

Market Overview

2ND TRIMESTER 2011

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Commercial property: beware!

In 1974, in the film "The Chinese in Paris" by Jean Yanne, France was invaded by the Red Army, which chose Galeries Lafayette as its HQ. In 2011, the Galeries' sales assistants are once again speaking Mandarin to tourists who gave the store on Boulevard Haussmann a 24% sales boost. A good example of the buoyancy of French commercial property which would serve to justify investors committing to it massively? We shall see...

Looking beyond prime locations and other Parisian flagship stores, underlying domestic commerce is far from dynamic. Indeed, in the wake of the 2009 recession, household spending remains muted due to high structural unemployment rates, low pay rises and the increasing drag caused by inflation on imported products. Furthermore, the prospect of a freeze on welfare payments and public sector salaries, as well as the likelihood of tax increases, signal the decline of the public shock absorber. Although steady high savings rates indicate that reserves exist, they also demonstrate uncertainty about the future, which is not going to encourage consumer spending. In fact, after a prosperous period of sustained growth in consumer spending, which justified the launch of many projects, commerce has once again found itself in an unpromising economic context that is set to persist.

Furthermore, commercial property is undergoing structural changes, such as competition from e-commerce, which accounted for €25 billion in 2010, a not inconsiderable sum when compared to total spending on manufactured products of around €270 billion.

Other changes are also at work, such as a growing preference for city centre locations and the gradual reduction in hypermarket shopping.

As a result, regardless of investors' undiscerning appetites, it is worth differentiating between the types of property that are able to perform well and those that are likely to suffer.

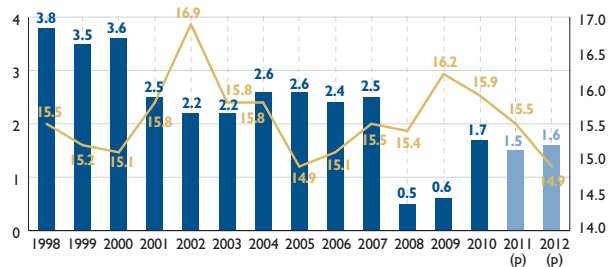
In the city centre retail segment, the gap will probably increase between prime locations in which chain stores are maintaining or even increasing sales, and low-prime and secondary locations which may suffer from periods of vacancy, rent reductions and adjustments to the value of business assets. This dichotomy may however be reduced by the nature of the tenant's business.

In the shopping centre segment, investors need to take the competitive positioning of the product within its catchment area into account. This is particularly the case for centres built recently, which are having greater difficulty ramping up sales and taking longer to do so than before the crisis. As rents paid by chain stores are mainly of the variable sort, the effects of variations in spending are felt immediately...

Finally, the retail park segment is where cannibalisation is taking place the most. In this segment, the parks that will succeed are those with good road access, critical size (greater than 20,000 sq.m.), a food anchor store and the presence of retailers that pull in consumers, such as Darty or Décathlon.

In an environment undergoing constant change, an in-depth analysis of the fundamentals is more important than ever, and this would apply even if the opportunity came up to buy the Galeries Lafayette building.

INTERBANK RATES, RISK-FREE RATES AND PROPERTY YIELDS



Sources: INSEE - Centre de Prévisions de l'Expansion - OCDE, April 2011.

■ Annual GDP growth and unemployment rates at the end of the period
— Consumer spending and household savings rates

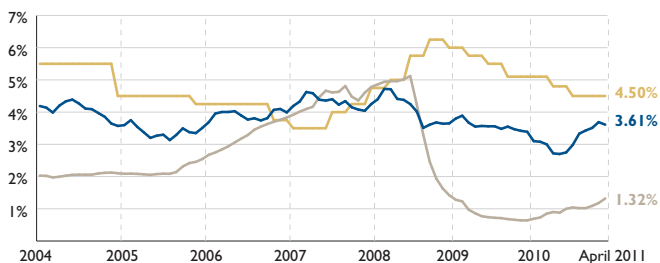
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Financial and economic environment for real estate investment

→ Financial environment

INTERBANK RATES, RISK-FREE RATES AND PROPERTY YIELDS



Sources: BCE / FRANCE TRESOR / COLLIERS UFG PM, April 2011.

- 10-year French treasury bills (OAT) - monthly average
- Prime office yields Paris CBD
- 3-month Euribor - monthly average

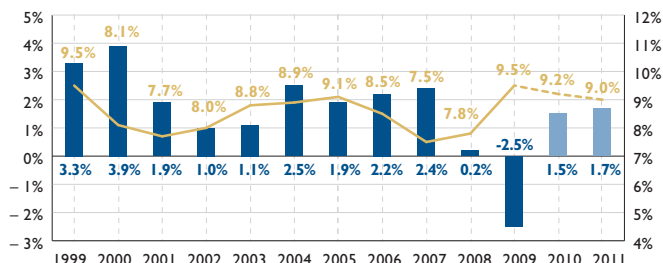
The underlying sovereign debt crisis of peripheral eurozone countries regularly shakes the financial markets. In the first quarter of 2011, it was the Portuguese government's turn to finally admit, by calling on the European Financial Stability Fund, that it would have trouble honouring its bond payments. Furthermore, rumours surrounding the potential restructuring of Greek debt, barely a year after the European bailout plan was set up, are also fuelling uncertainty. Indeed, no long-term solution has been found to the question of a fiscal rebalancing of the eurozone or, consequently, of the financial environment.

« The beginning of the end of very lax monetary policy »

Having exceeded the 2% threshold at an annualised rate, inflation triggered a response – as expected – from the ECB, namely an increase in key interest rates. This increase, limited but marking the beginning of the end of very lax monetary policy, has affected the value of the euro, bond yields, lending rates, particularly on property, and property yields, which are now in the process of stabilising.

→ Economic environment

ANNUAL GDP GROWTH AND UNEMPLOYMENT RATES AT THE END OF THE PERIOD



Sources: INSEE / EUROSTAT, April 2011.

- Annual GDP growth
- Metropolitan unemployment rate (according to BIT)

At the beginning of 2011, French property found itself in a fragile, uncertain economic context. While France, like most European countries, is only slowly coming out of recession, new troubles (the earthquake in Japan, the war in Libya) and new risks (the energy risk, etc.) are making things worse.

In addition, commodity price rises, in energy as well as industry and food sectors, have provoked inflationary pressures in Europe. While a price wage spiral is unlikely in view of high structural unemployment and under-used production capacity, the recessionary effect produced by this drain on household income will definitely materialise.

« A fragile, uncertain economic context »

In this turbulent environment, the French economy, which grew 1.5% in 2010, is continuing to go through a period of consolidation which should put it at around 1.7% in 2011. In this respect, 1Q11 proved to be very dynamic, owing particularly to the upturn in industrial output and corporate investment. After years of consumer-led growth, France seems to be embarking on a supply-led recovery.



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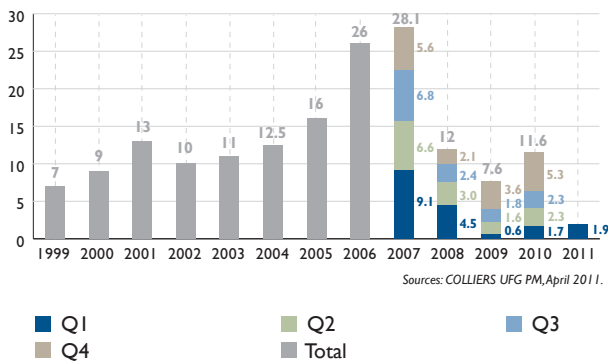


French investment property market

Demanding investors

→ A hesitant start to the year

AMOUNTS INVESTED IN BUSINESS PROPERTY IN FRANCE
(in millions euros)



In the course of Q1 2011, €1.9 billion was invested in commercial property in France, versus €1.7 billion one year earlier. Although this represents an increase, this level of commitment contrasts with the promising results recorded at the end of 2010 (€5.3 billion invested in Q4). There was a notable lack of major transactions at the start of the year, with only one deal worth over €100 million recorded.

While appetite for the property sector is undeniable, investors still prefer to invest mainly in low-risk, high-quality assets. Faced with persistent financing problems, the opening up of the market to “on spec” assets or assets needing conversion work was confirmed in Q1, but only involves a marginal number of investments. Unsecured assets located in markets that are oversupplied or lacking in infrastructure remain illiquid.

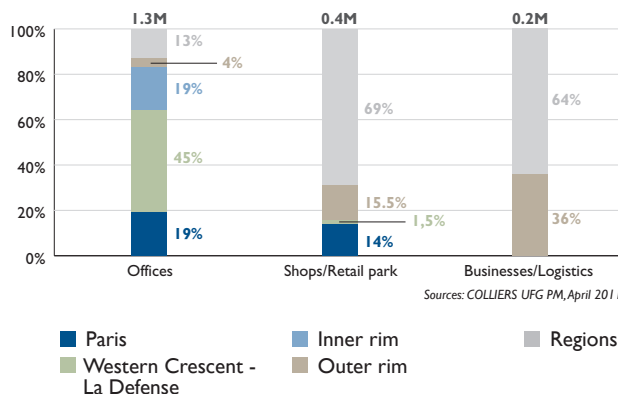
« Investors still prefer to invest mainly in low-risk, high-quality assets »

Caution and careful selection on the part of investors are further demonstrated by certain transactions being abandoned during the due diligence phase.

This demand for core assets is up against a lack of investment opportunities and, to a lesser extent, the high prices being asked by sellers. Indeed, developers (25% of sales) are flooding the market with risk-free products, a trend boosted by users redeploying to new properties. On the other hand, arbitrage programmes with respect to core assets of property companies and investment funds are still limited in relation to demand and are seeking to make the most of favourable market conditions. Prices asked by sellers are however being blocked by increases in lending rates and risk throttling the possibility of a more pronounced recovery.

→ New assets most popular

LOCATION OF INVESTMENTS BY ASSET TYPE
1ST TRIMESTER 2011*



At €1.3 billion, the office segment represented 70% of commitments.

The search for new or recent assets has translated into greater flexibility in terms of geographical investment criteria.

The Western Crescent is the focus of 45% of investment volumes, thanks particularly to the acquisition of Europe Avenue in Bois Colombes by Generali and Predica, for more than €400 million. In the inner rim, two “on spec” transactions, both acquired by developers, bolstered the start of the year: “Le Skallen” in Châtillon acquired by Area Property (€80 million) and 5,300 sq.m. in rue Maurice Arnoux in Montrouge acquired by STE (€25 million). The proportion of business property investment in the provinces has risen slightly, with a very clear preference for new buildings. On the other hand, less than €300 million of commitments were recorded in Paris, the lowest quarterly level since Q1 2009. The scarcity of opportunities on the market and sellers’ demands are limiting investment flows in the capital.

In the retail segment, €400 million have been invested since the beginning of the year. In line with the trend in 2010, this high level is based on acquisitions of shopping centres in the provinces, as seen by the acquisition by Grovesnor of “Heron Parc” in Villeneuve d’Ascq for €95 million.

The amounts invested in logistics platforms and in business premises have reached €200 million, representing 11% of commitments. Buyers favoured new leased logistics platforms located on the North-South axis. Paradoxically, the main transaction this quarter was Gecina’s sale to the Carval fund of a portfolio of 416,000 sq.m. of class B warehouses for €119 million (with several of the assets abroad).

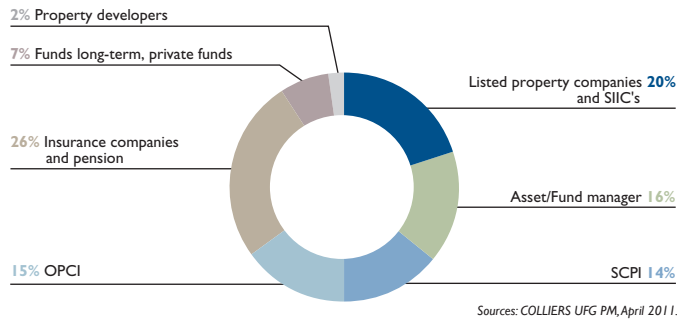
All asset categories combined, the preference for new properties reflects investors’ growing concerns regarding the impact of Grenelle. The increased risk of obsolescence of older assets and higher taxation are accelerating

French investment property market

Demanding investors

→ A market driven by French institutional investors

BREAKDOWN OF INVESTMENT VOLUMES BY TYPE OF BUYER
2ND TRIMESTER 2011

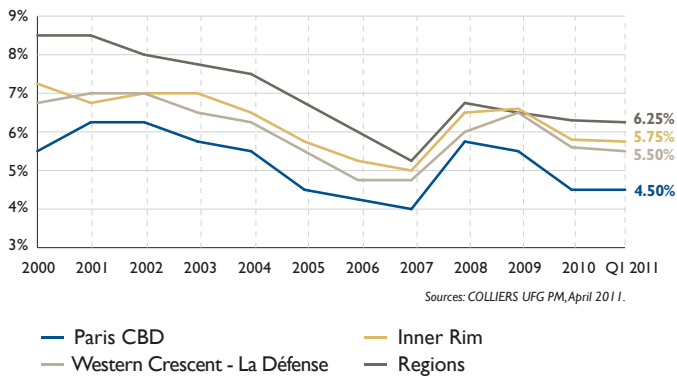


The breakdown of buyers did not change significantly this quarter, buyers with their own funds again being the most active. Foreign players remained in the background, with less than 20% of commitments. Due to a lack of products that meet their requirements, German investors, who invested €1.1 billion in 2010, are conspicuously absent this quarter.

Thanks to the acquisition of Europe Avenue in Bois-Colombes, the insurance companies' share of investment volumes came to 27%. On the back of historic inflows (€2.46 billion in 2010), SCPIs invested nearly €250 million in Q1, half of which was in the provinces. OPCIs, with 15% of commitments, have confirmed their arrival on the investment landscape. Property companies and SIICs together accounted for 20% of commitments and are taking positions on new assets.

→ Will a floor rate soon be reached?

CHANGE IN PRIME INITIAL YIELDS – OFFICES

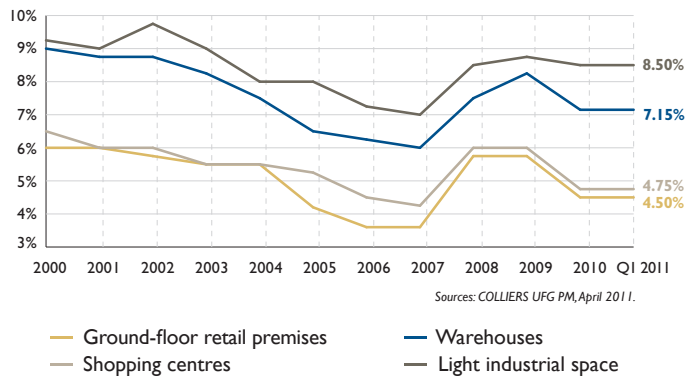


After a sharp adjustment phase between mid 2009 and the end of 2010, the reduction in yields on core assets is continuing albeit with decreasing intensity. On the one hand, sellers became fully aware of the preference for risk-free assets, demonstrated by the increasing number of bids received, and are asking for higher and higher prices. On the other hand, buyers, mainly institutional investors, are almost exclusively taking positions on risk-free assets but are asking for a risk premium in line with the level of risk-free rates. Expectations of inflation, which are likely to push long-term rates up, are prompting investors to take a less aggressive stance than in the previous few months and are opening the way to yields stabilising.

Strong competition among investors, initially restricted to Paris CBD, is now affecting all markets. The geographical ranking of yields is thereby gradually being eroded, ranging from 4.5% in Paris CBD to 6.25% in the large regional conurbations. However, investors are taking a discerning look at all the parameters of an asset (rental market fundamentals, build quality, nature of tenant, etc.) and refuse to compromise on the quality of public transport infrastructure. "On spec" deals are being carried out based on predicted yields of 7.5% and 8.5% depending on location and quality of infrastructure.

→ Status quo

CHANGE IN PRIME INITIAL YIELDS – OTHER BUSINESS PREMISES – WAREHOUSES – RETAIL



Prime yields in the logistics segment have remained stable, ranging from 7.15% to 8% for new or recent warehouses. Assets that are obsolete or less well located are the target of too few investors to be able to give any real evaluation. In light of the weak competition for this asset class as well as fragile rental market fundamentals, yields are unlikely to change significantly over the coming quarters. The business premises segment is attracting few long-term investors, a trend emphasised by the worsening of the rental market and insufficient availability of prime properties.

Investors, and German investors in particular, have shown a marked interest in shopping centres which resulted in a squeeze on yields in 2010. Ranging from 4.75% to 6.5%, prime yields are in the process of stabilising. The latest retail park transactions indicate yields of close to 7%. Competition among investors for city centre retail property in prime locations remains keen, with yields ranging from 4.5% to 5.5% for the best assets.

FOCUS

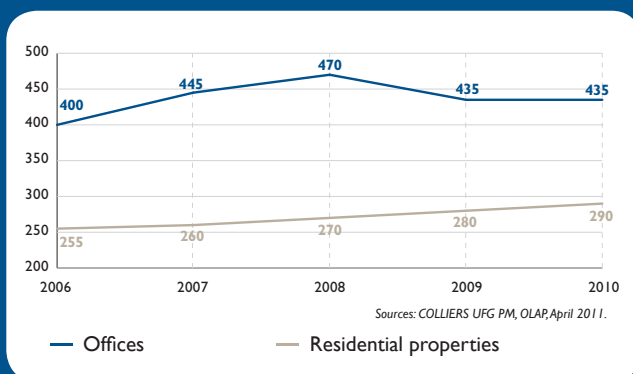
THE LIMITS OF CONVERTING OFFICES INTO RESIDENTIAL PROPERTY

Immense dynamism, and indeed scarcity, in the Parisian housing market have led to the resurrection of the old practice of converting offices into residential property, particularly in the case of old buildings, frequently of the Haussmann type, originally designed for residential purposes. Following the widely-publicised occupation of empty offices by charities, a Bill has been put forward with the aim of levying a tax on vacant business premises. Similarly, the Government will offer exemption from tax on capital gains on the sale of business premises destined for conversion into rental accommodation. A similar programme was previously launched in the capital following the law of 21 July 1994 and the Arthuis plan, which was supposed to provide a solution to the oversupply of office space at the start of the 90s. For the record, results were modest: between 1993 and 1996, only 135,000 sq.m. of office space was converted into residential accommodation whereas vacant stock in central Paris then stood at over 1.5 million sq.m.

Setting aside the technical difficulties, to what extent is converting offices into residential property an economically and financially viable solution?

Business and residential property markets in Greater Paris vary considerably in terms of rental values. In Western Central Paris, while average residential rents are €290 per sq.m. per year, rents for existing offices rise to €435 per sq.m. per year (cf. *graph 1*). In the Western Crescent, residential rents reach €215 per sq.m. per year versus €280 per sq.m. per year for offices. Therefore, in the context of an investment holding, converting offices into residential property results in a significant reduction in terms of the return on the asset. This only makes financial sense if investors believe that the offices will remain unoccupied in the long term, even after refurbishment. Only buildings that lack local infrastructure and are located outside the established business districts are candidates for conversion.

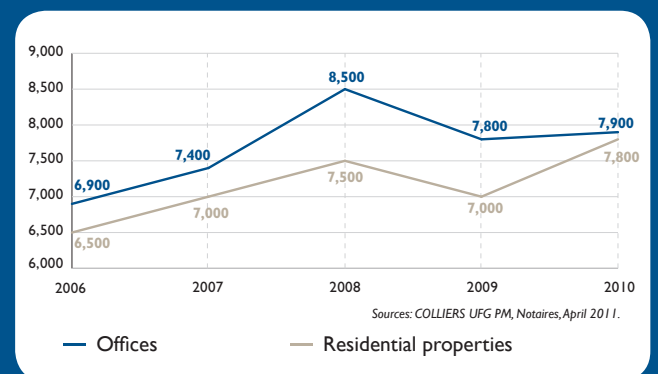
GRAPH 1 - CHANGE IN RENTAL PRICES IN WESTERN CENTRAL PARIS (per sq.m. per year)



Converting offices into residential property may also be envisaged as part of a strategy of selling them off separately. As shown in *graph 2*, prices of residential property located in central districts have recently caught up with those of office premises. If selling the marketability of office spaces can provide a significant source of value, a low cost of conversion and a high ultimate sale price are required for transactions of this type to be financially viable. Therefore, only buildings that are easy to convert and located in central districts meet these criteria. Furthermore, the residential surface area created must be less than 800 sq.m. in order to avoid having to include 25% of social housing, the price of which is frozen at a low level thereby undermining the financial result of the transaction. A hard equation to solve...

Changes of use therefore seem to affect only a narrow segment of the Greater Paris property market and are only a marginal solution to housing requirements. On the other hand, it seems more appropriate to work on modernising or converting existing office stock and reduce the number of abandoned office buildings in order to enable housing to be developed on the remaining land available.

GRAPH 2 - CHANGE IN SALE PRICES IN WESTERN CENTRAL PARIS (per sq.m. per year)

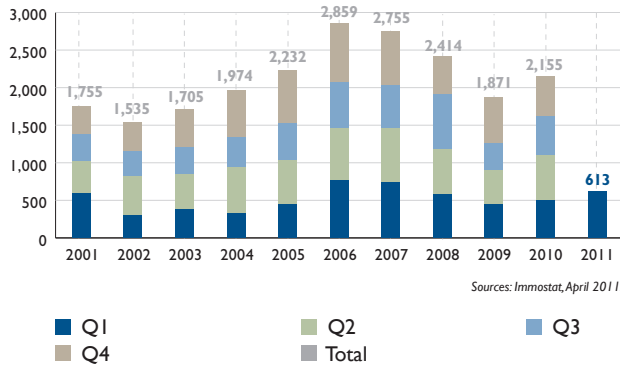


Greater Paris rental market

A dynamic market

→ Shifting demand

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



With 613,000 sq.m. sold in the course of the first three months of the year, occupier demand has increased by 20% compared with the same period in 2010. The Greater Paris market has thus confirmed its ability to recover, if we include all types of property. The drivers of property needs are, however, unchanged: the search for cost savings, grouping facilities together, modernisation... Thus, corporate moves do not lead to increased occupancy of building stock. In view of the economic outlook and the increase in salaried employment in 2010 (+ 0.7%),

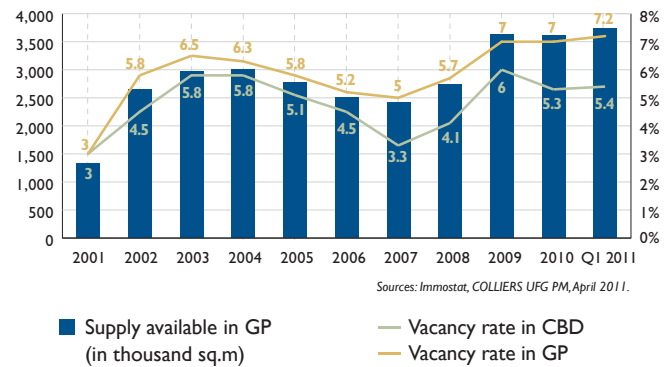
« The Greater Paris market has thus confirmed its ability to recover, if we include all types of property. »

Major users are continuing with their policy of rationalising premises and grouping facilities together in high-quality buildings. Business hubs in the suburbs have managed to attract some big industry names into new properties, such as Thalès with 82,800 sq.m. in Gennevilliers. While new developments are the most popular, AEF's recent signing of a lease for 14,500 sq.m. in Issy-les-Moulineaux shows that some users are interested in recent properties with very good infrastructure.

Up 25% in one year, the volume of business in the small-to-medium property segment remained high. Paris confirms its status as the driver of growth in the Greater Paris market, with 45% of regional demand for this property segment. The recovery that started in 2010 has gained strength in the business districts of the Western Crescent. On the other hand, the other markets of Paris's inner and outer rims are still seeing low volumes of business.

→ Significant stock outside Paris

OFFICE SPACE AVAILABLE IMMEDIATELY AND VACANCY RATE



Despite buoyant take-up, the available stock has continued to grow. At the end of March 2011, the supply of immediately available office space in Ile-de-France effectively stood at 3.7 million sq.m., up 3.5% compared with the end of 2010. Overall vacancy rates increased over the quarter, reaching 7.2%. While unsold new developments added to the stock in Q1 (+ 60,000 sq.m.), second-hand stock becoming vacant also weighed on the market (+ 75,000 sq.m.). The number of properties on offer in Paris CBD increased noticeably over 3 months (+ 3%), but the vacancy rate remained under control (5.4%). The quality of stock continues to deteriorate, however, with the proportion of new properties estimated at 15%. With only 39,500 sq.m. of properties under development available, this trend is likely to increase over the next few quarters. In other Paris markets, the vacancy rate is on the decline, ranging henceforth from 5.5% (South Paris) to 3.2% (North East Paris).

« Despite buoyant take-up, the available stock has continued to grow. »

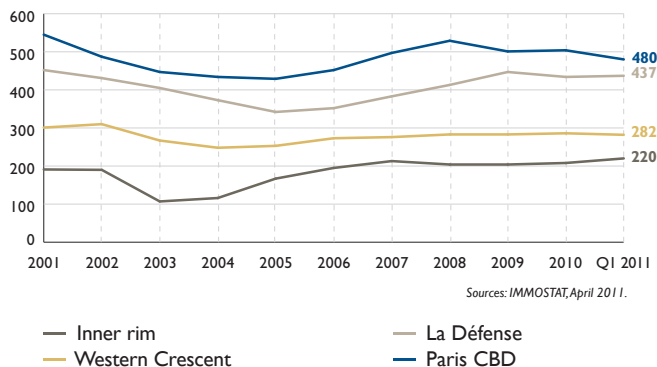
With a vacancy rate of 11.8%, there is an obvious oversupply in the Western Crescent market. Only the Neuilly and Levallois sub-markets have seen a reduction in property available (-11%). The lack of major deals and completion of First (41,000 sq.m. still for rent) have meant a 19% increase in stock available in La Défense, with the vacancy rate now standing at 7%. The number of properties available in the other markets of the inner rim has shrunk by 4% since the beginning of the year whereas a 3.5% increase was observed in the outer rim.

Greater Paris rental market

A dynamic market

→ The stabilisation of rental values is confirmed

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



The Greater Paris market has been in a phase of stabilising headline rents for the last few months. In view of the market's low turnover rate ⁽¹⁾ (60% in 2010 and 65% expected in 2011), values are unlikely to change significantly for several quarters. This trend does, however, mask certain disparities in terms of the quality of the products and the fundamentals of each sub-market.

Although headline rents for new properties remain stable, incentives are being gradually reduced in markets where supply is dwindling further, in particular the Paris CBD. In other markets, commercial benefits for large units still represent more than 1.5 months per year of lease and are maintaining headline rents at higher levels than effective rents. Changes in the rental values of second-hand premises differ greatly from one market to another. Paris CBD therefore saw a 5% drop, attribut-

able partly to a reduction in the quality of properties leased. In La Défense, a price adjustment is taking place as a result of the increase in available supply. Landlords are also carrying out significant refurbishment work before putting vacated premises back on the market. Average rental values in the Western Crescent have remained stable. However, users of medium and large properties have considerable scope to negotiate incentives.

« Incentives are being gradually reduced in markets where supply is dwindling further, in particular the Paris CBD. »

(1) Ratio of take-up in year n to the immediately available supply in year n-1.

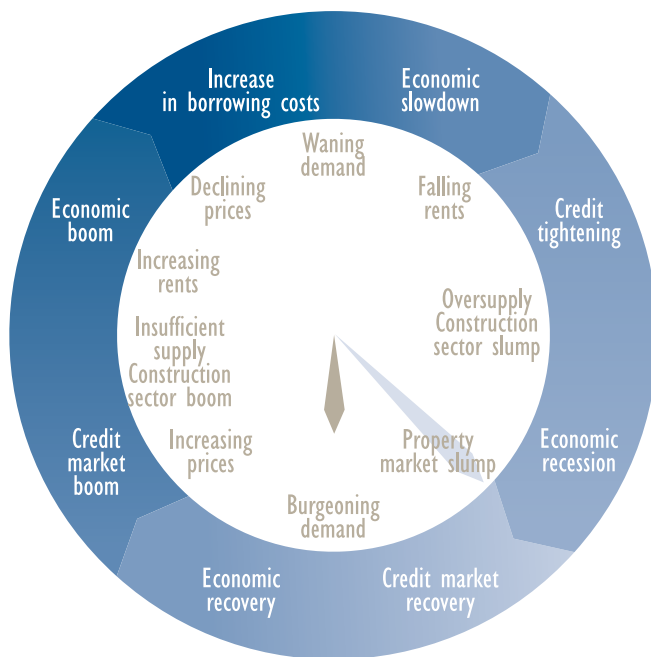


→ Main office property transactions in the Ile-de-France - Q1 2011

Address	Tenant	Surface area	Condition of premises
Carré 92 - Gennevilliers	THALES COMMUNICATION	82,800 sq.m	New HEQ buildings for completion in 2012
Cityzen - Bois-Colombes	COFACE	29,500 sq.m	New HEQ, THPE buildings for completion in 2013
Le Madone - Puteaux	HAVAS MEDIA	21,200 sq.m	Building converted in 2002 - Premises renovated
Carré Suffren - Paris 15 ^e	AON	15,000 sq.m	New building completed in 2009
8 rue de Londres - Paris 9 ^e	GOOGLE	10,300 sq.m	Building converted in 2003

→ The Colliers UFG PM Barometer

2ND TRIMESTER 2011



■ Economic cycle
■ Real estate cycle

→ Key figures

	Take-up 1 st trimester 2011	Offer available at the end of mars 2011	Vacancy rate	Under construction available supply	Prime rent
Paris CBD	95,000 sq.m	383 000 sq.m	5.4%	39,500 sq.m	€750 - 830 per sq.m
Southern Paris	48,500 sq.m	288 000 sq.m	5,5%	25,000 sq.m	€490 - 800 per sq.m
North Eastern Paris	57,000 sq.m	94 000 sq.m	3.2%	38,000 sq.m	€300 - 350 per sq.m
La Défense	14,500 sq.m	233 000 sq.m	7%	194,000 sq.m	€500 - 590 per sq.m
Western Crescent	234,000 sq.m	891 000 sq.m	11.8%	122,500 sq.m	€310 - 505 per sq.m
Inner Rim	45,500 sq.m	470 000 sq.m	8.2%	62,000 sq.m	€260 - 400 per sq.m
Outer Rim	88,000 sq.m	1 262 000 sq.m	6.7%	26,000 sq.m	€180 - 250 per sq.m

Sources: IMMOSTAT and COLLIERS UFG PM, April 2011.

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COLLIERS INTERNATIONAL

5 continents
61 countries
512 offices
12,500 professionals
Revenue (in millions euro): 1,142
73,972 transactions (in 2010)

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MARKET OVERVIEW

2nd trimestre 2011

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