AFFINIUS CAPITAL

UNLOCKING OPPORTUNITIES IN EUROPEAN LOGISTICS

Summer 2024

EXECUTIVE SUMMARY

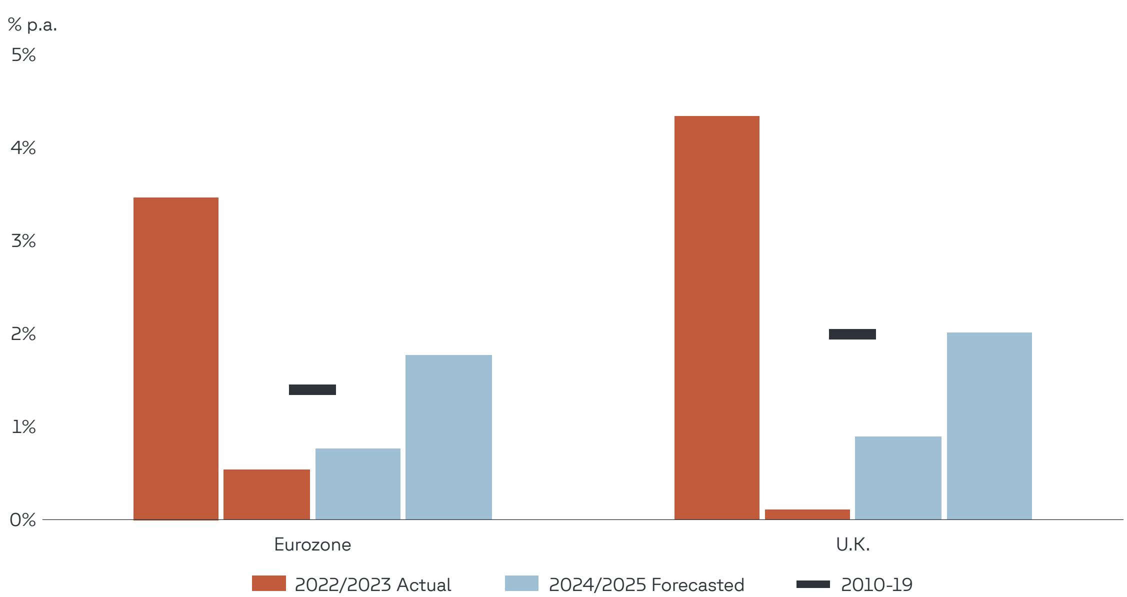
The European economy continues to expand at a steady pace and although market volatility persists, the environment remains supportive of logistics real estate investment. **According to a recent survey, the logistics sector ranks second (marginally behind residential) in terms of investor preferences in Europe over the next two years.**[1] The sector is supported by strong fundamentals and continued rental growth and therefore remains a natural preference for investors. Despite this, new logistics supply is struggling to keep up with the pace of occupier demand. Construction starts and the development pipeline continues to shrink due to barriers to entry and some developers pausing the development of new projects until the lending environment improves. **With positive demand side dynamics and less supply coming online, we believe now is an opportune time to enter the logistics development market in Europe resulting in a good vintage for new investments.**

MACROECONOMIC FUNDAMENTALS

The European economy is emerging from a period of stagnation that characterized most of 2022 and 2023. However, sentiment indices suggest the economy is recovering faster than expected.[2] We expect 2024 to be another year of modest growth, with recovery building momentum during the second half. Eurozone GDP growth of 0.8% is forecast in 2024, followed by a rebound to 1.8% in 2025 (**Exhibit 1**).

Private consumption, a key driver of logistics real estate demand, is the main catalyst for economic growth. As inflation decelerates, real wage growth and resilient employment should support a rebound in consumption. In addition, the growth of euro area exports should pick up over the coming quarters, as the global economy recovers coupled with near and onshoring activity. Finally, monetary policy should exert less of a drag on demand over time helped further by anticipated rate cuts this year.

EXHIBIT 1: REAL GDP GROWTH (ACTUAL VS. FORECASTED)



Source: Oxford Economics, June 2024

1. Oxford Economics. Eurozone: Wage growth win for haws but won't derail June cut. Published May 24, 2024.
2. INREV. Investment Intentions Survey. 2024

POSITIVE DEMAND DRIVERS

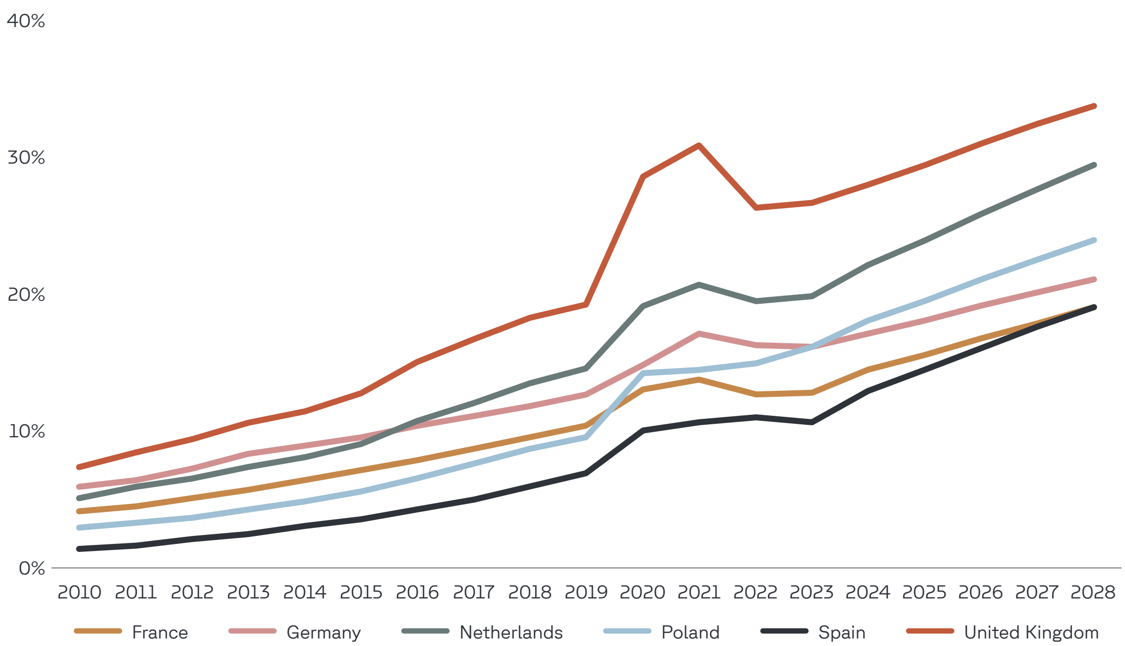
Although the economy is still in recovery mode, we expect three key secular themes to underpin demand for modern logistics space;

1. Continuation of e-commerce tailwinds and further adoption
2. Reconfiguration of supply chains and on/reshoring
3. Need for operational efficiency and sustainability

These themes hold significant potential for driving demand for modern quality logistics stock which we believe strongly favors a development-led strategy.

E-COMMERCE: We anticipate future growth in e-commerce to drive demand for logistics space. During the pandemic, online retailers expanded rapidly, occupying in a few months space what it would normally take them years to acquire. The pandemic era boom in e-commerce has weakened, though it is reverting to its pre-pandemic growth trend (**Exhibit 2**). We estimate that e-commerce accounted for 16% of European retail sales in 2023 and that this share will increase to 23% by 2028.[3] **It is estimated that for each incremental $1 billion in growth in e-commerce sales, there needs to be an additional 1.25 million square feet of distribution space to support the channel growth.** On this basis, we estimate demand for over 460 million square feet of additional logistics space in Europe over the next 5 years.[4]

EXHIBIT 2: INTERNET SHARE OF ALL RETAIL (E-COMMERCE PENETRATION)



Source: CBRE, June 2024

SUPPLY CHAIN RECONFIGURATION: Demand for logistics space in Europe is also being catalyzed by the reconfiguration of supply chains. **The movement from just-in-time to just-in-case strategies, centered around holding more inventory to protect against supply chain disruptions, continues to drive logistics demand.** Supply chains were put under immense pressure during the pandemic with retailers and manufacturers accumulating safety stock in locations close to their end-users to minimize disruption. We expect logistics occupiers to continue to look for more space and redundant space to insulate their positions against supply chain disruption.

3. CBRE. Q1 2024. Europe defined as Belgium, Czech Republic, France, Germany, Italy, Netherlands, Poland, Spain, U.K.
4. Affinius Capital Research and Statista. E-commerce Europe, Accessed June 24, 2024

Related to this trend, is a move amongst some logistics users to nearshore activities in Europe. CBRE's 2024 European Logistics Occupier Survey revealed 68% of survey respondents believe nearshoring will have a significant effect on Europe's logistics take-up, with Central Eastern Europe (CEE) and South Eastern Europe (SEE) expected to benefit most from this trend. Nearshoring, or the movement of production closer to end consumers, is not new, but it is on the rise. More companies mentioned nearshoring in 2023 earnings calls than any previous year since 2010, when data collection began, according to HSBC analyst Mark McDonald.[5] **The rising costs of labor, cost of transport, geopolitical factors, and social impact, amongst others, are driving businesses to examine their sourcing and supply chain strategies. As a result, European businesses are increasingly considering nearshoring of production and supply.**

OPERATIONAL EFFICIENCY & SUSTAINABILITY: We continue to see a strong preference amongst occupiers for modern purpose-built logistics facilities. E-commerce fulfillment typically requires faster order processing and quicker delivery times. Modern, often larger facilities, are better equipped to integrate automation and robotics, resulting in superior operational efficiency. Tenant expectations and environmental regulations also necessitate a focus on modern logistics space. In the wake of the energy crisis in 2022, many occupiers have put a greater focus on energy-efficient space. There is also an increased preference for highly amenitised logistics facilities. The influence of Class A office, residential, and hotels is being implemented in logistics buildings and creating further differentiation of new buildings in terms of human comfort and employee attraction/retention, as well as employee wellness. **Occupiers' preferences point toward modern stock or significant renovation of existing obsolete facilities. We expect this trend to intensify in 2024 and beyond.**

5. FD Intelligence. The Rise of Nearshoring FDI Close to Europe. Published February 21, 2024.

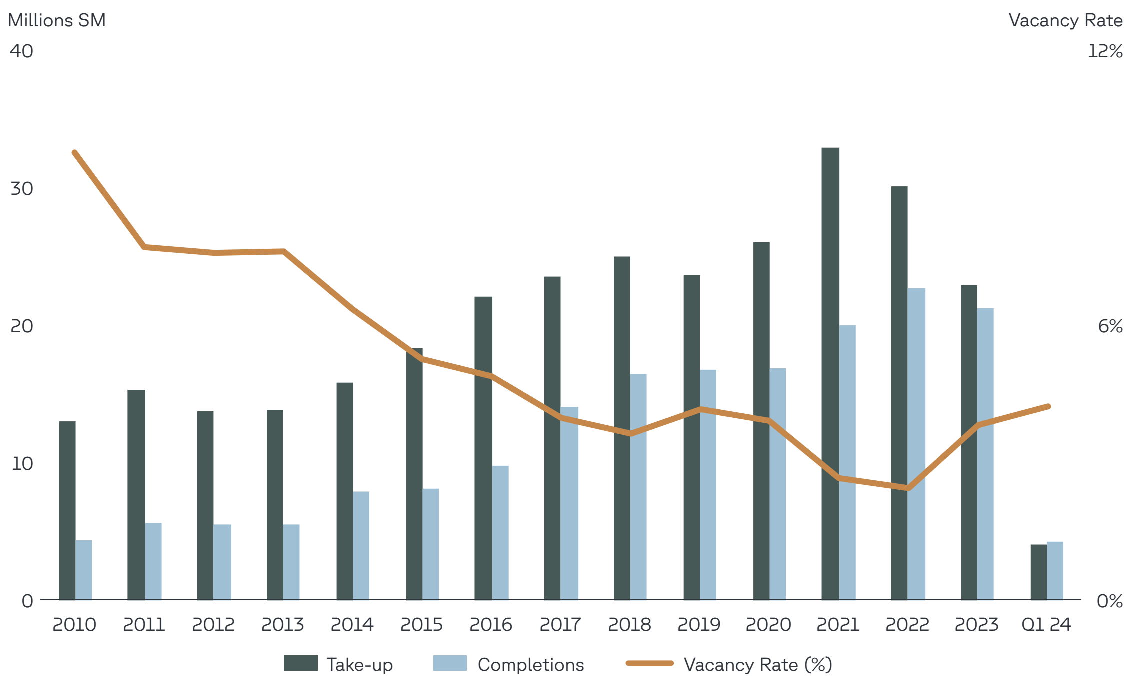
RESILIENT MARKET FUNDAMENTALS

European logistics take-up totaled 21.2 million sqm over the 12 months through Q1 2024. While this was below the 2021 peak figure of 33.1 million sqm, it is still above the previous decade average despite an uncertain economic environment in 2023.[6] In addition, as highlighted in the latest CBRE European Logistics Occupier Survey, occupiers are still in expansionary mode in Europe. **Almost 60% of survey respondents reported that they are planning to expand their European logistics footprint.**[7]

The moderation in leasing activity has only had a minor impact on the vacancy rate which increased to 4.3% in Q1 2024 (**Exhibit 3**), although the growth rate is slowing. Delivery of new supply continued to fall, and completions during the first three months of 2024 marked the lowest quarterly figure seen in over 12 quarters. Space under construction also decreased by over 25% compared with the same period last year.[8]

Low vacancy is continuing to fuel rent growth, **which increased by 5.4% on average over the 12 months to Q1 2024.**[9]

EXHIBIT 3: EUROPEAN LOGISTICS FUNDAMENTALS



Source: CBRE, June 2024

6. CBRE. Q1 2024. Europe defined as Belgium, Czech Republic, France, Germany, Italy, Netherlands, Poland, Spain, U.K.
7. CBRE. Power of Three European Summit May 2024.
8. CBRE. Q1 2024.
9. Ibid

With less supply coming online in 2024, this could be an opportune time to enter the market particularly as we see construction costs softening, rents continuing to grow, steady occupier demand, tenant incentives waning, and yields stabilizing.

We see limited risk of oversupply in the coming years due to high barriers to entry. Notably, we expect the lack of suitable land for development as well as planning and environmental restrictions to control new development with an increasing requirement for the redevelopment of brownfield sites. We believe these barriers to entry will continue to support rental growth and investment values in the sector. In addition, elevated borrowing costs have made it challenging for deals to pencil. As a result, we anticipate new supply will be absorbed more quickly than in the past given the fact that many developers have put the brakes on new construction projects and due to increased focus on new facilities.

GROWTH IN INVESTMENT MARKET

Logistics as an asset class has grown markedly in popularity among institutional investors, due to dependable cash flow, minimal capex requirements and the ability to access locations which can improve over time as cities grow and expand. In Q1 2024, European Industrial and Logistics (I&L) investment increased by 16% compared with the same period in 2023. With total European CRE volumes reaching €37bn (-7% YoY), I&L comprised 22% of this total. Volumes for the last 12 months are still 28% lower than the previous 12-month period (-34% for all CRE sectors) but were in line with the pre-pandemic trend and close to the 10-year average. Industrial values are down by around 20% as yields have risen in a higher interest rate environment, offering a more attractive entry point.[10]

10. CBRE. European Logistics Index. Q1 2024

Logistics has seen the quickest repricing and is now one of the first sectors to see sentiment improve. We think the majority of the valuation adjustment in logistics has occurred, given interest rates are considered to have peaked. The expectation of further rate cuts this year will heighten real estate's investment appeal and should gradually bring investors back into the market. Over the next 12 months, the majority of European logistics locations are forecasting yields to remain broadly stable, expecting little movement after continued decompression in 2023. In countries where we have seen strong repricing, such as in the UK, we can expect to see some inward yield movement over the year.

We see an opportunity to develop logistics assets in Europe with a broad appeal to occupiers and eventual institutional buyers. Healthy occupancy levels, and a compelling spread between the cost of new development and the market value of stabilized assets, provide a compelling investment opportunity. Although the market has matured over the last decade, there is further to go with Europe providing one-third as much warehouse space per capita as North America. **Development provides an opportunity to mitigate the risks of both physical obsolescence and low tenant renewal probability.** New, state-of-the-art logistics facilities that meet occupier requirements including higher clear heights, deeper truck courts, better site maneuverability, and a greater focus on sustainability and worker welfare, will have characteristics that improve second-generation renewal and re-letting probability.

We believe that pricing still adequately reflects a premium for development risk, and, with rent growth, will become increasingly accretive. As ever, site selection is critical, but we believe now is a good time for development and the next wave will be a good vintage. The land market appears to be recovering faster than in past cycles given the scarcity of consented land; however, we are well positioned to benefit from the current opportunity in the logistics sector. **The combination of having a significant consented land bank available for development, well-capitalized development partnerships, and long-term relationships with occupiers allows us to deliver best-in-class buildings that will remain resilient as we progress through the real estate cycle.**

CONCLUSION

Demand for European logistics space maintains a strong upward trajectory. New sources of occupier demand are being driven by i) E-commerce, ii) Reconfiguration of supply chains, and iii) Operational efficiency & sustainability. We anticipate vacancy rates will remain low given the combination of strong demand and constraints on development including the availability of consented land. **The scarcity of locations with planning approval and growing demand for modern distribution and logistics space has created an opportunity to generate significant gains from taking land successfully through the planning process.** Persisting supply-demand imbalances have contributed to strong rental growth, and we believe market rents will continue to increase due to continued strong demand and the scarcity of available modern space. We believe the current capital reallocation to the logistics sector is set to last and will be supportive of the market in the medium and longer term. With positive demand-side dynamics and continued robust fundamentals, logistics development provides an attractive investment option.

JUSTIN HILDEBRANDT

Senior Managing Director,
Head of Europe

justin.hildebrandt
@affiniuscapital.com

KAREN MARTINUS

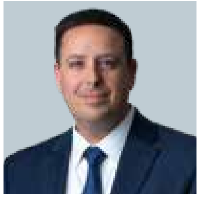
Senior Vice President,
Research and Investments

karen.martinus
@affiniuscapital.com

MAX VON BELOW

Managing Director,
Global Investor Group

max.vonbelow
@affiniuscapital.com



PAUL SEGRETO

Managing Director,
Logistics/Industrial

paul.segreto
@affiniuscapital.com

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AFFINIUS CAPITAL

WTC Amsterdam Tower One
Zuidplein 94
Amsterdam, NL 1077 XV

affiniuscapital.com