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BUSINESS

Downturn, Debt Slam Greek Builders

Global Recession and Nation's Financial Crisis Force Property Companies to Rethink Projects and Look Abroad

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The global economic downturn and the sovereign-debt crisis have forced Greece's property developers to put the brakes on some ambitious projects after a flurry of construction on shopping malls, residential homes and leisure parks for tourists.

The weak economy and the sharp fall in spending on public infrastructure and residential and commercial-property construction have hit Greece's builders hard. The continued government-debt crisis will help prolong the pain at least through 2011, say economists.

"The crisis is likely to continue for some time," says Claude Giorno, head of the Greece desk at the Paris-based Organization for Economic Cooperation and Development. "The question is, how solid are the companies, and will they be able to adjust?"

Judging by data from the construction industry, many building companies are already collapsing. The Association of Greek Contracting Companies (SATE), which represents the country's builders, says 58 construction companies went bust last year, a 10-year high, after 17 insolvencies in 2008 and three in 2007. And the outlook for the coming years is grim.

Larger builders, such as Ellaktor SA, Greece's largest construction group by sales, are compensating for declining domestic revenue by going abroad. In its latest financial report, for the first nine months of 2009, Ellaktor reported a 36% increase in revenue, to €1.3 billion ($1.8 billion). But as much as 30% of its revenue was generated outside Greece.

"The large companies are able to compensate for the loss of domestic business with their international sales," says Spyros Mountrouidis, managing director of SATE, the Greek builders' association. "But the majority of companies have no construction activity outside Greece."

The residential housing market has come to a halt.

During the building boom—from the time of the preparations for the 2004 Summer Olympics, which Greece hosted, until 2007—local authorities issued 70,000 to 80,000 building permits for residential homes every year. Statistics from the Bank of Greece show that, at the end of 2009, the volume of outstanding housing mortgages was €80.6 billion, of which €12.6 billion were securitized. And there is an overhang of about 250,000 new homes that were completed but not sold.

Commercial real estate has also been hit hard. In the Athens central business district, the country's most important market for offices, monthly rents for the best space fell 30% from the peak of the cycle in 2007 to €26.50 a square meter ($3.35 a square foot), its level today, says Dika Agapitidou, director of Athens Economics Ltd., which represents property consultants Jones Lang LaSalle in Greece. In the area around Kifissias Avenue, where foreign multinational corporations tend to settle, prime rents fell 19% during the same period, she said. Office vacancy rates in Athens have risen to 12% to 14% on average and have reached 20% in softer markets in the south of Athens.

The weakening of office markets is reflected in rising capitalization rates, which show the relationship of commercial property's cost and cash flow. A low capitalization rate indicates prices are rising, and higher rates suggest falling prices. At the end of December, before the sovereign-debt crisis emerged at the beginning of 2010, capitalization rates on prime offices had risen to 7.25% from about 6% at the peak in 2007.

In spite of the economic uncertainty, some development projects are moving forward.

Real Estate Development and Services group (REDS), a subsidiary of Ellaktor, is developing Greece's largest retail project, the Yialou retail park 15 kilometers (nine miles) outside Athens. Private-equity group Henderson Global Investors Ltd. agreed in 2007 to buy the park upon completion. Construction is scheduled to begin once prelease agreements have been signed with retailers. "We've rented about 30% so far. We're not finished, but we are in a good position," says Anastasio Yanthakos, a senior executive in charge of leasing.

Another promising area for investors is developing Greece's idyllic coastline. Dolphin Capital Partners, a private-equity group founded by Miltos Kambourides, started work three months ago on a project to build 10 resorts with luxury hotels, golf courses and adjacent residential communities. Dolphin has financing in place for the first €300 million of the €2 billion development. The first hotel and community is scheduled to open in 2012, says Mr. Kambourides. "This is a totally virgin market in Greece," he says.

One of the most active property sectors has been the retail industry. The first major mall to be built in Greece was Mediterranean Cosmos in Thesaloniki, the country's second-largest city after Athens. The mall was a joint venture between Lamda Development SA; Sonae Sierra, a Portuguese developer; and Acropole-Charagionis, a Greek developer. Mediterranean Cosmos opened in October 2005.

Not all of the planned mall projects have gone so smoothly. In 2006, Sonae Sierra and Acropole-Charagionis, one of the oldest family-owned companies in Greece, unveiled plans to convert the Galatsi Olympic Hall into a shopping and leisure center with 38,500 square meters of leasable space. The Galatsi hall hosted table-tennis and rhythmic-gymnastics competitions during the 2004 Summer Olympics. It was originally expected to open its doors as a modern shopping center in the second half of 2008, but, because of delays in obtaining permits and deteriorating economic conditions, construction still hasn't begun.

Tiago Eiro, Sierra's general manager in Greece, says the financial crisis has forced the company to review the timing of projects in its development pipeline. "We intend to start construction soon," he says, adding: "We cannot accurately confirm some of the opening dates."