BNP PARIBAS REAL ESTATE

Real Estate for a changing world

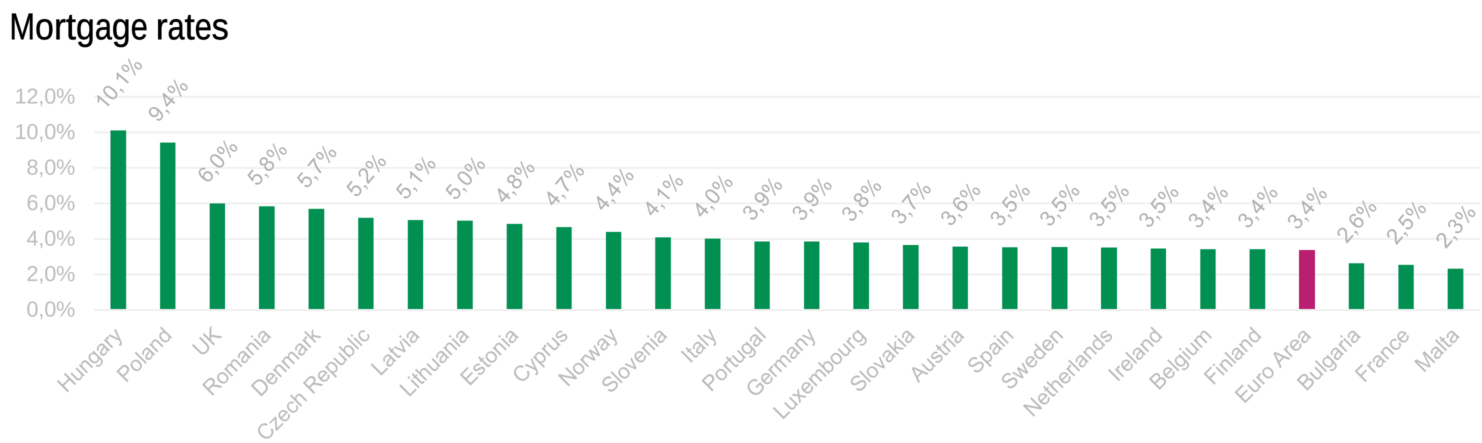
RESEARCH

AT A GLANCE H2 2022

European residential markets

THE PIVOT IN ECB MONETARY POLICY IS WORSENING THE HOUSING AFFORDABILITY. PRICES ARE NOW IN AN ADJUSTMENT PHASE.

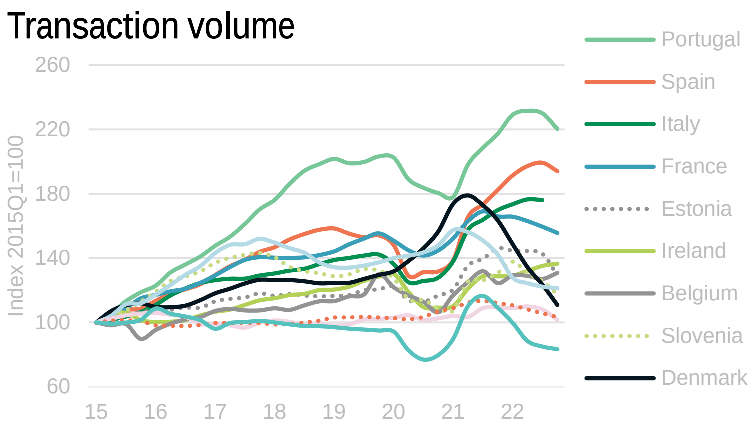
SIGNIFICANT RISE IN MORTGAGE RATES



- The ECB decided to raise the three key interest rates by 25 basis points in May. Accordingly, the interest rate on the main refinancing operations will be increased to 3.75%. This is the fastest increase in the Euro's history.
- The average mortgage rate in Europe has risen from 1.31% at the end of 2021 to 3.4% in Q1 2023: +206bps in 5 quarters. The largest increases are observed in the Nordics and Eastern Europe (Hungary +570 bps, Poland +447 bps, the United Kingdom +390bps, Denmark +320 bps, Lithuania +296bps , Slovakia +272bps, Finland +264 bps and Germany +253 bps).
- The 12-month Euribor reached 3.62% in Q1 2023, +412 bps since Q4 2021, paving the way for stronger growth in mortgage rates in the coming months.

TRANSACTIONS ARE COOLING DOWN

- Housing transaction volume dropped by 6.9% in Q4 2022 on a rolling year basis.
- The slowdown is driven by several factors: the tightening in credit conditions, the significant increase in mortgage rates and of course the constant increase in house prices. Consequently, we observe a significant worsening of housing affordability triggering a decline in the number of transactions.
- Housing transactions declined by 32% in Denmark, -24% in the United Kingdom, -15% in the Netherlands. The decline is more moderate in France (-6.2%), Norway (-7.7%) and Sweden (-7.1%).

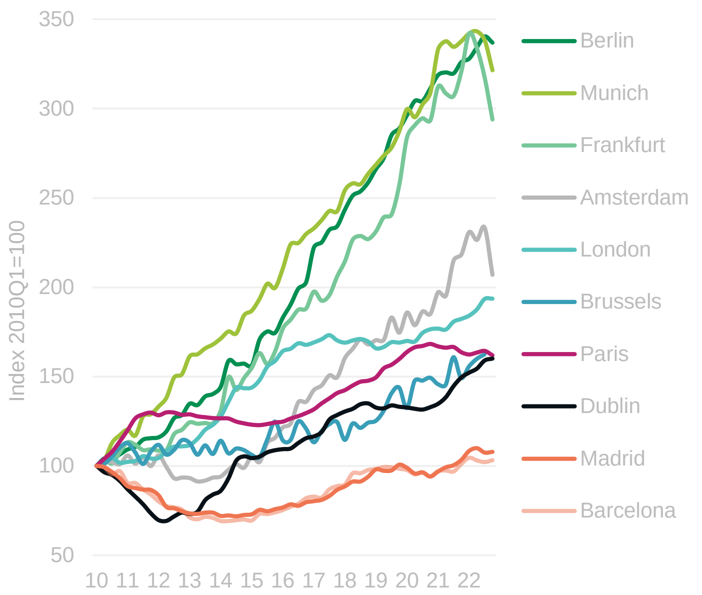


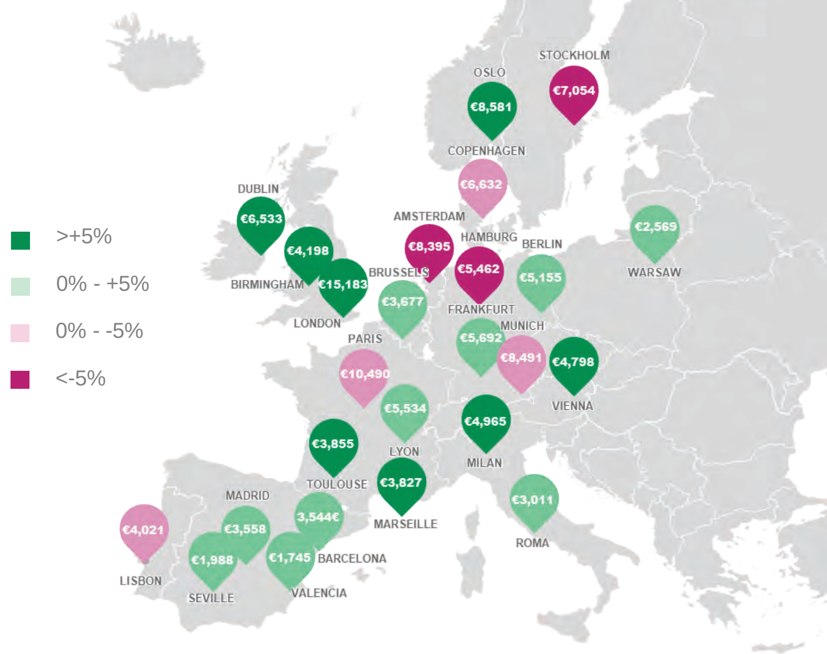
3.4% Average mortgage rates

-6.9% Over a year

HOUSE PRICES IN AN ADJUSTMENT PHASE

Residential price growth

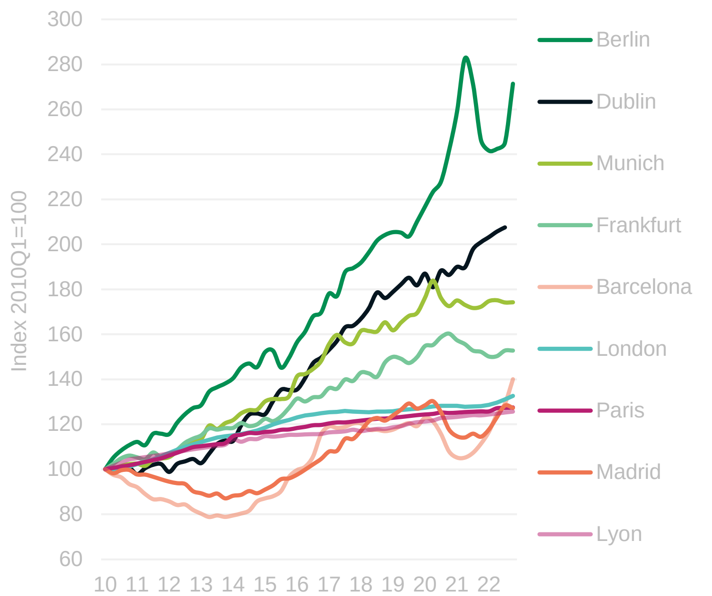


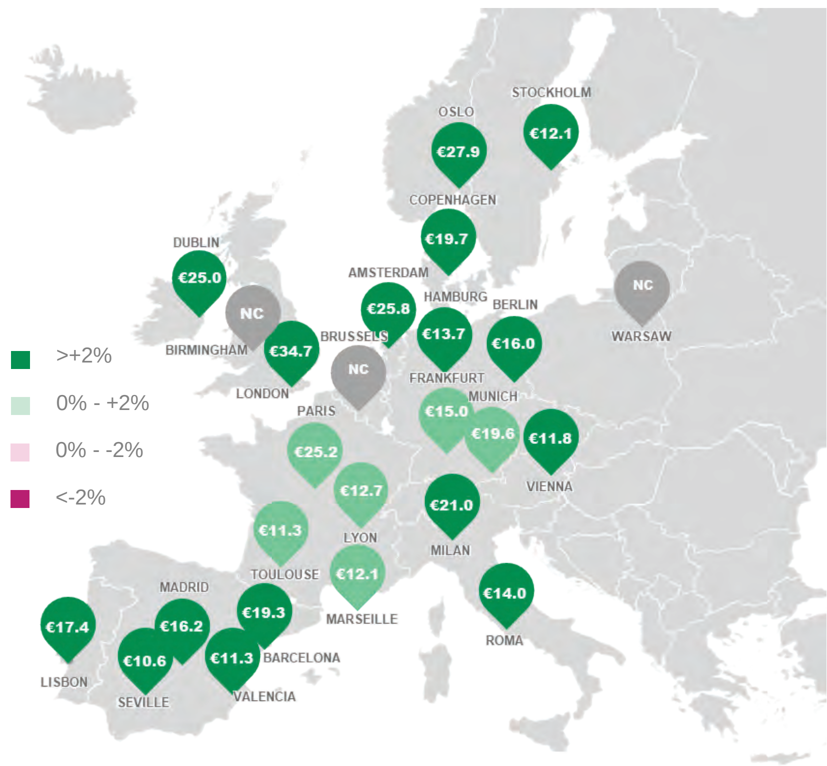


- House prices across European cities continue to rise, but at a slower pace, recording +2.8% y/y in Q4 2022 vs 6.7% y/y in Q1 2022.
- House prices start to decline slightly in 20 cities out of the 28 we monitor since the peak was reached over the last 2 years. For instance, house prices declined by -14% in Frankfurt, -12% in Prague, -11% in Stockholm and Amsterdam, -8% in Rotterdam and around -6% in Munich, Hamburg and Copenhagen.
- As result of interest rate hikes, the housing market is cooling down and the demand is moving toward cheaper markets such as suburbs.

RENTS INCREASING AS DEMAND PICKS UP

Residential rent growth





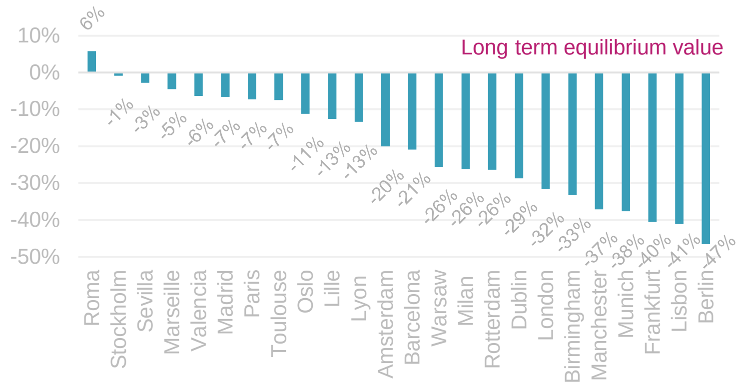
- Residential rental values across European markets are booming at +8.1% y/y.
- Since the beginning of 2022, we have seen a sharp increase in demand for rental properties owing to hikes in mortgage rates and the decline in the affordability of buying. As a consequence, numbers of rental dwellings listed in web platforms shrunk dramatically putting strong pressure on rental values.
- The spread between the cost of buying vs the cost of renting in main markets is fuelling rents. We record a double digit growth in 9 markets out of the 23 we monitor: Lisbon (+30.8%), Barcelona (+25.7%), Valencia (+20.9%), Prague (+18.4%), Oslo (+13.4%), Madrid (+11.2%), Milan (+11.1%), Amsterdam (+10.8%) and Berlin (+10.1%).

DROP IN AFFORDABILITY AND RISK OF OVERVALUATION IN MOST MARKETS

- The affordability index enables the computation of the volume of square meters a household can purchase earning a local median income, borrowing money over 20 years at the local mortgage rate, for a local average price per square meter.

- Comparing the affordability ratio, i.e. the number of square meter in Q4 2022 with the long term equilibrium value, we are able to assess the risk of overvaluation of each market regarding their affordability. Markets such as Roma is undervalued because households can afford between 6% more sqm compared to their equilibrium value. Stockholm, Seville, and Marseille are fairly priced because the affordability ratio remains between +5% and -5% around its equilibrium value. Nevertheless, other markets have been overvalued since the affordability dramatically decreased compared to their long term equilibrium. Concerns are arising regarding German and UK markets such as Lisbon with more than 30% of overvaluation vs their long-term equilibrium.

Affordability ratio



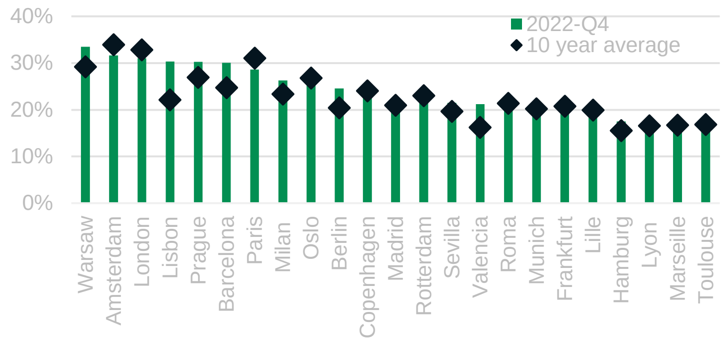
PRESSURE ON EFFORT RATE AS DEMAND RISING FOR THE RENTAL SECTOR

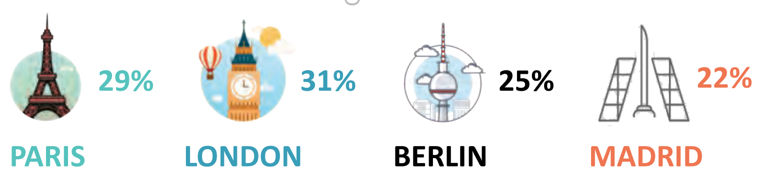
- The tenant effort rate represents the share of housing expenditure for a 60 sqm dwelling in the household disposable income.

- In Q4 2022, households dedicated on average 23.8% of their income to rent a 60 sqm dwelling, +114bps increases vs the 10-year average. Compared to the last 10 years, the most important rises in the effort rate were recorded in Lisbon (+825bps), Barcelona (+533bps), Valencia (+504bps), Warsaw (+429bps), Berlin (+415bps), and Prague (+337bps).

- There is a strong potential for rental growth in all markets since we observe a strong demand for the rental sector and the tenant effort remains particularly low. Nevertheless, even if demand is particularly high in Warsaw, Amsterdam, London, Lisbon, Prague and Barcelona, increases in rents should be more limited owing to a tenant effort rate over the 30% threshold.

Tenant effort rate (60sqm)



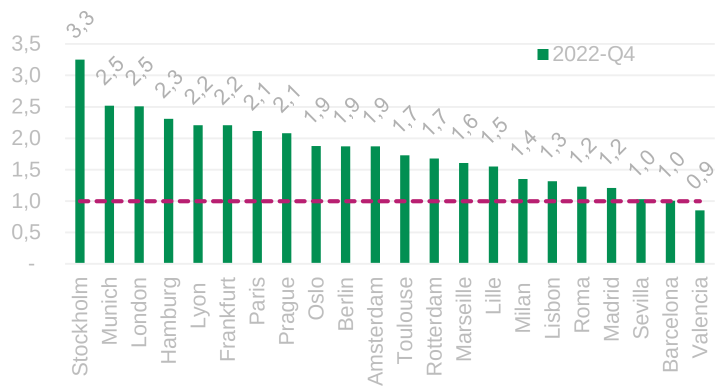


TREND TOWARDS HIGHER RENTAL DEMAND

- The ratio shows that it is better to rent than buying in all markets except in, Seville, Barcelona and Valencia. In Prague, Paris, Frankfurt, Lyon, Hamburg, London, Munich and Stockholm, it is more than two times more expensive to buy than to rent the purchasable area in each market. In Lille, Marseille, Rotterdam, Toulouse, Amsterdam, Berlin and Oslo it is between 50% and 90% more expensive to buy the purchasable area than to rent it.

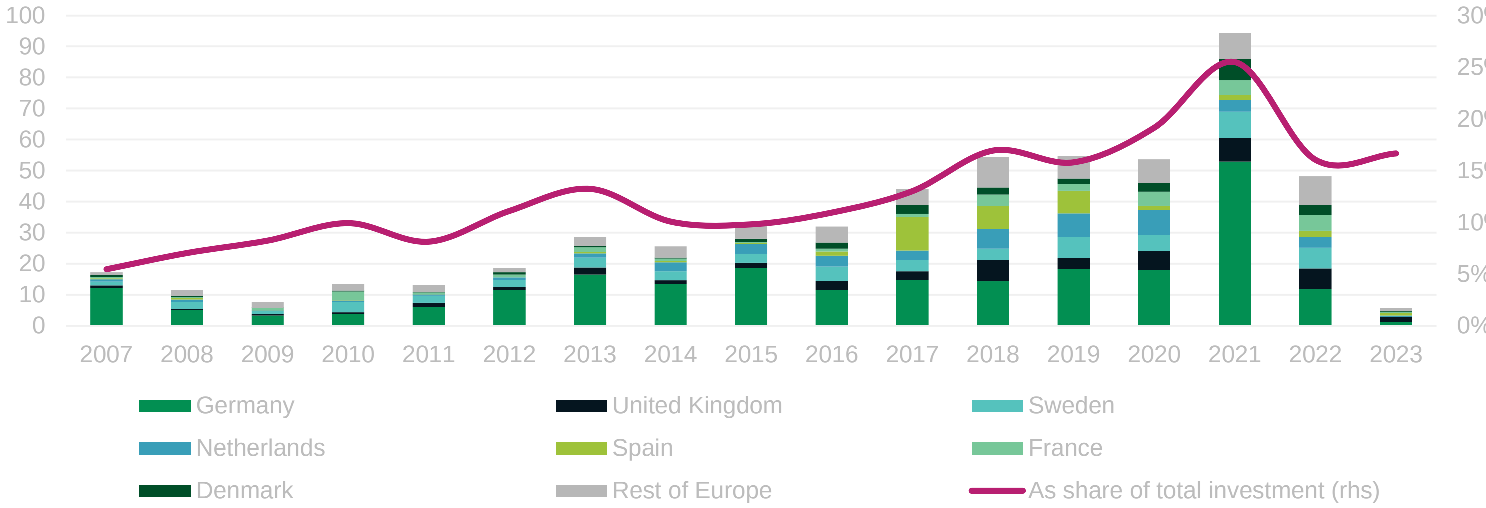
- If we compare in terms of square meters, renting enable households to afford more than 50 sqm than buying in Toulouse, Frankfurt, Munich, Hamburg, Lyon and Stockholm. Between 30 and 50 sqm more than buying in Prague, Rotterdam, Paris, Lille, Berlin, London and Marseille. In contrast, buying enables to afford 16 more sqm in Valencia 32 more sqm in Warsaw and Oslo than renting.

Buy-vs-rent ratio



DROP IN INVESTMENT VOLUME

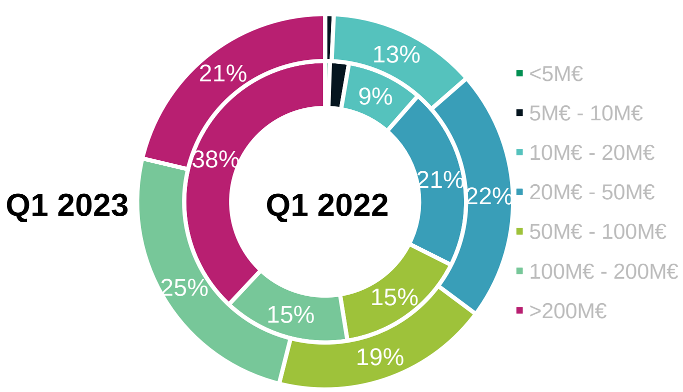
Residential investment volume



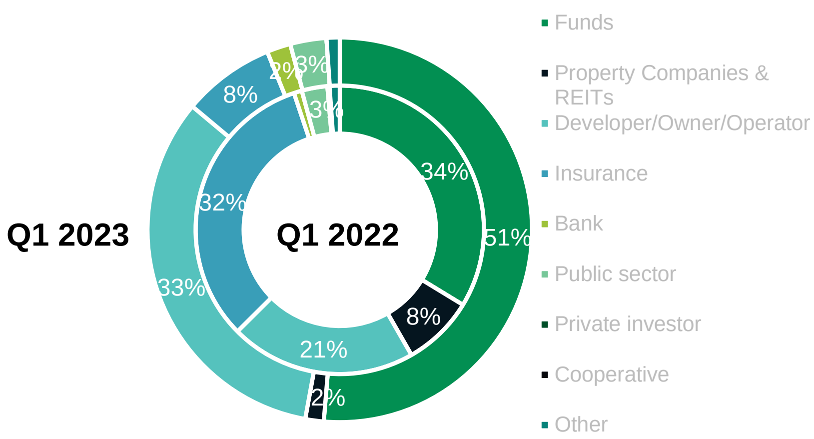
- Residential investment volumes in Europe reached €5.7bn in Q1 2023, down -70% compared to the same period last year and -53% vs the 5-year average.
- The residential investment in Europe is strongly impacted by interest rate hikes. Investors continue in a wait-and-see attitude despite a real interest in the asset class. The increases in mortgage rates and government bond yields are challenging the investment market by reducing the risk premium and the risk adjusted return of real estate. Hence, we expect yields to decompress and thus prices to adjust in order to balance the increase in the financing cost.
- Nevertheless, the underlying residential fundamentals are still very positive. We observe a strong disequilibrium between demand and supply in large urban cities. In these locations there is positive population and income growth and upwards pressure in the rental market, magnified by inflation and the shift in the monetary policy.

FUNDS AND DEVELOPERS ARE THE MOST ACTIVE PLAYERS

Breakdown by volume



Buyers' typology



- In Q1 2023, we record a total of 127 deals vs 406 deals in Q1 2022, which represents a decline of 69% in the number of transactions.
- Transactions greater than €100M represent 12% of the total of transactions on the market, on the rise compared to the same period last year (7%). We recorded 15 deals greater than 100M€ vs 29 in Q1 2022, a fall of 51%. Deals between €10M-€20M and €20M-€50M represents 41% and 31% respectively of all transactions, on the rise compared to last year. However, we recorded 52 deals for the segment €10M-€20M (-54%) and 39 deals for the segment €20M-€50M (-69%). We observe a significant decline in the share of less than €10M segment in the number of transactions: 4.7% in Q1 2023 vs 23.9% last year (-94%).
- In Q1 2023, Funds (51%) and Developer/Owner/Operator (33%) were the most active players in the market. The joint Venture between Dewag and Indigo invest bought two PRS in Germany for a total investment of €160M. The joint venture between Tuath housing and Land development bought 316 units in Ireland for €130M.
- Most important sellers were Developer/Owner/Operator (66%) and Funds (23%). Developer/Owner/Operator are gaining important market shares. We observe more and more transactions and investment volume in the Build-to-Rent segment.

LOCATIONS

(JANUARY 2023)

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ALLIANCES

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