MALLING & CO

MARKET UPDATE

September 2018

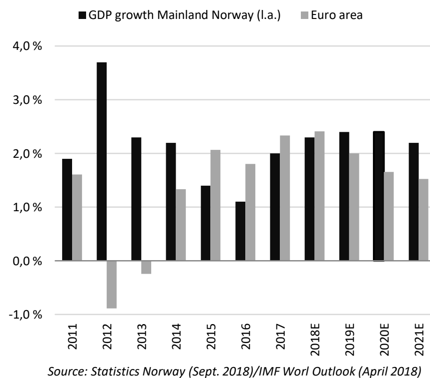
Økern Portal
Malling & Co has leased approx. 13 000 m² to Telia Norge AS in the new development at Økern, scheduled for completion in Q1 2021. The project will include offices, hotel, retail and service space, totalling more than 75 000 m².

Illustration: Dark Architects

Latest figures Norway

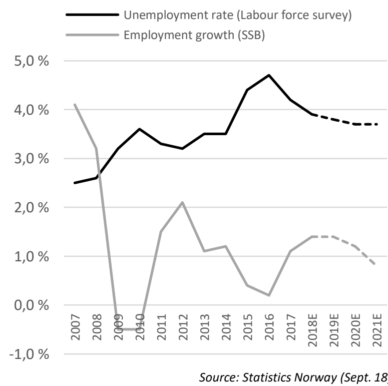
- GDP Mainland Norway is in the latest yearly estimate from statistics Norway estimated at 2.3 % for 2018, which is above the assumed trend growth. The estimate for 2019 and 2020 stands at 2.4 %.
- The unemployment rate (LFS) has stabilized around 4 % and was measured at 4.0 % in July 2018 (avg. June – August). However, employment is increasing, and counts a positive change of 49 000 new employees over the past 12 months.
- The key policy rate was increased from the record low level at 0.50 % to 0.75 % at the last meeting on 20 Sept. The Norwegian Central Bank is also signalling a gradually increasing interest rate in the coming years.
- Money market rates (3m NIBOR) increased from January to April, and after touching below 1.00 % during summer, it is now back at 1.12 %.
- The NOK is still considered relatively weak, despite an increasing oil price and a signal of increasing interest rates.
- The weak krone has again contributed to a high imported inflation, accompanied by higher energy prices, the 12 month change in CPI in August ended at 3.4 %. CPI is according to Statistics Norway expected to be approximately 2.8 % for 2018 and below 2 % 2019 and 2020.
- The crude oil price has increased steadily since the summer of 2017 from below 50 USD per barrel, up to just above 80 USD per barrel.

GDP: Mainland Norway vs. Eurozone



Source: Statistics Norway (Sept. 2018)/IMF Worl Outlook (April 2018)

Labour market Norway



Source: Statistics Norway (Sept. 18)

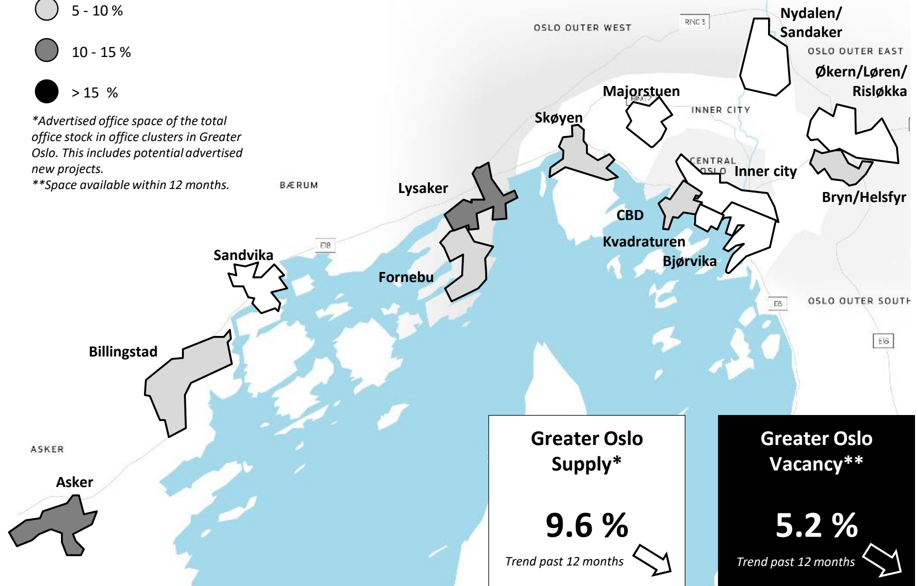
Latest lease contracts

Tenant	Address /Cluster	Size (m²)
Telia Norge AS	Lørenfaret 1 (Økern Portal) / Økern/Løren/Risløkka	~ 13 000
Aller	Kongens gate 21 / Kvadraturen	~ 3 500
Mattilsynet	Stensberggata 25-27 / Inner City	~ 2 500
EnTur	Rådhusgata 5 (Transperia) / Kvadraturen	~ 2 670
Spacemaker	Pilestredet 33 (Epicenter) / Inner City	~ 1 000

Latest transactions

Buyer	Address	Size (NOK million)
N/A	Equinor HQ Forus	Est. 2 500
Joh. Johannson	Alna Senter	Est. 2 000
Arctic Syndicate	Fyrstikkalléen 1	1 920
Storebrand EF Norge	Destilleriveien 11	1 700
Entra	Brynsveien 1-13	1 100

Vacancy** in office clusters in Greater Oslo (September 2018)



*Advertised office space of the total office stock in office clusters in Greater Oslo. This includes potential advertised new projects.
**Space available within 12 months.

Greater Oslo Supply*
9.6 %
Trend past 12 months

Greater Oslo Vacancy**
5.2 %
Trend past 12 months

Number formatting: SI style (English version)

Commercial Real Estate

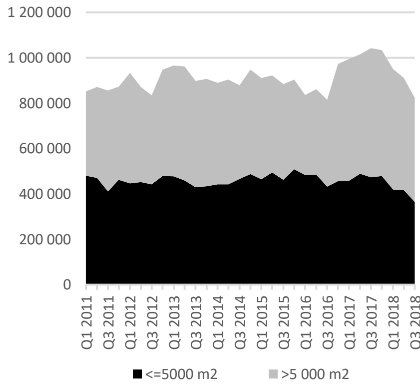
Office market

- The office vacancy level (office premises available within 12 months) has decreased since the summer of 2017, and is now at 5.2 % on average in the office clusters we follow. Low vacancy in attractive areas creates momentum to negotiate higher rents for Landlords.
- Construction pipeline is still moderate, but a strong office letting market is triggering new projects like Økern Portal. However, construction takes time and is not able to balance out decreasing office vacancy in the short term.
- Office rents continue to accelerate on the positive trend, an is currently at all time high in nominal terms. As vacancy is decreasing and supply is slow reacting, office rents are expected to continue upwards to new record levels in the coming 12 months.
- High business activity in Norway and Oslo in particular, is supporting our outlook.
- Rental growth estimate, Oslo Office (measured on average of signed rents):
  - **2018: + 10 %**
  - **2019: + 5 – 10 %**

Transaction market

- The pace has really picked up again with a registered volume of NOK 51.3 billion divided into 154 transactions. Another sign of a strong momentum is the high number of off-market deals that are taking place. To remain very strong in Q4, and reiterate our projection of a transaction volume between NOK 80 and 90 billion for the full year.
- Office is still the segment where the majority of the transaction volume is invested, and in our view the segment with the brightest outlook due to low vacancy and expected rental increases. Although the Norwegian Central Bank has increased key policy rate in September, our prime office yield estimate remains at 3.75 % and our estimate for normal yield is held firm at 5.10 %.
- The second highest volume is found in the industrial segment, and our prime logistic yield of 4.80% is a further reduction of 10 bps since the beginning of the year, and 25 bps over the past 12 months. Our yield outlook remains almost flat for the coming 12 months, with a marginal increase of 10 bps to 4.90 % in 12 months.
- The retail yields in high street areas have seen an increase. Our investor survey is revealing that the trend is expected to continue, and high street retail yields flat going forward. The prime yield is now at 3.75 % for high street at Karl Johan, while the normal yield for Majorstuen is estimated at 5.05 %.

Advertised office space in Oslo (m²)



Key facts real estate (office)

	PER SEP. 2018	PER SEP. 2017
Prime yield	3.75 %	3.65 %
Normal yield***	5.10 %	5.15 %
5 yr. swap rate (COB 25 Sept.)	2.02 %	1.49 %
Average of 15 % highest rents in Oslo, NOK/m²/yr. (Q2)	3 830	3 320
Office contracts signed, m² (Oslo) (Q4)	153 280	191 560
Largest office contract, m² (Oslo) (Q2)	15 173	37 085
Avg. contract length, yrs. (Oslo) (Q2)	5.6	4.4

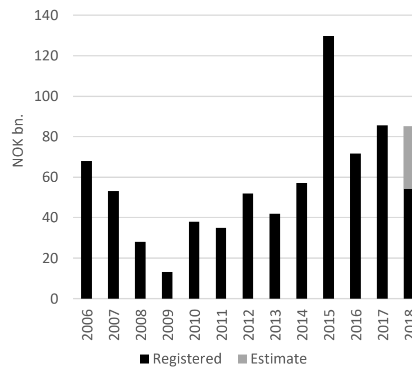
Source: Malling & Co/DNB Markets/Six/Arealstatistikk

Indicative office rents in Oslo (NOK/m²/yr.)

Office cluster	Prime rent*	Normal rent**
CBD	5 400	2 900 – 3 500
Skøyen	3 000	2 000 – 2 400
Inner City	3 900	2 400 – 2 800
Bjørvika	4 000	2 800 – 3 200
Lysaker	2 350	1 700 – 1 900
Fornebu	1 950	1 400 – 1 600
Nydalen/Sandaker	2 350	1 600 – 1 800
Økern/Løren/Risløkka	2 200	1 000 – 1 500
Bryn/Helsfyr	2 350	1 600 – 1 800

Source: Malling & Co

Transaction volume (>50 NOK million)



Source: Malling & Co

**Prime rents are consistently achievable headline rental figures that relate to a new, well located, high specification unit of a standard size commensurate demand within the predefined market area. The prime rent reflects the tone of the market at the top end, even if no new leases have been signed within the reporting period. One-off deals that do not represent the market are discarded.*
*** Normal rents reflect the interval where most contracts are signed in the specified market area.*
**** Normal yield is defined as the net yield of a well maintained building situated in the fringe zone with strong tenants on a 5 – 8 year lease contract.*

Special topic: Retail real estate facing headwinds

The shift in consumer preferences, from physical store sales towards e-commerce, is affecting retail in Norway. While retail real estate has provided solid returns for investors for decades, the structural changes are now hitting retail real estate, challenging rental growth and asset values.

Norway, on top of the list of total shopping centre space per capita, has seen weaker growth than in the early 2000s. Adjusting for expansions, turnovers are actually decreasing in real terms. Additionally, prime retail is struggling to increase rents. While physical retail is facing challenges, Norwegians are embracing online shopping. Norwegians' e-commerce spend from domestic and foreign sites has increased 13 % and 25 % p.a. respectively. Especially the toll-free limit of NOK 350 (approx. EUR 36) on online purchases is channeling low value retail. But retail is also facing changes in consumer preferences. Consumers are spending more on food and beverage, travel and events, and higher spending on services or leasing is in many cases the flip side of buying costly goods.

The headwind for physical retail comes at a time when the Norwegian economy is seeing a cyclical upturn. The changes are structurally driven as seen in other markets like the US. With increasing interest rates on high household debt levels, and clear expectations of continued growth of online retail, it is difficult to see that physical retail will grow and hence produce higher rents for the general retail landlords in the years to come.

That being said, we strongly believe that the best retail properties still will attract visitors through genuine experiences and naturally high footfall. These prime locations and assets will come out as the winners. If retail tenants are considering reducing their costs through limiting their number of stores, it is likely that the best one or two will be kept rather than five medium performing units. If this theory holds, tenants' willingness to pay should be higher for the very best spots, whether it is in the best shopping centres or in high streets. The "losing" assets will lose value and hopefully retain some of it through alternative use.

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