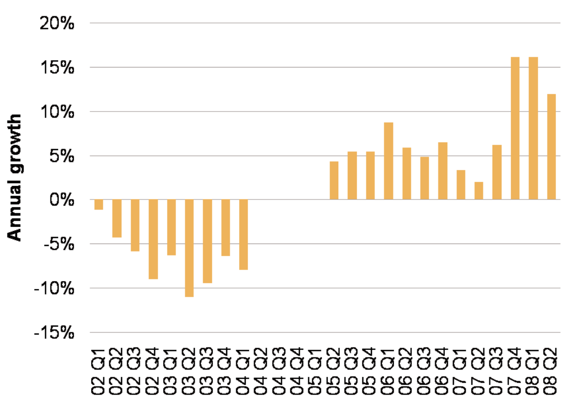
Barcelona office market

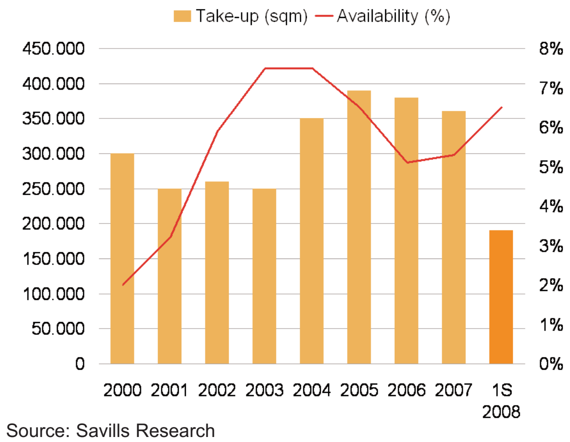
Autumn 2008

Rental growth



Source: Savills Research

Take-up and vacancy



Source: Savills Research

"Through to April, demand and rental values remained relatively stable. From May however, it was apparent that the occupier market was to become sharply weaker, due to the effects of the financial turmoil. This uncertain economic environment has mainly affected the investment market, with a rise in yield expectations on the part of investors of 150 points in the last twelve months".

Eusebi Carles - Director

- In the first semester, Barcelona's occupational market has maintained relatively high take-up rates and does not appear to have been strongly affected by the turbulence in financial markets.

- Notwithstanding economic indicators show an increasing tendency for deceleration, and demand is becoming increasingly affected by long decision making processes. We foresee a decrease in demand for the second half of the year and throughout 2009.

- Office vacancy has increased slightly in comparison to last year. Nevertheless, the vacancy rate remains at a healthy level, due to limited completion of projects.

- As a result of future forecasts predicting a weakening in demand, together with a considerable rise in volume of new supply, particularly from 2009, we are beginning to see a correction in asking rents.

- The misalignment between price expectations on behalf of the vendors and caution on behalf of purchasers has led to a considerable decrease in the volume of investment transactions.

- The sharp readjustment in the investment market has put pricing at a more attractive level for investors. Yields are on the increase, from 5.75% for prime assets. We foresee additional readjustments in the months to come.

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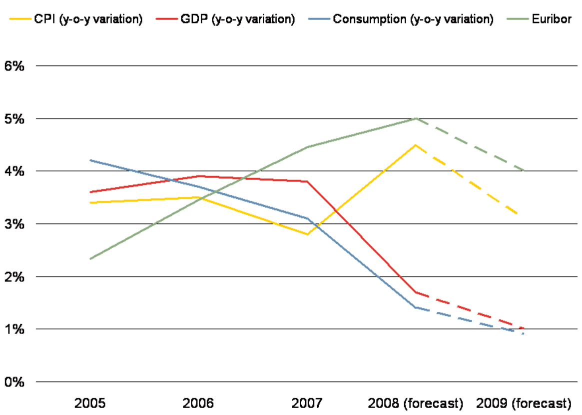
Demand and supply

Economy

Economic indicators for the second quarter confirm the generalised tendency for a slow down. The discreet rise in GDP, of 1.8% annually and only 0.1% for the first quarter of the year, the significant rise in unemployment (10.44% of the active population) and the future growth of annual inflation are some of the factors which confirm the current economic woes.

Main economic indicators



Source: INE, Funcas

Leasing market

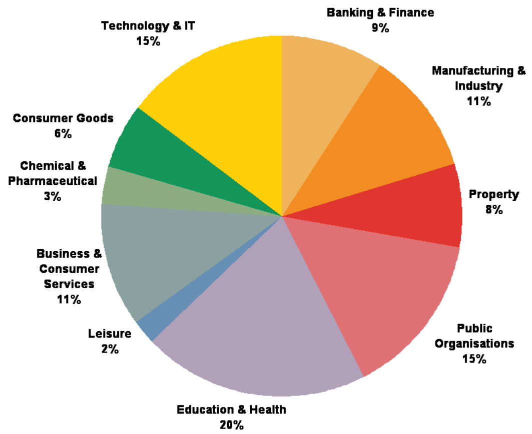
Demand and take-up

During the first semester of 2008, demand has maintained a pace similar to that of the four previous years, reaching approximately 190,000 sqm. The deals that most stand out are those above 1,000 sqm, which represent 80% of the total area leased.

As a result, the decision making process has been prolonged and some of the operations represent deals which should have been completed at the end of 2007. By contrast, the incipient economic downturn is starting to affect the office market, causing a contraction in demand. This contraction is stronger in the demand of smaller areas where the occupiers are being the first to show signs of caution.

Public entities have once again become players, with regard to demand in Barcelona during the last few months, representing some 15% of the total take up. The health sector has been the key player during this semester, mainly due to two large acquisitions for owner occupation, which absorbed approximately 20% of the total rental area. This type of deal has been particularly relevant this semester, accounting for 29% of the total absorption.

Take-up by sector



Source: Savills Research

Supply, stock and vacancy rate

During the first semester of 2008, 150,000 sqm of new supply have been added to the office stock in Barcelona, currently equating to 5.4 million sqm. With regard to developments handed over in this semester, 80% is incorporated as available stock. As a result, the vacancy rate has increased slightly reaching 6.5%, which equates to a total market vacancy of 357,000 sqm.

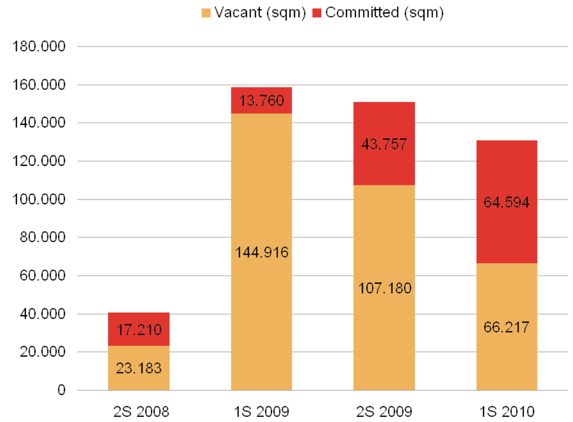
Due to the current credit crisis, the hand over date for several projects will be delayed, mainly due to the lack of finance. The majority of the projects that do not initiate in the current climate are unlikely to be delivered before 2012. Those projects which have commenced construction will be completed approximately to plan as they already have finance in place.

Taking into account the probability of completion of each project, we estimate that in the next 24 months some 480,000 sqm will be delivered, 30% representing turnkey operations and/or pre-lets. Those areas which have the largest number of developments include 22@/Poblenou, Plaza Europa/Gran Via Sud and San Cugat del Valles. These locations comprise some 90% of the new supply over the next two years. Companies who seek to consolidate their activities into one building or relocate to more efficient and modern facilities, will identify these areas as the main alternatives to the traditional CBD, where vacancy is below 2% and rents are comparatively higher.

The projects which are currently being developed will deliver a substantial volume of new supply onto the market in 2009, especially from the second quarter. This together with a weaker foreseeable demand will inevitably place downward pressure on rents.

Investment market and outlook

Development pipeline over the coming 24 months



Source: Savills Research

Rents

Following significant growth in rents at the end of 2007 early 2008, particularly in the CBD area, we have seen stabilization over the past few months. The maximum asking rentals in this area reaches 29€/sqm/month. However, due to the possible fall in demand, we have observed over these past few months some downward rental adjustment in certain buildings and greater flexibility on the part of landlords.

Invesment market

In the first six months of 2008, the volume of investment was some 616 million euros, which represents a 30% decrease from the previous year.

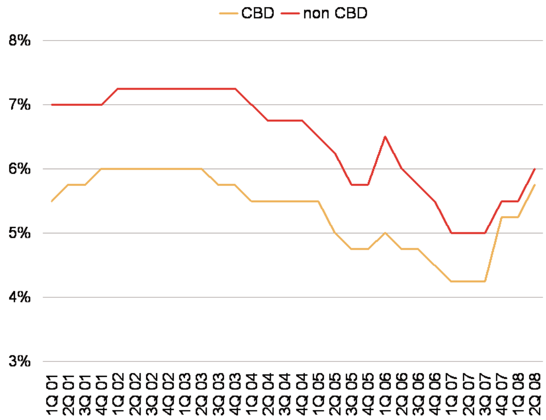
This fall in transaction level has come about in an environment where there is a far greater availability of product on the market. This has given rise to a large number of uncompleted open market sales processes, a relatively new phenomenon in the Barcelona investment market.

This situation can be explained due to the misalignment between the vendors’ price expectations and the purchasers’ greater aversion to risk, with very conservative offers being made. This combination of factors has rendered the closing of investment deals far more difficult, leading to a considerable drop in the volume of deals, with prime yields in the region of 5.75%.

Of all the investment formats, turnkey operations and land sales have been the most affected by this situation. Forward sales deals have also been hit hard. In the current market where risk is heavily penalised, transactions with the greatest probability of completion are those which offer buildings leased to grade A covenants, with low vacancy rates, sustainable rents and long term contracts without break options.

Other formats, which had previously fuelled the investment sector, such as floor or module sales to small investors and occupiers, and changes of use of properties, are in far lower demand, due to the dip in the housing market and the difficulties of finance. Vendors can no longer look to these alternative sales structures which adds to the growing lack of liquidity of assets.

Prime yields



Source: Savills Research

Outlook

Office take up will likely see a year on year fall of some 25% at the end of 2008. However, completion of new developments in the last quarter of 2008 will be limited for which reason we do not anticipate a significant rise in vacancy rates, and consequently the potential fall in rents should be mitigated.

However, given the fact that we are seeing a fall in levels of demand, and a number of projects for 2009 are currently being marketed for pre-lets we expect to see some rental reduction before the end of the year, which will continue into 2009.

With regard to the investment market, the immediate future will depend primarily on evolution of interest rates, the availability of finance and the pressure on property companies to sell. In essence, the market has already corrected yields by 150 basis points. In the current climate, some property owners, not necessarily under pressure to sell may choose to hold assets until the market shows signs of settling. Alternatively, those groups with greater immediate needs for liquidity, may have to be more creative in proposed sales structures to attract buyers in a market where lending is severely restricted.

In our opinion we believe that the market will see further and growing negative effects in 2009, as supply increases, the economy weakens, financing remains scarce and uncertainty continues to reign.

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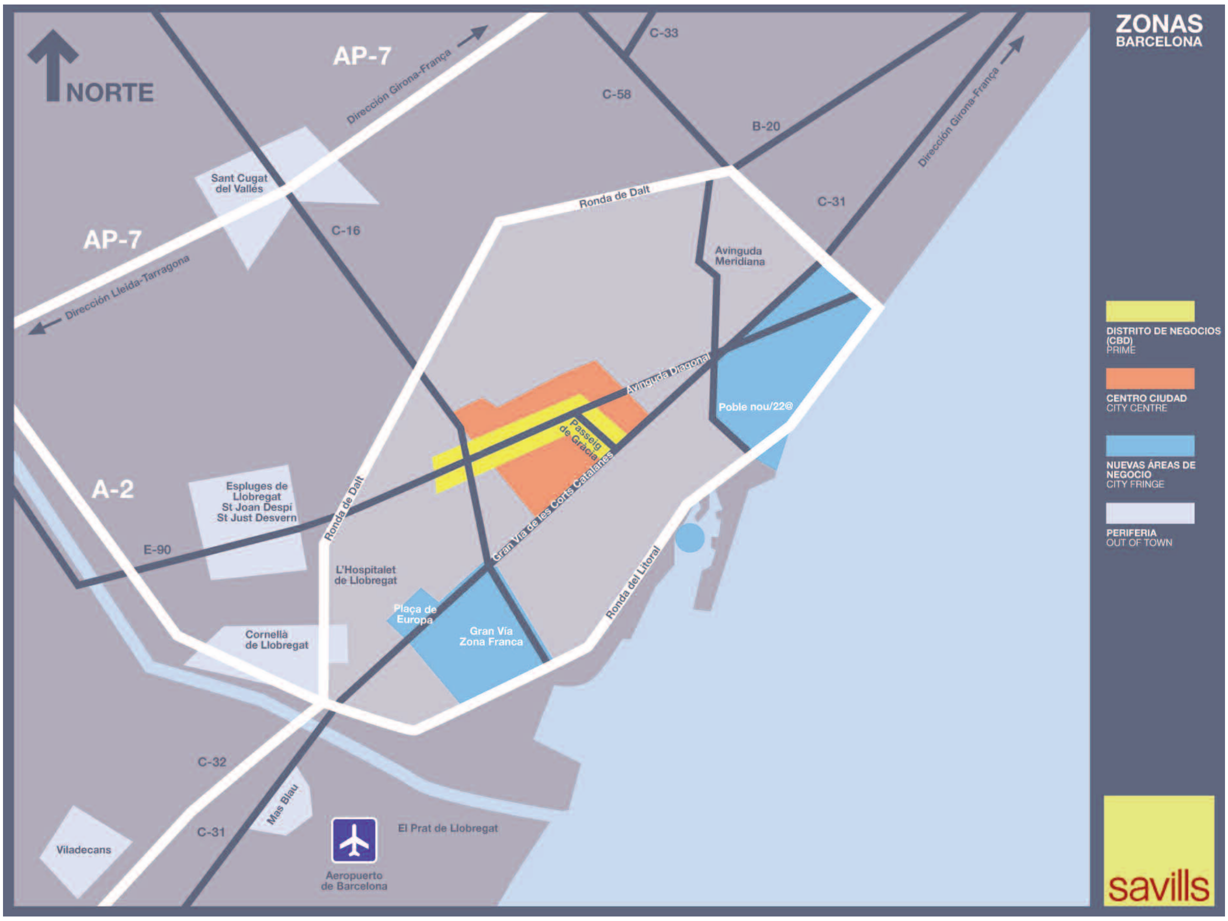
Barcelona office market map



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