

FAIR VALUE INDEX

Q1 2023

TABLE OF CONTENTS



SUMMARY

ECONOMIC ASSUMPTIONS

CAPITAL MARKET OVERVIEW

FAIR VALUE INDEX RESULTS

ABOUT THE EUROPEAN FAIR VALUE INDEX

The index was launched in August 2010 and covers 120 markets across Europe.

Fair value is the value at which an investor is indifferent between a risk-free return and the forecast return from holding property, taking into account the extra risk of investing in the property asset class.

When a property price is at fair value, an investor is being adequately compensated for the risk taken in choosing to purchase real estate; similarly, when the property price is below the fair value price, an investor is being more than compensated for the risk taken in choosing to purchase real estate. When buying at or below fair value, an investor does not necessarily buy at the bottom of the market.

Our fair value analysis focuses on prime assets and a five-year investment horizon and hold for the market overall; individual transactions may provide opportunities and risks beyond the average market view. In the report, we compare results for the current quarter with the previous quarter, which may differ from those published in the previous quarter's report; this is due to the forward-looking methodology. As such, when our forecasts change so too does the Fair Value Index.

SUMMARY

The European Fair Value Index score increased in Q1 2023 to 20, up from 0 in Q3 2022, indicating that commercial real estate valuations are beginning to turn, heading toward fair value.

Since our previous update real estate investor sentiment remains tested, with the continuation of interest rate rises which has not only heightened uncertainty regarding the outlook but has also provided challenges in pricing assets to reflect current conditions. The general consensus remains that the investment market will pick up in H2 2023 once pricing reaches equilibrium, narrowing the expectations between buyers and sellers. However, this is largely dependent on where interest rates will settle in the medium term – which will influence the return of activity in this next cycle.

Overall, the fair total return was lower in Q1 for 87% of the markets covered in our analysis versus six months ago. Fair total returns were higher in 16 markets, with noticeable improvements in Sofia and Hague offices, and Berlin logistics.

Although over the past six months, 5-year bond yields have continued to increase for most markets, we have begun to witness yields trending down, namely in Poland (-148 bps), Hungary (-107 bps), UK (-106 bps), Czech Republic (-65 bps), Italy (-31 bps) and Norway (-27 bps).

The majority of the 120 markets covered in the analysis are classified as ‘fully priced’ (67%) followed by ‘fairly priced’ (27%) and ‘underpriced’ (7%).

Sector-level data reveals there are still a few opportunities in the logistics sector, with all (eight) markets that are currently underpriced within the logistics sector. Of the markets that are now fairly priced, all but one (Rotterdam logistics) have been upgraded from being fully priced in the previous update, i.e. property yields have moved to be within our threshold of the fair value yield.

Geographically, market classifications remained in line with the previous update, with the exception of the UK, which is now witnessing a greater share of ‘underpriced’ and ‘fairly priced’ markets. This is not surprising given the rapid outward adjustment in yields that occurred in the UK, and in particular, in the logistics market.

ECONOMIC ASSUMPTIONS



Economic growth surprised on the upside in Q1, with the euro area achieving growth of 0.1%. This follows a downward revision to the previous quarter, now estimated to have registered -0.1% Q/Q. As a whole, the euro area looks to have narrowly avoided a 'technical' recession for now, however, there is no denying that growth remains muted.

Short-term events do have an impact on the bond market, even if they are temporary. Over the past twelve months, we have witnessed persistent inflation which has changed the landscape of the bond market. Although 5-year bond yields have been increasing for most markets, we have begun to witness yields trending down, namely in Poland (-148 bps), Hungary (-107 bps), the UK (-106 bps), Czech Republic (-65 bps), Italy (-31 bps) and Norway (-27 bps). Elevated political uncertainty in the UK and the fact that the Central Eastern European (CEE) tightening cycle began ahead of the European Central Bank (ECB) placed pressure on CEE and UK bonds.

Preliminary data indicates euro area inflation accelerated in April, and as a result, markets are pricing in further interest rate rises. Although the ECB has slowed the pace of its interest rate increases with a 25-bps increase (previous three have been 50-bps), they have signalled more tightening as it continues to fight against inflation.

Euro area	2021	2022	2023	2024
Real GDP (Y/Y % chg)	5.3	3.5	0.9	1.6
Employment Growth (Y/Y % chg)	1.4	2.3	1.1	0.6
Unemployment Rate (%)	7.7	6.7	6.9	7.1
Inflation (Y/Y % chg)	2.6	8.4	5.4	2.4
5-year Govt Bond Yield* (% Annual average)	-0.4	1.4	3.3	3.2

* Central government bond yield curve – Euro area average - Spot rate – 5-year maturity

Source: Moody's Analytics (*May vintage*)

CAPITAL MARKET OVERVIEW



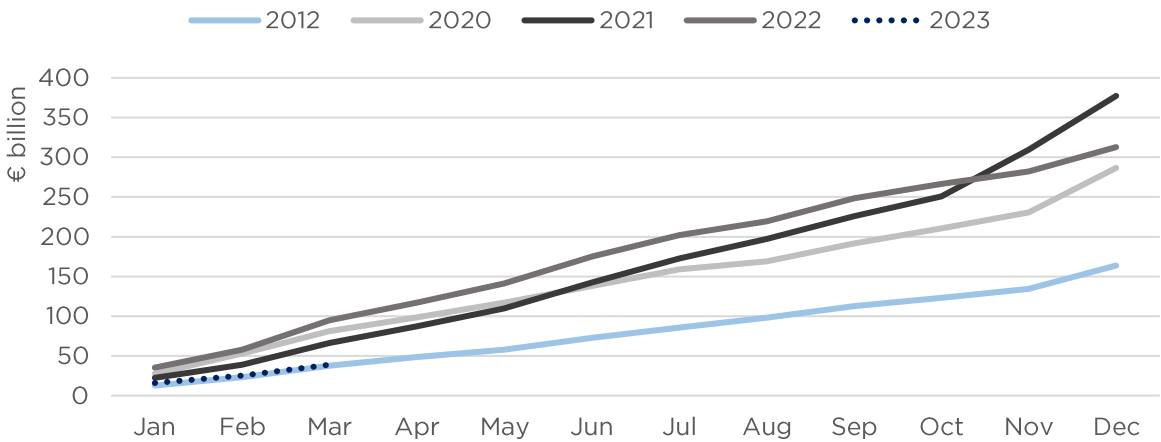
Total European investment volumes fell by 62% Y/Y in Q1 2023. Volumes were down in almost all the major property sectors with the exception of hotels.

In Q1 2023 the fall in office investment (-64%) accelerated, reaching a 13-year low. The office sector continues to battle the headwinds associated with hybrid working, evolving occupier requirements as well as ESG.

Noticeably, the industrial sector witnessed the largest Y/Y decline in volumes which were down by 76%. This was led by the decline in deals in the UK where deals have fallen from €8.6bn in Q1 2022 to just €1.4bn in Q1 2023, which is unsurprising given the fall in capital values. It is important to note that base effects are at play here – the logistics sector has witnessed record-breaking levels of investment over the past few years, therefore a decline in volumes was expected.

Retail investment volume has held up better despite the very low base. The fact that retail has already undergone rapid repricing provided a buffer for a further substantial adjustment. Nonetheless, the sector is not immune to wider uncertainty and low investor sentiment. Volumes fell by 43% Y/Y.

Cumulative investment volumes by month for each year



Source: MSCI Real Capital Analytics

Performance at the country level is no different, with most witnessing a continued slowdown from Q4 2022. Germany is amongst the most affected markets; volumes were down by 71% Y/Y in Q1 2023. Spain is one of the bright spots in Europe. It was the fourth most active country in Q1, despite volumes being down by 13% Q/Q; volumes were up by 22% if we look at the 12-month rolling. The Spanish market was mainly supported by strong demand for apartment and hotel properties.

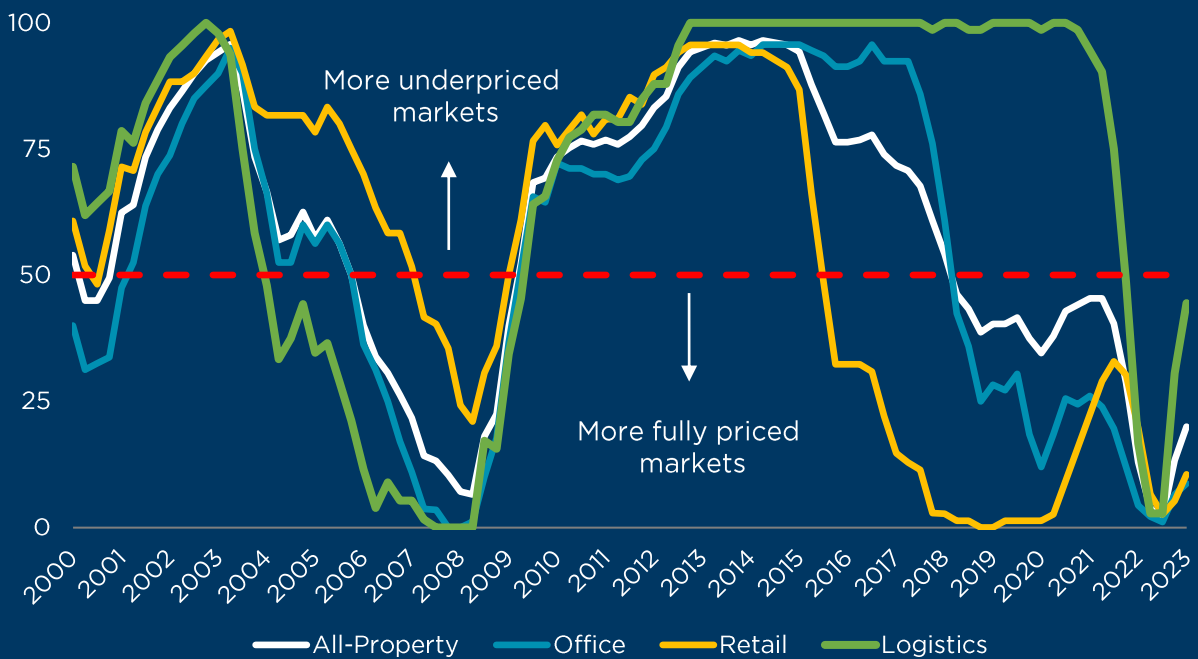


FAIR VALUE INDEX RESULTS



The European Fair Value Index score increased in Q1 2023 to 20, up from 0 in Q3 2022, indicating that commercial real estate valuations are beginning to turn, heading toward fair value.

The fair value index score encompasses the annualised nominal returns a property investor could expect over a five-year investment horizon in their chosen market with the estimated risk-adjusted nominal required (fair) return for that market. As an example, the results for this quarter compare the annualised returns an investor could expect from property investment over the five-year period (from Q1 2023 to Q4 2027) with the fair return for investment over that period. Our view from our previous forecasts was relatively unchanged, with yields expected to continue moving out, at least in H1 2023 (this varies across sectors), rental growth has surprised on the upside with some markets witnessing upgrades to rental growth prospects.



Source: Bloomberg; Moody's Analytics, Cushman & Wakefield Research

Overall, the fair total return was lower in Q1 for 87% of the markets covered in our analysis versus six months ago. Fair total returns were higher in 16 markets, with noticeable improvements in Sofia and Hague offices, and Berlin logistics.



FAIR VALUE INDEX RESULTS



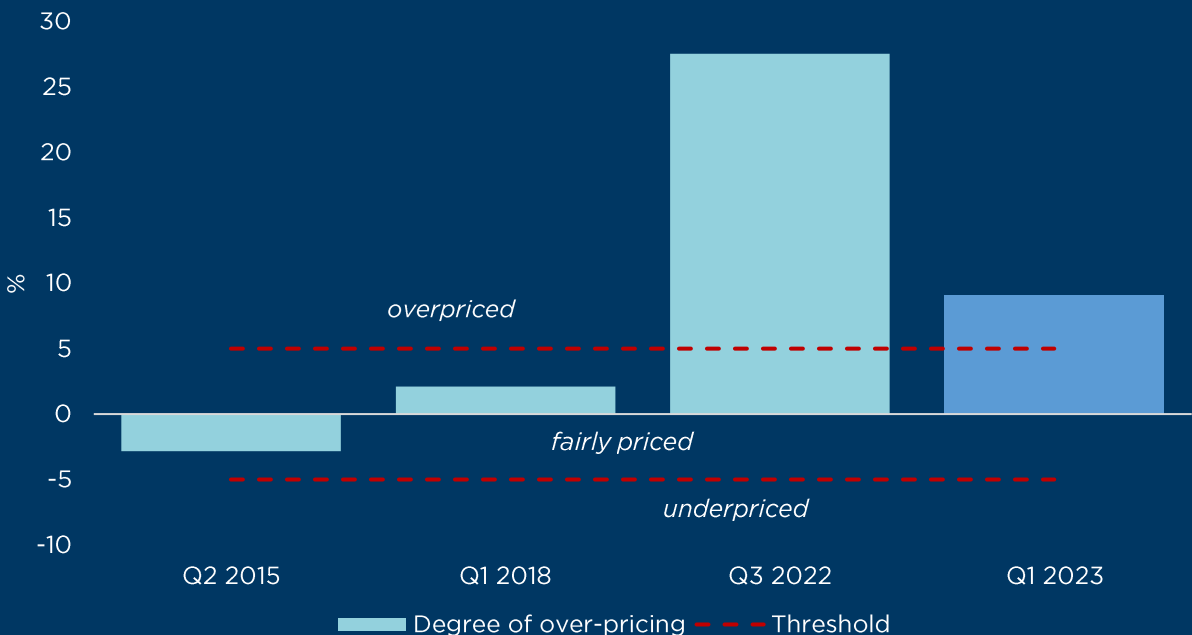
Real estate investor sentiment remains tested, with the continuation of interest rate rises which has not only heightened uncertainty regarding the outlook but has also provided challenges in pricing assets to reflect current conditions.

The general consensus is that the investment market will pick up in H2 2023 once pricing reaches equilibrium, narrowing the expectations between buyers and sellers.

However, this is largely dependent on where interest rates will settle in the medium term – which will influence the return of activity in this next cycle.

Rental growth has been upgraded across all sectors. Looking ahead, prime office rental growth will average 3.3% this year across Europe. Prime high streets have seen rent levels remain stable. Given the backdrop of a weak consumer outlook, we expect muted rental growth across Europe in 2023. Expectations are for momentum for logistics rental growth to remain throughout the year, averaging 7.3% for 2023 overall.

As shown in the chart below, the commercial real estate market remains overpriced, despite improving significantly from Q3 2022.



Source: Cushman & Wakefield Research



FAIR VALUE INDEX RESULTS



The majority of the 120 markets covered in the analysis are classified as 'fully priced' (67%) followed by 'fairly priced' (27%) and 'underpriced' (7%). The degree of market overpricing ranges from approximately 5-30%.

Across all sectors and all markets covered, there were no downgrades. There were no changes for the majority of the markets covered, with the remaining 33% being upgraded.

A further breakdown of the markets that were upgraded reveals, 80% of the markets went from being fully priced to fairly priced, and the remaining 20% were upgraded from being fully priced to now being underpriced. These upgrades were due in part to the stabilisation seen in sovereign bond yields and the largest re-pricing with year-end property yields moving out since H1 2022.



TOP 5 UNDER PRICED MARKETS

- 1 Newcastle logistics
- 2 Cardiff logistics
- 3 Birmingham logistics
- 4 West London logistics
- 5 Northampton logistics

TOP 5 FULLY PRICED MARKETS

- 1 Istanbul offices
- 2 Budapest offices
- 3 Istanbul retail
- 4 Budapest logistics
- 5 Vienna offices

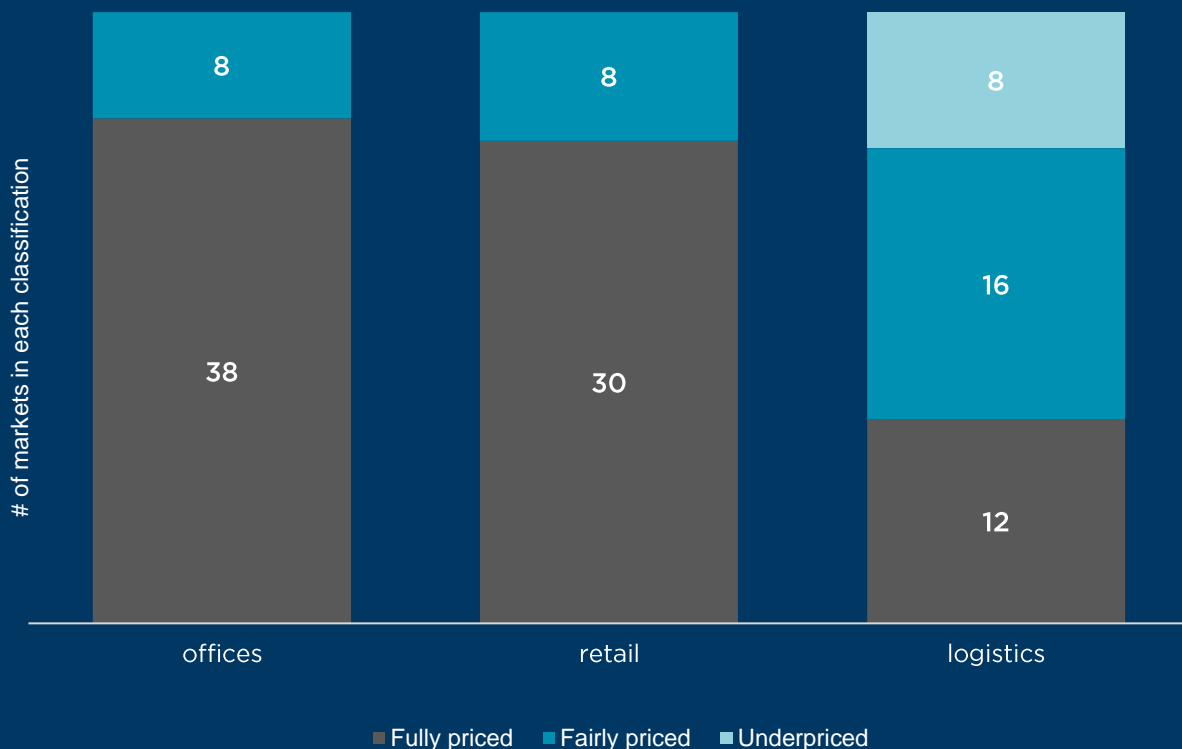


FAIR VALUE INDEX RESULTS

Sector-level data reveal there are still a few opportunities in the logistics sector, all eight markets that are currently underpriced are within the logistics sector.

Of the markets that are now fairly priced, all but one (Rotterdam logistics) have been upgraded from being fully priced in the previous update, i.e. property yields have moved to be within our threshold of the fair value yield.

Geographically, markets classifications remained in line with the previous quarter, with the exception of the UK, which is now witnessing a greater share of 'underpriced' and 'fairly priced' markets. This is not surprising given the rapid outward adjustment in yields that occurred in the UK, and in particular, in the logistics market.



Source: Bloomberg; Moody's Analytics, Cushman & Wakefield Research

DISCLAIMER



In using this data, the following should be noted:

- The data series has been prepared based on information which has been collected through our own research as well as information supplied by the client and material available to us from public and other external sources. In respect of all external information, the sources are believed to be reliable (unless stated) and have been used in good faith.

However, Cushman & Wakefield has not verified such information and cannot accept responsibility for their accuracy and completeness, nor for any undisclosed matters that would affect the conclusions we have drawn. Nonetheless, in interpreting the information used, we have had to rely on the validity and accuracy of the data and information sources available to us.
- We have taken every possible care in the collation of this data series. The data is believed to be correct at the time of reporting but may be subject to change during the life of the project and beyond and as new information becomes available. We reserve the right to change data without prior notice in the light of revised market opinion and evidence.
- In respect of any formal forecasting used in this project or any used in the background research supporting the opinions and material presented in this project, the following points should be noted and understood:
 - i. One is assuming that the historic data input to the forecasting process is accurate;
 - ii. The judgment of the forecaster(s) will influence the validity of the results;
 - iii. Unless stated, one is assuming that the market will continue to operate in future as it has in the past, and that its stability will not be disrupted;
 - iv. The forecasting is representative of only one moment in time;
 - v. The reliability of forecasts for the property market are dependent on the accuracy of the input forecasts for the economy as a whole; and
 - vi. The forecasts relate only to the type and quality of property indicated.
- In accordance with standard practice, we would confirm that the information is confidential to the parties to whom it is addressed, for their sole use, and for the stated purposes only. No responsibility is accepted to any third party in respect of the whole or any part of its contents. Neither the whole, nor any part of this project or data series, nor any reference thereto, may be included in any document, circular or statement without our written approval of the form and context in which it appears. It may not be reproduced by any means (electronic or otherwise) without prior written consent from Cushman & Wakefield.
- Information on assumptions, methodologies or definitions can be obtained from Cushman & Wakefield EMEA Research, London.

CONTACTS



SUKHDEEP DHILLON

Head of EMEA Forecasting
EMEA Research
Sukhdeep.dhillon@cushwake.com



GUILHERME NEVES

Senior Research Analyst
EMEA Research
guilherme.neves@eur.cushwake.com

About Cushman & Wakefield

Cushman & Wakefield (NYSE: CWK) is a leading global real estate services firm that delivers exceptional value for real estate occupiers and owners. Cushman & Wakefield is among the largest real estate services firms with approximately 50,000 employees in over 400 offices and approximately 60 countries. In 2021, the firm had revenue of \$9.4 billion across core services of property, facilities and project management, leasing, capital markets, and valuation and other services. To learn more, visit www.cushmanwakefield.com or follow @CushWake on Twitter.

Copyright © 2023 Cushman & Wakefield. All rights reserved. The information contained within this report is gathered from multiple sources considered to be reliable. The information may contain errors or omissions and is presented without any warranty or representations to its accuracy.

