FAIR VALUE INDEX

Q1 2024

CUSHMAN & WAKEFIELD

SUMMARY

PARADIGM SHIFT

THE EUROPEAN FAIR VALUE INDEX SCORE INCREASED IN Q1 2024, SIGNALLING THAT COMMERCIAL REAL ESTATE VALUATIONS HAVE REACHED THE TURNING POINT.

The higher Fair Value Index score suggests a growing number of investment opportunities are emerging.

Since our previous update real estate investor sentiment has been noticeably shifting. This is confirmed by our newly created TIME score, which shows CRE is currently in a transition phase.

This change in sentiment stems from the acknowledgment that interest rate hikes have ceased, diminishing uncertainties about the future outlook. This newfound clarity is facilitating the adjustment of asset pricing to accurately reflect present conditions and associated risks.

However, this varies by market, as markets that have not experienced sufficient repricing will constrain buyer interest.

The Fair Value Index covers 119 markets across Europe. Since the last update (Q3 2023), no markets experienced a downgrade. Instead, over two-thirds (66%) of the markets within our coverage are now deemed underpriced, with 29% of markets reaching fair value.

A sector breakdown reveals that the logistics sector continues to present more opportunities, with over four-fifths (82%) of logistics markets now considered underpriced, followed by the offices sector (63%) and retail (54%).

Geographically, market classifications points to the more liquid markets, UK, Germany and France witnessing a greater share of ‘underpriced’ and ‘fairly priced’ markets. This is not surprising given the rapid outward adjustment in yields that have occurred in these markets.

As both the European Central Bank (ECB) and the Bank of England (BoE) continue to see clear progress made on inflation both headline and core inflation (excluding more volatile items such as food and energy), and with wage costs somewhat easing we continue to expect that the ECB will begin to cut interest rates in June, followed by the BoE, expected to cut rates in August.

The prevailing expectation is that the lowering of rates would stimulate market activity and positively impact property values. In this context, the anticipation of rate cuts serves as a critical factor in shaping commercial real estate investment behaviour.

Notable improvements across most markets have been facilitated by a combination of improved total returns, fall in 5-year bond yields, and lowered credit spreads, thereby reducing risk.

The fluctuations in 5-year bond yields are influenced by various key factors, notably the recent decrease in inflation expectations has led to a corresponding decline in bond yields.

The increase in the Fair value index was largely anticipated, considering the further pricing adjustments over the past six months.

CAPITAL MARKET OVERVIEW

EVIDENCE INDICATES THAT CERTAIN MARKETS ARE EXPERIENCING STABILISED YIELDS OWING TO INTEREST RATE STABILISATION.

In Q1 2024, total investment volumes fell for the seventh consecutive quarter, down 26% year-over-year. Despite the overall transaction volume falling to its lowest level since 2011 this quarter we did see a moderation in the pace of decline. Within sectors, the office segment continues to face significant challenges, recording its weakest quarter in terms of deal volume on record.

Some evidence indicates that yields in certain markets have stabilised, especially in those that have experienced quicker yield adjustments. This stabilisation is attributed to the recognition that interest rate hikes are now behind us.

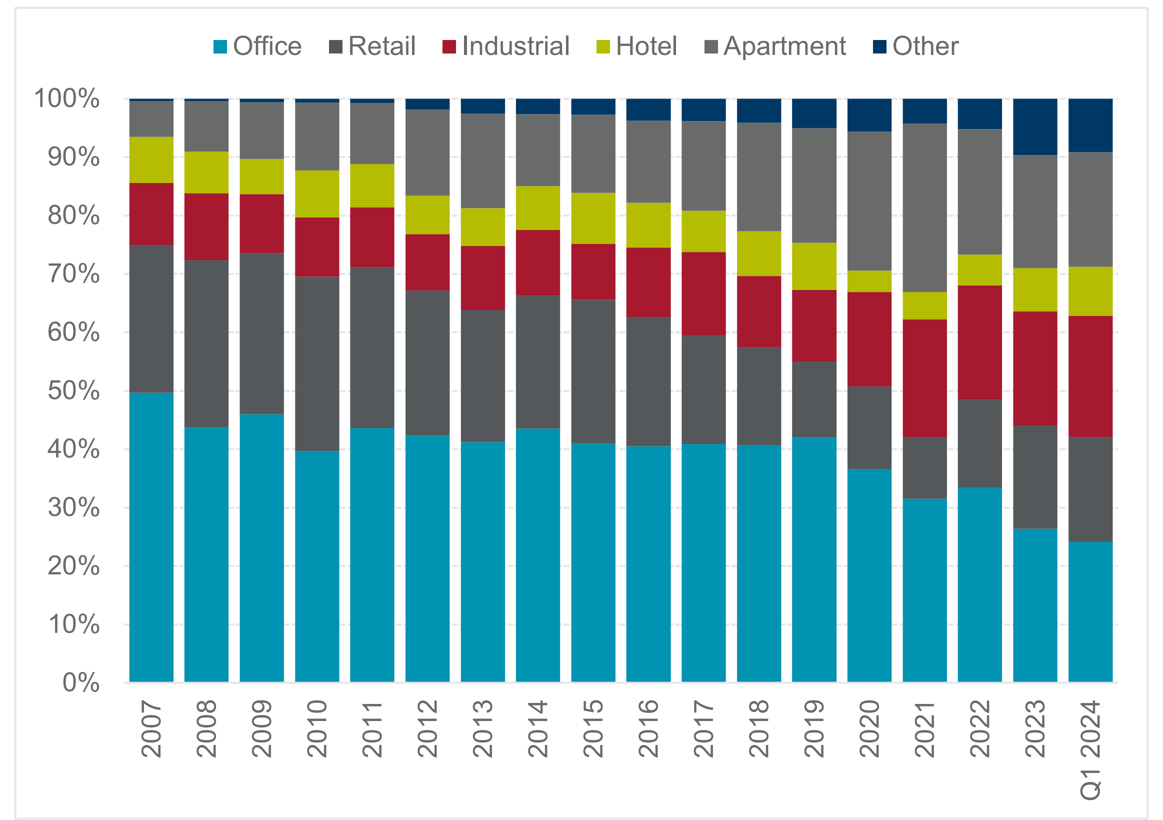
Over the period 2022-23 yields have moved out in total across Europe by 121 basis points (bp) – Office: +147bp; Logistics: +140bp and Retail: +72bp.

The common consensus now is that the first interest rate cut by the ECB will occur in June, the BoE to follow and cut interest rates in August.

Initially, it was anticipated that yields would level out in 2024; despite that being true for most markets, the situation is far more nuanced this year across sectors and markets. Sectors and markets that were slow to adjust to reflect the change in risk premium are likely to experience additional outward movements in H1 2024, which is reflected in the year-end figures. Conversely, sectors and markets that adjusted first and fast will see an increase in valuations in Q4, leading to yield compression.

Compression in yields across logistics and offices will occur mainly in 2025, with retail yield compression to follow in 2026, with a few exceptions.

EUROPEAN INVESTMENT BY SECTOR*



Source: MSCI, RCA

*excludes development

FAIR VALUE INDEX RESULTS

PRIME TIME

IF YOU BUY TODAY AND SELL AFTER A HOLD PERIOD OF FIVE YEARS IT WILL YIELD RETURNS HIGHER THAN THE RISK-ADJUSTED REQUIRED RATE OF RETURN.

The European Fair Value Index score rose to 81 in Q1 2024, up from 20 in Q3 2023, signalling that commercial real estate valuations have reached turning point, with more markets passing fair value.

The Fair Value Index covers 119 markets across Europe. Since the last update no markets experienced a downgrade. Instead, over two-thirds (66%) of the markets within our coverage are now deemed underpriced, with 29% of markets reaching fair value.

A sector breakdown reveals that the logistics sector continues to present more opportunities, with over four-fifths (82%) of logistics markets now considered underpriced, followed by the offices sector (63%) and retail (54%)

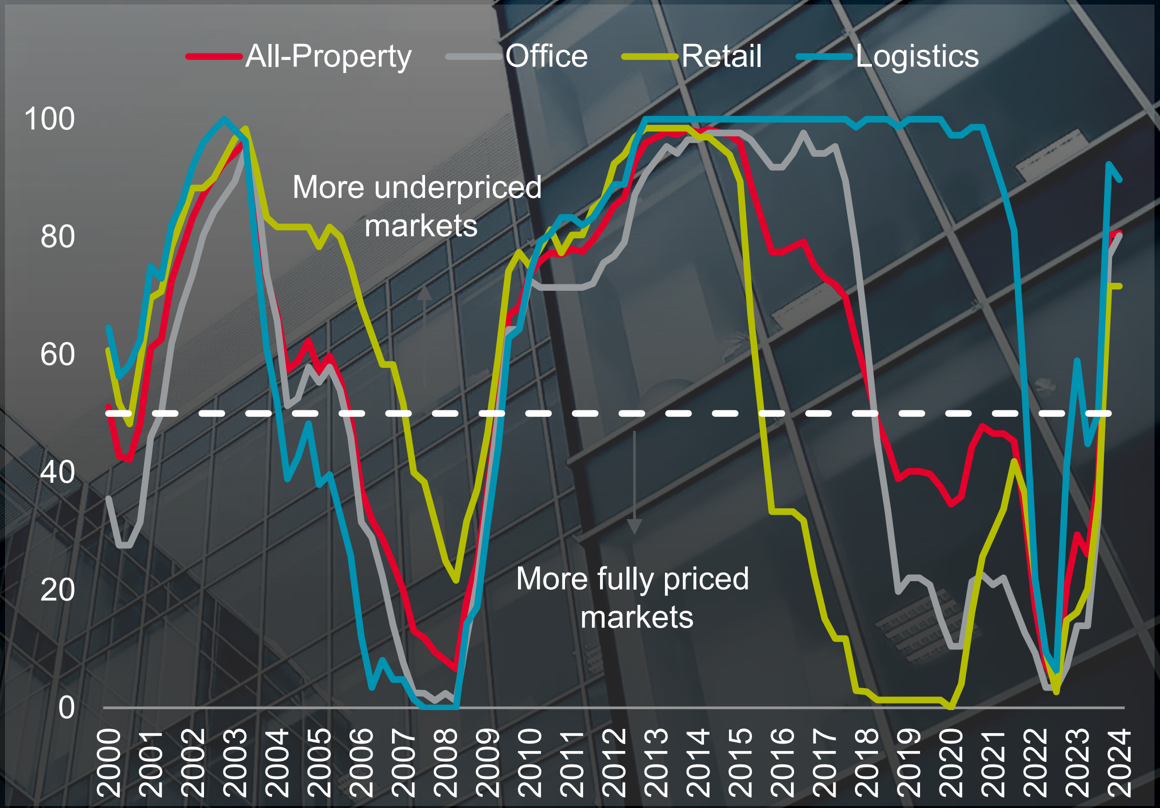
Notable improvements across most markets recorded within the Fair Value Index have been facilitated by a combination of improved total returns, fall in 5-year bond yields, and lowered credit spreads, thereby lower risk premium.

Rental growth has surprised on upside. Despite the decline in property values, robust market fundamentals have maintained upward pressure on prime rents across the three primary sectors.

The fluctuations in 5-year bond yields are influenced by various key factors, notably the recent decrease in inflation expectations has led to a corresponding decline in bond yields.

The increase in the Fair value index was largely anticipated, considering the further pricing adjustments over the past six months in a stable interest rate and bond market environment. Consequently, the current buying conditions are much more favourable than they were six months ago.

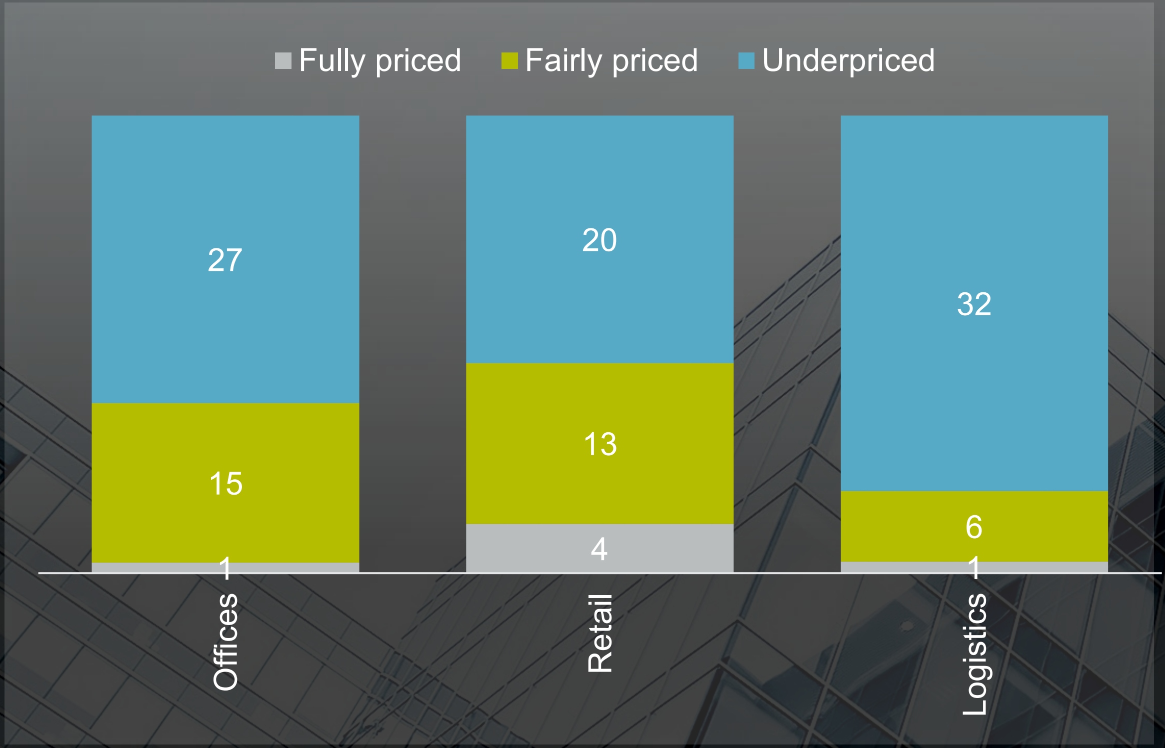
European Fair Value Index



Source: Cushman & Wakefield Research

FAIR VALUE INDEX RESULTS

THE LOGISTICS SECTOR IS STILL THE MOST ATTRACTIVE, FOLLOWED BY OFFICES, WITH MORE OPPORTUNITIES.



Source: Cushman & Wakefield Research

5 TOP MOVERS

- Vienna Offices
- Milan Retail
- Rome Retail
- Copenhagen Offices
- Munich Offices

5 UNDER-PRICED MARKETS

- Milan Retail
- London City Offices
- Munich Offices
- Gothenburg Logistics
- Stockholm Logistics

GEOGRAPHICALLY, MARKET CLASSIFICATIONS POINTS TO THE MORE LIQUID MARKETS, UK, GERMANY AND FRANCE WITNESSING A GREATER SHARE OF ‘UNDERPRICED’ AND ‘FAIRLY PRICED’ MARKETS. THIS IS NOT SURPRISING GIVEN THE RAPID OUTWARD ADJUSTMENT IN YIELDS THAT HAVE OCCURRED IN THESE MARKETS.

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