Q3 2017: Global Commercial Property Monitor

Capital value expectations remain most elevated in Europe

- European markets continue to post strongest underlying results
- Sentiment improves in China but remains flat in the US
- Conditions appear closer to stabilising in Brazil

The Q3 2017 RICS Global Commercial Property Monitor results show a continued, steady improvement in sentiment across the majority of markets covered by the survey. Overall momentum remains positive, both on the occupier and investor sides, in around two thirds of the countries tracked. Furthermore, although respondents remain cautious on the outlook in some areas, these negative trends have diminished to a certain extent when compared with earlier in the year.

The headline Occupier Sentiment Index* rose or turned less negative in 22 of the 32 national markets tracked, relative to the average readings over the previous two quarters (chart 1). On this measure, occupier market momentum remains firmest in Europe and, in particular, across CEE markets. Indeed, Hungary, Czech Republic and Bulgaria (accompanied by Spain and Portugal) recorded the strongest five OSI readings during Q3. This significant rate of improvement is in keeping with robust economic growth across these nations, with each posting an annual rate of GDP growth around, or in excess of, 3%. Smartly rising economic output is driving occupier demand higher and supporting elevated rental growth expectations in each instance. In further evidence of an increasingly widespread upswing in Europe, sentiment has now turned comfortably positive in Greece, where the revival in occupier demand has accelerated over the past two quarters, pushing near term rent expectations positive in all sectors.

With respect to the Investment Sentiment Index (chart 2), the top twelve national readings globally were all registered in Europe. Germany moved to the top of the pile in Q3, with Berlin and Frankfurt both seeing a surge in investment enquiries, while Munich also saw a strong (albeit more modest in comparison) rise in investor demand. Although a majority of respondents in Germany sense conditions are likely close to peaking in the current cycle, strong capital value growth is still anticipated across each of these cities over the next twelve months. Similarly, strong investment demand growth is outstripping that of supply (in net balance terms), producing firmly positive capital value expectations in Budapest, Dublin, Lisbon, Bangalore and Sofia.

By way of contrast, the backdrop remains challenging in Dubai, with respondents submitting negative projections for both capital values and rents for the year ahead. Rising supply is coming against softening demand, as the UAE economy continues to adjust to lower oil prices and a reduction in oil output. Notwithstanding this, capital values are expected to prove more resilient for prime assets and hold steady over the coming twelve months. Elsewhere, a few markets across Asia continue to return cautious feedback. Indeed, the largest share of contributors in Singapore, Indonesia and Malaysia sense the commercial real estate sector remains in the downturn phase of the current property cycle.

However, while these markets continue to struggle, near term momentum did improve in China during Q3. Both occupier and investment demand growth accelerated and, despite concerns of oversupply in some parts, capital values and rents are expected to rise firmly over the year ahead. Respondents across Shanghai envisage slightly more modest capital value gains when compared to the national average, although this is a result of some noticeable underperformance expected in secondary markets. In Beijing, the retail sector is seen posting stronger capital value gains than the China-wide figures, while the outlook is more subdued for the industrial and office sectors.

In India, current momentum remains somewhat modest with headline investor and occupier demand edging up only marginally during Q3. When disaggregated, the latest results point to Bengaluru seeing stronger growth than both Mumbai and the National Capital Region. Even so, going forward, respondents remain confident that capital values and rents will rise across all three areas over the coming twelve month and gain momentum at the three year time horizon.

Meanwhile, the outlook appears a little stagnant in the US, with all-sector average capital value and rental growth projections more or less flat twelve months out. That said, it is the retail sector weighing heavily on the headline picture, while the industrial sector displays solid expectations. In New York, respondents continue to express concerns over valuations, as around 80% feel the market may be overpriced relative to fundamentals.

Finally, conditions are showing further signs of stabilising in Brazil, as both OSI and ISI readings moved into neutral territory during Q3. In fact, this marks the first quarter since 2012 in which neither of these measures was negative. Even so, this improvement has been driven by a fall in supply across the market, rather than a significant pick-up in demand. In keeping with the somewhat mixed picture nationally, contributors' opinions are divided as to whether the market is in the late stages of a downturn, at the bottom of the cycle, or at the beginning of a recovery. However, in Sao Paulo, the largest share of respondents do now sense the market has started to recover. For now, this appears to be concentrated in the prime office and retail sub-sectors, which are the only two categories expected to see capital value growth over the year ahead.

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

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

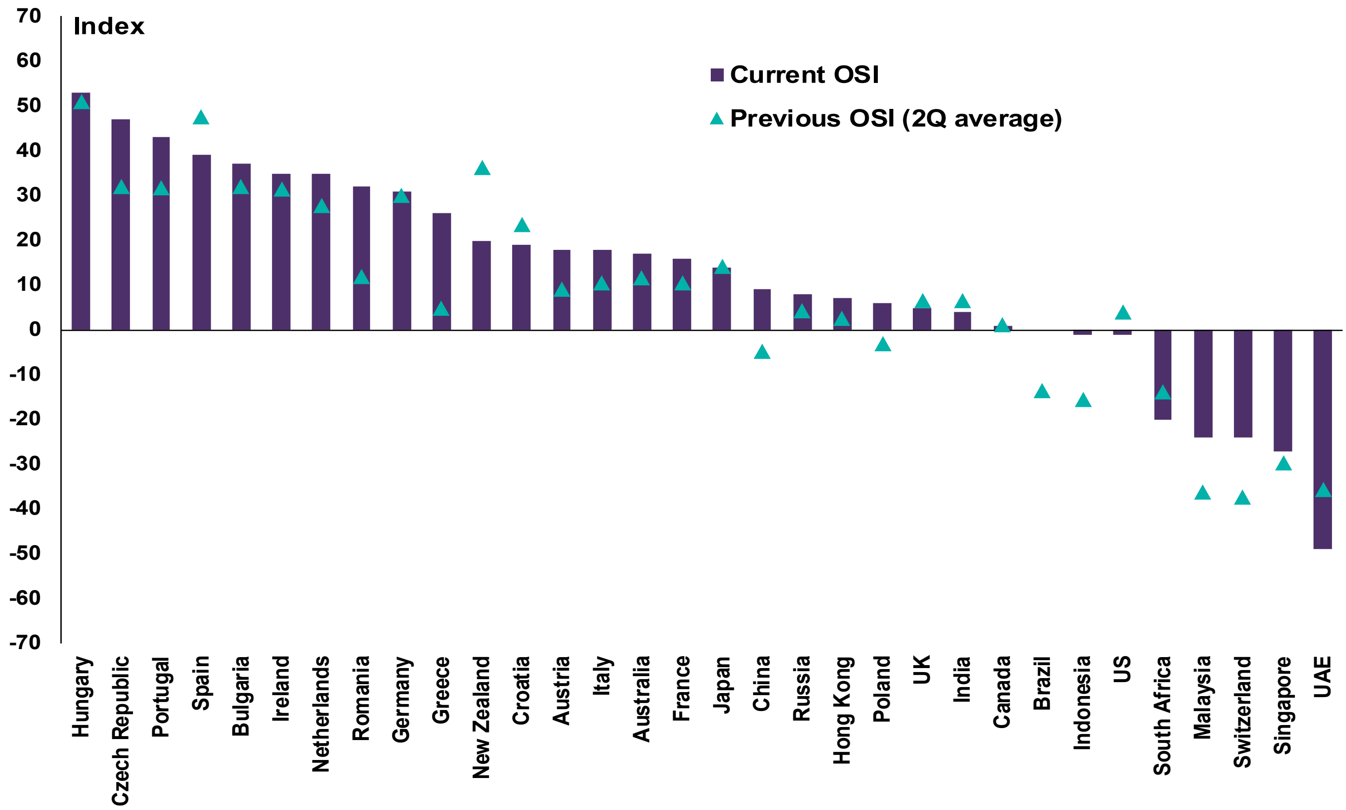


Chart 2 Investment Sentiment Index (change v previous qtr) - Net balance %

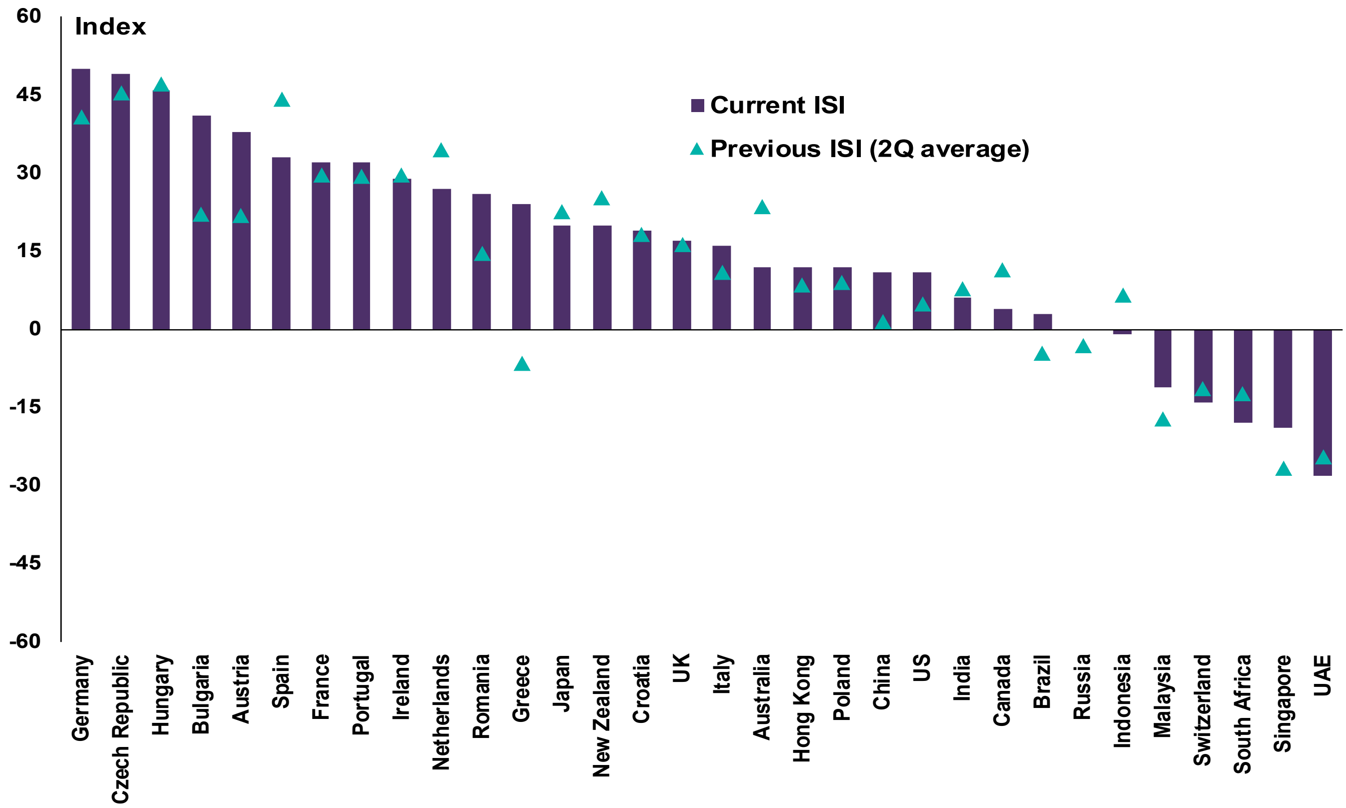


Chart 3 City Level Occupier and Investor Sentiment Indices- All sectors (net balance %)

Indicative of momentum over the previous quarter

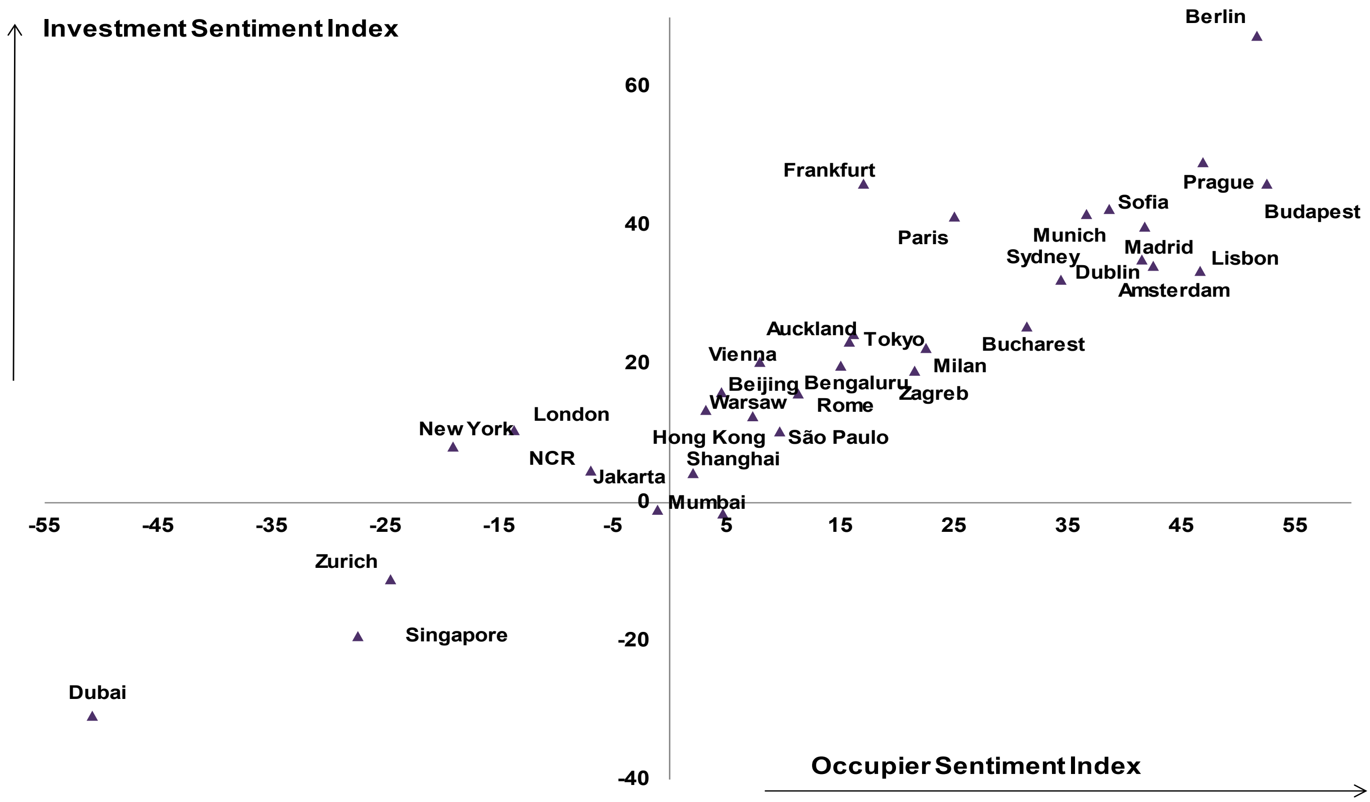


Chart 4 City Level Twelve Month Rental and Capital Value Expectations All sectors (net balance %)

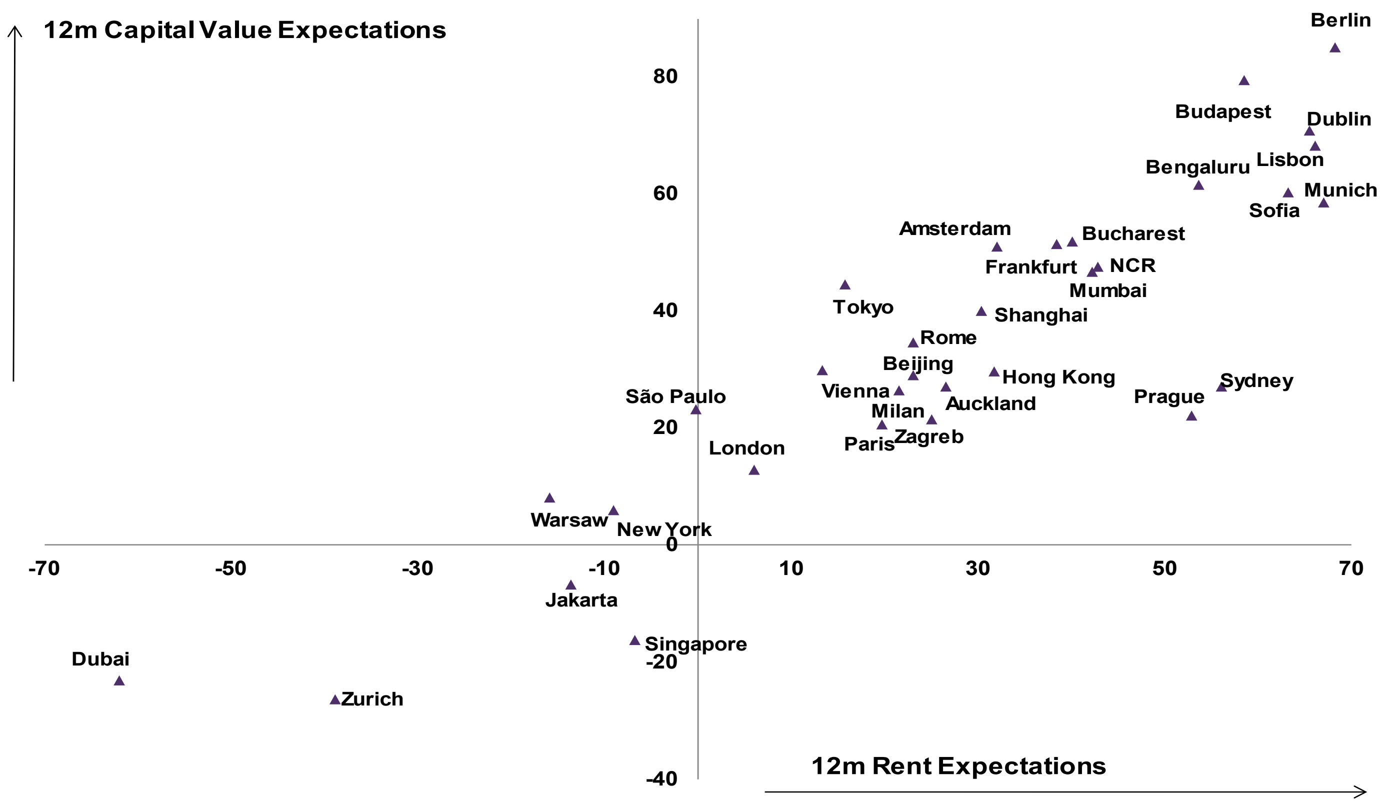


Chart 5 Valuations Perceptions

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

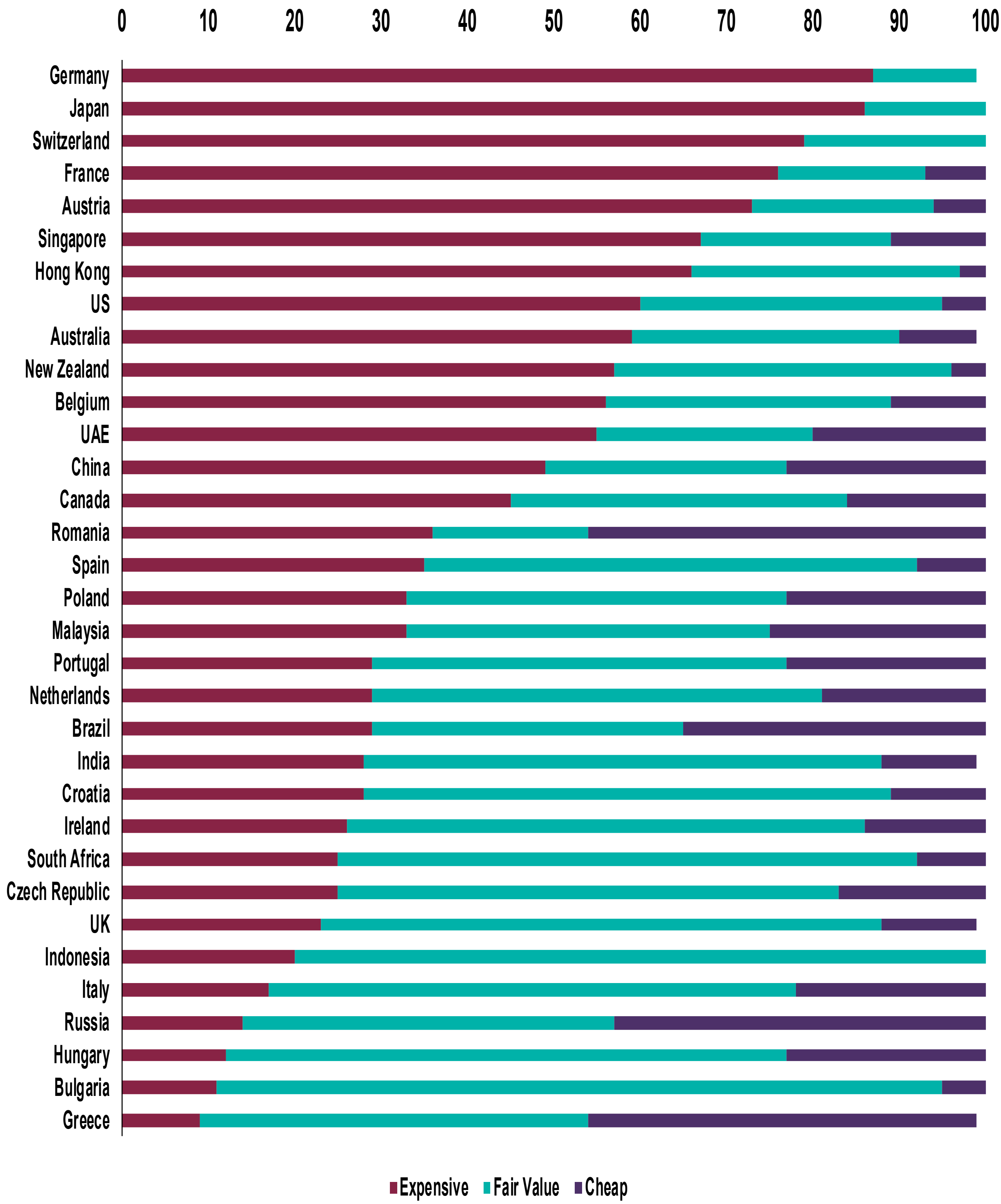
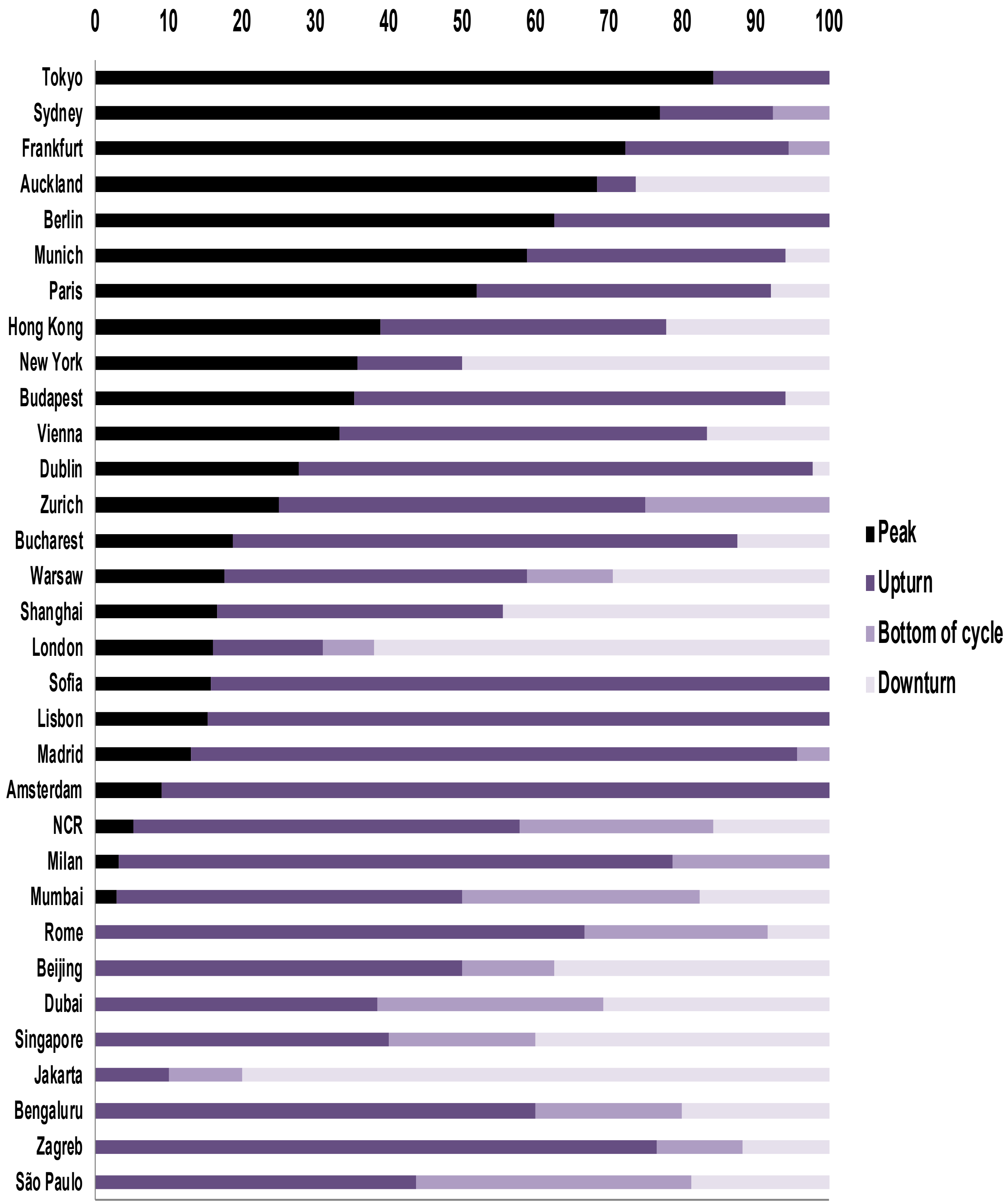


Chart 6 Property Cycle

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



Information

Global Commercial Property Monitor

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

Methodology

Survey questionnaires were sent out on 13 September 2017 with responses received until 6 October 2017. Respondents were asked to compare conditions over the latest three months with the previous three months as well as their views as to the outlook. A total of 1609 company responses were received, with 347 from the UK. Responses for Ireland were collated in conjunction with the Society of Chartered Surveyors Ireland. Responses for Spain and Portugal were collated in conjunction with Iberian Property. Responses for New Zealand were collated in conjunction with Property Council New Zealand.

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

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

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

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