



Research
Programme
2015–2018

EUROPEAN
CONSENSUS
FORECASTS

MAY 2015

Survey of Independent Forecasts of European Prime Office Rents

REPORT

This research was commissioned by the IPF Research Programme **2015 – 2018**

European Consensus Forecasts

This research was funded and commissioned through the IPF Research Programme 2015–2018.

This Programme supports the IPF's wider goals of enhancing the understanding and efficiency of property as an investment. The initiative provides the UK property investment market with the ability to deliver substantial, objective and high-quality analysis on a structured basis. It encourages the whole industry to engage with other financial markets, the wider business community and government on a range of complementary issues.

The Programme is funded by a cross-section of businesses, representing key market participants. The IPF gratefully acknowledges the support of these contributing organisations:



Survey of European Office Market Rental Forecasts May 2015

Economic Background

The eurozone economy as a whole grew by 0.4% in the first three months of 2015, although this figure was slightly below analysts' expectations. Growth in the bloc has been accelerating slowly over the past year to become the fastest quarterly growth rate for nearly two years, surpassing that of the UK as well as the USA. This performance may be linked to sharply lower oil prices, a weakened euro and increasing European Central Bank monetary stimulus. Bond yields have increased across Europe, with the German 10-year bund yield rising from 0.1% in April to 0.7% by the beginning of May. This increase, together with five-year inflation expectations hitting a three-month high of 1.76% in March, has led to predictions that the eurozone is in recovery.

This change is also reflected in an increase in consumer confidence among many of the eurozone countries. One industry driving(!) this increase is car manufacturing, with sales up by 24% in Spain and Italy, whilst in Ireland sales in the first quarter of the year totalled more than in the whole of 2009. Household expenditure across the eurozone has also increased in tandem with a fall in unemployment. At its worst, 2013 saw an average 11.1% unemployment for European Union countries as a whole, compared to 9.8% for the first quarter of this year.

From an investment perspective, commercial real estate investment within the eurozone has increase by 40%, to €51.4bn in quarter one 2015 compared to the first quarter of 2014. However, offices made up only 39% of this investment, the lowest percentage this sector has represented since 2011. Investment overall reflects a general trend of rising inflation and strengthening of economies, reaching 2007 levels with over €200bn-worth of transactions over a 12 month period.

However, a very different picture prevails in a number of member states, where any recovery remains very feeble. With an economy that has shrunk by 25% in five years and an unemployment rate of 26.5%, the desperation of Greece's situation has been clearly demonstrated by its recent use of International Monetary Fund funds to make a repayment to the IMF itself. This has led to expectations that the country will be unable to meet its further obligation of a €305m debt repayment due to the IMF on 5 June.

Looking nearer home, following the UK general election on 7 May, the return of a Conservative government raises the spectre of a referendum and potential "Brexit" from the European Union. These could have far-reaching consequences, even if the UK chooses to remain within the EU, calling into question many treaties and trade alliances throughout Europe. The UK is one of the largest contributors to the EU, although only constituting around 1.0% of its GDP, and the impact could be far greater for the other countries in the trading bloc. However, as the forecasts used in this report were generated prior to the UK general election, the implications of the forthcoming renegotiations and promised vote may not be reflected in the current analysis.

Key Points

Key Points

2015

- For the current year, sufficient forecasts have been received that Athens can now be reported alongside the other 29 locations covered by this survey. Rental growth expectations continue to range widely, with Dublin and Moscow again recording the highest and lowest average rates, at 13.5% and -13.4%. The median and mean rental growth projections across the entire region for 2015 are more restrained, at 2.3% and 2.2% respectively.
- Twenty four of the forecasts have improved in the six months since the last survey (10 by 1.0% or more), although the projections for all five of the centres that in November 2014 were expected to deliver negative growth in 2015 have continued to weaken.
- Aside from Dublin's sustained performance, which last year recorded nearly 38% growth over the 12 months (€ 491,48 psm compared to €365,81 psm reported as the average prime rent at the end of 2013), London's City and West End remain the other leading markets, with projected growth in the current year of 9.9% and 9.0% respectively (1.4% and 2.7% higher than the November average forecasts).
- Of the six markets (from five in November) predicted to weaken in 2015, four could fall by 1.0% or more over the year. The decline in sentiment for the Moscow market has accelerated significantly, from -4.2% in November to -13.5% currently. Warsaw, Prague and Rome are the other locations to have attracted further weakening of forecasts, albeit marginally in the latter cases, but rather more substantially for Warsaw, to -3.3% from -1.6% six months ago.

Next year and beyond

- In **2016**, all but one location are projected to show positive growth, the exception being Warsaw, although the rate of decline in that city is expected to reduce to -1.3%. The range of positive growth rates extends from 6.8% for Madrid (displacing Dublin as the leading office market) to Zurich at 0.4%. Compared to 2015, however, forecast rates for 14 locations indicate a slowdown in growth next year, halving in the case of Dublin, although the Irish capital is still expected to show a 6.7% increase. Growth in six other markets (Helsinki, Budapest, Luxembourg and all three UK centres) may be more than 1.0% lower than the 2015 projections.
- In **2017**, all centres are forecast to deliver positive growth, ranging from 0.1% in Budapest to 6.1% in Madrid. In 25 locations forecast rents are predicted to grow by more than 1.0%, with up to 17 centres being forecast to deliver growth of more than 2.0%, including Athens at 2.2%. Madrid again is currently anticipated to show the strongest growth at an average of 6.1%.
- The **three-year** rolling averages vary between -2.8% per annum for Moscow to 7.1% for Dublin (from 13.5% in November 2014). London City and West End have been displaced in the rankings by Madrid as the next best location, at 6.6% per annum. Twenty five centres are forecast to deliver average positive annual growth of 1.0% or more over the period 2015-2017, with only Warsaw prime rents, at -1.2% per annum, joining Moscow in being expected to fall.
- Similar to the November survey results, the **five-year** averages indicate all markets other than Moscow, at -0.2% (previously -2.0%) will deliver positive growth, although 11, as compared to 16 centres in November, may grow by 2.0% or more per annum between 2015 and 2019. Madrid and Barcelona, at 5.7% and 4.5% respectively, are now expected to outperform the Dublin market, which has weakened to 4.0% on average from the last survey's forecast of 9.0%.
- Changes in averages between November 2014 and May 2015 for each forecast period are detailed in Appendix 1.

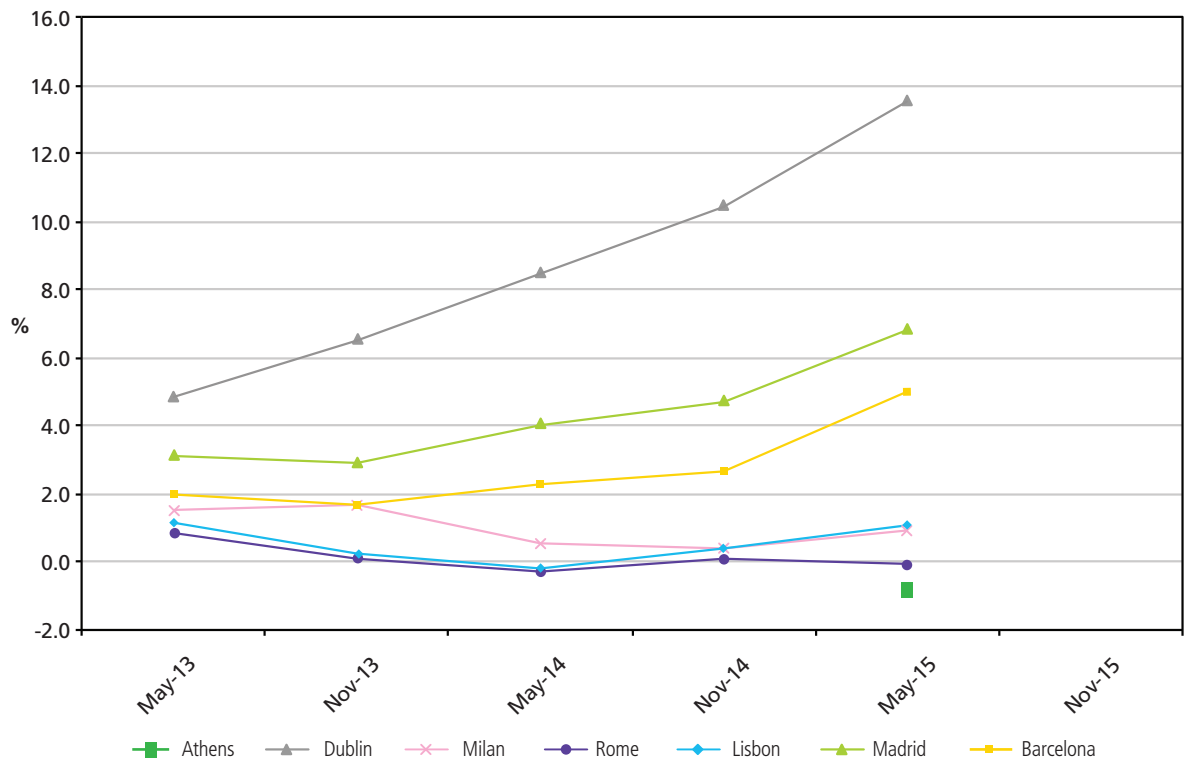
2015 to see improved growth in the majority of markets

For the current year, 16 office markets are predicted to show growth in excess of the 2.2% average across all centres monitored, including three of the four German and both Spanish cities, as well as all three UK locations. Comparative figures from the November 2014 survey suggested an average rate of 0.5% with 21 anticipated to grow by more than this, although only 13 centres were expected to deliver 2.0% or more.

Comparing individual average forecasts generated by the November 2014 survey with current projections, 21 of 29 locations have improved over the last six months, of which 10 have increased by 1.0% or more (and six by 2.0% or more). As previously identified, the negative growth rate for Moscow offices has fallen further, by an average of -9.3%, to -13.4% for 2015. This has been as a result of the continuing economic difficulties in Russia, combined with a weakening domestic currency and reduced occupier demand, putting office rents under downward pressure. Of the remaining locations where forecasts have reduced over the period, only Warsaw, Zurich and Prague have deteriorated by more than -1.0%.

The range of forecast average growth rates across all centres has increased to 26.9% from 14.6% in the last survey. The lack of consensus amongst individual forecasters for the Moscow market has fallen over the last six months, as the spread of forecast growth rates has reduced from 34.6% to 14.4% for 2015. This range of opinion in growth rates is only exceeded by those for the Dublin market, which has attracted a spread of 18.2% across the 12 contributor forecasts for this location. Clearly, views on economic growth expectations, of up to 4.0% in 2015, would make Ireland among the fastest growing economies in the EU and, combined with a rapid reduction in unemployment rates, could exert considerable influence on the performance of the office sector.

Figure 1 shows current forecasts for locations in those economies that have been under the greatest strain during the eurozone crisis. With the exception of Rome and Milan, all centres appear to be maintaining their upward course in terms of rental growth expectations. Milan's modest decline in November is likely to be reversed (to 1.0% from 0.4%), whilst the prospective growth in the two Spanish markets potentially reflects that country's successful implementation of structural reforms and management of its housing crisis, which have had a favourable impact on its growth outlook. Having received data from six contributors for Athens, it is now possible to analyse forecasts for this location, although the immediate average projection is negative for the current year (-0.8%), from an end-2014 average prime rent of €223,55 psm.

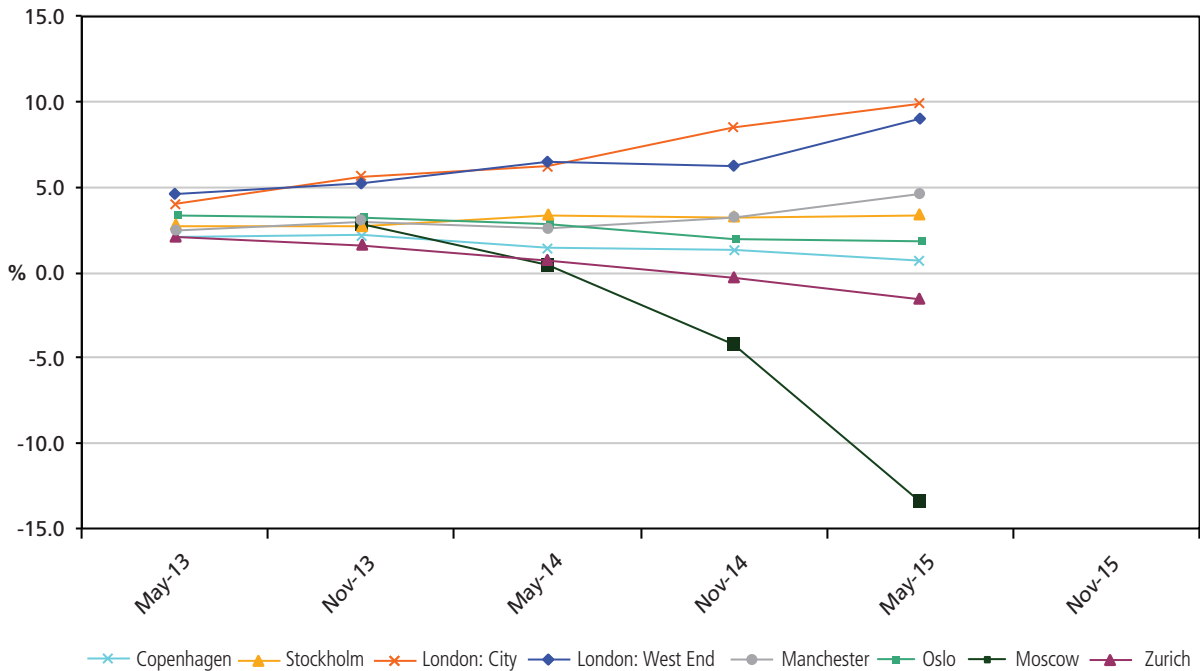
Figure 1: Weighted Rental Growth Forecasts 2015 – Peripheral Eurozone Economies

In eastern Europe, the average outlooks for Warsaw and Prague have worsened slightly (from -1.7% to -3.3% for Warsaw and from -0.5% to -1.5% for Prague), whereas the Budapest market is continuing to improve (from 1.0% to 2.8%).

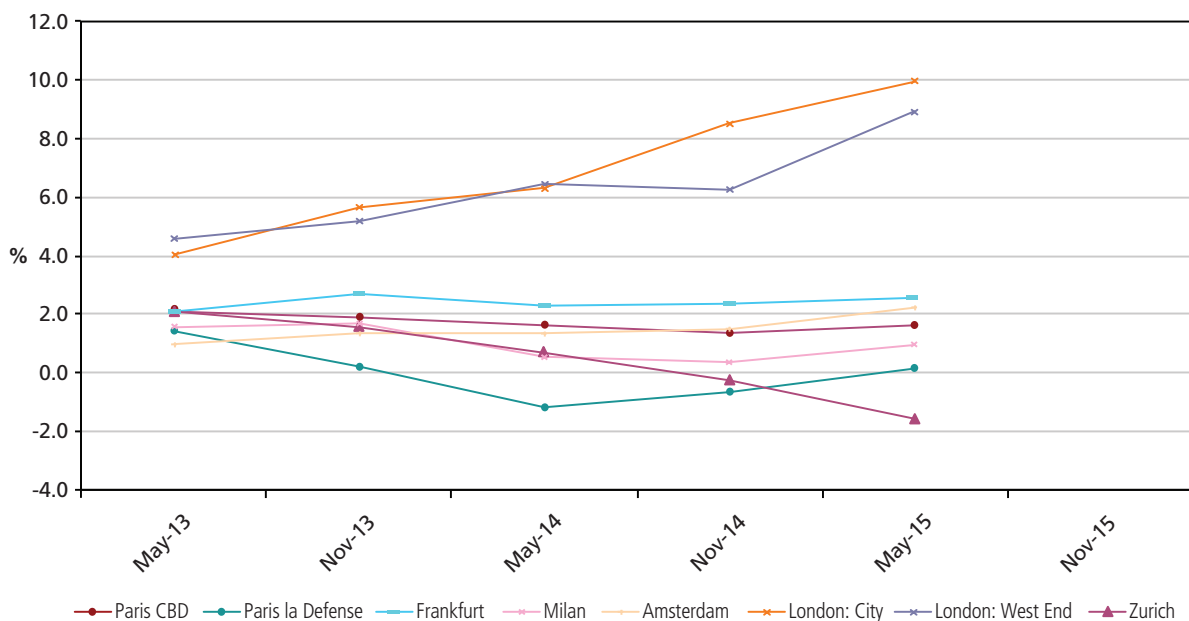
The remaining location expected to deliver negative growth in 2015 is Zurich at -1.6%, weakening from -0.3% in November.

Of those centres within the eurozone projected to deliver positive growth, in addition to Dublin, Madrid and Barcelona, the strongest expectations lie with Luxembourg (4.9% from 2.8% in November) and Munich at 3.0% (from 2.4%). For the remaining locations, all but Paris La Défense are expected to exceed 1.0% growth.

Outside the eurozone, prospects for growth have weakened compared to 2014 forecasts in five of eight locations, led by Moscow (-13.4%) and Zurich at -1.6%. Again, positive sentiment for the two central London markets is maintained with both expected to deliver increased growth of up to 9.9% (8.5%) in the City and 9.0% (6.2%) in the West End. The predicted growth rates for Copenhagen and Oslo have fallen to 0.7% and 1.8% respectively (from 1.4% and 2.0%), whilst for Stockholm the average rate has remained stable at 3.3%. Manchester's prospects have strengthened further to 4.6% (from 3.2% six months ago).

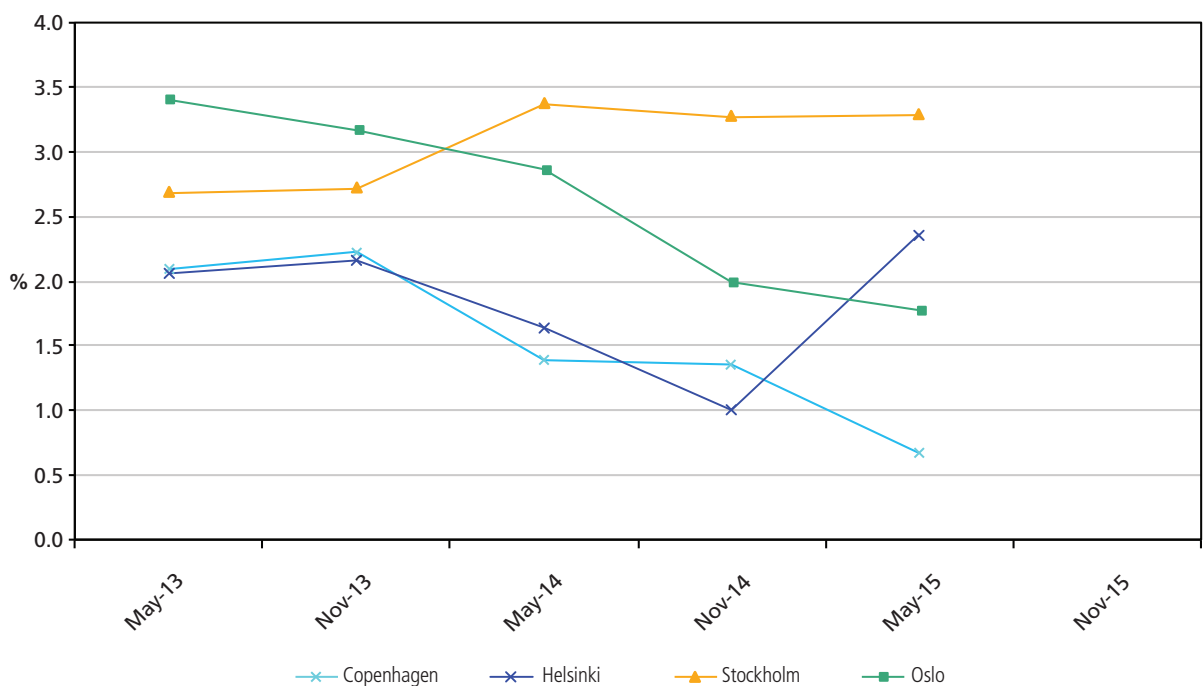
Figure 2: Weighted Average Rental Growth Forecasts 2015 – Non-euro zone Centres

Within the major financial centres, London, Frankfurt and Amsterdam are projected to achieve growth in excess of 2.0% in the current year, the latter being projected at 2.5% and 2.2% respectively. Rental growth rates in both Paris markets and Milan are expected to improve, reversing previous weakening projections.

Figure 3: Weighted Average Rental Growth Forecasts 2015 – Financial Centres

In the Nordic region, projections for Helsinki have resulted in a notable rise in average expectations, to 2.4% from 1.0% in November, despite a reported increase in the office vacancy rate. Both the Oslo and Copenhagen markets have continued to weaken (currently 1.8% and 0.7%), the former possibly reflecting continuing oil price uncertainty, which has resulted in a slowdown in the oil and offshore industry with consequent employee cutbacks.

Figure 4: Weighted Average Rental Growth Forecasts 2015 – Nordic Centres



Outlook for 2016 and 2017

Whilst all but one of the 30 centres are projected to deliver positive growth in 2016, forecasts have softened in almost half of these markets (14) over the last six months. In only five instances have forecasts improved by more than 1.0% over the half year since the last survey, these being for both of the Spanish and London markets and for Dublin. Despite this moderating of opinion amongst contributors, average growth expectations of 2.0% or more are recorded in 14 office markets, with Madrid moving ahead of Dublin in the rankings at 6.8% compared to 6.7%. The most improved market in 2016 may be Moscow, the projections for which average 1.2% (a 14.6% increase on 2015). However, the seven forecasters contributing data continue to hold widely differing opinions on the prospects for this market, ranging from 12.3% to -10.2% (the median figure being 0.0%).

The first forecasts for 2017 average 2.0% across all centres but range from a maximum of 6.1% for Madrid to 0.1% for Budapest. Contributors anticipate a continuation of the decline in growth rates, which extends to 19 centres, with the biggest possible reduction being in the Dublin market (from 6.7% in 2016 to 1.5% in 2017). However, the majority of weaker forecasts (12 of the 19) are currently projecting falls of less than 1.0% on 2016 figures.

Three and five-year average forecasts show markets in recovery

Only two of the **three-year** average forecasts indicate negative annual growth compared to seven in November 2014. Moscow and Warsaw continue to be the weakest projected markets, with average annualised rates of -2.8% and -1.2% respectively. In the six months since the last survey, 16 forecasts have improved by more than 1.0% per annum and, of these, eight by more than 2.0%.

Of the 28 markets averaging positive growth, only three (Zurich, Prague and Athens) may deliver less than a 1.0% improvement, whilst a further 13 are expected to deliver between 1.0% and 1.9% annually over the three years. For the remaining 12 locations, annual rental growth rates of between 2.0% (Luxembourg) and 7.1% (Dublin) are predicted. The table at Appendix 1 details individual market consensus forecasts.

With the exception of Moscow (averaging -0.2%), the **five-year** forecasts are positive for all centres. Average growth rates in 14 markets have improved since November, but only in two by more than 1.0% (Moscow and Paris La Défense). Of the 11 locations where average forecasts exceed 2.0% per annum, Madrid (5.7%) and Barcelona (4.5%) occupy the highest positions in this group, followed by Dublin (4.0%) and the City and West End of London markets (2.9% and 2.8%).

Conclusion

Whilst expectations in the near term for Dublin and the two London markets are robust and offer the best growth prospects in the current year, Madrid and Barcelona emerge as potentially strong centres of growth in the later years of the forecast period.

As indicated in the charts in Appendix 2, the three-year rolling averages fall within a band of predicted growth rates of nearly 10.0%, compared to just under 6.0% for the five-year averages, implying a gradual moderating of growth prospects over the medium term. Clearly, structural difficulties continue to impact on a large number of European economies and the very modest prospective improvement in rent levels in all but a few prime office markets signals little prospect of strong growth within much of the eurozone.

Appendix 1

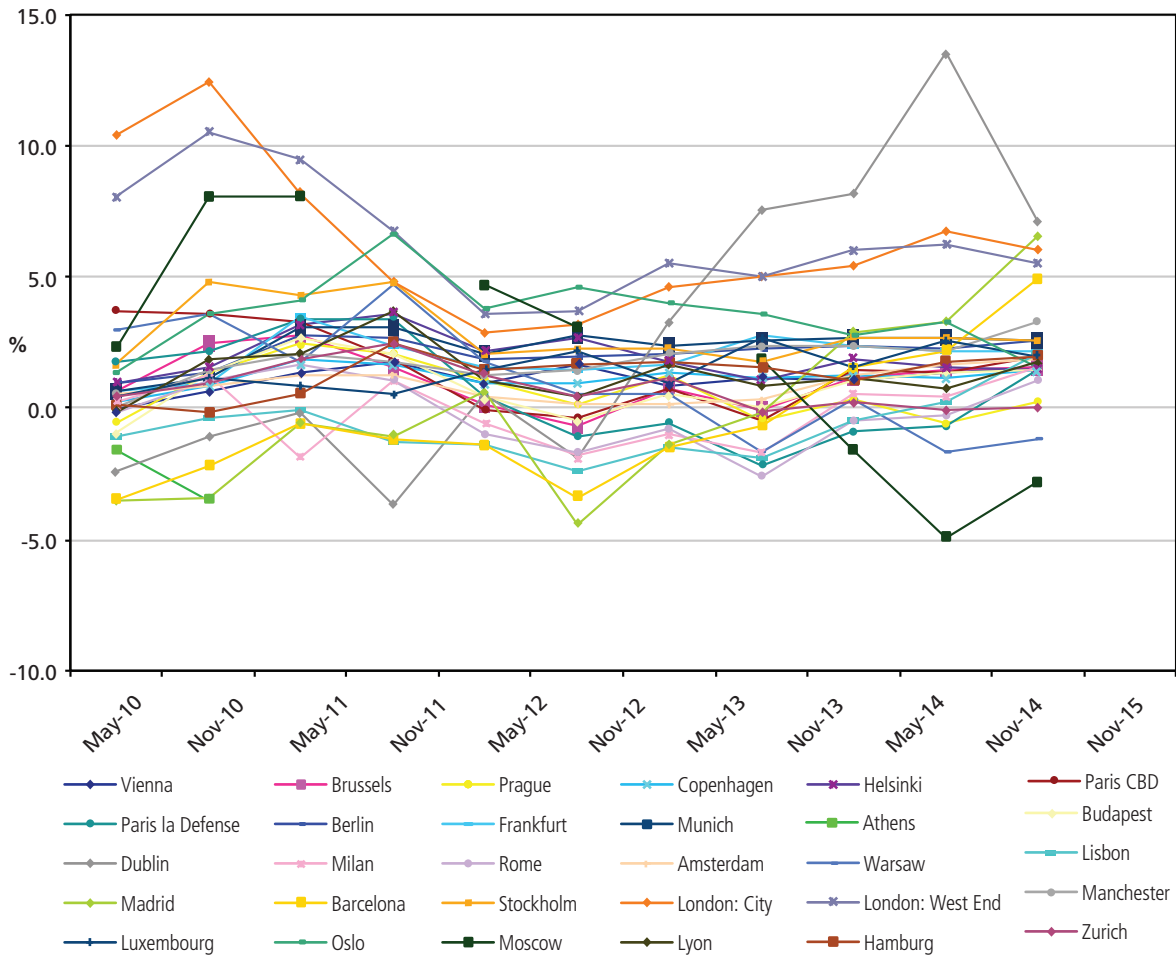
Table 1: Mean weighted rental value growth forecasts - May 2015

	Year weighted average rental growth forecast					Rolling 3-year average (2015-2017)		Rolling 5-year average (2015-2019)	
	2015		2016		2017				
Vienna	2.1	(1.4)	1.4	(1.6)	1.1	1.5	(1.3)	1.5	(1.4)
Brussels	2.3	(1.4)	1.5	(2.1)	0.8	1.5	(1.4)	1.7	(1.8)
Prague	-1.5	(-0.5)	0.6	(1.8)	1.8	0.3	(-0.6)	0.9	(0.8)
Copenhagen	0.7	(1.4)	1.5	(2.5)	2.1	1.4	(1.1)	1.7	(1.8)
Helsinki	2.4	(1.0)	1.4	(2.7)	0.6	1.5	(1.6)	1.8	(2.0)
Lyon	2.7	(0.7)	1.8	(1.7)	0.8	1.8	(0.8)	1.9	(1.3)
Paris CBD	1.6	(1.4)	2.2	(3.0)	2.0	1.9	(1.4)	1.9	(1.8)
Paris la Défense	0.2	(-0.7)	1.6	(2.0)	2.5	1.4	(-0.7)	1.8	(0.8)
Berlin	2.6	(2.1)	2.7	(2.6)	2.4	2.6	(2.3)	2.2	(2.3)
Frankfurt	2.5	(2.4)	2.7	(2.4)	1.2	2.2	(2.2)	1.8	2.0
Hamburg	1.6	(2.0)	2.2	(1.7)	2.1	1.9	(1.7)	1.6	(1.8)
Munich	3.0	(2.4)	2.6	(2.2)	2.0	2.5	(2.7)	1.9	(2.4)
Athens	-0.8	(na)	1.3	(na)	2.2	na	(na)	na	(na)
Budapest	2.8	(1.0)	1.5	(2.3)	0.1	1.5	(1.4)	1.6	(2.0)
Dublin	13.5	(10.5)	6.7	(5.6)	1.5	7.1	(13.5)	4.0	(9.0)
Milan	1.0	(0.4)	1.7	(2.4)	2.1	1.6	(0.5)	2.2	(1.7)
Rome	0.0	(0.1)	1.0	(1.6)	2.3	1.1	(-0.3)	1.6	(0.9)
Luxembourg	4.9	(2.8)	1.0	(2.3)	0.1	2.0	(2.6)	2.2	(2.0)
Amsterdam	2.2	(1.5)	2.0	(2.0)	1.4	1.9	(1.7)	1.9	(2.0)
Oslo	1.8	(2.0)	1.2	(2.8)	1.7	1.6	(3.3)	1.6	(2.8)
Warsaw	-3.3	(-1.7)	-1.3	(0.3)	1.0	-1.2	(-1.6)	0.3	(0.5)
Lisbon	1.1	(0.4)	2.4	(1.6)	2.8	2.1	(0.2)	2.1	(1.6)
Moscow	-13.4	(-4.2)	1.2	(0.9)	4.9	-2.8	(-5.0)	-0.2	(-2.0)
Madrid	6.8	(4.7)	6.8	(4.0)	6.1	6.6	(3.3)	5.7	(5.0)
Barcelona	5.0	(2.7)	5.5	(2.9)	4.3	4.9	(2.1)	4.5	(3.7)
Stockholm	3.3	(3.3)	2.4	(2.3)	2.1	2.6	(2.7)	2.5	(2.2)
Zurich	-1.6	(-0.3)	0.4	(1.3)	1.3	0.0	(-0.1)	0.6	(3.0)
London: City	9.9	(8.5)	5.6	(3.0)	2.7	6.0	(6.8)	2.9	(4.0)
London: West End	9.0	(6.2)	5.3	(3.8)	2.5	5.6	(6.2)	2.8	(3.3)
Manchester	4.6	(3.2)	2.8	(2.4)	2.6	3.3	(2.1)	2.3	(2.2)

Previous survey figures in brackets

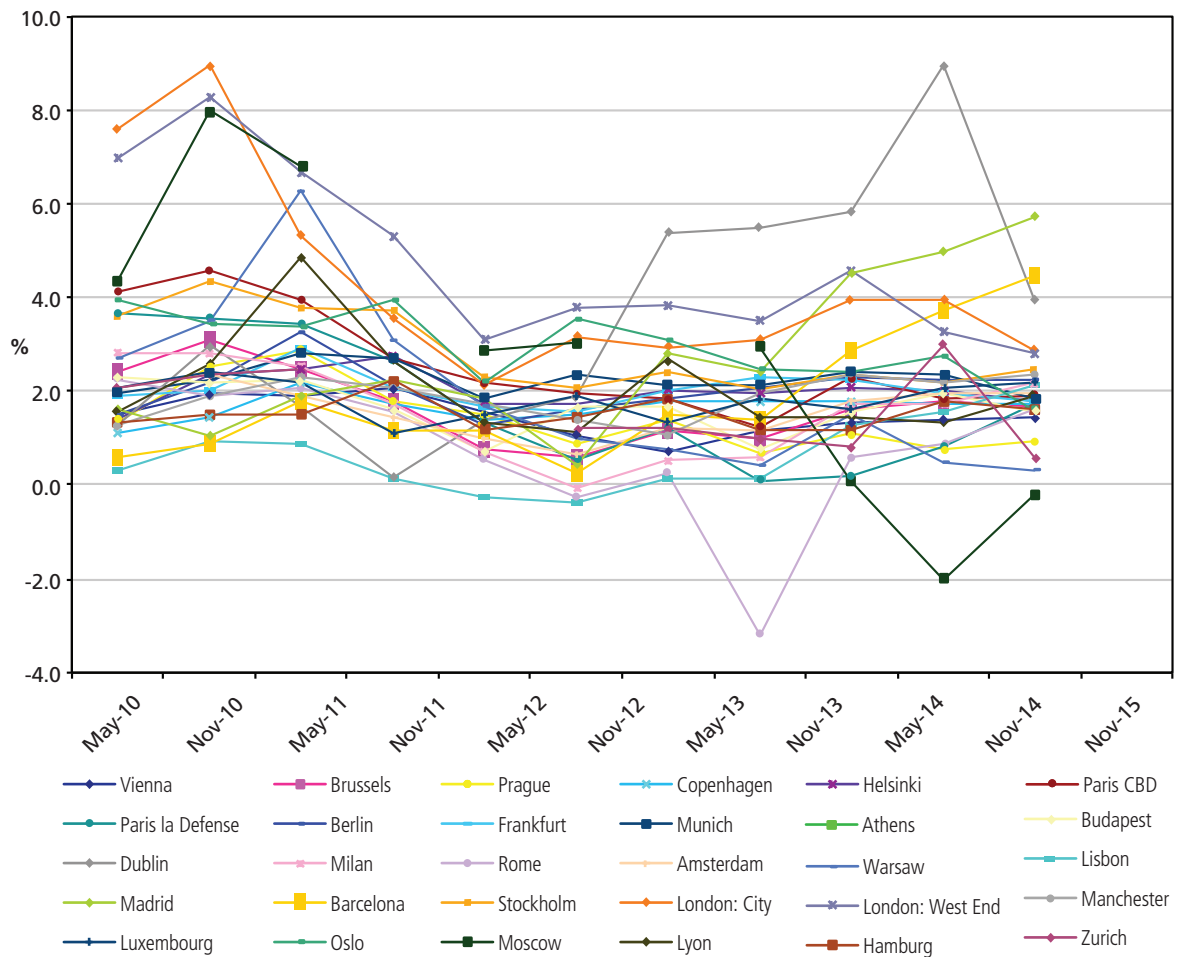
Appendix 2

Figure 5: Rolling three-year % weighted rental growth forecasts



Appendix 2

Figure 6: Rolling five-year % weighted rental growth forecasts



Acknowledgements

Forecast Contributors

IPF thanks all participants in the survey for contributing rental data to the May 2015 European Consensus Forecasts, including the following organisations:

Aberdeen Asset Management, AXA Real Estate, BNP Paribas Real Estate, Capital Economics, CBRE, CoStar Portfolio Strategy, Cushman & Wakefield, Danish Property Federation, DTZ, Invesco, JLL, LaSalle Investment Management, Rockspring, Standard Life Investments and TIAA Henderson Real Estate.

Notes

At present the IPF European Consensus Forecasts survey focuses on office rental value growth in major cities. It is not possible currently to assemble sufficient forecasts of all sectors across all European countries to produce a meaningful consensus of views, although our ambition is to extend and improve the scope of the survey.

In addition to the rental value forecasts, we run a consensus survey of forecast IPD European total returns by sector. The samples provided for this survey were once again insufficient to permit publication, as fewer than five forecasts were received for each sector/territory. We aim to produce a full release of this data at a future date, once the number of responses has grown to five or more.

The Data

This latest survey collected prime office rental forecasts for 30 centres for the calendar years 2015, 2016 and 2017. We request a three-year average forecast for 2015-2017 where individual years are not available, as well as a five-year average for 2015-2019. The survey requests both the percentage annual rental growth rates and also the year-end rent levels. The growth forecasts provided by each organisation are analysed to provide weighted average ('consensus') figures for each market. Figures are only aggregated and reported for office markets for which a minimum of five contributions are received.

The **definition of market rent** used in the survey is **"achievable prime rental values for city centre offices, based on buildings of representative size with representative lease terms for modern structures in the best location."** Prime in this case does not mean headline rents taken from individual buildings but, rather, rental levels based on market evidence, which can be replicated. All figures included in the survey are required to have been generated by formal forecasting models. This report is based on contributions from 16 different organisations (fund/investment management houses and property advisors).

Consensus forecasts further the objective of the Investment Property Forum to enhance the understanding and efficiency of the property market. The IPF is extremely grateful for the support those organisations that contribute to this publication, which is only possible thanks to the provision of individual forecasts.

The IPF welcomes new contributors for future surveys, so that the coverage of the market can be widened. If your organisation wishes to contribute to future surveys, please contact Pam Craddock, IPF Research Director at pcraddock@ipf.org.uk, tel. +44 (0)20 7194 7925.

Contributors receive a more detailed set of statistical outputs than those shown in Appendix 1 – for each office centre the sample size, median and range of rental values are also provided.

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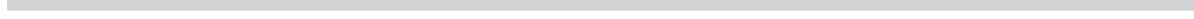
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