

Will Office Come Back Into Focus Beyond This Year?

The rise in hybrid working has structurally affected the office demand outlook, in particular in secondary, non-CBD markets that saw take-up fall and vacancy rise. At the same time, low yields came under pressure from quickly rising interest rates, leading to significant value declines and drying up liquidity. As economic growth returns, supporting occupier market performance, and interest rates are cut in 2024, alleviating pressure on values, office investments are set to move back into focus beyond this year.

Looking at economic fundamentals, office productivity growth (the rise in office output per office worker) and office real rental growth have been closely linked in the past. When office productivity rises, the ability for office tenants to pay higher rents

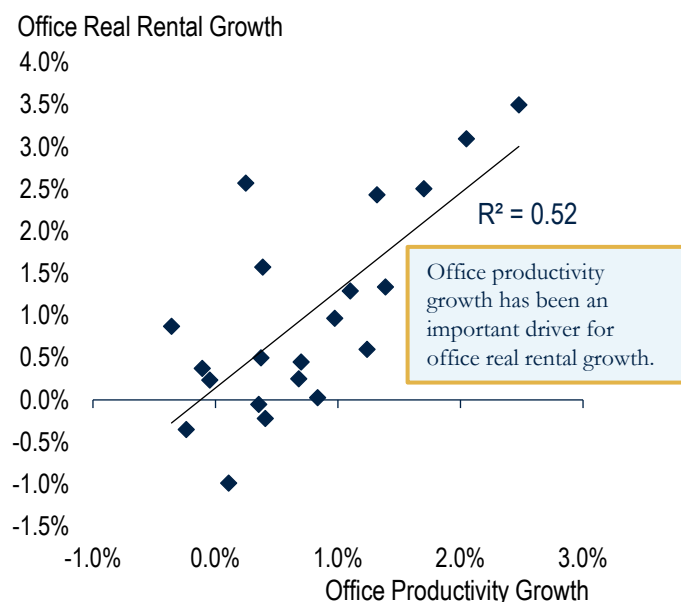
also increases (**Exhibit 1**) and landlords have usually been able to benefit.

With the interest rate outlook changing over the last quarter, forecasts for a pick up in office productivity growth over the next few years are gaining credibility as, among other factors, increased investment in a lower interest rate environment and the rising adoption of AI are forecasted to boost office productivity growth (**Exhibit 1**).

In conjunction with the constraints of prime office availability brought by ESG regulation across European markets, this means investing in office assets in CBD locations promises attractive income growth at potentially mispriced values for core investors.

Exhibit 1: Improving Economic Backdrop Will Drive Opportunities Beyond 2024

City Office Productivity Growth versus Office Real Rental Growth (1996 – 2023)



City Office Productivity Growth (2020-24 versus 2025-29)



Sources: Oxford Economics, PMA, Cushman & Wakefield, PGIM Real Estate. As of February 2024.

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