

Savills: Equity-rich buyers eye window of opportunity as global office market activity slows

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Investment into the world's office markets fell sharply in Q3, however, in its latest Capital Markets Quarterly report, <u>Savills</u> says that there is plenty of capital still circulating poised to target both the best assets, as well as any areas of discount, as debt-backed buyers withdraw and others pause decision-making.

Savills reports that its benchmark European prime office yields were pushed out by between 10bps (in Frankfurt) and 35bps (in Madrid) in Q3, New York saw prime office yields rise by 50bps to 5%, while they held stable for prime core office assets in Asia Pacific, although with a large dispersion, ranging from 1.7% in Hong Kong to 8% in Mumbai. But the international real estate advisor says that asset pricing remains 'sticky' in comparison with borrowing; half of the markets tracked in its report have seen the cost of debt rise by more than 200bps since Q1 2022, and it expects to see the potential for some further upward pressure on yields in the next 12 months across the majority of locations.

Oliver Salmon, capital markets analyst and director in Savills World Research, comments: "The good news is that inflation is probably close to peaking and therefore, by implication, so are market-based interest rates. But to prevent a larger correction in asset pricing, rates need to begin to come down. There will likely be some distress along the way, but there is still plenty of capital out there poised to take advantage of the current circumstances. This capital is most likely to deploy where discounts are available, or on core assets with strong fundamentals where pricing remains stable due to scarcity, and they either have the advantage through a currency play and/or through being one of only a few competing buyers in the market."



Rasheed Hassan, head of global cross border investment, Savills, adds: "Those that can most easily benefit from current pricing are those that are equity rich and have the potential to hold assets long term – most likely private capital and evergreen funds, in particular those who aren't answerable to committees. Opportunity funds are recognising value, but generally aren't unequivocally rushing in, unless they are able to find very 'special' situations. Achieving target returns without debt requires very severe asset discounting and we're not seeing that, unless the underwrite is for a sharp recompression of yields in the short term. This is hard to do for many as it is a market factor that is out of the buyer's control and is unpredictable from a timing perspective. As most of these funds are closed ended, this is challenging."

According to Savills, those investors that are active continue to be buoyed by robust leasing activity, particularly for best-in-class offices, with broadly stable vacancy rates across EMEA and Asia Pacific markets in 2022 justifying current valuations. The global economic outlook does challenge this narrative, but so far an under-supply of high quality buildings in many geographies, is keeping a floor on price declines.

To read the full report, please click here.