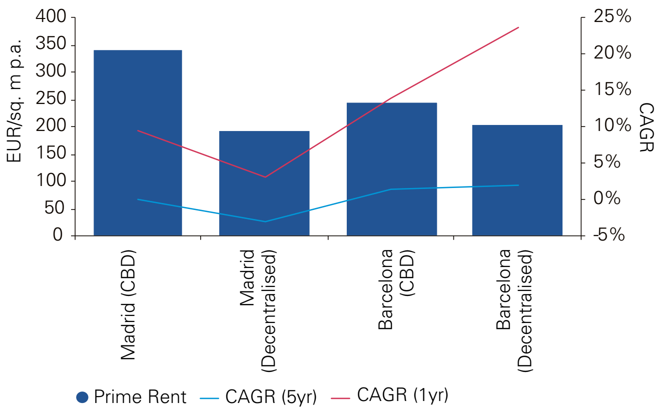
The growth in Spain’s economy is benefiting the market for office space. The growth in demand for office space remains very evident in the core and central business districts (CBD) of Madrid and Barcelona.

City centres are the most popular destinations for companies looking to set up. However, availability is low (around 7% in the CBD) and consequently rents are increasing. Whilst domestic companies continue to dominate the market at present, foreign investors are becoming increasingly important, and currently their strategy is to stimulate competition in order to actively undercut core real estate yields in Madrid and Barcelona. The limited availability of these high-demand sites is putting

Spain

pressure on some investors to focus on other market segments and second-tier cities, where higher yields can be expected.

Prime Office Rents

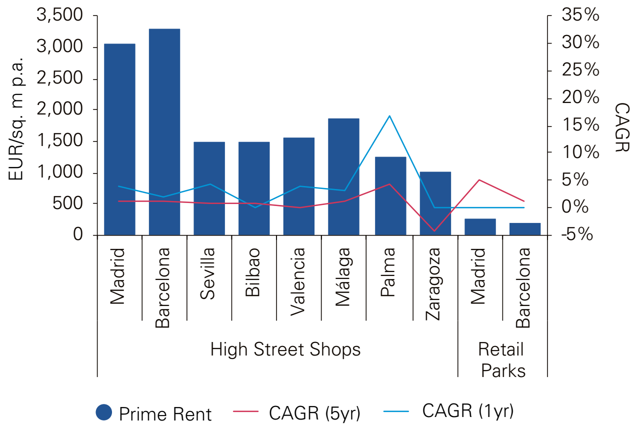


Source: Cushman and Wakefield

Retail Market

The positive impact of the recovery in employment, low inflation and weak interest rates are gradually boosting domestic demand in Spain. These favourable conditions are leading new international players and buyers to invest in the Spanish retail market, as they believe that it offers great potential for their flagship stores in core locations. However, the availability of space for such investments is limited, particularly in top locations in major cities such as Madrid and Barcelona. Demand for second-tier assets in good regional locations and for high-quality assets in secondary markets with an increased element of risk is also continuing to grow. Consequently, the gap between yields for primary and secondary assets is narrowing further as investors turn their attention more to non-core properties in promising locations.

Prime Retail Rents for High Street Shops

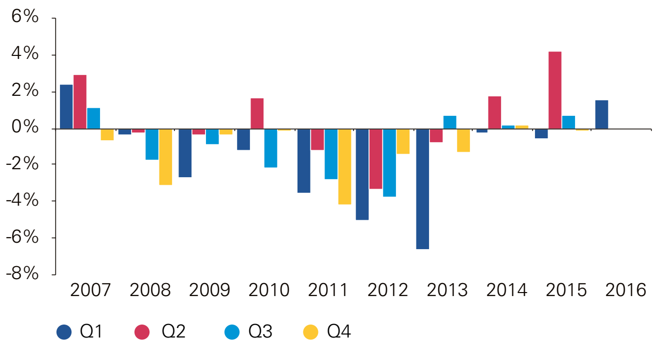


Source: Cushman and Wakefield

Residential Market

After almost seven years of falling house prices, Spain's housing market is gradually recovering, but not at a uniform pace or across the whole country. Rising demand, the recovery in investment activity and improved access to mortgage finance are some of the main factors behind this recovery. Spanish house prices increased by 0.83% during the year to the end of Q2 2016 (2.07% inflation-adjusted), the third consecutive quarter of Y-o-Y growth.

House Price Change (quarterly Variation)



Source: INE

Focus on Digitisation

The real estate industry in Spain is now starting to experience the impact on assets of the fundamental shift to digitalization.

Office Space Adaptation

An example of this transformation is the recent major change of approach by BBVA in its new corporate headquarters in "Las Tablas", a 114,000 sq. m complex on the periphery of Madrid where the concept of collaborative space is taking precedence over private space and telecommuting policies have become a priority for more than 6,000 employees. Another example of office space adaptation is the relocation of the head offices of KPMG Spain to a single skyscraper in the Four Towers Business Area in Madrid, where the entire office space of 23,000 sq. m is available to the 2,300 employees rather than allocating restricted private space for each employee. Moreover, a policy of enhancing mobility inside and outside the office by improving remote network access for all employees in Spain has resulted in an improved use of space.

Retail Footprint Adjustment

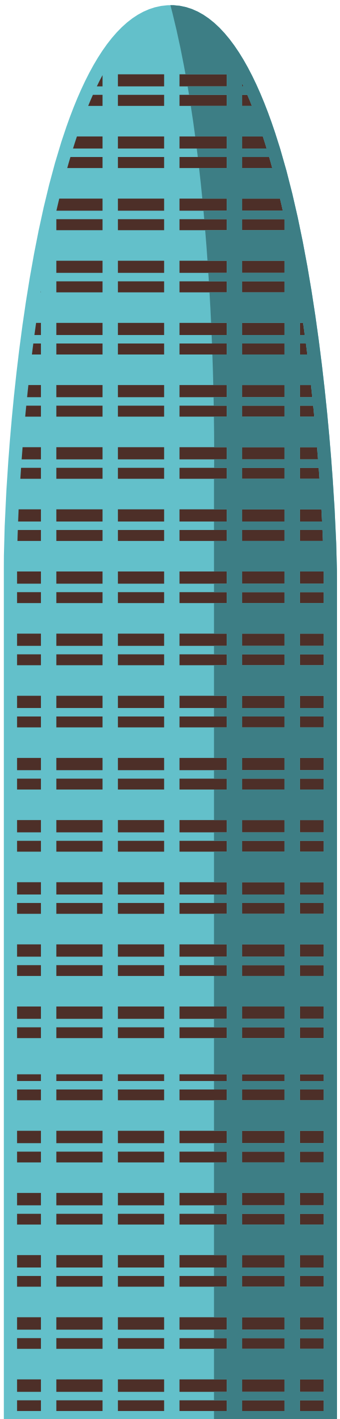
Some shopping centre operators have adopted a real estate strategy which involves intensifying both traditional store and internet channels (omni channel). An example is Neinver's approach in its "The Style Outlets" shopping centre in Alcobendas. Here, data from users' mobile devices is collected during the purchasing experience. This information can be analysed immediately and significant value can be obtained from it.

Other companies are focusing their retail strategy by concentrating their efforts on their internet channels alone, reducing their retail footprint. For example, Banco Santander has recently announced the closure of 425 branches in Spain and BBVA has forecast the closure of 2,800 branches over the long term.

Digital Transformation of Industrial Real Estate

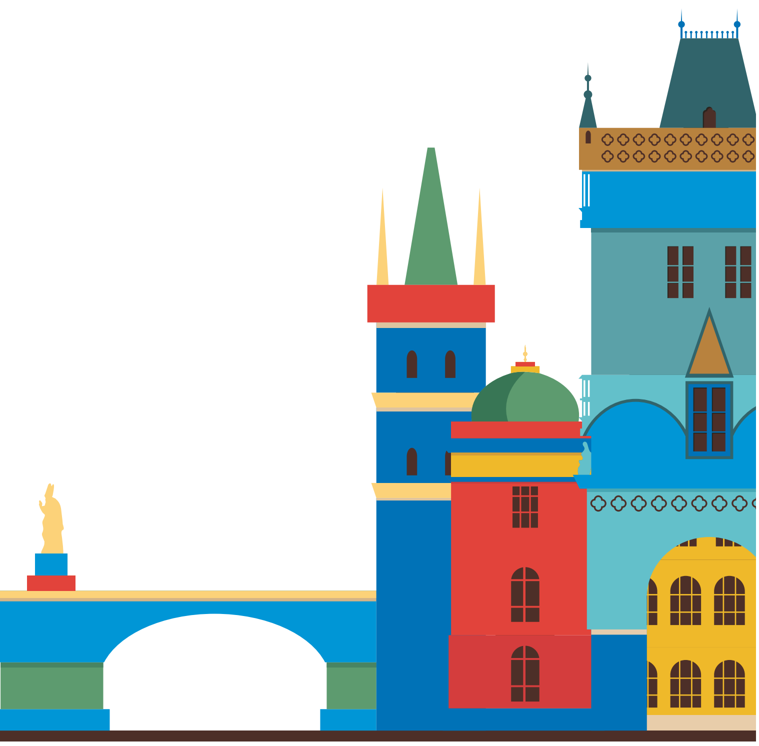
The increase in online sales has led to a reduction in the footprint of retail stores and investment in new, highly technical fulfilment centres to distribute stock to customers more efficiently.

Directly connected to this is the planned investment by Amazon in El Prat del Llobregat, consisting of 60,000 sq. m for a new logistic centre which will generate around 1,500 new jobs in Barcelona province, or the investment amounting to EUR70m by El Corte Inglés in a new fulfilment centre in Tarragona province.



CEE

Investment market at the highest level since the crisis



Macroeconomic Overview

At this stage, it would be difficult to make a full assessment of the impact of the Brexit referendum that took place on 23 June and resulted in a vote against the UK's continued membership in the EU, or to draw conclusions from the vote. Although the consequences are not yet clear, it is widely expected that Brexit will present a lengthy period of uncertainty and raise questions regarding the unity of EU countries.

The UK is the third largest contributor to the EU's structural and investment budget, whilst most of the CEE economies are recipients of EU funds; therefore, a possible restructuring of EU funding could have a negative impact on investment in the region. CEE currencies slid immediately after the final result of the referendum was announced, but this fall was short-lived as investors looked past the first shock of Brexit.

In annual terms, GDP in the **Czech Republic** grew by 2.5% in Q2 2016, boosted mainly by domestic consumption and a growth in automobile manufacturing. The automotive industry is the driving force of manufacturing and therefore of primary importance to the Czech economy. It grew significantly, by 16.9% in the year to April, and this growth also boosted related sectors. In addition, the unemployment rate fell to a seven-year low of 5.2% in June 2016 – the lowest rate in the EU.

Economic activity in **Poland** remained strong in H1 2016, with GDP growth of 2.6% and 3% in Q1 and Q2 respectively, the latter driven by growth in industrial production and retail sales. 2015's strong economic activity and business performance have led to improvements in the labour market. The unemployment rate stood at 10.3% in January 2016 and dropped to 8.8% in June 2016. Beside the improving macroeconomic indicators, the government has to deal with USD36bn of Swiss-franc dominated mortgages owed by Poles, equivalent to around 8% of the country's GDP. The plan to convert foreign currency loans into zloty loans at below-market rates could weaken the Polish currency, undermine Poland's credit rating and also push the banking sector into the red.

Romania is one of the most dynamic emerging markets in the region. In Q1 its GDP grew by 4.3% compared to the same period in 2015, followed by 6% growth in Q2 – the highest growth rate in the EU and the fastest since 2008. Domestic demand is the main driver of growth, boosted by tax cuts and rising wages in the state sector after the government agreed with trade unions to raise the minimum wage by 19% as of May 2016.

Hungary's economy lost momentum in Q1 2016, with the GDP figure showing negative growth over the year. The drop into negative territory was a result of a decline in EU funding that hit the construction industry hard, and a slowdown in the automotive sector, brought about by reduced activity by the local subsidiary of German car maker Audi. These developments highlight the economy's reliance on these two factors. On a positive note, the economy bounced back in Q2, growing by 2.6% Y-o-Y, supported by a pickup in wages and an acceleration in the absorption of the EU funds.

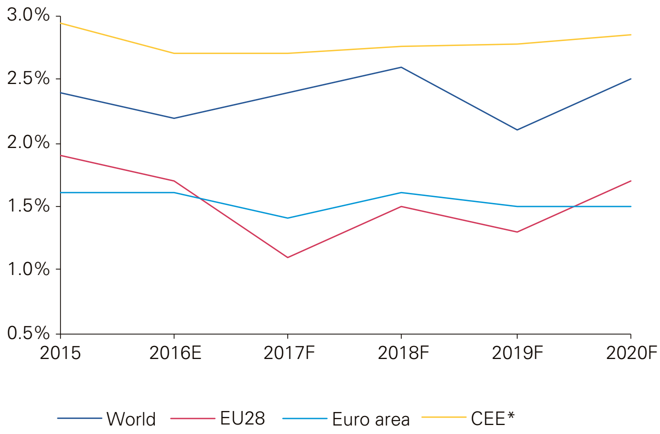
According to the EIU, the fastest annual growth is expected in Romania and Poland, at 4.5% and 3.3% respectively, whilst on the flip side Hungary, Croatia and Slovenia are anticipated to grow the slowest, at annual rates of 2%, 2% and 1.8% respectively.

Real GDP Growth Rate (in %)

	2015	2016E	2017F	2018F	2019F	2020F
World	2.40	2.20	2.40	2.60	2.10	2.50
EU28	1.90	1.70	1.10	1.50	1.30	1.70
Euro area	1.60	1.60	1.40	1.60	1.50	1.50
CEE*	2.93	2.71	2.70	2.76	2.77	2.84
BGR	3.00	2.80	3.20	3.40	3.00	3.30
CRO	1.60	2.00	1.90	1.90	1.70	1.90
CZE	4.60	2.30	2.60	2.20	2.10	2.20
HUN	2.90	2.00	2.30	2.70	2.20	2.40
POL	3.60	3.30	2.90	3.40	3.30	3.20
ROM	3.80	4.50	3.30	3.30	3.60	3.50
SRB	0.70	2.60	3.30	3.50	4.00	4.20
SVK	3.60	3.10	2.80	2.60	3.00	2.80
SVN	2.60	1.80	2.00	1.80	2.00	2.10

Source: Economist Intelligence Unit, December 2015
E – estimate
F – forecast
* = Baltics, Bulgaria, Croatia, Czech Republic, Hungary, Poland, Romania, Serbia Slovakia and Slovenia

GDP Growth, Global Outlook

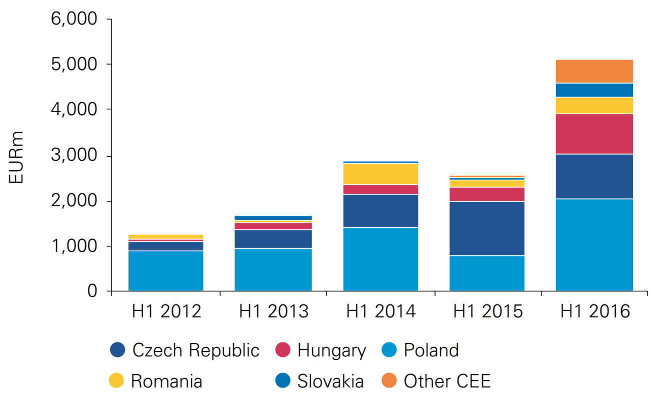


Source: Economist Intelligence Unit, December 2015
F - forecast
* = Baltics, Bulgaria, Croatia, Czech Republic, Hungary, Poland, Romania, Serbia Slovakia and Slovenia

Investment Market

The real estate investment market gained momentum in the CEE region in H1 2016 and reached the highest level since 2007, with transactions totalling EUR5.1bn, representing an increase of approximately 69% Y-o-Y. A record year is forecast in terms of transaction volumes, at over EUR10bn.

Total Real Estate Investment Transactions in CEE (H1 2012–H1 2016)



Source: JLL

The most notable transactions in the region were observed in Poland and Romania. Redefine became the owner of 75% of the total shares of a mixed asset portfolio with properties across Poland, and NEPI acquired a shopping centre in Sibiu, Romania for EUR100m.

As last year, Poland and the Czech Republic were the market leaders in the region, accounting for approximately 60% of the overall investment volume during H1 2016, although it is worth mentioning that Hungary, Slovakia and the Southeast Europe region witnessed solid growth in terms of investor demand.

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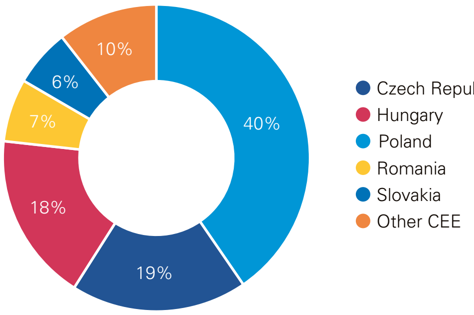
Over the course of H1 2016, Poland regained its leading role in the CEE region, with 40% of the total volume invested, or EUR2.1bn; it was followed by the Czech Republic, Hungary and Romania, with 19%, 18% and 7% respectively.

CEE Investment Market by Country, 2015



Source: JLL

In Hungary, the volume of investment nearly tripled compared to the same period in 2015, whilst in Poland the amount invested almost doubled. The Czech Republic was the only CEE country where investment volumes declined in H1 2016, by approximately 21% compared to the same period in 2015. The, first half of the year 2016 was exceptionally strong in the Czech Republic due to the sale of the Palladium shopping centre.

Almost half of transactions by volume were focused on the retail sector (48%), whilst investor interest in the office sector also remained strong, representing 36% of the total volume invested in the past twelve months. The industrial and hotel sectors accounted for smaller shares, of approximately 14% and 2% respectively.

Indicative Yields and Q-o-Q Change, Q2 2016

	Prime office	change	Prime retail	change
Belgrade	9.00%	↘	8.00%	↘
Bratislava	7.25%	→	7.50%	→
Bucharest	7.50%	↘	9.00%	→
Budapest	7.25%	→	6.75%	→
Prague	5.75%	↘	4.75%	↘
Sofia	8.50%	↘	8.75%	→
Warsaw	6.00%	→	7.00%	→
Zagreb	8.05%	→	8.00%	→

Source: JLL

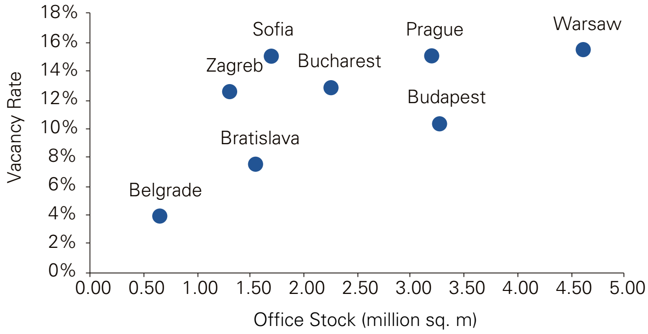
Looking at prime yields, yields in the office and retail sectors remained stable in Q2 2016, with minor adjustments in the Warsaw and Zagreb office markets, and also in the retail markets in Budapest and Zagreb. As in earlier quarters, the highest yields could be found in Belgrade and Sofia, whereas the lowest were in Warsaw and Prague.

Office Market

Owing to the improving business confidence and economic growth in the CEE region, a number of developments are expected to be delivered in the next 36 months, especially in the core CEE markets such as Warsaw, Budapest and Prague. Conversely, development activity remained relatively low in the less established locations, particularly in Sofia and Zagreb. The most notable volume of development has been seen in Warsaw, where 545,000 sq. m of office space is under construction, followed by Budapest, where approximately 302,410 sq. m of office space is expected to be handed over by the end of 2018.

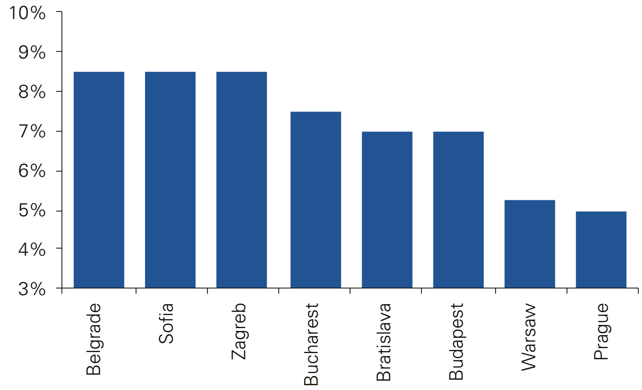
The largest office stock was recorded in Warsaw, accounting for 4.63m sq. m, followed by Budapest and Prague, with 3.28m and 3.19m sq. m Grade A and B office stock respectively, whereas the lowest stock was in Zagreb (1.3m sq. m) followed by Belgrade (0.7m sq. m).
Due to healthy occupier demand and positive net absorption, vacancy rates decreased in most markets. Average vacancy rates were between 3.8% and 15.4%. The lowest vacancy was observed in Belgrade (3.8%), followed by Bratislava (7.4%), whereas the highest proportion of empty space was in Warsaw, where the overall vacancy rate stood at 15.4% by the end of H1 2016, an increase of 1.3 percentage points over the past 12 months. In Warsaw, this change in the vacancy rate was driven particularly by increased supply. A further slight increase in supply is expected in Warsaw over the short-term, although vacancy there is forecast to stabilise from 2017. The most significant change was witnessed in the Slovakian, Hungarian and Serbian markets, where vacancy rates declined by 4.4, 3.9 and 3.2 percentage points respectively. As in previous quarters, the most active tenants on the market came from the IT, financial services and SSC/BPO sectors.

Office Supply and Vacancy Rate, Q2 2016



Source: JLL City Reports Q2 2016

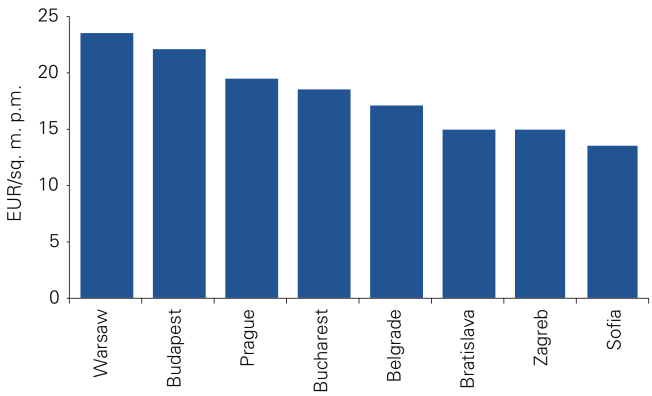
Prime Office Yield, Q2 2016*



Source: JLL
*Sofia, Zagreb H1 2016 data

Prime rents remained stable across the CEE region, although in Warsaw downward pressure on rents is anticipated owing to the increased supply. In certain locations, i.e. in Budapest, Bratislava and Sofia, a gradual withdrawal of tenant incentives and upward pressure over the long-term are expected. As in previous quarters, the highest prime office rents can be found in Warsaw (EUR23.50/sq. m. p.m.) followed by Budapest (EUR22.00/sq. m. p.m.) and Prague (EUR19.50/sq. m. p.m.), whilst the least expensive rents continue to be recorded in Sofia (EUR13.50/sq. m. p.m.). Headline rents in Zagreb and Bratislava follow at around EUR15.00/sq. m. p.m.

Prime Office Rents, Q2 2016*



Source: JLL
*Sofia, Zagreb H1 2016 data

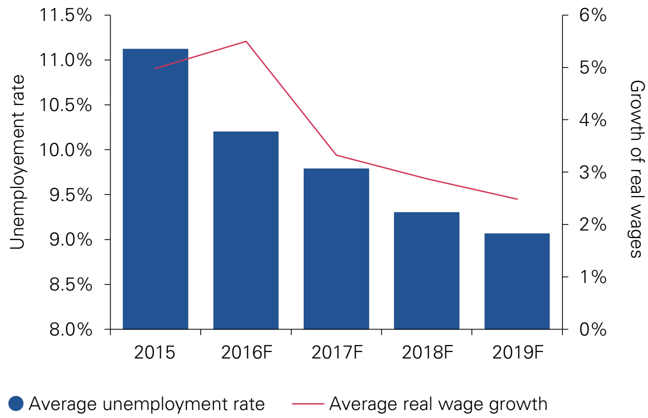
Despite the increase in investment activity in the region, prime yields remained stable in most of the CEE countries. Mirroring recent years, the highest yields were recorded in Belgrade, Sofia and Zagreb, at 8.5%. Conversely, Prague, followed by Warsaw, saw the lowest levels at 5.0% and 5.25% respectively.

Retail Market

Improving market conditions, reflected in rising retail sales and a falling unemployment rate, as well as growing disposable income in the CEE region, are making the market more attractive to international retailers. Retail sales growth has maintained its momentum across the CEE region and this trend is expected to continue in the short-term.

International retailers are also seeking opportunities to relocate to better-performing modern schemes in major cities, or to secure a presence in the best performing shopping centres and high street units and, as a result, there remains a gap between rental and occupancy levels in secondary and prime locations.

Regional average Unemployement Rate & Real Wage Growth



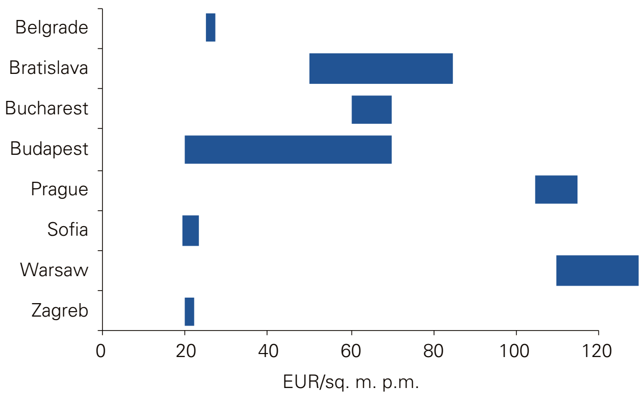
Source: Economist Intelligence Unit
Countries: Bulgaria, Croatia, Czech Republic, Hungary, Poland, Romania, Serbia, Slovakia
F – forecast

CEE

Based on forecasts by the Economist Intelligence Unit, average real wage growth will continue over the medium-term, whilst unemployment rates will decrease steadily in the countries under review. This decline will not be so marked in the CEE market because it is from a lower base; the most significant drop in the unemployment rate may be seen in Croatia, where it is forecast to fall from 17% in 2015 to 13% in 2019.

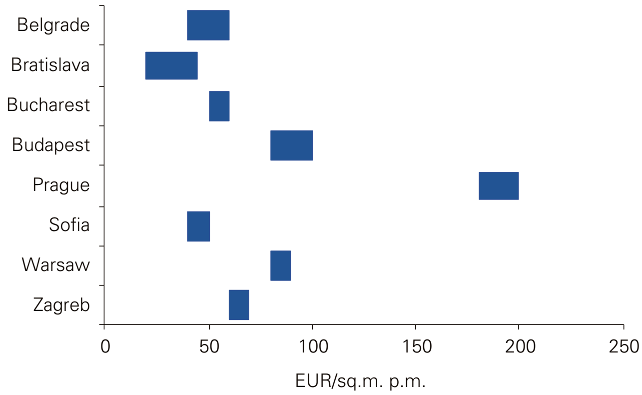
Despite the favourable market environment and the improved availability of finance, development activity in the first half of the year was muted. Total retail stock increased only in Sofia and Belgrade, where 12,000 sq. m and 48,000 sq. m respectively of new retail schemes was handed over. The highest level of retail stock was in Greater Warsaw, with a total of 1.66m sq. m of modern retail space, followed by Prague at 1.02m sq. m, and Bucharest with 1.01m sq. m. The lowest levels were registered in Belgrade and Sofia, with 175,000 sq. m and 424,000 sq. m respectively. A number of proposed schemes are in the pipeline in the core CEE markets, such as in Poland, Romania, Hungary and the Czech Republic. The highest level of new development was commenced in Bucharest, where approximately 191,000 sq. m is under construction, followed by Warsaw and Budapest, where 149,800 sq. m and 135,000 sq. m of modern retail stock will be handed over by 2018.

Prime Rents at Shopping Centres, Q2 2016*



Source: JLL
*Sofia and Zagreb H1 2016 data

Prime High Street Rents, Q2 2016*

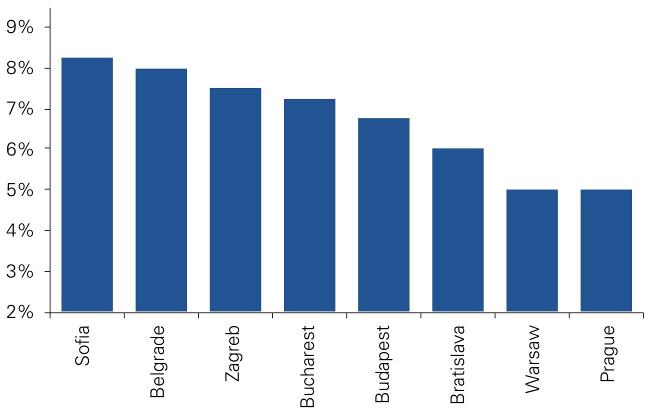


Source: JLL
*Sofia and Zagreb H1 2016 data

Prime rents for high street retail space remained stable, except in Prague where a slight increase in rents was noted. Looking at shopping centres, Warsaw, Prague and Budapest saw rental growth in the first six months of 2016. As in previous quarters, Prague was the most expensive market in terms of high street retail rents, whilst Warsaw offers the most expensive space for retailers in prime shopping centres. The lowest average prime high street rents are in Bratislava and Sofia, whilst Zagreb and Sofia are the least expensive markets for shopping centre rents.

Whilst retail property has become the most sought-after asset class in the region, prime retail yields remained stable across the countries under review. A slight decrease was recorded in Budapest and Zagreb. As in previous quarters, the lowest retail yields were seen in Prague and Warsaw, at 5% in both markets. Investors perceive Sofia and Belgrade as the riskiest locations in the region, with yields of 8.25% and 8% respectively.

Prime Retail Yields, Q2 2016*



Source: Source: JLL
*Sofia, Zagreb H1 2016 data
Note: Prime yields are for shopping centers in the case of Prague and Warsaw

Residential Market

In March 2016, average mortgage rates in the Czech Republic fell below the 2% mark for the first time to reach 1.97%. In June 2016, the average rate fell further, to a historic low of 1.87%, as a result of the relaxing of monetary conditions and increasingly intense competition amongst domestic banks. Significant growth was seen in the Czech mortgage market in the period January–June 2016, when the number of new mortgages reached more than 55,000 and total volume of loans reached CZK28.3bn, a new record. The average price of apartments in **Prague** reached EUR2,200 (CZK60,000)/sq. m for the first time because of the favourable lending conditions, improved economic growth and consumer confidence, and a shortage of new developments. Although some new residential projects are under construction, Prague is witnessing a shortage of apartments as a result of the rapid absorption of existing apartments on offer, whilst new projects have been hampered by delays in the approval process and have been slow to get off the ground.

Budapest saw a surge in residential property prices in H1 2016, due to a combination of low loan interest rates, a reduction in VAT on new-build homes from 27% to 5% and the Home Purchase Assistance Scheme (CSOK). Moreover, residential real estate has become a preferred form of investment, and Euro/Swiss Franc-dominated mortgages were replaced by less risky Forint-based loans. The number of mortgages increased by 50% in the first six months of 2016 compared to the same period in 2015. The low returns on bank deposits and comparatively high rental yields of 6% to 9% are also attracting the attention of both international and local investors purchasing apartments to let. By the end of 2016, some 3,500 new units are expected to be added to the market, with an additional 4,400 units already in the pipeline for completion in 2017. The capital's 5th District remained the most expensive, with prices above EUR2,500/sq. m, whilst the 11th and 13th Districts were the most sought-after areas.

2015 was marked as the best year in history for the **Bucharest** residential market, fuelled by wage growth, improved credit terms and the "Prima Casa" (First Home) programme. On the back of this, developers have launched numerous new projects or new phases of existing projects. The major new development activity is in the south and west of the capital, but there are also several projects under construction in other areas. The exclusive One Herastrau Park residential project will comprise two 11-storey towers with a total of 106 triplex apartments expected to be delivered in Q1 2017. Premio Exclusive City Centre brought a total of 32 apartments to the market in two buildings of eight and six floors. The fourth phase of InCity Residences will offer a total of 129 apartments, varying between 63 and 265 sq. m. This new phase will consist of 17 floors and will offer 12 types of apartment. In terms of prices, the Kiseleff-Aviatorilor district is the most expensive with prices above EUR2,700/sq. m, followed by Herastrau-Nordului at EUR2,400 and Dorobanti-Floreasca at EUR2,200/sq. m. Prices in other areas of the capital are below the EUR2,000/sq. m threshold.

The boom in the **Polish** residential market has continued, with record low interest rates and the MdM (Housing the Young) subsidy programme. Sales of residential units are up in the six largest regional markets (Warsaw, Wroclaw, Tri-City, Poznan Lodz and Krakow). However, and surprisingly, price rises were minimal. Warsaw's residential market is the most expensive, with an average price of EUR1,975/sq. m, followed by Krakow and Gdynia at EUR1,558 and EUR1,462/sq. m respectively. Zlota 44, at 192 m is Europe's tallest residential skyscraper, with 52 floors and 300 apartments, and has transformed the capital's skyline. The first phase of the Nordic Mokotów project will comprise a total of 125 apartments with completion anticipated in Autumn 2017. Housing investment continues to be profitable, bearing in mind the low returns on bank deposits and the scope for using rental income to finance the cost of credit. In Q1, 25% of apartments were sold with the support of the MdM scheme but this number dropped to 19% in Q2, mainly because of a tightening of lending policy but also because some subsidy pools have come to an end over the course of 2016. In Q1 2016, the number of building permits issued increased by 9.7% and the number of dwellings completed rose by 17.3%.

Focus on Digitisation

Technology has impacted on everything in today's business environment, and digital innovation has changed economies and markets across the globe. It has transformed the traditional characteristics of numerous industries as well as the features of the real estate industry.

Digital advances and a number of evolving consumer trends had an inevitable impact on all asset classes and related business models. A combination of newly developed technologies has influenced how properties are built, how traditional workplaces are configured and designed, and how commercial real estate is operated, sold or let.

Office

By the end of this decade, it is predicted that Generation Y will make up 50% of workers, dominating the workforce. As more and more millennials enter the workforce, its structure and working space are changing. To attract and retain Generation Y workers, organisations need to rethink their approach to design and develop or redevelop both new and existing space to enhance the occupier experience and optimise space more effectively. Since technology has begun to impact office space, there has been a trend towards hot-desking, where employees do not have permanent desks but instead work in a large open and collaborative environment. Open layouts allow a more efficient use of space and can save on rent and maintenance.

Technology also allows today's workers to work remotely, whether at home, in open-plan space in the office or even at co-working spaces. "Remote work" offers numerous advantages and opportunities for cost savings, but it requires organisations to provide their employees with sufficient office supplies, equipment and mobile devices to do their job efficiently and effectively. This will involve substantial investment and to some extent it will add to IT security concerns as remote users connect devices from home or public terminals to access company email using high-speed internet and small shared networks.

There is likely to be more sharing of space between smaller companies and start-ups, with office space vendors providing customers with access to premium workspace without needing long-term leases, guarantees or additional liabilities. Such collaboration will allow organisations to make more efficient use of under-utilised space, and enable owners to maximise the potential of their real estate assets.

Retail

Online retail is changing the way in which we all purchase goods and services, and it is forcing retailers to tailor their business models to retain and satisfy consumers. There is a trend towards online shopping, and many businesses are embarking on online retail, with a consequential impact on retail and warehouse properties.

In Poland, Tesco doubled the number of its stores offering online services from 14 to 27 between 2012 and 2015. In line with this growth, the number of its delivery vans increased from 86 to 236. Carrefour and its competitor Auchan also offer home delivery in Warsaw and its suburbs. Zabka Polska, a chain of convenience stores in Poland, has partnered with courier company TBA Express to establish 4,000 nationwide in-store collection points for online orders. In Romania, Carrefour has redesigned its e-commerce platform, improved its interface on mobile devices and introduced a same day delivery service. The Cora hypermarket has also introduced online shopping in Romania in partnership with logistics firm TNT. In Hungary, Tesco is already present in the online shopping market and also offers a "click & collect" service. CEE online grocery services are still less advanced than in Western Europe, but retailers across the region are prioritising such service lines to better meet consumer needs.

The increase of online retail is driving down interest in bricks and mortar retail properties but boosting demand for logistic property. Although e-commerce, with all its convenience, was supposed to bring an end to traditional retail, what is actually happening is consolidation and redefinition. Pop-up shops are a recent trend in retail, in which brands can try out a physical presence over the short or medium-term to see how they interact in different locations.

E-commerce is growing, and organisations will have to capitalise on online and physical shops, develop strategic mergers and ensure that they benefit from both online and local presence.

Russia

Facing the new reality

Macroeconomic Overview

It is clear that, in the middle of 2016, the Russian real estate market is facing a genuine crisis, and, due to its systemic nature, it is unlikely that things will improve much in the short term.

Most market players are struggling with the same challenges: oversupply, a fall in purchasing power, rouble uncertainty, a lack of liquidity, lack of finance and the need to gradually adapt to the new market environment.

Whilst there is still much uncertainty, demand seems to be heading towards rock bottom, pulling the whole market down with it. However, a gradual recovery in the market is still a possibility if the key players change their business models and the Russian economy can break out of its decline.

The silver lining is that the current situation, challenging as it is, can take the market to a new level, where the strong players and high quality projects survive and the weak ones leave.

In our analysis we focus primarily on the Moscow market, as the most mature commercial real estate market in Russia. However, most of the trends that we refer to can also be seen across the whole Russian market.

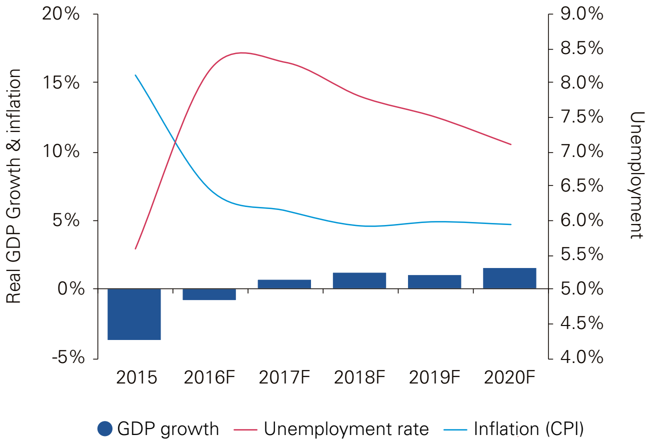
The Russian economy shrank by 3.8% in 2015, undermined by a plunge in household consumption and investment. The pace of the slowdown began to ease in H1 2016, with analysts expecting a slight contraction of 0.8% in 2016. The economy is forecast to rebound in 2017 on the back of rising oil prices, weakening inflation and exchange rate stabilisation.

In the medium term, average real GDP growth will not exceed 2.0%, constrained by structural weaknesses, including a lack of investment, high levels of state involvement in the economy and a lack of diversity in the economic structure.

After soaring to 15.5% in 2015, the average annual inflation rate eased to 7.5% on the back of a reduction in private consumption. The pace of inflation is expected to weaken to 6.7% in 2016 and level off at 4.6–5.5% in 2019–2025.

Russia

Economic Indicators



Source: Economist Intelligence Unit
F – forecast

The exchange rate trends witnessed in 2015 continued into H1 2016, with the rouble fluctuating between RUB 65.00 and 84.00 /USD, though gaining some ground by the end of H1. After reaching RUB 68.00 /USD in 2016, the rouble rate is expected to stabilise at RUB 58.00–62.00 /USD from 2017 onwards.

After a slide in 2015, real estate investment activity showed signs of a rebound in H1 2016, and the total investment volume reached USD2.5bn. With a number of major deals expected to close by the end of 2016, investment volumes are forecast to rise to USD3.5bn.

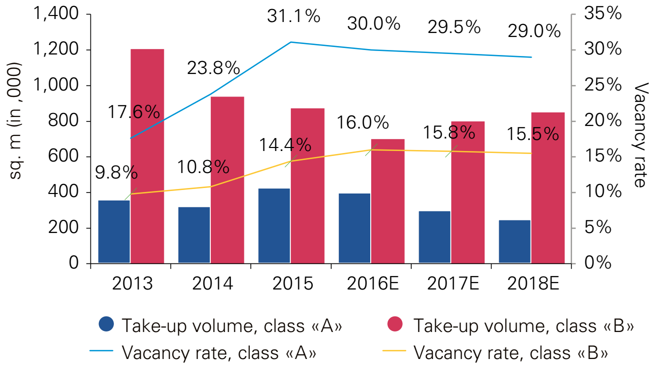
The share of foreign capital in investment transactions in H1 2016 fell to a record low of 5% in the face of continued market uncertainty. Investors focussed chiefly on prime assets located in Moscow (82% of the total investment volume), with the majority of deals executed in the office segment (67%).

Despite the upswing in investment activity, prime yields remained unchanged in H1 2016, ranging between 10.0% and 11.0% for prime offices and retail, and 12.0% and 13.0% for industrial properties.

Office Market

The deterioration in the overall economic situation and the consequent fall in demand against a background of strong development activity triggered an office market crisis in 2014, with falling rents, rising vacancy and significant oversupply. These trends continued into 2014-2015 and then into 2016.

Demand and Vacancy Rate of Office Space in Moscow



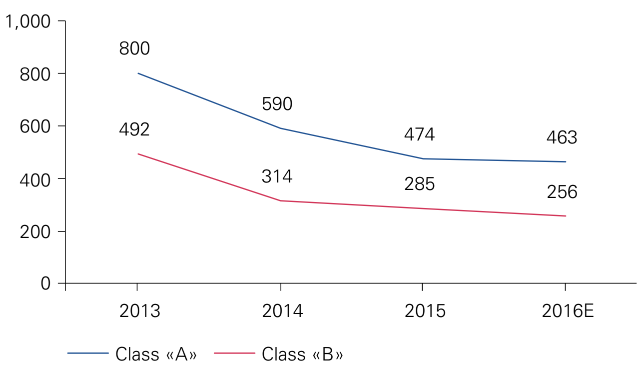
Source: Broker reports
E – estimate

In H1 2016, the total supply of quality office space exceeded 16.2m sq. m, with Grade-A accounting for 24.4%. The total volume of new construction volume is expected to drop compared to 2015, to 679,000 sq. m, the lowest figure in the past four years.

The take-up volume in 2016 is expected to decrease slightly to 1.1bn sq. m, with the absorption of Grade-A properties, primarily by large multinational companies, accounting for only 30% of the total.

The decrease in rents which started in 2014 has continued in 2016. The average dollar rate is expected to fall by 6% compared to 2015, when it will be 40% below the 2013 level. Nevertheless, the trend of falling rents made several significant deals possible in 2016, such as the acquisition of approximately 8,000 sq. m of Grade-A office space by Tinkoff Bank and a number of significant deals in Moscow city. Overall, there were around 980 new deals in H1 2016, totalling almost 658,000 sq. m. Around 93% of these deals were rouble-denominated.

Office rental Rates in Moscow, USD/sq. m. p.a.



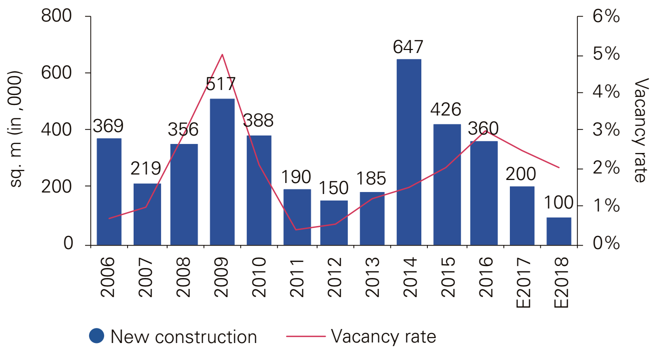
Source: Broker reports
E - estimate

Overall, experts tend to think that the real estate market in Russia is becoming more or less stable. However, it is too early to reach a final conclusion as to whether market equilibrium is close to being reached.

Retail Market

Despite higher construction costs, issues in finding finance and retailer difficulties, the total amount of new construction in the retail sector in 2016 could exceed 2.5bn sq. m of lettable area in Moscow (35%) and regional cities (65%). Most successful new shopping centres are expected to be 60%–70% occupied. The average vacancy for stable shopping centres remains at 7%–10%.

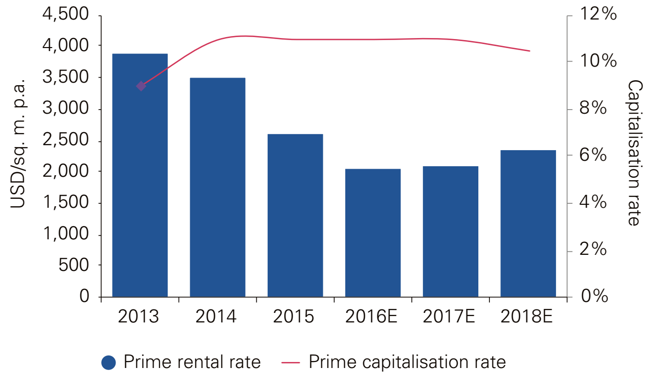
Quality Retail Construction in Moscow and Vacancy Rate



Source: Broker reports
E - estimate

Although real consumer income has dropped, store traffic has risen slightly in 2016 compared to 2015. The most efficient retailers and shopping centre owners have adjusted to a more practical and less impulsive type of consumer that is likely to dominate in the next two to three years, and they have started to offer new formats and concepts to attract visitors: brand mix supermarkets, pop-up designer markets, discount markets and entertainment and edutainment spaces.

Prime rental Rate and Capitalisation Rates for Retail Centres in Moscow



Source: Broker reports
E - estimate

In most shopping centres, owners reserve discounts and fixed exchange rates for dollar leases since currently they are more interested in stable occupancy than in higher rates.

Several well-known international brands have left the Russian market, to be replaced by new names, both Russian and international, which are taking advantage of a less competitive environment and lower rents. By the end of 2016, more than 20 new international brands are expected to enter the Russian market, including Walt Disney, Presse Café, Lillapois, and Cortefiel. Strong players are expanding their presence in Russia – IKEA, X5 Retail Group, etc.

Russia

Residential Market

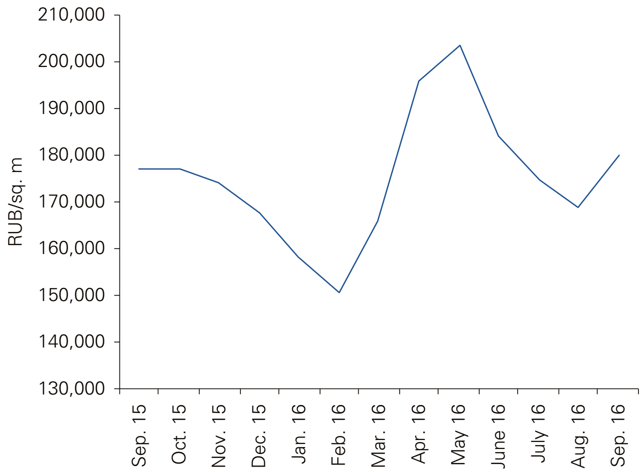
The trends witnessed in 2015 extended into H1 2016, with prevailing oversupply, reduced purchasing power and depressed prices contributing to the subdued market environment.

The deterioration in development activity which began in 2015 continued into H1 2016, with the commissioned volume falling by 9% compared to H1 2015. In Moscow this trend was even more pronounced, with a 26% slump recorded.

H1 2016 witnessed a marked shift in buyer preferences towards lower-priced units, with demand for smaller flats rising – including prime properties. With buyers becoming more price sensitive, developers reduced flat sizes and offered hefty discounts to boost affordability and meet their sales targets. In addition, in the face of stiffer competition developers were increasingly focused on reducing costs, although their marketing expenses increased.

Despite the overall slowdown, the Moscow market regained some sales momentum: the volume of sales rose by 11% in H1 2016 compared to H1 2015. The key contributors to this surge were mortgages (12%) supported by an extension of the state mortgage subsidy programme, and various discounts offered by developers.

Average House Price in Moscow



Source: Broker reports

H1 2016 saw an increasing variability between price growth in the various regions, with growth recorded in almost half of the largest Russian cities. At the same time, in Moscow the average price fell by 9% compared to the same period last year as a result of growth in supply in the economy segment. With developers gradually removing their discounts, prices are expected to bottom out by the end of 2016.

Focus on Digitisation

Digitisation is reshaping the real estate industry, shifting the focus in working patterns towards flexibility, customisation and speed. Digital innovation is penetrating every real estate sector, from visualisation technologies in construction to online letting services, leading to cost reductions, enhanced efficiency and an increase in the utilisation of properties. Furthermore, digitisation brings investment in commercial property within the reach of a large number of individuals through online platforms, stimulating the development of crowd funding in real estate.

The most profound impact from digitisation is felt in the retail sector. Whilst maintaining their core role of creating a shopping experience, offline stores are evolving through the integration of new technologies and adopting an omni-channel approach. To keep up with the pace of change, retailers are making increasing use of gamification, with a view to capturing customer preferences and ramping up their engagement. For example, various applications that reward users for their purchases or the number of footsteps in a shopping centre, are gradually catching on.

Drastic changes in the retail sector have also triggered a supply chain overhaul, with proximity to customer bases and speed of delivery assuming increased importance, and so driving demand for urban warehouses. A surge in demand from online retailers encourages the utilisation of technologies designed to cope with the demand volatility inherent in e-commerce, such as automated tracking systems or robotic pick-ups.

By enhancing employee mobility and creating a more connected working environment, digitisation is also transforming the workplace. In addition, new technologies, whether they be biometric authentication systems, phone-controlled smart locks or lighting systems with daylight sensors, are making offices safer and more comfortable.

Turkey

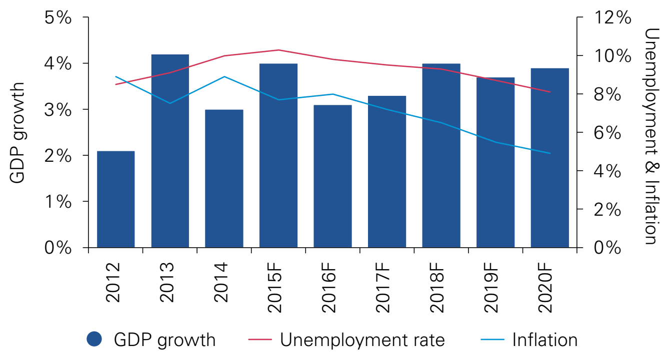
Geopolitical risks on the rise

Macroeconomic Overview

- GDP: A slowdown in the economy is expected in the medium-term.
- Inflation: Inflation is high, with strong underlying pressure on prices.
- Employment: Job creation is slowing because of economic and geopolitical risks.

During Q1 2016, the Turkish economy expanded by 0.8% compared to the previous quarter and 4.8% Y-o-Y, due mainly to increased consumer spending. In addition to private consumption, government spending increased by 10.9% Y-o-Y and this also boosted the economy. However, because of increasing geopolitical risks and violence, the economic outlook is not stable. Indications are that job creation and export orders may fall during H2 2016. It is expected that private consumption will remain the main driver for growth.

Economic Indicators



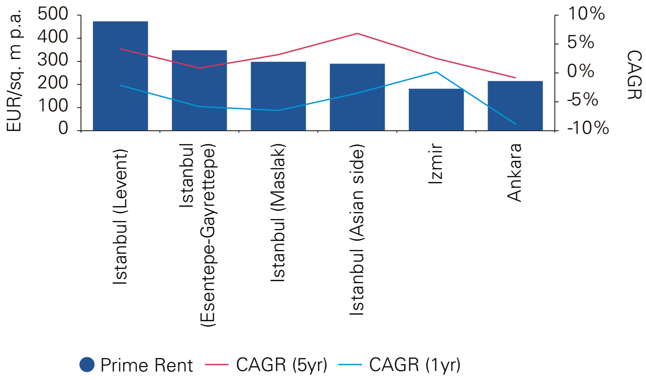
Source: Economist Intelligence Unit
F – forecast

Office Market

During Q2 2016, demand for office space weakened, mainly because of geopolitical tensions and increasing violence within the country. Demand was limited mainly to major business districts in Istanbul. The occupier market witnessed demand for space in the central business district (CBD) and Atasehir submarkets. On the supply side, the overall vacancy rate increased to 17%. No activity at all was recorded on the office investment market, major reasons being political instability and increasing violence. The outlook for office space remains weak because of an increase in speculative supply and falling demand; however, the situation may improve with development of some Grade A stock.

Turkey

Prime Office Rents – June 2016

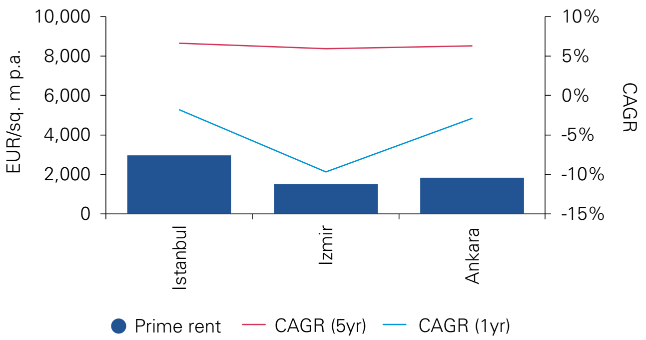


Source: Cushman and Wakefield

Retail Market

Despite increased geopolitical concerns, the retail real estate market grew during Q1 2016 due to the rise in private consumption. Notwithstanding weakness in some areas, the retail occupier market remained strong. The market saw the arrival of a number of international brands. In addition, around 213,000 sq. m of retail space was released onto the market. There were few major deals concluded in the investment market for retail space. The outlook for the retail market remains positive due to strong growth in private consumption and falling inflation; however, rising security concerns and the volatility of the Turkish Lira are expected to create weaknesses in the retail real estate market.

Prime Retail Rents – June 2016

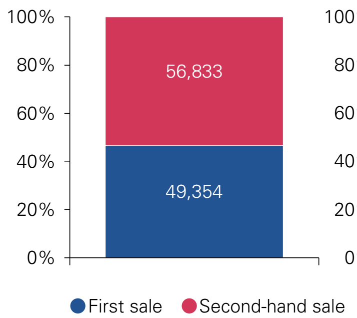


Source: Cushman and Wakefield

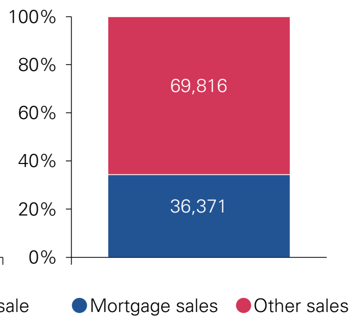
Residential Market

House prices have increased by 93% over the last five years, according to statistics published by the Central Bank of Turkey (THPI). According to the THPI, the price of residential properties in Turkey increased by 17% in the year to November 2015, with Istanbul witnessing the highest increase of all the residential markets, of 24%. Istanbul is expected to face continued demand for residential developments targeting lower-middle and middle income groups. However, this development is expected to take place in Istanbul's suburban districts due to the scarcity of land and the high cost of development in the city.

House Sales by State of Sale, June 2016

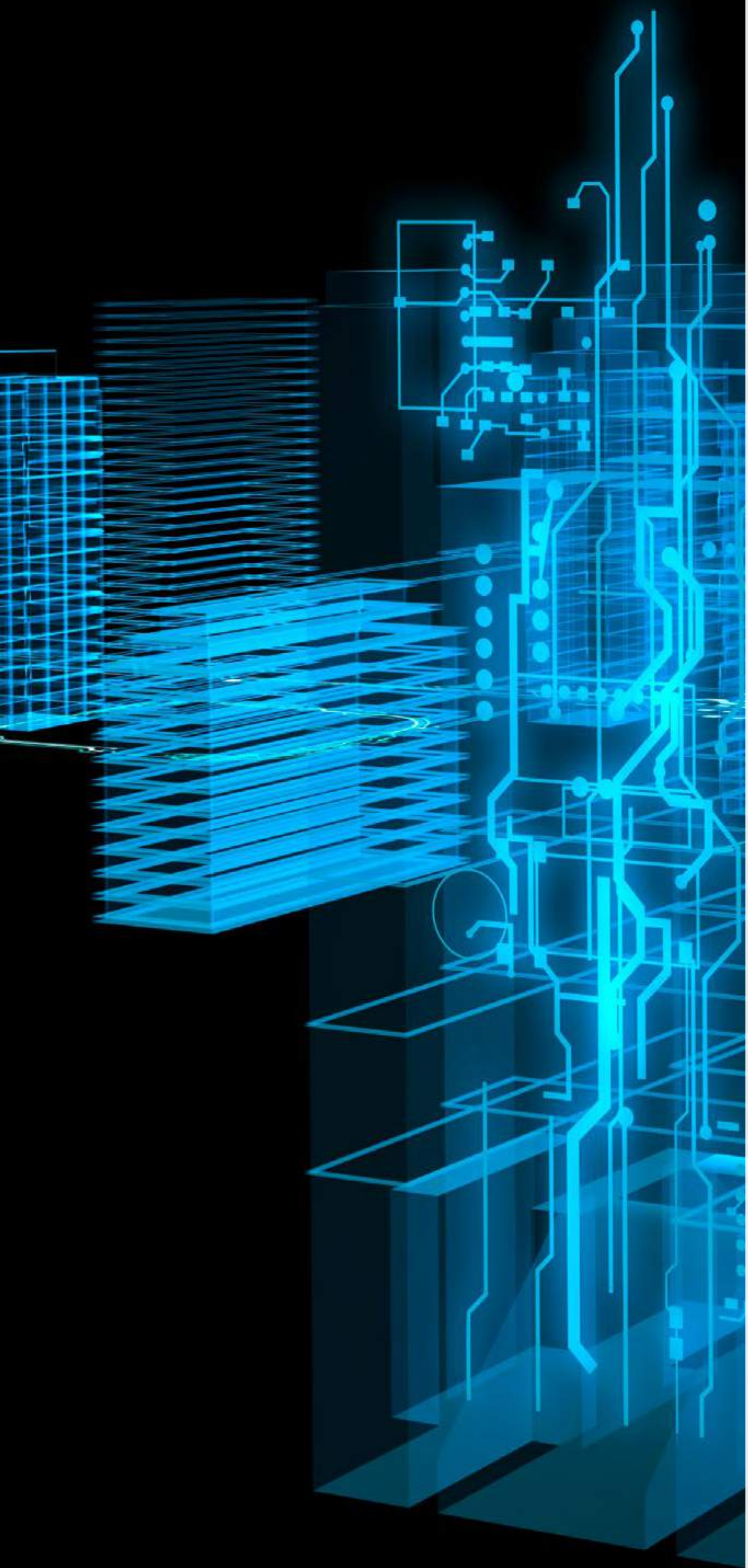


House Sales by Type of Sale, June 2016



Source: Turkish Statistical Institute

Glossary



bn	Billion
CAGR	Compound annual growth rate
CBD	Central Business District
CHF	Swiss Francs
CPI	Consumer Prices Index
E	Estimate
ECB	European Central Bank
EUR	Euro
F	Forecast
GBP	British pounds (sterling)
GDP	Gross domestic product
LTV	Loan-to-value
m	Million
NPL	Non Performing Loan
p.a.	Per annum
p.m.	Per month
QE	Quantative easing
Q-o-Q	Quarter-on-quarter
SNB	Swiss National Bank
sq. m.	Square meter
sq. m. p.a.	Square meter per annum
sq. m. p.m.	Square meter per month
USD	US dollar
Y-o-Y	Year-on-year

All-encompassing Real Estate Advisory from one Source

The challenging and increasingly complex real estate markets and the ongoing technological developments require a clear focus and a flexible strategy. Our real estate team is involved in every stage of the asset and investment lifecycle, working with all levels of stakeholders throughout the real estate industry. Whether your focus is local, national, regional or global, we can provide you with the right mix of experience to support and enhance your needs and ambitions. We provide informed perspectives and clear solutions, drawing on our experience from a variety of backgrounds including accounting, tax, advisory, banking, regulation, IT Advisory and corporate finance. Our client focus, our commitment to excellence, our global mind-set and consistent delivery build trusted relationships that are at the core of our business and reputation.

M&A/Capital Market
- Structuring and execution of transactions (Lead Advisory)
  - Asset deals: Acquisition and disposal of properties and portfolios
  - Share deals: Mergers, spin-offs, IPOs, private placements
- Arrangement of indirect investments, such as funds or trusts
- Fund raising for specific projects
- Debt advisory

Investment Advisory
- Investment advisory for national or international indirect real estate investments
- Structuring of real estate investments within portfolios
- Qualitative and quantitative analysis of investment products
- Monitoring and investment controlling, portfolio performance measurement

Strategy/Organization
- Strategy development and implementation
  - Business planning/business modelling
  - Corporate/public real estate management
  - Asset and portfolio management
- Analysis of organization and processes; organizational development, internal control system
- Performance management/MIS/investment monitoring
- Securing of digital readiness
- Risk management and financial modelling
- Turnaround and financial restructuring

Valuation/Due Diligence
- DCF-valuations of properties and real estate portfolios or companies
- Independent valuation reports for financial statements
- Valuations for acquisitions or disposals
- Feasibility studies and valuation of real estate developments
- Transaction-focused due diligence and process management
- Major Project Advisory

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