

Spain's fall from grace has been even more spectacular than Poland's rise. What does their future hold? **Martin Erbe** reports



Martin Erbe is managing director, Continental Europe, Westdeutsche Immobilienbank

It has not been this exciting and challenging for a long time in the European real estate markets. In some EU countries, market value corrections and weak economic data are causing property investors and bankers to break out in a cold sweat. However, other countries offer good opportunities for investment along with improved growth prospects.

Intensive use is already being made of these opportunities in countries such as the UK, France and Poland.

Investors in Spain need particularly strong nerves. The country is one of the so-called PIGS states (Portugal, Italy, Greece and Spain; some extend the term to Ireland as well (PIIGS)). The main reason is the high level of national debt in these states, coupled with a considerable downturn in the economy and negative growth prospects.

Greece has just avoided debt default with the help of the EU and the IMF. Meanwhile Spain, once the darling of investors, has become the problem child and is dragging Portugal down with it; the real estate market on the Iberian peninsula is suffering its worst crisis since World War II. This situation was triggered by the excessive construction boom, especially in the residential sector. As the property market in Greece is a semi-institutional one and the market in Italy is dominated by national investors, the following comments focus on Spain and Poland.

The two countries have a similar population size. They are also the two countries that demonstrate the most diametrically opposed development. In 2009, Poland was the only country in the EU to record positive economic growth, while unemployment in Spain reached its highest level for 30 years.

In Poland the real estate market still offers attractive commercial investment opportunities. It was no coincidence that the country was the guest of honour at MIPIM 2010; one of the biggest property transactions in Central and Eastern Europe in 2009 took place in Poland where MGPA Europe Fund III acquired two shopping centres (Karolinka in Opole and Pogoria in Dabrowa Górnicza) plus an option on a third property for €236m. Financing was provided by a consortium led by WestImmo.

What about the real estate markets in these two countries? In Spain, the situation remains difficult. The unemployment rate climbed to 18.8% at the end of 2009, its highest level for 30 years, and the budget deficit rose to 11.4%. Poland's budget deficit also rose last year, reaching 6.4%, while the unemployment rate was 11.9% at year end. One reason for this development is the strong domestic demand. In Spain, the onset of the housing crisis caused consumer demand, which had been supporting the sector, to slump dramatically, while in Poland, domestic demand kept the

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Warsaw is one of the most attractive cities in the CEE for investors

Role reversal

country on a stable course in 2009 as well.

In Spain, commercial property prices have plummeted by 30-50%. Office rents will not go up for a long time yet and vacancy rates are still high, particularly in secondary locations in Madrid, all of which continues to put prices under pressure. Nonetheless, individual core properties still offer attractive investment opportunities despite the poor key economic figures. Sound knowledge of the market is therefore essential for buyers and finance providers, and key real estate criteria must be fulfilled. During the boom, before Lehman's bankruptcy, these criteria had been forgotten in many other markets than just Spain.

The picture is very different in the Polish commercial property market, which stands out with its positive economic data. In March, the IMF raised its 2010 growth forecast for Poland from 2.2% to 2.75%; other sources are even talking about 3.4%. In contrast, the IMF is expecting a 0.6% decline in Spain with the economy here not expected to expand until 2011 with weak 0.9% growth.

Consumers are also expected to provide a positive impetus in the future – especially in light of rising wages. Just how robust the consumer climate is in Poland was demonstrated during the financial crisis. According to Eurostat figures, consumer spending there has risen continually over the past two years. Following the Lehman bankruptcy, consumer spending rose in the fourth quarter of 2008 by 1.2%. In contrast, it fell 1.2% in Spain in the same period.

And investors are rewarding Poland for the upturn in consumer spending over the past few years. The demand for property finance in this segment is high. Last year, WestImmo agreed loan commitments total-

ling around €250m for retail properties.

The high level of investor interest is hardly surprising. The conditions for shopping centres are good and domestic demand is stable. At 7-8%, initial yields are around 100-150bps above the average for Europe. Investors are concentrating on the major cities such as Warsaw, Krakow, Lodz, Wroclaw and Poznan. Nevertheless the smaller towns are worth looking at as well – as the saying goes: 'Better the best in the region than one of a million in the capital.'

The comparison shows that Spain and Poland are currently moving in opposing directions. There is no trend reversal currently in sight for the Iberian peninsula. Of course it should be noted that the Spanish property market has expanded very quickly over the past 10 years, and is still considerably ahead of the Polish market (for example, around 12m m² office space in Madrid, around 3.2m m² in Warsaw).

But Spain will recover. For many investors the mere fact that the Spanish market is in a downturn will be enough for them to look at new investment opportunities. From a banking perspective, Spain currently harbours many risks but also it offers many individual opportunities.

Poland is currently the most attractive of the Central & Eastern European (CEE) countries for investors. A further boost is expected when it joins the euro – originally slated for 2012 but expected to be delayed – which will eliminate the present currency risk on property investments.

A classic rotation has taken place. Property investors are turning their backs on (some of) the PIGS states and are focusing on the CEE. But if the PIGS states can get their budget deficits under control, this picture can always change.