Q2 2023 | Czech Republic

Industrial Market Overview

Industrial market overview

The Czech industrial market added 269,100 sqm of industrial space in H1 2023, resulting in the total stock reaching almost 11.3 million sqm. This is a growth of over 11% y/y. Facing more adverse market conditions, higher interest rates, stricter financing, a slowdown in the economy, a consumer confidence slump and ups and downs in industrial production, the Czech industrial space, somewhat surprisingly, still appears to have some aces up its sleeves.

The past 5 years in terms of market growth

The real story to highlight about the most recent developments in the Czech industrial market is the market growth and maturity. The developments of the past couple of years explain the current trajectory of the market. As mentioned above, the existing market was 11.3 million sqm at the end of H1 2023. Since H1 2018, that is a growth of nearly 3.5 million sqm in the past 5 years. Nearly 2 million sqm were added to the market in the past two years alone, which illustrates how significantly developments in the market took off after the Covid-19 pandemic sparked interest in industrial as an asset class more broadly among investors. Rental increases were a supporting factor in this development, as prime rents increased by 72% compared to 5 years ago and 50% since 2021, making the market undeniably attractive in terms of rental growth.

Still riding this wave, almost 1.5 million sqm of new modern industrial space is currently under construction and due to be delivered to the market within the next 6-18 months. And because of the flexibility of construction in industrial and the amount of pre-leased space, this number will likely stay the same or increase.

Stock (sqm milion)

11.23

Y/Y: +11%

Gross demand (sqm)

597,000

H1 2023: 941,400

Supply (sqm)

269,100

H1 2023: 487,000

Vacancy Rate

1.71%

Y/Y: +43 bps

Prime Rent

€7.50 – 7.80

Average rent regions:
€5.75 - 6.50

Under Construction (sqm)

1,433,500

Y/Y: +7%

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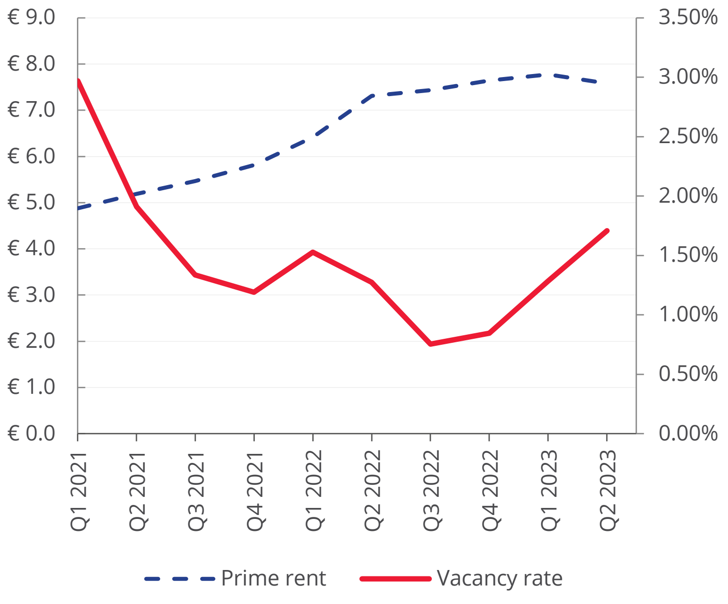
The busiest region in terms of construction used to be the capital city and surroundings, where the market has now reached what, compared to the previous 5 years, is a major decrease in construction activity. This is however a local specification of the subregion, as land is very scarce and permits harder to obtain there. Otherwise, construction booms in all other regions, even as demand for space is not as high in 2023. 26% of all construction is underway in the Karlovy Vary region, 13% in the Pilsen region and 12% each in the South Moravia, Usti nad Labem and Moravia-Silesia regions.

Rising vacancy – a healthy trend

Vacancy grew for the third consecutive quarter, now at 1.71% and constituting an increasing trend. This development is not surprising, the market feeling was that it could happen much sooner. We also have to highlight that <2% vacancy rates (and even lower vacancy rates in the large cities) is still quite low, when compared to other European markets. The current higher vacancy rates seem a natural result of the developments in the market and the economy. A healthy level of vacancy is around 4 – 5%. The last time the Czech market was at these levels was in 2019 and 2020 when vacancy started to decrease from around 4.5% – and the market still has a long way to go to get there again. The current increase can, in part, be caused by economic uncertainty affecting tenants and already existing agreements. However, we see the main driver of the increased vacancy in increased speculative construction activity among developers and the lower activity of tenants in pre-leasing and expanding their space into freshly constructed buildings. And yet again, it is not a bad thing, as the market ran on extremely low available space over the past two years. It lends the market some breathing room and tenants more options to consider, as well as larger spaces on offer.

Vacancy rate, prime rent
(%, € / sqm / month)



Sources:
Industrial Research Forum, Colliers

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TOP 3 Transactions of Q2 2023

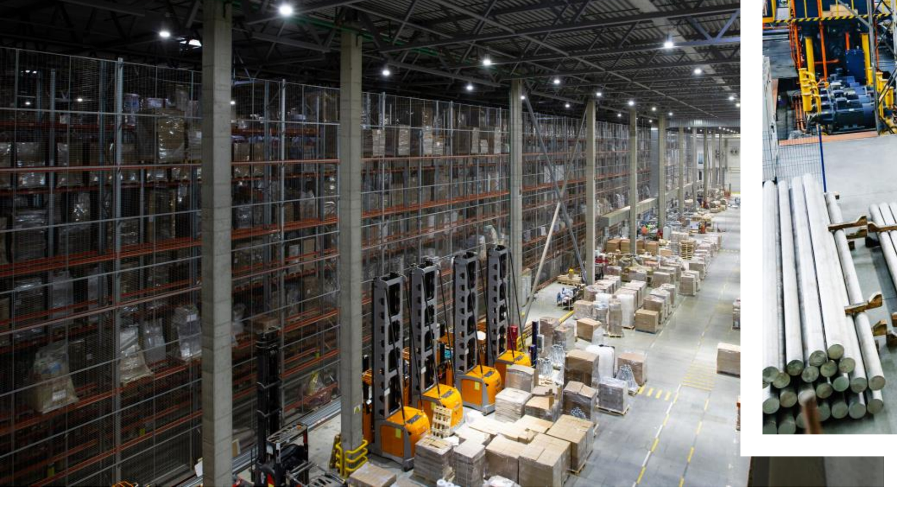
Tenant	Property	Size (sqm)	Transaction
Undisclosed	Prologis Park Prague-Jirny	136,900	Renegotiation
Undisclosed	Panattoni Park Ostrov - North	57,200	Pre-lease
Undisclosed	CTPark Bor	53,300	Renegotiation

Source: Industrial Research Forum, Colliers

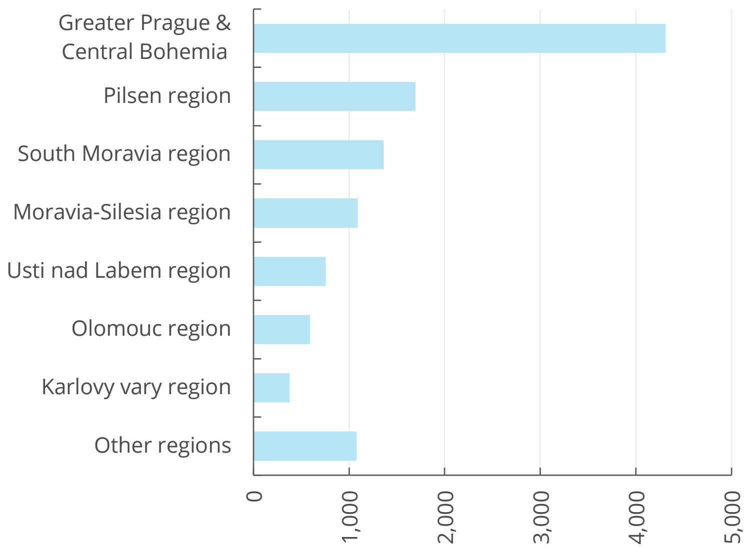
Trends in take-up: renegotiations and producers

Demand was the success story of the quarter, with 597,000 sqm of gross take-up leased and renegotiated in the market. This is almost a third more compared to the 5-year average and somewhat makes up for the past two slow quarters. Net take-up represented 46% of total take-up. After two years of net take-up dominating over 60% of total take-up, this figure is more subdued, and it is unchanged from the trend for net take-up in the previous quarters. The outlook for new leases, pre-leases and expansions has not changed. The increase in total demand was driven entirely by renegotiations. As we discussed at length in previous reporting, the specific market conditions in the Czech industrial space in the past year or so have negatively influenced the length of renegotiation processes. It looks like (at least some of) these have finally caught up and flooded the market with completed deals. One deal, in particular, stood out this quarter, the largest deal overall, an undisclosed logistics tenant in Prologis Park Prague-Jirny, who renegotiated 136,900 sqm of space.

In terms of sectors, net take-up was dominated by production tenants, as was the case in the past three quarters, taking over 60% of all net take-up, followed by logistics tenants with 23%. Renegotiations were dominated by logistics (largely because of the largest deal of the quarter), however, even in renegotiations, producers were the second most important sector. Overall, in commercial leasing of industrial space, producers are the most prominent tenants in the Czech Republic, especially owing to the strong role of automotive in the country (as may be opposed to other CEE markets – see our Colliers report "ExCEEding Borders Industrial 2023: Manufacturing and Warehousing sector in CEE-12" for more information). When the market is slower, producers, (and esp. automotive producers) are the backbone of the local demand. This may change if the economy turns even more sour and resources of producers dry up. It may also be positively or negatively affected by any changes of the automotive industry, and its potential transformation. As of now however, the role of producers locally is unparalleled.

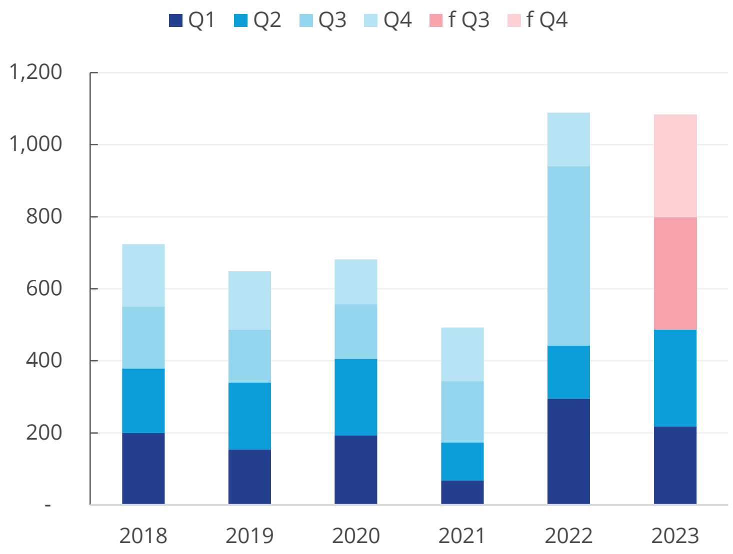


Industrial stock in regions
(sqm thousands)



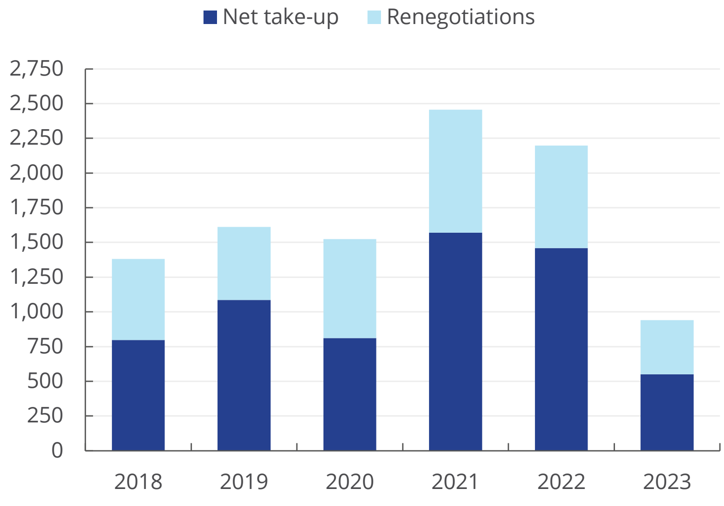
Sources:
Industrial Research Forum, Colliers

Annual supply & forecast
(sqm thousands)



Sources:
Industrial Research Forum, Colliers

Annual take-up
(sqm thousands)



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Forecast

Following the monumental growth of the past two years, prime rents in the market have slightly decreased, as we forecasted in the past report. The current prime rent in Prague is €7.50 - €7.80 / sqm / month. This development shows a movement towards the stabilisation of rents in the market after the high growth period. We now expect this development to continue (albeit without more dramatic decreases) and for prime rents in Prague to stabilise for the foreseeable future at around €7.00 - €7.50 / sqm/month. The regions outside of Prague constitute a different story and some room for rental growth can still be found there, although if the market situation worsened, we would more likely expect the rate to stay stable. Rents for mezzanine office space stand between €9.50-12.50 sqm/month. Service charges are typically around €0.75–1.00 sqm/month.

As for other forecasts for the rest of the year, it is likely that the industrial market will not reach 12 million sqm by the end of the year, although it will very likely cross that boundary in H1 2024. In the first half of 2023, developers were increasing speculative construction (in Q2, the share of speculative construction increased by 4% to 38%). That could still shake up the current situation, but the increasing tempo of speculative construction will likely not last if adverse economic conditions persist in the economy. It is always good to keep in mind that industrial is much more flexible than other real estate assets. It is quick to respond to both favourable and adverse market conditions and this will be the major driver affecting the final results for the sector at year end.

Macroeconomic overview

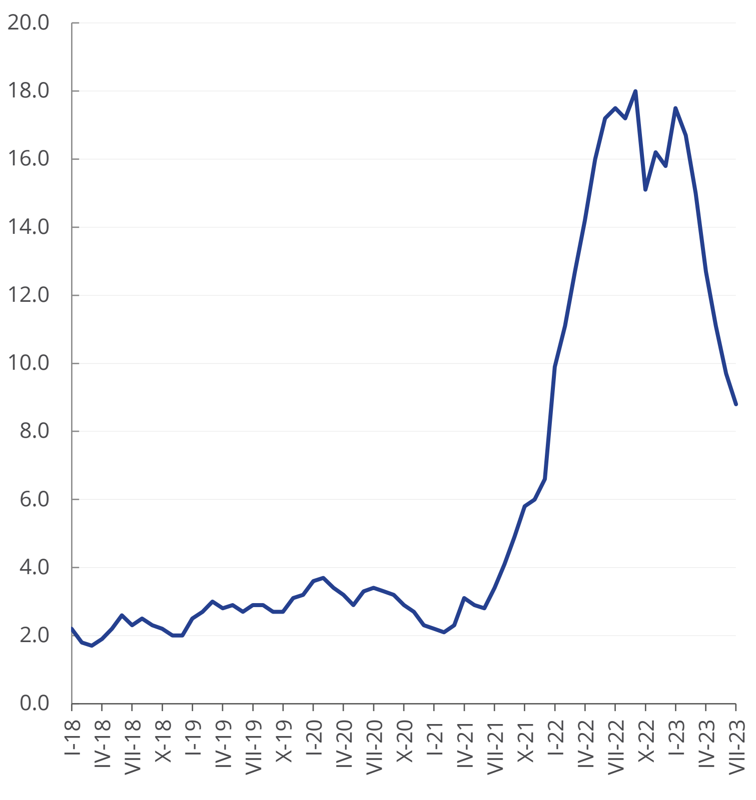
The Czech economy continued a similar weak growth trajectory as in Q1, despite better-than-expected Q2 results. Consumer spending remains in a depressed state and the stagnant growth is mirrored in the GDP growth projections. On the other hand, the inflation rate is finally easing. Even as inflation eases though, consumer confidence remains low, pointing towards a continued slow growth outlook and possibly even a recession in the Czech economy. Furthermore, external demand in the economy is significantly weakened across the markets and looks to slow further, depressing local growth. Industrial production and retail sales have been stagnant, as demand weakened. Because external demand is waning, this situation will likely worsen throughout the rest of the year.

The growth rate for the Czech Republic in 2023 is forecasted at -0.4% and for 2024 it is currently at 0.9%. Slow growth has been a prominent feature of the economy in the entirety of the first half of this year. Consumer sentiment and consumer spending have been on low levels all throughout the first half of the year. The two main factors behind this development is the significant drop in real incomes (by 6.7% y/y) and continued tight monetary policy that is squeezing lenders with increasing interest on consumer debt. Real incomes have yet failed to catch up with inflation and rates still remain high. There could be better times ahead, as inflationary pressures ease, but the fallout of H1 will be felt for the remainder of the year. Other sectors of the economy, such as retail sales and industrial production still record some, albeit limited growth and according to Oxford Economics analysts, will dry up in the second half of the year, as external demand wanes.

The positive news is that inflation has fallen below 10%, for the first time since 2021, now standing at 9.7% y/y*. The high year-on-year inflation will be easing throughout the year and will be back to the 2% target rate by this time next year. The Czech National Bank kept policy rates at 7% and this will likely stay at the same course until September. While helping to keep inflation down, consumer spending and confidence will likely suffer further. The labour market maintains its stable low rates of unemployment, which reached 3.2% at the end of Q2 2023.

Note:
* - in July the inflation was 8,8 %

Inflation rate
(Y/Y, %, 2018 –2023)



Source: Czech Statistical Office

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