Turkish real estate market outlook

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The re-opening of recent agreements and chapter negotiations with the European Union (EU) can be seen as positive developments for the Turkish economy, along with the commodity prices

Turkey is a country whose growth potential is challenged with reverse capital flow pressure and regional political uncertainty. However, the demand drivers of the Turkish real estate sector such, as the country's "crossroads" geographical location, urban renewal and development projects, strength in the construction sector and demographic advantage continue to support the Turkish real estate market. The Turkish real estate market, office and commercial property have outperformed over the past five years. Indeed the rental yields and selling prices for retail and residential prices have been continuing to grow since 2010. In the future, primary commercial properties in central areas are likely to attract investor interest. Real estate is one of the most significant drivers of the Turkish economy and will continue to be in future.

Historically, Istanbul has been the trade and cultural center between Europe and Asia. The city sits on the border of both continents, which has attracted many leading real estate companies and international investors. There are several factors that attract foreign investors to Istanbul, one of which is affordability—considering the more than 50 percent US Dollar appreciation against the Turkish Lira during last two years and also the straightforward and accessible financing tools in Turkey. After the elimination of the reciprocity principle in 2012 with regards to the sale of real estate to foreigners, the real estate industry has witnessed an increase in sales to foreigners. In addition, with the government's introduction of a new law in 2013 to supplement the existing law, foreigners' residence permits were extended from three months to one year and allowed the renewal of the residence permit, as long as the foreigner continues to own property in Turkey.

The various challenges in the global landscape are likely to continue in 2016. This prediction largely stems from the concerns about emerging economies, with Turkey unlikely to be exempt from this situation. Federal Reserve System (FED) kept interest rates unchanged during their session on 17 March—meeting most market watchers' expectations—yet FED expects to raise rates twice this year. It appears that extreme rate hikes are off the table for now, yet it would be optimistic to think that the pressure on emerging economies would decrease, including Turkey. However, it is also possible that there would be a relative decrease in the volatility with the start of the normalization process. There are some other uncertainties such as the discussions regarding the presidential system;

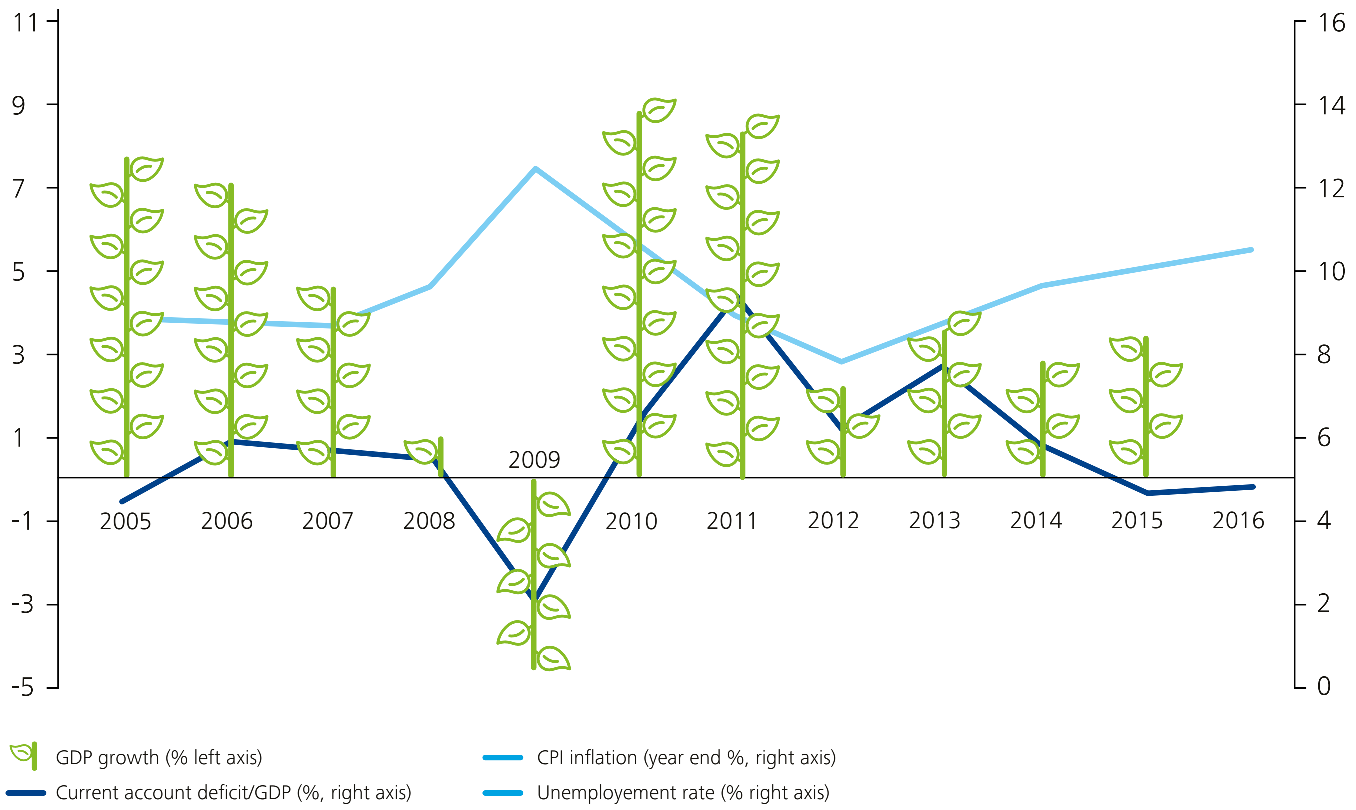
whether it will continue and how long it will occupy the public agenda are among the unknowns. The region is currently in a state of chaos due to Syria, which has reflections locally. Furthermore, the rising tension between Russia and Turkey and the outcome of the peace process are important drivers of political risk and uncertainty.

On the other hand, the re-opening of recent agreements and chapter negotiations with the EU can be seen as positive developments for the Turkish economy, along with the commodity prices. At the time of writing this article, the price of the Brent crude oil was below US$40 per barrel. Thus, Turkey's energy import bill might decrease further, though not as much as the decrease observed this year. Recovery in the Eurozone is a positive development for Turkey, however 2016 will be another challenging year. There may be a growth rate of 4 percent or more and inflation levels below 7.5 percent, however the current account deficit remains high.

What should we follow in 2016?

Apart from the unknown risks (termed black swans) and geopolitical risks, the main issues that should be monitored are FED, the course of China and other emerging economies including Turkey, and as well, the perceptions of investors regarding the emerging economies.

Figure 1: Main macro factors in Turkey



Source: Deloitte Turkish Economic Outlook Report

Long-term prospects for the Turkish Real Estate Market

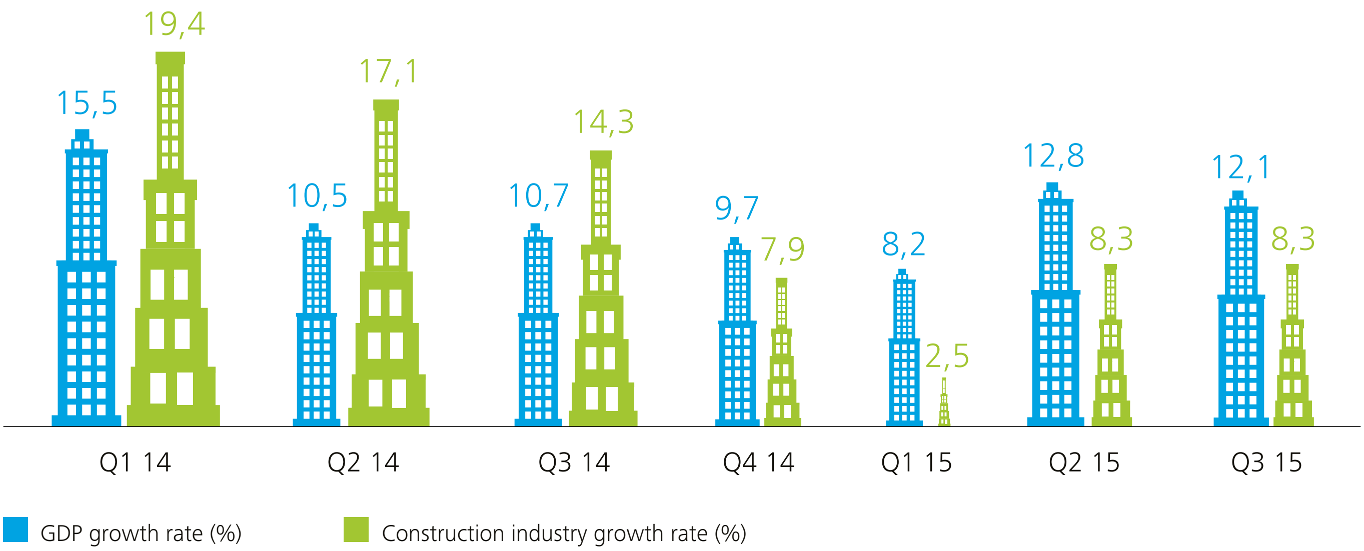
Although current investors remain hesitant to make transactions in the short term, the Turkish real estate industry presents many opportunities to both local and international investors over the mid to long term. Turkey, with its large and young population, drives domestic consumption to a considerable level. Along with a population increase in recent years, families are being divided due to cultural change, urbanization, increased levels of income and improved life standards; the division of families means that the demand for real estate is constantly increasing.

At the doorstep of Europe, the Turkish market addresses two fundamental flaws: a glowing economy and GDP growth, as well as, favorable demographics—further confirmed by a persistent growth in consumption. However, while offering a clear opportunity for the Turkish property market to attract non-domestic investors—especially investors from Gulf countries—risk aversion remains high due to geographical and regional uncertainty.

Gross domestic product increased by 12.1 percent compared to the same quarter of the previous year, while the growth rate for the construction industry was 8.3 percent for the same period.
The share of the construction sector in the overall GDP in Turkey was 4.7 percent.

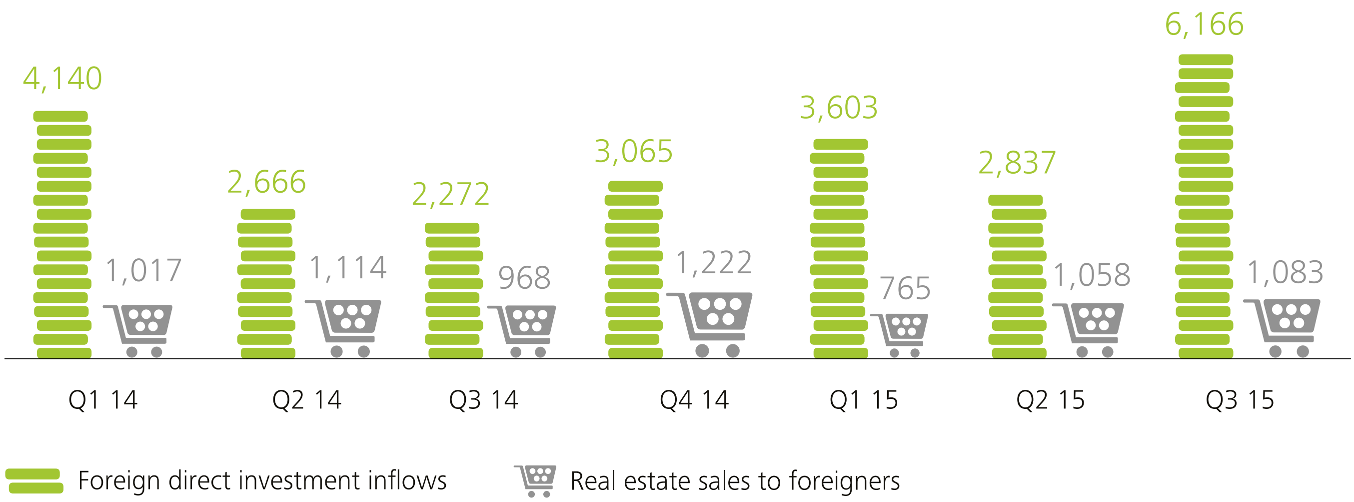
The share of property sales to foreigners decreased by six percent in the first nine months of 2015 compared to the previous period.

Figure 2: Construction industry vs. GDP growth rates (current prices)



Source: Turkstat

Figure 3: Foreign direct investments



Source: Republic of Turkey Ministry of Economy

In 2015, the total number of house sales reached 1.28, compared to 1.16 million in 2014, showing an annual growth rate of 10.6 percent

Residential

Turkey's population continues to migrate from rural regions to urban cities, where currently 75 percent of the population lives. This population shift increases the demand for the construction of new buildings in urban areas.

In 2015, the total number of house sales reached 1.28, compared to 1.16 million in 2014, showing an annual growth rate of 10.6 percent. Conversely, monthly mortgage loan interest rates, which were below one percent in the first nine months, showed an increasing trend in the last quarter of 2015, which can be seen as a possible decrease in demand. Total mortgage loans reached 132 billion turkish Lira (TRY) in 2015, compared to 114 billion TRY in 2014, showing an annual growth rate of 15.7 percent.

Logistics

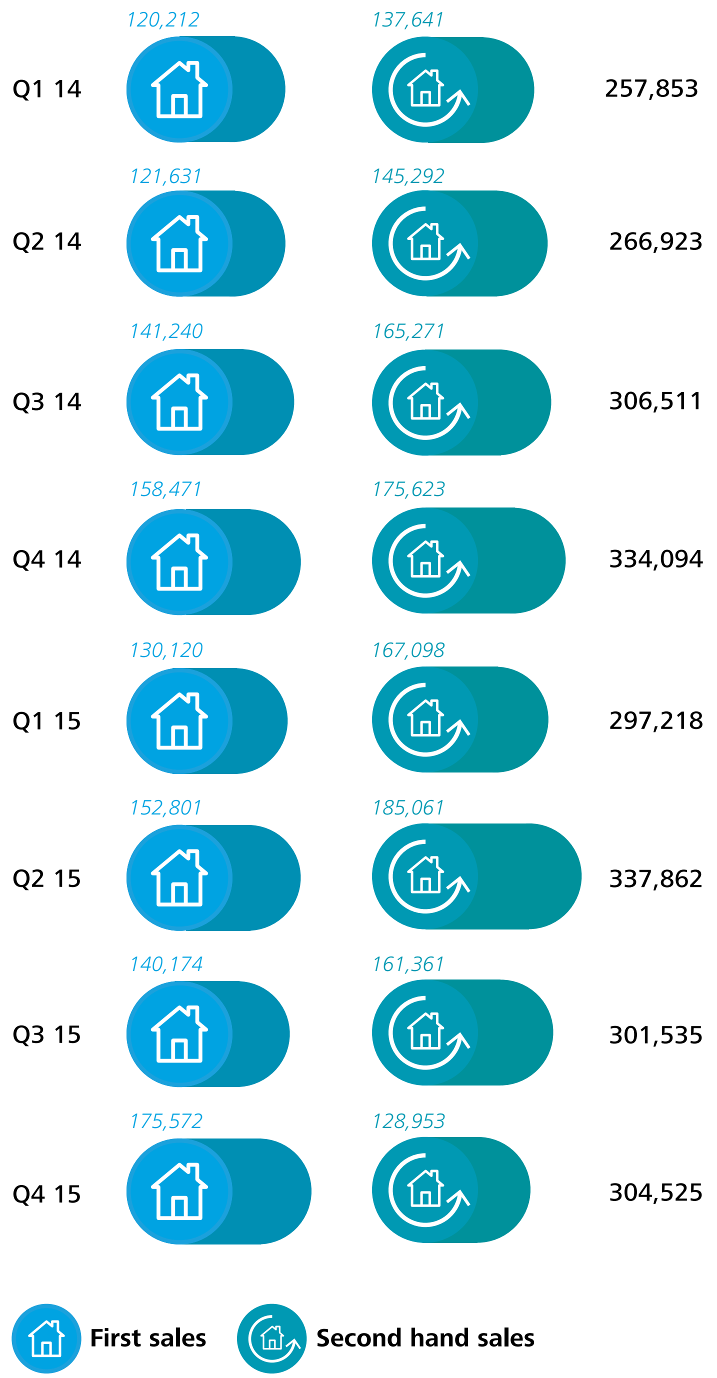
Turkey, as a regional hub providing easy access to 1.5 billion consumers in Europe and the Commonwealth of Independent States (CIS), and as an energy corridor between Europe, Central Asia, and the Middle East, creates more and more enterprises each year within its borders.

Infrastructure projects continue to increase the performance of the logistics industry and, given that the expected efficiency is achieved, more individual and corporate foreign investors will be willing to relocate their base to Turkey. There have been significant improvements in the logistic infrastructure of Turkey in the past years; new airports have been built in many cities of Anatolia, the capacity of ports have increased, many dual carriageways are ongoing and the high-speed train network construction has commenced connecting major cities—thus having an impact on freight and passenger transportation volume. There are several critical infrastructure projects that upon completion will have an impact on the real estate market development.

New Istanbul Airport: The first phase will open in 2018 and aims to serve 90 million passengers per year. This will increase to over 150 million passengers once fully complete. Terminal 1 of the new Istanbul airport will be the world's largest airport terminal under one roof, with a gross floor area of one million square meters.

Third Bridge: The third bridge will be the world's widest (59 meters) and longest spanning (1.4 kilometers). The bridge, which will be built on the Bosphorus as part of the Northern Marmara Motorway Project, is considered the future of transportation and commerce. It will be completed in 2017.

Figure 4: Housing sales number (units)



Source: Turkstat

Retail

Organized retail continues to grow with an increasing number of shopping centers around the country. In 2015, the number of malls increased to 360 in 2015. There are 58 cities out of 81 with shopping malls and new investments are in the pipeline. The total gross leasable area (GLA) reached 10.5 million square meters at the end of 2015 and the GLA per 1,000 people exceeded 120 square meters. These numbers are higher for Ankara, Istanbul, Karabuk, Bolu and Eskisehir, which have over 151 square meters in total density.

This ratio is still below the levels of most of the developed markets (EU-27 average was 265 in 2015), which indicates room for growth; currently there are 17 cities with more than one million people, in addition to the three main cities[1]. Thus, although the three large cities have reached a certain saturation level in terms of gross leasable area, there are many opportunities for growth in other cities across Turkey.

Figure 5: Shopping centers and Gross Leasable Area (GLA)

1 GLA per 1,000 inhabitants between 101-151 square meters in Bursa, Gaziantep, Antalya, Kayseri Kocaeli, and Aydın; 51-100 square meters in Adana Konya, Mersin, Diyarbakır, Balıkesir, and Samsun; 0-50 square meters in Hatay, Sanlıurfa, and Manisa

Office

Istanbul office markets continue to experience strong performance, especially in the central business districts where vacancy rates are in the range of 16-17 percent. Consequent to multinational companies establishing their regional management and operational centers in Istanbul, as well as, increasing growth and institutionalizing trends of national companies, the office demand continues to increase. This strong demand and requirement for office space continues to trigger office investments.

One of the significant office projects in Istanbul is the International Finance Center (IIFC), which includes office spaces, as well as, shopping centers, residences, congress centers and related businesses. The project will be completed in 2018. The Turkish government's goal for the landmark project is to establish Istanbul as a global center for finance. The IIFC will house the head offices of the Banking Regulation and Supervision Agency (BDDK), the Central Bank, the Capital Markets Agency, state-owned and private banks such as the Central Bank, the Capital Markets Agency, Ziraat Bank, Halkbank, Vakıfbank and other financial institutions. It will include 45 million square feet of office, residential, retail, conference, hotel and parking space.
Office construction licenses obtained throughout Turkey in 2015 increased by 8.6 percent compared to the previous year and topped up to 8 million square meters. Office building occupancy permits increased by 87 percent compared to 2015's first three quarters with a total of 7.5 million square meters, resulting in increase of office supply.

The Turkish real estate sector from the perspective of foreign investors

Investors in the Middle East and North Africa (MENA) region perceive Turkey as a growing and promising country with a long historical relationship. Most Arab investors want a second home, or they see Turkey's real estate market as more affordable than the EU, because it is still at its infancy phase. Going forward, MENA investors are bullish about Turkey, which saw doubling investments from this region in the last year. MENA now accounts for a similar fraction of total foreign investment in Turkey as the EU.

To the point

Although currently investors remain hesitant to make transactions in the short term in Turkey due to political and economic uncertainties in the region, with the favorable demographics and consumption growth levels, the Turkish real estate industry presents many opportunities to local and international investors over the mid to long term:

- Residential: Turkey's population continues to migrate from rural regions to urban cities, increasing the demand for construction of new buildings in urban areas.
- Logistics: There have been significant improvements in the logistics infrastructure of Turkey in the past years. New airports have been built in many cities of Anatolia, the capacity of ports have increased, many dual carriageways are ongoing and the high-speed train network construction has commenced, which connects major cities and has an impact on freight and passenger transportation volume. Furthermore, critical infrastructure projects such as Istanbul's new airport and Third Bridge, when completed, will also have an impact on the development of the real estate market.
- Retail: Organized retail continues to grow with an increasing number of shopping centers around Turkey. Although the three large cities have reached a certain saturation level in terms of gross leasable area, there are many opportunities for growth in cities with more than 1 million people across Turkey.
- Office: Consequent to multinational companies establishing their regional management and operational centers in Istanbul, as well as, a growth of national companies, the office demand continues to increase, triggering office investments.