THE ADVISERS
Prime Property

2010 ROMANIA MARKET OVERVIEW

Annual review & outlook

HIGHLIGHTS

- Office supply levels increased significantly in Bucharest as around 400,000 sq m of new space was delivered to the market in 2009, a factor exacerbated by the release of approximately 50,000 sq m by tenants. In conjunction with weakened demand from occupiers this has placed rents under downward pressure, although they are expected to stabilise by the end of 2010.
- The aggressive expansion retail strategies from 2006-2008 were replaced by optimization of resources, restructuring and even the closing of shops in 2009.
- New industrial supply is likely to be at a minimum in light of the lack of available development financing. Industrial park owners will not lower rents, but most of them will attempt to attract clients through other means, offering an increased attention to key efficiency indicators.

in association with Knight Frank

Contents

1. OFFICE MARKET

Supply

2009 was a record year in terms of new supply in Bucharest, with approximately 400,000 sq m delivered in 35 buildings, double the total achieved in 2008. In fact, the new space accounted for half of the total office stock at the end of 2008, bringing the total supply to around 1.25 million sq m.

Despite the increased levels of new supply in a time that could not be worse due to decreased demand, only 21% of the new deliveries had central locations whereas more than 45% were situated on the outskirts of the capital. Most of the new buildings had leasable areas below 10,000 sq m, with only one third exceeding this level. The increased number of small buildings available is in line with the difficult economic situation.

Tenants released almost 50,000 sq m of space, mainly in peripheral areas, therefore increasing the office market supply. The reasons that stood behind the decisions to sub-let space were mainly focused on the need to reduce costs in order to better cope with the crisis or as part of a consolidation strategy, of grouping all divisions of a company under the same roof by moving to new space and sub-leasing their previous accommodation.

Compared to previous years when the vacancy rate was close to zero in prime areas, in 2009 it increased significantly in all locations, but mainly on the outskirts of Bucharest, reaching an overall rate of approximately 20%. Only 60% of the space delivered last year was leased, the highest occupancy rate being registered in the semi-central areas.

Metropolis is a 11,000 sq m GLA development completed by Soravia in Bucharest

ALMOST 60% OF DEMAND WAS CONCENTRATED ON THE SEMI-CENTRAL AREAS AND 35% IN DOWNTOWN BUCHAREST


Floreasca Business Park, developed by Portland Trust, with 35,000 sq m GLA

Demand

In 2009, total take-up in Bucharest slightly exceeded 100,000 sq m, half of the level registered in 2008. The number of transactions increased in the second half of 2009 following a very quiet first half of the year, indicating market improvement that is expected to continue through 2010.

Almost 60% of demand was concentrated on the semi-central areas and 35% in downtown Bucharest. The decreased rents and the increased number of incentives made central and semi-central locations more affordable to tenants, while the peripheral areas were the least preferred option .

The average transaction was around 1,000 sq m, significantly smaller than in previous years. In fact, more than 50% of all leases were signed for less than 1,000 sq m while only 10% for areas above 5,000 sq m. The largest transaction of 2009 was the 15,000 sq m lease signed by Banca Romaneasca in BOC, a newly delivered building located near the Pipera subway station.

In contrast to 2008 when pre-leases accounted for approximately 80% of all transactions, most deals completed in 2009 were renewals or relocations. The reason for the small number of pre-leases was the difficulty in reaching decisions as the financial crisis made companies unsure of what might happen even in the short-term. Additionally, given the large existing supply on the market, tenants had multiple alternatives without having to wait 12-18 months to secure a good location, as would have been the case prior to 2009.

Tenants keen on reducing costs looked for the best option on the table. There were cases when they negotiated simultaneously a renewal of the existing lease or relocation to a new space. This clearly shows 2009 was a tenants' market.

The most active players on the market were companies from the financial sector, representing almost 25% of total demand, followed by public institutions and the service industry, with approximately 20% each. Pharmaceutical companies as well as utility companies constituted other important sources of demand. Compared to previous years, two novelties could be noticed when analyzing the distribution of demand based on activity domains: the appearance of a new category among the top 5 players represented by public bodies such the City Hall of Bucharest or the City Hall in District 1, as well as the significant decrease of requests coming from automotive firms.

THE AVERAGE SIZE OF TRANSACTIONS WAS AROUND 1,000 SQ M, SIGNIFICANTLY SMALLER THAN IN PREVIOUS YEARS


Peripheral Area
Tunari Forest
Baneasa
Forest
E60
Sector 1
Semi-Central
Sector 2
E60
E60
E85
Sector 6
Sector 3
Central
Mill Lake
Sector 5
Sector 4
Lake Cernica
E85
E60
E81
A2
Lake
Vacaresti
E70
E70
DN5
DN4
Cornetu
Forest

Table 1
Key office leasing transactions

No	Tenant name	Building	Area	GLA (sq m)	Agency
1	Banca Romaneasca (member of National Bank of Greece Group)	BOC	Semi-Central	15,000	Direct
2	Bucharest's General Mayor	Riverside	Central	12,556	Direct
3	Transelectrica	Platinum	Central	6,730	Direct
4	Sector One's Mayor	Bucuresti-Ploiesti	Semi-Central	6,235	Direct
5	PubliMedia	Aurel Vlaicu 62-64	Semi-Central	6,000	The Advisers/Knight Frank
6	Large Pharmaceutical Company	Izvor 80	Central	3,500	The Advisers/Knight Frank
7	GFK	BOC	Semi-Central	3,000	Direct
8	Romexterra	Elefterie 18	Central	2,700	The Advisers/Knight Frank
9	Ericsson	West Gate Park	Peripheral	2,300	Direct
10	BAT	BBP	Semi-Central	2,100	The Advisers/Knight Frank

Source: The Advisers/Knight Frank

A LARGER NUMBER OF TRANSACTIONS ARE EXPECTED TO BE FINALIZED TOWARDS THE END OF 2010 AND INTO 2011


Lakeview, developed by AIG Lincoln and BSGS, with 24,000 sq m GLA

Table 2
Class A office average rents (€ per sq m per month)

Location	Central	Semi-Central	Peripheral
Net Effective Rent	16-18	14-16	10-12

Source: The Advisers/Knight Frank

Moreover, demand was fairly equally distributed between local and international companies. While international firms had to wait longer for approvals from abroad, national companies were more connected to the local market and had simpler management structures which allowed them to reach decisions faster.

Rents

Rents experienced a downward trend in 2009 due to the increased vacancy rate, dropping on average by 15%-20% in central locations and even more in peripheral areas. Being measured at cost on the open book system, service charges are sensitive to changes in the structure of expenses and depend upon the service quality requested by tenants. Service charges did not increase in 2009, unlike during previous years. If at the end of 2008 the estimated service charge for a class A office building was between 4-5 EUR/sq m/month, at reconciliation there were several cases where the real cost was smaller than the estimated one. This was possible in part due to smaller costs negotiated by landlords with the service providers. Thus, service charges for a class A office space were in the range of 3.5-5 EUR/sq m/month.

Institutional landlords continued paying considerable attention to the quality of services provided to tenants, their attitude being embraced by an increasing number of local building owners who also started offering better services. Besides the financial incentives, the quality of the services provided started being a very important factor in the tenant decision matrix, whether to extend the contract in the same location or to relocate.

Along with rent decreases, several types of incentives were granted by landlords to attract new tenants and to keep current ones. The most common incentives were rent free periods, fit-out contributions, break-out options or shorter contract terms. There were even cases where the new landlord paid penalties on a tenant's existing contract so that tenants could exit their existing agreements and relocate to new buildings.

Forecast

New office supply is expected to reach approximately 250,000 sq m in 2010, 60% of the record amount delivered last year. Landlords have re-focused and started to mainly target the central and semi-central locations after facing high vacancies in the large developments built on the outskirts.

Deliveries during the next two years are uncertain, due to the still difficult access to financing corroborated with the projects' sizes proposed for development, many of which exceed 30,000 sq m. Since a great number of leases expire in 2010-2012 and new development works are rather scarce, the vacancy rate is likely to start decreasing towards the end of this year and the beginning of 2011.

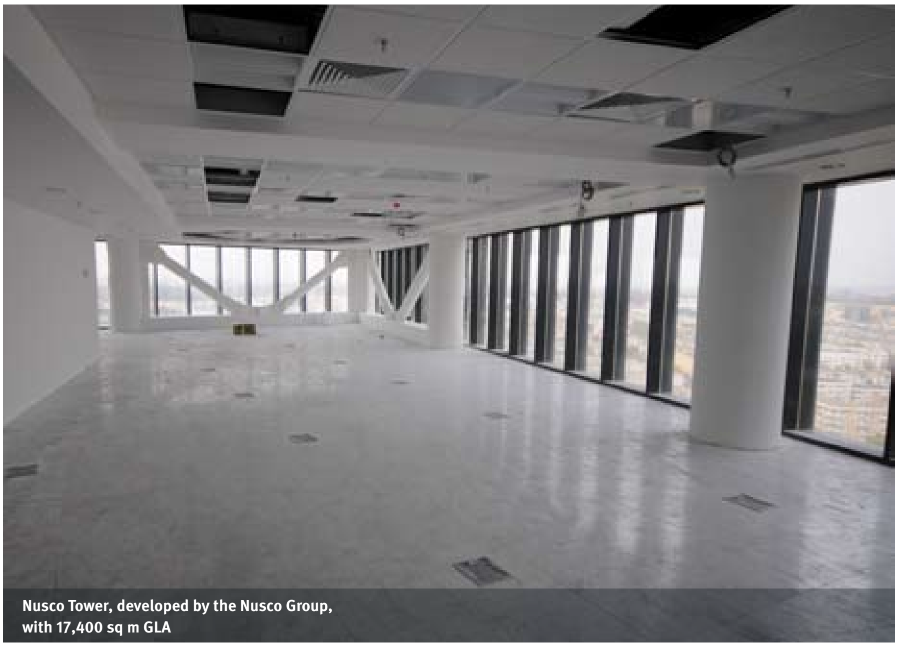
An increase in demand is likely to occur this year, and thus a larger number of transactions are expected to be finalized towards the end of 2010 and into 2011. We believe tenants will maintain a dominant position at the negotiation table this year, although the situation may change in the coming years as the current lack of financing for new projects will lead to a lack of sufficient supply.

Companies will continue targeting the central and semi-central areas while the

Euro Tower, Bucharest developed by Cascade Group, with 16,500 sq m GLA

average size of units leased is likely to increase to 1,500-2,000 sq m. The local office market has started maturing, as evidenced by the development of the first buildings with green features. Demand for this type of accommodation is mainly coming from multinational companies with a strong corporate culture of improving the sustainability of the environment. An environmentally friendly building may be more appealing to tenants due to lower operationg costs and increased corporate responsibility. From a landlord's perspective, it increases the chance of leasing the space quickly to better quality tenants, as well as making it attractive to potential investors. Bucharest can boast two almost completed buildings with a BREEAM rating of "very good", The Lakeview, developed by AIG/Lincoln and BSGS, and Euro Tower, developed by Cascade Group. Besides these, several other projects have been announced which will follow the trend of the green concept.

Rents are expected to further decrease slightly in the coming months, stabilizing towards the end of 2010. Moreover, tenants will shift their attention from the already reduced rent levels to the efficiency of the space, placing higher emphasis on the methods used for the measurement of the leasable area (BOMA/ GIF) or the level of the add-on factor.



Nusco Tower, developed by the Nusco Group, with 17,400 sq m GLA

RENTS ARE EXPECTED TO FURTHER DECREASE SLIGHTLY IN THE COMING MONTHS, STABILIZING TOWARDS THE END OF 2010

2. RETAIL MARKET

Looking back now, 2009 was a year of economic turmoil and uncertainty. The retail market was more or less anemic, with lots of projects being either stalled or permanently abandoned due to credit conditions.

Supply

Eight new shopping centers delivered to the market in 2009 and several extensions of existing retail developments increased the retail stock* increased by more than 230,000 sq m, to almost 1.5 million sq m across Romania.

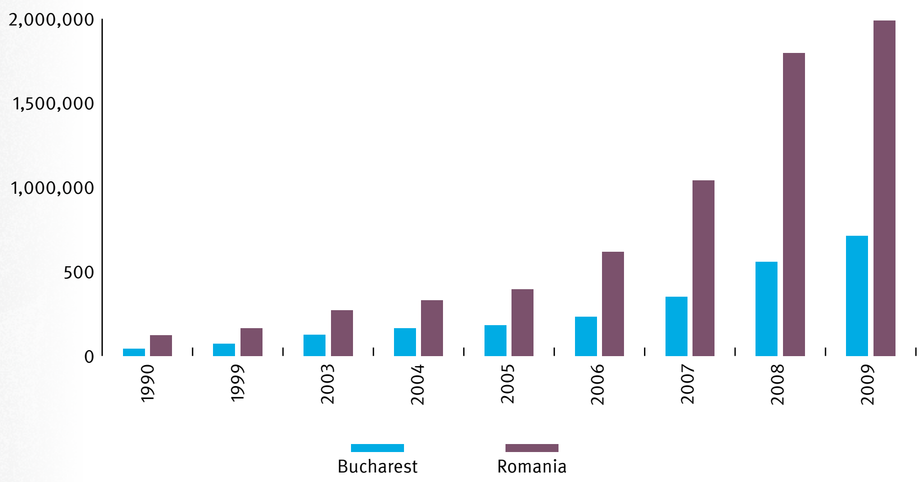
A total of 167,000 sq m of the retail space initially planned for delivery in 2009 has been put on hold indefinitely, while 163,000 sq m of retail space has been postponed to open in 2010.

We have calculated stock figures for cities with more than 100,000 inhabitants. Thus, Suceava, Pitesti, Sibiu, Cluj and Bacau, in this order, rank highest in terms of retail stock per person. At the other end, Deva, Ploiesti, Satu Mare, Craiova and Galati have the lowest stock of modern retail per person.

A glimpse back at the short history of the modern retail market in Romania shows that 2009 was the first real test period for all the players in this sector.

Well established shopping centers, recently opened retail schemes and planned projects – were all put to trial. Those who had taken substantial risks had their nerves tested, while cautious investors or lucky sellers of 2006-2008 congratulated themselves for their flair. All in all, the general belief is that only the most professional will be able to make it through the crisis.

Figure 1
Bucharest and Romania stock
sq m of GLA



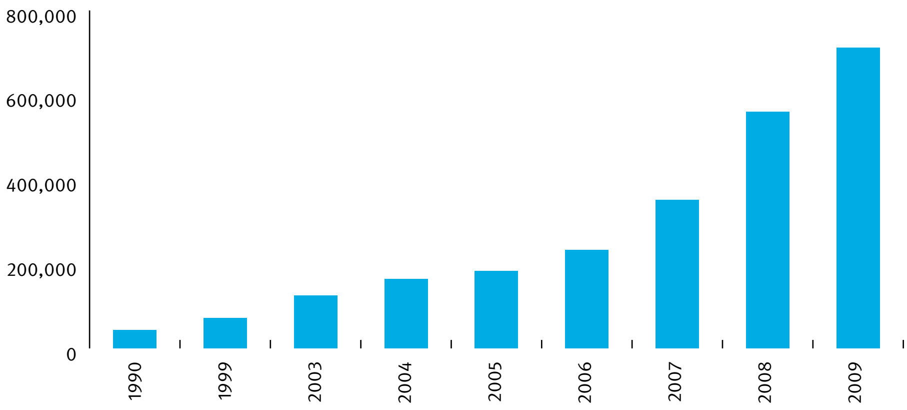
Source: The Advisers/Knight Frank

*The stock of modern retail takes into consideration traditional shopping centers, retail parks and outlets. In the case of stand alone big box units, we took into consideration only the size of the shopping gallery attached if it exceeds 5,000 sq m of GLA.

Figure 2

Bucharest retail stock

sq m of GLA



Source: The Advisers/Knight Frank

THE AGGRESSIVE EXPANSION STRATEGIES FROM 2006-2008 WERE REPLACED BY OPTIMIZATION OF RESOURCES, RESTRUCTURING AND EVEN THE CLOSING OF SHOPS IN 2009

There have been memorable episodes, such as the first closures of shopping centers in the local market due to their poor performance or the changing of a center's concept, as was the case for Armonia Braila and Trident Shopping Center Sibiu. Although closures also happen in mature markets, even during good economic conditions, they constituted an alarm signal for most players in Romania, urging an increased caution in future development plans. They provided the proof that an emerging market is more volatile and weaker than a mature one when faced with a crisis.

This somehow tumultuous background was counter-balanced by the overwhelming momentum created around the opening of AFI Palace Cotroceni, the largest shopping center in Romania. Even retailers that had signed lease agreements were facing the same dilemma with those still looking to expand: to open or not to open in AFI Palace Cotroceni. In the end, decisions were made and the occupancy rate proved that retailers trust the potential of the Romanian retail market.

The crisis affected not only new supply, but also the overall vacancy rate which was higher than in 2008. Nevertheless, the shopping centers that performed well before the end of 2008 succeeded in maintaining a comfortable occupancy rate, despite the need to replace some of the tenants. Still, there were extreme cases where 50% vacancy rates were recorded. Similarly to previous years, shopping centers in cities other than Bucharest were confronted with significantly higher vacancies than those situated in the capital city.

Demand

The aggressive expansion strategies from 2006-2008 were replaced by optimization of resources, restructuring and even the closing of shops in 2009. Overall demand dropped as a result of the anxiety created by the current economic downturn.

Given the rising unemployment rate and the reduction in consumer spending, mid-price retailers were put under a lot of pressure as shoppers bought only basic products. However, the discount stores and the food operators still enjoyed good performances. The most affected were the local retailers and those whose expansion was based on loans.

The entrance of discount stores into shopping centers was one of the few measures taken to adapt to the current conditions of the market. While in previous years discounters tended to operate only in individual locations, in 2009 they replaced some of the supermarkets that anchored traditional shopping centers (such as Penny Market in Galleria Suceava).

Although suffering from a decrease in sales volumes, some of the international retailers perceived all these changes as opportunities, especially in the second half of the year when the initial shock was over. They secured very good locations in existing shopping centers that were out of reach before, due to the close to zero vacancy rate. Zara is one of the examples that used the opportunity to enter into Bucuresti Mall.

Bucharest claimed the spotlight in 2009 in terms of the highest demand, partially generated through the opening of Grand Arena, Militari Shopping Center and AFI Palace Cotroceni. Despite the crisis, a large number of retailers opened their first units in Romania last year (C&A, Decathlon, Desigual, Gap, Imaginarium, Kiabi, Mladinska, Norauto,

Victoria City Center to be developed by CD Capital Partners in Bucharest.
Exclusive assignment of The Advisers/Knight Frank

BEARING IN MIND THAT THERE ARE RETAILERS WILLING TO EXPAND, THE PERIOD IN WHICH RENTS WILL CONTINUE TO DECREASE REMAINS UNCERTAIN

Smyk). Although there were a few exits from the market (Alexandra Books, Glou, Jack Wolfskin), the number of newcomers was much higher, showing retailer confidence in the recovery of the market.

In order to better understand the dynamics of the market, it is important to point out that a large number of international brands are present in Romania through local partners. As the local partners' strengths do not compare with those of the parent-companies, the expansion of these international brands has been either stopped or slowed down. With this in mind and having noticed the tremendous potential of the Romanian market, some parent-companies decided to step in and continue the expansion on their own (e.g. Mango, Promod), each with their own strategies.

Therefore, as the proportion of local brands is low in comparison with the international ones present in Romania and as the local partners' strength has been seriously put to trial through the crisis, the retail market was mainly driven by the international brands in 2009.

2009 was also the year with the largest number of insolvencies in retail, around 8,000 based on data obtained from the Trade Registry. As alarming as this number sounds, this total includes many of the small, corner-shop businesses that are mainly found in residential areas. At a closer glance however, the number represents approximately 0.8% of the total. Indeed, local retailers were the most affected, being forced to declare insolvency, in order to protect themselves against their creditors. They either closed all their stores, as in the case of PIC, Ultra Pro, Trident, or only the inefficient ones, as seen at Leonardo, Flanco and Mondex.

Rents

In 2009 the renegotiation of rents was top of the agenda for tenants trying to limit the negative effects of the crisis. Most rent reductions were granted on short periods of 6 to 12 months, but there were few cases where the new rent will last until the termination of the contracts. The overall rent decrease was in the range of 25% to 50% based on the performance of the shopping centers and the landlords' interest to maintain the occupancy rate.

In order to close new deals landlords had to structure leases in a tenant friendly manner. Based on this, the retailers have come up with a number of incentives, such as: turnover rents, possibility of terminating the contract in case an agreed occupancy rate is not reached at the opening of a shopping center, break options or fit-out contributions. However, overall, only some landlords accepted such clauses to attract major tenants.

Several of these new incentives stipulated by retailers make financing difficult to obtain for upcoming projects. Therefore, in order to maintain a sense of direction in this market, it all basically comes down to risk management for both developers and retailers, that is, knowing when to stop and commit to a choice in multiple, uncertain scenarios, in order to optimize profits with minimum costs.

Signs of an early maturity of the local market are backed up by the fact that nowadays rental levels are the result of a comprehensive analysis regarding the purchasing power of the population in the target area and the sale potential of the chosen space.

Forecast

At least four projects currently under construction are likely to be delivered in 2010. Approximately 200,000 sq m of GLA will be delivered all over Romania, out of which Sun Plaza (80,000 sq m of GLA), Atrium Center Arad (29,500 sq m of GLA) and Gold Plaza Baia Mare (30,000 sq m of GLA) were initially planned to open in 2009.

Usually, a shopping center development takes two to three years to be completed, depending on the size. As the previous 12-18 months brought no financing for the retail segment, new deliveries of shopping centers remain almost insignificant until the end of 2012.

Even though by the end of 2008, the projects in the pipeline were the darlings of the retail market, there is currently more than 3,000,000 sq m of GLA remaining at the stage of nice, colored brochures, with no clear delivery dates.

In Bucharest alone, there were more than 1,000,000 sq m of GLA announced. Out of this impressive figure, aside from 90,000 sq m of GLA that are planned to open in 2010, only Victoria City Center (68,000 sq m of GLA) and Pallady Shopping Center (85,000 sq m of GLA) have a confirmed opening date, for 2012.

Retailers looking for expansion will have to take into consideration either opening high street locations or choosing from the best performing existing schemes, as new developments will be scarce. Existing malls delivered less than 2-3 years ago will continue struggling for stability, while good property management will become more important than ever.

Bearing in mind that there are retailers willing to expand, the period in which rents will continue decreasing remains uncertain. This trend is bound to be maintained for the first half of 2010 given the relatively low level of consumer spending. Since financing conditions have gotten worse and with the new terms introduced byretailers, only fresh management decisions will make possible the closing of transactions on future projects. In order to improve, the market will have to shift from a reactive attitude, by trying to cope with the effects of the crisis, to a pro-active attitude, in trying to achieve the best results within the current economic environment.

If approved, the introduction of the fast food tax is going to affect an even greater proportion of retailers as well as consumers, already shaken by the crisis.

High street

Compared to previous years, 2009 brought different conditions to the high street segment: sufficient supply, but smaller demand. Not only did a large number of units become vacant, but stock also increased with deliveries of space in office buildings completed in 2009, contributing to a higher vacancy rate.

A new trend has been witnessed in terms of demand, leading to the opportunity of changing the image of the high street market. Tenants previously interested only in securing space in shopping centers started looking for high street units as well, especially in the area between Romana and Unirii.

As in the case of shopping centers, rent reductions were also granted depending on the tenants' networks.

15,000 sq m GLA industrial space + 3,000 sq m GLA office space, developed by EyeMaxx Real Estate

3. INDUSTRIAL MARKET

Together with the office segment, the industrial market proved to be the last affected by the downturn. The evolution of the industrial sector during the second half of 2008 was just a preview of things to happen in 2009. Caution was the guiding rule for both developers and tenants throughout 2009. Developers put projects on hold, while tenants were very prudent with their moves. 2009 saw the stabilization of the rents whereas the vacancy rate slightly increased.

For the first time in recent years the deals done outside Bucharest have been the icing on the cake. The development of the nation's infrastructure represents a constant concern for market players, who have to plan their strategy accordingly. Cities situated along the new Transilvania highway will be appealing in the medium term.

Supply

Bucharest's industrial stock passed the 900,000 sq m mark in 2009. If in H1 2009 developers reduced their construction pace, bringing to the market just 33,500 sq m. In H2 no new space was delivered. Compared to the deliveries from 2008 and 2007 those from 2009 posted a decrease of 90% and 85% respectively.

No new project was brought to the market in 2009; new supply was in the form of new phases in existing developments. The western part of the city remained the preferred destination for industrial developers, as 90% of the new deliveries in 2009 were built either along the western ring road or the A1 highway to Pitesti.

Demand

Demand was affected by the difficult economic environment. Potential occupants took a cautious approach and tried to be more cost efficient. This translated into longer decision periods and the reduction of the average deal sizes.

Total take up in 2009 reduced significantly, reaching 65,000 sq m, a third of the previous year's total. Demand came mainly from logistics companies and retailers. The low level of interest coming from new clients drove the vacancy rate above 10%, double compared to 2008.

During recent years the largest transactions in the country were registered in Bucharest: Carrefour (45,000 sq m), Centrum

(20,000 sq m) and Frans Maas (30,000 sq m). In 2009 though, the major deals in the industrial sector were closed in other cities. Two transactions stood out from the rest due to their size. In the attempt to serve the units situated in Transilvania and Banat, Carrefour opened a 20,000 sq m warehouse near Deva. Moreover, Unilever secured a 30,000 sq m facility in Ploiesti West Park, which was the largest transaction in the country in 2009.

Rents

Rents remained constant throughout 2009. Even if there was pressure coming from the increasing vacancy rate, most of the developers maintained their rent level due to the initial construction costs. Furthermore, they were aware of the impact a rent decrease would have on the value of their projects. The service charges were situated between 0.5 and 1 EUR/sq m/month depending on the quality and services offered and the level of local property taxes.

The tendency on the real estate market is to negotiate the rent downward. The industrial sector is probably the least affected segment for the moment, as expected new deliveries are few and a balance is kept between demand and supply.

Forecast

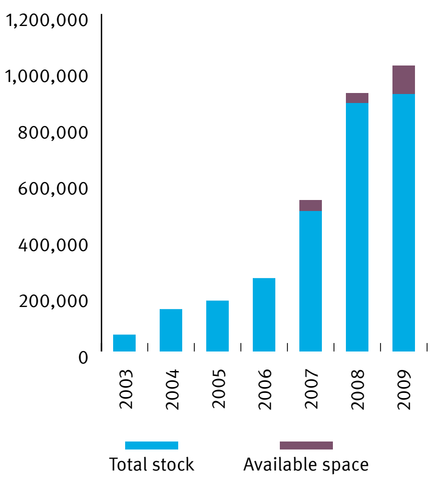
New supply will be scarce as financing is difficult to obtain and potential tenant interest has decreased. In 2010 we will likely see similar deliveries and take-up as in 2009. Industrial park owners will not lower rents, but most will attempt to attract clients through other means: more competitive service charges, access to railway, improvements of truck access and overall increased attention to key efficiency indicators.

Table 3
Prime rental ranges

Size (sq m)	Rent (EUR/sq m/month)
‹ 3,000	4.30-5
3,000-10,000	4.10-4.30
› 10,000	3.60-4.10

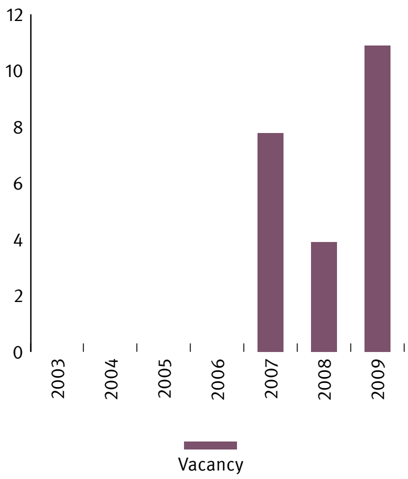
Source: The Advisers/Knight Frank

Figure 3
Total stock and available space
sq m



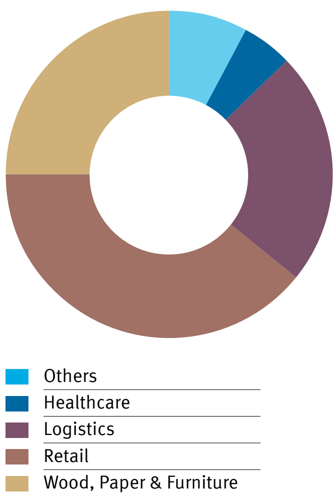
Source: The Advisers/Knight Frank

Figure 4
Vacancy
%



Source: The Advisers/Knight Frank

Figure 5
Take up by sector
%



Source: The Advisers/Knight Frank

4. LAND MARKET

In 2009, the economic crisis affected the land segment the most out of the whole real estate market. After several years of record transaction levels, 2009 marked a total standstill with no notable transactions. It was a difficult period for companies that purchased land in recent years with high levels of borrowing. They had to postpone their projects and restructure their loans.

Many owners put their properties up for sale with significant discounts compared to previous years, but finding buyers was in many cases impossible. The few buyers present on the market felt that "the bottom" had not been reached and preferred to wait. The poor demand and the increased supply of land for sale triggered a decrease in asking prices. As few transactions were made we can only estimate the trend in prices by observing the reduction in the owners' expectations. In central areas asking prices decreased between 30% and 50%, while in peripheral areas the decline was much sharper, estimated between 50% and 70% of the levels from the market peak of H1 2008.

Throughout the entire year, land transactions were isolated with no notable patterns observed. The only active buyers were either speculators or companies interested in acquiring sites suitable for their business: retail discounters, hypermarkets and medical units. As their core business is not real estate they were interested in buying sites with the relevant zoning already approved. In 2009 the transaction volume was a twentieth of that in 2007.

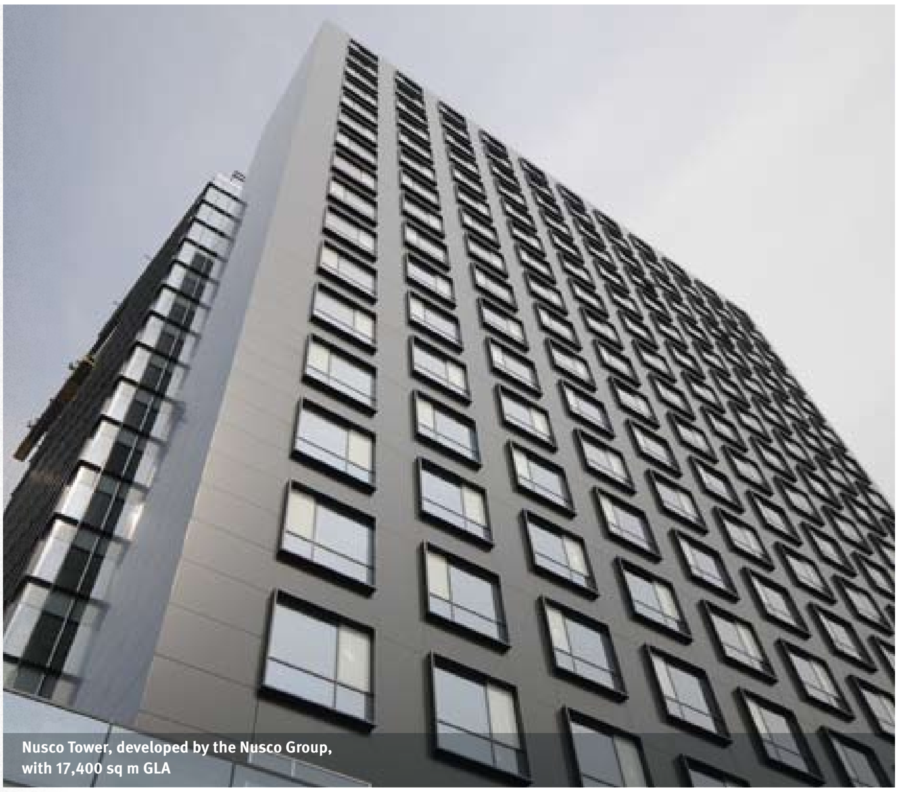
Demand was focused on small sites situated in central areas of the capital with clear zoning and good development coefficients. Furthermore, opportunistic buyers showed interest in different types of land, attracted by the substantial price reductions.

The largest transaction of 2009 was made in Bucharest by Liebrecht & Wood on the outskirts of the city. The company bought 60 hectares for retail purposes for an estimated 30 million EUR. Another transaction marked a first for the market: Raiffeisen Bank appointed PWC to liquidate a 124 hectare site located in Crevedia belonging to EFG Crevedia. The transaction was closed at 11 million EUR, a 75% discount compared to the value estimated by the owner at the peak of the market in 2008. It was the first forced sale of a large site in Romania since the start of the crisis.

Although the market was very quiet from the transactions perspective, important changes were made as concerns zoning regulations during 2009. The new zoning law adopted is an attempt to bring some clarity to a troubled domain. As a result, building permits will be more difficult to obtain and the development alternatives for land will not be so permissive compared to previous years. This new law will give an advantage to owners who already received the building permit for their properties.

After one and a half years of hibernation we expect a slow recovery in investor interest for land in 2010. The fall in land prices will see speculative interest from investors with long-term strategies who are targeting good locations for their projects.

5. INVESTMENT MARKET



Nusco Tower, developed by the Nusco Group, with 17,400 sq m GLA

The Romanian real estate investment market fell in line with the economic trend and failed to produce any surprising results during 2009. The figures in 2009 were similar with the ones recorded in 2003 when the market was in an incipient phase of development.

In the early 2000s the major setback was related to the lack of prime properties available on the market which is quite different from the present situation when the lack of financing and market uncertainty has kept the investors away.

Banks played a significant role in the evolution of the market. Their reluctance in providing loans made it almost impossible to conduct any investment transaction. On the other hand, banks tried to restructure existing loans to the detriment of sales at forced values.

Compared to other years, 2009 saw prime properties offered for sale in all market segments: office, retail and industrial, in Bucharest and in the rest of the country. Even if landlords decreased their asking prices, their expectations could not be fulfilled by the few investors still present on the market.

Foreign investors had viewed Romania as a secondary market and their perceptions worsened in 2009 due to the poor economic performance of the country. Even if they could identify premium properties in Romania, they focused more on the stable, mature markets of Western Europe.

Few transactions occurred in 2009 in Romania, most of them being complex and involving debt-takeovers, mergers or share payments. The turnover of these transactions barely exceeded 200 million EUR, an eight fold decrease compared to the maximum registered in 2007. Negotiations for some of the deals had been started in previous years, but the transactions were closed in 2009.

At the beginning of 2009 Dinu Patriciu's Black Sea Global Properties acquired the portfolio of the AIM listed company, Fabian Romania, for 50 million EUR. The portfolio includes 11 properties situated in Bucharest, Oradea, Satu Mare and Timisoara. The Austrian based company, Immoeast, the largest investor on the real estate market in Romania, took over the projects of its former partners, Eyemaxx and EFG (European Future Group). Eyemaxx's portfolio includes industrial projects while EFG had four mixed-use developments under planning or construction.

The largest two transactions took place in the second half of the year, both of them involving retail units. Enterprise Investors acquired 65 Profi units for 66 million EUR. NEPI (New Europe Property Investments) purchased the European Retail Park Braila for 63 million EUR from Belrom. Among the tenants were Carrefour, Media Galaxy and Staer. The transaction involved debt-takeover and a share exchange between the two companies.

Other transactions completed in 2009 include the purchase of the Hello Hotel Bucharest by Immorent and four Prodas stores in Bucharest by Mega Image.

Due to the low level of investment activity on the market it is quite difficult to estimate the yield range. The few transactions completed in 2009 were very complex and their main argument was the rescue of the sellers' cash flows in difficult times rather than achieving certain investment margins. Thus, the number and structure of these transactions provide insufficient information in order to have a clear understanding of the yield level.

Even if 2010 is a difficult year for the property investment market, it is expected to be better than 2009. In the fourth quarter of 2009 potential buyers' interest increased. Corroborated with a more realistic approach from the owners side it could lead to more transactions in the coming year.

6. REVISED ZONING AND BUILDING PERMITTING RULES

Florian Nitu,
Managing Partner,
Popovici Nitu & Asociatii

During 2009 certain interesting and practical regulation changes in real estate development and construction business have been enacted. Revisions were driven in two directions, namely: (i) land planning and zoning, where the law was amended successively during 2009[1] and (ii) construction works/ building permitting, with clarifications to the famous enactment of 1991[2].

Historically, the conversion of the economic use of a land plot (from agricultural use to urban/construction use) has raised various concerns and very high conversion costs. It is a complex procedure, with the need to involve central government authorities in authorizing the conversion process (when speaking about substantial areas of tens or hundreds of hectares).

Under the new land planning rules, once a land plot (initially qualified as agricultural) is included under the coverage of a General Urban Plan (the PUG) and on such a basis designated as urban land (in Romanian: intravilan), the procedure to convert the economic destination and the removal from agricultural circuit are no longer required.

Significant debates were triggered by the so called *"20% zoning coefficients rule"* that became effective (in practice) during the last year. For ease of reference, one should consider that zoning improvements (in terms of construction volume and density on a land plot) can no longer exceed 20% as compared to the PUG provisions or pre-existing zoning rules. However, certain related clarifications are required.

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[1] Law 350/2001 on land planning and urbanism amended by (i) Law no. 242/2009 on the approval of Government Ordinance no. 27/2008 amending and completing the Law 350/2001 on land planning and urbanism, published in the Official Gazette no. 460 as of 03/07/2009 and (ii) Law no. 345/2009 amending and completing the provisions of article 36 of the Law no. 350/2001 on land planning and urbanism, as published in the Official Gazette no. 778 as of 13/11/2009

[2] Law 261/2009 on the approval of Government Ordinance no. 214/2008 amending and completing the Law no. 50/1991 on construction works and building permitting, as published in the Official Gazette no. 493 of 16/07/2009

Floreasca Business Park, developed by Portland Trust, with 35,000 sq m GLA

First, the concept of CUT (land usage coefficient or the building volume/density), remains the only referential for the "20% zoning coefficient rule".

Secondly, after many years of vague interpretation, the concept of POT (in Romanian: *procentul de ocupare a terenului*) has finally been defined by reference to the internationally acknowledged concept of *building footprint*.

However, when within a new or revised zoning process that proposes an adjustment of CUT that is below the 20%, one should consider that the feasibility prior approval to such revised zoning (in Romanian: *avizul prealabil de oportunitate*) is no longer required. Many market professionals would definitely recall that issuance of such feasibility prior approval used to be, in most cases, a cumbersome process, particularly when not issued through the Chief Architect Division and the Mayor, but by the Municipality council.

Finally, under the revised regulations, higher qualification standards have been set for the chief-architect position with Municipalities and secondary regulations are still to come on this matter.

Construction works/ building permitting

We have counted three major areas were significant regulation changes have been implemented during 2009, which may be summarized as follows.

A limitation of pre-existing building's extensions and functionalities conversion has been provided, in the form of a rue similar to the "20% rule", according to which no pre-existing building may be extended by more than 20% gross area. It has been further imposed that a change in building functionality (in the context of an extension) could in no event conflict with the PUG and PUZ rules.

On the administrative side we have seen the powers and enforcement tools of the authorities strengthened – such as the expressly regulated right to demolish buildings erected without a building permit in the public domain. In such cases, a demolition permit is no longer required. There are also new rules intended to accelerate the granting of build permits (such as the generalization of the *tacit approval principle* to the applications for various pre-permits required under a Certificate of Urbanism, according to which no reaction from the authority within 15 days from submission of application or file triggers tacit approval to that application and file).

Finally, the most visible change in the regulation is of an economic nature. Indeed, after years of controversies (and various litigations, including numerous unconstitutionality motions), the obligation imposed to project owners to contribute with 0.5% out of their project construction budget to "Casa Sociala A Constructorilor" (Social Housing) has been expressly repealed.

PRICEWATERHOUSECOOPERS

7. INVESTMENT PROPERTY – ACCOUNTING AND TAX MATTERS


Francesca Postolache

Authors:

Francesca Postolache, Director, Real Estate Leader

Gabriela Marinete, Manager of the Audit Department

The article presents some of the main accounting concepts related to investment property with references to both International Financial Reporting Standards (IFRS) and Romanian Accounting Standards (RAS).

Investment property represents land and buildings held to earn rentals or for capital appreciation or for both. Assets used by entities for their own purposes do not meet this definition. Under IFRS, there is a separate standard that deals with investment property (IAS 40). Under RAS, investment properties are classified as tangible assets, similarly to all other assets used by entities.

Examples of investment property:

- land held for long-term capital appreciation;
- land held for a currently undetermined future use;
- a building owned by the entity (or held by the entity under a finance lease) and leased out under one or more operating leases;
- a building that is vacant but is held to be leased out under one or more operating leases;
- property that is being constructed or developed for future use as investment property.

Investment property is initially measured at cost including transaction costs. Cost comprises the property's purchase price. Transaction costs include legal fees, property transfer taxes and all expenses directly attributable to the acquisition of the property. Borrowing costs incurred for the purpose of acquiring, constructing or producing an asset should be capitalized as part of its cost. A similar treatment is included in both IFRS and RAS.

The costs of the day-to-day servicing of the investment property – primarily the cost of labor, consumables and other minor parts (often described as "repairs and maintenance") – should be expensed as incurred. However, other expenditure can be capitalized if they increase the investment property's originally assessed standards of performance or replace a fully depreciated component. The same treatment applies under both IFRS and RAS.

Under IFRS, subsequent to initial recognition, an entity should either carry investment property at fair value or at depreciated historical cost. Fair value is the amount for which an asset could be exchanged between knowledgeable, willing parties in an arm's length transaction. Acceptable valuation techniques include the use of market comparable information and discounted cash flow techniques.

When an entity carries its investment property using the fair value model, they should determine the fair value at the end of each reporting period and include the differences in the profit or loss account as an expense or an income, depending on the situation.

Under RAS, tangible assets (which include investment property as mentioned above) can be measured subsequently using either the cost model or the revaluation model. The cost model is similar to IFRS. It requires entities to show investment property at cost less accumulated depreciation and any accumulated impairment losses. The revaluation model requires presentation of land and buildings at fair value (similar to IFRS) and fair value is expected to be determined from market-based evidence by appraisal that is normally undertaken by professionally qualified valuers. The main difference versus the fair value model under IFRS is that differences arising after the valuation are not charged to the income statement, but directly to equity and more specifically to the revaluation reserve.

The Romanian tax treatment of revaluation differences changed during 2009, in the sense that they are no longer deductible for corporate income tax purposes. This change also has an impact on the recognition of deferred taxes under IFRS.

Two typical situations where the change has significant impact are as follows:

1. IFRS – historical cost; Statutory – revaluation model

In this case no deferred tax will be recorded at 31 December 2009, as the tax base is the historical amount, which is equal to the IFRS book value. Any previously recognised deferred tax asset should be reversed through the profit or loss account.

2. IFRS fair value model; Statutory – revaluation

Deferred tax arises due to the difference between the IFRS book value (fair value) and the tax base (historic cost).

Ownership of land and buildings is taxed in Romania as follows:

Building Tax

For buildings owned by companies, the building tax rate is set by the Local Council at **between 0.25% and 1.5%** of the entry value of the building, adjusted with the value of reconstruction, consolidation, modernization, modification and extension works and the revaluation, if the case. If the building has not been revaluated in the previous three years, the tax rate is increased by the Local Council to **between 5% and 10%**. The taxable value of fully depreciated buildings is reduced by 15%.

The building tax rates for 2010 in several Romanian cities are presented in Table 4.

Land Tax

Owners of land are subject to land tax established at a fixed amount per square metre, depending on the rank of the locality where the land is located and the area and / or category of land use, in accordance with the classification made by the Local Council. For example, for land in city with construction use, the land tax would range between **0.01-0.59 RON per square metre.**

Land underneath buildings is not subject to land tax.

Table 4
Building tax rates for 2010

City	Revaluated building	Not revaluated building
Bucharest	1.50%	10.00%
Timisoara	1.00%	5.00%
Cluj Napoca	0.90%	5.00%
Lasi	0.95%	8.75%

Source: PricewaterhouseCoopers

8. CLIENTS' CORNER

Landlords

Valeri Atanassov
Managing Partner CEE
Soravia Real Estate Development Gmbh

The best moment during 2009 was the successful completion of our Romanian project – Metropolis, where despite the market difficulties we reached occupancy of 98%. In reaching this great result your company did an excellent advisory service. Also in the last two months of the previous year we can say that the banks once again started discussions with the developers which are active in Romania.

At the beginning of 2009, **the worst** moment was when the banks stopped their usual dialogue with developers. In addition, many tenants in the business centers, did a re-estimation of their budgets and started to renegotiate their rent.

During the last quarter of 2009 and the beginning of 2010, a compression of yields has been noted. If in October 2009 we used to receive proposals and prognoses for 10% and more, so at the end of 2009 we saw 9% and at the beginning of 2010 – 8.5%. These figures give us an expectation that in the first six months of 2010 deals will be concluded in-between 8-9% maximum, depending on the project and the location.

Silviana Badea
Country Manager Romania
Valad Property Group

The best: cleaning out of the frivolous market players (both owners and tenants) with businesses unprepared for sustainable development.

The worst: the climate of uncertainty and deadlock in making business decisions.

Alex Van Breemen
Managing Director
Cascade Group

The best thing is that quality, location and market vision are again in fashion. Bad for others, good for me.

The worst thing is that Romania has temporarily dropped off the map for investment funds as risk is judged to have increased; they will return to the few good products in Bucharest in 2010.

Todd Cowan
Managing Partner
CD Capital Partners

Best in 2009 – AFI successfully opened AFI Palace Cotroceni sending a sign to the market that Bucharest is not over retailed and that good projects will continue to attract good retailers and customers.

Worst in 2009 – dissolution of the government sent a sign to foreign investors and the EU that Romania continues to suffer from political instability and risk.

Vlad Dumitrescu
Development Manager Romania
Immoeast Cpb Real Estate Consult SRL

The best: decrease in the construction and land prices – prices which exceeded significantly the "crash rates".

The worst: the crisis froze the Romanian real estate market and mostly of the country as well, since the main driver was real estate investments, together with all the other industries which performed well due to the real estate market.

Laurentiu Catalin Hanu
Manager Business Development Romania
CTP Invest

The best thing for 2009 was that the tough market conditions finally obliged all players to differentiate between quality products and serious tenants on one hand, and scrap deliveries, plus unhealthy businesses/client companies on the other. This can be the premise to start building the market in a more stable way.

Lack of demand and the fact that financing was extremely expensive and practically unavailable were the **worst** things for the market, forcing even the most determined players to pull back and remain in standby mode. As a result, all new business opportunities were cut.

Sven Lemmes
Country Manager
AIG Lincoln

The best: a broader acceptance of the challenges Romania poses to Real Estate development and investments and, therefore, more professional investor attitudes and lower land prices.

The worst: to realize how badly trained Senior Lender teams are (both Commercial and Risk Management) in even the most basic Real Estate and legal principles.

Robert Neale
Partner
Portland Trust

The best: despite an extremely difficult economic environment and a devaluation of the RON there was not a wholesale meltdown of those banks most involved in lending in Romania.

The worst: still by the end of 2009 there were very few opportunities for those with funds and appetite to invest in Bucharest at realistic, sustainable price levels.

Matthew Proskine
Director of Commercial Leasing
Avrig 35

The best part of 2009 is the fact that it is over! This was one of the toughest years in the past seventy for anyone! This year taught us how to not only survive, but to become a more efficient and stream lined developer. The lack of liquidity allowed us to really look deep into some of our core issues that were disregarded in the frenzy of the past years. We have emerged from 2009 as a stronger, competitive market leader and are excited for the prospects of 2010.

The worst part was clearly the absolute lack of capital, the markets spent an entire year virtually frozen; we are all hoping this will change this year.

Marian Roman
Managing Director
Europolis Real Estate Asset Management SRL

The best thing was closing the transaction between Europolis and Riverinvest and taking over the first part of the mixed use project of urban regeneration, Sema Parc, from its developer. The total value of the transaction exceeded 100 million EUR, the project consisting of two Class A office buildings with a total leasable area of 48,000 sq m, situated in the central – western side of the capital. This is the new favorite office destination for companies due to the proximity to all means of transportation and the good traffic infrastructure allowing smooth and easy access to and from all key points of the city. Along with the take over, the project received a new identity, now being referred to as Riverplace, and has been 100% leased since 2008 by large and prestigious companies such as Ipsos Romania, Zapp Telemobile, Computer Generated Solutions, Thales Rail Signaling Solutions, British American Tobacco, UPC and KRKA.

Nothing so bad happened to be worth mentioning.

Radu Tanasescu
COO
Anchor Group SA

The best thing was that many retail projects that were not meant to survive even in normal market conditions have been canceled. This will bring in the future a healthier development of the market.

The worst was that many international brands that were intending to enter in the market postponed their development plans.

George Teleman
Fund Managing Partner
Equest Balkan Properties

The lack of bank financing and the significant decrease of foreign investments were the factors which affected the local market the most in 2009, resulting in both positive and negative effects (a double edged sword).

The best effect was a decrease in land prices, design and consulting expenses, and construction costs, resulting in a much desired and awaited adjustment of costs. Another positive effect was the settlement of the real estate market through the at least temporary disappearance of the speculative investors who contributed to the market bubble. I would say that the market is not speculative like in 2007 and 2008.

The worst effects were the blockage of transactions, the decrease in rents and the delay in works in the case of projects under construction. In fact, works have been stopped for most of the commercial, industrial and residential projects. Another negative effect was the financial instability of tenants, which led to a high amount of uncollected rent and bad debts.

Leslie Warren
Director
Helios Properties / CIC Financiar SRL

The worst: at least from my perspective, was the lack of occupier confidence, although our competitors would say a lack of available funding, we are lucky to maintain the confidence of our investors in these challenging times.

Tenants

Mioara Bolozan
Marketing Manager
Whirlpool Romania

The best thing was the flexibility with regard to the re/negotiation of rents. This brought additional oxygen by reducing fixed costs in a business climate that was striving for efficiency gains.

The worst thing, though I would not put in antithesis – was the freezing of the offer of services or facilities given when acquiring space, especially those for storage. In other words, the real estate market did not respond to the needs left uncovered in late 2008, especially if this meant additional investments to be made by the owners.

Bogdan Bozdog
Expansion Manager Romania
New Yorker Romania

The best thing was the cancelation of unfeasible projects and the development only of the good ones.

The worst was the blocking of several important projects due to the financial crisis, resulting in few new openings in the coming years.

Tim Caiger
Vice President Real Estate & Facilities, EMEA
Oracle Corporation

The best was the formation of Prime Property Advisers who gave us great help and support in Romania.

The worst was the decline in the office rental market in the Thames Valley.

Bogdan Cocora
Managing Director
S&T Romania

Without being good or bad, I noticed a migration of IT companies from the center to the northern area of the city and a significant increase in available space, which along with the crisis, created a welcomed rent reduction.

Bogdan Enache
Country General Manager
TNT Romania

In 2009 the center of power in negotiating and trading has shifted from owners to tenants. The main reason behind this change has been the strong growth of the vacancy rate for office space. The time when buildings on the local market were leased entirely before completion has passed. In an unpredictable economic environment tenants do not wish to make long-term commitments like in the past. Therefore, to facilitate transactions, the owners had to be more flexible in negotiating contracts. Rents declined and tenants were interested in renegotiating even their existing leases.

Radu Enache
Managing Director
HP

The best thing, from a tenant's perspective, was the lower pressure of the rents.

The worst thing was that long term-lease contracts have not led to the effective reduction of costs despite the temporary financial incentives given to tenants.

Radu Ghita
Logistics Director
Geodis Calberson Romania

The best: improved communication between suppliers and clients (via agents) through the diversification and the flexibility of the offer as well as the settlement of the market on a realistic basis

The worst: deprivation of capital for development through lack of involvement of banks in financing projects of any kind.

Moshe Greidinger
CEO
Cinema City International NV

Best for Cinema City was the opening and the warm welcome by the public to CC Cotroceni. The clients love the cinema and the IMAX and we are pleased.

No **worst**.

Francesca Postolache
Director, Real Estate Leader
PricewaterhouseCoopers Romania

The best thing brought by last year was a selection of the good projects, particularly in the residential segment, which will continue this year as well. Developers are determined now to make a deeper analysis of the elements involved in an investment, be it location, construction quality or services. A drop in prices was also noticed, which aligned with those in the region (CEE). Discounts were given to boost sales. Construction costs dropped due to the decrease in the price of materials. Developers were more rigorous when choosing the construction companies to work with. Finally, there was a greater focus on the consumer's needs.

The worst problem was the lack of access to credit. This has also led to a significant reduction in transactions. In these circumstances a decrease in the capacity of valuing assets was noticed. Also, there was a decrease in the rental income from offices as well as retail units, caused by the increasing number of bankruptcies or by tenant pressure to re/negotiate the rent. Finally, investors reoriented to other markets less risky, or which were similar to the local one in terms of risk, but offered greater benefits.

Americas
USA
Bermuda
Brazil
Canada
Caribbean
Chile

Australasia
Australia
New Zealand

Europe
UK
Belgium
Czech Republic
France
Germany
Hungary
Ireland
Italy
Monaco
Poland
Portugal
Romania
Russia
Spain
The Netherlands
Ukraine

Africa
Botswana
Kenya
Malawi
Nigeria
South Africa
Tanzania
Uganda
Zambia
Zimbabwe

Asia
Cambodia
China
Hong Kong
India
Indonesia
Macau
Malaysia
Singapore
South Korea
Thailand
Vietnam

The Gulf
Bahrain
UAE

Romania
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Sharing resources within the Knight Frank network, our team offers to its clients international knowledge and expertise, tailored to the specific local needs.

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