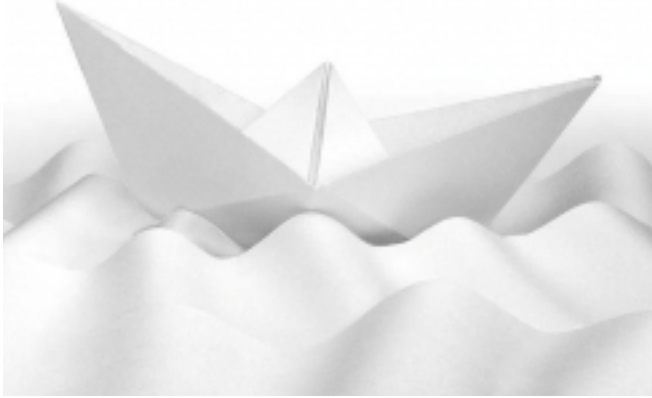


Real estate market: no reason to cry, no reason to rejoice



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“It is important to warn against overly optimistic expectations,” CNB Governor Miroslav Singer introduced cautiously the CNB Financial Stability Report. “The crisis is not coming to an end dramatically!” CNB and its Governor traditionally hold very modest and restrained position, which is now in place more than ever. The main problem of the Czech economic future lies not in the state of our economy, it rather depends on development abroad. “The key developments do not take place in our country,” M. Singer said. This is always the case, but in a situation where several EU countries are in catastrophic financial situation, their public debts are at least warning and world commodity markets are very volatile, the impact of external relations for the Czech economy could be doubly painful. However, if the CNB prediction proves to be right, we can expect stability on the market, and some optimists would perhaps add the sign „PLUS“.

Development: heavy legacy of the boom

The CNB analysis describes a significant deterioration in the financial health of developers in the years 2009-2010, mainly due to the significant decline in demand. The developers’ opportunity to respond to significantly lower sales has been, according to CNB, quite limited, and it included, besides a “relatively rigid” reduction in prices of finished projects, a significant reduction in new construction and a change the demand structure in favour of smaller flats.

An important indicator of the condition of a particular economic sector is the measure of credit risk, in other words, the number and overall level of overdue loans. It rises in the case of development - it rose to current 13% for some property developers (the selection is a reflection of the real possibility of credit monitoring in this sector of the economy) and to 9% for firms doing business in real estate. “In terms of stability of the financial sector and economy, this is not a cause for concern,” M. Singer says. The graph, presenting an upward curve of “bad” developer and real estate loans, shows that domestic development has already gone through worse times at the beginning of the last decade.

Selection property developers - roughly 1,000 firms and similar companies; NACE 68 - Active in real estate; NACE 411 - Property development; the selection doesn't include ownership unions and housing associations.

Residential: a smooth crossing

According to CNB, the expected one-time increase in VAT will help to sell the completed housing development projects (households will seek to accelerate their purchases of flats at a lower rate), after the introduction of higher VAT rate, however, there will be a decline in sales again. In the longer term, the level of sales will be determined by other factors rather than changes in VAT (macroeconomic developments, demographics, etc.).

Developers' interest in new projects stems from this prediction - the number of dwellings completed (in 2010 a decrease of 5%) and started (at the end of 2010 year on year reduction of 25%) clearly indicate downturn in construction, however, in comparison with the recent past, the market unquestionably revives. Further development will depend on market conditions, according to CNB. Despite this unoptimistic outlook, we can allegedly expect - after a slight decline in prices this year and the subsequent stability attainment - a slight increase in prices in 2012 and hence a greater interest in new projects by developers. As already noted, some risk can be represented by the expected "sales" of finished housing units (in Prague, they are estimated at around three thousand) and the impact of ending regulation. It is necessary to stress the word "mild". For example, the process of liberalization of rental housing in the past had more or less no impact on the market.

Regarding commercial properties, the Czech National Bank points out the well-known fact that this market goes through phases of moderate recovery in demand, which is most evident in the field of logistics (it reported sales increase by 45% last year due to the low comparison base).

The economy: fragile recovery

The CNB basic scenario for the immediate economic development of the Czech Republic (with many caveats) is in principle optimistic. CNB analysts foresee GDP growth in the interval 2.5 - 5% for the period 2011 - 2013, inflation rate oscillating slightly above 2%, rise in interest rates (from the current record low) somewhere to 3%, and further strengthening of the Czech currency, which should be between 23 to 24 crowns per euro.

The central bank has, however, more "scenarios" for the domestic economy, whose fulfillment is less likely, but it is not possible to eliminate them. The first, called Asymmetric development, counts on the restoration of recession due to recovery of economic growth abroad, which could lead to a drastic rise in commodity prices. The commodity prices are a hot topic today. Just in recent days French President Sarkozy called for greater regulation of speculative operations on the stock exchanges of raw materials and the President of the European Commission Barroso supported him. "To us it seems that the demand and the rise in commodity prices is driven by real developments in the world economy," says M. Singer with reference to very volatile, but parallel developments in commodity prices and GDP in the world.

The second scenario, called the Renewed recession, is even more pessimistic in its perspectives and mostly counts on negative impacts of development of Czech public finances, the overall decline in economic activity, a significant weakening of the Czech currency and re-fall in housing prices. Only banks would probably survive such crisis scenario in the Czech economy without harm. According to CNB calculations, banks could easily cope with even a double drop in GDP of 8% in 2012-2013. Their clients are in much worse situation, claims CNB. The moderate economic recovery of Czech economy, including the corporate sector, has not translated into economy of Czech households yet.

Illustrations: [Davide Guglielmo](#)

Graphs: CNB

