PROPERTY

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Investors look east again

INSIDE: Polish residential real estate is regaining popularity

PLUS: New stadiums have been springing up thanks to commercial tie-ups

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In This Issue

Investors wary but optimism returns
POLISH REAL ESTATE Jan Cienski examines whether investing in residential property in Poland is worth considering or if it should remain the preserve of locals **Page 4**

Effort to make best of a bad moment
REITS The sector has not enjoyed an easy start, although there are hopes that tax-efficient property vehicles will emerge as part of the market recovery **Page 4**

Builders braced for hard times
CONSTRUCTION Falling government spending is forcing companies in the sector to re-examine their business models and may lead to large-scale redundancies **Page 6**

Bankruptcy protection withdrawn
COEUR DEFENSE An unexpected court decision to remove bankruptcy protection for the Paris office building has implications for property investors in France **Page 6**

Life reflects architecture for Vitra
EDWIN HEATHCOTE The FT's architecture columnist explores the Swiss furniture maker's buildings that have been designed by the world's top architects **Page 7**

Build it and hope they will come
SPORTS STADIUMS Roger Blitz says commercial tie-ups have been a boon for sports arenas but developing existing facilities is a better and safer option for most clubs **Page 8**

Front page: Warsaw property attractive again Alamy

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Rising again: Warsaw's popularity among property investors is growing Alamy

CEE investors start to emerge from cover

Daniel Thomas says competition for the best assets is increasing but volumes remain low

Life has returned to the key property markets in central and eastern Europe after a two year slump, although investors warn that the region is not out of the woods.

Property investors were badly stung by the fall in the market, with many having sought out risky investments during the boom.

Such losses are being curtailed now, with the key markets of the region showing definite signs of recovery, helped in part by the bounce in values in more established markets such as the UK that has priced out some investors.

International buyers are back in the region, with local agents reporting competition for the best assets.

The markets across central and eastern Europe varied enormously in terms of performance and activity levels over the two years of the property slump. Some, such as Poland were among the most resilient in Europe.

However, the more niche markets further east were particularly hard hit. Markets collapsed in countries such as Ukraine – once the great hope of the entrepreneurial property investor – while a dearth of transactions has made it difficult to even establish pricing in Romania and Bulgaria.

Slovakia and the Czech Republic fared better, although Poland is almost on its own in attracting significant interest from established property investors keen to buy into a market still near its cyclical lows but where fundamentals support a recovery.

John Duckworth, managing director for CEE at Jones Lang LaSalle, says: "Last year saw a differentiation of the CEE markets. Poland, and to an extent Czech Republic, are being viewed in a different light. The pool of international investors may be smaller than before, but at least they are active again."

Poland has weathered the downturn better than its neighbours, with GDP growth of 1.7 per cent in 2009, helped by resilient private consumption.

Ian Coull, chief executive of Segro, the UK real estate investment trust, which has maintained a development business in Poland, says: "We like Poland a lot. It never stopped growing economically. It is a vibrant country with a good domestic economy.

"Our focus is on the major cities, as outside these hubs it is a bit like going back in time."

Alex Jeffrey, chief executive of MGPA, the private equity fund manager, which last month completed a €235m acquisition of two shopping centres in Poland, says: "As the largest country within the region and the only jurisdiction in Europe to have avoided recession in 2009 we are expecting investor activity to return strongly."

Advisers say that knowledge of the local market has never been more important. Institutional investors have been looking for opportunities in core central European markets, said Mr Duckworth, with a focus on prime office and retail properties in capital cities that offer long-term rental income from strong international tenants.

The nature of the market means that this has kept volume low – there is relatively little prime stock available. Vendors are also reluctant to sell at the bottom of the market.

> 'The pool of international investors may be smaller than before but at least they are active again'

Investment increased in the last months of 2009, taking volume for the region to just over €2bn, according to Jones Lang LaSalle. This was still a third of 2008 turnover, however, showing that the recovery has only just begun.

Central Europe accounted for more than half of turnover, focused on Prague, Warsaw and Budapest, according to CBRE, while south-east Europe's share fell by half to 12 per cent and eastern Europe to 32 per cent in 2009.

During the boom years, many investors were forced to back developments owing to the lack of quality property. Those who failed to build are now holding land that some deem close to worthless in current conditions. But, agents say, there could once again be a shortage of new schemes.

The reduction in central and eastern Europe's office development pipeline since the end of 2008 will have positive effects on the market, said CBRE, which expects office space completions in the next 18-24 months to be down almost a third from the end of 2008, as projects under construction are postponed or cancelled.

Development is unlikely to start again until after the financial markets open for speculative development funding.

PMA, the research house, is forecasting rental growth in prime Warsaw offices of more than 10 per cent in 2013 and 2014, for example. This could mean that a well-timed development will make considerable profit.

Vacancy rates remain high in many markets, however. Hans Vrensen, head of research at DTZ, says that office take-up was a mere 1.6m sq m in 2009, a 43 per cent decrease on the previous year.

Prague was the most resilient, down only 6 per cent, while Bucharest, Moscow and Warsaw all saw falls of more than 50 per cent.

Availability increased across all markets to 15.6 per cent at the end of the year, representing a threefold increase on 2007 figures. Markets such as Kiev and Moscow that saw the largest development boom experienced the sharpest rental correction.

Such factors will weigh on sentiment, although the money – both new and old – now targeting the region should ensure that demand remains high, even if the majority is seeking very specific product in well-let prime buildings.

There is expected to be a flood of new capital, as sentiment swings behind real estate again. There are a number of funds being prepared by the sort of UK-listed asset managers that came to dominate the market during the boom.

Ashmore, the listed asset manager, has raised $45m for a Russian real estate fund, for example, aiming to exploit the failed property bets of highly leveraged investors. Similarly, the First Property Group, another UK-listed company, is to launch a property fund with a focus on Poland.

Most of the money is still expected from existing investors, however, including domestic buyers that can again afford to invest.

Sparkassen Immobilien, Austria's largest property investment company, is looking to increase its holdings across the region substantially over the next two years, purposefully avoiding Austria and Germany, which are not considered growth markets any more.

There remains a lack of readily available bank debt, but investors are overcoming that using their own equity. Sparkassen said that the Serdika Centre in Sofia, for example, was developed with the company's own equity, to be leveraged after it opens in March this year.

Debt will also remain an issue. There will be further distress among existing property owners, with more expected to follow Orco, which invested across the region but has breached banking agreements.

However, banks will also be reluctant to force fire sales through foreclosures because of their large exposure to the market.

As such, the market can expect to see a drip feed of properties rather than a glut, which will be healthier in the longer term, as there is less chance of sudden oversupply.

Crucially, demand is holding up, particularly in Poland. If the numbers of investors now boarding flights to Warsaw is any indication, the market could bounce strongly over the next year.

New trades bring life to the market

Derivatives

Following the recession, there has been evidence of steady growth, writes **Daniel Thomas**

The property derivatives market was hit hard during the recession, with volumes falling sharply as investors stayed clear of anything associated with real estate.

With the market now in recovery, there are hopes that derivatives trading – effectively investing in an index based on the movement of underlying property values – could mature into a strong investment option.

But with continued uncertainty over the recovery in the physical real estate market, traders say that derivatives could give investors an edge by offering the chance to hedge out some risk – for example, stripping out capital growth to lock in income returns.

Derivatives also allow investors struggling to find property in a supply-constrained market to gain exposure to real estate in a liquid and low cost format. However, the size of the market remains a constraint, as finding counterparties is not always easy.

The final quarter of 2009 saw 99 separate trades worth just less than £1bn in the global property sector, bringing the annual total to just over £3bn – the lowest annual turnover since 2005; trading volumes reached £7.7bn in 2008 and £8.3bn in 2007. Over the final quarter, the average deal was worth £10m.

The fourth quarter completed a year of continuous steady growth, however. It is hoped the market will continue to attract participants to boost volumes.

In fact, traders are pinning their hopes on signs that there is an increased interest in derivatives among large institutions. An increase in these "end users" could drive trading in future.

Institutions are attracted by the market's growing sophistication. Since it started in 2005, most investments have been executed on the overall IPD (Investment Property Databank) index.

However there was a landmark trade by Prudential's property fund management arm, Prupim, that used underlying sector indices at the end of last year.

This meant that the fund manager could bet on regional offices while shorting the index against retail warehouses.

This reflects more closely the choices made by a typical fund manager in assigning money to different parts of the market that have lagged behind the recovery, or pulling money or short-selling other parts that have grown too fast.

Nick Scarles, chairman of the property derivatives group of the Investment Property Forum and Grosvenor's finance director, says: "It is reassuring to see a fourth quarter of continuing increase in derivative volumes; but the milestone was Prupim kickstarting sector activity with its £100m of trades with RBS.

"Sector trades open the market to a wider group of end users who have been held back by the inability to trade in the sectors in which they specialise, as well as portfolio manages seeking to fine-tune their sector exposures."

The market has also been slow to take-off internationally, which has been seen as a weakness in the past. The UK accounted for the vast majority of deals traded last year, with domestic traders executing 88 of the 99 trades in the last quarter worth £907m.

France, in comparison, saw just seven trades worth £44m and Germany, three trades worth £15m, a modest pick-up after successive dormant quarters.

Since the beginning of the market, trades have in fact been completed on IPD's Australian, Canadian, Italian, Japanese, Spanish and Swiss indices, although there remains liquid trading only in the French and German indices outside the UK.

The US has been surprisingly slow in creating a derivatives trading platform, given the size of the real property market and the use of indirect investment in other parts of the market.

This could change, given the IPD's attempts to establish its own index in the region. Part of the problem has been a lack of a single recognised set of data to track the US property market, which tends to be fragmented, given its size.

Signs of interest: Institutions are attracted by the market's growing sophistication Alamy

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GTC's caution pays off

When Eli Alroy arrived in Warsaw in 1994, he says two words best described the Polish capital: "cold and old".

While not much can be done about Poland's geographical location, the second adjective presented a big opportunity for the nascent real estate developer who had just arrived from Israel to set up Global Trade Centre (GTC), now one of central Europe's leading property companies.

"The impression was that a lot of face-lifting had to be done here, but we saw a lot of prospects," says Mr Alroy, chairman of GTC's supervisory board. "There was risk but we had drive."

Coming to Poland not long after 1989, when the country shrugged off 45 years of communist rule, may have been risky, but it was a time of opportunities that today's developers can only dream of.

GTC's first investment was a 7ha site in the southern Warsaw district of Mokotow – then home to crumbling factories, including a decrepit semi-conductor manufacturer.

The old plants were cleared away and GTC began construction of a low-rise office park – Warsaw's first modern office development that quickly became one of the capital's business hubs.

> The company has stuck with its careful approach, shying away from expensive high-rises

"The expertise of GTC is to take a big piece of land, put together a project and implement it in phases," says Mr Alroy.displaying an easy informality in his blue polo shirt and unzipped sweater.

The opportunities he helped uncover were a far cry from his previous experience in Israel, where the market is a lot smaller and the competition fierce. "It's difficult to have a big vision there," he says.

GTC then began the development of Warsaw's first modern shopping centre at one edge of its Mokotow property.

"We were the first to see the opportunity for shopping malls in Poland," says Mr Alroy, in his headquarters, a stone's throw from Galeria Mokotow, one of Warsaw's largest and most successful shopping centres, which was completed in 2000.

Having gained experience in commercial and retail development, GTC then built the city's first modern residential compound, a grouping of apartment buildings, complete with shops and a swimming pool.

"Today, it's not very impressive, but it was pioneering," says Mr Alroy.

The company has stuck with its careful approach to development, shying away from glamorous, and expensive, high-rises by first acquiring large swathes of land and then conservatively developing it in stages.

One of its more recent efforts is a 47ha site around the American school, on the southern edge of the capital, which has been turned into a slice of US-style suburbia.

It is the same method that the company has used as it has expanded, first to other Polish cities and then to the rest of central Europe. About 35 per cent of the company's business is in Poland, 20 per cent in Hungary, 13 per cent in Romania, 7 per cent in Bulgaria and the rest scattered across the region.

The company has grown rapidly. In 1996, it was valued at $25m. When it listed on the Warsaw Stock Exchange in 2004, it was worth $400m.

At present, it is valued at $2bn – although that is half of what it was two years ago before the crisis that hit central European real estate.

GTC's geographic reach did not provide a lot of protection, thanks to the global nature of the crisis, but its technique of building incrementally did.

"We stopped all new development," says Mr Alroy.

The company had a series of lucky breaks before the crisis hit, which left it with decent cash reserves.

It sold its share in Mokotow Business park for $287m in 2006, two projects in Prague and Romania in 2007, raised €200m in financing at low interest rates in 2007 and it raised an additional €100m on the stock market.

With its reserves, GTC has a loan-to-book value ratio of only 42 per cent.

In the first nine months of 2009, it made a loss of €43.6m (mostly because of the revaluation of investment property), compared with a profit of €135.9m for the same period in 2008.

Mr Alroy sees a limited revival this year followed by a definite turnround by 2011, as supply slowly dries up because of the financing troubles experienced by many developers.

GTC is already beginning to edge back into the market, restarting work on shopping malls in Croatia and Bulgaria.

Jan Cienski

Investors wary but optimism is returning

Analysis

Jan Cienski undertakes a survey of Poland's residential property market

Jacek Socko is doing something that many Poles had long shied away from: he is looking for a Warsaw flat that he hopes to pay for using a bank loan denominated in foreign currency.

"The time to buy is good. Prices have fallen over the past 18 months," says Mr Socko, a currency trader, who was attending a recent residential property show in Warsaw with his wife as they hunted for a 70 sq m apartment.

The show, one of the first in Warsaw this year, was crowded with other potential buyers, a sign that the loss of confidence in the local residential real estate market may be ending.

However, conditions are still not back to the exuberant times of the boom, as attested to by a banner advertisement in front on one developer's booth, which promises a Fiat 500 car with every flat sold.

"We are coming out of a period of stagnation, when almost nothing was being built," says Emil Szweda, an analyst with Open Finance, a real estate consultancy.

He adds that Warsaw prices have fallen just over 10 per cent from their peak.

"The market hasn't collapsed, it has simply returned to normal," he comments.

Financing loans in euros, and especially in Swiss francs, was enormously popular during the property boom that ended in 2008, because interest rates for those currencies were much lower than for loans denominated in Polish zlotys.

But the economic crisis caused the zloty to sag against the franc and the euro, driving up monthly payments and spooking both banks and potential borrowers.

Banks are now much more reluctant to lend in anything but zlotys, although many clients are still angling for forex loans – where the interest rate is about 4 per cent – because these are substantially cheaper than zloty mortgages, where the annual rate is currently more than 7 per cent.

"Taking a zloty loan is more expensive," says Mr Socko. "I am a little worried about currency swings, but we will eventually join the euro, and then the problem will go away."

Getting that loan may be difficult. Poland's banking regulators recently brought in a new recommendation toughening up earning requirements for potential borrowers, and introducing stress tests to ensure borrowers are not over-extended – all aimed at ensuring that banks do not get carried away, as the market revives.

"If the new recommendation is strictly enforced, it could reduce the number of loans," says Mr Szweda, worrying about a potential negative impact on prices.

He estimates that the number of new loans will rise by 10-15 per cent this year, signs that the residential market is shaking off the doldrums of the past 18 months.

Serge Klugman, whose company, Laor Development, is building projects in Warsaw and in western Poland, says that the past two years have been difficult, but that he now sees a revival of interest, albeit at lower prices than before the crisis.

The building he is completing in Warsaw is selling for about 9,900 zlotys (€2,475) a square metre, while flats would have sold for about 12,000 zlotys a square metre two years ago.

"I think the market will improve," he says. "Poland has had a good crisis and demand is still strong."

Even companies severely battered by the downturn, such as the Franco-Czech developer Orco, are seeing signs of a turnround.

The company is hoping to restart construction on its flagship Warsaw project, a city centre residential tower designed by Daniel Libeskind where workers have been absent for months.

> The crisis has changed the market, with flats – especially larger and more expensive ones – giving ground to houses

Jean-François Ott, Orco's chief executive, says: "This year is going to be a transition year, I don't believe in a sharp bounce. But in the mid-term we will see an improvement."

The crisis has changed the residential market, with flats – especially larger and more expensive ones – giving ground to houses often owner-built in suburbs that are as far as 20km from Warsaw's boundaries.

While the number of flats started by developers fell by almost 40 per cent last year, the number of private homes remained almost unchanged.

For now, the residential property market is almost exclusively of interest to Poles, many of whom are moving from smaller towns to larger cities in the search for jobs.

In the recent past, Poland attracted speculators, many of them small-scale, from such places as Ireland, Spain and Israel, who had seen their own property booms and were hoping to get a piece of the action in Poland's rapidly growing market.

But with the global decline in property, investors are nursing their wounds at home, and not looking at Poland.

"There are no investors on this market," says Mr Szweda, noting that the return on a rental apartment is only about 4.5 per cent, less than a bank deposit, and that prices are unlikely to change a lot in the foreseeable future.

"I wouldn't bet that apartment prices would be much higher two or three years from now than they are now."

After two years in the doldrums, construction work is happening again in Warsaw Alamy

Effort to make the best of what was a bad beginning

Reits

The investment vehicle has underperformed, writes **Daniel Thomas**

The real estate investment trust sector in the UK has not enjoyed the easiest of beginnings, although there are hopes that the tax-efficient property vehicles will eventually emerge as an important part of the market recovery.

The performance of Reits around the world has been broadly similar during the crash, although prices in the US and UK have rallied most since 2009 – in part because they were the first markets to peak.

However, UK Reits have underperformed the FTSE as well as non-Reit peers, even in the recovery phase.

Daniela Lungu, director of CB Richard Ellis Investors, a fund manager, says that one could be forgiven for believing the regime has proved a failure. However, she points out that the conversion coincided with a 20-year peak in the property market, and "everything from then on was bound to look less attractive".

"In many respects, the Reit regime was launched at the right time for the UK Treasury and at the wrong time for the UK commercial property sector," says Peter Beckett, a director at Ernst & Young. Nonetheless, groups that converted were able to write off significant amounts of latent capital gains tax and have enjoyed a tax-free regime since."

David Atkins, chief executive of Hammerson, admits that the timing was not ideal, but says this was not the fault of the legislation. "The timing was at the peak of the market, but it gave the Treasury the push to sit up and apply itself. So, while it is theoretically right to say that we would rather convert today, maybe the Treasury would not have applied itself."

More importantly, he says, the framework was not to blame – it has proven successful in allowing companies access to the capital markets. Reits have sold more than £7bn of properties in the past three years, according to DTZ, with a similar amount raised through equity raisings.

Mr Atkins says: "We all raised money when we needed it, so it shows that the market is an effective way to access capital. I think Reits have a great future. The problem is that the sector remains too small, but we will see more IPOs and investor interest."

However, there remain barriers to entry into the regime. Reits incur up to a 6 per cent charge on the market value of properties – 4 per cent stamp duty in addition to the 2 per cent entry charge.

Pete Sudell, executive director at BNP Paribas Real Estate, says: "Today, with values having fallen as low as they have, the advantage [of reduction in capital gains tax liabilities] is not so apparent and may not exist for several more years."

Reits aim to provide returns to investors that mirror those of owning the property directly but with greater liquidity. The tax-efficient status is internationally recognised – certain funds are even required to allocate funds to Reits – which has meant an influx of investors into the UK. For some companies, according to Berwin Leighton Paisner, international investment has doubled.

But there has been little evidence that the retail shareholder base has increased, which was a primary aim.

Ian Coull, chief executive of Segro, says: "I don't think Reits have worked as well as we hoped. The conversion issue was just bad timing. But Reits were designed as a place for retail investors to get exposure to the market, as in other countries, but has not worked as well here."

The regime was created in a bull market, which has meant that the industry has spent the years after it started trying to have the legislation amended to reflect a more normal environment. The UK government has so far ignored such requests.

There are broader changes needed to create a functioning sector, according to Chris de Pury, partner at Berwin Leighton Paisner. These include amending legislation for residential property Reits, as well as for mortgage Reits, which could be a way of helping banks reduce their exposure to real estate.

> 'With values having fallen as low as they have, the advantage is not so apparent'
>
> **Pete Sudell, Executive director, BNP Paribas Real Estate**

Adrian Levy, partner at Clifford Chance, says the wishlist would also include Aim Reits and an allowance for stamp duty. Even so, he says, the market is still large on a global scale and should prove good in the long run.

New companies could also be spun out of the large portfolios of properties held by the banks. At present, Reits are more likely to take advantage of the banks' desire to rid themselves of property by buying, joint venturing and asset managing.

Simon Clark, a partner at Linklaters, says: "There are two ways in which activity will commence: 'natural' Reits, the next step in the maturing of a business ready to come to market, and 'solution' Reits, where a Reit is the most appropriate exit."

Examples of the second sort include distressed loan books, a real estate fund that needs to restructure or the assets underlying a CMBS issue which is in trouble. But, as much as there is scope for change to the structure of Reits, there are also questions about the functions of existing vehicles. The decision by Liberty International to split its business has reopened the debate about whether Reits operate best as sector specialists or conglomerates.

Meanwhile, some investors want Reits to be simple cash providers, paying out a steady high dividend. This can – and some say should – inhibit development work, as well as the trading of properties. Instead, many UK Reits are run as active property companies, focusing on asset value generation rather than cash flow.

But others say that the market is working as it should – albeit with unnecessary constraints on conversion for new companies.

Phil Nicklin, a partner at Deloitte, says: "Reits fundamentally improve shareholder returns – by about 10 per cent for retail investors and 40 per cent for pension funds. You can certainly argue that the 2 per cent conversion charge now looks too high, but the system itself is proven to work for investors."

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Builders braced for hard times

Construction

Falling government spending is forcing companies to re-think their business models, writes **Ed Hammond**

Building companies in the UK are expecting this year's general election to be a trigger for fresh hardship, as government spending on expensive infrastructure projects is reined in.

Construction companies have come under intense pressure during the downturn, with overall activity falling about 12 per cent last year – the biggest fall since records began in 1955.

Even optimistic forecasts do not see much in the way of recovery before 2011, while a significant rebound is not expected until closer to 2020.

During the past 18 months, publicly funded infrastructure projects such as new schools and hospitals have offered a lifeline to recession-battered construction companies.

Their dependency on public sector contracts has been growing for a few years – in 2009, some 70 per cent of the 20 largest contracts in the industry were placed by government bodies. However, with sweeping cutbacks in state spending expected, the flow of public money into the industry looks set to dry up.

Prospects for publicly funded contracts are "very likely to reduce significantly and the question will be whether alternative private sector-funded projects will come forward to cushion the anticipated fall," explains Jim Rowland, head of building consultancy at property adviser King Sturge.

He warns that many small and medium sized building firms will be forced to cut staff numbers during 2010 as order books get slimmer and projects come to an end.

Nick Hood, executive chairman at Begbies Traynor, the restructuring specialist, warns: "It will be somewhere in the range between terrible and cataclysmic, in terms of the industry and the insolvencies it will create, and only broadly spread, well run companies will be able to weather it."

Even optimistic forecasts predict falls of about 30 per cent in terms of state investment in new infrastructure, although spending on roads and railways is expected to be less affected.

Big ticket contracts, such as Crossrail – the multi-billion pound project to build an east-west rail route under central London – offer some bright spots to construction companies. There are fears, however, that work on these lucrative projects is likely to be won by only the largest contractors and that small and medium sized companies will find themselves squeezed out of the market.

In an effort to mitigate the effect of the slowdown in government investment in the industry, some large contractors are focusing on support services contracts – industrial cleaning, maintenance and facilities management for example – in an effort to reduce their exposure to building work.

> 'It will be somewhere in the range between terrible and cataclysmic'
>
> **Nick Hood, Begbies Traynor**

As well as offering better profit margins thanconstruction contracts – which typically offer margins of 2 to 3 per cent – support services work provides good visibility over forward income with contracts often running for more than a decade.

In addition, maintenance and facilities management of the existing stock of state funded infrastructure will continue, regardless of cuts in capital expenditure.

Cancelling a new prison may be unpopular with voters, but it will be less politically damaging than halting the maintenance of schools and hospitals.

As well as looking at alternative revenue streams, construction bosses are sure that the sector, while likely to suffer, will not be affected more than other parts of the economy.

Ian Tyler, chief executive of Balfour Beatty, the UK's largest construction company, recently said that although government spending cuts were inevitable, "there is a real will to not disproportionately hit the construction sector".

While the worst of the cuts are unlikely to be felt until after the election, industry figures have warned that the prospects of significantly lower work levels are leaving construction companies under a cloud of uncertainty.

"What is needed is a clear steer that the inevitable public sector expenditure cuts will not unduly disadvantage [construction companies] and that the effects of a potential rise in private sector demand will not be wiped out by the need to reduce public sector debt," says Jack Kelly, an infrastructure partner at Deloitte.

However, with the government debt burden continuing to rise and scant signs of a rebound in either residential or commercial property, slim order books and fewer employees look set to be industry themes for sometime to come.

Corridor of uncertainty: construction companies such as Balfour Beatty will be affected by the expected cuts in public spending after the election PA

Investors remain wary despite reversal of decision

Coeur Défense

Removal of insolvency protection was unexpected, writes **Anousha Sakoui**

At the centre of the financial district of Paris is a white-clad cluster of office buildings – three low-rise and two high-rise – connected by a central atrium.

But Coeur Défense is more than a physical landmark. The acquisition of a majority stake for €2.11bn in 2007 by Lehman Brothers was also a financial landmark, one of the biggest direct property investments ever seen in France.

The building is now at the centre of a conflict between the owners and the debtholders who financed its purchase through a commercial mortgage backed securitisation deal (CMBS) worth €1.5bn.

The outcome may have far reaching effects on investor confidence in real estate investment in France.

In November 2008 after the collapse of Lehman, HOLD, the special purpose vehicle that owns the building, filed for protection under the *procédure de sauvegarde*.

This insolvency procedure – the French equivalent of US Chapter 11 – gives the company court protection from creditors while it formulates a plan to restructure debts, with the aim of preserving jobs and discouraging liquidation.

The move was unexpected, as SPVs designed to issue CMBSs in property financings usually have few, if any, employees. Because they only hold property, it was always assumed that bankruptcy was not an option.

"Safeguard proceedings were not generally understood to be intended to be available for special purpose entities," wrote analysts at Standard & Poor's in a report last year, adding that the unexpected court decision to allow the building to file for insolvency protection had potentially far reaching implications.

Debt specialists feared this shock decision would dissuade investors from considering debts secured against French assets.

However, on February 25 the courts decided that the safeguard filing was not appropriate and terminated it, to the surprise of many of those involved.

"The decision looks like a very pragmatic one," says Conor Downey, partner at Paul, Hastings, Janofsky & Walker. "International investors will take some comfort from it but the original decision to grant the safeguard will continue to cause concern until it becomes completely clear that it cannot happen again in similar transactions."

Mr Downey adds: "We had been speaking to lenders prior to this decision and they were telling us that the original decision to grant the safeguard had led them to re-evaluate their willingness to do business in France. There would have been a serious concern that this case could have had a long-term impact."

> The original decision to grant the safeguard had led lenders to re-evaluate their willingness to do business in France

The case highlights the difficulties investors in CMBSs face. Many complex financings need to be restructured because the value of the assets backing the debt have collapsed during the downturn.

The initial ruling may have been reversed but some believe it will still have a lasting impact: "Regardless of the most recent ruling, the past 15 months may still leave a sour taste with bondholders," says Euan Gatfield, analyst at Fitch Ratings.

"Looking forward, this may continue to deter some investors from resuming activity in French CMBSs."

In September 2009, the court approved a restructuring plan that would have allowed the borrower to impose a extension of its debts to 2014, from 2012.

Initially, the French courts ordered rental income to be escrowed in an account controlled by a court appointee. This would have stripped lenders of their original right to take control of rental income in the event of the borrower's default – know as "Dailly" assignment of rents.

However the courts have now upheld creditors' right to the rental income.

"The court has decided that the Safeguard was not justified . . . and declared the judgments opening these proceedings null and void," says Olivier Puech, lawyer at Gide Loyrette Nouel, adviser to EuroTitrisation, the managing company of FCT Windermere, the securitisation vehicle.

"The main decision was that the safeguard was not right. This is very good result for creditors."

Jacques Henrot of law firm De Pardieu, Brocas & Maffei, says: "Seeing the opening judgment, or the one approving the plan, revisited . . . and the decision on the assignment upheld, will be very important for the finance and business community.

"Predictability on who is eligible to a *sauvegarde* will certainly make investors more comfortable buying French debt."

Life reflects architecture for Swiss furniture maker

Edwin Heathcote

Imagine you could extrude a house shape, just stick it into a sausage machine and squeeze it through. Then break it up into sections and scatter them on top of each other.

Paint them black and stuff them full of furniture and you have Vitra's new showroom.

Vitra has built itself an extraordinary position, not just through its business but through its buildings.

Founded in 1950, the Swiss design company chose to manufacture in what it expected to be its largest market – Germany.

Weil am Rhein, just over the border from Basel, now hosts one of the most extraordinary collections of contemporary architecture in Europe.

As with their furniture, which has been designed by some of the biggest names in modern design – from Charles and Ray Eames to Jasper Morrison – the Fehlbaum family firm commissioned the buildings on its sprawling manufacturing site from a series of architects on the cusp of greatness.

Zaha Hadid's first building is here. The jagged construction was to be the town's fire station, although it proved hopelessly impractical and is now a chair museum.

Frank Gehry's first building in Europe is here too, the odd-looking collapsing architecture of the Vitra Design Museum (1989) predated the billowing titanium of the Bilbao Guggenheim by nearly a decade.

The main factory building was designed by Nicholas Grimshaw, whose metallic high-tech style perfectly suited the aestheticised industrialism Vitra was seeking.

There is another factory building by Portugal's Alvaro Siza, arguably the greatest and possibly the subtlest architect working today.

The conference centre is the European debut of Japanese architect Tadao Ando, while the petrol station came from the French pioneer of the engineering aesthetic, Jean Prouvé.

> The building acknowledges the increasingly intimate connection between soft art and hard sell

Under construction is a building by Japanese practice Sanaa, famed for its diaphanous, ethereal architecture. Even the bus shelter is by British industrial designer Jasper Morrison.

And now, most visibly, there is that blackened pile of extruded houses, the Vitrahaus, by local architects Herzog & de Meuron. Known for their radical and never less than striking designs, from the Beijing Olympic Stadium to London's Tate Modern, they are at the top of their game. But what they are designing here is effectively a furniture showroom on an industrial estate.

Vitra has achieved something extraordinary by linking its products and its buildings. This is not unknown, of course, particularly in this region. Nearby, on the banks of the Rhine Novartis the pharmaceutical group has built a sophisticated campus (including buildings by Gehry and Sanaa), although it is something few outsiders get to see. Its competitor, Roche, has also employed Herzog & de Meuron asan architect for many years.

Vitra's approach is certainly eye-catching and has proved a boost to the company's profile, making it the object of architectural pilgrimages.

Most corporate architecture is dull. Real estate is seen as a necessity. But in recent years, there has been acknowledgement that good design can help create a happier and more productive workplace.

But the dedication to architectural quality and experimentation seen at Weil-am-Rhein is unparallelled.

There were corporate towns in the past – most notably around the turn of the 19th and 20th centuries but what the furniture maker has done so effectively is to imbue the architecture with the spirit of its products. Design is the raison d'etre of the business, and design has been allowed to dictate the environment.

This is most clearly visible in Herzog & de Meuron's newest work, which acts as a visitor centre, museum, venue and showroom.

In a fascinating comment on how culture is blending into commerce, the architects have blurred the boundary between soft art and hard sell. The building is a tacit acknowledgement of the increasingly intimate connection between the two.

But it is also a spectacular piece of architecture.

The blackened, extruded boxes penetrate and smash through each other creating a series of intriguing collisions and junctions where the visitor can peer down into spaces below or courtyards outside, spaces that flare out into massive volumes suitable for big public events as well as intimate, domestically scaled corners that show off the colourful, often garish furniture to perfection.

Vitrahaus: an extraordinary building housing striking design

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20 – 21 March 2010

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Property

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Stadiums

Commercial tie-ups have been a boon for developments in the UK, writes **Roger Blitz**

When UK football clubs such as Plymouth Argyle, Milton Keynes Dons and Bristol City aspire to be World Cup venues, something is shifting in the business of sports venue development.

The stadiums of these three small provincial clubs are among those England's Football Association propose for venues for the 2018 Word Cup, if Fifa, the sport's governing body, select England as the host at the end of this year.

The three are at different stages of redevelopment projects and all are increasing capacity.

The catalyst of hosting a big tournament has led to stadium development in a number of European countries. Notable among these was Germany, which hosted the World Cup in 2006. The growth in attendances since at the country's top-tier Bundesliga matches has more than justified that investment.

Others that have trodden this path are the Netherlands, Belgium, Portugal, Austria and Switzerland, which have all been host nations of the European Championships in the past decade.

Poland and Ukraine are the latest to become fixated with development, having been awarded the Championships for 2012, while France, Italy and Turkey are drawing up plans in the event of winning hosting rights in 2016.

According to Hightex, which makes membrane structures for stadium roofs, there is a market for 100 new stadiums across the globe over the next three years. Brazil is in part driving that market, as host of the 2014 World Cup and the Olympics in 2016.

But in England, development seems to be driven not just by tournaments but the commercial aims of clubs. Nottingham Forest, Brighton & Hove Albion, Grimsby Town, Worcester City, Truro City, Chesterfield and Brentford have all considered expanding capacity.

The formula has been most prominently followed by Arsenal, which built a stadium near its old Highbury ground and now invariably fills its 60,000-seater Emirates stadium, completed in 2006.

It was built through a highly leveraged deal involving a big bank loan, followed by a bond issue, while the club also redeveloped its old stadium to help pay for its new home.

Premier League rivals are following suit, though not necessarily with the same financing model. But their projects are not without hiccups.

The plans of Tottenham Hotspur, Arsenal's arch rivals, have been questioned by heritage watchdogs; Everton's project, which is tied to a Tesco development, was rejected by the government; Liverpool has planning permission for a stadium but not the funds to start work.

Clubs and retailers have been working hand-in-hand, as retail sites are harder to come by, and clubs find lenders treating their ability to pay off their loans with scepticism.

According to Deloitte, more than half the new stadiums in the UK since 2003 have been helped along with linked retail developments. This trend will help stimulate development through the recession, says Mark Roberts of Deloitte's sports business group.

"The construction market is more competitive at the moment, which could lead to lower build costs,"he says. "We would expect the contribution of the public sector and retail developers and operators, which has been significant in recent years, to continue."

Matthew Walton, planning director at BNP Paribas Real Estate, says the experience of Everton is salutory.

"Everton's plans at Kirkby were thwarted by the refusal of an associated planning application for a Tesco foodstore," he says.

"A 'town centre first' policy for retailing makes it more difficult for similar schemes to come forward."

For some clubs, the redevelopment of existing facilities offers a better and safer bet. But such an option will not be available to all, Mr Roberts says.

"There will still be clubs that need to relocate to make a step change in fortunes. They will continue to face the same intertwining factors as pre-recession, such as finding a site, securing planning permission, managing construction costs and securing funding."

'The construction market is more competitive [now], which could lead to lower build costs'

Mark Roberts, Deloitte

Other factors complicate the picture. Tournament organisers such as Fifa and Uefa, require all spectators to be under cover. Developers also want stadiums to have greater security measures than they have had, and environmental features, such as solar panels.

Mr Roberts offers three rules of thumb for clubs going down the development route.

"First, engage a strong team of advisers. Money spent up front can save millions downstream," he says.

"Second, don't overstretch in terms of 'building for the future or just in case' – it is better to have slight excess demand than supply.

"Finally, it is important to strike the right balance between capitalising revenue streams to allow construction to take place and ongoing revenue streams to ensure operational performance is maximised once the venue is open."

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