EXECUTIVE SUMMARY

- Economic and real estate indicators for industrial and logistics real estate markets remain positive, but the general outlook across EMEA is uncertain. Protectionism fears are high on the agenda, and while Donald Trump and Jean-Claude Juncker agreed to hold off on imposing tariffs in July, a history of unpredictability means there is no room for complacency. The latest industrial PMI readings depict a trend of declining confidence – for the eurozone as a whole, and the major economies within. All key European economies are reporting declines in their index levels relative to 12 months ago.
- Despite these potential challenges, demand for industrial and logistics space enjoyed an expansive H1 2018 resulting in a significant rise in gross take-up. Over 50% of markets surveyed reported an expansion in demand compared with only 35% during H2 2017. Equally, the percentage of markets witnessing a decrease in take-up fell from 54% to 46%.
- Demand growth could have been higher but for a lack of quality, modern space. Vacancy rates remained very low in H1 2018, with the vacancy average across markets surveyed at 5.7%. Vacancy rates below 3% were reported in a range of locations including Lodz, Belgrade, Warsaw, London, Munich and Milton Keynes.
- Construction pipelines remain restricted, although conditions slightly improved relative to end of 2017. Some 52% of markets reported an increase in their pipelines in H1 2018 compared with 51% in H2 2017, but the percentage of markets registering falls in their development pipelines reduced from 40% to 32%.

- There are big discrepancies across Europe. In Poland, the vast majority of newly delivered supply in H1 2018 originated in the inner region of Lodz, where space under active construction (570,000 sq m) represented 28% of total modern stock in H1 2018. The pipeline was slightly above the 5-year average take-up level, but against a backdrop of extremely low vacancy of 0.79%.
- In other major markets such as Stockholm, Berlin and Munich, pipelines remain very low, at sub 100,000 sq m. Munich and Berlin are in much need of speculative development, but there are a number of obstacles to planning, not least from municipalities. In Munich, for instance, municipal authorities are reluctant to give planning permission for industrial developments, because they are associated with an increase in traffic, noise and pollution.
- The scarcity of industrial sites and planning constraints is pushing developers/investors into more creative development solutions. In some cases, outdated office parks are being transformed into modern logistics and business parks. The redevelopment of Port Park Pernis in Rotterdam will be the new headquarters and distribution centre of Nestle-Vat Logistics, in premises spanning 45,000 sq m. In Barcelona, where supply has been a major constraint on growth, Segro is regrouping the old Bacardi rum factory in Mollet del Vallés (Barcelona), to convert into 40,000 sq m of logistics space. Additionally, developers are turning to brownfield locations. In Cologne, Alcaro Invest is building a 26,000 sq m logistics centre on a brownfield site in Karpen, and refurbishing over 15,000 sq m of office and warehouse space in Frechen.
- Markets reporting landlord-favourable conditions expanded to a 41% coverage during H1 2018, although an equal number of markets reported neutral occupier conditions. Prime rents in both the logistics and distribution and city warehouse segments remained stable or grew in most of the EMEA cities monitored.

KEY METRICS IN MAJOR EMEA CITIES: H1 2018

<table>
<thead>
<tr>
<th>CITY</th>
<th>PRIME RENT</th>
<th>CITY WAREHOUSE RENT</th>
<th>PRIME RENT</th>
<th>LOGISTICS &amp; DISTRIBUTION</th>
<th>VACANCY</th>
<th>TAKE-UP</th>
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<tr>
<td></td>
<td>CITY WAREHOUSE RENT</td>
<td>PRIME RENT</td>
<td>LOGISTICS &amp; DISTRIBUTION</td>
<td>VACANCY</td>
<td>TAKE-UP</td>
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<td></td>
<td>€/SQ.M/ MONTH</td>
<td>€/SQ.M/ MONTH</td>
<td>€/SQ.M/ MONTH</td>
<td>(%)</td>
<td>(SQ M)</td>
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<td>Barcelona</td>
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<td>7.21</td>
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*UK industrial data relate to the region

Sources: Colliers International
MACROECONOMIC OVERVIEW

Macro Overview

Economic indicators in Europe remain positive, but the general outlook is uncertain. In late July, Donald Trump and Jean Claude Juncker agreed to hold off on imposing tariffs while trade negotiations are ongoing, providing a welcome respite to the protectionist measures.

That said, a history of unpredictability by the US President means there is no room for complacency, and as the relationship with key trading partners the EU and China becomes strained, investor and industrial confidence diminish. As the latest industrial PMI readings show, the trend for the eurozone as a whole — and the major economies within — is one of declining confidence. All markets are reporting declines in their index levels relative to 12 months ago.

Looking at the worldwide view, the current consensus global GDP forecast from Oxford Economics has been revised down by 0.1% (to 3.1%) for 2018. In the eurozone, the GDP growth forecast was also revised down by 0.1% (to 2%) for 2018, and from 1.8% to 1.7% for 2019, due to the impact of expected US tariffs on imported European cars. If it escalates, the trade dispute would hit Germany and France the hardest, as the core automotive production regions of Europe.

Meanwhile, in the UK, the risk of a Brexit ‘no deal’ outcome has come into increasing focus during the summer months. Companies such as Ford, Jaguar Land Rover, BMW and Airbus are some of the bigger names to have expressed serious concerns about the possible repercussions a no-deal scenario would have on their UK production operations.

The UK would revert to WTO rules, a disruptive development for the economy at large. Even if the UK and the EU strike a withdrawal agreement, there is a chance it could be rejected by parliament, with an ensuing political crisis.

In other European countries, the Czech and Polish PMI readings went down sharply to an 11-month-low in July. The Polish PMI fell to 52.9, and the Czech reading dropped to 55.4 — these readings remain above the 50 ‘growth watershed’ marker, so the markets continue to expand but at reduced rates of growth. The Spanish and Italian PMIs also fell in July, to 10-month and 20-month lows, respectively, despite a robust reading of 52.9 in Spain.

Oil Prices & Inflation

Trump’s withdrawal from the Iran nuclear deal in May, and the forthcoming US sanctions on Iran to be imposed in November, have led to an increase in oil prices. This price rise could dampen activity in the industrial and logistics sector, eating into the margins of distributors and, in the longer term, negatively impacting consumer spending – and thus demand for logistics. Inflation is picking up in Europe, with three of its largest economies — Germany, France and Spain – reaching above the European Central Bank target of 2% in June. The eurozone headline inflation was confirmed at 2.1% in July, the highest rate since late 2012. This could exert pressure on disposable incomes, leading to weaker consumption and thus, lower GDP growth rates.
Shrinking labour pool impacts the market

Falling labour market capacity has become a challenge for the industrial and logistics market, as employment expectations grow across Europe. In an increasing number of locations, the undersupply of labour is starting to act as an inhibitor to growth, or as a driver of relocation decisions. We are witnessing a number of companies seeking out new pockets of under-utilised labour pools across Europe to help stabilise their production footprint. As a counter to this, some manufacturers are increasingly resorting to automation.

On the bright side, falling unemployment is boosting wage growth, which in turn is driving consumption and domestic demand. This is helping to drive the industrial and logistics market, counter-balancing capacity constraints.

Take-up imbalances fuelled by a scarcity of modern space

There was a significant rise in gross take-up during H1 2018, with 50% of markets reporting an expansion in demand compared with only 35% during H2 2017, a figure consistent with an environment of strong demand by industrial and logistics tenants.

In Germany, the Big Seven (Berlin, Hamburg, Dusseldorf, Cologne, Munich, Frankfurt and Stuttgart) markets generated take-up of 2.7 million sq m in the 12 months from July 2017 to June 2018, down -5% year on year, but with big discrepancies across these markets. Cologne (-44%), Munich (-38%), Hamburg (-24%), and Berlin (-19%), all suffered significant declines. Dusseldorf grew by an impressive 61%, Frankfurt by 23%, and Stuttgart by a more modest 5%.

Take-up in the Netherlands displayed healthy annual growth of 14%, based on the 12-month rolling take-up to end Q2 2018. Activity was driven by industrial hotspots. The Schiphol-Rijk region, located outside Amsterdam and near the airport, continues growing as an industrial hub, with year-on-year (y/y) take-up growth of 178%. In Rotterdam, y/y take-up expanded by 99% on the back of trade around the port. The Venlo region, located near the German border, displayed decent take-up growth of 20% (y/y). The Tilburg region registered take-up growth of 12% (y/y).

The Spanish market had strong performance, displaying 12-month rolling take-up growth of 86% (y/y). This was mainly driven by activity in the Madrid region, which expanded by 81% - Barcelona growth was relatively muted at only 5%, but is severely constrained by a lack of existing availability - vacancy is at 2.7%, and the current pipeline appears inadequate to satisfy demand levels.

In Poland, tenants leased 1 million sq m of modern industrial space in H1 2018 across the country. Looking at the 12-month rolling figures, the fastest rate of take-up growth (56%) came from the traditionally industrial area of Lodz, in the Central Poland region – there has been around 1 million sq m of total take-up in this area over the last 12 months. Warsaw saw annual growth of 16%, having reached also 1 million sq m in total take-up over the last 12 months. The second fastest-growing location (45%) was the city of Wroclaw in Western Poland, reaching 465,000 sq m in annual take-up.
Vacancy decreases driven by lack of new completions

Vacancy rate compression continued during the first half of 2018. The percentage of markets registering vacancy declines was up by 2% to 58%, while the number of markets reporting vacancy rate rises dropped to 22% from 24% at end 2017. The outlook for the next 12 months is consistent with current trends, with declining vacancy rates expected in 55% of markets.

A closer look at vacancy by city size reveals some differences by market size. Downward pressure on vacancy is easing in mega cities (10+ million population), with a decrease of -15% by end of H1 2018, compared -35% falls registered during H2 2017. Yet the pace of vacancy rate compression is much higher than in large cities (5-10 million population) which saw vacancy declines slow from -8% in H2 2017 to -4% in H1 2018.

Vacancy rate compression varies by city. In Amsterdam, available supply has fallen significantly, from 600,000 sq m to just over 200,000 sq m in eight years’ time, reducing the vacancy rate from over 17% to 7% during the same period, but vacancy is still high when compared with the EMEA average of 5.7%.

In the UK, industrial vacancy reached very low rates in Milton Keynes, at 2.9%, Hemel Hempstead, at 3%, Northampton at 3%, Greater London at 3.4%, and Birmingham at 3.6% as of end H1 2018. Speculative development was reasonably active over the last 12 months in the UK, but demand continues to outstrip supply, and new schemes to market are usually pre-let or soon after completion.

Comparing these rates to Athens (15%) or Istanbul (14%) for example, gives a measure of the disparities across EMEA.

Construction pipelines are constrained in many markets

In a positive sign for the market, the development pipeline looked slightly more robust by end of H1 2018 than in the previous six-month period - 52% of markets reported an increase in their pipelines in H1 2018 compared with 51% in H2 2017. Meanwhile the percentage of markets registering falls in their construction pipelines went down from 40% to 32%.

In Cologne, developers are focusing on revitalising obsolete space, and most of Cologne’s take-up in this city was achieved through rentals of existing space. Munich and Berlin are in much need of speculative development, but there are a number of obstacles to planning in town centres, thus the popularity of industrial parks, where there is no residential element involved, is rising. In Berlin, a pick-up of large-volume rentals is forecast to take place in H2 2018, which may stimulate take-up and maybe even speculative development of new construction projects.

In Dusseldorf and Frankfurt, there are healthy construction pipelines, with new development projects due to mature in H2 2019. Rents for modern space remain constant, particularly in sub-markets such as Frankfurt am Main and Groß-Gerau, near the airport. Dusseldorf is also strong, with large-volume development projects boosting the market, although take-up is expected to moderate in H2 2018. In Hamburg, several construction projects are expected to complete by end of H2 2018.
City Warehousing

Rental growth in city warehousing across EMEA showed signs of stabilising in H1 2018 when compared with H2 2017, with the percentage of markets displaying a slowdown in rental growth at 19% as of the end of the first half of 2018, compared to only 2% at end 2017. Some of the best performers in the city warehouse space in H1 2018 included Venlo (10%), Munich (9.4%), Greater London (7.4%), Birmingham (7.4%), Rotterdam (7.1%), Madrid (6.3%), and Prague and Barcelona (both 5.9%).

The outlook over the next 12 months is for a greater degree of rent stability, with 64% of markets expecting rents to remain the same, up from 56% in the previous outlook.

Logistics/Distribution Rents

Regarding the logistics and distribution segment, the top performers included Venlo (11.1%), Rotterdam (7.7%), Stockholm (5%), Greater London (3.9%), Hamburg (3.4%), Budapest (2.6%) and Munich (2.2%). The weaker performers were again Istanbul (-4.3%) and Moscow (-10.5%). Barcelona, Prague and Madrid were some of the cities to display flat growth.

Factors influencing rental prices

Factors such as last-mile location and proximity to infrastructure continue to influence pricing. At other times, it is a simple function of demand far outstripping supply.

In London, Crossrail and Crossrail 2 are already impacting industrial rents, for instance in Woolwich (up 33% y/y to £16 per sq ft in the 12 months from July 2017 to June 2018), and in Tottenham (up 30% y/y to £14.50 per sq ft in the same period). The delivery of Crossrail 1 is now scheduled for late 2019, and Crossrail 2 is still in the initial phase. Similarly, due to the proximity to Gatwick airport and a chronic lack of Grade A supply, prime rents in Crawley also grow by an impressive 3.3% to £14 per sq ft over the same period.

Another factor exerting upward pressure on rents is demand for last mile and local distribution centres. There is increasing decentralisation at the end of the supply chain as occupiers continue to push into the urban core, where consumption is rising fastest. Significant undersupply and the loss of industrial land to other uses, is exerting upward pressure on prime rents in Croydon, owing to its strategic south London location, at £14.50 per sq ft (+32% y/y). Similarly, Merton’s rents are now reaching £15 per sq ft (+30%, y/y). Around London, overall some of the highest prime industrial rents remain in Park Royal (with demand for last mile distribution combined with relative proximity to Heathrow airport) pushing rents up to £17.50 per sq ft, above Heathrow’s £16 per sq ft rents. In the last 12 months, there was significant growth in other West London locations, with Acton now achieving £17 per sq ft.
MARKET OVERVIEW: OCCUPIER CONDITIONS

Despite a cooling of rental growth, limited development pipelines and availability continue to push the drive to landlord favourable markets. They account for 41% of markets as of end H1 2018, compared to only 31% of the total two years ago. The percentage of neutral markets has remained broadly the same during the two-year period, ending at 41% of markets by end of June 2018. Overall, this has seen the relative number of tenant favourable markets drop to only 18%.

Germany remains one of the strongest markets, with Berlin a landlord-favourable market since Q2 2017, Hamburg since Q1 2016, and Stuttgart, Dusseldorf and Munich, since Q2 2015. Cologne has been the longest-running landlord-favourable market, since Q4 2014.

The outlook for these cities is to continue enjoying these conditions. Stockholm has been landlord favourable since Q1 2015, however it is softening with the outlook set for a neutral environment starting in the next few quarters.

The evolution of Eastern European countries is interesting to watch, with the Czech Republic turning landlord favourable in Q3 2017, after several quarters as a neutral market. In Budapest the market turned landlord-favourable in Q1 2017. Warsaw overall remains a tenant favourable city, but in the Warsaw III sub-market covering the outer distribution ring of the city, the latest indicators now point to a landlord-favourable market.

Sources: Figure 11: Colliers International

FIGURE 11
EVOLUTION OF OCCUPIER CONDITIONS

Sources: Figure 11: Colliers International
**AROUND THE MARKETS**

**NETHERLANDS** Demand for I&L space is driven by growing business in trade niche sectors like the port of Rotterdam, Venlo on the border with Germany, and the industrial hub around Schiphol airport. In Rotterdam, logistics services provider Deltic, is developing a distribution centre with head office for Rebel-list, spanning 45,000 sq m. In the southern region of Tilburg, retailer Bijenkorf announced the opening of a new distribution centre to supply all stores, as well as e-fulfilment activities. In Amsterdam, demand comes from growing requirements for city distribution in e-commerce, and growth in the construction and hospitality industry. Deals including Clipper Logistics taking 615,000 sq ft in Sheffield, the largest deal for a second hand unit in 2018.

**GERMANY** Performance was polarised where vacancy rates were just under 1% in June 2018. Demand for industrial and logistics properties are on high, driven by the automotive industry and production growth of machinery and equipment. H1 2018 (40%) came from retail on the East and Yorkshire saw several large deals including Clipper Logistics taking 615,000 sq ft in Sheffield, the largest deal for a second hand unit in 2018. Although demand from industry is growing, the biggest share of take-up in H1 2018 (40%) came from retail on the back of demand for units over 100,000 sq ft, including food retailers like Lidl.

**HUNGARY** Developer activity continues unabated, with demand for each segment, supply in this fast-growing market continues high. Real estate developer and manager CTP started construction of new premises in Székesfehérvár which will expand the developer’s futureulative space in the area to 450,000 sq m and in Dunaharaszti. The retail sector was displaying strong activity, and Berlin and Munich, where a severe undersupply of modern premises, particularly in city locations, is slowing down the market. Take-up of 330,000 sq m in Frankfurt reached 246,000 sq m (Hamburg) and 104,000 sq m (Düsseldorf) was achieved in H1 2018, with the latter growing by more than 80% year on year. In Düsseldorf, deals of note included the lease of 15,000 sq m by beverage retailer Flaschenpost. The largest owner-occupier deal involved an operations centre built in Hamburg by logistics operator Flaschenpost.

**DENMARK** Modern industrial and logistics properties are in high demand from both investors and occupiers. Vacancy rates have been steadily declining since 2012, reaching 2.1% in H1 2018. In H1 2018, the gross take-up reached 615,000 sq ft and on track to exceed the long-term average in H1 2017. With demand increasing by 7% annually, there is a sharp imbalance between demand and supply, and vacancy rates in the central region continued to decline, reaching 2.1%. Retail rates were flat but are forecast to grow on the back of healthy, stable demand and the completion of new, high-quality warehouse buildings.

**POLAND** Most construction sites are located in the Central Poland region (around 350,000 sq m). The largest project currently under construction is Logistics Zalew, which will provide modern warehouse space of around 262,000 sq m. The highest level of supply was also recorded in Central Poland (286,000 sq m), where vacancy rates were just under 1% in June 2018.

**LITHUANIA** Strong developer interest in Lithuania translated into 55,000 sq m under active construction in Q2 2018. Most of the activity remains in the two main hotspots like the port of Rotterdam, Venlo and the industrial hub around Schiphol airport. In Rotterdam, logistics services provider Deltic, is developing a distribution centre with head office for Rebel-list, spanning 45,000 sq m. In the southern region of Tilburg, retailer Bijenkorf announced the opening of a new distribution centre to supply all stores, as well as e-fulfilment activities. In Amsterdam, demand comes from growing requirements for city distribution in e-commerce, and growth in the construction and hospitality industry. Deals including Clipper Logistics taking 615,000 sq ft in Sheffield, the largest deal for a second hand unit in 2018.

**RUSSIA** New supply of industrial space in H1 2018 amounted to 41,800 sq m, 50% lower than in H1 2017. With demand increasing by 12% annually, there is a sharp imbalance between demand and supply, and vacancy rates in the Moscow region continued to decline, reaching 2.6%. Retail rates were flat but are forecast to grow on the back of healthy, stable demand and the completion of new, high-quality warehouse buildings.

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**Greece** Demand for industrial space has remained stable during H1 2018 driven by occupancy in the top three spaces from 1,000 to 2,500 sq m and above 3,500 sq m. These size cohorts are experiencing really constrained availability. A key major new development by Europlate Logistics Gr. is in construction, with the first phase of the 120,000 sq m freight centre in "Thriassio Port". With a total budget of €70 million, this project is likely to drive demand of industrial space towards the western region of Athens.
OUTLOOK

Fierce competition for warehouse space and very limited availability will continue to weigh heavily on activity over the remainder of 2018, and most likely well into 2019. Looking at the macroeconomic picture, there are a number of uncertainties ahead that weigh heavily on the outlook for industrial/logistics real estate. The UK market has remained bullish in the face of Brexit, but there are big uncertainties around the impact of a possible ‘no deal’ outcome for supply chains after March 2019, when the UK is expected to be officially outside the EU. It is difficult to predict the course of events, and whether currency exchange fluctuations or inflationary pressures will be absorbed by the supply chain or passed on to consumers.

That said, UK rental forecasts remain positive for the UK industrial sector, set to outperform the other core property sectors in 2018-2022. According to the all-industrial MSCI rental index, they expect an uplift of 3.7% in 2018, slowing to 2.4% in 2019, before resuming an upward trend, bringing the 5-year average annual growth to 3.2%.

In the EU27, Germany and the Eastern European automotive regions, would be disproportionately affected by the trade wars with the US. Optimism in the manufacturing sector is at its lowest in almost three years, according to Markit, and a key theme in the latest survey is sharp inflationary pressures in the manufacturing sector. Inflation could also weigh on the outlook with businesses reporting more muted activity over the next few quarters in the latest Markit/PMI survey.

Generally speaking, occupiers looking for industrial accommodation in key geographies like Germany, the Benelux region and Scandinavia must prepare for further rental uplifts, but the market is stabilising in places. In cities including Stuttgart, Munich, Barcelona and Budapest, healthy demand will be clashing with reduced supply, but in cities like Lodz in Poland, active pipelines could be holding back uplifts in rental rates. A scarcity of land and labour are two of the most important factors acting as inhibitors of market growth. Technology will increasingly play a role in evolving roles in production and in creating more efficient supply chains. The I&L sector will have to evolve with the times to remain competitive, in terms of technological advancements. The fourth industrial revolution will mean that increasingly sophisticated automation will be a reality of ever more warehouses around EMEA.

The rapidly evolving e-commerce sector may also encounter challenges that could impact industrial real estate, such as increasing fiscal regulation. Recently, debate around business rates in the UK has come to a head, with the UK chancellor discussing an ‘Amazon tax’ to create a more level playing field between e-retail companies and traditional, notably high-street driven, companies.

As the e-commerce sector continues to grow and consumer demand increases, investors must prepare to adapt to new ways of doing business. Fierce competition for warehouse space and very limited availability will continue to weigh heavily on activity over the remainder of 2018, and most likely well into 2019. Looking at the macroeconomic picture, there are a number of uncertainties ahead that weigh heavily on the outlook for industrial/logistics real estate. The UK market has remained bullish in the face of Brexit, but there are big uncertainties around the impact of a possible ‘no deal’ outcome for supply chains after March 2019, when the UK is expected to be officially outside the EU. It is difficult to predict the course of events, and whether currency exchange fluctuations or inflationary pressures will be absorbed by the supply chain or passed on to consumers.

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