PwC-Immospektive

Interpretation of the FPRE real estate meta-analysis for February 2022
References to FPRE graphics in our text are marked with [1] etc.

Negative production gap – production is being ramped up again

18 February 2022

In the fourth quarter of 2021 the number of coronavirus infections rose sharply again with the new Omicron variant. In response, new measures were issued, which impacted the economy. Due to a possible natural immunity, hopes are rising for a lasting recovery and an end to the pandemic in 2022. The global inflation is also driving up inflation forecasts in Switzerland. However, the SNB continues to adhere to its policy of negative interest rates for the time being. A lack of investment options is once again reflected in falling net yields on real estate investments. Prices for owner-occupied properties remain at a persistent high. Residential rents are still largely stable, with office rents slowly levelling off.

In the course of 2022, the restraining factors are expected to dissolve

The optimistic growth forecasts seen since summer 2021 are being reined in for 2022 because of delivery bottlenecks and more stringent coronavirus-related measures.[1] The pandemic worsened in December 2021 because of the new Omicron mutation and new restrictions were imposed in response. The high level of infections put a temporary halt to the recovery.[2] Growth forecasts are being corrected to 2.8% as part of a return to economic normality, which still represents above-average growth [8].[1] If natural immunity kicks in, the factors holding back the markets can be expected to disappear in 2022. The coming year is viewed in two halves, with the first half marked by high rates of growth and inflation, which will then weaken in the second half.[3] The main risks remaining in the second half are possible setbacks in the pandemic, longer-lasting capacity bottlenecks and global economic effects that might impact negatively on the Swiss economy.[4]

The situation on the labour market reflects the steady but slow recovery in the economic position. The unemployment rate fell from 3.3% to 2.5% in 2021. Compensation for short-time working played an important role here, making a significant contribution to keeping firms in business in certain sectors.[5] The unemployment rate is likely to fall again in the course of 2022 in keeping with the negative production gap (–0.5%).[6] The consensus forecast is for an unemployment rate of 2.4% in 2022 and stabilisation at 2.3% in 2023 [8,9]. However, some service sectors, in particular the hotel industry, have still not returned to their pre-crisis level. The largest number of vacancies is to be found in the mechanical engineering sector, where they have risen 100% against the previous year [10].

The SNB is watching the inflation situation

In the developed economies, rising inflation forecasts are evident in the consumer goods markets. In the USA, inflation rose to 4.6% in the course of 2021. The forecast for 2022 is 4.2%. In comparison with the global inflation trend, Switzerland is

1 Staatssekretariat für Wirtschaft (SECO), Medienmitteilung vom 9. Dezember 2021: Konjunkturprognose
2 KOF, Konjunkturbarometer, Konjunkturanalyse: Prognose 2022/2023 Pandemie bremst konjunkturelle Erholung
3 UBS, Medienmitteilung vom 11.11.2021, UBS Year Ahead 2022: Ein Jahr der Erkundung
4 Staatssekretariat für Wirtschaft (SECO), Konjunkturprognose, Herbst 2021
5 Staatssekretariat für Wirtschaft (SECO), Die Lage auf dem Arbeitsmarkt, Dezember 2021
6 Schweizerische Nationalbank, Quartalsheft 4/2021, Dezember

less susceptible to inflation risks because of the consistent strength of the Swiss franc. For 2022 an inflation rate of 0.8% is forecasted, which represents an increase over last year's forecasts (0.5%).[7] The main factor in inflation in the Swiss franc has been rates of increase in the prices of services within Switzerland (not including residential rents).[6] The SNB is watching from the sidelines for the moment and maintaining its existing policy rate of –0.75% [11].

Slight increase in fixed-rate mortgages – Saron mortgages remain constant

The sluggish but nonetheless ongoing recovery of the economy and slightly increasing inflation figures are leading to rising yields on government bonds. Yield forecasts are at –0.76% for one-year, –0.5% for five-year and –0.16% for ten-year Swiss government bonds, which means they are well above the rates in the previous quarter (–0.78%, –0.62%, –0.31%) and remain on an upward trend [22]. Mortgage rates have risen slightly since September 2021 as a result of a series of policy rate increases in the USA and, at 1.05%, 1.10% and 1.39% for three, five and ten-year fixed-rate mortgages respectively, are a little above the rates for the previous quarter (1.03%, 1.09% and 1.37%).[8] Variable-rate mortgages, on the other hand, remain stable at 2.63% [23]. The low level of mortgage rates has meant an expansion in the volume of mortgages to around CHF 1,107,4 billion, representing growth year on year of 4.3% [24]. Following the steps to be taken next by the European Central Bank, the Swiss National Bank is not likely to indicate any changes in the short term.[8]

Construction index benefits from strong order books for builders

The forecast for construction activity for 2022 points to positive change compared with the forecast for 2021. In 2021 the commercial and infrastructure construction sectors were still regarded in pessimistic terms at –0.8% and –0.7%. Catch-up effects will enable steady growth in building activity in 2022 to 2024 (0.6% in 2022, 0.5% in 2023 and 1.1% in 2024) provided the shortage of key construction materials eases [16]. The economic recovery trend is also reflected in the construction index. In the fourth quarter of 2021 the index shows growth of 6.8% year on year, with a particularly sharp increase in building construction at 11.6 % [17].

Pressure on production costs easing off

The building industry continues to be a major pillar of economic growth. Despite ongoing problems with resources, companies are finding solutions to drive construction business forward. Additional expenses such as higher procurement costs are a frequent issue.[6] The production cost index reached an historical high in the third quarter of 2021. In the fourth quarter, the easing in materials bottlenecks can be seen in a declining index, with cost reductions of –0.4% for multi-family units, –0.5% for single-family homes and –1% for building construction and industrial construction compared with the third quarter. Nonetheless, the production cost index shows a considerable increase year on year, particularly in building construction and industrial construction at +12.7% [18].

Despite recent rises in mortgage rates, prices for owner-occupied properties remain challenging

The coronavirus crisis has fuelled the market for owner-occupied properties strongly. Even in the recovery phase, the pandemic has left its impression on people's minds, including in terms of shifts in living arrangements. Demand for owner-occupied property remains high, favouring further price increases.[9] The sharp rise in prices for owner-occupied property in the third quarter of 2021, with an historic increase of 6%, reduced the affordability of residential property, since household incomes did not keep pace.[10] The macro situation remains the central focus here, as affordable residential property is very much available in peripheral locations.[11]

National increases in property prices in the luxury sector

The positive trend in prices has been unchecked since 2016. Owner-occupied property prices have risen +11.1% for apartments and +13.7% for single-family homes since 2016, and no change to this trend is in sight [3,4,7]. In the fourth quarter of 2021 the highest residential property prices in history were recorded, with the index standing at 262.6 points (1985: 100). In 2021, growth of 5.9% was recorded (owner-occupied apartments 4.4%, single-family homes 6.9%). Quarter on quarter a moderate increase of 1.2% across all housing types was registered.[12] In regional terms, the change is positive across the board. For owner-occupied apartments, Basel has the biggest price increase against the previous quarter at +2.9%. The smallest rise was to be seen in eastern Switzerland at +0.5%. The largest price rise for single-family homes was registered in southern Switzerland at +3.1%. The smallest increase was recorded in the Jura at 0.3%.[12] It remained the case this year that prices in the premium segment rose the most year on year (owner-occupied apartments +6.9%, single-family homes +7.5%). Against the previous quarter, prices at the

[7] Swiss Life Asset Managers, Perspektiven Konjunktur / Januar 2022
[8] Credit Suisse, Credit Suisse Hypothekarzinsprognose 1. Quartal 2022
[9] Zürcher Kantonalbank, Immobilien aktuell / November 2021
[10] UBS Swiss Real Estate Bubble Index / – 3Q. 2021
[11] Raiffeisen, Immobilien Schweiz – 4Q 2021
[12] FPRE, Transaktionspreis- und Baulandindizes für Wohneigentum, 4. Quartal 2021

lower end of the market climbed the most (owner-occupied apartments +1.5%, single-family homes +2.6%) [58,64].

Discount rates are at a low of 1.73%

After a temporary lull in housing construction, the project pipeline now looks well filled. This is likely to be the result of catch-up effects, as some projects with building permits got behind schedule during the pandemic. In the medium term, however, the number of planning applications cannot be expected to rise further, with developers among others less interested in housing construction after years of overproduction.[13] Meanwhile, yield expectations for multi-family units in prime locations are falling steadily. The consensus estimate for the minimum discount rate for multi-family units (net, in real terms) is 1.73% [34,35]. The total return is down again from the previous year at 5.5% for multi-family units (2020: 4.8%). Market values gained 6.5% year on year [27].[14] In regional terms, market values rose uniformly year on year. The largest gain in value was recorded in the canton of Zurich with a rise of 5.5%. Southern Switzerland and the Alpine region showed the smallest increases in value at 3.8% and 3.2%. The net yield rose against the previous quarter in all regions except Basel and Southern Switzerland. The biggest drop was seen in Basel (–0.2%) and in southern Switzerland (–0.6%). Year on year, the net yield remained stable on a slight upward trend in most regions.[14]

Declining rental prices in Q4 with –1.0% vs. the same quarter of the previous year

In 2021 a falling vacancy rate was recorded for the first time since 2008. The reasons for this may be moderately lower construction activity combined with a positive net inward migration rate (+8,600 in November 2021) [12,13]. This trend can be expected to continue.[11] Higher rental occupancy levels are more accentuated in popular locations though. Despite falling vacancy rates in 2021, in rural districts there is still an oversupply of housing for rent. A certain ‘flight from the city’ is still to be observed, with many leaving the urban centres because of the obligation to work from home. The main beneficiaries of lower vacancy rates have been suburban locations, as they allow reduced living costs and do not necessitate a move when the rules on working from home change.[14] Residential rents have fallen 1% year on year, with new build properties largely stable at –0.3%. The drop in rents was sharper for existing buildings at –1.7%. The areas of Zurich (–2.4%), the Jura (–2.3%) and the Alpine region (–1.9%) recorded the largest reductions in rents, with rents for existing buildings also falling most sharply here. Against the previous quarter, slight increases in rents were recorded again, at +0.7% in the existing building segment and +0.4% in the new build segment. The Jura, Basel and the Alpine region showed slightly negative figures; overall in Switzerland across all segments a rent increase of +0.5% over the previous quarter was recorded [25,26].[15]

A softer landing than anticipated in the post-pandemic market for office space

In recent quarters there has been a great deal of uncertainty regarding the demand for office space. The requirement to work from home has caused delays in the conclusion of new rental contracts or in the extension of contracts. There has now been some stabilisation in the market for office space as elsewhere. The availability of office space rose only moderately year on year from 5.5% to 5.8%.[16] A tendency towards restructuring and optimisation can be seen, with clear trends in terms of ESG criteria.[17] In the long term the negative effect of increased working from home will be offset by an expansion in the number of jobs in the administrative sector [2,6].[17]

Uniform increase in transaction prices for office rents across all cantons

13 Credit Suisse, Bauindex Schweiz Q3 2021

14 Zürcher Kantonalbank (ZKB), Immobilien aktuell, Ausgabe November 2021

15 FPRE, Marktmieten- und Baulandindizes für Renditeliegenschaften Schweiz (Datenstand: 31. Dezember 2021)

16 Credit Suisse, Büroflächenmarkt Schweiz 2022

17 JLL, Büromarkt Schweiz 2022

The improvement in economic circumstances and the scaling back of coronavirus-related restrictions have impacted on transaction prices for office rents. Office rents nationally rose 4.2% against the previous quarter [36,37,38]. Year on year, an increase of 2.7% was recorded. The fourth quarter also shows increasing office rents at cantonal level. In the cantons of Basel-Land (–0.4%) and Thurgau (–4.0%) the change in rents is positive and points to a slow return in demand for office properties. It is mainly in the cantons of Schaffhausen and Zug that significant trends in demand were seen in 2021 compared with the crisis year 2020, with growth in both cantons of 21.5%. Falling rents are to be observed in the cantons of Berne (–2.7%), Lucerne (–2.7%) and Thurgau (–6.3%). The rise in rents is reflected in market values, with year-on-year growth of 10%. Only in the Mittelland region were declining market values recorded, at –1.5%. The lowest increase in market value in Q4 2021 compared to the same quarter of the previous year is in Basel with +1.8% [40].[15]

Retail sales remain above their pre-crisis level

In 2021 the retail trade benefited from extensive steps to re-open the economy, even with some temporary exceptions. Sales rose significantly because of catch-up effects following the pandemic, restricted retail tourism abroad and limited leisure alternatives such as eating out and going to events.[18] In November 2021 revenue growth of 5.4% was achieved year on year (adjusted for sales and public holidays and not including filling stations). Compared with the previous month, revenues were up again in nominal terms with a rise of 1.4%.[19] In 2022 the factors driving this growth are likely to abate. Lower revenue growth can be expected, though sales are likely to remain above their pre-crisis level.[19] According to UBS and WP, however, falling rents are forecast for bricks-and-mortar retail space (UBS: –2% 2021, WP: –0.2% 2022) [6].

In restaurants the recovery has not yet set in

Compared to the retail trade, the hospitality industry had to contend with more restrictive measures in the course of 2021. The sector continues to be plagued by staff shortages, both in the restaurant and hotel sectors. The recovery is consequently progressing at a sluggish pace. Sales figures remain below their pre-crisis level and optimism is muted. However, according to a GastroSuisse survey, 44.6% of the businesses surveyed expect an improvement in 2022.[20] The slow awakening from the pandemic can also be observed in the unemployment figures, which have fallen by 41% in the hospitality sector compared to December 2020.[5]

Authors

Sebastian Zollinger
+41 58 792 28 87
sebastian.zollinger@pwc.ch

Sorur Alizadeh
+41 58 792 22 84
sorur.alizadeh@pwc.ch

Carl Berzia
+41 58 792 90 04
carl.berzia@pwc.ch

Real Estate Advisory
PwC, Birchstrasse 160
CH-8050 Zurich

PwC, Avenue Giuseppe Motta 50
CH-1202 Geneva

[18] Credit Suisse, Retail Outlook 2022

[19] Bundesamt für Statistik (BFS), Medienmitteilung vom 7.1.2022: Umsätze im Schweizer Detailhandel gehen im November 2021 nach oben.

[20] GastroSuisse, Konjunktur / KOF, Q3 2021