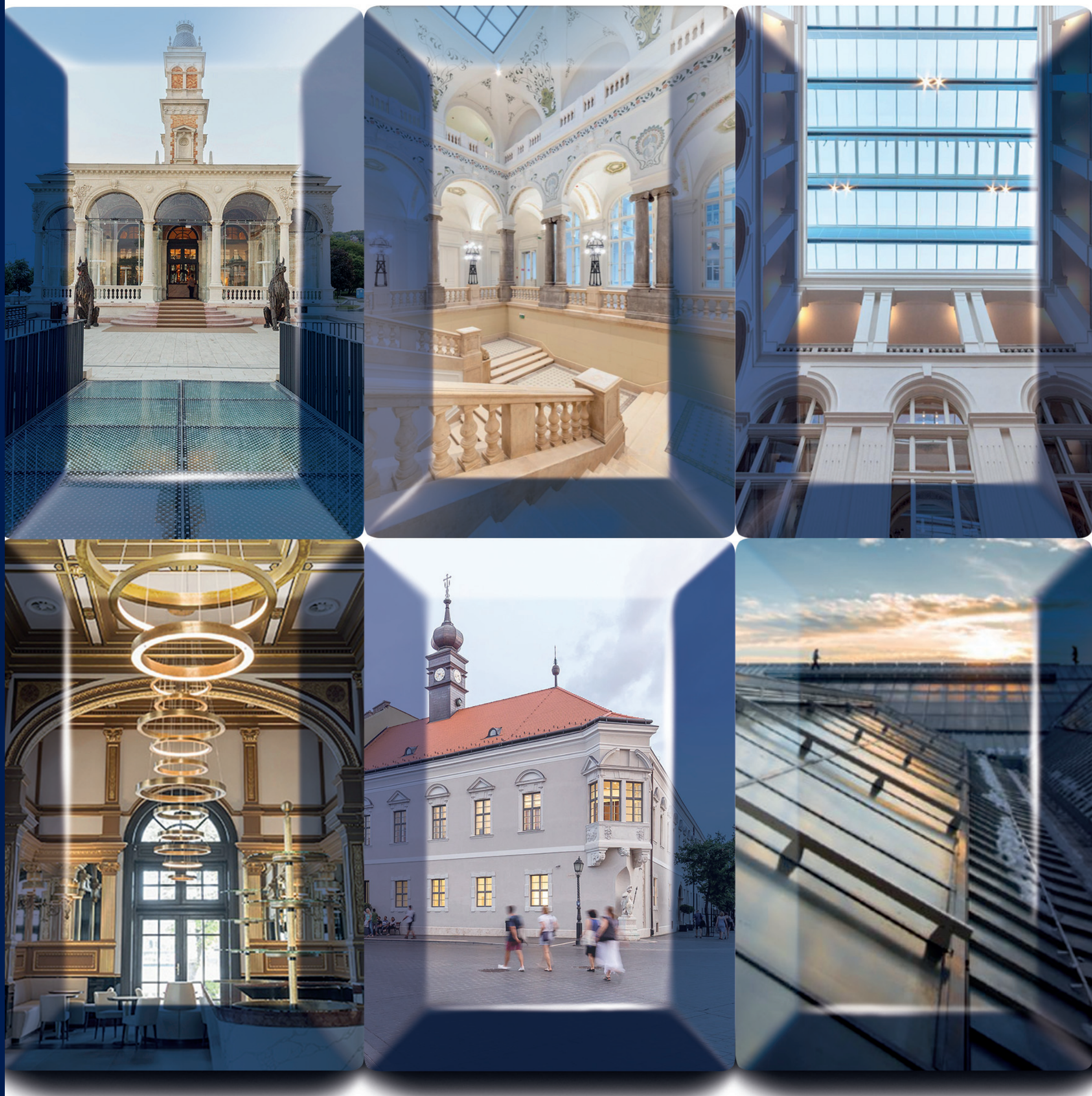
COMMERCIAL REAL ESTATE MARKET REPORT



2024

OCTOBER

"Your actions preserve you for the future."

Miklós Ybl

COMMERCIAL REAL ESTATE MARKET REPORT

2024

OCTOBER

Published by the Magyar Nemzeti Bank

Publisher in charge: Eszter Hergár

H-1013 Budapest, Krisztina körút 55.

www.mnb.hu

ISSN 2676-8755 (print)

ISSN 2676-8747 (on-line)

The commercial real estate (CRE) market is of key importance, as it influences all economic sectors and also plays a role in people's everyday lives. In light of this, the Magyar Nemzeti Bank analyses developments on the CRE market in this biannual report.

The following two factors are crucial to the analysis of commercial real estate:

I. On the one hand, commercial real estate is a fixed asset used by economic agents as a production factor; therefore, its value is influenced by the interplay of supply and demand for this asset.

II. On the other hand, commercial real estate is an investment vehicle: investors purchase such assets to realise a yield premium – over and above the available risk-free return – on the cash flow from utilising the real estate and/or the increase in value, while taking extra risk in the process.

Consequently, in addition to supply and demand trends, investor expectations are a key determinant in the value of commercial real estate, similarly to financial markets. Furthermore, developments on the CRE market also affect the functioning of the financial system. This is primarily due to the fact that a large portion of credit institutions' corporate loan portfolios are comprised of CRE-collateralised loans, accounting for almost 40 per cent of these portfolios in Hungary.[1]

As such a large amount of bank assets are CRE-collateralised, there is a strong relationship between CRE values and the credit cycle. During an economic upturn, a positive feedback loop may develop between rapid growth in real estate values and lending, which can lead to excessive lending and fuel borrowing for real estate speculation. In an economic crisis, banks' non-performing loans burden the institutions' capital adequacy, resulting in a reduction in credit supply. As seen in the 2008 crisis, the commercial real estate market plays a major role in banks' pro-cyclical behaviour. Moreover, corrections in CRE prices affect future investments and thus the real economy, which influences the operating environment of banks. A decrease in commercial real estate values generates losses for banks and institutional investors with large CRE stocks and contributes to financial instability.

Consequently, the CRE market can negatively affect the stability of the financial system via multiple channels, and thus it is of the utmost importance for the Magyar Nemzeti Bank as a macroprudential authority to monitor and thoroughly analyse the commercial real estate market.

The Commercial Real Estate Market Report aims to provide an overview of the underlying economic developments and the system of interactions between economic agents. Consequently, this Report represents a unique central bank publication at the international level, due to its integrated presentation of the macroeconomic and financial stability aspects of the CRE market. The set of information used by the publication includes the following:

- *The presentation of the macroeconomic environment influencing the CRE market is based on the information in the MNB's Inflation Report.*[2] *Key statistical variables relevant to the CRE market include changes in the volume of gross value added, employment trends, changes in retail sales and changes in the yield environment.*

- *The analysis of current commercial real estate market developments relies primarily on data provided by real estate consulting firms and information from meetings of the Housing and Real Estate Market Advisory Board. Developments in the commercial real estate market are analysed by market segment (office market, retail market, industrial-logistics market, hotel market), but due to the capital city-focused market structure the bulk of the data is limited to Budapest. A micro-database is available to monitor construction projects.*

- *The analysis of the CRE financing market relies primarily on balance sheet data from credit institutions, the interest statistics and granular, loan agreement level loan data collected by the MNB; information on the qualitative features of lending developments collected in the Lending Survey*[3] *is also used.*

[1] In addition to project loans secured by commercial real estate, this also includes classic corporate loans to which mortgage on commercial real estate was provided as collateral.
[2] Magyar Nemzeti Bank, Inflation Report https://www.mnb.hu/en/publications/reports/inflation-report
[3] Magyar Nemzeti Bank, Lending Survey https://www.mnb.hu/en/financial-stability/publications/lending-survey

Contents

List of Boxes

1 Executive Summary

In 2024 H1, yields stopped rising in the commercial real estate market, but lower-than-expected GDP growth was not yet able to significantly support domestic CRE activity. This is also reflected in the cyclical perception of the market, with the proportion of market professionals who believe that the market hit the bottom of its cycle was nearly two-thirds, while further 19 per cent already indicated upturn phase in the July survey by the Royal Institution of Chartered Surveyors (RICS). Looking ahead, faster and broader-based GDP growth may mitigate cyclical risks, but some segments will continue to face challenges stemming from structural changes.

Among the CRE segments, the performance indicators of the hotel sector improved, mainly due to foreign guest stays, but in conjunction with rising real wages the number of overnight stays by domestic guests also increased year-on-year in 2024 H1. In line with the improving trend in consumer confidence, retail sales rose and vacancy rates in this segment also improved, both in rural areas and in the capital's shopping centres. From 2025 onwards, we expect that some of the deferred investment projects will begin and external demand trends will start to improve, leading to more balanced growth with positive effects on demand in all CRE segments.

The vacancy rate in the Budapest office lease market rose by 0.6 percentage point to 13.9 per cent in 2024 H1, while the industrial-logistics market recorded a decline of 0.1 percentage point to 8.5 per cent. Given the levels of demand seen in recent quarters and the amount of new floorspace slated for completion, the indicator is expected to rise further in both segments. The volume of office space under construction increased in 2024 H1, mainly due to the start of construction of several owner-occupied office buildings during the period, including a number of office buildings for public institutions. The pre-lease rate for new space planned to be completed in 2024 H2 was 77 per cent in the office segment and 64 per cent for industrial-logistics projects, higher than in the previous two years, which should ease the upward pressure on higher vacancy rates. However, in light of the net absorption figures for the office and the industrial-logistics segments in the first half of the year, there is still a risk of oversupply.

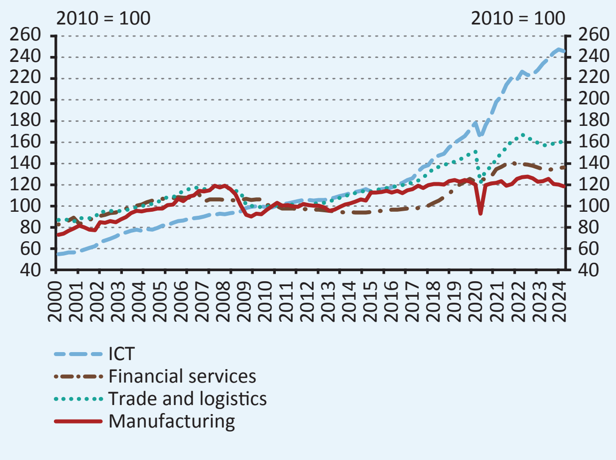
In 2024 H1, investment turnover on the domestic CRE market amounted to around EUR 180 million, down 21 per cent on the already low level from 2023 H1. Rising yields, still high financing costs in euro and subdued rental demand continue to encourage investors to wait, portending low investment flows for 2024 as a whole. In contrast to the domestic trend, average investment turnover in the CEE region already increased by 35 per cent, while the prime office yield (on real estate at prime locations and of the highest quality) stagnated. With investment flows in Czechia and Poland also expected to rise substantially for 2024 as a whole, the potential persistence of continued low and declining domestic investment turnover with high, 79 per cent proportion of domestic investors may pose risk to the perception of the domestic market. Capital values calculated on the basis of prime office yields and rents decreased by an average of half a per cent in the CEE region and 3.6 per cent in Budapest in 2024 H1, with cumulative depreciation of 14 and 24 per cent, respectively, over the past two years. However, with low investment turnover in all markets, this estimate is uncertain.

In 2024 H1, banks disbursed 37 per cent more CRE-backed project loans compared to the low base from one year earlier, with 80 per cent of the period's disbursements related to construction loans. Except for hotels and other real estate, all property types showed an increase in the volume of new loans. However, risk aversion continues to dominate market perceptions. According to the MNB Lending Survey, banks tightened lending conditions mostly for office buildings in 2024 Q2 and they plan further tightening in 2024 H2, citing changing risk tolerance and industry-specific challenges. Overall, the exposure of domestic credit institutions to project loans backed by CRE is less than half of the post-2008 crisis level in terms of both balance sheet total and own funds, and there has been no significant deterioration in the share of non-performing loans in the portfolio. In October 2023, due to potentially rising risks in the CRE market the MNB's Financial Stability Board reactivated the Systemic Risk Capital Buffer (SyRB) in a revised form for preventive purposes from July 2024, which was suspended for an indefinite term following the outbreak of the coronavirus pandemic.

2 Office Market

In 2024 Q2, gross domestic product expanded by 1.5 per cent year-on-year, but the value added of the service sectors which are important for CRE demand showed mixed results: in ICT, value added rose by 3.1 per cent and the financial sector's values added rose by 2 per cent, while that of manufacturing fell by 3.1 per cent. Gross domestic product is expected to expand by 1.0–1.8 per cent in 2024, driven by household consumption and net exports, while declining investment will restrain GDP growth. In 2024 H1, gross rental demand in the Budapest office market rose by 21 per cent year-on-year and was only 4 per cent below the average of the 2018 H1–2019 H1 levels before the coronavirus pandemic. This is nuanced, however, by the fact that the share of lease renewals in the composition of gross demand has increased substantially over the past four years, reducing net market absorption. In 2024 H1, net market absorption was positive, but not sufficient to offset the impact on underutilisation stemming from the vacant spaces from completions and lease expiries. The vacancy rate in the Budapest office market was 13.9 per cent at the end of June 2024, reflecting an increase of 0.6 percentage point versus end-2023, but this vacancy rate is not exceptionally high by historical standards. Based on data on ongoing development projects, 96,000 square metres of new office space is expected to be completed in 2024 H2. Completions and low market absorption are anticipated to further increase the vacancy rate, which may exceed 15 per cent by the end of 2024, and, given the net market absorption data from recent quarters, there is a risk of additional oversupply. The volume of office space under construction grew in 2024 H1, mainly due to the start of construction of several owner-occupied office buildings during the period, including a number of office buildings for public institutions, which account for nearly half of the total space under construction. In Central and Eastern European capitals, office space equivalent to 2 to 10 per cent of the total space is under construction, with Budapest at the top of the scale with a figure of 10 per cent.

Chart 1
Performance of sectors relevant to the CRE market



Note: Seasonally adjusted data. ICT refers to the information and communications technology sector.

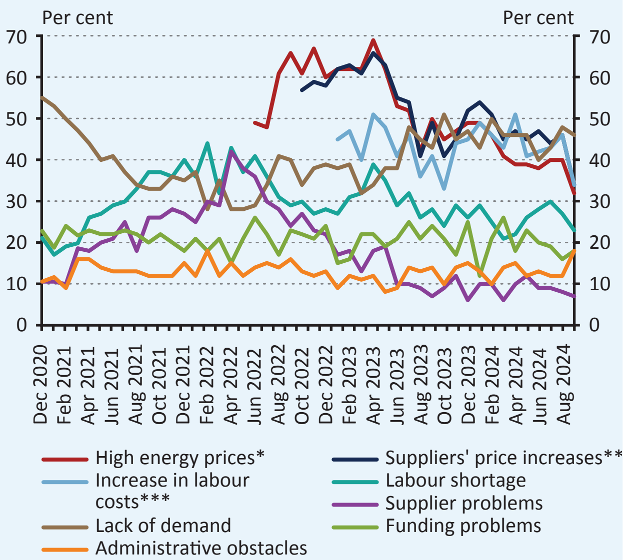
Source: HCSO

The output of the sectors most relevant to the CRE market grew in 2024 Q2, with the exception of manufacturing. Based on raw data, relative to the same period in the previous year, gross domestic product increased by 1.5 per cent in 2024 Q2, while it fell by 0.1 per cent in quarter-on-quarter terms. On an annual basis, GDP grew by 0.8 per cent in the European Union and by 0.6 per cent in the euro area in the second quarter. Of the main economic sectors, services and construction boosted year-on-year GDP, while industry and agriculture reduced it. Industrial output fell by 2.4 per cent, with value added in manufacturing down 3.1 per cent (Chart 1). The output of the sectors most relevant to the CRE market, aside from manufacturing, increased in the second quarter: ICT grew at a year-on-year rate of 3.1 per cent, with growth of 2 per cent in the financial sector and 3.1 per cent in trade and logistics.

Gross domestic product is projected to expand by 1.0 to 1.8 per cent in 2024.[4] Economic growth in 2024 may be supported primarily by private sector services. Looking at expenditure, household consumption and net exports are the main contributors to GDP growth, while investment, which fell sharply due to the unfavourable business climate, is retarding growth. Consumption growth is supported by rising real wages and historically high employment.

[4] Magyar Nemzeti Bank, Inflation Report, September 2024. Available at: https://www.mnb.hu/en/publications/reports/inflation-report/26-09-2024-inflation-report-september-2024

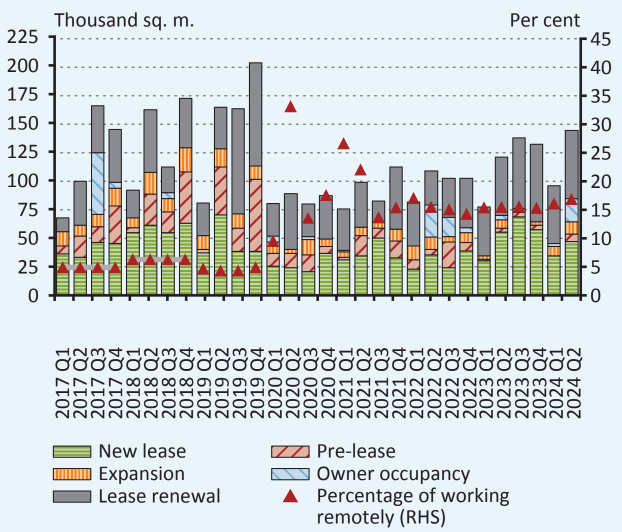
Chart 2
Factors hindering production growth



*Note: *This answer option has been included in the survey since June 2022. **This answer option has been included in the survey since October 2022. ***This answer option has been included in the survey since January 2023.*

Source: MNB corporate business sentiment survey

Chart 3
Demand in the Budapest office market and the ratio of employees in intellectual occupations working remotely



Note: The 3-month moving average of employees aged 15–74 working remotely at home as a percentage of those in intellectual occupations. For each quarter of 2017 and 2018, the annual rate of working remotely is shown; no quarterly data are available for these years.

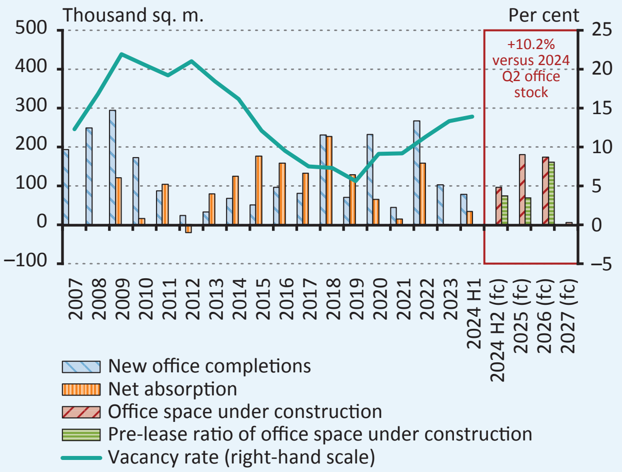
Source: CBRE, Cushman & Wakefield, HCSO

Domestic household consumption is in line with the regional pattern, while investment is underperforming in a regional comparison. Some of the deferred investment projects may commence and external demand trends may improve from 2025, contributing to more balanced growth and exerting a positive impact on demand in all CRE segments.

Lack of demand and the lingering effects of the period of high inflation are the principal obstacles to companies' production. In the MNB Business Sentiment Survey of September 2024, companies cited the lack of customers, price hikes by suppliers and rising labour costs as the main constraints on production (Chart 2). Supplier problems (delays and product shortages), funding problems and administrative barriers were the least mentioned by companies in the survey. According to a survey published by the European Commission (ESI), insufficient demand is also the chief obstacle in the construction sector, which is of key importance for the real estate market (Annex, Chart 1). Overall, construction output grew by 6 per cent in 2024 H1 with volatile performance, followed by a year-on-year decline of 6.2 per cent in July 2024. The volume of new contracts in construction was up 108 per cent in July 2024, driven by a surge in the value of government orders. The increase was driven by high-value contracts for road construction, according to the HCSO. Based on the EBI Construction Activity Report, the share of public investment in construction output, construction starts and construction completions decreased over the past two years as well. In terms of construction starts, the volume of public buildings shows the most prominent decline.

Demand for office space continues to be dominated by renewals. In 2024 H1, total demand for modern offices in Budapest was 21 per cent higher than in the same period last year. Breaking down demand, new rental transactions fell (by 5 per cent) in year-on-year terms, while the volume of other types of transactions rose (Chart 3). Net demand (excluding renewals) in the first half of the year was 25 per cent higher than a year earlier. The volume of lease contracts signed in 2024 H1 amounted to 238,000 square metres, of which 46 per cent were contract extensions, significantly higher than the 39-per cent average for the past six years (2018–2023). New leases accounted for 34 per cent of total demand, owner-occupancy for 9 per cent, extensions for 8 per cent and pre-leases for 3 per cent. In terms of the distribution of net demand for office space by economic sector, the share of technology and telecommunications and the share of services to households and retail trade decreased in 2024 H1 relative to 2023. An increase was mainly seen in the share of business services and trade (Annex, Chart 12). Based on white-collar occupations, the share of teleworking at the national level

Chart 4
Leasing and development activity in the Budapest office market



Note: Based on data from the end of 2024 Q2.

Source: Budapest Research Forum, Cushman & Wakefield

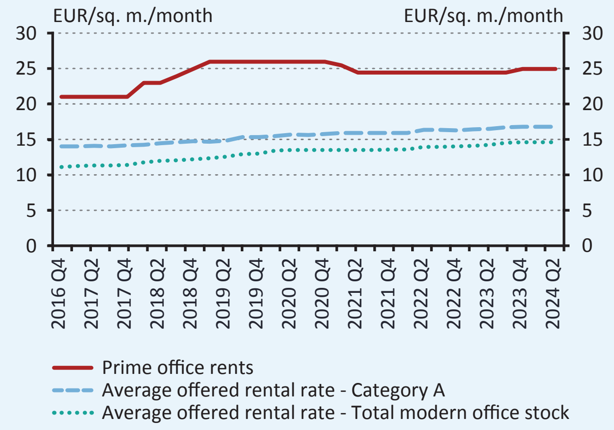
advanced steadily from 15 per cent in 2023 to 16 to 17 per cent in 2024 H1; this ratio may be substantially higher in the Budapest office market.

With demand levels similar to recent quarters, the vacancy rate is expected to rise further in 2024. In 2024 H1, 78,000 square metres of new office space was completed in the Budapest office market (equivalent to 1.8 per cent of the total space at the end of the previous year), up 22 per cent on 2023 H1 (Chart 4). This means that at end-June 2024, the total stock of modern office space in Budapest amounted to 4.44 million square metres, with a vacancy rate of 13.9 per cent, up 0.6 percentage point versus end-2023 and 1.3 percentage points versus end-June 2023. Net market absorption,[5] which shows the change in leased property, amounted to 34,000 square metres in the first half of the year, thanks to a higher volume of rental transactions in the second quarter. In 2024 H2, 96,000 square metres of office space is expected to be completed, 77 per cent of which was pre-leased at the end of June 2024. This rate is higher than the average of 51 per cent for the same period in the previous five years, and may take some pressure off the rising vacancy rate.[6] Contrary to European trends, the volume of office space under construction in Budapest has increased since 2023 Q4. The main reasons for this were construction starts driven by office demand from public institutions, but large-scale owner-occupied projects were also launched in 2024 Q2. Demand for new office space in the public sector will have an impact on net absorption and vacancy rates in 2025–2026. Preliminary estimates suggest that the relocation of public institutions may lead to an overall increase of 1.5–2 percentage points in the vacancy rate. At the end of June 2024, a total of 455,000 square metres of office space was under construction in Budapest, representing 10.2 per cent of the existing modern office space. Overall, the volume under development and low demand figures (e.g. net absorption) point to a further increase in the vacancy rate, which may reach 15 per cent by end-2024.

[5] For definitions related to CRE demand, see Annex 2.

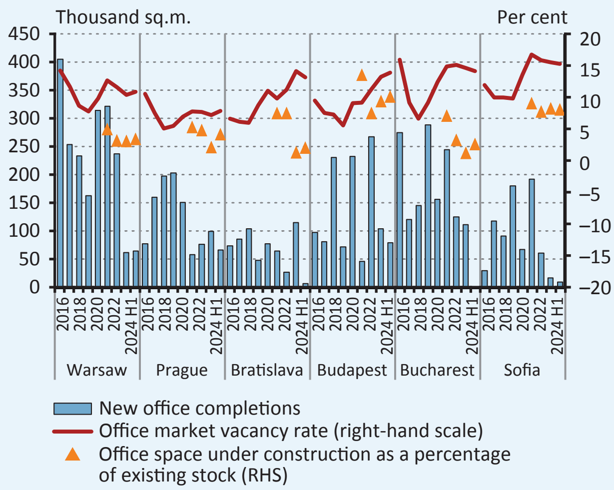
[6] The impact of the pre-lease levels of completions on the vacancy rate is influenced by the underlying proportion of demand for new rentals and of moves, as the latter leave freed-up spaces behind increasing the volume of vacant space and thus the vacancy rate.

Chart 5
Offered rental rates on the Budapest office market



Source: CBRE

Chart 6
Development activity and vacancy rates in regional capital office markets



Source: MNB compilation based on CBRE, Colliers, Cushman & Wakefield and JLL data

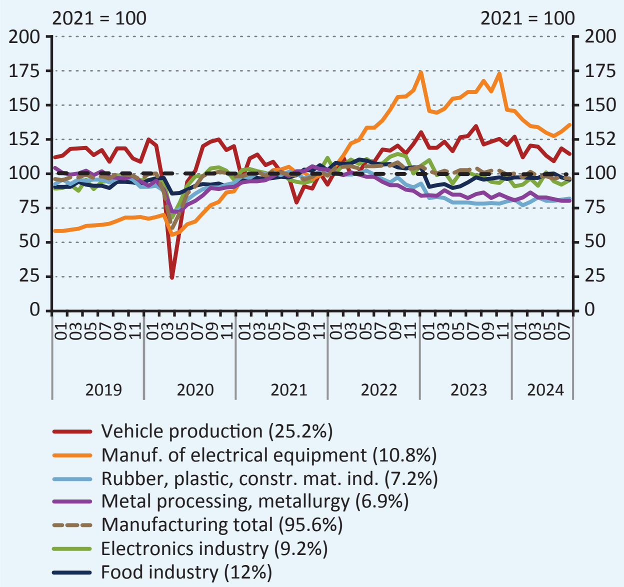
With low demand, rents rose in line with euro area inflation. With regard to the total modern office space regularly monitored by the Budapest Research Forum, the average monthly rate of the rental price offered was EUR 14.6 per square metre in 2024 Q2, reflecting a year-on-year increase of 2.8 per cent (Chart 5). For better quality offices (category "A"), the average rental price offered was EUR 16.8 per square metre per month, up 1.8 per cent from one year earlier. Prime rents for office buildings at the best locations and of the highest quality in Budapest rose by 2 per cent year-on-year. The rate of growth of the average rental price offered was broadly in line with the annual inflation rate (HICP) of 2.5 per cent in the euro area in June 2024.

Trends in vacancy rates in the capital cities of the CEE region varied. Within the region, the vacancy rate for office buildings increased in Budapest, Prague and Warsaw and decreased in the other capitals in 2024 H1 (Chart 6). In Bucharest, Bratislava and Sofia, the decline amounted to 0.3 to 1.0 percentage point, while in Budapest, Prague and Warsaw, the increase ranged from 0.5 to 0.7 percentage point. The lowest vacancy rate (7.9 per cent) was still observed in Prague and the highest rate (15.3 per cent) was seen in Sofia; at 13.9 per cent, Budapest ranked above the average of the six capitals surveyed (12.6 per cent). Of the six capitals surveyed, the ratio of office space under construction to existing stock fell only in Sofia. While this ratio was 2 to 4.2 per cent in Bucharest, Bratislava, Prague and Warsaw at end-June 2024, it amounted to 8.1 and 10.2 per cent in Sofia and Budapest, respectively. Looking at completions in 2024 H1, Bucharest and Bratislava recorded a decrease in completion volumes, while the other capitals saw an increase, compared to the same period in 2023. The highest volume of completions (78,000 square metres) was registered in Budapest; however, Prague and Warsaw also had 66,000 and 64,000 square metres of new offices completed, respectively.

3 Industrial-logistics Market

In the first seven months of 2024, output fell in most of the sectors that are also key to demand for industrial-logistics properties, with industrial production down 3.4 per cent year-on-year and domestic road freight transport down 6.1 per cent in tonne-kilometres. The vacancy rate of industrial-logistics space around Budapest stagnated in a year-on-year comparison, at 8.5 per cent at end-June 2024, which is not high by historical standards. Demand for industrial-logistics space was dominated by new leases and pre-lease in 2024 H1, with moderate net market absorption. If net market absorption remains at the levels observed in recent quarters, the vacancy rate is expected to continue rising. While 42,000 square metres of new industrial-logistics space was completed in 2024 H1, the area of completions planned for 2024 H2 may be several times larger, with an expected 340,000 square metres, increasing the risk of oversupply in the short term. Typical rents for industrial-logistics properties rose by 6.2 per cent on an annual basis.

Chart 7
Change in the volume of production of the main manufacturing industries (2021 = 100)



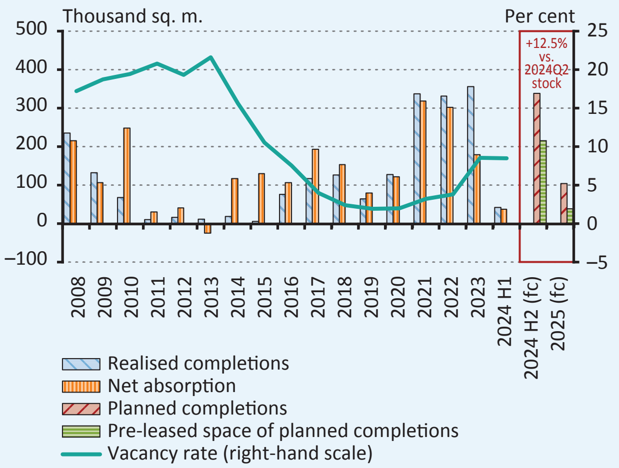
Note: Seasonally and working day effect adjusted data. Compared to the monthly average of 2021. In the legend, the percentage values in parentheses next to the manufacturing sub-sectors denote the sub-sector's share in the industrial production of 2023.

Source: HCSO

Industrial production continued to decline in July and August 2024. Industrial production in Hungary fell by an average of 2.9 per cent on an annual basis in the first six months of 2024. Subsequently, volumes in July were down 1.3 per cent year-on-year, while they stagnated relative to the previous month, according to data adjusted for seasonality and working days. Of the manufacturing subsectors, the output of the automotive industry, which represents the largest share, and the production of electrical equipment also fell by 10 per cent on an annual basis in July (Chart 7). The manufacture of computer, electronic and optical products decreased by 1 per cent. Food, beverages and tobacco production grew by 3.2 per cent versus the same period a year earlier, thanks to an increase in both domestic and foreign sales. Based on preliminary data, industrial output contracted at a year-on-year rate of 9.5 per cent in August 2024. Considering the low volume of orders and business confidence indices, industrial output in 2024 may be subdued. Investment in the national economy dropped by 16.8 per cent in 2024 Q2 versus the same period one year earlier. Most of the key sectors relevant to the CRE market showed a slowdown in annual growth (Annex, Chart 2). Investment in manufacturing, the most important sector, fell by 35 per cent.

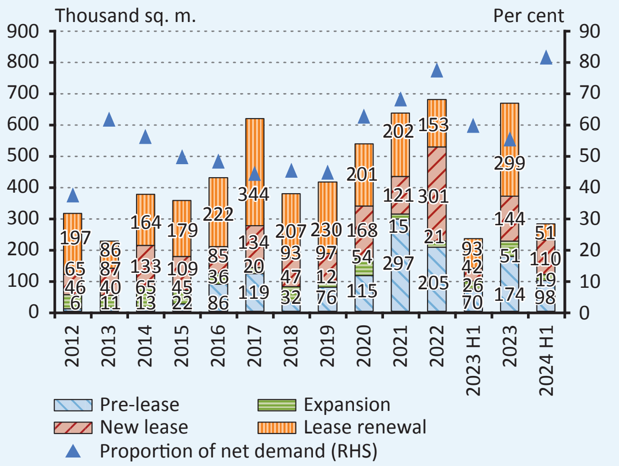
Barring a substantial increase in net absorption, the vacancy rate in the industrial-logistics market in and around Budapest is expected to continue rising. In 2024 H1, 42,000 square metres of industrial-logistics space was completed in Budapest and environs, which corresponds to 1.2 per cent of the total space at the end of 2023 and represents a low volume relative to H1 completions in the last few years (Chart 8). The new floorspace placed on the market during the first half of the year already had tenants at the time of completion. 340,000 square metres of industrial-logistics space (9.5 per cent of total space) is expected to be completed in 2024 H2, 64 per cent of

Chart 8
New completions, net absorption and the vacancy rate in the industrial-logistics market of Budapest and environs



Note: Based on data from the end of 2024 Q2.
Source: Budapest Research Forum, Cushman & Wakefield

Chart 9
Rental demand by contract type in the industrial-logistics rental market of Budapest and environs



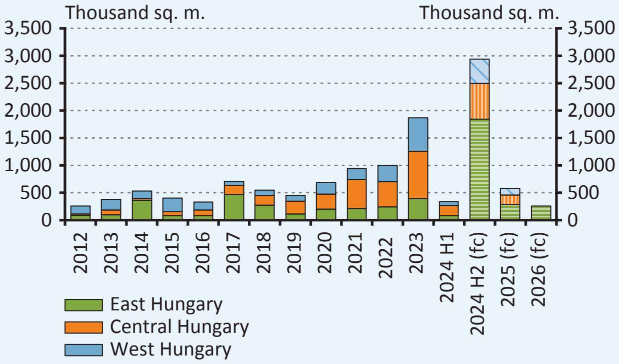
Source: Budapest Research Forum, Cushman & Wakefield

which was pre-leased at the end of June 2024. In terms of demand, net absorption in the first half of the year (37,000 sq m) was 180 per cent above the low level of 2023 H1 (13,000 sq m). As a result of the full occupancy rate of completions and the positive net market absorption in the first half of the year, the vacancy rate in the Budapest industrial-logistics market decreased by 0.1 percentage point during the period to 8.5 per cent at end-June 2024. Looking ahead, if net market absorption fails to increase substantially compared to the level seen in the first half of the year, the vacancy rate in the industrial-logistics segment is expected to continue rising, due to the impact of the vacant floorspace from completions entering the market.

Demand for industrial-logistics space was dominated by new leases and pre-lease in 2024 H1, with moderate net market absorption. In 2024 H1, 279,000 square metres of industrial-logistics space was leased in Budapest and its environs (Chart 9). This level of gross demand was 4 per cent higher than in the same period one year earlier and is only surpassed by the H1 levels in 2020 and 2017. Net demand excluding contract renewals in 2024 H1 was 29 per cent higher than a year earlier, while the volume of contract renewals was 45 per cent lower. This meant that the share of contract renewals in gross demand amounted to only 18 per cent as opposed to 45 per cent in 2023. New leases accounted for 40 per cent of gross demand, pre-leases for 35 per cent and extensions for 7 per cent. Retailers were the most active players in the industrial-logistics rental market in 2024 H1, accounting for 44 per cent of total rentals, but logistics services also had a high share of 40 per cent (Annex, Chart 15). Rents offered at end-June 2024 were typically in the range of EUR 5.3–5.9 per square metre per month (Annex, Chart 16). The median of the typical rent range increased by 6.2 per cent over the past year.

In 2024, the national stock of industrial-logistics real estate may increase by around one-fifth, mainly concentrated in locations of domestic industrial projects. At end-June 2024, the national stock of modern industrial-logistics properties amounted to about 14.9 million square metres, including real estate for rental purposes and proprietary use. In 2024 H1, 332,000 square metres of new space was completed, equivalent to 2 per cent of the total space at end-2023. Looking at completions outside Budapest and its environs (290,000 square metres), 27 per cent of the new space was constructed in Eastern Hungary, 47 per cent in Central Hungary and 26 per cent in Western Hungary (Chart 10). At the national level, ongoing major industrial projects, which are concentrated in a few industrial hubs, and the associated supply chain are generating massive demand for industrial-logistics real estate. With the floorspace completed in the first half of the year and scheduled for

Chart 10
Industrial-logistics completions and planned completions in Hungary



Note: Central Hungary includes property developments in Budapest and environs. Planned completions are based on data from end-June 2024.

Source: CBRE

completion in the second half, a record volume of 3.3 million square metres of industrial-logistics space is expected to be completed nationwide in 2024, representing an increase of 22 per cent compared to the end-2023 stock. In 2024 H2, 62 per cent of completions are expected in Eastern Hungary, 22 per cent in Central Hungary (including Budapest) and 15 per cent in Western Hungary. The high figure in Eastern Hungary is mainly due to ongoing investment projects in Debrecen, Kecskemét and Nyíregyháza. Foreign capital inflows in the industrial-logistics segment, challenges in the construction industry related to industrial development and the regulation of logistics parks[7] were among the items discussed at the meeting of the Housing and Real Estate Market Advisory Board in September 2024; see Box 1 for a summary of its key messages.

Box 1
Meeting of the Housing and Real Estate Market Advisory Board in September 2024

At the September 2024 meeting of the Housing and Real Estate Market Advisory Board (LITT), which focused on the CRE market, experts from the fields of construction, property development, investment and consultancy, as well as the competent ministries and key financing partners reviewed the current situation and prospects of the construction industry, the challenges facing CRE investment and financing, and trends on the rental market.

CONSTRUCTION, PROPERTY DEVELOPMENT

CRE market experts reported that the construction sector was seeing a gradual decline in the number of contracts and a low number of new development projects. On the other hand, fewer orders mean that construction is not facing capacity constraints. There are no delays in payments, although the SME sector is experiencing a slowdown, and some foreign investors delay payments by having their certificates of completion approved in the home country, with a processing time of up to 4–6 months. Experts believe that the downturn in European electric car sales may hold back and slow down major investment projects related to the battery factories being built in Hungary and the deployment of production capacity.

The Hungarian construction industry will reach another milestone as of 1 October 2024, when the concept of “Hungarian product” will be enshrined in law. At present, 45 per cent of construction materials need to be imported. However, in addition to the preference for domestic building materials, it is important to stress that their quality and cost-effectiveness must also be taken into account, i.e. inefficiently and expensively produced domestic materials and their manufacturers cannot remain competitive with foreign competitors.

RENTAL MARKETS AND INVESTMENTS

The office market has changed significantly since the outbreak of the coronavirus, and experts do not expect the high demand seen in previous years to return. Market participants believe that the correction in office prices in Western Europe and the region may continue. In Hungary, the low number of investment transactions is explained by the fact that sellers are not under pressure to sell properties at depressed prices, and for buyers, the current interest

[7] Government Decree No 161/2023 (IV. 28.) on science and innovation, technology, industrial and logistics parks.

rate environment does not yet make investments profitable. Because of the extremely high cost of construction and materials, few companies can afford to build their own office buildings. All of the main drivers of real estate development point to a negative outlook for the office market: rents are stagnating or rising at a slower pace than inflation; construction costs have increased significantly; and expected yields on investment have risen. As for old office buildings, experts noted that it would not be profitable to buy such properties at present, as tenants now expect ESG criteria to be met and such properties would not permit the recovery of the costs of renovation.

Vacancy rates stopped rising in the industrial-logistics market in Budapest in 2024 H1. However, according to market experts, this is temporary, as some of the projects under construction have already been completed but not yet been put up for lease due to poor demand. In addition, they see significantly lower lease volumes today relative to the increased demand and the ensuing expectations noted during the coronavirus epidemic. As a result, there is a tendency for some investors to start selling their industrial-logistics exposures. Some think it is doubtful whether all the 500 or so logistics and industrial parks will be granted Logistics Park rating by 1 January 2025. Some experts argued that compliance with the regulation could reduce supply. Several experts pointed out that an increasing number of manufacturing projects are starting operations in logistics parks, which may raise concerns, in particular with regard to the inadequate storage of hazardous waste. Currently, 700,000 square metres of industrial-logistics space for rental is under development, of which around 500,000 square metres is being built in Budapest and its environs. The high share of pre-lease may not fully reflect additional demand, and tenants moving out may weaken the positive effect on net absorption. Economic growth may boost the currently low demand for rentals, because as long as potential tenants believe the future to be uncertain, they are reluctant to commit for a longer term.

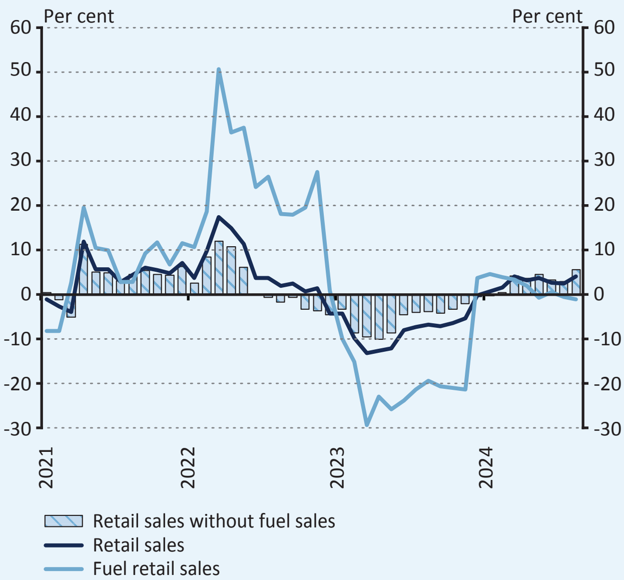
FINANCING AND INVESTMENTS

Most of the banks operating in Hungary can allocate capital abroad; hence, they are only interested in funding good projects in Hungary. The availability of subsidised schemes for the financing of CRE projects has been limited and, according to market experts, CRE lending rates are expected to drop slowly, making lending difficult. Real estate funds currently manage some HUF 2,500 billion, the return on which is also significant, which may have a positive impact on demand for investment. However, when it comes to the purchase of properties, funds are having it rough in the Hungarian real estate market: the rules on limiting the erection of shopping centres, which also pose challenges for operators in terms of tenant mix and tenant turnover, make the purchase of retail properties less attractive, and developers keep the majority of logistics development projects in their own portfolio, while the office market is also becoming less attractive with rising vacancy rates and falling demand caused by structural changes. Nevertheless, the HUF 150 billion allocation under the Baross Gábor Capital Scheme – a substantial part of which is still waiting to be invested by real estate funds – may have a positive impact on sales in the near future.

4 Retail Market

After 13 months of steady decline, retail sales volumes have transitioned to a slow rise since January 2024, increasing by 4.1 per cent year-on-year in August 2024. Real net household income has been rising again since September 2023, and household confidence has gradually improved. In 2024 H1, vacancy rates decreased for all retail property types, both in Budapest and in regional cities. The rental prices offered stagnated across all property types. The share of online retail sales channels in turnover fell below 10 per cent in 2023 and was 9.5 per cent in the January–August 2024 period.

Chart 11
Year-on-year change in retail sales and fuel retail sales volume

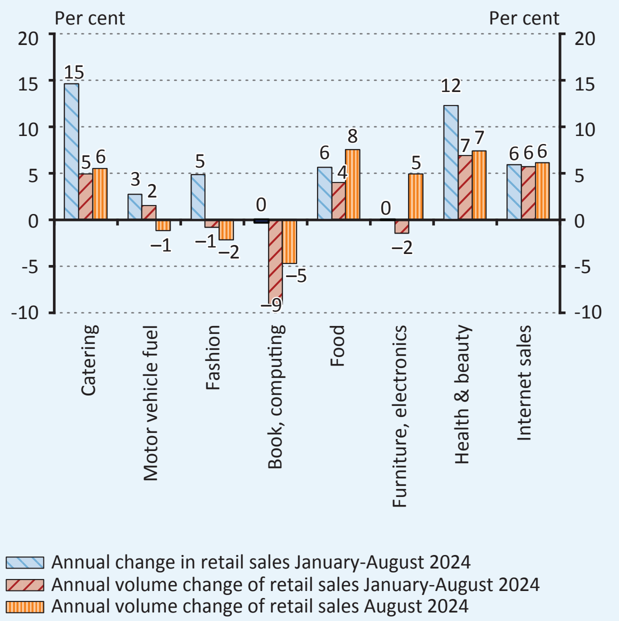


Note: Calendar-adjusted data. In 2022, fuel retail sales accounted for 16.5 per cent of total retail sales.

Source: HCSO

Retail sales are now expanding in year-on-year terms in 2024. After an average increase of 2.6 per cent in the first half of the year, retail sales volumes grew by 2.5 per cent on an annual basis in July and by 4.1 per cent in August 2024 (Chart 11), in line with growth in real average earnings (Annex, Chart 5). Based on data adjusted for calendar effects, retail trade excluding fuel sales rose by 5.6 per cent in August 2024. Food retail sales were up 7.5 per cent year-on-year in August, while sales also increased in the segments of pharmaceuticals, medicinal products, perfumes and fragrances (+7.4 per cent), online (+6.1 per cent), and furniture, hardware and ironmongery (+4.9 per cent). However, in addition to fuel sales, lower sales were registered in August in the segments of textiles, clothing and footwear (-2.2 per cent) and mixed manufactured goods (-2.8 per cent) (Chart 12). The sales volume of catering establishments also increased year-on-year in August 2024 (+5.6 per cent) and in the first eight months of the year (+5.2 per cent). The share of online channels in retail sales excluding fuel trade, at current prices, advanced from 10.1 per cent in 2020 to 11.4 per cent in 2021, before falling to 10.3 per cent in 2022, 9.8 per cent in 2023 and 9.5 per cent in the first eight months of 2024.

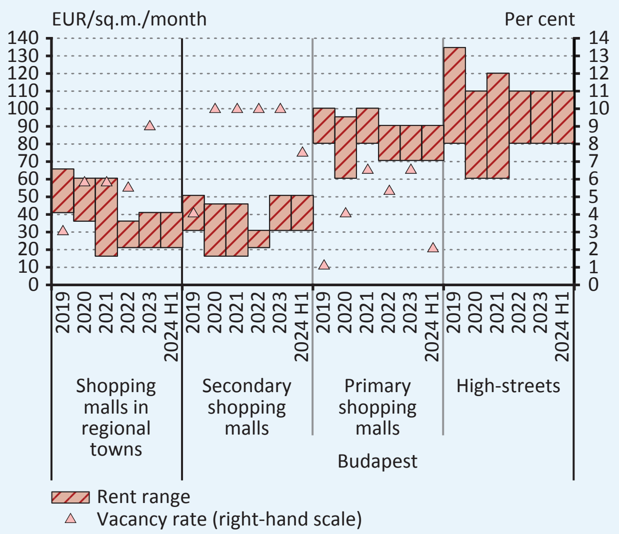
Chart 12
Development of turnover of retail store types and restaurants



Note: The change in the volume of retail store sales based on calendar adjusted volume indexes of retail sales, in the case of catering based on unadjusted volume index.

Source: HCSO

Chart 13
Retail rental rates and vacancy rates in Hungary



Note: The rental rate data refer to a retail unit of 100–150 square metres, and the columns show the dispersion of the highest rental rates for real estate in different retail property types.

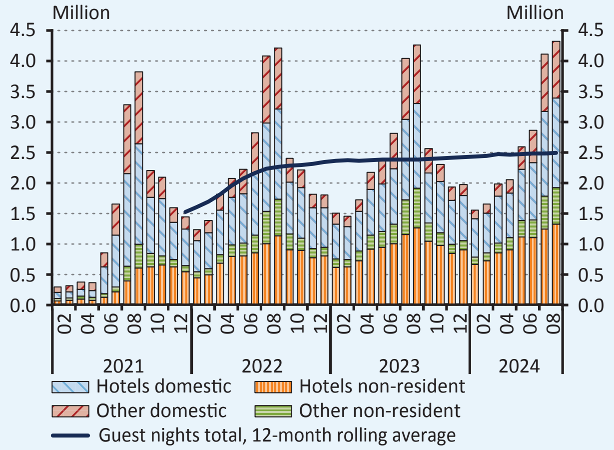
Source: CBRE

Rents for retail properties stagnated in 2024 H1 across all property types. In 2024 H1, the median of the typical ranges of rental prices asked for retail premises of 100–150 square metres stagnated across all property types (Chart 13). This means that the typical rent asked in prime shopping centres in Budapest remains between EUR 70 and 90 per square metre per month, while rents for premises in secondary shopping centres in Budapest range between EUR 30 and 50 per square metre per month. In terms of vacancy, the indicator decreased for all retail property types. Based on available data, the average vacancy rate of prime shopping centres in Budapest has improved significantly, to around 1–2 per cent, while the average vacancy rate of secondary shopping centres in Budapest amounts to around 7–8 per cent.

5 Hotel Market

In the first eight months of 2024, the number of guest nights spent in commercial accommodation establishments increased by 3.8 per cent at the national level versus the same period in 2023. After a decline in 2023, the number of overnight stays by Hungarians rose slightly (by 2 per cent) in the first eight months of 2024, while the number of overnight stays by foreign guests increased by 6 per cent year-on-year. Within commercial accommodation, hotel revenues in January–August 2024 were 14 per cent higher than in the same period of the previous year, while the number of hotel guest nights rose by 8 per cent. In the hotel sector nationally, around 2,700 new hotel rooms were under construction at end-June 2024, but the timing of completions remains uncertain, with delays expected to continue as in recent years. Similarly to Budapest, hotel occupancy rates in 2024 continued to improve in the CEE region's capitals, with a 5-percentage-point gap relative to the pre-pandemic level in 2019; Warsaw came the closest to the 2019 occupancy rate, recording only a 1-percentage-point gap, while Budapest remains 10.2 percentage points behind.

Chart 14
Monthly guest nights in commercial accommodation establishments

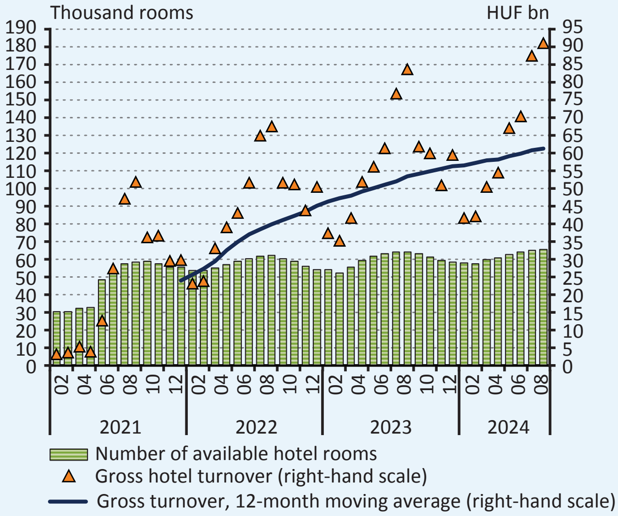


Source: HCSO

In the first eight months of 2024, hotel guest nights increased by 8.3 per cent nationally and by 9.5 per cent in Budapest, now also supported by domestic guest nights. From January to August 2024, 72 per cent of all overnight stays by Hungarian guests in domestic commercial accommodation establishments (21.1 million) and 77 per cent of overnights by foreigners were spent in hotels (Chart 14). The number of nights spent in hotels rose by 8.3 per cent year-on-year across the country and by 9.5 per cent in Budapest (Annex, Chart 8). In the period under review, the number of overnight stays by foreigners increased by 9.5 per cent year-on-year, while the number of nights spent by domestic guests also rose by 7.1 per cent, as opposed to the decrease seen in the previous year. In the first eight months of 2024, the number of overnight stays in hotels was about 15 per cent below the 2019 level nationally.[8]

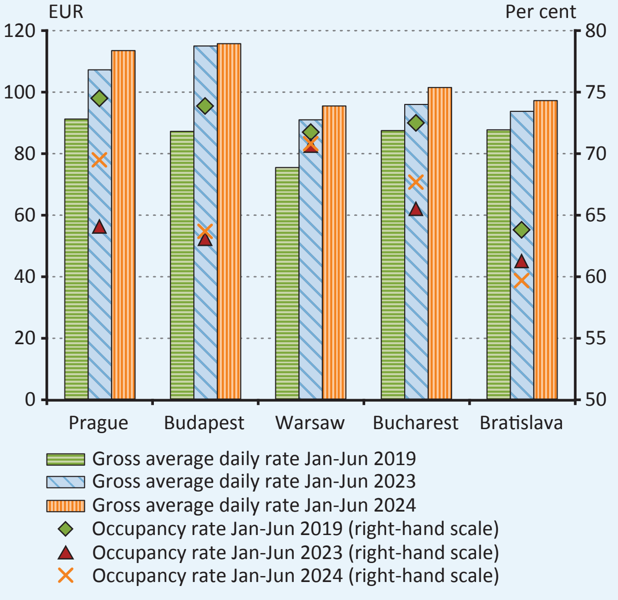
[8] From June 2022, the HCSO uses a new data source for data on commercial accommodation establishments, with data published back to 2021 from the new data source. Therefore, the comparability of accommodation data before 2021 and after May 2022 is limited. The change in the number of overnight stays in 2019 and 2023 was estimated using a correction factor calculated from the deviation of the data available from the old and new data sources of the HCSO for the same periods (January 2021 to May 2022).

Chart 15
Domestic hotel capacity and development of gross turnover



Source: HCSO

Chart 16
Average performance indicators for hotels in CEE capitals

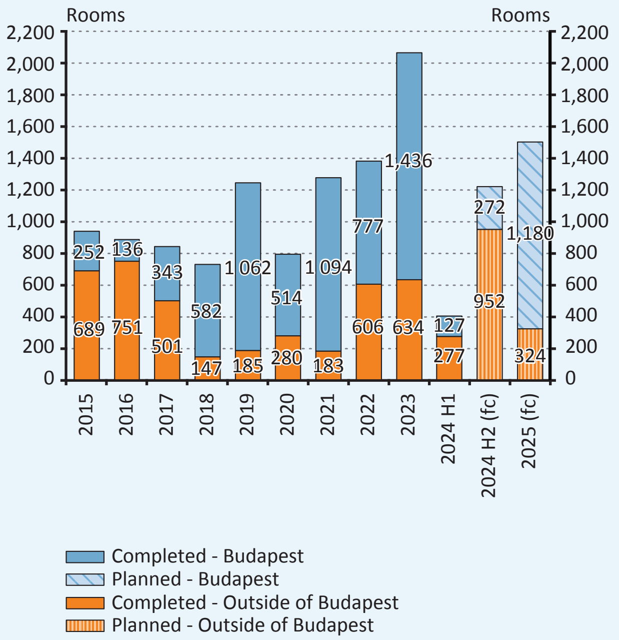


Source: CBRE, STR Global

In the first eight months of 2024, hotel revenues were 14 per cent higher than in the same period in 2023. The number of hotel rooms on offer in 2024 H1 continued to show typical seasonal patterns, with the lowest number of rooms available in February (57,900 rooms); however, this figure is 10 per cent higher than in the same month of 2023. There were 65,900 hotel rooms available nationwide in August 2024, up 2.1 per cent from a year earlier (Chart 15). With an 8-per cent increase in the number of guest nights, the gross revenue of domestic hotels in the January–August period of 2024 was 13.7 per cent higher than in the same period of the previous year.

Hotels in all of the CEE regional capitals saw improved performance, albeit with a slowing growth rate across all indicators. In 2024 H1, room occupancy rates in hotels in the regional capitals ranged between 60 and 71 per cent, with Budapest recording the second lowest figure at 64 per cent (Chart 16). The average for the region is still 5 percentage points below the occupancy rate for the same period in 2019. In terms of average gross room rates, Budapest hotels remain the most expensive in the region at EUR 115 in 2024 H1, 11 per cent above the regional average. In the first six months of 2024, hotel room prices rose in all of the capital cities, by an average of 4 per cent year-on-year.

Chart 17
Number of completed and planned hotel rooms in Hungary



Note: Completions planned are based on data from end-June 2024.

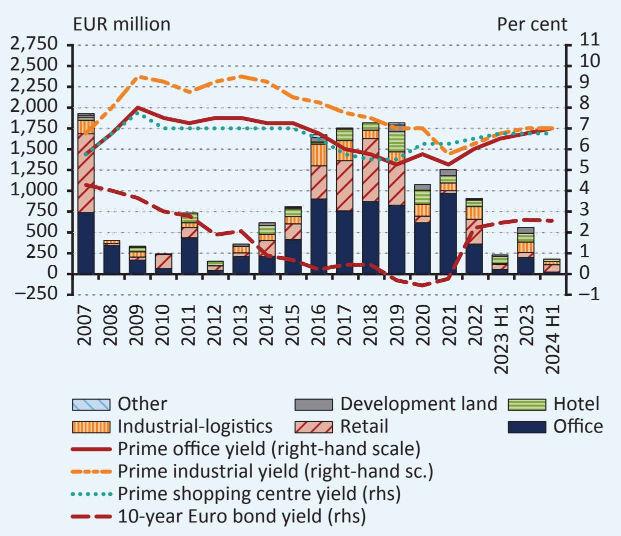
Source: CBRE, Cushman & Wakefield, Hungarian Hotel & Restaurant Association

In 2024, more new hotel rooms are expected to be completed in locations outside Budapest. A total of 400 new hotel rooms opened across the country in 2024 H1 (Chart 17). 31 per cent of the completed rooms are located in Budapest. Ongoing hotel development projects are expected to generate significant completion volumes in 2024 and 2025, with an additional 2,700 hotel rooms under construction, 45 per cent of which are scheduled to be completed in 2024 H2. In terms of room numbers, 53 per cent of the hotels under construction are located in Budapest, while the completions expected in 2024 H2 are dominated by locations outside the capital (78 per cent). In total, the number of rooms of hotel projects in progress at end-June 2024 is equivalent to 4 per cent of the existing national hotel capacity of around 65,000 rooms. There have been significant delays in hotel completions in recent years, and there is also considerable uncertainty factored into current completion plans.

6 Commercial Real Estate Investments

The domestic commercial real estate investment market recorded turnover of around EUR 180 million in 2024 H1, down 21 per cent on the turnover figure for 2023 H1. In 2024 H1, only the office market saw an increase of 25 basis points in prime yields, while yields in the industrial-logistics and retail segments stagnated; however, the fact that the number of transactions was extremely low may significantly affect the formation of yields. Elevated yields, continued high financing costs in euro and subdued rental demand are keeping investors on the sidelines, portending low investment turnover for 2024 as a whole. In several countries in the CEE region, investment volumes for 2024 H1 already increased year-on-year, and in four of the six countries surveyed, prime office yields stagnated, with the corresponding decline in capital values based on the changes in yields and rents coming to a halt in several countries. Looking ahead, market experts expect investment turnover in Poland and Czechia to rise substantially in 2024, while the potential persistence of continued low and declining domestic investment turnover with high (79 per cent) proportion of domestic investors may pose risk to the perception of the market. Between the end of 2023 and the end of June 2024, the capital value of prime offices decreased by 0.5 per cent on average in the CEE countries and by 3.6 per cent in Budapest. Measuring the change in capital values against the end of 2022 Q2, there is a decrease of 14 per cent on average across the CEE capitals and 28 per cent in Budapest. In the quarterly survey by the Royal Institution of Chartered Surveyors,9 80 per cent of respondents saw the real estate market cycle to be at some stage of recession in 2024 Q2, with most (63 per cent) putting it at the trough of the cycle. The professionals surveyed forecast negative capital value expectations only for the office segment, while for the industrial-logistics segment, they are now expecting an increase, as opposed to the steady decline in the last year and a half.

Chart 18
Investment volume on the Hungarian CRE market, its composition and prime yields



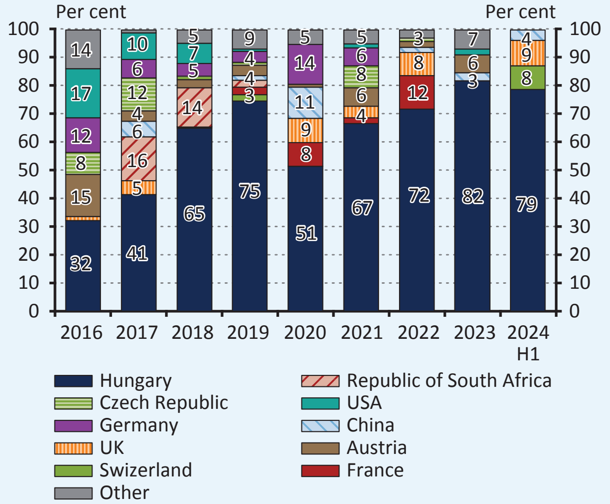
Source: CBRE, Cushman & Wakefield, MNB

Investment activity continued to weaken in 2024 H1. In 2024 H1, investment turnover in the domestic commercial real estate market amounted to around EUR 180 million, down 21 per cent on the previous year (Chart 18). Of this volume, 49 per cent was generated by sales of retail properties, 21 per cent by industrial-logistics estate, 16 per cent by hotels and 14 per cent by sales of office buildings. The average transaction size in the first half of the year amounted to EUR 12 million, 34 per cent below the 2023 average. In 2024 H1, prime yields[10] stagnated in the industrial-logistics and retail segments, and rose by 25 basis points in the office segment in the first quarter then stagnated in the second quarter. Since the trend reversal of falling yields in 2022 Q3, yields have risen by 175 basis points in the office segment, 150 basis points in the industrial-logistics segment and 50 basis points for shopping centres. The rise in yields is moderate when compared to the recession that started in 2008; however, at that time, the office market saw a yield increase of 200 basis points, the industrial-logistics segment 225 basis points, and shopping centres 150 basis points in the span of just one year. At the end of June 2024, prime office and industrial-logistics yields stood at 7 per cent, while shopping

[9] Royal Institution of Chartered Surveyors, Global Commercial Property Monitor. Available at: https://www.rics.org/news-insights/market-surveys/global-commercial-property-monitors

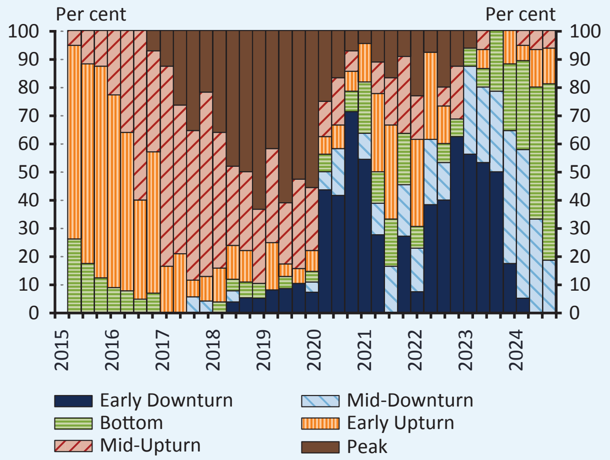
[10] Yield data refer to the (initial) gross yields of CRE transactions and are calculated as the ratio of the real estate's annual net rental revenue and the purchase price and reflect the yield level requirement of investors.

Chart 19
Investment volumes on the Hungarian CRE market by investors' country of origin



Source: CBRE, Cushman & Wakefield, MNB

Chart 20
Perceptions of the current phase of the property cycle



Note: Based on responses from July 2024.
Source: RICS

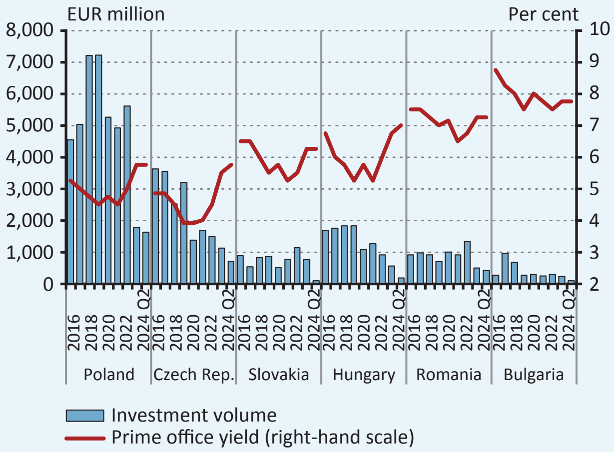
centres generated a yield of 6.75 per cent. Since the end of 2021, as monetary conditions tightened and then eased in response to high inflation, the yield spreads on real estate have declined by 100–230 basis points in each segment versus the 10-year euro bond yield[11] by the end of June 2024 (Annex, Chart 18).

The vast majority of investment turnover continues to be attributable to domestic investors, as purchases by Hungarian investors accounted for 79 per cent of investment turnover in 2024 H1 (Chart 19). Aside from domestic investor transactions, investments consisted of purchases by investors from the UK, Switzerland and China. Hungarian public open-ended real estate funds had a share of 12 per cent of investment turnover. Hungarian real estate investment companies accounted for 53 per cent of H1 investment volumes, foreign real estate investment companies for 8 per cent, domestic closed-end and foreign real estate funds combined for 6 per cent, and private investors for 5 per cent (Annex, Chart 17). The decline in investment flows and the low share of foreign investors may indicate a low level of liquidity in the domestic real estate investment market. Hungarian public open-ended real estate funds overall recorded a slight capital outflow in the first three quarters of 2024. The liquidity coverage of public real estate funds remains at an adequate level, with the ratio of liquid assets to net asset value – including the amount of credit lines available for immediate drawdown[12] – standing at 53 per cent at the end of September 2024 (Annex, Chart 20).

Most experts believe that the commercial property market bottomed out in 2024 H1. According to a survey by the Royal Institution of Chartered Surveyors (RICS), in 2024 Q1, one in three experts believed that the commercial property market would undergo a severe downturn, with only 19 per cent thinking the same in the second quarter, and the proportion of the experts surveyed claiming the cycle had bottomed out rising from 47 per cent in the first quarter to 63 per cent in the second quarter (Chart 20). The outlook for the commercial real estate market remained negative in 2024 H1: respondents reported a further decline in both domestic and foreign investor interest, with the downturn mainly affecting the office market. In this segment, capital value expectations in 2024 H1 remain negative for the three months ahead, while for the industrial-logistics segment, the experts surveyed anticipate an increase (Annex, Chart 25).

[11] The 10-year Eurobond yield is the average of the 10-year government bonds issued by AAA-rated euro area countries.
[12] Government Decree No 78/2014. (III. 14.) on the investment and borrowing rules applicable to collective investment forms permits the inclusion of unconditional and immediately drawable credit lines in the calculation of the ratio of liquid assets.

Chart 21
Investment volume and prime office market yields in the CEE region



Source: MNB compilation based on CBRE, Colliers, Cushman & Wakefield and JLL data

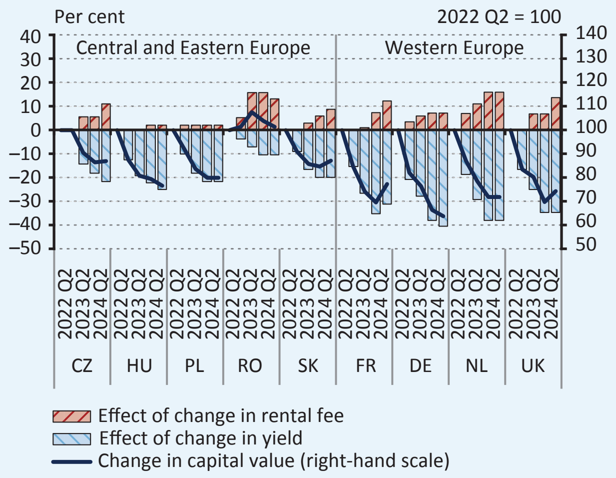
In 2024 H1, investment yields in the CEE region tended to stagnate, with the transaction volume increasing by an average of 35 per cent on an annual basis. In most CEE countries, prime office yields stagnated in 2024 H1, with only Czechia and Hungary recording a rise of 25 basis points (Chart 21). Among the countries surveyed, Prague and Warsaw had the lowest prime office yield of 5.75 per cent and Sofia the highest at 7.75 per cent. At the regional level, investment turnover in 2024 H1 was 35 per cent higher than in the same period of the previous year, with the largest increases in transaction volumes from a low base seen in Romania (132 per cent) and Poland (103 per cent) (Annex, Chart 19). Turnover decreased in Slovakia (-72 per cent) and Hungary (-21 per cent). Sales volumes stagnated in Czechia (+1 per cent) and went up by 12 per cent in Bulgaria. Looking ahead, a possible persistence of the still weakening H1 domestic investment flows may pose risk to the perception of the market.

The stagnation of expected yields in 2024 H1 broke the downward trend in capital values across Europe. After a year and a half of decline, investment turnover in the commercial real estate market in Europe as a whole rose by 10 per cent in 2024 H1. Nonetheless, the overall positive trend in investment continues to be accompanied by a low number of transactions, reflecting uncertainty about the market environment. With a few exceptions, prime office yields typically stagnated in the more mature Western European office markets and in the CEE region. Stagnating yields now helped to keep the value of properties stable instead of contributing to their depreciation as seen in the past year and a half. Based on the evolution of prime yields and prime rents in the office market in 2024 H1, the calculated capital value of prime offices in Western Europe[13] stagnated in Amsterdam and Milan, increased by 6.5 and 11 per cent in London and Paris, respectively, and dropped by 4 per cent in Berlin.[14] In Central and Eastern Europe, an average decrease of 0.5 per cent in capital values was observed, with corrections ranging from -4 to +3 per cent by country. Based on prime office yields and rents, the capital value of prime office investment in Budapest fell by 4 per cent over the six-month period reviewed. Compared to the end of 2022 Q2, when the upward trends in yields turned around, prime office yields and rents as at the end of June 2024 reflect devaluation at a rate of 28 per cent in Western Europe, 14 per cent in the CEE region and 24 per cent in

[13] The capital value of prime offices is a calculated, theoretical value, being the amount of the annual net rental revenue resulting from the level of prime rental rates capitalised by the prime yield as a perpetual annuity (annual prime revenue from rents/prime yield).

[14] As regards the changes in the capital value estimated based on the change in prime yields and rental rates it should be noted that the prime yield and rental rate represent the expected yield and rental rate in the case of top-quality properties at prime locations. The degree of the changes measured in the prime property category does not necessarily reflect the average trend in the entire office market, but it may serve as a good indicator of the direction of changes.

Chart 22
Change in capital value in the office markets of the major capital cities in CEE and Western Europe



Note: For every date the figure shows the change versus 2022 Q2. The rate of value change in the prime office market segment is not representative of the entire market, however, its direction is a good indicator of the tendency in the value development of the overall market.

Source: MNB calculation based on CBRE and Cushman & Wakefield data

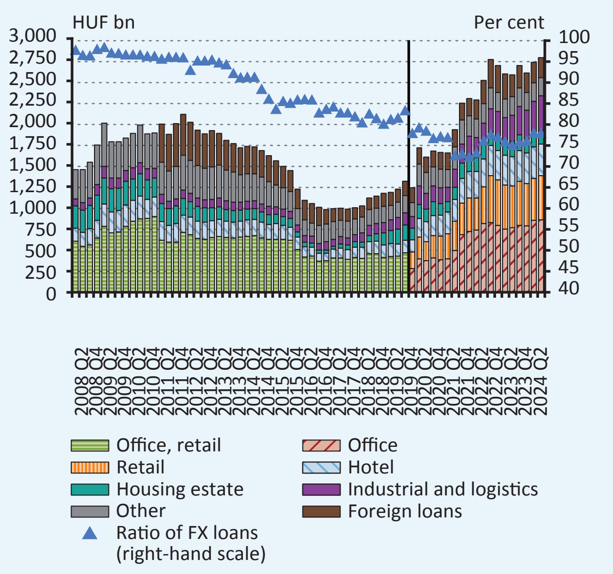
Budapest (Chart 22). Despite positive investment trends in certain locations, some market experts do not rule out the possibility of further yield rises across Europe in the short term. At the end of September 2024, the European Systemic Risk Board's decision-making body reviewed, among other things, the risks in the commercial real estate market. In its statement,[15] the board highlighted that with low activity and an increasing pool of non-performing loans, the sector remains vulnerable. In addition to these cyclical developments, structural challenges, such as the post-pandemic shifts in demand, the rise of teleworking and adaptation to climate policies, make the sector more vulnerable.

[15] Press release The General Board of the European Systemic Risk Board held its 55th regular meeting on 26 September 2024. Available at: https://www.esrb.europa.eu/news/pr/date/2024/html/esrb.pr241004~21064c0147.en.html

7 Commercial Real Estate Financing

By end-June 2024, credit institutions' total portfolio of CRE-backed project loans had grown by 8 per cent year-on-year, with this rise equivalent to 3 per cent after filtering out exchange rate effects. Aside from residential real estate and other real estate, project loans in all property segments increased in the year up to the end of June 2024. The share of project loans denominated in foreign currency advanced 3 percentage points over the past year to reach 78 per cent at the end of June 2024. In 2024 H1, banks disbursed 37 per cent more CRE-backed project loans compared to the low base from one year earlier. The increase in lending was evident across all property types, except hotels and other real estate. Nearly one-third (30 per cent) of all disbursements during the year went to financing industrial-logistics real estate, which rose 230 per cent year-on-year, with loans for the development or purchase of office buildings (accounting for a share of 25 per cent) up 91 per cent. Loans for residential development fell 52 per cent year-on-year in 2024 H1. Interest rates on EUR-denominated loans, which account for the bulk of project loans, stagnated in 2024 H1 compared to end-2023, while interest rates on forint loans continued to fall. According to the MNB Lending Survey, banks tightened lending conditions mostly for office buildings in 2024 Q2 and are planning further tightening in 2024 H2, citing changing risk tolerance and industry-specific challenges. Institutions reported an increase in loan demand in the second quarter for all property segments, but looking ahead they expect a decline in financing demand for office buildings, owing to the negative outlook for the sector.

Chart 23
Composition of the credit institution sector's project loan stock for CRE purchase or development, by real estate type



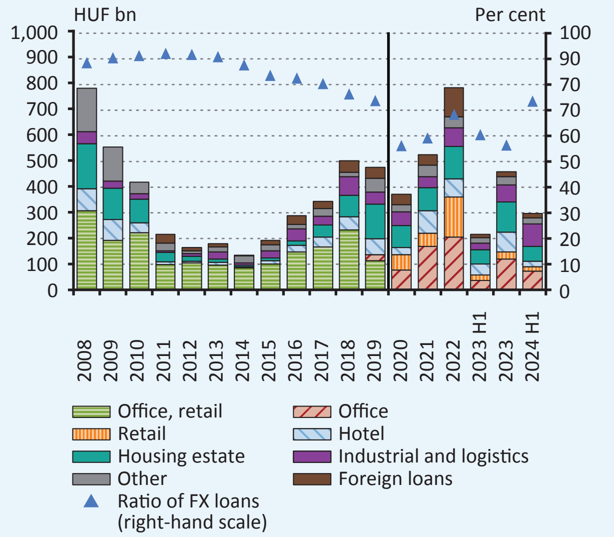
Note: No data breakdown by real estate type is available for loans provided to foreign companies before 2011. Based on aggregated data of the data-providing institutions up to 2019 Q3, and based on individual loan agreement data from 2019 Q4; the comparability of data from these two periods is limited. From 2019 Q4, the data include loans from financial intermediary institutions (including investment funds) in addition to non-financial companies.

Source: MNB

Expansion in the portfolio of project loans backed by CRE was supported by all segments except residential housing developments. In June 2024, credit institutions held CRE project loans[16] in the amount of HUF 2,784 billion on their balance sheets, up 8 per cent compared to the same period one year earlier or 3 per cent when adjusted for exchange rate effects (Chart 23). Loans for the development or purchase of office buildings accounted for the largest share of the portfolio, at around 31 per cent, with a year-on-year increase of 7 per cent after filtering out exchange rate effects. Industrial properties, representing 15 per cent of the total, saw the largest year-on-year growth of 26 per cent, while the loan portfolio of residential housing developments and retail properties shrank by 8 per cent and 1 per cent, respectively. Hotels saw an annual increase of 5 per cent in terms of data adjusted for exchange rate effects. Adjusted for exchange rate effects, the principal outstanding on foreign loans, which are defined as such by the location of the financed real estate, decreased by 14 per cent relative to 2023 Q2. Foreign currency loans, which are almost exclusively denominated in EUR, represented 78 per cent of the total portfolio at the end of 2024 Q2, after a year-on-year rise of 3 percentage points.

[16] In monitoring the portfolio and disbursements of project loans secured by commercial real estate, the MNB has switched to using the credit contract-level data of the credit registry data service, which is available from December 2019. Compared to the previously used data tables based on the CRR definition of project loans, the credit registry provides a broader view of project loans, and therefore the comparability of the portfolio data before 2019 Q4 with 2019 Q4 and onwards in Figures 23 and 24 is limited.

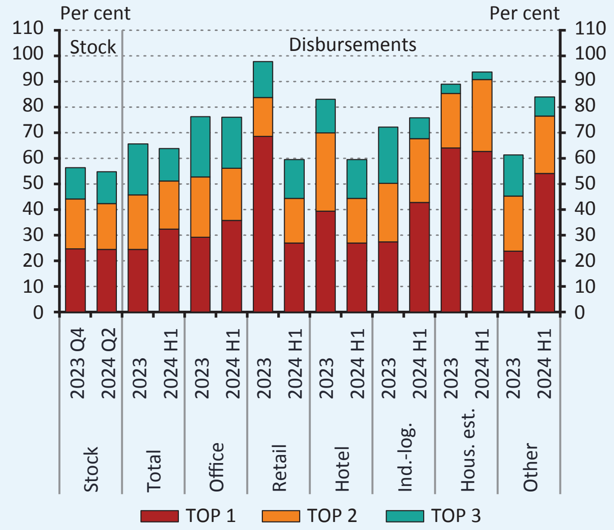
Chart 24
Project loan disbursements of the credit institution sector for the development or purchase of commercial real estate by property type



Note: No data breakdown by real estate type is available for loans provided to foreign companies before 2011. Based on aggregated data of the data-providing institutions up to 2019 Q3, and based on individual loan agreement data from 2019 Q4; the comparability of data from these two periods is limited. From 2019 Q4, the data include loans from financial intermediary institutions (including investment funds) in addition to non-financial companies.

Source: MNB

Chart 25
Concentration of the CRE lending activity of the credit institution sector



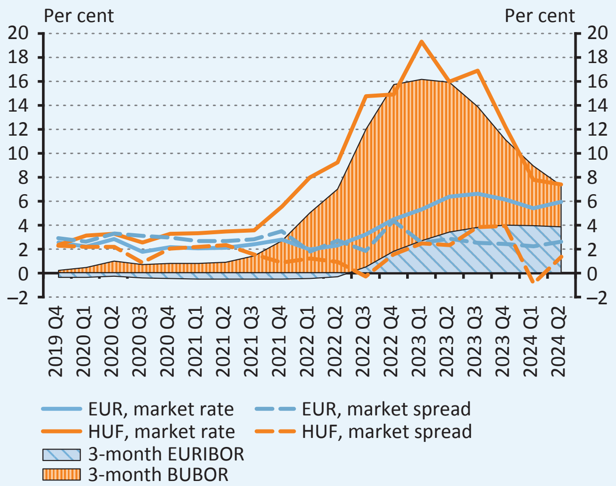
Note: Stock: the cumulative ratio of the stock of institutions with the three largest project loan stock secured by commercial real estate compared to the total stock of the credit institution sector. Disbursements: the cumulative ratio of the annual disbursements of institutions with the three largest commercial real estate-backed project loan disbursements within the total disbursements of the credit institution sector.

Source: MNB

Growth in project loan disbursements in 2024 H1 was supported primarily by disbursements related to industrial real estate. In 2024 H1, credit institutions disbursed a total of HUF 295 billion in CRE-backed project loans for development or purchase purposes, reflecting an increase of 37 per cent (33 per cent when adjusted for exchange rate effects) relative to the same prior-year period (Chart 24). For office buildings, which accounted for one-quarter of H1 volumes, disbursements doubled from a low base, and for industrial real estate, which represents a share of 30 per cent, banks disbursed more than three times the amount disbursed in 2023 H1. The volume of loans granted for the development or purchase of retail real estate and hotels fell by 21 and 52 per cent year-on-year, respectively, while loans extended to finance residential housing developments increased by 5 per cent over the same period. Loans for foreign real estate accounted for only 5 per cent of H1 lending, down from 7 per cent one year earlier. The share of foreign currency loans in new disbursements was 73 per cent in 2024 H1, reflecting an annual increase of 13 percentage points.

More than one-third of the CRE-backed project loans of credit institutions are related to eight groups of clients. At the end of June 2024, 15 credit institutions held the total project loan portfolio of the sector, with the three banks with the largest portfolios together accounting for 55 per cent of the principal outstanding in the sector (Chart 25). Looking at the composition of the CRE-backed project loan portfolio of credit institutions by client group, the three client groups with the largest outstanding principal amounts at the sectoral level account for almost one-fifth (19 per cent) of the total portfolio, while the eight largest client groups for more than one-third (36 per cent). In terms of disbursements in 2024 H1, the three most active financing banks disbursed 64 per cent of the sector-wide volume, 2 percentage points lower than the full-year figure in 2023. Breaking down the disbursement figures by type of real estate, the shares of the three institutions with the highest disbursement volumes range between 60 and 94 per cent within the different segments. In 2024 H1, housing projects (94 per cent) and other real estate (84 per cent) had the highest concentration of disbursements. Compared to disbursements in 2023, 2024 H1 saw a lower concentration for retail properties, hotels and overall, and a higher concentration for other real estate, residential complexes and industrial-logistics properties. In the case of offices, the combined share of the three institutions with the largest volumes of project loans stagnated, while the share of the institution with the largest amount disbursed increased by 6.5 percentage points.

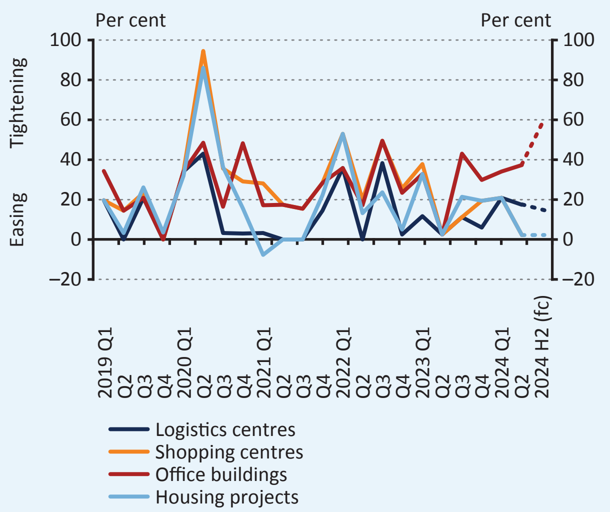
Chart 26
Average interest rate and spread on new project loan contracts secured by commercial real estate and 3-month interbank offered rates



Note: The average interest rate and spread weighted by the contractual amount of project loans secured by commercial real estate concluded in the given quarter. Interest rate spreads on interbank rates and IRS rates based on the loans' reference rate, type of interest rate fixation and maturity. Interbank offered rates are quarterly averages.

Source: ECB, MNB

Chart 27
Changes in credit conditions of commercial real estate loans



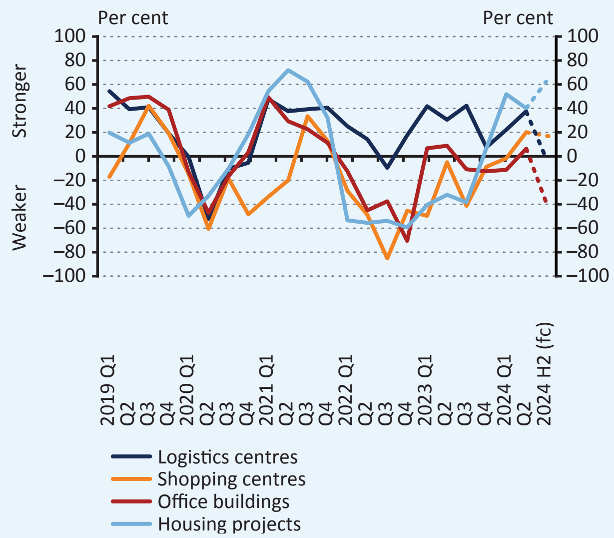
Note: Net ratio is the difference between tightening and easing banks weighted by market share.

Source: MNB, based on banks' responses

Interest rates on market-based HUF project loans followed the evolution of the cost of funds, approaching euro lending rates. In keeping with benchmark rate trends, the interest rate on new HUF-denominated CRE loans continued to decline, falling by around 4.8 percentage points in 2024 H1 and reaching 7.4 per cent in the second quarter, in line with the BUBOR. The interest rate on EUR-denominated loans rose by 0.5 percentage point to 5.9 per cent in Q2 2024, bringing the interest rate gap between HUF-denominated and EUR-denominated project loans (1.4 percentage points) back to the level that prevailed in the low interest rate environment three years ago (Chart 26). Since end-2019, spreads on new CRE-backed project loans have been relatively stable for EUR-denominated loans, ranging between 2–3 percentage points. For forint loans, however, the average interest rate spread was more volatile during the cycle of interest rate hikes and cuts. In 2024 Q2, the average spread on HUF-denominated new project loans was 1.3 percentage points, while the average spread on EUR-denominated loans was 2.6 percentage points.

Banks plan to keep tightening financing conditions for office buildings in the future. According to the quarterly MNB Lending Survey, in 2024 Q2, 37 per cent and 17 per cent of banks tightened financing conditions for office buildings and logistics hubs, respectively, due to worsening risk tolerance and the negative outlook (risk of oversupply) in the sector. Lending conditions for shopping centres and housing projects remained unchanged relative to the previous quarter (Chart 27). Looking ahead to 2024 Q3 and Q4, an increasing share of banks, 58 per cent in net terms, plan to tighten financing conditions further for office buildings, while 15 per cent intend to tighten financing conditions for logistics hubs. 37 per cent of banks cited changed risk tolerance and industry-specific challenges as the reasons behind the prospective tightening (Annex, Chart 24).

Chart 28
Changes in credit demand for commercial real estate loans



Note: Net ratio is the difference between banks indicating stronger and weaker demand, weighted by market share.

Source: MNB, based on banks' responses

Banks expect loan demand to pick up for residential projects and to weaken for office buildings in 2024 H2. Based on the responses to the Lending Survey, banks reported a pick-up in demand for all CRE loan types in 2024 Q2, with a net 41 per cent of the banks mentioning stronger demand for the financing of residential projects, 38 per cent for logistics hubs, 21 per cent for shopping centres and 7 per cent for office buildings, compared to the first quarter (Chart 28). Respondents believed that the recovery in demand for loans was supported by the decline in interest rates and improving appetite for real estate investment. Looking ahead to 2024 H2, a growing share of the banks, around 63 per cent, expect loan demand for housing projects to continue to pick up if the interest rate environment keeps declining, while in respect of the financing of office buildings, a net 38 per cent of the banks expect loan demand to weaken in view of the negative outlook for the sector.

Annexes

ANNEX 1: SUB-MARKETS OF THE BUDAPEST OFFICE MARKET[17]

The office market of Budapest is divided into the following eight sub-markets based on the data collection of the Budapest Research Forum (Chart 29):

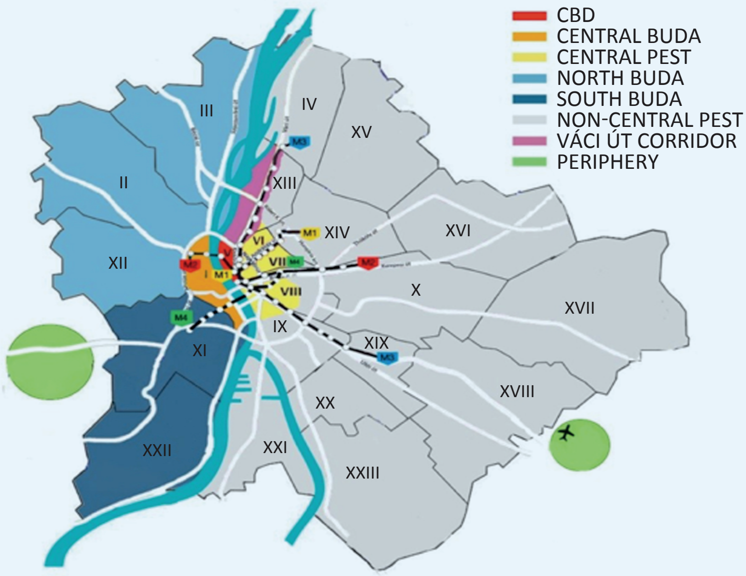
- **Central Business District – CBD:** The inner districts of Budapest, primarily the office buildings in the 5th district and on Andrássy út and the surrounding streets from Bajcsy-Zsilinszky út to the Oktogon. Most of the CBD is an architecturally protected area with a few category "A" office buildings and very limited development opportunities.

- **Central Buda:** Area bounded by the Margit körút–Krisztina körút–Böszörményi út–Jagelló út–Villányi út–Fehérvári út–Október huszonharmadika utca–Irinyi József utca. Similar to the Central Business District, development opportunities are limited.

- **Central Pest:** Area bounded by the Inner City–the Váci út Corridor–Dózsa György út–Thököly út–Fiumei út–Orczy út–Haller utca. Concentrated developments have been performed in this sub-market.

- **North Buda:** Most of districts 2, 3 and 12; investments are limited to smaller areas.

Chart 29
Sub-markets of the Budapest office market



Source: Budapest Research Forum

[17] Source: Cushman & Wakefield

- **South Buda (Non-Central Buda South):** Districts 11 and 22. In this sub-market, the available development areas are an alternative for the service centre office tenants of the Váci út Corridor, but these are less accessible than the Váci út Corridor.

- **Non-Central Pest:** Areas of Pest that are not part of the Inner City, Central Pest or the Váci út Corridor.

- **Váci út Corridor:** Area bounded by Szent István krt.–Váci út–Újpest Városkapu and the Danube. The Budapest office corridor is where the most significant office developments were realised due to the available development areas and good accessibility (public transport: metro line M3, car: via Váci út). This is the most popular sub-market among foreign companies for siting service centres.

- **Periphery:** Agglomeration areas, mainly Budaörs, Vecsés, Biatorbágy and Törökbálint.

ANNEX 2: CONCEPTS RELATED TO DEMAND IN BUDAPEST

Members of the Budapest Research Forum (CBRE, Colliers International, Cushman & Wakefield, Eston International, JLL, Robertson) collect CRE market contracts categorised into the following transaction types:

- **New lease:** A lease agreement of an immediately available area concluded with a tenant that was not previously present in the property.

- **Pre-lease:** A pre-lease contract concluded for a building that has not been completed yet and is not present in the current supply. Consequently, the volume of pre-lease transactions made in the period considered does not immediately increase the leased stock, but only later when it is actually placed on the market.

- **Expansion:** A rental agreement concluded with a tenant that is already present in the property, but rents area additional to its existing tenement.

- **Owner occupation:** The real estate owner utilises the property, basically removing it from the market, decreasing stocks offered for lease.

- **Lease renewal:** The extension of an existing contract with no effect on the rental stock.

The comprehensive measures of rental market activity are:

- **Total demand (gross demand):** The total volume of the above five lease transaction types in the period considered.

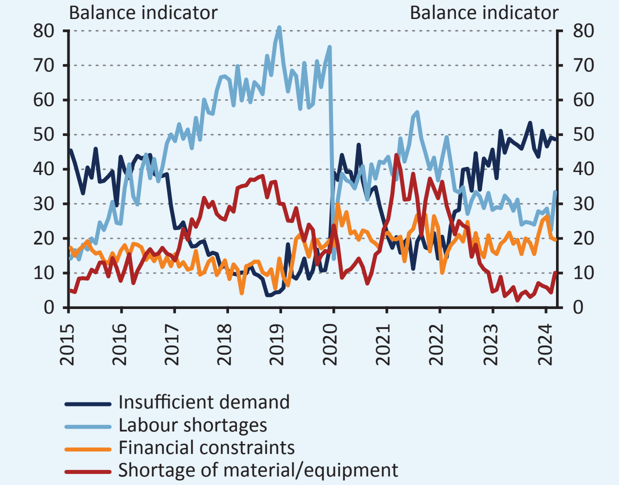
- **Take-up:** Measures the stock of actual new lease contracts; from the above, it includes the volume of new leases, pre-leases and expansions for the period considered.

- **Net absorption:** Shows changes in the lease stock in the period reviewed. The difference between net absorption and gross demand is caused by lease renewals, pre-leases and tenants which exit the market.

ANNEX 3: ANNEX CHARTS

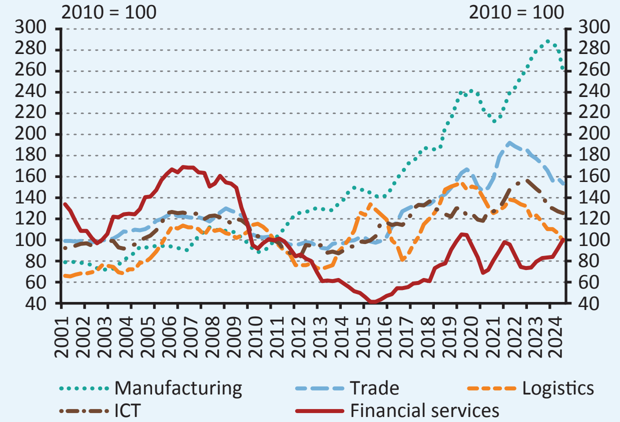
1. Macroeconomic environment

Chart 1
Factors limiting output in the construction industry



Source: European Commission

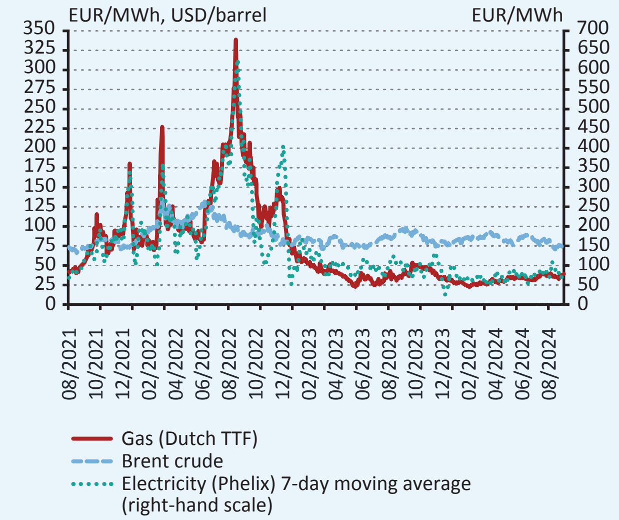
Chart 2
Investment activity of sectors relevant to the CRE market



Note: Four-quarter moving average. The ICT sector refers to the information and communications technology sector.

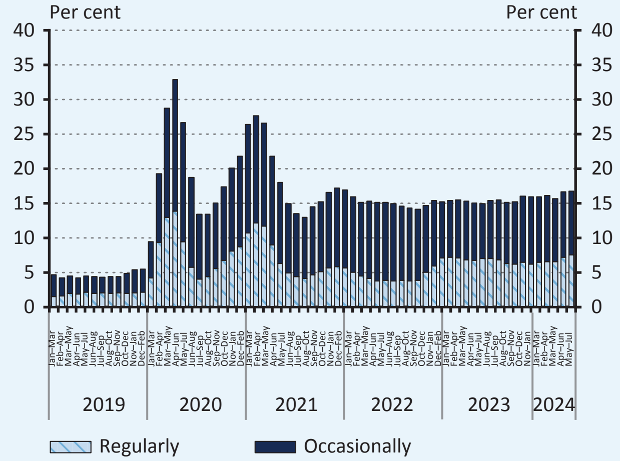
Source: HCSO, MNB calculations

Chart 3
Market price development for gas and electricity



Source: Bloomberg

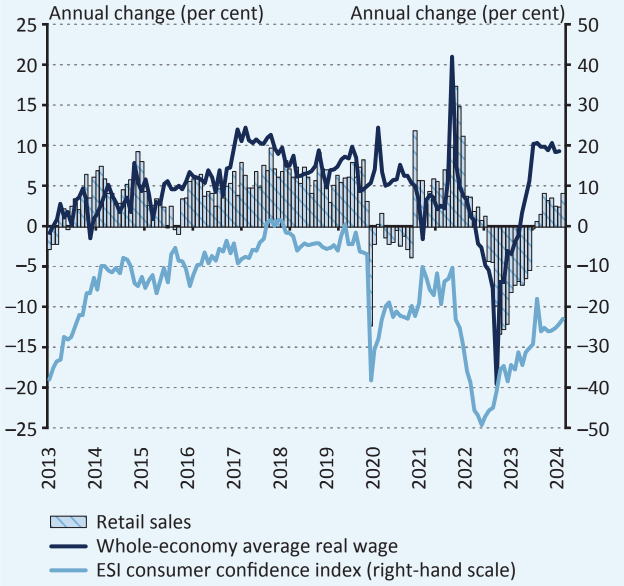
Chart 4
Employees working remotely or at home as a proportion of those in intellectual occupations



Note: Three-month moving average of employees working remotely or at home aged 15–74 as a percentage of those in intellectual occupations.

Source: HCSO

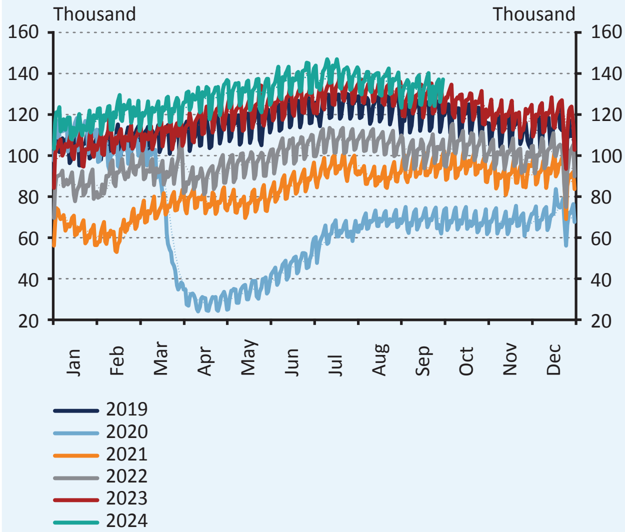
Chart 5
Development of retail sales, average real wage and consumer confidence



Note: Retail sales with calendar-adjusted data.

Source: European Commission, HCSO

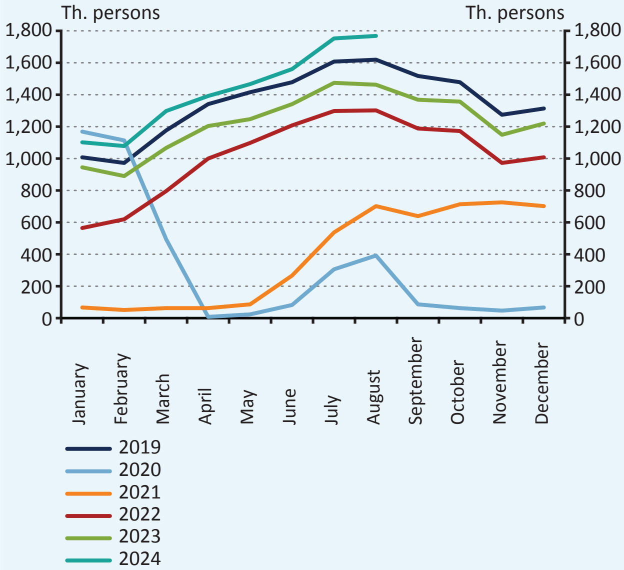
Chart 6
Development of the global number of commercial flights



Note: Commercial flights cover commercial passenger flights, cargo flights, charter flights and some business jet flight.

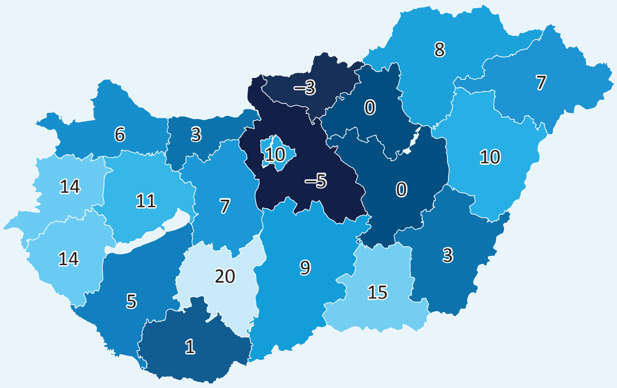
Source: Flightradar24

Chart 7
Budapest Liszt Ferenc International Airport passenger traffic



Source: HCSO

Chart 8
Annual change in the number of guest nights spent in hotels by county (January-August 2024)

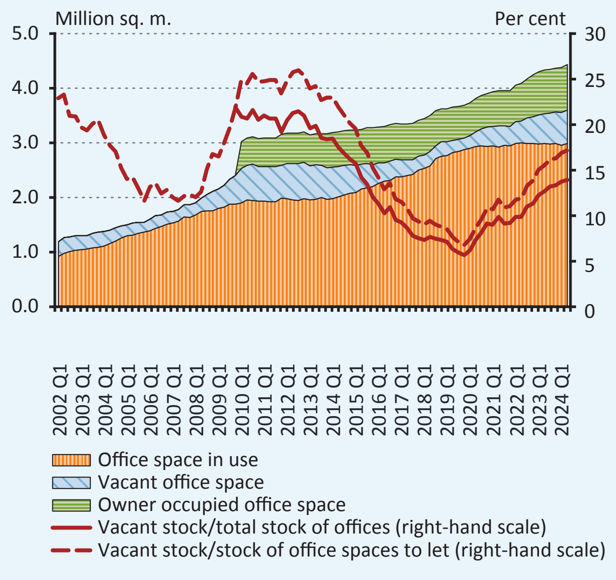


Note: Percentage change compared to the same period in 2023.

Source: HCSO

2. Office market

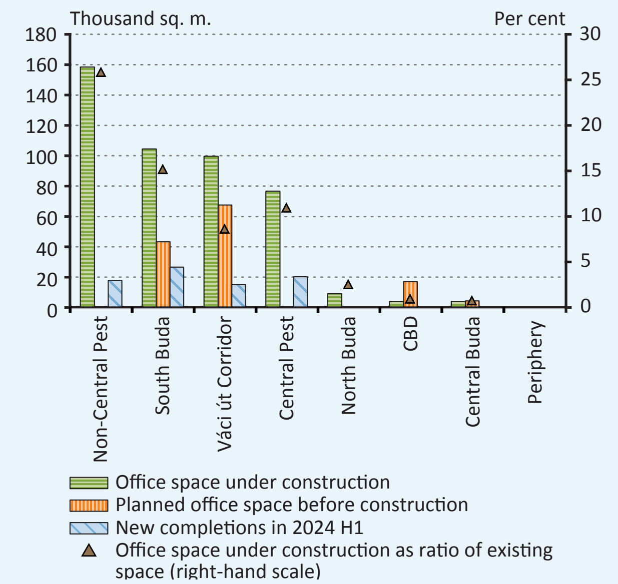
Chart 9
Floorspace and vacancy rates of modern offices in Budapest



Note: Data for owner-occupied offices only available from 2010 onwards.

Source: Budapest Research Forum

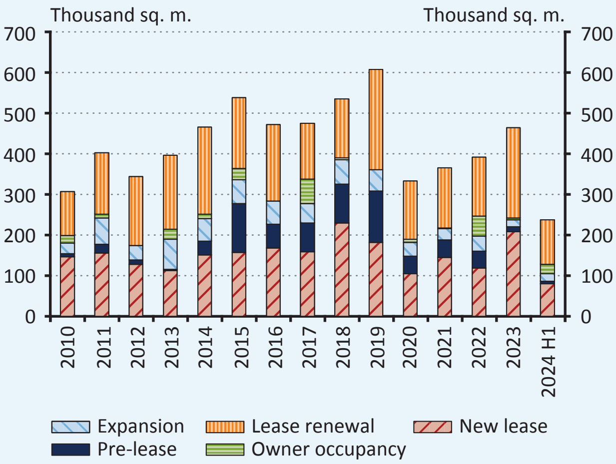
Chart 10
Distribution of Budapest office developments, renewal rate and new completions by sub-market



Note: Based on data from end-June 2024.

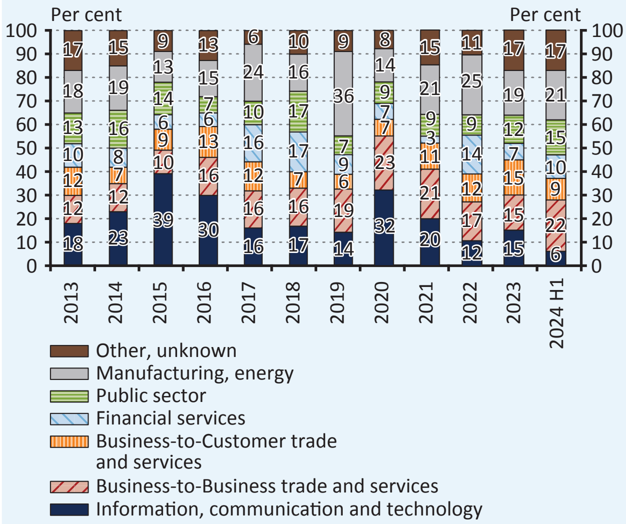
Source: Cushman & Wakefield

Chart 11
Volume and composition of rental demand in the Budapest office market



Source: Budapest Research Forum, Cushman & Wakefield

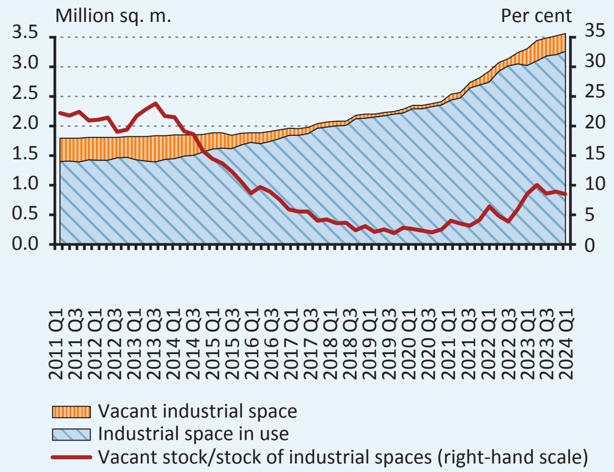
Chart 12
Take-up composition of the Budapest modern office market by tenant activity



Source: CBRE

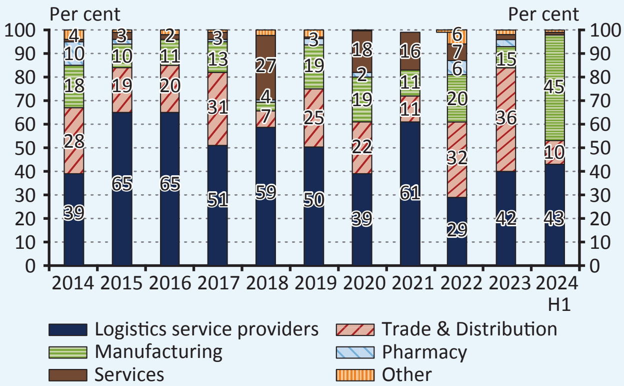
3. Industrial-logistics

Chart 13
Floor space and vacancy rates of modern industrial-logistics sites in Budapest



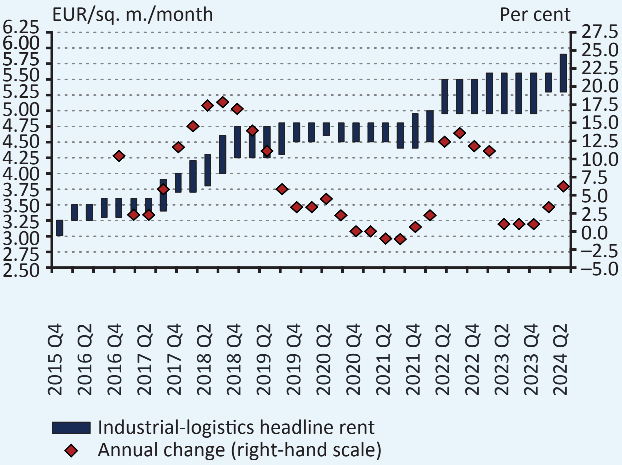
Source: Budapest Research Forum

Chart 14
Total demand composition on the industrial-logistics market of Budapest and environs by tenant activity



Source: Cushman & Wakefield

Chart 15
Typical rental rates of industrial-logistics properties in Budapest and environs

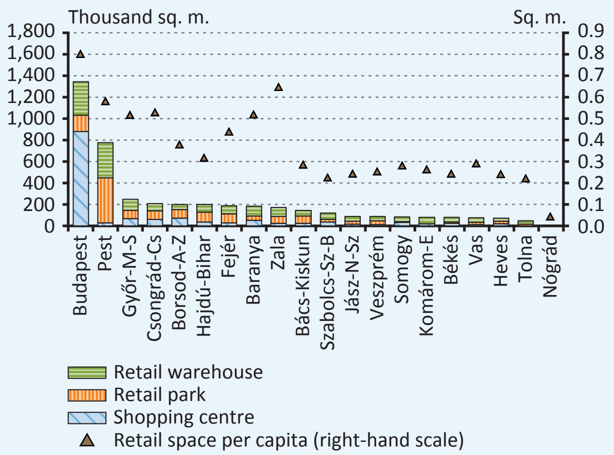


Note: Yearly change presents the yearly change in the mean of the rental rate range.

Source: CBRE

4. Retail market

Chart 16
County distribution and composition of the modern Hungarian retail real estate stock

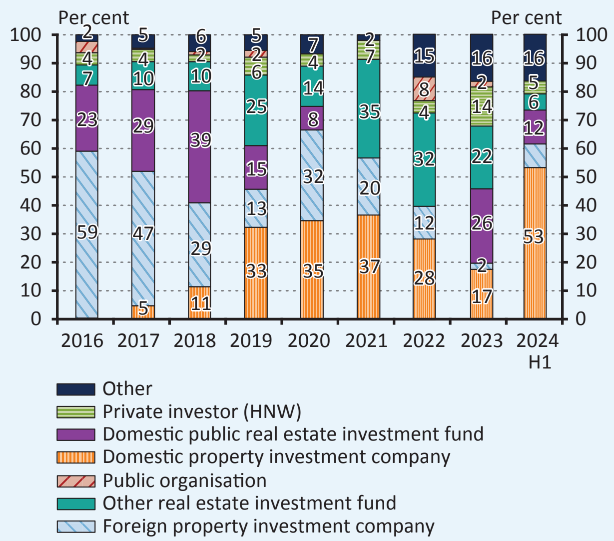


Note: Based on data from end-June 2024.

Source: CBRE

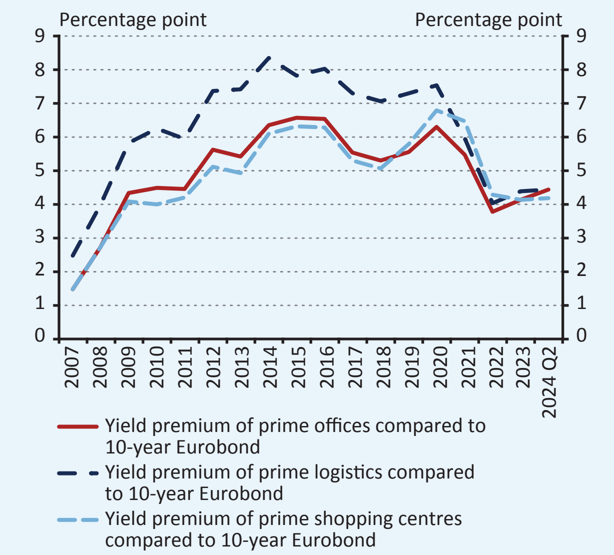
5. Commercial real estate investments

Chart 17
Investment volumes on the Hungarian CRE market by investor type



Source: CBRE, Cushman & Wakefield, MNB

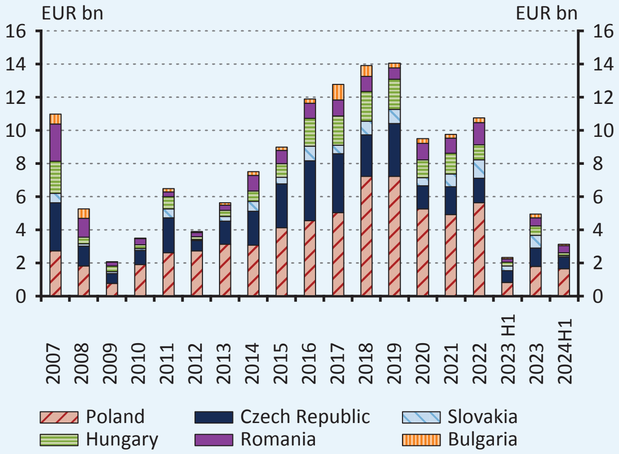
Chart 18
Yield premium of Budapest prime real estate investments compared to 10-year euro government bonds



Note: The 10-year Eurobond yield is the Q4 average, for 2024 Q2 the Q2 average of the 10-year government bonds issued by AAA-rated euro area countries.

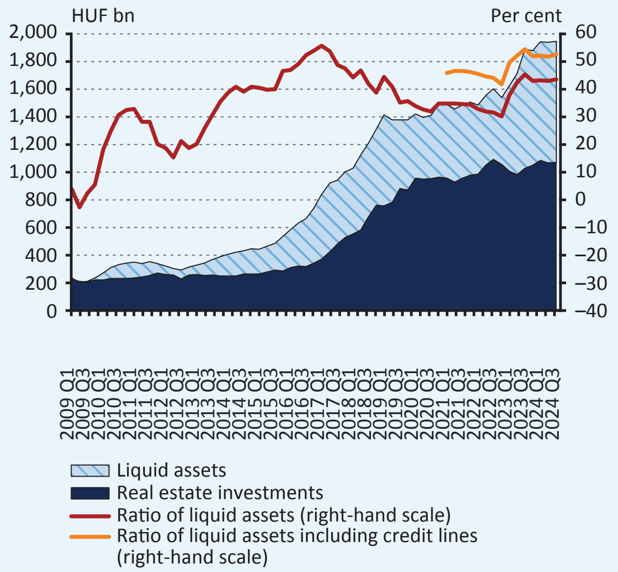
Source: CBRE, Cushman & Wakefield, ECB

Chart 19
CRE investment flows in the CEE region



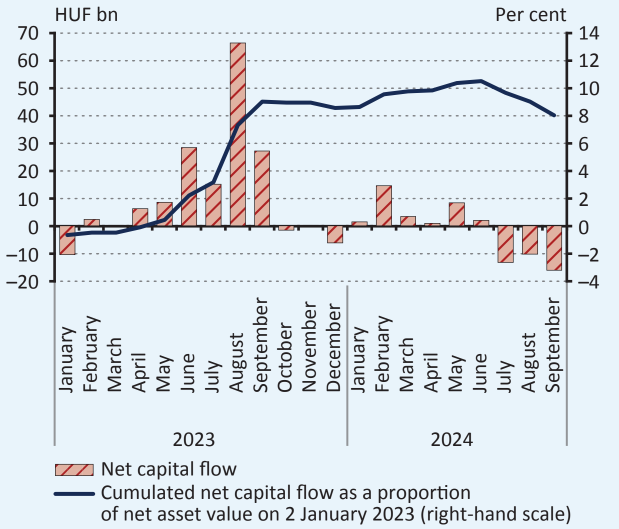
Source: MNB compilation based on CBRE, Colliers, Cushman & Wakefield and JLL data

Chart 20
Asset composition of public real estate funds and the ratio of liquid assets to net asset value



Source: MNB

Chart 21
Net capital flows in Hungarian public real estate investment funds

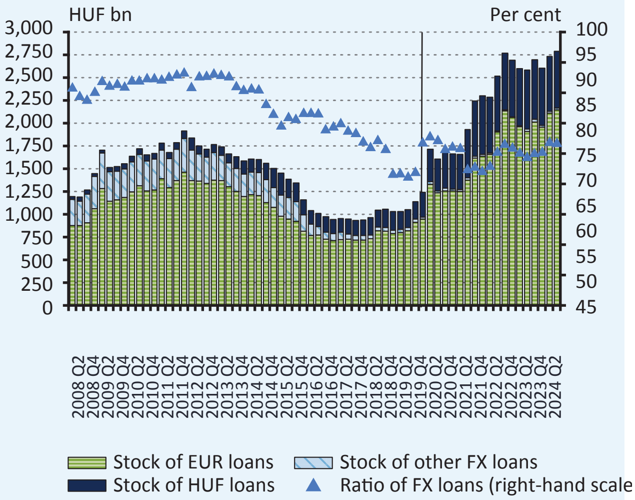


Note: The high capital inflows in August-September 2023 are related to the capital investments by the Magyar Fejlesztési Bank, won by the institutions in the tender of the Baross Gábor Capital Programme's Real Estate Fund Sub-programme.

Source: MNB

6. Bank financing of commercial real estate

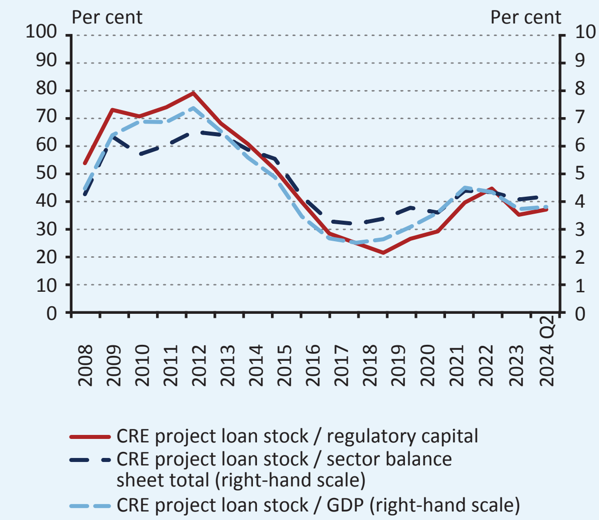
Chart 22
Composition of the credit institution sector's stock of CRE purchase or development project loans by currency



Note: Until 2019 Q3 based on aggregated data of the data-providing institutions, from 2019 Q4 based on individual loan agreement data, the comparability of data from these two periods is limited.

Source: MNB

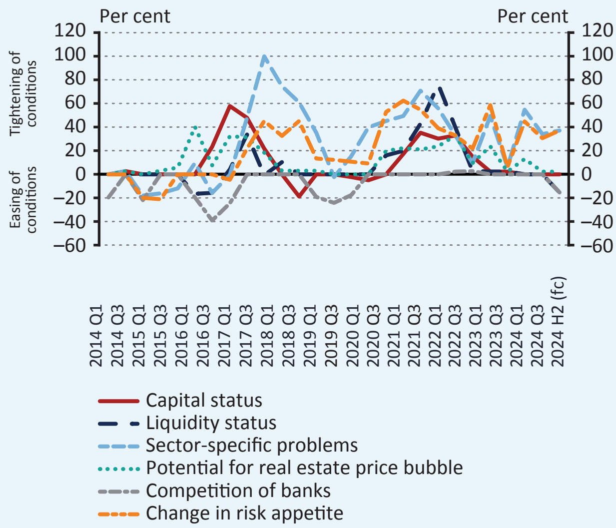
Chart 23
Importance of commercial real estate project loans in credit institutions sector



Note: Credit institutions sector without affiliates, based on non-consolidated data. Until 2019, based on the project loan portfolio according to the CRR project loan definition, from 2020 on the basis of a broader project loan definition, the use of the broader definition in 2023 Q4 results in a 28-per cent higher project loan stock compared to the CRR definition. From 2019 CRE project loans outstanding includes real estate Bond Funding for Growth Scheme (BGS) bond stock.

Source: MNB

Chart 24
Factors behind changes in CRE loan conditions

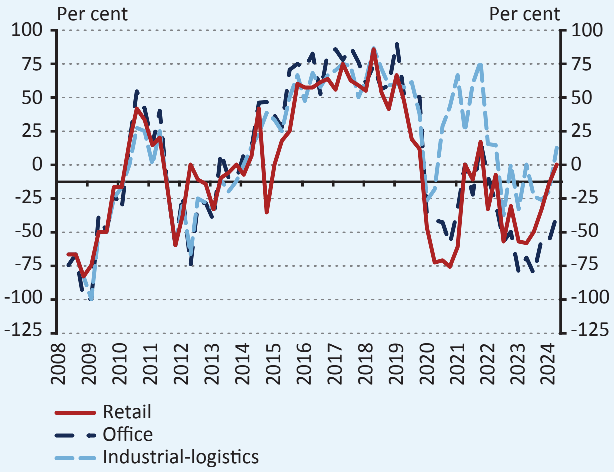


Note: Responses of the analysed banks weighted by market share.

Source: MNB, Lending Survey

7. Commercial real estate market survey of RICS

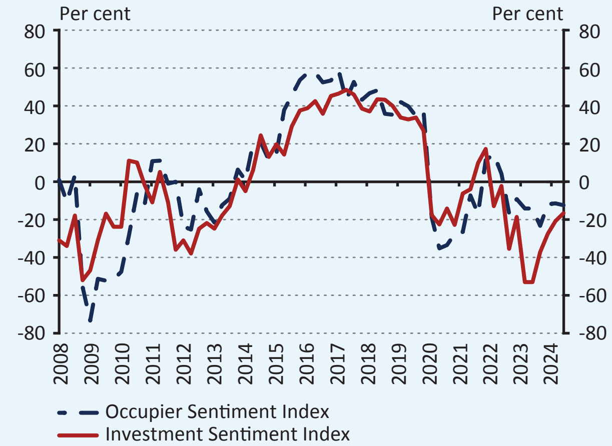
Chart 25
Three-month capital value expectations by segment



Note: Net ratio of respondents indicating increase and decrease in capital value. Based on responses from July 2024.

Source: RICS

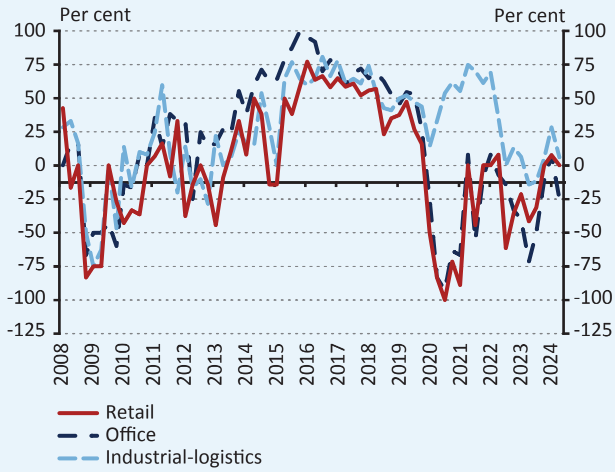
Chart 26
Development of Investment and Occupier Sentiment Index



Note: Based on responses from July 2024.

Source: RICS

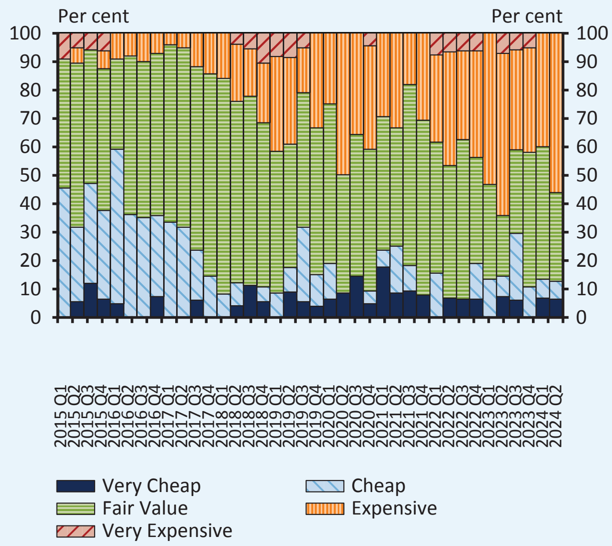
Chart 27
Development of rental demand by segment



Note: Net ratio of respondents indicating increase and decrease in capital value. Based on responses from July 2024.

Source: RICS

Chart 28
Valuation level of the commercial real estate market



Note: Based on responses from July 2024.

Source: RICS

Miklós Ybl

(6 April 1814 – 22 January 1891)

He was one of our greatest architects, belonging to the most prominent Hungarian masters of the 19th century. He was a representative of historicism on a European level. His reputation extended over the borders of Hungary not only due to his education, but also due to his works of art. His work covered several genres of art and he left a remarkably rich legacy. His early style was characterized by romanticism with Roman elements. He, later, dedicated himself to neo-Renaissance. He was an artist of major impact completing numerous assignments and receiving recognition in his lifetime. The design of symbolic, significant and long-lasting buildings of our national culture are associated with the name of Miklós Ybl.

He laid the foundation of his career in Hungary by completing international studies and gaining experience. Between 1825 and 1831, he was the student of the Imperial and Royal Institute of Technology (the Politechnikum) in Vienna. In 1840, he enrolled in the Bavarian Academy of Arts in Munich, and he went to Italy for learning purposes in 1841, which he repeated five years later. He started his work in the office of the well-known architect of the time, Mihály Pollack in 1832, then based on his referral he transferred to Henrik Koch in Vienna in 1836.

In 1841, he opened his first independent office named Architectural Institute together with Ágoston Pollack, the son of Mihály Pollack in Dorottya street in Pest. From 1843, he received a growing number of orders from the Károlyi family, for whom he worked as a royal architect until 1861. István Károlyi assigned the reconstruction of the castle in Fót to him in 1845. The assignment also included the designing of the adjoining Roman-Catholic church, which was built in Romantic style thus making reference to the Middle Ages. The church is considered as one of the most outstanding works of Miklós Ybl. Completing castle designs was a main part of his career. Of these works, it is worth mentioning the palace of earl Lajos Battyhány in Ikervár, as well as the castle of the Károlyi family in Parádsasvár.

The most important period of his creative years coincided with one of the most significant times of European urbanization. Among many other buildings, he designed the house with a passage on Múzeum Boulevard, the apartment block located at 17 Bajcsy-Zsilinszky road, as well as the Hungarian National Hall (Tattersall) during this period. The Tattersall was destroyed in the second world war. He designed the Customs House in Pest in 1870. His other prominent works included the bath at Margaret-Island, which was demolished after the second world war, and the House of Representatives at 8 Bródy Sándor street exhibiting the characteristics of the Renaissance Revival architecture (currently the Italian Cultural Institute).

His most significant works include the Hungarian State Opera House. A restricted tender procedure for its design was announced in 1873, which Ybl won. Construction started in October 1875 with royal support, and Miklós Ybl was soon made supervisor of the project. The Builders' rite was held on 7 December 1878, and the building was officially opened with the performance of Bánk bán on 27 September 1884, with the royal family also attending. At the same time, Miklós Ybl was working on the construction of the Castle kiosk and bazaar in Buda (1875-1882), which was built to resemble Italian, German and French hanging gardens. In 1882, he received the Cross of the Lipót-order, and was appointed a member of the House of Magnates by the king on 21 June 1885. Towards the end of his life, he continued the construction of Saint Stephen's Basilica designed by József Hild, and subsequently, he participated in the reconstruction of the Buda Castle. However, he could not finish this assignment, as he passed away on 22 January 1891.

COMMERCIAL REAL ESTATE MARKET REPORT

October 2024

Print: Prospektus Kft.

H-8200 Veszprém, Tartu u. 6.

mnb.hu

H-1013 BUDAPEST, KRISZTINA KÖRÚT 55.