

Demographics: As good or as bad as it could be for the Baltic Real Estate Market?

Demographics are usually (mis)quoted as one of the main, if not the main, obstacle for the real estate market development in the Baltics. Indeed, over the last 10 years population in the Baltics declined by 10% and are projected to decline by another 3-12% in the next 10 years. However, just as measuring an average temperature in the hospital may lead to false conclusions, so does the statement about demographics and real estate market developments just by looking at aggregate figures.

Who is buying real estate? Population aged 25-39 year old are by far the most active residential real estate market participants in the Baltics. Together they account for more than 70% of all newly issued housing loans (between 2007 and 2014), which is significantly higher than the euro zone average of 45% (ECB, 2007). Hence, in analysing the linkage between demographics and real estate market development one should primarily look at 25-39 years age category.

Can they afford it? Young professionals aged 30-39 years can boast themselves having the highest earnings in all three Baltic States. This is in sharp contrast with Western European countries, where citizens in their mid-50s or even 60+ (e.g. Italy, France) generally earn the highest income. In addition, even aged below 30 years earn close to average salaries compared to a mere 60-70% in most Western European countries. Hence younger generation in the Baltics have much higher relative purchasing power than in the Western Europe and are playing more active role in residential real estate market.

Are there enough buyers? The share of 25-39 year olds in the Baltics is close to the EU average. Hence, contrary to widespread belief, demographic situation in the Baltics is not worse than in the other EU countries. In fact, the share of 25-39 year olds is higher than in Scandinavia and most of “ageing” Western European countries such as Germany, Italy or France thanks to considerably higher birth rates in the 1980’s.

Which Baltic State has the most favourable demographics? The share of 25-39 year olds in the Baltics would have been similar if not international migration, which significantly reduced the number of potential housing market participants – especially in Lithuania and Latvia. As a result, Estonia has the most favourable demographic situation, while Lithuania – the least favourable with Latvia positioned in the middle. However, overall demographic situation is of little help in explaining differences in real estate market developments, since majority of transactions is taking place in capital cities.

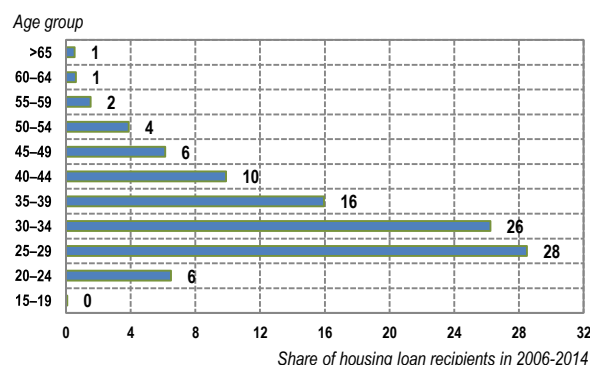
Population change, (in millions)

	2005	Δ, %	2015	Δ, %	2025*
Total Baltics	6.96	-10.7%	6.22	-3.1%	6.05
Lithuania	3.36	-3.4%	2.92	-2.9%	2.85
Latvia	2.25	-11.7%	1.99	-4.2%	1.91
Estonia	1.36	-13.9%	1.31	-2.0%	1.29

Source: Eurostat

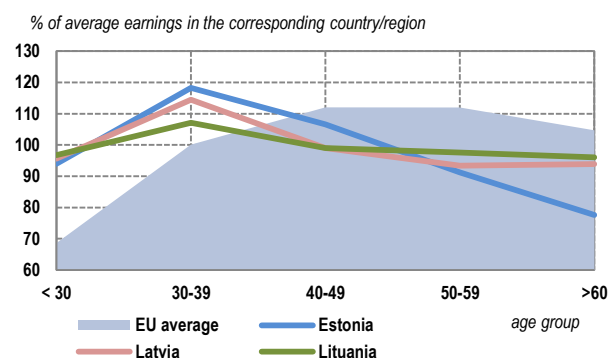
*No migration scenario (EUROPOP 2013 population projections)

Most active in housing market: 25-39 year olds



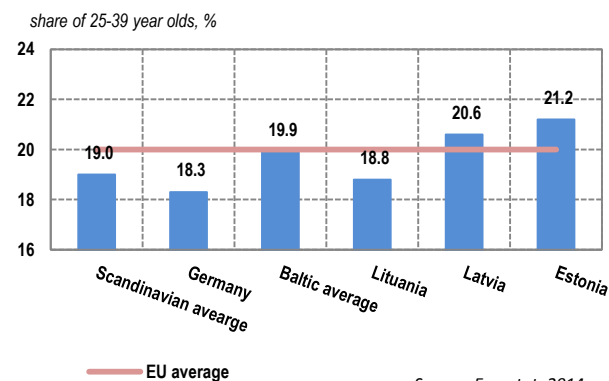
Source: Nordea

Young professionals are the highest earners



Source: Structure of Earnings Survey (Eurostat, 2010)

Share of 25-39 year olds is similar to EU average



Source: Eurostat, 2014

Vilnius is not Lithuania, Riga – not Latvia and Tallinn – not Estonia. Baltic States are characterized by unusually high concentration of economic power in capital cities: Riga generates 67% of Latvian GDP, Tallinn – 61% of Estonian and Vilnius – 39% of Lithuanian. Residential real estate market activities are even more concentrated. For example, in 2015 more than 80% of all newly build apartments in Lithuania will be built in Vilnius. Hence, in analysing real estate market developments one should look at demographics of capital cities.

Which Baltic capital has the best demographics? Due to an ongoing inward migration, the overall demographic picture in Vilnius, Riga and Tallinn is much better than in other regions. The share of 25-39 year olds not only exceeds EU average levels, but is also higher than in most other EU capitals. For example, Tallinn has more 25-39 year olds than Oslo, Stockholm, Helsinki or Copenhagen.

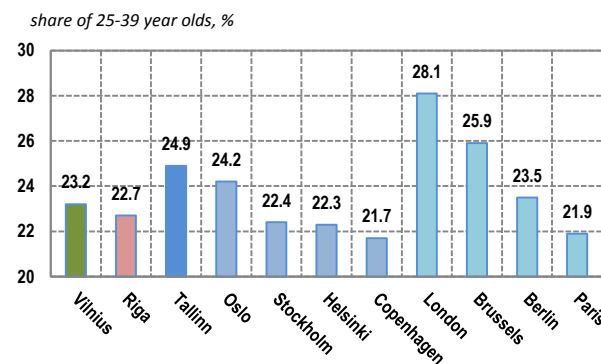
It's all about domestic migration. Tallinn and Vilnius are doing better job than Riga in retaining and attracting migrants. For example, population in Vilnius and Tallinn increased by 2 thousands due to positive net migration (international and domestic), but declined by 900 in Riga in 2014 alone. As a result, population aged 25-39 is growing steadily in Vilnius and Tallinn, but not Riga. Vilnius is also the youngest capital city having the highest share of 15-24 year olds youths (11.8%) compared to Tallinn (9.7%) and Riga (8.9%), which should sustain real estate market activity in the upcoming 5-10 years.

Will Vilnius become the largest city in the Baltics? If tendencies will continue, Vilnius may become the largest city in the Baltics in 10-15 year period. In fact, Vilnius already now has higher absolute number of youths (15-25 year olds) than Riga (+7 thousand), while Riga has significantly higher number of pensioners (+43 thousand). Vilnius also has the highest inward migration potential due to significantly higher number of youths (15-24) living outside the capital city (313 thsd in Lithuania vs. 156 thsd in Latvia and 98 thsd in Estonia).

Do demographics is of any help explaining recent real estate market developments? Yes. Vilnius and Tallinn have significantly higher number of transactions than Riga. In addition, Vilnius is leading by new construction activity followed by Tallinn and Riga. Finally, average real estate prices in Vilnius and Tallinn are also significantly higher than in Riga – in nominal as well as GDP-adjusted levels. Hence, it is not economic developments, but rather demographics that have the highest influence on real estate market developments.

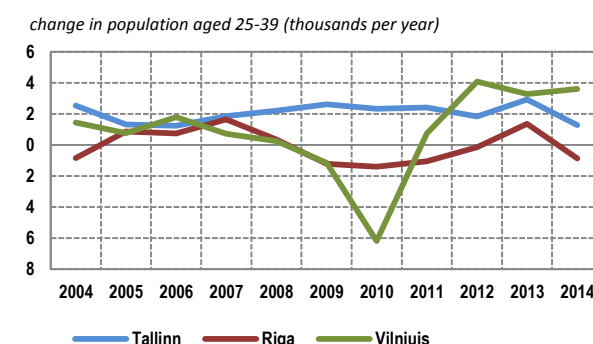
As good or as bad as it could be? Given large share of 25-39 year olds and ongoing inward migration, demographic situation in Vilnius and Tallinn is supportive for real estate market developments, while Riga has to try harder in attracting and retaining migrants.

Baltic capitals are no worse than European ones



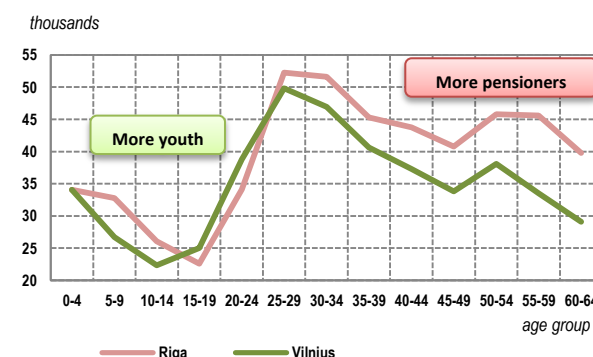
Source: Eurostat (2014, NUTS)

Vilnius is the fastest growing city in the Baltics



Source: National Statistics

Vilnius will become the largest city in the Baltics



Source: National Statistics

Number of competed apartments

	Vilnius	Riga	Tallinn
Population (thousands)	540	641	414
# of apartment transactions (Jan-Sep, 2015)	6971	6250	6363
Per 1000 population	12.9	9.8	15.4
compared to 2014, %	(-6%)*	(-10%)*	(+16%)*
New apartments build (2014)	2900	900	1100
Per 1000 population	5.4	1.4	2.7
New apartments build (2015)	4000	1400	1800
Per 1000 population	7.4	2.2	4.3
Average apartment prices (EUR/sqm)	1320	1050	1560
Per GDP per capita	0.90	0.64	0.79

Source: Oberhaus, 2015

*Number of transactions in Vilnius increased by as much as 18% y/y in 2014 Jan-Sep driven by euro introduction.

What can go wrong? Demographic situation is highly dependent on migration: both international and internal. Hence, the future of Baltic demographic situation in general and housing market in particular will depend largely on how Baltic countries will manage to convince 25-39 age olds from not emigrating abroad or at least choose inward migration by moving to the capital cities. The success of this endeavour will to a large extent depend on housing affordability and availability. Hence, it should be well understood that without affordable housing Baltics will inevitably face increased emigration and with increased emigration – no demand for affordable housing. I wish that this “chicken and egg” dilemma would be solved in favour of ample affordable housing and little or no emigration rather than ample emigration and little of none affordable housing.

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Population change in regions between 2012 and 2015 (25-39 year olds)

