

Urban Entrepreneurship Development Trends in Real Estate Market in Latvia

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Abstract

Relevance of the research is determined by the fact that the specific characteristics of the real estate market are different not only in the various countries but also within one country. Urban entrepreneurship in the real estate market in Latvia approaches several economic aspects related to this issue, as the business development trends of the industry are affecting the general industry and state development, so it needs the more focused attention. The objective of the research is to identify the urban entrepreneurship development trends in the Latvian real estate market, in order to provide recommendations for more efficient work planning of the representatives of the business and the public sector. Several theoretical aspects that describe the business sector development importance from the macroeconomic point of view have been examined, the region inequality problems and their impact on business sector have been explored. In the practical part of the paper the existing situation in the market has been studied and the key business development issues in the real estate and construction industry in Latvia and its regions have been identified, that has a great importance at country level. Analysis of influence of housing maintenance expenditures has a great importance for Latvia as well, and data processing in such form was not done before. The conducted real estate market researches allow assessing the situation on the perspective. Real estate market and construction branch are driven by the investment multiplier effect, so investments in this branches can be one of the solutions for solving regional development problems. The explored issues are affecting also the community and the environment, and thus the quality of life. In turn, purchasing power is affecting the business opportunities in the certain region. Comparative, historical and statistical methods have been used in the research. Timely regulating the real estate market and the business, it is possible to improve the long-term development, which will positively affect the overall development of the country and promote economic growth.

Key words: urban development, entrepreneurship, real estate market, construction, regulation

JEL Classification: R11, R32, R38

1 Introduction

The sector of real estate transactions and construction creates high added value, therefore it is of great importance for national development, so this sector development trends require special attention. At the same time, many countries are facing the problem of uneven regional development in the country. This issue is affecting a number of socio-economic problems.

Entrepreneurship is also a way to move out of the middle-income trap for countries that experience stagnancy and, in addition, the crowd-out effect of housing price on entrepreneurship is statistically significant and large (Li, Wu, 2014). *The objective of the research* is to identify the urban entrepreneurship development trends in the Latvian real estate market, in order to provide recommendations for more efficient work planning of the representatives of the business and the public sector.

The tasks of the study are the research of the thematic scientific-research literature and scientific articles, the research of business sector, as well as the interaction of regional and national development, the research of real estate market as the national economy component, the research of the construction entrepreneurship from the perspective of national sustainable development, as well as the detailed research of urban entrepreneurship development trends in the real estate market in Latvia. The macro-economic problems that affect the real estate market have been explored in the paper.

The main market functions are the following (Asaul, 2004):

- Information on prices, supply and demand
- Mediation - communication establishment between consumers, supply and demand
- Free pricing for real estate and property rights protection
- Reallocation of investments in real estate
- Provision of freedom of enterprise
- Effectiveness of the solution of social problems

Real estate items, land and its resources are undoubtedly the part of the national wealth.

The consolidated structure of the national wealth, represented by the total value of economic assets is presented in Figure 1.

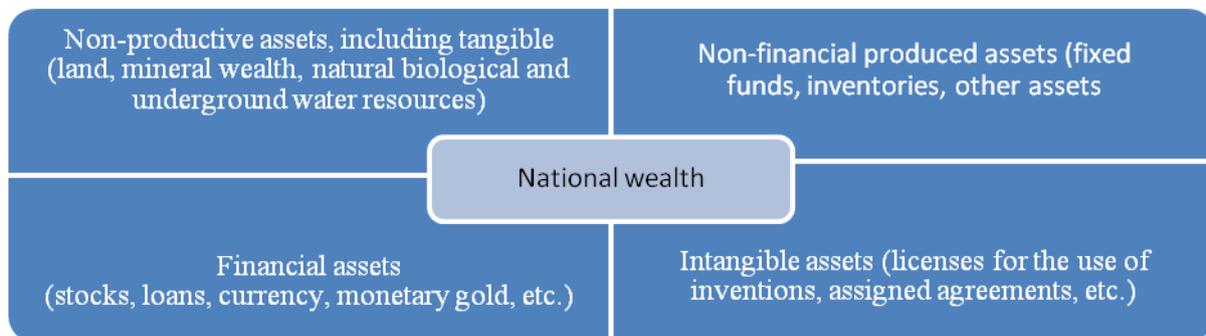


Fig. 1 Consolidated structure of the national wealth, presented by the aggregate value of economic assets (Construction Economics, 2009)

The market structure consists of real estates, entities and infrastructure, there are different levels of infrastructure (Asaul, 2004):

- National economic - macro level;
- Regional;
- Local (individual sector of real estate market);
- Object, micro-level (separate real property).

Real estate market has a number of functions and tasks, and the entrepreneurial activity in the real estate business has its own characteristics.

Timely regulating the real estate market and the business sector, it is possible to improve the long-term development that will positively affect the overall development of the country and promote economic growth.

2 Urban Entrepreneurship on Real Estate Market: Theoretical Aspects Overview

Now more than ever in the history, economic development and entrepreneurship have become strongly interconnected (Toma et al., 2014). At the same time, land derives its value from the fact it is a necessary input, or factor of production, and what makes one urban land parcel worth, describes residual theory of land value (Geltner et al., 2007). Greater entrepreneurship activity and innovation would enhance economic activity, and the latter would in turn have positive effects on innovation and entrepreneurship (Galindo et al. 2014).

It was proved that the improvement of the state socio-economic situation has a positive impact also on the real estate market (Geipele et al., 2014). The following list summarizes the major constraints and concerns that affect most investors, particularly on real estate market (Geltner et al., 2007):

- Risk;
- Liquidity;
- Time horizon;
- Investor expertise and management burden
- Size
- Capital constraint

Real estate investors have variety of risks. Entrepreneurship on real estate market, real estate development process has also a great social significance.

In an open city (Glaeser et al., 2010):

(A) An increase in the number of entrepreneurs will increase city population and land values and have an ambiguous effect on wages, the number of workers per firm, and profits of non-traded good entrepreneurs.

(B) An increase in the share of entrepreneurs who produce traded goods will increase wages, city population, land prices and the number of workers per firm and will have an ambiguous effect on profits of non-traded good entrepreneurs.

Hungary, as a result of conscious planning and developmental processes, made some regions more attractive for the foreign direct investments by the increase of the per capita GDP, which became 4.5 times higher between 1994 and 2003 (Dusek et al., 2014).

Most of definitions of term „urban” are based on one or more of three primary factors: total population size, population density, and impervious surface area or built structures (Wu, 2014). It is important to explore the issues related to sustainable urban development. The term sustainability consists from variety of indicators, that are shown in Figure 2.

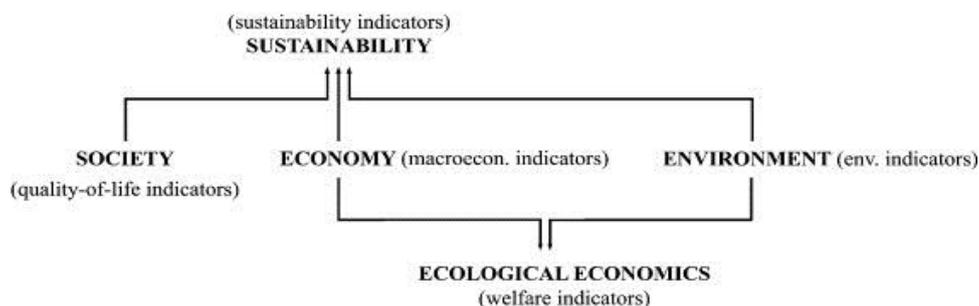


Fig. 2 An interdisciplinary study on indicators: A comparative review of quality-of-life, macroeconomic, environmental, welfare and sustainability indicators (Pissoriosis, 2013)

There are the significant infrastructure opportunities (such as roads, rails, airports and ports – but also non-traditional ones, including water and electricity) available across the globe within the real estate industry, and emerging markets, in particular, will have to make considerable investments to improve their existing infrastructure with respect to water, electricity and transport, among other areas, and within economic dimension of sustainable investment environment there are such significant aspects of enhancement of sustainable competitiveness as (Vanags and Butane, 2013):

- Economic growth
- Social cohesion
- Employment
- Competitive power in international competition
- Using resources in an efficient and sustainable way
- Minimizing negative environmental impacts

The pattern of urban land use and transport is responsible for energy and land resources consumption, which has major global environmental consequences, and the challenge at the Metropolitan level is to plan, design, and manage urban growth in moderate ways that contribute to sustainable development (Hasibuan et al., 2014). It is proved, that institutional entrepreneurs play an important role in sustainable urban development, institutional entrepreneurs use concrete tactics to sketch a possible ‘way out’ of this problem, and influence both formal and informal institutions to create a context that is more favorable to sustainable developments (Woolthuis et al., 2013). Enterprises need to consider a variety of factors. Framework of determinants of entrepreneurship is shown in Figure 3.

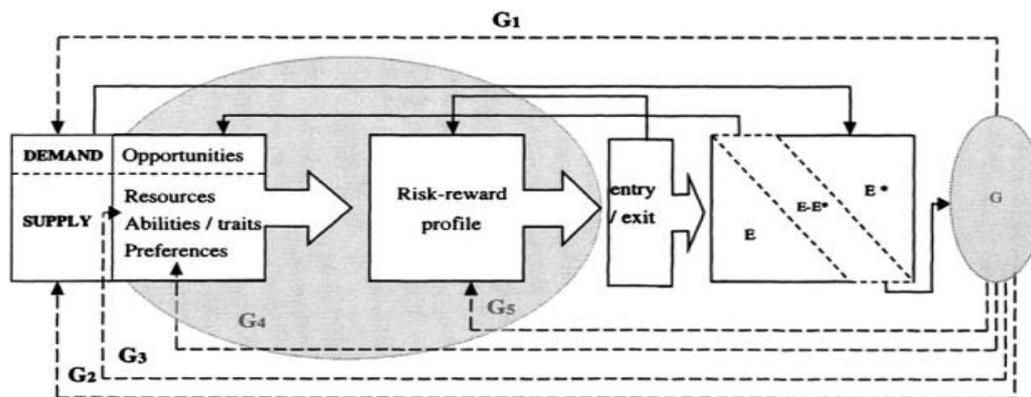


Fig. 3 Framework of determinants of entrepreneurship (Verheul et al, 2002)

Mai Thi Thanh Thai and Ekaterina Turkina (Thai and Turkina, 2014) findings demonstrate four means of reducing informal entrepreneurship and boosting formal entrepreneurship: nurturing a performance-based culture; creating favorable conditions for economic advancement; increasing quality of governance; and enhancing people's resources and abilities, and it is recommended to promote cooperation and networking to encourage social capital and to encourage informal entrepreneurship before undertaking the necessary governance and economic reforms to motivate entrepreneurs to transfer to the formal sector. At the same time Dimitratos et al. (2014) in the mentions a fact, that nowadays micromultinational companies mostly controls and manages value-added activities and they will have a great importance in 21st century.

For the comprehensive and effective government of a state, the strategic development plan should involve many factors. Strategic development plan of territories is the basis for the

development of territorial investment program, the construction of which is based on the following principles (Asaul, 2004):

- Subordination of territorial investment program to strategic plan and priorities of socio-economic development of the territory;
- Transparency and openness of the selection of investment projects;
- Development of business plans for the reconstruction and development of real estate items;
- Attraction of investors for the implementation of reconstruction and development of the real estate market;
- Attraction of borrowed resources;
- Orientation to the cumulative effect of budget credits (concentration of funds for using in the same direction);
- Activity can be achieved by providing tax and other incentives, guarantees and direct budgetary loans.

The need for a spatial planning reform was long debated at the end of the 1990s with discourses focusing on (Spatial planning systems and practices in Europe, 2014):

1. strategic planning (shifting the focus from the local to the regional and national levels);
2. devolution of the centralist spatial planning system (competences to the regions and local authorities); and
3. „bypassing” obstacles of mainstream planning, avoiding „fast track” solutions.

In defining the best use of real estate, such factors should be analysed (Tepman, 2008):

- market conditions (mainly types of land use in the researched area);
- existing zoning regulations;
- planned changes on the real estate market;
- existing type of real estate usage.

Timely regulation of the real estate industry and comprehensive events for the development of territories can not only improve the efficiency of the business sector, but also have the positive effect on the life of society as a whole.

3 Practical Research on Urban Entrepreneurship on Real Estate Market in Latvia

Creating intelligent enterprises is a natural progression for economies aspiring to become global and knowledge-based, these also is a need for construction-sector companies to level up to meet domestic as well as international challenges in order to remain globally competitive (B.H. Goh, 2006). One of the indicators that shows the significance of construction activities in the economy of the country, is total gross value added. Percentage of total gross value added in construction, at basic prices is represented in Figure 4.

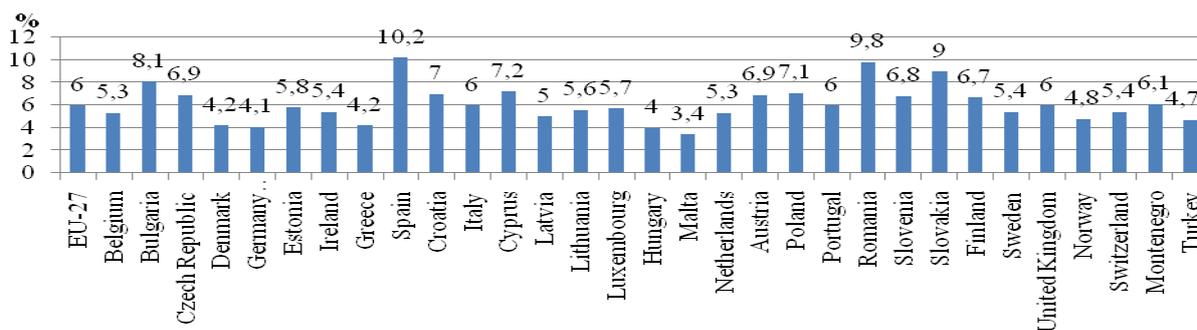


Fig. 4 Percentage of total gross value added in construction, at basic prices, %, 2010.

Source: Eurostat, figure made by authors

Figure 4 shows that the construction sector in Spain has the highest added value in 2010 among the EU countries, followed by Romania and Bulgaria. It is also related to a particular country's economy and real estate development cycle phase – particular national demand for construction products, the overall price level in the industry and other factors. Monthly labor costs per employee by kind of activity in Latvia are represented at Figure 5.

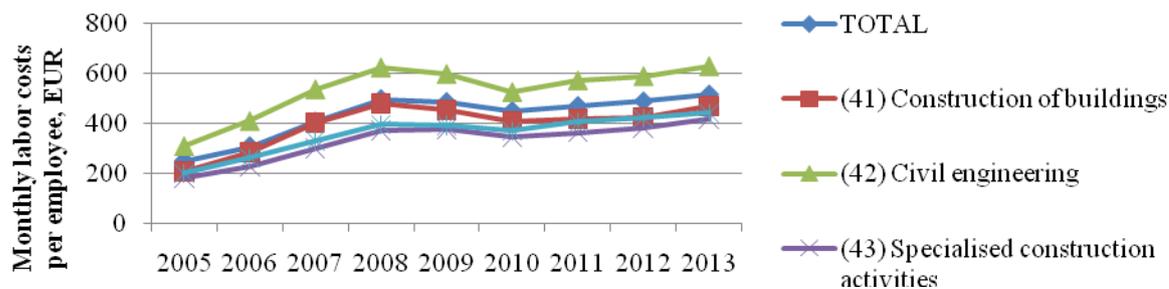


Fig. 5 Monthly labor costs per employee by kind of activity in Latvia, euro

Source: Central Statistical Bureau of Latvia, figure made by authors

The real estate market and the construction industry have a number of operational areas, and the average wages are different there. The highest wages are in the civil engineering sector, they exceed the average wages of all sectors in the country. According to the Central Statistical Bureau, the lowest wages in the construction industry are in the specialised construction activities sector. Important is the fact that the business activities and real estate market development trends are different. Firstly, it is felt that both Riga and Pieriga region show the more active construction industry development than in other Latvian regions. The lowest level of activity has been observed in Latgale. This is related to all investigation activities - construction of buildings, civil engineering and construction Specialised Activities (see Figure 6).

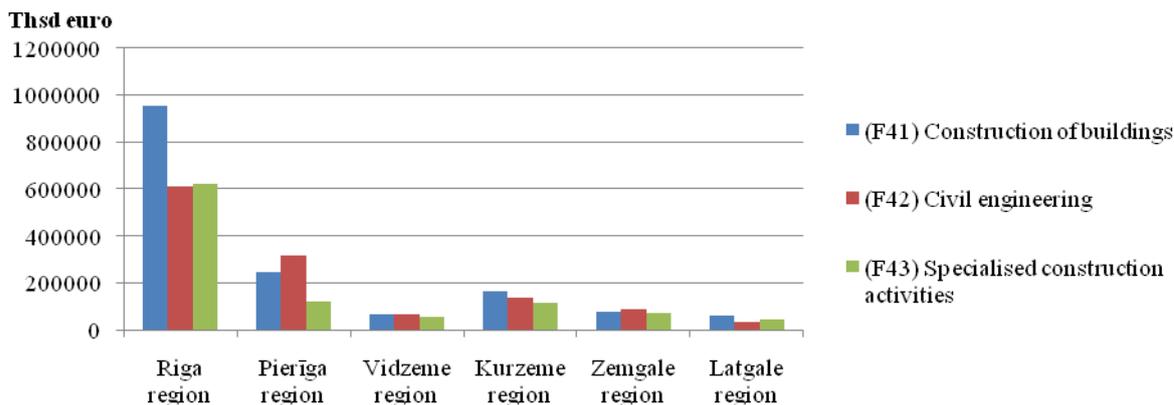


Fig. 6 Production value in construction by region, 2012 (thsd euro)

Source: Central Statistical Bureau of Latvia, figure made by authors

Uneven development trends in different Latvian regions can be observed not only in construction industry, but also in the overall business development. Over the period from 2009 to 2012, approximately 60% of all Latvian companies were operating exactly in Riga. The next is Pieriga region, but the number of the companies operating in Zemgale, Kurzeme, Vidzeme is at lower level. Number of commercial companies by region in Latvia is shown in Figure 7.

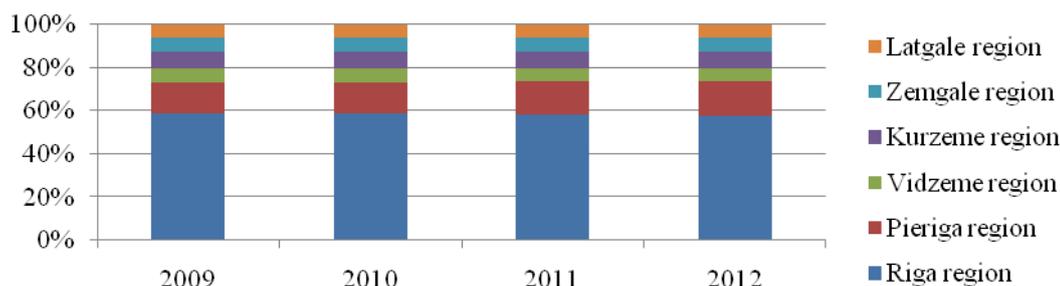


Fig. 7 Number of commercial companies by region in Latvia

Source: Central Statistical Bureau of Latvia, figure made by authors

At Figure 8 is shown that employment level at construction branch in Vidzeme, Kurzeme, Zemgale and Pieriga region is higher than in Riga. It can be concluded that the construction activities in these regions are more important for the certain people in the particular region, as they provide jobs and have a socio-economic significance. It can be concluded that the construction activities in these regions are more important for the certain people in the particular region, as they provide jobs and have a socio-economic significance.

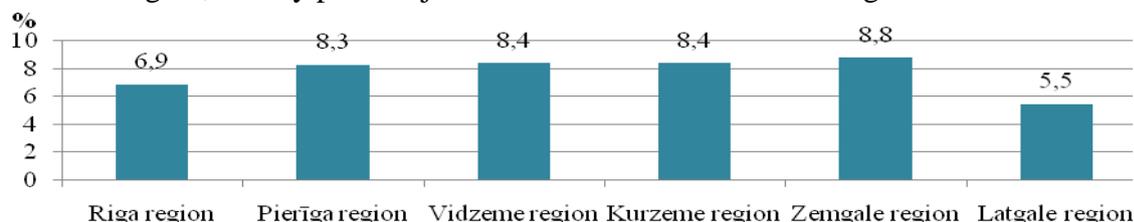


Fig. 8 Employment level in construction by region in Latvia, 2013 (NACE Rev. 2.)

Source: Central Statistical Bureau of Latvia, figure made by authors

Employment rate is only one indicator from the number of indicators, analysed by the investor before taking the decision on investing. Non-financial investments by kind of activity

in Latvia at constant prices of 2012 are shown in Figure 9. Non-financial investment refers to long-term investment in intangible assets, residential houses, other buildings and structures, cultivated assets, technological machinery and equipment, other fixed assets and inventory; as well as fixed asset formation and the costs of unfinished construction and capital repairs (Central Statistical Bureau of Latvia, 2014).

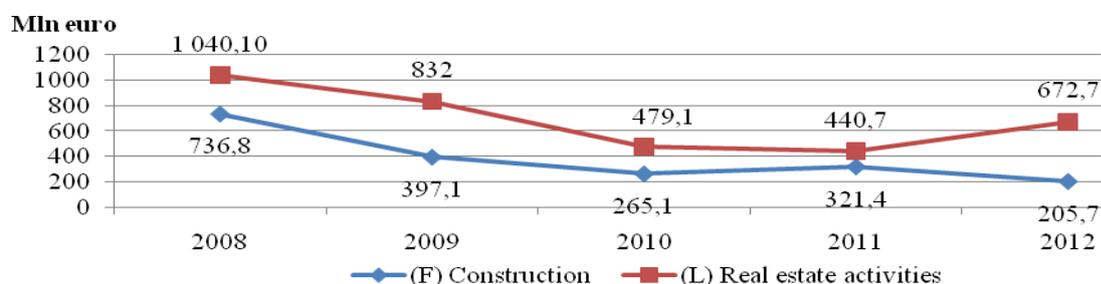


Fig. 9 Non-financial investment by kind of activity in Latvia (at constant prices of 2012, mln euro)

Source: Central Statistical Bureau of Latvia, figure made by authors

The recession phase of Latvian economics showed the reduction of the investment amount in several sectors, including the decreased financial investments in construction and real estate transactions. During the post-crisis period, in 2012, the indicators of real estate transactions have improved, which could have been caused by the increase in foreign investments in real estate. However, there are a number of reasons to suspect the presence of *spatial dependence* in models of FDI, especially at the city-level (Blanc-Brude, 2014). Figure 10 shows the uneven regional distribution of non-financial investments.

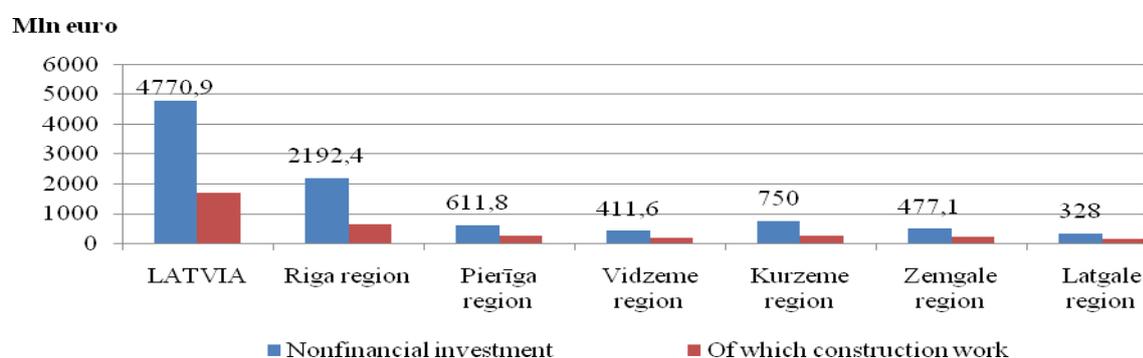


Fig. 10 Non-financial investment by statistical region (at constant prices of 2012, mln euro)

Source: Central Statistical Bureau of Latvia, figure made by authors

Public investment interdependencies can be influenced by the cohesion policy objectives, also by spatial distribution of population and economic activity (Tsekeris, 2014), so investments especially in real estate objects has a great role in development of regions, also because of investment multiplier (Keynes, 1936) effect on the economy. Uneven distribution of investments increases the difference between the national and regional development and too pronounced differences are not welcome. Therefore, link-age promotion policy should target matching between foreign affiliates and local firms, and upgrading of local suppliers' capabilities, to stimulate technological activities in existing foreign affiliates, as well as technological co-operation between domestic firms and affiliate (Giroud, 2012). The stage of regional development affects the standard of living of the particular region. One of the most important stages of the expenditures involves housing maintenance expenditures. Housing maintenance expenditures heavy burden 48% of respondents in Latvia (see Fig.11).

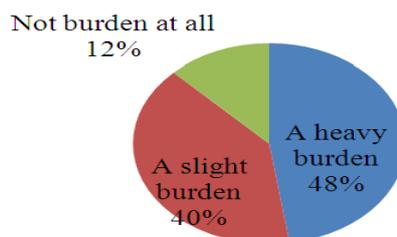


Fig. 11 Housing maintenance expenditure influence on household financial situation in Latvia in 2013, %
Source: Central Statistical Bureau of Latvia, figure made by authors

Housing maintenance expenditures, affecting the household financial situation in Latvia, are varying in different regions. Despite the fact that the average indexes show that the urban population is a little more dissatisfied with housing maintenance expenditures than the population in the regions, however, Zemgale dissatisfaction level is higher than the average indexes of the industry. Percentage of respondents, who heavy burden housing maintenance expenditure on household financial situation in Latvia in urban and rural regions, is shown in Figure 12.

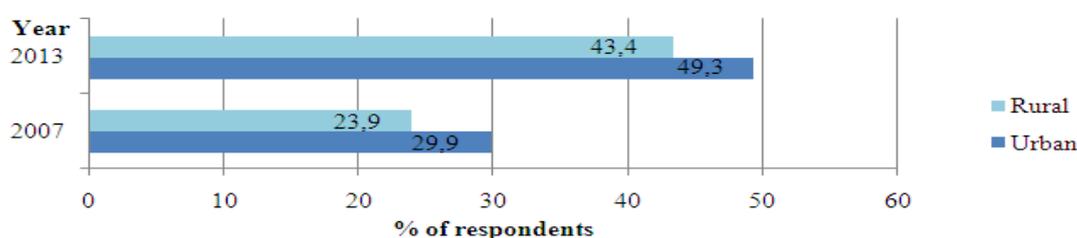


Fig. 12 Percentage of respondents, who heavy burden housing maintenance expenditure on household financial situation in Latvia, %

Source: Central Statistical Bureau of Latvia, figure made by authors

Despite the fact that the business profits and the average wages in urban areas are higher than in the regions, still the burden of city population is higher. There is also a significant fact that the housing maintenance expenditures in 2013 affected approximately 20% more of the population in both urban and rural areas, which is not a positive trend. Housing maintenance expenditures are the essential stage not only for households but also for commercial enterprises, as well as the real estate companies.

4 Conclusions

Real estate items, land and its resources are undoubtedly the part of the national wealth. By timely regulating the real estate market and the business sector, there is a possibility to improve the long-term development that positively affect the overall development of the country and will promote economic growth. Activities for the development of territories can not only improve the efficiency of the business sector, but have also the positive effect on the life of society as a whole. Now more than ever in the history, economic development and entrepreneurship have become strongly interconnected (Toma et al., 2014), this factor deserves special attention in strategic planning. Important is the fact that the business activities and real estate market development trends are different in the regions. Firstly, it is felt that both Riga and Pieriga region show the more active construction industry development than in other Latvian regions. Over the period from 2009 to 2012, approximately 60% of all Latvian companies were operating exactly in Riga, and in Riga there is the higher production value in construction. The lowest level of activity has been observed in Latgale. This can be

related to all researched activities – construction of buildings, civil engineering and specialised construction activities. Construction activities in the Latvian cities and regions are more important for the certain people in the particular region, as they provide jobs and have a socio-economic significance, so it is recommended to develop and support entrepreneurship, including construction industry and real estate market not only in the cities but also in the regions, paying special attention to the development of infrastructure and by defining best type of usage of real estate objects. It is important to promote urban entrepreneurial programs and researches. Public management efficiency is highly important for all above mentioned activities. At the same time, the multinational companies nowadays mostly control and manage value-added activities (Dimitratos et. Al., 2014), so it would be advisable to support and develop also the activities for this group of companies.

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