

Market Overview

2ND TRIMESTER 2010

CONTENTS

Financial and economic environment for real estate investment **p. 2**

Financial environment
Economic environment

French commercial property investment market **p. 3/5**

Investment volumes hampered by investors' selectivity
Retail investment segment surges ahead
Equity investors continue to dominate the market
Continued decline in yields
A new benchmark for retail yields

Major investment deals in 1st trimester 2010

FOCUS Retail property market: the importance of "prime pitches"

Greater Paris occupational market **p. 6/7**

A shift in letting activity in central Paris
A blip in supply and vacancy
Rents begin to stabilise in Paris CBD

Major transactions in 1st trimester 2010

The Colliers UFG PM Barometer **p. 8**

Green refurbishment of 2nd hand buildings: who's going to pay?

With sustainability issues at the top of decision-makers' agendas, the challenge of shrinking the property sector's environmental footprint has taken on increasing importance. In France, "Grenelle de l'Environnement", the government round-table on environmental stewardship, has provided further impetus to this process. Faced with mounting public pressure to "go green", all property sector participants are equally concerned by the trend. The extent to which property market players have risen to this challenge is indicative of the sector's maturity and is a commendable development.

Nevertheless, practical applications of these laudable principles have, so far, been restricted to the top end of the market. Indeed, of the new office buildings holding multiple "green" labels (HQE and BBC in France and Breeam in the UK) or operational high environmental quality labels, virtually all of them are very large office properties located in established business districts. Yet, the vast majority of the built office stock consists of older multi-tenanted properties in non-prime locations.

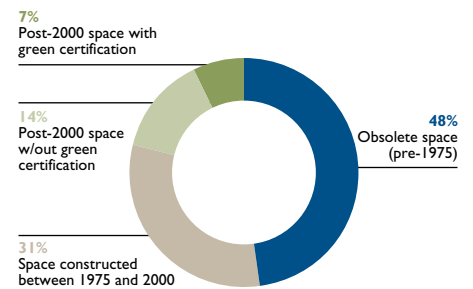
A number of avenues for the renovation of the existing second hand buildings can be envisaged. A first step consists in mobilising occupiers to increase their energy efficiency. However, this presents significant economic obstacles. While public sector and large corporate users are generally willing to enter into so-called "green leases", such leases are seen as too burdensome for other categories of tenants. In the current climate, SMEs are closely watching their bottom line and are reluctant to take on new commitments without an immediate financial payback. Moreover, there is a fundamental mismatch between the lifecycle of an office property and the business cycle of SMEs insofar as SMEs' office space requirements are subject to abrupt fluctuations. How can an SME letting property under a traditional nine-year lease with three-year break options be expected to commit to a building energy-efficiency programme?

Thus, the burden of greening the second hand buildings will probably fall to property owners. Various options lie open, e.g. improving building management, upgrading technical facilities and performing rehabilitation work. However, owners may face difficulties in passing on the cost of their investments to occupiers:

- It may be possible to get large corporate occupiers to commit to leases after rehabilitation work has been performed but this will be much more difficult for SMEs;
- The occupational market has not yet strengthened to a point where it can support speculative development;
- Possibilities for owners to increase the density of occupation (extensions, increasing vertical heights, etc.) in order to generate additional rental income.

Regarding the latter point, property owners' success in this area will depend on their ability to establish partnerships with town-planning authorities. This is particularly the case for property owners in the French regions.

TAKE-UP OF GREATER PARIS OFFICE SPACE BY VOLUME



Source: Colliers UFG PM research department (2010).

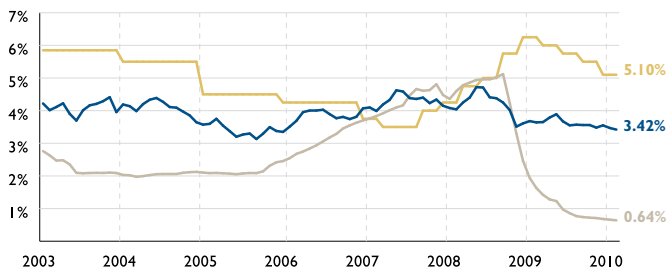
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Financial and economic environment for real estate investment

→ Financial environment

INTERBANK LENDING RATES, RISK-FREE RATES AND PROPERTY YIELDS



Source: BCE / FRANCE TRESOR / COLLIERS UFG PM, April 2010.

- 10-year French government bonds (OAT) - monthly average
- Prime yields - Paris CBD office market
- 3-month Euribor rate - monthly average

Across Europe, financial markets have been rocked by worries over European sovereign debt and the euro zone crisis. While the massive rescue package agreed for Greece by the EU countries and the IMF is certain to alleviate the Greek government's short-term liquidity needs and will help to stabilise financial markets, the situation will have a significant impact on future financing for property development and investment.

Firstly, hopes of renewed growth in credit availability within the commercial property sector have been dashed by the extent of German, French and other European banks' exposure to Greek sovereign debt risk.

Secondly, investor risk aversion is likely to be more negative, particularly for higher-risk asset classes such as equities, corporate debt and sub-prime property, etc.

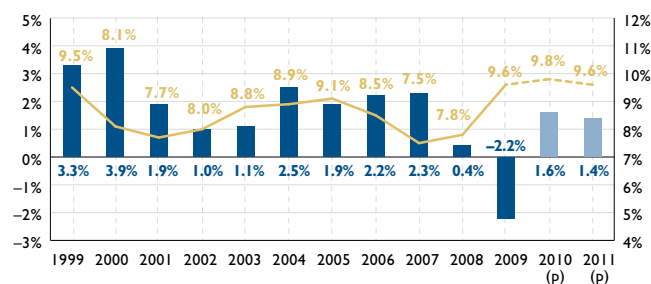
« A pall has been cast over the euro zone's reputation. »

Finally, a pall has been cast over the euro zone's reputation for financial stabilisation and macroeconomic convergence – the attributes that made it a haven for capital.

Therefore, we can expect that traditional property investors from outside the euro zone (US, UK and Middle Eastern investors) will factor this weakness into their international asset allocation decisions.

→ Economic environment

ANNUAL CHANGE IN GDP AND UNEMPLOYMENT RATES



Source: INSEE / MINISTERE DE L'ECONOMIE ET DES FINANCES, April 2010.

- Annual GDP growth
- Unemployment rate (ILO definition)

During Q1/10, the performance of commercial property in France reflected the tepid recovery underway in the French and European economies which contrasted sharply with the more vigorous upturn in the US economy and the dynamism of emerging economies.

At the end of the 2009 recession, French industrial output remained almost 10% lower than its 2005 level while consumer spending has stalled and is no longer an engine of economic growth. As a result, French GDP growth is expected to amount to 0.2% for Q1/10.

Over the short-term, there are distinct signs that the business climate continues to improve across all economic sectors and will receive a further boost from inventory restocking. For the moment, we have yet to see the positive impact on export figures from the 9% depreciation in euro/dollar exchange rates since 1 January 2010, but there is no doubt that external demand will pick up speed in coming months.

« A tepid recovery in the French and European economies. »

Thus, net direct job creation, which is projected by the French national employment service to be nil or marginally negative in 2010, should push the national unemployment rate to 9.8% this year. The unemployment rate is not expected to fall back to 9.6% until 2011.

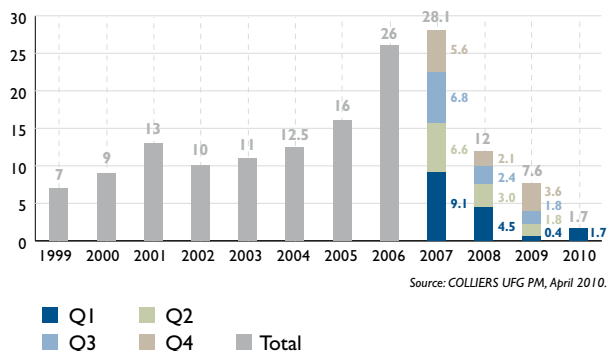


French commercial property investment market

Recovery remains weak

→ Investment volumes hampered by investors' selectivity

ANNUAL AND QUARTERLY INVESTMENT VOLUMES (in million euros)



In Q1/10, commercial property sales totalled €1.7 billion in France, representing a threefold increase on Q1/09 and a 50% reduction on the investment total for the final quarter of 2009. This amount was skewed by the impact of a high-profile deal, namely, the sale of HSBC's headquarters on the Champs-Élysées which accounted for close to 25% of the investment volume. So far, the recovery in commercial property investment has been shallow and gradual.

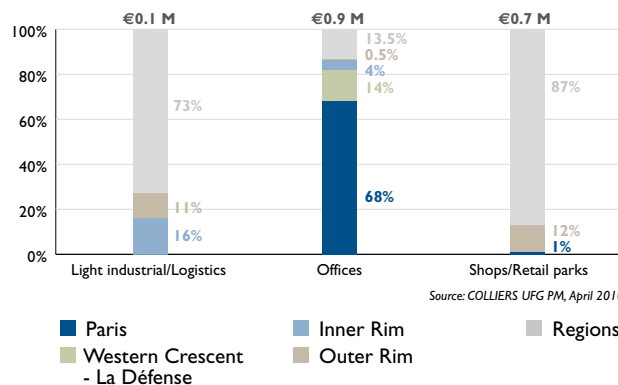
« The recovery in commercial property investment has been shallow and gradual. »

investors remain highly selective and risk adverse. Due to their almost exclusive focus on prime property assets, they face a scarcity of available products on the market. With a few rare exceptions, there has been no influx of distressed property sales.

Furthermore, although financing conditions have eased, there has been almost no evidence of investors making increased use of gearing. Financing for high-value deals remains difficult to obtain and there has been very little speculative buying in the past two years.

→ Retail investment segment surges ahead

LOCATION OF INVESTMENT DEALS BY ASSET CLASS



Offices accounted for 53% of total commercial property investment in Q1/10. Buyers have focused exclusively on the Paris CBD and other established business districts. Investment in property in regional cities amounted to €120 million, with Lyon and Marseille attracting 67% of this total. Overall, investors showed a marked appetite for new and recently constructed assets, reflecting their aversion for obsolescence risk.

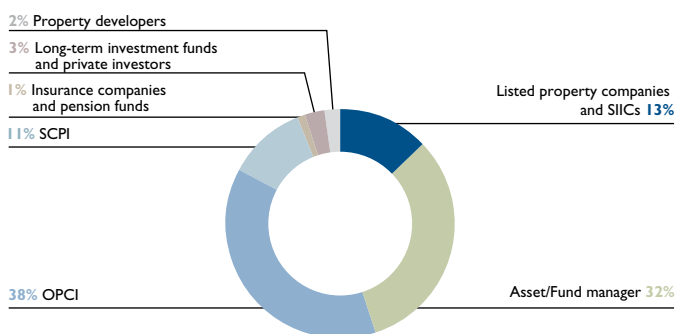
Retail property, which was the only asset class to record an increase in investment volumes in 2009, remains the most resilient segment in the commercial property sector. Approximately €720 million was transacted in the retail segment in Q1/10, with cross-border investors accounting for one-half of this total, and retail property now accounts for 42% of total investment in commercial real estate in France.

« A marked appetite for new and recently constructed assets. »

This performance is chiefly attributable to the attractiveness of high street shopping centres in the regional cities and renewed investor enthusiasm for retail parks. Less than €100 million was invested in warehouse and light industrial premises. This asset class is no longer being targeted by mainstream property investors.

→ Equity investors continue to dominate the market

INVESTMENT ACTIVITY BY TYPE OF INVESTOR - Q1/10



Source: COLLIERS UFG PM, April 2010.

The resurgence in investment by cross-border investors, which started in HY2/09, gathered pace in Q1/10. Overseas investors accounted for 30% of the investment volume, and 55% if we include the acquisition of the HSBC headquarters which was purchased through an OPCI by Middle Eastern investors. The majority of deals (seven transactions) completed by international investors concerned assets with a unit value in excess of €40 million.

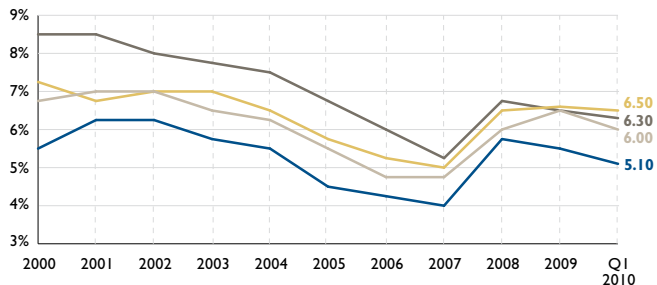
SIICs and other listed property companies invested around €200 million in Q1/10. This figure was relatively modest, but does not include sales made as part of reorganisations between SIICs. Insurers and pension funds, which had been active investors in 2008/09, pulled back from the market in Q1. Conversely, SCPIs and OPCIs remained active investors, as in 2008/09, accounting for 25% of the investment volume (50% including the HSBC/Ciloger deal). Finally, asset and fund managers were also active, particularly in the retail segment.

French commercial property investment market

Prime yields

→ Continued decline in yields

INITIAL YIELDS – OFFICE PROPERTY



Source: COLLIERS UFG PM, April 2010.

— Paris CBD
— Western Crescent - La Défense
— Inner Rim
— Regions

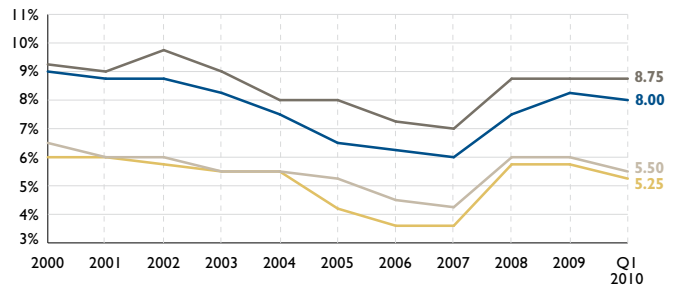
« Yield compression no longer exclusively concerns prime assets. »

The yield compression observed in 2009 continued in Q1/10, but no longer exclusively concerns prime assets. This trend reflects the selectivity of investors and the relative scarcity of high-quality products on the market. As from HY1/09, the reduction in yields initially observed in Paris CBD began to spread to other Greater Paris commercial property markets, thereby forcing investors to extend their searches beyond the established business districts. Recent transaction data shows that prime property yields range between 5.10% in Paris CBD and 6.50% in the Inner Rim.

Non-prime properties are generally changing hands at market values below their appraisal value as only a handful of investors are interested in these assets. There is virtually no market for properties that are either unlet, in need of improvement or that have high levels of tenant risk.

→ A new benchmark for retail yields

INITIAL YIELDS – LIGHT INDUSTRIAL – WAREHOUSE – RETAIL SPACE



Source: COLLIERS UFG PM, April 2010.

— Ground-floor retail premises
— Shopping centres
— Warehouses
— Light industrial space

After having risen by 150 bps between late 2007 and mid-2009, yields for ground-floor retail premises and shopping centres now show a marked decline. This trend, which has been restricted to prime shopping areas, reflects investors' preference for so-called "defensive assets". Indeed several deals involving retail parks were concluded at yields of around 7.25%.

« Investors show a preference for defensive property assets. »

Investors continue to see light industrial and warehouse properties as a risky asset class. Thus, prime yields for warehouse properties range between 8.25% and 8.75% compared with yields of between 9% and 10% for high-quality retail park properties.

Major investment deals in 1st trimester 2010

Address	City	Seller	Buyer	Floor area	Transaction price	Asset class
103, avenue des Champs-Élysées	Paris 8 th	HSBC	CILOGER	30,000 sq.m	€425 M (estimation)	Offices
Espace Saint-Georges	Toulouse	ALTAREA	COMMERZ REAL	13,000 sq.m	€90 M	Retail space
Ensemble commercial 65 croisette	Cannes	CODIC & FINAMAS	KANAM	NC	€75 M	Retail space
21-29 rue des trois Fontanot	Nanterre	CBRE INVESTORS	SILIC	14,500 sq.m	€73 M	Offices
Rue Sainte-Catherine	Bordeaux	CORIO	WESTINVEST-DEKABANK	16,700 sq.m	€67 M	Retail space

Source: COLLIERS UFG PM, April 2010.

FOCUS

→ Retail property market: the importance of “prime pitches”

Retail premises have become increasingly attractive to investors since the onset of the economic crisis and are sought after for their rental stability and limited exposure to the property cycle. Investor demand has been, in part, satisfied by the sale-and-leaseback programmes introduced by retail chains in an effort to reduce their debt burdens and refocus on their core operations. Retail property accounted for around 11% of the total investment volume between 2005 and 2008, and this share rose to 25% of total investment in 2009.

Despite this, investors are extremely selective in their decisions given the fact that many retail locations have been adversely affected the economic downturn.

Already hurt by declines in their revenues in 2009, retail chains now face a reduction in household spending, which fell by 1.9% in Q1/10.

As a result, many retailers have opted to renegotiate their leases in recent months, reflecting the lower profitability of their operations and the increase in their rent-to-income ratio. Furthermore, property owners have agreed to adopt the new ILC (index of rental rents) index which was intro-

duced to moderate rent reviews. The increase in the ILC index (up 18.2% over 5 years) is decoupled from retail sector revenues. Moreover, retail chains have revised their expansion plans and slowed down projects for new openings. In addition, properties are spending longer periods of time on the market while the average size of retail premises being let has fallen. The high level of retail developments underway in 2009 and 2010, which has been propelled by reforms to national retail planning guidelines, is out of synch with the economic climate and could create a significant imbalance.

Thus, for investors and retail chains alike, the focus is increasingly on high-quality city centre space, so-called “prime pitches”. Recent transactional data confirms the attractiveness of boutiques, city centre shopping centres and retail parks located on prime thoroughfares.

Conversely, shops located in secondary locations and out-of-town sites situated away from major road links have experienced major declines in rental values and are spending longer periods of time on the market.



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Greater Paris occupational market

Lettings market returns to fundamentals

→ A shift in letting activity in central Paris

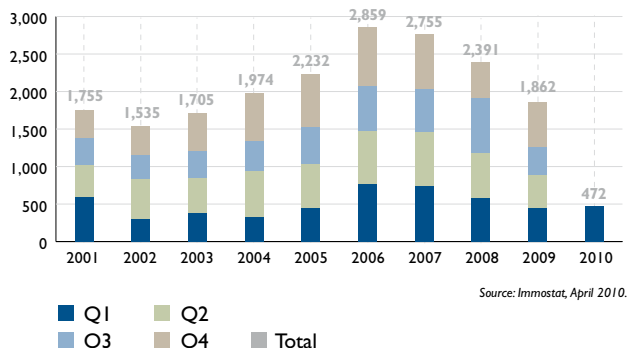
A total of 472,000 sq.m of office space was let in Greater Paris in Q1/10, a level 7% higher than the same period in 2009.

« In the absence of job growth, cost-cutting and rationalisation have been the main factors influencing occupiers' real estate strategies. »

This performance was on par with average quarterly take-up observed since September 2008. In the absence of job growth, cost-cutting and rationalisation have been the main factors influencing occupiers' real estate strategies, this is further reflected by the significant share (40%) of new and refurbished office space in total take-up.

Take-up of large office premises, which fell slightly, accounted for 35% of total space transacted. Occupiers' planning horizons for property needs have lengthened considerably in recent months. Letting activity in the 1,000 to 5,000 sq.m segment was up 50% year-on-year and up 12% on the previous quarter. Finally, demand for small office premises has stabilised

QUARTERLY TAKE-UP IN GREATER PARIS (in thousand sq.m)



at a low level and properties are spending longer periods of time on the market.

For the first time since 2006, central Paris accounted for more than half of the space transacted in Greater Paris. This reflected the brisk demand for small and medium-sized office premises and the very high level of large lettings (97,500 sq.m) in Q1/10. While demand for office space in the Outer Rim held up well, Inner Rim office markets showed considerably less resilience, particularly in La Défense.

→ A blip in supply and vacancy

At the end of March 2010, immediate supply of office space in Greater Paris amounted to 3.6 million sq.m, a level virtually unchanged from the previous quarter. The office vacancy rate now stands at 7%, a peak last seen in 1997.

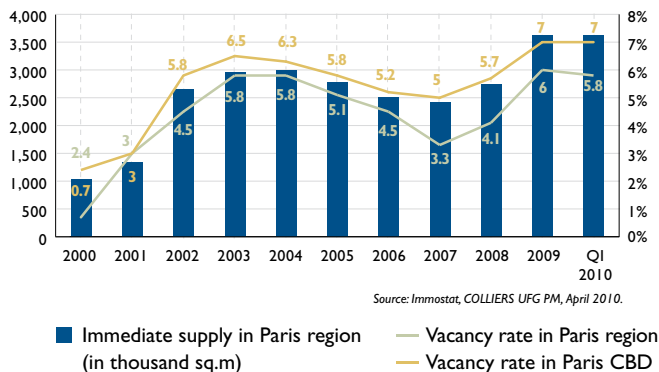
« Supply due within one year could exceed 5 million sq.m by end-2010. »

Despite this, there has been a marked shift in the structure of available space. Due to the increase in letting activity in central Paris, available supply

fell back by 5% while the Paris CBD vacancy rate dropped below 6%. Conversely, supply in the Outer Rim office markets, which is already abundant, rose by a further 7.5%. Supply fell back markedly in the Inner Rim, with the exception of La Défense (up 11%) and the Boucle Sud (up 12%).

In the regional cities, supply of new office space fell by 10% owing to the reduction in the development pipeline, with just 200,000 sq.m of space due to be completed in 2010. Conversely, supply of second-hand space continued to rise, reflecting the impact of the pipeline of tenant release space due to arrive on the market. Currently estimated at 4.8 million sq.m, supply due within one year could exceed 5 million sq.m by end-2010.

IMMEDIATE SUPPLY VERSUS VACANCY RATE



Greater Paris occupational market

Lettings market returns to fundamentals

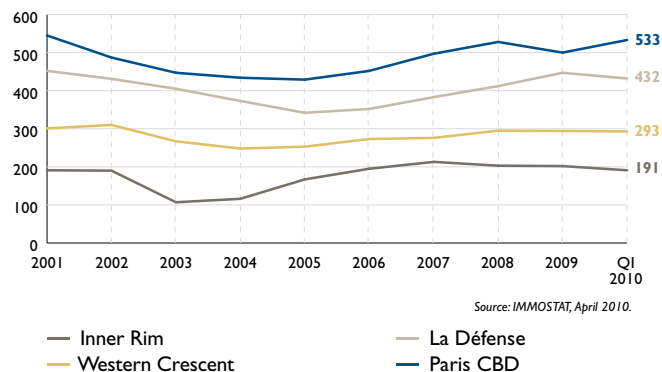
→ Rents begin to stabilise in Paris CBD

The deterioration in the Greater Paris absorption rate has weighed heavily on rental values. In addition to adjusting headline rents downwards, property owners increasingly have to offer generous tenant incentives, representing 15% on average of asking rents. However, this situation contrasts significantly from one submarket to the next.

« In Paris CBD, headline rents appear to be stabilising, particularly for prime office space. »

In Paris CBD, the adjustment in rental values underway since 2008 has helped to bolster letting activity, particularly in the medium and large office segments. Headline rents now appear to be stabilising, particularly for prime office space. Second-hand rents have risen by 9% year-on-year, chiefly as a reflection of the good quality of premises being let.

AVERAGE HEADLINE RENTS FOR SECOND-HAND SPACE (€ net/sq.m pa)



In the Western Crescent and the Inner Rim, rents for new office space continued to fall in Q1/10, following on from the trend observed in 2009. Average second-hand rents fell by 10% year-on-year in the Inner Rim. The trend was less pronounced in the Western Crescent (down 7.5%) and La Défense while second-hand rents stabilised in the Boucle Sud area.

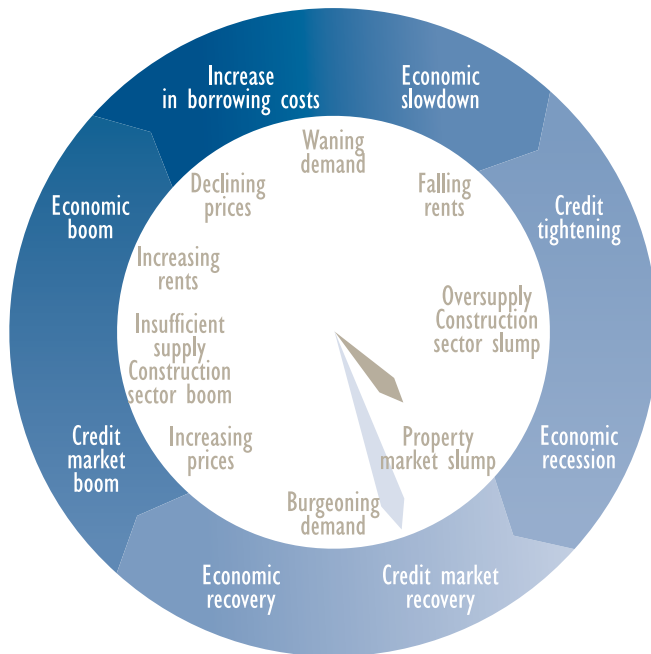
Major transactions in 1st trimester 2010

Address	City	Tenant	Floor area	Comment
ZAC Claude Bernard	Paris 19 th	BNP PARIBAS	41,000 sq.m	New
LE FRANCE 190/198 avenue de France	Paris 13 th	EHESS	17,000 sq.m	Second hand
TRAIT D'UNION 8 rue François Ory	Montrouge	MONDADORI	14,000 sq.m	New
14/16 rue de la Ville l'Evêque	Paris 8 th	ILIAD	13,000 sq.m	Refurbished
LE VIALA - SEINE PANORAMA 40/42 rue du Docteur Finlay	Paris 15 th	DCNS	12,000 sq.m	Refurbished
LA PORTE DU LAC Boulevard Victor Hugo	Saint-Ouen	GFI INFORMATIQUE	11,000 sq.m	New



→ The Colliers UFG PM Barometer

2ND TRIMESTER 2010



■ Economic cycle
■ Real estate cycle

→ Key figures

	SI Take-up 1 st trimester 2010	Offer available at the end of march 2010	Vacancy rate	Under construction available supply	Prime rent
Paris CBD	82,500 sq.m	409,000 sq.m	5.80%	45,000 sq.m	€700 per sq.m
Southern Paris	72,000 sq.m	286,000 sq.m	5.70%	66,000 sq.m	€700 per sq.m
North Eastern Paris	65,000 sq.m	113,000 sq.m	4.00%	30,000 sq.m	€350 per sq.m
La Défense	8,500 sq.m	162,000 sq.m	4.90%	131,000 sq.m	€545 per sq.m
Western Crescent	81,500 sq.m	831,000 sq.m	11.20%	144,000 sq.m	€505 per sq.m
Inner Rim	44,500 sq.m	530,000 sq.m	9.40%	88,000 sq.m	€340 per sq.m
Outer Rim	104,500 sq.m	1,189,000 sq.m	6.40%	122,000 sq.m	€215 per sq.m

Sources: IMMOSTAT and COLLIERS UFG PM, April 2010.

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