Investment Market Update
Baltic States Q1 2014
High investment activities - different investment paths

22 April 2014

Contents

Author

Aivar Tomson
Baltic Head of Research
+ 372 6 264 250
aivar.tomson@dtz.ee

Jurga Kusptyte
Project manager
+ 371 6 724 4811
jurga.kupstyte@dtz.lv

Kristina Kondratovica
Valuation expert
+ 371 6 724 4811
kristina.kondratovica@dtz.lv

Contacts

Magali Marton
Head of CEMEA Research
+ 33 (0)1 49 64 49 54
magali.marton@dtz.com

Hans Vrensen
Global Head of Research
+ 44 (0)20 3296 2159
hans.vrensen@dtz.com

- The overall market turnover in 2013 in the Baltic region was around € 600 M, equally distributed between the three countries. The directions that the capital flows undertake in the three countries however are very different:
  - In Estonia, the biggest share of market turnover is generated by a number of local institutional players, who are actively expanding and diversifying – location-wise, segment-wise, and risk-wise, - their portfolios. The average lot size per asset is around € 5 M; the market however is dominated by portfolio deals that simultaneously involve a number of assets;
  - In Latvia, the biggest share of market turnover is generated by the institutional entrants from the two neighbouring countries, and by private capital inflows from Russia and other CIS countries. The average lot size per asset is around € 5 M; portfolio deals are less common;
  - In Lithuania, almost one third of the annual market turnover was generated by a single asset deal with the buyer coming from Finland. The lion share of the remaining turnover involves participation of the local asset management company *Lords LB*.

- Pan-region wise, the most active purchasers were Estonian *EfTEN Capital* and *Capital Mill,* and Lithuanian *Lords LB.* The most active vendor was *Northern Horizon Capital* (former *Baltic Property Trust*), undergoing divestment process for a number of funds under its management, and *Ektornet*, real estate affiliate of *Swedbank.*

- Asset-wise, the interest was mostly geared towards the office segment in all three Baltic States. At the same time, each of the countries accommodated a number of deals with small to medium sized retail assets, and a few deals with medium to large sized industrial assets.

- The estimated investment volumes in 2014 are similar to those generated in 2013. The interest is expected to be mostly geared towards office and industrial segments.

Baltic States Q1 2014

Estonia

General overview

In Estonia, the investor's interest is mainly addressed towards the properties located in capital city Tallinn, but in smaller amount also towards other larger Estonian cities like Tartu, Pärnu, Jõhvi and Narva. The rest of Estonia even in larger settlements is from an investment point of view less valued.

Largest portfolios of Estonian real estate belong to *Northern Horizon Capital* (former *Baltic Property Trust*), *East Capital*, *Citycon, Homburg,* and local funds like EEREIF, *EfTEN Capital,* and *Capital Mill*. Funds that operate in Estonia are mostly of Northern European background, but also Russian investors have deployed investment possibilities in the country.

A large part of real estate investment transactions are share deals of operating companies; in such cases, the details on the actual transaction price remain undisclosed.

Transactions

The most active player on Estonian real estate investment market in 2013 was locally owned *EfTEN Real Estate Fund.* Within the year, the company invested around € 50 M into a very diverse – location-wise, segment-wise, and risk-wise, - portfolio of properties, employing various acquisition strategies. The portfolio hence includes sale-lease back transaction of two office buildings of *Eesti Energia* located in Mustamäe district (acquired through public auction, total deal volume € 8,85 M); purchase of retail property *Prisma Peremarket* in secondary city Narva; a joint acquisition together with *Esraven AS* (part of *Silikaat Group*) of *Hotel Palace*, - acquisition of hotel operator is part of the deal, - in central part of Tallinn at Vabaduse väljak (the volume of the deal is undisclosed); and a portfolio of five industrial/logistics properties that were on sale as part of divestment strategy of funds managed by *Baltic Property Trust.* This industrial/logistics portfolio includes *K-Rauta* hardware store in Tallinn, *Hanza Mechanics* industrial building in Tartu, *Logistika Pluss* logistics facility in Tallinn, *Mediq* warehouse property in Saue near Tallinn, and *Stora Enso* industrial building in Saku near Tallinn. The total volume of the deal was € 30.5 M. Within the year, *EfTEN Real Estate Fund* also made one divestment by selling the office property on Lõkke 4, Tallinn for € 3.8 M.

Another large market player (investment volume wise) in 2013 was *Colonna Capital Group,* the interest of which was exclusively geared towards office properties. Its daughter company *Pan-Estonian OÜ* acquired the portfolio of office properties from *Ektornet*, the real estate affiliate of *Swedbank*. The deal covered 16 office buildings across Estonia with the total area of 68 000 sq m. The total volume of the deal remains undisclosed, but the general market price sentiments implies an estimate of no less than € 40 M. The company also acquired the office building on Pärnu Road 67a, Tallinn for € 8.1 M.

Notwithstanding, *Baltic Property Trust,* which is in the divestment process for a number of managed funds, was one of the most active vendors on the market. Besides logistics portfolio sold to *EfTEN Real Estate Fund,* the company also sold two supermarkets in Tartu and Valga to the main tenant *Selver*, one of the largest food retailers in Estonia, and a portfolio that includes two properties in Tallinn (9 200 sq m Ravala Street 5 office centre and 6 500 sq m *Logistika* centre), as well as one logistics property in Vilnius and one office building in Riga, to Estonian *Capital Mill* (the volume of the deal remains undisclosed). In 2013, *Capital Mill* also acquired cold storage warehouse with the area ca 2 500 sq m in Rae Parish, Lehmja for € 2.1 M.

On a buying side, *Baltic Property Trust* in 2013 acquired the multifunctional building *Coca-Cola Plaza* in Tallinn for € 11,9 M, with the seller being signed as a long-term operator of the building.

Other large transactions in 2013 include *Mornington Endla* acquiring the office building located in the central city part on Endla Street for € 5,0 M; *Kawe Group* acquiring the property in the centre of Tallinn on 1 Tatari Street for € 3 M for future demolition and development of a modern energy-efficient office building; and *Coca Cola* selling ca 12 000 sq m industrial property in Tallinn to *Lotus Capital* for € 3.64 M.

Baltic States Q1 2014

Yields

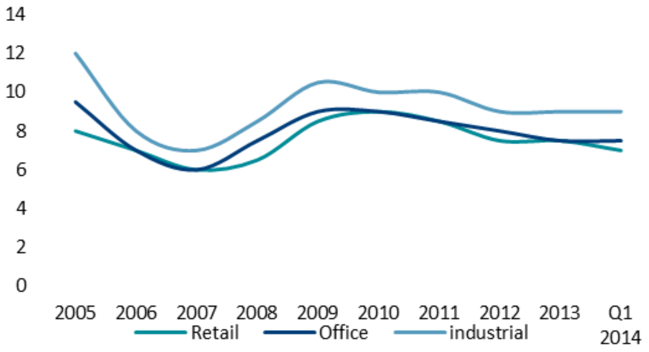
Compared to Northern and Western European countries, market yields in Estonia have been relatively high. During the years 2006-2007, the yields and interest rates fell dramatically, almost to the level of Northern and Western European countries. During the years 2008 -2009, yields rose again - during 2008, the increase was 150-250 basis points and during 2009, 50-100 additional basis points. In 2010, the yields remained quite stable. The year 2011 brought first signs of decrease in retail and office sector by 50-100 basis points and the beginning of 2012 also in industrial sector by 100 basis points. Starting from second half of 2012, the yields remained relatively stable. There has been slight decrease particularly in the segments of office and retail.

The 'low-end' of yields in industrial and logistics investment segment starts from 9.0% on the condition that an investment has good quality, a long term rental agreement (usually sale & lease-back deals), a trustworthy lessee, and a guarantee from a bank or from a mother company. The lowest yield for retail is 7.4%; for office properties - 7.6%.

Yields in Pärnu and Tartu are 1-3% higher, depending on the quality and future prospects of the property. The yields are significantly higher in other parts of Estonia and not comparable even in more populated settlements.

Figure 1

Yield dynamics in Estonia, %



Source: DTZ Research

Baltic States Q1 2014

Latvia

General overview

In 2013, the total real estate investment market turnover in Latvia was around € 170 M, which is more than double the annual turnover figure in 2012. Around 90% of the total investment volume was directed towards Riga and its immediate district. The scope of acquired properties meanwhile was very diverse, ranging from empty land plots for development, reconstruction and refurbishment investments, to A-grade office buildings.

In terms of purchaser profile, the trend was twofold. On one hand, institutional investors from Lithuania and Estonia set themselves firmly on course towards neighbouring market, with three major players, Lithuanian *Lords LB,* Estonian *EfTEN Capital* and Estonian *Capital Mill*, tapping into Latvia in 2013. On the other hand, Latvia with its policy of conferring residency status through investment in real estate attracts a lot of interest from private individuals from Russia and CIS countries, who subsequently account for the biggest share of foreign private capital contribution to the market. Domestic purchasers meanwhile are moderately active in small-scale investment segment, and usually acquire the properties that cannot be treated as real estate investment objects, but rather as owner-occupied small enterprises.

On vendors' side, similarly as in 2012, the biggest market share still belonged to the real estate companies affiliated with the banks. Another major vendor ever since the end of 2012 is former *Baltic Property Trust* (current *Northern Horizon Capital*), which throughout the whole 2013 was in the divestment process for a number of funds under management. At the same time, *BPT Baltic Opportunity Fund* is actively investing in the region, mostly through the sale-lease back transactions.

In Latvia, asset transfer deals and share transfer deals are both commonly used in practice, whereas institutional investment within the country is limited to close-ended real estate funds managed by asset management companies.

Transactions

While in the few previous years, the capital was mostly channelled into residential and hotel segments, 2013 offered a more diverse landscape of investment segments. In terms of number of transactions, the interest was primarily geared towards office (16 properties sold) and retail (eight properties sold) segments; industrial segment witnessed at least five investment transactions within the year. At the same time, the investment interest was also channelled into such segments as healthcare and entertainment.

In 2013, the market witnessed one major portfolio exit-entry transaction, in which Icelandic *SMI Group* sold all of its assets to Lithuanian *Lords LB* through a share transfer deal. The deal overall covered properties in both Lithuania and Latvia, with the portfolio in Latvia including five assets: two retail boxes in Riga (6 400 sq m anchored by DIY store *Depo* and 8 000 sq m anchored by *Rimi* and *JYSK*), 7 400 sq m shopping centre in Liepaja, 14 000 sq m shopping centre in Jelgava, and 52 000 sq m *Bergi Logistics Centre* in immediate Riga district, 97% of which is occupied by *JYSK.*

Besides the above mentioned portfolio deal, in 2013, the market witnessed four investment transactions that exceeded € 10 M. These include: disposal of residential complex *Panorama Plaza* (the property includes one residential tower with 120 apartments, one residential tower which is still under construction, and a land plot with technical project for the development of additional residential tower) by *Ektornet Latvia* to the investor of Russian origin in Q2 2013, and the subsequent disposal by the same seller to the same buyer an adjoining *Panorama Plaza* office building of 19 000 sq m in Q3 2013; *Dominante Logistics* (39 000 sq m) sale by *Swedbank* to the investor of Russian origin; and the disposal of A-class *Valdemara* office centre by *Baltic Property Trust* to Estonian *Capital Mill.*

The segment for € 5-10 M witnessed six transactions and was mostly dominated by investments into office (three transactions) and leisure (two transactions) segments. At the same time, all of the properties in this segment are historical buildings in the Old Town and central part of Riga city. To mention just a few: sale of fully renovated B-grade office building on Alunana Street 2 for € 9.5 M; acquisition of the former headquarters of *Rietumu banka* on Brivibas Street by *Latvijas Pasta Banka* for € 7 M; acquisition of entertainment centre (casino, restaurant, night club) on Terbatas Street 2 by *Citycon Group* for € 9.6 M; sale of leisure and entertainment complex on Kalku Street 12 by *NIF* (the company affiliated with *Citadele bank*). The rest of the investment market activity encompassed over 20 transactions between € 1-5 M.

Estonian *EfTEN Capital* tapped into Latvian market by acquiring land plot for retail development in Jelgava (pre-lease agreement with anchor tenant Rimi), followed by an acquisition of an office building in central part of Riga city (Stabu Street 10, requires additional investments into renovation) from Ektornet Latvia.

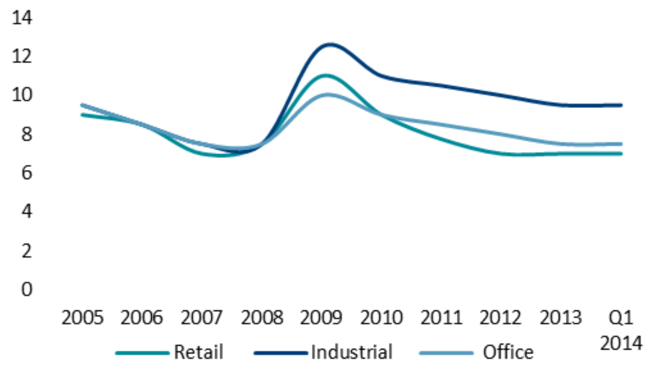
Baltic States Q1 2014

Yields

Market evidence suggests the following lower boundaries: 9.0-10.0% for industrial properties, 7.25-8.0% for office properties, and around 7.0% for other than prime retail properties. Low to moderate positive pressure is evident in industrial and office segments, for good quality, well located properties.

Figure 2

Yield dynamics in Latvia, %



Source: DTZ Research

Baltic States Q1 2014

Lithuania

General overview

Commercial real estate investment market in Lithuania originated in 2003, when *Baltic Property Trust* from Denmark made their first acquisition in the country. Subsequent accession to EU in 2004 intensified international interest in the market that previously was predominantly controlled by local owners and developers.

The upcoming four years were the 'golden times', with many international players following the footsteps of BPT; in year 2006, nineteen investors submitted their bids for one property located in the secondary city of Lithuania.

The things went standstill in 2009-2011; however, the market fundamentals proved to be quite resistant, with only one commercial property being overtaken by a bank as a non-paying liability and one property being sold through a forced sale tender.

Within the last two years, the market gradually returns to the 'healthy' status. The oversupply of commercial premises has been successfully absorbed, whereas rents stay within the reasonable brackets. In 2012, new developments in the office segment commenced; in 2013, retail projects that were put on hold five years ago have been re-introduced into the active pipeline.

The interest in real estate investment opportunities is mainly addressed towards capital city Vilnius. Smaller scale investment activities appeared in such cities as Kaunas, Klaipėda and Druskininkai. The largest real estate portfolios in Lithuania are held by international players, such as *Northern Horizon Capital* (former *Baltic Property Trust*), *East Capital*, *Citycon*, *EEREIF*, *Homburg*, *Deka Immobilien*, and local fund management company *Lords LB*.

Transactions

In 2013, Lithuania accommodated the biggest, - in terms of transaction volume, - single deal in the Baltic region. The asset of the transaction was office complex in Vilnius, consisting of two fully leased buildings with a rentable area of 31 200 sq m, and a third building of 11 000 sq m to be completed in early 2014, already 76% pre-let. The seller of the asset was local *Icor*; transaction volume is close to € 63 M, which gives 8.2% net market yield on the investment, and 7.6% net initial cash flow based yield. As a result of the transaction, the buyer, Finnish *Technopolis,* upgraded its EBITDA growth guidance from 9-12% to 14-17%.

Similarly as in the other two Baltic countries, *Baltic Property Trust* was active on both vendor and purchaser side also in Lithuania. As a result of its divestment process, the company sold *BPT Business Centre* in Vilnius CBD to a private investor of Russian origin for approximately € 5 M, and a 22 000 sq m *Zariju Logistics Centre* in Vilnius as part of a pan-Baltic four assets portfolio deal to Estonian *Capital Mill.*

On a buying side, *BPT Baltic Opportunity Fund* acquired soon to be delivered 11 000 sq m *Domus Pro* shopping centre in Vilnius from the developer Danish *TK Development.* The property was 80% pre-leased at the time of the purchase with *Rimi* anchoring the tenant list; net initial investment yield is announced to stand at 8.5%.

In 2013, the market also witnessed one major portfolio exit-entry transaction, in which Icelandic *SMI Group* sold all of its assets to Lithuanian *Lords LB* through a share transfer deal. The deal overall covered properties in both Lithuania and Latvia, with the portfolio in Lithuania including five retail assets: 12 000 sq m shopping centre *Arena* in Siauliai; 17 500 sq m shopping centre *Arena* in Klaipeda; 7 400 sq m shopping centre in Alytus; 7 400 sq m shopping centre in Marijampole; and a land plot for a 14 000 sq m mixed-use development in Kaunas. All existing retail properties subject to this deal are anchored by *Rimi* and *JYSK.*

Another acquisition made by *Lords LB* in 2013 was the purchase of holiday home *Viesnage* in Palanga through the auction organized by the State Property Fund. The company was also active as a vendor on the market, and disposed 8 500 sq m A-class office building on Saltoniskiu Street that hosts *Danske Bank* headquarters for approximately € 15 M.

The overall investment volume on Lithuanian real estate market amounted to approximately € 200 M in 2013.

Baltic States Q1 2014

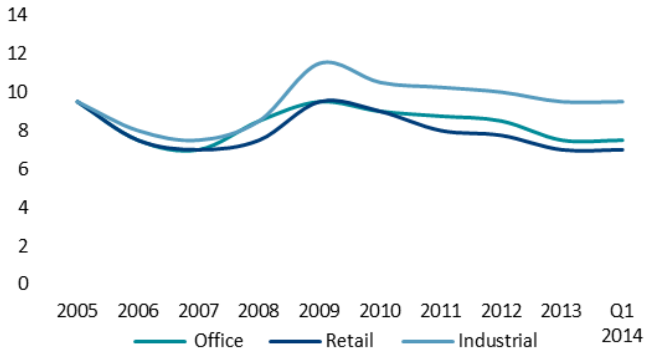
Yields

Market evidence suggest that the ‚low-end' for yields in industrial and logistic segment stands at around 9.5%, on the condition that an investment has good quality, long-term rental agreement (usually sale & lease - back deals), a trustworthy lessee, and a guarantee from a bank or from a mother company. Yields for well-established retail properties start at around 7.0%; yields for office properties start at around 7.5%.

Prime yields were generally stable in 2013, and are not expected to change substantially in the upcoming year.

Figure 3

Yield dynamics in Lithuania, %



Source: DTZ Research

Baltic States Q1 2014

Other DTZ Research Reports

Other research reports can be downloaded from www.dtz.com/research. These include:

Occupier Perspective

Updates on occupational markets from an occupier perspective, with commentary, analysis, charts and data.
Global Occupancy Costs Offices
Global Occupancy Costs Logistics
Obligations of Occupation Americas
Obligations of Occupation Asia Pacific
Obligations of Occupation EMEA
Global Office Review
India Office Demand and Trends Survey 2013-14
Sweden Computer Games Developers November 2013

Property Times

Regular updates on occupational markets from a landlord perspective, with commentary, charts, data and forecasts. Coverage includes Asia Pacific, Bangkok, Beijing, Berlin, Brisbane, Bristol, Brussels, Budapest, Central London, Chengdu, Chongqing, Dalian, Edinburgh, Europe, Frankfurt, Glasgow, Guangzhou, Hangzhou, Ho Chi Minh City, Hong Kong, India, Jakarta, Japan, Kuala Lumpur, Luxembourg, Madrid, Manchester, Melbourne, Milan, Nanjing, Newcastle, Paris, Poland, Prague, Qingdao, Rome, Seoul, Shanghai, Shenyang, Shenzhen, Singapore, Stockholm, Sydney, Taipei, Tianjin, Ukraine, Warsaw, Wuhan, Xian.

Investment Market Update

Regular updates on investment market activity, with commentary, significant deals, charts, data and forecasts. Coverage includes Asia Pacific, Australia, Belgium, Czech Republic, Europe, France, Germany, Italy, Japan, Mainland China, South East Asia, Spain, Sweden, UK.

Money into Property

For more than 35 years, this has been **DTZ's flagship research report, analysing invested stock and capital flows into real estate markets across the world.** It measures the development and structure of the global investment market. **Available for** Global, Asia Pacific, Europe, North America and UK.

Foresight

Quarterly commentary, analysis and insight into our in-house data forecasts, including the DTZ Fair Value Index™. **Available for** Global, Asia Pacific, Europe, UK and China. In addition we publish an annual outlook report.

Insight

Thematic, ad hoc, topical and thought leading reports on areas and issues of specific interest and relevance to real estate markets.
Deflation and Commercial Property March 2014
Tokyo Retail Market 2014
Great Wall of Money – March 2014
German Open Ended Funds – March 2014
China Investment Market Sentiment Survey January 2014
China The Technology Sector January 2014
Czech Republic Green buildings December 2013
Net Debt Funding Gap - November 2013
UK secondary market pricing - October 2013
Quantitative Easing - UK Regions - September 2013
Singapore Government Land Sales - September 2013
Property Investment Guide Asia Pacific 2013-2014

DTZ Research Data Services

For more detailed data and information, the following are available for subscription. Please contact graham.bruty@dtz.com for more information.

- **Property Market Indicators**
  Time series of commercial and industrial market data in Asia Pacific and Europe.
- **Real Estate Forecasts, including the DTZ Fair Value Index™**
  Five-year rolling forecasts of commercial and industrial markets in Asia Pacific, Europe and the USA.
- **Investment Transaction Database**
  Aggregated overview of investment activity in Asia Pacific and Europe.
- **Money into Property**
  DTZ's flagship research product for over 35 years providing capital markets data covering capital flows, size, structure, ownership, developments and trends, and findings of annual investor and lender intention surveys.

DTZ Research

DTZ Research Contacts

Global Head of Research

Hans Vrensen

Phone: +44 (0)20 3296 2159

Email: hans.vrensen@dtz.com

Global Head of Forecasting

Fergus Hicks

Phone: +44 (0)20 3296 2307

Email: fergus.hicks@dtz.com

Baltic Head of Research

Aivar Tomson

Phone: + 372 6 264 250

Email: aivar.tomson@dtz.ee

Head of CEMEA Research

Magali Marton

Phone: +33 1 49 64 49 54

Email: magali.marton@dtz.com

Head of Strategy Research

Nigel Almond

Phone: +44 (0)20 3296 2328

Email: nigel.almond@dtz.com

DTZ Business Contacts

Chief Executive, EMEA

John Forrester

Phone: +44 (0)20 3296 2002

Email: john.forrester@dtz.com

DTZ Baltic

Tambet Tiits

Managing Director

Phone: +372 626 4250

Email: tambet.tiits@dtz.ee

Estonia

Aivar Roosik

Director, Development

Phone: +372 626 4250

Email: aivar.roosik@dtz.ee

Latvia

Andris Juršāns

Director, Latvian office

Phone: **+371 6 724 4811**

Email: andris.jursans@dtz.lv

Lithuania

Valdemaras Ivaško

Director, Valuation & Consulting

Phone: +370 5 210 0252

Email: valdemaras.ivasko@dtz.lt

DTZ
a UGL company