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REAL ESTATE INVESTMENT: A GLOBAL PERSPECTIVE

EUROPE, AMERICA, ASIA-PACIFIC

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**Henry-Aurélien Natter,
MRICS, Head of Research**

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The real estate crisis, stemming from the surge in interest rates driven by escalating inflation, is not confined to Europe alone. Indeed, it also affects the other major continental blocks, such as China or the United States. In this study, we want to offer a global perspective on the evolution of real estate markets, explore the diversity of responses provided by international players, and draw the outlines of what could be a "global real estate allocation" in the next cycle.

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BLOOM – PARIS
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TOWARDS NEW EQUILIBRIUMS
FOR GLOBAL REAL ESTATE MARKETS

Global real estate markets are currently undergoing major transformations due to the reshuffling of the cards between the major continental blocks. The current geopolitical uncertainties and the potentially divergent economic developments across continents advocate in favour of adopting a global vision in order to guard against the volatility of the real estate markets of a single geographical area. With this in mind, international investors will therefore have an interest in diversifying between the major geographical blocks to spread their risk. Thus, as the frame of reference is becoming more complex, we wanted to offer our first analysis of global real estate markets. We have chosen to focus on 3 relevant blocks:

- Europe;
- America;
- Asia-Pacific.

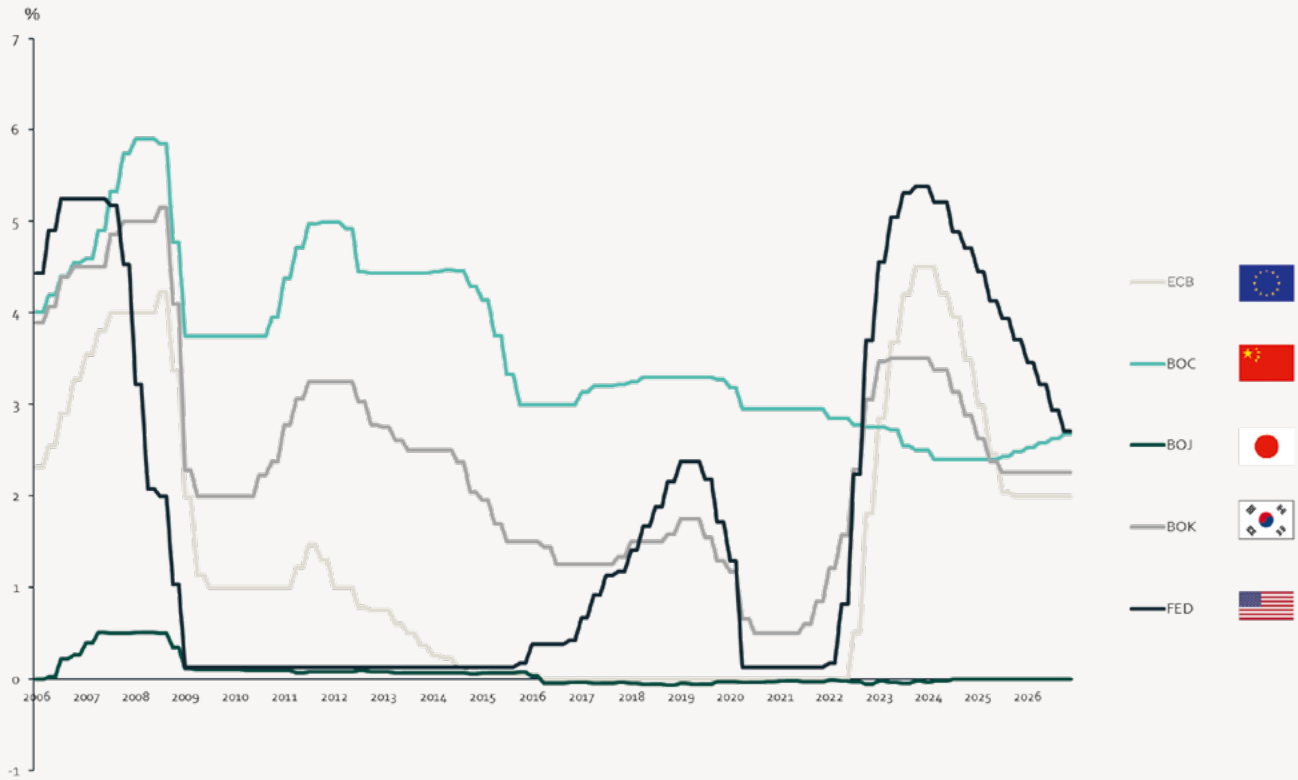
While these three major blocks seem quite heterogeneous, real estate dynamics have not always been the same, depending on the areas and periods analysed, particularly during the 2022–2023 crisis.

IN THE FACE OF INFLATION, DIFFERENT STRATEGIES ARE EMERGING

Since mid-2022, major central banks sought to curb the global inflationary trend by raising the cost of credit. **However, by the end of 2023, central bank strategies in major blocs appear to be diverging.** While central banks such as the FED (United States), the ECB (Europe) or the BOK (South Korea) still practice a policy of keeping their key rates at a high level for as long as necessary to control inflation, the BOC (China) has begun to reduce its rates to support an economy that is considered to be faltering. Despite inflation that is slightly above 2%, the BOJ (Japan) has chosen to maintain an ultra-accommodative monetary policy to continue to boost its growth.

Market conditions are expected to gradually stabilise, particularly in Europe and the United States, before triggering a more accommodating phase. However, the challenges should continue during the year 2024. The global economy will continue to face two major risks: on the one hand, the structural uncertainties that will weigh on the occupants, and on the other the high cost of capital.

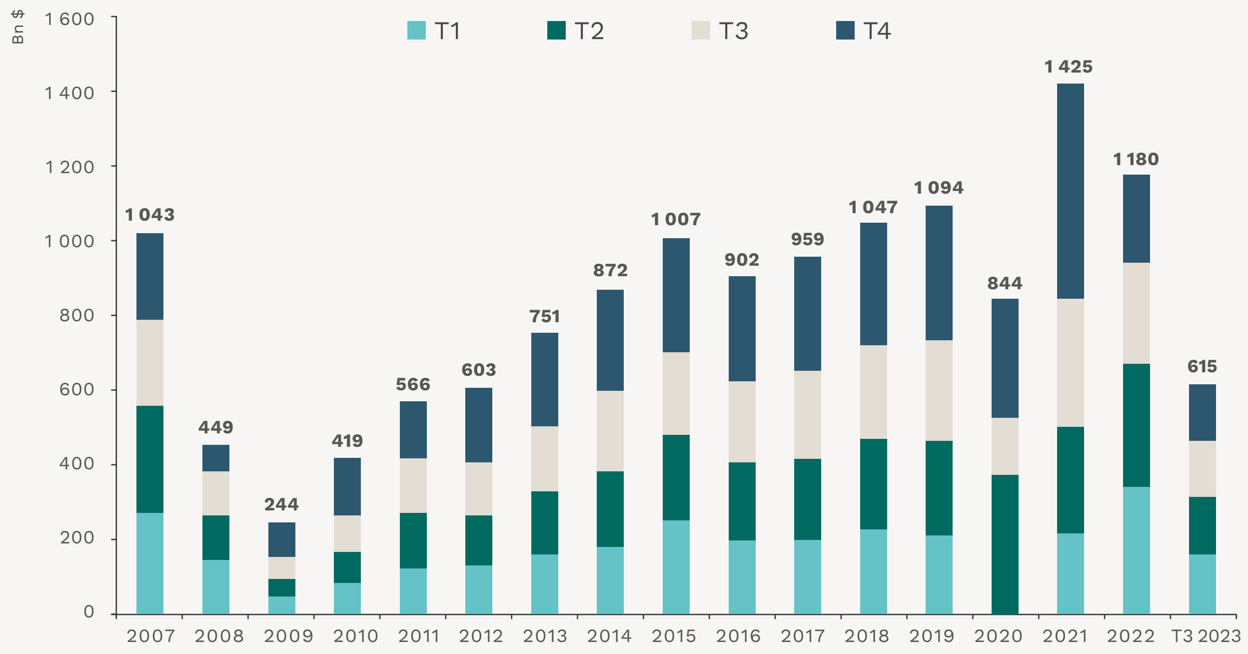
KEY INTEREST RATES OF THE MAJOR INTERNATIONAL CENTRAL BANKS



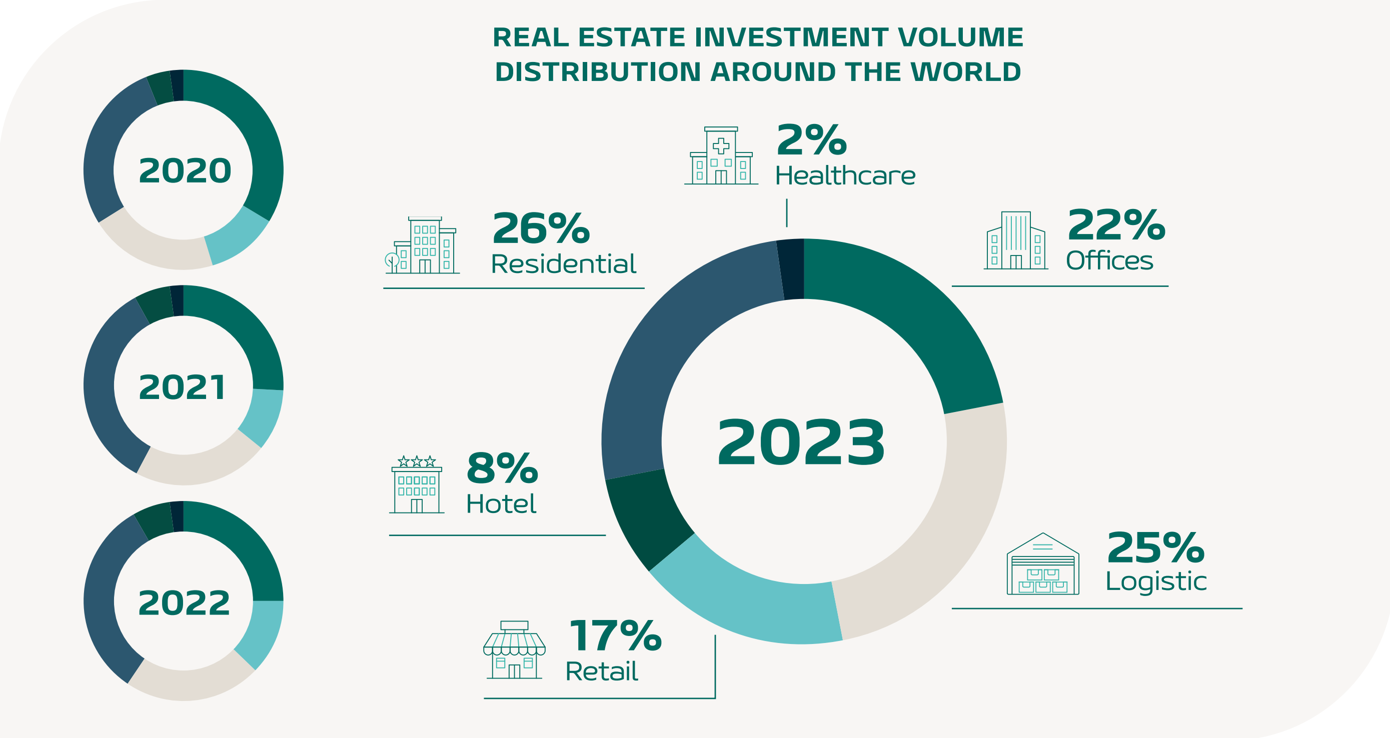
2023: A GENERAL DECLINE
IN REAL ESTATE INVESTMENT AROUND THE WORLD

Global real estate investment volumes experienced a strong deceleration during the year 2023 due to the impact of rising interest rates and uncertainties regarding economic growth. In this context, investors have shown a wait-and-see attitude on all 3 main continents, limiting capital flows. While the overall trend is similar, differences between areas and asset classes exist. After a complex year in 2023, 2024 and 2025 will mark a turning point with a gradual recovery in real estate investment after an easing of the restrictive policies of central banks.

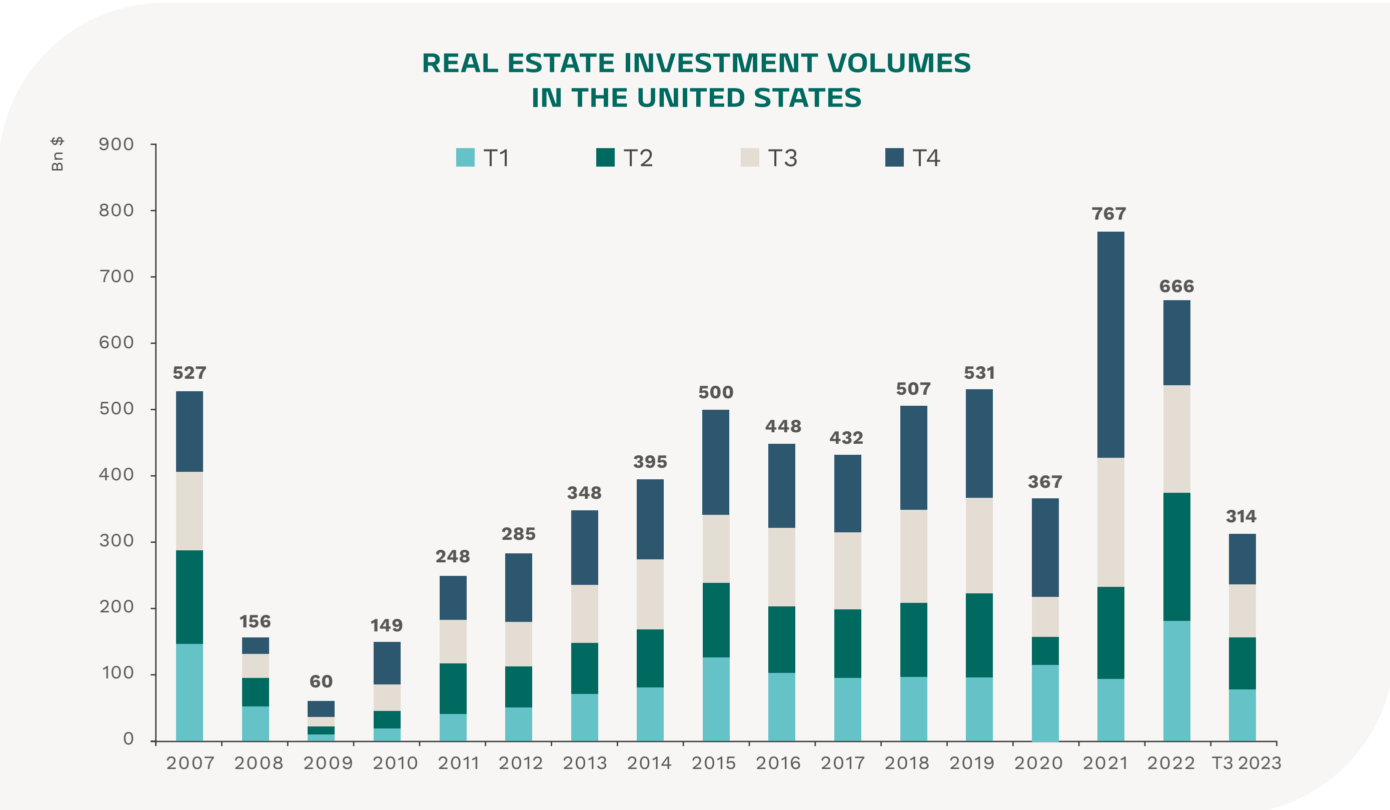
REAL ESTATE INVESTMENT VOLUMES AROUND THE WORLD



None of the three major areas of real estate markets have been able to escape the general slowdown in capital flows. 615 billion dollars of transactions were completed for the whole of 2023 (-48% in one year). The highlights of the year 2023 concern the fact that investors were defiant towards office real estate and opted for a balanced diversification of their capital allocation. Thus, logistics (25%) and residential (25%) were the assets that were most popular with investors, followed by office (22%), retail (17%), hotels (8%) and healthcare (3%).

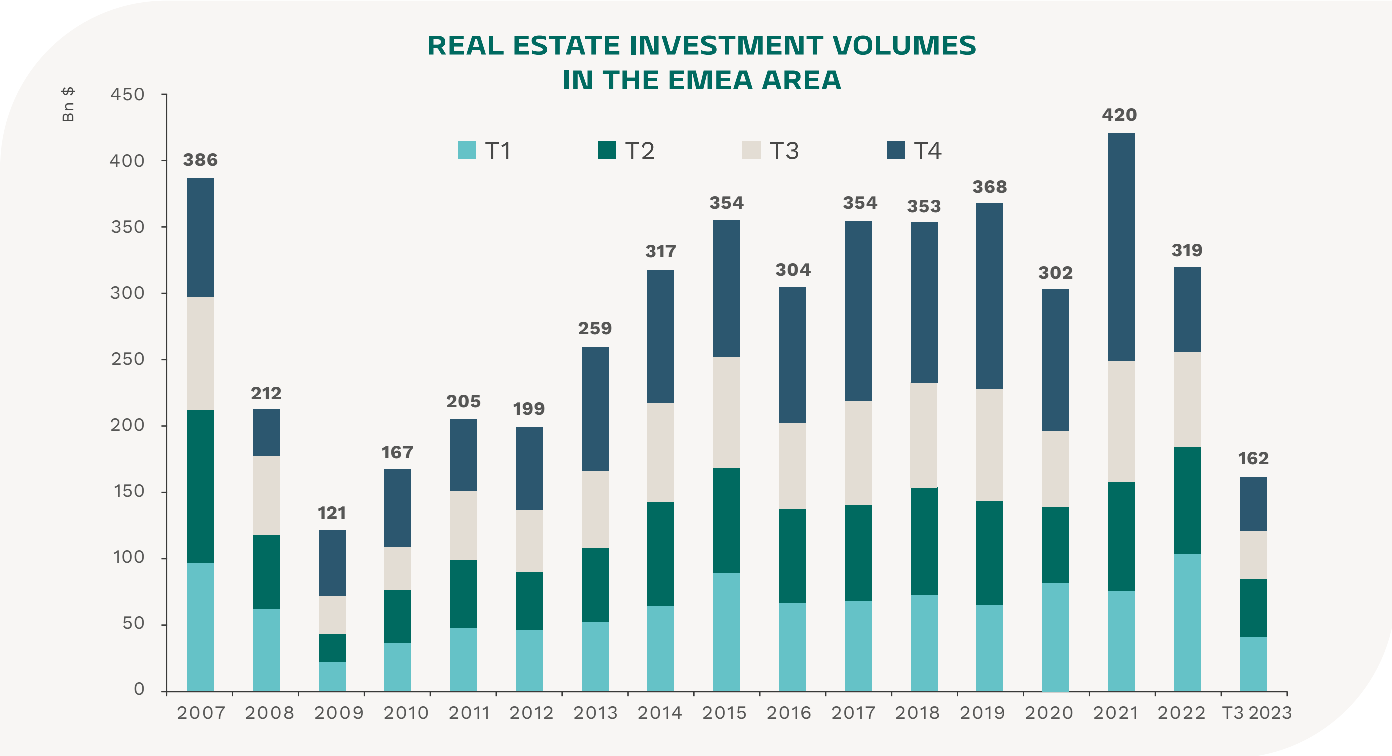


The largest investment zone in the world (51%), America, dominated by the United States, totalled nearly 315 billion dollars for the year 2023, down 53% compared to 2022. Residential real estate attracted the majority of capital, with more than $111 billion (-62% over one year), followed by logistics (84 billion, -42%) and retail (45 billion, -36%). The office sector in the United States, valued at 43 billion (a decrease of 60%), continues to face significant investor scepticism. This stems from occupancy rates that remain below pre-pandemic levels, primarily due to a widespread preference for remote work. In contrast, Europe and Asia have managed to strike a balance between office work and remote working. The hotel industry (21 billion, -49%) and healthcare (10 billion, -24%) have been able to resist relatively well.



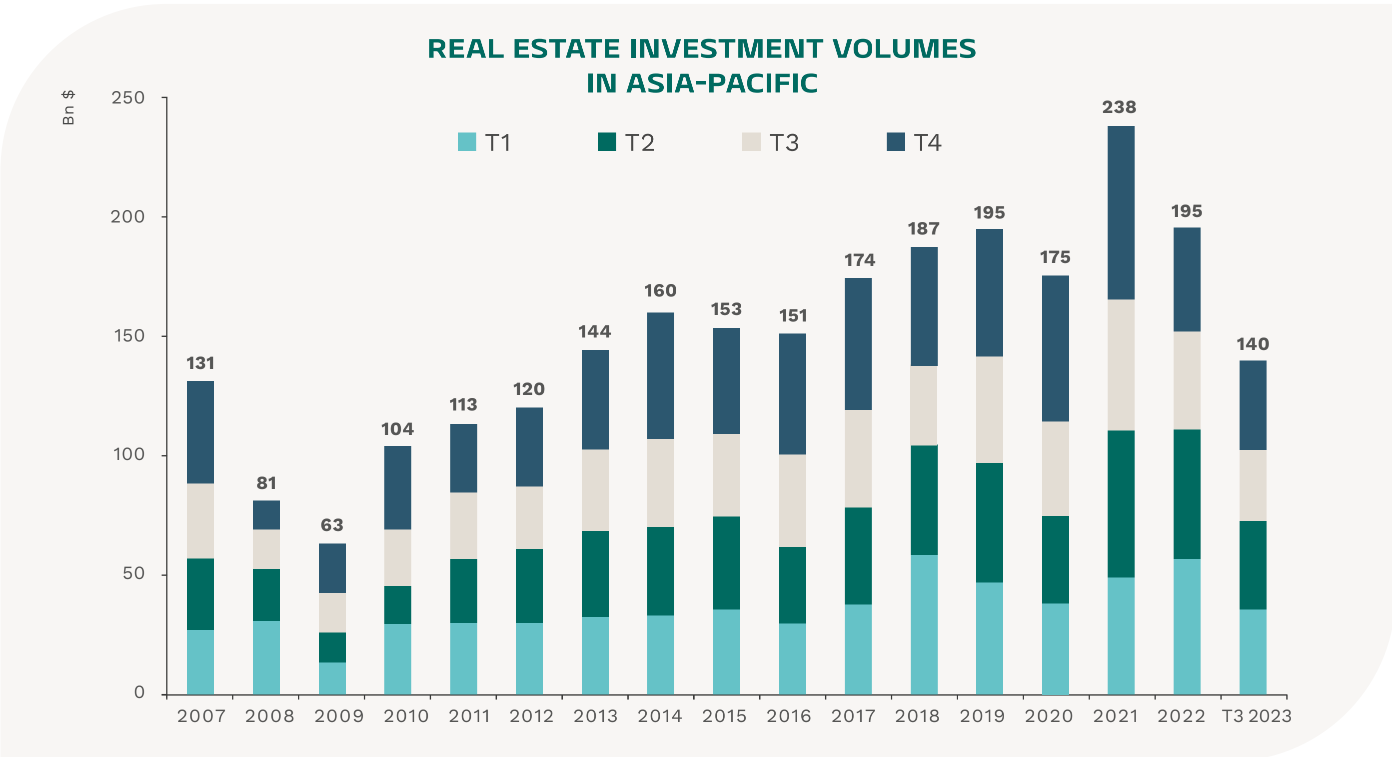
[1] *Off-site in development.*

The second block is the EMEA region (26%), dominated by Europe. This market also experienced a decline in investment volumes, with $162 billion in commitments for the whole of 2023 (-49% over one year). The wait-and-see attitude of investors has led to restraint in the market. By main countries, real estate investment volumes were highest in the United Kingdom, France and Germany. By asset class, it is interesting to note that the allocation methods have evolved towards more diversification. Office real estate still dominates with around 50 billion, or around 29% of the market, followed by logistics, which rises sharply with 33 billion (20% of the market), residential (33 billion), and retail (31 billion) accounting for between 19% and 20% of the market, hospitality (14 billion, 8% of the market) and healthcare (6 billion, 4%).



[2] Europe, Middle East & Africa.

Finally, Asia-Pacific is the third block (23%), with nearly $140 billion in investment for the whole of 2023. The region is dominated by Japan, which has suffered little from rising interest rates, and China. Office real estate continues to be the first asset class by volume, with $47 billion (-45% over one year), followed by logistics, with 35 billion (-28% over one year). Retail, with 31 billion (-5% over one year), hotels (9 billion, -12%) and residential (12 billion, +5% over one year) are the sectors that are resisting best. Healthcare accounted for nearly $1.5 billion transactions in 2023 (-46% over one year).



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REAL ESTATE PERFORMANCE WAS IMPACTED BY CENTRAL BANK POLICIES

The central bank's policies of raising the cost of credit to curb inflation have had repercussions on the real estate performance across different regions. Based on the latest available data from the MSCI indices, we note that **corrections have been made in all three major markets.** We anticipate that the repricing phase will continue, but in a smaller proportion compared to what we experienced between the end of 2022 and the course of 2023. We can then expect a stabilisation phase before experiencing a rebound when central banks begin to ease their policy rates.

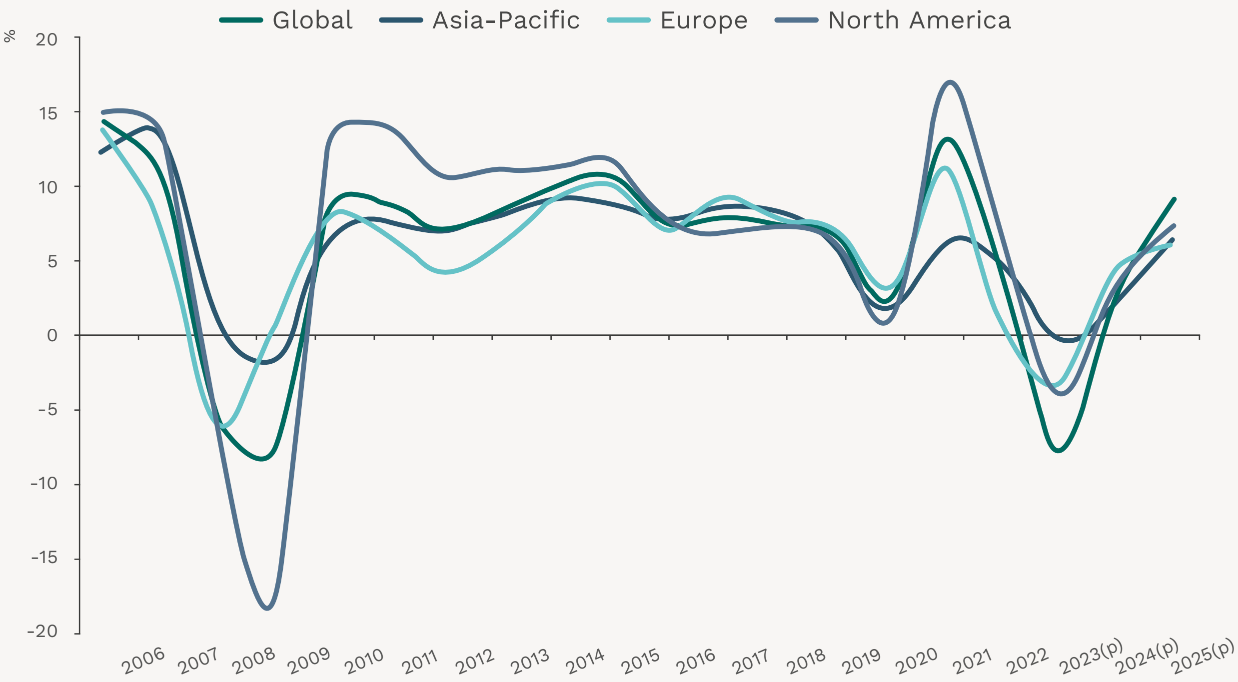
Performance: an alternative real estate premium

The analysis of real estate performance from 2006 to 2023 highlights several major lessons. First of all, the Americas, Europe and Asia-Pacific each have distinct characteristics. On the other hand, between 2006 and 2023, the average annual overall return was between 6.0% and 7.5% at fixed exchange rates in North America, Asia-Pacific and Europe. While the performance of all asset classes is fairly similar for these three major markets, **the United States has proven to be a much more volatile market for all asset classes compared to Europe and Asia-Pacific.** On the other hand, over this period, we can see that the assets have not fluctuated in the same way, with the same amplitude or at the same time. Thus, depending on the crisis, not all asset classes react identically in the three major areas.

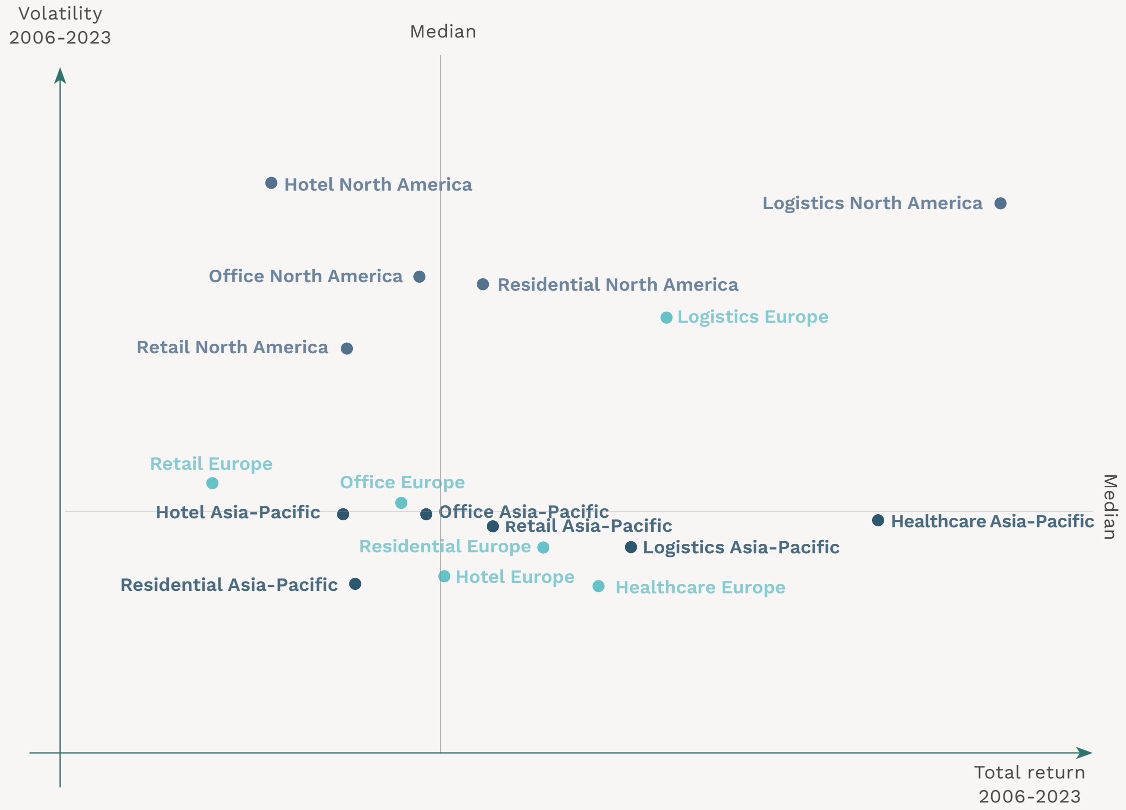
By asset class, healthcare real estate was the best performing, followed by hospitality and logistics, in the three areas analysed. Offices and residential real estate in Europe and Asia-Pacific offered a recurring return and fairly low volatility. Retail appears to be midway between all asset classes in terms of performance and volatility. This performance of retail is explained by the profound changes of recent years related to the new consumption behaviours.

Finally, the evolution of total return with its two components, namely rental return and capital gain, do not have the same characteristics. Thus, the capital gain tends to fluctuate according to the cycle, while the rental return on real estate has remained within a range of 3% to 6% on average over the period analysed, thus forming a stable component of the overall return.

TOTAL RETURN FOR REAL ESTATE WORLDWIDE FROM 2006 TO 2022 AND EXPECTED PERFORMANCE IN 2023–2025[3]



REAL ESTATE MARKET PERFORMANCE/RISK WORLDWIDE 2006–2023



[3] Index in USD.

FOR INTERNATIONAL INVESTORS, THE OPTIMAL ALLOCATION IN TERMS OF RISK/PERFORMANCE OVER THE PERIOD 2006-2023 OF REAL ESTATE IMPLIES A STRONG DIVERSIFICATION BETWEEN LARGE GEOGRAPHICAL AREAS AND BETWEEN ASSET CLASSES

The following graph illustrates the overall allocation recommended by SMARRT©, our allocation model that allows us to have an optimal view of the investment strategies combining risk and performance desired during the period 2006-2023.

We have therefore tested our allocation model, which has identified different efficient portfolios with a total return of between 5% and 8%. It appears that the optimisation of the risk/performance balance is achieved by focusing on diversification between large geographical areas internationally and between asset classes for investors who wish to diversify internationally.

When analysing the performance results for the 2006-2023 period, our model tends to focus on retail in Asia-Pacific and Europe at the expense of retail in the United States. Regarding logistics, the model tends to favour investment in Asia-Pacific over the period studied. However, it favours logistics in Europe and North America as part of a more offensive strategy, increasing respectively from 0.5% to 15% and from 1% to almost 15% of the allocation. While this evolution increases the potential return, it also increases the risk at the same time. These two consumer-related assets (retail and logistics) have a significant share in the tangent portfolio (about 30%). Indeed, one can replace the other according to the cycles and neutralise the risk.

Regarding alternative assets, it is interesting to note that the model highlights investment in healthcare real estate in Asia-Pacific and Europe, due to its resilience and the high level of return delivered by this asset class over the entire period analysed. According to our model, the share to invest in health in Europe and Asia-Pacific would be at least 10% of a portfolio, regardless of the risk and the level of return. Without market depth constraints, **our allocation model overweighs the healthcare real estate asset class.**

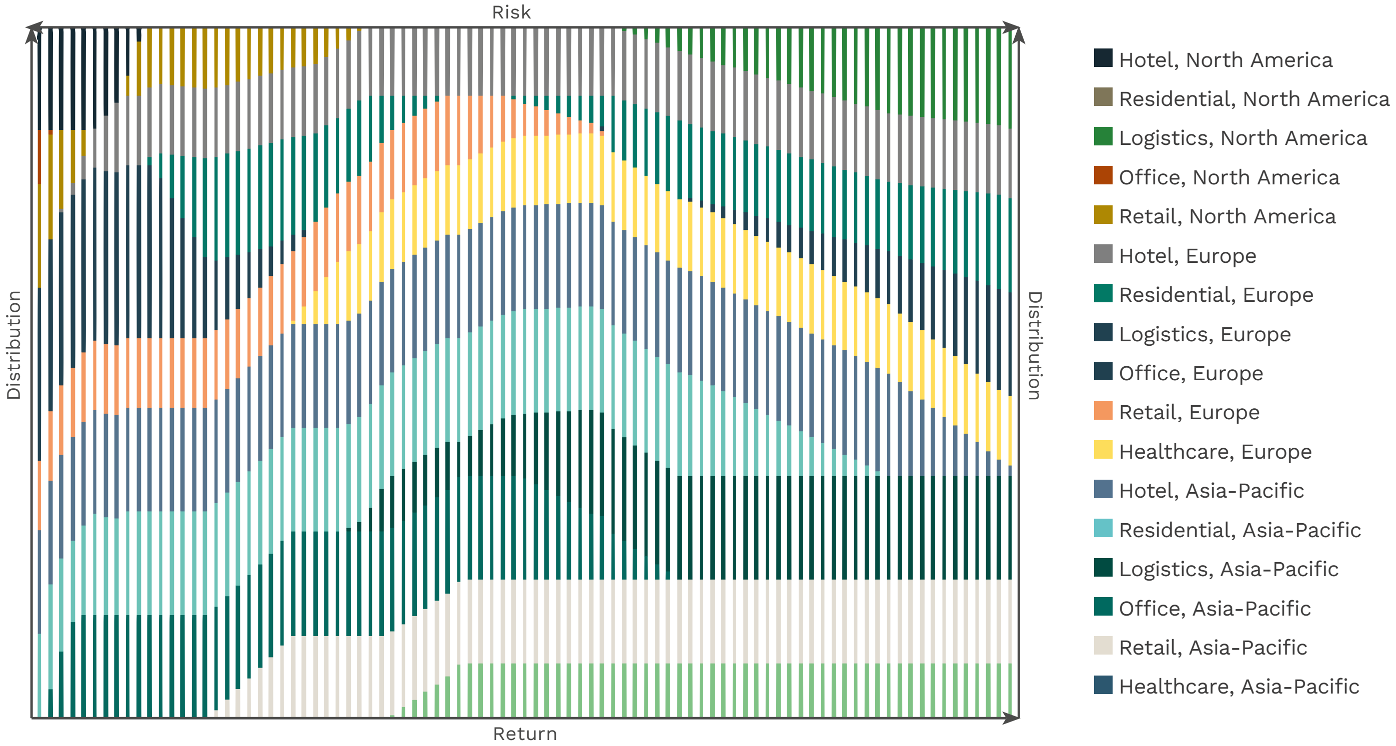
Our model tends to focus on the office in Asia-Pacific and Europe at the expense of the office in the United States, due to its high volatility over the period analysed. The volatility in the office sector in the United States can be attributed to the proactive policies of American companies encouraging remote work. This has resulted in a significant level of vacancy in many American cities and challenges in attracting employees back to physical office spaces. This behaviour has strongly impacted the value of offices in the United States, leading our model towards strong distrust. This trend has not been as prominent in Europe and Asia, where there is a greater emphasis on in-person work. Consequently, these regions exhibit a more contained volatility compared to the North American market.

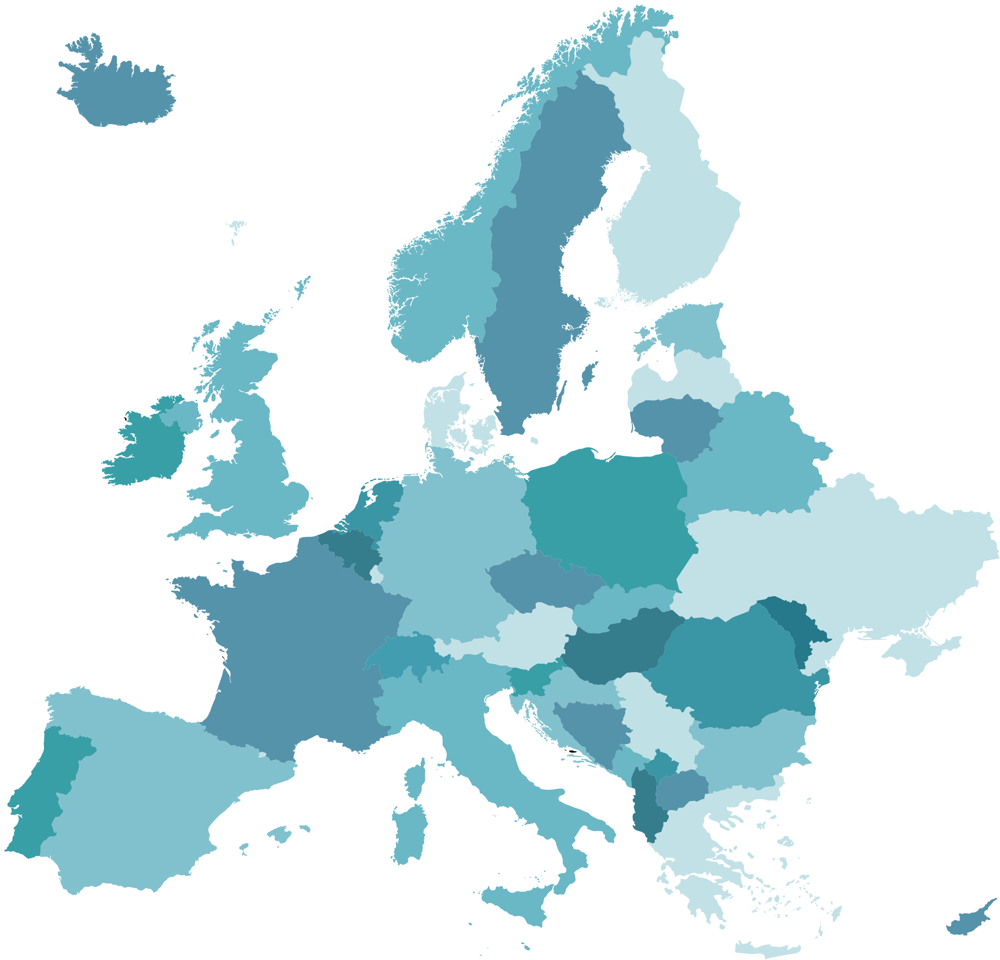
The model favours the residential sector in Asia-Pacific and Europe, up to 20% in the tangent portfolio. A resilient asset by nature, it has experienced a sharp increase in its value at the end of the health crisis. However, the crisis of major promoters in China invites us to be cautious about this asset class in this country. On the other hand, **in a more offensive approach, our model tends to reduce the share of residential in Asia-Pacific in favour of logistics in Europe and the United States.**

Regarding the hotel industry, despite the repricing phase during the health crisis, it is an asset class that has offered a satisfactory return on average over a long period. During the period analysed, our model favours Europe and Asia-Pacific, and to a lesser extent the United States.

This data is relevant for the 2006-2023 period only and cannot define future performance. An allocation policy must take into consideration the real estate cycle of each market to invest at the most opportune time. It will therefore be necessary to adapt the model according to the situations, according to the allocation strategy and according to the desired return/risk balance.

GLOBAL EFFICIENT PORTFOLIOS OVER THE 2006-2023 PERIOD ACCORDING TO THE SMARRT© MODEL





GLOBAL REAL ESTATE OUTLOOK:
EUROPE MAY EMERGE AS A FRONTRUNNER

The current consensus is that global GDP growth and inflation are expected to slow down in 2024, reflecting the easing of certain factors supporting economic activity and the delayed impact of interest rate hikes. This slowdown will lead the main central banks to intervene by easing their restrictive monetary policy to support the economy.

By major geographical areas: we anticipate that the ECB's key rates have entered a stabilisation phase and that **a phase of lower interest rates should begin in 2024, paving the way for a new real estate cycle.** The Asia-Pacific region is expected to experience further contained declines in the value of capital. However, with looming challenges (very high debt, widespread youth unemployment), the health of the Chinese economy remains a concern for the Asia-Pacific region. It is in this context that the rating agency Moody's lowered the country's sovereign rating in December 2023, from "stable" to "negative". The crises that China is currently experiencing could have a strong impact on the country's real estate values. Finally, concerning the American market, it could be the last market to complete its repricing phase with a potential impact on the banking system.

In terms of mega trends, we believe that the logistics sector in the three major markets, and the healthcare and hotel sectors in Europe and Asia-Pacific, will outperform the average due to favourable fundamentals. Retail on the ground floor of buildings in shopping streets and residential will show performances that are similar overall to the average of the global market. We anticipate that inflexible offices will be the worst-performing assets, due to their non-compliance with new energy standards. Conversely, well-located "prime" offices aligned with ESG policies are expected to be more resilient and outperform.

However, the outlook for real estate performance could be impacted by different elements depending on the markets in 2024 and 2025, such as:

- the continued transmission of rate increases to the market;
- the value in certain markets within the zones could still be impacted in 2024 due to risk premiums that are not fully reconstituted;
- a more marked slowdown in global GDP growth;
- a global financial crisis and/or a liquidity crisis.

Sources used throughout the document: Statistical models from Primonial REIM Research and Strategy, CBRE, Savills, BNP PRE, JLL, Knight Frank, MSCI-RCA, Oxford Economics, Eurostat, OECD, IMF, FED, BOK, BOJ, BOC, Stabel, NSI, CZSO, DST, Destatis, Stat, CSO, Statistics, INE, INSEE, DZS, ISTAT, CSB, Statistics Lithuania, Statec, KSH, CBS, Statistik Austria, Stat Poland, INE, INSSE, SCB, SSB, BFS, ONS.

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