INVESTMENT MARKET IN POLAND

H2 2018 MarketView

CBRE Research

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ECONOMIC BACKGROUND

In 2018 Poland witnessed one of the highest rates of economic growth for a significant period. Preliminary estimations of GDP are at the level of 5.3% reflecting one of the fastest growth rates in Europe. This is the result of very strong internal demand, largely resilient to external turbulence. Robust consumer consumption, a favourable labour market and continued record-high consumer confidence balance the weaker external demand impacting on Polish exports.

Current economic conditions, upward trends and cost advantages are attracting many investors to move their R&D Centres, Business Services or Risk Management Centres and other operations to Poland. The growing number of newcomers is boosting both the office and residential markets, which are developing in almost all cities in Poland. The hubs with a large numbers of students are strongly valued.

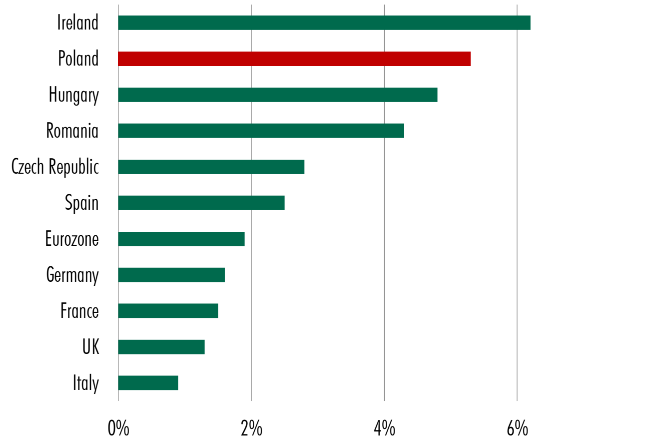
The record-low, but recently stabilising unemployment rate, has impacted on wage growth and the availability of labour. On the other hand, growing purchasing power and positive consumer confidence have translated into the rapid growth of e-commerce. Although traditional retail has suffered from the Sunday trading ban as well as structural changes within the hyper- and supermarkets' sector, total sales volumes and expenditure are rising. In addition, global trends relating to e-commerce are supporting the logistic market, which is flourishing in Poland.

All of the above trends and conditions are facilitating the inflow of capital to the commercial real estate market leading to successive records in terms of investment activity, turnover and capitalisation rates.

However, the forecasts for the next few years seem to be less positive, mostly due to the global uncertainty regarding international trade, oil prices, increasing interest rates in the US and weakening demand in Germany and other European countries. Additionally, Poland's conservative Law and Justice-led government has embarked on an interventionist policy agenda, which may undermine fiscal sustainability in the medium term. The new "exit tax" or return to VAT on property transactions is weighing heavily on private sector investor sentiment.

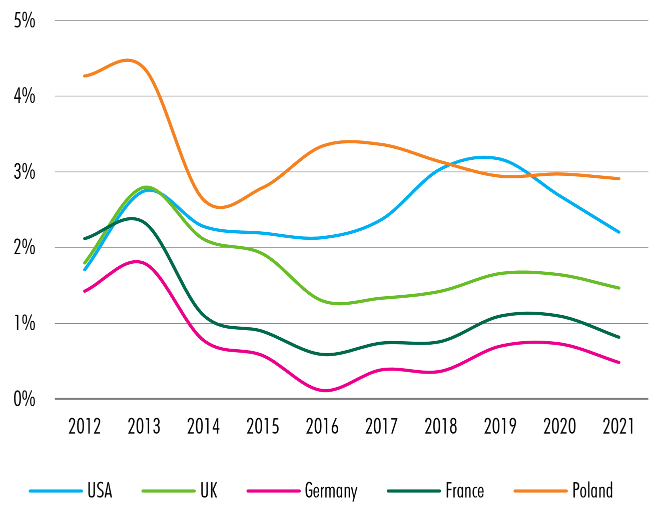
In general, the Polish economy is based on strong macroeconomic fundamentals, a sound banking situation and low imbalances; consequently, there are no reasonable prerequisites for a serious slowdown.

Figure 1. GDP growth 2018*



*Source: Oxford Economics, Q4 2018, *estimations*

Figure 2. Ten-year government bond yields (2012 – 2021)



Source: Oxford Economics, CBRE House View, 2018

Figure 3. Economic forecasts for Poland

Summary	2018	2019	2020
GDP Growth	5.3%	3.6%	2.7%
Unemployment	6.0%	5.5%	5.1%
CPI	1.8%	1.9%	2.2%
Short-term Interest Rates (%)	1.5%	1.5%	1.5%

Source: Oxford Economics, Q4 2018

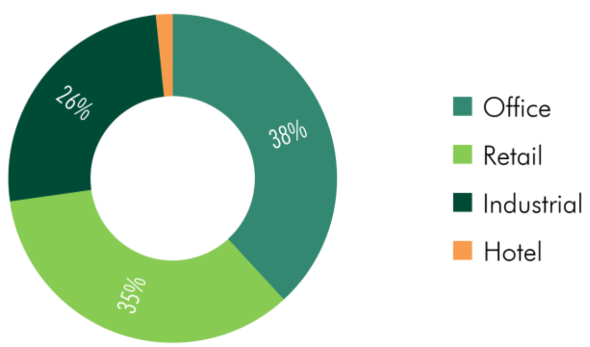
INVESTMENT MARKET SUMMARY

The Polish investment market is breaking new records annually. Whereas at the end of 2017 the total investment volume in Poland equaled to EUR 5.0 billion, the 2018 full-year result exceeded ***EUR 7.2 billion***. Taking into consideration the whole investment market in the CEE region, it constitutes almost the half of the total volume.

From the semi-annual perspective, the second half of 2018 had a EUR 750m higher volume representing a 19% increase in relation to the first six months.

Looking at the sectors, office investment volume in H2 2018 was EUR 1.8bn which was the best result among all sectors. Thanks to the significant increase in the second half of the year, offices finished the year as the sector with highest investment volume in Poland at EUR 2.75bn representing a 56% y-o-y increase. The second place was taken by retail with EUR 2.5bn. (29% y-o-y increase) at the end of 2018. H2 2018 was a very active period of time for industrial sector, at that time over 81% of the 2018 total volume for this sector was generated. Annually the industrial investment volume was twice as large as in the previous year with EUR 1.84bn. The investment volume in the hotel sector was 65% lower at the end of 2018 than in the previous year and amounted to
EUR 118.80m.

Figure 3. Sector breakdown of total investment activity in 2018 (%)



Source: CBRE, 2018

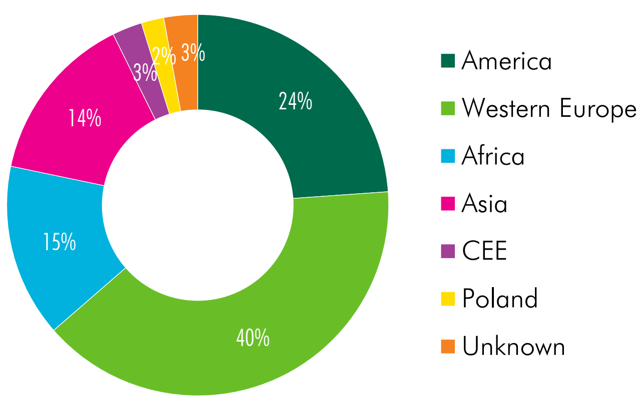
Similarly to H1 2018 in H2 2018 almost half of the investment volume was generated by portfolio deals. This time industrial portfolio deals dominated with 83% of the industrial investment volume in H2 2018 consisting of portfolio transactions.

Among biggest single transactions in H2 2018 there were the acquisition of Wars Sawa Junior for EUR 301.5m by Atrium Group, Savills IM's purchase of C and D buildings within Gdanski Business Center for more than EUR 200m and the Skylight and Lumen office buildings being purchased by Globalworth for EUR 190m.

The origin of investors

Capital from Western Europe remains the most active. In 2018 Western European investors placed 67% more money in commercial real estate assets in Poland than in the year before. Moreover, there was a 3 times y-o-y increase in the activity of American investor activity driven by the acquisition of the M1 retail portfolio and some industrial portfolios. It is noteworthy that investment funds from South Africa and Asia have become more and more active within the Polish market and for now jointly represent EUR 2 bn. Conversely, the commitment of domestic capital has remained low and has oscillated around 2% of total turnover.

Figure 4. The origin of capital within the Polish Investment market 2018



Source: CBRE, 2018

Record low prime yields

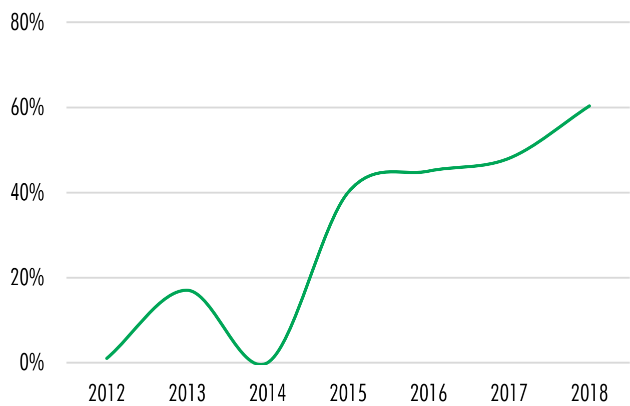
At the end of 2018 prime yields in almost all sectors reached record low levels. Prime office yields in Warsaw were compressed to and remain at ***4.75%***, whereas prime office yields in regional cities are estimated at 6.00%. Prime yields for shopping centres remain stable at ***5.00%*** and prime yields for industrial properties are at ***6.00%*** with the exception of e-commerce distribution centers let on a 10 year plus lease basis which fall below that level.

RETAIL MARKET

The total volume of retail investment deals amounted to ***EUR 2.50 billion*** representing the second largest investment sector in Poland (35% of the total investment volume in 2018).

At the beginning of the year, a huge transaction comprising of the acquisition of 28 retail properties by Griffin Real Estate was concluded. Three funds – Ares, AXA and Apollo-Rida – were the sellers. The total lease area amounted to approx. 700,000 sq m. Part of the portfolio (12 properties) will be ultimately taken over by Echo Polska Properties. The transaction was divided into three tranches. The first tranche was completed in January 2018 and covered four M1 shopping centres – in Czeladz, Krakow, Lodz and Zabrze. Among the major transactions of the last year, based on a single trade, the sale of Galeria Katowicka to the Malaysian EPF fund should be mentioned, as well as the purchase of King Cross Marcelin in Poznan by EPP.

Figure 5. Share of portfolio deals in the retail sector (%)



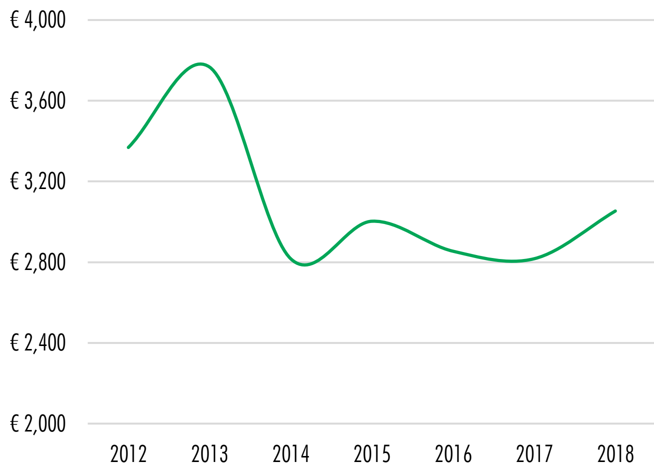
Source: CBRE, 2018

In addition to traditional shopping centres, recently two major transactions have been recorded involving Warsaw's high streets. The Wars Sawa Junior shopping complex, located in Warsaw downtown at Marszalkowska St., was sold by CBRE Global Investors; the Atrium Group was the buyer. The owner of Cedet has also changed - formerly the Central Department Store, originally commissioned in the 1950s, and then rebuilt by Immobel and reopened in May 2018, Cedet is a multi-functional building combining retail and service space with office space. The facility located in the centre of Warsaw, on the corner of Jerozolimskie Av. and Krucza St., was bought by GLL Real Estate Partners.

Pricing

The prime yields in retail should be evaluated at or even below 5.00%. Although there is as a negative sentiment towards retail across the whole of Europe there are some retail assets especially in Warsaw for which the yield would be below 5%.

Figure 6. CBRE Capital Value Index in the retail sector (EUR/sq m)



Source: CBRE, 2018

The CBRE Capital Value Index in the retail sector reached ***EUR 3,053 per sq m*** at the end of 2018. This represents a 23% increase in comparison to the end of 2017. The main reason for this increase was the influence of the acquisition of two high street projects. Nevertheless, this result was still 19% lower than the peak in 2013.

Outlook

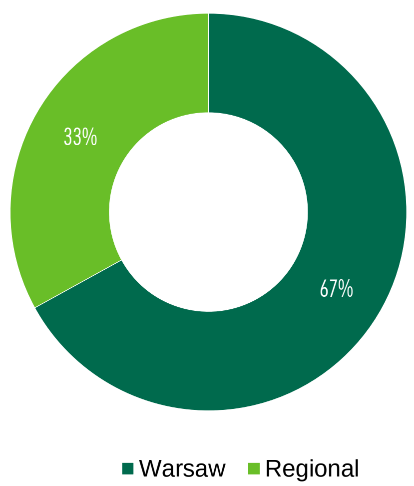
The favourable economic situation generates an increase in spending on consumption, which in turn largely determines the success of shopping centres and their growing turnover. Increasing consumer spending is boosted by high consumer confidence and a strong labour market. In response to the introduced Sunday trading ban asset managers are creating new spaces for meetings and leisure by implementing new social and entertainment services in order to attract customers. Shopping centres need strong and creative asset management to sustain the competition from e-commerce.

OFFICE MARKET

The investment volume for the office market reached *EUR 2.75 billion* and it was the best result in comparison to other sectors.

In H2 2018 there was increased investment activity in the office sector. In fact, all office transactions were responsible for 46% of total investment activity in this period. It is worth mentioning that the office investment volume in the third quarter alone was 13% higher than in the whole H1 2018 and amounted to nearly EUR 1.05bn. In Q4 2018 an additional EUR 768.9m was transacted. Moreover, 67% of the office investment volume in 2018 was concentrated in Warsaw.

Figure 7. Regional breakdown in office sector



Source: CBRE, 2018

One of the major transactions was the acquisition of the C and D buildings within Gdanski Business Center by Savills IM for more than EUR 200 m. Additionally, Globalworth took over the Spektrum Tower office building for EUR 101 m. as well as Skylight and Lumen office buildings for EUR 190m. Generation Park X was sold by Skanska to the Hansainvest Real Assets Fund for EUR 83m. The transactions identified accounted for 27% of the entire office investment volume in Warsaw in 2018.

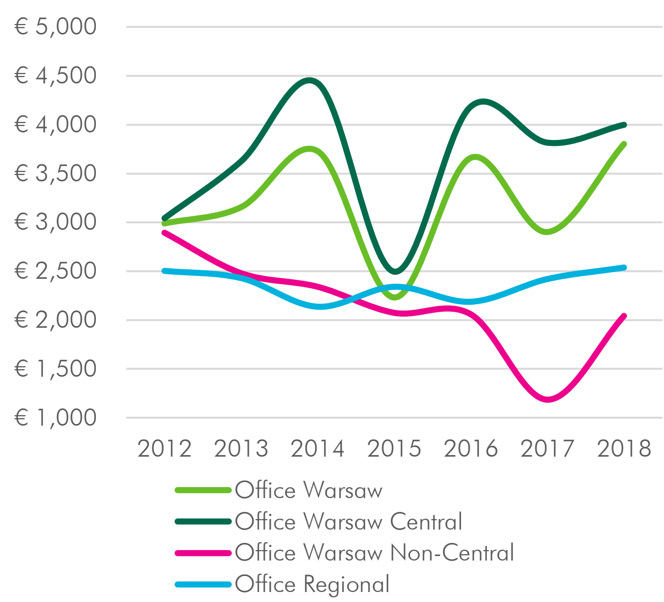
Investors mostly focus on Central Warsaw

Investor demand has been strictly concentrated on Warsaw City Centre. Only EUR 184m came from the acquisition of office buildings in Non-Central Warsaw. Looking at the regional market, the total volume in 2018 equated to EUR 907.50m. The major transactions were the acquisition of Quattro Business Park in Krakow for EUR 139m by Globalworth and Sagittarius in Wroclaw for almost EUR 69m by W-HIH Immo Invest.

Capital Value rising in Warsaw

A significant increase in Capital Value was noted in Non-Central Warsaw (72%) from EUR 1,185.60 per sq m to EUR 2,042.50 per sq m. In fact, the Index came back to its standard value after the fall in 2017 mainly caused by acquisitions of 16-20 years old buildings. Supported by the robust demand for office space, Capital Values are rising in central Warsaw. In the Central Warsaw area the change was quite minor, with only a 5% increase and amounted to EUR 4,000.20 per sq m.

Figure 8. CBRE Capital Value Index in the office sector (EUR/sq m)



Source: CBRE, 2018

Capital value for the Office Regional sector equates to EUR 2,537.70 per sq m which represents a 5% y-o-y increase.

INDUSTRIAL AND HOTEL MARKETS

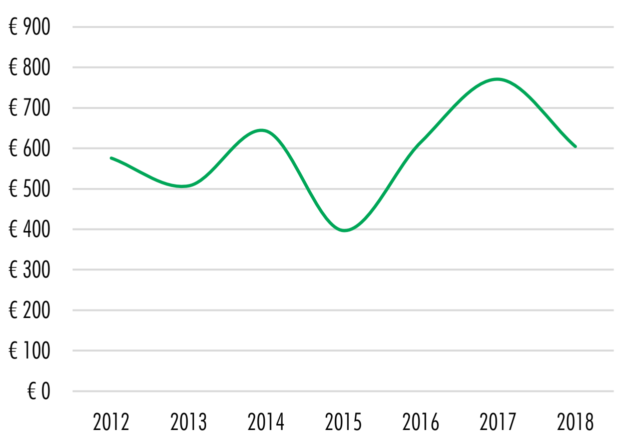
Industrial with twice the y-o-y volume

2018 turned out to be a record year on the industrial and warehouse investment market. The total volume in this sector last year amounted to ***EUR 1. 84bn***, which is more than twice as high as in 2017 and also as the 5-year-average.

In Q4 2018, the two largest transactions of the year were completed - the purchase of the Hillwood and Prologis portfolios by the Singaporean fund Mapletree, providing evidence of the growing popularity of Polish assets among Asian capital. The volumes of these transactions amounted to EUR 321m and EUR 260m, respectively, which represents almost one third of the total volume in 2018. Portfolio transactions prevailed significantly in the industrial and warehouse sector and accounted for 78% of the total volume of last year. The acquisition of 9 warehouses by Griffin (EUR 196m) and part of Goodman's portfolio by Blackstone (EUR 185m) were also significant transactions.

In 2018, the largest single transaction was the acquisition by Vestas Investment Management of Europe's second largest distribution centre in Szczecin for EUR 110m.

Figure 9. CBRE Capital Value Index in the industrial sector (EUR/sq m)



Source: CBRE, 2018

At the end of 2018, the CBRE Capital Value Index for the industrial sector went down from EUR 770 per sq m in 2017 to ***EUR 605 per sq m*** and reached a similar value as in 2016. Actually, the Capital Value rise in 2017 was strongly influenced by the acquisition of one big portfolio.

Growing hotel sector

At the end of 2018 the investment volume in the hotel sector was 65% lower than in the previous year and amounted to EUR 118.80m. In fact, in H2 2018 there was only one notable transaction. It was the acquisition of 30% of the shares of Puro Hotels (over 800 rooms in 5 hotels in Warsaw, Krakow, Poznan, Gdansk) by Family Investments 3, the entity owned by Marek Piechocki founder of LPP Group.
The y-o-y decrease of the investment volume doesn't mean that the hotel sector is in poor shape.
A significant increase of supply is expected in the coming years. For instance, the supply of hotel rooms in Warsaw should increase by ca. 35% in the next four years. Such development is remarkably visible in the most developed Warsaw's office zones such as the City Centre West or Sluzewiec. Moreover, a hotel function is added in many multi-use projects, located in Warsaw and regional cities. The creation of hotel portfolios worth over EUR 100m. should attract foreign investors which would not be willing to buy single hotel facilities.

Outlook

The booming economy and still attractive pricing in relation to other developed markets of Western Europe will certainly continue to support the domestic market in Poland. The synergy of investors' activity and a high supply of attractive projects mean that the Polish investment market has been constantly growing since 2009.
In the coming years, many projects especially offices in the Warsaw City Centre will be delivered, which could increase the share of market capital in total turnover. Furthermore, there is an increasing interest in alternative sectors such as residential, student or senior housing, which will become more prevalent in the next few years.

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