

# PwC-Immospektive

Interpretation of the FPRE real estate meta-analysis for August 2021

References to FPRE graphics in our text are marked with [1] etc.

## Unemployment rate falls to 2.8% in July

### Above-average economic growth forecast

In the second quarter Swiss GDP benefited from the progressive reopening of the economy and is likely to have returned to its pre-crisis level as at the end of 2019.<sup>1</sup> Although the KOF Swiss Economic Institute's Economic Barometer for Switzerland has been falling month by month since its historical high in May 2021, at just under 130 points in July it nonetheless still points to above-average economic growth.<sup>2</sup> Indeed, the expectation for GDP in 2021 has risen compared with May and stands at 3.6% (May 2021: 3.2%) [8]. The forecast for 2022 remains unchanged at 3.1% and is therefore above current potential growth of 1.5% [9]. However, forecast uncertainty remains high in view of political and pandemic-related risks.<sup>3,4</sup>

The positive outlook that prevails at present is largely due to the recovery prospects of Switzerland's trading partners. Catch-up effects as well as fiscal policy support measures, such as those in the United States, are likely to fuel the world economy and have a positive impact on Swiss export trade.<sup>1,2</sup> In Switzerland, too, positive consumer impetus is expected.<sup>5</sup> According to the consumer sentiment index, views of the economy in general and expected financial circumstances

## 20. August 2021

The recovery of the world economy is proceeding apace and ensuring momentum in the labour market. The outlook for inflation and interest rate expectations remain stable. In the real estate sector the expansion in supply is flattening off, while order books in the construction industry nonetheless remain healthy. Owners both of residential investment properties and of owner-occupied homes continue to record gains in market value. For commercial properties location is the deciding factor.

improved significantly in the July survey compared with April, although the current situation is still judged with caution.<sup>5</sup> On the labour market there was optimism as early as the spring and in July the unemployment rate dropped to 2.8%

(May 2021: 3.1%).<sup>6</sup> The forecasts for the unemployment rate have fallen compared with May both for the current year (3.2%, May 2021: 3.4%) and for 2022 (2.8%, May 2021: 3.1%) [8].



<sup>1</sup> Swiss Life Asset Managers, Perspektiven Konjunktur / Juli 2021

<sup>2</sup> KOF, Konjunkturanalyse, Prognose 2021/2022. Der Aufschwung ist da – früher und stärker als erwartet

<sup>3</sup> Staatssekretariat für Wirtschaft (SECO), Medienmitteilung vom 15. Juni 2021: Konjunkturprognose

<sup>4</sup> Swiss Life Asset Managers, Perspektiven Konjunktur / August 2021

<sup>5</sup> Seco, Medienmitteilung vom 03. August 2021: Konsumentenstimmung klettert deutlich über Vorkrisenniveau

<sup>6</sup> Seco, Die Lage auf dem Arbeitsmarkt / 09. August 2021



## Inflation forecast for 2021 remains at 0.4%

In July the national consumer price index fell by 0.1% compared with the previous month but it continues to point to a positive rate of change for the year (0.7%).<sup>7</sup> Crude oil prices in particular have risen sharply since the start of the year, intermittently adding to pressure on domestic inflation.<sup>8</sup> The consensus inflation forecast, however, is stable against May both for 2021 at 0.4% and for 2022 at 0.5% [8]. The Swiss franc's valuation remains high, which is why the Swiss National Bank is continuing to pursue its expansionary monetary policy. The policy rate remains unchanged at -0.75% [11].

## Capital market rates and interest rate forecasts stable

Robust economic prospects and a stable inflation outlook led to another increase in yields on government bonds in the second quarter of 2021 – particularly for longer-dated paper. In June the yields on one, five and ten-year Swiss government bonds were -0.78%, -0.52% and -0.13% respectively (April 2021: -0.79%, -0.63% and -0.29%) [22]. However, the forecasts from the State Secretariat for Economic Affairs, KOF and Créa for 2021 and 2022 for the yield on ten-year government bonds remain stable on average [20]. Interest rates on three, five and ten-year fixed-rate mortgages also remained almost unchanged in June at 1.04%, 1.09% and 1.35% respectively compared with March (1.04%, 1.09% and 1.37%) [23]. Unless the European or US central bank should indicate a switch away from

their negative interest rate policy, no major corrections in Swiss capital market rates are to be expected in the near future either.<sup>9</sup>

## Construction index loses 1.5% despite healthy order books for builders

Following two positive quarters, the construction index declined by 1.5% in the second quarter of 2021 [17]. This is predominantly attributable to the building construction index with a 5.3% drop in turnover expectations. Anticipated turnover fell by 3.5% in residential construction and by 1.2% in commercial construction. This meant that expectations for commercial construction turnover were still 13% above their prior-year level, while in residential construction they were down 2.6%.<sup>10</sup>

## Civil engineering continues to support the construction sector

Although construction order books remain healthy in both subsectors, declining numbers of building permits point to a decline in turnover in the medium term [16]. The building industry remains under pressure from delays in

deliveries and price fluctuations for some building materials. Turnover in civil engineering, by contrast, continues to benefit from major public civil engineering projects, and the index was up 2.2% over the previous quarter. Turnover expectations are 5.6% higher year on year.<sup>10</sup>

## Price increase for owner-occupied homes is flattening off a little

Owner-occupied residential homes remain sought after and equally in short supply.<sup>11</sup> Planning applications and building permits have been falling recently.<sup>10,12</sup> At the same time, demand remains high and residential property prices are likely to rise further. The demand for single-family houses received an additional boost from the pandemic as they usually offer more outdoor space and are roomier than apartments.<sup>11</sup> Because financing requirements remain stringent, the price increase is expected to flatten off.<sup>13</sup>

Prices for single-family houses up 7.5% year on year, owner-occupied apartments up only 3.8%

This trend can already be observed in the last quarter. The price increase for owner-occupied property weakened slightly compared with price movements in previous quarters, with a rise of 1.3% (fourth quarter of 2020: 1.9%; first quarter of 2021: 2.1%). Prices for owner-occupied apartments [3, 63, 64] recorded an increase of 1.0% (first quarter of 2021: +2.2%), while single-family houses [4, 57, 58] rose by 1.5% (first quarter of 2021: +2%). This means that prices for owner-occupied apartments were 3.8% higher year on year and prices for single-family houses were 7.5% higher. In regional terms, prices last quarter rose most sharply in the Jura (+2.8%) and Geneva (+1.7%) regions; however, prices in all regions were up year on year. Only in the southern Switzerland and Alpine regions did prices for owner-occupied apartments rise more than those for single-family houses. In sectoral terms, residential real estate prices in the most expensive price segment once again experienced the sharpest increase

<sup>7</sup> Bundesamt für Statistik (BFS), Medienmitteilung vom 02. August 2021: Landesindex der Konsumentenpreise im Juli 2021

<sup>8</sup> Schweizerische Nationalbank (SNB), Quartalsheft, 2/2021 Juni

<sup>9</sup> Raiffeisen, Immobilien Schweiz / 2Q 2021

<sup>10</sup> Credit Suisse, Bauindex Schweiz / 2. Quartal 2021

<sup>11</sup> Wüest Partner, Immobilienmarkt Schweiz 2021/2

<sup>12</sup> Credit Suisse, Immobilienmonitor Schweiz / Juni 2021

(owner-occupied apartments: 1.3%, single-family houses: 2.5%). Lower-price segments rose more moderately in the second quarter or prices actually fell slightly (owner-occupied apartments, low-price segment 1%, medium-price segment 0.8%; single-family houses, low-price segment -0.4%, medium-price segment 1.2%).<sup>14</sup>

### Expected yields on residential real estate fall again

In some Swiss towns and cities, the number of planning applications for residential real estate has risen since 2018, although on a national level it has dropped. According to analysis carried out by the Zürcher Kantonalbank, this reflects a reaction on the part of investors to the regional disparity between supply and demand.<sup>13</sup> However, current construction activity remains at a high level and is thus an indicator that rents being offered are likely to follow the trend of the last six years and, with stable net migration, will probably fall even further [12, 13].<sup>11</sup> In the second quarter, however, net income increased nationally (+1% in the second quarter of 2021) and the proportion of market participants expecting the price curve to invert and rents to rise has increased [30].<sup>15</sup> Irrespective of which way rents go, investors still have a strong preference for residential investment properties because of the pressure to invest, and yield expectations continue to decline. The minimum real discount rate on a new, mid-sized residential investment property at a good micro location in Zurich was lower in August at 1.81% than in April (1.88%) [34, 35]. Market values for multi-family dwellings rose by 0.8% nationally in the second quarter as a result of increased net income and falling yields [27]. The sharpest market price gains in the second quarter were recorded in the Geneva (1.3%) and Basel (1.7%) regions. Year on year, properties in the Zurich area rose particularly sharply (1.4%), while properties in the Alpine (-1.8%), southern Switzerland (-1.7%) and central Switzerland (-0.6%) regions declined in value.<sup>15</sup>

**Rents for apartments rose by 0.8% in the second quarter of 2021, following a fall of 1.8% in the first quarter**

In the second quarter, market rents for rental apartments (transaction rents) were up 0.8%, after falling across the board at the beginning of the year (-1.8% in the first quarter of 2021) [25]. As in previous

quarters, rents for new-build apartments (1.4%) are under less pressure than those for existing apartments (0.1%). Except in the Basel region and in southern Switzerland, rents for older apartments fell in all the country's regions, while rents for new-build apartments climbed higher. Taking all types of apartment together, rents have recently gone up most sharply in the Basel (3%) and southern Switzerland (2.1%) regions. Rents have gone down only in the Jura region (-1.4%) [26]. Despite higher rents in the second quarter, compared with the prior-year quarter rents have dropped 3.5% (existing properties: -5.6%, new-build: -1.4%).<sup>16</sup>

### Sharp regional differences in office rent trends

As in the rental apartment and owner-occupied property markets, the number of building permits in the office segment has likewise contracted recently and is below the long-term annual average. In view of the high level of uncertainty of the exact office space needs for businesses

and corporations in the aftermath of the pandemic and the continued recommendation to work from home, in the medium term an increase in vacancies is to be expected despite the slowing expansion in supply.<sup>12</sup> However, too bleak a picture should not be painted of the current situation. Even if some of the work is done at home in the future, the space needed by firms will not necessarily contract to the same extent. For example, more meeting areas and a workspace buffer will be needed for when the staff are on site at the same time. In addition, the market for office space can build on ongoing growth in office work.<sup>17</sup>

**Values for office premises in Zug rise by 7% in the second quarter of 2021**



<sup>13</sup> Zürcher Kantonalbank (ZKB), Immobilienbarometer / 2. Quartal 2021

<sup>14</sup> FPPE, Transaktionspreis- und Baulandindizes für Wohneigentum, Datenstand 30. Juni 2021

<sup>15</sup> FPPE, Marktindizes für Renditeimmobilien, Datenstand 30. Juni 2021

<sup>16</sup> FPPE, Transaktionspreis- und Baulandindizes für Renditeliegenschaften, Datenstand 30. Juni 2021

<sup>17</sup> Neue Zürcher Zeitung (NZZ), Medienmitteilung vom 24. Juni 2021: Corona bedeutet nicht das Ende des Büros



With regards to office rents (transaction rents), the situation in the market for office space remains stable for the time being. Rents rose by a slight 0.2% in the second quarter of 2021, the fourth quarterly increase in succession [2, 36]. This means that rents are above both the prior-year level (0.5%) and their level in the second quarter of 2019 (0.4%). In regional terms, however, significant differences can be seen [37, 38]. While rents rose in the second quarter of 2021 in cantons Freiburg (+4.1%), Schaffhausen and Zug (each +4.9%) and in each case are well above their prior-year levels (FR: 12.2%, SH: 9.9%, ZG: 21.5%), rents dropped in cantons Geneva (-1.8%), Lucerne (-2.1%) and Berne (-2.4%) and were also down year on year (GE: -8.9%, LU: -5.4%, BE: -4.4%).<sup>16</sup> Changes in rents in the second quarter of 2021 led at times to increases in market value in the regions referred to, with rises of up to +7% in canton Zug (SH: +6.5%, FR: +6.3%). In the cantons that experienced declining rents, such as Lucerne (-3.5%) and Geneva (-0.5%), as well as in Basel-Stadt (-2.2%) and Berne

(-0.6%), property owners have faced a loss in value recently [40].<sup>15</sup>

### Retail sales benefiting from catch-up effects

In the second quarter retailers benefited once again from further steps to open up and from positive prospects for the economy. Seasonally adjusted real sales (excluding filling stations) rose by 3.3% in the first quarter and then by 5.6% in the second quarter. The increase in sales this time was attributable to different sectors compared with the first quarter, though. For instance, recently sales have gone up by 21% and 22% respectively in the publishing products, sports equipment and toys and other goods categories (first quarter of 2021: -1.8% and -5.7%).<sup>18</sup> However, rising sales are likely to be on the agenda only temporarily and they will then probably return to their pre-crisis level once the situation normalises, and so follow a stable to falling trend.<sup>19</sup> As a result of the pandemic and the longer-term shift to online distribution for an

increasing share of sales, the sales pressure in bricks-and-mortar retail is likely to have increased further.<sup>12</sup> As value added declines, tenants' ability to pay is diminished, forcing landlords to reduce rents in order to avoid having vacant lots.<sup>11</sup>

## Rents for retail premises are likely to fall further

In the restaurants sector the market for premises has so far proved comparatively robust in view of the pandemic, which is attributable to state support measures. This is reflected, despite businesses being shut down, in falling bankruptcies in the sector and declining vacancies for restaurant premises during the crisis. This harbours risks for real estate owners, who will have to expect missed rent payments and vacancies once the financial support stops.<sup>9</sup>

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<sup>18</sup> Bundesamt für Statistik (BFS), Detailhandelsumsatzstatistik – vierteljährliche Zeitreihen: Datenstand 30.06.2021

<sup>19</sup> Credit Suisse, Schweizer Immobilienmarkt 2021 / März 2021