Q2 2018: Global Commercial Property Monitor

Supportive occupier trends underpin global real estate markets

- Tone of Q2 results remain generally positive in the majority of markets surveyed
- European cities still recording the strongest momentum with expectations also firm in India
- Concerns over valuation little changed over the quarter

The strong start to the year for commercial real estate reflected in the actual volume of investment activity looks likely to have persisted through the second quarter on the basis of the results for the latest RICS Global Commercial Property Monitor (GCPM). This shows that in around three-quarters of the countries included in the survey, the headline Investment Sentiment Index* (ISI) was in positive territory, a roughly similar proportion to the Q1 results (Chart 2). The ISI effectively captures feedback from respondents regarding the momentum of key indicators in the market.

Critically at an aggregate level, the generally firm investment market countinues to be underpinned by a supportive occupier environment. The Occupier Sentiment Index* (OSI) shows broadly the same proportion of markets displaying positive results (Chart 1). The resilience of this indicator comes in the face of growing trade tensions and increasing uncertainty as to how the rise in protectionist policies will play out for the global economy.

At one level, the extended nature of the current real estate cycle could leave markets more vulnerable to any industry specific or macro shock. However, valuation perceptions (Chart 5) have changed little in recent quarters and even in those markets where this is more of a concern, expectations for capital growth largely point to a soft landing rather than anything more damaging.

In terms of broad regional peformance, the momentum once again appears strongest in parts of Europe despite sign of slowing growth in the eurozone. In terms of current conditions, the underlying picture is firmest in markets such as Amsterdam, Budapest, Lisbon, Madrid and Frankfurt (Chart 3). Moreover, in most cases the solid tone is replicated in the twelve month expectations indicator (chart 4). The notable exceptions to the positive European story are the results from Zurich and Geneva, which continue to be consistent with a fairly flat picture, and London. Something in the region of three-quarters of respondents from the UK's capital view the market as being in a downturn.

The feedback for the Asia-Pac region remains generally upbeat although the forward looking indicators are typically stronger than the current ones. This is particularly true in India where Bengaluru, Mumbai and NCR all score strongly on one year projections. Significantly, economic growth surged in the first quarter in India (7.7%) helped by a strong contribution from government spending with improving underlying fundamentals suggest this firmer pace should be sustained, at least through the second half of the year. Rent and capital value expectations are both buoyant with occupier demand continuing to strengthen and little sense that any of these markets are close to peaking.

Other cities in the region where sentiment is positive include Hong Kong, Melbourne, Sydney and Tokyo. The former has seen a material improvement in recent quarters following a couple of years where the readings were negative, albeit only modestly so. A better run of macro data has been supportive and is reflected in the stronger tone to tenant demand which is fueling an uplift in rent expectations. Meanwhile, data for Melboune and Sydney show tenant demand continuing to run ahead of availability and is consistent with other reports suggesting vacancy rates to be at historically low levels. From the investor standpoint, both these Australian markets are viewed as being dear and either at the peak of the cycle or the early phase of a downturn. Nevertheless capital values are still anticipated to be higher in a year's time. Sentiment towards real estate in Singapore was little changed over the quarter and a pretty similar story was also evident in Shanghai.

The US results continue to show some disparity between the feedback from New York and the rest of the country. The ISI for the latter remains in positive territory although the OSI was little changed. In contrast for New York both indicators are marginally negative. The divergence in sentiment is particularly evident in the responses to the question regarding perceptions as to the 'point in the cycle' the market is currently at. For the US ex-New York, the lionshare of contributors view the market as being either mid-upturn or in the peak phase. For New York, the results overwhelmingly point to the market being in a downturn with respondents projecting modest declines in capital values. In Brazil, sentiment has held steady over the quarter despite a further round of political instability.

Once again, the feedback from key real estate centres in the Middle East remain cautious despite the recent uplift in oil prices. For Dubai, Doha and Abu Dhabi, the tenant demand indicator is continuing to soften as availablity rises, leading to concerns around oversupply which is picked up in the anecdotal remarks of respondents.

The latest results continue, at an aggregate level, to show outperformance from office and industrial space with retail lagging, particularly secondary units. Indeed this is the one segment of the market where both rent and capital value expectations (unweighted averages) are negative. Exceptions to the weaker retail results are to be found in India, Hong Kong (which picked-up over the quarter) and some smaller European markets.

*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 %

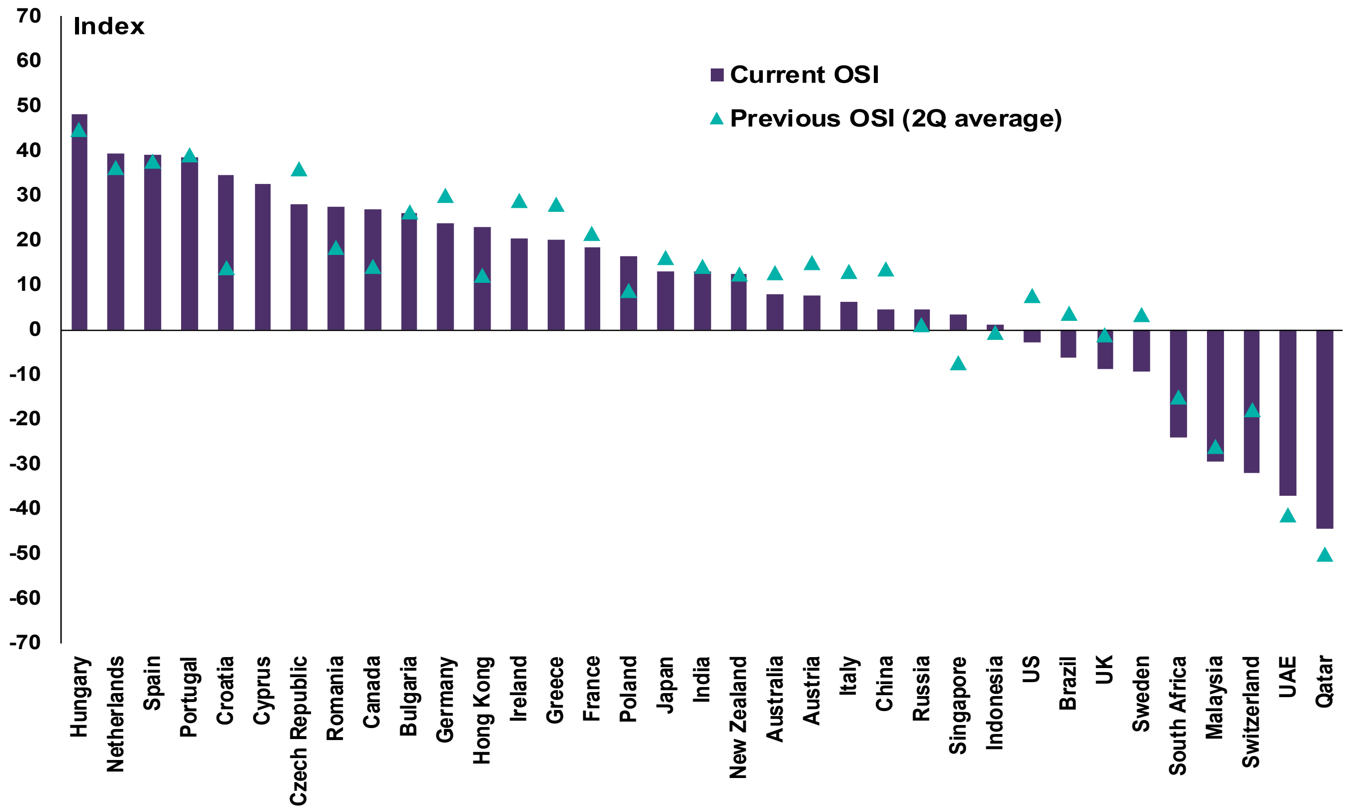


Chart 2 Investment Sentiment Index (change v previous qtr) - Net balance %

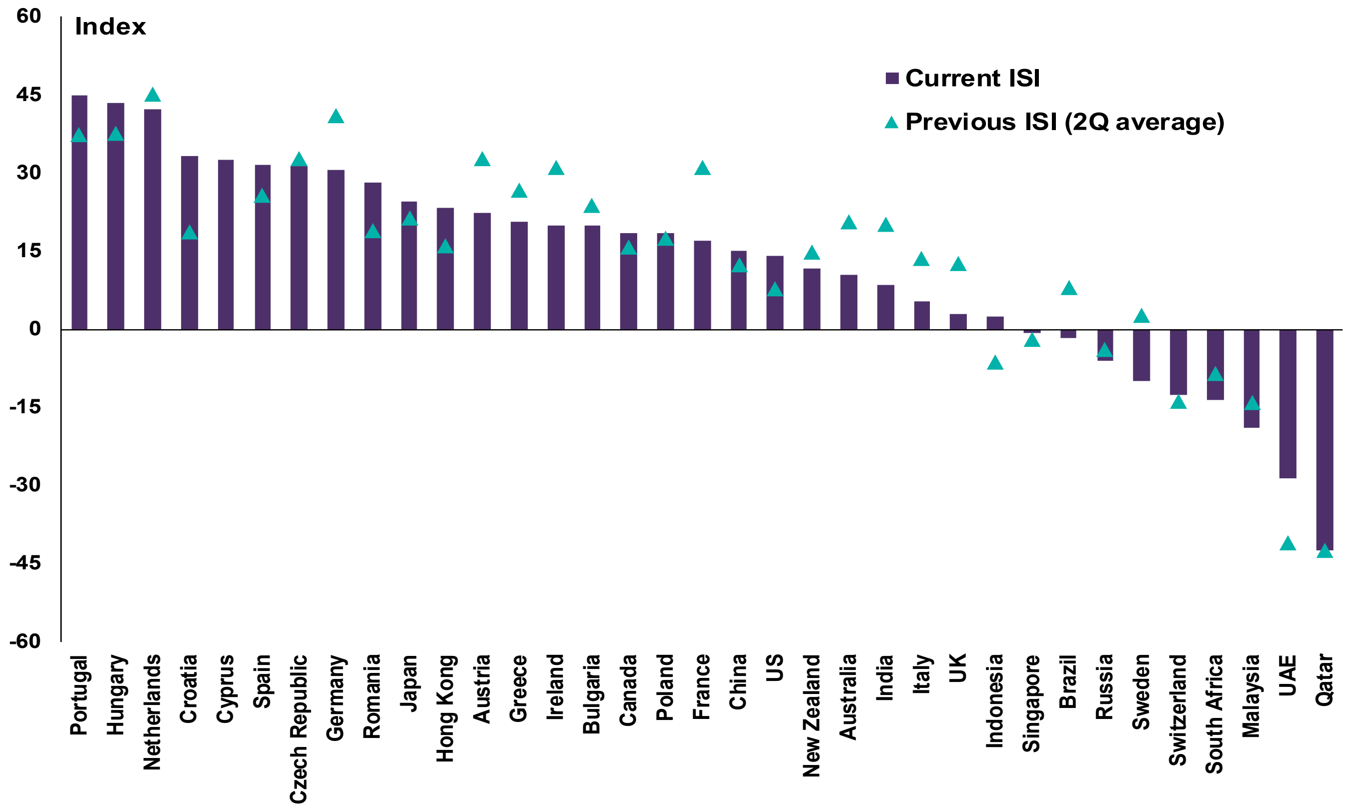


Chart 3 City Level Occupier and Investor Sentiment Indices- All sectors (net balance %)

Indicative of momentum over the previous quarter

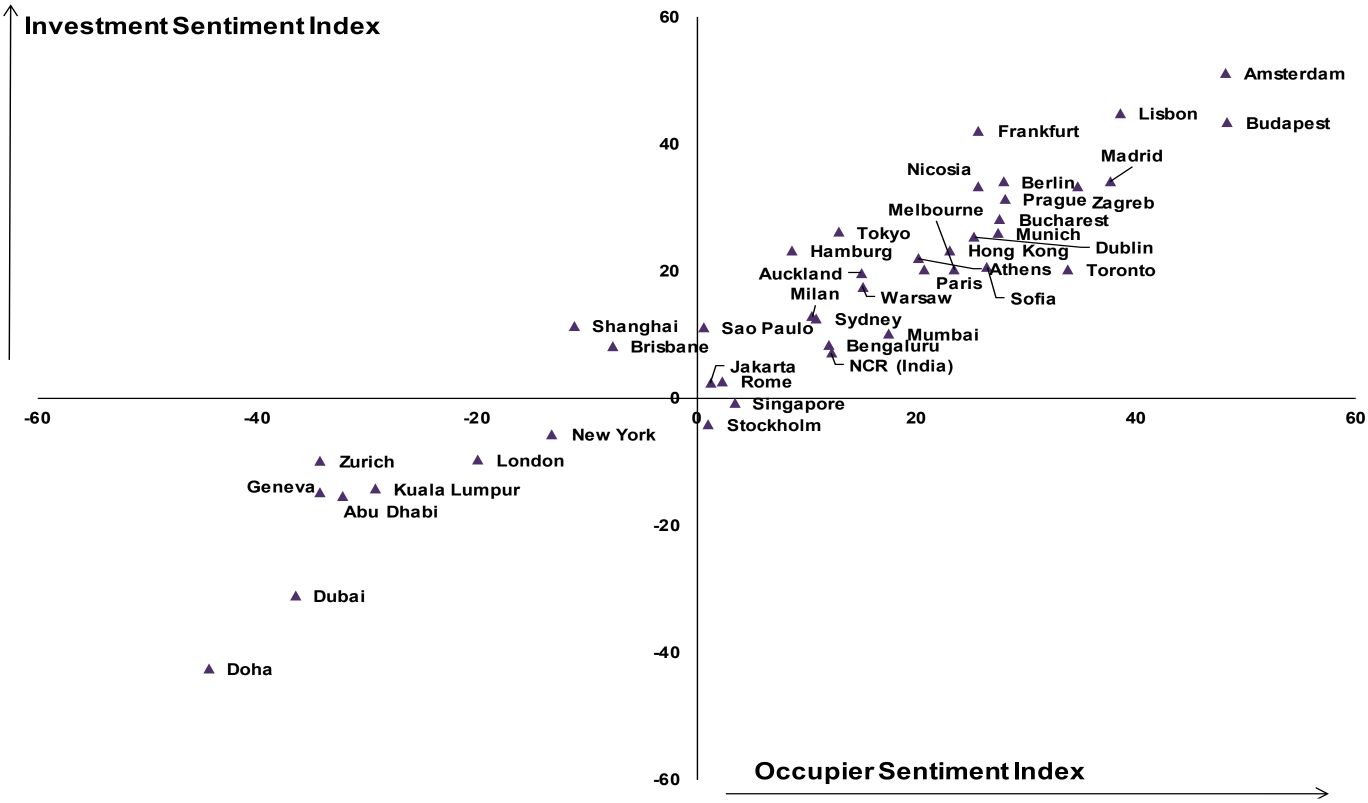


Chart 4 City Level Twelve Month Rental and Capital Value Expectations All sectors (net balance %)

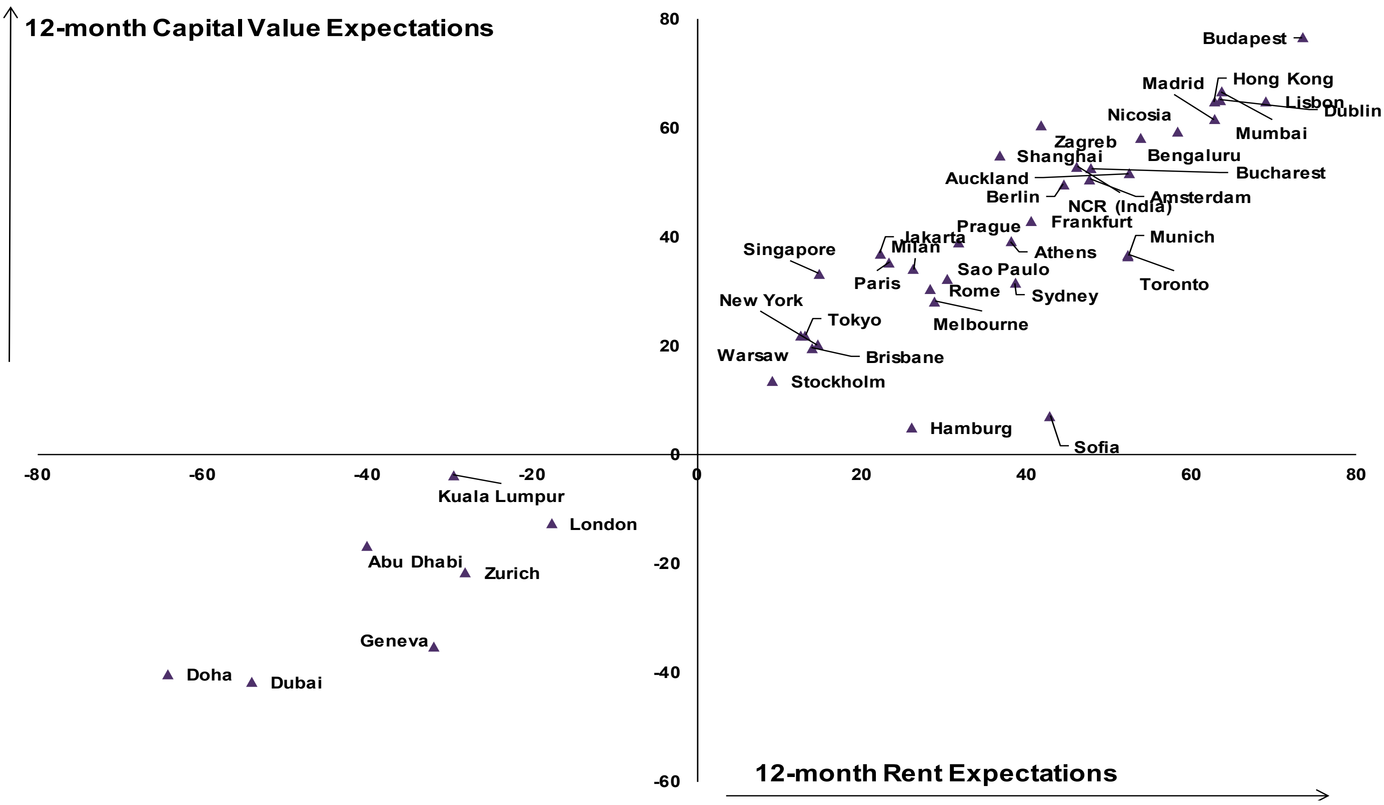


Chart 5 Valuations Perceptions

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

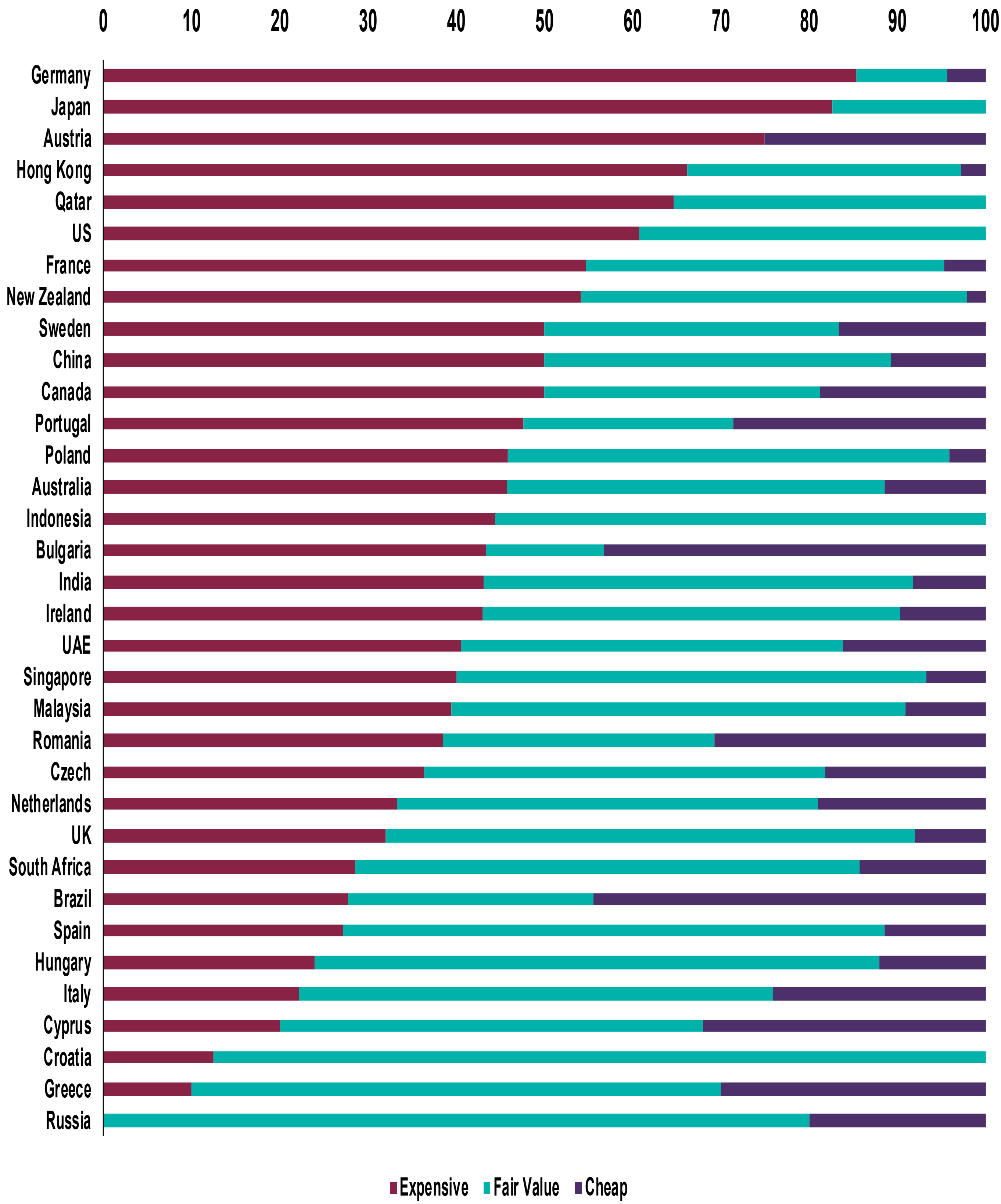
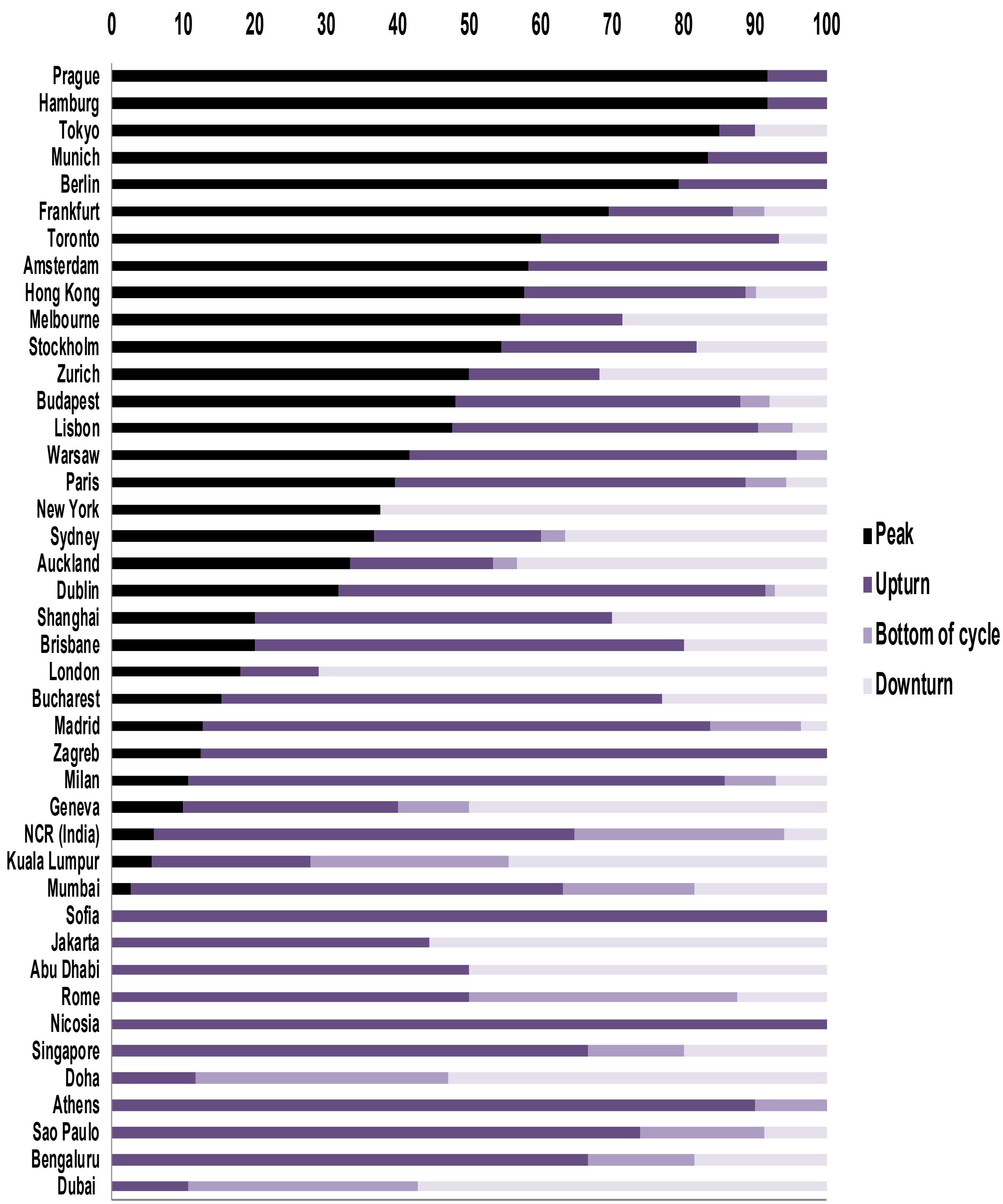


Chart 6 Property Cycle

% 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 June 2018 with responses received until 8 July 2018. 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 1965 company responses were received, with 385 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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