The Italian real estate market
The road to recovery

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This article provides an overview of the Italian real estate market, its current situation and future prospects as it continues on the road to recovery. Starting from an overview of the current economic situation and a brief description of the measures that the government is taking to stimulate growth and improve efficiency, the article focuses on the performance and future prospects of the various segments of the Italian market. Finally a summary of the main deals in the market is outlined demonstrating the increasing attractiveness of the Italian real estate market.

Political and economic setting

Italian political reforms

The Italian economy is continuing on the path to recovery, which started in 2015 and is continuing in 2016.

The center-left party government, led by Matteo Renzi since the first quarter of 2014, has implemented several political, economic, and institutional reforms as well as legislative changes aimed to stimulate growth.

The most important implemented reforms have been the Jobs Act, approved in September 2015, aimed at rationalizing the labor market, and the Stability Law, which came into force in December 2015. In particular, the Stability Law introduced important changes to the tax regime such as the abolition of the municipality service tax (TASI) and municipal property tax (IMU) on the first residential property owned by individuals, as well as the reduction of the corporate taxation rate (IRES) from its current 27.5 percent to 24 percent starting from 2017.

OPPORTUNITIES

Ambitious **reforms and austerity** measures will be crucial for economic growth and attracting foreign investments
Low international **oil prices** will contain energy and commodity prices
GDP **growth** has been forecasted
Reduction of **unemployment and taxation** are expected
Improvement in the **labour market** will help to drive domestic private consumption higher

THREATS

Slowdown in **emerging markets** could have an impact on the industrial sector that relies on exports
Long term unemployment persists, especially in the **youth segment**
An increase in the ratio of **public debt to GDP** could affect credit rating
Bank credit remains constrained due to the large and still rising amount of **non-performing loans**
Perceived complications **in legal and administrative processes** may dissuade investors

The Italian Government has implemented several reforms in 2015. This will make Italy an important market for foreign investors

Macroeconomic highlights

In a general climate of austerity across developed countries, the Italian market is showing signs of recovery. Estimates of GDP for the coming years are positive; in fact, GDP is forecast to increase to 1.4 percent in 2016, compared to 0.8 percent for 2015.

The ratio of debt to GDP is expected to remain substantially stable, slightly increasing from 132 percent in 2014 to 136 percent in 2015 (these are estimates as final data is not yet available), but is anticipated to reduce in the following years.

In 2016, private consumption is expected to grow by around 1.2 percent, a similar level to GDP growth.

Inflation in Italy is expected to increase to 1 percent in 2016 up from 0.3 percent recorded in 2015.

Figure 2: Real GDP growth and private consumption growth in Italy

Source: Institutional Paper - EU commission

Figure 1: Yearly inflation rate expected

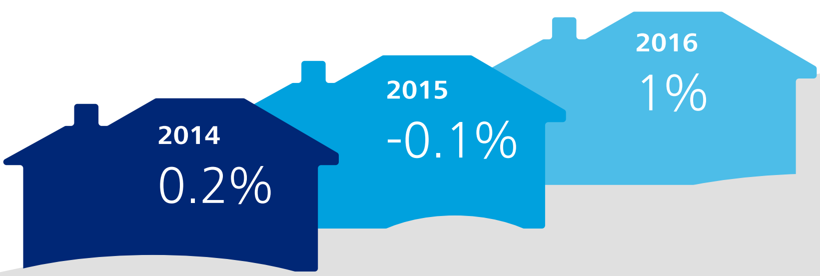
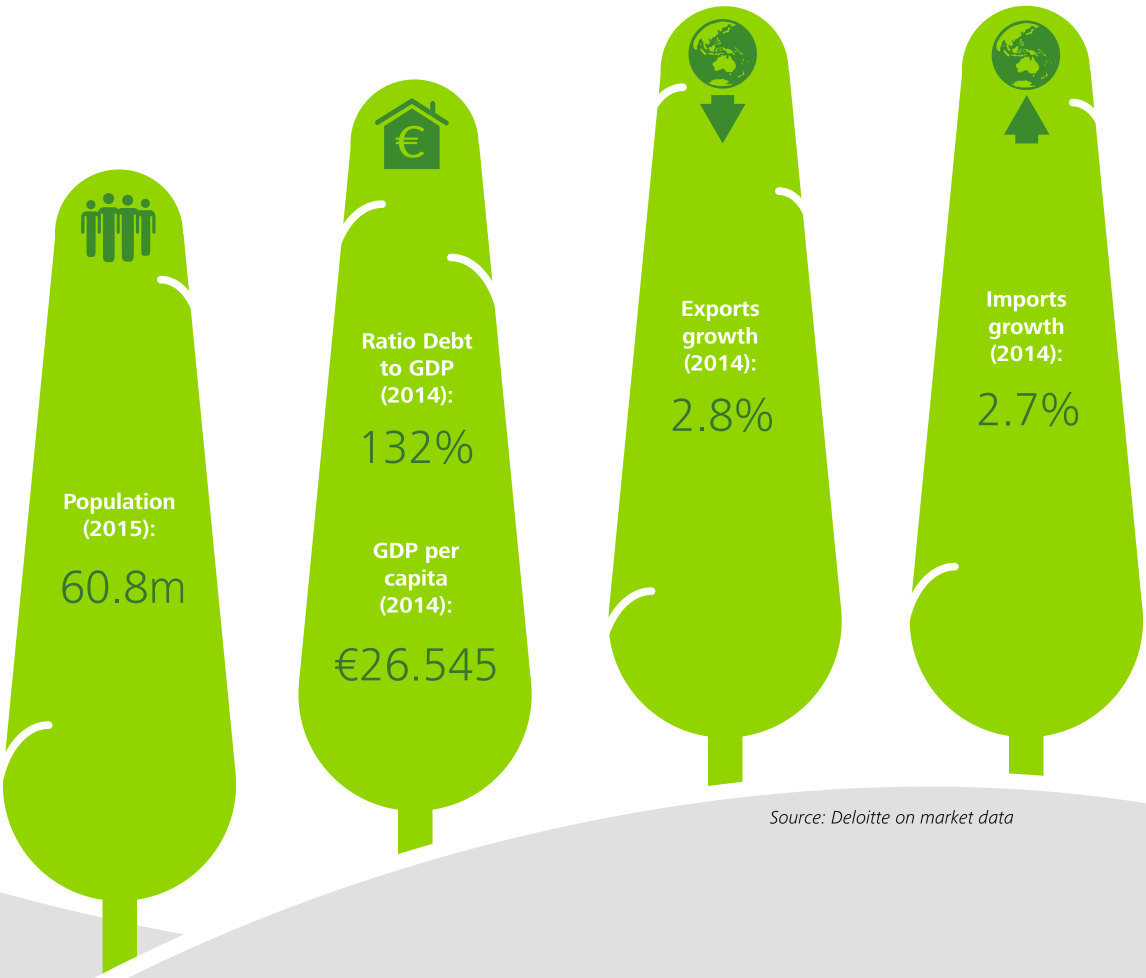


Figure 3: Key indicators of the Italian economy



Source: Deloitte on market data

In a general climate of austerity across developed countries, the Italian market is showing signs of recovery

The economic outlook for Italy is positive, with the diminishing risk of a return to recession

Labor market

Unemployment in Italy has started to show signs of improvement, reducing from13 percent in Q1 2015 to 10.3 percent in Q3 2015.

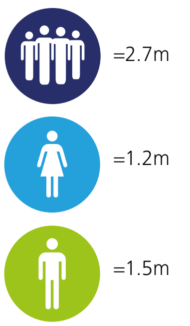
In absolute values, the number of unemployed people in Italy for the entire year of 2015 is expected to reach about 3 million out of a total of 25.5 million people currently in the active labor force.

Unemployment is still a significant issue within the younger population (15 to 24 years) and reached 40.5 percent in Q3 2015. The recently enacted Jobs Act is designed to address this issue by providing tax breaks for companies that hire workers on permanent contracts and make the employment market more fluid.

In addition, the labor legislation will more accurately align the Italian employment market with the other European industrialized countries and stimulate interest and investment from multinational corporations in the coming years.

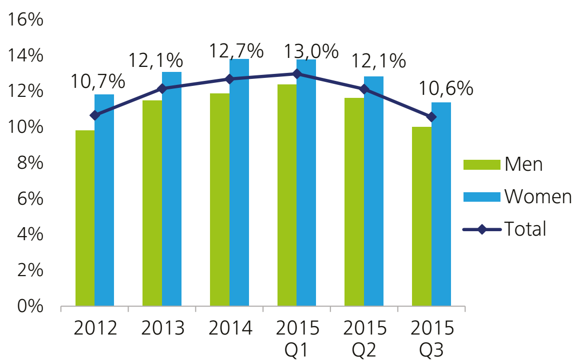
Overall, the measures taken by the government to improve the labor market, reorganize public administration, and support economic growth will have a positive impact on the economy over the medium to long term.

Figure 4: Unemployed people in Q3 2015 (m)



Source: Deloitte on market data

Figure 5: Italian unemployment rate breakdown by gender (percent)



Source: Deloitte on market data

Unemployment is forecast to decrease in 2016

Real estate market

Market overview

The Italian Real Estate market continues to show growth with a total level of investment in 2015 amounting to €8.2b, more than doubled compared to 2014, with the last quarter of 2015 accounting for around €3.1b of the total.

The majority of the investments have been made by foreign investors from the Middle East, Central Europe, and Asia. Of the total volume invested in Italy in 2015, 75 percent (6.1b€) involved foreign capital.

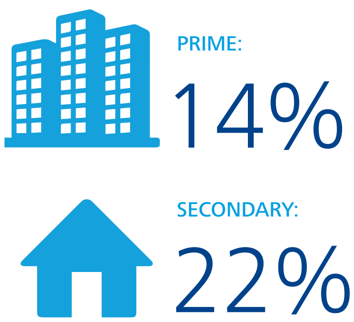
In 2015, total investment data showed that office properties were the preferred asset class, with the hospitality sector showing a good increase in the volume of transactions compared to 2014.

The retail and logistic sectors registered a reduction in investment volume compared to 2014, mainly due to the lack of quality in the offerings.

In terms of location, Milan and Rome still remain the main target destinations. A recent survey suggests Milan was the most attractive city, with 10 percent of respondents expressing their interest to invest in the Italian city rather than other European cities.

In fact, of the total investments in real estate made in 2015, 4.5b€ has been invested in Milan, representing an increase of about 3 times with respect to 2014, while 0.8b€ has entered the city of Rome, which represents an increase of 5 percent.

Figure 6: Percentage of investors who expressed an interest to invest in Italy in 2016 – breakdown by type of asset and location



European investors are looking for assets in prime locations to ensure a long term and secure income

Figure 7: Total Real Estate investment in Italy in 2015

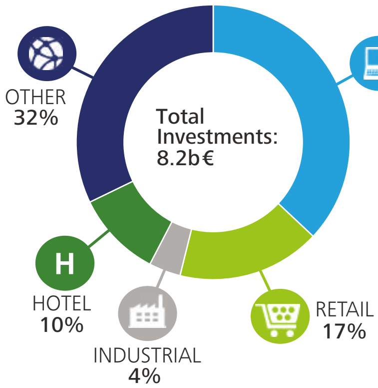


Figure 8: Total Real Estate investment in Italy in 2015

Milan continues to be an attractive target for real estate investors

Competition for quality assets towards the end of 2015 has led to the compression of net yields in the Italian commercial real estate market

Office

In 2015 the prime office market continued to dominate the interest of global investors, who targeted large assets and portfolios. Domestic investors showed the most interest in prime assets of a smaller size.

In Milan and Rome, prime net yields both decreased compared to 2014, passing from 5 percent and 5.2 percent respectively to 4 percent in 2015.

Prime rent in Milan and Rome CBD in 2015 remained stable at 490€/mq /yr and 380 €/mq/yr, a similar level to 2014.

Retail

In 2015, retail investments were focused on the northern and central regions of Italy with a focus on the shopping center segment.

Net yields generally decreased in 2015 in the main locations. Prime yields for high street, for example, decreased from 4.5 percent in Q4 2014 to 3.5 percent in Q4 2015.

Investment volume in shopping centers reached 0.7b€, equal to 51 percent of the total retail investment in 2015. Shopping centers are forecasted to remain the most attractive asset class within the retail segment.

Hotels

The Italian hospitality market continues to be one of the most attractive real estate segments, showing interest from key international investors as well as hospitality groups.

The key performance indicators remain very attractive with the average occupancy rate in the main cities reporting an occupancy rate above 70 percent. In fact, in 2015 Florence registered an annual average occupancy rate of 74.4 percent, followed by Rome and Milan, with 72.4 percent and 71.7 percent respectively.

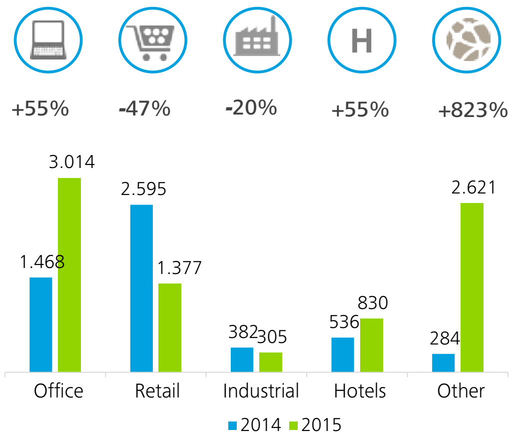
The World Exhibition Expo 2015 Milano concluded in October 2015 and attracted millions of visitors to Milan and Italy, improving the occupancy of many hotels in the Milan area. This positive trend has continued in Rome, thanks to the ongoing Jubilee celebrations that started in December 2015.

Industrial

Investments in the industrial sector in 2015 have been mainly focused on high quality logistic warehouses in target geographical areas such as the north of Italy, where investments in Lombardy accounted for nearly 60 percent of the total investment volume, followed by Piedmont, with 19 percent of the total investment volume.

Prime net yields in Italy in 2015 showed a decrease, from 7.5 percent in 2014 to 6.5 percent in 2015.

Figure 9: Total investment by market segment 2014-2015 (m€) and the variance YoY (percent)



Properties in secondary locations are becoming more attractive, especially within portfolio deals

Figure 10: Prime Net Yields by asset class (Q4 2014-Q4 2015)

Prime Net Yields (%)	Q4 2014	Q4 2015
Office		
Milan	5%	4%
Rome	5.2%	4%
Retail		
High Street Prime	4.5%	3.5%
Shopping Center Prime	6%	5%
Industrial & Logistics		
Prime Logistics	7.5%	6.5%

There is growing demand from retailers, not only for prime centers, with expected influence on the future rental trend

Figure 11: First cities by occupancy rate and changes from 2014 to 2015

Florence -0.6%

Rome +0.3%

Milan +2%

Source: Deloitte on market data

Recent transactions in Italy

Figure 12: Top deals in 2015 and beginning of 2016 by asset class

Asset Class	Property	Location	Buyer	Value (€m - est)	Year
Office	Porta Nuova (office complex)	Milan	Qatar Investment Authority	1.200 (60%)	2015
	Palazzo Broggi	Milan	Fosun Group	345	2015
	Office portfolio (2 buildings)	Milan	Partners Group	233	2015
	Palazzo Turati	Milan	Sofaz	97	2016
Retail / Mixed Use	Via della Spiga 26	Milan	Thor Equities (USA)	164	2015
	La Cartiera shopping center	Pompei	ECE Fund II	132	2015
	Zara store – Corso Vittorio Emanuele 11	Milan	Gruppo Inditex	97	2015
	Palmanova Outlet Village	Palmanova	Blackstone	80	2015
	Trony store - Via Torino	Milan	M&G Real Estate	75	2015
Hotel	Hotel Excelsior	Rome	Katara Hospitality	222	2015
	Gritti Hotel Palace	Venice	Nozul hotels & resorts	105	2015
	Hotel Intercontinental De la Ville	Rome	Katara Hospitality	222	2015
	Hotel Aldrovrandi	Rome	Dogus	90	2016

Source: Deloitte on market data

The majority of deals in Italy in 2015 involved foreign investors