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Semi-annual Report Spring 2022

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This Semi-annual report is intended to provide an overview of the Norwegian commercial property market, and has been prepared by the the Company's research department, which currently consists of 8 experienced research analysts. The report was last edited 22 April 2022.

Feel free to get in touch if there is anything we can assist with.

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Chapter 1

Introduction

2022 was to be the year when the global economy recovered after two years of the pandemic. Instead we are staggering from one crisis to the next with the war in Ukraine. In its wake follow a shortage of goods, accelerating price growth and rapid interest rate rises.

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The global economy

The problems in the global supply chains were predicted to ease during 2022 as Covid restrictions were lifted, but the issues now appear to be prolonged. With Russia's invasion of Ukraine, a dangerous and chaotic situation has arisen which will challenge the global economy. Ukraine and Russia are major producers of raw materials such as grain, timber, metals and energy. As these markets have virtually become inaccessible as a result of war and sanctions, the consequences are goods shortages, additional problems in the transport chains and rising prices.

Central banks the world over are now concerned that the already high consumer price growth will only escalate. To protect its inflation targets, the Federal Reserve has announced a sharp rise in the policy rate. Our trading partners are expected to see increased activity levels this year as a result of the service sectors recovering from the pandemic. Further ahead there is a risk of significantly weaker economic growth than we envisaged going into 2022.

The Norwegian economy

High energy prices mean that Norway is making good money. This has helped strengthen the Norwegian krone in otherwise uncertain times. However, Norwegian households and businesses have to prepare themselves for high living costs, which is likely to put a damper on consumption and investment. The Norwegian central bank has announced that the policy rate will probably rise so much next year that it will hamper economic growth. Growth in GDP and employment is likely to be strong this year, boosted by the services sector and supplier industry in particular. From next year, however, the increase in activity will in all likelihood slow down considerably.

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Commercial property

A shortage of factors of production and high price growth will probably hamper building activity in the times ahead. Areas and sectors where it is more difficult to recover rising costs by increasing rents will probably be the hardest hit. A sharp rise in activity levels in the Norwegian economy suggests a strong market for office leasing this year, and the shortage of available premises is likely to reinforce rising rents in the centre of Oslo.

From next year onwards things are looking more uncertain, however. Rising interest rates are bad news for all asset classes, including property. However, real estate can serve as a hedge against inflation, which we believe will become increasingly relevant. High interest rates and funding costs can contribute to a slowing-down of the transaction market ahead, although investor interest appears to be strong for the time being.

Rising interest rates will eventually force an increase in yields on commercial property. Given the strong interest amongst investors, we still expect the increase to be dampened and delayed.

Chapter 2

ESG

Property owners currently have higher environmental ambitions than tenants

Akershus Eiendom’s latest sustainability survey reveals high environmental ambitions amongst property owners and office tenants. Yet it appears that the office is some way down the list of priorities when it comes to the corporate sustainability agenda. Furthermore, our analyses show that the supply of green buildings in the transaction market remains low and that there is fierce competition for the few properties being transacted.

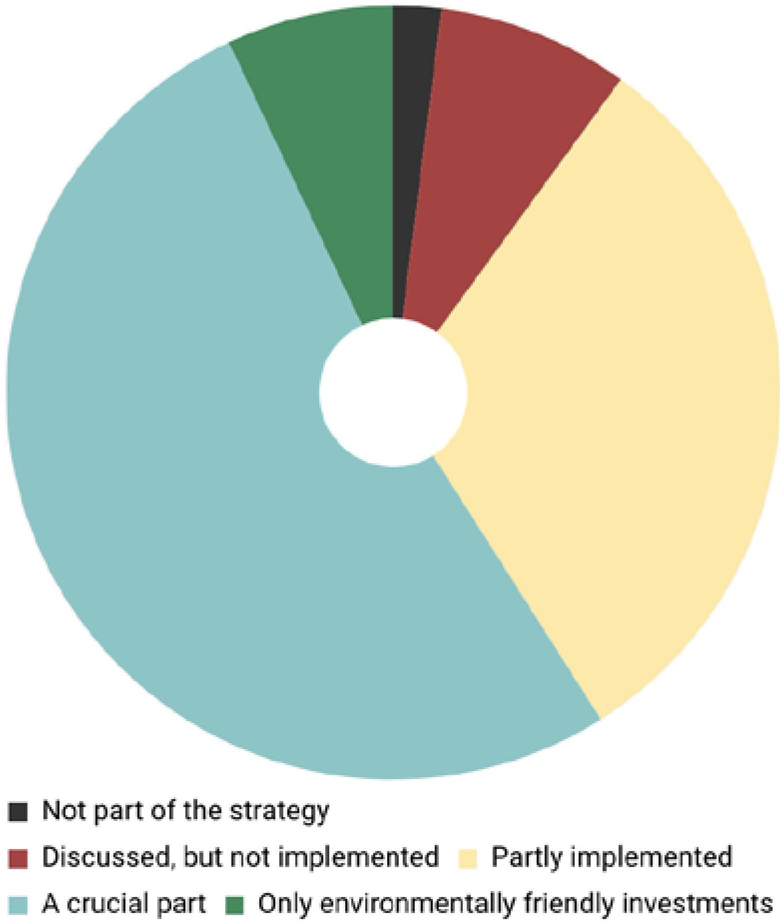
P roportion of property investors who have a dedicated sustainability officer

46%

The findings stem from three separate surveys of 150 of Norway's leading property owners, banks and tenants. Property companies, funds and syndication sponsors were all included. The property companies represent a combined gross property value of more than NOK 800 billion, and 85 percent of them have either bought or sold at least one building in the last two years. The tenants in the survey are Norwegian and international companies of varying sizes. In total they represent office demand for some 8,000–9,000 employees.

46 percent of the property investors and 52 percent of the tenants state they now have a dedicated sustainability officer. In the case of the investors, this is higher than expected considering their relatively slim organisations. The figure for tenants is slightly lower than our hypothesis suggested.

Investor: To what extent is sustainability part of your investment strategy?



60%

Proportion of property investors who state that sustainability is a vital element in their investment strategy

Proportion stating that they are willing to pay more for the most innovative sustainable buildings

84%

No fewer than 60 percent of the property investors state that sustainability is a vital element in their investment strategy, and seven percent of those say they exclusively invest in environmentally friendly buildings. A further third are in the process of incorporating ESG into their investment strategies. 84 percent state that they are willing to pay more for the most innovative sustainable buildings.

Of the 139 BREEAM-NOR certified office buildings that have been built or fully renovated in Norway, only a handful have since been sold. This implies that property owners must primarily seek to upgrade their existing portfolios or buy and develop green buildings if they are to realise their environmental ambitions. Simultaneously, it creates a scope for a green premium in the transaction market, for which we have already observed anecdotal evidence.

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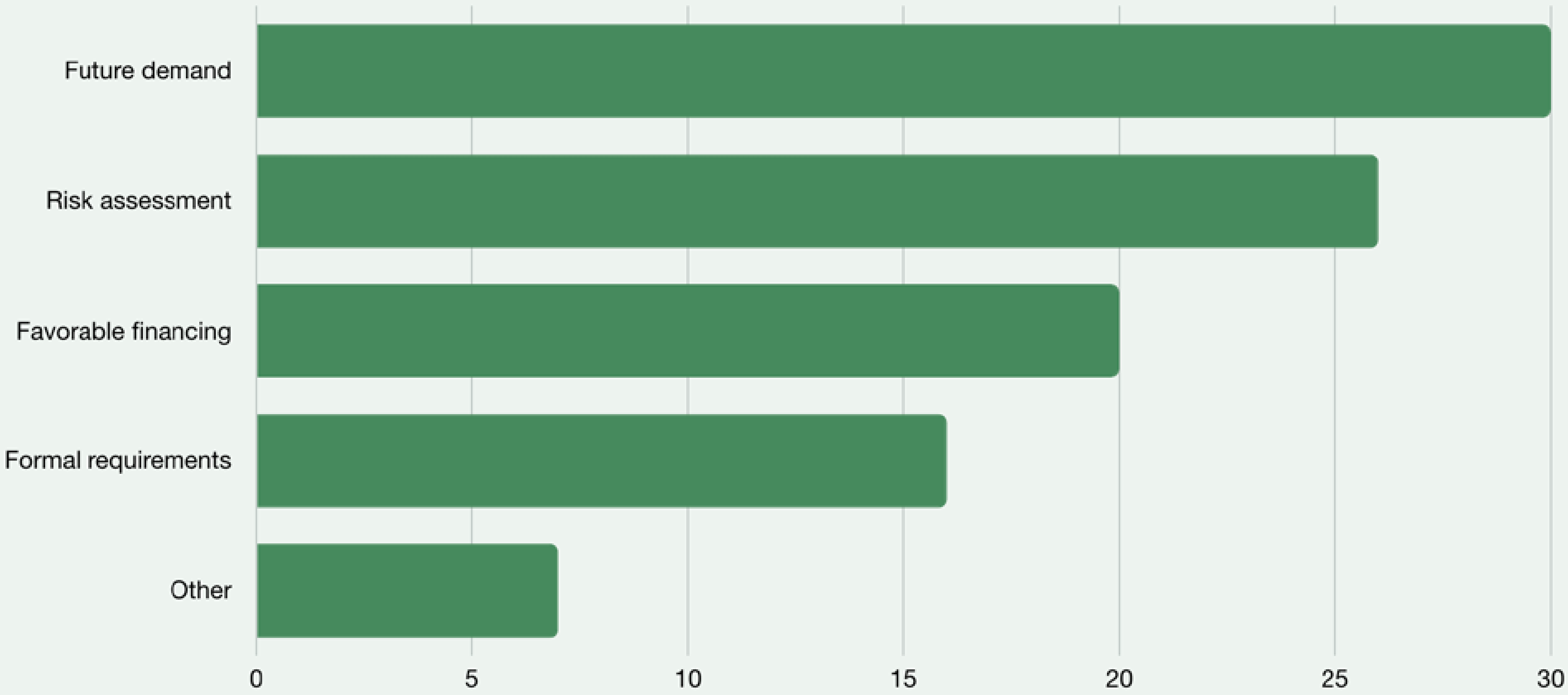
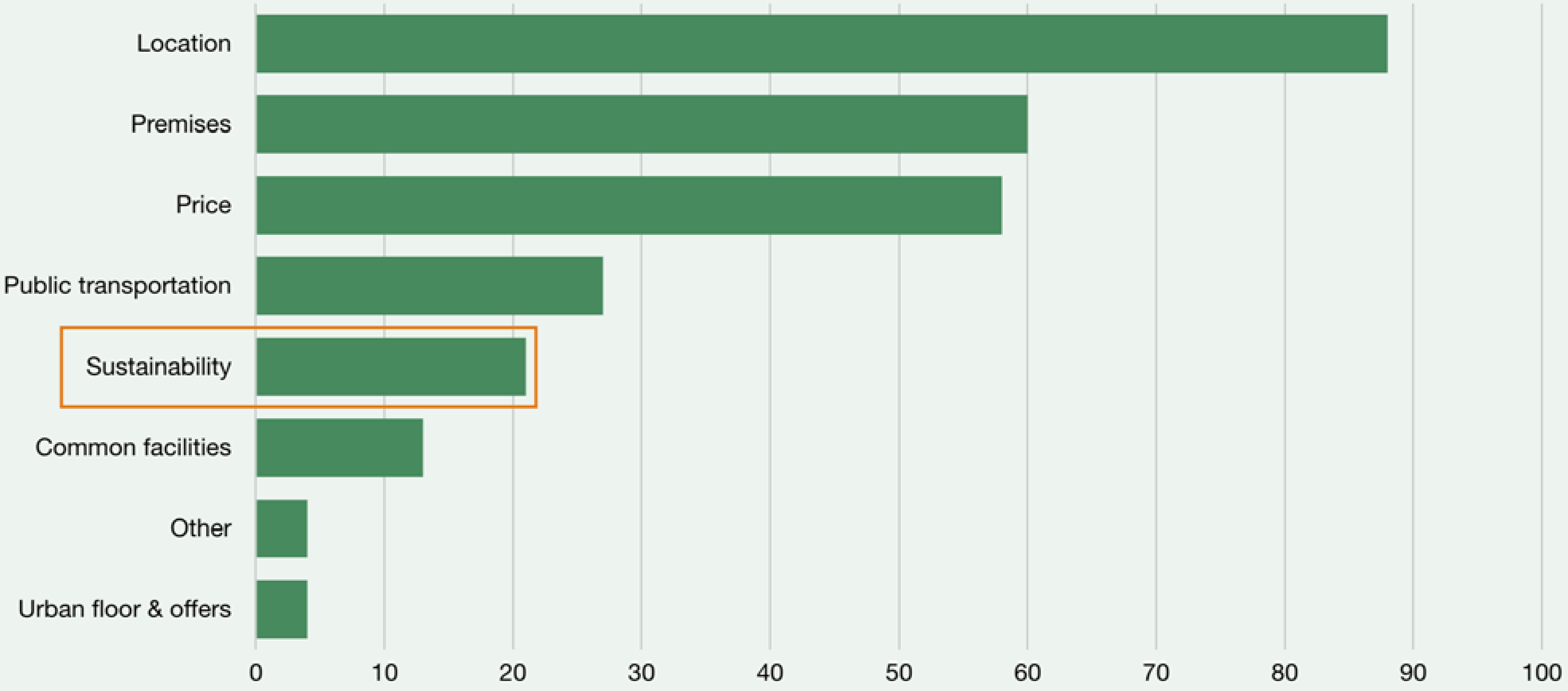
Investor: Motivation to include sustainability in the investment strategy (multiple choice), percent



Tenant: Most important criterias when choosing new offices (multiple choice), percent



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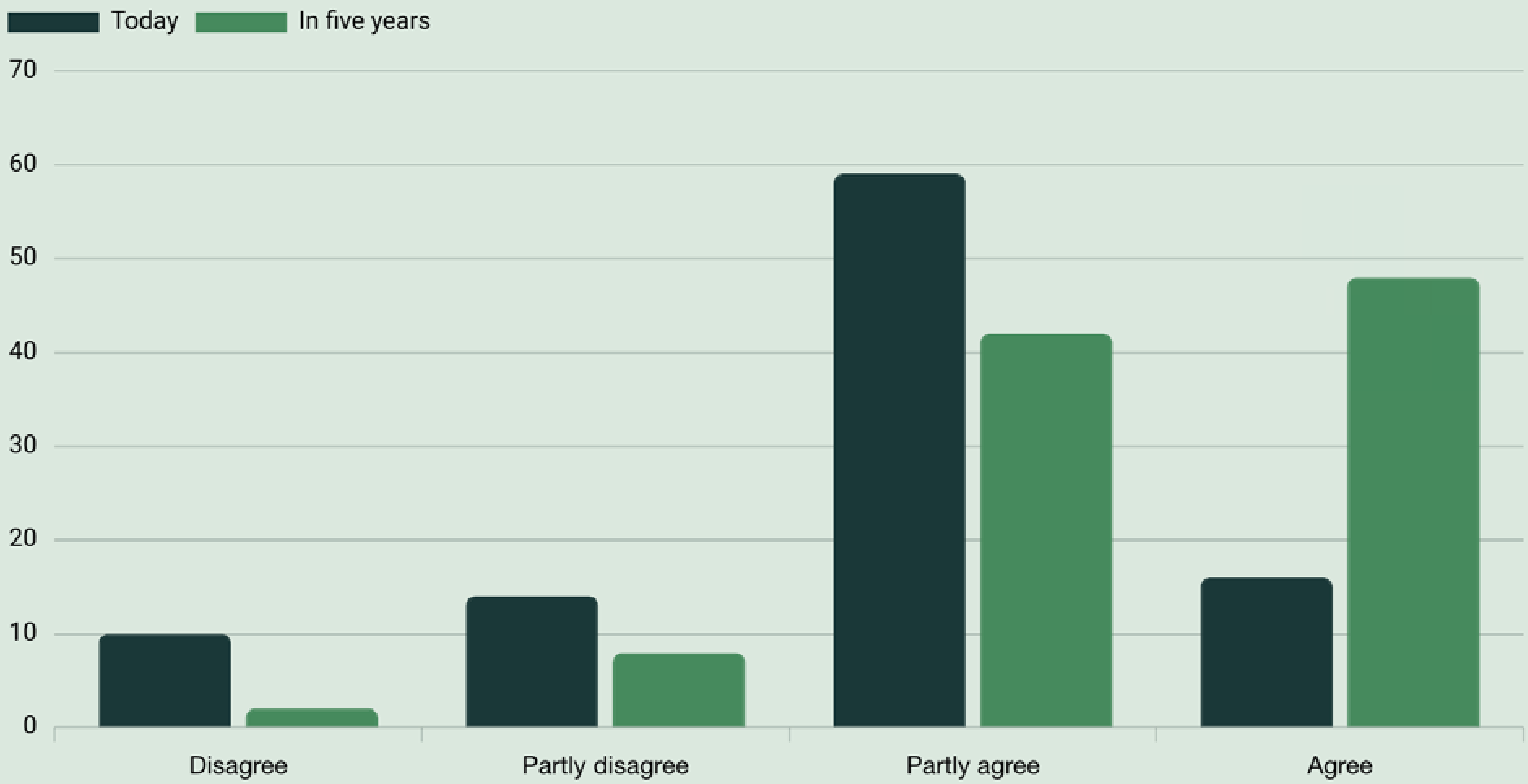
Tenant: «Choosing environmentally friendly offices is important for our sustainability work»



As many as 64 percent of the tenants responding to our survey state they have implemented sustainability as part of their corporate strategy. Yet most tenants place sustainability outside their top 3 most important criteria when choosing office space. Only when the location, design and price are right does sustainability come into play.

However, 75 percent state that office space is now a key element in their sustainability policy, while 90 percent indicate it will become important in the next five years – especially when it comes to recruitment and brand perception.

In 2021 and early 2022 we have observed an exponential growth in the number of companies certifying their sustainability goals under the Paris Agreement, so-called science-based targets. This suggests a rapid and marked shift in tenants' environmental ambitions. We expect the trend to begin to make an impact in the Norwegian rental market in the next two years. Property owners have spent several years rigging themselves for this, but further robust action needs to be taken in respect of existing buildings in order to meet future demand for sustainable offices.

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Chapter 3

Transactions

Transaction volumes reached NOK 17.5 billion at the end of the first quarter of 2022. There was an exceptionally strong, record-beating end to 2021, while the start of this year has been somewhat more tentative. Historically speaking, the first quarter is often quieter than the rest of the year, and the consensus is that the limited volume of investment is caused by diminished supply rather than dwindling investor sentiment.

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Increased policy rate, percentage points

0.25

During March and April, the policy rate increased by 0.25 percentage points, while the 5-year swap rate increased by no fewer than 88 basis points to 2.96 percent, yet there have been few indications so far of rising interest rates and higher credit spreads affecting property prices. Most transaction processes are successful, with strong interest and a large number of bidders. The war in Ukraine is obviously attracting much attention, but the impact of the war on the real estate sector is still uncertain.

NB: In Norwegian.

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NB: In Norwegian.

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Based on the current macro situation and the Norwegian central bank's interest rate trajectory, we do expect an increase in prime yields going forward – albeit not commensurate with the interest rate rises. Our analyses show increased allocation to property in the capital markets, something which helps safeguard property values despite higher interest rates. Akershus Eiendom therefore predicts changes in prime yield as follows:

2022 year end (up 10 bps from today)

3.40%

2023 (up 35 bps from today)

3.65%

2024 (up 45 bps from today)

3.75%

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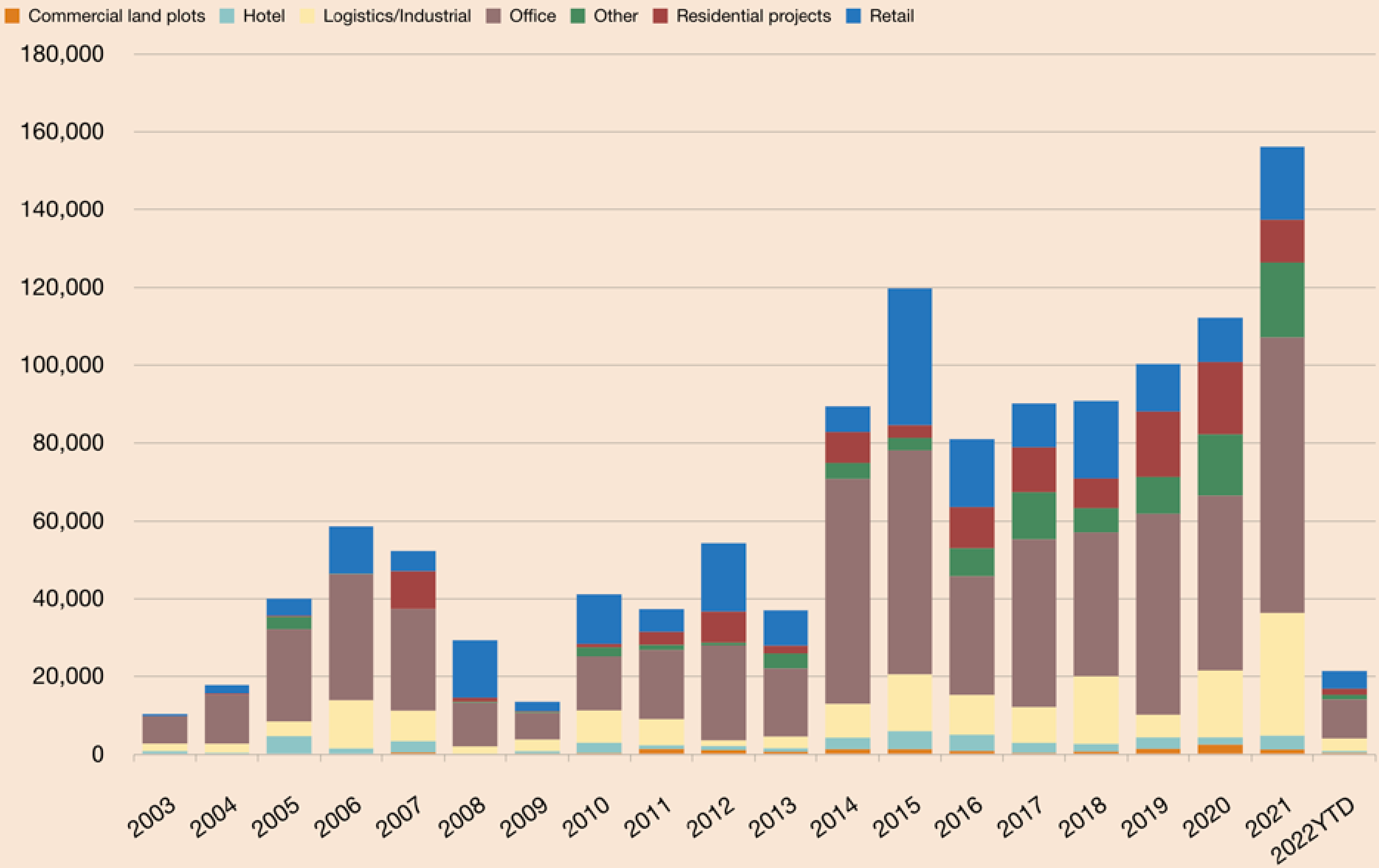
Transaction volume, NOK million



10-year gov. bond vs Oslo prime yield + forecast, percent

There are a number of major uncertainties in the times ahead which make it difficult to estimate a transaction volume for 2022 at this point in time. At the end of April, we are operating with a forecast of NOK 110 billion for this year.

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Chapter 4

Office

The commercial property sector has performed strongly in the past two years. Investor interest in the office segment still appears to be robust, albeit slightly overshadowed by the uncertainty surrounding rising interest rates and the war in Ukraine and its implications.

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Transaction market

We observed a yield compression for office buildings in Oslo in the second half of 2020 and reduced our prime yield estimate to 3.3 percent. The high pricing is a consequence of low interest rates, advantageous financing terms and easy access to equity. Strong investor interest and high pricing have prevailed throughout 2021 – a record year in which the office segment accounted for nearly 45 percent (NOK 67 billion) of overall transaction volumes.

Rental market

The office market received a notable boost in the second half of 2021 with a record number of leases signed. Office-based sectors have performed well during the pandemic, and many tenants are wanting to move and/or expand. It is worth noting, however, that we have never before observed this many renegotiations – almost 50 percent. This could suggest that many tenants are uncertain about the full impact of the pandemic and are buying time in order to decide how to use their offices in the future.

Vacancy rate Oslo

5.92%

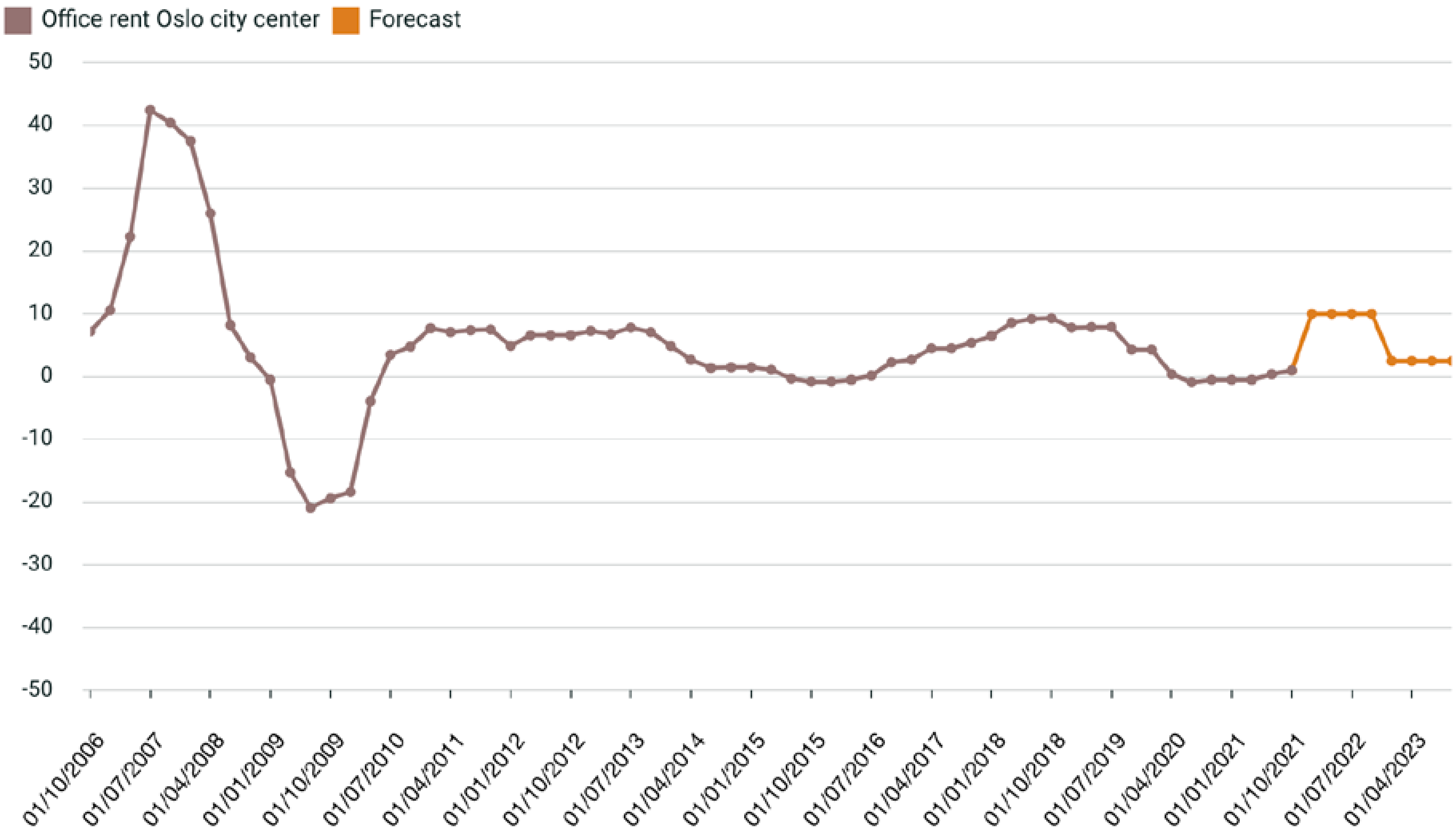
Gjennomsnittlig ledighet i Oslo sentrum

4.5%

Many office development projects were put on hold at the start of the pandemic amid fears of a more severe downturn. This has resulted in limited supply in the short to medium term. With a sharp rise in construction costs and uncertainties around deliveries as a result of the Ukraine crisis, it is likely that more projects will be put on hold in the times ahead.

Rents are being pushed up by the combination of a short supply of office space and strong demand. We are witnessing rising rents in all areas of Oslo with the exception of Nydalen. In Oslo's most sought-after office district, Vika/Aker Brygge, rents are now around NOK 5,200 per sq. m. – up by NOK 200 on the previous quarter. For more information about rents, please click here. Our latest vacancy analysis shows average vacancy rates of 5.92 percent in Oslo and 4.5 percent in central Oslo.

Office rent and forecast out 2023



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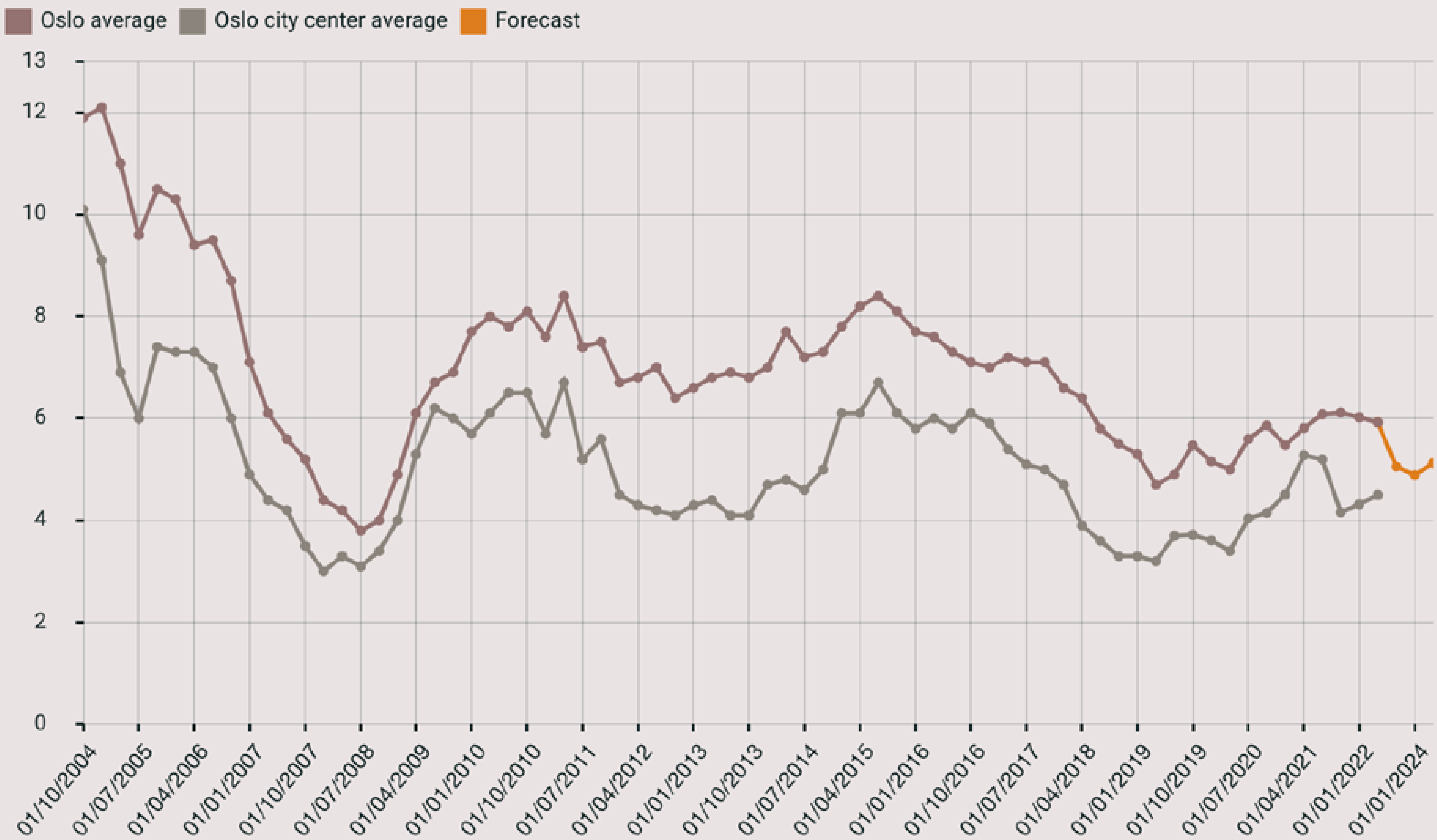
Office vacancy: Oslo average, Oslo city center average and forecast on Oslo average out 2024



Prime yield office

3.30%

Prime rent CBD, per sq. m.

5,200

Outlook

General demand for office property remains high, but due to the sharp pricing of prime office property, investors are increasingly looking to other segments for higher returns. Furthermore, we are finding that many investors are hesitating because of rising interest rates and widespread uncertainty. Yields will rise given the changes in interest rates, but the increase will probably be dampened and delayed due to high investor appetite for commercial property

Chapter 5

Regions

Bergen

Transaction volumes in Bergen totalled NOK 14.4 billion in 2021 – significantly higher than the previous year. As in the remaining part of the country, the largest segments were offices and logistics, as demonstrated by the sale of the region's largest logistics facility, Midtunbygget, in December. Prime yield in Bergen is now 3.75 percent after falling by 25 bps in the last quarter of 2021 and the first quarter of 2022. Figures from WPS Næringsmegling show that office vacancy rates have increased recently, now standing at 7 percent in central Bergen. The increase is primarily due to new office premises which have yet to be absorbed. Although rents for centrally located buildings have increased overall, prime rents have remained stable at NOK 3,200 since the end of 2020.

Bergen prime yield

3.75%

Trondheim

Norway's third largest city saw an impressive transaction volume of NOK 5.1 billion last year. Apart from offices and the Trondheim Areal acquisition, the sale of two large student housing portfolios accounted for the bulk of the total volume. The sale of Campus Life and 360 Campus involved more than 800 student units and had a combined property value of around NOK 1.5 billion. Prime yield in Trondheim fell by 25 bps in 2021 and now stands at 4 percent. Prime rents, meanwhile, increased by NOK 200 in the same period to NOK 2,500 for attractive properties in central Trondheim. 25,000 sq. m. of new office space is expected this year, which is well within the absorbed office space average of up to 30,000, according to Norion Næringsmegling.

Trondheim prime yield

4.0%

Stavanger

The commercial property market in the Stavanger region has picked up in line with increasing activity in the petroleum industry. 2021 was a record year with a transaction volume of around NOK 18 billion, in which the largest segment was logistics and industrial property. The two largest transactions last year were the sale of the data centre company Green Mountain by Smedvig Eiendom and the establishment of the new property company SVG Property with Entra, Camar and Oslo Pensjonsforsikring amongst its owners. SVG Property aims to become the leading property company in the region, and its inception involved the acquisition of Ankerkvartalet, Herbarium and Hinna Park for a total of NOK 4.5 billion. Office vacancy rates in Stavanger continue to fall, and Eiendomsmegler 1 expects rates to drop to 9.5 percent this year (down from 9.8 percent at the end of 2021). Prime yield in Stavanger fell by 25 bps in 2021 to 4 percent. Prime rents have remained stable in recent years at NOK 2,700. However, we have noted new leases attracting higher rents in some of the most attractive buildings such as the K8 tower.

Stavanger prime yield

4.0%

Chapter 6

Logistics

The logistics segment has matured considerably as an asset class amongst investors in recent years. Ever increasing e-commerce sales, the freight crisis, geopolitical tensions and increased risk in the global value chains help further underpin the segment’s attractiveness.

Transaction volumes (billion) YTD 2022 / 2021

3.8

31.3

European logistics and industrial property as a proportion of total transaction volumes has risen from around 10 percent to 20 percent in the past decade, according to figures from JLL. The same trend can be observed in Norway. Domestic and international figures both show an abundance of capital in search of logistics property, and transactions worth NOK 3.8 billion have been recorded in Q1 this year in the logistics segment. This is slightly higher than in the same period last year.

As a result of increased risk in global value chains, many logistics companies have changed their warehousing strategies in an attempt to mitigate the consequences of product shortages and delivery delays. Many firms are now seeking to stock greater volumes of raw materials throughout the value chain and store more of their finished goods closer to the end users. One direct consequence of this risk aversion is a growing need and demand for warehousing space. More information about the freight crisis and its impact on logistics property can be found in the February edition of our monthly analysis product “Innsyn & Utsyn”.

Prime yield

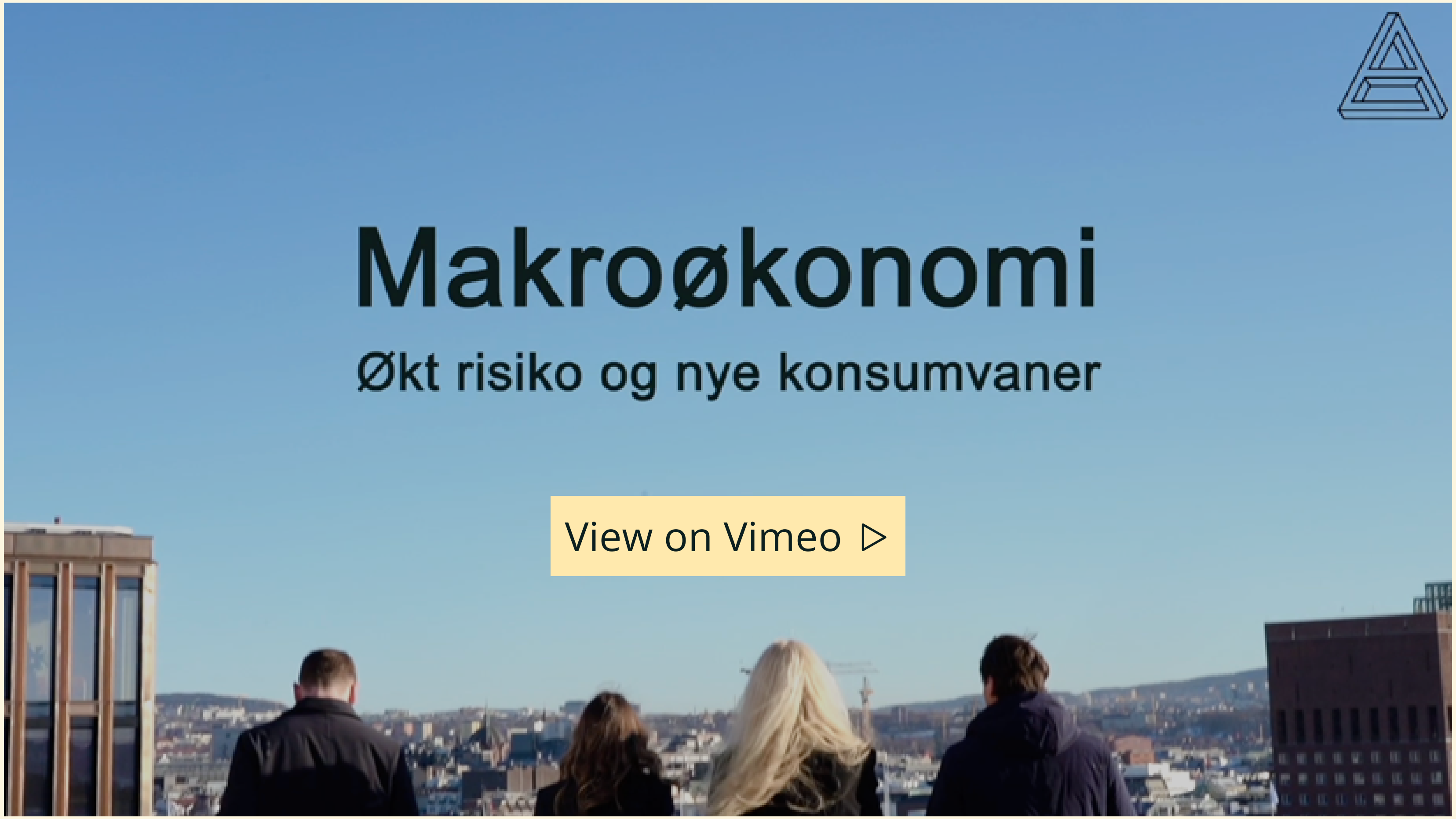
4.0%

Prime rent, NOK

1,400

There is a high level of activity in the rental market along with high demand for the most central and attractive logistics hubs in the Oslo region. These hubs have very low vacancy rates and have seen a considerable rise in rents in recent times, with rents topping out at NOK 1,400 for large warehouses (>10,000 sq. m.) in the most sought-after areas. Smaller premises nearer the city centre can achieve even higher rents. The emergence of last-mile logistics in the larger cities has done much to push up rents in strategic locations, and in some parts in eastern Oslo we are witnessing higher warehouse rents than office rents. We expect the positive logistics trend to continue, thus pushing up rents even further.

NB: In Norwegian.



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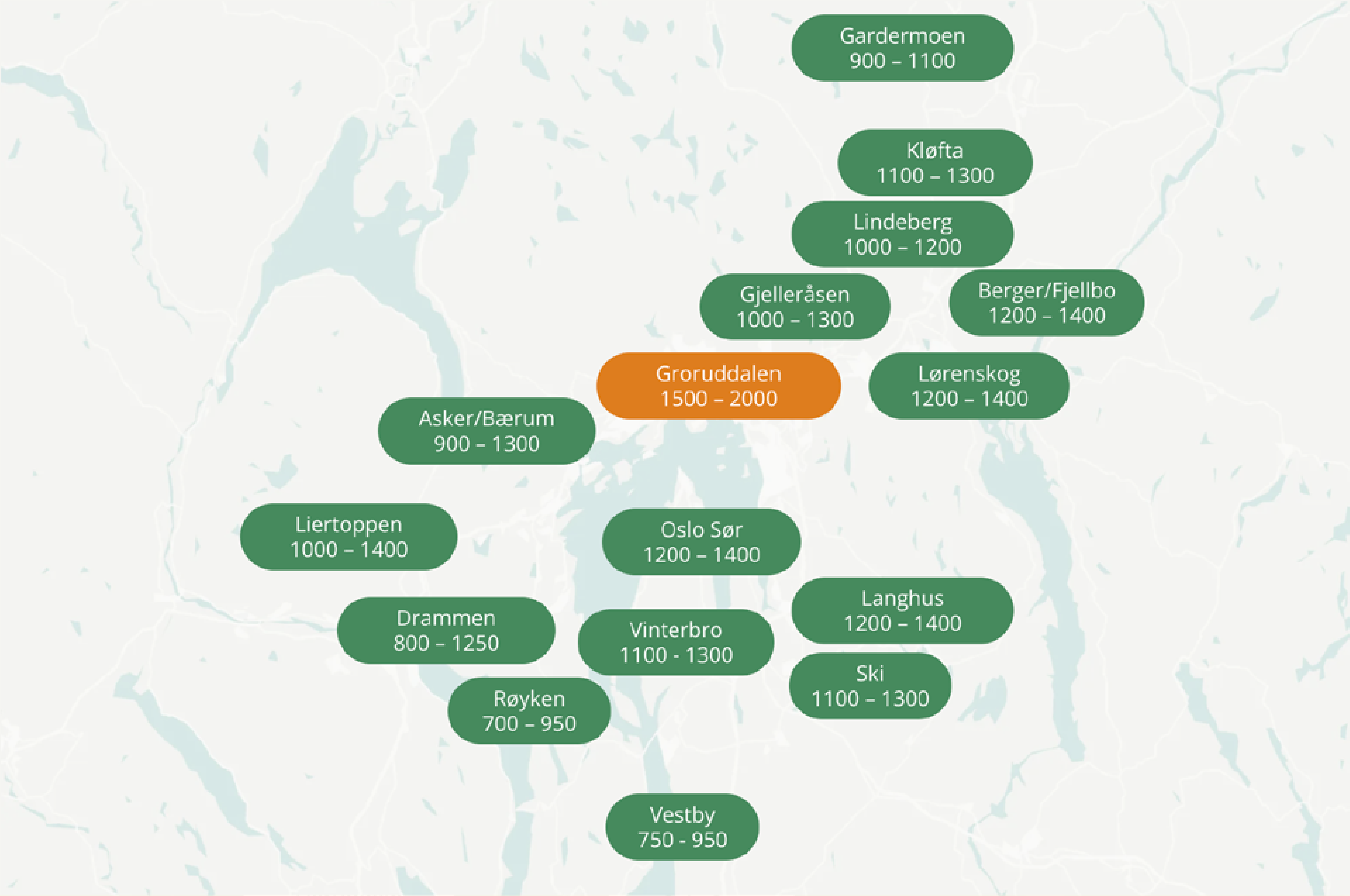
Rental price range in various logistics areas. (NOK / m²)



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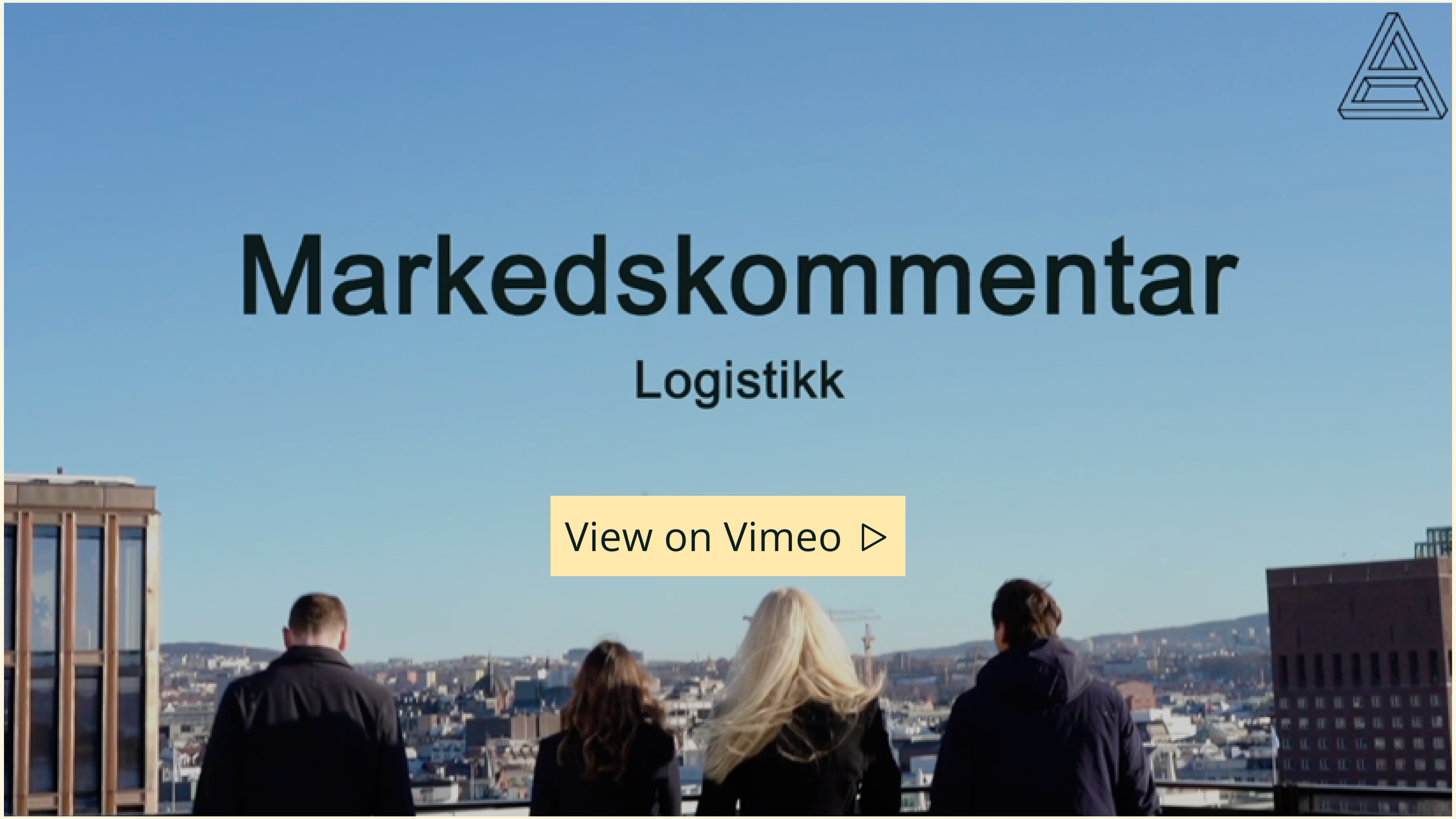
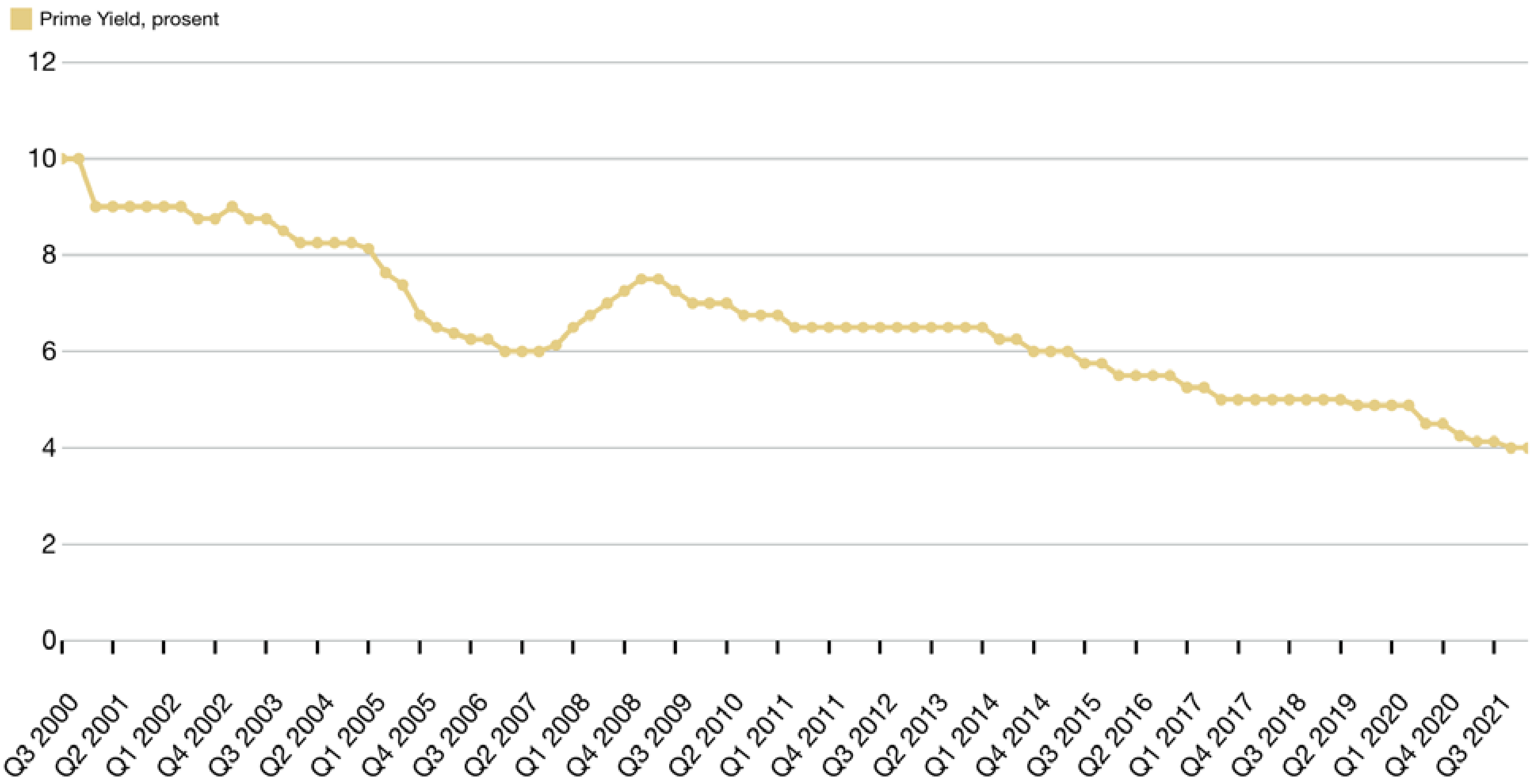
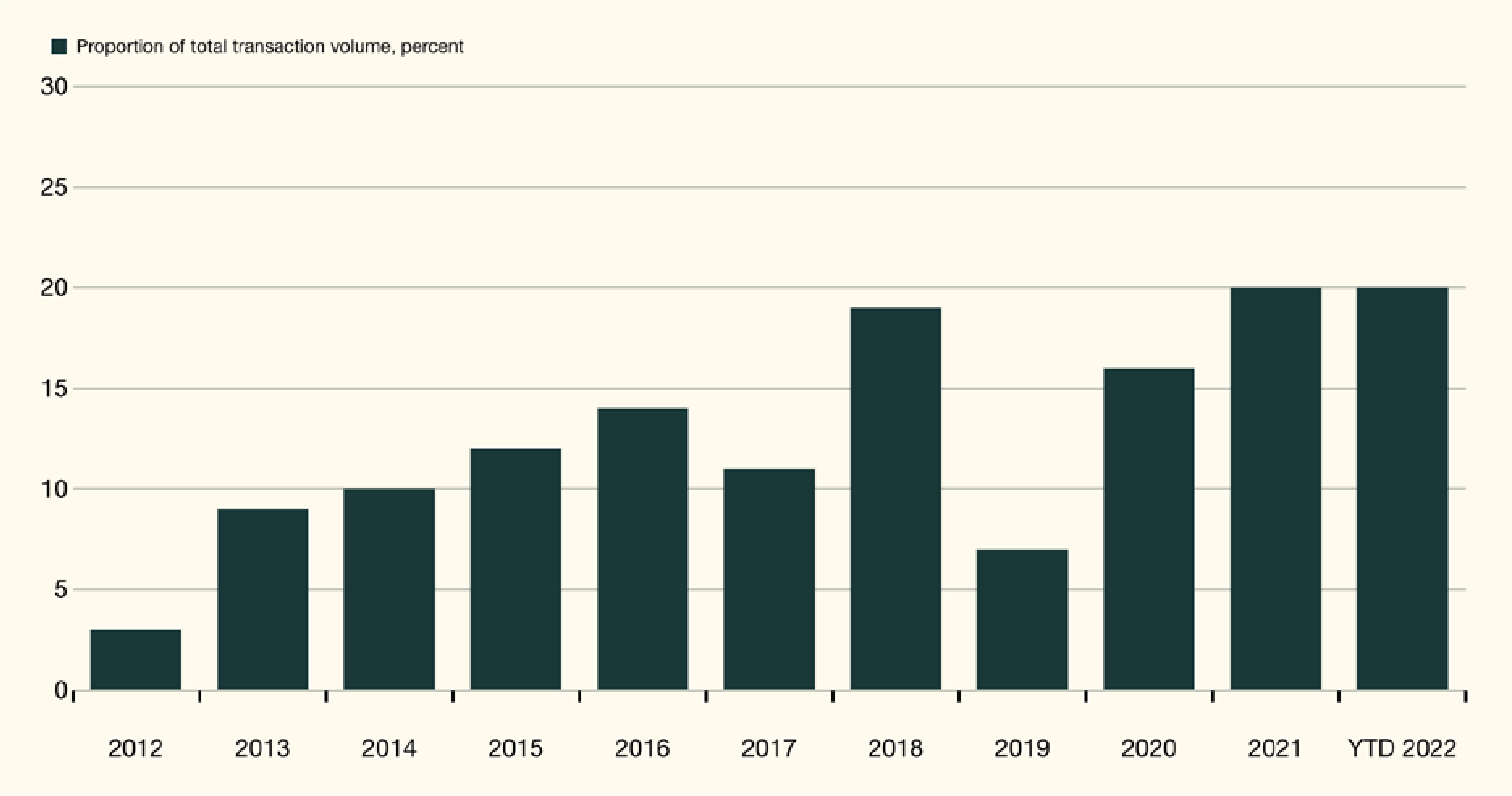


NB: In Norwegian.

Logistics prime yield, percent



Proportion of total transaction volume, percent



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Chapter 7

Retail

Retail was one of the sectors most severely hit by the pandemic. Strict restrictions to keep infection rates down brought about a material change in consumption patterns, and we spent less money on services and more on physical goods. Investor appetite has remained stable in recent years, while there has been low activity in the rental market – especially in the high street segment.

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Rental market

There has been low activity in the rental market for retail property during the pandemic, although it began to pick up slightly at the end of 2021. Despite the slump in activity levels, new leases have been signed at same rents levels as before the pandemic, which underpins our assumption of stable rent development. The highest levels of activity have been observed in the luxury segment along with the emerging electric car segment, the latter looking for central locations in Oslo and other large Norwegian cities.

Prime yield high-street

3.30%

Prime yield shopping centres

4.0%

Transaction market

Retail transaction volumes totalled NOK 18.7 billion in 2021, up from NOK 11.1 billion in 2020, and accounted for 12 percent of the total transaction volume. We find that appetite for retail property has remained stable during the pandemic, and its share of the total transaction volume was similar to 2019.

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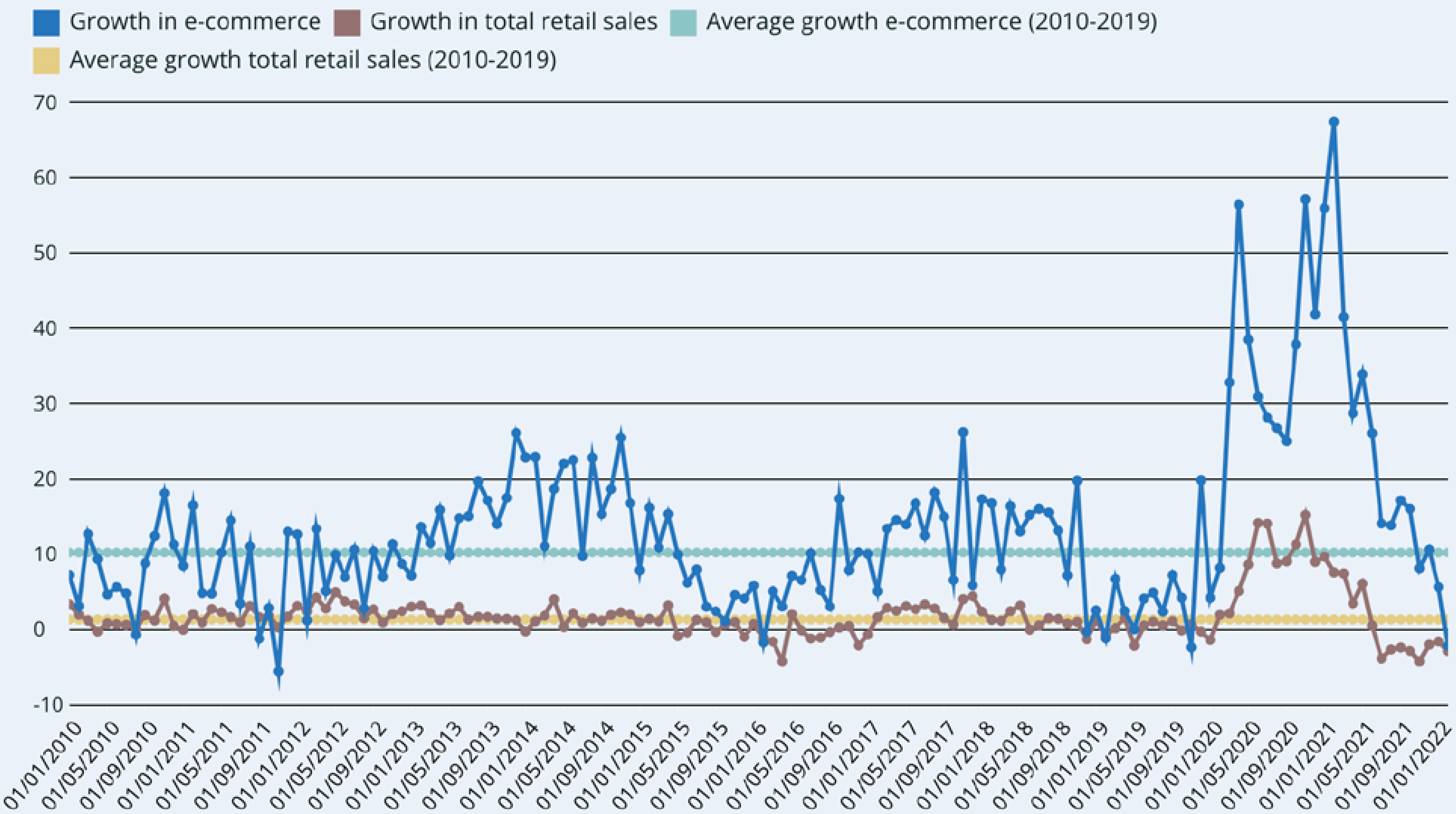
Growth in e-commerce vs total retail sales, percent



Online retail

Online shopping is nothing new, and even before the pandemic online retailers saw far stronger growth than overall goods consumption. In the period 2010–2019, online retailers posted annual growth of just over 10 percent, while total retail sales rose by just under 2 percent. During the pandemic, online growth accelerated at an annual rate which topped out at 67 percent. Moving forward we expect growth to stabilise, but at much higher rates than retail sales as a whole.

Prime yield big-box

4.0%

Outlook

The pandemic is for the most part behind us, and increased activity was expected in the retail rental market following the vacuum. However, the war in Ukraine has caused new shock waves, and the expectation that interest rates and high price growth will rise sent consumer confidence to a historical low in March. The changes in the consumption pattern that emerged during the pandemic are about to be reversed as society reopens, and it is expected that more money will once again be spent on services and less on goods.

Chapter 8

Hotel

In the past two years the hotel property market has been troubled by uncertainty and limited travel activity. The transaction market dried up in 2020, but demand recovered considerably in early summer last year. Occupancy rates have fluctuated in sync with restrictions. Room rates hit rock bottom at the end of 2020 and have since experienced a rising trend.

Transaction market

The transaction market for hotel property dried up at the start of 2020, when the pandemic struck with full force and society shut down. Uncertainty about how long the pandemic would last and when travel activity would pick up meant investors were reluctant to invest in the hotel market. As a result, we only recorded two hotel transactions in 2020.

Moving into spring in 2021, however, we noted that optimism in the market was returning, with a number of transactions completed before the summer. New lockdowns late last year and renewed uncertainty around the omicron variant meant that activity levels fell at the end of the year. Despite this, we recorded 16 transactions last year, the second highest number ever recorded.

Average occupancy rate 2018-2019

~55%

Average occupancy rate 2020-2021

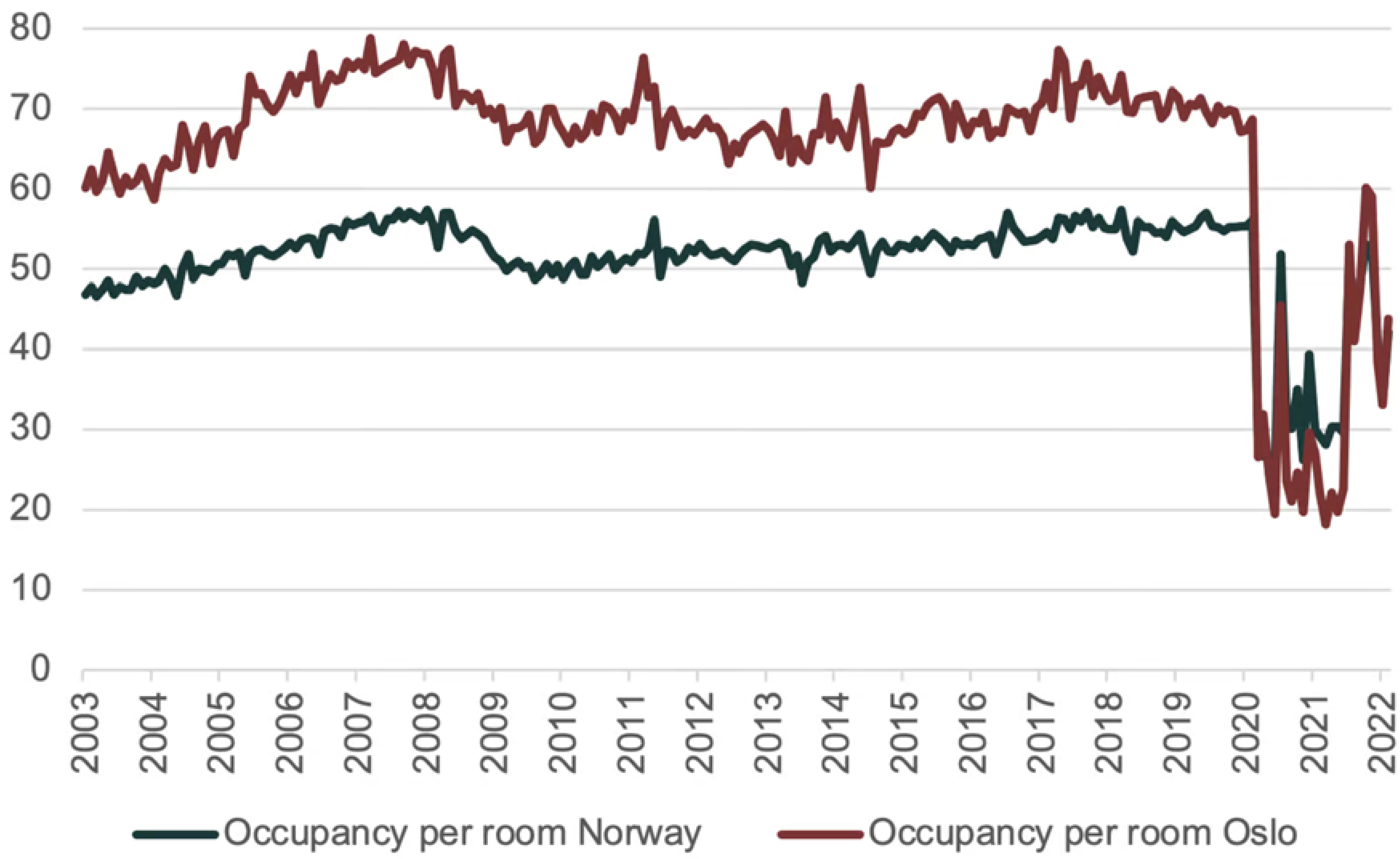
~37%

Occupancy and room rates

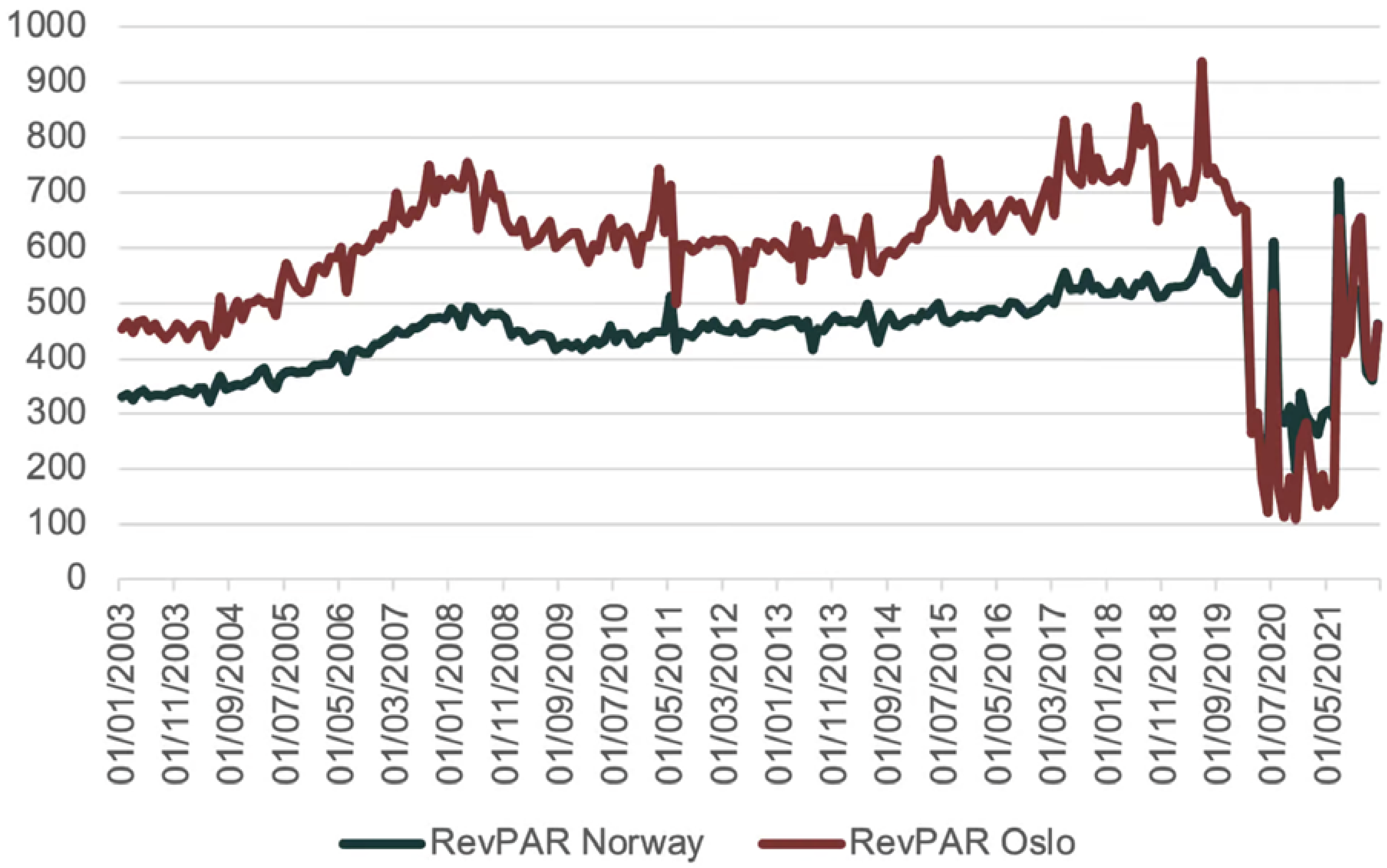
Exceptionally low travel activity since the Covid outbreak has severely affected hotel occupancy and room rates. As a result of the March 2020 lockdown, occupancy rates in Norwegian hotels fell from more than 50 percent in February to less than 20 percent in March. Occupancy rates rose sharply as the restrictions were lifted in early summer, albeit to a lower level than normally observed in the summer months. Occupancy rates during the pandemic have fluctuated as new restrictions have been introduced and lifted.

Room rates fell during 2020 and early 2021 before starting to rise last summer. Room rates are now almost back to pre-Covid levels but have fallen somewhat in recent months as a result of the latest restrictions introduced at the end of last year.

Occupancy per room – Oslo vs. Norway



RevPAR – Oslo vs. Norway



Outlook

If we avoid new Covid restrictions, we are of the opinion that investor interest in hotel property will increase, as was observed last year.

Furthermore, we consider that occupancy rates in Norwegian hotels could return to normal levels in early summer if new lockdowns are avoided.

Chapter 9

Residential

We are noting strong demand for residential property in the market, both development land plots and rental properties. The transaction market for rental properties had a record year in 2021, following a trend seen over the past three years. Housing prices have risen sharply during the pandemic as a result of less housebuilding and record-low interest rates. We now expect housing price growth to ease off as a result of increasing interest rates.

Transaction market

Investor interest in the Norwegian living sector has been growing in recent years and investment in the sector reached record levels in 2021. We are finding that a wider range of buyers are entering this market, and investors are buying into new segments in the living sector. For example, build-to-rent has become more widespread of late. We expect the growing interest in the living sector to continue.

On the other hand, the transaction volume for residential land plots was very low last year following two years of high volumes. This was primarily due to a shortage of large land plots in the market.

y-o-y growth resale property prices

6.2%

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y-o-y growth new-build property prices

7.0%

Rental market

Norway has a fairly small living sector. The country has a very high rate of home ownership as a result of political planning over many years. Around one million people in Norway currently rent their own home, which is around 18 percent of the population. In Oslo the proportion of renters is much higher at around 27 percent. The rental market has long been dominated by small private landlords, and we believe the living sector is in need of consolidation and professionalisation.

NB: In Norwegian.

NB: In Norwegian.

Housing price development

Residential building costs have spiked since the start of the pandemic – and the increase has been reinforced since Russia invaded Ukraine. At the same time, new-build prices in Oslo and the country as a whole have seen moderate growth in recent years.

On the other hand, prices for resale property increased by more than 19 percent during the last two years and is up by just under 4 percent so far this year, adjusted for seasonal variations. The sharp price growth is largely due to low interest rates, and in Oslo prices have been pushed up even further by a limited new-build volume relative to population growth for some time. The significant price growth seen so far this year can broadly be attributed to bottlenecks on the supply side as a result of more stringent rules on documentation when selling property.

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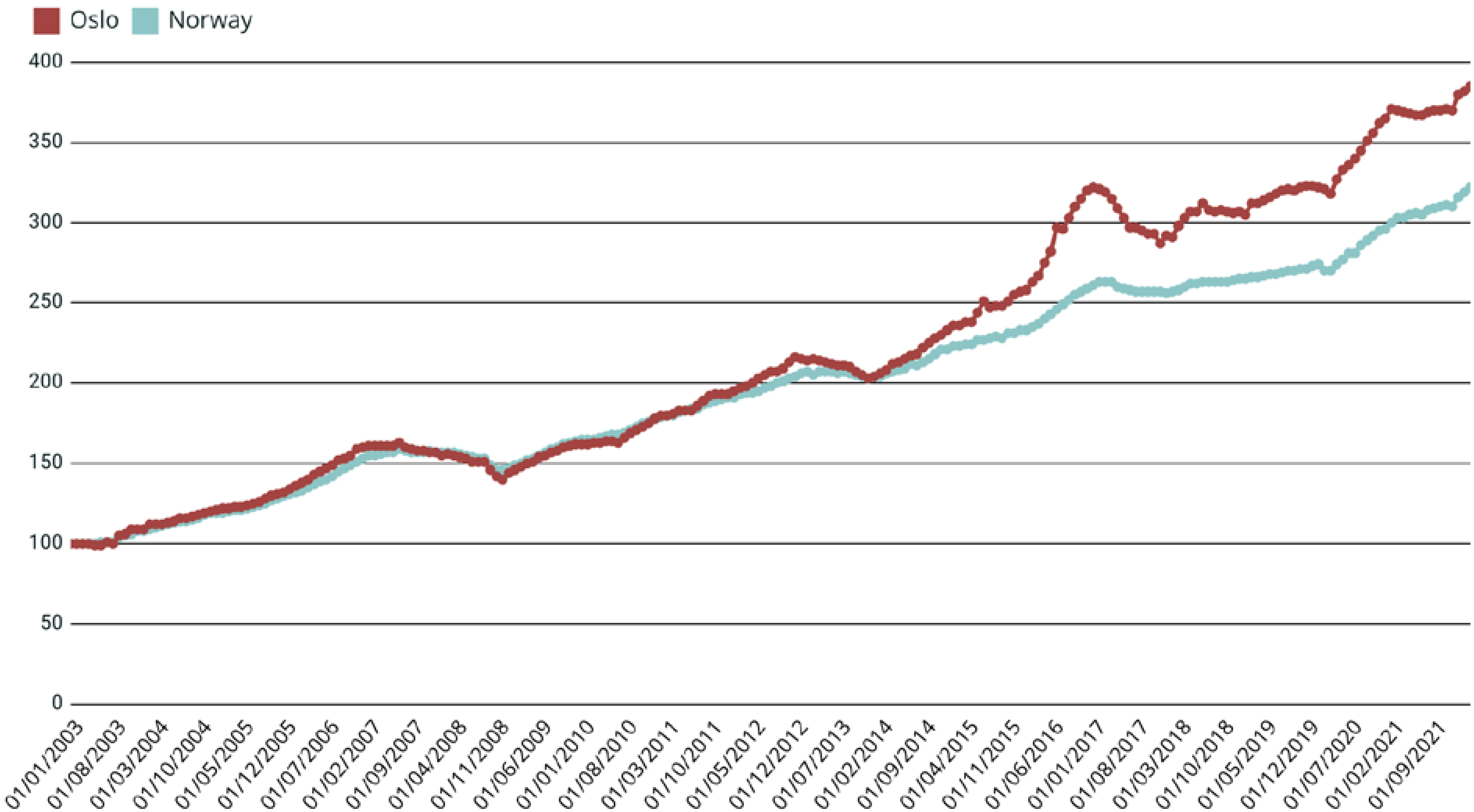
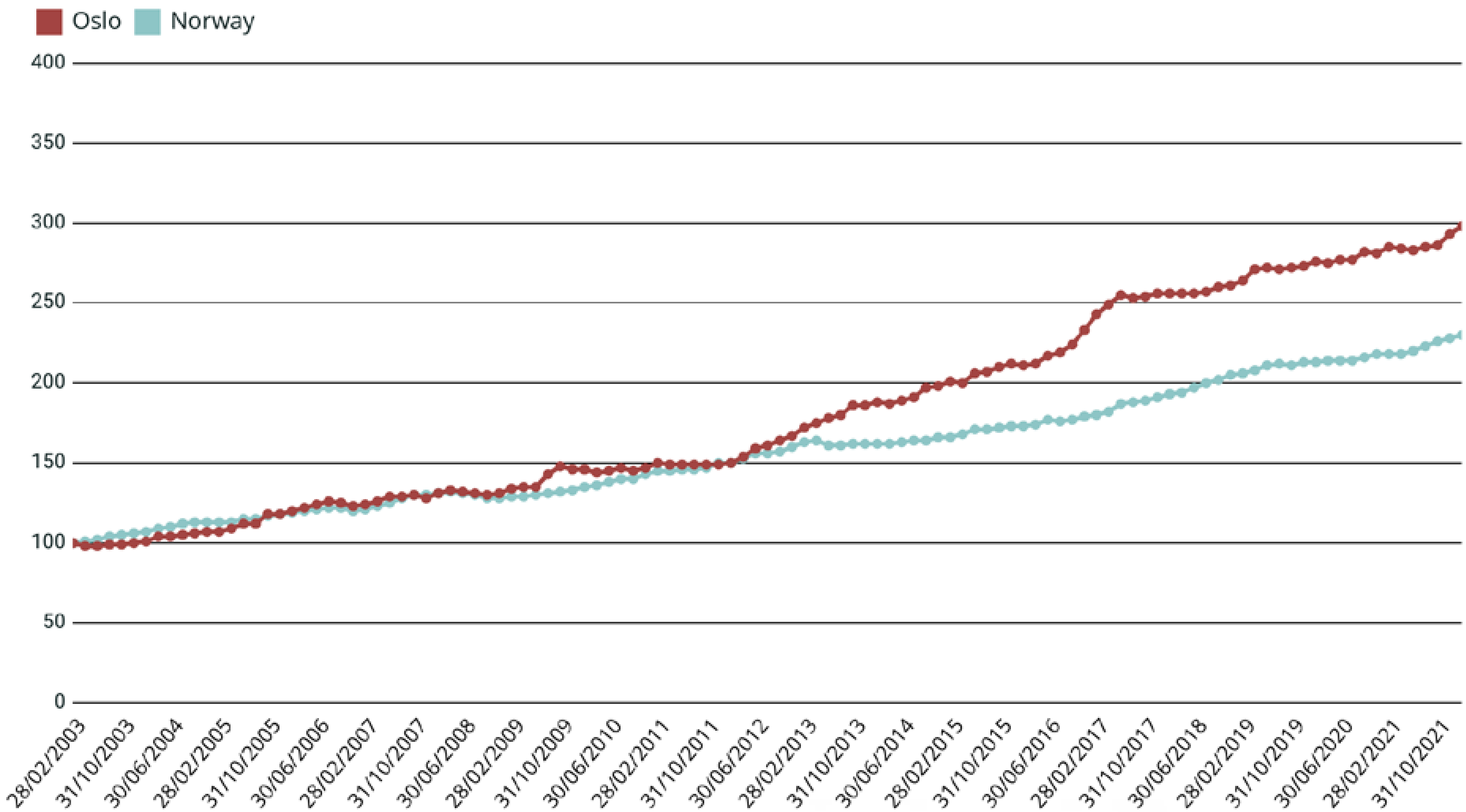
Price development resale property (seasonal adjusted), indexed



Price development new-build, indexed



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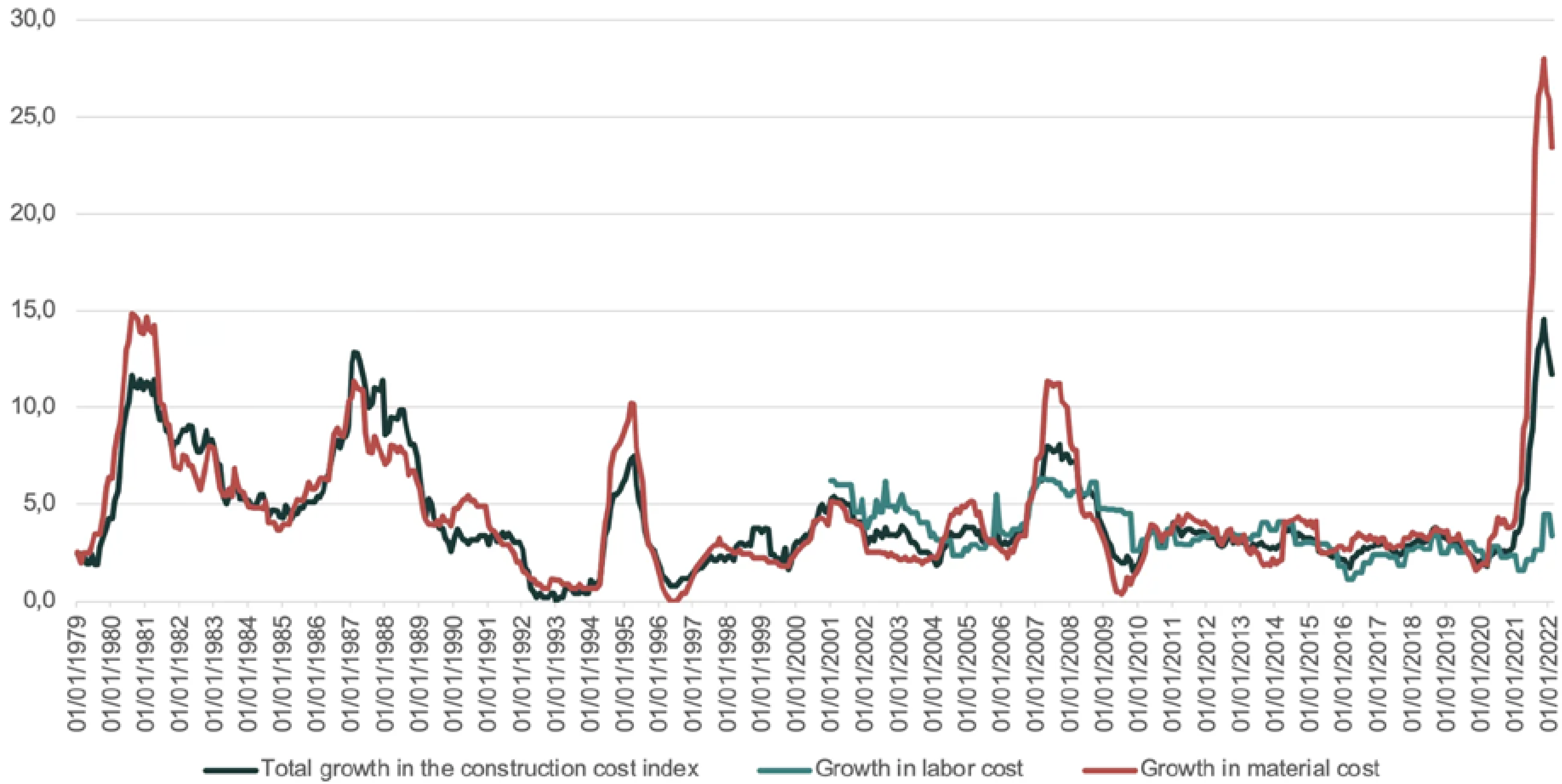
Construction cost index, incl components



Outlook

We now expect housing price growth to ease off as a result of higher interest rates, but still continue to rise.

Despite increasing building costs, we expect demand for residential land plots to remain strong and the trend of increased investor interest in the living sector to continue.