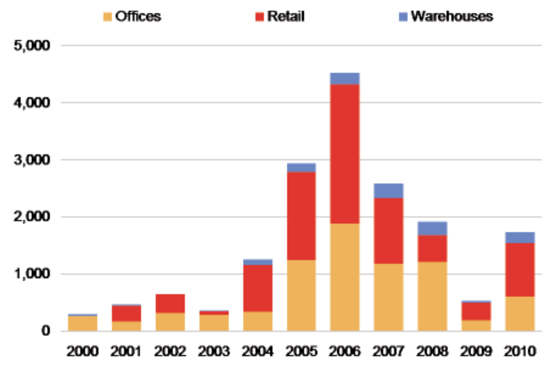
Poland Investment Bulletin

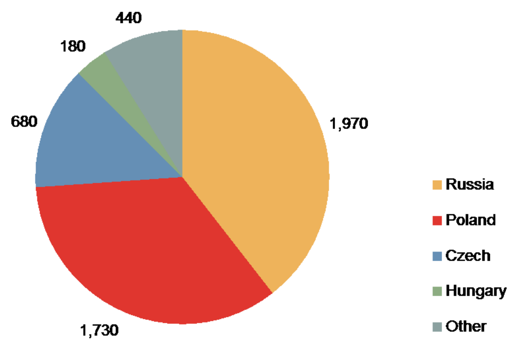
Winter 2010 / 2011

Investment volumes in Poland 2000 - 2010



Source: Savills Research

Investment volume in CEE region in 2010



Source: Savills Research

"In 2010 we witnessed an evolving investment market in Poland, starting with relatively small investment volume and few transactions, many actually overlapping from 2009, reflecting the weak market conditions at the start of Q1, through the more active market in Q3 into a very strong finish in Q4."

Michał Ćwikliński - Director, Head of Investment Department

- 2010 investment volume was at EUR 1,729 million, just 6% below the volume of 2008, up 185% on 2009.
- Poland accounts for over one-third volume (ca 35%) of the entire volume in Central-Eastern Europe.
- Q4 2010 net volume was about EUR 577 million, one-third of the total annual volume for the year.
- Cumulative 2010 volume almost tripled the total 2009 volume of EUR 608 million.
- In terms of the number of transactions, the retail sector overtook offices in Q4 and leads (53%) with the office sector taking second place at 33%.
- Savills had anticipated that the retail sector would increase it's domination of investment activity in 2010 and this has become fact and will be further supported with several more transactions coming through most likely already in Q1 2011.
- The most active investors in Q4 were UK, German, Polish, Spanish, American and Dutch.
- Based on the limited deal evidence, prime yields for Warsaw offices and shopping centres have stabilized with CBD offices around 6.50% and below 7% in non-central Warsaw locations; prime yield for modern shopping centres is at or below 6.25% in Warsaw and the best regional shopping centres.
- Volume in 2011 is projected to be more than EUR 2 billion, depending on the availability of the institutional grade property investment opportunities.
- Pre-purchase and forward financing transactions should be more popular, together with the acquisition of retail centres in the smaller towns and office properties in the Polish regional cities.

Economy and overview of 2010

Economy

In 2010 the Polish economy sustained its positive outlook with economic data indicating improvement in small and medium size companies as well as household budgets. As a result analysts expect Poland to emerge from the crisis in better condition than many other European countries.

In accordance with the initial estimations the GDP grew in 2010 by 3.8% and is forecasted by the National Bank of Poland to exceed 4.0% in 2011 which is significantly faster than the projected average growth in Eurozone (ECB forecast is between 0.7 - 2.1%). The GDP growth is driven mainly by stronger domestic demand, which makes Poland less dependant on trade balance than other CEE countries. Inflation in 2010 has been initially estimated at 2.5% just slightly ahead the EU average.

Employment in enterprise sector amounted in January 2011 to over 5.5 mln, has grown over 2010 by 3.8% and is close to reach the pre-crisis level from 2008. Average gross wage in January 2011 was PLN 3,392, around 5.0% higher than the year before.

The most important challenge for Poland is now the fiscal consolidation preventing the rise in public debt and budget deficit.

2010 activity

By the end of 2010 the total investment volume significantly exceeded the total annual volume for 2009 by 185%. The trend of increased activity of investors in the property investment market has become even more evident in Q4 2010 when the total turnover for the quarter was almost at the same level as the whole 2009.

Investors continued to seek office investments in 2010 as a priority, especially in Warsaw; originally this was limited to CBD but has extended to non-central locations. There have also been a few office investment transactions outside Warsaw, showing the ability of investors to seek opportunities in other large cities in Poland, providing that the investment product is meeting their criteria – long leases to prime covenant tenants. The examples of such transactions could be the acquisition of Avatar office building in Kraków by Azora International for EUR 30 million and as the purchase of Onyx office building also in Krakow by BPH Rynku Nieruchomości FIZ for EUR 12.6 million. Another example is the disposal of Dmowskiego Center in Gdańsk by BPT Optima fund to Key Financials for ca EUR 5 million.

More investors have been actively seeking shopping centre investments in the regional cities, both large and smaller agglomerations, and there were a few transactions that closed before the end of 2010, besides there are transactions in progress on a few modern centres. This has set a new trend with the significantly increasing retail property investment volumes. Due to a notable discount between the office and retail sectors, as well as the good prospects for retail sales growth in Poland in the next decade, investors have spotted an opportunity to secure good investments showing relatively high and stable returns.

Q4 2010 was marked by a number of such transactions. An American fund manager has purchased 75% of Malta Shopping Centre from Neinver for ca EUR 140 million, Rockspring Property Investment Managers have acquired Ferio Shopping Centre in Konin from RE Project Management for over EUR 47 million and AEW Europe / Tristan Capital have bought Jantar Shopping Centre in Słupsk for EUR 92 million. There are also a few transactions that are about to close in the near future as the completions of the negotiations were disturbed by the quieter Christmas time.

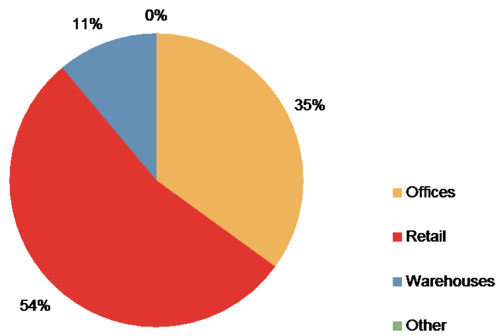
The retail share of the 2010 investment volume was 54%, higher than the 35% share of the office sector. The share of the office investments has decreased in comparison with the retail sector and this should be perceived as a sign of stabilization of the property investment market. Such trend shows more optimism among investors, who are more likely to seek opportunities in other segments of the market than prime offices in capital cities, which has been perceived as the most secure property investment product, especially throughout 2009 and in the begining of 2010. The amount and the scale of the retail transactions, such as the large Simon Ivanhoe transaction, have resulted in a return of the volume shares to the 12 year average.

It is possible that the more stable occupier conditions in the retail sector starting from early 2009, are now accepted by investors as more than a short-term factor. More recently there has been a significant rise in expansion activity by leading tenants, many are aware that there are fewer new centres currently being built that will lead to a significant slowdown in the growth of retail floorspace.

Buying activity by German funds was significantly lower in the last quarters, but this is a temporary lull as the funds reviewed the existing investment opportunities and are waiting for the prime investment product to be offered in the market, after the significant slowdown of the development pipeline in the last years. Savills expects many of these funds to return strongly to the market and become dominant buyers within the next months, as the new investment opportunities meeting their criteria start to arise.

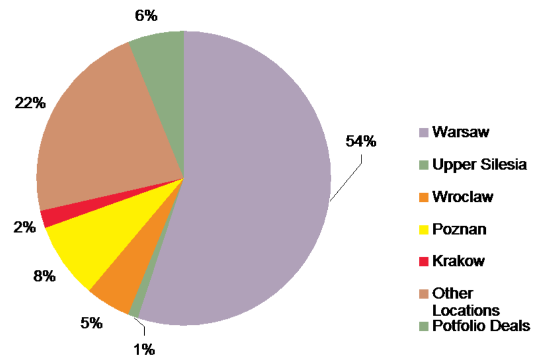
Prime yields

2010 investment activity by sector



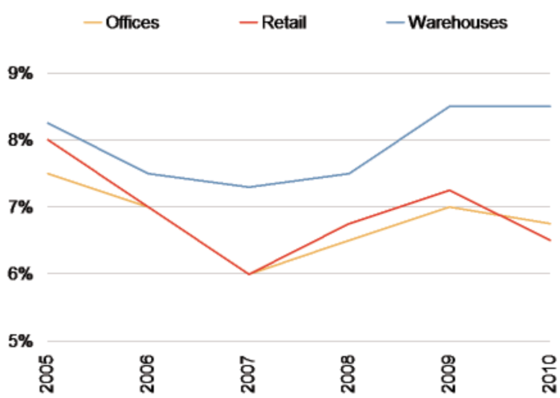
Source: Savills Research

2010 investment activity by location



Source: Savills Research

Average prime yields per sector



Source: Savills Research

Prime yields

The latest set of transactions in the Warsaw office market has signified a return to yield compression. This trend has been firmly established throughout last nine months of 2010 and may have more to do with the lack of good investment product to buy, as well as higher returns that the market here offers in comparison to the more established markets of Western Europe. Nevertheless the deals indicate investor competitiveness to secure transactions.

Those deals now under way in the market, especially in non-central locations are now reflecting initial yields of significantly less than 7.00%, possibly as low as 6.75% (a level at which Crown Square is rumoured to have been sold) . There are also advanced deals in the CBD with the initial yields expected to be significantly lower than for Mokotów at 6.50% or below.

Prime shopping centres in Warsaw as well as in the regional cities are in demand from investors and analysing as far as we can the current deals completed or in process, we conclude that the prime retail yield could be at or below 6.25% for the best performing centers. For shopping centres in major cities the initial yield is around 7.00% (this has been confirmed with Malta Shopping Centre disposal) and for shopping centres in cities with 100,000 – 250,000 population the initial yield is considered to fall to a range of 7.50%-8.00% for the best properties, depending on the size of the city and the track record of the centre. There is the expectation that with increased activity, these yields will compress.

Retail parks in the larger cities with long leases should achieve ca. 7.50% assuming favourable transaction volume and relatively long lease lengths. For smaller centres in small towns the cap rate rises to ca 8.75% - 9.00% depending on the rent level and the availability of high debt levels. Several ongoing transactions will shortly confirm these yields.

There is ongoing demand for sale & leaseback opportunities, especially in the retail and industrial sectors. This type of transaction has a security element attached to it, mainly due to the relatively long lease lengths and continue to attract those investors that specialize in sale & leaseback transactions. Whilst the volume of such transactions is not significant, due to limited availability of such transactions, they will further benefit from the interest of investors.

Prime yields and outlook

Outlook

From our observations, there is a greater number of investors actively looking for good investment opportunities in Poland in all property sectors. These investors are seeking to take advantage of the changing, more competitive investment environment, that is albeit still showing discounts in comparison to pricing levels in Western Europe.

There will be continued demand for office investments, especially those in the established Warsaw office locations such as CBD, Mokotów and Jerozolimskie, from all investor types, however, there will be lower availability of suitable product to buy over the next 12 months as a result of decreased development activity over the financial crisis years. Therefore investors will most likely turn their attention to the wider retail and warehouse and sectors. This trend has already been noticed in Q4 2010 and therefore is forecasted to carry on throughout 2011.

Whilst activity in the larger shopping centres in the main cities is setting the pace, there is also more interest in established centres in more regional cities and in retail parks and such interest will be increasing throughout 2011. There are transactions now in progress that will show that investors are now targetting investments on a wider geographical area. There is a number of shopping centres that are available to be purchased in the medium-sized cities, offering significantly higher yields than those in the largest cities. In some cases this can be as much as 200bps.

A similar situation is taking place in the logistic investment market. Investors are becoming more active in this sector, although current interest has been focused mainly on the long-let properties or larger portfolios. This market is showing significant discounts to the pricing levels of prime offices or retail. The last transactions in this sector have been completed in Q3 and at the beginning Q4 2010 at the levels of ca 8.50% - 8.75%. Yields are compressing as recent offers have been made at below 8.50% and for the prime assets with long lease terms as low as 8.00%. In-town locations will also be gaining in importance, as some investors are reconsidering their criteria and are reverting back to the logistics sector seeking higher returns. Activity in this market should therefore increase further if not limited with the lack of new supply.

We also predict that there will be more activity in the pre-purchase / pre-funding transactions, especially for new offices, as investors recognise that new supply is limited. This strategy will be supported by lower vacancy rates in all property sectors during 2010. New developments have been delayed mainly as a result of lack of equity and / or banking conditions requiring pre-leasing of part of the floorspace. This might be chaning however, as the banks are becoming more flexible and the letting market has been significantly improving.

Taken overall, conditions in the property market are positive with the expectation of greater investor activity with wider and expanding targeting leading to compression in yields. The property fair in Cannes – MIPIM, should be another milestone in development of the market and from that point investor activity should increase with a newer, stronger pace.

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