Commercial properties: revival is to come only in ...

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The half-yearly analysis of the real estate market development, conducted by Colliers, brings not just careful projections conditional upon GDP developments, but also a rather detailed description of the situation in the individual segments of commercial properties (logistics, offices, trade). In spite of some partial differences, all of these subsectors exhibit several universal characteristics: poor demand and corresponding rental activity (distorted by the included re-negotiations of existing contracts), but also idle construction activity.

Notoriety: poor demand

At the beginning of the year, the market in logistics areas showed some good results at least on the supply side, thanks to its previous momentum – there was a distinct year-on-year growth in the first quarter. The situation was much worse in sales – in the whole first half of this year, only 108,000 square metres of warehouse and industrial premises were leased, which marked a year-on-year decline of 72%. According to the same analysis, the new supply, i.e. finished construction, was about 185,000 square metres during that period (these figures are quite different from other estimates – according to Cushman & Wakefield, 231,822 square metres were built in the Czech Republic; DTZ even puts the figure at 263,100 square metres). In this light, the vacancy rate is continuously growing and currently stands at about 20%, but with relatively large regional differences – in Prague it is about 17%, in Plzeň 29% and in the north of Moravia 34%. And the analysis mentioned above does not expect any principal market revival before 2011.

The retail areas market is limping similarly. This is best described by the fact that in the first half no shopping centre was opened in the capital city, except for Galerie Harfa (42,000 square metres), and nothing is going to change about it by the end of the year. Unlike the rents in logistics parks, however, the rents for retail tenants are stable. Colliers expect a gradual revival of market activity in the second half of the following year.

Construction of administration buildings is not intensive, either. In the first half Prague, as the traditional centre of this type of construction – saw the completion of 85,000 square metres of new offices, which is 25% less than in the same period last year. The new areas for rent have an area of 97,000 square metres, which is 30% less year-on-year; a fifth of this area constitutes re-negotiated contracts. Supply exceeds demand even in this segment (the vacancy rate in Prague is only slightly over 10%), and the current market condition is perfectly illustrated by the level of rentals – although it remains the same this year at first sight, an increasing share in the declared rentals involves various incentives. “12-month rent-free periods are a standard today, which constitutes a 20% rent reduction in case of 5-year rentals,” says Karel Stránský, of Colliers. For the Prague office market, the analysis still predicts 6 to 18 months of poor activity and an ensuing slight decline in rents.

Careful (and non-transparent) investors

Demand intensity and the volume of executed investments correspond with the overall market condition. The fundamental parameters of the investment market in this year’s first half and the immediate outlooks are almost disastrous. According to the analysis by Colliers, we can expect purchases worth only EUR 200 to 250 million this year, which marks a decline of 80 to 90% compared to previous years. The statistics for the number of transactions look similarly bleak – from 40 to 60 in the past to 4 to 8 this year. Karel

Stránský, however, points at some uncertainty surrounding this data: “The investment market is not too transparent; all contractual arrangements involve confidentiality obligations.” The low interest in the publicity of investment operations can be explained by falling prices, while no owners or property developers want to be associated with underpricing. In addition, an increasing share of the investors are domestic entities, including private investors who are directly trying to avoid any publicity. The investment market is therefore rather non-transparent and may exhibit more activity than the available data shows, but the crisis is more than visible there as well.

According to the mentioned analysis, the current condition is characterized by a strong position on the demand side, which pushes on prices and requires better conditions for the whole operation, e.g. rent warranty. Therefore, real estate trades require more time, six to eight months instead of the former two to three months. In spite of all this, Colliers expects a certain revival of investment activity in the foreseeable future, especially under the pressure of financial trouble faced by owners and of the banks' interest in reducing their involvement in the real estate sector. That is why the prices should be rather lower and the yields should grow adequately. The caution of large institutional investors, however, results in a situation where the market continues to be dominated by smaller local investors, with a prevalent share of transactions at lower values (EUR 10 – 15 million). Big players should visibly return to the Czech real estate market next year, but a principal revival of the investment market cannot be expected before 2012.

Problematic projections

Not so long ago, (not only) consultancy firms were hurrying to make the most optimistic projections imaginable. These projections were mostly based on predictions of future growth based on past growth, without really taking into account macroeconomic, or fundamental, factors, developments in the financial sector etc. The crisis showed the short-sightedness or limited value of this type of predictions, which does not count on the development of the economy as a whole too much. The real estate market is not an isolated entity and its dependence on the external environment may be even larger than in other sectors or areas of the economy. The almost fatal actual problems and the criticism from outside forced real estate prognosticators to sober up – today they mostly concentrate on describing the actual market condition (usually in concert, yet with some slight differences), significantly less than on its future. And this is a general situation, with a single voice from the Capitol in Washington, D.C., to the Czech National Bank in Prague: in the economy, development trends and specific properties cannot be presently predicted reliably at all. That is why all real estate predictions are currently much more sober than in the past and are all based on the principle of “if … then …”, with a description of the development possibilities. The mentioned analysis, conducted by Colliers, counts on market revival in all of the monitored areas within two or three years. It sounds believable – more and more information hints at an end in the fall of key global economies, and the Czech economy could therefore experience a similar turn of events in the first half of next year. Along with the beginning of a gradual, but very slow recovery of the domestic real estate market.

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