CEE
Investment Market Overview
Spring 2009

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In 2008, real GDP growth slowed noticeably in all countries in the region

Executive Summary

Until the autumn of 2008, Central and East Europe (CEE) appeared relatively resilient to the global credit crunch, with “decoupling” remaining a fashionable theme. However, following the collapse of Lehman Brothers in September 2008, and the ensuing sharp rise in risk aversion, CEE emerged as the most vulnerable Emerging Market region to financial deleveraging because of many countries’ heavy reliance on external finance.

In 2008, real GDP growth slowed noticeably in all countries in the region, with the Czech Republic and Poland expanding by 3.5% and 4.8% respectively, and Russia growing by 6%. Much steeper falls in GDP are forecast for 2009, with outright recessions predicted for several markets in the region.

In Q4 2008, industrial production and exports in the core CEE markets fell rapidly. With the exception of Poland, these markets are heavily reliant on external demand and therefore more exposed to the collapse of the car industry. Some of the growth drivers in CEE went into reverse, with some international firms postponing their expansion plans and/or cutting costs by reducing their employment in the region. Retail sales in CEE, which were growing rapidly over the last several years, slowed dramatically in Q4 2008, particularly in Russia.

The external value of many of the region’s local currencies fell sharply in Q4 2008 as investors worried about the region’s financing requirements and growth prospects, often failing to differentiate between markets.

The CEE banking sector, which is 75%-owned by West European parent banks, came under severe pressure in Q4 2008 as deleveraging provoked fears about the ability of parent banks to keep financing their CEE subsidiaries. Developers and investors were suddenly confronted with severely restricted debt facilities.

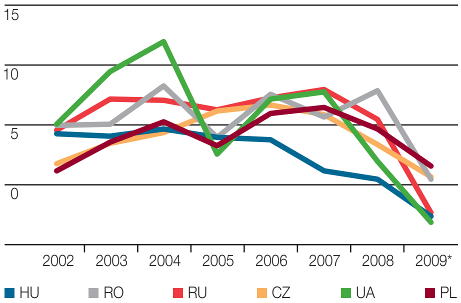
Equity-rich buyers remained the most active players on the market. The rise in risk aversion led to an even sharper focus on property fundamentals, with investors seeking long-term rental income secured on a braod range of tenants in good quality properties in the best locations.

However, the enduring mismatch between buyers’ and sellers’ price expectations led to a sharp fall in transactional activity in 2008 and precluded new benchmark transactions..

The prospects for the CEE investment markets hinge heavily on vendors’ willingness to accept higher yields and lower capital values. CEE is less advanced in its market correction and needs to demonstrate pricing levels which are more attractive to institutional investors on a risk-adjusted basis vis-à-vis West Europe.

GDP Growth

by country, 2002-2009*, percent

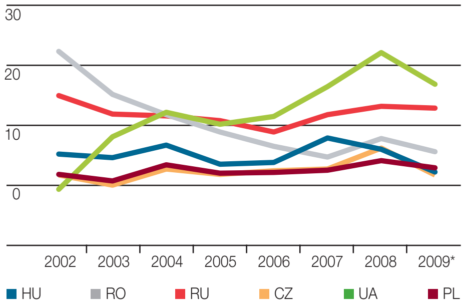


* Forecast

Source: DTZ Research

Inflation

by country, 2002-2009*, percent



* Forecast

Source: DTZ Research

Investment Volumes

Direct investment in CEE commercial property has been weakening gradually since early 2007. DTZ estimates that approximately 160 properties were traded in the six main markets of Poland, Hungary, the Czech Republic, Romania, Russia and Ukraine in 2008, constituting a total transaction volume of €8.9 billion. This represents a 43% fall on 2007 volumes, underscoring the continued uncertainty and risk aversion across CEE. To date, the total capital allocated to the six markets has reached almost €50 billion.

Despite the severe weakening of its economy in H2 2008 due to the collapse in oil prices, Russia remained the most actively traded market, and the only country which witnessed a rise in volumes relative to 2007. The largest falls in investment occured in Hungary, Ukraine and the Czech Republic.

The average size of transactions in the region continued to decrease, from €85 million in 2006 to €55 million in 2008. This can be attributed to properties of a lower lot size being transacted and a smaller number of portfolio transactions.

The share of deals over €100 million increased from 52% in 2007 to 60% in 2008, with a large portion of these transactions occuring in Russia.

Source of Capital

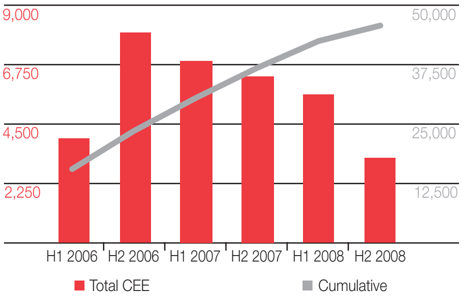
Purchases by local investors rose from 16% in 2007 to over 22% in 2008, with most of the activity taking place in Russia, Ukraine and the Czech Republic.

German investors remained the most active buyers on the market in 2008, accounting for 31% of the capital allocated to the region. They were followed by Russian purchasers, with a 14% market share. UK investors, which previously led investment activity in the region, saw their share of purchases drop to 10.6%.

Private property vehicles dominated investments across the region, while the share of institutional investors decreased significantly.

Investment Volume in CEE*

€ million

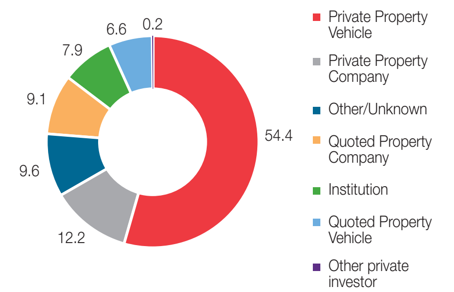


* CEE = Russia, Romania, Poland, Czech Republic, Ukraine, Hungary

Source: DTZ Research

Investment by Type

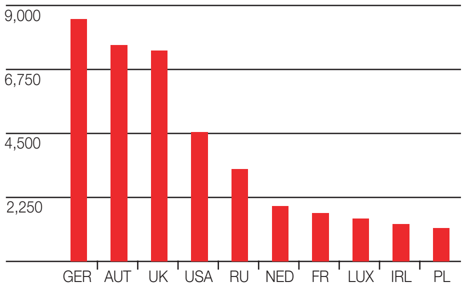
2008, percent



Source: DTZ Research

Source of Capital

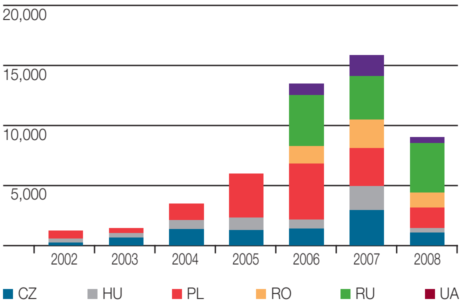
1999–2008, € million



Source: DTZ Research

Destination of Capital by Country

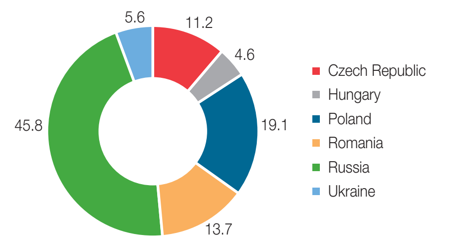
2002–2008, € million



Source: DTZ Research

Investment by Country

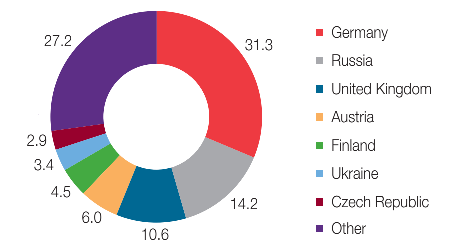
2008, percent



Source: DTZ Research

Source of Capital

by country, 2008, percent

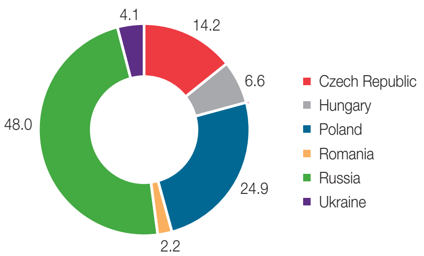


Source: DTZ Research

Investment by Sector

Office Investment Transactions

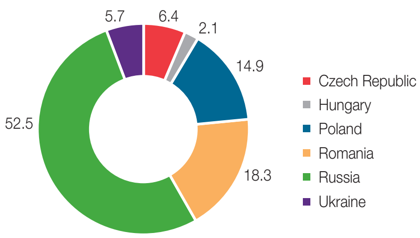
by country, 2008, percent



Source: DTZ Research

Retail Investment Transactions

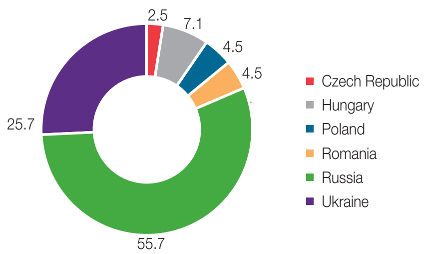
by country, 2008, percent



Source: DTZ Research

Industrial Investment Transactions

by country, 2008, percent



Source: DTZ Research

Offices continued to be the most actively traded sector in the six main markets, accounting for over 50% of the capital invested in 2008. Among all asset classes, offices were percived as bearing the lowest risk.

Retail properties accounted for 34% of total volumes, roughly on a par with last year`s figure.

The share of logistics/light industrial properties decreased from 11.2% in 2007 to 6.3% in 2008, while mixed portfolio properties' share dropped from 10.6% to 8.7%.

Office

Among the six main countries, Russia dominated the office market, accounting for some 48% of investments. Offices continued to be an attractive asset class in Poland, although its share dropped from over 30% in 2007 to 25% in 2008. Although offices remained actively traded in the Czech Republic, their share fell from 24% in 2007 to 14%.

Mixed portfolio

Mixed portfolios were no longer actively traded in the region. In 2008, Romania dominated the mixed portfolio sector in which three large lot size projects were transacted.

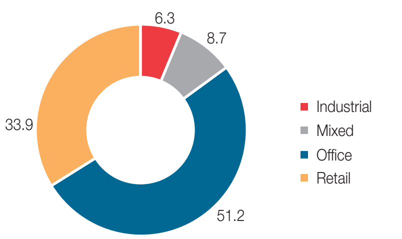
Retail

The share of investments in the retail sector in Russia was the highest among the six main markets in the region. 53% of retail transactions in 2008 were in Russia, despite the sharp fall in private consumption at the end of the year. Romania also had a high share of retail transactions accounting for 18% of total investments in the sector, overtaking Poland, previously the region's undisputed leader in retail transactions.

Retail investments in Poland had risen to an unsustainably high level, and thus saw its share in the region decrease from 45% in 2007 to 15% in 2008.

Investment by Sector

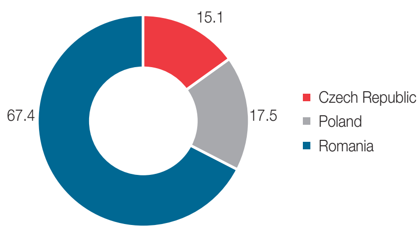
2008, percent



Source: DTZ Research

Mixed Portfolio Investment Transactions

by country, 2008, percent



Source: DTZ Research

Logistics/Light industrial

Logistics/light industrial investments in Russia remained on a par with 2007, accounting for over 55% of investments in this sector among the six main markets. The first significant transactions in the industrial sector were concluded in Ukraine, involving the purchase of a warehouse portfolio.

Pricing

Prime Yields Evolution									
	Office			Retail			Industrial		
	2007	2008	2009*	2007	2008	2009*	2007	2008	2009*
Prague	5.25	6.75	7.35	5.50	7.00	7.35	6.50	8.50	9.25
Budapest	6.00	7.25	8.50	6.00	7.25	8.50	7.00	8.75	9.50
Bucharest	5.70	8.00	8.50	6.50	8.50	9.00	7.50	9.50	10.00
Moscow	7.70	9.50	10.00	8.50	10.50	11.50	10.00	11.50	13.00
Kyiv	9.50	9.50	16.00	9.60	10.00	18.00	10.00	10.50	20.00
Warsaw	5.50	6.25	6.50	5.50	6.50	7.00	6.50	7.00	7.50

* Forecast

In 2008, the repricing of the CEE investment market significantly lagged the market correction in the UK because of an overall lack of liquidity and transparency. Many transactions were put on hold as a result of the persistent gap between buyers' and sellers' price expectations. There was a much smaller number of institutional-grade assets brought to the market in 2008.

CEE commercial property lost some of its appeal relative to other asset classes in 2008, with many investors turning to higher yielding and relatively safer investments., This caused German open-ended funds to suspend their redemptions in October and put their investments on hold.

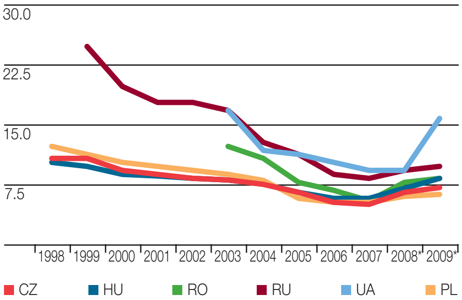
Prices of prime properties that had remained fairly resilient to the global credit crunch in the first-half of 2008 began to soften towards the end of the year. In some markets the upward pressure on yields resulted in a return to 2004/2005 pricing levels.

Overall, prime yields in all sectors in the six main markets moved out by up to 200 bps. Moscow, Prague and Budapest experienced the strongest yield decompression.

A further repricing of assets in 2009 is expected across all sectors.

Prime Office Yields

1998-2009*, percent



* Forecast

Source: DTZ Research

Prime yield – yield that an investor would expect at year-end for one of the best properties, fully let at market rents, which is of the best quality, in the best location and with the best tenant covenants and institutional leases.

CEE commercial property lost some of its appeal relative to other asset classes in 2008

Trends

- The heightened level of uncertainty in the CEE investment market will persist as the region enters its sharpest economic downturn since the early 1990s. Differentiation between markets, based on underlying macroeconomic and occupier fundamentals and exposure to financial sector deleveraging, will be key to real estate investment strategies across the region.

- Increasing cash-flow concerns and restricted debt facilities will put further upward pressure on yields. Reprcing and transactional activity across CEE will hinge on distressed vendors exhausting all other options to restructure their assets and accepting lower capital values and higher yields. Levels and access to funding will be key concerns of investors in 2009.

- The resilence of occupational markets against a rapidly deteriorating economic backdrop will be the key factor in pricing assessments in 2009.

- Opportunity funds, private investors and, provided they return to the market en masse, German open-ended funds will be seeking opportunities to re-enter the market by targeting distressed vendors in those markets most vulnerable to the economic downturn.

Major Investment Transactions, 2008

Country	Location	Sector	Property	Purchaser	Nationality	Volume, € million
Russia	Moscow	Office	Paveletskaya (forward sale)	KanAm Grund	GER	570
Russia	Moscow	Office	Citydel	KanAm Grund	GER	380
Russia	Moscow	Retail	Vremena Goda	Ivanhoe Cambridge, Europolis	CAN/AUT	350
Romania	Bucharest	Residential & office	Upground Project & Office building	RREEF Real Estate	GER	340
Russia	St. Petersburg	Retail	K-Rauta chain property	Northern European Properties Limited	SWE	240
Russia	Moscow	Office	Silver City	RP Capital Group	UK	222
Czech	Prague 4	Office	The Park phase I (1-7 buildings)	DEGI	GER	235
Russia	Moscow	Retail	Na Bagrationovskom	Orco Property Group	LUX	190
Romania	nationwide	Retail	Winmarkt Portfolio	IDG Group	IT	182.5
Poland	Warsaw	Office	TPSA portfolio	BPT	DEN	168
Poland	Warsaw	Office	Marynarska Business Park	DEGI	GER	167
Poland	Warsaw	Office	Rondo 1	Macquire Global Property Advisors	AUS	160
Russia	St. Petersburg	Warehouse	AKM Logistics, 50%	Raven Russia	UK	153
Romania	Bucharest	Retail	Iris Shopping Center	DEGI	GER	147
Hungary	Budapest	Office	Bank Center	GLL	GER	130
Czech	Olomouc, Ostrava	Retail	Haná retail park, Futurum Ostrava, Retail Park Ostrava	Pradera	UK	125
Poland	Wrocław	Office	Bema Plaza	Deka	GER	106
Poland	Katowice	Retail	Trzy Stawy	Union Investment	GER	95
Poland	Poland	Retail	12 shopping centres	GE RE	US	80
Poland	Poznań	Mix	Andersia Tower	Deka Immobilien	GER	80
Czech	Prague 1	Office	Praha City Centre	GLL	GER	76
Czech	Prague 5	Office	Anděl Park	SEB Asset Management	GER	71.5
Romania	Bucharest	Retail	Expo Market Doraly	HSBC European Infrastructure Investments	UK	70
Romania	Bucharest	Residential	Satul Francez ("The French Village")	Raptis Kavouras	GR	68
Hungary	Budapest	Office	Krisztina Palace	Unilmmo Global	BEL/GER	60
Poland	Sosnowiec, Gdańsk	Retail	Fashion House	AIB Polonia	IRL	60
Poland	Warsaw	Office	Tulipan House	Commerz Real	GER	59.7
Czech	Prague 5	Office/Retail	Anděl Palace	DEGI	GER	57
Czech	nationwide	Office	1/3 of the O2 Telefónica Portfolio	MEI	NL	52
Czech	Karlovy Vary	Retail	Varyáda	Invesco	USA	52
Poland	Poland	Retail	14 shopping centres	Balmain Asset Management	UK	52
Romania	4 cities	Residential & office	Real Estate Portfolio	Black Sea Global Properties	RO	50
Romania	Bucharest	Retail & residential	Parklake Plaza	Sonae Sierra	PT	45
Ukraine	Kyiv - left bank	Retail	Aladdin	Meyer Bergman	UK	42
Poland	Warsaw	Office	Salzburg	SEB Asset Management	GER	41
Poland	Gądki, Grodzisk Maz.	Warehouse	Raben Group	TMW Pramerica	GER	40
Romania	Bucharest	Office	BOB Tower	Eurobank Real Estate	GR	40
Poland	Gdańsk	Office	Arkońska	SEB Asset Management	GER	38
Ukraine	Kyiv region	Logistics	East Gate Logistic	Akron Group / AICEEII	AUT	35
Ukraine	Kyiv - Petrivka	Retail	Alta-Centre	VK Development / Davento Plc	UA	35
Poland	Wrocław	Office	Silver Forum	GE RE	US	34
Poland	Warsaw	Warehouse	Good Point	PBW II	LUX	27.5
Hungary	Budapest	Office	Vaci Utca Centre	Generali Austria	AUT	27
Poland	Lublin	Retail	Galeria Orkana	Endurance	LUX	26.5
Romania	Arad & Timisoara	Industrial	Arad & Timisoara Industrial Parks	Catalyst Capital	UK	25
Hungary	Biatorbágy	Industrial	Tulipan Park	SEB Asset Management	GER	21
Ukraine	Kyiv region	Logistics	Logistics Park East 1	Europa Capital	UK	18
Ukraine	Mykolayiv - CBD	Retail	City Centre	UNIQA Real Estate	AUT	18
Czech	Plzeň	Retail	Retail Park Plzeň	ING RE	NL	16
Czech	Prague 5	Office	Phillips Building	Heitman	USA	15

DTZ Research

Contact:

Consulting & Research

DTZ
Lumen Office Building/Złote Tarasy
Ul. Złota 59
00-120 Warsaw, Poland
Tel.: +48 22 222 3000
Fax: +48 22 222 3001
info@dtz.pl
www.dtz.com/pl

Kamila Wykrota
Senior Market Analyst, Consulting & Research

Mobile: +48 600 382 322
Email: kamila.wykrota@dtz.com

CEE Investment Team

DTZ
Bajcsy-Zsilinszky út 42-46
1064 Budapest, Hungary
Tel.: +36 1 269 6999
Fax: +36 1 269 6987

Doug Hardman
Regional Investment Director, CEE

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