Poland Investment, Q4 2017

Portfolio deals dominated the Polish investment market

Volume 2017 EUR 5 billion

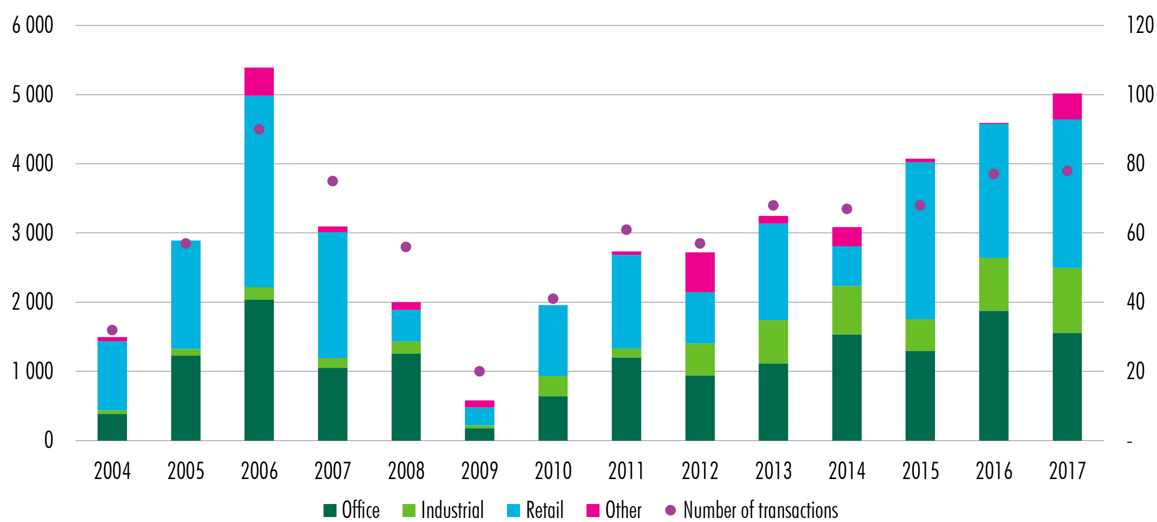
Prime yield retail 5.15%

Prime yield office 5.20%

Prime yield industrial 6.00%

*Arrows indicate change from the corresponding quarter in the previous year

Figure 1: Investment market in Poland – breakdown by type of property (in EUR million)



Source: CBRE Research, 2017

SUMMARY

- The last quarter of 2017 was the most active quarter since the end of 2015 with total volume amounting to more than EUR 2.5 bn. Investment activity in the whole year exceeded EUR 5.00 bn., equating to the highest volume since the peak in 2006.
- Investor activity focused mainly on the retail and office sectors which amounted to EUR 2.15 bn. and EUR 1.55 bn., respectively.
- Industrial & logistics was dominated by one single pan-European portfolio transaction, which accounted for 81% of total volume in the sector.
- New record volume was registered in the hotel sector, with total activity higher than EUR 0.35 bn.
- Investor interest was also directed towards alternative investment–new single PRS deals were recorded on the market.
- Prime yields are on a continuous compression path in all sectors of the commercial real estate market in Poland.
- Almost 55% of total volume was traded in portfolio transactions representing the greatest share in the history of the Polish investment market.

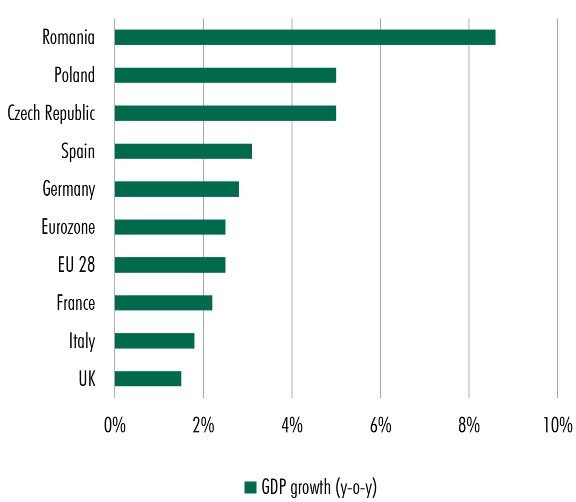
ECONOMIC BACKGROUND

The European economy is in good shape and this is reflected in property investor sentiment. The positive trend in the European economy influences directly on the development of the Polish real estate market. Investor commitment is supported by the great performance of the Polish economy, which is one of the leaders of growth not only in CEE but throughout the whole European Union as well. The main driver of GDP growth (5.0% y-o-y at Q3 2017) is robust domestic demand, which is supported by favourable labour market trends and record-high consumer confidence.

The low interest rate environment and economic growth in the EU have resulted in record-breaking capital inflows on the real estate market which is still attractively priced when compared to the yield on ten year government bonds – a benchmark for the yield on a 'risk-free' investment. The spread between prime office yields and the risk-free rate is currently around 250bps (Eurozone prime assets), which is 40bps above the 15 year average. It is important to note that these benchmark yields refer to the prime segment; looking at secondary yields, the market is attractively priced from a historic perspective.

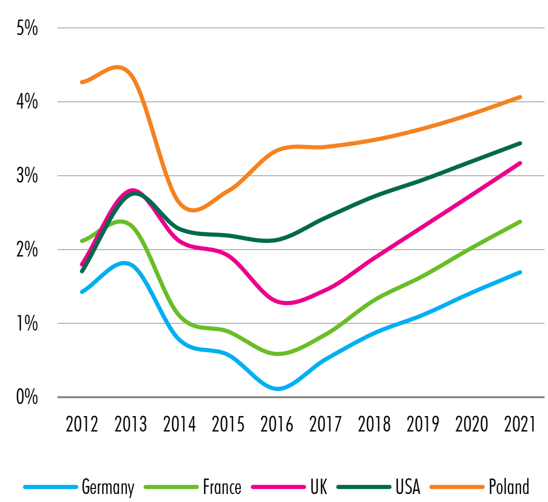
Global 'Assets Under Management' are forecast to grow by an annualised 6.2% between 2016 and 2025 (PwC, 2017), driven by inflows from high net-worth individuals and retirement savings. Due to growing transparency, diversification strategies and an ongoing search for yield, AUM in alternatives – including real estate – are expected to more than double in size over the same period. This will fuel further competition between investors in the search for products in which to deploy capital. Taking into consideration all of the above conditions, a developing economy with healthy fundaments like Poland with its still attractively valued real estate assets, could be one of the major beneficiaries of global trends.

Figure 2: GDP growth in selected countries (Q3 2017, y-o-y)



Source: Eurostat, Q3 2017

Figure 3: Ten-year government bond yields (2012 – 2021)



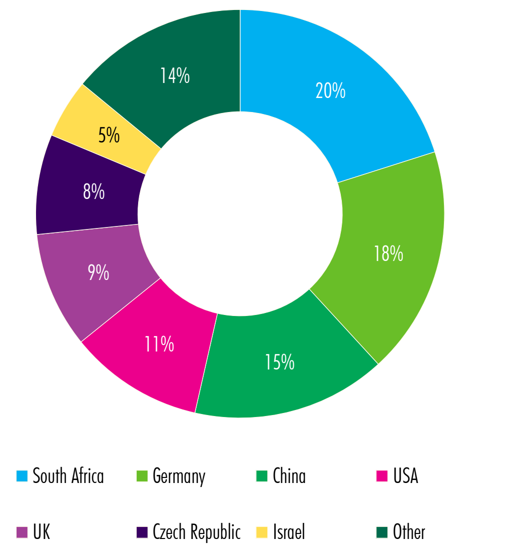
Source: Oxford Economics, 2017

INVESTMENT MARKET SUMMARY

As in other European markets, the Polish investment market continued its growth path in 2017 recording a 11% increase y-o-y and being 25% above the 5-year average in terms of total volume. The main drivers of this surge were the retail and office sectors, but noticeable investment growth was registered in the hotel sector as well.

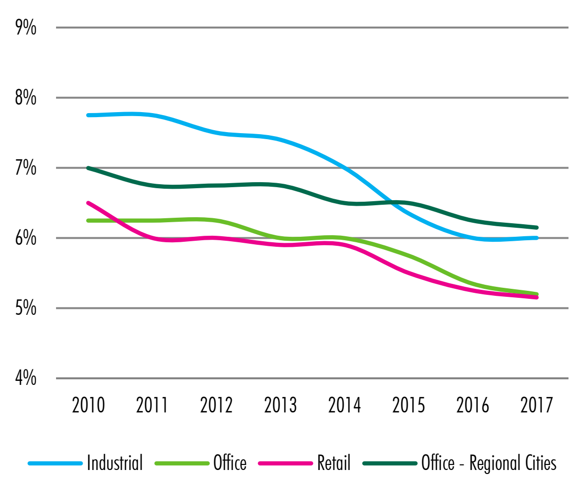
It is worth mentioning that more than 55% of volume was transferred in portfolio deals, keeping the market in line with major European trends. The EU market is entering a consolidation phase, and the maturing of the cycle will fuel demand for merger-and-acquisition (M&A) type transactions as investors are increasingly resourceful in finding exposure to real estate. Since the end of 2016 the main pan-European portfolio deals, which also involved Poland, were the sale of P3 (EUR 2.3 bn.) to Singapore fund - GIC, the purchase of Logicor (EUR 12.3 bn.) by CIC and the acquisition of Triuva by Patrizia. These mega deals are part of a broader consolidation phase that is not confined to the real estate market, but is illustrative of the maturing of the cycle. Furthermore, the largest portfolio transactions in Poland include the acquisition of Griffin Premium RE by Globalworth RE, the sale of an IKEA Retail Portfolio to Pradera and the purchase of the Fashion House Portfolio by DAWM.

Figure 4: Origin of investors in 2017 (%)



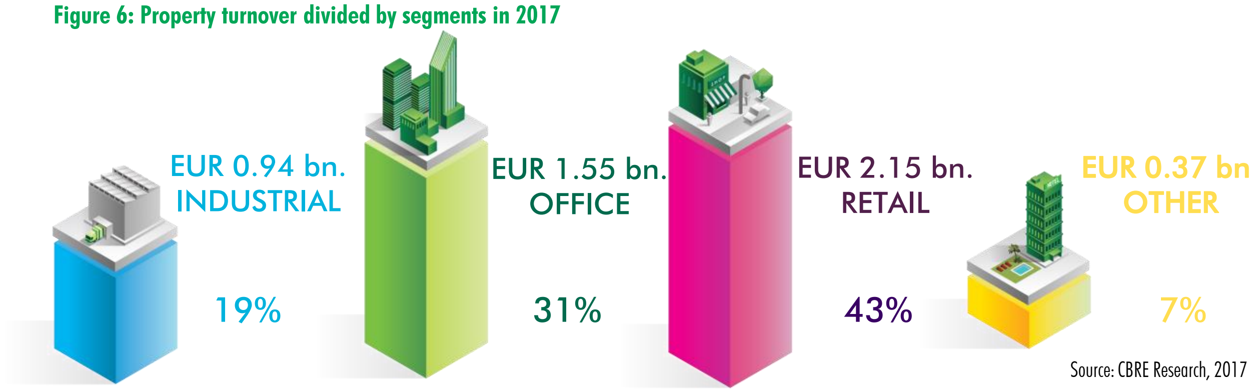
Source: CBRE Research, 2017

Figure 5: Poland prime yields



Source: CBRE Research, 2017

Figure 6: Property turnover divided by segments in 2017



Source: CBRE Research, 2017

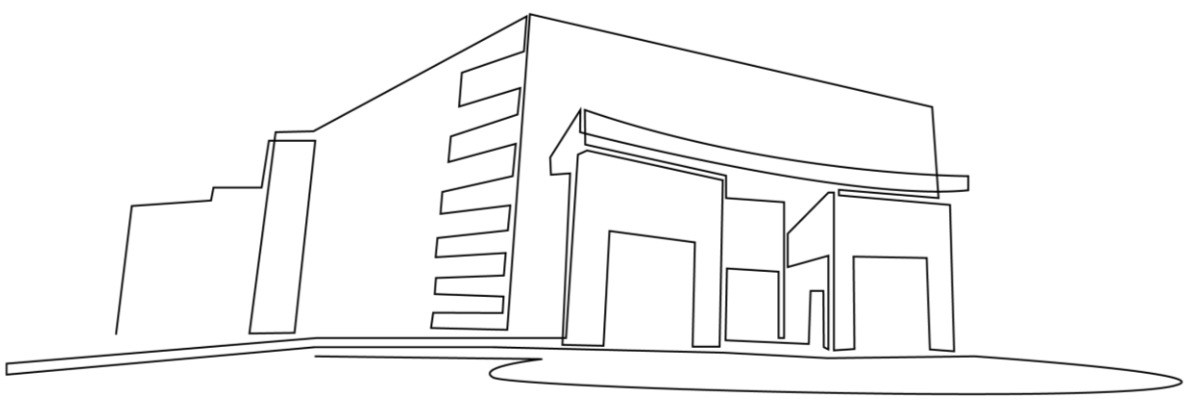
RETAIL MARKET

The retail market is boosted by similar drivers to the Polish economy e.g. robust domestic consumption and a tightening labour market with significantly high consumer confidence. Currently, all classes of retail assets, from prime shopping centres to suburban hypermarket-anchored galleries, are in demand.

The retail market remains bullish, however some issues could result from the implementation of the Sunday trading ban which will come into force in March 2018. The latest signed bill assumes a trading ban on two Sundays per month in 2018, three Sundays per month in 2019 and all Sundays in 2020. Although the trading ban has also been established in other European countries, objections have arisen in Poland as a result of the fast resolution process and short implementation period. On the other hand, CBRE assumes that investors will adjust to the new law and changes will be reflected in pricing and customer behaviour as well.

Apart from the portfolio transactions, such as IKEA or Fashion House, the most significant single deals were the acquisition of Magnolia in Wroclaw, purchase of Galeria Sloneczna in Radom and disposal of Alfa Bialystok. Robust demand for retail assets has exerted downward pressure on yields and prime retail assets are valued at yields little above 5.10%

Galeria Sloneczna



Source: CBRE

INDUSTRIAL & LOGISTICS

The industrial & logistics market in 2017 was dominated by one significant pan-European portfolio transaction, the acquisition of Logicor from Blackstone by CIC (944,141 sq m of warehouse space in Poland). The disposal of Logicor accounted for more than 81% of industrial investment volume which was recorded at EUR 0.94 bn. Although the industrial market is booming, with record-high volumes of supply and demand recorded at the end of 2017, rents remain stable and vary between EUR 2.40 – 3.90 sq m/month in the main hubs. Currently, yields for prime industrial assets amount to 6.00%, but occasionally single tenant BTS properties let by reliable tenants are traded with yields below 6.00%.

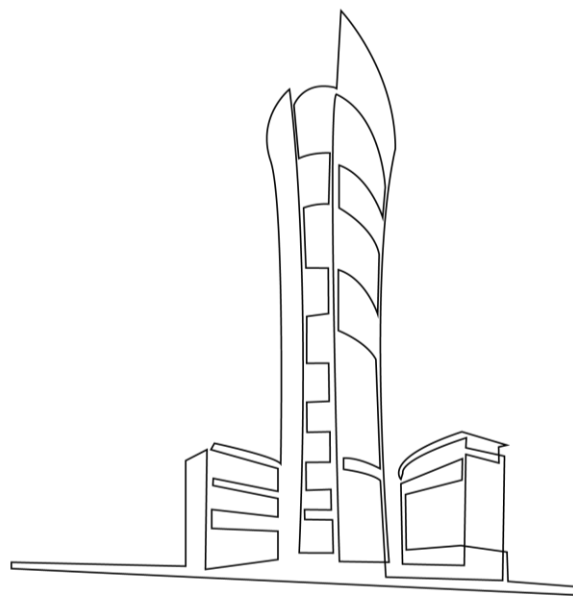
OFFICE MARKET

Demand for office buildings is supported by the inflow and expansion of global corporations in Poland. Nowadays, many worldwide companies have either opened or are planning to establish their offices in one of the main Polish cities. The best most recent examples are the arrival of J.P. Morgan in Warsaw and the expansions of Citi Service Center in Warsaw and of EY in Wroclaw. Currently, Polish cities are the most developing markets across Europe, with more than 1.8M sq m of office space under construction. Investment activity in the office sector has been somewhat limited due to restricted supply and the forecasted drop in the number of completions in years 2018-2019 could affect the investment market. Due to the estimated supply peak in 2020, investment activity in office sector will certainly increase in years 2020 – 2021.

Last year, two of the greatest transactions in Warsaw took place in City Centre West – the disposals of Proximo I and Warsaw Spire B. These deals and the achieved yields affirmed recognition for the CCW zone as the central and one of the most desirable office destinations. Other substantial transactions on the Warsaw office market were the sale of KroLEWska to Generalli and the opportunistic acquisitions of the SEB and BPH Portfolios.

As in previous years, for regional cities the real estate investor focus was mainly on Krakow, Wroclaw and Tri-City. Prime assets are traded at a yield slightly above 6.15% and the most significant transactions in regional cities included the acquisition of the EPP Portfolio (A4 Business Park, Tryton Business House, West Gate) by Griffin Premium RE, the sale of Maraton in Poznan to Union Investment, the disposal of Alchemia I in Tri-City to DAWM and the acquisition of Green Day by TRIUVA. In contrast to Warsaw, many investors accept a longer distance from the city centre for fully let buildings with reliable tenants. The best examples of the aforementioned trend are the acquisition of DOT in Krakow and Tensor Office Park in Gdynia.

Warsaw Spire (B)



Source: CBRE

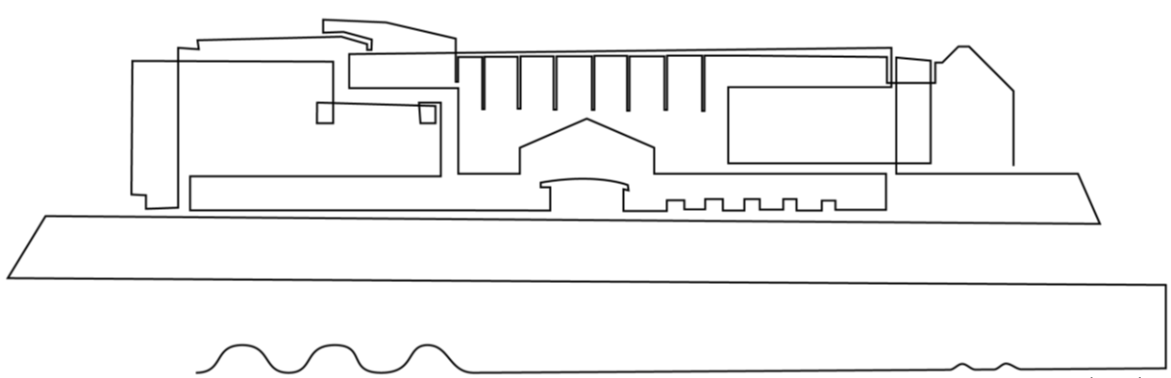
Source: CBRE

HOTELS & PRS

The new development path for the investment market in Poland could be the growth of alternative sectors like hotels and the PRS (Private Rented Sector). Investment activity in the hotel sector was the highest in its history and amounted to more than EUR 350 Million at the end of 2017. In comparison with the developed markets key performance indicators are very favourable for Poland and currently the hotel development market is booming. The hotel sector has been used to securing long-term lease agreements (minimum 20 years), therefore many office and retail projects have been converted into multi-use schemes with an accommodation part. This trend is remarkably noticeable in the newly emerging business hubs like City Centre West in Warsaw. All of the major hotels transactions took place in the first half of the year and included the acquisition of the Sheraton in Krakow, the disposal of the Westin and Radisson Blue in Warsaw and the pan-CEE Warimpex portfolio deal. Summing up, CBRE expects that investment activity within the hotel sector will increase in the coming years, with 4,500 new rooms planned in the Warsaw pipeline alone until 2022.

The Private Rented Sector has started slowly on the Polish market but the first transactions have been completed. PRS deals are very successful in the developed markets, with investment activity increasing every year, so investor interest in the Polish PRS market is enormous. Although demand from investors is high, currently the main drawback is lack of product from the developers' side. This is also entailed by the record-high consumer demand which exceeds the output, with developers preferring to dispose of flats to single customers and achieve higher margins. As long as the demand from consumers is high, this will become a significant obstacle for development of the PRS sector. On the other hand, several transactions have taken place or are at the final stage of confirmation. The major registered deal in 2017 was the acquisition of 72 apartments in Zlota 44 Tower by Catella Wohnen. In the first half of 2018, the Use Permit should be granted for Pereca Apartments (in close proximity to Warsaw CBD) which was acquired by Bouwfonds IM from Matexi.

Sheraton Hotel in Krakow



Source: CBRE

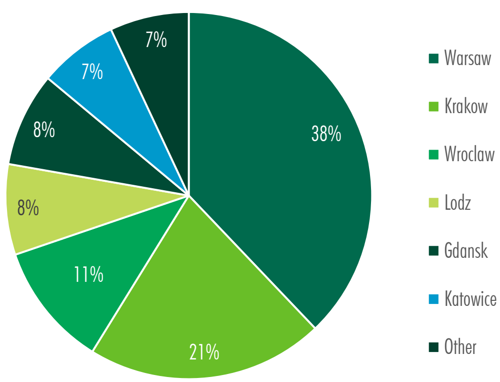
OUTLOOK

The European and Polish economies are in good shape and this is reflected in real estate investor sentiment. The Polish market looks set for another year of robust investment activity in 2018, supported by positive occupier demand, a growing economy and strong investment market fundamentals. Taking into consideration those transactions which are in the final closing stage, the upward trend will be sustained in 2018.

Further capital inflows and the low interest rate environment are putting yields under further downward pressure particularly in the retail and office sectors. It is worth noting, however that yields are on historical minima, but that pricing per sq m is still on market levels.

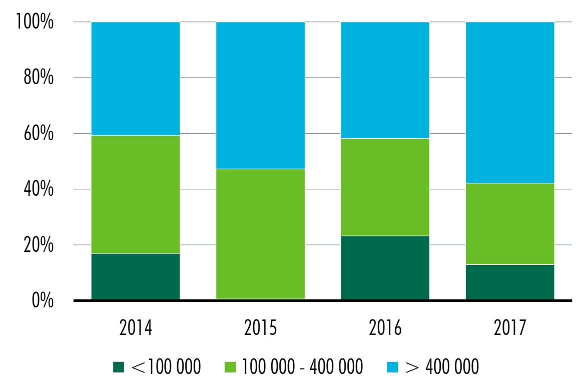
Moreover, the arrival of new investors from the Czech Republic and Israel are a positive signal for the market, reflecting an increase of demand for a differential class of assets and they could close the gap between core and opportunistic investors. Although the challenges, including an increase of construction costs or the Sunday trading ban are apparent, the investment market will adjust to new conditions and these obstacles will not slow the volume growth in 2018.

Figure 7: Office investment volume in Polish cities



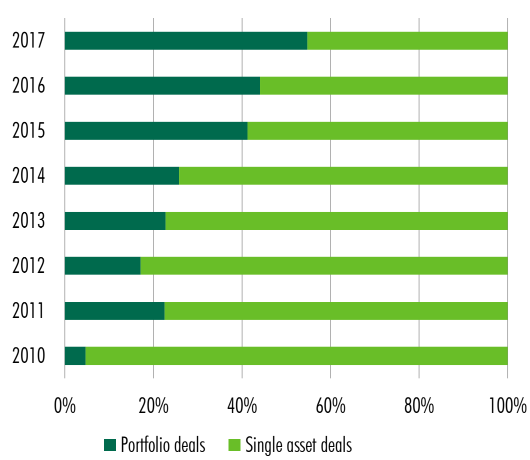
Source: CBRE Research, 2017

Figure 8: Retail investment by city size



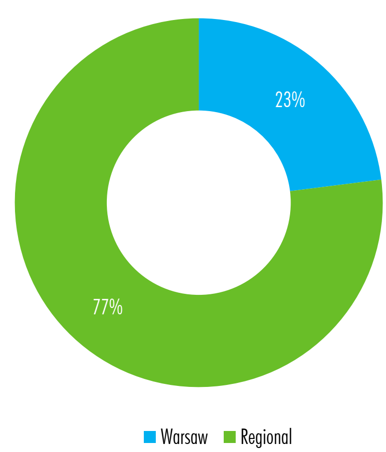
Source: CBRE Research, 2017

Figure 9: Share of portfolio deals



Source: CBRE Research, 2017

Figure 10: Investment market volume in Warsaw and regions



Source: CBRE Research, 2017

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