CEE Investment Market

H1 2019

CEE Investment Market, H1 2019

During the first six months of 2019 the CEE investment market saw a number of transactions for a total in excess of over €5.47 billion.

Poland, with a nearly 50% of that amount, is the clear front-runner and it seems that, due to the extensive pipeline for H2, the country may approach the record-breaking volumes registered in 2018.

In the Czech Republic, which accounted for 30% of those deals, investment appetite remains strong; however, the market there is hampered by a limited supply of prime assets and relatively high price expectations.

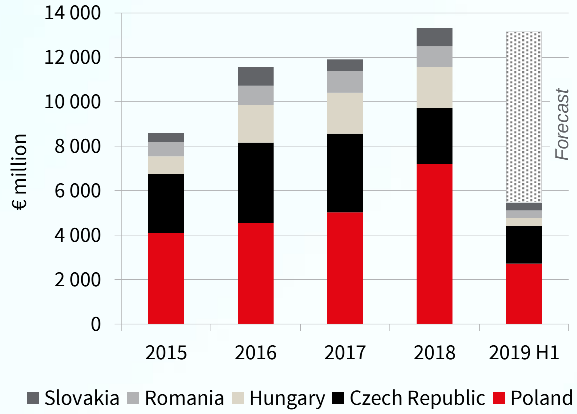
In both countries Asian investors, particularly those from South Korea, have been remarkably active.

The results recorded in H1 in Hungary and Romania may even triple by year-end, reflecting excellent performances, especially with regard to Romania.

The remainder of 2019 should be extremely busy for market players acting on the CEE investment market. In a very positive scenario investment volumes may even outperform the levels seen in the record-breaking 2018.

Over the last 12 months prime yields saw some downward pressures, with the most visible compressions noted in the office and industrial sectors.

CEE Investment Volumes 2015 – H1 2019 & Forecast



CEE Prime Yields (%) – Q2 2019

Country / Sector	Office	Retail (SC)	Industrial
Czech Republic	4.50	5.00	5.50
Poland	4.50	4.90	6.25
Hungary	5.25	5.75	7.25
Slovakia	6.00	5.75	6.50
Romania	7.25	7.00	8.00

Source: JLL, Q2 2019

01. Poland highlights

The Polish Investment market, which in 2018 continued to grow for the 4th consecutive year with a record-breaking €7.2 billion in assets traded, has carried its strong performance into the first half of 2019. The H1 2019 investment volume of €2.72 billion was slightly lower than the result for H1 2018 (€3.22 billion), but still represented the second-best volume ever achieved in the Polish investment market for that period. Yields remained relatively stable across asset classes, with further compression expected by year-end, excluding retail. There were ca. 60 transactions concluded throughout H1 2019, with the office sector dominating the investment landscape both in terms of volume and number of transactions. The split across sectors was as follows: office (€1.67 billion), retail (€430 million), industrial (€374 million), hotel (€135 million), residential (€47 million), and other (€60 million). Asian capital accounted for more than one third of acquisitions in terms of transaction volume, with the Polish office and industrial sectors attracting significant attention from far-eastern capital sources.

During H1 2019, the Polish office investment market was the most active sector, which resulted from transactions that were already at an advanced stage in 2018 and finally closed in H1 2019. Such a strong start into the year was driven by many smaller transactions as well as the following deals exceeding a volume of €100 million each:

- West Station (I+II) in Warsaw was sold by JV of HB Reavis & PKP to Singaporean investor Mapletree for ca. €190 million;
- Henderson Park acquired a 70% stake in EPP's regional-cities office portfolio (Malta Office Park in Poznań, Symetris Business Park I&II in Łódź, O3 Business Park I&II in Kraków);
- Akron sold Warsaw Trade Tower to Globalworth for ca. €133 million;
- Credit Suisse Asset Management acquired Ethos, a revitalised mixed-use project near Warsaw's Old Town, from Kulczyk Silverstein Properties for ca. €115 million.

Interestingly, office investment volumes increased by 78% compared to H1 2018 (€938 million), marking the best result ever in the history of the Polish office investment market. We have recorded the entire spectrum of transactions ranging from core, core+, through to value-add and opportunistic. This remarkable activity is set to continue in H2, with multiple Warsaw office tower deals either in exclusivity or at the PSPA stage as of the end of H1 2019 (combined value of only 3 such transactions exceeding €1 billion). Furthermore, multiple regional office portfolio transactions are expected to close by year-end. Overall, over €2 billion worth of deals are currently in the marketing, DD or PSPA stage.

Prime office yields in Warsaw stand at 4.50% and are expected to move downwards by year-end. Core regional city yields stand at sub 6.00% and are expected to reach 5.5% territory by year-end.

In H1 2019 we have observed significant decrease in the volume of retail investment transactions versus same period of 2018. It must be highlighted, however, that H1 2018 witnessed closing of the record breaking Chariot Portfolio transaction of ca. €1 billion, which alone accounted for over 50% of the overall recorded figure. While certain slowdown in the investment activity in the retail sector is visible the total investment volume already amounted to €728 million as of end of July 2019 with few notable transactions closed, namely:

- Atrium Felicity in Lublin and Atrium Koszalin acquired by ECE Fund from Atrium for €298 million;
- M1 Bytom, M1 Czestochowa, M1 Radom and M1 Poznań acquired by EPP from Chariot Top Group B.V. for €224 million. It is a second tranche of the portfolio deal that was agreed in January 2018. Currently EPP own 8 centres under M1 brand. The third tranche encompassing four Power Parks is expected to complete by June 2020;
- Galeria Leszno sold by Blackstone for undisclosed price;
- King Cross Jubilerska in Warsaw acquired by Atrium from CBRE Global Investors for €43.1 million;
- Silesia Outlet in Gliwice acquired by NEINVER and Nuveen Real Estate from 6B47 Real Estate for €31.5 million.

Prime shopping centre yields remain stable at 4.90% with prime retail park yields estimated at 6.80%.

In the industrial sector, volumes in H1 2019 were reported at €374 million. This marks the best result ever, about 9% above the second-best H1 2018 volume of €344 million. Over 88% of the volume was achieved in Q2, following a slow start into the year. It is worth noting that the result for H1 2019 was dominated by large single-let assets, including the following key projects transacted in H1 2019:

- Amazon, Wrocław and Eurocash, Konin acquired by Hines/Mirae from Blackstone for ca. €130 million;
- Zalando Lounge Distribution Center acquired by Hines/IGIS AM from Hillwood for ca. €85 million;
- Castorama, Stryków acquired by Tritax from Panattoni for ca. €55 million.

As in the office sector, investors with Asian capital sources – particularly from South Korea – were remarkably active in the Polish logistics sector in H1 2019.

Prime warehouse yields stand at 6.25% with exceptional, long leased assets trading at sub 5.00% and Warsaw inner city projects at around 5.50%.

We expect investment into logistics to continue at a very strong pace with both portfolios and large single assets expected to trade throughout 2019.

The Polish hotel sector recorded a volume of €135 million in H1 2019, already exceeding the result for the entire year 2018 (€119 million). Most notably, Sheraton Warsaw was purchased by Patron Capital from Benson Elliot and Walton Street for ca. €90 million.

In the residential sector, LRC Group acquired 175 apartments in Pacific Residence (Solec 24) in Warsaw for ca. €47 million.

We also recorded the first student housing transaction in the Polish market, with a JV of Kajima & Griffin Real Estate purchasing Student Depot for nearly €60 million.

Across the traditional sectors of office, retail, and industrial the H2 pipeline – committed, in due-diligence and in advanced marketing – is substantial, with the total Polish investment volume in 2019 expected to approach the record level achieved last year.

02. Czech Republic highlights

The Czech Republic still reports strong macro-economic performance and continues to be considered as the most stable country with the lowest investment risk rating within the CEE region. Retail sales continue to grow with an increasing importance and share of e-commerce sales. Office, industrial as well as retail occupational markets have registered strong performance, leading to low vacancies across the sectors, supporting the strong fundamentals of the real estate investment market.

These fundamentals brought investment volumes in H1 2019 to €1,683 million in 32 transactions, up 54% y/y. Czech investors keep dominating the market with 44% market share. Investors from South Korea now represent 32% of the market due to the strong appetite for product from South Korean investors. This puts them ahead of more traditional investors in the CEE region due to more aggressive pricing. As Korean investors depart from the UK market due to political and economical reasons, we expect the investment inflow from South Korea to prevail in the rest of 2019.

Office sector dominated, representing 55% of the investment volume. This is mainly due to three large office transactions closed by South Korean investors, namely Waltrovka acquired by Hanwha for €247 million, Main Point Pankrac acquired by Hana Financial for €130 million and Rustonka Office Complex acquired by Hana Alternative Asset Management for €163 million.

Retail sector witnessed 5 transactions with 10% market share. The largest transactions include the acquisition of ca 80% stake from SES in Europark Sterboholy by Czech investor DBK, Novodvorska Plaza by Greek investor Bluehouse and Retail Park Hradec Kralove by Czech investor Conseq. These two acquisitions underline continued strong interest in non-prime retail from Czech investors.

Investors are also more interested in the logistics sector than ever before but struggle to find opportunities for investment. In H1 2019, investment into the logistics sector represents only 7% of the volumes, with Contera Industrial acquired by TPG for €90 million being the most significant one among the 4 other closed transactions.

Investment into hotels sector, typical for its lack of investment product, recorded high activity, attracting €380 milion of investment or 18% of the investment volumes, mainly due to Hotel Intercontinental sold by J&T to local private equity group R2G, one of the biggest hotel investment transactions recorded on the Czech market.

Investor activity and appetite for investment product continues to be strong, however, it is limited by a lack of supply of prime assets and high price expectations of sellers.

In H1 2019, our view on prime yields is as follows: prime offices at 4.50% with further yield compression expected by the end of the year on the basis of currently on-going transactions, prime shopping centres at 5.00%. The industrial and logistics prime yield remains at 5.50%. Prime retail parks are at 6.00% while prime high-street assets would trade at 3.50%.

03. Hungary highlights

Since 2015 three main trends has been impacting the Hungarian property capital markets.

Due to the strong market fundamentals investment activity has been exceptionally strong showing constant growth year-on-year.

Hungarian retail real estate funds, typically long term holders, have represented a growing share of the acquisitions with 44% of the aggregate investment volumes between 2016 and H1 2019 almost without any disposals (regulatory change might impact this trend. See Important Regulatory Change paragraph).

As a consequence of the above and the limited pipeline of new projects (especially in the industrial and retail sectors), the supply of products available for sale has dried out.

By H1 2019 the effects of the above three trends became undisguisable. Investment activity during the first half of 2019 reached a mere €400 million, the lowest half-yearly volume for the past 4 years.

Based on the pipeline of transactions we expect the 2019 annual volume to remain 10%-15% below the 2018 level at around EUR 1.4-1.5 billion. Despite the fact that the interest for the Hungarian CRE market and the available equity from investors has never been so high since the GFC, volumes are constrained by the lack of products.

The strongest transaction activity was recorded in the office asset class, which generated 70% of the half-year volume followed by industrial (13%). Interestingly 10% of the volume was generated by development deals including development plots and unused properties in prime locations. The remaining 7% was made up by two hotel transactions and a small countryside shopping centre disposal.

The most significant transaction of the period was the disposal of White House, a new office development of 21,600 sq m by GTC. The property was acquired by a new market entrant, the German investment manager, Warburg HIH on an off-market basis for an open-ended fund for an institutional buyer. The transaction illustrates that committed international investors are able to unlock core properties in Hungary, despite the perceived hegemony of local funds.

Further important deals in the sector included the disposal of Advance Towers by Futureal to ERSTE RE Fund, the acquisition of the monument protected Andrássy 11 and Andrássy 12 office buildings, with a substantial high street retail component, by AEW Europe and the acquisition of Infopark B, C, I and Liget Center by WING.

Indotek continued its deployment of capital in countryside retail with the purchase of Duna Center, a strip mall in Győr, an important regional city in North-West Hungary. Over the recent years the investor became one of the leading landlords of countryside retail schemes by building up a significant portfolio.

In the logistics asset class, due to the limited supply and rotations of assets, investments remained subdued reaching ca €56 million (2 transactions) in H1 2019.

The largest single park deal of the past 6 years was concluded in H1 2019 with the disposal by M7 Real Estate of the 60,000 sq m Aerozone Business Park to the South African JT Ross Property Group, a new entrant on the logistic market in Hungary and a logistic specialist.

As supply is very limited in every asset class, prime yields are under pressure. After a 50 bps decline, we see the prime office yield at 5.25% with high street retail at 5.25%, shopping centres at 5.75% and industrial at 7.25% with significant compression forecast.

Although we expect investor appetite to remain strong in 2019 with liquidity in all asset classes and segments of the market from value add to core, the annual volume is forecast to remain below the 2018 level as a result of the supply constraints.

Important regulatory change

Effective from May 15, 2019 redemption time of newly issued shares in public open-ended real estate funds increased to 180 days (from 3 days). The aim of the regulation is to decrease the liquidity gap between the shares and underlying instruments held by the funds. We expect the change to slow down the collection of new capital from retail savings; but the rebalancing of the liquidity risk towards end investors may also entice the fund managers to increase their exposure towards fixed assets. The impact of the regulation shall become clear in the coming months.

04. Romania highlights

The H1 2019 property investment volume for Romania is estimated at circa €338 million, a value almost 64% higher than the one registered in the same period in 2017 (€205 million). However, there are a number of transactions in different stages of negotiations that will most likely be concluded during the remainder of 2019 or 2020

The number of transactions increased, however, the average deal size decreased, standing at approximately €25 million.

Bucharest accounted for over 27% of the total investment volume, mainly because of a very large office transaction which was closed in Q2 and a retail portfolio transaction closed in Q1, both in secondary cities. Market volumes were dominated by office transactions (52%), while retail accounted for over 33%.

The largest transaction registered in first half of 2019 was the acquisition of The Office, a 60,880 m^2 office park in the CBD of Cluj-Napoca, the second most important office market in Romania, by Dedeman. This is the first acquisition of a private Romanian group in a secondary city in the country and the second acquisition in Romania, after buying The Bridge in the Center-West sub-market of Bucharest.

Other notable office transactions in Romania were the acquisition by a private group of former First Bank HQ in the CBD of Bucharest for €20 million and the acquisition by Hagag Group of the Stirbei Palace, a historical building in the center of Bucharest which they plan to reconvert into an office scheme, for an estimated €10 million.

The largest and only retail transaction concluded in the first half of 2019 was the acquisition of an 80% participation in a portfolio of 9 retail parks in several cities across Romania by Mas REI from Prime Kapital. The South African group already owned 20% in the assets and paid for the participation an estimated €113 million.

The most important industrial transaction was the acquisition of a logistic park on the A1 Highway, at the Km. 13, the most important sub-market in Bucharest. Bought by CTP from Vabeld for approximately €40 million, the deal consolidated the position of CTP as the largest owner of industrial/logistic space in Romania.

The macro-economic forecast for Romania continues to be positive, despite some recent concerns. The country was one of the EU's top performer in 2018 (with GDP growth estimated at 4.1%) and is expected to continue its positive evolution in 2019 as well, with GDP increase forecast at over 4.0%. On the financing side, terms and conditions are getting closer to what can be expected in the core CEE markets. Consequently, sentiment is strong, with a total volume for 2019 estimated to surpass the €1.2 billion mark.

Prime office yields are at 7.25%, prime retail yields at 7.00%, while prime industrial yields are at 8.00%. Yields for retail are at the same level as 12 months ago, while office and industrial yields have compressed by 25 and 50 bps respectively over the year. There is a very soft downward pressure on yields, however, for the rest of 2019 we do not expect any compression, especially for retail and industrial, mainly due to the lack of prime product transactions.

05. Slovakia highlights

Through 2019 the Slovak real estate market bolsters its position as a stable investment destination. Interest from regional as well as international investors remains high, with increased transparency and new entrants among the positive signs.

In H1 2019 the total transactional volume approximates to €350 million of which €148 million - 42% share belongs to office asset class, €108 million - 31% to industrial and €43 million - 12% to retail asset class. Y-o-Y transactional volume is 31% lower compared to H1 2018, result of lengthy transaction processes and change in immediate availability of equity.

Whereas office and industrial sectors are experiencing continuing momentum, volumes in the retail sector dropped as majority of dominant retail schemes changed hands in recent years.

The office sector registered two important transactions in H1. The first significant transaction took place in Bratislava marking an entry of Korean capital into Slovakia. Mirae Asset Daewoo and NH Investment & Securities represented by AIP Asset Management and London – based Valesco Group acquired the Twin City Tower. The asset developed by HB Reavis traded for €120 million, reflecting CBD location and institutional tenant base with major covenant Amazon, which signed a long-term lease.

Bratislava is currently also on the radar of other Korean investors along with the main CEE investment capitals – Prague and Warsaw - which witnessed strong yield compression. From initial preference for single tenant assets with long wault, we see a shift to multi-let schemes with shorter wault of desired transactional volume and quality prime assets.

The second important transaction took place in 2nd largest Slovakian city Kosice. We witness international capital to invest in CEE regional cities infrequently, with the exception of Polish regional cities. It is therefore of significance that such deal has been concluded in Kosice. Business Centre Tesla 2, developed by Penta Real Estate, offers 14,600 sqm of office space leased to institutional tenants such as T-Systems, Deloitte and Diebold-Nixdorf. The buyer, ECE European City Estates, has also secured the upcoming Business Centre Tesla 3 via forward purchase agreement.

Three transactions took place in the retail sector in H1 of which two schemes – old Tesco department store and Shopping Palace, are in Bratislava. Interest from investors persist in regionally dominant shopping schemes with good tenant mix and large catchment areas, however this type of product is currently very limited.

View on yield on prime shopping schemes currently differs between owners and investors what creates adverse conditions for such deal to happen. Retail parks stand to be liquid assets as local investors are succeeding recently active Austrian investors. Should any of the major retail schemes in Bratislava change hands in 2019 we could see higher volumes to be traded in H2.

Activity in industrial sector continues as three transactions took place in H1, some of which started in 2018 slipping to 2019. Most notably a portfolio deal struck between Prologis as the seller and CNIC – an investment company owned by the Chinese government as the buyer. The portfolio consists of 4 halls (standing & u/c) of total GLA of ca. 120,000 sqm in locations of Nitra and Ziar nad Hronom. Additionally more than 140,000 sqm of industrial/logistics assets set in Western Slovakia has been in various stages of due diligence in a couple of deals, likely to close in the upcoming months.

Ongoing investment activity, especially in industrial and office sector (committed deals worth ca. €130 million in both asset classes) substantiate the fact that similar transaction volume to H1 should be achieved in the second half of the year.

The predicted annual investment volume could therefore reach ca. €700 – €750 million.

Evidenced by recent transactions our view on prime yields has moved as follows: shopping centres 5.75%; offices 6.00% (WAULT of 5 years); retail warehouse 7.00%; industrial & logistics 6.50% (WAULT of 5 years) and hotels (operations) in the capital at 7.00%.

06. Key deals

Property name	City, Country	Approximate sale price (€ million)	Vendor	Purchaser
M1 Portfolio (II tranche)	Bytom, Częstochowa, Radom, Poznań, PL	224	Chariot Top Group	EPP
Galeria Leszno	Leszno, PL	Confidential	Blackstone	Undisclosed
King Cross Praga	Warsaw, PL	43.1	CBRE GI	Atrium European RE
Amazon Wrocław & Eurocash Konin	Wrocław, Konin, PL	ca. 130	Blackstone	Hines/Mirae
Zalando Lounge DC	Olsztynek, PL	ca. 85	Hillwood	Hines/IGIS AM
Castorama Stryków	Stryków, PL	55	Panattoni	Tritax
West Station	Warsaw, PL	190	JV HB Reavis / PKP / Xcity Investment	Mapletree
EPP Regional Office Portfolio (70%)	Poznań, Łódź, Kraków, PL	ca. 137	EPP	Henderson Park
Warsaw Trade Tower	Warsaw, PL	133	Akron	Globalworth
Ethos	Warsaw, PL	115	Kulczyk Silverstein Properties	Credit Suisse AM
Business Garden (Phase I)	Wrocław, PL	95	Vastint Group	ISOC Holdings
Alchemia III (Argon)	Gdańsk, PL	92	Torus	ISOC Holdings
Diamant	Prague, CZ	80	GLL	BMO
Waltrovka	Prague, CZ	247	Penta	Hanwha
Hotel Intercontinental	Prague, CZ	225	J&T	R2G
Europark	Prague, CZ	Confidential	SES	DBK
Contera Industrial	Various, CZ	90	Contera	TPG
Main Point Pankrac	Prague, CZ	130	PSJ Invest	Hana Financial Investment
Rustonka	Prague, CZ	163	J&T RE	Hana Alternative Asset Management

06. Key deals

Property name	City, Country	Approximate sale price (€ million)	Vendor	Purchaser
GTC White House	Budapest, HU	60-70	GTC	Warburg HIH
Advance Tower	Budapest, HU	45-55	Futureal	ERSTE RE Fund
Aerozone Business Park	Budapest, HU	40-50	M7 Real Estate	JT Ross Property Group
Infopark B, C, I	Budapest, HU	35-45	Lonestar	WING
K+K Hotel Opera	Budapest, HU	30-40	Highgate Holdings, Goldman Sachs	Event Hotels, InterGlobe Enterprises
Andrássy 11&12	Budapest, HU	15-25	HGA	AEW Europe
Liget Center	Budapest, HU	Confidential	M7 Real Estate	WING
Retail portfolio of 9 shopping centers	Secondary cities RO	113	Prime Kapital	MAS Real Estate
First Bank headquarters	Bucharest RO	20	First Bank	private local
Industrial park A1 km 13	Bucharest RO	40	Vabeld	CTP
The Office	Cluj-Napoca RO	125	NEPI Rockcastle and Ovidiu Sandor	Dedeman
Prologis Portfolio	Various, SK	Confidential	Prologis	CNIC
KIK GoAsset	Dunajska Streda,SK	Confidential	Go Assets	Gramercy Europe
Business Centre Tesla 2	Kosice, SK	Confidential	PENTA	ECE European City Estates
Twin City Tower	Bratislava, SK	120	HB Reavis	Mirae Asset Daewoo & NH Investment via Valesco and AIP AM

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