



# RAC Quarterly Market Assessment (QMA) – Q2 2010

**EURO  
HYPO**

GRM-CR-ABF-RAC Research | July 2010

# Content

---

1. RAC Quarterly Market Assessment (QMA): Product Information Sheet	Page 2-3
2. Macro-Economic Conditions	Page 4-6
3. Office Market	Page 7-11
4. Retail Market	Page 12-15
5. Investment Market	Page 16-23

# Content

<b>1. RAC Quarterly Market Assessment (QMA): Product Information Sheet</b>	<b>Page 2-3</b>
2. Macro-Economic Conditions	Page 4-6
3. Office Market	Page 7-11
4. Retail Market	Page 12-15
5. Investment Market	Page 16-23

# RAC Quarterly Market Assessment (QMA): Product Information Sheet

---

## ■ Intention

- Comprehensive overview over current developments of commercial property markets (office, retail, investment), covering all relevant Eurohypo markets worldwide
- Real-time review of market conditions and early stage indication of short term developments already at the beginning of the quarter (publications of other market players' assessments sixth week after end-of-quarter at the earliest) → „to be ahead“

## ■ Approach

- Independent assessment based on in-house market expertise only
  - Quarterly standardised polling of RAC appraisers' opinion on the spot
    - Quarterly Market Survey (QMS): Focus on office and shopping centre markets, 3- and 12-months-outlook
    - Market Value Changes (MVC): Focus on investment markets, 12-months-review and prognosis for several real estate segments, scenario analysis
  - Anticipating Risk Assessment (ARA)/Economic Fundamentals: Early stage indication of risk potentials for CRE derived from macro-economic indicators
  - Latest economic forecast of Commerzbank Economic Research

## ■ Specifications

- Periodicity: Quarterly
- Language: English

# Content

---

---

1. RAC Quarterly Market Assessment (QMA): Product Information Sheet	Page 2-3
<b>2. Macro-Economic Conditions</b>	<b>Page 4-6</b>
3. Office Market	Page 7-11
4. Retail Market	Page 12-15
5. Investment Market	Page 16-23

## Economic Development – Real GDP Growth (in %)

### Economic Rebound Started to Diverge

	2009	2010f		2011f	
<b>Euro Area</b>	<b>-4.1</b>	1.2	↑	1.4	↑
<b>Germany</b>	<b>-4.9</b>	2.5	↑	1.8	↑
<b>France</b>	<b>-2.5</b>	1.3		1.5	
<b>Italy</b>	<b>-5.1</b>	0.7		1.3	
<b>Portugal</b>	<b>-2.7</b>	1.0	↑	0.6	↑
<b>Spain</b>	<b>-3.6</b>	<b>-0.3</b>		0.5	
<b>UK</b>	<b>-4.9</b>	1.1	↓	2.0	
<b>Poland</b>	1.7	3.5		4.4	↓
<b>Russia</b>	<b>-7.9</b>	5.0	↓	4.5	
<b>Turkey</b>	<b>-4.7</b>	6.0	↑	5.2	
<b>USA</b>	<b>-2.4</b>	3.3	↑	3.3	↑
<b>Japan</b>	<b>-5.2</b>	3.0	↑	1.5	

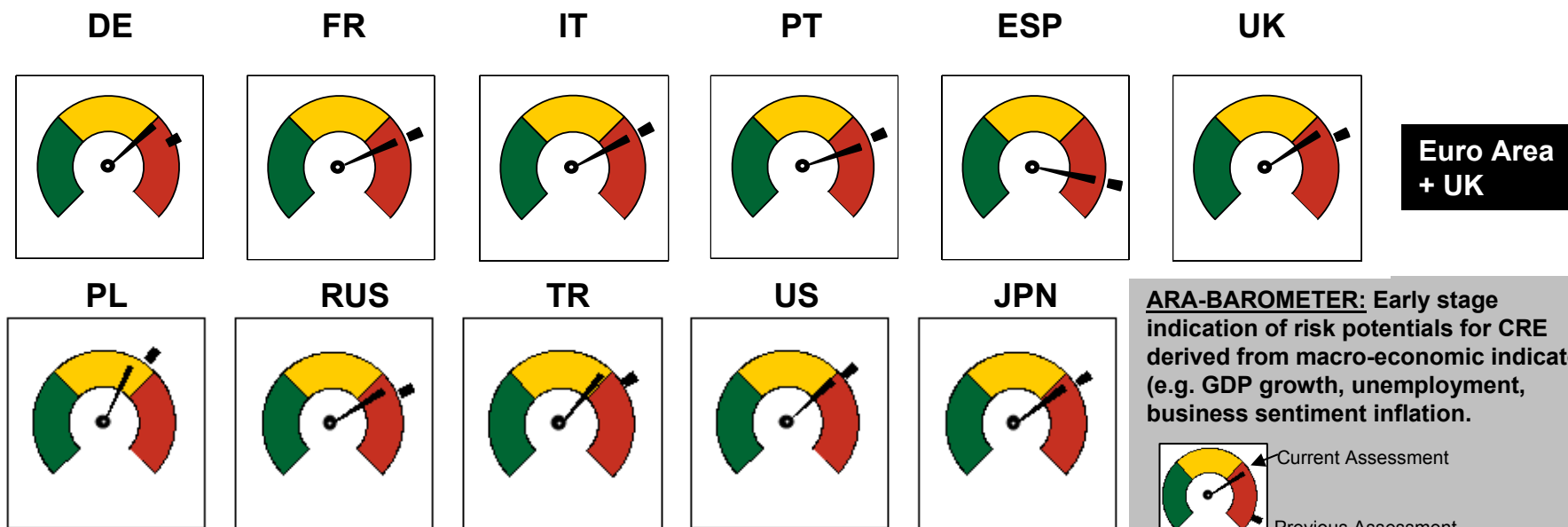
Compared to last QMA, the forecast was revised... upward ↑ downward ↓

- With the escalation of the sovereign debt crisis during Q2 2010, economic rebound started to diverge between countries which is clearly mirrored by the latest revision of the GDP forecasts:
- Euro Area: While fiscal consolidation is expected to drag growth prospective in economies with high budget deficits (particularly the Euro zone periphery and UK), growth of export-based Germany is the main driver for the general upward revision of the Euro area.
- Being one of the PIIGS-economies Spain is facing further contractions in 2010 yoy.
- CEE/Emerging Markets outside the Euro zone with strongest growth prospective.
- Other industrialized economies, which benefit from the worldwide recovery, are the US and Japan (both also with clear upward revised forecasts).
- However, as economic growth even in these countries is only modest compared to the drastic cuts of the recession, fundamentals of the related real estate markets hardly improve in the months to come (see next page).

Source: Commerzbank

# Economic Fundamentals of Commercial Real Estate Markets (CRE)

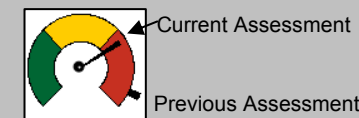
## Only Slight Improvements over Recent Months



- Reflected by the persistence of most markets in the red zone of the barometer, economic fundamentals of the real estate sector remain subdued for the months to come.
- The riskiest environment by far is found in Spain (long period of recession, renewed rising unemployment to 20%); contrarily, outer-Euro Area markets Poland and Turkey backed by strong GDP growth rates dipped already in the yellow zone.
- Due to the weak and fragile recovery process, only slight improvements could be recorded since last assessment. Strongest rebound during Q2 2010 could be proofed in Germany and Turkey, Portugal showed renewed deteriorating conditions.

Source: Eurohypo GRM-CR-ABF-RAC

**ARA-BAROMETER:** Early stage indication of risk potentials for CRE derived from macro-economic indicators (e.g. GDP growth, unemployment, business sentiment inflation).



**Green:** Market fundamentals perform clearly above long-term average implicating positive impact on the real estate market for the upcoming months.

**Yellow:** Market fundamentals perform within the scope of usual cyclical changes implicating non-critical impact on the real estate market.

**Red:** Market fundamentals perform clearly below long-term average implicating negative development with high risk potential for the real estate market.

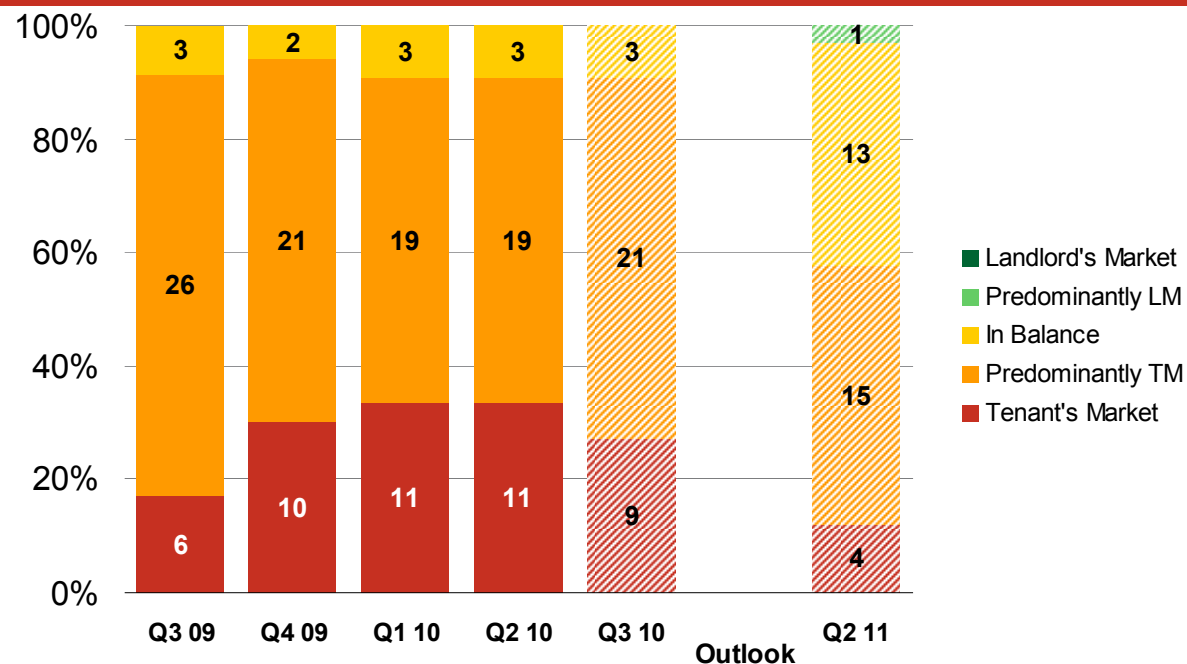
# Content

---

1. RAC Quarterly Market Assessment (QMA): Product Information Sheet	Page 2-3
2. Macro-Economic Conditions	Page 4-10
<b>3. Office Market</b>	<b>Page 11-15</b>
4. Retail Market	Page 16-19
5. Investment Market	Page 20-27

## Office Market Conditions of Eurohypo Markets

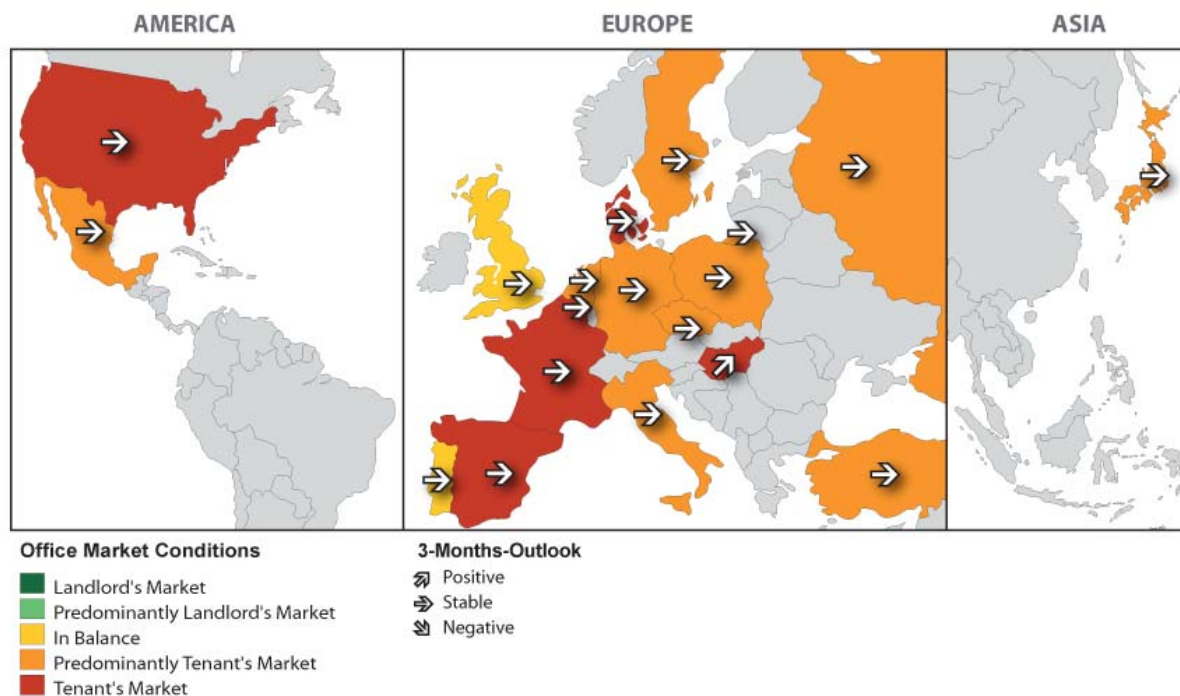
### Office Markets in the Middle of a Long-Lasting Consolidation Period



- Compared to last QMA, the overall picture of a long-lasting consolidation period persists: It is also expected to continue beyond year-shift 2010.
- Still 90% of all office markets are classified as tenant's markets and almost two-thirds are supposed to do so in 12 months.
- Progressively rising letting activity still derives from relocation and extension of existing lease agreements that quite often goes hand in hand with office space reductions. The lack of additional demand in most monitored markets results in negative net-absorption, rising vacancies and a broad-based reduction in rents which, however, lost slightly pace.
- With release from drying-up development pipelines, market corrections in the prime segment increasingly bottom out. However, due to occupier's prevailing negotiating-power incentives still play an import roll and longer re-letting periods point to a difficult market environment.

Source: Eurohypo GRM-CR-ABF-RAC

## Office Market Conditions and 3-Months-Outlook by Countries Consolidation Should Broaden

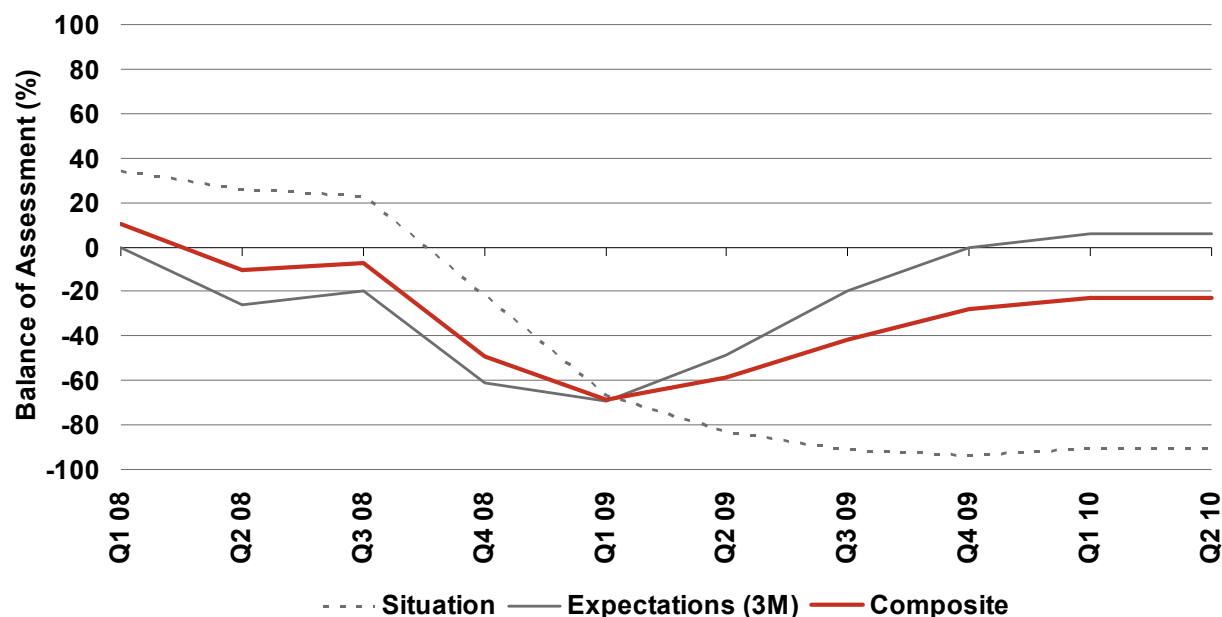


- Already indicated by the last two assessments, Hungary finally became a distinct tenant's market (red category) during Q2 2010 due to rising supply (completion of the last projects started before the crisis). Thus, vacancies are about to peak. A slow decrease should follow due to a supply pipeline drying out. Further constraints derive from the escalation of Hungary's political and financial crisis (e.g. government interrupted negotiations with IMF about further support, depreciation of Forint).
- Against the impending risks from devastating economic conditions, Spain's positive short-term outlook in Q1 has been offset.
- Predominantly based on London's prime submarket West-End – and also City to an increasing extent - UK is the precursor in the current letting cycle showing balanced market conditions. Active demand has increased as companies believe rents are unlikely to reduce further. Additionally, a severe shortage of new prime stock is likely to create landlord's market conditions from early 2011 onwards.

Source: Eurohypo GRM-CR-ABF-RAC

## RAC Sentiment Index – Office Letting Markets

### Sluggish Prospects Mirrored by Still Negative SI



#### Components of RAC Sentiment Index

**Situation Component:** reflects current situation on monitored markets (positive result: markets with favourable conditions of a landlord's market prevail; negative result: markets with unfavourable conditions of a tenant's market prevail)

**Expectation Component:** reflects expected evolution of monitored markets within the next three months (positive result: number of markets with improving conditions - compared to current status - prevail; negative result: number of markets with worsening conditions prevail)

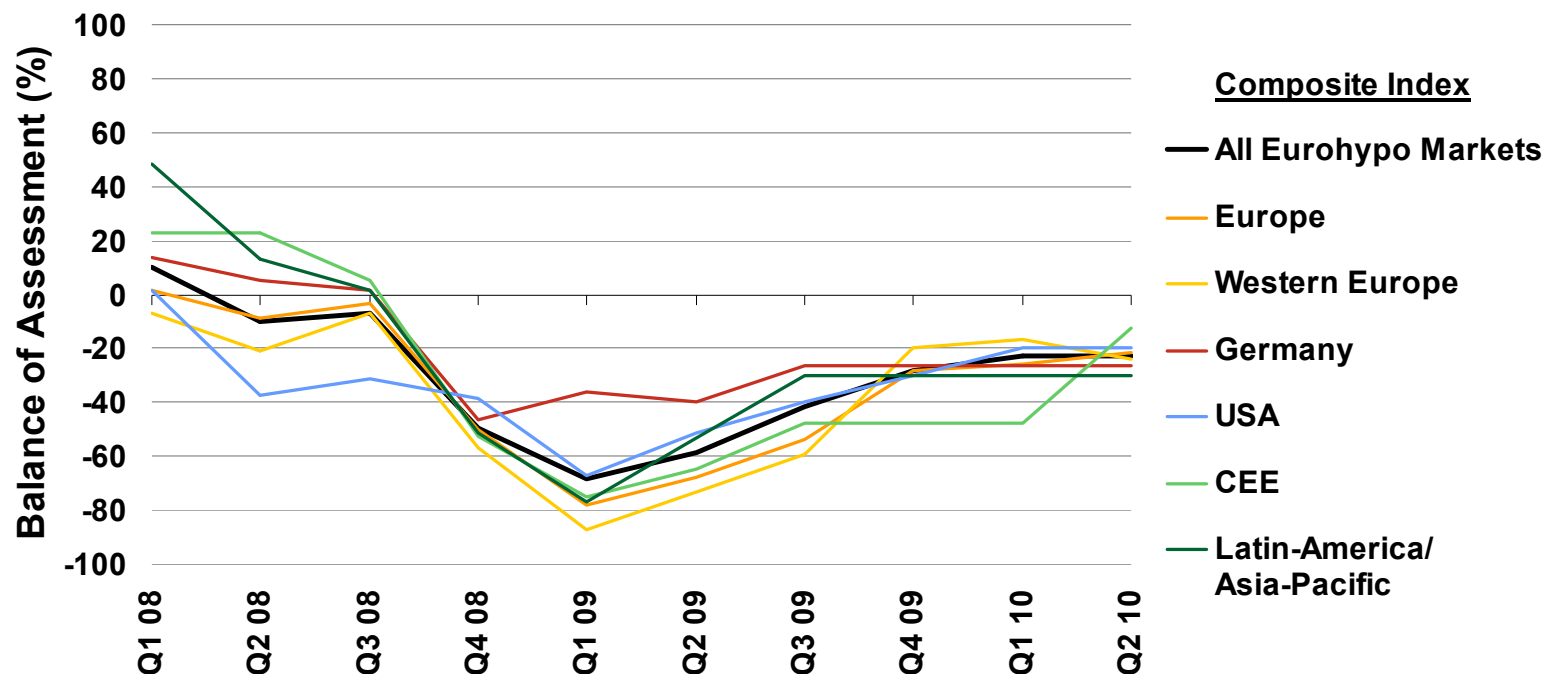
**Composite Index:** Weighted Average of Situation Component (30%) and Expectation Component (70%)

- During the last period under review, our early bird indicator, the RAC SI, stayed firm reflecting that a clear trend reversal to the better on Eurohypo's office letting markets is still far away.
- The situation component pauses near the lowest possible level and, thus, keeps the composite index clearly in negative terrain reflecting that the environment for office real estate markets is still devastating.
- A ray of hope comes from the expectation component mirroring a slightly positive sentiment for the second consecutive quarter.

Source: Eurohypo GRM-CR-ABF-RAC

## RAC Sentiment Index by Country Groups

### CEE Markets Slightly Ahead



- As in Q1 2010, the synchronised sideward trading in clearly negative terrain points out that the conditions are homogenously unfavourable across all country groups.
- Monitored CEE markets are regarded with more optimism than one quarter ago. This sub-index is now slightly ahead to those of other country-groups, which corresponds with comparatively favourable macroeconomic fundamentals.

Source: Eurohypo GRM-CR-ABF-RAC

## Content

---

1. RAC Quarterly Market Assessment (QMA): Product Information Sheet	Page 2-3
2. Macro-Economic Conditions	Page 4-6
3. Office Market	Page 7-11
<b>4. Retail Market</b>	<b>Page 12-15</b>
5. Investment Market	Page 16-23

## Market Fundamentals of the Retail Sector Despite Some Improvement Outlook Remained Retained

### Current Market Conditions ◀

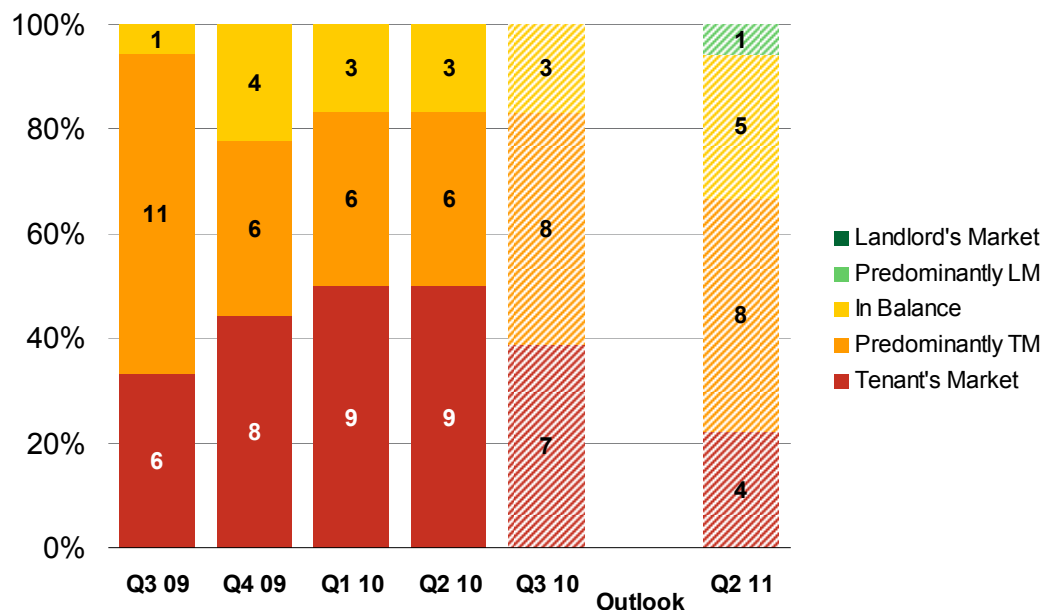
### ▶ 12-Months-Outlook



- Ongoing recovery, consolidation of labor markets, low inflation and numerous governmental stimuli were the supportive factors behind a rising number of countries with a stagnating or even slightly expanding retail sector over recent months.
- However, the 12-months-outlook point to a temporary standstill of the fragile consolidation trend as fading governmental measures and fiscal consolidation drag consumer confidence.
- As a result, only one market is supposed to show a clear positive trend.

Assessment of current market conditions based on retail sales (in general as volume, seasonally adjusted), outlook based on consumer & retailer confidence.  
Source: Datastream, Eurohypo GRM-CR-ABF-RAC

## Shopping Centre Market Conditions of Eurohypo Markets Downswing Bottomed Out in Q2 2010

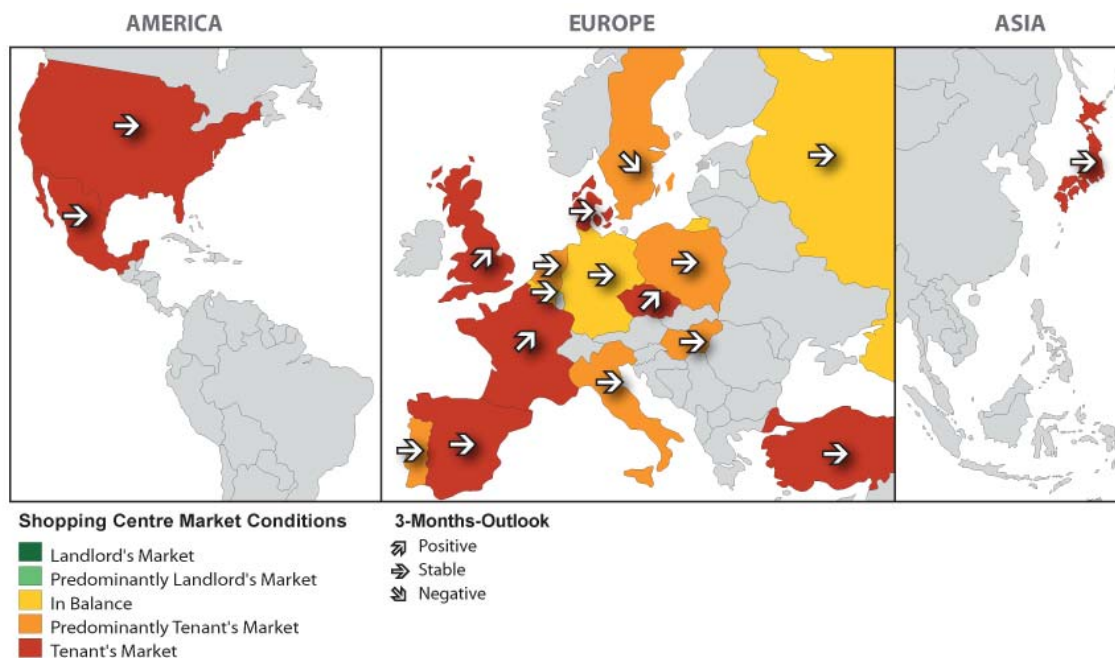


- As for the second consecutive quarter more than 80% of all monitored shopping centre markets are showing characteristics of a tenant's market the downswing can hardly go any deeper.
- Shopping centre are – to diverging degrees and depending on market, location and property quality – affected by rising vacancies and rents under downward pressure.
- Retailers are still seeking prime locations, but act increasingly selective and benefit from their strong negotiating position.
- Relief comes from the supply side as limited credit availability and renewed uncertainty regarding a sustainable economic recovery results in further delays for new developments.
- For the next 12 months a moderate trend reversal is expected.

Source: Eurohypo GRM-CR-ABF-RAC

## Shopping Centre Market Conditions and 3-Months-Outlook by Countries

### Shopping Centre Market in Germany and Russia Firm throughout the Crisis



- Remaining or increasing constraints for private consumption across all monitored markets results in an almost unchanged assessment for most countries compared to last QMA.
- DE: since many years retail sales proved to be unaffected by cyclical movements – booms as well as troughs; no backslide expected for the months to come; prime properties are almost fully let, so that rent increases can be expected in the short- to medium term
- RU remains an interesting place for retailers and investors. Continued wage growth, which persists throughout the crises, and a strongly rebounding recovery set up market potentials.

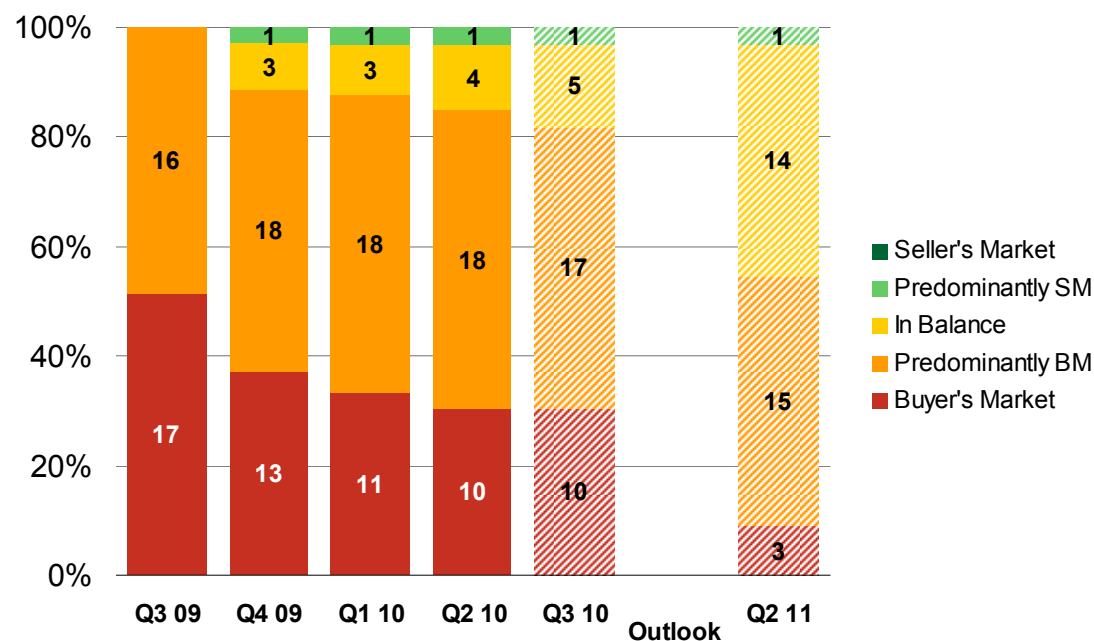
Source: Eurohypo GRM-CR-ABF-RAC

## Content

---

1. RAC Quarterly Market Assessment (QMA): Product Information Sheet	Page 2-3
2. Macro-Economic Conditions	Page 4-6
3. Office Market	Page 7-11
4. Retail Market	Page 12-15
<b>5. Investment Market</b>	<b>Page 16-23</b>

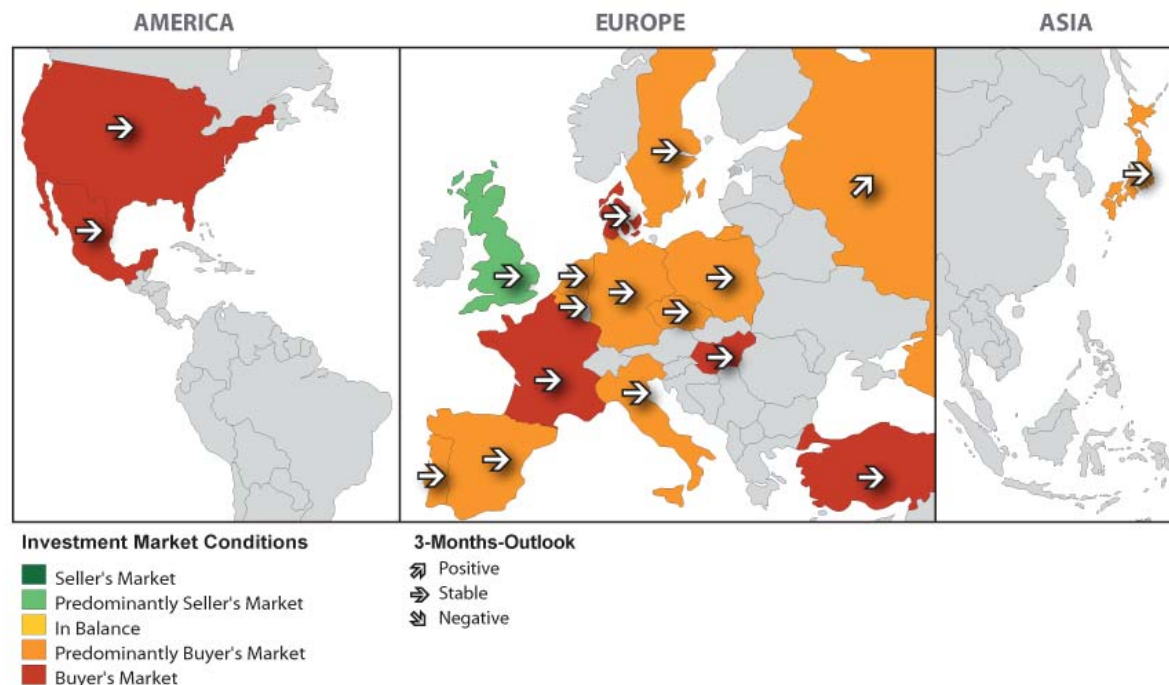
## Investment Market Conditions of Eurohypo Markets Consolidation Phase on the Extension



- Although transaction activity continues to rise, investment volumes are still far below long-term average as investor's interest is still focused on prime-properties in solvent markets.
- Against the backdrop of ongoing uncertainty on the financial markets (sovereign debt crisis, default risks of CMBS etc.) limited credit availability remains another burden.
- Little more dynamic lies in the 12-months-outlook as the number of balanced markets is expected to triple and further more distinct buyer's markets vanish. However, as long as significant stimuli from the letting market stay away, even in the middle of 2011 more than half of all monitored markets will show characteristics of a buyer's market. This foreshadows a distinct consolidation rather than a clear upswing.

Source: Eurohypo GRM-CR-ABF-RAC

## Investment Market Conditions and 3-Months-Outlook by Country London's Investment Market Plateaued for the Time Being

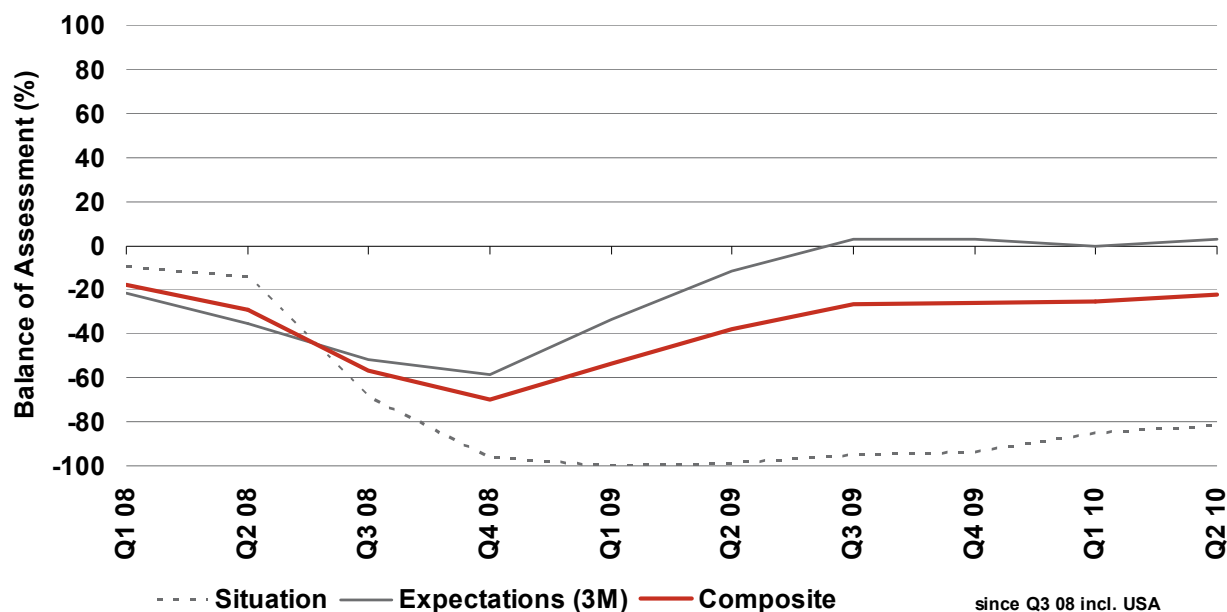


- London, particularly its submarkets West-End and City, are still facing strong investor's interest. Although a lack of eligible products has already been noticed, prices are not expected to increase further as they are now being assessed against the impending risk of a double dip in the UK economy and the improvements of other markets. As a result non-domestic investors reduced their activity on the London market while UK institutional investors and property companies returned.
- Russia is the only market with a positive 3-Months-Outlook.
- Japan left the "red category" (=distinct buyer's market).

Source: Eurohypo GRM-CR-ABF-RAC

## RAC Sentiment Index – Investment Markets

### Expectations Remain Indifferent



#### Components of RAC Sentiment Index

**Situation Component:** reflects current situation on monitored markets (positive result: markets with favourable conditions of a seller's market prevail; negative result: markets with unfavourable conditions of a buyer's market prevail)

**Expectation Component:** reflects expected evolution of monitored markets within the next three months (positive result: number of markets with improving conditions - compared to current status - prevail; negative result: number of markets with worsening conditions prevail)

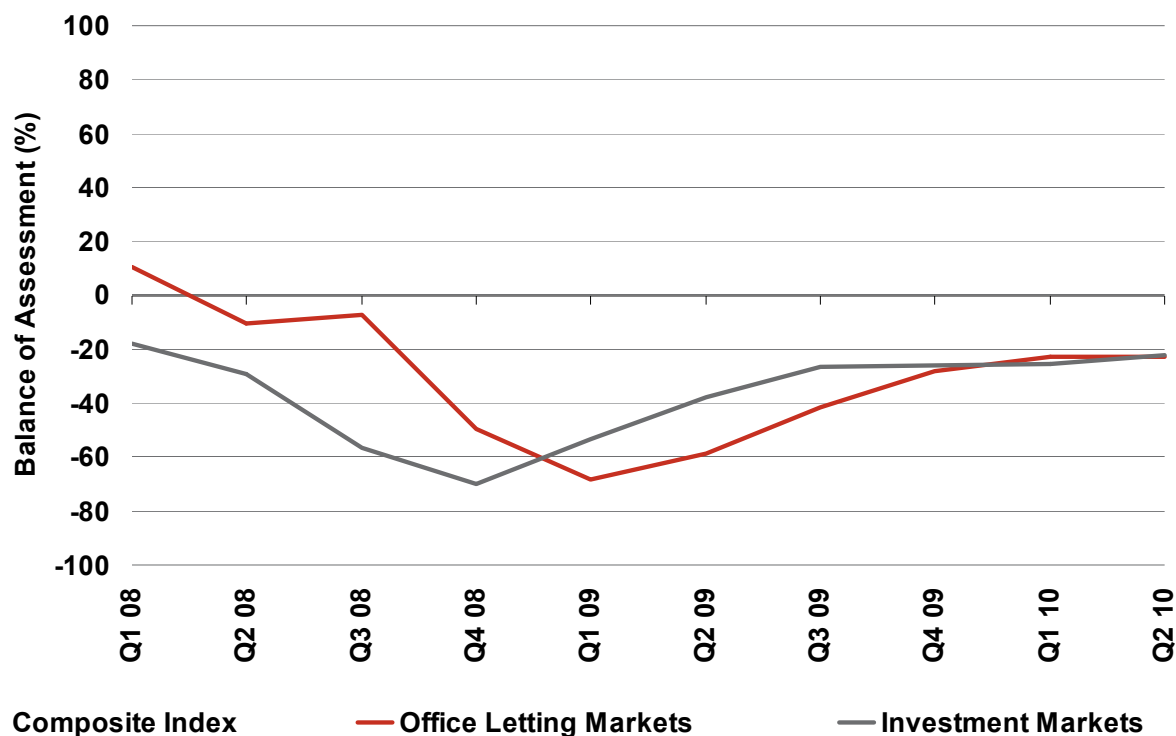
**Composite Index:** Weighted Average of Situation Component (30%) and Expectation Component (70%)

- Upcoming hope for strengthening investment markets derived by a slightly risen situation component in Q1 2010 has been disappointed by a sideward movement in Q2 2010.
- In the absence of a self-sustaining recovery both on letting markets and the capital market the expectation component remains close to the nil-line. This indicates that market sentiment regarding the short term development is still indifferent.
- Despite investment activity increases overall market conditions are not expected to improve significantly.

Source: Eurohypo GRM-CR-ABF-RAC

## RAC Sentiment Index – Office Letting Markets vs Investment Markets

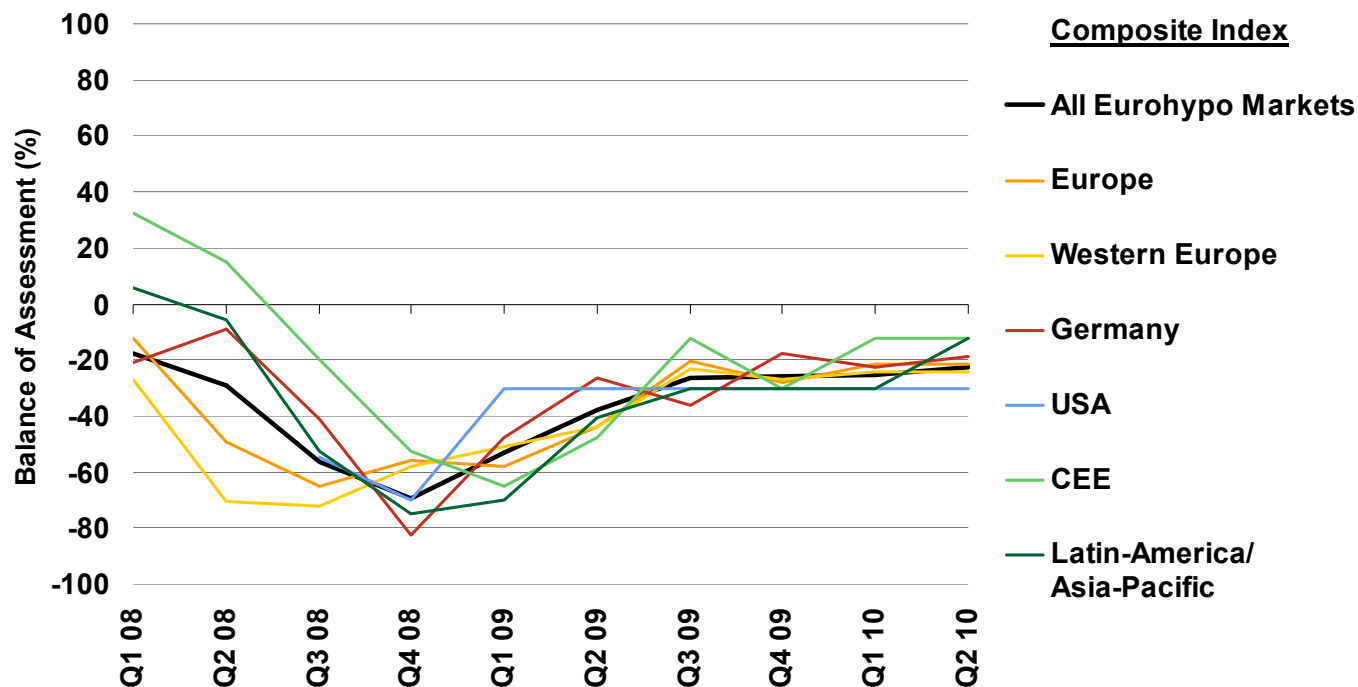
### Missing Stimuli from Letting Markets Continuously Drag Investment Markets



- Missing broad-based stimuli from the letting market and an unsteady economic recovery constrain investment markets for the second consecutive quarter.

Source: Eurohypo GRM-CR-ABF-RAC

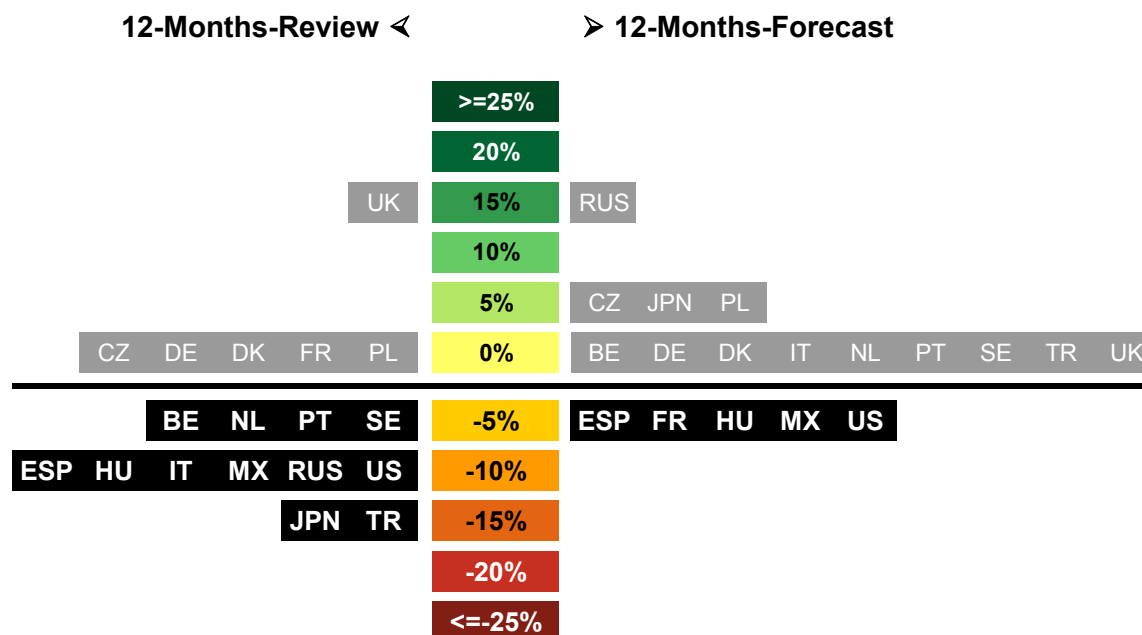
## RAC Sentiment Index – Investment Markets by Country Groups As For Letting Markets Diversified Developments Hard to Spot



- With sub-indices trading synchronously sideward in still negative terrain, diversification potential between monitored country groups are still hard to spot.
- As already pointed out by last QMA, slightly better performing indices of Eastern European markets and catching up Emerging Markets currently offer the most interesting perspectives due to more favourable underlying fundamentals.

Source: Eurohypo GRM-CR-ABF-RAC

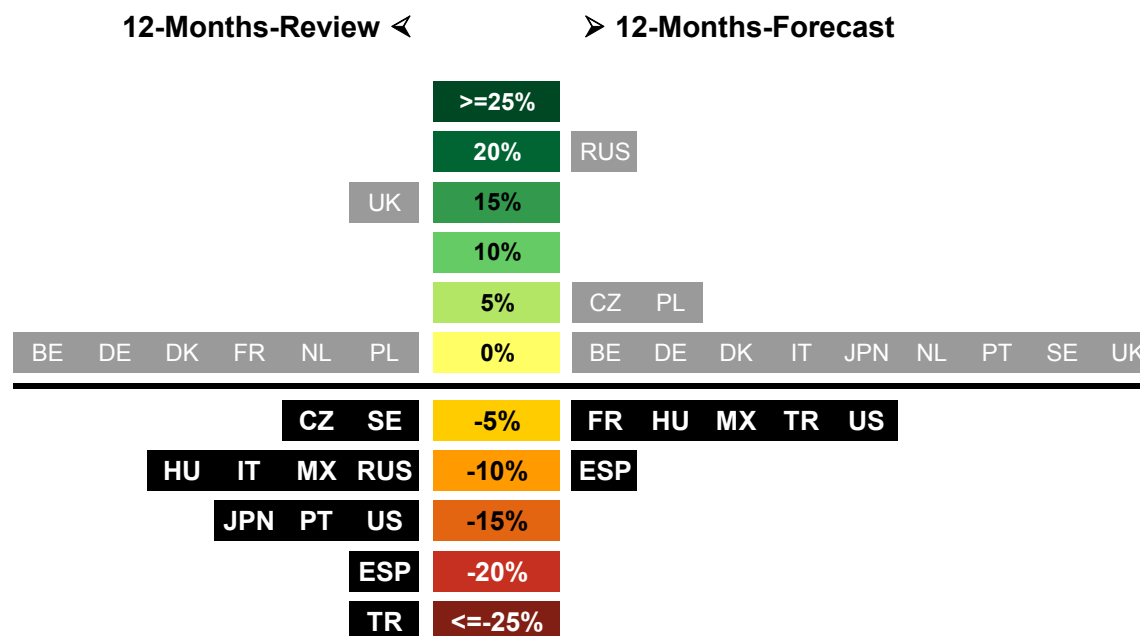
## Market Value Changes – Office Fading Corrections for an Increasing Number of Markets



- Corrections of market values are fading for an increasing number of markets.
- The 12-months-review now shows one third of all monitored markets with firm market values. Many markets recording value losses over the entire year could at least diminish depreciation during last period under review.
- Only one third of all monitored markets are expected to face slight value reductions over the next 12 months. With a fragile economic recovery and, thus, sluggish demand for commercial real estate markets, value gains will basically not exceed 5%.
- Against the background of drastic depreciations in the past, Russia might now see the heaviest trend reversal. UK office properties, in contrast, left their yield-driven growth path as many investors anticipate impending risks from the economic environment and assess the market as comparatively expansive with regard to market value development in other countries e.g. Germany.

Source: Eurohypo GRM-CR-ABF-RAC

## Market Value Changes – Retail Price Corrections Still More Diverse Than for Offices



- Contrary to office properties the market values of retail properties rebounded not so strongly since last QMA. Some markets were facing even higher value losses over the last 12 months. As a result, spreads of realised value changes between the markets were still considerably higher than for offices.
- This effect is expected to deteriorate during the next 12 months as half of all monitored markets will show consolidating market values. The ratio of markets with remarkably declining value losses will go down to 20% - the same figure as for office markets

Source: Eurohypo GRM-CR-ABF-RAC

## Disclaimer

---

The information contained herein was prepared by Eurohypo which does not undertake to influence your opinion on the information contained herein. It is furnished for your information only. It is not an offer to buy, sell or hold any securities. Though the figures are generated carefully, no representation or warranty, expressed or implied, is made as to and no reliance should be placed on the accuracy, completeness or correctness of any information contained herein. Eurohypo shall not have any liability whatsoever for any loss howsoever arising from, related to or in connection with any use of any of the information contained herein.

The investments discussed or recommended in any of these presentations may not be suitable for all investors. Investors must make their own investment decisions based on their specific investment objectives and financial position and using such independent advisers as they believe necessary. Be aware of the date of presentation and possible amendment thereafter. The information might not be amended or updated. Third persons may receive other or updated information, before it is made available to the use of this service.

This presentation may be restricted by law in certain jurisdictions. Persons into whose possession this presentation comes are required to inform themselves about and observe any such restrictions. The information contained herein may not be used by any person in any such jurisdiction in which it is restricted by law.

These materials are not an offer for sale of securities in the United States. The securities have not been registered under the U.S. Securities Act of 1933, as amended (the "Securities Act") and may not be sold in the United States absent registration or an exemption from registration under the Securities Act.

## **Christoph Kettel**

**Head of Real Estate Appraisal & Consulting  
GRM-CR-ABF-RAC**

Phone +49 (0)69 / 2548-2 15 36

Fax +49 (0)69 / 2548-8 15 36

E-mail [christoph.kettel@eurohypo.com](mailto:christoph.kettel@eurohypo.com)

**EUROHYPO AG  
Helfmann-Park 5  
65760 Eschborn  
Germany**

[www.eurohypo.com](http://www.eurohypo.com)

**EURO  
HYPO**