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2020 / 2021

The CEE Industrial Scene

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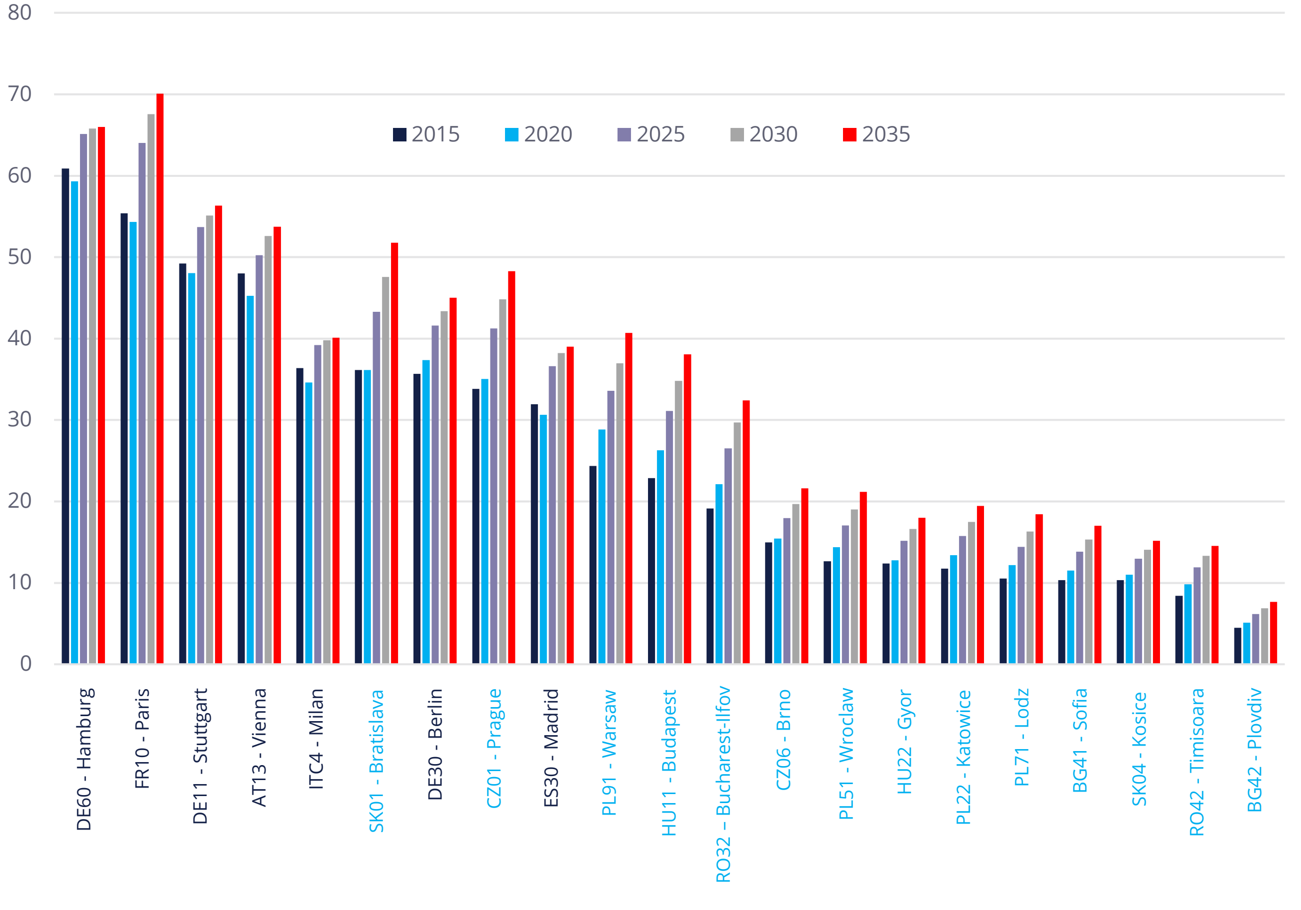
In this regional comparative report, we look at the CEE Industrial & Logistics markets to compare the key indicators from 2020, assess how they have been performing and furthermore, what trends we see are emerging as a result.

As the anniversaries of the first lockdowns and states of emergency roll over across the CEE, we take a look at the effect this has all had on the industrial and logistics markets in the region. The pandemic is still very much with us, albeit at different stages, depending on how individual countries have managed the spread and the impact on hospitals, plus, and equally important, how well they are managing the sourcing and rollout of vaccines. Achieving high levels of immunity through vaccination is of course key to enabling economies, and various industries, the chance to recover and adjust to post pandemic life.

Prior to the pandemic, the CEE region, much like other parts of Europe, had been enjoying a good run and stable levels of economic growth. Of course each country is different, in terms of maturity and the drivers that move their markets. There are also differences between regional markets within countries, for example proximity to major trading partners or networks, such as is the case for western Czech and Polish regions to Germany. These differences could also be transport infrastructure or labour and skills related drivers. All of these factors contribute towards making the CEE and all of its components a highly sought after destination and, something that we expect to continue for the foreseeable future.

Despite the pandemic causing widespread economic disruption, the majority of the selected CEE NUTS-2 regions in the chart are not forecast to show GDP per Capita declining in 2020 against the previous 5-year period. They are also expected to show quite strong levels of growth going forward as the region's economies gradually converge with select Western European markets.

GDP (Real) per Capita (€ Thousands) 2015 – 2035 (F) in Select European NUTS-2 Regions



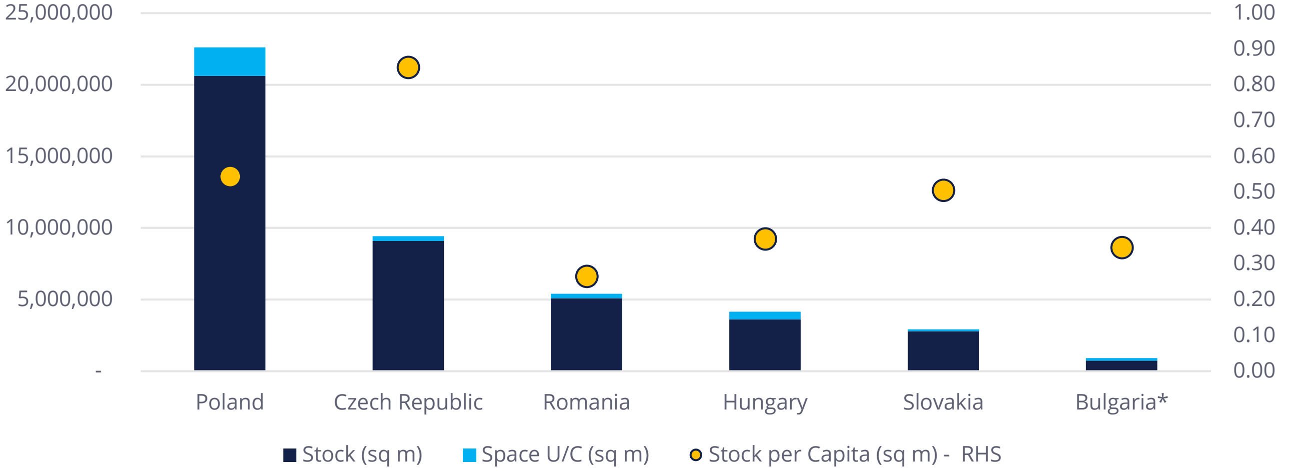
Source: Oxford Economics, March 2021

SUPPLY

All of the countries in the region have celebrated industrial histories and skillsets which have certainly been part of the driving forces behind the rise of property sector, alongside their proximity and lower labour costs compared to Western Europe. Unsurprisingly, Poland, as the largest country in the CEE-6 region covered in the report, both by Population and land mass, also has the largest modern industrial and logistics stock. At over 20 million sq m, it is only a fraction smaller than the other 5 markets combined. With a pipeline under construction of over 2 million sq m, this is unlikely to change in the short term. The Czech Republic, which is geographically located the furthest west, comes in second with almost 9.1 sq m and has the highest level of stock per capita in the region. Although industrial markets are quite challenging to compare, partly due to local market differences in definitions, the Czech density of 0.85 sq m is quite someway below the Netherlands, which is estimated at over 2 sq m per capita for example. Romania, as the second largest CEE country by population and area, is now seeing greater levels of development activity then ever before. Developers are looking to unlock the great potential the country has to offer, along with the regional markets within Hungary, Slovakia and Bulgaria. Outside of Poland, a further ca. 1.5 million sq m is currently under construction.

In terms of delivery costs, indicative prices for land across the region (assuming permits are in place) vary between EUR 10 and 80 per sq m. However, due to the scarcity of land in the most sought-after locations, particularly those closer to major cities or economic/productive hubs, prices can rise to between EUR 120 and 150 per sq m. Typical hard construction costs for a "standard" warehouse across the region range between EUR 370 and 600 per sq m. Higher costs have been reported in some markets but, overall, a combination of increased labour and materials costs have driven up construction costs by as much as 25% or more over the past few years.

CEE MODERN I&L STOCK & STOCK PER CAPITA BY COUNTRY* & PIPELINE U/C (SQ M) 2020

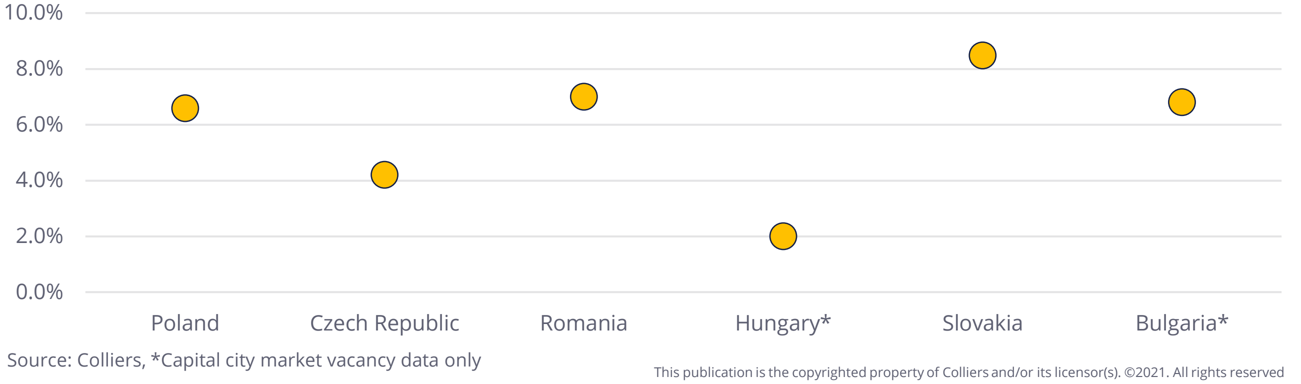


Source: Colliers, *Data for Sofia only

VACANCY

Availability of space in the CEE region as a whole averages at ca. 5.9% so, the markets are landlord favourable in most cases. Some developers are willing to build speculatively while others are under less pressure to do so and prefer the 'build-to-suit' route. Availability in some locations within countries are very tight, particularly in the most sought after locations so, potential occupiers looking to enter the region or expand should ideally start the search process early, to avoid disruption or delays to their plans. This is particularly the case in some markets for larger space requirements of 10,000 sqm and above. The limited availability in some markets is also impacted by the lack of available or suitably priced, zoned land. Additionally, many of the most sought after locations have higher levels of competition for labour so, our strategic site selection service is increasingly receiving more requests to provide support in these crucial decisions.

CEE I&L VACANCY 2020



Source: Colliers, *Capital city market vacancy data only

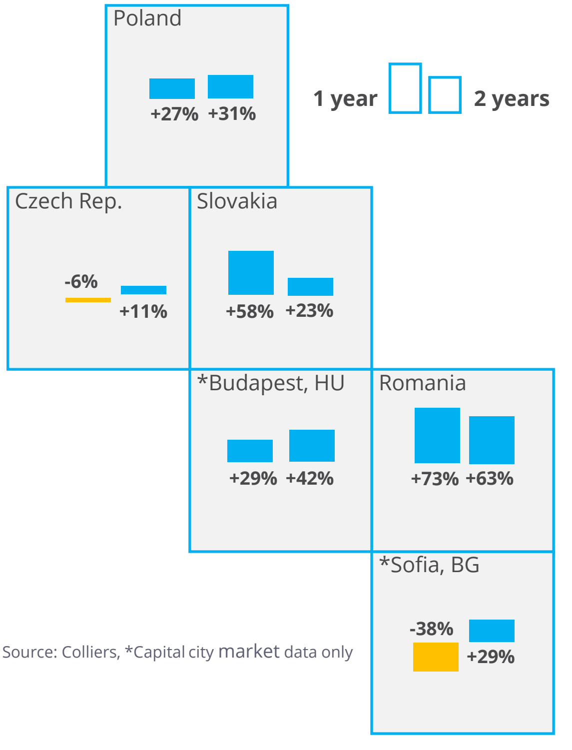
DEMAND

2020 was a undoubtedly a positive year overall for the industrial and logistics property sector. However, it was not without it's fair share of challenges. Afterall, the occupiers within this sector cover a huge range of industries, some of which were, and still are, quite heavily impacted by the pandemic, both positively and negatively. Despite the disruption, it is quite remarkable how so many companies have been able to adapt or ramp-up their operations so rapidly to meet the new sets of demands.

Looking at gross demand for industrial and logistics space over 2020, we have recorded very strong activity, with the region recording ca. 9 million sq m, a YoY growth of almost 25% on average. The Czech Republic and Sofia, both recorded declines in demand, but to be fair, these were off the back of very strong take-up in 2019. Inline with 2019 trends, the Bucharest and Bratislava markets attracted the majority of demand in their markets with 70% and 73% respectively. On the other hand, the Czech and Polish markets both saw greater levels of activity in their regional markets, with 67% and 78% respectively.

Net take-up across the region (excluding Romania) accounted for approximately 68%. The Czech Republic and Budapest markets both recorded above average renegotiations, which can in part be attributable to lower levels of availability in these markets.

GROSS TAKE-UP CHANGE YOY (2020 vs. 2019 & 2018)



Source: Colliers, *Capital city market data only

SECTORS

In terms of demand by sector, a few minor differences in definitions exist between the local markets. There are also a significant portion of deals that are marked as confidential so, it is not always possible to know the company or sector until that information becomes public sometime later. As we have said previously, the CEE region is a popular near-shoring destination, thanks to its geographical position, overall cost differential and skills of the labour force. As a result, companies relocate from other parts of Europe for example, which is sensitive for some period of time for those involved, as this often means closures and/or job losses in the source market. Another challenge is where you have large international companies that are involved in numerous industry sectors such as home appliances, medical equipment, control systems and automotive components for example so, not easy to know precisely what the space is being used for. However, thanks to the various research forums across the region, we are still able to collect high quality data and insights.

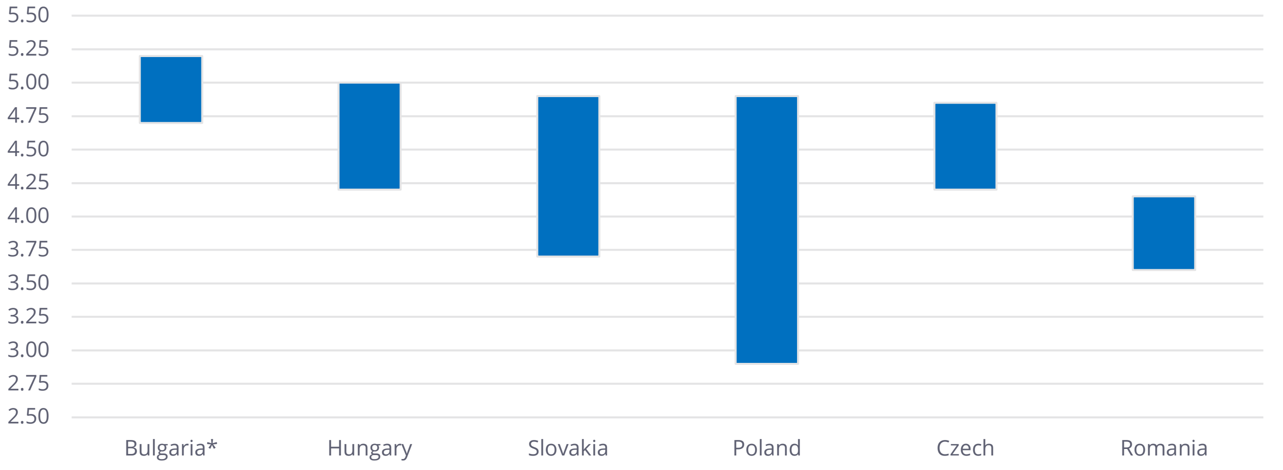
In 2020, the highest levels of activity were recorded by companies from the 3PL sector (ca. 28%), followed by the Retail (17%) and E-commerce (12%) sectors. According to the available detail, 3PL and Retail have quite similar shares when compared to 2019 but perhaps not surprising, E-commerce is up by 200% YoY on gross activity. We do however expect that some of the retail activity could technically be attributable to E-commerce as retailers adapted their operations to a higher proportion of online sales, due to the disruption to their brick-and-mortar operations. 9 out the top 10 deals across the region in 2020 have come from the Retail and E-commerce sectors.

Through the pandemic, we have recorded more demand for short-term leases to cope with additional demand however, typical lease lengths across the region range between 3 and 5 years for logistics and over 5 years for production. Logistics companies for example often have 3-year contracts with their clients so would prefer more flexibility however, we have also seen the end user taking longer term leases and having the logistics companies rotate instead. Build-to-suit facilities can be expected to command longer leases, often due to the additional investment put in by both developers and tenants.

RENTS

The behaviour of rents for industrial and logistics properties do vary from market to market, depending on various factors such as location or region, competition and availability, to name a few. Overall, we could say that rents have remained largely stable across the region, with some markets recording increases in the most sought-after locations. Prime headline rents across the region range from as low as EUR 2.9 per sq m / month in Poland and above €5.0 per sq m / month in Bulgaria. The level of achievable rent also depends on who the tenant is and under what terms are agreed in the lease. Construction costs also play their role as they have been on the rise over the past few years.

PRIME HEADLINE I&L RENTAL RANGES (€ / SQ M / MONTH) – Q4 2020



Source: Colliers, *Data for Sofia only

INCENTIVES

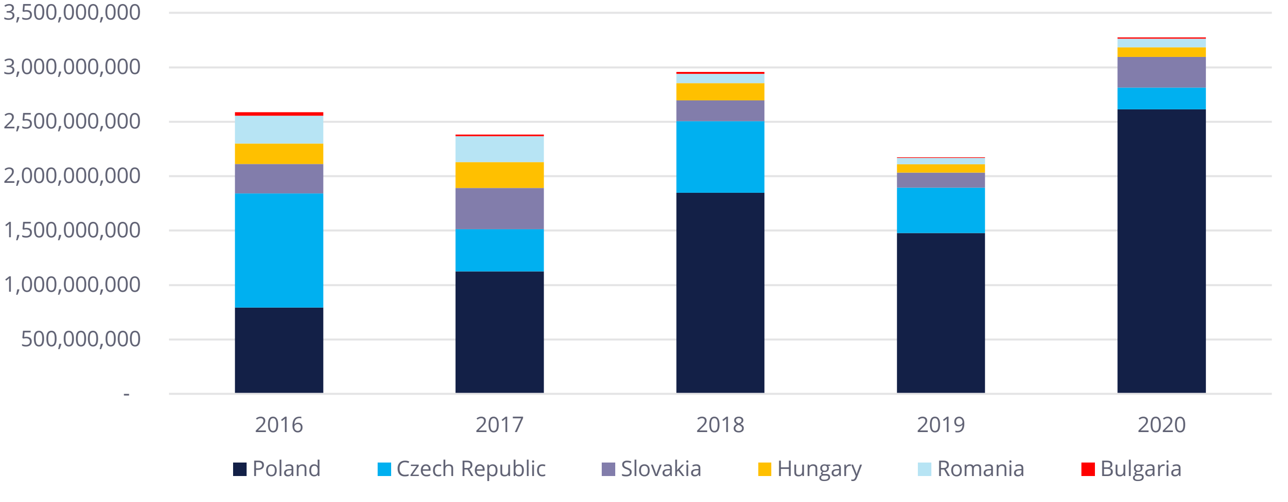
The level of incentives provided are of course individually determined by several factors including availability in the location, length of lease, additional standards required and tenant covenant, amongst others. Many developers have long term relationships with many of their clients across multiple markets, so this is also taken into consideration. It also works well for the tenant as they understand the property standards and services being delivered. Broadly speaking, the level of incentives can typically range between 1 and 2 months of rent free per year of contracted lease (ca. 8-16%). Depending on the availability or completion of the property, some landlords in Romania for example are allowing 1 to 2 months early access to the property. In Poland, subject to certain conditions, incentives of 20%+ of the contract value can be applied.

INVESTMENT

The pandemic had quite an impact on CEE investment activity in 2020, with total volumes ending up 24% below those of 2019. As was the case for many markets across Europe, international investors were disrupted from being able to travel and physically inspect properties. This however did not stop those targeting industrial and logistics assets, as 2020 was a record year for volumes, with ca. EUR 3.3 Billion transacted and a 32% share of total annual volumes.

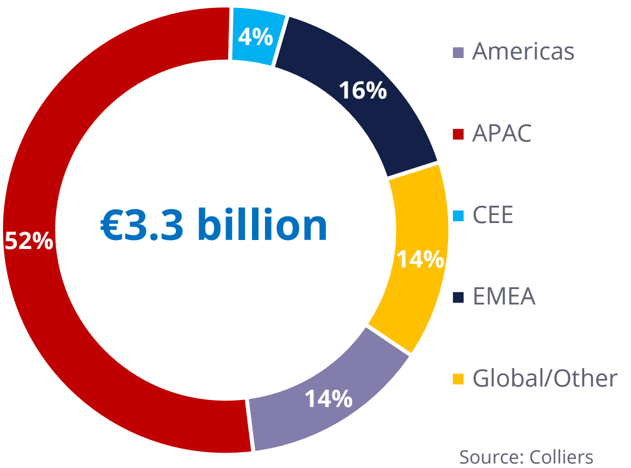
As one of the best performing property sectors throughout the pandemic, the industrial and logistics sector has certainly caught the attention of most investors. According to the recently launched Colliers Global Investor Survey, industrial and logistics, is now the second most sought-after asset type, marginally behind offices. In addition to regular transactional activity, there has also been increased activity in the sale and leaseback arena, as some owner occupiers look to free-up capital to invest in their core business. It all sounds good, however, the majority of the industrial and logistics product in CEE is tied up with long term players who are not likely to sell anytime soon.

CEE I&L INVESTMENT VOLUMES (€) 2016 - 2020



Source: Colliers

SHARE BY BUYER SOURCE OF CAPITAL 2020



Source: Colliers

The majority of investors looking at industrial and logistics investment product also prefer to acquire portfolios, platforms or opportunities with scalability. The ca. EUR 3.3 billion volume in 2020 consisted of approximately 45 transactions, giving an average deal size of over EUR 70 million. Among these transactions, were some very notable portfolio deals, the largest of which was GLP acquiring the Goodman assets in CEE for ca. EUR 1 billion. Also selling to Asian capital, Panattoni disposed of numerous assets, some of which were acquired by Savills Investment Management on behalf of undisclosed South Korean capital.

Capital from the APAC region, specifically from Singapore, China and South Korea, secured a dominating 52% share of volumes. This was followed some way behind by EMEA and US capital with 16% and 14% respectively.

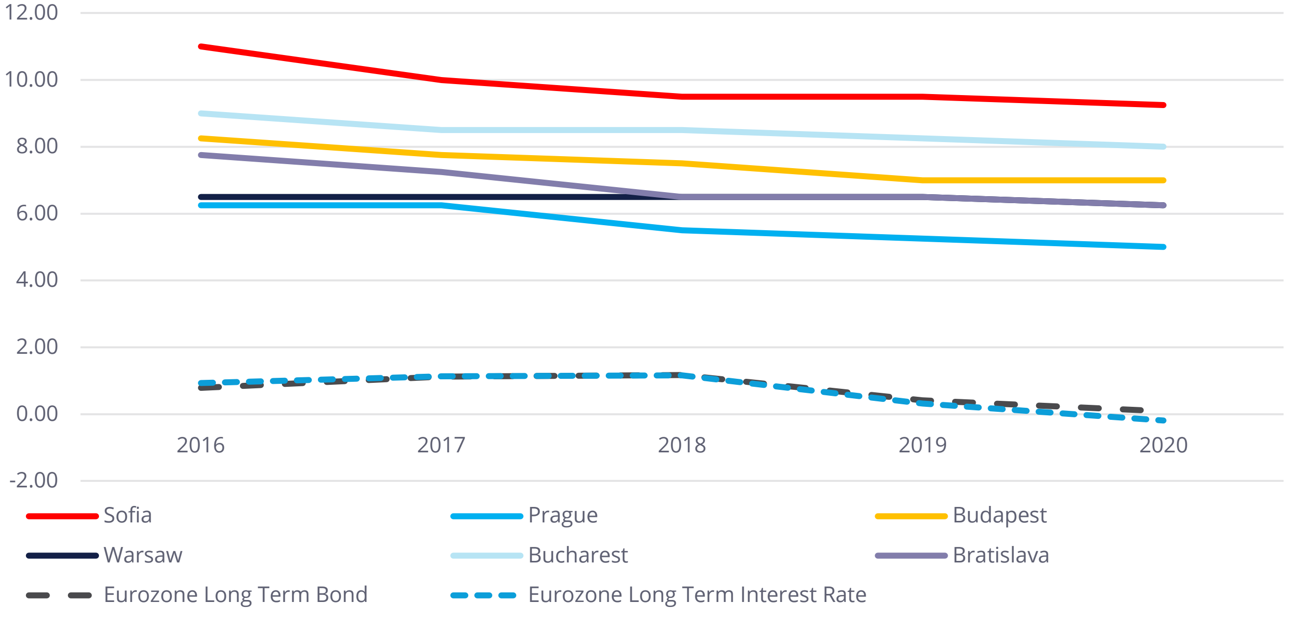
YIELDS

Since the outset of the pandemic in early 2020, it has been challenging to report prime yield movements across most property sectors, especially those where there has been a lack of transactional evidence to support it. For most sectors we have reported outward movements of 25 and 50 bps for office and retail assets respectively, with potentially further movements to be considered, should the pandemic cause longer term disruption.

For prime industrial and logistics yields, we have recorded a stable trend in some markets, again partly due to lack of evidence, while others have recorded compression. Further inward movement can be expected, particular as the product type is highly sought after and the bulk of product remains firmly in the hands of long-term holders.

2021 will see the closure of a few additional portfolio transactions so, we may well get to see more prime industrial and logistics yields push past prime shopping centre yields, as they have done so already in the Czech Republic. When benchmarked against other investment vehicles, such as 10-year Euro bonds and Eurozone long term interest rates, CEE real estate still maintains a significant spread and a compelling investment case.

CEE PRIME I&L YIELDS (%) 2016 - 2020



Source: Colliers, Oxford Economics

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