Austria’s real estate market

Extremely low interest rates + Economic recovery = Supercycle?

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The European Central Bank’s highly expansive monetary policy is boosting demand for real estate. With interest rates extremely low or negative, real estate assets are appealing since they offer significantly higher returns than alternatives such as government bonds. Direct investments in real estate also compare favorably with stocks and shares, as property prices are considerably less volatile. As a result, real estate has become an increasingly attractive asset class in recent years. Large institutional investors, and sovereign wealth and other funds which need to invest significant amounts of money have markedly increased the proportion of real estate in their portfolios.

This development is also plain to see in Austria. Foreign investors, increasingly those from overseas, are also putting money into the Austrian market, with a particular focus on large transactions up to hundreds of millions of euros. According to CBRE, the total value of commercial real estate transactions reached a record EUR 3.9bn in 2015. Transactions worth about EUR 1.3bn were concluded in the first six months of 2016, which was close to the level in the comparative period last year. Since the second half of the year is usually better than the first, and with a number of large deals in the pipeline, investment in 2016 looks set to at least match last year’s record level.

The UK’s decision to leave the EU has somewhat clouded the economic outlook for Austria. Nevertheless, our economists are still forecasting real GDP growth of 1.5% for 2016 – significantly above the 1.0% growth achieved in 2015. Although the effects of Brexit may put the brakes on growth more strongly in 2017, real GDP growth next year is still expected to be above 1%.

Due to strong demand, real estate prices have already risen sharply, and with rents broadly unchanged, yields are correspondingly low. Prime yields on core real estate have reached all-time lows in Austria – those on office properties stood at around 4% in mid-2016. This limits the scope for a further decrease, so investors and developers must bear in mind that although there are still many good reasons for investing in real estate, one key argument – the real estate cycle – has sounded a note of caution. The longer strong demand persists on account of the lack of suitable alternatives, the higher the risk of a price correction.

Over the years, Austria’s real estate market has earned a reputation for relative stability, and we assume that it will continue to live up to this reputation in the coming years. We are pleased to offer financing for promising projects, but a balanced risk/return ratio is essential.

Sincerely,

Karla Schestauber
Economic environment in Austria: recovery despite stumbling blocks

Austria’s economy picking up speed...
Against the backdrop of favorable conditions in the rest of Europe, the Austrian economy grew in 2015. However, following a strong start, growth slowed sharply as the year went on. While the European economy absorbed additional pressures – the result of concerns about growth in emerging markets, particularly China, as well as geopolitical problems including the ongoing crisis between Russia and Ukraine and the situation in the Middle East – this increasing uncertainty weighed stronger on growth in Austria.

With full-year GDP up by 1.0%, the country enjoyed stronger growth in 2015 than in the previous year, but underperformed the eurozone as a whole for the second year running.

The Austrian economy made a solid start to 2016, and growth in the first six months was higher than a year earlier, at 1.4%. Buoyant domestic demand – the key factor behind the recovery in most European countries – continued to drive growth, while net exports made no contribution to growth in the face of a challenging global environment. Although consumer confidence failed to pick up at the beginning of the year, consumer demand helped to revive the economy in the first half of 2016, thanks to the income tax reform which boosted disposable incomes at the start of the year. Initial public skepticism about the favorable effects of the tax reform gradually began to give way, and consumer confidence improved in summer to reach its highest level in two years. Greater stability in the labor market also helped in this regard. In mid-2016, seasonally adjusted unemployment was unchanged year-on-year, with the unemployment rate (EU-method) standing at 6%. This was due to a significant rise in employment thanks to the economic recovery and slower growth in the workforce. The advance in private consumption was also supported by low inflation – the rate averaged just 0.8% in the first half of the year. Declining oil prices played a significant role, as they were 30% down on average year-on-year. However, the positive effect of low inflation on domestic consumption was weaker in Austria than in other European countries where inflation was even lower. Rising hotel and restaurant prices as well as rents served to push up prices more strongly.

Domestic demand grew also as a result of spending for asylum seekers, which was funded by government borrowing, leading to an increased government deficit. Improved sentiment also led to an upturn in investment, which gradually gathered pace during the first half of the year. This was particularly true of spending on machinery and vehicles. Construction growth continued to lag behind, but did begin to rise at the beginning of 2016 after almost two years in decline.

After a modest start to the year, export growth improved somewhat. Export-driven sectors of the economy were able to maintain moderate growth on the basis of domestic orders, and production

Overview of Austria’s economic data

<table>
<thead>
<tr>
<th>Economic growth (real. year on year)</th>
<th>2010</th>
<th>2011</th>
<th>2012</th>
<th>2013</th>
<th>2014</th>
<th>2015</th>
<th>2016</th>
<th>Forecast</th>
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</thead>
<tbody>
<tr>
<td>Economic growth (real. year on year)</td>
<td>1.9</td>
<td>2.8</td>
<td>0.7</td>
<td>0.1</td>
<td>0.6</td>
<td>1.0</td>
<td>1.5</td>
<td>1.1</td>
</tr>
<tr>
<td>Private consumption (real. year on year)</td>
<td>1.0</td>
<td>1.3</td>
<td>0.5</td>
<td>−0.1</td>
<td>−0.3</td>
<td>0.0</td>
<td>1.3</td>
<td>1.1</td>
</tr>
<tr>
<td>Investment (real. year on year)</td>
<td>−2.1</td>
<td>6.7</td>
<td>1.4</td>
<td>2.2</td>
<td>−0.9</td>
<td>0.7</td>
<td>3.3</td>
<td>2.6</td>
</tr>
<tr>
<td>Exports (visible and invisible)</td>
<td>13.8</td>
<td>6.0</td>
<td>1.7</td>
<td>0.5</td>
<td>2.1</td>
<td>3.6</td>
<td>2.1</td>
<td>2.9</td>
</tr>
<tr>
<td>Imports (visible and invisible)</td>
<td>12.0</td>
<td>6.2</td>
<td>1.1</td>
<td>0.7</td>
<td>1.3</td>
<td>3.4</td>
<td>2.8</td>
<td>3.5</td>
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<tr>
<td>Current account balance (in % of GDP)</td>
<td>3.3</td>
<td>1.6</td>
<td>1.5</td>
<td>2.0</td>
<td>1.9</td>
<td>2.5</td>
<td>2.3</td>
<td>2.1</td>
</tr>
<tr>
<td>Inflation rate (CPI) (real. year on year)</td>
<td>1.9</td>
<td>3.3</td>
<td>2.4</td>
<td>2.0</td>
<td>1.7</td>
<td>0.9</td>
<td>0.9</td>
<td>1.8</td>
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<tr>
<td>Unemployment rate (EU definition)</td>
<td>4.8</td>
<td>4.6</td>
<td>4.9</td>
<td>5.4</td>
<td>5.6</td>
<td>5.7</td>
<td>6.1</td>
<td>6.3</td>
</tr>
<tr>
<td>Unemployment rate (national criteria)</td>
<td>6.9</td>
<td>6.7</td>
<td>7.0</td>
<td>7.6</td>
<td>8.4</td>
<td>9.1</td>
<td>9.2</td>
<td>9.6</td>
</tr>
<tr>
<td>Employment (year on year, in %)</td>
<td>0.6</td>
<td>1.8</td>
<td>1.3</td>
<td>0.5</td>
<td>0.6</td>
<td>0.9</td>
<td>1.3</td>
<td>0.7</td>
</tr>
<tr>
<td>Public-sector balance (in % of GDP)</td>
<td>−4.4</td>
<td>−2.6</td>
<td>−2.2</td>
<td>−1.3</td>
<td>−2.7</td>
<td>−1.1</td>
<td>−1.7</td>
<td>−1.3</td>
</tr>
<tr>
<td>Public-sector debt (in % of GDP)</td>
<td>82.3</td>
<td>82.1</td>
<td>81.6</td>
<td>80.9</td>
<td>84.0</td>
<td>85.5</td>
<td>85.2</td>
<td>84.1</td>
</tr>
</tbody>
</table>

1) Gross fixed capital formation / 2) excluding maternity leave, military service and training programmes
Source: Bank Austria Economics & Market Analysis, Austria
climbed around the middle of the year thanks to higher foreign demand. Bank Austria’s purchasing managers’ index reflected this positive development, rising to 54.5 points in mid-2016 – its highest value in more than five years.

...but Brexit is casting a shadow on prospects

Both consumer and business sentiment were tangibly more optimistic in the middle of 2016. But sentiment indicators at that time did not reflect the impact of the UK’s decision at the end of June to leave the EU. Despite all the positive signals, uncertainty resulting from the result of the UK referendum means that Austrian economic growth is expected to start slowing. Weaker growth in the second half will be offset by the better-than-expected performance in the first six months, and forecast GDP growth for 2016 as a whole is still 1.5%.

However, the upturn in the economy will be too slow to prevent unemployment from increasing, although the low growth in the workforce in the first half means that unemployment should only increase slightly, to an average of 6.0% in 2016. Inflation will also begin to creep up again from mid-2016, climbing more steeply towards the end of the year due to the base effect resulting from the dramatic fall in oil prices last autumn. The average rate of inflation in 2016 as a whole is expected to be 1.1%.

Uncertainty to result in lower growth in 2017

In 2017 the negative impact of the Brexit decision on investment and export demand will become more keenly felt. The UK is Austria’s eighth most important export partner by value and the country’s sixth most important export market after Germany, the USA, Italy, France and China. Exports to the UK account for about 1.5% of Austrian GDP. But indirect negative effects due to the impact on some of Austria’s other important export partners, such as Germany, France and CEE countries, will be at least as significant for the economy as the direct effects. GDP growth is therefore seen as being somewhat weaker in 2017, at 1.1%, although this is still slightly above the 2015 level. According to our calculations, the UK’s decision to leave the EU will cost the Austrian economy about half a percentage point of growth in gross terms over 2016 and 2017. Consequently, the effect on Austria will likely be below the European average. The medium-term consequences of Brexit on the Austrian economy should therefore be limited, but of course they depend on the political fallout from the decision.

In view of the slower GDP growth forecast for 2017, unemployment is expected to increase again, to 6.3%. Conversely, the expected rise in inflation will be more moderate. Inflation of 1.8% is anticipated for 2017, reflecting weaker global demand as a result of the Brexit decision and reduced upward pressure from commodity prices.

Extension of ECB’s quantitative easing program on the cards

The ECB may have its hand forced in the coming months as a result of the UK’s decision to leave the EU. Nevertheless, despite the downside risks to growth and inflation in the eurozone as a consequence of the Brexit decision, the ECB is not expected to cut rates further, since the negative side effects of such a move would outweigh any positive impact. Nevertheless, the combination of weak growth, somewhat lower inflation and increased threats to financial stability is likely to mean that the ECB extends its asset purchase program by at least six months, to September 2017.

Vienna’s economy continues to grow moderately

After sluggish growth in 2014, improved demand led to a modest recovery in the Viennese economy in 2015. Growth of just under 1% was driven primarily by the service sector, which picked up steam across the board. The uptick in global demand only provided a minor stimulus to Vienna’s industrial sector, which is less export-driven than the national average. However, manufacturing made a positive contribution to growth in 2015 for the first time since 2009, thanks mainly to the energy sector. In contrast, construction fell, impacted by the completion of a number of large infrastructure projects in the previous year.
The unemployment situation in Vienna worsened significantly despite the slight improvement in the economy – the unemployment rate for 2015 climbed to 13.5% according to Austrian methods. This was the highest level in Austria by some distance, and the result of the large increase in the labor supply, even though employment grew strongly. A third of the growth in the workforce is accounted for by the domestic working population and two-thirds by immigration from abroad.

**Moderate recovery to continue in 2016**

We expect Vienna’s modest economic recovery to continue in 2016. The service sector will be the key driver of this recovery, buoyed by the income tax reform. However, this stimulus will be partly offset by the further deterioration in the labor market – with the supply of labor set to continue rising, unemployment will increase to around 14%.

Meanwhile, the situation in the construction industry will improve thanks to a series of public construction projects. Residential construction in particular will provide a boost in 2016. Conditions remain largely unchanged for the industrial sector, with the gentle recovery set to continue. Overall Vienna’s economy will perform somewhat better year-on-year in 2016, growing by about 1.5% – roughly on a par with Austria as a whole.
Resilient demand for commercial real estate

ECB’s highly expansive monetary policy bolsters real estate demand
With interest rates extremely low or negative, real estate is becoming an ever more popular asset class. According to data published by CBRE, around EUR 3.9 bn was invested in commercial real estate in Austria in 2015 – a new annual record.

Investment totaled about EUR 1.3 bn in the first six months of 2016, which was close to the level in the comparative period last year. Since the second half of the year is usually better than the first, and with a number of large deals in the pipeline, there are strong prospects that investment over the year as a whole will at least reach the same level as in 2015.

Foreign investors, especially those from overseas, are showing strong interest in the Austrian market, in particular in large transactions valued in the hundreds of millions of euros.

Sharp rise in prices
Due to strong demand, core real estate prices are already very high and potential yields are correspondingly low. Prime yields for office properties stood at around 4% in mid-2016. Since returns on alternative investments such as government bonds have also fallen again – in some cases into negative territory – positive yield spreads are continuing to make real estate appealing. The proportion of real estate in the asset allocations of major institutional investors, as well as sovereign wealth and other funds, is therefore likely to remain relatively high or to increase.

Demand for office property in Austria was especially strong during the first half of 2016. A number of office towers changed hands during the period, including the Florido Tower, IZD Tower, and the Tech Gate Tower together with the whole Tech Gate complex. Large transactions were also seen on the hotel market as the Hotel Imperial, Hilton am Stadtpark and The Ring – all in Vienna – were sold to new owners.

Investment pipeline well stocked
The outlook for the second half of 2016 is good, with strong interest from investors. Properties for sale include DC Tower 1, the Marximum office campus, Millennium City and Millennium Tower, and the Design Tower (Sofitel hotel).
JLL ranks Austria among the transparent real estate markets

Investors like large, liquid markets, so Austria is not in the big leagues. But transparency is also becoming a more important factor. The Global Real Estate Transparency Index, published every two years by JLL, puts the Austrian real estate market at number 24th globally. Austria has been among the transparent markets for many years. The JLL ranking also confirms that Europe is the most transparent region worldwide.

The ECB has published a commercial real estate price index for the eurozone, which showed that prices reached an all-time high in the fourth quarter of 2015. As long as interest rates remain so low, this upward trend in prices will continue. However, the chart below shows that potential corrections could be strong.

MSCI/IPD confirms stable development of Austrian market

MSCI/IPD calculates the annual performance of an Austrian real estate portfolio covering the office, retail, logistics, residential and other segments. In 2015 the portfolio achieved a total return of 5.9% – an improvement on the 5.3% recorded in 2014. Approximately 4.7% came from income components and 1.1% was attributable to value components.

According to MSCI, Austria scores highly for its stable market development in comparison with other countries. The annual return since calculations began 12 years ago is 5.6%. Double-digit returns have not been achieved in any year since MSCI began tracking the portfolio, but even during the economic crisis in 2008 and 2009 the total return was quite impressive at 4.1% and 4.0% respectively.

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The need to effectively provide the population with housing is always influenced by the tug-of-war between free market forces and extensive regulations. That said, state intervention in the housing market is a necessity due to various sociopolitical and distribution-related factors. Shelter is not only a basic human need, it usually represents the single largest financial burden on private households. Around a fifth of income goes towards the acquisition of living space, its upkeep and housing-related energy costs. And although the limits of affordable housing can only be assessed on a case-by-case basis, calls for affordable living space mean that the residential market is balanced over the longer term, ensuring that significant excess demand does not occur.

**Imbalances returning on the residential housing market**

In a long-term comparison with other countries, the Austrian housing market has remained in balance for some time, despite strong shifts in individual segments of the market, particularly when it comes to more expensive, privately-financed properties. However, changes in the fundamental price indicator developed by Oesterreichische Nationalbank – Austria’s central bank – for residential property in Austria point towards the increased overvaluation of national average prices since mid-2015 (the indicator is a bundle of factors including population growth, development of prosperity, the housing subsidy and financing landscape, availability of land, the population's housing requirements and expected yields on the housing market).

According to the fundamental price indicator, privately owned apartments and homes in Austria were overvalued by 6.3%, and in Vienna by 23%. This trend was driven by an increase in the price of property which, having slowed somewhat in the second half of 2015, significantly picked up momentum once again and far outpaced the growth in household income, construction costs and consumer prices. In the fourth quarter of 2015 and the first quarter of 2016 the price of housing in Austria rose by an average of 9.3%, and by 5.2% in Vienna.

These substantial increases are a clear sign of growing undersupply on the market. Austria’s housing market has become increasingly off-kilter in recent years, particularly in major urban centers as a result of the sharp rise in the population. On a national level the “overcrowding” rate, as measured using the EU definition, increased from 12% in 2010 to 15% in 2015, reaching as much as 28% (up from 23%) in larger towns and cities.

**Growing population fueling demand for housing**

The Austrian population, which has grown by an average of 0.4% a year over the long-term, rose by almost 1% in both 2014 and 2015. In the first quarter of 2016 there was an increase of over 1% year-on-year, and of more than 2% in Vienna. In absolute terms, the Austrian population has risen by an average of around 70,000 a year. This sharp increase is largely due to immigration into Austria, which more than doubled in 2014 and 2015 compared with the ten previous years.
Strong demand on the housing market is expected to intensify over the next few years particularly since the number of 25- to 44-year-olds – the age range at which people typically set up homes – is growing, counter to the long-term trend. According to the latest forecasts, this particular demographic is set to expand by an average of 0.5% a year over the next ten years.

In the past decade an average of around 30,000 new households were established each year. In 2014 and 2015 this number exceeded 44,000. Around 37,000 new households are expected each year up until 2022, after which the increase is expected to plateau for the longer term. Forecasts show demand for apartments outstripping the number of new households established. This reflects the disproportionately high number of single-person households.

**Demand for 60,000 new apartments per year**

Increased demand for new apartments in Austria is primarily being driven by the above-average rise in immigration. Added to this comes pent-up demand that has built up during the course of recent years and which also has to be addressed. While demand for housing in Austria was largely covered by 45,000 to 50,000 units a year in the past, even construction of 51,500 new apartments a year over the past three years has proved insufficient. In addition to the rapidly increasing demand for new households, escalating demand for investment properties is compounding the situation (as also reflected in the evolution of prices on the real estate market).

Based on the latest forecast of more than 40,000 new households per year and the need to replace the estimated 0.4% of the total stock that has been demolished, combined or redesignated (around 18,000 units), the representative body for non-profit housing associations puts demand at around 60,000 apartments per year all the way through to 2020. After that, demand on the housing market is expected to relent, mainly due to a significant decline in the forecast number of new households. The number of apartments and buildings requiring refurbishment will drop owing to the higher overall quality of the building stock. Demand for second homes is also expected to fall.

**Sharp rise in number of construction permits**

In spite of rising real estate prices, the availability of cheaper financing, increased demand for living space and a record number of new building permits, building activity has remained weak in Austria for years. While an average of 64,000 apartment renovations or new builds have been approved each year over the past three years – more in total than during the housing boom of the mid-1990s – the number of completed projects has barely changed. The number of permits granted for new construction projects continued to rise sharply in the first quarter of 2016, with around 69,000 units predicted for the full year – the highest number ever recorded in Austria.
Even though only a part of the disproportionately high number of building permits granted actually result in construction projects, there are signs of continued growth in investment in housing construction. Conditions remain favorable thanks to cheap financing options and a distinct pick-up in household income growth for the first time in many years. Residential construction initiatives that will bring an additional 6,000 subsidised apartments and 2,000 privately financed rental and owner-occupier apartments will also help to stimulate construction. It remains to be seen whether this will be enough to redress the imbalances on the Austrian housing market.
Viennese office property market: New construction at an all-time low, but set to take off again in 2017

Vienna’s office property market is one of the most stable in Europe, and remains attractive for both domestic and foreign investors. In comparison with other European cities, office vacancy rates in the Austrian capital are still quite low, and those in the premium segment are very stable.

Old spaces being taken off the market
At present, construction of new office space is extremely low, although the various segments are benefiting in different ways. Older properties and outdated locations outside sought-after office axes are gradually disappearing from the market, as they can no longer compete with the ample supply of modern office space. However, older sites have received a boost from the strong demand for residential space. Where possible, and according to requirements, such sites are being converted into housing, hotels, student accommodation or serviced apartments. In some cases, completely new properties have been built at the old locations.

Including older space for which it is difficult to find tenants, the stock of office space in Vienna is currently just under 11 million m².

New-space production down slightly once again year-on-year
In 2015 construction of new office space in Vienna fell year-on-year, from 144,000 m² to around 115,000 m². In 2016, the amount of new space is predicted to be less than 60,000 m² – an all-time low. However, numerous projects are planned for the next few years, and some are already under construction, meaning that a significant jump in new construction is expected in 2017. Over the coming years the market will once again be dominated by large-scale developments. It is currently impossible to predict the impact of this massive increase in new space on the trend in vacancy rates.

The majority of the projects scheduled for completion this year are for own use, with a smaller proportion accounted for by the conversion, renovation or adaptation of existing space.

New rentals expected to top last year’s level by the end of 2016
The take-up of office space reached around 200,000 m² last year, a decline on 2014. However, over 120,000 m² was newly let in the first half of 2016. Last year’s level could be exceeded by the end of 2016, as new rentals were strong in the first six months and volumes in the second half are often higher than those in the first.

Consequently, compared with other West European cities, Vienna is only mid-table in terms of office space per capita, but the city still far outstrips the capitals of Eastern Europe. For example, Bratislava – the CEE leader when it comes to modern offices – has just slightly more than half as much space per capita as Vienna.

Office space in m² per capita 2016

New construction and take-up
Office space in Vienna 2001 – 2016

Source: Immobilien Rating, CBRE, EHL
Large-scale new rentals remain the exception, and relocations, consolidation of smaller units and/or upgrades still account for a substantial proportion of new lettings. Under current market conditions, this trend is unlikely to change significantly in future.

**Smart Campus: The largest office construction project of 2016, with 27,000 m²**

The biggest new development of 2016 is the Smart Campus close to the Gasometer site in Vienna’s 11th district. The property is home to the new headquarters of gas and electricity utility Wiener Netze.

Another own-use development is the Research Institute of Molecular Pathology (IMP) being built by Boehringer Ingelheim at the Vienna Biocenter, where around 15,000 m² of new space is scheduled for completion by the end of this year.

**New developments under construction at the Vienna Hauptbahnhof site**

New office space, as well as apartments, hotels and various educational facilities are currently taking shape on the site of the new main railway station (Hauptbahnhof). Many of these projects are mixed use, although René Benko’s SIGNA Holding is constructing an almost pure office development at the location. Known as THE ICON VIENNA, it comprises three buildings of different heights behind a curved facade, with a total of around 80,000 m² of modern office space.

Work is progressing on the new UniCredit Bank Austria headquarters on the site of the former Nordbahnhof station. Due for completion by 2018, the Austria Campus consists of state-of-the-art office space spread across several buildings, with a design that takes into account the latest work concepts and office structures (such as desk sharing). Retail space, a large canteen and a hotel are also planned.

Forecast new space, 2017ff (selected developments)

<table>
<thead>
<tr>
<th>Office project</th>
<th>Office space in m²</th>
<th>Status</th>
</tr>
</thead>
<tbody>
<tr>
<td>THE ICON VIENNA</td>
<td>74,000</td>
<td>under construction</td>
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<tr>
<td>Square Plus (components 1+2)</td>
<td>35,900</td>
<td>under construction</td>
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<tr>
<td>„Viertel Zwei Plus“, „Denk Drei“ project</td>
<td>22,500</td>
<td>under construction</td>
</tr>
<tr>
<td>„ORBI Tower“, Town Town (CB21)</td>
<td>21,600</td>
<td>under construction</td>
</tr>
<tr>
<td>Euro Plaza phase 6</td>
<td>12,500</td>
<td>under construction</td>
</tr>
<tr>
<td>Silo Plus/Silo Next</td>
<td>19,700</td>
<td>planned</td>
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<tr>
<td>HoHo Seestadt Aspern</td>
<td>19,500</td>
<td>planned</td>
</tr>
</tbody>
</table>

Source: Immobilien Rating

**Top rents for Viennese offices up slightly once again**

Rents for office space in Vienna remained largely stable in 2015 and the first half of 2016, although prices rose slightly once more last year in the premium segment. Top rents for class A office space in attractive locations were around EUR 26/m²/month in mid-2016.

However, rental costs can be higher for certain spaces in premium-quality properties, such as the top floors of office towers, and for highly exclusive premises. Rents in the premium segment could increase again slightly by the end of this year, but are expected to remain fairly stable on the whole.

Demand remains high for space in the city center and other key office locations, and there is also continued strong interest in offices in the mid-price segment. The comparatively large supply of modern office space at affordable prices is sufficient to satisfy demand. Effective use of floor space and low operating costs are among the key decision-making criteria for prospective tenants. Total costs play a far more decisive role in selecting office locations than the rental price alone. Certification is also growing in importance, and most big-name tenants are unlikely to rent spaces that have not been certified according to standards such as DGNB, ÖGNI, LEED or BREEAM.

There is persistent pressure on office buildings with low occupancy rates, old space in need of renovation, and premises in unattractive areas outside the most popular office locations, without suitable amenities and links to the public transport network. This negative trend has been apparent for some time, and has resulted in falling rents and rising vacancy rates.
Office vacancy rates generally stable
Vienna still has one of the lowest vacancy rates in Europe, and the relatively low level of new construction in recent years has helped to keep rates down. In mid-2016 the office vacancy rate in the Austrian capital was about 6.25%; this could fall further due to the lack of new builds this year and the level of new lettings anticipated in the remainder of 2016. It comes as no surprise that vacancies at older properties are frequently higher than at centrally located offices for which demand is strong. That said, though, vacancy rates are above average in some office towers. The effect of the sharp increase in new construction in coming years on vacancies remains to be seen. The main question is whether the removal of old spaces from the market will be balanced out by new construction and new letting.

Prime yields under pressure
Prime yields in Vienna’s office sector fell slightly in 2015, and again in the first six months of 2016, reaching around 4.1% at the end of the first half. No significant changes in yields are expected until the end of this year. However, a further decline in prime yields due to continued demand in the premium segment cannot be ruled out.

Vienna’s office hotspots
Central Vienna and the neighboring districts remain the most popular office locations, and demand is still high. Offices and numerous retail spaces dominate the city center, and over the past few decades the number of residential properties has fallen gradually. However, in the past few years, as a result of strong demand for large apartments and luxury residential space, parts of the city center have seen the reconversion of former office locations into apartments. Buildings dating back to the Gründerzeit era around the middle of the 19th century are particularly popular for this purpose, because the generously proportioned floor layouts cater to the demands of wealthier clients for expansive luxury living space. In the meantime this luxury boom has lost steam somewhat, and with high net worth buyers – in particular from Russia – leaving the market, market, this has sometimes had a detrimental effect on demand.

Numerous office properties are located inside the Gürtel outer ring road. The popularity of the districts bordering the city center is mainly a result of their location and ease of access, although new constructions are rare in these areas.

Besides the city center, the Donaucity (VIENNA DC) has grown to become one of the capital’s most important office locations. The skyline is dominated by several office towers, including the tallest in Vienna, DC Tower 1, which has further enhanced the standing of the Donautal area. A slightly smaller second tower – DC Tower 2 – is at the planning stage.

New office hotspots have sprung up in the areas around Handelskai and the Messe Wien exhibition center, and close to the site of the former Nordbahnhof and Nordwestbahnhof stations. The area around Praterstern – where the Austria Campus is currently under development – is one of Vienna’s largest urban development zones. In the near term, the Nordwestbahnhof site, which is still used as a rail freight station, will provide city planners with a host of options for creating a leafy district suited to a range of uses.

New offices built in the past few years, such as Marxbox and Marxim, as well as TownTown, which is gradually being expanded, have turned the Erdberg, St Marx and Gasometer areas into key office locations. The TownTown complex will be extended again by next year with the addition of the ORBI Tower.

Wienerberg in southern Vienna is now another firmly established office location. Phase 6 of the extension of Euro Plaza will see the creation of additional office space at the site.
Vienna’s newest office location has sprung up around the now-completed Hauptbahnhof, where the new headquarters of Austrian Federal Railways (ÖBB) and – among others – Erste Bank are located.

**Hauptbahnhof: an object lesson in developing a city-center office location**

The area around the new Hauptbahnhof is not yet complete. Further projects are now getting under way, including QBC 3 and 4, THE ICON VIENNA and purely residential developments such as PARK-APARTMENTS AM BELVEDERE.

These will add to the location’s cachet, as well as breathing new life into the district, as the new developments will also include a diverse mix of apartments, shops, hotels, catering outlets, service providers and health facilities, in addition to office space.

The developers will be looking to avoid the mistakes made in parts of the neighboring Sonnwendviertel area, which is criticized as being bland, cramped and monotone, as well as lacking green spaces. In view of the scope of the planned developments, it remains to be seen whether this can be achieved.

But the Hauptbahnhof site has already made its name as one of Vienna’s most sought-after locations in a very short time. There is strong demand for space in the properties now under construction, and by all accounts some of the offices have already been pre-let.

From an architectural point of view, the site also has plenty to offer – standing 88m, 66m and 38.5m, the three striking towers that make up THE ICON VIENNA will be a landmark feature. So developments look set to remain exciting at one of the last remaining urban development areas in the center of the Austrian capital.
Retail: the shift from ‘place to shop’ to ‘place to be’ – a success story?

Shopping centers (SCs) in Austria: fewer centers, same total space
As of 30 June 2016 there were around 125 shopping centers in Austria, with a combined gross lettable area of 2.7 million m². Although the number of centers dropped by two, the overall amount of space available remained virtually unchanged.

Since 2015 only one brand-new shopping center has opened in Austria (excluding Vienna) – the Weberzeile in Ried (approx. 22,500 m²). Three smaller locations (the Interspar shopping centers in Wels and Mistelbach, and Merkur City in Wiener Neustadt) have been remodeled or rebuilt. Construction work, which continues with only very limited areas of the centers in question in operation, is expected to be completed in 2016/2017. The Shopping Arena in Salzburg (formerly SC Alpenstraße) was demolished and rebuilt in 2015/2016.

Continuing trend towards modernization and expansion
The centers named above reflect the latest trend: a significant drop in the number of new openings in favor of modernization, relaunches and remodeling projects, as well as a distinct move in favor of demolition and reconstruction and the expansion of existing well-performing locations. Examples include the Fischapark in Wiener Neustadt, as well as Traisenpark in St. Pölten, which completed its latest phases of expansion in 2015/2016, bringing an additional 42,000 m² and 32,000 m² respectively.

Austria (excl. Vienna)
Selected SC projects under construction

<table>
<thead>
<tr>
<th>Shopping center</th>
<th>Gross lettable area (GLA), m²</th>
<th>Scheduled opening</th>
</tr>
</thead>
<tbody>
<tr>
<td>ELI Liezen</td>
<td>~15,000</td>
<td>H2 2016</td>
</tr>
<tr>
<td>Merkur City new Wr. Neustadt</td>
<td>~15,000 (relaunch and expansion)</td>
<td>H2 2016</td>
</tr>
<tr>
<td>Interspar Wels</td>
<td>~15,000 (demolition and rebuild)</td>
<td>2016/2017</td>
</tr>
<tr>
<td>Interspar Mistelbach</td>
<td>~10,000 (demolition and rebuild)</td>
<td>2016/2017</td>
</tr>
</tbody>
</table>

The fact that the Austrian market is already amply served with shopping centers is the main factor behind the slow addition of new space. It is also becoming increasingly difficult for developers to obtain permits for new builds or expansion projects in out-of-town locations, particularly as some city centers are faced with high vacancy rates.

Austria (excl. Vienna)
Selected SC openings, 2015/H1 2016

<table>
<thead>
<tr>
<th>Shopping center</th>
<th>Gross lettable area (GLA), m²</th>
<th>Opened</th>
</tr>
</thead>
<tbody>
<tr>
<td>Weberzeile Ried</td>
<td>~22,500</td>
<td>H2 2015</td>
</tr>
<tr>
<td>Traisenpark St. Pölten (expansion)</td>
<td>~13,500</td>
<td>H1 2016</td>
</tr>
<tr>
<td>Fischapark Wr. Neustadt (expansion)</td>
<td>~12,000</td>
<td>H2 2015</td>
</tr>
<tr>
<td>Shopping Arena Salzburg (demolition and rebuild)</td>
<td>~24,000</td>
<td>H1 2015</td>
</tr>
</tbody>
</table>

Source: Immobilien Rating, Standort+Markt, RegioPlan

This trend will continue. As things stand, only one new shopping center is under construction: ELI in Liezen (approx. 15,000 m²). At present there are no other new projects under development.

Shopping centre space in Europe
Leasable area in m² per 1,000 inhabitants


Compared with other European countries, Austria is in the top 10 in 2016 with 332 m² of lettable space per 1,000 inhabitants, which is significantly above the EU-28 average of approx. 238 m² per 1,000 inhabitants.
The Generali Center (mixed-use office and retail property) on Mariahilfer Straße is also currently being refurbished. After the scheduled reopening at the end of this year the new development, named Mahü 77, will have three major tenants (Eurospar, TK Maxx and CCC) covering approximately 7,500 m² in place of the previous 26 smaller retailers.

Elsewhere on the Viennese market, only significantly smaller retail spaces of under 10,000 m² are in the pipeline or under construction (e.g. Post am Rochus – Mein Marktplatz im 3., Trienno – Eurogate expansion and Einkaufen am Spitz). Mainly local neighborhood developments, they offer everyday shopping and catering amenities. Implementation of the Vio Plaza project (office and retail building with shopping center) with around 13,000 m² of retail space on the old Komet site in Meidling has been on hold for more than ten years now.

Areal density of shopping center space in Vienna unchanged

In Vienna the areal density of shopping center space per 1,000 people is currently unchanged year-on-year, at around 520 m². Any increase through moderate expansion was immediately offset by the above-average population growth in the city (up 2.8% in 2015/H1 2016).

The greater Vienna area has five large-scale shopping centers with more than 45,000 m² of lettable space. There are also 13 smaller shopping centers of less than 20,000 m². In terms of percentage share, the smaller segment has conceded seven percentage points over the past five years and now accounts for around 43% of the total.

Vienna SC projects under construction

<table>
<thead>
<tr>
<th>Shopping center</th>
<th>Gross lettable area (GLA), m²</th>
<th>Scheduled opening</th>
</tr>
</thead>
<tbody>
<tr>
<td>Huma Eleven phase II (demolition and rebuild)</td>
<td>~ 20,000</td>
<td>2017</td>
</tr>
<tr>
<td>Mahü 77** (relaunch)</td>
<td>~ 7,500</td>
<td>2016</td>
</tr>
</tbody>
</table>

*1) no longer a conventional shopping center following rebuild
Source: Immobilien Rating, Standort+Markt, RegioPlan

1) The center will continue to operate during construction work, albeit with severely restricted capacity, which will give rise to significant variances in calculations of the amount of space in the various periods.

2) The shops will no longer have a shared entrance or mall space. In terms of statistics, they will form part of the retail space on Mariahilfer Straße.

Vienna SC openings, 2015/H1 2016

<table>
<thead>
<tr>
<th>Shopping center</th>
<th>Gross lettable area (GLA), m²</th>
<th>Opened</th>
</tr>
</thead>
<tbody>
<tr>
<td>Citygate shopping mall</td>
<td>~ 17,500</td>
<td>H1/2015</td>
</tr>
<tr>
<td>Huma Eleven phase I (demolition and rebuild)</td>
<td>~ 30,000</td>
<td>H1/2016</td>
</tr>
</tbody>
</table>

Source: Immobilien Rating, Standort+Markt, RegioPlan

Rebuilt on the site of the old development, the Huma Eleven shopping center (the former Huma Einkaufspark) in Simmering is a special case. Following the demolition of the old center, the first phase opened in March this year with 60 shops on around 30,000 m². By the time it is completed in fall 2017, the 50,000 m² center will comprise 90 shops.

Number of shopping centers by size

<table>
<thead>
<tr>
<th>Number</th>
<th>Gross lettable area (GLA), m²</th>
</tr>
</thead>
<tbody>
<tr>
<td>13</td>
<td>Up to 20,000</td>
</tr>
<tr>
<td>12</td>
<td>20,000-45,000</td>
</tr>
<tr>
<td>5</td>
<td>more than 45,000</td>
</tr>
</tbody>
</table>

Source: Immobilien Rating, RegioPlan, Standort+Markt

1) The center will continue to operate during construction work, albeit with severely restricted capacity, which will give rise to significant variances in calculations of the amount of space in the various periods.
Real Estate Country Facts

Shopping centers expected to function as distinctive all-rounders and “places to be”

A number of the shopping centers in Vienna have been extensively modernized, extended or relaunched over the past five years to ensure their continued competitiveness in the era of online retailing and increasingly divergent customer requirements. Customers are becoming more and more discerning, which is leading to a greater range of shopping opportunities.

In an ideal world, modern and contemporary shopping centers should be distinctive all-rounders, which rather than “places to shop” are looking to become “places to be”. The aim is to create a USP over pure online sales and add value for visitors as part of a next-generation “shopping 2.0 experience”. There is a vast range of options available, depending on the type, size and positioning of the shopping center.

Providing a superior quality ambience (e.g. attractive architecture and floor plans, lighting, quiet zones, cleanliness, interior décor, etc.) is now a fundamental requirement in today’s centers. Many malls are trying to increase the length of time that visitors stay and optimize the overall shopping experience by offering a higher proportion of restaurant, lifestyle and entertainment options. Integration of bricks-and-mortar shops with the online world (click and collect, order and collect, click and eat, etc.), amenities (WiFi, kids’ zone, delivery service, etc.) and regional touches (regional and local stores) are playing an increasingly important role.

In terms of tenants’ demand for space, there is a trend towards flexible space concepts which range from new mini formats (1,000 m² Media Markt at the Rosenarcade Tulln, 300–700 m² Saturn Connect stores, IKEA outlets with pick-up points, etc.) to flagship stores at top locations. Industries that face stiff competition online (such as books, electronics, footwear and clothing) are scaling back their expansion plans, and focusing instead on optimizing existing locations and space usage while investing more heavily in location quality. These developments are being felt most strongly by shopping centers in B and C locations in the form of reduced demand for rental as well as closures.

Prime yields at shopping centers declining, rental prices stable

Monthly rents at shopping centers in Vienna in mid-2016 ranged from EUR 8–120/m²/month depending on store size. Prices at premium shopping centers are holding firm (for smaller units of less than 250 m²) or increasing slightly. By contrast, B and C locations are coming under increasing pressure and are often confronted with the need to cut rents.

Austria has enough retail parks

The market in Austria is well served with retail parks and retail park agglomerations, with a concentration of 586 m² per 1,000 people. Total space in this segment as of 30 June 2016 amounted to around 5.1 million m², about 30% of which was accounted for by retail parks.

The pace of expansion on the retail park market has slowed significantly in recent years due to high availability. It is also becoming increasingly difficult for developers to obtain permits for attractive locations. Only three retail parks with more than 10,000 m² of lettable space opened in Austria last year (Galleria Danubia in Hainburg, Pado Shopping Park in Parndorf and City Center in Völkermarkt). Expansion of the Hatric retail park in Hartberg from around 11,000 m² to 28,000 m² is scheduled for completion by fall 2016. While there are only a handful of projects in the pipeline for the immediate future, in most cases it remains to be seen whether they will actually come to fruition.
No changes in Vienna retail park market

There has not been any significant change in the amount of retail park sales space in Vienna, which remains just short of 750,000 m² (including the retail park agglomeration in Vösendorf, Lower Austria) for a concentration of approximately 398 m² per 1,000 inhabitants.

The five largest retail park agglomerations represent around two-thirds of the overall market; these include the retail park area around Shopping City Süd (SCS) on the southwestern outskirts of Vienna, with more than 200,000 m² of retail space. The next largest are located northeast of the Danube, on the city’s northernmost edge next to the S2 highway (Stadlau and Rautenweg retail park agglomerations) and on Brünner Straße.

Retail park trends: newer, bigger and more attractive

As with shopping centers, demographic shifts and online trade are putting pressure on retail parks’ ability to compete. As a result, construction quality, creating pleasant surroundings and offering a feelgood atmosphere are increasingly coming into focus. Operators are trying to address contemporary customer requirements and attract the necessary footfall through a broader-based tenant mix, range of catering options and entertainment programs.

As a result the lines between shopping centers and retail parks are becoming increasingly blurred. A number of new and/or refurbished locations are adopting hybrid forms (e.g. retail-park-oriented shopping centers) inspired by the general concept of “newer, bigger and more attractive”. Consequently, traditional shopping center tenants such as C&A, Ernsting’s Family, Depot, Intersport and Hervis are increasingly moving into retail parks. That aside, attractive large-format supermarkets and discounters are still important ways of increasing footfall as part of a well-functioning retail park.

Retail park rents

<table>
<thead>
<tr>
<th>Shops (depending on size and location)</th>
<th>6–15</th>
</tr>
</thead>
</table>

Source: Immobilien Rating

Demand remains healthy for rental space at easily accessible retail parks with high-level functionality and a balanced tenant mix. Rental costs for retail park units range from EUR 6–15/m² per month. Slight increases in rents are only expected for smaller units.
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Lender: UniCredit Bank Austria AG

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