

We experience a reduction in construction volumes, having reached by now the capital city as well, and the possibility of demand contraction effect of the austerity measures, on the one hand, and a growing interest towards property investments (fuelled by the introduction of the interest tax and an expected price-rising effect of increased investor costs), constant demand, due to a tone-down in seasonality, and enhanced need for quality, instead of mass character projects offered, on the other. These are the factors to shape the often ambivalent judgments of different players on market processes.

CONSTRUCTION VOLUME

By the first-half of 2006, figures for Budapest also began to reflect the country-wide trend of a decline in both the number of construction permits and that of the occupancy permits. According to data of the Central Statistical Office (KSH), in the first half of the year, occupancy permits were granted to 13,000 homes and, nationwide, construction permits were issued for almost 20,000 new homes. This is 14% and, respectively, 20% less than in the first half of 2005. This significant drop occurred primarily in the second quarter of the year.

Except for five counties (Tolna, Baranya, Szabolcs-Szatmár-Bereg, Fejér and Nógrád), the number of the newly occupied homes diminished everywhere. The drop in the number of newly issued permits concerned primarily construction projects in large cities. In the eastern half of the country, appetite for construction dropped in each county, while in Transdanubia, the number of new permits increased (by 10-27%) in the counties of Fejér, Somogy and Győr-Moson-Sopron, with a 2% increase observed in Pest County.

Decrease is even more spectacular in the numbers for Budapest: -21% in terms of occupancy permits and -32% in construction permits. As a result, the share of Budapest went down from last year's 30% to 26-28% in country-wide volumes (with 5200 construction permits and 3600 occupancy permits now). Parallel to volumes, this first-half represents in Budapest a turn in trend in respect of other important indicators as well. A 27% decrease was observed in entrepreneurship-based home construction, with a drop of 30% in housing projects for sale and an increase by one-third in constructions implemented by individuals. Still, in the cities, the direction of changes in home construction was exactly opposite to that. The resultant thereof is that no change occurred in the distribution of the two main groups of the builders: natural persons account for 54%, enterprises for 42%, the remainder being local government and other organisations.

This restructuring in terms of builders had a major effect also on the sizes of the homes built. After many years, the first half of this year was marked by an increase in the average floorspace area of newly built homes, from 62 sqm in 2005, to almost 69 sqm. As opposed to this, in county capitals this indicator dropped from 91 to 83 sqm. For the whole of the country, the average size remained unchanged at 90 sqm.

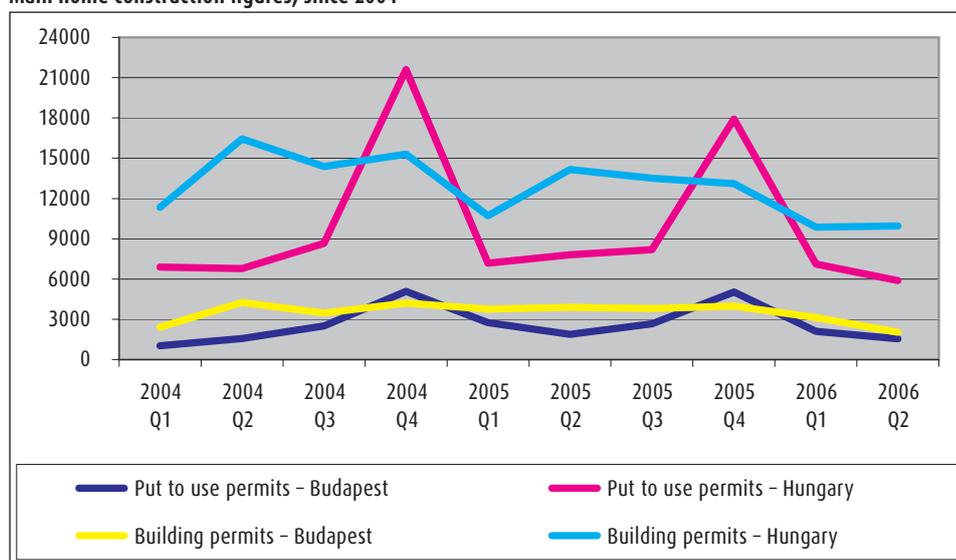
HOUSING POLICY, HOUSING SUBSIDIES, BANK FINANCING

After the parliamentary elections, within the framework of a government restructuring, the National Office for Housing and Construction was eliminated at the end of July. Within the newly established Ministry of Local Government and Regional Development, two specialised departments shall deal with the sector, which is considered by the industry to be clearly a step backwards.

In the last six months, for the first time since years, no government decision was made that could have a significant effect on housing loans and subsidies, i.e. on the housing market. At the same time, in the absence of a seasonal summer drop, a surprisingly flamboyant market shows the effects of the austerity measures announced after the elections and, even more, of the new taxes introduced on bank deposits. The point is that taxation of capital revenues logically implies an increase of the demand on the property market. Property continues to be considered a long-term, stable investment, even though a selection of the right item requires prudence, and maintenance costs shall be also taken into account. As the effect of the austerity measures shall become sensible actually only in early 2007, no drop shall be expected in the turnover this year, as yet.

According data of DEM Information and Economic Research Office, in the first eight months of 2006, demand for housing loans significantly, by about 20 per cent, exceeded the levels of both 2004 and 2005 and amounted to a total of 372 billion HUF. In housing loans, currency-based loans continue to play the main role, with an average size exceeding five million forints now. The volume of forint-based, subsidised loans became stabilised; less than one-third of the persons eligible still make use of this form. But with an increase in the central bank's prime rates, these loans shall also become more expensive. In addition, the planned elimination, in 2007, of interest subsidy and of tax allowances on loan redemption shall concern these customers, even if, due to the small share of subsidised loans, the austerity measures shall have no significant effect on the housing market.

Main home construction figures, since 2004



Source: KSH (Central Statistical Office)

Funding competition goes on, in spite of the squeezing margins for the banks. Increasingly favourable conditions, higher loan-to-value ratios keep demand at high levels for housing products (and so, indirectly, for properties), and that could lead to rising prices on the market.

Within lending, a dynamic increase is observed in the property lease sector. For the first three quarters of 2006, the Hungarian Leasing Association recorded on the market an increase of 150 per cent to the previous year. An extension of this form of funding is confirmed by a significant increase in the share of property leases within total funding. On the market of home leases, competition is tough. The players do not disclose exact data on the stocks, but the potential of the sector is evident from the constant accession of new companies to the players already active on the market. Parallel to competition, tools for attracting customers also expand, to include, in addition to softening lease terms, also the development of schemes to make use of allowances linked to leases, both for the population (tax allowances) and for entrepreneurs (tax reduction options).

Luxury tax, introduced this year, did not comply with the hopes attached to it. A major portion of the properties of 100 million worth is in the capital city, where, from a total of 409 taxpayers, an amount of 100 million forints was collected – far less than the preliminarily calculated amount for the country. Already in the summer, news appeared about the planned introduction of a general property tax and, potentially, of a land value increase tax. Even though later on, plans leaking out concerned a launch of such asset-type tax in 2008, professionals keep developing already now different assumptions and calculations, with a confrontation of pros and cons.

According to Otthon Centrum's database, consisting of ten thousand residential properties (i.e., a database that can be considered representative), if the average price would represent the lower limit for tax liability, taxes would become payable above 22.5 million forints in Budapest, whereas in the countryside, the limit would be at two-thirds of this value. Average prices exceed 20 million in 14 districts of the capital city. The basis for the introduction and operation of a property tax should be a reliable, public, constantly updated database containing a maximum of quality information on the properties – at present, no such database is available. At the same time, from the point of view of methodology, the much-criticised system of luxury tax zones would be most likely the one to be adapted – of course, after a revision of its most criticised categories.

From a logical point of view, the introduction of a property tax would initially imply a drop in the turnover. This, however, could be compensated by expectations of a price increase, in view of a reduction in the offer of new homes and an increase in investors' costs, whilst due to the competition of banks, favourable funding possibilities keep the purchasing power at high levels, on the whole. After that, a dual effect can emerge. On the one hand, prices, augmented with the tax burden, can result in a decrease of demand. On the other hand, however, the turnover might even accelerate, if many properties, unoccupied at present, would come to the market. This is when people intending to sell less liquid, high-value properties (such as larger one-family houses in the outer districts of Pest) could be in trouble, because the increase in offer would reduce the prices. For the time being, the overall effect cannot be calculated, because much depends on the final form of the tax.

On the whole, it would be reasonable to introduce a property tax of the wealth tax type, that is, a tax charged on residential property in private ownership. At the same time, a general tax – charged also on development-purpose land property and commercial properties held for investment purposes – would be detrimental in its effect. If a property intended for production purposes is charged, development becomes more expensive, leading to a decline in the competitiveness of the business sector. The additional burden on the investment-purpose properties would imply an increase in operating costs and, due to lower returns, to a fall in readiness to invest. (To give an example: in the case of a commercial property yielding 6.5%, a 1% property tax would reduce the yield to 5.5%, representing a value impairment of 15%.)

In order to promote the property market's efficient operation, here we give a couple of our suggestions for to-dos – as a simple list for the present purpose, without any prioritisation:

- » land registry data should be made public, as far as possible, in order to ensure a wider range of information for the market players;
- » investors shall be required to provide data on their projects in a mandatory order;
- » duty on the purchases of residential properties should be halved (to 3%) in respect of the amount above 4 million forints;
- » imputation of existing homes ought to be made more attractive for enterprises authorised to property dealings, with the elimination of charges payable above certain volumes;
- » it is necessary to increase the foreseeability of the authority permit procedures;
- » in order to promote the extension of the one-family house investor form, the VAT on public utilities construction, as well as VAT on land purchases from the local government or a developer, should be made refundable;
- » the targets for housing subsidies should be selected carefully, in order to lengthen the home mobility chains;
- » in order to increase legal certainty for the purchasers, a scheme similar to caution

money could be implemented to the benefit of the companies participating in the project (primarily, the investor);

- » a Chamber of Property, planned since years, could be established, to put special emphasis within its framework on the regulation of the sales.

MARKET OF THE NEWLY BUILT HOMES

On the market of newly built homes, a spectacular lessening of the seasonality effect took place. The usual summer slackness of the market was replaced by constant interest. This might be a surprise in the light of the austerity measures announced; still, it can be explained, primarily by the taxation of bank deposits from September. In addition to that, due to the price increases expected, accelerated purchases for investment purposes are showing a spectacular multiplication. An outstanding yield can be achieved in the case of projects (e.g. Sasad Liget) with good locations, good price/value ratios, with longer completion dates, where homes can be reserved at introductory prices and favourable (10-90% or 20-80%) timing for the payments.

On the basis of our database containing almost 600 ongoing residential projects, the unsold stock of homes is being gradually absorbed in the capital city. At the end of the 3rd quarter of 2006, there were about 1500 homes already completed waiting for an owner, i.e. one hundred less than half-a-year earlier. This can be attributed, on the other hand, to a diminishing number of new construction projects (this year, 11,000 homes are expected for completion, as opposed to 12,300 last year) and, on the other hand, this is due to a changing attitude of the purchasers, because search criteria such as a closer completion date or project already completed occur with increasing frequency.

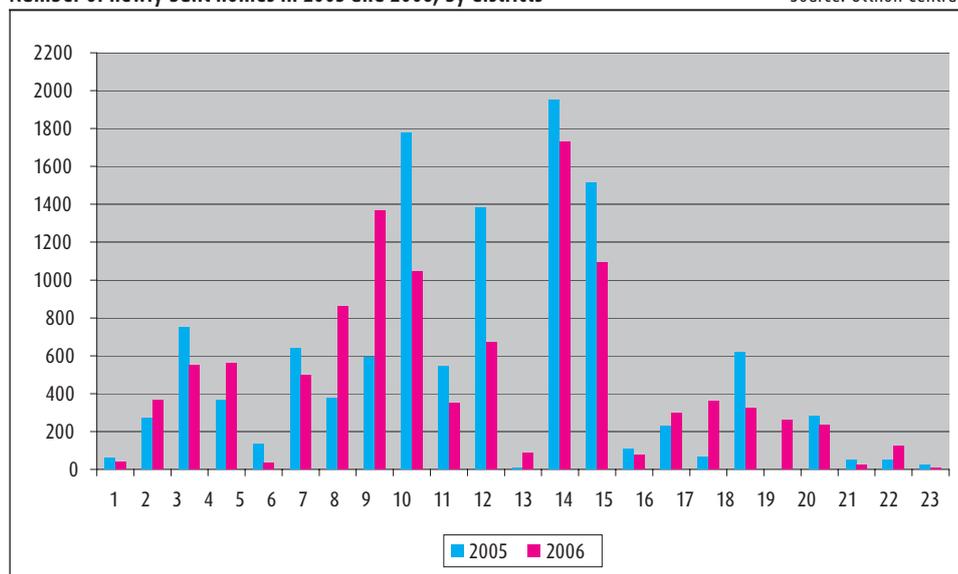
This is true in spite of the fact that purchases at an early stage have several advantages, because the investor's interest is to rev up sales at the very beginning of the selling stage and they try to entice buyers with different allowances for that purpose. Often, a favourable, low-installment payment schedule (10-90%) is provided solely during the introductory stage. Instead of a price allowance, provision of extra facilities occurs frequently – such as installation of kitchen furniture. Another allowance might be that the mandatory purchase of a garage can be postponed for after the early stage of the sale.

In addition to such immediately realisable benefits, with properties representing good investment, we can also achieve a significant value increase. For instance, with a downpayment of 10% for a project to be finished in 1.5 years from now, at a good location, with good plans (where in this period even a price increase of 15% can be realised), if we pay the remaining 90% and we sell the home right away, we can obtain a yield of 100%. Even after the deduction of the duty and of other associated costs, we retain a sizeable profit.

In the popular districts (13, 9, 14, 11), this year, the number of new homes completed shall be 15-55% lower than last year. This is attributable partially to the self-regulation of the market, but also to a shift in territorial focus, because in District 11, for example, with the saturation of the brownfield zone, the Sasad green area is about to boost. Meanwhile, the number of completed homes shall be more than doubled in District 7 and 8, and the offer is expanding spectacularly – although starting from low levels, of course – in District 4, 17 and 19 as well.

Number of newly built homes in 2005 and 2006, by districts

Source: Otthon Centrum



The big success of Sasad Liget in the Sasad segment of Újbuda and of the Sasad Resort project at Madárhegy might indicate the start of a quality turn in trends. In view of recent years' mass market dumping, there is an impressive increase in demand for residential park lifestyle, in classic green areas. Availability of comfort and security services, as well as sport facilities, high-level architecture, careful planning and a relatively fast access to the city centre are increasingly important requirements for an expanding stratum of home searchers. The energy certificate, already introduced from the 1st of September, orients towards a better quality in construction, as the investor will be obliged to certify the efficient energy use of any new homes.

The sale of garages, however, continues to be a general problem for investors. According to our experience, on the mass market, such as condominium houses in District 8, 9, 13, garage lots are sold at a proportion of about 20-30%. And in the best portions of the city centre, where parking is highly in demand and foreign buyers are numerous, up to 70% of the garages might have been sold by the time when the project is completed. It is not unprecedented, however, that here (where the purchase of garage lots is a good investment anyway, because of a lack of safe parking lots) the investor tends to build more such lots than provided for in the construction permit, offering these to external buyers.

Also in respect of garages, methods have been developed to incite purchases. Wherever the purchase of a garage is mandatory, the buyers can replace that obligation with redemption payable to the investor. This is a fee amounting to 20-25% of the garage price, still, should the buyers change their mind and decide to buy a parking lot prior to the completion, this amount shall be included in the price of the garage. Furthermore, in respect of homes, proven schemes with a payment timing of 10-90%, as well as payment by instalments are also increasing. Investors can also launch campaigns; for instance, any home buyer who brings one more buyer, obtains a free parking lot. Where the purchase of a garage is mandatory for each home, but part of the potential buyers has no car at all, the buyers of the studios can be granted an exemption. And in the case of projects where a low number of garages are expected to be sold, lots are offered at the level of their construction cost.

Typical garage prices in Budapest, by market segments

Inner city of Pest	2.8-5.0 million HUF
Inner Buda	3.0-4.0 million HUF
Buda, green area	2.2-3.8 million HUF
Mass market (e.g. District 9, 13)	1.8-2.7 million HUF
Lower-end mass market (e.g. District 10, outer parts of Pest)	1.4-2.5 million HUF
Castle Hill area	3.5-5.5 million HUF
Pest, external garden cities	1.3-2.6 million HUF
Ground-level parking lot, in general	0.4-1.7 million HUF

Source: Otthon Centrum

From among county capitals, important activity is observed in the case of Debrecen, Győr, Szeged, Pécs, Nyiregyháza and Veszprém. In these cities, there are 4-6 larger ongoing projects at present. The unit prices of the condominium houses being built here range between 230,000 and 290,000 HUF/sqm. A 300,000-average limit is exceeded in the case of some large projects in Pécs and Veszprém and in the case of almost all projects in Győr, due to its location by the Danube. A wide offer is available also at Lake Balaton. In almost a dozen of larger condominium houses under construction at Siófok and Balatonfüred, prices start from 300,000 and, in the case of the penthouse flats with panorama, even the 500,000 HUF/sqm threshold might be exceeded.

MARKET OF SECOND-HAND HOMES

According to our survey, in terms of willingness to buy homes from existing owners, such purchases are increasingly overshadowed – even if, naturally, their share is still far larger than the share of the newly-built ones. While during this last year, 29% of those who bought a home in Budapest bought a newly-built property, among those who intend to buy one within the next year, this category represents 37%. Supposing that in an actual purchase, many of them will finally decide to go for second-hand homes, the trend is obvious. In the countryside, this trend is even more marked, with ratios of 23% and 36%, respectively. Even though there are no major differences by age groups, an interesting feature is that homes from previous owners are bought mostly by people who are below 25 years of age and those above 56.

The main motivation for buying a home today is independence. Nationwide, the share of those who would like to buy a home for this reason is above 40%-72% of them are below the age of 35 years – and quarter of the buyers say they are not satisfied with the size of their homes. The hit clearly remains a home with two rooms. In Budapest, 31%, in the country, 29% of the people with an intention to buy indicate this category. Countrywide, homes larger than that account for 40% of the turnover.

Price changes of block of flats and brick-built flats, in some districts

District	Nominal price change at block of flats, 1998-2004 (%)	Nominal price change at brick-built condo houses, 1998-2004 (%)
III.	307	345
IV.	323	342
IX.	286	415
XI.	298	324
XIII.	290	384
XIV.	312	330
XVIII.	323	355

Source: Otthon Centrum (on the basis of the Hungarian Office of Duties and Levies)

Even though it is well-known that prefabricated block of flats are the 'poor cousins' on the market, even today, every 6th-7th buyer votes for these. The value of block of flats in real terms shows, for the whole of the last one-and-a-half decades, a slightly downward trend. The background thereto is a significant fall in market demand for this type of housing products. In districts that provided the scene for large volume housing projects in recent years, the rates of the price increase for block of flats is typically below the rates observed in respect of brick-built condominium houses. The difference is particularly large in District 9 and 13, both being model areas for mass housing construction. By now, in Budapest, a difference of 15-25% is observed in the prices of these two types of homes, in favour of the brick-built homes. This is the right difference to provide room for the buyers' sensitivity to pricing in their selection, while keeping demand for block of flats at constant levels.

The main problem about block of flats represents the useful value of the homes, more specifically, the high maintenance costs. The Panel Plus Loan Programme, extended last summer until the end of next year provides a preferential loan for the inhabitants' own contribution to energy-saving upgrades, renovation of the machinery and landscaping of the environment, under the condition that the refurbishment costs shall not exceed 1.2 million forints per home. According to the experience of Otthon Centrum, the programme did have an impact on the market of block of flats. In the buildings where the application was successful, the flats could be sold faster, and at prices closer to the initially published ones. In order to achieve further favourable effects, however, in addition to an extension of the programme, more efficient publicity, marketing would be also required. The point is that buyers typically are not looking for a new home in a building upgraded recently, in a target-oriented way or in a building that shall undergo a renovation within short – they mostly don't even have any information on this possibility. It is rather those who are offering flats in refurbished buildings who are in a better bargaining position and who can sell their properties more easily.

The main search criterion for the buyers of block of flats, however, is not quality, but rather price. A limit of ten million forints (sustained from Újpest to Újbuda, basically, in equal measure) is a good delimitation for the category of small flats, high in demand, relatively easy to sell from the larger block of flats, more expensive in terms of maintenance costs. Demand for dwellings in the range of 7-10 million HUF is boosted by the fact that these are ideal for students in Budapest and can be bought by parents living in the country even without the need for loan.

As witnessed by our country-wide survey, in the county capitals, the most important demand is seen for block of flats in the range of 7-9 million HUF, 50-60 sqm and, at the same time, dwellings in condominium houses of the same size or of one category higher, at 60-80 sqm, built a few years ago (in the range of 12-18 million HUF). At the same time, usually, it is very difficult to get rid of large-size detached houses, built in the eighties. For the time being, the oversupply of the newly built homes often means a price pressure on the second-hand market, therefore, a further stagnation of the prices is expected there. But we already mentioned earlier that, at least in the capital city, the overweight of supply is becoming moderate. Partly because of this, and partly because of a permanent increase in developer costs, in respect of newly built homes, a price increase shall be expected. And that will create a realistic possibility for a price increase in respect of second-hand homes as well.

The market share of property agencies is about 40% in terms of properties sold. The basis for an increase in this share is that a growing number of people realise the advantages of professional sales management. Among these, as our research has also shown, selling time (several times faster than in private sales) is of outstanding importance.

MARKET OF RENTED HOMES

In late summer, after the announcement of the admission results for high education, up until early September, the usual churning was experienced on the letting markets of the university cities. In addition to studios, demand is the highest for dwellings with two or three separate rooms, which are more cost-efficient for use by several persons. Such homes of 40–50 sqm are typically offered at the price of 60–65,000 forints in the favoured parts of Budapest, while in large cities of the countryside, these are 10% cheaper. The typical renting period is one year. In many cases, after the first school year at the university, college, the parents rather decide to buy a home for their student children. This is the time when demand for block of flats in the neighbourhood of the universities is boosting.

For young people employed or for married couples, central location and good transport connection are also important, but they may be looking for homes, subject to their workplaces, in outer districts as well. Depending on their earnings, they usually pay a rental of 60–120,000 forints.

No longer in the volumes observed 4–5 years ago, but still, managers of the local subsidiaries of foreign companies and other businessmen are looking for rented homes, for a couple of years. In their case, interest mainly is in some favoured, higher-prestige streets of the inner city of Pest, and they are ready to pay typically an amount of 150–250,000 forints for the rent. In the mountainside portion of Buda, even multiples of this price occur, but this is not the typical rental.

For tenants, the good condition of the dwelling is more and more important and, particularly for students, broadband internet connection is important. In addition, demand is increasing for newly-built homes available for rent. When making their selection on sublets, foreign students typically make their decisions faster, while Hungarians may have a look at dozens of them before they make up their mind. Caution money tends to decrease from three months to a one-month period. Already since years, it is not realistic to expect an increase in rentals. Subsequent to the introduction of the property tax in 2008, an eventual further pressure on the supply side (when a large number of empty, unused properties might come to the market in the quality of rented homes) might lead to a drop in the rates.

MARKET OF BUILDING / DEVELOPMENT PLOTS

The main stress remains on the market of plots suitable for the construction of condominium houses in the inner city. A good indication of investors' activity is that in Inner Buda, where offer is very limited according to our experiences, 60% of the sites (a total of about 7000 sqm) change hands every year, while in the inner city of Pest, this ratio is 70% (a total of about 10,500 sqm). The same ratio in the high-prestige, mountainside portions of Buda and in the external districts of Pest is only at about 15% – although the offered volumes are far higher. According to our estimates, annually about 1.3 million sqm land, suitable for building of condominium houses, change owners in the capital city.

From the table attached it becomes evident that the most spectacular price increases continue to take place in the areas that are close to the centre of the

city. Even so, in spite of a continuous upward trend, actual contractual prices for land keep lagging behind the published prices. Pricing bargains became usual on the market of land, too. Only about every third of the plots suitable for condo development are sold at the ask price, whilst half of the deals are made at a rebate of 10–25%. Moreover, in some cases, the final price sometimes may be higher than the list price was. All this is a function of the contractual terms and, in particular, of payment terms.

Typical prices of plots suitable for condominium development

Area	Net plot price projected on net saleable sqm of residential area (HUF)	Price trend in a comparison to the previous half-year
Inner portions of Districts 1, 2 and 12	120–180,000	↑↑
Districts 6 and 7, within the limits of Nagykörút	100–170,000	↑↑
Districts 6 and 7, outside the limits of Nagykörút	70–110,000	↑↑
Former brownfield zone of District 11	30–50,000	–
Rehabilitation area in District 9	40–60,000	–
The Angyalföld portion of District 13	40–50,000	↑
District 14	40–80,000	↑
Rehabilitation area in District 8	40–65,000	↑↑
District 10	20–30,000	↑

Source: Otthon Centrum

The sellers of the land lots with the highest value are Hungarians and Israelis, while the buyers nowadays mostly are investment companies from Western Europe – mainly from Spain. Smooth trading at levels of hundred millions-billions is often hampered by differences in business attitudes. The point is that seriously interested buyers would be ready to make an offer after a due diligence period of 4–6 weeks and they expect the seller not to leave the land on offer in the meantime. As to the sellers, 95% of them are ready to do so only against a special fee or earnest money.

In Budapest, integrated areas suitable for being parcelled are already very scarce. In addition to the recently sold parcels of Madárhegy in District 11, parcelling may take place in District 17 and 18, in a private investment exercise, with a total of less than 100 sites.

In Pilisjászfalu, 300 sites were parcelled recently, and these are for sale now at prices of 6–8000 HUF per square meter. In Gyömrő, 234 lots were parcelled, available on the market with unit prices of 11,400 HUF. In Pécel, 100 lots are expected to come and parcelling is under preparation also at Szigetszentmiklós (at 8–10,000 HUF/sqm), Ráckeve (1500 HUF/sqm), Halásztelek and Szigethalom as well. In the more expensive western part of the agglomeration belt, large-scale parcelling is in process in Nagykovácsi (about 20,000 HUF/ sqm), Telki (12,500 HUF/sqm), Tinnye (4–6000 HUF/sqm) and Diósd.

Prices of construction sites in some larger settlements of the Budapest agglomeration area

Settlement	Typical prices for sites ('000 HUF/sqm)
Szentendre	15–20
Pomáz	12–16
Pilisvörösvár	14–16
Üröm	28–30
Dunakeszi	12–17
Veresegyház	9–13
Gödöllő	9–15
Pécel	9–11
Dabas	5–10
Dunaharaszti	10–15
Szigetszentmiklós	7–14
Budaörs	25–40
Nagykovácsi	12–22
Solymár	12–30

Source: Otthon Centrum

Upon request, we also prepare structured reports on the property market; please contact us at:



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