# on.point

Office market in the Greater Paris Region
Q1 2013

Jones Lang LaSalle
*Real value in a changing world*

## Divergent trends

The rental market weakened in Q1 faced with a still complicated macro-economic situation.

Since 2009, immediately available supply has hardly changed and remains capped at close to 3.6 million sq m.

Prime rent in the CBD fell again in Q1 and is now €760 per sq m.

Over €2 billion invested since the start of the year – a rise of 43% in one year.

5 transactions exceeding €100 million registered in Q1 2013.

The key prime yield, in the Central Business District, remained stable in a range between 4.50 and 5.00%.

# A sluggish Q1 for the rental market

After very good results in 2011 and 2012 (over 2.4 million sq m leased each year), the rental market slowed in Q1, impacted by the poor economic conditions. In total, 393,500 sq m were leased during the first three months of the year, which represents a fall of around 24% compared to last year (Q1 already itself down 19%). It is the weakest quarter registered since 2009.

### The economic crisis has finally caught up with the office market

For a number of months already, companies have been wallowing in a sluggish and uncertain context: low confidence indicators, slowdown in activity, austerity, fiscal and social uncertainties, reduced margin level… an environment hardly likely to encourage relocation decisions but which, on the contrary, is forcing companies to cut costs.

This willingness to reduce costs is conveyed by a growing phenomenon over the past few years: renegotiations, which are limiting the level of the take-up. This solution is often chosen by companies whose motivation is to cut costs: the conditions for financial negotiations with their owner are favourable and the option to stay put proves to be the least risky solution employee-wise.

*"In fact, given the falls in effective rents in the established markets, relocating solely for economic reasons would now involve moving further away from the centre of Greater Paris Region. This type of decision involves risks with regard to human resources that companies do not want to take, particularly in Greater Paris Region where the majority of companies are present in the service sector, or are head offices of industrial groups, whose main asset is their employees. Conversely, companies that choose to shift do so for reasons that go beyond pure financial reasons: search for synergies, company image, recruitment and retention of talent"* says Jacques Bagge, Head of Agency at Jones Lang LaSalle.

### All market segments have been impacted

From the market viewpoint this is conveyed by a fall in rental activity in most of the sectors, with a sharp fall in the number of large transactions (exceeding 5,000 sq m), which fell from 17 to 12 compared to Q1 2012. The deficit is 30% in number of transactions, and 40% in surface area. In a crisis period, decisions take longer and projects, despite high managerial ambitions, can be delayed while waiting for a better context but also counting on even more favourable rental conditions.

Generally, all the surface area segments have been affected by this slowdown, with the market of transactions comprised between 1,000 sq m and 5,000 sq m having, however, resisted better.

### La Défense and Paris have resisted better than the Greater Paris Region average

From a geographical viewpoint no market has escaped the fall in rental activity with the Outer Suburbs in the front line, which registered the sharpest fall (-42%), the number of large transactions having been cut by three. La Défense and Paris have limited the fall with -12 and -15% respectively. The favourable rental conditions for tenants enable them, at the same budget, to remain in the central markets.

In Paris, the Central Business District is in line with the rest of the capital: -15% of its rental activity, and one transaction exceeding 5,000 sq m signed Rue Le Peletier by Keolis, which groups together several locations in Paris into one site.

In the Western Crescent, the Northern Bend and Neuilly-Levallois registered a good start to the year, driven by the signatures of the law firm of Francis Lefebvre in Neuilly (16,000 sq m) and a turnkey in Parc Silic in Colombes (8,700 sq m). In La Défense, the lease by the Fidal legal practice in the Prisma tower (14,000 sq m) has buoyed the market. For the other sectors in the Western Crescent, the slowdown is more marked. The Southern Bend, which experienced an exceptional start to 2012, finally achieved a more classic pace of transactions. This quarter Péri-Défense did not register any large transaction and therefore dropped by nearly 50% compared to last year, which included the Véolia transaction in Le Vermont (15,000 sq m).

### The dichotomy of the supply market continues

At the end of Q1, the immediately available supply in the Greater Paris Region remained stable at around 3.6 million sq m (i.e. a vacancy rate of 6.8%), which can be seen as good news given the slowdown of activity this quarter. This status quo with regard to immediate supply can also be explained by the reduced volumes of deliveries that took place this quarter, with less than 70,000 sq m delivered, for which only 5,000 sq m is available. The share of new buildings in available stock continued to diminish and represented 20% of this quarter's immediate supply (compared to 22% one year previously, 24% at Q1 2011 and 29% at Q1 2010).

At the end of Q1, the dichotomy of the Paris region market was still valid, with a Paris market that registered a very low vacancy of 4.5%, whereas the Western Crescent showed a vacancy of 12% on average, with peaks of 14% in the Northern Bend and in Péri-Défense. The immediate supply also remained significant in the Inner Rim, which reached 9.1% vacancy rate (10% in Northern Inner Suburbs). A noteworthy fact is that several new buildings, some vacant for several years, have gradually been taken up following the readjustment of their rental values like “Tryalis” in Montreuil (delivered in 2010), “Aristide” in Bagneux (delivered in 2009), “Etik” in Boulogne (delivered in 2011) or “Front Office” in Asnières (delivered in 2009).

### Prime rent fell again

The Greater Paris Region prime rent fell again this quarter, from €770 at the end of 2012 to €760 in the Central Business District and from €530 to €520 in La Défense.

The beginning of a fall in headline values, which began last year, should be confirmed in the coming months throughout the entire Greater Paris Region market. Currently the market offers outstanding buildings with the latest environmental certifications with very offensive value positioning. Headline values should therefore approach effective values (real rent after negotiations), which fell sharply last year and which currently are at record lows.

The upturn in the rental market will only happen if values are readjusted. Therefore, 2013 should be a year of transition, before a more pronounced recovery in 2014-2015 once values have been adjusted.

# Outlook

Taking into account the fall during Q1, and the probable contraction of the large turnkeys this year (whereas they represented over a half-million square metres last year), take-up should reach the 2 million sq m mark with difficulty, i.e. a level below the ten-year annual average (2.2 million sq m).

However, the fall in rental values and the necessity for landlords to fill up their buildings, makes the market favourable to tenants and could trigger opportunistic movements. In fact, although the values displayed are heading downwards, real values are already low and should remain so throughout the year. Furthermore, for companies searching for efficient buildings it can be stated that Grade A immediately available supply, although in the minority (around a third of the immediate supply of over 5,000 sq m), remains sufficient in certain sectors to meet demand under good conditions, as long as new deliveries are expected during the year.

In the coming months, supply could increase in some sectors such as La Défense due to the delivery of large speculative projects, which for the moment have not yet found a tenant.

In 2013, the number of new or restructured projects rose, after two years of a shortage of deliveries. In total, 860,000 sq m should emerge. To date 53% are pre-let. Nevertheless, over 400,000 sq m still needs to be leased to clear the new production this year, of which half is situated in the west of the Greater Paris Region.

# The investment market has started 2013 on a positive note

In the Greater Paris Region, over €2 billion was invested in Q1 2013, i.e. a rise of over 40% in one year. This good performance has given a positive signal to the confidence of investors in the Paris region investment market: this is the first time since 2008 that the investment market has reached this mark over the first three months of the year. As a comparison, the Q1 investment volume places the market at a level comparable to that of 2004 or 2005, years where the annual investment volume was situated between €10 and €12 billion.

*"This good start to the year can be accounted for by the earlier than usual launch of investors' arbitrage plans from summer 2012. They have enabled the market to conclude significant transactions from the start of the year"*, states Stephan von Barczy, Head of Capital Markets at Jones Lang LaSalle.

## Volumes are distributed equally over all the segments in terms of size

The good performance of the investment market is built in a balanced way on all the market segments in terms of size.

Five transactions of over €100 million, representing close to €800 million, were registered at the end of March, i.e. the same number as last year at the same time. Among the leading transactions for the quarter, we note the acquisition by GECINA from ABERDEEN IMMOBILIEN of the "Tour Mirabeau", situated in the 15th district of Paris for a price slightly below €200 million, the sale by RISANAMENTO to PRAMERICA of the "118 avenue des Champs Elysées" building for €135 million, or the acquisition by PRIMONIAL from ALTAREA COGEDIM of the "Okabé" building situated at Kremlin-Bicêtre for €120 million.

The market has been much more dynamic in the segment of intermediate size transactions (including between €50 and €100 million), with 10 transactions registered for close to €700 million, compared to only 3 for €160 million in Q1 2012. It is in this specific and very liquid segment that market performance rests on the first three months of the year.

## The office share still dominates, but there is a strong dynamism in retail space

The share of office buildings was still in the majority this quarter with 78% of the amounts committed. However, sales of retail space have been dynamic and totalled 16% of the amounts invested in Greater Paris Region. Three significant transactions were registered on unit shops. These are "118 avenue des Champs Elysées", sold by RISANAMENTO to PRAMERICA, "76/78 avenue des Champs Elysées" sold by ARCHON and finally the retail part of the "T8" transaction, situated in the 13th district of Paris purchased by DEKA at the start of the year.

## Paris preferred destination for capital

Inner Paris captured 51% of investments made in Q1 in the Paris region market. The Central Business District and South Paris represented 31% and 12% respectively of the amounts invested in the City of Paris. This high proportion is explained by the completion of transactions of over €100 million: the sales of "Tour Mirabeau", and of "118 avenue des Champs Elysées".

La Défense market still experienced several difficulties with only one transaction registered, less than €15 million. The unit volume of properties as well as the limited performance of the end-user market, combined with a shortage of financing, still explain the difficulties encountered by the business centre.

### Strong presence of French investors in the first part of the year

Q1 2013 was characterised by highly active French investors who represented 75% of the amounts invested. They have once again greatly occupied the terrain of transactions below €100 million with 80% of volumes invested. However, their share was also clearly in the majority in the segment of large transactions exceeding €100 million, with 3 transactions out of the 5 registered, i.e. 2/3 of the quarter's investments.

We note that retail property was a great success with foreign investors since the three largest transactions were purchased by international investors, who represented over 80% of the volumes invested in this quarter's retail space.

### Stability of yields in the majority of sectors

Yields remained stable in the majority of markets in the Greater Paris Region, with the appetite for prime products remaining high. The key prime yield, in the Central Business District, remained stable in a range between 4.50% and 5.00%. In Péri-Défense, Northern Bend and Inner Southern Suburbs the prime yield fell slightly (+25 bps) this quarter due to a less favourable rental context (vacancy rate, change in rental activity or values).

Since the start of the year we note an easing of the property financing market, with new players (debt funds, insurance companies), which have positioned themselves in this sector in addition to banks.

The financing of the most secure properties remains greatly assured by the market, both by the traditional networks (mortgage debt) and by the new players. Some participants (debt funds and certain banks) are "leaving" the very secure prime segment, where competition is fierce, to position themselves on "core +" assets.

Regarding the most risky properties, financing still remains complex and uncertain. In general, although financing solutions have become more numerous, the market remains very fragmented and financing conditions are more volatile than before the financial crisis.

# Outlook

The good start to the year and the volume of files already identified or being marketed, enable us to confirm our forecast of a 2013 investment volume around €12 billion at this stage. Although the rate levels seem perfectly confirmed by the market for 18 months, investors will remain very attentive to property rent levels compared to the change in the rental market.

Despite a difficult and uncertain economic context in France (rise in unemployment, low confidence indicators, slowdown in activity, fiscal and social uncertainties, etc.), investors will continue to invest in the Paris market, which remains a safe bet in Europe, both because of the depth and maturity of the market.

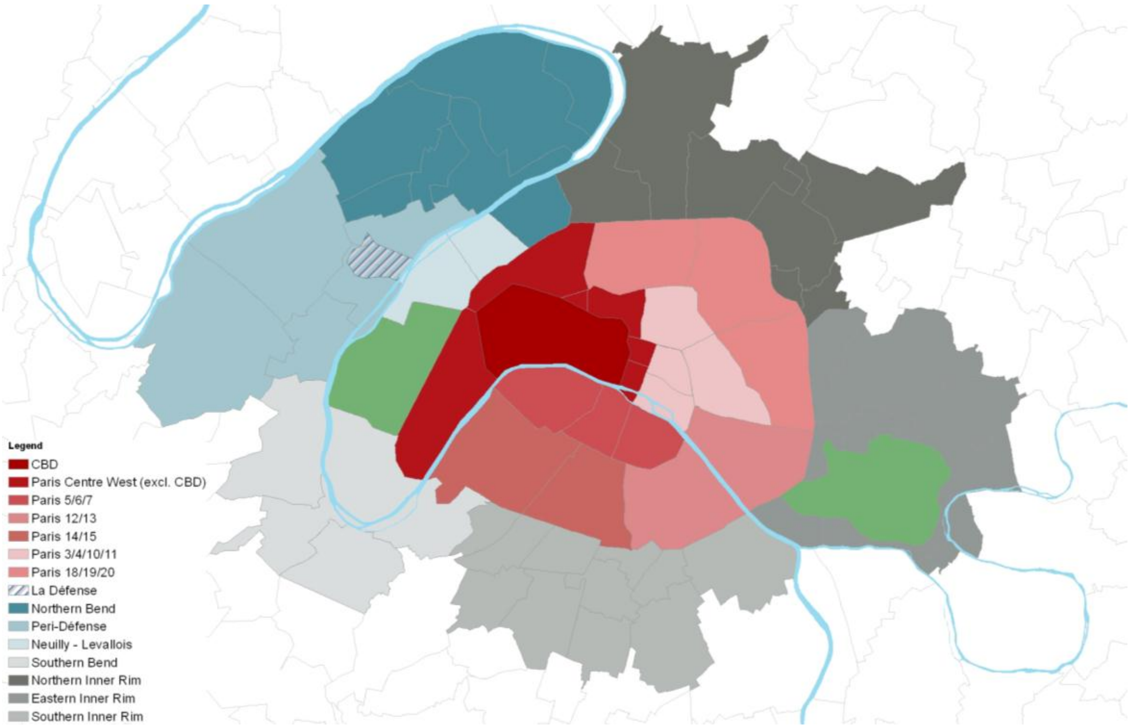
As for the sovereign funds, they are likely to slow down their investments in France to continue their acquisition strategy in other European countries such as Germany and Switzerland, where they began to position themselves last year. However, depending on opportunities offered by the market, we could still see them position themselves on "trophy assets".

In terms of typology of products, the appetite of the market for prime buildings does not disappoint and yields should again remain stable. They may even occasionally decrease, mainly because of the decrease of remuneration of French OAT (below 2%). Nevertheless, a growing number of investors are also turning to "core +" or "value-added" transactions.

## Key market indicators in Q1 2013

(Source: Jones Lang LaSalle/Immostat)

| Immostat Sector | Take-up as at 31/03/2013 (sq m) | Evolution y O y | Immediate supply as at 31/03/2013 (sq m) | Immediate vacancy rate as at 31/03/2013 | Prime rent (€/sq m/yr) | Average second hand rent (€/sq m/yr) |
|---|---|---|---|---|---|---|
| CBD | 61 036 | -15% | 352 000 | 5,2% | 760 | 519 |
| Paris Centre West (excl. CBD) | 18 024 | -16% | 111 000 | 6,1% | 565 | 385 |
| **Total Paris Centre West** | **79 060** | **-15%** | **463 000** | **5,4%** | **760** | **452** |
| Paris 5/6/7 | 8 247 | 109% | 25 000 | 1,9% | 705 | 486 |
| Paris 12/13 | 12 894 | -34% | 83 000 | 4,3% | 470 | 395 |
| Paris 14/15 | 21 907 | 31% | 74 000 | 3,7% | 485 | 399 |
| **Total Paris South** | **43 048** | **7%** | **182 000** | **3,5%** | **705** | **427** |
| Paris 3/4/10/11 | 9 549 | -34% | 51 000 | 3,2% | 430 | 328 |
| Paris 18/19/20 | 22 189 | -34% | 49 000 | 4,0% | 355 | 254 |
| **Total Paris North East** | **31 738** | **-34%** | **100 000** | **3,5%** | **430** | **291** |
| **Total Inner Paris** | **153 846** | **-15%** | **745 000** | **4,5%** | **760** | 395 |
| **La Défense** | **25 774** | **-12%** | **186 000** | **5,7%** | **520** | **379** |
| Northern Bend | 25 298 | 441% | 267 000 | 14,6% | 305 | 218 |
| Péri Défense | 19 573 | -46% | 329 000 | 14,0% | 385 | 248 |
| Neuilly / Levallois | 33 689 | 39% | 173 000 | 12,1% | 565 | 326 |
| Southern Bend | 36 296 | -58% | 218 000 | 8,3% | 465 | 311 |
| **Total Western Crescent** | **114 856** | **-25%** | **987 000** | **12,0%** | **565** | **276** |
| Northern Inner Suburbs | 9 140 | -52% | 238 000 | 10,0% | 340 | 205 |
| Eastern Inner Suburbs | 7 564 | 32% | 125 000 | 8,0% | 315 | 236 |
| Southern Inner Suburbs | 19 593 | -7% | 180 000 | 9,0% | 355 | 236 |
| **Total Inner Rim** | **36 297** | **-20%** | **543 000** | **9,1%** | **355** | **226** |
| Roissy Pole | 1 590 | -92% | 81 000 | 6,8% | 170 | 132 |
| Saint-Quentin-en-Yvelines | 24 510 | 303% | 153 000 | 10,7% | 180 | 145 |
| Marne-la-Vallée | 2 881 | -70% | 131 000 | 9,3% | 215 | 143 |
| Southern Outer Suburbs | 22 273 | -49% | 350 000 | 10,0% | 225 | 170 |
| Rest of Outer Suburbs | 11 450 | -61% | 405 000 | 3,6% | 235 | 151 |
| **Total Outer Suburbs** | **62 704** | **-42%** | **1 120 000** | **6,0%** | **235** | **148** |
| **Paris Region** | **393 477** | **-24%** | **3 581 000** | **6,8%** | **760** | **314** |



## Breakdown of amounts invested by Immostat sector

(Source: Jones Lang LaSalle/Immostat)

| Immostat zone | Investment volumes as at end of March 2009 (in € million) | % | Investment volumes as at end of March 2010 (in € million) | % | Investment volumes as at end of March 2011 (in € million) | % | Investment volumes as at end of March 2012 (in € million) | % | Investment volumes as at end of March 2013 (in € million) | % |
|---|---|---|---|---|---|---|---|---|---|---|
| CBD | 149 | 33% | 483 | 60% | 245 | 18% | 146 | 10% | 636 | 31% |
| Paris Center West (excl. CBD) | 7 | 2% | 25 | 3% | 84 | 6% | 40 | 3% | 177 | 8% |
| Southern Paris | 86 | 19% | 29 | 4% | 55 | 4% | 363 | 25% | 252 | 12% |
| North Eastern Paris | 0 | 0% | 22 | 3% | 33 | 3% | 130 | 9% | 0 | 0% |
| La Défense | 23 | 5% | 20 | 2% | 0 | 0% | 0 | 0% | 12 | 1% |
| Western Crescent | 105 | 24% | 98 | 12% | 641 | 47% | 340 | 23% | 477 | 23% |
| Inner suburbs | 0 | 0% | 30 | 4% | 150 | 11% | 126 | 9% | 262 | 13% |
| Outer suburbs | 40 | 9% | 92 | 11% | 138 | 10% | 243 | 17% | 139 | 7% |
| Greater Paris Region portfolio | 36 | 8% | 10 | 1% | 16 | 1% | 55 | 4% | 113 | 5% |
| **Greater Paris Region** | 445 | 101% | 810 | 100% | 1 361 | 100% | 1 443 | 100% | 2 069 | 100% |

## Breakdown of amounts invested by type of property

(Source: Jones Lang LaSalle/Immostat)

| Immostat zone | Investment volumes as at end of March 2009 (in € million) | % | Investment volumes as at end of March 2010 (in € million) | % | Investment volumes as at end of March 2011 (in € million) | % | Investment volumes as at end of March 2012 (in € million) | % | Investment volumes as at end of March 2013 (in € million) | % |
|---|---|---|---|---|---|---|---|---|---|---|
| Office | 358 | 80% | 704 | 87% | 1 154 | 85% | 1 303 | 90% | 1 617 | 78% |
| Light industrial / Mixed | 30 | 7% | 28 | 3% | 56 | 4% | 24 | 2% | 64 | 3% |
| Warehouse | 18 | 4% | 4 | 1% | 0 | 0% | 32 | 2% | 64 | 3% |
| Retail | 39 | 9% | 74 | 9% | 151 | 11% | 84 | 6% | 324 | 16% |
| **Paris region** | 445 | 100% | 810 | 100% | 1 361 | 100% | 1 443 | 100% | 2 069 | 100% |

## "Prime" yield

(Source: Jones Lang LaSalle)

| | Office prime yield range in Q1 2010 (%) | Office prime yield range in Q1 2011 (%) | Office prime yield range in Q1 2012 (%) | Office prime yield range in Q1 2013 (%) | Yearly evolution |
|---|---|---|---|---|---|
| Golden Triangle | 5.50 - 6.00 | 4.75 - 5.25 | 4.75 - 5.25 | 4.50 - 5.00 | ↘ |
| Financial district | 5.75 - 6.25 | 5.00 - 5.50 | 5.00 -5.50 | 4.75 - 5.25 | ↘ |
| Paris 5/6/7 | 5.75 - 6.25 | 5.25 - 5.75 | 5.25 - 5.75 | 5.00 - 5.50 | ↘ |
| Paris 12/13 | 6.00 - 6.50 | 5.25 - 5.75 | 5.50 - 6.00 | 5.50 - 6.00 | → |
| Paris 14/15 | 6.00 - 6.51 | 5.25 - 5.75 | 5.50 - 6.00 | 5.50 - 6.00 | → |
| Paris 3/4/10/11 | 6.00 - 6.50 | 5.50 - 6.00 | 5.75 - 6.25 | 5.75 - 6.25 | → |
| Paris 18/19/20 | 6.75 - 7.25 | 6.25 - 6.75 | 6.25 - 6.75 | 6.25 - 6.75 | → |
| La Défense | 6.00 - 6.50 | 5.50 - 6.00 | 5.75 - 6.25 | 6.00 - 6.50 | ↗ |
| Northern loop | 6.75 - 7.25 | 6.25 - 6.75 | 6.25 - 6.75 | 6.50 - 7.00 | ↗ |
| Péri Défense | 6.75 - 7.25 | 6.25 - 6.75 | 6.25 - 6.75 | 6.50 - 7.00 | ↗ |
| Neuilly-Levallois | 6.25 - 6.75 | 5.75 - 6.25 | 5.75 - 6.25 | 5.25 - 5.75 | ↘ |
| Southern loop | 6.25 - 6.75 | 5.75 - 6.25 | 5.75 - 6.25 | 5.50 - 6.00 | ↘ |
| Northern Inner suburbs | 6.75 - 7.25 | 6.25 - 6.75 | 6.25 - 6.75 | 6.25 - 6.75 | → |
| Eastern Inner suburbs | 7.00 - 7.50 | 6.50 - 7.00 | 6.50 - 7.00 | 6.50 - 7.00 | → |
| Southern Inner suburbs | 6.75 - 7.25 | 6.25 - 6.75 | 6.25 - 6.75 | 6.25 - 6.75 | → |

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Printing information: paper, inks, printing process, recycle directive.