



Hungary: A safe bet?

By Peter Grundberg

The British press is constantly extolling the virtues of investing in Central and/or Eastern Europe on the basis of low costs and stellar returns. This is true to some extent although do not be fooled as to the ease of generating these returns – they require careful research and hard work.

So, where is Hungary exactly? Oft-described as in Eastern Europe, Hungary is better characterised as being in Central and Eastern Europe (CEE). It shares borders with seven countries (Austria, Slovenia, Serbia, Croatia, Romania, Slovakia and Ukraine), of which four are EU member states. Also, Hungary's capital is Budapest NOT Bucharest!

Hungary is one of the 'safer' CEE countries in which to invest; it offers prospects for good medium-term returns on investment on account of:

- Transparent ownership and legal system
- Relatively low political risk
- Consistent rate of annual real GDP growth
- High levels of Foreign Direct Investment (FDI)
- Growth in air traffic and passengers considerably higher than EU average
- Sustained period of stable interest rates
- One of the lowest corporate

- tax regimes in the EU
- Phased accession to Schengen Agreement (see box below) scheduled for January–June 2008
- Adoption of Euro likely within the next five years

The Schengen Agreement came into effect in 1995 and is a multilateral agreement among EU states allowing for the abolition of border controls between participating countries and, more specifically, a common policy for the temporary entry of persons, harmonisation of external border controls and cross-border police and judicial co-operation.

Many Hungarians anticipated that EU

accession in 2004 would bring immediate wealth and Hungary would become the economic hub of Central Europe. Now, the post-accession euphoria has calmed down and the government has realised that it has work to do. The government is dedicated to joining the Euro, although it needs to fix Hungary's current budget deficit (running at around 6.5% of GDP) and government debt (currently 68.0% of GDP); the corresponding Euro accession criteria are 3.0% and 60.0%,

In 2005, the Economic Intelligence Unit listed Budapest as the most liveable city in CEE and cited improved transport and communications infrastructure as being significant in "slowly bringing these eastern European cities into line with the west".

With around two million people, this grand city is only a few hours drive from Vienna, Bratislava and Prague and is becoming a key conduit between Western and Eastern Europe.

“As the time draws nearer for Croatia to enter the EU, predictions suggest property prices could be set to rise”

which Morgan Stanley recently predicted Hungary should meet between 2010–12. In order to do so, Prime Minister Ferenc Gyurcsány launched his '100 steps' reform programme through which he strives to 'slim down' bureaucracy and cut taxes by the equivalent of 5% of Hungary's annual GDP over the next four years.

Gyurcsány's challenges were increased following the unrest in the latter half of 2006 brought about by his admissions that he misled the electorate about the state of the economy. This issue died down and the Hungarian Forint strengthened against the Euro by 15% immediately thereafter before settling within its 'natural' trading band of 248–255.

Hungary has attractive economic growth and development potential: its low corporate tax regime (flat tax of 18% on profits and no withholding tax on dividend or interest payments) presents tax-efficient investment opportunities to foreign investors.

Budapest

Budapest is an interesting and stylish city with many impressive landmark buildings and cultural attractions. The Danube adds great character, complemented by surrounding hills, forests and natural thermal spas, the beauty of which make Budapest a highly attractive place to work and live. UNESCO has awarded four central sites World Heritage status.

Infrastructure is developing fast and low-cost carriers operate between most major EU destinations and Budapest thereby encouraging new segments of its population to travel; Hungarian air traffic is anticipated to double by 2009.

Skilled labour costs are lower than many of the more established EU member states and many international corporations including Samsung, BT and Morgan Stanley have recently invested significant capital and management resources to join the likes of PWC, Deloitte, Citibank, Audi and Vodafone in Budapest, which has been a boon to its property market.

Many real estate investment opportunities exist throughout Hungary, but the Budapest residential market attracts particular interest given its relative ease of navigation and transparency for foreign investors.

Stock falls into one of four broad categories: Golden Period (1850–1910), Bauhaus (1920–35), Soviet-style (1950–80) and new stock, of which there has been a surge over the last few years. Newer developments cater for the lower to middle market and often lack the style of their gracious Golden Period counterparts, many of which are in poor condition but should prove to be good acquisition targets. Renovated homes in older buildings seem to be coming back into vogue, particularly those with historically or architecturally noteworthy features.

Hungary no longer operates the restitution system established by the first

Farrell's facts

Population:

9,956,108 (July 07 est.)

GDP per capita: \$13,560

Interest rate: 7.5%

Inflation: 7.4%

Unemployment: 7.3%

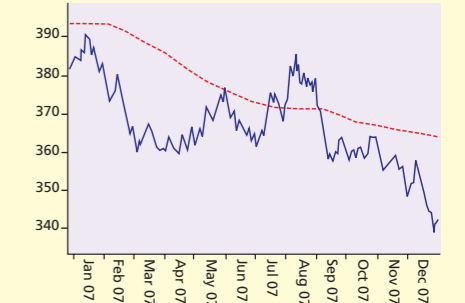
Foreign Direct Investment in millions (US\$): 8,760 (2006)

Tourist Trends:

Tourist arrivals: 9.3 million (2006)

International Tourism Receipts (€ bill): 4.5 billion (2006)

Daily Exchange Rates: Hungarian Forints per British Pound



Taxation:

Income tax: 18 - 36%

Corporation tax: 16%

Capital gains tax: 25%

Value added tax: 20%

Climate:

Hungary has a temperate climate. July and August are the hottest months. The coldest months of winter are usually January and February.

Average annual temperature: 11°C

July is hottest month at 23.2° C and January the coldest (-1.3° C).

Average winter temp.: 1 - 10°C

Carriers:

Direct Routes:

Budapest: easyjet, Wizzair, Aer Lingus (Europe), Ryanair, Jet2, BA, Malev Hungarian Airlines

Balaton: Ryanair

Focus on HUNGARY

post-communist government; antecedent title claims were only accepted within a 10-year window (closed in 1999). Now, most properties are registered with the central property registry and the system of title transfer is transparent.

Estate agents are a reasonable starting point to finding a good property, although they are unregulated and, as is true of their counterparts throughout Europe, it is unclear whose interests they really represent. Typically, agents charge sellers a hefty premium of 4–5%, although with some negotiation this fee can (and should) be revisited. The internet and local newspapers are good alternative starting points as sellers increasingly embrace these media to advertise their properties.

Legal fees for one-time purchasers typically range from 0.5–1.0% of the purchase price. 'Tourists' might receive fee quotations of 1.5%, although this should be resisted unless a transaction is particularly onerous. Not all Hungarian lawyers speak business-level English and care should be taken to instruct reliable and trustworthy counsel, particularly before granting a power of attorney to sign purchase and other documentation which is commonly requested. Estate

agents' 'recommendations' are generally best avoided.

Stamp duty is charged at 2% of the purchase price for properties under HUF 4 million (€16,000), thereafter the applicable rate is 6%. If the purchaser is a 'qualifying entity' (i.e. a company whose main activity is real estate trading), the lower rate will apply to the entire purchase price provided the property is resold within two years of purchase.

Foreign buyers traditionally comprised the Israeli, Irish, German and British contingent but are starting to include more Spanish, Chinese and Russian investors. Nonetheless, Budapest property prices remain quite low, even in downtown areas, and lag behind Vienna, Prague and even Bucharest, but are widely anticipated to catch up as the Hungarian economy picks up.

Prices vary with each district – the smartest spots are sited within Districts 1 and 5 with surrounding areas becoming increasingly gentrified. Unrenovated property generally sells for €1,000–1,500 per square metre whereas middle-range renovated property typically sells for €1,500–2,500 per square metre. Higher-end units can command €3,000 per square metre, although better deals

can be found through smaller, more entrepreneurial and creative developers.

Current market cap rates for decent residential property seem to average around 6–7%, although care should be taken to see whether yields offered by developers to retail investors are actually net or gross; a little careful analysis to ascertain what costs have been included or left out can serve to filter genuinely decent investment opportunities from slightly 'dressed up' ones.

So, should you invest your money in Hungarian property? Hungary is one of Europe's most exciting prospects and Budapest is without doubt one of its great cities, its wonderful views and vibrant nightlife making it attractive to Hungarians and tourists alike. There are economic and political hurdles for Hungary to overcome but for the investor its favourable tax regime, beautiful housing stock, relative political stability and solid economic growth make it a good long-term bet.

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