EUROPE
CRE 180

ECONOMIC OUTLOOK

REAL ESTATE PERSPECTIVES

GLOBAL RESEARCH
January 2022

BNP PARIBAS REAL ESTATE

Real Estate for a changing world

EUROPE CRE 180

CONTENTS

EXECUTIVE SUMMARY

IN A NUTSHELL

ECONOMIC GROWTH IS EASING IN THE EUROZONE

A normalization in growth is expected in Europe, with household spending underpinned by cheap financing conditions, a further improvement in the labour market and faster wage growth. Stronger supply chain disruptions and inflationary pressures may have a negative impact on 2022.

A NORMALIZATION OF INFLATION AND MONETARY POLICY

Most of this inflationary surge is still transitory, but that does not mean that we expect it to ease rapidly. This implies that monetary policy will normalize as well, but with important differences in timing, with the Fed and the BoE moving first.

INVESTMENT BACK TO PRE COVID-19 LEVELS

€272.7bn was invested in Europe over 2021, which represents a 15% increase vs 2020, in line with the pre-Covid-19 levels. Investment in logistics (+51%) reached an all-time high while office (+10%) and hotel (+33%) investments are on the road to recovery. However retail investment (-7%) continues its descent.

YIELD COMPRESSION RESUMED

After drawing to a halt during 2020, office prime yields froze all over Europe, but they seem to be narrowing again. Prime retail yields also froze and are now expanding again in some markets. Prime logistics yields, on the other hand, continually decreased during the crisis. Compression accelerated from Q2 2021 and is ongoing.

OFFICE: VERY DYNAMIC Q3 AND Q4

Take-up at the end of 2021 saw a significant increase (+27%) compared to last year. Slightly more than 10 million sqm was taken-up last year. Even though the pre-covid levels are not reached, take-up showed signs of normalisation in Q3 and Q4.

PRIME RENTS UNAFFECTED BY THE CRISIS

Despite the slowdown in take-up, the prime market segment did not suffer from the crisis. In many markets, prime rental values are now even standing at higher values than before the outbreak of the pandemic.

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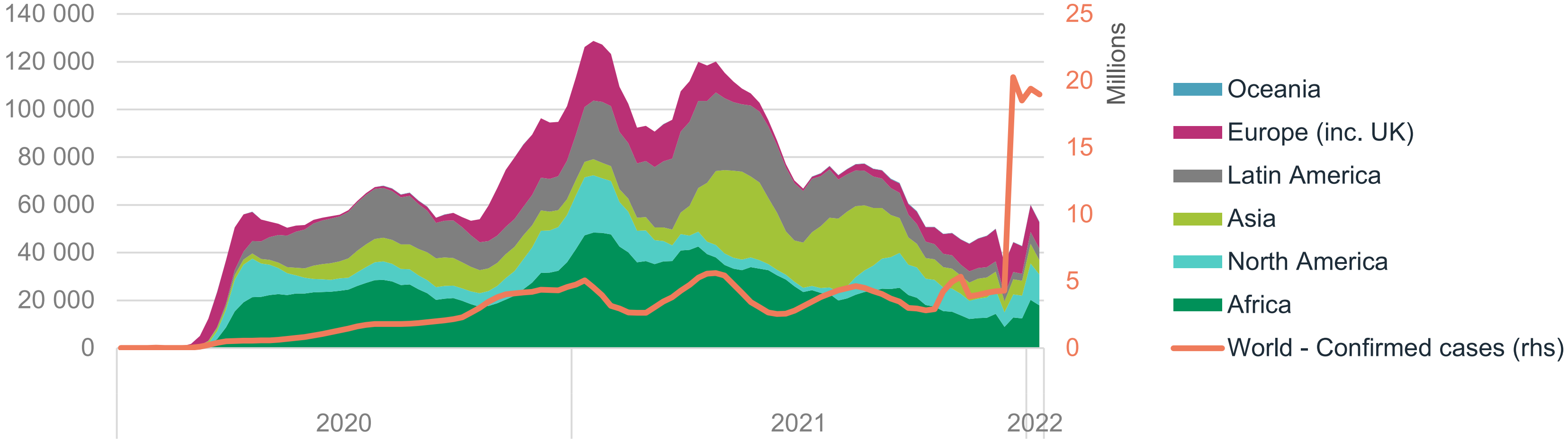
ECONOMIC OUTLOOK

BNP PARIBAS REAL ESTATE

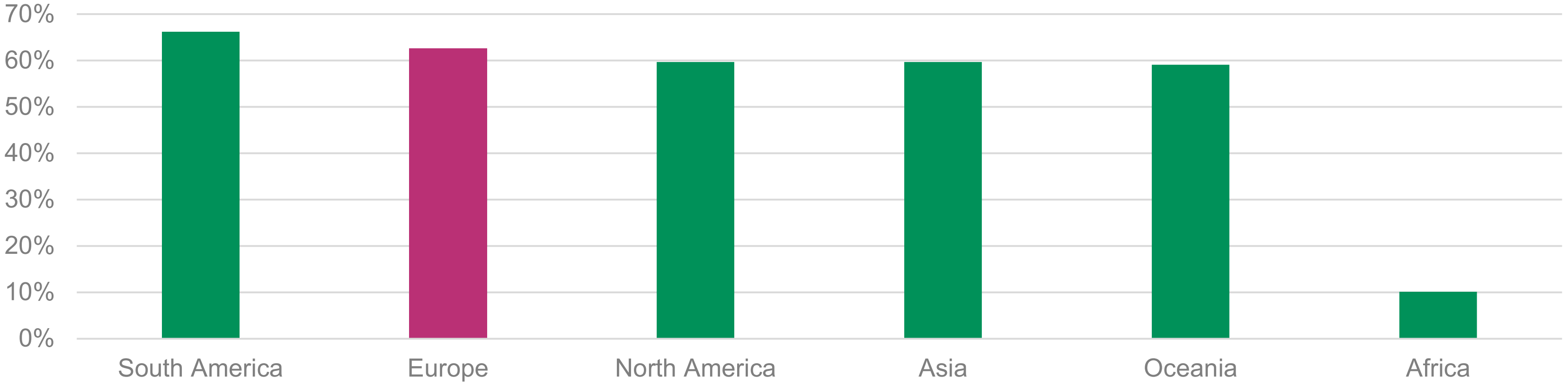
COVID-19: WHERE ARE WE?

NEW COVID CASES ARE RISING SHARPLY

Number of weekly deaths and confirmed cases



Vaccination around the World
(Share of the population fully vaccinated)



New COVID-19 case numbers continue to rise sharply

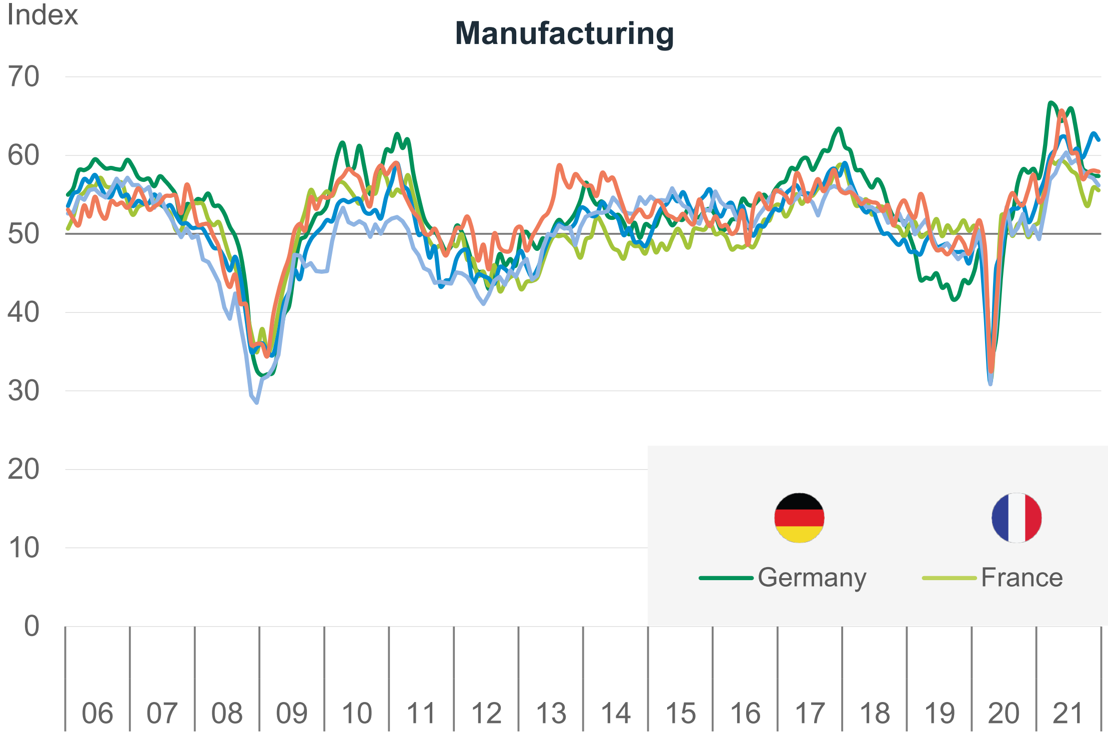
- The weekly number of new Covid-19 cases remains very high in most regions because of the Omicron variant. 21.2 million new cases were reported in the week of 10-17 January.
- The largest weekly increases were recorded in Asia (+95.7%), followed by North America (40%), Europe (6.7%). Africa experienced a decrease in the number of cases (-16.4%).
- On a weekly basis, the highest number of new cases in a single country was in the USA (6,178,670). France was next with 2,006,679 cases (+15.7%), followed by India (1,672,526), Italy (827,805), Spain (784,598) and the UK (599,966).

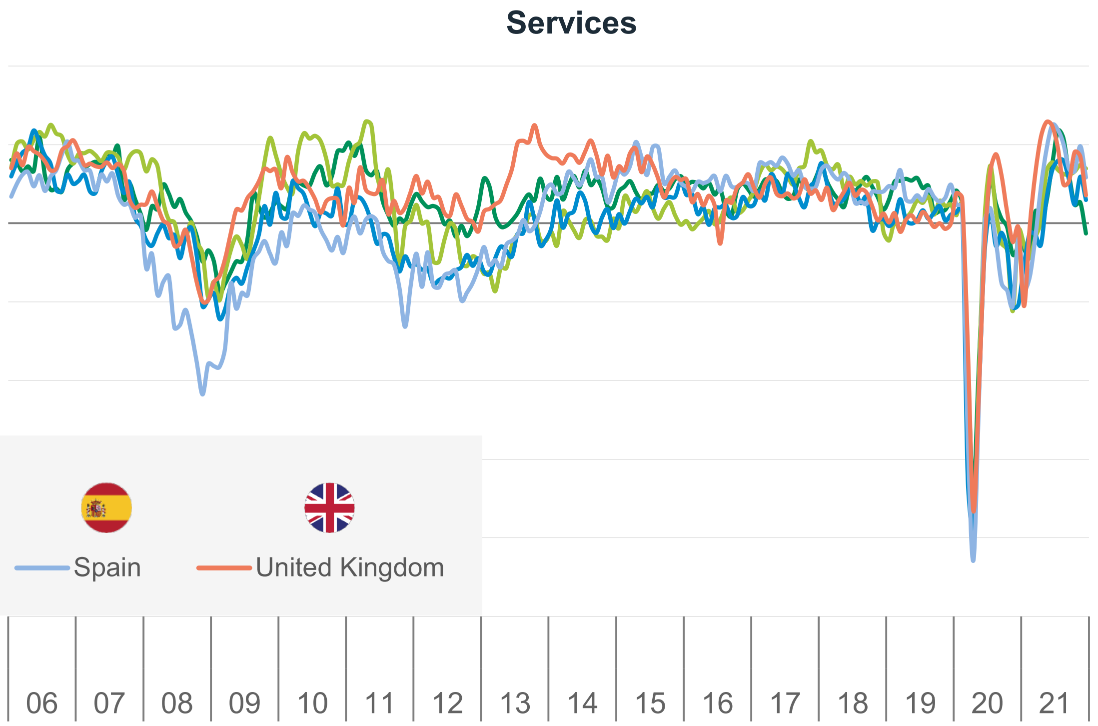
Vaccination levels are high

- To date, 9.57 billion Covid-19 vaccine doses have been administered worldwide since vaccination campaigns began in the fourth quarter of 2020, including 813 million booster doses.
- Nearly 60% of the world's population has now received at least one dose of a Covid-19 vaccine. However, there are still substantial disparities between rich nations, where 77% of the population has received at least one dose, and low-income countries (8%).
- On the mobility front, visits to retail and leisure facilities remain on a downward trend in Germany, Belgium, Italy, France, Spain, the US and the UK.

PURCHASING MANAGER INDEX SURVEYS

A BROAD IMPROVEMENT OF BUSINESS CONFIDENCE





Sources: Markit, BNP Paribas Economic Research.

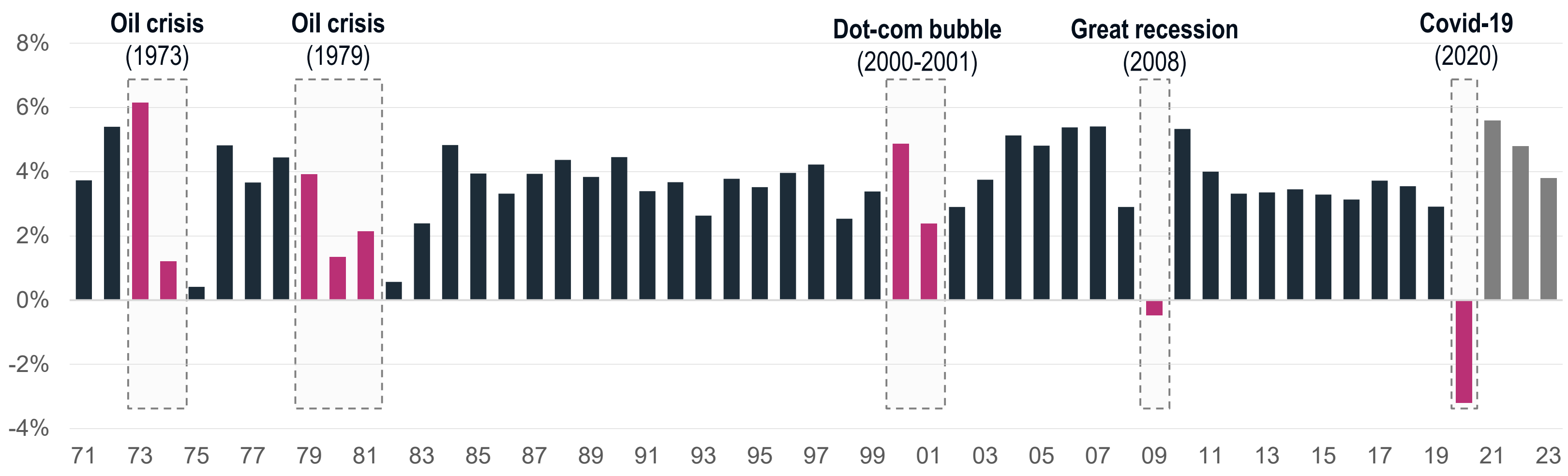
Numerous headwinds are constraining growth prospects in the Eurozone.
Supply bottlenecks and supply disruption have been dominant themes throughout the year, acting as a headwind to growth, both directly but also indirectly, by causing a pick-up in inflation to levels not seen in decades

Nevertheless, business conditions surveys have shown resilience so far. Indeed, company investments should benefit from improved profitability, very attractive financing conditions, increased capacity utilization and a favourable demand outlook. Although the downside risks have increased, our scenario for 2022 remains fairly optimistic.

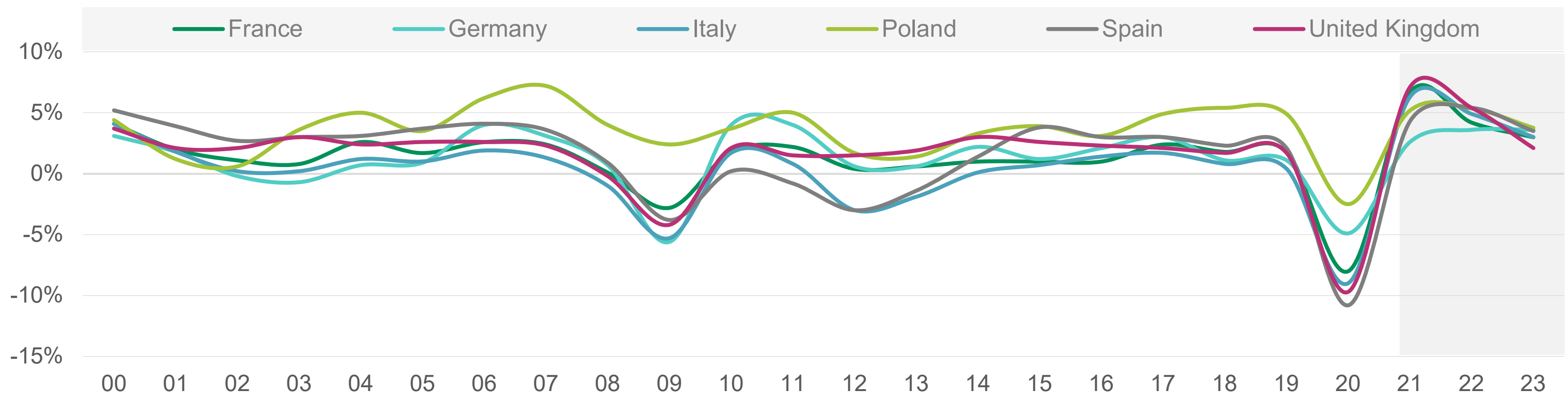
ECONOMIC OUTLOOK

WHAT OUTLOOK FOR THE MAIN ECONOMIES?

World GDP



GDP Growth in European countries



Sources: BNP Paribas Real Estate, OECD.

2022: A normalization in growth

- In the advanced economies, we expect above potential growth in real GDP, with household spending underpinned by cheap financing conditions, a further improvement in the labour market and faster wage growth.
- However, concern about the Omicron variant may lead to precautionary behaviour, weighing on certain household spending categories, slowing again the economic recovery.
- Finally, in several countries, household surveys reflect a growing concern about elevated inflation, which is eroding real disposable income. This is particularly an issue for lower income households.

Growth eases in the Eurozone

- After another quarter of vigorous growth (2.2% q/q in Q3), the Q4 outlook is much less attractive (0.4% q/q). We nonetheless estimate that full-year growth in the Eurozone will average 5% in 2021.
- Stronger supply chain disruptions and inflationary pressures should have a negative impact on 2022. Yet the main characteristic of growth in 2022 is that it will hold well above its long term trend.
- In 2023, growth is expected to remain strong.

GDP GROWTH IN EUROPE

GROWTH EASES

FORECAST (%):	2021	2022	2023
World	5.6	4.8	3.8
United States	5.5	4.7	2.8
Euro area	5.0	4.2	3.0
Japan	1.7	2.6	1.6
China	7.9	5.3	5.5
India	8.0	11.0	6.0
Russia	4.5	3.0	1.8
Brazil	4.8	0.5	2.0

Source: BNP Paribas Real Estate Research.

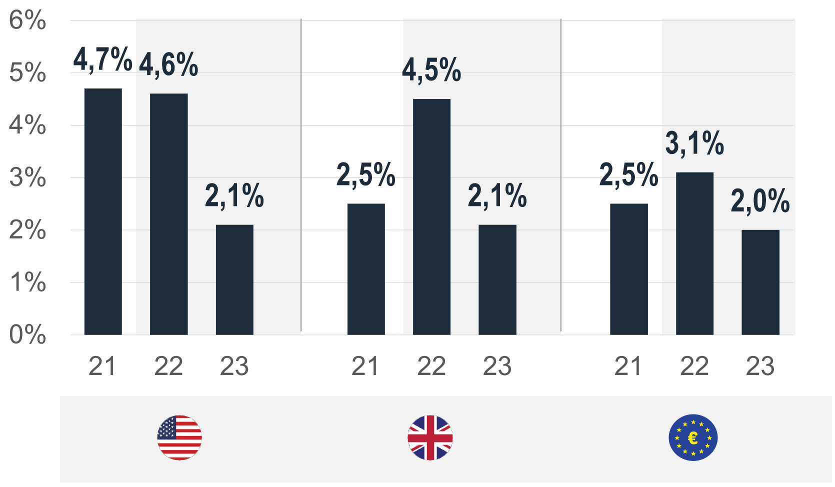
An optimistic scenario

- Growth in the Eurozone remained strong in Q3 2021, in line with expectations (2.2% q/q). However, the outlook for Q4 is much less bright (we expect growth to slow down to 0.4% q/q).
- However, in addition to the awaited normalization, headwinds have increased (supply-side problems, surging inflation and uncertainties arising from the new wave of the pandemic).
- Nevertheless, business conditions surveys have shown resilience so far. Although the downside risks have increased, our scenario for 2022 remains fairly optimistic.
- Albeit in a rather uneven manner, the US economy has bounced back swiftly from the Covid-19 pandemic and is now stronger than in 2019. Its growth rate, at 5.5% in 2021, is likely to return gradually to normal.
- In the US, the Federal Reserve has started tapering and this should lead to net asset purchases ending in March this year.
- In the Eurozone, the ECB has announced in December that it will stop net purchases under the PEPP in March 2022. Given the strength of the recovery, we expect underlying price pressures to build further and the ECB should increase its deposit rate in June 2023.

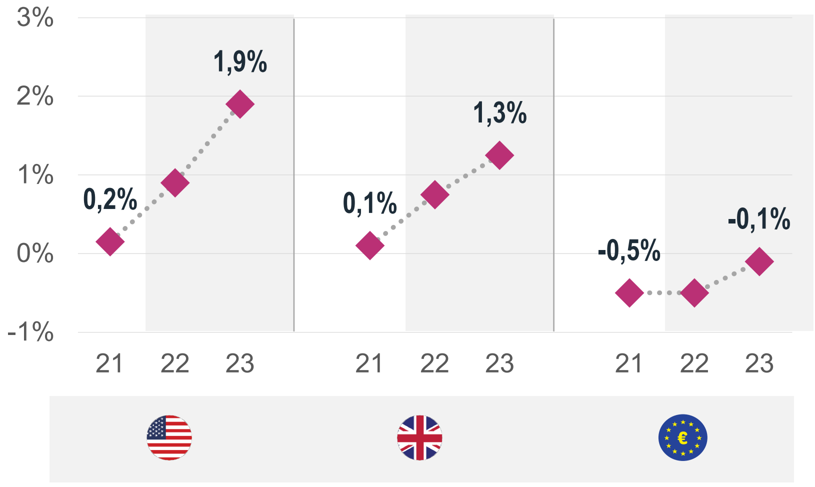
FINANCIAL OUTLOOK

ECONOMIC AND FINANCIAL INDICATORS

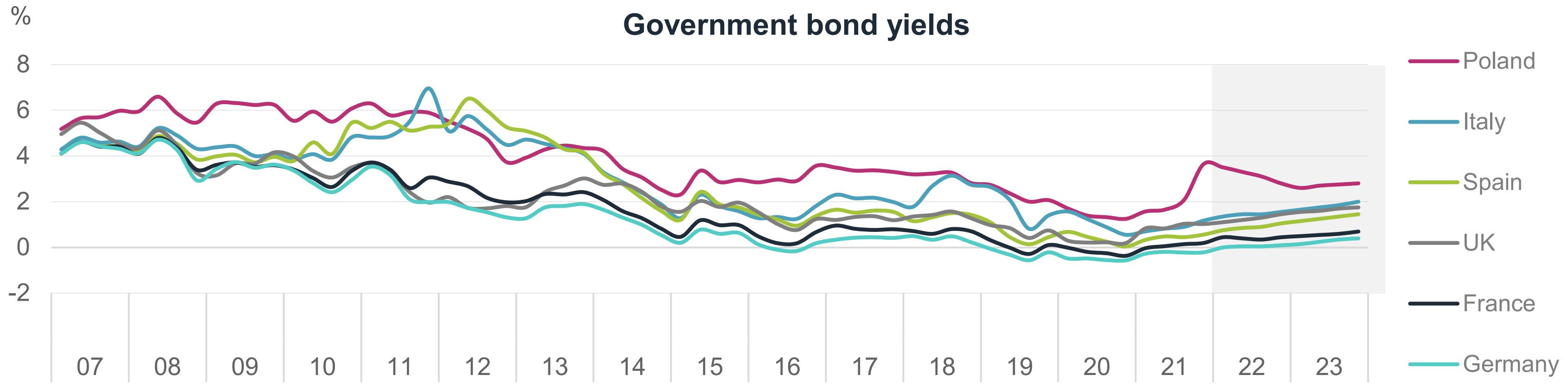
Inflation



Policy rates



Government bond yields



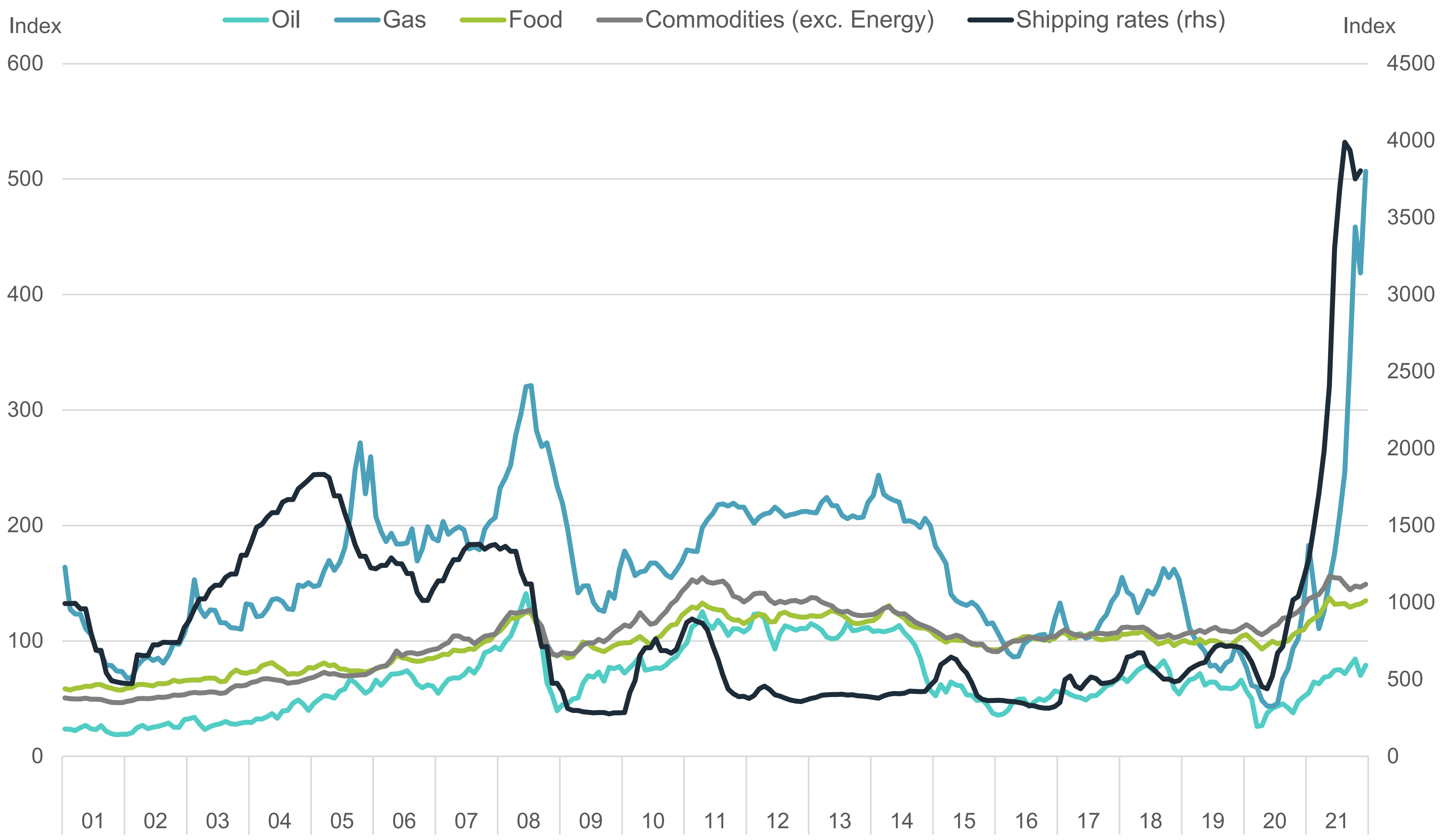
Sources: BNP Paribas Economic Research, OECD.

A normalization of inflation and monetary policy

- Covid-induced supply bottlenecks are still a dominant theme and caused a pick-up in inflation to levels not seen in decades.
- The main central banks in Western economies are arguing that the shock is mainly transitory. However, transitory does not necessarily mean 'short lived' and some forecasters are now considering a scenario in which inflation and upward pressure on wages could last.
- Indeed, the underlying dynamics of inflation are upwards, with an acceleration of wage growth, which could push companies to increase their sales prices.
- This implies that monetary policy will normalize as well, but with important differences in timing. In the US, the Federal Reserve has started to slow down the pace of monthly asset purchases and it should be followed by several rate hikes, starting around the mid 2022.
- In the Euro area, monetary policy should remain very accommodative. If the Pandemic Emergency Purchase Programme is expected to end in March 2022, we only expect a first increase of the deposit rate in June 2023.
- The monetary divergence between the Fed and the ECB should cause a further strengthening of the dollar versus the euro.

FINANCIAL OUTLOOK

INFLATION IS RISING AROUND THE WORLD



Sources: IMF, Harper Petersen, ICE, BNP Paribas Real Estate

Most goods and services are impacted by supply bottlenecks

- The world economy is experiencing multiple supply shocks: oil, gas, semiconductors, other materials, labour shortages. Some of these should be transitory because rooted in supply chain disruption; others will probably be permanent.
- Most of this inflationary surge is still transitory, but that does not mean that we expect it to ease rapidly. Inflationary pressures due to supply-demand imbalances will take a while to dissipate.
- Indeed, with the rebound in global demand, consumer prices have accelerated rather sharply in recent months, and these pricing dynamics extended into H2 2021.
- According to our latest scenario, this inflationary surge is unlikely to last. This is also the ECB's point of view. The European Central Bank expects inflation to peak this year. According to its latest macroeconomic projections, headline inflation will rise to 3.1% in 2022 (after +2.5% in 2021) before declining to 2.0% in 2023.

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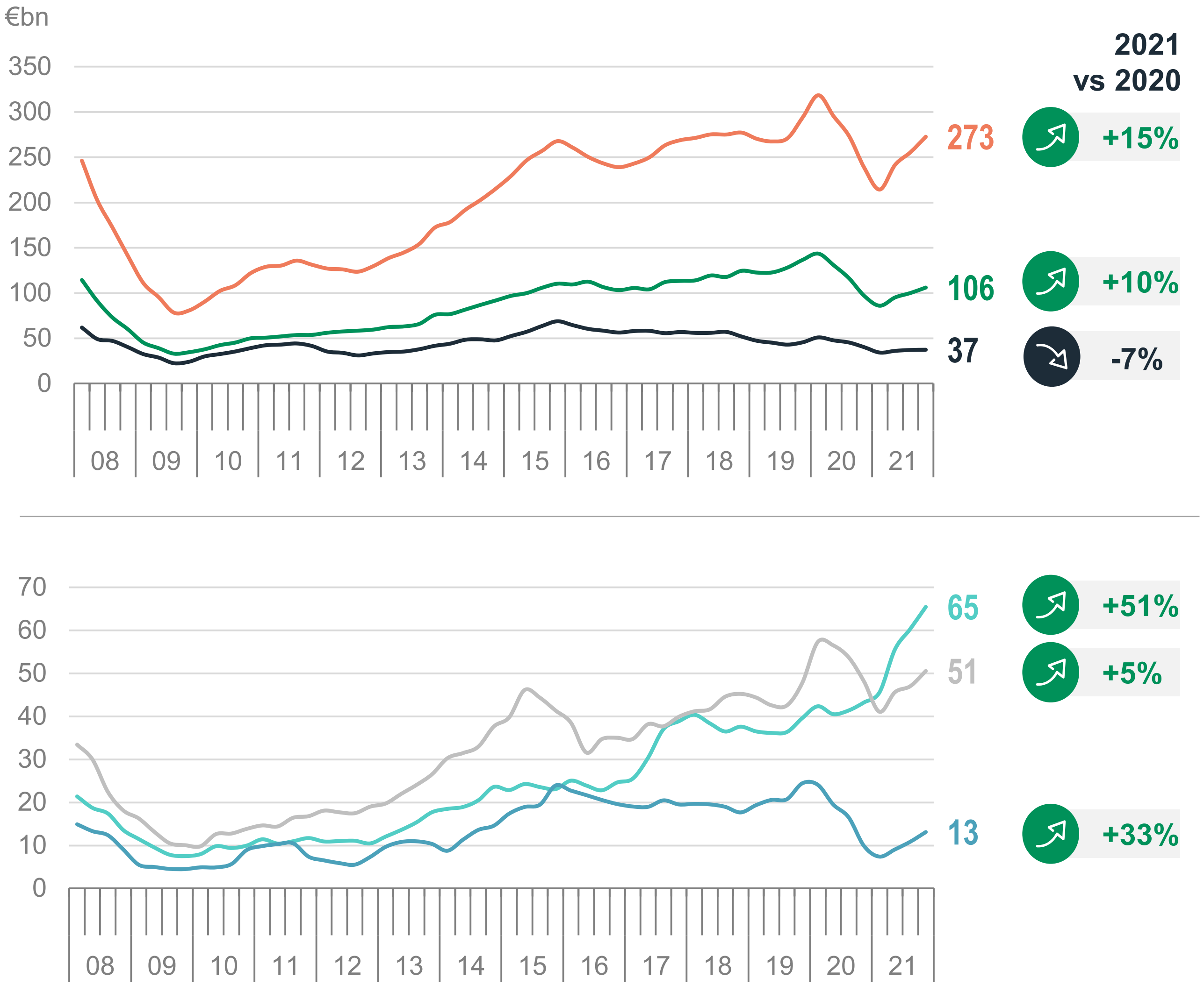
COMMERCIAL REAL ESTATE INVESTMENT MARKETS

BNP PARIBAS REAL ESTATE

INVESTMENT IN COMMERCIAL REAL ESTATE IN EUROPE

BREAKDOWN OF INVESTMENT BY ASSET CLASS



INVESTMENT BACK AT PRE-COVID-19 LEVELS

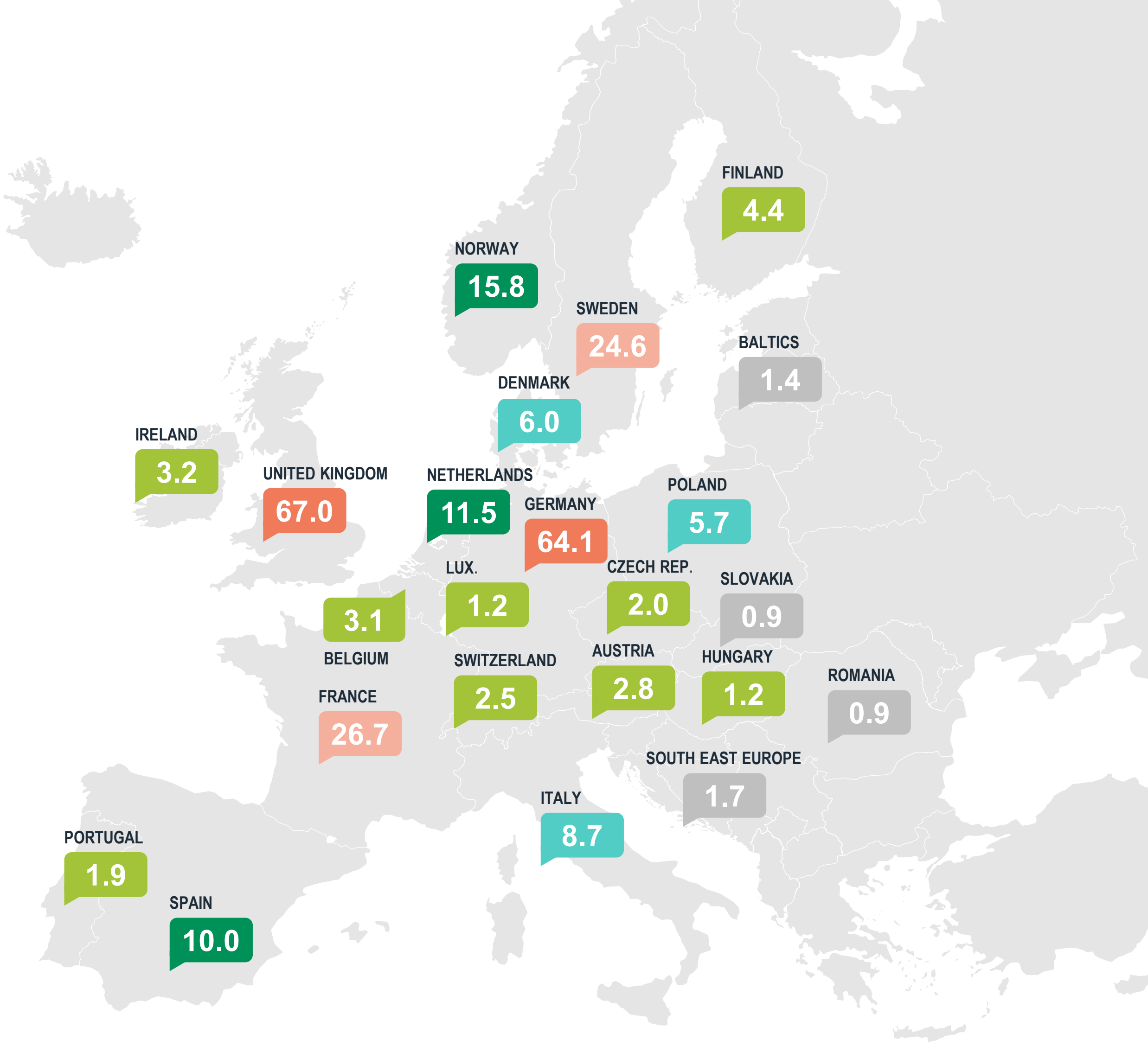
- After an all-time high in Q1 2020 (€319bn over 12 months), investment plummeted over 2020 and reached its lowest point at Q1 2021 (€212bn), 12% below the 5-year average. Investment was inhibited by the lockdowns all over Europe, travel restrictions as well as hesitation from institutional investors that adopted a wait-and-see attitude.
- Investment traction restored from Q2 2021 (€242bn) as European countries gradually took control of the outbreak mainly through vaccination and with the help of the summer lull in virus transmission. Q2 2021 (+70% vs Q2 2020) saw a strong impulse in investment, while the increase in Q3 and Q4 2021 (+29% and +22%) was moderate, almost reaching the average of the previous years.
- Most asset classes are affected by this turn of events, in positive or negative ways. Logistics profited from greater trust shown in e-commerce expansion. Office investment improvement is balanced as teleworking put a clear divide between modern and older units. Retail investment seems to have flattened with the sector becoming more opportunistic in character.

This excludes residential investment.

COMMERCIAL REAL ESTATE INVESTMENT

2021 vs 2020

GERMANY	+7%
UNITED KINGDOM	+21%
FRANCE	-8%
NETHERLANDS	-8%
ITALY	+4%
SPAIN	+31%
POLAND	+15%
IRELAND	+84%
BELGIUM	-44%
CZECH REPUBLIC	+47%
LUXEMBOURG	+7%



- ≥ €50bn
- €20-50bn
- €10-20bn
- €5-10bn
- €1-5bn
- < €1bn

(excludes residential investment)

Source : BNP Paribas Real Estate

EUROPE – 2021

€272.7bn

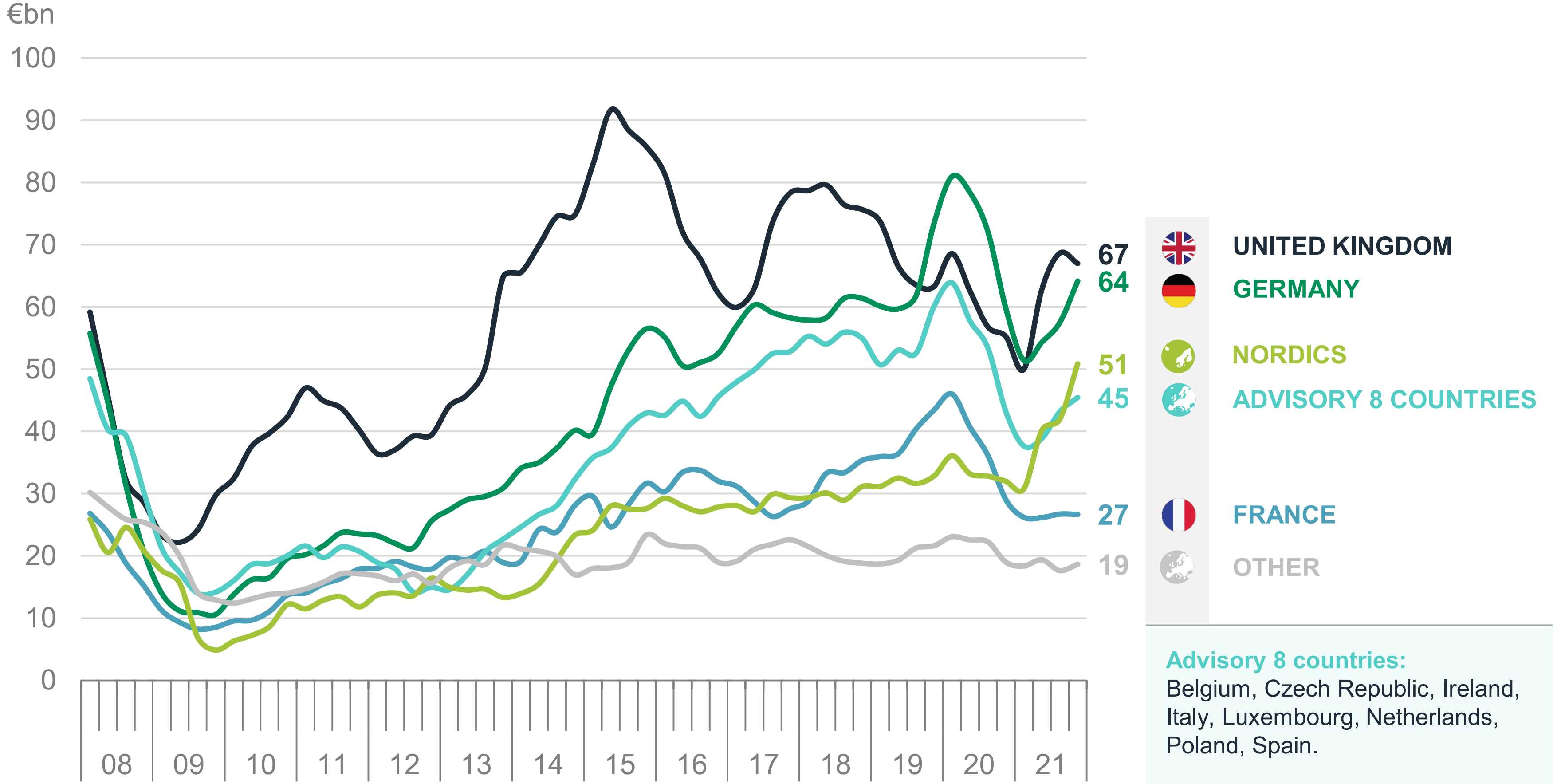
+15% vs 2020

- €272.7bn was invested in Europe over 2021, which represents a 15% increase vs 2020, in line with the pre-Covid-19 levels.
- However, a closer look at European countries shows geographical variance. The improvement in the United Kingdom, Germany, Sweden and Spain marked the rising trend. Investment levels in some other countries such as France, the Netherlands or Belgium are still below those of 2020.

COMMERCIAL REAL ESTATE INVESTMENT VOLUME

PROPERTY REMAINS AN ATTRACTIVE ASSET TO BUY

CRE Investment volume (€ billion)



Advisory 8 countries:
Belgium, Czech Republic, Ireland, Italy, Luxembourg, Netherlands, Poland, Spain.

- There is no comparison between the impact of the current crisis on investment volumes and that of the global financial crisis of 2008/9 throughout Europe. Volumes remain high, as today's credit conditions are not tight, and investors don't expect major deflation in prices in most markets for secure assets. Cash is there and definitely king over the current period.
- All countries are trending up except for France, which remained flat over 2021.
- The United Kingdom benefited from its advanced vaccination campaign and from the post-Brexit dynamic as investors returned to the market. It is back in top place among European countries despite a weaker Q4.
- Northern Europe suffered the least from the pandemic, and is even experiencing a surge in investor interest, with Sweden and Norway reaching all-time highs.

Source: BNP Paribas Real Estate Research.

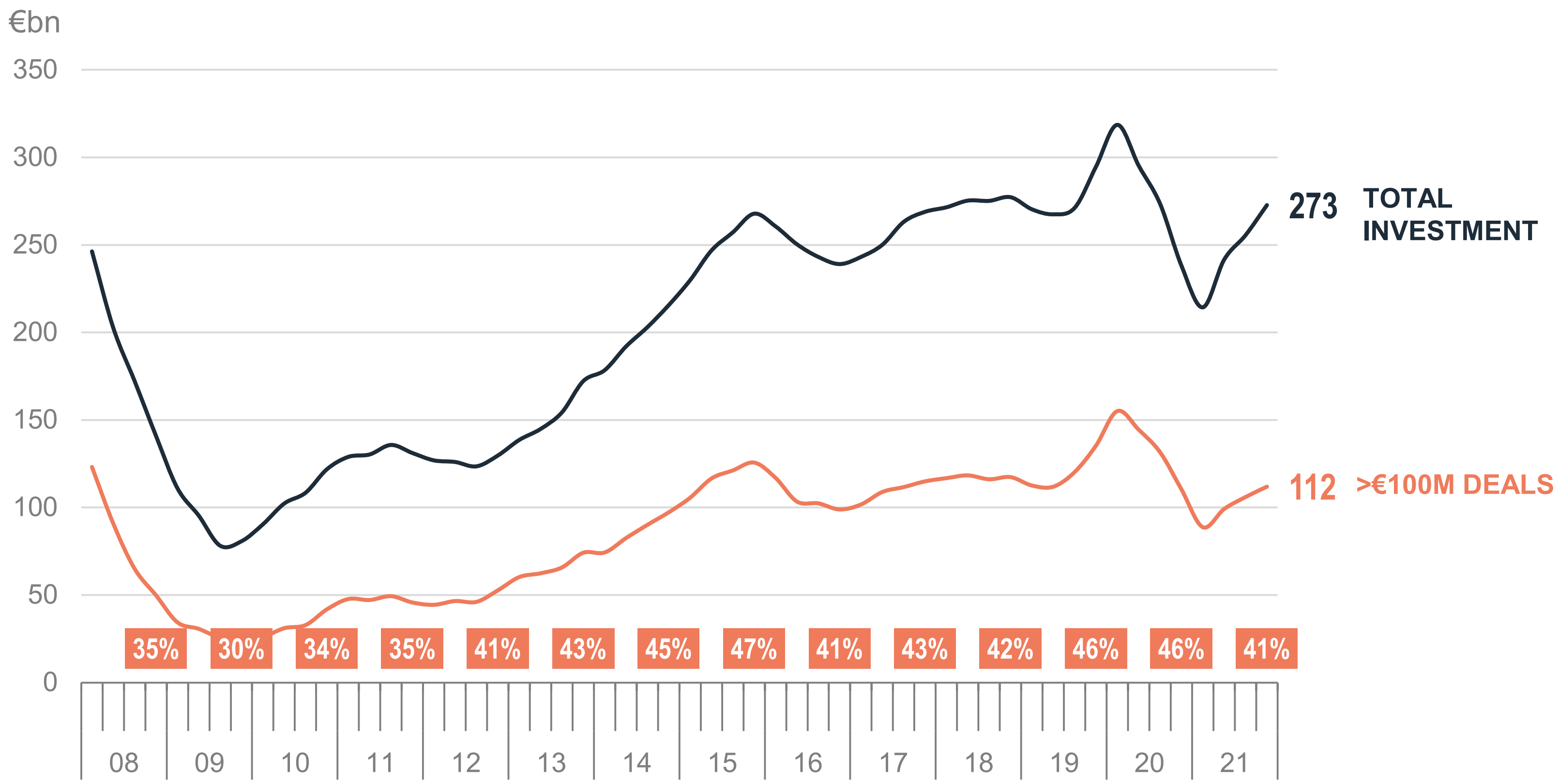
INVESTMENT BY SIZE BAND

MEGA DEALS MORE IMPACTED BY THE CRISIS

- Mega deals (>€100m) volume in Q1 2020 reached a record figure of €155bn (on a rolling-year basis), which represents 48% of the total investment, an unusually big share for a Q1. Mega deals had been on the rise from mid-2019.
- The volume of mega deals dropped from Q2 2020 and only reached €89bn at Q1 2021 on a rolling-year basis, down -43% vs the 12 months to Q1 2020 figure, versus -33% for total investment. The situation improved for mega deals too over the rest of 2021, albeit more slowly than for the other deal size segments.
- Big deals are more complicated and require a longer process before signature. The signature is a legal formality for a deal already done. This may explain why the corona virus outbreak initially impacted smaller deals. The process for small deals is easier to terminate. Yet as the crisis went on, the momentum behind closing big deals diminished because of the mobility problems of lockdown. With travel becoming easier, this segment maybe gaining traction again, although it will possibly be the slowest to restore full market normality.

Commercial Real Estate Investment in Europe

Total and >€100m size band - volume and share



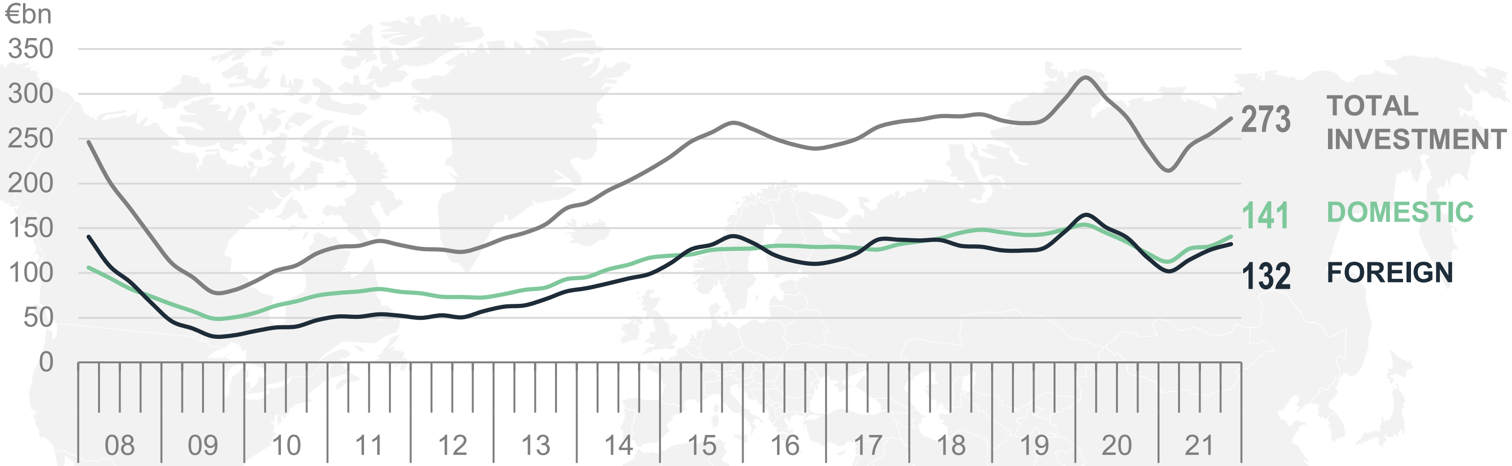
Source: BNP Paribas Real Estate.

CROSS-BORDER INVESTMENT MARKET

- **Foreign investment** was hindered by the spread of the virus through Europe. In spring 2020, m**ost foreign investors delayed their ongoing deals** until Europe was open again. Over the twelve months to Q1 2021, foreign investment plummeted (-38% vs Q1 2020), although the situation improved over the rest of 2021.
- Within foreign investment, **European cross-border investment was less affected** which makes sense as nearby deals were easier to do during the lockdowns. It increased by 7% in 2021 vs 2020.
- Conversely, investment from other continents was hit hard by the crisis. But the post crisis period seems to be differing from one continent to the next.
- On the one hand, **American investors** showed strong interest in the European market in 2021. With more than €41bn spent over the year, American investment is **back to pre-crisis levels**.
- On the other hand, investors from Asia Pacific and Middle East don't seem to be as active in their European investments. **They represented respectively 8% and 4% of foreign investment, which is very low** considering Asians represented around 20% of foreign investment back in 2019.
- As observed in 2009, the reduction in cross-border deals in Europe **was somewhat compensated by domestic investment** during the pandemic. But as restrictions eased, foreign investment resumed much more strongly than expected.

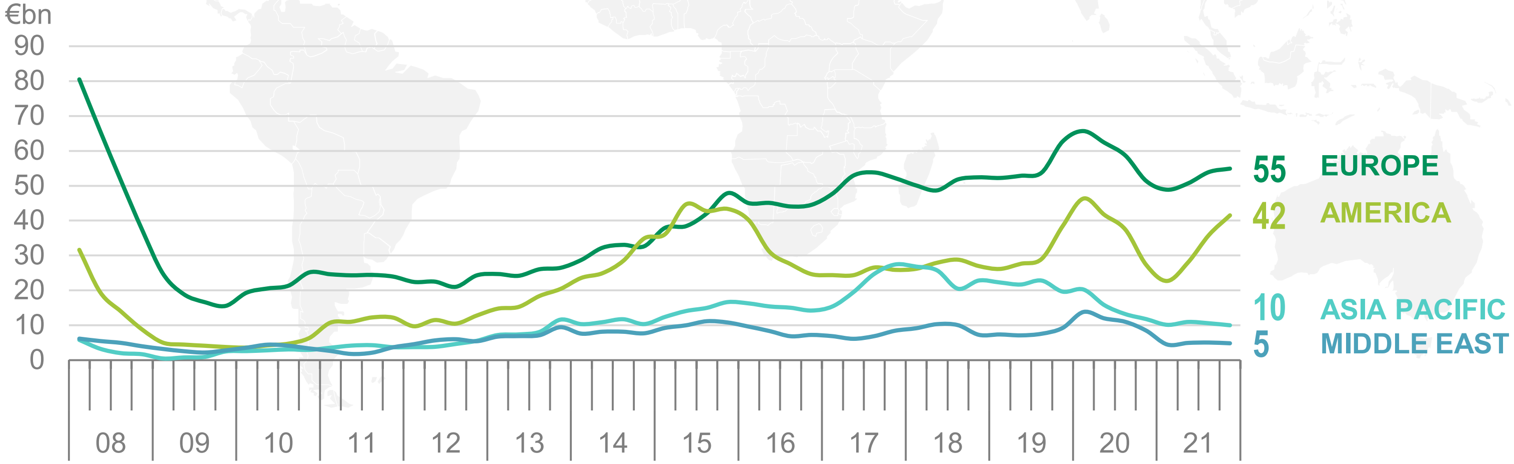
Commercial Real Estate Investment in Europe

Total, foreign and domestic investment



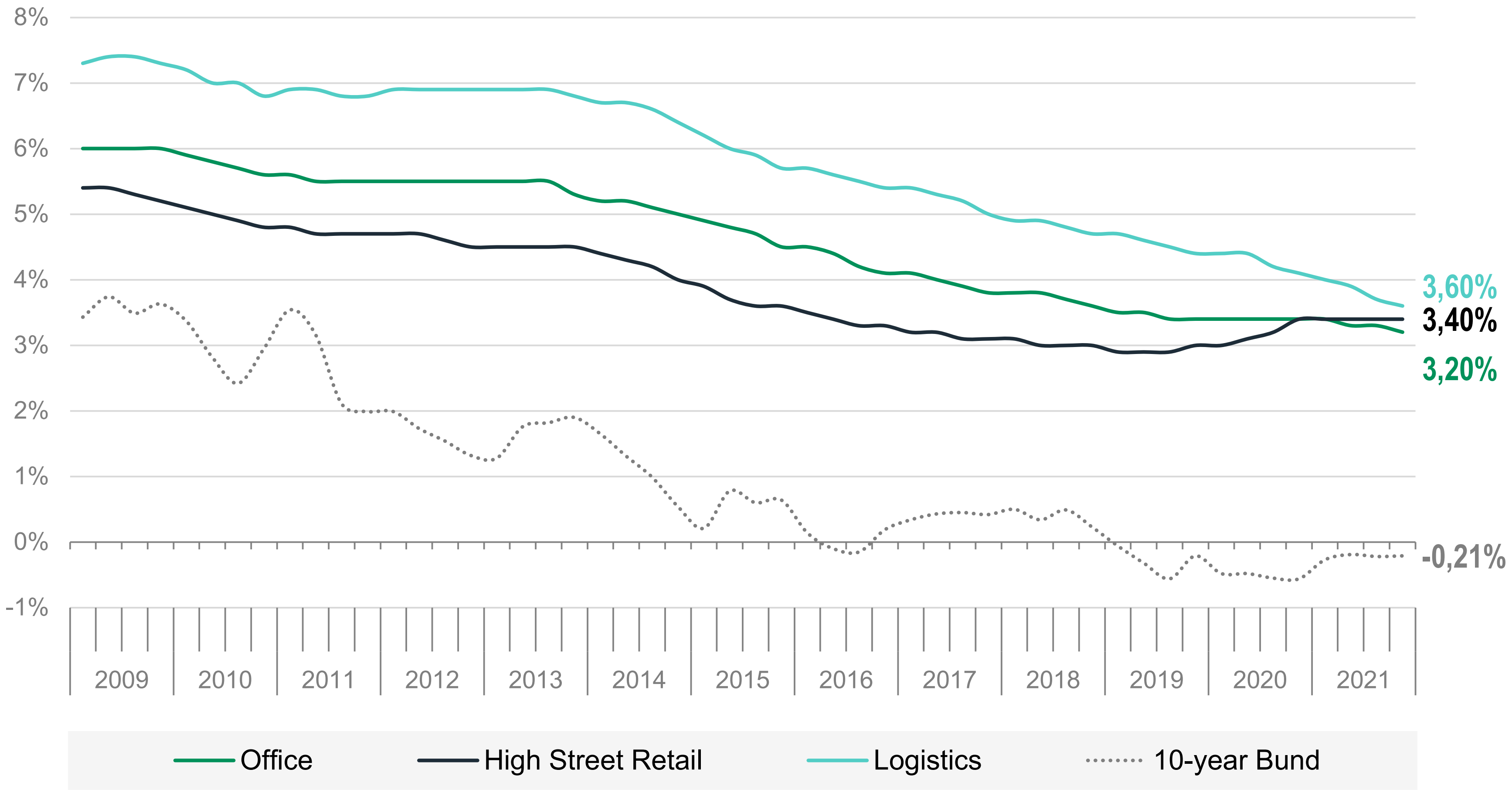
Commercial Real Estate Investment in Europe

Foreign investment detail



AVERAGE PRIME YIELDS IN EUROPE

BASED ON 15 MARKETS



Source: BNP Paribas Real Estate Research.

- After drawing to a halt during 2020, office prime yields froze all over Europe, but they seem to be narrowing again.
- Prime retail yields also froze and are now expanding again in some markets.
- Prime logistics yields, on the other hand, boosted by the scarcity of assets, continually decreased during the crisis. Compression accelerated from Q2 2021 and is ongoing.

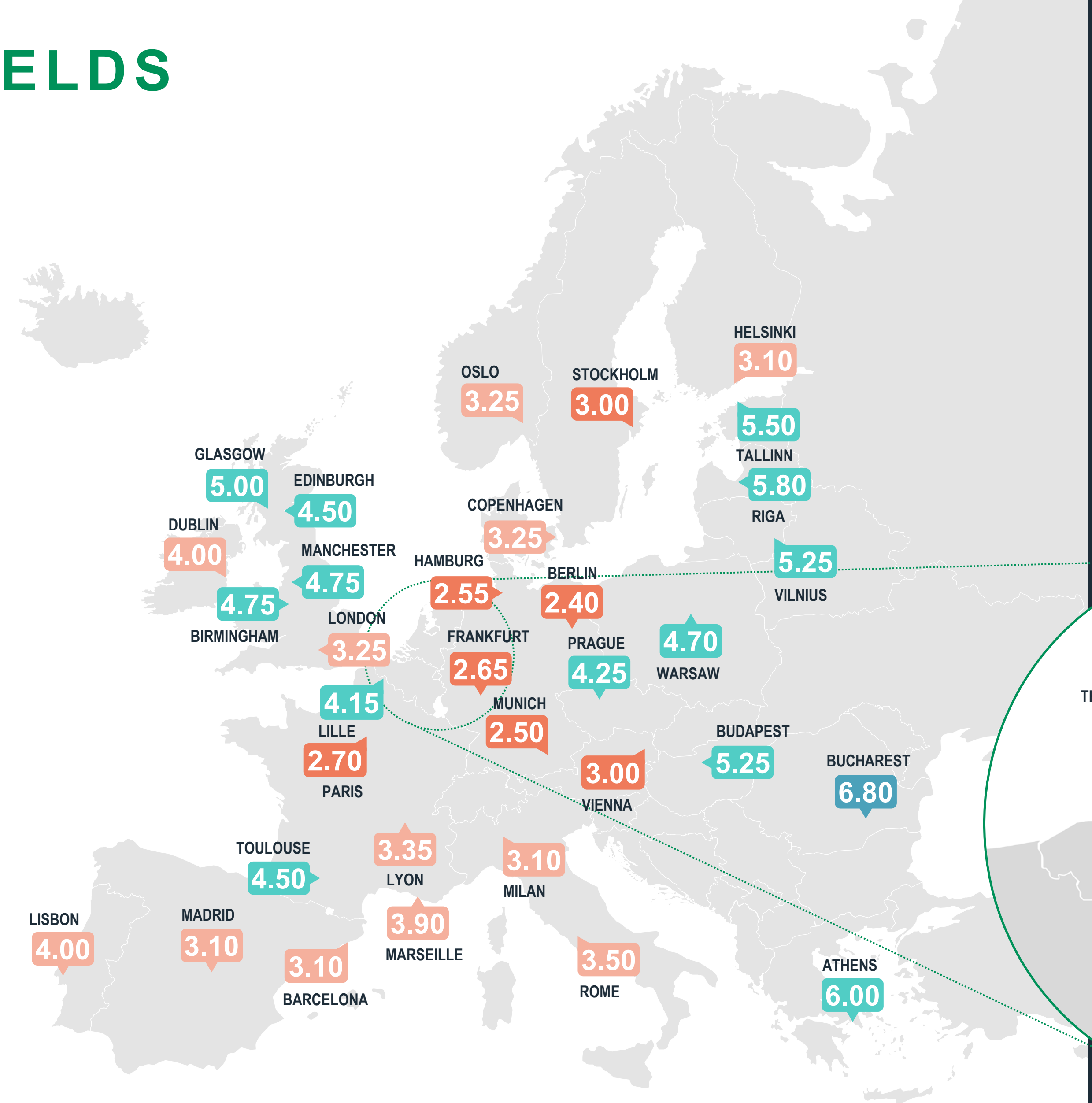
Based on 16 cities: Amsterdam, Berlin, Brussels, London, Paris, Dublin, Frankfurt, Hamburg, Lisbon, Luxembourg, Madrid, Milan, Munich, Prague, Vienna and Warsaw.

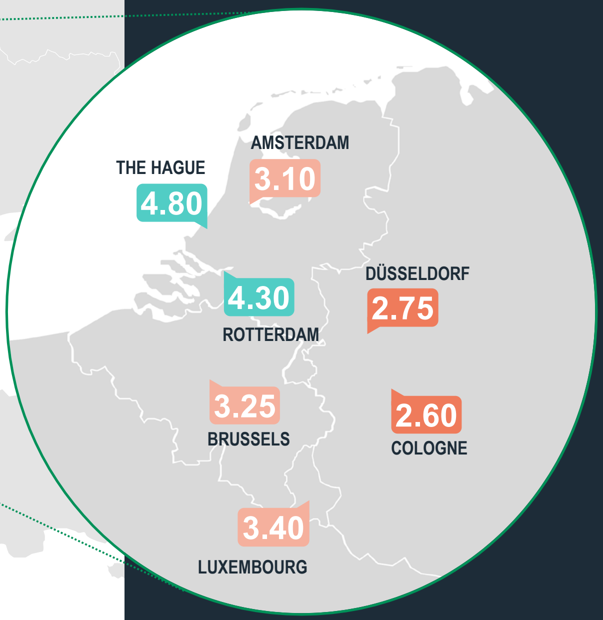
PRIME OFFICE YIELDS

Q4 2021 vs Q4 2020

BERLIN	-15bp
PARIS	=
AMSTERDAM	=
MADRID	-40bp
MILAN	-10bp
LONDON	-25bp
LUXEMBOURG	-30bp
BRUSSELS	-65bp
DUBLIN	=
PRAGUE	-25bp
WARSAW	+10bp

- ≤ 3%
- 3-4%
- 4-6%
- >6%





Source: BNP Paribas Real Estate

- The downward trend in office prime yields, ongoing for several years, slowed or ceased in most markets in 2020. Yet they kept narrowing in most European cities.
- With reopening, most European markets are now back to prime office yield compression, except for Paris, Amsterdam and Dublin where they remained stable while it was expanding in Warsaw.

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REAL ESTATE PERSPECTIVES

OFFICE MARKETS

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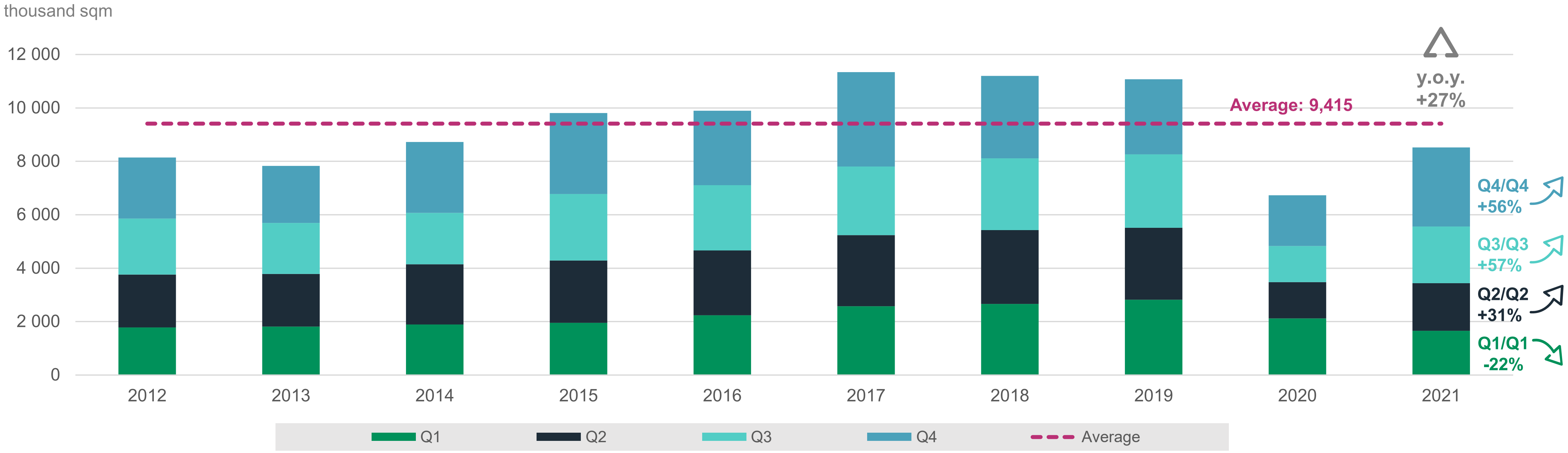
OFFICE TAKE-UP IN EUROPE – 2021

18 MAIN EUROPEAN OFFICE MARKETS*



Gradual improvement in letting activity throughout 2021

- 8.52m sqm was transacted in Europe's 17 main markets over 2021. Even though the start to the year was quieter than expected due to recurring waves of infection, take-up started to recover from Q2 and showed continuous improvement afterwards.
- Even though the overall result for 2021 is – as anticipated – still below the pre-crisis levels (-8%), signs of normalisation in letting activity are in sight.
- Indeed, take-up reached 2.95m sqm during Q4 2021, which is in line with pre-covid usual volumes for Q4.
- Most markets show strong rebound in volumes, such as in Barcelona (+85% vs. 2020), Central London and Brussels (+46% each), Central Paris (+36%) or in the 6 main German markets (+27%)

Source: BNP Paribas Real Estate Research.

* Berlin, Cologne, Dusseldorf, Frankfurt, Hamburg, Munich, Central Paris, Central London, Brussels, Barcelona, Madrid, Dublin, Milan, Rome, Luxembourg, Amsterdam, Warsaw, Prague

OFFICE TAKE-UP IN EUROPE

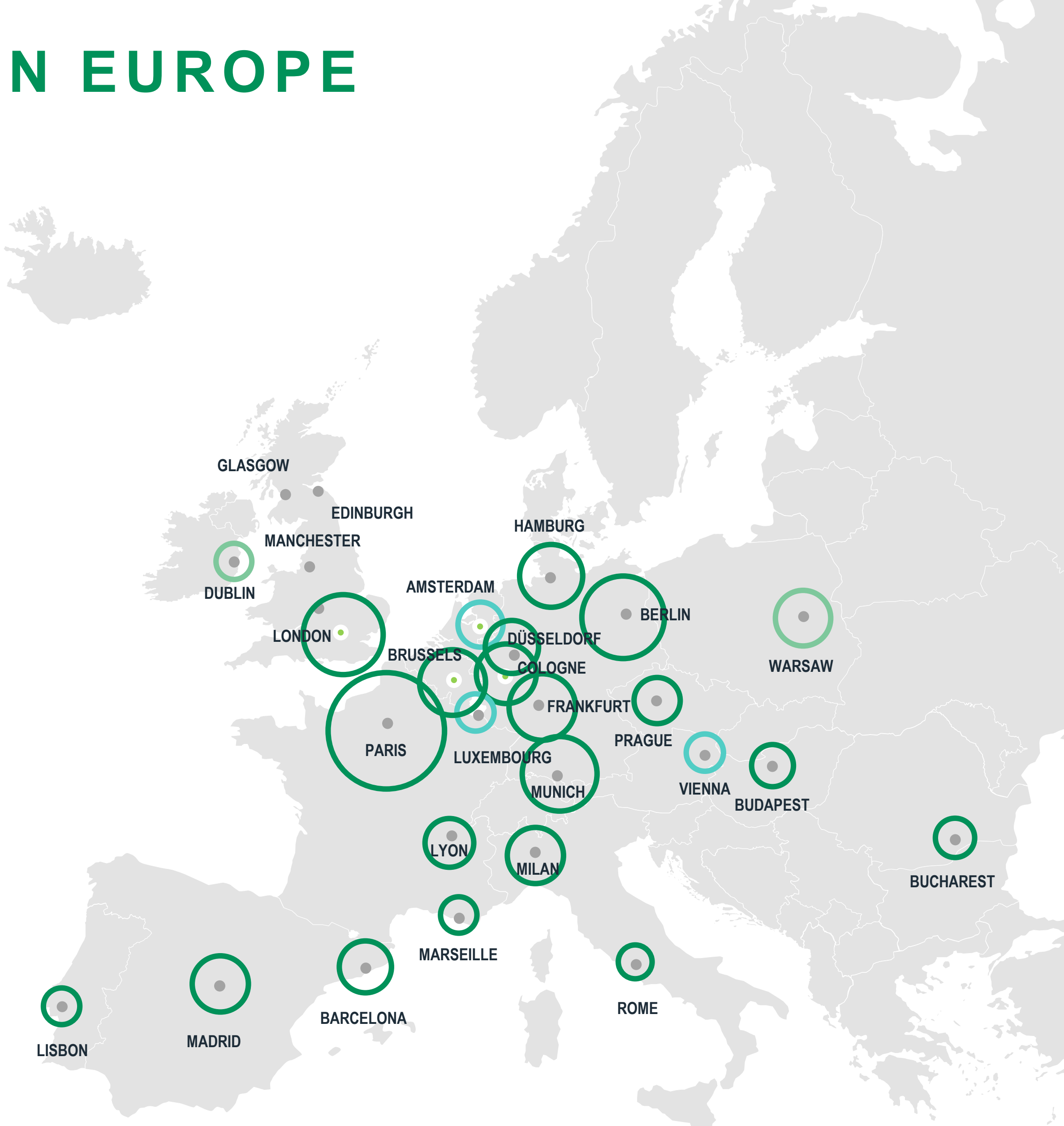
2021 vs 2020

CENTRAL LONDON	+46%
BERLIN	+17%
CENTRAL PARIS	+36%
AMSTERDAM	-11%
MADRID	+8%
MILAN	+34%
WARSAW	-3%
BRUSSELS	+46%
DUBLIN	-2%
LUXEMBOURG	-25%

Deals in thousand sqm

1,000
500
250

- > +5%
- 0 - +5%
- -5 - 0%
- < -5%



Source: BNP Paribas Real Estate.

EUROPE – 2021

10.08M sqm

26 markets
+27% vs 2020

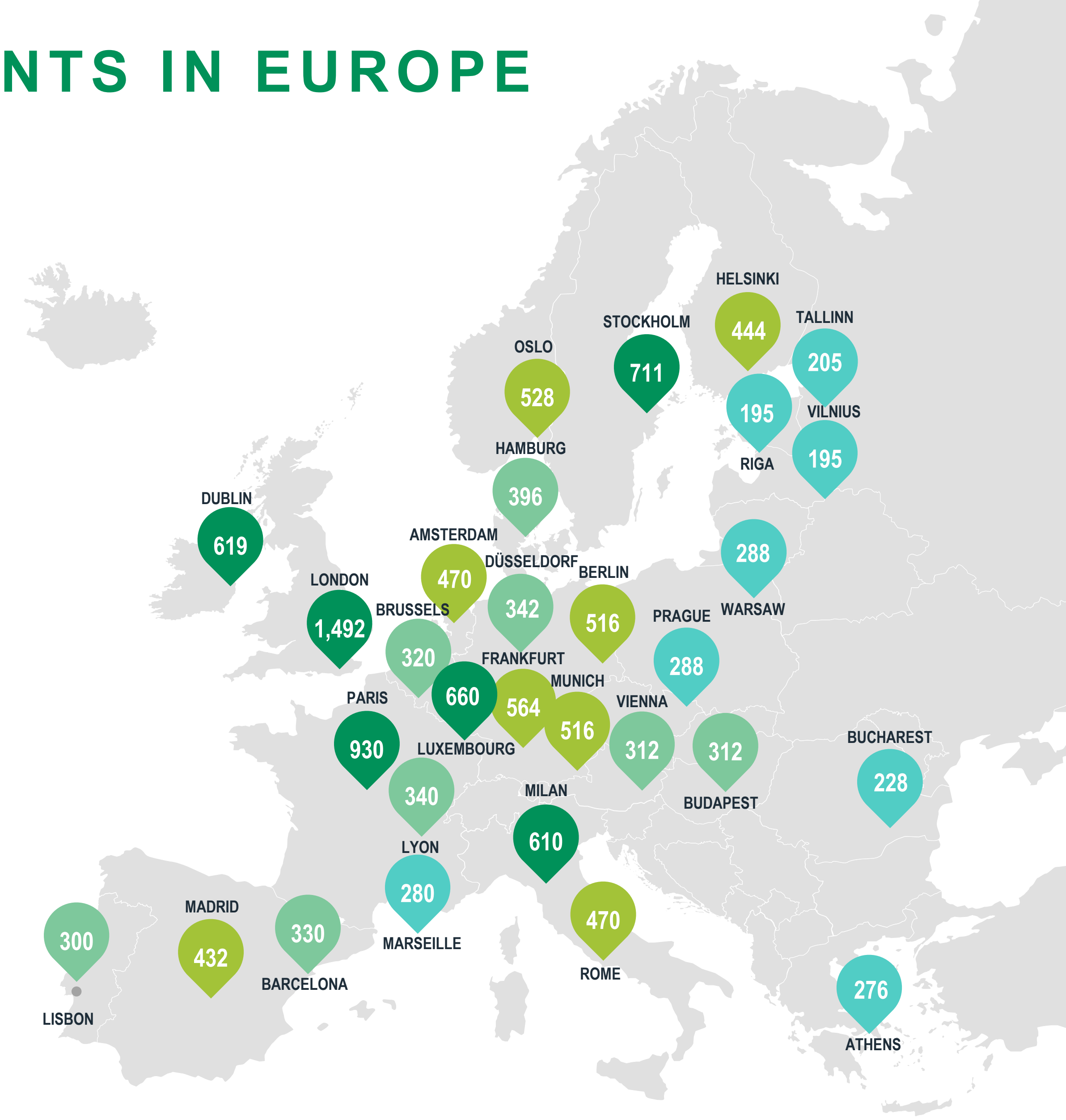
Strong increase in volumes but pre-covid levels are not reached

- Take-up at the end of 2021 saw a significant increase (+27%) compared to last year.
- 10.08m sqm was taken up in Europe, which is still far from the pre-covid years, when take-up amounted to approximately 13m sqm yearly (2017-2019).
- Volumes were on the rise in most markets. The market was buoyant in Central London and Brussels (+46% each) whereas cities such as Amsterdam, Luxembourg, Warsaw and Dublin still recorded decreases.

OFFICE PRIME RENTS IN EUROPE

Q4 2021 vs Q4 2020

CENTRAL LONDON	+4%
BERLIN	+8%
CENTRAL PARIS	+3%
AMSTERDAM	+2%
MADRID	-1%
MILAN	+2%
WARSAW	+4%
BRUSSELS	+2%
DUBLIN	-5%
LUXEMBOURG	+10%



Source: BNP Paribas Real Estate

Prime rents were mostly unaffected by the crisis

- Despite the slowdown in take-up, the prime market segment did not suffer from the crisis.
- Indeed, in most markets, prime rental values never decreased over the outbreak of the pandemic, and many of them are even higher than their pre-crisis level.
- The very low availability of prime assets and the appeal of high quality buildings located in the most sought-after districts drove the values up.
- Luxembourg (+10%) and Berlin (+8%), where vacancy rates are among the lowest in Europe, have seen the most significant increases in values.

LOCATIONS

(JANUARY 2022)

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ALLIANCES

AUSTRIA | CZECH REPUBLIC | DENMARK | ESTONIA | FINLAND | GREECE | HUNGARY | JERSEY | LATVIA | LITHUANIA | NORTHERN IRELAND | NORWAY | PORTUGAL | ROMANIA | SWEDEN
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