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APRIL (SPECIAL) 2012: The Hungarian Real Estate Market

If anyone wonders what a real estate market looks like after a breakdown of the euro or the expulsion of Greece or other members – they can't do much better than to look at Hungary. Hungary is an empirical example of an open economy whose financial services, as a sector, have been obliterated. Financing is practically non-existent, and political moves only exacerbate the situation.

Hungary is currently an unleveraged country. Finance from banks is not readily available, and where it is it costs something in the region of 700 basis points over EURIBOR. The insurance industry cannot step into the breach as it is in disarray with one pillar of the system effectively nationalised by the state. This means that the economy relies on equity to do deals as a result their number is low and their nature is erratic.

Last year there was a depreciation of the national currency, the forint, of 15%. This has not helped the economy as much as it should have because so many residential mortgages were denominated in Swiss francs. The Hungarian National Bank deserves much criticism to allow such an inherent risk to be built up in their banking system. But it was not only in Hungary but other countries of Central and Eastern Europe that have been left with a headache as a result of this regulatory/risk oversight.

It means that even with a nominal devaluation the situation has not improved for real estate owners. Real estate owners are left with a double hit of the depreciation of the value of their asset (in forints) with an increase in the value of their associated liabilities (in Swiss francs), as the Swiss franc has appreciated against all others as investors flight to the traditional European safe haven.

The Hungarian government is keen to hit the overhang of developments in commercial real estate and has, for example, passed a law to stop speculative shopping centre developments. However, like so many political initiatives this tackles the consequence not the cause of the problem. Although variously described as right wing or nationalist, the *Fidesz* party does not understand that the best way to help the country is through extracting the government from as many functions as possible. This accomplishes a double goal of increasing efficiency as well as eliminating cronyism in government. As a result the best way to deal with the wrongs of the past is to withdraw the drug of government from the economy. This is a simple principle yet a hard one to implement at the same time as being electable. The fate of Malev, Hungary's national airline carrier, which went bankrupt two months ago is an apt metaphor for misplaced pride in old industries and inefficiencies that cannot be supported indefinitely. Ryanair took over all operations of the defunct national airline overnight, and will turn a profit on assets that were not maximised during their ownership by Malev.

In real estate, the shrinkage of financing opportunities will emphasise fundamentals. Underlying performance cannot be hidden by financing arrangements. Occupying rent cannot be 'smoothed' by bringing forward and delaying income. Occupier's covenants will actually be tested, and assessment of management and their efficiency will be imperative to distinguish between lazy and the disciplined investors. In this way, a deleveraged country may not actually be such a bad thing.

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