

# Real Estate to go

## Living in Europe

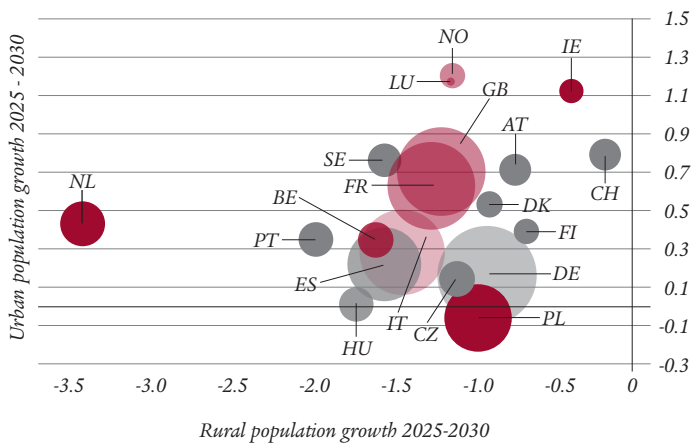
Issue 1 - October 2019

### All about the city

#### Growing urbanisation

Over the last decade most large European cities have recorded strong population growth. By contrast, rural areas, are losing residents – mainly young people. Due to the social and economic opportunities that large cities can offer, this trend is likely to continue in the medium term.

#### Population growth in urban and rural areas



The size of the circle illustrates the number of inhabitants.

Source: United Nations

#### Household growth is driving housing demand

It is household growth rather than population growth that is driving housing demand. In all major European cities, household growth will exceed population growth. Even in countries and cities where population is stagnating or declining, the number of households is likely to rise.

#### Population & household growth forecast by country 2018-2035



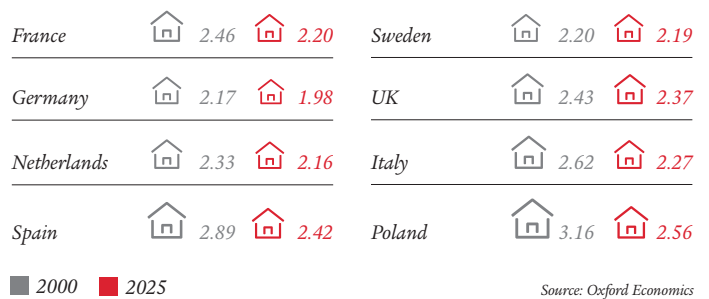
■ Household growth ■ Population growth

Source: Oxford Economics

#### Small becoming big

Household sizes are decreasing which is putting pressure on residential markets. The trend towards smaller households can be seen with varying intensity in all European countries. From 2007 to 2017 the average household size in Europe decreased from 2.41 to 2.26.

#### Average household size

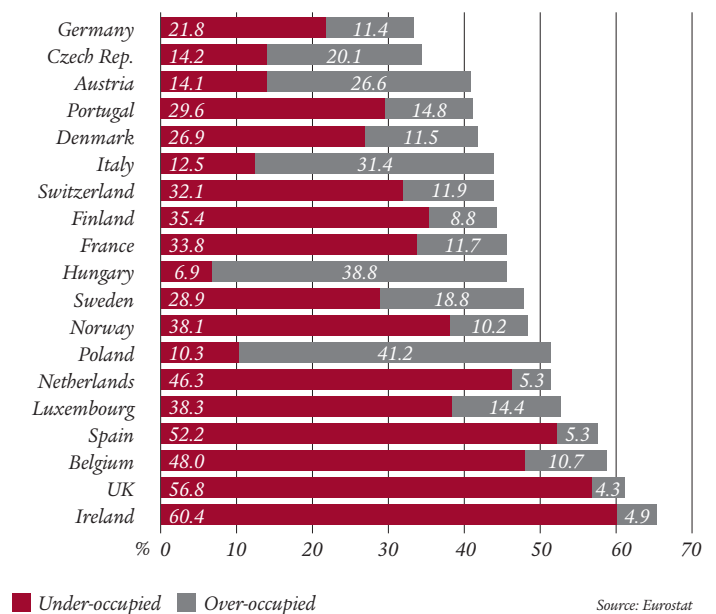


Source: Oxford Economics

#### Overcrowded versus under-occupied

Existing housing stock does not always align with need. In the Central Eastern European (CEE) countries, living space is often too small for the number of people in a household, resulting in overcrowding. In Western Europe and Scandinavia, there is more dwelling under-use as older individuals or couples remain in their homes once their children have left.

#### Share of population living in unsuitable housing



■ Under-occupied ■ Over-occupied

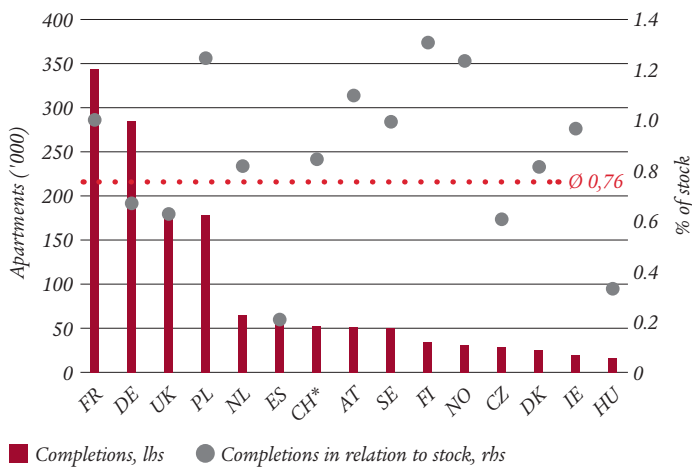
Source: Eurostat

# Not enough

## Supply far behind demand

Housing shortages, rising prices and low interest rates have led to increasing housing completions in many European countries. France has had the highest number of housing completions for the last couple of years, despite being less populated than countries like Germany and the UK. Nonetheless, completions have remained low relative to stock, especially in metropolitan areas where demand for new housing is highest.

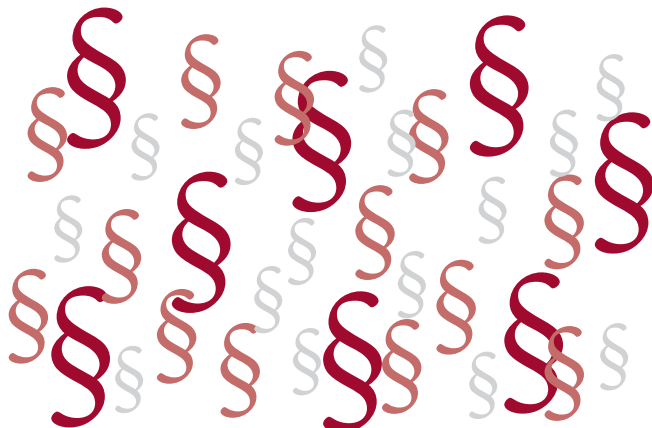
Completions in 2017



Source: Hypostat; \*Data for CH is from 2016

## Regulations increase construction costs

Rising construction costs are limiting the number of completions. The price of land, materials and skilled labour are all rising, but this does not paint the full picture. Another major factor driving up construction costs is the numerous building regulations. In recent years, new standards have been added, for example to achieve climate protection goals, to improve fire protection or to better insulate new dwellings against noise. Currently, there are around 3,300 standards with which building owners in Germany must comply.



## Productivity growth not building up

Rising construction activity has led to a shortage in skilled labour. One way to offset a reduced labour force is by increasing worker productivity. Yet construction productivity has evolved at a glacial pace. According to McKinsey, the German economy has become 1.32% more productive annually over the last two decades, whereas the construction sector has averaged only a 0.26% production growth per year over the same period.

German construction productivity growth since 1995

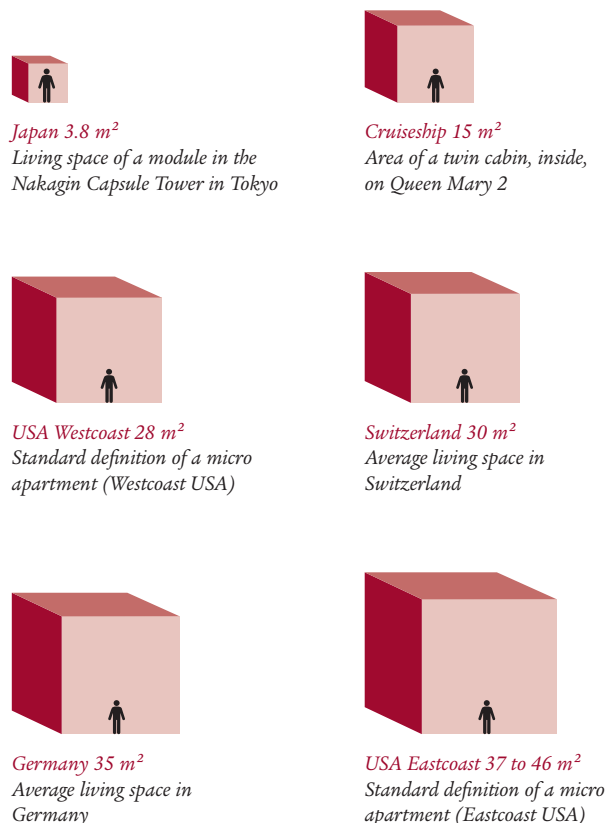
# 0.26 % p.a.

Source: McKinsey

## Micro-apartments – a future trend?

With the growing demand for flexible, sustainable and affordable housing, micro-living and micro-apartments have become a popular topic of discussion. Smaller properties are especially popular with singles, commuters, new graduates and students. However, there is no standard definition for the term micro-living. In Tokyo, where you can live in 5.87m<sup>3</sup> pods, “micro” is defined differently than in Zurich. Even within the US the general understanding of micro-apartments differs.

Standard definition of micro-apartments



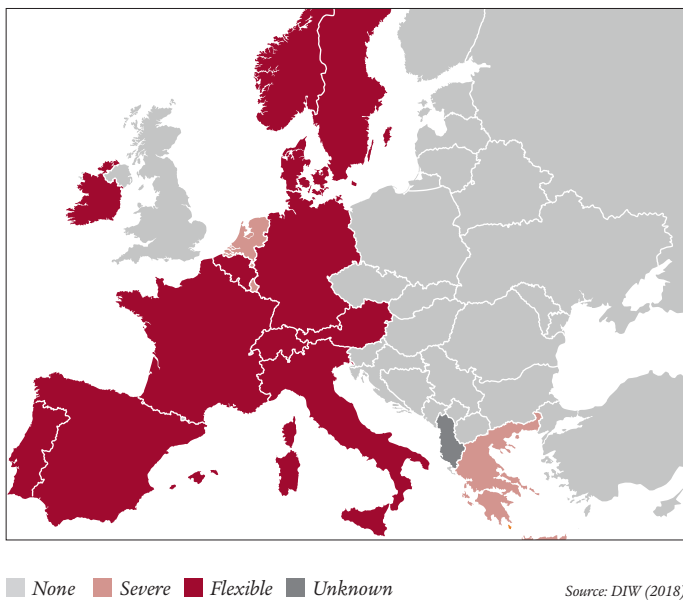
Source: Gottlieb Duttweiler Institut, BfS, Destatis

# Affordability is key

## Politicians want a say

With rent prices generally increasing, especially in urban areas where the lack of supply is coupled with growing demand for living space, regulation of the housing market has become a political focus. Examining regulations in individual European countries illustrates that rent controls are usually accompanied by strong economic performance, a developed democracy and an extensive welfare state.

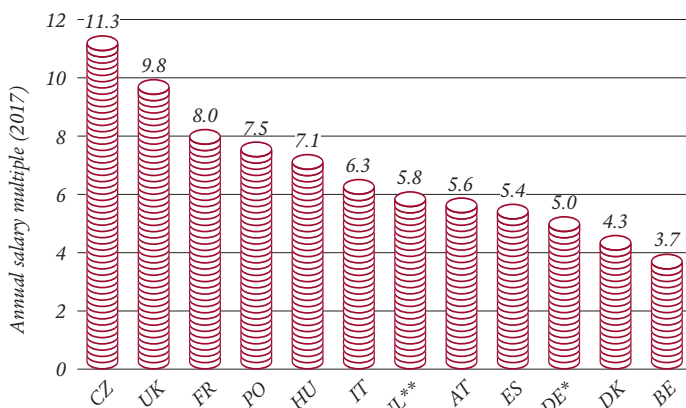
### Regulation of rental housing markets



## Can I afford to live?

Rising house prices have made homeownership a luxury in many European countries. Belgium is the most affordable; on average households must save 3.7 times their gross annual salaries for a new 70 m<sup>2</sup> dwelling. In other countries households must save much more. The Czech Republic is the most unaffordable; households must save 11 times their gross annual salaries for a 70 m<sup>2</sup> dwelling.

### Gross annual salaries for a new standardised dwelling

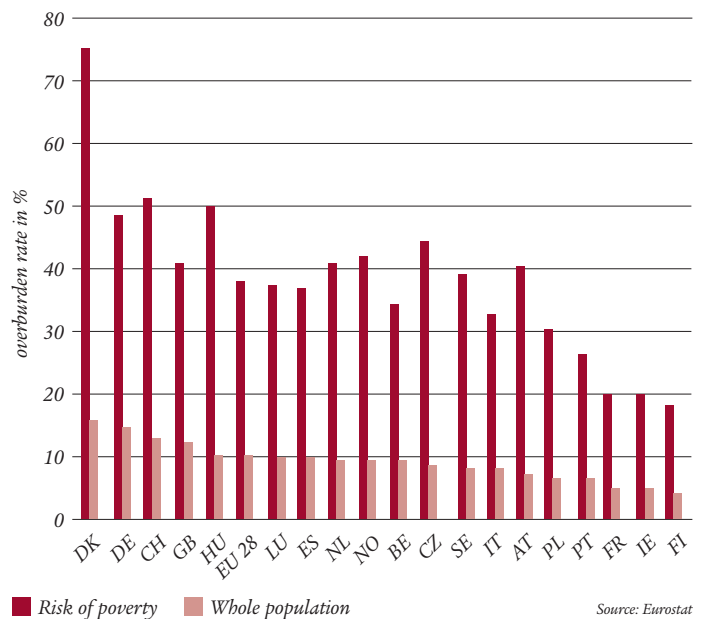


Source: Deloitte Property Index (2018); \*bid price; \*\*older dwellings

## High overburden rate

The overburden rate is defined as the proportion of households for whom housing costs represent more than 40% of disposable income. Across Europe the overburden rate indicates that some 11% of households cannot properly afford a dwelling. When only looking at the population at the risk of poverty (those with less than 60% of median income) the overburden rate increases to nearly 40%, ranging from 75% in Denmark to 18% in Finland.

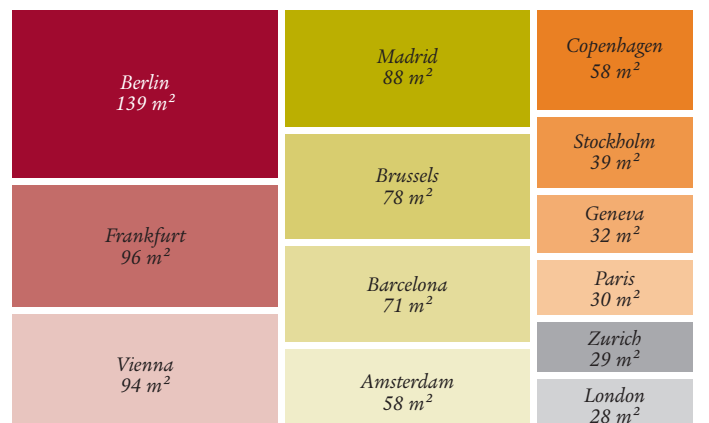
### Population share of housing cost overburden in 2017



## What USD 1,500 in rent can get you

Analysing the average living space available for a rent of USD 1,500 per month in major European cities, Berlin leads the way with 139 m<sup>2</sup>. This is nearly five times the amount of space available for the same cost in London (28 m<sup>2</sup>), Zurich (29 m<sup>2</sup>) or Paris (30 m<sup>2</sup>).

### Average apartment size at a rental price of USD 1,500



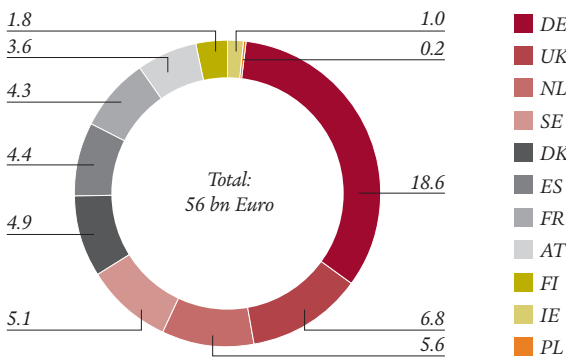
Source: RENTCafé (2018)

## Investors' darling

### Few choices

Institutional investment markets for residential real estate are established in only a few European countries. The highest transaction volumes in recent years have come from Germany, Sweden, Denmark and the Netherlands, where residential investments have long been an important market component. France, UK and Spain are among the emerging markets with increasing investment activity in apartment buildings.

Residential investment volumes 2018, € bn

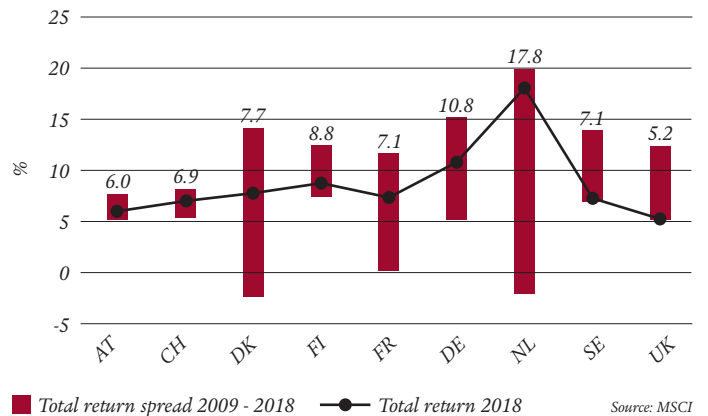


Source: JLL

### Extraordinary performance

Investments in residential real estate have achieved a strong and comparatively stable performance over the past decade. However, some markets such as German and the Netherlands have shown a considerable spread in the total returns achieved over 10 years. By contrast, very stable returns were achieved in Switzerland and Austria.

Total return in selected residential markets



Source: MSCI

## Research



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**Impressum:** Publisher: Released and approved by the Economics Department, Swiss Life Asset Management Ltd., Zurich • Editorial Board: Francesca Boucard, Severin Beltinger, Andri Eglitis • Translations: Swiss Life Language Services • Layout/Design: Thomas Grommes

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