Real Estate House View

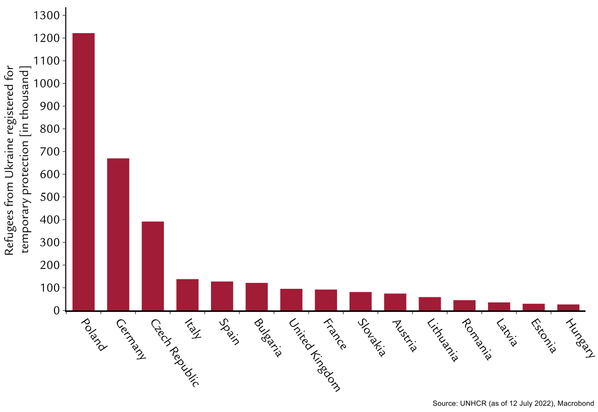
Poland, Czech Republic, Hungary

Second half-year 2022

Key takeaways

- **Investors strongly influenced by war in Ukraine:** Many foreign investors are currently viewing Eastern Europe critically and causing a significant reduction in transaction activity, while yields have switched to an upward trend.
- **Neutral view of the office markets:** The economic outlook is deteriorating, and construction activity is simultaneously decreasing. We view potential for rental growth with cautious optimism and need to differentiate locally.
- **Retail markets must continue to be differentiated:** High inflation is also dampening the retail trade in the consumption-friendly Eastern European countries and is ensuring that providers for day-to-day needs such as specialist stores and supermarkets remain the preferred retail category.
- **Deterioration on the logistics markets possible:** Large development plots are reducing rental growth expectations even though the demand for space remains high.
- **Housing markets unchanged**: The inflow of refugees from Ukraine is strengthening the demand for rental apartments and helping to establish rental markets in the CEE countries, above all in Poland.

Chart focus



The war in Ukraine is "very close" to the countries of Central and Eastern Europe and is impacting society, the economy and ultimately the real estate markets. The Ukrainian refugees are influencing the markets as users of properties, be this as private households or persons in gainful employment. However, the scale of these effects is spread significantly across the region: while Poland and the Czech Republic have accepted a large number of refugees, Hungary lags considerably behind and ranks behind small Eastern European countries. From a real estate perspective, the housing markets come first, especially in the hotspot region of Warsaw with around 250 000 refugees.

Owing to their geographical proximity to Ukraine, the countries of Eastern Europe are particularly affected by the greatest geopolitical crisis in over 20 years. Households are suffering from a sharp loss of purchasing power, while in all countries the state budget is suffering from a rising expenditure burden. While government spending is supporting GDP growth in the short term, momentum in the private sector is already slowing down considerably. The purchasing managers' indices for the manufacturing sectors in Poland and the Czech Republic were below the growth threshold of 50 points in the middle of the year. The Czech Central Bank has hiked its key interest rate from 0.25% to 7.0% since May 2021. Investments are accordingly becoming more expensive. A recession over the coming quarters is the most likely scenario for the entire region.

Turning point on investments?

The war in Ukraine is playing a particular role in its neighbouring countries and weighing on the sentiment of foreign investors in the same way as the gloomy economic outlook. Some investors have withdrawn at least temporarily and are waiting to see among other things how the rental markets develop. This is reflected on the investment market by a significant reduction in the volume of transactions in the second quarter of 2022: according to RCA, the volume in Poland, the Czech Republic and Hungary amounted to around EUR 1.4 billion, which is approximately 40% below the level of the previous quarter and 30% down year on year. Yields are on an upward trend and on a market average should gain 10-20 basis points by the end of 2022, also for prime products.

Office markets: thinking in the medium term

The office markets in Warsaw and Prague started 2022 with strong take-up; however, negative effects are to be expected at least in the short term in view of the subdued economic outlook for the region. There is a risk that international corporations in particular could defer their decisions to rent space. At the same time, a lot of new construction is coming onto the market this year in Budapest, thereby driving up vacancies. By contrast, construction activity in Warsaw is slowing, particularly as there are hardly any more plots in the CBD to be developed. This raises the prospect of the declining availability of space and rental growth potential in the years to come. However, downward pressure on rents is to be expected in the coming quarters.

Retail struggling with inflation

Retail volumes had reached pre-pandemic levels again at the end of 2021 and made gains in the first few months of 2022. However, prime locations, where footfall and the volume of tourists remain down, have benefited little. A positive picture emerged from the daily needs sector, and this situation is not set to change in the immediate future in view of the high inflation. Rents at main high street locations are therefore likely to remain under downward pressure.

More caution for logistics

Following strong demand for space and rising rents into 2022, divergent trends are to be expected on the logistics rental market: on the one hand consumption is slowing down due to high inflation, and demand in the retail sector for logistics space is set to lose momentum, while on the other hand demand is being generated by re-shoring to European regions with low-cost labour. The availability of space remains important for future rent development. Project developers have secured large amounts of land above all in Poland in order to be able to meet growing demand. We remain cautious with regard to rental growth potential in the region.

Refugees need homes

Rented accommodation in neighbouring countries has experienced an unprecedented surge since the start of the war in Ukraine. Warsaw is in the focus of this development as a hotspot for refugees, and although in many cases low-cost housing is being sought, wealthy families have also left their home country. Rents have already picked up noticeably this year. This upward trend is set to continue as there is also more demand among the native population: owing to increased financing costs, more households are renting housing than was customary in the past.

Figure 1: Logistics rent development

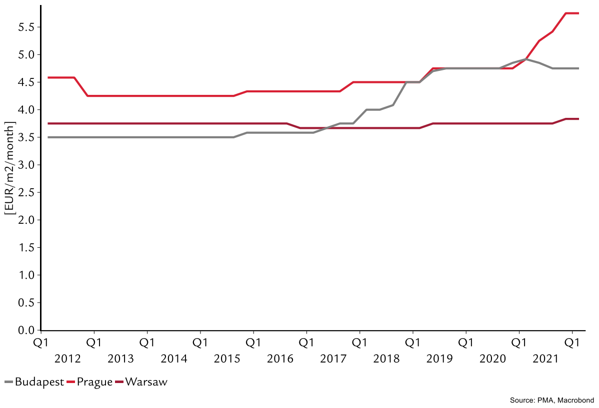
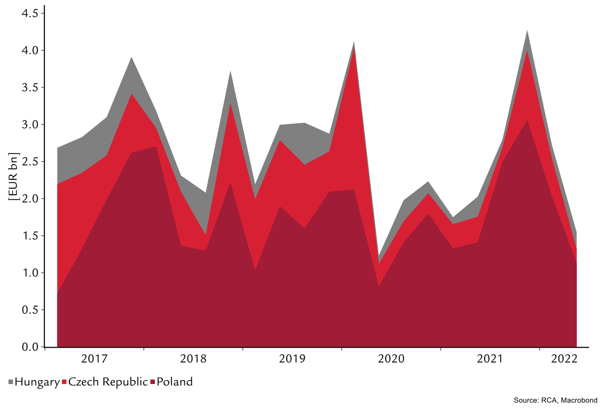


Figure 2: Investment volumes in CEE



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