



KTI Market Review

Autumn 2015

Transaction volume remains high

Prime yields at record low levels

Rental residential properties attract investors

Weak economy creates pressures for rental markets



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Globally high investment demand has positively affected the Finnish property market. Transaction volume of the first three quarters of the year is already close to last year's total volume, which was already significantly higher than in previous years.

The number of players in the market is increasing due to both new international investors entering the market and new domestic structures being established. Thanks to a diversity of investor strategies, investment demand is targeted at numerous sectors and regions. Strong demand has pressured prime yields to record low levels. However, the tight economic situation has kept investors cautious, and yield premiums for secondary assets remain rather high. Higher yields have also started to attract investors to riskier assets. Differently from the previous years, some properties with high vacancies have also been sold this year.

Tight economic conditions are clearly seen in the commercial rental markets. Office rents in the Helsinki CBD, which have increased steadily during the past years have now stabilized or have even decreased slightly. Some significant moves of major companies have slightly brightened the sentiment in the rental market. However, companies demand efficient space and – almost without exception – move to smaller premises, due to which office vacancy rates keep increasing.

Retail rental markets are challenged both by the economic conditions and the changing behavior of consumers. The ongoing structural change in the retailing business is also impacting space needs and usage. In the shopping centre markets, this is seen in increasing differentiation between centres, as well as changes in their tenant base. Traditionally large retail sectors – for example clothing – are decreasing their space usage, while the role of services is increasing in order to attract consumers to shopping centres.

The supply of rental residential apartments is increasing as new capital is being targeted at residential property investments. Residential rents continue to increase, especially in areas with lower rents, whereas in the most expensive areas, affordability seems to become an issue. Good location and traffic connections are increasing in importance.

The Finnish GDP growth remains close to zero

The Finnish GDP growth for 2015 is expected to end just slightly in positive territory. After three years of negative growth, this is a slight hint of positive news. Finnish exports are expected to start increasing towards the end of the year, driven by growth in the key euro countries as well as in the US. However, the outlook for the domestic demand remains sluggish. The GDP growth for 2016 is expected to be some 1%.

Investments starting to increase?

Construction investments continue to decrease this year. The volume of renovation construction is increasing steadily, and has already exceeded the volume of new construction. The Confederation of Finnish Construction Industries RT expects construction volumes to increase slightly in 2016. Residential construction is expected to maintain its current level. Starts of some major commercial property projects will impact next year's volumes.

Unemployment is increasing

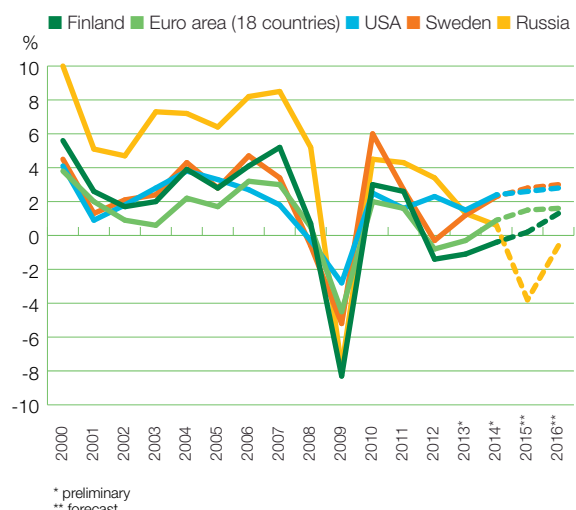
Sluggish economic development is now impacting employment more significantly than in previous years. The increase is caused both by an increase in the supply of workforce and by weak economic conditions. The unemployment rate has increased to 9.5 per cent this year, and is expected to remain high next year also.

Retail trade pressured by weak consumer demand

Increasing unemployment and low increase in earnings weaken consumers' purchasing power. On the other hand, record low – even negative – inflation supports the level of real income. Retail trading growth is expected to end in negative territory this year. The decrease is caused by both lower volumes and decreasing prices.

- GDP growth slightly positive in 2015?
- Unemployment and non-existent increase in earnings pressure retail trade
- Investments to increase slightly in 2016

GDP growth

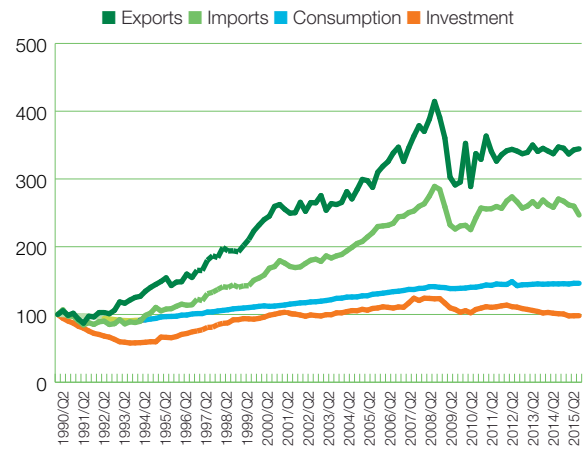


Source: Eurostat, OECD, IMF, Ministry of Finance

Adjustments in public economy will continue

The new government, which started in spring, is aiming at pursuing structural changes in the economy in order to strengthen competitiveness. The progress is, however, slow, and even when executed the actions' impacts will be seen with a lag. The level of public debt is now exceeding EMU criteria. Therefore, adjustments in the economy will continue.

Development of exports, imports, consumption and investment volume index 2000 = 100, seasonally adjusted



Source: Statistics Finland

Key figures – Finnish economy

	2010	2011	2012	2013	2014	2015**	2016**	2017**
GDP (change in vol)	3.0	2.6	-1.4	-1.1*	-0.4*	0.2	1.3	1.4
Change in exports	6.2	2.0	1.2	1.1*	-0.7*	0.9	3.0	3.3
Inflation	1.2	3.4	2.8	1.5	1.0	-0.1	1.1	1.5
Unemployment rate	8.4	7.8	7.7	8.2	8.7	9.6	9.4	9.1

* preliminary
** forecast

Source: Statistics Finland, Ministry of Finance

Property transaction market remains active

The property transaction volume of the three first quarters of 2015 totaled € 4.1 billion, which is some 30 per cent more than in the corresponding period last year. The outlook for the rest of the year also looks positive. Finland is getting its share of the globally strong demand and low interest rates keep supporting property investment. However, unlike in many other markets, the volume is not likely to achieve the levels of the record years in 2006 and 2007.

New players entering the market

The number and variety of players in the Finnish property market is increasing rapidly. Almost a dozen new international investors have entered the Finnish market this year. Altogether, foreign investors account for some 30 per cent of all transactions this year. New indirect investments also add to the market picture. In spring, the Swedish Balder became the biggest shareholder of the residential investment company SATO, and in September, Blackstone acquired a majority stake in the logistics and industrial property company Certeum. A fund established by a new fund management firm Sirius also brought new foreign capital to the Finnish market. Foreign investment demand is expected to remain strong: in the RAKLI-KTI Property Barometer survey, three out of four respondents expected foreign demand to continue increasing in the future.

The domestic player base is also changing. Of new Finnish initiatives, the most significant is Ankkurikadun Kiinteistöt Ltd, a joint company established by the Finnish Ilmarinen, the Swedish AMF Pensionsförsäkring, and the Finnish retailer Kesko. The company acquired some €650 million worth of retail properties from Kesko in the spring. Another company founded jointly by Ilmarinen and AMF is Antilooppi, who acquired a €400 million office property portfolio from Ilmarinen.

Institutions continue restructuring their portfolios

Market activity is also increased by the continued willingness to restructure property portfolios among the Finnish institutions. Ilmarinen in particular has been operating actively in various roles this year. In addition to the disposal of a significant office portfolio, it also sold a large residential portfolio to OP-Rental Yield special fund in the spring. Ilmarinen has also sold its stake in SATO. On the other hand, it has increased its property investments through acquisition of shares of

- Transaction volume higher than in 2014
- Secondary assets also attract investors
- Institutions have disposed of almost €900 million worth of properties
- More efficient space usage and tight economic conditions increase office vacancy
- Market sentiment turning more positive in the rental markets?

Ankkurikadun Kiinteistöt, as well as a proportion of the new shopping centre Redi. In addition, Ilmarinen has continued to pursue its international investment strategy through new joint venture investments in Belgium and in the US.

The disposal of the Certeum shares by Varma is another example of the pension funds' determined disposal and diversification strategies. Also Veritas and Etera have sold significant property holdings this year.

Altogether, domestic institutions have disposed of direct property holdings worth some €870 million this year. On the other hand, the total value of their new direct investments only amount to some €100 million.

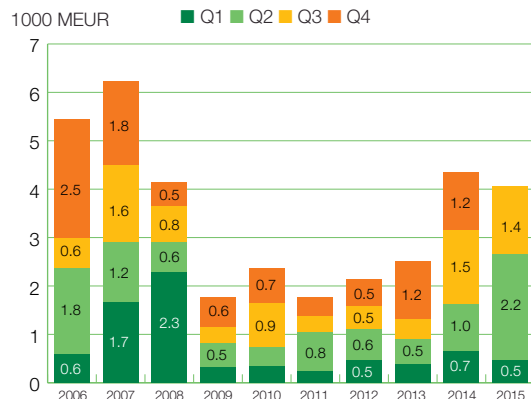
Investor interest diversified to various sectors

Retail properties have been the most traded sector in the first three quarters of 2015, with one third share of the total volume due to Kesko's major rearrangement along with some other large transactions. Office and residential properties both account for some 25 per cent of the total volume.

Yields at a record low level

Pressured by the strong investment demand, prime yields have decreased to record low levels. Investors still focus on secured cash flow, and, according to the RAKLI-KTI Property Barometer, prime office yield in the Helsinki CBD is now rated at 5.0% on average. The lower quartile, illustrating the very best assets, stood at 4.75%.

Transaction volume in the Finnish property market, quarterly



Source: KTI

Unlike the few previous years, riskier assets are attracting investors in the current market. Investors do, however, require a decent compensation for the higher risk, and secondary yields have remained stable. In the RAKLI-KTI Property Barometer, yields in all major cities outside the Helsinki metropolitan area even increased slightly compared to last spring. Secondary yield levels are maintained by the constrained economic situation.

Increase in Helsinki CBD office rents stopped

In the commercial property rental markets, sentiment remains sluggish. Best areas and premises still hold on better compared to secondary assets. In the Helsinki CBD, the amount of vacant office space remains moderate. However, even in the prime areas, the rental levels have decreased slightly in the past six months. In terms of both the number and the volume of new rental

agreements, market activity has decreased, and new agreements have not been made in the best properties. The KTI rental index shows an annual growth of 0.6% in new office rental agreements. Within the past six months, rental levels have decreased by 0.5%.

In the RAKLI-KTI Property Barometer, the outlook is now slightly less negative than last spring. Some 25 per cent of the respondents expect office rents to increase slightly in the Helsinki CBD. In all other areas, the proportion of respondents expecting a rental decrease is now lower than last spring, and the majority of respondents expect office rents to remain stable.

Large rental agreements have been released

The positive sentiment in the rental market is supported by a couple of large lease transactions recently released. For instance, Varma has rented out large premises in the former Nokia Research Center premises in Ruoholahti, as well as its own former premises in Salmisaari. Digia and BNP Paribas also announced a significant office lease in Pitäjänmäki. However, these leases are not likely to decrease the amount of vacant space, as, almost without exception, tenants move to smaller and more efficient premises.

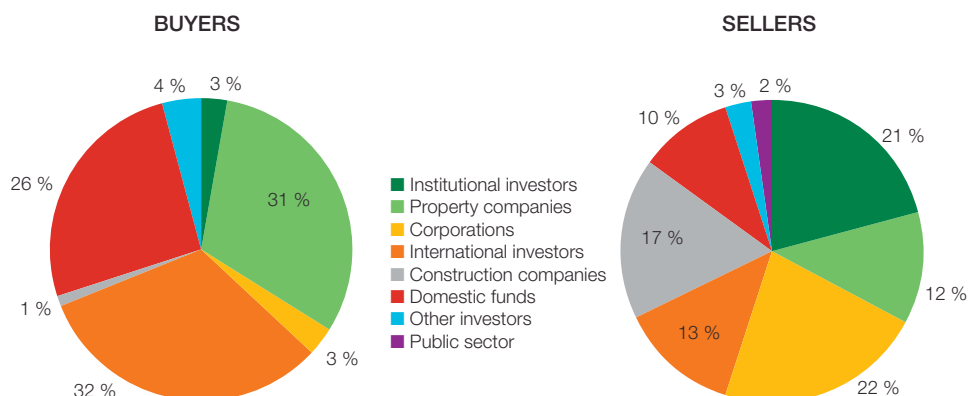
In the KTI rental database, the gross take-up of offices amounted to some 325,000 square meters between August 2014 and 2015, which is somewhat less than the annual average of the past decade. Compared to the previous year, gross take-up increased slightly due to, for instance, the completion of the new premises of OP Group in Vallila. Gross take-up measures the volume of new leases added by the amount of newly completed premises.

Office occupancy rate continues decreasing

The amount of vacant office space shows no signs of decreasing. According to Catella, the office vacancy rate in the Helsinki metropolitan area stands at 13.4 per

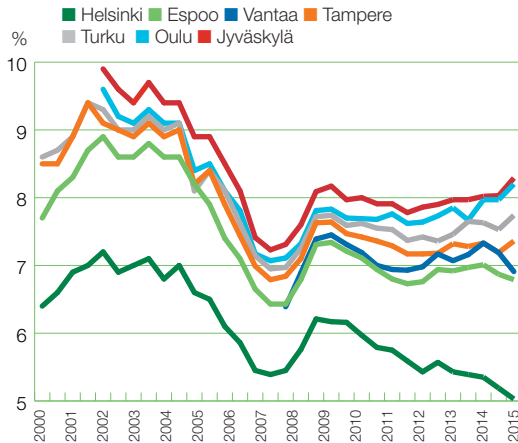
Profile of investors

% of all transactions, January-September 2015



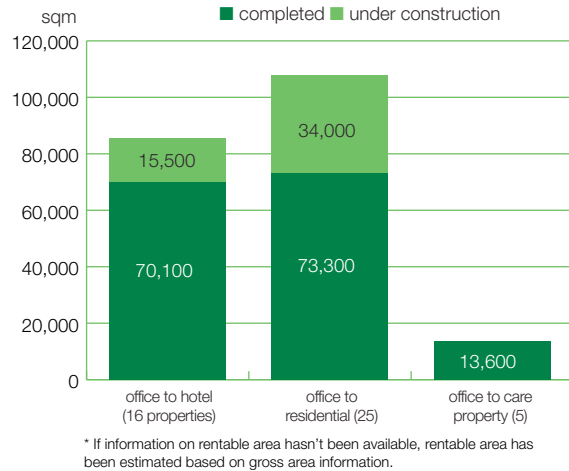
Source: KTI

Prime office yields in major Finnish cities



Source: RAKLI-KTI Property Barometer

Office redevelopment in other use in 2007-2015 in Helsinki metropolitan area, Rentable area*, sqm



Source: KTI, RPT Docu Oy

cent. In the KTI rental database, the occupancy rate of offices in major investors' portfolios decreased to 80 per cent at the beginning of September. The majority of the respondents in the RAKLI-KTI Property Barometer expect vacancy rates to continue increasing in the next six months as well.

Office construction volumes decreasing

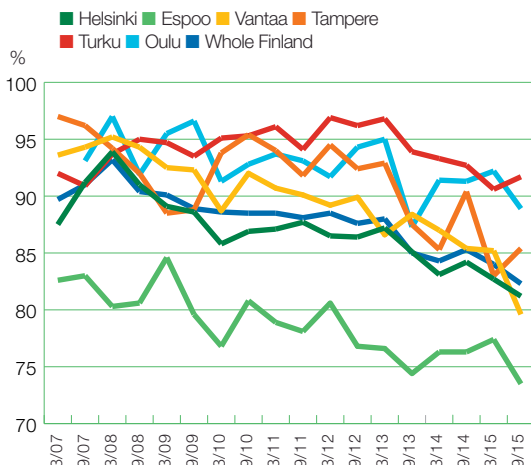
Despite of the tight economic situation and the large amount of vacant space, new offices continue being built in the Helsinki metropolitan area. Altogether, some 60,000 square meters of office space was under construction at the end of September. The total volume of completions in 2015 amounts to some 80,000 square meters.

Numerous renovation projects underway

The large amount of vacant office space pressures investors to search for new solutions for empty properties. In dozens of office buildings, change of use projects are being investigated as a solution for the vacancy issue. However, these processes tend to be slow, even impossible, due to planning issues and / or technical characteristics of the buildings.

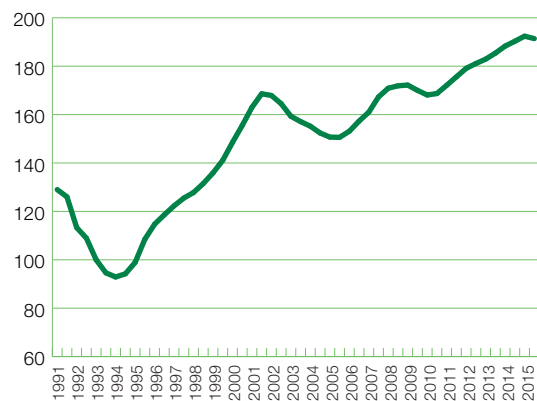
According to the KTI follow-up, more than 40 office buildings in the Helsinki metropolitan area have been renovated to another use between 2007 and 2015. Most commonly, properties are redeveloped to residential or hotel use. In 2015, the Lilla Roberts and Indigo hotel projects have been completed in the Helsinki CBD.

Office occupancy rates



Source: KTI

KTI office rent index, Helsinki CBD index 1993=100



Source: KTI

Shopping centres challenged by economic conditions and e-commerce

Retail sales are suffering from weak consumer confidence and sluggish development of consumer demand. According to Statistics Finland, retail sales decreased by 1.1 per cent in January-August compared to the previous year.

The sluggish situation can also be seen in the RAKLI-KTI Property Barometer, where the outlook for retail rental development remains negative – although slightly less negative than last spring. In the Helsinki CBD; the balance figure of rental development ended in slightly positive territory. The outlook for the development of vacant retail space is now also less negative than six months ago – even though the amount of vacant space is still expected to increase.

Number of visitors stable, sales decreasing slightly in shopping centres

According to the KTI indices commissioned by the Finnish Council of Shopping centres, retail sales in shopping centres have decreased by some 1.1 per cent in the first three quarters of 2015 compared to the previous year. The number of visitors has, however, remained stable and shows an increase of 0.3 per cent. There are significant differences between different retailer categories. Tight economic conditions also drive the shopping centres to rejuvenate and respond to the consumers' changing needs.

Shopping centres responding to the increase in e-commerce

According to the Shopping Centre Barometer of the Finnish Council of Shopping Centres conducted in October, the increase in e-commerce, together with the prevailing economic conditions, is the biggest future challenge for shopping centres. The majority of the respondents expect the impact of e-commerce to be negative. On the other hand, digitalization and technological development is seen to open new opportunities for shopping centres.

Retailers with successful omni-channel strategies combining physical stores and e-commerce are expected to outperform in the future. While in the past retailers

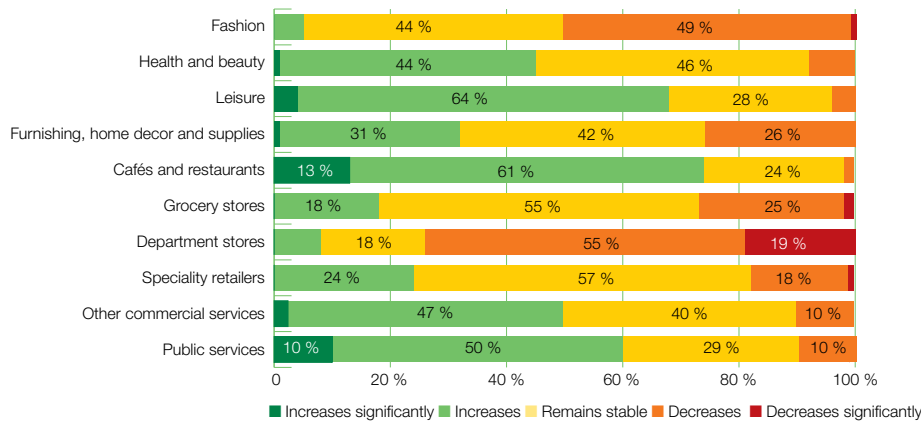
- Differences in shopping centre performance are increasing
- Services are increasing their proportion of total space usage
- The best performers pursue successful omni-channel strategies

with strong physical store chains aimed at developing their e-commerce strategies, traditionally strong online retailers are now strengthening their physical presence in order to reach consumers in various channels.

The importance of services increasing, and quality improving

According to the Shopping Centre Barometer, of the retailer categories, clothing and department stores are facing the biggest challenges. This will likely result as major changes in tenant mix strategies, as clothing currently represents some 25 per cent, and department stores some 11 per cent of the total space usage in the Finnish shopping centres. In the future, consumers have to be attracted to the shopping centres by different kinds of retail supply. The biggest opportunities are seen in food and beverage services, as well as in other consumer services – including public services. Of the retailer categories, leisure as well as health and beauty are expected to perform well in the future.

Shopping Centre Barometer: Development of space demand in different business fields



Source: Shopping Centre Barometer

Large centres in the Helsinki metropolitan area expected to outperform

Urbanisation, developing urban structure and increasing demand for services are creating new business opportunities for shopping centres. These trends support, in particular, larger centres in urban city areas or within good public transport connections. The future of the large shopping centres in the Helsinki metropolitan area is seen as clearly more positive than smaller centres in other towns. The trust and confidence in large centres' performance is also illustrated by the recent development of the supply: during 2012-2014, five new centres with a gross leasable area of more than 40,000 square meters were opened. The supply will also be increased through the development of the large ongoing projects of Redi in Kalasatama, Iso Omena and Ainoa in Espoo, as well as the Tripla project in Pasila, which will be started soon.

The position of shopping centres remains strong in both the retail and property investment markets

Despite of all the challenges, the outlook for shopping centre business remains positive, although the differentiation between centres and retailer categories is expected to increase. In the Shopping Centre Barometer, the majority of respondents expect shopping centres to increase their share in total retail sales. This also maintains shopping centre properties' position in the property investment market.

Shopping centre sales and visitor indices 2015:

Change in the number of visitors and total sales quarterly 2015:		
Visitors Q1: -1.2 %	Visitors Q2: +0.1 %	Visitors Q3: +0.3 %
Sales Q1: -0.9 %	Sales Q2: -1.2 %	Sales Q3: -1.1 %

Source: Finnish Council of Shopping Centers, KTI

Investments in residential properties continue to grow

Investors' interest in residential property investment remains strong. The position of residential properties in the investment market is supported by increasing rental demand in all major cities, especially in the Helsinki metropolitan area. Also, the continuous insecurity of the commercial property sectors is enhancing residential properties' attractiveness. In the RAKLI Rental Residential Barometer survey, the majority of the respondents report an intention to continue investments in rental residential properties.

Total transaction volume approaching € 1 billion

The volume of residential property transactions has increased to a new scale in recent years. While total annual volumes varied between €100 and 300 million in 2006-2012, they increased to €600-700 million in 2013 and 2014. In the first three quarters of 2015, almost one billion euros worth of residential properties have changed their ownership. A big proportion of the transactions are newly developed properties sold to property funds by construction companies. However, major portfolios of existing residential apartments have also been sold. In the spring, Ilmarinen sold some 1,200 apartments to OP-Rental Yield. ICECAPITAL sold the portfolio of their first fund to SATO, and Asuntosalkku Suomi Oy, a newly established structure, bought 1,200 apartments in two transactions from Quorum's funds.

Rents continue increasing

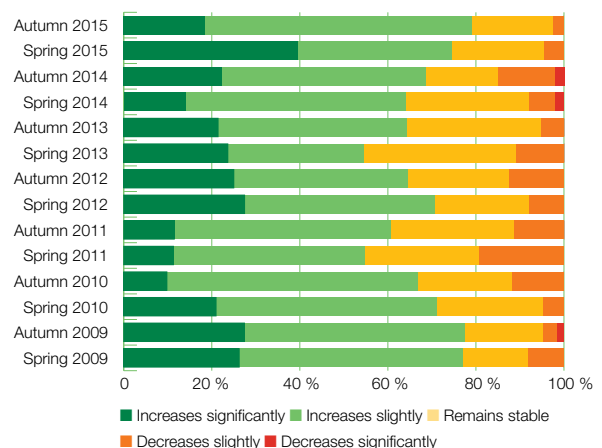
The strong demand has maintained continuous increase in residential rents. According to KTI Residential rent indices, rents of new agreements have increased by some 3-4 per cent in all major cities. In all areas, increase has been stronger in the autumn compared to the previous six months. The increase has been the strongest in Espoo and Vantaa - over 4 per cent in both cities.

The increasing supply as well as sluggish development of consumers' purchasing power is starting to set limits for rental increases. The increase has in recent months been stronger in areas with lower rental levels, as prime rents are approaching the limits of tenants' affordability.

- Record high transaction volumes in the residential sector
- Rents continue increasing in major cities

Development of rental residential property investments

How will the rental residential property investments of your own organisation develop within next 12 months?



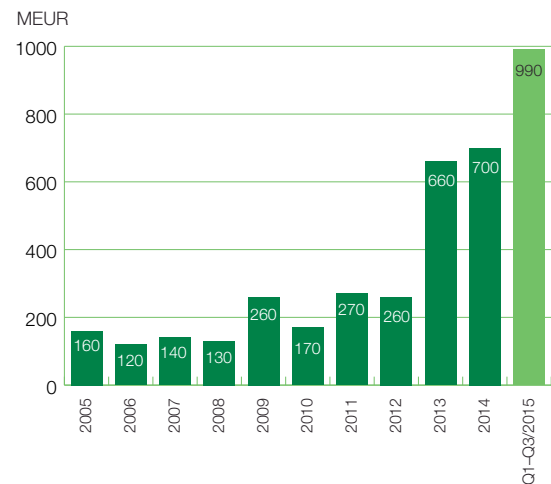
Source: RAKLI Rental Residential Barometer

Strong demand for small apartments

The leasing of large apartments continues to be challenging. In the RAKLI Rental Residential Barometer survey, the outlook for renting large apartments remains slightly positive in Helsinki, where the majority of respondents expect rents to remain stable. In all cities outside the Helsinki metropolitan area, rents are expected to decrease.

Although the demand for small apartments remains strong, tenants are becoming more selective in this segment, and the location – in terms of, for instance, rail connections – is increasing in importance.

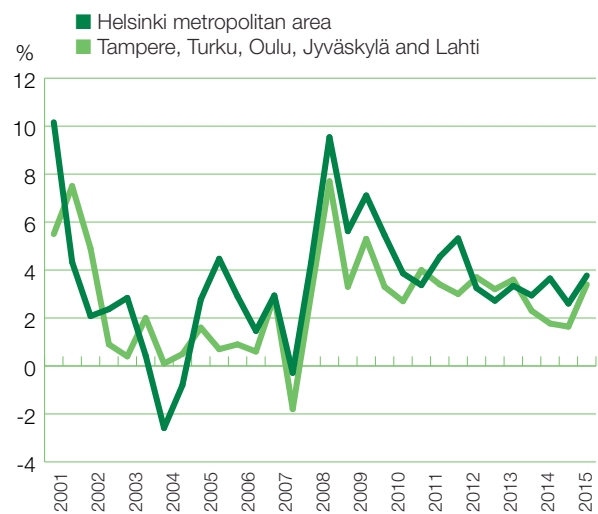
Volume of residential portfolio transactions



Source: KTI

KTI Residential rent index

Annual change, Helsinki metropolitan area and other major cities



index spring 2000 = 100,
market rents, new agreements

Source: KTI

Commercial property markets in growth centres

Several transactions in Tampere

KTI has recorded more than 20 significant property transactions in the Tampere region this year. Many of these transactions have been part of larger portfolios, comprising assets in different parts of Finland. Despite of the activity in the property investment market, the yield levels have not decreased. The respondents of the RAKLI-KTI Property Barometer estimate that prime office yield in Tampere city centre has remained clearly above seven per cent. The most significant commercial property development projects are Ratina shopping centre, developed by Sponda close to the city centre, the last phase of Technopolis' Yliopistorinne office project, as well as two logistics centre projects in the Linnakallio area in Pirkkala.

The respondents of RAKLI-KTI Property Barometer still expect negative development for office, retail and industrial rents in Tampere, but the expectations are slightly less negative than earlier. Twelve per cent of the respondents expect Tampere city centre office rents to increase during the next six months. Median rent for new office rent agreements in Tampere city centre was approx. 15 €/sqm/month.

The retail occupancy rate has remained above 94% both in the city centre and in all of Tampere, although the amount of vacant retail space has increased in the city centre area. The office occupancy rate increased during summer and stands currently slightly above 85% in the KTI rental database.

Office occupancy rate still rather high in Turku

The amount of vacant retail space in the Turku city centre is still high, while retail space supply is increasing outside the city centre. The largest ongoing project is the extension of shopping centre Mylly in Raisio. The amount of empty office space has decreased during the last six months in KTI's database by almost 3,000 sqm, and the office occupancy rate has increased to over 92%. The supply of new office space has remained rather low. In Kupittaa, the ElectroCity property is currently undergoing a major redevelopment project. One of the future occupiers of the property will be the research and development centre of LG Electronics.

The respondents of RAKLI-KTI Property Barometer expect Turku office, retail and industrial rents to remain stable or slightly decrease. There are, however, some positive signs especially in the industrial sector. The local respondents of KTI Regional barometer survey expect the space demand of industrial premises to improve, partly due to the new ship orders in the Turku shipyard.

Also in the Turku region, many significant property transactions have been completed in various property types. One of the latest examples was the transaction

- Transaction volumes at high level in many growth centres
- Outlook for commercial property rents still mainly negative

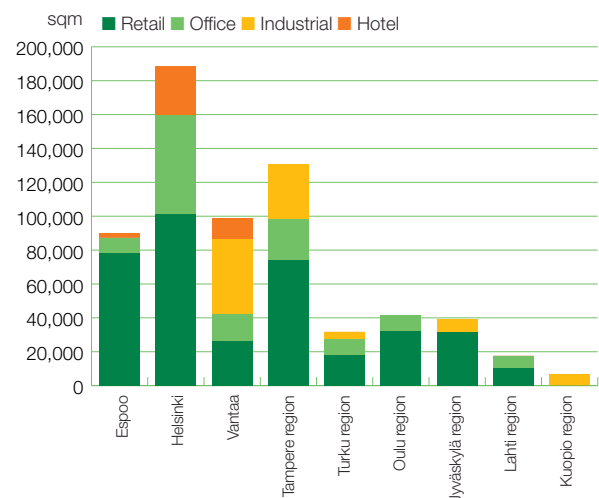
of Pulssi medical centre in the Turku city centre area, acquired by special investment fund eQ Care from AKR Aura property fund, managed by Auratum.

Retail supply increases in Oulu

Modern retail space supply is increasing in Oulu. The largest ongoing development project is shopping centre Valkea, to be completed in the city centre area next year. Additionally there are several smaller retail projects under construction in the different parts of the city. During the last six months several new retail rent agreements were signed in the Oulu city centre. The median rent of new retail rent agreements exceeded 25 €/sqm/month.

During January-September, the transaction volume in Oulu was almost €150 million, while in the previous years the total annual volume has remained below €100 million. One of the largest transactions was the

Commercial properties under construction including both new and major redevelopment projects rentable area*, sqm



* If information on rentable area hasn't been available, rentable area has been estimated based on gross area information.

Source: KTI, RPT Docu Oy

sale of Nokia's former 68,000 sqm R&D centre from NV Property Fund I to Sagax. Additionally, Citycon sold two retail properties in Oulu city centre to local retailer Osuuskauppa Arina for €13 million.

The outlook for Oulu rental development is a bit more negative compared to other growth centres. None of the respondents of RAKLI-KTI Property Barometer expect rents to increase in any commercial property type during the next six months.

Office and industrial space demand expected to improve in Jyväskylä

In the Jyväskylä region several residential property transactions have taken place as part of larger portfolio deals. The largest commercial property transaction this autumn has taken place in the Tourula area. Quorum's fund acquired a retail property for €7.8 million from a company managed by Niam. The most significant commercial development project is over 20,000 sqm new Prisma centre, to be completed in summer 2016 in the Seppälä area. Additionally, the 6,000 sqm logistics centre of Lindab is under construction in Seppälänkangas.

The outlook for office and retail rents is rather stable. The local respondents of KTI Regional barometer survey expect the space demand of office and industrial premises to improve slightly. The amount of vacant office space decreased during the last six months in KTI rental database. The office occupancy rate stood at 87% in the beginning of September.

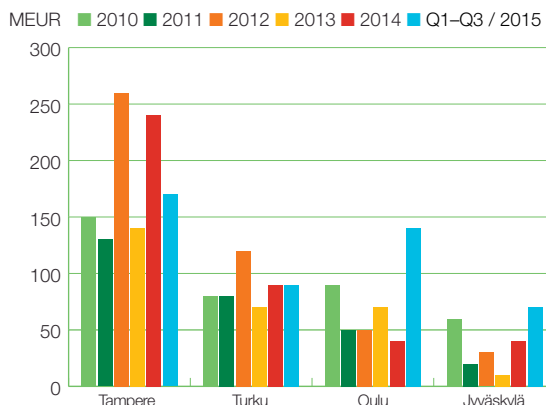
Other cities

In Lahti, commercial property development has been rather active this year and property transaction volumes have also increased. One of the largest new projects, BW Tower office property, will be completed late this year. BW Tower was acquired in spring by a consortium of Finnish investors. In summer, Fennica Properties I fund acquired an office property in city centre and Sirius' fund acquired a retail property from Citycon as part of the larger portfolio.

In Kuopio, large amount of new office and retail rent agreements have been signed in the city centre. The rental levels have been stable, but the amount of empty office space doubled in the KTI database during the last six months. This year's largest property transactions have been part of larger portfolio deals.

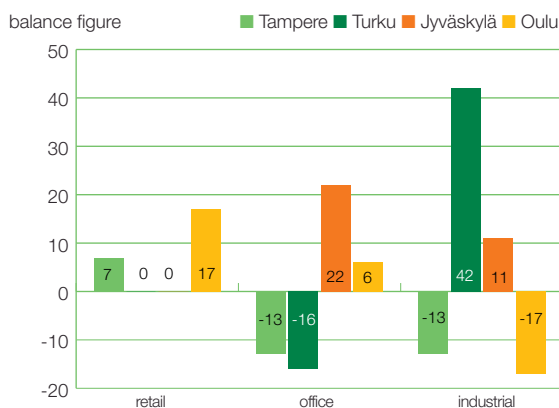
Due to increasing investor interest and large portfolio deals, many properties have also been transacted in the smaller Finnish cities. Large individual transactions have been completed in Pori and Hämeenlinna, for example. In Pori, Swedish investor Hemsö acquired a 23,000 sqm educational property development project from Citycon for €56.5 million. In Hämeenlinna, eQ Finnish Real Estate fund acquired two retail properties from a property fund managed by Nordic Real Estate Partners for €48 million.

Transaction volume 2010-2015 Tampere, Turku, Oulu, Jyväskylä



Source: KTI

Space demand growth expectations Tampere, Turku, Jyväskylä and Oulu regions, balance figures



Source: KTI Regional Barometer survey, autumn 2015



KTI Finland is an independent research organisation and service company providing information and research services for the Finnish real estate industry. KTI maintains extensive databases on returns, rents, transactions, operating costs and customer satisfaction measures in the Finnish property market. Based on these databases, various kinds of benchmarking and analysis services can be provided. KTI's clients comprise major property investors, managers, occupiers as well as service providers in the Finnish market. KTI is owned by the Finnish Real Estate Federation and RAKLI, the Finnish Association of Building Owners and Construction clients.

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