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The REVU

THE REAL ESTATE VALUATION UPDATE

EUROPEAN EDITION | 2017

Country Overview

U.K.

- Total transaction volume for U.K. **shopping centres** was at £982 million for H1, which is 33% lower than H1 2016. **High street prime yields** in the U.K. were at 4%, which is below the 10-year average of 4.25%. U.K. high street rents overall grew by 1% over the past 12 months.[1]
- U.K. **hotel transaction volume** in H1 2017 decreased by 9% year-on-year to €2.1 billion, which was attributed to a shortage of investable stock and large portfolio transactions in H1 2016.[2]
- **Prime office rents** in central London have fallen over the past year by 2% in the city and 8% in the West End, while they have been more stable in regional cities such as Manchester and Birmingham.[3]

European Investment by Sector, Q2 2017[11]

GERMANY

- **Prime retail yields** for high street shops in Berlin, Frankfurt, and Munich were at 10-year lows of 3.5%, 3.6%, and 3.1%, respectively, as of June 2017. The **prime rents for high street shops** in Berlin, Frankfurt, and Munich increased by a five-year CAGR of 2.4%, 1.7%, and 1.1%, respectively. German **shopping centre yields** fell to 3.7% in June 2017, down from 3.9% in June 2016.[4]
- German **hotel transactions** declined 10% year-on-year in H1 2017 to approximately €1.79 billion, while **hotel yields** in the five largest cities were at a three-year low of 4.2%. **Hotel vacancy** for the five largest cities was 6% on average in June 2017.[2]
- **Prime office rents** in Germany are up broadly due to strong demand and limited supply, with rents for the Berlin, Frankfurt, and Munich CBDs at €26.50, €39.00, and €35.00 per square meter per month, respectively, as of June 2017.[5]

FRANCE

- The French economy and office market are expected to improve on the back of recently elected **President Emmanuel Macron**'s ambitious reform program to address unemployment, fiscal imbalances, and shallow competitiveness.[6,7]
- **Prime retail yields** in Paris as of June 2017 are at a 10-year low of 2.5%, down from 3.0% in June 2016. **High street prime retail rents** in Paris increased by a five-year CAGR of 6.7% through June 2017. **Shopping centre yields** in the Paris region fell to 3.5% in June 2017, down from 4.0% in June 2016.[8]
- French **hotel transaction volumes** in H1 2017 decreased by 77% year-on-year to €225 million. **Hotel yields** in Paris were 4.5% while **hotel vacancy** was at 5.5% in June 2017.[2]
- **Prime office rents** in France are mainly stable, but areas with very tight supply have started to see sustained upward pressure on rents. Similarly, **prime office yields** in France are expected to decline in 2017.[6]

Sources:

1. CBRE Retail Property Perspective, H1 2017.
2. CBRE MarketView Snapshot Europe Hotel Investment, H1 2017.
3. Cushman & Wakefield United Kingdom Office Market Snapshot, Second Quarter 2017.
4. Cushman & Wakefield Germany Retail Market Snapshot, Second Quarter 2017.
5. Cushman & Wakefield Germany Office Market Snapshot, Second Quarter 2017.
6. Cushman & Wakefield France Office Market Snapshot, Second Quarter 2017.
7. IMF France: Staff Concluding Statement of the 2017 Article IV Mission, dated July 17, 2017.
8. Cushman & Wakefield France Retail Market Snapshot, Second Quarter 2017.

Country Overview (cont.)

ITALY

- **High street retail yields** in Rome and Milan decreased by 50 bps to a 10-year low of 2.75% in June 2017. **High street retail rents** in Rome and Milan increased by a five-year CAGR of 11.1% and 14%, respectively. Italian **shopping centre yields** dropped from 5.25% in June 2016 to 4.75% in June 2017.[9]
- **Hotel investments** were up 59% year-on-year in H1 2017, reaching €745 million. **Hotel yields** for Rome and Milan were 5.25% and 5.75%, respectively, as of June 2017. **Hotel vacancy rates** in Rome and Milan were 6.8% and 7.1%, respectively.[2]
- **Prime office rents** for the Milan CBD increased 8.2% over the past year through June 2017 to €530 per square metre per year, while rents for the Rome CBD have been flat at €400 per square metre per year.[10]

SPAIN

- **Prime high street retail yields** in Madrid and Barcelona decreased by 25 bps to a 10-year low of 3.4% in June 2017, down from 3.65% in June 2016. **High street prime rents** in Madrid and Barcelona increased by a five-year CAGR of 2% and 1.1%, respectively. **Shopping centre yields** are at a 10-year low of 4.25% as of June 2017.[11]
- Spanish **hotel investments** rallied in H1 2017, with investment volumes increasing by 228% year-on-year to over €2 billion. **Hotel yields** in Madrid and Barcelona were 5.25% and 5.0%, respectively, as of June 2017. The **room vacancy** in Madrid and Barcelona was 6.7%.[2]
- Institutional investor interest for Spanish **office assets** remained high through Q2 2017, with Madrid and Barcelona attracting most of the deals.[12]

Cap Rate Summary by Country and Asset Class[13]

	U.K.	Germany	France	Spain	Portugal	Netherlands	Ireland
Retail	5.10%	5.70%	3.55%	4.80%	5.60%	6.20%	3.30%
Multifamily	-	4.70%	-	4.05%	4.60%	-	-
Office	4.90%	5.90%	4.50%	4.60%	6.10%	6.60%	4.50%
Industrial/Logistics	5.30%	6.95%	6.10%	7.55%	8.30%	7.90%	5.80%

Key: **Red** = trending higher
Blue = flat
Green = trending lower

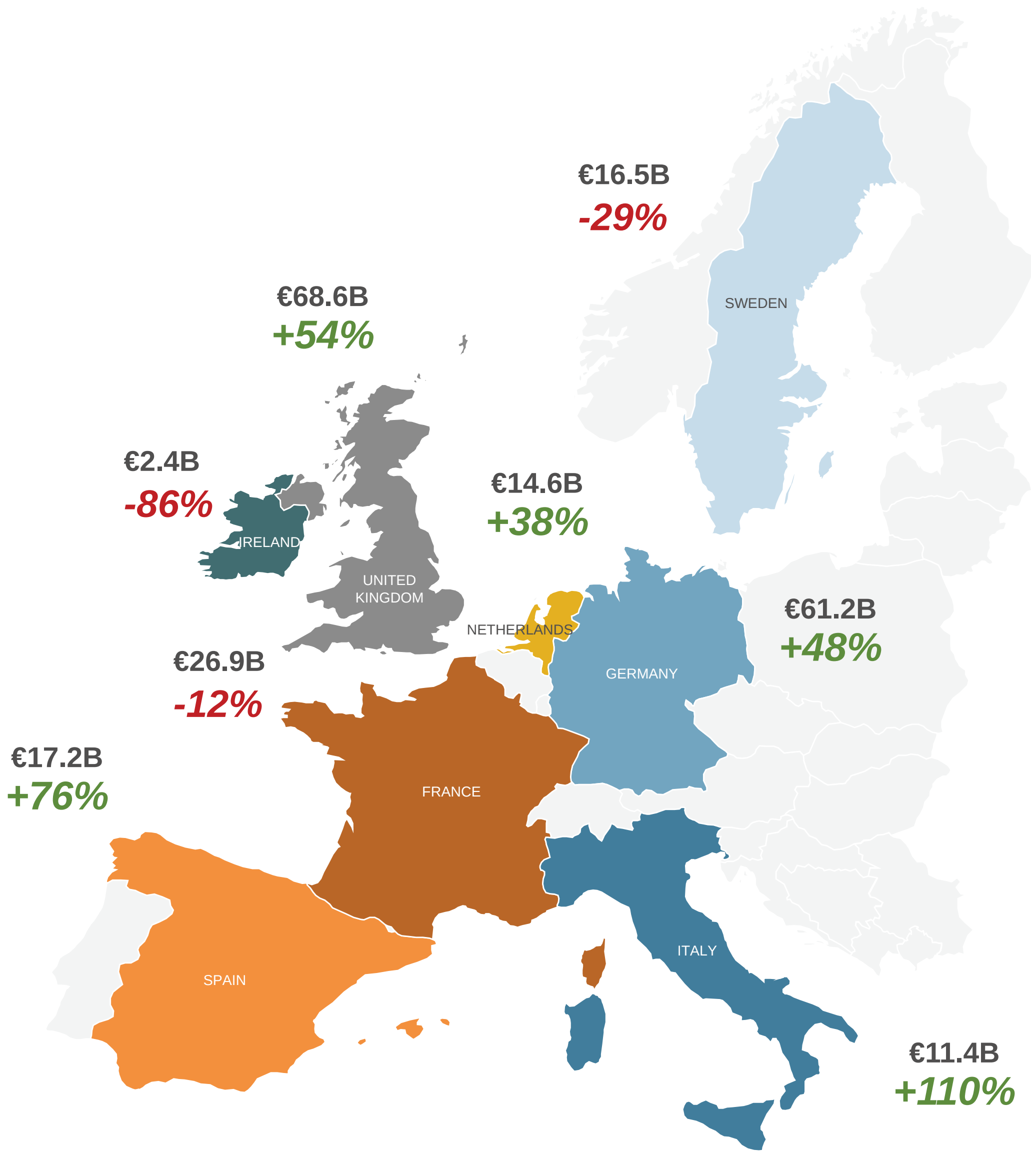
Economic Overview

- U.K. **real GDP** is expected to grow 2.0% in 2017 and 1.5% in 2018, following growth of 1.8% in 2016.[14]
- German **real GDP** is expected to grow by 1.6% in 2017 and 1.5% in 2018, down from 1.8% in 2016. Real GDP growth is supported by low unemployment, high job vacancy, strong domestic demand, and increased capacity utilisation.[15]
- French **real GDP** is expected to grow 1.7% on average over the period from 2017 to 2022, up from 1.2% in 2016.[7,14]
- Italian **real GDP** is expected to grow at a constant rate of 0.8% over the period from 2018 to 2022; however, high unemployment, low productivity, and moderate investment levels threaten the recovery.[16]
- Spanish **real GDP** is expected to grow by 2.6% in 2017, surpassing its pre-crisis GDP level. Spain has enacted tough reforms to develop a competitive and resilient economy. The unemployment rate was 18.8% as of Q1 2017—its lowest level since 2010.[17]

Sources:
9. Cushman & Wakefield Italy Retail Market Snapshot, Second Quarter 2017.
10. Cushman & Wakefield Italy Office Market Snapshot, Second Quarter 2017.
11. Cushman & Wakefield Spain Retail Market Snapshot, Second Quarter 2017.
12. Cushman & Wakefield Spain Office Market Snapshot, Second Quarter 2017.
13. Situs RERC Real Estate Report, March 2017.
14. IMF DataMapper Real GDP Growth, April 2017.
15. IMF Country Report No. 17/192: Germany, July 2017.
16. IMF Country Report No. 17/237: Italy, July 2017.
17. IMF Spain: Staff Concluding Statement of the 2017 Article IV Mission, dated July 18, 2017.

Country Overview (cont.)

The following graphic reflects transaction volume in Europe by country. We have highlighted the trends of select key countries.[18]



REAL ESTATE TRANSACTION VOLUME BY COUNTRY

Country Snapshot/What We See

- Europe posted a strong second quarter with over €74 billion in real estate transaction volume. This brings the total for the first half of 2017 to €130 billion, which represents an increase of 13% compared to the same period in 2016.
- U.K. transaction volume was impacted by BREXIT last year but has picked up this year with trailing twelve months as of June 2017 increasing 54% compared to the previous year.
- Transaction volume in France was somewhat muted during the first half of 2017, but the election of Macron as president could have a positive impact going forward.
- Italy, Spain, the Netherlands, and Germany have also seen a large volume of transactions compared to the previous year on account of stronger political and financial stability.

Map Key

Trailing twelve months transaction volume in euro (€) as of June 2017

YoY percentage increase (+) or decrease (-) in real estate transaction volume as compared to trailing twelve months from June 2016

Source:
18. CBRE – European Investment Market Snapshot, Q2 2017.

City and Sector Focus: London Office

London continues to go through a period of extraordinary change. After the Brexit referendum result, many analysts feared the worst for the London office market. However, the office investment market has performed reasonably well on the back of continued strong overseas investment as well as a reshaping of the London office landscape toward the technology, media, and telecommunications (TMT) sector.[19] Analysts and investors tend to agree that there is short-term uncertainty regarding the timing and form of Brexit, but London's long-term outlook remains strong due to its standing as a global city as well as the technological forces changing the way we live and work.[3,20,21]

Market Summary[22]

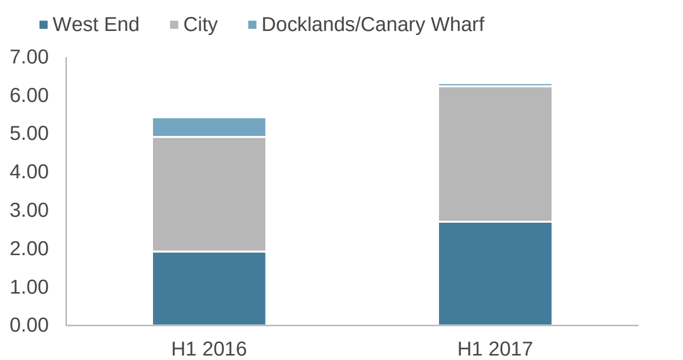
	West End	City	South-bank	Canary Wharf	Dock-lands
Vacancy	5.4%	5.2%	3.1%	5.9%	7.9%
Prime Rents	£118.00	£70.00	£67.50	£45.00	£30.00
Prime Yields	3.50%	4.00%	4.75%	4.75%	5.50%

Key:
Red = higher vacancy/yields; lower rents
Blue = flat
Green = lower vacancy/yields; higher rents
Reflects change over the prior quarter.

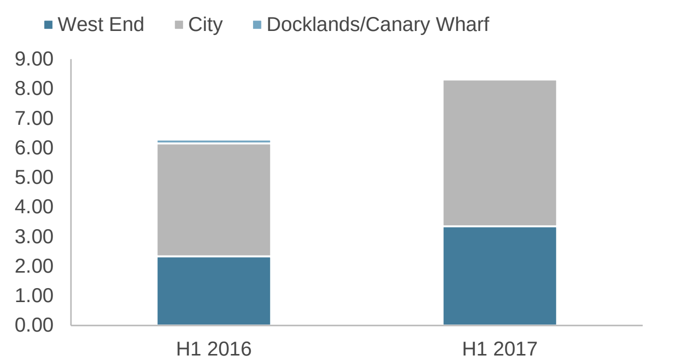
BREXIT

Brexit continues to dominate headlines in the London office market. Leading up to the EU referendum, and for some months after, both investors and occupiers of office real estate in London delayed their business decisions until they were able to gain greater clarity. There was an immediate fear that London would lose its status as a global financial centre and, thus, also lose large numbers of jobs to other EU cities. In early 2017, PwC found that around 90% of real estate professionals believed U.K. investment and property values would decline in the short term.[18] However, according to Savills, this risk "has been significantly overplayed."[23] One year after the referendum result, according to Knight Frank the market has surprised, with both demand and supply holding up to long-term averages.[18] While uncertainty persists, and London will continue to face Brexit headwinds, recent publications tend to show that London's medium- to long-term outlook remains solid.[3,13,18]

Take-Up (millions of sq. ft.)[20]



Investment (billions of £)[20]



> **"The tech revolution is perhaps of greater significance than Brexit. After all, leaving the EU is effectively a two year road bump for the London economy; whereas the coming revolution of AI (artificial intelligence), robotics, and fintech (financial technology), will reshape the very way we live. It has already created a new wave of office demand that remains active despite Brexit."**
>
> – Knight Frank, *The London Report, 2017*

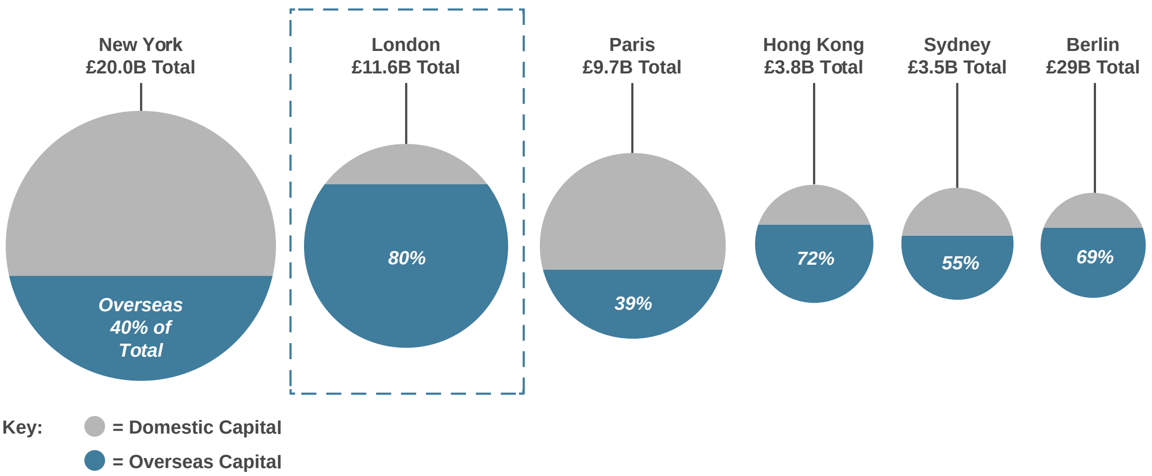
Sources:
19. Knight Frank The London Report, 2017.
20. Knight Frank Central London Quarterly – Offices, Q1 2017 and Q2 2017.
21. PwC Emerging Trends in Real Estate, 2017.
22. Colliers London Offices Snapshot, Q1 2016-Q2 2017.
23. Savills The Impact on the Central London Office Market, Brexit Briefing #2, February 2017.

City and Sector Focus: London Office (cont.)

OVERSEAS INVESTMENTS

Despite uncertainties around Brexit, Central London was the number one office market for overseas investors in 2016, attracting £9.3 billion—more than 15% above second-place New York.[17] Overseas money continues to dominate the London office market through Q2 2017, particularly in the city where approximately 85% of purchases were by foreign investors.[24] Chinese (from the mainland and Hong Kong) and German investors have been most active, according to JLL and Colliers.[20,21] Foreign investors view London offices favourably, due to often tight conditions in domestic markets, international diversification, and the fall in the pound post-Brexit. This trend is expected to continue over the next two years irrespective of the outcome of the Brexit negotiations.[13]

Select Top Global Cities by Volume of Inbound Capital[25]



Case Study

Situation

The portfolio company is a public limited company in the U.K. whose core business is the acquisition, ownership, and management of portfolios of commercial properties in the U.K. The portfolio company is also one of the largest commercial landlords in the U.K., covering approximately one million square metres, with ownership and/or management of over 750 assets located throughout the U.K.

Houlihan Lokey's Role

Houlihan Lokey was retained by a fund to provide its conclusions regarding the range of fair values of the fund's ownership interest in the portfolio company. Houlihan Lokey did the following:

- Determined the value of the investment on a sum-of-the-parts basis, which includes the valuation of the different underlying property portfolios held by the portfolio company
- Provided a valuation using market- and income-based approaches, including the market multiple methodology, the discounted cash flow analysis, and the net asset value approach
- Reviewed the business plan for the portfolio
- Identified and analyzed comparable companies in the U.K. commercial real estate segment to derive relevant market metrics and compute the appropriate weighted average cost of capital
- Reviewed recent developments and outlook in the U.K. office and commercial real estate sectors
- Provided a semi-annual report on the major findings and conclusions on the value of the investment

Sources:
24. JLL Central London Office Market Report, Q2 2017.
25. Knight Frank; Real Capital Analytics Knight Frank; Real Capital Analytics.

Valuation Services Offered by Houlihan Lokey

Portfolio Valuation Services

- Fair Valuation for Financial Reporting
- Structured Product Valuation and Pricing Services
- Derivatives Valuation & Risk Management
- Valuation Governance & Best Practices
- Securitization & Regulatory Compliance
- Fund Manager Valuation
- Fund Recapitalization & Transaction Opinions
- Portfolio Acquisition & Divestiture Services

Real Estate Valuation Services

- Real Estate Valuation & Appraisal
- Real Estate Entity Valuation
- Real Estate Due Diligence & Modeling
- Real Estate Debt Valuation
- Fixed Asset Valuation
- Market Analysis
- Fairness & Solvency Opinions
- Purchase Price Allocations
- Portfolio Valuation
- Estate & Gift Tax Valuation
- Dispute Resolution & Financial Expert Opinions
- Property Tax Valuation

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