Research
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Global Real Estate Perspective - Highlights

Investor and Corporate

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Overview

Market conditions stabilizing but set to remain challenging into 2024

The challenges facing the global economy continue as we approach the end of 2023, from a still high but falling rate of inflation, to monetary tightening by many of the major central banks, to signs of slowing in labor markets. Cyclical and structural uncertainty are weighing on occupier demand as companies review their portfolios and take longer to make decisions, while the high cost of capital and conservative underwriting from investors are slowing capital flows.

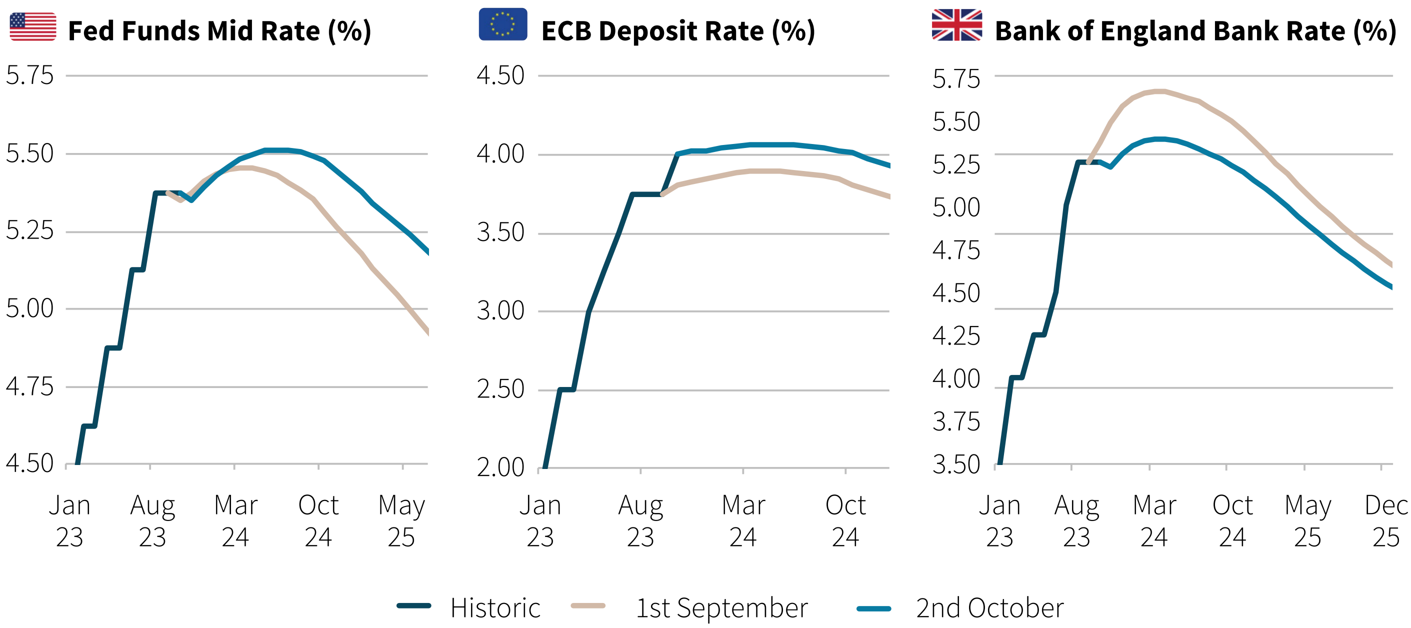
Global Capital Flows

Interest rates

Higher rates and recession risk will shape investment through next year

Market uncertainty was sustained through Q3 amid mixed economic data and shifts to the rate outlook. The fluid economic climate continues to influence central banks, and market consensus indicates that rates are now expected to hold steady through the end of the year, with the Federal Reserve, European Central Bank and Bank of England unlikely to cut rates until the second half of 2024. Expectations for the capital markets have been tempered heading into year-end 2023 and 2024, with momentum likely to build through next year. The pathway to market recovery is anticipated to be uneven, and as we navigate the end of the year, the gradual return of predictability will be critical to stabilizing valuations and unleashing liquidity. However, if volatility persists or recessionary risk worsens, their duration and extent will further impact pricing and the timing for a market recovery.

Financial markets' forward expectations of policy rates, 2023 – 2025



Source: Refinitiv. *Derived from OIS forward curves.

Debt markets

Cost of debt continues to inhibit transaction activity

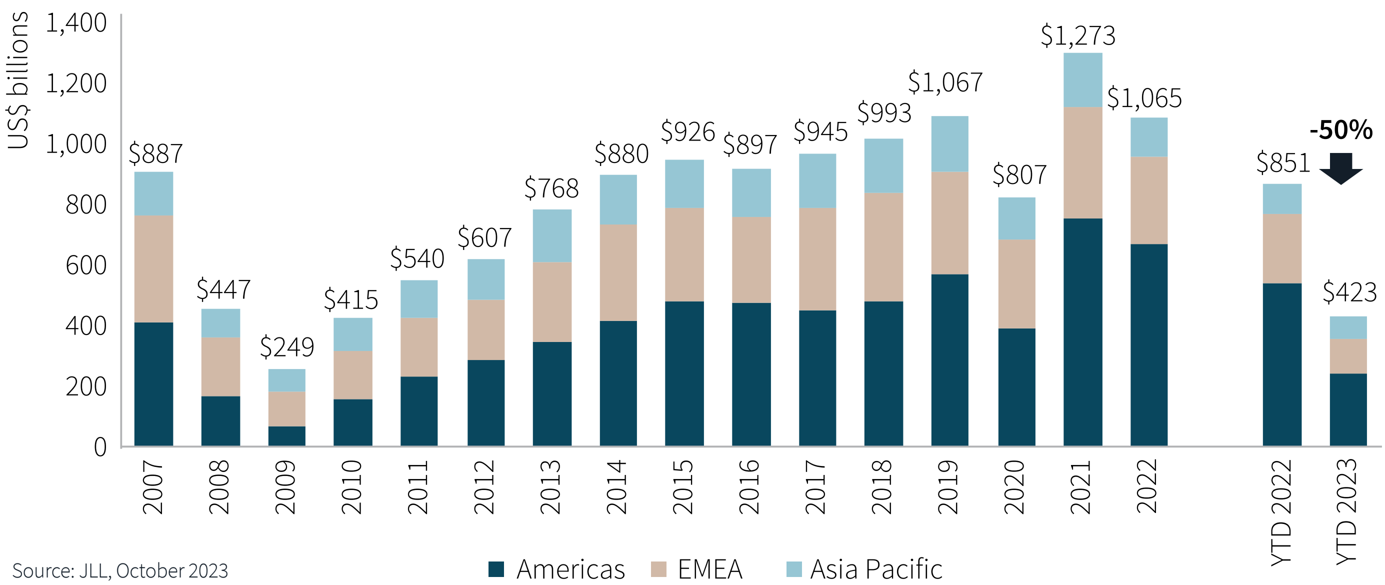
The rising costs of debt and volatility in indices are influencing lender sentiment and market dynamics globally. In the U.S., investor sentiment has been impacted by the run-up in government bond yields since the summer, with the 10-year Treasury most recently hitting its highest level since 2007. Shifts in lending costs have now firmly taken hold in most markets outside of the United States. Despite volatility in lending costs in most countries globally, debt markets continue to be liquid and the availability of credit is solid, albeit at an elevated cost of capital. Loan originations continue to be balanced and diversified across lender types, and alternative lenders are emerging and seeking to provide financing solutions throughout the capital stack. While cautious sentiment around the banking sector persists in the U.S., larger banks are selectively active again in the market.

Pricing

Bid intensity plateauing amid renewed pricing pressures

Price discovery has paralleled continued improvements in bid intensity since the start of the year. However, amid higher rates, gains in average bid counts have levelled off in recent months and the bid-ask spread is holding steady. Asset prices have undergone significant adjustments as a result of shifts in the economy, rates and lending markets. The U.S. is furthest along in its price adjustments, with values down significantly from peak levels. In Europe and Asia Pacific, valuations are now shifting across most sectors and markets. Pricing and liquidity dynamics have been most resilient globally in the logistics and living/multi-housing sectors and for the highest-quality assets. We expect the unevenness across property sectors and markets to be pronounced, particularly as less-liquid market segments become more active.

Direct investment by region, 2007 – YTD 2023



Source: JLL, October 2023

Investment activity
Pace of capital formation and transactions strained by higher cost of capital

The rising cost of capital and conservative underwriting are subduing the pace of transaction closings. Fundraising is more challenging in the current climate as investors put additional allocations to the asset class on hold until denominator effect uncertainty subsides. Direct investment declined globally during Q3, down 46% year-over-year to US$131 billion. This brought year-to-date volumes to US$423 billion, reflecting a decrease of 50% and the lowest level of direct investment in over a decade. Cross-border investment trended similarly, down by 56% year-to-date and representing the lowest share of cross-border investment on record.

Sector dynamics
Property sector bifurcation persists

While all major sectors experienced notable declines during the third quarter, sectoral outlooks in the short and long term are varied, as sentiment and performance across property sectors remain bifurcated. The living sector continues to be the most active globally year-to-date, although fundamentals are more muted and settling around long-term averages. Investor sentiment for logistics is still positive despite cooling fundamentals in the near term and volumes contracting globally by 40% year-to-date, and markets in the sector have repriced quickly. Office pricing and liquidity continue to be under pressure amid weak global sentiment from investors and lenders. Fundamentals across the regions reflect the increasing polarization in performance between the highest-quality assets and the rest of the sector. The uncertainty of future demand persists given the state of the economy and adoption of hybrid work policies, and investors and lenders alike are focused on existing office exposure.

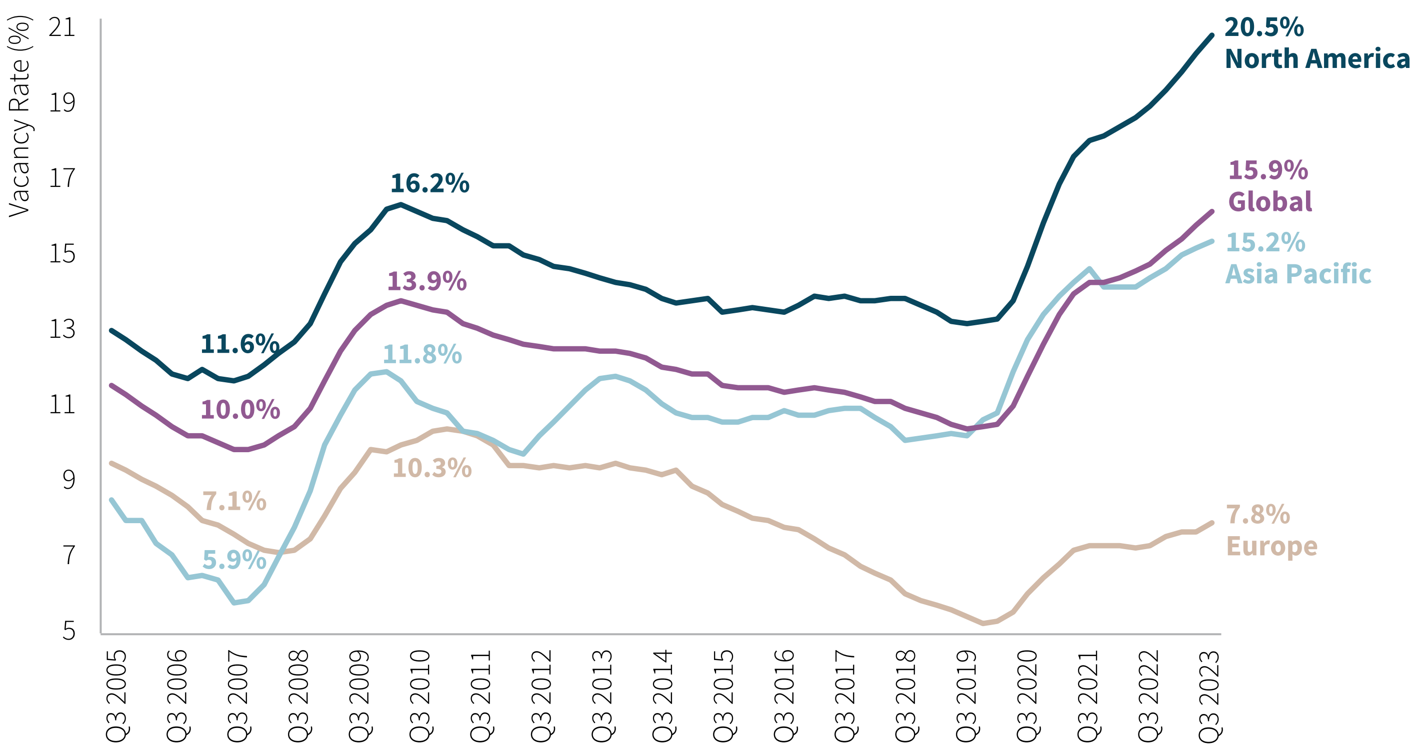
Property Sectors

Offices

Structural and cyclical uncertainty weighs on activity

The effects of heightened uncertainty around the economy, interest rates and working patterns continued to be felt in the office sector during the third quarter, particularly in markets where the cumulative impact of significant policy rate cycles is still building. Global office leasing volumes in Q3 were level with Q2, but 6% lower year-over-year and 24% below the pre-pandemic Q3 average. The regions recorded mixed results, with take-up in Asia Pacific 19% above Q3 2022, while year-over-year leasing activity fell by 15% in Europe and 12% in the United States. Occupancy losses increased from -0.1 million to -1.4 million square meters as net absorption in Asia Pacific was offset by declines in North America and Europe.

Global and regional vacancy rates, Q3 2005 – Q3 2023



66 markets in the U.S. and Canada, 23 markets in Europe, 25 markets in Asia Pacific. Grade A space vacancy only for Asian markets

Source: JLL, October 2023

The global vacancy rate in Q3 rose another 35bps to a new all-time high of 15.9%, with the largest increase recorded in North America (+47bps), followed by Europe (+20bps) and Asia Pacific (+14bps). Project delays have now pushed the peak of the current development cycle out to 2024; there are over 16.7 million square meters set to complete globally this year, with a nearly identical total in 2024. New groundbreakings have already fallen sharply in North America, while the pipeline is set to continue climbing into 2024 in Asia Pacific, and through 2025 in Europe. Completing projects will push up vacancy over the rest of 2023 and into next year, but resilient demand for new and refurbished space is likely to result in a growing shortage of suitable new supply as the pipeline reduces from 2025 onwards.

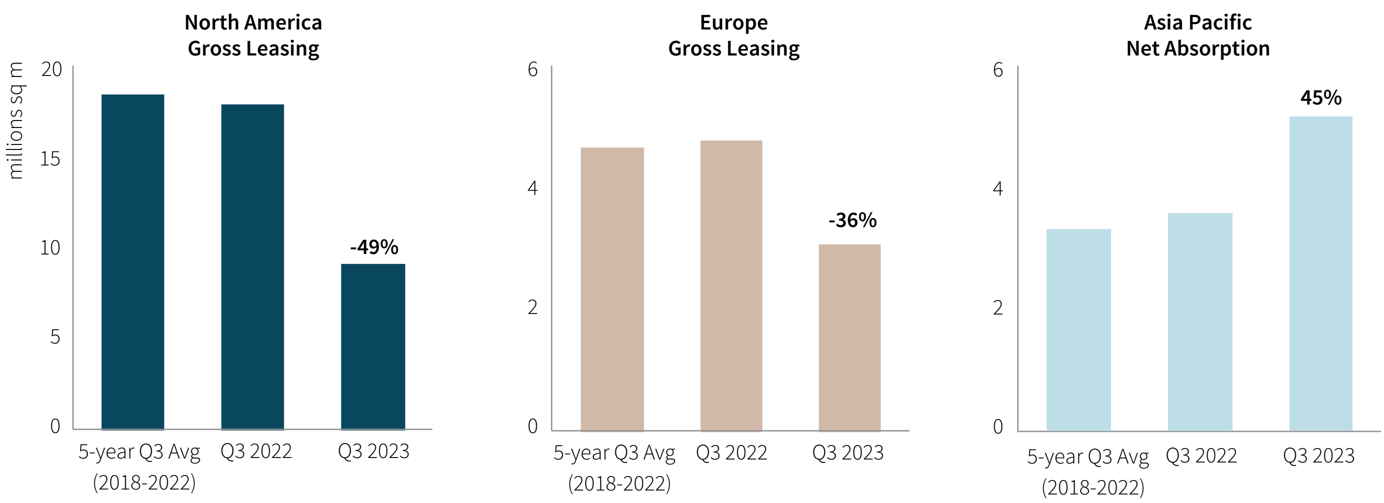
Logistics

Logistics activity squeezed by slowing economy

Activity in the logistics sector moderated further in North America and Europe during the third quarter, with longer decision-making as occupiers reassessed portfolios. Demand was more resilient in Asia Pacific as a wave of new supply boosted take-up above last year's levels. Construction is at record levels in North America and Asia Pacific, but new groundbreakings are declining due to rising construction and financing costs. Rents continue to increase globally, although at slower rates than the peak levels seen over the last two years, climbing by 14.9% year-over-year in North America and by 10.8% in Europe and with several Asia Pacific markets registering further gains.

Leasing volumes are expected to continue compressing into 2024 as occupiers weigh all viable options for their operations. As demand slows, vacancy rates across all three global regions will increase, with the U.S. experiencing a noticeable uptick due to deliveries slated for the duration of 2024. Rising geopolitical tensions, more protectionist industrial policies and the increasing cost of energy will encourage more nearshoring of operations.

Regional logistics demand, Q3 2022 and Q3 2023



North America: based on 55 city markets in the U.S. and 9 city markets in Canada; Europe: based on France, Germany, Netherlands, Poland and UK; Asia Pacific: based on Beijing, Shanghai, Hong Kong, Tokyo, Singapore and Seoul.

Source: JLL, October 2023

Retail

Solid leasing activity in many major retail destinations

Footfall and retailer sales have continued to increase in many dominant retail places around the world, supported by the recovery in international travel and softening but still-resilient labor markets. Sentiment improved over the third quarter in many locations across Asia Pacific on the back of higher tourism, which also contributed to a recovery in footfall to pre-pandemic levels in several markets across Europe. Net absorption also remains positive in the U.S. despite vacancy reducing to record lows.

Dominant retail cities and spaces have maintained their stronger performance as recovery lags in secondary locations. Financial results have become more mixed among major retailers as consumers continue to be selective in their purchases, with value operators and luxury firms standing out, while mid-market retailers face more challenging conditions. The strength of consumer demand will be tested over the next several quarters as economic growth slows in mature markets including the U.S., but falling inflation should support real wage growth and a moderate increase in global consumption through 2024.

Living

Rising interest in alternative living sectors as investors diversify

Strong demographic drivers and uncertainty in global investment markets are benefitting relatively higher-yielding alternative living classes such as purpose-built student accommodation and healthcare housing, as investors allocate a growing share of capital to these subsectors. The importance of a university education as an employment differentiator has perhaps never been higher than in the current age of artificial intelligence, while the world's ageing population continues to drive the need for more age-related housing solutions.

The U.S. living sector saw varied performance in Q3, with deal flow slowing to US$22.5 billion, the lowest quarterly total since Q1 2020 and the onset of the Covid pandemic. Student housing and single-family rental (SFR) continue to attract a range of new capital; 59% of all buyers of U.S. student housing in 2023 are new entrants into the space. Investment into student housing and healthcare accounted for over half of regional Q3 living volumes in Europe, up from a quarter of investment during Q2. The living sector was the second largest for Europe during the quarter, behind offices, with year-to-date investment volumes for the two sectors neck and neck. In Asia Pacific, living volumes totaled US$1.3 billion in Q3, rising 61% year-over-year from a low base. We expect transactional activity in the Asia Pacific living sector to accelerate in 2024 as developments start to reach completion and investors become more comfortable with underwriting investments in the sector.

Hotels & hospitality

Performance remains elevated but growth is slowing

Global Revenue per Available Room (RevPAR) increased by 10.2% relative to 2019 levels through the first eight months of 2023. Almost all regions are now fully recovered to pre-pandemic rates with Europe leading the way, followed by the Middle East and the Americas. Asia Pacific has yet to fully return to historic levels, although performance has rebounded since the reopening of China earlier this year. Urban market performance is expected to accelerate as group, corporate and international travel reemerge; conversely, resort activity will likely contract, leading to some stabilization in broader global performance over the coming months.

EMEA continues to see strong inbound travel and stands as the top-performing region worldwide. While demand has begun to normalize across some resort-heavy markets, urban performance has skyrocketed with many cities generating historically high RevPAR. Resort markets have also seen demand soften in the Americas as RevPAR growth decelerated for the first time in nearly three years, although urban travel continues to pick up pace. Intraregional tourism within Asia Pacific has surged following China's reopening in January 2023, which has resulted in RevPAR reaching a 94% recovery relative to 2019. Now that outbound Chinese travel has no remaining restrictions, we anticipate that the region's performance will accelerate further.

To find out how we can support your global real estate market strategy with research insights and strategic advice, please contact one of the members of the global research team.

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