PwC-Immospektive

Interpretation of the FPRE real estate meta-analysis for May 2021
References to FPRE graphics in our text are marked with [1] etc.

GDP of 3.2% forecast for 2021, and 3.1% for 2022

21 May 2021

Economic momentum has picked up over the last few months, fuelling both trade and consumer spending. Inflation expectations have increased, which has had a positive impact on interest rates. In the real estate sector, both office and residential rents have stalled. However, A-locations are still in demand across all sectors and yield requirements continue to decline. By contrast, a great deal of caution is being shown in peripheral locations. In the short term, the construction sector is benefiting from the current euphoria, although the longer-term outlook is bleak. Demand for owner-occupied property remains high, and prices are continuing to rise.

GDP expected to return to pre-crisis level within the year

Switzerland's KOF Economic Barometer began to regain momentum in March and rose to 138 points in April, its highest level since the beginning of 2010.[1] Experts have kept their GDP forecast for 2021 unchanged compared with the start of the year at 3.2%, but lowered it slightly to 3.1% for 2022 (Feb. 2021: 3.3%) [8] These figures are thus still well above the current long-term potential growth of 1.5% [9]. The ongoing easing of lockdown measures and the progress of the vaccination campaign are set to provide a further boost to the global economic recovery and define the pace of growth.[2] Subject to the high level of risk associated with all forecasts, under its baseline scenario KOF now expects Swiss GDP to reach its pre-crisis level as early as the second half of 2021. In February it was still assuming that this would not happen until the beginning of 2022 at the earliest.[3]

The consumer sentiment index recently returned to its pre-crisis level as of the beginning of 2020, driven chiefly by the positive outlook for general economic development.[4] Private consumption has benefited from catch-up effects since the economy began to open up in March and is set to continue its recovery.[3]

There has also been a recent increase in global demand, providing fresh impetus for Switzerland's export industry.[5] There has been a sharp increase in Chinese consumption, with exports reaching record levels in March. In the USA, strong retail sales have recently led to rapid economic growth. In Switzerland, manufacturing industries in particular have benefited from rising demand, while Europe's purchasing managers' indices climbed to record levels in April.[2] There will be a delay before the recent solid economic momentum feeds through to the labour market. Although further widespread job losses are not anticipated, a degree of uncertainty remains.[3] An unemployment rate of 3.4% is now expected for the current year, slightly lower than the February forecast (Feb. 2021: 3.6%). The economic upturn will deliver a boost to the labour market in 2022. Unemployment forecasts for 2022 are also slightly lower compared with February 2021, at an average of 3.1% [8].

1 Konjunkturforschungsstelle (KOF), Medienmitteilung vom 30. April 2021: KOF Konjunkturbarometer
2 Swiss Life Asset Managers, Perspektiven Konjunktur / Mai 2021
3 KOF, Konjunkturanalyse, Prognose 2021/2022. Schweizer Wirtschaft erholt sich – Coronavirus bleibt Taktgeber
4 Staatssekretariat für Wirtschaft (SECO), Medienmitteilung vom 4. Mai 2021: Konsumentenstimmung zurück auf Vorkrisenniveau
5 SECO, Medienmitteilung vom 11. März 2021: Prognose: Zügige Erholung nach schrittweiter Lockerung der Corona-Massnahmen

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Year-on-year inflation outlook positive again for the first time since the end of 2019

The national consumer price index showed an annual inflation rate of 0.3% in April, the first positive rate for 14 months, reflecting the improvement in economic activity.[6,7] As a result, April's inflation forecasts increased by 10 basis points compared with February, to 0.4% for 2021 and 0.5% for 2022 [8]. Higher crude oil prices and the slightly weaker franc had a positive impact on the forecasts. The currency's valuation remains high, however, which is why the Swiss National Bank is continuing to pursue its expansive monetary policy. The base rate remains unchanged at -0.75% [11].[8]

Economic momentum drives up yields, particularly at the long end

Yields have recently risen worldwide on the back of a more dynamic economic outlook and higher inflation expectations. In Switzerland this has affected longer-dated bonds in particular.[9] As at the beginning of April, the yields on 1, 5, and 10-year Swiss government bonds were -0.79%, -0.63% and -0.29% respectively (January: -0.8%, -0.76% and -0.55%) [22]. The consensus is that the 10-year government bond yield is set to remain around this level until the end of 2022, with the expectations for 2021 revised upwards from -0.5% to -0.3% compared with the beginning of the year [20]. The interest rate on a 10-year fixed-rate mortgage also increased significantly in the first quarter (March 2021: 1.37%, December 2020: 1.25%), whereas rates for short-term fixed-rate mortgages rose only slightly or even fell. The interest rate on a 5-year fixed-rate mortgage was 1.09% in March (December: 1.25%), while the rate on a 3-year mortgage was 1.04% (December: 1.03%) [23].

Positive momentum in the construction sector continues at the start of the year

The construction sector maintained its momentum from the end of last year, recording another positive showing in the first quarter. The construction index rose by 2.7% (fourth quarter of 2020: 2.6%) and was thus 2% higher than in the same quarter of the previous year. The increase was primarily attributable to residential construction (+4.8% quarter on quarter). The revenue outlook in this area was down 0.9% year on year, however, while expectations for commercial construction and civil engineering grew by 4.2% and 1.5% respectively compared with the previous year [17].[10]

Increasing pressure on building construction; civil engineering sector remains robust

Despite the recovery trend in building construction since mid-2020, the sector is facing a difficult period. Although the increase in both building permits granted for residential construction and building applications for commercial construction points to a slight improvement in revenue expectations over the short term, it is likely to be a very long time before revenue figures return to the levels seen in the 2019 construction boom [16]. The sector is also coming under pressure from higher prices of raw materials such as copper, wood and plastic compared with the previous year.[11] On top of this, the sector still faces huge uncertainty with regard to the pandemic and its impact on demand for real estate space. Further investment postponements have to be expected, and these will no longer be restricted primarily to private projects, but will also affect public building construction. Civil engineering remains robust, however, raising hopes of stable revenue growth. Road construction is likely to provide the main impetus in this sector.[10]

Further rise in prices for owner-occupied property

The financing environment and the impact of the pandemic on people's housing needs are continuing to fuel demand for owner-occupied property.[12] Both supply (condominiums: -4.3%, single-family homes: -8.3%) and the length of time properties were advertised fell year on year in 2020, illustrating the demand overhang.[13] Strong demand and rising prices for owner-occupied property are also expected in the current year. The additional upward price trend is likely to tail off before long, however, due to the regulatory financing requirements imposed on banks, meaning that the price curve will increasingly flatten out.[7] Prices for single-family homes [4,57,58] and condominiums [3,63,64] rose by 2% and 2.2% respectively in the first quarter of 2021, thus driving a continued trend for higher owner-occupied property prices across the board for the time being. Transaction prices consequently increased by 6.4% (single-family homes) and 2.7% (condominiums) year on year.

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6 Bundesamt für Statistik (BfS), Medienmitteilung vom 05.05: Die Konsumentenpreise sind im April um 0,2% gestiegen

7 Credit Suisse, Monitor Schweiz / 1.Q 2021

8 Schweizerische Nationalbank (SNB), Quartalsheft 1 / 2021 März

9 Zürcher Kantonalbank (ZKB), Immobilien aktuell / April 2021

10 Credit Suisse, Bauindex Schweiz / 1. Quartal 2021

11 Handelsblatt, Medienmitteilung vom 10.05.2021: Der neue Rohstoff-Fluch: Rekordpreise lasten auf den Gewinnerwartungen der deutschen Industrie

12 ZKB, Immobilienbarometer / 1. Quartal 2021

13 Credit Suisse, Schweizer Immobilienmarkt 2021 / März 2021

The Alpine (+4.4%) and Ticino (+4.2%) regions recorded the biggest year-on-year increases in condominium prices, while momentum in the other regions was attributable to prices for single-family homes. Prices for single-family homes rose most strongly in the eastern Switzerland (+4.3%) and Jura (3.3%) regions in the first quarter of the year.[14]

Prices for owner-occupied property as much as 7% higher year on year

Broken down by price segment, prices for owner-occupied property in the most expensive bracket rose particularly strongly in the first quarter of the year (condominiums: +3.3%, single-family homes: +3.2%). Condominium prices in this segment are still 1% lower than the same time last year, however. Condominium prices in cheaper price segments also increased, but to varying degrees (low: 2%, medium: 1%) and are now up more than 6% year on year. Prices for single-family homes are also significantly higher year on year across all three price segments (low: 6.1%, medium: 5.6%, high: 7% compared with the first quarter of 2020).[14]

Residential rents lower year on year throughout Switzerland

From an economic perspective, the pandemic had very little impact on demand for rental apartments. There was a further expansion in supply over the same period, meaning that a renewed increase in the residential vacancy rate is expected for 2021.[7] There is also evidence that the pandemic is leading to growing demand for larger apartments and an increase in the attractiveness of agglomerations compared with urban centres. A reversal of the trend towards urbanisation is not currently expected, however.[13]

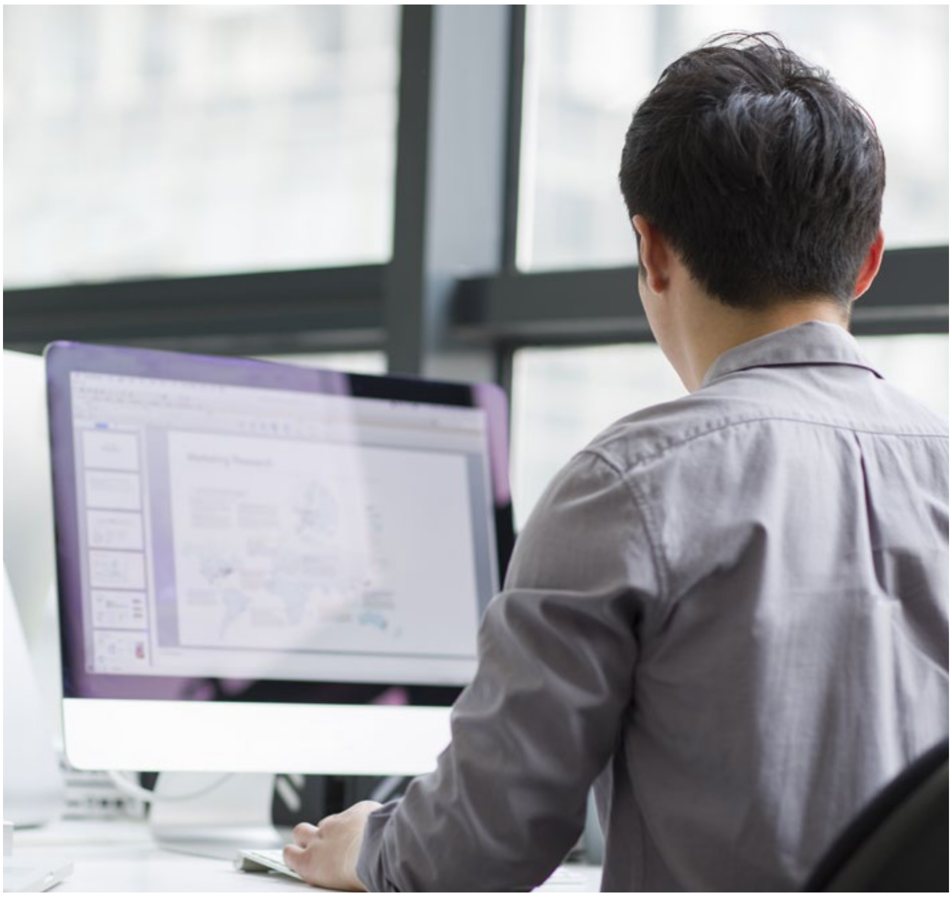
Residential rents down 2.2% year on year, further decrease in discount rates for central locations

Market rents for rental apartments (transaction rents) fell by 1.8% across Switzerland in the first quarter and were thus down 2.2% year on year [25]. The sharpest drop was in the Zurich region, where rents fell by 2.8% in the first quarter and were thus down 2.3% year on year as at the end of March. The correction compared with the previous year was even more pronounced in the southern Switzerland (-4.1%), Basel (-3.2%) and eastern Switzerland (-2.5%) regions [26]. As was already the case in the fourth quarter of 2020, rents for older apartments (-2.1%) came under more pressure than those for new-build apartments (-1.5%) in the first quarter of 2021.[15]

Despite falling rents, investors still have a strong preference for residential investment properties, and the yield requirement continues to shrink. The minimum real discount rate on a new, mid-sized residential investment property at a good micro location in Zurich fell again in April to 1.88% (January: 1.89%) [34,35]. According to an expert survey conducted by PwC in March, very low minimum yields are also expected in the cities of Geneva (2.0%), Lausanne (2.2%) and Basel (2.3%). These figures are up to 30 basis points (bp) lower than the estimates from last autumn. Declines of up to 35 bp in minimum yields were also observed outside of city centres. Experts have determined the lowest yields here to be in the Lake Geneva region (2.5%) and in the Zurich metropolitan area and central Switzerland (both 2.6%). In addition to class A locations in the Alpine (+20 bp) and southern Switzerland (+10 bp) regions, class B and C locations also tend to be viewed more conservatively. Yield expectations in these areas remained largely stable or even increased.

Office rents robust, yields for class A locations continue to fall

Investment pressure means the attractiveness of commercial space remains robust despite the increased uncertainty brought about by the pandemic.[16] Based on the building permits granted in 2020, planning activity in relation to commercial space actually rose above the long-term average last year. With a number of companies still adopting a wait-and-see approach, a decline in the expansion of floor space and rising vacancy rates are expected in 2021.[13,16] The preference for central over out-of-town office locations is also likely to intensify, as a company's choice of location is now seen as more important again in the context of motivating employees to return to the office.[13] The expert survey conducted by PwC in March 2021 also revealed that the best locations continue to do well. Since autumn 2020, yield expectations have fallen by between 10 and 40 bp in the centres of Zurich and Geneva (both down 2.2%) and of Basel and Winterthur (both down 2.6%), and in the Zurich and Lake Geneva regions (both down 3.1%). The other regions and their towns/cities are regarded with greater circumspection, however, with experts increasing their yield expectations for these locations by up to 50 bp compared with the autumn survey.



[14] FPRE, Transaktionspreis- und Baulandindizes für Wohneigentum, Datenstand 31. März 2021

[15] FPRE, Transaktionspreis- und Baulandindizes für Renditeliegenschaften, Datenstand 31. März 2021

[16] UBS, Schweizer Immobilienmarkt 1H21

Office rents in the canton of Zug up 21.5% year on year

Against this backdrop, office rents (transaction rents) presented a surprisingly varied picture. Rents in the more rural cantons of Basel-Land, Neuchâtel, Schaffhausen and Ticino recorded the strongest gains in the first quarter, rising by 4.9% in each case, while rents in the canton of Geneva fell for the fifth time in succession (-2.6% compared with the fourth quarter of 2020). The cantons of Zug and Ticino stood out in a year-on-year comparison, with rents rising by 21.5% and 13.9% respectively. Rents in the canton of Geneva recorded the strongest decrease over the same period, falling by 11.3%. Rents fell by 3.2% in the canton of Zurich and by 3.4% in Basel-Stadt [37,38]. As at the end of March, rents were down 3% year on year across Switzerland as a whole [2,36].[15]

Subdued outlook for retail sales despite good performance in the first quarter of 2021

Within the bricks-and-mortar service sector, the food and near-food segments are benefiting from the restrictions imposed on catering businesses and an increase in domestic holiday activity among Swiss people,[7] resulting in an exceptionally positive performance for overall retail sales since the middle of 2020. Seasonally adjusted real retail sales (excluding petrol stations) rose by 3% in the first quarter and were thus 10.3% higher year on year. Sales were driven primarily by the IT and communications technology equipment category (+16.2%) and the mail order and online retail category (+15.4%). The food segment also recorded a significant gain of 7.8%.[17] As soon as the situation has normalised, however, it is assumed that sales will generally settle at pre-crisis levels and then remain stable or even fall.[13]

Changes in mobility patterns are having a structural impact on the retail space market

Post-coronavirus scenarios suggest that the retail space market is unlikely to return to its customary state. Structural changes brought about by the pandemic look set to have a long-term impact on factors such as mobility and the associated foot traffic. Based on the assumption that home working will become increasingly established, there will be a reduction in passing trade in high-employment locations. By contrast, local stores and shopping centres will benefit, as these are less dependent on the surrounding employment density. There will be fewer spontaneous purchases by employees on their commute home from the office, and money will increasingly be spent at sales locations in outlying areas rather than in urban centres. Top shopping streets are likely to still perform well, however.[13] The experts surveyed by PwC anticipate peak yields of 2.5% for the cities of Zurich and Geneva and 2.9% for Berne, Basel and Lausanne. They forecast increases of up to 1% in yield expectations for regions outside the urban centres. Overall, the coronavirus pandemic is likely to have strengthened the ongoing growth of online shopping and the decline in demand for retail space. Investors will increasingly shift their focus towards logistics and industrial properties. At the start of the year, the risk/return ratio of this asset class was for the first time estimated to be higher than that of any other real estate segment.[18]

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[17] Bundesamt für Statistik (BFS), Detailhandelsumsatzstatistik – vierteljährliche Zeitreihen: Datenstand 31.03.2021
[18] JLL, Ausblick Schweizer Immobilientransaktionsmarkt 2021