TH Real Estate

a nuveen company

THINK European cities

Trends and tactics

Q1 2018

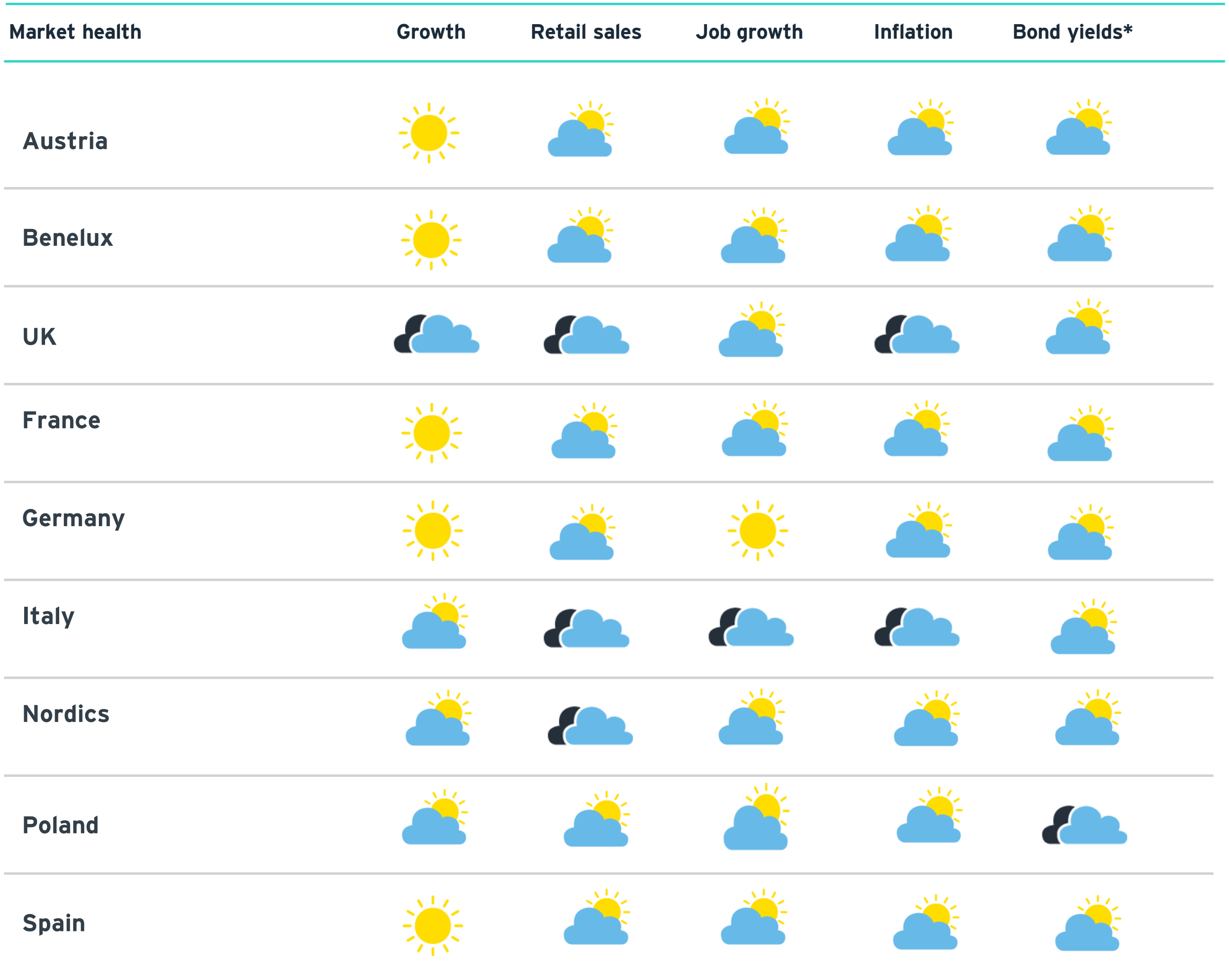
IMPORTANT: FOR FINANCIAL PROFESSIONAL USE ONLY. THIS DOCUMENT IS NOT FOR GENERAL PUBLIC DISTRIBUTION AND MUST NOT BE USED BY RETAIL INVESTORS. PLEASE SEE THE IMPORTANT INFORMATION ON THE FINAL PAGE.

Economic dashboard: Full steam ahead in 2018

Europe has emerged from hibernation and is enjoying a synchronised upturn. Brushing aside geo-political concerns, 2017 was the best year for Eurozone growth in a decade, growing by an impressive 2.5%. A strengthening euro may temper output, however, a healthy mix of increased consumption, investment and exports bode well for 2018. Easing fears of populism, higher bank lending, and unemployment across the region shrinking to a nine-year low, have all proven to be catalysts for expansion. However, unlike the US, there has been little sign of strong wage growth despite the improving labour market. The volatility witnessed across global equity markets in February 2018 relate to the Fed incorporating a steeper interest rate horizon - but that is not the prognosis for Europe. Broad consensus seems to be that the worst-case scenario of a sustained market rout, with major global macro consequences, is quite unlikely without the realisation of fundamental economic weaknesses and/or balance sheet vulnerabilities. The third quarter of 2018 may mark the end of European Quantitative Easing (QE), but our vision of very glacial rises in borrowing costs remain. Despite solid economic growth and positive survey evidence, the weak medium-term inflation outlook implies that the European Central Bank (ECB) will be extremely cautious about withdrawing monetary support, with the first interest rate hike delayed until late 2018 or early 2019. Political risks are never far away on the continent. The Italian election and the ongoing Catalan independence debate are obvious examples of potential downside risks, although GDP of 1.8% is still envisaged for 2019.

Quick read

- Growth momentum to persist into 2018. The latest business and labour market surveys support solid expansion.
- ECB to end QE in 2018. Aggressive tightening of monetary policy unlikely with inflation projected to undershoot.
- Italian elections should not de-rail the region's positive outlook.



Source: Oxford Economics, TH Real Estate, Q1 2018
*Bond yields symbols are illustrative of whether they are supportive for real estate pricing.

FOR FINANCIAL PROFESSIONAL USE ONLY. NOT FOR PUBLIC DISTRIBUTION AND NOT FOR USE BY RETAIL INVESTORS.

Offices: Occupier markets are booming in German cities

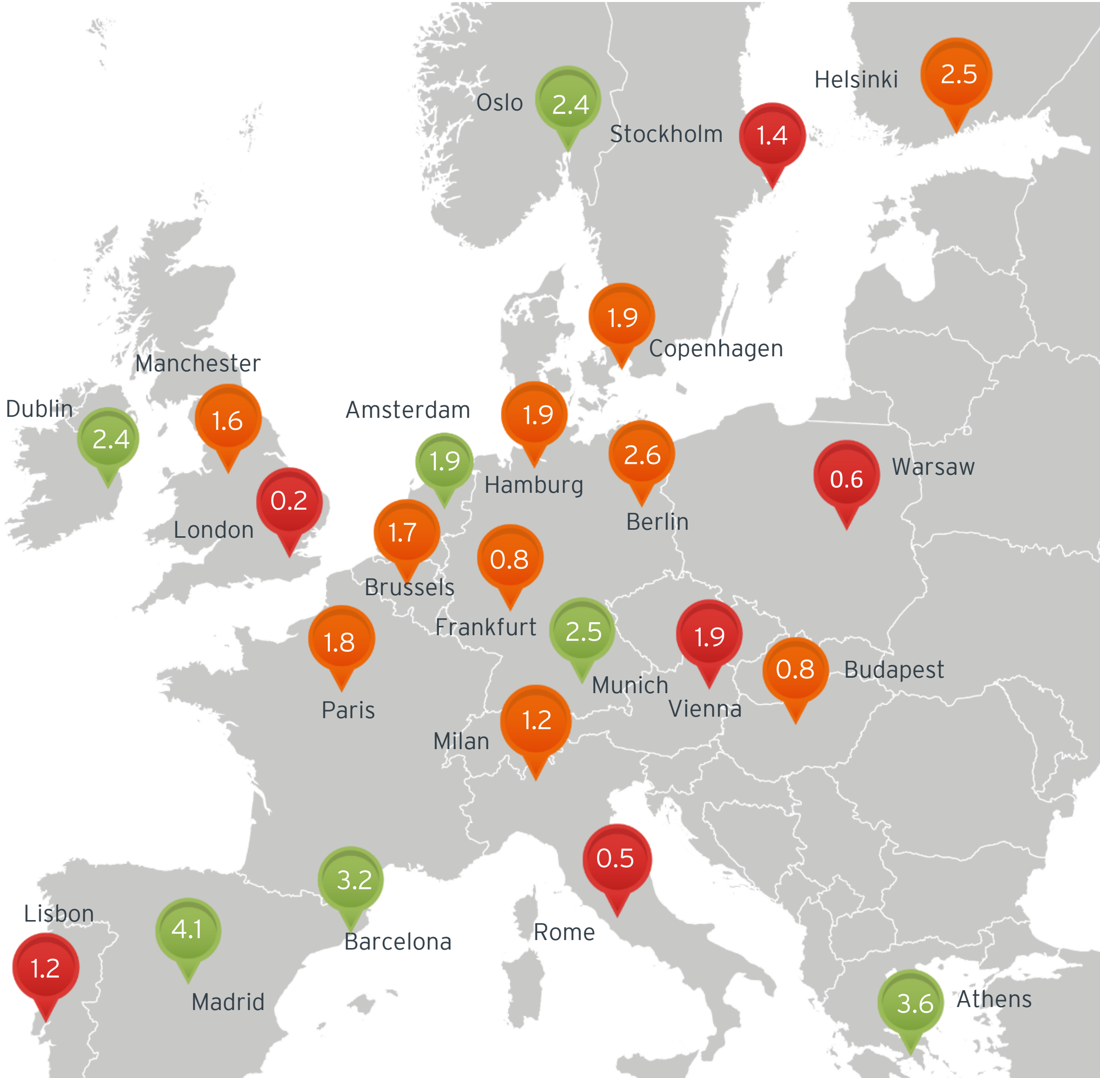
German cities are going from strength to strength and despite rental levels well in excess of previous cycle peaks, occupier dynamics point to further upward pressures in the key centres. In fact, gross take-up rates are way ahead of long-run averages; by 50-60% in the 'big four'. Our forecasts for annualised growth over the next five years look modest in light of these trends, however, much depends on the development response, which thus far has been muted. Only Frankfurt has an overhang of immediate vacancy (9.2% of stock) and much of the speculative space has been delivered. Meanwhile, vacancy in Berlin and Munich is chronically low and rental pressures are most evident. This is all welcome news in light of current yield trends. Berlin and Munich look set to overtake Paris Central Business District (CBD) in the near term to become Europe's most expensive markets.

In Central Paris, occupier markets have tightened further and immediate vacancy remains a notch above 3% in the CBD, although a few speculative schemes are underway. Strong demand for space continues to erode vacancy rates in La Défense. In contrast, a number of soon-to-be completed schemes has meant vacancy in the Western Districts remains high and sticky. Over the Channel, central London markets are also diverging, with the City experiencing high vacancy (when speculative space under construction is included), and the West End benefiting from a relatively benign occupier balance. Most parts of London are experiencing normal levels of take up, but Brexit uncertainty has underpinned caution on rents. Headline rents continue to flat line, and net effectives are under pressure.

Quick read

- The region's economic recovery is translating into improved demand for space. In particular, the German cities are experiencing booming occupier markets.
- Elsewhere, Tier 2 cities are benefiting from improved demand, but high legacy vacancy rates are still a feature of Madrid, Milan and Amsterdam. Prime rental office growth will outpace the average for a good while to come.

Fig.1: Rental growth forecasts, five-year annualised % p.a. (Q3 2017-Q2 2022)



Source: TH Real Estate, Q3 2017
Note: Forecasts cannot be guaranteed.

FOR FINANCIAL PROFESSIONAL USE ONLY. NOT FOR PUBLIC DISTRIBUTION AND NOT FOR USE BY RETAIL INVESTORS.

Retail: Growth in online changing the way we value stores

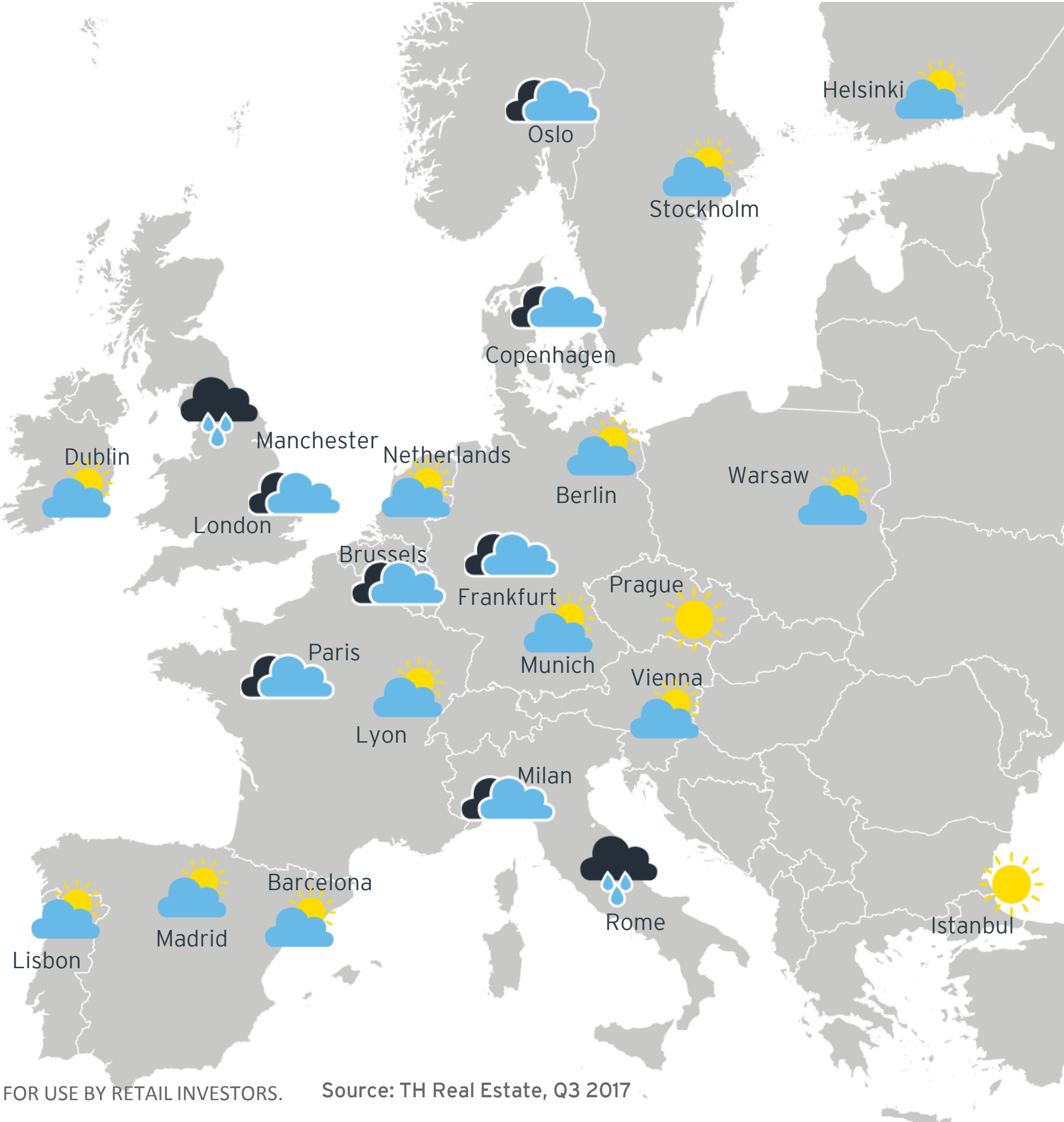
European retail sales grew by roughly 2.3% in Q4 2017 with a surprise slow down in German retail sales at 1.9% in Q4 versus 3.6% in Q3 2017. Spending data contradicts improving German consumer confidence with high employment, rising wages and low borrowing costs supporting spend. France, Ireland, Poland and the Nordics continue to outperform the European average with strong sales growth. Spanish sales slowed towards the year end averaging 1.1% in Q4 2017, and the UK consumer suffered from high inflation squeezing real wage growth. Looking ahead, Oxford Economics forecast European retail spending to remain in line with 2017 at 2.3%. Spending in France is forecast at 2.6% p.a. in 2018 followed by Sweden at 2.4%, UK and Spain at 2.2%, Germany underperforming at 1.9% and Italy's low growth position continuing with projected sales growth of 0.7%.

The UK market saw retailer administrations reach a five-year high in 2017. International retailers remain focussed on the prime malls but we see more activity in terms of domestic discount retailers focusing on mid-market space and retail warehousing, which outperformed. Spanish retail sales are expected to pick up in 2018, and demand remains strong for super prime malls where vacancy is around 3.0%. Spain still enjoys a cyclical recovery which will support rents in the short term.

Quick read

- Solid economic growth and healthy labour markets continue to provide a stable consumer back drop, although risks prevail due to household debt levels and rising interest rates.
- European retail spending forecast to remain stable in 2018 at 2.3%, although variation exists across European countries.
- Spanish retail sales to improve in 2018 and rental growth expected off cyclical-low rents.

Fig.2: Retail occupier sentiment (Q3 2017-Q2 2022)



Source: TH Real Estate, Q3 2017

FOR FINANCIAL PROFESSIONAL USE ONLY. NOT FOR PUBLIC DISTRIBUTION AND NOT FOR USE BY RETAIL INVESTORS.

Investment: Liquidity still buoyant but yield compression is slowing

Investment activity was up in 2017 compared to 2016, but fell short of the record year 2015. The big three markets, Germany, France and the UK, all recorded higher volumes along with most smaller markets. Most remarkable is the recovery of the UK market despite Brexit uncertainty. However, it was mainly overseas investors lifting volumes in the UK. This is in line with Germany, where for the first time, cross-border buyers have deployed more than domestic groups. In France, the market picked up in the second half of the year after the election of the new president. The Netherlands, Finland and Spain, all laggards in this economic cycle, finally returned to old form in 2017.

Sanguine real estate investment markets across Europe are supported by strong occupier market fundamentals as well as wider financial market optimism. Financial market volatility in early February 2018, including an upward trend in bond yields, has rekindled the discussion of the era of real estate yield compression nearing its natural end. As long as the correction can be contained, it should be greeted as a welcome start to an orderly normalisation. For real estate, it may come just in time before markets move cap rates to such extremes where any disruption could only end in a hard landing. One could argue that property market conditions are ideal to engineer a soft landing of asset pricing. Central banks signal that ultra-low interest rates are slowly being phased out. They can raise rates because the economy is booming, and real estate occupier markets are doing well. The idea is, as long as falling vacancies and rising rents assist real estate values, yields can safely adjust to more sustainable levels without causing havoc to the market.

Before the Global Financial Crisis (GFC), real estate had built up a number of significant risks; these are not present today. So a more dramatic revaluation of financial markets would still find the property sector in much better shape than in the years following 2007. Notably, real estate spreads over bonds remain elevated and well above long-run averages. This suggests any real estate market correction would be relatively limited. Additionally, the market correction is driven by expectations of rising inflation. Historically, demand-driven inflation has been good for real estate with investors buying into property as an inflation hedge.

Quick read

- 2017 was another strong year for real estate investment, even in the Brexit-dented UK and laggards Finland, Spain and the Netherlands.
- Increased financial market volatility and government bond yields slowly moving upwards suggest that the super-cycle of falling property yields is nearing its end. However, upward pressure on cap rates is not imminent.

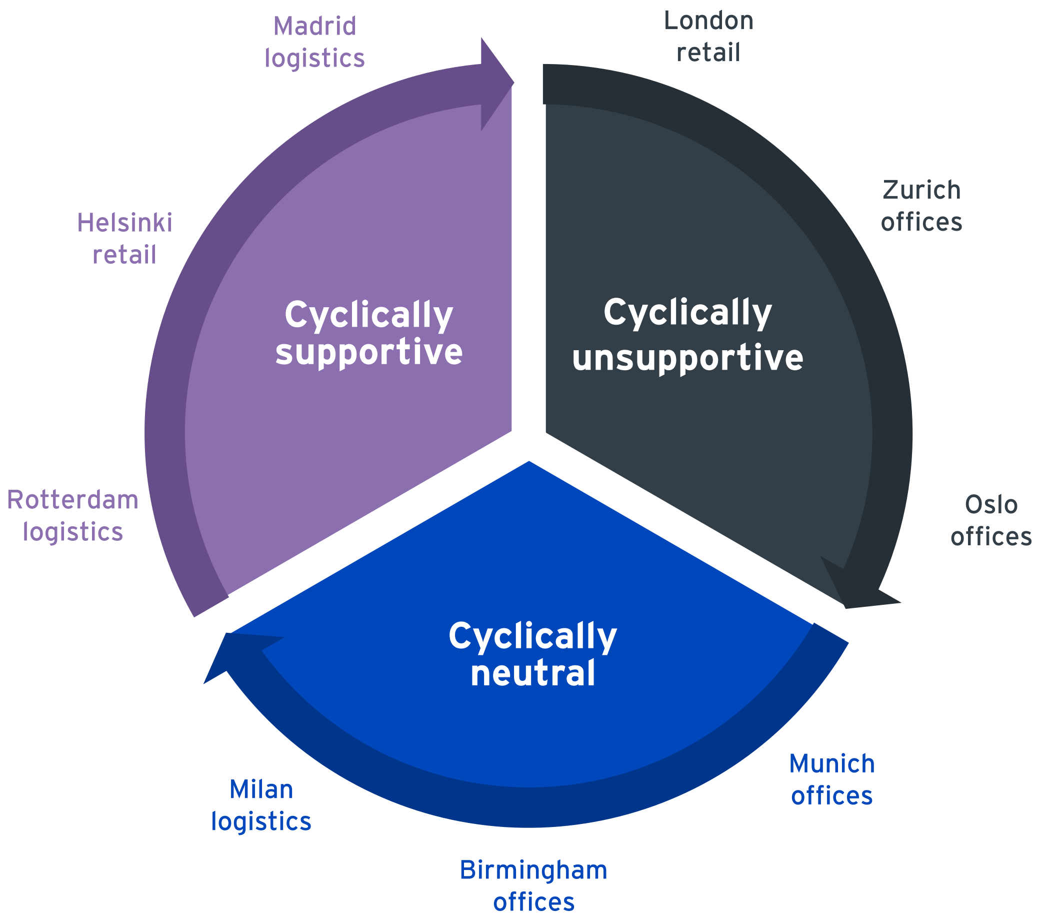
	Yield trend	
	5 years	10 years
Austria	↑	↑↑
Belgium	↑	↑↑
Britain	↑	↑
Czech Republic	→	↑
Finland	↑	↑↑
France	↑	↑↑
Germany	↑	↑↑
Italy	↑↑	↑↑
Netherlands	↑	↑
Poland	→	↑
Portugal	↑↑	↑↑
Spain	↑↑	↑↑
Sweden	↑↑	↑↑

Source: TH Real Estate, Q1 2018
Note: Forecasts cannot be guaranteed.

FOR FINANCIAL PROFESSIONAL USE ONLY. NOT FOR PUBLIC DISTRIBUTION AND NOT FOR USE BY RETAIL INVESTORS.

Cyclical city recommendations: A level playing field

Fig.3: Short-term city selection



Source: TH Real Estate, Q1 2018

Quick read

- With interest rates synchronising asset pricing across markets, cyclical recommendations rely mainly on differences in rental growth expectations.
- Due to the fallout of Brexit, the UK is now on a different path compared to all other European markets within or outside the Eurozone.
- Logistics in Southern Europe and the Netherlands remain among the top market recommendations.

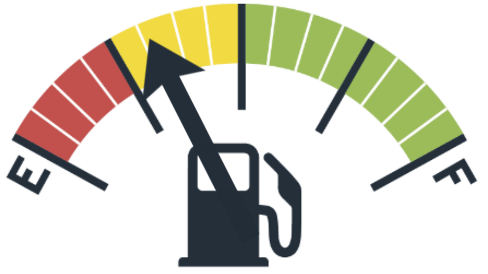
Fig.4: Key market themes

Source: TH Real Estate, Q1 2018

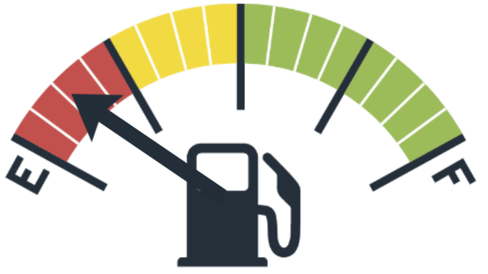
FOR FINANCIAL PROFESSIONAL USE ONLY. NOT FOR PUBLIC DISTRIBUTION AND NOT FOR USE BY RETAIL INVESTORS.

Headline views: Risks and opportunities

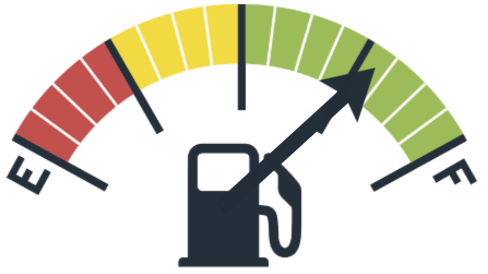
Politics



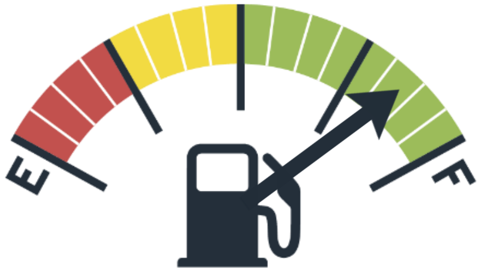
Yields



Economy



Occupier markets



Source: TH Real Estate, Q1 2018

FOR FINANCIAL PROFESSIONAL USE ONLY. NOT FOR PUBLIC DISTRIBUTION AND NOT FOR USE BY RETAIL INVESTORS.

Appendix: Financial data

GDP	2016	2017	2018	2019	2020	2021	2022	Average p.a. growth (2017-2020)	Average p.a. growth (2017-2022)
Austria	1.5	3.1	2.4	1.6	1.3	1.2	1.2	1.7	1.5
Belgium	1.5	1.7	1.6	1.5	1.4	1.4	1.4	1.5	1.4
Finland	1.9	3.0	2.4	1.8	1.7	1.5	1.3	1.9	1.7
France	1.1	1.9	2.1	1.9	1.8	1.5	1.2	1.9	1.7
Germany	1.9	2.5	2.4	1.8	1.3	0.9	0.8	1.8	1.4
Greece	0.0	1.3	2.3	2.3	2.2	2.5	2.6	2.3	2.4
Ireland	5.1	6.0	3.1	2.4	2.2	2.2	2.2	2.6	2.4
Italy	1.1	1.6	1.4	1.1	0.9	0.8	0.8	1.1	1.0
Luxembourg	3.1	3.3	3.6	3.5	3.4	3.1	2.9	3.5	3.3
Netherlands	2.1	3.3	2.5	1.7	1.2	1.1	1.1	1.7	1.5
Portugal	1.5	2.7	2.2	1.9	1.4	1.1	0.9	1.8	1.4
Spain	3.3	3.1	2.8	2.4	2.1	1.7	1.4	2.4	2.0
Eurozone	1.8	2.5	2.2	1.8	1.5	1.2	1.1	1.8	1.5
Czech Republic	2.5	4.6	3.9	3.1	2.3	2.0	2.1	3.1	2.6
Denmark	1.7	2.1	1.9	1.8	1.9	1.8	1.6	1.9	1.8
Norway	1.0	2.3	2.5	2.1	1.9	1.7	1.6	2.2	1.9
Poland	2.6	4.6	4.2	3.3	2.9	2.9	2.8	3.4	3.2
Sweden	3.1	2.7	2.6	2.1	2.0	1.8	1.7	2.2	2.0
United Kingdom	1.8	1.8	1.8	1.6	1.9	1.9	1.8	1.8	1.8
European Union	1.9	2.5	2.3	1.9	1.7	1.5	1.4	2.0	1.7

Source: TH Real Estate, Oxford Economics, Q1 2018
Note: Forecasts cannot be guaranteed.

FOR FINANCIAL PROFESSIONAL USE ONLY. NOT FOR PUBLIC DISTRIBUTION AND NOT FOR USE BY RETAIL INVESTORS.

Appendix: Financial data

Inflation	2016	2017	2018	2019	2020	2021	2022	Average p.a. growth (2017-2020)	Average p.a. growth (2017-2022)
Austria	0.9	2.1	1.9	1.8	1.8	1.8	1.9	1.8	1.8
Belgium	2.0	2.1	1.8	1.8	2.0	2.0	2.0	1.9	1.9
Finland	0.4	0.8	1.0	1.5	1.7	1.8	1.8	1.4	1.3
France	0.2	1.0	1.3	1.3	1.6	1.8	2.0	1.4	1.2
Germany	0.5	1.7	1.8	2.3	2.2	2.1	2.1	2.1	2.1
Greece	-0.8	1.1	0.8	0.7	1.3	1.8	2.0	0.9	1.4
Ireland	0.0	0.3	1.4	1.5	1.8	1.9	1.9	1.5	1.4
Italy	-0.1	1.2	0.9	1.6	1.8	1.8	1.9	1.4	1.5
Luxembourg	0.0	2.1	1.6	1.8	1.9	2.0	2.0	1.8	1.9
Netherlands	0.3	1.4	1.5	1.6	1.9	2.0	2.0	1.7	1.7
Portugal	0.6	1.4	1.4	1.8	1.8	1.8	1.8	1.6	1.6
Spain	-0.2	2.0	1.6	1.7	1.9	1.8	1.8	1.7	1.7
Eurozone	0.2	1.5	1.4	1.7	1.9	1.9	1.9	1.7	1.7
Czech Republic	0.7	2.5	2.5	2.0	1.8	2.0	2.0	2.1	2.2
Denmark	0.3	1.1	1.2	1.7	2.0	1.9	1.9	1.6	1.6
Norway	3.6	1.9	1.8	1.8	1.9	2.2	2.2	1.8	1.8
Poland	-0.6	2.0	2.5	2.2	2.5	2.3	2.2	2.4	2.2
Sweden	1.0	1.8	1.9	2.5	2.9	2.2	2.0	2.4	1.6
United Kingdom	0.6	2.7	2.2	1.5	1.7	1.8	1.8	1.8	2.0
European Union	0.3	1.7	1.7	1.8	1.9	1.9	2.0	1.8	1.8

Source: TH Real Estate, Oxford Economics, Q1 2018
Note: Forecasts cannot be guaranteed.

FOR FINANCIAL PROFESSIONAL USE ONLY. NOT FOR PUBLIC DISTRIBUTION AND NOT FOR USE BY RETAIL INVESTORS.

Appendix: Financial data

Interest rates (%) year end	2016	2017	2018	2019	2020	2021	2022
Eurozone	0.05	0.05	0.25	0.50	0.75	1.00	1.25
Czech Republic	0.05	0.05	0.50	1.00	1.25	1.50	1.75
Denmark	0.05	0.05	0.25	0.50	0.75	1.00	1.25
Sweden	-0.50	-0.50	0.00	0.25	0.75	1.25	1.75
Norway	0.50	0.50	0.75	1.00	1.50	2.00	2.50
US	0.50	1.25	2.00	2.50	2.75	2.75	3.00
UK	0.25	0.50	0.75	1.25	1.75	2.25	2.50

Exchange rates year end	2016	2017	2018	2019	2020	2021	2022
€/£	1.17	1.13	1.13	1.15	1.18	1.20	1.20
$/€	1.11	1.20	1.30	1.28	1.27	1.25	1.25
DKr/€	7.45	7.45	7.45	7.45	7.45	7.45	7.45
NOK/€	9.29	9.84	9.41	9.20	9.10	9.04	8.97
SKr/€	9.47	9.85	9.30	9.01	8.98	8.96	8.94
Zloty/€	4.36	4.17	4.10	4.05	4.03	4.00	3.98
Koruna/€	27.0	25.5	24.8	24.5	24.4	24.3	24.1

Source: TH Real Estate, Oxford Economics, Q1 2018
Note: Forecasts cannot be guaranteed.

FOR FINANCIAL PROFESSIONAL USE ONLY. NOT FOR PUBLIC DISTRIBUTION AND NOT FOR USE BY RETAIL INVESTORS.

Appendix: Financial data

10-year bonds (year end)	2016	2017	2018	2019	2020	2021	2022
Austria	0.4	0.6	1.4	1.7	2.0	2.3	2.5
Belgium	0.5	0.6	1.5	2.0	2.4	2.8	3.0
Czech Republic	0.5	1.6	2.2	2.7	2.9	3.0	3.0
Denmark	0.3	0.5	0.5	1.1	1.7	2.2	2.8
Finland	0.4	0.6	1.3	1.7	2.0	2.2	2.5
France	0.7	0.8	1.6	1.9	2.3	2.7	2.9
Germany	0.1	0.4	1.1	1.4	1.7	2.0	2.2
Greece	7.1	4.1	4.1	4.4	4.7	5.0	5.2
Ireland	0.8	1.1	1.7	2.0	2.3	2.6	2.8
Italy	1.8	2.0	2.7	3.1	3.5	3.7	3.8
Netherlands	0.4	0.5	1.3	1.7	2.0	2.2	2.5
Norway	1.7	1.7	1.8	2.4	2.9	3.3	3.5
Poland	3.6	3.3	3.7	3.9	4.1	4.4	4.6
Portugal	3.8	1.9	2.6	3.3	3.9	4.2	4.4
Spain	1.3	1.5	2.2	2.7	3.2	3.4	3.6
Sweden	0.5	0.8	1.4	1.9	2.4	2.8	3.0
United Kingdom	1.3	1.3	2.2	2.7	3.2	3.4	3.6
Eurozone	1.0	0.9	1.7	2.1	2.5	2.7	2.9

Source: TH Real Estate, Oxford Economics, Q1 2018
Note: Forecasts cannot be guaranteed.

FOR FINANCIAL PROFESSIONAL USE ONLY. NOT FOR PUBLIC DISTRIBUTION AND NOT FOR USE BY RETAIL INVESTORS.

Contact us

Alice Breheny
Global Head of Research
T: +442037278122
E: alice.breheny@threalestate.com

Stefan Wundrak
Head of European Research
T: +4420372781226
E: stefan.wundrak@threalestate.com

Andy Schofield
Director of Research
T: +442037278203
E: andy.schofield@threalestate.com

Michael Keogh
Director of Research
T: +442037278160
E: michael.keogh@threalestate.com

Angela Goodings
Associate Director of Research
T: +442037278147
E: angela.goodings@threalestate.com

Maria Grubmueller
Research Associate
T: +442037278311
E: maria.grubmueller@threalestate.com

Haoran Wu
Research Analyst
T: +442037278231
E: haoran.wu@threalestate.com

If you would like to register to receive future market updates from TH Real Estate's research team, please send an email to: contact@threalestate.com

threalestate.com

@THRealEstate14

FOR FINANCIAL PROFESSIONAL USE ONLY. NOT FOR PUBLIC DISTRIBUTION AND NOT FOR USE BY RETAIL INVESTORS.

Important information:

This document is intended solely for the use of professionals client in Europe, Wholesale Clients in Australia, Professional investors in Hong Kong, Institutional Investors in Singapore and United States and is not for general public distribution.

Any assumptions made or opinions expressed are as of the dates specified or if none at the document date and may change as subsequent conditions vary. In particular, the document has been prepared by reference to current tax and legal considerations that may alter in the future.

The document may contain "forward-looking" information or estimates that are not purely historical in nature. Such information may include, among other things, illustrative projections and forecasts. There is no guarantee that any projections or forecasts made will come to pass.

International investing involves risks, including risks related to foreign currency, limited liquidity particularly where the underlying asset comprises real estate, less government regulation in some jurisdictions, and the possibility of substantial volatility due to adverse political, economic or other developments. Past performance is no guarantee of future performance. The value of investments and the income from them may go down as well as up and are not guaranteed. Rates of exchange may cause the value of investments to go up or down. Any favourable tax treatment is subject to government legislation and as such may not be maintained. The valuation of property is generally a matter of valuer's opinion rather than fact. The amount raised when a property is sold may be less than the valuation.

Nothing in this document is intended or should be construed as advice. The document is not a recommendation to sell or purchase any investment. It does not form part of any contract for the sale or purchase of any investment.

This material is provided for informational or educational purposes only and does not constitute a solicitation in any jurisdiction. Moreover, it neither constitutes an offer to enter into an investment agreement with the recipient of this document nor an invitation to respond to it by making an offer to enter into an investment agreement.

This material may contain "forward-looking" information that is not purely historical in nature. Such information may include, among other things, projections, forecasts, estimates of yields or returns, and proposed or expected portfolio composition. Moreover, certain historical performance information of other investment vehicles or composite accounts managed by Nuveen has been included in this material and such performance information is presented by way of example only. No representation is made that the performance presented will be achieved by any Nuveen funds, or that every assumption made in achieving, calculating or presenting either the forward-looking information or the historical performance information herein has been considered or stated in preparing this material. Any changes to assumptions that may have been made in preparing this material could have a material impact on the investment returns that are presented herein by way of example.

This material is not intended to be relied upon as a forecast, research or investment advice, and is not a recommendation, offer or solicitation to buy or sell any securities or to adopt any investment strategy. The information and opinions contained in this material are derived from proprietary and non-proprietary sources deemed by Nuveen to be reliable, and not necessarily all-inclusive and are not guaranteed as to accuracy. There is no guarantee that any forecasts made will come to pass. Company name is only for explanatory purposes and does not constitute as investment advice and is subject to change. Any investments named within this material may not necessarily be held in any funds/accounts managed by Nuveen. Reliance upon information in this material is at the sole discretion of the reader. They do not necessarily reflect the views of any company in the Nuveen Group or any part thereof and no assurances are made as to their accuracy.

Past performance is not a guide to future performance. Investment involves risk, including loss of principal. The value of investments and the income from them can fall as well as rise and is not guaranteed. Changes in the rates of exchange between currencies may cause the value of investments to fluctuate.

438632-G-INST-Q-03/19