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REAL ESTATE CONVICTIONS

Asset Manager's View of the European Real Estate Markets

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ECONOMIC AND REAL ESTATE ENVIRONMENT

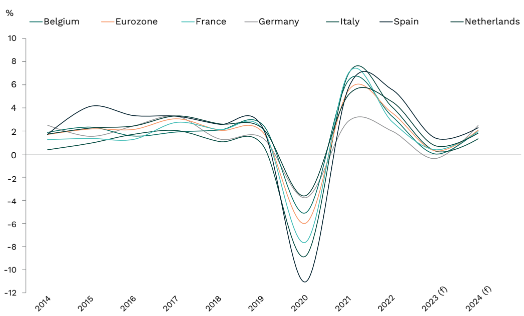
2022 saw a more pronounced than expected global slowdown, due to Russia's invasion of Ukraine, rising inflation, a tightening of financial conditions and the persistence of the Covid-19 pandemic in China. Although the clouds have continued to build up over economic prospects in the early months of 2023, rays of light could start to appear in the second half of this year, with the possibility of a recovery in 2024 now taking shape. Forecasts for global growth currently stand at 2.7% in 2023 and 3.2% in 2024.

In the eurozone, the energy crisis will continue to dominate the macroeconomic outlook. After the expected period of turbulence at the beginning of the year, a gradual recovery should slowly start to take shape as the energy crisis eases (economic growth of 0.0% in 2023). Controlled inflation will then be possible, provided that gas supplies are secured before next winter. A recovery is expected in 2024 (+1.8%). Looking at the main economies individually, GDP growth in Spain is expected to be +1.1% in 2023 and then +2.0% in 2024, followed by the Netherlands (0.5% then +1.5%), France (+0.1% and +1.6%), Italy (-0.1% and +1.0%), Belgium (-0.3% and +1.8%), and Germany (-0.7% and +2.2%).

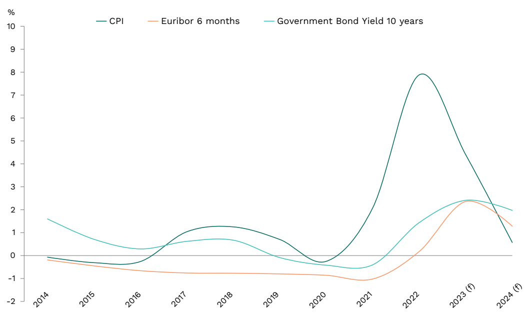
The spike in eurozone inflation in 2022 was a direct consequence of the war in Ukraine and the restarting of economies after the end of the Covid-19 pandemic. Although an optimistic path with inflation brought under control is possible, caution remains necessary. At the end of December 2022, the ECB increased its policy rates by an additional 50bp in order to limit the sharp rise in inflation (+8.4% year-on-year). Current forecasts suggest that inflation will remain high in 2023 (+4.9%), but that it will fall relative to 2022. As a result, the mandate of consumer price inflation of close to 2% is likely to see the ECB make further increases in its rates, starting in the early months of 2023, but these will be more moderate than those seen in 2022.

The increase in the policy rates in 2022 resulted in a significant increase in the cost of money via lending rates. By increasing the cost of borrowing for households and businesses alike, this led to a reduction in demand for credit, putting the brakes on economic activity and beginning to limit the inflationary spiral at the end of 2022.

ECONOMIC ENVIRONMENT: EUROPEAN GDP



GOVERNMENT 10-YEAR BONDS, EURIBOR AND CONSUMER PRICE INDICES IN THE EUROZONE



Over the course of 2022, the European real estate market saw more than €270 billion of investment[1], a 23% drop in volumes compared to 2021. After a very good start to the year, the market stood still in the second half.

2022 was hit by uncertainty in geopolitical conditions. Fresh questions over the economic outlook and increases in policy rates limited transaction volumes to €110 billion in the second half, a 50% drop over one year. Investors chose to take their time and focus on the acquisition of assets that conformed to their risk/return strategies. However, a new break in trend is starting to emerge. Investors holding cash will be the winners in 2023 as they will be able to seize market opportunities as they arise.

Looking at the major countries, investment volumes were €68 billion in the UK (down 12% over the year), €45 billion in Germany (-56%), €37 billion in France (+9%), €15 billion in Spain (+33%), €16 billion in the Netherlands (-20%) and €11 billion in Italy (+5%).

Offices were the dominant asset class, with €96 billion, followed by residential (€59 billion), logistics (€56 billion), retail (€38 billion), hotels (€14 billion) and healthcare (€7 billion).

[1]The real estate market covers offices, retail, logistics, services and residential assets for institutional investors.

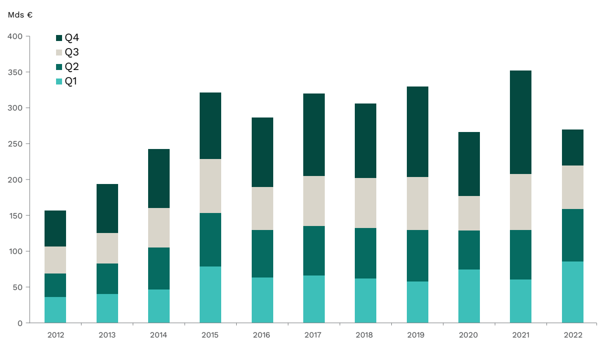
The increase in the cost of borrowing has consequences for growth in capital gains, but rental yields remain stable. For the time being, total returns (rental yield + capital gains) remain in the green for healthcare, whilst hotels and retail are making a good showing.

Although most asset values remained stable over the final months of 2022, there was an observable increase in yields over a one-year period. This can be explained by the tightening of monetary policy, which led to an increase in the risk premium, translating into higher yields being sought by investors.

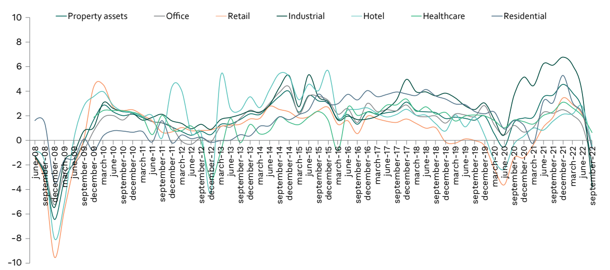
In parallel, total returns were faced, as expected, with fast-rising borrowing costs. Capital valuations were affected, although this did not produce panic selling. The market saw corrections in keeping with conditions. Moreover, as rental yields in Europe are indexed in whole or in part on the Consumer Prices Index, rental performances were strengthened, all other things being equal. The latest available figures suggest that so far healthcare, hotels and retail are the asset classes to have shown the greatest resilience.

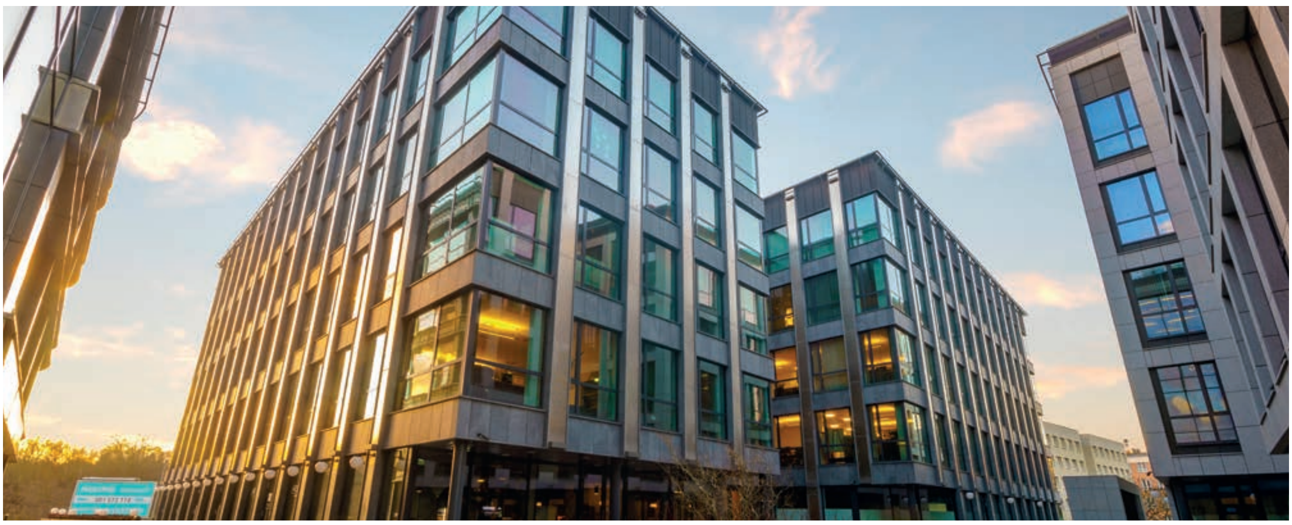
Although investors took a watching brief whilst prices adjusted for certain asset classes and markets in the second half of 2022, the most secure real estate assets, or those with the best prospects, were still sought-after investments.

REAL ESTATE INVESTMENT VOLUMES IN EUROPE



QUARTERLY TOTAL RETURN ON EUROPEAN REAL ESTATE ASSETS





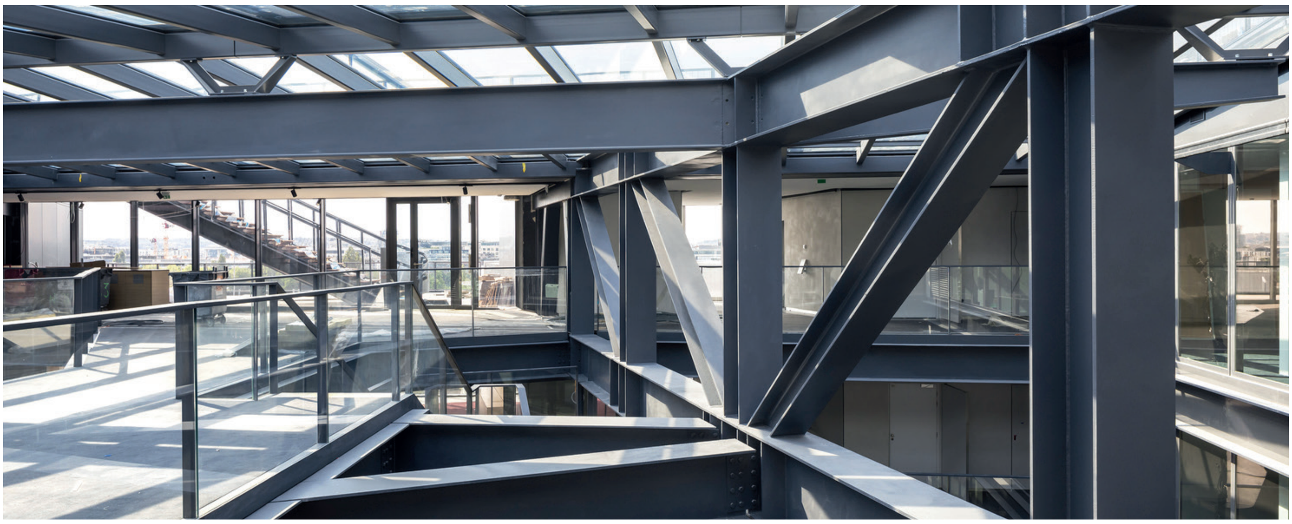
OFFICES

INVESTMENT IN OFFICE REAL ESTATE IN EUROPE – Q4 2022 (12 MONTHS)	**€96bn**
PRIME YIELDS IN EUROPE – Q4 2022 / Q3 2022	↗
SATISFIED DEMAND IN EUROPE – Q4 2022 (12 MONTHS) / Q4 2021 (12 MONTHS)	↗
VACANCY RATES IN EUROPE – Q4 2022 / Q3 2022	→
RENTS IN EUROPE – Q4 2022 / Q3 2022	↗
JOB CREATION – Q4 2022 / Q3 2022	↗

Although offices remained the preferred asset class, the increase in sovereign yields and the uncertain outlook led investors to take a cautious approach in the second half of 2022. The sector is being recomposed, with less attractive markets due to the changes brought about by remote working on one side, and on the other those where there is a risk of the asset base becoming obsolete because buildings have not completed their transition to new energy requirements. Total investment volume in the European office real estate sector was more than €96 billion over 2022 (down 15% over a year). The UK took €21 billion, followed by France where the market grew to over €17 billion, Germany, which saw a marked fall to €16 billion, Belgium with €6 billion, then Italy, Spain and the Netherlands with investment of between €3 billion and €5 billion each.

Over one year, a large majority of European office markets saw a decompression of yields, due to the sharp rise in bond rates[2]. Decompressions of between 50bp and 100bp were seen in office real estate markets between the end of 2021 and the fourth quarter of 2022. A new hierarchy of yields thus emerged. The most prime markets now have a yield of less than 4% in cities such as Paris, London, Munich, Vienna, Stockholm, Copenhagen and Helsinki. Markets with yields of 4% or above included Luxembourg, the Netherlands, Spain, Belgium, Portugal and Ireland.

Dynamic throughout 2022, the European rental market capitalised on new job creation (up 1.3% over a year) and was able to withstand geopolitical uncertainty and the inflationary spiral. Satisfied demand for offices totalled more than 11 million sqm in the first nine months of 2022, a sharp increase in volume compared to 9.8 million sqm let in 2021. Paris, the biggest European market with 2.1 million sqm take-up, put in a strong performance. The districts most attractive to users, in high-quality spaces and with good transport links, were the most sought-after. Paris was followed by London, Berlin and Munich, where new lease volumes were between 700,000 and over 1 million sqm. In the eurozone, cities such as Milan, Madrid, Barcelona and Frankfurt all saw transaction volumes of between 300,000 and 600,000 sqm.



Le Shift ©Boegly_Grazia

The overall trend between the end of 2021 and the final quarter of 2022 was one of falling available supply. However, significant contrasts emerged between various markets. Central districts in cities such as Paris, Berlin, Munich, Vienna and Lyon saw vacancy rates of less than 5% and falling over the course of the year. Less attractive districts, or those with substantial new supply relative to what the market can traditionally absorb, tended to see vacant space increase over the year. Cities such as Barcelona, Madrid and London City still have more than 10% of their total floor space vacant.

The increase in rental values was driven by central and well-connected districts and by the attraction for users of modern, flexible offices that meet ESG criteria. As the vacancy rate fell over the year in popular districts, rental growth was seen in several markets in the fourth quarter of 2022 relative to the end of 2021. The Paris CBD has the highest rents in the eurozone, at around €1,000/sqm, whilst rents in Berlin, Frankfurt, Munich and Milan run at €500 to €660/sqm and those in Brussels, Madrid and Barcelona are around €250 to €450/sqm.

[2]Of nearly a hundred European markets analysed by Primonial REIM Research & Strategy

EUROPEAN OFFICE REAL ESTATE INVESTMENT VOLUMES

Le Shift ©Boegly_Grazia

RETAIL

INVESTMENT IN RETAIL REAL ESTATE IN EUROPE – Q4 2022 (12 MONTHS)	€38bn
PRIME HIGH STREET LEVEL YIELDS IN EUROPE – Q4 2022 /Q3 2022	↗
PRIME YIELDS IN EUROPEAN SHOPPING CENTRES – Q4 2022 /Q3 2022	↗
E-COMMERCE PENETRATION RATES IN THE EUROZONE – 2022	↗
RETAIL SALES IN THE EUROZONE – Q4 2022 / Q3 2022	↗

After a period in early 2022, marked by opportunities being seized, investment started to decelerate in the second half. Total investment volumes in the European retail real estate sector were €38 billion over 2022, with the fall over the year limited to 4%. The UK was the most attractive market with more than €8 billion invested during the year, followed by Germany and France with over €5 billion each, Spain with nearly €4 billion, Italy with just over €2 billion and the Netherlands with slightly less than €2 billion.

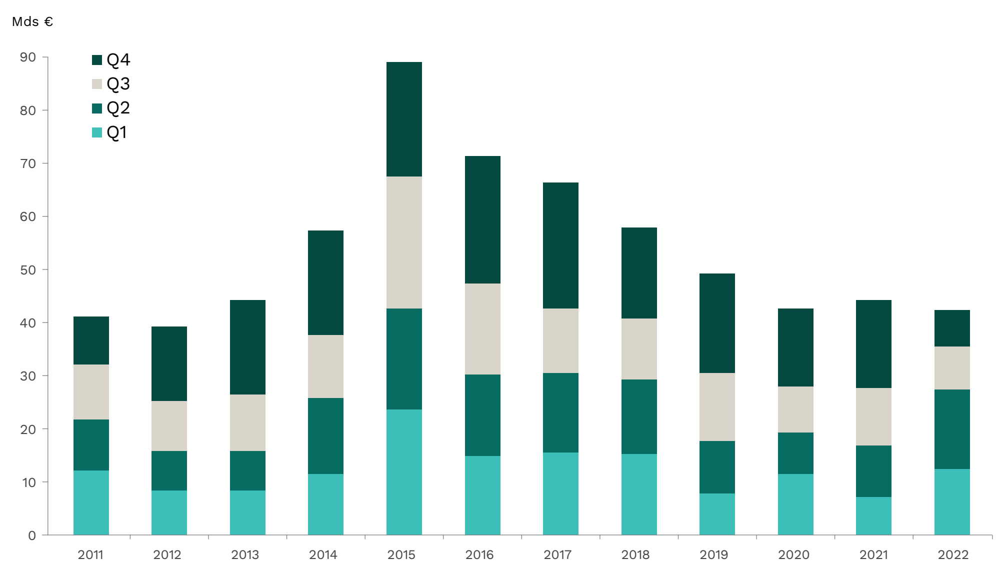
Yields on high street level assets and, to an even greater extent, shopping centres saw decompression in the final quarter of 2022. Yields decompressed by between 10bp and 50bp for hight street and by between 25bp and 75bp for shopping centres between the third and fourth quarters of 2022. Prime yields on high street in Paris, Amsterdam, Lyon, Vienna, Madrid and Brussels were 4.5% or less. Those in Munich, Helsinki and Dublin, for example, were 4.7% or higher. In shopping centres, yields in Paris, the large German cities and Vienna came in under the 5.5% mark, whilst Helsinki, Madrid and the major Italian cities were above 5.7%.

The average savings rate remained stable overall during the third quarter, suggesting that the steady level of consumer spending was the result of the strength of the labour market and the support from fiscal policy. This positive trend is likely to shift, as certain advance indicators relating to private consumption seem to be suggesting a drop in retail sector confidence but continued confidence in services in the fourth quarter of 2022. For the time being, store revenues saw year-on-year growth of 6% in the fourth quarter of 2022, with countries such as Austria and Portugal outperforming. Others, like Italy, Germany, Spain, France, the Netherlands and Finland, were close to or below the European average. Across the eurozone as a whole, retail sales volumes were down. This reflects the fact that increased store revenues were driven by higher prices rather than by volume growth.

Portefeuille High Street Retail ©Fabrice Debatty

Although rental values remained stable through the third quarter of 2022, this trend reversed in the fourth quarter for both high street assets and shopping centres. A large majority of high street in eurozone countries saw adjustments to their rental values. However, a few markets saw stability in values for both high street and shopping centres. This said, the attractiveness of the most sought-after locations for stores was not affected, as the majority of rents remained stable or increased over the year.

RETAIL INVESTMENT VOLUMES IN EUROPE



Portefeuille High Street Retail ©Fabrice Debatty

RESIDENTIAL

INVESTMENT IN RESIDENTIAL REAL ESTATE IN EUROPE – Q4 2022 (12 MONTHS)	€59bn
PRIME YIELDS IN EUROPE – Q4 2022 / Q3 2022	↗
RESIDENTIAL PRICES IN EUROPE – Q4 2022 / Q4 2021	↗
HOUSEHOLD INCOME IN THE EUROZONE – Q4 2022 / Q3 2022	↗

Investment in block residential assets in Europe ended up holding on to its second place, behind offices but ahead of logistics, with total investment volume of around €59 billion in 2022 (-42% over the year). With investors biding their time on Germany, after a record year in 2021, and Sweden, due to the downturn in the market, they turned instead to France, Spain, Belgium or the UK. Within the eurozone, Germany saw total investment of nearly €12 billion, followed by France with over €5 billion, then the Netherlands and Spain with over €3 billion each. Outside the eurozone, the UK market was the most active, with investment of €15 billion, followed by Sweden with over €5 billion and Denmark with over €4 billion.

Some decompression was observed in prime yields in the majority of markets, linked to the steep rise in borrowing rates. In the eurozone, after a low point in 2021, Paris and Munich still have the most compressed prime yields, but these are now approaching 3.0%. Both cities saw adjustments in the final quarter of 2022. Other major European cities followed a similar trend, with average decompression of between 20bp and 50bp, that is to say adjustments that were in line with rising borrowing rates.

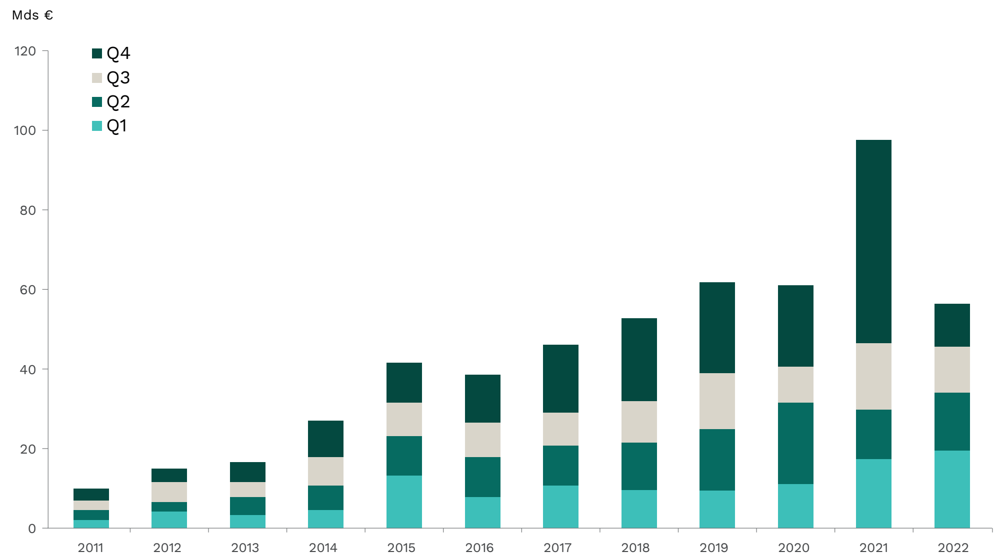
Although eurozone consumer price inflation (CPI) eased between November and December 2022, it remained at the high level of 9.2% over the year as a whole. For residential real estate, this increase in the CPI will be passed on through rent reviews in whole or in part, depending on the indexation mechanisms in use in each country. The countries where inflation was above this average were the Netherlands, Belgium, the UK and Spain. Countries at or below the average included Italy, Austria, Germany, Ireland, Finland and France. Meanwhile, regulations such as rent controls or energy performance criteria exist to protect tenants from abusive increases or energy-hungry homes.

Residential construction in Europe slowed in the second half in response to higher construction costs

Coliving Sharies - Bruxelles ©Jakub Mazur

and rising interest rates. In parallel, residential asset prices in the eurozone continued to rise on a year-on-year basis, but corrections began to appear in the fourth quarter of 2022. On average, residential prices in the eurozone continued to rise over the year as a whole (+2.5% year-on-year). Portugal (+10% y/y), Ireland (+8%), the Netherlands (+5%), France (+5%), Belgium (+4%) Austria (+4%), Spain (+3%), Italy (+2%) and Germany (+1%) all saw rising prices, whilst there was a correction in Finland (-2%) over the whole of 2022 relative to 2021. This said, between the third and fourth quarters of 2022, some markets saw adjustments due to a fall in demand and tighter borrowing conditions. At the same time, the introduction of energy performance standards in certain markets, such as France, has had a direct impact on properties with poor thermal performance, with such assets selling at a discount of around 15% to the prices of better performing assets.

INVESTMENT IN BLOCK RESIDENTIAL REAL ESTATE IN EUROPE



Coliving Sharies - Bruxelles ©Jakub Mazur

HEALTHCARE

INVESTMENT IN HEALTHCARE REAL ESTATE IN EUROPE – Q4 2022 (12 MONTHS)	**€7bn**
PRIME YIELDS IN EUROPE – Q4 2022 / Q3 2022	↗
FORECASTS OF BED DEMAND BY 2030 IN EUROPE	↗

After the sizeable investment volumes of the first nine months of 2022, investors in healthcare real estate were more cautious in the fourth quarter. Investment volumes (senior residences and care homes) totalled more than €7 billion in Europe in 2022, which was a year-on-year fall of 26% but above the average for the previous ten years. In Europe, capital flows were concentrated on the UK, with more than €1.8 billion invested over 2022, followed by Germany, with around €1.7 billion, France with around €650 million, then the Netherlands and Sweden with some €600 million each.

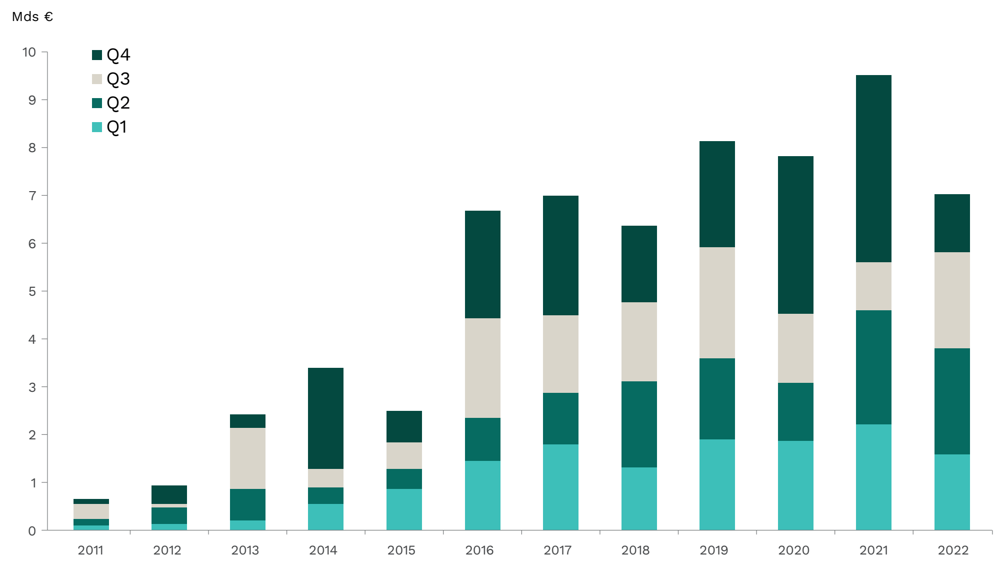
European prime healthcare yields were balloted at the end of 2022, between compression, stability and decompression. In France, Sweden, the UK, Belgium, Germany and Austria prime yields were at or below 4.50% for the best-quality senior care homes. For assets not in the heart of densely populated urban centres, this figure rises by between 50bp and 100bp. Prime yields in Italy, Spain, the Netherlands, Finland, Ireland and Portugal were above 4.50% for care homes at the end of the fourth quarter of 2022. Prime yields for clinics were stable over the year, at 5% or below in France and Germany but more than 5.5% in the Netherlands at the end of the fourth quarter of 2022.

The average price per bed in Europe was slightly less than €165,000 in 2022. The most prime assets changed hands at around €200,000 per bed, with assets in the bottom quartile moving above the €110,000 mark on average over the quarter. In France prices averaged close to €160,000 per bed over the quarter; Germany was next with an average close to €140,000 , whilst in Spain and Italy the average was above €100,000. Outside the Eurozone the average transaction price per bed was around €160,000 in the UK and Denmark, around €300,000 in Sweden and less than €100,000 in Poland.

Demographic shifts as a result of the ageing population have maintained pressure on the supply of healthcare real estate in the main European countries. At the same time, the obsolete section of the asset base needs to be renovated and the construction of buildings locked in, as there will be persistent demand over the coming years. At the end of 2022, Germany had the most over-75s (9.5 million people), followed by Italy (7.1 million), France (6.6 million), the UK (6.0 million), Spain (4.7 million),

Beausoleil EHPAD Korian ©Primonial REIM France the Netherlands (1.5 million) and Belgium (1.1 million). The dependency ratio, that is to say the ratio of the over-65 population to the population aged 15 to 64, is currently around 32.5% and is likely to rise to 52.6% by 2050. The consequence of an ageing population is an increase in the number of dependent older people. Loss of physical independence, particularly critical amongst those aged over 85, requires support or care provision.

SENIOR RESIDENCES AND CARE HOMES INVESTMENT VOLUMES IN EUROPE



Beausoleil EHPAD Korian ©Primonial REIM France

HOTELS

INVESTMENT IN HOTEL REAL ESTATE IN EUROPE – Q4 2022 (12 MONTHS)	€14bn
ROOM OCCUPANCY RATES IN EUROPE – Q4 2022 (12 MONTHS) / Q4 2021	↗
REVPAR IN EUROPE – Q4 2022 (12 MONTHS) / Q4 2021	↗
AVERAGE PRICE PER NIGHT IN EUROPE – Q4 2022 (12 MONTHS) / Q4 2021	↗
PRIME YIELDS IN EUROPE – Q4 2022 / Q3 2022	↗
EXPECTED TOURIST ARRIVALS IN EUROPE – 2022/2021	↗

After a satisfactory first half of the year, investors became more cautious in the second half of 2022. The hotel real estate market was worth €14 billion in 2022, down 22% year-on-year. Despite the marked upturn in international and domestic air travel, the uncertainties relating to the geopolitical and economic climate hobbled the completion of transactions. In Europe, capital focused on the UK, with just under €4 billion investment in 2022, followed by Spain, with nearly €3 billion, then France with over €2 billion, Germany at slightly under the €2 billion mark, and Italy and Portugal with around €1 billion each.

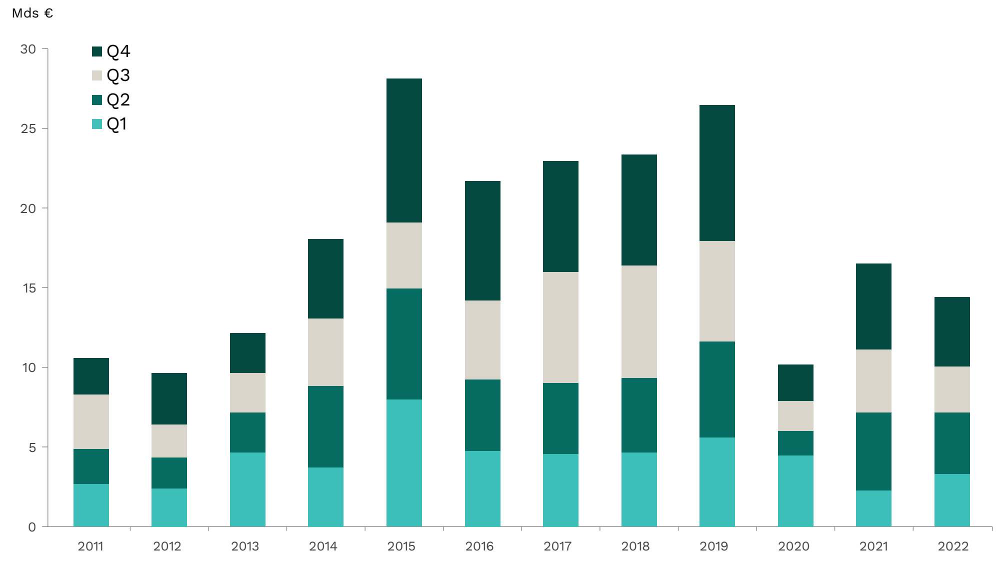
Prime yields on hotels saw further decompression year-on-year at between 5bp and 50bp on average at the end of the fourth quarter of 2022. Prime yields on leased hotels, based on rental profitability, were at or under 4.5% in London and Paris. In the big German cities, Madrid, Milan, Amsterdam, Brussels and Lisbon yields are now above 4.6%. Prime yields for hotels under management contracts, which allow hotel owners to capture value from both the operation of the hotel and the real estate asset, offer a supplementary yield above lease levels of between 100bp and 250bp.

The number of hotel rooms sold or let in Europe grew sharply in 2022 (78% higher over the year) as a consequence of the near doubling of passenger traffic in Europe in 2022 compared to 2021. This said, tourist numbers have still not returned to their 2019 levels, before Covid-19 brought air travel to a standstill and resulted in a collapse in passenger numbers in 2020. After the start of the year was affected by the Omicron variant and anxiety relating to Russia's invasion of Ukraine, traffic accelerated in the second half of 2022. Driven by these trends up-scale hotels (+83%) and the luxury category (+99%) recovered well. Budget hotels, which had suffered less, continued to perform well (+51% over the year). The mid-range category also made strong gains of between +75% and +86%.

Hotel B&B Nice Aeroport Arenas ©Primonial REIM France

Indicators for the hotel sector all showed strong improvement over 2022 compared to 2021 when restrictions were still in force. Occupancy rates in European hotels have risen steadily, gaining 214bp in 2022, taking them to over 64%. Average prices have followed a similar trend, rising to €137 per night at end-December, from €122 in 2021. RevPAR continued to rise, hitting €89 from just €53 a year earlier. By category, only budget hotels had an occupancy rate over 75%.

INVESTMENT VOLUMES FOR EUROPEAN HOTELS



Hotel B&B Nice Aeroport Arenas ©Primonial REIM France

Sources used throughout this document: Primonial REIM Research & Strategy data, Immostat, CBRE, Savills, BNP PRE, JLL, Knight Frank, MSCI, Oxford Economics, Eurostat, OCDE, FMI, Stabel, NSI, CZSO, DST, Destatis, Stat, CSO, Statistics, INE, INSEE, DZS, ISTAT, CSB, Statistics Lithuania, Statec, KSH, CBS, Statistik Austria, Stat Poland, INE, INSSE, Statistics Finland, SCB, SSB, BFS, ONS, STR, Operators.

DEFINITIONS

10-year government bonds: debt securities issued by a state for a period of ten years, generally acknowledged to be a risk-free investment.

Investment volume in corporate real estate: total volume of premises acquired in the offices, retail, business premises and warehouses segments by an investor.

Take-up of offices: all leases or sales to the occupant (as opposed to sales to investors) for premises to be used as offices. It is expressed as square meters of usable space.

Sale Before Completion: sale before completion is the contractual method for selling a building before it is built. The investor becomes the owner as it is built.

Free leases: favourable measures granted to tenants (rent cuts, renovation work, etc.).

Yield: ratio between the gross or net revenues from the building and the capital committed by the buyer (acquisition price + fees and transfer taxes).

Store premises: traditional ground-floor retail premises located in town-center high streets.

Shopping center: a building containing at least 20 retail outlets housed in indoor centers around a large food store that drives customer traffic.

Retail park: an outdoor shopping center built and managed as a single unit. It comprises at least five buildings linked by lanes and located on city peripheries.

Care homes: a health facility that houses dependent elderly people.

Medical, surgery and obstetric clinics: medical facilities for short-term care, with or without lodging, or for severe conditions during their acute phase.

RevPAR: abbreviation for Revenue Per Available Room. It corresponds to the turnover on accommodation of an establishment divided by the total number of rooms RevPAR also corresponds to Occupancy Rate multiplied by ADR

ADR: abbreviation for Average Daily Rate. It is calculated (excluding breakfast) by dividing total revenue by the number of occupied rooms.

Hotel Occupancy Rate (OR): ratio of the number of occupied rooms to the total number of rooms in a hotel.

About Primonial REIM

Primonial REIM has a workforce of 400 employees in **France, Germany, Luxembourg, Italy, United Kingdom** and **Singapore**. Its values of conviction and commitment as well as its expertise on a European scale are used to design and manage real estate funds for its national and international clients, whether they are individuals or institutions.

Primonial REIM currently has €34,8 billion of assets under management. Its conviction-based allocation breaks down into :

- **44%** offices,
- **33%** healthcare/education,
- **11%** residential,
- **6%** retail,
- **5%** hotels,
- **1%** logistics.

Its pan-European platform manages **61 funds** and has more than 100,000 investor clients, **54%** of which are **individual investors** and **46% institutional**. Its real estate portfolio consists of more than 1,535 properties (offices, healthcare/education, retail, residential, hotels) located in **10 European countries**.

www.primonialreim.com

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The Research & Strategy Department's role is to formalise Primonial REIM's real estate investment strategies, based on continuous monitoring of the French and European markets. Although collective real estate accounts for a growing share of institutional portfolios and household savings, it is at the crossroads of financial (hierarchy of rates), economic (tenants' business models), demographic (the metropolisation phenomenon) and societal (changes in usage) factors. This is why a cross-cutting analysis is needed, which is also long term and therefore in keeping with the horizon of most real estate investors.

Real Estate Convictions Europe offers Primonial REIM's quarterly view of its markets of choice, i.e. offices, retail outlets and healthcare and residential real estate, in the Eurozone.

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Ref.: Real Estate Convictions Europe Brochure – **022023** - Primonial REIM, a simplified joint-stock company with capital of 10,000 euros, registered with the Business and Company Register, Paris, under number 884 030 842, with its head office at 6-8 rue du Général Foy, 75008 Paris, and with the tax identification number FR18 884 030 842.