Poland Property Breakfast: Fundamentals supporting growth also in secondary cities

PIE's Poland Property Breakfast assembled five experts to discuss the topic: Is Poland property overbought or can value be found with the right strategy? Held in Tishman Speyer's newly-opened TaunusTurm in Frankfurt, PIE welcomed (left to right) Eric Assimakopoulos, Managing Partner of Revetas Capital Advisors in London; Walter Hampel, MD and Head of Real Estate Finance CEE, Austria & Switzerland for Munich's pbb Deutsche Pfandbriefbank; Adrian Karczewicz, Transaction Director for Skanska Commercial Development Europe in Warsaw; James Turner, founder and MD of Balmain Asset Management, based in London; and Anna Zabrodzka, Central and Eastern Europe Economist for Moody's Analytics, based in Prague.

Poland's strong fundamentals to drive growth

With Poland on a growth tangent projected at above-average rates over the coming 10-15 years, the country should be firmly on property investors' radar, the PIE Breakfast heard. While a few prime markets are becoming hot, Poland as a whole is not yet overbought yet.

"We are looking at a series of markets rather than a country focused around one major hub, such as London or Paris," said Balmain's Turner. He is happy to invest in smaller towns and assets as the whole country offers solid investment opportunities. "It is involved in smart economics, has strong regional production and industries and is a lot more diverse market than others in CEE, maybe apart from the Czech Republic, which is however far smaller." The strong relationship with Germany also helped Poland come out of the recent crisis virtually unscathed. "It's the reason why Poland did not go into recession," he noted.

A strong middle-class has emerged over recent years, which is particularly boosting the retail sector, and GDP growth has been at around 3% at the same time, far higher than that of its CEE peers or the Eurozone. "Apart from that, the society is young, there is a culture of entrepreneurship and hard-working people," said Skanska CDE's Karczewicz. Added Turner: "If you take all that in, there is no reason why the Polish market shouldn't continue to grow." Walter Hampel of German property financier pbb projected above-average rates over the coming 10-15 years. Moody's Analytics' Zabrodzka added that this growth was mainly driven by domestic demand. She expects it to slow down a bit in second half this year but no major downturn.

Looking at specific asset classes, retail emerged as a favourite. "Some 10-15 years ago, the sector as such didn't exist, now we are looking at a stabilised market," said Assimakopoulos, head of Revetas, an opportunistic and value-add investor. Even the large conglomerations still have capacity for new retail space, maybe with the exception of Poznan which has

an oversupply. Overall, both international as well as domestic retailers are expanding. "Polish shoe chain CCC is now moving to Germany, for example," said Turner. Balmain looks all retail assets, from high street to large malls, preferring grocery-anchored assets. Turner is cautious on the luxury segment as demand is not very high for these products yet. "The Poles are sensible, value-focused consumers," he said. Consumption has grown steadily, mirroring the rest of Poland's economic growth. "It never grew excessively, such as in Spain," said Zabrodzka. "Consumers are very realistic on what they can afford to spend."

For office assets, Assimakopoulos identified best opportunities in overleveraged assets, those with refurbishment needs and those out of funds that need to exit. "Warsaw also still offers good office opportunities," said Hampel. The gap between prime and secondary stock is widening, but good assets will find tenants in the capital, maybe at somewhat lower rents after a number of completions hit the market. "If the underwriting is sound, that means also at lower rental levels, we are happy to finance," he said.

Assimakopoulos and Hampel were not bullish on hotels, citing oversupply in many cities and revenues mainly from tourism rather than business travel. "The logistics sector, while a sound investment, is dominated by the large platform players and thus difficult to source as a product," said Assimakopoulos. The presence of these large players will attract other investors, however, who see their confidence in the country. Hampel said pbb will finance all asset classes in Poland, apart from residential, which should be a domestic play. As to lender competition, "that is usually strongest from other German and Polish banks," he told the panel. UK banks are not back in any strength yet, though Karczewicz noted that HSBC recently opened an office in Krakow. Continued Hampel: "We are positive on finding our share in the market." Non-bank lenders are "looking", he added. With insurers such as Allianz already very active on the direct investment side, he expects them to turn to lending soon.

Distressed assets coming out of banks are not an opportunity in the country. "Banks are not selling off their distressed assets and there are simply no €1bn portfolios out there," said Assimakopoulos. Austrian Erste Bank set an example recently, he added, with taking large write-down hits on their CEE portfolio. He expects other banks to follow suit. Hampel also doubts that much distressed product will come out of banks in Poland. "From Romania and Hungary, yes, but not Poland." ■ **pie**

Adrian Karczewicz (top left) talks about Polish labour force and work ethics, while James Turner (top right) points out the country's strong retail performance. Eric Assimakopoulos (bottom) is not too bullish on the hotel sector, however.

Polish residential starts to emerge

With 70% home ownership rate and government incentives to buy homes for young families, the Polish rental housing market remains small and fractured. Yet several domestic and international investors are planning activity in the sector, especially with new building schemes.

"We already invest in office and retail and are now thoroughly analysing the residential sector," Assimakopoulos told the briefing. Skanska, which has been active in the country since before the fall of the Iron Curtain, predominantly develops offices but has also started on some residential projects. "But only on a small scale, making up around 5% of our activity now," said Karczewicz. He does not believe the rental sector will ever be huge. "Even the Warsaw rental market is small, partly due to the fact that the city

Walter Hampel (top left) projected above-average growth rates for Poland over the coming 10-15 years. Anna Zabrodska (bottom) answers a question on the residential sector from the audience, and pointed to specific growth centres.

only has 2m inhabitants – which is merely 5% of the total population – and is mostly operated by small, private landlords."

Delegate Maximilian Mendel of REAS Residential Advisors noted that most of these flats are rented out illegally. "Nevertheless, the residential market is emerging," he said. "There are a lot of domestic initiatives for the development of new housing on a larger scale, and several German, UK or Dutch investors are looking to allocate in the sector, mainly in new product as no larger standing portfolios are ready to be taken over." Added Zabrodzka: "At the same time, the government continues its support for young families to acquire their own home." Mortgage lending has increased steadily over the past years, with domestic banks dominating the sector, "as should be," added Hampel.

"We believe it's a solid country, with a series of markets rather than just one centre," said Turner. The strength in the regions, which make him confident on retail investments outside the largest cities, also provide for good fundamentals for a broader residential sector. ■ **pie**

Time right to look into secondary cities

With the Warsaw office market having reached a peak, investors should look into the regional Polish cities, most of which have strong fundamentals to support an active investment market, panelists agreed.

Zabrodzka set out an east-west divide, with the eastern part more focused on agriculture. "But strong regional centres are also emerging there, with Lublin as one example." Moody's Analytics, which analyses employment, wages, retail sales and GDP across the regions now, attested strong overall performance not only for Warsaw but also for cities such as Wroclaw, Gdansk – where the new port is attracting business from Szczecin – or, more surprisingly, Rzeszow, close to the Ukrainian border, and Bielsko-Bialo in the south. "We are more careful on Lodz, as the population is actually diminishing in the city."

Assimakopoulos said Revetas is looking to invest in northern Poland and is in negotiations on several deals there. Skanska, which focuses on office development, started in Warsaw but is now firmly entrenched in the regional cities as well. "We recently sold assets in Katowice and Wroclaw, and have developments in Krakow, Poznan and Lodz," said Karczewicz. "We are trying to meet tenant demand rather than think of the investor." He added that his firm, as a total equity player, is a lot more flexible than other developers on the timing of their projects. "I can see that some are under real pressure in Warsaw."

Karczewicz noted that the biggest leases are now signed in the regional centres. New firms are settling there as well as old ones expanding. Business process outsourcing was identified as a strong driver of regional office take-up. Taking Indian IT firm Infosys as an example, Karczewicz said that it started only with basic operations and a 3,000 sq.m. office but is expanding to mid-management functions now, with 21,000 sq.m. space. "BPOs have become the biggest employment sector in Poland, with 130,000 people working in the sector," he said. "Some 20,000-30,000 are added each year." But Zabrodzka cautioned that with the growth of the service sector, wages rose accordingly. "There is still a gap to western countries but it is closing." She also underlined that the sector is changing in structure from low to mid-level support. "They currently find a well-educated young labour force but an unfavourable demographic development means that this supply will soon decrease." ■ **pie**