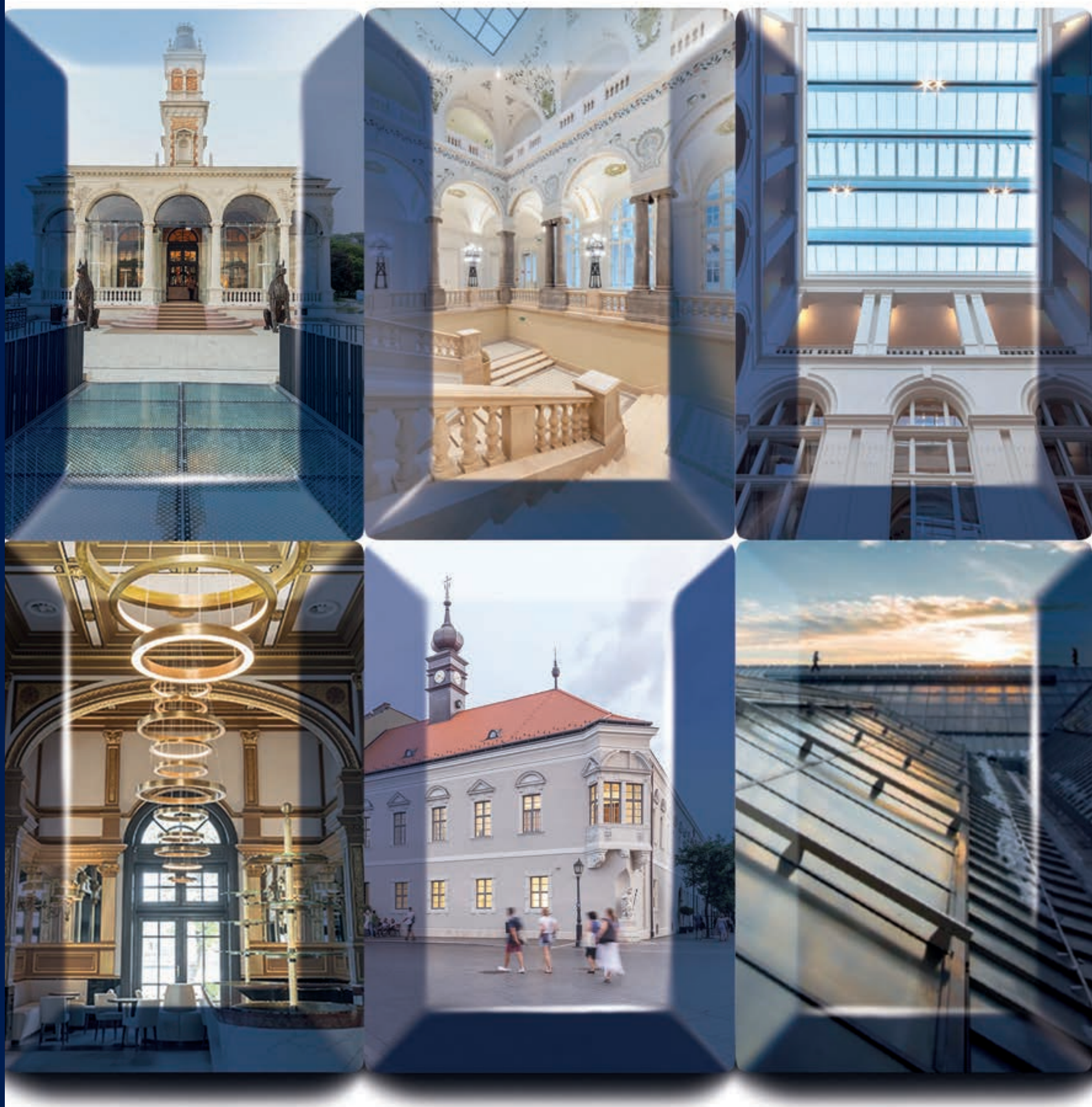
COMMERCIAL REAL ESTATE MARKET REPORT



2022

APRIL

“Your actions preserve you for the future.”

Miklós Ybl

COMMERCIAL REAL ESTATE MARKET REPORT

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The commercial real estate (CRE) market is of great importance, as it influences all sectors of the economy while also playing an important role in people's everyday lives. In light of this, the Magyar Nemzeti Bank analyses the development of the CRE market in this report, which is published biannually.

The following two factors are decisive for the analysis of commercial real estate:

I. On the one hand, commercial real estate is a fixed asset used by economic agents as a production factor; therefore, its value is influenced by the interplay of supply and demand for this asset.

II. On the other hand, commercial real estate is an investment vehicle: investors purchase such assets to realise a yield premium – over and above the available risk-free return – on the cash flow from utilising the real estate and/or the increase in value, while taking extra risk in the process.

Consequently, in addition to supply and demand trends, investor expectations are a key determinant in the value of commercial real estate, similarly to financial markets. Furthermore, developments in the CRE market also affect the functioning of the financial system. This is primarily due to the fact that most of the credit institutions' corporate loan portfolios are CRE-collateralised loans, accounting for almost 40 per cent of the portfolios in Hungary in 2021.

As such a large amount of bank assets are CRE-collateralised, there is a strong relationship between CRE values and the credit cycle. During an economic upturn, a positive feedback loop may develop between rapid growth in real estate values and lending, which can lead to excessive lending and fuel borrowing for real estate speculation. In an economic crisis, banks' non-performing loans burden institutions' capital adequacy, resulting in a reduction in credit supply. As seen in the 2008 crisis, the commercial real estate market plays a major role in banks' pro-cyclical behaviour. Moreover, corrections in CRE prices affect future investments and thus the real economy, which affects the operating environment of banks. A decrease in commercial real estate values generates losses for banks and institutional investors with large CRE stocks and contributes to financial instability.

Consequently, the CRE market can negatively affect the stability of the financial system via multiple channels, and thus it is of the utmost importance for the Magyar Nemzeti Bank as a macroprudential authority to monitor and thoroughly analyse the commercial real estate market.

The Commercial Real Estate Market Report aims to provide an overview of the underlying economic processes and the system of interactions between economic agents. Consequently, this report represents a unique central bank publication at the international level due to its integrated presentation of the macroeconomic and financial stability aspects of the commercial real estate market. The set of information used by the publication includes the following:

- *The presentation of the macroeconomic environment influencing the CRE market is based on the information in the MNB's Inflation Report.*[1] *Key statistical variables relevant to the CRE market include changes in the volume of gross value added, employment trends, changes in retail sales and changes in the yield environment.*

- *The analysis of current commercial real estate market developments relies primarily on information provided by real estate consulting firms. The analysis of developments in the commercial real estate market is presented by market segments (office market, retail market, industrial-logistics market, hotel market), but due to the capital city-focused market structure the bulk of the data is limited to Budapest. A micro-database is available to monitor construction projects.*

- *The analysis of the CRE financing market relies primarily on balance sheet data from credit institutions and the interest statistics collected by the MNB; information on the qualitative features of lending developments collected in the Lending Survey*[2] *is also used.*

[1] Magyar Nemzeti Bank, Inflation Report https://www.mnb.hu/en/publications/reports/inflation-report
[2] Magyar Nemzeti Bank, Lending Survey https://www.mnb.hu/en/financial-stability/publications/lending-survey

Contents

1 Executive Summary

Exceeding expectations, the Hungarian economy grew by 7.1 per cent in 2021, which puts it in the first third of the European recovery ranking. The favourable economic trends seen at the end of the year continued in early 2022 as well. However, prospects for the next quarters have deteriorated due to the Russo-Ukrainian war and the sanctions imposed. Future developments in geopolitical tensions represent an uncertainty for domestic and international economic performance, and already have a negative impact on demand for commercial property, appetite for property development, financing conditions and property investment decisions over the short run. If the Russo-Ukrainian war drags on, the downside risks to growth and upside risks to inflation will strengthen in the medium term as well. The performance of corporations in the service sector and construction was already hindered before the conflict, primarily by the shortage of labour and raw material. Looking ahead, further growth in corporate and construction costs can be expected, which may also result in the postponement of investments, while at the same time the accelerating inflation and the uncertainty caused by the war may reduce demand.

In 2021, the vacancy rates in the Budapest office market and the industrial-logistics market increased by 0.1 and 1.2 percentage points to 9.2 per cent and 3.2 per cent, respectively. Stagnation of this indicator in the office market was primarily attributable to the low volume of new completions resulting from postponements and to moderate demand, while the vacancy rate for the industrial-logistics segment rose as a combined result of the large volume of new completions and strong rental demand. The vacancy rate in the retail segment generally stagnated, but in the case of primary shopping centres in Budapest it rose by 2.5 percentage points to 6.5 per cent. In the office and industrial-logistics segments, the anticipated high volumes of new completions point in the direction of further rise in vacancy rates. However, rising construction material prices and supply problems, which have been further exacerbated by the war, represent a mounting risk for the timely completion of property developments. Average rental rates typically remained stable, and a moderate increase was also observed in the case of industrial-logistics properties and primary shopping centres in Budapest. Domestic hotel turnover improved in 2021, but the sector's revenues still fell short of the 2019 figure by 51 per cent. Plans for 2022 foresee the completion of almost 2,500 new hotel rooms, although delays are likely to occur in this segment as well. According to market experts, based on the assumption of a future recovery in tourism, the hotel developments are justified; nevertheless, the war may cause yet another shock for the tourism sector, though the degree and persistence of this remains uncertain.

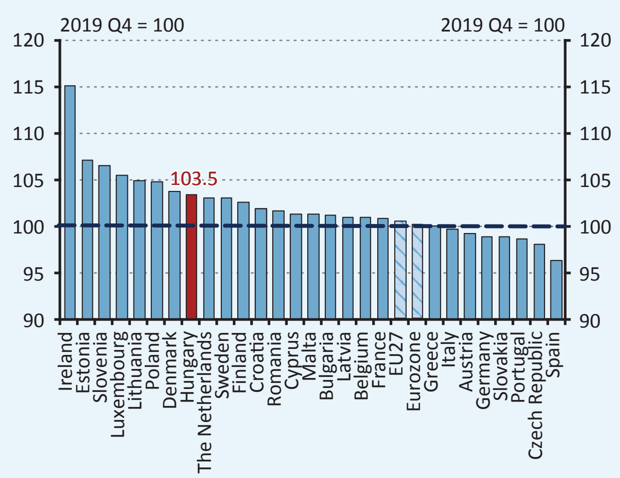
In 2021, the investment turnover of domestic commercial properties rose by 17 per cent to EUR 1.2 billion compared to the previous year, which is higher than the regional average. More than half (56 per cent) of this was generated by a few high-value transactions and 67 per cent of it related to domestic investors. The supply of investment products continues to be scarce, which results in falling yields. The monetary tightening cycle which has already started in several European countries and the world also reduces the yield premiums offered by property investments; however, the liquidity available maintains investors' interest in commercial property investments.

In 2021, credit institutions' project loan portfolio secured by commercial real estate expanded substantially, growing by almost 23 per cent on an exchange rate adjusted basis. In year-on-year terms, the ratio of foreign currency loans fell by 6 percentage points – supported in large part by the FGS Go! programme – and thus amounted to 78 per cent at the end of December 2021. In 2021, credit institutions' disbursements of project loans secured by commercial real estate was one third higher compared 2020. Almost half of the disbursements are linked to office buildings and shopping centres, while the highest growth (219 per cent) was observed in the amount disbursed to the hotel segment. Within that, disbursements for purchases registered the strongest increase (278 per cent) compared to the low base of 2020. At the end of 2021, 3.1 per cent of the project loan portfolio secured by commercial property was participating in the moratorium, which had been extended with a restricted scope from November; this is a much lower participation rate compared to the levels of over 40 per cent measured in 2021. Loans granted for hotel financing accounted for 65 per cent of the commercial property project loans participating in the scheme, while instalments were no longer suspended for any of the project loans in the industrial-logistics segment at the end of 2021. According to the Lending Survey, which was conducted in January 2022 before the outbreak of the war, no substantial change was registered in commercial real estate lending conditions at the end of 2021. On the other hand, according to the March 2022 survey, in addition to the deteriorating economic prospects resulting from the Russo-Ukrainian war and the ongoing increase in construction material prices, actors in the real estate market are experiencing a shortage in construction materials; as a result of all of this, they believe that credit institutions will significantly tighten financing conditions.

2 Office market

Exceeding preliminary expectations, the Hungarian economy grew by 7.1 per cent in 2021. The favourable economic trends seen at the end of the year continued in early 2022 as well. However, prospects for the coming quarters have deteriorated due to the Russo-Ukrainian war and the sanctions imposed as a consequence of it. In 2021, the vacancy rate of the Budapest office market stagnated overall and at the end of December it stood at 9.2 per cent. The stagnation was attributable to the low volume of new buildings, which resulted from postponed completions. According to the revised plans, in 2022 the volume of new completions may reach a record high, but the supply constraints and rising construction material prices represent a risk to the conclusion of construction projects. In 2021, annual rental demand in the Budapest office market rose compared to previous year, but it still falls short of the pre-crisis levels by more than one third. Despite the lacklustre demand, average offered rental rates in Budapest remained stable in 2021 as well, supported by the low annual volume of completions. Office market vacancy rates rose in most capitals in the CEE region. In terms of developments, the highest floor space of new office buildings in proportion to the stock (13.6 per cent) is under construction in Budapest, and thus vacant floor space may grow further when those appear in the market.

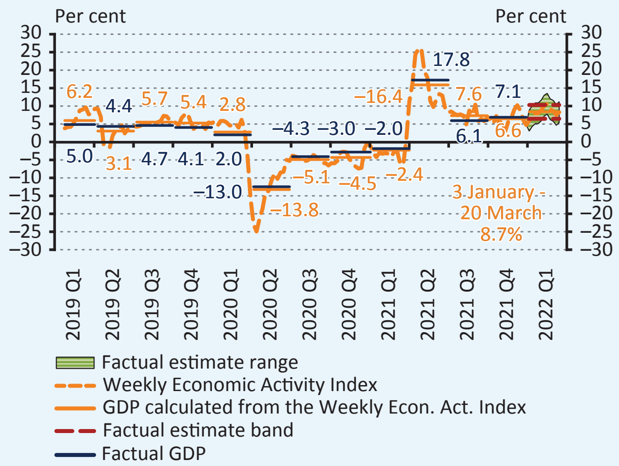
Chart 1
Development of GDP level in 2021 Q4 compared to the pre-crisis value (2019 Q4 = 100)



Note: Based on seasonally and calendar adjusted data.
Source: Eurostat, HCSO, MNB

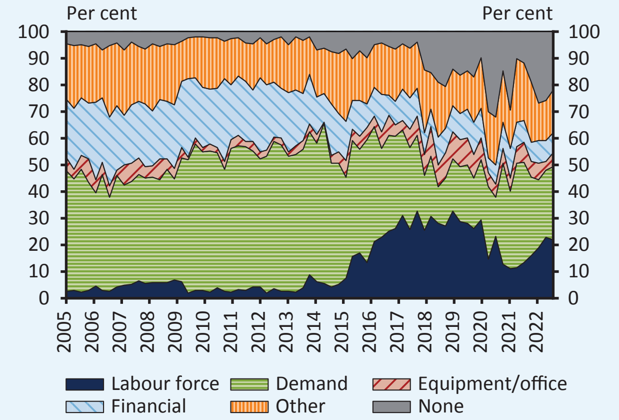
In 2021 Q4, GDP grew by 7.1 per cent in year-on-year terms, and economic output already exceeded its pre-crisis level by 3.5 per cent. Hungary's economic recovery is in the upper third of European Union ranking (Chart 1). With the exception of agriculture, the performance of all sectors of the national economy increased in year-on-year terms. Services' value added rose by 8.2 per cent, with the strongest (68.8 per cent) growth registered – due to the low base of last year – in the accommodation and catering sectors. In the fourth quarter, value added rose in most sectors that are critical for the commercial property market. Dynamic growth continued in the infocommunications sector. The performance of the trade and logistics, financial sector and manufacturing also reached the pre-crisis level. From the expenditure side, household consumption expenditure and investment rose by 8.2 per cent, and 3.2 per cent, respectively, in year-on-year terms. GDP growth in 2021 Q4 substantially exceeded market analysts' preliminary expectations.

Chart 2
Development of the Weekly Economic Activity Index, annual change



Source: MNB calculation

Chart 3
Factors limiting performance in the service sector



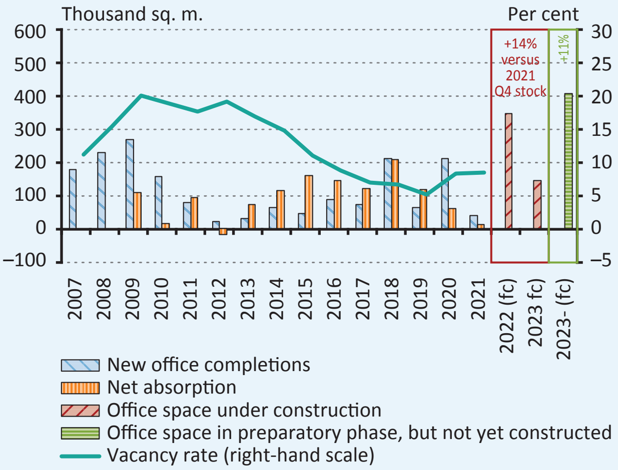
Source: European Commission

The economy has strong recovery potential, but growth is retarded by rising commodity and energy prices as well as by growing supply chain disruptions. Based on high frequency data, following the rapid recovery in 2021, the Hungarian economy expanded extremely dynamically again in early 2022 (Chart 2). However, the Russo-Ukrainian war and the sanctions undermine prospects for the coming quarters, and thus the MNB anticipates a deceleration in GDP growth this year. Based on the forecasts presented in the Inflation Report, growth this year may amount to around 2.5-4.5 per cent.[3] Future developments in geopolitical tensions entail substantial uncertainty with regard to Hungary's economic performance. If the war and sanctions persist, the downside risks to growth will also strengthen over the medium term. GDP growth is curbed by direct and indirect external trade impacts, as well as by further disruptions in international supply chains. Rising fuel and other commodity prices accelerate inflation, erode real wage growth and hamper corporate profitability.

The performance of corporations is mainly constrained by the shortage of labour and raw materials. In January 2022, employment reached a historic high, with the unemployment rate at 4.2 per cent. This is 0.8 percentage point lower than one year ago and is low by EU standards as well. According to the survey performed regularly among service sector companies, insufficient demand and labour shortage were the factors that hindered business the most in 2021 Q4 (Chart 3). Early this year, demand conditions deteriorated again in this sector, and labour force was already previously a bottleneck here. The ratio of corporations not reporting any factors hindering their performance declined. Similarly to the service sector, demand constraints also increased in construction at the beginning of the year (Annex, Chart 2). Looking ahead, the drastic rise in raw material prices results in increasing corporate costs, particularly in construction. In addition to rising raw material prices, corporations are also hit by increasing energy prices, which also affects the service sector. Accelerating inflation and the uncertainty caused by the war may lead to a fall in demand for the products and services of corporations.

[3] Magyar Nemzeti Bank, Inflation Report, March 2022: https://www.mnb.hu/en/publications/reports/inflation-report/24-03-2022-inflation-report-march

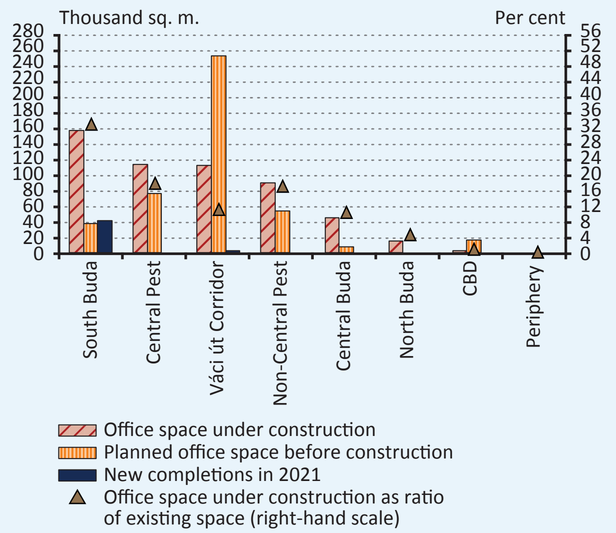
Chart 4
Leasing and development activity in the Budapest office market



Note: Some of the offices in the preparatory phase, but not yet under construction, may be completed in 2024 at the earliest, depending on when construction work actually begins. Based on data from the end of 2021. Net market absorption shows the change in the leased stock during the period under review. The difference between net absorption and gross demand is due to lease renewals, pre-leases and tenants leaving the market.

Source: Budapest Research Forum, Cushman & Wakefield

Chart 5
Distribution of Budapest office developments, renewal rate and new completions by sub-market



Note: Based on data from the end of 2021.

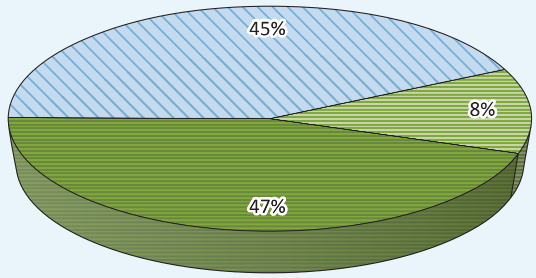
Source: Cushman & Wakefield

In 2021, the vacancy rate of the Budapest office market stagnated on the whole, but is expected to rise based on the demand level and anticipated completions. At the end of 2021, the stock of modern offices in Budapest amounted to 3.96 million square metres, which corresponds to the figure for the end of June 2021, as there were no new completions in the second half of the year. In 2021, the total volume of newly completed office space was 44,000 square meters, representing growth of 1.1 per cent, after a rate of 6.3 per cent in the previous year (Chart 4). The vacancy rate fluctuated between 9 and 10 per cent during the year, while the lack of new completions in the second half of the year reduced the rate to 9.2 per cent by the end of the year. On the other hand, developers' plans include high volumes of new completions in 2022 and 2023, which suggests growth in the vacancy rate, assuming that the demand levels observed in the previous quarters remain in place. No decline was observed in average office rents in Budapest in 2021 H2. The low volume of new completions prevented a decline in rental rates even in conjunction with poor demand. Looking ahead, a potential rise in the vacancy rate may put downward pressure on rents, but this is likely to be the case mainly for older properties with lower quality and services.

Construction of office space corresponding to 14 per cent of the existing modern office stock is under way, but supply chain disruptions and rising construction material prices hinder the progress of developments. At the end of 2021, office space amounting to 536,000 square metres was under construction in Budapest, 71 per cent of which is to be completed by the end of 2022 and the rest in 2023. That said, the timely completion of developments is adversely both by construction material supply problems and rising prices. The uncertainty related to office completion plans is highlighted by the fact that in 2021 only 28 per cent of the planned volume was actually completed. Of the total space under construction, 49 per cent had (pre-)lease contracts at the end of 2021. In addition to ongoing projects, the further development of almost 450,000 square metres may be launched shortly, which may boost the modern office stock registered at the end of 2021 in Budapest by another 11 per cent over the medium term. Examining the location of projects under construction by sub-markets, over the next two years the largest volume of new supply will be completed in the South Buda sub-market[4] (158,000

[4] For a detailed description of the Budapest office sub-markets, see Annex 1.

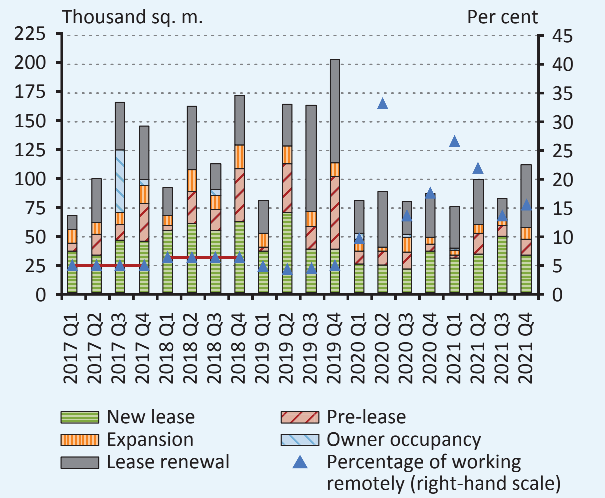
Chart 6
Composition of the modern office stock in Budapest according to green rating



Note: The green-certified office stock includes modern office buildings in Budapest with BREEAM or LEED certification.

Source: CBRE, HuGBC

Chart 7
Demand in the Budapest office market and the ratio of employees in intellectual occupations working remotely



Note: The three-month moving average of employees aged 15–74 working remotely at home as a percentage of those in intellectual occupations. For each quarter of 2017 and 2018, the annual rate of working remotely is shown, no quarterly data are available for these years.

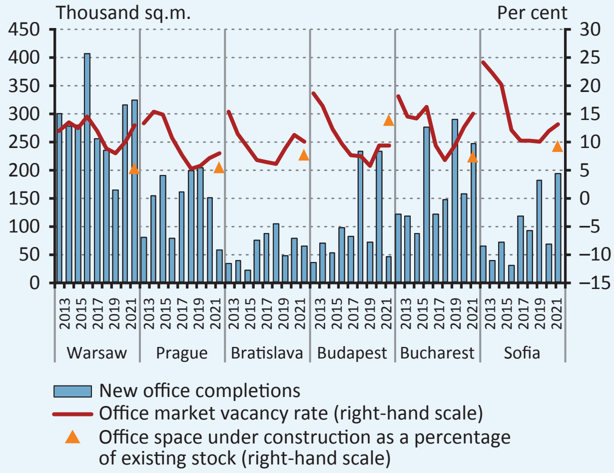
Source: CBRE, Cushman & Wakefield, HCSO

square metres), with a significant volume in progress in the Central Pest sub-market (144,000 square metres) and along Váci út (113,000 square metres) as well (Chart 5). Most of the developments that are not yet under construction, but could be launched in the foreseeable future, are concentrated on the Váci út office corridor. Active office developments and renovations in recent years have led to an increasing number of green office buildings in Budapest. At the end of 2021, more than half of the rental office stock was BREEAM or LEED certified (Chart 6). The establishment of sustainable commercial real estate is also supported by the MNB's Green Corporate Capital Requirement Discount Programme, a summary of which can be found in Box 1.

Amidst moderately increasing demand for offices, the ratio of those working from home is still relatively high. Although in 2021 total demand for office space exceeded the 2020 level by roughly 10 per cent, compared to 2018-2019 the decline still amounts to 32-40 per cent (Chart 7). In 2021, total demand for modern offices in Budapest amounted to 366,000 square metres, with contract renewals and new lease contracts each accounting for 40 per cent. The volume of the latter was particularly high in the third quarter, amounting to 49,000 square metres compared to 30,000-35,000 square metres in other quarters. In the first half of the year, net absorption measured by the change in the lease stock[5] was negative (-11,500 square metres), which then turned positive due to new lease contracts concluded in the third quarter. Total net absorption amounted to 14,000 square metres in 2021. In an environment marked by slightly growing, but moderate rental demand, working from home as a proportion of those in intellectual occupations remains at a relatively high level, at around 15 per cent, compared to the average of 5 per cent before 2020. In addition to teleworking, which also must be specified in the employment contracts, flexible or hybrid work offered by employers also raises the ratio of those working offsite, which substantially exceeds 15 per cent. The impact of teleworking on the office market was also discussed by the MNB and market experts; a summary is presented in Box 2.

[5] For definitions related to CRE demand, see Annex 2.

Chart 8
Development activity vacancy rates in the regional capital office markets



Source: MNB compilation based on CBRE, Colliers, Cushman & Wakefield and JLL data

In 2021, office markets in most CEE capitals featured rising vacancy rates. In 2021, vacancy rates rose in the office market of all CEE regional capitals except Bratislava and Budapest, reflecting lower demand and the market entry of new buildings resulting from the buoyant development activity in recent years (Chart 8). In Bratislava, the rate fell by 1.3 percentage points overall during the year, while it stagnated in Budapest. Once again, the lowest vacancy rate was registered in Prague (7.8 per cent) and the highest rate in Bucharest (14.9 per cent). At the end of 2021, in most capitals in the region construction of office space amounting to 5-7.5 per cent of the existing modern office stock was in progress. This ratio is higher only in Budapest (13.6 per cent) and Sofia (9.1 per cent). A rise in the vacancy rate is more likely in these latter capitals in 2022.

Box 1

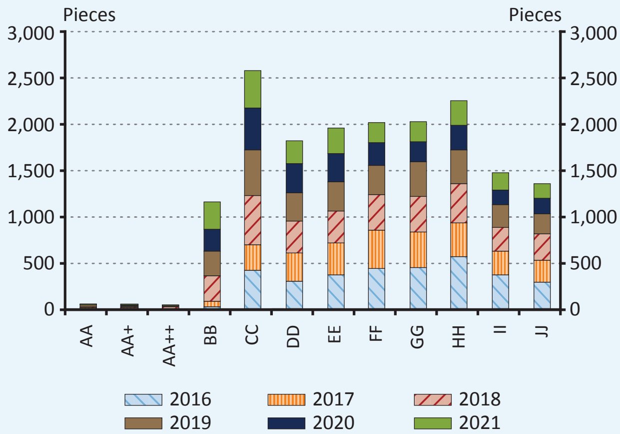
Supporting the greening of commercial real estate stock in the MNB's green corporate capital requirements discount programme

The energy modernisation of the Hungarian real estate portfolio is one of the most important steps in the greening of the Hungarian economy, both in the residential and industrial-commercial segments. In the case of commercial real estate, favourable market developments can be observed in the field of financing. A significant portion of the domestic green bond issues so far have been focused on the development of sustainable commercial real estate. However, the proportion of the stock that can be considered energy efficient can still be considered low: in the case of office properties, less than 8 per cent of the energy certificates issued since 2016 had a rating of at least BB. In order to strengthen the environmental sustainability of the economy and to manage the transition climate risks at the system level, the MNB considers it necessary to further improve the financing environment of sustainable commercial real estate in the Hungarian credit market.

In the spring of 2022, the MNB expanded the Green Corporate and Local Government Capital Requirement Discount Programme which was announced on 31 August 2021 to include the commercial real estate segment. Until then, green real estate loans supported by a capital requirement rebate were only available in the retail business, and thus the elaboration of the conditions for this amending measure had to be put on a new basis.

Utilising Hungarian expertise on the sustainable built environment, the central bank – in cooperation with the Hungarian Green Building Council (HuGBC) – developed the main parameters of the support factor. In order for Hungarian actors to become acquainted with the best practices accepted internationally and

Distribution of energy certificates for office properties by rating and year of issue



Source: Lechner Knowledge Center

to introduce uniform, predictable criteria systems at the EU level, the conditions for participation in the programme follow the structure of the EU Taxonomy.[6] Accordingly, with regard to commercial real estate, we also distinguish between green real estate loans for the construction of new real estate, the purchase of existing real estate and renovation.

The conditions for the capital requirement for commercial real estate can be met at three different levels:

- **Full compliance with EU Taxonomy:** The Taxonomy Regulation aims to classify businesses on the basis of their sustainability, thus setting out strict sustainability principles for the real estate and construction sectors, which play a key role in the transition to sustainability. As the principles and conditions laid down in the Taxonomy are quite ambitious, a 7-per cent capital requirement discount calculated on gross exposures can be applied to loans for the financing of properties that meet these conditions.

- **Compliance with conditions in line with Hungarian construction practices:** A framework of conditions that is more in line with Hungarian construction practices, but is still based on the EU Taxonomy, has also been developed, which can be more easily adapted for Hungarian actors. Credit instruments that merely finance less stringent properties that comply with the alternative framework shall entitle the participating credit institution to a lower discount of 5 per cent for that exposure.

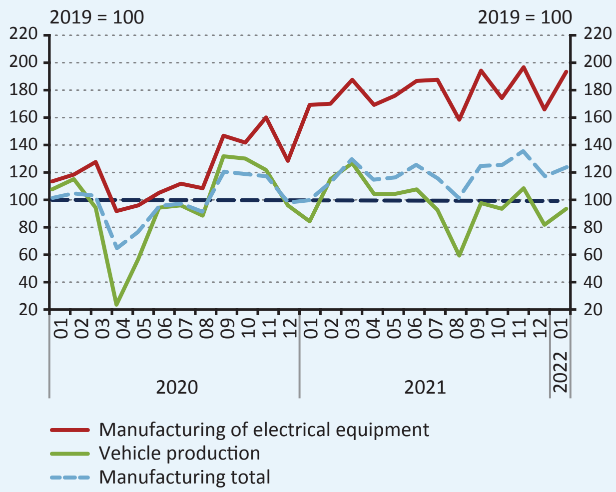
- **Compliance with Internationally Accepted Real Estate Rating Standards (BREEAM, LEED, DGNB):** A 5-per cent capital requirement discount may also be granted for credit exposures that are highly rated according to the assessment of internationally recognised and accepted green building rating systems. This option is primarily relevant for large corporate and project lending, as these standards have been part of the certification practice for large commercial properties for many years. These frameworks typically take a holistic approach, formulating sustainability requirements in several categories in accordance with domestic and international legislation. Compliance with the requirements is checked by accredited certifiers.

[6] Regulation (EU) 2020/852 of the European Parliament and of the Council of 18 June 2020 on the establishment of a framework to facilitate sustainable investment, and amending Regulation (EU) 2019/2088. Available at: https://eur-lex.europa.eu/legal-content/EN/TXT/?uri=CELEX%3A32020R0852
COMMISSION DELEGATED REGULATION (EU) supplementing Regulation (EU) 2020/852 of the European Parliament and of the Council by establishing the technical screening criteria for determining the conditions under which an economic activity qualifies as contributing substantially to climate change mitigation or climate change adaptation and for determining whether that economic activity causes no significant harm to any of the other environmental objectives. Available at: https://eur-lex.europa.eu/legal-content/EN/TXT/?uri=PI_COM:C(2021)2800

3 Industrial-logistics market

In 2021, industrial production rose, but the growth may be hindered and investments postponed because of the war, the renewed increase in supply chain disruptions and rising costs. The vacancy rate in the industrial-logistics market in Budapest and its environs advanced 1.2 percentage points in 2021 and thus reached 3.2 per cent at the end of the year, which is still a very low level both in historical terms and by international standards. In terms of new completions, 2021 was yet another record year as these amounted to 339,000 square metres compared to the volume of around 100,000 square metres registered in previous years. At the end of December, 26 per cent of the new completions planned for 2022 were covered by pre-lease contracts, which falls substantially short of the ratio seen in previous periods. In 2021, strong demand for industrial-logistics properties was able to keep pace with new completions. Total demand rose by 18 per cent in annual terms, and net demand excluding renewals accounted for more than two thirds of the leases concluded. In the industrial-logistics market in Budapest and the agglomeration, rising demand and low vacancy rates helped rental rates remain stable, and a slight increase can even be observed. On the other hand, due to the uncertainty surrounding the sustainability of high demand, a correction in rental rates still cannot be ruled out in the medium term. According to information from market participants, the growing supply improves Hungary's competitiveness in the tenders invited by international lessees for logistics properties in the countries of the region.

Chart 9
Monthly development of manufacturing output (2019 = 100)

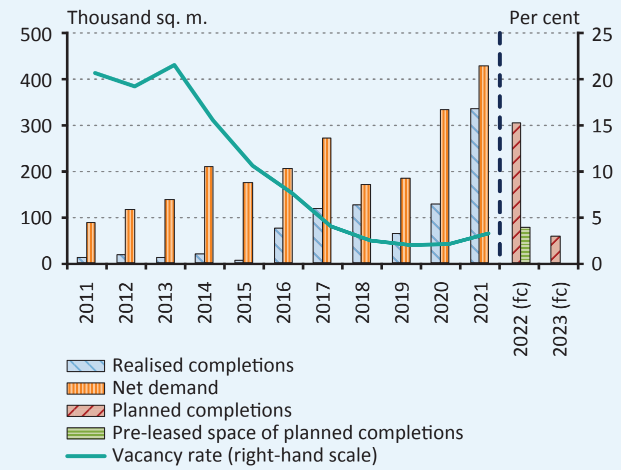


Note: Monthly average of 2019 = 100.
Source: HCSO

Industrial production rose, but the war is hindering growth via supply disruptions and rising costs and may also result in the postponement of investments. Industrial production has exceeded its pre-crisis level since November, but still falls short of the pre-crisis trend. According to January industrial production data, output rose in most manufacturing subsectors. The output of the automotive industry, accounting for the largest share, once again increased after a six-month decline calculated on an annual basis (Chart 9). In 2021 Q4, the volume of whole-economy fixed investments rose 0.2 per cent in year-on-year terms, while the majority of the sectors that have a bearing on the commercial property market were characterised by stronger growth than that. Investment in manufacturing, which represents the highest weight, increased by 16.7 per cent. Investment in the infocommunication sector rose 12.8 per cent, while investment in the trade and tourism-catering sectors rose moderately. On the other hand, investment in the construction and the financial and insurance sectors contracted. Investment activity in transportation and warehousing rose by 20.1 per cent. In addition to public infrastructure developments, investments by corporations engaged in passenger transport also supported growth. Looking ahead, rising corporate costs may result in the postponement of certain investments in the next quarters.

An increasing number of developments are starting in the industrial-logistics property market in Budapest and its environs, despite the lack of pre-lease arrangements. At the end of 2021, the stock of modern industrial-logistics

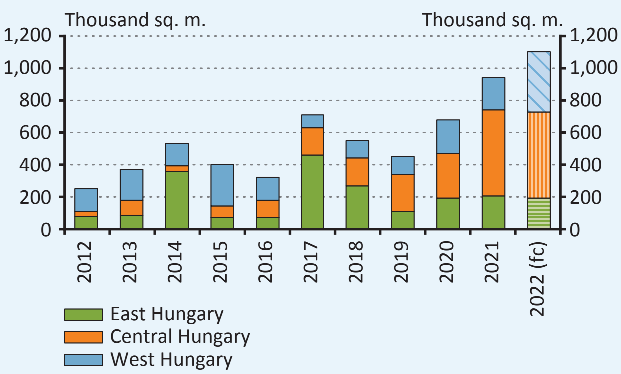
Chart 10
New completions, net demand and vacancy rate in the industrial-logistics market of Budapest and its environs



Note: Based on data from end of 2021.

Source: Budapest Research Forum, Cushman & Wakefield

Chart 11
Industrial-logistics completions and planned completions for 2022 in Hungary



Note: Central Hungary includes the developments in Budapest and its agglomeration. Planned completions for 2022 are based on data from end-2021.

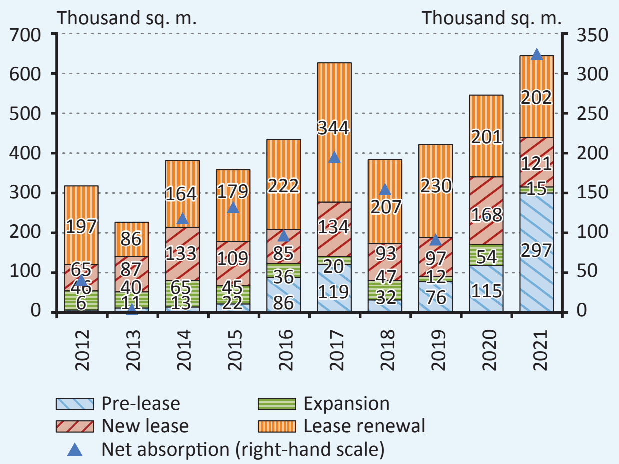
Source: CBRE

properties in Budapest and its agglomeration monitored by the Budapest Research forum amounted to 2.73 million square metres. The vacancy rate of the segment rose by 2 percentage points in the first half of the year, followed by a decline of 0.8 percentage point in the second half of the year, and at the end of December 2021 the rate stood at 3.2 per cent (Chart 10). Despite this rise, the rate can still be deemed very low. Development activity has increased substantially over the last two years, with new players also entering the industrial-logistics development market, and in 2021 several developments commenced even without a concluded (pre-)lease contract. During the year, 339,000 square metres of industrial-logistics area was completed in Budapest and its environs, which is a historic high and exceeds the 2020 figure by a factor of 2.7. In 2021, 64 per cent of new supply was covered by pre-lease even before completion. Based on the data of developments in progress, in 2022 new supply once again may exceed 300,000 square metres, 26 per cent of which was covered by pre-lease contracts at the end of 2021.

Industrial-logistics development activity is also strong at the national level, with 1.1 million square metres expected to be completed in 2022. At the end of 2021, the national stock of industrial-logistics real estate was around 11.2 million square metres. In 2021, 935,000 square metres of new space was completed in the first half of the year, including buildings completed in Budapest and its environs (Chart 11). When examining new completions outside Budapest (596,000 square metres), new areas were almost equally distributed among the West, Central and East Hungary regions. Based on data for projects in progress, 1.1 million square metres of industrial-logistics real estate is expected to be completed nationwide in 2022. In terms of the regional composition, in 2022 new completions in West Hungary are expected to rise by 89 per cent compared to previous year.

A strong rise in industrial-logistics demand – mainly driven by logistics service providers – was characteristic of 2021. During the year, lease agreements were concluded for 636,000 square metres of industrial-logistics space on the market for Budapest and its environs (Chart 12), up 18 per cent and 53 per cent on the total figures recorded for 2020 and 2019, respectively. Growth in net demand excluding renewals was even more spectacular: the contract portfolio covering 433,000 square metres in 2021 exceeded that of 2020 and 2019 by 29 per cent and 134 per cent, respectively. Rental demand was dominated by pre-lease contracts at 47 per cent, followed by renewals at 32 per cent, new leases at 19 per cent and expansions at 2 per cent. In 2021, net absorption measured by the change in

Chart 12
Customer demand by contract type in the industrial-logistics rental market of Budapest and environs



Source: Budapest Research Forum, Cushman & Wakefield

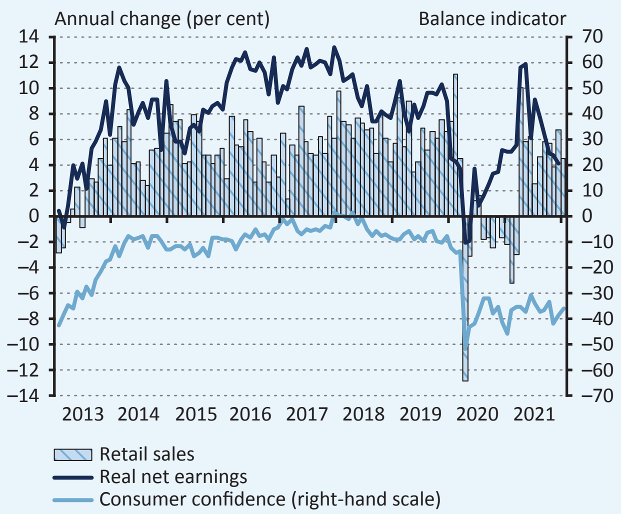
leased office stock rose by two and a half times compared to 2020 and by three and a half times compared to 2019 and exceeds even the record high registered in 2017 by two thirds. The logistics service sector remains the most active actor in the industrial-logistics rental market, accounting for 61 per cent of total lease volume in 2021 (Annex, Chart 14).

Strong demand and low vacancy rates kept rental rates stable and even drove a modest increase. Typical offered rental rates at end of 2021 were in the range of EUR 4.4-4.95 per square metre per month. Expectations of a correction in rental rates, based on the strongly increasing volume of property developments in recent periods, did not materialise, and in 2021 even a moderate rise was registered in typical rental rates (Annex, Chart 15). However, related to the previously unseen, strong demand, it is questionable how long the current level can be maintained, and thus a potential correction in rental rates still cannot be ruled out over the medium term.

4 Retail market

In 2021, retail turnover stabilised at higher level than seen before the pandemic, but still fell short of the growth trends observed in past years. Real wages rose by 3.4 per cent, but consumer confidence was at a relatively low level throughout the year. The vacancy rate of domestic shopping centres typically stagnated in 2021, with some increase in the Budapest primary centres in the second half of the year. Retail rental rates also remained stable in 2021, while some increase in rents was registered – after the fall in 2020 – in the case of Budapest's primary shopping centres and high streets. After 10 years, a new shopping centre was opened in Budapest in September 2021. Looking ahead, the implementation of planned retail developments is surrounded by uncertainties. Of the physical retail stores, turnover in furniture, technical goods, textile, clothing and catering fell short of the 2019 level by 10-17 per cent, while together with e-commerce channels the turnover of most merchandise groups increased. After the lifting of the epidemiological restrictions on 7 March 2022, retail and catering turnover may rise further, while the increasing interest environment, rising inflation and deteriorating growth prospects resulting from the war may curb consumption. The continued increase in energy prices and depreciation of forint raises lessees' costs in all real estate segments, while the exchange rate effect – through EUR-denominated rental rates – may give rise to difficulties mostly in the retail segment, as it tends to have less export revenue.

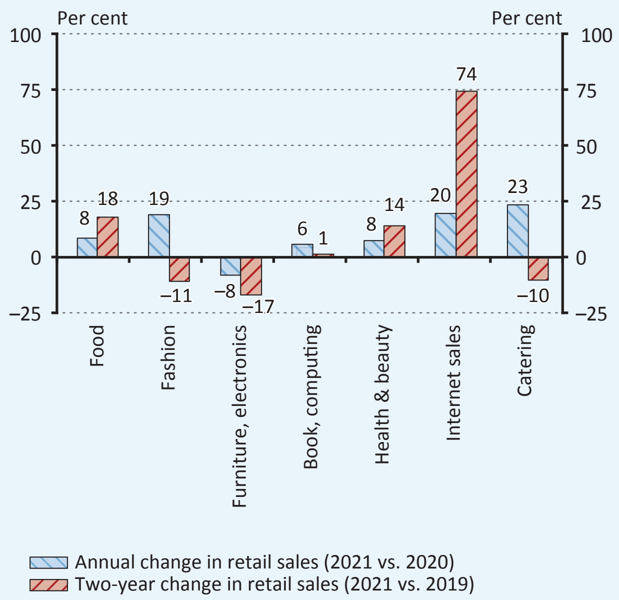
Chart 13
Development of retail sales, incomes and the consumer confidence indicator



Source: European Commission, HCSO

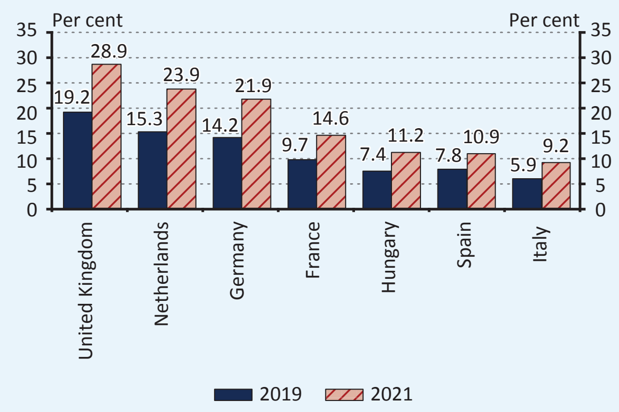
Retail sales stabilised at a higher level than before the crisis, but still fell short of the growth trends from past years. Of the macroeconomic factors that influence consumption expenditures the most, annual growth in the real net wage bill continued, averaging 6.8 per cent per month in 2021 (Chart 13). The consumer confidence index stagnated during the year on the whole and remained at a low level. The positive impact of the favourable income trends on retail trade may be curbed by several uncertainty factors in 2022.

Chart 14
Development of turnover of retail store types and restaurants



Source: HCSO

Chart 15
Share of online commerce in total retail sales in Europe

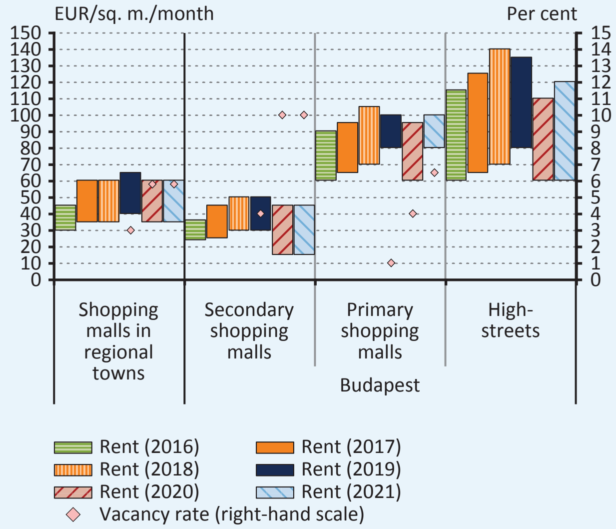


Note: Proportion of online retail sales within total retail sales excluding automotive fuel, automotive and vehicle parts.
Source: Centre for Retail Research, HCSO

The increasing interest environment, inflation and deteriorating growth prospects resulting from the war may curb consumption. In 2021, of the main retail store types, turnover in furniture and technical goods declined (by 8 per cent) compared to the previous year (Chart 14). Versus 2019, i.e. before the pandemic, in addition to furniture and technical goods, turnover in textile and clothing as well as in catering fell short of the level registered 2 years ago. Looking ahead, the tightening monetary conditions, increasing inflationary pressure and the negative impacts of the Russo-Ukrainian war on economic growth may reduce consumption.

Turnover in online retail channels rose further across Europe. Growth in the share of mail order and internet sales channels, fuelled by the outbreak of the pandemic in 2020, continued, and thus in Hungary it rose within retail sales volume – excluding automotive fuel, cars and automotive parts – from 7.4 per cent measured in 2019 to 11.2 per cent in 2021 (Chart 15). In a European comparison, the share of online sales has traditionally been the highest in the UK, where it rose from 19.2 per cent in 2019 to 28.9 per cent in 2021. High ratios of 22-24 per cent are measured in the Netherlands and Germany, while in France online sales channels accounted for 14.6 per cent of the retail sales volume. Of the Mediterranean countries, in Spain and in Italy, the ratio of internet sales is close to that observed in Hungary, at 10.9 and 9.2 per cent, respectively.

Chart 16
Retail rental rates and vacancy rates in Hungary



Note: The rental rate data refer to a retail unit of 100 square metres, and the columns show the dispersion of the highest rental rates for real estate in different retail property types.

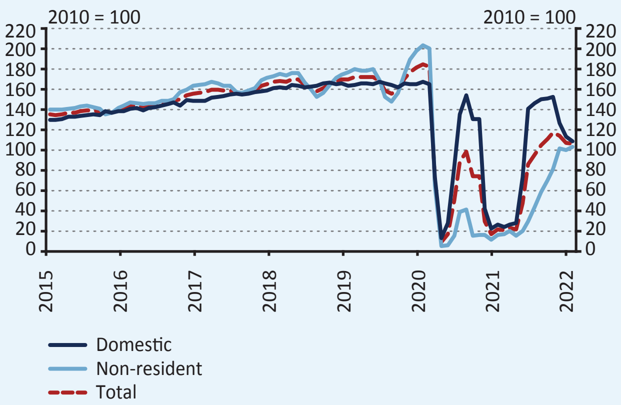
Source: CBRE

Retail rental rates remained stable in 2021, and some correction even occurred for certain property types compared to the decline in 2020. In 2021, the rental rates of retail properties stopped declining, and in the primary shopping centres in Budapest, offered rental rates once again stayed in the bands observed in 2019. In the case of the latter, rental rates for retail units of around 100 square metres have been in the range of EUR 80-100/ square metre/ month, while in the shopping centres in larger towns of Hungary retail units with a space of such size may be leased for EUR 35-60/square metre/month (Chart 16). After a long pause supply also grew: in 2021 H2 a new shopping centre was completed in Budapest, which increased the stock by 55,000 square metres. The vacancy rate of primary shopping centres in Budapest rose in the span of one year from 4 per cent at the end of 2020 to 6.5 per cent, while in the secondary centres in Budapest and in the centres of regional towns, the average vacancy rate remained 10 and 6 per cent, respectively. Looking ahead, implementation of the planned retail developments is surrounded by uncertainties. The continued increase in energy prices and depreciation of forint raises lessees' costs in all real estate segments, while the exchange rate effect – through EUR-denominated rental rates – may give rise to difficulties mostly in the retail segment, which has lower export revenue.

5 Hotel market

A slow recovery in the tourism sector poses a challenge for hotels and boosts uncertainty with regard to the implementation of additional developments. The revenues of domestic hotels rose by 26 per cent in 2021, but still fall a significant 51 per cent short of the revenues registered in 2019. At the national level, the number of overnight stays in 2021 was down 55 per cent versus 2019, while compared to 2020 an increase of 11 per cent was registered. Market experts are of the opinion that Budapest's hotel supply is low, and the planned volume of development is justified by the return of tourists. On the other hand, the war may cause yet another shock for the tourism sector, while the degree and length of the shock is uncertain for the time being. Russia was the fifth largest inbound market for domestic tourism in 2021 in terms of the number of overnight stays spent in hotels by foreign visitors, with Russian guests accounting for nearly 5 per cent of all foreign nights and Ukrainian guests for 3 per cent. In the capitals of the CEE region – similarly to Budapest – occupancy rates improved in 2021, but they are still only half of the pre-pandemic levels.

Chart 17
Monthly guest nights in commercial accommodation establishments

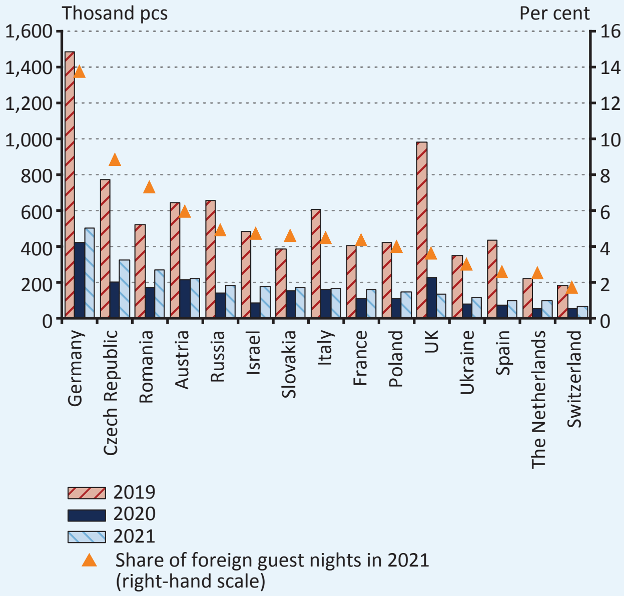


Note: Based on seasonally adjusted data. 2010 monthly average = 100.
Source: HCSO

From 7 March 2022, all epidemiological restrictions were lifted in Hungary. Restrictive measures on events and all restrictions that made the use of a service subject to an immunity certificate have been cancelled. Restrictions on entry into the territory of Hungary have also been lifted.

A slow recovery in international tourism poses a challenge for hotels and increases uncertainty with regard to additional developments. For Hungary as a whole, in 2021 the number of guest nights was down 55 per cent versus 2019, whereas an increase of 11 per cent was registered versus 2020. Passenger traffic at the Budapest Liszt Ferenc International Airport also started to rise in 2021 H2 and reached roughly half of the pre-pandemic level in the final quarter (Annex, Chart 7). The number of domestic overnight stays fell at the end of 2021 compared to the previous quarter and the rise in foreign tourism also halted in December (Chart 17). The recovery of international tourism may take years, and the speed of the recovery of foreign tourism is made even more uncertain by the geopolitical situation that developed in early 2022.

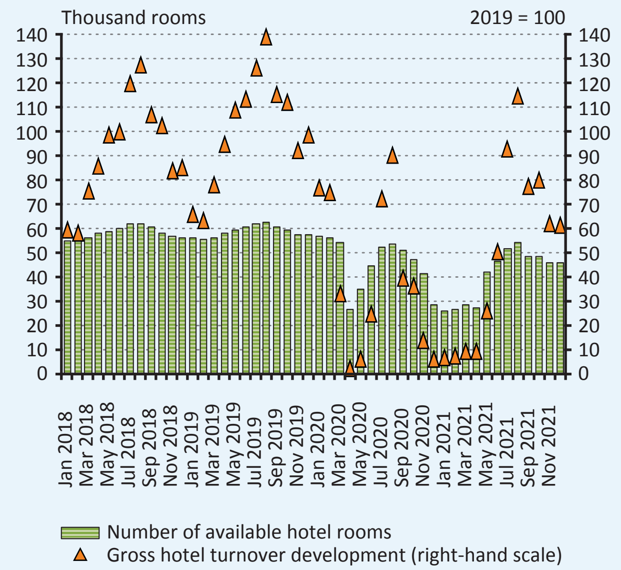
Chart 18
Number and distribution of foreign guest nights in domestic hotels by country



Note: The figure shows the 15 most significant countries, which together accounted for 75 per cent of foreign guest nights in 2021.

Source: HCSO

Chart 19
Domestic hotel capacity and development of gross turnover



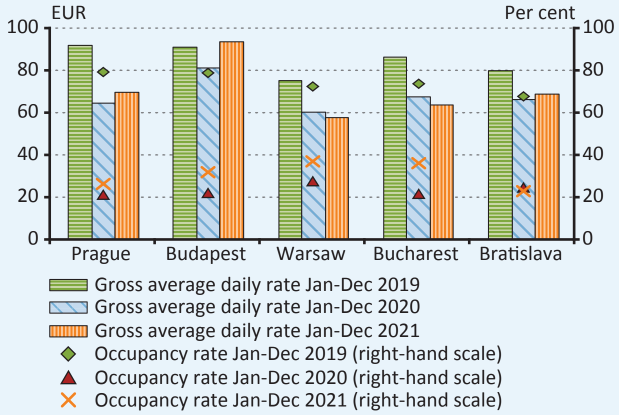
Note: In case of the gross hotel turnover development average of 2019 = 100.

Source: HCSO

In addition to the pandemic, the Russo-Ukrainian war may also have an adverse effect on tourism in terms of domestic accommodation. The renewed increase in the number of foreign guests after the pandemic-induced fall may be curbed by the Russo-Ukrainian war in 2022. Russia was the fifth largest inbound market in terms of the number of overnight stays spent in domestic hotels by foreign visitors in 2021, with Russian guests accounting for nearly 5 per cent of all foreign guest nights and Ukrainian guests for 3 per cent (Chart 18). In addition to the loss of Russian and Ukrainian visitors, the interest of travellers from other countries in Hungary and in region may also decline due to Hungary's proximity to the war.

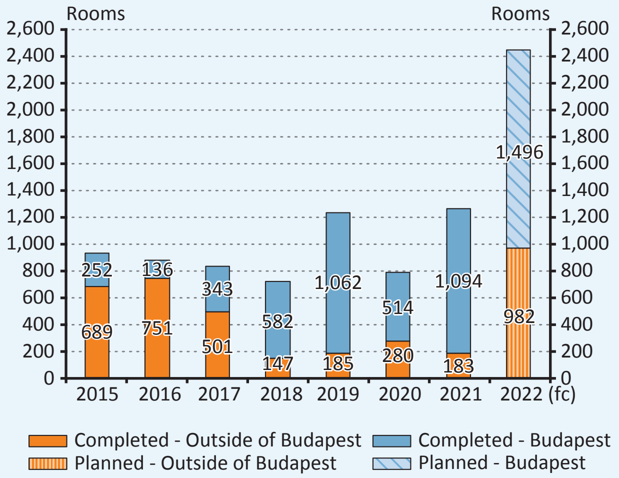
Domestic hotels' turnover rose in 2021, but still falls significantly short of the turnover registered in 2019. In 2021, the revenues of domestic hotels exceeded the level of 2020 by 26 per cent, while falling short of the 2019 figure by 51 per cent. Due to the third wave of the coronavirus epidemic, in the first four months of 2021 monthly revenues fell short of the average monthly turnover of 2019 by more than 90 per cent. A rising trend commenced in May 2021 and revenues in August already exceeded the monthly average of 2019 by 14 per cent and fell short of the August 2019 figure by 18 per cent, which is a relatively small degree in the light of the previous periods (Chart 19). The number of available hotel rooms in the months less exposed to the spread of the pandemic was still 15-20 per cent lower than in the same period of 2019, but in the first four months of 2021 more than half of the hotels were closed. Both in 2020 and 2021 hotels typically fully closed down as a result of the low number of guests and often prepared for the return of guest with some minor or major renovation. In 2021, the number of overnight stays in hotels fell short of that two years ago in all areas of Hungary. The loss of guest was the most pronounced in Budapest, where a decline of 71 per cent was registered compared to 2019 (Annex, Chart 8).

Chart 20
Average performance indicators of hotels in the region's capitals in 2019-2021



Source: CBRE, STR Global

Chart 21
Number of completed and planned hotel rooms in Hungary



Note: Completions planned for 2022 are based on data from the end of 2021.

Source: CBRE, Cushman & Wakefield, Hungarian Hotel & Restaurant Association

In the CEE region, occupancy rates improved in 2021, but are still at only half the pre-pandemic levels. In 2021, hotel room occupancy in the capitals of the region was around 22-37 per cent, down 50-70 per cent compared to 2019 (Chart 20). The highest room occupancy rate in the region was achieved by hotels in Warsaw (37 per cent) and Bucharest (36 per cent). As regards the average gross room price, hotels in Budapest are the most expensive in the region at EUR 93.4, which exceeds the average of the region by 32 per cent. In 2021, hotel room rates rose, in addition to Budapest, in Prague and Bratislava, by 15, 8 and 4 per cent, respectively, but the 2019 price level was exceeded only in Budapest.

The hotel sector is preparing for the return of tourists by boosting completion volumes, but the war increases the sector's level of risk. In 2021, 10 new hotels were completed nationwide, with a total of around 1,300 rooms (Chart 21). Six of the completed hotels are located in Budapest, and 86 per cent of the completed rooms were concentrated in the capital. The hotel developments in progress will result in significant new completions in the coming periods as well: almost 2,500 hotel rooms are being constructed, to be completed in 2022, and 60 per cent of those are in Budapest. Market experts believe that Budapest's hotel supply is low, and the planned volume of development is justified by the anticipated return of tourists. On the other hand, the war may cause yet another shock for the tourism sector, while the degree and length of it is uncertain for the time being.

Box 2
Impacts of the Russo-Ukrainian war on the property market and construction

With a view to monitoring property market trends and identifying potential risks, the MNB deems it important to consult market participants. Consultation with the construction industry and property developer federations, real estate developers and investors was organised in March 2022. Participants discussed the current situation and trends in the commercial real estate market, specifically addressing property developments, the increase in construction material prices and the impacts of the Russo-Ukrainian war.

Construction industry

Property market experts believe that the trends in construction orders by the state and the situation of the budget will be an important issue looking ahead. In 2021, 65 per cent of the construction orders came from the government sector, and thus the capacity available to the private sector was much lower. However, at present the interest environment is rising, thereby increasing the costs of finance. In addition, there are also some uncertainties in respect of the timing and degree of the absorption of EU funds. Experts feel that due to the current war situation, in addition to the steep drop in GDP dynamics observed early this year and persistently high inflation, there is also a real chance of stagflation.

Construction profitability in 2021 was worse than in 2019. On the demand side, the government sector indicated a reduction in orders in 2022, amounting to at least HUF 500 billion, which may even be higher due to the limited availability of EU funds. There are no signs yet of a fall in household construction orders. Moreover, both households and medium-sized and larger companies tend to accumulate construction materials. In line with funds available from the second half of 2022, it will be necessary to revise the ranking of the implementation of public investments. Due to the time needed for this, from mid-2022 larger construction capacities will be available to the private sector for some time.

In the period of less than three months between early January and mid-March 2022, experts estimated construction inflation to be around 13-15 per cent, as a result of the persistent supply chain disruptions seen during the post-pandemic opening of the economies and wage increases, which generally take place at the beginning of the year. Construction material prices rose 15-17 per cent, while the cost of labour was rose 10-12 per cent. Following the seasonal wage increases and larger price rises, there will presumably not be any major increase in labour costs for the rest of the year.

As a result of the dominant role of the countries involved in the conflict in some raw material and equipment markets, the construction materials market is likely to face a shortage of goods in the near future on a scale that has not been seen in decades. Due to this, it may be worth developing alternative channels for the procurement of materials. Experts noted that raw materials coming from Eastern countries are cheaper and often have EU certifications.

In 2021, the import ratio of Hungarian construction was 48 per cent. The main imported raw materials include iron, steel, lumber, heat insulation and copper. On the other hand, construction material prices in Poland rose to a lesser degree than in Hungary, which is partly attributable to the lower import ratio (around 20 per cent). The rise in energy prices is passed on at the EU level to the price of construction materials, such as steel, which is produced by one of the most energy-intensive manufacturing processes.

A good example of the short-term disruptions in the supply of construction materials is that there is no aluminium in the market in March 2022, and no orders can be placed for reinforcing steel either. Difficulties in the supply of raw material will inevitably give rise to further delays in completion deadlines, and on the whole it is difficult to plan not only the time of completion but also the costs. The shortage of raw materials may cause disruptions even in the case of products manufactured in Hungary. The Public Procurement Authority and the National Federation of Hungarian Building Contractors issued a joint recommendation[7] in March 2022 to construction enterprises on how to manage their contractual relations in the changed market environment resulting from the war, to ensure the implementation of previously concluded contracts. The recommendation primarily concerns contracts affected by public procurements, but it may provide useful guidance in respect of private sector contracts as well. Experts believe that one of the consequences of the Russo-Ukrainian war may be that after the end of the war, in the wake of the reconstruction of the destroyed buildings and infrastructure in Ukraine there will be an even larger shortage of raw materials, which may affect the entire region.

The conflict has no bearing on the situation (availability and quality) of the construction labour force overall. In recent years and currently as well, the Hungarian construction sector has employed around 15,000 Ukrainian citizens, which is unlikely to increase as a result of the wave of refugees.

Rental markets and developments

There is strong demand in the industrial-logistics segments, and both e-commerce and traditional trade are generating robust demand in the region. There is some uncertainty in the eastern part of Hungary with regard to capital inflows in areas near the Ukrainian border, the progress of investments that have already started and the vacancy rate of industrial properties, and also whether firms will continue to produce the same volumes in light of the high energy prices. On other hand, there are chances of international companies relocating their production activity from Russia or Ukraine to the CEE region, including Hungary.

Experts are also uncertain whether the buoyant demand in the industrial-logistics market can be maintained. Rental rates increased in the segment of industrial-logistics properties as a result of the strong demand. A correction in rental rates, which was anticipated as a result of the high volume of developments in recent periods, has failed to take place, as demand absorbed the completed areas and maintained or even increased the rates. The Hungarian logistics sector is less likely to be affected by the war, since Hungary serves as a connecting route to the Balkans and Turkey for the EU, while transport routes to the east are more likely to pass through Poland.

It is still difficult to estimate the long-term effect of the pandemic on the office market. If the ratio of working from home is around 5 per cent, it will generate a fall in demand that can be still managed by the sector, while a fall in demand on the order of 10-15 per cent would have severe consequences. In such a case – based on the average net absorption in the office market in recent years – office development activity should be adjusted to a loss of demand of 2-3 years. It is typical in the area of leases that even larger companies were still unable to decide on the work regime for the long run and on the size of office area they need in the future. The penetration of sustainability (ESG) requirements is an opportunity for office market developments: with the same cost budget, it would be possible to lease smaller but higher quality office areas with larger social spaces. However, rising financing costs, the higher technical content resulting from the ESG requirements and the lack of suitable plots put pressure on the costs of office projects, and thereby also on rental rates. However, higher rental rates may only be achieved at lessees with strong commitment to sustainability. Based on market information, in 2021, 12 lease contracts for over 2,000 square meters were concluded in the Budapest office market, which evidences the fact that it is extremely difficult to meet the 40 per cent pre-lease requirement prescribed by banks for financing. Overall, market participants believe that 2022 will not be a good year in terms of office developments.

Experts are of the opinion that the supply of hotel rooms in Budapest is low, and thus it would be justified to construct new rooms in anticipation of returning tourists. On the other hand, the war may generate yet another shock for foreign tourism, and adding to this the risks related to the increased price and availability of construction materials, market participants anticipate significant tightening in hotel financing.

[7] Recommendation – For the mitigation of business risks generated by the Russo-Ukrainian war in the area of construction and investment public procurements

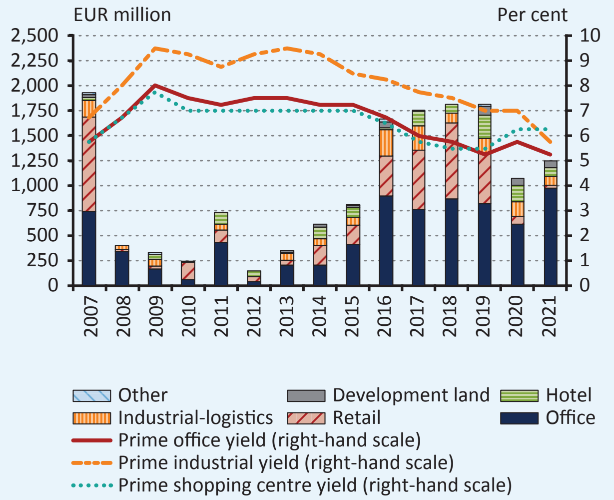
Financing

In 2022, several subsidised financing schemes will come to an end, and due to the rising interest environment customer interest rates as high as 9 per cent may also appear, which may generate surplus costs for investments that jeopardise the return. On the positive side, real interest rates are currently negative, but if stagflation develops, firms will not be able to adjust to rising costs. Banks regard a further increase in construction material prices as a very likely risk, to which they may respond by lending at higher pre-lease rates and lower LTV levels. Persistently low demand for offices, increasingly common decisions of lessees on hybrid work and the war, as yet another negative impact on tourism, point to a decreasing willingness of credit institutions to finance offices and hotels. Setting out from this and in light of the termination of financing schemes, experts noted that – in view of the risk of stagflation – it may be worth it to maintain a safe level of financing via state-subsidised lending schemes.

6 CRE investments

In 2021, the Hungarian investment market registered turnover of EUR 1.2 billion, representing growth of 17 per cent compared to the 2020 data. A major part (56 per cent) of the turnover was generated by a few high-value transactions and 67 per cent related to domestic investors. There is a shortage of properties for sale on the supply side of the investment market, resulting in falling yields. The monetary tightening cycle which has already started in several European countries and the world is also reducing the yield premiums offered by property investments, but mounting inflationary pressure may sustain investors' interest even in an environment of falling yield premiums, as they look for property investment opportunities in the region for a large volume of liquidity. Following the pause in 2020, declining yield trends returned to most countries in the CEE region in 2021, while annual investment turnover exceeded the level from one year ago by 3 per cent. In 2021, public real estate funds in Hungary registered a continuous, moderate capital outflow. However, their liquidity situation is stable. At the sector level, their liquidity ratio – including credit lines – stood at 46 per cent at the end of March 2022, which can be deemed safe.

Chart 22
Investment volume on the Hungarian CRE market, its composition and prime yields

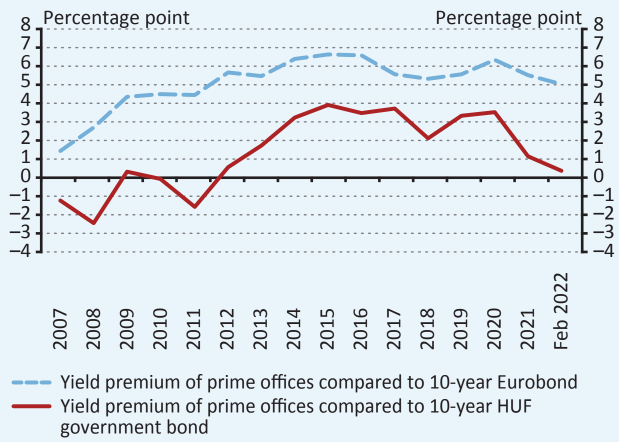


Source: CBRE, Cushman & Wakefield, MNB

2021 was characterised by increasing investment turnover, with a high ratio of high-value transactions and an appreciation of logistics investments. In 2021, the investment turnover of the commercial property market reached EUR 1.25 billion, falling short of the 2019 turnover figure by almost one third, but showing a 17-per cent increase compared to 2020 (Chart 22). The average transaction value was close to EUR 25 million, which exceeds the 2020 figure by 17 per cent. In 2021, there were eight major sales transactions (EUR 50 million or higher), accounting for 56 per cent of the total investment turnover. In terms of volume, 78 per cent consisted of sales of office buildings, 7 per cent of industrial-logistics real estate, 7 per cent of hotels, 6 per cent of development sites and 2 per cent of retail properties. The office market prime yield[8] decreased by 50 basis points to 5.25 per cent in 2021 H1, and has not changed until the end of the year. The primary yield level of the industrial-logistics segment fell every quarter in 2021, and after a drop of 125 basis points it stood at 5.75 per cent at the end of December, moving 50 basis points closer to the prime office yield. The latter well reflects the fact that logistics properties have become an increasingly preferred and less risky considered asset for investors over the past two years. The retail segment registered no decline in yields, with the prime yield at 6.25 per cent since 2020 Q1. A further decline in yields is supported by the shortage of investment products for sale on the supply side.

[8] Yield data refer to the (initial) gross yields of CRE transactions and are calculated as the ratio of the real estate's annual net rental revenue and the purchase price.

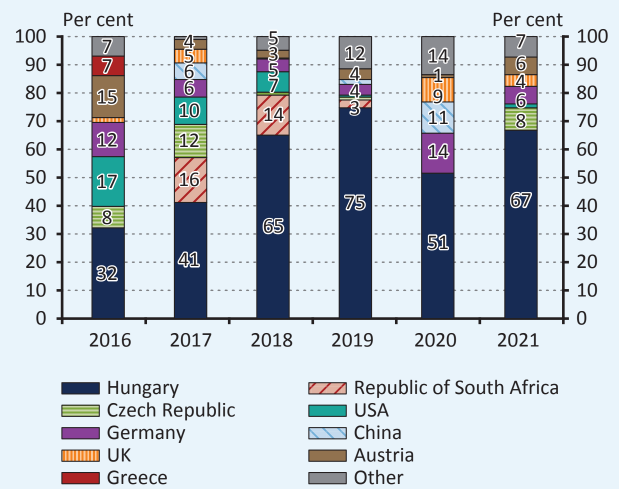
Chart 23
Yield premium of Budapest prime office investments compared to 10-year government bonds



Note: The 10-year HUF government bond yield is the Q4 average of the average yield of auctions. The 10-year Eurobond yield is the Q4 average of the 10-year government bonds issued by AAA-rated Eurozone countries. The yield premium for February 2022 was calculated taking into account the average yields on government securities in February 2022 and the prime office market yield at the end of 2021.

Source: CBRE, Cushman & Wakefield, ECB, MNB

Chart 24
Investment volumes on the Hungarian CRE market by investors' country of origin



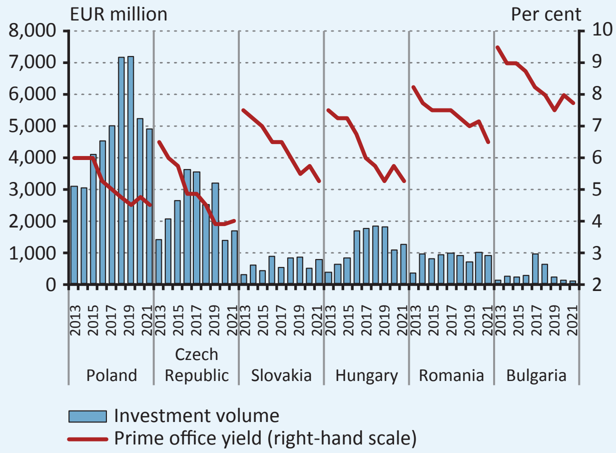
Source: CBRE, Cushman & Wakefield, MNB

Mounting inflationary risks maintain the attractiveness of the market, despite the shrinking yield premiums driven by tightening monetary conditions. The monetary tightening cycle, which has also started in Hungary, among other countries, has a downward impact on real estate investment yield premiums, in an environment of declining property market yields. Compared to the average yield of 10-year Hungarian government securities auctions in February 2022, prime office investments in Budapest exhibited a yield premium of 45 basis points over the average yield at the end of February 2022 (Chart 23). In the same comparison, the yield premium of prime industrial-logistics and prime shopping centres fell to 95 and 145 basis points, respectively. Compared to the yield on 10-year euro bonds, premiums are still around 5-6 percentage points, but a downward trend has also commenced in this relationship. Mounting inflationary pressure in Hungary and globally sustains investors' interest in commercial real estate investments, even in an environment of declining yield premiums.

The prevalence of resident investors increased again in 2021. Purchases by Hungarian investors accounted for 67 per cent of 2021 investment turnover, and 65 per cent of the turnover generated by high-value transactions is also linked to this group (Chart 24). The total value of purchases by Czech investors was the second highest after that of Hungarian investors, accounting for 8 per cent of the annual volume, while the share of transactions by investors from Austria and Germany was 6 per cent for each, and 4 per cent from the UK. In terms of the annual investment volume, 37 per cent belonged to Hungarian companies and 20 per cent to foreign real estate investment companies. The share of domestic private and foreign real estate funds was 35 per cent altogether. In 2021, there was a slight but steady outflow of capital from Hungarian public open-ended real estate funds, which used to be a major investor. On the other hand, the level of public real estate funds' liquid assets remained adequate and fluctuated around 45-47 per cent, maintaining the level registered at the end of 2020 – including the amount of immediately callable credit lines[9] – throughout 2021 (Annex, Chart 19).

[9] Government Decree No 78/2014. (III. 14.) on the investment and borrowing rules applicable to collective investment forms permits the inclusion of unconditional and immediately drawable credit lines in the calculation of the ratio of liquid assets.

Chart 25
Investment volume and prime office market yields in the region



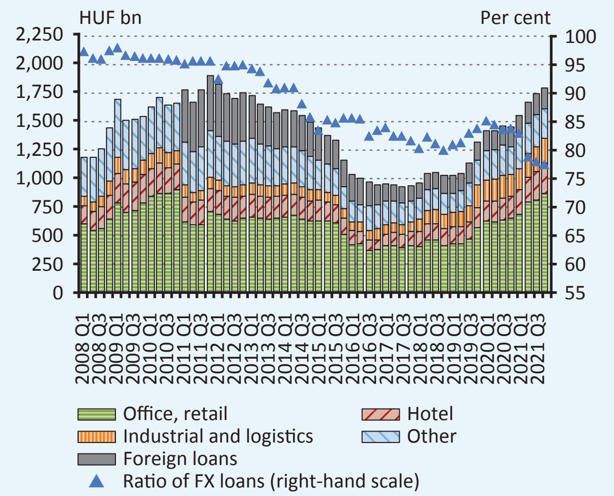
Source: MNB compilation based on CBRE, Colliers, Cushman & Wakefield and JLL data

Following the pause in 2020, the downward trend in yields continued in most CEE countries. In 2021, the investment markets in the regional CEE countries saw a decrease in yield of 25-65 basis points; prime office market yields rose by 10 basis points only in the Czech Republic (Chart 25). The lowest yields were still seen in Prague (4.0 per cent) and Warsaw (4.5 per cent). Compared to Prague and Warsaw, Budapest offers a prime office market yield premium of 125 and 75 basis points, respectively, while the yield level is the same as in Bratislava. Investment volumes in 2021 varied by countries: in Bulgaria, Poland and Romania volumes fell slightly short of the 2020 level (by 6-9 per cent), while they exceeded it in the Czech Republic, Hungary and Slovakia. For the region, investment turnover exceeded the 2020 level by 3 per cent on the whole, while it declined by 31 per cent compared to 2019 (Annex, Chart 18). The largest increase was observed in Slovakia, where the 2021 investment turnover exceeded that of the previous year by 52 per cent.

7 Commercial real estate financing

In 2021, credit institutions' project loan portfolio secured by commercial real estate grew substantially, expanding by almost 23 per cent. In year-on-year terms, the ratio of foreign currency loans fell by 6 percentage points –supported in large part by the FGS Go! programme – and thus amounted to 78 per cent at the end of December 2021. In 2021, credit institutions disbursed one third more project loans secured by commercial real estate than in 2020. Almost half of the disbursements were linked to office buildings and shopping centres; however, the strongest growth (219 per cent) was observed in the amount disbursed to the hotel segment, and within that disbursements for purchases registered the strongest increase (278 per cent). At the end of December 2021, 3.1 per cent of the project loan portfolio secured by commercial property was participating in the moratorium, which was extended with a restricted scope from November 2021. This is a much lower participation rate compared to the levels over 40 per cent measured in 2021. Loans granted for hotel financing accounted for 65 per cent of the commercial property project loans taking advantage of the suspension of debt servicing, while instalments were no longer suspended for any of the project loans in the industrial-logistics segment at the end of 2021. According to the Lending Survey conducted in January 2022, before the outbreak of the war, in the third quarter of 2021 there was no material change in conditions on commercial real estate loans, while in the fourth quarter only a small range of banks reported a tightening of conditions. In 2021 H2, credit institutions observed a pick-up in demand for commercial property project financing loans. However, looking ahead, expectations with regard to demand and conditions may substantially change as a result of the negative impacts caused by the war.

Chart 26
Composition of the credit institution sector's project loan stock for CRE purchase or development, by real estate type and denomination



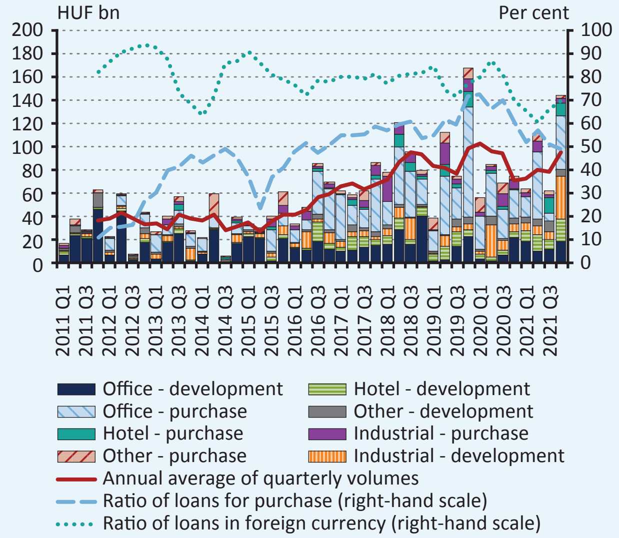
Note: No data breakdown by real estate type is available for loans provided to foreign companies before 2011.

Source: MNB

While the portfolio expanded, the foreign exchange ratio of project loans secured by commercial real estate continued to decline. At the end of 2021, project loans collateralised with CRE amounted to a total of HUF 1,805 billion in credit institutions' balance sheets (Chart 26). Compared to the end of 2020, this represents growth of 23.7 per cent, or 22.5 per cent if adjusted for the exchange rate effect. Of the annual growth, 62 per cent was achieved in the first half of 2021. Within the portfolio, due to a 6-percentage point decline, the ratio of foreign currency loans outstanding, which are denominated almost entirely in euro, fell to an unprecedented 78 per cent in 2021, largely supported by the FGS Go! programme. At end-December 2021, nearly half of the financial institutions' CRE-collateralised project loan portfolio was dedicated to office and commercial centre development and acquisition, with the hotel and industrial-logistics segments accounting for 15 and 12 per cent, respectively. On a year-on-year basis, outstanding loans for the hotel segment and for office buildings and commercial centres grew to the largest degree, expanding by 39 per cent and 33 per cent, respectively.

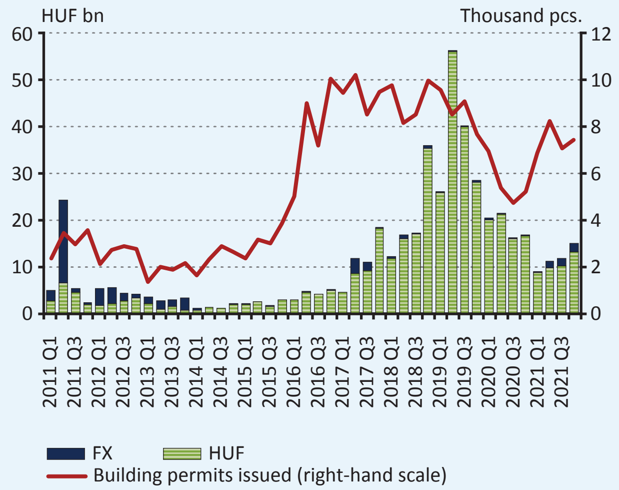
Participation in the moratorium with restricted scope is considerable only in the case of hotels. At the end of December, 3.1 per cent of the outstanding project loans secured by commercial property participated in the moratorium extended from November 2021 in a narrower form until the end of July 2022. This ratio is negligible compared to the level of over 40 per cent seen in 2021 H1. Loans granted for hotel financing accounted for almost two

Chart 27
Project loans provided to domestic companies for CRE purchase or development by the credit institution sector, by real estate type



Source: MNB

Chart 28
Volume of new project loans granted for residential park development or purchase



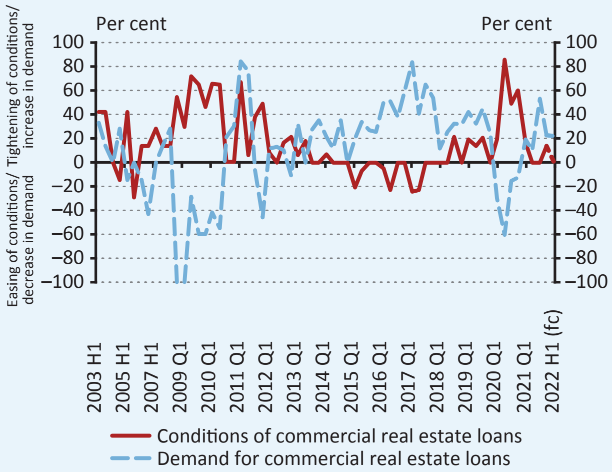
Source: HCSO, MNB

thirds of the commercial property project loans participating in the scheme. In the case of offices and shopping centres, the ratio of loans that remained in the scheme is below one half per cent, while at the end of December none of the industrial-logistics property financing project loans participated in the moratorium extended in a targeted manner.

A large volume of new project loans was disbursed even in the six months after the exhaustion of FGS Go!, in conjunction with a moderately increasing foreign currency ratio in an annual comparison. In 2021, credit institutions disbursed CRE-collateralised development or purchase project loans to domestic companies in a total amount of HUF 381 billion, exceeding the volume disbursed in the same period of 2020 by 34 per cent, but falling short of the figure registered two years ago by 3 per cent (Chart 27). Including loans disbursed to non-residents, disbursement of project loans secured by commercial real estate amounted to HUF 421 billion, up 32 per cent versus one year earlier. Of the annual volume disbursed to domestic companies, 49 per cent financed the development and purchase of office buildings and commercial centres, of which 68 per cent was for purchases. Another 20 per cent was linked to the hotel segment and 20 per cent to industrial properties. Compared to the previous year, in 2021 the volume of disbursements for hotel projects rose to the largest degree, advancing by 219 per cent. The amount of loans disbursed for the purchase of hotels and for developments rose by 278 and 196 per cent, respectively. While foreign currency loans accounted for 65 per cent in 2021 H1, the ratio rose to 73 per cent in the second half of the year. This rise may have been partly attributable to the exhaustion of the financial allocation for FGS Go! and to the tightening cycle's effect of raising forint funding costs.

The volume of project loans disbursed for the financing of residential parks declined by more than one third in 2021. The volume of new loans for residential park investment with risks similar to CRE financing also declined significantly in 2021, falling by 37 per cent in year-on-year terms (Chart 28). This fall may have been attributable to several factors: due to the increase in the standard VAT rate of new homes to 27 per cent, the number of new housing projects dropped off significantly in 2020; the real estate sector was also able to raise funds via bonds issued under the Bond Funding for Growth Scheme; and the rise in construction material prices starting in 2021 had a negative effect on projects in progress. On the other hand, investment appetite was positively influenced by the housing subsidies available from early 2021, the repeated general application of the 5 per cent preferential VAT on new homes and the FGS Green Home Programme launched in October 2021. For the summary of the real sector's participation in the Bond Funding for Growth Scheme, see Box 3.

Chart 29
Development of CRE loan demand and loan conditions



Note: Responses of the participating banks, weighted by market share.
Source: MNB, Lending Survey

In 2021 H2, the terms of commercial real estate loans did not change materially. In parallel with this, demand picked up substantially. According to the MNB's quarterly Lending Survey, conducted before escalation of the Russo-Ukrainian conflict, in 2021 Q3, banks did not change conditions on commercial real estate loan, while in the fourth quarter, a net 14 per cent of them tightened standards due to the uncertain prospects in several commercial property market segments (Chart 29). Looking ahead, banks did not anticipate further tightening in 2022 H1 in any of the commercial property segments; however, the economic effects of the Russo-Ukrainian war may change this. The decline in demand that accompanied the tightening of lending conditions in 2020 reversed in 2021, and in the third quarter 54 per cent of the respondent institutions already reported a pick-up in demand for commercial property financing loans. The last time when a similar ratio of banks reported this was the final quarter of 2017. In 2021 Q4, one quarter of banks observed a pick-up in demand and 23 per cent of them, in net terms, expected the same in 2022 H1. On the other hand, geopolitical tensions from the war and the economic effects of such may curb development and investment activity as well as credit demand. In terms of financing, market participants expect office and hotel projects to drop off in 2022.

Box 3
Participation of the real estate sector in the Bond Funding for Growth Scheme

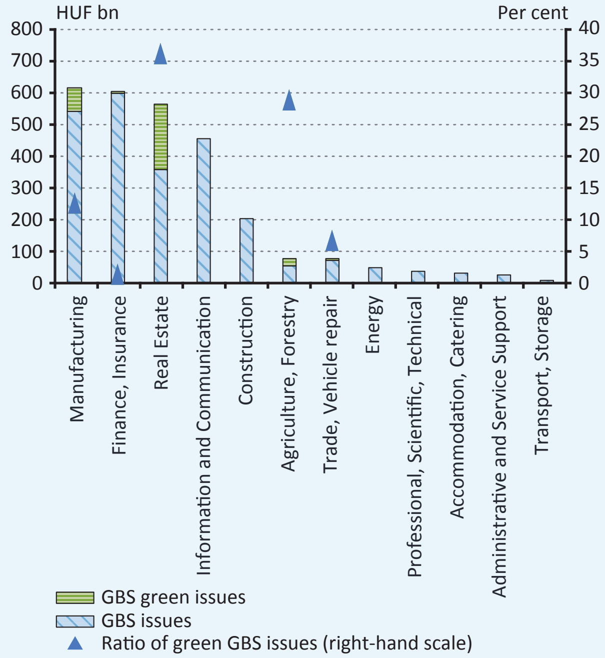
As a result of the strategic decision of the Monetary Council on capital market development, the MNB – supplementing its unconventional set of monetary policy instruments – launched the Bond Funding for Growth Scheme (BGS) on 1 July 2019.[10] The purpose of the scheme was to increase the liquidity of the corporate bond market and diversify the fund-raising options of domestic corporations, thus facilitating more efficient monetary policy transmission. The central bank made a financial allocation of HUF 1,550 billion to the scheme for purchasing issuers' bonds of good rating. The Bond Funding for Growth Scheme closed at the end of December 2021. Once the ongoing negotiations with issuers have been realised, up to the maximum envelope of the programme, the central bank will no longer purchase new corporate bonds.

The BGS broadened corporations' access to bond funding in a wide range of sectors, with almost 120 bond issues, where the aggregate nominal value of bonds was HUF 2,767 billion. In a breakdown by issued nominal value by national economy sectors, the third most active issuer was the real estate sector, accounting for 20 per cent of all issuances under BGS. The real estate sector is preceded by manufacturing (22.4 per cent of issuances) and asset management, financial and insurance activity (also including companies operating in the form of a holding company) (22 per cent of issuances). On the supply side, construction – closely linked to the real estate sector – was ranked fifth based in terms of issuance by sectors, accounting for 7.5 per cent of the aggregate nominal value of BGS issuances.

[10] Considerations behind the launch of the Bond Funding for Growth Scheme (BGS) and main features of the programme. Available at: https://www.mnb.hu/letoltes/no-vekede-si-ko-tve-nyprogram-eng-0326-2.pdf

Although there was no explicitly defined green objective when BGS was launched, the scheme has been instrumental in increasing the issuance of green bonds to finance sustainable activities. The real estate sector is a leader in green bond issuance, as more than one third (37 per cent) of its bond stock issued under BGS can be linked to the implementation of sustainability objectives. The sector's high share of green issuance is not surprising: according to the European Commission, buildings are responsible for 40 per cent of energy consumption and 36 per cent of greenhouse gas emissions in the EU, mainly from construction, use, renovation and demolition.[11] Accordingly, improving the energy efficiency of buildings is key to achieving the ambitious carbon neutrality target for 2050 set out in the European Green Deal.

Nominal value of bonds issued under the MNB Growth Bond Scheme by industry



Source: MNB

The vast majority of the funds raised by BGS bond issues provided additional funding for issuers in the real estate sector.[12] According to our estimate, less than one quarter of the issuers in the sector used the bond funds in part for loan repayments and the amount used by them for loan instalment amounted to roughly one quarter of the issued nominal value, on average. With more than HUF 560 billion of bonds issued in real estate transactions, tracking the project loan portfolio of credit institutions alone does not give a full view of the sector's liabilities. However, it is also not possible to treat bond funds as liabilities for the same purpose as project loans in their entirety, as the funds raised from these issues were not exclusively used for the financing of real estate developments and purchases, nor were they exclusively used to finance domestic projects.

Overall, the Bond Funding for Growth Scheme has substantially improved the financing of the real estate sector in recent years and made a major contribution to growth in green financing within the sector.

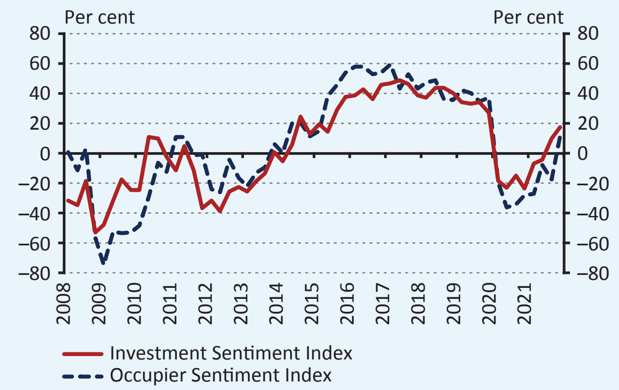
[11] European Commission – Department: Energy – In focus, Energy efficiency in buildings. Available at: https://ec.europa.eu/info/sites/default/files/energy_climate_change_environment/events/documents/in_focus_energy_efficiency_in_buildings_en.pdf

[12] For further information on the average ratio of funds raised under the Bond Funding for Growth Scheme and used for loan repayments for all economic sectors, see the Corporate lending chapter of the December 2021 Financial Stability Report. Available at: https://www.mnb.hu/letoltes/financial-stability-report-december-2021.pdf

8 Results of the RICS commercial real estate market survey

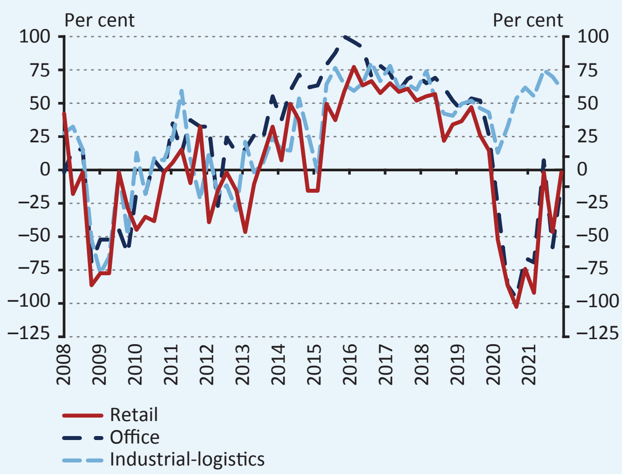
Based on the results of the Royal Institution of Chartered Surveyors (RICS) survey conducted in January 2022, an improving trend can be observed in business sentiment, which had deteriorated in the domestic investment and rental markets in 2020 due to the pandemic. On the other hand, experts reported varying trends by segments. The strongest investor and lessee demand can be perceived in the industrial-logistics market, to which the market responded by increasing supply. On the other hand, experts reported declining demand in the office market and retail real estate market in 2021 H2. The uncertainty in the commercial property market due to the coronavirus pandemic is well illustrated by the fact that there is no strong consensus among experts on the cyclical position of the market.

Chart 30
Development of Investment and Occupier Sentiment Index



Note: Based on responses from January 2022.
Source: RICS

Chart 31
Development of rental demand by segment

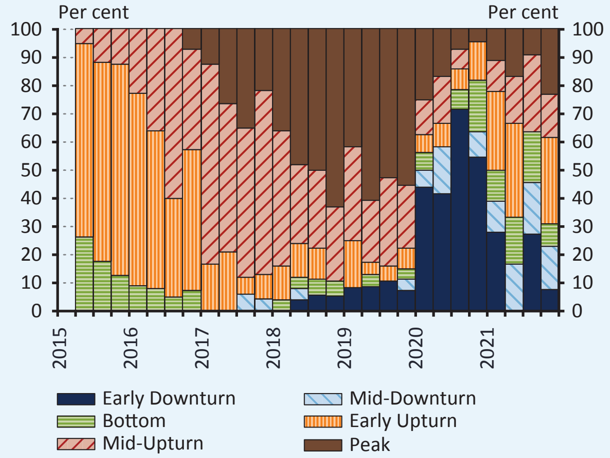


Note: Net ratio of respondents indicating increase and decrease in demand. Based on responses from January 2022.
Source: RICS

Business sentiment improved in 2021 H2 both in the investment and rental markets. According to experts surveyed by the Royal Institution of Chartered Surveyors (RICS), sentiment in the commercial property market improved in 2021 H2 (Chart 30), but respondents reported diverging trends in certain segments. In the industrial-logistics real estate market, experts perceive substantially more favourable investor demand compared to other segments, and within that stronger domestic investor interest was reported for 2021. As a result of the increased demand, respondent experts perceived a historically high rate of developments commencing in the industrial-logistics segment, but development appetite in the office market also improved at the end of 2021, following a low in 2020-2021 H1. In line with keen investor demand and wide-ranging development in the industrial logistics market, respondent experts expect prime industrial logistics property values to rise the most in the coming year, by an average of around 5.2 per cent, while the non-prime segment is expected to see an increase of 3.5 per cent. In the other segments, respondents expect property values to stagnate or slightly decrease in 2022.

In the rental market, rising demand was observed only in the industrial-logistics segment. In 2021 H2, the respondents perceived weakening rental demand both in the retail and office markets. By contrast, the experts reported continuously increasing demand for industrial-logistics areas offered for lease (Chart 31). In terms of rental supply – in view of the rising vacancy rates – office and retail properties continue to show a significant volume of availability, while in the industrial-logistics market, respondents reported an expansion from 2021 H2, replacing the previous tight supply; this resulted from new completions. There was a change in rental rate discounts in 2021 Q4. Contrary to the previous higher ratios, significantly

Chart 32
Perceptions of the current phase of the property cycle



Note: Based on responses from January 2022.
Source: RICS

fewer experts noted that they would provide new tenants with a discount in the office and retail property segment.

There was no strong consensus among market experts on the cyclical position of the commercial property market at the end of 2021, albeit most perceived a recovery. It is a good indication of the uncertainty in the market due to the coronavirus pandemic that in 2021 Q3 the ratio of respondents believing that the market cycle is in its downturn phase rose significantly, from 17 per cent of the previous quarter to 45 per cent. However, by the fourth quarter their ratio once again fell to 23 per cent. At that point, 46 per cent of respondents said that the market was recovering and 23 per cent of them believed that it was at the peak of the cycle at the end of the year. The ratio of experts who perceived an initial recovery was the highest in the fourth quarter, at 31 per cent. Overall, there was no strong consensus among market experts on the cyclical position of the commercial real estate market in 2021 (Chart 32).

Annexes

ANNEX 1: SUB-MARKETS OF THE BUDAPEST OFFICE MARKET[13]

The office market of Budapest is divided into the following eight sub-markets based on the data collection of the Budapest Research Forum (Chart 33):

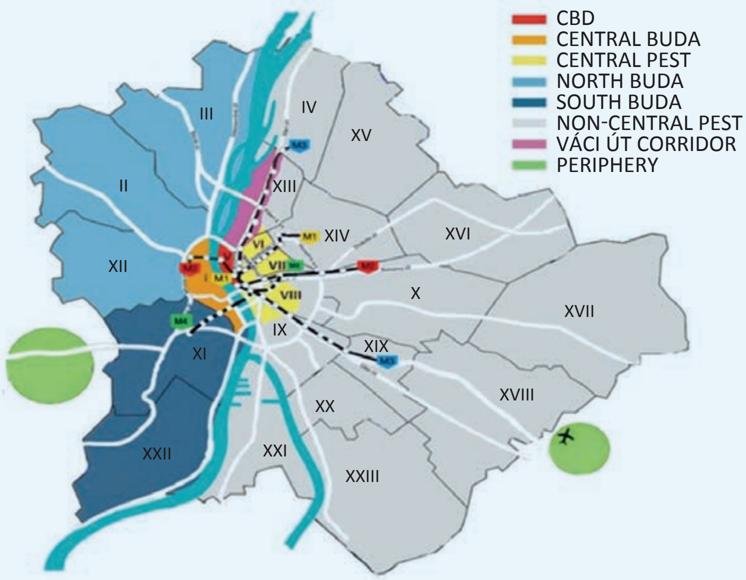
- **Central Business District – CBD:** The inner districts of Budapest, primarily the office buildings in the 5th district and on Andrássy út and the surrounding streets from Bajcsy-Zsilinszky út to the Oktogon. Most of the CBD is an architecturally protected area with a few category 'A' office buildings and very limited development opportunities.

- **Central Buda:** Area bounded by the Margit körút–Krisztina körút–Böszörményi út–Jagelló út–Villányi út–Fehérvári út–Október huszonharmadika utca–Irinyi József utca. Similar to the Central Business District, development opportunities are limited.

- **Central Pest:** Area bounded by the Inner City–the Váci út Corridor–Dózsa György út–Thököly út–Fiumei út–Orczy út–Haller utca. Concentrated developments have been performed in this sub-market.

- **North Buda:** Most of districts 2, 3 and 12; investments are limited to smaller areas.

Chart 33
Sub-markets of the Budapest office market



Source: Budapest Research Forum.

- **South Buda (Non-Central Buda South):** Districts 11 and 22. In the development of this sub-market, available development areas are an alternative for the service centre office tenants of the Váci út Corridor, but these are less accessible than the Váci út Corridor.

[13] Source: Cushman & Wakefield

- **Non-Central Pest:** Areas of Pest that are not part of the Inner City, Central Pest or the Váci út Corridor.

- **Váci út Corridor:** Area bounded by Szent István krt.–Váci út–Újpest Városkapu and the Danube. The Budapest office corridor where the most significant office developments were realised due to its available development areas and good accessibility (public transport: metro line M3, car: via Váci út). This is the most popular sub-market among foreign companies for siting their service centres.

- **Periphery:** Agglomeration areas, mainly Budaörs, Vecsés, Biatorbágy and Törökbálint.

ANNEX 2: CONCEPTS RELATED TO DEMAND IN BUDAPEST

Members of the Budapest Research Forum (CBRE, Colliers International, Cushman & Wakefield, Eston International, JLL, Robertson) collect CRE market contracts categorised into the following transaction types:

- **New lease:** a lease agreement of an immediately available area concluded with a tenant that was not previously present in the real estate.

- **Pre-lease:** a pre-lease contract concluded for a building that has not been completed yet and is not present in the current supply. Consequently, the volume of pre-lease transactions made in the period considered does not immediately increase the leased stock, but only later when it is actually placed on the market.

- **Expansion:** a rental agreement concluded with a tenant that is already present in the real estate, but rents area additional to its existing tenement.

- **Owner occupation:** the real estate's owner utilises the area, basically removing it from the market, decreasing stocks offered for lease.

- **Lease renewal:** the extension of an existing contract with no effect on the rental stock.

The comprehensive measures of rental market activity:

- **Total demand (gross demand):** the total volume of the above five lease transaction types in the period considered.

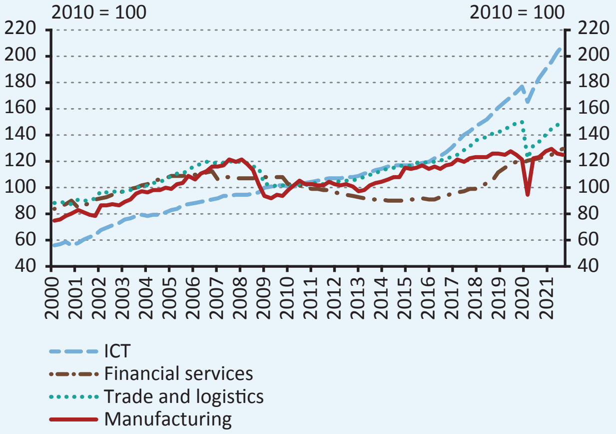
- **Take-up:** measures the stock of actual new lease contracts; from the above, it includes the volume of new leases, pre-leases and expansions for the period considered.

- **Net absorption:** demonstrates changes in the lease stock in the period considered. The difference between net absorption and gross demand is caused by lease renewals, pre-leases and tenants which exit the market.

ANNEX 3: ANNEX CHARTS

1 Macroeconomic environment

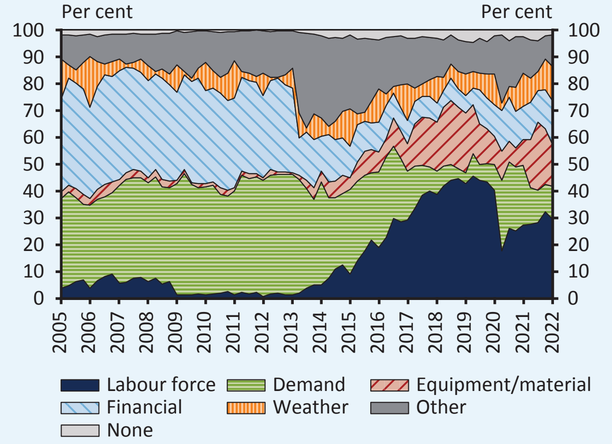
Chart 1
Performance of sectors relevant to the CRE market



Note: The ICT sector refers to the information and communications technology sector.

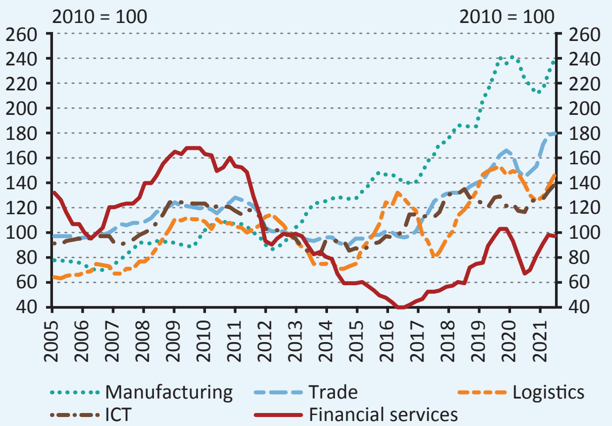
Source: HCSO

Chart 2
Factors limiting output in the construction industry



Source: European Commission

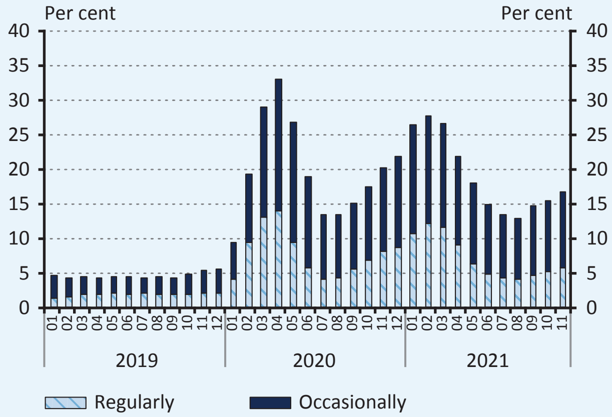
Chart 3
Investment activity of sectors relevant to the CRE market



Note: 4-quarter moving average. The ICT sector refers to the information and communications technology sector.

Source: HCSO, MNB calculations

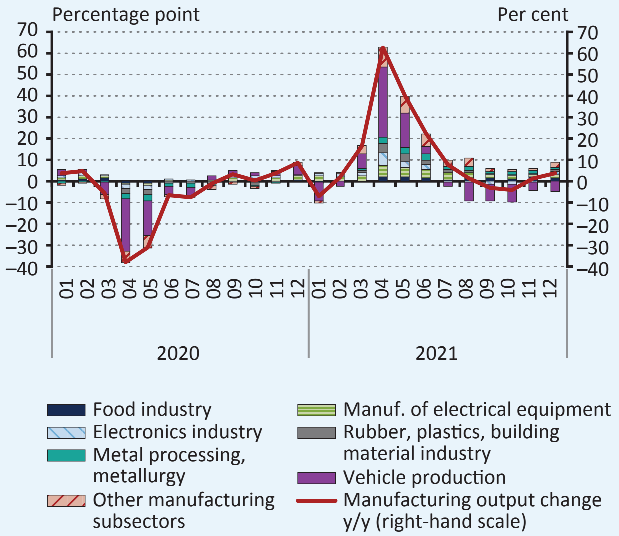
Chart 4
Employees working remotely or at home as a proportion of those in intellectual occupations



Note: The three-month moving average of employees working remotely of at home aged 15–74 as a percentage of those in intellectual occupations.

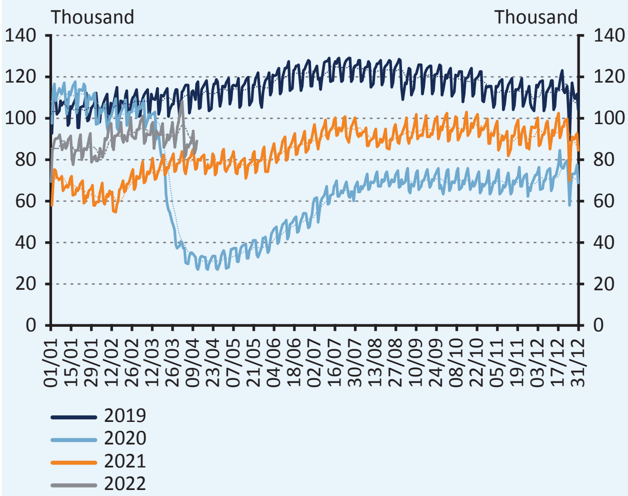
Source: HCSO

Chart 5
Contribution of subsectors to changes in the volume of manufacturing output on a monthly basis



Source: HCSO Weekly monitor

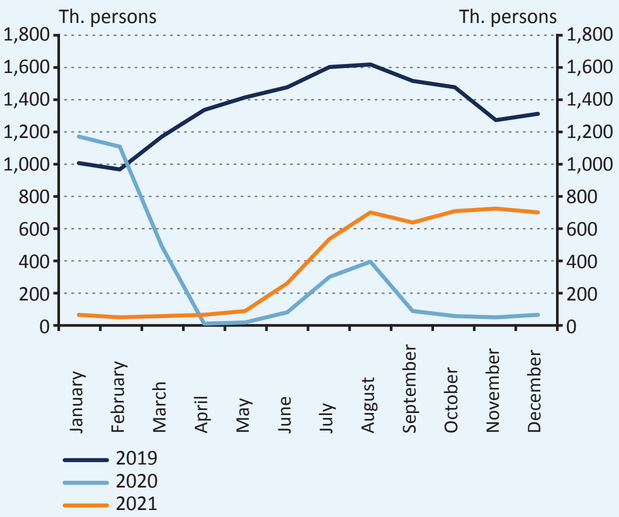
Chart 6
Development of the global number of commercial flights



Note: Commercial flights cover commercial passenger flights, cargo flights, charter flights and some business jet flight.

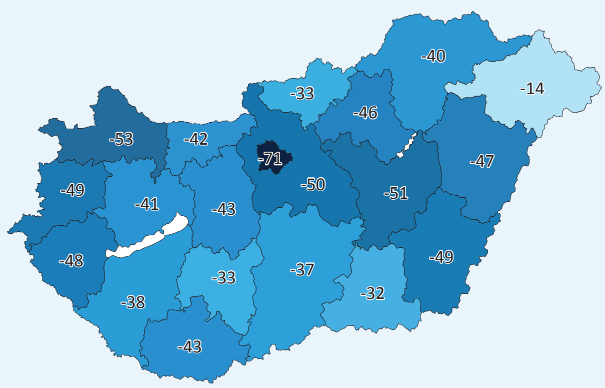
Source: Flightradar24

Chart 7
Budapest Liszt Ferenc International Airport passenger traffic



Source: HCSO

Chart 8
Biennial change in the number of hotel guest nights by county (January-December 2021)

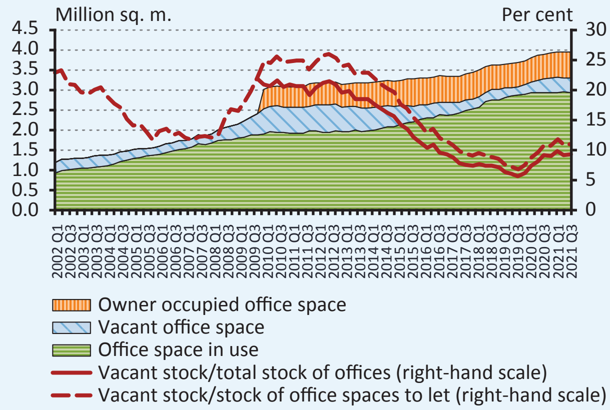


Note: Percentage change on 2019.

Source: HCSO

2 Office market

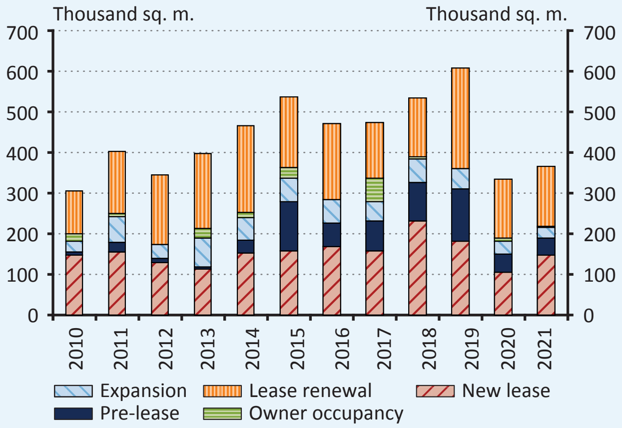
Chart 9
Floor space and vacancy rates of modern offices in Budapest



Note: Data for owner-occupied offices only available from 2010 onwards.

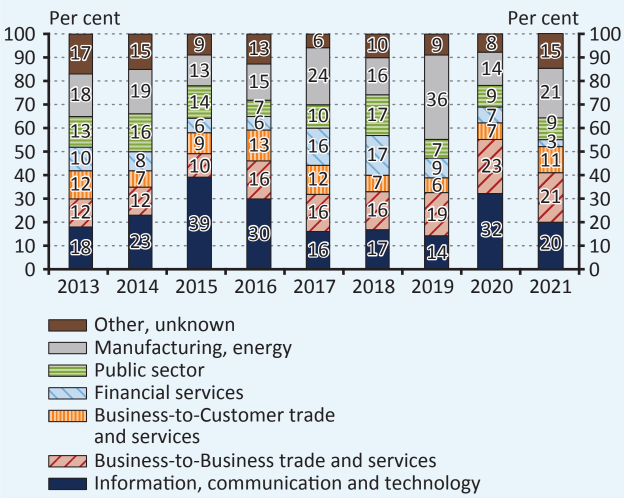
Source: Budapest Research Forum

Chart 10
Volume and composition of rental demand in the Budapest office market



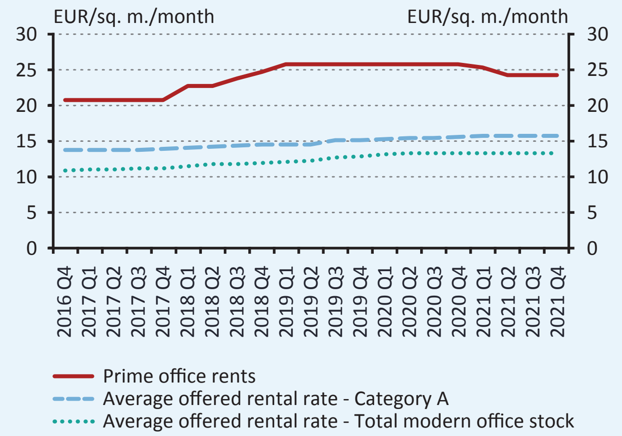
Source: Budapest Research Forum, Cushman & Wakefield

Chart 11
Take-up composition of the Budapest modern office market by tenant activity



Source: CBRE

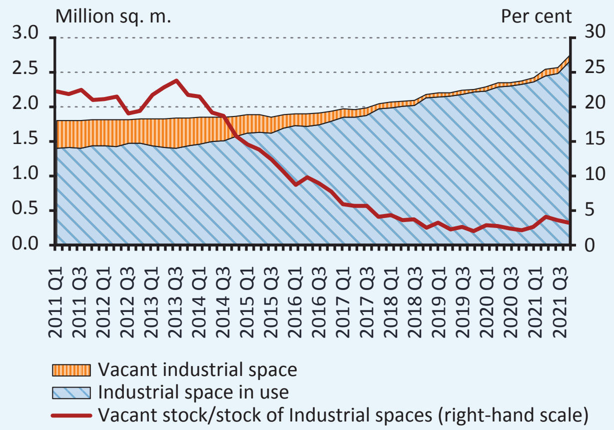
Chart 12
Offered rental rates on the Budapest office market



Source: CBRE

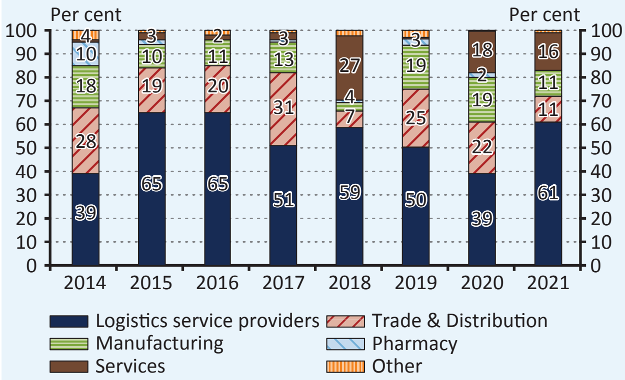
3 Industrial-logistics

Chart 13
Floor space and vacancy rates of modern industrial-logistics sites in Budapest



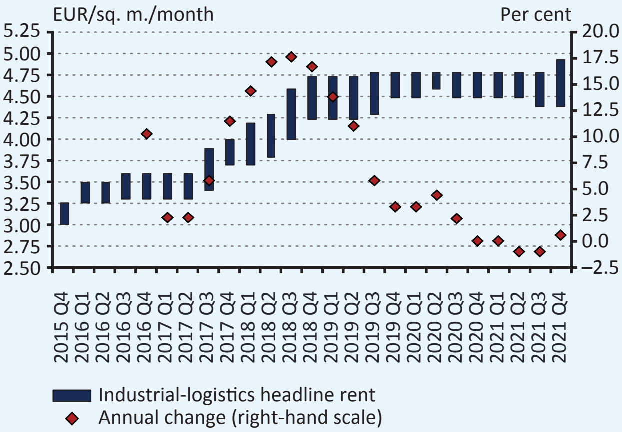
Source: Budapest Research Forum

Chart 14
Total demand composition on the industrial-logistics market of Budapest and environs by tenant activity



Source: Cushman & Wakefield

Chart 15
Typical rental rates of industrial-logistics properties in Budapest and environs

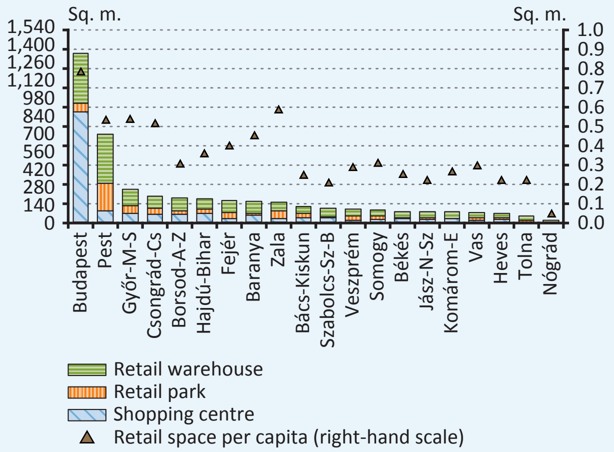


Note: Yearly change presents the yearly change in the mean of the rental rate range.

Source: CBRE

4 Retail

Chart 16
County distribution and composition of the modern Hungarian retail real estate stock

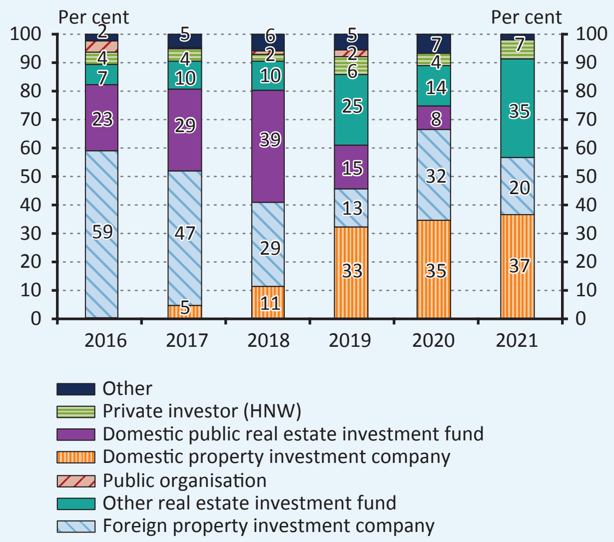


Note: Based on data from the end of 2021.

Source: CBRE

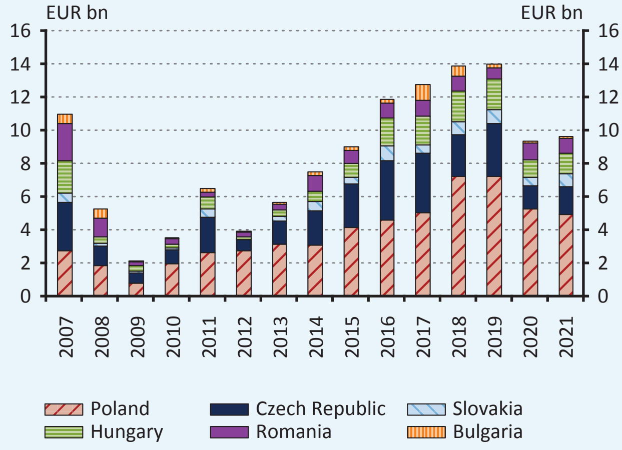
5 Commercial real estate investments

Chart 17
Investment volumes on the Hungarian CRE market by investor type



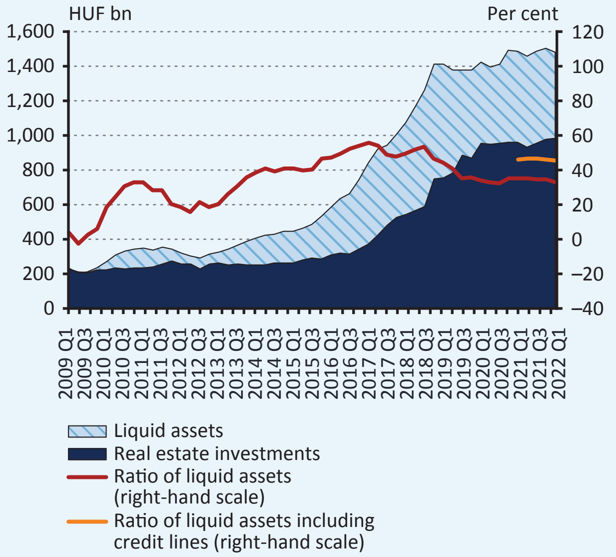
Source: CBRE, Cushman & Wakefield, MNB

Chart 18
CRE investment flows in the CEE region



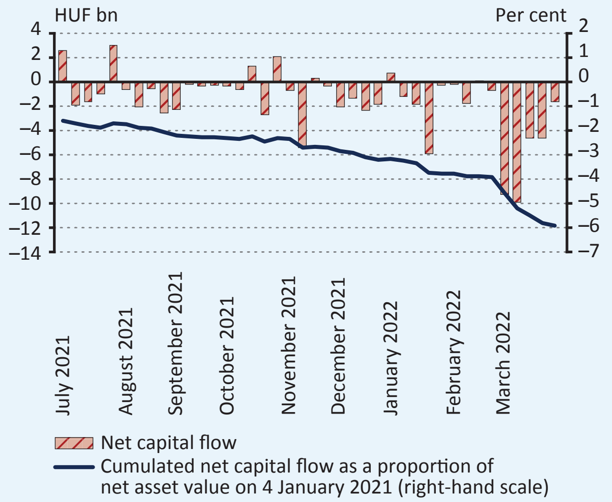
Source: MNB compilation based on CBRE, Colliers, Cushman & Wakefield and JLL data

Chart 19
Asset composition of public real estate funds and the ratio of liquid assets to net asset value



Source: MNB

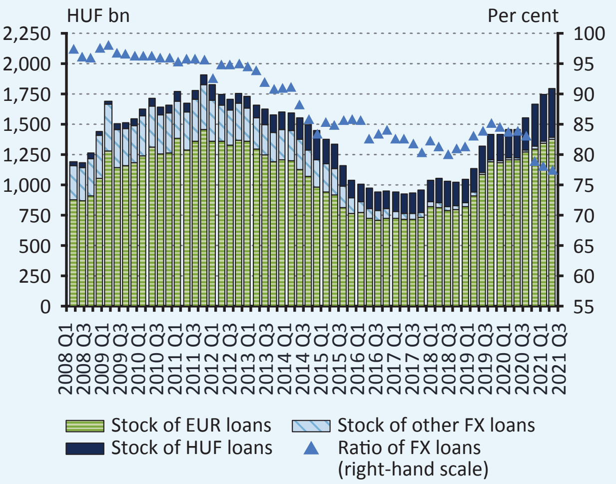
Chart 20
Net capital flows in Hungarian public real estate investment funds



Note: Weekly data.
Source: MNB

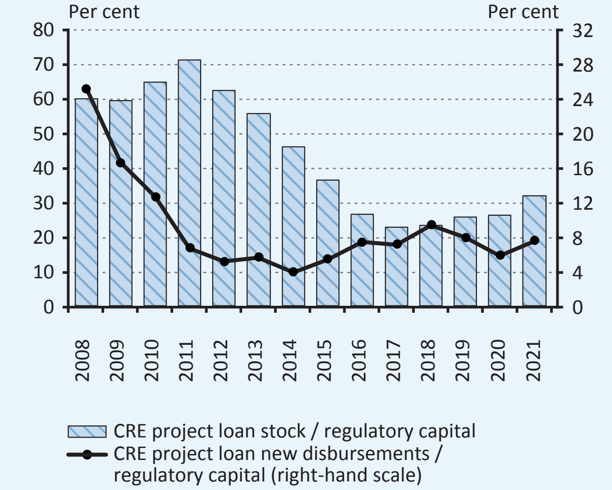
6 Bank financing of commercial real estate

Chart 21
Composition of the credit institution sector's stock of CRE purchase or development project loans by currency



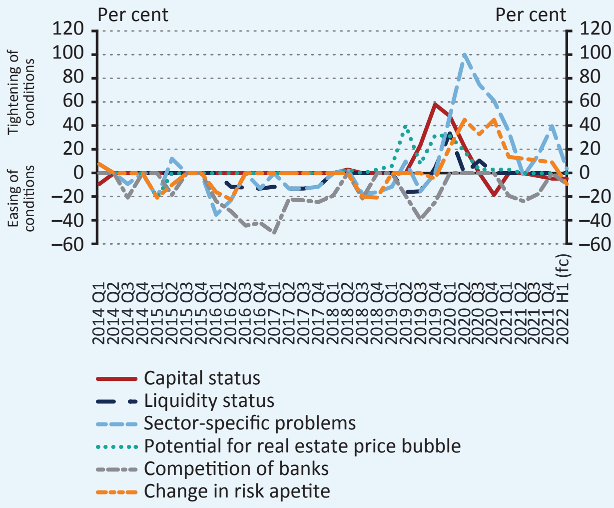
Source: MNB

Chart 22
CRE project loan portfolios of credit institutions and disbursements as a percentage of regulatory capital



Source: MNB

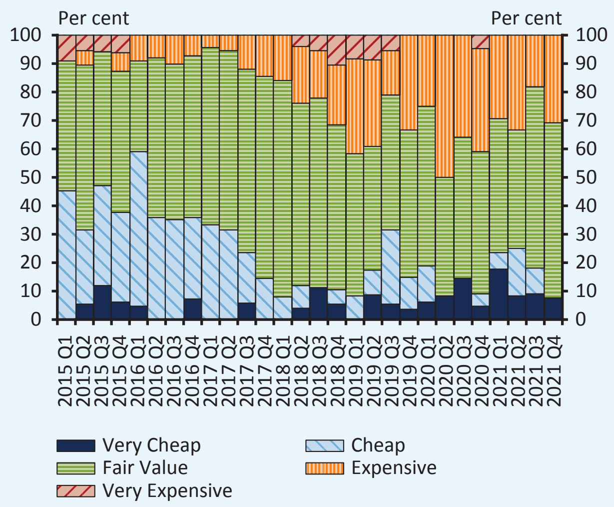
Chart 23
Factors behind changes in CRE loan conditions



Note: Responses of the analysed banks weighted by market share.
Source: MNB, Lending Survey

7 Commercial real estate market survey of RICS

Chart 24
Valuation level of the commercial real estate market



Note: Based on responses from January 2022.
Source: RICS

Miklós Ybl

(6 April 1814 – 22 January 1891)

He was one of our greatest architects, belonging to the most prominent Hungarian masters of the 19th century. He was a representative of historicism on a European level. His reputation extended over the borders of Hungary not only due to his education, but also due to his works of art. His work covered several genres of art and he left a remarkably rich legacy. His early style was characterized by romanticism with Roman elements. He, later, dedicated himself to neo-Renaissance. He was an artist of major impact completing numerous assignments and receiving recognition in his lifetime. The design of symbolic, significant and long-lasting buildings of our national culture are associated with the name of Miklós Ybl.

He laid the foundation of his career in Hungary by completing international studies and gaining experience. Between 1825 and 1831, he was the student of the Imperial and Royal Institute of Technology (the Politechnikum) in Vienna. In 1840, he enrolled in the Bavarian Academy of Arts in Munich, and he went to Italy for learning purposes in 1841, which he repeated five years later. He started his work in the office of the well-known architect of the time, Mihály Pollack in 1832, then based on his referral he transferred to Henrik Koch in Vienna in 1836.

In 1841, he opened his first independent office named Architectural Institute together with Ágoston Pollack, the son of Mihály Pollack in Dorottya street in Pest. From 1843, he received a growing number of orders from the Károlyi family, for whom he worked as a royal architect until 1861. István Károlyi assigned the reconstruction of the castle in Fót to him in 1845. The assignment also included the designing of the adjoining Roman-Catholic church, which was built in Romantic style thus making reference to the Middle Ages. The church is considered as one of the most outstanding works of Miklós Ybl. Completing castle designs was a main part of his career. Of these works, it is worth mentioning the palace of earl Lajos Battyhány in Ikervár, as well as the castle of the Károlyi family in Parádsasvár.

The most important period of his creative years coincided with one of the most significant times of European urbanization. Among many other buildings, he designed the house with a passage on Múzeum Boulevard, the apartment block located at 17 Bajcsy-Zsilinszky road, as well as the Hungarian National Hall (Tattersall) during this period. The Tattersall was destroyed in the second world war. He designed the Customs House in Pest in 1870. His other prominent works included the bath at Margaret-Island, which was demolished after the second world war, and the House of Representatives at 8 Bródy Sándor street exhibiting the characteristics of the Renaissance Revival architecture (currently the Italian Cultural Institute).

His most significant works include the Hungarian State Opera House. A restricted tender procedure for its design was announced in 1873, which Ybl won. Construction started in October 1875 with royal support, and Miklós Ybl was soon made supervisor of the project. The Builders' rite was held on 7 December 1878, and the building was officially opened with the performance of Bánk bán on 27 September 1884, with the royal family also attending. At the same time, Miklós Ybl was working on the construction of the Castle kiosk and bazaar in Buda (1875-1882), which was built to resemble Italian, German and French hanging gardens. In 1882, he received the Cross of the Lipót-order, and was appointed a member of the House of Magnates by the king on 21 June 1885. Towards the end of his life, he continued the construction of Saint Stephen's Basilica designed by József Hild, and subsequently, he participated in the reconstruction of the Buda Castle. However, he could not finish this assignment, as he passed away on 22 January 1891.

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