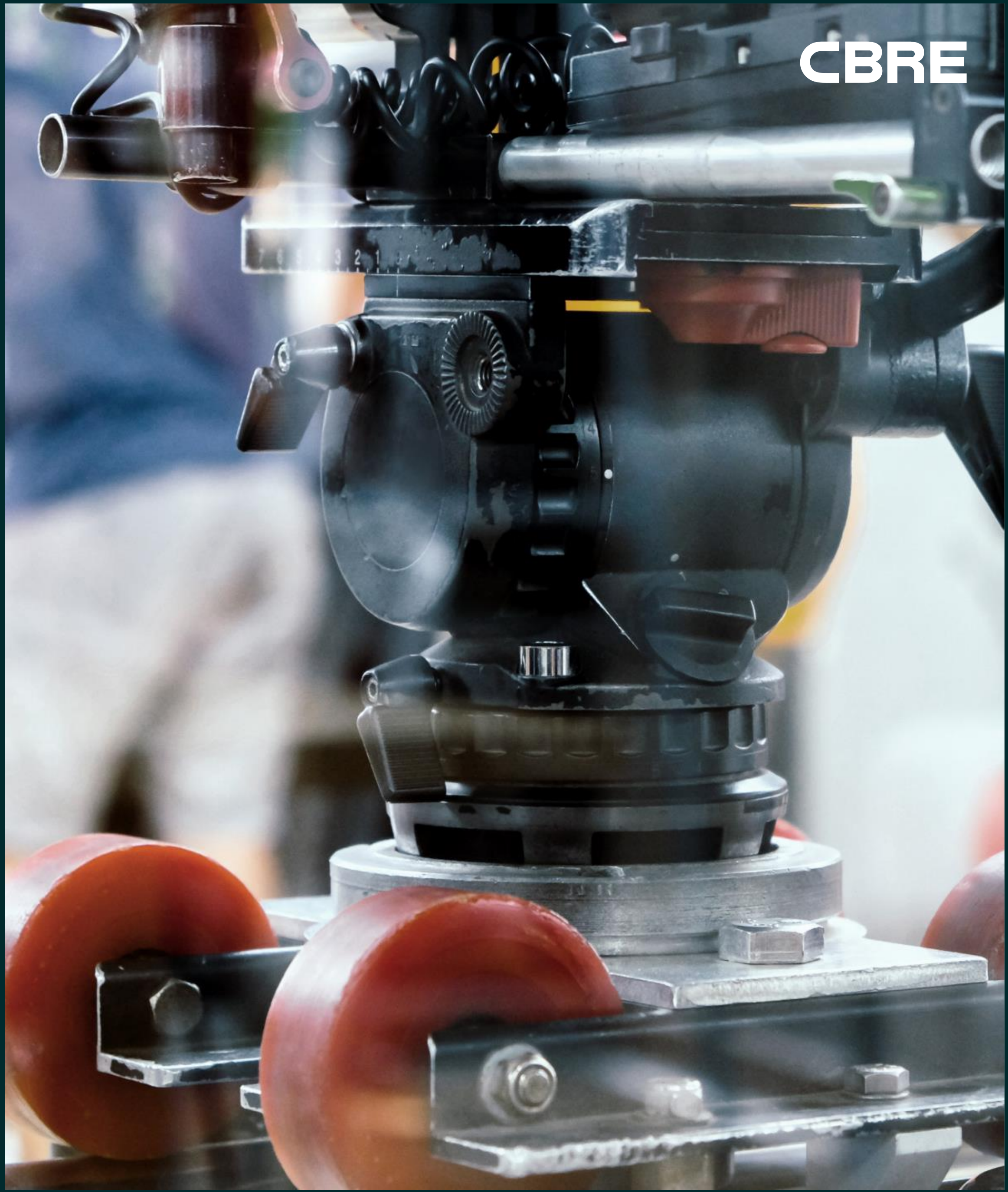
Creating Resilience

Manufacturing trends

CENTRAL AND EASTERN EUROPE

Manufacturing activity in Central Eastern Europe

CBRE RESEARCH
MAY 2023



Economic Growth in 2023

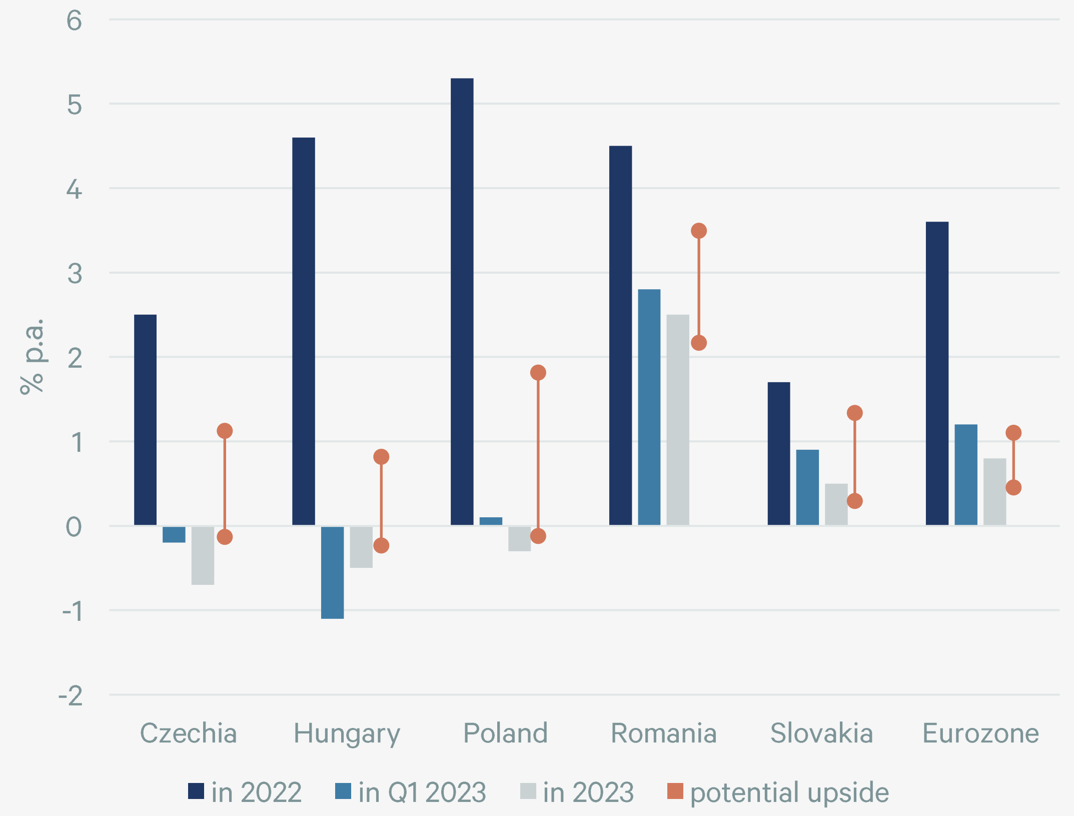
The economy of the CEE region was expected to expand only at a meager pace this year. Inflation is still high and sticky and make savings and purchasing power fall, leading to a contraction in domestic consumption. Tight financing conditions continue to weigh on domestic demand. Lower energy prices can help desinflation and economic growth, while the prolongation of the Ukraine war clouds the outlook.

All with this in mind, first estimate on Q1 GDP surprised on the upside and make forecasteres upgrade their annual forecast to the upside; practically forecasting that the region can post postive growth rate for 2023 as a whole:

- Czech economy is out of the mild technical recession and might post a growth rate up to 1% in 2023 (as an average);
- Hungary is still in technical recession, the decline was smaller than expected, bringing annual forecast to 0.5%;
- Polish economy suprised the most to the upside with a robust (3.9%) q/q growth, pushing estimation for the annual GDP growth towards 2% for 2023;
- Romania continued to outperform the region with no hint of a recession, annual growth might climb to 3.5% for the year;
- Slovakia has avoided recession as well and is likely to outpace Eurozone with a GDP growth above 1% in 2023.

FIGURE 1

GDP Growth Actuals and Forecast Range for 2023



Source: Oxford Economics, CBRE Research

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Economic Growth in Coming Years

Stronger global trade, fewer supply-chain bottlenecks, resilient consumers and more public and private investment will support economic growth in the long run. Next years are already promising regarding economic growth in the region.

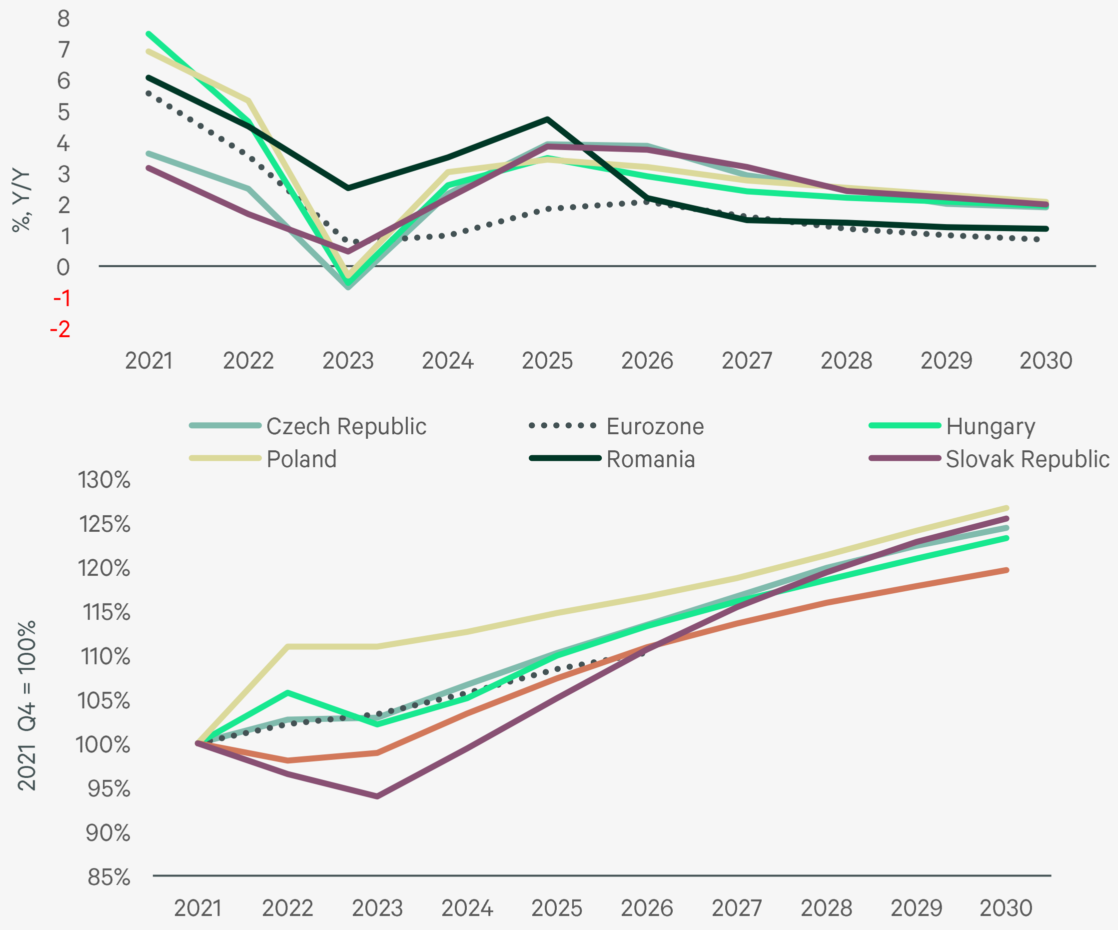
Physical infrastructure in the region has improved significantly over the last decade and is now considered to be at high quality in most of the countries, granting easy access to major manufacturing hotspots in the Blue Banana area in the EU. Supported by the sustained relative advantage of the cost of labour, CEE is a primary target for further FDI targeting the manufacturing & production sector.

While 2023 seems to be a sluggish year for the industrial growth in the region, expansion should pick up from next year and will remain above the Eurozone average, clearly outperforming other regions (like Southwest-Europe).

The region has a quite tense labour market; however, CEE countries have various subsidy policies to attract labour force from 3rd countries - as this is visible in the growing foreign population in these countries. For obvious reasons, Ukrainians accounted for the biggest share in new foreign workforce in the region last year, a trend to be continued this year as well.

FIGURE 2

Annual GDP Growth (above) and Cummulated Industrial Output Growth (below) in CEE



Source: Oxford Economics, CBRE Research

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Wages and Retail Sales Growth

Households in CEE have been exposed to higher inflation than their counterparts in WE therefore real wages and consumption has contracted more here than in core WE markets (except for Romania). With disinflation on the way, domestic consumption is expected to re-bounce again. A stronger economy from H2, an expanding workforce and real growing wages all argue for a boom in retail sales as the economies pick up.

Retail sales growth in CEE is forecast to be stronger in coming years than that in WE. Increasing consumption brings an expansion in e-commerce: both in absolute figures and also in relative terms - as these markets are still below the WE average in online penetration (except for Czechia). This boosts further demand from 3PL companies: they might become more active again in coming years and will account for a growing share in I&L absorption.

FIGURE 3

Hourly Average Wages in Manufacturing Sector in European Countries

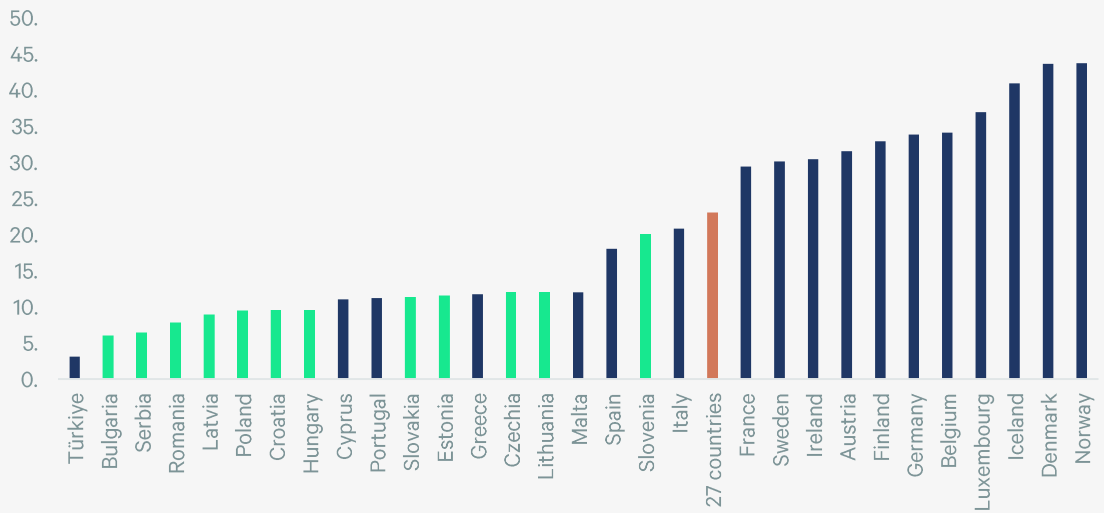
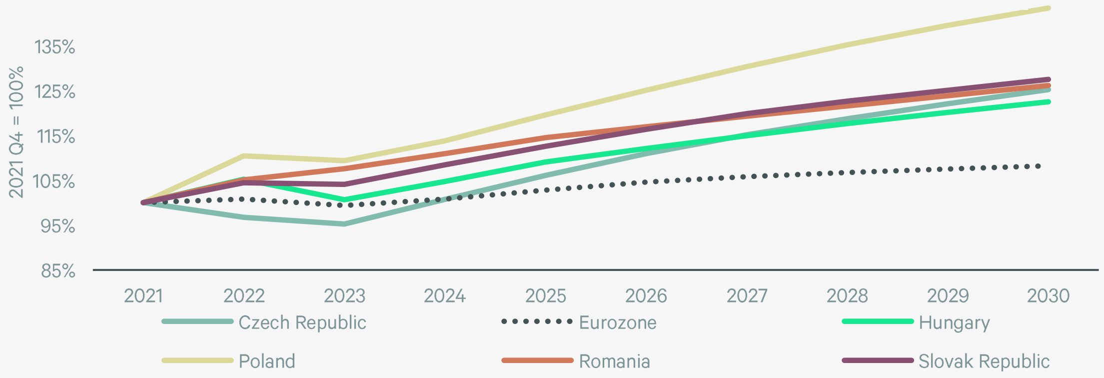


FIGURE 4

Cummulated Retail Sales Growth in CEE



Source: Eurostat, CBRE Research

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I&L Vacancy and Annual Market Growth in Europe

CEE has a relatively strong pipeline to accomodate the growing needs of logistics service providers and to cater for the real estate needs of new manufacturing & production facilities.

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Industrial companies' activity in industrial and logistics sector in real estate

Manufacturing companies are increasingly taking industrial and logistics units in whole Europe, similar trend is being observed in CEE. Taking into account sectoral distribution, in Q1 2023 a significant increase of sq m leased by manufacturing companies was observed – 34% of take-up. Compared to 2022, it is an increase by 11%. The increase was compensated by a decrease of transactions from retail and online retail sector. This trend is going to continue.

It is important to underline that many production companies choose to invest in their own production facilities rather than lease space from logistics developers, so the nearshoring occurence is in fact higher than presented.

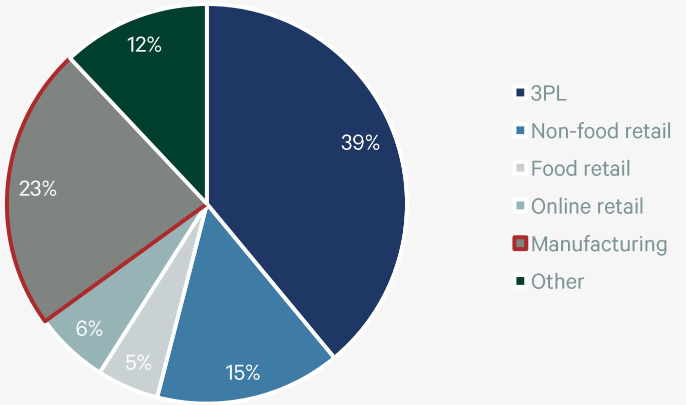
Table 1 Selected manufacturing lease transactions in 2022-Q1 2023 in CEE

Country	Tenant	Sub-sector	Size (sq m)
Croatia	Jabil	Electronics	60,000
Poland	FoodPrint	Packaging	41,200
Serbia	NIDEC Elesys	Automotive	37,500
Czech Republic	BJS Czech	Furnishing	37,400
Czech Republic	Shape Corp	Automotive	36,400
Poland	Steyr	Automotive	35,000
Hungary	Apollo Tyres	Automotive	25,000
Slovakia	LKW Komponenten	Automotive	24,900
Slovenia	Bosch	Home Appliances	24,500
Hungary	Ennoconn Hungary Kft.	Electronics	20,800
Romania	Diehl Controls	Home Appliances	18,200
Romania	Ferro NovaServis	Armature	16,000
Slovakia	MAHLE	Automotive	14,800

Source: CBRE Research

FIGURE 5

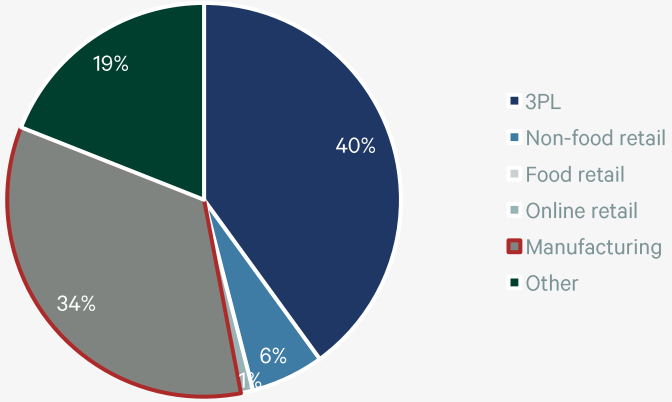
Sectors in I&L take-up in CEE-5 countries in 2022



Source: CBRE Research

FIGURE 6

Sectors in I&L take-up in CEE-5 countries in Q1 2023



Source: CBRE Research

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Czech Republic

The Czech Republic is one of the most sought after country in Europe when it comes to manufacturing, mainly from Automotive sector – one of the main drivers of industrial demand. Due to the volume of automobile manufacturers located in the Czech Republic and surrounding countries, the Czech Republic is a popular choice for automotive suppliers.

The Czech Republic benefits from the central location in the Europe and offers safe investment environment and skilled and well-educated workforce. It is one of the most opened economies of the world with stable social and political system.

Crucial is the link of the strongly export-oriented Czech economy with the German economy. In the past five years, Germany has accounted for almost 30% of the Czech foreign trade turnover.

Hungary

In Q1 2023, the Hungarian industrial property market has lost somewhat from its enormous dynamics of the last two years. Logistic companies are more cautious in their expansion plans, calculating with a general slowdown in their business due to the recession - however, this might be short-lived.

On the other hand, production-linked occupiers are becoming more active. New FDI in Hungary reached all-time high in 2022, mostly driven by massive investments of Asian companies into the EV industry. These investments are likely to trigger further needs for modern warehouse space in certain locations: mostly in regional industrial markets. High new supply volume in Greater Budapest area poses a certain threat of overdevelopment; there isn't any such risk in regional markets given the still limited development volume.

Poland

Poland was named as Europe’s top nearshoring destination because of three key pillars: workforce, geographic position and the infrastructure, especially in tems of rail, roads and one of the largest logistics stock in Europe and the largest one in CEE region.

Automotive sector is the largest export field and given the price competitvenes, proximity to Europe’s largest automotive hub in Germany, the investment into this branch is set to continue. As an example, the largest in Europe LG Chem factory producing lithium-ion batteries for electric cars. This investment resulted in the introduction of the most modern technology to Poland and also attracted another big investment in this field more recently, Mercedez Benz electric battery and engine factory followed by their whole electric delivery trucks factory.

Another branches that are going to develop include: electronics, aerospace and defence, chemicals and pharmaceuticals. Poland is already seen as an attractive destination to locate manufacturing and that perception is strengthening due to re-evaluation of supply chains and looking to move closer to final markets.

Romania

Romania is one of the most attractive countries for the manufacturing industry, with 17% of the total employment overall country represented by this domain of activity with an increasing trend for the following years. The growth will be sustained by the state-aid scheme, which will grant 500 million EUR annually, increasing Romanian competitiveness throughout the region. Additional to the incentive from the State, the accession of Romania to Schengen space is a new factor that will positively impact the evolution of Romania on the map of manufacturing players. Meantime, there is a lot of infrastructure work that will facilitate road transit from all parts of the country and open new areas with high labor density and availability.

A third of the industrial take-up (meaning total leasing activity excluding renewal/renegotiation) in the last ten years was represented by the players from the manufacturing sector. Most of the leases in Romania are developed as built to suit projects characterized by high space customization.

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Slovakia

Slovakia's economy heavily relies on its manufacturing sector, which is fueled by a competent and cost-effective workforce. This has made the country an attractive destination for foreign companies seeking to increase their production's value. With a robust supply chain and excellent transportation infrastructure, Slovakia stands out as one of the top car manufacturers per capita, hosting OEMs such as Volkswagen, Stellantis, KIA, and Jaguar Land Rover. Recently, Volvo announced its plans to produce electric vehicles in Slovakia, adding to the country's growing list of foreign car companies.

Moreover, Slovakia's strategic location in the heart of Europe and the CEE region provides it with excellent connectivity to neighboring countries. Although many manufacturers own their production spaces in Slovakia, there is also a significant presence of strategic manufacturers operating in rented premises.

SEE – Southern Eastern Europe

Traditionally, the manufacturing sector in SEE was owner occupied and with no factories being leased. However, with the entry of international developers, such as CTP and Log Expert, to name a few, leasing market for factories has been created. Additionally, Bulgaria, Croatia and Slovenia followed with several transactions recorded over the previous 24 months. Such trend is expected to continue, and increasing number of transactions is expected, which has been supported by increasing number of international investors and rise of demand.

Large potential within the region lies in the location and excellent traffic connections, as well as the fact that the labour force is skilled and the local municipalities are flexible towards investments.

Baltic countries

The sentiment on manufacturing transactions in the Baltics is cautiously optimistic. The manufacturing industry in the Baltics has been experiencing steady growth in recent years, with an increasing number of companies considering operations in the region. The country's skilled workforce, favorable business environment, and strategic location have all contributed to its growing popularity as a manufacturing hub. The Baltics' expanding network of free economic zones is also a key factor driving growth in the region's manufacturing sector (offering tax incentives, streamlined regulations, and other benefits).

However, the availability of manufacturing lease transactions remains limited, with built-to-own projects being the more prevalent option. As the region's infrastructure continues to develop, with initiatives such as Rail Baltica and expanding intermodal hubs, the potential for international companies to establish a presence in the region is expected to grow further.

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