Italian Quarterly MarketView

Q4 2011

Quick Stats Milan

	Change from Q4 10	Change from Q3 11
Prime Rents	→	→
Prime Yields	↓	→

Quick Stats Rome

	Change from Q4 10	Change from Q3 11
Prime Rents	→	→
Prime Yields	↗	→

Country Topics

- The dramatic worsening of the sovereign debt crisis in Europe has necessitated a further (the third) correction of the public accounts for the years 2012-14, with a new manoeuvre approved in December by the new Parliament with the aim of achieving a balanced budget in 2013.
- While uncertainty about growth prospects for Italy - and Europe in general – remains high, the new government marked a decisive change in the image of Italy, recognised at a European and international level. The fiscal tightening manoeuvres and the liberalisations' plans should be now followed by policies to encourage economic growth.

Market Topics

- Record take up, but the availability of new and/or high quality offices has decreased: vacancy rate has exceeded 10% in Milan, completions are down 66% compared to 2010.
- Investments have declined, domestic investors, both institutional and private, have been the major players.
- The lack of financing is rendering certain types of asset classes illiquid.

OVERVIEW

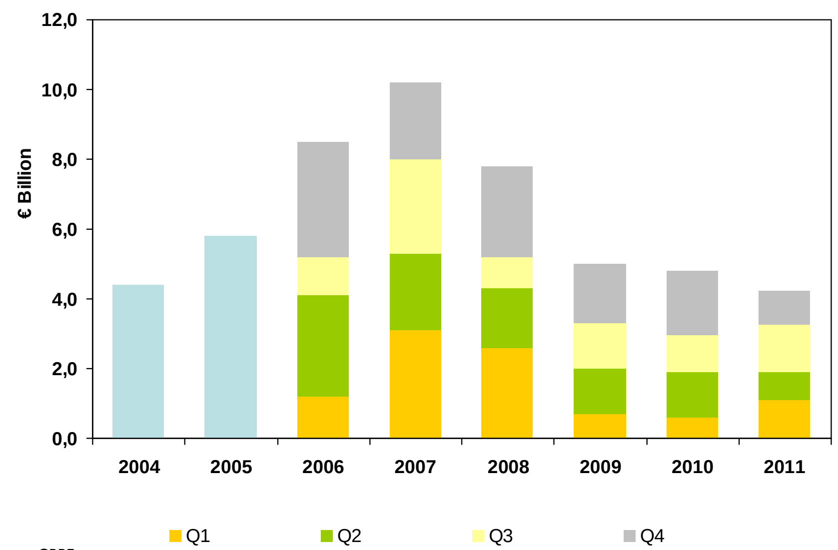
- **Tenants still lead the occupier market, fundamentals are sound**
  Office take up in Milan and Rome in 2011 grew by 23% and 54% compared to 2010, with volumes amounting respectively to 336,200 sqm and 199,760 sqm. In Milan, Q4 take up increased from the previous quarter, recording two pre let transactions and some medium to large units transactions. Grade A space supply has started to decrease and demand has remained unchanged from the last quarter. Despite this, the yearly net absorption is negative and reached -56,000 sqm.

- **Continued growth of available space in Milan, Rome is stable**
  The vacancy rate rose for the fourth consecutive quarter in Milan, standing at 10.3%, and remained stable in Rome. In Q4, Milan central and semi-central areas recorded the largest increases in vacancy due to the releasing of existing space, equal to +12% and +29% respectively, compared to previous quarter. In Rome, availability is expected to grow only slightly in the coming months as the potential future rationalisation of public spaces will have an effect on the real market only in the long term.

- **Prime rents in the CBD are stable, but the use of incentive is increasingly common**
  Prime rents in Milan CBD remained stable at 520 €/sqm/yr, while the average rent decreased by 25% in the last quarter compared to previous one, standing at 221 €/sqm/yr. The market is still strong tenant's favorable and the use of incentives today is increasingly common. The quality is confirmed as the main driver of demand.

- **Worsen the financial conditions, and capital flows in the real estate are slowing**
  In Q4 2011, € 990 million was invested in Italian real estate, a decrease of 26% over the previous quarter. The result for the whole of 2011 stood at € 4.3 bn, a decrease of 12% compared to 2010. The retail sector was confirmed as the main driver of investment with 55% of the total volume. More generally, high street and offices together accounted for 58% of the total volume, confirming the dominance of risk-averse investors who continue to target core assets with a low risk profile: prime gross yield for both assets were unchanged in the quarter at 5.25%, but the outlook is weakening.

Real estate investment evolution in Italy



Source: CBRE

CBRE

MILAN OFFICE MARKET

Take up 18% higher than the annual average of the last 5 years

In the last quarter of 2011, office take up in Milan equalled 108,600 sqm, more than double that of Q3 2011. Take up of the entire 2011 year stood at 336,200 sqm, an increase of 23% compared to 2010. During the quarter, transactions were made by companies actively seeking a new headquarters for its offices for over a year, always to meet the needs of consolidation and rationalisation. In particular, almost 50% of the total take up in Q4 was determined by four large transactions. Two of these were offices completed in late 2009 and early 2010, empty for over a year, one involved a newly completed building and the last one was a pre-let transaction of over 20,000 sqm in the Milanofiori area, which must be built (2014). The search for lower rents has driven the quarter's take up, with 20 transactions out of the total 34 made in the peripheral areas, approximately 50% in terms of sqm. During the quarter, the central and semi-central areas have each shown an absorption rate of 8% of the total, corresponding to four transactions per area. This has changed the composition of the annual take up by area to favour the peripheral zones, compared to the first half of 2011, in which the central areas were dominant. In fact, annual take up in terms of sqm equalled 34% in the periphery and 20% in the centre. Semi-central areas accounted for 17% of the total take up, Hinterland for 18% and Milanofiori for 10%. Compared to 2010, the number of transactions per unit between 5,000-9,999 sqm has increased from four to ten, higher than in 2007 (nine transactions). The number of transactions for units greater than 10,000 sqm remained in line with 2010, equal to five.

Vacancy rate exceeds 10%, completions decreased

In Q4, three new offices were completed, totalling about 26,000 sqm, all located in the periphery. Two of these offices are empty and available on the market, while the other, in the Affori-Maciachini area, was leased to Richemont, a leading company in the field of luxury goods. For an annual total, just under 110,000 sqm of new stock was completed in Milan, a decrease of 66% compared to last year. The projects completed over the year include the new Microsoft headquarters, the refurbishment of the former Post Office (Ferrante Aporti), the new Vittoria Assicurazioni headquarters, the new WPP headquarters and the new Richemont headquarters. Vacant space in 2011 continues to grow, with a vacancy rate of 10.3%. The vacancy of Grade A space is decreasing gradually, from 36% to 32% of the total space available, while Grade B space is increasing, equal to 54%.

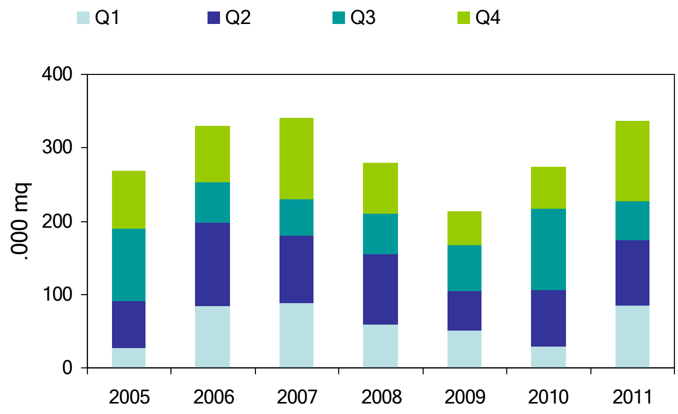
Milan offices, key indicators

	Year to date 11	Q-on-Q Change	Y-on-Y Change
Completions (,000 sqm)	108.8	--	-66%
Take up (,000 sqm)	336,2	>100%	+23%
Vacancy* (,000 sqm)	1,238	+3.9%	+10%
Vacancy rate* (%)	10.3	--	--
Prime Rent (€/sqm/yr)	520	0	0
Prime Gross Yield (%)	5.25	0	-45bps
Office Investment Volume (€ million)	501	129%	-56%

Source: CBRE

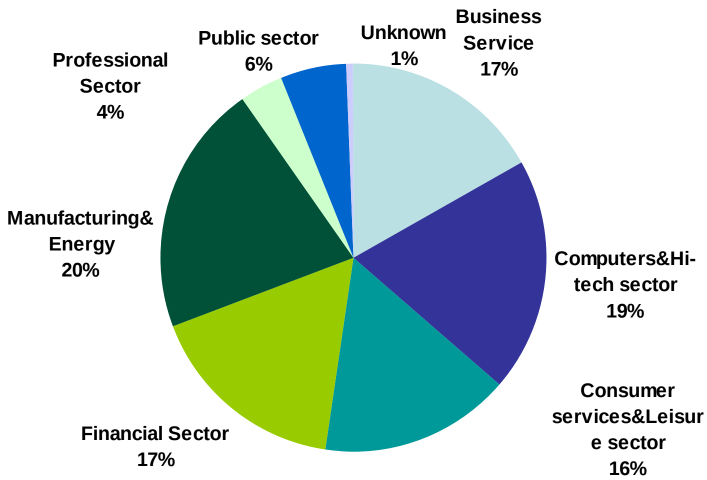
* Vacancy (available space to be occupied immediately) refers to the market in Milan, which includes the city of Milan and the Hinterland municipalities.

Office take up evolution in Milan (sqm)



Source: CBRE

Office take up in Milan by sector, 2011



Source: CBRE

MILAN OFFICE MARKET

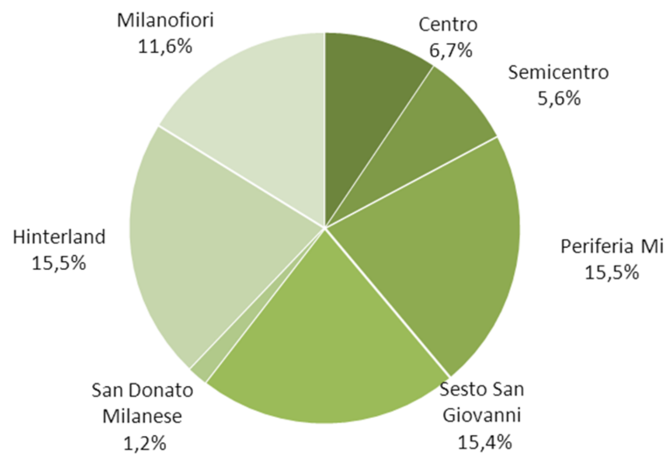
Increasing availability as a result of releasing existing spaces, but quality is decreasing

Compared to the beginning of 2011, available space has increased by 11%. Only 38% of this increase was due to new stock completed during the year. Most of the increased availability was determined by the release of existing spaces, resulting from the consolidation and rationalisation of companies. The central areas have shown the biggest increase in available space over the year, equal to 24%, mostly due to areas outside the CBD. In the periphery and semi-central areas, the annual variation was +10% and +11%, followed by the Hinterland and SSG, each recording an increase of +13%. Only Milanofiori and San Donato Milanese showed a reduction in available space during 2011. The sub-market that recorded the highest increase of available space, as previously expected, was Porta Nuova.
Over 2011, the stock has remained essentially unchanged in Milan on the level of 12 mln sqm. This, combined with rising vacancy rates, despite the high level of take up, resulted in a negative net absorption of -56,000 sqm.
The increasing difficulties related to the deteriorating economic position of Italy and the consequent increase in the cost of money continue to act as a brakes on potential new developments, which remain in line with previous months. In particular, in the last quarter of 2011, projects under construction that were scheduled to be completed by 2011 were postponed to 2012, while the trend for potential speculative projects is to start construction only after securing a tenant.
The estimate of projects under construction with delivery scheduled between 2012 and 2015 remains unchanged compared to previous quarter, approximately 370,000 sqm. Approximately 61% of the total sqm under construction is speculative. The potential surface area in the pipeline with future delivery date expected by 2015 has increased by 6% from the previous quarter as a result of the newly announced project in the Milanofiori area. Of the potential surface area in the pipeline scheduled for delivery within the next four years, 71% is speculative, a slight decrease compared to previous months.

Demand is still buoyant

The demand for medium-large sized spaces with a surface area between 5,000-10,000 sqm remains high, with a total volume that remains between 150,000-200,000 sqm. The combination of quality, floor plate efficiency and sustainability (certification) at affordable rents is becoming the main driver of demand, especially for those companies that are not focused only on the CBD, such as law firms and banks (front-office).

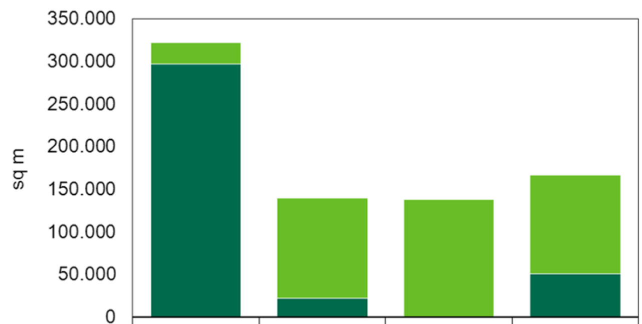
Vacancy rate* by market area in Milan, 2011



Source: CBRE

*The vacancy rate is calculated as the ratio between the available empty surface area and the total estimated stock for the same area.

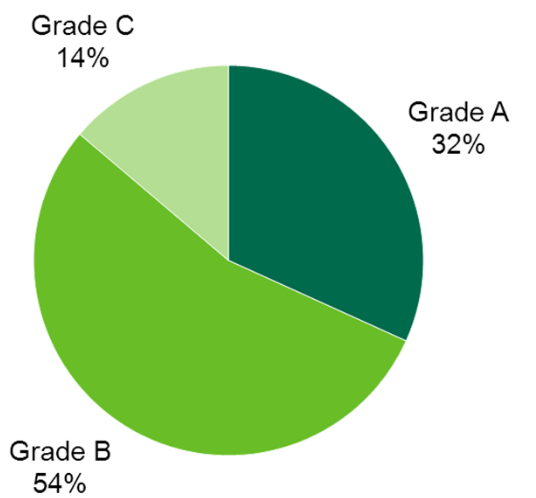
Estimate of office development projects in Milan, speculative and non-speculative, 2011



	2012	2013	2014	2015
Planned	25.000	117.854	137.800	116.165
Under Construction	297.186	22.000		51.000

Source: CBRE

Vacancy (sqm) by property grade, 2011



Source: CBRE

MILAN OFFICE MARKET

The gap between prime and secondary areas shrinks, but grows between quality products and the rest

Prime rent remained unchanged in Q4, amounting to 520 €/sqm/yr. The highest rent recorded in Q4 was less than last quarter, amounting to about 450 €/sqm/yr, obtained by a newly renovated office downtown. The average rent has fallen by 25% over the previous quarter, reaching the level of 221 €/sqm/yr, not far from the weighted average rent of 216 €/sqm/yr. The weighted average rent for Milan in 2011 is 260 €/sqm/yr, influenced by the greater weight of the transactions carried out in peripheral areas, mainly in the second half of the year.
Analysis of the weighted average rent for sub-market areas, relative to 2011, shows a decline in average rents compared to the previous quarter, but brings out another element that confirms quality as a distinguishing factor in the determination of rent. In fact, the maximum rents recorded in the year have been for the most part for new or refurbished units.

Declining investments in the office sector of Milan

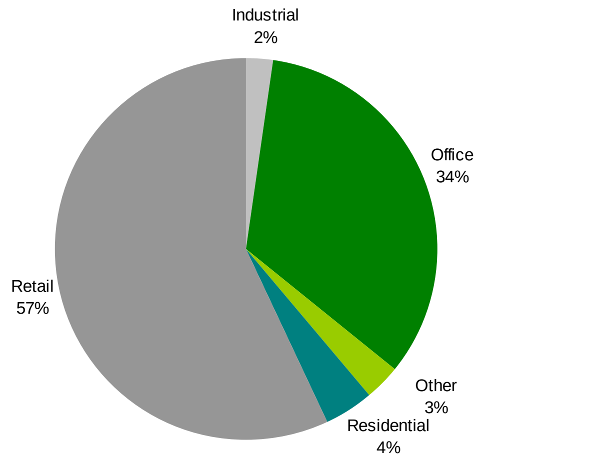
In Q4, there were approximately € 123 million invested in the office sector in Milan, an increase over the previous quarter but down significantly, by almost 80%, compared to the quarterly average (last quarter of each year) of the last 6 years. This has led the whole investment volume in the office sector in Milan over 2011 to close at € 501 mln, almost 60% less than last year. In Italy, the total amount invested in the office sector in 2011 amounted to approximately € 1.5 bn, of which only 34% was in Milan.
Domestic investors still dominate the acquisition of offices in Milan, accounting for 19 investors out of 20 transactions recorded. The number of foreign investors among the sellers reached four in 2011, including three German Open-Ended Funds. The deepening of the Italian debt crisis in recent months has cooled the interest from investors, local and international, who have returned to a wait and see attitude, in order to careful evaluate the opportunities, especially in relation to the increased cost of capital. Prime yields have remained stable at 5.25%, but with an expected growth in the coming months. Secondary yields have continued to grow, +20 bps in Q4, closing the year at 7% (gross). In 2011 in Milan, about 25% of the volume invested in the office sector affected assets that were partially occupied or empty to be refurbished and/or value added investment. This is a trend that could grow during 2012.

Milan office market: sub-market values, 2011

	Prime rent €/sqm/yr	Weighted *Avg. Rent €/sqm/yr	Max Achieved** rent €/sqm/yr
CBD	520	483	542
Centre	400	438	520
Semi-centre	360	292	360
Periphery	260	222	310
Sesto San Giovanni	190	185	185
San Donato Milanese	210	220	220
Milanofiori	220	213	235
Hinterland	--	146	215

Source: CBRE
* Weighted average rent is based on leasing transactions (owner occupiers not included) for units above 500 sq m where rent is available, recorded over the first nine months of 2011. In detail, the number of transactions used for the above calculations are: CBD (12), centre (15), semi-centre (23), periphery (51), Milanofiori (8), SSG (1), SDM (2) and Hinterland (9). ** The maximum rent recorded for units greater than or equal to 500 sqm in 2011.

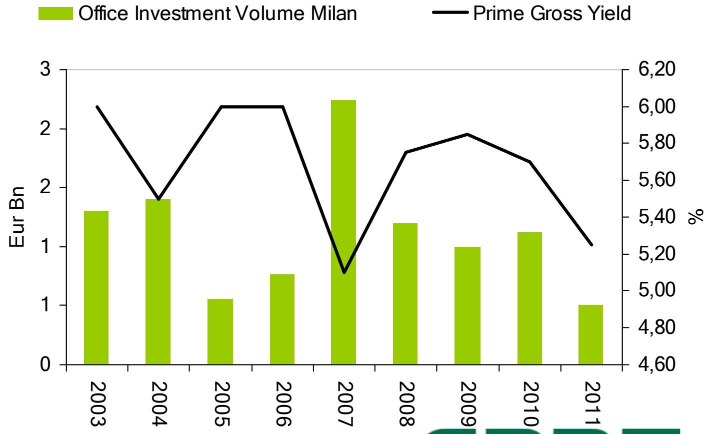
Volume of real estate investments in Milan, by sector, 2011



Source: CBRE

Total: € 1,484 Mln

Investments and yields evolution in the Milan office sector



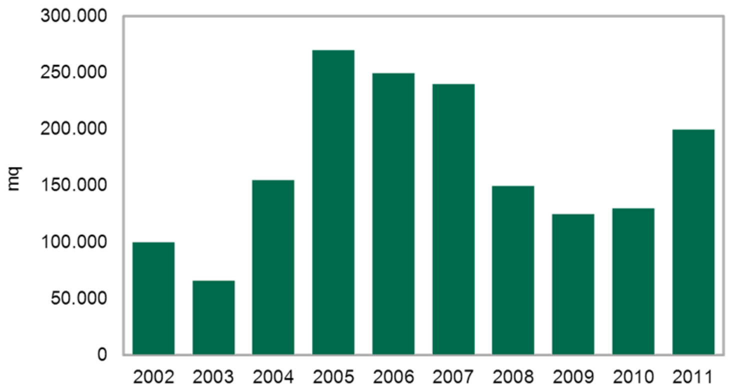
Source: CBRE

Rome offices, key indicators

	Year to date	Q-on-Q Change	Y-on-Y Change
Completions (,000 sqm)	22	0	0
Take up (,000 sqm)	199.76	-49%	+54%
Vacancy (,000 sqm)	558	0	-2.6
Vacancy rate (%)	8.1	--	--
Prime Rent (€/sqm/yr)	420	0	0
Prime Gross Yield (%)	5.80	0	+5bps
Office Investment Volume (€ million)	597	-79%	+36%

Source: CBRE

Evolution of office take up in Rome (sqm)



Source: CBRE

Prime office rents in Rome by sub-market, 2011

	Prime rent €/sqm/yr	Outlook
CBD	420	→
Center	370	→
Parioli	280	→
EUR	340	→
Torrino	270	→
Parco de' Medici	280	→
Fiumicino corridor	220	→
Tiburtina	110	→

Source: CBRE

* Weighted average rent is based on leasing transactions (owner occupiers not included) for units above 500 sqm where rent is available, recorded over the whole 2011.

ROME OFFICE MARKET

Take up increased compared to 2010, but strongly linked to large one-off deal

In the last quarter of the year, office take up in Rome was half that of the previous quarter. Nevertheless, the annual volume of take up reached almost 200,000 sqm, an increase of 54% compared to 2010. In terms of sqm, 32% of take up was determined by two large transactions made in the first half of the year. Excluding these two transactions, total annual take up would remain in line with 2010, about 135,000 sqm. During the quarter, 15 transactions were recorded, mostly for small units. This brought the number of units transacted in 2011 with a surface area less than 500 sqm to represent 38% of the total units recorded, 29 out of a total 77 units. With regard to the quality of space absorbed in the year, 80% of the units had an average quality (Grade B), confirming the limited availability of spaces that meet international standards of quality in Rome. The area that has seen increased take up throughout the year, in terms of number of units, has been the CBD, with 17 units absorbed, all with an area less than 500 sqm, with the exception of a small-medium sized unit (1,000-4,999 sqm) involving a company in the banking and finance sector. Instead, the macro-area in the south of Rome, including the sub-markets, EUR, Torrino, Laurentina and Fiumicino Corridor, has recorded 26 transactions, confirming the greater dynamism of this part of town where there is a higher supply of quality spaces and larger sizes.

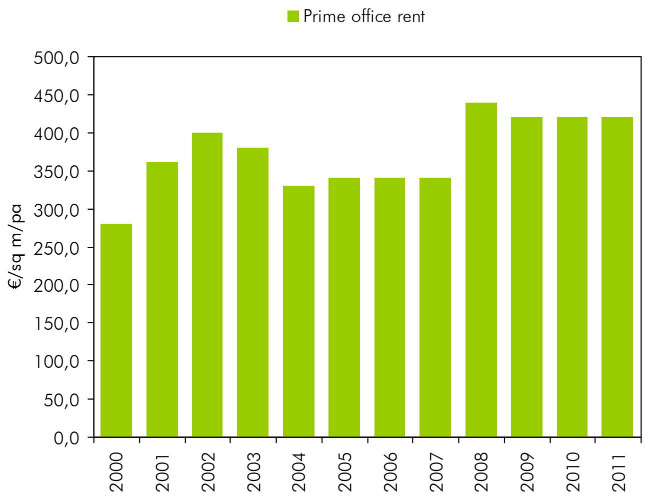
The industrial sector has driven take up in Q4, but some companies have been searching for more than a year

In the last quarter of the year, the most dynamic companies in the market were those active in the industrial sector, which accounted for 55% of the total sqm taken up in the quarter, in the south of Rome. This included a pre-let and a leased transaction of a portion of the Da Vinci Business Centre by a U.S. multinational company, which was on the market for over a year.

Rents are stable in all sub-markets

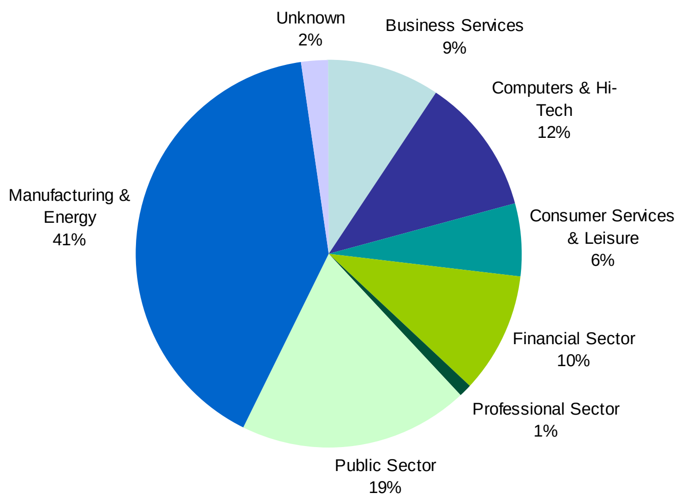
Prime rent in the CBD remained stable in the fourth quarter, at 420 €/sqm/yr. Rents continue to remain stable even in the Eur area, at 340 €/sqm/yr. For the entire year, the weighted average rent* is estimated at 232 €/sqm/yr. In the central area, companies continue to pay a high rent to occupy prestigious historical buildings: the highest rent recorded over the year was about 500 €/sqm/yr.

Prime office rent in Rome



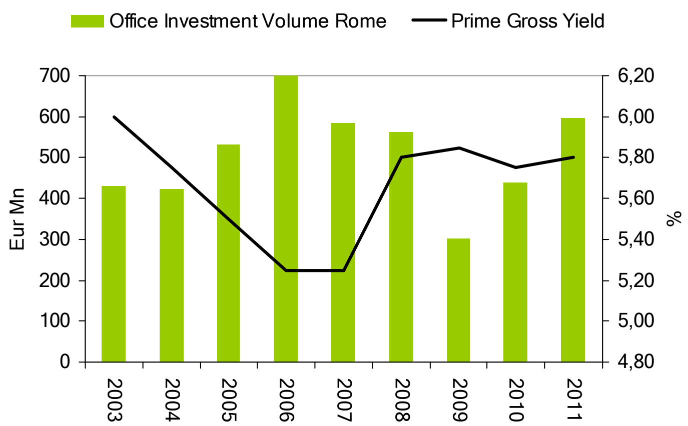
Source: CBRE

Office take up in Rome by sector, 2011



Source: CBRE

Investments and yields evolution in the Rome office sector



Source: CBRE

ROME OFFICE MARKET

Speculative developments halted, vacancy rate stable

The situation regarding the availability of office space in Rome remains unchanged compared to previous months, and the only construction (office) activity is limited to the new development of Europarco, where there are already the new Headquarters of the Ministry of Health and of P&G. The area under construction in this development is approximately 90,000-100,000 sqm, and only slightly more than 20,000 sqm is speculative. There is also a potential further development of just under 50,000 sqm, however work will likely begin only upon securing a tenant. The availability of office space in the fourth quarter remained in line with that of the previous quarter, confirming a vacancy rate of 8.1%.

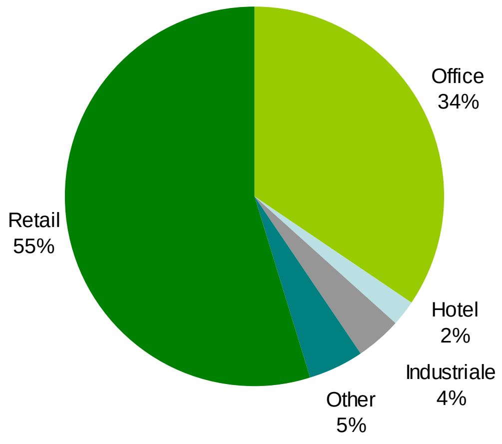
Campidoglio 2 project back in the agenda of the urban planner

After the announcement of the new headquarters, pending completion from the Province and the Transport Company (ATAC), the capital is once again hearing talks of the *Campidoglio 2* development: a project of rationalisation and concentration of branches and offices of the Public Administration that should take place near the Ostiense Station, in the XI Municipio. In addition, the project to add value to the Rome real estate public portfolio and its subsidiaries continues. To this end, the Municipality of Rome has signed, in January, an agreement with ANCI, Agenzia del Demanio e Agenzia del Territorio in order to realize a census of the assets, an analysis of their potential and a projection of interventions to enhance its market value.

Volume of investments in Rome continues to increase, but there are few core investments

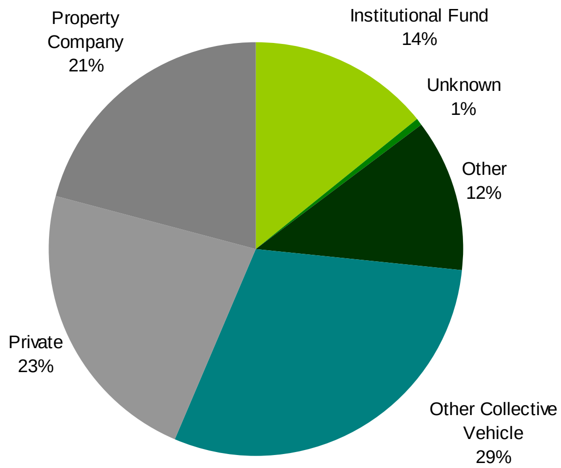
The total amount invested in real estate in Rome in 2011 reached € 723 million, a decrease of 29% compared to 2010. Most of the capital invested, 83%, was in the office sector, confirming the trend of the year. In Q4, the volume invested in offices, amounting to € 75 million, showed a decrease from the previous quarter, and was mainly driven by the sale of an office occupied by a leading company in the luxury sector, for € 42 million. The second investment, just over € 30 million, was the disposal of an asset by Beni Stabili in the south of Rome. The interest of investors in the capital remains high, with Italian real estate companies expressing a willingness to invest in 2012. Prime yields have remained stable.

Volume of investments in Italy by sector, 2011



Source: CBRE

Investments volume in Italy by type of buyer, 2011



Source: CBRE

Main real estate investments in Italy, Q4 2011

Name/ Address	Type	Price mln €	Purchaser
Via Moscova 3	Office (MI)	30.1	Fondo Inarcassa RE
Via Brera 17	Office (MI)	17.1	Fondo Inarcassa RE
Megalò	Retail - SC	140	ECE
Via del Tritone 142	Office (RM)	42	Fondo Fedora (Prelios sgr)

Source: CBRE

REAL ESTATE INVESTMENT

In Italy, the volume invested in the last quarter was close to €1 billion, down 26% compared to Q3 and half of the volume invested in the last quarter of 2010. The value has returned to the level recorded in the last quarter of 2003. This brought the total real estate investment in 2011 to € 4.3 bn, a decrease of 12% compared to 2010.

In the wider European scene, real estate investments in 2011 reached € 115 bn, an increase of 4% compared to 2010. Italy, Spain and Portugal were the only countries to record a decline in annual investments, reflecting the more general crisis of confidence and credibility that has engulfed these countries, especially in the last months of 2011.

Regarding the analysis of the whole investment volume by asset in Italy in 2011, it confirms the prevalence of the retail sector over the total invested, with 55% of the total. High Street and sales of portfolios have accounted for a majority of the retail investments, 66%, with just over € 1.5 bn invested. The above mentioned portfolios, in addition to the METRO Cash & Carry and branches of Banca delle Marche, include the sale of 10 Coop supermarkets by Unicoop Tirreno to the fund Augusto managed by Castello sgr, which took place in the last quarter of the year at almost € 50 million. Yields remained unchanged for the high street assets, equal to 5.25%, but with a potential of future growth. Prime yields for shopping centres increased by 10 bps, reaching 6.25%. The office sector, with 34% of the total volume invested, recorded around € 1.5 bn, 25% less than in 2010. The average size of office deals decreased from € 39 million in 2010 to € 23 million in 2011. In fact, in terms of number of office investment transactions, in 2011 64 operations were recorded against 51 in 2010. Prime yields remained unchanged for prime assets in prime locations, but have continued to grow for secondary assets, a further 20 bps in the last quarter, placing it at 7%.

The difficulty of the industrial/logistics sector continued in Q4, with a single transaction for a recorded value of approximately € 20 million, by a tenant who purchased an already occupied warehouse. The total annual investment in the sector was € 156 million, an increase compared to last year. Compared to the previous quarter, prime yields increased by 25 bps, reaching the level of 8% (gross).
Hotel sector total investment volume recorded for the whole 2011 was virtually unchanged from the previous quarter, amounting to approximately € 100 million, 60% less than in 2010.

OUTLOOK

The last quarter of 2011 was marked by a succession of events that brought Italy to the centre of sovereign debt tensions, which have widened and extended in the euro area, assuming systemic importance. Despite changes in the government, which managed to recover the credibility of the country at an international level, and despite the significant fiscal imbalance corrections made by the new government, the road to the future is all uphill. It is now widely accepted that Italy is about to enter a recession that will last at least through 2012, with growth estimates falling and worsening expectations for employment.

Italian real estate market in the last months of the year was characterised by a general cooling of investor sentiment, directly proportional to the intensification of the debt crisis, which has led to a decrease in the total volume invested in the quarter and subsequently the year. Also, the decrease in the weight of foreign capital invested in Italy continued in 2011, thus affecting the declining of the whole investment volume in 2011. In fact, international investors bought assets for about € 1.1 billion in 2011, 22% less than in 2010.

But, in light of these conditions, what possible scenario for the real estate in Italy?

Certainly the next few years will be dominated by extreme economic and political uncertainty that will affect the real estate market, and this will be the *normal* condition in which global markets will operate. The lack of debt availability is likely to be a major constraint on future growth of real estate investment activities, which means that even in the best scenario, it will be difficult to predict strong growth in investment volume in 2012. Given the current landscape of the Italian market - unless there is a significant improvement in the financing conditions – which is unlikely at the moment – the expectations on the total volume of investments in 2012 will remain in line or slightly above the levels seen in 2011. The future investment volume will be affected by the further contraction of foreign capital that could continue in 2012. In fact, to see a massive return of foreign capital in Italy, today, the distressed portfolio would be sold on the market, able to attract major international investment banks, as we were at the beginning of the year 2000, and/or a significant re-pricing of some asset classes (from core plus investments to developments) should take place. Something is already moving in this direction: some financial institutions - such as leasing companies - are starting to repossess assets with the need to provide a way out. But it is still early to understand if it will have an impact on the market in 2012.

The following is the 2012 outlook for the main real estate sectors in Italy:

- **Office:** The worsening of growth prospects and fears over the resilience of employment keep investors – especially foreigners – away from this asset, despite the good "real" market results. In 2012, the repositioning activities of large companies in search of real estate solutions for their needs will continue, and market fundamentals will remain sound. From the investment side however, the polarisation between strong demand for prime properties will continue, as well as the weak demand for secondary asset. The market will still be dominated by investors with a strong risk-adverse attitude, mainly local – Pension Funds, institutional investors and real estate companies.

- **Retail:** The retail sector in 2012 will continue to attract strong demand for large prime schemes, with a dominant market share in their catchment, and we believe that it can continue to offer good prospects for growth. This sector will continue to attract the interest of investors, including international, especially retail specialists who want to take advantage of the sustainable level of values to ensure a presence in Italy, a market that, despite the adverse conditions, continues to present solid fundamentals. The strong investor interest in high street is confirmed also over 2012, that, together with offices, confirms itself as the core asset by definition. Also, the number of institutional investors is growing, including pension funds, insurance companies and sovereign wealth funds, which are increasing their exposure in real estate, looking also in the retail sector.

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