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CEE REAL ESTATE ADVISORY PRACTICE

CEE Property Lending Barometer 2012

A survey of banks on the prospects
for real estate sector lending in CEE

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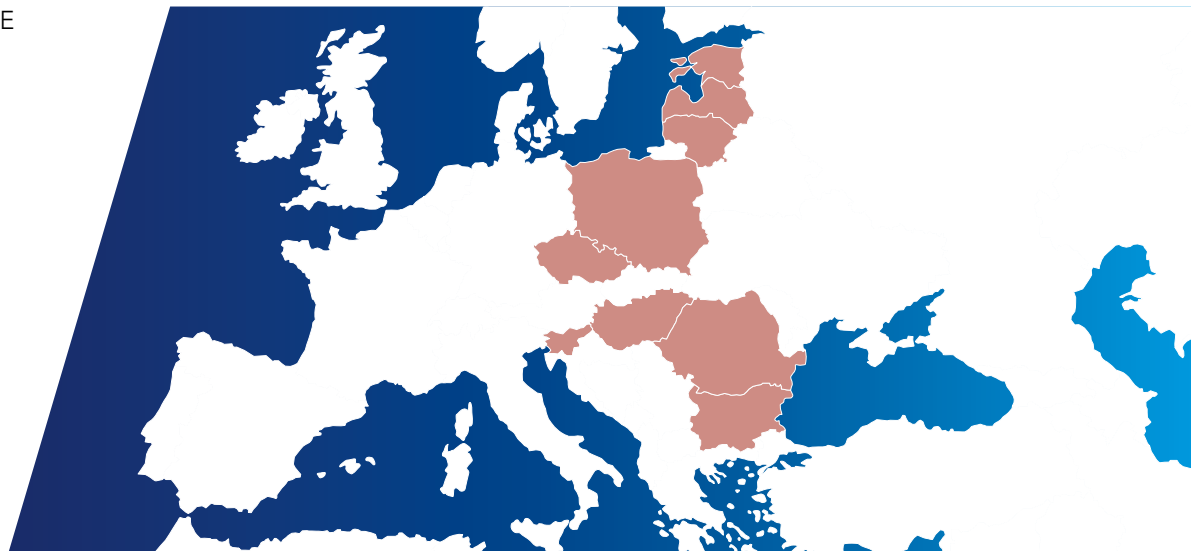
Dear Reader,

I am delighted to present the Central and Eastern European (CEE) Property Lending Barometer 2012. After showing signs of recovery last year, in most of the countries the real estate sector appears to be entering a renewed period of recession this year. The performance of real estate in different countries and asset classes still varies widely.

As a follow-up to previous years' surveys, we have conducted a survey amongst leading banks in the region, with the purpose of assessing the prospects for bank financing in the real estate sector in CEE. The barometer includes input from over 35 banks active in these markets, mostly obtained from in-depth interviews. Representatives of leading financial institutions have provided their views on the key issues affecting property lending. The following countries were included in the 3rd edition of the survey: the Baltics, Bulgaria, the Czech Republic, Hungary, Poland, Romania and Slovenia.

Many banks still have significant non-performing real estate loans to manage. In this report, we first focus on how banks are managing these non-performing loans; we then assess how banks are strategically approaching real estate lending and what they expect for the next 18 months. Finally, we address the prospects and terms available for developers and investors to finance new real estate developments and income-generating properties.

■ Surveved countries in CEE



The survey provides insights for developers and investors alike on the future prospects for real estate financing, and enables banks to benchmark their practices with their peers.

Some highlights from the CEE Property Lending Barometer 2012 are:

- The prospects for the real estate market in a given country remain generally linked to its macroeconomic outlook.
- Banks are still looking to restructure existing loans which are in default, rather than seeking foreclosure. Higher quality projects with a potentially strong business model have a better chance of successful restructuring.
- Basel III is likely to make bank financing more expensive.
- Compared to a year ago, banks are focussing less on real estate financing.
- Banks are still more interested in financing income generating projects than development projects, whilst their openness to finance new developments decreased slightly in comparison to 2011.
- Bank expectations on the potential increase in the size of their future loan portfolios show a generally negative shift in sentiment in each country surveyed.
- The hotel sector remains the least preferred by banks in terms of financing, but again good projects can obtain reasonable terms.

I would like to take this opportunity to thank all of the participants in this survey. Their co-operation is key to the success of this initiative.

As the initiator and coordinator of this survey, I hope you will find our report informative and enlightening in supporting your future business decisions related to real estate financing.

If you would like to receive any clarification or discuss this year's survey results, please feel free to contact any member of the Real Estate Advisory Practice of KPMG in Central and Eastern Europe or me.

Yours faithfully,

Andrea Sartori

Abbreviations

BAL	The Baltics
BUL	Bulgaria
CZE	Czech Republic
HUN	Hungary
POL	Poland
ROM	Romania
SLV	Slovenia

Methodology, sample profile and survey limitations

This survey aims to provide an analytical overview of the approach of banks to real estate financing in the Central and Eastern European region. The following countries are represented in the 2012 survey: the Baltics¹, Bulgaria, the Czech Republic, Hungary, Poland, Romania and Slovenia.

Data collection for the survey was primarily made through in-depth interviews with bank representatives. Depending on the organisational structure, interviewees were the heads of real estate, project financing or risk management departments. Banks were selected from among the leading financial institutions operating in each individual country. The survey participants included over 35 banks active in the real estate market in CEE and the data collection for this survey took place from May through to July 2012.

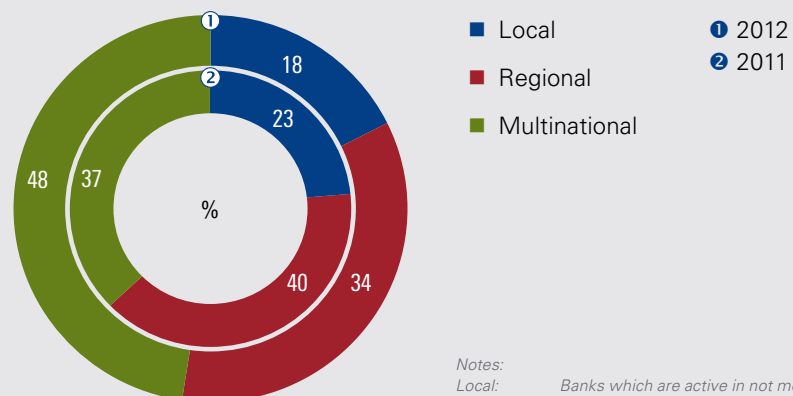
Approximately 18% of survey participant banks were local banks, i.e. they operate predominantly in one country within CEE, whilst regional or multinational banks comprise larger shares of the respondent mix.

Survey limitations

The following limiting factors should be noted:

- When the answers provided to specific questions were not sufficient to provide reliable information on a specific country, we have indicated this, or the country was omitted from that part of the analysis.
- In the case of some parameters and some cross tabulations, the output of the survey may be considered indicative but not representative due to a low number of responses.
- As in past years, our assessment of the residential sector excluded residential projects with construction costs below EUR 10 million.
- Some of the answers to the survey's queries should be considered as an expression of opinion or may be timely market information that is subject to change over time.
- As Slovenia was not included in the 2010 survey, it is not represented in the comparable 2010 results.

Geographic orientation of the banks included in the surveyed sample



Notes:

Local: Banks which are active in not more than 2 CEE countries

Regional: Banks which are active in at least 3 CEE countries excluding multinationals

Multinational: Banks which are active on at least 3 continents

Source: KPMG in CEE Property Lending Barometer 2012

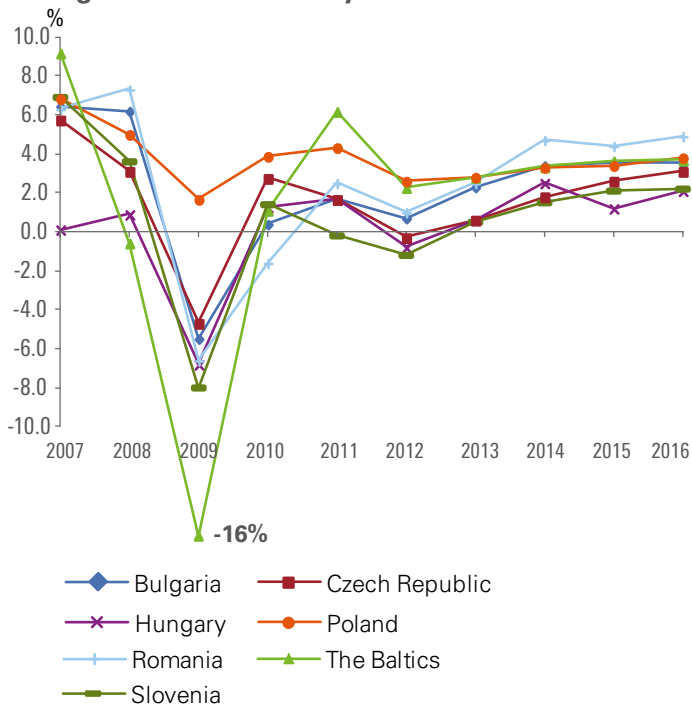
¹ Based on responses received from the banks surveyed the Baltic countries may be grouped together from the point of view of bank financing.

Overview of the CEE Real Estate market

The Eurozone crisis is still leaving its mark on Europe, including the CEE region, and prolonging uncertainty for good economic prospects. At a summit in late June 2012, European leaders outlined further strategies, including a EUR 120 billion growth package for dealing with the debt crisis and strengthening the Eurozone over a longer time horizon. Investors initially responded favourably to the broad policy announcements, but optimism soon disappeared due to a lack of detail and uncertainty about the implementation of the measures.

The CEE region is still an area with decent potential, which is mainly attributable to a few economies performing adequately such as Poland, whose economic growth has been one of the highest on the continent. However, these positive signs are not matched across the region. The economic climate varies greatly, both in economic and political terms.

GDP growth in the surveyed CEE countries



Note: growth figures for 2012-16 are forecast by EIU.
Source: Economist Intelligence Unit, 30 August 2012

Real GDP change among surveyed countries (%)

	2010	2011	2012 (f)
Bulgaria	0.39	1.67	0.70
Czech Republic	2.74	1.66	-0.30
Estonia	2.26	7.64	2.10
Hungary	1.26	1.65	-0.80
Latvia	-0.33	5.47	2.20
Lithuania	1.44	5.87	2.40
Poland	3.87	4.32	2.60
Romania	-1.60	2.50	1.00
Slovenia	1.38	-0.2	-1.20

Source: Economist Intelligence Unit, 30 August 2012

Unlike many slow-growing or recessionary CEE markets, the **Polish economy** is in the favourable position of not being burdened by excessive debt. However, its growth forecast still remains far below pre-crisis levels. GDP growth is expected to slow down to 2.6% in 2012, due to weakening domestic demand, the upcoming period of fiscal austerity and the overall slowdown of the Eurozone.

The **Czech Republic** is one of the more mature markets in the CEE region, but is heavily dependent on exports to the slowing German economy. Estimates for GDP growth in 2012 have been continually downgraded throughout the year to -0.3% with further downside risk.

In **Hungary**, any future reduction of excessive indebtedness will come at the expense of growth and future purchasing power. Banks are in a difficult situation, due to an additional bank tax and foreign currency loan legislation – they have no appetite for lending in an unpredictable Hungarian economy.

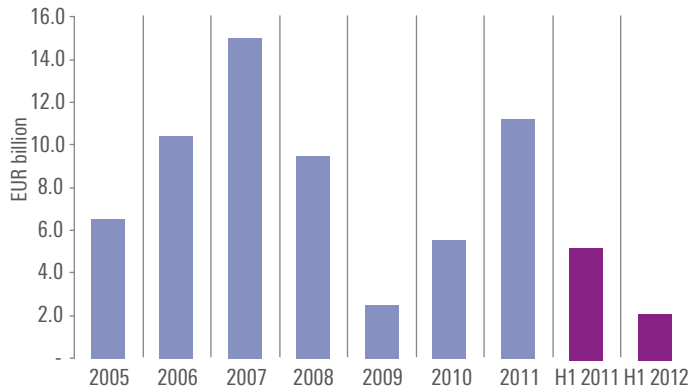
The **Bulgarian** government's austerity programmes towards future euro adoption have produced some sound financial numbers, but the cost to the real economy has been harsh in terms of growth and consumption. In 2011 the economy showed signs of moderate recovery with 1.7% growth, which has proved fragile and turned out to be unsustainable.

Like the other markets, Bulgaria's growth rate is expected to slow to 0.7% in 2012.

Romania entered a technical recession at the start of 2012 after two successive quarters of negative growth, reporting 0.1% in the first quarter this year. After signs of recovery of 2.5% GDP growth in 2011, the Romanian economy is expected to slow this year to 1.0%.

In **Slovenia**, after the deep recession of 2009, economic growth returned in 2010, with real GDP increasing by 1.4%. However, economic performance began to deteriorate in the second quarter of 2011, pushing the economy back into recession in 2011. Domestic demand has remained sluggish and, as in previous years, household consumption will be constrained in 2012 by continuing high unemployment and by the debt-servicing requirements facing many consumers after years of high borrowing. The rising amount of bad debts in the country's banking sector and the rising borrowing costs of short-term government debt give grounds for concern that Slovenia might become the sixth Eurozone country to need a bailout.

Total real estate investment transactions in CEE, 2005 – H1 2012



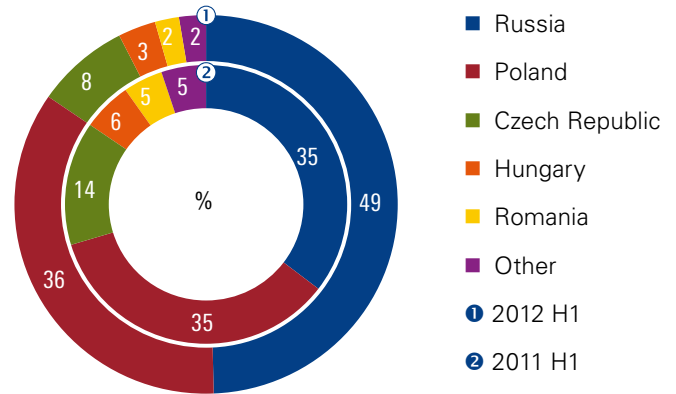
Source: CBRE

Note: In this table CEE includes Bulgaria, Croatia, Czech Republic, Hungary, Poland, Romania, Russia, Serbia, Slovakia and Ukraine

In line with the economic slowdown in 2012, investment sentiment remained at a low level in the region. The ongoing uncertainty in Europe resulted in a significant decrease in the value of investment transactions reported for the first half of 2012 compared to the same period last year.

Following a strong 2011, the first half of 2012 brought no major investment activity in most of the countries within the region, resulting in a 60% drop in investment levels compared to H1 2011. The recorded transaction volume in the first half of 2012 was approximately EUR 2.1 billion.

CEE real estate transactions broken down by country



Source: CBRE

Even more striking than in the first half of 2011, only two countries showed significant investment activity in H1 2012: Russia and Poland. These two countries combined accounted for over 85% of the invested capital in the region (70% last year), whilst no other country, with the exception of the Czech Republic, can boast investment activity in excess of a 5% share of the real estate transactions in the CEE market.

As for the outlook for H2 2012, Poland is expected to drive commercial real estate investment volumes in the CEE, even though purchasers will be more selective about real estate investments. According to forecasts, the value of transactions on the commercial real estate market in Poland will reach between EUR 2 and 2.5 billion and should be comparable to 2011.



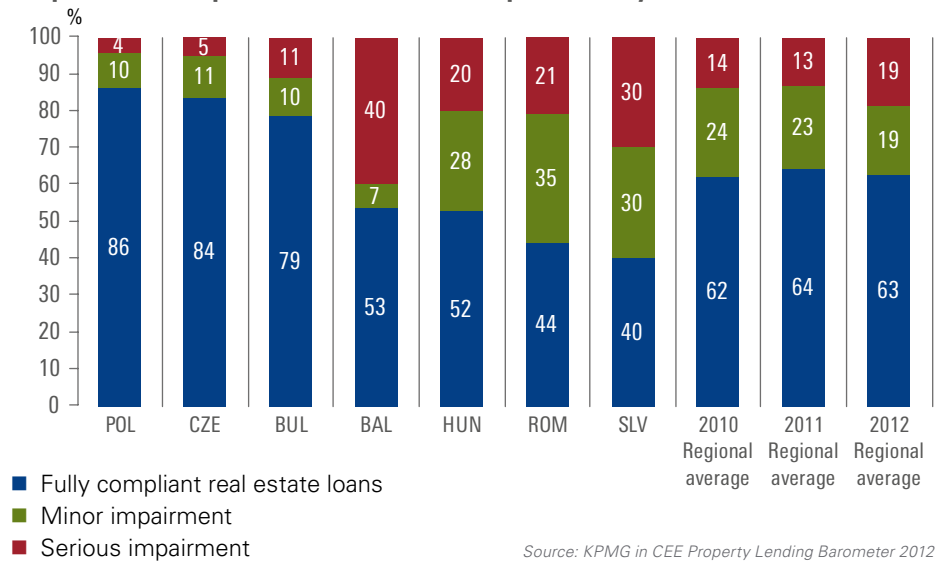
Managing impaired loans

The global economic crisis had a detrimental impact on the financing of the real estate sector. However, many banks in the region still have large real estate portfolios, a sizeable proportion of which are not performing. In this part of the survey, we focus on banks' opportunities to manage real estate loans where debtors cannot pay their capital and/or interest on time, or there is technical breach of contract terms.

Current state of and future expectations for impaired loans

Based on the responses collected this year, the highest ratios of impaired real estate loans are in Slovenia (30% serious and 30% minor impairment), Romania (21% serious and 35% minor impairment), and Hungary (20% serious and 28% minor impairment), whilst the highest proportions of fully compliant loans are in Poland (86%) and in the Czech Republic (84%)². These results generally reflect the overall macroeconomic conditions of the countries under review. With the exception of the Baltics and Romania, the ratio of impaired loans increased from last year in each of the surveyed countries. The ratio of fully compliant real estate loans was stable at a low level in Romania, whilst it decreased slightly in Slovenia. The regional average did not change significantly compared to last years' findings.

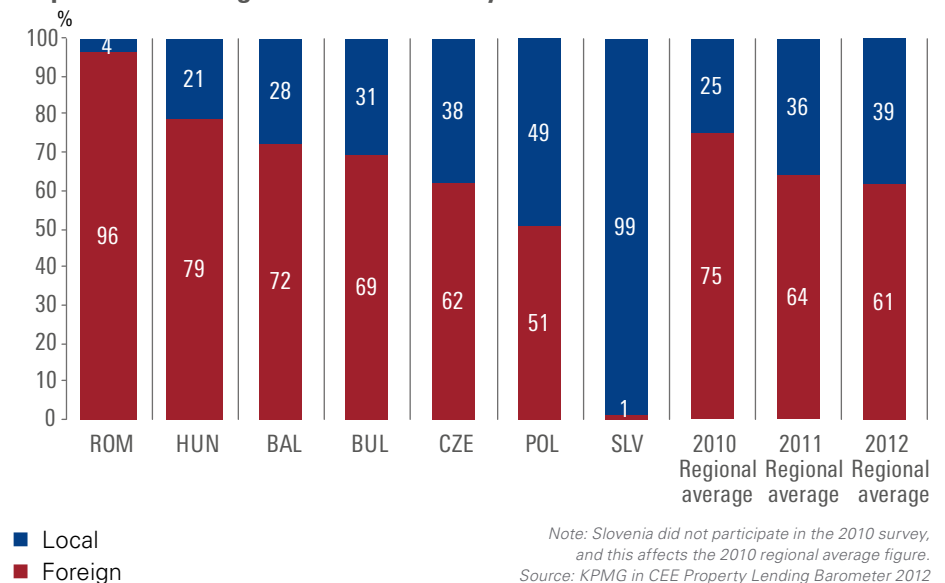
Proportion of impaired real estate loans per country



Source: KPMG in CEE Property Lending Barometer 2012

The regional average of foreign currency denominated loans is 39% in 2012. Data from the countries surveyed – except for Slovenia where the euro is the local currency – show that a higher proportion of local currency loans is correlated with a higher proportion of fully compliant loans. Compared to the 2011 survey, the percentage of foreign currency denominated loans decreased considerably in the Baltic countries.

Proportion of foreign and local currency real estate loans



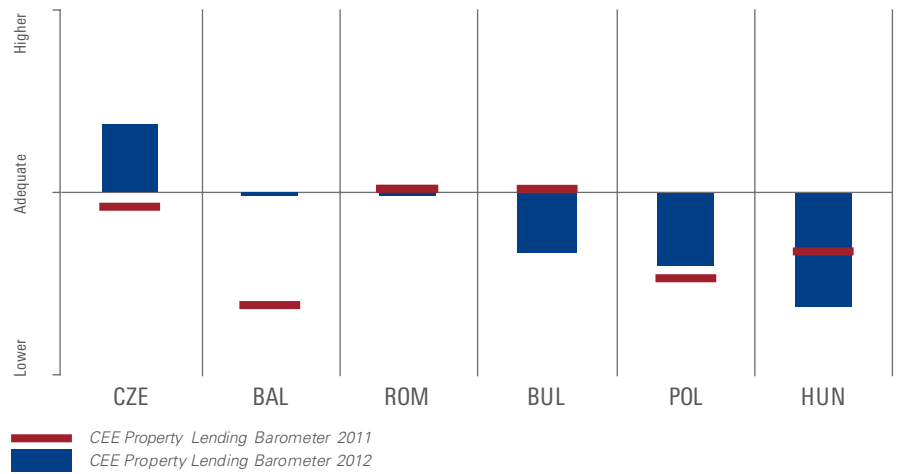
Note: Slovenia did not participate in the 2010 survey, and this affects the 2010 regional average figure. Source: KPMG in CEE Property Lending Barometer 2012

² For some counties (especially Romania, Bulgaria and the Baltics) the results are skewed by small sample sizes for this question and may not be representative.



Provision levels are considered below adequate in Hungary, Poland and Bulgaria, while they are considered adequate in Romania and the Baltics. Only Czech banks indicated moderately higher than adequate real estate provisions.

Banks' perception of the level of real estate loan provisions

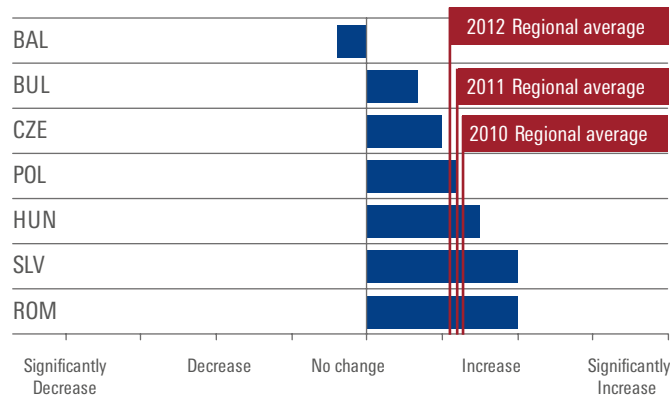


Source: KPMG in CEE Property Lending Barometer 2012

The level of provisions (loan value adjustments) is not expected to decrease significantly in any of the countries surveyed before the end of 2012, except in the Baltics. In Romania, Slovenia and Hungary banks expect a significant increase in the level of provisions this year. The responses to a related question – regarding the expected change in the proportion of problem loans as a percentage of the total real estate lending portfolio – show a similar pattern.

These results, overall, suggest that banks still do not expect a recovery in the real estate market any time soon.

Expectation for changes in the amount of provisions for real estate loans

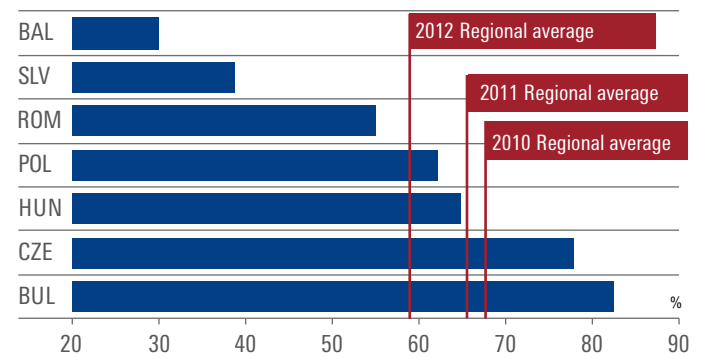


Source: KPMG in CEE Property Lending Barometer 2012

Restructuring as an opportunity to manage impaired loans

Most representatives of banks in all countries believe that impaired loans may be managed successfully through restructuring. Similarly to the previous year’s findings, responses were especially positive in Bulgaria and the Czech Republic, where the majority of respondents believe that more than 75% of impaired loans may be restructured successfully. The picture is gloomier in the Baltic countries where, according to the respondents, only about a third of impaired real estate loans are expected to be successfully restructured. Although the regional average is lower than last year, the proportion of potentially renegotiable loans did not change dramatically in the surveyed countries.

Proportion of impaired real estate loans that may be managed successfully through restructuring



Source: KPMG in CEE Property Lending Barometer 2012

These results confirm that banks are still doing their best to actively manage their real estate loans rather than immediately seeking foreclosure. The rescheduling or restructuring of loans is understood to be a good approach, at least in the short term. While it is still unclear whether restructuring will be an effective long-term solution, banks continue to choose this option.

The primary precondition before any restructuring is the cooperative behaviour of the borrower. Once this condition is met, a strong business model is the most important factor to drive successful restructuring, together with additional equity being available.

Unsurprisingly, there was no significant change regarding the top criteria in comparison to the two previous editions of the survey.

Most important criteria for successfully restructuring non-compliant real estate loans	
Strong business model/quality of the asset	•••••
Additional equity	•••••
Market prospects	••••
Additional collateral available	••
Opportunity to increase the bank’s margin	•

Source: KPMG in CEE Property Lending Barometer 2012

Overall prospects for banks' real estate portfolios

In this section, the expectations of banks for the future of their real estate loan portfolios are assessed in light of recent developments and their strategic approach to real estate financing.

Compared to last year's outlook, the surveyed countries exhibited a constant or decreasing appetite for real estate financing in 2012. Even in Poland and the Czech Republic, where the forecast regarding the importance of real estate financing in their portfolio development in 2011 was positive, the outlook is less favourable. Results from Romania and the Baltics suggest that banks feel the heavy pressure on the real estate market and do not foresee a quick recovery in the sector compared to other sectors of the economy.

Change in the focus of real estate financing within banks' lending activities

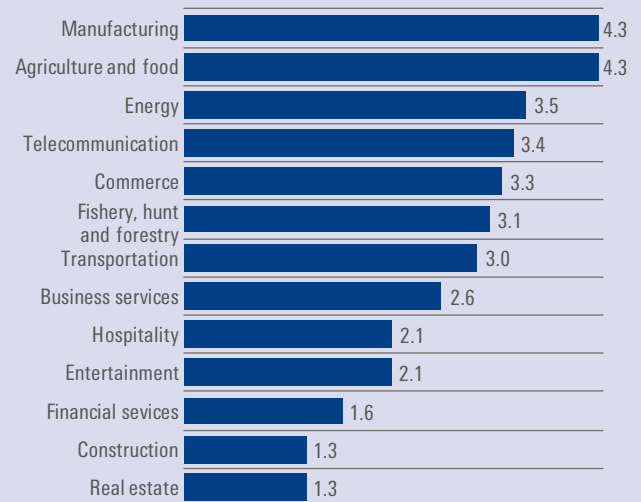
	2010–2011	2011–2012
POL	↑	↔
ROM	↑	↓
CZE	↑	↔
BAL	↔	↓
HUN	↓	↔
SLV	↓	↔
BUL	↓	↔
Regional average	↑	↔

Source: KPMG in CEE Property Lending Barometer 2012

In Hungary, the focus on real estate is getting worse in comparison to last year. This is supported by another recent survey conducted by KPMG in May 2012, in which 10 leading Hungarian commercial banks and the Hungarian Development Bank were queried about their industry preferences for corporate lending. The least preferred sectors for lending were the real estate, construction and financial services sectors.

Attractiveness of the industries

(1 – Not attractive, 2 – Below average attractive, 3 – Average, 4 – Above average attractive, 5 – Attractive)



Source: KPMG Corporate Lending Sentiment Index 2012

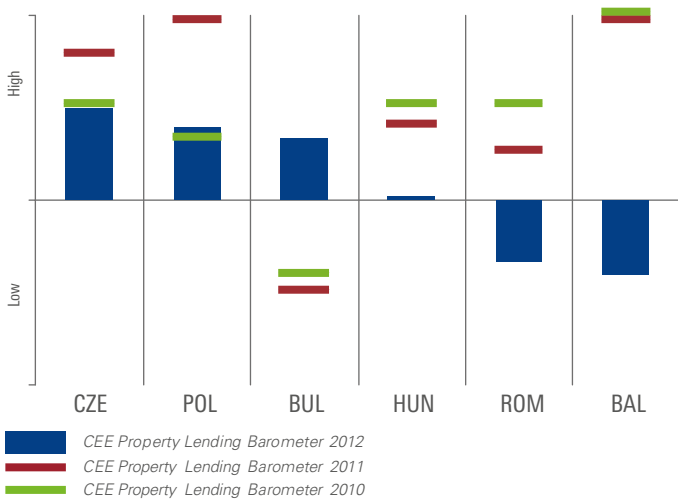
“We do have real estate loans in our portfolio, but I wish we didn’t.”

Bank representative, Hungary

Real estate projects are strategically more important to banks in the Czech Republic, Poland and Bulgaria. In most countries banks are less enthusiastic about the long-term prospects of the real estate market and continue to monitor developments. Furthermore, the strategic importance of real estate financing may also reflect the fact that a number of banks have significant non-performing real estate loan portfolios that they have to manage.

Overall, there has been a negative shift in the strategic importance of real estate financing expressed over the last two years. The most significant change in attitude is found in the Baltic countries, where banks attributed relatively high strategic importance to real estate financing in 2010 and 2011, but show reduced interest in 2012. On the other hand, the Bulgarian results highlight a more positive sentiment compared to the previous two years. These findings do not fully reflect the underlying macroeconomic conditions and might not prove to be enduring.

Strategic importance of real estate financing for banks



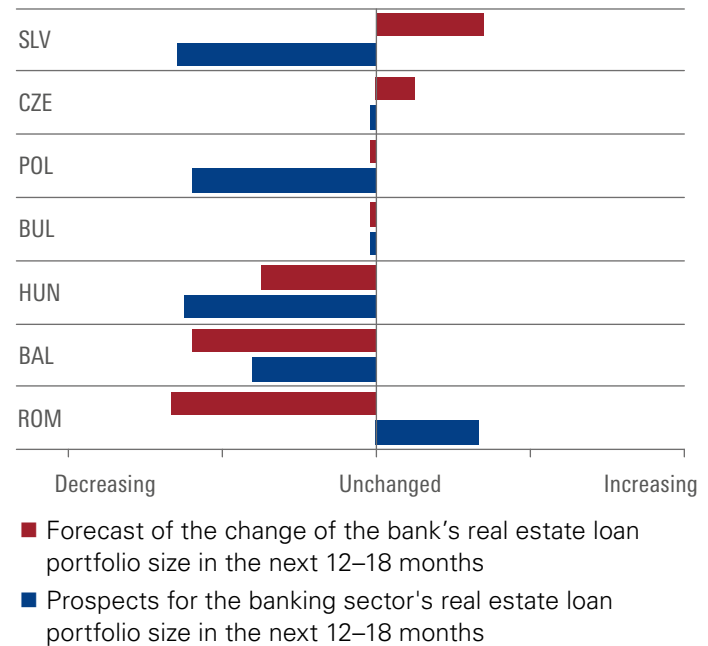
Source: KPMG in CEE Property Lending Barometer 2012

The future of real estate loan portfolios

Bank sentiment towards real estate loan portfolio size varies greatly from country to country and from year to year. This year Czech and Bulgarian responses indicated fairly neutral growth prospects in their own and the sector’s real estate portfolio. Hungarian and Baltic banks expect negative growth prospects, i.e. they expect the size of their real estate loan portfolio and those of other banks to decrease. In Poland, Romania, and Slovenia banks indicated different prospects for their own bank compared to the growth of the sector as a whole. Romanian banks assume that the Romanian banking sector will considerably outperform their own performance in terms of the size of the portfolio, while in Poland banks foresee a decreasing loan portfolio at the sector level, but no change in their own loan portfolio. Comparing the banks’

future expectations with last year’s results, there is a general negative shift in sentiment in each country surveyed.

Banks' forecast on the change in size of the loan portfolio in the next 12–18 months



Source: KPMG in CEE Property Lending Barometer 2012

Banks were also asked to identify the key drivers affecting their real estate portfolio. The most significant factor is the local macroeconomic environment. The ranking of the European macroeconomic environment has gained importance in comparison to the 2011 results. A lack of investors, equity and prime properties have also been identified as equally important restricting factors.

In respect of the question as to where banks expect additional funds to come from if the overall size of their share in financing decreases, the majority of banks indicated private equity and additional developers/investors as the most relevant sources.

Most important factors affecting real estate loan portfolios



Source: KPMG in CEE Property Lending Barometer 2012

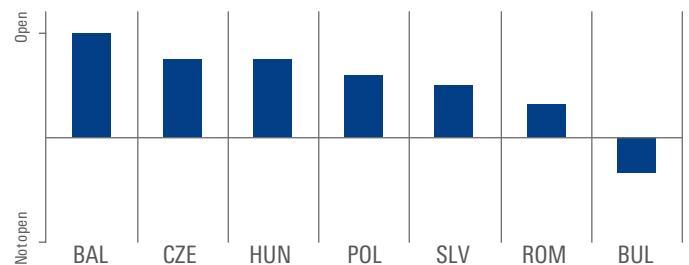


In terms of real estate loans maturing in the near future, on average 20% of real estate loans are due in the next year and 40% are due within two years. Compared to the data from the previous year, the proportion of short-term loans is increasing as previously granted facilities gradually expire, while the overall portfolio contracts.

The willingness to refinance loans due in the next two years is generally positive across these countries. Taking into account the country averages, banks are reasonably open to refinancing, although Bulgarian and Romanian banks are relatively less open. The attitude of the surveyed banks to refinancing did not change significantly compared to the previous year's findings.

Less than 10% of the surveyed banks are considering disposing of part of their commercial loan portfolio.

Openness of banks to refinance loans coming due in the next two years



Source: KPMG in CEE Property Lending Barometer 2012

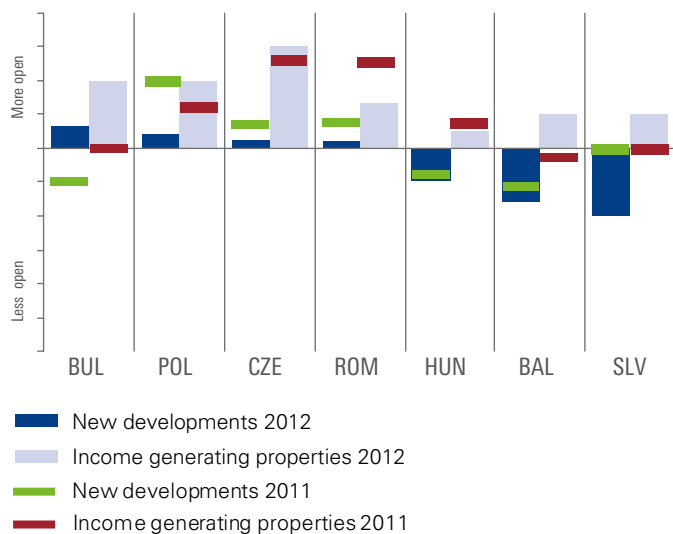
Bank representatives were asked to comment on how Basel III regulations will impact their business. The majority responded that the new regulations would not have significant effect; however they are expected to negatively affect the size of their real estate loan portfolios. In most countries banks expect an increase in the margins applied by banks due to the regulatory changes, which will make financing more expensive.

Opportunities for financing new real estate projects

This section assesses the opportunities for developers to obtain bank financing for real estate projects, as this is still the most important issue that developers face in the current environment.

The majority of the bank survey respondents are still more interested in financing income-generating projects than development projects. Overall, the openness to finance new developments decreased slightly in comparison to 2011, after a quite significant increase from 2010.

Openness of banks to finance development/ income-generating projects



Source: KPMG in CEE Property Lending Barometer 2012

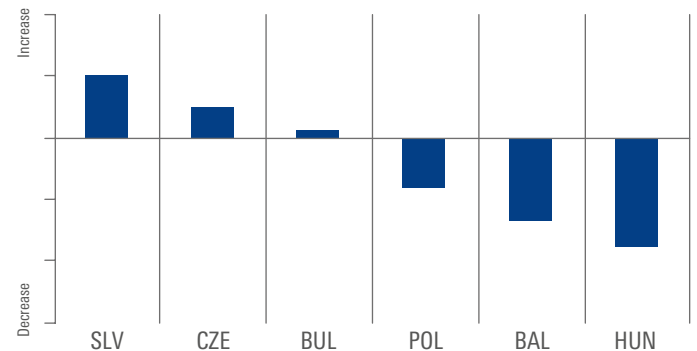
The majority of the positive responses are from countries that have a high proportion of fully compliant real estate loans: the Czech Republic, Poland, and Bulgaria. Meanwhile, banks in Hungary, the Baltics, and Slovenia are proportionally less open to real estate financing than their regional peers. In Poland, interestingly, in comparison with last year's results there is a shift of interest to income generating assets rather than new developments, which were highly rated in last year's edition of the survey.

"We practically do not finance new real estate projects."

Bank representative, Hungary

In respect to maximum loan size, Slovenian banks reported a slight increase, Hungarian and Baltic banks indicated moderate decrease, whilst in other countries no significant change was reported.

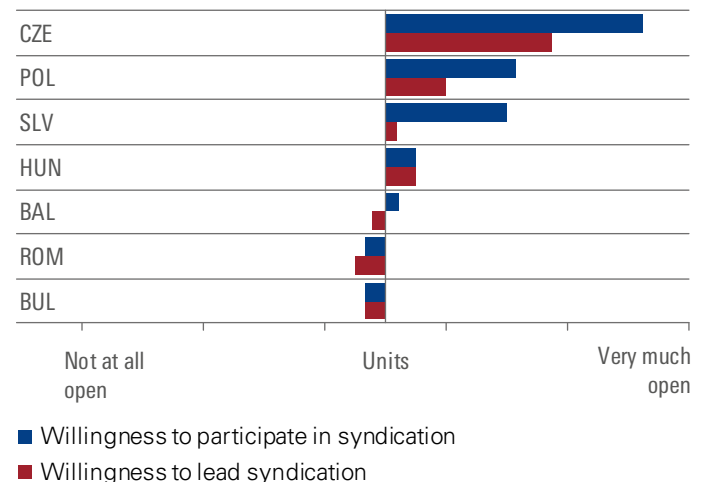
Change in limit of loan size compared to three years ago



Source: KPMG in CEE Property Lending Barometer 2012

Banks were also asked if they were open to participation in syndication loans for real estate projects. Answers reveal that in the Czech Republic, and to a lesser extent in Poland and in Slovenia, banks are quite open to participation, whilst in the rest of the countries they are generally neutral about the opportunity.

Banks' willingness to participate in and/or to lead syndication



Source: KPMG in CEE Property Lending Barometer 2012

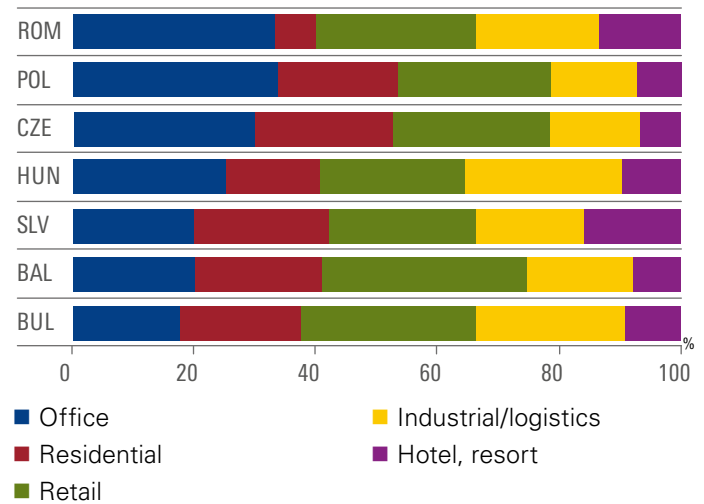
There is a general tendency that banks are significantly less open to lead syndication, even in the three most willing countries. The Czech Republic, again, is the most positive regarding the maximum participation rate. Half of the respondents were open to taking more than 50% of the total loan value. In Poland, however, respondents were only willing to take 50% or less.

Asset Class Preferences and Interest Premium

Further to the analysis of the general openness to lending, banks were queried about their preferred asset class in each country. Their responses show that financing institutions have not indicated any clear preferences in terms of their preferred sectors. In Romania and Poland office properties are most preferred, whilst in other countries there is no clear preference of any one sector. However, the hotel segment clearly remains the least preferred target, similarly to the last two years.

In addition to sector preferences, participants were asked to give a range of the loan interest premium they would apply on a 3-month Euribor basis, if a developer or investor of

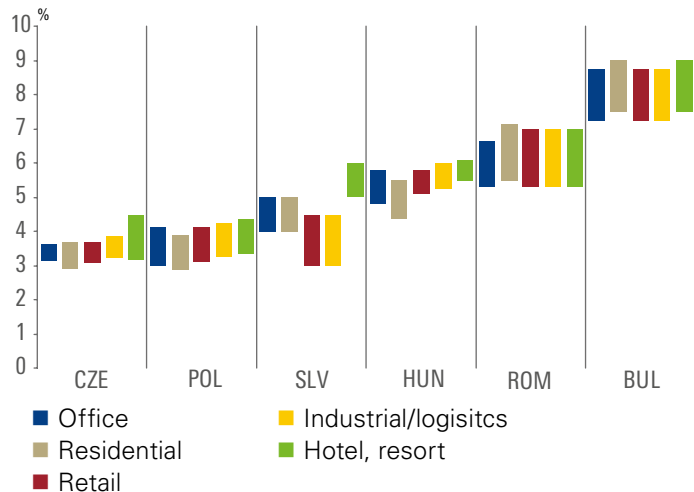
Banks' sector preferences in providing development financing by asset class



Note: The longer the coloured bar, the more preferred the asset class is for the banks. Source: KPMG in CEE Property Lending Barometer 2012

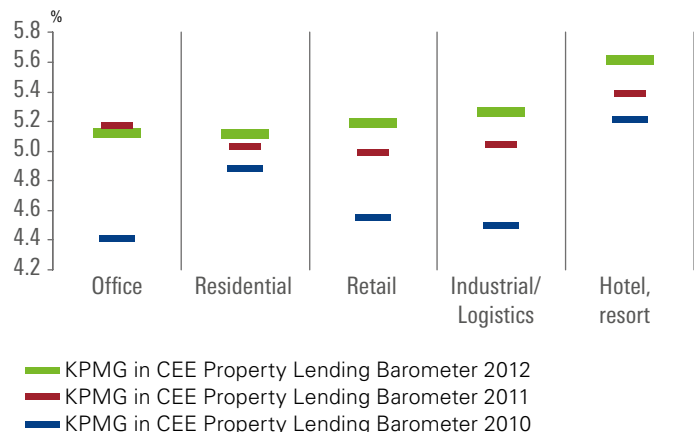
New development properties

Loan interest premium applied by banks for highly rated real estate development projects in selected countries



Source: KPMG in CEE Property Lending Barometer 2012

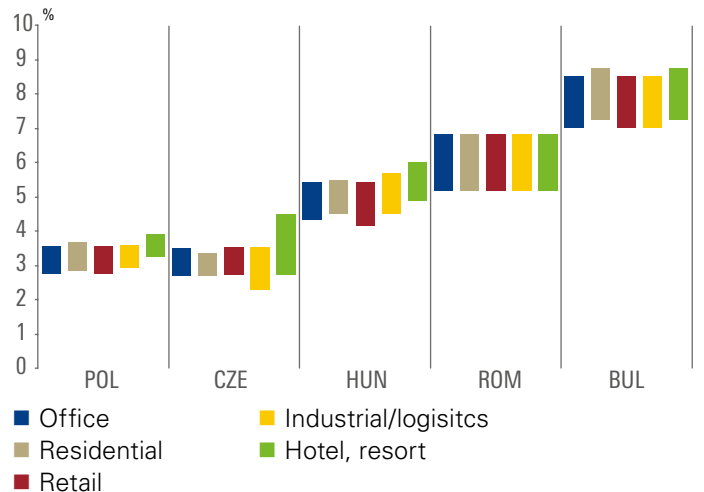
Regional averages



Note: Due to the low response rate, Slovenia is not included in this comparison. Source: KPMG in CEE Property Lending Barometer 2012

Income-generating properties

Loan interest premium applied by banks for highly rated income-generating real estate projects in selected countries



Source: KPMG in CEE Property Lending Barometer 2012

Regional averages



Note: Due to the low response rate, the Baltic countries and Slovenia are not included in this comparison. Source: KPMG in CEE Property Lending Barometer 2012

outstanding reputation with a solid business plan approached them. Similarly to last year, no meaningful average figures for the region were apparent, as premiums vary significantly across countries.

For new development properties, the lowest loan interest premiums are in the Czech Republic and Poland, which denotes their lower risk profiles and perhaps more competition from other banks to finance highly rated real estate projects. Meanwhile, the highest premiums have been reported in Bulgaria.

At the regional level, no major differences are visible in the premiums applied by banks across the sectors, with the exception of the hotel sector, where the premium is slightly higher at close to 5.6%. From a dynamic perspective however, premiums have increased over the last two years across all sectors.

Banks were also asked about the loan interest premium that they would apply on a 3-month Euribor basis for loans on high quality income-generating properties. Premiums also vary greatly across countries, with Poland and the Czech Republic offering the lowest premiums. However, there are no major differences across sectors, with the hotel sector having slightly higher premiums which are close to 5.14%.

On average, premiums are higher for income-generating properties compared to last year. The hotel sector still has the highest premiums and the largest variance in responses.

The variance in premiums may partly be explained by varying country risks, as reflected by credit default swap (CDS) values. In general, those countries perceived as high risk command the highest loan interest premiums.

Average CDS premium in the period May-July 2012, in selected countries (basis points)			
Country		Country	
USA	33	Russia	222
Switzerland	62	Lithuania	263
United Kingdom	69	Latvia	279
Australia	74	Bulgaria	324
Germany	92	Slovenia	386
Netherlands	112	Romania	415
Estonia	118	Italy	504
Czech Republic	130	Hungary	529
Austria	169	Spain	555
France	191	Ireland	619
Poland	220	Portugal	1006

Note: Average CDS rates over the period when the interviews were conducted (between 1 May 2012 and 31 July 2012.)

Source: Thomson Reuters (average of 18 market maker spreads, 5Y senior CDS, end of day composite prices, USD)

Criteria for financing

Having seen how open banks are to financing properties, and their sector preferences, the following section reviews the criteria considered for selecting projects to finance.

In terms of inputs to the decision making process, participating bank representatives stated that a strong business model and a high quality of assets were the most important considerations, together with the level of equity, additional collateral and the reputation of the developer or investors. The top criteria have not changed since last year.

Most important criteria when considering real estate financing	
Strong business model/Quality of the asset	● ● ● ● ●
Level of owner’s equity	● ● ● ● ●
Reputation and references of the developer/operator	● ● ● ●
Financial background of the developer	● ● ● ●
Preletting/pre-sale level	● ● ● ●
How well the project is planned, status of permitting process	● ● ●
Size of the requested loan	● ●
Existence of an independent feasibility study/valuation	●

Source: KPMG in CEE Property Lending Barometer 2012



“Banks generally do not want a large concentration of risk with one client.”

Bank representative, Poland

“Office lending is considered the safest form of lending as the demand currently exceeds the supply.”

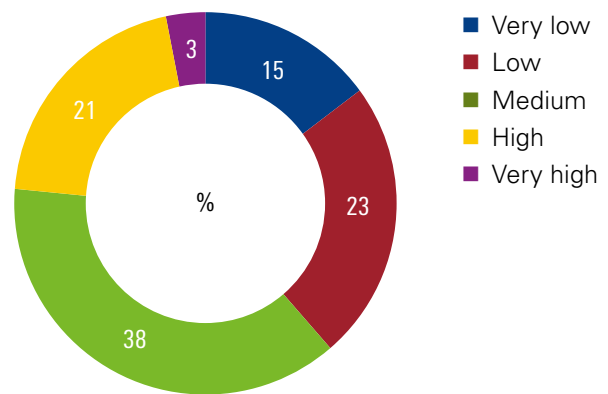
Bank representative, Poland

Independent valuation is still important, as more than half of the participating banks continue to report medium to very high reliance on valuations provided by external service providers. However, it is interesting to observe that more than 40% of surveyed banks have either low or very low reliance on independent valuations.

Banks were asked to spell out their technical criteria for financing. When questioned about loan-to-cost ratios, the responses differed greatly across countries. Similarly to the prior year, new developments in the office, residential, retail and industrial/logistics sectors have an overall maximum loan-to-cost ratio of 0.6-0.7 (i.e. reflecting a capital structure of 60-70% debt and 30%-40% equity). Once again, due to the perceived higher risk, the hotel sector requires more equity.

The ratios for the hotel sector decreased slightly compared to 2011, reflecting the overall investment sentiment in the sector. In H1 2012, Jones Lang LaSalle Hotels announced that hotel investment volumes in the EMEA region had reached EUR 3.7 billion, a 12% decrease compared to the same period last year.

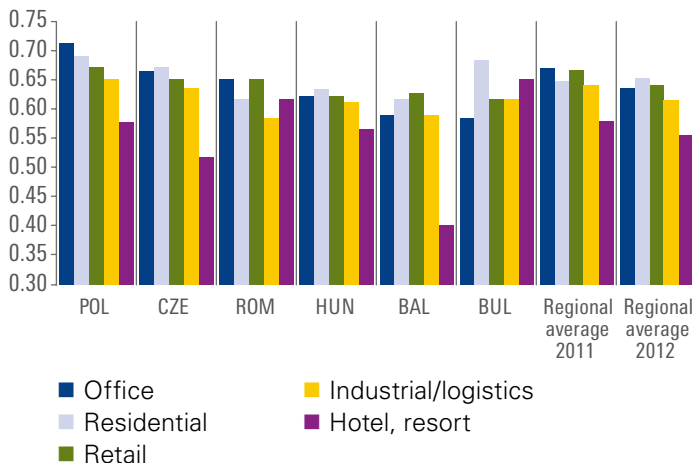
Banks' reliance on valuations provided by external service providers



Source: KPMG in CEE Property Lending Barometer 2012

New development properties

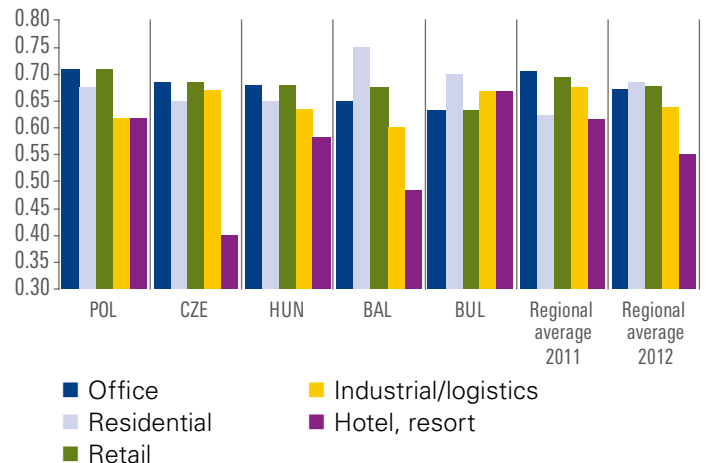
Loan-to-cost (LTC) ratio expectations for financing highly rated real estate development projects in the next 12-18 months



Note: Due to the low number of answers, Slovenia is not included in this comparison
Source: KPMG in CEE Property Lending Barometer 2012

Income-generating properties

Loan-to-value (LTV) ratio expectations for financing highly rated income-generating real estate projects in the next 12-18 months



Note: Due to the low number of answers, Slovenia is not included in this comparison
Source: KPMG in CEE Property Lending Barometer 2012

For income-generating properties, the office, residential, retail and industrial/logistics sectors have an overall maximum loan-to-value ratio of 0.6-0.7 (i.e. reflecting a capital structure of 60-70% debt and 30-40% equity). With the exception of Bulgaria, the ratios for hotel properties are slightly lower, close to 0.55 on average, with much greater variance across countries.

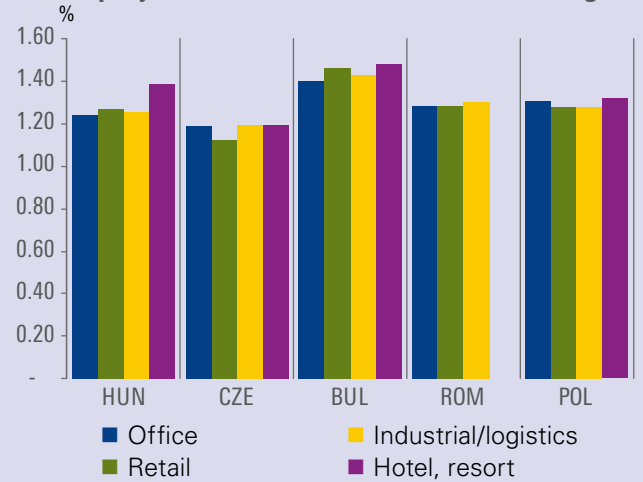
On average the sector loan-to-value ratios are only slightly lower than last year.



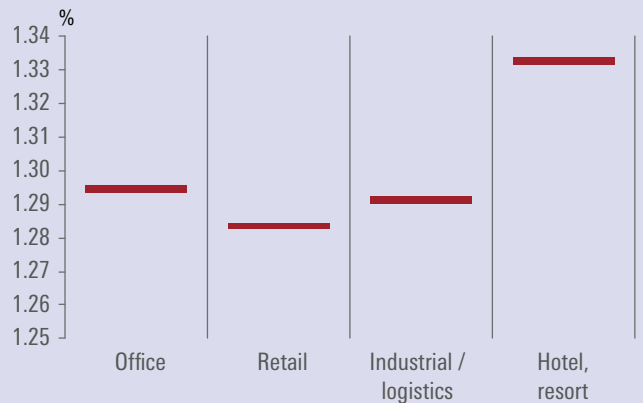
Banks are still demanding high pre-let and presale ratios. The expected ratios vary greatly across countries and sectors. Bulgaria has the highest ratios on average, closely followed by Hungary.

The pre-let ratios for the office and retail sectors are similar, being in the range of 45-65%. In general, most industrial and logistic projects are built to suit specific tenant requirements.

Debt service coverage ratio expectations for financing highly rated income-generating real estate projects for selected countries in the region



Regional averages



The debt service coverage ratios expected for income-generating projects initiated by investors with an excellent reputation and a sound business plan have also been examined.

In almost all countries, the hotel sector ratios tend to be higher than for any other asset class, exceeding 1.3 on average.

Conclusion

As a conclusion to our report, KPMG's Property Financing Sentiment Index illustrates how positively banks approach the financing of real estate projects in each country covered by this survey.

As in previous years, the index has been calculated using responses to the following 10 issues:

- An increase or decrease in focus on real estate financing within the bank's lending activities compared to one year ago;
- Proportion of fully compliant, minor impaired and seriously impaired real estate loans per country;
- Proportion of impaired loans perceived as being able to be managed successfully through restructuring;
- Expected change (increase or decrease) in size of real estate loan portfolios in the next 12–18 months (measured by two questions);
- Openness of banks to finance new development projects;
- Openness of banks to finance income-generating properties;
- Loan interest premium applied by banks for quality real estate projects;³
- Loan-to-cost ratio expected by banks for quality real estate projects³ in the next 12–18 months;
- Pre-let ratio applied by banks for quality real estate projects³ in the next 12–18 months; and
- Debt service coverage ratio applied by banks for income-generating properties.

Based on the ranking of the surveyed countries for each one of the 10 issues assessed, the following rankings were calculated for the last three years.

Property Financing Sentiment Index			
Overall ranking in:	2010	2011	2012
1	Poland	Czech Republic	Czech Republic
2	Czech Republic	Poland	Poland
3	Hungary	Romania	Bulgaria
4	Bulgaria	Hungary	Romania
5	The Baltics	Bulgaria	Hungary
6	Romania	Slovenia	Slovenia
7		The Baltics	The Baltics

Note: Slovenia was not included in the 2010 survey.

Poland and the Czech Republic are consistently strong performers in terms of their index ranking over the last three years and significantly outrank the other countries. The Baltics and Hungary showed gradually worsening results, whilst Bulgaria and Romania do not seem to be able to hold a stable position over the years.

As the macroeconomic conditions in most of these countries do not seem to be improving, the real estate sector is showing no signs of returning to the pre-crisis years' performance. In almost all countries, the importance of real estate financing for banks decreased over the last three years. Banks are consistently less and less open to financing new real estate projects, whose risk is also reflected by gradually increased loan interest premiums.

Overall, the results of our survey show that while there is still financing available for high quality real estate projects, the appetite for finance is deteriorating, potentially signalling the start of another downturn in the industry.

³ Quality projects have been defined in our survey as follows: a project initiated by a developer/investor with an outstanding reputation and a solid business plan.

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