**Construction markets look broadly overheated across the CEE-6 countries presently**

**Warsaw, January 28, 2018** – Office development as a proportion of total stock is at cycle highs, in the 10%-21% range in the CEE-6 capital cities. It is 10%-28% in the Polish regional cities and at a peak in the industrial sector as well, reveals Colliers International, global industry-leading real estate services company, in its latest research report “[CEE construction markets: The Icarus effect](http://news.colliers.com/collect/click.aspx?u=/G1GTPto3VUlLccYk7E2sKUfM57pNy/osPFE4iN9n99RfiTw1UMcgWZfl5yaNHaLziiVpBEYxTtUjtVoVvASwUtL4vdbGKOPCqP1duAuxM8PU2JDTc0xaZ6y23/ZrR37L0Lb2BLdGBk=&rh=ff0045909e76588a253c93679d4a9183dba8fb9b)”.

**Mark Robinson**, CEE Research Specialist at Colliers International explains: “In Greek mythology, Icarus flew too near to sun, melting the wax on his wings and he plunged into the sea. We believe this is the correct analogy for construction markets in CEE, currently. Economic sentiment indicator appears to have passed its recent peak in most of the CEE countries. And examining the top of the last cycle in 2007-08, we found that it was spikes in construction costs and prices that helped define the turn at the peak even before the 2008-09 Global Financial Crisis struck”.

We found that it is labour shortages in particular that appears to be driving up construction costs and with minimum and average wages looking likely to rise at similar rates to last year in the CEE-6 in 2019, the heat is not abating. Romania and Hungary look to us to have the most profound labour supply and pricing issues, whilst demand growth momentum looks softer in Slovakia and might unfold in the Czech Republic. Bulgaria appears to have the least supply-side worries presently, whilst Poland’s larger and more liquid construction market may help it weather any incipient downturn.

*“*In contrast to 2008 (where despite a fall in commercial real estate investment levels the economy/employment statistics was buoyed up with EU infrastructure investment and  BPO/SSC investment), following Brexit and the EUs reduction and reallocation of structural funds, Poland may see reduced infrastructure spending, economic stagnation and a resulting overcapacity in the construction sector. This would be further compounded as Polish and Ukrainian workers return from Western European markets,” comments **Jonathan Cohen**, Senior Partner, Director of Building Consultancy Services in Poland.

**Demand to return to Earth**

We asked our CEE Valuations experts their opinion on what factors matter to commercial real estate developers right now. Demand from clients came out on top everywhere except in Poland. Why? One explanation may be the persistent and steady supply of new development build in the Polish cities we have already referred to. We perceive that developers, in the more liquid office marketplace, may be more confident of building “on spec”. Even in the industrial sector, the sqm under active construction as a proportion of industrial stock in Warsaw (6%) and across the 8 Polish regional cities (average of 13%) exceeds that of Prague and Budapest (both 5%) presently. Liquidity may be engendering confidence; or complacency if a downturn strikes. The most important factors for real estate developers in Poland are currently labour, materials and commodities costs.

**Low labour supply melts the wings**

The end 2018 wage growth and labour shortage situation dwarfs that of 2006-07, both in CEE and in the EU as a whole. When wages have risen by a quarter or by up to half in less than 3 years, profitability comes under pressure. Development costs for typical office projects in the capital city CBDs rose c. 5%-17% over the last 12 months. It looks like 2019 is another year of wage hikes in the CEE-6, with our estimates of national wage rises in the 5%-10% year-on-year, cross-sector minimum wages increasing 7%-10% and outliers like Romania’s just-announced stunning 58% year-on-year minimum wage hike for construction workers. So, development costs may well go higher, in the face of slowly melting demand.

**The Achilles Heel. Will the falls continue?**

Economic sentiment in the CEE-6, even with the fall since February, remains at historically elevated levels, so not predicting a recession as yet. The deteriorations in sentiment are mostly export-led and correlated to the economic/export slowdown in the Eurozone. Ahead for CEE-6 and Europe in 2019 are Brexit and potential trade issues with the US. Brexit itself may also lead to lower investment in the CEE-6 via the EU’s Structural Funds programme from 2020 onwards, affecting civil engineering construction.

**Soaring too high - construction prices have jumped**

Construction prices for commercial real estate in the CEE-6 have jumped. The change in GLA development costs for a typical 15,000 sqm office space located in the capital city’s CBD is,

according to our Valuations experts, ranged between c. 5% and c. 17% over the past year in the CEE-6 region. Locations in Budapest (10%-15% up) and Bucharest (11%-17% higher) have seen the more significant pricing pressures through 2018. In Poland, Colliers continued to observe double digit cost increases in commercial construction costs resulting from both labour and material shortages. Interestingly, official GUS statistics over the same period present lower cost escalation through the year, possibly correcting for earlier anomalies.

**Supply side factors defying gravity**

Labour shortage is now the most important single constraint across the region. Financial constraints, which encompasses project risk, currency risk, debt interest costs and wage/margin pressures remains the second-most important constraint but with only moderate cyclical variation in recent years.

**Labour force hubris - pay hikes sustaining into 2019**

Even given the economic slowdown unfolding across Europe and potentially in the CEE-6, wage pressures look likely to sustain into 2019 in the region. National minimum wage recommendations being enshrined into law now are for hikes of between 7%-10% this year. These levels are an anchor for the expectations of the most unskilled workers on a construction site. Wages in the construction sector across the region have leapt since 2015, according to Eurostat data. Excluding the tax code-influenced near-doubling of gross wages in Romania, it is Hungary (149 level versus 100 in 2015), Poland (129) and Slovakia (126) which have seen the big jumps.

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**About Colliers International Group**

[Colliers International](https://www2.colliers.com/) Group Inc. (NASDAQ: CIGI) (TSX: CIGI) is top tier global real estate services and investment management company operating in 69 countries with a workforce of more than 13,000 professionals. Colliers is the fastest-growing publicly listed global real estate services and investment management company, with 2017 corporate revenues of $2.3 billion ($2.7 billion including affiliates). With an enterprising culture and significant employee ownership and control, Colliers professionals provide a full range of services to real estate occupiers, owners and investors worldwide, and through its investment management services platform, has more than $25 billion of assets under management from the world’s most respected institutional real estate investors.

Colliers professionals think differently, share great ideas and offer thoughtful and innovative advice to accelerate the success of its clients. Colliers has been ranked among the top 100 global outsourcing firms by the International Association of Outsourcing Professionals for 13 consecutive years, more than any other real estate services firm. Colliers is ranked the number one property manager in the world by Commercial Property Executive for two years in a row.

Colliers is led by an experienced leadership team with significant equity ownership and a proven record of delivering more than 20% annualized returns for shareholders, over more than 20 years.

[Colliers International](http://www.colliers.com/en-pl/poland) has been active in the Polish market since 1997 and operates through offices in Warsaw, Kraków, Wrocław, Poznań, Gdańsk, Katowice and Łódź with over 250 employees in total. The company has been often honored for its achievements by industry organizations such as Eurobuild, CIJ Journal, CEE Quality Awards and the International Property Awards. Colliers’ distinctions include the “Outsourcing Star”, given in recognition of its status as one of the most active real estate advisors in the outsourcing sector; and the “Gazele Biznesu” for being one of the most dynamically developing companies in Poland. More about us on [www.colliers.pl](http://www.colliers.pl).

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