Savills Research – Review and Outlook 2024

Ireland Investment Market

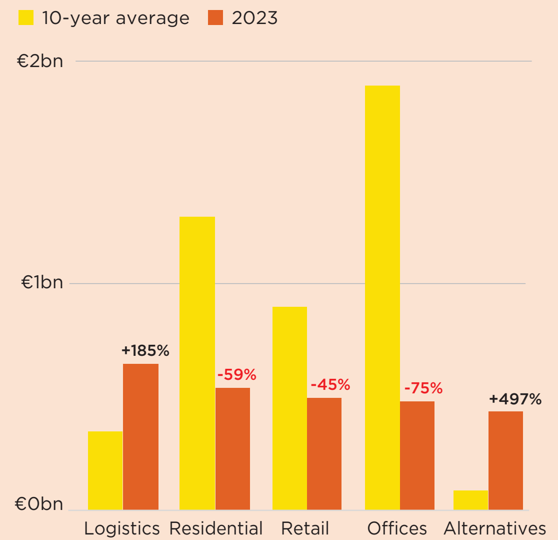
Outlook for 2024

1

Sector spend evenly spread

There was €2.2 billion worth of investment transactions in 2023, just over half (52%) of the 10-year average of €4.2 billion. Decomposing the sector contributions to overall volume provides some interesting insights. For example, the contribution of each sector was relatively evenly spread, ranging from €351 million for alternatives to €520 million for logistics, whereas typically there would be a much larger dispersion. This was driven by large declines in volumes for the big sectors compared to their 10-year averages, while at the same time the smaller sectors had a bumper year. Specifically, the offices (-75%), residential (-59%) and retail (-45%) sectors all fell sharply compared to their 10-year values, while alternatives and logistics grew by 497% and 185% respectively. That the offices sector saw such a large decline in volumes but still maintained a relatively robust performance demonstrates the importance of this sector to overall investment volumes. While offices is undergoing a painful transition at the moment, buffeted by the structural shocks of ESG and flexible working, we believe that the sector will recover and remain the main driver of investment volumes in the medium to long-term.

Figure 1: Investment volumes, 10-year average versus 2023



Source: Savills Research

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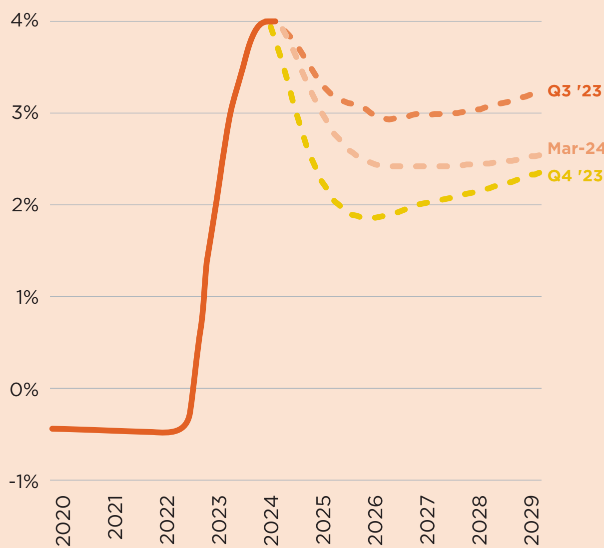
Renewed upward shift in interest rate expectations

Figure 2: Market implied ECB deposit rate



Source: Savills Research

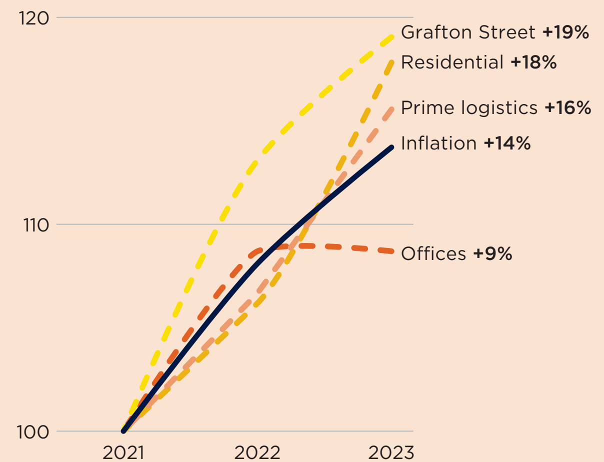
The final quarter of 2023 witnessed an extraordinary rally in capital markets, with the real estate segment of the S&P 500 returning a market-leading 19% in Q4 alone. That optimism was built around promising inflation data which indicated that central banks would cut rates significantly in 2024. Specifically, by the end of the year, the market implied ECB deposit rate for year-end 2024 was 2.3%, down from the 3.3% expected just three months earlier. However, the early stages of 2024 have seen a renewed upward shift in interest rate expectations, as optimism on inflation faded once more with the rate at the end of 2024 now expected to be 3.0%. Clearly, a stabilisation in interest rate expectations is a necessary condition for a recovery in the real estate market, with the gyrations in the forward curve making it hard to underwrite deals with the required degree of certainty. This means the recovery in the investment market that was expected to begin in H1 has now been kicked back to H2 at the earliest, and possibly drift into early 2025.

3

Income returns exceeding inflation

When inflation first started to take off in earnest in H1 2022, real estate was cited as an investment that would outperform due its qualities as an inflation hedge. This has not turned out to be the case, as the negative impact on values via the rise in interest rates has more than offset the inflationary hedging qualities of real estate. Real estate is an especially interest rate sensitive segment of the economy, and the pace and extent of rate rises over the last two years has far surpassed even the most bearish of expectations. Nevertheless, it is illuminating to see that real estate has worked in protecting the income component of return, with rents for prime high street retail (+19%), residential (+18%) and logistics (+16%) all growing faster than general inflation (+14%). Only prime offices has underperformed, but even then it has seen inflation of +9% despite the unique challenges in that market segment. Looking ahead, the higher rate environment has reduced new commencements and thus new supply into the future, an aspect which will further support rental growth.

Figure 3: General inflation versus rental inflation by property sector, 2021=100



Source: Savills Research, CSO

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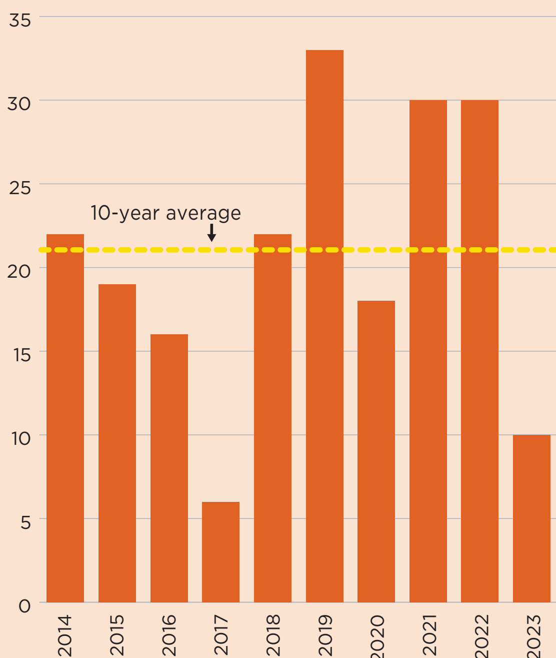
Figure 4: Number of deals, €50m or above



Source: Savills Research

Dearth of liquidity for large lot sizes

While the higher interest rate environment has impacted transactions across all lot sizes, it has particularly impacted large deals. In total, there were just 10 deals greater than €50 million in 2023, just under half of the 10-year average of 21 and just a third of the 30 witnessed in both 2021 and 2022. The lack of liquidity for larger lot sizes reflects a wider global trend in this regard. It is partially driven by the general risk-adverse sentiment prevailing in the market, with participants unwilling to make large investments relative to existing portfolio holdings at a time of heightened uncertainty. Secondly, larger deals are more reliant on debt as a source of funding due to their size but leverage is not accretive to returns at current levels. Furthermore, any investor cash holdings that normally would be available for new deals is under pressure for use as equity injections to shore-up loan to value ratios. We nevertheless envisage an increase in lot sizes this year, driven by an increase in receivership sales for offices and motivated sellers of shopping centres, with significant value adjustments required to attract investors to participate in bidding for these larger assets.

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Transactional activity falls as higher rates bite

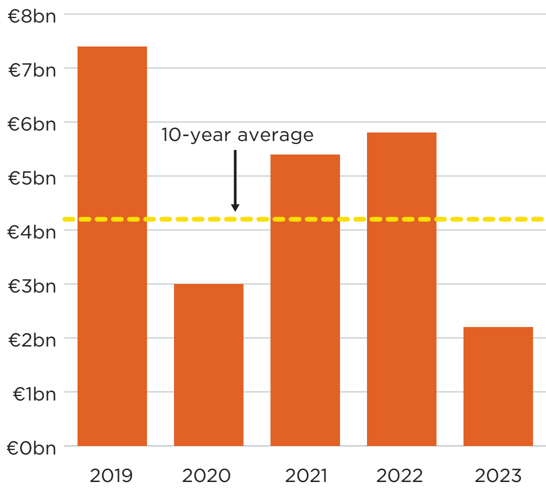
€444.2 million worth of investments transacted in Q4, which compares with a 10-year quarterly average of €1.1 billion. For full-year 2023, investment volumes finished the year at €2.2 billion, 48% below the 10-year average of €4.2 billion. In total, there were 28 deals in Q4, down from the 10-year quarterly average of 54. On an annual basis, there were 115 deals, compared to a 10-year average of 218. The average deal size in Q4 was €15.8 million (versus a 10-year average of €20.9 million), while the full-year average deal size was €18.7 million (versus a 10-year average of €20.3 million).

Q4 SUMMARY

The largest deal of the quarter was the sale of Mountpark Baldonnell II by Mountpark to Pontegadea for €225.0 million. The fully let scheme extends to 1.1 million sq ft, of which over half is let to Amazon. It is believed that the deal represented a net initial yield of just under 5%. It was the second transaction of the year by Pontegadea, having purchased the residential scheme Opus, 6 Hanover Quay, for €101.0 million in Q1 in what was the fourth largest deal recorded in the market in 2023. The second largest deal of the quarter was the purchase of Trinity Point by the OPW from a private individual for €40.0 million. The building is currently majority occupied by the OPW, on leases that were due to expire in March 2032. The property was originally offered in Q3 2022 for €57.0 million, at a net initial yield of 4.1%, illustrating the decline in office values witnessed in the last 18 months.

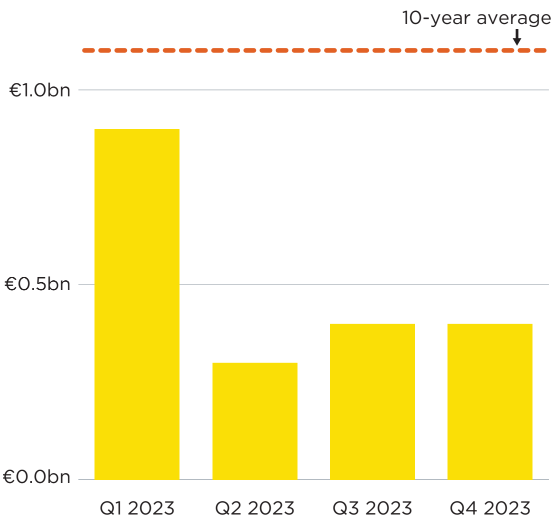
Other significant deals in Q4 included the sale of The Chancery in Dublin 8 for approximately €14.0 million, selling to Sretaw PE. The property was brought to the market in Q3 2022 with a guide price of €24.75 million, again illustrating the depth of price adjustments taking place in the market. The property previously changed hands in 2017 for €23.8 million when Hibernia REIT sold it to Credit Suisse. Elsewhere, Avivia sold The Grafton Port Collection to a private individual for €13.5 million, representing a net initial yield of 6.8%.

Figure 5: Annual investment volumes



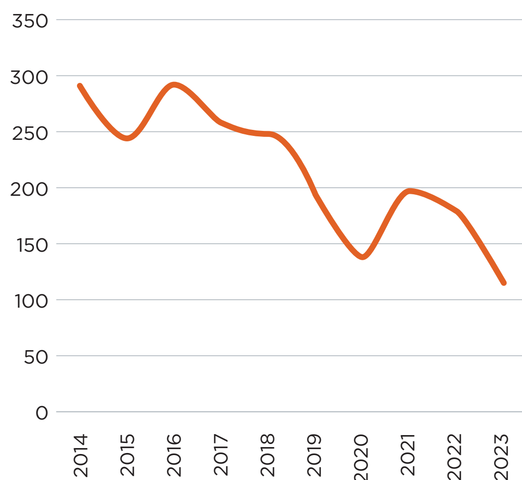
Source: Savills Research

Figure 6: Quarterly investment volumes



Source: Savills Research

Figure 7: Number of deals



Source: Savills Research

Table 1: Top five deals in Q4

Property	Sector	Vendor	Purchaser	Price
Mountpark Baldonnell II, Baldonnell Business Park, D22	Logistics	Mountpark	Pontegadea	€225.0m
Trinity Point, 10/11 Leinster Street South, D2	Offices	Private Irish	OPW	€40.0m
Douglas Court Shopping Centre, Cork City	Retail	Varde Partners	Private Irish	€21.5m
Confidential, Citywest, D24	Logistics	Confidential	Confidential	€20.6m
Trinity Street Car Park, D2	Mixed-use	BCP Capital	The Mercantile Group	€18.0m

Source: Savills Research

Waterside, Citywest, D24

FULL-YEAR 2023 DEAL ANALYSIS

Looking at the full-year, the largest deal was the acquisition of the Valley Healthcare platform by KKR through its subsidiary company John Laing for €300.0 million. The Valley Healthcare platform consisted of 20 operational primary care centres – which are operated and managed by the HSE – assembled through a combination of acquisitions and development projects. Each site has inflation-linked leases for periods of 25 years with five-year extension options. The third largest deal of the year also involved KKR, this time on the sell side as it disposed, along with its joint venture partner Palm Capital, of Greenogue Logistics Park to Ingka Investments for €110.0 million at a yield of 3.9%. Greenogue Logistics Park consists of 450,000 sq ft spread across three units, and the deal marks a successful exit for the investors who speculatively delivered the units in late 2022.

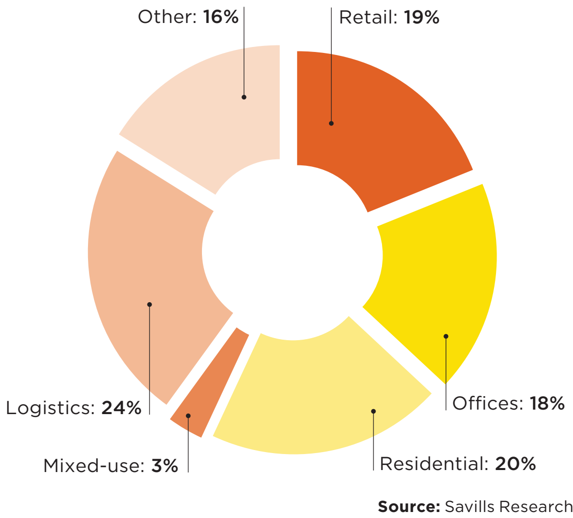
The fourth largest deal was the sale by Angelo Gordon and their local partner Carysfort Capital of Opus, a prime PRS scheme located in Dublin's south docklands at 6 Hanover Quay. The 120 unit scheme was purchased by Pontegadea Investments, the family office of Zara founder Amancio Ortega. Excluding the minor associated commercial element of the deal, the yield on the residential component is estimated to be 4.25%. The private rented sector was also behind the next largest deal of the quarter and also involved a new market entrant, as M&G acquired Eglington Place, Donnybrook, for €99.5 million, representing a yield of 4.1% and an average price of €672,000 per unit.

Table 2: Top 10 deals, 2023

Quarter	Property	Sector	Vendor	Buyer	Price	Yield
Q1	Valley Healthcare platform	Medical	Irish Infrastructure Fund/ AMP Capital	John Laing/KKR	€300.0m	4.9%
Q4	Mountpark Baldonnell II, Baldonnell Business Park, D22	Industrial & Logistics	Mountpark	Pontegadea	€225.0m	4.7%
Q1	Buildings 1A, 1B and 2, Greenogue Logistics Park, D24	Industrial & Logistics	Palm Capital/KKR	Ingka Investments	€110.0m	3.9%
Q1	Opus, 6 Hanover Quay, D2	Residential	Angelo Gordan/ Carysfort Capital	Pontegadea	€101.0m	4.4%
Q1	Eglington Place, D4	Residential	Richmond Homes	M&G	€99.5m	4.1%
Q1	Lisieux Hall, Murphystown Road, D18	Residential	Noel Smyth	Respond	€92.0m	n/a
Q3	George's Quay House, D2	Offices	Henderson Park Capital	Corum	€81.0m	6.2%
Q3	Hexagon Portfolio, nationwide	Retail	Reciever KPMG (Harcourt Developments)	Davy	€74.0m	11.0%
Q1	Waterside, Citywest, D24	Offices	IPUT & Davy	Fine Grain	€65.5m	7.0%
Q2	Bessboro Park, Mahon, Cork	Residential	First Step Homes/ Angelo Gordon	New Beginning	€55.0m	3.7%

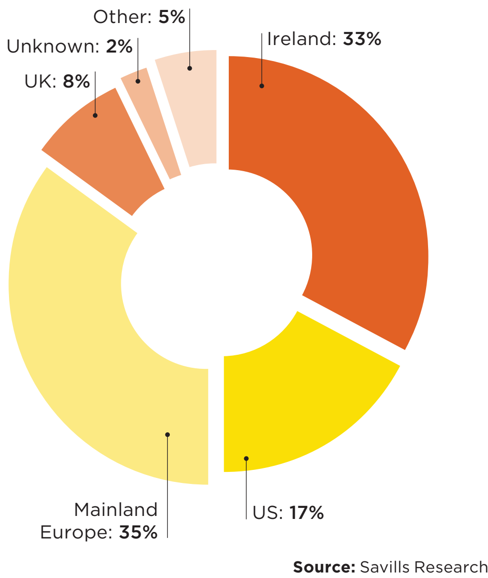
Source: Savills Research

Figure 8: Market share by sector, 2023



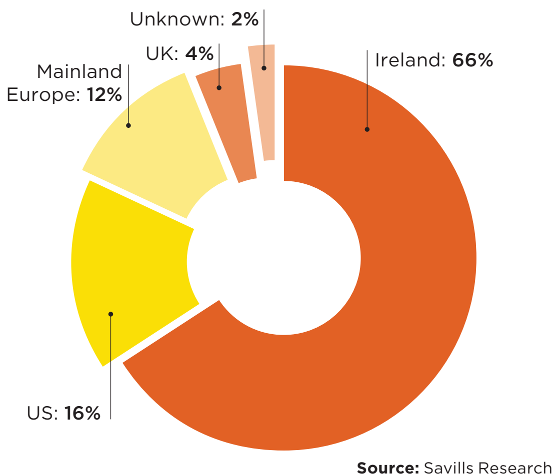
Source: Savills Research

Figure 9: Buyers by geography, 2023



Source: Savills Research

Figure 10: Sellers by geography, 2023



Source: Savills Research

MARKET SHARE BY SECTOR

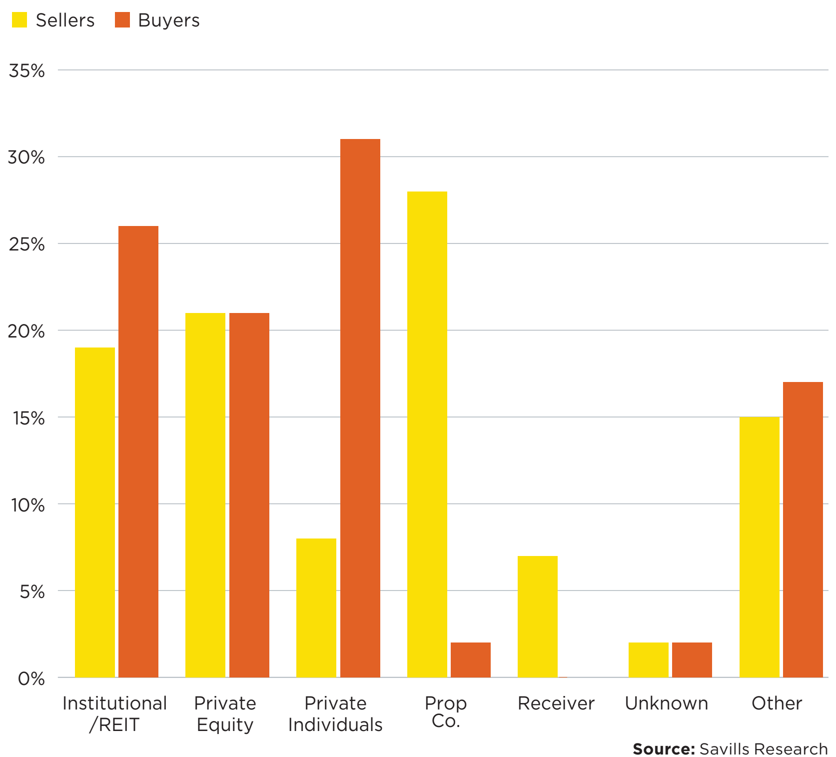
Looking at the breakdown by sector, the most noteworthy development was the fall in the market share of the residential sector to just 20%, compared to a five-year average of 35%. The impact of higher interest rates combined with rental caps lies behind the drop in investment in the sector. The logistics sector accounted for the largest share of activity at 24%; the first time on record the sector had the highest market share. To put this into further context, it is only the second time on record that the sector achieved a double digit market share. By contrast, the office sector market share of 18% was its weakest on record. Retail had another relatively strong year with a 19% market share compared to a five-year average of 13%. The strong performance of retail was driven by the high passing income yields available in the sector, and thus, it was less affected by the rise in debt costs compared to tighter yielding investments.

BUYER – SELLER ANALYSIS

In terms of geographical capital flows, mainland Europe buyers were the most active with a 35% market share, followed by Ireland at 33%, US at 18% and the UK with 8%. Looking at the disposal side, Ireland accounted for the highest share at 66%, followed by the US at 16%, mainland Europe at 12% and the UK at 4%.

Breaking down activity by investor type, the biggest trend was the large market share of private individuals as buyers (31%) compared to sellers (8%). Low savings deposit rates, less reliance on debt and less competition from institutional and private equity buyers has driven this private money to account for the largest market share for buyers in 2023. However, it is also noteworthy that institutional funds were still net buyers in 2023, having a 26% market share for acquisitions versus 19% for disposals. Private equity's share was relatively even on both sides of the market, meaning their market position remained unchanged. Property companies were the largest sellers (28%), which mostly comprised of developers exiting completed developments.

Figure 11: Seller versus buyer type market share, 2023



Source: Savills Research

Table 3: Yields by sector

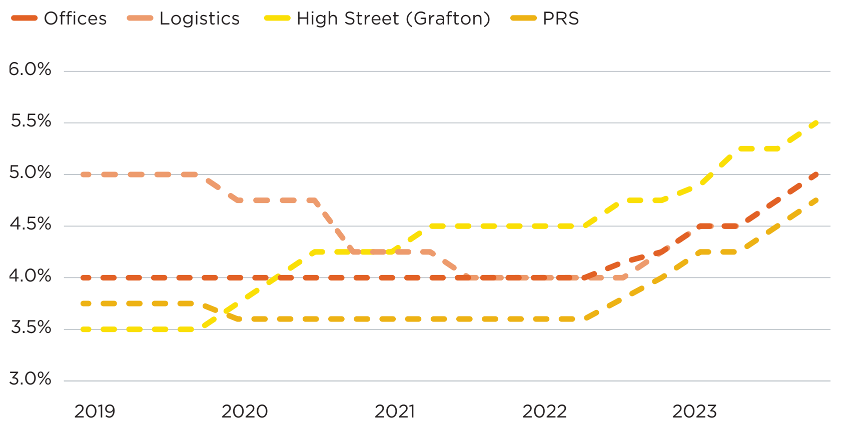
Sector	Q4 2023	Y/Y change
Offices - prime CBD yield	5.00%	75 bps
Offices - secondary CBD yield	7.50%	150 bps
Industrial - prime yield	5.00%	75 bps
Industrial - secondary yield	6.50%	75 bps
Shopping centres - prime yield	7.00%	100 bps
Shopping centres - secondary yield	10.50%	50 bps
Warehouse retail - prime yield	6.25%	75 bps
Warehouse retail - secondary yield	9.75%	-
High street - prime yield	5.50%	75 bps
High street - secondary yield	8.25%	75 bps
PRS - prime yield	4.75%	75 bps
PRS - secondary yield	6.50%	100 bps

Source: Savills Research

YIELDS

Yields pushed out significantly in 2023, as the high interest rate environment fed through to the property sector. Secondary offices saw the greatest outward yield adjustment, going from 6.0% to 7.5% over the course of the year while prime offices moved from 4.25% to 5.0%. Prime PRS yields saw the largest outward shift of all the prime areas of the market, with the movement from 4.0% to 4.75% representing a fall in value of 18.75%. Prime industrial and logistics yields now stand at 5.0%, prime shopping centres at 7.0%, prime warehouse retail at 6.25% and high street yields at 5.5%. The outlook for 2024 promises to be more stable, given the expectation that interest rates have already peaked, alleviating the downward pressure on property values.

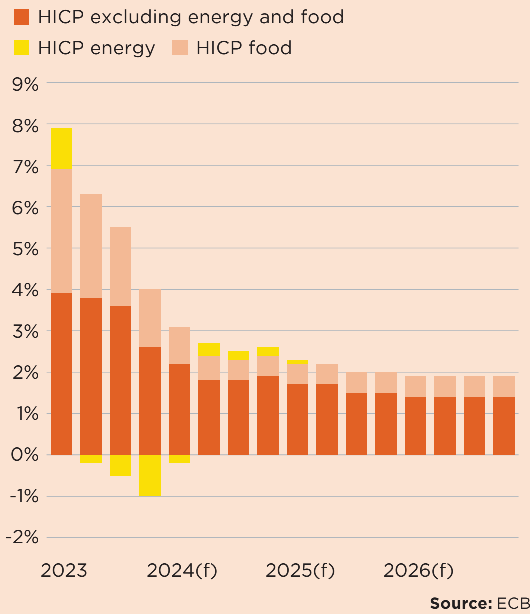
Figure 12: Prime yields by sector



Source: Savills Research

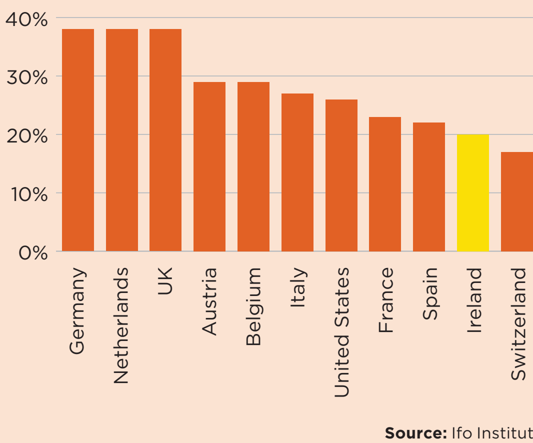
Greenogue Logistics Park, D24

Figure 13: Eurozone inflation decomposed



Source: ECB

Figure 14: Expectation of recession in 12 mths



Source: Ifo Institut

Macro View

Falling inflation and higher economic growth expected

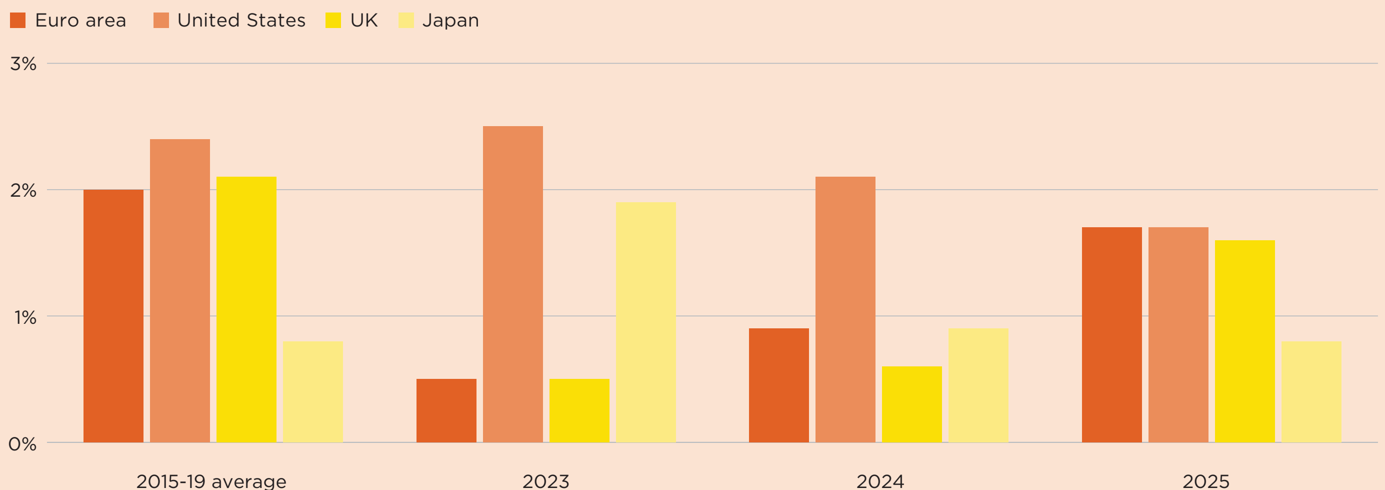
Inflation in the eurozone halved during the course of 2023, going from over 8% to 4% during the 12 months. The fall in energy prices was the main driver of this, which had a negative contribution to inflation last year, having previously been the main driver of the spike in inflation witnessed in 2022. The other big driver, food, also moderated significantly, going from over 3% contribution to inflation to just 1% by year end. By the end of 2024, it is anticipated that food inflation will contribute just 0.5%. However, bond yields remain elevated, reflecting the fear that inflation has become more embedded in the service sector of the economy. Though we are relatively close to the inflation target of 2%, this last leg of the inflation fight will likely be the most challenging.

GLOBAL ECONOMIC OUTLOOK

Ordinarily, one would expect the pace of interest rate rises witnessed over the last two years to result in a recession. However, the greater prevalence of fixed rate mortgages as well as relatively conservative levels of debt means that the pass-through mechanism from higher rates to slowing consumer demand has not been as linear as in previous cycles. As a result, expectations around recession risk have broadly receded, though it still very much depends on geography. A recent survey by ifo Institute found that 38% expected a recession in the next 12 months in Germany, Netherlands and the UK, compared to 26% in the United Sates and just 20% in Ireland.

Looking at global economic growth prospects more broadly, the euro area is expected to expand by 0.9% this year according to the IMF, up from growth of 0.5% in 2023. Therefore a recession is expected to be avoided again this year, with growth accelerating further to 1.7% in 2025. Growth is less than that of the United States, which is expected to expand by 2.1% this year, following last year's 2.5% expansion, before slowing to match the euro area's growth in 2025. Given its economic ties, Ireland will likely benefit from the stronger prospects emanating from the United States but it remains to be seen whether either jurisdiction can return to the higher economic growth rates witnessed between 2015-2019, which were fuelled by a low interest rate environment.

Figure 15: IMF growth forecasts



Source: IMF

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