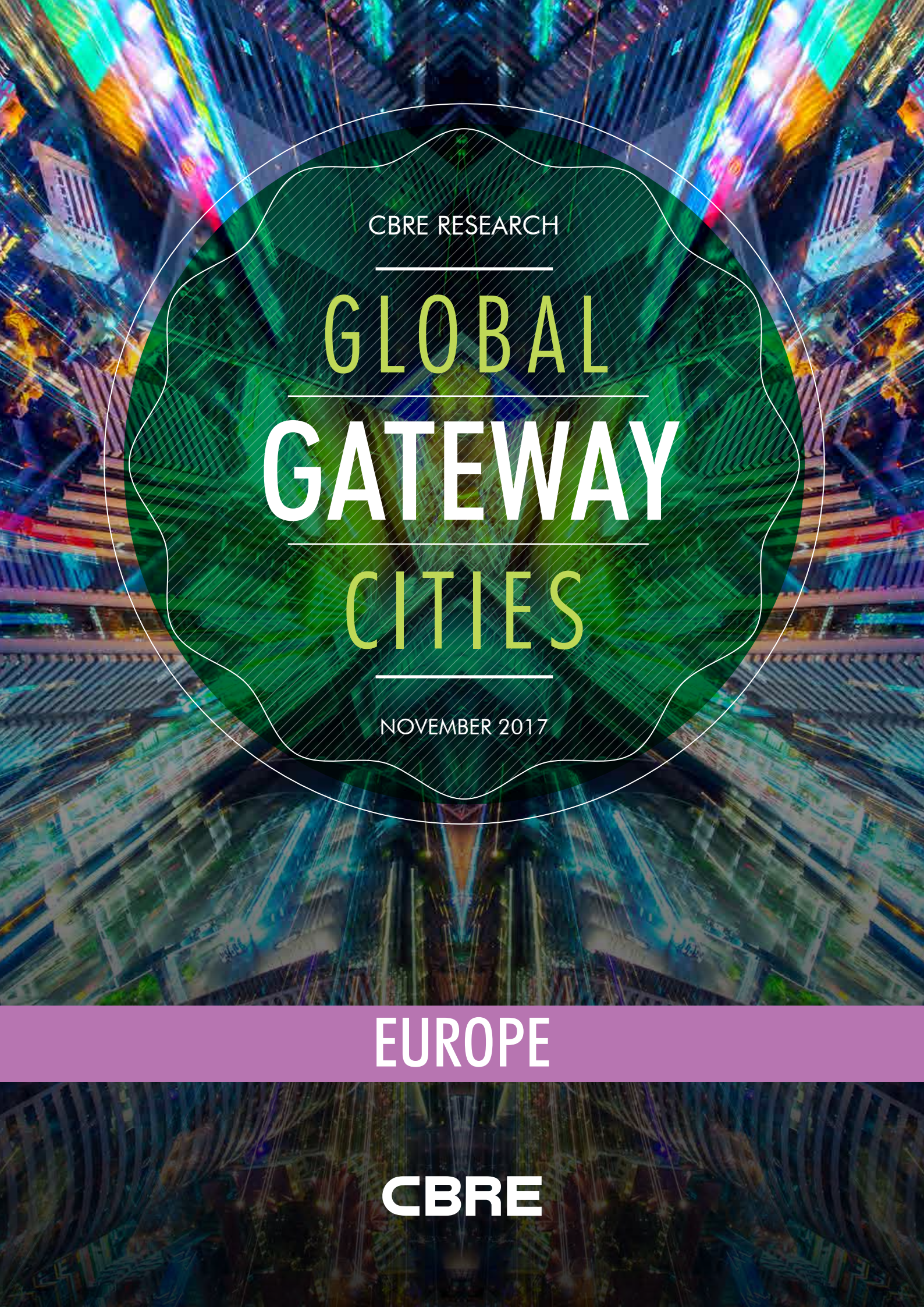

CBRE RESEARCH

GLOBAL GATEWAY CITIES

NOVEMBER 2017

EUROPE

CBRE

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INTRODUCTION

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We live in an age of cities. In emerging markets, they are hubs of explosive growth in production and distribution facilities. In the developed world, where the service sector drives economic activity, cities have reinvented themselves as vibrant live-work-play destinations. Millennials continue to flock to cities to work in the highly dynamic sectors of tech, fashion and high finance.

Nowhere is the spirit of the age better embodied than in the world's great gateway cities. These are, as the name suggests, world-class transport hubs. They are networked into the global economy via their ports and airports, and to their hinterlands via road and rail networks. They are large, important markets in their own right. They have highly diversified economies with many sectors and subsectors that, alongside their entrepreneurialism, make them highly resilient to the ebb and flow of economic events. London and New York took hits during the Great Recession, but they were not down for long.

The global gateway cities are centers of learning, culture, the arts, music and fashion. They have world-class retail facilities featuring major international brands, but also a wide selection of boutique and independent retailers. Their central business districts, with extensive stock of modern offices, host national and regional corporate headquarters and the legal, accountancy and consulting services these require.

From a real estate perspective, global gateway cities offer many benefits. First and foremost, their attractiveness to people and businesses means that space demand in their commercial real estate markets increases steadily over the long term, underpinning rent growth. They are also highly liquid markets, where real estate assets can be readily bought and sold. Some investors do trade regularly, playing the cycle, which they are able to do thanks to these markets' high transparency. With competitive markets for real estate advisory services, the advice is good and the cost of transacting is low. Other investors like to deploy capital over the long-term: Real estate in the global gateways provides good capital protection and, in this era of low bond rates, a good income return. Lot sizes vary from small to huge, so large sums of capital can be deployed if necessary.

We have compiled the third edition of this report so that those looking to invest in one or more of the world's great cities can quickly and easily understand pricing and market conditions using the most up-to-date information available. We look forward to your feedback, and, more importantly, to working with you to fulfil your chosen investment strategy.

Richard Barkham
Global Chief Economist

GLOBAL GATEWAY CITIES

Europe

	Office Rents (LCU)	Office Rents (US$)	Office Yields (%)	Retail Rents (LCU)	Retail Rents (US$)	Retail Yields (%)
AMSTERDAM	405 €/sq. m.	43	4.0	3,100 €/sq. m.	329	3.2
BERLIN	336 €/sq. m.	36	3.3	4,020 €/sq. m.	426	3.3
FRANKFURT	474 €/sq. m.	50	3.5	3,840 €/sq. m.	307	3.5
LONDON	105 £/sq. ft.	136	3.8	2,225 £/sq. ft.	1,821	2.3
MADRID	357 €/sq. m.	38	3.8	3,108 €/sq. m.	329	3.3
MILAN	530 €/sq. m.	56	3.5	6,000 €/sq. m.	636	3.2
MUNICH	414 €/sq. m.	44	3.0	4,800 €/sq. m.	509	2.9
PARIS	810 €/sq. m.	86	3.0	21,000 €/sq. m.	1,402	2.9
STOCKHOLM	6,500 SEK/sq. m.	72	3.5	21,000 SEK/sq. m.	231	3.8

Office Retail

Source: CBRE Research, 2017.

Notes: Local currency unit (LCU) rents are denoted in LCU per annum. Rents in U.S. dollar are as of Q2 2017 market rates (please see the conversion rates in the methodology section). All Office rents are denoted as Prime/Class A building rents for the best location in a given market. All Retail rents are based on the achievable rent which an international retailer is willing to pay for an up-to 200 square meter gross retail unit in the best location of a given market (according to CBRE's Global Prime Retail Rent publication). For global comparison we incorporate an ITZA conversion for London and Paris retail.

CBRE

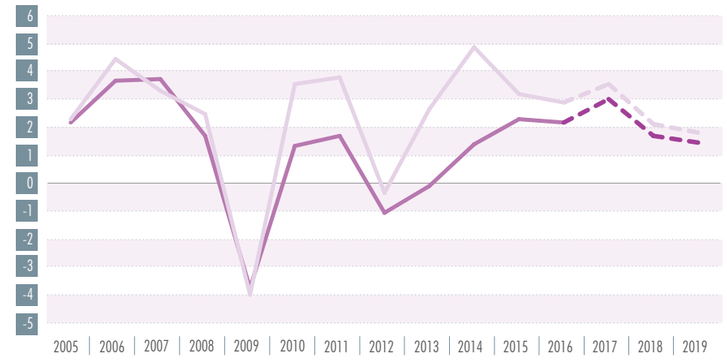
AMSTERDAM

Significant investor interest in prime properties in Amsterdam bringing greater attention to secondary assets.

ECONOMIC TRENDS

The Netherlands is one of Western Europe's fastest growing economies and its outlook for the remainder of 2017 is robust. Unemployment is on a downward trajectory, supporting leasing activity in property markets. Amsterdam is the Netherlands' center of business activity and forms a core part of the Randstad conurbation—one of the strongest economic regions in Europe. The city boasts a growing young workforce and a multilingual population.

Real GDP Growth (%)

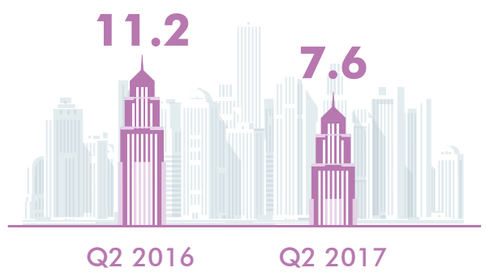


Source: Oxford Economics, CBRE Research 2017.

OCCUPIER TRENDS

Amsterdam's office market is performing well. The city has posted three consecutive years of take-up growth, in 2014-2016. Leasing activity has continued this trend in 2017, with take-up having increased versus H1 2016. Although Amsterdam is traditionally an anchor for financial and business services, technology is currently the fastest-growing sector. Tech firms are attracted by a pool of highly educated young talent and rents are favorable compared to Amsterdam's counterparts across Europe. Amsterdam accommodates several regional headquarters for large international tech firms like Booking.com, Netflix and Uber.

Office Vacancy (%)



Source: CBRE Research, Q2 2017.

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SUPPLY TRENDS

In a European context, Amsterdam's office development pipeline is very limited, as regulations were implemented by the local government during the financial crisis in response to oversupply. In 2016, less than 50,000 sq. m. of office space came online and the current development pipeline through 2019 consists of less than 3% of the current office stock. With the upturn in leasing activity and rapidly declining vacancy, market conditions in Amsterdam are tightening rapidly.

0.03 MSM
New Office Completions

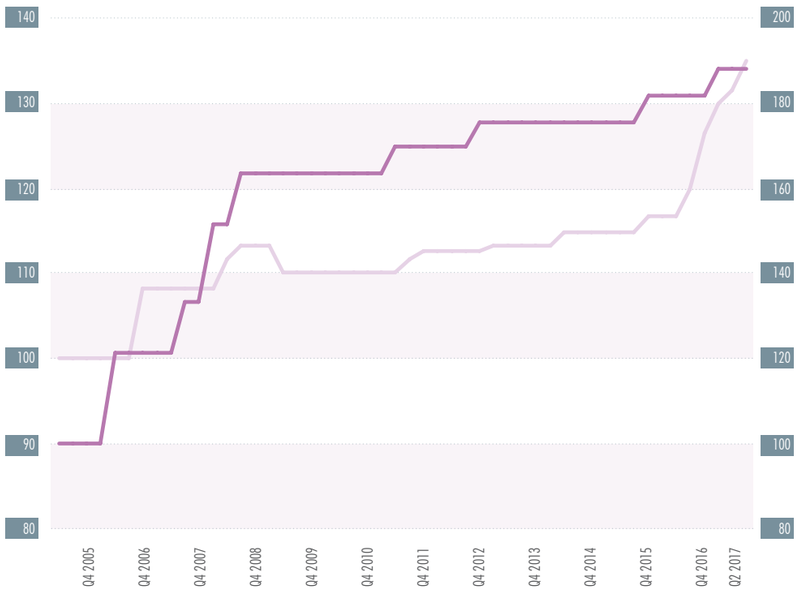
0.1 MSM
Office Space Under Construction

Source: CBRE Research, Q2 2017.

RENT TRENDS

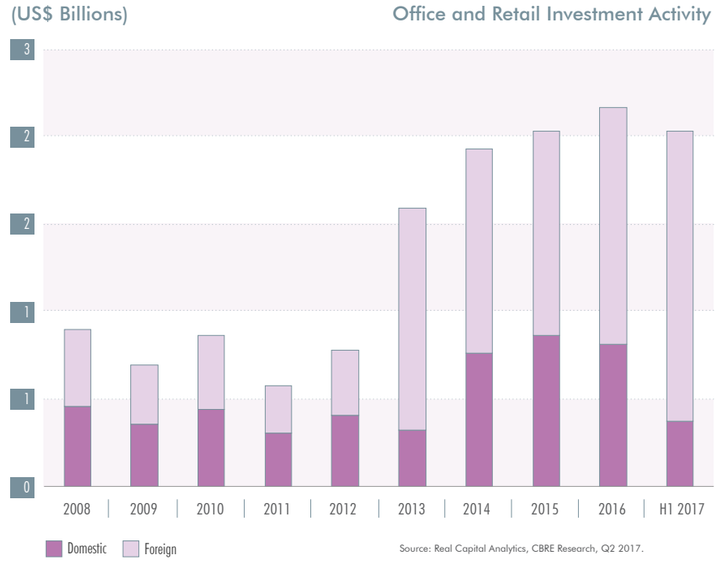
The tightening office market is pressuring rents upward. Prime rents have increased by 13% over the past twelve months. While rental growth was initially confined to core submarkets, it is now spread more broadly across the city due to increasing scarcity and spill-over effects. For retail, rental growth is more muted, although prime high street retail continues to perform well.

Office and Retail Rent Trends



INVESTMENT ACTIVITY

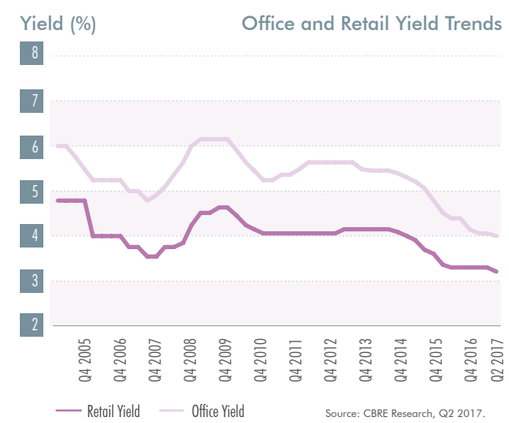
Amsterdam witnessed strong investor demand over the past twelve months; investment volume increased to more than €5 billion (US$5.7 billion) —growing 57%, year-over-year. Trading volume is traditionally dominated by office, hotel and residential. Appetite for high street retail is generally strong, although this product is more fragmented than the other asset classes.



Source: Real Capital Analytics, CBRE Research, Q2 2017.

YIELD TRENDS

In the prime segment, yields have moved below pre-crisis levels. However, across all asset classes the gap between prime and secondary remains substantial and above its 15-year average. While strong competition for prime product could further lower yields, room for significant yield compression is limited in this segment. Driven by improving occupier fundamentals, investors are increasingly drawn to secondary segments of the market.



Source: CBRE Research, Q2 2017.

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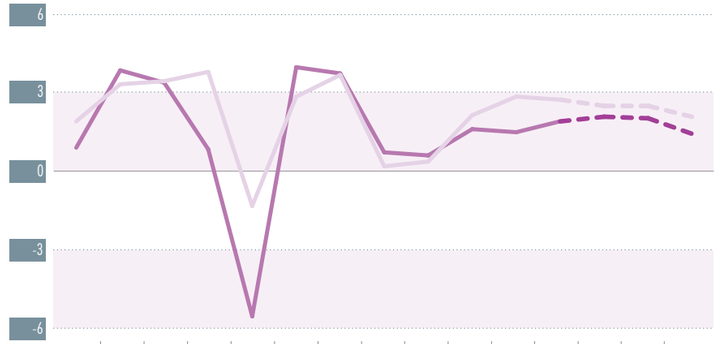
BERLIN

A record year for investment is expected, due in part to a series of large-scale transactions. Strong take-up activity is forecast to drive further rental growth.

ECONOMIC TRENDS

The outlook for Germany's economy in the coming year remains favorable; robust GDP growth during the first two quarters laid a strong foundation for the remainder of the year. With the interest rate policy of the ECB likely to change over the next year given growing inflation, foreign policy issues are likely to determine future growth prospects. Private consumer spending is likely to continue to be another key driver, supported by currently low interest rates and tight labor market conditions. With a growth rate of 2.7%, Berlin's GDP growth was clearly above the German average in 2016, but that gap is expected to narrow slightly. A 70-bps year-over-year decline in city's unemployment rate reflects the continuing improvement in its economy.

Real GDP Growth (%)

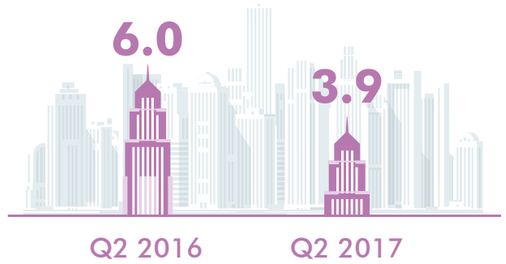


Source: Oxford Economics, CBRE Research 2017.

OCCUPIER TRENDS

Berlin's H1 2017 take-up was 403,700 sq. m. Around half occurred in the inner-city submarkets City-East (30%) and City-West (20%), with the largest transactions taking place in Mediaspree. Berlin being Germany's start-up capital, its technology, media and telecommunications (TMT) sector claimed 40% of take-up, increasing the total space it occupies by 22% versus a year earlier. The public sector accounted for 17% of take-up. Given the tight supply conditions in Berlin's office market, co-working spaces and business centers played an important part in total take-up, providing an alternative for start-ups and creative industries. Over the past year, vacancy has declined by 35% to 692,400 sq. m., or 3.9%.

Office Vacancy (%)



Source: CBRE Research, Q2 2017.

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SUPPLY TRENDS

The high levels of office take-up contrast with a low level of office completions. A total of 140,000 sq. m. of new-build or refurbished space was completed during H1 2017—12% less than in the previous year. Only 26% of it was speculative. Of the 524,100 sq. m. of office space expected to be completed by the end of 2018, 71% is already pre-let. For deliveries anticipated in 2019, the pre-let rate is currently 50%. New supply is therefore not expected to ease markets considerably until at least 2019.

0.1 MSM
New Office Completions

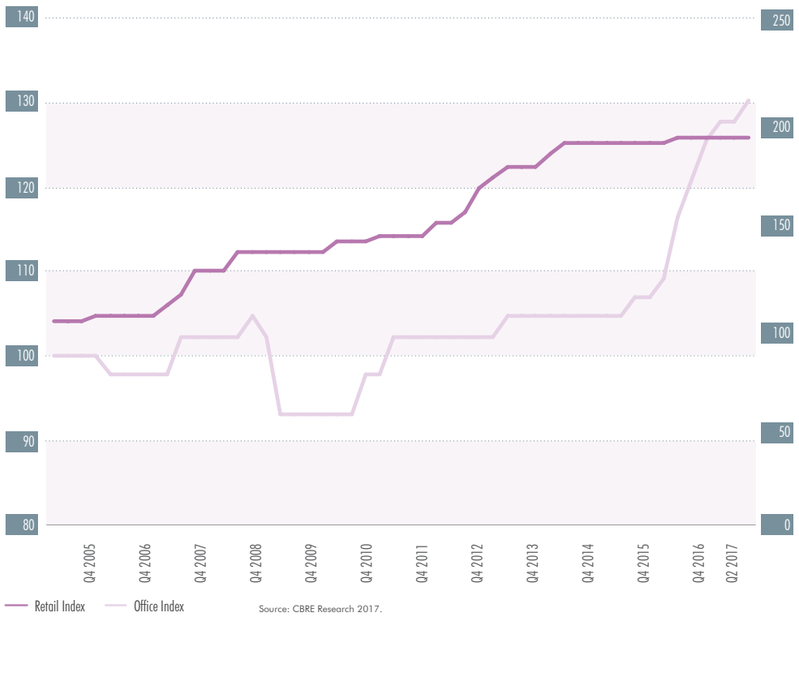
0.1 MSM
Office Space Under Construction

Source: CBRE Research, Q2 2017.

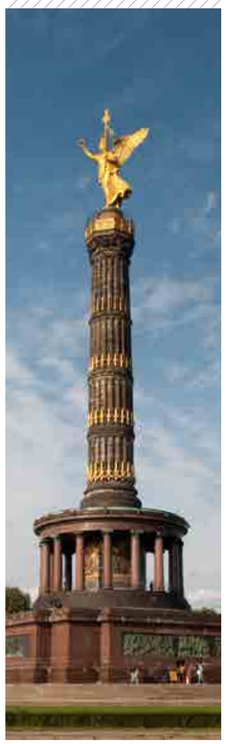
RENT TRENDS

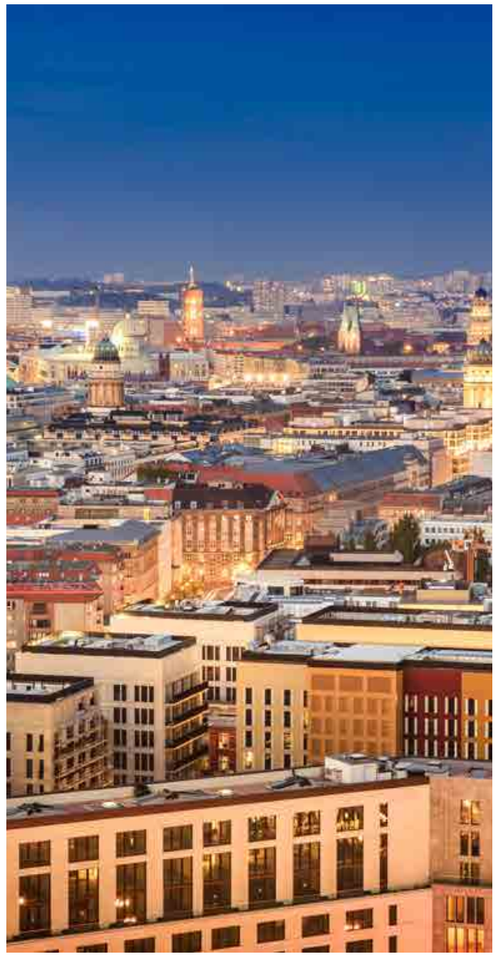
The shortage of space combined with high demand pushed up rents by €0.50 from Q1 2017 to €28.00 /sq. m./month in Q2 2017: 8% growth year-on-year. The strongest rental growth year-on-year was in City-West, where year-on-year growth reached 26%. This growth was due to the completion of the office tower Upper West, which set a new rental tone for the area. High street prime retail rents have been shaped in particular by the dynamic development of the sub-market City-West. Here, rents have grown from €250/sq. m./month in 2011 up to €335/sq. m./month in 2016. The prime retail rent for first-class high street properties remained stable at €335/sq. m./month in Q2 2017.

Office and Retail Rent Trends



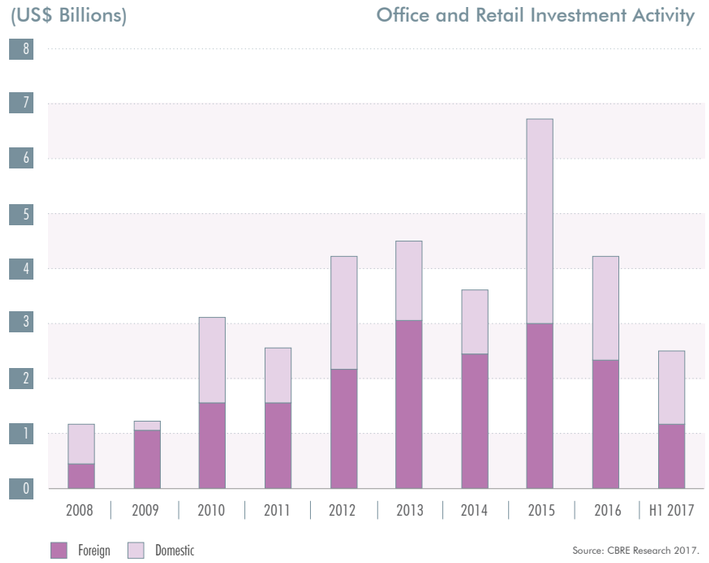
Source: CBRE Research 2017.





INVESTMENT ACTIVITY

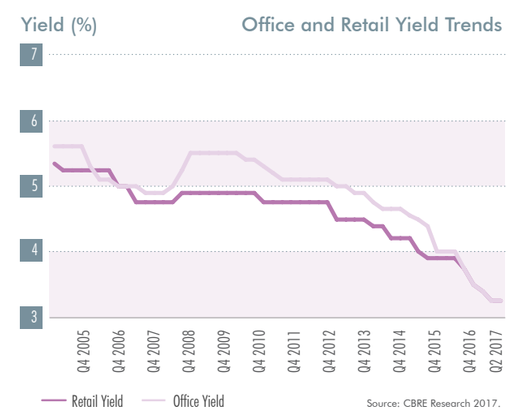
H1 2017 saw Berlin's commercial investment market record its best half-year results since records began. Transaction volumes totaled €2.86 billion (US$3.25 billion) – a year-over-year increase of 36%. Office property attracted the greatest share (by far—72%), followed by retail (12%) and hotels (11%). Most transactions were single asset deals, and only 15% were transacted as part of a portfolio. More than half (55%) of the buyers came from abroad, as Berlin continued to cement its position as a leading global tech center. By mid-2017, Berlin's investment market has already seen transactions exceeding €100m than occurred in all of 2016, and many were large lot-sizes. These large-volume transactions will continue in the second half of 2017 with at least three mega-transactions expected.



Source: CBRE Research 2017.

YIELD TRENDS

Prime office and retail yields remained stable at 3.25%, though their year-over-year change was a decline of 50 bps. For non-CBD assets, office yields declined by a slightly lower 45 bps, to 3.75%, while peripheral locations saw yields fall by 30 bps to 5.6%, both reflecting investor interest in centrally-located, core assets. Further yield compression is expected during the remainder of 2017, but yields are anticipated to stabilize in the following period.



Source: CBRE Research 2017.

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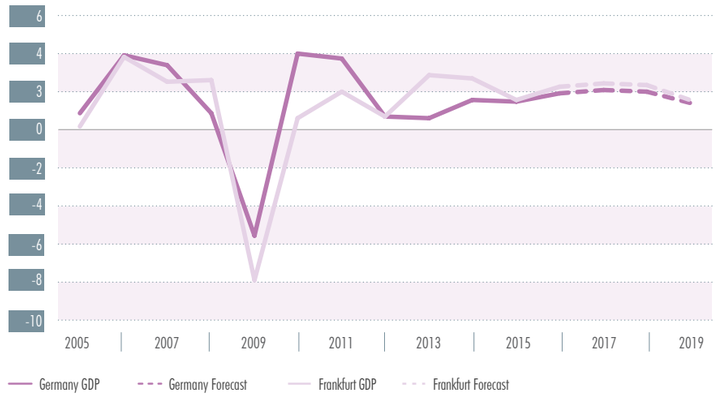
FRANKFURT

Exceptional investor interest has driven general yield compression. Although core and core-plus properties were the principal focus, a lack of supply in those segments has forced investors to shift interest to the value-add segment and peripheral locations.

ECONOMIC TRENDS

The outlook for Germany's economy in the coming year remains favorable; robust GDP growth during the first two quarters laid a strong foundation for the remainder of the year. With the interest rate policy of the ECB likely to change over the next year given growing inflation, foreign policy issues are likely to determine future growth prospects. Private consumer spending is likely to continue to be another key driver, supported by currently low interest rates and tight labor market conditions. Frankfurt's 2016 GDP growth of 2.3% was above the German average; this differential is expected to continue to 2019.

Real GDP Growth (%)

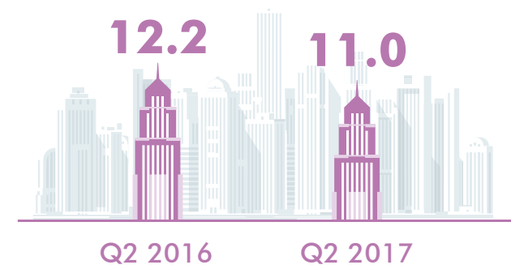


Source: Oxford Economics, CBRE Research 2017.

OCCUPIER TRENDS

Total take-up in Frankfurt's CBD—including the Banking District, Westend and Frankfurt City submarkets—was 95,900 sq. m. in H1 2017, or nearly 44% of total take-up in Frankfurt. The largest deal during the period was the letting to Clifford Chance of 11,700 sq. m. in the Junghof Plaza in the Banking District. Spaces under 2,500 sq. m. accounted for around half of the take-up, suggesting the letting market is still characterized by a well-balanced mix of size categories. Consultancies were the most active occupiers, accounting for 14% of total take-up, followed by the IT sector (11%), and banking and finance (9%).

Office Vacancy (%)



Source: CBRE Research, Q2 2017.

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SUPPLY TRENDS

Due to the robust office letting market and the constrained completion pipeline, it is likely that there will be a growing shortfall of top-grade centrally located office space. Frankfurt's current pipeline amounts to 85,000 sq. m. through the end of 2017. Of this, only 23,700 sq. m. remains available to let. Furthermore, the supply of refurbished and newly constructed office space is unlikely to increase significantly over the coming year. Only in the following year will the supply situation ease, with 141,000 sq. m. scheduled for completion in 2019; however, this is still well below the 10-year annual average of 181,000 sq. m. Vacancy in existing high-quality properties will continue to fall, limiting letting activity and reducing the probability of large-scale lettings. Three major development projects (Four, One and Global Tower, totaling around 164,000 sq. m. of office space) are due for completion around 2021, however, making the long-term outlook more promising.

0.1 MSM
New Office Completions

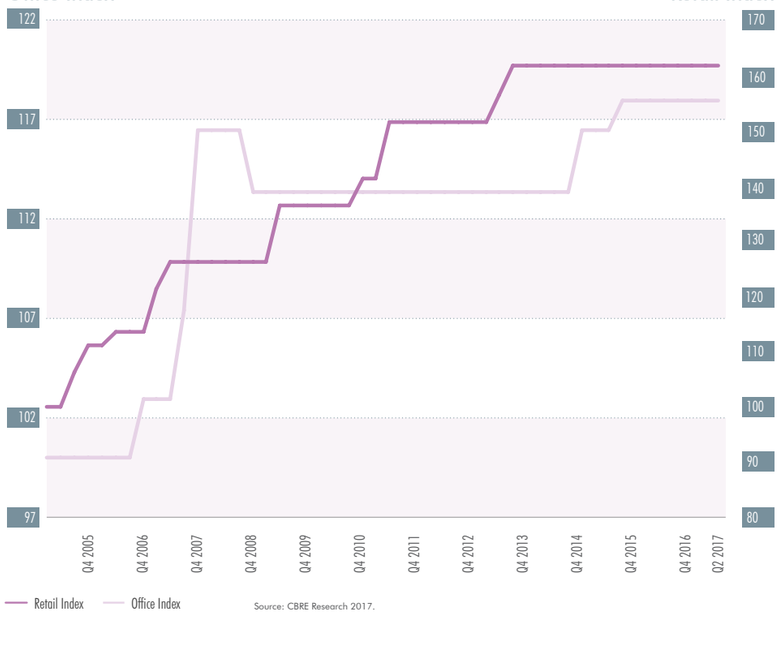
0.4 MSM
Office Space Under Construction

Source: CBRE Research, Q2 2017.

RENT TRENDS

Frankfurt's weighted average office rent was €19.10/sq. m./month at the end of Q2 2017, having risen 5%, year-over-year. The high levels of take-up in CBD submarkets have been the main contributor to the significant increase in weighted average rents. Although the prime rent again remained stable at €39.50/sq. m./month, an increase in the second half of 2017 is expected due to high demand. Prime retail rents in Frankfurt's top locations are at €320/sq. m./month but this level may become unsustainable given the growth of online retailing.

Office and Retail Rent Trends

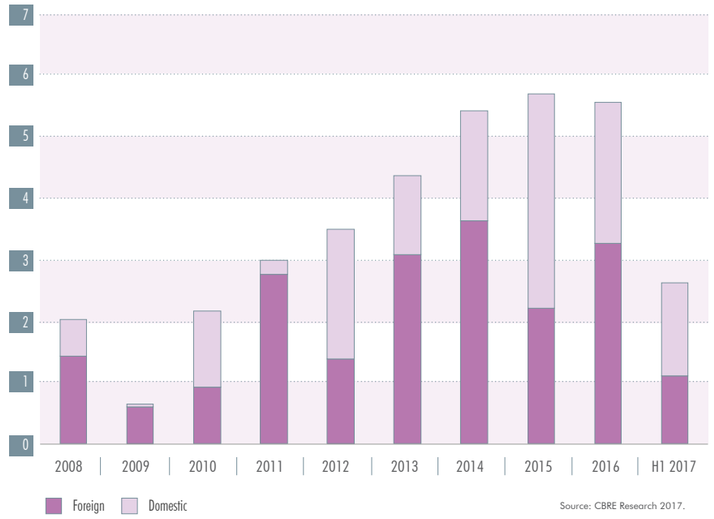


Source: CBRE Research 2017.

INVESTMENT ACTIVITY

Frankfurt's commercial property investment market had a remarkable half-year with a total transaction volume of €2.8 billion (US$3.2 billion), of which €2.0 billion (US$ 2.3) was registered in Q2 alone. This represents a rise of 73% over the year-earlier period. The most actively transacted asset class was office, accounting for 97% of transactions during H1. Large-scale transactions exceeding €100 million (US$113 million) totaled around €1.2 billion (US$1.4 billion)—a major proportion of the total volume. Since office properties are the dominating asset class in Frankfurt, the retail investment market does not show a strong figure for H1 2017.

(US$ Billions) Office and Retail Investment Activity

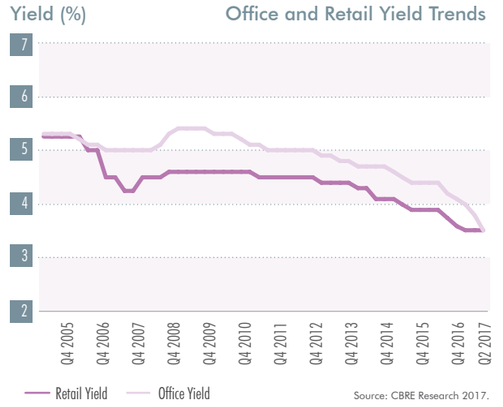


Source: CBRE Research 2017.

YIELD TRENDS

Strong investor activity during the second quarter led prime yields in the CBD to drop again—by 30 bps, quarter over quarter, to reach 3.5%. Although investors' focus remained on the core and core-plus segments of the market, short supply in those segments prompted greater interest in value-add and peripherally-located properties. Yields for city fringe and peripheral submarkets have consequently fallen by 20 bps, to their current levels of 4.2% and 5.5%, respectively. Prime retail yields remain under pressure due to the general high demand from investors, and reached 3.5% at the end of Q2 2017.

Yield (%) Office and Retail Yield Trends



Source: CBRE Research 2017.

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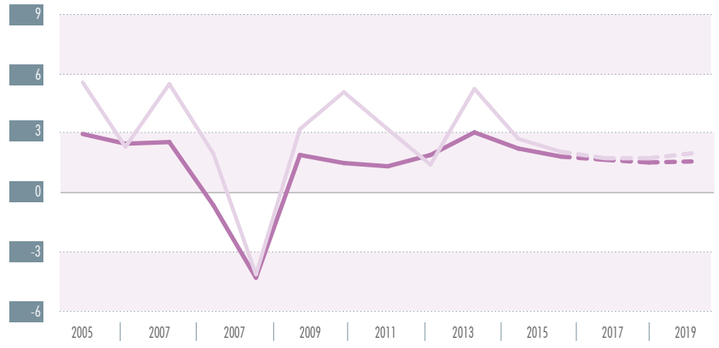
LONDON

London is the largest, most transparent and most liquid investment market in Europe. There are few barriers to new entrants and, historically, transactions in all lot sizes are available at most times. Despite certain specific political and economic risks, the fundamentals of the market remain well supported.

ECONOMIC TRENDS

A year after the EU referendum, the UK's economy has begun to slow and forecasts point to below-trend growth in the short term. Economic growth has been largely driven by consumers in recent years, but several factors are now curtailing household spending. One key concern is that average earnings have been growing less than inflation, despite unemployment posting its lowest rates since 1975 (4.5% in the three months to May). Indicators of UK consumer confidence show resilience, and tourist spending will be supportive (particularly in London); however, this resilience might end as consumer spending comes under pressure.

Real GDP Growth (%)

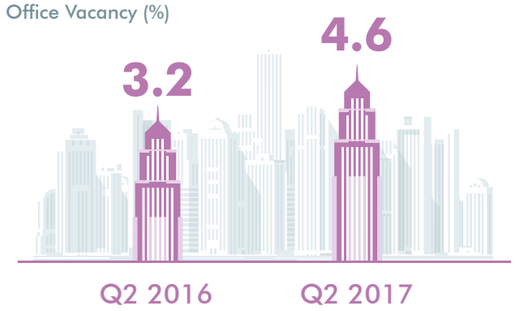


Source: Oxford Economics, CBRE Research 2017.

OCCUPIER TRENDS

Below-trend economic growth and a slowing pace of job creation are likely to curtail demand in the near term. However, demand will continue to be fed by lease events and space consolidation/M&A activity. Occupiers from creative industries (technology, media and telecom) and business services (especially providers of flexible space) will be the main sources of future office demand. Prime rental values are lower now than they were 12 months ago in nearly every London market and submarket. Further decline is expected to be relatively muted, however, with tenant-friendly lease terms expected to slow the pace of rental decline.

Office Vacancy (%)



Source: CBRE Research, Q2 2017.

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SUPPLY TRENDS

Central London's vacancy rate stood at 4.6% at the end of Q2, above the long-term average of 4.4%. This is likely to be mitigated by low levels of speculative development; of the 2.7 million sq. ft. of office space completed in H1 2017, 70% is already let or under offer. And 13.0 million sq. ft. is currently under construction in Central London, of which 47% is already taken. Looking ahead, the supply pipeline is uncertain as developers reassess the market in light of political uncertainty and construction cost inflation.

2.7 MSF
New Office Completions

13.0 MSF
Office Space Under Construction

Source: CBRE Research, Q2 2017.

RENT TRENDS

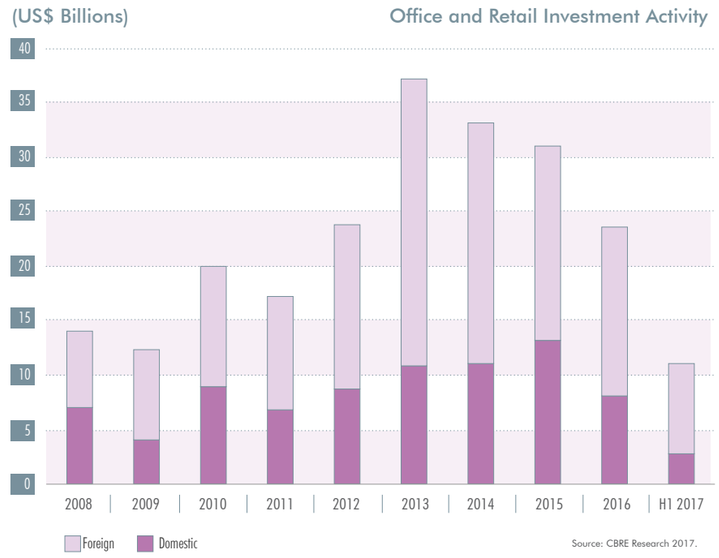
Rental growth has been relatively strong in recent years, having averaged 4.5% per annum in the City and 5.3% in the West End over 2011-2015. At the end of 2016, prime rents stood at £70.00 per sq. ft. in the City and £112.50 per sq. ft. in the West End. Prime rents in core West End are now £105 per sq. ft. and £69.50 per sq. ft. in the City. Rents are forecast to fall in all markets in the near term, although extended rent-free periods and greater flexibility in lease terms have the potential to moderate declines. By 2020 a gradual recovery in rents is expected in most markets. Prime retail rents are at an all-time high of £2,225 (ITZA) and are set to grow by an average of 1.7% over the next five years.

Office and Retail Rent Trends

Source: CBRE Research 2017.

INVESTMENT ACTIVITY

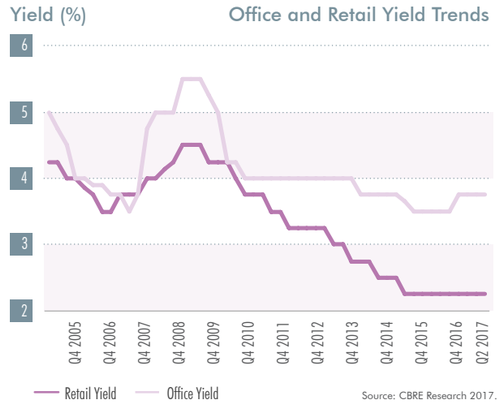
Office investment turnover in H1 2017 totaled £8.2 billion (US$10.6 billion), up by 13% from the same period last year. Once again, investment volumes were driven by large-lot deals. A total of 25 deals of £100 million (US$130 million) or more were completed in H1 2017. There were 19 deals during H1 2016. For a 15th consecutive quarter, overseas buyers accounted for the largest proportion of investment—71% of all transactions. Overseas' investor appetite for big-ticket assets was demonstrated by their involvement in the five largest transactions of the period. London retail transaction volumes for H1 2017 were down 50% on the five-year trend due to fewer large transactions than usual; only three retail properties above £50 million (US$65 million) have been sold this year.



Source: CBRE Research 2017.

YIELD TRENDS

Prime office yields have remained steady in the West End since Q3 2016, at 3.75%. In the City of London, yields tightened from 4.25% to 4.0% during Q1 2017 and then held there through Q2. Despite deep uncertainty in the market, pricing continues to be supported by the strong weight of capital flowing in from overseas investors. Prime retail yields for Bond Street remained at 2.25%, while Oxford Street registered 2.5%. The pricing resilience has been due to the limited supply of property at the prime end of the market.



Source: CBRE Research 2017.

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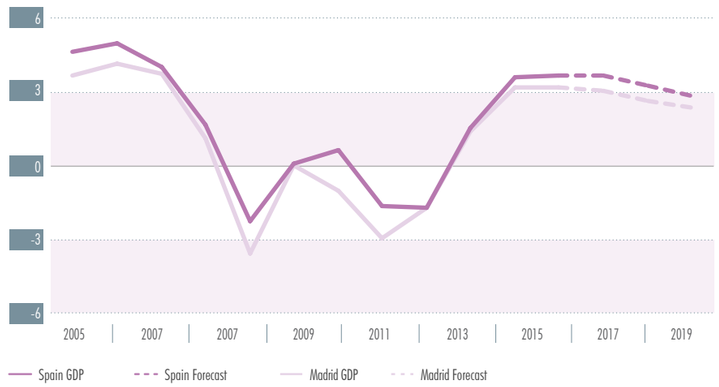
MADRID

Investor interest Madrid remains high, with prime office yields below historic minimum levels. After a decade of little or no speculative development, refurbishment and development activity has picked up, offering investors new opportunities.

ECONOMIC TRENDS

The Spanish economy is performing better than expected and is set to grow by 3.1% in 2017, roughly in line with 2016. Once again, Spain will be one of Europe's fastest-expanding economies, its recovery having gained momentum. Growth is being driven mainly by private consumption (which is expected to grow by 3.7% in 2017), sustained by the recovery of the job market. Although the 17.2% unemployment rate for Q2 2017 remains high, it represents a substantial year-over-year drop, and further decline—to 15%—is expected next year. Madrid is one of Spain's strongest growth areas, with 3.7% GDP growth forecast in 2017 and 3.3% in 2018. The region has experienced years of strong job creation and is growing as a tourist destination.

Real GDP Growth (%)

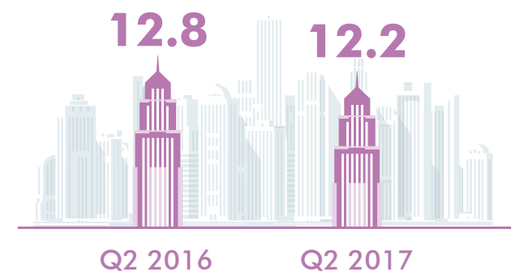


Source: Oxford Economics, CBRE Research 2017.

OCCUPIER TRENDS

Following the formation of a new government in October 2016, office leasing activity picked up; 2016's top three letting transactions were all signed in the final quarter of the year. 2017 is continuing this upbeat trend—in H1 2017, take-up was at its highest level since 2008. The CBD is accounting for the largest share, with 36% of all leased space. Tenants remain cost-conscious, but Grade A space with access to public transport and amenities—a combination not easily found outside the city center—is in high demand.

Office Vacancy (%)



Source: CBRE Research, Q2 2017.

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SUPPLY TRENDS

After years of subdued development, 2017 will see a significant volume of office space, largely in centrally-located refurbished buildings, coming onto the market. The new supply currently under construction is more peripherally located, along the A-1 highway to the North and the A-2 to the East. In the High Street market, several new projects are being marketed—such as the Canalejas scheme due for completion in 2019—but in the short term no space will be added to the stock. However, many prime high street units are being reconfigured to meet the demand of large flagship stores, resulting in a consolidation of existing units.

0.1 MSM
New Office Completions

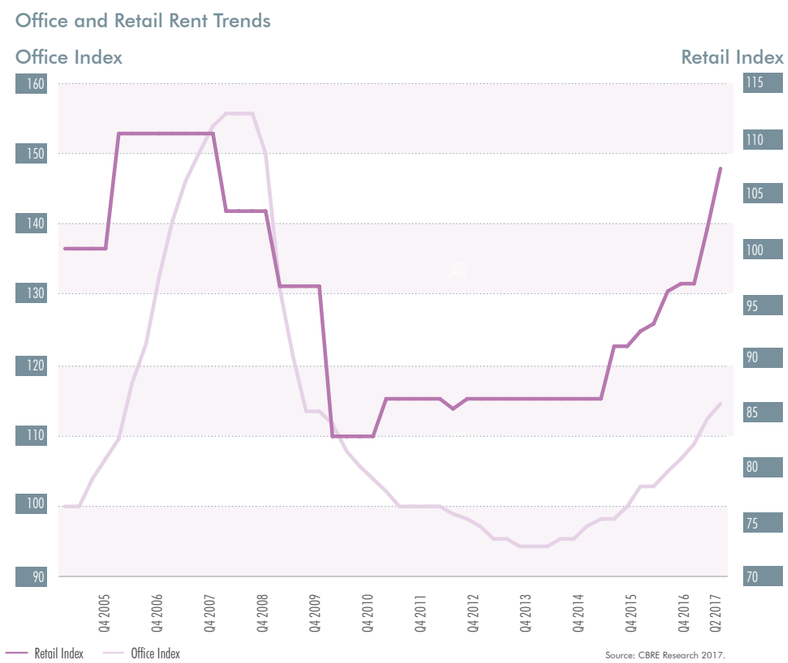
0.4 MSM
Office Space Under Construction

Source: CBRE Research, Q2 2017.

RENT TRENDS

Prime rents increased by around 10% during the first half of 2017; retail activity remains strong in prime, high street locations. In the office sector, prime CBD rents have increased by 14% over the past two years, and a lack of good quality space is pushing rents upward in more peripheral areas as well. We expect rental levels continue their upward trend over the coming months, although it is likely that poorer-quality serviced buildings will not benefit from the rental recovery in the short-to-medium term.

Office and Retail Rent Trends

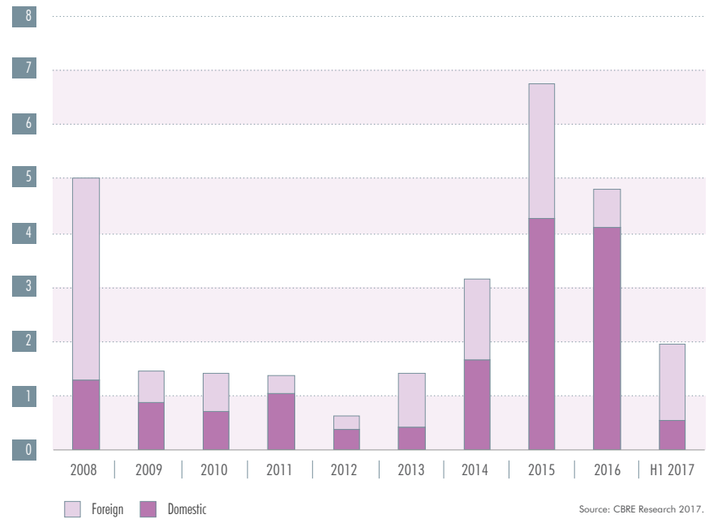


Source: CBRE Research 2017.

INVESTMENT ACTIVITY

Investor demand has remained positive in 2017. Total office investment volume reached almost €635 million (US$722 million) in H1 2017—a 10% increase, year-over-year—with Madrid accounting for 64%. There is growing interest in secondary areas that are outside the CBD but generally within Madrid's first ring-road, the M-30, and in well-established business parks in strong locations. Retail investment figures rocketed upward in H1, thanks to the acquisition of Xanadu Shopping Centre by Intu for a reported €530 million (US$602 million), which also contributed to the high ratio of foreign to domestic investment during the period. In the high-street market, lack of prime product has limited investment, but secondary streets are becoming an increasingly popular alternative.

(US$ Billions) Office and Retail Investment Activity

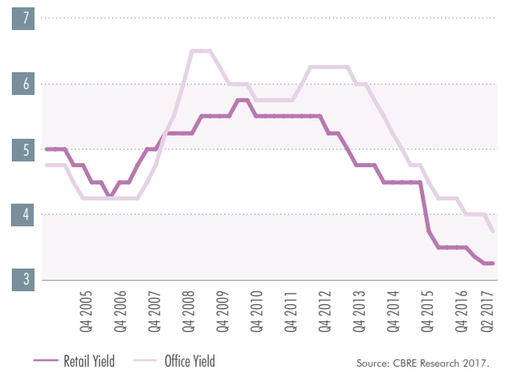


Source: CBRE Research 2017.

YIELD TRENDS

Yield levels for prime retail properties have been historically low since 2015, as demand continues to be very strong from both private investors and investment funds. Madrid's office yields further compressed during H1 2017, to 3.75%—even lower than they were at the peak of the previous economic cycle—and yields for super prime assets are even lower. With further rental growth anticipated for prime assets in the CBD, investment appetite remains high.

Yield (%) Office and Retail Yield Trends



Source: CBRE Research 2017.

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MILAN

High capital values for prime properties in the CBD and Porta Nuova have boosted refurbishment activity as players reposition well-located, value-add real estate to realize capital appreciation.

ECONOMIC TRENDS

The recent recapitalization of several major Italian banks has boosted economic sentiment in Italy. This has broad implications for the confidence of the banking and finance sector in Milan, which accounts for around a fifth of this sector's output in Italy. The growth forecast—0.9% at the beginning of the year—has been revised upwards to 1.4%. This is expected to continue, with a rate of around 1% through 2018 and 2019. By the end of 2017, Milan's economy will have recovered to the level of the previous peak of 2011. According to Oxford Economics, GDP growth averaging 1.8% can be expected between 2017 and 2020, with the largest contribution coming from business services sectors. With improved infrastructure and labor market conditions, occupier demand is expected to continue to strengthen over the short-to-medium term.

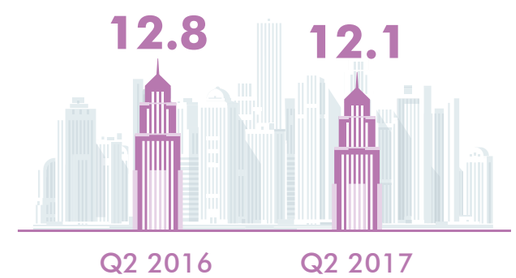
Real GDP Growth (%)

Source: Oxford Economics, CBRE Research 2017.

OCCUPIER TRENDS

Given the ongoing economic growth, international brands are increasingly seeking space in Milan. While the core high street market at Via Montenapoleone is still performing well, Corso Vittorio Emanuele II is attracting retailers seeking larger flagship-size stores at comparatively lower rents. Central submarkets like the CBD and Porta Nuova remain attractive, and several large-scale refurbishment projects are likely to be quickly pre-let. Pharmaceutical and law firms were especially active during Q2 2017, accounting for 20% of take-up.

Office Vacancy (%)



Source: CBRE Research, Q2 2017.

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SUPPLY TRENDS

Office development remained limited during H1 2017. Completions reached 71,622 sq. m., but with developers and lenders still cautious about securing tenants before starting construction, few completed developments and refurbishments were speculative. Projects underway in Milan total around 225,800 sq. m.; approximately 170,000 sq. m. of this is refurbishments. Retail development has been similarly limited since the 2016 completion of two shopping centers comprising 130,000 sq. m. The retail pipeline for 2017 includes of 32,000 sq. m. in the CityLife development, located slightly outside the city center, scheduled for completion by the end of the year. Europe's largest mall is being developed here by Westfield; it is in the planning stages and is expected to complete between 2020 and 2022.

0.1 MSM
New Office Completions

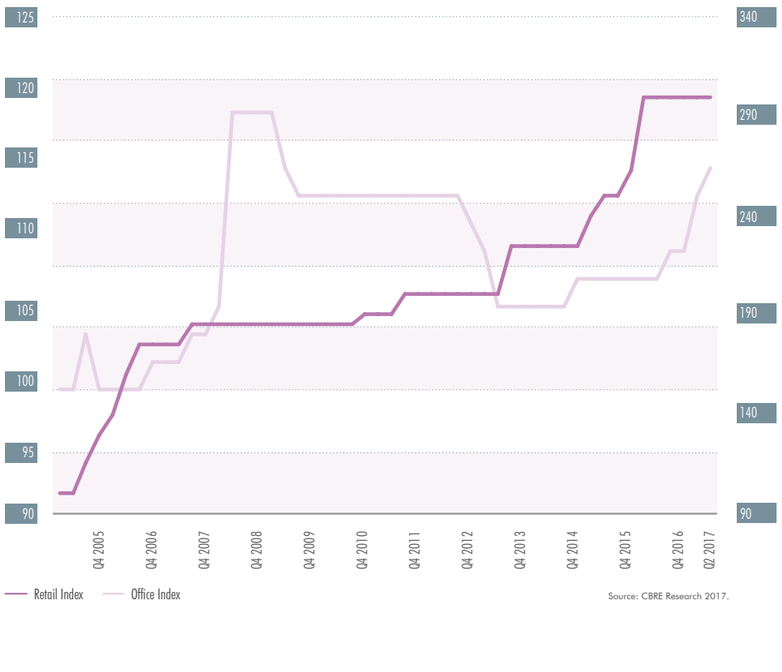
0.2 MSM
Office Space Under Construction

Source: CBRE Research, Q2 2017.

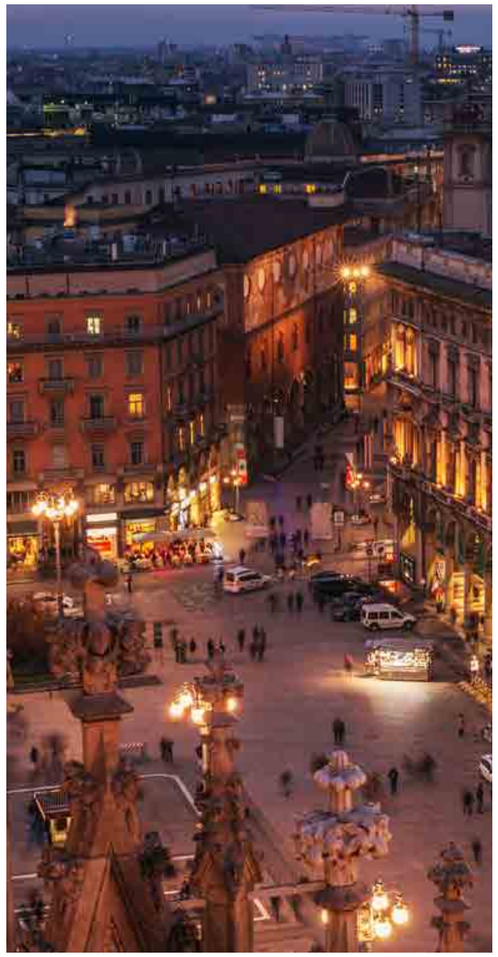
RENT TRENDS

Increasing demand from international corporations and scarce supply of Grade A office stock raised prime office rents to €530 p.a. in H1 2017, close to the 2008 peak. We expect rents to continue to rise at around 6% this year, as market dynamics remain supportive of growth. Similar trends are supporting high street rents, which have plateaued since Q1 2016. Tight supply and strong retailer demand are expected to push prime rents up further in H2 2017, however.

Office and Retail Rent Trends



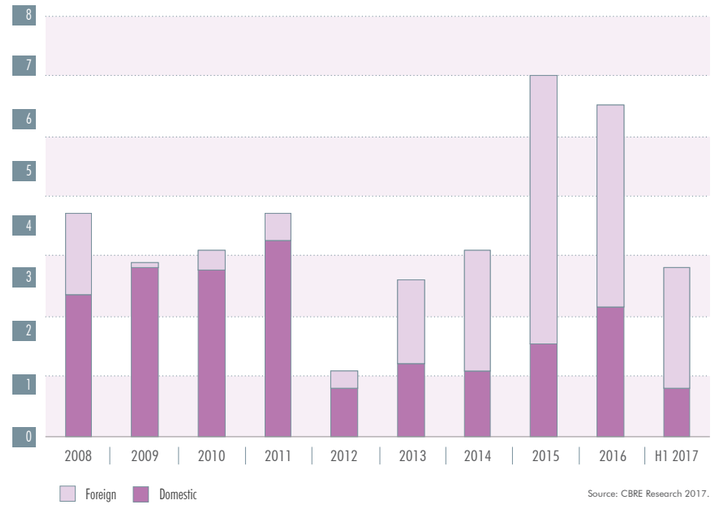
Source: CBRE Research 2017.



INVESTMENT ACTIVITY

Investment totaled €1.4 billion (US$1.6 billion) for office and retail in H1 2017. A lack of good quality product continues to be an issue for real estate in Milan and across Italy. Nevertheless, development activity in Milan is creating new deal opportunities for investors, so we are expecting some forward purchase deals in H2 2017, mainly in the office sector. High street investment activity strengthened in the first half 2017 with some large lot-size deals—namely HM Duomo. The historically low yield levels have incentivized some disposal of retail assets, a trend that is expected to continue in H2. Strong pricing continues to be driven by overseas buyers, who executed 71% of purchases by volume in first half of 2017.

(US$ Billions) Office and Retail Investment Activity

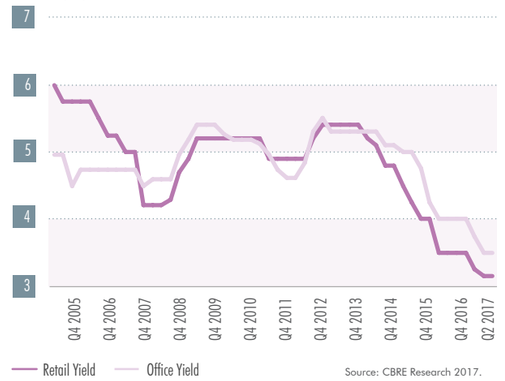


Source: CBRE Research 2017.

YIELD TRENDS

Property yields in Milan are at an all-time low. H1 2017 prime office yields and high-quality secondary yields fell again, to 3.5% and 5.25%, respectively. Strong competition and scarcity of product have continued to put downward pressure on yields. Prime retail net yields dropped from 3.5% in H1 2016 to 3.15% in H1 2017.

Yield (%) Office and Retail Yield Trends



Source: CBRE Research 2017.

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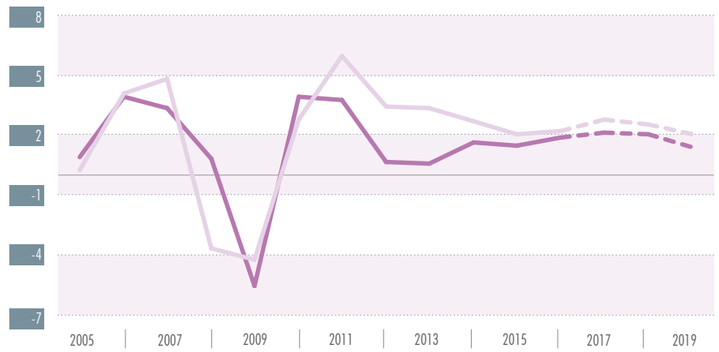
MUNICH

Further declines in prime yields are likely to shift investors' focus toward value-add opportunities and accessible locations outside the CBD. We expect forward purchases and alternative asset classes like hotels, logistics properties and healthcare facilities to increasingly be on investors' radar.

ECONOMIC TRENDS

The outlook for Germany's economy in the coming year remains favorable; robust GDP growth during the first two quarters laid a strong foundation for the remainder of the year. With the interest rate policy of the ECB likely to change over the next year given growing inflation, foreign policy issues are likely to determine future growth prospects. Private consumer spending is likely to continue to be another key driver, supported by currently low interest rates and tight labor market conditions. As with the other German gateway cities, Munich's economy outpaced national growth during H1 2017, which is expected to continue. Expected to support this growth is local population growth, which is forecast to expand by approximately 16% by 2030, according to Munich's Department of Planning.

Real GDP Growth (%)

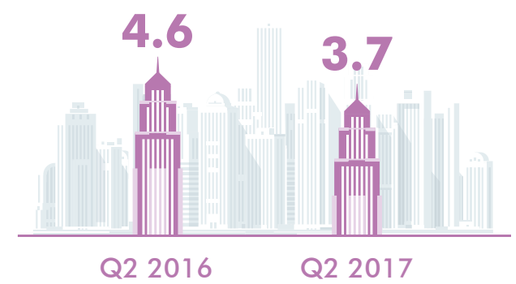


Source: Oxford Economics, CBRE Research 2017.

OCCUPIER TRENDS

Take-up in the Munich office leasing market was 416,900 sq. m. during H1 2017, a year-over-year increase of 5%. A third of it was space in the >5,000 sq. m. category. The most active sectors were the technology, media, telecommunications (TMT) industry with 25% of the total, construction (20%), and consultancies (11%). While more than two-thirds of the take-up occurred in the city of Munich, peripheral areas registered a 62% year-over-year increase primarily due to the scarcity of large-scale modern office supply within the city limits of Munich. The competition for good office space in inner city-locations is unlikely to ease, causing occupiers to increasingly seek space in secondary and peripheral locations.

Office Vacancy (%)



Source: CBRE Research, Q2 2017.

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SUPPLY TRENDS

As there were hardly any speculative completions in the second quarter, and existing vacant office space was largely removed by demolitions or conversions (mainly to hotels and residential), office vacancy continued to decline in Munich, in both the core and the periphery. Of the 171,800 sq. m. expected to be completed in 2017, just 20% remains available, so the supply situation is not expected to ease much this year. In 2018, approximately 284,100 sq. m. will be completed, of which 42% has already been pre-let or is owner-occupied. Only during 2019 will the supply pipeline become less constrained; of the several new projects anticipated that year, 80% remains unlet.

0.1 MSM
New Office Completions

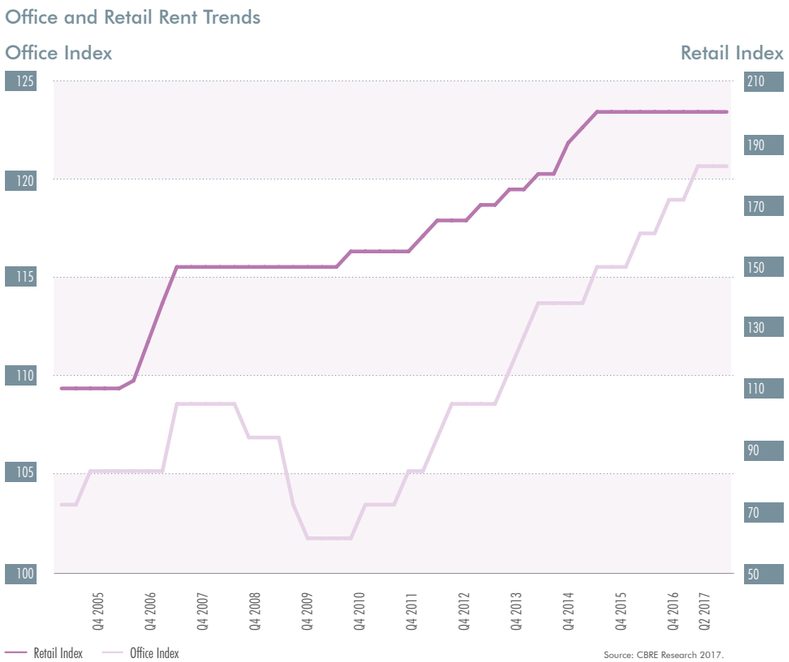
0.5 MSM
Office Space Under Construction

Source: CBRE Research, Q2 2017.

RENT TRENDS

Mid-year 2017 registered year-over-year increases in both the achievable prime office rent and the weighted average rent, which stood at €35.00/sq. m./month and €16.43/sq. m./month, respectively. In peripheral markets, the average rent increased by 4% to €11.12/sq. m./month, due in part to strong demand for new-build space. Over the next 18 months, another rise (around 5%) is expected for prime office rents as a result of the very limited premium office space in Munich's top city locations. Meanwhile, prime high street retail rents are at all-time high of €400 per sq. m. per month, and are forecast to slightly increase over the next five years, due to the solid high levels of demand from both German and international retailers.

Office and Retail Rent Trends

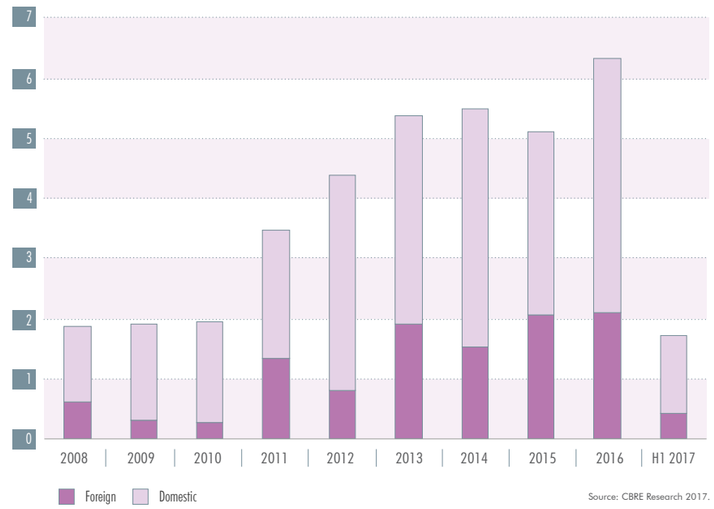


Source: CBRE Research 2017.

INVESTMENT ACTIVITY

The positive economic conditions in Munich and ongoing strength of local letting markets continue to provide ideal conditions for commercial real estate investment. The total transaction volume for the half-year was €2.2 billion (US$2.5 billion) (including all commercial investment classes)—a 12% year-over-year increase and 11% above the 5-year H1 average. More than half (58%) of the total investment volume was attributable to 13 large-scale transactions, each exceeding €50 million (US$57 million). However, scarcity of product remained a significant limiting factor, particularly in the core segment. Although the portion attributable to international investors rose by 42% quarter over quarter, domestic investors remain responsible for 75% of the total volume.

(US$ Billions) Office and Retail Investment Activity

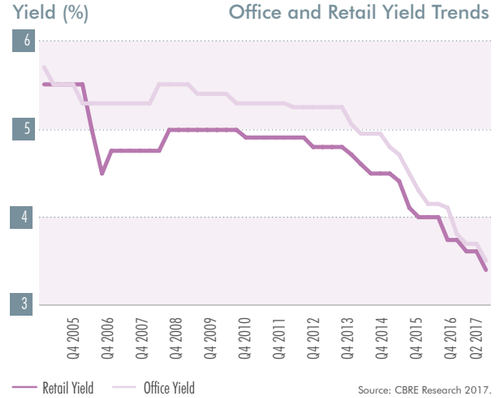


Source: CBRE Research 2017.

YIELD TRENDS

Due to continued high demand for investment product, net initial yields remained under pressure across the whole market. The continued demand focus on premium office properties has resulted in prime office yields' further descent to 3%. For top-class retail properties in central retail locations, the yield fell again—to 2.9%, making Munich the most expensive investment location in Germany.

Yield (%) Office and Retail Yield Trends



Source: CBRE Research 2017.

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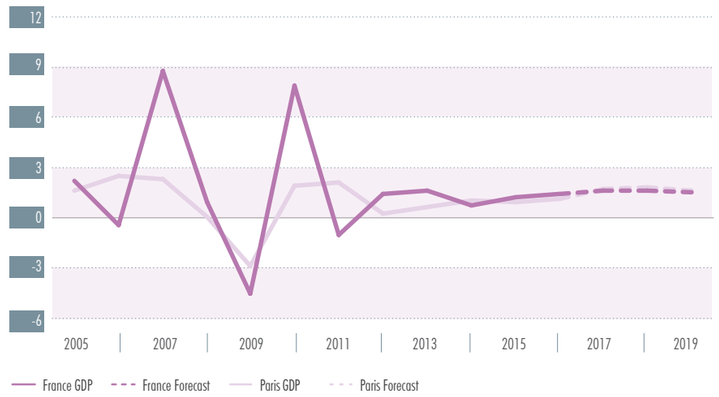
PARIS

Record low yields for prime assets mean that investors need to cast their nets more widely to find properties offering higher returns. Paris offers an environment of low macroeconomic volatility and reduced exchange risk, which will be attractive for buyers developing defensive investment strategies.

ECONOMIC TRENDS

Boosted by a recovery in exports and solid domestic demand, France's GDP growth is expected to accelerate mildly to 1.7% and 1.8% for 2017 and 2018, from 2016's 1.1%. The outcome of the presidential election has generated optimism and dissipated concern about the country's political and economic future. Unemployment is under the 10% threshold and finally seems to have started to decline; this is reflected in the consumer sentiment index, which has returned to its long-term average.

Real GDP Growth (%)

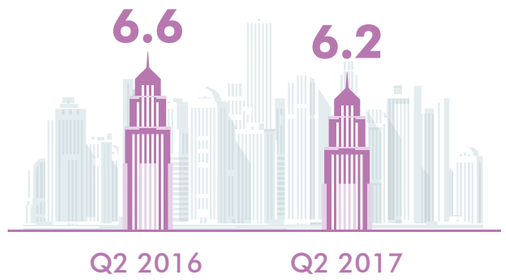


Source: Oxford Economics, CBRE Research 2017.

OCCUPIER TRENDS

The second quarter's 502,100 sq. m. of office take-up was down from Q1's strong 662,600 sq. m., and represents a 16% year-over-year decline. Nevertheless, the H1 2017 total (1,164,600 sq. m.) was 4% above the H1 2016 figure and 6% above the H1 average for 2007-2016. Paris's reputation and strong tourist industry puts it atop the list of markets being targeted by retailers. Among the U.S. brands entering Paris's retail market for the first time, sportswear is notably prevalent, along with cosmetics and beauty.

Office Vacancy (%)



Source: CBRE Research, Q2 2017.

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SUPPLY TRENDS

At the beginning of July 2017, the office development pipeline had begun to expand once again, with 2 million sq. m. underway, of which about 1.5 million sq. m. is in units larger than 5,000 sq. m. The resumption of speculative development was confirmed in H1 2017, with 18 programs underway. The outcome will be a renewal of quality supply in Paris and the region to its west, from 2018 onwards.

0.4 MSM
New Office Completions

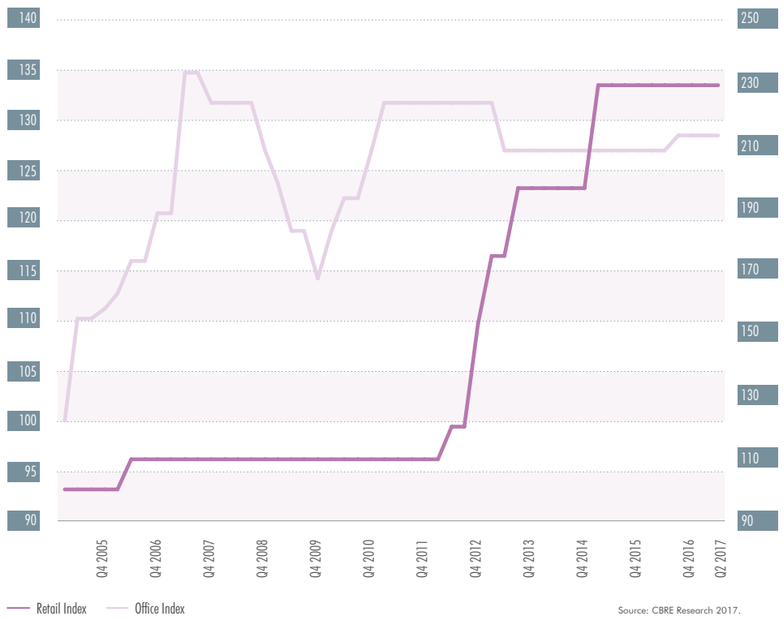
2.1 MSM
Office Space Under Construction

Source: CBRE Research, Q2 2017.

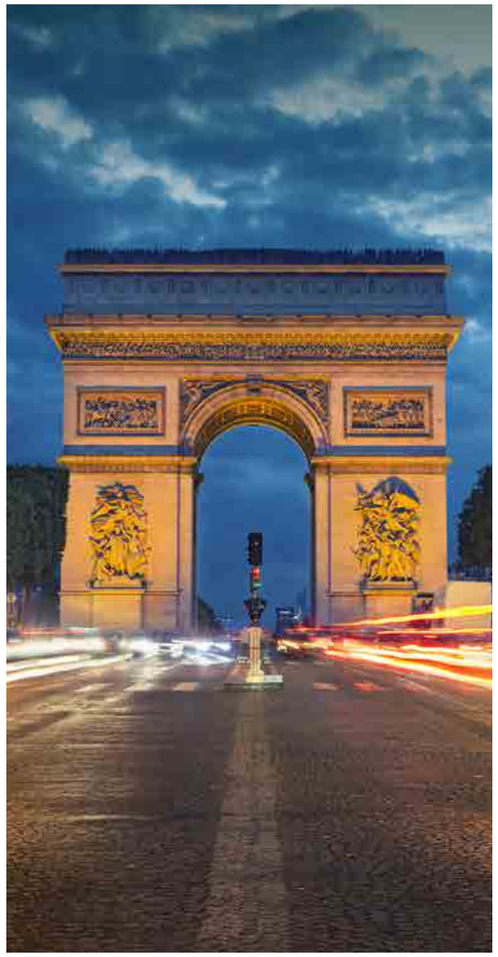
RENT TRENDS

In central Paris, headline rental values are reaching maximum levels, with business occupiers no longer able to absorb further rent increases. Incentives are high, especially in the Inner Rim submarket. In Q1 2017, the effective rent was, on average, 22.1% lower than the headline rent in the Paris region, 16.5% lower in Paris-Centre West, 23.1% lower in La Défense and 26.3% lower in the Inner Rim. Retail rents have remained stable since 2015 and seem unlikely to move significantly from their current position.

Office and Retail Rent Trends



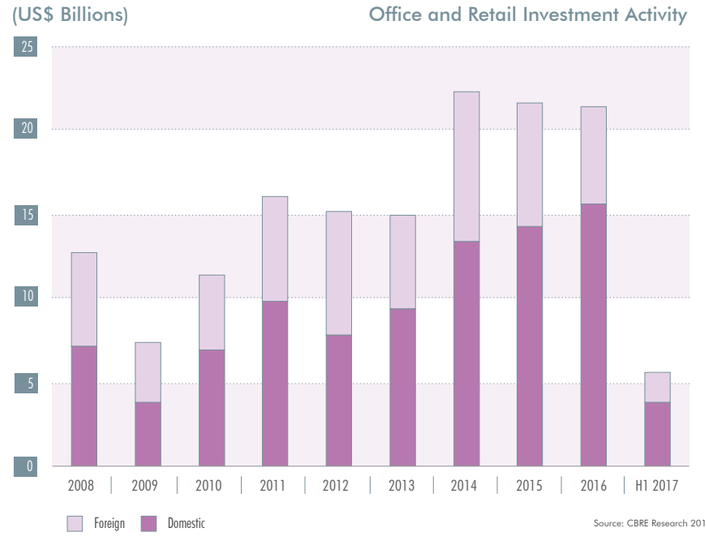
Source: CBRE Research 2017.



INVESTMENT ACTIVITY

In H1 2017, Paris investment volume was down 27%, year-on-year. Transactions larger than €100 million (US$114 million) accounted for just 40% of volume, versus almost 60% in 2016. However, given the transactions in the negotiation pipeline and the structure of supply due on the market, the outlook for H2 2017 appears to be more positive. High street assets accounted for two-thirds of the H1 retail investment market, and €480 million (US$545 million) of this was in Ile-de-France. Total investment volume was limited by an absence of available core assets in this market where demand is high.

Office and Retail Investment Activity

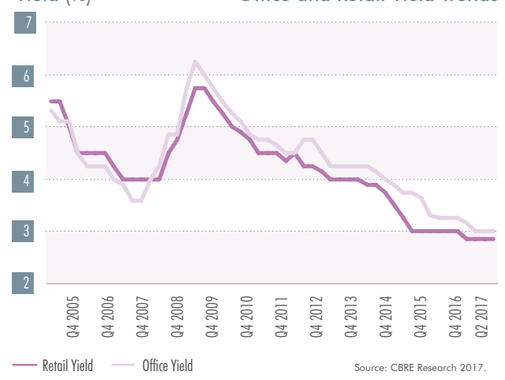


Source: CBRE Research 2017.

YIELD TRENDS

Due to strong competition for prime assets and cheap financing opportunities, Paris prime yields have remained at historic lows: 3% for offices and 2.85% for retail. It is unlikely that yields will fall further, given the potential for interest rates increases, although capital values will be supported by a scarcity of investable product becoming available for purchase.

Office and Retail Yield Trends



Source: CBRE Research 2017.

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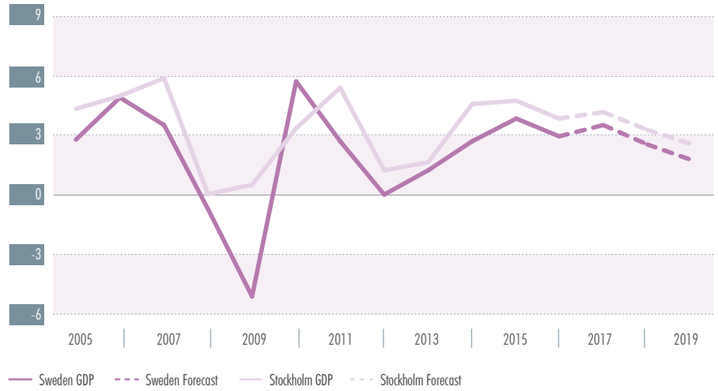
STOCKHOLM

Interest in Stockholm real estate has been especially strong in recent quarters. The current prime yield is at a record low and rental levels are the highest recorded, boosted by a relatively strong economy and extremely low vacancy. Stockholm's rapid growth and a lack of supply in core areas will mean that value-add properties will be the most attractive for investment.

ECONOMIC TRENDS

The investment-led recovery in the OECD countries is good news for Swedish exports, whose contribution to GDP growth will grow in the years to come. On the other hand, domestic demand growth is more subdued, and government consumption will grow more slowly. Housing investment, which has risen rapidly in recent years, is also set to increase less quickly, further depressing growth in domestic demand. The slower growth in homebuilding is due in part to mounting shortages of labor in the sector. The continued economic boom means that demand for labor will be high in 2017 and 2018. Firms' recruitment plans indicate a major need for more personnel, but the increasing scarcity of labor with the right skills will curb employment growth in 2018.

Real GDP Growth (%)

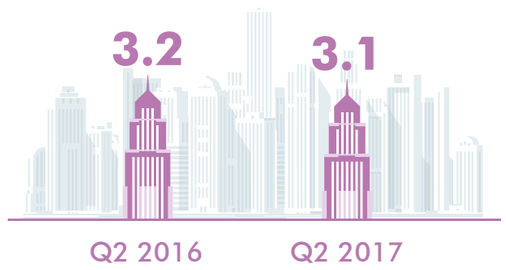


Source: Oxford Economics, CBRE Research 2017.

OCCUPIER TRENDS

In both central Stockholm and peripheral office zones, demand for modern and efficient premises with good access to public transport—preferably the tube—remains high. This has put downward pressure on vacancy rates in most submarkets, and rents continue to increase.

Office Vacancy (%)



Source: CBRE Research, Q2 2017.

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SUPPLY TRENDS

There is a general lack of office supply in Stockholm, especially within the core office sector. With demand for modern, efficient and flexible space high, the limited supply and high rental levels have prompted occupiers to seek quality office space beyond the city center. The borders of the perceived central office area are being pushed outwards. Many office projects are scheduled to begin construction in 2017, with completion dates in 2020 and 2021. Between 2017 and 2019, approximately 420,000 sq. m. of new and refurbished office space will be completed, of which around 70% is already pre-let. This pipeline is significantly concentrated in large schemes in Solna/Sundbyberg, the south suburbs and the CBD.

0.1 MSM
New Office Completions

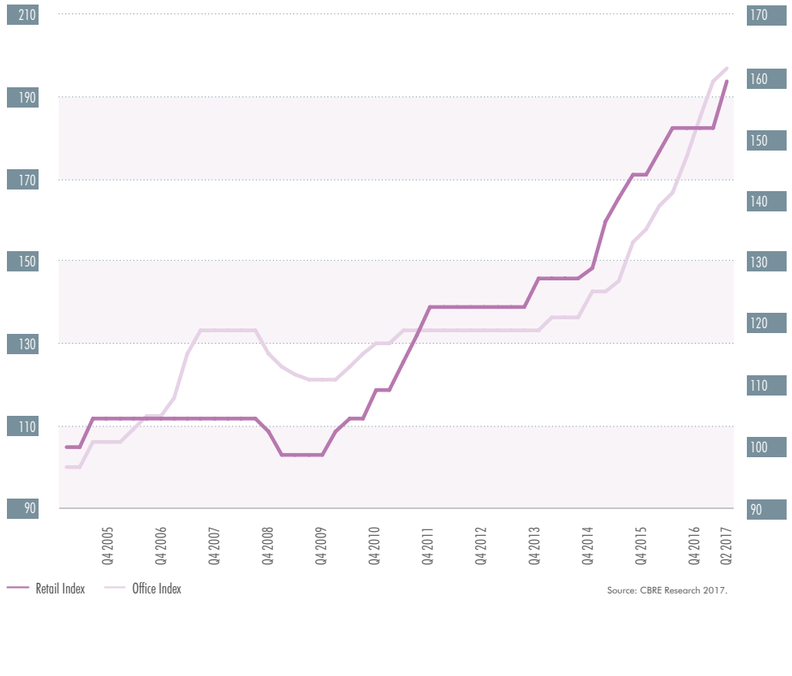
0.4 MSM
Office Space Under Construction

Source: CBRE Research, Q2 2017.

RENT TRENDS

Given the underlying economic strength and employment growth, high demand and lack of supply, prime rents are at record levels. The CBD has the highest office rents in Stockholm, with top rents above SEK 8,000 per sq. m. p.a. Low levels of speculative completions, low vacancy rates and the strong Swedish economy are expected to drive continued rental growth during 2017, albeit at a slower pace than in previous years. Retail demand in the CBD from international retailers remains high while the availability of good facilities in good locations remains low; this ensures continued rental growth through 2017.

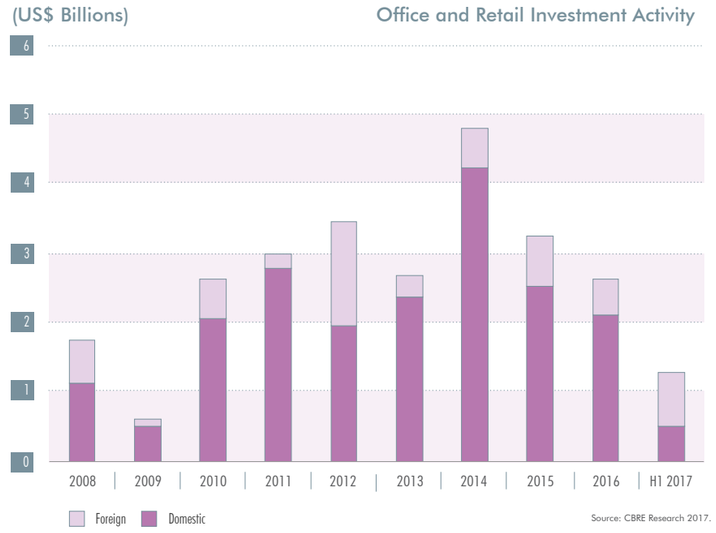
Office and Retail Rent Trends



Source: CBRE Research 2017.

INVESTMENT ACTIVITY

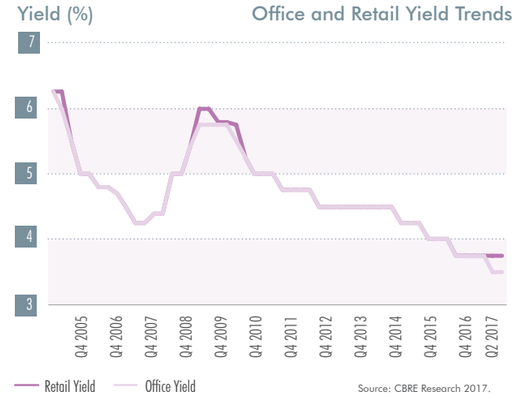
The first half of 2017 witnessed a confident Swedish investment market, with high levels of activity across most markets and segments. The global political and economic uncertainty has not yet had a negative impact on Sweden's investment market, and the Brexit referendum has potentially benefited the Swedish real estate market as interest from international capital sources is particularly high. Foreign investors have been most active in established areas. The office and residential sectors dominated during H1 2017, each representing 25% of the total investment turnover.



Source: CBRE Research 2017.

YIELD TRENDS

With interest in Stockholm's real estate investment market stronger than ever, prime yields are at record lows. Low vacancy and limited supply in the office and retail markets have served to reinforce this situation.



Source: CBRE Research 2017.

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METHODOLOGY

GENERAL

As there is no universally accepted definition of a "gateway city," we fully accept that many cities outside our sample could claim the title. In choosing our cities, we have considered size, transport infrastructure, corporate presence, real estate investment flows and several other indicators of importance. Amsterdam, Beijing, Berlin, Boston, Chicago, Frankfurt, Hong Kong, London, Los Angeles, Madrid, Milan, Munich, New York, Paris, San Francisco, Seoul, Shanghai, Singapore, Stockholm, Sydney, Tokyo, Toronto, Vancouver and Washington, D.C., are the cities we have selected as most relevant to international investors. This report is based on our judgement of which real estate variables are most important from the perspective of an investor seeking a detailed, but not exhaustive, global overview. We have focused on the prime office and prime retail locations in these 24 global gateway cities. Data used this report were derived from CBRE's proprietary data and key external databases, and cover the following topics: economic trends; occupier trends; supply trends; rent trends; investment activity and yield trends.

ECONOMIC TRENDS

In general, for country- and city-level economic growth forecasts, we use Oxford Economics. Due to data restrictions, we use Moody's for GDP forecasts for U.S. and Canadian cities. We think this is a reasonable basis for economic comparison across countries and cities.

OCCUPIER TRENDS

Occupier trends are based on take up activity and vacancy rates. Due to considerable differences in market size, take-up and vacancy figures vary substantially across markets. Take-up in the Americas and EMEA is based on leasing activity minus renewals. In Asia Pacific, net absorption, which represents differences in occupied stock over time, is used to indicate occupier-market conditions. Finally, the vacancy rate is the difference between total stock and occupied stock, measured as a percentage.

SUPPLY TRENDS

Supply trends are based on the current and future development pipeline. Due to considerable differences in market size, development pipeline figures can vary substantially across markets. The development pipeline is based on new office space completions in 2017 in local units (i.e., square feet, square meters or tsubo). Office space under construction is measured as new office space expected to be completed within a two-year window. Each market does have its own set of period and size criteria for reporting office space completions and pipelines. We will underline measurement differences where applicable.

RENT TRENDS

Prime rents are stated in local currency and in terms of the prevailing unit of floor-area measurement (i.e., square feet, square meters or tsubo). All Office rents are denoted as Prime/Class A building rents for the best location in a given market. All Retail rents are based on the achievable rent which an international retailer is willing to pay for an up-to 200 square meter gross retail unit in the best location of a given market (according to CBRE's Global Prime Retail Rent publication). Our prime rents are never based on individual units, but usually represent a relatively small area of town that, over the long term, always seem to command the highest rent. They should not be considered the market average rental value. For global comparison we incorporate an ITZA conversion for London and Paris retail. For convenience, a conversion to USD is provided at current market rates as of end Q2 2017. Therefore, we use the following conversion equivalents for U.S. $: 6.78 RMB, 112.35 JPY, 1144.74 KRW, 1.30 AUS, 1.38 SGD, 7.81 HKD, 1.30 CAN, 0.77 GBP, and 0.88 EURO.

INVESTMENT ACTIVITY

Reported investment activity is based on data from CBRE and Real Capital Analytics. From time to time, global definitions of relevant market area, and transaction types constructed for the purpose of international comparison, may differ from local definitions compiled to give a more granular analysis.

YIELD TRENDS

Outside the Americas, yield information is based on local CBRE estimates of the income return an investor would receive when acquiring a Class A building in a prime location, fully let at current market rental values. The CBRE North America Cap Rates Survey database is the source of yield data for the Americas. The terms "yield" and "capitalization rates" are interchangeable in this report. All data as of Q2 2017.

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