Institutional Real Estate
Europe

The investor-focused global real estate publication

The case for real estate 18
Championing allocations to property in 2025
by Marek Handzel

Returning home 24
Nearshoring's transformative powers
by Chris Anderson

Looking ahead with confidence 28
Key office and logistics predictions
by Iain Finnegan

Pinning down tomorrow's winners 32
Identifying up-and-coming inner city districts
by Luca Gudewill

A meeting of minds 34
Aligning interests in stranded offices
by Luke Duckworth

COMMENTARY

1 › Editorial
Constipation
by Geoffrey Dohrmann

5 › Market Perspective
Is it time to call the market?
by Keith Breslauer

DEPARTMENTS

8 › Market Pulse

10 › News & Views

17 › Acquisition Watch

38 › Last Word

40 › People

Is it time to call the market?

A bottom-up approach will be needed to unearth the best real estate investment opportunities in 2025

by Keith Breslauer

We are about to discover if there is any substance to the phrases "survive until '25" or "don't deep six until '26".

These phrases have been doing the rounds in property investment circles in 2024, in reference to a time in 2025 when expectations of falling interest rates would spark a bounce-back in real estate markets, lowering refinancing risks and driving a recovery in valuations. As we approach the New Year, then, can European real estate investors look ahead with confidence?

Let's start with where we are now. Arguably, the most important driver of the macroeconomic backdrop over the past six to 12 months has been confirmation that inflation is falling, largely thanks to the weakening of the Chinese economy reducing inflation across western nations. Euro zone inflation recently fell to 1.7 percent, sinking below 2 percent for the first time in three years. This has given the ECB and other major central banks the confidence to start cutting interest rates. But "start" is the operative word, and the magical question for real estate investors going into 2025 is where central banks go next. Or in other words, how much they ultimately cut rates by.

On the basis that inflation is falling and keeps falling steadily in 2025, European policy rates dropping by 100 to 200 basis points is rational. The expectation now is the short end of the yield curve will drop, meaning we would expect the curve to get steeper as Europe's economies soften, which tariffs introduced by a Donald Trump presidency could make more likely. The inversion of the curve or the parallel of the curve leads to recession, whereas the normalisation of the curve ultimately leads to a growing economy. However, the assumption that inflation will keep falling steadily is far from certain.

The return of inflation

In the United Kingdom, the Bank of England has forecast chancellor Rachel Reeves's first budget will increase inflation by up to half a percentage point over the next two years, driven by big rises in public spending, contributing to a slower decline in interest rates than previously thought.

Trump tariffs are also expected to be inflationary in the United States because they will likely drive up prices — however, the level of impact tariffs have on inflation will ultimately depend on how far they go and how aggressive they are. Other tax cuts and policies designed to drive growth mentioned by Trump in his election campaign could also increase the chances of the US economy overheating.

All this has seen investors scaling back how quickly they expect the Federal Reserve to cut rates in the United States, with yields on 10-year US Treasuries rising. If we see delays to rate cuts in the United States, we may see the same in Europe, given the potential knock-on impact and the tendency of other major central banks to move in sync with the Fed.

> **Can we assume 2025 will be a vintage year for allocating capital? The short answer is that positive opportunities are out there, but mainly on an individual case-by-case, asset-by-asset basis**

Keith Breslauer
Patron Capital

Real estate's attractiveness as an investment also rests on the level of finance available to support asset purchases and the level of liquidity in the marketplace. The good news is that although access to finance is not quite at the level most European real estate investors would like it to be, it is available.

A vintage year ahead?

Banks are much healthier and have higher capital ratios than when coming out of previous downturns, so it's not like 2008. Finance is also available at a time when land and asset valuations, especially in the logistics and residential sectors, may be near the bottom.

Logistics land values have fallen by up to 20 percent in some key regional markets in Germany,

yet occupier demand and rental growth for grade A space is strong. Can we therefore assume 2025 will be a vintage year for allocating capital? The short answer is that positive opportunities are out there, but mainly on an individual case-by-case, asset-by-asset basis, as opposed to broad-brush portfolio acquisitions.

Institutional investors with capital to deploy are also increasingly looking to dip their toes back into real estate markets, driving more competition for the best assets in 2025.

The rub for investors, however, is that even many potentially attractive asset-specific opportunities are not necessarily cheap, because the market has not reached a scenario where higher leverage and rates mean owners are in severe distress. Instead, we have a situation where there is reasonably high leverage, relative to valuations, which have fallen in recent years, but because rates are now coming down, more investors are reassessing their financing arrangements and aiming to keep their business plans on track with recapitalisations.

New energy-efficiency regulations for buildings — although still coming down the track — are being rolled back by governments nervous of placing too much pressure on industry, which will also alleviate the pain that building owners may have otherwise felt by giving them more time. In other words, they've survived until '25 and are not under as much pressure as they might have been. Institutional investors with capital to deploy are also increasingly looking to dip their toes back into real estate markets, driving more competition for the best assets.

Getting superior returns

Achieving outperformance on core buy-and-hold income-focused strategies will, therefore, be tricky.

Against the current backdrop, agile, value-added investors with the expertise to identify not just property-specific opportunities, but also the construction management skills to deliver complex refurbishment programmes, are best placed to achieve superior returns.

But it is not straightforward. Unearthing the best opportunities will likely mean having local, on-the-ground teams with the knowledge to identify individual projects with the best potential, and then deep relationships with local construction supply chains to transform them.

From a value-added perspective, the German market is particularly exciting. Parts of the logistics and residential sectors in Europe's largest economy now look especially ripe for development. Despite the improving macroeconomic backdrop, there is still a level of dislocation in the market, providing an attractive entry point for investors.

Capex-constrained landlords unable to bring their properties up to scratch to meet modern occupier demands, and in the face of changing energy-efficiency regulations, are choosing to bring them to market at a discount today, rather than risk them becoming obsolete in the future. There are also developers continuing to face significant debt issues on land purchased when interest rates were far lower, and their problems will only be exacerbated if rates take longer to fall from here. Investors with the ability to connect with these landlords, and with the capital and skill set to develop or transform properties to meet modern ESG standards, are set to be rewarded in a market where vacancy rates for grade A logistics space in Germany's main regions, for example, are close to zero.

Pockets of value

Going into 2025, pockets of value are also emerging tied to residential, both in Germany and other European markets including the United Kingdom. BTR is one example, where in recent years investors bought land with leverage at much lower interest rates. Although rates are falling, they will likely prevail at a higher level, meaning there are situations where land has become cheaper and some higher-leveraged owners are ready to sell.

With base and mortgage rates on the way down, buyers and investors are returning to the residential sales markets again too. This, combined with acute supply/demand imbalances, has put build-to-sell back on the agenda, shifting from the environment seen in recent years where soaring interest rates made purchasing homes using mortgage finance even more unaffordable for most people. This is one of many reasons, for example, that Patron invested in Cala Homes in the United Kingdom, which operates in the mid-market where short supply is especially acute.

For real estate investors who have "survived until '25", there are ample opportunities out there, but only those with the right bottom-up skill sets look set to thrive. ❖

Keith Breslauer is managing director and senior partner at **Patron Capital.**