Market Insights on European non-listed real estate in December 2024

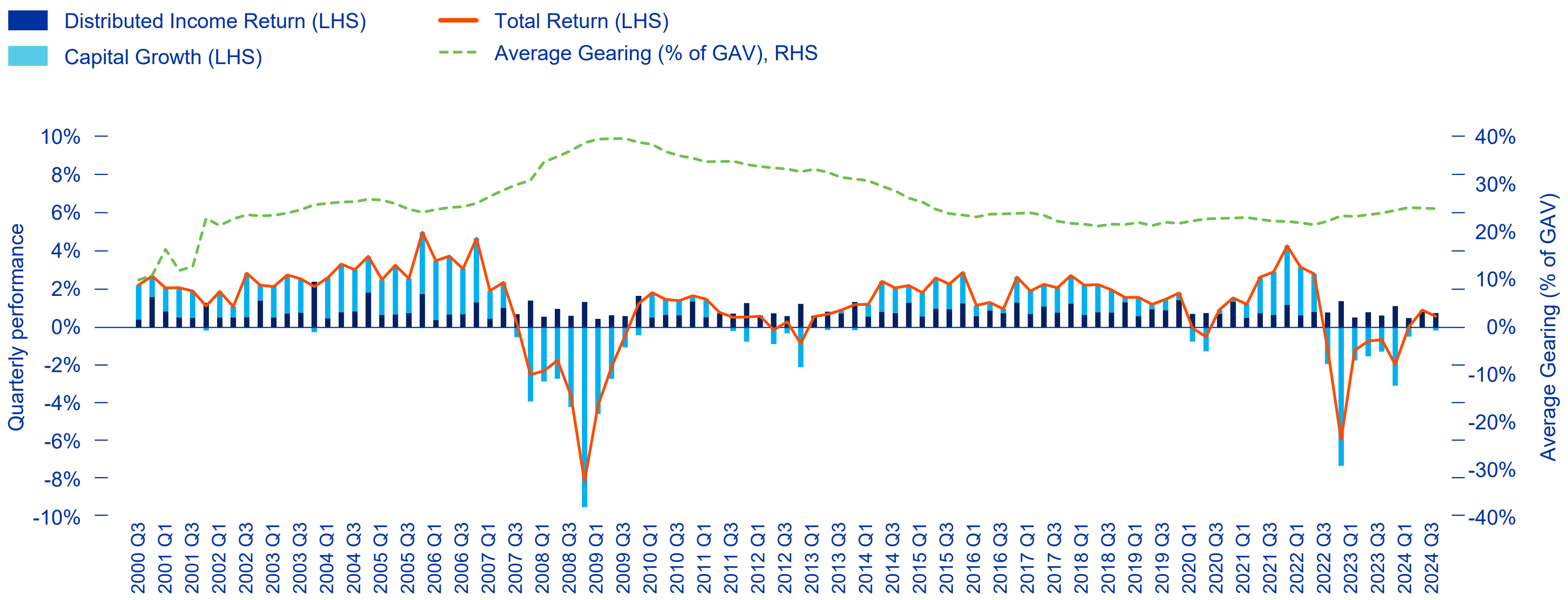
The latest edition of the INREV Market Insights indicates a growing sense of optimism for European real estate. The December Consensus Indicator rose to 57.8, a fourth consecutive quarterly improvement (see p.4 for more details). The Q3 2024 INREV Fund Index posted a total return of 0.59%, a third consecutive quarter of positive performance, albeit a decline from the 0.91% equivalent reported in Q2 2024.

Capital growth turned negative to -0.16% in Q3, after only one quarter of positive results (0.09% in Q2). Notably, residential and industrial/logistics focused funds achieved their strongest performance in nine quarters.

Retail focused funds managed to maintain positive performance, while office funds slipped back into negative territory after a brief rebound last quarter.

For the overall INREV Fund Index, the distributed income return decreased to 0.75% in Q3 2024 (0.83% in Q2), bringing the one year rolling distributed income return to 3.24%.

Figure 1: European non-listed real estate performance



Source: INREV Pan-European Quarterly Fund Index, Q3 2024

Residential and industrial/ logistics assets lead the Q3 results

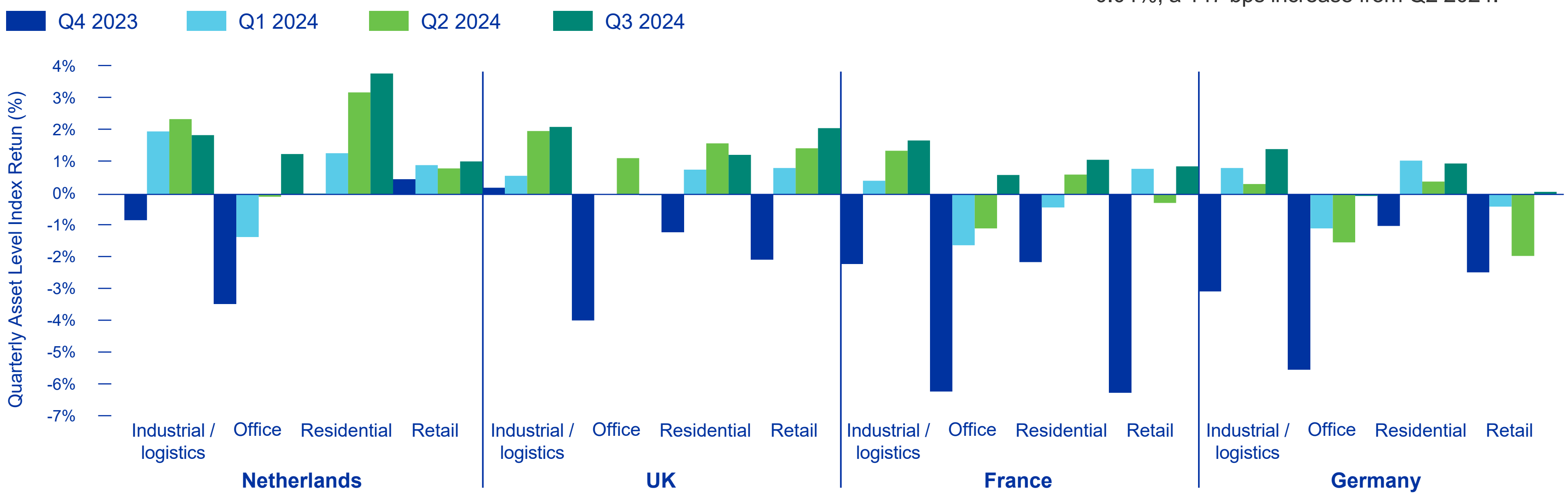
In Q3 2024, the Netherlands reported positive returns across all major sectors, returning 2.98% at a country level and marking another quarter of outperformance. The latest results were primarily driven by the exceptional performance of residential assets, with 3.81% (+59 bps quarter-on-quarter). At 1.27% and 1.04%, respectively, the performance of Dutch office and retail assets improved from last quarter. The Netherlands demonstrated consistent outperformance in recent quarters, driven by robust fundamentals in its industrial/ logistics and residential sectors.

UK assets reported a total return of 1.54% in Q3, down from Q2's 1.59%. Capital growth decreased by 5 bps quarter-on-quarter to 0.47%. Its industrial/ logistics sector, forming 45% of the UK Asset Level Index, reported a quarterly performance of 2.13%. This is the only market in Europe where retail assets came close second (2.09%) and ahead of the Q3 residential performance (1.24%). While its office sector presented encouraging returns in Q2 at 1.14%, it fell back into the negative at -0.02% in Q3. By contrast, only Dutch and French office assets posted positive returns this quarter.

At 1.10%, the French assets recorded the highest total return in nine quarters. The Q3 result was largely led by strong industrial/ logistics sector returns (1.69%), indicating a third straight quarter of improvement. French residential and retail assets followed, reporting Q3 total returns of 1.10% and 0.88%, respectively. The French office assets also delivered a positive performance of 0.61%, displaying a notable +168 bps increase q-on-q.

After eight consecutive quarters of negative returns, German asset performance turned positive on an all-sectors level at 0.56%. German industrial/ logistics led this increase with the Q3 total return of 1.43%. Residential and retail assets both showed a noticeable performance spike, with the Q3 returns standing at 0.98% and 0.09%, respectively. German offices demonstrated encouraging signs, returning -0.04%, a 147 bps increase from Q2 2024.

Figure 2: Performance of European real estate assets by country and sector

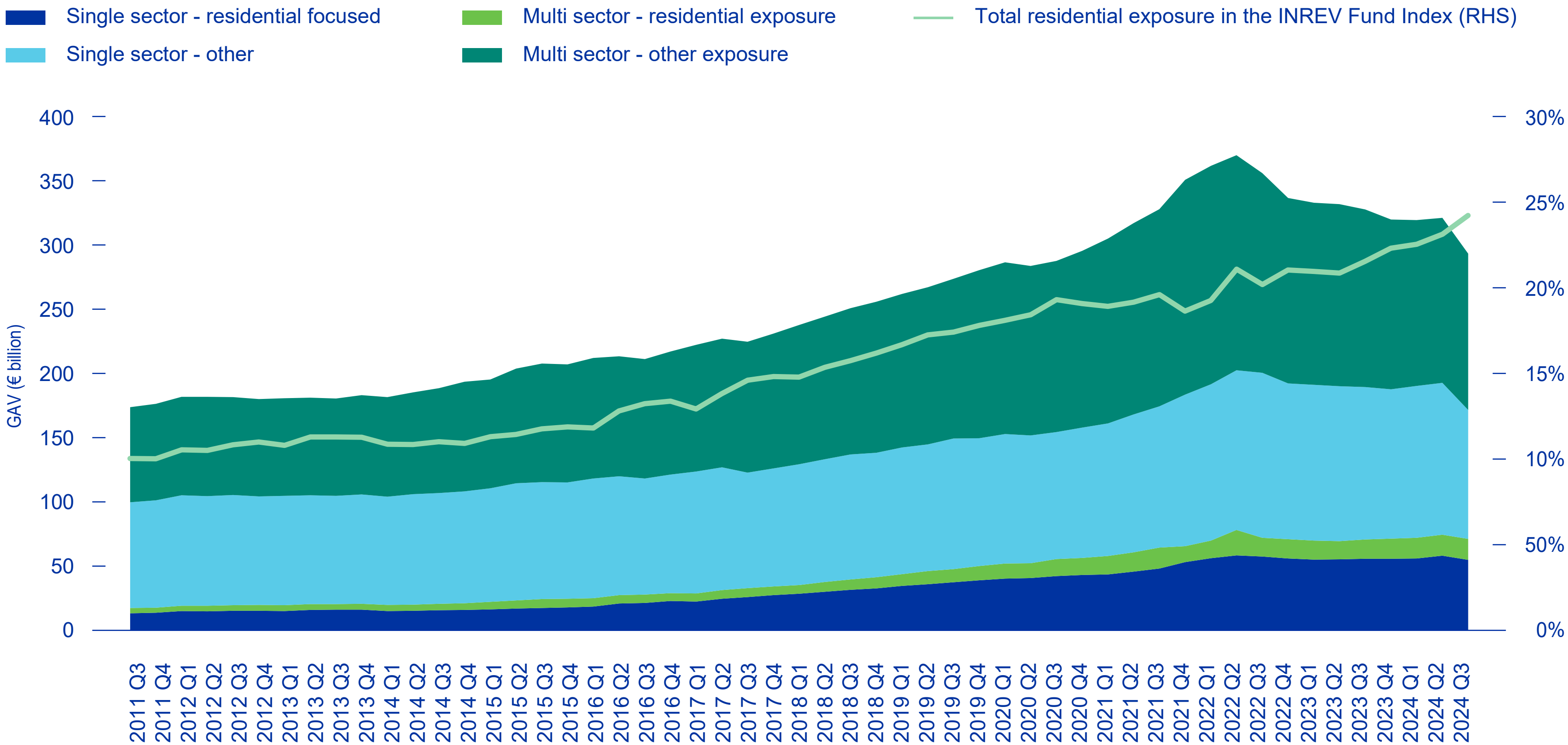


Source: INREV Pan-European Quarterly Asset Level Index, Q3 2024

Residential has become the largest single fund specialist sector in Europe

The residential sector has grown significantly in importance over the last decade. Indeed, in terms of value over these ten years, it has moved from being the smallest to the largest major sector across single sector funds. Additionally, residential is a growing proportion of multi-sector funds. Together, residential allocations represent 25% of the INREV Quarterly Fund Index, becoming the largest major single sector, while offices and retail have both contracted. The latest INREV Consensus Indicator cites residential among the top preferred sectors, with a net positive sentiment of 24% (see p. 9).

Figure 3: Residential sector grew to 25% of INREV Fund Index



Source: INREV Quarterly Fund Index, Q3 2024

December Consensus Indicator picks up as investment liquidity and lending improve. Downside risks remain unabated as the economic subindicator deteriorates

The December INREV Consensus Indicator recorded a headline reading of 57.8, a notable increase from September's 55.8. This marks a fourth consecutive quarterly improvement, setting a new all-time high since we started to track the market consensus in March 2023.

For the first time, three of the five subindicators surpassed the 60 mark. At 63.3, the investment liquidity subindicator maintained the lead for the second consecutive quarter. The financing subindicator showed the most significant improvement, now at 61.5 (see p.5 for more details).

The leasing and operations subindicator also rebounded to 61.5 after two consecutive quarters of decline, marking its first reading above 60 since March 2024. Notably, 58% of indicator contributors reported net effective rent improvements for new leases and rent renewals.

The new development subindicator remained steady, with a reading of 49.5, just shy of the 50 'growth' threshold for the second consecutive quarter.

Driven by expectations for the European GDP growth to diminish over the next 12 months, the economic subindicator fell to 47.4. It is a notable slide from 58.6 in September, falling below the 50 mark for the first time since December 2023. Downside risks remain unabated, and a bifurcation of the letting market is of particular concern.

Figure 4: INREV Consensus Indicator

Figure 5: INREV Consensus subindicators

Lending activity improves across the board

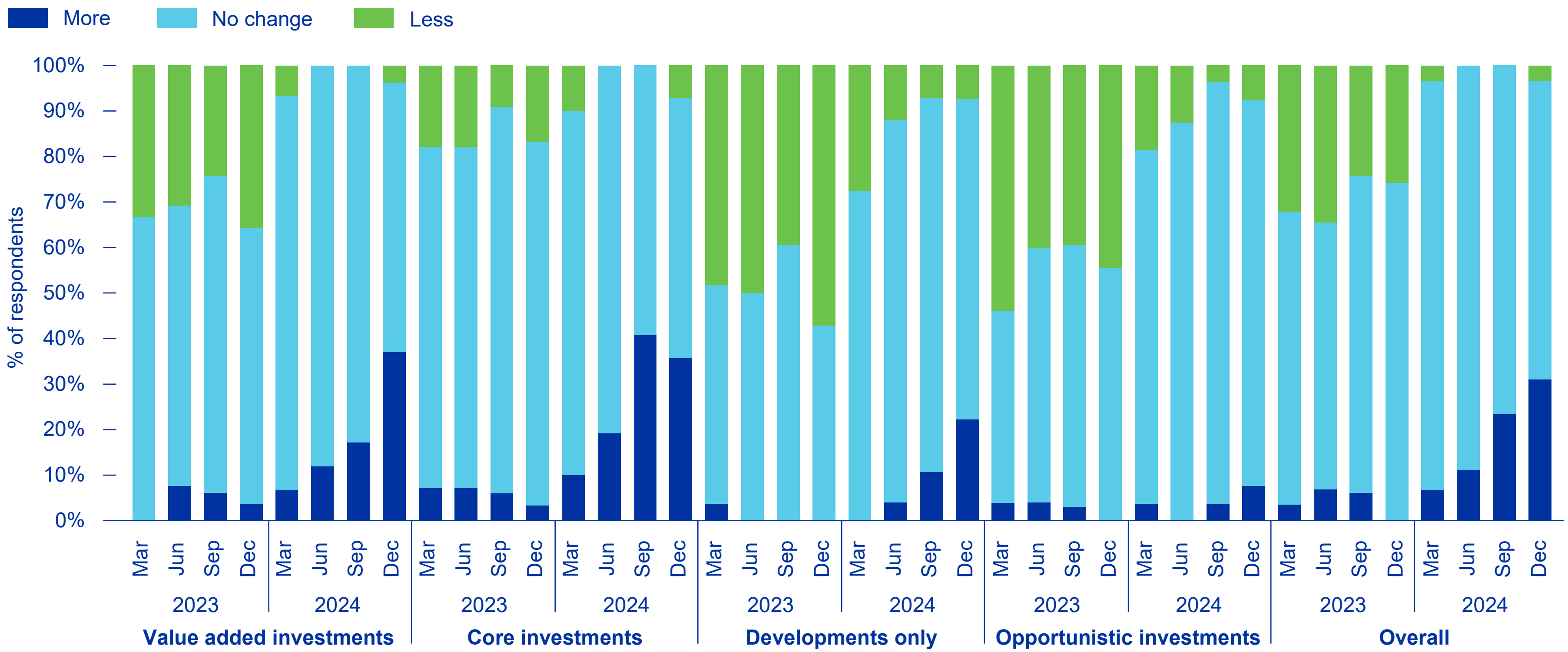
The financing subindicator showed the most significant improvement, increasing to 61.5 from the 56.6 three months prior. More than a quarter of respondents suggested that not only alternative lenders but increasingly traditional lenders, ie banks, have started to be more active in providing new financing opportunities. Furthermore, there is some evidence that financing conditions are becoming more favourable.

December marks the first point in time since we started monitoring market consensus when the availability of financing has improved across the full spectrum of risk strategies. Around 32% of Consensus Indicator participants report greater availability of financing for core and value added investments relative to September.

The equivalent for development financing has also notably improved, with 19% of participants highlighting it to be the case.

Lending toward opportunistic investments, which typically involve a high level of letting risk, improved only marginally. This could be due to weaker sentiment not only from lenders but also the borrowers engaging in such deals.

Figure 6: Availability of financing



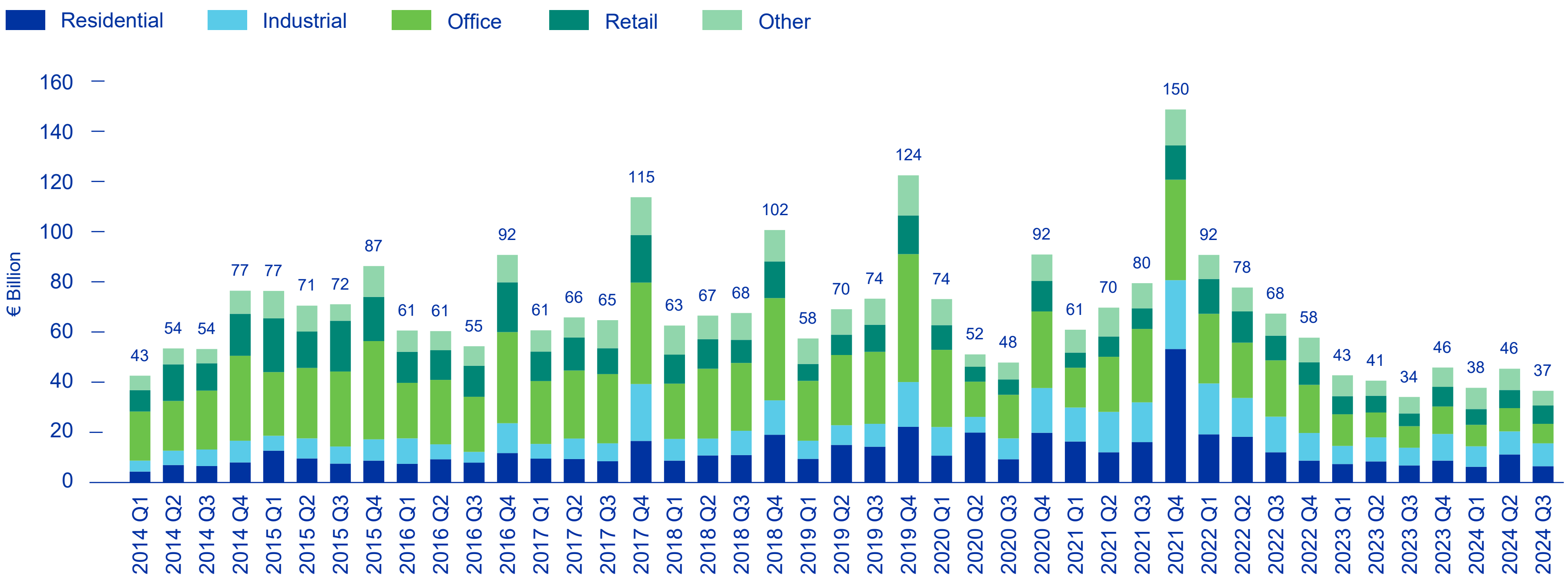
Source: INREV Consensus Indicator Survey, 2024

European transaction volumes are yet to pick up

European transaction volumes decreased to €36.9 billion in Q3 2024, down from €45.7 billion in Q2 2024. While this is a relatively low figure compared to the 10-year quarterly average (€69.4 billion), it is above the €34.4 billion registered in Q3 2023, the lowest point in the past decade.

While the overall transactional volumes are yet to recover, the latest Consensus Indicator results signal a notable improvement in sentiment. The investment liquidity subindicator climbed to 63.3, maintaining its lead for the second consecutive quarter. This suggests a build up of a deal pipeline and a growing desire to transact.

Figure 7: European direct real estate transaction volumes by sector



Source: MSCI Real Assets, December 2024

Drivers of near term performance

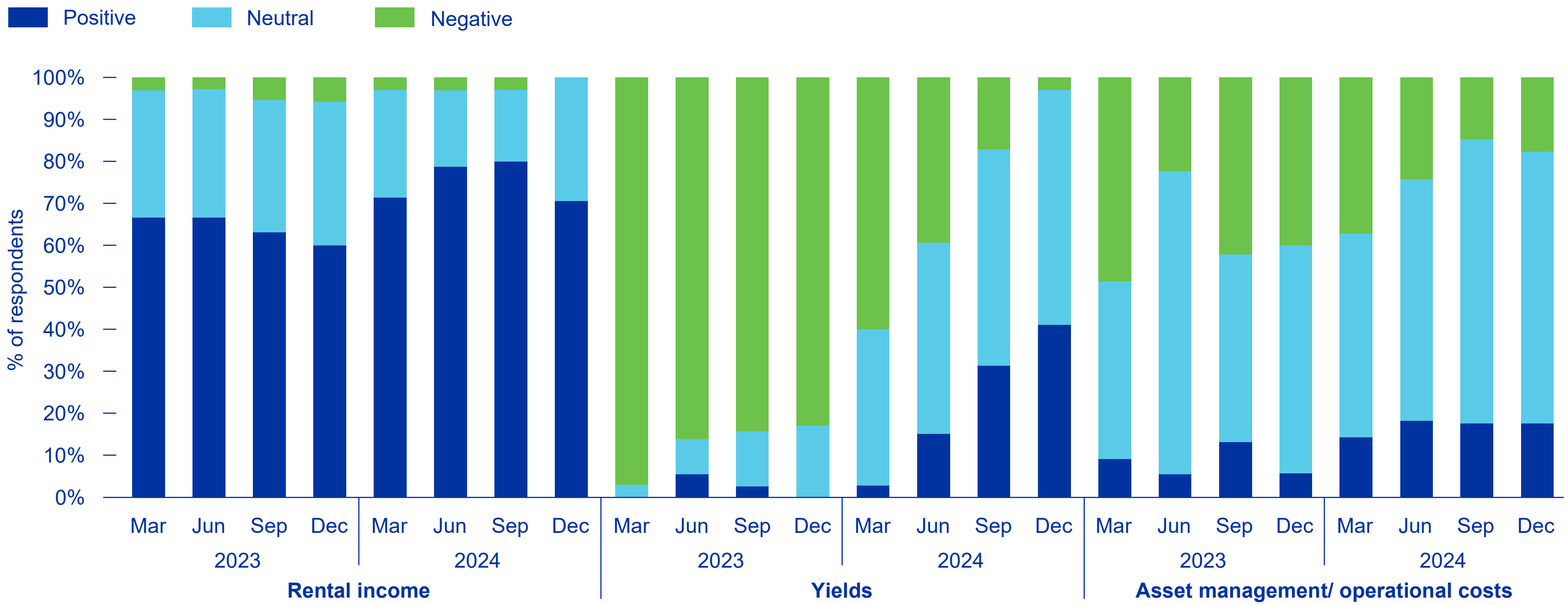
The latest Consensus Indicator revealed that downside risks remain unabated. A bifurcation of the letting market is of particular concern given the degree of economic slowdown. It will be critical to near term performance, with 74% of participants expect rental income to be a primary return driver Q1 2025.

Moreover, 37% expect yield compression during the next quarter. This is the highest result since the monitoring began in March 2023 and an increase on the 31% reported in September 2024.

It is worth pointing out that, on a net basis, respondents don't anticipate active asset management and operational costs to have an impact on the Q1 2025 performance.

This neutrality reflects the relative stability of these cost components compared to more market-sensitive factors like rental income and yields. That said, 18% of participants are anticipating an increase, which is offset by 18% that expect a decrease most likely as part of the strategic decision to pursue a more or less active asset management strategy, or as a reflection of upcoming acquisitions or disposals.

Figure 8: Drivers' impact on the next quarter's performance



Source: INREV Consensus Indicator Survey, 2024

Spain sentiment holds up strong in H2, while the UK slides down

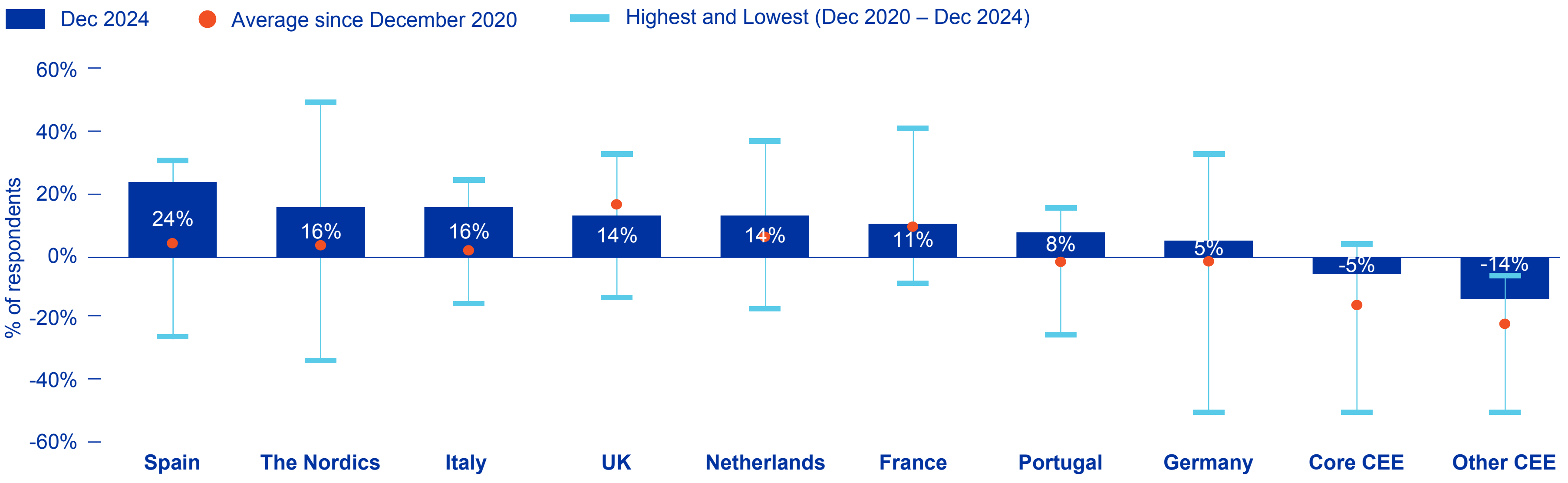
With 24% in December, Spain remained the most preferred European non-listed real estate investment destination for the second quarter in a row, albeit displaying a slight decline from the September results (31%). Compared to other western European countries, Spain looks to be on the other side of the economic recovery curve; the post-Covid recovery is steady, and living sectors and hotels are performing especially well[1].

For the first time, the UK has dropped from its traditional position among the top three most preferred investment destinations into the middle tier, taking a fourth place. While the UK remains a key market for investors, its current sentiment scores fall below the historical average. The net share of surveyed participants intending to increase their UK allocations declined significantly to 14% in December, well below the 25% reported in both last quarter, as well as a year ago.

Italy and the Nordics continued their ascension in positive sentiment, both with net 16% this December. Italy, in particular, is riding a wave similar to Spain, benefiting from southern European economies' competitive yields. This appeal is further encouraged by a tourism-led recovery, which has provided momentum for key sectors such as retail and hospitality. The Nordics are supported by sustained economic growth expectations, high levels of transparency and availability of sustainability-focused investment opportunities.

France's sentiment has been shifting up since early 2024, ending the year with its highest level (11%) since March 2023. Trailing behind, Germany displays only a slight positive sentiment (5%), with no improvement in sight. Net sentiment towards Core and Fringe CEE markets deteriorated to -5% and -14%, respectively as the war in Ukraine and geopolitical tensions continue.

Figure 9: Net sentiment towards European real estate by geography



Source: INREV Consensus Indicator Survey, 2024

[1] *INREV Asset Level Index, 2024*

Retail at its highest sentiment since May 2020

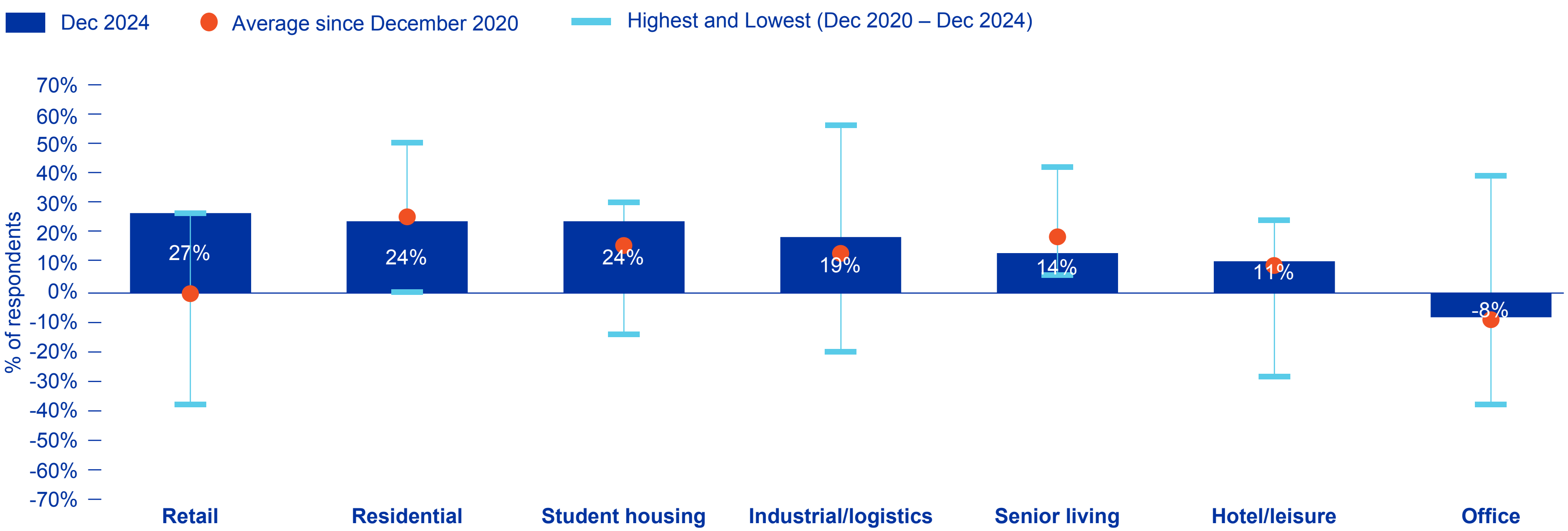
The retail sector sentiment has been consistently improving over the past four editions of Market Insights. At 27% this December, it reached its highest level since the record began in December 2020. Notably, for the first time in ten quarters, none of the surveyed participants indicated plans to reduce their retail allocations.

Despite this shift, the living sectors continue to demonstrate strong appeal. Sentiment towards residential is strong, with 24%, supported by high and steady returns. Additionally, student housing and senior living gained momentum, with sentiment climbing to 24% and 15%, respectively.

In contrast, the office sector remains out of favour, with a persistent net negative sentiment for eleven quarters straight.

The last net positive sentiment for offices was recorded in March 2022, at 29%. However, the latest result of -8% is an improvement on the previous three consecutive quarters of deep negative sentiment ranging from -25% to -29%.

Figure 10: Net sentiment towards European real estate by sector



Source: INREV Consensus Indicator Survey 2024

Assessment of investment risk increases at the end of 2024

As of December 2024, the performance expectations for European non-listed real estate strengthened further, with 26% of surveyed participants reporting an improved outlook (see Figure 11). This concludes 2024 as the first year since the survey inception in 2020 to record only net positive views on performance. This sentiment aligns with the latest INREV Quarterly Indices results which reported positive returns at both fund and asset levels and a notable increase in the INREV Consensus Indicator as a leading indicator for the European non-listed real estate market.

However, views on investment risk presented a contrasting narrative. On a net basis, 3% of respondents noted an increase in perceived investment risks compared to the previous quarter. This uptick can be attributed to political and geopolitical uncertainties, as well as to slowing economic growth which translates into unabated concerns around the bifurcation of the letting market and occupiers' financial health.

Figure 11: View on European real estate performance

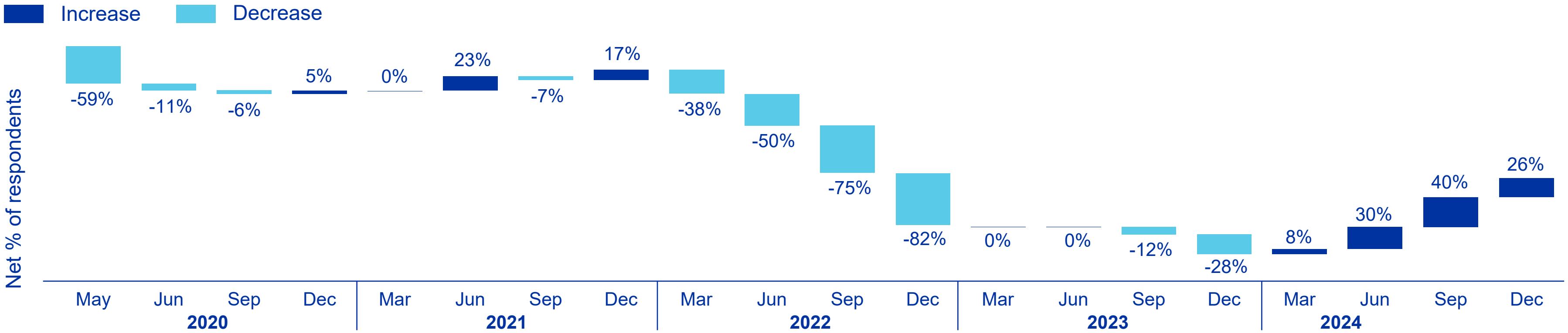
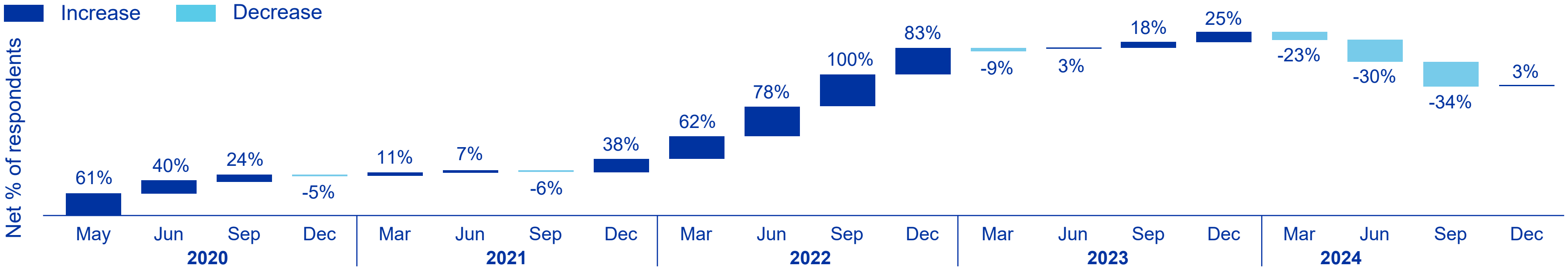


Figure 12: Assessment of investment risk for European real estate



Source: INREV Consensus Indicator Survey, 2024

This update highlights the latest results from the [INREV European Quarterly Asset Level Index Q3 2024], [INREV Quarterly Fund Index Q3 2024] and [INREV Consensus Indicator December 2024] to illustrate the impact on market performance, investment plans and operations.