

Baltics Investment, H2 2019

High European investor activity leads investment market over EUR 1.2 bln



Investment Vol
EUR 744 mln (EUR 1.2 bln annual)



Prm Office Yield
5.80-6.20%



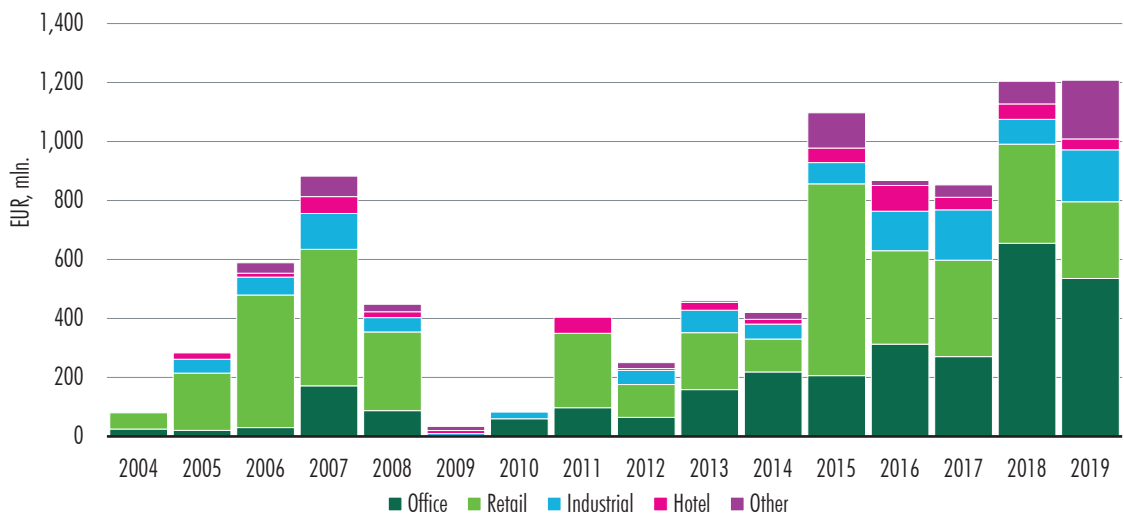
Prm S/C Retail Yield
6.25-6.75%



Prm Logistics Yield
7.25%

*Arrows indicate change from the corresponding period of previous year

Figure 1: Investment volume by sector, 2004 - 2019



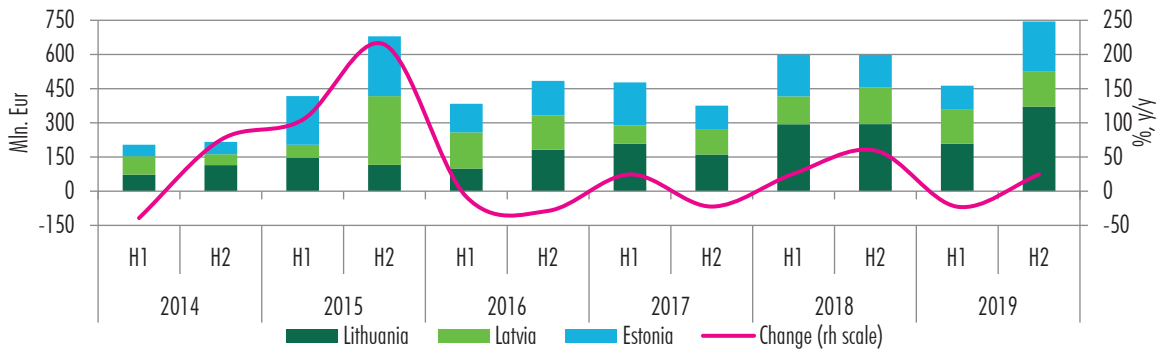
Source: CBRE Baltics; 2020

KEY POINTS

- In H2 2019 GDP increased within the 2.5-4.2% y/y range in the Baltics. The projections for future growth broadly remain at above 2.5% in 2020 and 2021¹. The ongoing Covid-19 pandemic will have negative economic impact.
- Annual investment volume surpassed EUR 1.2 bln for a second consecutive year.
- The pace in the Baltics' investment market has increased. In H2 2019, total investment volume reached EUR 744 mln and was 24% higher compared to the same period a year ago.
- The largest transaction of the year was the Quadrum business centre project acquisition in Vilnius by German institutional investor from Schage Real Estate for ca. EUR 156 mln at a yield below 6%.
- Intermediate Capital Group (ICG) acquired the Raadiku municipal housing scheme in Tallinn from LCN Capital Partners for EUR 144 mln at 6.2% yield.
- Austrian Vienna Insurance Group concluded a transaction by buying a part of Baltic Re Group's office and retail properties in Riga's historical centre for EUR 59 mln.
- Investment in the industrial sector constituted 12% of the total investment market in the second half of the year (15% 2019).
- Investment market is getting broader and deeper, attracting new entrants such as Vienna Insurance Group (VIG), ICG, Kildare (2018), Nepi Rockcastle (2018) and others who deploy capital from institutional investors.
- Deka Immobilien who had paused the Baltics for more than 10 years, started investing in a new asset class – offices.

¹Macroeconomic forecasts obtained before 31st January 2020

Figure 2: Investment Volume by Country 2014-H2 2019, Semi-Annual



Source: CBRE Baltics; 2020

ECONOMY

There were signs of a somewhat slowing economic growth pace in the Baltic states at the end of 2019, although GDP growth both in Lithuania and Estonia was among the highest in the Eurozone. In 2019 GDP growth in the Baltic countries increased within the 2.5-4.2% range y/y. However, the ongoing Covid-19 pandemic will have negative economic impact.

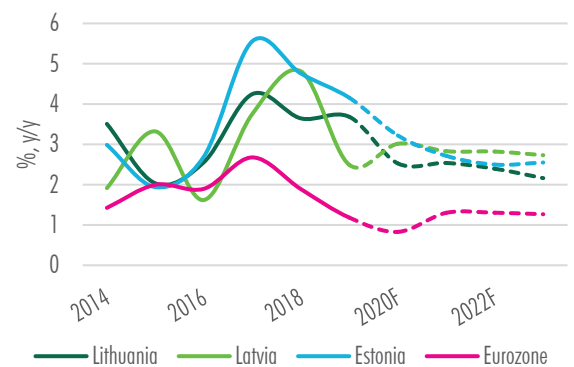
The growth was supported by the robust performance of other economic indicators. At the end of 2019, the average inflation rate in the Baltics ranged between 2.3% and 2.9%. In Lithuania and Estonia, the inflation rate has decreased and remains just above the targeted 2% level. Price growth in all Baltic countries is mainly supported by continuous salary growth. The labour market in Baltic states has been tightening for the past few years. At the end of 2019 the unemployment rate in Estonia stood at a surprisingly low 4.4%. Latvian and Lithuanian unemployment rates were below the Eurozone average, respectively 6.9% and 6.4%.

Bank lending in the Baltic region remains limited. At the end of 2019, the average cost of borrowing for businesses increased in the Baltic states and currently stands at 2.7% - 3.2%, while at the same time it slightly dropped in the Euro area. Market concentration among a few banks and low competition is one of the reasons behind it.

INVESTMENT MARKET

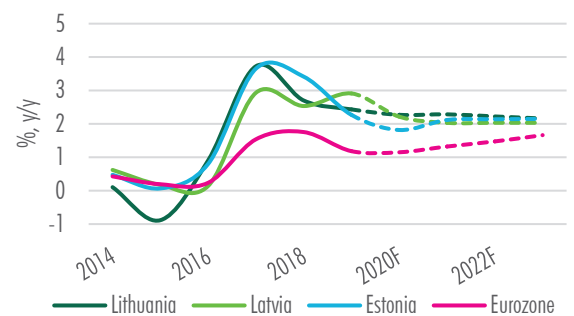
Despite a high degree of uncertainty, especially regarding Brexit effects, US trade tariffs targeting Europe and overall economic concerns, investment activity in the Baltic region remained at a historic high. In 2019 more than 130 investment transactions were signed with a total volume for the second consecutive year of more than EUR 1.2 bln.

Figure 3: GDP growth and forecast



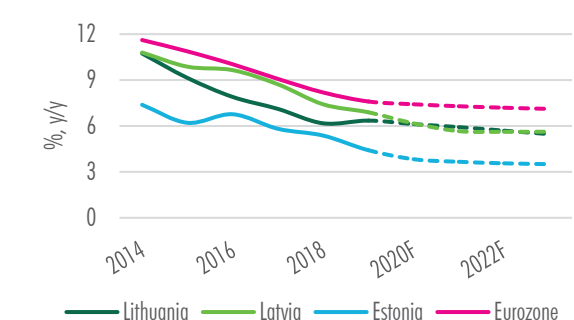
Source: Oxford Economics, CBRE Baltics, 2020

Figure 4: Inflation rate by country



Source: Oxford Economics, CBRE Baltics, 2020

Figure 5: Unemployment rate by country



Source: Oxford Economics, CBRE Baltics, 2020

The second half of the year was marked by especially vigorous activity, which reached the record high semi-annual result. Total investment volume touched EUR 744 mln and was 24% higher compared to the same period in 2018. Investment volume in Lithuania accounted for 50% of total Baltic transactions in terms of value and recorded the highest investment activity in Lithuania in the past ten years. Estonia showed strong competition and mainly due to one large transaction reached the highest result since H2 2015. The Latvian market remained in line with H1 2019.

In terms of origin, some investment came from Baltic investors already present in the market, mainly investment funds. In 2019, it was observed that the majority of investment volume was coming from European (excl. Baltic and Nordic) investors, there were 16 transactions with a total value of EUR 484 mln. Baltic investors followed it with EUR 390 mln, and Nordic investors above EUR 300 mln, which could be a continuous trend in upcoming years. High investment volumes and attractive yields are appealing not only Baltic and Nordic investors, but 2019 was also marked by growing global investor interest, which concluded in increasing number of transactions and total investment volume.

In 2019, the office sector, as in previous periods, was dominant in the investment market accounting 44% of all transactions. It was followed by the retail (22%) and industrial sectors (15%). Unusually, the private rental sector (PRS) accounted for 13% because of significant single transaction. The Estonian market observed a EUR 144 mln sale of 9 residential buildings with a total of 1,215 apartments and 5 storey parking facility, all complex leased to Tallinn municipality with a long-term contract. It was the third largest transaction of the year.

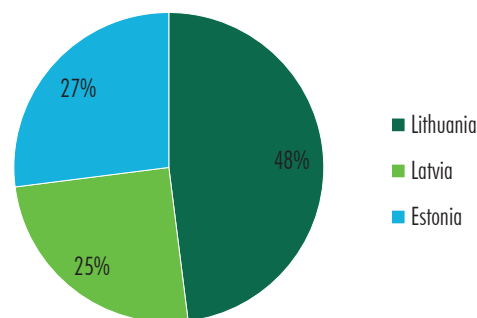
OFFICES H2 2019

The office market, as usual, showed strong confidence with 46% of total investment market transactions during the second half of the year, with major transactions carried out in all three Baltic states.

Notable deals in H2 2019 included the Quadrum BC transaction in Vilnius, where the German Deka Immobilien Investment acquired it from Norwegian owned Schage Real Estate for ca. EUR 156 mln at a below 6% yield.

VIG entered the market at the end of the year acquiring part of the Baltic RE group portfolio in Riga. The transaction included three mainly office buildings with minor street retail in the historic centre of Riga.

Figure 6: Investment Volume by Country, 2019



Source: CBRE Baltics; 2020

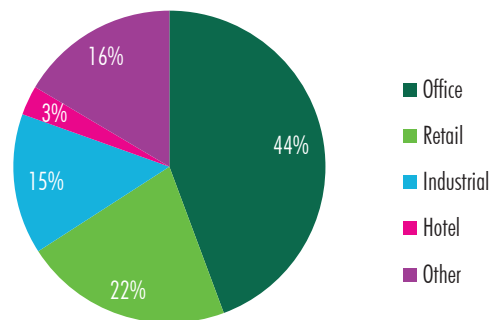
Figure 7: Investors origin by region | Baltics 2018-2019

Region	2019	2018
Baltic	↓33%	54%
Europe*	↑40%	25%
Nordic	↑27%	10%
Other	↓0,5%	11%
Total	100%	100%

Note: Europe excluding Baltics and Nordics.

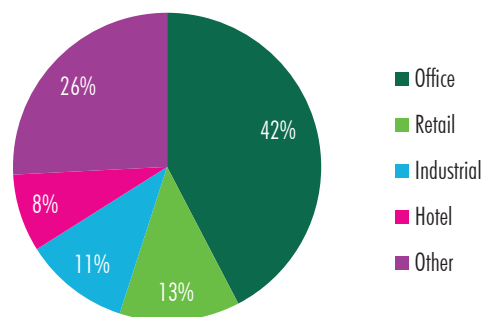
Source: CBRE Research, 2020

Figure 8: Investment volumes by sector in Baltics, 2019



Source: CBRE Baltics, 2020

Figure 9: Investment volumes by sector in Europe, 2019



Source: CBRE Research, 2020

The total transaction value was ca. EUR 59 mln. Among other noteworthy transactions were the Capital Mill sale of Valdemara Centre's office building in Riga for EUR 24 mln to Eastnine investment fund. Also, Collonna Kinnisvara bought the Luminor HQ in Riga.

Overall, modern offices with quality tenants remain a desirable investment, and there is a downward yield pressure across all three countries from the current 5.8%-6.2% level.

RETAIL H2 2019

During the second half of the year, investments in retail increased by 34% compared to the same period in 2018, yet the moderate first half of the year resulted in overall lower activity in 2019. Low retail investment activity in the Baltics is in line with the rest of Europe, as investors wait for retailers to adjust to the structural shift of e-commerce and changing shopping habits of consumers. While the multitenancy retail experiences major transformation, some retail submarkets show resilience in the eyes of both developers and investors: among them – financially and commercially sound big-box formats, shopping galleries in the city centres, retail in transit locations, retail as part of mixed-use, as well as the usual «bread and butter» formats driven by supermarket and convenience sector.

Two significant sale-and-leaseback transactions were recorded during the H2 2019 both in Lithuania. Two DEPO DIY stores were sold to French asset managers Corum with a total transaction value of EUR 53.6 mln. The current yield level (SC) at 6.25-6.75% remains stable, somewhat opposing the trend of weakening yields on the pan-European level.

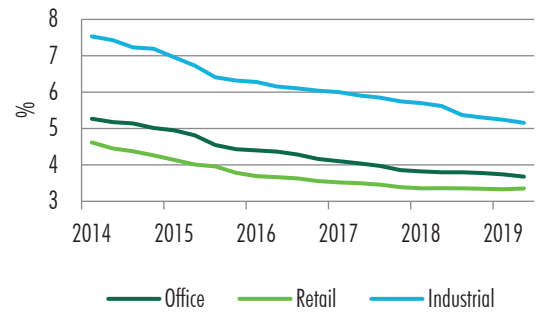
INDUSTRIAL

After impressive results in H1 2019, the industrial investment market levelled at the end of the year. Overall annual investment activity in the sector increased more than twofold. In H2 2019, the most notable transaction was executed in Latvia, where development company Pitche sold The Airport Park logistics centre near to Riga airport to East Capital Baltic Property Fund for EUR 19 mln.

Industrial yields have moved downward, with continuing yield compression. Currently, a prime warehouse yield stands at 7.25% across all three states.

The structural shift in retail is transforming the industrial sector as well. It is expected that the

Figure 10: Eurozone yields, 2014 - 2019



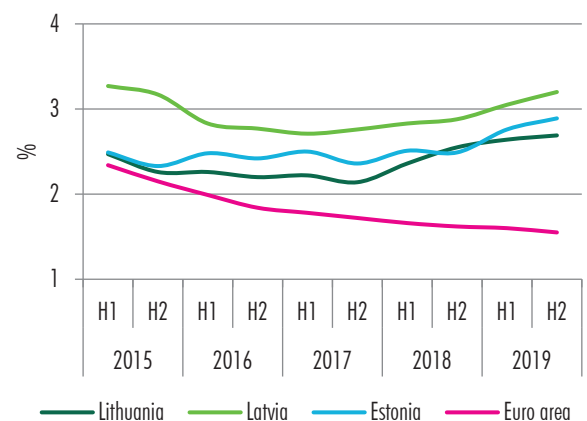
Source: CBRE Research, 2020

Figure 11: Yields in H2 2019 in selected Eurozone countries and change in direction compared to the previous period

Prime	Offices	Retail S/C	Industrial
Lithuania	5.80	6.50	↓7.25
Latvia	6.20	6.50	↓7.25
Estonia	↓6.00	6.00	↓7.25
Austria	↓3.45	↓3.10	↓5.00
Belgium	↓3.90	↓3.50	4.75
Finland	↓3.25	↓4.60	↓4.75
France	↓2.85	↓2.75	↓4.00
Germany	↓2.70	↓2.70	↓3.60
Greece	↓5.75	↓5.75	9.00
Ireland	4.00	↓2.50	5.10
Italy	↓3.30	↓3.00	↓5.20
Netherlands	↓3.00	↓3.10	↓4.00
Portugal	↓4.00	↓4.00	↓6.25
Slovakia	↓5.60	N/A	↓6.25
Spain	↓3.25	↓3.25	↓5.00

Source: CBRE Research, 2020

Figure 12: Cost of Borrowing for Non-Financial Corporations



Source: European Central Bank, CBRE Baltics; 2020

demand for modern industrial properties will grow and yields will shrink even more. Investment should also increase as properties are actively developed in all countries, including multiple built to suit schemes.

EUROPEAN INVESTMENT ACTIVITY

In H2 2019, investment activity in Europe was the highest in the past decade, with strong confidence in all investment sectors, except for retail (due to ongoing retail sector re-development and the changing environment in traditional retail influenced by the growing e-commerce sector). Commercial real estate investment in Europe (excl. Russia) showed semi-annual growth of 11% y/y. Together with increasing activity in European markets, European investors showed significant interest in the Baltic market surpassing local investor investment volumes in 2019. During H2 2019, 40% of all Baltic purchases were by investors from core European markets.

OUTLOOK

CBRE Baltics expects that during the next few years investment activity in the Baltic region will continue to increase in investment volumes with further yield

compression. One of the stimulating factors for further increase in investment volume increase will be low interest rates that are set to be lower for longer.

Furthermore, the Baltic investment market should witness more institutional newcomers during the next few years. There are expectations that interest from European and Global banking sectors will materialize into additional capital for real estate lending. Global real estate investors and companies outside the traditional real estate industry with available capital already are monitoring the Baltic region.

Local investors are widening their interest criteria, and CBRE Baltics can already see increasing activity in alternative sectors such as student housing and residential markets.

CBRE expects COVID-19 to have a negative short-term and medium-term effect on the commercial real estate market in Europe, provided the outbreak is brought under control in a reasonable timeframe.

Figure 13: Investment transactions | Baltics 2019

No.	Property	Sector	Country	Investor	Vendor
1	Quadrum BC	Office	Lithuania	Deka Immobilien Investment	Schage Real Estate
2	Raadiku municipal housing	Residential	Estonia	ICG	LCN Capital Partners
3	S7 (I-III stages)	Office	Lithuania	Eastnine	Galio group
4	Galerija Centrs SC	Retail	Latvia	Baltic Horizon Fund	Linstow
5	Kalku 15, Kalku 12, Brivibas 21 (portfolio)	Office	Latvia	Vienna Insurance Group	Baltic RE Group
6	Luminor HQ	Office	Latvia	Collonna	Luminor, Blackstone
7	Harmet modular houses	Industrial	Estonia	Corum	ITT Capital
8	Depo Kaunas	Retail	Lithuania	Corum	Depo
9	Vakaru Medienos Grupe	Industrial	Lithuania	DIRE Fund	Vakaru Medienos Grupe
10	Depo Ukmerges	Retail	Lithuania	Corum	Depo

Source: CBRE Research, 2020

RESEARCH DEFINITIONS

Sellers' Market - a market situation where sellers are outnumbered by buyers by a big margin and the quantity of income generating commercial properties available for sale becomes far less than the quantity demanded. As a result, sellers are able to increase the prices and obtain better sale conditions and the situation becomes favourable for sellers.

Prime Yield – represents the net yield that an investor would receive when acquiring a class A building in a prime location (for an office in the CBD, for example), which is fully let at current market value rents. Prime Yield should reflect the level at which relevant transactions are being completed in the market at the time but need not be exactly identical to any of them, particularly if deal flow is very limited or made up of unusual one-off deals. If there are no relevant transactions during the survey period, a hypothetical yield should be quoted, and is not a calculation based on particular transactions, but it is an expert opinion formed in the light of market conditions, but the same criteria on building location and specification still apply.

Transaction Count – the number of single investment transactions in the Baltic region during the research period; portfolio transactions across the Baltic region are counted as one transaction. The transaction count may differ if counted for each country separately - in that case a portfolio transaction could be divided by the number of properties located in each country.

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- Part of the **CBRE** Affiliate Network
- Offices in Riga, Vilnius and Tallinn
- Providing services in:
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 - **Consulting,**
 - **Valuation,**
 - **Property Sales,**
 - **Property & Asset Management,**
 - **Tenant Representation,**
 - **Agency Services – Retail, Offices, Industrial & Logistics,**
 - **Financial Services, Accountancy**
 - **Landlord/Investor Representation,**
 - **Transaction Management**

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