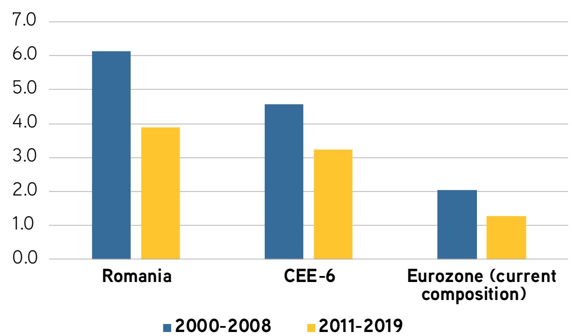
COLLIERS INTERNATIONAL ROMANIA
MID-YEAR MARKET UPDATE

ECONOMIC OVERVIEW

ECONOMY CONTINUES TO RUN FAST DESPITE INCREASED HEADWINDS

If the Romanian economy was running in a contest, it would be in marathon territory right about now (and close to finishing it, at that). After the strong GDP growth in the first half of the year (and in spite of signs of a weaker second quarter), the full year expansion figure looks more likely to top 4% versus our previous call of 3.7%, which also suggests that some professional forecasters (i.e. local bank analysts) may have gone too far with a pessimistic approach, as estimates event went below 3% at one point. Either way, 2019 looks set to become the 9th consecutive year of continuous growth for Romania, equaling the previous record streak, seen between 2000 and 2008. Still, in tune with what has been happening with other CEE economies, the convergence process to western European levels has cooled quite a bit, but Romania remains the outlier in terms of economic performance. Also, as we underscored in the past, the so-called potential growth rate – which designates what can be regarded as the sustainable expansion rate – is still one of the highest in the EU in European Commission estimates, at over 3% for the next couple of years, more than double the Union's average.

Romanian growth streak already reached previous record in 2011-2019 period

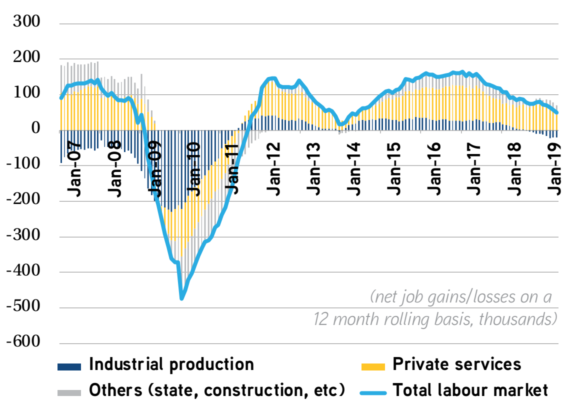


Data Source: Eurostat, Colliers International

The robust 5% year-on-year GDP growth rate seen in 1Q19 was second best in the EU, marginally behind Hungary's, though the second quarter GDP, for which no detailed figures exist, saw growth cool to 4.4% according to the flash estimates released mid-August. These developments are largely the result of strong private consumption (up by around 7% year-on-year), which continues to be the main driver. A bit worryingly, capex expenditures remain soft and net exports have become a drag on growth for some time on account of higher imports and weaker exports. And as things look right now, it is unlikely for external demand to stage a significant recovery. On the contrary. In fact, Romania's current account deficit (which measures the net FX outflows on this channel), mostly generated by the goods trade gap, looks set to breach the 5% of GDP level this year, setting Romania apart from other CEE countries which are rather running surpluses. Still, it is important to note that Romania has historically run higher deficits than the regional peers and would still win the “most improved” badge in the region when compared to pre-crisis levels.

As the fiscal gap could drift past the 3% of GDP threshold by year-end, the twin deficits (i.e. the budget and current account gap) look a bit troublesome, though the robust GDP expansion means that the correction need not be brisk or rough

Labour market cooling, indicative of late phase of economic cycle



Data Source: INSSE, Colliers International

and that Romania can still grow its way out of trouble. The base case for the local economy going forward looks like a gradual softening coupled with adjustments rather than a deep recession. That said, with the government already having hiked some taxes in September in order to cope with the wider budget deficit (more such decisions may be on the way), headline inflation could move higher than the c.4% reported mid-2019. Still, with major central banks (Federal Reserve, European Central Bank) in easing-mode, it is highly unlikely that the National Bank of Romania will move the other way; rather, it will hope that the economic slowdown will help with watering inflation down, thereby keeping rates largely flat, and this looks like a safe bet.

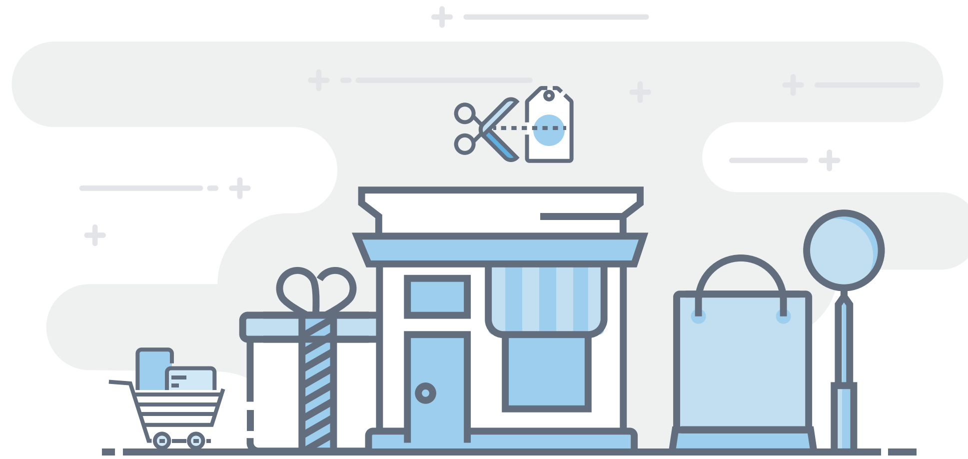
There are signs that the economy has already peaked for this cycle and that it is getting ready to shift into a lower cruising speed. In recent years, growth has been closely tied with the rise in wages, which came on account of a couple of reasons: i) state wage policies (minimum pay hikes and state wage increases) and ii) a tight labour market. The former is no longer the case, given the limited fiscal room that the government has and the fact that minimum wages have increased very fast. At the same time, the labour market tightness could start reversing soon, as job creation has cooled down markedly in recent months, while for industry, at least, it has actually moved in negative territory for more than half a year – external demand likely played the big part in this. It will take some time before this feeds into visible weakness and though it might not be obvious this year in absence of any negative external events (say, related to Brexit, the US president’s foreign trade policy or the weakening Eurozone economy), the outlook for 2020 is softer than for this year. Otherwise, the jitters in the global financial markets in August mean that external risks are worth closely monitoring, as these could ultimately serve as a magnifying glass for the internal issues like the twin deficits. Still, as we highlighted above, the GDP expansion is still likely to trump that of developed Europe, so enough to keep the economic convergence engine going, meaning the overwhelming long-term case for Romania remains quite bullish.

POLITICS REMAIN A BLUR, BUT THERE ARE REASONS FOR OPTIMISM

With 3 very important election rounds in the next year and a half (presidential, local and general elections), politics will be one of the main themes during this period. The warm-up round already took place in May, with the vote for the European Parliament signaling a possible turning point and potential changes on the horizon (mostly for the good). The ruling coalition’s score almost halved to below 27% (with centre-left PSD at under 23%) from almost 51% at the end 2016 general elections, with centre-right opposition party PNL scoring nearly 27% and the surprising newcomer reformist USR+ polling at over 22%.

It is important to note that in the EIU’s Democracy Index, Romania has consistently underperformed in two major categories: political culture and political participation. Recent years offer some reasons for optimism, with massive street protests and a spike in voter turnout. A bit over 9 million Romanians voted a few months ago, a surge of over 60% versus the previous European Parliament elections, reaching a level of turnout reserved in the past for the much more popular presidential elections; among young people, interest has reached record levels. To look at the positives: 1) despite the government’s fiscal largesse and populistic rhetoric, the ruling coalition dropped in voter intentions, suggesting that such an approach does not sell anymore; 2) Romanians showed overwhelming support for the EU with this vote, with no Euro-skeptic party scoring big (though the ruling coalition did take frequent jabs at the EU); 3) post-elections, the ruling coalition has started to back down from its controversial changes to the judiciary. Over the longer run, increased popular pressure on politicians could lead to stronger reform drive and meaningful structural reforms.

RETAIL MARKET



SUPPLY

The first semester of 2019 saw limited deliveries, with just an extension of Electroputere Parc in Craiova (just over 9,000 sqm) partly inaugurated, though the second half of the year is expected to be much more prolific; this seems to be a similar situation to last year's, which also had just two new projects inaugurated in the first semester and a much busier second semester. Meanwhile, for 2019, taking into account this aspect, the full year total stands at an estimated 216,000 sqm, a 50% increase on 2018 and the highest figure since 2011; it is worth underscoring that a fairly large project has been bumped by the developer to 2021 and with development still under strain from increased costs and a tight labour market, some additional delays might occur.

Besides deliveries, we want to underscore the fact that refurbishments remain an important trend amid more demanding consumers; this means shopping centers are tweaking their tenant mix to find just the right balance and keep people spending (including by updating the entertainment and food components). For older shopping centers facing stiffer competition, refurbishments are also a way to remain relevant in front of new and shiny retail schemes.

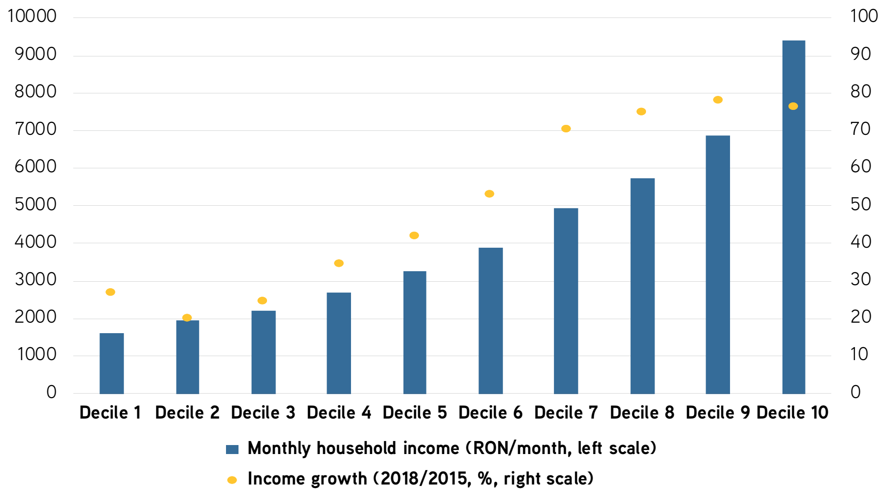
Overall, there are a couple of big trends (not necessarily new) to report on the supply side: 1) growing focus for retail parks; 2) developers eying cities that would have not been on their radar several years ago; 3) small strip malls near dense residential areas.

DEMAND

In spite of some less encouraging signs in some parts of the economy, the consumer seems in very good shape. While inflation is clocking higher speeds than the central bank would be comfortable with (around 4% as of mid-2019), the robust wage growth means that real earnings (i.e. CPI-adjusted) are still growing in double-digits. The tight labour market is underpinning the dynamic wages and this aspect has helped keep consumer confidence, as measured by the European Commission, comfortably above its historic average. This general context has pushed non-food retail sales up by around 10% in the first 6 months of 2019, which is already better than the full year result for 2018 (in the 6% region).

We looked at the detailed breakdown of household earnings by deciles for any hints it may offer about consumption patterns (the first decile means the 10% households with the smallest earnings, the subsequent 10% and so on). Surprisingly, despite a socialist government pursuing policies aimed at boosting income, particularly for those with small earnings, the main beneficiaries of this economic cycle seem to be those at the top end of the earnings scale. The top 40% households saw their income jump by over 70% in the last four years while the bottom 30% had an average income increase of around 24% between 2015

Very uneven gains in Romania in recent years offer good hints on private consumption patterns



Data Source: INSSE, Colliers International

and 2018. Without looking into the causes behind this phenomenon, we believe that it explains why brands in the low- and medium-price bracket category are doing so well, with discounters also seeing very robust results.

Otherwise, we are seeing a lot of interest from retailers in various countries - CEE countries (Poland, Czechia is fairly new to the game, despite Turkish brands dialing it down a notch). As a novelty, we are also seeing players from the Republic of Moldova active (food, cosmetics, shoes). Interestingly, we can also report on an opposite trend gaining much more traction: i.e. Romanian brands expanding in regional countries.

On the other hand, brands that would not have been the typical retail park tenant – like H&M, C&A, LC Waikiki, Hervis – have to go with the flow, since a significant part of present and future deliveries are of this sort. Still, these tenants can receive quite favourable terms, have lower rents and fit-out costs, making the end-results fall only marginally below those in a mall. This is due to the fact that a large number of the new retail parks are popping up in cities with very low competition.

Overall, looking at the current picture on the demand side, the number and diversification of brands is good (maybe leaning on too crowded), in terms of various categories of goods – shoes, jewelry, children's apparel, sports, men's fashion; there is still some room for new players, especially on the entertainment side and women's fashion.

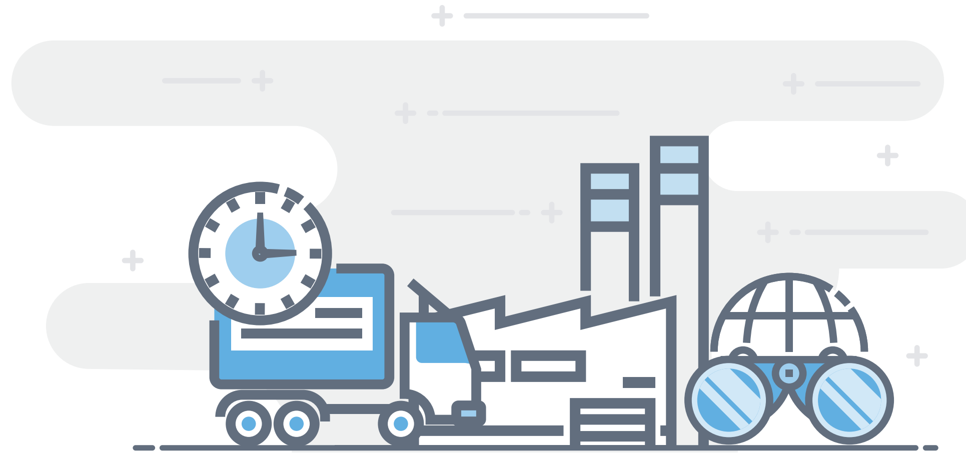
RENTS

Not a lot can be said in terms of rents, particularly after we reported that last year saw the first generalized hike in the post-crisis period. Still, we are noting that as the delivery calendar got heavier, landlords have started becoming ever more careful in attracting the tenants they want. Otherwise, amid increased labour costs and pressures on other prices, service charges are moving north.

FORECAST

Robust consumer confidence thus far, together with strong wage growth is setting the stage for another very good year in terms of retail sales; and this is coming on top of already good results, as Romania has been the CEE champion in terms of consumption expansion this economic cycle. Consequently, developers are keeping their options open and in a town like Bucharest, this also means looking again at long-forgotten projects, some from before the crisis. Overall, some 216,000 sqm of new retail spaces could be delivered this year and 2020 is shaping up to be even busier. Otherwise, since supply growth is no longer coming from the established markets, well-known brands now look at even smaller cities, but their expansion drive is quite cautious and based on carefully thought-out plans and studies.

INDUSTRIAL MARKET

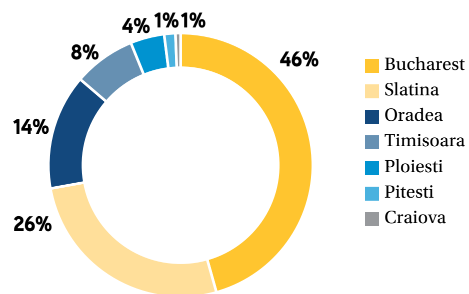


SUPPLY

Around 300,000 sqm of new modern storage spaces came online in the first half of 2019, based on figures reported by the major developers. Due to the somewhat opaque nature of the market, it is difficult to pin the exact figure down, though it is a bit below last year's 330,000 sqm reported for the first semester.

Bucharest accounted for over 40% of the total deliveries, with developers focusing both on the already established western part of the city, alongside the highway to Pitesti, and on various up-and-coming locations spread around the northern part of Bucharest's ring road. Outside the capital, investments continue to be mostly geared towards cities in the region of Transylvania, which accounted for over one third of new I&L spaces.

Storage spaces take-up by location in H1 2019 (%)



Data Source: Colliers International

The market continues to be very much dominated by CTP and WDP, both of which accounted for over half of the supply in recent months, though other players are also growing very fast, like Globalworth, via their own company and through a JV. P3 is also launching a new project in the Chitila area (their second in Romania), while other players like MLP or Element Industrial have also just started setting up shop in Romania, choosing Bucharest as a starting point for their investments.

DEMAND

Market take-up more than doubled in the first semester, to a bit over 240,000 sqm (versus around 110,000 sqm in H1 2018), though this is quite a bit below 2017's first half print, which was north of 330,000 sqm. We mentioned side by side all three figures to highlight that we can see huge swings in terms of market activity, so we would not take this robust growth in 2019 versus 2018 at face value. That said, the figures we have seen thus far suggest a strong market.

A notable transaction was that of Pirelli, which leased 64,000 sqm at a WDP facility in Slatina in one of the biggest deals we have seen in recent years. This also helped cement a strong lead for automotive as a driver for demand, accounting for nearly 52% of the reported take-up in the first semester. This is quite a change of tune compared to last year, which was much stronger on the electro-IT or logistics fronts. Otherwise, in the first 6 months of 2019, industry companies, logistics and FMCG were also strong drivers of demand.

RENTS

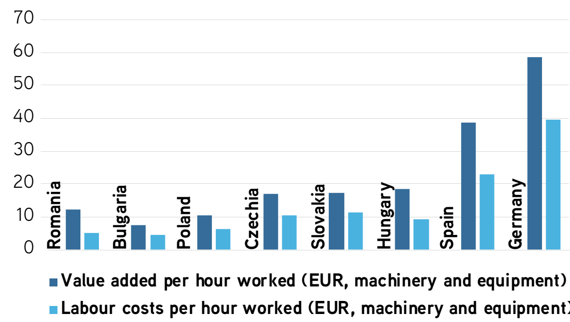
While the market remains oriented towards landlords, the increasing number of active developers (hence, rising competition) and the slightly higher vacancy rates (still in single digit territory throughout most of Romania) mean that rents remained more or less unchanged compared to end-2018, at around 4.15 EUR/sqm, though a touch higher than a year ago. In a sign of developers becoming more flexible, the minimum rental period for existing spaces is starting from 3 years; for new warehouses, on the other hand, developers still demand 5 years in Bucharest and upwards of 7 years in other parts of the country.

FORECAST

So far, 2019 is shaping up to be another strong year – maybe not on par with the record levels seen in recent years, but close enough. Overall deliveries could be in the tune of around half a million sqm, taking the grand total to around 4.7 million sqm of modern storage spaces by year end. Risks to our call seem tilted to the upside.

Still, favourable figures reported over the short term are less important, especially now as the economy seems like it is getting ready to shift in a lower gear. Consequently, the medium-term outlook (i.e. the next couple of years) looks less rosy for several reasons: 1) industrial activity in Western Europe, Romania's main export market, is plunging (in Germany, for instance, based on confidence indicators, manufacturing is posting mid-2019 its biggest decline since early 2009); 2) domestic private consumption could cool down as labour market is starting to look less tight; 3) increasing risks of a fallout from a global trade war. As a special observation, the second point we made will help landlords quite a bit in the not too distant future, as recently, due to the very tight labour market, they had to resort to offering special amenities in order to keep their tenants and their employees happy, like on-site housing.

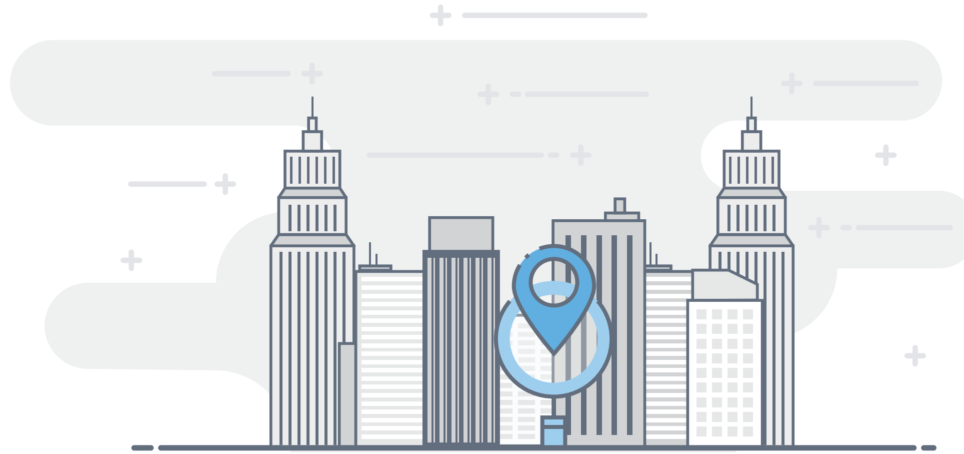
Romania still displays a healthy gap between labour productivity and costs



Data Source: Eurostat, Colliers International

Over the very long run, the outlook remains quite bullish, particularly as Romania continues to look undersupplied relative to CEE peers, while, at the same time, retaining specific advantages compared to most neighbouring countries. For example, looking at the spread between value added and labour costs for manufacturing of machinery and equipment, Romania had the second highest gap in the CEE region, after Hungary, though all CEE was well behind Western European countries. Overall, a market of 8 million sqm of modern warehouse spaces by the end of the next decade (so nearly doubling on 2018's level) looks like a safe call.

OFFICE MARKET



SUPPLY

The first half of 2019 was quite busy in terms of market deliveries, with the market seeing some 185,000 sqm in new spaces, a nearly six-fold jump compared to the same period in 2019, taking the Bucharest modern office stock to 2.6 million sqm. This is also an increase of over 10% compared to last year's end-June stock, making Bucharest the most dynamic among the CEE capitals.

Otherwise, the stock was quite spread across the capital, with the biggest projects, being the new Renault headquarters (47,000 sqm) in the West submarket and Business Garden Bucharest (over 41,000 sqm) in Center West. Other major completions included The Mark, in the CBD, and the third phase of Oregon Park in Floreasca-Barbu Vacarescu (both in the 25,000 sqm area) and also Timpuri Noi Square C and the second building of The Bridge in Center West (both in the 20,000 sqm area). So overall, quite a nice mix between older and newer submarkets, though the balance clearly tilts in favour of the latter. It is also worth noting that in spite of the increased pace of deliveries, the new buildings coming online have quite respectable occupancy rates at delivery (on average, around 75 to 80%, by our estimates).

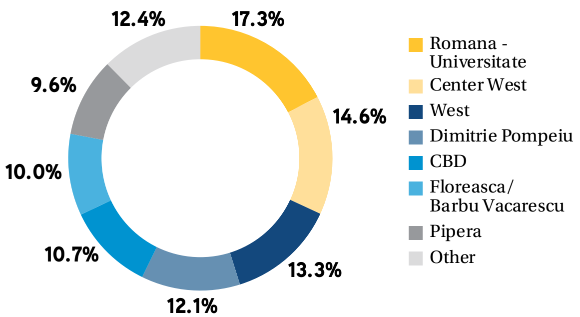
DEMAND

In terms of demand, it is sort of a mixed picture: total demand for modern office buildings stood at 188,000 sqm in the first half of the year in Bucharest, marginally above the previous record for the post-crisis period, set two years ago. That said, upon closer scrutiny, the details reveal some softer aspects, like the fact that relocations from competitive stock amounted to 86,000 sqm, closing in on the record-high figure of over 100,000 reported for the whole of 2018. Also, net take-up decreased by over 40% compared to the first semester of 2018 (which was nearly a post-crisis high), to a reported 49,000 sqm; this includes only actual new demand which is not the result of relocations from competitive stock, as well as expansions. Admittedly, due to the nature of the market and the way figures are reported, it is impossible to pin the exact figure down and it is likely that at least part of the relocations from competitive stock include an expansion component (so new demand).

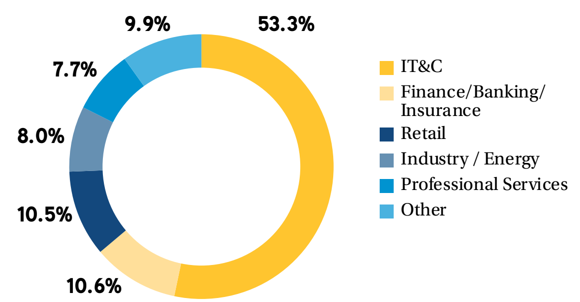
Otherwise, the IT&C dominated the market, accounting for over half of the total demand for office spaces, followed at a great distance by the financial and industrial sectors. That said, to underscore again how tight the labour market is, particularly for qualified employees, just a fraction (about 15%) of the gross take-up generated by IT&C was actual new demand, with the rest either renewals or relocations.

In terms of areas, it was quite an interesting first half of the year, as deals were spread throughout Bucharest rather than a handful of submarkets.

Bucharest 1H19 gross take-up by location and sector

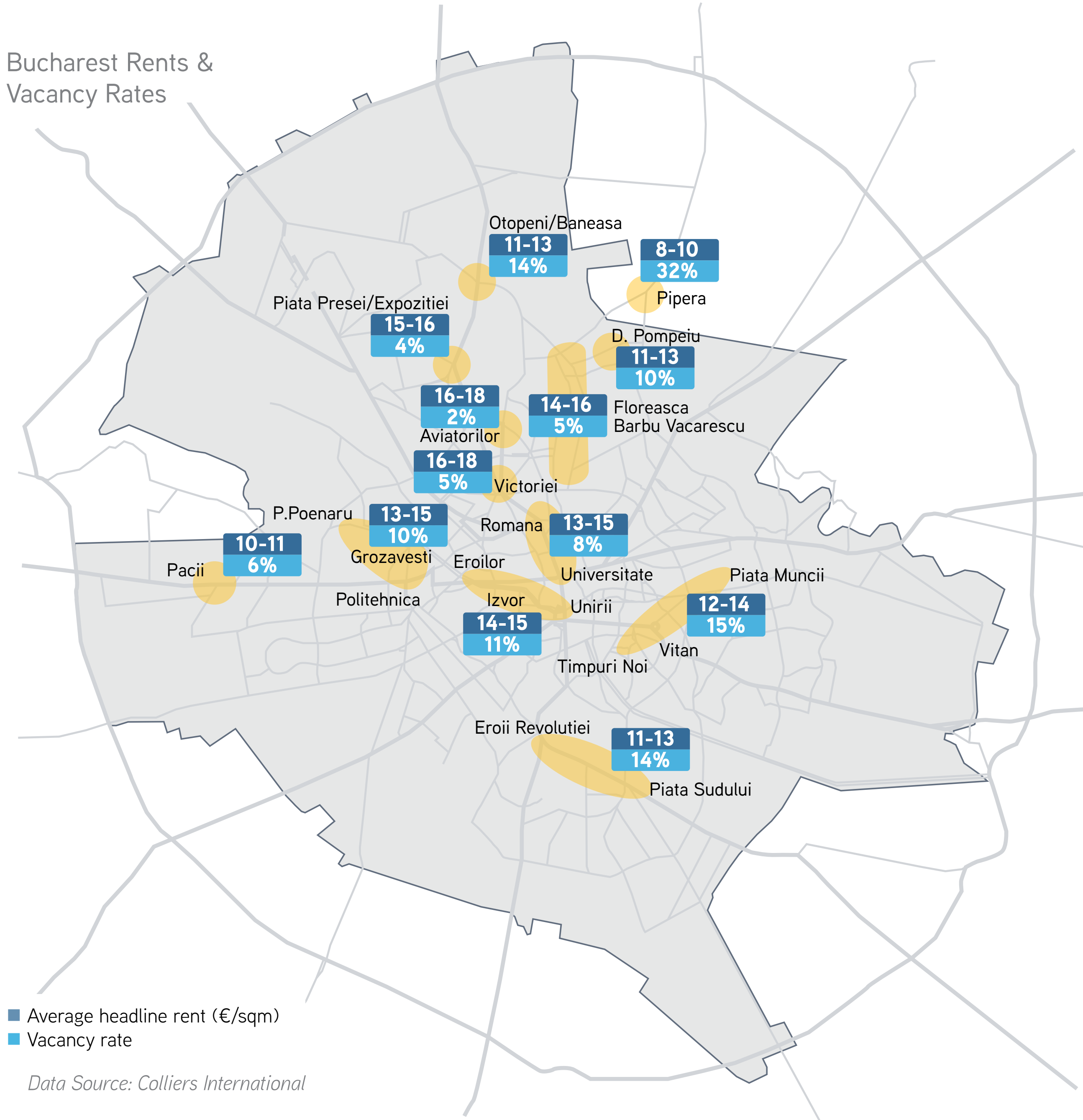


Data Source: Colliers International



Data Source: Colliers International

Bucharest Rents & Vacancy Rates



Data Source: Colliers International

Consequently, Romana – Universitate was the most active area, accounting for around 17% of all deals, but it is not an absolute leader, as the second and third places (Center West and West, with around 13-14% each) are not too far behind. Overall, companies seem to be heading for areas where there are new buildings delivered (particularly Center West), but at the same time, areas like Floreasca/Barbu Vacarescu remain very attractive, as we have not seen too many relocations from here; the CBD is also seeing healthy demand, though there is also some vacancy here that can accommodate it.

RENTS AND VACANCY

Asking rents have remained more or less unchanged in Bucharest, though as the market is becoming more and more crowded, landlords in certain submarkets, as well as those with new buildings seem ready to be a bit more generous in terms of incentives.

Thus far, vacancy has only inched higher, ending 1H19 at around 10% from 9.5% end-2018 and 9% in June 2018. This is quite respectable given what we have been mentioning at the start, that Bucharest has seen the fastest growing stock in the CEE region in the last year.

FORECAST

The Bucharest office market remains quite lively, with another c.150,000 sqm set to come online in the second part of the year and over 230,000 sqm in 2020. Still, it looks like the developers have come to terms a bit with the reality of a slower market and moved a significant part of their projects from 2020 to at least 2021; we would expect that the pipeline for 2021 (currently nearing half a million of sqm) to suffer adjustments and if developers cannot manage to seal some deals, some of the projects due in two years would get pushed back further.

On the other hand, we do expect vacancy to continue climbing and though our call for the end of this year (13%) may seem a bit on the pessimistic side right now, we do see things moving in this direction. A possible explanation for this situation would be the delayed effect of relocations as the bulk of the c.75,000 sqm of pre-leases signed in 1H19 were relocations from competitive stock, so these tenants have not yet vacated their current office space, but may do so later this year or in 2020-2021. Over a longer run, should the vacancy rate climb a bit higher, towards 14-15%, we may see some underlying pressures surfacing on the aggregated rent level for the Bucharest office market, though for now, good office buildings may continue to command solid demand and, in certain cases, even higher rents than a couple of years ago.

REGIONAL OFFICE MARKETS

Total demand in Romania's major office markets outside Bucharest (i.e. Cluj-Napoca, Timisoara, Iasi and Brasov) nearly doubled in the first semester, to just under 30,000 sqm altogether, with around two thirds of this generated by new demand. It is worth noting that in regional markets, quite a lot of deals are direct, meaning that they end up unreported, so the actual market volumes may be quite larger. For the most part, Romania's regional office submarkets remain a bit stronger than Bucharest, as indicated by the lower vacancy rates for modern office spaces, with Iasi's virtually non-existent free space and Cluj-Napoca's well below 10%. Meanwhile, Timisoara, despite the heavy pipeline in the last couple of years, has actually managed to score an increase in occupancy rate. With general unemployment levels smaller than in Bucharest and lower wages, the regional cities remain an attractive prospect for companies seeking to expand their operations in Romania or even a good starting point if the Capital seems too crowded for their taste.

	Vacany rate (%)	Usual class A office rent (EUR/sqm)
Cluj-Napoca	7%	13-15
Iasi	0.6%	12-14
Timisoara	10%	13-15
Brasov	12%	11-13

INVESTMENT MARKET

TRANSACTIONS

The first semester closed with a total real estate investment volume of around EUR 345mn, close to last year's EUR 357mn (revised from over EUR 400mn, mostly due to the exclusion of part of the Oregon Park transaction, as it was paid in two tranches, one in 2018, one in 2019). Given that this is one of the best first semesters in the post-crisis period and there are quite a lot of transactions which could close fairly soon, it is looking like 2019 should be another solid year (the EUR1bn handle could be exceeded by end-2019). Some deals closed around the mid-2019 mark were included in the Q3 figures.

The year's biggest transaction so far was closed outside Bucharest, in Cluj-Napoca, where Dedeman, the Romanian DIY chain, purchased the class A project The Office for around EUR 130mn from a JV formed by NEPI Rockcastle and Romanian developer Ovidiu Sandor. This deal sets many benchmarks to beat in the future: it is by far the biggest office deal closed outside Bucharest and also the third biggest pure office deal ever closed on the local market.

The other significant transaction, of above EUR 110mn, was the buyout of Prime Kapital's shares in 9 retail parks by its joint venture partner, South African group MAS REI, thereby freeing capital for the former to continue developing fresh projects together. Interestingly, in a change of tune compared to last year, just around 28% of the total volume seen in the first semester was generated by properties on the Bucharest market (including the third office building of Oregon Park) versus nearly 90% a year ago. Still, this shouldn't last as quite a lot of big-ticket office assets in Bucharest are currently in various stages of the sale process and some might close soon. Otherwise, office assets still dominated the market in the first semester, accounting for c.62% of the total investment volumes.

Another interesting aspect is the fact that Romanian and South African capital were neck and neck and both accounted close to 50% of the total market volume, so generating all the major deals. We would normally expect Romanian high net worth individuals to continue being active as they are reaping the benefits of the growth cycle and increasingly see real estate as a viable long-term investment vehicle for excess capital.

Prime office yields at end-June 2019 (and change compared to June 2018)

	Bucharest	Warsaw	Budapest	Prague
Office(CBD)	7.25% (0)	4.50% (-0.5ppt)	5.50% (-0.5ppt)	4.50% (-0.25ppt)
Retail	6.50% (-0.5ppt)	4.00% (-1.0ppt)	5.50% (-0.5ppt)	4.75% (-0.25ppt)
Industrial	8.25% (-0.25ppt)	6.50% (0)	7.25% (-0.25ppt)	5.50% (-0.5ppt)

Data Source: Colliers International

The investor base continues to diversify: we are seeing names that wouldn't have considered Romania some years ago, like pension funds from triple A-rated countries, large institutional asset managers or high net-worth individuals/family offices from other countries. Furthermore, we have had interest from investors coming from new regions not so active on the local market (Asia, Middle East).

PRICES

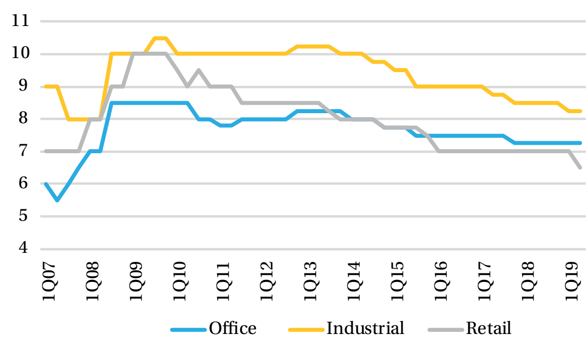
We see quite strong demand for prime office products, which means that there might still be some downward room for yields going forward. Though we haven't seen an office building being sold at or below the 7% threshold, some assets in the market have seen offers at this level and there is momentum for a yield compression, especially for prime assets with long-term contracts. Industrial also remains attractive given the strong leasing market, though investment yields have remained unchanged.

Otherwise, for prime retail assets, we decided to quote the prime yield lower due to several reasons: 1) we kept it flat at 7% for more than 3 years despite increasingly favourable market conditions (increased base rents and much higher sales for tenants); 2) similar assets in CEE countries have seen much more significant declines (some in excess of 1ppt) in the same period. Since so few prime retail spaces exchange hands, it is difficult to gauge the yield without an actual benchmark trade, but we believe that should such a deal take place today, it would likely imply a prime yield around 6.50-6.75% rather than our previous 7% call.

FINANCING CONDITIONS

Banks remain quite open to real estate and this should not come as a surprise given the fast-growing economy that has supported rental activity across al major submarkets, as well as the interest from potential investors. Margins have remained more or less unchanged throughout the last couple of years - around 250 basis points for prime properties, but the major issue that potential buyers are impacted by is still the low amortization period. The good news is that this might slowly be changing and depending on the project and sponsor, it can climb upwards to 20 years on an exceptional basis. Otherwise, the local real estate investment sector dodged a big bullet after the government ultimately significantly sweetened a major tax it decided to slap on local bank assets starting 2019; such events underscore why Romania has a higher sovereign risk premium than neighbouring peers in the first place.

Prime real estate investment yields (%)



Source: Colliers International

Otherwise, while at the start of the year we could have mentioned the prospect of monetary policy tightening at the world's major central banks, now even that is gone and both the Fed and ECB switched to easing mode. Markets have responded positively to the news, meaning that the benign context is being extended, presumably, through 2020.

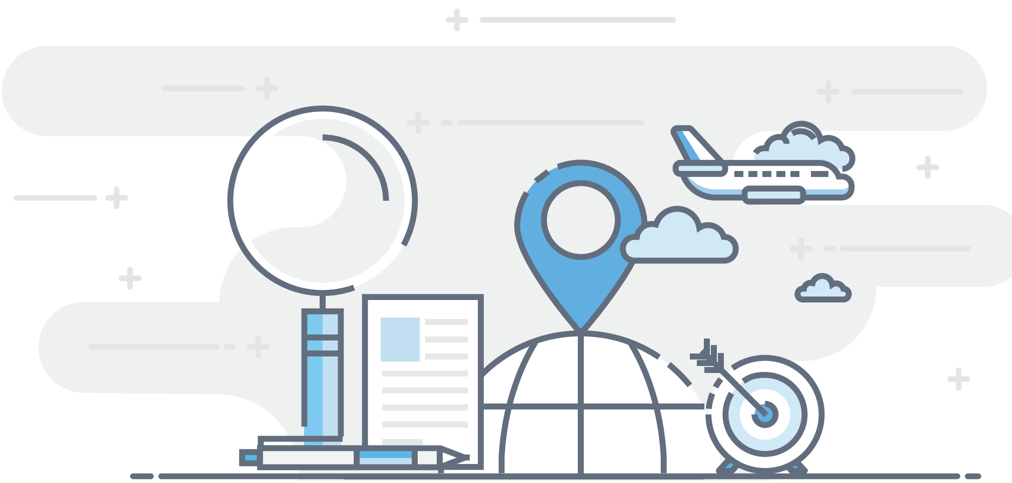
FORECAST

Given the robust office pipeline, it is likely we will surpass EUR 1bn in total investments during 2019, though as usual, deals can get delayed. With two thirds likely to come from the office segment and yield compression events taking place when deals get clustered (at least in other CEE countries), we may see yields move a bit lower in the second half for prime products (maybe even below 7%, though this may be a bit of a longshot). On the other hand, we expect that as the market is seeing lots of deliveries of very good office buildings, it will get even more layered and thus, assets with a value-add angle may actually see yields a bit higher in one-year time from now.

Meanwhile, we are noting that investors seem very attentive to the fluid political scene in Romania and given that we have 3 rounds of elections in the next year and a half (general, local and presidential elections), surprises may lead to big swings in investor sentiment.

Overall, we believe that loose monetary policy at the world's major central banks should arrest any significant risks as long as the global economy remains in decent shape, thereby setting the stage for another decent year for the Romanian real estate investment scene.

LAND MARKET



DEMAND

The land market is coming from what was arguably its best year in the post-crisis period and while it may be difficult to follow through on this, demand remains, overall, very strong. We are seeing healthy appetite across the board, maybe a touch dimmer for the residential sector.

The bulk of the demand is concentrated for plots inside the cities, ideally with a zoning permit in place; the latter aspect is mostly the case for residential, where the foggy outlook for the sector over the next couple of years means that buyers want to acquire a land plot on which development works may start shortly after. On the other hand, for office developers (especially in Bucharest, but also in other big cities which are attractive for such projects), adequate land plots are becoming much scarcer, thereby forcing companies to become more flexible in terms of requiring a zoning permit or having to settle for a smaller surface. This also means that companies look at locations that would not fall into the traditional office submarkets, rather places which at least offer good connectivity to the public infrastructure routes (mostly subway), as well as closeness to educational hubs. Otherwise, there are big developers which are looking at former industrial platforms allowing for large mixed-use projects which would set them apart from any competition.

Retail developers continue to be quite active, both in Bucharest and in other parts of the country. In the Capital, there is still some interest for FMCG, DIY or small proximity strip malls, though the market is quite mature and crowded, meaning that a project needs to position itself correctly in order to succeed.

In other parts of Romania, demand is still quite strong on all segments, mostly from residential and retail developers, while in big cities, we see new players that weren't active here previously.

The retail sector is spearheading demand, with a wide variety of market participants showing interest, from companies owning retail parks and DIY to standalone food retailers.

SUPPLY

Market supply is limited in some cities like Bucharest, Cluj-Napoca or Iasi (especially the central areas for the latter), which is helping sellers nudge prices up a bit in some cases; for instance, for plots that would be suitable for office projects and which have no outstanding legal issues. Owners are also trying to be proactive, with some actively seeking to obtain zoning permits in order to increase the value of the land in any future deal.

On the other hand, in a somewhat new addition to the supply side, some developers are selling some of their plots, due to the fact that they do not have the financial resources to develop everything at the same time; plus, the general rise in land prices in the last years makes it an appealing alternative.

As a relevant side note for the supply side, local authorities in Bucharest and in other cities are drawing up fresh general or zonal urban plans, which could help the market as they might allow for more flexibility on parameters, while also offering more clarity on the development potential.

PRICES AND TRANSACTIONS

Currently, there are several significant land deals stuck in various stages of negotiation and due-diligence, so the first half of the year was not particularly strong in terms of market turnover. Furthermore, some of the really big deals, both in Bucharest and elsewhere have become stuck in recent months either on account of actual outstanding issues related to property rights or to the urban development permits, either due to the buyers' reluctance to take on risk. This trend has been noticeable especially for office and residential developers, who display a much more risk adverse attitude than in past years.

Overall, supply and demand seem quite balanced, with isolated price hikes reserved for just the best of the best land plots in terms of location and which have zoning permits in place (especially for office and residential projects). Otherwise, for projects located at the outskirts, interest is smaller and prices actually come under downward pressures, while in Bucharest, for instance, this lower appetite is also significantly correlated to the lack of a metro station in the vicinity.

Usual land prices intervals for the major cities in Romania (EUR/sqm)

	Central	Semi-central	Periphery
Bucharest	800-3,000	200-1,000	80-400
Cluj-Napoca, Timisoara, Iasi, Brasov	500-1,000	150-500	70-250
200-300k inhabitants	200-800	100-300	50-200
100-200k inhabitants	150-500	100-200	50-150
50-100k inhabitants	150-300	100-200	30-100

FORECAST

We expect the second semester will turn out better than the first one, but we cannot speculate with regards to the big deals that have been consistently delayed. These will make the difference between a full year result that is comparable or not to last year's turnover of over EUR 400mn. While jitters regarding the residential market, where sales are set to decrease this year, as compared to last year's volume, or problems with zoning may push away some developers from purchasing new land plots, retail developers are pushing full steam ahead, as there are still significant parts of the country which are undersupplied and could accommodate at least a small retail park. For office, demand remains good in Bucharest and in main regional cities, but as we stated above, very good land plots are becoming increasingly short in supply and could force developers to become much more creative with regards to location.

Price intervals are indicative and are based on Colliers' transactions and/or market expertise. They highlight the most targeted type of land plots. As usual, the prices are influenced by size, destination, building parameters, status of the permitting process.

Source: Colliers International

554 offices in **68** countries on **6** continents

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Latin America: **24**
Asia Pacific: **231**
EMEA: **112**

$3.3
billion in annual revenue

2
billion square feet under management

+17,000
professionals and staff

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