Intelligent Investment

Market Outlook 2023

REPORT

FINLAND

REAL ESTATE

CBRE RESEARCH

Contents

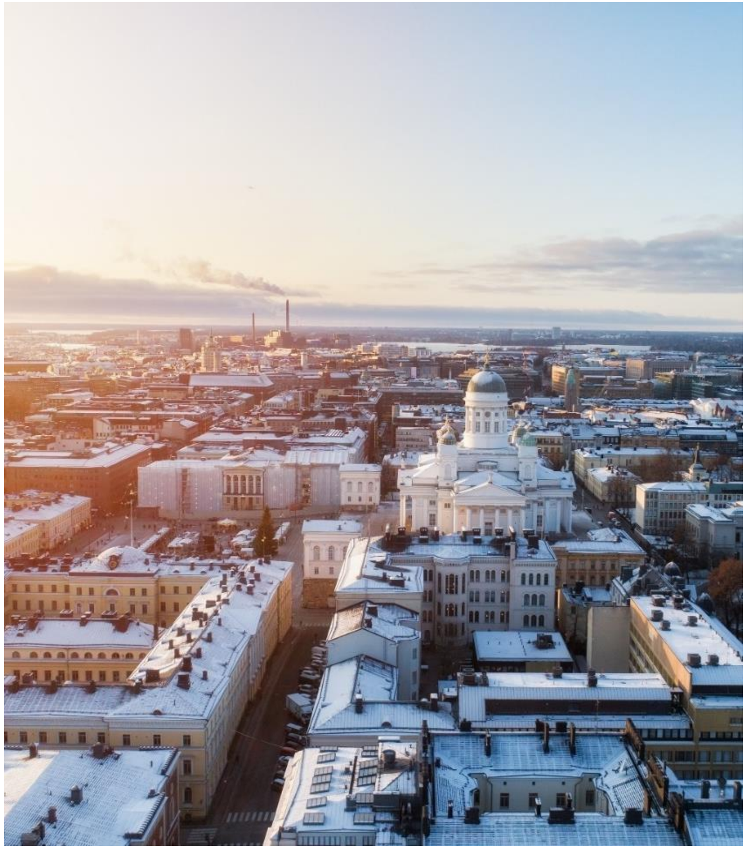
Introduction

Finnish real estate market saw a year of two different halves in 2022 with the first six months reaching new record volumes, while the second half saw a slowdown in investment over rising cost of capital and continued high inflation. Economy will see a moderate slowdown in 2023 with continued high inflation and increases in interest rates putting brakes on the economic activity. Real estate investment is expected to pick up after the pricing environment balances out in early 2023 and recovery is expected in the second half of 2023.

Siri Tulikoura
Managing Director, CBRE Finland

The Finnish economy is forecasted to enter a moderate recession declining by 0.2% in 2023 due to continued high inflation, slowing business and consumer demand and tighter financial conditions. Investment market had a strong year in 2022 with €7.23 billion in investment, up 1% year-over-year, driven by record volumes in the first half of the year. Residential sector was again the leading sector, drawing in a record level of foreign capital, and the second largest sector, social infrastructure, saw record-high investment activity with several large-scale deals in 2022. The shift in the pricing environment was one of the main themes in 2022, and sector prime yields saw decompression of 60 to 90 basis points from the early-2022 lows to reflect this change. Investment market is expected to pick up in the second half of 2023 as there remains a high level of dry powder in the real estate market. Despite short-term uncertainty, the long-term fundamentals of the Finnish market remain strong.

Sustainability will continue to have an increased importance for all market participants in the Finnish real estate market. Finland has set one of the most ambitious sustainability policies in the world, targeting carbon neutrality in 2035. Importance of sustainability is increasing in the real estate market as participants take concrete actions for reaching their sustainability goals.

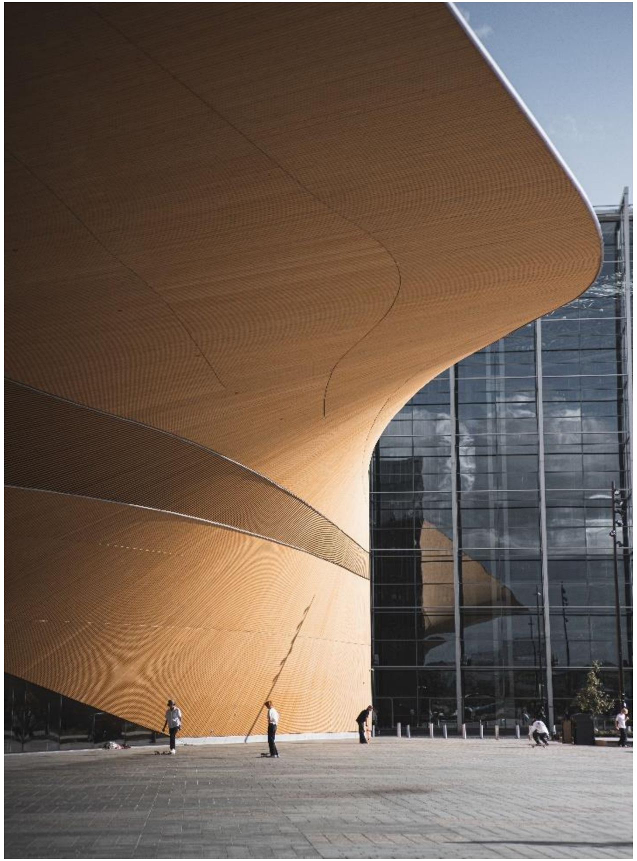


01

Economy

Economy will see a moderate recession in 2023 and GDP will fall by 0.2% in 2023 with continued high inflation and the increase in interest rates putting brakes on the economic activity.

Key Takeaways – Economy



01

FINNISH ECONOMY CONTINUED THE PANDEMIC REBOUND IN 2022

Finnish economy grew by 1.9% in 2022, while monetary tightening and falling business and consumer sentiment tapered growth towards the end of the year.

02

HIGH INFLATION AND TIGHTER MONETARY POLICY WILL SLOW THE ECONOMY IN 2023

Finnish economy is forecasted to enter a moderate recession declining by 0.2% in 2023 due to continued high inflation, slowing business and consumer demand and tighter financial conditions.

03

STRONG LABOUR MARKET THE BRIGHT SPOT FOR THE ECONOMY

Labour market has remained strong despite increased uncertainty, but there is more uncertainty and a rise in unemployment expected as the economic activity softens.

04

FINLAND REMAINS A RESILIENT AND POLITICALLY STABLE INVESTMENT LOCATION

Finland has proved resilient during difficult economic times, and the well-functioning and politically stable environment with high ambition in sustainability and green transition will remain a viable location for investment.

Economy

Continued post-pandemic rebound in 2022

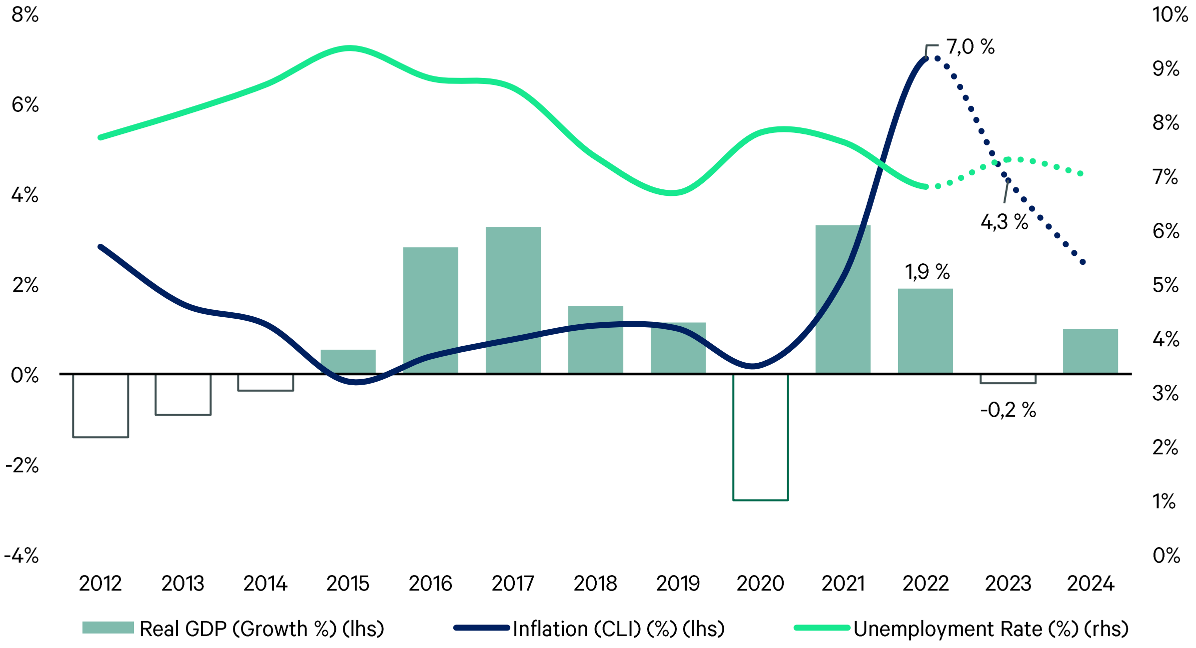
Finnish economy grew by 1.9% and unemployment decreased to 6.8 % in 2022. The labour market continued to show strength and companies reported difficulties in recruiting due to record amount of new job openings and labour shortages.

Inflation saw a large uptick during the year with the recovery from the pandemic, supply bottlenecks and rise in energy prices driving prices higher. The December inflation rate came in at 9.1% (y-o-y) and the average inflation rate rose to 7.0 % in 2022.

Finland fared relatively well despite the European energy crisis as the country had a low reliance on Russian gas exports and the energy sector showed resilience with many of the energy importers succeeding in replacing Russian oil with other sources and continued growth in renewable energy balancing the energy mix during winter months.

Finnish economy will see a moderate recession in 2023 on the back of continued high inflation, slowing business and consumer demand and tighter financial conditions. Finland's GDP is expected to decline by 0.2% in 2023, and unemployment rate will increase to 7.3% as economic and labour market activity trends lower. The surge in inflation is expected to settle down from the highs towards the end of 2023, while tighter monetary policy and easing of the energy crisis will begin to impact inflation.

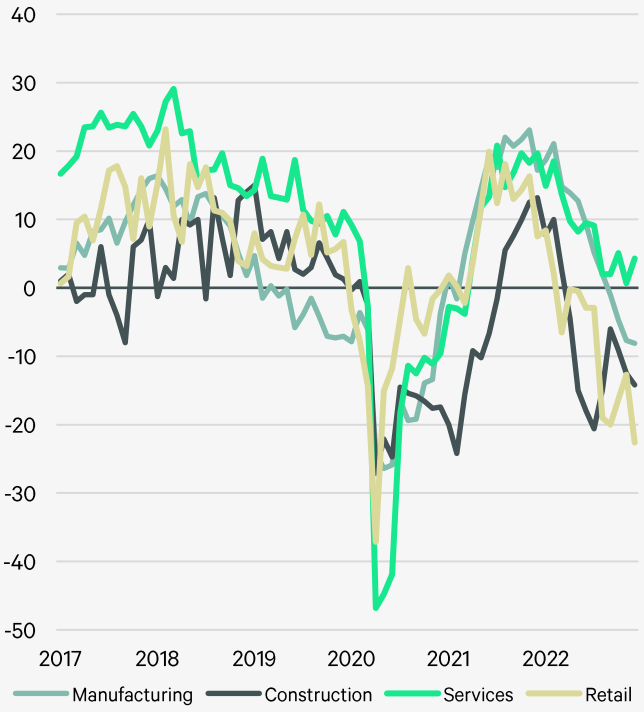
Figure 1. GDP growth, inflation and unemployment rate in Finland.



Source: CBRE Research, CBRE House view, January 2022.

Economy

Figure 2. Business confidence indicators in Finland.



Source: Statistics Finland, Confederation of Finnish Industries, CBRE Research.

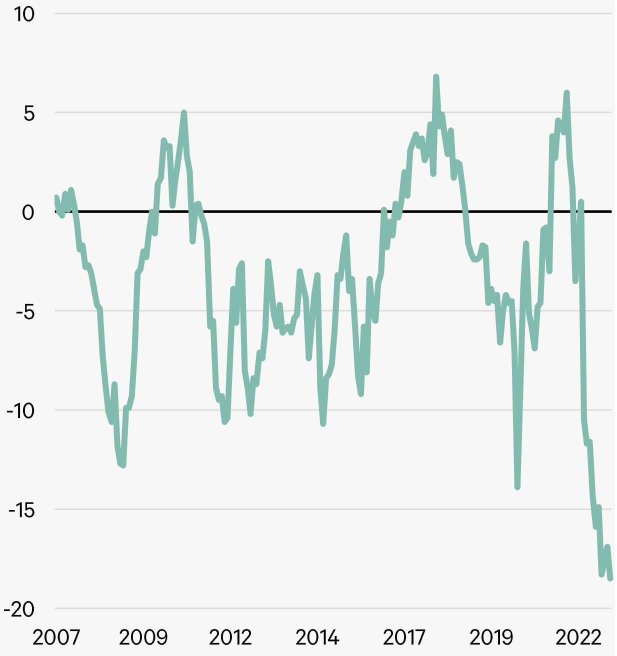
Business and consumer sentiment drop-off

Businesses have remained resilient despite higher uncertainty over slowing economy and spiking inflation. The main industries in Finland have entered the downturn in solid financial condition and strong orderbooks but listed companies reported softer numbers during the last quarter as inflation and slowdown in key trading partners have had their impact. Retail activity saw a boost from the removal of all pandemic restrictions in early 2022. Retail sector continued to have a strong performance with sales and footfalls rebounding despite increased uncertainty in the last quarter.

Retail, construction and manufacturing confidence have trended below the long-term average levels during 2022, and there will be continued downward pressure for company earnings going forward. Consumer sentiment was quick to react to uncertain market conditions, and the Finnish consumer confidence index fell to historical lows in 2022 on the back of the consumer cost crunch.

We expect Finland's economy to withstand the moderate slowdown well in 2023, while the longer-term challenges for the economy remain the rapid pace of ageing population and the need for public sector restructuring. Finland has proved resilient during difficult economic times, and the well-functioning and politically stable environment with high ambition in sustainability and green transition will remain a viable location for investment.

Figure 3. Consumer confidence in Finland 2007-2022.



Source: Statistics Finland, CBRE Research.

02

Investment

Real estate investment volumes reached €7.23 billion in 2022, highest volumes since 2018. Investment market is expected to pick up in the second half of 2023 as there remains a high level of dry powder in the real estate market.

Key Takeaways – Investment

01

STRONG YEAR FOR THE FINNISH INVESTMENT MARKET

The first half of 2022 was record-breaking with investment totaling €4.6 billion, and full-year investment volumes crossed the €7 billion threshold with €7.23 billion, up 1% (y-o-y) and highest volumes since 2018.

02

RESIDENTIAL REMAINS LARGEST, SOCIAL INFRASTRUCTURE REACHED NEW RECORD

Residential sector remains the largest sector in 2022 with 29% of the total investment volume of €2.1 billion, followed by social infrastructure (26%, €1.9 billion) and retail (16%, €1.2 billion).

03

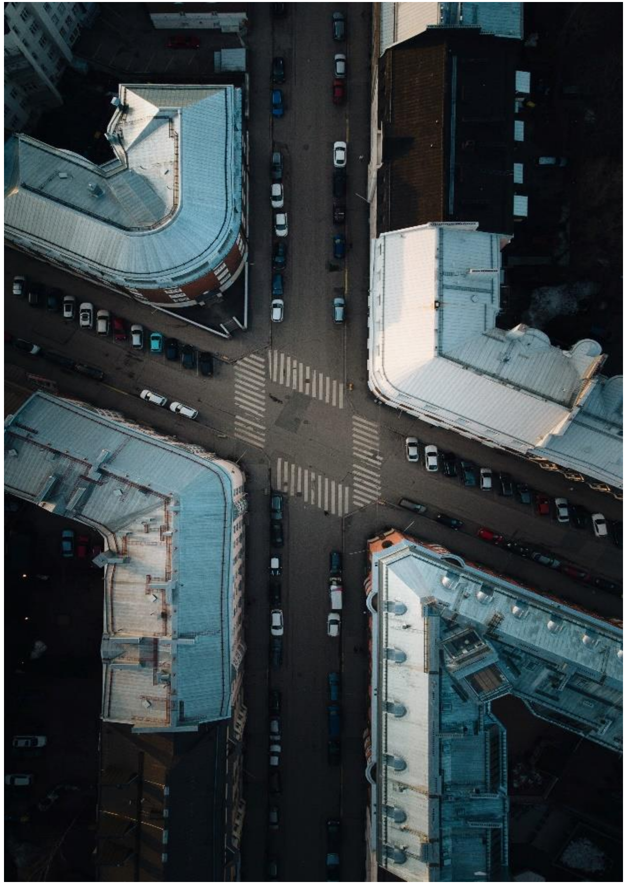
RISING INTEREST RATES AND FINANCING COSTS PUSH YIELDS UPWARDS

Prime yields decompressed 60 to 90 basis points during 2022 as European Central Bank began the monetary tightening and financing costs increased drastically.

04

ESG ADOPTION CONTINUES DESPITE A CHALLENGING LANDSCAPE

According to CBRE Investor Intentions Survey 2023, 81% of investors will continue to adopt ESG criteria in all investment decisions despite macro-economic headwinds and a challenging geopolitical landscape.



Record first half of 2022 propelled real estate investment higher

Strong year for Finnish real estate investment

Despite the increased uncertainty, 2022 was a strong year for Finnish real estate investment. The first half of 2022 was strongest on record with real estate investment totalling €4.6 billion, and full-year investment volumes crossed the €7 billion threshold ending the year at €7.23 billion, up 1% from the previous year. This marks the highest investment volume since 2018 for the Finnish market.

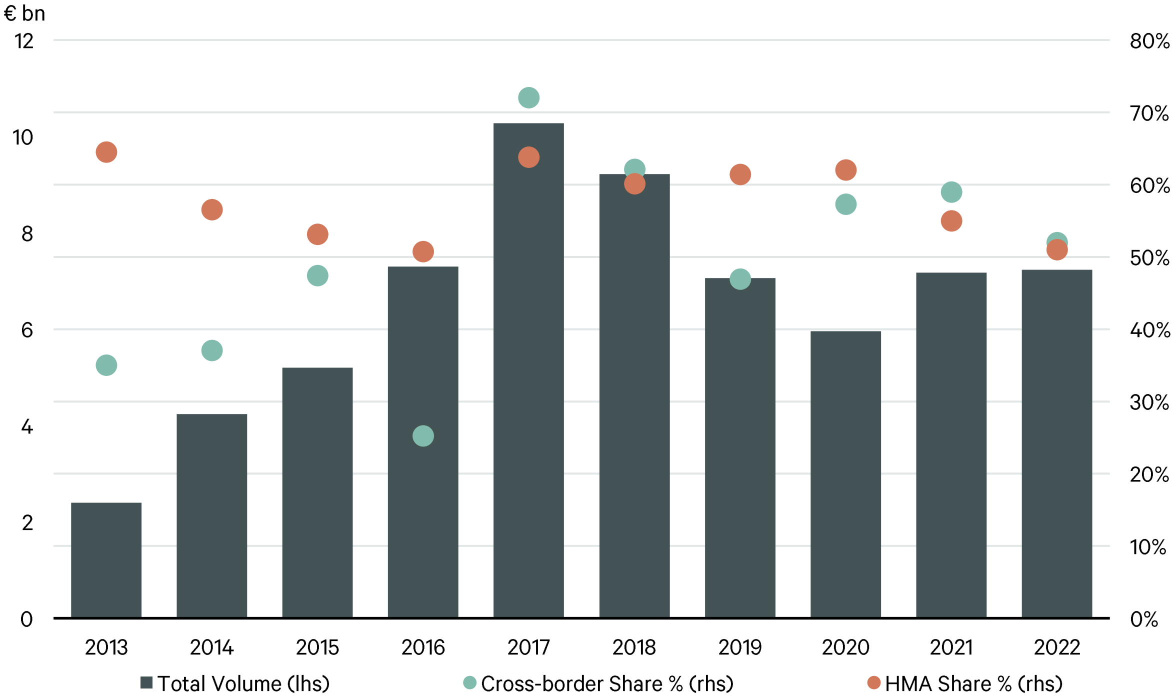
Market activity slowed down towards the end of the year as a result of the growing market uncertainty caused by global inflationary pressures and rising interest rates. Fourth quarter investment volumes slowed down to €1.05 billion, down 57% year-over-year.

Cross-border capital remains active in Finland

International investors continue to view Finland as one of their core investment locations despite temporary slowdown, and central European and other active cross-border investors have kept deploying more capital to the Finnish market in 2022. 52% of total investment volume came from cross-border investors, and Helsinki Metropolitan Area's share of the total investment volume was 51% in 2022.

Capital city region remains the key driver of transactional activity, and in some sectors, such as industrial and logistics, the activity has spread out to the larger Greater Helsinki region due to lack of zoning and limited new supply of investable product in Helsinki, Espoo and Vantaa.

Figure 4. Investment volumes, cross-border share and Helsinki Metropolitan Area share of total volumes.



Source: CBRE Research.

Residential remains the largest sector, social infrastructure reached a new record in 2022

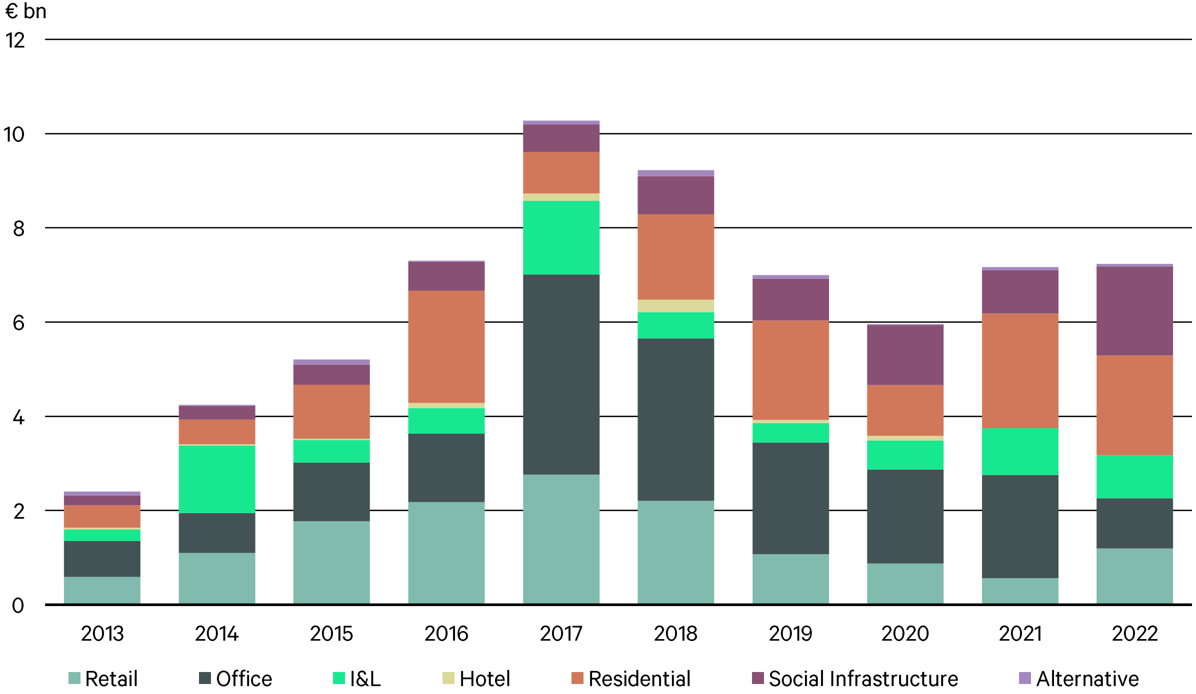
Several large-scale transactions in 2022

Residential sector remains the largest sector in 2022 with 29% of the total investment volume (€2.1 billion), followed by social infrastructure (26%, €1.9 billion) and retail (16%, €1.2 billion). Office investment reached €1.1 billion with 15% of total investment, and the industrial and logistics sector has attracted €907 million and 11% of total investment in 2022. Retail and social infrastructure sectors had the strongest growth from the previous year as investment more than doubled in these sectors.

Finnish investment market witnessed several large-scale transactions during 2022, and the largest transaction in 2022 was Orange Capital Partners' acquisition of over 2,200 apartments from Starwood and Avara in August, where CBRE advised the seller. Orange Capital Partners and GIC acquired another nationwide residential portfolio with 1,900 apartments from Morgan Stanley in March and Heimstaden continued its expansion in Finland with the purchase of over 2,000 apartment portfolio from Sato in April as residential remained in the crosshairs for investors.

Other notable deals during 2022 were KEVA's acquisitions of the Stockmann department store for €400 million and Kaari shopping centre for €207 million as well as Lähitapiola's €300 million acquisition of the Espoo hospital from the City of Espoo.

Figure 5. Investment volumes by sector.



Source: CBRE Research.

Prime yields decompress amidst higher interest rates and cost of capital

Peak-to-trough yield shifts of 60 to 90 basis points

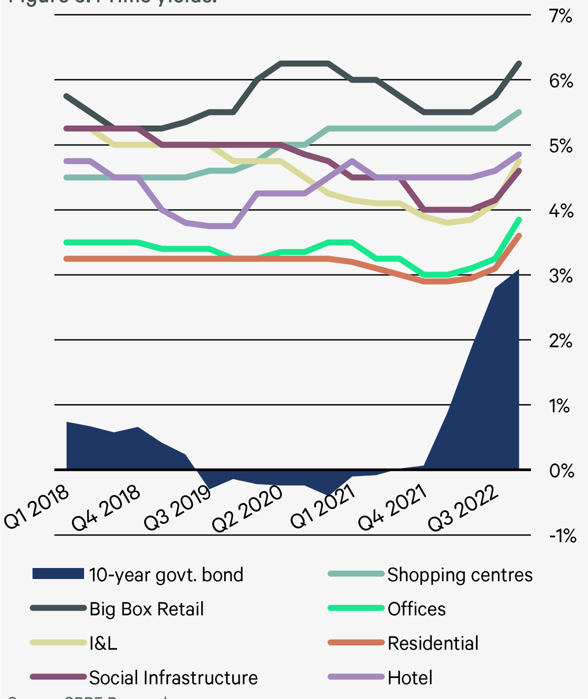
Prime yields decompressed due to increased financing costs and rising interest rates. Residential and office prime yields decompressed 70 to 85 basis points and stood at 3.60% and 3.85% at the end of the year, respectively.

Industrial and logistics sector was one of the sectors most influenced by the shift in pricing dynamics and prime logistics yield moved to 4.75%, up 85 basis points year-over-year. Prime yield for social infrastructure moved out 60 basis points to 4.60%, while hotels, shopping centres and big box retail yields were standing at 4.85%, 5.50% and 6.25%, respectively.

The mismatch in buyer and seller pricing expectations, tighter lending conditions and recession fears made it more difficult to close deals in the second half of 2022. These were the main challenges cited by investors in the CBRE Investor Intentions Survey 2023.

Survey respondents signalled a willingness to sustain purchasing/selling activity as well as maintain or increase allocations to real estate. When putting capital to work, investors favour opportunistic and distressed strategies as they seek to capture attractive yields. These findings provide a degree of optimism for continued European and Finnish real estate market activity despite the difficult economic backdrop.

Figure 6. Prime yields.



Source: CBRE Research.

ESG and green credentials in the spotlight

According to CBRE Investor Intentions Survey 2023, over 80% of investors affirmed that they would continue to apply ESG criteria to all investment decisions, and the most popular ESG strategy is to upgrade existing assets to meet the standards of sustainability certifications. Additionally, one-third of investors surveyed stated that they were willing to pay a premium to acquire ESG friendly assets. More than half of those willing to pay a premium said the premium could be more than 20%.

Opportunities arise as asset pricing stabilises

CBRE forecasts that 2023 European investment volume will decrease 5-10% relative to 2022 levels, and Finnish real estate will see similar downward trend in investment volume. However, current market environment will present opportunities as the asset pricing is expected to stabilise in 2023, and a recovery may commence in the second half of 2023 as macroeconomic challenges abate.

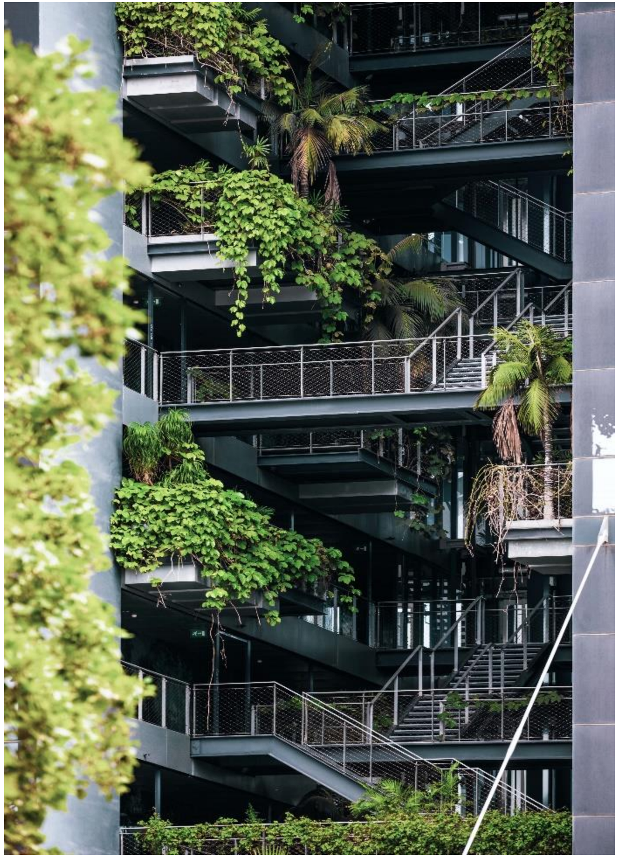
The Finnish investment market has not seen a full stop in activity and continues to be active with several deals in the pipeline. Despite the uncertainty from spiking inflation and short-term slowdown in the economy, Finnish market will continue to see activity in different sectors in 2023. The continued central bank interest rate hikes and the cost of financing will be key themes for the next 12 months.

03

Sustainability

According to CBRE Investor Intentions Survey 2023, over 80% of investors affirmed that they would continue to apply ESG criteria to all investment decisions, and the most popular ESG strategy is to upgrade existing assets to meet the standards of sustainability certifications. The focus for ESG and sustainability will continue to intensify during 2023.

Key Takeaways – Sustainability



01

The changed energy price environment is set to continue throughout 2023. High prices will create strong incentives to improve energy efficiency. Sustained higher electricity prices will make onsite renewable energy sources more attractive.

02

A better understanding of the value of sustainability features will be established as sustainability data is increasingly integrated into asset valuations. This will allow increasingly accurate measurement of how green features can protect against value depreciation and insulate assets from transition risks.

03

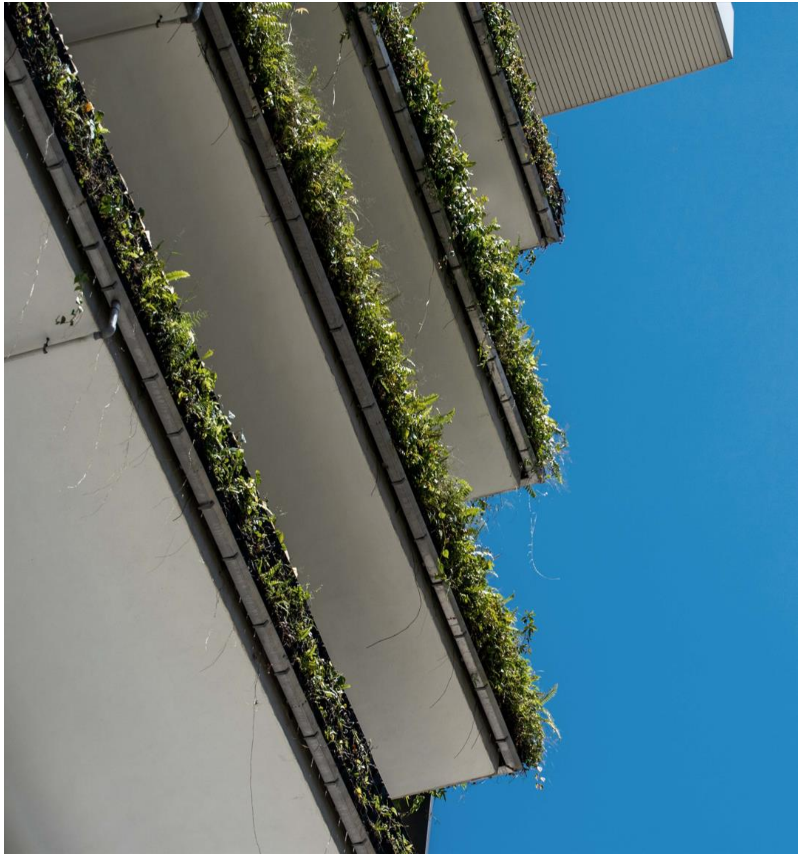
Rental premiums[1] for sustainable buildings, currently only measured in the office sector, will appear in other sectors as tenants and end-users start to demand higher levels of environmental performance.

04

Greater scrutiny of net zero buildings will occur as demand increases and more come to market in 2023. Despite net zero guidelines, there is a lack of transparency and verification for net zero assets and currently no formalized certification process

[1]Source: CBRE Research, Is Sustainability Certification in Real Estate worth it?, November 2022

Sustainability



In the context of dramatically increasing energy prices and ongoing climate change, sustainability concerns have never been as salient an issue as in 2023. Investors and occupiers alike are continuing to showcase their demand for the most sustainable stock through hefty premiums, causing significant divergence in pricing between primary and secondary assets which shows no sign of abating. This will continue to influence real estate decisions into the future.

LOOKING AHEAD

Sustainability and ESG concerns more generally will continue to exert significant pressure on investment committees and corporate decision-making in 2023. These pressures are compounded by an increasing need for investors to incorporate or pre-empt future sustainability policy into asset allocation decisions.

Companies and policymakers will contend with a number of new or impending directives in 2023 including:

- The implications of 2030 net-zero (or carbon reduction) targets,
- The European Union's Sustainable Finance Disclosure Regulation (SFDR),
- Corporate Sustainability Reporting Directive (CSRD).

While green premiums are difficult to disaggregate and precisely measure, the existence of such premiums is clearly apparent in some sectors and the demand for stock with the highest sustainability ratings is clearly more robust[1].

Contrary to narratives regarding the "stranding" of secondary assets, CBRE believes that 2023 will bring significant opportunities for "brown-to-green" refurbishment, particularly in offices, as falling secondary prices significantly increase the viability and potential returns of such projects.

[1]Source: CBRE Research, Is Sustainability Certification in Real Estate worth it?, November 2022

04

Offices

Investors and occupiers alike are more focused on higher quality properties in prime locations across the Helsinki Metropolitan Area office submarkets. This flight to quality trend and sustainability are the key themes for offices in 2023.

Key Takeaways – Offices

01

OFFICE INVESTMENT VOLUME LOW COMPARED TO 2021

Office investment reached €1.07 billion in 2022, down 51% from the previous year. Increased financing costs and higher uncertainty pushed prime yields higher towards the end of 2022.

02

INVESTOR DEMAND CENTRED TOWARDS CORE OFFICE PROPERTIES

Amidst uncertainty more emphasis is being placed on environmentally certified assets, as well as strong, established locations and robust tenant credits.

03

OCCUPATIONAL DEMAND STRONG IN CENTRAL LOCATIONS

Leasing activity is even more centred in prime locations in Helsinki CBD and other strong submarkets as companies are fitting the needs of hybrid work.

04

SUSTAINABILITY REMAINS HIGH ON THE LIST FOR OFFICE INVESTORS

Demand is highest for environmentally certified offices as investors have set ambitious sustainability targets, and are keeping high standards for new office investments.

05

RESTORING THE CONNECTION

As employees returned to their physical workplaces, there occurred a growing emphasis on tech-enabled and wellness-capable buildings, in order to foster a sense of community among employees.

Modest office investment volume in 2022

Office investment declined in 2022

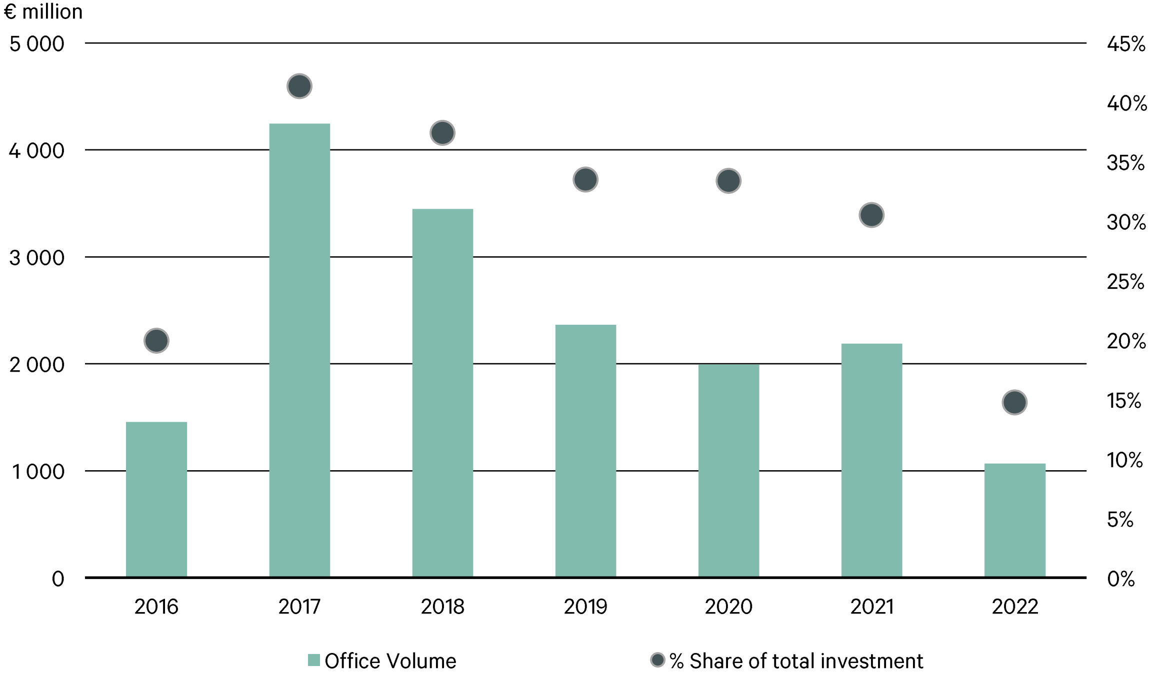
Office real estate investment volume decreased by 51% year-over-year and reached €1.07 billion in 2022. Last quarter of the year saw -64% year-over-year decline with €270 million of transactions taking place before the end of the year. Helsinki Metropolitan Area was again in the spotlight for investment activity as 85% of total office investment, €907 million, was targeted in the capital city region.

International investors were active in deploying capital to office investment during 2022, and 59% of the total office investment came from foreign capital. Increased interest rates and financing costs led investors being more selective in allocating new capital under the uncertain market conditions.

Largest office transactions in 2022 were NREP's purchase of the landmark office property Eteläesplanadi 2 from Allianz in Helsinki CBD in December, Swiss Life's acquisition of the Danske Bank HQ from Fennia in Pasila in September and Genesta's sale of the prime CBD office asset Fab 9 to KanAm in April. CBRE acted as the advisor on the sell-side in all three of these transactions.

A growing emphasis is being placed on environmentally certified assets as investors place greater importance on ESG and sustainability factors. Ambitious sustainability targets are being set by investors, leading to higher standards for green credentials in both existing portfolios and new investments.

Figure 7. Office investment volumes and share of total investment, %.



Source: CBRE Research.

Flight to quality prevails in office investments

Tilt towards higher quality and ESG

The office market is seeing a flight to quality trend, and the gap between grade A and secondary office properties and locations was evident in 2022. Both investors and occupiers are increasingly interested in modern office buildings with green credentials located in convenient transportation hubs and submarkets.

Prime office yields decompressed in 2022 amidst rising interest rates and higher financing costs. Prime office yield for Helsinki CBD moved out 85 basis points to 3.85% and prime yield for offices outside CBD (Keilaniemi, Pasila and Vallila) increased 90 basis points to 4.50%. The prime yield for major provincial cities (Turku & Tampere) saw an increase of 75 basis points to 5.75% at the end of the year.

Outlook for offices in 2023

Office investment market enters the year in uncertain market conditions. Inflation is expected to remain high in 2023, which could put pressure on rental income for office properties. Despite current uncertainty in the market, the long-term fundamentals of the Finnish office market remain strong, and the office investment is expected to pick up in the second half of 2023 as office investors actively look for opportunities

Figure 8. Prime office yields, %.

Source: CBRE Research.

Occupier

From 'wait-and-see' to active mode

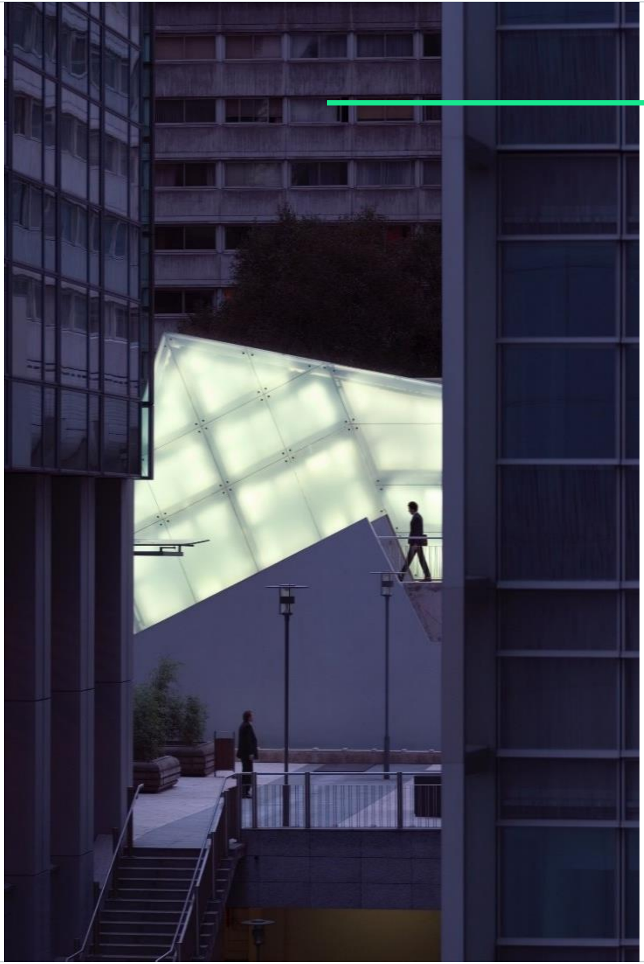
Office leasing market saw positive development in the first half of the year, and leasing activity for smaller to mid-sized office spaces (>1,000 sqm) in strong transport locations remained strong during 2022. Larger office occupiers reviewed their space needs more closely, and there was a clear trend of companies aiming for higher quality office assets in key submarkets.

Vacancy rate in the Helsinki Metropolitan Area was at 12.6%[1] in 2022, and there continues to be large differences between prime and secondary offices and locations across the key office submarkets. Leasing activity picked up in 2022 along with the improved market sentiment, especially in Helsinki CBD, SBD, Pasila, Ruoholahti and Keilaniemi submarkets. Lowest vacancy rates are in Pasila and Keilaniemi submarkets, where vacancies are only 4-6% at the end of the year. Prime rent in Helsinki CBD remained at €45/sqm/month in 2022.

Occupational demand led by IT & technology companies

The demand for office space was driven by IT and technology firms, management consulting companies, and other professional services such as law and finance occupiers. Companies were eager to reconnect with their employees and foster a sense of belonging and community within their workforce. Occupiers were less concerned with the cost of office space, and more focused on attracting and retaining talent. Health and well-being remained at the core for office occupiers after the pandemic.

[1] Helsinki Research Forum



Flight to quality and sustainability the key office trends in 2023

€45

/sqm/month
Prime rent in Helsinki CBD

12.6%

Vacancy rate in Helsinki Metropolitan Area[1]
(12.6% in 2021)

05

Retail

Retail sales recovered to pre-pandemic levels in 2022 as retail activity balanced out from the pandemic shock and consumers remained active in retail locations despite worsening consumer confidence and cost crunch from inflation.

Key Takeaways - Retail

01

STRONG RETAIL INVESTMENT LED BY LARGE-SCALE TRANSACTIONS

Retail volumes more than doubled to €1.19 billion (111% y-o-y) on the back of the Stockmann department store (€400 million) and Kaari (€207 million) transactions.

02

NORDIC INVESTORS REMAINED ACTIVE BUYERS OF RETAIL ASSETS

Nordic investors continued to deploy capital into retail real estate with all buyers being either Finnish or Nordic players.

03

FOOTFALLS AND SALES IN SHOPPING CENTRES RECOVERED IN 2022

Footfalls and sales in shopping centres saw a positive boost from the removal of the pandemic restrictions, and retails sales and overall activity surged close to pre-pandemic levels.

04

CONSUMER SENTIMENT AT RECORD LOWS, DIFFICULT YEAR AHEAD FOR RETAIL

Difficult year ahead for consumers as inflation is hurting household incomes and consumption is targeting more defensive and counter-cyclical sectors, such as groceries.

Retail

Large-scale retail transactions boosted activity

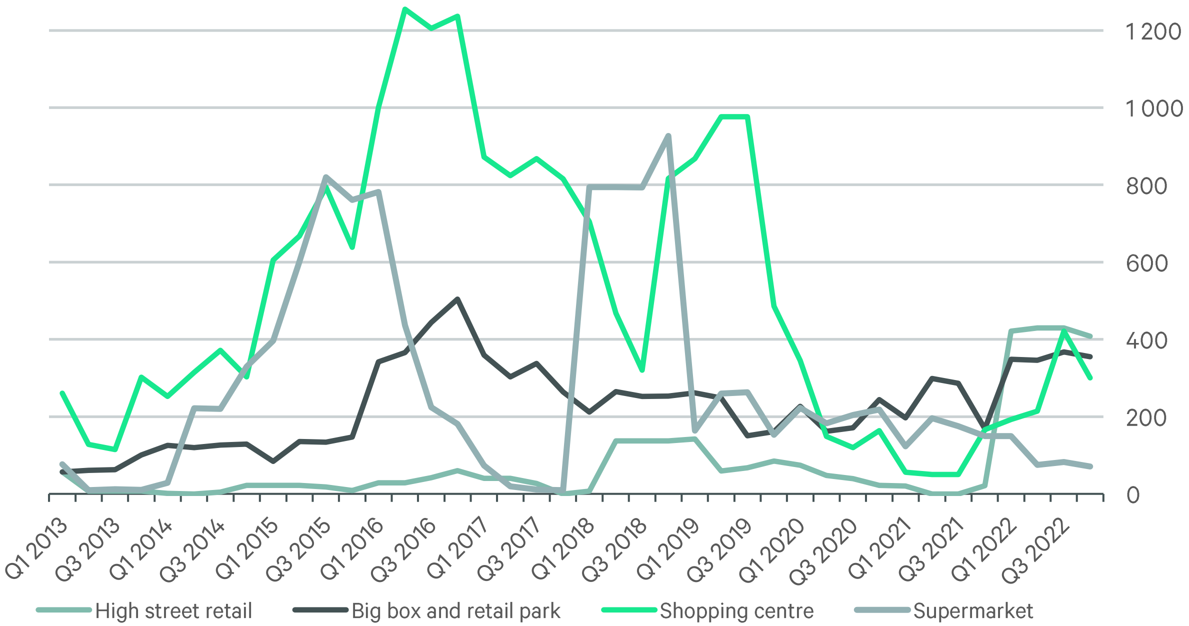
Retail sector saw a fair share of transaction activity in 2022 with investment volumes reaching €1.19 billion, up 112% from the previous year and strongest level of investment since 2018. Retail was the third largest sector in 2022 after residential and social infrastructure with 16% share of total volume.

Finnish retail investment market was boosted by large-scale transactions, such as the €400 million sale-and-leaseback of the Stockmann department store and the €207 million Kaari shopping centre transaction, where CBRE advised NIAM on the sale. In both transactions, the buyer was the Finnish pension fund KEVA. Other notable deals during 2022 were Nyfosa's two portfolio acquisitions, the €200 million retail portfolio from Partners Group in February and the 16-asset mixed-use portfolio transaction from M7 in April.

Nordic investors continued to deploy capital into retail real estate with all buyers being either Finnish or Nordic players. This investor base consists of fund managers, institutional investors and Nordic specialist investors who have a strategic appetite and a long history in operating in different sub-sectors in the Finnish market.

Investors remained more interested in resilient big box and grocery-anchored assets and portfolios with 36% of total retail investment landing in either big box and retail park or supermarket assets.

Figure 9. Moving 4-quarter volumes in retail sub-sectors (€ million) .



Source: CBRE Research.

Retail

Retail yields decompress on the back of rising rates

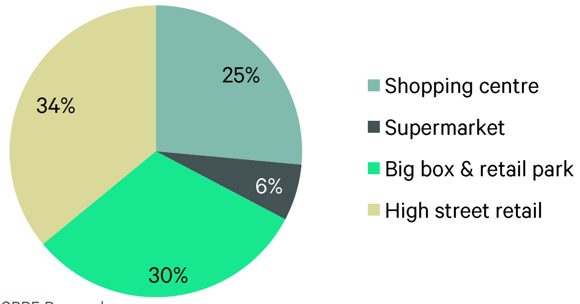
Higher financing costs and rising interest rates pushed prime yields higher during 2022, and there was decompression across different retail sectors. Prime supermarket and shopping centre yields moved out by 25 basis points to 5.00% and 5.50% during 2022, while big box retail prime yield decompressed 75 basis points to 6.25%. High street prime yield saw a decompression of 55 basis points during 2022.

Rebound in shopping centre sales and footfalls

Shopping centres witnessed a positive recovery in sales and footfalls during 2022, and in many retail locations the performance reached or even surpassed the pre-pandemic levels. Restaurants and cafes saw a good share of activity when activity returned to normal after two years of pandemic restrictions. Afterwork and Christmas parties, company events and other normal end of the year activities were back on the agenda and sales performance saw positive momentum across different tenant categories despite declines in consumer confidence.

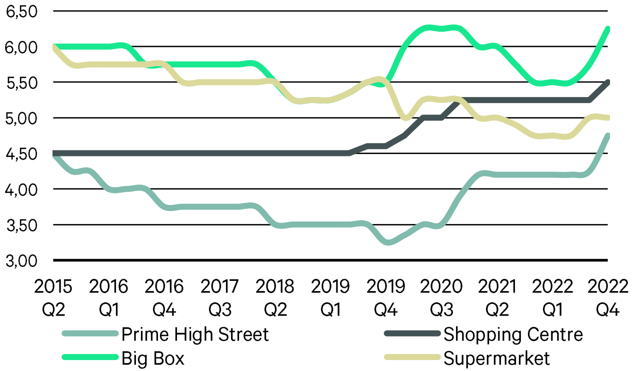
Second-hand fashion is seeing strong growth across different locations in both brick-and-mortar and shopping centres, and companies, like UFF, Relove and similar second-hand retailers have been active in opening new locations. Fashion retailers are making their comeback after the pandemic and budget retailers, such as Normal, are aiming for more growth in Finland.

Figure 10. Retail sub-sector shares in 2022



Source: CBRE Research.

Figure 11. Retail sub-sector prime yields.



Source: CBRE Research.

Low-cost retailers' pandemic boost came to an end

Low-cost retailers enjoyed a booming market environment during the pandemic, but during 2022 the reopening of the economy, spiking inflation and worsening consumer confidence had an impact on this retail sub-sector. Various big box and cyclical consumer goods companies reported softer operating performance towards the end of the year and listed names, such as Tokmanni and Verkkokauppa.com reported profit warnings on cost inflation and softening purchasing activity.

Defensive asset types will lead retail in 2023

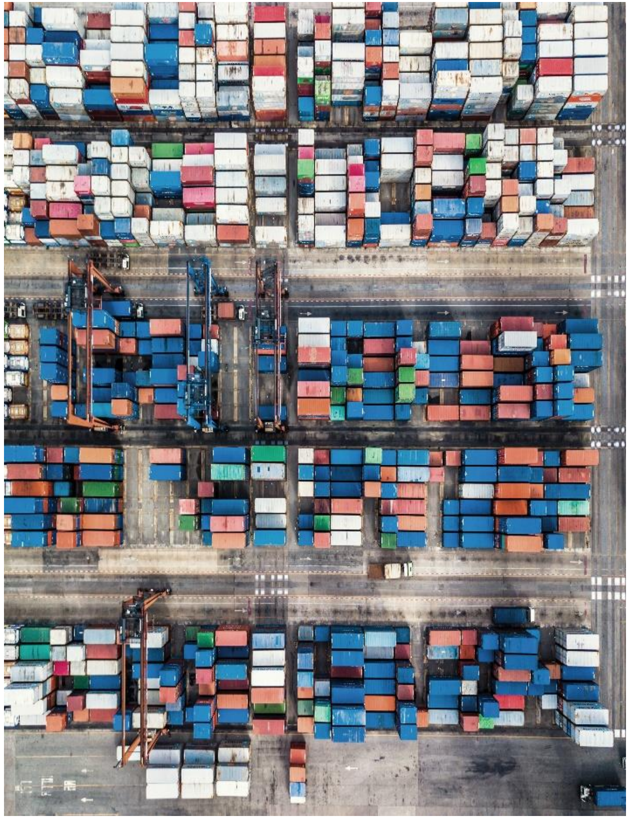
As consumer sentiment is at historical lows, the retail rebound is expected to fade in 2023 and consumption is targeting the defensive and counter-cyclical subsectors. Investors continue to prefer necessity-driven and defensive asset types, and big box and grocery-anchored retail is expected to be the most active segments in 2023.

06

Industrial & Logistics

Industrial and logistics sector will continue to see growth from e-commerce driven logistics and warehouse demand on both occupier and investor side.

Key Takeaways – Industrial & Logistics



01

INDUSTRIAL AND LOGISTICS INVESTMENT CONTINUED STRONG IN 2022

Investment volumes in industrial and logistics sector reached €907 million in 2022, the second highest level since 2017.

02

SHIFT IN THE PRICING ENVIRONMENT

Prime yield for I&L surged by 85 basis points to 4.75% during 2022 as financing costs and inflation rose sharply in 2022.

03

NEW DEVELOPMENT FOCUSED ON THE REGIONAL CITIES IN THE OUTSKIRTS OF HMA

Lack of zoning and low availability of industrial use land plots in Helsinki Metropolitan Area are driving new developments into areas outside the capital city region.

04

LONG-TERM VALUE DRIVERS REMAIN E-COMMERCE AND INCREASE IN PARCEL DELIVERIES

Both investors and occupiers remain active in industrial and logistics market, and growth in e-commerce continues to be the main driving force for the sector.

Industrial and logistics sector remained strong

Active year for industrial and logistics

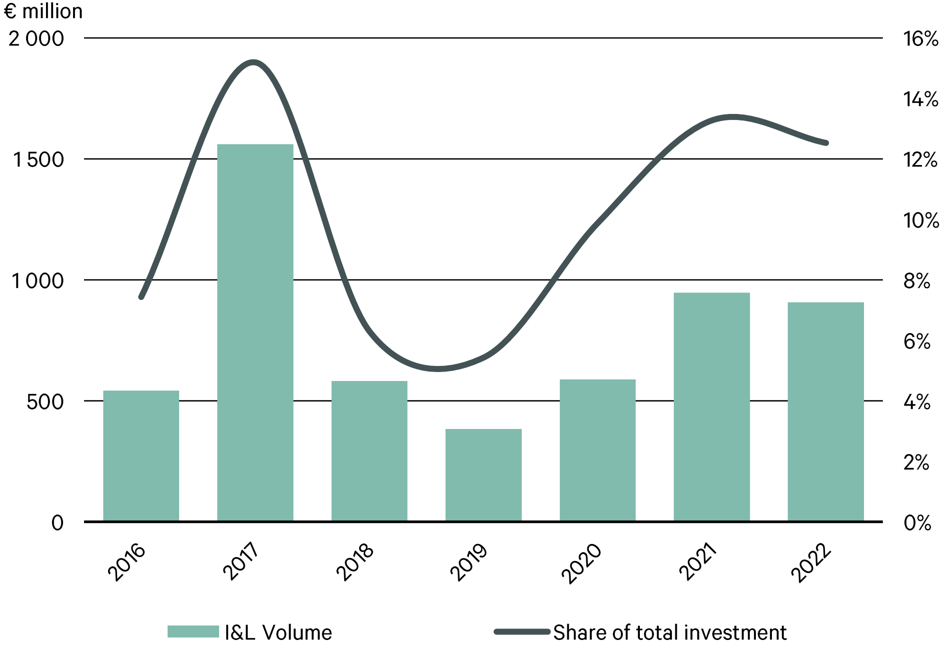
Industrial and logistics sector saw another strong year as investment volume reached €907 million in 2022. Foreign investors were actively investing capital to Finnish market as 79% of the capital came from international investors. Most notable transactions in 2022 were the Partners Group's acquisition of the nationwide last-mile logistics portfolio from Mandatum in July and Mileway's purchase of 11 logistics and light industrial properties in the Helsinki Metropolitan Area from Akiva in June. Prime yield for logistics surged by 85 basis points to 4.75% during 2022 as financing costs and inflation rise sharply in year 2022.

Intense competition for the right type of investable products

The Finnish market for industrial and logistics properties is facing a shortage of investable products, which is limiting investment volumes. This has led to intense competition among investors for properties that meet specific criteria, such as modern logistics properties with reputable tenants in prime locations. These types of properties are particularly attractive to investors and the demand is diversified among multiple sub-sectors, such as cold storage and last-mile assets. Demand for prime assets is expected to remain strong in 2023.

Despite the low supply of investable products which may impede growth, we anticipate 2023 to be another active year for the industrial and logistics market in Finland as pricing in the market finds a level of equilibrium.

Figure 12. I&L investment volumes and share of total investment.



Source: CBRE Research.

4.75%

Prime I&L Yield (Q4 2022)

79%

Cross-border share of total I&L investment in 2022

Occupier activity remain high in prime locations

Occupiers actively looking for available spaces

Fundamentals of growth remain in the industrial and logistics market. The increased use of online shopping and the rise in parcel shipments drives demand for logistics properties. Occupier demand continues on a high note, and lack of modern warehouse and logistics space is evident in the capital city region. The scarcity of modern stock and lack of speculative construction has kept the vacancy rate below 4% in prime submarkets and for modern higher quality stock ultra-low, at 1.c%. Strong occupational demand drives rental growth expectations in 2023.

There is a high demand for modern industrial and logistics properties across various industries and sub-sectors in prime locations. This is driven by e-commerce and retail companies looking for suitable properties to expand their operations as online orders continue to grow, and package handling requires more space. Additionally, industrial and manufacturing companies have built up inventories to mitigate the impact of supply and material shortages. Companies from various industries are seeking more warehouse and logistics space to meet their needs, and in some cases, settling for older stock as new developments cannot keep up with the large demand.

New developments in 2023

Helsinki, Espoo and Vantaa are not actively zoning land for industrial and logistics use. This has led to the new development moving outside of the Helsinki Metropolitan Area and into other regional cities such as Sipoo, Nurmijärvi and Mäntsälä, which are actively working to zone more land plots for large logistics operations. Regional cities have seen an increase in their development pipeline in recent year and are projected to have a higher growth in stock as compared to the HMA in the future. However, high borrowing and constructions costs and increased uncertainty in the market may cause delays in projects.

The amount of new I&L completions in HMA is expected to be 80,000 sqm in 2023, below the long-term average. Notable new completions for 2023 are the Eaton's UPS and energy storage manufacturing plant (14,000 sqm) in Vantaa and Logicenters' warehouse development (22,000 sqm) in Nurmijärvi.

Figure 13. Share of e-commerce in the Nordic countries.

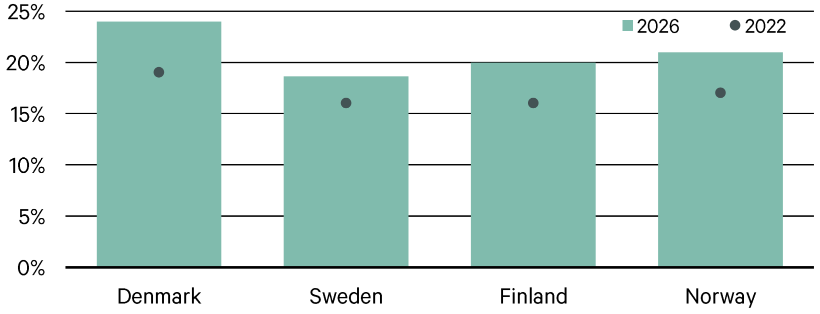
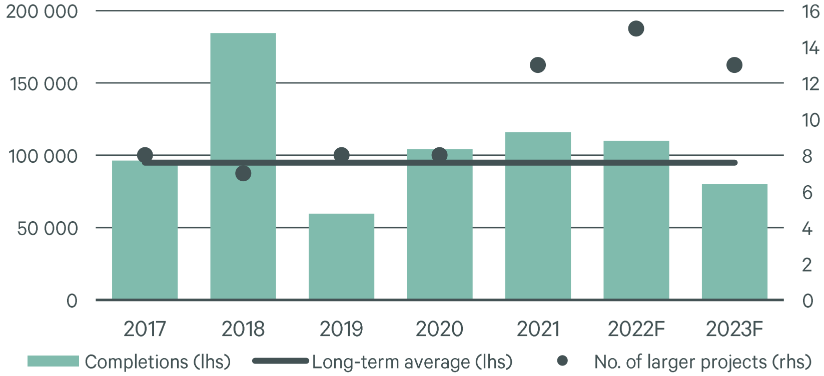


Figure 14. Construction activity in the Helsinki Metropolitan Area.



Source: Euromonitor, Statistics Finland, CBRE Research.

07

Residential

Finnish residential market remains one of the most transparent and least regulated markets in Europe, and the long-term fundamentals remain in place for more growth in the sector despite short-term uncertainty and price discovery.

Key Takeaways – Residential

01

RESIDENTIAL REMAINS THE LARGEST SECTOR IN 2022

Strong investment demand and several larger portfolio deals accelerated residential to third highest investment levels in history as investment volumes reached €2.1 billion in 2022.

02

RECORD LEVEL OF CROSS-BORDER CAPITAL IN THE FINNISH RESIDENTIAL MARKET

The demand for institutional grade residential investments is high in the Finnish market and 2022 recorded the highest volume of foreign capital entering the Finnish residential market.

03

YIELD DECOMPRESSION AMIDST MARKET UNCERTAINTY AND RISING INTEREST RATES

Increases in interest rates and financing costs led to decompression in prime yields in the Finnish market with prime residential yield moving out by 70 basis points to 3.6%.

04

CONSTRUCTION ACTIVITY REACHED ITS PEAK LEVEL IN 2022

High inflation and rising interest rates are expected to limit construction activity in 2023, and construction starts are expected to decrease to the historical average of 36,000 dwellings p.a.

Record level of cross-border capital entered the Finnish market in 2022

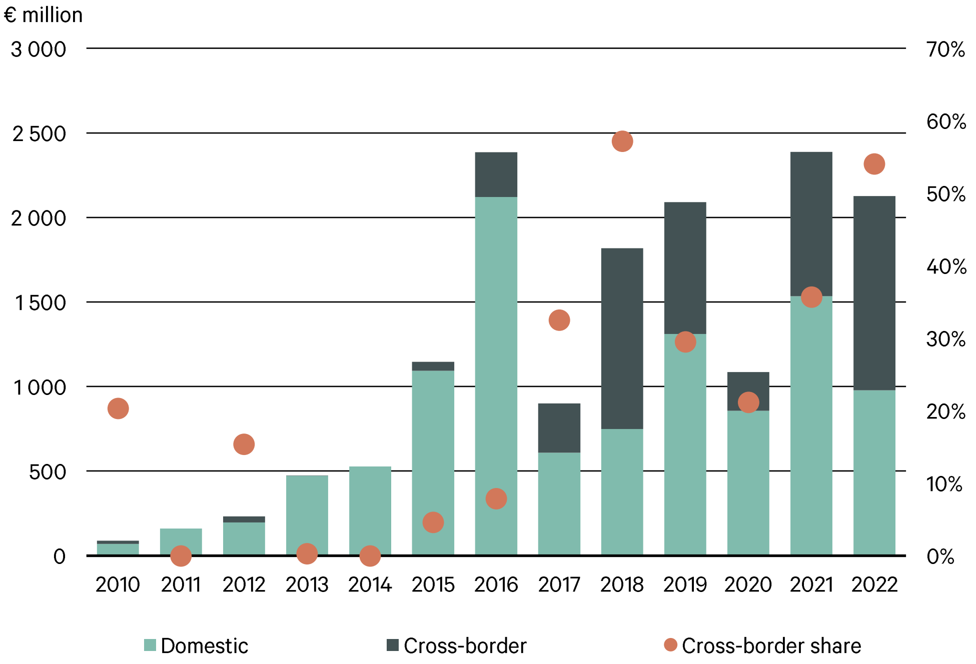
Residential the largest sector in 2022

Residential investment continued a high note in 2022, and investment volumes reached €2.1 billion. 70% of the transaction volume consisted of large-scale portfolio deals that closed above the €50 million threshold. Cross-border investment recorded an all time high with a transaction volume of €1.2 billion and 54% of total residential investment coming from international investors. Orange Capital Partners and GIC as well as Heimstaden were some of the most active buyers in 2022.

Largest residential transactions in 2022 were OCP's acquisition of a nationwide residential portfolio of 2,200 apartments from Starwood and Avara, OCP and GIC's purchase of the 1,900-apartment portfolio from Morgan Stanley and Heimstaden's acquisition of a residential portfolio with 1,900 apartments from Sato.

Despite the higher uncertainty over cost of capital and inflation, there are active deals in the pipeline in the Finnish residential sector market in 2023, and it is expected that investment activity will trend higher in the second half of 2023 as the pricing environment balances out from early 2023. The long-term fundamentals of the Finnish residential market remain strong, and the sector is expected to continue to be favoured by both domestic and cross-border investors looking to deploy more capital into rental apartments.

Figure 15. Residential investment volume and cross-border share.



Source: CBRE Research.

3.60%

Prime Yield (Q4 2022)

29%

Residential share from total investment in 2022

Rental market and construction activity

Prime yield decompression

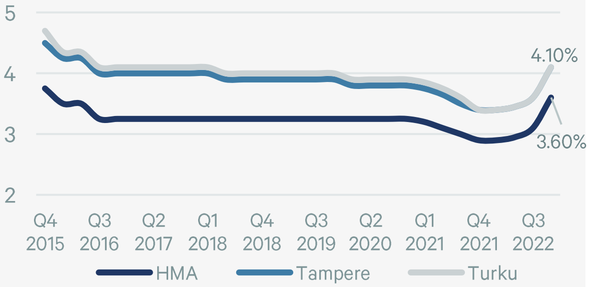
Increased cost of capital and higher interest rates had their impact for prime residential yields during 2022, and further decompression is expected in the current year. Prime yields have increased to 3.60% in Helsinki Metropolitan Area and 4.10% in Tampere and Turku.

Sales prices trended lower in 2022

In the last quarter, average sales prices decreased by 5.2% in the Helsinki Metropolitan Area, 4.7% in Turku, 3.2% in Tampere, and 4.1% nationwide from the previous year. Regional differences remained large in the Finnish market as the largest city regions continued to lead the growth. Prices have been more stable in larger dwellings compared to small apartments.

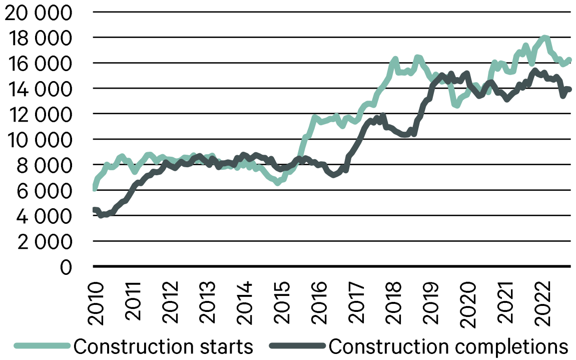
During the last quarter, average rents increased by 0.6% in the capital city region, 2.3% in Turku and 2.8% in Tampere (y-o-y). Rent increases remain smaller than inflation, which creates pressure for larger rent increases in the future. However, high availability of rental dwellings will moderate the rent increases in the near term. There are no additional government regulations planned for the Finnish residential market, which remains one of the most transparent and least regulated in Europe, and the Finnish market benefits from liberal rental legislations with no restrictions on rent levels, rent increases or rent periods.

Figure 16. Residential prime yields.



Source: CBRE Research.

Figure 17. Construction activity in the capital city region.



Source: CBRE Research, Statistics Finland.

Construction activity slows down in 2023

New apartment completions are still on a high level, and this may limit the rental growth expectations in the near term. High inflation and rising interest rates are expected to slow down construction activity in 2023, and construction starts are expected to decrease close to the historical average of 36,000 dwellings per annum. Cost inflation is expected to have reached its peak. Yet, the inflation is still at a high level and the prices have inflated in both materials and services. Increase in inflation has had an impact on both operating expenses and household disposable income.

Outlook for the 2023

Despite the challenges in the market in the short term, the long-term fundamentals of the Finnish residential market remain strong. Rising interest rates and continued high inflation remain a challenge for homeowners and investors. However, the growth drivers for the Finnish residential market remain intact – Urbanization, the growth of single households in cities, and the elevated household borrowing costs increase the popularity of renting an apartment. The share of rental households is already above 50% in the largest cities, Helsinki, Tampere & Turku. 2023 will present more opportunities for residential investors to acquire quality assets at lower prices. Deal activity is expected to pick up after the markets find equilibrium in pricing.

08

Social Infrastructure

Record year for social infrastructure investment in Finland with €1.89 billion and 26% of total investment volumes. Finnish market saw several larger deals, where municipalities sold their public and healthcare properties to investors before the new wellbeing services counties started their operations in 2023.

Key Takeaways – Social Infrastructure

01

RECORD YEAR FOR THE FINNISH SOCIAL INFRASTRUCTURE MARKET

Stellar year of investment activity for social infrastructure and investment volumes reached €1.89 billion, an increase of 107% from 2021.

02

SEVERAL LARGE-SCALE SOCIAL INFRASTRUCTURE DEALS IN 2022

Finnish market saw several large-scale social infrastructure transactions, and larger municipalities were active sellers of over €1 billion worth of assets and portfolios.

03

PRIME YIELDS MOVED OUT ON THE BACK OF INCREASED FINANCING COSTS

The prime yields increased by 60 bps from 4.00% to 4.60% on the back of increased financing costs and higher market uncertainty.

04

LONG-TERM VALUE DRIVERS OF AGEING POPULATION AND PUBLIC OUTSOURCING UNCHANGED

Finnish population continues to age in a rapid pace, quicker than any other European country. This demographic trend aligned with the pressure for the public sector to outsource will support the growth of the social infrastructure sector in Finland.

Record year for Finnish social infrastructure investment

Social infrastructure the second largest sector in 2022

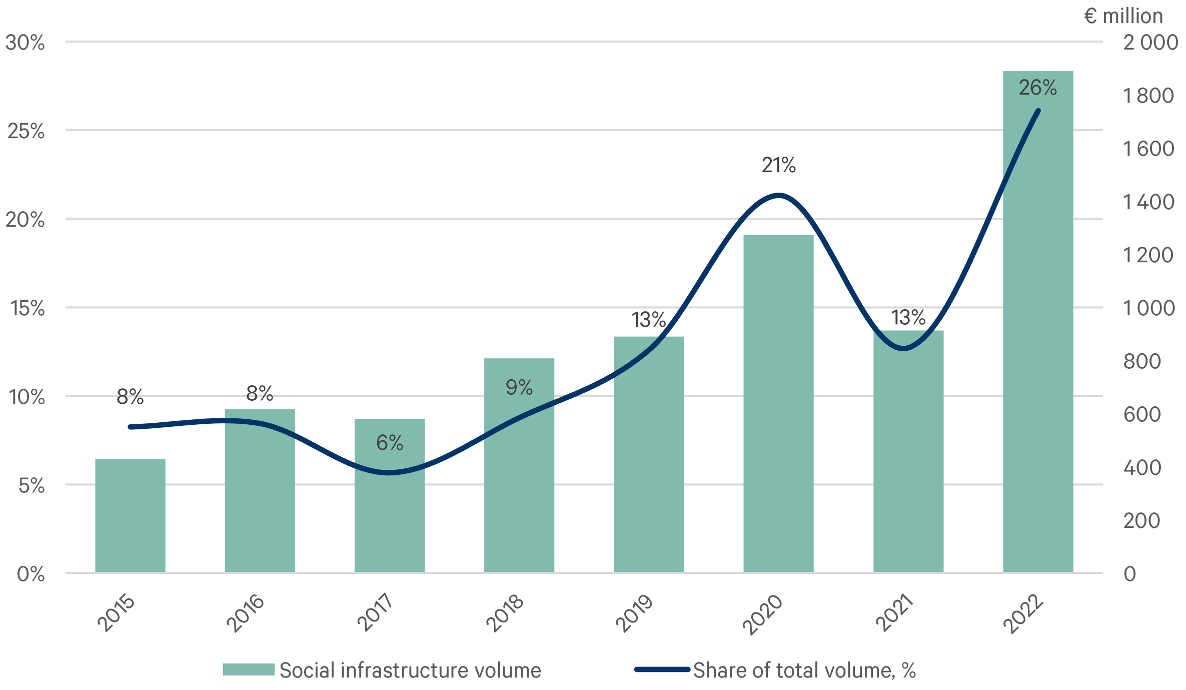
Social infrastructure reached a new record in 2022 as the investment volumes for the sector increased by 109% from the previous year and reached €1.89 billion in total. Social infrastructure was the second largest sector in Finland with 26% of total investment.

The record performance for the sector was aided by several large-scale social infrastructure transactions where municipalities and cities sold their social and healthcare portfolios to investors. Larger cities, such as Espoo, Tampere and Oulu were some of the cities that divested their social and healthcare assets and portfolios to investors during 2022, and overall municipalities were on the sell-side for over €1 billion worth of assets.

LähiTapiola and eQ were the largest net buyers and social infrastructure investors during 2022. LähiTapiola deployed ca. €500 million into social and healthcare properties and purchased a hospital property from the City of Espoo for €300 million early in the year as well as the social and healthcare centre from the City of Kirkkonummi for €64 million in October. eQ's open-ended Community Properties fund was again active in the Finnish market with more than €300 million net purchases, including the €166 million City of Oulu healthcare portfolio acquisition in June.

The Finnish social infrastructure sector continued to be dominated by sector specialists, who have gained a strong position in recent years, and investors, such as Hemsö, Kinland and Belgian REITs, Cofinimmo and Aedifica were again active in 2022.

Figure 18. Social infrastructure investment volume and share of total volume, %.



Source: CBRE Research.

More restructuring ahead for the social infrastructure

New market entries in 2022

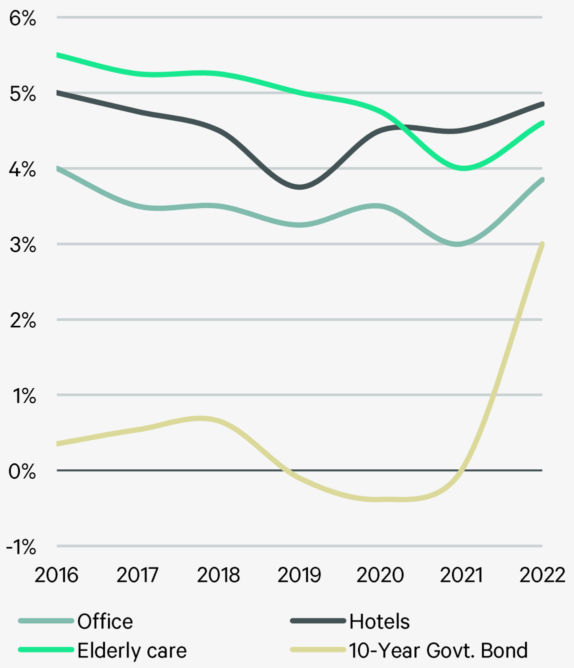
There were two larger market entries in the social infrastructure sector in 2022. Medical Properties Trust entered the Finnish market by purchasing the nationwide Pohjola hospital portfolio in March, and Infranode made its entry by purchasing the social and healthcare portfolio from the City of Jyväskylä for €84 million in October.

The prime yield for social infrastructure has decompressed 60 basis points during 2022 on the back of higher uncertainty from rising interest rates and higher cost of capital, and the prime social infrastructure yield (elderly care) is standing at 4.60% at the end of the year.

Finland faces parliamentary elections in 2023

Finland's social and healthcare reform remains one of the driving forces in the sector, and the wellbeing services counties, which started their operations in January 2023, are facing challenging decisions on resource allocation and public to private outsourcing. The pressure to decrease costs and outsource real estate to the private sector will not ease in 2023 as Finland faces parliamentary elections in April, where social and healthcare issues will be one of the most important themes.

Figure 19. Prime yields in offices, elderly care and hotels.



Source: CBRE Research.

The need for public restructuring continues in 2023

The healthcare sector has seen serious labour shortages in recent years, and largest operators are actively looking for thousands of additional workers for their locations nationwide. Largest employers are aiming for over 1,000 new recruits in the near-term, and these companies are recruiting and attracting talent from both domestic and international markets.

Finnish population continues to age in a rapid pace, quicker than any other European country. This demographic trend aligned with the pressure for the public sector to outsource will support the growth of the social infrastructure sector in Finland.

Investors remain interested in the sector due to the demographic and structural megatrends that are driving the demand in many subsectors within this growing sector. Social infrastructure offers long-dated inflation-linked income profiles with strong public sector covenants, which remain viable despite the increased uncertainty.

09

Hotels

Transaction market continued to be quiet for hotels as owners chose to hold on to their properties amidst higher market uncertainty and increased financing costs. Operator demand has continued strong despite slower post-pandemic recovery in Finland.

Key Takeaways – Hotels

01

HOTEL INVESTMENT REMAINED QUIET IN 2022, BUT IS EXPECTED TO PICK UP IN 2023

Transaction market continued to be quiet for hotels as owners chose to hold on to their properties amidst higher market uncertainty and increased financing costs.

02

STRONG OPERATOR DEMAND, ESPECIALLY FROM INTERNATIONAL OPERATORS

Operator demand has continued strong despite slower post-pandemic recovery in Finland. International operators have also expressed interest in the more resilient Finnish regional market.

03

HOTEL CONSTRUCTION AND PIPELINE REMAINS STRONG DESPITE DELAYS

The pandemic supply shock, higher construction costs and energy prices have delayed projects in Finland, especially in Helsinki Metropolitan Area. Despite the uncertainty, seven new hotels opened in 2022 in the region and the pipeline is abundant for the following years.

04

SLOWER RECOVERY DUE TO REDUCED DEMAND FROM THE EAST

International travel resumed with lifting the restrictions in 2022. However, the major sources of visitors from Asia are limited due to closed routes over Russian territory. Hotels in the HMA have been reliant on foreign demand and are experiencing slower recovery, while regional hotels have already surpassed their 2019 performance.

Limited transaction activity for hotels in 2022

Another quiet transaction year for hotels

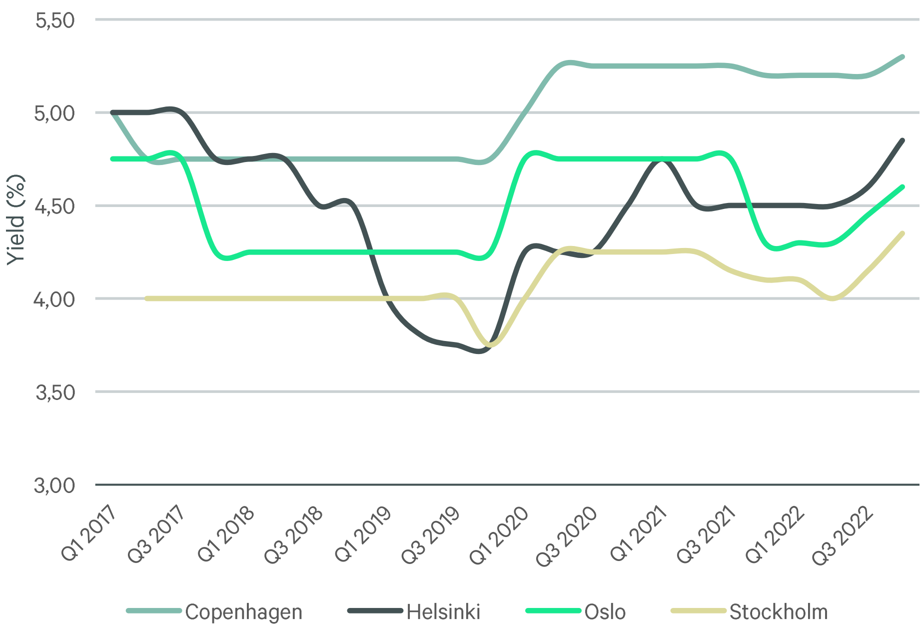
Transaction activity continued to be quiet in the hotel sector in 2022. The availability of investable products continued to be limited and the hotel owners were unwilling to bring hotels to the market. With increased development costs affecting selling price, new properties were no longer feasible for the hotel investors. One notable transaction was recorded in Helsinki in the third quarter of 2022, where a mixed use property with the serviced apartment hotel component was acquired. The property represents flight-to-quality asset characteristics which appear to be the most attractive to investors in the current market conditions.

Challenges in the hotel sector remain as hotel operators are faced with high inflation affecting the payroll and operational costs, extreme energy prices and adjusted minimum rents. With foreign tourists demand still in recovery, existing and newly opened properties face difficulties achieving projected revenues.

Investor sentiment impacted by higher uncertainty

Prime yields have moved out in the Nordic hotel markets along with the increased interest rates and higher financing costs. Nordic hotel yields decompressed by 20 to 35 basis points from the early-2022 lows, stand at 4.35% in Stockholm, 4.60% in Oslo, 4.85% in Helsinki and 5.30% in Copenhagen. There is some further decompression expected in 2023 as central banks continue their tightening to curb the high inflation rates.

Figure 20. Hotel prime yields in the Nordics.



Source: CBRE Research.

4.85%

Prime Hotel Yield (Q4 2022)

10%

Increase in hotel rooms in Helsinki by 2024.

Outlook slightly improved, but more resilience required for hotels

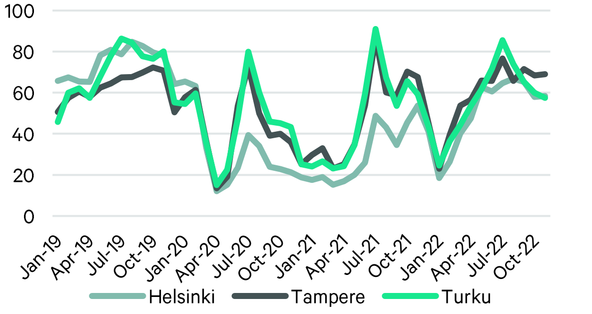
Moderate rebound in tourism and travel in 2022

The pandemic restrictions still affected travel and leisure sectors in early-2022. Shortly after the re-opening, new challenges in the shape of geopolitical uncertainty hit all business sectors – hospitality included. While domestic travel stayed active, it was not enough to help hotels recover to the pre-pandemic levels. The top seven source countries did not include any of the Asian countries in 2022, but some of the European countries took the lead – Sweden, Germany, France, as well as the United States and UK.

Strong domestic demand continued to keep the occupancy rates in Tampere and Turku high above Helsinki hotels' occupancy levels through most of the year. Tampere in particular has succeeded in attracting visitors by hosting world-class sports and music events.

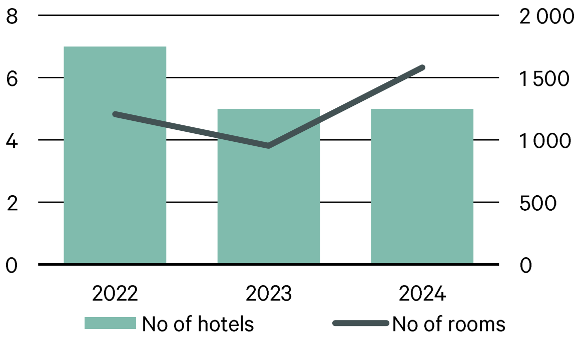
The hotel offering has been diversified with new hotel concepts entering the market – focusing on building communities (Unity hotel), supporting remote work and flexibility (Scandic Hub), experience-focused concepts (Hotel Ax). While the hotels and hospitality sector's outlook is brightening post-pandemic, resilience is still required from operators as the economic growth slows down in 2023.

Figure 21. Occupancy rates in Helsinki, Tampere and Turku, %.



Source: Statistics Finland, CBRE Research.

Figure 22. New supply and pipeline in the capital city region.



Source: CBRE Research.

Strong supply of new hotel development

As of the 2022-year end, the hotel market in Helsinki comprises 81 hotels and aparthotels with ca. 13,700 rooms. The room count has increased by c. 950 rooms in 2022, and the expected growth in hotel rooms is 10% by the year 2024. Majority of hotels in the capital city operate in the midscale segment, where international operators would still see a room to grow.

Helsinki hotel pipeline is looking strong with 8 new developments in Helsinki with ca. 1,400 rooms. Most of the new hotel supply is positioned towards aparthotels (over 50%) – a hotel class sitting between traditional hotels and residential living. The second biggest group luxury hotels represents c. 25% of the Helsinki pipeline. One of each Upscale, Midscale and Budget hotels are expected to open their doors in the next two years as well.

Several hotel projects were put on hold due to spiking construction costs and challenging financing conditions. It is also expected that some of the hotels will face rebranding in the following years.

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