CB RICHARD ELLIS

EMEA ViewPoint

www.cbre.eu/research

March 2011

CHALLENGES IN DISPOSING OF PUBLIC SECTOR REAL ESTATE

By Richard Holberton, Director, EMEA Research & Consulting

OVERVIEW

With many European governments still committed to aggressive deficit-reduction plans, the prospective sale of public sector real estate assets remains firmly on the political agenda. However, the most recent evidence indicates that success in executing sales has been limited. Public sector sales totalled around €1.1 billion in 2010, with over 75% of this in Sweden, Germany and the UK. There is wide variation in the quality of public sector assets, and hence their appeal to prospective investors. There are also political challenges in a number of countries that restrict the practical scope for large-scale disposals. Despite these challenges, we expect the commitment to disposal of publicly-owned assets to remain strong.

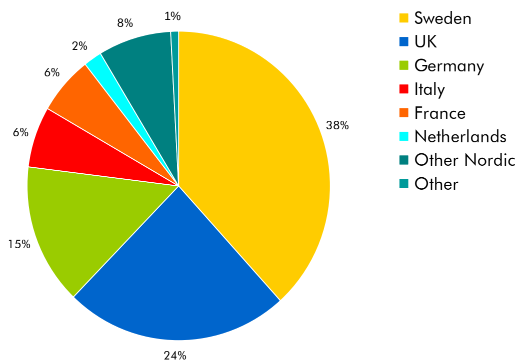
INTRODUCTION

While many governments around Europe are actively considering disposal of real estate assets as one element in their deficit-reduction plans, the latest evidence indicates that significant challenges remain in executing these programmes. In 2010, government property sales around Europe totalled only around €1.1 billion (predominantly in Sweden, Germany and the UK), which is significantly up on the previous year's figure but still only around 7.5% of all occupier disposals - compared with 15% in 2006/07 - and 1% of the total 2010 investment market.

There is considerable variation around Europe in the strength of government commitment to this type of activity, and in the degree of success in executing planned programmes. In general, the ability of governments to dispose of real estate assets successfully depends partly on the motive for disposal and the type of asset. With current investor appetite heavily focussed on prime assets, investor demand is likely to be stronger for assets that are still needed for operational purposes (and which therefore produce investments with long government-backed income streams) than for surplus buildings that may be in poorer locations and incur probable vacancy risk. In parallel, many governments are also looking more actively at the scope for space rationalisation and other means of using operational space more efficiently, even without any change in ownership. Beyond this, however, the situations are highly specific.

There are some countries where stronger public finances or political opposition mean that sales programmes are either unnecessary or inadvisable. In Denmark for example, the relatively small deficit means that the government doesn't need to consider extraordinary measures beyond raising taxes and cutting public spending. The value of real estate holdings owned by the agency responsible for disposal of government buildings is valued at around €116 million. Despite some increase in disposal activity in 2010, property sales were not a significant source of fiscal revenue. In Belgium, there was a substantial sales programme in the 2001-06 period, which met with public and political opposition and has not been revived.

Public sector property sales, 2010



Source: CB Richard Ellis

In other countries, various types of outsourced vehicle have been set up, or are under consideration, for the management and selective disposal of government assets. In Austria, for example, a major stake of the former state-owned real estate has been placed in a quasi-private company under state control, but from which there have been no disposals as yet. In Italy the new "federalismo demaniale" aims to update the list of state-owned assets in order to transfer them to local authorities, which in turn are committed to the enhancement of these assets. Some municipalities are likely to create new real estate funds from those assets in order to manage and improve them. For instance, the Municipality of Milan launched a new fund, the Fondo Immobiliare – Comune di Milano II. The portfolio consists of 65 units in the Milan area with a total asset value of approximately €120 million. Separately, ENASARCO, one of the Italian Public Pension and Insurance Funds, has launched a plan to divest a large part of their real estate assets, mainly residential but with some retail assets too.

In Germany, there are no specific asset sales programmes proposed by the German government or public authorities. Recently some municipalities have increased taxes and fees, and downgraded their scope of services to cut costs, but there is no special programme to sell their assets. It is likely however, that some local (and cooperative) housing companies could be privatized in the near future, but this is politically very contentious. Political obstacles exist in other markets too. In Poland, for example, there are often many ownership claims towards the buildings occupied by government agencies and public institutions, which is one of the reasons why disposals have not been widely pursued yet.

In Spain, there is some momentum behind plans to create regional level vehicles to house public real estate assets. There is the intention, with or without these vehicles in place, to auction selected assets held by regional bodies.

Activity should therefore pick up, although it could take some time not least because there are legal hurdles to clear first: many assets lie on land zoned for public use, which may present an obstacle to sale although solutions are being actively sought. Another factor to consider is the destination of the proceeds: several ministries occupy prime pitches on the Castellana in Madrid but a central government department retains ownership of the assets. In the absence of separate property P&L accounts, if these buildings were to be sold, the proceeds would go into central coffers, which could be politically difficult. Finally, a number of state-owned companies have plans to dispose of real estate assets, although again the political sensitivity should not be under-estimated.

In Ireland there have been no specific statements of intent from the Office of Public Works, partly because there are higher priorities on the political agenda, but it is likely that moves in this direction will accelerate in 2011, particularly in light of the recent general election. There is more prospective activity in Northern Ireland, where the public sector is rationalising, with potentially substantial impacts on the market. The Northern Ireland Executive has announced plans to dispose of over £500 million of assets by 2014, although this may prove to be over-ambitious.

In the UK, where public asset disposals have been limited in scale over the past two years, recent indications appear to have softened the intention to dispose of £35bn of assets over the next ten years, in favour of seeking greater operational efficiencies from occupied buildings. In part this reflects the view that prices achievable in markets outside London would not generate adequate returns, and that a more selective approach is needed focussing only on assets where sale would produce clear cost-saving benefits.

In France, the government is estimated to have sold around €1.5bn of real estate in the three years 2007-09, although the scale of disposals fell sharply last year, partly because the proposed sale of the Ministry of Defence buildings in Paris did not go ahead. The latest valuation (which is not universally accepted) puts the total value of French state real estate holdings at over €60bn, which provides a strong basis for the government's ambitious sales programme over the next couple of years. Indeed, the share of the proceeds of real estate sales dedicated to lowering national debt is projected to rise from 15% to 20% in 2012. In tandem with its asset sales programme, the signs are that the French government intends to enforce its rent ceiling for buildings occupied by state ministries: parliament recently forced the Justice Ministry to select a cheaper location that complies with the €400/sq m/year rent ceiling imposed on state bodies.

CONCLUSIONS

Sale of publicly-owned real estate remains on the political agenda in many parts of Europe and further sales are expected. However, the most recent evidence indicates that actual activity levels remain muted. There is wide variation in the quality of public sector assets and hence their appeal to prospective investors. There may also be political tensions between the need to be seen to be considering all options for deficit-reduction, and concerns that some previous programmes have only been partially successful. As a result there is additionally a growing focus on measures focussed on cost-saving and improved operational efficiency.

CBRE
CB RICHARD ELLIS

For more information regarding the MarketView, please contact:

Richard Holberton
Director, EMEA Research
CB Richard Ellis
St Martin's Court,
10 Paternoster Row
London EC4M 7HP
t: +44 20 7182 3348
e: richard.holberton@cbre.com

John Wilson
Executive Director, Corporate Strategies
CB Richard Ellis
St Martin's Court,
10 Paternoster Row
London EC4M 7HP
t: +44 20 7182 3561
e: john.wilson@cbre.com

Robert Oldham
Senior Director
Government & Infrastructure – Regeneration and Development
CB Richard Ellis
Kingsley House
1a Wimpole Street
London W1G 0RE
t: +44 20 7182 2579
e: robert.oldham@cbre.com