CEE REAL ESTATE LANDSCAPE – THE MARKET AT A GLANCE

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The widespread perception remains that the real estate market in CEE is undervalued and continues to offer exciting opportunities for investors. It would seem this is with good reason and early signs suggest that this year we may approach record levels of activity in the sector.

Funds from continental Europe, including Germany and Austria, remain the most active in the region. An interesting development is the evidence of a heightened level of interest from the Middle East and Asia, particularly in terms of the long-expected arrival of Chinese capital.

The market sentiment and investment approach parallels that of 2017. The vast majority of investors are long-term property holders with a view of owning the property for decades rather than years. First and foremost, investors are seeking income-producing assets and yield compression continues.

The shortage of core real estate investment opportunities has naturally resulted in increased demand. Investors are particularly attracted by properties which can readily be leased to good tenants under long term lease agreements. This is particularly the case in regional cities, if such assets are available.

Analysis of Asset Classes in CEE

The above qualities in real estate continue to be the key drivers of investment in the sector, yet there are several noteworthy developments with respect to interest in asset classes.

High-end offices continue to attract a substantial amount of attention from investors as demand increases for hyper-modern spaces which can accommodate and lure the interest of millennial employees.

Meanwhile, as a result of the shortage of supply for high quality commercial real estate, there has been an increased interest in prime residential assets by international property funds.

There was also another sound year of transactions in the hotels sector, although there is an observable gap in SEE between the high demand and low offer of all quality hotels for sale, especially along the Adriatic coast. This gap is expected to grow as a result of the current anti-short-term lodging propaganda.

With respect to logistics, activity was exceptionally high in Eastern Europe, with the market share averaging above 30%.

The largest talking point remains the relationship between the retail and logistics spheres. As has been widely reported, the US retail market has hit the floor and leasing rates have had to be adjusted accordingly. Suggestions have been made that CEE may go down the same path. State-of-the-art retail properties which showed a world of promise in the 80s and 90s now appear empty and dysfunctional and many have suggested that in capital cities the market has been saturated with available retail space over the recent decades, resulting in many dormant shopping malls.

It can largely be said that the prediction the retail market would collapse, to be replaced by high tech e-retail and consequent distribution real estate, has yet to be borne out. In 2017 transactions in the retail sector far outperformed any other asset class and the market remains as buoyant as ever.

Particularly in SEE, traditional shopping mall targets have attracted a significant amount of attention in recent times – as opposed to office buildings or heavyweight logistic centers. We have also witnessed a growing interest in the social infrastructure facilities, including elderly housing solutions. This corresponds directly with the demographic trends in CEE that resemble those in continental Europe and the UK, but this is also a very regulated sector and finding the right operating model can be challenging. It will be interesting to see whether this will develop into an increased interest in general housing or student housing solutions or other forms of assisted living, healthcare, and medical facilities.

It would appear that the retail market is being pulled in different directions throughout CEE. On the one hand there are surging economies with growing prosperity, yet the market is perhaps being compromised by the swelling demand for e-retail.

Unlike the United States, we have yet to see any significant evidence of the closing down of shopping centers, and rental costs for retail space remain as expensive as ever, especially with major new international retailers entering the market. Notably, across CEE we also see many new shopping centers under construction.

Modern premises have been substantially adapted to modern technology. In the regional cities of Poland and the Czech Republic the implementation of technology – for instance in various forms of rapid self-service checkouts – is advancing at an unprecedented pace.

It is interesting to consider the typical elements of a shopping center, which include various retail outlets, a supermarket, a parking area, a gym, a food court, and cinemas. To varying extents it would seem the need or desire for these elements can be questioned, although with respect to gyms, wellness centers, cinemas, and food courts it is hard to see any viable replacement.

It is these sorts of social elements of shopping malls that appears to be immune from advancements in technology. Particularly in the parts of CEE countries that are far from national capitals, shopping malls are viewed as trendy and attractive meeting places which many would designate as the landmark of their community.

It remains to be seen if the path of US will be followed, but as one of the most rapidly changing areas in real estate, investors will certainly closely monitor how retail evolves in the near future.

Outlook Moving On to 2019

As is typically the case in CEE, the market will be dictated by how the economies of the CEE countries will perform, and more importantly how the world's economy will perform. If we continue to see strong economic growth in the region the demand for real estate will continue at the current level.

A slowdown in the world's economy would have an immediate strong impact on the emerging markets, including CEE. Particular places to watch are Romania and Bulgaria, which due to an economic boom have experienced a substantial growth in demand for real estate.

On a more high-tech note, it will be interesting to watch and shape the effects of blockchain, augmented reality, machine learning, and AI on the movements on the real estate market. It will be more important than ever to keep an eye on developments in the IT industry.

More than ever, lawyers should be able to quickly adapt and adopt these new technologies. For industry middlemen such as realtors and other agents, the unstoppable rise of peer-to-peer communication continues to serve as a secondary channel of services and represents a significant threat to them of being by-passed.

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