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The CEE Investment Scene

2021 / 2022

2021 / 2022 REVIEW & OUTLOOK

We bring you this edition of the CEE Investment Scene a little later than usual as we had originally planned to release it in early March. However, considering Russia's illegal invasion of Ukraine, which commenced at the end of February 2022, we felt that it would be prudent to speak with a broader base of clients at Mipim and to share some of the sentiment that we received.

The war was certainly a key topic at Mipim, especially for those active in, or with interests in the CEE region. There is of course growing concern for the people of Ukraine and the impact on the wider region, particularly from a humanitarian standpoint, with the sheer volume of refugees that have already been displaced. A great deal of respect has been shared for those countries, such as Poland, that have gone over and beyond to help during this horrific time, but it must also be recognised that more needs to be done to help these countries cope as this may last for some time. Along with the majority of the global population, we stand with Ukraine and hope for a rapid return to peace.

Outside of the atrocities being inflicted on the Ukrainian people, the war is having a massive impact far beyond the country's borders and far beyond those countries that border with it. Due to the largest number of sanctions ever placed on any country and specific people of influence, we can already see widespread impact and disruption on Global economics, which will in turn have both a direct and indirect impact for property markets.

In these relatively early but uncertain stages of this war, it is very difficult to arrive at any precise or meaningful predictions. And while it may seem insensitive for some to think about other impacts beyond the humanitarian ones, there are many related consequences which also need to be addressed in parallel.

The topics of fuels and energies, supply chain and near shoring, construction and production materials, rapidly rising inflation and interest rates were, and continue to be frequently debated in relation to building, occupying, operating and financing acquisitions and developments. In addition to these, the impact on rents and pricing, not forgetting of course all things ESG related, are also at the forefront of discussions, to name just a few.

Taking a step back for a moment, after two years of pandemic related disruption, the world was hoping to start the year with a more positive outlook, with Covid severity and cases slowly subsiding, and some level of normality returning. Although the year started out well, with renewed confidence and promising levels of transactional activity spilling over from 2021, fresh outbreaks have appeared around the globe, causing further health worries, disruptions to travel, businesses and economies.

Let's not forget that the pandemic has uncovered flaws and shaken up many industries and pushed forward change that was perhaps already on its way, or long overdue. Either way, change has been accelerated at a much faster pace than some might like, but even that change is constantly changing, and we all need to deal with it, whether we like it or not.

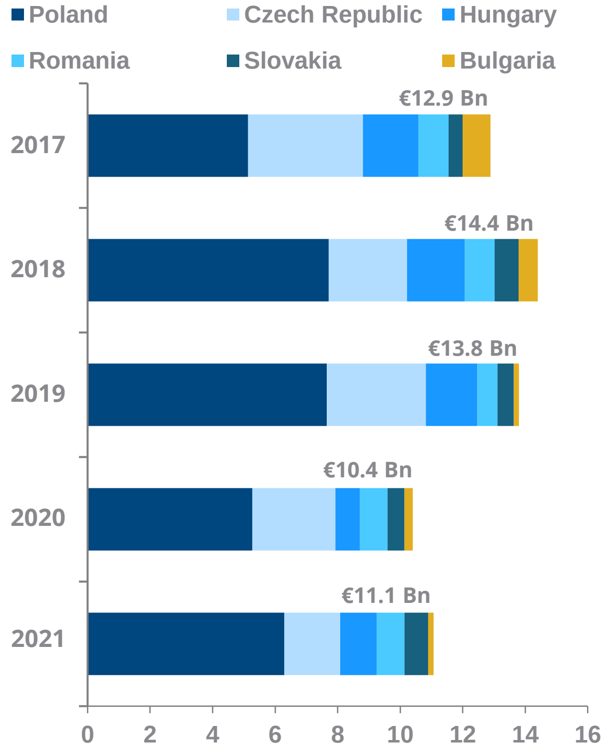
In the CEE region, we are currently registering some investors returning to a wait-and-see approach before making investment decisions. This was quite like the start of the pandemic, but for a very different set of reasons. Similarly, we have also seen some leasing deals put on hold or completely withdrawn. Some of these are claimed to have been related to Russian companies being involved and others due to the uncertainty of the war and its physical proximity.

These are not unreasonable reactions, but we must also remember that many of the challenges that confront our decision-making processes are not new and have again re-highlighted issues that need to be considered and resolved. Furthermore, there will always be those that continually look for and find opportunity even in the most challenging of times.

Throughout 2022, we will go into greater depth on these topics and how they drive or disrupt the various property sectors that they touch.

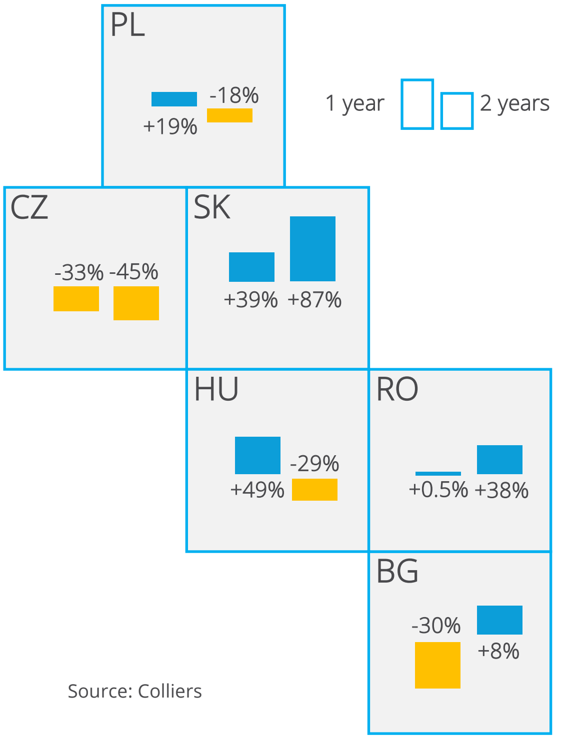
CEE INVESTMENT VOLUMES BY COUNTRY
2017 to 2021 (€ BILLION)

Despite the disruption of the pandemic, full year investment volumes for 2021, totalling €11.07 billion, were up by 6% YoY but ca. 20% lower than the same period of 2019. Colliers originally estimated that year-end volumes for 2022 could reach in excess of €12.0 billon, however, the war in Ukraine could impact this outlook.



CEE INVESTMENT VOLUME GROWTH RATES
(2021 vs. 2020 & 2019)

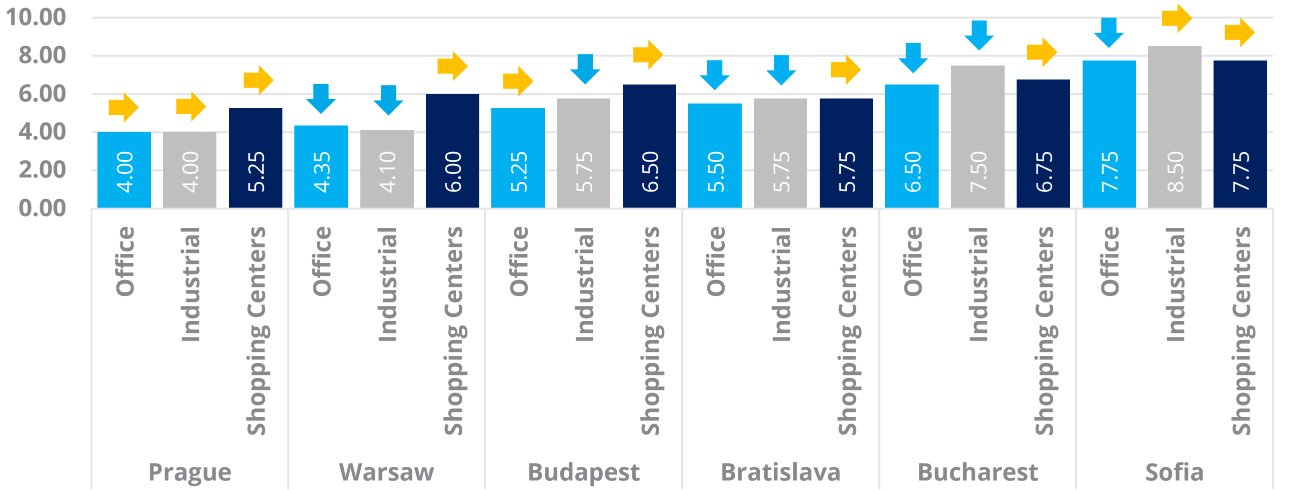
Individually, most countries are behind their pre-pandemic volumes, but Poland, with 57% of 2021 volumes, has reached its 5-year, pre-pandemic average. There was certainly a pick-up in activity in the final quarter of the year, but many markets were still held back by a lack of available product.



Source: Colliers

Q4 2021 PRIME YIELDS (%) & 12 MONTH FORECAST

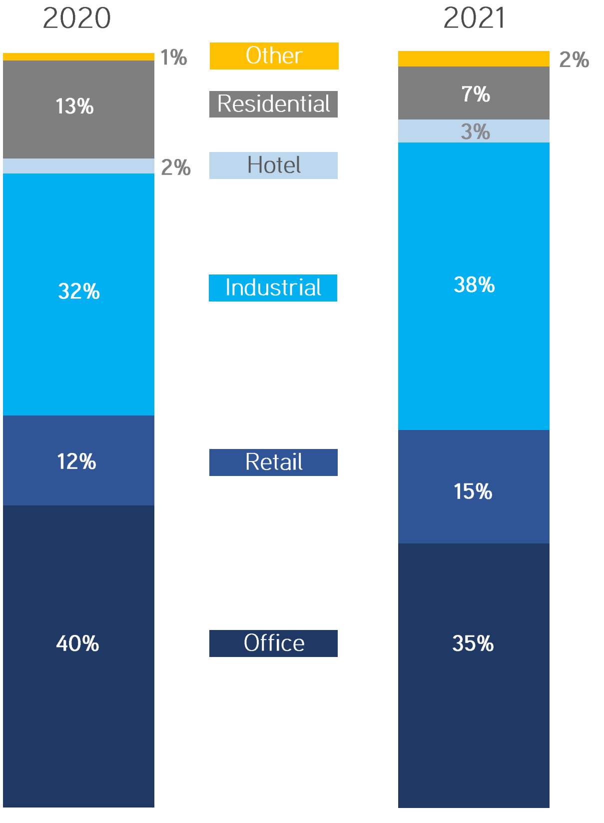
We have recorded limited movements in prime yields for many markets in the region, primarily due to the ongoing lack of transactional evidence to support further shifts. The exception, however, is prime logistics yields that have come in by almost 100 bps on average across CEE since Q1 2020, with Poland reaching over 180 bps. Our view remains that some markets will see further inward shifts although the pandemic and the impact of the war in Ukraine is driving inflationary pressures and negative economic sentiment. During 2022, we will therefore see how central banks will manage these pressures, which may be positive in terms of indexed rents but, will at some point eventually be reflected in the cost of debt.



Source: Colliers

CEE FLOWS BY SECTOR (%)

For the first time since 2008, the industrial sector secured the top spot with a 38% share of 2021 volumes. Offices and residential continue to record stable volumes, despite a relative shortage of available product for sale on the market. Retail volumes continue to be supported by retail park and supermarket assets, while hospitality volumes remain limited overall.

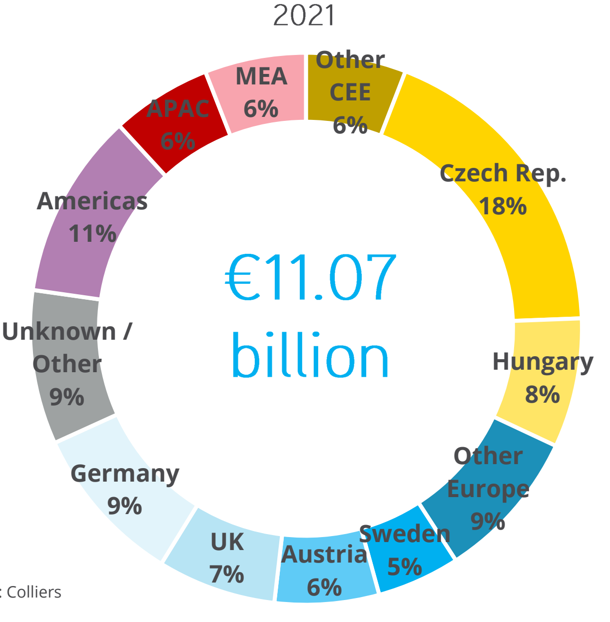


CEE FLOWS BY ORIGIN OF BUYER (%)

Western and Northern European funds were behind 36% of all transaction volumes in 2021, most notably capital from Germany, the UK, Austria and Sweden.

CEE capital was also very strong with a 32% share of total volumes. Czech domiciled capital was the most active overall with an 18% share overall and responsible for 52% of Czech Volumes, 68% of Slovak volumes and acquisitions also recorded in Poland, Romania, Hungary and Bulgaria.

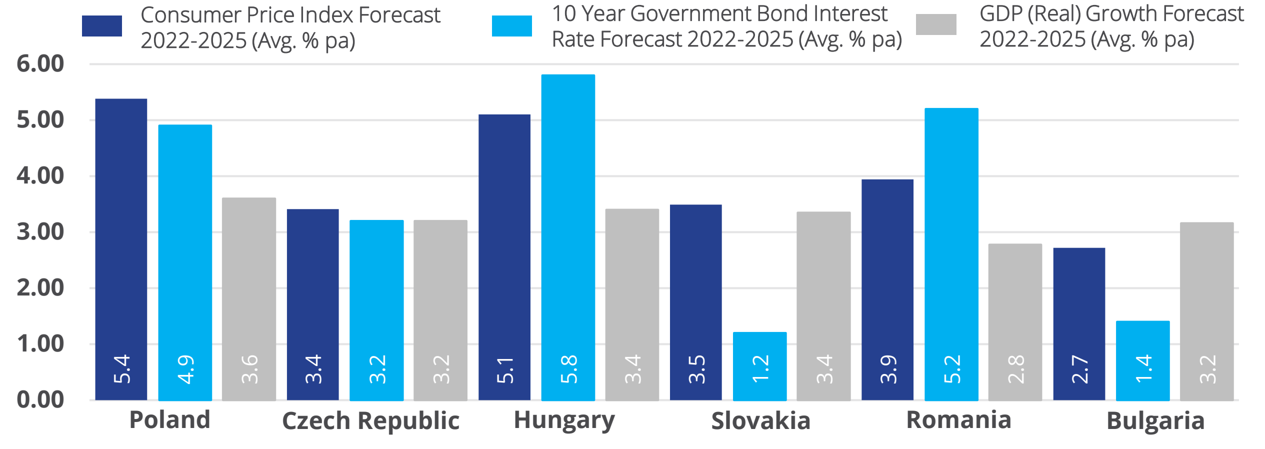
Hungarian capital also remained active, with a 42% share of its domestic market acquisitions in both Romania and Poland.



Source: Colliers

ECONOMIC INDICATORS & DRIVERS

With the geopolitical and health related crises, the global economic outlook continues to change frequently and is extremely difficult to predict. The current situation is highly complex, impacts on a broad spectrum of the economy and is most likely to worsen throughout 2022 before getting any better. The war and related sanctions, on top of pandemic and ESG drivers and disruptions, will impact property markets in terms of supply, demand and affordability. Not all these impacts are negative but, will differ between property sectors. However, it is both rising inflation and interest rates that are being very carefully monitored as they will bring an end to the long running 'low for longer' period which will not only impact the cost of debt and pricing, but also multiple other costs for real estate investors, developers, occupiers and consumers alike.



Source: Colliers, Oxford Economics

ESG: INTEGRATION INTO COMMERCIAL REAL ESTATE DUE DILIGENCE PROCESSES

Despite everything else that is going on the world, one of the most discussed and important topics in the real estate industry currently is that of ESG (Environment, Social and Governance) and its impact on the industry and related sectors.

There is an increasingly urgent need for the integration of ESG factors into real estate investors' decision-making, especially due to the variation in ESG benchmarking and implementation occurring across real estate players and sectors within the CEE region.

You have all heard the term 'stranded assets' and, depending on whether you are buying, holding, or selling, this term will make you perceive real estate or transactions in quite different ways. Going forward, the elements that make up ESG are already and will become increasingly more important to investment strategies.

Conducting an ESG review in the due diligence process can help investors eliminate deal issue threats and identify key ESG opportunities for improvement post-acquisition, while highlighting deficient standards and identifying regulatory liability.

As part of the ESG due diligence, a company's policies, procedures and management systems are also reviewed to identify the possible risks that might not only be financial, but also reputational.

As part of our own commitment as Colliers, we have recently appointed an ESG Chief Officer to help provide ourselves with expert guidance in this field, but also for our clients that we provide services to.

The following table highlights the key factors that we believe investors need to integrate into their commercial due diligence processes, to help identify major sustainability risks and opportunities and to manage it properly after acquisition:

ESG aspects reviewed during a Due Diligence process

Environmental	Social
• Monitoring, tracking and using Environmental KPIs • Environmental policy and the existence of a responsible team for implementation and review • Compliance with national and international regulations (e.g.: EU Taxonomy, CSRD) • Climate Change transition plan: - Measuring and reporting GHG emissions - Offsetting GHG emissions strategy - Verification of a Net Zero Target, SBT target or Carbon Budget • Energy Performance: - Energy efficiency strategies - Energy Audits • Monitoring systems for the management of ESG systems • Sustainability Reports	Policies: • Health & Safety • Human rights • Labour standards • Diversity, equality and inclusion • Privacy and data security
	Governance
	• **Risk management systems** • **Corporate codes of conduct** • **Corporate code of ethics** • **ESG budget and ESG training programs**

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