Ukraine Real Estate Review

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SUMMARY

Ukraine's construction and real estate were among the first crisis-stricken sectors. Many development projects, already in construction phase, were frozen; those only planned - were postponed or canceled. Now developers are looking for investors; some of them are ready to sell their businesses entirely.

In the last few years the number of new development projects was growing swiftly. Developers were buying up land plots and planning grandiose projects of hundreds m^2. Money was pouring into real estate sector. Kyiv alone received about USD 950 million in 2007. The same 2007, investment growth into commercial real estate reached 380% y/y. New projects were growing in space, reaching one million m^2 of total area in multifunctional complexes.

Financial crisis ruined developers' far-reaching plans – they were faced with financing problem. As a consequence, many construction sites were frozen, as declared, at least for a year; investments into real estate significantly shrank; and the number of development projects 'for sale' increased.

Large-scale projects, especially those dependent on external financing, turned to be the least viable under crisis conditions. Less vulnerable seem to be small development projects in good locations, and promising high annual yields, preferably in excess of 25% interest rates.

Foreign Developers Freeze Their Projects in Ukraine

Already four foreign developers officially declared about freezing their Ukrainian projects. These are Russian Inteco and Mirax Group, as well as Austrian Sparkassen Immobilien and German ECE Projecktmanagement.

The first to make such official declaration was Russian Mirax Group, which in mid-September froze its Ukrainian project – multifunctional complex Mirax Plaza in Kyiv. This large-scale project was planned as a 46-storey two-tower building; the project was frozen when only 10 floors of the first tower were raised.

Next came Inteco, Russian construction company, owned by Yelena Baturina, Russia's richest woman and spouse of Moscow mayor, Yury Luzhkov. Inteco decided to withdraw from Ukraine – the only project they had here was residential district Moskovsky in Kyiv.

Austrian Sparkassen Immobilien was planning to invest into Ukrainian commercial and residential real estate about 500 million euro. January 2008, Sparkassen Immobilien announced about two deals in the office real estate segment, that the company was about to conclude. However, the company still does not have any projects in Ukraine. Austrian developer decided to take a time-out and freeze all their activities; they promise to be back in Ukraine but most likely with much less money to invest than initially.

One of the largest European developers, German Einkaufs-Center-Entwicklung Projektmanagement, which also planned to invest into Ukrainian real estate several hundred million euro, is freezing all ongoing negotiations on perspective projects and dismissing its Kyiv office staff of 30-40 employees. The ECE-Ukraine office will be closed in December, however, the company plans to keep 2-3 people to monitor the investment climate in Ukraine.

The main reason for all these withdrawals from Ukrainian market is the financial crisis, which so far has only slightly touched upon Ukraine. However, the situation aggravates because of unfavorable investment climate and political instability, which is unlikely to improve after another Parliament re-elections, planned for December.

Residential prices are gradually sliding down. The most affected are cities-millionaires, where housing market was overheated. Among the most overheated cities were Donetsk, Kyiv, Dnepropetrovsk.

In Donetsk, during the last 2-3 years residential prices were showing over 50% annual growth. This surge of prices was absolutely ungrounded. Now, when the number of deals is even fewer than during summer months, housing prices went down 15-20%. This tendency is especially evident on the secondary market, where apartment owners are eager to get rid of devaluating real estate.

Dnepropetrovsk housing market turned to be more rigid under crisis conditions; prices are going down but not significantly – just 5-10% so far. Price cuts are as well more wide-spread on the secondary market. Primary market is still waiting for the renewal of mortgage lending and cannot get used to smaller yields of residential projects.

Kyiv is still resisting inevitable housing slump. The number of deals on the secondary market is approaching zero, however, sellers are not physiologically ready to substantial price cuts. Kyiv housing market was the most speculative in Ukraine during the last few years and beginning of 2008. Therefore, those who invested in apartments here now refuse to believe that they might lose.

Kyiv oblast is less resistant to price decreases. Even primary market is already reacting to the crisis. Developers are ready to sell apartments in the first stages of construction at cost prices. For example, local developer T.M.M. decided to sell apartments in their residential complex in Obukhiv at cost price of $850/sq. m. in beginning stage of construction.

Tendency of price declining will persist. Given the expected economic recession and unlikely resumption of mortgage lending till financial crisis is over, prices will be forced further down.

Office and Retail Also in Trouble

Office and retail real estate, believed to be the most viable under crisis conditions, experience problems as well. Despite the shortage of high-quality office and trade centers, the majority of projects in these segments are also frozen.

In 2008, about 30 office centers of total area around 300 sq. m. were planned to be completed in Kyiv. Now it is obvious that at least half of them will not be finished this year. First of all, class A office space, which used to be in great demand, is the least likely to be completed on time – majority of office projects of class A are frozen.

Retail segment also suffers from financial crisis. In October, the number of Kyiv trade space rent deals shrank by 10%, while purchase deals – by one third. As a consequence, rental rates for nonprofessional trade space (usually first storey of residential buildings) went down by 10%. Nonprofessional trade space can be purchased now for a smaller price as well – on average prices declined by 15%.

Trade centers do not let prices down yet. However, they will be forced to do it very soon. Declining wages and rising inflation in Ukraine decrease purchasing power of population. Sooner or later, retailers will be leaving expensive trade centers and that's when the prices will drop.