DNB NÆRINGSMEGLING

MARKET REPORT

2. half-year 2017

Christian Kroghs gate 32

Sale assignment on behalf of Anthon B Nilsen Eiendom and OBOS Forretningsbygg

DNB NÆRINGSMEGLING AS

DNB

DNB Næringsmegling

We are one of the country's leading commercial real estate brokers and the only one with offices in the four largest cities. We can provide support with analysis and valuation, advice, letting and the sale/purchase of commercial property. Our team have extensive experience and a broad range of expertise and their work will be dedicated to finding the best solution for you as client.

TRANSACTIONS

Our experienced team can provide support through the entire process of buying or selling commercial property, tailored to our clients' preferences. We have a very good understanding of the investor market within commercial property.

LETTING

Our brokers can find good and value-creating solutions for clients and tenants. We focus on the letting of office premises, warehouses and combination properties as well as retail premises.

ANALYSIS

Whether one is looking to develop, buy/sell or let commercial property, there are often substantial values involved. We offer high-quality advice and analysis which considerably increases the likelihood of success. Since establishment in 2003 we have closely followed the market and built-up extensive know-how and a comprehensive set of databases.

VALUATION

In a steadily more professional property market there is an Increasing need for external property valuation. We have long experience in carrying out valuations, whether these are of portfolios, individual properties or development projects. We are one of the largest and most recognised participants in the market.

The only constant is change

Anne Helene Mortensen
CEO, DNB Næringsmegling

Welcome to our latest market report which is filled with relevant commentary, updated forecasts and market data. We started the autumn with a new approach to our autumn seminar with all the various property teams in the DNB group inviting guests to a property conference held on 19 September. More than 400 clients and investors were present and as many as ten company presentations were held, in addition to several analysis presentations from macro to micro. The conference concluded with a very interesting panel discussion about the future structure of retailing, which is also relevant to our market. The conference was so well received that we wish to repeat the success next autumn. Reserve 20 September 2018!

We are already in the last quarter of 2017 and can look back on a very active year so far, as well as being well aware that history shows that a great deal happens in the last three months of the year. Norway is still regarded as an attractive market and is considered predictable in many respects. Many indicators are pointing in the right direction, including a healthy development in the Norwegian economy and rising rent levels in the most important individual segment, offices in Oslo. In spite of expectations of rising long interest rates, a relatively low interest rate level in the coming years will contribute to commercial property continuing to be an attractive asset class.

The transaction market is still characterised by a high level of demand, and many investors are taking more risk both to acquire property in general and in order to obtain a good return. This has also been more noticeable in the larger cities outside Oslo, and we find that the combination of DNB Næringsmegling's local and national expertise has been particularly relevant. Several leading clients on both the buying and selling side have stated that the interaction they experience between local and national expertise is a big advantage.

In addition, we are seeing new and higher requirements from tenants. We regularly encounter new approaches and solutions and can be certain about one thing: the right answer is changing and we can be sure that the "ideal office" of 2027 will look completely different from that of 2017. We therefore find that a relatively conservative sector, such as the property sector, is more curious and becoming more open to change in response to new expertise, new demands, new and stricter environmental requirements as well as digitalization. The philosophy that Heraclitus propounded in 500 BC: "The only constant is change" is as relevant today as ever.

We will be following developments closely, but first and foremost look forward to an active last quarter with our customers and partners.

Contents

Munkedamsveien 45, «Vika Atrium», letting assignment on behalf of Thon Eiendom

Summary

2017 has been a good year for investors with growth in values as a result of falling yields and rental growth in several segments. Our investor survey shows that investors are optimistic with regard to the Oslo market and expect yields to continue to fall and rents to continue to rise. A majority intend to increase their investments in commercial property, while investors are divided in their views with regard to logistics and retail property.

DNB Markets macro forecasts suggest that commercial real estate will have good conditions in the coming years, but that the outlook for returns on investments has weakened. The fact that GDP growth and employment is ticking up is positive for rental markets, but lower CPI growth and upward adjustments in interest rate forecasts point in the opposite direction. The 10-year swap rate is expected to rise by 90 basis points from 2016 to 2019.

In general yields have continued to fall this year, particularly for properties with long leases. We consider that the sales of the Barcode buildings Midtbygget and Eufemia earlier this year confirm indirectly that the prime yield stands at 3.75%. With the prime yields levelling out we now see a two-way movement in yields. The spread against other clusters and segments is being reduced, at the same time as the spread internally in the office clusters in Oslo is increasing by reference to the distance from public transport hubs.

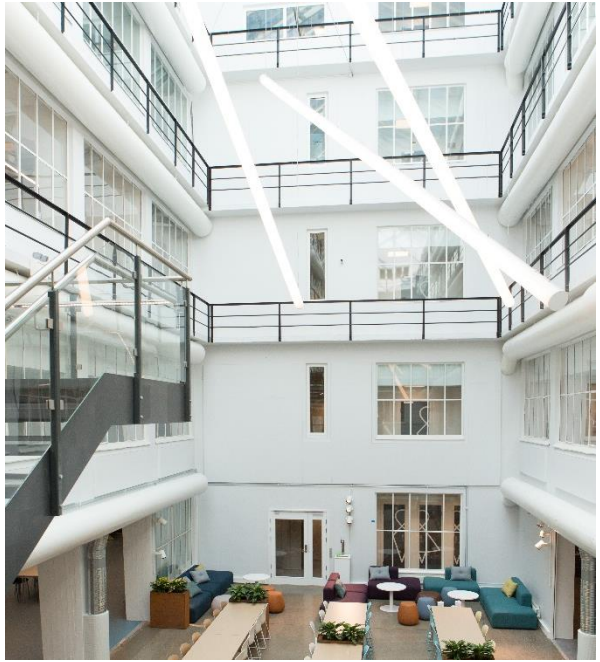
Currently many large properties are in play and if the fourth quarter proves to be in line with last year we will end 2017 with the second highest transaction volume on record at NOK 85 billion, and a record number of 285 transactions.

Office vacancy in the Oslo area has fallen from 8.2% last winter to 8.0%. We still expect a high level of conversion to housing but have reduced our forecast for 2017–2019 from 240,000 to 195,000 m². In addition, we have adjusted upwards our forecasts for new building and demand. In total our forecasts indicate that vacancy will fall to 6.7% by the end of 2019. We expect overall growth in market rent levels of 14% for the current three-year period. We have adjusted our growth expectations downwards due, among other things, to the fact that we have put greater weight on new buildings outside the centre acting as a brake on rental growth.

In Bergen, Trondheim and Stavanger we have recorded 42 transactions this year with an aggregate value of NOK 10.4 billion. Measured by value, investors from outside the respective cities have accounted for 60% or more of the acquisitions in all three cities. In Bergen and Trondheim yields are trending lower for both prime and “normal” property, and we have made a downward adjustment of our yield forecasts. We have also made a downward adjustment of the prime yield for offices in Stavanger, but maintained our yield estimates for normal property.

Christian Kroghs gate 32

Sales mandate on behalf of Anthon B Nilsen Eiendom and OBOS Forretningsbygg



Summary

Office vacancy in the three cities varies from 9.0% in Trondheim to 11.5% in Stavanger. In all three cities vacancy is significantly lower in the centre. In Bergen, we expect that conversion to housing will contribute to a slight downward trend in vacancy. Rents are in the process of bottoming out in the peripheral zones and we expect weak growth in the city centre. In Trondheim the high level of new building will contribute to vacancy rising to 11.5% at the end of 2019. We expect slightly falling rents in the peripheral zones and slightly rising levels in the city centre. Our forecast indicates that vacancy in Stavanger will increase from 11.5% today to 15.0% at the end of 2019. Since 2014 there has been a marked fall in rents and we expect a levelling out in the future.

Retail: There has been a broad range of transactions and these have included four sales totalling NOK 1.6 billion involving car showroom properties. The British firm DCC Energy invested NOK 2.4 billion in petrol stations and another British firm Via Outlet bought Norwegian Outlet at Vestby for NOK 1.1 billion. Shopping centre turnover has only risen by 1.4% so far this year, while the online sale of goods is expected to grow by 21% this year to NOK 33 billion.

Logistics: There is strong buyside interest for logistics properties. Many investors expect growth in values, others consider that logistics is overpriced. Based on individual transactions we have adjusted downwards our estimate for prime yield by 50 basis points to 4.75%. This year we have registered five transactions with yields of 5.5% or lower and eight different club-deal arrangers among the buyers.

Hotels: So far this year we have only registered seven sales for a total of NOK 1.2 billion. Among the four largest cities only Bergen has experienced a fall in RevPAR. Oslo has experienced the strongest development in key figures and average room prices passing NOK 1,000 in the first half year.

Housing: Several participants in our investor survey stated that they would give priority to commercial property ahead of housing. Nevertheless we find that interest remains high for properties suitable for conversion to housing, both in Oslo and Bergen. DNB Eiendom expects that secondary house prices in the capital will bottom out during the autumn and new building prices in the coming winter.

Macro and loan financing	2016	2017E	2018E	2019E	2020E
GDP Mainland Norway	0.9%	2.0%	2.0%	1.9%	1.9%
CPI	3.6%	2.1%	1.6%	1.4%	1.5%
Employment	0.3%	0.4%	0.9%	0.9%	0.9%
Private consumption	1.6%	2.1%	2.1%	2.2%	2.3%
House prices	8.3%	5.7%	-2.5%	1.0%	2.0%
3m NIBOR	1.0%	0.9%	0.9%	1.0%	1.4%
10y SWAP	1.6%	2.0%	2.2%	2.5%	2.5%
Typical credit cost***	3.4%	3.9%	4.2%	4.3%	4.6%

Office market	Prime yield	Prime rent	Office vacancy	Forecast rents	Forecast vacancy
Oslo and Akershus	3,75 %	4 200	8,0 %	↗	↘
Bergen	4,75 %	2 700	9,3 %	→	↘
Trondheim	5,00 %	2 400	9,0 %	→	↗
Stavanger	5,25 %	2 600	11,5 %	→	↗

Transaction market	Key factor	2016	2017	Prime yield Oslo****	Volume, bn. NOK (number)
Office	Employment	0.3%	0.4%*	3.75%	24,0 (59)
Retail	Shopping centre turnover	1.7%**	1,4%**	3.75%	10,6 (31)
Logistics	Top rent, warehouses	1 200	1 200	4.75%	6,8 (38)
Hotel	RevPar Norway	492	503	4.00%	1,2 (7)

* Forecast 2017 (DNB Markets) ** Adjusted for space changes. 2017 so far this year . *** 5Y SWAP + margin **** 7-year lease for offices, and 12-year lease for logistics properties and hotels

Source: DNB Markets, SSB, and Kvarud Analyse

Hedgehaugsveien 21

DNB Næringsmegling handled the transaction on behalf of a private investor

Oslo

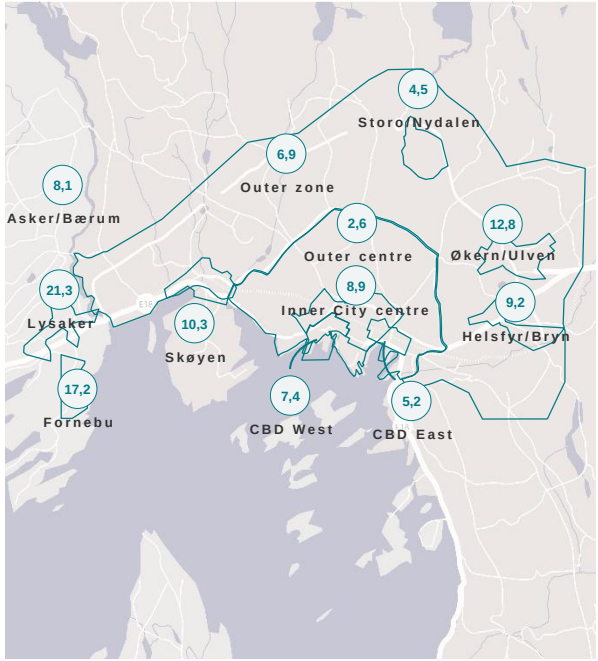
Thomas Ramcilovic
Analyst, DNB Næringsmegling

The office market in Oslo, Asker and Bærum has largely moved on from the oil price crash, we expect vacancy to continue to drop and an increase in market rents

Prime Yield	Since Q1-17	Prime Rent	Since Q1-17	Office vacancy	Rent forecast	Vacancy forecast
3,75 %	Unchanged	4 200	Unchanged	8,0 %	↗	↘

- **Office vacancy is down 0.2 percentage points from the first half year to 8.0% and is estimated at 6.7% at the end of 2019**
- **We expect that market rent levels for high standard offices will rise by around 13% in the city centre and the office clusters in the period 2017–2019.**
- **A reduction in the conversion of office premises to housing is expected**

Office vacancy Oslo Q3 in percent



Snarøyveien 36

Letting assignment on behalf of Akastor

Main features - continued fall in vacancy, growth in rents

- Office vacancy is slowly falling and rents are rising.
- Vacancy is expected to fall further, but level out in 2018 and 2019.
- Access to public transport is more important for tenants.

For the fourth half year running office vacancy fell in Oslo, Asker and Bærum. The reduction in vacancy was moderate, from 8.2% in the first half year to 8.0%. We expect a further fall in vacancy driven by relatively good demand and a low net supply of capacity.

An increase in the supply of new buildings towards the end of the forecast period is expected to restrict the fall in vacancy, which we have adjusted slightly down since the previous half-year report. A reduction in the space converted from offices to housing is expected to have similar effect. This reduction can be attributed to a slowdown in house price growth, while the growth in Oslo in recent years has meant that a number of the most suitable conversion properties have already been taken out of the market.

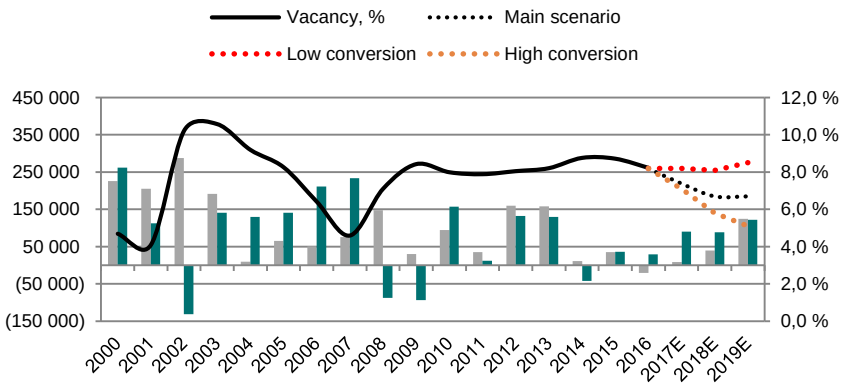
Demand – Growth in the Norwegian economy and optimism among companies is contributing to increased demand

The slowdown following the oil price crash appears to have come to an end and there is rising activity in the Norwegian economy. Growth in 2015 and 2016 slowed considerably as a result of a substantial fall in petroleum investments, but has increased in 2017 and a growth rate above the "normal" level looks likely for the current year.

NAV's business survey for Oslo 2017 shows that a majority of companies in the capital expect to increase their work force, the main exception being public administration – an office-intensive segment where a majority reported an expected reduction in employment.

In addition, estimates from NAV Oslo also show that the population of working age in Oslo is expected to increase by 1.6% in 2017. Net commuting to Oslo is also expected to increase a little. NAV Oslo forecasts employment growth in Oslo in 2017 of 1.6%, admittedly with a relatively large element of jobs with low office utilisation, such as construction.

Office vacancy



	Good standard	High standard	Forecast, high stand. growth	Vacancy Q3 2017	10 largest vacant/ vacancy
Asker/Bærum	1 200 - 1 500	1 500 - 2 000	1 %	8 %	62 %
Lysaker	1 400 - 1 800	1 800 - 2 250	3 %	21 %	66 %
Fornebu	1 300 - 1 500	1 500 - 1 850	0 %	17 %	94 %
Skøyen	1 800 - 2 450	2 450 - 2 950	7 %	10 %	71 %
CBD West	2 400 - 2 800	2 800 - 4 200	6 %	7 %	53 %
Inner City Centre	1 850 - 2 700	2 700 - 3 300	6 %	9 %	38 %
CBD East	2 100 - 2 600	2 600 - 3 300	6 %	5 %	99 %
Outer City Centre	1 550 - 1 900	1 900 - 2 500	3 %	3 %	64 %
Storo/ Nydalen	1 400 - 1 900	1 900 - 2 300	6 %	4 %	82 %
Økern/ Ulven	1 300 - 1 700	1 700 - 2 200	2 %	13 %	96 %
Helsfyr/ Bryn	1 300 - 1 750	1 750 - 2 100	4 %	9 %	73 %

Source: DNB NM/SSB/NAV

Supply – Reduction in conversion to housing

During the recent years' very strong housing market it has been attractive to convert office space to housing. This has been particularly relevant at locations outside the most sought-after clusters, where it has been more challenging to attract tenants at good rent levels. With the slowdown in the housing market investors have become more cautious about conversion properties. Furthermore, many suitable properties have already been converted. Conversion projects often have cash flow for some years and thus lead to an effect in the future if investors awaits investments today. In addition, expectations of increased rents and falling vacancy are making office rental more attractive relative to housing development.

Based on the above we have reduced our estimate of conversion by a total of 45,000 m² for 2018 and 2019. The conversion rate will affect vacancy as the graph [on the previous page] shows. Without any conversion in the forecast period (Low conversion) vacancy would increase to 8.5% in 2017. With 120,000 m² converted annually from offices (High conversion) vacancy would fall to roughly 5%.

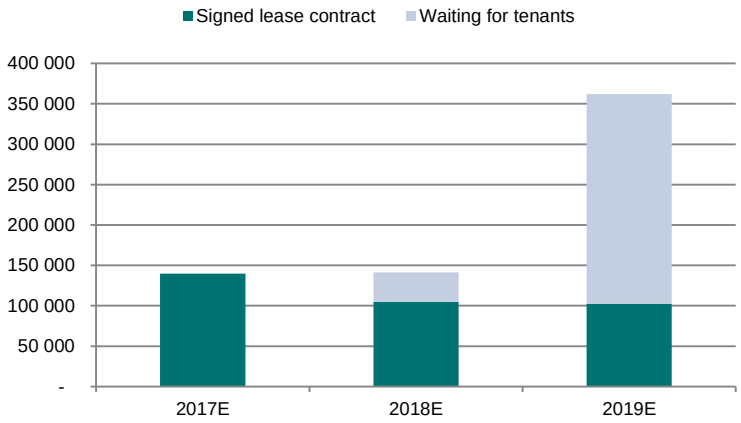
New building

New building will mean that capacity in the market increases towards the end of the forecast period and will contribute to vacancy levelling out in 2019. We note that a large proportion of the largest tenants wish to move to new buildings, 7 of the 10 largest searches last year ended with leases in new buildings. This naturally leads to vacancy in the premises that are vacated.

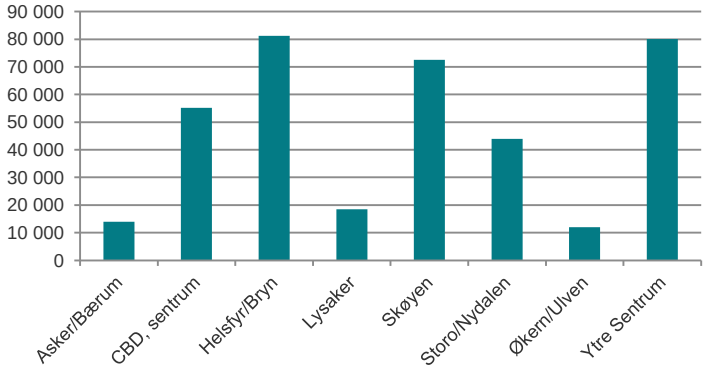
In recent years new building projects have provided the office market with less capacity than the historical average of 120,000 m² a year. In 2017 and 2018 completed new buildings will amount to around 100,000 m² a year, while in 2019 considerably more and larger projects will be completed, which will increase the supply-side and contribute to the fall in vacancy levelling out.

Skøyen, Storo/Nydalen and Helsfyr/Bryn are areas where major new building projects will be completed in the coming years.

New building volume 2017–2019



New building volume 2017-2019



Searches – The high volume continues in 2017

There is still a high level of activity in the office rental market and the number of searches as of 1 October 2017 was already close to the total figure for 2016. In 2016 we registered some 200 searches, which is roughly the same as the number so far this year. The searches in 2016 amounted in total to more than 350,000 m², while the corresponding volume at the start of October this year was around 325,000 m².

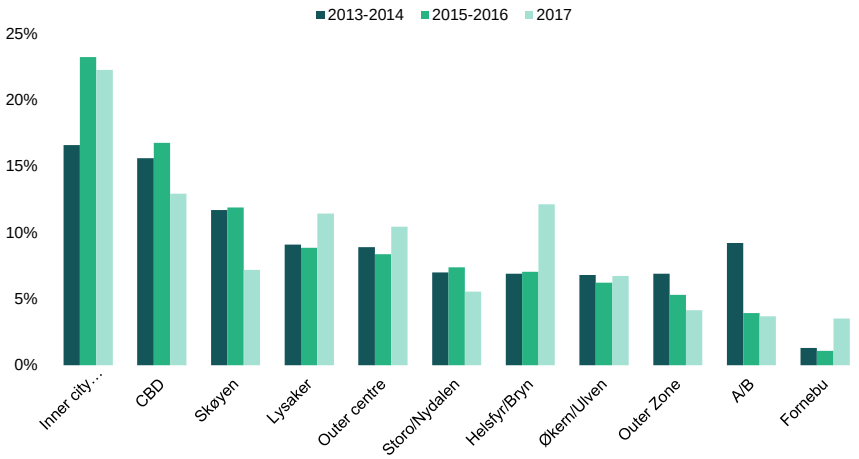
There are still by far the most searches for locations in the Inner City Centre, which together with the Outer Centre also has by far the most office space out of the defined areas. The areas with the highest search volume so far in 2017 in relation to the total office space are Økern/Ulven, Lysaker and Helsfyr/Bryn. With regard to Økern/Ulven search volumes are characterised by individual large searches, with Statsbygg, among others, as search broker. This year Helsfyr/Bryn has had the highest increase in the share of search volume compared with the last couple of years.

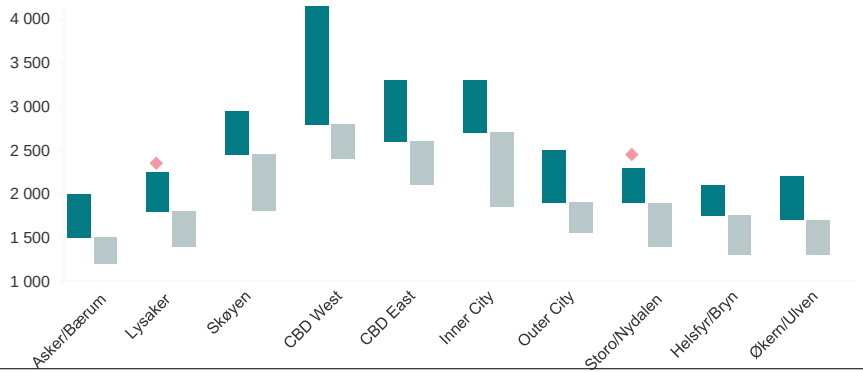
The highest search volume in square metres so far in 2017 in relation to vacancy has been in CBD East (the Bjørvika district). This is the only area where searches in square metres so far this year have been higher than the vacant space. We recorded the lowest search interest in relation to vacant space in Asker/Bærum, the Outer zone, the Outer centre and at Fornebu.

Searches so far this year support the impression that the city centre and office clusters with good public transport connections are the most attractive areas.

A trend from recent years is that the largest searches have often ended with leases in new buildings. In the case of public sector tenants, locations outside the city centre with lower rents and proximity to public transport are often preferred to city centre locations.

Searches in the period 2015–2017 measured in square metres





Market rents - Continued growth

Arealstatistikk's figures for the second quarter of 2017 show that rents rose a little further from the low point in early 2016, the market thus appears to have moved on from the oil price crash. The six-month rolling average rent stands at NOK 2,050 per sq. metre per year, which represents a rise of some 11% from the low in Q1 2016.

We forecast further growth in market rents. The central areas and the office clusters are expected to see cumulative growth of around 14% for the period 2017–2019. Lower vacancy will contribute to price growth, at the same time we have reduced the reduction in vacancy and price growth slightly since the previous report.

We expect that price growth will be uneven. The highest growth by 2020 is expected in the city centre and CBD in line with high demand and the current moderate vacancy. The same mechanisms will contribute to price growth in clusters with good access to public transport and short travel time to the city centre.

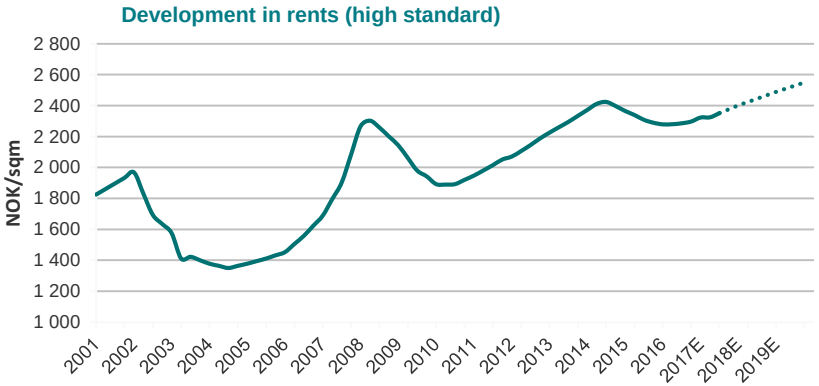
The weakest price growth is expected in locations outside the centre and in areas with limited public transport provision. At Fornebu where vacancy has been high for some time and where public transport to the centre of Oslo is poorer than for many of the other established areas, we expect a flat price development in the forecast period.

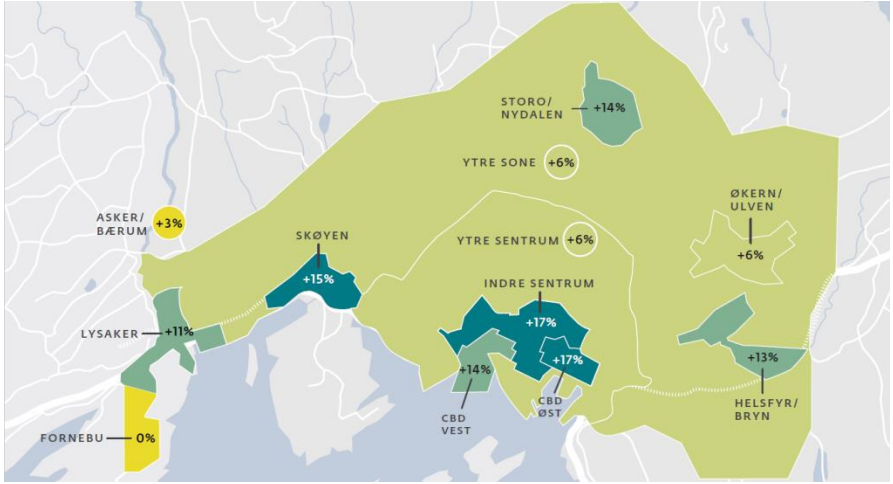
The following drive price growth:

- A rising market after the oil price crash
- Premises with a high standard close to public transport hubs and new buildings are preferred.
- Lower vacancy

We have nevertheless adjusted our price estimate down slightly due to the following:

- The fall in vacancy is expected to take place more slowly and be less than previously forecast.
- New buildings outside the city centre are preferred by large public sector tenants achieving prices at market average.
- Somewhat less demand than previously for the most highly priced area - CBD West - based on recorded searches.





Philip Pedersens vei 20, Lysaker

Letting assignment on behalf of Oslo Areal

The transaction market

Gunnar Selbyg
Head of Research
DNB Næringsmegling

Demand-driven fall in Norway in the short term, interest-driven yield increase from 2019

Prime Yield office Oslo	Forecast Q4 2018	Trend normal yield	Expected credit cost	Value development offices in Oslo	Forecast volume 2017	Bergen, Trondheim, Stavanger 2017
3,75 %	3,85 %	↘	→	→	NOK 85 bn./280 transactions	NOK 16 bn./60 transactions

- **Approaching the second highest transaction volume on record**
- **Leading investors still intend to be net buyers**
- **Clear differences in investors' views on logistics and retail**
- **Two-way movement in yields in the Oslo office market**

Skoggata 19, Moss

DNB Næringsmegling handled the transacion on behalf of Cleaves Marine Finance

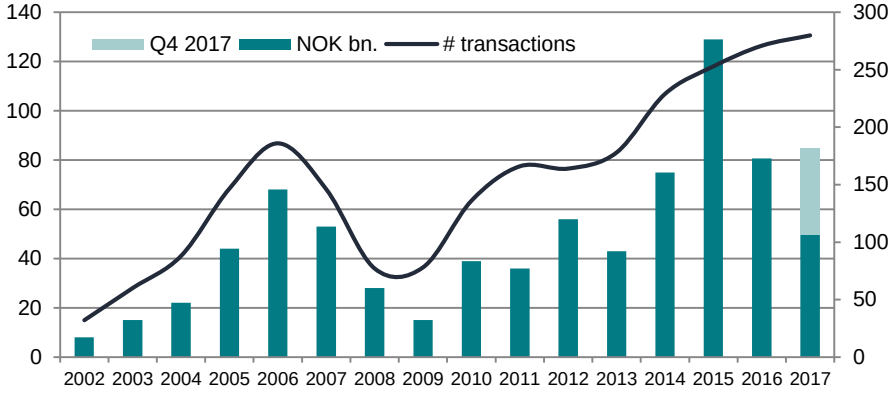
Towards the second-highest transaction volume on record There is currently a high number of ongoing processes involving large properties. If we assume a fourth quarter in line with last year, we will end 2017 with a transaction volume of around NOK 85 billion and a record number of 285 transactions.

Leading investors are looking to increase their volume of commercial property

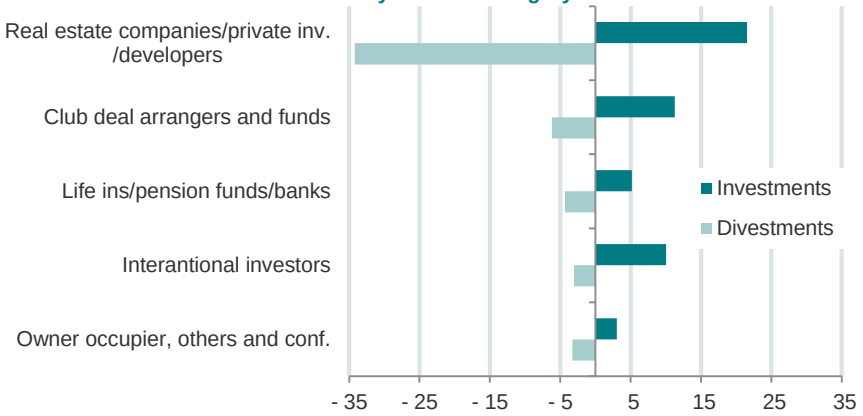
Our survey at the end of August shows that as many as 13 out of 25 aim to be net buyers in the coming year and only 3 out of 25 expect to be net sellers. Assuming the market continues to be characterised by surplus demand, the survey suggests that the large Oslo-based investors will increase their market share in Oslo and the other main cities at the expense of smaller local investors. Another factor that may mean there will be many sellers in the future is that developers are under-represented in the survey. We expect there will still be many transactions related to a strategy to sell developed property, and that many investors will sell property to refine their portfolios.

International investors back as the largest net buyers. The newly established Swedish company SBB Norden, which did large acquisitions in Kristiansand and Nydalen last year, this year followed up with the acquisition of DNB's Midtbygget in Bjørvika for NOK 4.3 billion. In addition, four international investors have made their first investments in Norway. The Finnish private equity fund CapMan Nordic Real Estate bought St. Olavs gate 23 from an Aberdeen fund and has indicated its intention to make further acquisitions in the Oslo region for around NOK 2 billion. The British DCC Energy has bought petrol station property for NOK 2.4 billion, the British Via Outlet has bought Norwegian Outlet Vestby for NOK 1.1 billion and the Swedish Bonava has bought land in Bergen and Askøy. Developers, private investors and property companies are still the largest net sellers. Measured by number however they have bought and sold as many properties (108) so far this year. Club-deal arrangers have been the second-largest net buyers. They have nevertheless completed at least 24 sales for NOK 6.2 billion this year, and "only" four of the seven arrangers interviewed expect to be net buyers in the coming year..

Annual transaction volume measured by number (right hand axis) and value



Transaction volume in 2017 YTD by investor category – NOK bn.



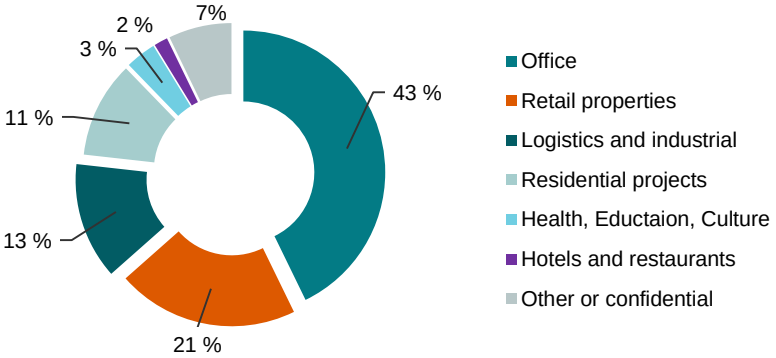
Continued high level of interest for housing related properties Over 20 investors have bought housing related property so far this year for a total of NOK 5.6 billion. In addition, there is a large number of properties where conversion to housing is probable in the longer term. Several investors stated that they now wish to give priority to commercial property, but in several sales processes we have experienced strong interest for properties suitable for conversion to housing - preferably close to hubs for public transportation.

Many investors think alike, but there are differing views on logistics and retail The fall in yields has been fully passed on to logistics, where we have adjusted downwards our estimate for the prime yield to 4.75%. Several investors are sceptical about the segment and believe that it is overpriced due to the re-letting risk, low land values and the fact that it is cheap to build new. “Supporters” of logistics point to the low alteration costs for new tenants, the limited downside in rent levels and the fact that large unexpected costs are rare, and that growth in online shopping creates an additional need for warehouse property close to the main cities.

The key to what differentiates investors is how large a risk premium one should have, or how much more positive and solid the cash flow should be to compensate for the fact that the land value is low in relation to the acquisition price and loan value. In the case of a centrally located property there is a greater range of potential tenants and the property can be used in several ways. In the case of a warehouse property that lacks a central location one risks owning a property that is difficult to let when a tenant relocates.

Retail property is another segment that divides investors. The key here that divides investors is how dramatic one believes or fears the consequences of increased online shopping will be in the long term. Those who believe that retail property is overpriced point to the low growth in retail turnover in recent years. Big boxes represent a sub-segment within retail that can be compared to logistics in that it is cheap to build new, the land value tends to be low and alternative use possibilities are often limited. Several investors therefore prefer centrally located retail property.

2017 volume YTD measured in value divided by segments



Number of transactions per value range

NOK mill.	# 2017 YTD	# 2014-2016
50-149	88	331
150-299	54	202
300-999	34	175
1.000 +	9	50
Total	**185**	**758**

Strong transaction market in Oslo/Akershus At the start of the fourth quarter we had registered 100 transactions for NOK 30.8 billion in Oslo/Akershus against NOK 23 billion in 75 transactions at the same time last year. At least 28 transactions have had a value of NOK 300 million or more and the Oslo area has had a higher share of the national total than last year.

Falling yield trend in Europe In the years 2014–2016 international investors accounted for 24% of the investment volume in Norway and were behind most of the acquisitions with yields below 4 %. Several international investors have been in the forefront of the yield development and contributed to the downward pressure on yields. In the context of the development in yields in Norway it is thus relevant to note that yields have continued to fall in Europe during 2017. Data from Knight Frank for 26 European markets shows that the prime office yield fell in a majority of the cities by 25 to 50 points during the first half 2017. None of the cities experienced a rise in yields and the average for all cities was a 14 point fall. Correspondingly none of the markets had an increase in the prime yield for logistics and 18 out of 26 cities saw a fall in the first half year. On average the level was down by 26 basis points. The table shows a selection of European markets and four largest cities in Norway arranged by the yield gap for prime offices based on the 10-year swap rate. From a European perspective Norwegian prime property appears to be aggressively priced in relation to the cost of credit. If we also adjust for higher credit margins in Norway, the yield gap (prime yield minus credit cost) suggests the Norwegian prime property is priced to be among the most secure (solid economy and politically stable) and the most attractive in Europe.

Investors expect a stable prime yield and falling normal yield for offices in Oslo Only 2 out of 25 investors expect a further decrease in the prime yield, one investor expects a rise and as many as 88% expect a stable development in the coming year. 17 out of 25 investors expect however a continued falling yield trend for “normal” office property, which in our definition is a property with 4–5 years remaining on its leases, an acceptable location in one of the clusters on the Oslo Outer ring-road, a good standard and ordinary companies as tenants.

Number of transactions in Oslo/Akershus by value range

NOK mill.	# 2017 YTD	# 2014-2016
50-149	43	157
150-299	29	105
300-999	22	112
1.000 +	6	25
Total	**100**	**399**

Yield levels for Norwegian and European cities arranged by gross yield gap

Offices	Prime yield	10-års swap	Spread
Brussels	4.75%	0.91%	3.84%
Dublin	4.50%	0.91%	3.59%
Milan	4.25%	0.91%	3.34%
Amsterdam	4.00%	0.91%	3.09%
Helsingfors	4.00%	0.91%	3.09%
Stavanger	5.00%	1.99%	3.01%
Madrid	3.90%	0.91%	2.99%
Copenhagen	4.00%	1.10%	2.90%
Trondheim	4.75%	1.99%	2.76%
Geneva	3.00%	0.31%	2.69%
Zürich	3.00%	0.31%	2.69%
Bergen	4.50%	1.99%	2.51%
Hamburg	3.30%	0.91%	2.39%
Berlin	3.25%	0.91%	2.34%
Stockholm	3.50%	1.27%	2.23%
London West End	3.50%	1.41%	2.09%
Paris	3.00%	0.91%	2.09%
Oslo	3.75%	1.99%	1.76%

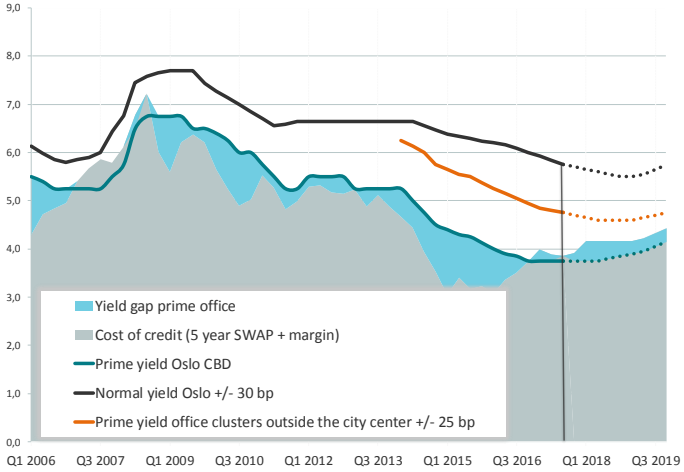
Source: Knight Frank – «European quarterly commercial property outlook»

Two-way yield movement for offices in Oslo Our definition of prime yield is based on a seven-year lease and we consider that the sales of Midtbygget and Eufemia earlier this year indirectly confirm the prime yield at 3.75%. The yield spread against other locations is decreasing and is generally also decreasing for office properties with shorter leases. We see this in the context of the office rental market improving and the difference between yield and credit cost has been particularly high for "normal" property. At the same time there has been a parallel yield movement internally in the office clusters where the yield spread is increasing with the distance from public transport hubs. Increasingly investors state that they put more emphasis on the distance from public transport. Properties that are situated close to stations obtain a higher value both from a higher rent level and through a lower yield which reflects a lower letting risk.

Demand-driven yield fall in the short-term, interest driven yield increase in the longer term On a purchase of a prime office with normalized credit costs the yield gap is currently negative and illustrates why most investors can't buy property in the CBD areas. A solid market participant that today buys with a 50 basis points more favorable credit margin than the market and with half the loan fixed through a five-year swap and half the loan floating has a credit cost of around 3.1%. Several buyers also fund themselves in the bond market at a cost of around 3%. Expectations of rental growth and continuing surplus demand are good arguments for a continued fall in the prime yield. We have however given greater weight to the tight yield gap, weaker CPI growth and gradually rising long term interest rates. Our forecast involves the prime yield rising by 40 points from the end of next year to the end of 2019. In the case of other segments, we expect that excess demand will continue to press yields downwards in the coming year. DNB Markets estimates that the 10-year swap rate will rise by as many as 90 basis points from 2016 to 2019, and that rising credit costs will be reflected in generally slowly rising yields towards the end of the forecast period

Generally falling yield trend We have once again adjusted downwards a number of our yield forecasts, and particularly for properties with long leases the fall in yields has been noticeable this year.

Yields, yield gap and credit cost for offices in Oslo 2006-2019



Yield levels in the various property segments in the four largest cities

Q3 2017	Oslo/Akershus	Bergen	Trondheim	Stavanger
Prime yield offices*	3.75%	4.75%	5.00%	5.25%
Normal yield offices	+/- 5.75%	+/- 6.75%	+/- 6.75%	+/- 7.50%
Prime yield retail	3.75%	4.75%	5.00%	5.25%
Normal yield retail**	+/- 6.25%	+/- 7.00%	+/- 7.00%	+/- 7.50%
Prime yield logistics***	4.75%	5.75%	5.75%	6.25%
Normal yield logistics	+/- 6.50%	+/- 7.25%	+/- 7.25%	+/- 8.00%
Prime yield hotels ***	4.00%	5.00%	5.25%	5.50%

** Offices 7-year lease, ** Retail outside the city centre, *** Logistics and hotels: 12-year leases*

Økernveien 97-99, Oslo

DNB Næringsmegling handled the transaction on behalf of Bavaria Eiendom Bil

Øyrane Torg, Bergen

DNB Næringsmegling worked buy-side to assist DNB Scandinavian Property Fund in acquiring the shopping center Øyrane Torg east of Bergen

Bergen

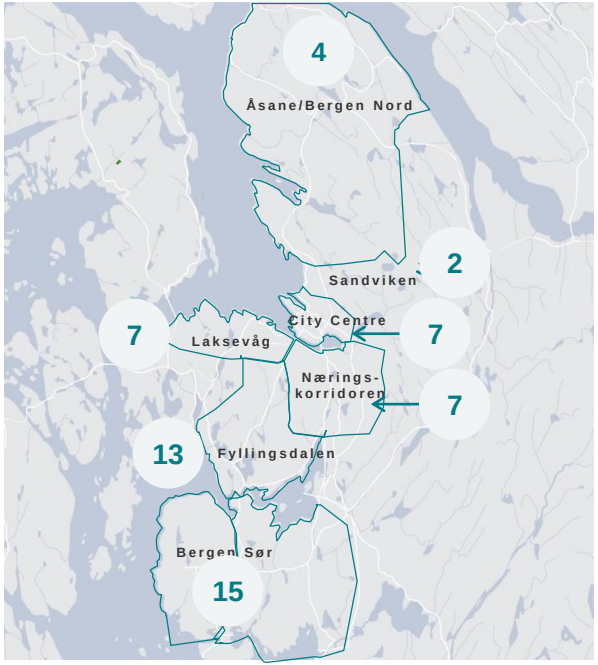
Magnus Havikbotn Jacobsen
Analyst, DNB Næringsmegling

The active and liquid transaction market from 2016 has continued in 2017. In the rental market office vacancy is down from the last count and we believe that there will be a continued fall in vacancy in line with an increased volume of conversion to housing.

Prime Yield	Yield trend	Prime Rent	Since Q1-17	Office vacancy	Rent forecast	Vacancy forecast
4,75 %	↘	2 700	Unchanged	9,3 %	→	↘

- **40% of the year's transactions relate to housing**
- **A wave of conversions has hit Bergen and we expect office vacancy to fall**
- **Increased optimism in Bergen South, where rents are in the process of bottoming out**

Office vacancy Bergen Q3 2017 in percent

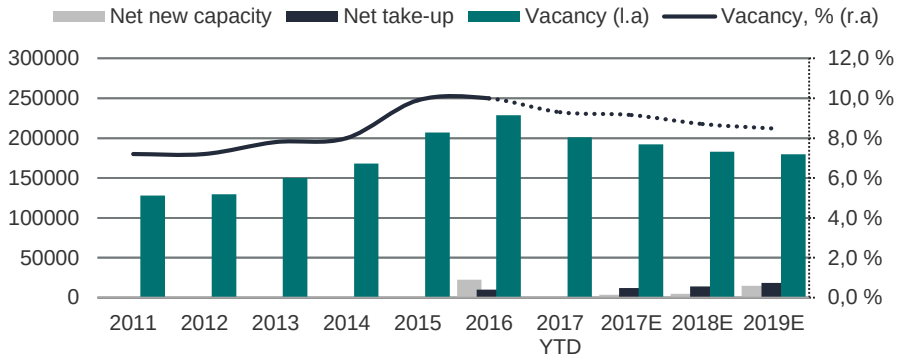


A wave of conversions is leading to lower vacancy Office vacancy in Bergen has fallen by close to 28,000 m² from the previous count, corresponding to an office vacancy level of 9.3% (10.0%). We see a fall in vacancy in all of the four largest office clusters, while the largest decrease has been in the city centre to 7.0% (9.3%). Despite continued large geographic differences with the oil dependent Bergen South continuing to struggle with a high vacancy level, we also see a slight downward trend in vacancy here. Even with this improvement vacancy in Bergen South still accounts for close to half of all office vacancy in the Bergen region, at the same time as only having about a quarter of the overall office space in the region.

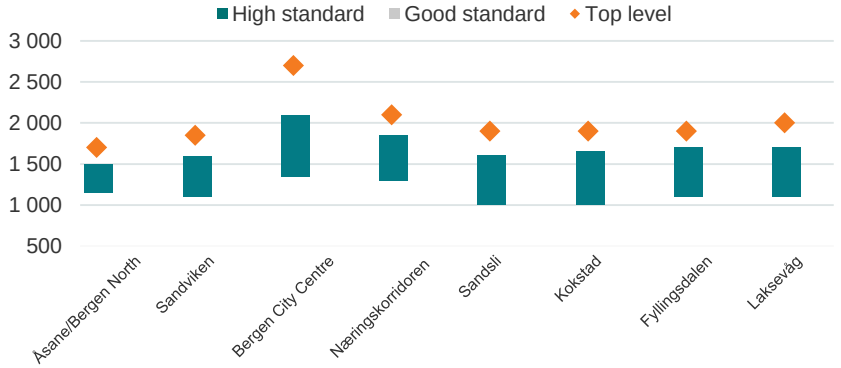
Our forecast for office vacancy in Bergen suggests that the vacancy level will continue to decrease. Increased conversion, a low level of new building and expectations of renewed employment growth will contribute to a downward trend in vacancy. Offices have not only been converted to housing but a lot of space has also been converted to hotel use. Just in 2017 we have seen several examples of office buildings, particularly in Bergen South, that have been purchased with some years' cash flow with the intention of converting to housing. With relatively high vacancy, low rent levels and not least suitable areas for housing, conversion is expected to be strong contributor to lower vacancy in Bergen South and other areas in the coming years.

Rents bottoming out in Bergen South After several years of falling rents and the use of rent-free periods and discounts, we now see some improvement in business optimism in Bergen South. The wave of conversion is expected to contribute to reduce vacancy in the area, while increased optimism in the Norwegian economy could contribute positively on the demand side. However, despite these signs of improvement vacancy is still high and it will take some time before we see any marked increase in rents in this area. There is still a considerable contrast with the city centre, which is characterised by stable high rents and low vacancy.

Office vacancy



Rents



Rosenkrantzkvartalet, Bergen

Sold on behalf of DNB Liv

Liquid and housing-influenced transaction market Last year saw a transaction volume record in Bergen of NOK 9.1 billion. This made the Bergen market by far the most active market outside Oslo. 2017 has also started very well. So far this year 17 transactions have been recorded for a total of NOK 3.3 billion (NOK 4.3 billion) which illustrates a continued very liquid and active market.

2017 has been characterised by many housing related transactions and continued strong demand for low-risk properties. Close to 40% of this year's transactions relate in full or in part to housing. With this the housing segment, somewhat unusually, is the largest segment measured by the number of transactions. This mainly relates to commercial property that is planned to be converted to housing, but also some large land purchases. Companies such as Bonava, Selvaag and Profier are all examples of participants that have been active on the buying side in this segment. Interest is still high for prime property with long and secure cash flows, and many of these transactions have achieved high prices. So far this year we have recorded five transactions with a net yield below 6%. Pressure is greatest in the city centre, where we also see that short leases are achieving very good prices. A low letting risk, good rent levels and a limited supply contribute to making city centre properties particularly attractive.

We consider that the prime yield for offices in Bergen is 4.50–4.75%. Our forecast for the coming year is for a continued liquid market and for yields to continue on a downward trend in line with increased demand for low-risk property.

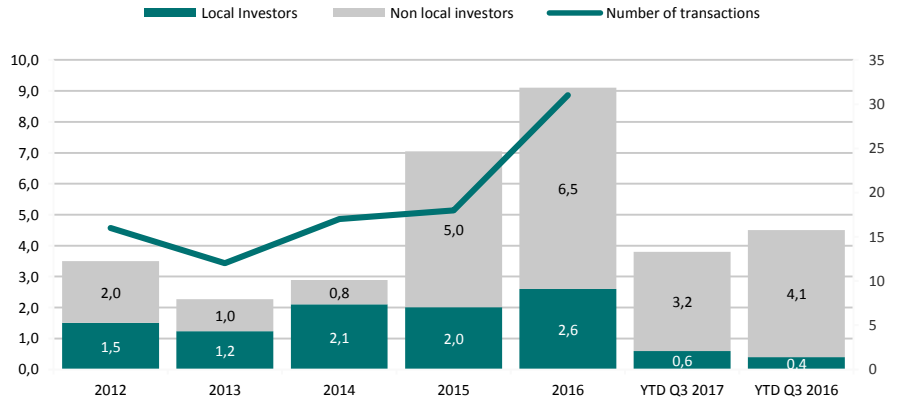
Transaction examples Bergen 2017

- DNB Scandinavian Property Fund bought the shopping centre Øyrane Torg from Nistad Eiendom.
- Hemfosa bought the office building Myrdalsveien 22 from DNB Scandinavian Property Fund.
- Nordea Liv bought the office building Olave Kyrres gate 22 from Jens Petter Teigland.
- Bonava bought the Tine site, Minde Allé 10, from Tine

Yield table

	Office	Logistics	Retail
Prime Yield	4.75 %	5.75 %	4.75 %
Normal Yield	+/- 6.75 %	+/- 7.25 %	+/- 7.00 %

Transaction volume 2012–2017 (NOK billion)



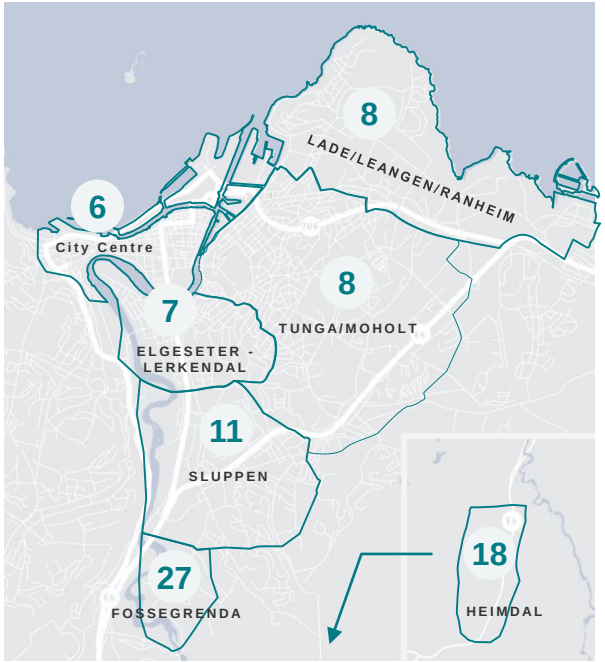
Trondheim

Magnus Havikbotn Jacobsen
Analyst, DNB Næringsmegling

Increased interest for prime properties and new buildings in the transaction market. In the rental market the high level of new building will affect office vacancy and increase the differences between the city centre and peripheral zone.

Prime Yield	Yield trend	Prime Rent	Since Q1-17	Office vacancy	Rent forecast	Vacancy forecast
5,00 %	↘	2 400	Unchanged	9,0 %	→	↗

Office vacancy Trondheim Q3 2017 in percent



- **We expect that office vacancy will increase to 11%**
- **Up to 170,000 m² square metres of new buildings will enter the market in the years to 2021**
- **Strong increase in the number of signed leases - particularly in the city centre**

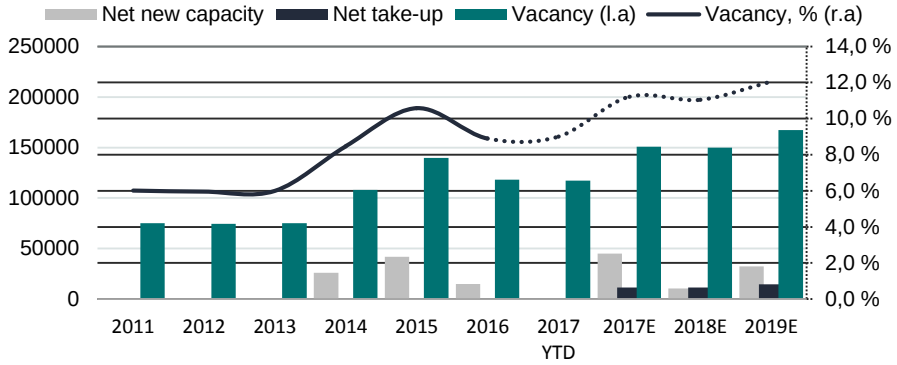
A high level of new building is increasing the difference between the peripheral zone and the city centre Office vacancy in Trondheim is virtually unchanged from last winter at 9.0%. Vacancy is expected to rise gradually through the year as a result of the high level of new building, as the market will receive close to 60,000 m² of new office space in 2017 alone. Our forecast indicates that office vacancy will rise further to 11% before gradually levelling out in line with a more moderate level of newbuilding and increased employment growth. The Trondheim market, which has a higher proportion of public sector and lower proportion of oil industry employment, has experienced much more stable demand than we have seen in Bergen and Stavanger. Nevertheless, this has not been sufficient to absorb the space that has come onto the market

We believe that the market will continue to be characterised by a high supply side. Our estimates indicate that the market may receive more than 170,000 m² in new office space up to 2021 if all the known projects are completed. While new building will increase the office space in the peripheral zone by close to 20%, the corresponding increase in the city centre will be only 5%. We believe this will increase the pressure on centrally located properties and the trend of lower vacancy and higher rents in the city centre will intensify. So far the new buildings are largely fully let, leaving the older vacated premises as the losers.

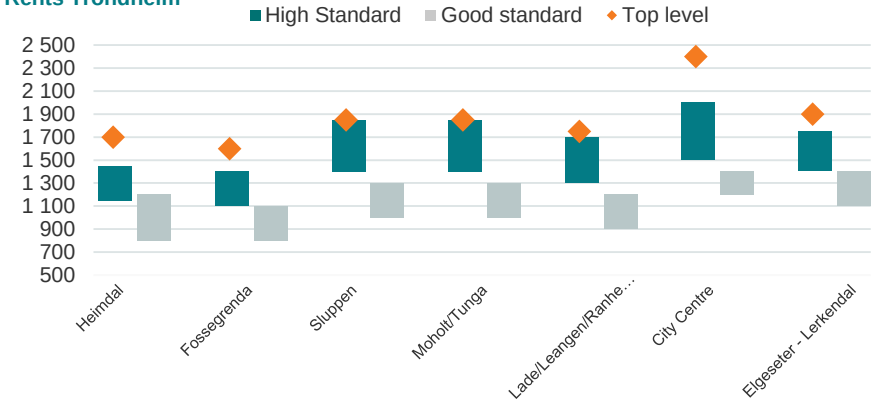
High volume of new leases Activity compared with 2016 is increasing. In the first half year we recorded let space of 47,000 m² (43,000) divided between 136 leases (124). We have seen the greatest increase in the city centre where 60 (51) new leases have been signed, which is the highest number for several years.

Rents show a stable development, with particularly the city centre and development areas holding up well. New buildings in the peripheral zone typically achieve rents in the range NOK 1800 – 1900 per m², while there are still relatively small differences between the centre and the peripheral zone. Our forecast indicates that particularly city centre properties will have a good price development in the future with a low supply of new office space and low office vacancy.

Office vacancy



Rents Trondheim



Lysgården, Sluppenveien 19, Trondheim

Letting of a planned office building on the half of R. Kjeldsberg and Veidekke. 70% is let to Sweco, Norway, Veidekke and others

Increased demand for low risk properties

We have seen a divided transaction market in Trondheim in which there has been steadily increased demand for new buildings and low risk properties, while on the other hand it has been demanding to sell vacant properties. Funds, syndication arrangers and international investors are all showing increased interest in low risk property in Trondheim, which is the same trend as we have seen in both Bergen and Stavanger. The sale of Falkenborgveien 28 is a good example of this. We also offered for sale in Q2 two properties operated by Møller Bil (Orkanger and Stjordal). The properties with 13 years remaining on their leases and an attractive tenant drew strong interest from local and national investors in spite of their location a little outside Trondheim. Following a bidding round, Castelar was the purchaser of the two properties for NOK 105 million.

So far this year the volume of transactions has been slightly above what we saw at the same date last year. In spite of there being no large portfolio transactions, 11 transactions above NOK 50 million for a total of NOK 2.2 billion have been recorded, with most of them being in the low risk segment with a typical value of NOK 100 million upwards. We have seen an increase in transactions with long leases, which illustrates the interest for this type of property. Investors from outside Trondheim still account for the largest volume, the keenest prices and the most transactions.

We believe that the prime yield stands at 4.75–5.0% for property with a central location in Trondheim city centre. Given the marked increase in demand for prime property in particular we believe that the yield level is on a clearly downward trend. In the current market we believe that the right properties could challenge the yield levels we normally see in the Trondheim region.

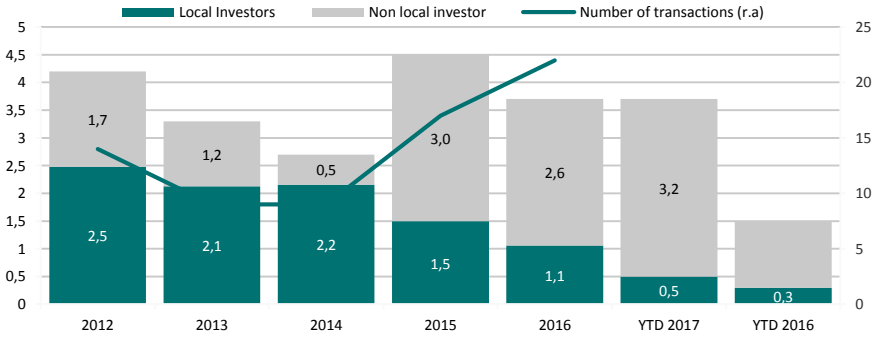
Transaksjonseksempler i Trondheim

- Carsales properties at Orkanger og Stjørdal sold from Møller Eiendom to Castelar for NOK 105 millions.
- The office building Falkenborgveien 28 was sold from Realinvest to a syndicate by DNB Markets for NOK 370 millions.

Yield table

	Offices	Logistics	Retail
Prime Yield	5.00 %	5.75 %	5.00 %
Normal Yield	+/- 6.75 %	+/-7.25 %	+/-7.0 %

Transaction volume 2012–2017 (NOK billion)



Stavanger

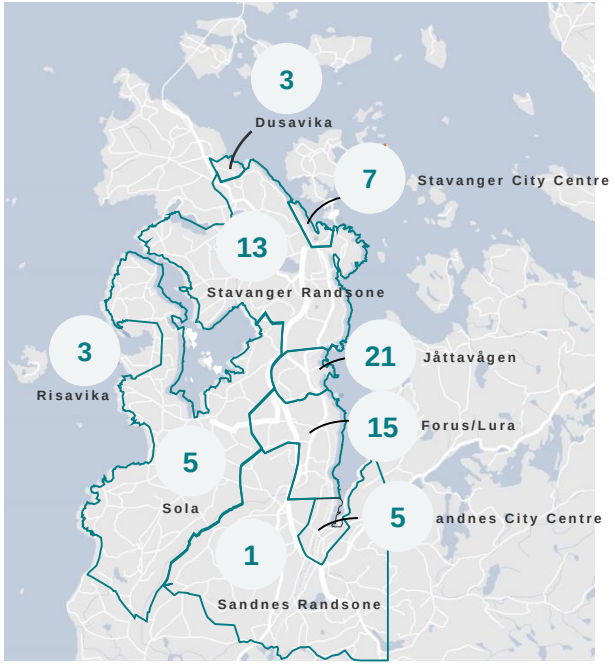
Magnus Havikbotn Jacobsen
Analyst, DNB Næringsmegling

Increased optimism in the market and a considerable improvement in the transaction market. The letting market continues to be characterised by large geographic differences, while the central zones remain good.

Prime Yield	Yieldtendens	Prime Rent	Since Q1-17	Office vacancy	Rent forecast	Vacancy forecast
5,25 %	↘	2 600	Unchanged	11,5 %	→	↗

- **Office vacancy virtually unchanged**
- **Prime yield for Stavanger adjusted down to 5.25%, but Stavanger is still historically cheap**
- **A record good start to the 2017 transaction year, but this is still mainly related to low-risk property**

Office vacancy Stavanger Q3 2017 in percent



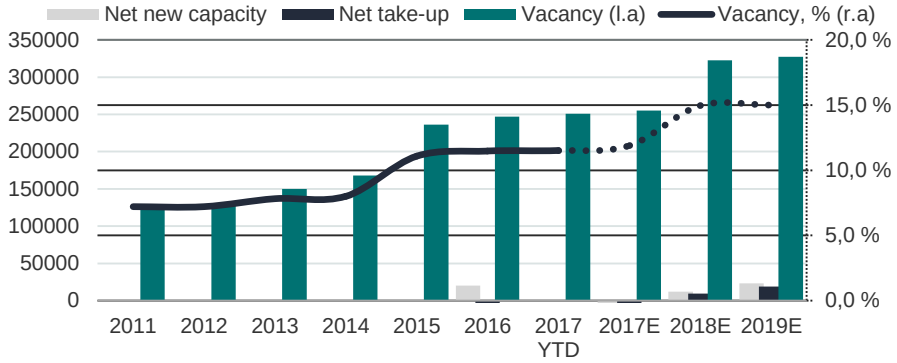
Peak vacancy not yet reached In our last office count we recorded virtually unchanged office vacancy in the Stavanger area of 11.5% (11.3%). The situation in the central areas of Stavanger and Sandnes remains good, but it is still much more demanding in the peripheral zone and the petroleum-related areas. The division in the market can be illustrated by the fact that vacancy in the different zones varies from 7.3% in the centre of Stavanger and 0.9% in centre of Sandnes to 14.6% at Forus and 20.8% at Jåttåvågen. The increase in vacancy that we have seen in the centre of Stavanger to 7.3% mainly relates to the fact that with effect from this count we have included buildings with a combination of offices/retail and offices/restaurant (where the main part is offices). This mainly affects vacancy in the central areas and at Sola, where vacancy is therefore not directly comparable with the previous count.

Our forecast suggests that office vacancy will rise gradually towards 15%, but that the increase will mainly take place outside the central areas. Most of the increase in vacancy relates to the fact that Statoil is moving out of two office buildings at Forus.

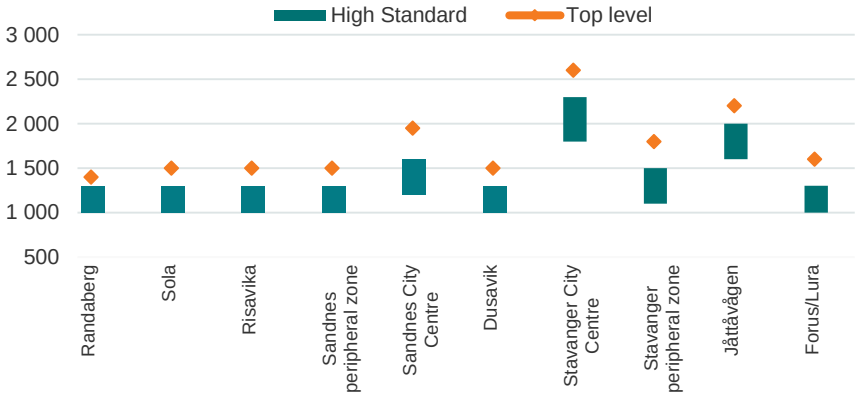
Despite the increased optimism in the market in several quarters it is still expected that employment growth will be low/negative this year. From 2018 we expect that vacancy in the Stavanger area will gradually level out in line with expectations of increased optimism and increased demand for space, but that increased new building volumes, particularly in 2018 and 2019, will mean that it will take some time before we see vacancy on a downward trend.

Rents have bottomed out After several demanding years with increased vacancy and falling rents we now see signs that rents have bottomed out in the peripheral zone and the petroleum-related areas. This is to some extent a sign that we are approaching a critical point, but at the same time is also a result of there being more optimism in the market. Most companies appear to have completed the main restructuring operations and it is easier to look forward than previously. Despite these positive signs, we nevertheless believe that it will take time before we see a marked increase in rents, both in the central areas and the petroleum-related areas.

Office vacancy



Rents



Vestre Svanholmen 13, Stavanger

Sales assignment on behalf of Starwood Capital Group/Anvil Asset Advisors

Increased optimism Several key figures are contributing to increased optimism in the Stavanger market. Unemployment, economic barometers and house prices indicate an improving market. We also see optimism in the transaction market, but this mainly relates to low-risk property. So far this year commercial property has changed hands for NOK 4.7 billion (NOK 1.1 billion) which is close to the volumes we normally see on an annual basis in the region. Despite the fact that the five largest transactions account for close to 80% of the volume, there is no doubt that we have seen a marked shift in sentiment. The question is now whether this will carry over to the normal market with shorter leases. Our experience is that the gap between buyers' and sellers' expectations is decreasing, but that buyers are still selective.

We are adjusting downwards our forecast for the prime yield in Stavanger to 5.25% (5.50%) and believe that the yield is on a clearly downward trend in line with greater optimism and a noticeable increase in demand for low-risk property. We also see that properties with particularly long leases can change hands for well under 5%.

Yield discount on the way down, but still historically cheap

In spite of the positive development Stavanger is still priced at a considerable risk premium in relation to what we have seen historically and against comparable cities. Today the prime yield in Stavanger is considered to be at 5.25%, which in spite of a downward adjustment still gives a risk premium of 150 basis points against the best properties in Oslo. It is not many years since this premium was only 100 basis points, a level at which Bergen stands today. With a historical risk premium over the last 10 years of 130 basis points between Oslo and Stavanger, there is still a potential upside of close to 20 basis points just to reach the historical difference. This is due to the fact that rents must rise by more than 20% to return to the historical difference against the capital.

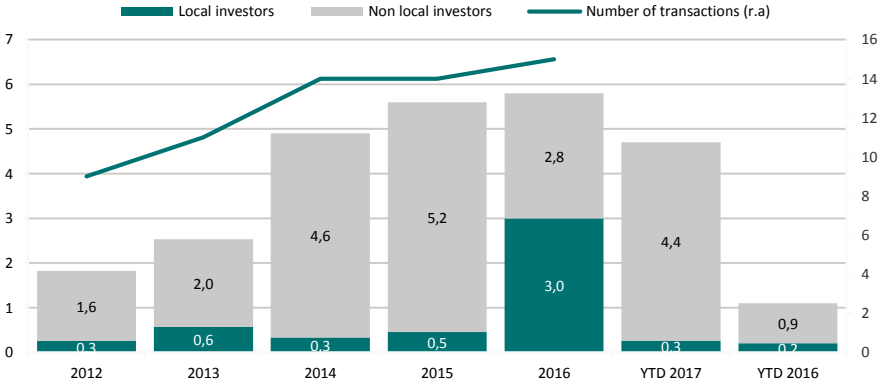
Transaction examples Stavanger 2017

- Union Real Estate Fund II bought the Anker quarter from Øgreid Eiendom
- Nordea Liv bought the office and retail building Nykirkebakken 2 and Verksgata 1A in the centre of Stavanger for NOK 777 million.

Yield table

	Office	Logistics	Retail
Prime yield	5.25 %	6.25 %	5.25 %
Normal yield	+/- 7.50 %	+/- 8.00 %	7.50 %

Transaction volume 2012–2017 (NOK billion)



Retail

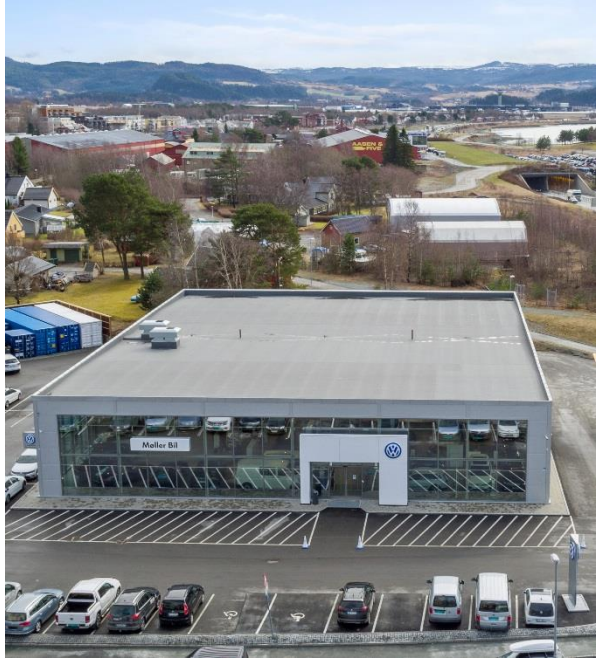
Magnus Havikbotn Jacobsen
Analyst, DNB Næringsmegling

Online shopping is accounting for a steadily greater proportion of shopping for goods, and is expected to increase significantly in the present year as well. A large number of buyers and a high volume of transactions illustrate continued very good demand for retail properties.

Prime yield	Since previous	Total transactions	Transaction volume
3,75 %	-	31	NOK 10,6 bn.

- **Online shopping is expected to pass NOK 100 billion in 2017**
- **Online shopping for goods is expected to grow by 21%**
- **50 different purchasers of retail property in the last two years**

Car showroom at Stjørdal and Orkdal Sold on behalf of Møller Eiendom and Møller Bil



Online shopping to pass NOK 100 billion in 2017 Figures from DIBS annual e-commerce report show that online shopping is expected to grow by 16% in the current year. The forecast indicates that online shopping will rise to NOK 105 billion in 2017, corresponding to growth of a full 74% over the last four years. Within online shopping for goods is among the categories that is expected to grow most. In 2017 online shopping for goods is expected to amount to close to NOK 33 billion, corresponding to an increase of 21% since last year. In simple terms this can be said to be Internet leakage for retail property.

Good growth for shopping centres in Oslo The shopping centres in Kvarud's shopping centre index have recorded growth of 1.4% so far in 2017 after adjustments for space changes. District and local centres have had relatively more growth than the regional centres, while the greatest growth was recorded by shopping centres in northern Norway (3.1%), Oslo (2.2%) and Trøndelag (1.9%). The only Norwegian county with negative growth was Rogaland (-0.1%).

Continued high demand for retail properties in the transaction market So far this year 31 (35) retail transactions have been recorded with an aggregate value of close to NOK 10 .6 billion (NOK 9.0 billion). Retail property continues to be very attractive and just in the last two years we have recorded almost 50 different buyers within this segment. Since 2014 more than half of all retail transactions have related to shopping centres and close to 80% of this volume has related to transactions involving property in and around four largest cities.

Examples of retail transactions in 2017

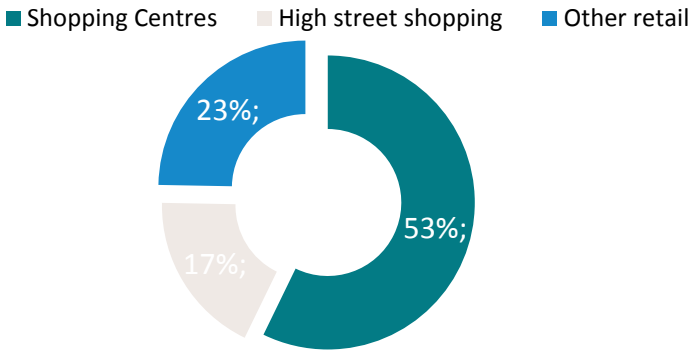
- Via Outlet has bought Norwegian Outlet Vestby for NOK 1.1 billion.
- DNB Scandinavian Property Fund has bought the shopping centre Øyrane Torg from Nistad Eiendom
- A Clarkson syndicate has bought a portfolio of three buildings in Haukås Næringspark from Profier for NOK 309.2 million.

Key figures – Retail

	2013	2014	2015	2016	2017 YTD Jul.
Online shopping	16 %	15 %	13 %	16 %	16 %*
Retail store sales	3.3 %	1.8 %	3.8 %	3.2 %	2.1 %
Private consumption	2.1 %	1.9 %	2.1 %	1.4%	2.1 %*
Shopping centres	1.7 %	2.7 %	1.9 %	1.7 %	1.4 %

*Internet trading and private consumption are forecasts for 2017

Retail transactions by type of transaction 2014-2017



Source: DIBS, Virke og DNB Markets

Four properties in Haukås Næringspark, Bergen

Sold on behalf of Lønne Eiendom Holding AS

Warehousing and logistics

Ketil Ervik
Letting broker, DNB Næringsmegling

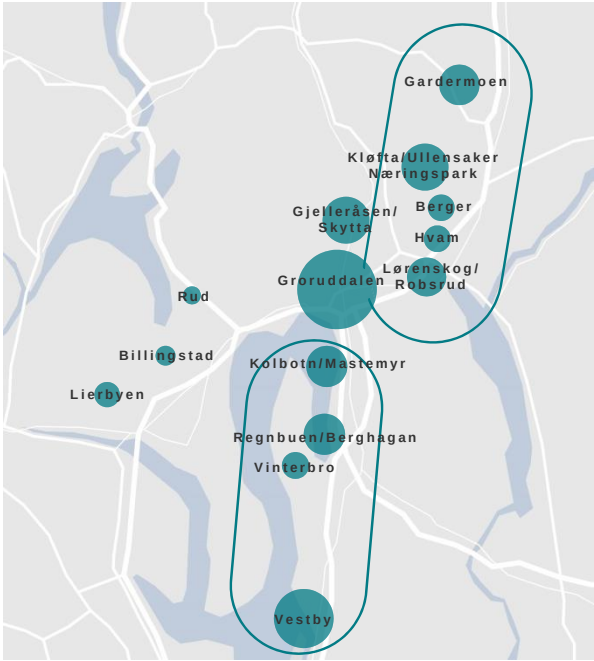
The number of transactions so far in 2017 is in line with last year, but this year there have been few transactions at the highest prices which means that the volume in NOK is below last year's.

Pricing is in some respects keener and the yield spread in relation to prime office property has been reduced

Prime Yield	Since Q1-17	Prime Rent	Total transactions 09 2017	Transaction volume 09 2017
4,75 %	-	1 200	38	NOK 6,8 bn.

- **The prime yield has been reduced by 50 basis points to 4.75%, many investors expect growth in values**
- **Few alternatives within Oslo, a good rate of lease signings for new buildings outside Oslo**
- **Rents expected to rise within Oslo, a flat development outside.**

Warehouse clusters, Oslo and surrounding region



Main features In recent years tenants have had limited choices within the Oslo Outer ring road partially due to the conversion of logistics premises to housing and offices. That trend is expected to continue outside the ring road in the coming years meaning that logistics premises will to a greater extent be located outside Oslo. Still a cooling of the housing market has likely slowed conversion to residential use.

There is broad supply of new projects both to the north and south of Oslo. The rate of lease signings for both existing and new buildings is good, although rent levels in existing buildings continue to be under pressure from new projects. The top rent for existing buildings with a central location is considered to be NOK 1200 per m²/year. Most leases are in the range NOK 900–1,050. We expect an increase in rents within Oslo but a sideways movement outside Oslo.

Letting examples

- Felleskjøpet, about 13,000 m², Gardermoen
- Ntex, 8,000 m², Sofienmyr
- Prime Cargo, newbuilding 38,000 m², Vestby

The transaction market So far in 2017 we have recorded 38 transactions with an aggregate value of approximately NOK 6.8 billion. There are considerable variations in pricing within warehousing and logistics where the remaining lease term is a very important factor. As of October 2017 we have recorded 15 transactions priced at NOK 15,000 per m² or higher.

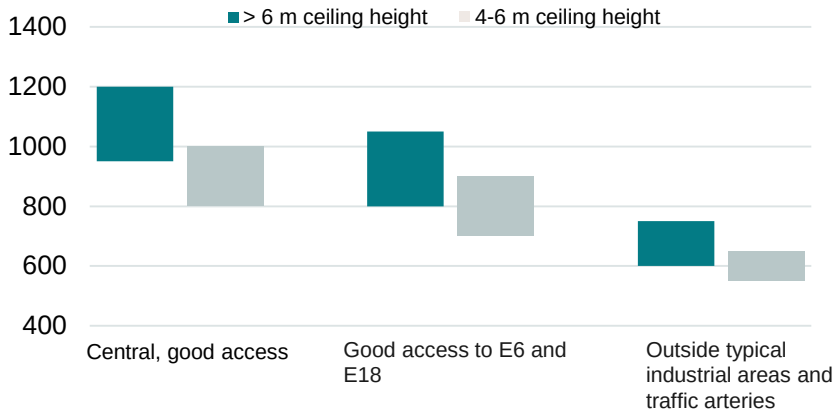
We consider that the prime yield within warehousing and logistics is 4.75% on the basis of specific transactions, which is a reduction of 50 basis points since our last market report. So far in 2017 we have recorded five transactions with a yield of 5.5% or less. In our survey of leading property investors many said that they expected value growth in the segment.

Transaction examples

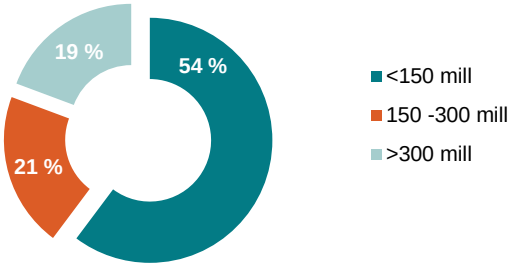
- Bjorgen Property Investments' sale of the Onninen main warehouse at Skedsmo to Fabritius.
- OBOS's sale of Persveien 26 at Ulven - a new building to be completed in January 2018 - to a syndicate established by Arctic

.

Rent levels



Transactions 2014–2016



Brages vei 2, Gardermoen

Let on behalf of Thon Eiendom to Felleskjøpet (approx. 13,000 m²)

Hotels

Magnus Havikbotn Jacobsen
Analyst, DNB Næringsmegling

On a national basis we see a continued strong development, and there have not been so many months with continuous price growth since 2008. Oslo has had the strongest development in key figures, while the situation is more challenging in several of the other main cities.

Prime Yield	Since last	RevPAR	Since last	Total transactions	Transaction volume
4,00 %	Unchanged	503	+7,1 %	7	NOK 1,2 bn.

- **8 months' continuous increase in room prices**
- **The Oslo hotels achieved an average room price over NOK 1,000 for the first time**
- **Growth in business traffic but decline in overnight stays by foreign visitors**
- **Capacity increase of 1,300 new hotel rooms in the Bergen market in 2017**

Radisson Blu Royal Hotel, Bergen

Valuation on behalf of DNB Næringseiendom

8 months' continuous price rises in the hotel market There has been continued strong growth in the Norwegian hotel sector with both occupancy and prices increasing. We have now seen eight months of continuous price rises, although figures for the first half year are somewhat affected by the strike in April and May last year. The greatest growth has been in business traffic, while for the first time since 2013 there has been a decrease in international traffic.

- The Oslo hotels achieved an average room price above NOK 1,000 for the first time. Market growth was positive, but a reduction in room capacity also contributed to the good figures in the first half year. Both the Royal Christiania and Europa are undergoing total renovation.
- Bergen is affected by considerable capacity growth. In 2017 close to 1,300 new hotel rooms will enter the market, while the effect in the first half year is capacity growth of 8%. The price level has so far remained stable, but occupancy is down to below 60% for the first time in 10 years.
- Trondheim has seen a rise in both prices and occupancy. The number of sold rooms however is more or less unchanged. The positive development is largely related to the renovation of Britannia Hotel which has benefited the other hotels in the market.
- Stavanger has been affected by a continued decline in demand. The number of room days sold fell by 8%, and the positive development in prices is mostly due to capacity being reduced by close to 12% in the same period. On the positive side the business segment saw growth of 6.4%, but this was not enough to counter a reduction in both the holiday and conference segment.

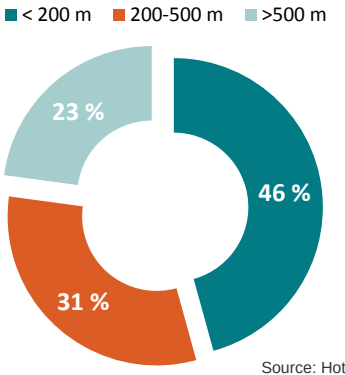
Transaction examples So far this year 7 hotel transactions have been completed for an aggregate volume of NOK 1.2 billion. Examples of completed hotel transactions in 2017 include:

- Midstar bought Quality Hotel Entry from Strawberry Properties (Petter Stordalen).
- Strawberry Properties bought the remaining 50% of Quality Hotel Pond from Base Property.
- Bergen Hotell Gruppen bought 50% of Dr Holms Hotel from Frydenbø Eiendom.

Key figures Hotels

	Price Per room		RevPAR		Capacity(in.mill)		Capacity utilization	
	H1 2016	H1 2017	H1 2016	H1 2017	H1 2016	H1 2017	H1 2016	H1 2017
Countrywide	908	947	470	503	13,6	13,8	51,7 %	53,1 %
Oslo	979	1 016	641	716	2,3	2,2	65,5 %	70,5 %
Bergen	986	988	604	582	0,9	0,9	61,2 %	58,9 %
Trondheim	821	890	481	549	0,6	0,6	58,6 %	61,7 %
Stavanger	866	892	409	439	0,6	0,5	47,2 %	49,2 %

Hotel transactions 2014– 2017



Source: Hotelia, SSB, DNB Næringsmegling

Macro-economy

Jeanette Strøm Fjære
DNB Markets

Higher temperature in world economy, low inflation stops interest rate fall.

Read more on the economic outlook from DNB Markets here.

Key figures	2016	2017e	2018e	2019e
GDP Mainland Norway	0,9 %	2,0 %	2,0 %	1,9 %
Interest rates – 10-year swap	1,6 %	2,0 %	2,2%	2,5 %
Inflation/CPI	3,5 %	2,1 %	1,6 %	1,4 %
Employment	0,3 %	0,4 %	0,9 %	0,9 %

DNB Markets

- **Globally: Higher temperature, but low inflation is keeping interest rates down**
- **Norway: Increase in investment expected, but the upturn will be moderate**
- **Housing market: Shifting from being a motor to a brake**

Global

Global GDP growth is expected to be higher than last year as a result of higher growth in both industrialised countries and emerging economies. Continuing strong demand growth from China and broad optimism have contributed to a synchronised upturn in growth across countries and sectors. We believe that we are now in the strongest phase of the cyclical upturn, but that growth will also be higher than normal going forward so that unemployment will continue to fall. At the same time wage growth is being held down by national and global factors in many countries. This is restricting inflation and limiting rise in interest rates. However, we expect a gradual tightening of monetary policy in the coming years. There is considerable uncertainty attached to the forecasts and many factors could lead to a different outcome. If wage growth rises more than expected, the rise in interest rates could be steeper. The market could also be less prepared for a reversal of the expansive monetary policy than we assume. Furthermore, the high level of corporate debt in China, together with imbalances in its property market, may lead to significantly weaker demand stimulus. We believe the risk attached to China to be slightly lower than at the time of our previous report, although the geopolitical risk has increased.

Norway

Growth in the Norwegian economy is also on the way up after two years of declining petroleum investment. Households are more optimistic than for some while, which again is shown by higher consumption growth. Together with continued high growth in housing investments and a smaller fall in oil investments, this has lifted GDP growth considerably from last year. The momentum looks like continuing over the next year before slowing a little. Impulses from finance policy will shift from being strongly positive to neutral in the coming years. In addition, housing investments will decrease somewhat, following strong growth last year and this year.

GDP growth of just below 2% towards the end of the forecast period is a half percentage point less than the average since 2000. At the same time, it is probably a little over what one can expect as the new normal for Norway.

Key figures - global

GDP	2017E	2018E	2019E	2020E
Eurozone	2.1%	1.9%	1.4%	1.1%
Sweden	3.0%	2.3%	1.9%	1.8%
Great Britain	1.6%	1.1%	0.9%	0.9%
10-year swap	**2017E**	**2018E**	**2019E**	**2020E**
Eurozone	1.0%	1.3%	1.5%	1.5%
Sweden	1.3%	1.8%	2.0%	2.0%
Great Britain	1.5%	1.5%	1.5%	1.5%

Key figures - Norway	2016	2017E	2018E	2019E
GDP mainland Norway	0.9%	2.0%	2.0%	1.9%
CPI	3.5%	2.1%	1.7%	1.6%
CPI adjusted	3.6%	2.1%	1.6%	1.4%
Private consumption	1.6%	2.1%	2.1%	2.2%
Exports of traditional goods	-8.2%	1.2%	3.2%	3.0%
Employment	0.3%	0.4%	0.9%	0.9%
Unemployment rate, labour force survey	4.8%	4.3%	4.2%	4.1%
Gross investments petroleum activities	-16.4%	- 4.7%	0,0%	5.0%
Oil price (USD/bbl)	45	55	61	68
Secondary house prices	8.3%	5.7%	-2.5%	1.0%
Interest and exchange rates				
3m NIBOR	1.0%	0.9%	0.9%	1.0%
10 year swap	1.6%	2.0%	2.2%	2.5%
EUR/NOK	9.3	9.2	8.8	8.6
USD/NOK	8.4	8.2	7.4	6.9

Source: DNB Markets Economic Outlook January 2017

With production growth above normal, employment is likely to rise further and unemployment fall a little in the coming years.

We expect a slight rise in wage growth as a consequence of a stronger economy and lower unemployment, but a wish among parties on both sides of industry to protect its cost-competitiveness will contribute to lower wage growth than seen in previous decades.

Price growth

Price growth was higher last year due to the strong rise in import prices as a result of the NOK weakness during 2014 and 2015. Consumer price growth ended at 3.6% last year while core inflation was slightly lower at 3.1%. We estimate that core inflation will be 1.6% this year and 1.5% next year. In 2019 there is a likelihood of even lower inflation before it increases to 1.4% in 2020. A stronger NOK and continued low wage growth are the most important reasons for low core inflation.

Monetary policy

The upturn in the Norwegian economy means that Norges Bank does not need to stimulate the economy with further interest rate cuts. But with inflation well under the target of 2.5% it will take some time before Norges Bank lifts interest rates. We expect that the first increase in the base rate will be in September 2019, after both the Swedish Riksbank and the European Central Bank have raised interest rates. Norges Bank will probably continue to place emphasis on the high level of household debt and the need for higher interest rates to counter financial imbalances.

Housing

House prices rose very rapidly in 2016, particularly in Oslo. In February this year the annual rate of growth was as much as 13% on a national basis and 24% in Oslo. At that time there were several arguments that house prices would level out. The effect of steadily lower interest rates had largely worn off, and lower population growth together with an increase in new housing projects suggested a more balanced relationship between supply and demand in the housing market. Higher household income growth, increased optimism and an improvement in the labour market were arguments in favour of somewhat higher house prices. The risk of a more substantial reversal was nevertheless considerable. Firstly, the potential drop was big after many years of strong price growth. Secondly regulations on mortgage loans were tightened at the start of the year and the effect of such regulation was uncertain. Household debt had reached a high level and the new requirement that mortgage loans could not exceed five times gross income could affect many house-buyers.

The reversal has been more marked and house prices have fallen for the last five months. A large number of unsold houses, particularly in Oslo, indicates that the fall in prices will continue for some quarters more. Low interest rates and brighter prospects for the Norwegian economy, with falling unemployment and rising income growth, will nevertheless limit how much house prices fall and mean that from the middle of 2018 some growth can be expected. The risk of a more substantial fall in prices, which could also have negative knock-on effects on the Norwegian economy, is still present however.

The housing market: Super seniors (65+) will be more important buyers for house builders

DNB Eiendom expects that housebuilders will have good possibilities to complete profitable projects in Oslo in the future but will be more dependent on their projects meeting identified needs. DNB Eiendom has an understanding of what works and has clear expectations regarding the market. In this article Jørn Are Skjelvan, head of new building in DNB Eiendom, shares his views on the development of the Oslo market and what kind of conversion projects appear to be the most promising.

1. What expectations do you have regarding the volume of new building in Oslo in the future?

We expect that the volume of newbuilding in the capital will be at the same level as in 2015, 2014 and earlier years – around 2,000 units a year. 2016 was an exceptional year when the small number of homes for sale in the secondary market made the new building projects that were available very popular. Combined with the fact that new building prices were roughly at the same level as secondary market prices for newer properties, a record number of new apartments were sold in Oslo.

2. What expectations do you have for price developments for new apartment projects in Oslo in the future?

We expect a levelling out of prices in Oslo over the remainder of the year even though there may be isolated examples of rises and falls in individual districts. Prices fell by a further 1.6% in September, leading to more negative media articles on a house price crash and bubble trends. Nevertheless, the volume of sales is holding up, so it is not only those who can obtain a good price who are choosing to sell, as we saw in Stavanger following the oil crisis. There has been a positive development in house prices in the Stovner, and Nordre and Vestre Aker districts, which have a large number of family houses. It is primarily apartments in Oslo that have seen a price correction following the substantial price increases last year. Towns such as Moss and Drammen have also had price growth in a market where the average prices has gone down.

3. Several investors are buying commercial properties with some years' cash flow planning a future conversion to housing. In addition, you have said that the right location is now more important for the sale of new building projects in Oslo. Bearing in mind both timing and location, what kind of conversion projects would DNB Eiendom recommend to investors and what kind of conversion projects should one avoid?

Conversion projects in areas with little new building activity are winners. Most people who will move in the coming years will be 65+. They mainly want to stay in the same area as long as the housing alternative is an easily managed home with high standard and proximity to shops and public transport.

Tåsen, Nordberg, Smestad, Vinderen and parts of Groruddalen will be good areas in the future, in addition to the defined transport hubs in the new city plan. It is noticeable what has happened at Nordstrand where there have recently been several projects close to shopping centres that have sold for high prices compared to levels for used houses in the area.

Prices will bottom out during the autumn and the volume of new building sales will pick up in the New Year

With the introduction of new lending regulations at the start of 2017 a reduction in demand and activity in the housing market was expected. Demand has been lower than the record year last year, but has been higher for both new and used homes than the average for the years before 2015 and 2016.

As an example the number of new homes sold so far this year in Oslo is 39% higher than in the corresponding period in 2013 and as much as 71% higher than in 2014. For the period June to August this year the number of new homes sold in Oslo was 5% higher than in 2014 and 41.2% higher than in 2013. We see a similar trend throughout Eastern Norway. At the same time the number of homes sold in the secondary market so far this year in Oslo is only 6% lower than the record year last year, and 18.6% above 2014 and 16% above 2013.

Along with demand being good there is an unusually high number of both used and new homes being offered. As an example 46% more used homes were offered for sale in Oslo in July than in the same month last year, and in total 10% more have been offered so far this year against last year. This has resulted in a short-term imbalance in supply/demand and contributed to a correction in the prices of used homes, as well as giving a more normal price difference between new and used, as shown by figure 1. This trend with an increased price differential can be seen throughout the whole country.

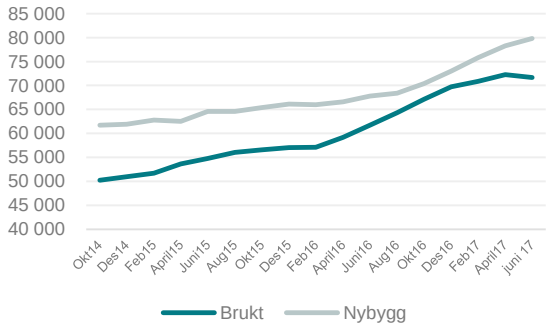
Price growth has been decreasing over the last five months and we expect a further levelling out during the autumn. With continued low interest rates, a high and rising employment level, good purchasing power and a weak increase in inflation, we expect continued good demand. In a buyers' market with plenty of choices and good timing with regard to price and long-term investments, it is likely that demand will remain good and stocks reduced. Population growth has slowed this year in Oslo, but is expected to pick up from the start of next year to an average annual increase of 1.7% to 2022. Given continued good demand and a slowdown in the number of used homes being offered, house prices are expected to balance.

Within the family segment prices are roughly in line with last year in Oslo, particularly with respect to detached houses, terraced houses and semi-detached houses. For example, 133% more terraced houses have been sold this year compared with last year. Demand in the segment depends on developments in the real economy and employment, so we expect that this demand will continue. We have also seen greater selectivity in house purchases, and internal qualities such as location and proximity to infrastructure and shops have been given greater importance. We believe that this will continue and affect demand in all segments in future.

There has been an increase in investment in land in the peripheral zones during recent quarters. As an example land purchases in Lørenskog during the third quarter of this year reached their highest level ever and the same was the case in Bærum in the fourth quarter last year and second quarter of this year. In Lørenskog investments were made for the development of 478 apartments during the second quarter – a volume over 400 has never previously been recorded in a single quarter. And the number of new homes sold increased by 22% for Øvre Romerike from the first to the second quarter this year, in Asker and Bærum by 291%, and in Buskerud by 51%. The volume of conversions is however low and virtually zero in the peripheral zones, apart from in Bærum where 11 new conversion projects are decided. Given an increasing rate of infrastructure development, the new rules on mortgage loans and the taxation of the property in Oslo, together with a low supply and increased preference for new homes in the peripheral zones, we believe that the potential is particularly great here and that the trend of increasing development and demand will continue into 2019.

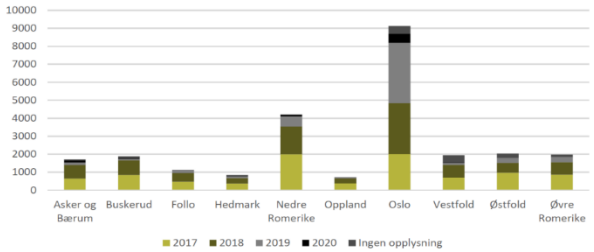
At the same time a large number of new apartments will be completed in Eastern Norway as a consequence of the high sales volumes in 2015 and 2016. This may have consequences for the housing stock, particularly in Oslo, as people moving to a brand-new home often will have a used one they wish to sell. This may contribute to maintaining a large supply of homes in the secondary market in the coming years.

Prices new vs used Oslo



Source: Econ

Expected completions towards 2020



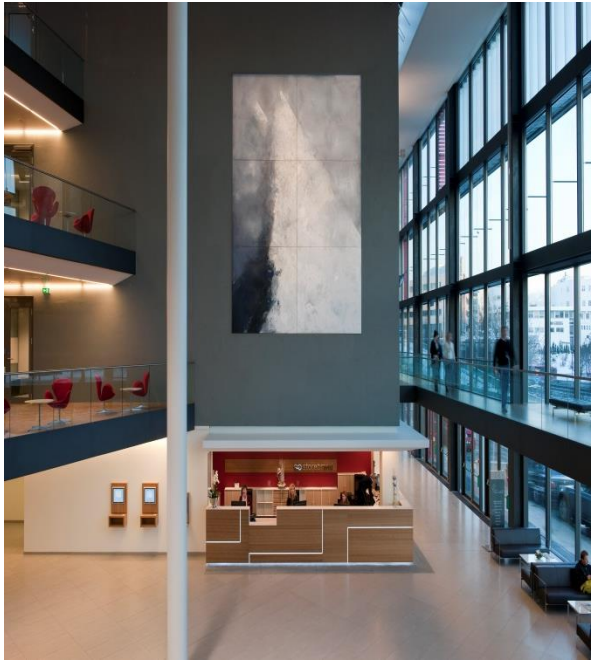
The bond market

Magnus Vie Sundal
DNB Markets

Attractive conditions in the bond market contribute to continued strong growth

- **Property companies have issued NOK 24.6 billion in the bond markets so far in 2017, against NOK 23.9 billion for the whole of 2016**
- **Credit margins fell in the first half year, and have subsequently stabilised**
- **In five years the number of active property company issuers in the Norwegian market has increased from 23 to 90, and the outstanding volume has increased by around 500% to more than NOK 80 billion.**

Professor Kohts vei 9 - Lysaker Park
Letting assignment on behalf of Storebrand



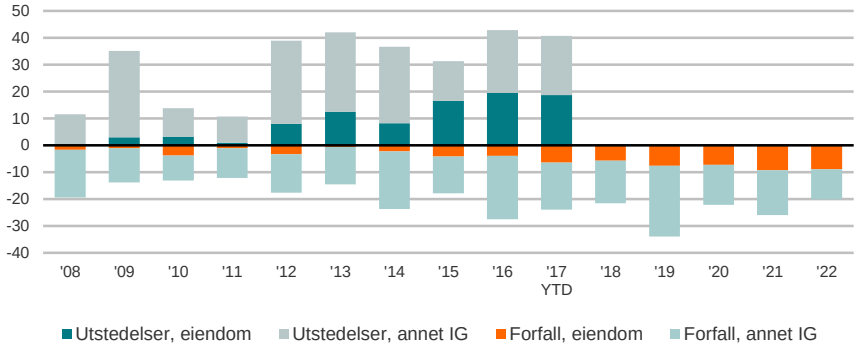
Continued good financing terms

2017 has continued the positive trend from 2016. The main driver in the world's credit markets, loose monetary policy, has contributed to attractive financing terms. In addition, many other factors have contributed to create a strong credit market: companies in both Europe and the USA have increased their earnings, labour markets have continued to develop well, debt defaults are low and the various sentiment indicators show strong optimism as to future developments. The Norwegian market for investment-grade bonds remained stable during the summer when the oil price fell from around USD 55 a barrel to the mid 40s. It helped that the fall was short-lived. A better balance between supply and demand, aided by OPEC's production agreement, has contributed to the oil price returning to where it started the year, a factor that is positive for stable credit margins.

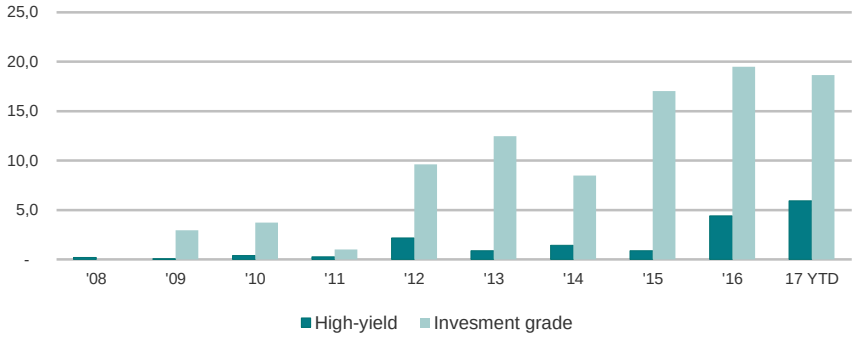
Credit market at a fork in the road

Looking forward we expect however that credit margins could increase a little in 2018. After several years of expansive monetary policy, the US Federal Reserve recently announced that it would begin to scale down its balance sheet in October. In the first instance the amounts will be modest, but within a year we expect that USD 50 billion in liquidity will be taken out of the market each month. We believe that this could contribute to somewhat higher credit margins of around 20-30 basis points for investment-grade credits during the next couple of years. We do not believe there will be a powerful and dramatic reversal, and expect continued stable markets in 2017 helped by the European Central Bank's continued support purchases.

Issues and maturities, investment-grade bonds in the Norwegian market



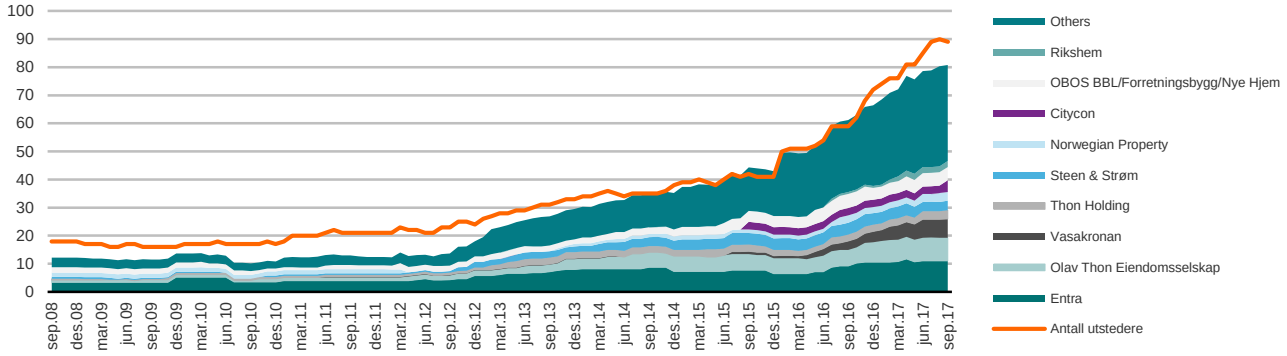
Good conditions have contributed to strong growth



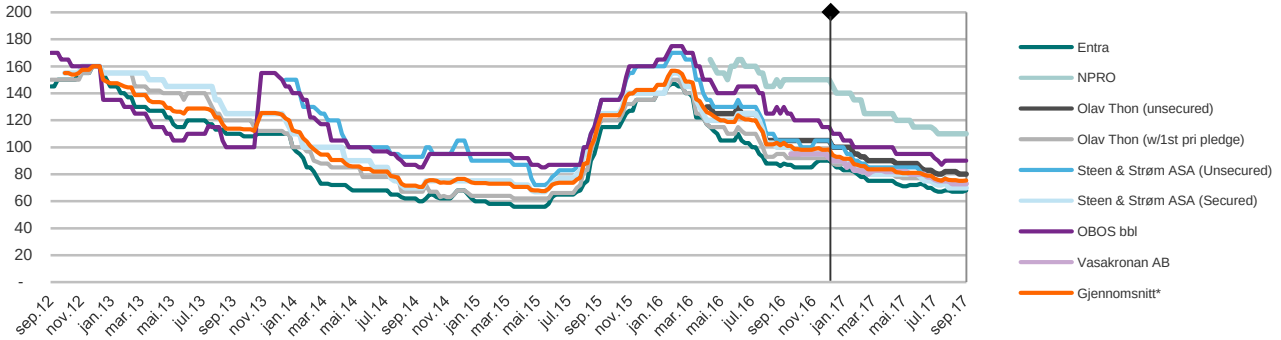
Good conditions have contributed to strong growth

With the banking sector being subject to tougher regulation, we have seen continued strong growth in outstanding property bonds in 2017. This has been the case both for the established names but also for a number of smaller issuers. During the last 5 years the number of active issuers in the Norwegian market has risen from 23 to 90. The outstanding volume has risen from NOK 14 billion to more than NOK 80 billion, a growth rate of around 500%. Among the contributors, the Swedish issuers have been very active with more than NOK 10 billion of outstanding bond debt. In addition to Rikshem and Vasakronan, Willhelm AB recently raised NOK 1 billion in its first bond issue. The Finnish company Citycon has also been active in the market and recently made its fifth NOK bond issue, raising NOK 1 billion. In spite of the substantial growth, most of the Norwegian property debt is still held by the banks. We believe however that the current trend will continue, and we see the potential for considerable growth in the bond market for property companies in the coming period.

Outstanding property bond loans in the Norwegian market (NOK bn.)



Indicative credit margin over 3m NIBOR (basis points)



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