CBRE

New prime yield confirmed, as occupier market records sluggish first quarter

▼ 24,900 m^2
Take-up

▲ 3.3%
Vacancy rate

▶ 54€/m^2
Prime rent

▼ 4.60%
Prime yield

Note: Arrows indicate change from previous quarter

HIGHLIGHTS

- New office lettings and sales were slow in the first quarter, as take-up totalled 24,900 m^2.
- Vacancy remains very limited to a tight 3.3%, which is hindering further movement in the office market.
- New completions totalled 27,100 m^2 in the first quarter, with just 17% of space still available.
- Prime office rent in Cloche d'Or increased to 38 €/m^2/mo (excl VAT), after a letting deal in a new office.
- The acquisition of Royal Park sets the new prime yield in an otherwise quiet quarter for investments.

ECONOMY

The Luxembourgish economy was flat in the fourth quarter, resulting in a yearly change of -1.1%. The Grand Duchy thus joined a handful of other eurozone countries in experiencing a recession in 2023, including Germany, Ireland and Austria. The financial sector was a drag on growth, but early 2024 economic metrics are slightly more favorable. Overall, STATEC continues with its 2024 forecast of 2.0% GDP growth.

Inflation continued to fall through the year in Luxembourg to 3.7% for 2023 (NCPI). In this respect, the Grand Duchy seemed rather resilient to global supply chain pressures. STATEC foresees further moderation of NCPI to 2.2% in 2024, following a downward revision.

2.0%

Forecast for 2024 Luxembourg GDP growth by STATEC (as of March 29)

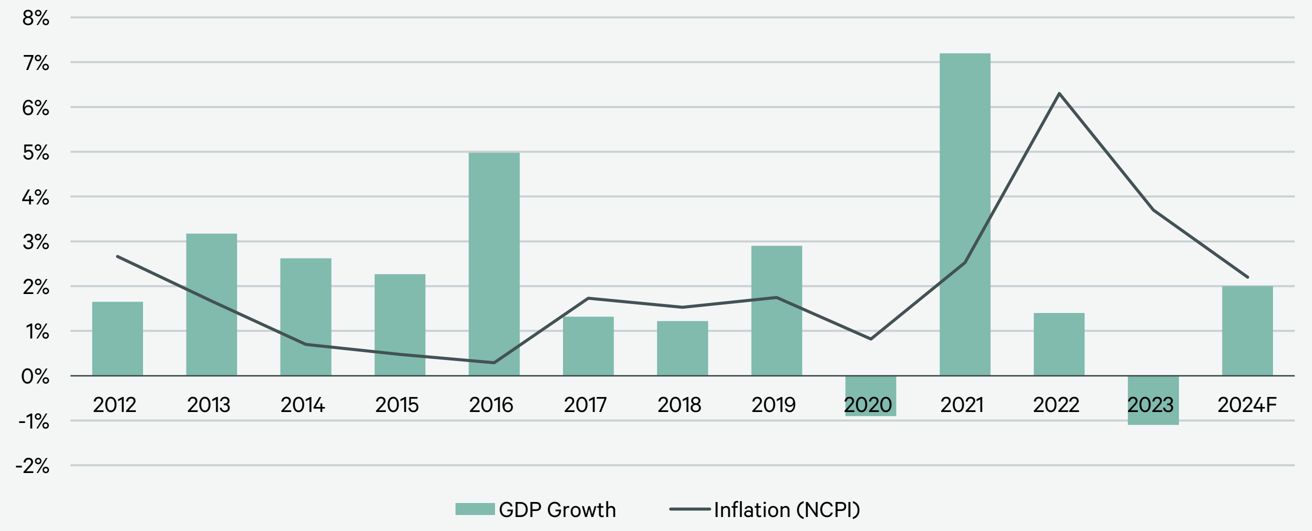
The labour market slowed notably in 2023, year-over-year, but still remained ahead of the eurozone. Construction, real estate and business services contributed the most to the decline. On the other hand, public administration, health, education and defence saw employment expansion. A relatively weak employment dynamic is expected in 2024. The unemployment rate has followed suit, rising to 5.2% from 4.8% in 2023. STATEC forecasts the unemployment rate to increase further to 5.9% in 2024.

Following a relative low in 10-year bond yields (monthly average) in December 2023 of 2.60%, Luxembourg has experienced three successive months of rising yields in Q1 2024, the only country in western Europe to do so. 10-year bond yields are now 2.95% in Luxembourg, higher than its neighbors Germany (2.36%), France (2.82%) and Belgium (2.91%).

Luxembourg is tipped to return to growth in 2024 of 2% after dipping into a recession in 2023

Luxembourg economic growth and inflation as of Q1 2024 (March 29 update)

Source: STATEC



DEMAND

After a rampant final quarter last year, the Luxembourg office market took a breather in Q1 2024, with just 24,900 m² of take-up activity. At 35 transactions, it is the slowest for some time. However, the low take-up volume is not unprecedented for first quarters.

The Luxembourgish State returned to the market to close the biggest deal of the quarter - the pre-letting of the Red Sky F office in Esch-Belval (9,910 m²). In Cloche d'Or, PwC continues to expand, securing two floors in the newly-completed Emerald building (2,054 m²). The third largest deal goes to flex office space operator IWG securing three floors in the Moonar D office building by the airport.

24,900 m²

Q1 office take-up in Luxembourg

The BFI sector was relatively active, accounting for 27% of total take-up volume this quarter, or 6,766 m². The three largest of these deals were all closed in the Kirchberg market, including Fisher Investments (1,364 m², Commerzbank Finance (997 m²) and Scottish Widows Europe (851 m²).

Also this quarter, a flurry of activity saw the new The Arc renovation along Avenue de la Liberté in the Station market close 81% of its available space over five deals. The building will house Sfeir Benelux, Zimmer Partners, BCD Travel, Raiffeisen and Janus Henderson Investors.

VACANCY

Approximately 159,600 m² of office space is considered vacant out of a total stock of 4.885 million m², resulting in a very tight market of just 3.3%. This is a slight increase over the previous quarter but still does not leave occupants much space for maneuvering. One newly completed building added 3,000 m² to the market, and part of a building in Munsbach was vacated, adding to the uptick in availability.

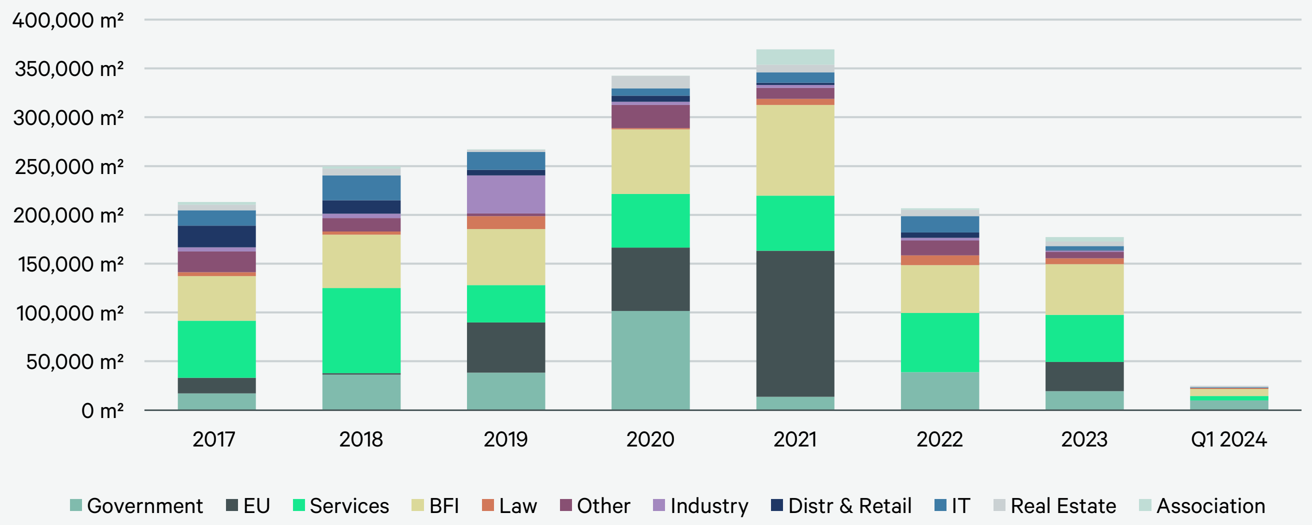
As a result, the CBD (2.5%) and Munsbach (17.2%) saw upticks in the vacancy rate as did Strassen (4.8%). Changes in all other markets were marginal. Station and Kirchberg remain well below 2% of availabilities, while Cloche d'Or is under 3%.

159,600 m²

A slight increase to 3.3% office vacancy in Q1 2024

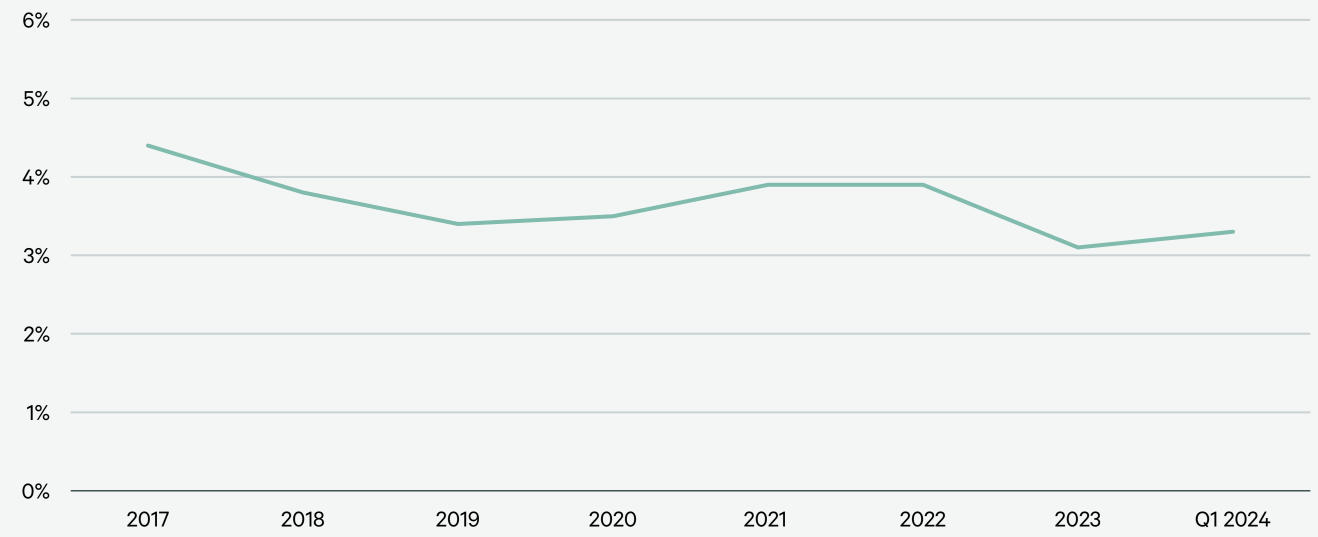
Luxembourg office take-up (Q1 2024)

Source: CBRE Research



Luxembourg office vacancy (Q1 2024)

Source: CBRE Research



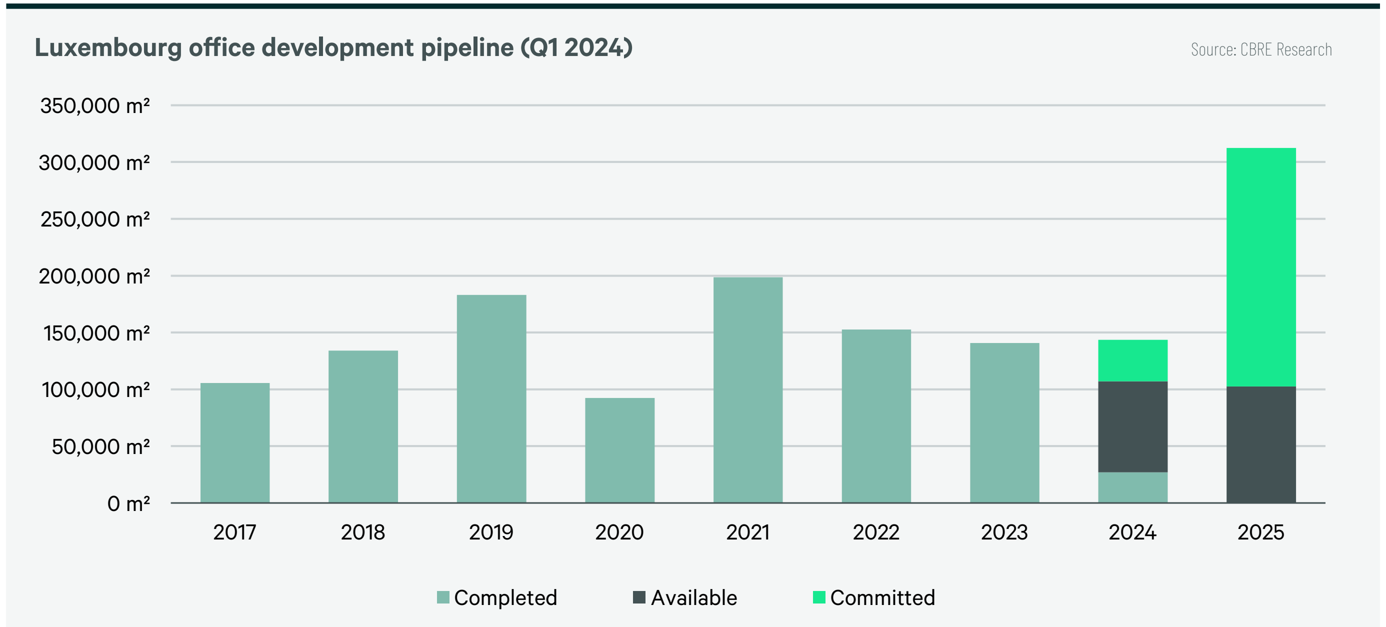
DEVELOPMENT

Five projects totalling 27,100 m² were completed in the first quarter. Of this amount, three projects had availabilities of 4,680 m² (17%) upon completion. All completed projects were of modest size, with the largest being the 10,500 m² Royal Park in the CBD developed by Baltisse that was delivered 95% pre-let. Also in the CBD, Monterey 31-33 was completed with 81% available (3,700 m²). Elsewhere, White House was delivered in Cloche d'Or (6,993 m²), the mixed-use Manhattan was delivered in Esch-Belval (1,600 m² offices), and Emerald was delivered in Munsbach (4,300 m²).

27,100 m²

Office projects delivered in Luxembourg in Q1 2024

For the remainder of 2024, the pipeline totals 116,560 m², of which 80,000 m² (69%) is available. Looking even further ahead, the 2025 pipeline has grown to 312,000 m², of which about one-third is currently available for lease. The Jean Monnet 2 is a significant portion of this overall pipeline at 180,000 m² (phase I and II).



RENTS

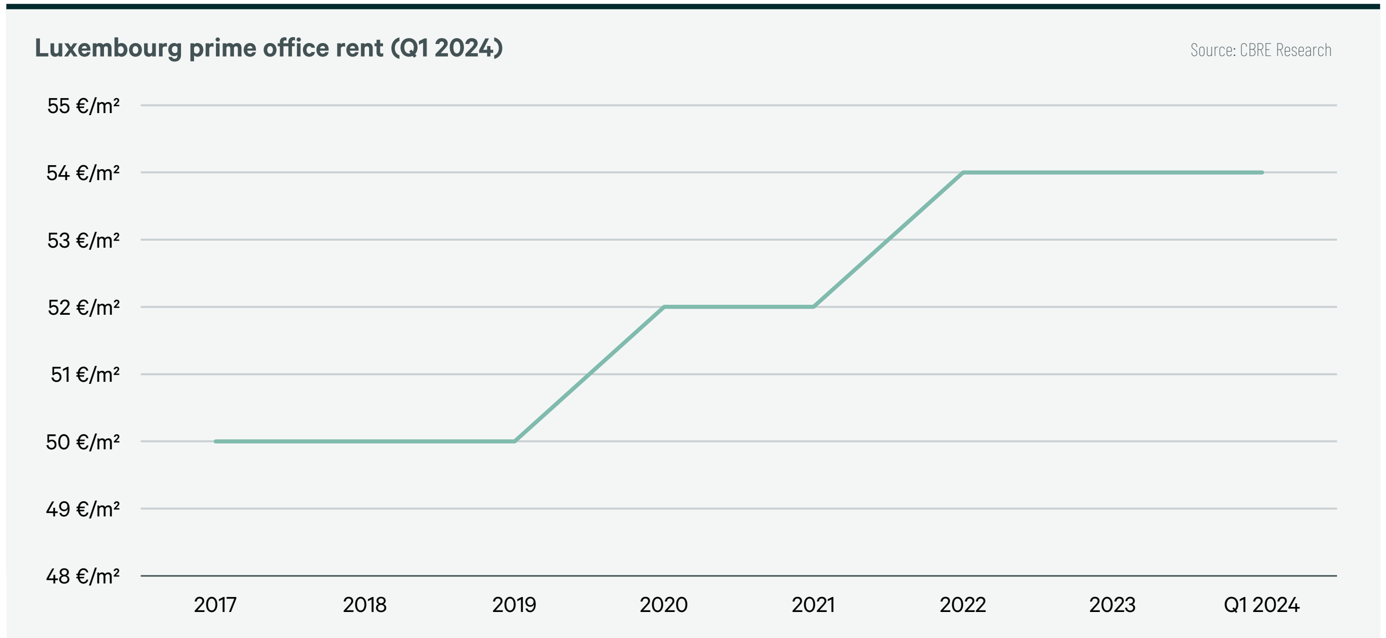
Overall, modern demands for ESG-compliant spaces and recent inflation in construction prices in the face of very little available space will keep upward pressure on rents. That is why - despite the low office take-up - Cloche d'Or saw a prime rent increase of 2.7% to 38 €/m²/mo (excl VAT) in the first quarter.

The overall prime rent for Luxembourg holds in Q1 at 54 €/m²/mo (excl VAT) in the CBD. This market commands a premium over the next highest Kirchberg at 42 €/m²/mo (excl VAT) and Limpertsberg and Station at 40 €/m²/mo (excl VAT).

54 €/m²

Prime office rent recorded in Luxembourg

Average achieved rents from the last 12 months were 32.9 €/m²/mo (excl VAT). This is the third consecutive quarter experiencing declining average rents (rolling four quarters). Though, rents have been increasing over the medium and long term.



INVESTMENT

The hangover in the investment market from the year before continues in the first quarter of the year, with just two major deals recorded for a total of €179 million. One deal was the private acquisition of a 4,200 m^2 out-of-town retail development from Nextensa. The other was a landmark office deal. That is, the newly-completed Royal Park office in the CBD was acquired by Pontegadea - a Spanish family office - from developer Baltisse.

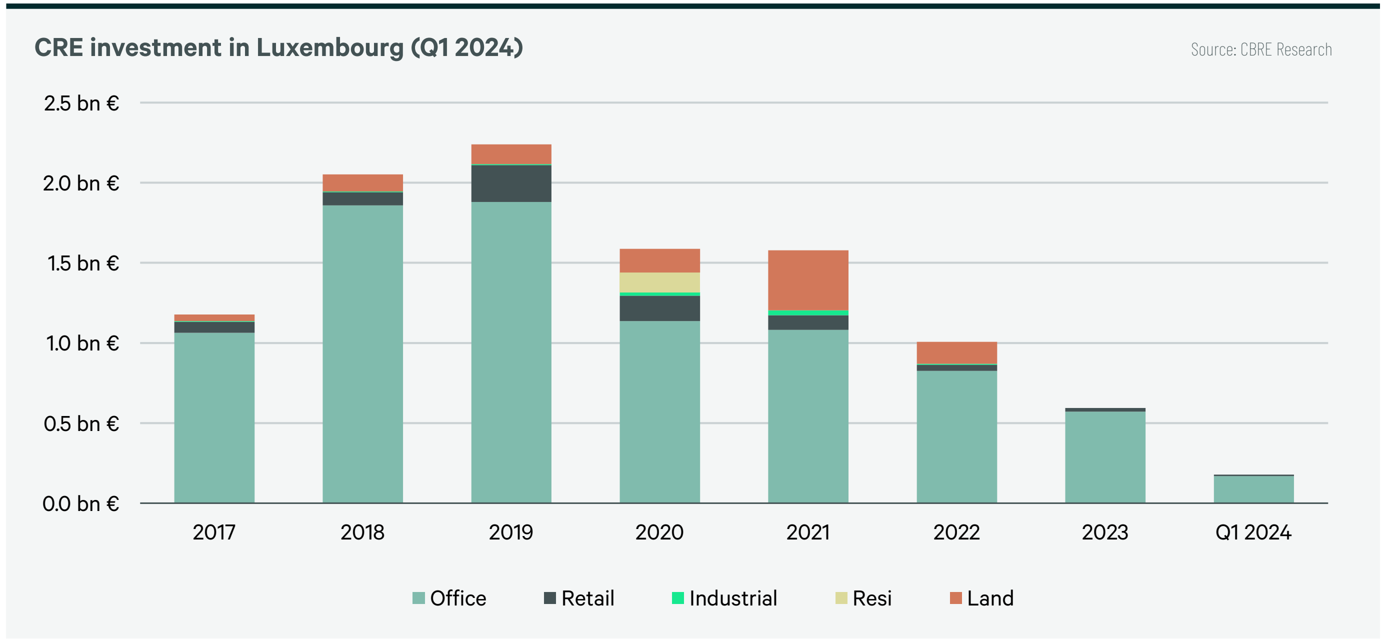
€179 mn

CRE deals closed in Luxembourg in Q1 2024

Both acquisitions in Q1 were completed by private funds. This is particularly unusual for a high-value prime asset like Royal Park that would normally be the target of institutional capital. This underscores the current environment where cash-rich private investors are leading the market, while institutional buyers wait for a more certain interest rate and market outlook and more normal bid-ask spreads.

With the conclusion of the Royal Park transaction, market evidence now supports a prime office yield of 4.60%. This represents a 130 bps change since the beginning of the interest rate hike cycle in 2022. Overall, the solid fundamentals and positive outlook for Luxembourg as an economy and office market still hold over the longer term.

Note: Total investment figures include all property types inclusive of commercial land, projects and purchases for own occupation.



Market evidence now supports a prime office yield of 4.60% in the first quarter

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