

Real Estate Outlook

Edition 3, 2021



Undertows diverge by sector.

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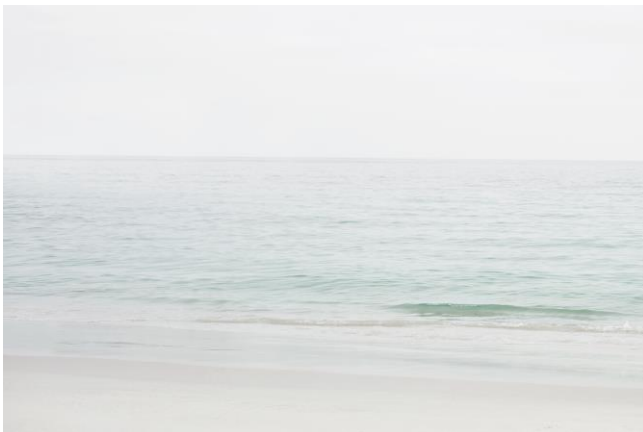


Our research team

Darnesha COLLIER
Kurt EDWARDS
Nicola FRANCESCHINI
Zachary GAUGE
Fergus HICKS

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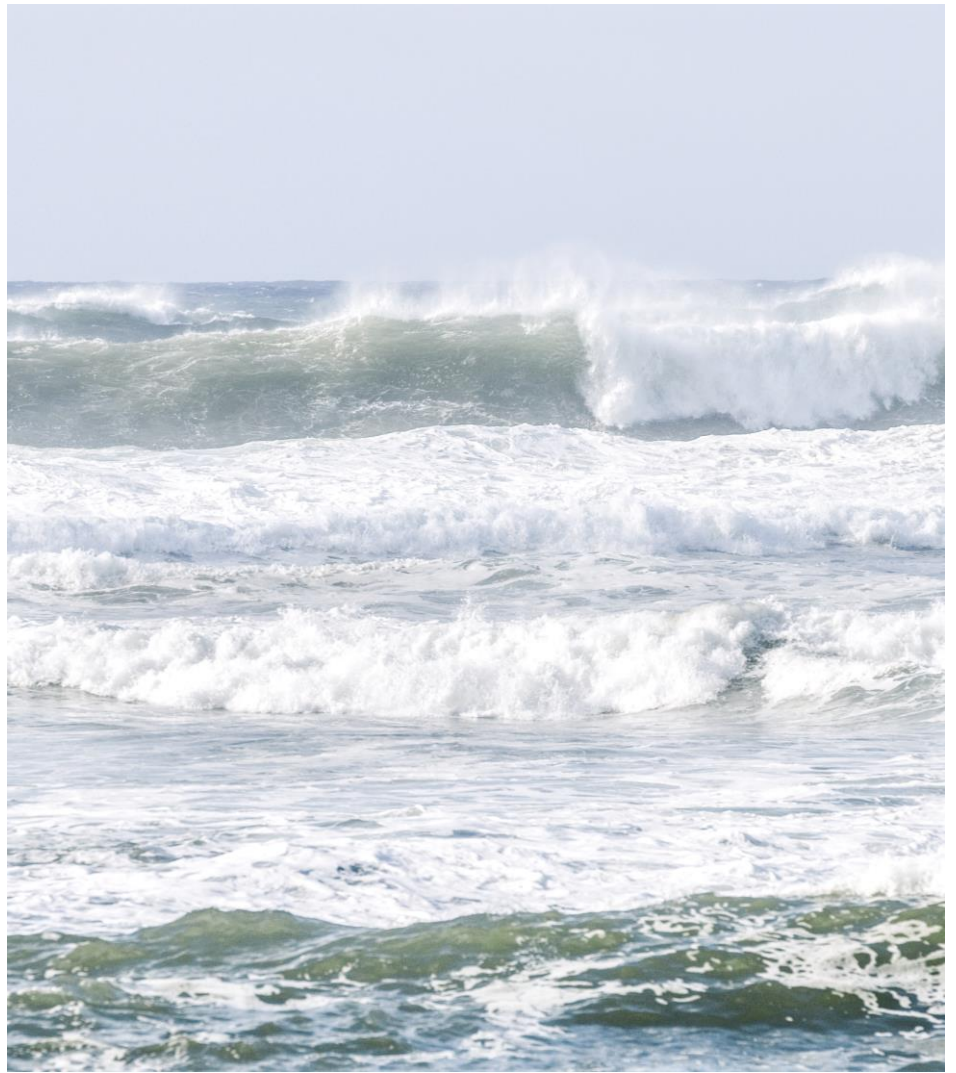
US outlook



Brice HOFFER
Amy HOLMES
Courtney LEE
Shaowei TOH



Fergus Hicks
Real Estate Strategist



Global overview

Finding direction in the waves of change.

Recovery in the economy and real estate investment markets gathered pace in the second quarter, though the new Delta variant of the virus poses a threat. Real estate showed strong returns in the first half of the year, driven by a stellar performance by the industrial sector. Investors should start to think about how to rebalance portfolios away from strong overweights to industrial.

Market overview and outlook

Rising tides from industrial in first half.

The economic bounce back gained traction in the second quarter of the year. Vaccines were rolled out to the wider population and virus case numbers fell, allowing economies to re-open. However, the newly emerged Delta variant of the virus has seen a renewed rise in cases and poses a threat to the recovery, particularly for northern hemisphere countries when they enter winter. The evidence to date is that virus infection remains possible for those that are vaccinated, but is much less likely and the effects a lot less severe, with much lower chances of hospitalization or fatalities.

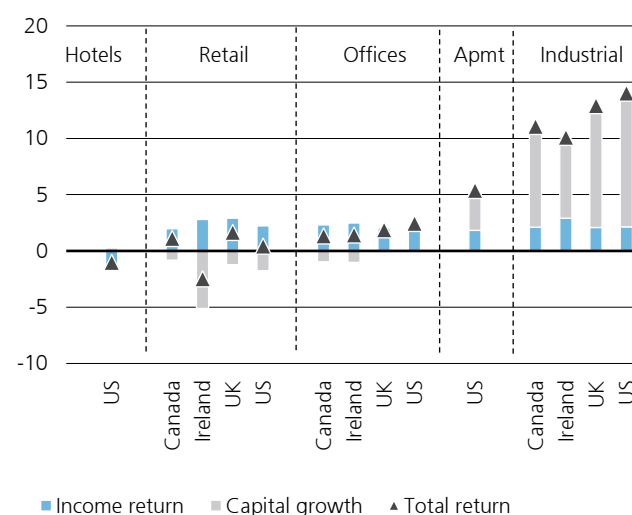
Inflation remains a key focus and has accelerated across most countries; to 5.4% in the US in June, which was significantly above the Fed's long-term target of 2%. Central banks continue to believe that price pressures will be transitory, allowing them to keep very easy monetary policy in place. However, central banks are increasingly acknowledging and flagging the risk that inflation might be more enduring, a scenario which investors should be prepared for. Indeed, if central banks did change their view and expected the pick-up in inflation to be more sustained it would imply that they should be taking steps to tighten policy to bring it back down and raising rates.

The inflationary pressures are being driven in part by turbulence and upheaval in the economy as it adjusts to its post-pandemic structure. For example, labor shortages are being reported in the hospitality and trucking sectors, with employers having to raise wages and offer sign-on bonuses to attract workers. Similarly, rising online fulfilment, of both consumer goods and meals, is creating new jobs in the warehouse and logistics sectors, while bricks and mortar retail suffers. It remains to be seen how labor markets will settle when job furlough schemes and enhanced benefits end.

Real estate markets saw a particularly strong first of the half of the year, driven by a stellar performance in the industrial sector. According to valuation indices from NCREIF and MSCI, industrial returns were in double-digits for the first half of the year, followed by residential at 5%, while retail and offices delivered small positive returns (see Figure 1). Overall, returns across sectors have been better than we expected. We attribute the strength of the market to the demonstrated recovery in the economy, the rollout of vaccines and their proven effectiveness giving a visible pathway out of the pandemic, and the large support from central banks and governments continuing to feed through to asset markets.

The total return performance figures were mirrored in pricing trends. The widespread appeal of industrial to investors drove demand and saw yields and cap rates fall for four consecutive quarters in a majority (55%) of the 69 industrial markets we monitor globally. The re-pricing in retail showed signs of easing, with yields rising in 15% of the markets we monitor, compared to 52% of them a year ago. The office market was pretty balanced, with falls occurring in slightly more markets than rises (17% versus 4%). We expect the pace of decline in industrial yields to gradually ease, while trends in retail will vary by country depending on the stage of pricing adjustment.

Figure 1: 1H21 total returns by sector and market (%)



Source: NCREIF; MSCI, August 2021. Past / expected performance is not an indication of future results.

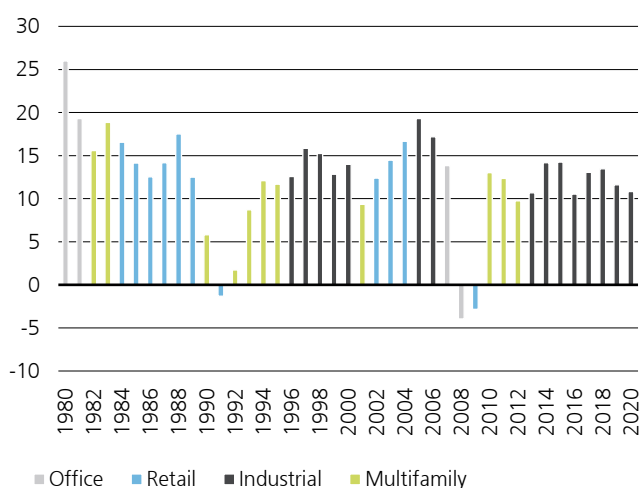
Real estate market activity mirrored the economy and, after a set-back in the first quarter due to new lockdowns, showed further recovery. According to data from Real Capital Analytics, after adjusting for seasonal effects global investment volumes rebounded strongly in 2Q, to within 3% of the high in 3Q19. Cross-border activity remains curtailed by ongoing travel restrictions, but has shown some recovery. Inter-regional deals accounted for 17% of global investment volumes prior to the pandemic in 4Q19, but slipped to 12% by 3Q20. In 2Q this year they had recovered to a 16% share. EMEA and Asia Pacific are the most driven by investors from outside the region, whose share of market activity is normally above 20%, compared to below 10% for the Americas.

Strategy viewpoint

Start thinking about rebalancing.

In a historical context, the run of industrial property is unprecedented. At the global level, our analysis of market valuation indices from MSCI and NCREIF show that in 2020, industrial was the strongest performing sector for the eighth year in a row, delivering a total return of 10.8% (Figure 2). This marks the longest run of outperformance by a single sector since data started in 1980, and is followed only by a six-year outperformance by retail in the mid-1980s. Historically, industrial yields have been above those of other sectors, providing a greater income return. Hence their compression over recent years has been a strong tailwind for capital values.

Figure 2: Total returns of global highest performing sector by year (%) (local currency, unleveraged)



Source: MSCI; NCREIF; UBS Asset Management, Real Estate & Private Markets (REPM), August 2021. Past performance is not an indication of future results.

Transaction activity in the industrial sector has also been very strong. According to data from Real Capital Analytics, industrial's share of global investment volumes has doubled from 11% in 2016 to 22% in 2020 and reached 24% in the second quarter of 2021. The rising share has been boosted by both rising transaction numbers and keener prices. By contrast, retail's share stood at 19% in 2016, but slipped to 12% in 2020 and was 11% in 2Q21. These are significant shifts that reflect how the market has evolved, with the pandemic accelerating the changes.

We think it is a near certainty that industrial will be the strongest performing sector again this year and most likely in 2022 as well. Industrial looks set to continue to ride the wave of strong rental growth driven by booming occupier demand, along with strong investor interest in the sector. However, we think that caution is needed to ensure that investors do not pay excessive prices in some parts of the market and that rental growth assumptions are achievable. Industrial valuations are also catching up with strong price growth.

At the current juncture we consider well-positioned real estate portfolios to be significantly overweight to industrial and logistics, underweight to offices, minimal weight to retail, overweight to multifamily and growing an allocation to the emerging and niche sectors like lab space and data centers. We think that this strategy will continue to perform strongly, until at least the end of 2021 and into 2022. However, the backdrop of sustained outperformance by industrial should also make investors pause for thought.

In describing its policy meeting discussions in June 2020, Fed Chair Jerome Powell said "We're not even thinking about thinking about raising rates." Turning this maxim on its head, we believe that real estate investors should now be "starting to think about thinking about rebalancing their portfolios." Indeed, moving into 2022 we think that investors should be ready to scale back any overweights to industrial and the options for doing so.

Reducing industrial exposure may seem like an unnerving prospect and begs the question of where to deploy capital instead? Retail may become viable again as market repricing occurs more widely in this sector. Indeed, some parts of the market already look to have bottomed out, such as retail warehouses in the UK, while others, such as continental Europe, likely remain some way off. Uncertainty over offices may begin to ease, allowing for greater exposure to this sector. Finally, the growing multifamily sector, along with the alternatives and niche sectors, also present good opportunities for investors to flesh out their portfolios. Even once the adjustment has been made, industrial will make up a larger share of investors' portfolios than it did pre-pandemic and before its record-breaking run started. The rise in occupier demand for logistics property and increase in physical stock will drag the share of industrial higher.

Real estate investment performance outlook

2020 actual and 2021-23 outlook are measured against the country-sector's long-term average total return, with the average +/- 100bps described as "in line with long-term average." The long-term average refers to the period 2002-20. The red underperformance quadrant refers to negative absolute total returns, either in 2020 actual or the 2021-23 outlook.

		LTA	Office	LTA	Retail	LTA	Industrial	LTA	Multifamily
North America	Canada	8.9		8.7		10.2		n/a	
	US	7.5		8.9		10.0		7.9	
Europe	France	7.7		9.3		9.3		n/a	
	Germany	4.7		5.3		7.7		n/a	
	Switzerland	5.6		6.2		n/a		6.3	
	UK	7.0		4.8		9.5		n/a	
Asia Pacific	Australia	10.0		8.9		11.0		n/a	
	Japan	5.2		5.4		6.0		5.6	

: Actual 2020

: Outlook 2021-23

: Underperformance (negative absolute returns)
 : Underperformance vs. long-term average
 : In line with long-term average
 : Outperformance vs. long-term average

Source: UBS Asset Management, Real Estate & Private Markets (REPM), August 2021. Note: Abbreviation LTA: long-term average. Expected / past performance is not a guarantee for future results.



Shaowei Toh
Head of Real Estate Research
& Strategy – Asia Pacific



APAC outlook

Big ripples, or **small waves?**



While the stuttering pandemic situation will weigh on near-term growth, the outlook for real estate in APAC is more sanguine. Demand for commercial real estate is expected to reverse into positive territory across most markets by the end of 2021. Investment activity in the logistics segment will be partly driven by the availability of quality stock. Investors could benefit from increased exposure to emerging segments.

Market overview and outlook

A matter of perspective.

We cannot stop the waves...

The stuttering pandemic situation will continue to weigh on growth in the near-term, especially as vaccination rates remain low in most of APAC. The latter partly explains the harsh and sharp responses towards virus outbreaks. Minor clusters of infections have led to entire economies being shut down. Unlike in many other western countries, governments have shown limited to zero tolerance towards COVID-19. To be fair, the headlines do not paint the entire picture. It is a matter of perspective. In developed APAC, the recent spike in new infections looks relatively manageable, at least on paper. As of 26 July 2021, there were only 5.7, 30.9, 30.6 and 27.0 new confirmed COVID-19 cases per million people¹ in Australia, Japan, South Korea and Singapore, respectively. To put it into context, these figures are significantly lower than the 564.2 and 157.1 in the UK and US, respectively.

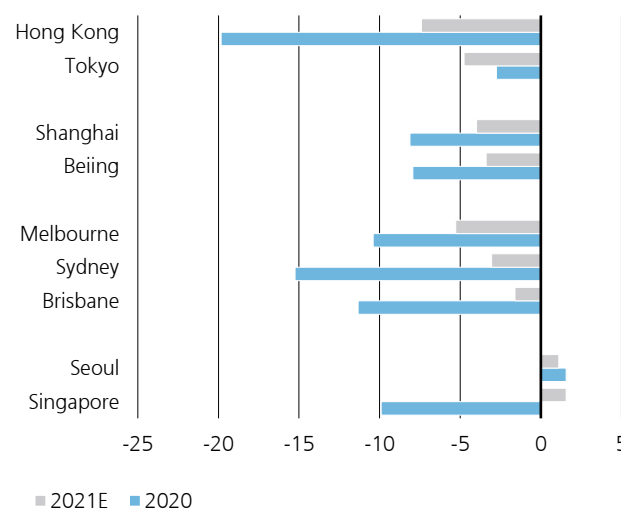
...but we can learn to surf

One saving grace is that most APAC governments have generally learned from lockdown experiences in 2020, evidenced by the muted ripple effects of more recent lockdowns. Furthermore, global demand has been improving over the past few quarters and that bodes well for the APAC economy, which is predominantly trade driven. Supported by the economic behemoth in China, regional economic performance was largely ringfenced and we saw APAC's aggregate GDP fall by only 4.0% YoY in 2Q20, improving to 9.4% YoY growth as at 2Q21.

Most APAC office markets continued to see weak performance in 2Q21. Despite that, demand for office space is expected to reverse into positive territory across most markets by the end of 2021. A year of turmoil has led to some increase in secondary and shadow office space, and office tenants are now more cost conscious. These will still be key drags on overall rent performance (see Figure 3). The markets where we saw the biggest rent corrections are markets in which prime rents have had a huge run-up over the past few years, such as Sydney. With limited supply expected in 2021 and 2022, the Tokyo office market will have the breathing space to cope with the emerging secondary vacancy later this year.

New-economy occupiers, such as those in the technology and media sectors, will continue to satisfy their deep appetite for office space in China and Singapore. Across APAC, high quality office assets have maintained tight vacancy rates and have proved to be more resilient. Looking forward, aging office buildings with less sought-after locations may suffer more in the medium-term, especially as occupiers put an added focus on the wellness of their employees.

Figure 3: Prime office rent growth (%)



Source: PMA; UBS Asset Management, Real Estate & Private Markets (REPM), June 2021

We think the glass is half full in the much-maligned retail sector. The pandemic has separated the wheat from the chaff in the retail space. There is still significant headroom for e-commerce penetration in APAC, which is not supportive of retail. However, the prospects for retailing lie in the two extreme ends of the spectrum, namely essential retail and prime retail. Every other retail format in the middle of the spectrum has and will be disrupted by the growth in online share of spending. Disclosure by public REITs across the region tells us that non-discretionary retail performed relatively well before and during the pandemic. This will still be the case after the pandemic.

On the other end of the spectrum, the outlook for prime retail is likely to improve once borders are re-opened. The downside risk is the uncertainty around that timeframe. However, astute investors can start to identify assets which have seen significant re-pricing and embark on value-adding strategies to adapt to the evolving retail formats and habits.

¹ Source: Our World in Data (7-day rolling average), as at 26 July 2021. (<https://ourworldindata.org/covid-cases>)

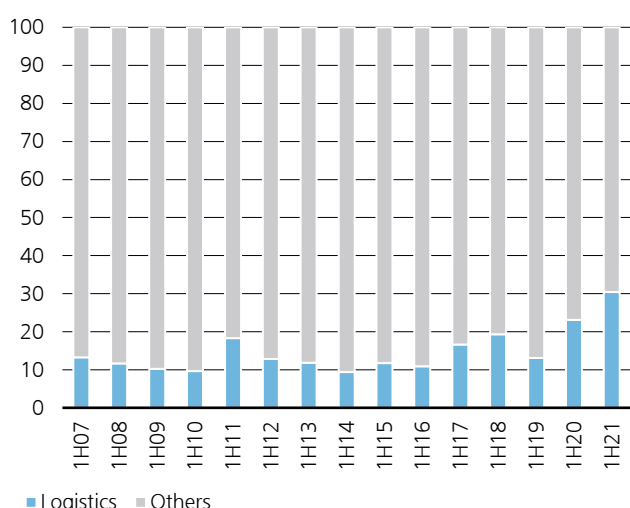
Strategy viewpoint

Riding the logistics wave.

According to preliminary data from Real Capital Analytics, total commercial real estate transaction volumes in APAC amounted to almost USD 66.7 billion in the first half of 2021, up by around 14.9% YoY from the same period last year. Total logistics property transaction volumes were up by a solid 51.4% YoY in 1H21, building on a strong 26.4% YoY growth in 1H20. As cyclical demand for the office and retail sectors toned down, logistics made up more than 30.0% of total investment activity in 1H21, up from the 23.1% we saw in 1H20 (see Figure 4).

As much as margins are low in the e-commerce space, logistics rent growth is still possible, albeit marginal. Lastly, we are seeing a cut-back in the supply of industrial land across APAC, and that has really pushed up the rents and capital values of logistics assets, especially the well-located ones. Japan, South Korea, China, and Australia are the few markets that will see better availability of modern logistics assets. Investment activity will likely be centered around these markets in the next few years.

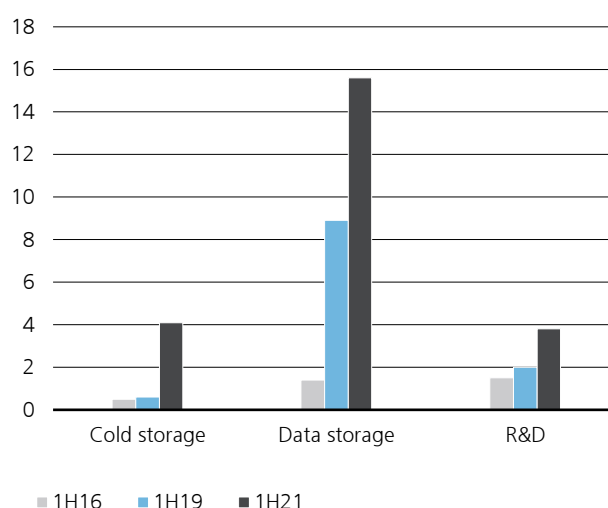
Figure 4: APAC transaction volumes (% by proportion)



Source: RCA, as of 29 July 2021

The surge in warehousing needs is underpinned by a few factors. First, countries and companies are increasingly safeguarding the integrity of their supply chains by engaging in near-shoring and on-shoring. This has led to greater demand for storage space domestically and regionally. Second, the exponential growth in e-commerce and the drive for efficiency have resulted in end-users struggling to keep pace with the parallel rise in warehousing requirements. Third, warehousing costs typically make up less than a third of total logistics costs for operators, with transportation costs driving another 50%. This means that it is cost-effective for end-users to pay more for higher quality and better located logistics space, and achieve costs saving on transportation.

Figure 5: Share of total logistics transaction volumes (%)



Source: RCA, as of 29 July 2021

The low cost of capital in the region should support pricing in the logistics sector over the next few years. Notably, we have also seen increased activity in the niche sub-segments of the logistics sector, due to the chase for returns as well as structural changes in occupier demand. The share of total logistics investment volumes of cold storage warehouses, data centers and R&D facilities have grown exponentially in recent years, although they still make up just a small proportion of overall transaction volumes (see Figure 5). The runway for growth is long, and investors could benefit from increased exposure to these emerging segments to ride on fundamental shifts in long-term trends.



Zachary Gauge
Head of Real Estate Research
& Strategy – Europe ex DACH



European outlook

Go with the flow, or swim against the tide?



Economic recovery is well underway in Europe, although the Delta variant dampens some of the promise from the first half of the year. Investor sentiment is more resilient than the underlying occupier markets, but is heavily targeted towards the “beds, sheds and meds” sectors. We continue to expect stronger returns away from the most crowded part of the market, or through development targeting markets and sectors with the strongest occupational dynamics.

Market overview and outlook

Delta variant muddies the water.

Economy

Much of the second quarter of 2021 was filled with positive economic news and upgrades to GDP forecasts. Vaccine rollouts accelerated, economies re-opened and a glut of pent-up savings and demand was released. As this demand has coincided with some global supply-chain issues, there has been sharp price inflation for some specific products and commodities. Based on Oxford Economics forecasts, Eurozone CPI inflation will peak at just under 3% this year. However, once the distorting effects of the pandemic subside it is expected to drop back to below 2% from mid-2022.

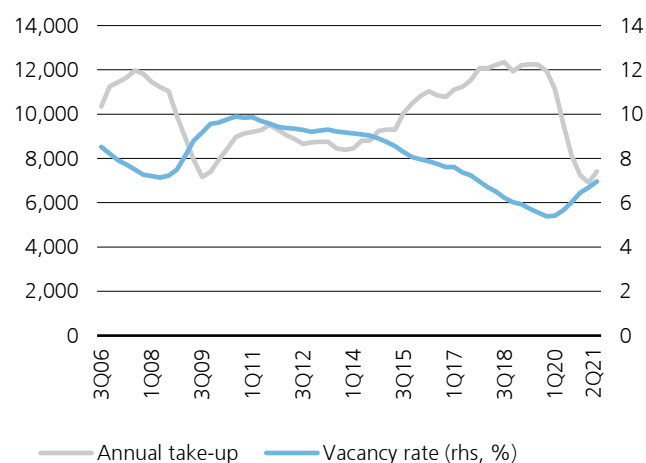
More concerning is the widespread prevalence of the highly transmissible Delta variant. This has already resulted in several European countries reinstating some restrictions. The vaccines appear to be effective at limiting serious illnesses from the variant, but with cases on the rise it will be a testing few months. If hospitalizations were to increase in the coming months, further major lockdowns cannot be ruled out and this would dent the positive momentum which developed in the first half of the year.

Occupier markets

European office markets continued in the same vein in 2Q21. Based on data from JLL, take-up only increased by a small margin and remains 35% below pre-pandemic levels (see Figure 6). Vacancy continued to edge up in 2Q, by 0.3pps, but is still low in a historical context.

Figure 6: European vacancy rate and take-up

(000 sqm, %)



Source: JLL, 2Q21

The lack of high-quality supply kept prime office rents stable in virtually every market. On the retail side, there was finally some positive news, with stores able to open across much of Europe. A few markets recorded prime rental declines, but this was far less widespread than in previous quarters. And whilst demand for logistics space remains very strong, prime rents have not taken off in the way that the pricing levels have implied. It suggests that despite all the strong fundamentals, logistics may not be a naturally high rental growth sector – particularly in markets where there is significant land availability.

Capital markets

Investment markets continue to demonstrate stronger characteristics than the underlying occupier markets. Data from CBRE shows that European investment volumes in 2Q21 reached EUR 69 billion, a 26% increase on 1Q21 and just 5% below the comparable pre-COVID-19 investment level. Nearly half of the investment volumes were accounted for by the much sought-after *beds and sheds* sectors. With a large weight of capital chasing a limited pool of assets, there has been sharp price inflation for both sectors. In addition, industrial transaction yields dropped below office CBD yields for the first time in history.

Despite ongoing questions around the future of the office, transaction volumes for the sector showed some recovery, coming in at EUR 22 billion, but remained 22% below the level in 2Q19. Within the sector, investor appetite is heavily skewed towards core assets with defensive income streams. Prime yields were flat in most markets, but further compression was recorded in Brussels, Paris, Berlin, Cologne, Stuttgart and Milan. However, outside of the very core space, the situation is more challenged. Quarterly valuation data is not available in most markets, but pricing of assets in more secondary locations are under pressure except those with a long lease in place to a low-risk tenant.

Retail investment volumes remain well below historical levels, but there was an increase of 35% QoQ in 2Q21. There are still challenges ahead but the reopening of retail assets should encourage further liquidity into the sector. And after generally moving out since the start of the pandemic, prime yields were mostly stable in 2Q21. Although COVID-19 related closures are hopefully behind us, the continental European retail market is still yet to face the full revaluation from the structural shift to e-commerce. We do not expect this to retrench too far from the levels hit during the pandemic.

Strategy viewpoint

Different strokes for offices and retail.

Keep the fundamental differences in mind

It only took e-commerce penetration to reach around 15% to start a sharp correction of global retail real estate values. With consensus assuming that most office-based companies will take a hybrid approach to home working, we can realistically expect average working from home (WFH) days to increase from 1 to 2.5 day per week. This equates to a potential fall in day-to-day occupancy of 1.5 days per week. This potential reduction in corporate demand for offices is double the level of e-commerce penetration that led to a sharp correction in retail values. *So shouldn't landlords of office space be worried?*

Not necessarily. Retail and office businesses are fundamentally different. Bricks-and-mortar retailers all share the same business model – to sell products from a shop. The office by contrast is a unit in which to do business, but those businesses vary considerably. What this means is that when retail suffered from a structural shift, it was a systematic risk that negatively affected all bricks-and-mortar occupiers. Whereas the industries of most office occupiers have not been negatively impacted by the pandemic. And rather than the structural shift to WFH having a negative impact on their cash flow, it can actually improve it if they reduce their occupation through more remote working.

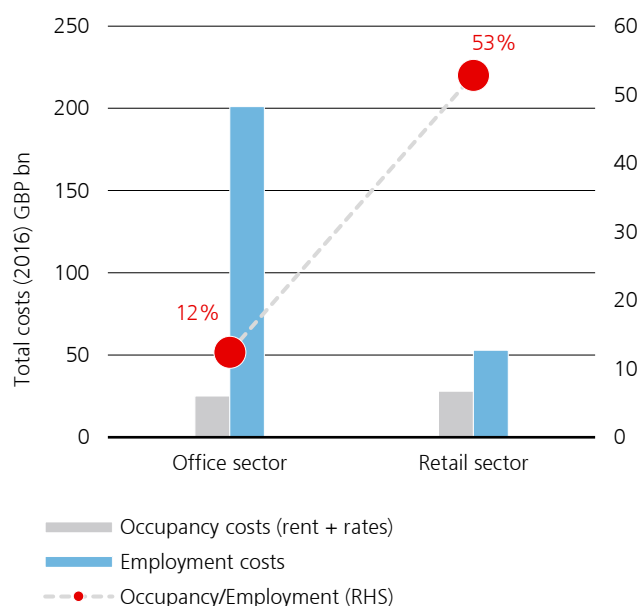
A further difference is the far higher relative real estate costs for retail, compared to offices (see Figure 7). Reduced retail occupancy has a greater impact on the bottom line than reduced office occupancy. If an office occupier needs to save costs, its first call is nearly always to reduce headcount, before space. With most office-based companies in a healthy position financially, we're not envisaging significant reductions in headcount leading to lower office requirements.

Instead, there will be reorganizing and consolidation, as real estate teams accommodate more staff into less space. This will be gradual and new demand will negate some of the challenges caused by a shift to flexible working. While COVID-19 will lead to longer-term shifts in occupation, this impact will be uneven.

Office-based companies are recruiting again, and the war for talent in many sectors is as fierce as before the pandemic. The space they occupy to support growth will need to be accretive to the value of the company and the experience of the employees. Buildings will need to accommodate changing usage, moving from functional workspaces to an interactive and collaborative environment. The most relevant locations

will facilitate a range of features that add value to the employee making the commute.

Figure 7: Occupancy costs for offices and retail in the UK (GBP, %)



Source: IPF PIA Property Data Report; 2017

Many office buildings will not meet these criteria. Repurposing well-located city-center space to meet future demand can protect values. But in weak, secondary markets, particularly with poor transport connections, the outlook is less positive. Deals in out-of-town locations which add little value to the workplace experience are generally going through at discounts to their pre-COVID-19 valuations. Furthermore, the more established locations with a wide range of amenities and transport connections are proving to be far more defensive.

One exception is life sciences, where there is vast investor demand. This space is often in out-of-town business parks and there is a key differentiator between traditional office space. The work done at a life sciences facility has to be within a highly controlled environment – traditional office work is much more transferable. And it is the more functional, workstation-led offices that are likely to suffer the most as we come out of the pandemic.



Kurt Edwards
Head of Real Estate Research
and Strategy – US



US outlook

Closer to **calm.**



US economic recovery is pushing through the lingering headwinds of virus variants and sluggish job growth. A year of pent-up demand is powering progress in necessity-driven asset classes. By autumn, real estate investors should gain insight from increasing comparable leases and sales.

Market overview and outlook

Rediscovering sea-legs.

The NCREIF-ODCE Fund Index showed income return offsetting capital depreciation in private commercial real estate resulting in a positive total return of 3.93% for the second quarter – the highest quarterly total return since 2015 – and 8.02% for the year ending 2Q21.

A year of pent-up demand is affecting multifamily and industrial the most (tailwinds are expected to outpace the headwinds). Office and retail continue to have hardships but more dynamic sub-segments of these property types such as life-science, medical office, and grocer/cloud-kitchen trends in retail, have upside surprise factors.

Fourth quarter 2020 showed a fairly normal surge in transaction activity. 2Q21 volume was in line with 2Q19. Increased transaction volume should give investors more clarity and confidence in values as 2021 progresses.

Interest rates remain low and support increasing transactions. Spreads available in private real estate remain near long-term averages. Borrowers have options as lenders become more competitive, especially for high-quality credit, long-term leases, multifamily and industrial properties.

Most sectors saw notable acceleration in total returns over the quarter. However, retail continued to post negative returns, albeit at a diminishing pace (see Figure 8). Industrial returns continue to exceed the other sectors. Office returns finally turned upward increasing over the previous quarter for the first time in more than two years. Apartment returns accelerated to the highest level since 2016, potentially heralding a rapid recovery. At the market level, we forecast a recovery growth pace for industrial and apartment returns but modest performance for office and retail during 2021.

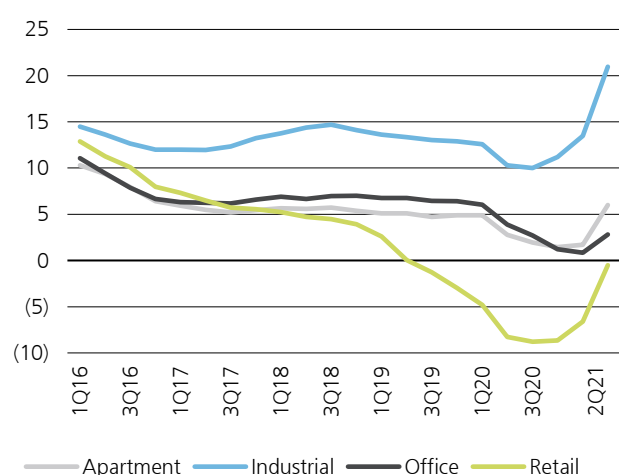
Apartments – Apartment fundamentals are beginning to stabilize and are likely to see occupancy and rent values recover fully during 3Q21. According to CBRE-EA average apartment rents increased by 3.5% QoQ in 2Q21; sufficient for a YoY growth rate of 0.4%. Vacancy declined by 60bps in the year ending 2Q21 to 4.0%, and is the lowest it's been since the end of 2019.

Industrial – Many consumers have become accustomed to the convenience of online shopping. Industrial remains the sector with the strongest fundamentals. Despite a nearly 2% increase in national inventory, according to CBRE-EA 2Q21 industrial availability was 6.4%, down by 40bps from 2Q20. YoY rent growth accelerated to 5.0% in the year ending 2Q21.

Office – Total office vacancy continues to rise rapidly, and reached 16.5% in 2Q21 (350bps over 2Q20) according to CBRE-EA. Development has not slowed, with over 45 million sqft of new supply delivered over the past year into a market with diminishing demand. Over the past year, downtown vacancy has risen to 15.8%, 440bps above one year ago; while suburban vacancy, at 16.8%, is 290bps above last year. Asking rent declines are expected to continue through mid-2022.

Retail – The full impact for traditional brick and mortar stores and restaurants remains to be seen. The most vulnerable appear to be businesses unable to adapt to online or app-based strategies. Neighborhood & Community Center availability is down by 20bps to 8.8% in the year ending 2Q21 according to CBRE-EA, but we expect rent growth to be moderately positive by year end 2021.

Figure 8: ODCE returns by sector (Four-quarter rolling returns, %)



Source: NCREIF as of June 2021. Data show unlevered NCREIF Property Index total returns filtered for only ODCE managers. Past performance is not an indication of future results.

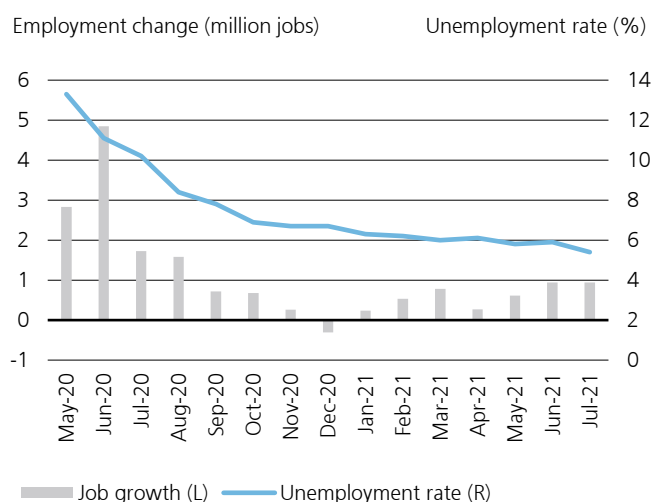
Strategy viewpoint

Strong sailing, expect headwinds.

The US economy began to recover during 1H21, bolstered by additional stimulus and legislation designed to seed expansion. Preliminary data indicates that 2Q21 GDP has exceeded the pre-pandemic level, with steady growth anticipated for 2H21. Variant virus strains and the below-expectation rate of adult vaccinations have led to confused messaging and sporadic reinstatement of masking requirements posing a risk to continued growth.

The 10-year US Treasury rate declined by 50bps from the start of 2Q21 to the writing of this piece (6 August 2021). The Federal Reserve continues to focus on payrolls and is putting little weight on the increase of COVID-19 Delta infections, given the increase in vaccinations leading to lower death rates. If payrolls continue to improve, the decision to reduce the Fed bond buying program is likely to come later this year.

Figure 9: Monthly job growth

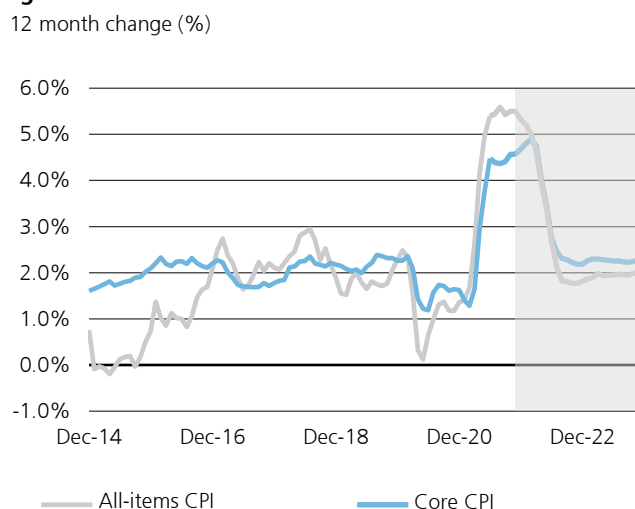


Source: Moody's Analytics, as of 6 August 2021

Although employment gains have been strong in recent months, the overall number of jobs is still below pre-pandemic levels. Along with push back on low wages, there remains a higher exposure risk associated with customer and food service jobs. The monthly unemployment rate declined to 5.4% in July, after holding steady near 6% for six months (see Figure 9). Average hourly earnings increased by a solid 0.4% MoM. While childcare concerns have kept many from seeking employment, the general return to in-person schooling this fall and the expiration of the federal USD 300 unemployment bonus, should drive increased employment.

Rebuilding confidence in the economy will be a long process given the recent uptick in COVID-19 Delta variant cases. The UBS Knowledge Network expects that the peak of this new COVID-19 wave could be seen by early September 2021.

Figure 10: Inflation forecast



Source: BLS; UBS, as of 3 August 2021. Shaded area indicates forecast.

UBS is forecasting inflation to remain at elevated levels, above 4.5% (12-month rolling) until early spring of 2022, but then slowing in the second half of the year (see Figure 10). Any surprise inflation that is more than transitory will affect capex heavy real estate sectors/sub-segments that do not have clear increased demand drivers (i.e., traditional office and malls).

Investor confidence remains higher in the industrial and apartments sectors, given the persistent, necessity-driven tenant demand. In retail, office and hotels, constrained transactions, and higher capex burdens make it difficult to assess whether current risk premiums compensate adequately for the risk. We expect industrial and apartments to continue to outperform retail and office in 2021.

For more information, please contact:

UBS Asset Management

Real Estate & Private Markets (REPM)
Research & Strategy

Fergus Hicks
+44-20-7901 6022
fergus.hicks@ubs.com



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