

European Fair Value Index

Q4 2018

Number of markets classified as "fully priced" continued to rise



The all-sector European Fair Value Index score dropped to 16 in Q4 down from our Q3 score of 28, and approximately the same level recorded in Q2 2007, reflecting the advanced stage of the property cycle and fewer attractive prime opportunities (Figure 1).

As such, a considerable number of markets were downgraded this quarter (32 in total), with the largest component moving from fairly priced to fully priced (25 markets). The sector downgraded the most was the retail sector, reflecting the recent subdued sector performance.

The combination of property yield compression coupled a higher illiquidity and risk premium has narrowed the spread between the fair and forecast return further, deteriorating property attractiveness and causing the index to fall further. The illiquidity and risk premium in part depends on the spread between corporate and 5-year bond yields, and is used as a proxy for tenant risk. A deterioration of risk sentiment led to the broad-based underperformance across corporate bonds relative to government bonds.

Opportunities in the logistics sector have reduced dramatically as investors seeking higher returns are driving strong demand in the sector, where yields continue to fall. As a result, the logistics index shows an increasing number of fairly priced markets as at Q4 (Figure 5).

Geographically, the CEE and Semi-Core have the most underpriced markets while Core markets such as the UK and France have more fully priced markets. Top picks include logistics in Dublin, Lisbon, Madrid and Hamburg logistics (Figure 7).

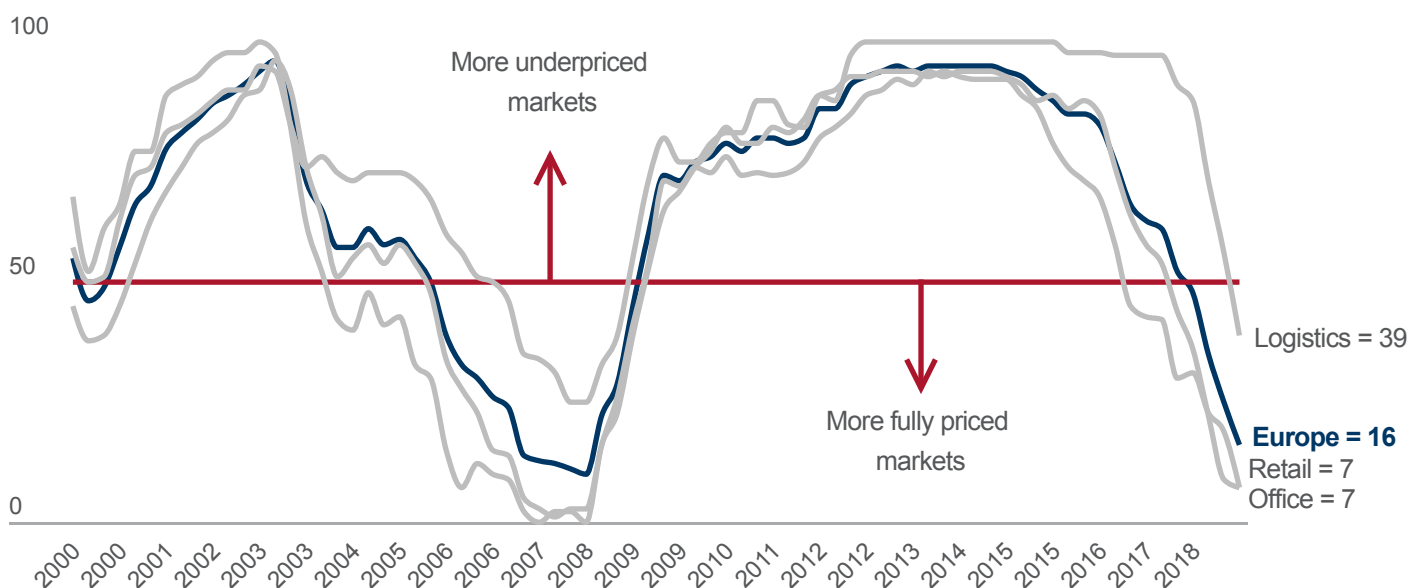
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If government bond yields rise and the risk premium remains broadly at today's level, then investors will need to have higher long-term income growth expectations to justify real estate pricing at today's levels.

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Riccardo Pizzuti, Senior Analyst EMEA Forecasting

Figure 1: C&W European Fair Value Index by Sector, Q4 2018



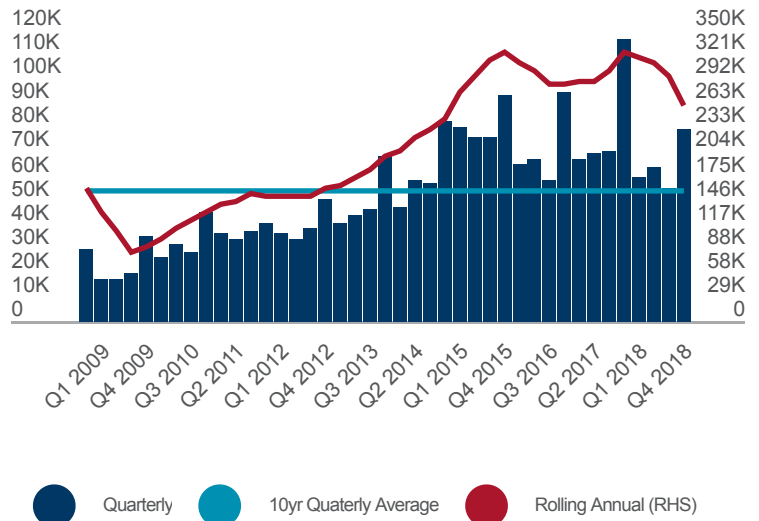
Source: Cushman & Wakefield Research & Insight

Figure 2: Prime Yield Movement, Q4 2018 vs Q3 2018, bps



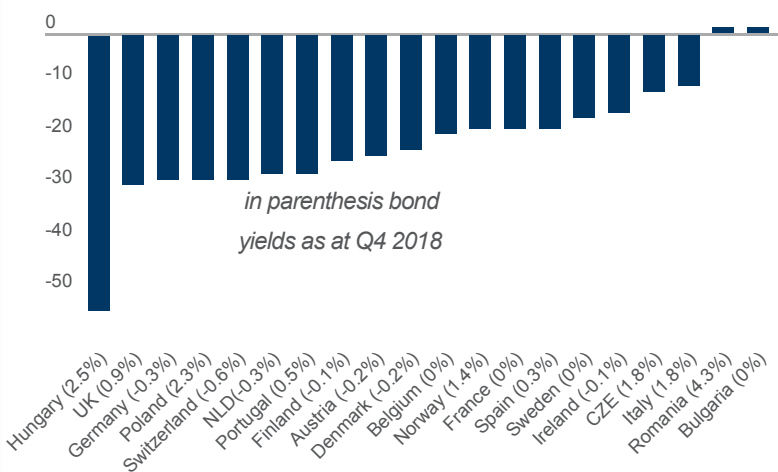
Source: Cushman & Wakefield Research & Insight

Figure 3: European Investment Activity, EUR bn



Source: RCA

Figure 4: Government bond yields bps change, Q4 2018 vs Q3 2018



Source: Bloomberg

Figure 5: Share of markets in each category by sector



Source: Cushman & Wakefield Research & Insight

Figure 6: Share of markets in each category by region



Source: Cushman & Wakefield Research & Insight

Figure 7: Five most under/fully priced markets in Europe

Most Underpriced Markets	Most Fully Priced Markets
1. Bucharest logistics	119. Milan offices
2. Madrid logistics	120. Milan retail
3. Dublin logistics	121. Rome retail
4. Antwerp offices	122. Istanbul retail
5. Bucharest retail	123. Istanbul offices

Source: Cushman & Wakefield Research & Insight

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MARKET IN FOCUS

Dublin Logistics

Ranked 3rd overall in our Fair Value Index in Q4, Dublin Logistics is underpriced by 6.8% according to our Fair Value analysis.

The performance of the industrial sector continues to improve, albeit with a lack of availability of quality stock impacting occupier options. This lack of availability is not only placing upward pressure on rents, but has also culminated in a strengthening of lease terms in favour of the landlord.

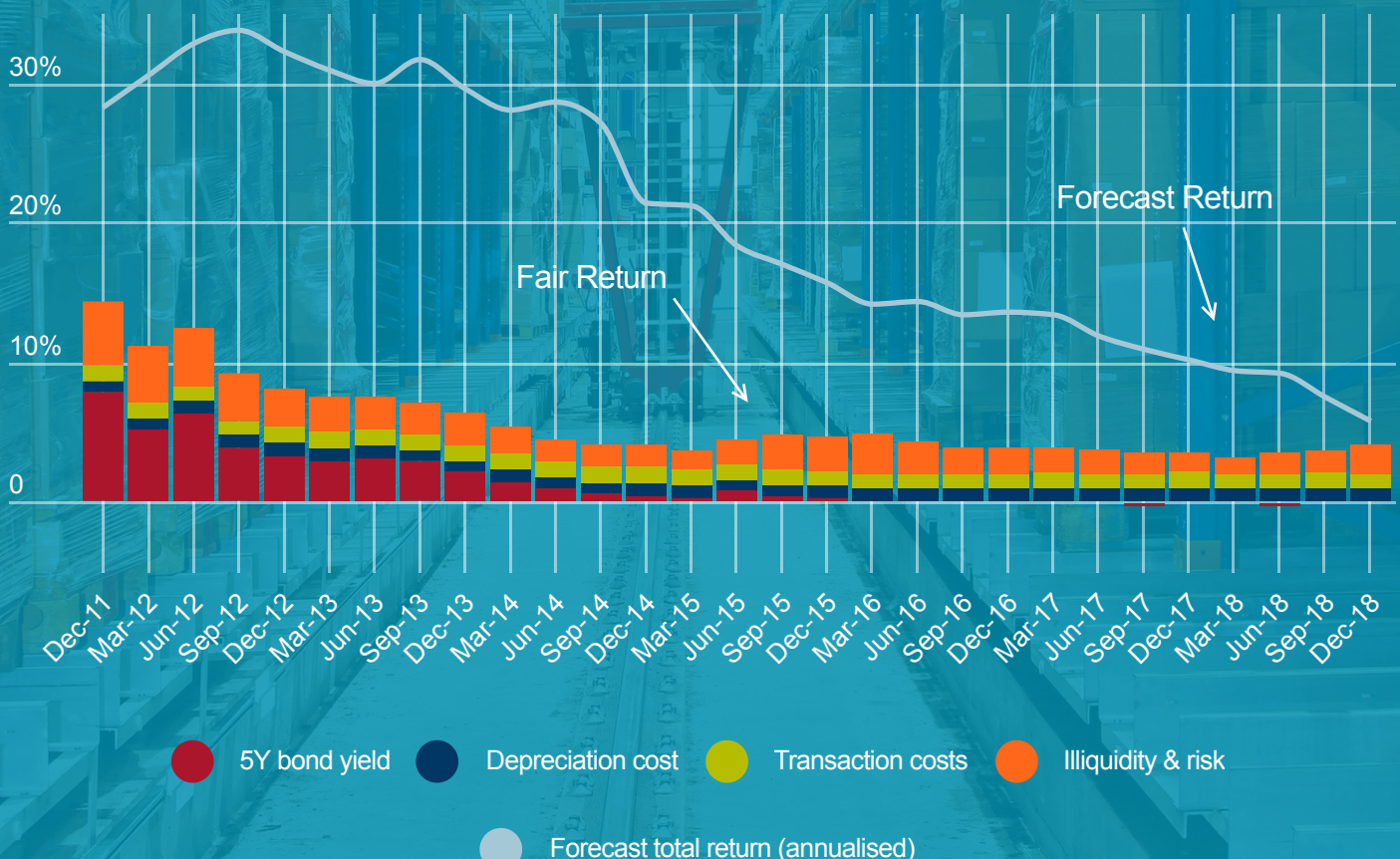
Some occupiers are struggling to obtain Grade A space for a term of less than ten years due to contract driven requirements.

The low (negative) bond yield and positive logistics return outlook maintained the degree of under-pricing for Dublin in Q4. Despite strong investor interest, a lack of product is a factor hindering the market.

Industrial assets account for quite a small share of the overall investment market, as lot sizes tend to be small. Like other sectors, investors are also looking regionally to satisfy their industrial requirements

Our expectation is for stable yields this year, supported by healthy investment volume, and continued rental growth, aided by strong occupier demand. This leads us to forecast prime total returns of c.5.7% p.a. over the next five years (Figure 9).

Figure 9: Dublin Logistics fair and forecast returns



Source: Cushman & Wakefield Research & Insight

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Cushman & Wakefield Fair Value Methodology

The Cushman & Wakefield Fair Value Index was launched in 2010 and covers 123 markets across Europe. Fair value is the value at which an investor is indifferent between a risk free return and the forecast return from holding property, taking into account the extra risk of investing in the property asset class.

When a property price is at fair value, an investor is being adequately compensated for the risk taken in choosing to purchase real estate; similarly, when the property price is below the fair value price, an investor is being more than compensated for the risk taken in choosing to purchase real estate. When buying at or below fair value, an investor does not necessarily buy at the bottom of the market.

Our Fair Value analysis focuses on prime assets and a five-year investment horizon, and hold for the market overall; individual transactions may provide opportunities and risks beyond the average market view. In the report we compare results for the current quarter with the previous quarter which may differ from those published in the previous quarter's report, this is due to the forward-looking methodology. As such, when our forecasts change so too does the Fair Value Index.

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