EMEA MARKETFLASH | 28 FEBRUARY 2019

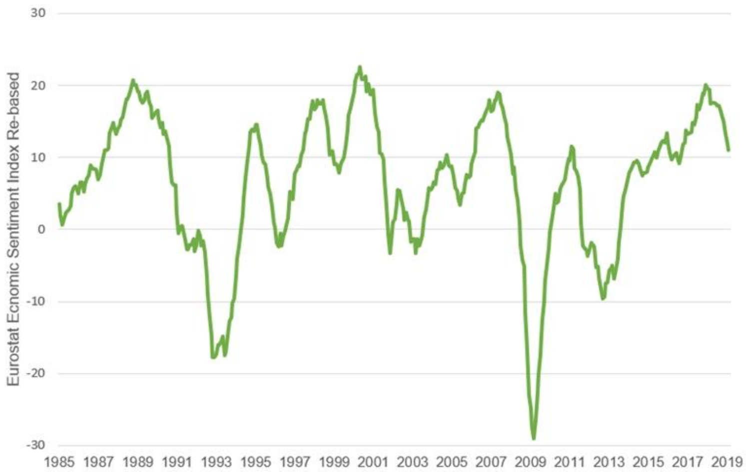
CBRE

European commercial property market remains robust, despite economic slowdown

The “Big 5” European economies have entered choppy waters over the past year, but the situation is unclear and not unambiguously negative

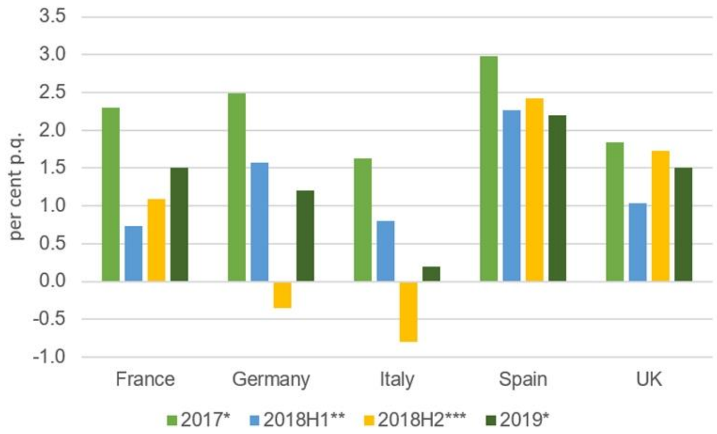
After a strong year in 2017, economic surveys started to flash warning lights in early 2018, followed by a deterioration in official data in H2 2018.

Figure 1: Economic Sentiment - EU Total



Source: Eurostat, CBRE

Figure 2: GDP Growth: Big 5 European Economies



* Annual average
**Q2 and Q4 annualised
***Q4 on Q2 annualised
Source: Eurostat, CBRE (2019 forecast)

Italy entered a technical recession after the new coalition government's programme of tax cuts and spending increases led to conflict over fiscal limits with the European Commission, damaging consumer and investor confidence.

In the UK, disagreements and delays in setting the future post-Brexit relationship with the EU is causing considerable uncertainty. Despite a hit to business investment, however, the impact has not been as serious as some commentators expected.

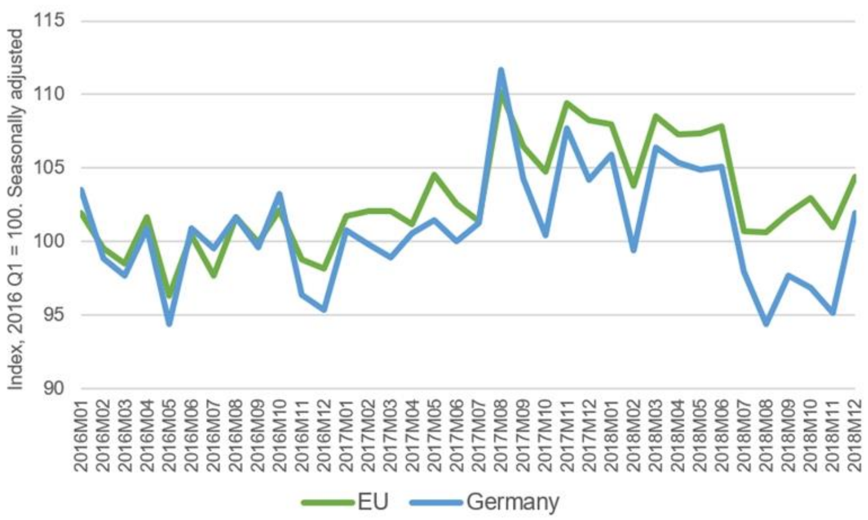
Political uncertainty and populist politics are also an issue in France, where the Yellow Vest protests continue. However, as in the UK, GDP growth in France was faster in H2 2018 than in H1 2018. Spain has also had its political issues, but growth has remained robust.

Germany narrowly avoided a technical recession after posting flat growth in Q4 2018, mainly due to the struggling car industry, by far its most important export.

Credit controls in China have led to an abrupt slowdown in car imports, while the introduction of new emission standards (WLTP) have caused considerable disruption and some short-term closure of plants.

The upswing in new car buying fuelled by cheap and easy credit appears to be coming to an end, and the emergence of electric vehicle technology is contributing to a pause in both consumers' and producers' behaviour.

Figure 3: Index of Production for EU Motor Vehicles



Source: CBRE

Although December data indicated that the disruption caused by new environmental legislation may have passed, it would be premature to expect the European car industry to return to its 2017 highs any time soon.

What does It mean for commercial property?

Despite weak economic growth in H2 2018, there are hopes for a more positive outlook for growth in 2019, supported by low interest rates, fiscal easing, low energy prices, and a partial recovery in car production. Q1 2019 GDP numbers will be crucial for sentiment but will not be released until May, meaning that the markets will be watching survey data closely

Nevertheless, risks including a Hard Brexit, Italy's economy, weak business confidence in Germany and uncertainty over U.S. trade policy will ensure

European businesses retain a cautious attitude towards investing and hiring.

Commercial property has been robust in the face of the economic slowdown, supported by solid fundamentals, ongoing structural changes and strong liquidity.

Although the office pipeline has picked up, new prime office development has been slow to come through compared with previous cycles. Even if the momentum of the last few years slows, CBRE expects 2019 to be another reasonable year for prime office rents, with growth forecast at 3.5% Q4-on-Q4 [1] on average for Europe's major markets. Many office markets appear to have plenty of impetus, with prime office rents in most major European cities, including the City of London, Milan and all German cities, increasing in Q4 2018.

Rental growth in the logistics sector has been weak for several years. However, 2019 could see stronger momentum driven by robust e-commerce expansion and solid net absorption that may well exceed the substantial pipeline under construction. Full-year prime industrial rental growth is projected to be 2.0% y-o-y.

Retail, especially non-prime properties, continues to struggle under the impact of structural change and slower economic growth. Even on high streets, key money is disappearing, and incentives are rising. There is a reasonable chance that even headline prime rents, especially for shopping centres, will fall in 2019.

Prospects in the residential sector remain broadly positive, supported by strong cross border investment. Further capital value growth is expected.

Despite slower economic growth, investment sentiment in Continental Europe is strong and is expected to remain so in 2019, provided no major economic or political shocks arise. Lower for longer interest rates, driven by a global savings glut, will ensure the debt as well as equity side of the market remains liquid. In the UK, market liquidity will depend on how Brexit unfolds.

Nevertheless, the lack of stock for sale, especially in Germany; political and economic uncertainty in several countries; and fewer one-off big M&A transactions in others, is likely to see investment transaction volume decline from its 2018 peak.

[1] All forecasts assume that either a deal will be agreed on Brexit or that Article 50 will be extended.

Contacts:

Dr. Neil Blake
Global Head of Forecasting and Analytics
EMEA Chief Economist
CBRE | Global Research
neil.blake@cbre.com

Jos Tromp | MRICS
Head of Research Continental Europe
Head of Thought Leadership and Data Strategy EMEA
CBRE | EMEA Research
jos.tromp@cbre.com