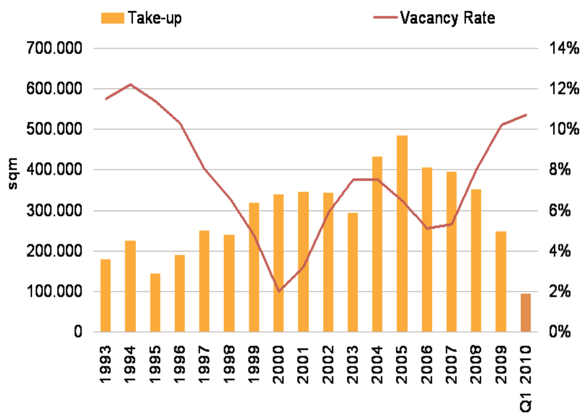
Barcelona office market

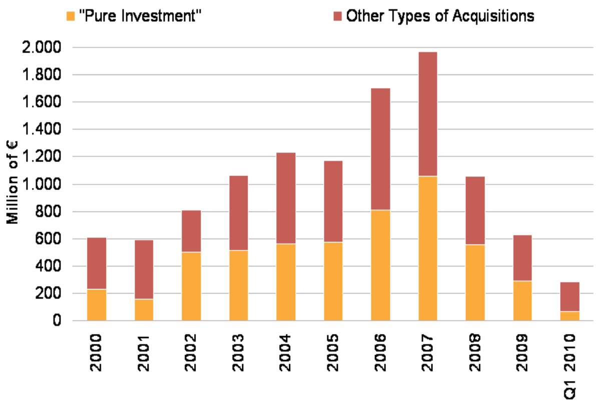
Spring 2010

Take-up and vacancy rate



Source: Savills Research

Investment volume



Source: Savills Research

"There has been an exceptional level of office take-up activity in the first quarter. Combined with compression of prime yields and a certain stabilisation of rents, this seems to have resulted in a change of trend of capital values that will have to be maintained over a few consecutive quarters before we can confirm it."

Eusebi Carles (General Manager Barcelona)

- The letting market in Barcelona has started to show the first signs of recovery in office demand in Q4 2009, following a very quiet previous year. The volume of take-up in Q1 2010 has exceeded all expectations, with an increase of 130% from the same period in 2009.
- Practically no new supply has come to the market. We expect the completion of nearly 224,000 sqm of new stock throughout 2010, of which 60% will be speculative, mostly in the New Business Areas. This will lead to an increase in vacancy rates, which could reach 1994 levels.
- Rents remain unchanged from last quarter in all Barcelona's office sub-markets. Prime rents in the CBD remain at €20/sqm/month, reflecting a year on year fall of 16%. This fall has been less prominent in the Periphery and the New Business Areas.
- Over the first few months of this year there were five investment transactions, with a total value of €291 million. Although the actual level of transaction size is lower than this figure suggests, there are some signs of optimism creeping back in. The number of investors keeping an eye on the market is increasing, and prime yields are still falling steadily.

Economy and demand

Economy

The European Union's economy is slowly recovering from the longest, deepest recession since the Second World War, although there are still a number of obstacles that will make any recovery fragile. Although a large number of countries in the EU started to record positive GDP growth in summer 2009, which "technically" brought them out of recession, this growth slowed down in Q4 2009 as the effect of a number of temporary tactical measures wore off.

Spain recorded quarter on quarter GDP growth of 0.1% in Q1 2010, with a year on year fall of 1.3%. Thus the Spanish economy also comes out of recession following six quarters of falling GDP, the longest destructive period experienced by any of the developed economies.

On the plus side, the rate of decline in consumer spending and investment continued easing during the first quarter of 2010. Household spending grew from -3.5% to -0.6%, and was given a big helping hand by a 30% increase in car sales. However, other goods (food, housing etc) keep their downward trend although at a lower pace. The drop in investment in equipment eased considerably from -15.3% to -2.5%. Although these data are positive, this improvement could well be a result of fiscal stimuli which may have temporarily boosted consumer spending levels. However, the high levels of consumer and corporate debt, combined with a lack of available credit, could turn this trend back around.

The hardest problems to solve for the Spanish economy are the high levels of public deficit and the alarming level of unemployment. Since the start of the global downturn, some 2.8 million jobs have been lost, and the unemployment rate has increased from 8% to 20%. The labour market will continue to be plagued by pessimistic forecasts of investment and the real estate sector's struggling recovery. Consequently, there will be a noticeable fall in household spending (which has accounted for 50% of GDP until now). It will be hard to maintain economic growth via public spending, bearing in mind the troubled state of the public sector (ie a vast deficit).

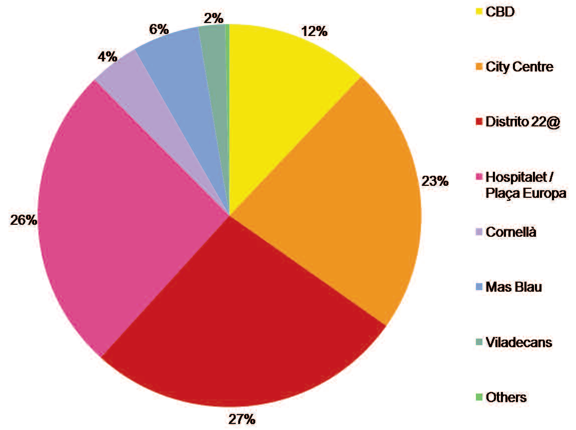
Although an improved international economic climate could help stimulate Spain's economy through exports, there is also the risk that the ECB could raise interest rates if it feels that the powerhouses behind the European economy (France and Germany) start to show solid signs of recovery. The subsequent negative impact on household spending and investment could outweigh the positive impact of increased demand for export goods elsewhere in the eurozone. We will have to wait and see to what extent this recovery could help Spain, and whether the Government's intended structural reforms will be both effective and sufficient.

Letting market

Demand and Take-up

The letting market is starting to show signs of recovery following a very quiet 2009. In Q1 2010 there were 95 deals, reflecting a gross take up of roughly 94,500 sqm an increase of 133% from the 40,500 sqm recorded this time last year. The recovery appears less significant when compared to take-up levels from Q1 2008 (+9%), when the rental market had not yet started to feel the effects of the economy starting to go downhill.

Take-up distribution by sub-markets



Source: Savills Research

Deals in excess of 1,000 sqm have taken the limelight in Q1 2010, with 75% of total take-up accounted for in just 13 transactions. The majority of these deals were in the New Business Areas (64%), with the remainder split evenly between the City Centre and the Periphery. For example, the consultancy Sellbytel Group chose 22@ district as the location for its new offices, where it has leased four floors in D197 owned by Credit Suïsse - a total of 4,358 sqm. Bankpime also opted for an off-prime location, and has leased an entire building comprising 2,753 sqm on Pere i Pons.

Other deals of interest include the new headquarters that Grupo Ferrer is planning in the Biopol in l'Hospitalet de Llobregat totalling 17,500 sqm, and the sale of a building over 2,000 sqm Calle Consell de Cent in Barcelona.

The New Business Areas are proving that they have become consolidated. Nearly 54% of all floor space taken up and 23% of all deals were closed in these

Rents and investment market

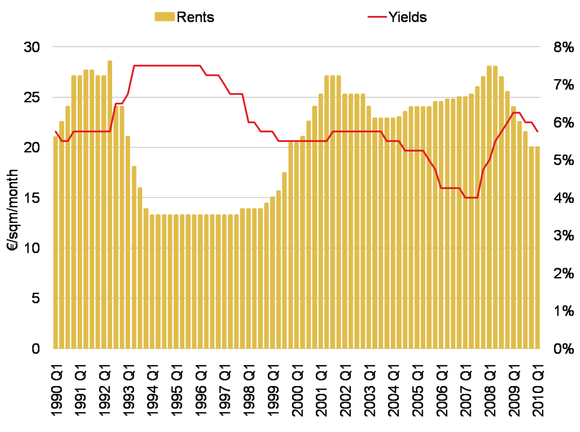
areas. Availability of large floor areas, new and highly efficient buildings and continually improving services and communications network, are all helping attract businesses to areas such as the 22@ district or Plaça Europa, where the average deal size is 1,060 sqm. Deals for under 500 sqm are still focused in Prime or City Centre areas.

Supply and Vacancy rate

Practically no new built offices came onto the market in Q1 2010. Consequently, the total office stock in Barcelona remains at 5.3 million sqm - similar to last quarter. However the vacancy rate rose quarter on quarter from 10.2% to 10.7%. This half percentage point increase mainly reflects the reduction in office size that many companies have been forced to implement, either to reduce or optimise their productivity.

Despite the discernible reduction in new office development, the completion of nearly 224,000 sqm of new supply throughout 2010 will mean a notable increase in the vacancy rate. Although only 60% of the development pipeline is speculative, we estimate that the vacancy rate will easily rise above 12% by the end of 2010, taking into account and optimistic neutral net absorption scenario.

Prime rents and yields



Source: Savills Research

Rents

Following six consecutive quarters of falling rents, Q1 2010 has finally seen an end to the slide, with rents staying unchanged from the previous quarter in all of Barcelona's office sub-markets.

Prime rents in the CBD remain unchanged at €20/sqm/month, reflecting a fall of 16% from this time last year. The drop has been less pronounced in the Periphery and New Business Areas such as the 22@ district, with falls of 11% and 5% respectively. We predict that rents will fall slightly (or even remain stable) over the coming months. It is possible that the market will start to show signs of recovery towards mid 2011 as it starts to absorb new supply, which is not expected to increase significantly until at least 2012.

Investment market

The investment market has remained sluggish, as clearly depicted by the small number of deals that have been closed. There were five investment deals in the first three months of 2010 to make a total sum of €291 million; however, the small number of deals that make up this figure, and the fact that some of them had already been agreed last year, paint a less positive picture than this total might lead us to believe.

Nonetheless, the market is showing some signs of optimism. The number of investors keeping an eye on the market is increasing, and yields in the best areas are still falling steadily. The Achilles heel of the market is without doubt the lack of quality product for sale, which has resulted in highly competitive bidding situations when buildings come to market at a fairly reasonable price.

Forecasts

We predict that a number of different macroeconomic factors will still prove to be a Sword of Damocles over the market until any substantial market recovery takes place - which is not likely at any point in the next nine months.

Consequently we believe that, although the letting market will continue to show improvements from 2009 levels, it is clear that any such improvements will be slight. This realistic approach will result in a noticeable rise in vacancy rates, which could start to drop back again during 2011 - the point at which current vacant stock levels will start to fall, and when we should start to see more robust and consistent signs of recovery.

Barcelona office market

Survey map

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