REAL ESTATE REVIEW

CZECH REPUBLIC

2010

ECONOMIC OVERVIEW I OFFICE I INDUSTRIAL I INVESTMENT

COLLIERS INTERNATIONAL

Our Knowledge is your Property

The role of experienced consultants, who can analyse the market and come up with a novel solution, is gaining importance.

Dear Colleagues and Friends,

I am sure you would agree with me if I summed up 2009 as a test. A harsh test each one of us had to undergo with reluctance. Some were more prepared than others. Regardless of the business sector the impact of the economic recession was felt by all. The most important thing we should take from 2009 is the ability to manage the new challenges we learnt to face under changing market conditions.

To summarize the last year in just a few simple phrases such as the drop in market activity, the halting of new construction and the slump in investment transactions would be extremely short-sighted. The character of the market has changed, so our approach to it should change too. The many years of rapid demand growth and under-supply, when the work of real estate consultants comprised processing deals, has changed. The overheated market suddenly turned in favour of tenants and it seems we can expect the same in the coming year. The role of experienced consultants, who can analyse the market and anticipate future market development is gaining importance.

The ability to analyse facts and find mutually beneficial solutions, is again becoming a merit of our work, the work of real estate consultants.

I will leave the evaluation of the past year upto you - whether you consider it interesting and perhaps positive, or you will try to forget it as soon as possible. I am sure you will agree that the best thing to do is to look to the future. And just like last year, the ability to make the right decision quickly with the support of high quality and trusted advice is the key. I am sure you will find some of this information outlined in our market report.

In conclusion, allow me to thank my team at the Prague office sincerely. They deserve it. Despite the difficult times, my team has proved once again that real professionals can find solutions and interesting opportunities when others may not be able to do so.

I look forward to working with you in 2010!

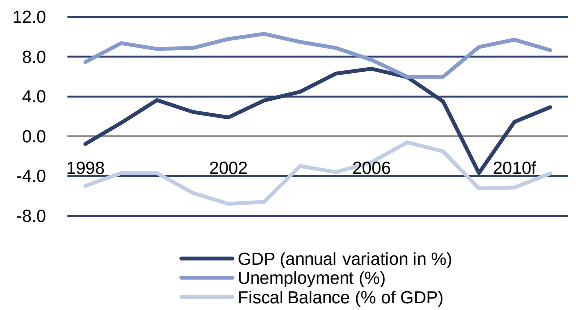
Karel Stransky

MANAGING PARTNER
CZECH REPUBLIC

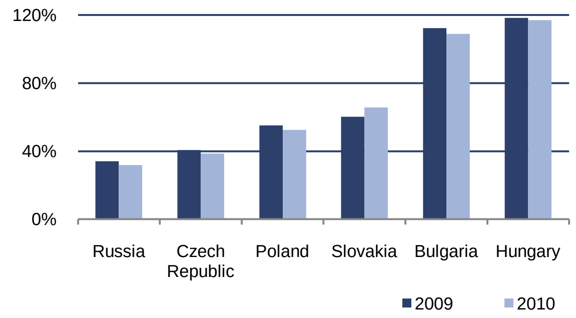
ECONOMIC OVERVIEW

The economic situation in the Czech Republic reached bottom in 2009, analysts are getting more optimistic and raising their expectations for 2010.

GDP / UNEMPLOYMENT / FISCAL BALANCE



EXTERNAL DEBT



MARKET INDICATORS

↓ GDP GROWTH	↓ NET INITIAL YIELDS
↓ INFLATION	→ OFFICE RENTS
↓ INDUSTRIAL PRODUCTION	→ INDUSTRIAL RENTS
↓ RETAIL SALES	↓ RETAIL RENTS

THE ECONOMY BOTTOMS-OUT IN 2009…

• For the first year since 2000, there was a GDP decline in the country of 3.7%. The situation is expected to stabilize with the latest forecasts showing GDP growth of 1.5% in 2010.

• 2009 saw a record increase in corporate (42%) and personal (147%) bankruptcies. We believe this trend will continue up until mid 2010 as a result of continuing company defaults.

• As a direct result of recent bankruptcies the unemployment, reached its highest level since 2003 at 9.0%. It is expected to increase to 9.5%-10% in 2010 before stabilising toward the end of the year.

• The Czech inflation rate continued to decrease over the course of 2009 to reach 1.0% compared to 2008 (a record low since 2003). Analysts, however, are now forecasting more “reasonable” levels of inflation for 2010. On average, a 2.0% increase compared to 2009 seems likely.

• Czech external debt increased to a record 40% of GDP in 2009 but is expected to decrease back to 38% in 2010. However, the Czech Republic shows a healthier financial situation compared to other CEE countries.

…BUT SET TO RECOVER IN 2010?

• Despite the major downturn of 2009, the Czech economy remains in better shape than most other Central and Eastern European countries. The combination of low external debt, strong foreign direct investment volumes and the latest optimistic forecast in terms of exports makes for a more optimistic scenario for 2010. This does not mean a major recovery is likely - we see 2010 as a stabilization period.

• That said, there are many external risks to the economy recovering and stabilising. In particular, economic growth will mostly depend on

a) an upturn in consumption in western European economies as over 60% of Czech exports are aimed at these markets, and

b) the strategy of banks regarding their future investment in the country from both a corporate and retail banking perspective.

• The real estate market will benefit from this and the first signs of recovery were witnessed in the last quarter of 2009 with renewed leasing and investment activity across the country.

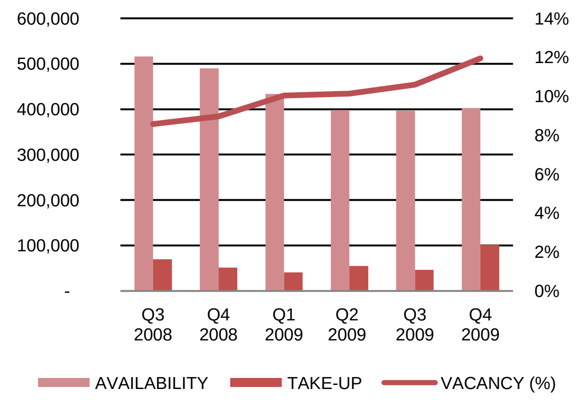
Low external debt of 40% compared to the EU average of 70% is a healthy sign.

GDP declined by 3.7% in 2009, but the latest forecasts show an optimistic 1.5% growth for 2010 in line with the growth in exports.

OFFICES

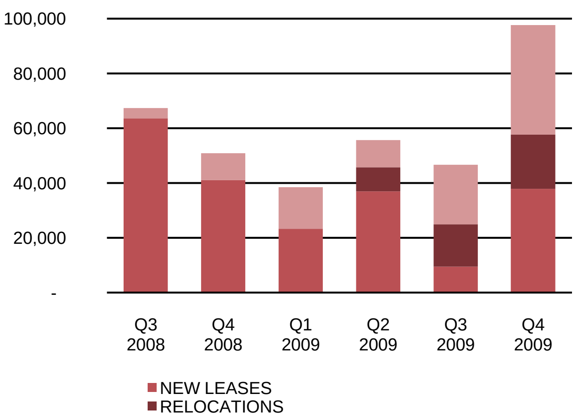
Vacancy increased by 300 basis points. New supply dropped by 50%. Net take-up weakened. Renegotiations represented 35% of take-up in 2009.

PRAGUE: AVAILABILITY / TAKE-UP



* Colliers/PRF

PRAGUE: TAKE-UP STRUCTURE



* Colliers/PRF

SUPPLY

• After the record breaking year of 2008 when the new office supply exceeded 322,000 sqm, 2009 brought only 162,000 sqm to the market. This represents a 50% y-o-y decline. The total office stock now stands at 2.7 million sqm.

• Many projects planned for delivery in 2010/2011 have been postponed until pre-lets are secured. We monitor about 70,000 sqm of office space under construction.

DEMAND

• As a result of negative GDP growth, the take-up also declined over the year reaching only 245,000 sqm – only 6% less than in 2008.

• Take-up, however, was mostly driven by renegotiations and relocations that amounted to more than a half. Net take-up actually weakened, reaching only around 115,000 sqm.

• Almost 30% of companies that renegotiated their lease terms were from either the IT & Telecoms, Professional Services and Manufacturing sectors. The largest renegotiation was by Vodafone in Vinice Centre, Prague 10.

• The largest transaction in 2009 has been a 25,700 sqm pre-let in PSJ Invest's Main Point Karlin.

VACANCY

• Due to the changed market conditions coupled with a large delivery of space in late 2008 and early 2009, the overall vacancy rate increased. It grew continuously over the year reaching 11.8% at the end of 2009 compared to less than 9% at end 2008.

• Prague 8 recorded the most significant increase, from 4.7% to 18.5%.

• This occurred despite the drop in new development recorded in 2009 (162,000 sqm delivered in the whole of 2009 compared to 207,000 sqm constructed in the last six months of 2008).

2009 brought 162,000 sqm to the market. This represents a 50% y-o-y decline.

Renegotiations, sub-leases and relocations accounted for 55% of take-up. Net take-up practically diminished.

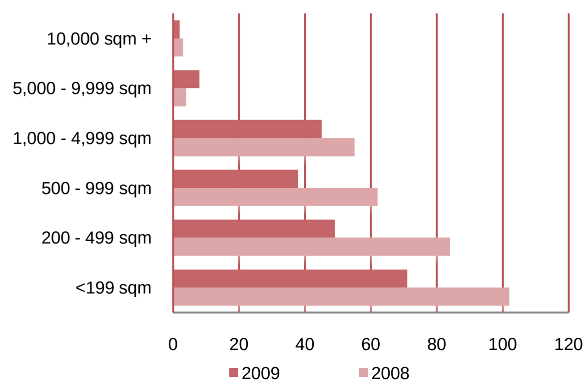
2009 MAJOR TRANSACTIONS IN PRAGUE

TENANT NAME	PROPERTY NAME	OWNER / DEVELOPER	SIZE (sqm)	TRANSACTION TYPE
Kooperativa	Main point Karlin	PSJ invest	25,700	Pre-lease
Vodafone	Centrum Vinice	Immoeast	19,691	Renegotiation
Hewlett Packard	BB Centrum C	Immoeast	7,800	Renegotiation
ICZ	Kavci Hory Office Park	Europolis	7,194	Relocation
Accenture	Office Park Nove Butovice	CSIA	6,650	Renegotiation
RWE Interni sluzby	Prosek Point C	J & T	5,870	Relocation
Citibank	Explora Jupiter	Quinlan Private Golub	5,740	Relocation
Microsoft CR	BB Centrum Alpha	Invesco	5,300	Renegotiation
Czech Airlines	Airport Business Centre	Immoeast	5,229	Lease
RWE Transgas Net	Kavci Hory Office Park	Europolis	5,097	Lease

OFFICES

Low net take-up. Leasing activity mostly based on renegotiations, relocations and sub-leases. Growing vacancy. Market searching for balance in 2010.

2009 DEAL SIZES (NO OF DEALS)



PROJECTED PIPELINE

PROPERTY NAME	DEVELOPER	LOCATION	SIZE (sqm)	COMPLETION
Vaclavske namesti 17	VN 17	Prague 1	1,810	2010
Parizska 26	FIM Group	Prague 1	1,700	2010
Havlickova 3	FIM Group	Prague 1	1,962	2010
BB Centrum Filadelfie	Passerinvest	Prague 4	28,160	2010
Main Point Karlin	PSJ Invest	Prague 8	22,000	2011/2012
Harfa Office Park	Lighthouse	Prague 9	24,000	2011/2012
Palac Krizik 2nd phase	Cecopra	Prague 5	6,000	2012
City Deco	PPF ECM Holding	Prague 4	10,000	2011/2012
City Element	PPF ECM Holding	Prague 4	7,000	2011/2012

RENTS

• Office prime headline rents decreased slightly in 2009. Monthly rents in the city centre dropped to €20 - 21 per sqm, and to €12 – 14 per sqm in the outer city. Rents in the inner city remained at €15 - €17.5 per sqm.

• To keep existing tenants or gain new ones, landlords continued to provide discounts and incentives. With a 5 year lease tenants were able to secure a 3-5 month rent free period and fit-out contribution of €30 - €50 per sqm, on average.

FORECAST

• A total of 34,000 sqm of office space is estimated to be delivered in 2010 comprising only one significant project – Filadelfie, a further phase of the BB Centrum project situated in Prague 4.

• Only construction of few other projects will commence in 2010 – fully pre-let Main Point Karlin, or two buildings in the CITY in Prague 4.

• Leases signed in 2005 and 2006 are coming to an end in 2010/2011. Assuming that the majority of current tenants will stay in their leased premises and adjust the lease terms to prevailing market conditions, we expect renegotiations to keep a significant share of the take-up in 2010.

• Sub-leases will also take an important role in the upcoming year as companies continue to optimize their leased space and offer, where possible, some of this space back on to the market. We expect take-up to be based on subleases in prime locations (City Centre, Andel, Pankrac), in particular.

• Relocations provide another opportunity for tenants to reduce costs and optimise space as they seek more favourable terms. We assume that tenants will occupy less space in the newly leased premises.

• Based on these trends and our analyses, we expect the overall vacancy to grow continuously over the next 12-18 months. In the worst case it could climb up to 14% by the end 2010 or early 2011 before reducing to 10%. This of course, is dependent on how fast the economy recovers and the confidence of decision makers in the market.

• In prime locations with low availability, vacancy is likely to return to its ‘natural rate’ as currently vacant space is absorbed fairly quickly.

• Prime rents are expected to remain at current levels, while net effective rents should continue to decrease in the next 6 - 12 months.

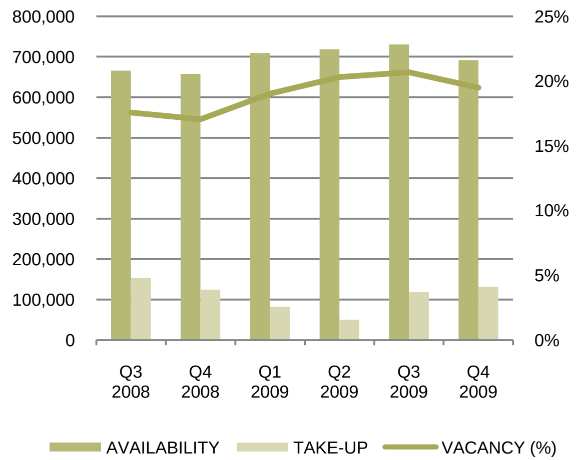
Vacancy may reach up to 14% by end 2010 or early 2011, placing negative pressure on rents.

Less than 35,000 sqm of new space is expected for delivery in 2010, an 80% fall compared to 2009. Only a few projects will commence construction.

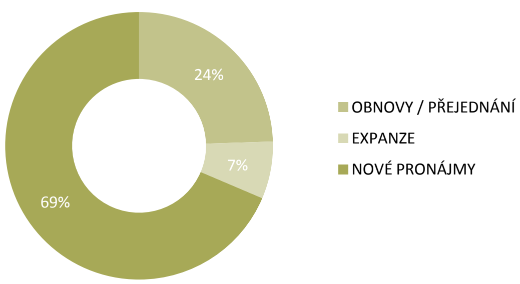
INDUSTRIAL

The total industrial take up amounted to just over 380,000 sqm representing only 56% of the total demand recorded in 2008.

CZECH REPUBLIC: AVAILABILITY / TAKE UP



2009 TAKE UP - STRUCTURE



DEMAND

• Industrial leasing activity in 2009 was driven mainly by retailers (30% incl. wholesalers) and logistic services providers (27% of total demand).

• Around 66% of leases were signed in the 2nd half of 2009; while in 2008, the majority of demand was generated during the first six months of the year.

• 24% of total demand comprised contract renewals/renegotiations; 7% comprised pure space expansions. The remainder was a combination of pre-lets and standard leases.

• Prague continues to play the key role in the industrial property market in terms of leases as well as number and volume of renegotiations.

• Most of the largest transactions (i.e. those over 10,000 sqm) were either contract renewals signed with existing tenants, renegotiations, pre-lets, or instances where a company replaced another existing tenant. None of these transactions impact upon the rate of vacancy.

RENTS

• Incentives in the form of a rent-free period of 3-6 months, cash or extra fit-outs are still being offered. Effective rents are generally 5-15% lower than headline rents.

SUPPLY / VACANCY

• The total of 440,000 sqm was supplied to the market in 2009, with VGP having built the largest hall (51,100 sqm) in Horni Pocernice.

• Despite the lack of new construction there has not been any dramatic decrease in vacancy. The highest vacancy rates still occur in Central Moravia (62%), Pilsen & D5 highway (31%) and Northern Moravia (26%).

• VGP is currently the only developer planning a purely speculative construction - third hall in VGP Park Dobrenice (having successfully leased the second one) and also a smaller facility in Horni Pocernice.

• Although a number of developers actively offered built-to-suit solutions to the market, not all of them were able to deliver such facilities within the time required by the client.

• The sublease trend continues to evolve. Tenants offering space to potential subtenants can be more flexible than developers. Usually, they are also able and willing to accept short-term sublets. The quality of the space, however, is not always comparable to units offered by developers (especially in terms of unit separation, individual energy consumption etc).

Contract renewals and renegotiations accounted for 24% of total activity in 2009.

Industrial property market demand was driven mainly by retailers and logistic services providers.

MONTHLY PRIME HEADLINE RENTS

UNIT SIZE	RENT
500 sqm	€5.00 - €5.40
1,000 sqm – 2,000 sqm	€3.80 - €4.20
2,500 sqm – 5,000 sqm	€3.70 - €4.10
5,000 sqm – 10,000 sqm	€3.40 - €4.00
> 10,000 sqm	€3.30 - €3.60
Built-to-suit solution	€3.60 - €4.00

INDUSTRIAL

Number of large tenders expected to affect the leasing activity in 2010 (consumer goods & retail). Lease renegotiations to rise.

THE MOST ACTIVE DEVELOPERS

DEVELOPER	SUPPLIED SPACE	NEW LEASES
VGP Industrialni stavby	138,700 sqm	67,700 sqm
CTP Invest	91,200 sqm	34,600 sqm
ProLogis	63,900 sqm	44,300 sqm
Panattoni	49,600 sqm	26,500 sqm

TOP 5 INDUSTRIAL TRANSACTIONS

PROJECT	DEVELOPER	TENANT	LEASED AREA
CTPark Modrice	CTP Invest	Electro World	20,800 sqm
Panattoni Park Prague Airport	Panattoni	Domo Service	17,400 sqm
CTPark Brno	CTP Invest	ModusLink	16,900 sqm
ProLogis Park Ostrava	ProLogis	Geis	14,800 sqm
Pohorelice	Outulný	DHL	14,400 sqm

INDUSTRIAL SALE TRANSACTIONS

LOCATION	SIZE (sqm)	BUYER	SELLER
Melnik	11,300	Zasobovani a.s.	PST Ostrava
Prague 10	5,100	TTC Credit	Mediaservis

REGION	PREDICTION OF RENTS FOR EXISTING PREMISES
Prague	↓
Pilsen	↓
Ostrava	↓
The rest of the Czech Republic	→

KEY MARKET PLAYERS

• The industrial market was ruled by VGP, ProLogis and CTP in 2009. VGP generated the largest volume of new leases (67,700 sqm) and ProLogis renewed / renegotiated contracts exceeding 50,000 sqm in total.

• The other large developers such as PointPark Properties, Orco / Heitman, Valad, Goodman, Segro and Amesbury focus on leasing their existing premises and renegotiating existing contracts. In Q3 2009 Panattoni completed the third building in Park Prague Airport and is currently offering the last unit.

• There has been no progress on the sites of Skanska (Jenec), Allfin (Modletice), PDP (Hermanova Hut), Charnwood (Pilsen), AIG (Breclav, Pilsen) and few others. All of these developers are waiting for a pre-lease that would help them secure the financing for their projects.

• Two small projects were completed in 2009 by Omikron Group – one in Nupaky and the other in Hostoun.

• VGP and CTP have supplied a few industrial halls to the market, however, the vast majority of this space was pre-let.

FUTURE TRENDS

• Take-up in 2010 is likely to be similar to 2009. Most developers are still not planning any speculative construction in 2010 (with VGP being the first known exception). Therefore, the competition among developers in various regions is unlikely to change.

• We anticipate demand is most likely to emanate from retailers and logistic operators (mainly generated by tenders issued by producers and retailers).

• Users will continue to renegotiate their existing lease terms in 2010.

• As vacancy remains high, the rent gap between 'existing space' and a new 'built-to-suit' solution will deepen making new construction more expensive.

• The vacancy rate will evolve differently in various parts of the country, impacting rents accordingly. We expect stable situation in Eastern & Northern Bohemia and South Moravia. The volume of premises immediately available on the market will reduce especially in Prague.

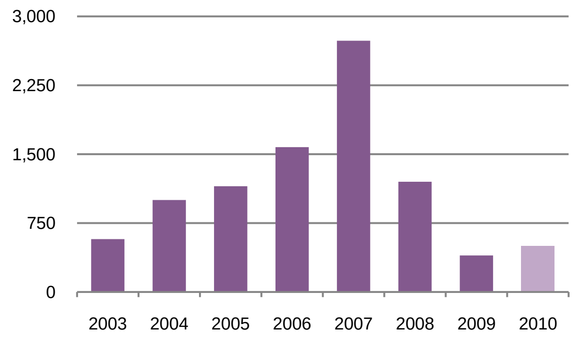
Activity expected in Prague, western Bohemia and northern Moravia.

Omikron Group entered the Czech industrial market with two smaller developments in Nupaky and Hostoun.

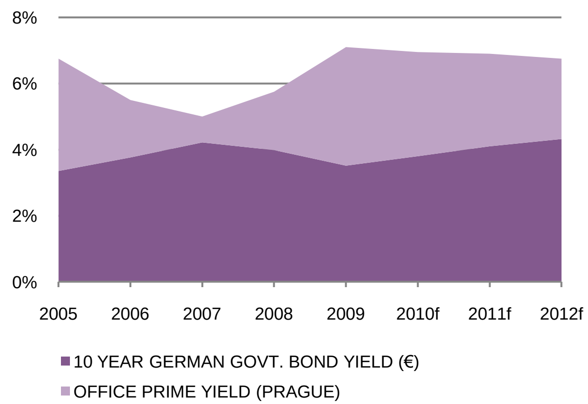
INVESTMENT

Investment volumes decreased by 70% from 2008. Only €360MM were invested in real estate in 2009, which is the lowest recorded volume since the past 6 years.

INVESTMENT VOLUMES (€ MILLION)



YIELDS VS GOVERNMENT BOND (€URO)



SUMMARY

• A total of €396mn was invested in real estate in 2009. Most of it was spent on office properties in the prime locations - Prague 1 and 4 - Pankrac).

• Q4 2009 was the most active period of the year with €276mn invested. DEKA drove this trend with two acquisitions - Gemini for €110mn and Tesco's distribution centre for €36mn. December also saw the largest deal of 2009 - the sale of City Tower to an unnamed private investor for €130mn (equivalent net initial yield of 7.00%). We believe this transaction to have set a new benchmark for prime office properties.

• Other than the three acquisitions from DEKA (Jungmannova Plaza, Gemini, Tesco), activity in 2009 was mostly driven by local investors who had remained passive in previous years, unable to compete with large foreign institutional funds. Local buyers look typically at lower volume transactions (€10–40mn) with higher profit thanks to active management and costs savings.

• To date there have been no distressed sales on the Czech market. We do, however, expect banks to put more pressure on developers struggling to sell their most attractive assets.

FORECAST

• In 2009, most of the investment transactions were financed through equity. We do expect this trend to slowly change and banks to start financing again, for prime properties, at a reasonable level (a 65-70% LTV ratio, with funding at a 200–250 bps margin).

• Although investment activity over the first three quarters of 2009 was mostly driven by private investors, we saw renewed interest from foreign funds, especially German open-ended funds, which we believe will drive activity in 2010. The main target location will remain Prague with a focus on prime office properties providing a steady income stream and value growth prospects.

• The gap between the 10yr German government bond yield and prime yields over the past 5 years is 175bps, on average. The latest OECD forecasts shows that the 10yr German government bond yield should not exceed 4.50% in the next 3 years, therefore we do expect prime yields to stabilize at 6.75–7.00%.

• Industrial and shopping centre yields remained stable over 2009 at 9.50-10% and 7.25–7.50% respectively and are expected to remain stable in 2010.

Prime yields to stabilize at 7.00% through the course of 2010.

Growing interest from private investors (30% of the total volume invested), focused mostly on office properties in Prague.

INVESTMENT

Key Investment Transactions 2009

TYPE	DATE	PROPERTY NAME	LOCATION	SIZE (sqm)	PRICE (€MM)	CAP. RATE	BUYER	SELLER
Industrial	Q4 2009	Distribution centre of Tesco	Postrizin (Melnik district)	60,100	36	7.75%	Deka	Tesco Stores
Office	Q4 2009	City Tower	Prague 4	40,000	130	7.00%	Private Slovak Investor	ECM REI
Office	Q4 2009	Gemini	Prague 4	33,500	110	7.20%	Deka	Immorent
Office	Q3 2009	East Building	Prague 4	6,800	20	8.00%	DBK	Sekyra Group
Industrial	Q3 2009	Kolma 467	Trutnov	26,000	4	N/A	Crescon	Rotoprint
Office	Q3 2009	Budejovicka Alej	Prague 4	11,673	31	7.50%	DBK	ING Real Estate
Office	Q3 2009	Unilever Building	Prague 8	6,570	12	8.25%	Private Slovak Investor	Invesco Real Estate
Retail	Q3 2009	Centrum Brno	Brno	4,900	5	N/A	Private Czech Investor	ORCO
Hotel	Q1 2009	Acc-Nifos Atom Hotel	Ostrava	193	6	N/A	CPI	N/A
Office	Q1 2009	Jungmannova Plaza	Prague 1	10,300	41	6.75%	Deka	Immoeast AG

Offices in established locations are the most attractive assets.

Prime yields always remained at around 6.75% – 7.25%, which is a correction of only 125 basis points compared to 2008.

DEFINITIONS

EFFECTIVE RENT – includes all incentives and discounts offered by the developer / landlord. The effective rent is therefore always lower than headline rent and represents the true rent considering rental concessions, spread over the life of the lease.

HEADLINE RENT – is stated in Lease Agreements and does not include any incentives or discounts provided by the developer / landlord.

INCENTIVES – usually in the form of rent free period, cash, higher standard of the premises (extra fit-outs etc).

VACANCY – represents the share of all existing premises that are vacant (i.e. immediately available to potential tenants). Can be expressed as percentage of the total existing stock (being the rate of vacancy) or in sq m as the total volume of existing vacant space. Premises that are still under construction or planned are not taken into account.

(TOTAL) LEASING ACTIVITY / TAKE-UP – takes into consideration all new leases, pre-lets, expansions, renegotiations, relocations and subleases.

NET TAKE-UP – takes into consideration all new leases, pre-lets, expansions, (renegotiations, subleases or contract renewals are not included)

AVAILABILITY – includes existing vacant space and space which is under construction and has not been pre-let.

YIELD / CAP. RATE – rate of return on capital (income) expressed as a compound annual percentage rate.

LTV RATIO / LOAN-TO-VALUE RATIO – ratio between a mortgage loan and the value of the property pledged as security expressed as a percentage.

CITY CENTRE – Office projects located in Prague 1

INNER CITY – Office projects located in Prague 2, Prague 3, Prague 4 – Pankrac, Prague 5 – Andel, Prague 8 – Karlin

OUTER CITY – Office projects located in Prague 4 – rest, Prague 5 – rest, Prague 6, Prague 7, Prague 8 – rest, Prague 9, Prague 10

CONTACT US

CZECH REPUBLIC

Mysak Gallery
Vodickova 710/31
110 00, Prague
Phone: +420 226 537 618
Fax: +226 013 579
e-mail: prague@colliers.cz
www.colliers.cz