Spain's Office Prices May Decline to 2001 Levels (Update1)

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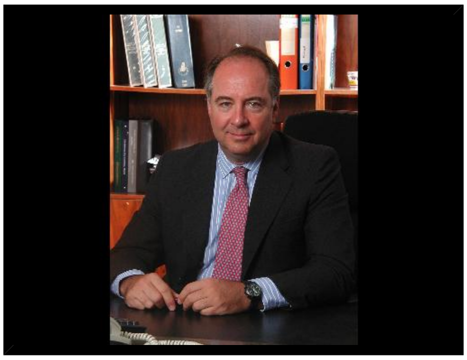
By Sharon Smyth



Oct. 13 (Bloomberg) -- It wasn't hard for Miguel Angel Zuniga to persuade his landlord to drop the rent for his printing company in northern Madrid by 20 percent.

More than a third of the buildings in the industrial park a 30-minute drive from the city center are empty. One close to Zuniga's burned down and the owners haven't rebuilt. Zuniga also knew he could get a third more space in the same complex for what he was paying.

"Three years ago when the business was set up, you had to fight tooth and nail to find premises; now you can pick and choose," said Zuniga, 46, manager of Grupo Imant, whose monthly rent for 1,000 square meters (10,764 square feet) of office and warehouse space fell to 3,600 euros ($5,319) from 4,500 euros.

Spain's commercial property market is suffering as the unemployment rate approaches the highest in at least 15 years. Business rents in city centers have dropped 22 percent in the past year, the most since 2002, according to Jones Lang LaSalle Inc. Average selling prices for all office buildings in Spain may fall 25 percent through the end of next year, bringing them back to 2001 levels, said RR de Acuna & Asociados, a property researcher in Madrid.

Office values in the country's central business districts have already fallen about 50 percent since the peak in 2007, according to Savills Plc in London, the largest publicly traded U.K. commercial real-estate adviser.

Zuniga's landlord, Daniel Estebaranz, didn't respond to telephone calls left at his Madrid office for comment.

Businesses Close

The supply of potential tenants is shrinking as more businesses fold. About 66,400 Spanish companies closed in 2008, and about 2,770 sought protection from creditors in the first half of 2009, up from 901 a year earlier, according to the National Statistics Institute.

"Commercial property prices are very much linked to the performance of the economy, and at the moment nobody knows when it's going to flourish again," said Pedro de Churruca, managing director for Spain at Jones Lang in Madrid.

Spain's property boom started after it adopted the euro in 1999 and interest rates plummeted to about 3 percent from as high as 15 percent. Real estate and construction accounted for as much as 20 percent of gross domestic product at the peak in 2007, according to KPMG.

Commercial real estate prices climbed 51 percent from 2000 to the end of 2007, research from Investment Property Databank Ltd. shows.

Office Space Jumps

Office space has expanded 38 percent in Madrid since 2000 to 11 million square meters, said Cushman & Wakefield Inc., the largest closely held commercial property broker. It jumped 41 percent in Barcelona. Spain now has 514 shopping malls, up from 300 in 2000, according to the

Spanish Association of Shopping Malls.

The global credit crisis led Spain's economy to contract for the first time in 15 years in the third quarter of 2008. The unemployment rate rose to 18.9 percent in August of this year, almost double the euro-region average, the European Union statistics office said. It will probably reach about 25 percent by the end of 2010, according to Fernando Rodriguez de Acuna, president of Acuna.

Some developers in Spain were trapped when the boom ended because they had already committed to projects that can take as long as five years to complete, said José Luis Suárez, professor of financial management at the IESE business school in Madrid.

"You have to take into consideration planning, getting permits and financing and actually constructing the buildings," he said.

Shops, Warehouses

Warehouses and shops in Spain will probably lose 31 percent and 20 percent of their value, respectively, by the end of 2010, according to Acuna.

Evidence of the country's decline can be found even on the upscale Calle Velazquez in central Madrid, where an antiques store, a bar, a gift shop and a home-decoration store have all closed. For Rent and For Sale signs are scattered on either side of the street.

Sara Perez-Frutos, managing director at Dracon Partners, an investment company on Calle Velazquez, said about half the 20 tenants in her building have left in the past three months. She can now get a parking space outside her office every day.

"You don't encounter a soul in the lift these days," said Perez-Frutos, 35.

Madrid's office vacancy rate was 8.4 percent as of June 30, the highest since 2005, according to Aguirre Newman, a Madrid- based property consultant.

New Supply

"The amount of stock will continue to rise above 10 percent as demand continues to fall and new supply continues to enter the market," analysts Javier Garcia-Mateo and Angel Estebaranz from Aguirre wrote in a July report.

The severity of the slump means Spain may be starting to represent good value to some investors, said Michael Haddock, director of research for Europe, Middle East and Africa at CB Richard Ellis Group Inc. in London.

Yields on the best properties have risen more than 2 percentage points since the middle of 2007 to between 6.75 percent and 7.5 percent, he said. That's about 50 percent more than the increase in yields on similar buildings across the EU since peak prices.

Signs of recovery may already be emerging, Haddock said. He cited the 235 million-euro sale of a Madrid shopping mall by Banco Santander SA's real estate fund in May, and Inmobiliaria Colonial SA's sale of another retail center in June for 126.5 million euros.

'Moment of Opportunity'

"We are at a moment of opportunity, where prime assets can be purchased at good prices before the competition between buyers increases," Rafael Merry del Val, general director of Savills's Spanish unit in Madrid, said during a presentation to reporters in September.

Analysts Nick Webb and Jacqueline Cheung at Goldman Sachs Group Inc. are less optimistic. They rate Metrovacesa SA, Spain's biggest real estate company by market value, as a "sell" and expect the stock to reach 12.8 euros. Metrovacesa now trades at 21 euros, after a 59 percent decline in the past year.

"Our greatest caution surrounds Spain and industrial rents," Webb and Cheung wrote in the report. "Spain will remain challenging for some time."

Ursula Guerra, a spokeswoman for Metrovacesa, didn't respond to requests for comment.

Shrinking Economy

Industrial production slid for a 16th month in August, down 13.1 percent from a year earlier. GDP shrank 4.2 percent in the second quarter, according to the National Statistics Institute. The Organization for Economic Cooperation and Development expects Spain's GDP to contract 0.9 percent in 2010 as consumer spending dwindles, making it the worst performer in the 30- nation group after Ireland and Hungary.

House prices in Spain fell 8.3 percent in September from a year earlier, Tasaciones Inmobiliarias SA, the country's biggest home valuer, said today.

Spain plans to raise the rate of value-added tax on goods and services to 18 percent from 16 percent in July to address a budget deficit slated to reach 9.5 percent of GDP this year. That could hurt real estate even more, de Churruca said.

"Increased taxes will reduce consumption that will in turn have a negative impact on commercial properties," he said. "I don't see adequate measures are being taken to reactivate the economy."

That's bad news for Zuniga's printing business. He's worried companies will scale back more on advertising and he'll get fewer contracts for less money as he cuts prices to fend off the competition. Sales in the industry are already down as much as 35 percent, he said.

"My old rent was set on the premise that Spain was booming and there was no sign of the economic crisis we are caught in now," he said. "Those times have long gone."

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Last Updated: October 13, 2009 10:57 EDT