



Arbitrage
Real Estate Advisors

REAL ESTATE MARKET OUTLOOK

Greece and Athens Snapshot

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GREEK REAL ESTATE MARKET OUTLOOK

In ULI and PwC 2018 Emerging Trends in Real Estate Europe survey report, Athens was ranked 19th among 31 major European cities on its expected growth prospects in rents and capital values. The ranking was based on more than 800 responses from the most influential leaders in the global and European real estate industry.

The report also states that interest in Athens is quietly picking up and several international investors committed capital in 2017 and put boots on the ground. The sector is attracting most interest in hospitality, which is not so linked to the local economy. International arrivals have gone up in each of the last three years, and the country is viewed as a safe European holiday destination. Prominent Athens hotels have traded at less than replacement cost this year. In the vanguard are US investors and private equity firms, often operating with local partners. Chinese capital is going into logistics at Piraeus Port and in residential assets, shopping centres are beginning to attract opportunity funds. Like hotels, retail including food and beverage gets a boost from tourism. Prime office yields have started to move in slowly off the bottom and Athens is one of the few cities left in Europe where there are opportunities for yield compression. As one experienced pan-European player now operating there says: “Investing in Greece doesn’t feel so crazy.”

Yet there is a lack of good stock of all asset types, it is too early in the recovery to develop opportunistically. Non-performing loans remain a huge headache for Greece with €101 billion clogging the books of its banks: an estimated 60-70 percent is either commercial real estate loans or collateralised by real estate. The Greek banking system has set an ambitious target of reducing it by €40 billion by the end of 2018, which will test investors’ appetite. And the country is still under the institutions supervision.

According to our analysis, since 2008, economic uncertainty, political instability and more recently the immigration crisis seem to have been the main determinants hampering international investors from looking at allocating capital in the local real estate market apart from the hospitality market, driven by the growth in the tourism market. As a result, the real estate market in 2016 was standing at its lowest point, almost 50% of where it was almost a decade ago. In 2017, the commercial real estate market experienced the first solid signs of an upward recovery trend in letting activity and investment demand, predominantly for prime space and locations. This came as a result of political stability and the first signs of noticeable economic growth.

We believe that growth will continue in 2018 as the outlook is looking better according to forecasts by the European Commission. Especially, if the country manages to negotiate with its creditors an unwavering exit from its current economic adjustment programme at the end of Q3 2018. Indeed, 2018 will be a crucial year for the continuation of the real estate market recovery.

If we are to take a deeper look into the local market, what has really changed during the last 12 months? What kind of investment interest was witnessed, and which asset classes were favored?

What do the macros say?

- Unemployment has started to show some notable shrinking signs; the rate was 20.7% at the end of Q3 2017.
- Latest Harmonized Consumer Price Index at 0.7%.
- Q3 2017 GDP has risen y-o-y 1.3%.
- Gross public debt remains high and totaled 177.4 % of GDP in the third quarter of 2017.
- Greece's general government deficit is projected to stand at 1.2% of GDP in 2017.
- The Commission is forecasting that Greece will have a primary surplus of 2% in 2017. According also to the Commission, the surplus is likely to rise to 3.9% of GDP in 2018, beating a target of 3.5%.

What is the domestic market indicating us?

In the **residential market**, downward pressures on residential property values soften in 2017 compared to 2016 showing a stabilization trend. Market demand remained limited for a ninth consecutive year, essentially as a consequence of the economic situation, the prolonged high unemployment rate, the squeeze in household incomes, the imposed property ownership taxation and the absence of a healthy mortgage market. More specifically, house prices have dropped more than 40% between 2008 and 2017.

In general, the housing market is characterized by excess supply, a limited number of transactions and a downward trend in valuations and pricing, albeit at a more moderate pace since historical low rates in 2012 and 2013. Following our analysis, the highest price drops were related to aged properties (built more than 30 years ago) in Athens and Thessaloniki metropolitan areas,

Despite the remaining macroeconomic difficulties, there were certain residential market segments that are showing some very positive signs, especially in the holiday property market and in high-end properties market. These segments were driven mainly by foreigner investors and individual buyers, especially after the recent introduction of the favourable residence permit scheme for non-EU citizens. More specifically, Greece's visa-for-investment program offers non-EU nationals a five-year residency permit when they invest capital in acquiring real estate in excess of €250,000. This has drawn the interest from investors coming mainly from the eastern Mediterranean region, Turkey, Russia, and China. Residency permits are also granted to the investor's immediate family and can be renewed.

In addition, there was also an activity hike in the historical city center of Athens. This was driven by the short-term rental market through the use of electronic platforms, such as Airbnb. In general, holiday property transactions went up in popular tourist destinations such as Mykonos and Santorini. The demand originated from individuals mainly coming from countries in the Middle East, Northern Europe and Russia. This trend was partially reflected by Bank of Greece's Short-Term Indices, such as the rate of net inflow of capital coming from abroad used for real estate acquisitions in Greece. This returned to positive grounds in 2016, recording an increase of 45% (€ 270 million) compared to 2015 (€ 186 million). In Q3 2017, the same rate increased by almost 77% compared to 2016.

In the **retail market**, during the last 12-18 months and up to the 2nd semester of 2017, the main domestic retail markets continued to be influenced by the economic uncertainty and the lack of consumer's liquidity. This was more evident in secondary markets and locations, in which capital controls had hampered the smooth operation of small domestic players, particularly in their dealings with certain foreign suppliers. The inadequate economic recovery combined with the additional tax obligations and insurance contributions opposed, in an already burdened tax environment, have also further deteriorated the purchasing power and thus household consumption.

However, in 2017 the market witnessed the first solid signs of an upward recovery trend in letting activity and investment demand, predominantly for prime retail space, which it seems it will continue in 2018. At the same time, the growth in commercial transactions via internet (e-commerce), combined with the promotion of retail products via social media, continued to bring about alterations in consuming behavior and is gradually leading to the transformation of the supply chain. This has intensified the reduced demand for large-scale retail spaces. It will also augment the need of businesses currently operating only physical stores to switch to e-commerce (bricks vs clicks) and therefore invest or let space in small logistic inner-city hubs.

Furthermore, the continuous need for improved operating costs is expected to lead to further demand for commercial premises of contemporary specifications and standards. Concurrently, there is an onward tendency from international retail chains to enhance their corporate social profile by adopting environmentally friendly specifications within their retail units. This shift, combined with the offer of additional services by new technologies and the internet, will create a demand for retail spaces into more organized, higher standards properties.

We believe that the aforementioned trends in conjunction with the recovery of economic expectations are expected to determine the evolution of retail property space and shopping centers market in the near future.

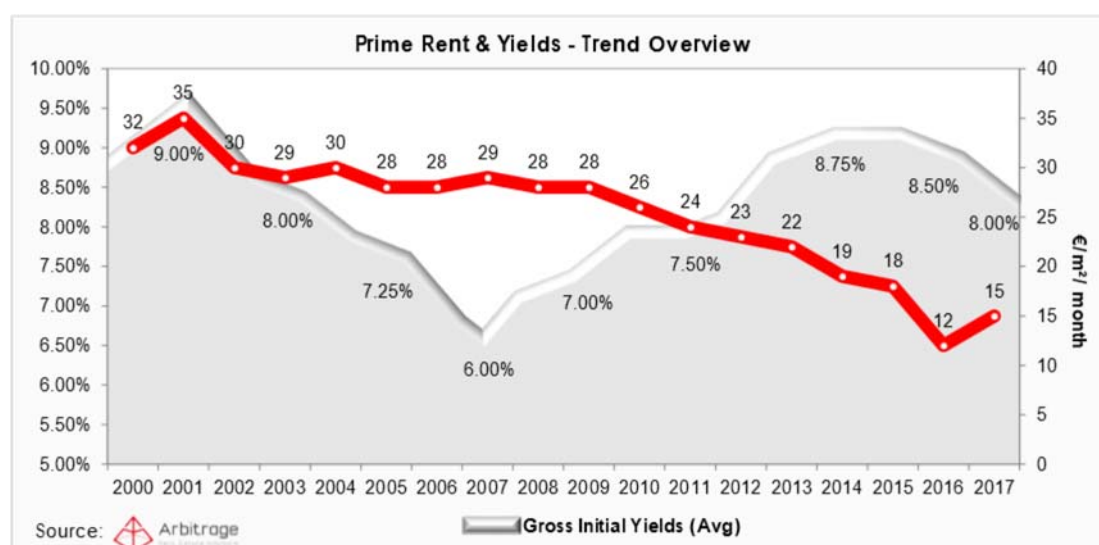
In the Athens market, the traditional high street destinations have rebounded, with vacancy rates recorded below 5% in the main commercial roads of central Athens and of the affluent suburbs. The corrected rental values of previous years combined with the departure of key retailers have led to new retail chains entering the market. Ermou street in the Athens centre keeps the lead with average annual rental values reaching €10.000/m² for high street brands. Shopping malls continue to resist recession, with vacancy rates in traditional malls below 4% and rental values stable. Two new regional malls have come to the market that accounted for 7% of the overall stock, which proves there is further room for expansion, given also the lack of quality stock, Gross initial yields are currently between c. 8% and 9%. In addition, increased activity had been recorded in the big box retail sector, where apart from the entry of new DIY brands, traditional players were active further expanding within urban areas, in contrast to their past regional priority. This was a consequence of lower rental values and repositioning opportunities in existing retail facilities.

In the **office market**, letting activity has been focusing on lease renegotiations, occupied space consolidation and relocation to office spaces near metro stations, urban rail transit or major roads. In prime offices, a relative small part of the market, there was an upward trend in demand due to targeted requests and limited supply. In general, average quality and

specifications (i.e. Grade B and C) offices in secondary locations have experienced additional rent pressures because of tenant lease renegotiations. On the other hand, prime located offices of good quality and high specifications (i.e. Grade A) have started going up in rental values and yields started to get compressed. Consequently, in conjunction with the stabilization of the economic environment, local and listed investor's interest, prime office market has witnessed an upward trend during 2017, a trend expected to continue in 2018

In the Athens office market, the demand for office space is centered on newly constructed buildings of high specification standards, with a total area of up to 3,000 m² and an average area per floor ranging from 300 m² to 500 m². The Central Business District (CBD), Northern Kifissias Avenue (Northern Suburbs) and Lower Syngrou Avenue (Southern Suburbs) areas have been Athens's districts attracting the most interest from corporate tenants seeking for prime office space. During the second half of 2017, rents in Grade A offices ranged between € 12 to € 17/m²/month, whereas for Grade B and C offices rental prices were significantly lower between €5 to €9 /m²/month. In retrospect, office rents have declined almost 50% since the pre-economic crisis period (prior 2009).

Gross initial yields for offices in prime locations ranged between 7.5% and 8.5%. Corresponding yields 8 years ago ranged between 6.5% and 7.0%, with a record low between 5.5% and 6.0% during 2006-2007.



The **industrial and logistics sector**, despite the lack of substantial new infrastructure investment, remains one of the core pillars of economic development, contributing approximately 10.8% to Greek GDP each year. In 2018, the logistic industry is also anticipated to benefit from the expected recovery and the consecutive growth in retail trade.

Additional benefits for the logistics sector are expected to come from the new infrastructure investment in the Piraeus Port by COSCO, the new major shareholder and manager of the port. The on-going investment combined with the port's railway connection with the Thriaseio Freight Center is expected to decrease significantly the delivery time of freights from Asia and Eastern Mediterranean to main Europe. In addition, the assignment of Thriaseio Freight Center management to the ETVA – Goldair Handling consortium is expected to upgrade further the

logistics and distribution capabilities of the center, under an € 180M investment program in the next 10 years.

Furthermore, due also to the country's geographic location, the sector is expected to benefit by increases in freight flows from Asian Markets seeking safe gateways for their products to the European market. Furthermore, the continuous business growth of e-commerce will continue to impact in a positive way the inner-city logistics warehouses and those in close vicinity to main highways and transport hubs.

Rental values for good quality logistic space have been stabilizing the last two years, varying between €2/m² and €4.5/m²/month. Vacancy rates remain low (below 5%) for quality space in prime industrial locations. Therefore, the expected increase in demand will eventually lead to increasing rental values and investment yields are anticipated to further shrink. However, this increasing demand has not yet fully materialized into transactions because of the limited quality product in the market. Currently, gross Yields for Grade A industrial buildings range between 9%-10.5%, whereas for Grade B & C industrial buildings between 10.5% and 13%.

In the **hospitality property sector**, the country's ranking as one of the top touristic destinations worldwide has helped the sector to steadily strengthen its fundamentals due also to increasing international arrivals and the characterization of Greece as a safe holiday destination in the wider region. This was coupled with the encouraging returns of international tour operators, the arrival of new global hotel brand managers and the promotion of Athens and Thessaloniki as city break destinations. We believe these fundamentals will continue to have a positive impact on the investment flows and commercial activity in the hospitality real estate and related leisure sector.

Based also on data and forecasts from the World Travel & Tourism Council (WTC), the long-term effect of tourism in the Greek economy is mainly linked with indirect contributions. It is estimated that indirect contributions to the country's GDP exceeded € 18 billion in 2017, surpassing direct contributions which amounted to over €13 billion. According to WTC, the tourism contribution to the Greek GDP during the current year is expected to reach € 32 billion, amounting to 22.5% of the GDP. According to WTC, there will be a long-term increase in capital investments in tourism as well as in businesses operating in the related food & beverage, transportation and logistics sectors. It is anticipated that capital investments will increase annually by 4% on average until 2026. The analysis also shows that a major factor affecting the hotel market relates to revenues from international visitors. This market indicator has seen an increase in recent years and according to long term forecasts its upward trend is expected to continue in the coming years and exceed € 23 billion by 2026.

Nonetheless, a series of challenges remain ahead. As an example, the persistent weak domestic economic environment has led to, among other things, underinvestment in the needed improvement of major transportation infrastructure and unpredictability in the hospitality business tax regime. At the same time, a potential resurgence of the refugee crisis and any fresh economic uncertainty in key international tourists' origin markets might also affect the sector.

The investment activity in 2017 has mainly concentrated in the acquisition, renovation and upscaling of existing hospitality properties and in the operational repositioning of obsolete and aged commercial buildings into city hotels, demonstrated a trend for luxury and higher standards hotels of, mainly in the 5* category.

More specifically, two major transactions were recorded in 2017, reaching an investment value of € 80M and comprising of c. 425 rooms in total. Athens Ledra Hotel (ex Ledra Marriott) in Athens center was acquired by Hines along with Henderson Park (for €106,000 per room), to be operated under Hyatt brand. In addition, King George Hotel (103 rooms capacity) in Syntagma Sq., was acquired by LAMPSA S.A (owners of Grande Bretagne) for €421,500 per room and will continue its operation under the brand of Starwood – A Luxury Collection.

Moreover, a new trend is the development of small high-tech boutique units in the Athens CBD and the redevelopment of commercial buildings to serviced apartments and boutique hostels. More specifically, LAMPSA S.A has recently leased, on a long-term basis, a commercial building of approx. 13,000m², located near Grande Bretagne & King George that will be redeveloped to 4* hotel, under global hotel brand. Furthermore, ex La Mirage Hotel (208 rooms capacity) located in Omonoia Sq, has been long term leased by a local hotelier and it will be renovated and operated as budget hotel.

Regarding hospitality sector in the Greek Islands, Tour Operators are currently controlling more than 16,000 rooms. In terms of recent transactions, TUI has acquired a plot of land in southern Crete in order to develop and operate from 2019 an additional (already operates three units in Greece) Robinson Club. On the other hand, Thomas Cook will launch its 3rd Casa Cook (boutique lifestyle brand) in Greece, in Crete island, whereas Alltours proceeded in the acquisition of two (2) resort hotels of 220 keys & 273 keys respectively.

LOOKING AT THE YEAR AHEAD

Which are the key determinants for the year ahead?

- Timely completions of the third and fourth fiscal adjustment programme evaluation in Q1 and Q2 2018 respectively would give the right to the country to receive the next loan tranches to cover the government's outstanding debt of the state to the private sector, which would give a much-needed liquidity boost to the economy.
- The successful completion of the programme evaluations will include how the government will establish and expand electronic auctions of properties, seized to pay off debt to the state, insurance funds and banks. This will be overwhelmingly important not only for the survival of Greek banks but also for the expansion of the transactional and investment activity in the commercial real estate market.
- The successful completion of the evaluations is also a precondition for Greece to exit the current bailout programme, which ends in Aug. 20, and turn the corner like Ireland, Portugal and Cyprus did. This will boost business confidence and attract further investment in the Greek market including commercial and residential real estate. The exit could be followed by a credit line arrangement with close oversight by the institutions to help the country access the Europe Central Bank's quantitative easing (QE) program and boost investor confidence; especially if the eurozone fails to deliver substantial and credible debt relief.
- Greece continues successfully with its fiscal consolidation and structural reforms in the next 6 to 8 months and it creates space for the European Commission and the Eurogroup to discuss and strike a deal on the conditions for any further debt relief and the post-program life for Greece deal in an adequate manner to averse any risk of a sovereign default
- The active management and successful sale of a series of non-performing loan (NPL) portfolios of the 4 systemic banks could lead to an indirect disposal of a large number of commercial and residential real estate assets to experienced investors that tend to follow a more hands-on approach and also consequently to capital investment upgrades in repossessed aged building stock.
- Politically difficult privatizations of strategic asset continue to gather pace after years of persistent delays to boost growth, gain the trust of investors and reboot the corporate economy Completions privatizations including TRAINOSE (railways), OLTH (Thessaloniki Port) and AIA (Athens airport), 17% of Public Power Corp., 65% of state-controlled natural gas supplier and 35.5% of Hellenic Petroleum SA
- Greek authorities complete in Q1 2018 the preconditions needed for the start of the Hellinikon project. Kick-off of the development of the former Hellinikon airport will turn the area into a world class metropolitan park with mixed use facilities, covering 2 million m² in total. An investment budget of more than € 4,5 billion is expected for the next 10 years.

- Planned public and private investment co-funded by EU funds and major international development bank (EIB, EBRD) in large scale urban regeneration programs could reshape derelict areas, develop new city hubs and result in capital appreciation in neighbouring building stock.