DTZ RESEARCH

# Risks from Overheating Markets

## Money Into Property

DTZ



DTZ INSIGHT

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## Money into Property 2015

15 June 2015

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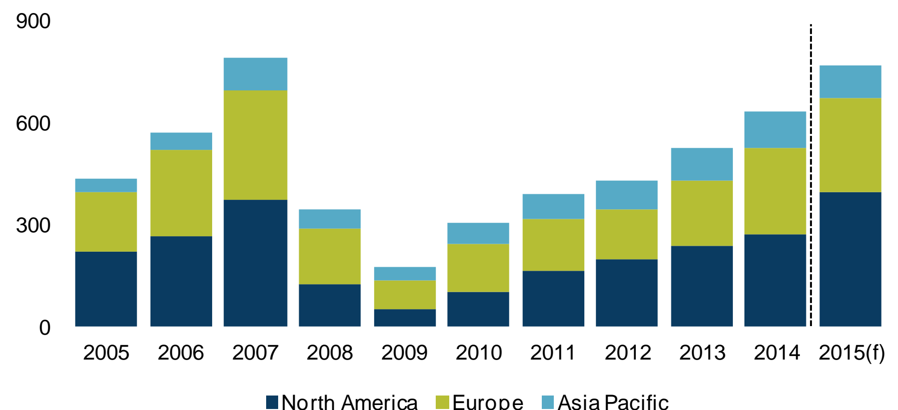
- Global invested stock reached a new record level of USD13.6tn in 2014, a 5% increase on a year ago. Regional stock levels have now recovered from the downturn and stand above their previous peak in local currency terms.
- In the current cycle, equity continues to replace debt in the capital stack. Equity grew 8% in 2014 compared with a 2% growth of debt. Overall leverage levels continue to fall globally and across each region.
- Non-bank lenders are increasing their activity, especially across Europe, at the expense of banks. The workout of legacy debt across Europe continues, with the volume of debt outside the UK only 2% below its peak. The US is now recovering, with the UK not too far behind.
- The rise in equity is being driven more by unlisted funds. The equity value of assets held by this segment has increased more than that of listed companies and institutions. The growth in funds has been supported by increased flow of equity into them over recent years.
- Investment activity has continued to flourish and is set to close in on 2007 peak levels in 2015 (Figure 1). Activity in gateway cities has been supported by stronger cross border, institutional and sovereign capital. Activity is moving across other cities led by increased weight of capital, especially from funds.
- Lack of opportunities in core and record low yields is leading investors to target non-core opportunities. Investors need to move now whilst the window of opportunity remains as yields will compress quickly.
- Real estate remains attractive in the current low interest rate environment, but weight of capital is leading to signs of overheating in some markets. Expectations of rising interest rates could diminish real estate's attractiveness and lead to a reversal in the flow of equity into funds with non-gateway markets more exposed. Investors therefore need to focus on fundamentals.

Figure 1

**Global investment volume forecast, USD bn**




*Source: DTZ Research, Real Capital Analytics*

# Money into Property 2015

## Introduction

It is with great pleasure that we present the 41st edition of Money into Property, probably the industry's longest running report. Having started out as a UK focussed publication covering the flow of capital into the UK investment market, the report today now covers 40 countries globally and considers the stock of real estate held by investors, as well as the flows of capital.

This report is split into three key sections. In the first section we take a historical look at the size of the real estate universe and what is driving the trends we see across countries and regions. In the second section we look at trends in capital flows across the globe and focus on major cities, where we see the largest concentration of this global capital. In the final section we draw together these trends and analyse what this means for the market going forward. We also present the recent results from our annual investor survey.

Nigel Almond

Head of Capital Markets Research

DTZ

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## Stock Update

### Growth across all markets

Global invested stock[1] continued its upward trend with a 5% increase to USD13.6tn. We have now seen continuous growth in stock at a global level since 2009, when we saw a dip in the wake of the global financial crisis (Figure 2). Globally stock is now 19% above its previous 2008 peak.

Asia Pacific benefitted from the strongest increase as stock grew 10% to USD5.1tn. The region is now driving itself away from the other regions driven by further growth in China. It is the only region to have seen continuous growth in stock over the past decade.

North America saw 5% growth from USD4.0tn to USD 4.2tn. Its stock is now 2% above its previous peak of USD4.1tn in 2007. It is also closing the gap on Europe, whose stock stood still at USD4.4tn. Although flat in dollar terms, this is masked by currency movements during 2014, which saw the dollar strengthen against the Euro. Although 10% below its peak in 2007 in dollar terms, in Euro equivalents its stock has now passed its 2007 peak of EUR3.3tn to stand at EUR3.4tn.

### Currency movements impact dollar growth

As ever currency movements are impacting the movements in dollar terms. Whereas Europe's stock was flat in dollar terms, in local currency it posted growth of 3% (Figure 3). Similarly Asia Pacific saw much stronger growth of 14% in local currency terms against 10% in dollar terms.

Asia's strength reflects the strength of China which saw its stock rise 21% in 2014 in dollar terms. Excluding China, Asia's growth in stock was a more modest 1%.

### Asian markets dominate top 10 as Europe lags

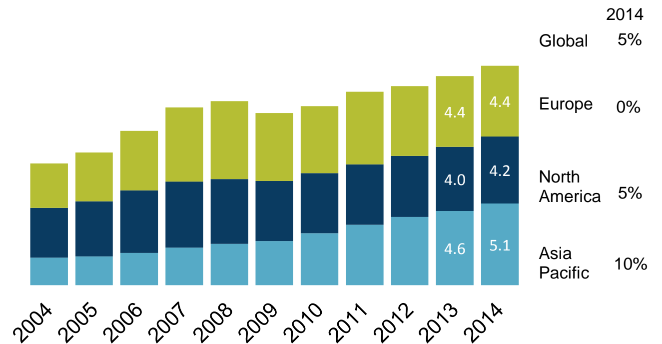
The strongest growth in stock during 2014 was seen in Turkey, although this comes off a low base. Mexico, also relatively small in terms of its stock, saw strong growth of 25%. China leads five Asian markets in the top 10 growth markets in 2014 with its stock increasing by 23% in local currency terms. Four other Asian markets in the top 10 growth markets also recorded double-digit growth in 2014 (Figure 4). Of note is India where we have seen continued development and new additions to stock.

European markets dominate the bottom 10 growth markets. All these markets saw their stock fall in value over the year. The weakest growth market was Russia, falling by 19%. Investment activity has collapsed in the wake of sanctions and hostilities in Ukraine. Spain, and to a lesser extent, the UK, also saw their stocks reduce, both driven by further falls in debt. New Zealand is the only non-European market in the bottom 10, and its stock was flat over the year.

[1] Invested stock relates to the open market value of commercial real estate held by investors (see definitions page at end of the report).

Figure 2

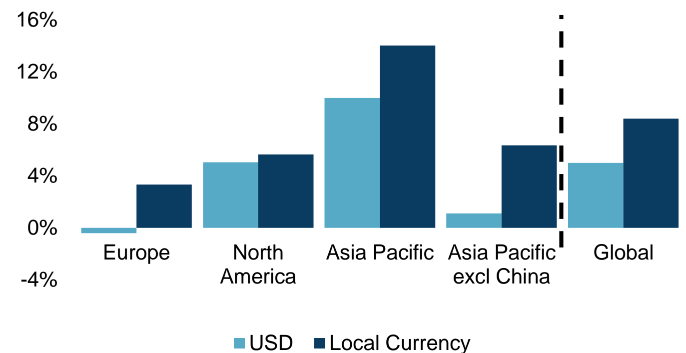
**Global Real Estate Invested Stock, USD tn**




*Source: DTZ Research*

Figure 3

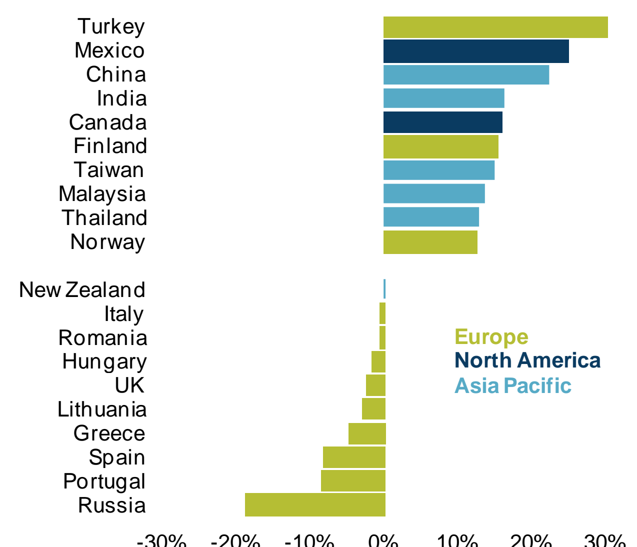
**Change in Invested Stock, 2014**




*Source: DTZ Research*

Figure 4

**Top and bottom 10 growth markets, local currency, 2014**




*Source: DTZ Research*

## Debt continues to lag equity growth …

Breaking down growth at the global level highlights the continued trend of equity increasing and also replacing debt in the capital stack. The equity component of stock has been in recovery since the end of 2009 and has risen by over 50%, compared to 10% growth in debt. In 2014 these trends remained with equity up 8% and debt up 2%. This contrasts with a more balanced growth of debt and equity up to 2007.

Private equity remains the key driver, which rose by 10%, compared to the publicly listed sector where equity was up by just 2% (Figure 5). We will consider these trends in more detail later. On the debt side we see more muted growth. In the private markets we continue to see a reduction in debt held by bad banks, with non-bank lenders continuing to increase their activities at the expense of traditional commercial banks particularly as the ongoing work out continues in Europe.

The public markets continue to be characterised by reductions in CMBS and covered bonds (especially across Europe). Property company bond issuance remains on the rise in the low interest rate environment. The total outstanding rose a further 12% to USD425bn globally, and is now close to double its 2008 level. The USD45bn increase in bonds was insufficient to offset an USD87bn fall in CMBS and covered bonds though.

## … leading to further deleveraging

With the value of equity continuing to grow ahead of debt, we have seen aggregate gearing shrink further. The global average gearing fell to 55% compared with 56% last year. Asia Pacific continues to see the lowest leverage at 49%, down from 50% last year. North America continues to see the highest gearing at 64%. Europe's leverage was down to 53% compared to 55% last year (Figure 6).

## Growing diversity in lending sources

As we have highlighted in previous reports, the trend of greater diversity in the sources of debt continues (Figure 7). This is a welcome shift, as having a wider source of funding should provide more resilience and stability to markets. Europe, which has historically been dominated by traditional banks, has seen its share fall from 89% in 2007 to 87% today. Part of the fall has been offset by growth in non-bank lenders (institutions and private equity funds) whose share has risen from 1% to 5% over the same period. Low interest rates have also made bonds more popular. We discuss these trends in more detail later.

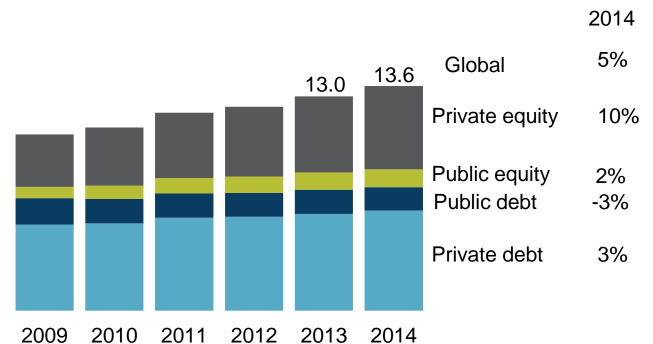
Perhaps more striking has been the increase in non-bank lending in Asia Pacific. This shift is restricted to China, where government policies to curb credit has led to the growth in alternative sources including tuts funds, as well as bond issuances[2]. In fact excluding China the non-bank share is negligible in the region.

North America has the most diverse lending market by source, where banks represent only half the outstanding debt. This has supported a stronger recovery in the markets compared to Europe. Non-banks in the US (mostly institutions) have increased their share. This reflects less activity compared to the peak of the market in 2006/07. As a result loan books did not shrink and have since shown a stronger recovery.

[2] See DTZ Money into Property 2014

Figure 5

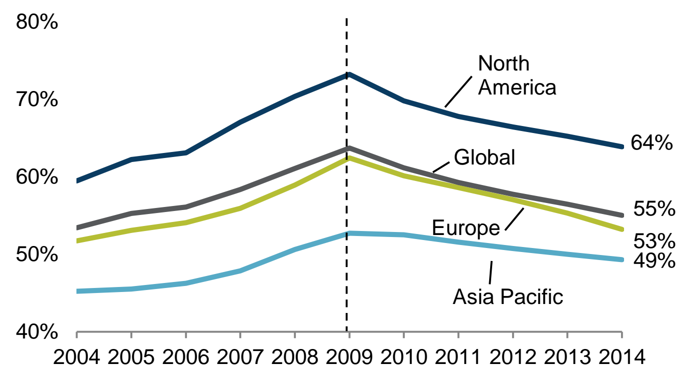
**Global invested stock by source of capital, USD tn**




*Source: DTZ Research*

Figure 6

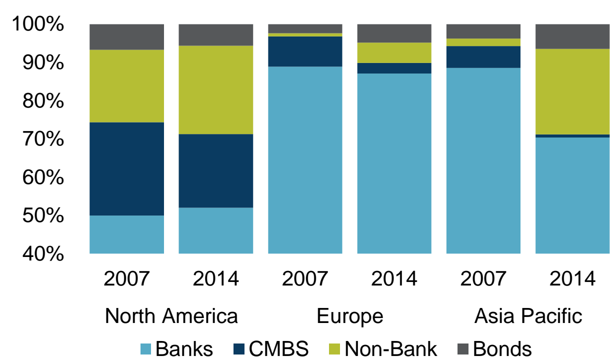
**Debt as a percentage of stock**




*Source: DTZ Research*

Figure 7

**Outstanding debt by capital source and region**




*Source: DTZ Research*

## Lower leveraged markets grow faster

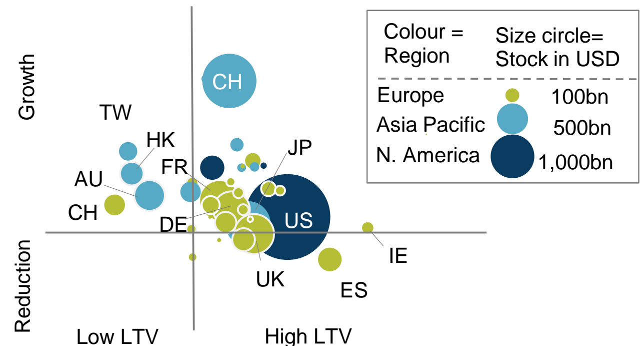
In the wake of the global financial crisis, more highly leveraged markets have been held back. Whilst growth in the period 2005-07 was supported by a debt-fuelled binge.

In recent years we have seen more equity rich (lower leveraged) markets grow faster (Figure 8). More established and relatively more leveraged markets such as the US and UK (which saw their stock nearly double in the five years to 2007), have both languished in recent years, with little or negative growth. Other European markets saddled with debt, such as Ireland and Spain are also in the bottom right corner.

Asia Pacific has been impacted less, with markets in the upper left quadrant such as Australia, Hong Kong and Taiwan. China with an average LTV, has also seen strong growth, though some of this has also been fuelled by debt.

Figure 8

**Change in stock v Leverage**




*Source: DTZ Research*

## European debt burden remains elevated

Across North America debt has returned to growth having fallen over 10% from 2008-2012. The degree of deleveraging in Europe remains weak, especially in some markets. This suggests there is further work to be done. Overall debt outstanding to commercial real estate in Europe at end 2014 was EUR1.8tn. This is just 7% lower than its peak of EUR1.9tn in 2008(Figure 9).

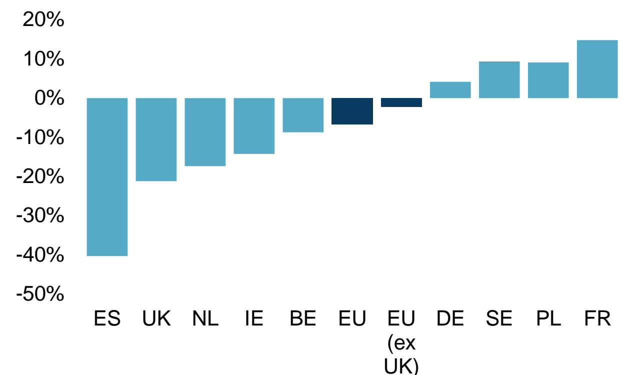
The biggest falls have been in Spain, the UK, the Netherlands and Ireland. Much of this has been the result of write downs, increased equity injection and lower levels of lending, as debt now secured by bad banks and non-banks is included in this analysis. In some of these markets, notably the UK, the unwinding of legacy debt is reaching a close.

Europe's 7% decline is driven by the UK. Excluding the UK from the analysis shows a more modest 2% fall. This suggests there is further work to be done in working-out legacy loans, especially when the debt burden in some markets, notably Germany and France, has actually increased over the period.

Increases in Sweden reflect greater caution from previous crises, so exposures in the country have been able to grow more quickly since the lows in 2008/09, especially as investment market activity has now risen back to pre-crisis levels. That is not to say that local Swedish banks have not been exposed to markets such as Denmark or the Baltic States.

Figure 9

**Change in European debt 2008-2014, selected markets**



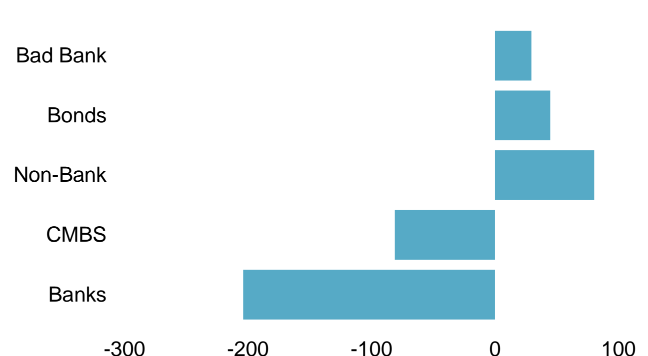

*Source: DTZ Research*

## Banks and CMBS bear the losses

Overall the biggest reduction in outstanding debt has been with traditional banks. Since 2008 their aggregate loan books have shrunk by over EUR200bn (Figure 10). CMBS balances have also shrunk by over EUR80bn. Some of this debt has shifted. Bad banks now hold close to EUR30bn of assets. In 2008 they did not exist, though their holdings are now shrinking. Non-banks lenders (institutions and funds) have grown their balance sheets by over EUR80bn. We expect this trend of more activity from non-bank lenders to continue.

Figure 10

**Change in sources of European debt 2008-2014, EUR bn**




*Source: DTZ Research*

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## Listed and unlisted funds grow at the expense of private companies

Just as there have been changes in the structure of debt markets, so too has the pattern of holdings changed on the equity side in the wake of the financial crisis.

Excluding any debt, the equity portion of private companies and individuals have dominated the North American and European markets (Figure 11). Since the onset of the financial crisis these two groups have seen their share of holdings shrink, no doubt reflecting their greater reliance on debt and struggles in the wake of the financial crisis. Asia portrays a different picture of growing ownership. Here we have seen accommodating policies, especially in China, that have led to growing investment in land and non-land assets since 2008.

Institutional investment, although increasing, has not been at the same level of other groups. Across North America listed companies and to a lesser extent unlisted funds have increased their equity holdings. In Europe it has been driven mostly by unlisted funds.

## Unlisted funds increased most over last two years

If we consider the timing of change we observe globally a rise in holdings from the listed sector in 2012. Since then growth in holdings has been less strong. This is consistent with transaction data that has shown net sales by many listed companies in part of 2012, 2013 and 2014 as they sought to further reduce leverage (Figure 12).

In contrast unlisted funds have been growing their holdings and new equity into funds has grown over this period, having fallen briefly in the wake of the crisis. Many of these funds have relatively short hold periods of around six years or benefit/ suffer from strong inflows and outflows, which may have impact moving forward. Although many have used high levels of leverage in the past, on a more positive note, separate analysis[3] implies gearing is now lower, requiring investors to place more equity into deals. This has been especially true in Europe where average lot sizes have yet to return to pre-crisis levels, even though the number of transactions has surpassed 2006-07 levels and volumes are nearing previous records. Institutions continue to grow their holdings, but increases are more modest.

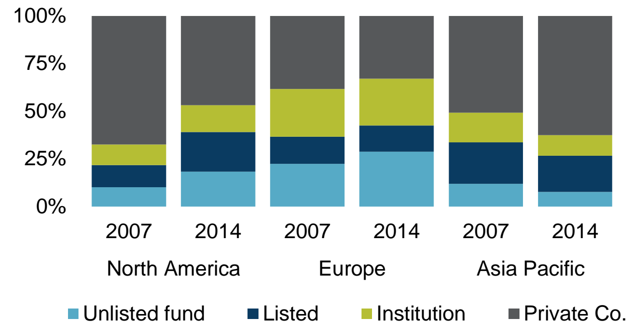
## Capital values help drive equity growth

Recent growth in the value of equity has been in relatively smaller markets and or those in recovery. Ireland saw the biggest increase in 2014, despite aggregate debt levels continuing the fall (Figure 13). The increase reflects improving investor sentiment that has compressed yields and led to rising values. Similarly Mexico has also seen a recovery in values. Turkey and also Norway have also seen strong growth, again reflecting improved capital values, although in the case of Turkey, there has also been an increase in debt. China has followed a similar path. Markets burdened by debt or by falling values driven by outward yield movements sit at the bottom of the table.

[3] See for example DTZ Insight, Great Wall of Money, April 2015

Figure 11

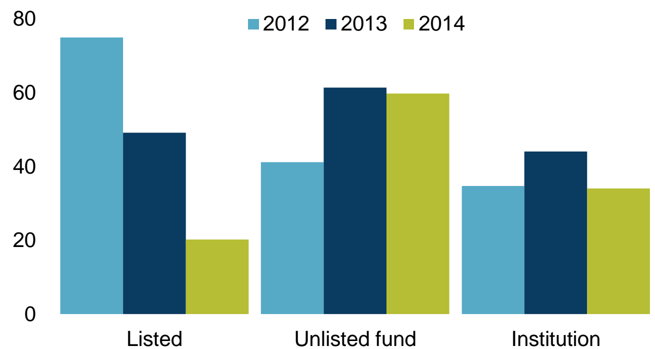
**Equity by source and region 2007 v 2014**




*Source: DTZ Research*

Figure 12

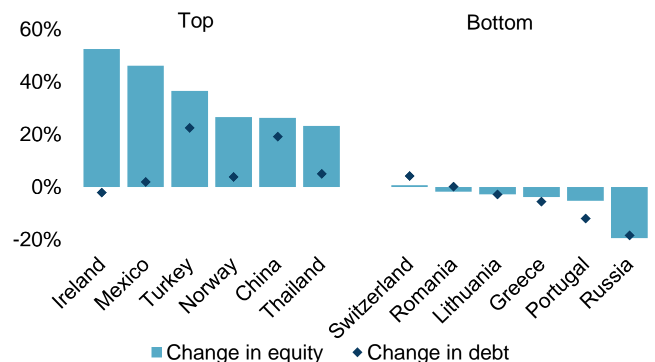
**Change in equity ownership globally, USD bn**




*Source: DTZ Research*

Figure 13

**Change in equity and debt, 2014**




*Source: DTZ Research*

## Capital Flows

### Global recovery continues

Global investment markets continue to flourish. By the end of 2014 global volumes reached USD633bn, a 20% increase on 2013. Growth was observed in all three regions, led by a 32% increase in Europe (Figure 14). The momentum has continued into 2015, with global volumes in the twelve months to end Q1 2015 reaching USD653bn. This is still below the peak in 2007.

Having reached a record high of USD107bn at the end of 2014, activity across Asia Pacific slowed in the first quarter compared with the same period a year ago. We believe some of this is due to a temporary pause as investors take stock of conditions and struggle to find suitable product. Strong growth continues in both Europe and North America. European volumes were up nearly 30% in Q1 2015 compared to Q1 2014 at USD263bn. North America volumes were up 12% to USD291bn over the same period.

### London on top, US cities dominate top 15

London continues to attract the largest volume of investment in deals over USD20m, with USD35bn invested in the past twelve months (Figure 15). Close behind is Manhattan (USD26bn) and San Francisco (USD23bn). At USD20bn, Tokyo was Asia's top city for investment. Of the top 15 cities highlighted, half are located in the US, with just two in Europe – Paris being the second dominant city. No German cities make the top 15, but the major 5 combined come close to investment levels in Paris and underscore the diverse investment opportunities in Germany. The Australian cities of Melbourne and Sydney, both rank high and ahead of Singapore, where we have seen investment activity slow in the last twelve months.

London's dominance reflects its appeal to cross border investors (see Map 1 overleaf). USD21bn or 60% of total investment came from capital outside of Europe (Inter-regional) in deals over USD20m. In the other leading cities inter-regional investment was still sizable, though typically no more than 30% of total activity. Domestic investment is still dominant in the major US cities, but partly reflects the sheer size of the US. Domestic investment is also strong in Asia Pacific, but in some markets which are typically 90%+ domestic, we do see increased cross border activity, e.g. Tokyo.

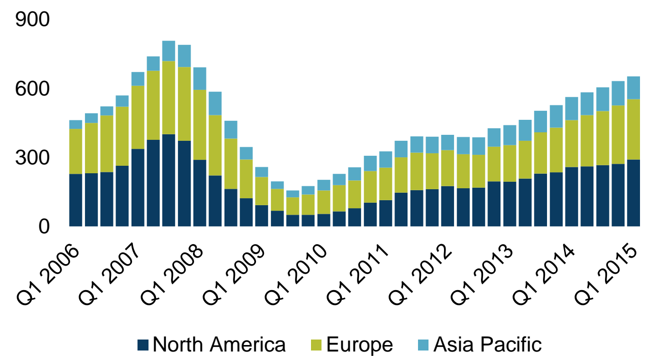
### Cross border investment drives growth

A higher level of cross border investment is helping to drive overall market growth (Figure 16). Even in relatively smaller cities we see higher levels of cross border investment, helping to drive higher growth in activity. These include cities such as Madrid, Melbourne, Prague and Brussels. A number of markets in the lower left quadrant show weak growth in overall and cross border investment. These are typically smaller Asian markets including Guangzhou and Osaka.

Equally some major cities show weaker volume growth, despite higher levels of overseas investment, including Chicago, Seoul and Munich.

Figure 14

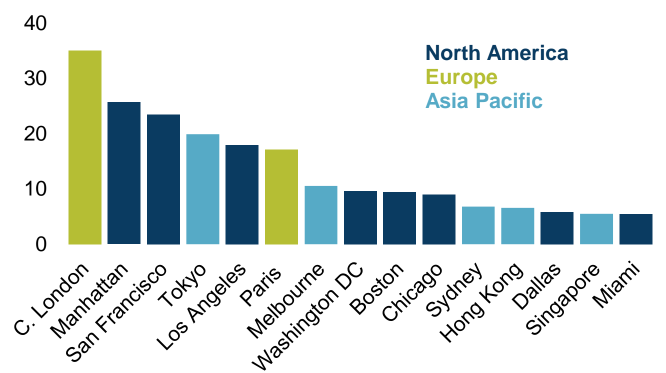
**Global investment activity, rolling annual, USD bn**




*Source: DTZ Research, Real Capital Analytics*

Figure 15

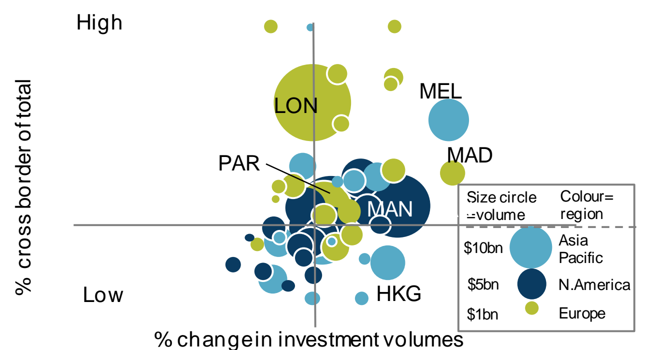
**Investment in major global cities, Q2 2014-Q1 2015 USD bn**




*Source: DTZ Research, Real Capital Analytics*

Figure 16

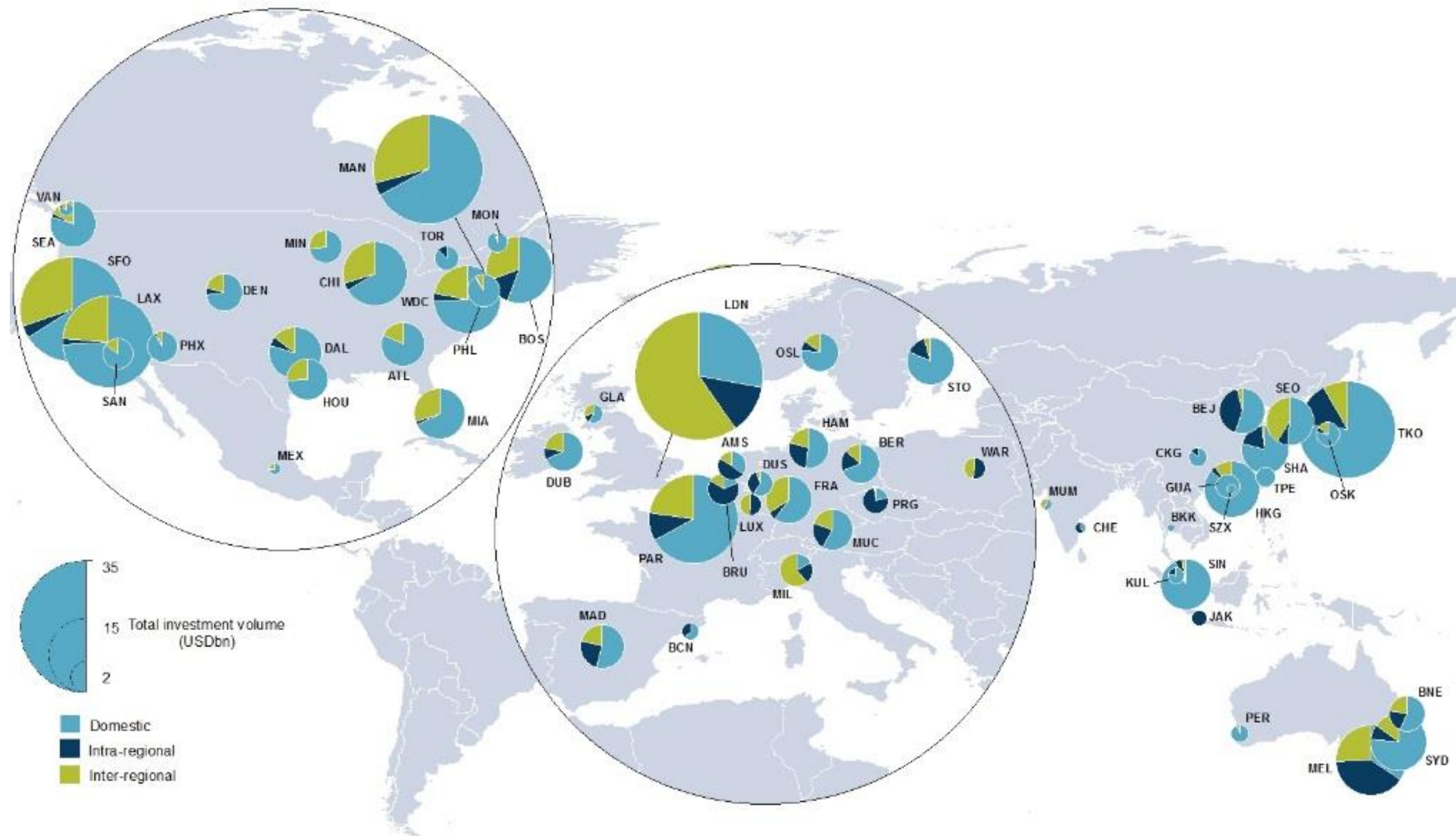
**Investment in major global cities, Q2 2014-Q1 2015**




*Source: DTZ Research, Real Capital Analytics*

# Money into Property 2015

**Map 1. Investment volumes across key global cities, Q2 2014-Q1 2015**




*Source: DTZ Research, Real Capital Analytics*

## Global and North American capital dominates

Consistent across all regions is the strength of capital raised by funds from across multiple jurisdictions, where ultimately there is no one single source (international sources of capital). The past year has seen close to USD30bn invested across all three regions from these international funds. North American capital (both US and Canada) is the next largest pool with over USD18bn invested (Figure 17).

## Growth in Asian and sovereign capital

The other key trend we see is the rise in Asian money invested in Europe and North America – especially from China and Singapore. More recently we have also seen these investors becoming more active in their home region. This has included GIC investing USD1.5bn at Pacific Century Place, Marunouchi, Tokyo, with CIC also behind the commercial property complex Meguro Gajoen in Tokyo for USD1.2bn. Similar trends have been observed in Sydney and Melbourne.

Norwegian capital, driven by the Sovereign Wealth Fund (Norges Bank) has also been highly active in North America and Europe. This has included investments in New York, San Francisco and Boston. Mature gateway cities in Asia Pacific are expected to be a target over the next couple of years.

Middle Eastern capital, led by Qatar, is also growing, and predominantly in Europe. This excludes the recent takeover of Canary Wharf group alongside North American investor Brookfield.

## Asian and Middle Eastern investors grow holdings

Across both Europe and North America, Asian investors are increasing their holdings with relatively limited sales in major cities. The same is true of Middle Eastern sources. Having been strong investors over the past decade, North American investor are showing a higher degree of trading, especially across Europe (Figure 18).

Activity is no longer being restricted to the leading gateway cities, such as London. In the past twelve months investment has spread to include Amsterdam, Brussels, Hamburg and Milan in Europe and across North America we have seen investments in Boston, Houston, Seattle and Vancouver.

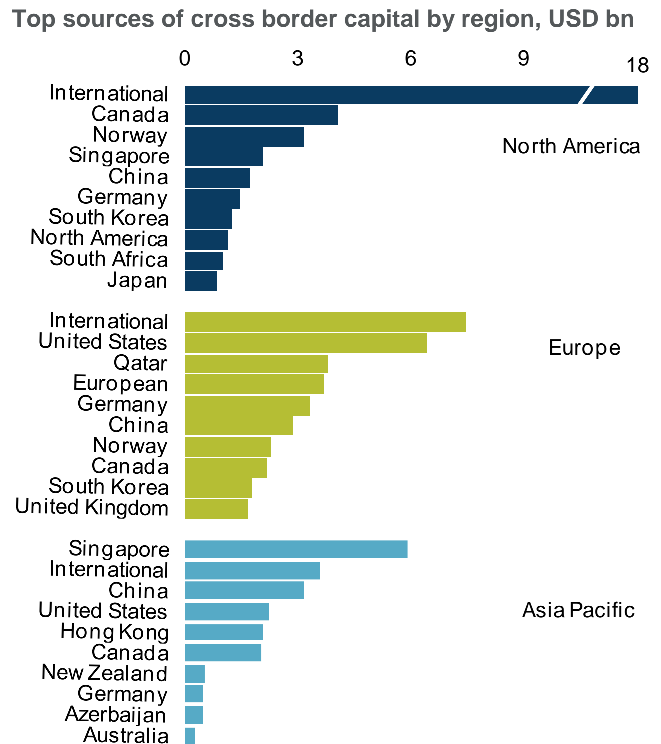
## SWFs & institutions bring diversity to gateway cities

The strength of Asian and Middle Eastern flows, is driven by Sovereign Wealth Funds (SWFs) and institutional sources. Across all regions SWFs were net buyers in the leading 60 cities we monitor (Figure 19). Most of the activity was in leading gateway cities including London, New York, Paris, San Francisco and Tokyo. This provides greater diversity in the type and source of capital. Institutional investment was largely net positive, except in North America where there has been a higher degree of trading. Here the listed sector was the biggest net investor, supported by capital raisings.

Unlisted funds have typically been net sellers over the period, reflecting their shorter hold periods and higher propensity to trade in major cities. More broadly we continue to see strong levels of activity, with many shifting their focus more broadly.

Figure 17

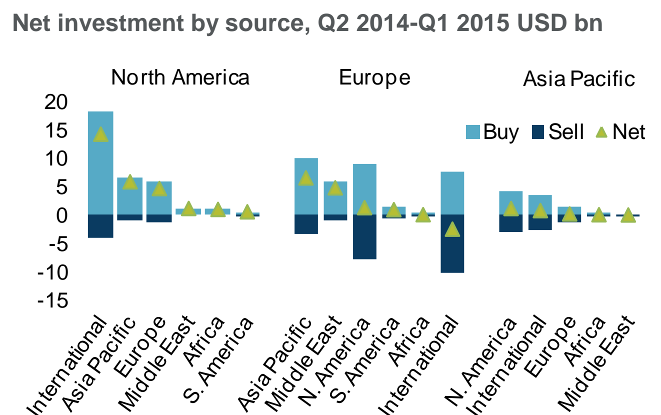
**Top sources of cross border capital by region, USD bn**




*Source: DTZ Research, Real Capital Analytics*

Figure 18

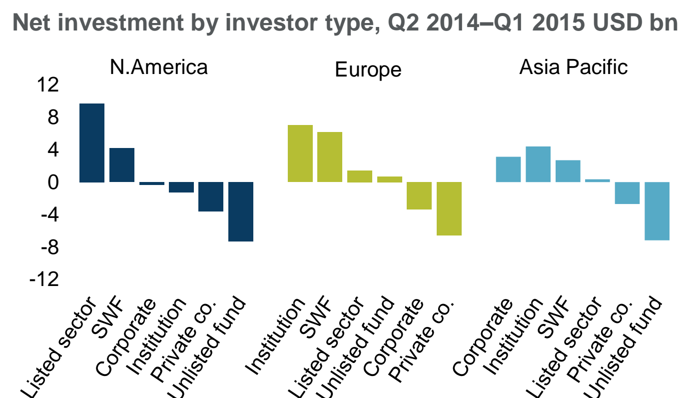
**Net investment by source, Q2 2014-Q1 2015 USD bn**




*Source: DTZ Research, Real Capital Analytics*

Figure 19

**Net investment by investor type, Q2 2014–Q1 2015 USD bn**




*Source: DTZ Research, Real Capital Analytics*

## Outlook

### Economic fundamentals remain strong

Current economic fundamentals remain strong and supportive of positive growth across the globe. Asia Pacific is expected to post the strongest performance over the next couple of years (Figure 20), followed by the US and Europe, which is expected to rebound from negligible growth. A number of economies continue to receive monetary support and benefit of low interest rates. Although interest rates have been low for a number of years in many markets, the projected economic recovery is likely to coincide with an increase in interest rates.

### Supporting occupier fundamentals …

The improved economic environment is also expected to be supportive of property market fundamentals. Improved take-up and a relatively low supply pipeline is expected to generate rental growth, averaging around 4-5% this year and marginally lower next year. The strongest growth is expected in Europe and the US.

### … and investment performance

This backdrop is underpinning positive investor sentiment. Based on our recent survey of 140 investors globally, the majority expect improved returns this year compared with our survey last year. Whilst a majority expect returns of between 0-9%, a higher proportion expect double digit returns in EMEA and North America. The same is true of overall global returns (Figure 21). The trends are similar to our own expectations where we see double digit returns in Europe and close to double digit in the US.

Prime yields have continued to compress over the past year, supported by the strong level of investment activity highlighted in the previous section. Average grade yields are also benefitting strong compression.

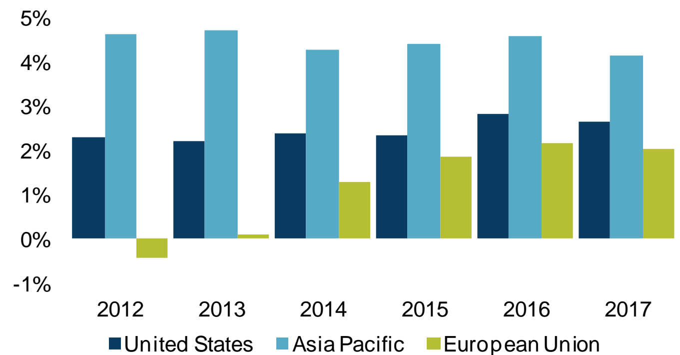
### Further yield compression storing future risks

Whilst prime yields in a number of major cities are now at or below levels seen in the previous crisis, they continue to enjoy a positive spread relative to bonds (Figure 22). This is in sharp contrast to the previous boom during 2006/07, when the yield gap turned negative for a while. Today in many cities we see a spread of at least 200bps. As a result, real estate still appears attractive relative to other assets classes. Given the low interest rate environment and continued demand we could see prime yields fall further, especially where the supply of prime stock is constrained.

As we move forward, and reflecting the positive economic environment, we do expect interest rates to rise. Were prime yields to fall further, and interest rates and bond yields to rise, there is a clear risk for property yields to correct. The impact of an outward shift from 3% will be greater that at 4%.

Figure 20

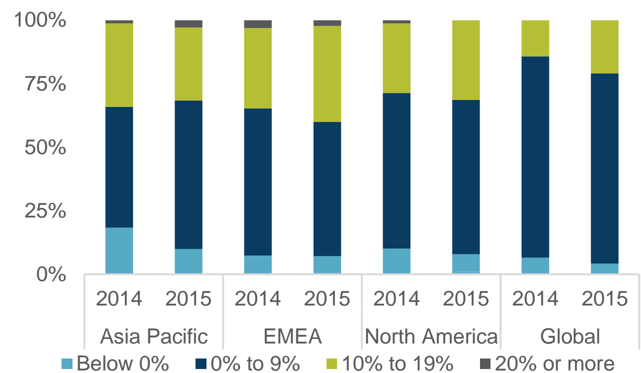
**Regional real GDP growth expectations LCU**




*Source: DTZ Research, Oxford Economics*

Figure 21

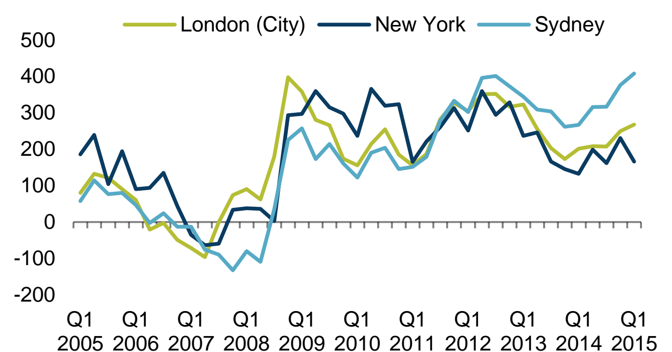
**Expected performance of CRE by region, 2014 vs 2015**




*Source: DTZ Research*

Figure 22

**Yield spreads selected markets, bps**




*Source: DTZ Research, NCREIF, Bloomberg*

## Record levels of new capital

The low interest rate environment, strong relative pricing and quantitative easing in some markets have led to strong growth in capital targeting real estate. DTZ estimates there to be a record USD429bn of new capital targeting CRE globally in 2015. This has reflected growth across the board (Figure 23). A marginal fall in capital targeting EMEA reflects the strength of the dollar against the Euro over recent months. In Euro equivalents capital rose by close to 12%, but the appreciation of the dollar against the Euro, wiped out these gains. In reality the region is now more attractive to dollar denominated capital.

## Equity continues to drive growth

Target gearing levels remain stable. This is largely a reflection of more appropriate lending conditions in the current market cycle as lenders generally adopt more rational lending policies. Few investors are able to gear above 80%, and in most cases no more than 70% in the leading cities. It is closer to sub 60% in tier 2/3 cities unless additional mezzanine finance can be found. This provides a buffer against falling values on the debt side. Investors will still be exposed to falls on the equity side.

## Accessing product increasingly difficult

Our survey of investors highlights the issues facing investors in the wake of this wall of capital and overheating markets. In prime markets investors report that it is increasingly harder to source product at a global level (Figure 24). Compared with previous years, no investors reported accessing prime product as easy. For non-prime the situation is easier, however a small, but growing, number of investors report that accessing product is more difficult. These trends are repeated across each region. Markets have moved quickly into recovery phase. As a result a growing number of investors are finding it hard to source product given limited supply and strong competition. Thus what seemed achievable in fund raising, is now becoming harder in deployment, especially sourcing opportunities at the right return levels. Those adept at accessing product, and taking opportunities off-market will be winners.

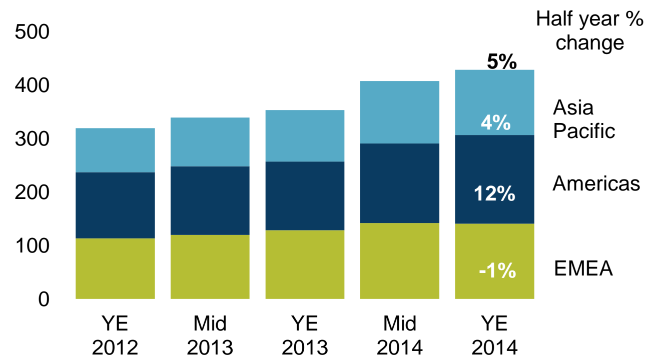
## Focus broadening from leading markets

The primary target for most investors (based on our survey) in each region is the larger and most highly transacted markets, though not necessarily most liquid. Across EMEA, the UK, Germany and France (Figure 25) are the primary targets, with Spain and Italy the next key targets. In fact as secondary targets, both Spain and Italy attract a similar level of investor interest as the UK and Germany, highlighting the increased attractiveness of these two markets today. Fewer are targeting the Nordics or Central and Eastern Europe (CEE). CEE markets remain more of a secondary target.

Japan, Australia and China are the main focus in Asia Pacific, accounting for around two-thirds of investor interest. Fewer are targeting Hong Kong or Singapore. Although Australia is the main secondary target, Singapore and South Korea are also more in favour, with limited interest elsewhere. Unsurprisingly the US is the main target for investors in the Americas, with over 70% of investors targeting this market. The US and Canada are the main secondary targets. With few mature markets in the region, these results are not surprising.

Figure 23

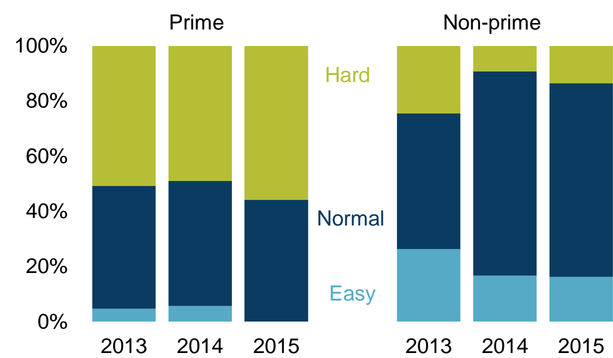
**Available new capital for investment, 2015, USD bn**




*Source: DTZ Research*

Figure 24

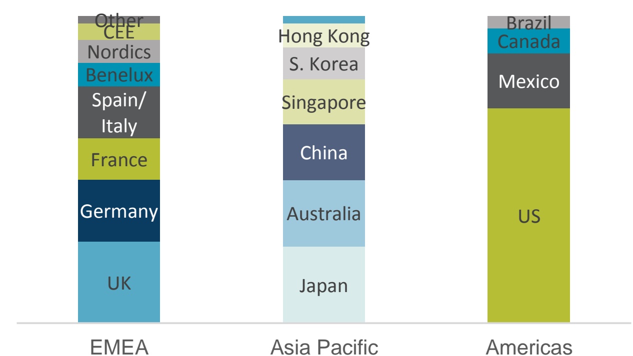
**Global buying opportunities**




*Source: DTZ Research*

Figure 25

**Primary target markets by region, 2015**




*Source: DTZ Research*

## Investors focus away from core

Typically less than a third of investors in each region are focussed on core. Most investors are moving further up the risk curve to core-plus or value-add (Figure 26). Typically fewer than 10% are opportunistic investors in primary markets. Perhaps not surprisingly, this level does increase in secondary markets. The only difference tends to be in the Americas where we see little variation in strategy. In Asia Pacific we do see more opportunistic capital in secondary targets, again a high proportion is still in major markets such as Australia, implying some restraint on the degree of risk they are willing to take. We observe similar trends in Europe.

## Investment to reach new record in 2015

The strong weight of capital will drive investment activity higher. The upward momentum in investment activity highlighted earlier will continue throughout this year with global investment activity expected to reach USD771bn (Figure 27). This is just short of the USD791bn record in 2007. However, regionally we see volumes surpassing their peak in North America this year, and also in Europe (in Euro equivalents). Asia Pacific volumes will remain close to their recent peak levels. We see the appetite for investment continuing into 2016 as the weight of capital to deploy remains strong and real estate still looks attractive to other assets in the low interest rate environment. We see more institutional investment targeting gateway cities, especially from Greater China, where the flows to date have just been the tip of the iceberg.

## Weight of capital clear and present risk

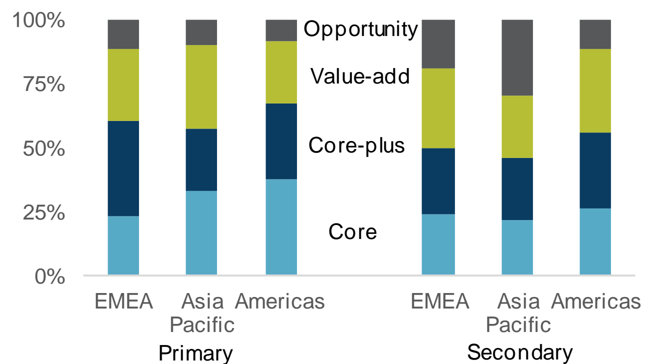
Weight of capital represents a clear and present risk for the market, driving a disconnect between pricing and fundamentals. Our survey highlights that a majority of investors (62%) perceive weight of capital and consequent overheating in the market to be a real risk (Figure 28). Interest rates will not remain this low forever. Whilst pricing can be justified at current rates, we would foresee greater risks if rates rise by 200bps, especially if yields compress even further, as they may do.

Lack of opportunities in core and record low yields is leading investors to target non-core opportunities. Investors need to move now whilst the window of opportunity remains as yields will compress quickly. Whilst we do not see major turbulence in the near term, rising interest rates could pose a risk. As rates rise we see the relative attractiveness of CRE diminishing. Whilst improved rental growth may offset some of the performance, higher required returns could lead to reversal of flows of new capital, especially that into retail (unlisted) funds.

Our earlier analysis highlighted how, amongst others, unlisted funds have recently grown in size through growing inflows of equity. Just as the flow of money can increase, so that flow can be reversed as investors seek to redeem their investments. This could have an impact for the market if funds are forced to sell assets expeditiously. Although these funds are active across the spectrum, we see relatively higher levels in non-gateway markets. These markets might be more exposed to a reversal in flows. Not all markets are in the same phase of the cycle globally, with opportunities available for those with a broad strategy. It is critical that investors focus on a market's fundamentals - demand, supply and income will be critical to minimise any risks.

Figure 26

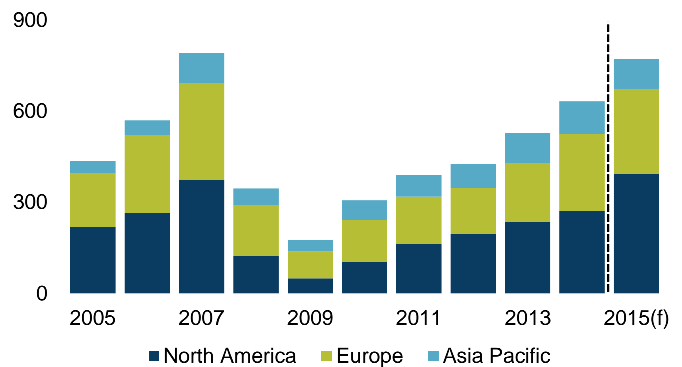
**Target investment style by region, 2015**




*Source: DTZ Research*

Figure 27

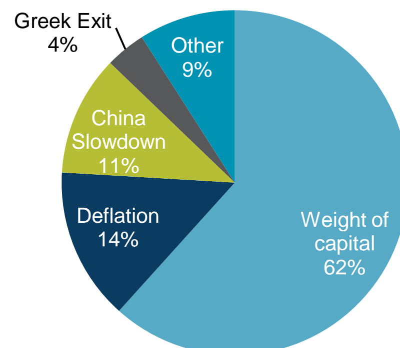
**Global investment volume forecasts, USD bn**




*Source: DTZ Research, Real Capital Analytics*

Figure 28

**Major risks to the market outlook**




*Source: DTZ Research*

## Definitions

*Invested stock*
The value of investment grade commercial real estate held by different investor groups. The total value of the real estate capital market is defined as the total volume of commercial real estate debt outstanding plus the total value of equity in commercial real estate holdings.

*Private Debt*
Total value of outstanding loans to the real estate sector that are not held in the form of listed financial securities. Loans granted and subsequently securitised prior to maturity are not included in this data. Private debt relates to the activity of all participants involved in the provision of commercial real estate loans including commercial banks and non-bank lenders such as institutional lenders, insurance companies and debt funds. The balance of the loan transfers to so called “bad banks” such as NAMA in Ireland and SAREB in Spain are also included in this category.

*Public Debt*
Total value of outstanding loans to the real estate sector held in the form of listed financial securities, i.e. property company corporate bonds, covered bonds with commercial property as collateral and commercial mortgage backed securities (CMBS).

*Private Equity*
The equity proportion of the commercial real estate holdings of insurance companies, pension funds, private property companies, high net worth individuals and unlisted property funds. The debt proportion has been stripped out by applying a different leverage ratio for each investor group.

*Public Equity*
The equity proportion of the commercial real estate holdings of listed property companies, REITs and other listed property vehicles. The debt proportion has been stripped out by applying a different leverage ratio for each investor group.

*Institution*
Refers to transactions and holdings where investor in commercial real estate is an insurance company or/and pension fund.

*Unlisted Fund*
Refers to transactions and holdings where investor is an unlisted property fund. In this category we include both open-ended and close-end funds as well as collective investment schemes under country specific legal framework such as OPCI and SPCI in France, Spezial and Open-ended funds in Germany, Portuguese unlisted funds (FIIs) and Unlisted REITS in the US.

*Listed Company*
Refers to transactions and holdings where investor in commercial real estate is a listed property company, REIT or other listed property vehicle.

*Inter-regional*
Refers to cross-border investors that invest outside their home region e.g. US capital invested in Europe.

*Intra-regional*
Refers to cross-border investors that invest in their home region e.g. UK capital invested in France.

*Domestic*
Refers to transactions where the buyer is sourcing capital from the country where the transaction took place e.g. UK capital invested in the UK.

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