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Istanbul Property Market

OFFICE · INDUSTRIAL · RETAIL · | Q4, 2011

Construction is Turkey's fastest growing sector expanding 24.6% in Q3 2011 with demand for prime A Class residential units and A Class office space well outstripping supply.

Law firm Chadbourne & Parke entered the Turkish market opening an office in Istanbul in September. The Carlyle Group acquired a 48% stake in Bahçeşehir College. Dow Chemical Group along with Aksa signed a $1bn manufacturing deal. Vodaphone acquired Koç.net in a $22.99mn deal aiming to corner the corporate market. IHH is to buy a controlling stake in Acıbadem Medical Group.

Mergers and aquisitions reached US$15bn in volume with a total 74% out 241 transactions involving foreign parties.

A continuing thorn in Turkey's proverbial side is the grey market with informal or "grey" trade held responsible for $2.6bn of the country's current account shortfall with analysts attributing 40% of all activity annually to the grey market.

4th QUARTER AT A GLANCE

- Prime Office Rents →
- Prime Office Yields ↓
- Vacancy Rates ↓

OVERVIEW

Turkey's overheated economy marginally slowed down in the Q4 2011 as the European economic crisis took its toll on the world markets. Nevertheless, GDP growth, standing at 10.4% in August, was projected to be 10.6% by year's end up from 8.9% in 2010. FDI stood at $12.1bn in December, an increase of over $2bn from 2010. EU countries took the lion's share of FDI in Turkey providing at least 90% of all foreign investment in 2011.

Inflation stood at 11.89% year end, a rather steep increase from 7.9% a month earlier in November. The government's 2011 target was 5.5% with an almost identical target being set for 2012.

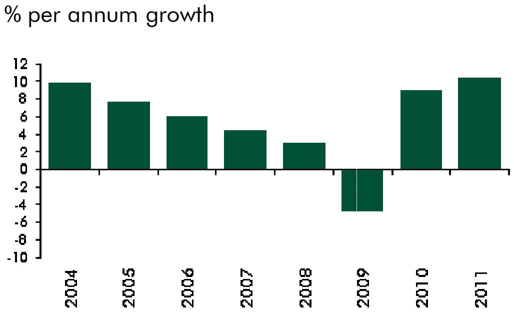
Unemployment dropped to 8.8% in October last year, a sharp from 11.9% of the same period in 2010. The service industry holds the largest percentage of employment with 49.5%, followed by the industrial sector at 26.8% and then the agricultural sector at 23.7%.

Turkey's ever billowing account deficit peaked to an all time high of $78.6bn in December standing at around 10.2% of the GDP, around 80% higher than the same time last year with energy imports especially natural gas accounting for nearly two thirds of the country's deficit in 2011. The Turkish Lira was the worst performing currency against the US Dollar, amongst others, depreciating by over 22% last year to almost a record low of 1.92tl in late December. The Turkish Central Bank intervened and sold off over $3bn in the last days of 2011 to stave off further slides with only minimal effect.

Turkey has been criticized for not sufficiently increasing interest rates enough to stave off any ripple effect from the EU's ongoing economic crisis. Interest rates hovered at 11% on average in December with a corridor of 10.5% to 12.5% up from 7.5% to 10.5% earlier in the year. The current one week repo interest rate stands at 5.75%. The earlier low rates encouraged a trend of "spend" rather than "save" with a low savings rate of approximately 12% of the GDP.

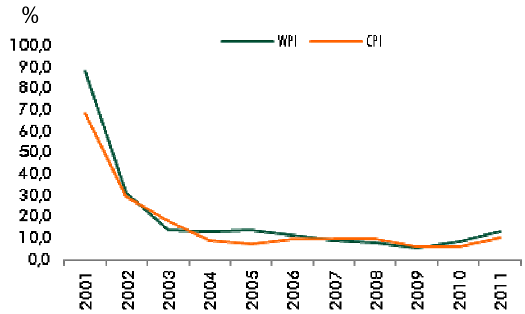
There was a steady increase of 18.2% in foreign export trade from 2010 with $134.6bn in exports by year end having made the Turkish government's target of $134.8bn for 2011 a rather good estimate. There was also a substantial rise in imports from 2010's $185.5bn to 2011's $240bn raising the trade account deficit to over $105bn though there was a drop of $200mn in November. Turkey's biggest trading partner is still the EU with European Union countries accounting for 40% of all foreign trade. Moreover, bilateral trade between Turkey and the EU currently stands at $134bn, an increase of $34bn from 2009's economic crisis period. Turkey's largest exporting industry is the automotive sector with car exports rising 16% to $17.38bn. Second from the top is the textile sector rising 10% to $14.64bn. The third best performer is the chemical sector increasing 32% to $12.72bn. Agriculturally based sectors account for 13.4% of overall exports, industrial sectors account for 82.3% and mining sectors account for 3.22%.

GDP GROWTH IN TURKEY



Source: CBRE

INFLATION RATES



Source: CBRE

THE OFFICE MARKET IN ISTANBUL

The Istanbul office market continued to be active in the fourth quarter of the year and a number of leasing transactions were completed by several multinational companies.

CBRE completed a leasing transaction for Servcorp Tekfen Tower and several lease renewals for a few multinational companies in their existing buildings following a five year occupation at full market rates.

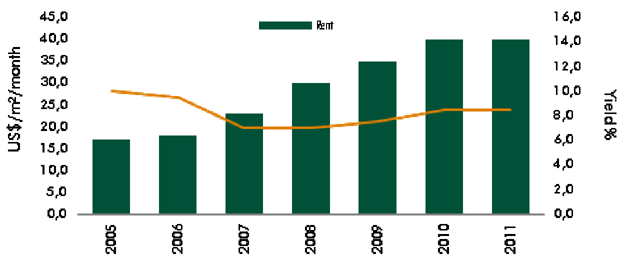
In the Metrocity D Block in Levent, the owners achieved a rate of $25/sqm/m for a 2250sqm office space. The vacancy rate on the European side of Istanbul remains slow in spite of asking rents in prestigious office towers remaining between $30-$43/sqm/m range in Levent and Esentepe. The vacancy rate in the secondary market of Maslak is around 4% and the rents here vary between $18-$30/sqm/m.

In the decentralized neighbourhoods of Kavacik and Umraniye on the Asian side of the city, there is plenty of space still available at rents varying between $20-$25/sqm/m.

The owners achieved a rate of $20/sqm/m for a 1660sqm office space in Kavacik Ticaret Merkezi in Kavacik.

A new office tower known as the Nida Kule Goztepe is being developed by Nida Insaat on the Asian side and is expected to be completed in mid 2012. The project will comprise 29,000sqm GLA in total and the asking rents varying between $25-$30/sqm/m in accordance with the level of the leased floor.

PRIME OFFICE RENTS AND YIELDS



Source: CBRE

OFFICE AREAS IN ISTANBUL

Source: CBRE

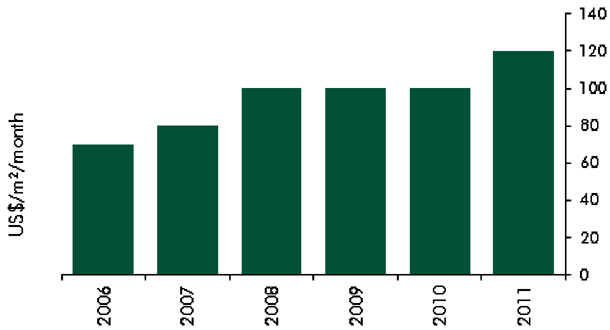
NIDA KULE GOZTEPE

SOYAK kristalkule

CBRE

ISTIKLAL STREET

PRIME RETAIL RENTAL LEVELS



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INDUSTRIAL AREAS IN ISTANBUL

THE RETAIL MARKET

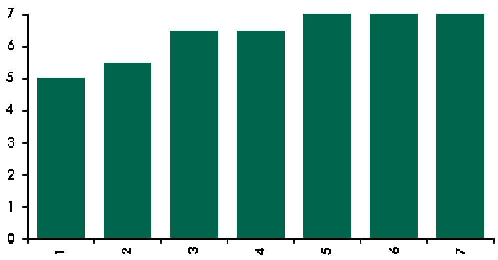
The retail market continued to be active in the fourth quarter of the year with the opening of new shopping centres. According to Turkey's Council of Shopping Centres, the highest retail sales in this sector were recorded in November of 2011. Q4 2011 was the best performing period (m2) of efficiency since the beginning of 2010. Many international companies opened their first stores in 2011 because of the steady economic growth experienced in Turkey over the past two years. Victoria Secret, Bath and Body Works, Michael Kors, Adolfo Dominguez and Emporio Armani Ristorante are just a selection of those which found the Turkish retail market an attractive environment to invest in during late 2011. Eventhough there is a long list of foreign brands actively investigatng Turkey, a few companies have recently announced the postponement of their entry into the Turkish retail market because of the risk of potential negative economic exposure from the EU in 2012. Therefore, the outlook for foreign investment into the Turkish retail sector has been revised from postive to conservative for 2012. The yields for shops in prime high street locations were considered to be 6,50% and for the shopping centers 8,00% in the last quarter of 2011.

THE INDUSTRIAL MARKET

Although the industrial market slowed down in the last two quarters of 2011, many foreign developers & occupiers were still actively investigating the industrial market in Turkey in order to set up their own production facilities in the near future. There weren't any notable leasing or sale deals closed in the fourth quarter of 2011. However, there were a few small land sales closed between local companies in the last months of 2011. Market investment estimates are conservative for the first half of 2012 with a slow year predicted in general. Rents continued to remain stable in the industrial sector at around $6.0 to $7.0/sqm/m in Hadimkoy and $5.5 to $6.5/sqm/m in Gebze. The yields for industrial properties were considered to be 10,50% in the last quarter of 2011.

INDUSTRIAL RENTAL LEVELS

US$/m²/month



Source: CBRE

LEASE TERMS

Occupational leases are generally short, being for periods of up to five years, usually quoted in US dollars or Euros. A form of indexation generally revises rents annually, which may be to a fixed percentage of a variable such as US inflation or treasury bills. Rent is currently subject to VAT @ 18.0% (which is recoverable by corporate tenants) or to a non-recoverable withholding tax of 20.0% with a 10.0% surcharge when landlords are private individuals. Retail rents are generally based on turnover subject to a minimum basic rent. Insurance premiums and property taxes are generally paid by the landlord. New properties are leased on a "shell and core" basis with tenants being responsible for fitting-out costs although landlords can sometimes be persuaded to participate in these costs by granting rent-free periods. Services charges are payable by tenants and currently represent approximately US$7.00/m²/month to US$12.00/m²/month in modern air-conditioned offices. They are significantly higher in shopping centers because of extra services required such as security, cleaning of common areas and other high maintenance costs associated with heavy pedestrian traffic.

YIELDS

Although there have been few transactions to test yields in the various sectors of the markets; office, retail and industrial, it is safe to assume that yields generally are coming under pressure not least because of interest shown in the Turkish market by foreign investors. Hovewer, we estimate the prime yields for offices would be in the region of 7,75% , 8,0% in the retail sector and 10,50% in the industrail sector.

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