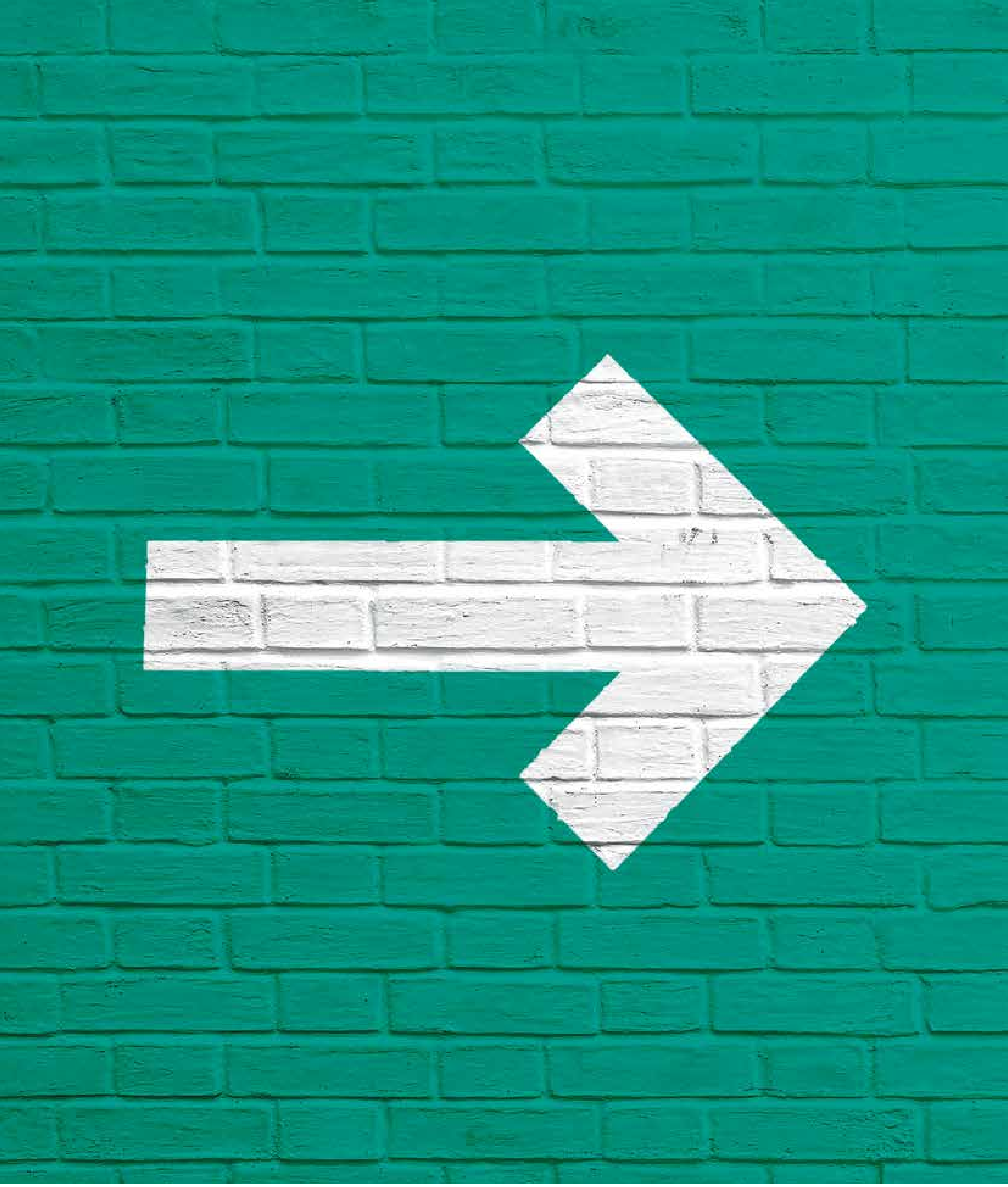


gesvalt®

2021 Real Estate Trends

General Situation

At the end of a year marked by the health and economic consequences derived from the pandemic, we are facing the beginning of massive vaccination worldwide. The speed of recovery in the economic scenario will depend on how fast and effective this process is. On the other hand, the increasing number of cases after the mid-year months and restrictions on mobility and activity in many countries that had completed their de-escalation led to higher uncertainty in Q4 2020. These two circumstances define the current projections, since they will be those marking the evolution of the main economic indicators during the next year.

Based on the analysis of end Q3 2020 data, it is observed that the year-on-year decline in our economy moderates to -8.7%, after the -21.5% drop recorded in Q2 2020. In quarter-on-quarter terms, the variation in GDP in Q3 was +16.7%, the highest increase in the series since data started to be recorded. This is due to the rebound after the fall in the previous quarter, marked by restrictions.

The latest growth projection update published by the Bank of Spain (BdE), dated June 2020, envisages three possible scenarios including data for the next three-year period. The mild scenario predicts a favourable health evolution and an effective distribution of the vaccine in Q1 2021, this being the least uncertain scenario. Secondly, the central scenario contemplates the possibility of emergence of new outbreaks of similar intensity to the most recent ones in the coming months, with a limited impact on business operations. Eventually, the most severe scenario takes into account the possibility of a rebound in the disease in the short term, which would require a tightening of containment measures above those necessary after the increases in recent months.

GDP figures for 2020 year-end in each of these scenarios are: -10.7% in the mild scenario; -11.1% in the central scenario; and -11.6% in the severe one. Differences in growth rates are higher for the next few years; the less uncertainty, the greater and faster the recovery is expected to be.

As regards inflation, the latest data published by the National Institute of Statistics (INE) in November 2020 is -0.8% year-on-year, this being the eighth consecutive month recording a negative figure and reversing the growing trend of recent years. BdE forecasts anticipated a negative inflation rate as of 2020 year-end (-0.3%, the same for the three scenarios), and a return to positive figures during 2021, which will be greater in the mild scenario and more contained in the severe one.

At end Q3 2020, date of the latest published data, the unemployment rate had grown by 1% quarter-to-quarter, standing at 16.3%. The increase was slightly higher among the younger population, since the unemployment rate for workers under 29 rose by 1.1% to stand at 29.5%. BdE forecasts greatly improved the year-end prediction, anticipating that the unemployment rate would stand at values between 15.7% (mild scenario), 15.8% (central scenario) and 16.2% (severe scenario). Unemployment is expected to continue to rise in 2021, and it will not be until 2022 when we begin to see a rate recovery.

Summary of Macroeconomic Indicators

GDP ANNUAL RATE OF CHANGE	-9,10%	Q4 2020 (advance estimate)
CPI ANNUAL RATE OF CHANGE	-0,60%	January 2021
UNEMPLOYMENT RATE	16,13%	Q4 2020
CONSUMER CONFIDENCE INDEX	63,1	December 2020
BUSINESS CONFIDENCE INDEX	109,3	Q1 2021
CORPORATE TAX RATE	0,25	2021
INTEREST RATES LESS THAN 1 YEAR TRANSACTIONS	1,66%	November 2020
10-Y BOND YIELD	0,10%	01/02/2021
MANUFACTURING SECTOR PMI	49,3	01/02/2021
HOUSEHOLD DEBT PERCENTAGE OF GDP	61,20%	Q3 2020
IBEX 35 THIS YEAR´S CHANGE	-3,92%	29/01/2021
PUBLIC DEBT PERCENTAGE OF GDP	114,47%	November 2020
RETAIL SALES VOLUME ANNUAL RATE OF CHANGE	-1,50%	December 2020
RETAIL SALES VOLUME MONTHLY RATE OF CHANGE	-1,00%	December 2020
CONSUMER PRICE INDEX	104,7	December 2020
SALARY GROWTH RATE ANNUAL RATE OF CHANGE	0,14%	December 2020
COVID-19 IMPACT	2,743,000 cases 58,000 deaths	

Housing Market

Prices

2020 ended with the price adjustment trend in the housing market that began in March, with a 1% decline in Q4 and prices per sq. m standing at € 1,391 nationwide. This contraction in housing prices is lower than that in mid-year forecasts, where a 3%-4% drop in housing prices was expected.

Breaking the trend of general price contractions during the two previous quarters, in Q4 2020 six Autonomous Communities saw a year-on-year increase in average prices. The most remarkable increases were recorded in Asturias (+1.8%) and La Rioja (+1.0%), while prices rose less than 1% in Galicia, the Canary Islands, the Basque Country and Cantabria. On the contrary, the most significant declines were seen in the Balearic Islands (-6.6%), Aragon (-2.4%), and the two Castiles, with a -1.6% draw.

Madrid, with an average price of € 2,218 / m^2, surpassed the Balearic Islands (€ 2,212 / m^2) in the price ranking by autonomous community. The third position is occupied by the Basque Country, which this quarter stands at € 2,197 / m^2. The lower end of the price ranking is headed by Extremadura, with 839 € / m^2, followed by Castile La Mancha with € 854 / m^2, Murcia with € 993 / m^2 and Castile and León with € 995 / m^2, these being the only communities with prices per sq. m less than € 1,000. At the provincial level, the increases in Soria (+5.0%), Cáceres (+4.1%), Málaga (+2.0%) and Orense (+1.9%) are the most remarkable ones. On the contrary, provinces with the most negative changes include Palencia - with a 6.0% drop- and León -where prices fell by 5.4%-.

As regards provincial capitals, no changes were observed in the top positions in the unit sale price ranking. San Sebastián records a slight quarter-on-quarter increase, with an average of € 3,887 / m^2. Prices in Barcelona also grow up to € 3,266 / m^2, while Madrid sees a slight drop down to € 3,046 / m^2, in a similar way as Bilbao, standing at € 2,430 / m^2. Palma de Mallorca records a slight increase, with an average unit price at € 2,229 / m^2. Together with A Coruña (€ 2,075 / m^2) and Málaga (€ 2,027 / m^2), these are the seven capital cities where unit prices reach values higher than € 2,000 / m^2.

2020 Scenario

Initial forecasts impossible to achieve
in a worldwide pandemic scenario.

Registry and Notarial activity halted
during months of total lockdown.

Uncertainty both at health and economic levels.

Shift in trend, from decelerated growth
to contraction in prices.

Change in demand preferences.

COMMENCED AND COMPLETED DWELLINGS	HOUSING TRANSACTIONS	MORTGAGE LOANS SIGNED	HOUSING STOCK	SALE PRICES
-24% / +11%	-21%	+1%	+0,31%	-1%

Trends

In general, drops in rental prices are expected to be lower than in sale prices, as already observed during the last months. Likewise, prices in most demanded areas (which tend to be those with the least volume of supply available) will remain more stable and will recover faster.

The current situation has led to a change in Spaniards' habits. More time spent at home, together with the possibility for the majority of workers of using a remote connection system, facilitates that criteria such as a location closer to the workplace give way to others such as a larger size or the possibility of having a terrace or garden. This has led the shift in the demand from buyers towards peripheral locations -already observed since mid last year- to increase in recent months, since it is in these areas where homes are better adapted to these new preferences, and at a more competitive price.

Over the last months, both sale and rental price drops were less pronounced in new-build homes than in second-hand ones. Everything indicates that this trend will continue over the next year, since new-build homes adapted to this circumstance, offering solutions such as a greater number of bathrooms, larger or higher quality open terraces and specialisation of communal spaces and services.

It will be interesting to observe what the position of the labour market will be in relation to the continuity of work-from-home policies once the health crisis is over. If so, this could lead to a permanent change in demand preferences (and therefore in prices), especially as regards the search for homes in downtown locations and close to business areas in large cities.

We expect a significant decline in the volume of new real estate developments in the coming years, since the main listed real estate companies reviewed downward their development forecasts for the next five years to half a million homes.

The reactivation speed of international demand will also be a relevant factor in the recovery of prices at the end of next year. It should not be forgotten that, with 2019 as a reference year, more than 12% of homes were purchased by foreign buyers.

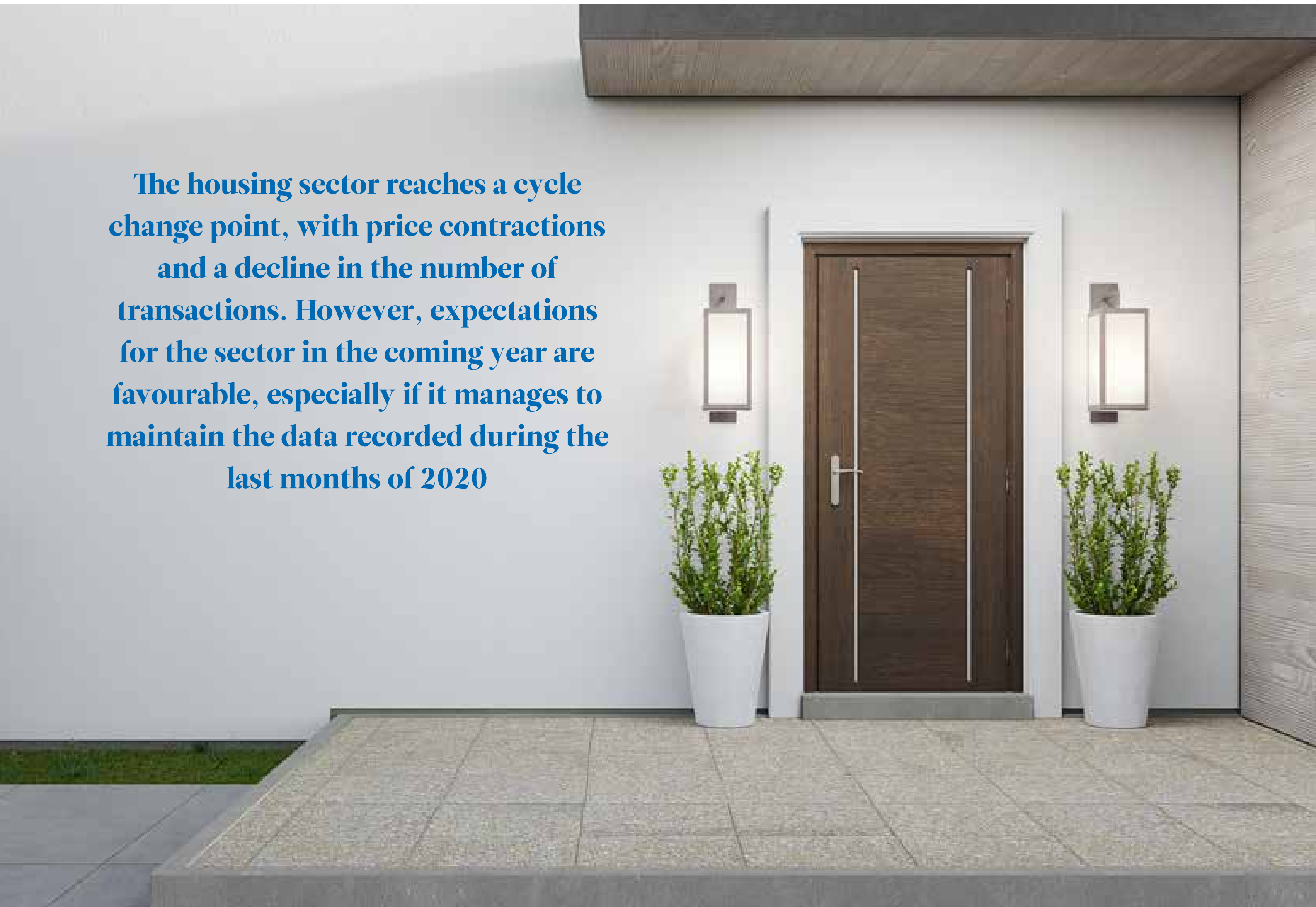
2021 starts at a time of great uncertainty. Confidence will gradually recover throughout the year, and investment in the housing market is expected to rise by 15%-25%, boosted by the Build to Rent model. This will be the year when we observe which of the demand behaviours derived from the pandemic are here to stay

Challenges

The biggest challenge to face in 2021 both in the housing sector and the global real estate industry will be to recover the confidence and interest of the investor profile, very damaged by the uncertainty generated by both health and economic crises. Fortunately, in this situation the real estate industry has proven one of the strongest in the Spanish business fabric and may be one of the keys to future economic recovery.

This situation has only increased the enormous heterogeneity in the Spanish residential market, generating new demand needs at an increasingly rapid pace, so the real estate development segment will have to adapt to respond to these requirements. In this sense, it is obvious that new-build homes will have greater adaptation capacity than second-hand ones, although it could be an opportunity for the existing property restoration plans.

The foreseeable economic downturn and the job destruction already observed in 2020 are going to result in an increase in restrictions on access to home purchases for some groups, such as young people. If we add to this the aforementioned new requirements in the search for housing, the rental option will once again pick up steam in 2021. Not only does it become the only viable option for a percentage of the population, but it can also be a very good choice due to its temporality to tackle the uncertainty of the current moment. In this sense, Build to Rent proposals that grew in strength at the end of 2019 could continue to play a very important role this year.



> **The housing sector reaches a cycle change point, with price contractions and a decline in the number of transactions. However, expectations for the sector in the coming year are favourable, especially if it manages to maintain the data recorded during the last months of 2020**

Retail Market

Prices

The retail sector was -along with hospitality- one of the most affected sectors in 2020. Restrictions on mobility and limitations -either total or partial- in the opening of businesses, resulted in a significant reduction in sale figures, well below the projections for this year.

This caused a significant contraction in prices within all retail segments, although street-level stores were the most affected -with drops by 12.5%-, followed by shopping centres -with a 7% rent reduction-. The retail park segment performed best, although it also saw a contraction of around 5%.

Retail is the only sector in which investment activity increased year on year in 2020, reaching an investment volume close to € 1.9 billion.

Trends

Despite the poor sales figures, the retail industry closed the year with an investment volume close to € 1.9 billion, being the only segment which saw an increase in activity compared to 2019. This was due to the large number of transactions involving large supermarkets and hypermarkets, mostly concentrated during H1 of the year.

As a result of the pandemic, we find how the changes in the population's consumption habits already observed in previous years were strengthened. Mobility restrictions caused an increase in the volume of purchases and in the penetration capacity of ecommerce in our country. In fact, Spain exceeded the European average in terms of the number of people who purchased products online for the first time during the restrictions. In this sense, a 20% increase in income derived from ecommerce is expected, mainly driven by the food industry.

One of the main challenges the sector must tackle in 2021 is that of omnichannel retail, not only as an element to drive an increase in sales, gain permeability in the market or generate a competitive advantage, but also because it may become the only possibility of sale in specific circumstances, as seen during the past year. In this sense, it will be necessary to improve the 360º vision each business has of its end consumer.

Despite this, the vast majority of sales still take place in physical stores. Therefore, an additional challenge will be to encourage physical stores to remain relevant in an environment where buyers are increasingly putting their attention and time in multiple digital spaces. For this purpose, stores are becoming experience spaces. Mixed options are also increasing, with a significant expansion of options such as Click & Collect.

Office Market

In early 2020, the prospects of the office market were highly positive, having demonstrated its resilience and investor's interest in the previous year. All these forecasts were shattered when the lockdown led to the emptying of offices, arousing great uncertainty which caused this type of assets to lose the first place in terms of investment volume. In 2020, the YoY decline in investment has been 50%, with the housing market being the most resistant segment in this scenario, capturing just over € 2.1 billion.

Madrid and Barcelona continued to be the major players. Of the total investment, almost two thirds went to the capital city, while the rest was registered in Barcelona almost entirely. Regarding absorption, at Q3 end the figure for Madrid was 225,000 sq. m, which represents a 50% YoY decline. In Barcelona, office space absorbed was 125,000 sq. m, meaning a 65% reduction.

The shortage of transactions and the dormant state of investors led rents to remain relatively stable, especially considering how turbulent the year has been. We observe how prime rents in Madrid saw a slight decrease of about 3%, standing at € 34.5 / m^2 per month. In Barcelona, with an increasing trend, prime rents rose up to € 28.5 / m^2 per month, 2% higher than in 2019.

The "forced" work-from-home experiment has shown that, in general, the business fabric of our country was ready to work remotely. In addition, it opens up new possibilities for companies in terms of work-family reconciliation or physical space reduction. Furthermore, health requirements resulted in an increase in working space required per worker. The new demand for office space will depend on the balance between these two factors, and above all, on their permanence in time.

In 2021 office space will increase, with a 1 million sq. m expansion almost entirely concentrated in Madrid and Barcelona

Logistics Market

The logistics market was the one that discovered the most opportunities in the extraordinary situation we found ourselves in during the past year, demonstrating great resilience and an excellent ability to adapt to unforeseen scenarios. Since the second quarter, demand for logistics platforms spiked due to the increase in ecommerce sales. This, coupled with high returns, means that the logistics industry will continue to be a highly desirable type of asset in 2021.

As it happened in the office market, most transactions in the logistics market concentrated in the Madrid and Barcelona areas. Specifically, in Madrid, a total of 650,000 sq. m were absorbed during the first nine months of 2020, growing by more than 50%. In the case of Barcelona, 330,000 sq. m were contracted, which represents a 70% YoY rise.

If we analyse the demand behaviour, the greatest interest in Madrid is found in the inner metropolitan area, which concentrates 50% of the transaction volume in Q3. In Barcelona, however, the regional arc was the most dynamic during Q3 2020, with 75% of the total contracted space.

Both prime and average rents remained very stable in this scenario. At this time, prime rents in Madrid are around € 5.75 / m^2 per month, with an 8% vacancy rate. In Barcelona, prime rents stand at € 6.75 / m^2 per month, with a 3% vacancy rate.

After a year with the focus set on overcoming the enormous challenge that the pandemic has posed for the logistics industry, 2021 aims to be the year in which the new proposals planned for last year are put into practice. The good results and the strengthening of the industry may support the implementation of concepts such as picking automation, growth of city hubs and green logistics, which may represent a new step towards a qualitative improvement of this segment.

The logistics industry will remain a key player in 2021, facing new challenges such as greater penetration of ecommerce, last mile logistics and ecological transformation.

Rural Properties

The special health situation derived from the pandemic may lead us to think that the food industry, and consequently the land where these products are grown, would have seen a positive price performance; but this has not been the case for all farmland and uses. In 2020, we witnessed the highest volatility in food prices in the last 15 years, with year-on-year declines in half of the products. The rationale for this paradox may lie in several reasons, the main one being the fact that 70% of the Spanish production is destined for export, which is why it has been severely affected by mobility restrictions imposed on people and goods. As regards the remaining 30% of the production, approximately 20% is destined to food industries and only 10% is acquired by large distribution companies for direct sale, which resulted in national oversupply of food products.

Along with this volatility, a maximum gap price throughout the supply chain from origin to end consumer was observed in 2020. This difference reached 550% for livestock products and more than 300% for agricultural ones. This led to lower interest in the purchase of agricultural land, since many crops were produced with costs higher than the income derived from their sale (dumping), as has been, for example, the case of potatoes or broccoli.

Due to the abovementioned reasons, land prices maintained last year the trend seen in 2019 and continued to decline; -0.9% in nominal terms, and -1.4% in real terms (assuming the -0.5% annual deflation data published). The number of sale and purchase transactions was at minimum levels, close to figures reached in 2010 and 2011. However, we have detected a completely opposite circumstance to that occurred during the 2009 downturn. If at that time the land with the best behaviour -in terms of price- was that with the lowest value (grassland, dry meadows and farmland properties below class III), at present, the properties that had started with the highest values were the most stable in price. Specifically, in nominal terms the price of farmland would have contributed + 0.2 overall, compared to the fall in exploitable land (grassland, meadows and farmland properties below class III).

In 2021, the trend observed in Q1 2020 -price stagnation and reduction in the number of transactions- is expected to continue. Perhaps, until Q4 2021 it will not be possible to draw unquestionable conclusions on the evolution of the rural property market.

Finally, we observe the consolidation of the practice that began a decade ago with the inclusion of an increasing percentage of rural land in real estate investment funds. Although it is still a residual percentage, we think it will be an increasing trend and as a result a price increase in farmland can be expected. It is also worth highlighting the excellent performance of pig farming during 2020, undoubtedly the "star product" among investments in the livestock sector, which, in our opinion, will maintain its good results this year.