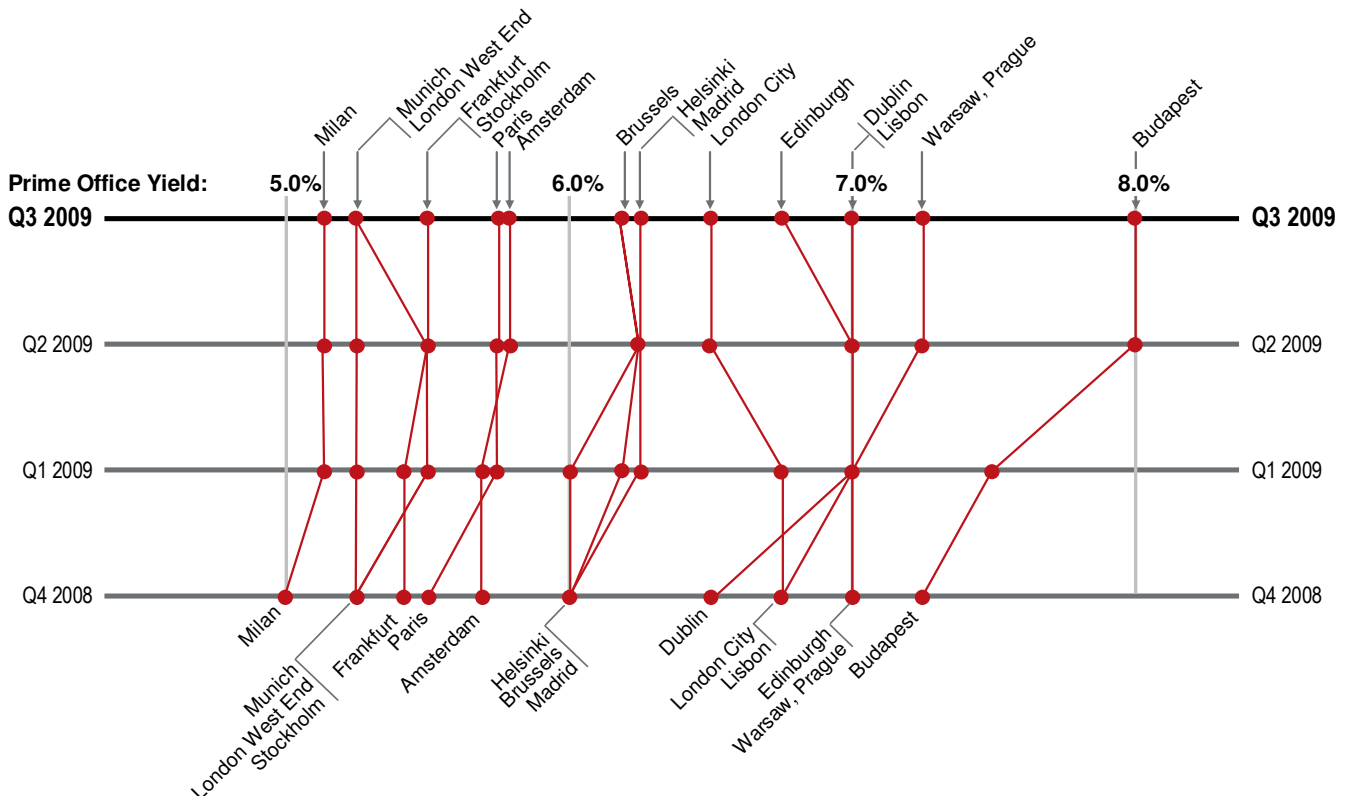


Prime Office Yields at Point of Inflection

Prime European Office Yield Movement Q4 2008–Q3 2009 (Selected Markets)



Source: Jones Lang LaSalle 2009

Notes: Jones Lang LaSalle's prime yield represents the best (i.e. lowest) "rack-rented" yield estimated to be achievable for a notional office property of the highest quality and specification in the best location in a market, as at the survey date. The property should be let at the prevailing market rent to a first class tenant with an occupational lease that is standard for the local market. The prime initial net yield is quoted, i.e., the initial net income at the date of purchase, expressed as a percentage of the total purchase price, which includes acquisition costs and transfer taxes.

Prime office yields continue to stabilise as we approach the bottom of the investment cycle and in some locations prime yields have begun what will be a slow and bumpy journey back towards long term averages. Jones Lang LaSalle's European aggregate yield moved in by just 5bps. The majority of this was accounted for by Western Europe, with the blended Central and Eastern European yield remaining flat.

The vast majority of European markets saw yields remain stable on the quarter or move in marginally. Out of the 46 markets we track, only three markets recorded yield decompression, these were Eindhoven and Bucharest, which moved out 25bps, and Utrecht which moved out 20bps. A total of 10 markets showed prime yields moving in over the quarter, between 50bps in Leeds and 5bps in

Brussels, Gothenburg and Malmö. These 10 markets are joined by London City, where yields corrected in by 25bps in Q2, as the only markets which have shown yield compression in this cycle.

Despite a continued trend of stabilising yields (24 markets have seen stable or compressing yields over the last two quarters) prime office yields remain above their levels at this time last year in all 47 markets and well above their peak levels in 2007. London West End, for example, despite moving in 25bps over the quarter remains 25bps above its level a year ago and 175bps above its peak level. Several markets remain significantly above their Q3 2007 levels including Moscow (+400bps), Bucharest (+275bps), Prague and Warsaw (+125bps), Stockholm, Paris and Helsinki (+75bps).

Even though yields have stabilised across Europe they have done so at differing levels from their peak. Compare London West End with Milan, for example, Milan has seen stable yields for the past three quarters and is now just 102 basis points above its peak. Given that in some markets yields are moving back in we may see some balancing of overall yield movement, i.e. those markets where yields moved out the most will also see yields move in the most—although we do not expect yields to move close to peak levels for some time.

This stabilisation signals prime yield ceilings for the majority of markets, with limited outward movement to come in a small number of markets. Despite prime yields reaching their ceilings, yields in secondary markets continue to move out as investor appetite remains focussed on low risk, income producing assets.

Within this low risk space investors have demonstrated a willingness to transact, to enter competitive bidding processes and to drive new pricing levels. Although London is in the front line of investor interest, Paris is not far behind and the impact of investor demand on yields is inevitably moving across Europe as a lack of suitable opportunities and keener pricing encourage investors to look at new locations. Although this scenario of 'seeking yield' may sound familiar what we are seeing is more of 'seeking opportunities'.

These opportunities need to sit well within the prime investment space as buyers continue to remain focussed on core income producing assets. We are yet to see any signs of significant activity in the value added space, even in those markets which are ahead of the curve and new development activity is unlikely over the medium term.

Although new lending remains scarce for some investors, others have proven that it is possible to secure new financing for prime investments. Many investors are pure equity players or are able to purchase with equity and finance later—this remains an attractive prospect for vendors who are now attracting multiple bids.

The focus on a narrow band of prime has demonstrated that a market driven largely by equity does have the ability to move prime pricing levels in spite of the malaise in the banking sector. However, investment volumes will remain well off peak levels until new financing is more widely available and investors are willing to take on more real estate specific risk. Another constraint on investment activity will be the availability of prime product as vendors sense an improving market and hold out for a better deal or come under less pressure to release assets. Finally as yields move in, in some locations, the attractiveness of un-gearred returns may diminish and it is unknown whether investors playing in the prime segment today have the appetite for riskier real estate investment.

Capital values still remain well below peak levels and will stay below them for some time to come. So far in this cycle occupier markets

have been lagging investment markets and as prime yields begin to stabilise prime rents continue to decline. Falling rents will further erode capital values in many markets and provide a drag on capital value recovery where yields are moving in; increasingly this will make the case for investing in properties with long leases and strong covenants.

Prime Office Yield Change

	BP change Q-o-Q (Q2 2009–Q3 2009)	BP change Y-o-Y (Q3 2008–Q3 2009)
Europe	-4 ↓	68 ↑
Western Europe	-5 ↓	47 ↑
Central and Eastern Europe*	- ↔	294 ↑
Amsterdam	- ↔	40 ↑
Athens	- ↔	150 ↑
Barcelona	- ↔	50 ↑
Berlin	- ↔	25 ↑
Brussels	-5 ↓	35 ↑
Bucharest	25 ↑	275 ↑
Budapest	- ↔	175 ↑
Dublin	- ↔	150 ↑
Düsseldorf	- ↔	25 ↑
Edinburgh	-25 ↓	50 ↑
Frankfurt/M	- ↔	40 ↑
Hamburg	- ↔	35 ↑
Helsinki	- ↔	75 ↑
Lisbon	- ↔	25 ↑
London City	- ↔	25 ↑
London West End	-25 ↓	25 ↑
Luxembourg	- ↔	50 ↑
Lyon	-30 ↓	35 ↑
Madrid	- ↔	50 ↑
Milan	- ↔	30 ↑
Moscow	- ↔	400 ↑
Munich	- ↔	40 ↑
Oslo	-25 ↓	25 ↑
Paris	- ↔	75 ↑
Prague	- ↔	125 ↑
Rome	- ↔	25 ↑
Rotterdam	- ↔	45 ↑
St. Petersburg	- ↔	450 ↑
Stockholm	- ↔	75 ↑
Warsaw	- ↔	125 ↑

Jones Lang LaSalle surveys prime yields in 46 office markets across Europe. The 30 markets listed above represent a selection from that list.

* Central and Eastern European Index includes: Prague, Warsaw, Budapest and Moscow

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