PRESS RELEASE

Challenging times for homebuilders and real estate companies

Hong Kong S.A.R, February 26, 2024 – Construction and real estate sectors are among the most cyclical sectors. Sensitive to changes in the labour market, prices in commodities and, first and foremost, the interest rate environment and accessibility of credit, they are currently under strain. And things are unlikely to get any better in 2024.

Homebuilders are seeing some fractures

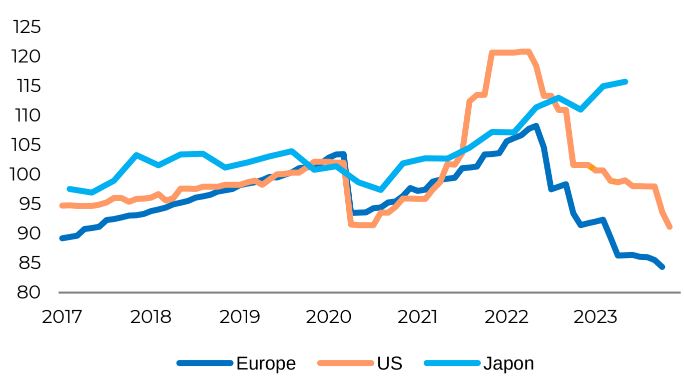
The residential market is facing a **double constraint**, on both supply and demand. The **rise in interest rates** has resulted in a rapid deterioration of demand, as households cannot afford to buy houses, especially as home prices had gone up.

Added to this is a **global shortage of labour**, the biggest impediments to construction cited by European companies from 2021 to late 2023[1]. This is echoed in the United States where job openings in construction are almost 30% higher than before the pandemic, and in Japan where 60% of construction companies mentioned shortage of labour according to a 2022 survey[2].

All these initial supply-side issues, along with the rapid increase in interest rates over the past two years, have resulted in **construction costs rising** from all avenues: materials prices have gone up, wage pressures have intensified, and financing costs have skyrocketed.

High interest rates challenging commercial real estate companies

Commercial property prices in key markets



Index : 2019 = 100 - Sources: Greenstreet, Bank of International Settlements, Coface.

Commercial real estate companies – who are mainly active in non-residential segments such as industrial, office and retail – have been **particularly sensitive to the plights of previous years** with retail space challenged by lockdowns and the acceleration of e-commerce, whereas the office segment is still adapting to hybrid work that has resulted in **lower and**

1 Source: ECOFIN, Coface
2 https://www.statista.com/statistics/1113127/japan-full-time-employee-labor-shortages-among-companies-by-industry/

changing demand for working spaces. Office vacancy rates were the highest in more than 15 years at 20.2% in Q1 2023 in the US and back to 2016 levels in Europe at 7.5%.

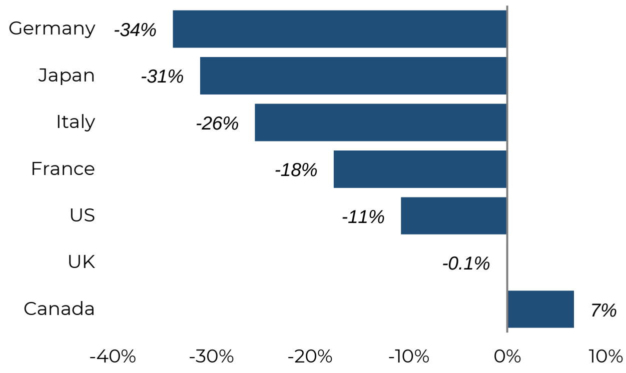
High interest rates pose challenges for real estate companies from different avenues, with the most obvious and immediate impact being a **slowdown in both the number of property transactions and their overall value**. In the current environment, this is already visible with the volume of commercial property transactions in Europe more than halving over the past year and at its lowest level since 2010. On top of this, the second avenue is interest costs which have been rising rapidly over the past two years.

Outlook 2024: towards home prices fall in advanced economies

The real estate market is still navigating a **delicate balance between high interest rates and a limited housing supply**.

Although house prices have adjusted somewhat to higher rates, the **persistent supply constraints** (caused by prospective sellers' unwillingness to move from their low mortgage rates or sell at a lower price) have kept them buoyant in 2023.

Expected change in real residential prices between 2023 and 2024



Source: National sources, BIS, Macrobond, Coface

The year 2024 should mark a turning point in this dynamic, with **price falls forecasted in the majority of advanced economies** (34% in Germany, 31% in Japan) from a buyers' perspective.

At the same time, the challenging landscape of commercial real estate is compelling certain companies to resort to drastic measures such as selling off assets. **Heading into 2024, commercial real estate prices have already plummeted by 25%** from their peak. Notably, there have been high-profile instances of prominent buildings being sold at over 50% discounts, underscoring the dire straits some companies find themselves in amidst the current economic climate.

In 2024, we anticipate a year of mixed fortunes, assisted by a **welcomed decline in policy rates. Yet, amidst this backdrop, concerns still persist**. With a portion of existing debt already locked in at fixed rates and lending margins for new loans at their lowest in over a decade, the pressing question looms: will anticipated rate cuts prove adequate and timely enough to shore up a market showing signs of weakness?

Find the full publication [here]()

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