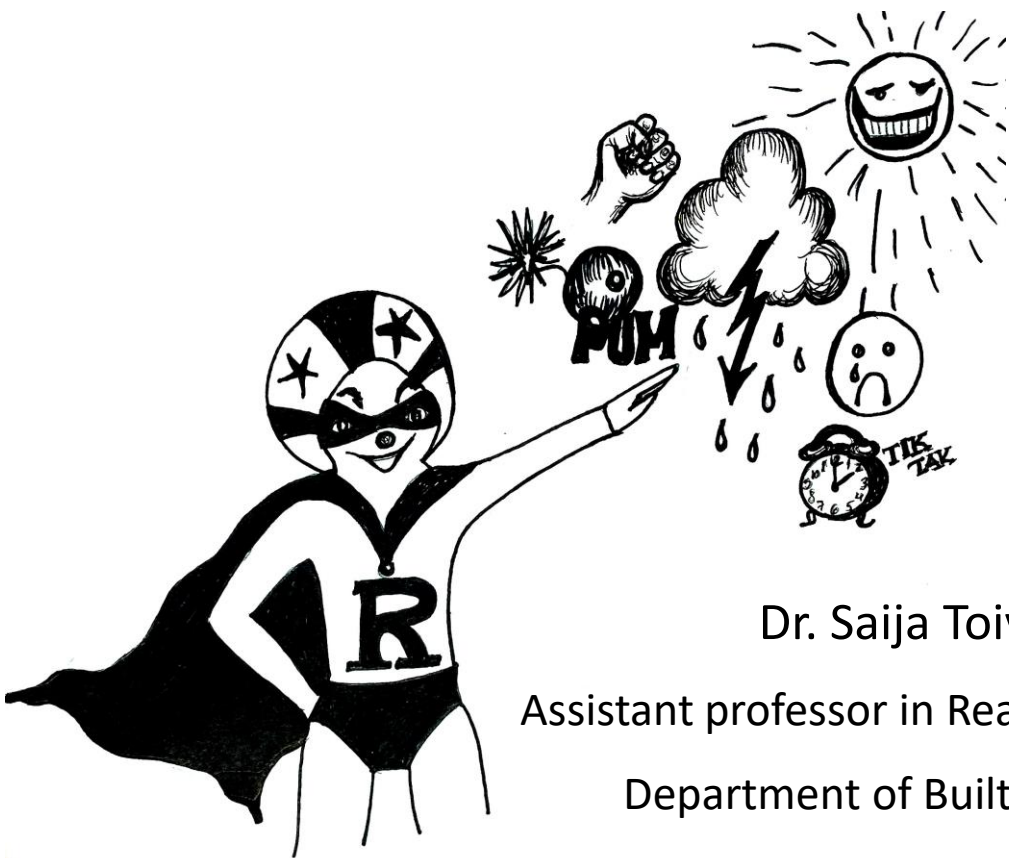


33RD BALTIC VALUATION CONFERENCE

CRISIS IMPACTS AND PERCEPTIONS OF REAL ESTATE MARKET PARTICIPANTS



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Greetings from
**The Finnish Association
for Real Estate Valuation**



Real Estate and Sustainable Crisis Management in Urban Environments RESCUE



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 - Consortium leader, Ass. Prof. in Real estate Economics Saija Toivonen
- **Aalto University, School of Arts, Design and Architecture, Department of Architecture:**
 - Prof. of Urban and Regional Planning Kimmo Lapintie
 - Post Doc Johanna Lilius
 - Prof. of Health and Wellbeing Architecture Laura Arpiainen
- **University of Turku, Finland Futures Research Centre:**
 - Prof. in Futures studies Markku Wilenius
 - Prof. emerita in Futures studies Sirkka Heinonen
- **Tampere University, Faculty of Built Environment:**
 - Ass. Prof. in Sustainable housing design Sofie Pelsmakers



FUTURE CRISES FOR REAL ESTATE MARKET ENVIRONMENT

- Many and increasing...
 - We have typically relied on probabilistic approach and narrowed down the number crises to be monitored.
 - Interconnectedness and rapid changes (e.g., riots, cyber attacks)
 - Actualization vs. fear of (e.g., fear of war, wildfires)
- Characteristics vary
 - Megatrends (e.g., urbanization)
 - Trends (e.g., hyperinflation, lack of workforce)
 - Weak signals (e.g., extreme spatial segregation, AI is no longer controlled by humans)
 - Wild cards (e.g., wide mistrust towards/unpredictable legal system)



SEVERAL CRISES → VARIETY OF IMPACTS

• CHARACTERISTICS:

- **Material** capacities (e.g., physical destruction of building materials, capacity of wastewater infrastructure, availability of space)
- **Immaterial** capacities (e.g., data, knowhow, networks, values)
- **Disturbances** (e.g., availability of data, transportation connections, unsuitable indoor conditions)
- **Total collapse** (e.g., lost of lives, no access to electricity)

• TIMEFRAME:

- **Immediate** collapse (e.g., terrorist attack, natural hazard)
- **Slowly** developing (e.g., significantly rising levels of alienation/marginalization, shrinking cities)

• CAUSALITY:

- Flood → 1st level impact: Physical destruction
- Riot → 1st level impact: Physical destruction
- Shrinking cities → 1st level impact: Unfavorable value development → 2nd level impact: Lack of repairs → 3rd level impact: physical destruction



PERCEPTIONS OF REAL ESTATE MARKET PARTICIPANTS IN A CRISIS SITUATION

- **Aim:**
 - to deepen the understanding of how the impacts of crisis are perceived in the real estate market context, using COVID-19 as a case.
 - COVID-19 has been particularly challenging for the real estate sector which makes it therefore an ideal crisis to study (Naz et al. 2022)
- **Objective:**
 - to identify the factors influencing market dynamics, such as market sentiments, preferences, and procedures.
- **Methods and data:**
 - Semi structured interviews (04/2020 & 9/2021) with 19 real estate market professionals in Finland (incl.10 authorized valuers)
- **Contribution:**
 - to understand the diversity of crisis impacts, their interconnections, and how they are perceived.
 - contribute to the real estate literature by offering a qualitative perspective that supports individuals and organizations in developing risk and crisis management skills
 - to build a more resilient real estate market to support communities.

(Toivonen et al. 2023)

Background

- Typically, real estate is considered a rather high-risk business. Risk = potential for economic loss (Brueggeman & Fisher, 2011; Graaskamp, 1981).
- Several ways to categorize and manage risks (e.g. due diligence, market and property analysis, insurance, agreements, and diversification) (e.g. Brueggeman & Fisher, 2011; Kaleva et al., 2017).
- There is a lack of understanding of market sentiments, perceptions, and preferences of real estate market actors when a crisis situation has been faced and the risks have been actualized.
- The limited understanding may prevent learning the lessons of a crisis and building resilience capacity (Allen & Holling, 2010; JLL, 2022).



Market sentiment

- **Sentiments as market drivers**

- Market sentiment played an important role in the RE market
- Prudence among buyers and sellers → projects put on hold
- The market sentiment followed closely the local cyclical nature (waves) of the pandemic itself. However, local impacts spread and were indirectly felt in the global context.

- **Resource dependency**

- When **financing** was not available, those who possessed their own equity garnered significant market benefits and could continue their activities as usual.
- Lack of **market evidence/data** was seen to result in a vicious circle.
- Misleading market statistics due to delay.

- **Inconsistency**

- Observations of market decisions that were not necessarily rational.
- Uncertainty and negative atmosphere were also reflected in sectors not directly affected by the pandemic or its countermeasures.

Market preferences

- **Investment preferences:**
 - **Core type of investment** targets were preferred
 - **Segregation** within and between sectors and properties increased
- **Space preferences:**
 - Space related decisions were **postponed**
 - Employers willing to invest more in the **quality of spaces**, but unsure about the quantity
 - Technical and functional **flexibility:**
 - The layout, increase/decrease and flexible lease agreements
 - Attention to ability to be adapted for different uses and different users.
 - **Safety**-related space requirements, including hygiene, ventilation and air quality, antibacterial materials, and room for physical distancing

Market procedures

- **Transactions**

- Physical visits to properties → virtual site visits
- Travel restrictions vs. domestic actors
- Prolonged leasing processes
- Procedures and legal guidelines differed between countries → variation between countries
- E.g. force majeure policies implemented in rental agreements.

- **Valuation procedures**

- Increasingly careful consideration of property sector type and the viability of the tenant
- Implementation of a novel clause in real estate valuation reports reflecting the uncertain times (modified according to the pandemic's development and its impact on various asset types).
- Difficulty to decide when the changed market situation became the “new normal”

- **Closer collaboration**

- Investors and asset managers: more attention to their tenants' business viability and more systematic ways to evaluate tenants and their ability to pay rent (monitoring of KPIs, credit ratings, and solvency).
- Owners engaged more actively with their tenants and showed greater interest in their future plans and coping mechanisms.
- Tenants sought flexibility in their rental payments (e.g., free months and discounts), and keen to sign shorter leases, even with higher rents with the aim of transferring risk from tenants to owners. (Toivonen et al. 2023)

Lesson learned

- Also, **positive impacts**:
 - e.g. new opportunities that would not have emerged without the pandemic.
 - A new spirit of collaboration among market actors (e.g., real estate valuers, real estate owners, and tenants) → Could increase the transparency and resiliency of the market environment.
- Waking everyone to **the possibility of sudden, powerful shocks** and highlighting the importance of risk management, a future-oriented perspective, and preparatory activities.
- **Broader understanding of new potential risks** as crises do not necessarily emerge within the real estate field or affect its diverse sectors equally.
- Analyze **secondary level risks, their interconnections, and their simultaneous effects**.
- COVID-19 crisis increased learning and enhanced resilience to future risks.

(Toivonen et al. 2023)

THANK YOU 😊

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