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France: Property market in the midst of dynamic upturn


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1. Introduction

France's property market benefits from economic recovery

France's economy gained considerable momentum in 2017. After the election of Emmanuel Macron as president, there was a clear revival of the economy, particularly in the second half of 2017, which had a positive effect on the labour market. Tourism also picked up markedly after the difficult years of 2015 and 2016, which were shaped by terrorist attacks. The fundamental forecasts for France's economy remain stable for 2018 and 2019.[1] As a result of the economic recovery, the property market is looking extremely positive. The dynamic upswing in the French property market, especially the Île-de-France region with the capital Paris, is reflected in a high demand for first-class commercial property. The situation on the office property market has now become challenging in some areas. Available space in the centre of Paris is becoming increasingly scarce, which is leading to a shift to alternative market segments. Given currently favourable financing conditions, the residential property market is also on a dynamic growth path.

Aim of the study

The aim of the study is to analyse the current market trends and explain the potential and challenges of the French property market. In addition to the macroeconomic conditions, the focus will be on the latest developments and trends in the office, retail, logistics, hotel and residential market segments. An overview of Europe's currently largest infrastructure project, Grand Paris, will also be provided.

[1] Forecasts: NORD/LB Economics

2. Macroeconomic conditions

Dynamic economic growth in 2017

France, the second-largest economy in the European Monetary Union (EMU), experienced dynamic economic growth in 2017. In 2017, GDP rose at its highest rate since 2011 of 2.0 percent (previous year: 1.1 percent). Given the GDP forecast for 2018 of an increase of 2.1 percent, the economy continues to be on a robust growth path, although it lags behind the forecasts for Germany (2.4 percent) and the eurozone (2.4 percent).[2] Confidence in the reform policy of the new French government is already bearing fruit and a certain spirit of optimism has been in the air since the election of Emmanuel Macron as president in May 2017. A major engine of growth was domestic demand. Gross capital investment increased by almost 4.0 percent, and public consumption grew noticeably. Private consumption provided positive impetus, although this was somewhat less dynamic than in 2016. In addition, the tourism sector gained significant momentum again after the numbers of visitors had dropped appreciably in the wake of the terrorist attacks in 2015 and 2016. Economic dynamism was one again curbed by the foreign trade balance. There remains a rather high foreign trade deficit - especially with Germany, as the key trading partner. The reason for this was the increase in investments by private companies, which led to a rise in imports, while the global share of exports declined.

Economic indicators

Economic indicators (change from prev. year in %)

	2016	2017	2018f	2019f
Real GDP growth	1.1	2.0	2.1	1.9
Unemployment rate*	10.0	9.4	8.7	8.2
Inflation rate (HICP)	0.3	1.2	1.6	1.6
Budget deficit**	-3.4	-2.6	-2.6	-2.4
Current account balance**	-1.3	-0.5	-1.0	-1.0

Source: NORD/LB Economics, f - forecast, * as % of employed people, ** as % of GDP

Economic power by region

As at 1 January 2016, France's 27 regions (of which five are overseas) were reduced to 18 regions by an administrative reform in order to increase administrative efficiency. France has a monocentric city system. By far the most economically powerful region is Île-de-France (GDP per capita 2016: EUR 51,100), which accounts for around 30 percent of French GDP. In second place is the newly formed Auvergne-Rhône-Alpes region that came into effect on 1 January 2016, with a share of total French GDP of around 11 percent.[3]

New French government with strong reforming zeal

The outcome of the French presidential elections provided relief and economic momentum. The new French head of state, Emmanuel Macron, is keen on reform. Reforms are aimed at eliminating structural problems on the labour market and generating more growth by strengthening international competitiveness. Social security contributions and corporation tax are to be cut and bureaucracy reduced overall. A crucial measure is the planned reform of the labour market. In this context, for example, compulsory redundancies are to be made easier and pay settlements in the event of industrial tribunal

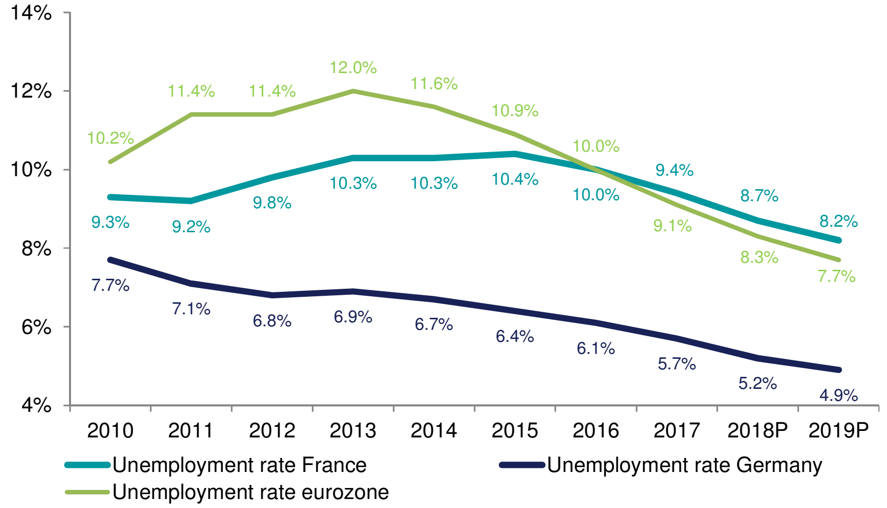
[2] Forecast: NORD/LB Economics
[3] Eurostat

disputes are to be limited. It is also intended to strengthen works agreements and simplify employment negotiations between employers and employees. The subject of unemployment insurance is also on the agenda. The lack of skilled workers is to be countered by launching an extensive training programme. Companies and investors have welcomed the reforms which have been announced.[4] Business expectations have increased perceptibly. In December 2017, at 112.1 points, business confidence reached its highest level since the end of 2007, although market sentiment worsened somewhat at the beginning of 2018. Business confidence fell to 109.1 as at March 2018.

Unemployment rate down, but still at a high level

France's economic recovery is providing a positive stimulus to the job market. In 2017, the unemployment rate was below the ten percent mark for the first time since 2013 at 9.4 percent. However, it was still running at a high level and above the average of 9.1 percent for the eurozone. The forecasts for 2018 and 2019 of 8.7 percent and 8.2 percent respectively assume a drop in the unemployment rate, but the anticipated figures are still higher than the expected eurozone average. Moreover, youth unemployment is well above average at 21.6 percent (EU average: 15.9 percent).[5] It remains to be seen what effect the implementation of labour market reforms will have on the targets of increased productivity and improved labour market momentum.[6]

Development of average unemployment rate[7]



Source: EU Commission, Forecasts: NORD/LB Economics, own research

Positive demographic trend

France is the most heavily populated country in the EU behind Germany and ahead of the United Kingdom. In 2017, France had around 67.2 million inhabitants. Population growth of 0.3 percent compared with 2016 was somewhat lower than in previous years (2016: +0.4 percent; 2015: +0.5 percent). Growth was made up of a surplus of births over deaths of 164,000 and immigration gains of 69,000 persons. After Ireland (1.92), France continued to have the highest birth rate in Europe in 2017 of 1.88. By comparison, the birth rate in Germany is currently only 1.59 children per woman. According to forecasts by the French statistical office INSEE, France's population will rise to approximately 70.7 million inhabitants by 2040. A further

[4] NORD/LB: Economic Adviser October 2017/GTAI
[5] Bundesagentur für Arbeit (German Federal Labour Agency): Comparison of labour market statistics, February 2018
[6] European Commission/forecasts: NORD/LB Economics
[7] ILO concept, annual averages

increase to 76.5 million inhabitants is expected by 2070.[8]

Loss of real spending power due to higher inflation

While private consumption lost momentum somewhat in 2017 with a plus of 1.3 percent (previous year: 2.1 percent), production above all contributed to the economic upturn with a growth rate of 2.3 percent (previous year: 0.9 percent). This led to a marked improvement in the investment climate. The inflation rate increased in 2017 to 1.2 percent (previous year: 0.3 percent). Somewhat higher rates are expected in the coming years (2018: +1.6 percent; 2019: +1.6 percent). The reasons for the slightly higher values are the revival of the economy and the increase in energy tax at the beginning of 2018.[9]

Highest spending power in Île-de-France

The average spending power in France in 2017 was EUR 19,537 per capita (previous year: EUR 19,254). Therefore, France ranks thirteenth in Europe. Of the 13 French regions (excluding overseas regions), only two regions are above the national average. Île-de-France, with the capital Paris, leads the nationwide rankings by a long way. The per capital spending power here was EUR 22,983 in 2017 (approximately 65 percent above the European average), followed by the Auvergne-Rhône-Alpes region at EUR 19,849 per head.[10]

National deficit reduced

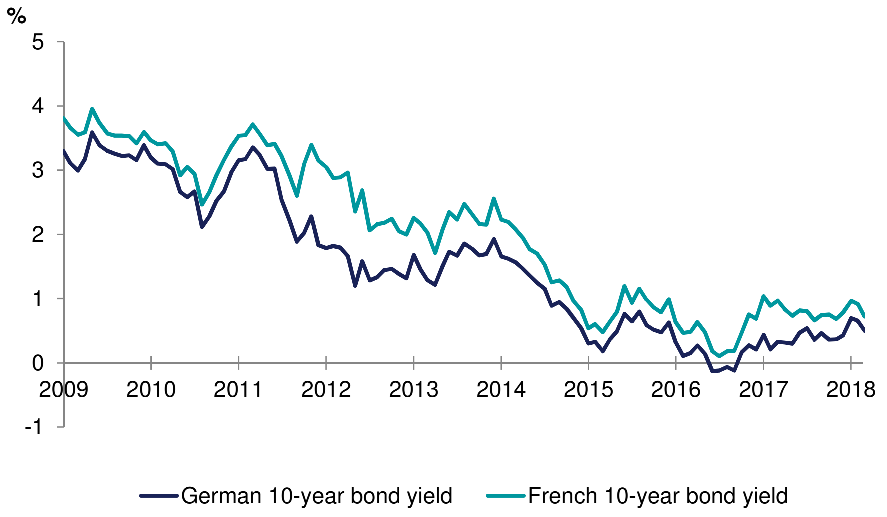
For the first time since 2007, France almost met the Maastricht criterion of not exceeding the cap on annual borrowing of 3 percent of GDP. The deficit ratio in 2017 was -2.6 percent of GDP. For 2018 a budgetary balance (as percentage of GDP) of -2.6 percent or for 2019 of -2.4 percent is expected. Of all the EU Member States, France has the highest public spending of around 56 percent of GDP. A long-term strategy is required from many quarters to reduce the high government spending.[11]

Stable risk assessment

France’s refinancing costs are currently 0.86 percent (based on 10-year bonds). After the yield gap between 10-year French and German government bonds at the beginning of 2017 was between 60 and 70 basis points, the spread is currently back to around 20 basis points. This level should be maintained in 2018.[12] Furthermore, the ratings of the agencies provide a uniform picture: Standard & Poor´s (AAu/stable outlook), Moody´s (Aa2/stable outlook) and Fitch (AA/stable outlookl).[13]

[8] INSEE
[9] Forecast: NORD/LB Economics
[10] GfK Purchasing Power Europe 2017
[11] INSEE/Forecast: NORD/LB Economics
[12] NORD/LB: Economic Adviser, January 2018
[13] Bloomberg

Yield performance French vs. German government bonds



Source: Bloomberg, own research

Outlook macroeconomic conditions

Demographic development	↗
Real GDP growth	↗
Number of employees	↗
Unemployment rate	↘
Inflation	↗
Real purchase power	↘
Tourism demand	↗

As described above, France reported a dynamic economic upturn in 2017. France is still below the European average in terms of economic growth and unemployment, but all the signs point to a sustained improvement. The reasons for this are the good prospects for the global economy and increased confidence in the wake of the Macron effect. How sustained the Macron effect is remains to be seen. The tourism market looks back on a challenging phase following the terrorist attacks. The situation eased again in 2017 and visitors numbers once more increased. Although the situation remains uncertain at the present time, we assume that there will be a further rise in tourist demand that will also provide positive impetus for the French economy. Therefore, overall we expect the dynamic trend of last year to continue in 2018 in light of the positive general conditions. The economic upward trend is also having a revitalising effect on the French property market, which could be clearly observed in fiscal year 2017.

3. Office property market

Île-de-France Europe's largest office property market

France's office property market is largely defined by the Île-de-France region, which is the largest European office property market with an office space inventory of just under 53 million m². France's key regional office markets are Lyon, Lille and Marseille.[14]

Dynamic demand in the Île-de-France region

On the office property market of Île-de-France there is currently such a high demand that especially in the centre of Paris there is already a shortage of office space. The Paris office property market is also benefiting from the dynamism of the technology and digitisation sector, which is further intensifying demand and driving the development of new flexible workplace concepts such as co-working and serviced offices. From the end of 2015 to mid-2017, the number of co-working spaces in Paris CBD rose by 84 percent to 149. In Greater Paris, there are already 238 co-working spaces in total. A further dynamic trend is also expected for 2018: In Paris, along with London and Berlin, the highest growth rates in the co-working sector are set to be

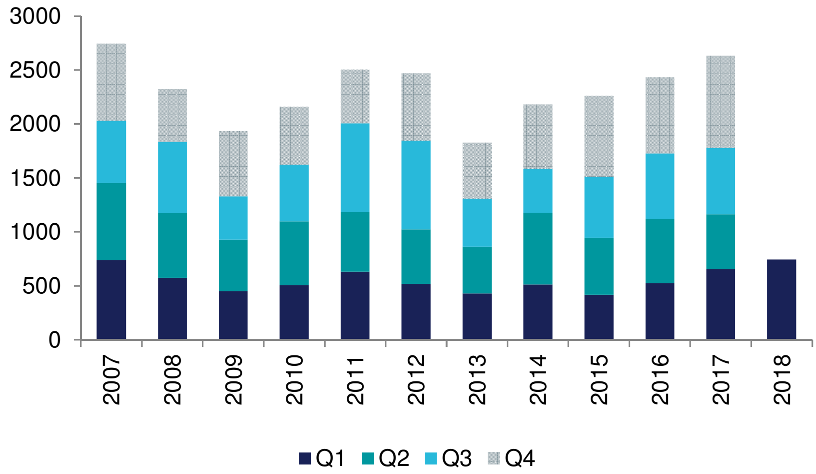
[14] Cushman & Wakefield: France Office Market Snapshot Q3 2017/Jones Lang LaSalle: Why invest in Paris? 2017

achieved.[15] Another trend worthy of mention is the serviced office. This office concept offers flexible contracts and flexible spaces. Moreover, infrastructure such as IT, reception, garages or the management of warehousing space is offered as required in addition to office space.[16]

Rise in take-up in Île-de-France

In fiscal year 2017, the office property market of Île-de-France benefited from the positive economic and labour market trend. 70,000 new jobs (previous year: 55,000) were created in this region in 2017. Take-up increased by 8 percent compared with 2016 to around 2.633 million m² (previous year: 2.435 million m²). This result was much higher than the ten-year average of around 2.273 million m². In comparison with 2013, which had the lowest take-up over the past ten years, this even equates to an increase of over 44 percent. The last quarter of 2017, in particular, was very positive with a take-up of around 853,900 m² (+21 percent compared with Q4 2016). Demand in the large-scale segment of 5,000 m² and upwards developed dynamically with 88 transactions (of which 38 in Q4 2017). In this segment, take-up grew by 27 percent to around 1.139 million m², which corresponds to a share of 43 percent of total space turnover. The large lease of the new "Bridge" headquarters of the Orange corporation in Issy-les-Moulineaux with floor space of 57,000 m² is especially worthy of mention here. On the other hand, the number of transactions involving smaller units (< 5,000 m²) has fallen slightly. Take-up decreased by 3 percent in this segment compared with 2016, but remained at a stable level of around 1.493 million m². The first quarter of 2018 was able to build on the successful fiscal year 2017. Take-up amounted to 741,800 m², which represents an increase of 13 percent compared to the same quarter of the previous year.[17]

Development of take-up in the Île-de-France region (in thousand m²)



Source: Immostat, own research

Vacancy level in Paris CBD at record low level

The amount of space available in Île-de-France fell slightly in 2017 with a drop of 1 percent to 4.358 million m² (previous year: 4.385 million m²). The proportion of new builds and refurbishments as a percentage of the total supply remained at a very low level of 22 percent in 2017. With regard to the individual market segments, especially Paris CBD (-30 percent),

[15] Knight Frank: Coworking in Paris 2017/Knight Frank: European Commercial Property Outlook 2018/Savills: Spotlight: The future for serviced offices in Europe, July 2017
[16] https://www.wohnnet.at/business/buero-gewerbe/serviced-office-13002
[17] BNP Paribas Real Estate: Paris Office Market, At a glance Q4 2017/Immostat

Neuilly/Levallois (-19 percent) and La Défense (-16 percent) suffered the largest decline in available space, which resulted in a sharp reduction in vacancy rates. In total, the vacancy rate of Île-de-France in 2017 stood at 6.5 percent (previous year: 6.6 percent), with the individual market segments exhibiting very diverging levels. The lowest vacancy rate of 2.9 percent, a record low, was posted by Paris CBD (previous year: 3.6 percent), followed by Paris excluding CBD at 3.3 percent (previous year: 3.1 percent). Amongst the Parisian suburbs, the vacancy rate in 1ère Couronne Est of 4.3 percent (previous year: 3.6 percent) was also below the average of Île-de-France. The vacancy rates were considerably higher in the other market segments. In La Défense, where the office market is structurally volatile due to the dependence on large property users, the vacancy rate decreased to 7.3 percent (previous year: 9.0 percent). Although it was above the average vacancy rate for Île-de-France, the vacancy rate has declined sharply in recent years. As in the preceding years, the market segments Péri Défense and Boucle Nord recorded the highest vacancy rates of 16.1 percent (previous year: 15.6 percent) and 15.6 percent (previous year: 12.6 percent) respectively, and they continued to increase compared with 2016.[18]

Rise in spaces under construction in Île-de-France

The amount of space under construction rose compared with 2016 with an increase of 6 percent to 1.200 million m² (previous year: 1.133 million m²). In light of the improved economic situation and the associated lower risk of finding suitable buyers for properties, the percentage of speculative building projects grew markedly. Looking at the individual market segments of Île-de-France, significant increases were posted especially in La Défense (+40 percent), Péri Défense (+252 percent) and in the Parisian suburb 1ère Couronne Nord (+73 percent). “Grand Central Saint-Lazare” should be mentioned as an example of a current project underway in the centre of Paris, which is to provide around 20,100 m² of office and retail space. Completion is scheduled for mid-2019.[19]

Office market data for the Île-de-France 2017

	Take-up	Take-up	Vacancy rate	Availability of space	Availability of space	Space under construction	Space under construction
	in m²	∆ y/y	in %	in m²	∆ y/y	in m²	∆ y/y
Paris CBD	481,000	7%	2.9	308,000	-30%	147,000	-19%
Paris without CBD	614,000	-8%	3.3	523,000	-1%	237,000	-19%
La Défense	180,000	-35%	7.3	319,000	-16%	223,000	40%
Péri Défense	199,000	27%	16.1	512,000	6%	218,000	252%
Neuilly/Levallois	169,000	55%	7.8	169,000	-19%	38,000	-34%
Boucle North	23,000	-18%	15.6	132,000	5%	-	-
Boucle South	270,000	53%	8.7	368,000	-	90,000	-46%
1st Couronne North	212,000	144%	10.7	391,000	18%	111,000	73%
1st Couronne South	129,000	40%	10.5	317,000	6%	5,000	-87%
1st Couronne East	72,000	-23%	4.3	156,000	37%	52,000	37%
2nd Couronne	284,000	-4%	6.2	1,163,000	5%	79,000	13%
Île-de-France	**2,633,000**	**8%**	**6.5**	**4,358,000**	**-1%**	**1,200,000**	**6%**

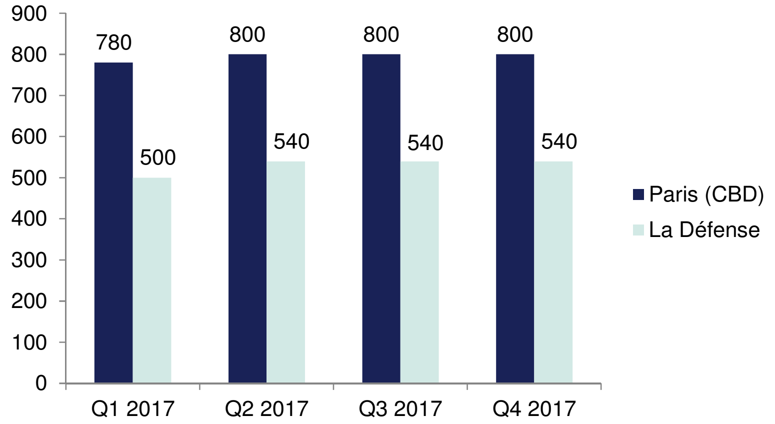
Source: BNP Paribas Real Estate, own research

[18] BNP Paribas Real Estate: Paris Office Market, At a glance Q4 2017
[19] ibid.

Stable prime rents in Île-de-France

Top rents in Île-de-France remained stable overall. At the end of 2017, the top rent in Paris CBD was EUR 800/m²/year, which equates to a slight rise of 1.3 percent compared with 2016. In La Défense, the top rent of EUR 540/m²/year was at the previous year's level.[20] At the beginning of 2018, top rents in the centre of Paris remained at a stable level in Q1, with moderate rental increases expected in the course of the year, given the shortage of space. At the end of the year, average tenant incentives in Île-de-France for new office letting (space of 1,000 m² and upwards) fell to 21.8 percent (Q3 2017: 22.2 percent), but were slightly higher than the value for the prior year (21.5 percent). Overall, incentives continue to run at a high level. The range across all market segments extends from 14.8 percent in north-east Paris to the Inner Rim with incentives of up to 25.8 percent.[21]

Development of prime rents (in EUR/m²/year) in 2017



Source: Cushman & Wakefield, own research

Regional office markets with dynamic demand

France's regional office property markets also experienced dynamic demand in 2017. The seven largest regional markets alone[22] exceeded the 1 million mark in 2017 with take-up of 1.121 million m². In Lyon, France's second most important office property market after Île-de-France, the take-up decreased by 7 percent in 2017 to 269,241 m² (previous year: 290,511 m²). This was due, in particular, to the lack of suitable offers. Amongst the regional office property markets, Lille achieved the second-highest take-up in 2017 of 213,416 m² (previous year: 252,246 m²), followed by Bordeaux with a particularly marked increase in take-up to 165,000 m² (previous year: 106,300 m²).[23] An extended review of the 16 most important regional office property markets[24] also shows a positive trend. The total take-up of these 16 markets rose in the first half of 2017 by 6 percent to 745,000 m² and was therefore well above the ten-year average. The market was also shaped by an increase in transactions in the large-scale segment (> 5,000 m²). The share compared to the same period in the prior year was up 37 percent.[25]

Space available on regional office markets

The amount of office space available within one year on the 16 regional office markets fell by 5 percent in the first half of 2017 to 2.418 million m² (previous year: 2.534 million m²). This was mainly due to a decrease of 6 percent in

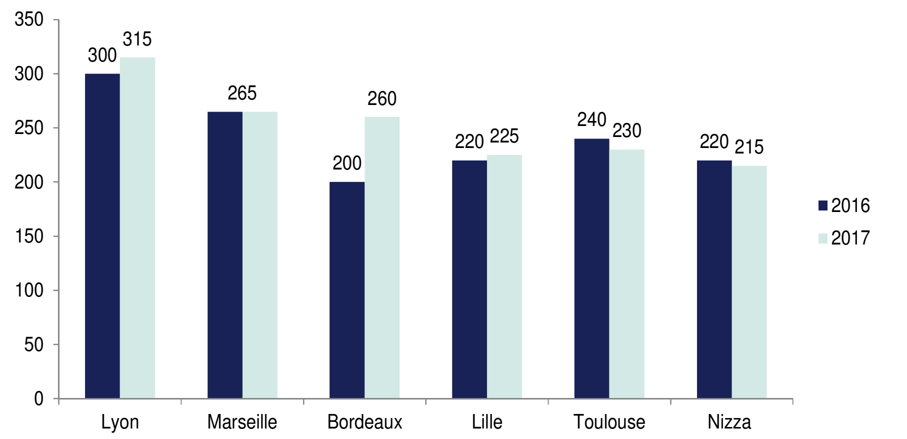
[20] Cushman & Wakefield: Marketbeat, Île-de-France Bureaux (2017/T1 2018)
[21] Immostat: Rent Incentives Q4 2017
[22] This includes the towns of Lyon, Lille, Bordeaux, Toulouse, Aix/Marseille, Nantes and Nice/Sophia.
[23] Jones Lang LaSalle: Panorama du marché des bureaux en régions T4 2017
[24] Along with the seven largest office property markets, there are the towns of Dijon, Grenoble, Metz, Montpellier, Nancy, Orléans, Rennes, Rouen and Strasbourg.
[25] BNP Paribas Real Estate: Regional Office Market, At a glance H1 2017 (annual figures were not yet available for publication)

second-hand space to 1.804 million m². However, the share of second-hand space at around 75 percent is still very high compared to new space.[26]

Regional rental trend

Top regional rents remained largely stable in 2017 compared with 2016. Exceptions were the office property markets of Bordeaux and Lyon, which developed extremely dynamically. Given the low supply combined with high demand, the top rent in Bordeaux increased by 30 percent to EUR 260/m²/year (previous year: EUR 200/m²/year) and in Lyon by 11 percent to EUR 315/m²/year (previous year: EUR 300/m²/year).[27] In addition, the average rents for new properties coming onto the market continued to rise due to the lack of supply. On the other hand, the average rents for second-hand properties in the regional office markets remained low. Incentives such as rent-free periods were further reinforced in light of this.[28]

Regional prime rents (in EUR/m²/year) 2016 vs. 2017

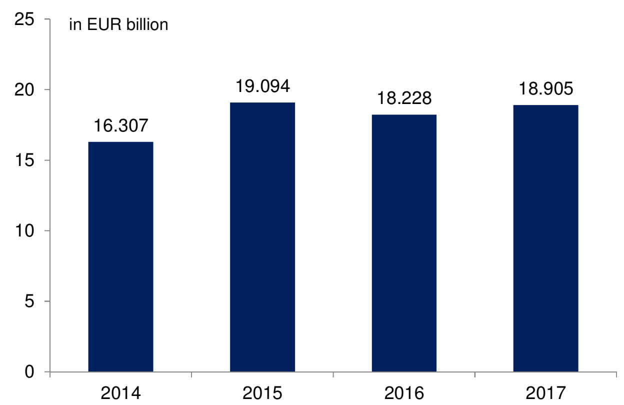


Source: Jones Lang LaSalle, own research

Office property is popular with investors

The nationwide transaction volume for office property was around EUR 18.91bn in 2017, which is an increase of 3.7 percent on the previous year. Consequently, office property was once again by far the most popular asset class in France, with a share of total commercial transaction volume of 72 percent. National investors still defined the market, with international investors (especially Asian) succeeding in increasing their influence.[29]

Transaction volume on France's office property market



Source: BNP Paribas Real Estate, own research

[26] BNP Paribas Real Estate: Regional Office Market, At a glance H1 2017 (annual figures were not yet available for publication)
[27] Jones Lang LaSalle: Panorama du marché des bureaux en régions T4 2017
[28] Cushman & Wakefield: France Office Market Snapshot Q3 2017
[29] BNP Paribas Real Estate: Investment in France, At a glance Q4 2017

Transaction volume in Île-de-France down slightly

Île-de-France, with a share of 86.2 percent, reflects virtually the whole investment market for office property in France. The transaction volume declined slightly in 2017, with a drop of 2 percent to around EUR 16.30bn (previous year: EUR 16.70bn), although Q4 was a record quarter with a transaction volume of EUR 7.7bn. The share of transactions worth EUR 100+m increased to 69 percent (previous year: 65 percent). An example of a particularly large-scale transaction is the sale of the Coeur Défense in La Défense for EUR 1.8bn in Q4 2017. The Western Crescent market segment developed extremely dynamically with an increase in transaction volume versus 2016 of 12 percent to EUR 4.6bn. Given the small supply of first-class properties, the proportion of core plus and value-added properties rose. In terms of the total of all transactions over EUR 20m, their share in 2017 was around 55 percent.[30]

Yields remain under pressure

As a result of the high investor demand for core properties and the current supply shortage, prime yields on the French office investment market are at a ten-year low. In Île-de-France, the prime yield in 2017 in Paris CBD was 3.00 percent (previous year: 3.00 percent) and in La Défense, 4.00 percent (previous year: 4.25 percent). Furthermore, the prime yield in Lyon was down significantly at 3.95 percent (previous year: 4.80 percent). Owing to this low level, one can assume that for better performance, investors will be increasingly focusing their attention on core plus and value added properties outside the centre of Paris. In addition, attention will switch more and more to regional markets such as Bordeaux and Marseille.[31]

Outlook for the office property market

Demand	↗
Supply	↘
Office employees	↗
Vacancy rate	↘
Top rent	↗
Investment volume	→
Prime yield	↘

The fiscal year 2017 was extremely gratifying for the French office property market. Improved economic conditions combined with the revitalisation of the labour market had a positive effect. A record result was achieved in 2017 in terms of take-up, and 2018 got off to a very successful start. In Île-de-France, by far the most important office property market in France, there is now a shortage of first-class offers, given the high demand. Especially in Paris CBD, the vacancy rate has reached a critical level of less than 3 percent, and so investors are now switching to other market segments such as Île-de-France, which will benefit from the positive stimuli. In addition, the demand for new forms of workplace areas, such as co-working, is extremely dynamic, which can also be seen outside the centre of Paris. Paris could also turn into a Brexit profiteer in the coming years. At least the marketers of the La Défense business district are hoping so, who launched an advertising campaign with the slogan "Tired of the Fog? Try the Frogs! Choose Paris La Défense". Given this momentum, we assume there will be continuing upward pressure on prime rents in Île-de-France. In the years ahead, the Grand Paris infrastructure project[32] will provide additional tailwind for the office property market of Île-de-France, meaning that a significant increase in office space can be expected and the vacancy pressure should be somewhat reduced.

Overall, we believe that the supply shortage is likely to continue in 2018, and this is likely to limit investment activity. Prime yields will probably continue to be under pressure. In light of this, the regional market segments will increasingly provide attractive alternatives for investors to generate higher

[30] Knight Frank: Paris, Île-de-France, Office Property Market Q4 2017
[31] Jones Lang LaSalle: Panorama des bureau en Île-de-France T4 2017/BNP Paribas Real Estate: Investment in France, At a glance Q4 2017
[32] See chapter 8: Digression: The Grand Paris project

yields. In summary, in view of the positive economic conditions, we assume that the dynamic upward trend on the French office property market will continue in fiscal year 2018.

4. Retail property market

France's retail market is one of the most important locations in Europe

France is one of Europe's most sought-after retail locations. In times of digitisation and a boom in online shopping, there is significant pressure for change in the over-the-counter retail sector. In the case of bricks-and-mortar retailing, the shopping experience and enjoyment factor has become a key competitive advantage, so a rethink of retail channels is taking place. In light of this, France's retailers are focusing less on expansion and more on optimising existing spaces.

Improved consumer sentiment, but which is still weaker compared with the first half of 2017

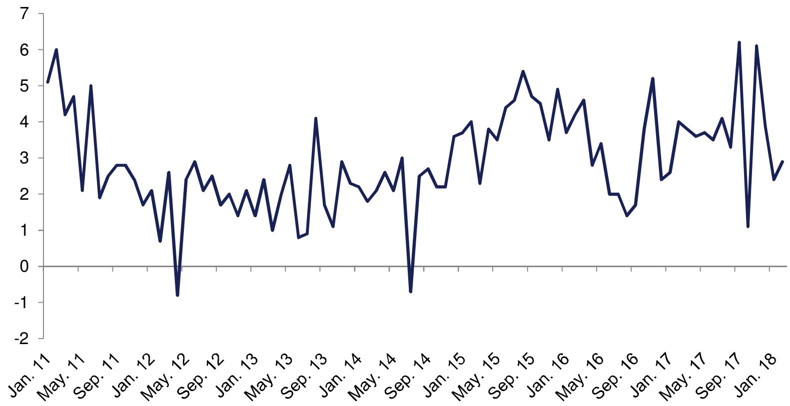
After consumer sentiment rose appreciably in the first half of 2017 as a result of the election success of Emmanuel Macron, the mood worsened in the third quarter of 2017. At the end of 2017, the mood barometer improved again. The economic tailwind with a drop in unemployment increased economic expectation at the end of 2017 to 43.4 points, which represents growth of 13.2 points compared with the previous quarter. The strong momentum of the first two quarters of 2017 could not be achieved, but the prospects remain positive. In Q4 2017, at -13.7 points, however, income expectation was negative, but improved by 5.2 points compared with the prior quarter. Buying propensity remained virtually at the level of Q3 2017 at 22.2 points.[33] Overall, private consumer spending only increased by +1.3 percent (previous year: +2.1 percent) in 2017, with the inflation rate slowing growth somewhat. The higher tourist figures especially in the capital Paris and the larger cities such as Bordeaux and Lyon had a positive effect on the retail property market compared with previous years.[34]

Development of real retail sales

The average growth rate of real retail sales (excluding automotive) increased in 2017 by 3.8 percent (previous year: 3.1 percent) compared with 2016. Especially in the second half of 2017, momentum increased. In December 2017, the year-on-year increase in real retail sales (excluding automotive) was 3.9 percent. On the other hand, in February 2018, at 2.9 percent[3], the growth rate of real retail sales (excluding automotive) had once again dropped back slightly compared with the prior year.

[33] GfK consumer climate: Press release for Q4 2017
[34] Knight Frank: Retail property in France, 2017 summary & 2018 outlook

Real retail sales (excluding automotive), change in % (yoy)



Source: Bloomberg, Eurostat, own research

Largest retail shop property market in the EU

France's retail shop property market is the largest market within the European Union (EU) with a sales volume of around EUR 438bn (2016) ahead of United Kingdom and Germany. Per capita retail sales of EUR 6,811 (2016) are the highest of the EU countries.[35] Sales from online trading amounted to around EUR 82bn in 2017 (previous year: EUR 72bn), which corresponds to a year-on-year increase of 14 percent. The EUR 100bn mark should be reached by 2020. Compared to the rest of Europe, France is in therefore in third place behind United Kingdom and Germany.[36]

Shopping centre market reacts to changing customer needs

France's retail property market has over 630 shopping centres with retail space of approximately 15 million m².[37] 2017 was relatively quiet compared to previous years with completions of approximately 141,400 m². For 2018, the pipeline has been replenished with around 245,000 m² of planned new shopping centre space. France's shopping centre market is a comparatively mature market and has a high refurbishment potential. Consequently, in 2017 the focus was less on building new shopping centres and more on extending or modernising existing ones. The increasing competition from online trading is forcing existing shopping centres to adapt more and more to changing customer needs. Traditional shopping centres with the emphasis on clothing, shoes and supermarkets are now considered to be old-fashioned. To growing degree, the focus is on the entertainment factor when shopping, with the aim of giving customers an enjoyable purchasing experience. This especially includes developing services (e.g. massage studios) and exclusive restaurants. Retailers increasingly see the interlinking of the offline business and e-commerce as a sustained competition factor. One example here is the click-and-collect model, where customers can order products online and collect them from the retailer's premises.[38]

Market for outlet centres offers growth potential

Further potential for the market will be generated by outlet centres. Here, with sales space of around 5.4 m² per 1,000 inhabitants, France is comparatively less developed than for example Italy (8.1 m² per 1,000 inhabitants) or United Kingdom (8.0 m² per 1,000 inhabitants). The Île-de-France region with its high purchasing power and the tourist cities along the Mediterranean offer

[35] GfK: European Retail Study 2017
[36] Knight Frank: Retail property in France, 2017 summary & 2018 outlook
[37] CBRE: France Retail, Shopping Centres, Q3 2017
[38] Savills: France Retail, Shopping centres and retail parks: Let´s buy happiness, November 2017

particularly attractive locations.[39]

Paris as top retail location

With an above-average purchasing power level, Paris is one of the world's top retail locations, alongside London and New York. International shopping tourism is a key driver of growth. The most important and best known retail location in Paris is the Avenue des Champs Élysées in the eighth Arrondissement. Other attractive regional locations are Marseille and Lyon. Given the boom in online shopping, retailers are increasingly selective when it comes to site optimisation, tending to concentrate mainly on highly frequented locations. High transfer fees, known as key money, are paid for shops in prime locations.

Rents in prime locations at high level

Prime rent levels remained stable and high in the top Paris location, Avenue des Champs Élysées, at EUR 18,000 EUR/m²/year in 2017. This is the most expensive retail location in Europe. In the key regional metropolises, prime rents also largely remained at the previous year's level. Exceptions were the cities of Marseille and Lille. In Marseille, prime rents went down by 6.7 percent year on year to EUR 1,400/m²/year, due to competition from projects in the Euroméditerranée quarter. Prime rents in Lille also declined. Prime rents fell in 2017 compared to 2016 by 5.6 percent to EUR 1,700/m²/year due to growing competition.

Shop rents in 1a locations (EUR/m²/year) Q4 2017

City	Prime rents	Δ 1 year (%)	5 years CAGR (%)
Shop rents in 1a location			
Paris	18,000	0	+3.7
Lyon	2,500	0	+2.6
Marseille	1,400	-6.7	-6.9
Bordeaux	2,400	0	+1.8
Lille	1,700	-5.6	-5.0
Toulouse	2,200	0	0
Nice	2,200	0	0
Retail Park			
Île-de-France	180	0	0
Shopping Centre			
Île-de-France	2,000	0	0

Source: Cushman & Wakefield, own research

Retail investments down

Im 2017, investment volume in the retail segment fell by 28 percent to EUR 3.6bn (previous year: EUR 4.7bn), which corresponds to a share of almost 14 percent of the total commercial transaction volume in France. Therefore, the share was well below the 24 percent average for the past five years. It was also the lowest figure since 2008. The decline can be attributed above all to the lack of adequate available properties. Furthermore, booming online trade has led to increased reticence among investors. Shopping centres accounted for a share of total investment volume of around 26 percent. The investment volume was distributed virtually equally over the Île-de-France region and the other regional metropolises.[40] The proportion of foreign investors was 28 percent (previous year: 41 percent). Prime yields were stable overall and, with the exception of Marseille, are at a ten-year low given the high demand. In Paris prime returns fell slightly in 2017 to 2.25 percent (previous year: 2.40 percent). Top yields for shopping centres in the Île-de-France region remained

[39] GfK: European Retail Study 2017
[40] CBRE: France Investment, Q4 2017/Cushman & Wakefield: Club GRI Future tendance du Retail, Janvier 2018

at the prior year level of 3.50 percent. Prime yields for retail parks in Île-de-France were down slightly at 4.25 percent (previous year: 4.50 percent).

Prime yields in the retail sector (net, in %)

City	Q4 2017	Q3 2017	Q4 2016	10-year high	10-year low
Shops in 1a location					
Paris	2.25	2.25	2.40	5.00	2.25
Lyon	3.85	3.85	3.85	6.25	3.85
Marseille	5.00	5.00	4.75	6.25	4.75
Bordeaux	3.85	3.85	4.00	6.25	3.85
Lille	4.25	4.25	4.25	6.25	4.25
Toulouse	3.80	3.80	4.00	6.50	3.80
Nice	3.80	3.80	4.00	6.25	3.80
Retail Park					
Île-de-France	4.25	4.25	4.50	7.25	4.25
Shopping Centre					
Île-de-France	3.50	3.50	3.50	5.50	3.50

Source: Cushman & Wakefield, own research

Outlook for the retail property market

Demand	→
Supply	→
Prime rent	→
Retail sales	→
Investment volume	→
Prime yield	→

In view of the positive economic prospects, the French retail property market can approach the rest of 2018 with confidence. The consumer climate is on an upward trend and is likely to gain further tailwind through growing tourism in 2018. We assume that the demand for core properties will remain stable. The rents in Class A locations should retain their level. However, in light of the growing competition from online trading, it can be assumed that rents in secondary locations will continue to be under pressure and that vacancy rates in these places will increase. Retailers will continue to focus on space consolidation and optimisation. We expect that demand for space will continue to be extremely selective and will concentrate on highly frequented locations. We think that successfully bridging the over-the-counter and online trade is a crucial competitive advantage. As a result of the online boom, dealers have an obligation to react to the new requirements of the market. On the supply side, the investment market will continue to be defined by a lack of core properties in 2018. Given that yields are already at a ten-year low, we assume there will only be selective slight decreases in yields. Overall, they should run at the level of 2017. In summary, the retail property market should develop in a stable manner in top locations. For secondary locations, we continue to assume a moderate downward pressure.

5. Logistics property market

Record year for logistics property market

The French logistics property market had an exceptionally successful year in 2017. The economic recovery coupled with the strong growth of the e-commerce market increasingly strengthened the demand for logistics space. The optimisation of value creation chains, which has become necessary due to the boom in online shopping, represents a key engine of growth for the logistics property market. The space available has become slightly more diversified and ranges from large-scale distribution centres to small hi-tech distribution centres, such as urban parcel collection stations.[41] The demand on the north/south axis with the leading logistics region Île-de-France was particularly dynamic. France's second most important logistics location is the

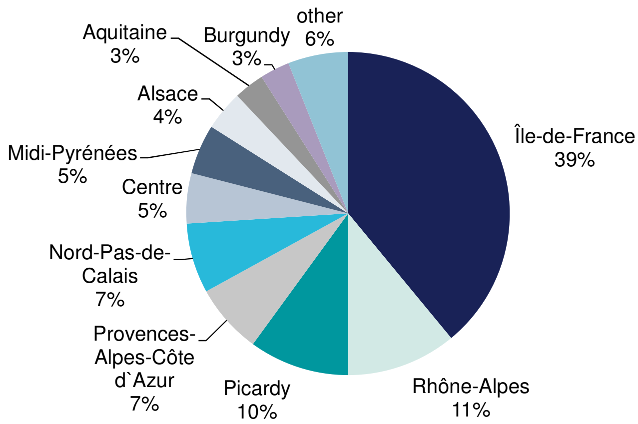
[41] CBRE: France Logistics, Q4 2017

Lyon region, followed by Marseille in the south and Lille in the north.

Dynamic demand for space

With an increase of 4.0 percent to around 4.138 million m² (previous year: 3.979 million m²), nationwide floor space turnover in 2017 reached its highest level for ten years. Particularly in demand were Grade A logistics premises, which accounted for over 80 percent of turnover. In addition, the ten largest transactions accounted for over 20 percent of the take-up. Half the total take-up was attributable to owner-occupier deals and turnkey properties built for users.[42]

Share of take-up 2017 by region



Source: CBRE, own research

Decreasing available space

Total space availability fell by 5.6 percent to 2.980 million m² (previous year: 3.158 million m²) due to the dynamic demand. Particularly sought-after Grade A premises remained at a low level and below the long-term average of 1.900 million m² with a current supply of 1.475 million m²

Region Île-de-France dominates

The Île-de-France region, with a take-up of 1.922 million m² (previous year: 0.976 million m²), recorded an exceptionally high result in 2017, which represents a share of 46.4 percent of the nationwide take-up. Take-up in 2017 was twice as high as the long-term average (0.860 million m²) since 2008. The region around the capital enjoys very high customer demand and is particularly popular for large-scale logistics centres. The five largest transactions accounted for 30 percent of total turnover. Some examples are the transactions by Conforama of 193,000 m² in Tournan-en-Brie and Amazon, and its 141,000 m² project in Brétigny-sur-Orge. Space availability in Île-de-France decreased by 6.9 percent in 2017 to around 1.357 million m² (previous year: 1.458 million m²).[43]

Regional markets with differentiated development

In Lyon, floor space turnover fell by 24 percent to 310,000 m² in 2017, which can, among other factors, be attributed to a significant shortage of properties in L`Isle d`Abeau. Instead, Marseille had a dynamic fiscal year with almost double the floor space turnover compared with 2016 of 200,000 m². In light of the strong preceding year, take-up in Lille fell by 47 percent to 185,000 m².[44]

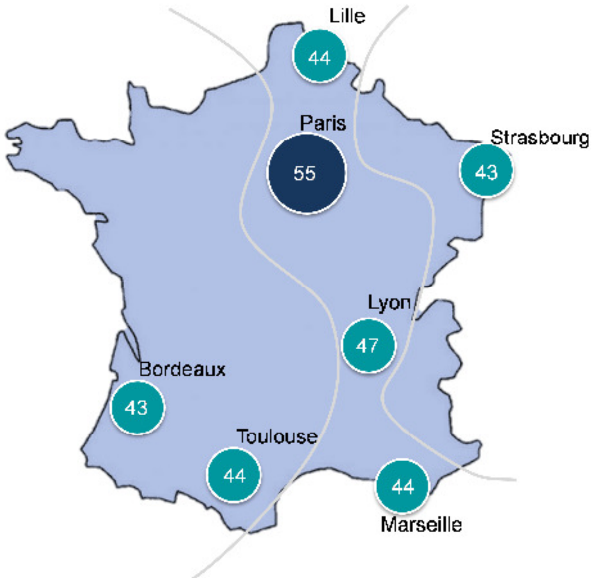
Rents at stable level

In general terms, average prime rents for Grade A logistics premises remained at a stable level in 2017. The highest top rent by far of EUR 55/m²/year was

[42] BNP Paribas Real Estate: At a glance Warehouses > 5,000 m² in France, Q4 2017
[43] CBRE: France Logistics, Q4 2017
[44] Cushman & Wakefield: France Industrial Market Snapshot, Q4 2017

paid in Île-de-France. In the regions, the figure was between EUR 43 and EUR 47/m²/year. In Lyon and Marseille, prime rents remained unchanged compared to the prior year at EUR 47 EUR/m²/year and EUR 44 EUR/m²/year respectively. This was especially due to the low supply of grade A logistics premises. We assume that overall rent levels will remain stable in 2018. A slight upward pressure on rents can be expected in some market segments, given the low supply of Grade A logistics premises.[45]

Top rents 2017 (EUR/m²/year)



Source: Cushman & Wakefield, own research

Record result for investment market

2017 was an extremely dynamic fiscal year for the French investment market in terms of logistics property. Transaction volume was around EUR 3.4bn. This record result was especially attributable to some large-scale transactions. These included the Europe-wide sale of Blackstone's Logicor portfolio to China Investment Corporation (CIC), with France garnering EUR 1.6bn, which represents a 13 percent share of the total. Prime yields continued to decline overall in 2017 - substantially in some cases – to reach a ten-year low. In Île-de-France, prime yields were 5.00 percent (previous year: 5.75 percent). Prime yields in Lyon also fell to 5.00 percent (previous year: 6.00 percent). For 2018, we expect further decreases in yields, although the low level already reached should limit the downward pressure.[46]

Outlook logistics property market

Demand	↗
Supply	↗
Vacancy rate	↘
Prime rent	↗
Investment volume	→
Prime yield	↘

The French logistics property market had a record year in 2017. Île-de-France, in particular, achieved a record result in terms of take-up, due to a high demand for XXL platforms. The decisive growth driver for the logistics property market is online trading, which generates a high demand for large platforms. In the future, it will be important to react to changing consumer behaviour. This will require flexibility and realignment of processes between producers, suppliers, service providers, dealers and end customers. There is enormous pressure for change - not only for the French logistics property market - in transport and city logistics. Given the good fundamental economic conditions, we assume there will be a further rise in demand in 2018. Based on the above, we may expect a continuing shortage of first-class properties,

[45] BNP Paribas Real Estate: At a glance Warehouses > 5,000 m² in France, Q4 2017
[46] Cushman & Wakefield: France Industrial Market Snapshot, Q4 2017

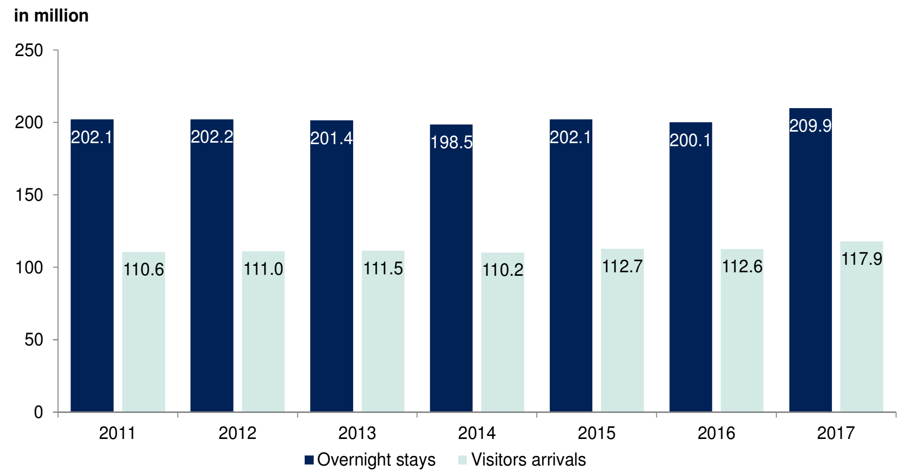
especially in Île-de-France. Slight rent increases can also be anticipated in view of the increased demand for space. The investment market is also set to record dynamic investor demand in 2018, although a further increase in transaction volume due to the shortage of first-class properties should be limited. The yield pressure is likely to continue. In view of the positive economic situation and the structural changes to the logistics property market, the signs for 2018 point to continued growth.

6. Hotel property market

Dynamic demand in 2017

France is among the most popular tourist destinations in the world. In 2017, the French hotel market comprised more than 16,000 hotels with around 603,000 rooms. After the attacks in 2015 and 2016, new record figures were achieved nationwide in 2017, with 117.9 million domestic and foreign visitors (previous year: 112.6 million) and 209.9 million overnight stays (previous year: 200.1 million). Furthermore, the room occupancy rate increased year on year by 5 percent to over 60 percent. The tourist industry has consequently proved to be extremely robust and stable.[47] In the worldwide tourism rankings, which are compiled every two years by the World Economic Forum, France again occupied second place behind Spain in spring 2017, as before, despite losing a significant amount of points for the security ranking.[48]

Overnight stays and visitors arrivals



Source: INSEE, own research

First place for visits by foreign tourists

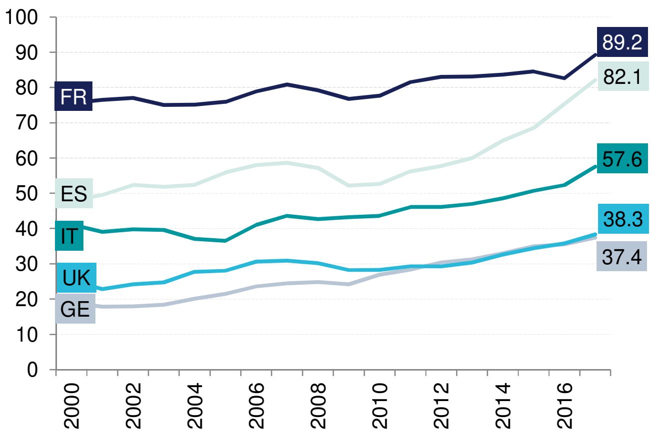
When it comes to foreign visitors, France has been in first place worldwide ahead of the USA for years. After a drop in foreign tourists to 82.6 million was recorded in 2016 due to the terrorist attacks, foreign visitors again increased in 2017 by 8 percent to around 89.2 million (provisional). France is particularly popular with European tourists from the United Kingdom and Germany. The most important country of origin of foreign tourists worldwide is the USA. In addition, the numbers of visitors from China and Japan are growing steadily.

[47] INSEE
[48] The Travel & Tourism Competitiveness Report 2017: The "Travel & Tourism Competitiveness Index" examines 14 different subject areas from the tourism sector for 136 countries, and them calculates an average value.

Rise in income from tourism

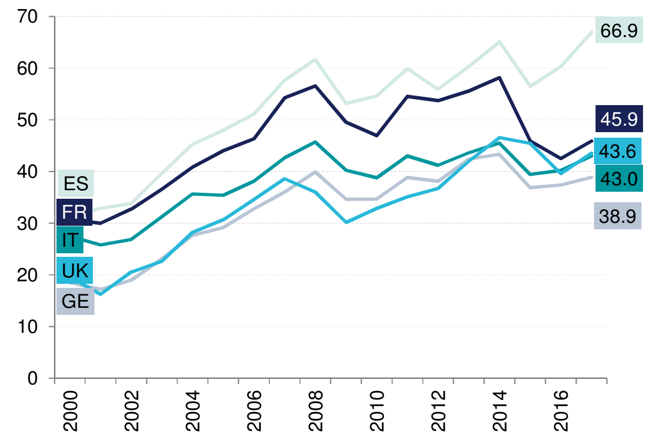
In terms of income from foreign tourists, after dips in 2015 and 2016, France once again posted an increase in 2017 of 8 percent to USD 45.9bn (provisional). With this, France lies in fifth place worldwide and in second place in Europe behind Spain.[49]

Arrivals of foreign tourists in million



Source: World Tourism Organization (UNWTO), figures from 2017 provisional, own research

Income from tourism in USD billion

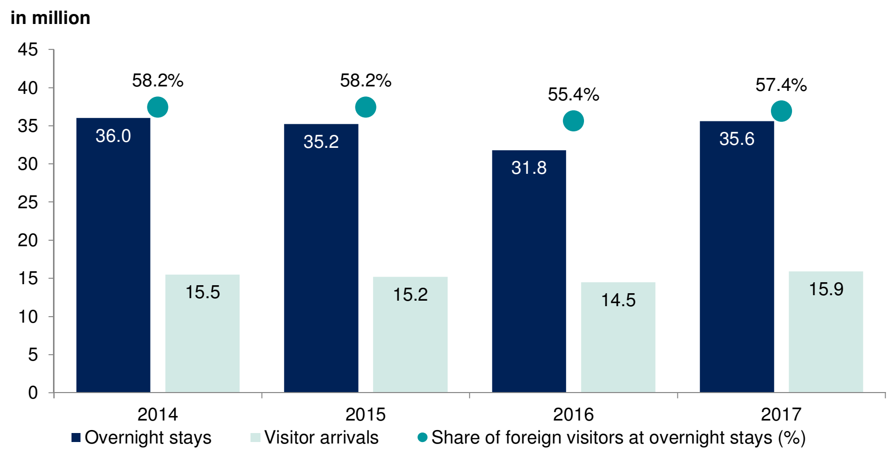


Source: World Tourism Organization (UNWTO), figures from 2017 provisional, own research

Paris as leading tourist destination

Île-de-France with Paris is France's key tourist destination. Worldwide, Paris is one of the most visited cities. In view of the many tourist attractions and a wide range of trade fairs and congresses, demand consists of a balanced mix of tourists and business travellers. In the years 2015 and 2016, the Paris hotel property market clearly felt the effects of the terrorist attacks. Particularly in 2016 compared with 2015, the number of overnight stays (-9.7 percent) and guest arrivals (-4.6 percent) fell sharply. In addition, demand from international visitors was considerably weaker. In 2017, the signs were once again pointing to recovery. With an increase of 11.9 percent to 35.6 million, the number of overnight stays had clearly recovered in 2017, with visitor numbers up by 9.7 percent to 15.9 million. Furthermore, the proportion of foreign visitors rose to 57.4 percent (previous year: 55.4 percent).

Paris: Overnight stays, visitor arrivals and share of foreign visitors



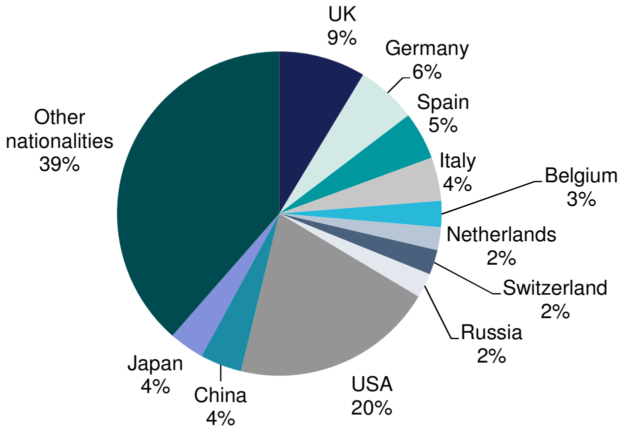
Source: Observatoire du Tourisme Parisien, own research

[49] World Tourism Organization (UNWTO): Tourism Highlights 2017 Edition/UNWTO: European Union Short-Term Tourism Trends, Volume 2 2018

High demand from the United Kingdom and the USA

The main countries of origin of foreign tourists in Paris are the United Kingdom and the USA. In the period January to November 2017, the shares in the total numbers of foreign visitors amounted to around 9 percent and 20 percent respectively. The proportion of German tourists was 6 percent. Visitor numbers from Japan developed particularly dynamically with an increase of 37 percent compared to the same period of the previous year.

Paris: Countries of origin of foreign tourists (January to November 2017)



Source: Office du Tourisme et des Congrès Paris, own research

Paris: Slight increase in hotel accommodation in 2017

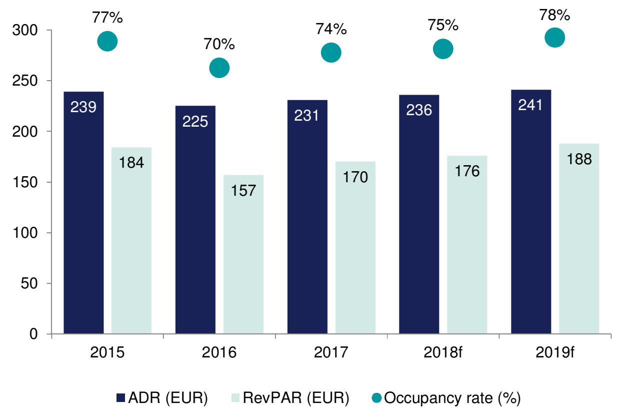
Accommodation in Paris increased slightly in 2017 by 0.5 percent to 1,573 hotels and 80,617 rooms. In total, the accommodation consists of a good proportion of 3-, 4- and 5-stars hotels. In the lower categories, only a small choice is available. Compared to London, for example, hotel accommodation growth in Paris is only possible to a very limited extent. The trend is currently predominantly for 4- and 5-stars hotels. For example, the opening of the luxury hotel Cheval Blanc (LVMH) in the former department store La Samaritaine is scheduled to take place in 2018.[50]

Paris: Improved hotel performance in 2017

The performance figures for 2017 also show that the Paris hotel property market has made a marked recovery after the attacks. In 2016, performance dropped considerably despite the Football European Championships and the Paris Motor Show. The revenue per available room (RevPAR) fell by 14.7 percent to EUR 157, notably due to the 9.1 percent reduction in occupancy rate. The average daily room rate (ADR) fell by 5.9 percent to EUR 225. In 2017, the RevPAR rose significantly again by 8.3 percent to EUR 170. The occupancy rate (+5.7 percent to 74 percent) and the ADR (+2.7 percent to EUR 231) were also up. The positive performance is likely to continue given the good macroeconomic conditions in 2018 and 2019. The expected increase in ADR to EUR 241 by 2019 is based, in particular, on the upward trend of luxury hotels in Paris. The RevPAR is forecast to be around EUR 188 by 2019. This would mean that Paris would be in first place Europe-wide ahead of Geneva in terms of room yields.[51]

[50] PwC: Best placed to grow? European cities hotel forecast for 2018 and 2019, April 2018
[51] ibid.

Paris: Development of hotel performance



Source: STR Global, forecast(f): PwC, own research

Paris: Hotel performance in 2017 by category

Category	ADR (EUR)	RevPAR (EUR)	Occupancy rate (%)
1 star	-	-	-
2 stars	71	53	75
3 stars	102	82	77
4 stars	176	140	75
5 stars	400	297	71

Source: Office du Tourisme et des Congrès Paris, own research

Transaction volume distinctly lower

The transaction volume in hotel property was down significantly in 2017 by 28 percent to EUR 1.496bn. This means that in Europe, France slipped back to fifth place.[52] On average, two-thirds of the focus of hotel investment is on Paris. Prime yields in fiscal year 2017 were between 4.5 and 5.5 percent in the capital. Paris is considered an extremely liquid market which offers investors attractive diversification opportunities.[53] This is also confirmed by the current result of the Hotel Investment Attractiveness Index (Europe 2017). Out of 20 large European cities, Paris was in first place ahead of London and Barcelona. In this respect, particularly the lower development costs compared to London had a positive effect. [54]

Outlook for hotel property market

Demand	↗
Supply	→
RevPAR	↗
ADR	↗
Occupancy rate	↗
Investment volume	→

France’s hotel property market has recovered considerably from the losses caused by the terrorist attacks of previous years. The number of foreign tourists increased noticeably again, and this was reflected in the performance figures. The risk of geopolitical unrest and terrorist threats still remains. There is also uncertainty because of Brexit, since the United Kingdom is one of France’s most important countries of origin for foreign tourists. Beyond this, there is strong competition from private accommodation portals such as Airbnb. However, overall we assume that 2018 will be a positive year for the French hotel property market unless any further unrest occurs. This will probably be supported by improved economic conditions. In summer 2017, the new tourism strategy - “Plan Tourisme” - was also presented, with its primary focus on quality, security and the creation of new jobs. Within this framework, the visa application procedure is to be speeded up and the waiting time for border controls at airports reduced. The aim is to further enhance the attractiveness of France for foreign tourists. The quantitative aim of this strategy is to increase the number of foreign visitors to 100 million by 2020 and raise revenues to EUR 50bn. The Olympic Summer Games in Paris in 2024 should provide a further and long-lasting tailwind. Overall, despite the uncertainty, the signs bode well for a dynamic hotel property year in 2018.

[52] CBRE: Marketview Snapshot, Europe Hotel Investment Q4 2017
[53] Jones Lang LaSalle: Paris hotel market 2017
[54] The Colliers Index includes 12 weighted study variables such as per capita GDP, number of employees, occupancy rate, ADR and RevPAR.

7. Residential property market

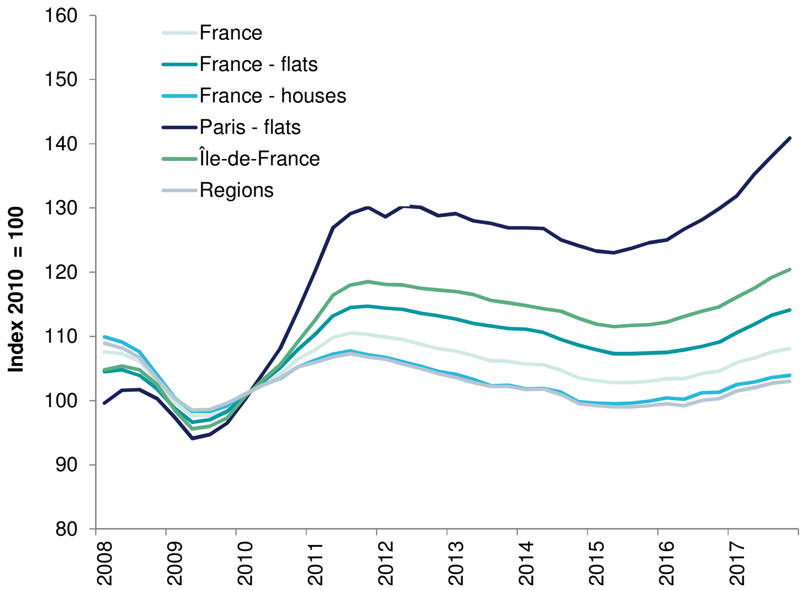
Residential property market in upswing

The French residential property market has been in an upswing phase since 2016. While in the years 2012 to 2015 the demand for houses and apartments combined with weak economic growth was sluggish, the residential property market developed dynamically in 2017. With positive economic development, a decline in unemployment and the historically low interest rates, the general conditions are extremely favourable. The amount of house-building loans reached a new record figure in 2017 of EUR 272bn (previous year: EUR 252bn).[55] In addition, the number of households is growing steadily. Given the positive demographic trend combined with an increase in smaller households, a national increase in households of approximately 3.2 percent is forecast for the period between 2017 and 2022. While a growth rate of approximately 2.8 percent to around 5.5 million households is expected for Paris, the predicted regional increases are considerably higher in some cases. The leaders are Toulouse and Bordeaux, with an expected increase in households of approximately 6.8 percent (633,000 households) and of approximately 5.7 percent (579,000 households) respectively.[56]

Rising prices on the housing market

After prices for French residential property dropped in the period from 2012 to 2015, the price level has again increased dramatically since 2016 due to the dynamic growth of demand. Particularly large increases were reorted in Paris in the apartment segment. Here, prices have risen by over 40 percent since 2010 and at the end of 2017, they were well above the last all-time high at the beginning of 2012. The other segments, however, also performed extremely positively. From a regional perspective, the price level has increased far more strongly in Île-de-France in the past two years than in the other French regions, with the result that the price discrepancy between Greater Paris and the provinces has further widened.

Price trend on the housing market



Source: Notaires, INSEE (Q4 2017 forecasts), own research

[55] CBRE: France Residential, Q4 2017
[56] Knight Frank: France Insight 2017

Significant regional price gaps in the existing apartments segment

The regional price gaps are especially apparent in the apartments segment. In Q3 2017, the average purchase price for existing apartments in Paris was EUR 8,940/m², which equates to an increase of 7.7 percent compared to the same period in the prior year. Considering that the top prices are over EUR 16,500/m², there are therefore considerable price differences within Greater Paris. Regionally, the city of Bordeaux registered the highest increase in the average price of older apartments with a plus of 11.9 per cent to EUR 3,730/m². This price increase is, among other factors, due to the TGV high speed rail link inaugurated in summer 2017 between Tours and Bordeaux, thereby reducing the journey time from Bordeaux to Paris from over 3 hours to 2 hours. The attraction of Bordeaux has increased hugely due to the significantly lower property prices in Bordeaux and now the quicker accessibility of Paris. Furthermore, Lyon posted a sharp price increase with a plus of 7.6 percent to EUR 3,670/m², but at a much lower level than Paris.[57]

Rising prices on the house market

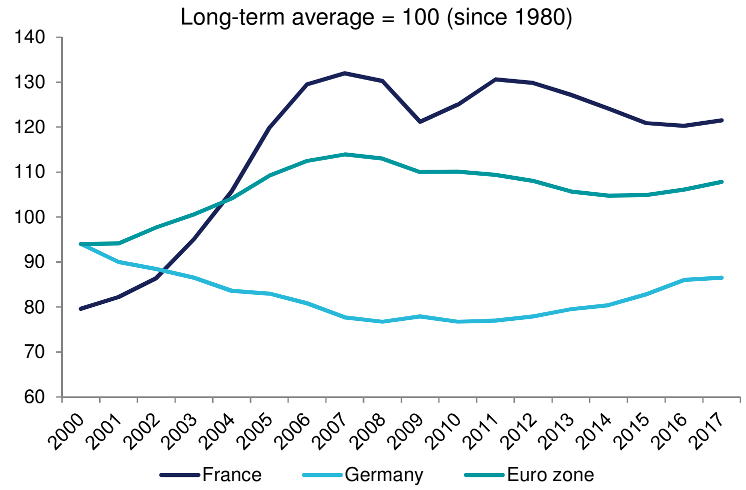
The French market for existing houses stands out because of the lower price gaps between Île-de-France and the regions. In addition, the price situation on the housing market is occasionally more challenging in the individual regions than in the capital city region. In Greater Paris, the average price for older houses in Q3 2017 was EUR 307,400 (+ 2.7 percent yoy). On the other hand, prices in popular tourist destinations on the Mediterranean are considerably higher in some cases. In the port city of Toulon, the average house price of EUR 359,800 (+3.7 percent yoy) in Q3 2017 was the highest nationally, followed by Marseille/Aix-en-Provence at EUR 341,500 (+9.4 percent yoy). In Bordeaux, the TGV effect also made itself felt on the development of house prices. Hence, prices for existing houses increased by 8.0 percent to EUR 310,000 compared with Q3 2016. On the other hand, in northern France, the prices of older houses are far lower in cities such as Lille, where they stand at EUR 189,700 (+2.5 percent yoy).[58]

Improved affordability

A glance at the affordability index for houses (relationship between house prices and disposable income) in France shows that the figure in 2017 is 21.5 percent higher than the long-term average of 100, but the valuation ratio initially dropped down after the high in 2011 and went up again slightly in 2017. Improved affordability can be attributed, for example, to the favourable financing conditions. In addition, at the beginning of 2016, public funding through interest-free loans (Prets à Taux Zéro) was extended from up to 26 percent to up to 40 percent of costs.[59] In Germany, the house price/income ratio in the period under review 2000 to 2017 was well below the long-term average of 100, meaning that affordability on the German house market compared with the French market is far more favourable. One criticism concerning the above data is that this index represents the housing market as a whole and does not enable any conclusions to be drawn about regional markets.

[57] Notaires de France: French property market report No. 38, January 2018
[58] ibid.
[59] GTAI: Property market in France sends positive signals, April 2016

Affordability Index (price-to-income ratio)

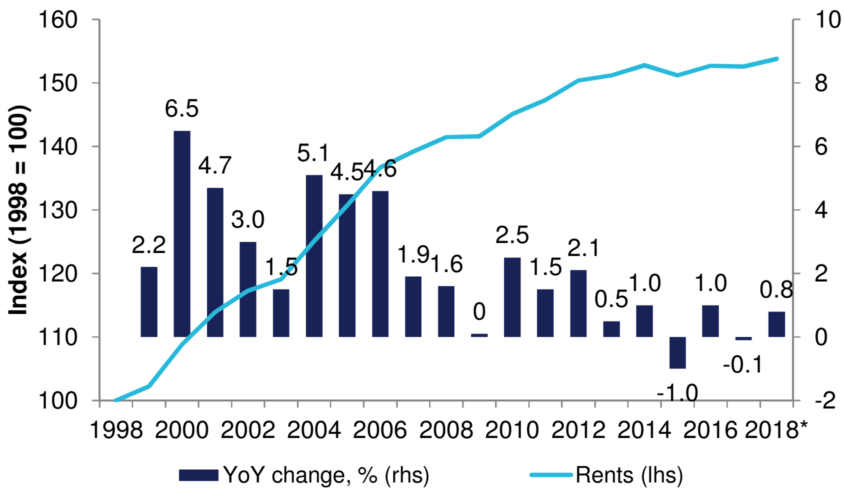


Source: OECD, own research

Challenging rental market in Île-de-France

The national average apartment rent in February 2018 was EUR 12.70/m² and was therefore at a stable level, although there are significant regional differences. Particularly high rents have to be paid in Île-de-France, whereby the smaller the apartment, the higher the price is per square meter. The average price per square metre for a one-room, unfurnished apartment in February 2018 was EUR 23.80. Nationally, the rental rate for a comparable apartment was EUR 17.10/m². According to the rental index based on the 1998 rates, the national rate for 2018 was 153.8 points. In Île-de-France the figure was consequently higher at 165.5 points.[60]

Change in rents



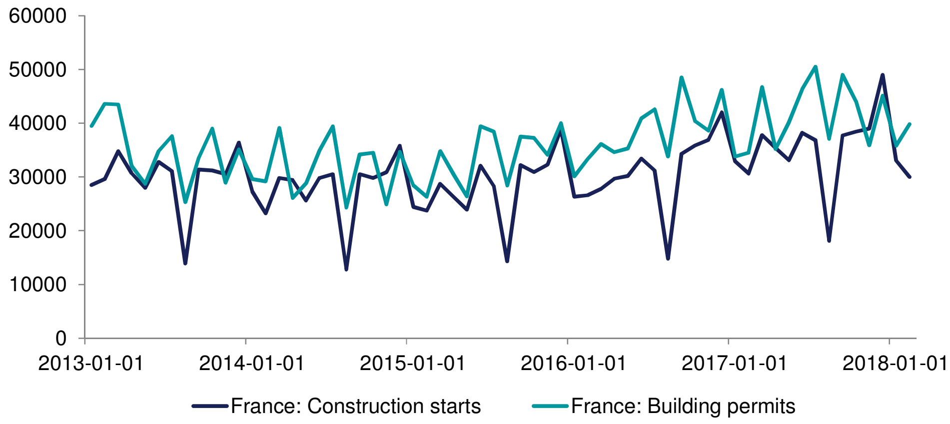
Source: Clameur, own research, *as at February 2018

Dynamic construction activity

The economic recovery is also reflected in the French building industry. Since 2016, construction activity has increased markedly, with momentum again rising in 2017. In fiscal year 2017, the number of house building starts stood at 427,000, which represents an increase on the previous year of 15.7 percent. Planning approvals also increased by 8.2 percent to 498,300. The record level from 2006 and 2007 has not been reached, but the upturn is palpable and is providing positive signals for France's residential property market.

[60] Clameur: Les tendances du marché entre 1998 et 2018

Change in construction starts and building permits



Source: Bloomberg, own research

Number of transactions at record level

Since 2015, the number of transactions on the French housing market has risen markedly, with investor focus on Paris. The cumulative number of transactions for existing properties over twelve months stood at 968,000 at the end of October 2017 (previous year: 845,000), which is a new all-time high. This is particularly due to the low interest rates combined with improved affordability. Prime yields in 2017 ranged between 2.5 and 3.0 percent in Paris and between 3.9 and 4.5 percent in the regions.[61]

Outlook for residential property market

Household demand	↗
Supply of housing and construction activity	↗
Prices	↗
Rents	↗
Investment volume	↗
Prime yield	↘

2017 was an extremely dynamic year for France’s residential property market. In addition to the improved economic situation, this was due to the currently favourable financing conditions, which significantly increased demand for mortgage loans. The dynamic demographic trend compared to other western European countries also had a positive effect. Accordingly, purchase prices for apartments and houses rose appreciably, although there were considerable regional differences across the country. In particular, the price delta between the housing market in Greater Paris and the regions widened further. The housing market in Paris is set to remain challenging in 2018. We also assume a further increase in transactions combined with downward pressure on returns. The Grand Paris infrastructure project should provide further impetus for the residential property market of Île-de-France. This project will increase the housing stock substantially and is described in the following chapter.

8. Digression: The Grand Paris project

Europe’s biggest infrastructure project

The Grand Paris project is one of the largest urban developments in Europe. Planning began as early as 2007 under the former state president, Nicolas Sarkozy. The project is scheduled to be completed by 2030. The main aim is to restructure the economic development of the regions around Paris city centre. In particular, the suburbs are to be connected to Paris city centre by an underground circle line around the city. The previously comparatively small city area of Paris is consequently to be enlarged to Grand Paris. With this circle line, Paris will more than double in terms of area and increase the number of inhabitants from the existing around 2.2 million (by comparison Berlin: 3.7 million inhabitants) to approximately 7.0 million. Grand Paris would then be comparable infrastructure-wise with major conurbations such as Greater London with around

[61] CBRE: France Residential, Q4 2017/CGEDD

9 million inhabitants. This would greatly increase the attractiveness of many of the suburbs. The biggest contractor is Société du Grand Paris, which is responsible for project implementation. The socio-economic goals include strengthening economic development, establishing and revitalising urban centres, providing a more intensive city experience, building a more attractive public transport network, promoting better integration of the boroughs and overall, creating a sustainable Grand Paris. The total cost is put at over EUR 35bn. On top of this, there is approximately EUR 6 to 10bn for residential, office and commercial property facilities which are to be created around the new Metro network. The project will be financed entirely by the public sector. It has not been decided yet how quickly and to what extent Paris and the surrounding area will merge administratively. In 2016, the Métropole du Grand Paris was founded, which is to unite the centre and 130 municipalities and towns and be responsible for land use planning and transport.[62]

Project description

The project covers a total of four new automated Metro lines with a 200 km-long rail network and 68 railway stations. In addition, two existing lines will be extended. Ninety percent of the new lines are to run underground with an average depth of 35 m. The lines running mainly through the Paris suburbs are to connect the regional centres through a link to the three Paris airports Charles de Gaulle, Orly and Le Bourget, so that they are more closely linked to the city centre. For example, the journey time from Gare de Lyon railway station to Orly airport should be reduced from 50 to 25 minutes. The aim is also to improve the links between the business districts and scientific clusters around the suburbs and combat urban sprawl. Daily passenger traffic of 2 million persons is expected for the new Metro lines. The timetable is quite tight. The first section is scheduled for commissioning in 2019. All the sections should be completed by 2030. The award of the Summer Olympics for 2024 to Paris especially creates a high priority for important connections in the north to Saint-Denis-Pleyel.[63]

Importance for the Paris property market

Within the scope of the Grand Paris project, new urban districts are expected over a total area of 140 km². In the suburbs, between 250,000 and 400,000 new apartments are to be built. Rises in purchase prices for apartments that will be located close to the new railway stations and where completion is planned in the coming years is already evident. One example is the extension of Line 14 to Saint-Denis-Pleyel. The suburbs in the south, such as Montrouge, Clamart and Pont de Sevres, are also in demand. Purchase prices in Clamart of EUR 7,000 to 8,000/m² are already almost at the level payable directly in Paris. It is also apparent that in places where completion of the Grand Paris Express is not planned until after 2024, as yet, there has been no effect on property prices. Improved accessibility is also expected to significantly enhance the attractiveness of the office market of Paris suburbs. One of the largest residential area projects in the region is Les Lumières Pleyel, with a gross floor area of approximately 176,000 m², where offices, hotels, apartments, student apartments and sports and leisure facilities are to be built. Until now, in the main, it has been French investors that have participated in the invitations to tender. In future, the Grand Paris project is also to be marketed more intensively abroad for the purpose of creating a number of international investment opportunities.[64]

[62] Credit Suisse: Thematic Insights: Infrastructure September 2017/Handelsblatt: 1 February 2018
[63] Jones Lang LaSalle: Why invest in Paris? 2017/Vinci: Grand Paris Express: Europe’s biggest infrastructure project, December 2017
[64] Handelsblatt:1 February 2018/MilleursAgents: Paris: Les prix de l`immobilier par métro

Opportunities for retail trade

The expansion of the Grand Paris Express offers a raft of opportunities for the retail property market. Two-thirds of France's travel retail revenue is generated at airports and Metro stations. The importance of the travel retail sector is illustrated by comparing the numbers of visitors. Gare du Nord railway station has a daily customer frequency of 700,000, which is considerably higher than the 125,000 of Les Quatre Temps shopping centre in La Défense, one of France's most popular shopping centres. Given that the number of Metro users is expected to rise by around 40 percent to 2 million passengers a day, this offers considerable potential for the retail trade. The majority of Metro users are commuters who have limited time and prefer to use the shopping amenities in the Metro stations. They appreciate 24/7 shopping on their way home 365 days a year. This makes Metro stations in residential areas a particularly attractive prospect for retail. Bearing in mind that Paris has around 15 million visitors a year and with Charles de Gaulle, the second-largest airport in Europe, Charles de Gaulle, tourists are another key consumer group. Above all, the new Metro stations will become more attractive for airports with high customer traffic. The focus here is mainly on retail concepts such as pop-up stores and concept stores with innovative products and higher margins.[65]

Economic impact

The economic impact of the Grand Paris is estimated to be considerable. The merger of key hubs such as research and development, health and biotechnology is expected to bring a positive economic effect of over EUR 29bn.[66] Added to this is the extra tax revenue. Société du Grand Paris anticipates that long term, 115,000 new jobs will be created and a further 15,000 during the construction period. Owing to the increased use of public transport instead of people using their cars, it is also anticipated that greenhouse gas emissions can be cut to around 27 million tons.[67]

Conclusion

The Grand Paris project, which already started eleven years ago, is Europe's largest infrastructure project. The core city of Paris is to merge with the surrounding area by 2030, meaning that the number of inhabitants will roughly triple. The times when the centre of Paris was enclosed by the orbital motorway will be a thing of the past. As described, this should generate considerable growth momentum for the economy and create a large number of jobs. The effects on the property market are regarded as very positive, with significant potential for investments. Whether the challenging housing situation in Paris city centre can be improved remains questionable, however, we assume that the very high demand in the city centre will continue and that the price level will stay the same. It will be a challenge to keep the construction time and costs under control given the length of the project. All in all, the Grand Paris project will give Paris the opportunity to become the most attractive capital in Europe.

[65] Savills: Grand Paris Express to create potential ´gold mine` for retailers, November 2017
[66] Business Immo, Mars 2018/Jones Lang LaSalle
[67] Credit Suisse: Thematic Insights: Infrastructure September 2017

9. Outlook

Outlook for France's property market

Demographic development	↗
Real GDP growth	↗
Unemployment rate	↘
Number of employees	↗
Retail sales	→
Tourism demand	↗
Demand for logistics real estate	↗
Household demand	↗

The French economy developed extremely dynamically in 2017. France's new president, Emmanuel Macron, provided positive signals for the economy with the package of reforms he announced. The French property market can benefit considerably from the economic recovery and significantly boost its attractiveness.

The rise in the number of office staff has meant that demand on the office property market in Greater Paris is currently very dynamic. The supply of core properties in Paris CBD has fallen sharply, and so interest in office space in alternative locations is growing. The office property market in Île-de-France already recorded a promising start, so that we expect the take-up to increase further in 2018. The capital is also one of the potential profiteers of Brexit. According to a Reuters survey published in March 2018, Paris is the most popular alternative location for job relocations from London, ahead of Frankfurt, Dublin and Luxemburg. Here, the Macron effect appears to be bearing fruit. France's stationary retail sector is currently under great pressure to change as a result of the boom in online shopping. It will be a crucial competitive advantage to be able to react to changing customer needs and develop attractive shopping experiences for customers. In view of the rental trend, a sideways movement is expected in the top locations. The logistics property market can benefit perceptibly from the strong growth of the e-commerce market. The Île-de-France region is experiencing particularly high demand for space. However, changes in consumer behaviour are also creating a considerable need for adjustment in the transport and city logistics sphere. Overall, logistics demand is set to remain high and continue exerting pressure on prime rents. The hotel property market is experiencing a significant upturn, with tourist numbers rising again after the terrorist attacks in 2015 and 2016. Especially in Paris, hotel performance figures improved substantially in 2017. We expect a continuing positive trend in 2018, although uncertainty remains. France's residential property market is developing extremely dynamically. There is unabated high demand for apartments in the centre of Paris, which is why rents are far above the national average. Given the currently favourable financing conditions, interest in purchasing property is particularly high at the present time. Demand is likely to remain dynamic in 2018, especially considering the prospect of a medium-term moderate increase in interest rates. Furthermore, Grand Paris, Europe's largest infrastructure project, is providing additional movement on the Paris property market and will offer a variety of investment opportunities in the years ahead. Beyond this, we expect the staging of the Summer Olympic Games in Paris in 2024 to have a positive effect on the property market. Paris is a particularly liquid and transparent market and is one of the most sought-after investment locations in Europe alongside Berlin and London. France's regional markets also offer interesting alternatives for investors. Since prime rents in Lyon have also come under considerable pressure, the city of Bordeaux offers significant potential, for example, due to the new shorter high-speed rail link to Paris.

Overall France's property market is in the throes of a dynamic upswing. The uncertainty in the international environment as a result of Brexit negotiations and US policy remains, but the prospects for 2018 are positive. We assume that fiscal year 2018 will be able to build on the successful property year in 2017.

Contact

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