SWECO

# SWECO CAPITAL CONSULTANTS

## Quarterly European Insights

### SCC BOILERPLATE

Capital Consultants is an independent advisor within Sweco, exclusively dedicated to real estate and infrastructure investments. Uniquely focused, our involved and approachable team strategically advises institutional investors for future-proof investments. Its Sweco's job to stay one step ahead. Our proficiency across markets is supported by Sweco's global network of technical asset expertise, positioning our team to overcome any challenge facing real asset portfolios.

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Quarterly European Insights

# MANAGEMENT LETTER

We are very pleased to share these unique market insights on the European market which have been the product of our commitment as the leading independent advisor for institutions seeking specialized knowledge of real assets. Over the past few quarters our team has grown quite significantly with a dedicated effort to channel the best in class resources from within our global Sweco network.

The approachable enthusiasm and efficiency for problem solving our team provides has become a real point of pride within the organization. Our experienced consultants not only strive to exceed client expectations, all efforts to reinvest in our people maintain our ability to stay one step ahead. We intend to maintain progress for raising the standards of our advice and appreciate all the trust our clients provide us as partners for building a sustainable future.

Hope you enjoy reading our European market insights and wish you a nice summer

Regards,

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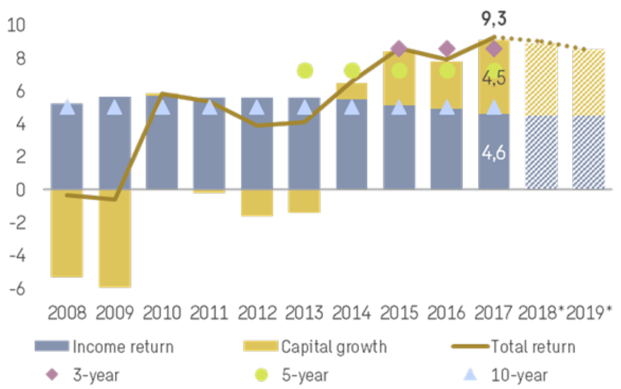
# EUROPEAN MARKET UPDATE

## ATTRACTIVE RETURNS

Overall, 2017 was a great year for investors in European real estate, with a total return of 9.3% for the eurozone (see Figure 1), up from 7.9% in 2016. Return figures were fuelled by economic growth, low interest rates and investor confidence, and driven by real estate appreciation. On a 3-year basis the eurozone index delivered an annual total return of 8.6%. The best performing cities in Europe are the Dutch cities of Amsterdam, Rotterdam and Utrecht, Madrid and Barcelona in Spain, and the German cities Berlin and Munich. In the UK, where the real estate market is traditionally more volatile, especially in the politically instable environment following Brexit, the total return, measured in local currency, rose to 9.6% in 2017 from a meagre 3.9% in 2016.

On a fund level basis, the annual return of European non-listed vehicles increased to 9.4% in 2017 from 6.0% in 2016. European funds continued their good performance in 2018, with a total return of 2.3% in Q1 2018 from 1.9% in Q1 2017. British funds saw the largest improvement in 2017, with an annual return of 9.8% up from 2.2% for 2016. Dutch funds outperformed the INREV index with a total return of 14.7% in 2017.



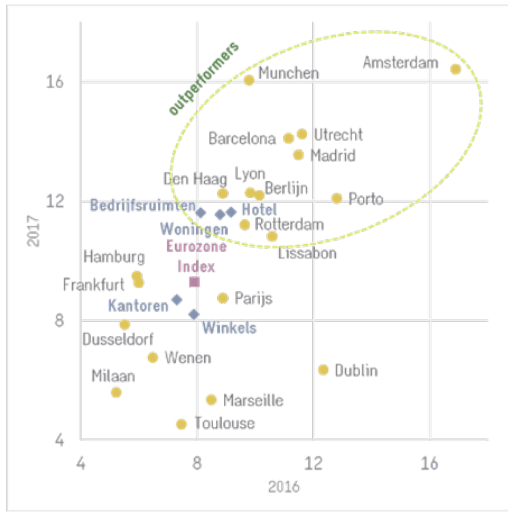




Figure 1 - Annual real estate return in the eurozone, 2008-2017, with forecasted returns for 2018-2019 (left), and outperforming cities and sector in 2016-2017 (right), in % (source: MSCI IPD; Sweco)





## LIQUIDITY AND PRICING

The pricing of prime real estate in Europe is expensive nowadays, with historically low yields in the large cities (see Figure 2). Investors therefore increasingly target value added strategies where real estate appreciation is more likely to continue. Sweco anticipates that there will be no further yield compression in the second half of 2018 for prime real estate. In secondary markets, some yield compression is still likely.

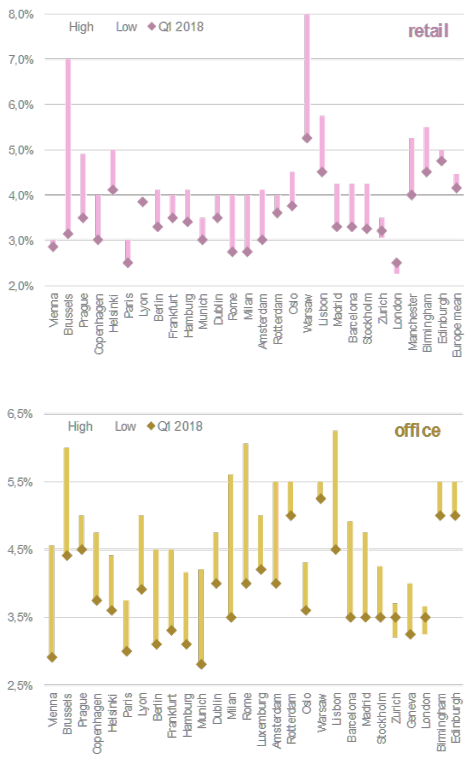



Figure 2 - Prime yields for the main European office and retail cities in Q1 2018, with a high-low for the period Q1 2015-Q1 2018 (source: Cushman & Wakefield; Sweco)

From a fundraising perspective, the number of European funds closed is declining (see Figure 3). Meanwhile, the aggregate capital raised is increasing, indicating larger funds on the market. The UK and Germany are traditionally the most liquid markets for fund raising. This is also visible in the transaction volumes on the European real estate market. The UK (€ 75.7 billion) and Germany (€ 57.4 bn) are by far the most liquid markets on a trailing twelve-month basis as of Q1 2018, followed by Spain (€ 13.8 bn), France (€ 26.5 bn) and the Netherlands (€ 19.8 bn).

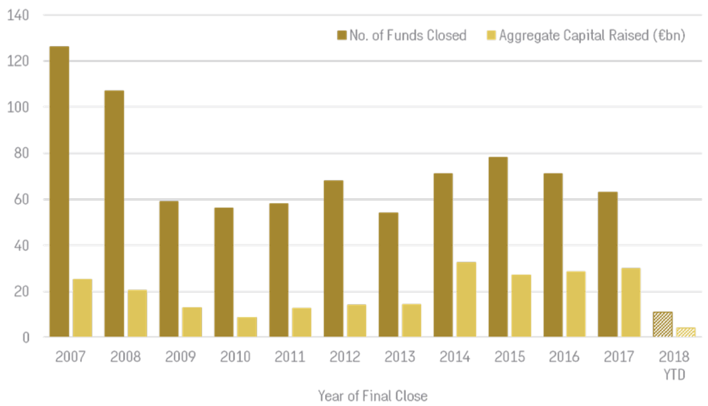



Figure 3 - Annual Europe-focused closed-end private real estate fundraising, 2007 (peak) towards Q1 2018 (source: Preqin)

## OUTLOOK

For 2018 and 2019, Sweco expects that the European real estate market remains attractive for investors from a return perspective. The income return will stabilize around 4%-5% annually, while the expected capital growth will slow down to 3,5%-4,5% in 2018 and 3,0%-4,0% in 2019. Corresponding with the overall urbanization trend in Europe and the current supply constraints, investments in the residential/multifamily, logistics and hotel sectors in the main metropolitan areas in Europe remain the most robust investment opportunities. Investors mostly target the three main European economies, UK, Germany and France, which is, according to INREV, a clear reflection of the size, maturity and transparency of these real estate markets.

# PROJECT FOCUS

## BUY SIDE STEWARDSHIP FOR DUTCH RETAIL INVESTMENTS

Sweco Capital Consultants in early July advised two of three major Pension funds alongside their investment subscriptions into the ASR Dutch Prime Retail Fund. A total issued capital of EUR 275 million between the three investors. Pensioenfonds Vervoer and Akzo Pensioenfonds utilized extensive Sweco consulting services for pre-selection and due diligence on their allocations.

The ASR retail mutual fund is focused toward the best performing areas in the Netherlands, having a target IRR return greater than 7% and ASR Nederland N.V. as the anchor investor. Overall, the Dutch retail market is still improving given the continued polarization between core style future-proof assets and more opportunistic retail assets. Dutch investor sentiment toward the retail segment has been sluggish over the past few years but is now finding its footing again.

The strategic services conducted by Sweco Capital Consultants was geared toward both a quantitative and qualitative research analysis of the non-listed retail market, further leveraged by the sustainable technical asset advice from Sweco's in-house real estate development experts. Dependent upon the rigid investments guidelines and layered capital responsibility set by the pension funds, the distinct choice emerged within the retail focus. Additionally, Sweco Capital Consultants utilized a newly developed method of classification in order to measure the extent to which the a real estate portfolio is future proof against market conditions.

Our dedication for best in class buy side stewardship of the Dutch and greater European marketplace is our continued challenge. Our clients who drive this sustainable future recognized this ambition as a source of opportunity to implement and fulfil their strategic set of goals.





# BEST PRACTICES FOR IMPACT INVESTING

Arguably real estate and infrastructure could be the hallmark asset classes for responsible investors wishing to add social impacts to their investment strategy. Relatively, social impact measurement within a portfolio is still very much in its infancy and presently holds some questionable claims which challenge investor confidence. In effort to meet investor demand for better understanding impact return on investment within portfolios, this general framework consists of a few best practices for keeping accountability between investors and asset managers.

Recent trends for social improvement and large asset privatization have contributed to a general surge in impact investment vehicles hitting the market. Regardless of the impact goal or management team, our research of integration and measurement methodologies at the portfolio level could be applied to any asset class.

Through this process, it became apparent that broad definitions for impact keep returns equally broad. So the first element to adopt is a standard that similar to any investment, impact investments must still be an instrument with the goal to generate future income or appreciation. The term Impact is commonly aligned with social improvements and philanthropic goals, which positions the main components for impact investing around calculating and accounting for the Social Return on Investment (SROI) alongside standard financial cost benefit analyses.

## CHANGE MANAGEMENT

Quite often an overlooked component to impact SROI is establishing a philosophy for change management, serving worthy for connecting the moving pieces and parties within a typical portfolio management process. Possibly more important than people connecting on social impact beliefs is making sure the philosophy adheres to the input output formats for forecasting impact in an analytical sense. Starting with the desire to take action, following with an assessment enhances SROI integrability and accountability into readable formats.

### Action Input

Input suppliers such as philanthropic groups, activists and downright doers are driving innovations for measurement. Naturally the United Nations and their 17 Sustainable Development Goals (SDG's) serve a popular alignment choice for investors wishing to add impact alongside financial ambitions. Enriching these goals, under common units of impact action for measurement is best accomplished by the assignment of Key Impact Indictors (Kii's).

### Assessment Output

In portfolio management, tools and templates for communizing units of measurement are paramount to progress. The reflective assessment raises the overall standard necessary for progress and view of impact being a successful strategy. Today's marketplace has a growing depth of data for social change, understanding impact enables the investment strategy to find stable returns.

## IMPACT PORTFOLIO INTEGRATION

Deriving model portfolio with integrated impact investments starts by utilizing common industry investment practices and overlaying SROI action and assessments in a complementing fashion. This practice of high level modelling takes a three-stage investment process around the lifecycle of an asset within a portfolio.

- **Portfolio Management Stage: Formulate Objectives**

  This strategic development of is very similar to a traditional finance equation where projected social returns should exceed their associated social costs of capital. Building this social impact formula based on Kii's should only return a premium for diversifiable social risk and return characteristics.

  **Asset Lifecycle Stage: Profiling**

  Profiling impact can be accomplished by matrixing investor risk profiles against asset risk profiles to find the overlap in strategy. Plenty of data analysis suppliers translate these number crunching and back-testing models to show social returns in capital terms.

- **Portfolio Management Stage: Implementation**

  Following the strategy with statistical analysis, scanning the asset and manager universe with target impact criteria lead into a more standardized due diligence process. Through ownership and control rights, procurement protocol and vestment periods whereby social change may have time risk should be discounted. Financial and social return due diligence may require some technical asset knowledge for Kii's integration.

  **Asset Lifecycle Stage: Procurement**

  Execution tend to fall under traditional transaction powers of procurement and the use of side letter agreements or other contractual methods for Kii adherence is generally encouraged.

- **Portfolio Management Stage: Evaluation**

  During the evaluation, strategy and implementation basic social reports like standard financial ones should show the returns across time, quantifiable both by an adapted version of net asset valuation and internal rate of return.

  **Asset Lifecycle Stage: Management**

  Asset management can foster a long relationship between investor and investee, ensuring the right mechanisms for impact performance should be validated within the management agreements. One important practice is to review social valuation methodologies on a consistent basis.

  **Asset Lifecycle Stage: Exit**

  Another commonly overlooked social impact inherit in impact investing is encouraging positive systemic sustainability. Naturally each investor seeks the most return for the lowest risk and up until now this framework had no forbearance on financial return in lieu of social impact. If ever a place to give up financial returns in pursuit of impact should be during the assets exit, where valuations, leverage and volatility stringencies be

## KEEPING MOMENTUM

Headwinds facing the impact investing confidence are generally the interoperability of products and services for standardizing impact returns. Additionally, the high variance in measurement quality potentially leaving impact strategies "green washed" if the action or assessments are made ex-ante. Therefore, these best practices should serve investors and managers with a basis to align incentives and continue progress towards an important trend.





# SWECO URBAN INSIGHTS

## CHALLENGES AND SOLUTIONS FOR THE INTEGRATION OF E-COMMERCE IN CITIES

E-commerce growth is challenging our supply chains. The existing supply chain designs are complex and are undergoing dramatic development. Many supply chains are not adapted or optimized for the anticipated increase in services and volumes. The key challenges in urban areas are the resources required, environmental and cost efficiency of last mile transport, and the location and function of facilities.

These challenges resonate throughout the supply chain and in urban planning– from warehouse design and location, delivery networks of hubs, depots and transportation, to and into consumers' private homes. Smart packaging solutions that improve fill rates, reduce waste, and enable recycling and re-use are a natural part of efficient logistics. The ineffecency of today's solutions highlights the need for innovative thinking to identify solutions for efficient distribution principles and supply chain strategies and design, integrated into urban structures. Stakeholders throughout the supply chain will benefit by looking beyond their current boundaries and interests to search for efficient solutions through collaboration, co-ordination, co-location and co-transportation.

Incorporating new trends and needs into urban planning and design will benefit citizens as well as e-commerce businesses. Stakeholders in urban logistics and those responsible for land and property planning need to be co-ordinated as future requirements are specified for urban logistics facilities' location and function. Adequate domestic logistics reception capability and capacity also need to be ensured. Logistics facilities will have different requirements for space and location as compared with more traditional set-ups.

Public authorities and other powerful stakeholders can promote and support new ideas and new thinking regarding the development of solutions for efficient distribution principles and supply chain strategies and design. Authorities can also inform citizens about the impact of e-commerce on urban areas. Logistics needs to be given high priority on the regional political agenda, and authorities can guide development through regulations and incentives to steer development in a desirable direction.

**ROBERT SOMMAR**
**Transport and Logistics Expert at Sweco**

Robert Sommar holds an M.Sc. in Automation and Mechatronics and a Lic. Eng. in Logistics, both from Chalmers University of Technology in Gothenburg, and has over ten years of experience as a consultant. He works with description, analysis and development of transport systems on the strategic and tactical level, covering rail, sea, road and intermodal transport. Robert oversaw the production of this report and co-ordinated the experts from Sweco who provided their expertise.