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THE REAL ESTATE MARKET IN CROATIA ANNO 2016

The Croatian economy is finally showing signs of recovery from the recent economic downturn. After entering the European Union in July 2013 as the 28th member state, the government has been striving to raise Croatia's competitiveness to compete in the large EU market and maximize the opportunities that a membership brings, especially the interest of a large amount of EU Structural Funds.

The structure of the Croatian economy is dominated by the service sector, primarily due to the well-developed tourism, with tourism revenues representing around 16% of the country's GDP. The ex-socialist government failed to implement the necessary reforms and the impact of policies on the entire social flows remains a concern above all stasis.

Croatia has been unable to take advantage of its unique geographic location; at the sea side and yet close to the central European markets. The Croatian companies are primarily connected by business to Bosnia, Serbia, Macedonia and Montenegro and will in the short term lose trades with traditional partners in CEFTA.

The industry is expected to fare slightly better over the forecast period (2015–2019), however, with new investment in transport infrastructure, energy, industrial and commercial projects, and improving investor confidence as regional and global economic conditions improve. Croatia's banking system, which is mostly foreign owned, has remained stable, liquid and well capitalized. Most of the banks faced a sharp decline in loans, due to the economic crisis and have been faced with a significantly lower loan activity.

PREDICTIONS FOR 2016:

- The economy is estimated to increase by 1.1% by 2016
- No new projects for shopping centres are expected in 2016, leading the hyper and supermarkets to open their own stores.
- The retail market in Zagreb is oversaturated and therefore the developers are shifting their attention towards smaller cities on the seaside such as: Pula and Dubrovnik.

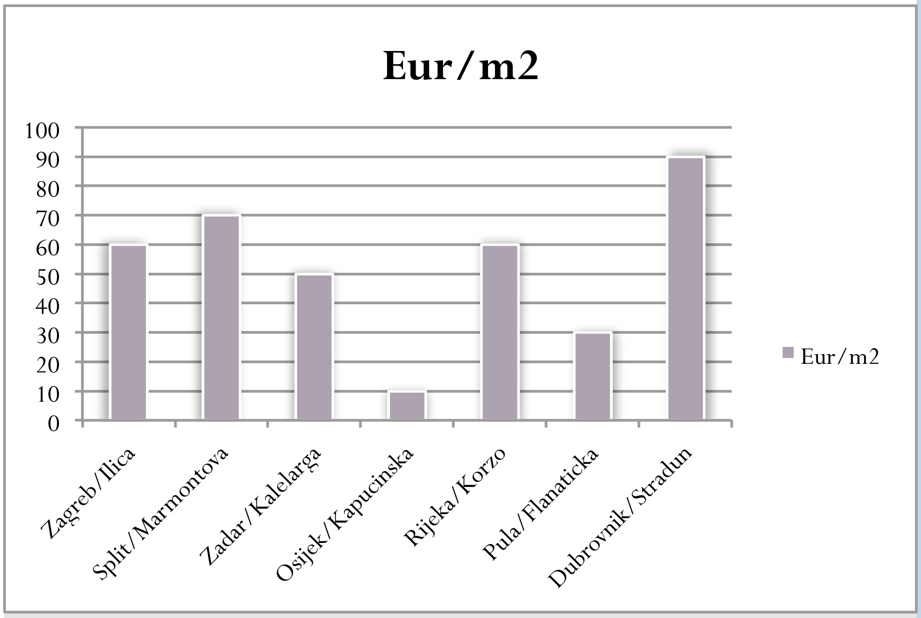
RETAIL MARKET CROATIA

Since Croatia joined the European Union in 2013, retailers have focused on reducing suppliers' prices by making use of cheaper imports from EU countries or by streamlining their logistics. The Croatian retail sector is known for its elevated overhead costs due to low sales volumes as well as high distribution costs because of geographic particularities. There has been a price war between retailers over the past two years, with companies competing to become more competitive in a market where prices dictate consumer behavior. Due to price reductions, not only in the retail sector, the Croatian economy has recently experienced a rare case of deflation, with prices declining in 2014 and 2015. While consumers appreciate falling prices, retailers are in the middle of a price war, which is thinning their profit margins.

VACANCY RATE:

The vacancy rate is the numerical value calculated as the percentage of all available units in a rental property, such as a shopping centre or apartment complex, that are vacant or unoccupied at a particular time.

PRIME RENT IN HIGH STREETS



PRIME RENT:

Represents the top open market net rent that could be expected for a national prime position shop situated in the best-located shopping center in a market, as at the survey date. The rent quoted normally reflects prime units of 200 m^2 of gross lettable area. A shopping center is created as a single entity and GLA that exceeds 5000 m^2 and where more than 10 shop units are present in the mall.

RETAIL RENT

The highest average rents contracted in year 2007/2008 amounted to an average of 30 eur/m^2, where the highest were in City CentarOne West. After years of continuing falling rents, the rents stabilized in 2015 and a slight increase is expected the next couple of years. At the moment, the prices are depending on the number of floors (ground floor or higher floors) and surface. It is also negotiated on percentages of turnovers, which are moving on an average of 6%. Most high profile tenants renting a space are only paying a percentage of the turnover. Big tenants (measured over 1000 m^2) and small tenants in Croatia are in the ratio of half-half. The tendency is to increase the surface areas in shopping centers for larger tenants in relation to smaller, which is 60:40.

HYPER & SUPERMARKETS IN CROATIA

Supermarket retailers were relatively unaffected by the recent economic downturn due to the fact that products within this area are perceived as being essential, with customers making cuts in other areas. However, in 2015, with the economic downturn ending, supermarket retailers did not have a strong growth, and therefore sales remained stable.

Agrokor is the undisputed leader in Croatia, with its two companies, Konzum and Tisak. After the acquisition of Mercator, the Konzum part of the business found itself in turmoil and had to make a smooth transition of the Mercator brand into Konzum and get rid of 96 outlets rapidly. Despite this, Agrokor managed to immediately increase its market share by 9% to 30%.

The U.S. real estate investment trust W.P. Carey purchased 8 of Agrokor's Konzum supermarkets in Croatia, worth a reported €34.6 million. The Konzum supermarkets, which the American company purchased, are located in Zagreb and surrounding areas. W.P. Carey has leased back the stores to Agrokor, making Konzum the tenants of W.P. Carey. This is the fourth 'sale-leaseback' deal between the two in the last three years, reflecting a net initial yield of 10%, which places Konzum in a difficult position in relation to their competitors, due to the disturbing financing of the World Bank and the EBRD cheap capital to the Schwarz group. The Schwarz group received more than 46 million euros for further expansion and development in Croatia and its surrounding countries in 2013, and has yet again been approved 305 million euros by the International Finance Cooperation (IFC) and is by that making it harder for their competitors on the market. Konzum has a market share of 25% at the moment and 30% including their smaller partners. Due to a competition regulation in the country, they are not allowed to have a bigger market share.

Lidl, owned by the German Schwarz group, plans to raise its investments in Croatia to 40 million euro in 2016. The figure would top Lidl's 2015 investments in the Croatia, which totaled 35 million euros. Lidl entered the Croatian market in 2006 with the simultaneous launch of 13 supermarkets. The company operates a total of 86 supermarkets and two logistics centers in Croatia and employs 1,700 at the moment. Another Hypermarket chain owned by the Schwarz group is Kaufland. The first hypermarkets opened in Croatia in 2001 in Čakovec and Karlovac. Kaufland has now 14 supermarkets throughout the country, with the last opening in Vukovar in 2012.

Another supermarket in Croatia is the Austrian chain Spar. They opened their first supermarket in Croatia in Zadar in 2005 and have since then expanded throughout the country and developed the supermarkets into small shopping centers called Interspar. Today they own 18 hypermarkets and 35 supermarkets in Croatia, having a market share of 6%, which they partly achieved through the acquisitions of 20 branches as well as reorganizing existing and opening of new stores.

Furthermore the Croatian chain Tommy has 184 supermarkets throughout Croatia, mostly on the coast side.

Billa, owned by the German REWE group has 49 stores throughout Croatia.

SUPERMARKETS IN CROATIA:

- Konzum
- Kaufland
- Billa
- Lidl
- Spar
- Tommy
- Plodine

The hypermarkets in Croatia represent 70% of the entire retail market in Croatia, while other smaller business represent 30%.

Yield

The retail yield is at the moment 8%.

(Mall of Split)

ZAGREB OVERVIEW

Existing Shopping Centres:

- Arena Centar
- Vrbani Shopping Centar
- King Cross
- Avenue Mall
- City Centar One East
- City Centar West
- Super Nova (Buzin)
- Garden Mall
- Ikea

Average Rents Zagreb.

In City Center one East and West the rent depends on florr and surface. For a larger surface the rent is 10 eur/m^2 – and between 25-30 eur/m^2 for smaller surfaces. In Arena Centar the rent for smaller surfaces is between 35-40 eur/m^2 and 12 eur/m^2 for larger surfaces. In Avenue Mall the rent for smaller surfaces is 25-30 eur/m^2 and 8-9 eur/m^2 for larger surfaces. Additionally in every shopping centre the rent is also measured as a percentage of the turnover.

Prime Rent in High Street:

Ilica - Starting from the main square to Gunduliceva, Cvijetni trg and Bogoviceva: 60 eur/m^2

RETAIL MARKET ZAGREB

Over the previous decade, the retail market has witnessed a huge level of development. Since 2007, the shopping centre stock has evolved rapidly with a significant level of new supply added in the period from 2009 and onwards. Additionally has the retail market been extended by several new developments in Zagreb.

In 2010 the big shopping mall *Arena Centar* opened in the southwestern part of Zagreb. Arena Centar is known as Croatia's premier shopping centre. It is a new and modern 4th generation shopping-entertainment centre and an architecturally impressive building. It features a cinema in top class as well as a casino. It was Croatia's first shopping centre of its kind.

The construction activity in 2011 was strong and the shopping centre stock varied throughout 2011. Several new shopping centres opened, such as Cvjetni Centar in the high street. As a result of the economic downturn, the centres suffered from the crisis, leading the occupiers to reduce costs. At the end of 2011 the shopping centre stock in Zagreb and its metropolitan area totalled 430.000 m^2.

The leasing activity was at that point very strong due to the pre-leasing of the shopping malls Cvjetni trg, Vrbani, Garden Mall and City Centre One East as well as new tenants entering existing arrangements. Moreover new tenants in existing shopping centres being mainly anchors, led to a decrease in average rent.

In October 2012 City Center one East opened in Zagreb, being the third project invested by the Kaufmann group, after City Center One West Zagreb in 2006 and City Center One Split in 2010. The Austrian company *CC Real* manages the centre with around 1000 employees.

At the beginning of 2014, a Supernova Shopping centre/park was build, adding 30,900 m^2 to Buzin. That year the first IKEA store in Rugvica opened, totalling 38,000 m^2. In late 2014, the Meridijan 16 shopping centre by Agrokor, was opened in Gracani, including a new Super Konzum store, spread over 2,000 m^2.

SPLIT OVERVIEW

Existing Shopping Centres:

- Joker
- City Centar
- Mall of Split

Vacancy Rates Split:

- City Centar: 10%
- Joker: 5%
- Mall of Split: 40%

Average Rents:

The average rents in the newly opened Mall of Split and City Centar One are 18 eur/m^2 for smaller surfaces and 10 eur/m^2 for larger surfaces.

In the shopping centre of Joker, the rents are mostly charged as a percentage of the turnover especially on higher floors. Joker has always had stable prices and tenants.

Prime Rent in High Street:

Marmontova: 70 eur/m^2

RETAIL MARKET SPLIT

Currently there are three modern shopping centres in the town of Split and its surroundings: *Joker*, by the investor Kerum with 53.000 m2, and *City Centar* by the Austrian investor CC Real, covering a surface of 50,000 m^2 including more than 100 stores and 2000 workplaces. Additionally a brand new centre – *Mall of Split* – just opened in March this year and is the biggest of its kind in Dalmatia. It is invested by *Mejaši Prvi* and covers a surface of 62,700 m^2, including a cinema, a children world and a casino.

The catchment in Split is 300.000, which makes two big shopping malls at the size of *City Centar* and *Mall of Split* too many at one place. The city is at the moment being over supplied with shopping malls, which will in the end lead one of them to lose. *Joker* stands strong due to its long time on the market and location. It is located in the centre of the city and has many years of experience. As for City Centar, they are located a little outside the main city, which can be a disadvantage. With the new shopping centre Mall of Split opening, it may take the lead as the main shopping centre in the city.

Marmontova is the main shopping street in Split. From the waterfront to the top of the street numerous of shops are lined up, turning the street into the main shopping oasis in the city. The main rent on the high street lays at 70 eur/m^2.

OFFICE MARKET

At the moment there are two business towers being build in the city of Split with an investment of 65.5 million euros. According to information from the city government, the project includes two towers – one with 14 floors on the south and one with 17 floors on the north side – with a total of 50,000 m^2. In the lower building the *SC Splitska Banka* will accommodate offices for their 700 employees and it will be their head building, while the second tower is designed to be a business center and hotel with 100 beds intended for business clients. Moreover it will include a conference hall, restaurants, bars and underground parking.

RETAIL MARKET ZADAR & OSIJEK

ZADAR

There are 155 retail outlets on the gross area of 17.400 m2 of the shopping centre in Zadar at *Relja*. The shopping centre Zadar is dominated by shops selling famous branded clothes and footware and sports equipment as well.

At the moment the *Relja* shopping centre is being expanded and a big Müller drugstore will be opened adding event more square meters to the mall. The rent price is at the moment app. 12 eur/m^2. A *Supernova* opened in Zadar in 2010. It was a huge success with occupiers wanting a place from the beginning. It contains 72 stores with some of the biggest brands like New Yorker, Peek & Cloppenburg, Müller, Deichmann and Benetton adding 700 new working places to the city and its surroundings.

With Relja being expanded and the opening of Supernova, the city is fully supplied - with a catchment in Zadar of 100.000 the demand is small and there is at the moment no need for further expansion.

The main street in Zadar is Kalelarga. It is one of the oldest of its kind and a shopping oasis for the inhabitants and the tourists visiting the city each year. The prime rent on Kalelarga is about 50 eur/m^2.

OSIJEK

At the moment there are two shopping centres in Osijek: *Portanova* and *Avenue Mall*. Portanova opened in March 2011 being the biggest in the region. It has a surface of 80,000 m^2 and was invested by businessman Željko Biloš. It contains over a hundred stores with world-class brands, hypermarkets, restaurants, bars, a cinema and casino.

Avenue mall opened in April 2011 being the first multifunctional shopping centre in Osijek. It covers a surface of 62,000 m^2 with 26,700 m^2 being retail space for more than 80 stores. It has now been bought by the Croatian company *HOK Osiguranje* and has already being emptied, leaving it with a very high vacancy rate.

ZADAR OVERVIEW

Existing Shopping Centres:

- Trgovacki Centar Zadar-Relja
- Supernova

Average Rent:

In the Relja shopping centres in Zadar, the average rent is 12 eur/m^2 – depending on surface and floor and in Supernova the rent is 18 eur/m^2.

Prime Rent in High Street:

Kalelarga: 50 eur/m^2

OSIJEK OVERVIEW

Existing Shopping Centres:

- Portanova
- Avenue Mall

Average Rent:

The average rent in Portanova Osijek for smaller surfaces is 20 eur/m^2 and between 7-10 eur/m^2 for larger surfaces.

High Street Rent:

Kapucinska 10 eur/m^2

RETAIL MARKET RIJEKA & PULA

RIJEKA

At the moment there is two shopping centres located in Rijeka. It is *Tower Centar*, which opened in November 2006, extending on the area of 127,000 m^2. In 2012 ZTC Shopping opened in Rijeka covering a surface of 57,000 m^2 – and 20,000 m^2 being retail.

In Porec a new shopping mall is planned. The concept of the shopping centre will be in line with the needs of the tenants. A project is prepared with a retail park on the down floor and shopping facilities on the upper floor. The concept has been proven good, as the hypermarket has accepted to be located at the upper floor, which it normally never does.

In 2014 the first shopping mall *Slatina* opened in Opatija. It was built on the top floors of a garage building, which was constructed due to the lack of parking opportunities in the city. The mall covers a surface of 4,200 m^2 and is invested by a local investor. The project is one of the biggest private investments made of its kind in the last years in Opatija.

PULA

In the city of Pula there is not a shopping centre at the moment. One shopping centre is planned to open in the end of this summer and is invested by *MID-Bau* Croatia. The shopping centre will have a surface of 28,0000 m^2.

Istra is going to develop much on the retail front - new shopping centres are planned during the next couple of years in Pula and Porec. This means a huge improvement in the retail sector within this region in Croatia.

RIJEKA OVERVIEW

Existing Shopping Centres:

- Tower Centar
- ZTC
- Slatina (Opatija)

Average Rent:

In ZTC Shopping the average rent is 30 eur/m^2. In Tower Centar the rent is measured as a percentage of the turnover.

Prime Rent in High Street:

Korzo: 60 eur/m^2

PULA OVERVIEW

Planned Shopping Centres:

- Shopping Mall in Pula
- Shopping Centre in Porec

Prime Rent in High Street:

Flanaticka: 30 eur/m^2

OVERVIEW DUBROVNIK

Existing Shopping Centres:

- Sub City

Planned Shopping Centres:

- Two new ones in the port of Gruž

Prime Rent in High Street:

Stradun: 90 eur/m^2-

Od Puca 60 eur/m^2.

Average Rent:

In Sub City the average rent is: 18 eur/m^2.

RETAIL MARKET DUBROVNIK

Dubrovnik is one of Croatia's most visited cities. It contains years of history and the tourism is at its highest every year.

The *Sub City* shopping centre has just opened in Srebreno a little outside of Dubrovnik, giving the city a new supply of retail. It covers a surface of 14,000 m^2. It is a smaller shopping centre with only big retailers occupying the mall. With two new shopping centres coming to Dubrovnik, the competition will be big and Sub City will at some point lose due to their size and location. A South African Fond has bought Sub City.

Two new shopping centres have long been planned in the port of Gruž in the city of Dubrovnik, but problems between partners, investors and the local authorities keeps the project undefined. The shopping centres are planned on a first-class and prominent location as a part of a new and modern bus and cruising terminal. One of the centres will cover a surface of 20,000 m2 and be invested by the Turkish company Global Ports Holding and the French construction group Bouygues Batiment International S.A. The infrastructure is first-class with all necessary facilities and the shopping centre will be located within the city with possibilities of further expansion. There is a large seasonal income and strong purchasing power of foreign visitors. This will strengthen the purchasing power of Dubrovnik in comparison to other cities in Croatia.

The disadvantages are the difficulties for the logistic retailers to come through, due to the traffic isolation in Dubrovnik. The hypermarkets will occupy the largest area with a surface of app. 4000 m^2. The second largest Croatian food chain Interspar, has no logistics south from Makarska, therefor it is necessary for Dubrovnik to build a new logistic park in Dalmatia. The competition in the smaller business centers in Gruz are: *Tommy hypermarket*, retail chains *Takko Fashion*, *Magic Baby*, *Planet Shoes*, surface 2500 m^2. Downtown with retail: *Deichmann*, *DM*, *Minčeta center* and *Atlant business center*.

OFFICE MARKET

In Dubrovnik there are A-class offices in the Grave business centre in the port of Gruž covering a surface of 3,600 m^2.