GLOBAL CAPITAL DIVERSIFICATION: EUROPE IN CONTEXT
Global real estate assets under management (“REALM”) doubled over the latter half of the investment cycle with the top 100 global fund managers increasing REALM from $1.6 trillion in 2014 to $3.3 trillion at end 2018. Meanwhile REALM held by the top 10 global fund managers expanded by 60%, pointing to increasing levels of global capital diversification.

While institutions account for the bulk of activity, the growing influence of high net-worth individuals (HNWIs), sovereign and family wealth is changing the global capital landscape. They now own a similar level of assets globally.

So when we consider that increasing allocations to real estate from global institutions reached at least $840 billion in 2018, this figure could be twice the size when accounting for HNWIs and family offices. Given that the institutional allocation to real estate only reached 10.4% as of end 2018, further expansion is expected. As allocations continue to expand alongside levels of wealth, new capital looking at real estate could hit $2.5 trillion by 2020, if we reach a 12.5% allocation.

When we review closed-end real estate funds specifically, we can also see a strategic shift in activity. The new funds raised have generated a $340 billion war-chest to be deployed to real estate in 2019, with the bulk of money aimed at opportunistic, value-added and debt plays. Available capital in debt funds was up to $61 billion as of March 2019, and is clearly en-vogue. Colliers’ proprietary analysis of a range of global investors shows that at least two thirds either have, or are in the process of, deploying more funds in debt vehicles and structures, some with a particular focus on development. This reflects the shift in acquisitions we have seen in recent years, as structural and late cycle factors shape activity.
Diversity Trends
Colliers has reviewed the activity of a select range of global investors, from a range of different domiciles and at various stages of global expansion. We have steered away from the biggest global investors, which would skew the results, sticking with those that Colliers know to be actively expanding across Europe and globally. This highlights some interesting trends globally, and of specific relevance to activity in Europe. The investors chosen have been anonymised.

In summary, what we can see is that APAC and European domiciled investors tend to be the most adventurous in terms of the number of countries, cities, sectors they focus on – and the rate of expansion in activity has been vast since 2010. As of end 2018 they are far more diverse than their Australian and North American counterparts.

In our analysis of North American investors, we have seen an effective consolidation of activity, whereby two of those analysed have reduced the number of assets, sectors and cities they are active in, sticking with bigger assets in bigger cities. Our analysis of Australian investors shows that they are expanding globally, and by sector but on a measured and select basis.

Sector Momentum
Global and European investor trends clearly point towards growth in residential investment activity primarily, followed by growth in industrial/logistics investment. Investment in offices has maintained a high market share, while retail has seen investment activity decline until 2018 when it started to rise again, just ahead of industrial/logistics.

Colliers’ analysis of select global investors who are increasingly active globally shows a clear amplification of these trends. Although offices and retail continue to dominate activity in terms of size, the clear momentum in activity is behind residential (in all its forms), followed by industrial/logistics, hotels and increasingly development. In fact it is the increase in activity in development land/sites that is most striking, as investors see a different, late-cycle route to market. As mentioned previously, the shift to debt is also significant, and represents another longer-term diversification strategy.

Can Europe continue to attract global capital?
The European market has been a direct beneficiary of the increase in global capital diversification, especially in terms of fresh and increasing levels of capital from Asia. As of March 2019, the positive FX and hedging benefits of buying in Europe, combined with better yield spread positions compared to other North American and APAC markets will continue to drive global capital diversity in Europe and we expect to see greater levels of both North American and Asian capital take advantage of this.
Global gateway cities dominate

Big global cities have dominated the deployment of capital over this cycle, with New York and London leading the charge, ahead of Los Angeles, Tokyo and Paris. A further four markets – Hong Kong, Washington DC, San Francisco and Chicago join the global gateway club of nine that have amassed more than $100 billion of investment since 2008.

A striking trend across many major global cities is the growth of international, cross-border capital, yet there are clear differences by geography. London really stands out as a truly global city with around 70% of investment generated outside of UK borders, encompassing an increasingly balanced range of domiciles from the Americas, Asia and Europe.

Many of the major US markets are almost the reverse being only 20-30% cross-border, with the bulk of this coming from north of the border.

The New York metro area is in-line with this trend but central Manhattan has been a bigger international magnet, where cross-border activity accounts for closer to 45% with diverse sources of European and Asian capital taking positions in the market.

Within Europe, the major German cities of Berlin, Munich and Frankfurt alongside Stockholm form the European contingent of the next big group of global cities, witnessing between $50-100 billion in investment activity since 2008. Madrid and Amsterdam have been picking up momentum recently and moving into this sphere of influence. The role of cross-border capital continues to expand across European cities and is at or well above the 50% mark.

---

**FIGURE 7:**
**GLOBAL CITY INVESTMENT VOLUMES**
**(10YR VS CUMULATIVE) VS GDP OUTPUTS | 2018**

Sources: Figure 7: Colliers International, RCA, Oxford Economics
GLOBAL INVESTOR DIVERSITY

Across the global cities surveyed, European markets are the most capital diverse, with Sydney not far behind. North American cities tend to be dominated by domestic and North American capital, although the global gateway cities of New York, LA and San Francisco are more international.
In Europe, all the major cities have seen increasing levels of cross-border activity, with only the odd exception. Stockholm tends to be by domestic investors and is yet to witness any significant international cross-border activity. Warsaw is the reverse. The other key feature is cross-border activity comes from European and EMEA-domiciled investors, while North American investors play a role everywhere. Yet Asian-domiciled activity is starting to expand into more locations including the core German, UK and Paris markets but also further afield into Amsterdam, Madrid, Lisbon, Helsinki and Warsaw. Asian capital rose to 30% of all cross-border activity in 2018, double the rate of 3 years ago, and we expect it to diversify across a broader range of cities and sectors in 2019 and beyond.

As the influence of Asian capital grows alongside the diversity of investors, we expect to see a bigger influx of international capital into a range of key European cities, especially those with a good story to tell.
EUROPEAN CITY INVESTMENT TRENDS

Market Momentum vs Critical Mass

Within Europe recent investment momentum has been into late economic/occupier cycle markets operating at higher yields. This has seen Helsinki and Lisbon topping the momentum charts.

Of the longer-term, top ten European capital destinations this cycle, only Amsterdam and Frankfurt sit within the group of currently active markets, although Paris La Defense features at a sub-market level - all three locations have benefited from their position as the most likely net benefactors of any Brexit-related corporate relocations, plus their record low vacancy levels for grade A space, driving office rent growth.

Other key cities that have benefited from a late-economic/occupier driven upswing in investment are Dusseldorf, Vienna, Utrecht and Rotterdam and make up the most active group of city markets compared to their five year point.

When we look at activity in terms of volumes, however, London remains out in front ahead of Paris, highlighting that critical mass and liquidity continue to drive investors to the key gateway cities. The other factor that will continue to drive investment activity, notably for offices, is the very tight levels of availability across a multitude of locations. With the balance of supply and demand remaining largely in favour of landlords, and thus supportive of further rental growth in 2019. Very few cities have vacancy rates of over eight percent, and many of those that do are seeing vacant space being absorbed rapidly.
OFFICES

The role of flexible workspace

By sector, the rapid growth of flexible workspace has grabbed the headlines, with flexible workspace operators expanding by close to four hundred per cent in the last few years. Yet when compared to levels of modern stock per city, at most it represents 5% of the market in the most mature flexible workspace cities of London and Amsterdam. It’s only around 1% in many other major European cities, and is clearly being implemented by an increasing number of landlords as a part of their overall client focused offer. A balanced view of market participants expect it to reach 10% or more of modern office space, driven by the occupier and market requirement for shorter leases and flexibility.

Our view is that the risk to office investment is somewhat misplaced, but it needs to be included and priced in as an important element of office portfolios going forwards. Managing Capex is clearly an increasingly important challenge for landlords/investors at the heart of this, despite the rental premiums being charged for flexible vs conventional office space. Maintaining these premiums should be achievable short-term, as conditions across the vast majority of office markets are in favour of landlords, with very tight vacancy and availability underpinning rental growth and values in 2018. Over the mid-term, as employment and economic growth slows, getting the flexibility balance right will be important as a loosening of occupier conditions could impact the demand and premium dynamic.

For a more in-depth view of current office trends across Europe, please link to our latest office snapshot here.
INDUSTRIAL & LOGISTICS

City logistics or distribution centres?

While logistics has benefited from the growth in e-retailing, we are now seeing signs of this hitting penetration across Europe. Pureplay retailers are resorting to omni-channel to survive and deliver profits, putting the onus back on the need for retail space supported by modern logistics.

The headline outcome is twofold
1. Countries moving off a low e-retailing base with room for further growth will continue to see an increase in demand for new logistics space.
2. All countries will see further growth in demand for modern logistics space, as the shift towards omni-channel will require the ongoing replacement of older logistics stock.

The type and scale of opportunity to deliver new logistics facilities will, however, differ markedly by location.
1. The major European distribution core locations will benefit from demand growth for regional and sub-regional distribution/big-box space.
2. We could well see growth in cross-docking demand around major European cities, fulfilling timely delivery needs. This is particularly likely in cities pushing a car free agenda/policy. Cross-docking will keep bigger trucks out of cities, with leaner and cleaner, small e-vans distributing goods within a city. Freight is one of the biggest contributors to congestion and missions, and cities like Oslo, Hamburg, Copenhagen and many others are already addressing this challenge.

While urban/city logistics demand growth is clearly a growth trend, the shift towards microhubs appears smaller than anticipated by landlords and investors. A recent study by Colliers Germany points to a big disparity in expectations at this level, as the consensus of occupier demand supports units of 5,000-10,000 sq m+ aka, big box, e-fulfilment and cross-docking.

Demand for smaller micro-hub units of 1,000 – 3,000 sq m units is limited. The lack of city-logistics product being developed across European cities reflects this, which is driven by the inability of logistics rents to generate gross development values that can get close to existing use values in cities.

Demand for micro-hubs will be possible when facilitated by the delivery of mixed-use space, be it new or old (such as in the form of empty office car parks and ground floor units), and this is where we expect to see opportunities emerge via the creation of mixed-use communities.

To get a more in-depth view of trends shaping the European Industrial and Logistics market, click through to our year-end snapshot report here.

E-RETAIL
% OF HOUSEHOLD CONSUMPTION (END 2018)

TABLE 1: I&L OCCUPIER LOCATION REQUIREMENTS: LARGE (E-FULLFILMENT) VS SMALL (MICRO HUBS)

<table>
<thead>
<tr>
<th>LOCATION</th>
<th>E-FULFILMENT</th>
<th>MICRO-HUBS</th>
</tr>
</thead>
<tbody>
<tr>
<td>Industrial areas</td>
<td>27%</td>
<td>4%</td>
</tr>
<tr>
<td>Traffic junctions</td>
<td>21%</td>
<td>10%</td>
</tr>
<tr>
<td>Near motorway on-ramp</td>
<td>18%</td>
<td>3%</td>
</tr>
<tr>
<td>As close to the city centre as possible</td>
<td>18%</td>
<td>43%</td>
</tr>
<tr>
<td>Densely populated districts</td>
<td>14%</td>
<td>43%</td>
</tr>
</tbody>
</table>

FIGURE 14: E-RETAIL
% OF HOUSEHOLD CONSUMPTION (END 2018)

FIGURE 15: I&L OCCUPIER REQUIREMENTS VS DEVELOPER, INVESTOR EXPECTATIONS: GERMAN SURVEY, 2018

Sources: Figure 14: Colliers International, Statista | Table 1: Colliers International | Figure 15: Colliers International
RETAIL

Despite the bad press the retail sector has received, it certainly isn’t all bad and at a global level retail has started to come back. In Europe, major retail destination locations and dominant shopping centres have continued to deliver results over the course of this cycle, leading to growth in retail capital values. Although capital value growth has slowed relative to offices and industrial/logistics in Europe, forecast growth in consumption levels and slower rates of e-retailing penetration should result in retail bucking its unpopularity trend.

We have recently witnessed the benefits a strong branded store can provide all retailers, notably those engaging omni-channel strategies via varying forms of showroming. The fact that this can drive higher on-line sales as a result of higher brand visibility in local areas is increasingly persuading pure-play retailers to reverse engineer retail space into their on-line portfolio.

This will continue to drive demand for retail space across markets, especially in strong, tourism-led locations where a physical presence is necessary. Experiential retail incorporating Food and Beverage (F&B), leisure, and various forms of pop-up retail and events will continue to drive demand for retail space. Increasing use of residential can help deliver effective mixed-use space and place. Evidence exists in the multiple major urban development and regeneration schemes that have been created globally, where residential is a key component in making these schemes work and become successful - from direct sales and investment values, and as a key demand driver of other uses.

Equally, as populations urbanise the growth in demand for residential space will continue to support this trend. As an asset class it is clearly building momentum globally, and European markets are only just scratching the surface of the potential available to investors. It is likely that investors will continue to adjust their portfolio allocations to residential and the associated uses/niches including the form of student housing, senior living and healthcare as ageing populations drive demand for these related services.

As European cities continue to expand and improve city layouts, with a notable shift to public transportation and pedestrianisation, the scope for residential investment as a key part of large to mid-scale development around transport nodes is significant.

RESIDENTIAL

Sources: Figure 16: Colliers International | Figure 17: Colliers International, RCA

Sources: Figure 18: Colliers International, Oxford Economics | Figure 19: Colliers International, RCA
INVESTOR OUTLOOK: EUROPE

In summary, diversification, a reliable income stream and inflation hedging are at the top of the agenda and pricing levels in Europe offer a highly attractive alternative to other global regions. By sector, as of end 2018, European logistics (first place) and European offices (second place) represented the best risk-adjusted yields globally. In fourth is European retail, just behind Asian logistics.

Europe has been a direct beneficiary of the increase in global capital diversification, particularly in terms of fresh capital from Asia, which accounts for 30% of cross border investment notably from Korean, Singaporean and Hong Kong based investors with increasing interest from Japan and Australia. It is expected that Asian capital will continue to increase as a result of positive foreign exchange conditions and the hedging benefits of buying in Europe.

- Korean investors have the greatest FX advantage and are increasingly seeking core office and logistics with an income strategy, and now starting to look at Tier 2 countries and cities in Europe
- Singaporean investors remain very active looking at core plus logistics and offices / business parks
- Japanese capital may not have the FX benefits of other Asian domiciles, but it is coming and likely to go into funds as a route to market
- Australians are also coming with a co-investment strategy, and debt is a strong feature of activity, especially for UK-based product and increasingly office assets across major European markets.

The same hedging benefits apply to North American capital, which invested heavily across continental Europe in 2018 with similar levels expected this year. Europe accounted for five out of the top six destination countries for US capital in 2018 – Spain, UK, France, Germany and the Netherlands most notably in the city metros of Madrid, London, Paris and Amsterdam.

- Canadians are increasingly active in the co-investment market, and the likes of QuadReal and Oxford Properties have both made big commitments to new JV logistics development platforms focusing on Europe.
- US investors are lowering their return expectations of the market and will continue to be active at both a direct asset and entity level, via M&A opportunities.

Economic factors, notably the Brexit result, may well change the attractiveness of Europe and the current pattern of investment, but markets offering well-priced opportunities that embrace the structural factors driving growth for modern space across all asset classes will continue to be successful in attracting cross-border investment.
WHAT ABOUT THE ECONOMY: BREXIT

Although Brexit remains an ongoing concern, with ‘no deal’ a particular risk to economic growth, one of the biggest dilemmas for global investors waiting on the UK sidelines, is guessing when Sterling will present best value. That said, the devaluation of Sterling and the Euro versus other global currencies over 2018 has enhanced hedging benefits, and waiting too long could result in an opportunity missed.

If a deal is agreed, it’s business as usual with economic growth for the UK and Eurozone forecast to reach 1.5-1.6% in 2019.

Given that a surge in corporate investment is expected following a Brexit decision, there is a possibility of a slight uptick in economic output in 2019/2020, which could also feed into higher investment volumes as capital waiting in the wings can be deployed with greater certainty.

Under a no-deal scenario, expect a longer lag in activity as economic growth contracts to close to zero growth in 2019. A weaker pound may help to attract capital into the UK during this time, but this could be offset by “imported inflation” which would act as a drag on consumption, GDP and thus retail and logistics demand in particular.

For offices, although London-based banks have increased their interest in locations such as Paris, Dublin, and Frankfurt in anticipation of Brexit, not much has actually happened yet – only around 1,500 jobs have been relocated.

It remains highly unlikely that businesses will roll out big relocation programs as the cost of relocation is enormous, staff don’t want to move (from London) and finding talent in other locations – especially outside of London – is an even bigger challenge with unemployment rates at historically low levels.

It is worth remembering that the UK is one of few European countries with a positive working population position. Once a Brexit decision is made this should support a higher rate of economic growth mid-term than across the Eurozone.

London is, and will remain, the No.1 investment market in Europe although Paris and many other European cities will continue to offer a range of diverse and interesting investment opportunities.
Colliers International Group Inc. (NASDAQ: CIGI) (TSX: CIGI) is top tier global real estate services and investment management company operating in 69 countries with a workforce of more than 12,000 professionals. Colliers is the fastest-growing publicly listed global real estate services and investment management company, with 2017 corporate revenues of $2.3 billion ($2.7 billion including affiliates). With an enterprising culture and significant employee ownership and control, Colliers professionals provide a full range of services to real estate occupiers, owners and investors worldwide, and through its investment management services platform, has more than $20 billion of assets under management from the world’s most respected institutional real estate investors.

Colliers professionals think differently, share great ideas and offer thoughtful and innovative advice to accelerate the success of its clients. Colliers has been ranked among the top 100 global outsourcing firms by the International Association of Outsourcing Professionals for 13 consecutive years, more than any other real estate services firm. Colliers is ranked the number one property manager in the world by Commercial Property Executive for two years in a row.

Colliers is led by an experienced leadership team with significant equity ownership and a proven record of delivering more than 20% annualized return for shareholders, over more than 20 years.

For the latest news from Colliers, visit Colliers.com or follow us on Twitter: @Colliers and LinkedIn.

© 2019 All rights reserved.