U.S. Opportunistic Investment in European Real Estate

by

Benaim Murray

M.Arch., Yale University, 1993

B.Arch., Illinois Institute of Technology, 1991

Submitted to the Department of Architecture in Partial Fulfillment of the Requirement for the Degree of Master of Science in Real Estate Development

at the

Massachusetts Institute of Technology

September, 2001

2001 Benaim Murray
All rights reserved

The author hereby grants to MIT permission to reproduce and to distribute publicly paper and electronic copies of this thesis document in whole or in part.

Signature of Author
Department of Architecture
August 10, 2001

Certified by
William C. Wheaton
Professor of Economics
Thesis Supervisor

Accepted by
William C. Wheaton
Chairman, Interdepartmental Degree Program in Real Estate Development

U.S. Opportunistic Investment in European Real Estate

by

Benaim Murray

Submitted to the Department of Architecture on August 10, 2001 in partial fulfillment of the requirements for the Degree of Master of Science in Real Estate Development at the Massachusetts Institute of Technology

Abstract

This thesis will look at the investment activities of US real estate opportunity funds after the collapse of the late 1980's and early 1990's and how their strategies have evolved over the last decade. It will investigate the strategies that these funds are currently employing in the attempt to maintain their high yield mandate and in particular will study issues affecting US capital flows into high yield European real estate investments.

The body of the thesis will have four major sections. The first will investigate the history of US real estate opportunity funds and the economic conditions in the US and Europe that led to their creation. The second part of the thesis will describe what opportunity funds are and how they structure themselves legally, their capital structure and fees. This section will also attempt to describe deal types which opportunity funds have used to achieve their returns in the past. The third part of the thesis will describe the four largest economies in Europe from an economic, real estate, lease contract and taxation policy perspective. The fourth part of the thesis will build on the previous three and raise issues that will affect US opportunity funds that choose to invest in Europe.

Thesis Supervisor: William C. Wheaton
Title: Professor of Economics

TABLE OF CONTENTS

1. INTRODUCTION

PREFACE 6

OUTLINE OF THESIS 6

2. OPPORTUNITY FUNDS

WHAT ARE OPPORTUNITY FUNDS? 8

DEAL TYPES 10

Big Broken Buildings 11

Asset Management 11

Distressed Debt Purchases 12

Development 12

Public to Private Arbitrage 13

Alternative Assets 13

3. BACKGROUND

UNITED STATES 14

EUROPE 23

4. COUNTRY PROFILES

GERMANY

ECONOMIC OVERVIEW

Economic Background 27

Current Economic Condition 29

REAL ESTATE SEGMENTS

Office 30

Retail 32

Industrial 33

Hotel.. 34

LEASES AND TAXES

Leases.. 36

Taxes.. 37

FRANCE

ECONOMIC OVERVIEW

Economic Background.. 38

Current Economic Condition.. 40

REAL ESTATE SEGMENTS

Office.. 41

Retail.. 43

Industrial.. 45

Hotel.. 46

LEASES AND TAXES

Leases.. 48

Taxes.. 49

ITALY

ECONOMIC OVERVIEW

Economic Background.. 50

Current Economic Condition.. 51

REAL ESTATE SEGMENTS

Office.. 52

Retail.. 54

Industrial.. 56

Hotel.. 57

LEASES AND TAXES

Leases 59

Taxes 60

UNITED KINGDOM

ECONOMIC OVERVIEW

Economic Background 61

Current Economic Condition 62

REAL ESTATE SEGMENTS

Office 64

Retail 65

Industrial 66

Hotel 67

LEASES AND TAXES

Leases 69

Taxes 70

5. CONCLUSION 72

6. BIBLIOGRAPHY 79

7. LIST OF READERS, INTERVIEWS AND CONFERENCES ... 82

8. ENDNOTES 83

1. INTRODUCTION

PREFACE

This thesis will look at the investment activities of US real estate opportunity funds after the collapse of the late 1980's and early 1990's and how their strategies have changed over the last decade. I will be investigating the strategies that these funds are currently employing in the attempt to maintain their high yield mandate. In particular I will be studying issues affecting US capital flows into high yield European real estate investments.

OUTLINE OF THESIS

The body of the thesis will be divided into four parts. The first part will describe how opportunity funds structure themselves legally, what returns they are attempting to achieve, the level of debt used, the size of the industry and how fees are established. Acknowledging that all deals are unique, this section will also attempt to outline the main deal types which opportunity funds have used to achieve their returns in the past. These deal types are not presented as a complete list and have been compiled through information gathered in interviews with prominent industry players.

The second section will investigate the history of these funds and the economic conditions in the US and Europe that led to their creation. In this section I will look at what attitudes, regulatory stimuli and market forces led to the US real estate boom and its eventual crash. I will further

look at what role opportunity funds had in the solution devised by US government agencies and industry players to the decline in the US real estate markets. I will finally look at how and why opportunity funds decided to focus their attention on Europe after their success in the US and the reasons why US high-yield investors still feel that Europe is a viable investment.

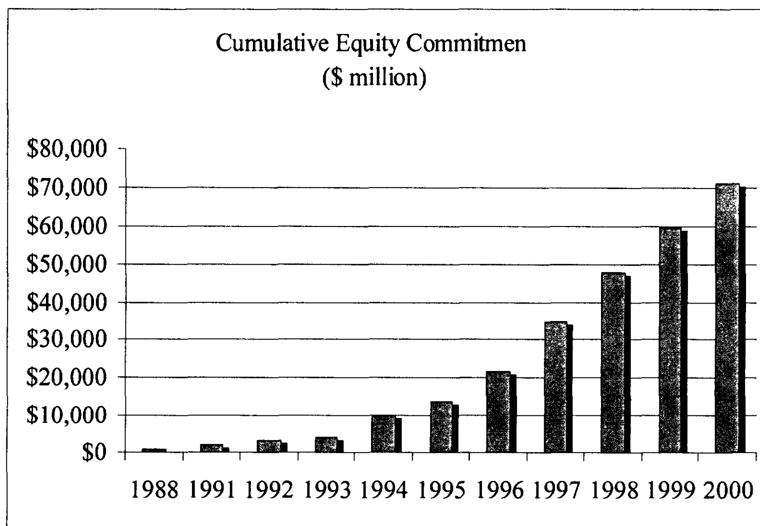
The third part of the thesis will give a description of the four largest economies in Europe, looking at the economic events and attitudes that led to their respective real estate slumps in the early 1990's, the current state of their economy, and an industry review of the current state of their commercial real estate markets divided into office, retail, industrial, and hotel segments. It will also attempt to give insight into what may be the current possible plays in successfully achieving high yields. This information was gathered from interviews of real estate professionals directly involved in the European real estate industry

Given the nature of opportunity funds, their mandate, their history in both the US and Europe and the history and current state of Europe's four largest economies and their real estate markets, the fourth section of this report will attempt to highlight the main issues that opportunity funds will have to address in their pursuit of superior returns.

2. OPPORTUNITY FUNDS

WHAT ARE OPPORTUNITY FUNDS?

Opportunity funds may be described as limited partnerships with a finite life. The general partners normally have a stake in the fund resulting in incentives that are in tune with their limited partners. This reduces the perception of these funds acting as advisors and gives them a stronger platform when raising funds for what are considered to be more sophisticated investments. In general opportunity funds seek leveraged average annual returns in excess of 20% over a five to seven year period. Opportunity funds differ greatly from core real estate investors partly due to their expected higher returns and also due to their greater use of leverage. The real estate opportunity fund industry has seen tremendous growth since its origin in 1988 mushrooming from a total equity commitment of US$ 875 million to a current level of 71.4 billion representing a market capitalization in 2000 of approximately US$ 142 billion.



Note: Results shown for 187 funds[1]

This rapid increase in size can be attributed to the success of these funds in achieving return requirements and a contagion within the financial community for the want of higher returns without the associated risk. Currently the average fund size is US$ 425 million with a median of US$ 320 million. Opportunity funds rely partly on the use of debt to achieve their required return on equity with an average debt/equity ratio of 50%. There tends to be a large variance in the amount of debt used, from all equity investors to funds that leverage up to 80%. Many of the deal structures are very complex and the total amount of debt used by a particular fund may be difficult to determine.

Most general partners in the opportunity fund industry charge an investment fee that is taken from the fund itself when it is closed. This fee normally ranges from 1-1.3% committed capital with a lead investor committing in the US$ 50-100 million range generally being exempted from this charge. Some funds that have integrated management services into their operations also charge a management fee. Most funds do not do their own asset management and use joint venture partners who then charge a fee. A vast majority of general partners of these funds , 91% , co-invest with their limited partners generally with a commitment ranging from 1-5% of committed capital. General partners normally get distributions from profits on a pari passu basis with on average a 20% carried interest and 10% hurdle rates. There is also a pervasive use of catch ups, GP clawbacks and reserve accounts in structuring the relationship between the general and limited partners.

Most opportunity funds, 79%, employ the extensive use of joint venture partners in structuring the way in which they make investments. As funds progress many are beginning to provide services that they would normally shop out in an attempt to reap the benefits of all profit centres throughout the whole investment process. As the high yield environment becomes more competitive this type of vertical integration may become important. In sourcing their deals these funds rely greatly on contacts that they have developed in the industry and in only approximately 20% of the time actually rely on brokers. In general they rely very heavily on off market deals attempting to avoid an auction like process that would lead to a premium added to the cost of the asset that they are trying to acquire and to avoid the heavy dead deal costs of auctions.

DEAL TYPES

In order to achieve their returns opportunity funds have used many different methods of investment. All cases involve bringing a specialized knowledge base to the table, having funds ready to invest, allowing them to take advantage of capital starved environments, and an ability to assess risk. Acknowledging that every deal is different I have attempted to describe broad deal types that will help in understanding how opportunity funds achieve their returns. Through discussion with industry players I was able to identify six main deal types of which one deal may contain a combination of types. An individual opportunity fund may be involved in a variety of these different deal types.

(i) Big Broken Buildings

(ii) Asset Management

(iii) Distressed Debt Purchases

(iv) Development

(v) Public to Private Arbitrage

(vi) Alternative Assets

Big Broken Buildings

With this deal type opportunity funds purchase a single building that has a problem or many issues that the current owner and local market players are not able to solve. These issues could require a range of problem solving expertise including asbestos abatement, lease restructuring, restructuring of financing, or refurbishment and development. Due to the inability of the current owners to solve the existing problem opportunity funds are in a good position to negotiate an attractive price and then add value to the property. In acquiring the property at a discount and then fixing what is broken resulting in an increased market value, these investment funds are able to achieve superior returns.

Asset Management

This approach relates more to funds that have acquired a portfolio of properties and through the vertical integration of asset management services are able to add value through economies of scale and superior service within the marketplace thereby increasing the value of their properties.

These funds invest in asset management companies taking on a venture capitalist's role. By affecting the strategic approach of these asset management companies they are able to customize and standardize operations to suit their clientele base. This ability to provide extra services set their buildings apart allowing them to become dominant niche players. In Europe these funds will have to rely on joint venture partners or groups that provide these services for a fee.

Distressed Debt Purchases

This is a classic opportunistic play that involves opportunity funds buying large portfolios of non-performing loans from governments or banks. This occurred on a large scale in the US during the RTC era and in France during the mid-1990's. The eventual goal would be to convert debt positions into equity positions in the underlying real assets. This would allow for the repositioning and eventual disposal of the assets for a gain.

Development

The development option normally comes later in the real estate cycle. Generally the buying of bad loans and the acquisition of properties to which value must be added signal the bottom of the cycle. As the market improves and liquidity returns it becomes more difficult to find properties to acquire that will produce the required returns without taking on unacceptable risk. At this stage opportunity funds generally start to do joint venture deals with developers who are capital starved but have a strong local knowledge of the markets and have the infrastructure in place to

provide development services. This allows for quick entry into given markets and allows opportunity funds to time their investments well.

Public to Private Arbitrage

With public UK property companies trading at a discount to NAV, opportunity funds have found a way in which returns can be extracted. This is done through taking public companies private, then restructuring a portfolio of properties by splitting up assets and regrouping them in a way that will allow them to be sold at a premium in the private markets. This is a trend that is occurring in the UK markets with publicly traded property companies not able to reach a market capitalization size that justifies their existence.

Alternative Assets

Another way in which funds have been attempting to achieve their returns given the competitive environment that has developed over the last few years has been to invest in assets that could be seen as specialized real estate. These include gas stations, oil rigs, car parks, cold storage facilities, vineyards and train car manufactures. Investment in these alternative assets is viewed as a way to create a competitive advantage and to diversify portfolios.

3. BACKGROUND

UNITED STATES

The American real estate overbuilding of the 1980s'and its eventual crash in the late 1980's and early 1990's can be attributed to a convergence of misguided government policies and market forces. The four forces which are generally thought to have been the major contributors to this historic period of excessive building are the view that real estate inherently acts as a hedge against inflation, the deregulation of the financial industry, changes in income tax policy and the flood of foreign capital into the US real estate markets.

Investors in the 1970's were heavily hit by the erosion of the value of their investments in stocks and bonds due to rapid inflation. Funds were redirected into real estate investments successfully protecting them against the inflationary economic environment of the time. Instead of viewing this as a one time event real estate began to be viewed as a safe bet against the effects of inflation and other assets types were viewed to be always vulnerable, "...in the early 1980's, most pension fund investors concluded, based upon what had happened to them in the late 1970's, that inflation was a real threat to their portfolios."[2] This led to the beginning of an irrational flood of investment into real estate for reasons other than the economic merits of given investment opportunities, " ...rapid inflation did not reappear after the 1982 recession, and the values of stocks and bonds skyrocketed. More over, the overexpansion of real estate development caused real property equities to cease being hedges against inflation, because effective rents had stalled by about 1985 and declined thereafter."[3]

Also in the late 1970's there was a strong movement in the US government to deregulate the financial industry in order to give banks, Savings and Loans (S&Ls), and insurance companies a more competitive advantage. There had been a change in what was considered the most appropriate way for US financial intermediaries to be operated. At the time it was felt that free markets with open competition would produce more efficient markets resulting in better pricing of capital and a stronger economy. Deregulation allowed financial intermediaries to merge and reduced the restrictions on how they invested their assets. This was done partly to combat the effects of the high inflation environment of the time and allowed them the freedom to set higher rates.

It will be seen later that deregulation of the financial industry had the most impact on the S&L's and that the freedom given to these institutions led to the demise of a great many, precipitating one of the largest financial crises in US history. Deregulation placed S&Ls on a level playing field with the banking industry. Past limits on their interest rates and restrictions on the ways they were able to invest were removed. This allowed for a flood of new money to enter the marketplace producing an imbalance between money available and quality opportunities in which to invest. Competition for the limited number of quality investments forced the price of capital to drop, resulting in the underpricing of risk associated with these investments and the flow of excess capital into fringe areas of investment in which investors did not have the expertise to assess the risk involved. In the earlier stages of this period of excess capital for investment, many of the investments made turned out to be profitable and the more unusual investments were seen as a way to strengthen an investment portfolio through diversification. Financial institutions continued to underprice the risk associated with individual investment

partly due to a lack of expertise needed to make a proper assessment and partly due to a tolerance for risk that had become the norm within the financial community.

The S&L industry had built itself on making relatively small fixed rate first mortgages to homebuyers and this was the area of their expertise. After deregulation they shifted their efforts out of this area of expertise and into development. The inflationary economic environment helped in making their initial investments successful, boosting the growth of housing prices. These initial successes led to the S&L industry's change in focus to lender to the development industry for land speculation, construction, and development. Many of them moved far enough up the risk curve to be considered essentially merchant banks which were comfortable taking large risks with depositors' money which had been insured by the federal government. At this stage the S&Ls decided to move away from their traditional industry of housing to enter the commercial property markets in search of higher returns. The combination of an excessive amount of capital chasing a limited amount of sound investment opportunities and the shift of S&Ls from the traditional industry in which they had developed their expertise led to a severe fall out when the macroeconomic environment deteriorated. By 1987 the foundation for the S&L crisis had already been set. Billions of dollars had been loaned to finance projects that had dangerously high levels of debt and to acquire developments that had been given abnormally high valuations given their economic fundamentals. Due to the shocks from the capital markets and a retreat in consumer and business confidence, financing for the overvalued and over leveraged properties began to dwindle. It was at this stage that development projects across the US began to experience major difficulties meeting their debt service commitments and that S&Ls began to incur massive losses and an unprecedented amount of bad debt and foreclosures.

By 1991 S&L commitments in the commercial real estate markets dropped by one third due mostly to a tidal wave of foreclosures.

Commercial Mortgages Held by Savings Institutions[4]
($ Billions – All data is year-end except 1991)

1987	1988	1989	1990	1Q1991
$150.9	$141.4	$134.4	$109.2	$101.2

Source: Federal Reserve Bulletin, September 1991, p.A37

S&Ls fell into insolvency by the hundreds. During the period between 1979 to 1991 the number of S&Ls was reduced to 50% and the federal government found itself reimbursing depositors and taking control of massive portfolios of real estate. The quality of these assets varied greatly from ill-conceived developments with no economic merit to high quality real estate products that had been too highly leveraged.

The circumstances for the banking industry were similar but their abuses following their new freedoms were not as wide spread nor did they penetrate the industry to the same extent. Since the 1930's the banking industry had been limited in the way they were allowed to compete. The federal government had decided to insure depositors and decided to protect itself by creating regulations that would limit the level of risk that banks were permitted to take with their deposits. With deregulation the banks found themselves in a much more competitive environment which forced them to look for riskier investments in order to achieve their needed returns. This search for higher returns led them to the development industry that by nature is hungry for investment. During this period there were many development projects in need of debt financing and developers seeking high returns on equity and therefore willing to use high levels of leverage. This suited the banking industry in that they were able to justify pricing their capital

at higher levels due to the inherent risks associated with the debt levels of these projects. Within the banking industry real estate loans very quickly became a prominent feature on balance sheets with an industry average of 25% of assets represented by this loan type. "By 1987, the national office-space vacancy rate – which was under 5% in 1981 – had exceeded 19% for three years running. Yet banks accelerated their investments in new construction loans in 1988 and 1989."[5] In many cases projects were refinanced based on overvaluations allowing investors to take out their equity while further increasing the amount of debt that their development was securing. "Only under conditions of "normal" liquidity will movements in property prices directly reflect changing net rental incomes. When real estate markets are swamped with funds looking for properties, competition among buyers loaded with money can drive property prices upward even if effective rents are falling."[6]

The collapse of the oil industry hastened the crisis. As a result of the drop in oil prices a regional recession in Texas and Arizona began to threaten the viability of investments made in their gleaming new skylines. Other parts of the nation did not feel these initial ripples in the economy. Eventually the problems in the US economy were found to be pervasive and the country was stuck with a massive over supply of commercial real estate. By 1990 the banking industry throughout the US held bad loans and real estate assets from foreclosure with a market value of US$ 99.1 billion.

The tax laws that were in place at the time were another major factor in the real estate crisis of the 1980's. Laws that were enacted in 1981 created incentives for investors to fund real estate developments based not on their economic principles or due to a need in the marketplace for a

particular product, but due to the impact that the project would have on the tax liabilities of the investor involved. The tax laws before 1986 created tax shelters for all income flows for investors who put capital in real estate investments. This was done by allowing tax burdens to be reduced by the amount of interest on loans, operating expenses that exceeded rental income, and most importantly, through the deferment of tax payments due to depreciation. Thousands of limited partnerships were created and marketed to investors precisely for these benefits completely neglecting to underpin such partnership with a sound investment rationale. This created again another flood of capital into the real estate markets for all the wrong reasons. Too much capital was chasing too few quality deals resulting in the funding of very shoddy projects that had been structured to carry too much debt. With the change in tax laws in 1986 deductions were no longer allowed for income that was not directly related to real estate and the time period over which a project's value was to be depreciated was increased resulting in a substantial reduction in the effectiveness of real estate as a tax dodge. This led to investors being stuck with not only investments that were not performing due to market conditions and poor financial structuring but also with the inability to take advantage of losses. Out of pocket contributions were being demanded and many limited partnerships began to go bankrupt.

Into this volatile mix of deregulation and poorly crafted incentive for investment in real estate there was an inundation of foreign capital in the mid-1980s. The Japanese followed by investors from Western Europe entered the market and made very large investments in very prominent and mostly over valued properties allowing some developers to luckily exit unscathed. These new investors also were not interested in the underlying economics of the assets they were acquiring but were fueled by the prestige derived by ownership and the misguided perception that the price

of the assets they were acquiring was good value due to the relative price of real estate in their own countries. This influx of new capital fueled the escalation of the valuation of properties allowing developers once again to refinance their overvalued portfolios increasing the risk of default.

With the crash of the real estate industry and its direct effect of driving thousands of S&Ls and banks into bankruptcy the US federal government found itself holding approximately 400 billion dollars worth of bad loans and property that had been foreclosed upon. Of this total 300 billion had come from S&Ls while the balance came from the banking industry. "More than 22 million depositors were protected during the takeover of 743 failed thrift institutions. Without this deposit insurance, financial chaos along the lines of a major depression would have been a strong probability."[7] The FDIC that had been set up to dispose of the assets of failed banks was also given the burden of disposing of assets seized from the S&L industry. Given the size of the failures that were occurring and the weakness of the US banking industry the FDIC had to change its approach in disposing of the assets of these failed financial intermediaries. For the first time instead of selling whole banks and their assets to sound banks which were looking to increase their presence in the marketplace the FDIC was forced to sell the assets of these collapsed institution on a piecemeal basis. This approach was useful because it opened the size of the market in which the FDIC could dispose of its assets. The US congress set up the RTC in 1989 specifically to deal with the disposition of assets from the S&L industry and placed it under the supervision of the FDIC. By 1991 the RTC was separated from the FDIC due to administrative problems and began functioning as an autonomous agency allowing the FDIC to fulfill its role of disposing of assets from the banking industry.

It is in this environment that the original real estate opportunity funds were formed. The RTC and the FDIC had been given a mandate by the US congress to dispose of all of their assets which were primarily loans, and to do so within a given time frame. The government had no interest in holding on to or operating any of these assets and as a result was selling at great discounts. “Everything the RTC has under its jurisdiction is for sale at today’s market prices,” says Kelly (Lamar Kelly, RTC senior vice president for asset sales). “You don’t speculate, you don’t hold it, but sell it on an as-is basis.”[8] Another reason for an average discount of 40% that was being obtained by buyers of these assets was the sheer volume of real estate which was being put back onto the market and the lack of liquidity in the real estate markets at the time and buyers’ and sellers’ inability to establish fair market values. This resulted in a further depression in real estate prices. By 1991 Wall Street and astute private real estate funds began to be attracted to the fire sale prices offered by these two government agencies and the possibility for abnormally high returns when real estate markets returned to equilibrium. From the period of 1991-1995 billions of dollars of discounted real estate was sold to opportunity funds who through various methods ranging from holding a property waiting for cyclical changes to total redevelopment and repositioning, were able to achieve leveraged returns of 35-50%. Methods used by opportunity funds at this stage involved Distressed Debt Purchases, Big Broken Buildings and Asset Management. Opportunity funds were able to buy large portfolios of bad loans as a way to take control of large portfolios of real estate. Once the underlying assets were under their control, opportunity funds were then able to fix whatever problems the properties may have had, be it through restructuring of financing, re-leasing or redevelopment in preparation for placing the product back on the market. With an improved product and an

expected rebound in the marketplace opportunity funds positioned themselves to make superior returns with a relatively short turn-around time. Opportunity funds were also able to take advantage of Asset Management opportunities. In acquiring large portfolios of real estate from the RTC opportunity funds were able to take advantage of existing inefficiencies. These large pools of property could be regrouped in a more efficient manner according to location or asset type and managed in a way that reduced costs due to economies of scale or added value due to newly available services. By 1994-1995 sales from the RTC were beginning to dwindle and it was felt that by 1996 the agency would finally be closed having fulfilled its mandate.

During this period another large opportunity became available for funds that were in the pursuit of high returns through real estate investment. The Japanese recession was beginning to take its toll on the large trading houses, insurance companies, banks and private investors who had made ill advised purchases of trophy real estate in the mid to late eighties for astronomical prices. The Japanese had US$ 77.3 billion invested in US real estate and in 1994-1995 sold approximately US$ 10 billion of which 60% was acquired by the US opportunity funds. "Sales of Japanese-owned real estate assets in the United States more than tripled in 1995 to approximately $7 billion (including the disposition of the Japanese interest in Rockefeller Center). In addition, at the end of last year, the Japanese had contracted to sell or were actively marketing $1.87 billion of assets."[9] The disposition of these assets in the depressed property markets of the mid-nineties again allowed these funds to buy real estate with sound economic fundamentals for a discount. Opportunity funds generally viewed these quality assets as Big Broken Buildings mainly due to the fact that they were over-leveraged. With the purchase of these assets at a discount and the ability to refinance them in the low interest environment opportunity funds were able to quickly

turn these assets into attractive acquisition targets for more conservative institutional investors. The buying spree of 1992-1994 led to the first exit period of 1994-1997 during which the opportunity funds disposed of their assets, reaped their returns signaling the end of the first stage of the US high yield investment period as real estate markets came back into equilibrium. The exit strategies that were used by opportunity funds in the disposition of real estate assets varied and included sales to REIT's, financial institutions, private investors. Some funds restructured their portfolios clustering assets according to sector, geography and through Wall Street intermediaries sold their story to retail investors as a REIT initial public offerings. Other funds feeling that the timing for the disposition of their assets was not right took the option of refinancing their portfolios. By 2000 US$ 71.4 billion dollars of total investment had been invested by opportunity funds in US real estate much of which has not been disposed as yet.

EUROPE

As the US real estate markets came back into equilibrium and the era of the RTC came to a close US investment funds seeking high yield had to change their focus. Wanting to take advantage of their expertise that had been developed during the high yield investment period in the US these funds sought out other economies that were experiencing similar economic problems that had plagued the US. Most importantly they were looking for economic environments that were at the bottom of an economic downturn in which there were many distressed sellers of real estate assets be they banks which had foreclosed on non-performing loans or owners of distressed property. Very key to the equation was to find a real estate market that was capital starved, this illiquidity forcing down the cost of acquisitions, and which was experiencing what could be thought to be

only a short term inefficiency that would be quickly corrected. They were able to find these conditions in both Japan and Europe.

The first commitments of capital seeking high yields in Europe came in 1994 and 1995. They were first attracted by a similar real estate recession that the US had experienced and that was partly induced by the impact of the downturn in the US economy that had taken a couple of years of lag time to fully impact the European markets. During the 1980's the European real estate markets experienced strong growth due to rapid growth in the economy and an over supply of capital. Developers and investors expected a longer economic expansion period and overbuilt the commercial property markets. During the recession of the nineties demand for commercial space was drastically reduced due to downsizing in corporations resulting in an increase in vacancies, plummeting rents and a negative correction in property values.

The French property markets had been the hardest hit and many of the French banks and financial institutions were on the verge of insolvency. The French government had been assisting the banking industry and wished to repair its bad loans crisis before EU integration. At this stage the French government made the announcement to sell the non-performing loan portfolio in bulk. Due to the lack of liquidity in the market, the US funds were able to get the loan packages at a great discount. Again US opportunity funds began the process of going through the underlying assets of these distressed loans to see where they could apply proven techniques that had been utilized during the US recovery. This has involved fixing problems that these assets may have had and repositioning them in the market place.

Attempts to enter other primary European property markets were not as successful. US funds looking to acquire properties in the distressed UK markets found that the banks and financial institutions were taking a longer term perspective on how to dispose of foreclosed assets. Instead of selling properties to US funds at fire sale prices they decided to hold on to properties and wait for the markets to turn around allowing them to recoup a larger portion of their investment. Compared to the French scenario opportunity funds found that the federal government was not encouraging the quick resolution of the existing problem and that local markets were more efficient with local high yield players also wanting to acquire assets at a discount. Nevertheless US funds did enter the UK markets in a substantial way beginning in 1996 taking advantage of what was the beginning of an upturn in the markets.

Many of the funds that entered the markets in the mid-nineties are now looking for an exit strategy and are also poised to take advantage of the next set of opportunities that are arising in a more consolidated EU environment. In the last few years there has been a wave of privatization of government owned businesses. Once in the private sector these newly privatized companies are attempting for the first time to maximize shareholder value. This has become a priority also due to competitive forces and the possibility of hostile takeovers. This in the past may not have been seen as a threat but with the recent takeover of Mannesman by Vodaphone this reality is starting to impact European corporate strategy. In an attempt to maximize their competitiveness these companies are looking to rationalize their balance sheets by liquidating assets that are not seen to been essential to their core businesses. "Analysts estimate that as much as 70 percent of the 3,400 billion Euro (US$ 3,091 billion) of commercial real estate assets in Europe is owned by corporate occupiers; this compares with around 20 percent of the 4,000 billion Euro (US$ 3,637

billion) market in the United States."[10] There is a trend for these larger companies to focus on the industry in which they specialize. As a result it is expected that very large portfolios of property varying in quality, location and size will be available for purchase. An example is De Te Immobilien which is a company formed by Deutsche Telekom as a real estate subsidiary. "De Te is a massive company, with 32,000 properties totaling 180 million square feet (17 million square metres)...last valued at US$ 22 billion."[11] Another example is Milano Centrale a subsidiary set up by Pirelli that has liquidated portions of the company's real estate holdings. "The initial portfolio consists of 370 buildings valued at US$ 1.6 billion..."[12] Due to the volume of real estate that is expected to flood the markets some investors are anticipating a reduction in prices, but there are those who are skeptical that a discount will materialize due to the amount of funds that have been raised to take advantage of these opportunities. Having been mismanaged for years by companies that do not specialize in real estate it is felt that inherent to these portfolios are basic inefficiencies that opportunity funds can take advantage of. The combination of the discounts expected, the inherent inefficiencies, the ability to add value through proven techniques developed in the US, the expectation of continued economic growth in Europe, and the demand for modern facilities, services and lease structures have led US opportunity funds to believe that there are still many high yield opportunities left in Europe. As a result there is currently US$ 8 billion in equity committed for use in high yield investment when leveraged potentially totaling US$ 25 billion.

4. COUNTRY PROFILES

GERMANY

ECONOMIC OVERVIEW

Economic Background

The combination of the German reunification in 1990 and the world recession had a great impact on Germany's real estate markets. The reunification of the country created optimism and the expectation that Germany would become the centre of the European Union and that there would be vast demand for all types of commercial real estate. Germany differs from other European countries in that the bulk of its real estate market is divided among five major cities each having its own specialization while in the UK, France and Italy a large majority of the commercial real estate is concentrated in one or two commercial centers. "Frankfurt is the country's financial center, Dusseldorf its fashion and advertising headquarters, Hamburg the media and publishing mecca, and Munich the electronics base."[13] Berlin in particular with the fall of the Berlin wall and the impending relocation of the federal government from Bonn was viewed as a market that would receive an insatiable demand for new office space. In an attempt to stem a flow of East Germans into the west large amounts of government funds were funneled into East Germany, "which has a long-term need for investment capital to develop and modernize manufacturing plants, research and development centers, warehouse and distribution facilities, office buildings, and other assets."[14] This was done in an attempt to stimulate its economy but acted as a drain of

capital resources from the west. The tax laws encouraged the funding of real estate developments due to tax benefits and was favourable to closed-ended funds. Local banks and financial institutions attempting to achieve returns better than that of fixed interest investments began to make aggressive commercial loans. Funding from Japanese investors who were still greatly expanding their position in the international real estate markets joined local financing. The abundance of financing and the optimism felt regarding a reunified Germany led to a vast oversupply of commercial real estate at a time when there was a global contraction in demand especially in the financial and manufacturing sectors. This oversupply and bust was felt most strongly in Berlin. "Rental rates for prime office space began to climb, reaching a peak of $34 per square meter per month in the period from 1992-1994. Berlin's office boom was followed in 1994 by a period of overbuilding … Rental rates declined in the 1995-1996 period to $17 per square meter per month…"[15] This led to a real estate crash similar to that experienced in the UK and France. What has been very different about Germany's recovery from this financial crisis is that there has been very little international involvement in its recovery. The German markets regained their health not through an influx of US capital buying distressed assets and non-performing loans at a discount but was driven by a surge in liquidity introduced by an expansion in the German open-ended fund market. These funds which started to appear in 1992 and 1993 were offered to the public as liquid units providing returns of 5-6% that could be used as a substitute for savings accounts and were marketed by the banking institutions. They were then used to acquire real estate at a discount taking the burden of bad loans and unwanted real estate assets off the hands of the banks and insurance companies. This allowed Germany over a 7-year period to work through its financial crisis with a domestic solution maintaining control over its real estate markets.

Current Economic Condition

Germany is currently experiencing very strong economic growth which is being fueled by a combination of factors. The 3% growth in GDP can be partly attributed to the relatively low value of the Euro compared to the US dollar which has lead to a 12% increase in exports. There appears to be a continued increase in consumer spending and investment by businesses in machinery and equipment. Consumption is expected to increase as income tax reductions for individuals and businesses are implemented. This should have the impact of fueling industrial production that will allow for the continued investment in machinery and equipment. Unemployment is already at its lowest level since the 1990 having dropped to 10.2% and is expected to continue to fall. Fortunately for businesses this drop in unemployment has not been accompanied by growth in wages. This decrease in unemployment is mostly due to an increase in part-time employment in the labour market. On the horizon there is concern that the combination of increases in the cost of oil and deflation of the Euro may create inflationary pressures. This could have the impact of slowing the drop in unemployment. The current interest rates set by the European Central Bank are slightly higher than would be considered ideal for the German economy but are still considered to be within an acceptable range.

German Economic Profile - Insignia Richard Ellis

	1997	1998	1999	2000	2001
GDP	1.5	2.2	1.5	2.9	3.0
Inflation	1.7	0.6	-0.3	1.2	1.5
Consumer Expenditure	0.7	2.3	2.1	2.3	2.7
Short Term Interest Rates	3.3	3.5	3.0	4.3	5.1
Long Term Interest Rates	5.7	4.6	4.5	5.8	6.2
Unemployment (OECD)	9.8	9.3	9.0	8.5	7.7

REAL ESTATE SEGMENTS

Office

The German office market has been experiencing a boom which has been wide spread affecting its five main urban markets. The absorption of office space has been at record high with 2.4 million sq m of space taken up in 1999 and 1.4 million sq m of space absorbed in the first half of 2000. This represents an increase of 17% over the first half of 1999. Due to this robust demand and the inability to provide adequate supply vacancy rates have been dropping. Vacancy rates in Germany's largest cities are steadily moving downwards with Munich experiencing a vacancy rate of 0.4%, Frankfurt 2% while Hamburg has dropped to 2.4%. Berlin due to over building during the last five years has a vacancy rate of 8%. The Berlin market continues to display softness with a low pre-let level of 22% for new inventory in the pipeline. This is very low

considering the average of 52% for Germany's six major cities and the high performances in Munich and Frankfurt with pre-let levels of 73% and 63% respectively. Very importantly there is a limited supply of centrally located office space with floor plates that exceed the 2000 sq m barrier. Apart from straight development many old buildings are being updated or converted to new uses. The combination of these factors has lead to the first noticeable increase in rents since 1990 and if these conditions continue rents are expected to increase. This strong take up which has led to a drop in vacancy rates and increase in leasing and pre-letting is a result of the strongest growth seen in the German economy since 1991. Corporate expansion in the banking and financial services has been one of the main engines of growth. One important source of demand for office space was the IT sector. It accounted for 30% of Hamburg's office take up. With its recent demise most of the pressure in these markets should be alleviated.

At this stage of the German real estate cycle opportunity funds will have difficulty finding low risk investments yielding high returns. There may be opportunities in secondary locations which lack investment and have assets which need to be repositioned to take advantage of the low vacancy rates in Germany's major centers other than Berlin, and the movement of corporations to the periphery of city locations. There may be also some opportunities in the purchase of owner-occupied portfolios, some of which are coming onto the market. The real estate cycles in Germany tend to be shorter and are less volatile than other markets, lasting 2-3 years, allowing for small waves of speculative development which if it involves the right local partners and timing can provide high yields.

Retail

Demand within the retail sector of Germany's main five urban markets has been very strong. Competition among German retailers has been very high and this has been further exacerbated by the entry of Walmart into the discount segment of the market. There is an undersupply of suitable retail space that has led to increase in price. In spite of this activity among retailers for new and improved space the demand from consumers has remained soft which has further fueled the competition among retailers. The biggest concentration of activity is occurring in the five main markets with Berlin achieving the highest retail rents. This is partly due to the introduction of foreign retailers. Outside of the five main urban markets the retail sector is showing decline even in what would be considered prime areas. The eastern states have been the hardest hit due to an oversupply of space and a substantially lower consumer purchasing power. There has been an attempt to introduce new product types including Planned Urban Entertainment Centers and Factory Outlet Centers. In both cases there has been difficulty establishing these product types in the marketplace. The PUEC's which were in the pipeline have been put on hold and the FOC's are performing more as discount centers due to the lack of luxury goods being offered. There has also been an attempt to change the retail business culture adopting some US customs. "Traditionally, European shopping hours have been much shorter than those in the United States, with Sunday closings, half-days on Saturday, and early evening closings on weekdays. In recent years, the trend has been toward lifting these restrictions. Germany, for example, has recently lengthened shopping hours."[16] Given the mixed readings in the marketplace, it is hoped that the

new consumer income tax cuts will spur consumer spending in the retail sector justifying the recently incurred increases in rent. Regardless of whether this happens or not it is expected that secondary locations especially outside of the urban zones will fare poorly.

Achieving high yields within Germany's main real estate markets will be very difficult given the liquidity of the markets and the high valuations in this sector at the present time. In order to obtain superior returns funds will have to delve into secondary locations taking what would at this time seem an unacceptable level of risk. Financing for these types of deals will be difficult to obtain in that banks and lending institutions are reluctant to enter these markets thereby pushing up the cost of debt and increasing the likelihood of default with a downturn in the market. From a lending perspective retail development is seen as less attractive than office development due to the shorter lease terms for non-anchor tenants.

Industrial

The industrial sector of the German economy grew by an impressive 5.1% in the year 2000. Given that industrial production contributes to approximate 30% of GDP this increase has had a significant impact on the German economy. Most importantly it has had a very positive impact on the industrial real estate sector. Most industrial real estate is owner-occupied but due to the peak in industrial production the industrial leasing sector is beginning to expand. Some corporations are placing unneeded property and land into the marketplace, but most of it tends to be of a low quality. Much of this growth in demand is due to the logistic sector. "When the European Common Market was established on January1, 1993 cross border barriers to the

movement of goods were removed, eradicating the need for national distribution centres in individual countries."[17] This led to the development of regional hubs for the distribution of goods within the EU.

The type of inventory useful for this sector needs to be located close to main forms of transportation, this includes truck roads, rail lines, and water networks. There is a demand for the development, which could provide high yields for a relatively small amount of risk, of modern properties that would exceed the current average size and that would be equipped with up to date facilities and equipment. New space of this description has been quickly absorbed into the marketplace but despite this there is little new development in the pipeline. This is partly due to the high price of land and constraints set by the local planning boards giving funds that have the right local connections and access to already permitted projects a great advantage. Given these separate factors rents have experience strong increases. With Euro hovering at low levels in relation to the US dollar it is thought that manufacturing exports may continue to increase leading to further demand for industrial space and a continued upward pressure on industrial rents.

Hotel

The hotel sector has been experiencing a strong recovery since 1998 which can be shown by a series of indicators. There has been a 13% increase in revenue per available room and a 5% increase in average occupancy. The average room rate has also increased by 8%. Hanover received a strong boost to its hotel sector with EXPO 2000. Berlin seems to be one of the main

beneficiaries of this current boom. This increasing demand has been stimulated by the move of the national government from Bonn to Berlin, increased tourism and an increase in corporate conferences.

Property Market Profile - Insignia Richard Ellis

	1997	**1998**	**1999**	**2000** Q2
OFFICES				
Frankfurt - euro m2 p.a.	398	447	484	522
Berlin – euro m2 p.a.	288	294	298	399
RETAIL				
Frankfurt - euro m2 p.a.	1,961	1,961	2,235	1,840
Berlin – euro m2 p.a.	2,206	2,206	2,235	2,331
INDUSTRIAL				
Frankfurt - euro m2 p.a.	61	68	74	92
PRIME INVESTMENT YIELDS				
Office	5.5	5.5	4.9 – 5.5	4.9 – 5.6
Retail	6.0	5.5	4.75 – 5.5	4.75 – 5.5
Industrial	9.0	9.0	7.5 – 8.75	7.5 – 8.75
HOTELS - Frankfurt				
Annual Average Room Rate - DM	196.36	198.4	204.41	N/A
Occupancy - %	65.7	68.1	69.4	N/A

LEASES AND TAXES

Leases

There is no standard lease contract in Germany but there does exist legal guidelines that must be followed in the creation of a lease. The standard lease length is 5 to 10-years which is commonly accompanied with a 5-year option. Rent reviews are generally related to an existing economic index. All clauses relating to the indexing of rents must receive approval from the state bank. One stipulation is that movement in rents due to indexing must move both up and down given the current economic condition. Owners of buildings are normally liable for the repair of the external and common areas of the building and are also responsible for building insurance. Owners usually get reimbursed for external repairs and building insurance by the tenants. Tenants are responsible for the upkeep of the area of the building that they have under contract. There is no obligatory method of measuring the size of a leased space but the normal tends to be a net internal area inclusive of reception and common areas. German rents are generally expressed at a monthly rate and do not include service charges or property taxes, which are normally paid by the tenant. Rent is submitted at the beginning of the month and there generally exists a three-month deposit. Leasing fees range from 1.5 to 3 months rent and are generally paid by the Lessor. Selling costs consist of a transfer tax which sits at 3.5%, an agent's fee of 1-3%, legal fees of 0.2-1.5% and a VAT of 16% of the rent. Management cost are based on net rents and sits at 3%.

REAL ESTATE TAXATION SUMMARY – GERMANY- Insignia Richard Ellis

Key Facts

- The rate of tax on income for corporations is 40%, but this is reduced to 30% where the profits are distributed to shareholders. In addition, there is a 5.5% surcharge.

- In addition to federal income, municipalities also levy a trade tax on income. The basis for computing this tax is different to the Federal basis, primarily because 50% of interest on long term debt is added back. The effective rate is between 13% and 20.5% and the tax is deductible for federal tax purposes.

- Deductions are normally available for operation expenses specified including – tax depreciation and interest expenses. Interest paid to a 25% non-resident shareholder may be treated as a dividend where the debt to equity ratio exceeds 3:1 (1.5:1 after 31 December 2001). Higher ratios of up to 9:1 (3:1 after 31 December 2001) may be sustained for certain holding company structures.

- Value added tax (VAT) at a standard rate of 16% may become payable and claimable on property acquisitions. The leasing or sale of commercial office space is tax exempt and any input tax will be irrecoverable, subject to an option to tax rental income such that input VAT is recoverable

- Transfer tax is charged on certain transactions involving direct or indirect real estate sales. It also applies where 95% or more of the share capital in a German company owning real estate is acquired. The rate is 3.5% of a special assessed standard value which will be close to fair market value.

Commentary - Insignia Richard Ellis

- There is annual land tax on real estate in the region of 1% of the assessed standard value.

- Currently investment through a foreign holding company is favoured. The acquisition of assets may enable a step up in the base cost of the underlying assets and the acquisition could be financed by up to 75% debt or even 90% where a holding structure is used.

- The income arising from short term letting of property is taxed as ordinary business income at the full federal rates. A charge to trade tax may be avoided if the company holding the property is regarded as a real estate investment company.

- Generally it is difficult to avoid capital gains tax on the disposal of property interests in Germany, however, the capital gains tax can be deferred by selling shares in a real estate corporate entity through a domestic or foreign corporation.

FRANCE

ECONOMIC OVERVIEW

Economic Background

As in the UK and the US, France also experienced a rapid expansion in their real estate markets during the 1980's. Most of the projects of this period were based on the idea that the French and world economy would continue to expand justifying the speculative nature of a sizeable amount of the investments being made. As the expansion continued French financial institutions became more involved in the real estate sector mostly due to current sector performance as opposed to opportunities that made economic sense in the long run. When the global recession of the early 1990's hit undermining many of the underlying assumptions for these developments the French real estate market was badly affected. For the French this was a shock, "...with 1993 being the first year of recession since the second world war."[18] This led to a wave of defaults on real estate loans and the accumulation of foreclosed properties on the balance sheets of banks and other financial institutions. "In the early 1990s, the recession wiped out more than US$ 75 billion in commercial property values..."[19] The fragility of the French markets was exacerbated by a lack of discipline in the construction underwriting process with banks lending at more than 100% LTV. The French financial institutions which were partly owned by the French government had a very slow response to the crisis partly due to an impending election. The French government attempted to mitigate the crisis by giving financial support to banks so that they could avoid foreclosures and benefit from an eventual economic recovery. The support of these institutions continued until 1995. With market values merely a third of valuations of 1991, the banks and

insurance companies involved realized that a strategy for the disposal of their bad loans and real assets had to be set. US investors were the first to respond to this crisis seeing an opportunity to buy distressed real estate from financial institutions in the same manner that they did during the RTC era. "U.S. investors – mostly investment banks and opportunity funds – were until recently (1998) the main foreign players in the market for distressed real estate assets in France."[20] A majority of the real estate assets and bad loans had been disposed of between 1995-1998 and by year 2000 the sale was mostly over. "Some U.S. investors realized attractive returns in acquiring, restructuring, and selling distressed real estate assets in the U.S. markets earlier in this decade, and now they have hopes of duplicating that success in the French market."[21] The major difference between this period of disposal and that of the US is the lack of efficiency with which the French assets were disposed of. French law unlike that of the UK and the US strongly favour the borrower making the taking of title a very complex process. This coupled with a lack of credible information that was available in relation to the financial state of the economy and assets for sale made it difficult for opportunity funds to assess what they were or should be buying. The US funds responded to this lack of transparency by adopting very rigorous due diligence processes allowing them to make proper assessments of risk and value. In the last couple of years the opportunity funds have been looking for institutional investors as an exit to fully realize their returns. "In Paris, some of the largest deals of 1999 involved risk-averse German funds buying previously "broken" property assets that had been fixed by the U.S. investors who acquired them only two years earlier."[22] As US funds dispose of their assets they are also positioned with newly raised funds to make investments in French real estate looking to take advantage of the structural changes which are underway in Europe.

Current Economic Condition

The French economy accelerated its rate of growth to 3.3% in 2000. This was founded mostly on consumer spending which has been growing consistently at a rate of 2% and on a surge in the export segment of the economy. Much of the growth in consumer spending is attributed to the current decline in unemployment that hit a near decade low of 10.2% in 2000. This increase in job creation is expected to continue allowing for further reduction in unemployment and in turn the continued strength in consumer spending. Income tax cuts also stimulated the current high level of consumer spending and further cuts of 18.3 billion euro are expected over the next two years. The combination of high oil prices and a weak Euro in relation to the US dollar has led to a pronounced increase in inflation. The consumer price index for France more than doubled in 2000 compared to 1999 but has leveled off below the average inflation rate for the EU. The drop in unemployment has been most noticeable in the Ile de France. The levels have dropped to the point where there is considered to be a shortage in labour. This may lead to upward pressure on labour costs that could fuel the current increase in inflation. It is expected that GDP and exports will continue to grow but at a slower rate and that this will continue to positively affect job creation and the reduction of unemployment.

French Economic Profile - Insignia Richard Ellis

	1997	1998	1999	2000	2001
GDP	1.9	3.2	2.9	3.7	2.9
Inflation	1.2	0.6	0.5	1.4	1.2
Consumer Expenditure	0.1	3.4	2.3	3.1	3.3
Short Term Interest Rates	3.5	3.6	3.0	4.3	5.1
Long Term Interest Rates	5.6	4.7	4.6	5.9	6.3
Unemployment (OECD)	12.4	11.8	11.1	9.8	8.8

REAL ESTATE SEGMENTS

Office

The French office market has had strong growth since 1996. The year 2000 was no exception. The absorption rate in the Ile de France was at its highest since 1990 with an increase of 14% over the previous year. This accounted for 2.26 million sq m of office space. Given this high level of absorption there still seems to be a lack of supply in the Ile de France. As a result corporations are moving to secondary locations in the Paris area and are benefiting from cheaper rent. The pattern has been to move into buildings with large vacancies in which substantial renovations are not needed. One aspect of the high absorption rate is the level at which new developments are being pre-let. In 2000 75% of developments which were coming online were pre-let. This is an increase from 60% in 1999. The years 2001 and 2002 look promising with

68% of developments in 2001 already pre-let and 13% of development coming on line in 2002 currently pre-let. This is due to a lack of modern office space. "If you look at the stock of offices currently on the market in Paris, only 3 percent conform to international norms of raised floors and big floor-to-ceiling heights."[23] The availability of quality office product has been greatly reduced due to the strong demand that has been in effect since 1996. The vacancy rate for office in the Ile de France has fallen from 4.2% to 2.0% while the office vacancy rate for Paris has moved from 4% to 1.2%. "The difficulty is in assembling large blocks of office space (more than 20,000 square meters) to meet the needs of major domestic and international corporations and other large tenants."[24] Due to this lack of office supply and the growing demand, rents have been soaring in the Ile de France area. The government has been attempting to stimulate demand in the Parisian suburbs and have been achieving some success in the north. There has been strong rental growth in these areas just outside of the city center due to businesses relocating from the CBD. This is partly due to the high rents in the CBD and the lack of quality supply. In general speculative development is increasing and La Defense is doing very well. It is not expected that increases in office rent will continue at the same rate but over the next couple of years strong growth is expected to continue.

It is felt that high yield investments in the CBD office sector are no longer available without incurring unacceptable risk. German institutional investors have entered the market and the opportunity funds which made their investment earlier in the cycle are now looking for an exit. Development is a possible option however this is prohibitive due to strict planning codes. Another option is to buy a building and attempt to replace the tenants given the strong increase in rents. The latter strategy would not work in the French markets due to leasing laws that favour tenants making it very difficult to roll over leases. The option of following the trend to the

suburbs would be considered too late since all the low-risk high-yield projects have already been taken and opportunity funds have already had enough exposure in these markets.

The markets which have just been discussed are no longer viable options for opportunity funds due to the liquidity of the market resulting in lowered cap rates and the correction of any inefficiencies. An option that is still available for these types of funds are large corporate office portfolios that are being put on the market by companies looking to raise capital cheaply. These large portfolios partly due to their size are of interest to opportunity funds. The number of investors who are able to realistically make a bid is small creating an illiquid environment. With these large portfolios there is also the benefit of leasing back the once owner-occupied building to the original vendor which reduces leasing risk. These portfolios will also allow opportunity funds regional exposure into secondary markets such as Lyon, Lille, and Marseille. MSREF has recently bought a portfolio of buildings from EDF, France's power company, at a price of FF 3.6 billion. This represents an 8.9% cap rate for a group of buildings that are now 100% leased back to EDF for a 6-year term with a 3-year option. France Telecom is currently putting to the market a 650 asset portfolio of office buildings on which MSREF and Whitehall are bidding. There is stiff competition within a small group of funds for this portfolio but again there is a barrier to entry for a portfolio of this size due to the amount of funds required and the need for strong local groups to provide extensive asset management services in order to achieve the required returns.

Retail

Consumer expenditure in France has seen significant increases due to a combination of strong GDP growth, solid job creation and a reduction in income tax. There is very strong demand from

retailers but a pronounced lack of supply. Outside of Paris the secondary cities of more that 150,000 are also experiencing a retail boom. This is due mostly to national and international chains that have decided to set up in these locations. This is occurring mainly in the prime and central locations of these smaller cities. In both the Paris area and in the smaller cities there is a lack of supply of medium to large retail spaces resulting in an upward pressure on rents for this asset type. Even with the growing demand in retail space in the prime locations of the smaller cities the rents that they command are far lower than what is achieved in the prime locations in Paris. Prime rents in Paris can range from FF53,000 – FF55,000 while in the secondary markets the retail rents are in the range of FF10,000 – FF12,000. It is expected that the expanding GDP and current tax cuts will result in an increase in household disposable income. This should stimulate consumer spending which will ultimately drive retail rents upwards. It is thought that Paris retail rents have reached a psychological ceiling and will stabilize, but due to the lack of Parisian retail supply, retailers will continue their move into the secondary market driving rents up in these markets.

Currently the French retail market appears to have few opportunities for opportunity funds. The Parisian markets are very tight and obtaining building permits is very difficult and fraught with pitfalls. There is a dearth of permitted developments that need investment and the option of buying existing developments and changing the tenant mix or increasing rents could be difficult due to the French 3/6/9 leasing structure. The secondary markets pose development opportunities that could yield high returns but these markets are too small in size warranting developments that would not meet the minimum investment requirements for most opportunity funds.

Industrial

The Ile de France area is experiencing an under supply of modern industrial space. This is particularly pronounced in the market for space ranging above the 10,000 sq m threshold. The demand for this type of space is coming mainly from the warehousing and transportation sectors. In general there was an increase in absorption of industrial space in 2000. There are a series of speculative industrial developments in the pipeline which should alleviate this lack of supply. These types of development opportunities are difficult to locate and require more effort to execute than in the US. "Conditions for development of warehouse facilities in Europe vary considerably from those in the United States. Land is more expensive in almost all countries, and gaining the necessary zoning, permits, and infrastructure improvements is far more time consuming. A minimum wait of one to two years before construction is standard"[25] Outside of Paris, Lyon and Marseille are the two most buoyant markets with the Marseille market being very constrained. This is partly due to a lack of appropriate land suitable for industrial real estate development. Developments in the pipeline for the French industrial sector over the next two years amount to 520,000 sq m. It is felt that this supply will ease the current shortage of quality industrial space resulting in only modest industrial rental growth over the next two years.

Possible investments for opportunity funds in the industrial sector can be divided in to two categories, light industrial and logistics. Light industrial generally includes light manufacturing or perhaps pharmaceuticals taking up the majority of the space. These types of developments with tenants that let relatively small spaces tend to be management intensive. They also tend to have higher than average vacancy rates, and can be more susceptible to downturns than other

industrial products with a more solid user base. It is possible in buying a portfolio of these properties, with the right asset management in place, to benefit from economies of scale and higher rents by providing better service thus differentiating the product. This could also lead to greater demand in the market and the lowering of vacancy rates. Again this is more likely with larger portfolio investments that need to be coupled with the right asset management infrastructure.

The other industrial asset type that may be of interest for funds looking for high yields would be large logistics warehouses in excess of 20,000 sq m. There is a shortage of supply of this asset type and appropriate land is relatively inexpensive. The barrier to entry has been the development approval process for land that had industrial zoning, was acquired and land banked during the 1991-1995 period and is now being put to use. The construction and market risks of these developments are not high in that they use simple and inexpensive construction types and are quickly completed. Large investors and developers have entered this market with German institutional investors, looking for core assets, seen as the exit.

Hotel

The Parisian hotel sector has in the last year had increases in its occupancy levels and average room rates have also increased by 5% over the previous year. This has led to an increase in the revenue per available room. The Parisian market has many quality hotels which came online in the year 2000. This includes the Sofitel Bercy, the Zac de Bercy, an extension of the Sofitel Paris Saint-Honore, the Pierre et Vacances 188 room serviced apartments and the George V. The Sol

Melia group refurbished two hotels in the core of Paris. Expected in the next two years are a 205 room Park Hyatt and a 156 room Marriott. The Parisian occupancy rates are considered to be the highest for major cities in Europe and are expected to be maintained.

Property Market Profile - Insignia Richard Ellis

	1997	**1998**	**1999**	**2000** Q2
OFFICES - Paris				
Golden Triangle - euro m2 p.a.	457	480	518	732
La Defenses – euro m2 p.a.	275	289	305	458
RETAIL				
Paris - euro m2 p.a.	5,490	6,100	6,871	8,397
INDUSTRIAL				
Paris - euro m2 p.a.	53	53	53	84
PRIME INVESTMENT YIELDS				
Office	6.0	5.5	5.5	5.5
Retail	8.0	6.0	6.5	6.5
Industrial	12.0	10.5	10	10
HOTELS - Paris				
Annual Average Room Rate - DM	402.3	459.55	465.14	N/A
Occupancy - %	75.8	78.0	77.7	N/A

LEASES AND TAXES

Leases

French lease structures generally referred to as 3/6/9 normally run for 9 years with a 3-year option for the tenant. Owners can end leases at the end of 9 years at a cost in contrast to tenants who can terminate leases at the end of every 3-year phase. Leases are indexed to increases or decreases in the cost of construction and are adjusted to the market rate at the end of the lease terms. Owners must pay for insurance and upkeep of external and common areas, which is then reimbursed by the tenant. Tenants are responsible for the upkeep of the area that they are directly leasing. Rents are based on leased areas and common spaces, do not include services charges and payment is made at the beginning of each quarter. The payment of real estate taxes is negotiated between owners and tenants. A deposit equal to 3 months of rent is standard and may be accompanied by other guarantees. Leasing fees can be as high as 30% of the first year of rent and payment is usually shared between the Owner and tenant. There is a value added tax of 20.6% on the sale of a building within 5 years of completion and a fee of 19.9% on any subsequent sale. Stamp duty has dropped from 18.6% to 4.9% in 1998 and the brokerage fee for the sale of a building ranges from 1-3% of the buildings value. Management fees which are normally paid by the tenant are in the range of 2-4% of annual rent.

REAL ESTATE TAXATION SUMMARY – FRANCE - Insignia Richard Ellis

Key Facts

- Rate of tax for resident corporations and French branches of foreign resident corporations is 33.33% plus a 10% surtax. This gives an effective tax rate of 36.66%

- Where the ultimate shareholders of an investment in French real estate are resident in a deemed tax haven country the French company owning the property is liable to pay an annual 3% real estate tax based on the market value of the property.

- Deductions are normally available for operating expenses, collection costs and interest expense

- There is a maximum debt to equity ratio of 1.5:1 for loans from direct shareholders. In addition, the rate of interest should not exceed the average published rate on private bonds.

- Value added tax (VAT) at a rate of 19.6% may become payable on property acquisitions.

- Since 1 January 1999, transfer tax is charged at a rate of 4.8% on direct real estate acquisitions or 4.89% on the acquisition of the shares in a real estate company.

Commentary - Insignia Richard Ellis

- Income arising from short term letting of property is taxed as ordinary business income at full income tax rates.

- The capital gain on a disposal of real estate or shares in a real estate company is taxable in France.

- Tax depreciation is available on commercial an industrial properties at a rate of 2-5% on a straight line basis.

- The approach to taxation planning should focus upon the projected cash flows arising from the acquisition and not merely the structural aspects of the transactions.

- It is often difficult to increase the level of debt allowable for tax purposes by means of an internal reorganization. Debt should normally therefore be introduced into the structure as part of the acquisition process.

- The impact and timing of the incidence of VAT need to be properly recognised to avoid unnecessary liabilities arising.

ITALY

ECONOMIC OVERVIEW

Economic Background

The most generally accepted portrayal of the Italian real estate markets is that they lack transparency and that the political system lacks continuity "... as a country, it has lacked stability and substance. From 1947 to 1993, it had 51 governments."[26] creating caution on the part of international investors. During the global recession of the early 1990's the Italian real estate markets were largely obscured by a lack of credible information and imperfections in the markets ability to value property. In some respects the opacity of the markets reduced the effects of the recession by hiding the problems but at the same time it also prolonged inherent problems and discouraged liquidity that could have been created by foreign investment. During this period there did not seem to be the same financial debacle as evidenced in the UK, France, Germany and the US. Most of the commercial real estate in Italy is owned by the largest financial institutions or government owned corporations who do not rely to the same extent on the use of debt in the capital structure of their real estate holdings. These assets tended to be debt free, owner occupied buildings which were held due to their utility or their hedging effects against inflation. That said there are still some properties which were over leveraged and foreclosed upon. Since the late 1990s these portfolios of loans have been coming onto the market. "An investment opportunity that is attracting particular interest is the acquisition of non-performing real estate loans from Italian banks, which, like banks in other industrialized countries, were left

with large portfolios of such loans due to the global economic downturn of the early 1990s."[27] During the 1990's opportunity funds had very limited exposure to the Italian real estate markets discouraged by its lack of transparency. It was felt that "Italy's desire to join the EMU would move the government to initiate large-scale sales of state property in order to raise cash for the reduction of public sector debt. State properties include large housing estates, as well as office buildings, industrial properties, hotels, and other assets."[28] These portfolios have recently been put on the market and opportunity funds have brought some liquidity by doing purchase lease-back deals with the Italian government and other large institutions.

Current Economic Condition

The Italian economy grew by 2.8% in the year 2000 and was mostly stimulated by domestic demand and increases in exports. This has led to an increase in industrial production that has Italy at its highest use of industrial capacity since the early nineties. Employment grew by 1.3% over the previous year. Italy has been making significant progress in relation to unemployment but still has an unemployment rate above the EU's average. There is a big divide between unemployment rates in the north and south with northern Italy experiencing an employment rate of 4.5% and in isolated areas shortages of labour. The combination of high oil prices and the weak Euro and an exchange rate depreciation for the Lira have led to an increase in inflation. At this point inflation in Italy is hovering at 2% while the EU average is stable at 1%. Interest rates are expected to increase and domestic demand is expected to drop but this is expected to be counterbalanced by an increase in exports. This should result in the growth in GDP remaining basically the same as the previous year.

Italian Economic Profile - Insignia Richard Ellis

	1997	1998	1999	2000	2001
GDP	1.8	1.5	1.4	2.9	3.1
Inflation	1.7	1.8	1.7	1.9	2.7
Consumer Expenditure	3.0	2.3	1.7	1.5	2.2
Short Term Interest Rates	6.9	5.0	3.0	4.3	5.1
Long Term Interest Rates	6.9	4.9	4.7	5.6	6.4
Unemployment (OECD)	11.8	11.9	11.5	11.0	10.5

REAL ESTATE SEGMENTS

Office

The Italian office market was very buoyant in 2000 with most transactions taking place in Milan. There has been a pronounced increase in demand for office space due to both international and domestic concerns. The supply of new office space did not keep up with demand creating a shortage of space in some areas. The only new developments on the horizon are large high-end modern schemes but these projects have yet to be delivered. The central Milanese business district has had a lack of development due to a lack of appropriate sites and restrictive government planning policies. This lack of quality office supply in Milan has given the secondary markets a boost with small and medium size developments doing very well. "Italy has

a lot of commercial property that people don't want any more. Much of it was forced on the banks in return for bad debts. It is a perfect scenario for predatory foreign investors looking for bargains."[29] Most of the modern office supply has been through the refurbishment of older buildings and have tended to be located outside the center of the city, generally to the north or south.

Alternative office products are doing very well including the serviced office space with 100% occupancy rates in Milan and Rome. This may change as new inventory is brought into the marketplace. Since the early nineties the Italian absorption levels have been increasing. Supply of office space over this period has not been able to keep up and this has resulted in the current low vacancy rate of 3.5%. The development pipeline over the next two years will exceed what came online in 2000 but is not focussed on the Milanese central business district. This decentralization of new office inventory may further boost the office markets in the secondary areas. It is thought that rents over the next two years will increase due to the obvious mismatch between supply and demand. This is expected to have most impact in the traditional downtown business districts. In Rome the same situation may not exist due to an expected increase of government owned real estate that will hit the marketplace.

In order to achieve the necessary returns without undue risk in the Italian office sector, opportunity funds must partner with local developers who can guide them through the local planning maze and deliver the product. These developments tend to be speculative in nature due to rapidly rising rents. Pre-letting can greatly reduce the cash flows coming from a project if the developer is locked in to low rents relative to the marketplace when the product is delivered. Tenants are well protected by lease contracts which are normally 6 years with a 6 year option. Normally a developer will do a mix of pre-letting and speculative to hedge against market risks.

The lack of development is due to a slow moving or stationary bureaucracy that has not changed the planning codes to reflect the change of Milan from an industrial to a service economy. There are also corporate office portfolios that are being put on the market. Peabody has recently bought a portfolio from ENA, an insurance company, and Whitehall has just acquired a portfolio from Immobolinnere ENI, a power company. Combined these two transactions exceed US$ 1 billion in value.

Retail

The retail sector is seen as Italy's strength and has received much attention by international retailers. It is a sector that has not been consolidated and is still made up of a series of smaller entities. There is a current movement towards consolidation with some houses looking to achieve economies of scale by increasing market share. Consumer expenditure especially in the industrialized north has been increasing which has resulted in a boom for retailers. This has attracted more foreign concerns and is one of the main drivers for this sector. There is also a loosening of regulatory red tape for retailers allowing for an increase in demand. "In Italy, for instance, a 1994 law simplified authorization procedures for opening, expanding, or transferring retail businesses. Application for a retail license must now be approved or rejected within 60 days of submission; a lack of government response within that period means that an application is considered accepted."[30] Quality retail space in downtown areas has become very difficult to find and are leased only at a premium. Traditional Italian houses such as Armani and Gucci have had taken central locations in Milan. This increase in demand and almost no new supply in the pipeline have led to dramatic increases in rents. This rise in rents is considered a trend that will continue due to the predicted increase in household consumption. Italy has also changed aspects

of its retail leasing process allowing for a more flexible relationship between owner and tenant. "It has liberalized the so-called fair rent law to allow the landlord and the tenant to negotiate the price and certain key terms of a lease contract. And the licensing process for most types of retail business has been dramatically shortened to only 30 or 90 days, depending on the size of the business."[31] Alternative forms of retail are starting to take hold in the form of factory outlet centres. Three FOC's have opened in Milan, Turin and Genoa. These are the first of the kind and their sales have been doing very well. There is expected to be an increase of this type of retail centre; a second phase is expected to come online in the near future. In relation to shopping malls the most activity is in Rome where two major malls are anticipated to be completed by 2003. "Some of the biggest names in the development business in Europe are following the example of U.S. development practices – specially, the development of retail projects with multiplex cinemas as their centerpiece and food courts as an activity generator – to redevelop city centers."[32] These two malls will be amongst the largest in Italy ranging in the area of 100,000 sq m.

The Italian retail markets currently is very liquid. In order for opportunity funds to achieve superior returns they will have to engage in development. The two segments of the retail market that seem poised to produce these types of return are the shopping mall and urban entertainment development markets. "The idea behind the UEC is to integrate retail shops and entertainment attractions to provide an all-round experience designed to keep visitors in the center for as long as possible."[33] This combination of retail and leisure is a new product type for the Italian market and has not been tested through a full cycle. The main concern is the exit strategy and whether there will be a market for this type of product; to date none has sold. Again with this product

type the barrier to entry lies with getting approvals and finding a qualified partner with local expertise and an understanding of this product type.

Industrial

Italy is experiencing a dearth of quality modern industrial facilities that have easy access to main infrastructure corridors. This is partly due to a lack of interest by developers to engage this product type. Most industrial facilities are owner occupied leaving the market for leasing industrial space very limited. The logistic sector in particular is finding it hard to find spaces with adequate accommodations in the 10,000 sq m range. Storage and distribution are the two segments of this sector that have demonstrated sustained demand for leased industrial space. "In fact, more than two-thirds of warehouses in several core industries are outsourced to companies with expertise and information systems tailored to optimising warehouse, logistics, and supply chain performance."[34] Again this demand is not being fully met. Due to Italy's growing economy it is expected that demand for industrial space will continue. As a result it is expected that there will be modest rent growth over the next two years. Space of the 500 – 1,000 sq m range will not move in price. With this state of price equilibrium any substantial increase of inventory especially in the form of large warehouses would have the effect of reducing industrial rents.

For opportunistic investment in the Italian industrial sector these logistics centers may fulfil the criteria of achieving high returns for a relatively low amount of risk. There is a strong demand for this product type coupled with an inability to match supply due to barriers created by the

government and a lack of appropriate land. There are very few of these products currently in place and existing facilities are generally obsolete.

Hotel

Occupancy levels in the Italian hotel sector are very high especially in Rome which has occupancy levels in excess of 80%. Due to the tightness of supply the market room rates have been increasing at a rate that is faster than inflation. Many projects came online in 2000 including the 500-room Hilton at the Malpensa airport, the 130-room Rocco Forte, the 200-room Jolly Hotel, and the 257-room Melia Roma Aurelia. In spite of this flood of new inventory it is still expected that the hotel sector will be able to maintain its profitability. Florence, Milan and Venice have shown strong performances mostly due to the buoyant Italian economy and should be able to maintain these positive results given that there is no new hotel inventory in the pipeline.

Property Market Profile - Insignia Richard Ellis

	1997	**1998**	**1999**	**2000** Q2
OFFICES				
Milan - euro m2 p.a.	192	217	256	281
Rome – euro m2 p.a.	216	184	245	243
RETAIL				
Milan - euro m2 p.a.	878	930	1,033	1,020
Rome – euro m2 p.a.	697	775	826	1,020
INDUSTRIAL				
Milan - euro m2 p.a.	52	59	62	66
PRIME INVESTMENT YIELDS				
Office	6.0	5.5	5.25 – 5.5	5.50
Retail	6.5	6.0	4.50 – 5.0	5.0
Industrial	10.0	9.5	8.5 – 9.0	8.5 – 9.0
HOTELS				
MILAN				
Annual Average Room Rate - DM	272.92	251.08	366.39	N/A
Occupancy - %	67.4	70.0	67.4	N/A
ROME				
Annual Average Room Rate - DM	280.69	308.51	327.66	N/A
Occupancy - %	78.6	79.4	76.7	N/A

LEASES AND TAXES

Leases

Italian leases are standardized and have a basic structure of an initial 6-year term with the option for an additional 6 years. There is generally no review of rents during the first two 6-year terms. During the lease term rent is indexed to 75% of Italy's inflation index and an adjustment either up or down is assessed at the end of the term given market rates. Unless the owner does a full renovation or needs the building for its owns use the tenant cannot be evicted. The owner is generally in charge of external repairs and upkeep of common areas while tenants are responsible for utilities and upkeep of the area they are leasing. Rents are based on gross internal area making the efficiency of the building an important issue when calculating effective rents. Rents normally do not include service charges and are paid at the beginning of each quarter. The equivalent to 3 months rent is the standard deposit for a commercial lease and the owner normally pays property taxes. Leasing fees are in the 12-15% range of annual rent while brokerage fees for the sale of a property is in the 1.5-5% range. In order to avoid a 20% value added tax the sale of most buildings is achieved by purchasing shares in the company which owns the asset. Management fees normally run in the range of 5-7% of annual rent.

REAL ESTATE TAXATION SUMMARY – ITALY- Insignia Richard Ellis

Key Facts

- Resident and non-resident companies with a permanent establishment in Italy investing in real estate are chargeable on their income and gains at a corporate tax rate of 37% (IRPEG). Regional tax (IRAP) is due at a rate of 4.25%. This is not deductible for IRPEG purposes.

- An annual real property tax is imposed by municipalities based on the cadastral value of the property at rates of 0.1% to 0.7%.

- Deductions are normally available for direct operating expenses and interest where the property is used commercially. There are no fixed thin capitalisation rules and interest is normally fully deductible regardless of debt/equity ratios. Interest expense is not deductible for IRAP purposes.

- Property disposals and rents of business premises or land available for building purposes are generally subject to VAT at a rate of 20% which may be recoverable.

- Registration tax at a rate of 77% is levied on documents conveying title. A further 3% is payable as cadastral and mortgage taxes. However, if a transaction is subject to VAT, registration tax is fixed at ITL 250,000. Cadastral and mortgage taxes follow similar rules.

Commentary - Insignia Richard Ellis

- Transactions relating to real estate between related parties must be at arm's length. Anti avoidance provisions exist which may lead to the disallowance of any tax benefits which arise.

- Property held by construction companies is treated as trading stock and sales proceeds as trading income.

- Residents and non-residents with a permanent establishment where the property is used in the conduct of a business in Italy, are taxed on income derived from the real estate. A deduction for depreciation of commercial buildings (usually at a rate of 3%) may be taken. On sale, the capital gain may be spread and taxed in up to five yearly installments provided that the real estate had been owned for at least three years prior to sale.

- Real estate owned in the other circumstances is taxed on an imputed cadastral basis determined by the Ministry of Finance. Direct and actual costs including interest and depreciation are not deductible from taxable income. For rented residential buildings, the taxable income is determined as the higher of the cadastral basis income and the accrued rental income reduced by a 15% flat deduction for costs.

UNITED KINGDOM

ECONOMIC OVERVIEW

Economic Background

In some respects the factors which led to the US boom and eventual crash also contributed to the over heating of the UK property markets during the mid to late 1980's and decline during the early nineties. The deregulation of the US financial industries led to an expansion in international US activity much of it directed at London due to its position as one of the main financial centres and the gateway to Europe. One can list "...its time zone, its liberal regulators and low costs as reasons why London acts as a central hub for the world's financial markets."[35] This led to a great demand for office space in the London markets, particularly high-end office space in London's financial core, the City. Supply of new office space was not able to keep up with the new internationally induced demand partly due to planning regulations resulting in dramatic increases in modern office rents, "rents increased by 108% between 1984 and 1988".[36] In response to the strong demand for office space in the city and the extremely rapid rental growth being experienced the government loosened their planning provisions. This in combination with the availability of financing from both the US and German debt markets led to an unprecedented construction boom. Most of this development was directed at the City changing the face of London's financial district, "Between 1989 and 1992, 1.79 million square feet of office space were completed in the City. Over that period, total stock increased by 19%".[37] An added boost to this already robust expansion was the influx of capital from Japan looking for prestigious

acquisitions partly due to the strength of the Yen. At the height of this expansion there was an economic contraction that was felt worldwide. This worldwide recession led to a substantial drop in office demand accompanied by a dramatic drop in office rents. This forced many developments that had been over-leveraged into bankruptcy and filled the balance sheets of UK banks with foreclosed properties and bad loans. Many banks at the beginning of the crisis held onto their assets not wanting to dispose of them in such an unfavourable market for unacceptably high discounts, but eventually, as the markets began to recover and as their resources were beginning to dwindle began to sell portfolios of property and loans. The main purchasers of these properties were US opportunity funds and German institutional investors. They were particularly interested in UK assets due to the long leases, normally 25 years in length, which were associated with the assets that they were acquiring at a discount. This allowed for them to maintain rents at the unprecedented levels of the early nineties even though current market rents were much lower, "Taking into account the longer rent-free period, real effective rents in 1993 were just 32% of their 1975 value."[38] The combination of the depreciation of asset values and the maintenance of unusually high rents allowed opportunity funds to achieve superior returns and led to a further increase in the ownership of UK commercial real estate by foreign companies, "the overseas ownership of City office property has increased from around 3% in 1985 to around 18% in 1997."[39]

Current Economic Condition

The UK economy grew at a rate of 3% in the year 2000 mostly due to an increase in household consumption and a decline in household savings. There has been strong demand for UK products

in the US despite the resilience of the Pound. The Sterling is at its highest level since the mid-1980's hampering the manufacturing sector of the economy and making it more vulnerable to competition from other EU members. Unemployment dipped to 5.5% and is expected to remain at this level. This is the lowest rate of the leading European economies and has been achieved without a substantial increase in inflation, but has resulted in a 6% increase in wages. The growth in GDP is expected to slow down despite an expected increase in industrial output. This is due to the strong ties between the UK and North American economies and the impending slowdown in the US economy.

United Kingdom Economic Profile - Insignia Richard Ellis

	1997	**1998**	**1999**	**2000**	**2001**
GDP	3.5	2.2	2.1	2.9	2.3
Inflation	3.1	3.4	1.6	2.9	2.9
Consumer Expenditure	3.9	3.2	3.9	3.2	2.6
Short Term Interest Rates	6.8	7.3	5.4	6.6	7.0
Long Term Interest Rates	7.0	5.5	5.1	5.7	6.1
Unemployment (OECD)	7.0	6.3	6.1	5.6	5.3

REAL ESTATE SEGMENTS

Office

The UK's strong economic growth has led to a very strong year for the office market. Central London which constitutes "200 million or so square feet of space"[40] recorded its highest level ever of absorption even though absorption dropped by 1/3 in the third quarter. Vacancy rates are hovering at 2.6% which is the lowest level since 1988. Of this very low vacancy rate only 13% existed in new projects. With this low vacancy rate there is also a relatively small pipeline for UK office space when compared with the boom of the late 1980's. There is currently 1.3 million sq m in the pipeline one quarter of which is speculative and one third of which is located in the City. This combined with an increase in demand has resulted in a very healthy increase in rental growth. The West End of London which has demonstrated the most growth in rental values grew at a rate exceeding 30% over the previous year. This was due to a lack of available land for development and very strong demand. It is thought that demand for office space in London will ease in 2001 but that the market will still experience some rental growth. The secondary markets had a good year with high absorption rates and a 15% drop in vacancy rates. There is a very strong demand for office space in the 10,000 sq m range in the city of London. The demand is being satisfied mostly by speculative development that is coming on line. At this point in time it is thought that the UK office markets are approaching a comfortable equilibrium.

At this stage of the UK real estate cycle and the fact that these markets tend to be more efficient than on the continent, it is difficult to detect where opportunistic investments may lie. At this point in London there does not seem to be the possibility for much rental growth. The fact that

the office market is thought to be close to equilibrium and that cap rates have bottomed out suggests that attaining high yields without excessive risk will be difficult to achieve. The one area where there may still be some room for opportunity funds to make successful high yield investments could be in the arbitrage of taking public UK real estate companies private, "...the divergence between the performance of the direct property market and the quoted real estate sector has led to a major shake out. The deep discount between net asset values and share prices has prompted a wave of mergers, acquisitions and privatisations..."[41] The timing for these types of opportunities may be right since the strength of the market will allow a quick disposal of assets.

Retail

Retail construction is still very strong but has experienced a 10% drop from the previous year. This still amounted to 2 billion Euros of construction. There has been a noticeable shift in schemes moving from out of town locations to central locations. Centrally located schemes doubled in the last year. "The urban leisure idea that has captured the market's imagination most is the 450,000-square-foot Trocadero on London's Piccadilly Circus."[42] This was due to a combination of changes in planning regulations and a shift in emphasis by retailers. The retail market was buoyed by a 4.3% increase in sales. This increase was taken up mostly by smaller operations while the larger established retailers are losing market share. The large clothing and fashion retailers have not been able to maintain profits even given the increases in consumer spending. In an attempt to address this problem they have been closing locations and putting their space in the marketplace. The discount/value segment of the retailer sector has been quick to absorb the newly available inventory. Over the year 2000 growth of rent for retail space has

slowed from 5.7% at the beginning of the year to 3.9% in December, with southern England experiencing the slowest growth of 3.2%. Retail warehouses had the fastest rate of rental growth of 5% while shopping malls had the slowest growth of 2.9%.

Given the maturity and slowing in growth of the UK retail market opportunities for high-yield investment are thought to be scarce.

Industrial

Demand for industrial space in 2000 was the same as in the previous year. This amounted to 4.1 billion Euros in construction. There was a slowdown in manufacturing which was partly brought on by the strong pound resulting in a 14% decrease in schemes for new construction of factories. This was counterbalanced by a 23% increase in new development for warehouses. It is expected that in the year 2001 demand for industrial space will decrease. Even though the manufacturing sector was on the rise at the end of 2000 is it felt that exports will begin to wane in the face of the impending US slowdown. Much of the existing capacity for industrial production is not being fully utilized. In light of these changes in the market rents for industrial space have still been increasing at a healthy rate with an average growth rate of 4.8%. Industrial zones in the London area have benefited the most with a growth rate of 8% while distribution has increased by only 3%. The Heathrow industrial showed the best increase in rents achieving a growth of 8.7% over the previous year.

Opportunity funds will have difficulty finding investments in this sector due to declining industrial rents and the maturity and efficiency of the markets.

Hotel

In the year 2000 revenue per available room in the secondary UK hotel industry experienced a drop after years of continual growth. Occupancy levels also dropped while the average room rates increased. The London market did much better with an increase in occupancy over last year and an increase in average room rates greater than inflation. This combination of factors led to a rise in revenue per available room. London's growth rates have contributed to it having the highest revenue per available room of Europe's major cities. Many new hotels opened in 2000 including Ian Shrager's Sanderson Hotel, the Great Eastern, the MyHotel, and the 50-room addition to the Mandarin Oriental at Hyde Park. In 2001 many luxury hotels are expected to open including the Sofitel, the Pall Mall, and the Hilton Trafalgar.

Property Market Profile - Insignia Richard Ellis

	1997	**1998**	**1999**	**2000** Q2
OFFICES				
West End - euro m2 p.a.	802	882	997	1,222
City – euro m2 p.a.	737	802	852	925
RETAIL				
Oxford St - euro m2 p.a.	7,618	7,618	7,240	8,941
INDUSTRIAL				
Thames Valley - euro m2 p.a.	146	156	187	207
PRIME INVESTMENT YIELDS				
Office	5.0	5.5	5.0 – 5.5	5.0 – 5.5
Retail	4.5	4.25	4.75	4.75
Industrial	7.0	7.0	6.25 – 6.5	6.25 – 6.5
HOTELS - London				
Annual Average Room Rate - DM	369.98	405.17	406.39	N/A
Occupancy - %	82.5	80.7	80.9	N/A

LEASES AND TAXES

Leases

UK leases are usually 25 years in length, but since the recession of the early 1990's lease terms have shortened and it is not unusual to see leases in the 10-15 year range. Rent adjustments occur every 5 years, usually only move upwards and are based on market rates. Renewal of leases is normally the option of the tenant unless the building is to be fully renovated or is needed for use by the owner. Unlike leases on the continent tenants are normally responsible for external, internal repairs, insurance and property taxes. Rents are based on net internal area reducing the significance of building efficiency from a tenant's perspective and do not include service charges and property taxes and are paid at the beginning of each quarter. A deposit of 1 years rent is standard. Leasing fees are in the 10-15% of annual rent range with the fee split between owner and tenant. On the sale of the building there is a stamp duty of 2.5%, a brokerage fee of 1% of the buildings selling price, legal fees of 0.5% and a 17.5% value added tax on brokerage and legal fees. Management fees range from 2-4% of annual rent which is partly reimbursed by the tenant.

REAL ESTATE TAXATION SUMMARY – UNITED KINGDOM - Insignia Richard Ellis

Key Facts

- Corporation tax rate is 30% (lower rates apply for small companies). Basic income tax rate 22% (individuals maximum rate is 40%)

- Resident corporations and only those non-resident corporations with UK trading branches pay corporation tax on rental income. Individuals, trustees and other non-resident corporations pay income tax on rental income.

- Deductions normally available for operating expenses, collection costs and interest expense provided that amounts paid to connected entities can be shown to be calculated on an arm's length basis.

- Resident corporations, trustees and individuals pay taxation on capital gains at the above rates after taper relief/indexation. Higher rate tax paying individuals who hold business assets may only pay an effective 10% rate of tax on capital gains if they hold their business assets for 4 years or more. Non-residents are generally not subject to UK tax on their capital gains.

- Value added tax (VAT) at a rate of 17.5% may become payable on property acquisitions but is often recoverable by the payer.

- Stamp duty on real estate acquisitions is charged at rates up to 4% for disposals in excess of 500,000 pounds. Lower rates apply below this.

- Local property taxes (uniform business rates) are payable by occupiers of commercial properties.

Commentary - Insignia Richard Ellis

- Taxation treatment is dependent upon whether real estate is acquired as an investment of as a trading asset.

- Non residents, individuals and corporations can benefit from exemption of capital gains on disposals of investment properties.

- Although no fixed depreciation rates apply to commercial and retail properties, it is often possible to negotiate that a significant proportion of the expenditure relates to a buildings plant and machinery content which can be depreciated for tax purposes at 25% per annum.

- The approach to taxation planning should focus upon the projected cash flows arising from the acquisition and not merely the structural aspects of the transaction.

- The taxation consequences of transactions need to be factored into the negotiation process rather than being addressed after the price etc have been agreed.

- The impact and timing of the incidence of VAT need to be properly recognised to avoid unnecessary liabilities arising.

5. CONCLUSION

On investigating what main issues opportunity funds will have to address in their pursuit of superior returns in real estate investments in Europe I felt that it was necessary to define what should be the basic tenets of any opportunistic investor given the successes which have been achieved in the past whether it be in the US or Europe. From discussions with industry players it appears that the basis of the opportunity funds' ability to outperform the market is related to self-interest, smarter management, low risk for high yield scenarios, and a contra cyclical focus.

A key element in the success of opportunity funds has been the incentive for management to perform by having their funds in the investment pool. This has reduced possible agency conflicts of interest by aligning the interests of management and shareholders in the maximization of shareholder value. Self interest in management can engender discipline and good intentions in relation to shareholder value by diminishing agency issues but this will only remain a well-intended sentiment without the other factors mentioned.

The ability to assess risk is the key to smarter management when it comes to opportunistic investment. A well developed risk assessment team allows these funds to enter into environments that most investors would avoid because of their inability to understand and control inherent risks. In many cases the inability to assess risk can lead investors to be too conservative when valuing a deal, resulting in missed opportunities for quality investments. Having good risk assessment skills should not imply that these funds feel comfortable entering into risky investments but that they are able to make more informed decisions that lead them to invest in

deals that seem risky to most but which on analysis are in fact very sound. The amount of research done in relation to each deal tends to be greater both in terms of allocation of personnel and time. Opportunity funds in general have few positions given their size and as a result can expend far more resources and perform greater due diligence for each deal. In general European companies do not engage in the same amount of research when it comes to acquisitions of real estate and rely much more on personal contacts.

In the European context it will be even more important for US funds to conduct thorough due diligence given the different customs and laws as one moves from country to country within the EU. A prime example is the differences that exist in relation to leasing contracts. Leasing contracts in the UK in general are the longest and most stable of the four countries surveyed while France with its 3/6/9 structure is considered to be the most volatile. This allows for different opportunities depending on whether a fund is in the acquisition or disposal phase and at what stage the tenant is at in their lease term. While UK leases allow for a stable cash flow it also discourages the acquisition of properties that have tenants that are too early in the lease term. The French model by virtue of its structure has a higher amount of risk due to 3-year options which are given to tenants but this also allows for more opportunities due to the possibility of tenant roll-overs.

When considering the assessment of risk and the need for extensive due diligence no where is it more important than in the purchasing of distressed debt portfolios. Part of the reason that US opportunity funds were among the few groups interested in the purchase of these types of portfolios was the daunting amount of due diligence that was necessary to make an assessment of

risk and value. Within the European context US funds have insisted and should continue the practice of relying on their own primary research down to the asset level taking advantage of their expertise in this area which they developed during the RTC era.

Another factor which allows opportunity funds to have better management is their reliance on the best local talent in the respective market they are considering. This use of local JV partners in a market where they do not have local expertise allows them to fully take advantage of local incentives and idiosyncrasies in the marketplace. As the amount of funds raised for European high yield investment increases the importance of loyal top quality contacts and joint venture partners will greatly increase. It is these local groups that allow US funds to find opportunities and successfully navigate the relationship based governmental and business communities. Without these relationships foreign funds will find themselves in a public arena attempting to locate quality deals among opportunities that have been discarded by their better connected competitors.

In essence the idea of smarter management has to do with gaining access to information and opportunities and being able to make sound decisions in relation to risk and value. Funds that are not drawing on expertise acquired during the RTC era and that do not have solid relationships with top local players will be at a disadvantage.

The central issue of achieving high returns with low associated risk is the flow of deals from acquisitions to disposals as markets move from illiquid to liquid states. In attempting to achieve high yields opportunity funds have in one way or another relied on opportunities being created by some type of barrier to entry which reduces how competitive the market is in relation to the type of products they are acquiring or producing. This illiquidity can be produced by many different factors ranging from economic cycles, government barriers, specialized knowledge bases and services, to the size of the deal. In any of these cases the lack of players who are able to take advantage of existing deals puts the well positioned and well funded opportunistic investor in a position to reduce risk by getting whatever deal they are pursuing at an initial discount. The basic procedure for opportunistic investment is to buy low due to illiquidity, add value if necessary, and sell high into a liquid market. In order to achieve this initial discount opportunity funds need to avoid an auction like process which can be created when there is an abundance of capital and instead rely on negotiated transactions. They then also have to be mindful of the environment into which they attempt to dispose of their assets choosing ones which are liquid allowing them to achieve full market values. The ability to realize the appreciation in value of an investment by disposing of the asset at the right time is a key strategy to opportunistic investment in real estate. A disposal strategy is important because it is difficult to achieve the mandated 20% leveraged returns from cash flows alone. Investors must time their investment so that within the shortest period of time an asset can be repositioned, stabilized, and traded into a liquid market. Time is of the essence in that the leveraged 20% return is an IRR which means that the residual value of the property has less and less impact on the IRR over time.

Given the current liquidity of the European real estate markets finding opportunistic investments will be more difficult than it was during the RTC era in the US or during the last illiquid period in Europe during the mid 1990s. Opportunistic investors will have to rely on niche environments which are capital starved.

There are three main environments where these types of deals will be found. The first will be off-market deals which the majority of opportunity funds would consider to be too small for consideration and which most local investors would consider to be too large. The scarcity of investment for these types of deals allows opportunity funds to avoid an auction process putting them in a better position to negotiate an initial discount. The quality deals for this level of investment would be grade-A buildings which have a problem, big broken buildings, in secondary locations. As stated earlier there is demand for quality modern office space that due to the lack of supply in the prime European CBDs is beginning to move to secondary locations on the outskirts of Europe's main cities. The danger of entering into too many of these smaller deals is that a fund could find its resources for conducting due diligence spread too thinly. A benefit of these smaller deals is that a buyer is more readily found when it is time to dispose of the asset.

The second area of opportunity would be development deals in real estate sectors and locations that have great demand but due to government policy have not had matching supply. This can range from modern office buildings with large floor plates in prime CBD locations to logistic centers in key locations. These types of deals require very strong local contacts who already have permitted developments which need investment or who are in a position to negotiate with local governments for the easing of planning controls. In either case once past this barrier opportunity

funds should find that developing quality product in these supply constrained environments should allow them to achieve superior returns for a relatively low amount of risk. When conceiving these projects opportunity funds and their local partners must be careful not to create assets which are too large to comfortably dispose of once they have been built and stabilized.

The third area where opportunity funds may find an abundance of opportunities may be in the acquisition of government and corporate real estate portfolios that are being put on the market. Due to the size of these portfolios very few buyers are able to put in a realistic bid. Also needed for success in this area is access to an extensive or perhaps even pan European asset management network. With these transactions there is also the possibility to strike off market deals in that some of the entities involved may have special needs that can only be fulfilled by certain groups. Again a possible draw back for these types of large purchases is not being able to find buyers when it is time to exit. This can be dealt with by breaking the properties down into smaller portfolios depending on potential buyers in the market at the time.

Opportunity funds have also been able to achieve their mandate in part because of their ability to resist investment trends. One of the basic rules for opportunistic investment is to invest in quality low risk investment that provide high yields and not based on sector performance. In most cases once an economic sector's performance begins to attract investment most opportunistic investments have already been taken. Many times the pattern is for opportunistic investors, due to their local contacts, superior risk assessment skills and their liquidity to spot sectors which have quality opportunities before more main stream and less informed investors. This allows opportunity funds to enter into markets, make superior deals, eventually attract capital which

then enters the market due to sector performance stimulated by the opportunity funds' initial investments allowing opportunity funds to use this new liquidity as an exit. With the amount of capital raised currently by these funds and the pressure that managers may feel to make investments the discipline of knowing not to make investments is crucial. In order to be able to take advantage of these contra cyclical opportunities it is crucial that opportunity funds raise their funds before the investment opportunities arise so that they can be exploited once available. The ability to time these opportunities correctly requires a constant presence. With the current amount of capital that has been raised for investment in Europe this may make the difference between successful and unsuccessful funds. Examples of this contra cyclical approach to opportunistic investment were seen both in the US during the RTC era and more recently during France's period of illiquidity in 1996 and 1997. In the case of France, opportunistic investors already had funds available and felt that the lack of liquidity in the Parisian property markets was an indication that low risk, high yield investments were available. This proved to be true and investors in the Parisian market in this period are now looking for an exit given the liquidity of the market. With the current liquidity in the European market it makes most sense for current investors to dispose of stabilized assets and to wait for the next period of illiquidity.

In conclusion opportunity funds must focus on the principles of opportunistic investing and attempt to apply these rules in the European context. The level of success achieved will be partly determined by executing strategies that were developed during the RTC era, and by not making investments on the basis of current trends but on the basis of investments that present low risk, high yield opportunities.

6. BIBLIOGRAPHY

Appel, Lieberman, Todd. "Western Europe: Are the Opportunities Worth the Risks?", The Real Estate Finance Journal, West Group, Winter 1998.

Baum, Andrew, and Colin Lizieri. "Who Owns the City? Office Ownership and Overseas Investment in the City of London," Real Estate Finance, Spring 1999, pp. 87-100.

Branson, Clive. "Going Private," Urban Land, *Europe Supplement*, December 1998, pp.24-26.

Brealey, Myers. Principles of Corporate Finance, Sixth Edition, Irwin McGraw-Hill, USA, 2000.

Dipasquale, Wheaton. Urban Economics and Real Estate Markets, Prentice Hall, Englewood Cliffs, NJ, USA, 1996.

Dobson, David M. "Retail Development in Europe's City Centers," Urban Land, July 1997, pp.53-55.

Downs, Anthony. "What Have We Learned From the 1980s Experience," Salomon Brothers Real Estate Research Report: Real Estate Investment, July 1991.

DTZ, European Commercial Property Markets Overview, 1999, DTZ, 1999.

DTZ, European Commercial Property Markets Overview, 2000, DTZ, 2000.

EIU Country Report, Country Profile – France, 2000, The Economist Intelligence Unit, London UK, 2000.

EIU Country Report, Country Profile – Germany, 2000, The Economist Intelligence Unit, London UK, 2000.

EIU Country Report, Country Profile – Italy, 2000, The Economist Intelligence Unit, London UK, 2000.

EIU Country Report, Country Profile – United Kingdom, 2000, The Economist Intelligence Unit, London UK, 2000.

"European Real Estate Investment Markets," Urban Land, January 1998, pp.69-76, 103.

Europroperty, Europroperty: Profiles 1997, Estates Gazettes, London UK, 1997.

Europroperty, Europroperty: Profiles 1999, Estates Gazettes, London UK, 1999.

Europroperty, Europroperty: Surveys 1997, Estates Gazettes, London UK, 1997.

Europroperty, Europroperty: Surveys 1999, Estates Gazettes, London UK, 1999.

Europroperty, Europroperty: The Pan European Briefing on Commercial Property, Estates Gazettes, London UK, February 1999 – April 2001.

Financial Times, “Financial Times Survey: Property, Quarterly Review”, The Financial Times, March 9, 2001.

Frampton, Rachel. “Buoyant Booming,” Urban Land Europe, July 2000, p.17.

Frampton, Rachel. “Recovery Confirmed,” Urban Land Europe, January 2000, p.17.

Goobey, Alastair. Bricks & Mortals, Century Business, London UK, 1992.

Grogan, Bradley C. “Berlin Builds,” Urban Land, February 1998, pp. 66-69, 93.

Grogan, Bradley C. “Capitalizing European Real Estate,” Urban Land, January 1998, pp.89-92

Insignia Richard Ellis, European Property Market Report, Summer 2000, Insignia Richard Ellis, London UK, 2000

Jacoby, Charlie. “Making a Mark,” Urban Land, *Europe Supplement*, December 1998, pp.28-32.

Jacoby, Charlie. “Urban Entertainment International,” Urban Land Europe, January 2000, pp.54-59.

Jones Lang Lasalle, European Property Investment: Key facts and issues for investors, September 2000, Jones Lang Lasalle, 2000.

Jones Lang Lasalle, European Property Investment: Key facts and issues for investors, September 1999, Jones Lang Lasalle, 1999.

Jones Lang Lasalle, European Property Investment: Key facts and issues for investors, September 1998, Jones Lang Lasalle, 1998.

Jones Lang Lasalle, Investment Strategy Annual 2001: Opportunities for 2001, Jones Lang Lasalle, 2001.

Jones Lang Lasalle, Market Watch 2Q 2001: Prospects for European Real Estate, Jones Lang Lasalle, 2001.

Lewis, Ric. “At What Price Fear?,” Investment and Pension Europe, April 2000.

Lietz, Dewey, Chan. Real Estate Opportunity Funds: The Numbers Behind the Story, Pension Consulting Alliance, Inc., 1999.

Marshall, Jeffery. "Learning from the RTC," United States Banker, New York USA, September 1993.

McClintock, Marilee. "The Logistics of Supply and Service," Urban Land Europe, July 2000, pp.36-39.

Newberg, Sam. "Competing for Investment," Urban Land Europe, July 2000, pp.50-55.

OECD, Economic Surveys France – July 2000, Organization for Economic Co-Operation and Development, Paris, France, 2000.

OECD, Economic Surveys Germany – May 2001, Organization for Economic Co-Operation and Development, Paris, France, 2001.

OECD, Economic Surveys Italy – May 2000, Organization for Economic Co-Operation and Development, Paris, France, 2000.

OECD, Economic Surveys United Kingdom – June 2000, Organization for Economic Co-Operation and Development, Paris, France, 2000.

Peiser, Richard. "Structuring Real Estate Deals with Institutional Financial Partners," Real Estate Review, New York, Fall 1999; Vol. 29, Iss. 3; pg. 6.

Pizzo, Muolo. Profitting from the Bank and Savings & Loan Crisis, How Anyone Can Find Bargains at America's Greatest Garage Sale, HarperBusiness, New York USA, 1993.

Rodman, Jack. "For Sale," Mortgage Banking, Washington D.C. USA, July 1996.

ULI-The Urban Land Institute. ULI Market Profiles 1997: Europe. Washington D.C.: ULI-The Urban Land Institute, 1997.

ULI-The Urban Land Institute. ULI Market Profiles 1998: Europe. Washington D.C.: ULI-The Urban Land Institute, 1998.

ULI-The Urban Land Institute. ULI Market Profiles 1999: Europe. Washington D.C.: ULI-The Urban Land Institute, 1999.

Watkins, Birge. "Examining the past and present of the RTC," National Real Estate Investor, Atlanta USA, June 1994.

Zuckerman, Howard A. Problem Real Estate, How to Restructure Refinancing and Remarket Troubled Commercial Properties, Probus Publishing Company, Chicago USA, 1992.

7. LIST OF READERS, INTERVIEWS AND CONFERENCES

READERS

Dan Prigmore, Baupost Group Inc., Cambridge USA

INTERVIEWS

Adam Minnick, Goldman Sachs International, London UK

Alex Midgen, N M Rothchilds & Sons, London UK

Brian Niles, Goldman Sachs International, London UK

Charles Humber, The Blackstone Group, London UK

Christopher Staveley, Jones Lang Lasalle, Paris France

James Max, Morgan Stanley, London UK

Jonathan Hodnett, JER Partners, London UK

Michael Follett, Jones Lang Lasalle, Milan Italy

Michael Stellwag, Jones Lang Lasalle, Frankfurt Germany

Nick Marsh, Jones Lang Lasalle, London UK

Rob Reiskin, Curzon Global Partners, London UK

Serge Platonow, Colony Capital, Paris France

Seth Lieberman, Lehman Brothers, London UK

Tony Edgley, Jones Lang Lasalle, London UK

Tony Gibbon, BH2, London UK

CONFERENCES

Real Estate Opportunity Fund Investing Forum, May 31-June 1, 2001, New York, NY, USA

8. ENDNOTES

[1] Lietz, Dewey, Chan. Real Estate Opportunity Funds: The Numbers Behind the Story, Pension Consulting Alliance, Inc., 1999.

[2] Downs, Anthony. "What Have We Learned From the 1980s Experience," Salomon Brothers Real Estate Research Report: Real Estate Investment, July 1991.

[3] Downs, Anthony. "What Have We Learned From the 1980s Experience," Salomon Brothers Real Estate Research Report: Real Estate Investment, July 1991.

[4] Zuckerman, Howard A. Problem Real Estate, How to Restructure Refinancing and Remarket Troubled Commercial Properties, Probus Publishing Company, Chicago USA, 1992.

[5] Downs, Anthony. "What Have We Learned From the 1980s Experience," Salomon Brothers Real Estate Research Report: Real Estate Investment, July 1991.

[6] Downs, Anthony. "What Have We Learned From the 1980s Experience," Salomon Brothers Real Estate Research Report: Real Estate Investment, July 1991.

[7] Watkins, Birge. "Examining the past and present of the RTC," National Real Estate Investor, Atlanta USA, June 1994.

[8] Marshall, Jeffery. "Learning from the RTC," United States Banker, New York USA, September 1993.

[9] Rodman, Jack. "For Sale," Mortgage Banking, Washington D.C. USA, July 1996.

[10] Frampton, Rachel. "Buoyant Booming," Urban Land Europe, July 2000, p.17.

[11] Branson, Clive. "Going Private," Urban Land, *Europe Supplement*, December 1998, pp.24-26.

[12] Branson, Clive. "Going Private," Urban Land, *Europe Supplement*, December 1998, pp.24-26.

[13] Grogan, Bradley C. "Berlin Builds," Urban Land, February 1998, pp. 66-69, 93.

[14] "European Real Estate Investment Markets," Urban Land, January 1998, pp.69-76, 103.

[15] "European Real Estate Investment Markets," Urban Land, January 1998, pp.69-76, 103.

[16] Dobson, David M. "Retail Development in Europe's City Centers," Urban Land, July 1997, pp.53-55.

[17] McClintock, Marilee. "The Logistics of Supply and Service," Urban Land Europe, July 2000, pp.36-39.

[18] EIU Country Report, Country Profile – France, 2000, The Economist Intelligence Unit, London UK, 2000.

[19] Jacoby, Charlie. "Making a Mark," Urban Land, *Europe Supplement*, December 1998, pp.28-32.

[20] "European Real Estate Investment Markets," Urban Land, January 1998, pp.69-76, 103.

[21] "European Real Estate Investment Markets," Urban Land, January 1998, pp.69-76, 103.

[22] Frampton, Rachel. "Recovery Confirmed," Urban Land Europe, January 2000, p.17.

[23]Jacoby, Charlie. "Making a Mark," Urban Land, *Europe Supplement*, December 1998, pp.28-32.

[24] "European Real Estate Investment Markets," Urban Land, January 1998, pp.69-76, 103.

[25]McClintock, Marilee. "The Logistics of Supply and Service," Urban Land Europe, July 2000, pp.36-39.

[26]Jacoby, Charlie. "Making a Mark," Urban Land, *Europe Supplement*, December 1998, pp.28-32.

[27] "European Real Estate Investment Markets," Urban Land, January 1998, pp.69-76, 103.

[28] "European Real Estate Investment Markets," Urban Land, January 1998, pp.69-76, 103

[29] Jacoby, Charlie. "Making a Mark," Urban Land, *Europe Supplement*, December 1998, pp.28-32.

[30] Dobson, David M. "Retail Development in Europe's City Centers," Urban Land, July 1997, pp.53-55.

[31]"European Real Estate Investment Markets," Urban Land, January 1998, pp.69-76, 103.

[32] Dobson, David M. "Retail Development in Europe's City Centers," Urban Land, July 1997, pp.53-55.

[33] Jacoby, Charlie. "Urban Entertainment International," Urban Land Europe, January 2000, pp.54-59.

[34] McClintock, Marilee. "The Logistics of Supply and Service," Urban Land Europe, July 2000, pp.36-39.

[35]Baum, Andrew, and Colin Lizieri. "Who Owns the City? Office Ownership and Overseas Investment in the City of London," Real Estate Finance, Spring 1999, p. 87.

[36] Baum, Andrew, and Colin Lizieri. "Who Owns the City? Office Ownership and Overseas Investment in the City of London," Real Estate Finance, Spring 1999, p. 90.

[37] Baum, Andrew, and Colin Lizieri. "Who Owns the City? Office Ownership and Overseas Investment in the City of London," Real Estate Finance, Spring 1999, p. 91.

[38] Baum, Andrew, and Colin Lizieri. "Who Owns the City? Office Ownership and Overseas Investment in the City of London," Real Estate Finance, Spring 1999, p. 91.

[39] Baum, Andrew, and Colin Lizieri. "Who Owns the City? Office Ownership and Overseas Investment in the City of London," Real Estate Finance, Spring 1999, p. 91.

[40] Baum, Andrew, and Colin Lizieri. "Who Owns the City? Office Ownership and Overseas Investment in the City of London," Real Estate Finance, Spring 1999, p. 87.

[41] Jones Lang Lasalle, European Property Investment: Key facts and issues for investors, September 2000, Jones Lang Lasalle, 2000.

[42] Jacoby, Charlie. "Urban Entertainment International," Urban Land Europe, January 2000, pp.54-59.