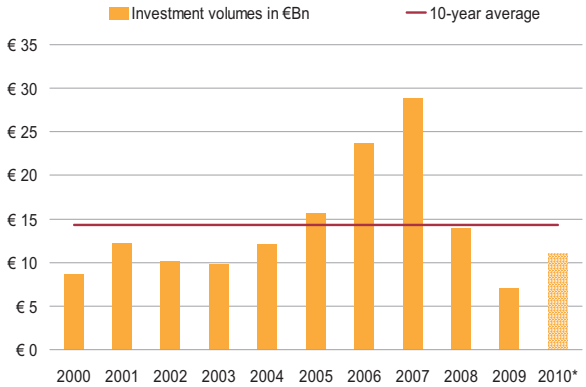
France investment bulletin

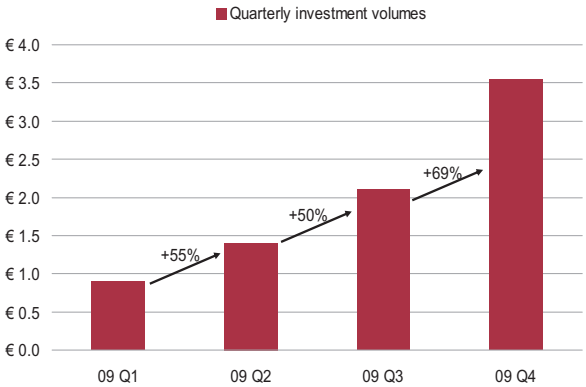
Winter 2009-10

Investment volumes



Source: Savills Research / * Forecast

Quarterly investment volumes



Source: Savills Research

"Paris, and in particular the Central Business District, remains a secure and privileged destination for core funds seeking to invest in secure office property "

Pascal Rupert (Director Investment)

- After reaching the bottom of its cycle in the first quarter, the French market levelled out with an average quarterly growth of 58%. In 2009 the amount invested totalled €7.9 billion (-43.2% y-o- y), half the average volume of the last ten years.
- The credit market has slackened slightly encouraging the return of high-volume transactions.
- In the early part of the year, buyers were displaying interest almost exclusively in ultra-secure opportunities – office and retail property located in Paris, and particularly in the Central Business District. Almost no activity, however, was recorded in secondary locations or for secondary products.
- However, in the second quarter, core funds with rising levels of liquid assets faced with a very weak supply of prime property shifted their interest towards secure assets in the inner suburbs.
- Prime yields have been pushed down by investor competition. Yields for secondary assets have continued in their adjustment to integrate risk-based premiums.
- The market's recovery will strengthen in 2010. Demand will remain important but limited secure investment opportunities and the lacklustre rental market will restrain the investment volumes, which should range between €10 and €11 billion by the end of the year. The gap between prime and secondary property yields is likely to grow.

Economy and overview of 2009

Economy

The French economy has come out of recession and is experiencing a moderate upturn. The major indicators have recovered, limiting the annual reduction in GDP to 2.2%. The economic situation however remains fragile. Although consumer confidence surveys indicate a relative improvement in the economic climate (+17 annual points up to 92), the employment market has deteriorated significantly – the unemployment rate is 9.2% and business investment has dropped by 7.1% over the year.

Overview of 2009

Investment in commercial property in France totalled €7.9 billion (-43.2% yoy) in 2009, half the ten-year average volume. Having reaching its lowest point in the first quarter the market levelled out to an average quarterly growth of 58% reaching its long-term level at the end of the year. Accompanying this improvement are numerous signs of recovery.

Firstly, banks, although remaining selective are financing higher volume transactions when secured. Since July, 14 deals worth more than €100 million were closed in contrast with only 3 in the first half of the year.

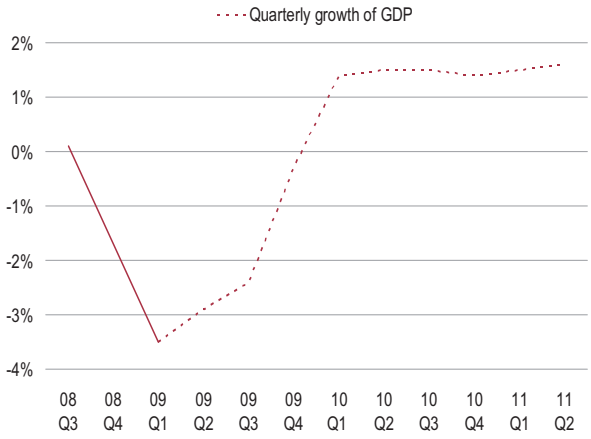
In addition, the proportion of equity capital required by banking institutions has decreased slightly for medium-sized assets. Private investors, with or without private banking support, have successfully been able to secure financing for 70% of the total volume.

Finally, buyers' risk aversion is slightly less pronounced. Demand remains greatest for secured products but supply in this area is fast being exhausted. As a consequence, investors are beginning to turn their attention to assets that are still secure but which are second hand or located outside central districts. Furthermore, value added investment fund activity has increased bringing with it a new interest in property offering a measured rental risk. Consequently, although Paris remains the second European destination for commercial property investment with €3.9 billion committed in 2009, investments have risen by 95.5% in the Western Crescent and by 46.3% in the Inner suburbs in the last quarter. At the same time, regional performance increased by 84.3%, with a strong polarisation of transactions in Lyon.

Despite the market revival, equilibrium both in the investor landscape and the proportion of invested amounts by type of asset is struggling to catch up. North American, British and Dutch investors have been slightly more active in the fourth quarter responsible for 23.2% of investments. The majority of transactions however continue to be initiated by equity buyers. 55.4% of the investment turnover since October has been invested by French investors and 19.4% by German investors.

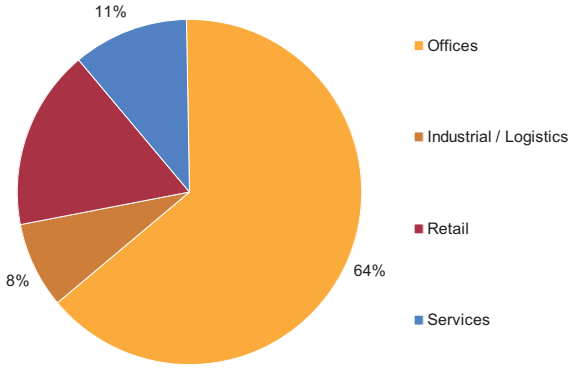
Office space continues to win an increasing share of investment flow - up from 52% of total investment in

Growth



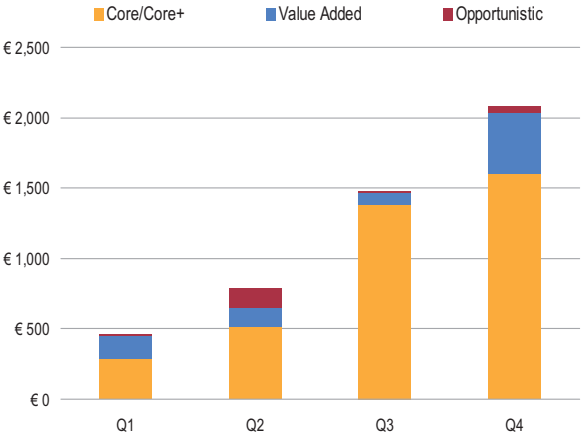
Source: Consensus Forecasts

Breakdown per product



Source: Savills Research

Breakdown per type of funds (offices)



Source: Savills Research

Yields and outlook for 2010

the first quarter to 71% in the last 3 months. At the end of 2009, investment in office space totalled €5.05 billion, a drop of 46.3% against 2008. Bolstered by arbitrage on shopping centres and malls, retail property held its own with annual growth of 16.3% to €1.4 billion – €753 million of which was invested since October. The unfavourable climate in the manufacturing sector and the halt of portfolio diversification strategies sent the industrial warehouses market into a downward spiral. Activity slowed to 62.7% in 2009 at €622 million. The majority of transactions involved grade A warehouses (75%) or grade B assets secured by long term leases (9%). Total investments for industrial properties represented €890 million (-45.5%).

Yields

Investor competition drove down yields for prime property. In the last quarter an office building located in Paris Central Business District was sold at 5.30%, reflecting an annual drop of 105 basis points and a quarterly drop of 20 basis points. Risk-based premiums on secondary products levelled out resulting in increased yields.

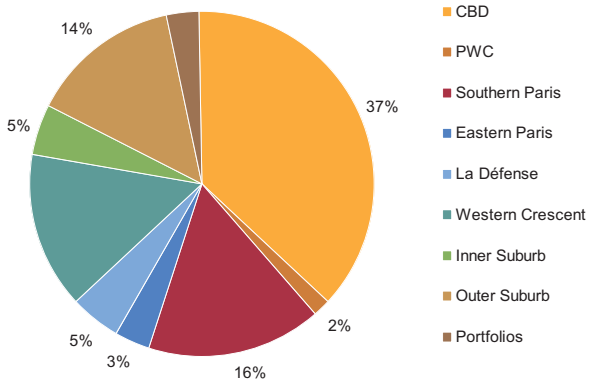
Outlook for 2010

Despite improvements observed over the last few months the outlook for the investment market in 2010 remains uncertain. Investors will retain a marked interest in prime property sectors, with a growing preference for HEQ and BBC certified buildings (High Environment Building and Low Energy Consumption). Foreign investors, stimulated by a more favourable exchange rate, will reinforce their presence. The lack of quality investment opportunities is likely to grow. The number of new opportunities arriving on the market will decrease with the rapid drop in rates eliminating the risk of forced sales. Under these conditions, buyers will be led to broaden their definition of prime property and will revitalise some currently neglected market sectors.

Two factors will influence investment in the coming months. Firstly, the deterioration of the end user market will present investors with the threat of vacancies and falling rents. They will therefore be prompted to delay buying.

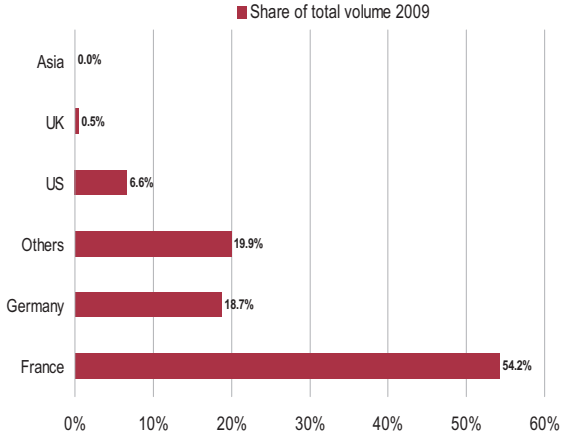
Equally, the possibility of a second shock wave from the financial markets cannot be ruled out. Such an event would jeopardize access to borrowing and therefore the stabilisation of the market. In 2010, investments should total somewhere between €10 and €11 billion. The growing imbalance between supply and demand will once again push prime yields down but this drop will be contained by falling rental values and the likely increase in long term yields. With the market's gradual shift to accepting more risk, second hand and suburban secure real estate should benefit from more sustained demand, but yields will only follow an evolution to integrate risk-based premiums.

Breakdown per location



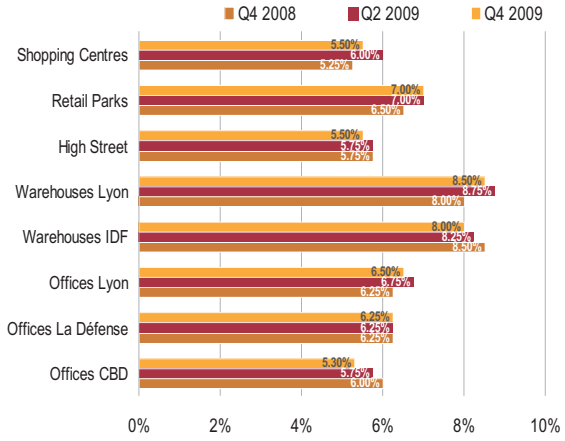
Source: Savills Research

Breakdown per nationality



Source: Savills Research

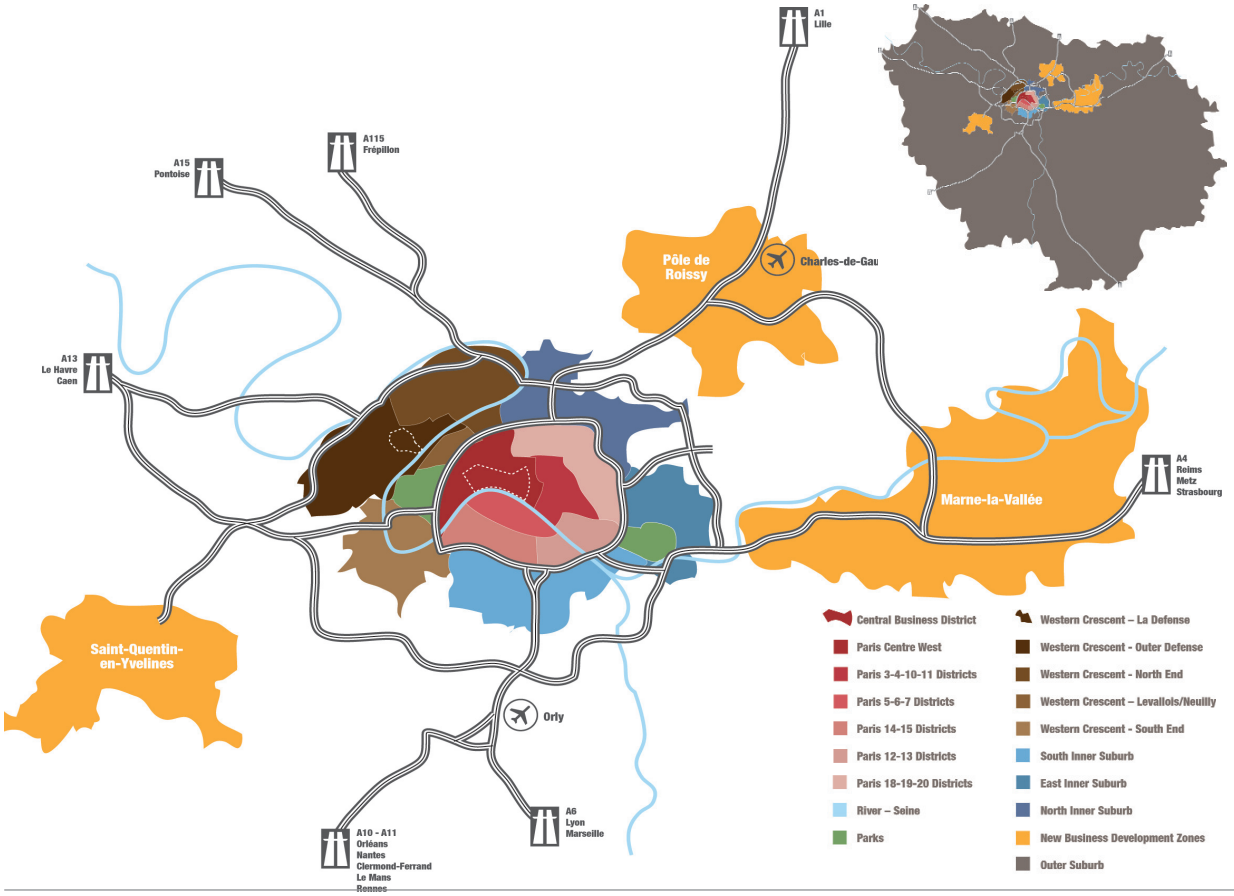
Prime yields



Source: Savills Research

France investment bulletin

Geographic areas



For further information please contact:

Pascal Rupert
Director
Investment
+33 1 44 51 73 89
prupert@savills.fr

Boris Cappelle
Associate Director
Investment
+33 1 44 51 77 17
bcappelle@savills.fr

Lydia Brissy
Associate Director
Research
+44 20 7016 3776
lbrissy@savills.com

Magalie Mollet
Associate
Research
+33 1 44 51 73 88
mmollet@savills.fr

Savills is a leading global real estate service provider listed on the London Stock Exchange. The company established in 1855, has a rich heritage with unrivalled growth. It is a company that leads rather than follows, and now has over 180 offices and associates throughout the Americas, Europe, Asia Pacific, Africa and the Middle East. A unique combination of sector knowledge and entrepreneurial flair give clients access to real estate expertise of the highest calibre. We are regarded as an innovative-thinking organisation backed up with excellent negotiating skills. Savills chooses to focus on a defined set of clients, therefore offering a premium service to organisations with whom we share a common goal. Savills takes a long-term view to real estate and works hard to invest in long term and strategic relationships and is synonymous with a high quality service offering and a premium brand.

Savills
Research

savills.com/research

savills