**At a glance**

**INVESTMENT SPAIN Q1 2017**

HIGH INVESTMENT VOLUME IN THE FIRST QUARTER

**ECONOMIC CLIMATE**

Headline inflation in the Eurozone is rising although core inflation remains subdued. Core inflation is less volatile way of measuring consumer prices because it does not include components such as energy products (petrol, electricity) and unprocessed foods (fruit and vegetables). Unlike headline inflation that is subject to commodity price swings created in the financial markets, underlying inflation is more closely aligned to supply and demand in the economy itself. Little evidence of sustained recovery in underlying inflation led the Governing Council of the ECB in March to maintain monetary stimulus, meaning that capital markets remain awash with liquidity. The Spanish economy continues to grow and GDP increased 0.8% between Q1 2017 and Q4 2016.

**FOREIGN CAPITAL IS THE SOURCE OF INVESTMENT**

The momentum gained over the last two years continued during the first quarter of 2017 with the amounts invested directly in real estate in Spain reaching 3.38 billion Euros, a figure above the annual average for 2009-2013. It represents an increase of 27.5% in comparison with Q1 2016 (€2.65bn) and 16% in comparison with Q1 2015 (€2.915bn). Just five deals made up 41% of the 3.38 billion: Intu acquired Xanadú from Ivanhoe (€560m); Blackstone acquired a residential portfolio from BBVA (€324m); TH Real Estate bought three shopping centres from Neinver (€187m); Freo acquired an office portfolio from BBVA (€160m) and Merlin purchased the Agbar office tower from the company of the same name (€150m). Property yields continue to fall. The prime yield on offices has fallen by 0.25 percentage points to 3.85%. High-street retail is showing a prime yield of 3.15% and the prime yield on logistics units has fallen to 5.9% from the 8% seen at the close of 2013. Other notable deals in the Spanish real estate market excluded from the investment volume (due to the type of transaction) were the sale of 49% of the Quinta Torre for 323 million Euros and the sale of 50% of the Canalejas Centre for 225 million Euros. In addition, Värde acquired Via Céleres for 90 million Euro.

Capital continues to flow into the Spanish property market through US vehicles, representing 36% of the total in the first quarter. Spanish vehicles invested practically same percentage as the British ones, namely around 24%. These are the main channels through which money is reaching Spain. At BNPPRE we estimate that foreign capital invested in the Spanish real estate sector amounts to around 75%.
**Funds and Socimis - The Leading Investors**

The pace of activity on the part of investment funds remains comparable to 2016, being responsible for 50% (1.7 billion Euro) of investment in the year to date. The Socimis have become the main seekers of offices and continue to specialise. Of the total €667 million Euros invested by these vehicles, 313 million were assigned to offices and the remainder to retail and hotels.

**Retail Is a Clear Winner**

Offices. By asset type, shopping centres were the clear winners during the quarter with investment of €1.04bn, of which €747m was swallowed up by just two deals. Adding together the remaining retail segments (supermarkets, retail premises, etc.) the volume reaches €1.7bn. The solidity of consumer spending is leading investors to focus their attention on this sector. Retail sales have now seen 29 consecutive months of positive year-on-year growth.

Investment in offices reached 600 million Euros; half of that taken up by the Freo and Merlin deals. Growth expectation for rents, together with a trend of net positive take-up over recent quarters, is leading to continued appetite for these buildings. 2016 closed with a new record in overseas tourists: 75.6 million visitors, some 10.3% more than during 2015. The main provider of foreign tourists to the Spanish market continues to be the UK. Hotel assets amounting to 514 million Euros have been transacted in the year to date.

In the logistics market, 2016 closed with a record investment volume of 1.05 billion Euros. Following on from this figure, 2017 started more gently with 141 million Euros. E-commerce continues to grow and will remain a driver for this sector.

**Outlook**

Downward pressures on the yields of real estate assets will continue throughout this year and somewhat more softly in 2018. It is anticipated that the Spanish economy will continue to expand along with job creation. In addition, the abundant liquidity in the financial markets plus low interest rates will continue to help with credit easing.

**Initial Yields vs. Sovereign Bonds vs. Euribor**

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Further information: BNP Paribas Real Estate | Telephone: +34 914 549 600 | www.realestate.bnpparibas.es
Investment: Thierry Bougeard — Managing Director - Transactions — Spain. Email: thierry.bougeard@bnpparibas.com
Research: Daniel Capanin — Senior Analyst, Spain. Email: daniel.capanin@bnpparibas.com