M&G REAL ESTATE'S GLOBAL OUTLOOK REPORT FORECASTS CONTINUED UNCERTAINTY AS 'NEW NORMAL' FOR COMMERICAL REAL ESTATE

- ***Report reveals the impact of COVID-19 on real estate investment trends in the UK, Europe and Asia***
- ***Themes include uncertainty as the 'new normal' and adjusting existing business models to place climate action and social equality at their heart***

LONDON, 10 November 2020 – The impact of COVID-19 is significantly reshaping the way in which investors are thinking about the long-term future of the global real estate sector, according to the latest Global Outlook Report by a leading global financial solutions provider for real estate investors, M&G Real Estate.

The findings reveal how the pandemic is causing investors to grapple with significant, unforeseen economic upheavals and the major shifts in work/life balance, which may in time force investors to repurpose their assets. It also highlights the potential widening gap between sustainable and 'stranded' assets. Issues such as social equality and climate action are impacting business models more strongly than ever before, particularly with the aspirations of many governments to achieve net zero carbon emissions in the coming decades.

The report suggests that the world has moved towards an increasingly risk-off environment during 2020 to such an extent that uncertainty in the markets is becoming the 'new normal'. At the same time, as bond levels and interest rates remain low across the UK and Europe, real assets have emerged as the asset class best placed to offer a safe haven to multi-asset investors.

M&G's research acknowledges that while many economies have started to recover from the initial impact of the COVID-19 crisis, the speed and strength of that recovery is still heavily dependent on an effective implementation of a medical solution. The findings touch upon the challenges facing governments in striking a balance between managing the spread of COVID-19 in the short-term and reducing its longer-term underlying effects on societies and economies.

The relative success of many Asian markets in managing the pandemic – underpinned by robust fiscal and monetary support from governments - as well as better preparedness for a flu-style pandemic – has resulted in a generally softer economic impact than in Europe and positions the developed APAC economies for a faster recovery.

Jose Pellicer Head Investment Strategy at M&G Real Estate, **comments**: "2020 will be known as the 'year of the pandemic'. COVID-19 has affected economies and communities worldwide and the aftermath of such widespread impact requires a considered and targeted response.

"In many markets, the response to the virus has either accelerated or consolidated already established trends, such as an increasing acceptance of home working for those able to do so. Our attitudes towards future investment decisions must be guided by the new environment in which we are all operating and we must accept that a high level of uncertainty will continue for some time.

"We are already seeing growing momentum among investors who are keen to take a more proactive and considered investment approach in the real estate sector."

Other key findings include:

- Property yields across UK, European and Asian-Pacific markets currently reflect a record wide spread over bonds and are likely to attract multi-asset class investors;

- A 'flight to quality' is being driven by investors seeking 'safe haven' investments, prompting an increased demand for prime office assets in core markets of major European cities. The big 7 **German office markets** are currently proving to be particularly attractive to investors. Persistently low vacancy rates (Munich and Berlin circa 2% and circa 3% for the other markets) and a restricted supply of new stock should insulate the sector from a cyclical downturn in demand, however, the long-term health of the sector is dependent on its ability to adapt to new ways of agile working. The Amsterdam, Stockholm and Paris central business districts are also proving resilient thanks to their front office locations and connectivity, which help with client facing activity and talent retention;

- Continuing Brexit uncertainty has allowed investors to take advantage of a higher property risk premium for **UK property** – especially in the office sector – than is reflected in other European markets. Despite the potential uncertainty around the future role of offices, the report forecasts sustained demand for office space in key employment hubs, particularly those offering amenities which encourage productivity and collaboration and support wellbeing. although cultural differences mean this will vary across regions. There is mounting evidence of a softening of attitudes towards remote working in Asia which may affect future demand for office space;

- The decision of **Nordic governments** to pursue a strategy of early or less restrictive lockdown means that their economies are more potentially more likely to recover and grow at a faster rate than those of other major European economies, particularly as they entered the pandemic with a fiscal surplus - Nordic markets only saw a decline of -6% GDP in Q2 versus -12% in the Eurozone. The Swedish Krona (SEK) has been one of the best performing G10 currencies since lockdowns began, up 10% against the Euro (as of 09/11/20).
- The **residential sector** has demonstrated its resilience during the pandemic across most markets due to a shortage in housing stock, particularly in the UK and in key European cities such as Amsterdam, which has a shortfall of circa 300,000 homes, most keenly felt in the Amsterdam and Utrecht regions. In a new era of heightened uncertainty, residential is seen as a defensive play that is less sensitive to economic downturns. The research highlights the symbiotic relationship between office and residential, as living spaces best configured for home working are more likely to be sought after in the current market;

- The **logistics sector** has held up extremely well, benefiting from the huge rise in e-commerce, particularly in societies where tight restrictions have been placed on in-store shopping and demand for fast and reliable home delivery has escalated. In the UK, undersupplied logistics markets near to end-consumers in areas such as the South East and around London, have experienced some of the biggest business upturns during 2020. Across Asia, e-commerce growth has amplified the undersupply of prime modern logistics facilities across select markets and the need for further investment in this sector.

- **Bricks and mortar retail** needs to offer convenience or experiences that shoppers cannot access online, while offices must continue to offer what home working does not provide, specifically places to collaborate and reinforce a company's values and culture. Some suburban retail centres in Asia have even bucked the retail property trend throughout the crisis, helped by local travel restrictions requiring shoppers to remain bound to their local areas.

The report suggests that a widespread acceptance of flexible working in many societies is set to be one of the pandemic's lasting legacies. **Germany** is leading Europe's return to the office and **Asian markets** have witnessed a rapid return to the workplace – driven by a business culture founded on the importance of face-to-face relationship-building and constraints on home space. However, the report highlights significant support for long-term flexible working compared with the pre-pandemic situation. This, in turn, will impact on future demand for commercial space in those markets.

The findings reveal that a symbiosis between office and home working is not necessarily detrimental to the office market. In **Sweden and The Netherlands,** for example, both of which had well-established flexible working patterns prior to COVID-19, rents in key cities such as **Stockholm and Amsterdam** have continued to grow before and during the pandemic. Rental levels in Amsterdam's central markets have continued to climb by more than 30% in the last 5 years.

Pellicer continues: "We need to question the fundamental role that real estate plays for its occupiers. Certain trends that were already in play prior to COVID-19 have been accelerated by lockdown in many countries, including a sharp rise in online shopping and increased flexibility in working patterns. Flexible working has prompted a fresh take on how and where we live, with a greater demand for spaces that encourage productivity and social interaction.

"Irrespective of all the change that has taken place in such a short space of time, real estate must continue to be relevant to the needs of occupiers by offering a built environment which impacts positively on their health and wellbeing, as well as being environmentally responsible and sustainable."

Link to M&G's global outlook report: https://m-and-g.preview.ceros.com/global-real-estate-outlook/page/page-5f7d8f2871299

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For nearly nine decades M&G Investments has been helping its customers to prosper by putting investments to work, which in turn creates jobs, homes and vital infrastructure in the real economy. Its investment solutions span equities, fixed income, multi asset, cash, private debt, infrastructure and real estate.

M&G recognises the importance of responsible investing and is a signatory to the United Nations Principles for Responsible Investment (UNPRI) and is a member of the Climate Bonds Initiative Partners Programme.

Its £33.7 billion property arm (as at 30 June 2020 including cash), M&G Real Estate, is a leading financial solutions provider for global real estate investors, has a sector leading approach to responsible property management and is committed to continuously improving the sustainability performance of its funds.

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