Colliers

2021

2022

2023

Romania
in the Next Decade

The New Roaring 20s

2027

2028

2029

Dear friends and partners,

At the beginning of last year, we hoped that 2020 could be the year real estate goes to the next level. Instead, we experienced a year like never before. Our agility, adaptability, intuition, creativity, presence of mind, interpersonal relationships and team spirit were vital.

There were and still are difficult and complex times. However, the way we handle the pressure can positively change our long-term perspectives. You can either look at your obstacle and see a dead end, or, on the contrary, see a new challenge. It gets complicated only when these challenges start hitting you from everywhere. John Churton Collins was very right when he said: ***In Prosperity, our friends know us; in Adversity, we know our friends***. In turbulent times, you see who you can count on. We are a source of energy for those around us; we have the power to empower each other. And when the stormy weather is gone and you finally succeed, isn't the rainbow even more spectacular?

We are going through some structural changes. Resistance can be harmful in these situations: a strong structure resists, it fights back but, under high pressure, it yields, sometimes in the most catastrophic way. Resilience, the ability to keep returning at the same point, has its limitations, too. When we talk about structural changes, I believe the short-term solution is Agility, and the long-term solution is Adaptability: the power to move forward, to do things differently, to recalibrate as the context asks you to. Look at nature, how it evolves and adapts, especially in critical circumstances.

I think that this pandemic, corroborated with the changes we experienced in Romania at the end of last year, must wake us up to make much-needed structural changes in four main areas: Education, Health, Infrastructure and IT. Through Education, we can change Romania for the better in the long run. A good Health system gives us courage to look ahead. If we improve Infrastructure in the next 10 years, we will immediately see enormous benefits in all market areas, and IT can make a difference quickly, if it becomes a priority in our national strategy.

We have just started a new decade and I am convinced that the next 10 years are a great challenge, but also a great opportunity, perhaps one that Romania has not had for a very long time.

Let the new roaring 20s begin!

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Top 10 Predictions

Our traditional (by now) top 10 predictions face a much more difficult task this year in anticipating what may be, as certainties are few to spare at the beginning of 2021 following one of the rockiest years we have seen in a while. We will try to do our best to remain relevant, but as far as we're concerned, the general atmosphere right now could be summarized in: if it is good, it will be a great year, if it's bad, it may turn out terrible, so lower chances for a mid-ground scenario.

1 Uneven, but fairly swift economic recovery

Romania should recover most of last year's losses in economic activity by end-2021, but the path is still fraught with many uncertainties (like in the vaccines' ability to return everyday life more or less back to normal or if monetary policy will start tightening a bit, with deep ramifications in the global economy). Furthermore, the recovery will be quite uneven. Some economic sectors (e-commerce, construction, certain IT&C subsectors) have not blinked at all during the crisis, some should recover by end-2021 (retail trade and professional services in general), some may take years (if ever) to crawl back to a decent activity level (aviation, automotive or tourism). We look for GDP growth in the 4% region in 2021 after a decrease of c.5% last year.

2 Laying the groundwork for future economic breakthroughs

Romania is nearing a decade and a half as an EU member state and it should have gotten the hang of how to bring in EU money. The new pandemic package from the European Commission and the potential for somewhat improved flexibility from the European authorities suggest that we may start seeing some results soon. Romania could attract as much as EUR 80bn in extra capital in the next years, one third of the country's GDP, which should have a much greater impact than in neighbouring countries if correctly utilized. We will carefully look for signs of breakthroughs with regards to reforms and changes that could greatly accelerate economic development over the medium-term and we are moderately optimistic with respect to this.

3 The pandemic won't be the same, but some things will seem déjà vu

The emergence of coronavirus vaccines and their deployment in many developed countries as of late 2020/early 2021 means that the economies and particularly impacted sectors (like tourism and entertainment) ought to see the light at the end of the tunnel, particularly in the second half of the year. Reaching a reasonable threshold of immunity could be challenging in some countries like Romania, which face a bigger percentage of popular skepticism towards vaccination, but it is still doable. We also expect tourism to become more local and more frequent as things return to normal. Then again, 2021 will seem like a déjà vu from some aspects, as the pandemic will still influence things greatly, for instance, in canceling/delaying certain events, bringing ups and downs to economic activity.

4 Remote work to become a new normal

One of the biggest changes to come out of the COVID-19 pandemic, with deep ramifications for various real estate sectors, is the rise of remote work for wide categories of employees. It may be tempting to jump on a bandwagon prophesying something like the end of offices or of big cities as people move to suburbs, but when the dust will have settled, the overall context may end up not that dramatically different. Yes, remote work will become a permanent fixture, but we believe that companies will also want to bring their employees at least 2-3 days a week in the office in order to foster teamwork and corporate culture. A more significant return to offices of employees is expected around the middle of 2021, with buildings located in residential areas at the forefront, benefiting from a reduced commuting time.

5 Office tenants reign supreme

A robust office delivery calendar is in store, with over 250,000 sqm of modern offices due to be delivered in Bucharest. With a rapidly rising secondary market of sublease alternatives (low range estimates place it at over 2% of current stock at present) and a vacancy rate in excess of 10%, tenants reign supreme. Consequently, it may be a good time for tenants to lock in more favourable leasing terms over the longer run, as we expect that office market conditions should return to neutral in the first half of this decade. As for 2021, things may look worse for landlords before they look better (vacancy set to increase sharply, to c.17-18%, with risks skewed to the upside), though in line with recent trends, good modern buildings are still set to outperform.

6 The I&L boom is far from over

The industrial and logistics market did not blink as the pandemic hit the global economy in 2020, ending its strongest year in history for Romania. 2021 should be no different as recent trends supportive for the development of warehouses remain in place: the rise of e-commerce in a competitive landscape, the need to cater to a rapid expansion of modern retail schemes nationwide, the need to replace the old and uncompetitive stock (including from a safety standpoint). There is also some potential for business amid Brexit and the overhauling of relations between the EU/US and China, but this theme would become viable rather over the medium term. A good pace in infrastructure development (including Bucharest's external ring road) would unlock new markets/locations.

7 Retail under pressure, but there are silver linings

Retail sales have seen a fast V-shaped recovery, but not everybody benefited from this. The growth in e-sales greatly outperformed that of traditional brick-and-mortar stores through 2020 and this trend should hold in the new year. That said, we believe that some retail schemes ought to still do good post-pandemic: the large dominant shopping centers (as these remain major destinations), small proximity schemes and retail parks in towns which have limited modern retail coverage. Rents and vacancy should remain under pressure through 2021 and may not recover until 2022 or even 2023. That said, Romania's higher profitability for retailers and the low stock of leasable modern retail spaces per capita should insulate the market from any major negative news and lead to a good subsequent recovery of losses.

8 Investment deals to dip, but market not soft at all

2020 did not turn out to be a bad year at all; in fact, strictly from a volume perspective, it was one of the better years this past decade, but there is a lot of inertia at play as a new investment deal may take years to be completed. So, 2021 investment market may see a dip in activity from around EUR900mn to around EUR500-600mn. Some buyers may remain on the sidelines amid a lack of clarity about future revenues (particularly regarding better positioned assets in sectors like offices and hotels); on the flipside, we should see much more in terms of distressed assets or properties with a value add angle, which may offer a more attractive proposition for buyers.

9 Diverse opportunities in the land market

Given the considerable number of deals initiated in the recent period (including in 2020), the land market looks set for a good year. Retail (including big box operators) and residential developers will remain the driving force. Demand for land plots for offices and hotels will remain soft and we would not expect things to change too much given elevated uncertainties with regards to the leasing/revenue side. More clarity the latter could help unlock some deals frozen at the start of the pandemic. Pricewise, we expect to see a small downward adjustment on average, which is normal given that there is a lag between economic developments and the real estate scene, though some segments/areas may escape altogether a negative price change.

10 Breather year for residential

One of the bigger surprises of 2020 was the fact that despite the adverse economic reality, the residential market still saw strong demand and modest price gains (on average). This was due to the labour market remaining quite robust, but things look a bit different for 2021. Barring any second-round aftershocks from the pandemic, wage growth has ground to a halt in the private sector and it may take some time to start rising again, while civil servant wages are frozen amid fiscal consolidation. Hence, 2021 should be a bit softer than 2020 for the local residential market. Otherwise, the dynamic cities from an economic standpoint and their outskirts remain attractive in the longer run given Romania's overcrowding problem.

Romania in the Next Decade

A new roaring '20s?

Top 10 best performing economies in the world in the last two decades

	Change in GDP/capita 2000-2020 (percentage points)	GDP/capita. 2000 (USD. PPP. % of avg for advanced economies)	GDP/capita. 2020 (USD. PPP. % of avg for advanced economies)
Ireland	65.2	108.4	173.6
Lithuania	42.1	32.9	75.0
Singapore	37.0	148.7	185.7
Taiwan	32.0	72.9	104.9
Romania	30.4	28.1	58.6
Panama	30.1	28.3	58.3
Estonia	29.7	42.2	71.9
Latvia	29.3	30.1	59.4
Korea	29.0	57.0	86.0
Poland	25.5	40.0	65.5

In the past two decades, Romania's GDP/capita increased from a level of 28% relative to the advanced economies to 58.6% in 2020, with this performance placing it in the 5th spot globally.

The roaring '20s have been dubbed as such after the decade between 1921 and 1930 saw great economic and cultural enrichment in many developed nations on both sides of the Atlantic Ocean. We may be on the cusp of a new decade that can receive this moniker as innovation and loose monetary policy, coupled with an increased appetite for consumption after a lockdown year will take hold. It is also somewhat telling that the actual roaring '20s came right after the - arguably much deadlier - Spanish Influeza, which impacted the world between 1918 and 1920.

Romania is well positioned to take advantage of this new reality. To start off, we need to point out that the future is, in a lot of instances, an extension of the recent past. And the trend here is favourable to say the least. We looked at the IMF's GDP/capita adjusted to purchasing power parity and represented each country as a percentage of the average among developed economies for that year; then we looked at changes in GDP/capita, relative to the average of advanced economies (which eliminated the idea of a base effect) and Romania's performance is truly jaw-dropping. In the past two decades, Romania's GDP/capita increased from a level of 28% relative to the advanced economies to 58.6% in 2020, with this performance placing it in the 5th spot globally. This improvement of 30 percentage points outstrips that of most regional economies and China's, for example, with Lithuania being the only other country in the CEE a bit ahead. Ireland, Singapore and Taiwan are also ahead. And while the Irish so-called "leprechaun economy" has been called into question, as such numbers are not seen as reflecting the reality of growth, this means that Romania may be not too far from the podium and a bronze medal.

It is important to note that this performance has often been achieved in spite of (not thanks to) the general backdrop. Romania lags regional countries, let alone developed ones, in terms of: 1. Rule of law; 2. Infrastructure in general (including healthcare); 3. Efficiency of public administration; 4. Instability in general (with regards to laws and policies, but also in the political arena). Herein lies the main selling point for Romania: if any major improvements were to come from these factors, the growth potential that would be unlocked would be significant.

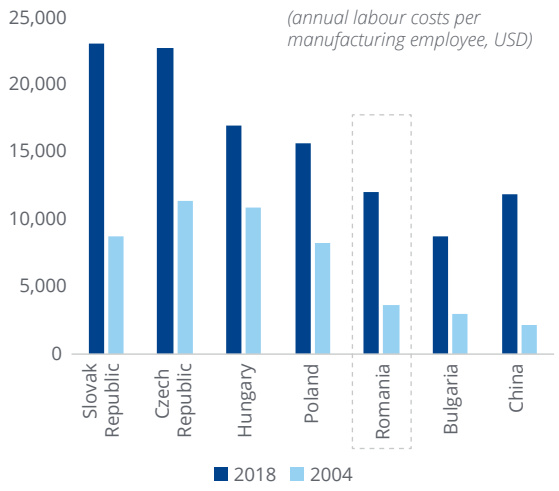
And Romania still has enough growth resources to come on top in this decade as well. Firstly, there is the labour market, where the story can be summarized by the following: relatively cheap and productive employees. You needn't have low wages, just lower than the major competitors. In manufacturing, Romania's labour costs are comparable to China's and several times smaller than in Western European countries, while in the high-value added sectors things also look good; though IT&C wages can be half of the levels seen in Western European countries, living costs in Romania (particularly real estate-related) means that the purchasing power may actually look better here. A second major advantage is the position and with geopolitics mattering more and more, Romania is in an important region for its more developed Western allies. Somewhat elevated corruption and a historically low drive for reforms constitute major drawbacks but, then again, Romania did score the 5th best economic performance in the world with these around.

There are also a few major trends than can move things around quite a lot in the Romanian economy, creating both opportunities for those with foresight and issues for those not prepared. Slightly more than half of Romania's inhabitants live in urban areas, as per the UN's definitions. Compare this to 80% in high-income countries and an average of nearly 70% in Eastern Europe and you get the prospect of a lot of fast-rising urban hubs in the next decades. This will create a lot of opportunities for various companies, including construction and real estate.

Automation (both in manufacturing and business services) is another big trend. People tend to focus on the potential job losses, with some older estimates from Brugel, a Belgian think-tank, suggesting that in excess of 40% of jobs in Romania, much more than in other EU countries, could be at risk of automation. That said, research indicates that there is a pretty high and positive correlation between labour costs and robot density. In other words, automation will come somewhat gradually, as wages continue to creep up in Romania, while rising from very low levels compared to developed economies. Statistics from a couple of years ago show that Romania had some 20 robots per 10,000 workers in manufacturing, half of Poland's level and several times smaller than Czechia's.

State intervention via programs and education will be key to ensuring that this transition will not lead to a negative social result. Education in general will be an important topic, though adequate reforms taken now would yield results rather in the subsequent decade. Either way, if the state policies can arrest the negative externalities from automation, this process will prove a very positive dynamic as it will likely support Romania climbing even more the economic complexity ladder in terms of its output.

After factoring in transport costs, customs, potential delays and geopolitical issues, some CEE countries start to look attractive versus China



Source: The Conference Board, Colliers

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A fourth point we believe will shape the next decade is related to globalization. It is not that globalization is set to be materially reversed by any means, just that things may start becoming less global and more regional. This ought to open quite a lot of opportunities for countries like Romania, which can serve as re-shoring destinations for advanced European economies (particularly in light of what we mentioned earlier, i.e. labour costs comparable to China's for manufacturing). Brexit and the reshuffling of relations between advanced economies and China should lead to some positives for Romania and the CEE region as a whole.

A major opportunity which Romania should take advantage of relates to EU funds: the coronavirus aid package plus the normal allocation for the 2021-2027 period for Romania is around EUR 80bn or one third of the country's GDP. Since capital accumulation is usually one of the aspects holding down emerging countries like Romania, it is that much more important to correctly utilize these funds. For now, it is too early to speculate on the outcome, but we would hope that after a decade and a half as a member of the European Union, Romania will have learned the ins and outs of Brussels bureaucracy and can now absorb all of these funds. And a point we made earlier needs to be underscored again: since Romania grew so well in spite of a lack of infrastructure, should such investments lead to big improvements, this would unlock significant (and sustainable) GDP growth.

2020 has shown that one cannot anticipate at all the events coming out from external factors and that these can turn things around quite a lot; these cannot be anticipated. But we can think about Romania's internal issues. A key topic this decade will be keeping growth alive to escape any middle-income trap, though for Romania, the growth resources (including capital) look favourable. Another challenge will be managing such rapid growth without the economy becoming "too hot", leading to a sharp correction down the line. Both of these themes will require a good governance in the years to come.

In conclusion, while the first years of the new decade may not seem too enticing in terms of outlook for most economies, Romania included, we would argue that it may be a bad idea to judge a book by its cover and to judge a decade by its first years. And we see more arguments in favour of than against the idea that the next decade will look for Romania much like the last two, leading to a significant economic overperformance over most countries in the world.

First recession in a decade, but there are silver linings already

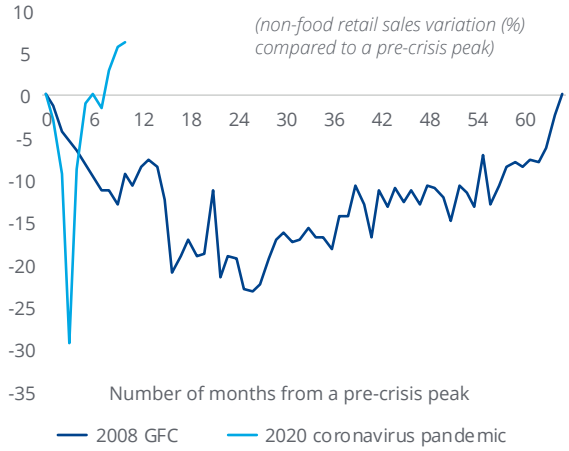
Yes, Romania had a recession with a GDP drop in the -5% region (this is also the figure recorded in the first 3 quarters of the year), but part of the negative impact was arrested by some state aid measures and by the risk-friendly atmosphere globally thanks to the generous quantitative easing measures from the likes of the Federal Reserve and the European Central Bank.

2020: a bit better than it looks

To start off with sort of a conclusion, 2020 looked quite a bit better than the previous recession following the Global Financial Crisis (GFC) of 2008 and also better than one might have thought during the darker days of the pandemic, in the spring period. Yes, Romania had a recession with a GDP drop in the -5% region (this is also the figure recorded in the first 3 quarters of the year), but part of the negative impact was arrested by some state aid measures and by the risk-friendly atmosphere globally thanks to the generous quantitative easing measures from the likes of the Federal Reserve and the European Central Bank. Furthermore, economic recovery does look noticeably better if we exclude agriculture from the GDP's calculation, as it is a small, but very volatile sector in Romania (at around 4% of the economy, it accounted for about 1 percentage point of the economy's decrease).

Probably the most important indicator that highlights this more positive view is the fact that the job market has remained quite robust. Compared to February 2020 (peak employment before the crisis hit), the economy lost some 104,000 jobs by May on a net basis, then, during the summer, it started recovering and by November – the earliest available month at the time of writing, job losses versus February levels were down to less than 70,000. Compare this to the recession that ensued after the GFC: in the initial phase, the current recession looked slightly worse – particularly if we take the Lehman Brothers bankruptcy of September 2008 as the starting point, but over a year's time, net job losses topped by end-2009 and would rise further, above 700,000, by late 2010.

Steep drop followed by a record-speed recovery highlight difference versus previous recession



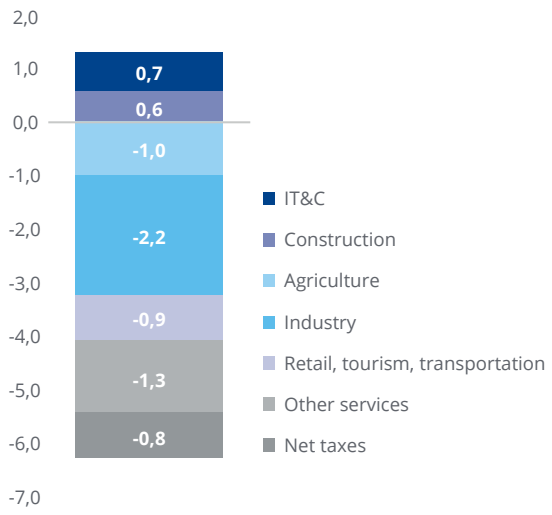
Source: National Institute of Statistics, Colliers

Wage growth also remained in the black during 2020 (in year-on-year terms), but this was largely because of a more generous public sector pay policy in the context of last year's elections, as in the private sector, based on our estimates, earnings were largely flat in the initial part of the pandemic, quite a departure from nearly 10% in previous years, but then accelerated towards 7% YoY by year end. Either way, a fairly positive picture which we also need to take into account is the fact that banks continued handing out consumer loans at significant levels and, hence, we saw more than a decent year in terms of household spending. Yes, some big-ticket purchases (like cars) suffered, though others were very robust (like home purchases), while on the retail side, things looked very good. All in all, a lot of the big segments of private consumption barely blinked in 2020, leading to a V-shaped recovery in non-food retail sales for instance, which have been already above pre-crisis highs as of autumn 2020, though other segments – particularly HoReCa – were particularly hit. This has led economists to dub this a K-shaped economy, where some sectors move up, some down – an underlying theme which should hold for some time in the near future. Either way, a quick comparison in how non-food retail sales behaved this time versus the 2009-2010 recession shows two completely different worlds: this time it took sales just a few months to reach January 2020 levels, whereas a decade ago, it took more than 5 years to return to September 2008 levels.

Meanwhile, external-oriented business sectors had somewhat of a mixed year. IT&C did well, unsurprisingly, in a year where emphasis has been on efficiency and automation; so did some BPOs and SSCs. On the other hand, industrial activities not geared towards sought-after consumer goods struggled quite a bit, especially the heavy industries, like automotive and aviation. Consequently, exports of goods were down some 10% last year, while if we were to exclude tourism and transportation, service exports were largely unchanged in 2020 versus 2019, quite an excellent result if we consider the latter to be a very good year. Also on the GDP supply-side figures, it is important to note that besides IT&C (which added around 0.7 percentage points to growth in the first 3 quarters of the year), construction works were the second biggest growth driver, a touch behind in terms of net impact.

A trickier aspect of 2020 was going into a new recession with markedly higher risks than most other EU countries, particularly with the twin deficits (current account and budget balances) looking worrisome; this bore a striking resemblance to the 2008 moment, when Romania also had worse internal risks than the likes of Hungary or Poland. The current account gap was largely unchanged in 2020 as the drop in exports was matched by the drop in imports, though a level around 5% of GDP is quite elevated and remains a medium-term vulnerability. The fiscal deficit, on the other hand, was potentially trickier as 2020 was also an election year and the impetus to pursue reforms was much lower; but going into this recession with probably the worst structural fiscal position in the EU meant that Romania's room to support the economy was already going to be lower than most other countries. So, even without adopting as generous stimulus measures, the fiscal gap swelled towards 10% of GDP last year. Amid all of this, Moody's also lowered Romania's sovereign rating outlook to negative back in April, following a similar decision from Standard&Poor's at the end of 2019. Thankfully, after last year's elections, Romania did end up with a governing coalition based on 3 parties which, while not the most stable (a collapse in the coalition remains a medium-term possibility given wide divergences on key topics), was a positive note from a sovereign risk standpoint, as the last thing the country needed was an internal political crisis.

IT&C and construction were the only private sectors still growing in 2020



Q1-Q3 GDP impact on GDP growth by sector (percentage points)

Source: National Institute of Statistics, Colliers

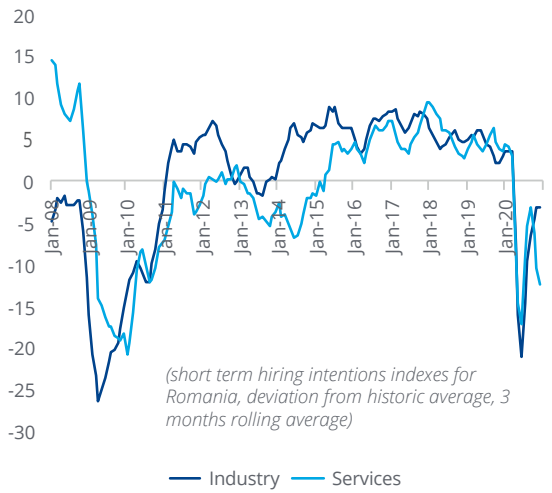
Financial markets have been remarkably stable, with the EUR/RON increasing by just under 2% last year; by comparison, the Polish Zloty and Hungarian Forint both softened by around 5.5-5.6% against the Euro. Furthermore, "imported" disinflation and a fairly competitive backdrop have led to prices remaining quite stable throughout 2020, with the inflation hovering comfortably within the central bank's target interval of 1.5-3.5%. This allowed the central bank to cut its key rate by 1 percentage point throughout 2020, to 1.5% (a subsequent 25bp cut was enacted at the start of 2021, taking the key rate to 1.25%). A special notice should be made about the start of a local quantitative easing program, with the central bank purchasing longer-dated T-bonds from the secondary market.

2021: a difficult year, but maybe not that bad

On a similar note to last year, one might be tempted to place more emphasis on risks and caution, but 2021 does look like it could be much better than such a train of thought would suggest. First of all, easy money is here to stay for now and this risk-on attitude in the global markets should rub off on the Romanian economy as well, as companies will want to start expanding, for instance, in order to prepare for the new upward business cycle. As a relevant side note, given what we said earlier about Romania's lack of fiscal space to adopt stimulus measures, this means that the country's economy has limited room and resources to accelerate materially above its European peers over the next couple of years. Consequently, a GDP expansion in the area of 4% (compared to a 4.1% forecasted expansion for the EU in 2021) is the best we could hope for. Unlocking further growth down the line is tied to structural reforms like improving infrastructure, cutting red tape or materially accelerating the absorption of EU funds.

Also, given Romania's somewhat vulnerable position which we mentioned earlier – in particular its twin deficits problem – the country is much more exposed to changes in the global backdrop. And for sure, there are many aspects to keep track of, from geopolitical tensions in various parts of the world to strained valuations in global financial markets to potential issues about the major central banks' ability to keep things afloat via more quantitative easing. Then there's the pandemic, which is far from over; in fact, 2021 may have quite a few ups and downs caused by this, as the new lockdown measures, the second-round effects and the uneven deployment of vaccination are bound to reverberate throughout the year, creating problems. Still, we would expect, nevertheless, the pandemic to be much less of an issue than in 2020. Then there is also the longer-term impact of the coronavirus pandemic to keep track of, especially on a macro level, as it will end up shifting big chunks of capital from certain sectors into others. We would also like to give a special note to the prospects of automation, which could particularly hurt Romania's labour market, as it has quite an elevated number of employees in low value-added sectors of manufacturing and services that could easily be replaced by machines.

Second lockdowns impacted quite a bit hiring intentions for services, suggests bumpy economic recovery



Source: Eurostat, Colliers

Turning to the more near-term outlook, with the labour market in decent shape and employers hiring intentions picking up much faster than after the 2008 GFC, it is clear that we are dealing with a different economy this time around. Furthermore, Romania stands to receive as much as EUR 80bn in EU funds over the next years, the equivalent of one third of the country's GDP, which, if correctly utilized, could unlock significant growth down the line, though the impact on private capital expenditures in 2021 should be limited.

Financial markets look set to have another somewhat stable year: we do not expect to see the EUR/RON or interest rates in wildly different regions than they are in right now. Interest rates could come down a bit lower as inflation looks a non-issue in 2021, whereas the RON could soften some additional 1.5-2% versus the EUR by the year's end.

That being said, we remain concerned about two aspects that are somewhat connected: 1. The political situation and 2. The budget situation. The ruling centre right coalition has a fairly thin majority in Parliament and there are already signs of noise not just between the 3 different parties, but inside the parties as well. And this is not exactly the most suitable backdrop to tackle difficult questions regarding the fiscal situation, which requires immediate corrective measures; take the so-called rigid expenditures – wage and social expenditures: these make up a staggering 87% of current revenues in Romania's budget, most likely the biggest share in the European Union, leaving much less room for necessary investments and increases in expenditures in areas where they are really needed, such as education and healthcare. In fact, while Romania did not see a sovereign rating downgrade to junk in 2020, it was the only major CEE economy to see a rating outlook worsening to negative. So, unless said corrective measures are adopted in a credible manner, Romania risks having its rating cut to junk territory, possibly in 2021, which would dent the longer-term outlook.

On the flipside, should the governing parties learn to coexist with each other, there is a fairly positive perspective, as the next 3 years are election free, meaning that this is an ideal moment to tackle the more difficult structural reforms. All in all, the context certainly demands a careful approach, but we still believe there are more arguments in favour of a fairly robust 2021, which should be just the start of a new upward cycle.

	2014	2015	2016	2017	2018	2019	2020E	2021F
GDP growth (%)	3,6	3	4,7	7,3	4,5	4,1	-4,7	4,1
GDP per capita (EUR)	7.600	8.100	8.600	9.600	10.500	11.500	11.100	11.800
Private consumption (%)	3,9	5,8	8,4	10,7	7,6	5,4	-4,2	5,2
Industrial output (%)	4,6	3,1	4,5	8,2	4,2	-0,8	-12,4	1,3
Unemployment rate (%, year end)	6,6	6,5	5,3	4,5	4,0	4,0	4,9	4,4
Current account balance (%/GDP)	-0,7	-1,2	-2,1	-3,2	-4,6	-4,7	-5	-4,8
Net FDI (%/GDP)	1,6	2,2	2,7	2,4	2,7	2,6	0,9	1,1
Budget balance (%/GDP. EU definition)	-1,2	-0,6	-2,6	-2,6	-2,9	-4,4	-10,3	-7,6
Inflation rate (%, year end)	0,8	-0,9	-0,5	3,3	3,3	4,0	2,1	1,7
ROBOR 3M (%, year end)	1,7	1,0	0,9	2,1	3,0	3,2	2,0	1,5
EUR/RON (average)	4,44	4,45	4,49	4,57	4,65	4,74	4,84	4,94

Bucharest Office Market

Supply

Some 156,000 sqm of new modern offices were delivered in 2020, quite a bit less than our c.200,000 sqm initial assessment at the start of the year and a long way from the 286,000 sqm seen in 2019. That said, it is still a fairly robust figure at around 5% of the current modern office stock in Bucharest, so not a poor year by any means. The major additions were spread throughout different markets: Ana Tower in the up-and-coming Piata Presei/Expozitiei submarket, the third phase of Globalworth's Campus project in Dimitrie Pompeiu, One United's One Tower in Floreasca/Barbu Vacarescu, another building in Skanska's Campus 6 project and the final phase in the Forte-developed The Bridge in Center West. This means that the overall leasable area of offices in Bucharest is closing in on the 3 million sqm threshold, which it should cross in 2021.

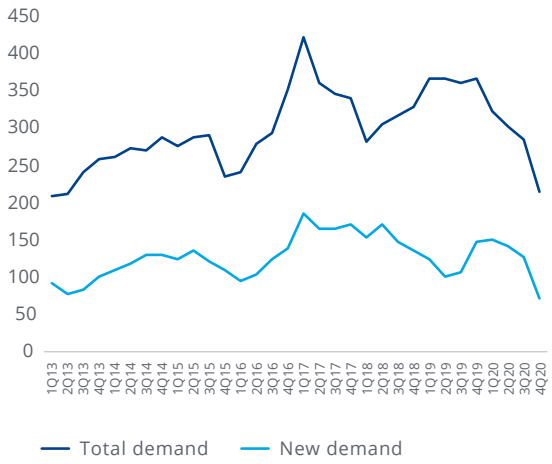
In general, the new supply remained well received in Bucharest, as the city still has a low supply on a per capita basis, plus a large part of the offices here are fairly old and not up to par with modern standards. That said, the moment has not been a favourable one, meaning that some of the new deliveries had below-average occupancy rates.

Demand

By some metrics, 2020 was the poorest year in more than a decade (probably since 2009, though some past data revisions make comparisons not as reliable). Gross take-up stood at 214,000 sqm, which is the lowest level since 2012 and some 40% below the previous year. But since 2020 had a bit more renewals being reported, this sweetened the picture a bit for gross take-up, as new demand more than halved, towards 70,000 sqm.

2020 turned out to be the softest market this cycle

(sqm, 4Q rolling sum)



Source: Colliers

It is important to stress that companies which were not in advanced stages of negotiations or were not pressed by immediate needs (for instance, a contract expiry) placed on hold all major real estate related decisions until they had more clarity; as of early 2021, nothing much has changed on this front, with companies still expecting to see how things will pan out later in the year (particularly with regards to vaccinations) and when/how many employees would be returning to work.

As an interesting development, the pandemic favoured the emergence of a secondary market built up by the extra spaces leased by large corporations. Most of these companies leased speculatively some additional spaces in order to match the expected increase in the number of employees. Based on our estimates which may be on the low side, the sublease offer at the end of 2020 was already in excess of 60,000 sqm (so more than 2% of the stock).

Companies which were not in advanced stages of negotiations or were not pressed by immediate needs (for instance, a contract expiry) placed all major real estate-related decisions on hold until they had more clarity

As a positive aspect, we believe that a significant part of the upcoming sublease tenants, some of which likely were not accustomed to modern offices until now, may extend their leases with the landlord a few years down the line.

As the coronavirus pandemic hit, most "officeable" employees in offices started working from home and though there were some optimistic assessments that they may return by the end of the year to offices, the explosion in coronavirus cases as of autumn scrapped such plans. In general, somewhere between 10% and 20% of employees came to work, but quite a lot of companies had single digit percentages. We would also like to emphasize that the bigger companies in particular have been more prone to implement a more aggressive remote work regime, as they had both the HR practices and the equipment at hand.

Rents & Vacancy

Rents are usually a bit more inelastic in relation to demand and it may take some time before they start moving lower, but for sure we are now living in a tenant's market and landlords are forced to become more flexible and more generous with incentives. As such, we are now seeing landlords sometimes offering leases below the 5-year standard duration and they are also a bit more flexible on the break options. Further pressures on rents are emerging from the rising sublease market, which offers prospective tenants fitted-out offices at quite attractive rents and even more flexible conditions.

However, the impact on rents is likely to be quite nuanced. Prime buildings should be fine: they tend to have big blue-chip tenants and though these may start subleasing part of their offices, historically, the very good offices in Bucharest have had above-average occupancy. Meanwhile, older buildings, maybe with poor positioning, should be much more exposed; their landlords may be forced to be even more flexible and maybe cut back rents by 5-10% in order to remain competitive relative to newer buildings.

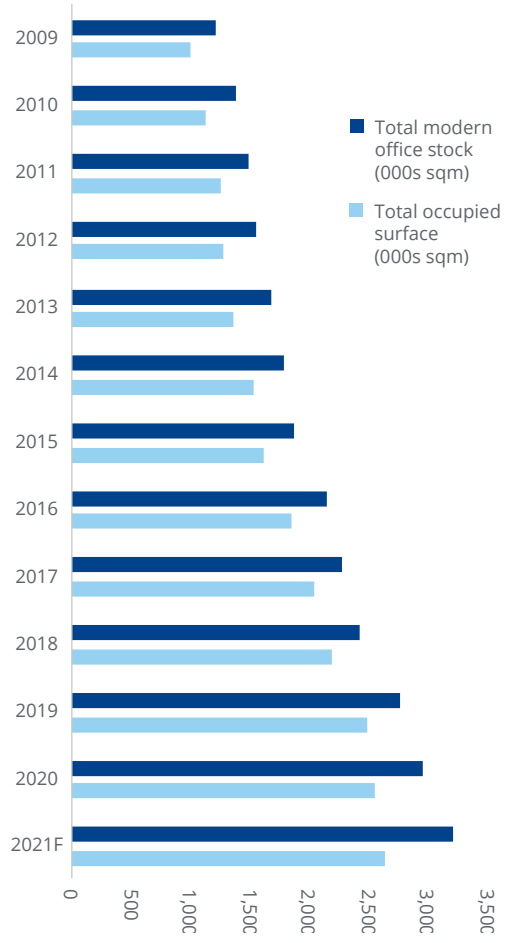
Turning to vacancy, last year saw it increase to a 4 year high of 13.75% from a little over 10% in the previous year. Vacancy continues to be generated especially by older, less prime buildings.

Outlook

Storm clouds are gathering on the office market in Bucharest: over 250,000 sqm of new modern offices are set to be finalized this year (with pre-lease ratios looking a bit worse than they did in the past, at around 40% for 2021 projects), though, as usual, some buildings may end up being pushed into 2022. Furthermore, we normally have at least 400,000 sqm of lease expiries every year and at least part of these may end up being much lower at renewal due to both current economic issues and the permanent impact of remote work.

On the latter aspect, we carried a few surveys with local tenants in 2020 and some conclusions hold important consequences for 2021 and beyond. First of all, almost all of the nearly 80 companies we surveyed will implement a remote work scheme, with most employers looking to offer around 2-3 workdays per week in the office and the rest, remotely (the surveys hinted at slightly more time in the office than for remote work, on average).

Mind the gap: over half a million sqm of Bucharest offices to be vacant by end-2021



Source: Colliers

We expect a lot of buildings due in 2022 or later to be postponed at least until the market balances itself out. But we remain quite optimistic about the Bucharest office market in the longer run

A second question with significant ramifications tackled what companies plan to do with their current occupied office space: 47% of respondents said they would keep it the same, whereas 43% of them said they would be looking to scale it back by as much as 30%; as an important detail, the bigger companies were more likely to cut back their offices than the rest, skewing the impact on vacancy to the upside.

The vacancy rate could climb towards 18% this year and in a negative scenario, we would not exclude seeing the rate climbing towards all-time highs seen during the 2009-2010 recession, of over 20% (though back then, the stock was only around 1.2 million sqm). But we see some mitigating factors that should keep things from becoming overly negative: 1. The economic recovery is much faster this recession than the previous one; 2. Bucharest is also a much more mature economy than it was a decade ago, with more blue-chip tenants which rely heavily on corporate culture and offices. This last aspect is particularly important, as we believe – also based on our surveys and other reports – that companies cannot rely entirely on remote work without negatively impacting productivity and team cohesion; consequently, our base scenario is that over the long term, we will see a hybrid work regime, with the dosage between remote and office work dependent on industry profile and employee preferences (to some extent).

Either way, we will have to see how the vaccination campaign continues and if inoculation can take place at a significant rate. As such, the return of at least 50% of employees could be possible towards the middle of the year, though hiccups at the start of the year (too few vaccines) could suggest this may be rather optimistic. However, in tune with companies not making too many long-term plans, we expect flexibility on all sides and should the vaccination campaign lag behind initial plans, companies would delay plans to return to the office towards the second half of the year.

Over a longer-term, we expect the Bucharest office market to remain a tenant's one for at least a few years, likely throughout the first half of this decade, as it will take some time before demand mops up the excess supply. Consequently, we expect a lot of buildings due in 2022 or later to be postponed at least until the market balances itself out. But we remain quite optimistic about the Bucharest office market in the longer run due to its strong labour market (it is in the top EU cities based on the density of its high value-added employees) and the fact that the city does not have an office oversupply issue at all.

Regional office markets update

City	Office stock (sqm)	Vacancy rate (%)	Pipeline (sqm)	Average rent (EUR/sqm)
Cluj	298,000	7.75%	8,000	12.5 - 14.5
Timisoara	224,000	12.00%	59,000	12.5 - 14
Iasi	198,000	12.50%	60,000	12 - 14
Brasov	166,000	10.75%	26,000	11 - 13

Gross demand in the four major office submarkets outside Bucharest (namely Cluj-Napoca, Timisoara, Iasi and Brasov) decreased some 19% in 2020, to c.60,000 sqm, though more than half of last year's take-up came from a single lease, a renewal of over 30,000 sqm in Iasi (Amazon). Without this deal, things would have looked worse statistically than in Bucharest though we would not read too much into this as quite a lot of direct transactions here possibly went unreported last year (as opposed to Bucharest, where we saw a bit more of these in 2020). We continue to hold a rosy long-term view for these markets, which hold a cumulated modern office stock of close to 900,000 sqm, less than one third of Bucharest's while at the same time, these cities tend to have a similar pace for job creation in 'officeable' sectors, with a prospect for acceleration in the future. Below-Bucharest vacancy rates are a testament to these markets' long-term potential.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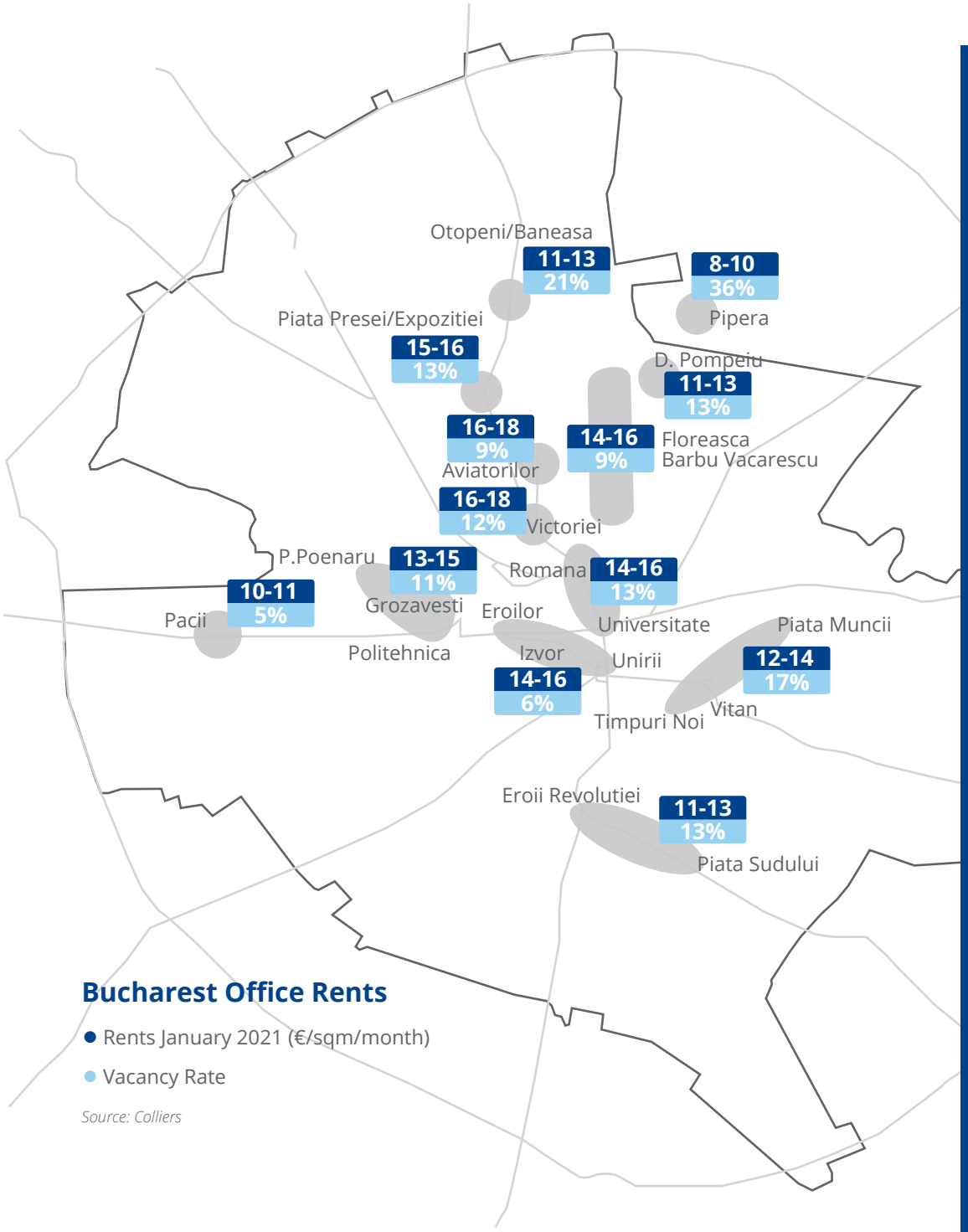


Bucharest Office Rents

- Rents January 2021 (€/sqm/month)
- Vacancy Rate

Source: Colliers

Romania in the next decade – office market

Special Topic

The next decade will see the stabilization of the office market after the integration of remote work in the work model of most service companies. This makes reading into the crystal ball nigh impossible, as we are on the cusp of a major change. That said, the positive factors that propelled Bucharest into becoming one of the most interesting and dynamic service centers in Europe will remain in place. In a nutshell, relatively low wages (versus Western Europe) paired with good technical and language skills. Consequently, we would expect the city to grow not just on a quantitative basis, but on a qualitative one as well, with many more global blue-chip companies (tech-oriented, but not limited to this) to set up shop here. Growth will also come from the lively start-up scene which has already delivered one of the fastest growing tech companies in the world (UiPath). Furthermore, we see the undersupply of modern offices in Bucharest as an insulating factor over the longer term and we would rather expect the modern office stock to start growing again in a few years; consequently, it could surpass 4 million sqm by the end of the new decade. Meanwhile, regional cities will remain behind Bucharest in terms of development, but they will grow and prosper nevertheless; these will seem more budget-friendly alternatives compared to Bucharest and will continue to offer somewhat less tight labour markets. We expect these to start growing much faster than Bucharest sometime this decade.



Retail Market

Supply

A bit over half of our initial forecast of c.250,000 sqm of new modern retail spaces were added in 2020, namely 142,400 sqm, as the pandemic caused delays in building and rental activities and prompted developers to take a more cautious stance. The bulk of deliveries came from 3 malls: the AFI-developed scheme in Brasov (45,000 sqm), NEPI Rockcastle's Shopping City Targu Mures (40,000 sqm) and Prime Kapital's Dambovita Mall in Targoviste (33,000 sqm). All in all, one of the lower figures we have seen in recent years, but this was to be expected given the difficult backdrop.

Demand

The closure of shops during spring months amid pandemic restrictions and subsequent drop in foot traffic due to distancing practices have chipped away at the retailers' brick-and-mortar revenues; local quarantine instituted in certain towns impacted things in the second part of the year going into 2021. Still, consumers have remained rather robust during this economic downturn, as job losses were several times smaller than after the 2009-2010 recession (bellow 100,000 net jobs lost this time versus close to 700,000 back then), while wage growth remained, on average, in the black (largely thanks to the public sector though). So, unlike the previous recession, money continued to flow in the economy, but there have been some major shifts in spending patterns.

Retail sales have generally kept up with the robust labour market, with 2020 looking nothing like 2009

Source: National Institute of Statistics, Colliers

Furthermore, non-food retail sales have, overall, completed a V-shaped recovery and are comfortably expanding in year-on-year terms, more than making up for the sharp decline during the first part of 2020. That said, a bigger part of this spending could not be captured by brick-and-mortar retailers as 1. consumers purchased increasingly more online (e-sales, as tracked by the statistical institute, possibly understated, expanded by 35% in 2020 versus a c.5% increase in non-food retail sales) 2. spending shifted quite profoundly towards sport goods, homeware or items aimed at improving living standards, including home renovations and white goods, at the expense of articles like clothing.

Turning back to brick-and-mortar retailers, as in any economic downturn, low prices tend to attract more people, hence discounters have had very good results (some growing their business double-digits amid expanding), while the mass-market fashion segment has seen similar results to those in 2019 – maybe a small decrease in some instances, but this is still better than the whole clothing market, which was down by a lot.

At the other end of the spectrum, there are many sectors that have not performed at all well amid the difficult conditions. The entertainment sector, which was one of the darlings before the crisis, remains particularly hit by restrictions. Consequently, some market players may face insolvency and some may actually not make it out at all after this crisis (particularly local/smaller players with limited financial support, and this is not only tied to the HoReCa sector).

Other segments that were particularly impacted are general and upscale fashion and shoes retailers (including office and evening wear), which tend to have the biggest share in terms of GLA in shopping centers. Some good months – like September – cannot make up for an overly poor year. Thankfully, December, which makes up for around 15-20% of a retailer's full year revenue showed non-food sales up by close to 7% over a year ago.

Rents & Vacancy

Landlords are feeling the double pinch of both smaller rents (with base rent cuts in the 15-20% region mostly amid added rent-free months, and as much as 30% in some special cases) and higher vacancy (with some large shopping centers seeing this creep up towards higher single digits). It is quite a departure from the pre-2020 situation, when some malls had waiting lists for tenants and limited to no free spaces. Pressures on rents (via renegotiations) and vacancy could remain in place through 2021 at least until tenants get their finances back on track – and this is in case we assume that the economy normalizes; under an adverse scenario, things would take a turn for the worse.

Forecast

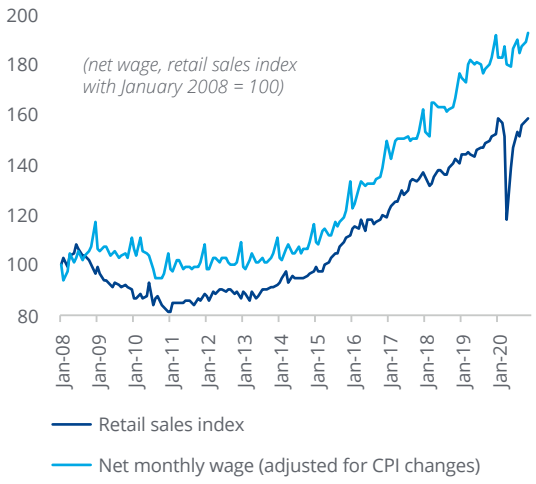
For the future, things are as cloudy as ever, but some seem to have changed already. We note that impulse buying has been drastically reduced, almost completely disappearing, while at the same time, shopping sessions have become shorter, less frequent, but with bigger overall tickets in some cases. This trend is likely to remain in place at least until uncertainties dissipate, so at least through 2021.

In the longer run, we believe that several categories of market participants (landlords or tenants) stand out to emerge as winners: 1. those with a dominant/ significant market share, who can leverage their position accordingly; 2. proximity-based retailers/ schemes, notably in emerging residential areas; 3. small-/medium-sized schemes, particularly retail parks in towns with low coverage of modern retail schemes. The second and third points are not particularly recent trends and have only been reinforced by the pandemic, so we will emphasize on the first aspect. We believe that an established fashion brand, for instance, could more than leverage its position and might be able to promote attractive multi-channel sales opportunities, like BOPIS models (buy online pick-up in store); in fact more traditional brick-and-mortar players that became e-sellers have chipped away at the market share of the pure online stores. Furthermore, the dominant shopping centers will likely retain their destination status, further reinforced by flagship stores and big retailers (including BOPIS).

This means that the middle ground may end up suffering the most: non-dominant shopping centers in competitive towns, retailers with limited financial power to support expanding adequately the e-sales channel. Some may end up exiting Romania or selling their local business down the line, in the next few years.

With regards to the development schedule for 2021, the total GLA adds up to over 150,000 sqm of new modern retail spaces, with the bulk of these coming from just two developers the Prime Kapital/

Wages versus retail sales show the latter having some potential upside room at the start of this new cycle



Source: National Institute of Statistics, Colliers

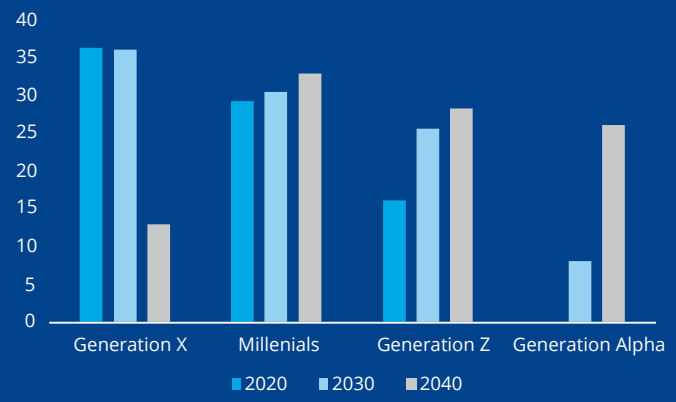
MAS REI joint venture – nearly 53,000 sqm from 3 new schemes (in Ploiesti, Sfantu Gheorghe and Barlad) and Mitiska – close to 25,000 sqm in 4 new schemes (in Baia Mare, Tulcea, Medias and Slatina). A noteworthy addition is for Bucharest – one of the larger deliveries we have seen in the Capital in recent years, with the expansion of the Colosseum Retail Park by over 16,000 sqm. Another novelty is the entry of a new player, Polish developer Scallier, which has secured several land plots throughout the country and promises 40,000 sqm of new retail spaces by 2022; part of these are slated to come in

2021. As a relevant detail, over 80% of the new retail spaces expected in 2021 will be in the form of retail parks (including smaller strip malls), highlighting a market shift towards proximity-based schemes or those with a smaller financial footprint for the developer, hence smaller risks.

In terms of rents and vacancy, it is likely that 2021 will bring more suffering and we would not expect things to return back to 2019 levels sooner than 2022 or even 2023 on a more generalized basis. That said, amid a fairly low per capita stock of retail spaces in Romania (one third below Poland's for example), negative events like the ones we have been through in 2020 should be absorbed by the market and the subsequent growth should lead to a swift recovery of losses – profitability of local retailers is several times higher than that of the EU average, as per Eurostat figures.

Romania in the next decade - Retail sector

Changing of the guard: age cohorts as % of working age population in Romania



Source: United Nations, Colliers

Special Topic

With a total modern retail stock of around 4 million sqm currently, we could be moving past 5.5 million by the turn of this decade, which would still likely be lower on a per capita basis than what some regional peers have. The vast majority of these new schemes will be in towns with limited retail presence, while in other parts, developers will be ever more cautious as the rise in e-commerce is more than a fad; omnichannel sales will make or break a retailer's position in the coming years, as the integration of personal preferences and added flexibility will push forward a mix of offline-online commerce. A change in generations could also define a lot of things, as millennials and 'zoomers' (gen Z) tend to have a more conscious attitude towards consumerism and topics such as ecology or spending ethically; generation Z, which consists of the first individuals truly raised in the digital world, will start mattering more in the workplace in the next decade, making them more relevant as consumers. We would also look for Romania's wages to continue climbing much faster than the EU average in the next decade, which would likely lead to both higher consumption and to an increased predilection for upscale goods. We would look over the coming decade for Romania's actual individual consumption to close in on 90% of EU average from below 80% currently.

Projects to be delivered in 2021

City	Baia Mare
Scheme	**Baia Mare Shopping Park**
Owner	Mitiska Reim
GLA (sqm)	8,000

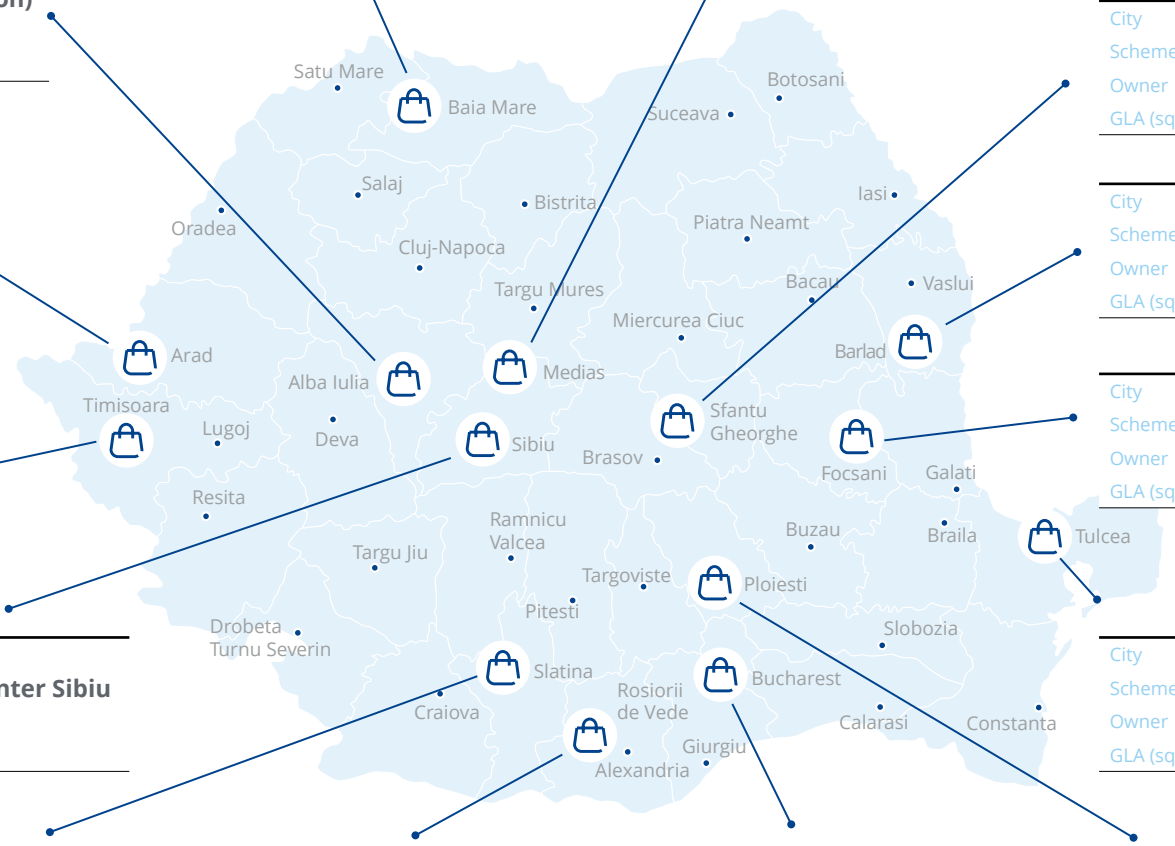
City	Medias
Scheme	**Medias Shopping Park**
Owner	Mitiska Reim
GLA (sqm)	6,000

City	Alba-Iulia
Scheme	**Alba Mall (extension)**
Owner	-
GLA (sqm)	6,000

City	Sf. Gheorghe
Scheme	**Sepsi Value Center**
Owner	Prime Kapital/MAS REI
GLA (sqm)	16.300

City	Arad
Scheme	**Galleria Arad**
Owner	-
GLA (sqm)	20,000

City	Barlad
Scheme	**Barlad Value Center**
Owner	Prime Kapital/MAS REI
GLA (sqm)	16,700



City	Focsani
Scheme	**Funshop Park Foscani**
Owner	Scallier
GLA (sqm)	6,400

City	Timisoara
Scheme	**Funshop Park Mosnita Noua**
Owner	Scallier
GLA (sqm)	11,000

City	Sibiu
Scheme	**Prima Shopping Center Sibiu**
Owner	Oasis/Supernova
GLA (sqm)	9,000

City	Tulcea
Scheme	**Shopping Park Tulcea**
Owner	Mitiska Reim
GLA (sqm)	5,000

City	Slatina
Scheme	**Slatina Commercial Center**
Owner	Mitiska Reim
GLA (sqm)	6,500

City	Rosiorii de Vede
Scheme	**Funshop Park Rosiorii de Vede**
Owner	Scallier
GLA (sqm)	5,000

City	Bucharest
Scheme	**Colosseum (2nd phase)**
Owner	Colosseum Mall SRL
GLA (sqm)	16,500

City	Ploiesti
Scheme	**Ploiesti Value Center**
Owner	Prime Kapital/MAS REI
GLA (sqm)	20,800

Industrial & Logistics Market

Supply

In excess of 0.5 million sqm of new modern I&L spaces were delivered in 2020, based on our estimates, with the bulk of these coming online in the Bucharest area (around half of the total) and the rest scattered throughout the country – mostly in cities from Transylvania, but also in some southern parts of the country. While Bucharest remains the heart of the local logistics market, there have been some slight changes from one year to another in the sense that more and more new warehouses are being developed outside Bucharest and 2020 was no exception. The overall stock stands at around 5.7 million sqm.

While some speculative developments were initially put on hold, the rosy economic results in the second part of 2020, coupled with the swift recovery in consumption, brought these back on the map in the second part of the year. CTP and WDP remain the major players, but we have some new names on the market that have the potential to make major investments in the next period – Globalworth/Global Vision and Element Industrial.

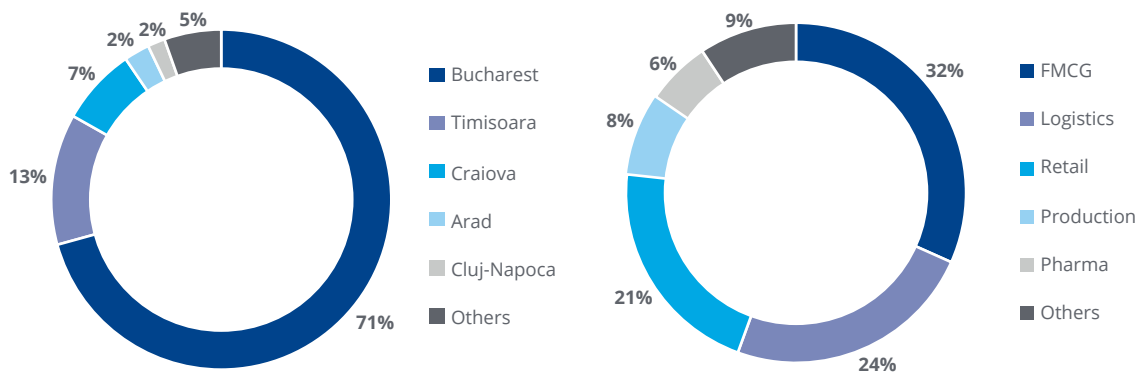
Demand

2020 turned out to be a bumper year for industrial and logistics, with total demand increasing by a staggering 72% over 2019, to nearly 784,000 sqm of leasing deals, most likely an all-time high for Romania (we lack historical comparable data to confirm this, but it is unlikely we would have seen such levels of demand in the past, given the much lower stock we had back then).

A large part of the demand seems to be consumer oriented and is coming from a) various retailers (including FMCGs) expanding their presence nationwide, not just in Bucharest, as the boom in spending in the past cycle caught the market off guard and b) various companies (not just pure e-commerce players) looking to branch out in the e-sales segment.

Bucharest remains at the forefront of activity and generated over 70% of the total leasing deals, with Timisoara and Craiova following at a great distance. Meanwhile, on a sectorial basis, FMCGs accounted for one third of total demand, with just Carrefour and Profi's 3 leasing deals (which were among the biggest of the year) totaling 200,000 sqm. Second and third places - logistics and retailers - were not too far apart from each other though in a lot of instances, the 3PL tends to serve the retail sector to

Gross take-up structure by location and by sector (% of total)



Source: Colliers

a significant extent, so it would be safe to say that consumer-oriented industries generated at least two thirds of demand in 2020. This is quite a departure from 2019, when automotive generated one third of demand, though in a market like Romania, only a few very big deals are enough to swing things to one side.

We view the structure of demand as a consequence of the underlying strength of the consumers, seeing as the local market delivered the best growth rates (by far) in the EU in the past decade; furthermore, if we were to look at just consumption per capita based on volume-based indexes, Romania has already caught up with Poland and surpassed Hungary, for example and yet, still lags its peers greatly when looking at I&L stock per capita.

Rents & Vacancy

We observe little changes with regards to rents, which remain in the 3.8-3.9 EUR/sqm region for prime warehouses near Bucharest and just a bit below such levels in other parts of the country. In spite of the somewhat competitive backdrop with a fair few major developers, we consider that we may see rents trekking upwards a bit in the next years as Warsaw and Budapest can close in on 5 EUR/sqm for prime assets.

Meanwhile, vacancy has been climbing a bit in the last couple of years (5% in 2019) towards 8% for Bucharest, based on our estimates; a similar level is also seen in Timisoara, with a bit lower levels in other parts of the country. That being said, such levels still suggest a fairly balanced market, not a tenant's one.

Outlook

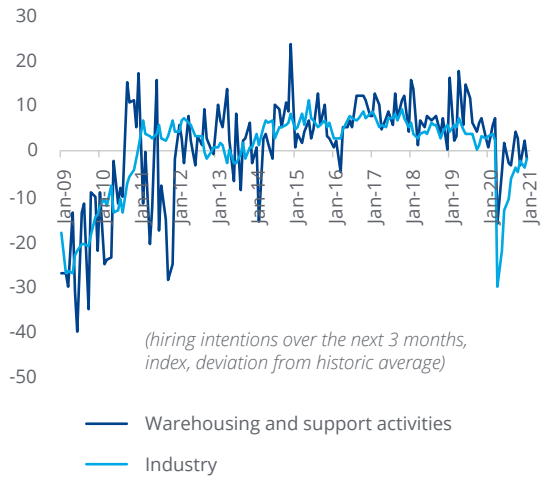
I&L has been, arguably, one of the most interesting asset classes – and this is valid not just for Romania, but also for large parts of the global economy, as warehouses proved to be a source of steady income even during such difficult times. Consequently, one of the first trends which we consider worth mentioning is that post-pandemic, a lot of investors that have not been exposed to this sector will want a slice of this pie. We expect to see more and more non-traditional developers either developing themselves or in partnerships or purchasing income-producing assets; we have quite a few companies active on the office and residential sectors in Romania that serve as examples.

This also means that sale and leasebacks are an attractive proposition, particularly if the tenant company operates in an interesting sector. For companies which own their warehouses, this can be an opportunity to get some liquidity at improving terms compared to previous years and free capital that can be used for other purposes – like investing, and it is a great moment for this given the growth perspectives in the new upward business cycle that is just getting started.

With regards to demand, we continue to see major upside from consumer-related sectors and in particular e-commerce. As a relevant side-note, quite a few of these companies are planning to use Romania as a base of operations for other smaller economies in the region, like Bulgaria, Serbia and Greece, turning Romania into a smaller regional hub.

With regards to supply, developers are promising in excess of 0.6 million sqm of new developments in 2021, as new supply is needed both to account

Hiring intentions normalizing much sooner than after the previous recssion



Source: European Commission, Colliers

for the robust demand and to replace a significant stock of older warehouses which are not up to par with current technical and safety requirements. We would also want to emphasize that speculative developments, which were halted during 2020 amid elevated uncertainties, should come back to life and matter much more: possibly as much as 20%, double the share we registered in 2019, could come from speculative developments.

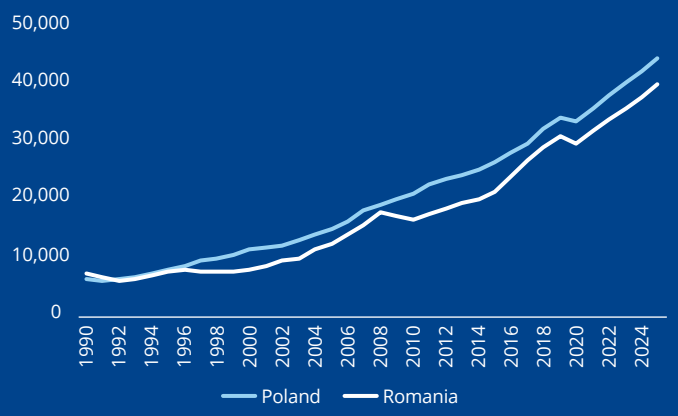
Turning to a longer-term outlook, there are a few things to keep an eye on which could be visible in the next years, but may offer some upside as soon

as 2021. Firstly, we need to emphasize the prospects for infrastructure developments, particularly now that, Romania has hopefully learned its way around attracting EU funds. Should some major progress be made, this would unlock quite a lot of investments even ahead of finalization of said investments. A special note can be made with regards to the development of A0, a new ring road around Bucharest (works starting in 2021); this would mean the development of new areas in the southern part of the Capital which currently have almost nothing in terms of modern warehouse options. Secondly, there is the prospect of much more activity in the long run from external developments, like Brexit and the reshuffling of EU/USA relations with China; both of these have the potential to bring in some manufacturing or logistics activities in Romania, particularly if we regard that labour costs in manufacturing, for instance, are comparable between Romania and China. Overall, all of these aspects create quite a rosy picture for I&L over the medium to longer term.

Romania in the next decade – I&L sector

Romania's growth gap versus Poland seen shrinking in the 2020s versus the 2010s

(GDP/capita in purchasing power parity terms, USD)



Source: IMF, Colliers

Special Topic

A simple rule of thumb based on some of the big numbers (like GDP/capita) is that Romania is several years behind Poland, but growing at a similar pace. Some say 5 years, some say 7 years, though IMF data suggest this gap has been shrinking. Just catching up to where Poland is now, in the next decade, would mean doubling the modern warehouse stock (at least), meaning over 10 million sqm by the end of the decade; a lot of this hinges on infrastructure developments, but if these would to come to pass, then the 10 million sqm may actually be quite a low guesstimate. But this is just scratching the surface in terms of changes to the market. As e-commerce will become a staple of everyday life and deliveries will need to take place in short duration (sometimes, same day delivery), retailers will need a heavier warehouse presence, including last-mile logistics, as well as in other parts of the country. Automation will also be featured much more frequently as companies will try to circumvent higher labour costs and lower availability of labour altogether. The next frontier will consist of integrating even newer technologies into logistics, such as driverless cars, robot or drone deliveries and so on.

Investment Market

CEE Market

End-2020 prime yields and change compared to 2019 (%)

	Bucharest	Budapest	Prague	Warsaw
Office	7.00% (flat)	5.25% (+0.25ppt)	4.25% (flat)	4.65% (+0.15ppt)
Retail	6.75% (+0.25ppt)	6.25% (+0.75ppt)	5.25% (+0.50ppt)	n/a
Industrial	8.00% (-0.25ppt)	7.00% (flat)	5.00% (-0.25ppt)	6.25% (-0.25ppt)

Source: Colliers

2020 delivered some of the poorer results for the CEE-6 region in the past decade, with total real estate investment deals dropping by a quarter over 2019, to EUR 10.4bn. That said, it was not a particularly bad year as deals could not be closed due to the overall context and uncertainties related to future revenue streams (so the global backdrop). Furthermore, on a positive note, we can note a lack of available products as well, as most owners are either long-term holders or waiting for markets to settle rather than selling at a discount, so major pivot towards distressed assets. Otherwise, yields increased quite a bit for retail assets and, to a lesser extent, for offices – as these have had a pretty good run in the last decade, while industrial assets saw some compression.

Romania Investment Market

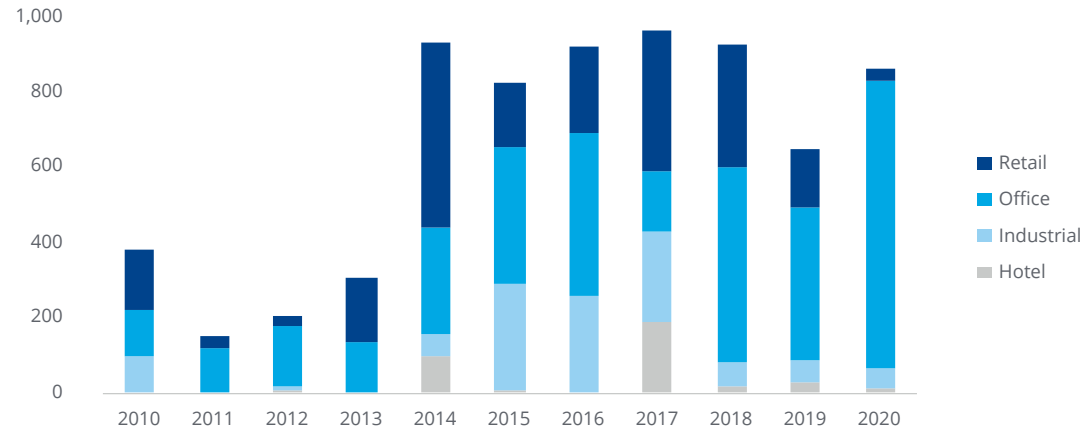
Overview

The investment market in Romania remained healthy even in the COVID-19 pandemic period with a robust market liquidity to show for; it printed a total investment volume of EUR886mn, up from EUR644mn in 2019, highlighting a 37% year-on-year increase. Given the robust pipeline at the start of 2020 (over EUR500mn in large deals in quite advanced stages), this was to be expected. Furthermore, for methodological reasons we cannot include the share deals which saw CPI Property Group purchase nearly one third of Globalworth's shares; this would have taken the overall volume to over EUR 1.2bn, making this the best year after the 2008 financial crisis.

While the result is more or less an extension of the strong business cycle that culminated in 2019, with many high profile deals started previously, there are some aspects worth cheering about. One of the highlights of this year enclosed a notable milestone: the largest commercial real estate transaction ever concluded on the Romanian office market and one of the biggest in CEE. On the other hand, limitations caused by safety restrictions and worries regarding the real estate revenue stream weighed on deals. Consequently, several other big-ticket items initiated before/ during 2020 have either been frozen, fell through or were postponed for the next year.

As another positive highlight for 2020 we want to note that Romania closed the year with a nearly double market share in the CEE-6 region, up from

Offices stole the show in terms of investment volumes in 2020 (EURmn)



Source: Colliers

4.7% in 2019 to 8.5% in 2020. This is quite an achievement that underscores Romania's potential to punch higher than its current weight in the region.

Overall, the assortment of acquisitions attained in 2020 placed Romania on the map of large strategic investors, which, in turn, has the potential to become a catalyst for further significant transactions in the future as well as contribute to increasing investor confidence.

Transactions and Investors

In terms of investment dimensions, the office sector remained the most fertile source of deal activity in 2020, conquering the market arena with a total of EUR 762mn. Two notable transactions stole the show and despite these being expected, what is even more positive is that the deals closed in the summer, after the full negative impact of the pandemic; these added up to over EUR 400mn.

The first one, the sale of the NEPI Rockcastle office portfolio to AFI Europe was the largest office transaction in Romanian real estate history, a record-breaking EUR 307mn. As a result of the transaction, AFI Europe has become the second largest office owner in Romania with a c. 225,000 m² portfolio (including the current pipeline). Another significant deal was GLL's sale of Floreasca Park to a joint venture of Resolution Property (Fosun Group) and Zeus Capital Management for EUR 105mn.

Elsewhere, a significant proportion of Romania's larger deals in the office sector involved two other transactions which accounted for around EUR55 mn each, and included the purchase of The Bridge III by Dedeman from Forte Partners and the acquisition of Global City Business Park by Arion Green from Global Finance. Another noteworthy transaction was made by the Hungarian long-term investor, Optima, which has acquired the majority shareholder (61.5%) in the Polish company GTC for EUR 116mn.

Driven by a solid tenant demand and the lockdown induced boom in e-commerce, industrial was the next most active sector, though deals accounted for only 10% of the total volume. The vast majority comes from several transactions made in Bucharest, with CTP's purchase of Equest Logistic Center for EUR 30mn as the year's biggest acquisition. That said, the supply issue on the investment side regarding I&L assets fails to show the true scope of potential demand.

Overall, 2020 saw a mix of old (including newly reactivated) and new buyers. Fosun is also a somewhat spectacular new entry as it marks the first major deal involving Asian capital on the local market and this is relevant particularly given how these investors changed the landscape in neighbouring CEE countries in the recent past. Beyond the visible news, we also note quite a lot of interest from new names which continue to look at the Romanian market even in this context (family offices rather than institutional investors).

Pricing

This past cycle, yields in Romania lagged the downward trend seen in major CEE countries, making them a bit more resilient in the current context. With regards to offices, some upcoming deals which could be closed in 2021 could see yields trend a bit lower, though for now, we believe that prime yields remained largely unchanged versus

previous quarters, at 7%. For I&L assets we can report some positive developments amid recently closed and upcoming deals, with prime yields dipping some 0.25 percentage points, to 8%. With a lack of benchmark prime retail deals, we cannot accurately pinpoint yields for this sector, but we believe that should such a deal close, it would be in the region of 6.75% (up some 0.25 percentage points over the previous year).

Funding Conditions

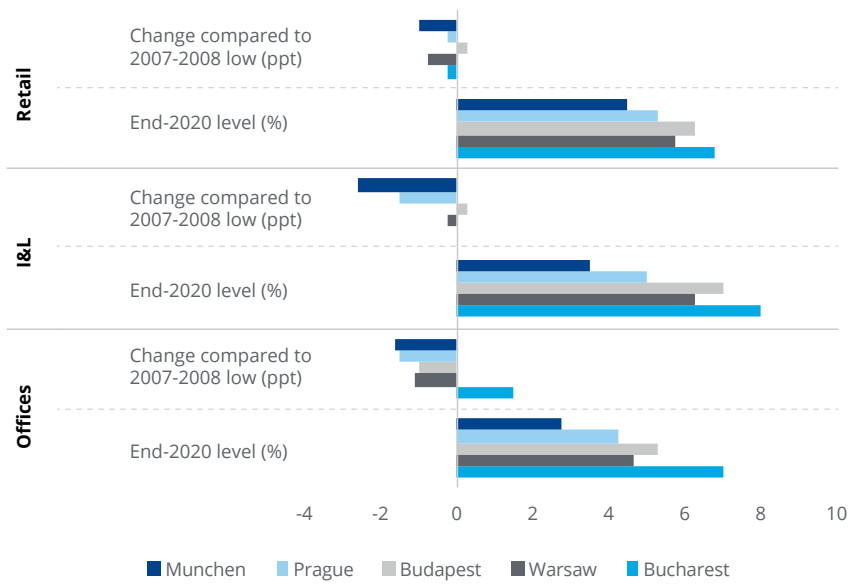
In a different take on the previous recession, this time around, funding did not disappear; in fact, liquidity remained abundant in general in financial markets globally (Romania included), despite a somewhat higher reluctance from banks towards taking on new risk during the first part of the pandemic. Otherwise, banks remained rather open to financing income generating properties and, to a lesser extent, new developments. The least preferred asset classes were hotels and retail, with a clear preference being expressed for financing projects in primary markets, especially prime standing office and industrial investments. The obtainable margin stood at around 250-350 basis points, with the low amortization period remaining tricky. However, the current environment confusion is likely to enhance supplementary downward heaviness on already flat interest rates, which will probably reinforce the taste for real estate asset class.

Forecast

While it seems unlikely that any considerable upturn is looming, the overall atmosphere for the investment market remains reasonably constructive: the private equity market is still sturdy, shy deals are being made despite the stormy landscape, funding is still willingly available and interest rates are still low. That said, given the nature of the investment market and the fact that deals can take years to close in some instances, it is likely that 2021 will look a bit worse despite the fact that activity will continue; just to give some flavour to this, we started 2020 with some EUR 500mn in big deals in due diligence, while for 2021, the start is at around EUR 150mn.

We foresee a total volume for commercial real estate transactions in excess of EUR0.5 bn and also see room for a slight decrease in yields by the end of the year, for prime office and prime industrial, but this is conditional on some pretty big 'ifs', like if the economy, political and monetary system will be satisfactory. Furthermore, we continue to see many uncertainties on the horizon for each of the big sectors which may delay deals altogether, let alone lead to yield compressions: for offices, it is about the uncertain revenue stream amid the rise of remote work on a permanent basis; for hotels, it is the decline in tourism as a whole (including business travel) which will squeeze revenues, for retail, it is about the ongoing impact of e-commerce that was accelerated by the pandemic; for I&L, it is about uncertainties related to certain manufacturing sectors that may take years to recover. Overall, while 2021 will not necessarily look bad, it will not shine as one of Romania's brightest years either.

Local assets look relatively cheap historically, which bodes well for the recovery prospects



Source: Colliers

Land Market

2020 proved to be much different compared to 2009, mostly as the market did not dry up at the first sign of trouble – with activity thawing in the second part of the year after a troublesome first half

Demand

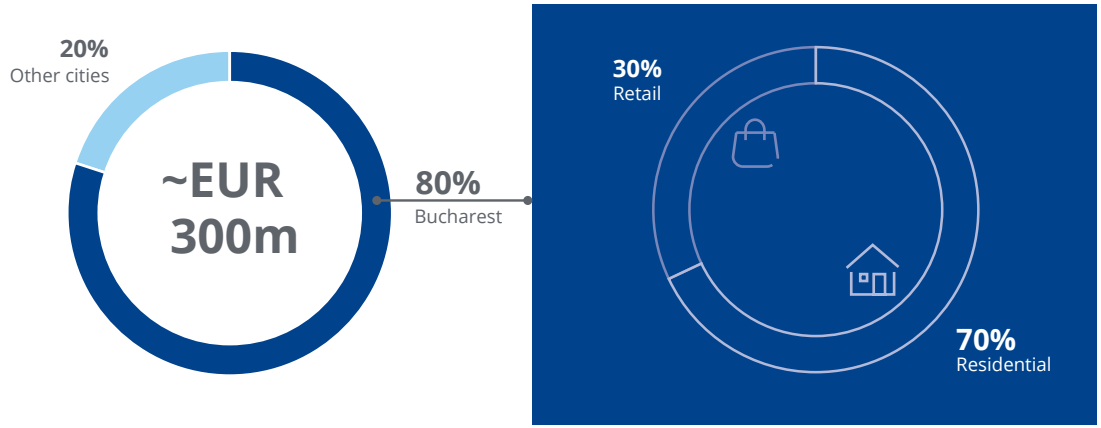
Overall activity dropped in the land market by over a quarter in 2020, but it still printed a quite decent level of slightly above EUR 300mn; the transacted land market includes, in our definition, sizeable land plots purchased with the aim of delivering residential, retail, office, mixed-use or other categories of real estate projects (and excludes industrial/logistics destination, forests and agricultural land).

However, 2020 proved to be much different compared to 2009, mostly as the market did not dry up at the first sign of trouble – with activity thawing in the second part of the year and ending the year with high volumes after a troublesome first half. That said, with two months of inactivity given the lockdown, which complicated things from a logistical standpoint, and some investors moving to the sidelines, a drop in transacted volumes was to be expected.

Bucharest continued to account for the lion's share of deals, generating close to 80% of the land deals, higher than the previous years. In turn, residential continued to account for the bulk of deals is the Capital, coming in at c.70% of all deals, with the rest coming from retail (we have had quite a few mixed-use deals, where we divided the transacted volume between residential and retail based on our insights). Other sectors had a negligible influence on land deals in Bucharest, to our knowledge. Outside Bucharest, the retail segment generated nearly three quarters of land deals.

Robust sales of apartments, even during some of the more uncertain months of the pandemic (for some, 2020 helped achieve record sales months) has propped up the demand for residential land projects.

Land deals and Bucharest sectorial split for 2020



Source: Colliers

But there are some changes: the pandemic has shifted a bit the focus in the residential market, with a rise in demand for peripheral areas (which would be good for houses or low-density apartments), near forests or lakes. Hence, we have seen quite a bit of activity in areas such as Baneasa, Pipera, Straulesti, Sisesti and Jandarmeriei, but also outside the Capital, in areas such as Corbeanca or Balotesti. Overall, demand for land plots was robust on all categories of price, but also for a fairly wide variety of projects: from those aimed at a large scale to smaller land-plots in good/central locations (with a zoning in place) for smaller projects to those aimed at villas (developers that were already active in peripheral areas, but also some coming from the central areas have shifted their attention to this type of projects).

Meanwhile, retail saw quite intense activity, though maybe some market participants were a bit more cautious. Then again, retail sales have been doing well in general in Romania – the sector saw a clear V-shaped recovery, with both food and non-food retail sales at or over pre-crisis levels; so while most shopping centers saw fewer customers, with people spending less money on clothing or eating out, others have been growing at brisk paces – food, discounters, DIY, furniture, sportswear for instance. Wholesales have also been doing quite well.

Besides some big box operators, it has been a good year in terms of demand for land plots designated for retail parks, particularly in small and average formats; this is relevant as food anchors are also scaling back their footprint. In general, developers are looking for land in almost all towns – big, average or even the smaller ones, but also in neighbouring villages/towns that are part of bigger metropolitan areas.

Meanwhile, on the office side, we did not see any major deals struck in 2020 and some buyers have, in fact, switched their projects from office into residential; furthermore, we had some sizeable office deals that remained either frozen (pending board approval) or have fallen through as developers waited for more clarity on the revenue stream post-coronavirus. That being said, most of the established developers know that this is just a phase and they remain closely watching the market for any opportunities and if a very good land plot (with exceptional location and/or attractive pricing) would appear, some would jump on the opportunity.

Supply

Supply remains adequate and in a sign of a maturing market, largely stable. We have not seen any major distressed land opportunities on the market as most owners remain solid from a financial standpoint and did not feel the need to reduce prices dramatically. In fact, we have seen cases where landowners that had been looking to sell until recently decided to develop themselves a residential project (mostly in the Bucharest outskirts). On the other hand, inexperienced developers that were owning land, amid elevated uncertainties, resorted to either selling their projects or bringing in a partner in order to share risks.

Also on the supply side, we need to mention the resellers: we note that there are instances where developers that purchased sizeable land plots, but ended up selling a small part of these (most of the times, the best position) to retailers, which paid well above market rates for the opportunity to develop a project there.

Otherwise, we still underscore that there is a good pipeline on the land market coming from former industrial platforms that can be reintroduced in the urban backdrop; these would allow for large scale projects, with a mixed-use flavor and elements that some are looking for (such as generous green areas).

Prices & Transactions

Since the year saw healthy demand, in spite of the adverse economic backdrop, we did not notice any downward trend in prices, though sellers were more open to negotiations; in fact, deals were rather closed at prices negotiated in 2019. So, while prices were, in general, stable, we have seen rare instances where retailers drove up prices by as much as 30-40% amid competition for very good land plots. These retailers also tend to have deeper pockets than residential developers in a lot of cases, so they tend to get first pick of the best locations.

On the other hand, we did not notice any major distressed land plots sold, but this is an area to keep an eye on as the negative effects of an economic downturn can cause ripple effects stretching over a couple of years. That said, such a phenomenon will likely be greatly reduced in size compared to what we saw after the 2008 Global Financial Crisis.

The year's biggest deals were generated by SIF Banat Crisana with the purchase of a former industrial platform in southern Bucharest (IMGB) for around 40 million euros and almost half of that for the purchase of another former factory in the eastern part of the city(Helitube); consequently, SIF Banat Crisana made up nearly one fifth of the 2020s land deals.

Usual asking land price intervals (EUR/sqm)

	Central	Semi-central	Periphery
Bucharest	900-3,000	250-1,000	100-450
Cluj-Napoca, Timisoara, Iasi, Brasov	350-1,000	200-400	100-250
200-300k	250-800	150-300	50-200
100-200k	200-500	100-200	50-150
50-100k	150-300	100-200	30-100

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.

2021 should see good volumes as well as most real estate players continue to see through the current recession and look at the long-term potential of Romania

Outlook

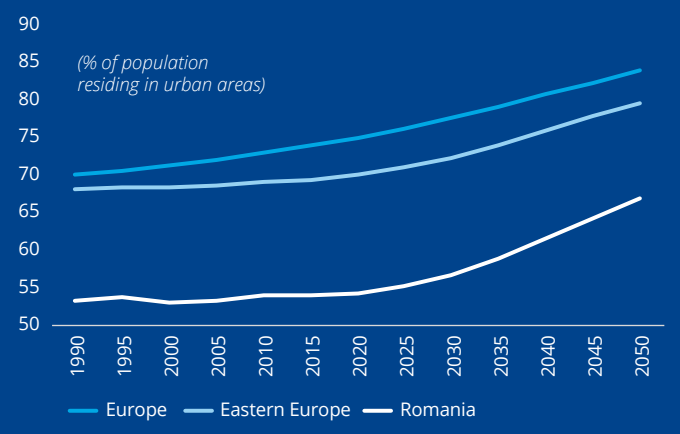
Overall, the general atmosphere in the land market is nothing like that in 2009-2010, though many developers are expected to remain on the sidelines a bit longer until more clarity appears regarding future revenues (offices, hotels); however, a recovery on these segments should only be gradual and is conditioned on constructive developments which we do not yet currently see. On the positive side, in other parts of the economy where long-term trends are holding, it is almost business as usual. We are talking here about residential – where Romania faces a significant overcrowding rate in big cities, suggesting that future supply could be absorbed – and retail – where the overall stock of modern retail facilities is lacking in large parts of the country given how fast the economy has been developing in general.

Otherwise, regarding prices, we would look for a modest price drop over the very short term as the real estate markets tend to lag developments in other segments of the economy, hence, they react with a bit of a delay. This was also highlighted by a majority of respondents in a survey we did in Q4 2020. 29% of respondents are expecting to see declines on a case by case basis (but things to remain largely unchanged in general) and another 29% expect to see more of a generalized decrease. Overall, a slightly negative assessment, which means that 2021 is shaping up rather like a breather year for the local land market following a very strong cycle up until 2020. In fact, so long as the economy remains in decent shape, we would still expect some price hikes in certain areas/for certain types of land.

Our survey also hinted that quite a lot of buyers will remain active this year, meaning that volumes should remain rather robust. In fact, given the large pipeline of ongoing deals for retail and residential projects, where closing is dependent on zoning/construction permits, 2021 should see good volumes as well as most real estate players continue to see through the current recession and look at the long-term potential of Romania.

Romania in the next decade – residential sector

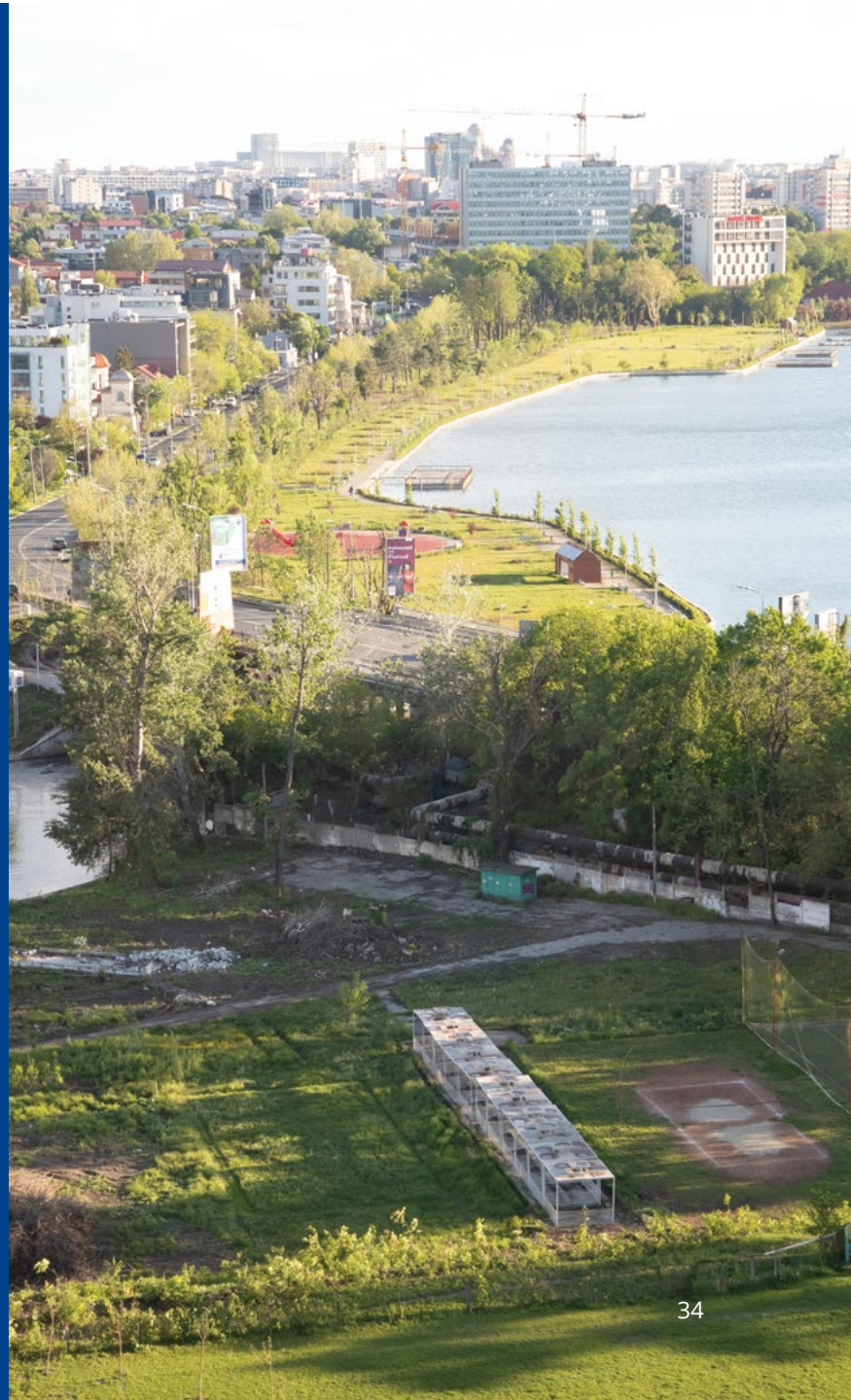
Migration towards urban areas set to start in 2020s and accelerate in subsequent decades



Source: United Nations

Special Topic

Since the residential sector is such a major driver of land market deals, we will focus on it in this thematic box. We believe that in a decade's time, the residential scene in Bucharest and some of the few lively cities in the country will thrive, as more and more people will move here for economic opportunities; if we also take into account the need to replace the very old stock, these towns should absorb a decent amount of deliveries each year. On the flipside, smaller towns and those with limited economic opportunities, as well as rural areas, ought to see a good supply of older apartments/ houses, lowering appeal for new projects. This internal shift of population will keep the residential markets attractive in certain areas even as ageing and external migration could see the overall population drop towards 18.3 million by 2030 from over 20 million in 2010; moreover, in the context of ongoing internal migration towards cities, with Romania greatly lagging urbanization rates seen in Western Europe, the population of towns in Romania will gradually increase over the next decades even as the country's population decreases.



Sustainable Buildings, Designing the Right Balance

As buildings consume the greatest share of energy, we see developers and landowners increasingly preoccupied by rethinking green infrastructure, trying to ensure a dutiful nod towards biodiversity and wellbeing.

Overview

We can consider this moment of the current global epidemic a unique prospect to shift the entire attention towards the pathway of the real estate sector and earmark investments for green development. The Covid-19 has accelerated certain tendencies such as energy performance improvement, a spontaneous digitalization imposed by social distancing approaches, new hygiene and safety protocols, restructuring of the working spaces and the use of the new technologies or gears previously integrated in the existing office buildings. As buildings consume the greatest share of energy, we see developers and landowners increasingly preoccupied with rethinking green infrastructure, trying to ensure a dutiful nod towards biodiversity and wellbeing. Just to accentuate this topic, we observe that Romanian office buildings are embracing some enticing novelties: a) Skanska's Equilibrium and Campus 6.2 were certified with the newest International WELL Building Institute rating standard that attests their adherence to top safety standards that diminish the risk of virus transmission and smoothly generate healthy and safe workplaces in the post-COVID certainty; b) Palas Iasi is the only LEED Neighborhood Development certified project in CEE, being one of only five projects across Europe to be awarded this certification. These are coming on top of the already established interest for for BREEAM (Building Research Establishment's Environmental Assessment Method) and LEED (Leadership in Energy and Environmental Design) standards, along with the more multilayered WELL certifications.

Changing perspectives and navigating towards mitigating climate change, EU leaders have committed to reducing 32.5% of the EU Member States' expected energy consumption by 2030 and earmarked an impressive 30% of the 1.8 trillion Euros budget (for the 2021-2027 period) towards climate-related spending. Therefore, in Romania, as in all other member states of the European Union, the end of 2020 brought a major change for new private buildings, whether we are talking about individual homes, multifamily blocks of flats, office buildings or other types of spaces. As a regulatory requirement, all buildings that will be built starting with 2021, must comply with the nZEW standard ("nearly zero energy building"), a consumption standard close to zero, with energy provided largely from renewable sources. The renovation of old buildings in order to bring them up to the nZEB standard is vital, as they represent the largest share of the Romanian real estate portfolio. Such changes aim to keep the same thermal comfort for a building while lowering its energy input by at least 60%, while also ensuring that a significant percentage of energy consumption must come from renewable sources such as photovoltaic or wind energy, heat pumps or heaters from the central heating system. At the present moment, the construction and operation of buildings generate 40% of all energy-related carbon dioxide (CO2) emissions, even more than transport or industry.

WELL Certifications

2020 penciled a robust activity adding a few new WELL certifications currently in advanced stages of progress: Portland Trust's Expo Business Park Office Portfolio comprising 3 office buildings and Skanska's Equilibrium Building 1.

Furthermore, 2020s addition to the market is the new WELL Health-Safety Rating standard, a score to meet and support this moment which reflects significant changes based on evolving market conditions in the context of Covid-19. This type of certification addresses to all kinds of buildings in use, is evidence-based and focuses on adopting operational policies, implementing maintenance protocols and developing contingency plans.

Equilibrium and Campus 6.2 were already certified and another Skanska project is registered to receive the WELL Health-Safety Rating certification in the near future. Similarly, Tiriac Imobiliare is the first Romanian developer which announced that it will implement the WELL Health-Safety standard for its entire mixed building portfolio, consisting of: Stejarii Residential Club 1, Tiriac Center office building, but also its projects under construction - Tiriac Tower office building and Stejarii Residential Club 2.

The subsequent points summarize what this standard means and why it is relevant in the current context:

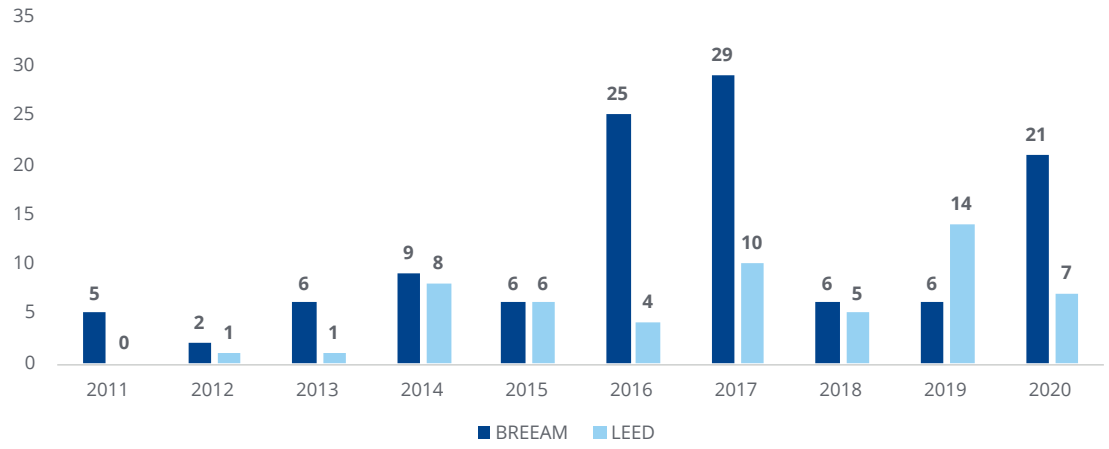
- The WELL Health-Safety Rating features are a subset of those available through the WELL Building Standard, adapted to focus specifically on facilities operations and management;
- Projects enrolled in the WELL Health-Safety Rating can elect to pursue the standalone rating or in conjunction with WELL Certification;
- The WELL Health-Safety Rating focuses on six main health-safety themes, including: Cleaning and Sanitization Procedures, Emergency Preparedness Programs, Health Service Resources, Air & Water Quality Management, Stakeholder Engagement & Communication and Innovation;
- 25 features to be investigated and minimum 15 features to be achieved in order to receive the WELL Health-Safety Seal;
- The WELL Health-Safety Seal is valid for one year from the date of issuance. The landlords and tenants must apply annually in order to demonstrate ongoing commitment to upholding operational policies, maintenance protocols and emergency plans;
- The process is shorter than the one for a typical green certification, being estimated to be completed in maximum 6 months;
- The standard is flexible and adaptable for any type of existing asset: office buildings, office interior spaces, shopping centers, residential projects, industrial facilities etc.

Green certifications

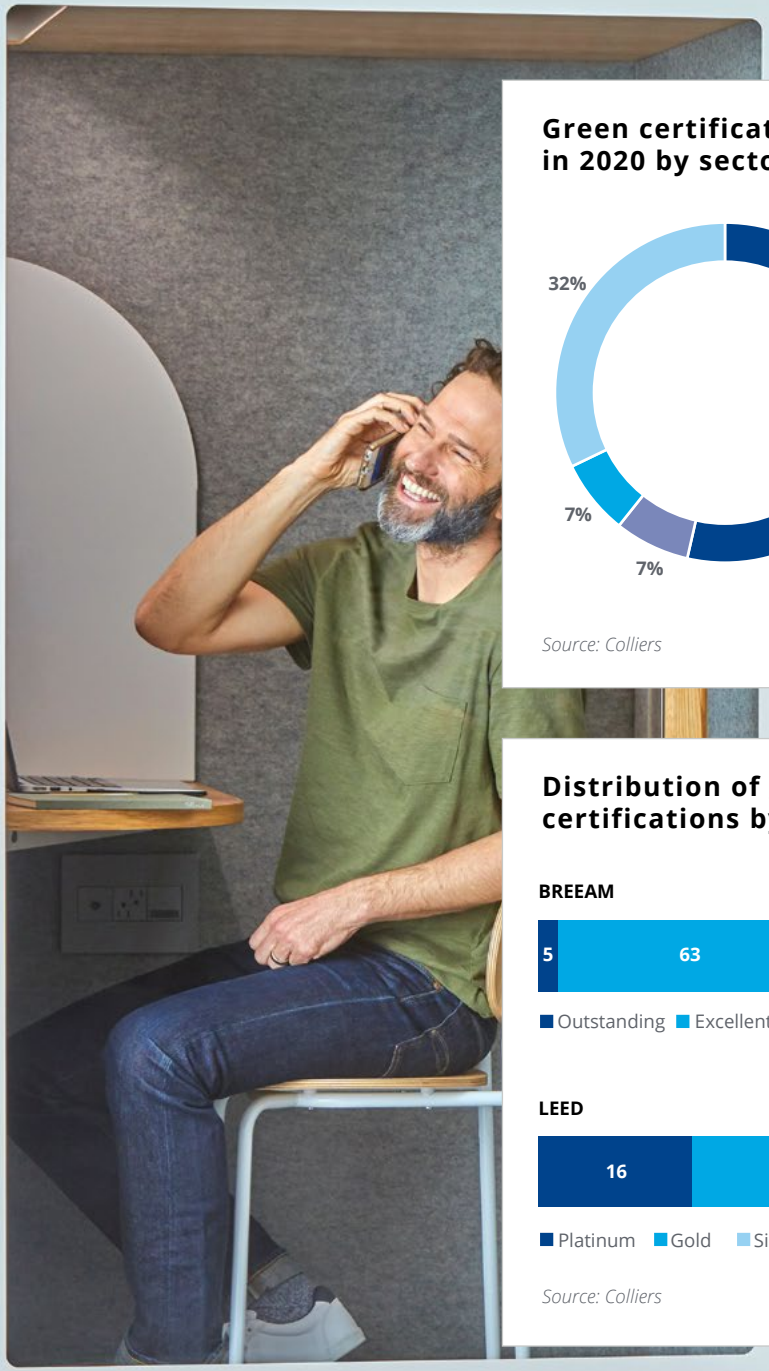
In 2020 the number of BREEAM and LEED certifications saw a slight increase, 28 versus 20 and almost triple when compared to 2018. Overall, this takes the number of such sustainable-certified projects in Romania to over 180. Nevertheless, the upward drift for renewals continues and we see ever more owners interested in renewing their sustainability certificate. Therefore, the pipeline remains fairly solid, with lots of projects planning to obtain their green certification, especially nowadays when sustainability and energy-efficiency retrofits are getting greater consideration.

Hasty urbanization predilections need community development procedures that are idyllic for green involvement and change. Neighborhoods will be the essential components of urban transformation and modernization.

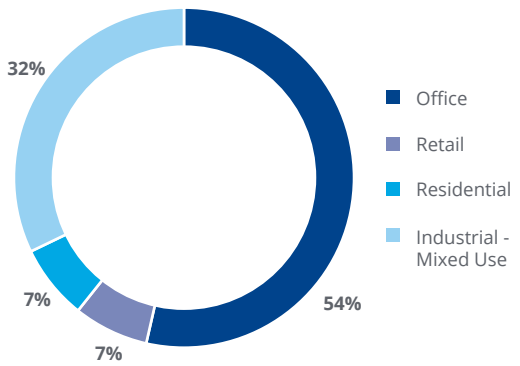
Annual number of new green certifications in Romania



Source: Colliers

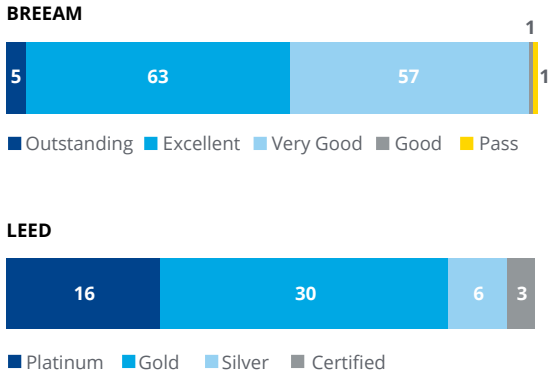


Green certifications in 2020 by sector



Source: Colliers

Distribution of green certifications by qualification



Source: Colliers

In Romania there are only two projects certified according to LEED Neighbourhood: Palas Iasi (Silver level, v2009) and City Point (Gold level, v4). In particular, LEED ND benefits are distinguished by three main pillars: scale, comprehensiveness & synergies and longevity. In other words, a sustainable neighborhood design, which pays green dividends for generations, characterized by a complete spectrum which allows unique chances to capture synergistic benefits.

Shifting angles, last year saw a downward trend with only 4 projects reaching the top LEED Platinum, down from 2019. All LEED Platinum titles were given to noteworthy office projects based in Bucharest: the first building of AFI Europe's project – AFI Tech Park, Vastint's H building of the Timpuri Noi Square, Ana Tower as well as United Business Center 3 in Timisoara. Elsewhere, last year saw several BREEAM Outstanding buildings: two of Portland Trust's developments, Vox Technology Park - Timisoara, Penny Market Otopeni and the Lidl headquarters.

Overall, the majority of certified projects are located in the capital city and its proximity - more than half, but there have been attained quite a few in regional hubs such as Timisoara, Cluj-Napoca or Iasi, with main constant accent on office, industrial and mixed-use schemes. However, we estimate that the competition among green building rating systems will intensify and there are still some large developers that may try to certify their retail or industrial portfolios, but also new entrants in specialized niches (such as office interiors) can arise.

Hotel Market

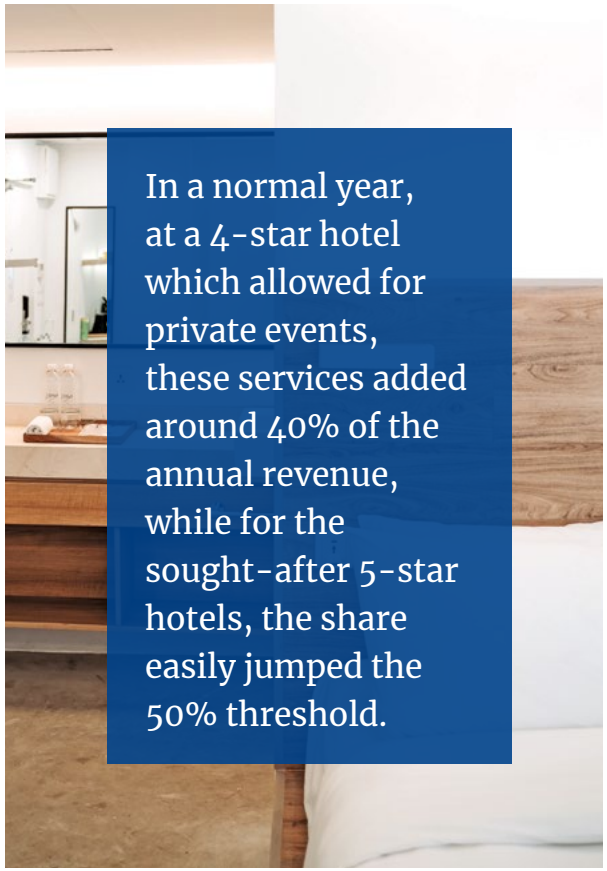
General overview

Critical worldwide responses to control the spread of the COVID-19 contagion have included various travel limitations, shelter-in-place and social distancing instructions. With millions unexpectedly out of work, ambiguity over economic retrieval, and global worries of continuing COVID-19 spread and its imminent waves, the hospitality industry was amongst the first industries affected, and it will be amongst the last businesses to recover. According to STR estimations, during September, the Euro area occupancy dropped from 43% to 39% and the ADR from 103 to 91 EUR/night/room and this downward trend remained valid until end of 2020. Therefore, substantial and swift measures have been needed to support this sector during these tempestuous times, as a stimulus to prevent it from collapse has already been supported by governments in many countries. The Romanian authorities have established a state aid scheme to compensate the losses suffered by companies in the field of HoReCa, hospitality industry and travel agencies, amounting to 20% of the turnover recorded in 2020 compared to 2019. While this will help, the road to recovery involves learning how to make the hotel experience a safer one. Wearing a mask, presenting a negative test or an anti-COVID vaccine, these are the new normal ingredients which may be needed for the tourism & hospitality industry to regain some vitality. Moreover, new benchmarks for hospitality initiatives has been set, as an outcome of the evolution at the societal level, in part as a consequence of the increased consumer awareness of all things sustainable and eco-friendly.

Bucharest hotel market

In our country, year-on-year declines remained significant in comparison with 2019. Occupancy persisted at low levels. For instance, a good 4-star hotel in central areas witnessed around 30% occupancy, versus upwards of 80% last year. In a decent scenario, the occupancy rate was supposed to increase towards 50% by year-end for established hotels, but the second wave of high number of positive tests did not allow the industry to recover. As Bucharest is not a standard summertime vacation option and is more related to the business travel scope, the occupancy rates remained low during summertime, within the same level of 10-15%. The ADR was also affected, but to a lower extent. The average ADR between June and August dropped by 20-25%, compared with the average registered last year in the same period, reaching an average of 250 RON/room/night.

Furthermore, the combined outcome of the travel limitations and government guidance on social distancing has resulted in the postponement or cancellation of many high-profile events, conferences or conventions, which directly drove down travel for business and leisure. In a normal year, at a 4-star hotel which allowed for private events, these services added around 40% of the annual revenue, while for the sought-after 5-star hotels, the share easily jumped the 50% threshold. Interestingly, newer and more flexible hotels may be somewhat more advantaged by this situation, as they tended to place a slightly lower emphasis on restaurants/events.



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The supply growth previously expected for 2020 was impossible to meet the initial forecast and was partly delayed for 2021, Bucharest seeing only two significant large hotel deliveries: Ibis Style City

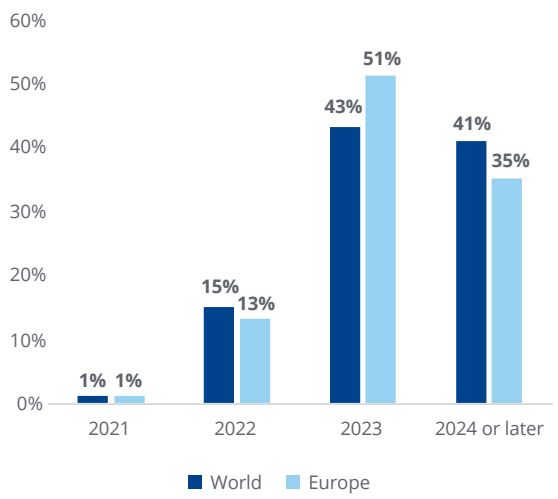
Center, of 150 rooms, located on the Stirbei Voda street, was the first hotel opening in Romania during the pandemic and Moxy Bucharest Old Town with another 117 rooms was completed in a dominant ultra-central location.

General trends and forecasts for hotels in Romania

Considering the market history before the pandemic period, we are optimistic about the capacity of the market to recover and that the investors' interest in this market will again come back in time (though the next few years will certainly prove difficult ones). The developers continued their hospitality projects and found ways to negotiate with the financing banks. Even during pandemic, the novelty of the Moxy brand, for example, succeeded to create an occupancy of 20-30% during weekdays and of 45-50% during weekends. In terms of future pipeline, in 2020, the Accor chain signed a new management agreement with Alexandra Residence Designed for construction of a new hotel under Ibis branding, including 144 rooms, SPA and an event center of 1,000 sqm. The hotel is situated in Tunari, adjacent to the airport and to the future new subway terminal. The project was planned to open its gates in 2022 but due to the international pandemic situation, some delays are expected. Moreover, by the end of 2021 we expect to see the opening of Ibis Airport (85 rooms) and the new luxury hotel Autograph Collection in Bucharest's Old Town (215 rooms), as they are in an advanced stage of development. Projects like Indigo (100 rooms) or Corinthia (50 rooms) or the reconversion of Oscar Maugsch Palace, recently sold by BCR to a group of investors in the hospitality industry, who are yet to announce their strategy.

Either way, the medium-term outlook remains challenging. Globally, tourism has fallen in 2020 to a 30-year low in terms of activity. The World Tourism Organization within the United Nations (UNWTO) published recently the results of a survey: in Europe, most tourism experts are seeing the return of activity to pre-pandemic levels of international travel no sooner than 2023. Furthermore, the survey also mentioned that a more material recovery in international travel should come in the second half of 2021, but quite a few see this as rather a 2022 event. We would expect Romania to follow suit and rebound at a similar pace to other European countries. And while Romania as a whole did not rely that much on foreign tourists (the country had one of the lower numbers of international visitors in CEE), Bucharest will suffer, as it did see an increasing amount of both business and leisure tourism in the run-up to the coronavirus pandemic.

When will international travel recover to pre-pandemic levels (% of responses)



Source: UNWTO

> In Europe, most tourism experts are seeing the return of activity to pre-pandemic levels of international travel no sooner than 2023.

The epidemic has fundamentally changed the customer experience, and certain types of travel, like summits, which may never fully return to pre-pandemic levels. As it will take some time for international business travel to recover, local tourism will continue to play a significant role more than ever. Operational changes, particularly related to health, cleanliness and flexibility and the use of outdoor spaces will become key. New hospitality services and asset management, digitalized guest experiences and increased use of contactless technology, sustainability, automation and technology gained their momentum and 2021 will bring fresh trends in the hospitality area. Furthermore, a concentration on minimizing food waste, substantial promotion of vegan choices and locally produced products and a proactive interest for smart devices planned to diminish energy consumption are just a few trends intended to shape a more sustainable future starting 2021. The core essentials circle around reducing waste, saving energy, and cutting down on water usage.

Questions for the Romanian Real Estate in the Next 10 Years – a Legal View


Oana Bădărău, Francisc Peli
PeliPartners

The past 12 months have been a test as to how the Romanian real estate market would react to a crisis and how resilient and solid its fundamentals are.

We can now safely say that – given the size and the sheer volume of transactions signed, closed, or pending – the interest of institutional investors for the Romanian assets remained unchanged and is expected to further materialise in the years to come. As sophistication and complexity increases among investors and proposed deal structures, one would think that there is an effort of the authorities to bring the Romanian legal framework in line with Western standards for investments – at which point we advise you to take a closer look to the specifics of the market.

Here are some issues which will turn out to be relevant irrespective to the type of real estate transaction you will aim to implement in Romania.

1. Will the burden of residual title issues finally be lifted?

More than thirty years elapsed since the end of the communist regime and more than fifteen years after the deadlines for submitting claims under the special restitution laws. Nonetheless, Romania is still struggling to clean up property matters and solve restitution claims in what seems a textbook example of procrastination.

To make matters worse, information on claims is scattered between multiple authorities and difficult to obtain. The standard legal due diligence process now developed to include sending close to twenty different letters to various authorities for each property.

In Romania, validity of title depends on validity of previous titles. The good faith defence is relevant only to the extent it is preceded by due and proper due diligence. The standard (particularly) for institutional investors is very high and that puts potential acquirers in the position of investing a considerable amount of time and money in the pre-acquisition checks.

Even with a couple of months allowed for due diligence, sometimes deals end up being subject to conditions precedents which relate to obtaining confirmatory letters from authorities or, more often lately and almost as a standard requirement, to obtaining title insurance coverage – all to deal with title risks which cannot be addressed otherwise in due course.

2. Will land book registration finally amount to proof of title?

Checking the registration of the ownership right of the current and previous owners with the Land Book represents an important step in all real estate due

diligence reviews. Ownership rights (as well as other real estate related rights) must be registered with the Land Book to be opposable against third parties.

However, land book registration is not absolute proof of ownership and validity of current title still depends on the validity of previous titles.

Following the entry into force of a new Civil Code ten years ago, the effect of land book registrations should have changed, for the registration to become a condition to the actual transfer of rights over real estate. However, this new effect of land book registrations will come into play only after the cadastral works are completed for each administrative unit (city or village). Until completion of the cadastral works, land book registration will continue to be performed for opposability purposes only and potential acquirers will still be unable to rely (solely) on land book registration.

3. Will urban planning finally become coherent and predictable?

With NGOs and private individuals becoming more aware and involved in urban planning matters, case law on challenged urban plans has expanded, along with the odds of vulnerabilities in the process of preparing and/or approving an urban plan being speculated by third parties. Much to the surprise of anyone not familiar with the local market, not only that challenges have been aimed at urban plans prepared by authorities themselves, but some of such challenges were also successful. When the annulled urban plan regulated a large area, private investments may also be affected, despite the investors themselves having done nothing wrong.

One of the basic rules in urban planning concerns the hierarchy between various types of urban plans: each plan must observe the higher-ranked ones, while changes are allowed only within specific limits. Nonetheless, corelation is not always achieved and that puts developments at risk. Most of the times, flaws cannot be cured otherwise than starting the whole process over.

Legislation on terms for challenging urban plans is particularly complex and prone to a variety of interpretations, which leads investors needing proficient legal advisors to grasp the severity of potential issues.

Transactions are often subject to urbanism considerations – as ultimately urbanism is a matter of permitted use and (via building permits) title to buildings. The real estate legal industry for many years focused its due diligence efforts on issues related to title to land but has now started to develop more capabilities in assessing urbanism matters. Urbanism is no longer the exclusive backyard of architects. This sometimes brings the two professions to collide upon various urbanism issues, as lawyers are more conservative in interpretation while architects deal more often with local authorities.

Any future legislative changes will need to bring more clarity and coherence so that the two worlds – formal and functional – are not disconnected and in permanent struggle.

4. Will business transfers become the norm?

For a long period of time, transactions with operating assets have been structured almost exclusively as share deals. Share deal are more straight forward to implement and incapsulate the initial planning of the developers in view of an exit.

However, in recent years larger transactions turned increasingly into business transfers – firstly to give prevalence to asset valuation and secondly to eliminate as much as possible the risk of past operation.

Once properly prepared and diligently planned so as all elements to be transferred are taken into consideration, structuring a real estate deal as a business transfer in Romania seems like cherry-picking the "pro's" column from both share deal and asset deal structures. In respect of single asset transactions, we expect business transfers to become more like a norm and share deals to remain an exception; in portfolio transactions share deals are expected to be largely used going forward.

About PeliPartners

A team specialising in complex projects that require innovative approaches, PeliPartners have a wealth of experience in a variety of fields, including mergers and acquisitions, financing, competition, infrastructure & concessions, energy, real estate and corporate law - being involved in some of the landmark real estate transactions on the Romanian market for the past 20 years. More details about PeliPartners may be found on www.pelipartners.com.

At a Glance - Real Estate Taxation Today

Alex Milcev
Partner at Ernst & Young,
Head of Tax & Law

	Capital gains	Dividends	Rental income	Real estate sale
Corporate income tax	16%/0%*	5%** (withholding)	16%	16%
Value Added Tax			VAT exempt with option to tax at 19%	5%, 19%, VAT exempt****
Income tax (individuals)	10%	5%	10%	3%, applicable to the amount exceeding RON 450,000
Social charges	YES***	YES***	YES***	NO
Property taxes	The annual local tax for non-residential buildings ranges between **0.2% and 1.3%** applicable to the taxable value of a building as at 31 December. Moreover, a higher building tax rate of **5%** is applicable for buildings owned by companies which are not revalued for more than 5 years. For residential buildings the tax is between **0.08% and 0.2%.** The annual land tax is established by taking into account the surface of land, the rank of the locality where it is situated, as well as the area and/or its category of usage, as established by the local council. In case of real estate transactions, certain Notary and Real Estate Register fees apply (in total approximately **1%**, depending on transaction value).			

Footnotes:

**In certain situations (i.e. participation exemption regime or tax treaties), sale of shares held in Romanian companies may be exempt from tax in Romania.*

***This rate could be reduced based on tax treaties or EU Parent-Subsidiary Directive.*

**** The health fund contribution is due only if the cumulated private income, other than salary, would exceed the value of 12 national minimum gross salaries (i.e., RON 27,600 for 2021). If so, the health fund contribution due is capped at RON 2,760/year.*

***** The 5% reduced VAT rate applies for supplies of social housing under the threshold of RON 450,000, exclusive of VAT, a maximum useful surface of 120 sqm. The VAT exemption can be applied in case of old buildings or non-building land (potentially subject to VAT adjustments).*

Deductibility of financing costs

A corporate income taxpayer's exceeding borrowing costs (i.e. the amount by which deductible borrowing costs exceed taxable interest revenues) in relation to various types of financing (including e.g. bank loans) may be deducted for corporate income tax purposes up to 30% of the company's EBITDA, adjusted for tax purposes. This EBITDA limitation will be applied to those exceeding borrowing costs which are above an annual threshold of EUR 1,000,000 (i.e. the first EUR 1,000,000 would not be subject to the limitation).

Micro-enterprise tax regime

Under the current Romanian tax legislation a company may fall under a corporate income tax regime, or a microenterprise tax regime. Under the micro-enterprise regime, the taxpayer is subject to 1% (or 3% tax in case of no employees) - applied to the revenues derived.

A micro-enterprise will switch to the standard corporate income tax regime if during the course of a tax year, it obtains revenues higher than EUR 1million. Moreover, if the taxpayer has a minimum share capital of RON 45,000 and at least 2 employees, it will be able to opt to apply the corporate income tax regime instead of the micro-enterprise regime.

Emerging Trends in Real Estate Taxation

How 2021 and beyond will look like from an investment point of view and what the players in the field should expect. Top 10 tips from EY specialists.

Tax consolidation. The long-awaited measure, endorsed by other countries for some time now, has been recently adopted into our domestic legislation. A tax consolidation for corporate income tax purposes will be available for taxpayers starting with 1 January 2022. In short, companies belonging to the same group will be able to consolidate their positions of profit and loss and owe tax only on the consolidated profit of the group. This will allow the recovery of tax losses in real time, by compensating them with the profit made by other companies in the same group. For larger real estate players this is certainly a relief, since their projects are frequently done via separate companies that make losses in the first year(s).

Property tax. Despite the ongoing growth of the real estate properties prices in the last years, the tax cost of acquiring, and most importantly maintaining, a house is significantly lower in Romania than in many western countries. These differences are rooted in Romania's turbulent economic and social history of last decades. The current system of tax rates was partially harmonized years ago to diminish the discrepancies between corporate landlords and individual landlords. Still the differences persist, e.g. in how the taxable base is determined or in frequent disconnect between such base and real market value of properties.

In the future, there will be a trend to reduce such discrepancies to the highest common denominator. In addition to this, considering high pressure on public finances and gaping budget deficits in the years to come due to covid-19, it is increasingly possible that for a longer-term, the legislator may consider increasing the effective tax cost on properties. So, the favorable tax gap with more expensive countries may shrink over time.

Sale of shares. Under the Romanian law, the sale of shares is an exempt transaction provided some conditions are met (i.e minimum holding of 10% for 1 year). As Romania needs to stay competitive internationally and preserve its level of attractiveness for the investors, we consider that these measures will not be altered in any near future.

Rental income investment. Rental income is an increasingly important revenue source for many individual property owners. In Romania, due to the standard 40% deduction, the income tax rate is actually reduced from 10% to 6% for all owners of 1-5 properties. This situation changes when the property owners offer for rent more than 5 properties, since such income would fall under the "independent activities" income category and therefore different taxation rules would apply.

Airbnb (and like). The recent changes brought to the tax law provide for the taxation based on the tax "norm" for individuals who derive rental income from up to 5 rooms (rentals for tourist purposes, for any period between 24 hours and 30 days, during a calendar year). The new legislative framework, complexity of the reporting for the rentals over 30 days, along with the travel bans, will likely have adverse consequences on the Airbnb landlords in the following year. However, after that, we believe the simpler rules for this innovative industry will make life of landlords easier.

Future of the individual taxation. Currently, in Romania we have a flat personal tax rate of 10%, which is very attractive. However, given the economic environment and low levels of tax compliance, periodically some governments have debated the merits of moving to progressive tax system, implying introduction of the tax free bands, along with the progressive tax rates.

While the governing coalition has pledged not to increase any taxes in 2021, we consider that this idea may have a come-back in the near future and that Romania might join other European countries already using such system.

VAT – a Real (estate) Perspective. Taxable supplies of land and buildings are subject to reverse charge, provided that both the supplier and beneficiary are VAT registered in Romania. Thus, the parties do not need to prefinance the VAT.

In case a landlord decides to apply the VAT exemption for rental services, as a principle, the input VAT incurred in relation to that real estate should be adjusted (returned to the state budget at landlord's expense). However, the adjustment is not done all at once, but yearly for each of the years left of the 20 years VAT adjustment period. Thus, the landlord would not need to incur the entire VAT adjustment cost in a single year.

Real estate investments placed on hold for objective reasons should not trigger negative VAT consequences. However, our experience during tax audits demonstrates that the tax inspectors require a minimum evidence of the intent of the taxable person (e.g. a real estate developer) to carry out economic activity, such as e.g. contracts with real estate agencies for the sale/rent of the investment, etc. Documenting this intention is essential in order to benefit of VAT deduction right.

VAT deduction related to holding companies. Based on settled case law of the European Court of Justice (ECJ), pure holding companies are not taxable persons from a VAT perspective. However, recent developments at the level of the ECJ in the case C-320/17 Marle Participations shows that a holding company which involves itself in the subsidiaries' management by letting them a building should be capable of being deducted in full. Involving the holding company in economic activity could allow VAT deduction right for costs such as legal fees, due diligence fees etc. at the level of the holding company. And this may imply material tax savings over a long term.

Joint tax audits. One of the recent practices at the level of the European Union - joint tax audits across borders – could foretell an improvement on how tax disputes are resolved by the competent authorities. In Romania, we have already the legal framework in place for such measures, which, on the long term, could indicate a stronger collaboration of the Romanian tax inspectors with their cross-border colleagues. This will put increasing pressure on multinational players in terms of overall compliance costs and more internal coordination effort than it is today.

Common Consolidated Corporate Tax Base. By now, the EU Commission initiative for a common corporate tax base and a common consolidated corporate tax base is well known and anticipated by many. The Commission's intention is to standardize the rules for computing the taxable profit across the EU member states. The proposal was first introduced in 2011 and reinforced in 2016 without finding its way into a new EU Directive so far. Nonetheless, we do not rule out the possibility that this initiative to be resumed, along with many other tax ideas that are evolving at record speed at EU level in the last years.

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