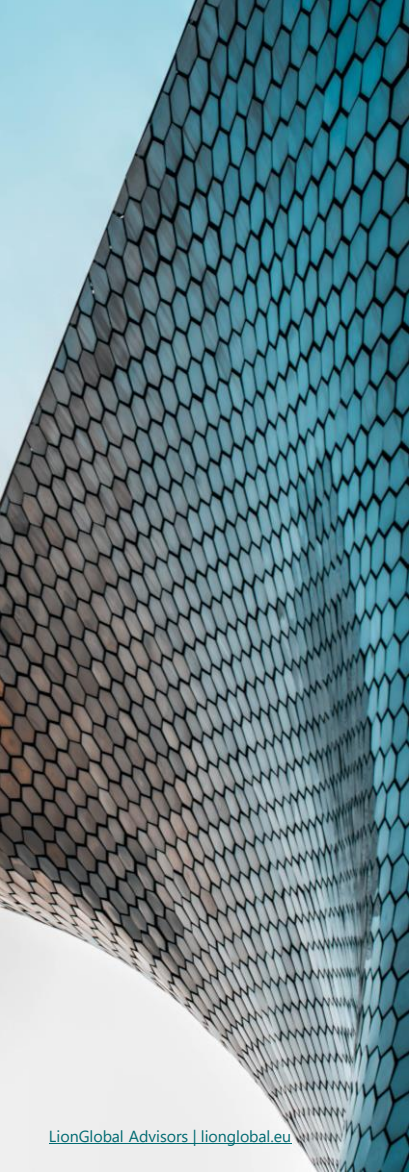
COVID-19 Impact on Real Estate Markets

While the primary impacts of Coronavirus are currently being felt by individuals and communities around the world, the duration and severity of its effect are still largely unknown. All sectors of the Economy will certainly feel the direct impact of the pandemic related to escalating number of event cancellations, office closures, travel restrictions and quarantined areas but what is also important to analyse is the indirect effects over the different sectors of the Economy. This crisis will certainly change our way of living and working, potentially leading to new operational models. But how all these affect the Real Estate sector?

The coronavirus's ultimate impact on real estate markets will largely depend on the length of the outbreak and whether there is a quick recovery (with a return to overall social and economic stability) or a more extended one.

Real estate market has a history of performing relatively well after economic shocks compared to the more volatile stock market and despite what many people believe, there is no direct connection between stock market performance and real estate values. All has to do with the overall health of the economy and consumer's behavior. As long as consumers feel confident about their jobs and income, they will continue to spend—and that includes investing in real estate.

To better understand the current and future impact on real estate markets, LGA team has assembled their initial guidance and analysis here. As the situation is rapidly evolving, some of the perspectives in this article may fall rapidly out of date.



Economic impact

The pandemic continues to expand with more than 175 countries and territories reported cases of COVID-19, the disease caused by the coronavirus (SARS-CoV-2). On March 11, 2020 the World Health Organisation officially recognised coronavirus disease 2019 (Covid-19) as a pandemic. The virus was initially identified in China in December 2019 and as of April 2020 more than 1 million cases of Covid-19 have been recorded, resulting in dozens of thousands of deaths around the globe.

As a result of the wide spread of the new virus, many countries' governments have imposed strict measures such as quarantines, travel restrictions, curfews, event cancellations and postponements in an effort to prevent further spreading of the pandemic. As a consequence of the above, in the short term the impact of the covid-19 on the global economy is irrefutable while the production activity in many countries has already been reduced significantly and the travel and tourism sectors have been affected as well. Therefore, as long as the new coronavirus is spreading, the economic consequences are increasing accordingly and even if the world's GDP growth rate will be recovered after the end of the pandemic, a gap between the old and the new path will be created, demonstrating an one-off damage for the majority of the world's economies.

Many analysts have inevitably drawn a correlation between Covid-19 and previous disease outbreaks such as SARS, MERS, and avian flu. If the virus follows previous trends, the economic impact will not last for long and the markets will soon rebound. However, in the short term, COVID-19 is expected to hit the economy harder than previous outbreaks due to the extremely strict measures introduced by the local authorities or people themselves.

Economic centers around the world are subject to Wuhan-style shutdowns as people panic over the spread of the virus. All these have resulted in a significant decline of equity and corporate bond markets, with investors preferring to hold government securities because of the uncertainty created by the pandemic.

As always, in time of adversity there are always some opportunities, with some business and markets (mainly parts of the technology industry) that are benefiting from the considerable changes forced on society.
This includes online shopping platforms, telecommunication industry, ecommerce, electronic payments, cloud computing etc.

In Cyprus, the first two cases of the new coronavirus were recorded on March 9, 2020 and on March 21, 2020 the first death was confirmed. With hundreds of cases of the new coronavirus, Cyprus government already announced a number of measures including a near lockdown, closing of all borders, closing of schools, shopping malls, catering establishments, hotels and entertainment venues among others.

The tourism sector is the most important factor of Cyprus' economy with almost 4 million tourist arrivals per year. As a result of the above and due to the measures imposed by the government, the country's economy has already been affected and the further impact on the economic performance of the country is undeniable. Regarding the real estate sector, taking into account that the 43% of total sales transactions referred to overseas buyers for 2019 and as the construction activity has stopped, it is clear that the impact of the covid-19 on the factor will be substantial.

On the other hand, the government has already announced a package of financial measures equivalent to 3% of country' s GDP, including fiscal and liquidity support measures in order to support businesses and labor, while further measures are expected to follow. In addition, Cyprus is coming from a 5 consecutive year period of economic expansion with a remarkable improvement in public finances and therefore the country is in a good financial position to withstand the following challenging period.

Tourism & hospitality industry

While COVID-19 is impacting all industries, the tourism & hospitality sector has experienced the most significant impact to date given increasing travel restrictions, major event cancellations and overall risk aversion to travel internationally and domestically.

The magnitude of the impact would depend on the duration of the outbreak and counteracting measures.

Based on The World Tourism Organization (UNWTO), it is too early to estimate the full impact of the COVID-19 on international tourism. For its initial assessment, UNWTO takes the SARS scenario of 2003 as a benchmark, factoring in the size and dynamics of global travel and current disruptions, the geographic spread of COVID-19 and its potential economic impact:

- As of today, UNWTO estimates that in 2020 global international tourist arrivals could decline between 1% to 3%, down from an estimated growth of 3% to 4% forecast in early January 2020.
- This could translate into a loss of US$ 30 to 50 billion in spending by international visitors (international tourism receipts).
- So far, the Asia and the Pacific region is expected to be the most affected (a decrease of 9% to 12% in international tourist arrivals, down from growth of 5% to 6% forecast in early January 2020).
- Estimates for other world regions are currently premature in view of the rapidly evolving situation.
- UNWTO underscores that any estimate must be treated with caution due to the volatile and uncertain evolution of the outbreak which might lead to further revisions.

On the other hand, The World Travel and Tourism Council (WTTC) has warned the COVID-19 pandemic could cut 50 million jobs worldwide in the travel and tourism industry. Specifically, latest figures from WTTC, show that global travel could be adversely impacted by up to 25 per cent in 2020. This is the equivalent to a loss of three months of global travel. This could lead to a corresponding reduction in jobs of between 12 and 14%.

Finally, based on experts there is a potential for a rapid rebound in the second half of 2020 as activity returns to normal level, however there is a risk that the return to normalcy could be protracted. Destinations considered epicentres of the outbreak, or that responded ineffectually, may see a prolonged downside.

Residential

As Real estate transactions typically require a lot of in person interactions, the rapid spread of the covid-19 has already affected the global residential real estate market. Especially in Cyprus, where a high percentage of residential transactions refers to foreign buyers and as travel and face to face meetings are restricted, the impact of the virus on the market is already felt by real estate professionals.

As one might expect, caution will likely increase in the short-term as the impact of the virus is felt in various sectors. In residential real estate it would seem that the biggest impact to have taken so far is on enquiries, with real estate professionals around the world already reporting a dramatic drop in enquiry levels over the past three weeks. Some buyers may choose to delay purchase decisions and be more cautious until the situation improves. As a result, an impact to the near-term is expected but this will be transient as the fundamentals are strong.

History has certainly shown that while markets slow down during an outbreak, they usually bounce back relatively quickly. The real estate market is inherently slower moving than public equity and bond markets, as transactions are usually take months to compete.

This means that momentary disruptions are unlikely to result in immediate volatility for investors. On the other hand, the speed of the market rebound depends on the duration of the outbreak and its impact on the macroeconomic results of each country (unemployment, consumer demand etc.). What we know from studies during previous pandemics is that while home sales dropped dramatically in the short term (during the pandemic period), asset prices remained about the same or suffered a slight decrease in the long term. In short, similar events happened in the past have simply put the housing market on pause as buyers take a 'wait-and see' approach.

Real Estate as an asset class, is expected to remain resilient to the effects of the COVID-19 outbreak with its more stable, longer-term income profile and defensive investment characteristics. Although it is certain that there will be a degree of decline in viewings and enquires whilst the coronavirus threat remains present, various researches suggest that consumer confidence will prove resilient, at least for the time being.

Office market

In terms of the real estate life cycle, the office sector is going to be one of the last to feel the true impact of the virus. A large portion of office tenants are still able to conduct operations and will be able to cover their rent for the near future. The percentage of tenants that can function in this format is much higher than retail, hospitality and industrial. However, corporations unable to operate remotely. with lower IT infrastructure will be most affected by Covid-19.

Local and foreign firms are expected to be prudent in relocation or expansion activities, while small and medium-sized enterprises are likely to experience higher financial liquidity risks. As a result, a delay to investment activity and softer rental growth than previously forecast are expected for the second half of the year.

Landlords with exposure to short-term leases are the most vulnerable as remote working increases and the fact that the leasing or licensing arrangements around these may make it simpler for occupiers to exercise the flexibility of these agreements, and reduce or cancel their commitments.

Coworking providers during this pandemic will lose tenants, as many leases will not be renewed.

We are at the beginning of the greatest test of the ‘working from home’ in history and organisations are adopting, refining and testing policies, procedures and infrastructure to make it work. In the face of COVID-19, corporations have largely demonstrated prompt business continuity actions, with timely decision making and close monitoring of a highly fluid situation helping to stabilize the business environment and eventually recover from the current crisis. Looking ahead, we expect landlords and tenants to place greater emphasis on wellbeing and smarter workplaces, with factors such as intelligent building management, wellbeing and safety management key to enhanced office property competitiveness.

Retail market

As the pandemic is spreading rapidly around the world, many countries came under quarantines orders and other restrictions. Retail companies are facing challenges around supply chain, labor force, cash flow and consumer demand while many of them are temporary closed or forced to operate only online.

With some exceptions, the majority of the retailers have already seen an important decrease in their turnover mainly due to the measures imposed by the governments. In the medium to long term, the main problem will probably be the decreased consumer demand due to the potential economic slowdown, while the biggest declines in the revenue of such companies may be observed in tourist areas.

The impact of the covid-19 on the retail real estate market will depend on the duration and severity of the outbreak.

packages of measures that include financial support for affected businesses and labor and also measures that aim to maintain domestic consumption, If the spread of the virus decreases significantly in the following period, the effects on the market will be minimal and the retail real estate sector will return to normal levels relatively quickly.

On the other hand, if the transmission of the virus continues through the end of the year, significant downside risks will be appeared. More specifically, if the spreading of the virus continues, the decreased consumer demand will result in many retail companies unable to meet their financial obligations and many of them will probably want to negotiate the terms of their rental agreement. As a consequence, default risk for current tenants and vacancy losses will be increased and rental yields for the landlords will decline. All of the above, are expected to affect the retail property prices in the medium to long term.

Key takeaways:

Economy	• Globally, coronavirus outbreak will hit economy hard in the short term, but we can hope that the economic impact will not last for long and the markets will soon rebound. • At the national level, government's strong response in addressing the spread of COVID-19 virus, including a revised economic support package which will amount to at least €1.5 bln, supports mid to long term confidence for the economy.
Tourism & Hospitality industry	• Tourism and hospitality sector are among the hardest hit so far by coronavirus outbreak, given the increasing travel restrictions, major event cancellations and overall risk aversion to travel internationally and domestically. • The magnitude of the impact would depend on the duration of the outbreak and counteracting measures. • It is unlikely that Covid-19 will trigger a structural change in the industry.
Residential market	• An impact to the short term is expected as a result of the uncertainty and the dramatic drop in enquiry levels but this will be transient as the fundamentals are strong. • Residential real estate has a history of performing relatively well after economic shocks, however the speed of the market recovery depends on the duration of the outbreak and its impact on the macroeconomic fundamentals of each country.
Office market	• A delay to investment activity and softer rental growth than previously forecast are expected over the upcoming period • Short term leasing activity and the coworking sector will likely be hardest hit • Looking ahead, we expect landlords and tenants to place greater emphasis on wellbeing and smarter workplaces
Retail market	• Domestic retail expenditure, especially on travel, luxury and leisure, will weaken in the short-term, but ecommerce will definitely receive a boost. • The consequences of the outbreak could be limited and the market can return to normal levels relatively quickly if the spread of the virus decreases significantly in the upcoming period

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