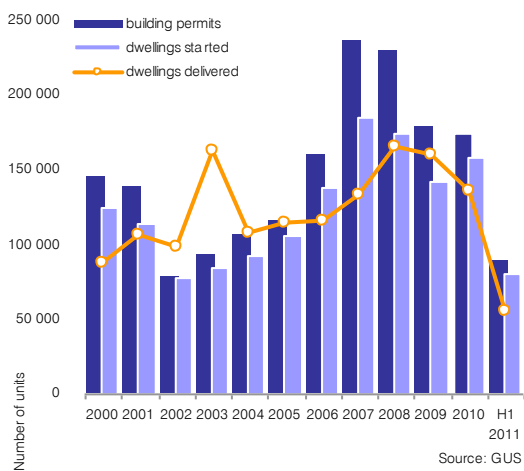


Despite a surplus of supply over demand developers continue to launch many new projects. With stable sales and growing offer the market is becoming increasingly competitive.



Statistics of residential construction in Poland



## Q2 2011: Record-breaking offer, sales stabilization

The second quarter of the year is usually a time when the number of new projects started reaches its peak. On the one hand, this is typically reflected in the statistics of construction starts and on the other – in the number of residential units launched for sale. Traditionally, spring is also a time of significant sales increase. Did the market behave according to these expectations in Q2 2011?

Results of the market monitoring study conducted by REAS at the end of Q2 2011 indicate that the residential sales offer available in the six largest markets in Poland (Warsaw, Krakow, Wrocław, Tri-City, Poznań and Łódź) has increased for the seventh successive quarter and was higher by 29% than the 12 months earlier.

One reason for this situation is the fact that the number of units launched for sale remained high. Moreover, the sales result was slightly lower than in Q1 2011 and at the same time much lower from the number of dwellings introduced to the market. Additionally, even though the developers usually expect better commercialization in this period, the spring quarter of the year brought about a drop in sales, following three successive quarters of increased sales.

Analysis of the previous four years indicated, however, that the sales noted in the primary residential market is characterized by an upward trend. During the previous 4 quarters, a total of ca. 29,900 residential units were sold in the analyzed markets, i.e. 8% more than in the year 2010 and over 17% more than in the year 2008.

Although the market environment did not experience any dramatic disturbances, increased inflation brought about a rise of the NBP rates and interest rates on loans. The growth of salaries in real terms ceased. Media reports insist that “the prices must drop”. Yet, economic growth remains on a stable, advantageous level, the unemployment rate decreased slightly, and both domestic and international financial institutions predict that in the current year the Polish GDP growth should amount to ca. 4%. However, Europe is concerned about the situation in Greece, Portugal and Italy, and the potential destabilization of the European currency will result in an even stronger destabilization of the Polish zloty.

If the projection of the GDP growth in the years 2012-2013, presented in July by the NBP, proves correct, the domestic demand dynamics will experience a significant drop to the level of less than 3% (year on year), while the high risk of inflation growth may cause further increase of interest rates.

What is more, the country is preparing for the election campaign. This is probably the reason why the two largest parties submitted bills regarding developer activity in residential construction. If passed, such a bill would make it more difficult for new players to enter the market while favoring large developer companies. Still, considering the tight schedule of the parliamentary works, passing such a bill in this term does not seem highly probable.

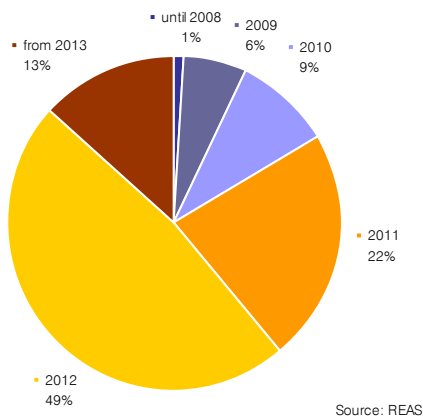
## Supply

According to the results of the REAS monitoring study conducted in Q2 2011, the number of dwellings launched for sale in six agglomerations amounted to over 10,600, i.e. was higher by over 20% than in Q2 2010 and lower by 1% than in Q1 2011. The number of units introduced to the market during the previous four months exceeded 37,000, which was a result higher by close to 5,000 from the number of units launched for sale in the four quarters of the year 2008. In H1 2011, a total of over 21,300 dwellings were launched for sale. Only in the first half of the record-breaking year 2007 was this result higher.

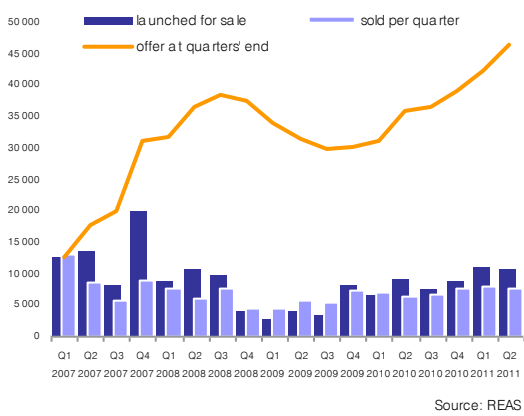
In this context, data published by the Central Statistical Office on the number of dwellings started in H1 2011 seem puzzling. While in Q1 we observed a significant, 14.5% increase as compared with 2010 results, the total number of units started in H1 was lower by 9.3% than in analogous period of the previous year and amounted to 28,529. Since the number of units launched for sale in the major Polish markets is currently growing, either part of these dwellings are launched for sale after building permits are obtained but before the formal construction launch – or we are witnessing a repeated concentration of developers' construction in the largest agglomerations, accompanied by decreased activity in smaller markets.

Despite rather advantageous and stable sales, the offer volume calculated for the six agglomerations exceeded 46,000 units at the end of Q2 2011 and reached the highest value in the history of the Polish developers' market. The offer is dominated by units under construction,

Structure of the market offer according to the projects' delivery date declared by the developer (aggregated data for the markets in Warsaw, Krakow, Wrocław, Tri-City, Poznań and Łódź).



Residential units launched for sale and sold quarterly vs. the volume of the offer at quarters' end (aggregated data for the markets in Warsaw, Krakow, Wrocław, Tri-City, Poznań and Łódź)





which constitute 78% of dwellings and by units scheduled for completion in 2012 (a 47% share in the offer).

In comparison with the previous quarter, the number of completed and unsold units was slightly higher. In total, the six analyzed agglomerations offered close to 9,700 completed and unsold units and this index increased by 6% within the year. However, at the end of June, in Warsaw there were ca. 4,000 such dwellings, slightly less than in the previous quarter.

The second quarter of 2011 saw a breaking of the downward trend regarding the asking prices of units newly launched for sale. After a period of price drops or stabilization, which lasted since Q4 2008, in Q2 2011 the developers increased both the number of units introduced to the market and their prices. Consequently, for the first time in a long time, the prices of units launched have started to resemble the prices of units already found in the offer. This could be one of the reasons for the sales slowdown. According to the market's logic, considering the current surplus of supply over demand in the following quarters, the prices should decrease or remain on the present level.

## Demand

In Q2 2011, the number of sales calculated for the six analyzed markets decreased in comparison with Q1 by close to 5%, even though the market expected a slight growth or stabilization of the sales level. Considering the growing volume of the offer, this translates into a rather significant sales drop per average project, which was confirmed by information coming from many developers.

Sales intensity in the six markets, calculated as the ratio of the number of units sold within the quarter to the volume of the offer at the quarter's beginning, amounted to 18% at the end of June, therefore it decreased by one percentage point in comparison with Q1 2011. Bearing in mind the volume of the offer, the sales rate seems rather satisfactory, since theoretical balance is achieved at the level of 25%. The best result was noted in the Tri-City (21%), while the lowest intensity was observed in Łódź (11%) and Poznań (12%).

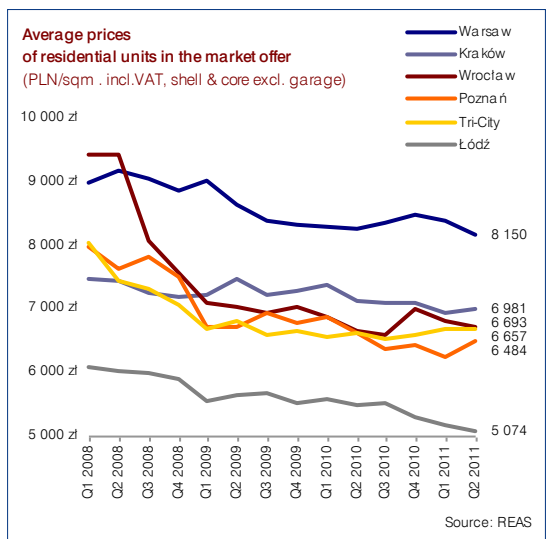
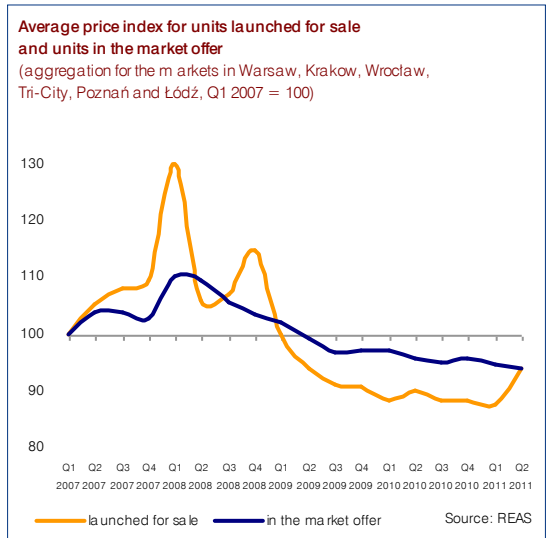
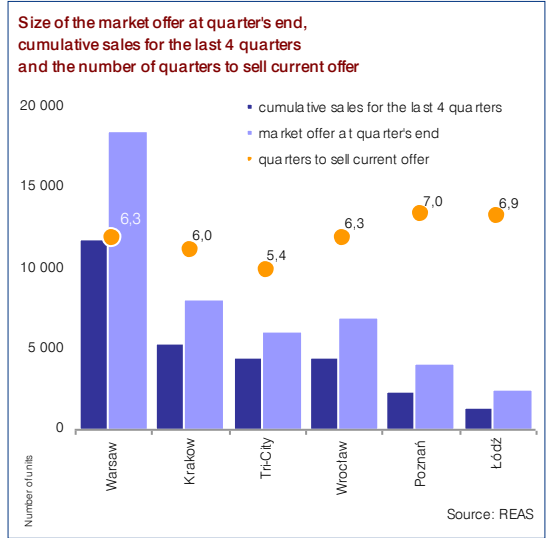
It is also worth considering the current offer volume against sales in the previous four quarters. In general, the index ranges from

136% in the Tri-City (i.e. the local offer constitutes 1.36 of annual sales) to 175% in Poznań. With the exception of Wrocław, where after Q2 the index remained on the same level as in the previous quarter, in other cities the ratio of the offer volume to the sales result increased (i.e., it takes longer to commercialize the whole local offer.)

In the majority of cities, the total sales level in the previous four quarters was slightly higher than the long-term average for these markets, while in Wrocław the surplus was significant. In this respect, the one exception is Warsaw, where in the analyzed period a total of ca. 11,800 dwellings were sold, less by ca. 1,000 from the long-term average transaction level for this market.

The demand in five agglomerations is supported by fundamental factors: the next age-groups of the second baby boom are graduating, entering the job market or gaining independence. These locations remain attractive for young Poles from smaller cities and villages, while the government has underlined that in the current decade it will focus on economic development in the major agglomerations.

On the other hand, despite the stable and advantageous sales results, residential market offer continues to grow. Consequently, the sales level for the average investment project diminishes. This translates into an increasing diversification of the condition of various developers: in some companies sales remained on the previously noted level, while in others it decreased considerably, causing liquidity problems. The market becomes increasingly competitive not only in terms of prices, but also when it comes to the flexibility of payment systems offered to the buyers. Companies will then have to secure more loans or increase the commitment of their own capital. Profitability of developer activities will then begin to decrease and so will the willingness to launch new projects. Within the following months, we are likely to witness a drop in new supply. However, macroeconomic and psychological factors will decide whether this will decrease the size of the offer. The following quarter will show if the current sales stabilization is only a temporary phase or a sign that a further increase of sales is impossible considering the existing price levels, interest rates and offer features.





## Selected REAS' Clients



## About REAS

REAS is an advisory company specializing in issues relating to the residential market. Since 1997, we have been cooperating with developers, banks, investors and other entities operating in the residential market. Only during the four previous years we worked for over 310 different clients, effectively supporting them in the process of project planning and implementation. The high quality of our services is proved, among others, by the fact that REAS has implemented more than five advisory projects for over half of our clients.

Since the year 2000, REAS has been conducting continuous monitoring of the primary residential market, accumulating data on projects in a database based on the GIS system. REAS database currently features 10,475 projects, including 3,279 projects on sale offering 79,801 flats and houses, as well as 1,382 planned projects which have not been launched for sale yet. This knowledge allows REAS to offer a broad range of market analysis services and to devise long-term market forecasts supporting the process of strategic planning.

REAS provides advisory services at all stages of the investment process, supporting the developers in the process of designing and preparing a product with the best market potential and competitiveness. The implemented advisory projects feature the following services: location analysis based on market and zoning conditions, recommendations regarding the project-mix and functionality of residential units, opinion and recommendations regarding architectural designs, pricing strategies and units' price lists, and recommendations regarding marketing and sales strategies.

REAS specializes also in valuations of investment land and existing residential buildings. The valuations are conducted by certified property valuers with many years of experience allowing them to use both domestic and foreign valuation standards, i.e. British (RICS), European (TEGOVA), American (USPAP) and international (IVSC).

Thanks to our long-term cooperation with institutions financing the residential market in Poland and the recognized reliability of our business plans, valuations and feasibility studies devised by the company, REAS is able to effectively support investors in the process of obtaining financing for new residential investments.

In 2007, REAS became a partner of Jones Lang LaSalle, the global leader in advisory services in the commercial real estate market.

## Key Services

- Market research, analysis & forecasting
- Competition monitoring & analysis
- Highest & Best Use studies based on market, zoning and financial analysis
- Development consultancy, location analysis, recommendations regarding the project-mix and functionality of units
- Guidelines for architects and review of designs
- Marketing & sales consultancy
- Property valuations (RICS, TEGOVA, USPAP, IVSC)
- Business plans & financial feasibility studies
- Capital raising & search for equity partners
- Investment sites disposal & acquisition

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