Q4 2017: Global Commercial Property Monitor

Real estate sentiment remains generally upbeat

- European markets continue to lead the way despite prospect of a shift in monetary policy
- Accelerating global economy helps strengthen outlook for property in emerging markets
- Valuations appear elevated in a number of markets but results appear consistent with a soft landing

The Q4 2017 RICS Global Commercial Property Monitor suggests that sentiment remains generally upbeat across the majority of real estate markets covered by the survey. The positive mood music is also reflected in the forward looking indicators, most visibly in the readings for expectations twelve months out. Concern around valuations does persist in a number of markets but even where this is the case, there is little sense from respondents of a material correction in pricing anytime soon.

The headline numbers from the survey are striking; the Occupier Sentiment Index* (OSI) is in positive territory, to a greater or lesser degree, in 28 out of the 34 countries reported on (chart 1) while the comparable figure for the Investment Sentiment Index* (ISI) is 27. Momentum for both indices remains strongest in Europe with well established markets such as Berlin, Amsterdam, Frankfurt and Madrid continuing to be most attractive to investors and tenants alike. However, medium term indicators point to some rotation towards smaller CEE markets with cities such as Sofia, Budapest and Prague also producing firm results. One feature that is consistently highlighted by contributors to the survey from European cities is a lack of supply of good quality property with vacancy rates in the office sector, for example, now at their lowest level since 2008. This is proving important in underpinning the current pricing environment in the more expensive markets; it may also partly explain the relatively sanguine assessment of the prospects in the face of the likely shift in the direction of monetary policy from the ECB as the year develops.

The contrast to the robust picture across much of Europe continues to be more the challenging environment for real estate in parts of the Middle East which is, amongst other factors, a function of the somewhat more chequered macro picture in the region. Significantly, the feedback we have received for Dubai in Q4 remains pretty cautious and that is regarding both the investment and occupier side of the market. Even so, the actual performance of property in the Emirate has been hitherto rather more resilient than its regional peers as a result of the more diversified nature of the economy.

More generally, the increasingly positive growth picture in many emerging markets helped by the upswing in global trade volumes is clearly visible in the outlook for real estate in these countries. The results for India, China and Brazil are all a little stronger in the latest survey compared with Q3 with cities such as Bengaluru, NCR, Mumbai, Beijing and Shanghai scoring particularly highly in the forward looking indicators. The majority of respondents in the first four of these cities continue to view real estate as, broadly speaking, still close to fair value although in the latter, the market is not surprisingly viewed as being expensive.

The London market remains attractive to investors even though it continues to be seen as being expensive on most valuation metrics; indeed, something in the region of two-thirds of respondents to the survey take this view. Nevertheless, the broader set of results do suggest that despite this, investors are increasingly optimistic that the market can sustain these somewhat elevated levels. This is also evident in the continuing appetite from overseas buyers.

Meanwhile, the US results show a marked contrast between the feedback from New York and the rest of the country. Both the OSI and the ISI remain in positive territory for the latter while for the former, they are in negative territory. To be clear the results for New York are only consistent with very modest declines in rents and broadly flat capital values over the course of 2018 but the caution partly reflects the fact that around four-fifths of respondents view the market as expensive and two-thirds see it as being in the early stage of a downturn.

The picture across Asia-Pac seems more solid than previously was the case. Singapore, in particular, appears to be benefiting from the pick-up in world trade and this is visible in the survey both through broadly flat Q4 readings for the OSI and ISI and, more significantly, the first positive reading in twelve month capital value expectations since Q2 2015. The office sector, most notably, seems to be benefiting from the shift in the mood music with foreign interest gathering steam and the rental environment providing greater support for pricing. The results for Hong Kong remain solid with the office sector again proving the most resilient part of the market. Elsewhere, the feedback from Auckland, Sydney and Melbourne tells a broadly similar story with contributors generally sanguine about the outlook despite roughly three-quarters of them viewing their respective markets as being in the peak phase of the cycle.

Finally, despite reports suggesting that the UK's decision to leave the EU is likely to result in the loss of fewer jobs in the former than some earlier estimates indicated, respondents to the survey working in a number of European cities continue to suggest they are receiving enquiries from British businesses regarding the availability of space. This is particularly so in Amsterdam but also in Warsaw, Dublin, Paris and Frankfurt. Meanwhile, around one quarter of contributors from central London continue to report that they have been approached by companies looking to relocate at least part of their business overseas.

*The Occupier and Investment Sentiment Indices are both composite measures capturing overall market momentum, encompassing variables on supply, demand, and expectations

Chart 1 Occupier Sentiment Index (change v previous qtr) - Net balance %

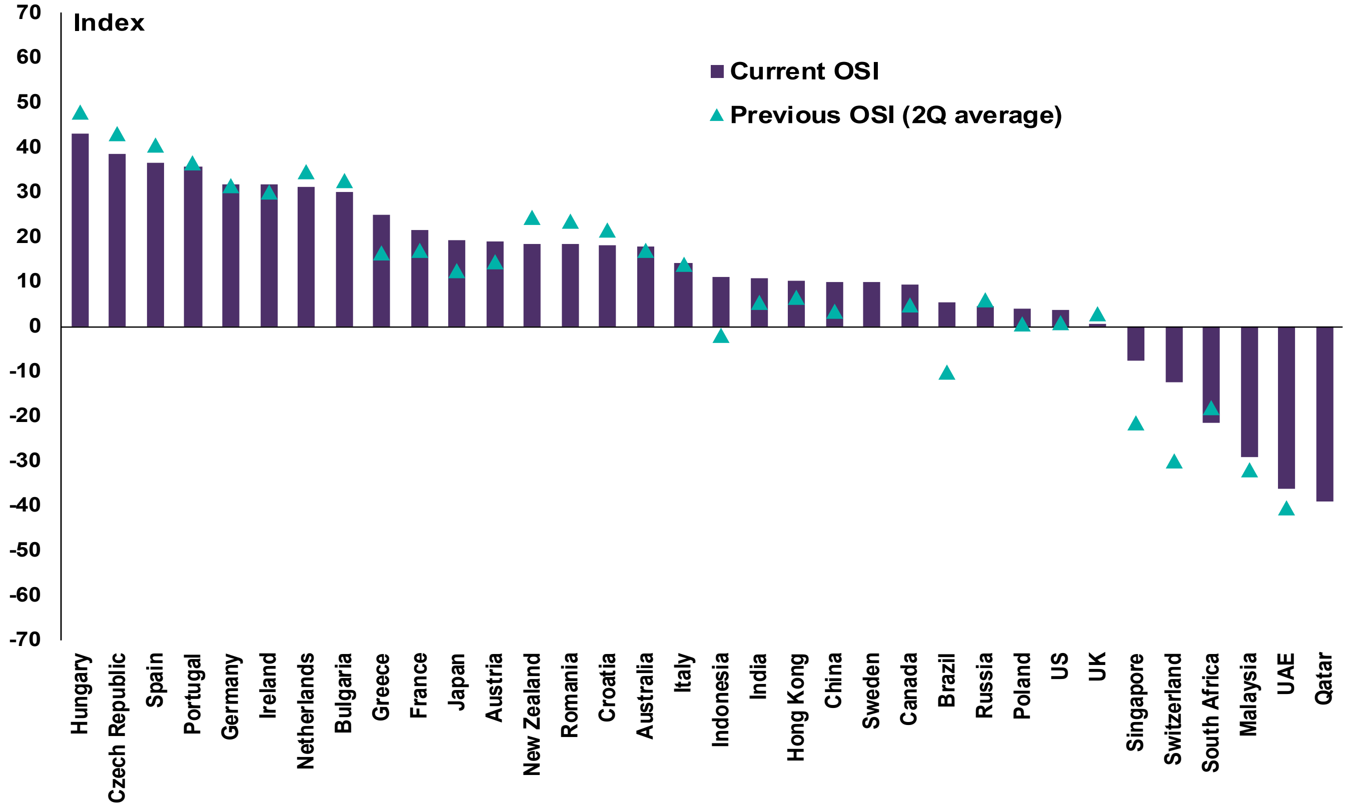


Chart 2 Investment Sentiment Index (change v previous qtr) - Net balance %

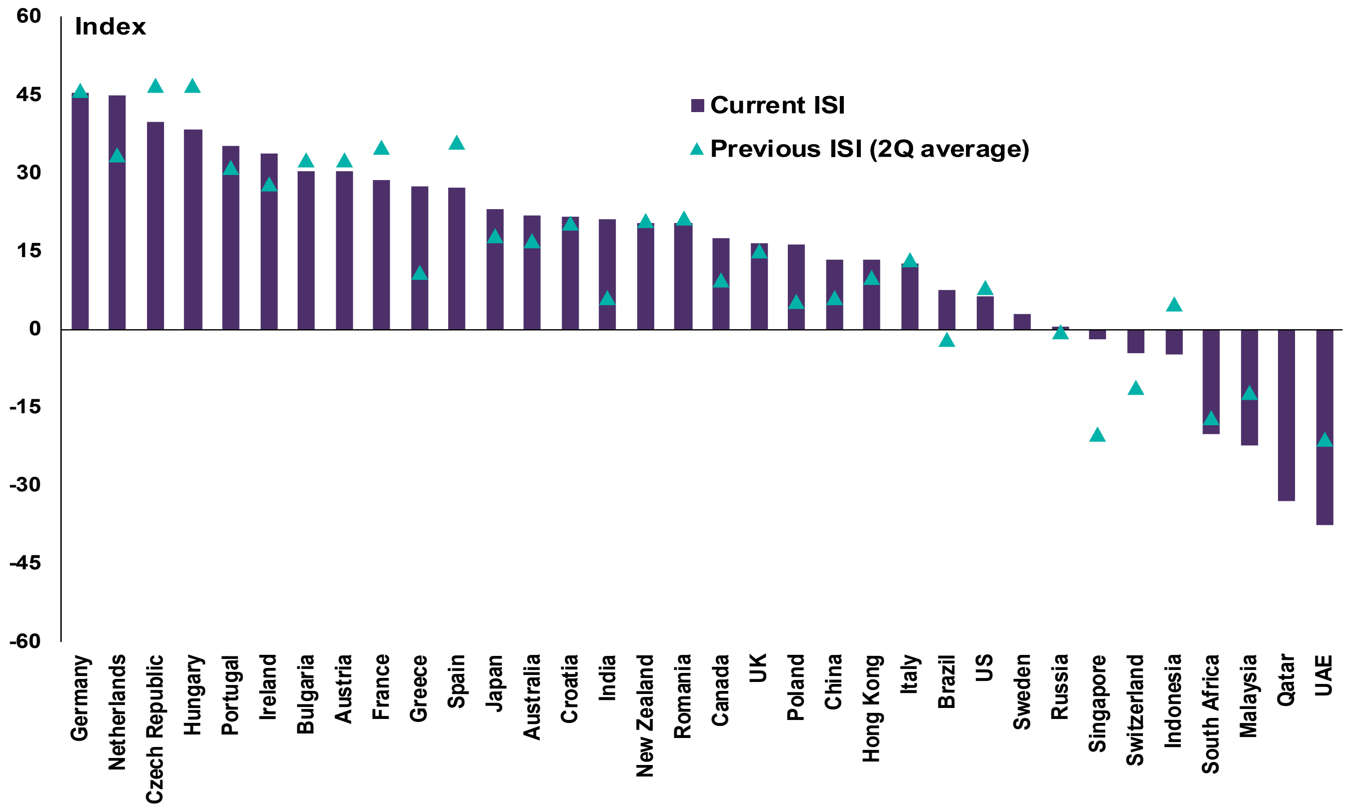


Chart 3 City Level Occupier and Investor Sentiment Indices- All sectors (net balance %)

Indicative of momentum over the previous quarter

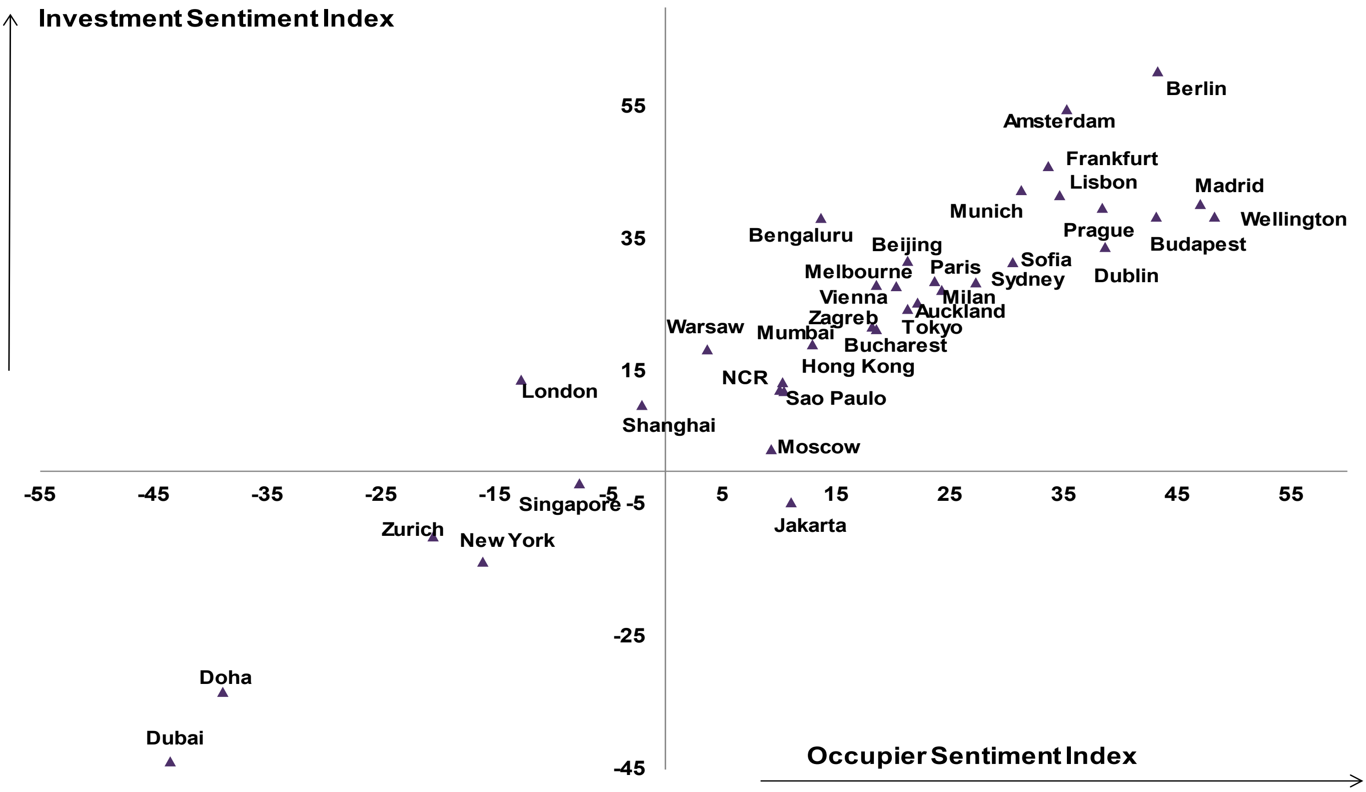


Chart 4 City Level Twelve Month Rental and Capital Value Expectations All sectors (net balance %)

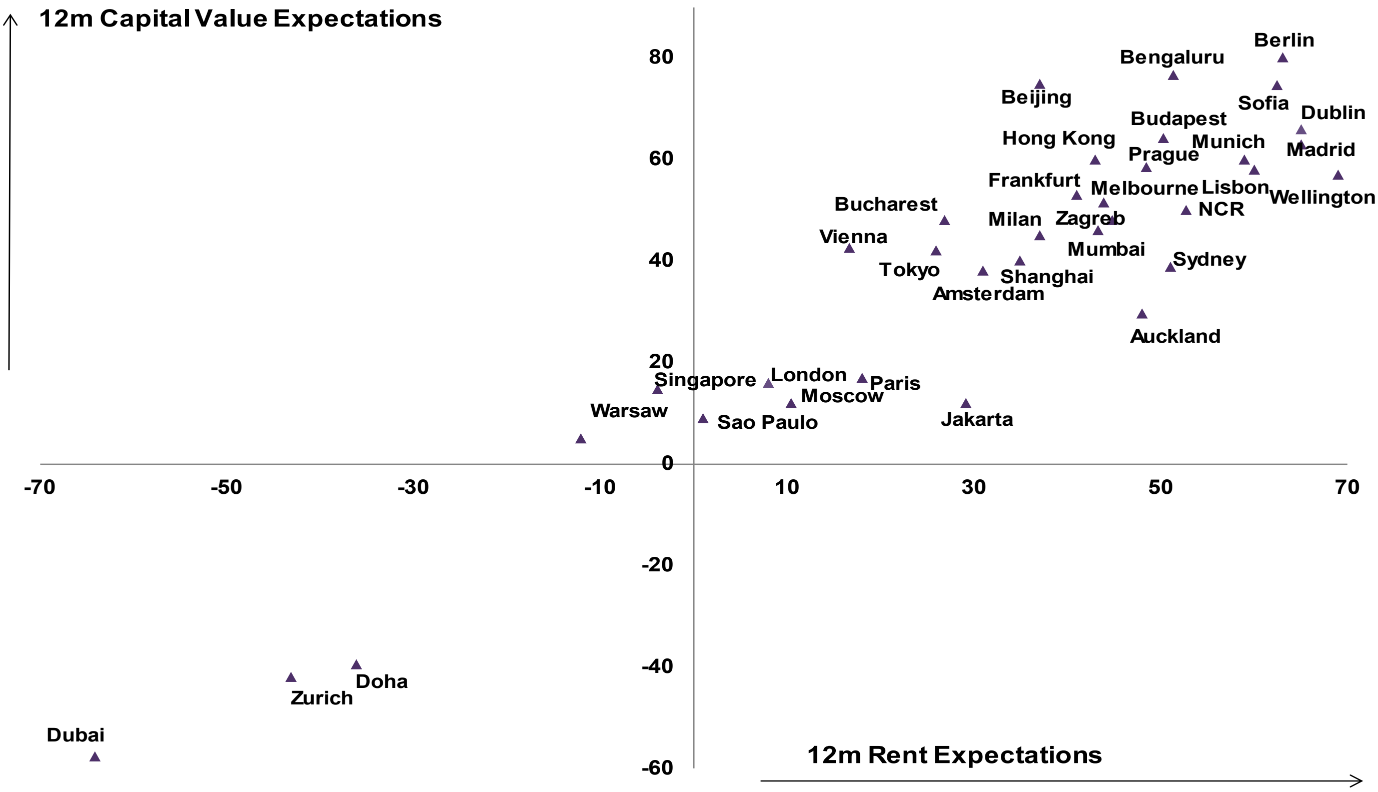


Chart 5 Valuations Perceptions

% of respondents viewing their local market as cheap, fair value or expensive

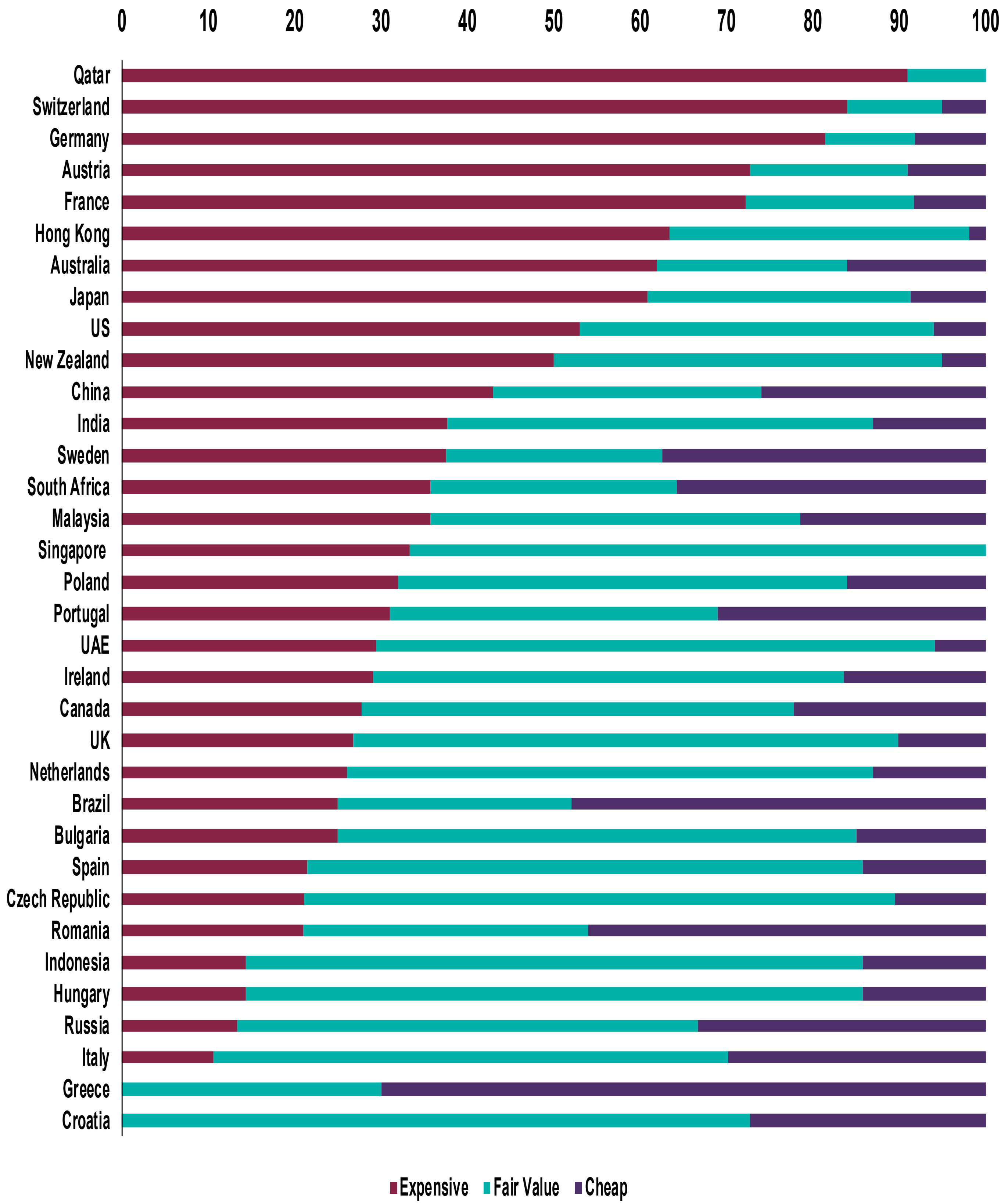
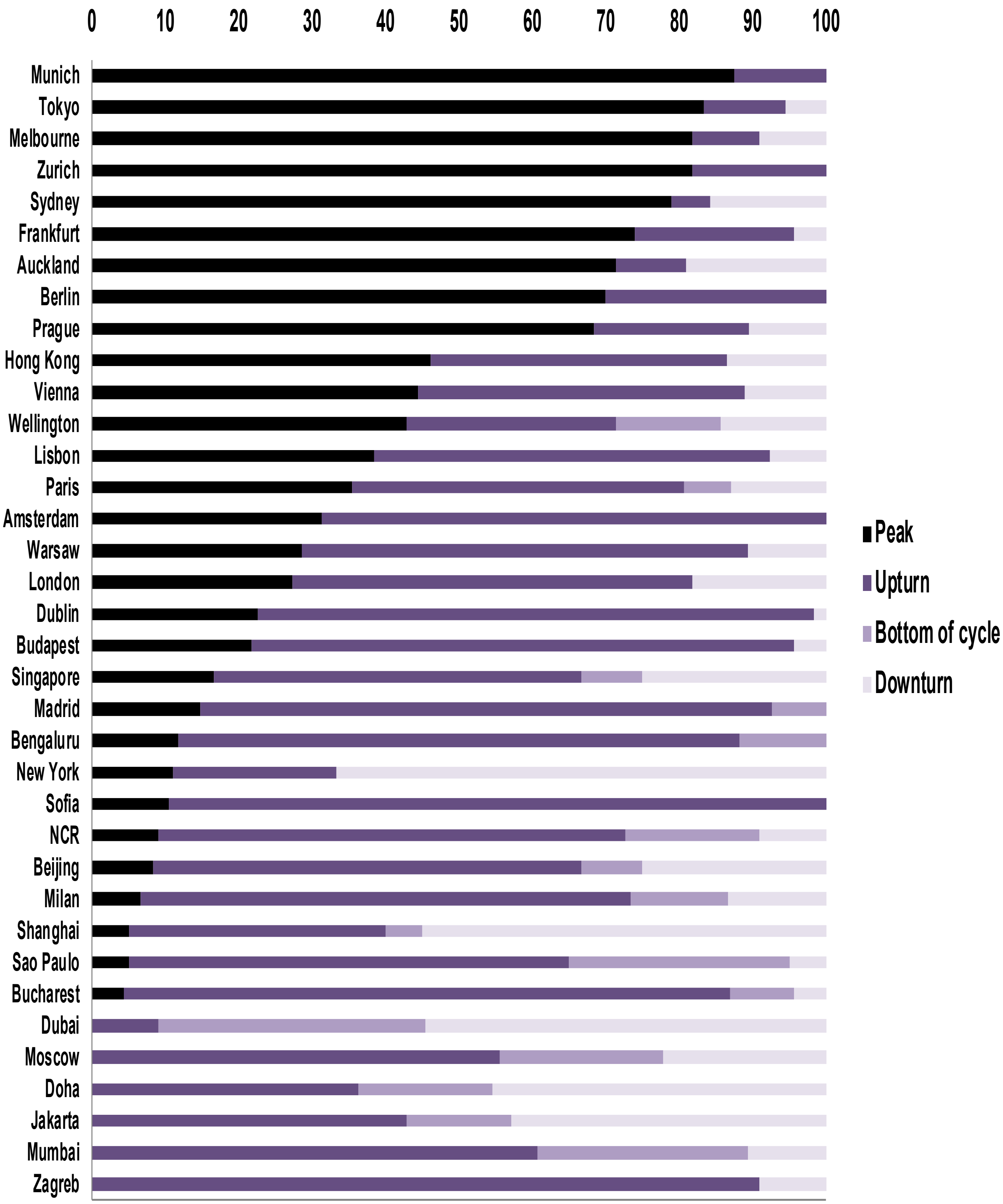


Chart 6 Property Cycle

% of respondents perceiving market conditions to be in various stages of the cycle



Information

Global Commercial Property Monitor

RICS' Global Commercial Property Monitor is a quarterly guide to the trends in the commercial property investment and occupier markets. The report is available from the RICS website www.rics.org/economics along with other surveys covering the housing market, residential lettings, commercial property, construction activity and the rural land market.

Methodology

Survey questionnaires were sent out on 13 December 2017 with responses received until 10 January 2018. Respondents were asked to compare conditions over the latest three months with the previous three months as well as their views as to the outlook. A total of 1612 company responses were received, with 434 from the UK. Responses for Ireland were collated in conjunction with the Society of Chartered Surveyors Ireland. Responses for Spain and Portugal were collated in conjunction with Iberian Property. Responses for New Zealand were collated in conjunction with Property Council New Zealand.

Responses have been amalgamated across the three real estate sub-sectors (offices, retail and industrial) at a country level, to form a net balance reading for the market as a whole.

Net balance = Proportion of respondents reporting a rise in a variable (e.g. occupier demand) minus those reporting a fall (if 30% reported a rise and 5% reported a fall, the net balance will be 25%). Net balance data can range from -100 to +100.

A positive net balance reading indicates an overall increase while a negative reading indicates an overall decline. The RICS Occupier Sentiment Index (OSI) is constructed by taking an unweighted average of readings for three series relating to the occupier market measured on a net balance basis; occupier demand, the level of inducements and rent expectations. The RICS Investment Sentiment Index (ISI) is constructed by taking an unweighted average of readings for three series relating to the investment market measured on a net balance basis; investment enquiries, capital value expectations and the supply of properties for sale.

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