THE NETHERLANDS

CAPITAL MARKETS OUTLOOK 2015

CBRE

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CAPITAL MARKETS OUTLOOK 2015

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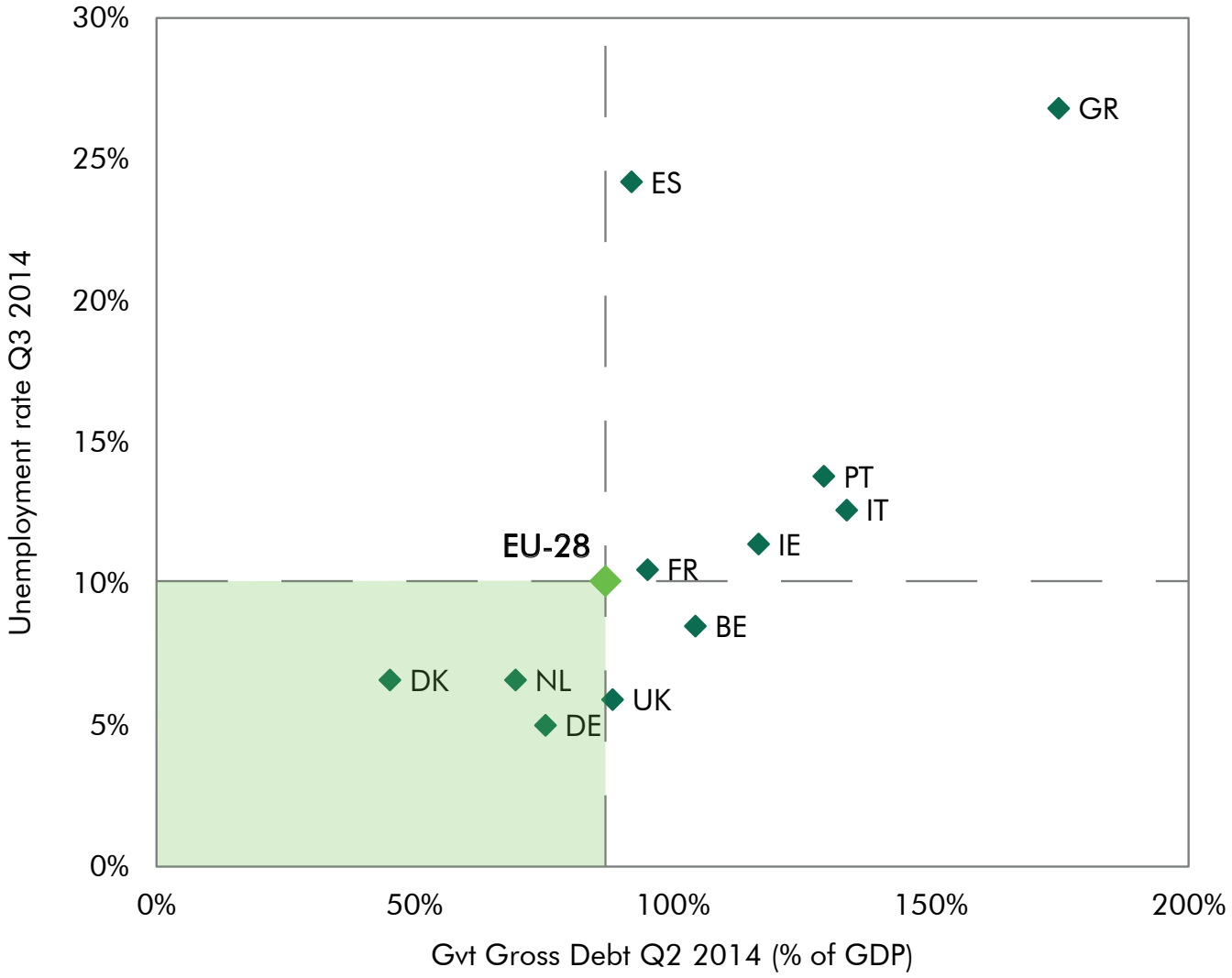
INTRODUCTION
CAPITAL MARKETS OUTLOOK 2015

In this publication CBRE reflects on the rising opportunities for real estate investments in an increasingly dynamic capital markets environment. In the special report "Making A Difference", released early 2013, we addressed the internal differentiation between the performance of submarkets in the Netherlands and the consequences for making sound investment decisions. Strong diversification attracted investor interest for multi-functional and multi-modally accessible locations. This report draws on these previous findings, supplemented by new insights and recent market evidence.

In addition to regional differentiation, competitive pricing has led to a second major trend at the macro level. Secondary assets have become increasingly affordable, which has pushed investors towards value-add opportunities and recovery strategies. Landlords can afford to add value through renovations and to attract tenants by lowering rents. With this report, CBRE provides insight in these and other changing market mechanisms, with an emphasis on post-crisis investor demand.

THE NETHERLANDS IN EUROPEAN CONTEXT



Source: Eurostat (2014); Oxford Economics (2014)

THE NETHERLANDS
ECONOMY

COMPETITIVE ECONOMY
The Netherlands ranks 2nd in the 2014 World Bank Logistics Performance Index and 8th in the World Competitive Index 2014-2015, emphasising its global attractiveness and gateway function for the European continent. The country has a prosperous and open economy with a focus on foreign trade. The services sector is the most important sector and roughly represents 70% of the economy. With labour participation in the Netherlands already high compared to other European countries, unemployment rates fell in Q3 2014 for the second consecutive quarter (ILO definition). Moreover, government debt is relatively low and purchasing power standards are substantial with respect to other EU member states.

STRONG FUNDAMENTALS FOR GROWTH
The combination of high labour participation and moderate debt makes the economy resilient to external shocks and provides strong fundamentals for economic growth. The Dutch budget for 2015 reveals easing of austerity, reflecting anticipated recovery. Currently, economic upturn is largely driven by export growth which benefits from world trade picking up. Also, recovery of the housing market – with Amsterdam and Utrecht as the most notable examples – is likely to lift consumer sentiment and might result in private consumption growth on the medium run.

CHANGING OCCUPIER PREFERENCES
Flexible and innovative workplace strategies – often referred to as "New Ways of Working" – ideally result in an environment where living, leisure and everyday work come together. Preferred locations are easily accessible both by private and public transport, with a functional mix of business services, retail supply and a high level of amenities. As such, different property market segments become increasingly intertwined and they all face a similar concentration trend towards urban centres.

RESILIENT AND FLEXIBLE ECONOMY
COHERENT PROPERTY MARKETS
STRONG FUNDAMENTALS
GLOBAL ATTRACTIVENESS

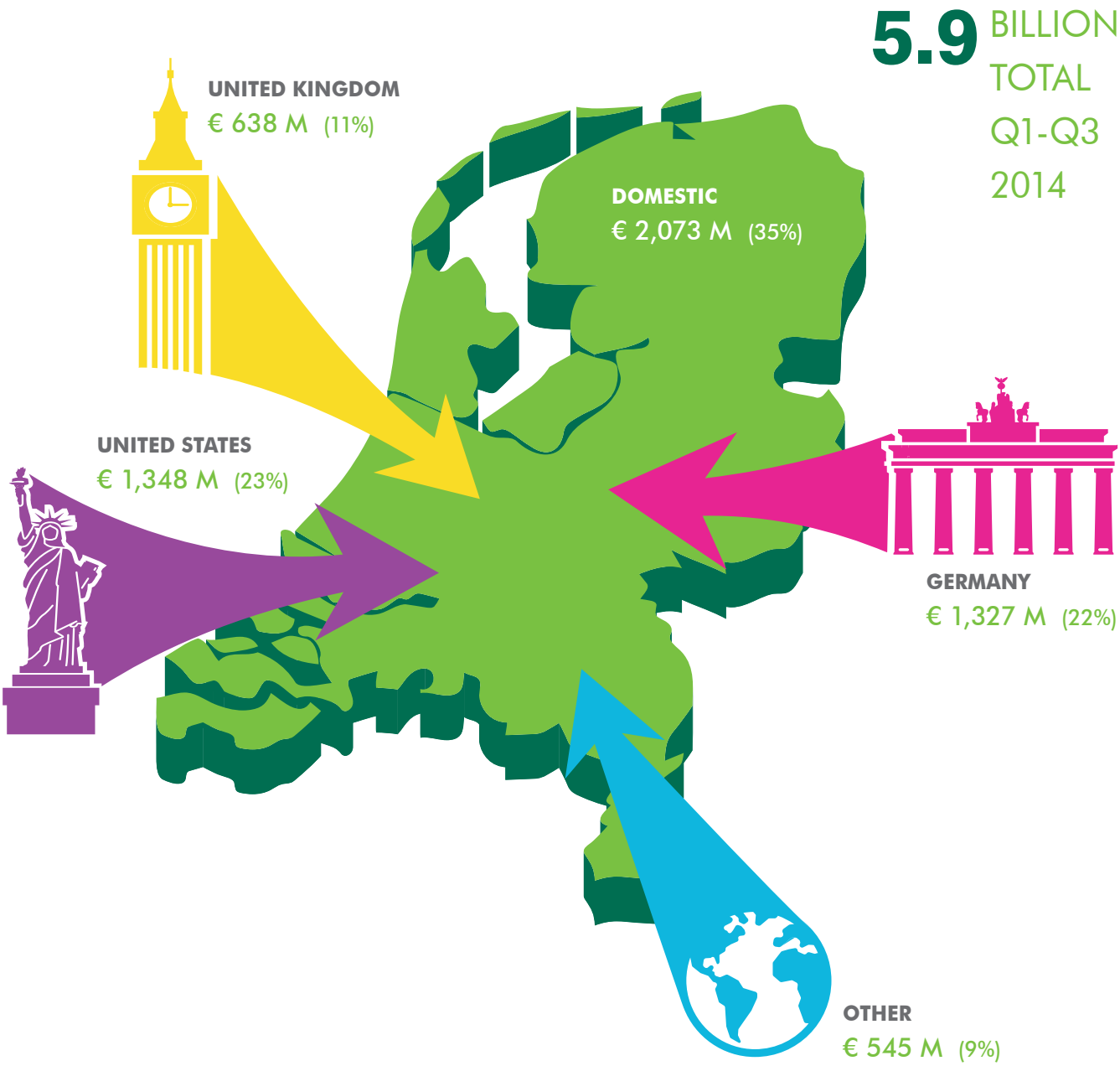


Figure 2 Capital flows in The Netherlands

CAPITAL FLOWS
INTERNATIONAL ACTIVITY

RISING INTERNATIONAL ACTIVITY

The Dutch investment market recently experienced unprecedented demand by foreign investors with cross-boarder investments comprising almost two thirds of the total investment volume. While the domestic market was generally responsible for at least 50% of total investment turnover in pre-crisis years, the share of foreign investments has strongly increased after the trough in 2009.

An important driver for the current influx of foreign investments are strategies anticipating on property values bottoming out, fuelled by economic recovery. Particularly overseas private equity parties have proved to be highly responsive to changing market dynamics and low asset prices. These low prices allow them to add value to the property or adjust rent levels according to post-crisis occupier demand. Either way, investors actively attract new tenants, thereby improving the overall market dynamics in these areas.

EMERGENCE OF EASTERN CAPITAL

To date, Asian institutional investors are still relatively under-allocated in real estate compared to their US and European counterparts. In the medium run however, diversification strategies of Asian funds are likely to increase their allocation to real estate. Additionally, they are experiencing a growing influx of pension and insurance capital, which will impact the property markets regardless of the relative allocation. As a result of this capital pressure, Asian investors are increasingly widening their scope towards the European continent, where risk-adjusted returns are perceived to be more attractive than in emerging market regions.

Illustrative for this trend is the increasing number of Asian investors exploring the Dutch market. This has already resulted in the first indirect investments, including equity raised by institutional funds and the establishment of seperate accounts. In both cases a party with local market knowledge is generally responsible for managing the final direct transaction. In 2015, however, the Netherlands is also expected to witness its first direct investments by Asian investors.

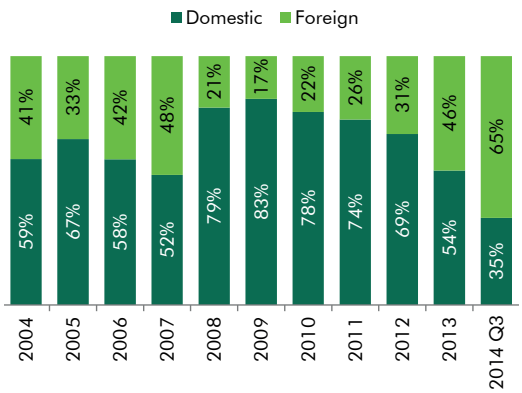


Figure 3 Unprecedented share of foreign investments

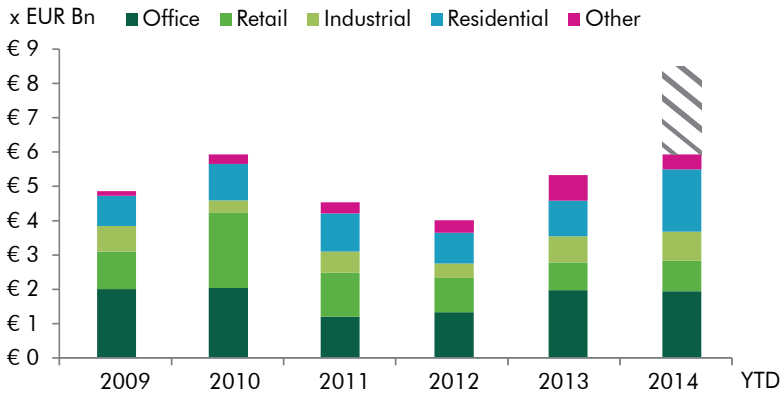


Figure 4 Investment turnover per sector

Source: Amsteltower, Provast Projectontwikkeling, 2014

DEBT MARKET
THE RETURN OF FOREIGN LENDERS

DIFFERENTIATED CREDIT SUPPLY

While financing is already widely available for the prime product in the Netherlands, it is now shifting to other market segments. Lenders who became locally oriented during the crisis are reopening their eyes towards cross-border opportunities. With tightening margins in the most liquid core markets, international suppliers of capital are shifting their focus to the Netherlands, resulting in the entry of new lender types such as debt funds and insurance companies. A major recent example of foreign debt entering the Netherlands is the Vestia residential portfolio acquired by Patrizia and set to be financed by Deutsche Hypo.

EASING MARKET CONDITIONS

The increasingly differentiated credit supply provides relief on a previously rather tight debt market. Lenders are currently also offering customised (co-) financing solutions, in which each component of the loan – with its own particular risk/return profile – is allocated to the appropriate lender. Although liquidity for small transactions (< EUR 15 M) is more limited, several parties are gradually making the shift towards this segment in a high-yielding stretched senior capacity.

COMMERCIAL MORTGAGE-BACKED SECURITIES

CMBS is starting re-appear with for example the Deco Tulip CMBS, recently put on the market by Deutsche Bank for EUR 250 million. It concerns a combination of two senior loans partially backed by office and retail assets in the Netherlands. Increasing CMBS activity reflects a shift in sentiment among lenders towards the appreciation of loans as a financial product.

"CUSTOMISED FINANCING SOLUTIONS"

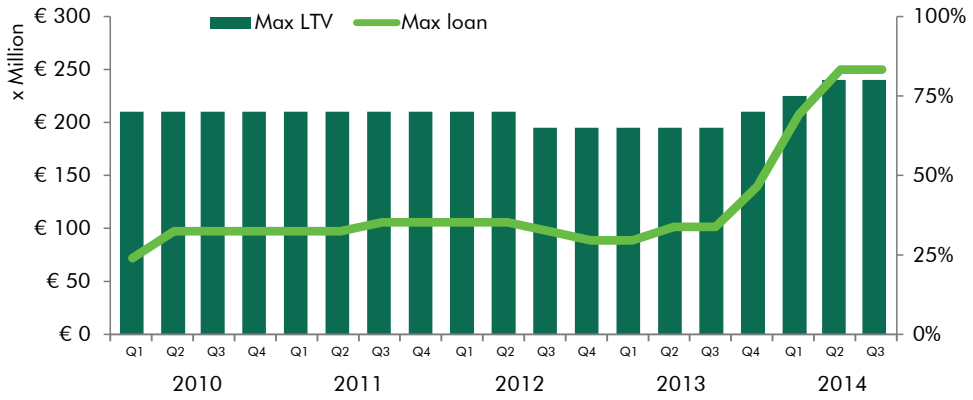


Figure 5 Indicative financing conditions in the Netherlands

CAPITAL MARKETS

THE PERFORMANCE OF REAL ESTATE

RELATIVE VALUE OF REAL ESTATE

Supplemented by low interest rates, the "new normal" of moderate economic growth has paved the road for CRE investments. With stock markets highly responsive to external shocks, CRE has proved to be an attractive low-risk opportunity for investors. Also compared to traditional low-risk assets such as government bonds, CRE provides a more favourable risk/return profile.

YIELD COMPRESSION

In line with property markets across Europe, the Netherlands is facing a renewed yield compression. Capital values are carefully rising, and, instigated by accelerating investor activity and anticipated economic upturn, appetite for secondary assets is emerging. The appetite for favourably priced peripheral properties has put secondary yields under downward pressure. As of Q1 2014, the historically large gap between prime and secondary yields has narrowed for the first time in almost three years.

"COMPETITIVE PRICING **AND FAVOURABLE** GROWTH POTENTIAL"

FAVOURABLE PRICING

Assets in the Netherlands are still favourably priced compared to other core countries in Europe. Prime yields in Paris and London for example, are exceptionally tight with levels below 4%. Although German markets seemingly provide slightly more favourable returns, current yields in prime locations have already dropped below pre-crisis levels. Prime yields in Amsterdam on the other hand currently still supersede the former cycle low, which might indicate assets are still relatively undervalued. Compared to other core countries with strong economic fundamentals, yields in the Netherlands remain favourable with prime yields moving around 5.4% (NIY) – up to 90 BPs above prime German markets and 165 BPs above prime UK markets.

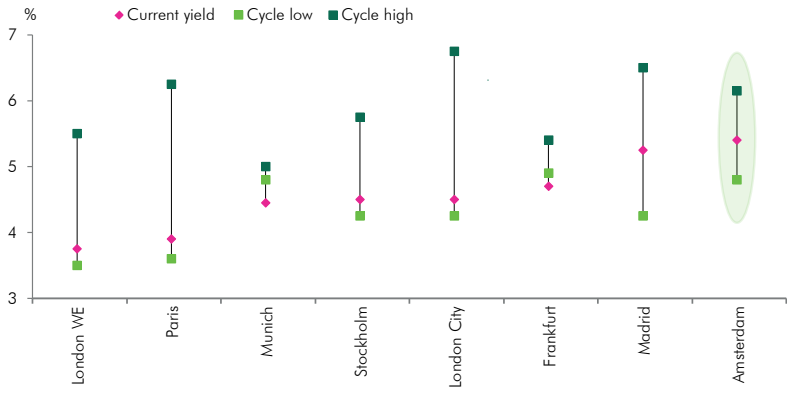


Figure 6 International prime yield comparison over a 10-year cycle

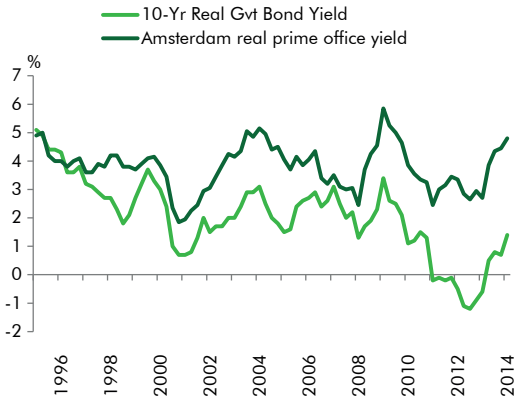


Figure 7 Yield benchmark

OUTLOOK
PROSPECTS FOR THE NETHERLANDS

INCREASE OF EQUITY AND DEBT

As Europe is becoming familiar ground to Asian investors, new capital flows into the Netherlands are imminent. The stabilising economy provides fundamentals for investment opportunities and competitive pricing of secondary assets in particular is attracting strong investor interest. Against these favourable prices, investors can afford to add value to this type of asset and fully employ their upside potential.

In addition, greater competition in the lending market is expected to result in a continuing easing of lending terms. Rather than competing at lower margins for prime assets, lenders are looking to other market segments. In line with the shift in investor focus towards more peripheral locations, borrowing against assets in second and third tier locations is also becoming easier with more attractive lending terms. The inflow of capital, both in terms of debt and equity, is likely to drive further investment growth.

Acquisitions by Blackstone, Lone Star and M7 have illustrated the demand for portfolios among new funds as they provide an opportunity to quickly establish a mature investment platform. With the strong appetite for secondary locations, portfolios still provide sufficient volume for investment targets to be met.

RENEWED OPPORTUNITIES

A major example of an emerging asset class is the Dutch multifamily residential market. For years, this commercial market segment had been squeezed between directly subsidised home ownership and a strong indirectly subsidised social housing sector. Triggered by austerity measures, the playing field of multifamily residential has now opened up to international investors.

Economic forecasts point out that private consumption will improve over the coming years, which is likely to have a positive impact on the retail market and the demand for retail space. Although retail recovery has been trailing other market segments, more clarity about the performance of retail in different locations is expected to fuel investor demand. With private consumption bottoming out, the trend to look for is renewed opportunities for retail investments.

It must be noted that current occupier demand has concentrated in multi-functional, well-accessible urban centers. Favourable locations feature a mix of business services, retail supply and a high level of amenities. Despite the opportunities favourably priced secondary assets provide, these underlying market dynamics should not be overlooked.

NEW CAPITAL FLOWS
EASING OF LENDING TERMS
PRIME-SECONDARY SHIFT
YIELD COMPRESSION
RENEWED OPPORTUNITIES

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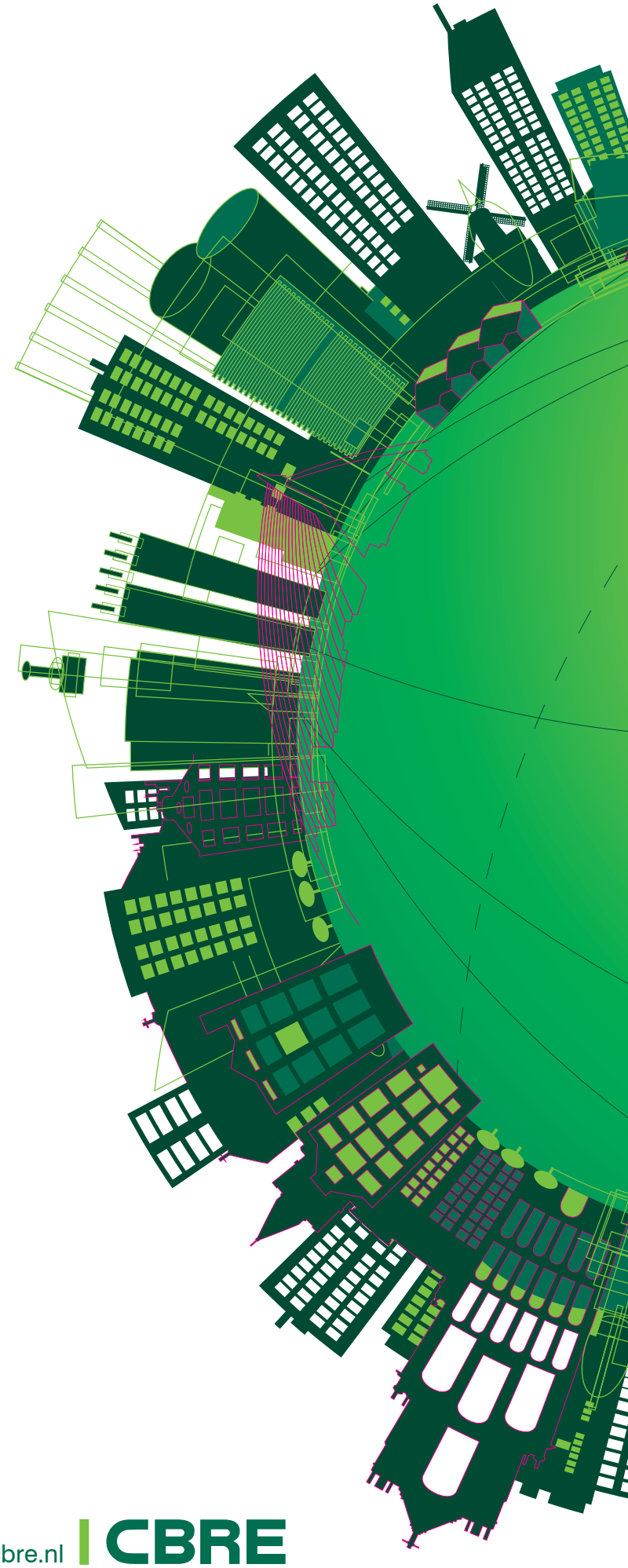

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