

P R E S S R E L E A S E

CURRENCY FLUCTUATIONS IMPACTING CEE PROPERTY MARKET

Property occupiers most affected in the short term

Prague, 14 April 2009 – Falling currencies in Central & Eastern Europe (CEE) are impacting property investors, developers and occupiers across the region, with some countries more affected than others, according to CB Richard Ellis' forthcoming publication, *CEE Currency Fluctuations ViewPoint*.

The key impacts of currency fluctuations on the CEE property market can be explained as follows:

- Local currencies in CEE have fallen in value over the last nine months.
- Many CEE businesses and consumers took out loans or issued bonds in foreign currencies in recent years, when their currencies were much stronger.
- Most countries in the CEE region are not part of the Eurozone. Recent devaluations are therefore having a material impact, particularly combined with the wider economic slowdown.
- Homeowners face the prospects of falling house prices and rising mortgage costs on mortgages taken in FX-denominated currencies (in local currency terms). This has the potential to sharply reduce their disposable income.
- In the CEE commercial property markets, it is property occupiers who are most affected in the short term. Whilst their earnings will generally be in local currency, rents will typically be denominated in euros. A fall in the local currency therefore represents an equivalent increase in rent.
- Over time, this will feed through into market rents, and thus investors are only partially shielded from the effects of currency changes.

Jos Tromp, Head of CEE Research, CBRE, explained: "The impacts of currency fluctuations on the CEE property market are not uniform across the region - different countries and players are being affected more than others."

In many ways, the impact of recent currency fluctuations on the property market depends not only on the country concerned, but on two other key factors: (1) whether an actor is based locally or outside the country concerned; and (2) what an actor's involvement in the market is, as the impacts will be different for occupiers, developers and investors.

Tromp continued: "For businesses that operate internationally, currency risk is a fact of life and a well-understood cost of doing business. To a large extent, real estate is no different in this respect. Nevertheless, the globalisation of the financial markets and the ability of citizens of the emerging CEE economies to take out euro or Swiss Franc denominated mortgages does pose some particular challenges to these economies and their property markets. The fact that rents are denominated in euros offers investors some protection against income devaluation, but this is only temporary and in some cases will prove illusory. In essence, investors have two options: mitigate the currency risk, or accept the consequences and deal with them as best they can."

In the current climate, it is evident that the principal risk to investors lies in the medium-term threat posed to their income. Pavel Schanka, Director CEE Capital Markets, commented: "The view that investors have no currency risk where the rental income is denominated in euros is highly misleading. If the weaker currency causes tenant default due to an increased rent burden, the risk to the investor is very real. The key for investors is flexibility – to understand the position of the tenant and adapt to find the best medium-term outcome." What may look like a difficult decision from a short-term perspective can result in positive outcomes longer term. For example, agreeing to a rent reduction allied to a lease extension with a good quality tenant can actually enhance the value of the asset (through the longer term and by reducing the risk of over-renting), even at the expense of short-term income.

"Clearly, finding a sustainable longer-term solution may have implications for any loan secured on the property – but it is equally important to consider the alternative. Insistence on adherence to an unchanged rent payable in 'hard currency' may risk the failure of the tenant's business, which is not in the interests of the investor or the bank that granted the loan, particularly as re-letting prospects are currently diminishing," concluded Schanka. It is impossible to be definitive – but in markets with significant currency fluctuations, flexibility in dealing with tenants is an essential long-term strategy.