Real Estate House View

Norway, Sweden, Finland, Denmark

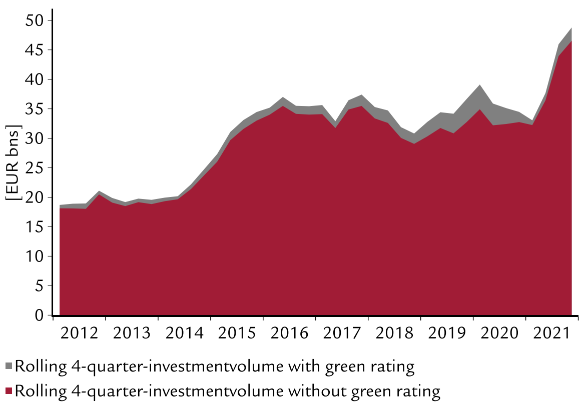
SwissLife
Asset Managers

First half of 2022

Key takeaways

- **Almost half of Germany:** Due to M&A activities on top of normal transaction activity, the investment volume of the Nordic countries has reached a new record and now amounts to almost 50% of the market volume of Germany, Europe's largest real estate investment market. Even without M&A activities, the positive momentum is set to continue in 2022 as indicated by the fundamental data.
- **Green is the new black:** The awareness of and demand for sustainable real estate is increasing among both tenants and investors. This is particularly apparent for the office type of use, while the other sectors are set to follow suit.
- **Polarisation is continuing:** Investors in the Nordic countries, fundamentally considered to be "safe havens", are also increasingly attracted to Core properties, particularly in the office sector. The shift towards more "resilient" segments, such as (discount) food and household goods, is continuing in retail.
- **Shortage:** The logistics sector would like to run hot but is being curbed by the lack of (modern) space. This is in turn affecting rents and yields.
- **Shortage overcome:** The residential sector is sending out initial signs of the shortage being overcome. Positive figures are coming from construction activity. Nevertheless, residential rents are set to rise further – also in a partially regulated environments such as in Denmark and Sweden.

Chart in focus



Source: RCA (data for Q4 2021 are provisional).
Nordic countries = Denmark, Sweden, Finland, Norway;
green rating according to RCA

New year, new record. The Nordic real estate investment market has peaked again. Around EUR 48.8 bn were invested in the Nordic countries in 2021 – 42% more than in 2020 and 40% above the five-year average. While M&A activities are also one of the causes, the data still remain positive even when adjusted for these: a swift economic recovery, low interest rates and a banking system that supports real estate investments are exerting a positive impact. The only downside is that investors would prefer to see more ESG-compliant properties and investment opportunities with green ratings.

Measured against the purchasing managers' index for manufacturing, the North European economies were among the most dynamic in the world at the end of 2021. There are increasing signs of overheating in some sectors in the region. For example, Denmark's unemployment rate recently fell to 2.4%, putting it well below the average rate of 3.2% in the four years preceding the pandemic. In view of these tendencies, Norway's central bank has already started to hike its key interest rates. We anticipate further rises in interest rates in 2022 and expect Sweden's Riksbank also to carry out an initial interest rate hike in the near future.

Office: it has to be Core and ESG

A tentative recovery and continued polarisation in favour of ESG-compliant Core properties at prime locations are also emerging in the Nordic office rental markets. The topic of ESG in particular has gained momentum in recent months. In Oslo, for instance, a trend towards green roofs can be observed. Oslo is also the market in the Nordic countries with the highest rental growth for high-quality office space (Q3 2021: +3.5% compared with Q3 2020). Helsinki, by contrast, is the leader in vacancies: a vacancy rate of above 13% was recorded again in 2021 for the first time since 2018; the rate in Oslo is 6.8%. Copenhagen is the only core market in which vacancies are already falling again (Q3 2021: 7.4%). The investment market posted a record thanks to a corporate merger. However, real asset investors are continuing to focus on Core properties, which means that volumes of investments in rare CBD properties are remaining stable and prime yields are falling further. The lowest prime yield is offered by real assets in Stockholm (3.0%).

Retail: floor reached?

Despite an above-average vaccination rate in the Nordic countries and a consequent lifting of restrictions and increasing consumer mobility, the retail sector remains fragile and is undergoing restructuring, with the absence of tourists (from abroad) and the fall in real wages, particularly in Denmark and Finland, curbing potential. Retail is witnessing a series of closures on the one hand, particularly in the fashion segment, and on the other hand the entry of new players and expansions in the food (discount) and household goods segments that are coming up with new concepts. All in all, both the rent corrections and the rise in vacancies continued in the retail sector in 2021. We expect rents to bottom out. The prime yields of high street properties, which remained stable in 2021, can also be expected to bottom out. The picture for shopping centres was more pessimistic, with their risk premiums continuing to increase in 2021. However, a slight price correction can be anticipated in the medium term.

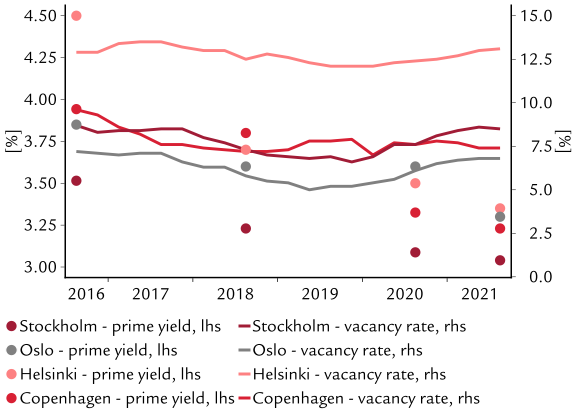
Logistics: potential and shortage

The fundamental data of the rental market are good, and investors are displaying interest. The only problem is the shortage in Denmark of well-located warehouses and in Finland of modern buildings. This is exacerbated by the low share of speculative completions compared with other European countries due to market restrictions, which together with high planning requirements is preventing the potential for logistics space in the Nordic countries from being exploited. According to Newsec, the supply of modern logistics space per capita in the Nordic countries therefore lies below 1 m^2/capita, which is behind core markets such as Germany (1.6 m^2/capita) and the Netherlands (1.3 m^2/capita). At the same time, the Nordic capital cities have an advantage: they are protected against competition thanks to their location. Investors are recognising the potential and pouncing on the scarce supply, which is causing yields to decrease further.

Residential: more and regulated

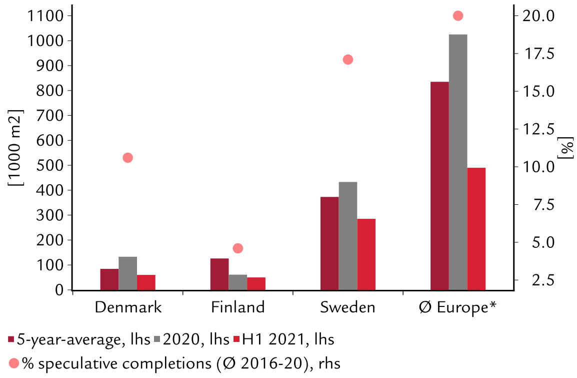
On the other hand, the residential sector is displaying positive availability trends: at 36 569 units, the number of newly begun apartment constructions in the first three quarters of 2021 in Finland was 20% above the five-year average. There were 26 318 apartments completed in Denmark over this period (+24% above the five-year average). Furthermore, the conversion of offices into residential buildings got underway in Copenhagen. Unlike that of Finland, the Danish housing market is highly regulated: residential buildings constructed prior to 1992 (80% of stock) are subject to rent control. Nevertheless, investors are placing their capital in them and pushing down yields, which in Copenhagen came to 3.2% at the end of 2021 (-5 bp on 2020). Rents in Sweden are set to rise below the level of inflation due to regulation.

Figure 1: Office sector: vacancy rates and prime yields



Source: PMA

Figure 2: Logistics completions (>10 000 m²) and share of speculative completions



Source: PMA,
Europe* = Belgium, Czech Republic, Denmark, Finland, France, Germany, Hungary, Ire-land, Italy, Netherlands, Poland, Portugal, Spain, Sweden, UK

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