SAVILLS WORLD RESEARCH
2016

Around the world
in dollars and cents

WHAT PRICE THE WORLD?
Trends in international real estate trading

GLOBAL REAL ESTATE TIPS
Savills experts reveal the next real estate hotspots

savills

The new march of money

World real estate is a global stage on which a variety of economic and monetary acts are played out. Some actors have access to large amounts of equity, others to cheap debt. Many players in recent years have been operating under much looser monetary conditions than in previous decades so money has become cheaper and opportunities have been presented in those countries where asset prices were hit by domestic recession.

This means that cross-border activity in real estate has generally grown since the global financial crisis of 2008. The proportion of deals done where buyers originate in different countries has increased from a low 17% in 2009 to 20% in 2015. Over the same period, cross-border volumes have grown by 334% from $65 billion to $217 billion.

In this issue of *Around the World in Dollars and Cents*, we have taken a look at how much real estate there is in the world and how much of that is available for investors, both domestic and cross-border. For the first time we have included agricultural in our assessment, so we are presenting a complete cross-sector picture that includes residential and commercial assets.

We then take a look at how asset values are distributed across global regions and how recent flows of money from one region to another may be in the process of changing this. Differences in monetary conditions and investor practices in global regions are then examined. The results have important and profound implications for global real estate trends.

Looking to the future of world real estate, we study the investing intentions of the equity-rich private sector and see that some money is becoming not only footloose but also more adventurous in the asset classes it is willing to invest. This is a theme that has been picked up by many of our researchers around the world who have each given their tips for real estate investment in 2016 and beyond. ■

'Some money is becoming not only footloose but also more adventurous'

YOLANDE BARNES
Director of Savills
World Research
ybarnes@savills.com
Twitter: @Yolande_Barnes

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KEY POINTS

- **Global real estate assets comprise nearly 60% of the value of all global assets, including equities, bonds and gold.**
- **Three-quarters of global real estate value is residential, 13% commercial and 12% agricultural.**
- **About 1% of global real estate assets trade each year in big ticket deals.**
- **Long-term global investment prospects are governed by population growth and the resulting demand for housing.**
- **Near-term prospects for higher interest rates mean the global search for yield and rental growth is now full-on.**
- **Our three pillars of real estate investment for the next decade are the rise of:**

1. **Secondary and tertiary markets**
2. **Second-tier cities**
3. **Alternative asset classes and locations.**

- **Our global real estate tips for the next five years include logistics in the tech age, high-quality small cities for the digital creative classes, residential for growing middle-class populations and new resorts in Asia and EMEA.**

GLOBAL ASSETS

What price the world?

Real estate in the global asset universe

Worldwide real estate assets comprise nearly 60% of the value of all global assets, including equities, bonds and gold

We estimate that the value of all developed real estate in the world amounts to approximately $217,000,000,000,000 (217 trillion US dollars, *see fig. 1*). This covers retail property, offices, industrial, hotels, residential, other commercial uses, and agricultural land.

The world owns real estate assets of nearly three times its annual income. Global property value in 2015 amounted to 2.7 times the world's GDP and represents an important store of national, corporate and individual wealth. It accounts for roughly 60% of all mainstream global assets. The value of all gold ever mined (in the region of $6 trillion) pales into insignificance next to the value of all developed real estate.

The fact that the value of global real estate exceeds by almost one-third the total value of all globally traded equities and securitised debt instruments highlights the important role it plays in economies worldwide (*see fig. 3*). Real estate is the pre-eminent asset class that will be most impacted by global monetary conditions and investment activity and which, in turn, has the power to most impact national and international economies.

In recent years, quantitative easing and resulting low interest rates have suppressed real estate yields and fuelled high levels of asset appreciation globally. Investment activity and capital growth have swept around the major real estate markets of the world and led to asset price inflation in many instances.

We estimate that around one-third of the value of the global real estate market identified here is readily investable at scale (*see fig. 2*), with the remaining $145 trillion not being publicly traded in any meaningful way. Most of it, even in the commercial sector, is owner-occupied or owned by small and private entities.

Of the $72.5 trillion of commercial and residential real estate that we count as 'investable', around $1.05 trillion or 1.45% was traded in big ticket deals of over $10 million in the 12 months to Q3 2015[1]. This investment grade stock has increased in value by 3.56% in the two years since our last estimate of world real estate value in Q3 2013. This represents average annual growth rate in global capital values of 1.77% per annum but covers a range of experiences, from high-growth in the US to negative or no growth in parts of Asia.

This year we have included for the first time the value of agricultural land, at an estimated $26 trillion, of which about $7.8 trillion (around 30%) is corporately and institutionally invested. Most agricultural land is owned by non-investing entities, operators and occupiers, especially in emerging economies where this is a sector with great potential for further growth and investment. If the land is owned by non-investing entities, it is likely to be non-investable.

Not included in the global calculation is the value of local commercial properties: workshops, workspaces, shops and small business premises that are not part of the high quality commercial real estate universe that constitutes global property markets, but which are important components of economic growth and prosperity, especially in emerging markets. They are almost impossible to value at a global level but have huge potential for future investment as economies mature and real estate markets develop within them, adding to the global stock.

Overall, the most important component of global real estate value is the homes that people live in. By far the biggest proportion of these are owned by the people who inhabit them, which makes this sector the least concentrated, in terms of ownership, and most closely tied to the fortunes of ordinary people. There are approximately 2.5 billion households on the planet and those in developed economies occupy housing at much higher price points than those in less developed economies. We estimate that the median value of the dwellings occupied by all these households is $43,000. ■

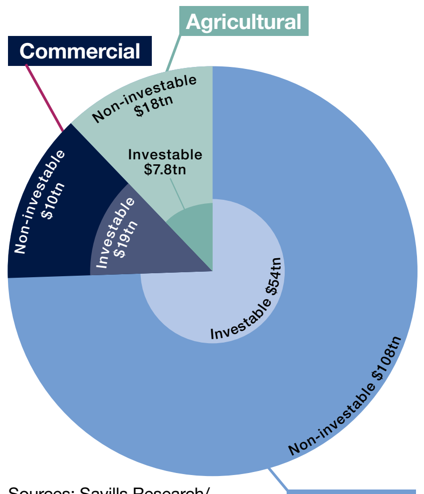
[1] These deals form the basis of the information and analysis on global investment trends analysed in the Around the World in Dollars and Cents research programme

FIG. 1 Global asset universe

Asset*	Investable (trillions)	Non-investable (trillions)	All (trillions)
ALL REAL ESTATE	**$81**	**$136**	**$217**
RESIDENTIAL	$54	$108	$162
HIGH QUALITY, GLOBAL, COMMERCIAL	$19	$10	$29
AGRICULTURAL LAND	$8	$18	$26
OTHER INVESTMENTS	**-**	**-**	**$155**
EQUITIES	$55	-	$55
OUTSTANDING SECURITISED DEBT	$94	-	$94
ALL GOLD EVER MINED	-	-	$6
GLOBAL MAINSTREAM ASSET UNIVERSE	**-**	**-**	**$372**

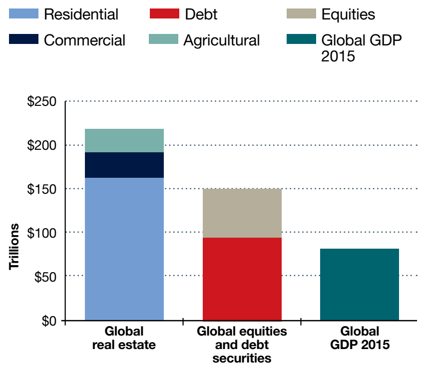
***(values in US$ trillions – rounded)** Sources: Savills Research, Bank for International Settlements, Dow Jones Total Stock Market Index, Oxford Economics

FIG. 2 Global real estate universe



Sources: Savills Research/ Oxford Economics

FIG. 3 Global real estate universe in comparison



Sources: Savills Research, Bank for International Settlements, Dow Jones Total Stock Market Index, Oxford Economics

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US$217,000,000,000,000

Our estimated value of all developed real estate in the world. This covers retail property, offices, industrial, hotels, residential, other commercial uses and agricultural land

Total assets breakdown

Old world economics contain the highest share of global real estate value so potential for growth in emerging markets is significant

The value of the world's real estate is unevenly distributed across the globe. Western nations contain the lion's share of asset value, while less developed nations contain the least.

The dominance of real estate in Western economies is most noticeable in commercial markets, where nearly half of the total asset value resides in North America and over a quarter in Europe (*see fig. 2*). Asia and Australasia contain 22% of commercial asset value, leaving just 5% for South America, the Middle East and Africa.

Part of the reason that the US market is so big is because it is the most mature. The US market is much more transparent than many others and is therefore easier to measure well and in detail. Consequently, it is where data coverage is most comprehensive. This is assisted by the fact that it is also probably the most institutionalised market and therefore recorded and reported on by those entities. The US also contains more of the most valuable real estate in the world on a $ per sq ft/metre basis.

The US, including Chicago, continues to dominate the global real estate market

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On the evidence of these regional real estate total values, the potential for the growth and development of investable commercial assets across the developing world would appear vast, but it is not necessarily the case that Western-style commercial property markets will develop in these new frontiers in the same way as they have in the west and parts of Asia.

Currently, many commercial premises in the less developed parts of the globe are informal, small-scale, flexible workspaces and shops. These have not been priced into overall asset value in this publication because they are traded in informal and opaque markets, often not recorded at a national, let alone international scale. Many workspaces and even retail spaces of this type are often mixed with residential property, either in buildings, blocks or neighbourhoods. The norm in nations which have not experienced widespread car ownership and suburban built environments is mixed-use and live-work space.

There is a real tension between two possible future built environment development scenarios in the nations which have not yet seen widespread, large-scale development in their cities. Recent development in China and other parts of Asia has shown that it is often easier, cheaper and faster to demolish existing structures to make way for large-scale developments. Improvements in infrastructure, land reclamation and investment in public transport lead to rising land values that exclude all but the large-scale and corporate players from participation. Landmark, world-class 'trophy' projects often involving named 'starchitects' are also beloved by politicians and planners alike, so they take priority over the smaller-scale integrated neighbourhood developments.

There is a big question mark, however, as to whether big-box, energy-hungry office blocks or retail malls will remain the universally preferred types of business accommodation in the 21st-century digital age and where the economy is developing along different lines to the late 20th-century Western experience.

Whatever the future development model adopted, the creation of new commercial real estate markets in Asia, Latin America, MENA and Africa is a potentially huge market. If the quantity and value of commercial space in these regions were to reach the current global average per head of population, the total value of commercial real estate globally would rise by 54%.

Residential real estate value is slightly more evenly distributed than commercial, broadly in line with the size of affluent populations (*see fig. 1*). China accounts for nearly a quarter of the total value, having nearly one-fifth of the world's population. Having said this, the weight of value is still in the West: 21% of the world's total residential asset value is in North America – despite the fact that only 5% of the population lives there. Europe contains 24% of residential assets by value but only houses 11% of the population.

45%

Of total high quality commercial real estate is in North America

The growth of residential real estate value in Asia illustrates the role of housing in developing economies. Its growth means there is now more collateral in the personal finance and small business sector of these countries. If African residential real estate markets were to develop in the same way over the next decade or two as the Asian markets (excluding China) have, this would add $5.8 trillion to the global total.

The global potential for economic development to impact on residential real estate is huge. A growing middle class and growing home ownership in areas of economic growth will increase the size of residential property as an asset class. If residential property in Middle Eastern, African and Asian countries were to move towards the global average per head of population, this would increase global residential asset values by 32% or $52 trillion.

There are big prizes for the super-opportunistic investor. While emerging economies will always be seen as high risk, the fundamentals of economic growth with strong demographics will undoubtedly increase demand for housing, workspace and retail/leisure space in population centres. This will create compelling opportunities for those able to deploy capital into the right types of real estate – the highest demand locations of the more stable nations. ■

FIG. 1 Global population v total residential value

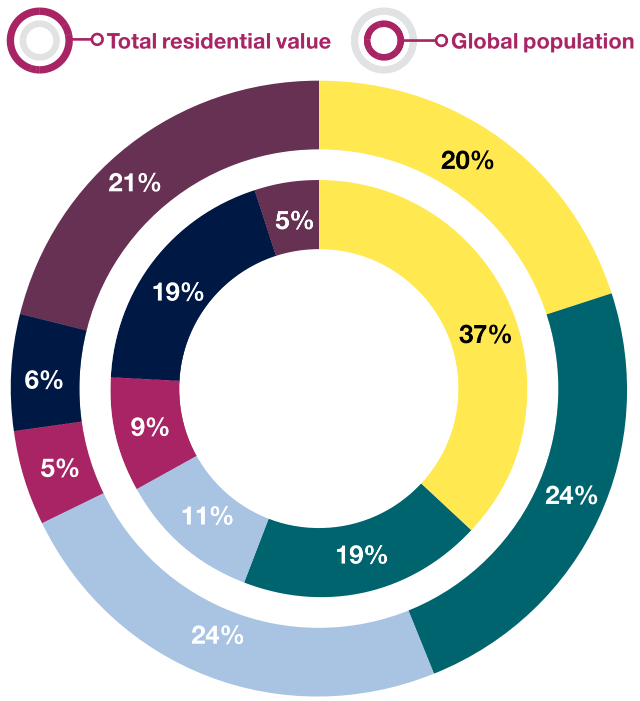
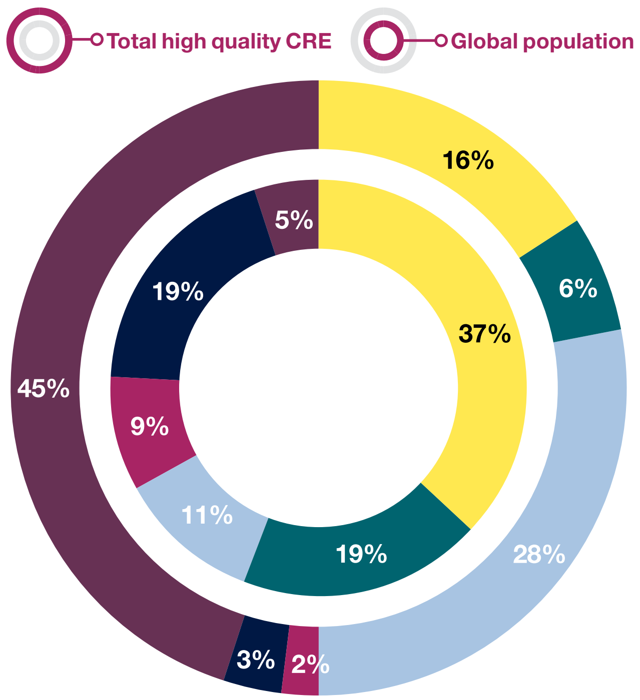


FIG. 2 Global population v total high quality commercial real estate



Asia & Pacific · China & Hong Kong · Europe · Latin America · Middle East and Africa · North America

Sources: Savills Research/Oxford Economics

INVESTOR REPORT

How will tighter monetary conditions impact global real estate investment?

Yolande Barnes looks at the implications of rising interest rates

London tends to attract opportunistic, short-term buyers

JASON HAWKES

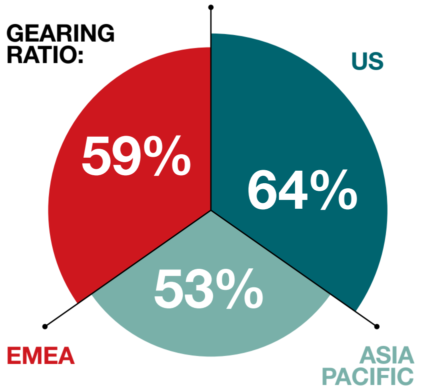
The world of real estate investment seems to have fallen into two halves since the global financial crisis (GFC) of 2007-08. In one, investors are accessing debt and making leveraged purchases and in the other, investors are using equity, seeking income and/or security. This means that there are significant differences in both the timescale of investments and the hurdle rates.

This division between the equity-rich and the equity-poor has a geographical component. North American real estate deals tend to be more highly leveraged than Asia Pac deals, as we found in our analysis of a sample of big-ticket ($10 million plus) deals in 2015. Figure 1 shows the loan to value ratios found and how they differ between geographies.

Leveraged investments are more likely to be short to medium term than equity investments because debt eventually has to be repaid. Timescales will be set by lenders rather than the nature of the project or built environment requirements.

Sophisticated lenders will understand the timeliness of real estate investments: the influence of market cycles, development planning and build phases, income optimisation as well as maturity and depreciation profiles. Others will be more influenced by the availability and cost of wholesale funds, imposing these on the real estate investment environment rather than vice versa.

FIG. 1 **Loan to value ratios**



Leveraged investors will clearly be more constrained by monetary conditions than equity investors. Interest rates will impact on equity investors as well, inasmuch as their opportunity cost of funds will be affected. However, temporary disparities between these and the income or total returns on their property holdings will be more easily carried than by highly leveraged investors who need to service interest.

As an example, the effects of leverage on performance can be seen in China on developers. Figure 2 (opposite) shows the impact of gearing on relative outperformance and underperformance. This is despite the fact that borrowing rates have reduced substantially over the past year in China.

In the post-GFC world of low interest rates and constrained lending, equity has been searching for a home and asset price inflation has been inevitable. Low and even negative bond yields in some countries have meant that the opportunity cost of funds are low. As a result, investment in high-yielding jurisdictions has been particularly attractive. In prime locations of major cities, which are favoured by overseas investors, yield compression has been rapid and pronounced, sometimes taking yields to record lows as competition for trophy assets in safe havens has led to higher prices and lower cap rates.

The highly leveraged investor has found it increasingly difficult to compete unless there is a clear value-add component to their purchase. Leveraged US funds buying into London, for example, have tended to be opportunistic and shorter term while some Asian and Middle Eastern investors have looked for longer-term holds for income growth and/or longer-term capital growth.

In a world where borrowing costs and opportunity costs are returning to 'more normal' conditions, both equity investors and leveraged funds are likely to refocus on yield levels and the potential for income growth. However, there is still a level of 'global real estate arbitrage' to be completed between equity investors targeting lower hurdle rates and high-yielding jurisdictions. The variety of net effective income returns across world cities illustrates this.

FIG. 2 **China developers: profit growth and leverage in 2015**

	Out-performers	Sector average (highly polarised)	Under-performers
CORE PROFIT GROWTH	+16.%	+2%	-33%
NET MARGIN	13.2%	11.2%	10%
NET GEARING	59%	63%	68%
NET GEARING, INCLUDING DEBT REPACKAGED AS BONDS	(61%)	(80%)	(95%)
INTEREST COSTS AS A MULTIPLE OF CORE PROFIT	0.56x	0.78x	1.71x

Source: City Research

Higher-risk emerging markets may be expected to remain higher yielding but economic recovery and growth in transparent, developed markets may yet see further yield compression, especially where rental growth is expected. We expect global cross-border capital flows in real estate to continue to reflect a pattern of relatively cheap money at source and higher yields at destination coupled with a global search for rental growth. As such, many of our value-add and opportunistic researcher tips for 2016 and beyond are focused on secondary (and lower grade) property, second-tier locations (which have seen lower levels of investment in the past seven years). We also focus, especially, on new and alternative asset classes where the weight of investor money has not yet had such a dramatic impact as on the mainstream asset classes. ■

MARKET INSIGHT

Will the US continue to zig while the rest of the world zags?

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Heidi Learner explains why further monetary tightening may be likely in the US

As we approach the eighth year since the start of the global financial crisis, there is little sign that monetary policy has returned to normal, even with the recent announcement by the Federal Reserve to raise rates by 0.25% to 0.5%. No other major central bank has raised rates in close to a decade and bond yields globally remain 'extremely low' (*see fig. 1*). Inflation-adjusted policy rates are negative across most developed countries and in some places, such as Switzerland, even nominal base rates are negative.

Quantitative easing may have come to an end in the US and the UK, but asset purchases by other central banks continue. The European Central Bank is buying a set amount of assets per month, while the Bank of Japan is targeting a set increase in the monetary base for as long as necessary. Low oil prices and, in some cases, currency strength and soft import prices, have dampened global inflation pressures and the rest of the world continues to foresee weak growth prospects. Yet in the US, all 17 Federal Reserve Board members expect further 'policy firming' in 2016. Was the time really right for a rate rise?

Nominal exports as a percentage of nominal GDP growth in the US have risen from 9.8% in 1980 to 13.5% in 2014, so external growth is an important source of US GDP growth. However, export growth can be damaged by a strong dollar. Analysis from the Federal Reserve Bank of New York shows that when the impact on exports and imports is considered, a 10% appreciation of the US dollar in one quarter shaves 0.5 percentage points off GDP growth the next year. If the strength of the dollar persists, an additional 0.2 percentage point reduction occurs in the subsequent year, too. While this decline is not trivial, a 0.7 percentage point pullback in growth over two years is unlikely to thrust the US back into recession. Would further dollar appreciation be enough for the Fed to persistently deviate from its 2% inflation target and avoid further rate rises?

This is possible if monetary tightening provokes an upward spiral of capital flows that serves as the catalyst for further dollar strength. The strong dollar does not appear to be curbing domestic inflation away from the transmission of oil prices. From July 2014 to March 2015, the real dollar effective exchange rate index rose by almost 12%. Over the same period, import price inflation (less petroleum) fell by a cumulative 1.8% (*see fig. 2*). But the US CPI (less energy) rose by a cumulative 1%. This suggests that lower import prices are a minor factor affecting inflation.

2.7%

Average 10-year government bond yield in US, 2008-2015

In November, the CPI for all items (less food and energy) rose 2%, the largest 12-month increase since May 2014. Most categories in the service sector have shown acceleration over the past three months versus the past 12 months, suggesting that inflation pressures may be brewing.

Longer-term inflation breakevens have begun to stabilise, even though the Fed's measure of five-year inflation remains close to post-recession lows. Importantly, the Fed's Chair, Janet Yellen, recently highlighted in a speech that the restraint on inflation imposed by economic slack is now relatively modest. It would have been a mistake for the Fed to delay a rate hike due to concerns over further US dollar strength, especially given policy lags.

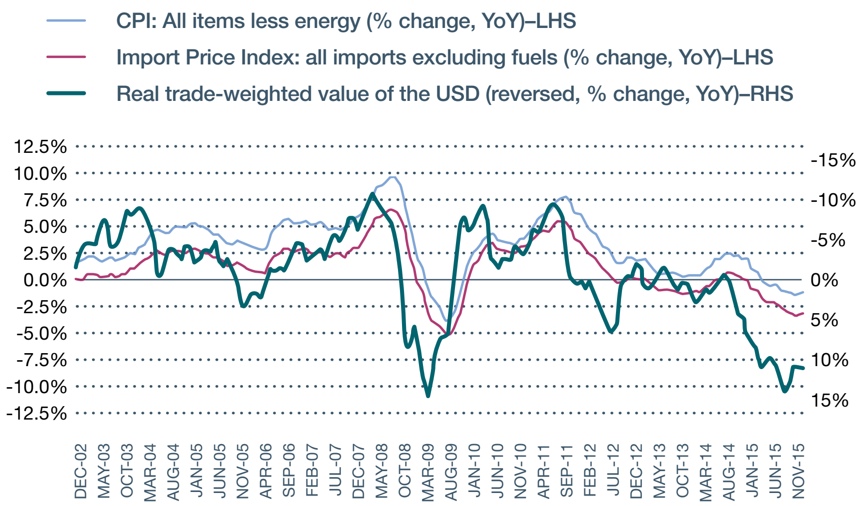
We believe that a very slow return to more normal monetary conditions has now begun in the US and will continue in 2016, with implications for central banks around the globe. ■

FIG. 1 Looser monetary policy everywhere

Country	10-year government yield average 2000-2007	10-year government yield average 2008-2015
US	4.69%	2.71%
UK	4.78%	2.90%
GERMANY	4.30%	2.22%
JAPAN	1.47%	0.96%
CANADA	4.83%	2.60%
AUSTRALIA	5.72%	4.33%

Source: Bloomberg

FIG. 2 Strong dollar impacts on US inflation have weakened, freeing the Fed to hike base rates



Sources: BLS/Federal Reserve

Where is the smart money going?

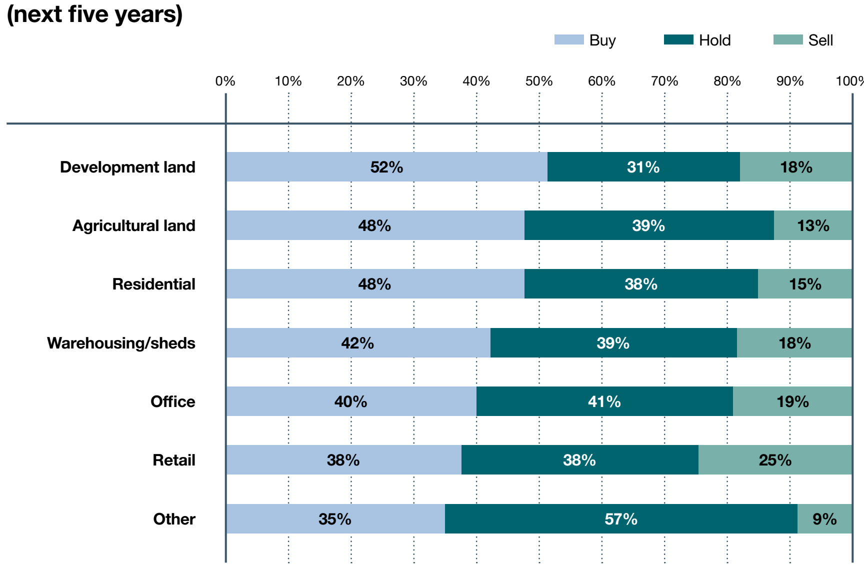
Using the *Savills Wealth Briefing* survey, we find out which cities are set to see the most investment from HNWI in the coming years

In our last issue of *Around the World in Dollars and Cents* we started to look at the impact of private wealth on global real estate. Recovering participation by institutional investors means that investment share by private wealth has since reduced slightly but still accounts for between 16% and 20% of all big ticket global transactions. The investing intentions of this sector are thus still an important indicator, especially as leverage tends to be low and the appetite for alternative assets high (*see fig. 1*).

The role of private wealth has been instrumental for example in the development of the student housing sector outside the US. Many privately funded blocks built in the UK are now being traded to US institutions. It is therefore worth understanding not just in which sectors ultra high net worth individuals (UHNWIs) and high net worth individuals (HNWIs) are interested, but also which geographies. This article looks in detail at future investing intentions of this group from a survey of advisors undertaken by Savills World Research with Wealth Briefing in 2015.

We asked wealth advisors to identify the sectors, regions and cities in which their clients intend to buy, hold and sell real estate in the next five years. The aggregated results are shown opposite (*see fig. 2*).

FIG. 1 **UHNWI and HNWI intentions: top sectors for investment (next five years)**



Source: Savills World Research/Wealth Briefing

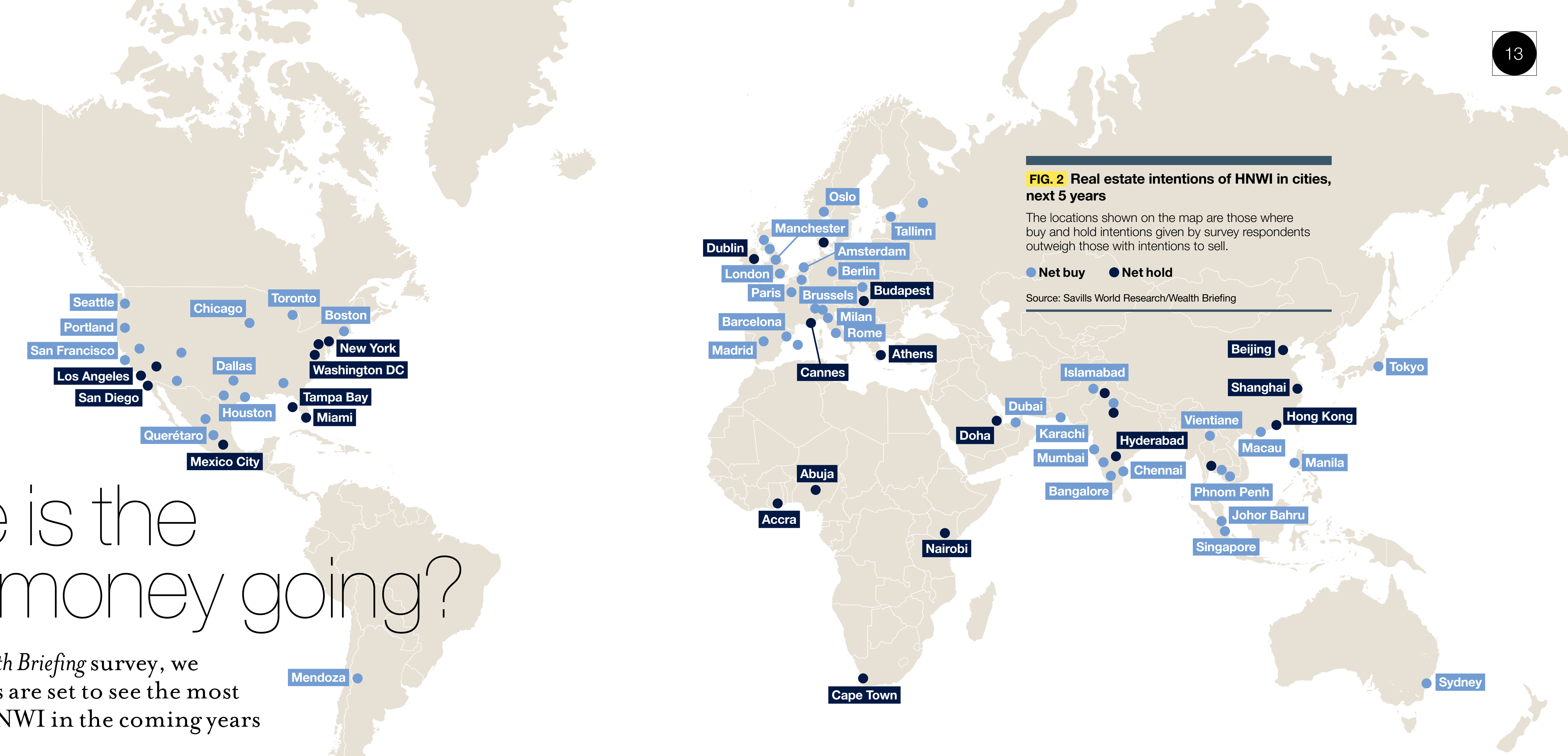


FIG. 2 **Real estate intentions of HNWI in cities, next 5 years**

The locations shown on the map are those where buy and hold intentions given by survey respondents outweigh those with intentions to sell.

● Net buy ● Net hold

Source: Savills World Research/Wealth Briefing

REAL ESTATE INVESTMENT INTENTIONS: CITIES

Gateway global cities remain buys, despite very strong recent performance and plateauing prices in some of them. Important global centres of business such as London and Dubai lead the pack, and reflect the trend for UHNWI and HNWI to invest in the cities in which they are active in business, visit often or, simply, know.

The results of our survey also reveal a broadening of purchasing intentions to other centres. Madrid, Manchester, Barcelona and Chicago are all emerging as net buys. This reflects a global trend in a crowded investors' market towards higher yielding secondary property, second-tier cities and alternative assets.

European cities exhibiting this trend include Amsterdam, Oslo, Brussels and Berlin.

In Asia, Tokyo looks set to see more UHNWI and HNWI investment as market recovery gathers pace. Singapore is a buy, along with neighbouring Johor Bahru, a nod toward the strategic benefits of the neighbouring Malaysian city. Cities in emerging economies also feature on shopping lists for the next five years. Manila is a pick in the Philippines, Vientiane as Laos' economic centre, and Phnom Penh, Cambodia's fast-growing capital.

In Latin America, Mexico City is a hold among UHNWI and HNWI, while smaller Querétaro, a safe, business-friendly city with a historic centre (designated a UNESCO world heritage site), is a buy. In Argentina, Mendoza, the largest wine-producing centre in Latin America and gateway to the Andes, stands out as a city of choice in the region.

In the US, UHNWI and HNWI investors are set to concentrate in certain pockets: the Pacific Northwest, California, Texas, parts of the south-west and north-east, along with Toronto in Canada. Cities in these regions are driven by the knowledge economy, fast-growing local populations and, in many cases, a burgeoning tech industry.

Net holds (but not new buys) include Beijing, Shanghai and Hong Kong and reflect the fact that these are already fully invested cities, as well as uncertainty around China's growth prospects. In the US, prospects for Los Angeles, New York, Washington DC and Miami remain positive but as economic recovery spreads across the country there are numerous other buying opportunities, especially in small tech-friendly regenerated cities.

African centres, including Nairobi and Cape Town, are net holds. While there has been plenty of foreign investment into income-producing assets on the continent (such as land and mining), African cities have yet to experience the same levels of inward investment seen into other regions. Africa is likely to see more acquisition activity – especially beyond the five-year horizon of our survey.

Overall, the world still offers a big field for global real estate investors to play in. Private investors and quasi-private equity like sovereign wealth funds will often point the way to where corporate money and institutions follow. ■

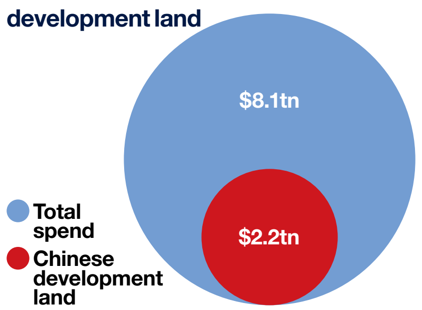
Selling the world

The amount of global investable real estate traded is at its highest level since 2008 – a recovery that's taken place over four specific phases

A total of $8.1 trillion of global investable real estate has been traded since the beginning of 2007 in the form of big ticket ($10 million-plus) deals. Of those deals, $2.2 trillion-worth were made up of Chinese development land deals. This represents 3.7% of all global real estate and 11.1% of all tradeable investment stock.

Just under 1% (0.9%) of the world's investable real estate stock trades in big ticket deals each year.

Between 2007 & 2015, 27% of global real estate deals were Chinese development land



Average annual real estate trading volumes (excluding Chinese land) since 2007 have been $683 billion, which is 39% lower than the global peak of $1.13 trillion in 2007.

Volumes have increased steadily since 2012 and, last year, they reached their highest level since the global financial crisis of 2007-08 (GFC) began. In 2014, volumes were $871 billion and we project that they will hit $887 billion in 2015. This is 338% more than their 2009 low of $262 billion.

THE PAST EIGHT YEARS IN DETAIL

Global trading in real estate since the financial crisis of 2008 has seen four distinct phases: downturn, bounce back, cooling and stability (excluding Chinese land deals and joint ventures, *see fig. 1*).

Downturn
Q1 2008-Q3 2009

IN THE AFTERMATH of the GFC, investment activity was substantially reduced, especially in North America, where it fell by 84% from $418 billion in 2007 to an average annual figure of $93.7 billion over this period.

As US volumes fell, EMEA took over as the region with the highest real estate trading volumes during this period – averaging $151.8 billion per year – while Asian trading volume fell the least (61%), buoyed by stronger economic growth in China and Asia Pacific countries and a growing appetite for real estate.

Globally, and especially in North America, institutions that had been dominant buyers in 2007 reduced their trading volumes by 79% in the downturn. This impacted all the major real estate asset classes equally, except for development land, which was held up because it was being traded in large quantities in China.

The market share of owners, users and operators increased during the downturn period as their reasons for trading were less investment-motivated and therefore less affected by recession in these markets.

Bounce back
Q4 2009-Q3 2011

THE IMPACT OF quantitative easing during this period was profound and continued to last for more than five years. Low interest rates and expectations of lower yields resulted in increasing expectations of significant value inflation in a range of commodities and asset classes, not least real estate. The end of the last quarter of 2009 marked the beginning of this turnaround in global stock markets. World-class real estate markets quickly followed suit and global real estate investment volumes were showing annual rises by the fourth quarter.

The most active players during this period were the more opportunistic REITs and REOCs, who had been net sellers to institutions in 2007. They were able to re-enter markets at lower pricing points and, with their listed status, raise funds in the newly reinvigorated stock markets.

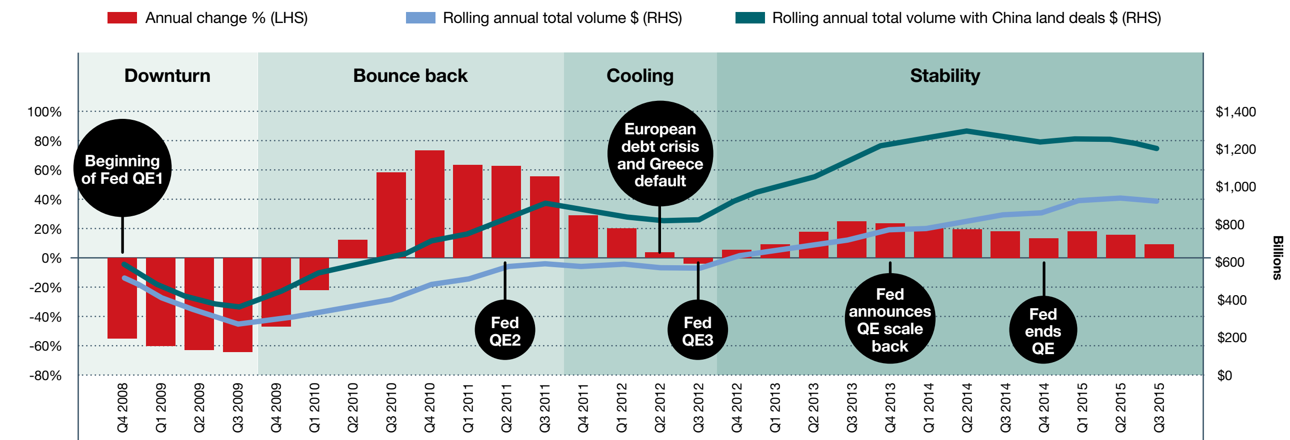
The biggest recovery in transaction volumes was in markets that had been hit hardest in the downturn because they came off a particularly low base. Over and above this, though, a notable change happened in the appetite for sectors previously considered more alternative or niche. It also marked a period of much lower market share in the office markets. The volume of office trading simply did not bounce back to the same extent as other sectors.

Hotels and industrial property showed the strongest rebound, while the apartment market started a sustained increase in market share, which has since not abated. Volumes in residential property increased by 150% as some buyers took advantage of bulk deals from distressed owners and developers. The number of hotel deals also increased by 221% over the same period, for similar reasons. This period, therefore, marked the beginning of a maturing process for some sectors.

Cooling
Q4 2011-Q3 2012

THIS COOLING PERIOD relates to a period of much slower rates of growth in the volume of big real estate trades. Average global volumes were still slightly higher during this phase than they had been. The slowdown in volume growth rates was led by Europe as investors, particularly institutions and REITs/REOCs, became somewhat more

FIG. 1 **Global investment volumes (all buyer types)**



Source: RCA (>$10m deals)/Savills World Research nervous in the wake of the eurozone debt crisis and began avoiding euro-denominated assets. EMEA volumes fell by 10% over the period.

Private investors came to the fore during this phase, taking market share where the less adventurous corporate buyers left off. This helps to explain the resilience of residential property, an asset class favoured by these investors, during this period. It was a relatively short phase of global jitters compared to the downturn and started to reverse when the Fed announced yet another round of quantitative easing (QE3).

Stability

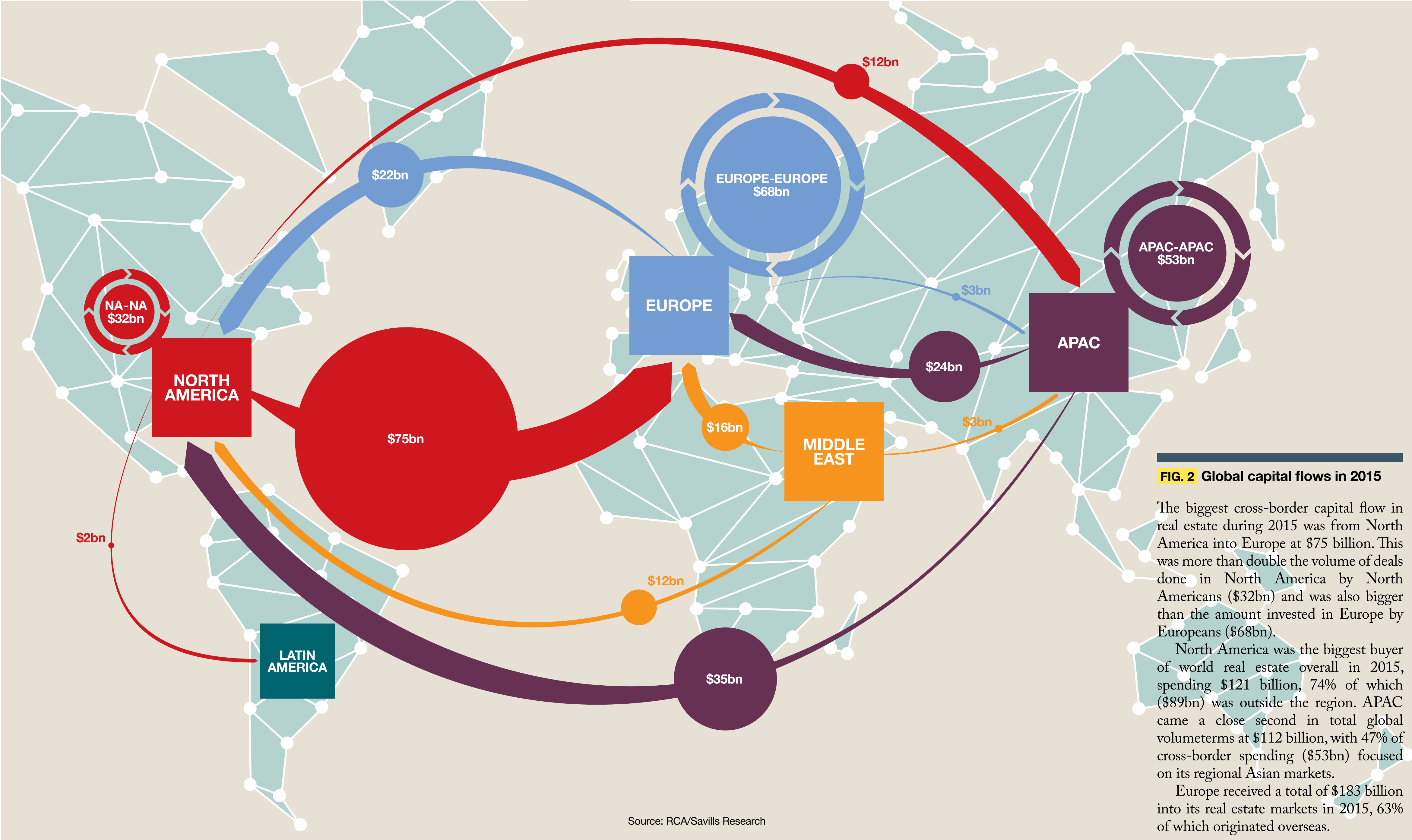
Q4 2012-Q3 2015

FOR THE PAST three years there has been a period of steady growth in global real estate trade volumes, particularly in North America and EMEA, which have grown by 62% and 65% respectively. Annual North American volumes have been $322 billion, compared to their 2007 peak of $418 billion. Annual EMEA volumes have averaged $246 billion, compared with $355 billion in 2007.

Asia Pacific (APAC) has seen much more subdued rates of growth in average annual trading volumes – at 18% over the same period – partly as a result of slower economic growth in China. Having said this, APAC volumes are the closest of any world region to their $160 billion 2007 peak, having averaged $155 billion during the stability phase.

Hotels and apartments have continued to grow as sectors during this period but development sites have shown weak growth (even without counting the sharp demise in Chinese land deals).

This period of stability has particularly favoured those investing institutions whose participation in deals has increased by 69% during the latest stable growth phase of Q4 2012-Q3 2015.



Source: RCA/Savills Research

FIG. 2 Global capital flows in 2015

The biggest cross-border capital flow in real estate during 2015 was from North America into Europe at $75 billion. This was more than double the volume of deals done in North America by North Americans ($32bn) and was also bigger than the amount invested in Europe by Europeans ($68bn).

North America was the biggest buyer of world real estate overall in 2015, spending $121 billion, 74% of which ($89bn) was outside the region. APAC came a close second in total global volumeterms at $112 billion, with 47% of cross-border spending ($53bn) focused on its regional Asian markets.

Europe received a total of $183 billion into its real estate markets in 2015, 63% of which originated overseas.

Construction in Wuhan's Han Street business district

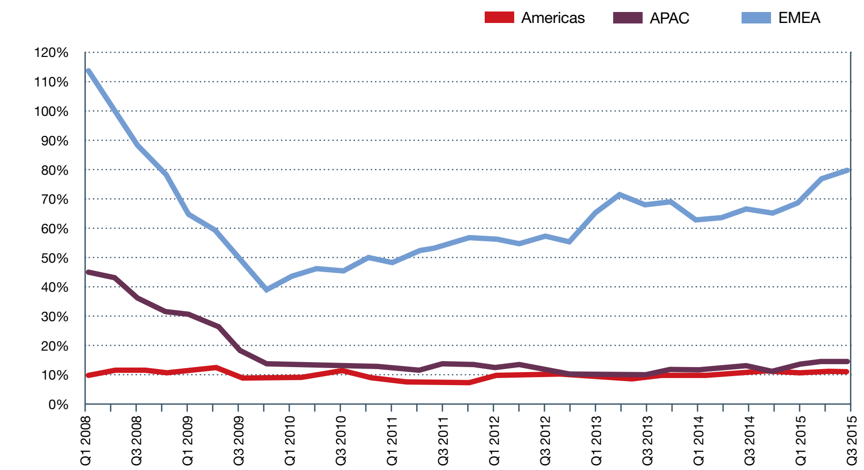
GETTY IMAGES

THE GEOGRAPHY OF CROSS-BORDER REAL ESTATE TRADING

Inward investment from overseas is more important to European real estate markets than Asian and American ones. Prior to the GFC, Asia was a greater recipient of overseas real estate investment, with one in every two domestic deals bought by investors outside the region. It is now more like the Americas, which see just over one deal in every ten traded outside the region.

EMEA, though, is a much more global real estate market. In 2007, there were more cross-border deals done than trades within the region. This plummeted in 2008-2009 but has since picked up strongly. Cross-border deals by a wide variety of international players now account for 8 in every 18 EMEA deals (*see fig. 3*).

FIG. 3 Cross border to domestic investment ratio (rolling annual)



Source: RCA/Savills Research

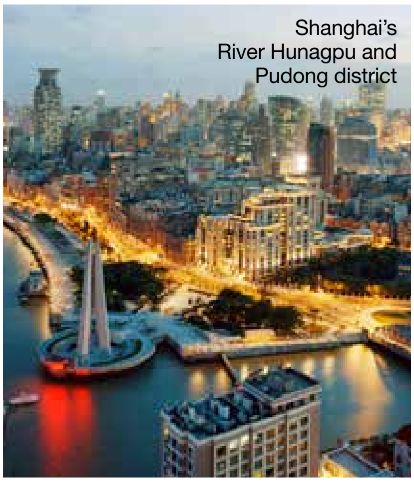
The sector seesaw

The demand for offices is markedly lower since the downturn, but this drop is mirrored by an increased appetite for residential property

The impact of world capital flows and new types of money in global real estate since 2008 has shown up in changing investment volumes in different asset classes. Offices are still the largest traded asset class but have fallen out of favour in relative terms. Since 2008, offices observed the biggest drop in trading of 6%, although it is still the most dominant asset class with more than a third of total trading volumes at 36%. Some of this fall is due to lower availability resulting from less frequent trading and grade A stock being locked up in long-term portfolios.

The drop is partly the result of falling institutional appetite as well as changes in working practices, which have altered occupier behaviour and threatened the performance of some locations and building types.

Meanwhile, an appetite for residential property has burgeoned among both private investors and REITs – a trend that is likely to continue as it is supported by growing occupier demand from both Generation Y in developed economies



Shanghai's River Hunagpu and Pudong district

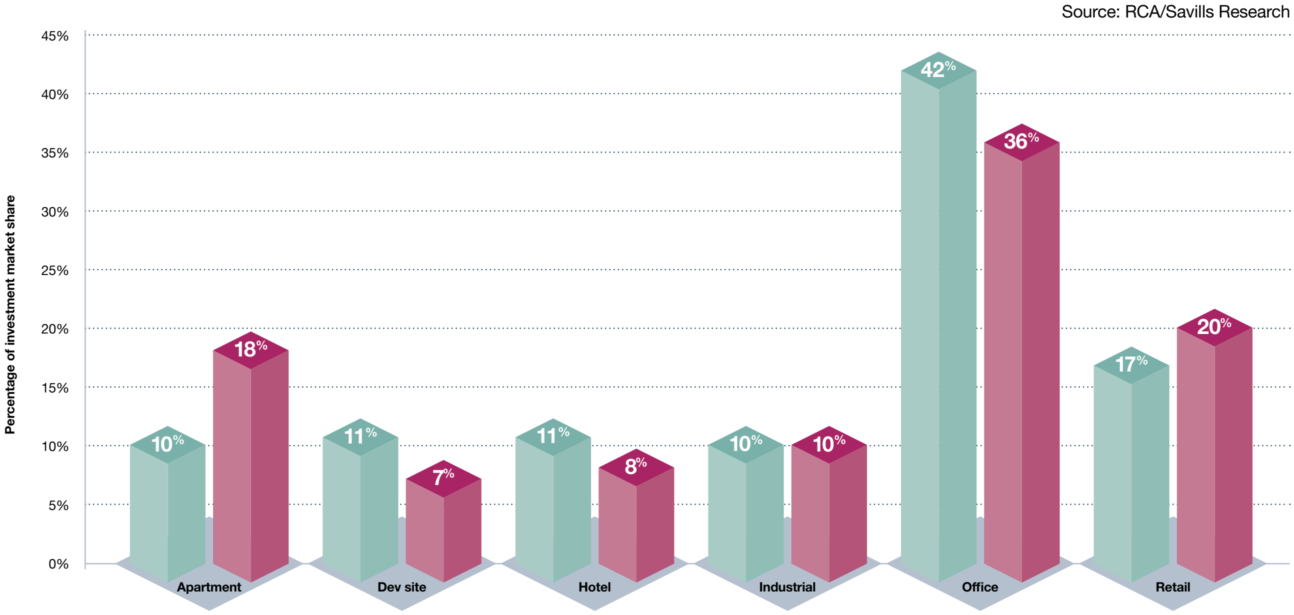
and a growing middle class in emerging ones. Residential investment market share has nearly doubled since the downturn, and is currently hovering at 18%. Growing investment in this sector outside as well as inside the US by institutions is also likely to fuel greater future transactional activity in apartments. Office and residential exhibit a weak inverse correlation trend, suggesting that money has transferred from one sector to the other fairly efficiently.

In addition, demand for retail property is underpinned by similar demand characteristics as a result of new housing development creating the need for new neighbourhood services.

Consumer spending also increases in line with urbanisation, wealth creation and growth in the number of middle class consumers, fuelling retail demand and the prospects for growth in the sector globally. The retail sector has also shown some resilience, growing its market share by nearly 4% over the past seven years. We expect to see increasing transaction numbers in the coming years as well.

The steadiness of the industrial sector belies a big difference between logistics warehousing, closely allied to the retail sector and dated manufacturing units. The global growth in e-tailing means there is more investor interest in logistics in many parts of the globe and this has offset what might have otherwise been declining appetite for out of town manufacturing and workplaces. ■

FIG. 1 Investment market share – 2008 v 2015



Source: RCA/Savills Research

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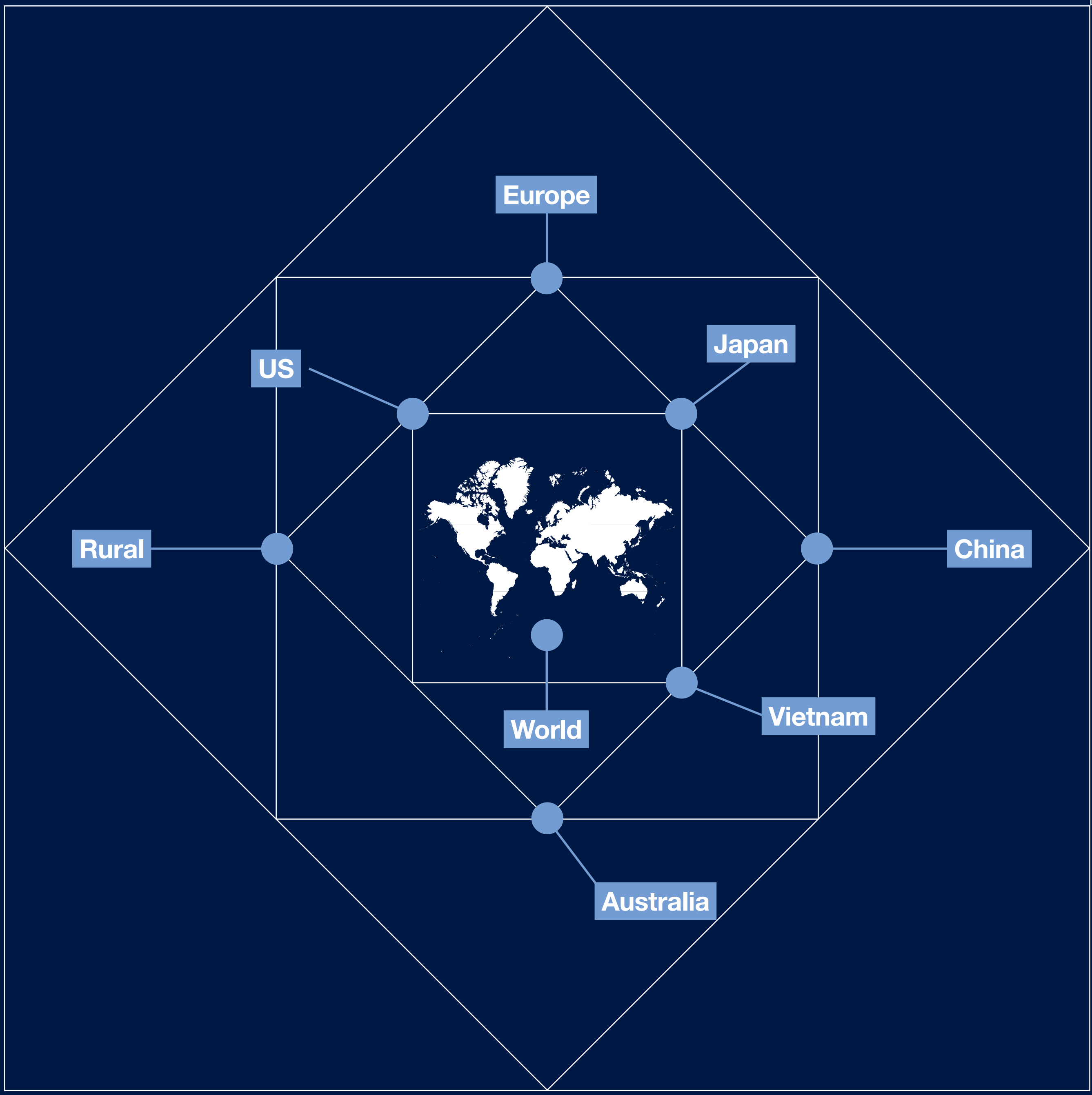


Global real estate tips

Savills' experts reveal the next real estate hotspots

THE FOLLOWING section of this report explores in more detail what and where the future playgrounds might be for a wide variety of investors.

Over the next five years we are likely to see further recovery in those markets that were hit by the economic downturn, particularly Europe. Stable prices but lower transactional activity seem to be on the cards for core prime cities that have been fully invested in recent years. Meanwhile, small cities that are succeeding in the tech economy, as well as those where strong economic growth is expected nationally or locally, are likely to see increased transaction levels.

Smaller US cities and key European cities are likely to be the mainstay of this trend, while India seems the most likely country to benefit from growth in emerging markets. However, barriers to real estate investment are still a feature in many jurisdictions. Anti-foreign investor regulation and legislation will reduce cross-border activity, as will high levels of corruption and lack of transparency in some places.

Geopolitical factors will also dampen appetite in certain regions, notably the Middle East, although conflict and displacement may boost the appetite for outward, 'safe-haven' cross-border activity, and for some of the more stable real estate and cities within the region.

Turn the page for our tips

Australia

The devaluation of the Australian dollar over the past five years means the country is in a prime position for investment, with demographic change creating opportunities

TIPSTER: TONY CRABB, HEAD OF AUSTRALASIA RESEARCH

River Yarra, Melbourne

GETTY IMAGES

Australia is known as 'the lucky country' because it is blessed with an abundance of natural beauty and resources, and all the amenities the first world has to offer. And with these great endowments come great opportunities.

The Australian dollar has devalued against the US dollar over the past five years, which means real estate looks 36% cheaper to overseas buyers (*see fig. 1*). It also means that cross-border investment is inward rather than outward, and Australia is well-placed to attract overseas currency.

Demographic change is one of those opportunities. Over the next 30 years, Australia's population of over-65s is forecast to grow from 3 million people to 9 million. There is a very strong real estate story in this, with opportunities for residential downsizing, lifestyle and leisure property, retirement living, care homes and the evolution of shopping centres.

At the other end of the age scale, a higher number of women in the workforce means that the demand for childcare is growing dramatically. Demand for premises exceeds supply, making returns look compelling. Government regulation of the sector should mean secure tenants and a relatively low-risk property play. The right buildings, locations, operators and service pricing should reap rewards.

CORE-PLUS TIP
AUSTRALIAN CITIES – SHORT, MEDIUM AND LONG TERM

Australia's population growth is among the strongest in the world (*see fig. 2*). The vast majority of immigrants are under 35 and have skills that are either in short supply, or are going to become scarce because of the high number of older workers who are leaving the workforce and heading into retirement.

This creates ongoing demand for residential property, retail goods and services, which feeds into logistics, warehousing and manufacturing, and demand to occupy office property. The two cities set to benefit the most from this trend are Melbourne and Sydney.

As the population of these two cities is set to double over the next 35 years, long- and short-term property opportunities abound. Perth, Brisbane, Adelaide and Canberra will also see the benefits of this trend.

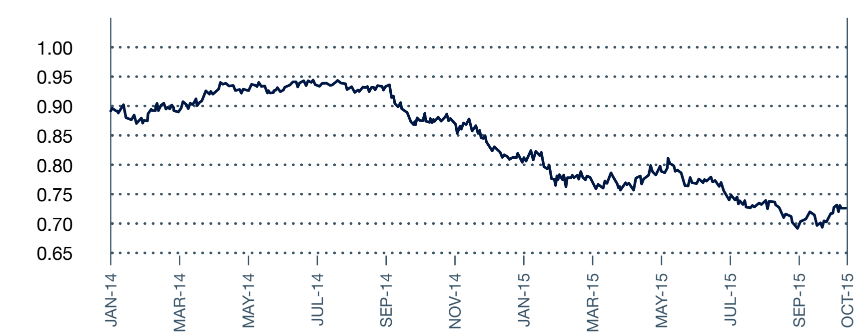
Demand from a growing population will impact many types of real estate

VALUE-ADD TIP
STUDENT HOUSING – SHORT AND LONG TERM

Another sector related to demographics, but with implications that are less explored, is student accommodation. Australia is the fourth-largest international student market in the world behind the UK, the US and France. Not only does it have a strong, well-developed tertiary education sector, but its marketing of university places overseas is also advanced. However, the provision of accommodation for international students is grossly undersupplied.

Demand for tertiary education is growing globally, so the opportunities in this sector are both short and long term. When the Australian dollar was at parity with the US dollar, international students would show a preference for universities in the US, but the exchange rate has essentially put a '36% off' sale tag on tertiary education in Australia. With its universities ranked highly in the world, demand has begun to skyrocket. Student accommodation is currently estimated to only be enough to cater for 10% of the total demand; Melbourne is the third-largest international student city in the world behind London and New York.

FIG. 1 Australian USD Exchange Rate ($) January 2014-October 2015



Sources: Australian Bureau of Statistics/Savills Research

FIG. 2 Major City Populations and Growth Forecasts 2015-2025

City	2015	2020	2025	Per annum forecast growth
BRISBANE, QLD	2,345,000	2,607,000	2,872,000	2.0%
SYDNEY, NSW	4,904,000	5,317,000	5,725,000	1.6%
CANBERRA, ACT	398,000	437,000	475,000	1.8%
MELBOURNE, VIC	4,514,000	4,978,000	5,439,000	1.9%
ADELAIDE, SA	1,324,000	1,404,000	1,480,000	1.1%
PERTH, WA	2,112,000	2,461,000	2,817,000	2.9%

Sources: Australian Bureau of Statistics/Savills Research

OPPORTUNISTIC TIP
RESORTS AND HOSPITALITY – SHORT AND LONG TERM

Currency movements and visitor volumes are also a theme for my final tip: tourism. Tourism property takes the form of resorts and hotels, and can be found in locations across the country.

In the short term, with the currency not purchasing as much foreign money as it once did, Aussies are more likely to holiday at home. That trip to Hawaii, Las Vegas or New York is now 36% more expensive so a domestic break starts to look more appealing. The resorts of Queensland and northern New South Wales, as well as the state capitals, have much to offer and ought to expect to see greater occupancy from locals.

The other compelling element of the exchange rate is that Australia has become cheaper for overseas visitors. While the tail-end of the Global Financial Crisis is still having an impact on tourism worldwide, Australia has gone from being an expensive place to visit to somewhere that could be considered reasonably priced, or even good value. We would expect to see more international visitor numbers in the near term too.

In the long term we expect to see an incredible increase in the number of Chinese visitors, encouraging us to recommend long-term plays for Australian tourism assets. Starting in first-visit destinations such as Sydney and Melbourne, we believe AsiaPac visitors will later branch out into other pursuits, or return visits. This is where the forecasting risk increases as Chinese tourism is still in its infancy. A new-found penchant for sunshine and ocean pursuits might bode well for the Gold Coast, growth in snow pursuits would benefit ski resorts, while a search for the wilderness and outdoor sports might make the right real estate in the Northern Territory look good value.

The development of real estate to cater for these huge potential markets will require cutting-edge intelligence and a highly tuned responsiveness to this fast-growing sector of Asian tourism. ■

China

There's long-term value to be had from limited office supply in prime locations, while demand for residential space has been boosted by recent interest rate reductions

TIPSTER: JAMES MACDONALD, RESEARCH DIRECTOR, CHINA

Chinese real estate markets started slowly in 2015 (*see fig. 1*), but investment picked up in response to falling interest rates (five-year loans were down 165 bps in 12 months to 4.9% in October 2015). The large issuance of domestic bonds at comparatively lower coupon rates, along with other supportive measures from the government, also meant lower costs on development debt finance.

Domestic purchasers continue to dominate the Chinese market, although some international investors have been building war chests in anticipation that slower economic growth will create pockets of distress and buying opportunities. Others hope to unlock new opportunities in niche markets using approaches learned in other international markets. So far, most investment has focused on the first-tier cities, particularly Shanghai. Here, we present some alternatives for these investors.

CORE TIP

PREMIUM GRADE A OFFICES IN SHANGHAI'S LUJIAZUI AND BEIJING'S FINANCIAL STREET – LONG-TERM HOLD

Shanghai's office market fundamentals look weak because significant volumes of new supply are expected, but much of this is located in decentralised and non-prime locations. Prime locations, especially in Lujiazui, will see limited supply but we expect demand to be strong from financial institutions that are expanding rapidly on the back of the Shanghai Free Trade Zone policies.

Beijing's Financial Street has similar characteristics, with limited new supply and strong demand from financial institutions. Both these markets represent some of the most expensive commercial real estate at close to the top of their current rental cycles.

So far, most investment has focused on first-tier cities, particularly Shanghai

Nevertheless, these areas are unlikely to be dislodged in the mid to long term and present tremendous long-term value – if the assets can be prised away from current owners.

CORE-PLUS TIP

GRADE B OFFICE PROJECTS IN SHANGHAI AND BEIJING – SHORT TO MEDIUM TERM

One of the mainstays for core-plus investors is the investment in slightly dilapidated office buildings in central locations and spending some capital to bring them closer to Grade A standards. We think this will hold true in 2016. Although certain failures in the original design may be impossible to overcome (low ceilings, for example), relatively simple value-add steps can sometimes increase rents and capital values by 10% to 20%. Building maintenance, while improving, continues to fall far short of international standards. This means buildings that are sometimes only ten years old appear much older, and there is potential to add value by improving this.

CORE-PLUS TIP

EQUITY INJECTIONS TO LOGISTICS OPERATORS – LONG TERM

Logistics have been a favourite of investors for the past two years on the back of the rapidly growing e-commerce market and demand from third-party providers. The market is dominated by a handful of international and domestic players who have established large market shares and made it difficult for other investors to make inroads – apart from in the more specialised logistics fields.

Investors still looking to get into these markets are partnering with some of the mid-size developers to provide the capital to grow rapidly and carve out more market share. Alternatively, equity injections into some of the larger players has also been a route for larger investors. Developers focusing on leading cities with scarce land supply will be better positioned in coming years as only limited new supply is expected. However, lower-tier cities are expected to see burgeoning supply in the coming years.

SOHO, Wangjing District, Beijing

GETTY IMAGES

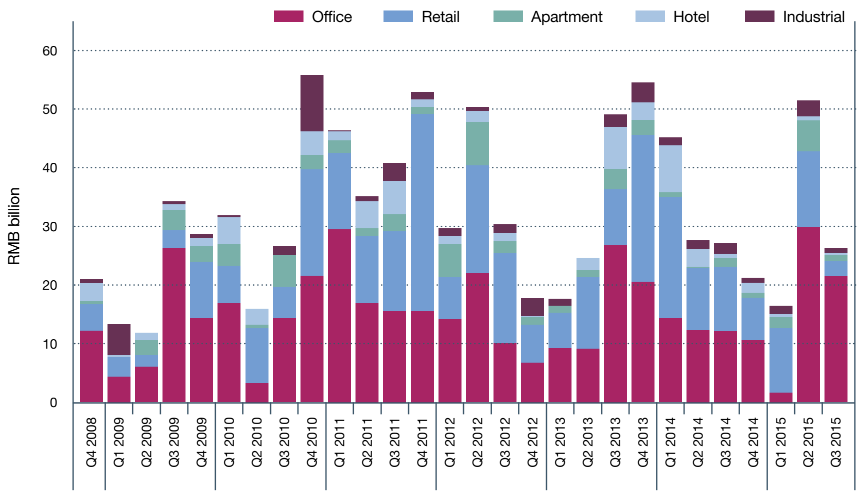
OPPORTUNISTIC TIP

RESIDENTIAL DEVELOPMENT IN CENTRAL/MATURE LOCATIONS OF SECOND-TIER CITIES – SHORT TERM

The residential market can be extremely fraught in China, with policy changes throwing curveballs to developers and investors alike. Recent policies and interest rate reductions have stimulated demand, especially in first-tier cities, pushing prices in leading cities to new heights. Smaller cities, however, are still plagued with oversupply that will take several years to digest.

Nevertheless, opportunities are once again presenting themselves in second-tier cities that have started to see prices rise on the coat-tails of rapid price growth in first-tier cities. Land premiums have started to rise but continue to remain affordable when compared to the irrational prices that residential land is selling for in first-tier cities. Our top picks include Hangzhou, Nanjing, Wuhan and Suzhou.

FIG. 1 Investment Volumes Excluding Development Sites (deals larger than RMB100 million)



Sources: Real Capital Analytics/Savills World Research

ALTERNATIVE TIP

NICHE MARKETS – ESPECIALLY ELDERCARE AND HEALTHCARE – LONG TERM

There is a lot of money floating around in China at the moment; however, a large portion of this is passively invested, as is chasing traditional asset classes all the way to the top of the market cycle. The smart money, however, is looking at mid- to long-term plays in niche markets. These can be tricky areas as there are few established players and business models are still in a state of flux – and some of these industries have had false starts in the past.

For braver investors, niche sectors represent the best bet for higher returns. Key sectors to look out for are eldercare and healthcare. Rising incomes and an ageing population, as well as a creaking state system that cannot accommodate the growing needs of a burgeoning urban population, are creating unprecedented demand against extremely constrained supply. The state is opening up the sector to competition, which creates a number of opportunities for private companies. ■

Around the world in dollars and cents ■ Savills.com

Japan

A boost in tourism from China, a burgeoning logistics sector and stable rental income from office space means things are looking bright in the Land of the Rising Sun

TIPSTER: SIMON SMITH, HEAD OF ASIA RESEARCH

Cityscape of Tokyo showing the Tokyo Tower

Economic recovery, a rapidly expanding tourist industry and the forthcoming Olympics are a few of the factors driving the Japanese real estate markets.

OPPORTUNISTIC TIP
HOTELS AND HOSPITALITY – MEDIUM TERM

Japan's hospitality sector is in a good position to profit from a growth in tourism, especially from mainland China. For example, average daily hotel room rates (ADRs) have already grown by 40% over the past three years in Osaka and by around 20% in Tokyo. We expect this trend to continue as the Tokyo 2020 Olympic Games draw closer and Japan's global profile increases. That said, investors in this space need to be nimble and must be prepared to risk disruptive events that could dramatically change the outlook of the industry. These include both natural and man-made disasters. In addition cap rates have compressed significantly of late, so entry costs can be high. However, income growth should justify this as we expect ADRs to rise even further.

VALUE-ADD TIP
LOGISTICS – MID TO LONG TERM

The logistics sector has been enjoying strong demand in Japan. E-commerce currently accounts for just 5% of all Japanese commerce, compared with 15% in the UK and 10% in the US, so there is considerable scope for growth. We think that Japan's widely reported ageing demographic will help e-commerce to grow. This has an impact on the logistics sector, which is instrumental in fulfilling orders in the face of what should be significant future demand for the convenience of home delivery. Japan's supply of logistics warehouses will increase substantially over the next year so there may be a temporary softening in values over the short term, possibly offering buying opportunities. In the mid to long term, we expect a substantial growth in demand for the right premises in strategic locations that are able to service the changeable needs of e-commerce delivery and returns.

GALLERY STOCK, GETTY IMAGES

Dotonbori, Osaka's famous pedestrian street

CORE (STABLE INCOME) TIP
GRADE B OFFICES – MEDIUM TERM

There are opportunities in core locations such as Tokyo, Osaka and Nagoya for investors who are looking for income. Grade B offices should continue to provide stable income streams to core investors. Potentially, rents could even increase. Considering the ultra-low funding costs in Japan – the yield carry (NOI – borrowing costs) is currently an attractive 3% to 5% – cash-on-cash returns should be comfortably higher.

CORE-PLUS TIP
GRADE A OFFICES – MEDIUM TERM

Despite Grade A rents in Tokyo having risen steadily for consecutive quarters since Q2 2012, the rental average remains approximately 40% below the previous cyclical high of 2007. This not only

Japan's widely reported ageing population could help e-commerce to grow

mitigates downwards risk but indicates that the market has an upside potential. In combination with strong occupier demand and reduced availability, the recovery in rents is expected to continue although tenants will tend to be price-sensitive in the event of any economic uncertainty. Recent uncertainty in the global economy has made property investors cautious, although slow but steady growth is expected in the rental market. ■

Vietnam

Improving economic conditions have led to a rise in the fortunes of Vietnam's property industry, with urbanisation, tourism and retail development leading the way

TIPSTER: TROY GRIFFITHS, RESEARCH DIRECTOR VIETNAM

The property industry in Vietnam enjoyed a good 2015. Following on from the government's monetary policy of 2013-2014, Vietnam's macro-economic conditions are now the best they've been for some time. Almost all asset classes have rebounded, most notably the residential sector. Legal reforms, meanwhile, continue to transform industry practices. Vietnam performs counter-cyclically to the region, and in 2015 it outperformed its regional peers. This trend is set to continue in 2016, although some headwinds persist.

VALUE-ADD TIP

VIETNAM LANDED RESIDENTIAL DEVELOPMENT – LONG-TERM CAPITAL GROWTH

Rapid urbanisation, a fall in household occupancy and a young population will continue to underwrite residential property demand in Vietnam through 2016 and beyond. In the short term, economic fluctuations represent the main risk, but the growing middle-class demand for new homes will be a long-term phenomenon, as long as the economy continues to perform. Amended housing laws now allow for foreign investment in this sector.

The landed residential markets in Ho Chi Minh City and Hanoi enjoyed strong supply and good absorption in 2015. Products are now diversified and oriented towards consumers, with developers vying for market share and producing villas and townhouses with 'cradle-to-grave' facilities, including healthcare and tertiary services for the aged. This asset class also benefits greatly from improvements in infrastructure and new links, drawing the 'mortgage belt' closer to the city.

OPPORTUNISTIC TIP

VIETNAMESE RESORTS – LONG-TERM TOTAL RETURNS

More than half of the world's tourists come from China and Russia, and Vietnam's long coastline and good weather are in close proximity to both countries. Hospitality development throughout the country kicked off with fervour in 2015 and will deliver world-class product, supported by great coastal locations, quality golf courses and international architecture in outstanding destinations in 2016 – from Halong and Danang in the north to Nha Trang and Phu Quoc in the south.

More than two-thirds of the country's tourists are domestic Vietnamese travellers. The second generation of hospitality development will leverage initial success by developing second homes and resort accommodation.

The growing middle-class demand for new homes will be a long-term phenomenon

River Saigon, southern Vietnam

Residential district of Ho Chi Minh City

GETTY IMAGES

Throughout 2016 there will be a range of coastal homes available all over Vietnam from affordable levels to global prestige quality.

CORE-PLUS TIP

VIETNAM RETAIL – LONG-TERM TOTAL RETURNS

Retail development has been feverish as foreign and local developers compete in this rapidly changing environment. Year-on-year growth in retail sales stood at 9.1% in September 2015, one of the highest rates globally. Little wonder that there has been so much M&A activity in retail. Alongside the strong Vietnamese retailers, many foreign developers are now rolling out their formats. In 2016 there will be more contemporary space added, with new retail formats to be tested such as the Takashimaya/Saigon Centre in Ho Chi Minh City. ■

Europe

There are opportunities in all sectors of real estate on the 'old continent' thanks to an increase in students, immigrants, a talented workforce and an ageing population

TIPSTER: ERI MITSOSTERGIOU, RESEARCH DIRECTOR, EUROPE

Diverse, multi-speed Europe continues along the path to recovery with growing demand for real estate in major cities. 'Tech cities' such as Berlin and Dublin have outperformed as they attract a young, well-educated workforce.

CORE/CORE-PLUS TIP
SHOPPING CENTRES IN GROWING CITIES – SHORT TERM

Prime, dominant shopping centres with strong catchment areas will remain winners in the retail scene. They will continue to attract shoppers and visitors; whether they generate sales on site or online, retailers will want consumer exposure via these leisure, lifestyle and experience destinations. London, Paris, Munich, Madrid, Berlin and Moscow are expected to show strong population growth over the next decade and, importantly for retailers, to retain a high share of affluence.

CORE/CORE-PLUS TIP
PRIME SUSTAINABLE WORKSPACE – MEDIUM TERM

Innovation sectors are expected to grow quickly over the next decade in Dublin, Madrid, London, Barcelona and Warsaw. This should attract a talented workforce so buy prime 'green' offices in these and other innovative/smart cities. Occupiers will be focused on attracting human capital and the top talent wants smart, sustainable cities with a good lifestyle. Investing in flexible, sustainable buildings favoured by a 21st-century workforce is essential, as this will be a key parameter for innovative companies that have corporate social responsibility high on their agenda.

VALUE-ADD TIP
HOSPITALITY AND MIXED USE IN EUROPEAN HERITAGE CITIES – MEDIUM TERM

People like to visit and live in cities that have history, creativity, tourist attractions, lively, mixed-use city centres, a diverse retail offering and leisure activities. There are several of these in Europe that are attractive in this respect, and in many of them there are historic buildings in attractive locations that are not being used to their full potential. Refurbishments and conversions, and the use of new technologies, can add value to such properties. In London, Madrid, Milan, Vienna, Paris, Stockholm and Amsterdam, an increasing number of buildings are being converted from offices to residential homes or hotels, and are being redesigned and reused for retail, cafés and restaurants. The 'old continent' offers many opportunities for imaginative re-use, innovation and hospitality.

OPPORTUNISTIC TIP
OFFICES AND OFFICE DEVELOPMENT IN EASTERN EUROPE – MEDIUM TERM

Lower labour and property costs in eastern Europe, combined with high education levels, are acting as a magnet to back-office operations for large Western companies. Eastern Europe presents a good alternative to outsourcing in the more remote and culturally different markets of the Far East. It also benefits from being in a closer time zone. Near-shoring is a trend which may offer opportunities for office investments/developments in secondary office locations/cities in places such as Poland, the Czech Republic, Hungary, Romania, Slovakia, Bulgaria and Slovenia.

OPPORTUNISTIC TIP
EUROPE HEALTHCARE – LONG TERM

Europe's ageing population, as well as the influence/affluence level of the post-war baby boomers, means that there is a need for more and better healthcare facilities that offer a wide spectrum of services and support. Because of the high debt levels of some European governments, it is less likely that the public sector will provide the facilities that might be in demand in places such as Spain, Italy, France and elsewhere. Investing in private clinics, care homes and other facilities, especially in markets with above-average affluence levels such as Germany and France, is an already-emerging trend.

Top talent wants smart, sustainable cities with a good lifestyle

PLAIN PICTURE


Piazza del Duomo, Milan

OPPORTUNISTIC TIP
MICRO-APARTMENT DEVELOPMENTS IN HIGH-DEMAND CITIES – SHORT TERM

The rising number of single households, smaller households, immigrants and students in big cities – as well as ageing populations – where conventional housing supply is limited, is translating into demand for affordable 'micro-living'.

Investments in student housing and micro-apartments in cities with large student communities, as well as rapid urbanisation trends, is something that is already happening in the UK, the Netherlands and Germany, and accounts for a rising share of investment activity.

In the future this can continue to focus on the megacities of Europe (London, Paris, Berlin, Madrid and Munich) but also in growing innovation hubs such as Dublin, Barcelona, Amsterdam and Stockholm. In this sector there could be two options: to focus on affordable accommodation for the mid to low incomes, or on high-end accommodation for higher income professionals or students.

VALUE-ADD TIP
LOGISTICS IN EUROPE – SHORT TERM

E-commerce in Europe grew 22% last year, creating a higher demand for warehousing space and distribution networks. Investment and development opportunities abound in warehouses that can service the changing needs of the e-commerce sector in Europe, primarily in megacities such as London, Paris, Berlin and Madrid.

Depending on the type or scale of the logistics space and its role in the supply chain, logistics premises may be located within the regions of these urban centres (urban logistics) or in well-positioned and well-connected Eastern European locations where land and labour costs are lower, for example in Poland and Romania. The sector is evolving and being driven by the growth of e-commerce, technological evolution and innovations in logistics, so demand is varied but is expected to grow significantly. We expect rents and values to be driven up for the right property in the right locations. ■


The wealthy Östermalm district of Stockholm

US

The stateside market is looking buoyant, and a global search for yield makes investing in a range of US real estate an increasingly attractive proposition in key locations from east coast to west

TIPSTER: KEITH DECOSTER, DIRECTOR OF RESEARCH, USA

Suburban housing development in Scottsdale

GETTY IMAGES

Call it what you will – a wall or tsunami of money, dry powder or patient capital – there is no shortage of investors seeking safety and a bit of yield. However, finding quality properties is a challenge. With turbulence and capital outflows in emerging markets on the increase, commercial real estate in the US is looking ever more appealing. Cap rates in the gateway markets – Manhattan, Boston, Washington DC, Los Angeles, San Francisco and Chicago – have fallen below 5%. Pricing per square foot, per unit and per key is at near-record levels.

It is therefore not surprising that the competition for assets in secondary markets and alternative asset classes has heated up. As sellers cash out in gateway markets, some are redeploying capital. Investors seeking higher yields, either through income growth or capital appreciation, will have to follow suit and take a chance on more peripheral locations, buy and improve lower-grade assets or undertake lengthy development or conversion projects.

The US real estate market has an abundance of assets in need of repositioning and developers looking for investors. As they proceed deeper into secondary and tertiary markets, or into alternative assets, they run the risk of digesting too many exotic assets. Knowing which projects will be successful in the long term requires good advice and detailed local knowledge in such a varied and granular landscape.

CORE-PLUS TIP

SELECT SUBURBAN US SUNBELT CLASS A OFFICE BUILDINGS – SHORT TO MEDIUM TERM

Core-plus is increasingly about geography and capturing the upside in secondary and tertiary markets. Buyers seeking a bit more income growth will have to look outside the top markets to 'late recovery markets' in major metro areas and pursue properties in secondary locations.

More investors are following the flow of businesses and residents from costlier north-east and mid-west markets to high-growth/low-cost markets in the south-east, south-west and Mountain West – the 'sunbelt' markets. Migration to the sunbelt has been the norm for several decades but was curbed during the recession. The recovery has seen resurgent flows of people and businesses eager to capitalise on the lower costs of living and doing business.

Tech firms in particular have participated in this shift. Although initially focused on major cities such as New York, Chicago and Boston, they have discovered that sunbelt metros have a lot of talent. Many sunbelt markets have seen the emergence of particular tech specialities: fintech in Atlanta; defence/software and chipmakers in Phoenix; biotech/biopharm in Raleigh/Durham; and alternative energy in Denver. Investors will need to focus on buildings with proximity to mass transit and residential neighbourhoods. Average cap rates in these markets are 6.8% to 7.9%, which compares to an average of 5.2% across all US CBDs. These markets are likely to register moderate NOI growth.

Understanding the local scene, alongside key drivers, is critical

CORE-PLUS/VALUE-ADD TIP

US A-/B+ OFFICE PRODUCT ON THE EDGE OF PRIME, NEARBY DISCOUNT MARKETS AND B & C BUILDINGS IN SUPPLY STARVED LOCATIONS – SHORT TO MEDIUM TERM

Class A rents have hit levels previously thought unattainable in prime CBDs and some submarkets. As the gap in rent between top-tier buildings and A-/B+ properties widens (often to more than 20%) the prospects for incremental NOI growth in older properties improves. Some cap rate compression for A-/B+ space has occurred, but the prospects for short-term rental rate growth are still strong.

Value-add options even include some of the most iconic properties, such as the Willis Tower in Chicago (formerly the Sears Tower) and the Empire State Building in Manhattan. Inefficient space configurations, older building mechanicals and outdated amenities will require a lot of improvement and restacking of tenants.

VALUE-ADD TIP

US CLASS B/C-STARVED SUBMARKETS

TAMI (technology, advertising, media, and information) companies have taken over some submarkets (Midtown South in Manhattan, Cambridge in Boston, LoDo in Denver and River North in Chicago) and stripped these areas bare of Class B spare. In turn, they have pushed the traditional tenant base in these districts (non-profits, architects, small business) into neighbouring areas such as Penn Plaza/Garment District in Manhattan and the Financial District in Boston. ▸

The displacement of traditional space users has been accelerated by a rush of developers to convert older office buildings and some industrial product to creative office space, luxury condos and hotels. Pricing in TAMI-fuelled submarkets such as Santa Monica, and River North and Midtown South (Manhattan) has spiralled higher, so opportunities to achieve both NOI growth and capital appreciation are in more peripheral sections, such as Downtown Los Angeles, Playa Vista and El Segundo. In Orange County, California and the Peninsula (between Silicon Valley and San Francisco) very limited new construction and growing demand for larger blocks is turning buildings that were considered distressed assets a few quarters ago into 'value-add' gold mines.

CORE-PLUS TIP

US SECONDARY WAREHOUSES AND DISTRIBUTION PRODUCT – SHORT TO MEDIUM TERM

As recently as a year ago the industrial sector, even at the heart of the supply chain, was still undervalued, but it is now a core investment. The fundamentals underlying it are, in many ways, the strongest of all of the asset classes. Multiple demand drivers continue to support steady leasing in warehouse and distribution facilities. These include surging e-commerce sales and the scramble to reduce 'click to delivery' times, strong import activity and household income growth resulting in rebounding housing and auto sales. The sector is the most supply-starved asset class – net absorption in warehouses totalled 141 million sq ft in the first three quarters of the year, but only 130 million sq ft is currently under construction. Low supply prevails, not only in logistics and distribution hubs such as Los Angeles and Miami, but also in secondary and tertiary markets such as Portland, Oregon and Oklahoma City.

Investors have recently increased their focus on 'final mile' logistics and third-party logistics (3PL) facilities within a day of large urban centres in locations such as northern New Jersey, Long Island and southern California. As space in primary markets tightens, further rental growth has spread out to the edge of logistics/distribution hubs. There is increasing willingness to enter secondary markets, while competition for assets has intensified. Cap rates in Orange County, for example, average 4.6% and 5.1% in NYC boroughs, but move out to more than 7% in Salt Lake City and Atlanta.

OTHER CORE-PLUS/ VALUE-ADD TIPS

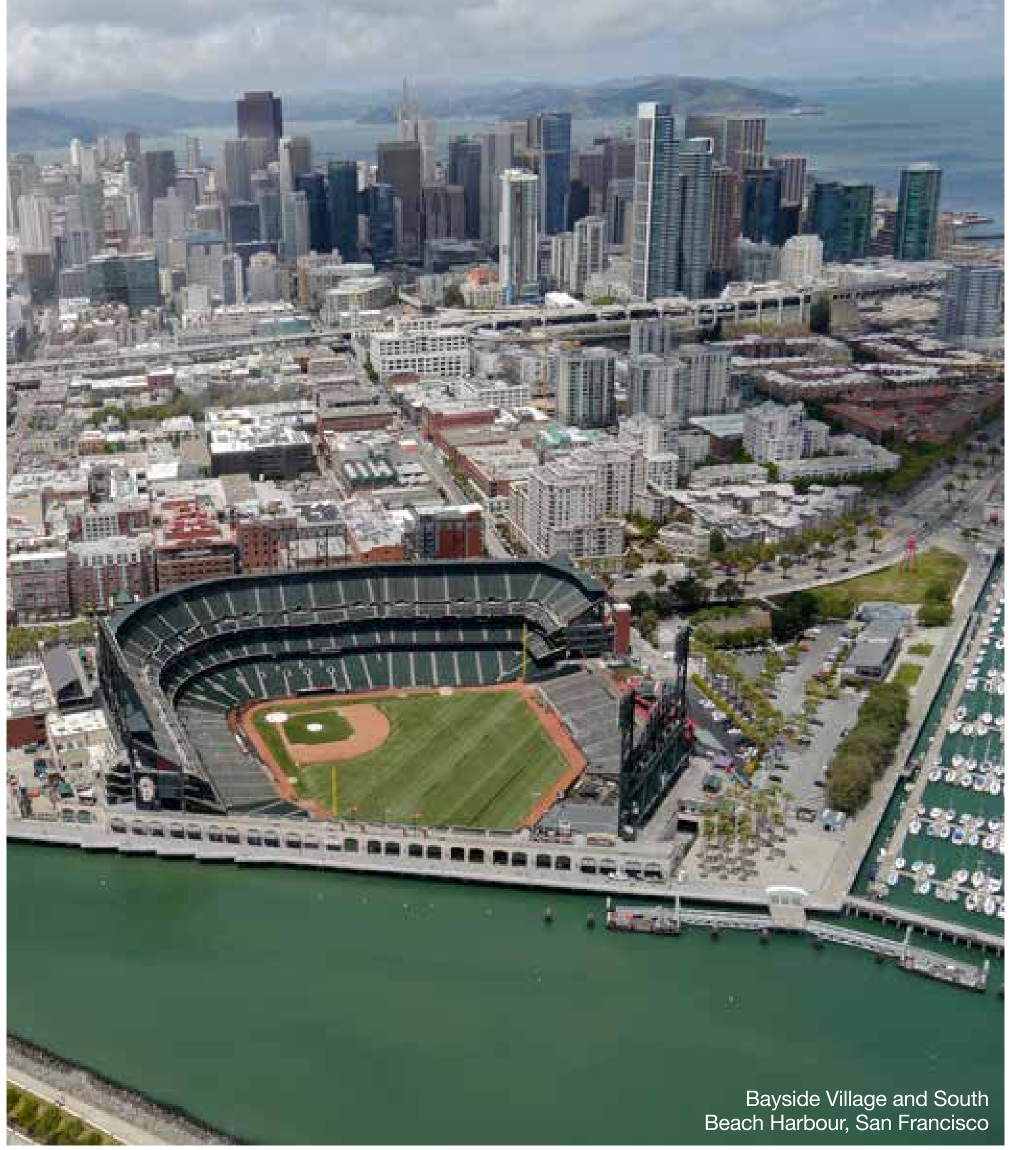
GARDEN APARTMENT PORTFOLIOS IN SUNBELT AND WESTERN MARKETS

The multi-family market was the first asset class to gain momentum when the recovery started and it remains a favourite target of core and core-plus investors, so cap rates have come in to under 5% in Boston, Manhattan and San Francisco, and even Washington DC and Los Angeles. Garden apartment buildings in south-eastern and south-western markets are priced at a fraction of the high and mid-rise product in urban areas.

Most millennials are still priced out of the housing market, so metro areas with a growing number of recent college graduates, such as Phoenix, Austin, Denver, Atlanta and Washington DC, have a steady base of apartment-dwellers. Rental growth has picked up in many of these markets, particularly in proximity to mass transit, retail and other attractions. These cities may also offer value-add options to update older apartment buildings and loft buildings, particularly in the high-demand urban core. Value-add purchase and upgraded, older garden apartment buildings built several cycles ago has the strongest upside potential, although investors need to watch out for competing supply in some markets, where there can be thousands of additional units in the development pipeline.

Cityscape from Reunion Tower, Dallas

US



Bayside Village and South Beach Harbour, San Francisco

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OFFICE AND FLEX BUILDINGS IN SECONDARY AND TERTIARY 'TECH MARKETS'

The quest for tech talent and innovation has led some big employers to secondary and tertiary markets, such as Austin, Nashville, Salt Lake City and Minneapolis. Acquisitions and investments fund extensive hiring initiatives, spurring strong demand for office space. They can also make a big splash in markets that have a limited amount of institutional grade flex and office product.

Secondary and tertiary markets cannot offer all of the attractions of the 24-hour cities/gateway markets, but they generally have enough talent and a cool/authentic vibe that tech and creative sector companies covet. Some are set in university towns or former 'company towns' with a high percentage of educated professionals. This includes tertiary markets such as Huntsville, Alabama, as well as Knoxville, Tennessee and Albuquerque, New Mexico. Even Nashville's music and entertainment sector has fostered entertainment start-ups (as well as being on a growing list of smaller cities like San Luis Obispo, California; Worcester, Massachusetts, and New Haven, Connecticut) that have a burgeoning healthcare start-up scene. Cap rates for workspace in these cities are usually in excess of 7% and can be over 9%.

Affluent tech residents will demand luxury high-end retail in new places

UNDERSERVED/OUTMODED RETAIL IMPROVEMENTS IN GENTRIFYING COMMERCIAL DISTRICTS AND INNER SUBURB/CITY EDGE

Retail product has not always been adequately developed alongside new residential and office development in some older commercial corridors and close-in suburbs. Older 1980-1990s buildings could gain higher rent and foot traffic with building improvements to serve new and growing populations. There is also a gap in luxury high-end retail in 'new tech' markets with increasingly affluent younger residents.

OPPORTUNISTIC TIP

PLACE-MAKING

Part of the appeal of many cities is their unique and authentic culture, but as investors from China, Canada and Europe increase their stakes in major US developments, it may seem to validate the notion that 'the world is flat'. However, an increasing number of people and businesses in the US are pushing against homogenisation, or the 'cookie-cutter/chain-store' settings often associated with suburban subdivisions and strip malls. The overwhelming mantra or catch-phrase among suburban planners and developers is creating 'live/work/play settings with a sense of place'. The authenticity much prized by the millennial tech generation may be tough to build but it pays dividends. Replicating the 'cool and edgy' vibe of SoMa, the Meatpacking District in Manhattan or Downtown Austin and Nashville, may be impossible in suburban locations but urban amenities or the creation of a town centre, even in suburban markets, offer businesses and residents a lot of convenience, not to mention higher property values.

It doesn't take a development the size of Hudson Yards in Manhattan to spur value-add and opportunistic buys. Renovations to industrial business parks or corporate campuses can enhance the value of properties surrounding these facilities. ■

GLOBAL REAL ESTATE TIPS

Rural

Farming offers up many routes for investment, whether it be in the US's Corn Belt, emerging markets in central Europe, or Africa for those who are willing to roll the dice

TIPSTER: IAN BAILEY, HEAD OF RURAL RESEARCH

World farmland markets are attracting significant investment activity. Demand for land is underpinned by growing global food and energy needs.

CORE-PLUS TIP
US CORN BELT – LONG TERM

The Corn Belt is ideal for the private or smaller scale investor. It offers scale and the ability to aggregate land investments to create large farming units focusing on corn and soybean production. Illinois, Indiana and Ohio are the states which present the best opportunities. The Corn Belt benefits from the class A soils and relatively little of the climatic volatility that is typical of the US midwest.

The best opportunities lie in identifying under-performing farms. Long-term gains in asset performance can be achieved by increasing crop yields, using technology such as hybrid seeds and highly mechanised production. This productivity gain is, over time, capitalised into the land value, despite short- to medium-term commodity price volatility.

VALUE-ADD TIP
UK RURAL ESTATES – LONG TERM

A diversity of assets (agricultural, residential, commercial and, more recently, renewable energy) helps to spread risk and high-quality rural estates with a range of assets within one property fit this bill. The Savills Estate Benchmarking Survey, which has surveyed rural estates across the UK since 1996, shows they have delivered a steady upward performance in both gross and net incomes, which has reduced exposure to commodity price volatility.

UK properties are an attractive proposition to high net worth individuals as they are safe shelters for wealth and a tax-efficient way of transferring wealth from one generation to the next. They also offer a range of ownership benefits, from residential to sporting, and the long-term investment performance of rural estates is comparable to most alternative assets, with an annualised total return of 10% over the past 30 years. The economic outlook for rural estates remains positive, despite weaker short-term agricultural prospects.

OPPORTUNISTIC TIP
CENTRAL EUROPEAN FARMS – LONG TERM

Achieving top performance in a farming operation and adding value along the supply chain is key to maximising investment returns. This is especially so in the emerging markets, including central Europe, where farming businesses have been inefficient (small and fragmented) and under-resourced (capital and skills). However, many of these regions have significant resources in terms of land, water and labour. Agriculture in the EU also benefits from subsidies. If farming operations can achieve the scale and adequate resources to perform in the top quartile, then this increase in performance will translate into stronger capital values.

Farmland values in the emerging markets have, historically, shown the strongest capital growth. Although the current fall in commodity prices will lead to some pressure on average farmland values in the short term, we believe that the right product in the right place can offer real opportunities for top long-term investment performance, underpinned by the fundamentals of food and energy security.

OPPORTUNISTIC TIP
AGRICULTURAL INVESTMENT IN SELECTED AFRICAN COUNTRIES – LONG TERM

Africa continues to grow in economic significance and is playing an increasingly important role in the global economy. Agriculture and, more specifically, land, are Africa's greatest assets.

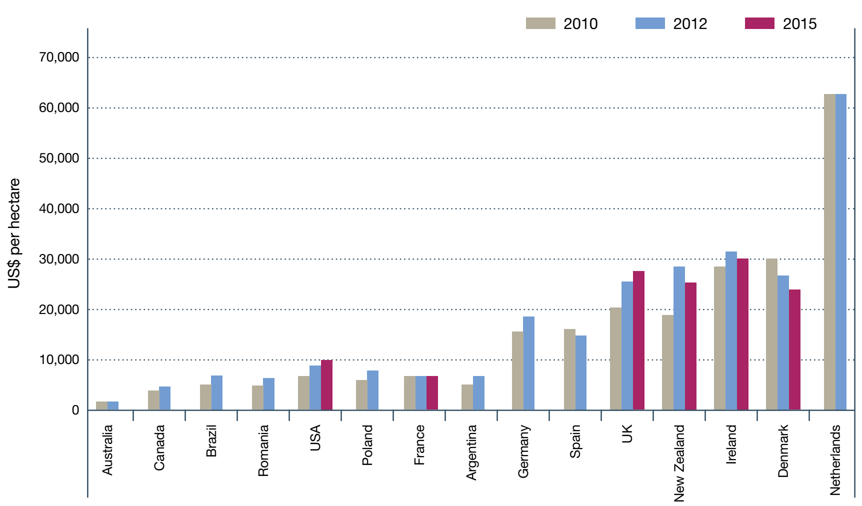
Africa is often seen as a homogenous region. However, there are significant 'growth corridors' developing in southern and eastern Africa that not only unlock the potential for export for investors but also significantly strengthen local and regional markets.

The land tenure system and regulations vary from country to country, but it is generally based on a long leasehold interest of between 50 and 99 years, often with a renewable clause written in to allow effective ownership in perpetuity.

Africa offers a significant agricultural investment market, but is not for the faint-hearted *(see fig.1)*. As ever, it is vital to be focused and to 'know your market'. The risks can be substantial, but for the well informed there is an opportunity to acquire large productive farms that are likely to significantly increase in capital value over time.

Performance will depend on the enterprise and location, and the level of capital required to develop the farm to full operational capacity. External infrastructure and access to markets are key to maximising financial returns so this may be an investment that is best made alongside infrastructure investments or improvements. ■

Global land values



Source: Savills Research using Eurostat & various data/estimates

An aerial view of farmland in Indiana, US

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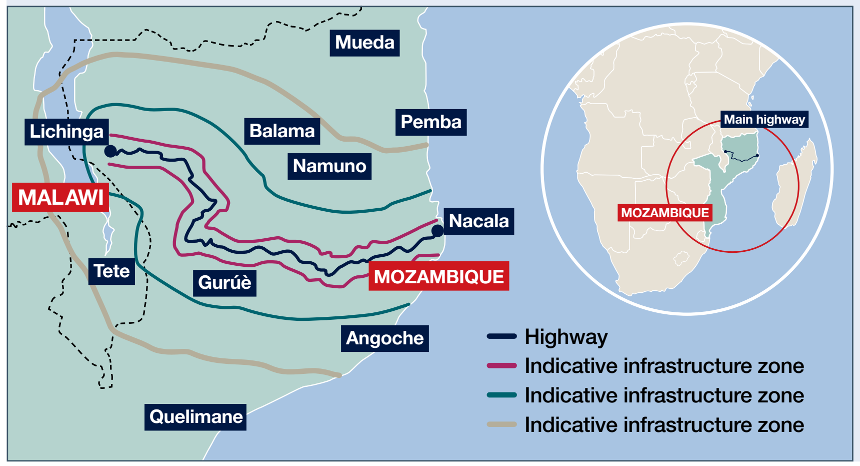
FIG. 1 **Infrastructure in Africa**

There are potentially lucrative investment opportunities in Africa's agricultural sector, but these also carry a high level of risk. A combination of real estate and infrastructure investments may yield the best returns.



MOZAMBIQUE

- Transport can account for as much as 30% of crop output
- Transport approx: 20 cents per km per tonne along main highway
- 60% of roads are unpaved and are only accessible in dry season
- Transport times are excessive and unreliable
- Costs and accessibility increase either side of road and depend on distance from main road and local conditions

COSTS CAN BE MITIGATED BY:

- Linking road and rail investment
- Acquiring land in accessible locations
- Increasing output/reducing costs (especially if agronomic factors outweigh transport costs).

Sources: Savills Research and publicly available data

World

Those who are unafraid of taking a punt on a risky, long-term investment should look no further than Africa, but we also identify further opportunities in the UAE, Vietnam and Cuba

TIPSTER: YOLANDE BARNES, HEAD OF WORLD RESEARCH

San Francisco Bay and Transamerica Pyramid

Our researchers operate alongside experienced practitioners in established and functioning markets, but the world is a bigger place than these key centres alone and the real fun comes in predicting which markets our next generation of researchers will be sitting in 20 years from now. Looking at a broader time horizon, some of the biggest changes and developments in the world of real estate are likely to happen either outside or on the edge of their current geographies. Some of the most exciting opportunities for investors will be in places many of us have not yet heard of.

Indulging a taste for the exotic, and even extreme, my three tips are opportunistic – for those willing to take a long-term position they are high on the risk curve.

OPPORTUNISTIC TIP
URBAN LAND AND EDGE CITY LAND IN GROWING (BUT AS YET OBSCURE) AFRICAN CITIES – LONG TERM

Africa is huge, but while many eyes are focused on the megacities of Lagos and Nairobi, the continent's huge potential for economic growth will likely play out in cities most people in the northern economies have never heard. Oxford Economics forecasts that 7 of the 10 fastest-growing cities in the world to 2030 will be in Africa (three are in Tanzania, two in Malawi). Cities where real estate opportunities are likely to arise are in fast-growth areas such as Kigali in Rwanda, Dar Es Salaam in Tanzania and Addis Ababa in Ethiopia, while countries experiencing a peace premium and prosperity will also be favoured (*see fig. 1*).

However, a word of caution: opportunities may not be conventional. Institutional, Western-style holdings such as big-box, plate glass offices do not always perform well in challenged, emerging and hot countries with unreliable power supplies). The purchase of land for expansion or redevelopment, as well as small retails, workshops and logistics with the potential for appropriate development and redevelopment, could play out better. Participation in the purchase of land rights in slum areas that are ripe for pacification and gentrification by their occupants may also be an area for investigation. Real estate capital will be needed for the development of neighbourhood commercial uses in these areas. Western-style legal systems and transparent property markets will make some locations more attractive for the more risk-averse so conventional asset classes in South Africa will have a place within a value-add strategy.

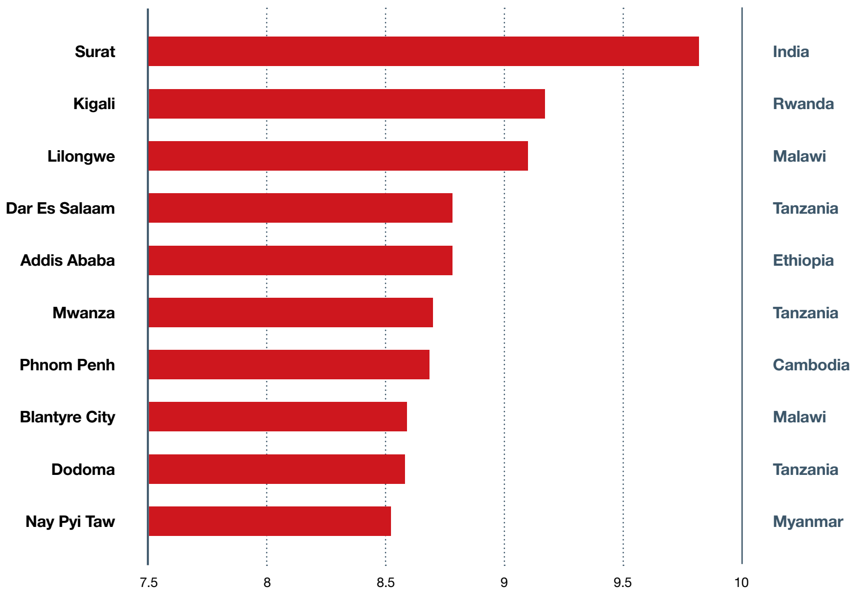
Future growth will occur in cities of which most people in northern economies have never heard

OPPORTUNISTIC TIP
RESIDENTIAL IN DUBAI – MEDIUM TERM

It is difficult to recommend any real estate investment within a region as troubled as the Middle East, especially when a significant number of investors are looking for safe-haven jurisdictions outside the region. But there is potentially a strong role for residential property – for both main residences and second homes – to perform a wealth storage function in the region's safer countries.

Dubai is well-placed to service not only those with wealth in the Middle East, but also its own growing middle class. Falling oil revenues threaten wealth creation in many parts of the Middle East, although Dubai has never been oil-reliant and started to diversify its economy many years ago, putting it in a better position to ride out the storm. It is likely to continue to attract businesses that want to trade with the West and its economy is forecast to grow strongly. The hybrid nature of the city as both a business and tourist destination means it has the potential to attract both residents and leisure/lifestyle second-home owners. These are more likely to come from within the region in the coming years, although we are cautiously optimistic for high quality, low and mid-rise sustainable housing and resort developments.

FIG. 1 Growth in GDP (% year on year)



Source: Oxford Economics

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OPPORTUNISTIC TIP
RESORT AND LEISURE DEVELOPMENTS IN HITHERTO INACCESSIBLE LOCATIONS – MEDIUM AND LONG TERM

The potential growth in demand for leisure properties in Asia is a major force that cannot be ignored. A growing middle class and an ageing, wealthy population will not spend all of its time in newly urbanised cities. Local tourists are already a growing force in Thailand and Vietnam, and we anticipate that this is a market poised for massive expansion.

Dubai has never been a significant oil producer, putting it in a better position to ride out the storm

The development of Hainan Island by China illustrates the potential for Chinese tourism in the South China Sea and beyond. Some of it may look quite different to Western tourism; at present, it focuses less on sun, sea and sand and more on social activities in urbanised centres, but it is still evolving and participants will need to keep abreast of fast-developing trends.

Vietnam is a good example of how changes in land ownership and development rights can open up areas for tourism very quickly. Burma is another country in the region where recent political developments could also lead to this sort of change, although any country with the natural resource of a long and beautiful coastline is in the running to capture this growing market.

Outside Asia, other countries may be faced with a changing political climate, and changing land rights. Cuba is an obvious example of an opportunity on the doorstep of North America, with a huge potential to capture that mature market – particularly if it can develop in a unique and distinctive Cuban way that makes the most of its culture, heritage and built environment, without destroying it in the development process.

The destruction of natural and cultural assets anywhere is perhaps the biggest potential pitfall of any resort and leisure development as it threatens the long-term attractiveness of the location, as many old Western resorts have discovered. It is something that investors will need to guard against if they are concerned about the long-term performance of their investment. ■

Summary

Same but different – global economic forces mean that tips for the future have taken on a degree of uniformity worldwide, while the digital age is changing the face of the workplace

YOLANDE BARNES, HEAD OF WORLD RESEARCH

It is striking just how similar some of our tips across the world are, despite the fact that they have originated in different markets and among different researchers operating in completely different geographies. This clearly shows that there are global forces at work that act as a heavy hand on the tiller of local markets.

Foremost among these global forces is simply the nature of money. The impact of looser monetary policy almost everywhere, low inflation, low interest rates and quantitative easing cannot be overstated. Every global region seems to be reporting asset price inflation, particularly in the core prime markets.

Added to this is the creation of wealth in an increasing number of emerging economies, as well as ageing populations that have more invested equity in the developed world. All this means that there is more capital at large, seeking both capital appreciation and, increasingly, income.

The other theme to emerge from our researcher's prognoses is the dawning of the digital age and the impact it is having on the built environment. The importance of logistics to service the needs of e-commerce has been identified in every region. Meanwhile, the more subtle effects of a changing workforce are beginning to be identified in some key cities, in North America especially.

If the first industrial age was about proximity to raw materials, the manufacturing age about proximity to markets and the service age about proximity to capital, the digital age is different again. Entrepreneurial tech industries are all about proximity to talent so successful locations are those that are capable of attracting this human capital.

New corporations and enterprises can no longer attract their workforce to homogenous out-of-town buildings where there is no other human interaction or activity. Their city has therefore become a commercial entity for them, a unit of currency in the digital age that will either attract or repel their human capital.

All this supports the three pillars of real estate investment for the next decade, which regular readers of our other publications will have seen rehearsed before. They are:

1. **THE RISE OF SECONDARY AND TERTIARY MARKETS**
2. **THE RISE OF SECOND-TIER CITIES**
3. **THE RISE OF ALTERNATIVE ASSET CLASSES AND LOCATIONS**

This will make for an interesting, varied and increasingly global real estate investment market in the coming decade. Our global researchers will enjoy exploring and explaining this new landscape in 2016 and we would like to wish all our readers a happy, successful and prosperous year. ■

Dublin's Temple Bar area

ALAMY

Savills global presence

30,000 EMPLOYEES ACROSS A NETWORK OF OVER 700 OFFICES IN MORE THAN 60 COUNTRIES

UK, IRELAND & CHANNEL ISLANDS
ENGLAND
GUERNSEY
IRELAND
JERSEY
NORTHERN IRELAND
SCOTLAND
WALES

ASIA PACIFIC
AUSTRALIA
CAMBODIA
CHINA
HONG KONG
INDIA
INDONESIA
JAPAN
MACAU
MALAYSIA
MYANMAR
NEW ZEALAND
PHILIPPINES
SINGAPORE
SOUTH KOREA
TAIWAN
THAILAND
VIETNAM

CONTINENTAL EUROPE
AUSTRIA
BELGIUM
CROATIA
DENMARK
FINLAND
FRANCE
GERMANY
GIBRALTAR
GREECE
ITALY
LUXEMBOURG
MONACO
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NETHERLANDS
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PORTUGAL
RUSSIA
SERBIA
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BAHRAIN
BOTSWANA
KENYA
MAURITIUS
MOZAMBIQUE
NAMIBIA
OMAN
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CANADA
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GRENADA
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ST LUCIA
US

SAVILLS WORLD RESEARCH TEAM

Yolande Barnes
Director
+44 (0) 20 7409 8899
ybarnes@savills.com

Paul Tostevin
Associate Director
+44 (0) 20 7016 3883
ptostevin@savills.com

Vladimir Tikhnenko
Research Analyst
+44 (0) 20 7299 3043
vtikhnenko@savills.com

For more information, please visit: www.savills.com

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