Budapest and Bucharest back on investors' radar

Off-limits in recent times to all but the most risk averse investors, Hungary and Romania are now seen as offering value outside the fiercely competitive prime areas of Europe, particularly in the office sector.

There are distinct signs that Hungary is on the up after several years of political instability and risk, coupled with an unpredictable taxation regime.

Meanwhile, overseas investor interest in the Romanian capital of Bucharest is increasing.

Morgan Stanley's €180m acquisition of a Budapest portfolio from an AEW-managed fund in July is widely seen as marking a turning point in Hungary's property sector. The assets consisted of MOM Park, a 31,500 sq m prime shopping mall with an adjacent 19,300 sq m office on the Buda side of Budapest; the West End Business Centre, a 28,800 sq m office building; and EMKE, a 13,700 sq m office building on the Pest side of the city.

The group of investors also includes Hungarian developer and investor WING and the Austrian shopping centre manager and investor CC Real. Richard Wilkinson, head of commercial real estate at Erste Group Bank, which provided a €126m loan, hails the transaction as "a strong sign of the overall recovery of the Hungarian real estate market".

Budapest review

Troy Javaher, JLL's head of CEE capital markets, says: "The deal has kick-started a full review of Budapest by a number of funds – less so the German ones, which remain a little more caught up in the political situation, but more among the US and other foreign players who are looking at the favourable fundamentals."

Javaher estimates prime Budapest office yields to be around 7.25-7.5%.

"Budapest and Bucharest are buying opportunities right now and for the next few years. Bucharest has had growing pains but the standard of construction is comparable to the rest of central Europe," he adds.

Matthias Naumann, vice president research and strategy at Deutsche Asset & Wealth Management, says: "The Morgan Stanley deal represents the first institutional money that has gone back into Budapest after donkey's years of Hungary being in the doldrums. The office vacancy rate in the capital could fall to quite low levels after being quite high, as there has been so little development recently. It is an interesting rebound and there are future rental growth prospects."

Cushman & Wakefield highlights a rally for the Hungarian office market during the second quarter, supported by strong economic growth. While the investment market was reasonably active, the occupational sector was record-breaking.

As demand continues to outstrip supply, the vacancy rate in Budapest continues to fall and as the market begins to swing in favour of landlords and tenant incentives are being whittled away for the best space, hopes of rental growth are high. Take-up over the first half of 2015 was 280,000 sq m – marginally ahead of the same period in 2014, itself a record year.

CEE developer HB Reavis has noticed this and is pressing ahead with Budapest Central Towers, a 120,000 sq m office and retail project. Acquired from multiple owners in June, the sites are located in the 13th district of Budapest.

Radim Rimanek, director of Czech Republic, Hungary and London, says: "It's our plan to start the first phase of the project in the first half of 2016. Hungary has been out of favour with developers and activity has lessened so we decided to invest. Last year we completed Váci Corner Offices, a 21,600 sq m scheme which is fully let. We see a lot of demand for an undersupplied market where rents are firming."

Meanwhile, Friedrich Wachernig, board member with responsibility for project development and asset management of Vienna-listed S Immo, is upbeat about Romania. "The best city for us is Bucharest. It is the sixth largest agglomeration in CEE and it is coming up again on the back of growing demand for shared service centres," he says.

At the turn of the year the developer and manager will press the start button on a speculative office project called The Mark, a 15-storey, 28,000 sq m scheme bordering the Romanian capital's CBD.

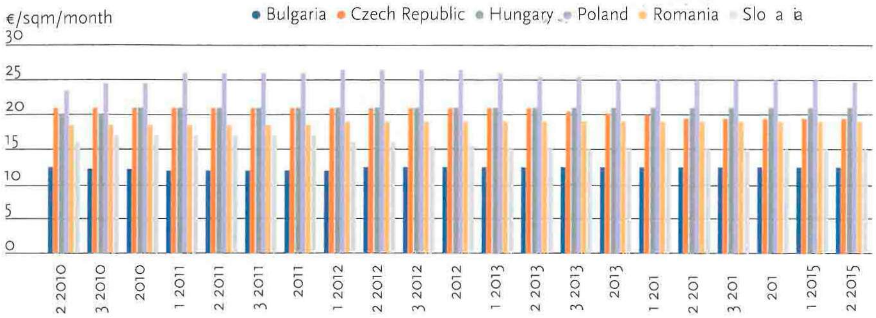
German investors return

It is also enlarging its 80,000 sq m Sun City shopping centre in Bucharest by another 10,000 sq m. "German investors are coming to look at the city again. We also believe in Budapest, where prices and still low but starting to rise as investors get used to the political situation; it will come back as a western-style city in the CE region."

Another company building speculatively in Romania is P3, the pan-European logistics property owner, developer and asset manager. It has started work on a new 28,000 sq m unit at its P3 Bucharest park, the first one to be developed by the company in Romania following its purchase of the 215,000 sq m park earlier this year.

CEE office rents 2010-2015

Hopes for rental growth are high as demand continues to outstrip supply



Source: Cushman & Wakefield

"Romania is one of the few countries where there is a fundamental need for office due to the rise in office employee numbers. We see a lot of international companies, such as IT providers, trying to concentrate their activities in Romania and I see rental growth here."
Bruno Ettenauer, CA Immo

Managing director Peter Bekar says: "Over the past 18 months our team in Romania has grown from three to eight. The rapid growth of the Romanian logistics market has resulted in extraordinary take-up of warehousing space, so much so that the vacancy rate has dropped to just 5% in the greater Bucharest area."

Vienna-quoted CA Immo, which already owns offices totalling 106,000 sq m in Bucharest, has renewed its interest in the country too. "We are really in favour of Romania," says chief executive Bruno Ettenauer. "The country is one of the few where there is a fundamental need for offices due to the rise in office employee numbers. We see a lot of international companies, such as IT providers, trying to concentrate their activities in Romania and I see rental growth here.

"Our occupancy rate in the country has been 95-98% so we haven't been able to meet the expansion plans of our tenants. Therefore, last month we decided to develop there and started building Orhideea Towers in the centre-west of the capital."

The €75m scheme will comprise 37,000 sq m and be delivered in 2017. Ettenauer has decided to keep it in CA Immo's €400m Romanian investment portfolio.

Fellow Vienna stock exchange-listed firm Immofinanz has also seized on Bucharest office development. Bettina Schragle, investor relations and corporate communications head, says: "Romania has a stable recovery and office demand is increasing."

The company's biggest project is the 40,000 sq m Metroffice, which is the first part of a long-term masterplan. This involves the redesign of the entire area within Immofinanz's 92,855 sq m Iride Business Park, northern Bucharest, into what will become Iride City, and incorporate hotel and conference facilities. Completion of the €34m three-building Metroffice first phase is set for the first quarter of next year and will offer 20,000 sq m of space.

Immofinanz is also rolling out logistics space in the city. An initial 40,000 sq m first phase of LOG.IQ Bucharest will be delivered by the first quarter of 2016. The company is also building LOG.IQ Ploiesti, a large-scale industrial development, where a first phase of 15,000 sq m is complete; a second 15,000 sq m phase will be delivered next year.

The investment market in Romania is lively, with some 15 deals already having taken place this year, featuring some newcomers to the country including P3, Lone Star, and CTP. Prime yields have decreased for all sectors: office from 7.75% to 7.5%, shopping centres from 8% to 7.75% and industrial from 9.25% to 8.75%.

Improving yields

Prime yield compression is continuing, based partially on improved general sentiment towards the economic environment in Romania, but also because of yield compression in other CEE markets and the reduced cost of debt financing in Romania. Still, the yield spread between Romania and other more mature CEE markets, notably Poland and the Czech Republic, remains significant, says CBRE.

This summer German investment fund GLL Real Estate Partners bid to acquire the 38,000 sq m Floreasca Park office project in northern Bucharest from its developer Portland Trust for more than €70m in a deal reflecting a yield of around 8%. GLL already owns the Charles de Gaulle Plaza office building close to the Aviatorilor subway station in the capital.

Meanwhile, the South African investment fund New Europe Property Investments (NEPI) purchased the 74,730 sq m Auchan Titan Shopping Centre in a €86m deal. NEPI and its partner Real4You this year opened the new €165m Mega Mall shopping centre in Bucharest. The 72,000 sq m mall has 200 shops including international tenants Marks & Spencer, H&M, Zara, Mango, and Tommy Hilfiger.

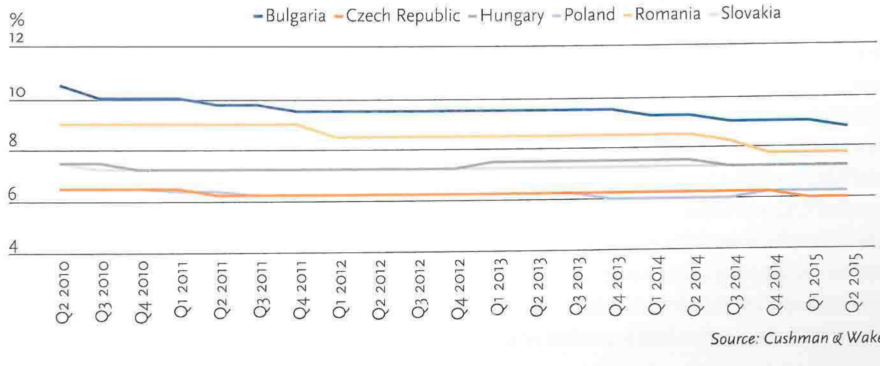
Total office take-up in Q2 in Bucharest was 42% higher than in Q1, reaching 82,000 sq m, says Cushman & Wakefield. This was largely supported by two key deals, both of which were more than 20,000 sq m: Genpact signed on 22,000 sq m, and Oracle took 20,000 sq m. Both deals were prelets and contributed to the highest quarterly prelease activity since 2008. The IT sector continues to evolve, representing 40% of the quarterly total in Bucharest.

While investors are optimistic about economic growth in Romania they will carry on buying into it. During the first quarter of the year the economy expanded by 4.2% year-on-year, marking the best performance in the EU.

Growth has been broad-based, led by robust consumer spending and a surge in investment. However, it remains territory for the more adventurous investor and more conservative companies, such as Invesco Real Estate, are still not ready to step in.

CEE office yields 2010-2015

Hardening yields reflect Romania and Hungary's increasing attraction for investors



Source: Cushman & Wakefield