Logistics: The New High Street. Is Greece Capable of Following the Example of Poland?

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Key words: Real Estate, Investments, Industrial, Logistics, Poland, Greece

SUMMARY

Many investors, especially pension funds and sovereign wealth funds, prefer to invest in real estate because real estate offers a stable income stream, attractive returns and the potential capital appreciation. At the same time, many investors start to seek alternative sectors to invest in order to move up the risk curve. One of these sectors is the industrial and logistics market. Could a country use this trend for its own benefit and growth?

During the last few years, Polish real estate sector seems to be a market that attracts investors not only from Europe but from all over the world. The main advantage of the Polish market is the location of the country. This strategic location facilitates the distribution of goods and products in the countries of central Europe. In this way Poland achieved high real estate performance, attracting investors from all over the world. Greece is a country that experiences a financial crisis and is in the seventh consecutive year of recession. Could Greece identify potential real estate investors in order for its economy to rise up again?

This paper is trying to answer this question and its aim is to identify the way Greece could take advantage of its logistics real estate market. Using an economic analysis, it is examined why the industrial and logistics real estate market is considered to be the new most attractive alternative real estate sector. By taking into consideration all the economic, political, geographical and social factors that could transform a country into an attractive real estate market, the specific fundamentals of Poland and Greece are described. The next section of this project concerns the comparison between the two countries. Finally, conclusions are drawn as regards the factors that drive performance in Polish logistics real estate market and help the economy of the country to boom. The result of this paper is the description of the way Greece would follow the Polish example.

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1. INTRODUCTION

Despite ongoing political, economic, and financial uncertainties, financial market globalization continues. Cross-border real estate investment has also been on the increase (Chen and Hobbs, 2003). Investors and managers try to take on more risks by allocating capital to secondary locations and assets as well as by investing in alternative sectors. Their objective is to generate more income and take advantage of possible yield compression and emerging dynamic sectors.

This paper sets the economic outlook of two European countries, Poland and Greece. At a second stage the real estate sector of the two countries is described. Then, the Polish and the Greek logistics market is presented. Finally, this paper tries to identify if Greece can follow the example of Poland and use the potential investments in the industrial real estate sector as a mean to boost its economy and improve its financial situation.

2. ECONOMIC OUTLOOK

2.1 Poland

With a population of about 38 million and GNI per capita of US$13,400 (2015), Poland has the largest economy in Central Europe (The World Bank, 2016).

Since the fall of the Iron Curtain, Poland has refashioned itself as a model of free-market economics. From 1989 to 2007 its economy grew 177 percent, outpacing its Central and Eastern European neighbours as it nearly tripled in size—the result of a series of aggressive measures taken by the government after the collapse of communism. Price controls were lifted, government wages were capped, trade was liberalized, and the Polish currency, the zloty, was made convertible. The policies left millions out of work but freed Poland to begin to recover from decades of mismanagement. The economy got a further boost with the country's entry into the EU in 2004 (Faris, 2013).

Table 1: Country Context, Source: The World Bank, 2016

Poland	**2015**
Population, million	38.0
GDP, current US$ billion	534.3
GDP per capita, current US$	14058
Poverty rate ($5/day 2005 PPP terms)	5.1
Life Expectancy at Birth, years	76.7

From September 2008 to February 2009, the zloty lost about a third of its value relative to the euro, before stabilizing later that year at about 70 percent of its peak value. The resulting boost in global competitiveness for Polish companies quickly accomplished a rebalancing that the euro area's weaker economies are still struggling to achieve. Measured in euros, the value of Polish exports dropped 15.5 percent from 2008 to 2009—but in zloty terms it grew 4.4 percent (Faris, 2013).
The drop in the zloty not only made Polish exports more competitive but also raised the relative cost of imports. The result was a boon for local companies, which increasingly are concentrating on quality (Faris, 2013).

If someone examines the current economic outlook, economic growth slowed in the first half of 2016 to 3.1% y-o-y, largely reflecting a surprisingly weak first quarter and a minor improvement in the second. Although private consumption grew at a robust pace of 3.2% accompanied by a 4.4% growth in public consumption, investment declined by 3.6% y-o-y in the first half of 2016. Exports and imports expanded by 8.9 and 9.6%, respectively, leaving the contribution of net exports to growth close to zero. The economic outlook remains favourable, with real GDP projected to increase by 3.2% in 2016 and pick up gradually to 3.4% in 2017 and 3.5% in 2018. Employment grew by 1.2% in the first half of 2016 after increasing 1.4% in 2015 (The World Bank, 2016).

The economy is expected to remain well balanced both internally and externally. Prices are expected to continue to fall in 2016, with low inflation forecast for 2017 and 2018. The external current account deficit is projected to increase only slightly to about 1% of GDP by 2018 (The World Bank, 2016).

2.2 Greece

As regards the economic outlook of Greece in 2017, the economy remains in recession and prospects of a swift recovery appear elusive. Since the agreement of the third adjustment programme in August 2015, the government has enjoyed cross-party support and has successfully pushed two sets of reforms through parliament. The next set of planned reforms have faced more sustained opposition, however, and many challenges remain to get the economy back on a more sustainable footing. The business environment remains very weak, with the continued imposition of capital controls and other restrictive measures undermining confidence. Both the import and export sectors have been hit hard by these capital controls, with imports falling by 6.9% in 2015, while exports fell 3.7%. Both sectors are expected to shrink even further in 2016. Fixed investment is forecast to contract by 8.9% in 2016 and is not expected to pick up until 2019 at the earliest. While the government has made some progress on the reforms as stipulated in the August adjustment programme, it is facing strong opposition on other reforms that have the potential to heavily impact on households. These include further cuts in pension entitlements, higher social security contributions, tax increases for farmers and the resolution of non-performing loans for SMEs and primary home mortgages. Greece has previously benefited from disagreements between its creditors on how it could best satisfy the terms of the bailout, but all of Greece's creditors came to a compromise in March. What this means is that Greece is going to face intense pressure for additional fiscal tightening, but also that debt restructuring will be considered in order to reduce Greece's debt service costs. In summary, the economic outlook for Greece remain highly uncertain and the prospects of a sustained recovery appear some way off (Simbouras, 2016).

Table 2: Greece, Country Context, Source: The World Bank, 2016

Greece	2015
Population, million	10.82
GDP, current US$ billion	194.9
Life Expectancy at Birth, years	81.2

3. ANALYSIS OF REAL ESTATE SECTOR

3.1 Poland

Direct and indirect investments in real estate are an important part of the capital market. Real estate development companies' and construction companies' shares and bonds, closed real estate fund investment certificates and units of open-ended equity funds in the real estate sector allow investors to invest indirectly on the Polish real estate market (Dittmann, 2016).

The real estate market in Poland enjoys an undiminishing popularity among investors. Low interest rates, attractive capitalisation rates compared to Western Europe, combined with mature and safe market as well as a growing economy attract both Polish and foreign investors. Other factors of great importance are the constant infrastructure development, the impact of new technologies, the growth of e-commerce and shared services centres. All this has contributed to the record-breaking volume of transactions in 2015, which exceeded EUR 4 billion, making Poland, once again, the leader in Central and Southern Europe (CSE) (EY Real Estate Group, 2016).

3.2 Greece

2015 included two national elections, a referendum, the imposition of capital controls and the signing of the third agreement with creditors. (PwC, 2016)

High unemployment rates, lack of liquidity and the unstable tax framework have created negative pressure on the real estate market during 2015. As a result, considerable delays have been recorded in the realization of various deals which had been under way. Expectations for positive investments returns and stabilization were not fulfilled during 2015. These events have caused further decreases of residential and commercial property prices in 2015. In spite of the negative conditions, the consistency in bringing forward structural changes, as agreed with the participating governments of the European Union, will embed a climate of trust and political and economic stability. This should lead anew towards expectations for positive economic effects and the recovery of real estate market. Specifically, during 2015, the first signs of the aforementioned conditions have made their presence felt through the low number of residential and commercial property transactions which have taken place. Surely, one needs to note that many of these transactions were probably distressed sales. The unwillingness of a large number of owners to conclude a sale was prevalent as they expected that higher prices would be recorded in the near future (Andritsos, Mavraganis et al, 2016).

4. ANALYSIS OF LOGISTICS

The location of logistics activities and the infrastructures to support them are important strategic components for the competitiveness of the sector. A logistic zone should be viewed as an integrated space whose competitiveness is determined by a variety of factors. The most important factors to consider are the following: connections with backbone transport infrastructure (rail, road, airports, and ports); access to a qualified workforce; charges (fees and taxes) for services (such as good road access, illumination, availability of public transport for the workers); proximity with complementary activities (horizontal integration) and/or users and contractors of upstream or downstream services (vertical integration); distance from the consumer and end-markets; potential for two-way transport (to avoid empty loads on return trips); cost of land and construction; social, environmental, and political risks. To be competitive and efficient, a logistic zone should be planned not only thinking of the needs of the industry today, but also of its developments several decades from now (e.g., large access roads to accommodate the ever larger trucks and containers, flexible and easy to restyle facilities, etc.) (The World Bank, 2013).

4.1 Poland

At the end of 2015 total modern industrial stock in Poland stood at 9.9 million sqm, with Warsaw and its suburbs accounting for the largest share (around 30%). Improving transport infrastructure have facilitated the development and expansion of the other core regions such as Upper Silesia, Central Poland, Poznan and Wroclaw, which together contain nearly 59% of the country's total stock. Given the number of warehouse schemes under construction, these regions are expanding and therefore further strengthening their position on the Polish industrial map. The smaller markets of Tricity, Cracow, Lublin, Szczecin, Rzeszow and Torun are becoming increasingly attractive for occupiers and developers. Together they account for 11% of Poland's total stock, up two percentage points from last year (Cushman & Wakefield, 2015).

The first quarter of 2016 saw a continuous increase in the development and demand activity on the modern industrial market in Poland. At the end of March 2016 total warehouse stock exceeded 10,300,000 sqm (Cushman & Wakefield, 2016).

The take-up in Q1 2016 was high, with approximately 637,000 sqm of warehouse space leased. This was an increase by 8% (45,000 sqm) compared to the same period of 2015. The first quarter still indicated a healthy development activity, with some 783,000 sqm of modern warehouse space under construction (Cushman & Wakefield, 2016).

Headline rents remained flat or fell slightly in core warehouse markets in Poland. The highest rents were posted in Warsaw's inner city (EUR 4,00–5,40/sq m/month); the lowest were in Central Poland (EUR 2,40–3,95/sq m/month) and in the Warsaw Suburbs (EUR 2,40–3,80/sq m/month). In the remaining regions rents were around EUR 2,70–3,60/sq m/month (Cushman & Wakefield, 2015).

On the warehouse market, the vacancy rate is lowest ever, amounting to only 4.6%. The great demand and interest in the sector stems, among other things, from the dynamic growth of e-commerce (EY Real Estate Group, 2016).

4.2 Greece

Most logistics zones in Greece have developed without planning, generating inefficiencies in the facilities. Logistics zones (for warehousing, container depots, truck depots, etc.) in Greece have clustered in relatively few areas. In the Attica region, the main concentration is in areas connected by Attiki Odos: Mesogeia, Asporpyrgos, Mandra, Magoula, Elefsina, and Thriasio. Small-scale logistics activities are concentrated closer to the centre of Athens in Elaionas. The warehouse facilities have developed over time and clustered without planning or attention to the special needs of the industry. The warehouses were built on land with different uses (industrial, commercial, unclassified), and sometimes with ad hoc specifications and no proper authorization. Not all buildings are compliant with zoning or safety regulations, especially in Elaionas. By contrast, the more recent Sindos zone in Northern Greece is a planned logistics zone with adequately designed layout and multimodal access. When the authorities developed the Sindos industrial park, a majority of investors were logistics companies interested in taking advantage of the exceptional location of the park. Another planned but different concept has been the Thriasio Pedio multimodal logistics centres operated by Gaiose, the real estate management company of rail facilities, where relatively small spaces can be rented (The World Bank, 2013).

In the logistics property submarket, there has been limited investment activity in 2015. Slight upgrade trends were witnessed during the 4th quarter of 2015. Supply for new logistics space has remained limited, primarily due to the unwillingness of developers to break ground without concrete prospects of signing with buyers or tenants, while at the same time limited big deals concerning such properties have been consummated. During 2015 there has been an increasing trend in demand with prices and yields remaining in the same range as in the previous period for both industrial properties and warehouses. Modern warehouse space (large internal height, high standards of construction, support function offices, ramps etc) is increasingly sought after. Small to medium size warehouses (1,000-2,500sqm) are considered more attractive, thereby achieving rents of €1 – €2.5 per sqm. Logistics properties of older construction and lower quality remain vacant. For these properties, despite the collapse of rents, which often reach levels close to €1 per sqm, demand remains quite low. It is worth mentioning that the demand increased for logistic spaces along the National Highway (from Metamorfosi to Krioneri) and decreased close to Attiki Odos and to Aspropirgos (Andritsos, Mavraganis et al, 2016).

Average rents in the primary areas of Attica remain between €2.5 and €4.0 per sqm per month. In standalone cases of modern properties, slightly higher prices are achievable depending on their location and specific characteristics (Andritsos, Mavraganis et al, 2016).

5. CONCLUSIONS

Real estate market and real estate prices are closely linked with general economic cycles (Wang, 2003). Hon-Chung (2009), Ludwig and Slok (2004), Case et al. (2005), Bardham et al. (2007), Goodhard and Hofmann (2007) and Zhang and Wu (2008) argue that among macroeconomic factors related to the real estate prices, the key factors were gross domestic product (GDP), unemployment, share index, current account of a country, demographic factors, household income, interest rate, industrial production and consumption of households.

International real estate investment represents considerable decision-making, organization and managerial challenges above and beyond the problems of achieving the desired cash flows at the building level. One means of mitigating risk is through the process of portfolio diversification. Diversification simultaneously pools and subdivides risks. Diversifiable risk is also referred to as unsystematic risk or idiosyncratic risk. It is the portion of the total risk of an asset that is not captured by its beta. Unsystematic risk is the risk unique to a particular asset. Since investors can eliminate unsystematic risk from their portfolios by diversifying, they are not rewarded for taking this risk (Kevenides, H., 2002).

One of the most compelling reasons for investing abroad is diversification. Once properly diversified, a portfolio is less exposed to risk, but consequently also closer to average rather than maximum returns. This trade-off between risk and return is known as the risk-return frontier (Kevenides, H., 2002).

In order to minimise the risk, an investor should analyse all the potential risks that a potential investment could have. Some of these risks are mentioned below.

<u>Political Risk</u>:

Country risk analysis involves an examination of a country's economic outlook and the stability of its government, as well as such factors as corruption, the crime rate, and the possibility of expropriation. In addition to these risks, real estate is also subject to numerous legislative and regulatory risks, such as changes in tax laws, rent control, zoning, and other government-imposed restrictions. There is no unanimity yet on what constitutes political risk in a given country and how to measure it. Measures of political stability may include the frequency of changes of government, the level of violence, the number of armed insurrections, conflicts with other states, and so on (Kevenides, H., 2002).

<u>Business Risks</u>:

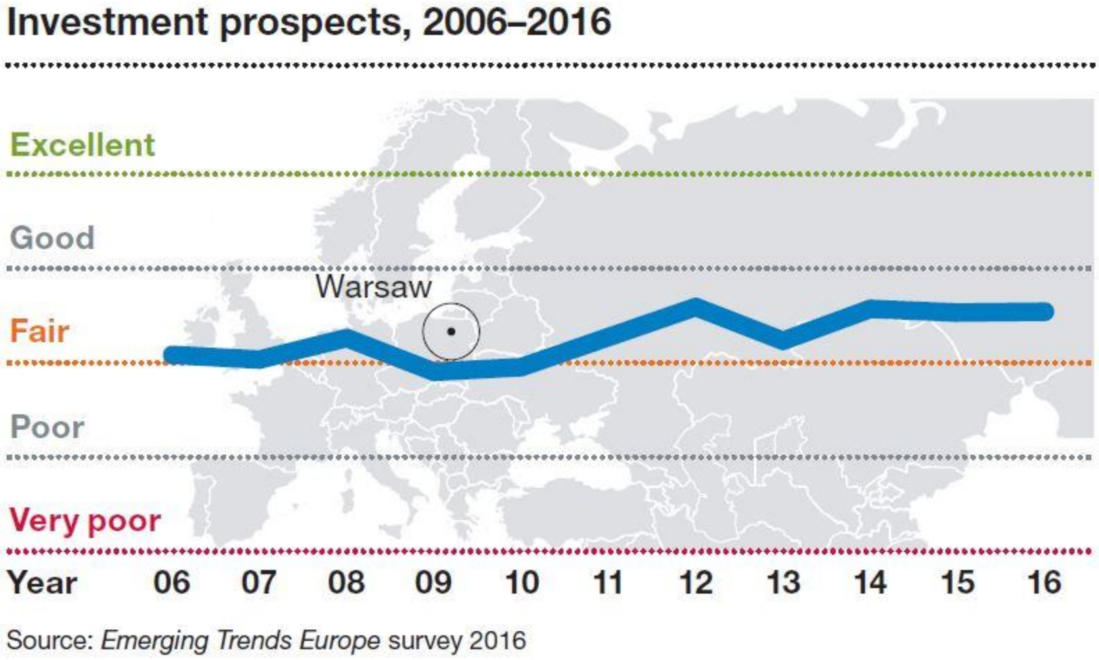
Business risks involve changes in occupancy rates, the level of new construction, and zoning and permit regulations, as well as additions to the competitive supply. Other risks include labour problems and moratoria on various types of utilities, for example gas, sewers, water, and electricity (Kevenides, H., 2002).

<u>Risks from Unsound Monetary and Fiscal Policies</u>:

Fiscal irresponsibility is a sign that a country is likely to be politically risky. The government deficit as a percentage of gross national product is a risk indicator. The higher this figure, the more the government is promising to its citizens relative to the resources it extracts in payment. The greater the deficit, the higher the possibility that the government will not be able to keep all its promises without resorting to expropriations of property (Kevenides, H., 2002).

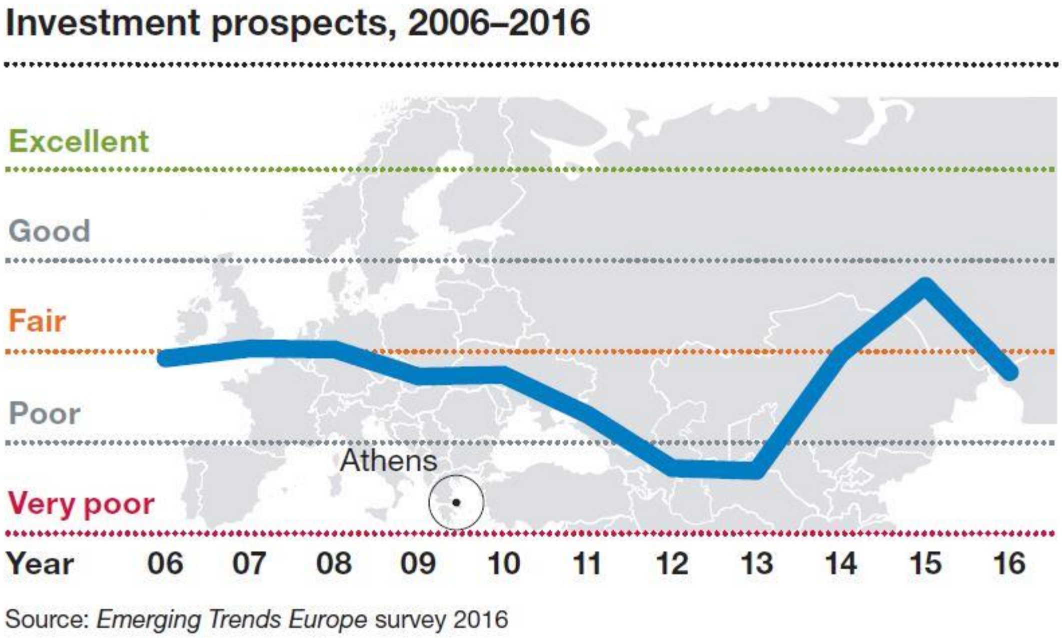
Greece is a country that has high political risk as well as risks from unsound monetary and fiscal policies. The financial crisis that the country experiences in combination with the capital controls that were imposed in July 2015 increase this kind of risks. The debt crisis in Greece creates uncertainty and many investors feel insecure. As a result Greece’s real estate market shows high volatility.

The graphs 1, 2 taken from the *Emerging Trends Europe* survey show the investment prospects between 2006 and 2016 in Warsaw and Athens accordingly. Concerning Warsaw, the investment prospect in the Polish capital starts to increase slightly after 2013 and seems to be stable until 2016.



Graph 1: Investment Prospects, Warsaw, Source: PwC, 2016

On the other the investment prospect in Athens, the capital of Greece, was declining until 2012. After 2013, the investment prospect started to increase. However, another decline is observed in 2016.



Graph 2: Investment Prospects, Athens, Source: PwC, 2016

Despite the fact that someone initially could argue that Poland and Greece seem to have a totally different investment prospect, by a more detailed analysis and through another perspective the two countries present some similarities. Until 2010, Poland and Greece have the almost the same investment prospect and after 2013, in both countries it increases.
Logistics constitute a significant pillar not only of the Polish real estate sector but also of the whole economy of Poland.

Efficient logistics can play an important role in Greece's recovery in several ways: It can reduce the costs of importing and exporting; it can contribute to GDP growth as a service sector; and it can reduce the fragmentation of the domestic economy, thus improving economies of scale and productivity. Greece is geographically and economically well-located. Piraeus Port, the deepest seaport on the Mediterranean, is close to the Mediterranean maritime route and has already started developing as a significant trans-shipment centre. Both Piraeus and Thessaloniki have the potential to evolve into gateway ports to South East Europe and Central Europe. Provided that a long-distance, reliable railway connection can be established, Greece can take advantage of the economic growth in Eastern Europe and the regional production networks established between Eastern and Western Europe. Becoming a regional gateway will require competitive logistics along the whole supply chain, in addition to efficient ports and railway connections (The World Bank, 2013).
Therefore, logistics could contribute to the Greek economy and improve the financial situation of the country. However, in order for something like this to happen many changes should occur.
Changes to other sectors are necessary to push Greece's logistics industries to mature. Some factors holding back the modernization of the logistics industry are directly related to the design and implementation of government regulations. In particular, licensing issues and regulations surrounding the construction and fire-protection of warehouses should be simplified. The steps required for becoming a third-party logistics provider, also, should be simplified and clarified. In

addition, the government should take more steps to support the provision of appropriate services to providers of logistics services, such as allowing the construction of roads appropriate for industrial traffic and working with business-owners to find appropriate solutions for waste disposal (The World Bank, 2013).

In case that some of the above happen, the Greek industrial market could attract local and foreign investors. The Greek logistics could become an alternative real estate sector that could help many investors to diversify their portfolio by moving the risk curve and to have expectations of high returns from an uprising market.

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BIOGRAPHICAL NOTE

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