BNP PARIBAS REAL ESTATE

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RESEARCH

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FEBRUARY 2024

EUROPEAN LOGISTICS MARKET

MARKET SLOWDOWN IN 2023

-31%

LOGISTICS TAKE-UP FOR WAREHOUSES OVER 5,000 SQM

(2023 vs 2022)

TAKE-UP

Transaction volumes have returned to 2019 levels. Supply remains limited, especially as land becomes scarcer and its allocation is increasingly regulated.
Market fundamentals remain healthy with low vacancy rates in most countries and the lack of new developments still contribute to rental growth in prime sectors.

- Take-up softened in 2023 to reach just 19 million sqm in the 6 leading European countries (28 million sqm in 2022).
- GDP growth contracted sharply in the Euro area from +3.5% in 2022 to +0.5% for 2023 and +0.6% for 2024.
- Prime rents rose by 6.3% in the last 12 months in a panel of 49 markets in 22 countries.
- Supply has become scarce and speculative developments have been few. Vacancy rates remain generally low between 3% and 7% depending on the market.

-48%

INDUSTRIAL & LOGISTICS INVESTMENT IN EUROPE

INVESTMENT

The investment market bottomed out in 2023. While waiting for improvement in financial conditions which did not occur, all markets experienced a significant drop in investments of -40 to -70%.
The likely cuts in policy rates by the ECB in 2024 should boost jumbo deals and encourage the return of pan-European portfolios.

- The volume of investment contracted sharply from €61bn in 2022 to nearly €32bn in 2023.
- Prime yields rose by 60 bps in the past 12 months in Europe (+18 bps over the past quarter)
- Stabilization of logistics prime yields is expected throughout Europe. This will reflect the changes in interest rate policy in 2024 as terminal rates are reached.

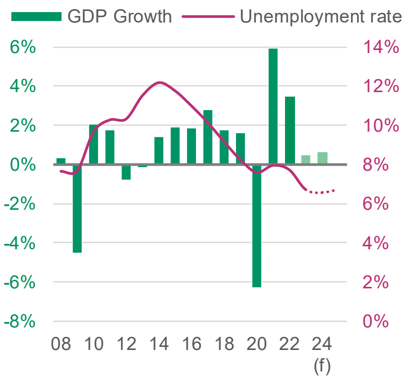
Vincent Robion
Head of Research - Logistics Europe

EUROPE ON TRACK FOR A GRADUAL RECOVERY

+0.5%

GDP GROWTH
EURO AREA – 2023

GDP and Employment growth in the Eurozone



Economic activity has shown resilience in recent quarters against a backdrop of above-target inflation and higher interest rates. It appears that the eurozone narrowly avoided a recession in the second half of 2023 as several factors provided much-needed economic support. These included savings built up during the pandemic, structurally tighter labour markets and the EU Next Generation fund disbursements. At a country level, the peripheral markets – Italy and Spain – remained the key source of strength, while France and Germany saw weaker performance.

Looking ahead European economies will continue to face challenging economic conditions in the near term as interest rates remain elevated. However, the worst appears to be behind us. Indeed, the European Central Bank has made significant progress in the battle against inflation, which means it is only a matter of time before it considers cutting interest rates. This has led to growing optimism around the economic outlook.

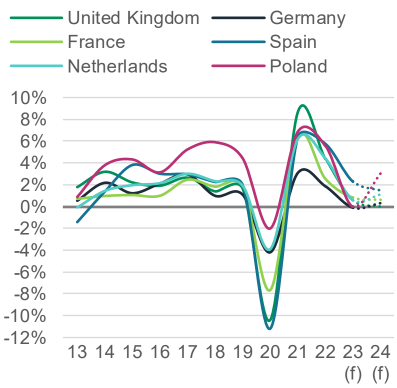
In 2023 the Eurozone (+0.5% GDP pa) and UK (+0.2%) economies recorded little economic growth. However, **we forecast a gradual recovery in 2024 for both economies; Eurozone (+0.7%) and UK (+0.3%)**. Spain is likely to be the best performer in the Eurozone over this period (+1.9% p.a.) followed by Italy (+1.2% p.a.) and France (+1.0% p.a.). By contrast, economic growth in Germany is set to lag (+0.7% p.a.).

The challenges faced by households over the past year were reflected in their spending habits. Eurozone retail sales volumes in December were around 1% lower than in the same month a year earlier. That said, **consumer confidence is on the mend, with the European Commission's sentiment indicator recovering significantly** over the past year. This trend is likely to carry into 2024 as inflation continues to fall and wages increase further, which will provide increasing support to consumer spending in the coming quarters.

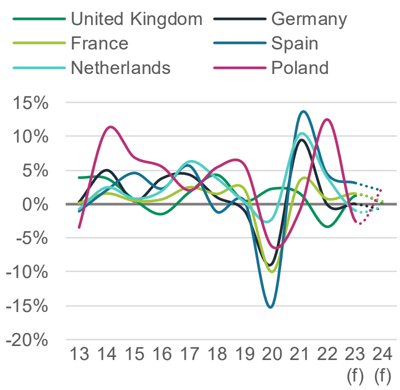
The outlook for manufacturing remains challenging. While supply chain pressures have eased since the Covid-19 pandemic, heightened geopolitical tensions represent a significant risk. One recent example of this was the disruption to ships passing through the Red Sea which led to a lengthening in suppliers' delivery times, according to the January Purchasing Manager's Index (PMI). The PMI surveys also show that weak demand for manufactured goods has created spare capacity at Eurozone factories, evidenced by the declines in backlogs of work. On the plus side, the slump in the manufacturing sector eased in January as new orders and factory output declined at their slowest rate since last April. What's more, the surveys reported an uplift in business confidence and expected output over the next 12 months.

The resilience in economic activity has been underpinned by a strong labour market. The Eurozone unemployment rate was 6.4% in December, its lowest level in over 20 years. That said, a broader range of indicators point to some loosening in labour market conditions. Both the job vacancy rate and number of firms reporting shortages of workers have declined in recent quarters, which is feeding through to slower wage growth. Looking ahead, structural factors such as demographics and a possible sectoral mismatch are likely to keep the labour market tight by historical factors, easing fears that the economy may enter a deep contraction.

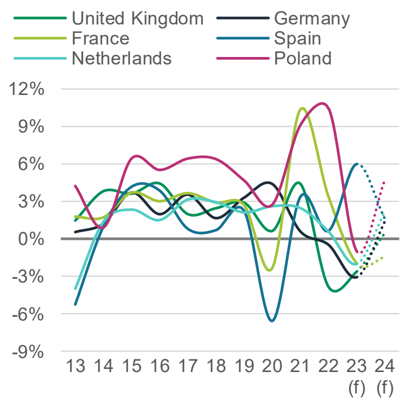
GDP growth
(year-on-year change)



Manufacturing Output
(year-on-year change)



Retail Sales
(year-on-year change)



Source: Oxford Economics, BNP Paribas

BELOW ITS 5-YEAR AVERAGE, THE MARKET IS SLOWING DOWN

-31%
TAKE-UP
(2023 vs 2022)

± 5%
VACANCY RATE
(Q4 2023)

The occupier markets held up a little better than the investment markets even though volumes fell significantly. They were naturally impacted by the economic slowdown and the drop in consumption.

The decline in 2023 is all the more pronounced as the markets had reached exceptional levels in previous years. They were supported by very strong activity in the mass distribution and e-commerce sectors in particular.

Transaction volumes in 2023 returned to 2019 levels. Take-up decreased by 31% to 19 million sqm in the 6 leading European countries in 2023.

Supply remains limited and speculative developments have been few. Vacancy rates remain generally low between 3% and 7% depending on the market.

Rents have increased almost everywhere in Europe, by 6.3% in 2023. The sharp increase in recent years is a supply side phenomenon. It also reflects the price of land that has risen over the past five years. In turn this stems from the difficulty in obtaining sites with planning permission as usage is increasingly scrutinized. ESG requirements and the scarcity of new products are still putting pressure on rents.

In Germany, take-up fell by 27% to 5.7m sqm, approaching the volumes recorded in 2020. Supported by an improved economic outlook, the logistics market has been hampered by the challenging conditions for project developments in and outside the major logistics regions. The upward trend in rental prices continued across locations. On average, prime rents rose by 9% in the past 12 months.

In France take-up decreased by 23% to 3.6m sqm. The logistics market has been slowing down as demand for XXL warehouses and build-to-suit solutions dropped significantly, especially in Greater Paris. Overall, land is becoming scarce in most markets and supply is drying up. The vacancy rate is still low in France at 3.6%, pushing up rents (+19% in 2023).

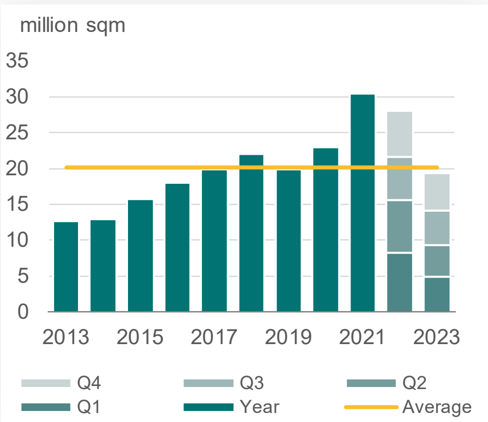
In Poland, following a slow start at the beginning of the year, the market picked up in the second half. Take-up reached 3.4m sqm (-25% vs 2022). The vacancy rate stepped up above 7% In 2023. A noticeable trend is the sharp decrease in the share of new construction projects launched on a speculative basis. Prime rents rose by 2% during 2023 to €51.6/sqm/yr in Warsaw II and €50.4 in Poznan.

In the UK, like most European countries, take-up decreased significantly in 2023 after the exceptional volumes recorded the previous years. Although take-up dropped by 42% to 2.8m sqm in 2023, activity picked up in Q3 and again in Q4 and could suggest that the market has already bottomed out. The tightening supply of best-in-class units combined with strong requirements means that rental growth is set to continue.

In the Netherlands, following two years of buoyant activity, the market slowed sharply in 2023. Take-up dropped by 47% to nearly 2m sqm. This reflected lower economic activity and the lack of good quality supply. High land prices, high development costs and lower exit prices are affecting new developments. Low availability is still putting pressure upward on rents, as seen in the main markets but also in secondary regions.

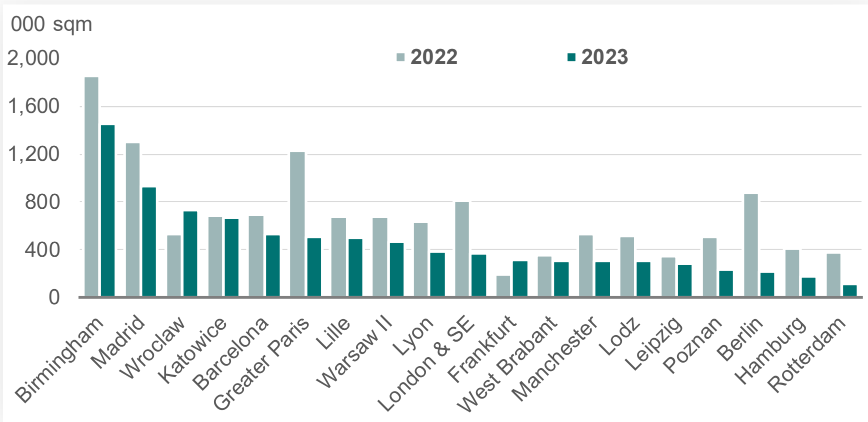
The Spanish market maintained a good volume of transactions during 2023, and unlike most European countries, above the 5-year average. Take-up reached 1.8m sqm in 2023 (-23% vs 2022). Vacancy rates eased in Barcelona and Madrid above 6%, whilst supply remained scarce in Valencia. Supported by steady demand, prime rents increased by 4% in Madrid and 7% in Barcelona during 2023.

Take-up – 6 countries*



(*France, Germany, Netherlands, Poland, Spain, UK)

Take-up – Warehouses over 5,000 sqm



PRIME HEADLINE RENTS WAREHOUSES OVER 5,000 M²

European average

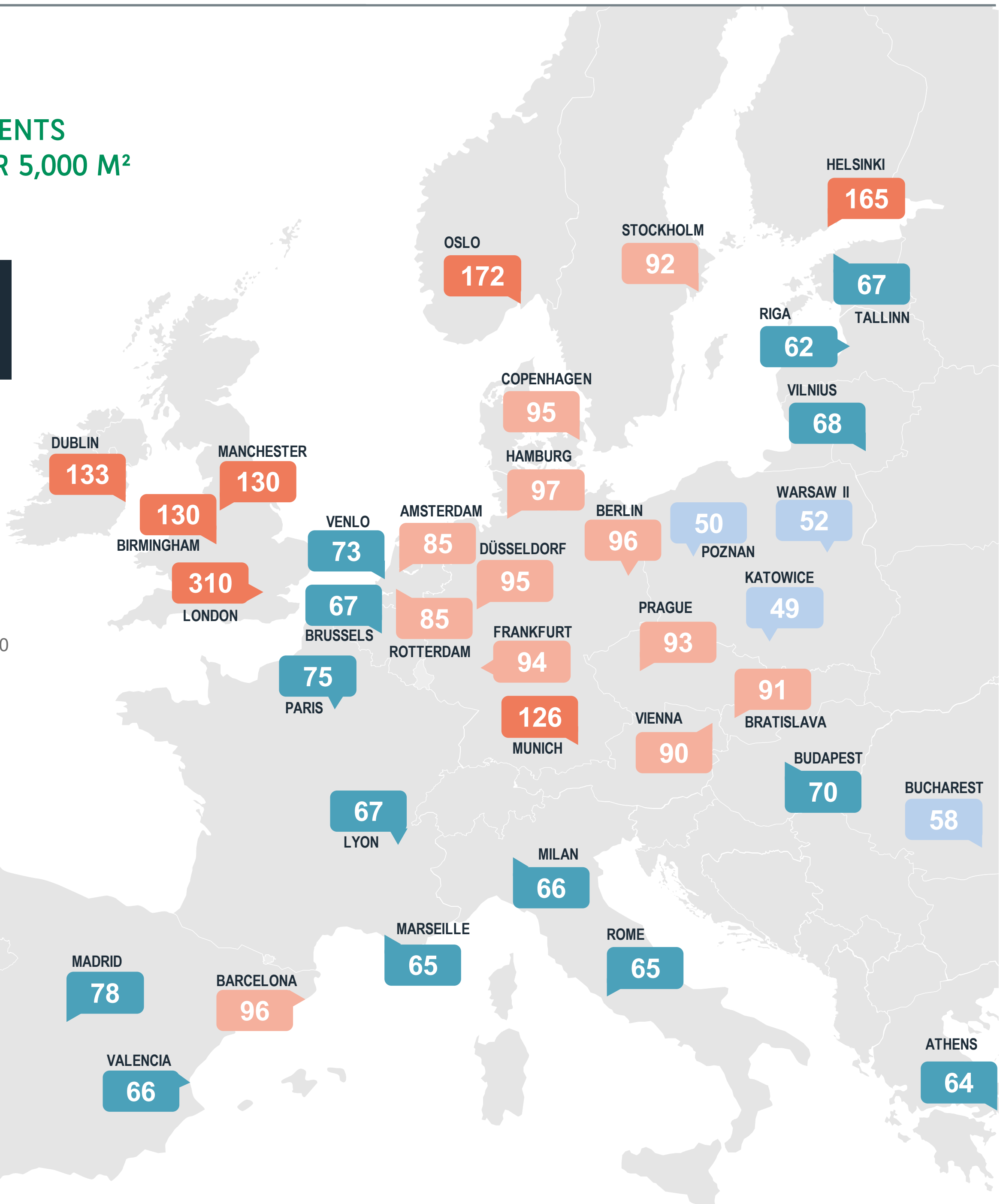
+6.3%
2023 vs 2022

49 markets, 22 countries

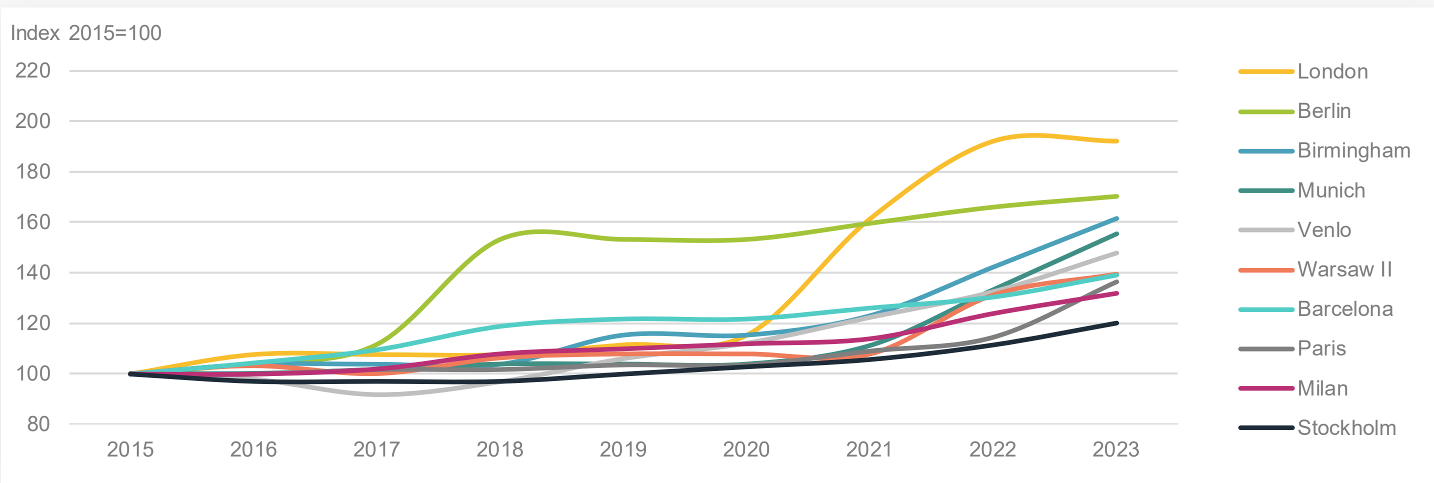
Rents in €/sqm/yr

- ≥ €100
- €60-80
- €80-100
- ≤ €60

1 GBP	€ 1.1535
1 SEK	€ 0.0872
1 DDK	€ 0.1341
1 NOK	€ 0.0859



Prime headline rents



-65%

Investment volume (2023 vs 2022)

24%

Share of Logistics in Commercial Real Estate

INDUSTRIAL AND LOGISTICS INVESTMENT BOTTOMED OUT IN 2023

In 2023, the amounts invested in industrial and logistics in Europe fell by 48% in Europe to €32bn. While waiting for an improvement in financial conditions (which did not occur), all markets experienced a significant drop in investment of -40 to -70%.

Two countries, Germany and the UK, captured more than half of investment in Europe. The United Kingdom alone represents a third of European investment in this asset class.

Industrial and logistics is maintaining strong market share against other assets. Investment shifted from 15% in 2017 to 24% of total commercial real estate in 2023.

In 2023, logistics yields increased significantly, on average by 60 bps, on top of similar increases in the previous year. Full decompression seems almost to have been reached in most countries. However, further adjustments are still expected in some markets for 2024.

The **United Kingdom** was the first country where a correction was observed at the start of the crisis. Today, it is also the first country where rates have started to readjust between 4.75 and 4.50, thus marking the start of a compression.

In **Germany**, investment dropped by 40% to its lowest level in 7 years to €6.1bn after reaching a historical high in 2022. Prime yields rose again at the end of the year (4.25% in Q4).

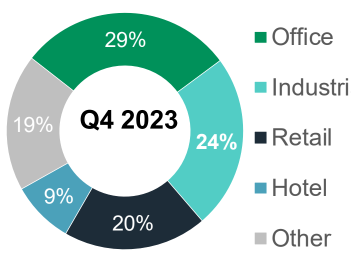
In **France**, investment dropped by 55% to €3bn but it appears that repricing is almost complete. This could result in stronger activity in forthcoming quarters. Logistics prime yields shifted by 115 bps over the past year to reach 4.75% in Q4 2023.

In the **Netherlands**, the market in industrial and logistics fell by 69% in 2023 to €1.7bn. Logistics prime yield corrections were amongst the earliest and the highest in Europe. The decompression slowed down to 4.9% in Q4 2023. Given demand strength yield adjustment may unlock investment.

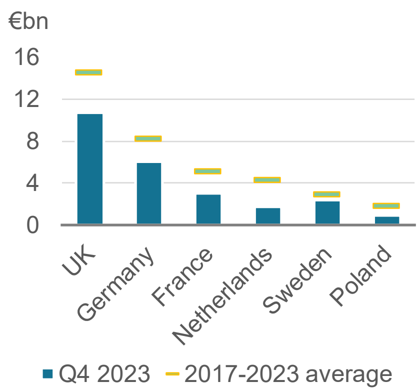
In **Poland**, Industrial and logistics remains the country's strongest performing market sector amounting nearly €1bn in 2023. This represented more than half of total commercial real estate investment. Yield decompression is slowing reaching 6% in Q4 2023.

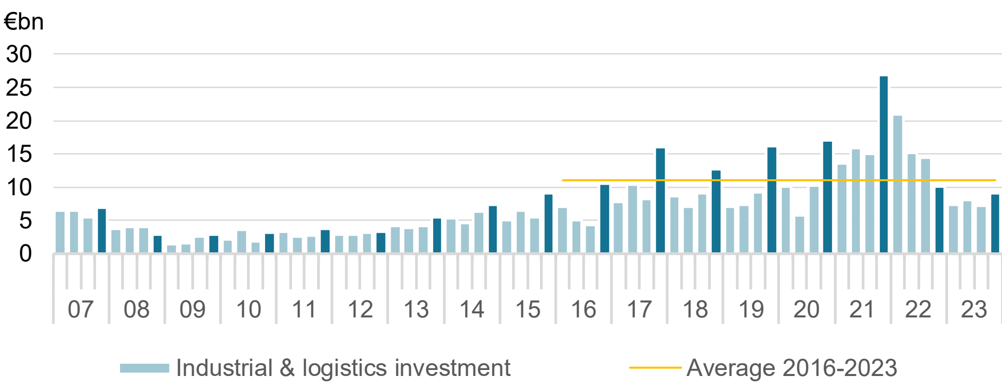
In **Spain**, the volume of investment in industrial and logistics decreased to €1.1bn, just below its 10-year average. Prime yields decompressed by 40 bps during the year to reach 5.25% in Q4 2023. Repricing is expected to support the market again in the next few quarters.

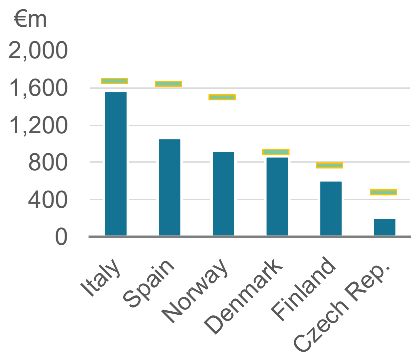
Investment volume in Europe



Industrial & logistics investment







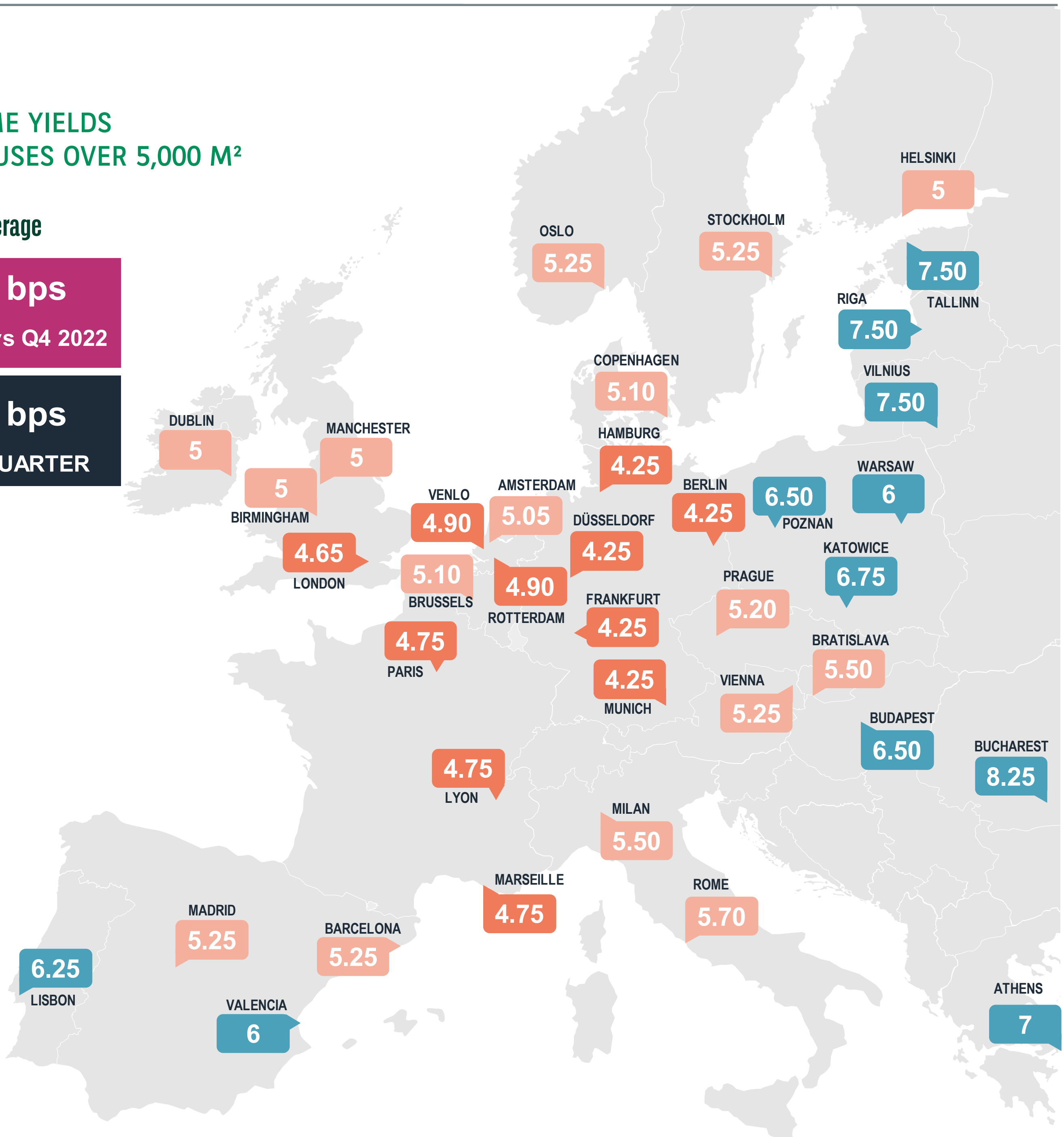
NET PRIME YIELDS
WAREHOUSES OVER 5,000 M²

European average

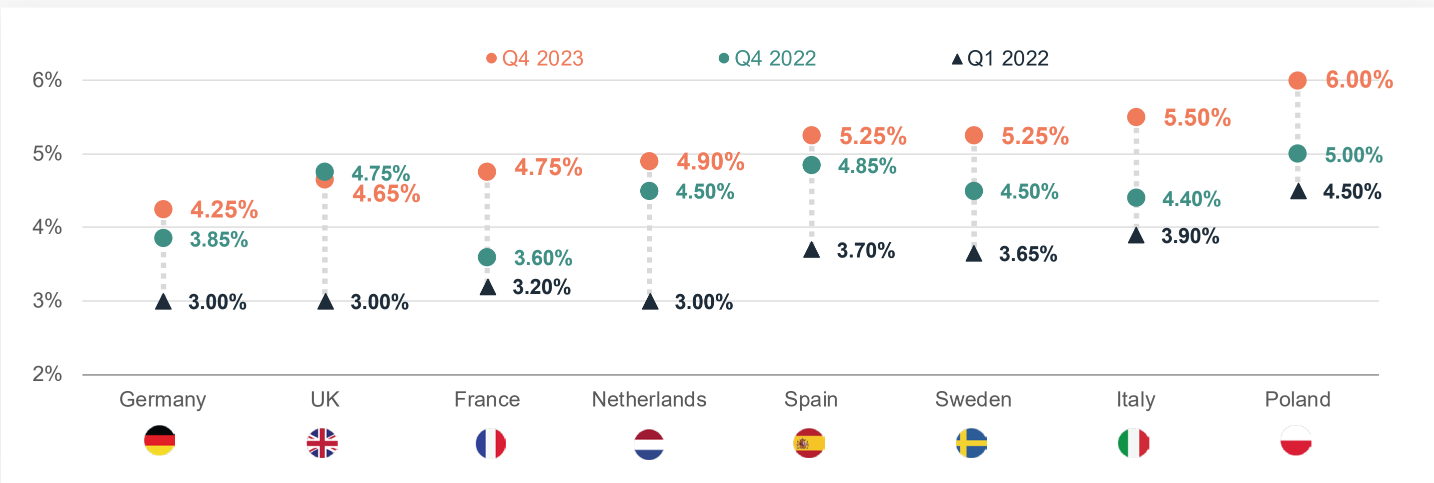
+60 bps
Q4 2023 vs Q4 2022

+18 bps
LAST QUARTER

< 5%
5-6%
≥ 6%



Net prime yields - Grade A warehouses (big boxes) for standard lease terms (5 to 15 years)



DEFINITIONS

LETTING & SALES

Take-up: represents the total floor space known to have been let or pre-let, sold or pre-sold to tenants or owner-occupiers during the survey period. It does not include space that is under offer.

- A property is deemed to be "taken up" only when contracts are signed or a binding agreement exists.
- Pre-let refers to take-up that was either in the planning or construction stage.
- All deals (including pre-lets) are recorded in the period in which they are signed.
- Contract renewals are not included
- Sales and leasebacks are not included as there had been no change in occupation.
- Quoted take-up volumes are not definitive and are consequently subject to change.

New space: premises that have never been occupied in new buildings.

Second hand space: premises that have been previously occupied by an occupier or vacant for more than five years.

Vacant space: all completed buildings actively seeking rental or sale to occupiers.

New supply: all building restructuring that adds to the existing stock. These are analysed according to progress.

- Completed new supply: buildings on which construction work is finished.
- Under construction: buildings on which construction has effectively begun. Prior demolition work is not taken into account.
- Planning permission granted: authorisation to build obtained, generally booked after settlement of third party claims.
- Planning permission submitted: planning permission requested, being processed.
- Projects: identified intention of a building operation for which no request has been filed.

Speculative / Non speculative developments:

- Speculative: construction launched without prior rental or sale to the occupier.
- Non-speculative: construction launched after partial or complete sale or rental to an occupier.

Rent: common annual headline rent, expressed per square metre per year, and excluding taxes and charges.

- Average rent: weighted average of rented area. The average featured is a moving average over three quarters, to smooth out the changes.
- Prime rent: represents the top open-market rent at the survey date for a real estate unit and should be representative at around 3 to 5% of the market volume (sqm):
  - of standard size commensurate with demand in each location.
  - of the highest quality and specification.
  - best location in a market.

INVESTMENT

Initial net prime yield: ratio between net income (excl. operating costs) over the purchase price including all acquisition costs.

Prime Yield: net lowest yield obtained for the acquisition of a unit:

- of standard size commensurate with demand in each location.
- of the highest quality and specification.
- in the best location in each market.

Portfolio: group of several assets located in different places.

ASSET TYPES & LOGISTICS

Warehouses: buildings intended for storage, distribution or packaging.

- **Distribution centres**: national or regional used for storage located in the outskirts of cities with good transport connections.
- **Fulfilment centres**: allow additional activities, often automation driven. Typically larger than standard logistics to allow other activities than storage.
- **Cross-dock**: Little storage time. Properties used to unload goods and reassemble / move them directly for outbound distribution.
- **Last mile**: for city distribution. Includes a wide range of warehouses and storage units including older space.
- **Cold storage**: Storage for fresh or frozen products, with thermal insulation and specific equipment as part of the warehouse. Involves higher construction costs.

Logistics: the process of planning, implementing, and controlling procedures for the efficient and effective transportation and storage of goods, and related information from the point of origin to the point of consumption. Includes inbound, outbound, internal, and external movements.

Supply chain: all the elements in the process of supplying a product to a customer. The chain begins with the sourcing of raw materials and ends with the delivery of finished merchandise to the end-user. It embraces vendors, manufacturing facilities, logistics service providers, distribution centres, distributors, wholesalers, other intermediaries, etc.

Supply chain management: Encompasses the planning and management of all activities involved in sourcing and procurement, conversion, and all logistics management activities.

BNP PARIBAS REAL ESTATE

Real Estate for a changing world

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(January 2024)

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