

The Real Estate Market in Romania – A Post COVID Analysis

Alina Elena Cerchia (Ionașcu)

Alexandra Zaif (Popa)

Daniel Lipară

“Ovidius” University Constanta, Faculty of Economic Sciences, Romania

alina_cerchia@yahoo.com

andra_zaiif@yahoo.com

daniel.lipara@yahoo.com

Abstract

The aim of this article is to analyze the direct investment opportunities in real estate in Romania and the future trends and forecasts for the real-estate market, focusing on the residential segment. The Romanian residential market changed after the 2009 economic crisis when the prices dropped down dramatically. Nowadays, the properties became slightly overpriced and also the value of yields from the rentals are going up.

The paper presents an analysis of the value of the yield from rent fee in Romania and the methods for calculating the yield, the factors that have a direct influence over the yield and the main reasons why the yield from rent is fluctuating.

Taking into account the current situation, the commercial real estate market is analyzed before pandemic but also post - pandemic consequences are emphasized.

We conclude with the future modern trends are how the market can adapt to “new” by using the innovation in the real estate market for the economic growth.

Key words: real estate, yield, rent, properties

J.E.L. classification: R30

1. Introduction

There has been an intense debate over economic growth and variations from the original model by Robert Solow in 1950s, model recognizing the ‘technological change’ as the main growth attribute (87.5%) versus increased use of capital (12.5%), and the need to clarify the model in today’s terms. The modern growth theory places innovation as the center of economic growth and recognizes innovation as the mechanism pushing forward the autonomous growth factor (McDonald & McMillen, 2011).

Similar to the principles of above growth model, Romania has been placed as one of the global leaders with high growth potential according to 2021 Annual Report released by Colliers. Although, Romania has some inefficiencies “in terms of rule of law, transport infrastructure, healthcare, efficacy of public administration or stability in general, with regards to laws and policies, should any improvements take place on these fronts, the growth potential that would be unlocked would be significant”, Colliers consultants predict.

2. Theoretical background. The value of yield from rent fee

On market value, a very popular rule has the price/winnings ratio as a starting point, which measures how big the net incomes depending on the price on the stock market are. The same mechanism is applied also in real estate, price/annual rent ratio (yield) being a simple mathematical calculation which can be made by anyone that knows how to use a calculator (Căpraru et al., 201, p. 45).

In Romania, in approximate 99% of the cases the one that buys a real estate moves in that property, that's why the price/rent is irrelevant. Although, many reasons exist for which people should pay attention to this „assessment parameter”. In case the level of yield rent is high, that means the interests paid when buying a house are less than the cost of rental. In other words, potential customers will pay less if they opt for a loan from the bank to buy the property, rather than remaining a tenant. Also, entrepreneurs will find the idea to buy property for rent more attractive. Both factors make an upward tendency over real estate prices.

On the other hand, a price/rent ratio translates to a higher rent yield. In this case, the idea of living on a rent is not so bad, the costs of buying a house being much bigger with the rent alternative. Countries with high rent fees of the nominal interest and the ones with low mortgage market, like Romania, will have indices price/rent ratio relatively low (Anghel et al, 2013, p. 76).

The Romanian residential market moved from de list of countries with underestimated properties to the one with slightly overestimated prices, the value of yields from the rentals going from 3,3% to 5,5%. Although, for the market to reach a normal level considered by the international analysts, the value of the yields should reach a minimum of 7%. The index of the yield value from the rent is just one of the four base rules used worldwide to figure out the right price in real-estate. In order to correctly evaluate property, it is useful both the replacement price, index of accessibility and the comparison price (Anghel et al, 2013, p. 36).

Real estate in Romania is one of the most recommended investments. In the western countries, it is rated in the middle somewhere between the high investments risk and safe investments risk, being neither on the deposits and state titles area (security zone, minimum risk), neither stock zone, corporate bonds etc. (high risk zone, with big winnings).

Romania is a different country, in which real estate have a big share in the average wealth of every person. A recent study made by Credit Suisse, the famous Swiss bank, shows that the average non-financial assets in the average wealth of Romanian people are with 84% over the European average, a big share being made by real estate. Another indicator, Home Ownership Rate, show that 96% of the property are lived by the owners while the European average is 66%. This 96% brings the country to the first place in Europe on the percentage of property lived by the actual owners, and second place in the world.

They all lead to a simple conclusion. Romanians like real estate investments. They like them so much that the first investment in everybody's mind, after the classic „Put the money in the bank and live on the interest” is „Buy and apartment and rent it”. Not investing the money, keeping the cash or making deposits, are likely to devalue because of the inflation, which is growing higher.

The fact that real estate for renting is the first option for investing in the mind of Romanian people take them to the safe zone, low risk security, because the potential request for this kind of investments in very big. Moreover, the request for real estate is much bigger on a world-wide level, where there are studies that 90% from the billionaires from the planet in the last 200 years made or strengthened their fortune investing in real estate.

3. Research methodology

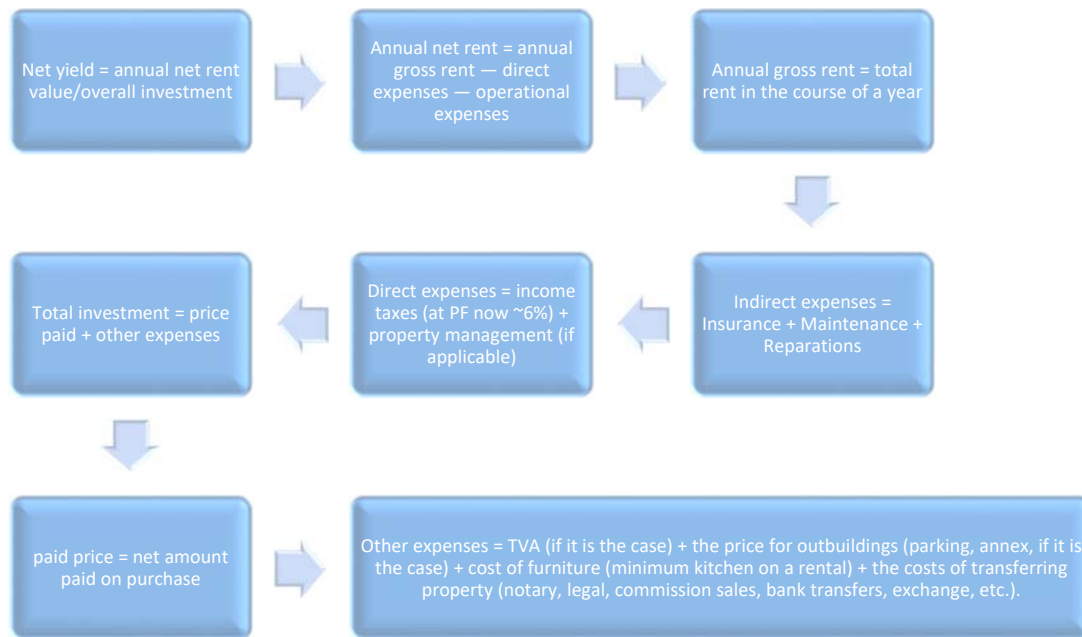
The study was conducted based on real estate literature review. The main sources for analysis are the reports for the residential market provided by the main research companies, national and international books and also the international data bases. We proposed a mathematical model for calculating the yield for real estate properties taking into account the rent values. The post - Covid analysis and consequences of the pandemic on the real estate market were resumed after reviewing and observing the last three years reports for the residential market in Romania and also the specialized literature regarding the phenomenon.

This paper concludes with an analysis of the factors that influence the real estate market tenancies' purchase decision, focusing on the residential segment study.

4. YIELD calculation methods

First of all, it has to be made a difference between gross yield and net yield. Gross yield is the one before the direct and operational costs, while net yield is the one that remains at the end of the year (figure no.1).

Figure no. 1: Yield Formula



Source: processed by the author

Regarding the rents yields requested by categories of apartments, Bucharest is naturally at the forefront big cities, with average values of 250 euros per month for studios, 400 euros per month for two rooms and 600 euros per month for three, respectively rooms. The country's capital city is closely followed by Cluj-Napoca, where the owners request 250 euros per month for a single-room home, 370 euros per month for one bedroom apartment and 450 euros per month, respectively for a two bedrooms apartment. Interestingly, Timisoara continues to occupy the last place in the ranking of rents in big cities, with 200 euros a month for a studio, 300 euros per month for two rooms and 350, respectively euros per month for three rooms (Table no.1)

Table no. 1 Value of rents for the main cities in Romania

City	Studio	One bedroom	Two bedrooms
București	250	400	600
Cluj-Napoca	250	370	450
Brașov	250	350	420
Constanța	200	320	450
Iași	230	310	380
Timișoara	200	300	350

Source: imobiliare.ro, processed data by Analize imobiliare, 2021

5. Commercial real estate market, before the epidemic

Before de COVID-19 pandemic, commercial real estate had a better position, in comparison with the economic growth in 2008. Even though the prices for the residential real estate since 2011 are, on average, by 7.3% below the long-run average, in 2015 the prices surpass the average sustainable rate of economic growth, as the real estate market began to recover (Ionașcu, 2021, p. 100). The specialist that participated at a global study made by Deloitte in the summer of 2019 were expecting an investment growth in real estate for 2020. But, from the second week of March, when the epidemic of COVID-19 was declared pandemic, financial markets dropped, and the commercial real estate was immediately affected, especially as a decision of the authorities to close numerous activities.

The same thing happened in the Romanian real estate, where closing the large commercial centers put pressure on the liquidities of the owners of the buildings and on the income of the tenants, and the measures that followed, such as postponing the payments of the rent, brought extra modifications in the commercial equilibrium between the two parts.

An estimation regarding the return to normal and in what it consists of is impossible to make, but it can be analyzed, based on the existing data, the challenges and perspectives in this area, directly affected by the restrictions, from the sudden change in the way the entire population manages activities and their life-style.

Every crisis assumes three stages: first is the period of reaction of response, in which it is tried to understand de implications and limitations of the immediate effects, then follows the period of recovery, in this period new business strategies develop and then comes the last period, the period of growth, in which, starting from the new strategies created, development opportunities appear. In the response phase from the beginning of the pandemic, the companies from the area of the commercial real estate focused on treating the liquidities problems on the short term, protecting the owned properties but also on maintaining the connection with the tenants and respecting de governmental directives. Naturally, follows the recovery phase, in which companies will evaluate their options for reopening spaces, will redesign price policies as well as the way they use resources efficiently.

6. Post - pandemic consequences

Generally speaking, a really good investment in real estate should start from an annual yield of minimum 6-7%, which would equate with an amortization period of 14-16 years. With the yield being higher and the recuperation period being smaller, it is much better, obviously- overly positive estimates should rise questions regarding risks in that investment.

The atypical crises from the COVID-19 affects in different ways the economic sectors, regarding the events that caused in the past, recession. Real estate field reacted, traditionally, with a delay of almost six months to the rest of the economy, but at this moment reacted a lot faster because of the extension, depth and lack of predictability for this crisis (Ionașcu, 2013, p.103).

Among the last century, external shocks, such as an epidemic or pandemic, followed by an economical slow down, have had an immediate impact or short term over the prices of the commercial real estate, but with a minimal influence over transactional activities, shows a Deloitte analysis that takes in regard the evolution of this area during major events from the past. Commercial real estate has recovered the loss caused by these events in different rhythms. After the punctual events a shorter recovery took place, but long-term events, such as 2008 recession have led to a slower recovery, of much more trimesters.

In the first place, players from the area need an efficient and structured plan to bring people in physical spaces after the elimination of the restrictions, such as offices, commercial spaces and hotels. It is clear that returning to the physical spaces does not mean return to normal. Therefore, companies need to keep in mind the new methods of human interaction and to adapt their spaces accordingly.

The usage of technology is important in every area in this period, and the real estate area is no exception. Therefore, a focus area is technology, for the employer (the required necessities for work from home, applications for the rotation of the employees etc.), as well as improving their activity and their customer's activity (for example: automatic solutions for the warehouses for online commerce). The technology comes with risks which determine companies to consolidate security measures and data confidentiality.

Property portfolio reevaluation to lower the risks on the long term and prudent manage of capital flux are meant to help players in the industry to pass much easier this crisis. For developers that have a wide ranged portfolio, it will much easier to navigate through this period. For example, owning logistic commercial spaces was a natural instrument in managing commercial risk. Other investors will try the diversification of their property portfolio.

To head more rapidly to the growth phase, the companies and people must understand the new normality: what elements will the new tenants cherish when they will choose their spaces in the future? Maybe contract flexibility, maybe more online facilities, maybe less owned spaces etc. Which will be the biggest challenge of the real estate market? Maybe the modified demand, maybe the increase in costs as a need to upgrade or maybe the aversion to risk of the investors, which will prefer more liquid investments.

Prices for apartments and houses will increase with 15% in the next period, real estate experts estimate. It is the effect of the growth of price for construction materials with approximately 20% since the beginning of 2021. The news concerns the buyers, which noticed an increase in prices even in 2020.

Regarding the real estate transactional activity, the year 2021 started in a positive note, despite the difficulties created by the COVID-19 pandemic. Therefore, the data published by the National Agency of Cadastral and Real estate publicity (ANCPI) and archived by Real Estate Analysis show that in the first trimester of the current year were sold almost 162000 properties national, an increase of 11,9% from the same period of the last year. To note is the fact that in individual unit segments took place an advance much more significant, almost 42,7% to a total of 40000 properties. „An important weight on transactions in residential real estate market is financed through credit. The index regarding access on mortgage real estate market emphasizes the fact that a typical household owns, according to the data from December 2020, approximate 71% from the necessary income for acquiring a location with 2 rooms. In Bucharest, from 2013, the accessibility index increased, that means the income of one family increased enough to afford to buy a home. Without financial aid from a bank, the necessary time to acquire a property with 2 rooms at a national level is of about 8,5 years (price to income), and regarding a property with 3 rooms it is of about 11 years (data from December 2020).” Simona Iftimie, Economist, Department of financial stability – National Bank of Romania.

In line with the overall tendency of the market, all eleven cities (with over 200000 people) constantly monitored by Real estate Analysis, registered, in the first trimester of 2021, had an increase in the medium price for an apartment. In contrast to the previous three months, when the growth ratio where all, with one exception, below the 2%, at the beginning of 2021 more regional centers succeeded in overcoming that percentage.

Despite maintaining the restrictive measures in times of COVID-19, local residential market maintained, in the first trimester from 2021, on an ascending path regarding prices of the properties. So, the most recent report realized by Real Estate Analysis, the platform launched and maintained by Imobiliare.ro, show that, in January-March, listing prices of residential Romanian property (apartments, and also houses) noticed a trimestral advance according to normal conditions in the market. „According to Real Estate Analysis, the medium price solicited by the salesman of apartments and houses increased with 2,2 % in the first trimester in 2021 to the previous trimester. The annual rate of the growth in prices slowed down because of the decrease in the demand and the increase of the current offer; this indicator was, in the indicated period, at 3% compared to 3,5% from the end of the last year. The annual average growth of 3% reflected differently on the two segments of the market: existent real estate price (old) registered a slight decrease, of 0,5%, meanwhile the new property prices increased with 6,8%”. Dorel Niță, Head of Data & Research, Imobiliare.ro

7. Conclusions

After the 2008 economic crisis ended, everybody was waiting for the prices to drop down. The prices, though, are not dropping. The market is increasing, if we are taking a look at the numbers. Official statistics show that there is an increase and that it will continue to exist, everything, automatically, if it will be sustained by the economy. Therefore, the Covid-19 pandemic, did not have a major negative impact over the real estate market so far.

The Covid-19 changed the behavior of the people and companies and the reconsidered the options regarding the real estate sector. One of the general tendencies produced by the necessity to spend more time in their own houses is the amplified need to enjoy the outdoors, once in a while. This is the reason for which the properties located in the more nature like, close to nature or that offer the possibility for a pleasant walk are, today, more appreciated. For the population of the bigger cities – like Bucharest, Cluj, Iasi, Timisoara, Constanta, Brasov, and not only, this trend means an increased interest for residential projects with low density, located, usually, in the quieter areas from the edge of the big cities.

In the present situation of the coronavirus epidemic, one of the predilections that can be identified on the real estate market in 2021 is represented by the need to feature the property with all the necessary things for working from home – starting with a good quality connection to the internet and a special featured space and continuing with all the equipment and technological solutions necessary in order to assure optimum working conditions. It is very likely that in the future, working from home and working from the office will be combined, these investments will continue, and with this trend, developers will provide spaces in which people that live in residential places to work and even have business meetings.

Regarding the rental market, the studies show that most of the tenancies want a series of facilities – parks, tendencies and playgrounds count today almost as much as the proximity of public transportation. Additional, if the proximity of a supermarket was always an important request, in the present moment almost half of the tenants consider the even the proximity of a pharmacy is in top of the preferences.

This research aimed to study the residential and commercial market in Romania before and after the Covid-19 pandemic started, considering the new behavior trends of properties demand and supply. Depending on the duration of the epidemic, this topic will remain open, as the real estate market will continue to suffer changes and further analyses can be made during the present situation, but also after the pandemic stops.

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