



French Property Snapshot

Economy

The French economy remained weak in the first quarter of 2009 with GDP contracting by 1.2% quarter-on-quarter. The recession in France has been milder than in most other eurozone economies with the GDP decline half the size so far. Although activity is expected to fall further in the current quarter, business confidence rose for the third month running in May, while increased destocking of inventories suggests that the pace of contraction of activity may slow in the second half of 2009.

Industrial production dropped by 6.8% in the first quarter compared with Q4 2008, amounting to an annual decline of 15.5%. Although business investment is likely to remain moderate, firms are expected to face difficulties for some time, as weak exports restrain the investment cycle into 2010.

French consumer spending held up well in the first quarter with an unexpected increase of 0.2% in Q1. Household consumption of manufactured goods increased for the second consecutive month in April and has been boosted by a car scrapping scheme which lifted auto sales. Moreover, housing market activity is also beginning to improve, with a strong increase in sales during Q1 as a result of lower prices and more affordable mortgages.

Household budgets are being squeezed by falling employment levels, the bulk of which has been concentrated in temporary employees. The unemployment rate rose to 8.7% in Q1 and the number of unemployed was up by almost 530,000 from a year earlier; the largest increase on record, although the pace of increase has been less than that of the eurozone overall. Consumers have been provided some relief by easing price inflation. CPI inflation was down to 0.1% on a 12 month basis to April due to falling energy prices, having been at over 4% a year previously. However, inflation is expected to pick up moderately after the summer, implying a fall in real wages which, combined with the decline in employment, could depress spending.

Outlook

Interest rates in the eurozone have dropped 325 basis points since last October to just 1.0%, however, there is still scope of further interest rate cuts. In comparison to the US Federal Reserve and the Bank of England, the European Central Bank has been slow to cut interest rates and has only announced small scale "unconventional" measures to buy private sector assets.

With financial credit conditions difficult, there are some doubts over the effectiveness of monetary policy. As such, the French Government has announced various fiscal packages to encourage private sector spending at the cost of 1.5% of GDP in 2009. In particular, the Government is lowering the VAT rate for restaurants from July, at an estimated cost of €2.4 billion which will give some support to domestic spending.

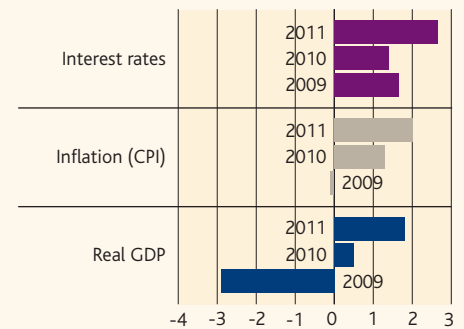
Nonetheless, the huge drop in manufacturing and export activity will cause the French economy to contract by 2.9% in 2009, according to our predictions. This would be the largest peacetime fall in economic activity since the 1930s. For 2010, we expect economic growth of 0.5% as manufacturing stages a modest recovery with better global trading activity, although a lack of labour market flexibility and high minimum wages mean that the economy is not in a strong position to benefit from higher global trading activity. A trend rate of growth of 2% is envisaged by 2011.

Risks

On the downside, after a modest slowdown in the pace of economic contraction in the months ahead, the global economy shows significant renewed weakness into 2010, due to the lack of final demand. Bank de-leveraging will not abate and low interest rates and quantitative easing will gain little traction. A negative feedback loop will develop between tighter financial conditions, weaker asset prices and the real economy.

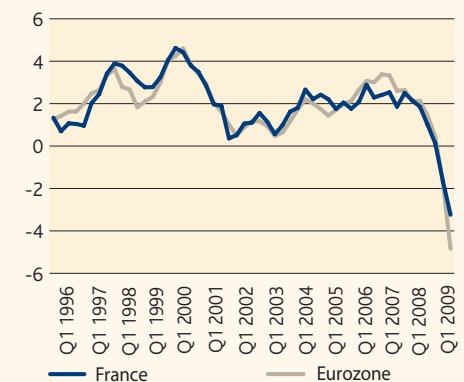
An upside scenario entails a stronger "V" shaped recovery in the global economy, with a more typical acceleration in activity in 2010, increasing growth in the region by 4-5%. The catalyst for such an upturn would be the unprecedented array of monetary and fiscal policy measures currently in place. If these policies take effect on domestic demand conditions more quickly than we assume in our base case scenario, trend-like growth could then be achieved by early 2010.

France economic forecasts (%)



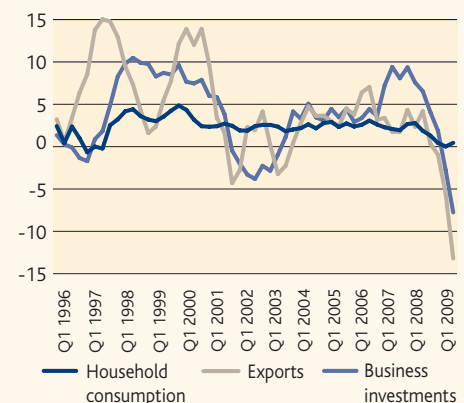
Source: Aberdeen Property Investors

French real GDP (% annual change)



Source: INSEE/Reuters

Falling exports, business investments and resistant consumer spending (% annual change)



Source: INSEE/Reuters

French Property Snapshot

Property market outlook

Recent performance

After three record years with total returns of above 15%, and for the first time since its creation in 1998, the French IPD All Property Index is in negative territory, recording a 0.9% decline in 2008. Whereas income returns remained stable for all property sectors, none have been spared by falling capital values. Capital returns are negative across the board for the first time. The 'All Property' capital return in 2008 was -6.0%, whereas income returns remained stable at 5.4%, due partially to favourable indexation effects.

The weakest total return was delivered by the industrial sector at -3.8%, followed by offices at -2.5%. Retail remained positive in 2008 with 1.9%, and residential at 1.5%.

Capital return for offices, fell by -7.9%. The Paris region markets have been the most hurt, with capital returns of -8.3% and -9.1% for the Paris CBD and the Paris WBD respectively. In contrast, offices in provincial cities outperformed, with a total return of 3.8%, pulled up by dynamic income returns of 7.9%, compared with 5.0% in the Paris CBD.

Despite the highest income return in 2008, at 7%, the industrial sector has been the weakest performer, with a total return of -3.8%, explained by a plunge of -10.1% in capital values.

In spite of a severe decrease, from 22.4% in 2007 to 1.9% in 2008, retail has been the only sector to produce a positive return in 2008, due to a limited fall of 'only'-3.4% in capital return.

Retail

The footfall in shopping centres has decreased sharply since the beginning of the year, despite a moderate growth in consumer spending. According to CNCC figures (covering 56 French shopping centres) footfall has decreased by -3.4% between H1 2008 and H1 2009, with a trough in May 2009, at an annualised -8.4%.

Hard discounters appear to be the main winners of the current turmoil having benefited from both the recession enticing consumers to their shops and the new LME (Loi de Modernisation de l'Economie) – raising the threshold of the requested approval for an opening from 300 square metres to 1,000 square metres – which has made the expansion of their networks easier.

Consequently, the main mass retailers, such as Carrefour or Auchan, have pushed the development of their own discount brand in city-centres.

Retailers, as investors, are now prioritising the best locations, preventing prime high streets from a big fall in rental values. Nevertheless, retailers suffering from the current crisis are increasingly prone to negotiate incentives with their landlords. In addition, a lower level of expected indexation in the near future - due to the generalisation of the new Index des Loyers Commerciaux, partly based on a low inflation should release pressure on rental values.

Office

After a decrease of 14% in 2008, letting activity in the Ile-de-France office market has continued to contract in H1 2009. The 860,000 square metres let during H1 2009 was 27% lower than in H1 2008, and has brought levels back to those observed in the first part of the decade. On a quarterly basis, take-up levels have stabilised in Q2 2009, for the first time since the beginning of the crisis.

Given the more stable market during Q2 2009, and assessing that the second half of 2009 will be at least as dynamic as the first, the take-up level for the whole of 2009 should amount to between 1.6 million square metres, in a worst case scenario, and 1.9 million square metres in the best case scenario. In any case, the take-up level in the Paris region might be in line with the long term average.

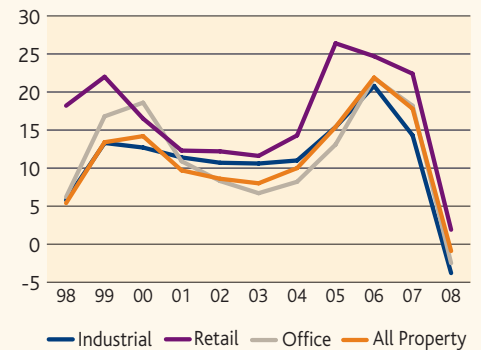
Merger and acquisition deals which currently dominate the letting market have resulted in older office space becoming increasingly vacant. As a consequence, immediate supply of lettable space has grown at a marked pace, reaching 3.2 million square metres at the end of Q2 2009, 8% higher than the level as at the end of Q1 2009.

Prime rental values, which were quite stable until Q1 2009, have started to fall, reflecting the gradually more important incentives granted by owners. The spread between facial and effective rental values has become too important, to keep the former stable.

The Paris market, as expected, was the first to experience a correction, with a decrease in prime rental values of around 10% since the market peak.

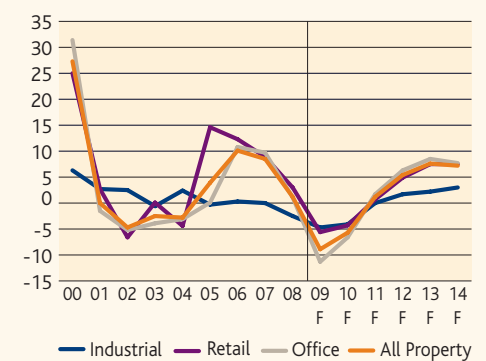
The French market is just at the start of this cycle, with rental values forecasted to decrease at least until the summer of 2010. Second-hand assets are obviously under more pressure than brand new ones.

Total return France (%)



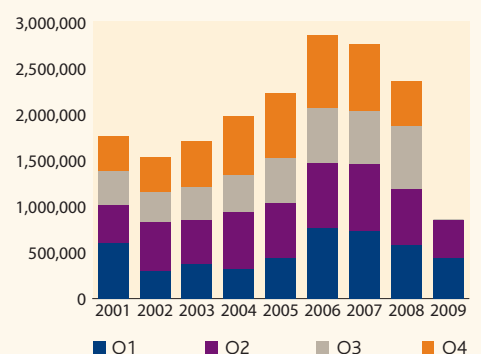
Source: IPD

Prime rental growth France (%)



Source: Aberdeen Property Investors

Office take-up in the Ile-de-France (in square metres)



Source: Immostat, July 2009

French Property Snapshot

Industrial

Following the weakening national consumption, production and exports, leasing activity in the industrial market has seen a sharp decrease in 2009. Tenants have been keen to renegotiate their existing lease contracts rather than implement an often expensive move. The main driver of those few deals observed in Q2 2009 is still cost cutting. Increasingly cautious about operating costs, tenants are looking for modern premises which allow them to rationalise their activities, in terms of property use.

Following the example of other asset classes, the activity has refocused on prime locations in prime markets. Indeed, the bulk of the activity has been on the North-South axis, from Lille to Marseille through Paris and Lyon, while other markets have been almost non-existent.

As a direct consequence of the lethargic letting market on the one hand and the delivery of speculative schemes launched in 2008 on the other, immediate supply has soared by 20% since the beginning of the year, reaching 2.9 million square metres at end of H1 2009. However, developers' activity has slowed, with the number of building permits granted falling by 15% since December 2008.

Given the weak outlook, rental values are on a decline. Incentives are increasingly common and tenants with low visibility are reluctant to agree to long term commitments. Nevertheless, French industrial rental values, currently amongst the lowest at a European level, shouldn't experience a sharp decrease.

Investment market

The investment market, completely static in Q1 2009, now seems to be moving again, after almost two years of continuing decrease in activity. Q2 2009 has seen the return of both foreign investors and larger lot sized investments. Three deals above €100 million have been recorded in Q2 2009, all on retail assets.

With €2.6 billion invested since the beginning of the year, H1 2009 represents 37% of the amount invested in the same period last year. This slump in investments is mainly explained by the total absence of large deals in Q1 2009. Indeed, the number of deals has 'only' decreased by 25% for the same period.

Property yields decompression is still ongoing, although the pace has slowed as the year has progressed. After 18 months, the yield movement is about to reach a floor, at least for prime assets. Prime office yields in the Paris CBD ranged between 6% and 6.25%, at the end of Q2 2009, a historically high level. On the other side, re-pricing should continue for secondary sizeable assets, which are less liquid and less sought after.

Investors are benefitting from historically low interest rates, largely compensating the higher bank margins. The spread between property yields and State bonds is now very positive, even for very prime assets, (more than 200 basis points for a prime office building in the Paris CBD), whereas only 18 months ago, the spread was negative.

Market outlook

In the second half of the year, capital values are likely to continue to fall, although no longer as a result of ending yield decompression, but now as a consequence of falling rental values.

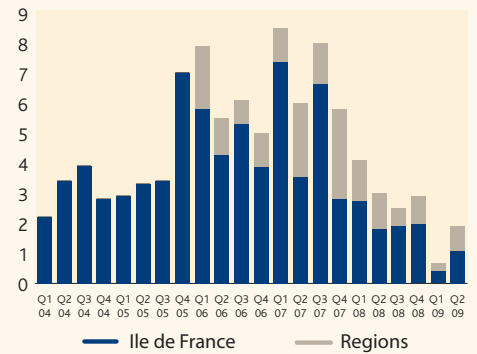
On a five-year basis to end June 2014, the retail segment is forecast to see the highest rental growth, at an average level of 1.8% per annum. This sector is expected to benefit from resilient consumer spending, which is forecast to remain in positive territory in the coming years.

However, the industrial segment is expected to go through the most difficult path, with an annualised -0.2% of rental value growth over the same period. Despite a relatively soft fall over the next couple of years, the recovery in rental values from 2011 is expected to be limited. As observed since the beginning of the crisis, the office segment is suffering the most from the current turmoil (with -9.2% forecast over the next 12 months), although should experience the sharpest recovery, with an economic growth come-back as of 2011.

For the first time since the beginning of the crisis, forecasts have not been downgraded from one quarter to another, reflecting the slower expected contraction in economic activity.

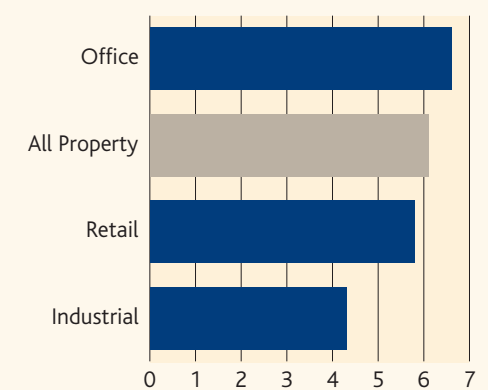
With an average total return of 6.1% per year, over the next five years to end June 2014, the French property market is forecast to outperform the eurozone average, at 5.3% per year over the same period.

French property investment market in € billion



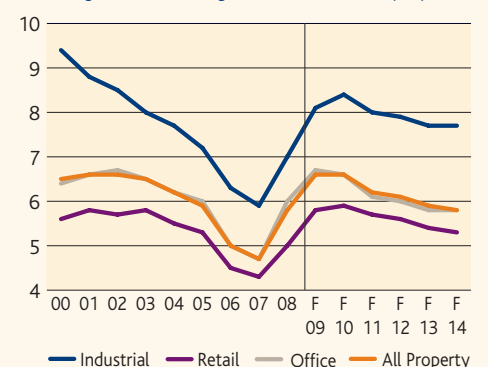
Source: CBRE, Atisreal

Five year rolling total returns (% per annum to June 2014)



Source: Aberdeen Property Investors, July 2009

Prime yields history and forecasts (%)



Source: Aberdeen Property Investors, July 2009

French Property Snapshot

The office segment is predicted to be the best performer, at 6.6% per year between June 2009 and June 2014, followed by the retail segment at 5.8% per year and finally, the industrial segment at 4.3% per year.

Investment policy

The table below shows Aberdeen's recommended positions on the French market, relative to the European EU Property Benchmark, in order to achieve outperformance over a five-year period.

| Sector | Strategy |
|------------|-------------|
| Office | Overweight |
| Retail | Neutral |
| Industrial | Underweight |

Important Information

FOR PROFESSIONAL USE ONLY

This document is strictly for information purposes only and should not under any circumstances be considered as an offer or solicitation to deal in the property market. Accordingly, no warranty whatsoever is given and no liability whatsoever is accepted for any loss arising whether directly or indirectly as a result of the reader acting on any information, opinion or estimate contained in this document.

The information contained herein, including any expressions of opinion or forecast has been obtained from or based upon sources believed by us to be reliable, but is not guaranteed as to accuracy, adequacy or completeness.

Some of the information in this document may contain projections or other forward looking statements regarding future events or future financial performance of countries, markets or companies and actual events or results may differ materially. Any research or analysis used in the preparation of this document has been procured by the company for its own use and may have been acted on for its own purpose. Aberdeen Property Investors does not accept responsibility for any loss arising from the use hereof.

The value of investments and any income from them may go down as well as up; they can be affected by exchange rate movements between currencies and it is possible that investors may not get back the full amount invested. Physical property assets are illiquid in nature and, under adverse market conditions, the sale of such assets may take a considerable time. Delays in selling underlying assets may lead to similarly lengthy constraints being placed on the sale of shares by investors in a fund. Past performance is no guarantee of future performance.

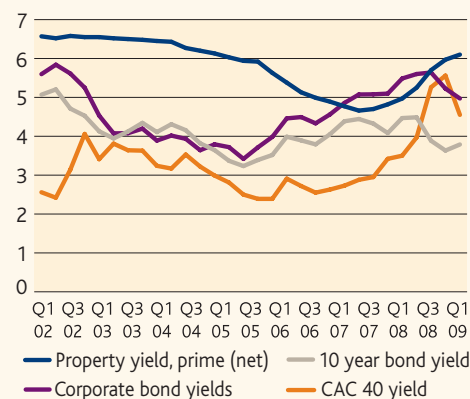
No part of this document may be copied or duplicated in any form or by any means or redistributed without the written consent of Aberdeen Property Investors.

© 2009 Aberdeen Property Investors. All rights reserved.

UK INVESTOR INFORMATION

Issued and approved by Aberdeen Property Investors UK Limited which is authorised and regulated in the UK by the Financial Services Authority.

Property, equity and bond yields (%)



Source: Aberdeen Property Investors, Reuters EcoWin, Thomson DataStream

Contact details

Massinissa Fedala - Research Analyst

Telephone: +33 1 7674 1767

Email: massinissa.fedala@aberdeen-asset.com

Dr. Thomas Beyerle - Head of Global Research

Telephone: +49 69 768072 241

Email: thomas.beyerle@degi.com

Alessandro Bronda - Head of Global Investment Strategy

Telephone: +32 4 7634 9279

Email: alessandro.bronda@aberdeen-asset.com

Website: www.aberdeenpropertyinvestors.com