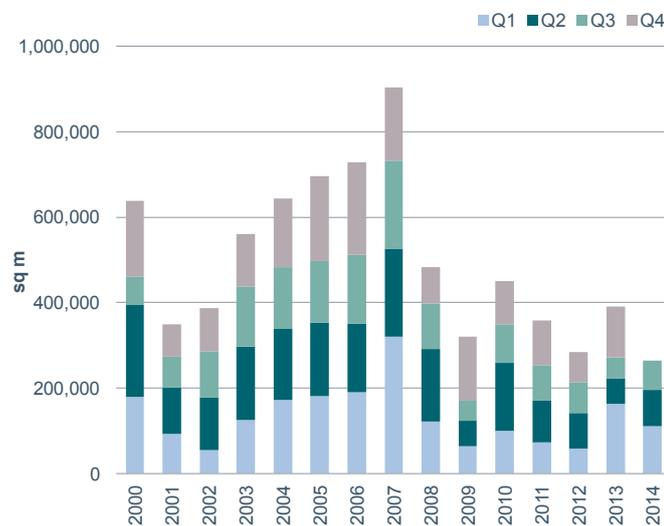


Market Report Madrid offices

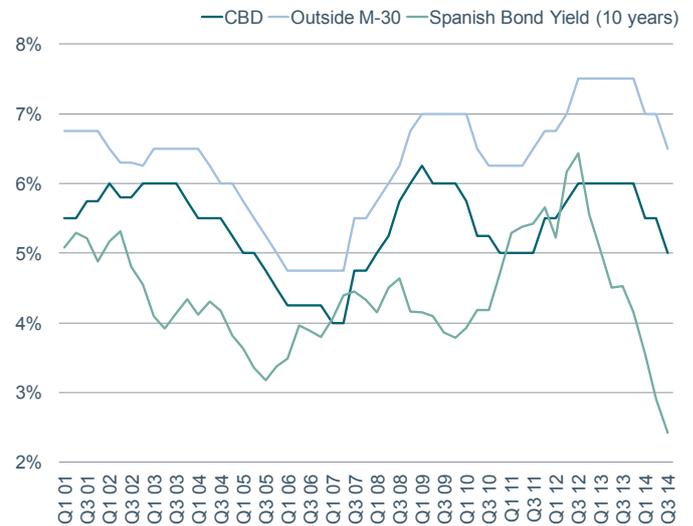
Q3 2014

GRAPH 1
Annual Take-up



Source: Savills

GRAPH 2
Prime yields vs Spanish bond yields



Source: Savills, INE

SUMMARY

Number of investment deals at pre-crisis levels

■ The volume of take-up registered since January stands at a similar figure to that seen in the same period the year before, just 3% below, however, we must note that the 2013 figure was heavily inflated by the letting of the new Vodafone headquarters. If we disregard this transaction, the y-o-y change stands at 19%.

■ In terms of transactions, demand was much more active, with 25% y-o-y more commitments registered between January and September 2013.

■ In addition, the number of transactions registered so far this year, equates to 80% of the total in 2013.

■ The overall market vacancy rate continues to touch on 14%.

■ The average closing rent in commercial properties has continued to rise, thanks to the good performance of sole-use office buildings, where the number of transactions signed at the highest recorded rents has increased. Conversely, the number of lettings signed at below €10 per sq m/month has fallen.

■ The Madrid office investment market has now reached €1.25bn, which accounts for 60% of the total investment across the whole of Spain. This is now more than twice the amount of investment registered in 2013 and the number of transactions is now back up to pre-crisis levels.

■ The increased confidence in Spain and appearance on the scene of Socimis (Spanish equivalent of REITs) has driven up demand considerably, although this is not being serviced due to the lack of product on the market. The knock-on effect: yields are falling.

Economic outlook

The Spanish economy continues on its path to recovery. For the first time since the start of the crisis, many Spanish economic indicators are above those of the Eurozone.

According to data published by Eurostat, in Q2 the y-o-y economic growth stood at 1.2%, compared to 0.7% in the Eurozone. All of the above has improved national and international investor confidence in Spain's economy and the expected increase in forecasts from various bodies, who believe that the economy will continue to improve.

However, it would appear that the strong economic increases registered so far, particularly in terms of national demand, have been due to a rebound effect. Hence, the growth of various variables is now beginning to slow. On the one hand, the latest Retail Index data published by INE, shows that the progress made between July and August has slowed compared to Q2 figures. In addition, the Consumer Confidence Index published by CIS, registered a y-o-y change of 27.80% in August, the lowest figure over the past 13 months.

In any case, national demand had a positive effect on economic growth for the second consecutive quarter. This fell very slightly compared to the previous quarter, due to a slight decrease in public

spending. External demand improved compared to Q1, thanks to a recovery in exports, going from -6.6% to zero.

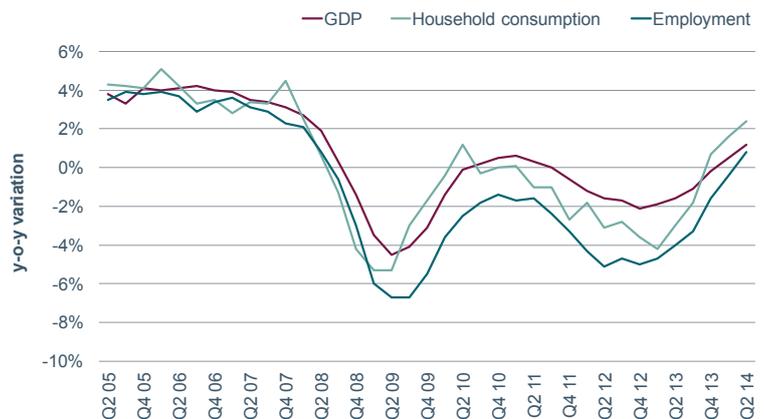
It appears that the job market is beginning to verge on net employment. The latest EPA publications (Q2), show the first y-o-y growth in employment since the start of the crisis (0.8%), which was complemented by a third consecutive quarter of the unemployment rate falling. After five years of decreases, the number of people signed up to social security also increased. Despite this, it would still be a huge undertaking to return to the employment figures seen prior to the recession.

In terms of the balance of payments, according to the Bank of Spain, accumulated data over the

last 12 months produced a lending capacity of 0.7% of GDP.

Finally, despite the fact that the Spanish economy is on the path to recovery, it currently finds itself in a slightly conflicting situation. The most competitive countries in the Eurozone, which up until now had strong economies, are now beginning to show signs of weakness. This could affect the Spanish economy, although at the same time, it will bolster further confidence in Spain.

GRAPH 4 GDP, consumption and employment



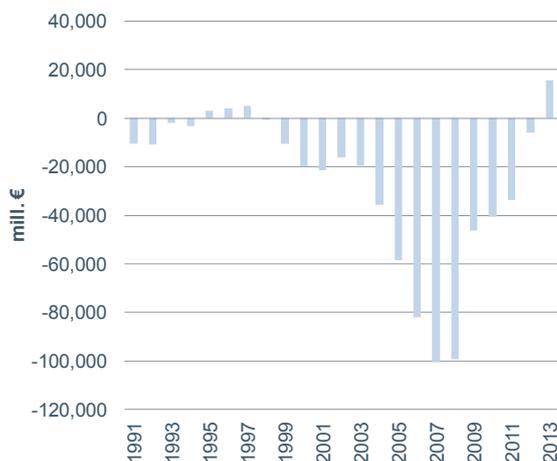
Source: INE

TABLE 1 Economic indicators

Indicator	2013	2014*	2015*	2016*	2017*
GDP	-1.2%	1.2%	1.8%	2.1%	2.2%
Consumer spending	-2.1%	1.9%	1.8%	2.0%	1.9%
Unemployment	26.1%	24.7%	23.4%	21.8%	20.5
CPI	1.5%	0.1%	0.7%	1.1%	1.2%

Source: Focus Economics (october 2014) / *forecasts

GRAPH 3 Balance of payments



Source: Banco de España

Take-up and demand

As was to be expected, the summer break affected activity in the office occupier market. The almost 67,000 sq m contracted between June and September hardly accounts for 26% of the 2014 aggregate total, however, in comparison to the same quarter a year ago, the same figure is up 40%. The year-on-year variation in registered take-up since the beginning of the year, stands at -3%, which is due to the 50,000 sq m Vodafone letting which heavily inflated take-up in 2013, if this figure is disregarded take-up would be up 19%.

In terms of transactions, both the quarterly comparison, as well as the accumulated comparison have risen by 45% and 25% respectively. In addition, it is important to point out that the number of transactions registered up until now, equates to 80% of the total figure in 2013.

It therefore seems that the market is limbering up little by little, which is corroborated by INE's latest Business Confidence data, which shows signs of stability compared to the previous quarter (it hardly increased more than 0.2%), but stands at slightly over 9% compared to the same quarter in 2013.

Size of spaces

There continue to be more large-scale lettings (over 1,000 sq m) compared to small lettings (less than 499 sq m), which in Q3 did not even account for 50% of the

total. Despite this, it is important to point out that the average size in this space bracket has gradually increased over time and currently stands at around 300 sq m. Whilst the medium sized office space sector remained stable at close to 700 sq m, the large space category fell to 2,600 sq m, 20% less than the average level since 2000. This is not unusual if we take in to consideration the number of mega-deals signed in the pre-crisis era and the relatively few lettings of over 10,000 sq m over the past few years.

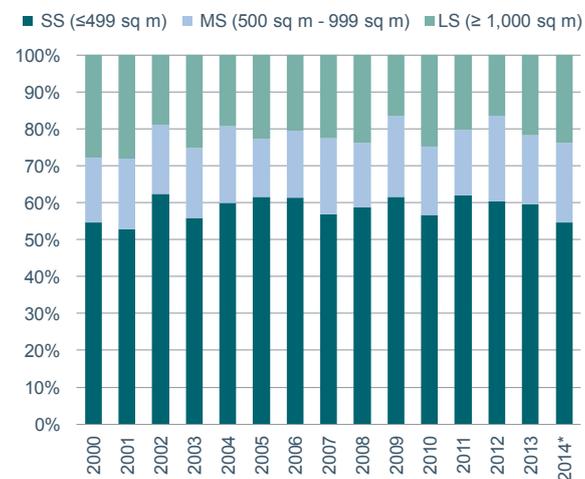
City centre vs. out-of-town

Occupiers looking for office space continue to focus on inner city locations, primarily within the M-30 ring road. The renovation of out-of-date office spaces in the city centre, as well as the marked drop in rents from the top of the market, has meant that since 2009, more than 50% of the transactions signed were concentrated within the M-30 ring road.

On top of this, if one carries out an analysis by tier, one can see that occupiers are not just looking to obtain a new location in the city centre, but that they positively value moving closer to the centre of the market, in comparison to their previous location. Hence we are seeing companies move from properties located well out of the city, to the inner suburbs and better quality properties, with good public transport links and rents that are

GRAPH 6

Number of deals by size



Source: Savills / *unit Q3

similar or lower than in other further afield areas.

Sustainability

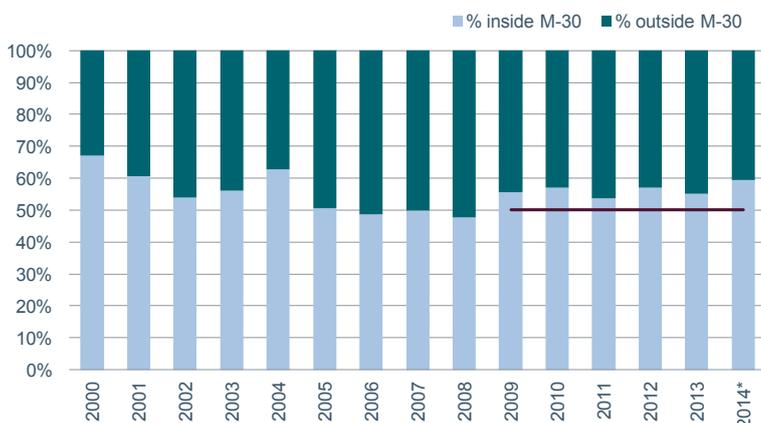
In terms of requirements for new office space, there are ever more requests for aspects related to energy efficiency and sustainability. These requests are generally coming from international companies, who are following the guidelines set out by their head office, and in many cases this involves the office having a seal of approval from an internationally recognised body, which endorses its commitment to the environment.

Up until now occupiers that needed to justify a sustainable office space, started the process to obtain a green certificate for their office, but this green fever has now spread to landlords. We have detected an upturn in the number of office owners that are interested in sustainable properties, as well as an increase in the number of properties that now comply with the main international sustainability rating systems.

On the supply side, hardly 5% of all current office stock is certified, however, many of the refurbishments and new build offices in the pipeline that are expected to be completed over the upcoming years are working towards gaining these certifications.

GRAPH 5

Number of deals with regards to the M-30



Source: Savills / *until Q3

Current availability

At the end of September, there was around 1.8m sq m of vacant space in the Madrid office market, which means that the vacancy rate has remained at close to 14%. Despite the fact that this figure is high, the consolidation and strength of the main business areas in the market, where supply and demand are relatively balanced, now have a vacancy rate of between 6% and 8%.

Delivery of new space

The total amount of office stock has hardly changed at all and this is due to the extreme lack of construction activity and the fact that some offices have had a change of use. The latest is a property owned by Generali and located on Gran Vía, which is the tourist heart of the city and is becoming an ever more prominent shopping and leisure destination in Madrid. The new hotel will be managed by the hotel chain Vincci, which expects to open its doors in 2016.

New space coming on to the office market is currently only refurbished space, which means that some of the capital's obsolete office space is seeing a much-needed makeover. Some of the latest and most noteworthy properties to come back on to the market, include the previous headquarters of the Social Courts at Calle Hernani 59,

and a property located in the first stretch of the CBD, which back in the day was the headquarters of the publisher Planeta. Both properties have been adapted in order to meet current occupier requirements and refurbished to the most exacting of standards, despite both being very different in style and building specifications.

No new-build office property has come on to the market since 2013. The latest properties to have increased office stock were the Castellana 200 complex and Torre Titania.

The next new-build property to come on to the market will be delivered in 2015, with the completion of the second phase of BBVA's finance city in the northern area of the market. Another large new-build project, which will also be for own-use and also for another financial institution, is the new Banco Popular headquarters, which is being constructed on the plot of land it acquired from Vocento in 2008.

Office space optimisation is all the rage in the business community and large corporations are opting to bring all of their head offices under one roof, in order to increase business efficiency and thereby make significant cost savings.

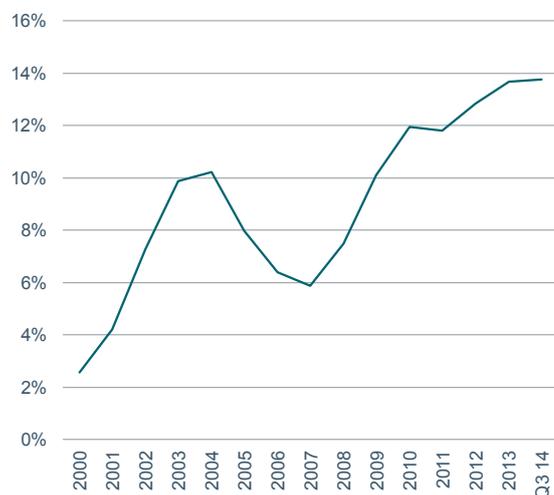
Committed space

Gradually pre-lets are beginning to appear again in the market. What used to be standard practice for new-built office space in the pre-crisis years is making a comeback in refurbishment projects, albeit on a more moderate level, due to the lack of large quality office spaces. The latest letting took place in the replica property across from the one ICEX took recently, which is located on the final stretch of the Paseo de la Castellana.

In addition, the good marketing results achieved for refurbishment projects have encouraged some investors to acquire vacant properties in good locations (preferably city centre), in order to then fully refurbish the properties in order to gain added value.

However, the limited levels of financing that most owners have at their disposal in order to carry out a refurbishment project is a determining factor, when it comes to when the works will start and the scope of the refurbishment. The solution, as was the case over the past few years in the shopping centre sector, is to progress the works, as the various sections of the property are let.

GRAPH 7
Vacancy rate



Source: Savills

GRAPH 8
New developments and refurbishment projects



Source: Savills / *forecasts

Two-speed market

The average closing rent for commercial properties (sole-use and high-tech) continues to rise. The year-on-year change in accumulated data since January is showing growth of 1.2%, but we should point out that the previous figure stood at -5%.

The upturn has primarily been headed up by the good performance of sole-use office properties, where there has been an increase in the number of lettings completed in the top rental brackets and a decrease in the number of lettings signed at below €10 per sq m/month.

The CBD and its immediate surrounding areas are leading the way in terms of rental increases. Lettings at over €24 per sq m/month account for almost 40% in the area, whilst in 2013 they only accounted for a third of the total. We should point out that the highest recorded rents are found in new and renovated properties, or those that are held in high regard by occupiers and these are always found in prime locations.

However, despite the fact that there have been very few increases in areas located furthest from the city centre, we have already detected some increases in very specific heavily consolidated office hubs in

"The CBD and its immediate surrounding areas are registering every more transactions at over the achievable rental figure. This always relates to prime properties, in terms of building specifications and the prestige of the property and these properties are always located in the very best areas". Gema de la Fuente, Savills Research

the inner suburbs and further afield areas.

Incentives

The growth in closing rents for prime properties in the best areas, has also meant that incentives have been reduced, which in turn is increasing the net rent.

Achievable rental price

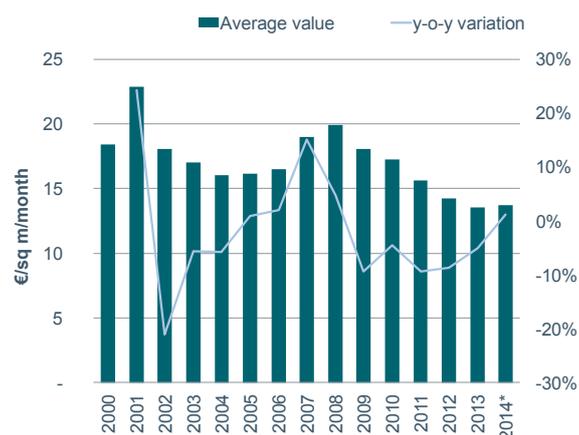
Achievable rents are now trending upwards. The achievable rent in the CBD now stands at €25.50 per sq m/month, which is a q-o-q and y-o-y increase and a reduction in the difference compared to the previous top of the market prices.

TABLE 2 Main deals - Occupier market - Q3 2014

Tenant	Zone	Floor area (sq m)	Activity sector
Grupo Sigla	Urban area	5,700	Professional Services
Técinas Reunidas	North Zone	4,200	Energy
Despacho de abogados	Urban area	3,400	Professional Services
Genómica	Vía de los Poblados	2,500	Industry
Xerox	A-2	2,400	Industry

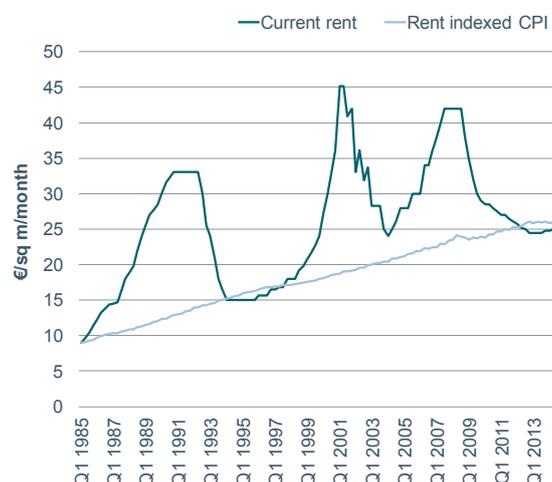
Source: Savills

GRAPH 9 Average closing rent and y-o-y variation



Source: Savills / *until Q3

GRAPH 10 CBD Rent



Source: Savills / INE

Investment market

The surge in investor activity over Q3 in the commercial property market has driven the investment volume transacted up to more than €5.5 billion, which is now double the figure achieved in 2013.

A study of the office sector shows that the aggregate total up until now and across the whole country, stands at slightly more than €2 billion, this has also doubled the total registered for the whole of 2013 and also exceeds the average investment volume over the past five years.

The Madrid market accounted for close to 60% of all investment in Spain and 70% in terms of the number of deals.

If we were to compare number of deals in 2014 with 2007, data would show that investor activity is at similar levels. If we were to compare investment volume, and apply the average price per sq m in 2007 (bearing in mind there has been a correction of up to 60% in price per sq m), investment volume in 2014 would have already surpassed that of 2007.

Increase in demand

From the end of 2013 onwards, the improvements in the main economic indicators, growth forecasts and the assurance that the market had bottomed out, favoured an increase in investor confidence in the Spanish market.

In addition, the appearance on the scene of Socimis (Spanish equivalent of REITs), which accounted for 35% of the total investment volume in commercial properties, rapidly increased the level of demand and sped up the need to invest excess liquidity.

Lack of properties for sale

The immediate response from sellers was to increase the amount of properties for sale via open market sales, but this still remains insufficient in order to satisfy the investment appetite of the active players in the market.

There is a clear lack of prime product and this type of property can only be accessed off market, but it is possible to find good opportunities for the remainder of product and locations.

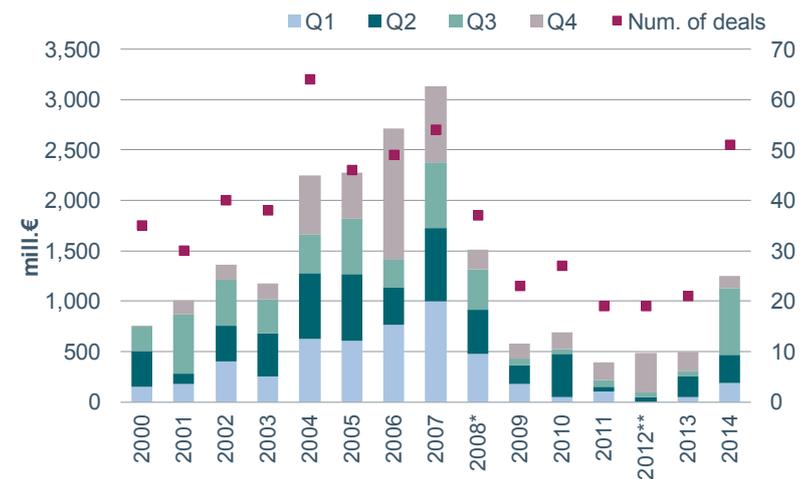
Hence, we will see income-producing properties take more of a prominent role in the last few quarters of the year, but these are just another alternative, as buyers are also looking at secondary and value-add products.

Socimis

Socimis have already invested 80% of the capital they raised, which will mean that they will not be so active in the market over the coming months, although there continues to be talk of new Socimis being set up. The office sector accounted for almost a third of total investment and Madrid was the focal point, accounting for 80% of all office investment.

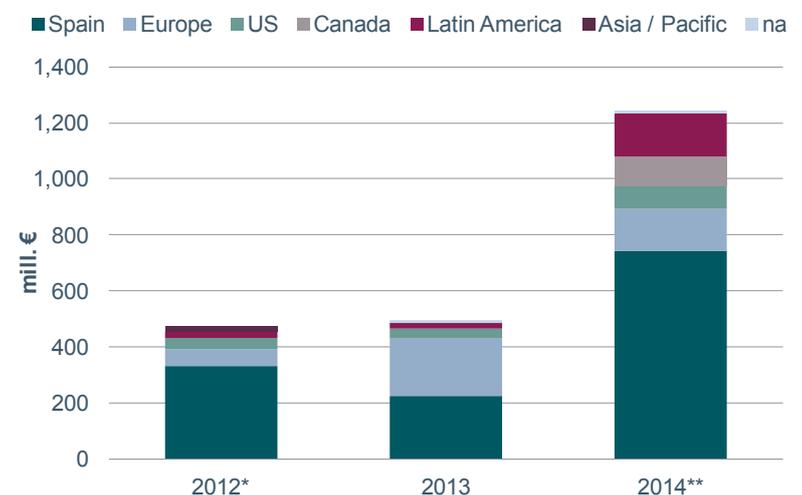
The most frequent deals were portfolio transactions, some of which comprised properties from other sectors, such as the IDL portfolio purchased by Hispania

GRAPH 11 Investment volume



Source: Savills / *excluding Ciudad Financiera Santander / **excluding Torre Picasso

GRAPH 12 Investment volume by purchaser origin



Source: Savills / *excluding Torre Picasso / **until October

"Open-market sales are increasing due to the increase in investor activity and the excess liquidity in the market. Even so, there is more investor appetite than there is supply"». Pablo Pavía, Spain Investment

Activos Inmobiliarios, which comprised four office properties in the northern area of the market and two urban hotels or the Wereldhave portfolio comprising two office buildings, one in Arroyo de la Vega and another in the city centre, which were accompanied by a logistics complex in Rivas Vaciamadrid (Madrid) and a shopping centre in Collado Villalba (Madrid). The latter was signed by Axia Real Estate Socimi. In terms of sole office use portfolios, we would highlight Oncisa's portfolio, which was sold to Hispania for €120m and more recently, and which will form part of Q4's figures, Levitt's properties in the Pau de Sanchinarro that Merlin Properties Socimi acquired for €130m.

Investor profiles

The sudden appearance of Socimis on the scene and their frenetic activity has drastically reduced the market share of overseas investment, having said that, if we

compare absolute values, this figure has increased by 70% compared to 2013.

Socimis have been counted as domestic capital as they are national companies, although they do have a large amount of international capital behind them, which has seen Socimis as a good way of getting their foot in to an unknown market, but at the same time minimising their risk.

Yields

The imbalance between supply and demand for prime properties continues to drive the prime yield down.

Over Q3 the yield in the CBD contracted by 50 basis points reaching an achievable yield of 5%. This equates to a y-o-y variation of 100 basis points. This is merely a benchmark, as certain product in very specific locations has been sold below this figure

and offers are being received at around 4.5%-4%.

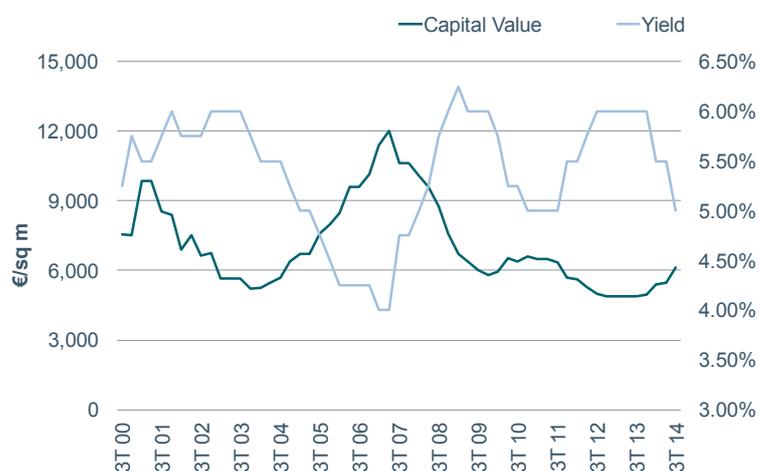
Prime properties outside of the M-30 are following a similar path, although yield compression has been more subdued there: only 25 basis points, which puts the achievable yield at 6.75%. In any case and as is the case in the CBD, the yield for quality properties in consolidated areas, could well be below the achievable level.

Price per sq m

The increase in the achievable rental value and the correction in the achievable yield have meant that prices per sq m have increased, which after 11 quarters has now broken the €6,000 per sq m barrier.

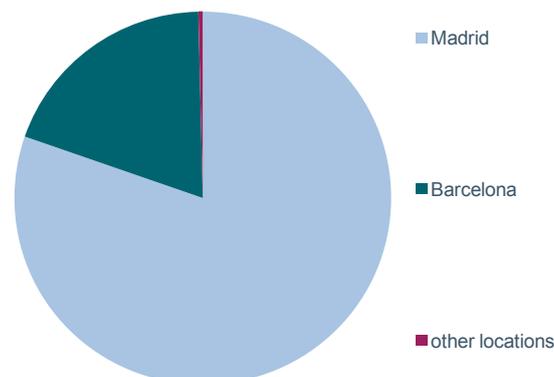
As with the other achievable indicators, this is merely a benchmark figure, as several deals since January have been signed above this figure. Private investors and family offices that are collecting properties, are scouring the market in order to make new acquisitions. ■

GRAPH 13 Prime CBD investment indicators



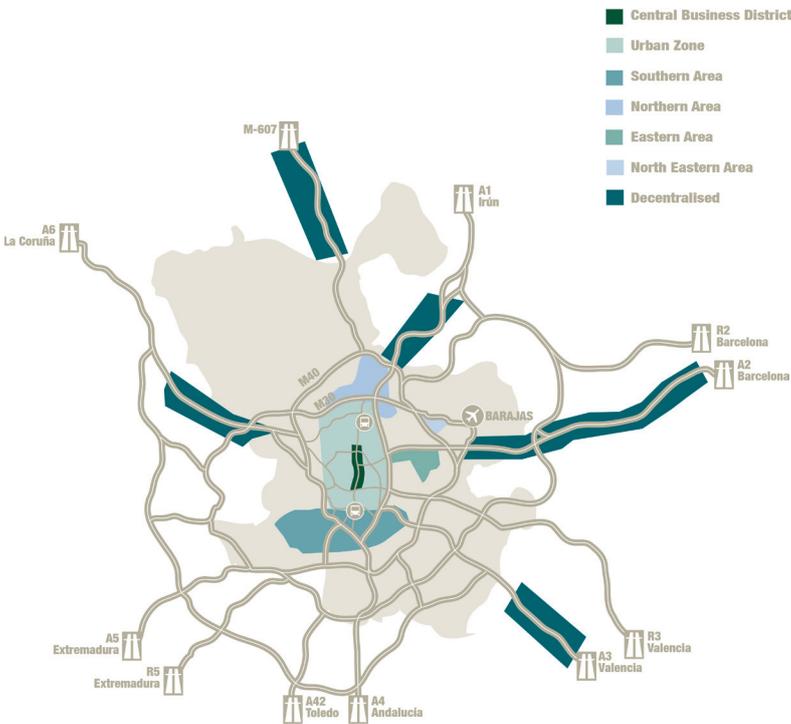
Source: Savills

GRAPH 14 Socimis investment volume by location 2014*



Source: Savills /*until October

MAP 1
Madrid office market



Forecasts

2014

■ Judging by current demand for large office spaces exceeding 1,000 sq m, this sector continues to be active. Various space requirements have materialised both to let and for sale for own-use, and depending on how these negotiations pan out, gross take-up could exceed 400,000 sq m. This figure would be in line with the take-up figure registered in 2013 (including the Vodafone letting), but would still be well off the historic average (around 500,000 sq m), which could be achieved in around 24 months.

■ The recovery in closing rental values is now a reality for the best properties in the best areas (within and outside of the M-30 ring road), due to the lack of quality available space on the market. The majority of secondary areas have now seen their rents stabilise, however, the areas furthest from the city centre, where the extreme lack of demand means that over-supply is not being taken-up, will continue to see rental corrections.

■ The office market investment pipeline is now close to €1bn across Spain and close to 80% of that figure, i.e. €750m, is located in Madrid. Madrid could post an annual investment volume of close to €1.5bn.

■ Buyer pressure continues to push yields down, as despite the fact that more properties have come on to the market for sale, there is still a clear lack of supply in order to satisfy the needs of the different investor profiles.

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