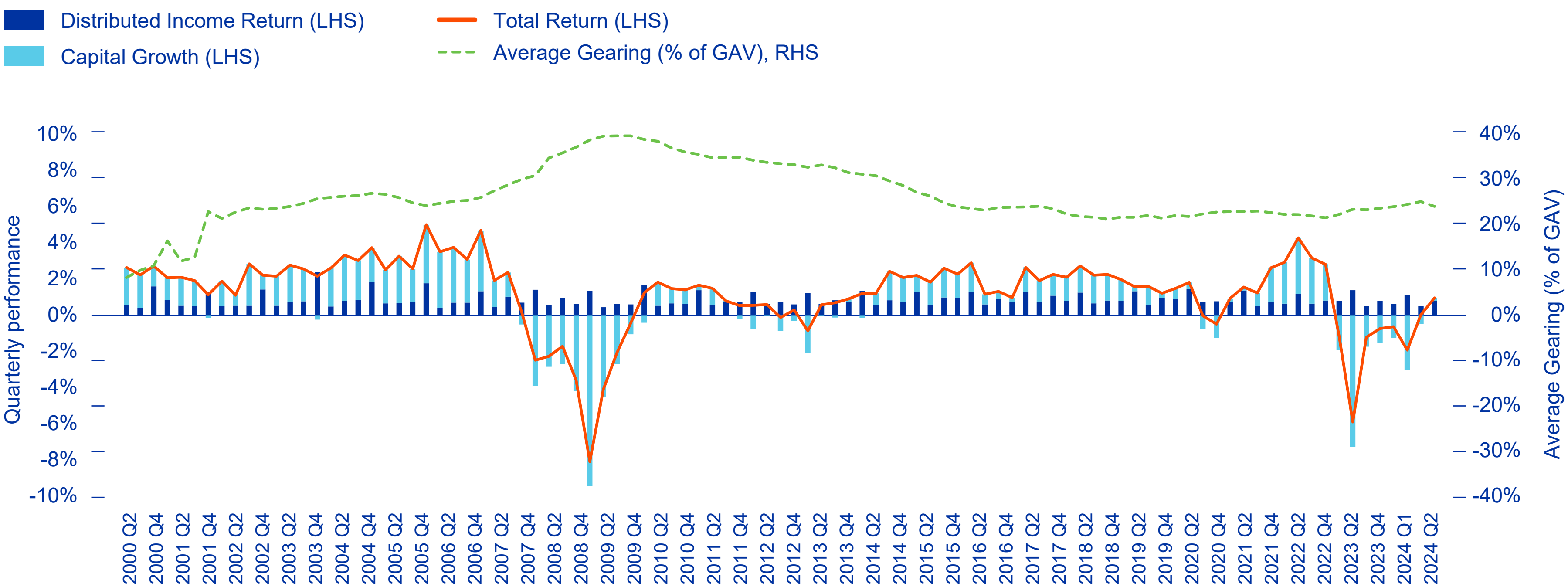
Market Insights on European non-listed real estate in September 2024

The latest edition of the INREV Market Insights indicates that confidence in European real estate is rising. The September Consensus Indicator stood at 55.8, a third consecutive quarterly improvement (see p.6 for more details).

The Q2 2024 INREV Fund Index posted a total return of 0.97%, an improvement from an already positive return of 0.02% in Q1 2024.

At 0.17%, capital growth turned positive for the first time since Q2 2022, a 66 bps quarter-on-quarter (q-on-q) increase. Furthermore, all single sector fund segments recorded positive Q2 2024 performance. Distributed income return increased from 0.51% in Q1 2024 to 0.80% in Q2 2024, bringing the one-year rolling distributed income return to 3.08%.

Figure 1: European non-listed real estate performance



Source: INREV Quarterly Fund Index, Q2 2024

Dutch and UK assets report positive performance for all main sectors

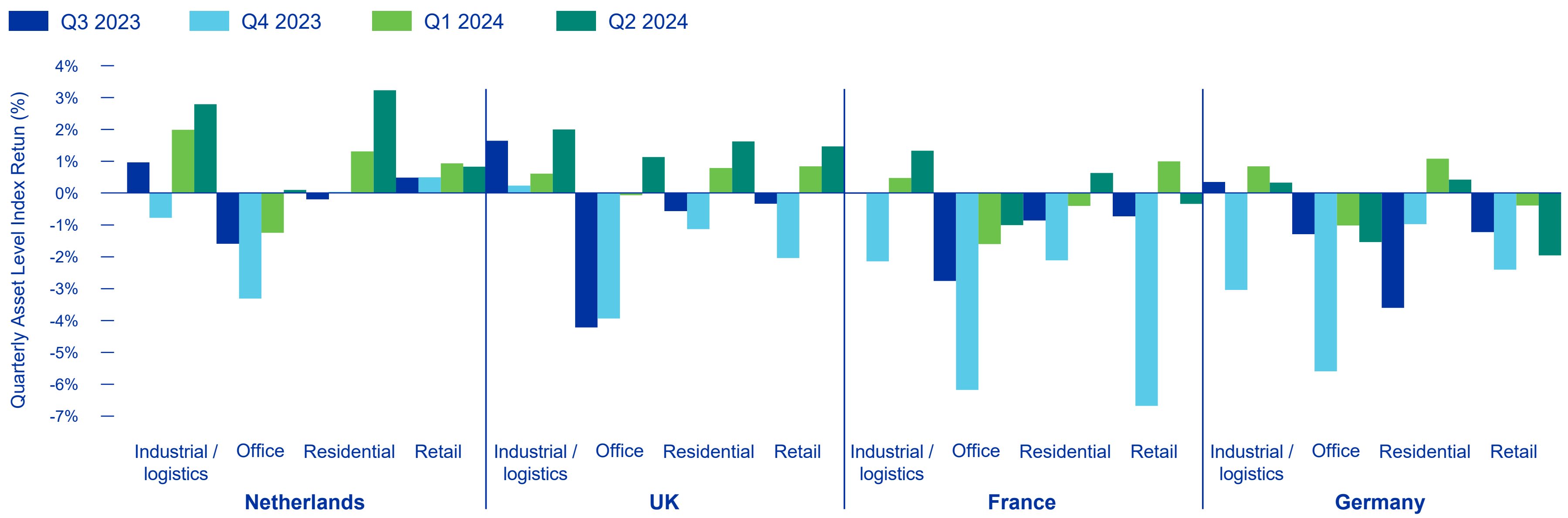
In Q2 2024, both the Netherlands and the UK reported positive returns across all major sectors, marking yet another quarter of outperformance. Dutch assets led with a total return of 2.56%, more than double the 1.11% achieved in Q1. The latest improvement was primarily driven by the industrial/logistics sector. Netherland's consistent performance over the recent quarters is underpinned by the strong fundamentals of its industrial/logistic and residential sectors.

UK assets also saw an improvement in Q2, achieving a total return of 1.59%. The latest results maintain the UK's outperformance over the wider pan-European Asset Level Index since Q1 2023. Industrial/logistics assets led the way, while office assets returned 1.12%, an encouraging sign for the sector, and a stark contrast to the Continental European office market.

France reported solid results in its industrial/logistics sector, with a return of 1.32% for Q2, followed by the residential sector (0.62%). However, French offices posted a negative performance of -1.01%.

Germany, meanwhile, continued on its streak of negative performance for the eighth consecutive quarter, posting a total return of -0.61% for Q2 (a q-on-q decline of -51 bps). German retail sector reported a steep q-on-q decline of 157 bps to -1.96%. At -1.54%, office sector returns remained in the negative territory for the 8th quarter in a row, with further value falls anticipated.

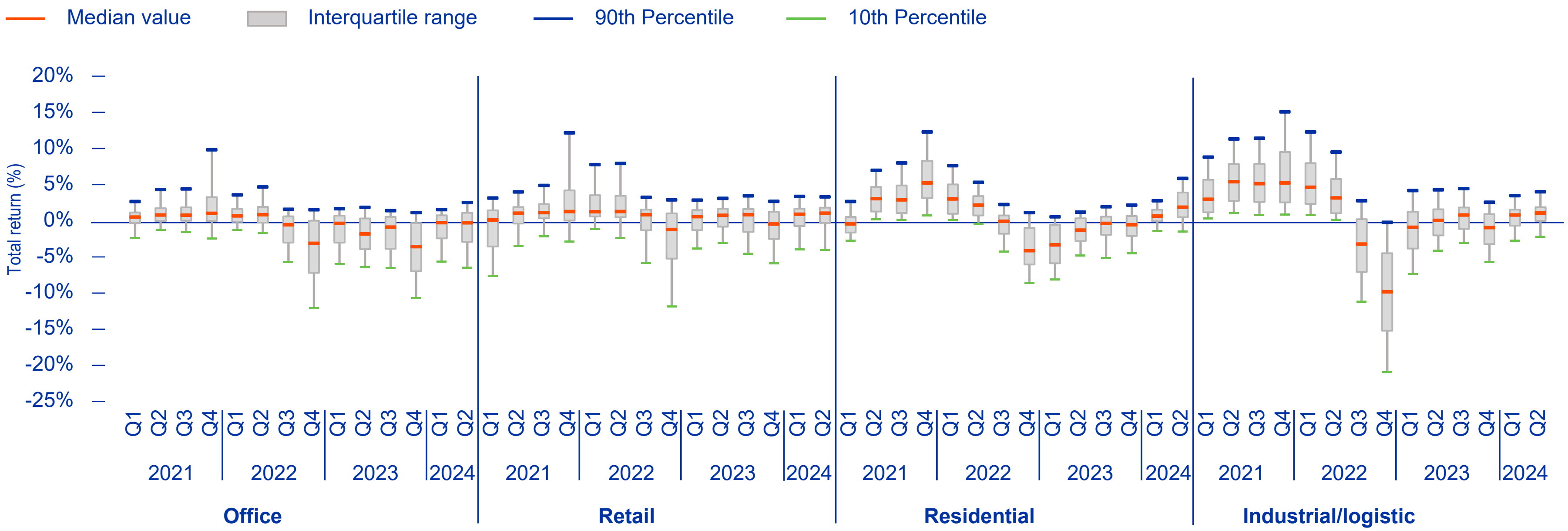
Figure 2: Performance of European real estate assets by country and sector



Source: INREV European Quarterly Asset Level Index, Q2 2024

While each geography reflects different levels of sector bifurcation, the Q2's European best performing sectors showed the lowest dispersion between their best and worst performing assets (see Figure 3). Most notably, the performance range continued to narrow for industrial/logistics and residential assets. The interquartile range narrowed to 6.25% for industrial/logistics assets, a further improvement from an already narrow 8.42% average over the Q1 2023-Q1 2024 period. Given the well documented bifurcation of the office sector, office assets show the highest levels of performance dispersion, a 9.03% difference between the 10th and 90th percentile.

Figure 3: Pan European sector performance distributions



Source: INREV European Quarterly Asset Level Index, Q2 2024

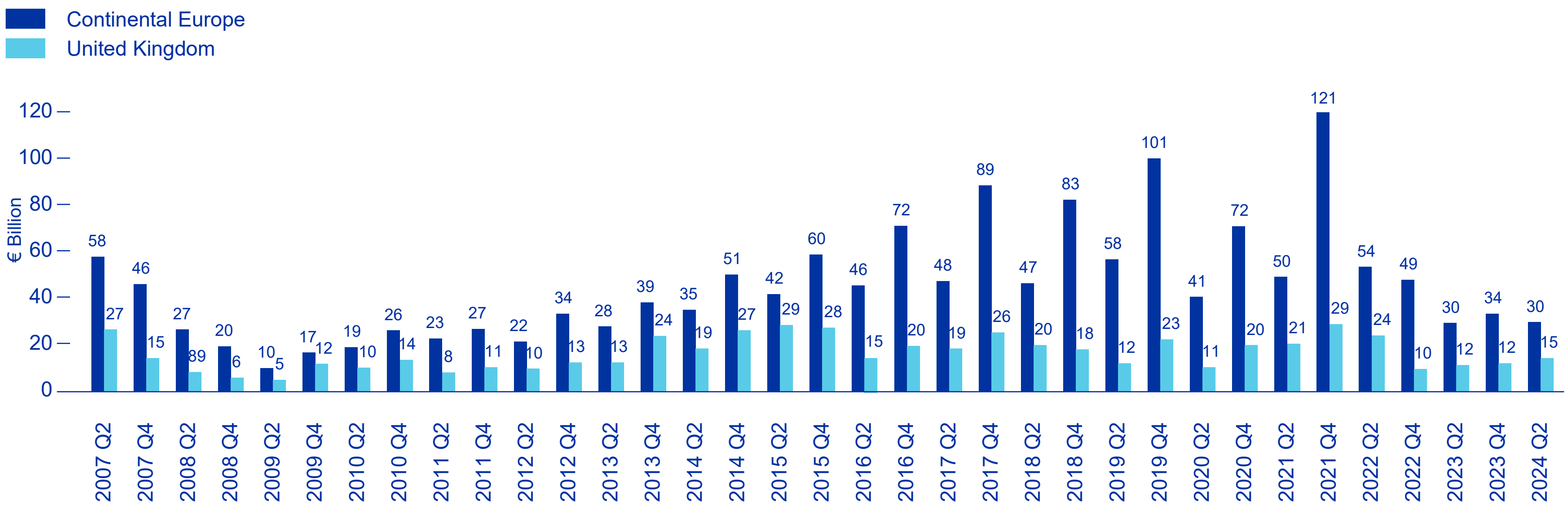
Gradual pick up in Continental Europe and UK transaction volumes

European transaction volumes showed signs of recovery in the second quarter of 2024, with activity picking up in both the UK and Continental Europe.

Total transaction volumes for Continental Europe reached €30.1 billion in Q2 2024, up from €24.2 billion in Q1, with Germany and France driving the improvement. This figure mirrors the Q2 2023 levels (€29.6 billion), though it still falls short of the highs recorded in 2021. The UK Q2 transaction volumes rose to €14.6 billion, up from €13.1 billion in Q1. This marks the highest UK quarterly result since Q3 2022 when it reached €16.7 billion.

Given that the INREV investment liquidity subindicator registered the most significant increase this quarter (59.5 in September from 54.1 in June), a further uptick in investment activity is expected in H2 2024 (see p.6). While transaction volumes are still below historic averages, the improving liquidity signals growing investor confidence and the tentative return of core capital.

Figure 4: Transaction volumes for European real estate



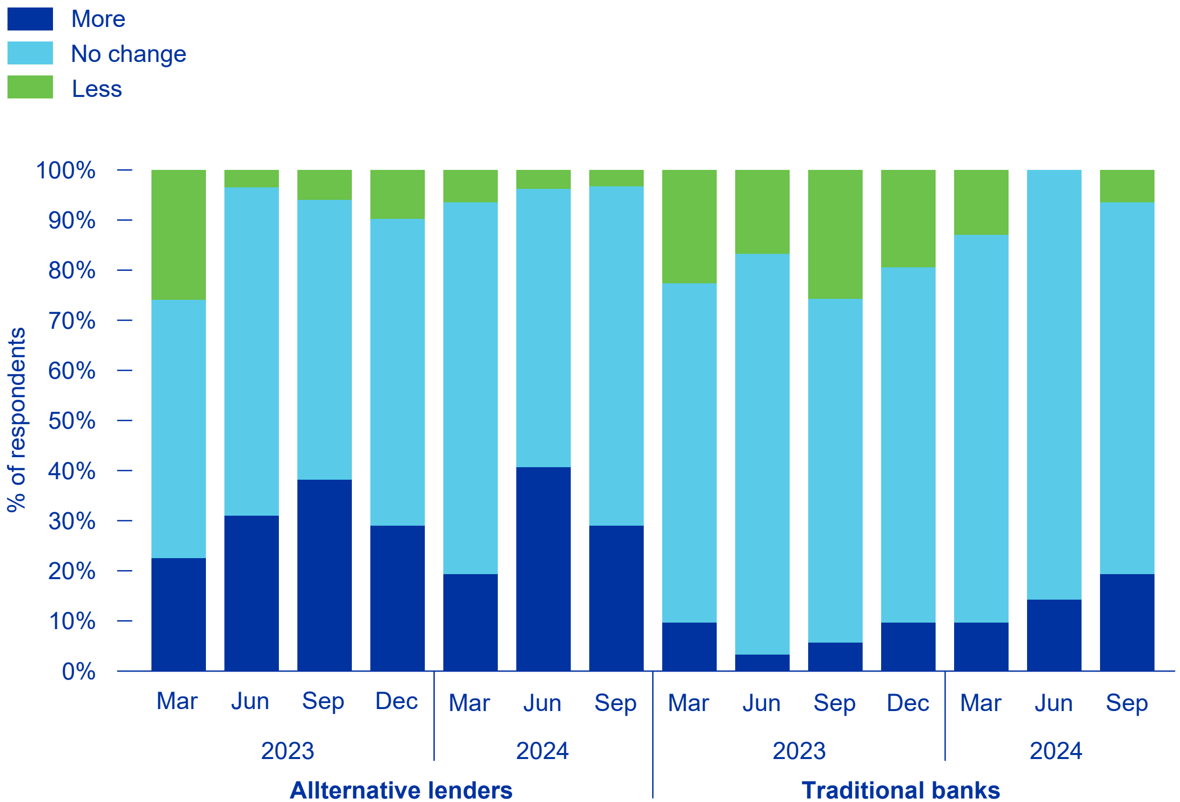
Source: MSCI Real Assets, September 2024

Tentative return of core capital

The latest insights on the new financing activity reveal an early sign of rebalancing between the two key sources of debt. Alternative lenders featured prominently as active lenders since we started monitoring the topic in March 2023. Traditional lenders, ie banks, have only started to be more active in the last two quarters (see Figure 5).

This mirrors recent improvement in investment activity and suggests a tentative return of core capital to the European real estate market. Traditional lenders tend to focus on core strategies and assets and the latest results are encouraging. Better still, there is plenty of room for alternative lenders who tend to focus on the higher risk strategies.

Figure 5: Source of new financing



Source: INREV Consensus Indicator Survey, 2024

September Consensus Indicator confirms European real estate recovery but the leasing and operations subindicator deteriorates

The September INREV Consensus Indicator stood at 55.8, confirming the anticipated European non-listed real estate market recovery. This marks the third consecutive quarterly increase and an all-time high since we started to track the market consensus in March 2023.

Four of the five subindicators showed continued improvement over the last three quarters and most notably since June. Investment liquidity took the top spot among the five subindicators, increasing to 59.5, a sharp uptick from the 32.0 recorded a year earlier. The financing subindicator also reported a strong improvement to 56.6, its second reading of above 50. The economic subindicator remains in the high 50s.

At 49.7, the new development subindicator is the only subindicator that remains below 50, albeit slowly nudging upwards since December 2023.

As mentioned previously, leasing and operations is the only subindicator to deteriorate in September. At 56.3, it revealed its lowest result since we started to track the consensus in March 2023. In December 2023, we anticipated the uncertainty of how long and to what extent the positive momentum for leasing and operations can be maintained, citing a bifurcation of the letting market as a growing risk. Despite this, it remains above 50, still pointing to growth.

Figure 6: INREV Consensus Indicator

Source: INREV Consensus Indicator, 2024

Figure 7: INREV Consensus subindicators

Source: INREV Consensus Indicator, 2024

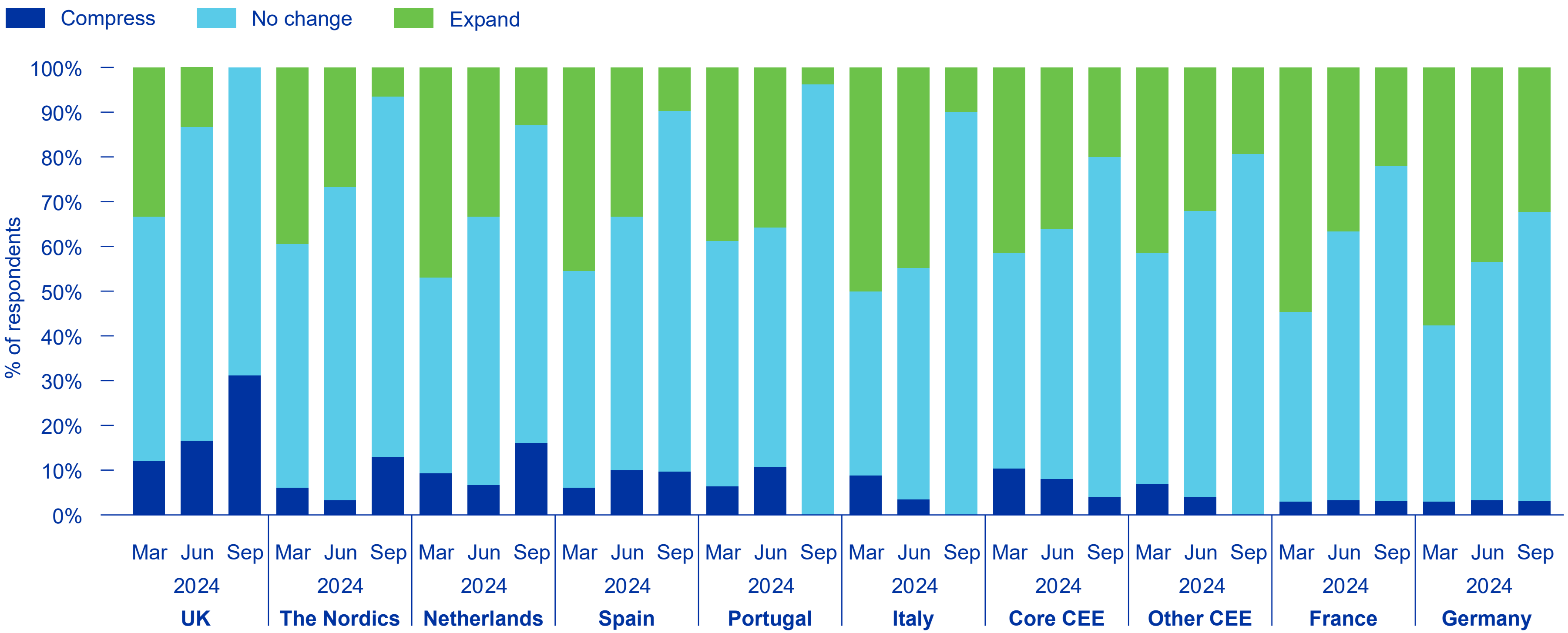
Yield outlook is mixed

Looking ahead, around 80% of the INREV Consensus Indicator Survey participants expect pan-European Q3 2024 performance to be driven by rental income. There is a mixed view on yields, with over 30% of participants expecting yield compression and a further 17% anticipating expansion of yields in Q3, albeit the expectations vary greatly across geographies (see Figure 8).

The UK market is in focus, with the biggest shift in expectations as 31% of respondents anticipate yield compression in Q3 2024.

Several other markets, most notably the Nordics, Netherlands and Spain, appear to be near the end of repricing. Only 10% of participants anticipate yield expansion in Spain in Q3, a notable improvement from the 33% equivalent for Q2 2024. This aligns with the sharp uptick in sentiment towards the Spanish market this quarter (see Figure 9). In contrast, more than 20% of participants predict yield expansion in France and Germany in Q3.

Figure 8: Quarterly change in European real estate yields



Source: INREV Consensus Indicator Survey, 2024

Spain recorded the highest sentiment, pushing the UK into second place

The latest results highlight a significant shift in sentiment for Spain. In September Spain became the most preferred European non-listed real estate investment destination for the first time since the start of the questionnaire in December 2020.

With 31% of contributors preferring it, Spain surpasses the UK, consistently holding first position for the previous seven quarters.

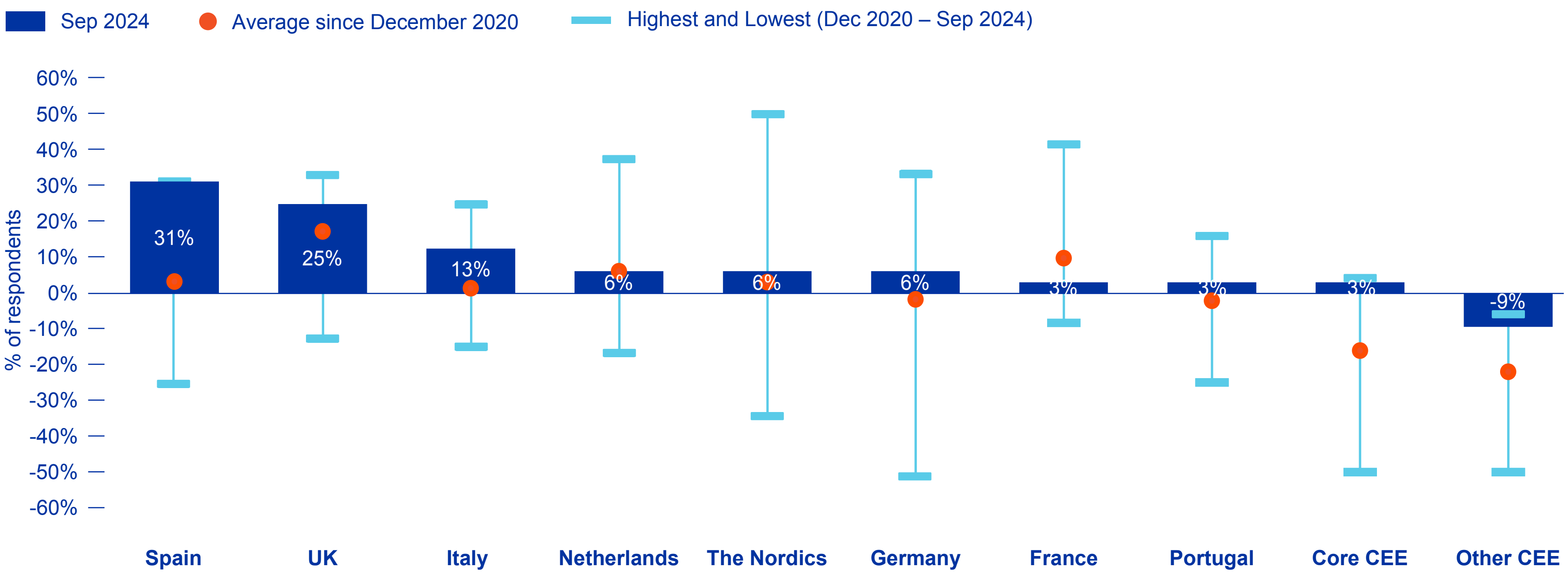
Interest in Spain is predominantly driven by improved economic conditions and higher yields.

Meanwhile, the UK maintains its strong position, with 25% of participants favouring it as an investment destination, marking the eighth consecutive quarter of positive sentiment. The UK's high levels of repricing, high liquidity and relatively robust market fundamentals have kept it in the upper ranks.

Other Southern European markets continued to demonstrate positive momentum. Italy recorded a 13% net positive sentiment, surpassing the Netherlands, with an equivalent result of 6%.

In Northern Europe, Germany, the Netherlands and the Nordics report a stable moderate positive sentiment, all holding at net 6%. For Germany, this marks the second consecutive quarter of positive sentiment, maintaining the same levels as seen in June. The sentiment towards France is weaker, with a net 3%, albeit a slight deterioration on the 6% reported in June.

Figure 9: Net sentiment towards European real estate by geography



Source: INREV Consensus Indicator Survey, 2024

Sentiment for residential remained strong

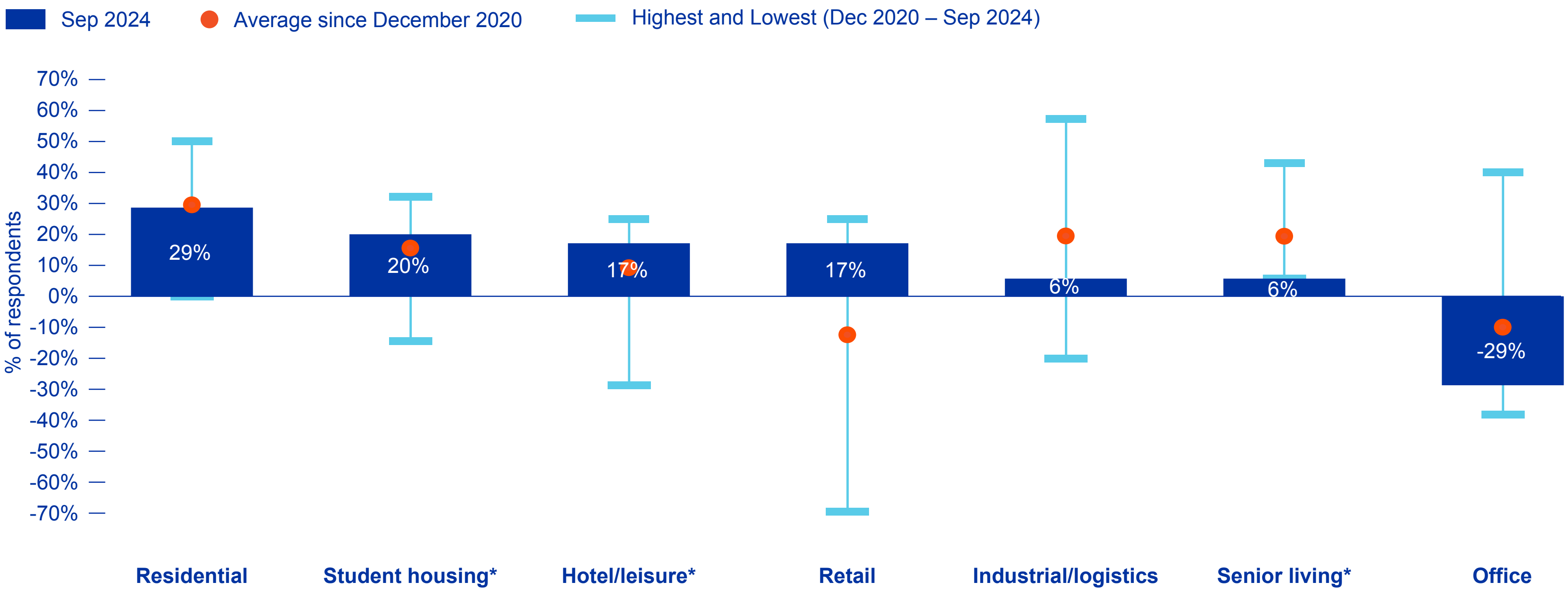
As of September 2024, residential remained the top preferred sector, maintaining a strong position with 29% net interest, reflecting only a slight decline from the June 2024 results.

Hotel and leisure assets saw a significant surge in interest, climbing from 9% to 17% this quarter. This marks the highest sentiment for hotel/leisure since December 2022, a positive shift driven by a recovery in tourism and an increase in travel demand post-pandemic[1].

At 17%, retail is now on par with hotel/leisure, a marked turnaround from an average of -12% over the December 2020-September 2024 period. This is consistent with recent positive quarterly and annual performance, showcasing an improved outlook off the back of significant repricing in some of its subsectors and renewed investor confidence in others (see Figure 2).

Unsurprisingly, offices remained in last place with a negative sentiment of -29%, reporting yet another quarter of decline in interest. The ongoing challenges in the office market are exacerbated by shifts in working patterns and increased vacancy rates. As reflected in the recent performance figures, Germany is particularly affected due to high office allocations and an oversupply of office stock.

Figure 10: Net sentiment towards European real estate by sector



Source: INREV Consensus Indicator Survey 2024

[1] *Southern Europe Leads the Way in Tourism Recovery, Statista, 2024*

Performance outlook improves for the third consecutive quarter

Overall, the latest European real estate market results are encouraging. Performance expectations have improved for the third consecutive quarter, with 40% of respondents expressing a further positive shift in September (see Figure 11).

At the same time, the perception of investment risks has continued to decrease, with a net reduction of 34% (see Figure 12). These results mark a third consecutive quarter of improvements and should positively feed into the H2 2024 European real estate market performance.

Figure 11: View on European real estate performance

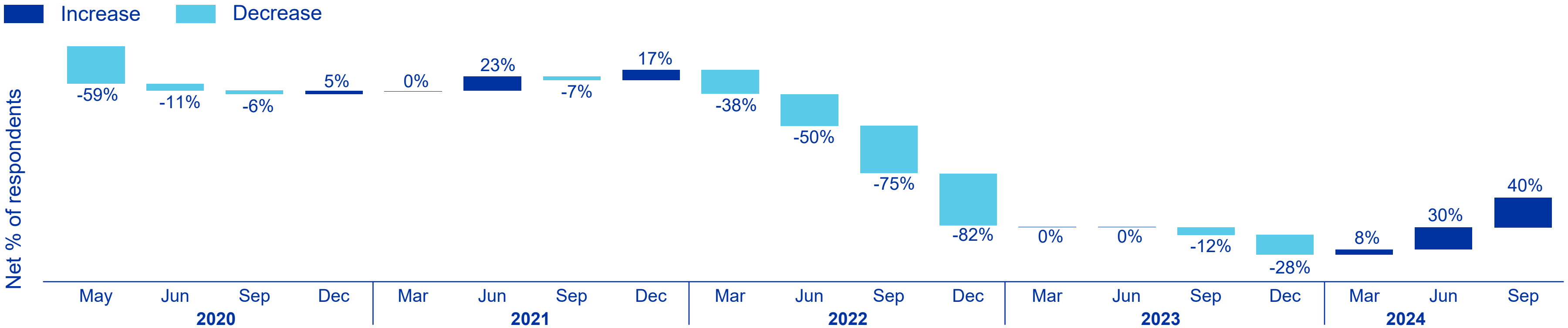
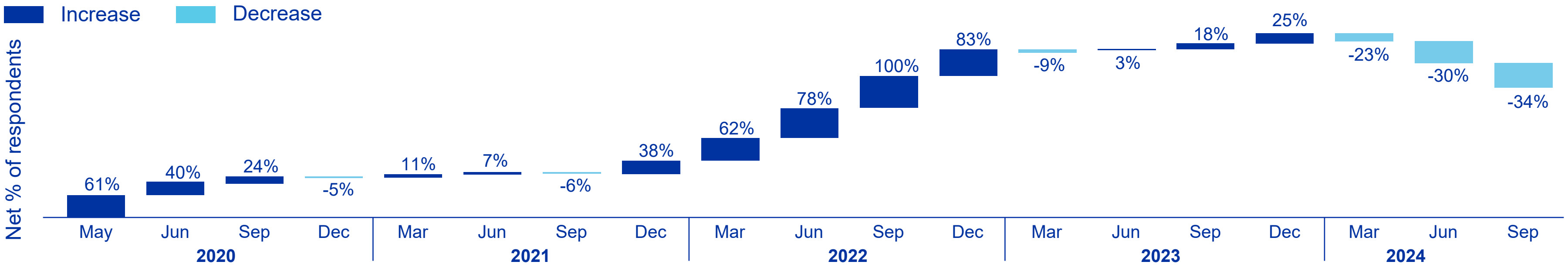


Figure 12: Assessment of investment risk for European real estate



Source: INREV Consensus Indicator Survey, 2024

This update highlights the latest results from the INREV European Quarterly Asset Level Index Q2 2024, INREV Quarterly Fund Index Q2 2024 and INREV Consensus Indicator September 2024 to illustrate the impact on market performance, investment plans and operations.