BRICKVEST

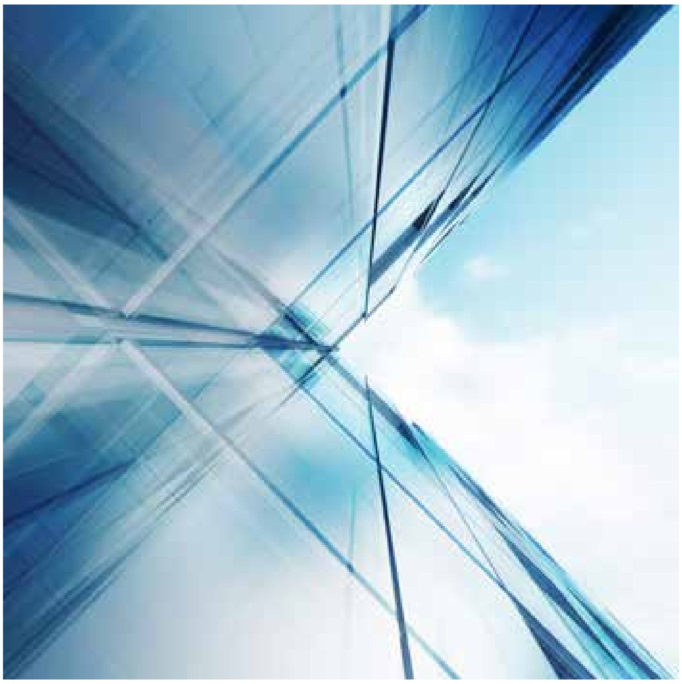
COMMERCIAL REAL ESTATE **TRENDS 2018**

MARKET RESEARCH & SURVEY

INTRODUCTION

BrickVest has polled over 4,500 investors and 600 deal sponsors with a combined AUM of €446bn to bring together one of the largest commercial real estate surveys focussing on commercial real estate investment in 2017 and 2018.

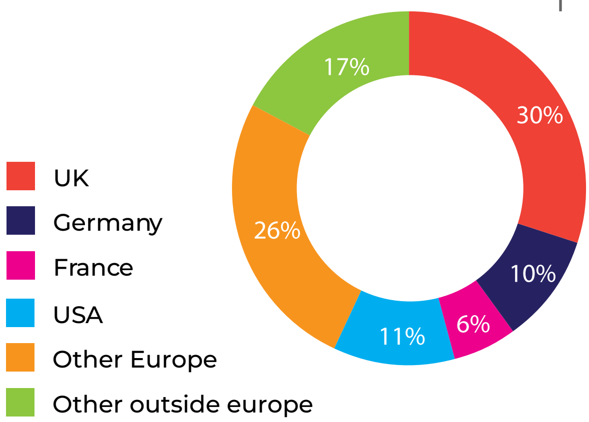
Real Estate continues to be attractive to investors, with more money being allocated to this asset class in the current economy of lower returns and higher volatility. This report focuses on investment strategies of deal sponsors as well as identifying where investors are looking to place their money.



SPONSORS PANEL

600+ international sponsors polled on a quarterly basis

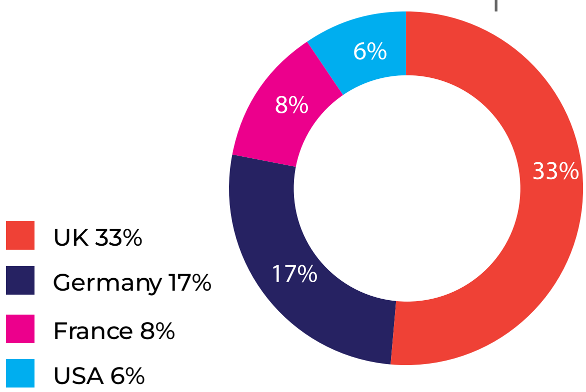
Deal sponsors panel composition



INVESTORS PANEL

4500 international investors polled on a quarterly basis

Investors panel composition



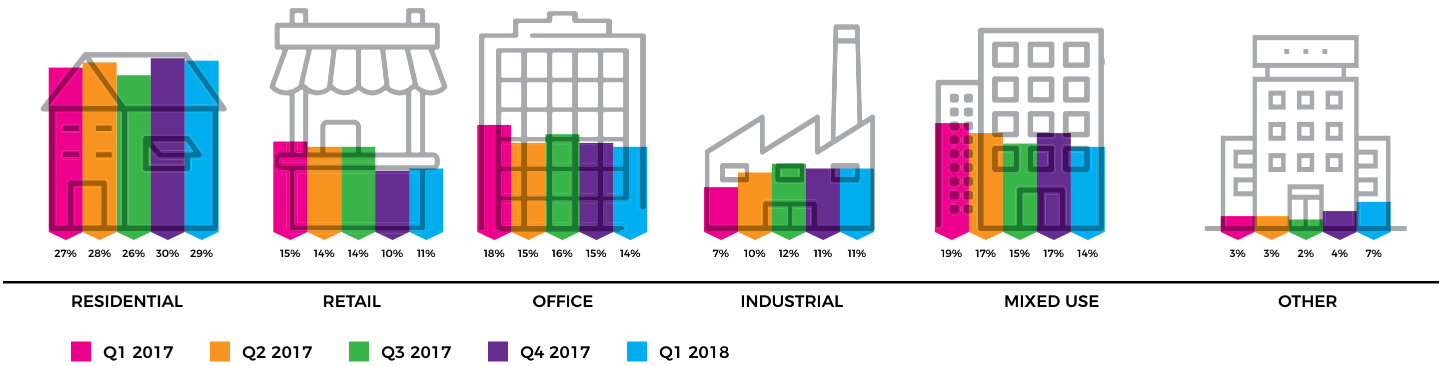
ASSET CLASS PREFERENCES

Last year $698 billon transacted in the global real estate market across all asset classes.

Our poll of over 600 deal sponsors highlights that residential assets remain at the top spot as the preferred asset class. Retail, office, industrial and mixed-use assets have broadly similar levels of interest, albeit there have been slight fluctuations in sponsor preference over the time period Q1 2017 to the end of Q1 2018.

The data shows that office assets are slightly less favoured, by all sponsors, than they were 18 months ago, and there is a greater focus on industrial assets than at the start of 2017. Deal Sponsors with AUMs under £100m have a preference towards residential real estate when compared to those with AUMs over £1bn who have identified Industrial as their main target in 2018.

Deal sponsors asset class preference quarterly 2017-2018



RESIDENTIAL

Residential assets have been an attractive asset class throughout 2017 and into 2018 with prices broadly across Europe rising. Sponsors have turned towards the real estate residential 'alternative' sectors including, student accommodation, retirement housing and private rented schemes, initially because of yield compression in the other asset classes and now they are a popular focus as sponsors look to increase their property returns.

RETAIL

Retail asset focus has fallen slightly in the past 12 months. The retail market has struggled with high profile company collapses, uncertainty over the future of the traditional high street retail units and weakening consumer confidence. Forecasts by PwC for UK consumer spending growth indicate that it will fall from 1.6%, achieved in 2017 to 1.1% in 2018. Rental growth is expected to be limited as more retailers move to further towards omni-channel sales strategies, albeit for the right unit in the right location, there will be occupier demand and rental growth.

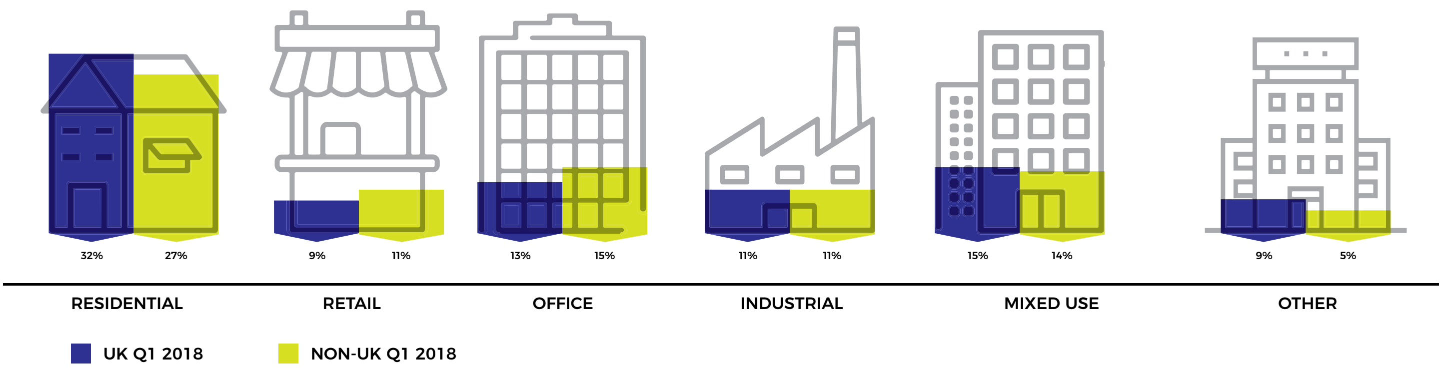
INDUSTRIAL

Industrial and Logistics assets have achieved high capital growth with increasing rental levels and strengthening yields. Our poll has highlighted the trend towards industrial assets increasing as the AUM of the deal sponsors increases. This asset class is particularly attractive due to the strength of the occupier market. Jones Lang Lasalle have stated that in Q4 2017, the overall vacancy rate of the European logistics market was less than 5.0% and is currently trending downwards. The nature of the retail market is also supporting the industrial and logistics market as demand for distribution warehouse space increases.

UK/NON UK SPONSORS

When comparing UK deal sponsors with non UK deal sponsors there are differences in preferences towards the asset classes. UK deal sponsors have a preference for residential and mixed use assets and we have seen this trend growing over the past 18 months whereas commercial assets, including office, retail and industrial assets are favoured more amongst non-UK deal sponsors.

UK/Non-UK deal sponsors asset class preference - Q1 2018



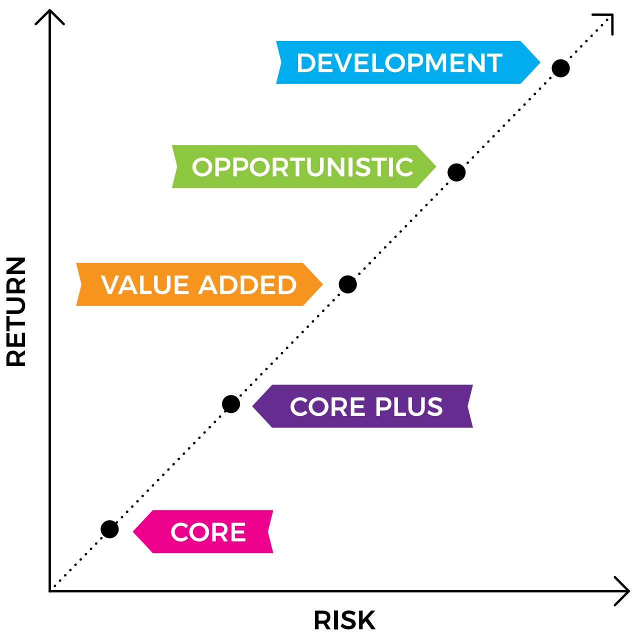
INVESTMENT STRATEGIES

Our deal sponsors and investors are polled on their investment strategies in order to determine where their focus lies and their tolerance for risk.

In conjunction with the opinion polls, BrickVest undertakes a Sponsor and Investor Risk Appetite Index analysis, focussing on how risk appetite changes over different time periods for sponsors in different locations and with different AUM's; as well as investors across the globe.

We asked investors and deal sponsors to identify which of the following categories they are targeting.

Real estate investment strategies



CORE:
Usually unleveraged, with a low risk, low return strategy

VALUE ADDED:
Considered as a medium to high risk , medium to high return strategy

OPPORTUNISTIC:
A high risk and high return strategy with leverage

DEVELOPMENT:
Development of land or buildings with varying risk and return profiles

RISK APPETITE

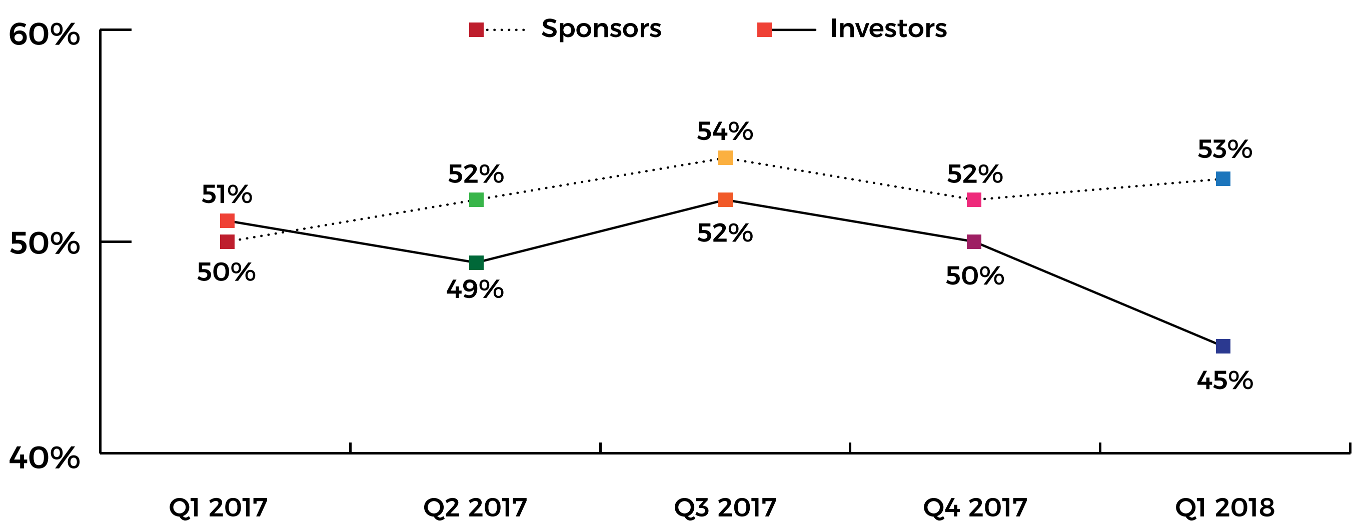
Deal sponsors of all different AUM categories have become marginally less risk averse from Q1 2017 to Q1 2018.

When comparing risk appetite in the UK to non UK deal sponsors, the analysis indicates that the non UK deal sponsors are more risk averse than the UK deal sponsors during the time period from Q1 2017 to Q1 2018. Given that certain locations are considered to be at full capacity and competition for core assets is continuously growing, Sponsors are looking further up the risk curve in order to obtain higher returns and deploy their capital. Sponsors that are non UK based have a higher desire for value add strategies than UK based deal sponsors, where as UK sponsors are targeting opportunistic and development investment strategies - higher along the risk curve.

On the other hand the investor risk appetite analysis suggests that overall, investors have reduced their appetite for high risk opportunities and are targeting low to moderate risk investments and this is demonstrated in countries such as the UK, the US and France. This trend is not mirrored by investors from Germany who have indicated that they are looking at the high risk, opportunistic and development strategies, which perhaps gives a demonstration of the consumer confidence and the current German real estate market.

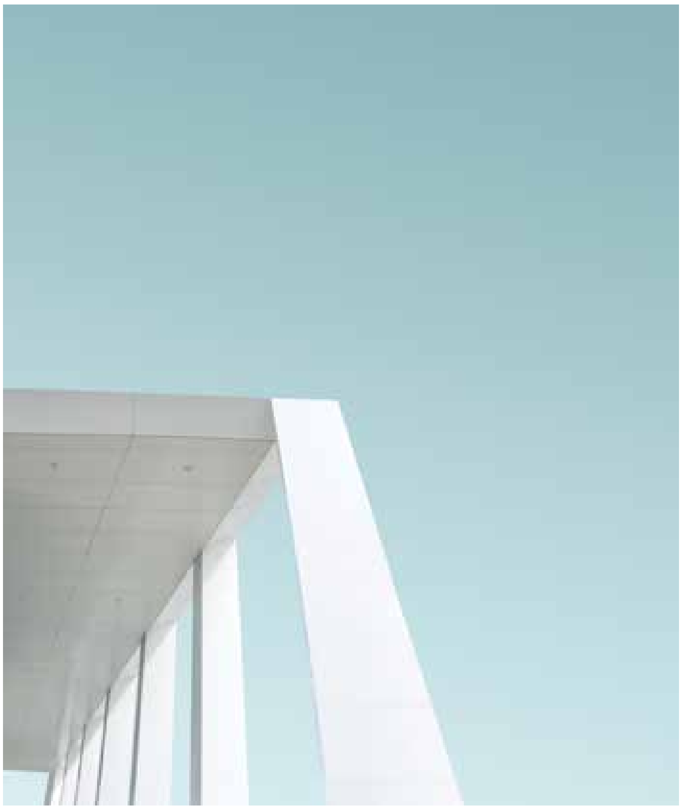
There is perhaps a slight misalignment between the investment strategies that deal sponsors are targeting and those that are being targeted by investors. It is important for deal sponsors to consider which investors are looking to target the same strategies as themselves.

Compared deal sponsors and investors risk appetite - quarterly 2017-2018



Risk is calculated on a scale from 0 (low risk - income) to 100 (high risk – capital).

STRATEGIES

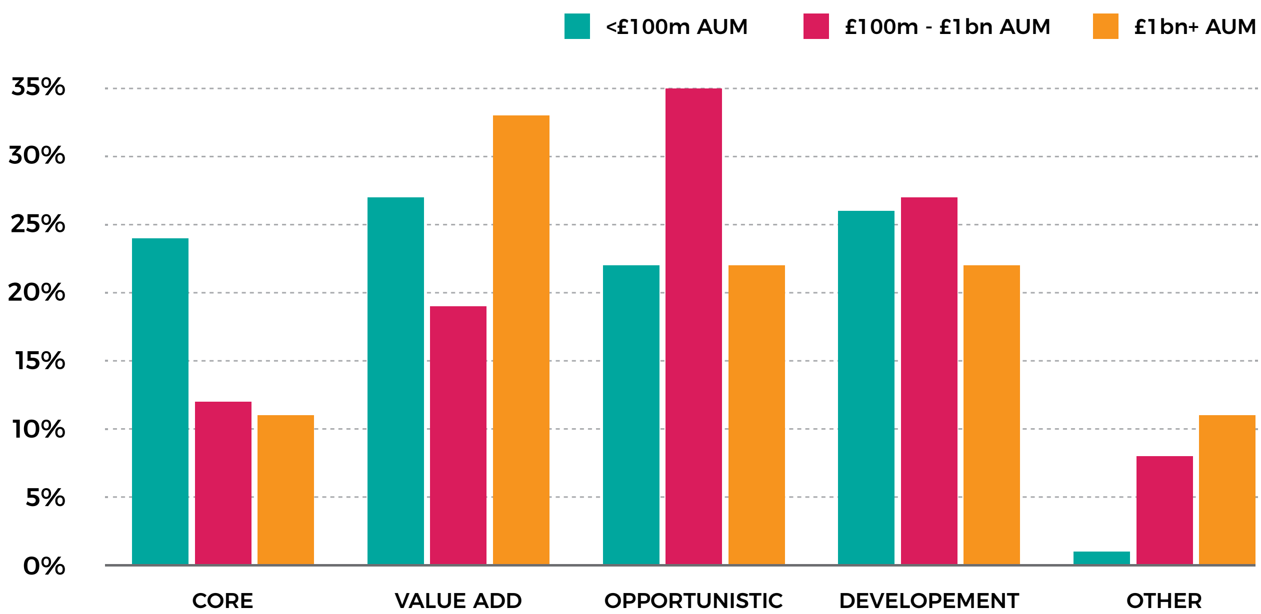


Across all deal sponsors, there are similar weightings to all the identified strategies.

With many sponsors under pressure to deploy capital and grow their AUMs, different investment strategies are under review in order to generate investment growth. Value add real estate opportunities are favoured by the largest deal sponsors and this category has grown on a y-on-y basis.

Core focus has remained largely stable, albeit is currently the least targeted by deal sponsors with over AUM £1bn This could be due to their ability to seek a different risk and return profile which smaller deal sponsors might not be willing or able to do. For deal sponsors with an AUM of between £100m and £1bn opportunistic strategies are most favoured. For smaller sponsors with an AUM of less than £100m, core investment strategies are favoured, albeit the number of respondents in this category have on average split their allocation equally over all categories.

Investment strategy by deal sponsors size (AUM) - Q1 2018

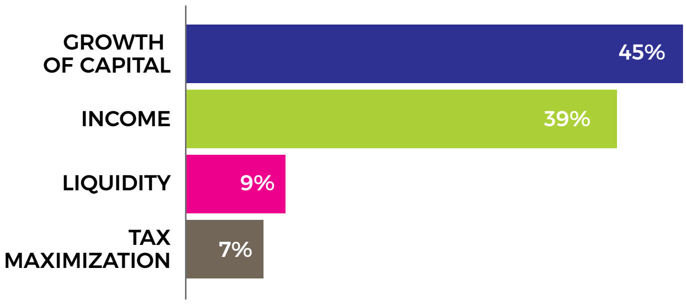


INVESTMENT OBJECTIVES

As near term returns from direct property ease, we have noted that investors are considering ways to enhance performance of their investments. The key investment objective and motive identified in the poll is capital growth. Capital growth has been the lead driver behind investment in 2017 and so far in 2018.

Income return, closely follows capital growth across all investors, as the importance of this has been trending upwards in 2017 and 2018. We have also identified an increasing trend in preference for liquid asset. All combined investors desire for liquidity has increased by 40% from Q1 2017 to the start of Q2 2018.

Investors' objectives - Q1 2018

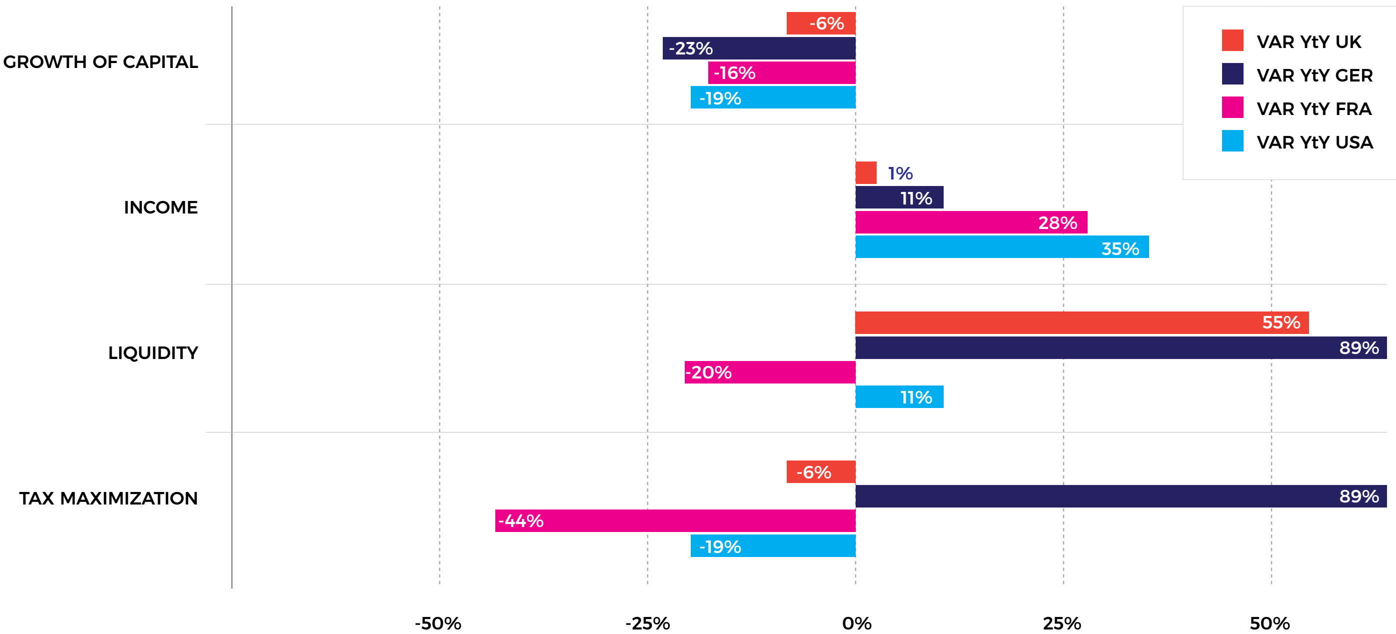


There are also geographical differences between investment objectives.

The UK investors main objective is to have growth of capital, albeit income is becoming a more important investment objective in this low-interest rate environment throughout Europe. Liquidity is also valued by UK investors with a 55% increase over the time period.

This trend is mirrored by German investors, although the important of tax efficiency optimisation has been identified by many investors from Germany in 2018. Liquidity of real estate is a less important investment objective for investors polled in France and a greater number of investors located in France are targeting income over capital growth. The investors situated in the US are looking for income and capital growth, with liquidity as a less important objective.

Investors’ objectives - evolution by country - 2017-2018



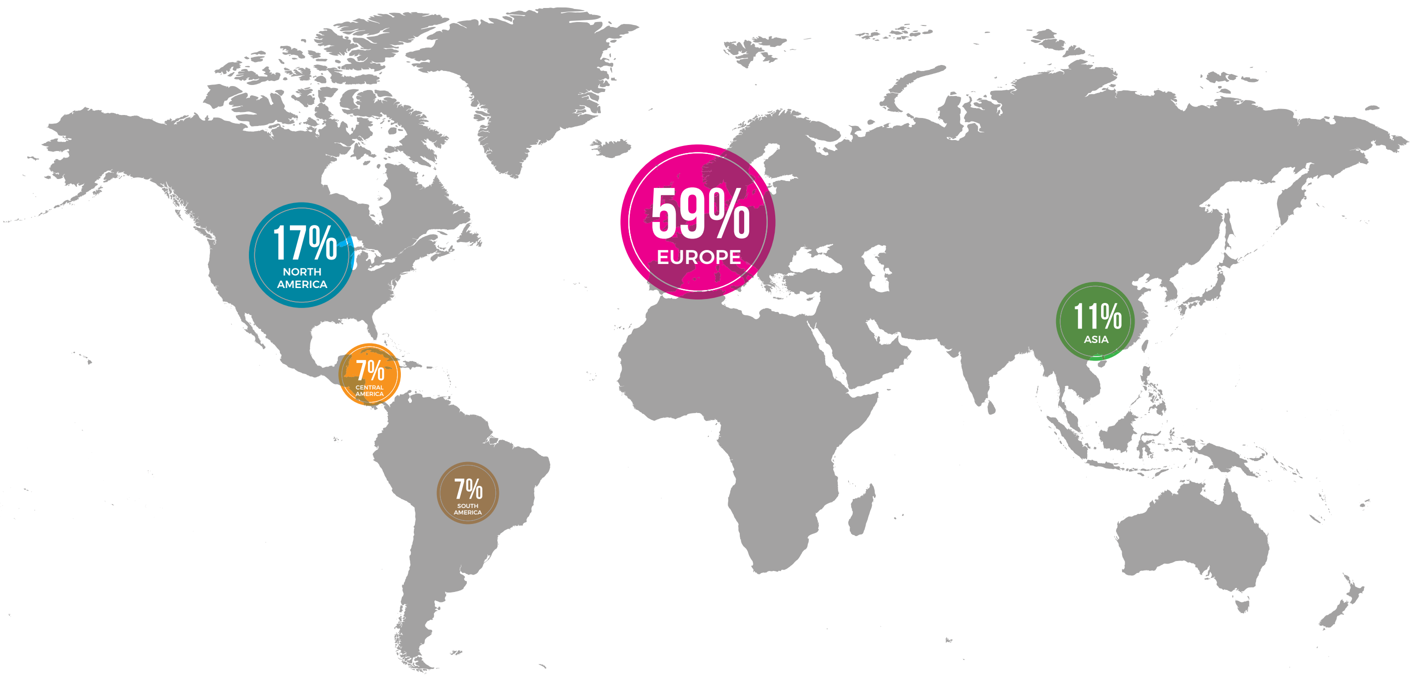
REGIONAL AND COUNTRY PREFERENCE

Optimism is spreading through Europe's property industry, buoyed by an improving macro-economic outlook from the Eurozone and real estates continuing attraction as an investment asset class. GDP forecasts are much more positive now than comparatively in the last few years and these forecasts are bringing in strong flows of capital.

Emmanuel Macron's influence has ensured economic growth in France as well as cement strong growth forecasts. It is predicted that Europe will still lead growth, ahead of the US, albeit there is still uncertainty surrounding the UK. Brexit is causing issues for investor sentiment and decision making. Previously, London and the wider UK has always had a premium over mainland Europe, however investors are looking to place their capital elsewhere, as identified in our recent polls.

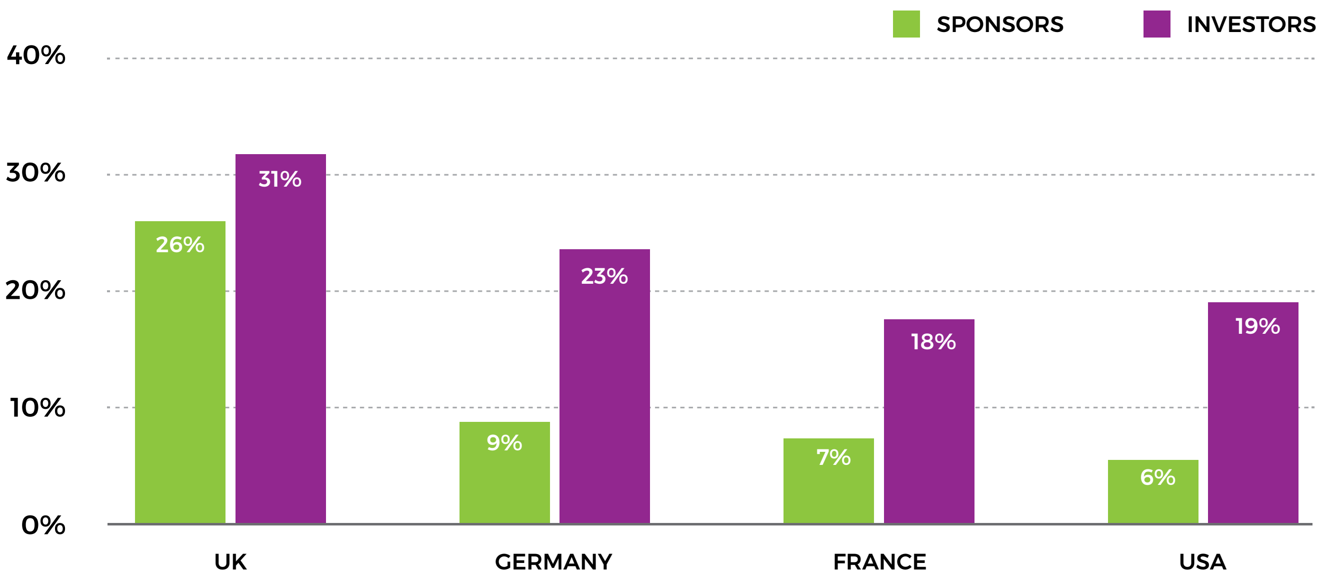
With increasing pressure to place capital into real estate and with a Global AUM, forecast by PwC, to grow 6.2% per annum until 2025, deal sponsors are having to consider different countries and locations, combined with different strategies and asset classes. It is considered that certain locations are already at full capacity and therefore competition for assets and exposure to real estate, is set to increase as both investors and deal sponsors look for returns.

Deal sponsors regional focus - Q1 2018



Europe is the preferred continent amongst both deal sponsors and investors. Within Europe, the UK, Germany and France are the most favoured countries. Of the Sponsors polled, almost 60% of them said that they were focussing on Europe, and of these companies, 42% would be directing their attention to the UK, Germany and France. Despite market uncertainties, the UK retains its top spot for investors, albeit Germany is chasing on its heels and is one of the favoured markets for US capital.

Sponsors/Investors compared country focus - Q1 2018

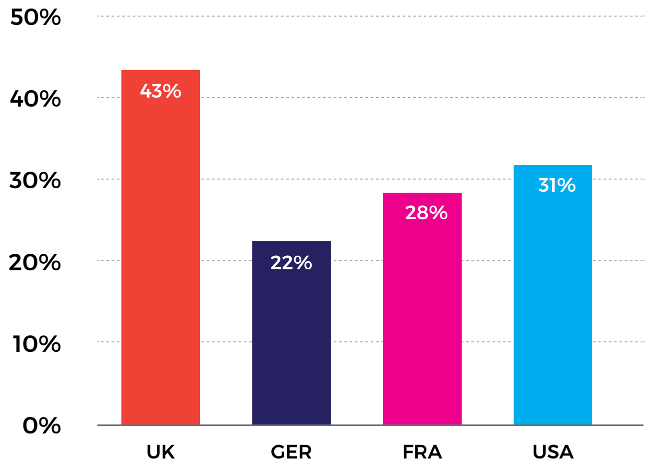


CROSS-BORDER INVESTMENT

Unsurprisingly each investor base highlights their own country as their favoured location with UK investors having the highest percentage of home bias amongst the other investor countries.

This could perhaps be due in part to the weaker sterling, which has reduced their buying power abroad. Of the 4,500 global investors polled, 31% stated in Q1 2018 that they would be looking to invest into UK real estate, which will be aided by yield conditions and favourable currency exchanges.

UK as an investment destination (by investors' location) - Q1 2018



International buyers were particularly active in the UK, as identified in the latest poll, with the UK remaining in first place on the global sponsors and investors list. Property is still offering a significant spread over gilts, despite yield compression and interest rate rises. The UK market has seen a wealth of transactions in 2017 and is expected to still be popular in 2018.

The UK is still able to provide long term income, secured to financially strong multinational firms. The UK is also underpinned by a strong and open legal and regulatory framework, which will help counterbalance some of the wider economic issues facing the UK. It also has higher yields than comparable European cities. Knight Frank forecasts Manchester prime office yields at approximately 4.75%, compared to Berlin at 2.9% and Paris at 3.00%.

CONCLUSION

With almost $700 billion transacting in the global real estate market in 2017 and positive wider economic 2018 forecasts for the market, investors and sponsors are continuing to channel capital into the industry.

The current global economic background of low interest rates and strong property fundamentals makes real estate a particularly attractive market. Residential remains the most favoured asset class going into 2018, followed by industrial assets due to their positive occupier markets and increasing rental levels. Non UK sponsors prefer the traditional commercial assets, whereas UK sponsors are targeting residential and mixed use assets due to the countries current dynamics and housing shortages.

Deal sponsors are looking further along the risk curve to increase their real estate returns although the investor market, on the whole, is trending in the opposite direction and are looking to invest in lower risk opportunities. Investor objectives are also developing and an increasing number have highlighted the desire for income and liquidity over the timer period Q1 2018 to Q2 2018. Capital growth however is still the lead driver behind investment in real estate. Europe has been identified as the global top spot for investors worldwide, with the UK, Germany and France leading the way.

With the ability to offer exciting opportunities throughout Europe to investors looking for capital growth, income, liquidity and tax optimisation as well as connect deal sponsors to investors with similar investment strategies, BrickVest is looking forward to another exciting year in the real estate investment market.