

## France in the limelight as emphasis shifts to income

### Key Highlights

- Total returns in European commercial property are expected to become increasingly reliant on income return and growth in rental values.
- Commercial property in France is forecast to outperform the wider European market.
- France offers significant opportunities to add value to market returns through asset management.

Total returns on European commercial property are expected to become increasingly reliant on income return and growth in rental values, as the positive impact of yield compression abates. In the 2005-07 period, market driven capital growth was an important contributor to above-average returns, however we have now reached a point in the cycle when the emphasis shifts towards active management to capture rental value growth. In the future, slight declines in capital growth as a result of tightening credit markets are therefore expected to be largely offset by rising income returns (Figure 1).

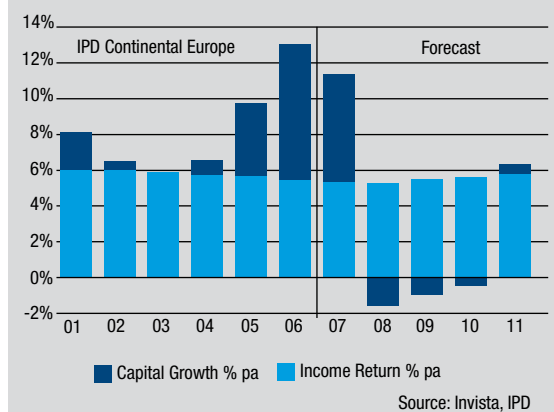
Commercial property in France is forecast to outperform the wider European market over the next four years, with average total returns of 7.0% per annum compared to 4.9% per annum for Continental Europe (see Figure 2).

A key contributor to this outperformance is the level of income return in France (see Figure 3), currently estimated to be around 5.9%, which is comfortably ahead of the other main European property markets.

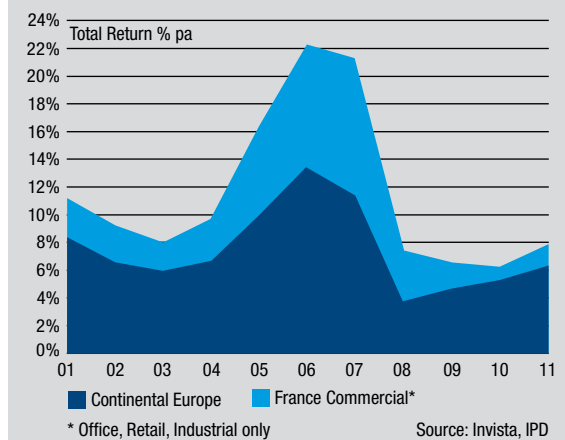
Our forecasts suggest that French income returns will remain above the wider European market over the next four years. Furthermore we believe there is significant scope for growth in French income returns beyond 2008, due to:

- the annual indexation of almost all commercial property leases in France at a forecast rate of around 2.5%–3.0% per annum;
- rental value growth across France is forecast to remain high, not only in Paris' buoyant leasing market but also in the major regional markets such as Lyon, Lille and Marseille; and
- the possibility that such rental growth will be captured through the re-negotiation of six-year leases which were originally agreed at the previous low point in the rent cycle (2002-04).

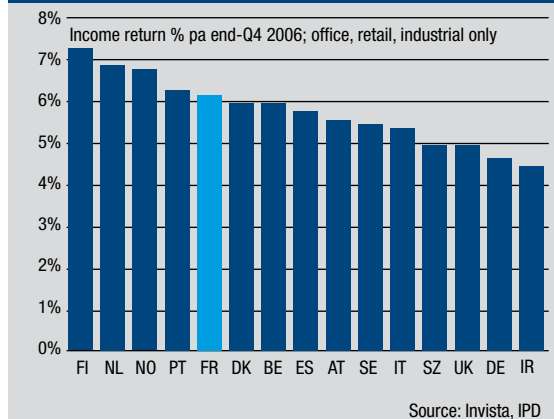
**Figure 1: Income will become the key contributor to total returns**



**Figure 2: French commercial property consistently outperforms the wider European market**



**Figure 3: France is a leading market for income returns**



France has a mature, transparent, liquid and established commercial property investment market. This has been an important driver of recent growth in investment turnover in Paris and other key regional centres (Figure 4). The size of IPD's France Index (office, retail and industrial properties only) has increased since 1998 by 500% to Eur 80 bn and by 330% to nearly 5,700 properties. This is further evidence of the extent to which liquidity in the investment markets has improved across France, helping to develop new regional markets and cycles.

The structure of the French economy supports an active property market in regional centres. Figure 5 shows that over 50% of economic activity occurs outside the three largest city-regions of Ile de France (Paris), Rhône-Alpes (Lyon) and Provence-Alpes-Côtes-d'Azur (Marseille and Aix). This diversity means it is possible to benefit from growth in a large number of property markets each with locally-driven market cycles, in many cases without taking additional credit (ie. tenant) risk.

Against the background of improving leasing activity and rental growth prospects (see Figure 6), significant opportunities exist to execute lease re-gears, refurbishments, redevelopments, extensions and to capture rental reversion. The increasing maturity and 'institutionalisation' of the French commercial property market also means it has become much more conducive to implementing such active asset management strategies.

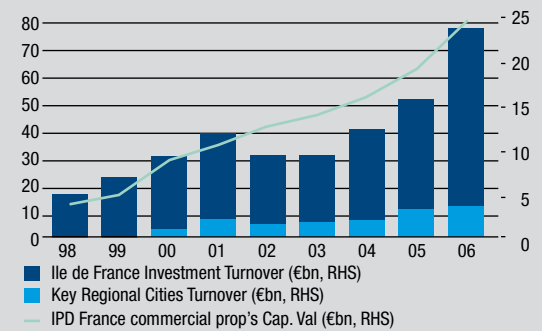
This combination of micro and macro factors support a buoyant outlook in relation to future growth in income returns from French commercial property. The ability to add value to 'market returns' through asset management is an important factor which enables investors to drive up income returns, boost capital growth and in turn outperform the wider European market.

Invista Real Estate opened its Paris office in November 2007 heralding a significant step forward in establishing the Company's Continental European reach and driving its ambitious plans for growth. Invista Real Estate, which currently has circa €13.4bn under management (31 October 2007), has a substantial portfolio in France and is in the process of growing this further through new fund launches.

Invista Real Estate has a dedicated in-house research team that is focused on adding value to all aspects of the investment process. The team facilitates strategic decision-making across all funds which is based on a robust understanding of macro and micro trends affecting property performance.

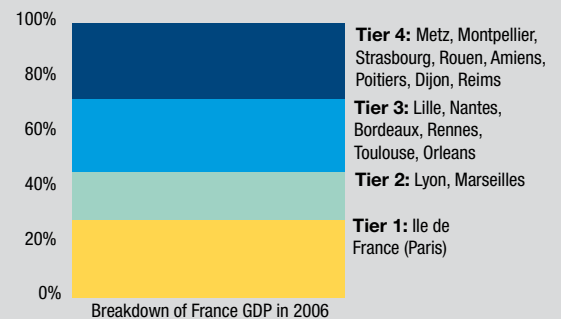
As part of our ongoing commitment to provide investors with insightful perspectives on European Commercial Property markets, we now publish a regular series of research articles exploring important aspects of property investment performance. If you have any comments or suggestions please contact us at [info@investarealestate.com](mailto:info@investarealestate.com)

**FIGURE 4: A deeper pool of opportunities in France**



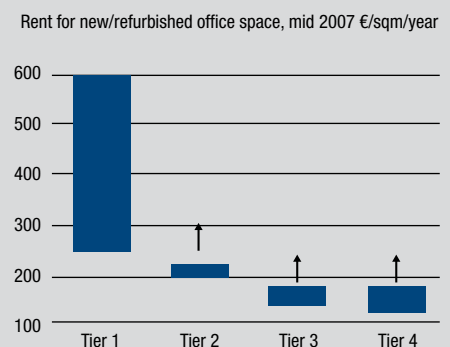
Source: CBRE, IPD

**FIGURE 5: Diversity of economic activity supports property demand in regional centres**



Source: INSEE

**FIGURE 6: Scope for rental growth in regional centres**



Source: CBRE

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Past performance is not a guide to future performance and the past performance of property funds is not always represented by the performance of the property market as a whole. The value of property is a matter of a valuer's opinion rather than one of fact. Investments in property are relatively illiquid and more difficult to realise than equities or bonds.

The value of an investment and any related income may fluctuate and cannot be guaranteed. Depending on the investor's currency of reference, currency fluctuations may adversely affect the value of investments and the income there from. Any forecast, projection or target where provided is indicative only and is not guaranteed in any way.

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