New Business Opportunities for Prefabricated housing in Russia, Ukraine, and Kazakhstan

The housing market in the United States continues to cool and demand for pre-fabricated housing and housing components is slowing down. However, the markets for pre-fabricated housing in Eastern Europe, and particularly in Russia, Ukraine, and Kazakhstan present considerable expansion opportunities for U.S. manufacturers. Russia, Ukraine, and Kazakhstan, with a combined population of 200 million, represent a major untapped market for pre-fabricated housing manufacturers. Existing housing stocks are aging and need replacement, while demand for new housing is steeply trending upward in step with rapid economic growth.

Rapid economic growth in these countries means that salaries have risen considerably since 2000 with many people now seeking to purchase their own homes. However, the very slow process of constructing high rise multi-family housing combined with the desire to live in a single family home is driving the enormous interest in cost efficient pre-fabricated housing. Competition in the pre-fabricated housing market in Russia, Ukraine, and Kazakhstan is currently very low, making it the ideal time for U.S. manufacturers to establish manufacturing facilities and secure a significant portion of the market share.

Russia Highlights

Russia is home to a rapidly developing real estate and mortgage market. The tremendous growth of Russian businesses, sustained high price of oil and gas, political and economic stability, as well as growing foreign direct investment and international trade have all contributed to the growth of Russia’s real estate market and have created considerable demand for affordable housing and housing components. With thirteen cities that have a population greater than 1 million, many Russians are looking for opportunities to move from aged high rise apartment buildings to suburban single family homes. However, single family homes are currently typically custom built and too expensive for many middle class Russians.

Pre-Fabricated Housing Opportunities

The recent increased availability of home mortgage loans for the middle class and high demand for housing are driving demand for housing upward. Residential construction increased by 15% in 2006, which is the highest annual growth rate since 1991. As a whole, the construction industry grew by 19.5% in real annual terms in 2006, accounting for 5.8% of GDP growth. Long-term growth in the housing market is being stimulated by the Russian government. In 2005, Russian President Vladimir Putin launched the National Priority Project (NPP), a national Initiative focused on heavy investment in education, healthcare, agriculture, and housing. The housing component of NPP includes $3.5 billion in annual state guarantees to develop Russia’s affordable housing sector and grow mortgage lending. The Russian government’s NPP program seeks to have one in three homeowners with a mortgage by the end of 2010. This means an estimated 1.05 to 1.4 billion square feet of new housing will be brought onto the market every year.

According to the Russian Government, about 16 billion square feet of available housing is needed to meet the present housing demand of the Russian population. Most of the current available housing in Russia is

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2 http://www.realestate.moscowtimes.ru/archive/realestate/116
old and outdated. A recently conducted population census in Russia revealed that over half of all private householders occupy buildings that were constructed between the 1950’s and 1980’s.5

Growth is robust in the commercial sector, which runs complementary to the housing sector. In 2006, Business Week estimated that foreign investment funds invested as much as $1.5 billion into Russian real estate projects, nearly double the level in 2005.6 The market is especially attractive to commercial real estate investors who are seeing annual returns that are in the double digits vs. 4% to 5% in Western Europe and the U.S.7 Analysts predict this growth to persist as demand continues to outstrip supply by a wide margin.8

Construction of entertainment centers and shopping malls is also on the rise. Moscow is expected to have at least 17 new shopping centers by the end of 2007 as developers look to reap the benefits of rising incomes and growing consumer spending. Expansion is also occurring outside of Russia’s major cities as developers have begun investing in the 13 cities with populations of more than one million that are throughout the vast country. By the end of 2008, 11 large shopping malls with a total of about 22 million square feet of new retail space will open in cities like Yekaterinburg, St. Petersburg, Nizhniy Novgorod, and Samara.9 Despite the spectacular growth, the market is still considered to be in its infancy and is expected to continue to drive demand for housing in the coming years.

The U.S. government reports that Russia has a large potential market for the U.S. construction and building products industries. Traditionally, European manufacturers have been better represented in Russia than U.S. firms. However, given the dollar/euro exchange rate, Russian importers of building products have expressed an increased interest in U.S. suppliers.10

There are many prime locations outside of major cities such as Moscow and St. Petersburg available to set up a manufacturing facility for prefabricated housing. The transportation network and logistics around major Russian cities is extremely developed and makes it relatively easy to transport the necessary inputs and outputs for the facility. Russia’s wide network of transportation has close to 550,000 miles of roads and a railway system considered to be one of the most extensive in the world, covering some 95,000 miles of broad rail.11 Furthermore, there are many U.S. government programs that can be taken advantage of in constructing such a facility in Russia. U.S. government agencies such as OPIC and Ex-Im Bank specifically exist to support and expand the international reach of U.S. businesses. These organizations can assist with financing the construction of the facility and further represent American interests abroad.

Ability of Middle Class to Purchase New Homes

Russia’s mortgage market is set to almost double this year as growing wealth among the nation’s 143 million people drives demand for better housing and banks continue to offer cheaper loans.12 The World Bank recently reported that Russia has the largest potential mortgage market in Europe.13 Yet currently the market is nowhere near its potential, standing at only $1.8 billion in 2006, still less than 1% of GDP.14

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7 Ibid
9 Ibid
13 “Russia Primary Mortgage development project” International Finance Corporation
The mortgage market is one of the fastest growing sectors of retail lending in Russia, with the amount of Russian banks offering mortgages growing to 600 in 2006, double the number in 2005.\textsuperscript{15} The development of the mortgage lending sector "is driving more banks to offer mortgages and others to cut rates, offer longer-term loans, and forego initial deposits" said Ilya Zibaryev, head of Alfa Bank’s mortgage business.\textsuperscript{16} Russia’s mortgage industry is growing fastest outside Moscow as banks open branches in the Volga, Urals, and Siberian federal districts.\textsuperscript{17} Analysts expect the mortgage market volume to increase at least tenfold from its current level to reach $20 to $60 billion by 2010.\textsuperscript{18} The development of the mortgage market is attracting high levels of investment from foreign banks and is becoming more sophisticated as mortgage and construction bond markets rapidly develop.\textsuperscript{19}

The U.S. Government is heavily involved in developing Russia’s mortgage lending market and has recently announced that it will provide $200 million in financing for a mortgage credit facility in Russia that could potentially support more than $1 billion in securitized mortgages. Robert Mosbacher, President of the U.S. Government's Overseas Private Investment Corporation, recently said, "We expect this project to generate a ripple effect that will carry through the Russian economy and reduce the cost of home ownership."\textsuperscript{20} The mortgage facility will enable financial institutions to bring the liquidity and efficiency of the international capital markets to the private housing sector in Russia.\textsuperscript{21} Furthermore, it is expected that the U.S. Government’s involvement will increase the flow of private capital and expertise to this vital sector of the Russian economy.”\textsuperscript{22}

**Ukraine Highlights**

**Pre-Fabricated Housing Opportunities**

Booming business and rising personal wealth mean that demand is up for all types of property in Ukraine. According to Colliers International, “strong demand and drastic undersupply will persist within most property sectors”.\textsuperscript{23} Ukraine represents an excellent investment opportunity for foreign property investors mainly due to its large size, strategic location within Europe, and an enormous potential for development. Ukraine represents a market of almost 50 million people whose rising incomes and old housing is driving demand for new affordable housing. Wages have risen dramatically since 2000 levels and 2006 saw another impressive increase of 18 percent in real wages.\textsuperscript{24} The increased incomes have given rise to a new middle class that is yearning to move out of Soviet era apartments and into new single family homes. As a result, both multifamily and single family housing construction has recently started on a massive scale in the suburbs of the big Ukrainian cities such as Kiev and Odessa.\textsuperscript{25}

\textsuperscript{16} Ibid
\textsuperscript{17} Ibid
\textsuperscript{21} Ibid
\textsuperscript{22} Ibid
\textsuperscript{25} Construction Ukraine. Available on-line at:http://www.constructionukraine.com
The commercial real estate market is just as active as the residential. Within the last year several office, retail and hotel transactions altogether worth over $300 million have been registered on the Kiev property market, and another $500 million worth of deals is currently in the pipeline.26 Industry experts estimate that well over $5 billion of capital is searching for investment on Ukraine’s property market.27 According to Colliers International, “the time to enter the market is now. As the competition is heating up and property prices are soaring, investors are advised to take advantage of investment opportunities in Ukraine without delay.”28 In 2006 the market for office premises in Kiev also continued active expansion. Growing scarcity of available office space on the market allowed the landlords to raise rental prices by 40%, while retaining low vacancy rates.29 As such, experts predict the market power to rest fully with the landlords for at least the next two years.30

Construction has spread to shopping malls and entertainment centers. In December 2007, the first IMAX movie theatre in Ukraine will be opened in the shopping and entertainment center Blockbuster in Petrivka, Kiev. The entertainment zone will consist of carting, roller skating, bowling, billiard club, leisure complex for children, cinema, modern virtual play stations, Internet club, alpine climbing wall, shop of multimedia production, exhibition hall, food court with 400 seats, offering the dishes of 10 cuisines, restaurant and café.31 Projects of this size are becoming the standard norm in Ukraine, and the average size of delivered shopping centers is expected to increase further from 2007 and on.32 Shopping center growth is being driven by rising consumer spending. As a result of the steady increase in personal incomes, the retail turnover growth rate reached an impressive 25.3% in 2006.33 The markets growth has also attracted a number of famous international hotel chains to the region such as Hilton, Rixos, Marriott, and Intercontinental, which have all committed to entering the Kiev hotel market.34

The country’s rapid development and strong economy has produced the ideal environment in which to establish a local prefabricated housing manufacturing facility. As the middle class continues to increase, more of the population will be seeking to purchase single family housing in the suburbs of the cities. The availability of cheaper labor and a highly educated working class make this location even more attractive. The low fixed costs will enable the manufacturer to recover the cost of the facility at a much faster rate than in Western Europe or North America. The well developed logistics around the major cities of Ukraine will make it easy to transport the necessary supplies and equipment. Local logistics are bound to only become more efficient with time as the transportation network continues to expand, especially with the pledge of the Ukrainian government’s investment of $15 billion into the logistics network in the coming years.35

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### Ability of Middle Class to Purchase New Homes

Ukraine’s economy is growing rapidly, with GDP rising at an annual rate of 7.1% in 2006 and 6.5% expected in 2007.36 Ukraine’s mortgage market is one of the fastest developing and most promising banking sectors in Ukraine. A leading Ukrainian bank recently indicated that mortgage lending grew at a

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27 Ibid
28 Ibid
29 Ibid
30 Ibid
32 Ibid
33 Ibid
34 Ibid
rate of 138% in 2006.\textsuperscript{37} Outstanding mortgage loans exceed $5.7 billion; doubling in a single year.\textsuperscript{38} The new mortgage law passed in 2005 gives Ukrainian banks needed regulatory support to provide mortgages at competitive rates. The result is a substantial increase in residential construction.\textsuperscript{39}

The U.S. Government is heavily involved in supporting the Ukrainian mortgage system. It has recently provided a long term loan to the International Mortgage Bank, a Ukrainian bank specifically created to meet the growing demand for housing financing. This financial capital from the U.S Government is allowing the bank to offer a considerable amount of loans at attractive interest rates to local consumers.

A number of international banks are also actively involved in growing Ukraine’s mortgage lending market. The European Bank for Reconstruction and Development (EBRD) has recently agreed to develop a $30 million Loan Framework Facility aimed at the development of mortgage financing in Ukraine. Under the Framework, credit lines will be used to provide long-term financing to individuals for home purchases, construction, or repairing of residential properties.\textsuperscript{40}

Another international financial institution actively supporting Ukraine’s mortgage market is the World Bank. The World Bank is also providing multi-million dollar financing to Ukraine’s International Mortgage Bank.\textsuperscript{42} The loan will support the growth of International Mortgage Bank’s mortgage portfolio and expand access to credit for Ukrainians seeking to purchase homes or make home improvements.\textsuperscript{43}

Kazakhstan Highlights

Kazakhstan’s rapidly developing economy has sustained an incredible average growth rate of 9% (GDP) over the last five years.\textsuperscript{44} This growth is being led by rising incomes and foreign direct investment in the Kazakh economy which grew 45.5% to $9.6 billion in 2006.\textsuperscript{45} This rapid growth has given rise to vigorous real estate and mortgage lending markets. This growth is expected to continue. The President of Kazakhstan recently stated, “I have a long-time goal to lead Kazakhstan to become one of the world's 50 most competitive countries in the next decade.” This feat is considered very likely, considering Kazakhstan has overcome five other global economies in just one year, moving from 61st place in 2005 to 56th in 2006.\textsuperscript{46}

Pre-Fabricated Housing Opportunities

Kazakhstan’s real estate market has been rapidly growing over the past five years especially in its three major cities: Almaty, Astana, and Atyrau.\textsuperscript{47} Dynamic growth is also expected to pick up in second-tier cities, such as Aktau, Ust-Kamenogorsk, Karaganda, and Shymkent, which will likely come to the.


\textsuperscript{38} Ibid.


\textsuperscript{40} International mortgage bank. Available on-line at: http://www.ipoteka.com.ua/about


\textsuperscript{43} Ibid


forefront for developers over the next several years. Similar to Putin’s National Priority Project in Russia, Kazakhstan’s government has also implemented a “State Housing Program” with the goal of constructing around 130 million square feet of affordable housing. The U.S. Government recently reported that growing incomes and increasing urbanization have stimulated demand for affordable housing which is seeing the highest demand in the market and is expected to further increase as more of the country’s 47% rural population relocates to cities.

The growth in construction is also occurring in the commercial market, as local development companies are actively investing into construction of shopping malls and entertainment centers. Analysts indicate an emerging retail boom. Since 2000, about 15 new shopping malls opened in Almaty (Kazakhstan’s capital) and four more are planned for later this year as retail turnover is projected to grow by 15-22% over the next 2-3 years.

Growth in Kazakhstan’s economy combined with growth of the real estate and construction sectors has increased demand for building equipment and materials. The U.S. Government reports that the fastest growing sector of the market is high quality imported products and materials used in the finishing and renovation process which include: wall & floor coverings, ceiling products, doors & windows, kitchen & bath equipment, plumbing & electrical equipment, and hardware.

Ability of Middle Class to Purchase New Homes

Kazakhstan’s flourishing real estate market can be attributed to its highly developed mortgage lending system, which has significantly increased the availability of real estate mortgages to the majority of the country’s working population. In 2004, the volume of mortgage loans issued in Kazakhstan totaled $350 million. By 2005 the volume of mortgages issued grew to $1 billion. In 2006, it was estimated to have increased to $1.5 billion. The development of Kazakhstan’s mortgage lending market has set a model for other Eastern and Central European nations to follow as about 80% of real estate transactions in the country are now financed through mortgages, while four years ago the level was below 25%. The availability of mortgage lending is driving strong demand for real estate and housing, with demand exceeding available supply.

With a population of more than 15 million people and an economy that is considered to be one of the most dynamic transitional economies in the world, Kazakhstan is a great location for setting up a pre-fabricated housing manufacturing facility. As the country continues to modernize and more people migrate to the cities, demand for affordable single family housing is only expected to rise. Locations around major cities such as Almaty and Astana have plenty of real estate available for such a facility and the current ongoing modernization in the transportation network should make it easier to transport all the necessary goods to and from the facility.

Business Opportunities for U.S. Companies

Home ownership in Russia, Ukraine, and Kazakhstan is in high demand. However, demand is much higher than the available supply. Pre-fabricated housing is a new concept that is catching on as a way to meet the rising demand with high quality housing at affordable prices. The growth in the housing sector enjoys the support of the U.S. government and the governments of Russia, Ukraine, and Kazakhstan. The current environment provides substantial opportunities for U.S. companies already involved in the

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50 Ibid.
51 Ibid.
54 Ibid
55 Ibid.
prefabricated housing sector to expand and establish manufacturing and distribution centers in Russia, Ukraine, and Kazakhstan.

These markets represent an opportunity for U.S. companies with a global vision to gain a first mover advantage in a prefabricated housing market that is virtually untapped by foreign, as well as local competition. Establishing a prefabricated housing manufacturing facility in the region will allow companies to not only fulfill the growing demand for affordable housing, but also supply energy efficient housing components such as windows, doors, and heating systems to the growing market. Such a facility can serve as a sales office for the region and be utilized as a distribution base for housing components. The wide availability of raw materials and low labor costs will aid in keeping operating expenses down.

Aginsky Consulting Can Help You Enter the Eastern European Markets

U.S. companies willing to be early movers in establishing operations in these countries stand to reap the rewards of a very attractive market. A U.S. Government publication (“BISNIS”) recently stated that companies interested in the Russian, Ukrainian, and Kazakh market “should consider qualified outside consultants to assist with preparing a market-entry strategy plan and assist with its implementation. The added value of having professionals with in-depth experience in these markets will help U.S. companies successfully establish a profitable business with opportunities for long term growth.”

AGC is highly experienced in assisting U.S. companies in entering or strengthening their position in Russia, Ukraine, and Kazakhstan. Relying on our resources and vast experience in the region, ACG is able to provide companies with the necessary services to take advantage of these opportunities. ACG can conduct further market studies and determine the best location to set up such a facility with considerations for logistics, demand, and the overall economic and political climate of the country. Furthermore, ACG would like to become your true “global partners in growth” and assist you with every step in the process. ACG will guide our clients through all phases of business development, from market research and analysis, financial planning, and operations management, to sales channel development, risk mitigation, and project execution. ACG can also assist with all the necessary functions onsite, such as recruiting local bilingual personnel, undertaking major marketing and PR campaigns, optimizing and increasing distribution, fostering development of strategic alliances, helping with major client negotiations, and developing culturally sensitive sales strategies.

For additional information about this business opportunity and a free initial consultation, please contact Aginsky Consulting Group at 877-WITH-ACG or write to us at info@aginskyconsulting.com.

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56 “Launching a business in Russia: Careful planning is vital for success,” BISNIS publications. 9, October 2006.