

## Market Views

- analysis and updates from the Norwegian real estate market

January 2024

### Transaction market

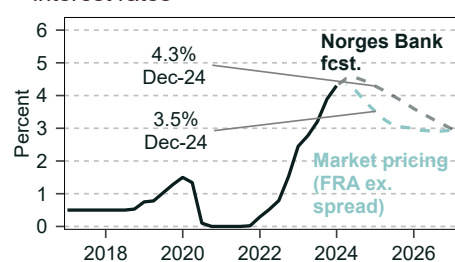
# Increased Liquidity at New Levels

## Macro Insights

### The worst is likely over

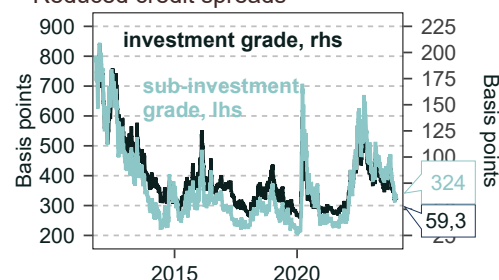
- Although the further decline in interest rates may not be as rapid as market participants have assumed, the worst is likely behind us, both for short and long-term rates.
- Credit spreads have significantly decreased, and banks seem to be easing off a bit.
- Going forward, we expect market sentiment to remain positive.

Moderate decline expected for long-term interest rates



Source: Bloomberg and Norges Bank

Reduced credit spreads



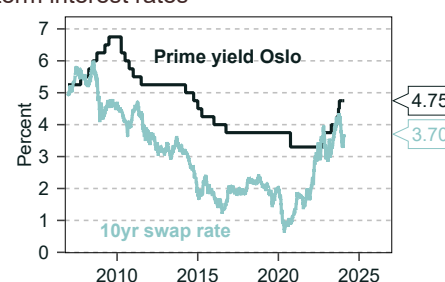
Source: Macrobond

## Commercial Real Estate

### Positive outlook in the transaction market

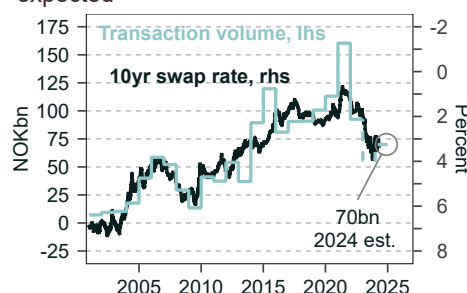
- The consensus that the peak in interest rates has been reached has fostered a positive sentiment in the transaction market as we enter the new year.
- Lower financing costs have provided favourable conditions, allowing us to maintain our yield estimates. Coupled with stable rent price forecasts, we believe that the decline in property values is now levelling off.
- Based on the observed decline in interest rates and the moderately decreasing outlook for long-term rates, we estimate a transaction volume of NOK 70 billion in 2024.

Increased spread between yield and long-term interest rates



Source: Macrobond and Akershus Eiendom

Moderate increase in transaction volume expected



Source: Macrobond and Akershus Eiendom

## Macro | The worst is likely over

Policy rates have most likely peaked in the United States, the Eurozone, and Norway. Both central banks and market participants agree on this. However, there is a clear discrepancy in how quickly and by how much central banks and market participants expect rates to be cut this year. Market participants may have gone a bit too far in anticipating how early and how much the rates will be cut, and recently, uncertainty has spread in the market. The uncertainty has been triggered by stronger-than-expected figures from the U.S. economy, casting doubt on the further decline in inflation and thus how much the central bank will actually loosen monetary policy this year. This has also contributed to the sharp decline in long-term rates slowing down at the turn of the year and reversing somewhat since then.

In the short term, we may see significant volatility in market rates, depending on incoming data.

Nevertheless, it is reasonable to expect that central banks will indeed cut rates this year. In that case, long-term rates should not return to the highs of October last year but are likely to trend moderately downward over the next two years.

Since last autumn, market sentiment has improved considerably. This has manifested itself, among other things, in lower risk premiums in the corporate bond markets. In the European bond market, credit spreads are now approaching pre-pandemic levels. At home, Norges Bank's lending survey indicates that banks may also be starting to ease off a bit.

Although the further decline in interest rates may not be as rapid as market participants have assumed, the worst is likely behind us, both in terms of short and long-term rates. Going forward, we expect market sentiment to remain positive.

## CRE | Positive outlook in the transaction market

Consensus that the interest rate peak has been reached has generated a positive sentiment in the transaction market into the new year. Returns for leveraged structures are approaching normal levels, and in the last month, we have seen "yield gap", the difference between prime yield and long-term interest rates, increase to between 100 and 140 basis points. This appears sufficient for buyers and sellers to meet.

Future yield development will depend on whether interest rates remain lowered. Bloomberg consensus suggests a moderate decline in long-term rates over the next two years. Current market conditions suggest we keep our yield estimates unchanged. Combined with stable rent estimates, we believe the decline in value is now levelling off.

In addition to lowered long-term rates, we also observe lower credit margins in the bond market. A functioning bond market is also expected to have second-round effects, as banks become less concerned about unused revolving credit facilities, thus expecting increased loan capacity in the future. After a period of increased risk and continuously tighter credit practices, we now see examples of somewhat reduced bank margins and increased loan-to-value in certain transactions.

The commercial real estate transaction market is in a better place than it has been the last 18 months.

# The worst is likely over

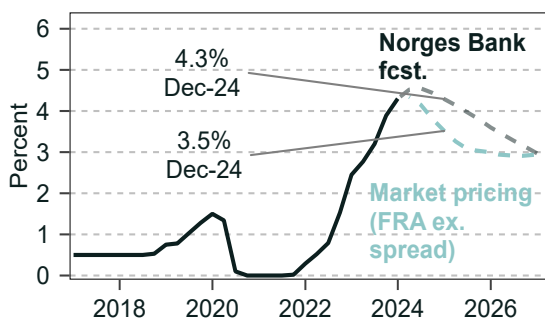
by Kari Due-Andresen - Managing Partner and Chief Economist, Akershus Eiendom

Market participants may have gone too far in expecting interest rate cuts in 2024, and the extensive decline in long-term interest rates has probably been hasty. Nevertheless, the interest rate peak is most likely behind us, which in itself will support market sentiment going forward.

## Interest rate peak has been surpassed

Policy rates have most likely peaked in the United States, the Eurozone, and Norway. Both central banks and market participants agree on this. However, there is a significant discrepancy in how quickly and how much central banks and market participants expect rates to be cut this year. In the U.S., the Fed has signaled up to 3 rate cuts in 2024, while the market expects 5-6 rate cuts. At home, the Norges Bank has indicated that the policy rate could be lowered "in the fall," but envisions only one rate cut this year.

Figure 1: Norway: Policy rate expectations, Norges Bank vs market pricing (FRA)



Source: Bloomberg and Norges Bank

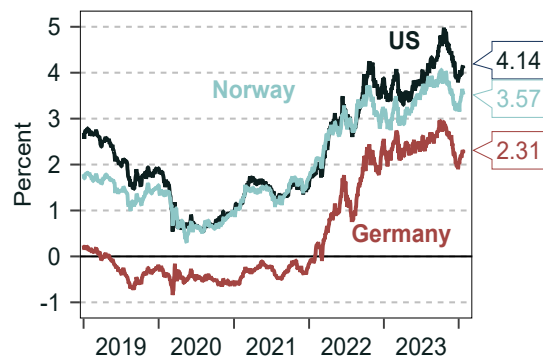
However, pricing in the FRA interest rate market suggests that market participants expect the first rate cut from the Norges Bank in June. Throughout 2024, market participants expect 3-4 rate cuts. This would potentially bring the policy rate down to around 3.5 percent by the end of 2024.

Are market expectations for the policy rate in 2024 realistic? Or have market participants gone too far in anticipating rate cuts? After the turn of the year, some uncertainty has emerged in the market, which has also contributed to affecting long-term market interest rates.

## Long-term rates have fallen rapidly

Long-term rates have fallen significantly since the beginning of the fourth quarter last year. The 10-year Norwegian government bond yield had fallen by nearly 100 basis points at most and was at levels at the beginning of 2024 that analysts last fall did not expect to be reached for another two years. Long-term rates in Norway closely follow international long-term rates, and the rapid and extensive decline in Norway was led by a similar development both in the U.S. and Germany.

Figure 2: 10 year government rates



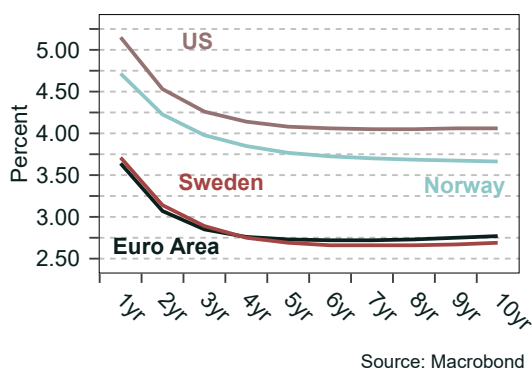
Source: Macrobond

The decline in long-term rates was triggered by signals from the Fed that the central bank envisioned starting to cut the policy rate in 2024. However, recently, the decline in long-term rates has slowed down and reversed. The reason is stronger-than-expected data from the U.S. economy, contributing to uncertainty about the further decline in inflation and thus how much the central bank will loosen monetary policy this year.

Long-term rates likely came down too quickly, and we may see significant volatility in rates in the short term, depending on incoming data. Nevertheless, it is reasonable to expect that central banks will cut rates this year, but perhaps not as much as market participants have expected so far. In that case, long-term rates should not return to the highs of October last year. The market expectation now seems to be a limited decline in long-term rates over the next two years. According to consensus estimates collected by Bloomberg, it is expected that the 10-year government bond yield in Norway will be at 3.3 percent at the end of 2025, thus moderately lower than the current level.

Yield curves have been inverted for a while and still are. If policy rates are cut in the near future, while long-term rates decrease only moderately, it implies that the yield curves will flatten out and eventually have a more normal, upward slope.

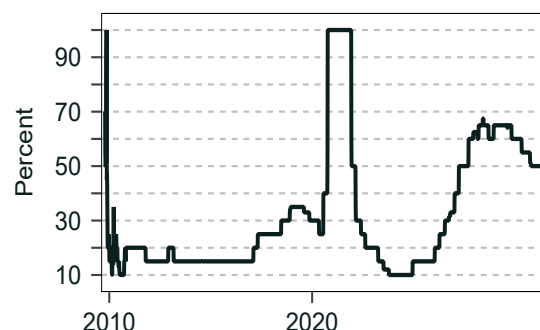
Figure 3: Swap rates



This would be consistent with gradually moving towards more normal conditions in both inflation

and economic activity, both internationally and in the Norwegian economy.

Figure 4: USA: Probability of recession (Bloomberg consensus)



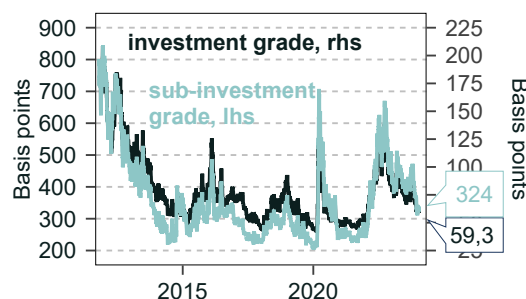
Source: Bloomberg

It also appears that the fear of a global recession, which increased towards the summer last year, has started to diminish. For example, analysts' expectations of a recession in the U.S. over the next 12 months have clearly fallen back after increasing towards the summer of 2023, according to Bloomberg.

## Lower risk premiums and improved sentiment

Since last fall, market sentiment has significantly improved. This has manifested itself in lower risk premiums in the corporate bond markets. Recently, credit spreads for companies with both high (investment grade) and low creditworthiness (sub-investment grade) have fallen considerably in the European bond market and are now approaching pre-pandemic levels.

Figure 5: Credit spreads, 5 years, corporate bonds Europe (ITRAXX)



Source: Macrobond



At home, Norges Bank's lending survey indicates that banks may be starting to ease off a bit. According to the survey, banks' credit practices towards commercial real estate companies were roughly unchanged in the fourth quarter last year, after banks had continuously tightened throughout the previous year.

In summary, it seems that market participants expect a gradual normalization of both the Norwegian and international economies. The path there is probably neither straight nor well-dosed, but nevertheless, the interest rate peak is most likely reached. This means that the worst is likely behind us, both in terms of short and long-

term interest rates. This has, in turn, contributed to lifting market sentiment and lowering credit spreads. As long as there are prospects for policy rate cuts in the coming months, we expect market sentiment to remain positive.



# Positive outlook in the transaction market

by Sindre Vesje Bråtebæk - Senior Advisor, and Even Stølen - Analyst, Akershus Eiendom

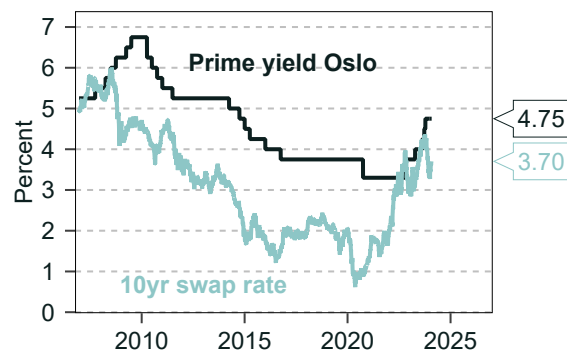
Based on the recent decline in long-term interest rates, there is currently a positive sentiment in the transaction market. Returns for leveraged structures are approaching normal levels, with a "yield spread" between 100 and 140 basis points over the last month. Recently, transactions of stabilised "core" office properties in Oslo have been completed, something we have seen little of since interest rates began to rise in the summer of 2022. The transaction market is in a better place than it has been in the last 18 months.

## Interest down or yield up

Due to the significant rise in interest rates since 2022, property returns have come under pressure. In our transaction analysis from October 2023, we outlined two possible outcomes for improving returns and restoring liquidity in the transaction market. Either long-term rates had to come down significantly, or yields had to rise further for the "yield gap", the difference between yield and long-term rates, to return to historical levels. Since October of last year, interest rates have fallen significantly. At the time of writing, the 5-year swap rate has somewhat increased after falling by a full 120 basis points to 3.40 percent throughout the fourth quarter.

The future development of yields will depend on whether interest rates will remain lowered. If we assume historical covariance, there will still be upward pressure on yields even with a 5-year swap at 3.40 percent. Nevertheless, our assessment is that the decline in interest rates is significant enough for us to keep our yield estimates unchanged since Q4 23.

Figure 1: «Yield gap». Prime yield office Oslo and 10 year swap rate



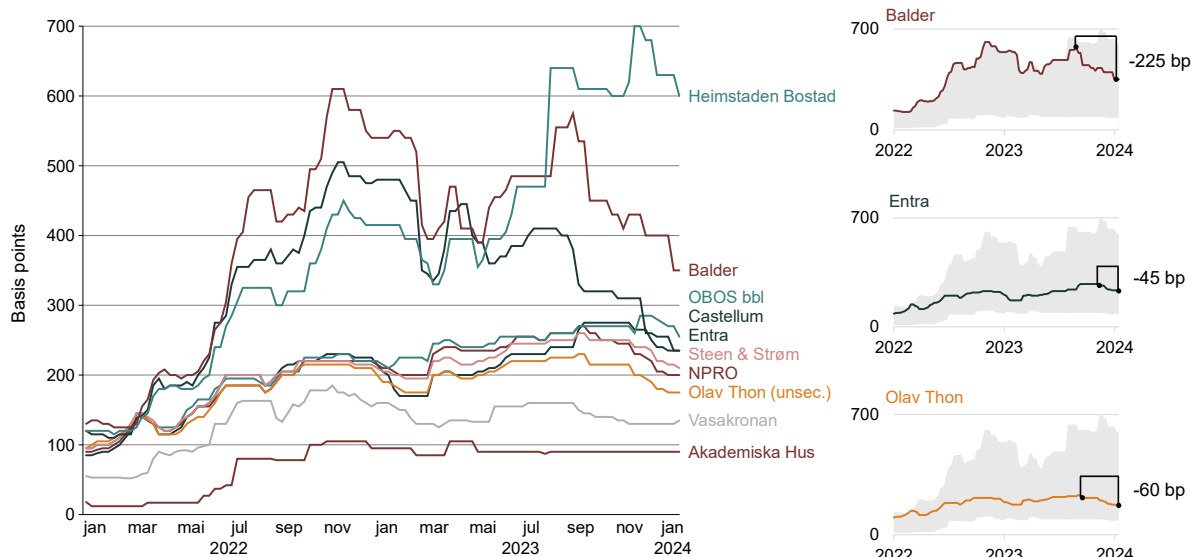
Source: Macrobond and Akershus Eiendom

*"In the last quarter, long rates have fallen sufficient for our yield estimates to remain unchanged."*

## Credit margins down

As mentioned in the macro section, the consensus that the interest rate peak has been reached has also contributed to lower credit margins. After a period of increased risk and tightening credit practices for commercial real estate, we now see examples of slightly reduced bank margins and increased disbursement in certain transactions.

Figure 2: DNB Markets' indicative credit margins for real estate companies



Source: DNB Markets

Indicative credit spreads have tightened in parallel with the declining long-term interest rates. In addition, in recent months, bonds have been issued with lower credit margins than the market expected in advance:

- OBOS, January 2024: 5-year bond of NOK 400 million at 3m NIBOR + 250 bp
- Castellum, January 2024: 5-year bond of SEK 1 billion at 3m STIBOR + 230 bp.
- Balder, January 2024: 2-year bond of SEK 700 million at 3m STIBOR + 200 bp.

In addition to an improvement in real estate and high-yield in general, credit margins on investment grade have significantly tightened. A functioning bond market is expected to have second-round effects as banks become less concerned about unused revolving credit facilities (RCF) and anticipate increased lending capacity going forward.

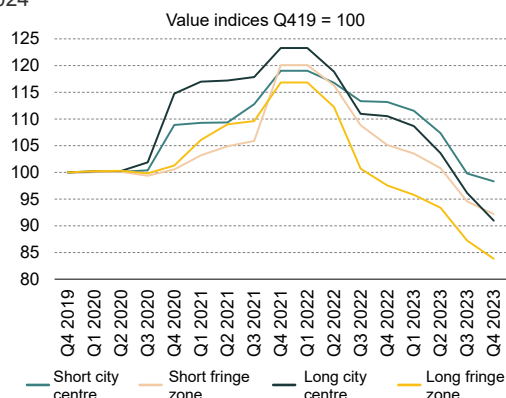
The dual effect on financing costs from falling interest rates and lower credit margins has provided improved conditions for real estate investors.

### Value decline slows down

Due to rate hikes and increasing discount rates, property values have fallen every quarter for the past seven quarters according to our

observations. We believe that this decline will now level off. For a typical office property in downtown Oslo with a short remaining lease term, values are back to pre-pandemic levels, according to our assessments. Prime yield is 100 basis points higher than back then, but strong growth in rents has offset the interest rate effect. However, more interest rate-sensitive properties with a long remaining lease term in Oslo's outskirts have not received the same boost from the rental market. Such properties have experienced the largest value declines according to our analyses. Given flat to slightly declining interest rate outlooks, we expect property values to remain around current levels in the short term.

Figure 3: Akershus Eiendoms' value indices as of January 2024



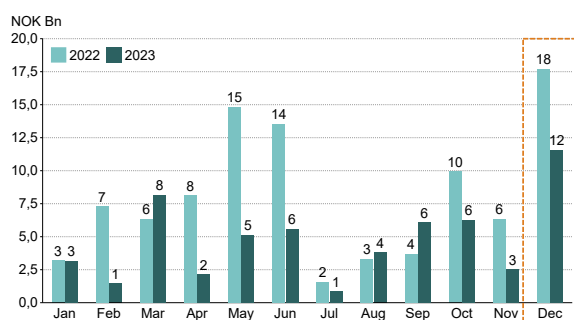
### Looking ahead

Despite today's yield gap of 100-140 bp being 30-50 basis points below historical levels, it



seems to be sufficient for liquidity to slowly return to the transaction market. However, if the historical correlation between long-term interest rates and yield is to hold, we need further interest rate declines for yield to stabilize at current levels. Likely, we need long-term interest rates to fall another 40-50 basis points for yield to be reduced again. Bloomberg consensus suggests, however, that long-term rates will only move moderately downward over the next two years. But even though the yield gap is still somewhat low compared to historical values, we still find that pricing is at a level where it is starting to become interesting to buy commercial real estate again. This is evident in the transaction volume towards the end of last year.

Figure 4: Transaction volume 2022 vs 2023 (Akershus Eiendom)



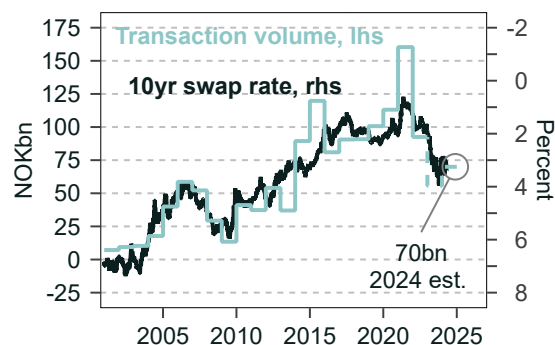
Thus, the supply side becomes pivotal for liquidity in the market. Internationally, we observe several projects that were previously put on hold, now wanting to enter the market before supply increases. At the same time, our international partner, JLL, expects a somewhat slow start to the year in the European commercial real estate market, as it takes time for sellers to structure new sales processes.

In Norway, we experience few forced sales. Credit teams in several Norwegian banks report that they find refinancing risk now more manageable than anticipated. At the same time, we observe several sales from real estate companies and developers wanting to invest in their development pipeline, reallocating capital from their cash flow properties. Capital is thus recycled in the portfolio, rather than expanding

the portfolio with new external capital.

With increased liquidity in the first half of the year, we anticipate a higher transaction volume in 2024 compared to 2023. Historically, there has been a strong correlation between transaction volumes and the 10-year swap rate. Based on the observed decline in interest rates and moderately decreasing prospects for swap rates, we estimate a transaction volume in 2024 of NOK 70 billion.

Figure 5: Inverted swap rates vs transaction volume



Source: Macrobond and Akershus Eiendom

## Conclusion

Lower financing costs due to falling interest rates and reduced credit margins have provided favourable market conditions, and we maintain our yield estimates. With stable rental forecasts for both office and logistics sectors, we expect values to remain at current levels in the short term. The future development of yields will depend on long-term interest rates, with consensus indicating a moderate decline over the next two years. The pricing of commercial real estate is now at a level where investing is becoming attractive again, and liquidity in the transaction market is expected to increase gradually throughout the year.



## Team



Kari Due-Andresen

+47 911 30 526

[kda@akershuseiendom.no](mailto:kda@akershuseiendom.no)



Birgitte Heskestad Ellingsen

+47 481 45 247

[be@akershuseiendom.no](mailto:be@akershuseiendom.no)

*Find our full range  
of analyses by  
clicking here*



Sindre Vesje Bråtebæk

+47 934 25 929

[sbr@akershuseiendom.no](mailto:sbr@akershuseiendom.no)



Kristian Småvik

+47 901 63 303

[ks@akershuseiendom.no](mailto:ks@akershuseiendom.no)



Even Stølen

+47 414 70 962

[est@akershuseiendom.no](mailto:est@akershuseiendom.no)

## Akershus Eiendom

### Address

Ruseløkkveien 30  
P.O. Box 1739 Vik  
NO-0121 Oslo

### Phone

+47 22 41 48 00

### Web

[www.akershuseiendom.no](http://www.akershuseiendom.no)