



# Swiss Real SnapShot!

**There is no means of avoiding  
real estate investments**

Current developments  
in the Swiss real estate  
investment market

**Spring 2016**





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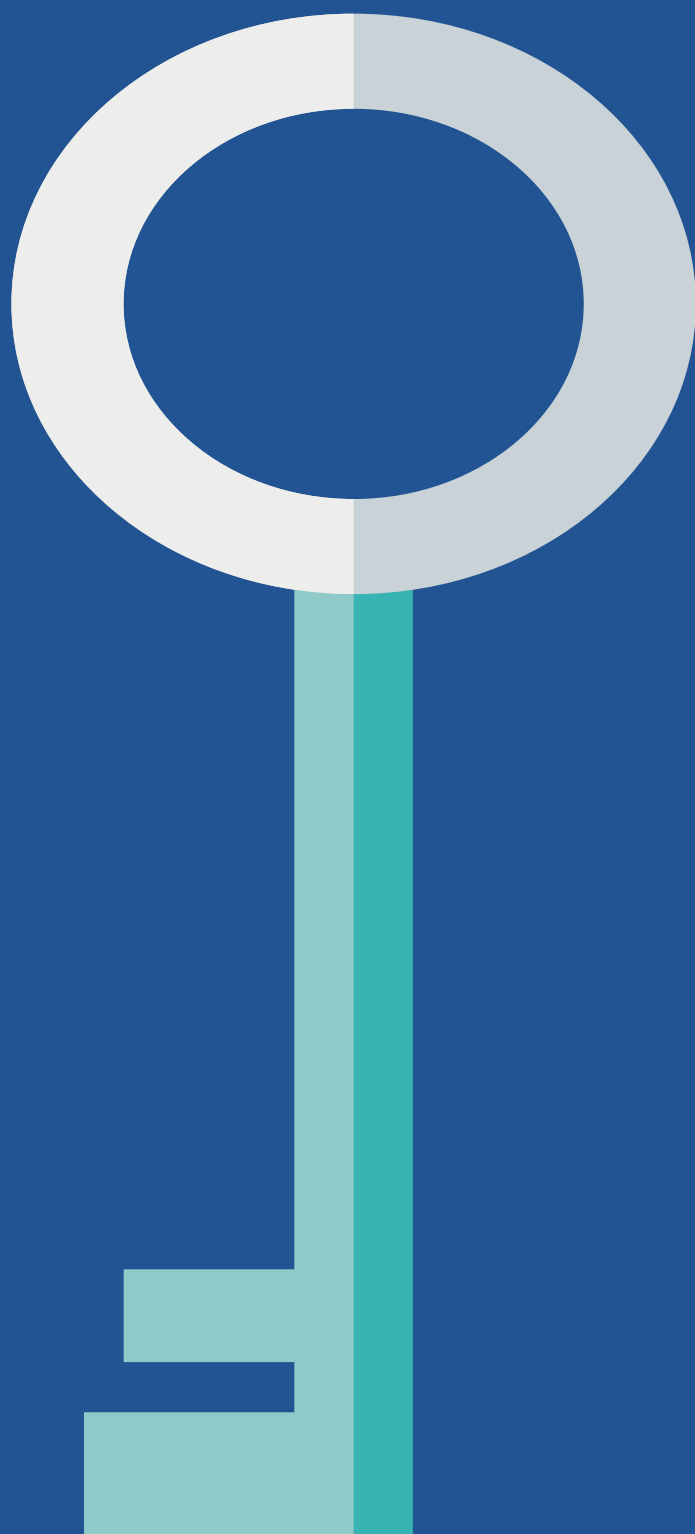
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# Introduction

Dear Sir or Madam

KPMG Swiss Real SnapShot!, published every 6 months, provides you with an overview of the current developments in the Swiss real estate market and its influencing factors.

The Swiss real estate market is a heterogeneous and strictly segmented structure. Thus, KPMG Swiss Real SnapShot! limits itself to global observation, without addressing regional deviations in detail.

KPMG Real Estate has both, Swiss specific and global expertise in the real estate markets. Our extensive data pools in local markets along with competent and in-depth consultation generate added value for our clients in all areas connected with real estate.

Turn to the last page of KPMG Swiss Real SnapShot! to see what we can do for you and how you can benefit from our services.

We wish you a pleasant and informative reading.

With kind regards,



Ulrich Prien  
Partner, Head of Real Estate Switzerland



Beat Seger  
Partner, Real Estate M&A

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# There is no means of avoiding real estate investments

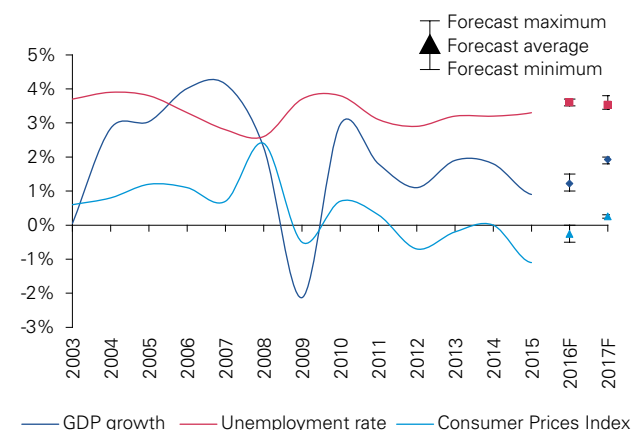


## Macroeconomic Overview

The Swiss economy is still labouring under the effects of the abolition of the Franc-Euro exchange rate mechanism by the Swiss National Bank (SNB). After economic growth practically came to a standstill in the first half of the year, the real Gross Domestic Product (GDP) also stagnated in Q3 2015. The marked slowdown in economic trends is mainly the result of the revaluation of the Franc on January 15, 2015, which – together with weaker world trade activity – has been a significant burden on foreign trade. In Q3 2015, whilst the balance of trade in goods made a positive contribution to growth, the balance of trade in services was nonetheless negative. Furthermore, important domestic economic drivers have also lost momentum in recent quarters. This is affecting the construction industry in particular, which has entered a phase of consolidation after several years of strong growth.

The consequences of abandoning the exchange rate mechanism and the introduction of negative interest rates by the SNB will also be felt in the Swiss economy in 2016, even if the initial rise of the CHF/EUR exchange rate of almost 20% has since fallen to 10%. Many businesses are struggling with falling margins and as a result, some are considering relocating abroad. Some of them are already doing just that. Nonetheless, a slight positive trend is forecast for the current year. The Consensus GDP forecast for 2016 stands at 1.2%. A recovery to 1.9% is anticipated for 2017.<sup>1</sup>

### Macroeconomic Indicators

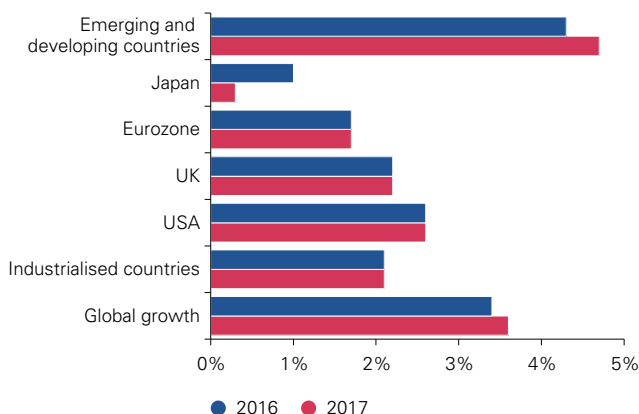


Sources: BAKBasel, Credit Suisse, KOF, SECO, UBS and KPMG  
F – Forecast

<sup>1</sup> The Consensus Forecast is based on projections by BAKBasel, Credit Suisse, KOF, SECO and UBS

Following a slight downward revision in its forecasts in January 2016, the International Monetary Fund (IMF) is expecting global growth to accelerate slightly in the current year, from 3.1% to 3.4%. For industrialised countries, an expansion of 2.1% is anticipated, with expectations pinned above all on the USA (2.6%) and the United Kingdom (2.2%), and less on the Eurozone (1.7%).

#### Global GDP Growth



Source: IMF and KPMG

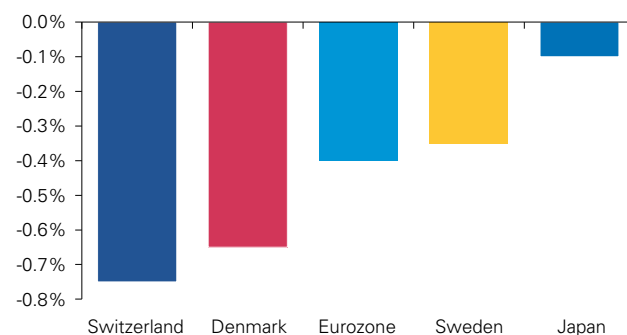
The US economy is in the sixth year of recovery since the severe economic collapse following the 2009 financial crisis. The labour market has largely stabilised and, with over 200,000 new jobs created each month, the unemployment rate has halved from over 10% to its current level of 5%. Because the labour market was increasingly drying up and signs of earnings growth were becoming apparent, the US Federal Reserve, after hesitating several times, raised interest rates for a first time in December 2015.

The Eurozone is benefiting particularly from the role played by the US economy in growth and the strength of the US Dollar over the last two years. At the start of 2014, the Euro was still above USD 1.40, but by announcing its own loan purchase programme, the European Central Bank (ECB) triggered a devaluation of the Euro in the spring of 2014, as a result of which its value compared to the US Dollar has fallen by around a quarter.

Despite the relatively stable economic data, a high degree of volatility has characterised the international financial markets since the start of 2016. The Swiss Market Index has also lost over 12% of its value since the start of the year. It is true that there is increased speculation about the threat of recession, perhaps because of the low oil price, the difficult position of European banks or the ailing Chinese economy. However, if one then looks at the available economic data at present, there are only a few signs pointing to a recession.

In the middle of December 2014, the SNB introduced negative interest rates for credit balances on its current accounts. The negative interest rates acted as a brake on inflows into the Franc, which is seen as a “safe haven”. Foreign banks in particular have reduced their cash holdings in Francs. However, the policy seems to have had less success in encouraging Swiss investors to make investments in foreign currencies. For institutional investors, negative interest rates have further accentuated the investment crisis. Whilst these investors have also reduced the cash component of their portfolios, they have been shifting the money into property investments, amongst others.

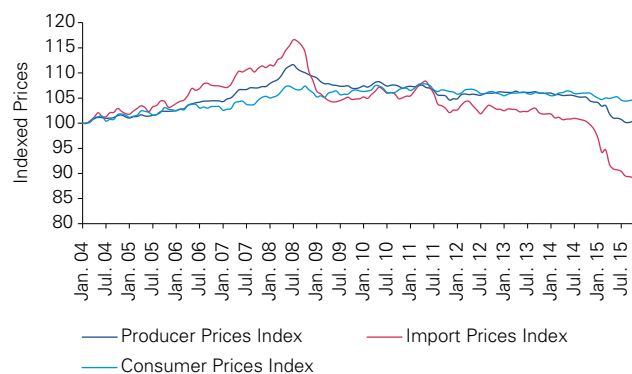
#### Summary of Negative Interest Rates on Deposits with Central Banks



Source: IMF and KPMG

The appreciation of the Franc, combined with a heavy fall in crude oil prices, has resulted in a significant fall in the price of imports over the past year by almost 10% compared to the previous year. The greatest price drops have resulted in lower prices for crude oil and crude oil products, chemical and pharmaceutical products and machinery. In December, this pushed consumer prices down by 1.3% compared to the previous year. Negative inflation, of -0.3%, is also anticipated for the current year.

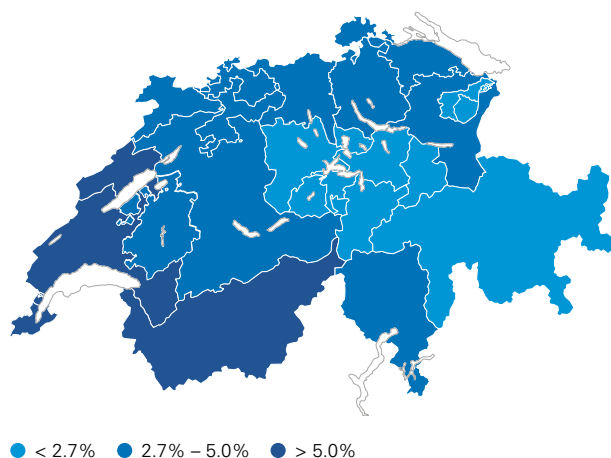
#### Producer, Import and Consumer Prices



Sources: BFS and KPMG

According to surveys by the State Economics Secretariat (SECO), at the end of March 2016 around 155,000 unemployed were registered with the regional employment exchanges, 6,000 less than in the previous month. Therefore, the unemployment rate has decreased from 3.7% in February 2016 to 3.6%. Compared to the same month in the previous year, unemployment has risen by more than 10,000. For the current year, because of the emerging downturn in the economy, economic institutes anticipate average unemployment of 3.6%, a rise of 0.3 percentage points compared to last year.

#### Unemployment rate by Canton

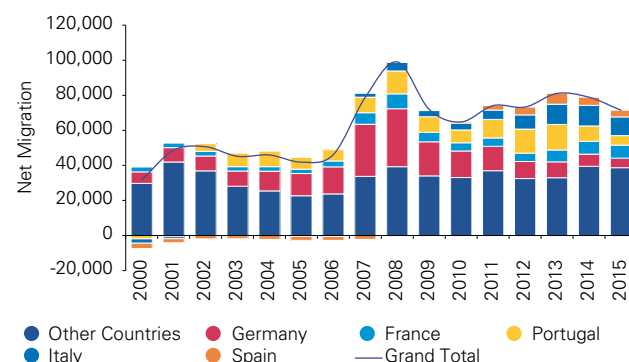


Source: SECO and KPMG

For the past year, the State Migration Secretariat reports net immigration of 71,500. Over the past five years, average annual net immigration has been 75,800. The fall in immigration can largely be explained by the weaker domestic economy.

A breakdown by country shows that Italians currently make up the largest group of immigrants, at 11,000, after a net emigration of Italians was still being recorded between 2000 and 2006. They are followed by the French, with over 7,000 immigrants. Germans and Portuguese are roughly on a par, with net immigration over 5,400 in each case. Compared to last year, a drop of 38% in Portuguese immigration can be seen, which can be accounted for not least by the trend towards consolidation in the construction industry.

#### Net Migration



Source: State Migration Secretariat and KPMG

Because of the weak economic outlook, we anticipate a further reduction in immigration figures in the current year. Depending on how the Mass Immigration Initiative is implemented, a marked fall in immigration figures can be expected once it is brought into force.

## Office Market

Despite a certain easing on the supply side, the market environment for office space remains competitive. At the end of October 2015, the volume of planning applications submitted stood 3% above its long-term average since 1994, although building permits were 7% below that level. Demand on the market for office premises has meant that, despite the pressure to invest, investors have been rather cautious in planning new office space, so that the existing imbalances have not been further accentuated.

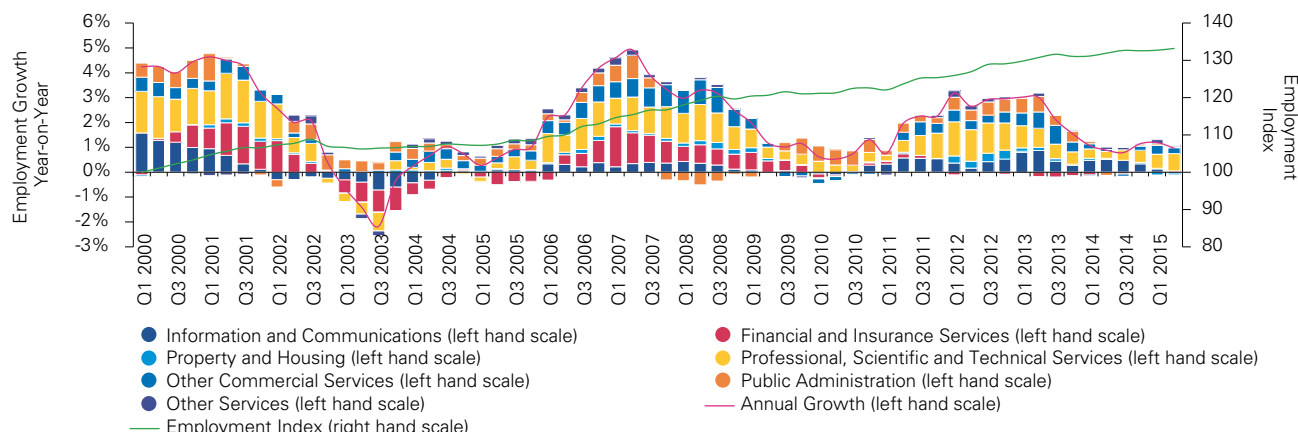
In view of the subdued trend in office employment, the significant expansion of supply in recent years and the rise in the vacancy rate, the limited expansion of supply is a welcome development. As many new-build developments are still only now being released onto the market, letting and reletting office space is likely to remain challenging.

Overall, since the end of the 1990s growth in office employment has turned out to be astonishingly robust in the face of economic upheaval. The employment figure stagnated only between 2002 and 2003; otherwise, demand for office employees has grown each year. The 2% growth in employment during the period from 2011 to 2013 has halved to 1% since 2014. In view of the moderately optimistic economic prospects, office employment should continue to grow at a similar rate this year and next.

The supply index for office space across Switzerland as a whole currently stands at 6.9%, an increase of 0.1



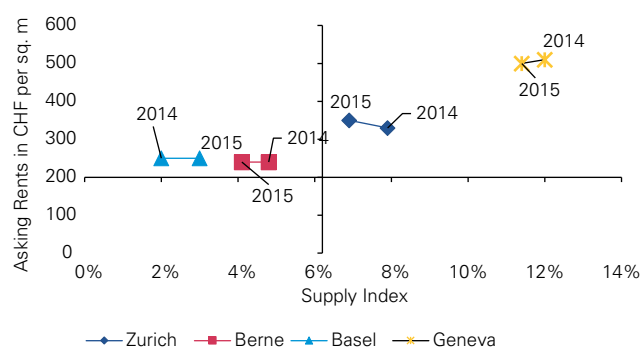
## Changes in Employment in Typical Office Occupations by Sector



Source: BFS and KPMG

percentage points compared to last year. Amongst the four largest Swiss cities, by far the highest supply index is recorded in Geneva, at 11.4% (last year: 12.0%). In Zurich, this figure stands at 6.9%. In Berne and Basel, availability of office space is more limited, at 4.1% and 3.0% respectively. Supply indices in recent years are also reflected in high levels of vacancy. At the start of June 2015, over 520,000 sq. m of vacant space were recorded in the four major urban office markets. This represents a marked increase of 33% compared to the previous year. An 80% rise in available space has been seen over a period of three years. The current vacancy level is also high in historic terms. Since 1999, a higher vacancy level has only been recorded in 2005 (545,000 sq. m).

## Supply Index and Asking Rents in the Major Centres



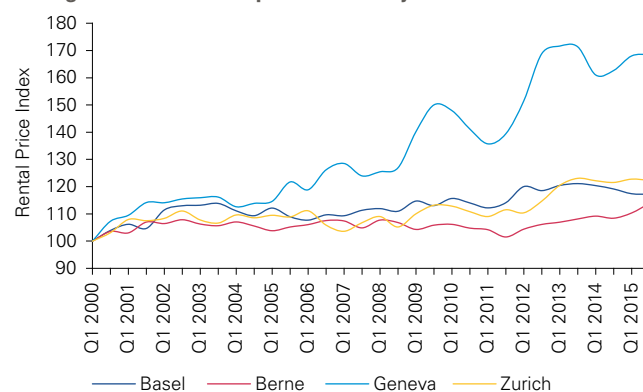
Source: W&P and KPMG

At 4.1%, the highest vacancy rates are currently seen in the cities of Geneva and Berne. In contrast, the recorded vacancy rate in Basel and Lausanne remains low, at 1.8% in each case. In Zurich, vacancies have fallen slightly, by 0.1 percentage points to 2.9%.

The very recent increases in the Index of Office Rents do not signal a reversal in the trend; rather, they can be

explained by the fact that recorded asking rents take no account either of changes in the quality of the supply or of concessions by landlords. Therefore, for example, a shift in availability towards smaller and in some cases fitted out premises will lead to a further rise in the Rental Price Index, whereas newly agreed rents have been stagnating or even falling for some time. In the rental index for new lease contracts, which is adjusted for qualitative effects, falls in rents can be seen in many locations. Between the mid-point of 2014 and the mid-point of 2015, average rents fell by 1.2%. This trend should accelerate during the current year.

## Asking Rents for Office Space in the Major Centres



Sources: W&P and KPMG

Weak demand and the relatively high supply of quality office space mean that tenants find themselves in an exceptionally comfortable position. As well as reductions in rent and concessions by landlords, they can count on a high degree of flexibility from landlords in structuring the duration of their leases. New lease contracts for business premises currently are most frequently being concluded for a fixed term of 5 years (frequently: 48.7% and very frequently: 44.9%). Next come 10 year leases (frequently: 46.1% and very frequently: 5.9%). A high proportion of newly concluded lease contracts

The relatively short terms of newly concluded lease contracts for business premises can be explained first by the current market environment and second by the requirements imposed on the modern workplace. As a result of current trends in the labour market such as the home office, outsourcing and shared workspace, firms are seeking a high degree of flexibility when structuring their leases. This leads to shorter terms and unilateral tenant break options. The trend towards shorter lease terms should be accentuated further by the proposed introduction of new accounting rules for leases.<sup>3</sup>

The chart displays the percentage of respondents for various office and retail space types, categorized by the change in demand. The Y-axis represents the percentage from 0% to 100% in 10% increments. The X-axis lists six categories: Central Business District (CBD: City Centre), Wider Business Area, Peripheral Locations, CBD and other well-frequented locations, Residential Districts and Built-up Areas, and Peripheral Locations. The bars are stacked with four categories: Significant Decrease (dark blue), Slight Decrease (red), Unchanged (light blue), and Significant Increase (yellow).

| Space Type                                   | Significant Decrease | Slight Decrease | Unchanged | Significant Increase |
|--|----------------------|-----------------|-----------|----------------------|
| Central Business District (CBD: City Centre) | 20%                  | 5%              | 10%       | 65%                  |
| Wider Business Area                          | 45%                  | 5%              | 10%       | 40%                  |
| Peripheral Locations                         | 70%                  | 5%              | 10%       | 15%                  |
| CBD and other well-frequented locations      | 5%                   | 2%              | 43%       | 50%                  |
| Residential Districts and Built-up Areas     | 35%                  | 10%             | 10%       | 45%                  |
| Peripheral Locations                         | 60%                  | 5%              | 10%       | 25%                  |

Regulatory uncertainty is also undermining the modest demand for office space. In this context, particular mention should be made of the implementation of the Mass Immigration Initiative and Business Tax Reform III (USR III).

Firms that do not know whether they are going to find sufficient qualified staff within Switzerland in the future tend not to be inclined to embark on major investment projects. According to a survey by Economiesuisse, more than 80% of respondent businesses expect investment and employment to fall if the Mass Immigration Initiative is strictly implemented. As a consequence, negative impacts on the office market are also emerging.

Since 2007, Switzerland has been experiencing increasing international pressure, particularly from the European Union, on the privileged tax regime applied to so-called “status companies” (mixed, domiciliary and “principal companies” and the financial sector). In response, the federal government and the cantons have produced the proposed USR III.

The current uncertainties surrounding the detailed implementation of USR III turn out to be detrimental to Switzerland as an international corporate location. Companies are delaying setting up or are actually setting up in other countries. However, if USR III is implemented successfully, we expect a positive impact on Switzerland's attractiveness as a location, which would also have a positive effect on the property investment market. We consider the lower standard rates for taxes on profits, combined with the patent box measures and research and development incentives to be well-suited to reinforce Switzerland's competitiveness.

More Action Needed    ■ ■ ■    Less Action Needed

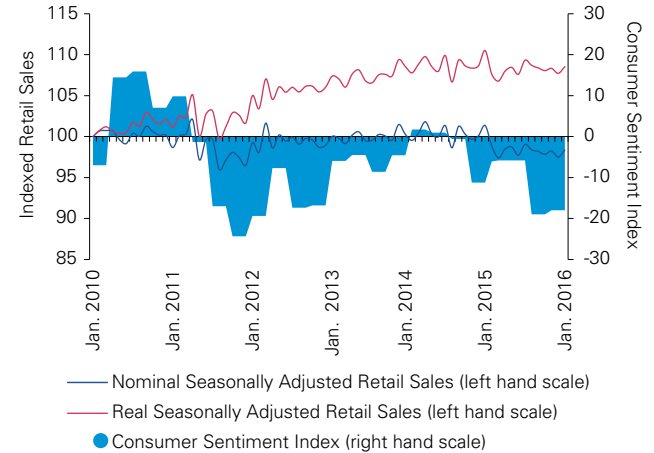
<sup>3</sup> Under IFRS 16, lease contracts will be included in the balance sheet.

# Retail Market

After the currency shock of January 2015, retailers began the year with significant falls in sales. Sales did recover slightly over the course of the year, but this could not prevent a negative year-end result. At the end of 2015, despite the growth in population, nominal retail sales fell by 3% compared to 2014 (0% in real terms).<sup>4</sup> The main driver behind the fall in sales was the continued strength of the Franc, encouraging consumers to purchase abroad. The volume of foreign purchases, at around CHF 10.7 billion, increased by a further 6% compared to 2014. Furthermore, towards the end of the year consumer confidence fell to -18 points, placing it below the long-term average of -9 points once more, after positive prospects at the start of the year.

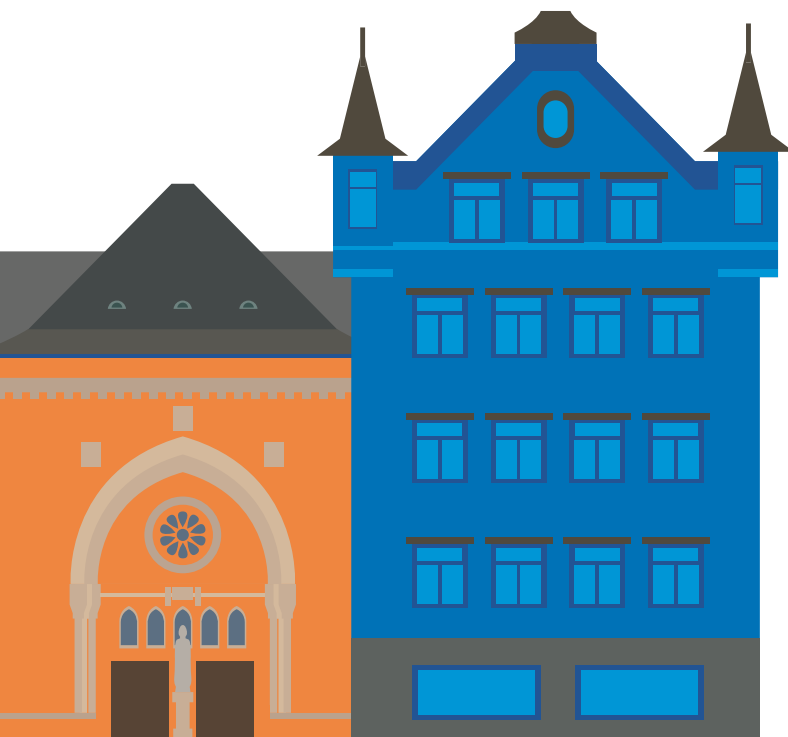
<sup>4</sup> The difference between nominal and real sales figures is due to the fall in prices for convenience goods.

**Retail Sales and Consumer Sentiment**



Source: BFS, seco and KPMG

Moreover, over-the-counter retail lost further market share at the expense of online retail in 2015. Whilst overall retail sales are stagnating, we expect online retail sales to increase in 2016. In 2015, online retail accounted for 7.5% of retail sales, excluding fuel. If online retail continues to grow at the same pace as over the past eight years, it can be expected to make up 9.8% of retail sales by 2020 on conservative estimates. After a period in which pure online retailers such as Zalando have been entering the market, further movements can be expected as over-the-counter retailers build up their online businesses. Today, a retailer which does not have an online division is unlikely to survive, as is shown by the examples of Migros with its acquisition of Galaxus, or the Siroop joint venture between Coop and Swisscom. For example, with growth of 4.1% in 2015, online sales were also taking a growing share of the Coop group turnover. As online stores become increasingly important, demand from retailers for space will shift towards smaller collection points and requirements for logistic premises will alter. Online retail also offers benefits in terms of collecting data on customer behaviour. With the increasing digitisation of sales outlets, over-the-counter retailers will also further develop their data collection. It will become increasingly important to measure the flow of passers-by, to record purchasing behaviour and to react immediately to customer feedback. The use and further development of existing technologies could improve the position of over-the-counter retailers in the near future and reduce the current information imbalance compared to online retailers. However, in this context, there are also issues regarding data protection. Consumers are likely to be more sensitive on this issue in the offline world than might be expected from their readiness to divulge information in the online environment.



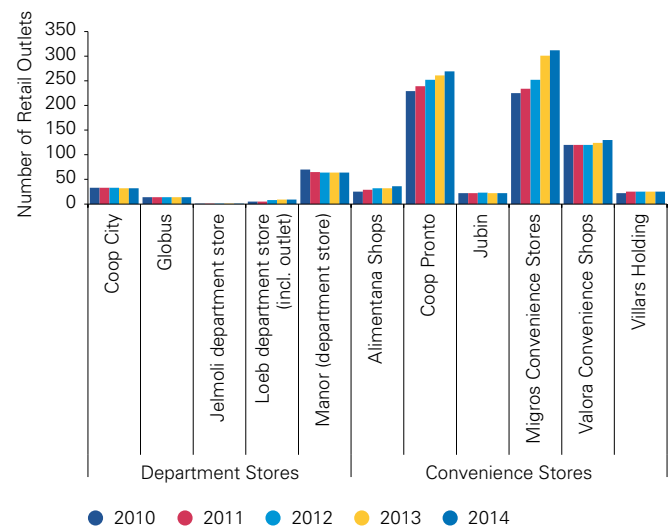
### Forecast Online Sales as a Proportion of Retail Sales



Source: BFS, GfK and KPMG  
F – Forecast

Despite stagnating sales in over-the-counter retail, due to competitive pressures and crowding out, up until now hardly any retailers have given up premises. Therefore, the number of large department stores remained unchanged in 2014 compared to the previous year. Proximity to customers, with fast access and easy availability, is becoming increasingly important. This is also supported by the growing number of convenience stores. Therefore, for example, Migros and Coop, the two sectoral leaders, have increased the number of their convenience stores over the past year by 3.7% (Migros) and 3.1% (Coop). In addition, with its “Take It” format, Coop is testing a new freshly-prepared take away offering, including small store formats in busy locations. According to the most recent media reports, both Coop (+2.3%) and Migros (+1.7%) increased the number of their retail outlets again in 2015.

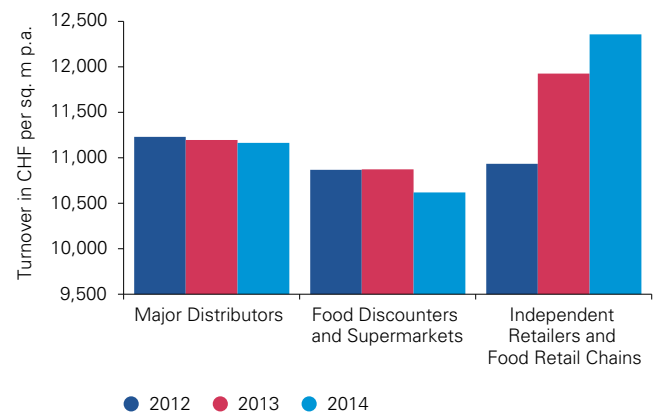
### Number of Department Stores and Convenience Store Outlets



Source: GfK and KPMG

The expansion in space in the food sector, despite stagnating sales, is resulting in a fall in sales productivity at the major distributors, the food discounters and the supermarkets. In contrast, the independent retailers and food retail chains have been able to increase sales productivity to over CHF 12,000 per sq. m p.a.

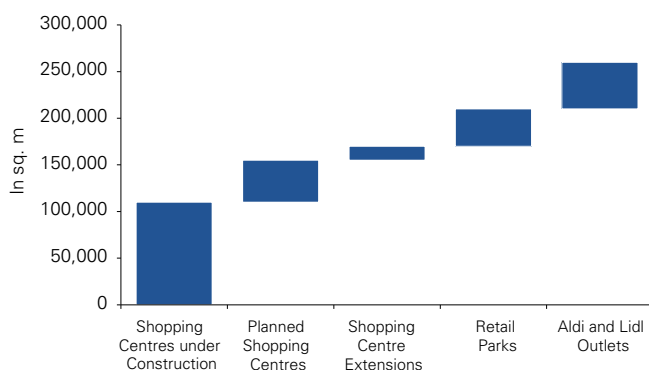
### Sales Productivity by Category



Source: GfK and KPMG

The increase in competitive pressure in retailing has also left traces on the property investment market. Investors and developers are becoming increasingly cautious. As a result, the volume of planning applications in January 2016 fell by 6.8% compared to the previous year, to CHF 313 million. Planned expansions in space over the next three years also declined in 2015 compared to the previous year, by 13.5% to 260,000 sq. m.

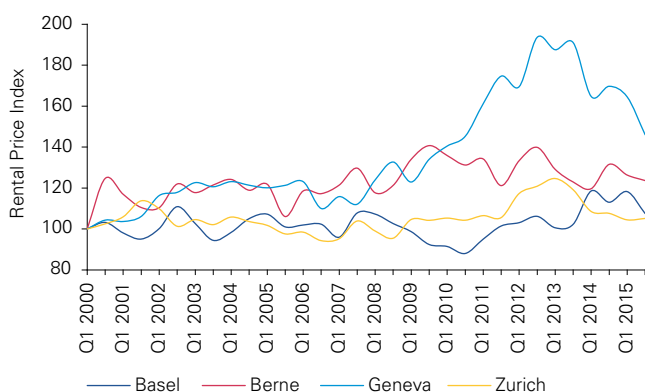
### Swiss Retail Expansion 2015 to 2017



Source: GfK and KPMG

As well as the reduction in the construction of new space, the falling asking rents for retail space in the major centres suggest saturation. In all four of the major centres, both average asking rents and prime rents for retail premises have fallen.

### Asking Rents for Retail Space in the Major Centres



Source: W&P and KPMG

Compared to asking rents, the rise in vacancies has been disproportionately low. The reason for this is the increased competitive pressure in the retail sector and occupiers holding on to existing premises. In peripheral locations, saturation has become much more noticeable.

Overall, the environment for the retail premises market remains challenging. Falling values and overall yields can therefore also be anticipated for 2016. However, as constant availability becomes more important, there is still potential for specific projects orientated around the change in consumer behaviour and for retail space in locations with a high footfall.



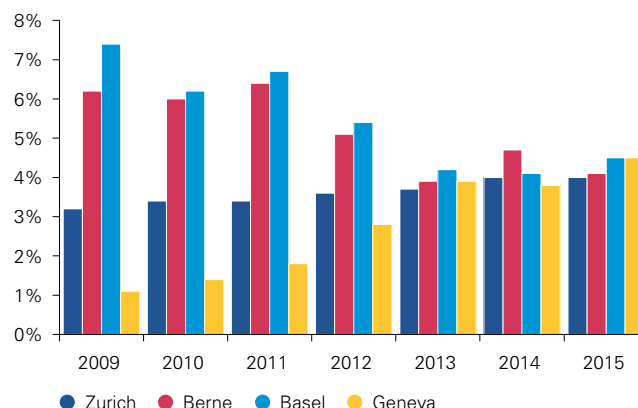
# Residential Market

Thanks to continuing immigration, the trend in demand for rented homes has so far been robust, but the increased supply of residential properties has now over-compensated for it.

Due to the low interest rate environment and the resulting shortage of suitable investment opportunities, investment in residential properties has enjoyed the favour of investors for years. Furthermore, the high prices of some owner-occupied apartments and the stricter financing requirements for owner-occupiers has had a positive impact on demand for rented homes. Nonetheless, very recently, a consolidation in construction activity has been seen in relation to rental apartments. According to Credit Suisse, as at the end of Q3, the 12-month total stood at 25,800 rental apartments, that is about the same as the figure for the previous year. However, in the conurbations, construction activity has been in decline since 2013. Construction activity in the major centres has been stagnating more or less at the level reached at the mid-point of 2014. In contrast, the number of residential building permits granted in municipalities outside the conurbations and in tourist areas is increasing. Building permits for rental apartments have recently fallen back to their previous level, after a brief boost resulting from the second homes initiative<sup>5</sup>.

The high level of construction activity and slight fall in immigration have led to a marginal easing in the cities, where a shortage of housing had prevailed. Even major centres such as Geneva, Lausanne or Basel, which had long stood out for their lack of housing, are currently recording availability rates of around 4.5%.

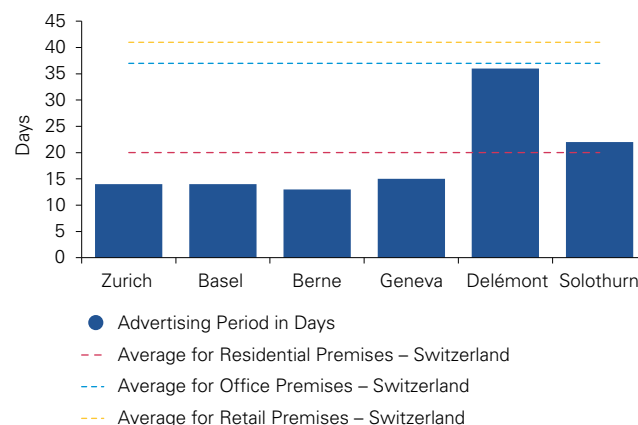
Supply Indices for Rented Homes



Sources: W&P and KPMG

In and around Switzerland's four largest cities, not only does vacancy remain low, but also the time period for which rental homes are advertised has been shorter. In Zurich and Basel, the median advertising period is 14 days. In Berne and Geneva, it is 13 and 15 days respectively. In comparison: in Delémont or Solothurn, the figures are 36 and 22 days respectively; the average for Switzerland is 21 days.

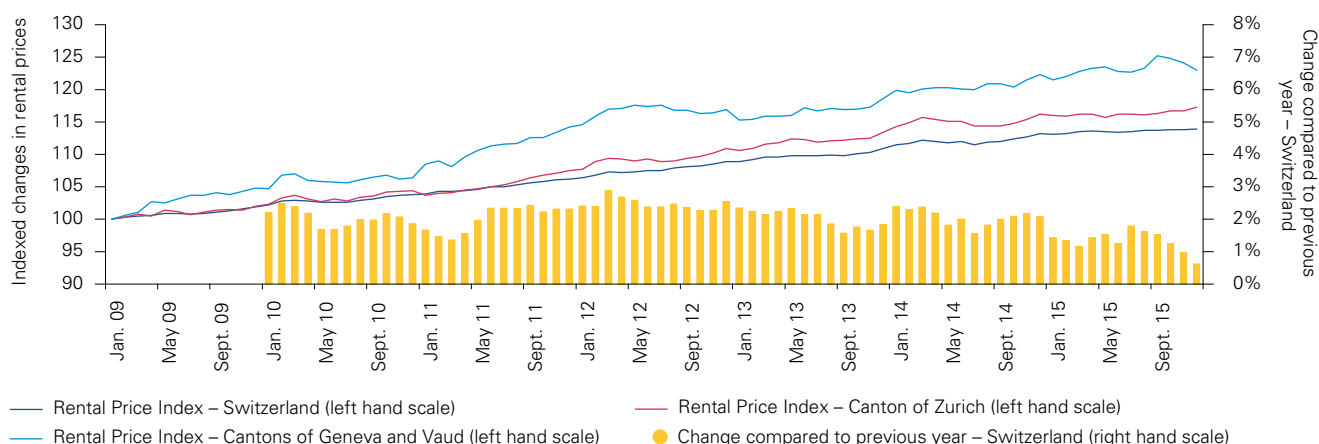
Average Advertising Period for Rental Homes



Source: immodatacockpit and KPMG Real

<sup>5</sup> The transitional regulations in the second homes initiative (ordinance governing secondary residences) have been in force since 1<sup>st</sup> January 2013. The secondary residences act is in force since 1<sup>st</sup> January 2016.

## Index of Asking Rents, after Qualitative Adjustment

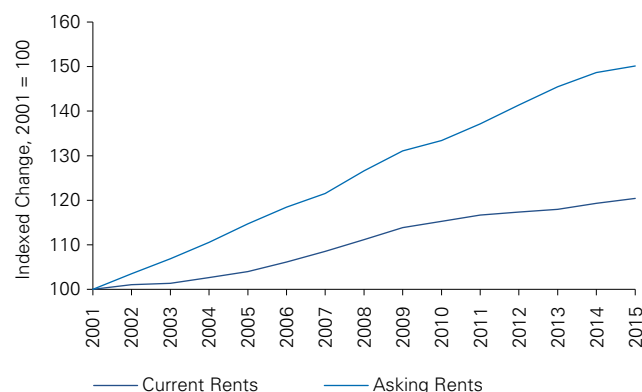


Sources: Homegate.ch, ZKB and KPMG

The weakening in year-on-year rental growth has continued. According to Homegate.ch and ZKB<sup>6</sup>, in 2015 asking rents for rented homes, after qualitative adjustment, rose only marginally by 0.6% across the whole of Switzerland compared to the previous year (2014: 2.1%). The highest increases were recorded in Cantons of Basel (1.9%) and Solothurn (1.5%). In contrast, asking rents have remained almost stable in Cantons of Zurich (0.9%), Vaud and Geneva (0.6%).

In contrast to asking rents, rents under existing leases have been affected by reductions in reference interest rates in recent years. The crucial mortgage reference interest rate has fallen from 3.50% in 2008 to 1.75% at the mid-point of 2015 and could even reach a record low of 1.50%. Therefore, in the case of existing properties, in recent years it has been possible to realise rental potential only when there is a change of tenant or following value-enhancing investments. An analysis at lease contract level shows that so far there has been no wholesale reduction of rents under existing leases because of the reductions in reference interest rates. In consequence, for a large proportion of leases there is only limited potential to increase rents, even if interest rates rise.

## Indexed Changes in Rents under Existing Leases and Asking Rents



Source: W&P, BFS and KPMG

The impact of the moderate economic recovery should not be strong enough to interrupt the trend of falling immigration. Experience shows that there is some delay in the response of net immigration to changes in employment growth. This has halved over the past two years, from 2% to 1%. Combined with the continued strong supply of rental apartments, we therefore anticipate a slight increase in vacancies and falling rents across the whole of Switzerland.

<sup>6</sup> The index measures the monthly changes in rental prices for new and existing rental apartments, after qualitative adjustment.

# Direct Property Investments

By shifting the target interest rate range into negative territory, the abolition of the exchange rate mechanism by the SNB gave further impetus to property investment prices. This drastic measure may have dampened economic prospects, but at the same time it also boosted the relative attractiveness of investments in property. Multi-asset investors such as insurers and pension funds are seeking alternatives to the very low yields from fixed-interest investments. According to the Credit Suisse pension fund index, at the end of December 2015 the proportion of real estate in pension fund investments stood at over 22%, reaching an all time high. Clearly there is no means of avoiding real estate investment.

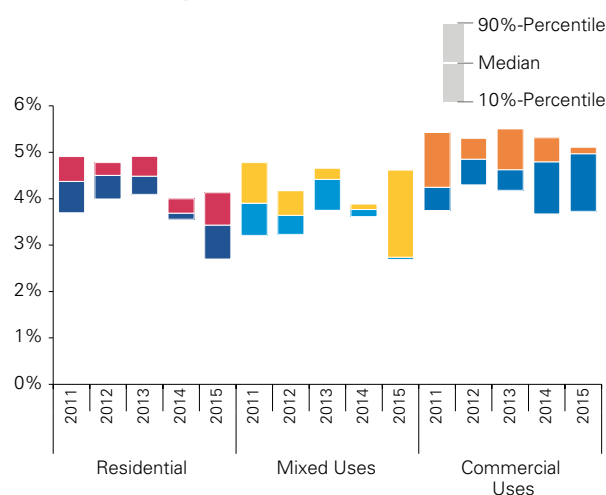
Overall pension fund performance across all asset classes over the past year stood at a meagre 0.95%. That is less than the minimum interest which pension funds are required to credit to their policyholders, and it lies below the target yields which the funds require in order to fulfil their long-term obligations. According to ASIP, the pension fund association, in 2015 direct property investments in Switzerland in a pension fund portfolio yielded a median of 5.3%. Therefore, property investments made a decisive contribution to the positive overall yield amidst the turbulence of the capital market environment. In the past, property was held primarily as a yield-to-risk optimiser, because of the low correlation between its performance and that of other asset classes. In the present environment, property yields have taken on a new function as a yield maximiser, and they are used in order to achieve above average returns.

In the last Spring edition of the Swiss Real SnapShot! we predicted that the property investment market would split in

two as a result of the abolition of the exchange rate mechanism by the SNB. We included income-generating residential properties amongst the beneficiaries of this step. We were rather critical of investments in commercial properties. Trends in transaction-based cash flow yields<sup>7</sup> reinforce that appraisal. If according to REIDA, cash flow yields for residential properties still stood at 4.4% in 2011, in 2015 they were only at 3.4%. Compared to 2014, in 2015 the cash flow yield fell by over 25 bps.

The opposite can be seen for commercial properties. For investments in these properties, a slight increase in cash flow yields was seen in 2015 compared to 2014; this is linked to a slight fall in sale prices.

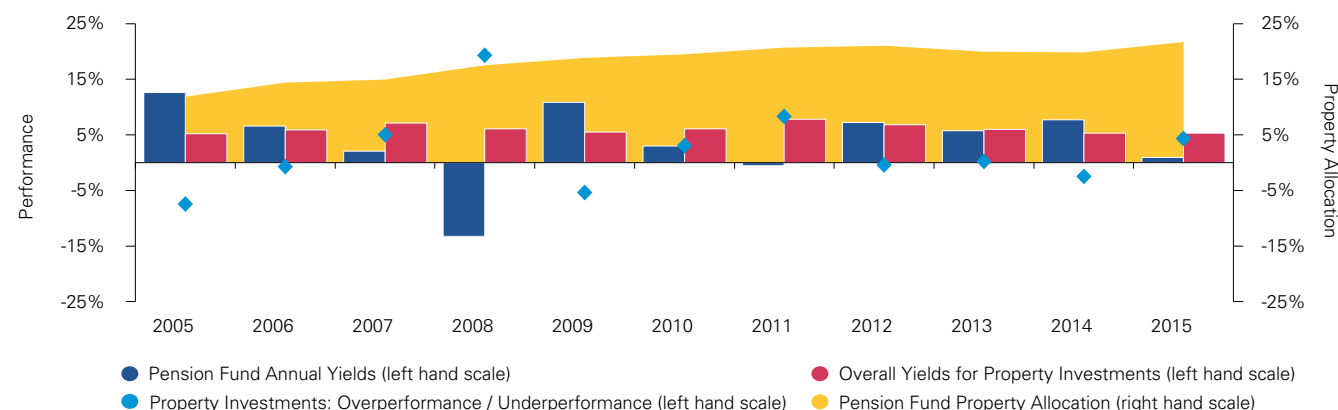
Cash Flow Yield by Use



Source: REIDA and KPMG

<sup>7</sup> Cash flow yield = (net rental receipts less capitalised repairs) / transaction price

Property Investment Performance and Property Allocations of Pension Funds

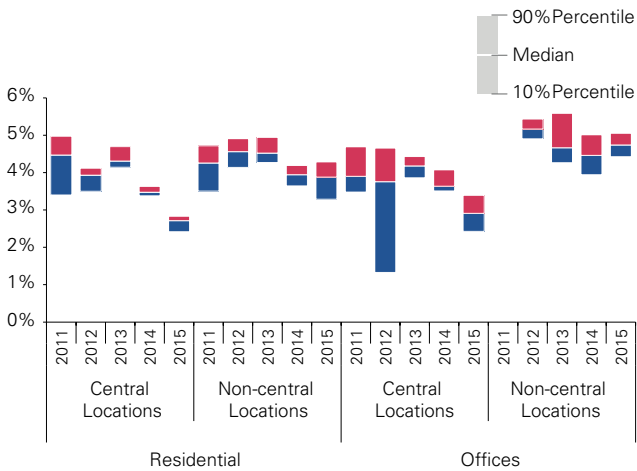


Source: Credit Suisse, IPD, ASIP and KPMG



A breakdown by location quality shows that it is mainly central locations<sup>8</sup> which have experienced price increases. In 2015, the median cash flow yield for residential properties in central locations stood at 2.7% (2014: 3.5%). In contrast, the median yield for non-central locations remained unchanged from 2014, at 3.9%. This preference for residential properties and central locations points to a strong aversion to risk amongst market players. Investors consider the values of such investments to be more stable. We anticipate a continuing divergence between yields for residential and business properties in the current year.

Cash Flow Yields by Location and Use



Source: REIDA and KPMG

<sup>8</sup> The overall yield on quoted property investments is measured using the SXI Real Estate Total Return Index.



# Indirect Property Investments

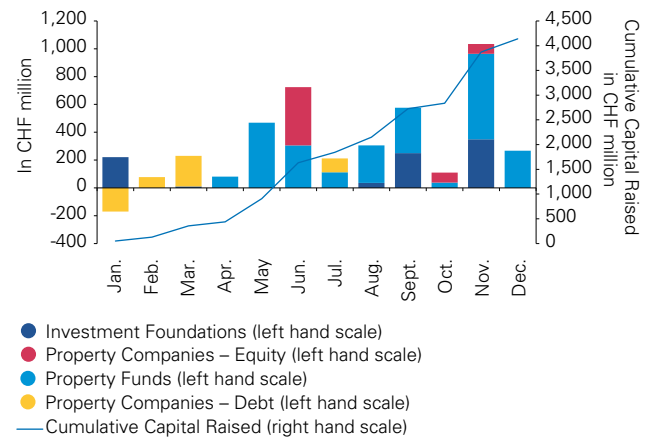
In the past year, indirect property investments recorded a strong performance overall. Quoted property investments boasted overall average performance of nearly +6% (previous year: +15%).<sup>9</sup> Broken down by investment vehicle, it appears that property companies (+10%) achieved a far higher overall return than property funds (+4%).

Despite the weaker overall performance compared to the previous year, more activity was seen on the capital market. In 2015, Swiss property investment vehicles<sup>10</sup> secured investment funds (equity and loan capital) of nearly CHF 4.1 billion. According to UBS, this was the highest since 2007. The great attractiveness to investors can be explained not least by the monetary measures introduced by the SNB on January 15, 2015. The abolition of the exchange rate mechanism was accompanied by a fall in the rate of interest payable on credit balances in current accounts and a reduction in the target range for three month Libor. Because of these measures, major institutional investors have, in some cases, had to accept negative interest rates on their cash holdings since then. At the same time, the already low federal bond yields fell further. So it is hardly surprising that, because of their stable dividend yields, indirect property investments are a popular substitute for long-term bonds.

<sup>9</sup> The overall yield on quoted property investments is measured using the SXI Real Estate Total Return Index.

<sup>10</sup> In this analysis we investigated Swiss property funds, property companies and investment foundations.

Capital Flows into Indirect Property Investments, Switzerland

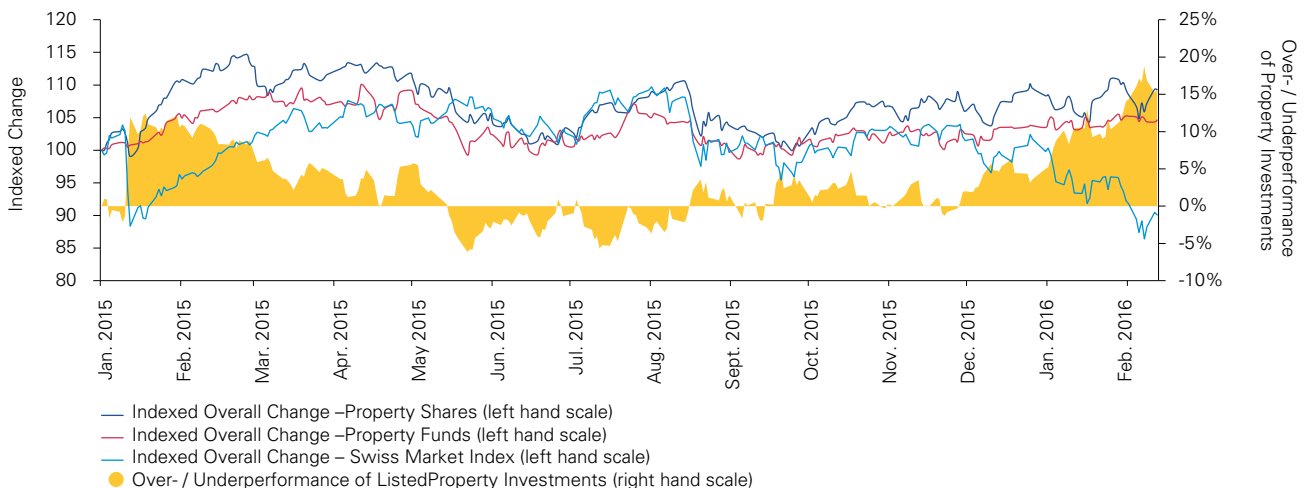


Source: Bank J. Safra Sarasin and KPMG

Many property investment providers made use of market conditions to raise capital or to launch new products. With around 60% of the extra investor money, property funds raised by far the greatest amount of capital. 21% of investors' capital went to investment foundations and 19% to property companies.

Amongst investment funds, we must highlight the launch of Swiss Life's "REF Swiss Properties" (CHF 450 million) focused on residential uses. The property portfolio originates from Swiss Life's insurance holdings. The financial supervisory authorities granted this transaction an exemption from the prohibition on acquisitions and transfers (Capital Investments Act [KAG] Art. 63). Another new launch was the "SF Retail Properties Fund" from Swiss Finance and Property, with a focus on retail premises, to the sum of CHF 270 million. Amongst the established property funds,

## Trends in Listed Property Investments



Source: SWX, SNB and KPMG

UBS's "Siat" fund undertook the greatest capital increase in 2015, of around CHF 239 million. Other large issues were placed by UBS's "Foncipars" (CHF 177 million), Mobiliar's "MobiFonds Swiss Property" (CHF 154 million), Credit Suisse's "Interswiss" (CHF 149 million) and UBS's "Swissreal" (CHF 128 million).

Property companies also obtained additional funds in 2015 by taking up new debt capital (CHF 230 million) and equity capital (CHF 560 million).<sup>11</sup> Amongst issues of debt capital, we should mention issues of fixed-rate bonds by Allreal (CHF 220 million) and Intershop Holding AG (CHF 100 million). The sector leader Swiss Prime Site used the positive movements in the value of its registered shares to convert over 90% of a convertible bond issue of CHF 300 million to equity capital. Furthermore, Wardeck Invest AG undertook a successful equity capital increase with gross proceeds of nearly CHF 77 million. In the past year, the properties company Plaza Immobilien AG also went public. The surplus properties of the Conzzeta corporation were listed as Plaza AG on the SIX Swiss Exchange.

Investment foundations were able to raise new funds to a total sum of CHF 870 million. The largest share of this came from the launch of an investment foundation for residential property by Swiss Prime Site ("SPA Immobilien Schweiz"). On its first issue, it took in funds of CHF 550 million. The

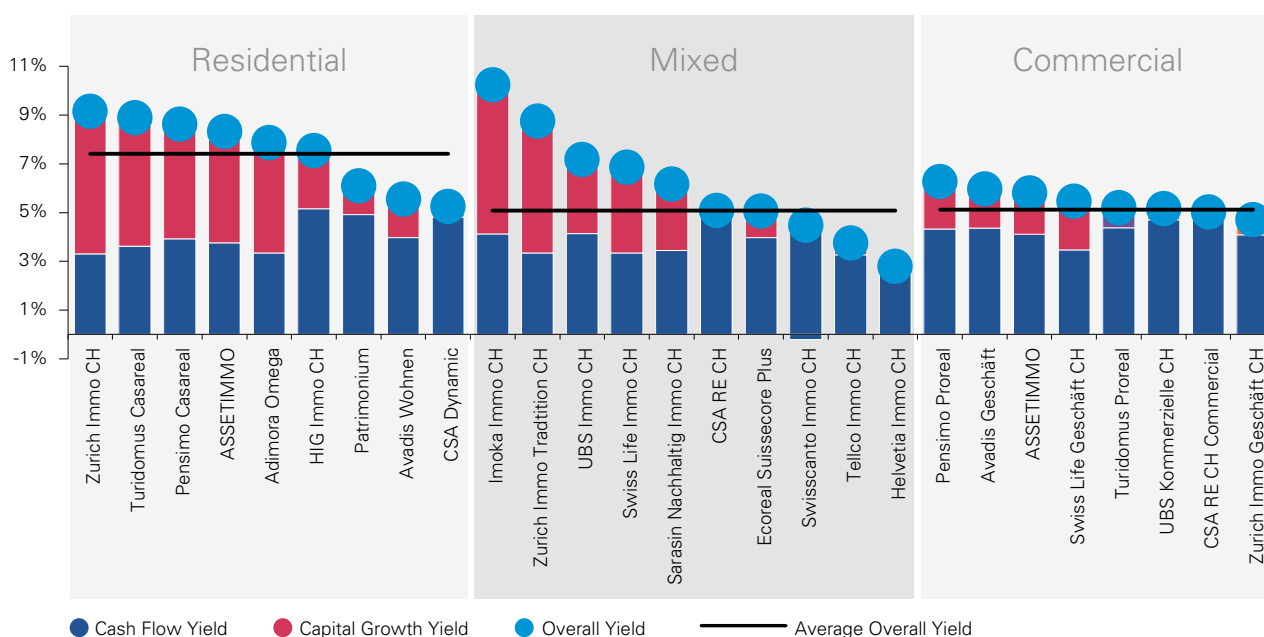
Credit Suisse Investment Foundation took in CHF 221 million by way of capital increases by its "Residential" and "Commercial" investment groups. Both relaunches were several times oversubscribed ("Residential" twenty-seven times and "Commercial" twice). The massive oversubscription of the investment group focusing on residential properties underlines the current investor preference for this segment.

Portfolio managers used the additional funds mainly to expand their property portfolios and to realise potential for consolidation and building extensions. The surplus of demand makes it difficult to invest fresh capital in acquisitions to expand portfolios. Moreover, portfolio managers find themselves confronted by a trilemma between the three objectives of growing their portfolios, securing their return and maintaining their risk profiles. With a given risk profile, at present it is actually only possible to acquire investment properties with lower yields than the existing portfolio, which inevitably leads to a dilution of yield.

Over the past year, property investment foundations (KGAST Index) recorded an overall yield of 5.8% (previous year: 5.1%). A breakdown of this performance shows that here too there were marked differences between individual investment segments. By far the best performance was recorded by investment foundations focused on residential properties (7.4%). They are followed by mixed vehicles and commercial investment foundations, each with an overall yield of 5.1%.

<sup>11</sup> Conversions from debt to equity capital or buy-backs of securities were excluded from our review of debt capital volumes.

#### Performance of Investment Foundations in 2015



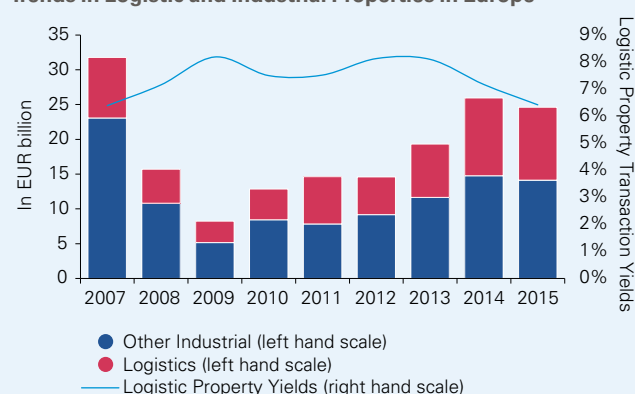
Source: KGAST and KPMG

The differences in overall yields are the result mainly of differences in capital growth yields and less from differences in income yields. Therefore, capital growth yields for residential properties stood at 3.5%, whilst in the mixed (0.9%) and commercial segment (0.8%) only moderate capital growth was recorded. This trend is consistent with the tendencies seen in the transaction market.

## Market for Logistic Properties

Over the past year, logistic properties valued at EUR 10 billion changed hands in Europe. A further EUR 14 billion of industrial properties can be added to this. The volume of transactions in this asset class has more than trebled since its low point in 2009. The increased interest in logistic properties has at the same time led to a compression of yields. In 2009, yields for logistic properties stood at over 8%; since then they have reduced to around 6.5%.

**Trends in Logistic and Industrial Properties in Europe**

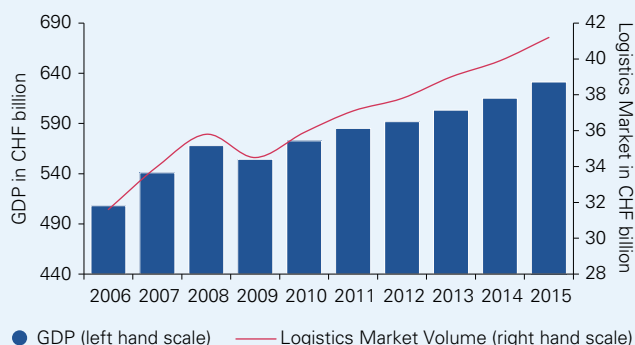


Source: Real Capital Analytics and KPMG

There have been established and professional markets with investors specialising in logistic properties in the USA and Europe for years. Their business models range from development projects by way of investment and asset management to pure advisory services. In Switzerland too, logistic properties have now become established as a specific asset class. There are already several investment vehicles focusing on logistic properties. They include the CS "Logisticsplus" property fund and the fund provider Procimmo, which has already launched four vehicles focusing on industry/logistics. These vehicles hold investment properties totalling CHF 1.5 billion. This represents around 4% of the property holdings of the quoted property funds and property companies. According to a non-exhaustive analysis by Real Capital Analytics, logistic properties with a value of around CHF 350 million changed hands in 2015.

The high significance of the logistics sector suggests that there is substantial growth potential for investments in logistic properties. HSG's study of the logistics market estimates the volume of that market at more than CHF 40 billion, and since 2006 it has grown more quickly than GDP, at an average of 3%.

### Trends in the Swiss Logistics Market

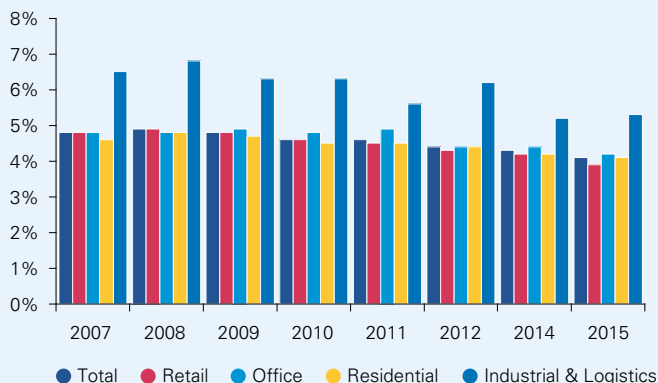


Source: HSG logistics market study and KPMG

The range of logistic properties is broad, extending from basic warehouse sheds, including transshipment sheds, distribution centres, business parks and high-bay warehouses, as well as specialist properties for the pharmaceuticals and food industries, to the most modern logistics parks. The diversity makes for substantial differences between yield requirements and also means that there are substantial differences between the demands made of investors, depending on the type of logistic property.

Logistic properties are often distinguished by long lease terms and indexed rents, as well as higher yields compared to other property types. In return, investors have to accept higher vacancy and cluster risks. Location, alternative / third party use potential and the occupier's creditworthiness are the most important considerations when identifying a profitable logistic property investment. Also, the investor must consider whether it wishes to operate the property itself (operating and management contracts) or whether it will remain passively in the background, relying on "structure and fabric" leases.

### Income Yields for Swiss Logistic and Industrial Properties



Sources: IPD and KPMG

The most important location factors for logistic properties are access to the commercial conurbations and infrastructure and supply routes. In Switzerland, the roads remain the most important means of transport: in terms of weight volume, over 85% of goods are transported across the country by road. Rail plays an important role particularly in long distance transport. Logistic buildings are therefore concentrated particularly on the main Swiss transport axes, especially along the A1 motorway. They are in particular noticeable around the A1/A2 motorway junction, which marks the centre of Switzerland from a transport perspective. Other logistics hotspots are Greater Berne and Greater Zurich, and also the frontier regions around Basel and Geneva, and in Ticino.

Demand for logistic properties is volatile and primarily dependent upon developments in the market for goods (industry, wholesaling and retail). To a significant degree, investments in logistic properties therefore run in parallel with growth in retail sales and export volumes. Besides these economic demand considerations, the logistics market is also strongly driven by structural changes. The continuing trend towards a subdivision of production processes means that more and more primary products and partially finished goods must be moved.

A further trend which should increasingly shape changes in demand for logistic properties is the rise in the importance of e-commerce and multi-channel retail. This trend is already leading to a displacement of a portion of the demand for retail space to logistic premises, because "door-to-door" logistics chains are partially replacing over-the-counter retail. Whilst overall retail stagnated in 2015, online retail sales rose by 6.0% to CHF 7.3 billion. The requirements and locational characteristics of the distribution centres of carriers in the e-commerce supply chain are different from those of traditional logistic properties, whose arrangement and location are designed to supply goods to shops. Large parcel operator sorting centres and food retailer fulfilment centres are representative of the new logistic properties<sup>12</sup>. This is leading to the emergence of a new logistic property market, which brings changes and opportunities for occupiers, developers and investors in equal measure.

<sup>12</sup> Order fulfilment duties are often entrusted to specialised logistics providers, which are then designated as "fulfilment centres". The term "fulfilment" is found mainly in association with online retail. In these cases, the logistics provider takes on all duties which take place after an online order is placed. The operator of the online store has transferred these duties to a specialist.

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- Structuring and execution of transactions (Lead Advisory)
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- Arrangement of indirect investments, such as funds or trusts
- Fund raising for specific projects
- Debt & Capital Market 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**

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  - Business planning/business modelling
  - Corporate/public real estate management
  - Asset and portfolio management
- Analysis of organization and processes; organizational development, internal control system (ICS)
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- Risk management and financial modelling
- Turnaround and Restructuring
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