Newsletter (3) - Megatrends in Real Estate

(1) Introduction

In today's edition of our weekly newsletter, we explore megatrends reshaping the real estate industry. For real estate investors, understanding these structural supply-demand imbalances often drives investment decisions. In the following, we will examine how aging populations, urbanization, deglobalization, and immigration are influencing the real estate industry and presenting fruitful investment strategies.

(2) Aging Population

Firstly, a major demographic megatrend is the shift toward an aging global population. While this trend is not uniform across all economies, it is particularly evident in more mature CRE markets such as Western Europe, the US, and Japan. For instance, JLL forecasts that the 75+ population will grow 44% in the next ten years, compared with just 5% overall. This demographic shift presents both challenges and opportunities for the real estate industry, especially in two areas: health and social care provision, and housing.

As societies grow older, the strain on health and social services intensifies. This aging cohort will start to live longer and will face more complex healthcare needs. Consequently, there's a higher demand for enhanced health and social care services specifically designed to cater to the needs of retirees. This shift is not just a challenge but an opportunity for real estate developers and investors to innovate in providing specialized care facilities. As such, in anticipation of future demographic-driven demand, KKR has raised a $4 billion fund aimed at investing in healthcare facilities.

In addition, the aging population also creates demand for the residential sector, particularly in senior living. Today's seniors are more active and wealthier than ever before. They seek housing that combines luxury with social connectivity, often favoring mixed-use, community-focused environments. Furthermore, surveys of senior living residents show that they especially prioritize good food and highly amenitized spaces, where they can enjoy activities like lectures, movie nights, or small concerts. Additionally, the best senior living facilities offer tiered groupings, allowing residents to remain social and feel young. Their proximity to family and community resources is a priority, creating a vibrant market for real estate developers to explore and innovate. To capitalize on this growing trend, Harrison Street, for instance, has invested over $7 billion in senior housing since 2005. Beyond the structural demand, the sector offers attractive investment opportunities due to relative underregulation, high occupancy rates, and the potential for rent increases. This demographic shift toward an aging population is a defining megatrend, reshaping the real estate industry's approach to healthcare and housing development.

(3) Urbanization

Urbanization has emerged as a megatrend in real estate, reshaping the industry in strong economies and rapidly growing cities. Migration to cities allows people to leverage the advantages of improved access to healthcare, education, and job opportunities. Hence, urbanization enables better living standards and career prospects. Correspondingly, the UN forecasts that Europe's urbanization rate will increase from 75% in 2020 to 84% by 2050. This influx of the urban population fuels the requirement for housing, making real estate a pivotal element in supporting urban growth.

However, despite strong demand, the supply of residential real estate remains low, mainly due to strict regulations around tenant rights, price controls, and social housing requirements. While these rules aim to protect tenants and ensure affordability, they often deter developers and investors from the sector. Furthermore, Cushman & Wakefield argues that regulatory uncertainty makes it challenging for investors to commit to long-term projects.

Hence, to encourage more investment in residential real estate, structural changes are needed. Streamlining planning processes and cutting bureaucratic delays would help developers bring projects to market faster. Additionally, a stable and predictable regulatory environment is important to provide investors with the confidence to pursue long-term projects without the risk of sudden policy changes impacting their returns.

These structural adjustments are important to unlocking residential investments and meeting the housing demand driven by urbanization. With a balanced approach, policymakers can create an environment where urban growth and housing supply align to support growing city populations.

(4) Deglobalization

Before the pandemic, companies aimed to maximize efficiency in their supply chains through low-cost offshore manufacturing and typically holding less inventory. However, as the pandemic illustrated, this supply chain model proved unsustainable. Consequently, companies are now focusing on stabilizing their supply chains by onshoring or near-shoring manufacturing and holding more inventory. Furthermore, potential for higher global tariffs on international trade also necessitate deglobalization, thereby reducing the economic risks faced by local production facilities. Additionally, the rise of e-commerce and growing expectations for faster delivery times have accelerated this shift toward deglobalization.

For real estate markets in larger economies, this megatrend is driving strong demand for well-located logistics and advanced manufacturing facilities. To meet customer expectations for quick deliveries, "last mile" logistics centers are especially desired by retailers. These assets require prime access to transportation networks and warehouse designs that support high efficiency (e.g., high dock-door ratios and clear height). Due to this megatrend and the high standards for prime logistic assets, investors are capitalizing on the opportunity. Blackstone, for instance, recently acquired a €1 billion European logistics portfolio with properties across Germany, France, and the Netherlands. Excluding this transaction, Blackstone acquired €2.6 billion worth of logistics assets in Europe over the last 12 months.

While logistics has been a standout beneficiary of deglobalization, sectors like life sciences, semiconductors, and data centers are also seeing shifts towards local production and self-reliance. This trend is reshaping real estate, driving demand for specialized facilities in these strategically important industries.

(5) Immigration

Lastly, immigration has emerged as a megatrend in real estate as people migrate to new countries in search of better opportunities. This trend is particularly evident in Germany, which recently recorded approximately 1.1 million arrivals from Ukraine alone (German Federal Statistical Office). This increase in immigration has significantly impacted the real estate industry, increasing the demand for temporary and permanent housing. As immigrants bring diverse economic positions and cultural preferences, they drive the demand for a variety of housing options, leading to diversification in both rentals and property ownership within the sector. Beyond residential, immigration also induces commercial real estate growth, including retail, office, and industrial properties. Particularly notable is the cultural impact, with international shops and restaurants flourishing in urban areas, further attracting investment and revitalizing entire neighborhoods. Thus, the megatrend of immigration requires a high level of responsiveness from the real estate industry. To effectively capitalize on these evolving markets, industry stakeholders must adapt to the changing demands and preferences brought about by immigration.

(6) Conclusion

In conclusion, megatrends are reshaping the real estate investment landscape, creating opportunities for certain asset classes while posing challenges for others. We look forward to exploring each asset class in depth to understand how their viability will evolve in the coming years.