Real Estate Investment Management and Macroeconomic Sustainability: Case of Latvia and International Experience

Linda Kauškale, Ineta Geipele
Institute of the Civil Engineering and Real Estate Economics
Riga Technical University
Riga, Latvia
Linda.Kauskale@rtu.lv; Ineta.Geipele@rtu.lv

Abstract— Macroeconomic sustainability is a complex indicator that influences the wealth of each country. It significantly depends from economic fluctuations and variety of other aspects. Macroeconomic environment influences the volumes of real estate investments and investment decision-making. The aim of the research is to define interconnection between real estate investments and its management and macroeconomic stability. Comparison, quantitative data analysis and logical access methods have been used in the research. The results of the research can be used by real estate investors, real estate sector representative and other market participants.

Keywords— real estate market; investments; management; sustainability; macroeconomic stability

I. INTRODUCTION

Macroeconomic sustainability is influenced by implemented fiscal and monetary policy in the country. Macroeconomic sustainability significantly depends from economic fluctuations and variety of other aspects. The aim of the research is to define interconnection between real estate investments and its management and macroeconomic sustainability. The role of information shocks and variety of other related aspects are analyzed as well. Comparison, quantitative data analysis and logic access methods have been used in the research.

Open-system theory nowadays has a great importance on entrepreneurship, as influence of variety of external factors on organization is without controversy. Traditional monetary theories interpreting monetary movements as a primary source of impulses to real activity, and they are key to understanding market failures, and this should be important aspect of macroeconomic analysis [1]. Real estate price shocks have a crucial role for real estate investors and investment decision making. It was analyzed, that house prices can be influenced also through mortgage market measures, but this influence is limited, and also other exogenous reasons are the reasons of house price boom [2]. At the same time a monetary policy shock depends from real estate investment returns and changes in economic growth are also connected to a fall in REIT returns, as inflation news result in lower REIT returns, because an aggregate price shock is expected [3].

Many globalization theories devote attention to the nature of global flows and special attention is being paid to their internal relationships, and nowadays global cities are often viewed as units that passively convey and transmit flows [4]. A large price jumps exist on the international securitized real estate markets in crisis and non-crisis periods [5]. For example, there still can be found that there is a correlation between economic crisis and skyscraper index – they mark a boom that is followed by recession [6]. The financial crisis once again showed, that negligence of real estate booms can have disastrous and far-reaching consequences, mainly because of increased leverage in the real (households and construction sector) and financial sectors [7]. Big part of institutional owners is holding commercial real estate for long-term estate transactions, unlike residential real estate markets and its different methodologies to solve illiquidity problems [8]. Different tendencies in investment management can be found not just between different real estate sectors, but also between different real estate markets worldwide.

II. THEORETICAL PART - AN OVERVIEW

Despite a progress in forecasting techniques, there still are challenges in customer demand forecasts and price uncertainties at the supply end also exists, that is why effective management of demand and supply uncertainty is important in each company to keep customers satisfied at lower costs [9]. There is heterogeneity in real estate investment cost and total performance, mainly determined by mandate size and an investment approach [10]. However, international investors face a number of risks, and risks associated with real estate in general are (Investing in international real estate [11]:

2. Financial risk.
3. Liquidity risk.
4. Inflation risk.
5. Management risk.
6. Interest rate risk.
7. Legislative risk.
8. Environmental risk.

The key determinant of macroeconomic stability is trust - it lowers macroeconomic volatility and cyclical character of investments [12]. Quick reaction to news is one of the most important characteristics of asset prices [13]. Trust and power imbalance between buyer and seller impacts asymmetrical allocation of specific investments [14]. Macroeconomic news have economically and statistically significant impact on credit markets by increasing spreads, especially news from U.S., Eurozone and China [15]. Also urban process, as a process of generating novel development, is inseparable and depends on the availability and spread of information [16]. For instance, Sweden, Finland, Norway, and the United Kingdom all have integrated real estate information systems, data is available and it also allows data exchange and improves the management [17]. A little systematic mispricing of commercial real estate derivatives relative to REIT equity during the recent financial crisis can be found and the market temporarily overreacts news announcements [18].

At the same time homeownership often impairs the labour market, on example of Germany as unusually low homeownership and low level of unemployment –and it has implications for Spain and Italy – countries with high homeownership and high unemployment level [19]. For the comprehensive macroeconomic policy realization also impact of labour income on aggregate demand and its interaction with monetary policy should be analyzed, because reduction of wages in crisis can even arrogate it [20]. One of the crisis management recommendation in Lithuania is a reduced value added tax for the entire home-building sector – to maintain and extend it [21]. For example, a cap-and-trade policy is also one of the automatic stabilizers of the economy, dampening business cycle fluctuations [22].

International real estate investments are gaining wide currency worldwide and recipients of international property investment more often are developed countries, because that many developing countries are concerned as too risky, but also a reverse flows are observed, as the former has comparative advantages in skills, technologies and capital [23]. By analysis of 20 national real estate markets, was found that a huge number of linkages between national markets stay from one time to the next, but the long-term stability of the international real estate securities’ correlation structure in markets descends during some time period [24]. On the example of Argentina, external financial liberalization affects welfare and increase volatility more than domestic liberalization, but at the same time it also mitigates the impact of domestic deregulation [25]. There is a positive association in 36 countries (OECD and emerging markets) between the appreciation of real estate valuation and the growth rates of credit and increases in current account deficits (as fractions of the GDP) [26].

Impact of cycles should not be ignored or over-simplified, because they are a major determinants of business success or failure, that is determined by their impacts on real estate returns, investment values and risks over the time, so portfolio managers should develop and implement strategies to diversify by cities, countries and submarkets that have different micro and macro cycles and different development tendencies [27]. The diversification benefits can be found also for Australian investors that can be achieved by adding real estate investment to a share portfolio, including a diversification into residential and commercial real estate [28].

The company's activities are required to implement anti-crisis management from the outset; this is not only for overcoming the crisis, but as a complex of activities, also at early stages of problem development [29]. Ideal development team, in which developer directly communicates with [30]:

- Capital provider.
- Acquisition officer.
- Analyst.
- Portfolio manager.
- Asset manager.
- Property manager.
- Finance and accounting.
- Administrator.
- Attorney.
- Environmental consultant.
- Architect.
- Surveyor.
- Planning and zoning.
- Title officer.
- Brokers.
- Investment comittee.

At the same time, investments in real estate market and construction industry are of great importance because of their influence on overall national economy development [31]. During analysis of 1997 Asian financial crisis was found that Asia-
Pacific property markets are integrated, despite a fact of structural shift occurring at the time of the Asian crisis, so this is a particularly important finding for fund managers, to analyze the impact of globalization in their real estate portfolios [32].

In China the housing price effects on entrepreneurship are large and statistically significant, in opposite with situation in U.S., and there may be large negative effects in terms of discouraging entrepreneurship [33]. Foreign direct investments also have taken important role in the recent China’s economic success [34]. For instance, as a result of Europe-China dialog on energy issues, Chinese Go Global policy and Chinese energy policy, foreign direct investments become an important aspect of regional integration between China and Europe [35]. Macroeconomic sustainability has a great influence on real estate investments and has an important role in the development of each country at all levels of researches.

III. PRACTICAL RESEARCH

Investments can promote economic growth, but at the same time, economic growth in some particular regions also can attract real estate investors, as such factors are influencing investment portfolio management significantly. There are three main reasons that pursue growth: growth is seen as a progress, there is a necessity to avoid economic instability and recessions, and it is necessary for a compensation of labour productivity improvements which otherwise can cause structural unemployment [36]. Growth rates of regions, where they plan to invest their funds, is an important indicator for international investors for decision making. Real GDP growth rates by economies are shown in Figure 1.

Figure 1 shows, that one of the highest real GDP growth rates in 2016 and 2017 are planned to be in South Asia. Still high growth rates are forecasted to be in East Asia and Pacific region, followed by Sub-Saharan Africa region. Countries with higher growth rate can be more attractive for international investors. The highest real GDP growth rates in general in period from 2013 to 2017 (forecasts) have low income economies; next highest real GDP growth rates have BRICS countries (see Figure 2).
Figure 3 shows composition of growth in European Union in 2014, 2015 and 2016. Annual rate of change of investment, as well as volume of exports and final demand in European Union is planned to increase, which is a positive development tendency.

The highest foreign direct investment intensity in Baltic States in analyzed period was observed in Estonia (see Fig.4). This indicator can also show a level of competitiveness of countries in field of attraction of foreign direct investments. The highest foreign direct investment intensity between European countries has Luxembourg (968.6), Malta (92.5) and Belgo-Luxembourg Economic Union (74.5). Other European countries are represented graphically in Figure 4. Ireland, Hungary, Montenegro, Estonia, Switzerland and Sweden has high market integration indicators, but Iceland, Denmark and Slovenia have even negative index. Figure 4 shows foreign direct investment intensity in European Union in 2012.

In national economy development, the highest investment ratio to GDP in Latvia has corporations or business sector, and their decisions can affect demand shocks. However, in real estate market also government investments and households have a great role. Investment ratio to GDP in Latvia is shown in Figure 5.
Real estate investment volumes also influence real estate price level. The most rapid house price growth in Baltic State countries had Estonia, then follows Latvia and Lithuania. The growth of real estate prices in Baltic States was higher than average house price index in European Union in analyzed period. Housing price index by quarters is shown in Figure 6. Reduction in real estate prices in 2014Q4 and 2015 Q1 in Latvia, as a reaction to reduction in demand and foreign real estate investment volumes, is observed as well.

Number of registered real estate purchase agreement shows the number of real estate deals and can show the trends in real estate investing as well. Number of registered real estate purchase agreements is shown in Figure 7.
Capital and liquidity buffers could be used to soften financial system and the economy, by using effective macroprudential policy [41]. In international real estate investment analysis money market interest rates have a significant role as well. Figure 8 shows monthly data of money market interest rates in Euro area, United Kingdom, United States and Japan.

![Money market interest rates - monthly data, 3 months rates. Data: Eurostat [39], figure made by authors](image)

Significant for international real estate investors are the changes of money market interest rates nowadays. In comparison with period from 2004 to 2008, the development tendencies in world economies have changed. Each new cycle has its own peculiarities, but anyway, a special attention always should be paid to financial markets analysis.

One of the important indicators that show structure of income distribution in the country is Gini index. Gini index in Baltic States it is higher than average Gini index in European Union, and in most of years highest Gini index between Baltic States countries was observed in Latvia. Gini coefficient of equivalised disposable income is shown in Figure 9.

![Gini coefficient of equivalised disposable income (scale from 0 to 100). Data: Eurostat [39], figure made by authors](image)

Ministry of Finance of Republic of Latvia [42] forecasts 3.6% GDP growth in Latvia in comparable prices in 2018 that in general is a positive development tendency. As macroeconomic stability and real estate investments are interrelated indicators, for successful sustainable macroeconomic development, special attention should be paid to both of them in policy planning.

IV. CONCLUSIONS

In the research the real estate investment management and macroeconomic sustainability question were analyzed, including analysis of situation in Latvia; international experience was analyzed as well. Exogenous factors have a great significance in real estate investment portfolio management and decision making, and they cannot be ignored. Macroeconomic sustainability is a complex indicator that influences the wealth of each country. Real estate investment
volumes also influence real estate price level, reduction in real estate prices in 2014Q4 and 2015 Q1 in Latvia, as a reaction to reduction in demand and foreign real estate investment volumes, was observed as well. Investments themselves can promote economic growth, but at the same time, economic growth in some particular region can attract also real estate investors. In national economy development, the highest investment ration to GDP in Latvia had business sector, and their decisions can affect demand shocks. However, in real estate market also government investments and households have a great role as well. Macroeconomic sustainability in particular country influences the investment volumes and number of registered purchase agreements and at the same time regulation and trends on real estate market differs between countries. Macroeconomic sustainability considerably depends from economic fluctuations, investment policies, financial markets and variety of other aspects, so all such exogenous factors should be applied by real estate investors in portfolio management, and for policies regulations as well. Combination of effective real estate investment portfolio management and preventive analysis of macroeconomic sustainability can help to achieve successful entrepreneurial results. Future research directions can be connected to practical analysis of more countries, and including problems of environmental sustainability of researched question.

REFERENCES


[17] [http://dx.doi.org/10.1016/j.jce.2012.10.002


Linda Kauškale, M.g.oec., is lecturer, PhD student, researcher assist. at Riga Technical University, Faculty of Engineering Economics and Management. With distinction has obtained Professional Master Degree in Civil Construction and Real Estate Management and qualification of Real Estate Economist. The Head of International Real Estate department at Ltd. „AVA HOLDING”. Participated in international scientific conferences: IEOM-2015 in United Arab Emirates, International Conference on Environmental Engineering (ICEE-2014); Modern building Materials, Structures and Techniques (MBMST-2013), The Head of International Real Estate department at Ltd. „AVA HOLDING”. Participated in international scientific conferences: IEOM-2015 in United Arab Emirates, International Conference on Environmental Engineering (ICEE-2014); Modern building Materials, Structures and Techniques (MBMST-2013),

Ineta Geipele, is the Professor at the Faculty of Engineering Economics and Management, the Director of the Institute of the Civil Engineering and Real Estate Economics, the Head of the Chair of the Civil Construction and Real Estate Economics and Management of the Riga Technical University (RTU), Latvia. She has earned Doctor's degree of Economics and Master's degree of Economics in Engineering Sciences at the RTU. Her professional skills are improved in Austria, Germany, Denmark and England. She is an author and co-author of more than 180 scientific publications. Her current research interests are focused on Sustainability Development Problems of Real Estate Market, Construction Industry, including Land Use Management and Institutional Economics.

© IEOM Society International