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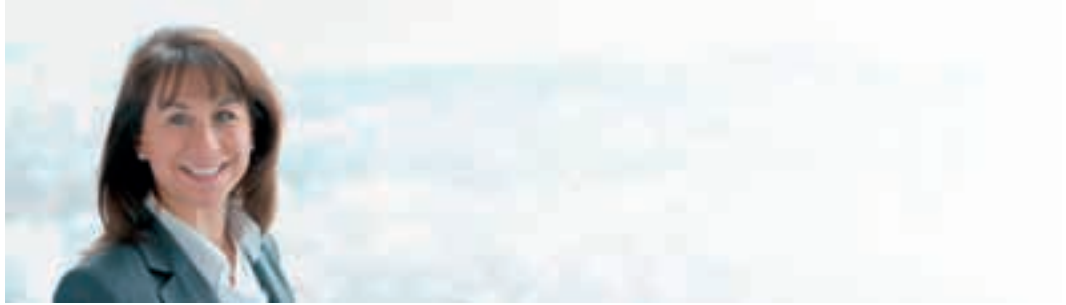
Frankfurt Office Market: Quality Counts

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Editorial



Dear reader,

As an integrated universal bank with strong regional roots, we feel a special sense of commitment to Hesse and Thuringia. That is also true for the focus of our research. For example, in the past we have already prepared numerous analyses on the financial centre Frankfurt and the economic development of Hesse and Thuringia, and have identified the 100 largest companies in these two federal states.

With a view to the core business areas of Helaba, we have now expanded our research through the addition of real estate analyses. In the real estate report that has been published regularly since April, we identify and examine trends in various real estate markets and investments.

In the present special study, “**Frankfurt Office Market: Quality Counts,**” we combine specialized knowledge about the region with real estate expertise. Manhattan - as Frankfurt is also called - is among the most important office locations in Germany. In fact, with its striking skyline, the city is unique in Europe. And its economic productivity is also outstanding: nearly a quarter of Hesse’s economic strength is generated in Frankfurt, which accounts for only 11 % of the state’s population. No other city in Germany has such a prominent position within a federal state.

And while the financial crisis left its mark also on the Frankfurt office market, signs indicate a stabilisation by the end of 2010, which means that office real estate in the financial metropolis will presumably present itself in better shape again in the coming year.

In Frankfurt a number of urban development projects are in the planning stage, which envisage a more or less large ratio of office utilization. Each one of these projects offers the city of Frankfurt excellent development opportunities over the long term. However, in view of what is expected to be fairly moderate demand for office space in the coming years, it is important to bank on quality, not quantity. That is the only way to do justice to the high standards that are placed on office space in Frankfurt.

Yours sincerely,

Dr. Gertrud R. Traud
Chief Economist/Head of Research

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Summary

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For valuable information on the Frankfurt office market we are grateful to Mr. Peter Salostowitz, GIB Gesellschaft für Immobilienbewertung, and Mr. Il-Sin Chung, OFB Projektentwicklung.

Focused economic power in southern Hesse

Frankfurt plays an outstanding role in Hesse. Nearly a quarter of Hesse's economic output is generated here. No other city in Germany holds such a prominent position within a federal state. In the national ranking, as well, Frankfurt holds one of the top positions and ranks fourth - behind Hamburg, Berlin, and Munich - in terms of the GDP share in Germany.

Unique economic structure: financial sector, logistics, and the trade fair

Decisive for the economic strength of the region of southern Hesse and Frankfurt is the special sector mix: a financial centre, an international airport, and a renowned fair are concentrated in a single city and make it unique in Germany.

The upswing continues

Industry is the driving force in the current upswing, as previously in the downturn. However, since industry has a below-average share in Hesse, the growth rate in 2010 should be slightly below the average of 3.0 %. In 2011 the service providers will cushion the economic slowdown in Hesse, as a result of which we can at least expect average growth of 1.6 %.

Only slight job growth over the medium term

In spite of the serious recession, Frankfurt has not experienced a noticeable decline in employment. Because of an overall flatter growth trend and the continued personnel reductions at financial service providers, only a slight increase in jobs can be expected over the medium term. From that one can deduce for the coming five years a growth in office employment in the city of at least 2 %. That amounts to about 6,000 additional office jobs.

Bottom formation in the Frankfurt office market

In the current year the Frankfurt office market will be still burdened by a weak demand for space and higher completions. In 2011 turnover in the rental market should continue to rise. With a markedly lower volume of completions, prime rents could rise slightly, though a reduction of the high vacancy rate is not in sight.

No noticeable invigoration of new construction activity

For the vacancy rate not to continue to rise over the medium term from the current level presupposes, on the one hand, a low activity of new construction and thus continued careful operating by investors and financiers; on the other hand, the high demands on quality by those using Frankfurt office space, in particular, requires extensive construction work on the existing stock. On the basis of our employment forecast, the demand for office space in Frankfurt will grow only moderately by 2015 at up to 200,000 m².

Too many city development areas at the same time?

Central inner city locations continue to have good prospects. The airport, too, will become more important as an office location in the future. All in all, there are in Frankfurt a number of urban development projects in the planning stage that call for a more or less extensive use of office space. Every one of these projects offers the city excellent development opportunities. From the perspective of the office market, however, the simultaneous realization of all of these projects seems neither necessary nor desirable.

1 Frankfurt - important beyond its region

Mainhattan - as Frankfurt is also called - is among the most important office locations in Germany. In fact, with its striking skyline the city is unique in Europe. And this even though Frankfurt is neither the capital of the state of Hesse nor the federal capital. However, the metropolis on the Main is characterized by an international flavour that is grounded not only in the fact that it is the headquarters of the European Central Bank, but also in the presence of many banks and companies from around the world.

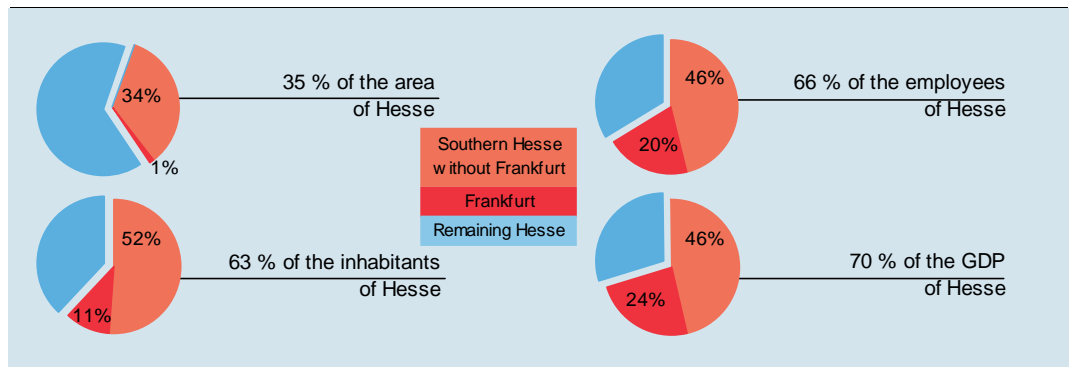
Concentrated economic power in southern Hesse

Economic focal point
in southern Hesse

The hard facts also speak for Frankfurt and its surrounding region, southern Hesse¹. This is not the largest region within Hesse in terms of surface area, accounting for 35 % of the state, but it is home to 63 % of the population. Two-thirds of the employed in Hesse work in the region. Southern Hesse generates 70 % of the state's gross domestic product (GDP), by far the largest share. Such a high concentration of economic strength into one administrative district (*Regierungsbezirk*) cannot be found in any other federal state.

High concentration of economic power in southern Hesse with Frankfurt as the centre

Share of Hesse overall, 2008



Sources: Hessisches Statistisches Landesamt, Helaba Research

Frankfurt: an international economic center

Frankfurt plays an outstanding role in this context. Nearly a quarter of Hesse's economic output is generated in this city, which has a population share of only 11 %. No other city in Germany holds such a prominent place in any other federal state. Frankfurt is also very high up on the ranking list in terms of absolute size of German GDP. It ranks fourth after Hamburg, Berlin, and Munich in terms of its share in Germany's GDP. And this even though, with a population of 685,000, it is markedly smaller than the other three.

Frankfurt compared to selected German cities

	Frankfurt	Munich	Berlin	Hamburg
Inhabitants* (thousands)	685	1,369	3,442	1,778
Area (km ²)	248	310	892	755
Population density (inhabitants per km ²)	2,762	4,416	3,859	2,355
GDP (nominal, billion €, 2008)	54	74	89	87
GDP per capita (thousand €, 2008)	81	56	26	49
Employees (thousands, 2008)	617	954	1,638	1,114

*2010 (last available number)

Sources: Local statistical offices, Helaba Research

¹ Hesse is divided into three administrative districts, whereby the administrative district of Darmstadt is used for southern Hesse.

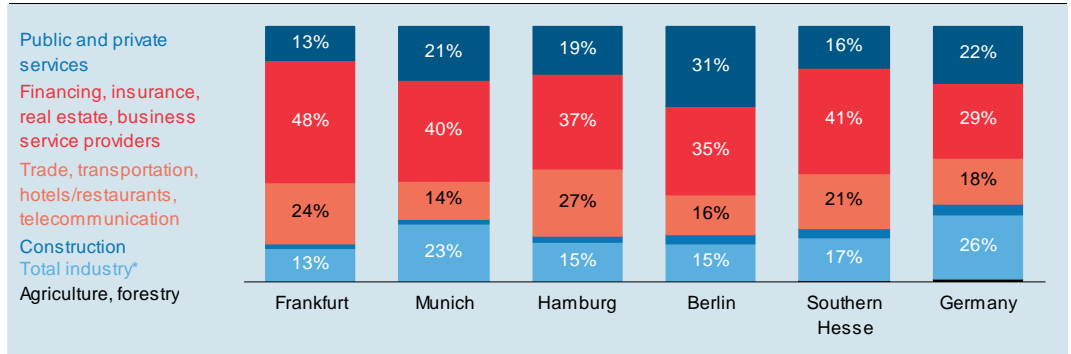
High services ratio
in Frankfurt

Unique economic structure: financial sector, logistics, trade fair

Crucial for the high economic strength of the region of southern Hesse and Frankfurt is the special mix of sectors: no other city in Germany can boast a financial centre, an international airport, and a renowned fair. This is also reflected by the statistical data: 48 % of Frankfurt's and 37 % of Hesse's gross value added are created in the economic sector "financing, insurance, real estate, business service providers." Another quarter of the output in Frankfurt comes from the sector "trade, transportation, hotels/restaurants, telecommunication". This combination of large ratios does not exist in Munich, Hamburg, or Berlin.

Frankfurt with a unique economic structure

Share of gross value added in %, 2008

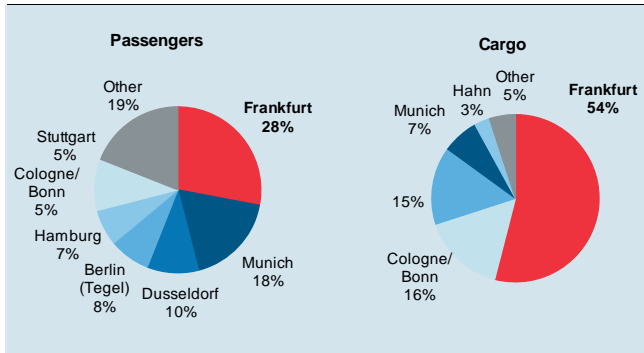


*minus construction sector
Sources: Arbeitskreis VGR der Länder, Helaba Research

Behind this unusual sector mix stands, for one, the financial centre Frankfurt, which constitutes a major factor for the office market. Thus, 220 domestic and foreign banks are headquartered in Frankfurt, which accounts for around 40 % of all financial institutions in Germany that are trans-regionally active (that is, not including savings banks and credit unions). The financial and insurance sector in Frankfurt employs 74,000 workers, that is 15 % of all employees in the city subject to social insurance contributions.

Frankfurt airport of national ...

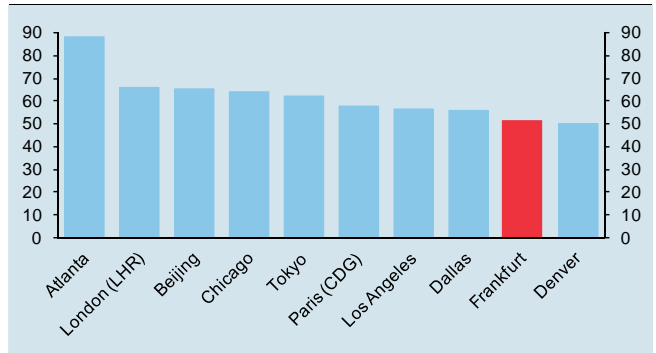
Share of Germany overall in %, 2009



Sources: Statistisches Bundesamt, Helaba Research

... and international importance

Passengers in million, 2009



Sources: ACI, Helaba Research

Second, Frankfurt airport is a central location factor that is used by 28 % of passengers and 54 % of the cargo volume in German air traffic. With that it holds the unchallenged first place within Germany, and after Paris it is the second-largest logistics hub in continental Europe. The fair is another asset that reinforces the international orientation of the region. In terms of visitors and exhibitors, the fair ranks number one in Germany, with international exhibitors once again favouring the location.

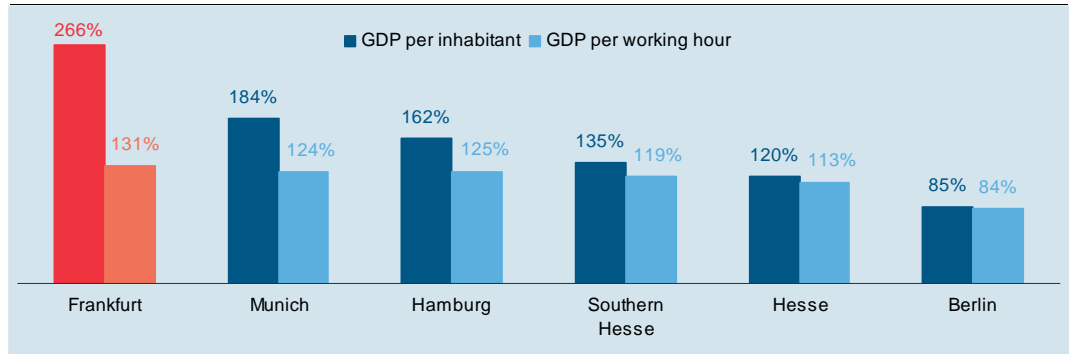
Very high productivity through sector mix

High level of prosperity with above-average productivity

The location advantages of Frankfurt are also clearly evident in the GDP per capita. At 266 % the city is several times above the average for Germany as a whole, and no other large city even comes close to this level.

High economic performance in Frankfurt and its environs

In % of the German average



Sources: Arbeitskreis VGR der Länder, Helaba Research

However, the high per capita figure in Frankfurt also reflects the low population number, which the city compensates for with very large numbers of commuters. Thus, the GDP per working hour is noticeably lower. Still, because of the unique sector mix, productivity is higher than in Munich and Hamburg, and is around one-third above the German average.

2 Economic development in Hesse characterized by services

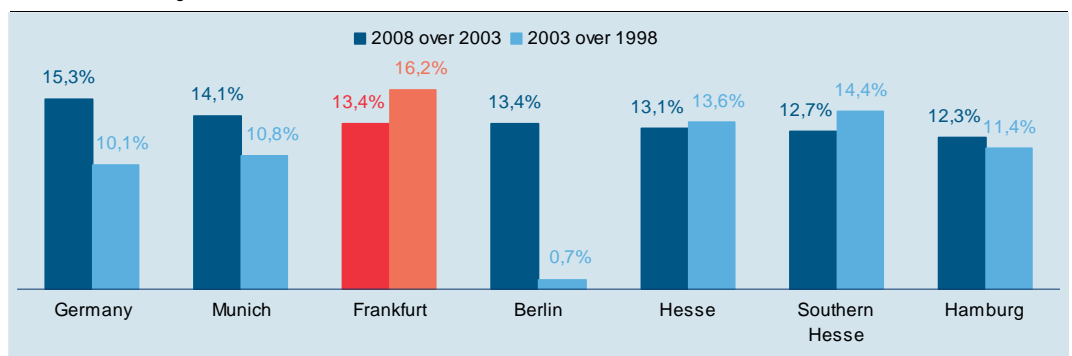
Service providers as stabilizers in the economic crisis

Service providers influence the economic cycle

The statistical state offices disclose economic growth at the level of the administrative districts and the counties (*Landkreise*) only on a nominal basis. According to this calculation, the Hessian economy grew in 2008 by around 13 % over 2003, which was below the average of 15 % for Germany as a whole. By contrast, in the previous economic cycle, Hesse achieved above-average growth rates.

Below-average dynamic in Hesse during the economic cycle 2003-2008

Nominal GDP, change in %



Sources: Arbeitskreis VGR der Länder, Helaba Research

Even more pronounced is the development in southern Hesse and Frankfurt. The region with the strong orientation towards service providers was able to participate only to a limited extent in the industry-driven upswing between 2003 and 2008, and the growth rate remained under that for Germany as a whole - as was the case also in many other large German cities. Because of the relatively minor importance of industry, the direct growth effects were less palpable for the overall growth in southern Hesse, especially since the Frankfurt airport had reached its capacity limits. Between 1998 and 2003, by contrast, the growth impulses came from the services sectors, as a result of which the city expanded at an above-average rate during this period.

Economic recovery has begun

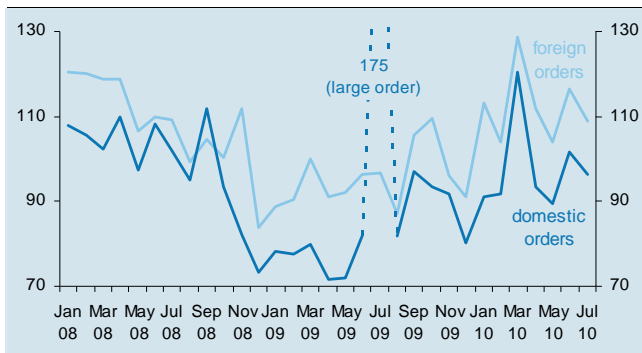
In the economic crisis of 2008/09, service providers probably acted as stabilizers, since the deepest slump occurred in industry. This is also evident from the rate at which the Hessian economy contracted last year: With a -4.3 %, the contraction of the price-adjusted rate was less than the -5.0 % for Germany as a whole. By now, the economic slump has proved to be a canyon and not a broad valley. The cyclical forces are strongest at the beginning of an economic recovery, and in Germany as a whole they have led once again to positive growth rates over the previous quarter since the second quarter of 2009. This development has strengthened further in the first half of 2010.

The economic recovery continues

Incoming orders signal a robust growth surge for Hesse in the current year. They rose by 14 % in the first seven months of 2010, with the invigoration more pronounced in the foreign markets. However, the industrial driving forces in Hesse remained below the national average, since last year a large order distorted the rate of change for domestic demand (in the first half of 2010, Hesse was about equal with Germany). The robust increases create a good basis for the second half of 2010.

Domestic and foreign demand back on growth track

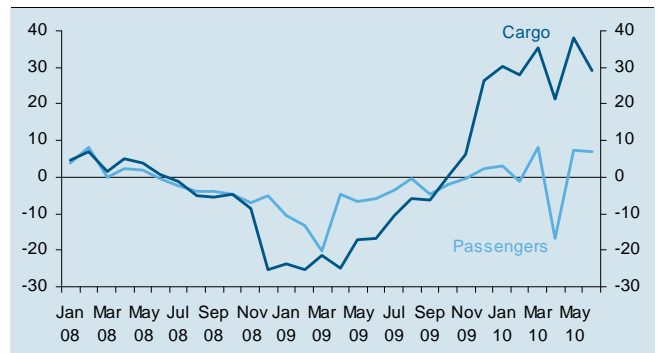
Hesse: orders received, volume index, 2005 = 100



Sources: Hess. Statistisches Landesamt, Helaba Research

Air traffic at the Frankfurt airport on the rise

Change over the previous month, in %



Sources: Statistisches Bundesamt, Helaba Research

Industry and logistics with high growth rates

Air traffic, too, is in an updraft again, and cargo transportation, in particular, is benefiting from this. During the first six months, the volume of cargo that was moved at the Frankfurt airport rose by 31 % (Germany: 26 %). But passenger numbers also recovered by 1.3 %, after having declined by around 5 % in the previous year. Over the medium and long term, the construction of an additional runway (planned completion: October 2011) and of a third terminal will expand the capacities of Frankfurt airport enormously. According to company information, this could boost aircraft movements from currently 83 per hour to 126. With that, a passenger volume of almost 90 million a year would be possible. Given the 50 million passengers last year, this would constitute gigantic growth. The Frankfurt airport, as a real estate location, should benefit from this.

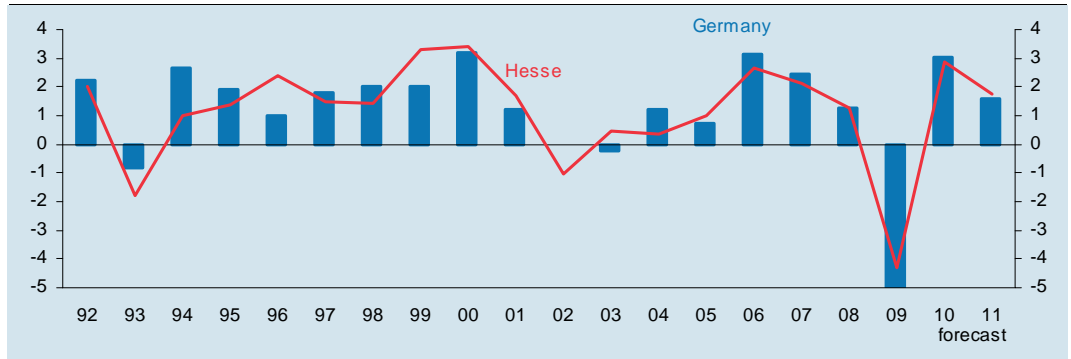
The banking sector, another important sector for Frankfurt, is beginning to stabilize. This will initially show itself more in the business development of the financial institutions. Positive employment effects, however, should not be expected from this over the medium term (see p. 12).

GDP growth in Germany
2010: 3 % and
2011: 1.6 %

In the current upswing, as during the downturn before, industry remains the driving force. Exports are expanding robustly and the investment cycle in Germany is under way. Even private consumer spending is recovering. However, the cyclical forces in industry will weaken in the second half of 2010, since the stimulus programs around the world are slowly expiring. Overall, however, economic growth of 3 % should be possible in Germany in 2010. The process of normalization in the global economy will continue, as a result of which the growth rate in Germany should weaken to 1.6 % (not adjusted for working days) in 2011.

German and Hessian economies on the upswing again

Real GDP, change over previous year in %



Sources: Arbeitskreis VGR der Länder, Helaba Research

Hesse can hold its
own in growth

Since industry has a below-average share of the economy in Hesse, the growth rate in 2010 is likely to be slightly below the expansion of the German economy overall. In 2011 the service providers will cushion the economic slowdown in Hesse, as a result of which we expect at least average growth. Because of their large service sectors, this is especially true for southern Hesse and Frankfurt, which means that, in spite of the city's high starting level, above-average growth rates are expected in the coming year.

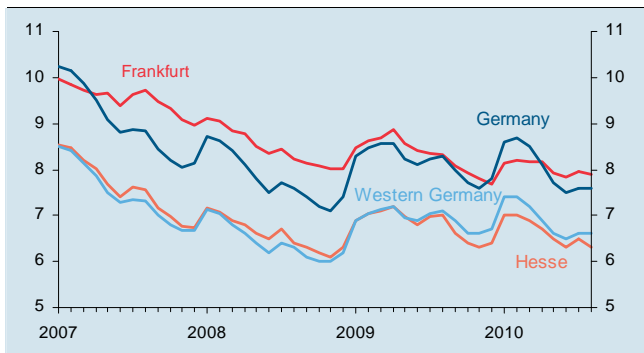
3 Employment at a high level

Slump in labour market
did not happen

In spite of the serious recession last year, Germany has not experienced a noticeable decline in employment. The unemployment rate barely moved up and stood at 8.2 %, after 7.8 % in 2008. By now unemployment is actually dropping again. In August 2010 the national rate was 7.6 % and the rate in Hesse 6.3 %, which was noticeably below the rates last year, 8.3 % and 7.0 %, respectively.

Unemployment rates dropping again

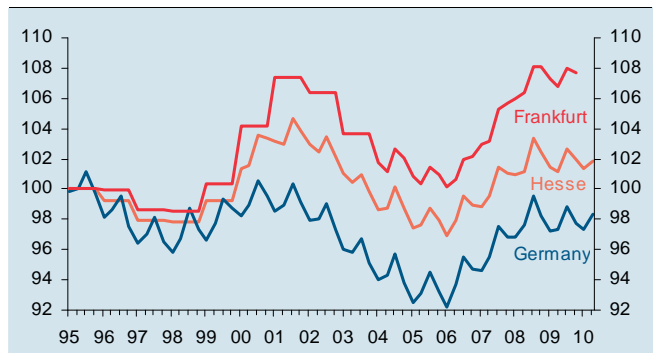
Unemployed in % of labour force



Sources: Bundesagentur für Arbeit, Helaba Research

Employment number in Frankfurt barely declined

Employees subject to social security contribution, Index 1995 = 100



Sources: Bundesagentur für Arbeit, Helaba Research

Frankfurt labour market defies the crisis

As a city, Frankfurt has a fundamentally higher unemployment rate of 7.9 %. But even here improvement in the labour market is evident compared to August 2009, when unemployment stood at 8.3 %. So far the city has not experienced a noticeable decline in the employment figure. According to the most recent available data, the city had nearly 493,700 employees subject to social security contribution at the end of 2009, which was down by only 0.4 % from the previous year. During the last downturn in the Frankfurt labour market from 2002 to 2005, employment in the Main metropolis declined by around 32,000. However, this had been preceded in the years before by a more robust expansion of jobs (1999-2001: +40,700, compared to around +29,000 in 2006-2009). The fact that there was no noticeable decline in jobs during the deepest recession since the existence of the Federal Republic now limits on the potential for possible employment growth in the current upswing.

Only a minor rise in office employment in the future

Demographic trend less of a problem in Frankfurt

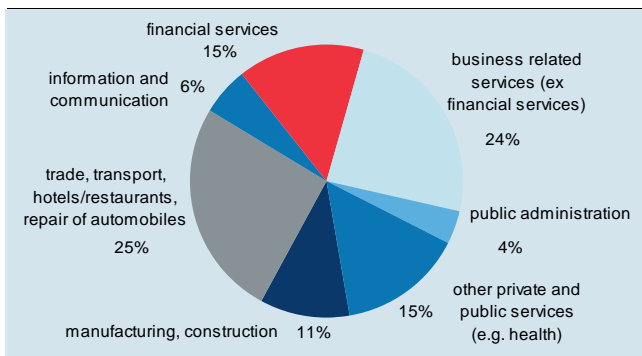
In the coming years, the development of employment in Germany will be characterized increasingly by the decline in the employment potential resulting from demographic trends. As a result, we will see declining employment numbers in many parts of the country. However, the Rhein-Main conurbation should be able to largely escape that trend, thanks to its high attractiveness for domestic and foreign workers. Still, in the period up to 2015, the demographic trend will at least constrain job growth also in the Rhein-Main region.

Over the medium term, there are countervailing sectoral trends in the Frankfurt labour market. The decline in employment in the manufacturing sector should continue in the coming years, even if at a slower pace. The employment level should remain intact in commerce and hotels/restaurants, while job growth is expected in the transportation sector.

Further noticeable growth should be expected also in the other private and public services, which include dynamic growth areas like health or education. However, because a relatively small share of those will be office jobs, hardly any impulses for the office market will emanate from that.

Employment structure in Frankfurt: not only bankers

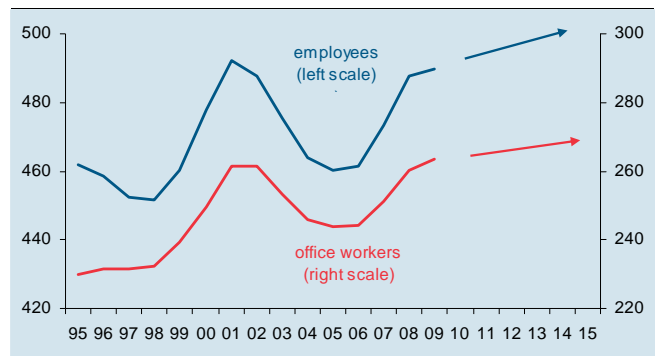
Employees subject to social security contribution at the end of 2009, in %



Sources: Federal Employment Agency, Helaba Research

Only slight rise in office employment

Employees subject to social security contribution, in thousands



Sources: Feri, Helaba Research

Different developments are apparent over the next few years in those sectors of the Frankfurt economy that are relevant to the office market. Thus, the job cuts among financial service providers should continue. In public administration, as well, we see no leeway for additional jobs over the medium term because of the pressures towards consolidation. With that, the other business-related services take on the decisive role as the motor of growth in office employment. They currently account for about one quarter of all employees in Frankfurt. This includes especially business, legal, and tax consulting, as well as auditing and advertising.

Banks continue job cutting

Banks make further job cuts

The financial services and insurance providers that characterize the banking centre employed most recently 15 % of all workers. From the height at the end of 2008 until today, nearly 3 % of jobs were cut here, primarily as a result of the worst financial crisis of the post-war period.² The job losses are contained by the ongoing concentration within Germany on Frankfurt as the leading financial centre, and by the stable development at many foreign banks. However, this should not deceive us as to the excess capacities in terms of personnel at some domestic banks, where the adjustment process will take some time yet because of employment guarantees. About half of the personnel reduction in the sector is likely to have occurred so far, and it should continue at least until 2012 before stabilization takes place. Taking into account the upcoming move of the Deutsche Börse to Eschborn, the number of employees subject to social security contribution in the financial sector in Frankfurt should be about 3,000 lower in 2015 than it is today.

6,000 additional office jobs by 2015

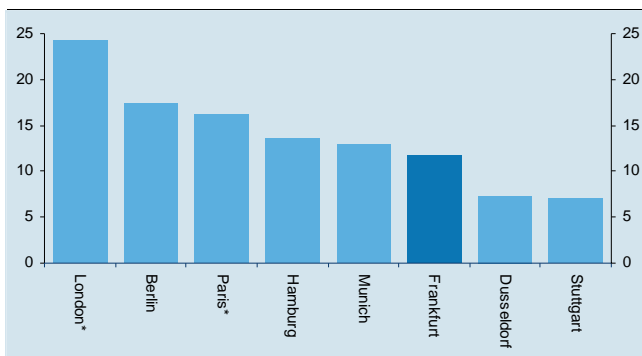
The countervailing employment trends in the various sectors and an overall flatter growth trend allow only a slight expansion in jobs in Frankfurt city over the medium term. By 2015, the number of employees subject to social security contribution could increase to around 502,000. Of those, a solid 54 % will be office workers. Taking into account additional office jobs that are not subject to social security contribution, we can deduce for the coming years a growth in office employment of at least 2 % over 2010. That is tantamount to about 6,000 additional office jobs.

4 Frankfurt office market forms a bottom

The Frankfurt office market³ was not able to escape the financial and economic crisis. Following the rise in the boom years 2006-2008, office rents came under pressure. With a noticeably declining demand for space and a rising volume of new completions, the vacancy rate - starting from an already high level - rose. However, stabilization seems on the horizon by the end of 2010, which means that the office market in the financial metropolis will presumably be in better shape in the coming year.

Internationally and nationally only mid-size

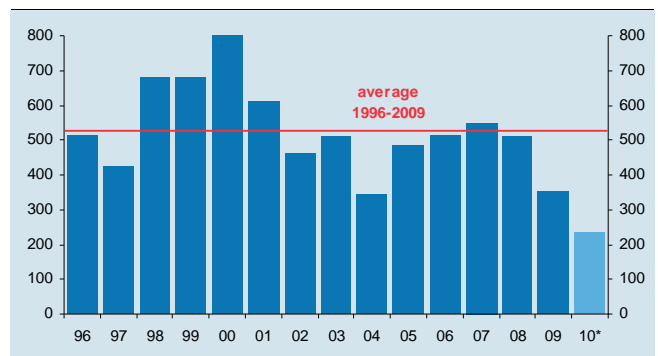
Office space in million m²



* London und Paris: only downtown area
Sources: Feri, Helaba Research

Rental volume Frankfurt office market*

In thousand m²



* Include owner-occupiers, with Eschborn and Kaiserlei, 2010: first half of year
Sources: GIF, Helaba Research

² On this see also our Financial Center Focus “Moderate job cuts at Frankfurt’s banks” of May 25, 2010.

³ In what follows we use the conventional definition of the Frankfurt office market, which comprises, in addition to the down town office districts, also Eschborn and Kaiserlei (Offenbach).

Anaemic demand and increasing completions weigh on the market

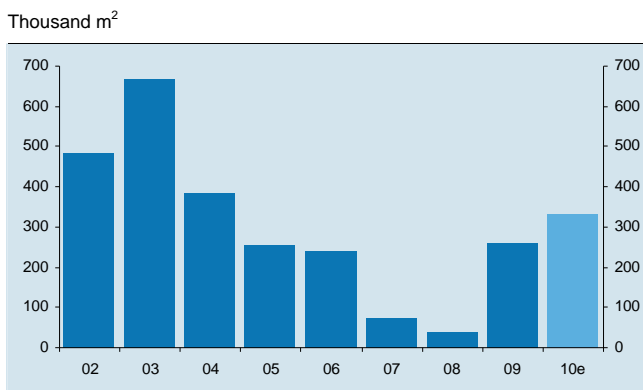
Volume of leased space at low level

At around 350,000 m² in 2009, the rental turnover in the Frankfurt office market had dropped to its lowest level since 2004. Although the contracts reported for the first half of 2010 point to a somewhat better overall performance in the current year, nearly half of the approximately 230,000 m² in the first six months was due solely to the new building of the European Central Bank, which already made its way into the statistics, even though it is not scheduled to be completed until the end of 2013. In general, an analysis of the Frankfurt office market must take into account that by international and even German standards, we are dealing with an office market - with total office space of 11.8 million m² - that is only medium sized (however, in terms of office space per capita, the city ranks at the top internationally). The result is that quarterly or half-year figures can be strongly distorted by large, single transactions. In spite of the ongoing recovery, the rental performance this year should remain below 400,000 m² and thus once again miss the long-term average of more than 500,000 m².

After-effects of the economic crisis

It is largely thanks to the quick and robust economic recovery that the slump in the demand for space in the Frankfurt office market was not even more pronounced. Especially the robust labour market helped to keep the demand for space from plunging even more last year. Thus, on the one hand there have been few reductions in space. On the other hand, however, in what continues to be an uncertain economic climate, businesses continue to be very restrained in making new rentals. More often we are likely to see extensions of leases at more favourable conditions. Moreover, we know from experience that the rental market reacts with a time lag to the overall state of the economy. It can therefore not be ruled out that individual businesses will yet reduce their need for space as their leases expire. Against the backdrop an increasing exchange of space, the need for additional office space should remain low in 2011. All in all, we expect for the coming year an only moderately increasing turnover in the Frankfurt rental market.

Completions have risen from a low level*



* Including Eschborn and Kaiserlei
Sources: GIF, Helaba Research

Few large completions in sight

Selected new construction projects and complete renovations* in Frankfurt

year	project	location	office space
2009	Neues Ordnungsamt	Gallus quarter	26,000 m ²
	Palais Quartier	City	38,000 m ²
2009/10	Opera Tower	City/Westend	63,000 m ²
2010	Neue Börse	Eschborn	53,000 m ²
	Baufeld Nord 1, BNP	Europaviertel	23,000 m ²
	Deutsche Bank towers*	Banking district	102,000 m ²
2010/11	Squaire (Airrail Center)	Airport	93,000 m ²
	Tower 185	Fair district	90,000 m ²
2011	Silver Tower*	Station district	63,000 m ²
2013	EZB	Ostend	110,000 m ²

Sources: Press reports, information from companies and brokers, OFB Projektentwicklung, Helaba Research

High volume of new completions in 2010, noticeable decline 2011

As recently as 2007/2008, very low completions led to a slight decline in the vacancy rate in the Frankfurt office market. But as early as 2009, in the middle of the financial and economic crisis, the volume of completions rose markedly. The high in the current cycle of new construction should be reached in 2010 with a volume of over 300,000 m². Compared to the previous year this would be yet another rise by nearly a third. However, it would be well behind the new construction activity during the last boom at the beginning of the millennium. The largest recent completions include the Opera Tower and the Palais Quartier. In the current year, a marked increase in office space comes chiefly from the partial completion of the Squaire at the Frankfurt airport, the Neue Börse in Eschborn, and the renovation of the Deutsche Bank twin towers. In addition, by the end of the year the first space in the Tower 185 will be ready for occupancy, the rest of the space in 2011. In addition to the conclusion of the complete renovation of the Silver Tower (formerly the

Dresdner Bank skyscraper) in the railway station district, no larger completions are evident for 2011. With that, the projects launched before the crisis are completed, and with the exception of the ECB, no new large-scale projects have been begun lately. As a result, completions should be noticeably lower in 2011.

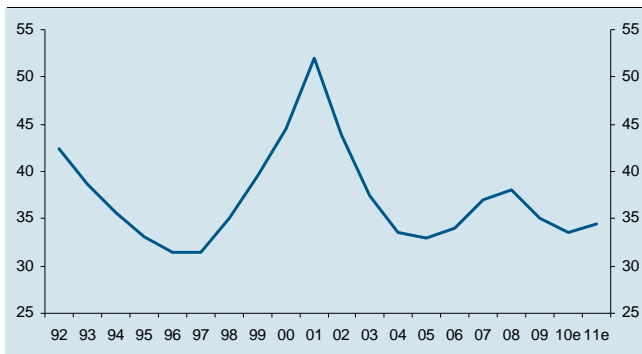
Stabilization of office rents against backdrop of high vacancy

In international terms
favourable and less
volatile

Traditionally, Frankfurt has shown the highest volatility in rents among German office locations. In addition, by far the highest prime rents are achieved in this city. As the German office centre with the strongest international flavour, this market should also be assessed in comparison to its European counterparts. And here a more differentiated picture emerges: with the recent decline in prime rents by a solid ten percent (including incentives ca. 15 %), Frankfurt is at best in the middle of the pack in Europe. Metropolises such as London, Dublin, or Madrid recorded declines that were at times up to 40 %. In contrast to these markets, however, no new highs were reached in Frankfurt during the previous boom - which then led to a correspondingly lower potential for set-backs in the crisis. In fact, with prime rents of 33-34 euro/m², office space is actually favourably priced compared to the other leading European financial centres. Currently prime rents in London's West End reach more than 90 euro/m² and in Paris more than 60 euro/m² - though those markets have much lower office space per employee.

Prime rents have reached the bottom

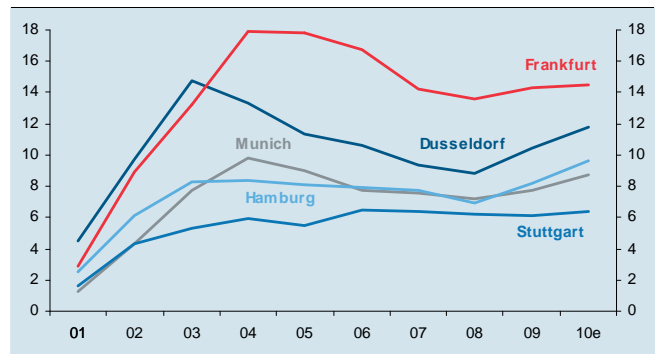
Prime office rent in Frankfurt, in euro/ m²



2010 and 2011: own estimate
Sources: GIF, Feri, Helaba Research

Frankfurt with highest office vacancy

Office vacancy rate, in %



2010: own estimate
Sources: GIF, Helaba Research

Office rents in Frankfurt am Main have been under pressure since the end of 2008 and should have found their bottom by the end of the year. And here one should bear in mind that comprehensive incentives are still in play on new leases. Landlords are currently also willing to make concessions to existing tenants and are trying to extend expiring leases as early as possible to avoid the risk of vacancies. In what remains a difficult environment, landlords should be able to push through at best a slight rise in prime rents in the coming year.

Vacancy remains
at high level

Against the backdrop of weak demand, the growing volume of completions does not allow for a reduction in the office vacancies this year. At the same time, though, no dramatic increase in the vacancy rate was evident over the last two years. At the beginning of the millennium the vacancy rate in Frankfurt hit a low of only 2 %, a level from which it rose to nearly 18 % after the bursting of the New Economy bubble. What is striking is that it did not prove possible during the last boom to significantly reduce the high vacancy in Frankfurt. Compared to the dramatic increase back then, the rise since 2008 by nearly one percentage point to about 14 ½ % does not seem very spectacular. Still, ahead of Düsseldorf, Frankfurt thus has by far the highest vacancy rate among the leading German office centres.

Typical for the current market phase is the effort by individual office tenants to reduce office space to save costs. If a move takes place, smaller spaces are often leased. As a result of this, the overall vacancy in the office market can increase. In the best case, an equally large space is leased and a corresponding space is left behind empty. A noticeable reduction in the vacancy rate is thus unrealistic over the short term. This raises the question whether, with a continuing economic recovery, a reduction in the high vacancy rate in the Frankfurt office market is possible over the medium term, or whether - what happened during the last upswing - the high vacancy rate will consolidate further.

5 Over the medium term restrained prospects in the Frankfurt office market

Additional need over the medium term below 200,000 m²

On the basis of our employment forecast (see p. 12), the demand for office space in Frankfurt will increase only moderately in the coming years. In purely mathematical terms, one can calculate from the additional 6,000 office workers by 2015 - depending on one's assumption regarding the average office space per capita - an additional demand of up to 200,000 m².⁴ This would equal no more than two larger, new office towers.

But this is a rather optimistic estimate, since we do not assume a declining office space per capita over time. However, the trend to higher space efficiency points to exactly that. Thus, during a change of space from older into new or renovated office buildings, the average office space per employee is usually reduced. In addition, given a continuing rise over the long term in the share of part-time workers and telecommuters, who only spend occasional days in the office, smaller office spaces can be set aside for them. A decline of merely one square meter of average office space per employee would already - again, in purely mathematical terms - more than compensate for the additional need of the 6,000 new office jobs. However, it cannot be ruled out that with a continuing economic recovery, various companies could once again prefer more generous office space solutions.

No clear invigoration of new construction activity in sight

Completions remain at low level

In spite of extensive plans for new office projects, we do not see in Frankfurt a noticeable rise in new construction activity in the coming years. Hardly any new projects were undertaken since the beginning of the financial crisis; instead, various developments were in fact put on hold or postponed. This leads to a smaller volume of new completions next year and presumably also in 2012. Whether the cycle of new construction will start up from 2013 on, and if so, how strong it will be, is difficult to estimate from the perspective of today. However, the experiences of the most recent financial crisis suggest that the share of speculative projects will initially remain small. We assume that banks will continue to demand a high percentage of pre-leases and a high equity ratio. Under this assumption, one should expect no more than a moderate growing volume of completions in the years ahead.

Particularly high quality demands in Frankfurt

Not least because of the international character of the financial centre, tenants in Frankfurt have especially high demands on the quality and location of office space. Higher quality demands than in other German office markets lead to a more rapid ageing of existing space in Frankfurt and could provide an explanation for the high vacancy rate. At least 40 % of the current office vacancy totalling around 1.7 million m² is considered outdated and thus difficult or impossible to rent out. In most cases, the only way to return these spaces to the office market is a comprehensive renova-

⁴ Calculations on average office space per-capita arrive at quite divergent results, depending on the method, time frame, and timing of the study within the market cycle. 30 m² per capita results in a need for space over the medium term of 180,000 m² for Frankfurt, 33 m² per capita in a need for about 200,000 m².

tion or demolition and rebuilding. However, current examples like the Opera Tower and T185 show that even in a difficult environment, modern and especially larger office spaces in central locations can, in the end, be rented out. The current market phase allows companies to secure for a longer period of time attractive spaces in central locations at now more favourable rents. Even though there is little need for additional office space, the new objects are benefiting from the exchange of space. By contrast, the older spaces that are opening up are causing problems.

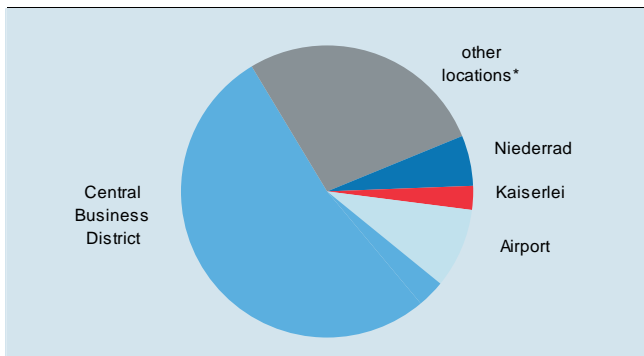
Greater importance of building activity involving existing space

All told, we expect for the coming years a persistent, high vacancy rate in the Frankfurt office market. That the vacancy will not rise from the current level of a good 14 % presupposes, for one, a low new construction activity, and thus continued, cautious action by investors and financial backers. On the other hand, the high quality demands by users, in particular, require a continuous and extensive construction activity involving the existing space. Given the high ratio of older buildings among the vacancies, renovation and modernization activities should henceforth gain in importance over new construction.

If there is an accordingly moderate increase in office space, the chances are good that the prime office rents in Frankfurt will be able to increase noticeably over the next few years - however, the historical high of more than 50 euro/m² from 2001 does not seem attainable over the medium term.

Existing space according to office locations in Frankfurt

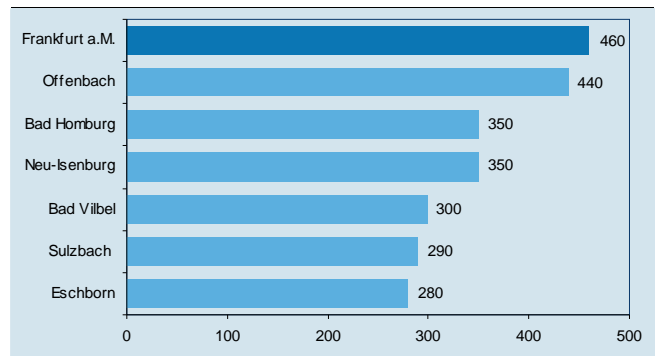
In % of total office space, 2009



Source: OFB Projektentwicklung, Helaba Research
* Office districts West, North, East, and South

Current business tax rates in the region

%



Sources: Cities and communities, Helaba Research

Secondary locations remain problematic

The high quality demands in the Frankfurt office market will be reflected in the future in different developments of the office locations. Central downtown locations have favourable prospects, while the often older office spaces in secondary locations - especially in Niederarrad, but also in the Mertonviertel - are affected disproportionately by vacancies. They stand in tough location competition with neighbouring communities, which score points with cost advantages and good transportation links. For example, the current business tax rate in Eschborn at 280 % is substantially below that in Frankfurt at 460 %.

The vacancy problem in Niederarrad is probably unsolvable over the short term. Approaches like the rededication of office space into living space are costly and are likely to make sense only with certain office buildings. Longer-term prospects for the Mertonviertel could come from the proximity to the new Riedberg quarter and the university campus located there.

The Frankfurt airport should gain in importance over the next few years as an office location. Its position is strengthened by the current expansion of its capacities, which also suggests growing employment in Germany's largest business establishment. Extensive spaces in direct proximity to the airport exist above all in Gateway Gardens (formerly the residential area of the US Air Force),

but also in Zeppelinhof, to satisfy the future demand for offices, especially from airport-affiliated businesses - many of which are today still located in the wider environs of the airport.

Too many city development areas at the same time?

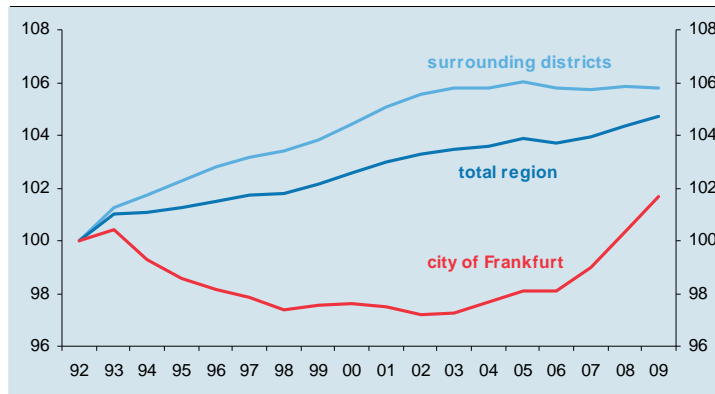
All in all, there are in Frankfurt a number of urban development projects in the planning or construction stages that call for a more or less extensive use of office space. With no claim to completeness, we will mention here the Europaviertel on the area of the former central freight train station, the MainTor on the Degussa area, the former university campus Bockenheim, and Gateway Gardens at the Frankfurt airport.

Great opportunities, but
not everything is feasible

Every one of these projects offers the city excellent development opportunities. From the perspective of the office market, however, the simultaneous realization of all of these projects seems neither necessary nor desirable. The planned office spaces in the Europaviertel, alone, should exceed the need for new office construction in Frankfurt for many years. From today's perspective, one should thus assume that in the end - as happened always in the past - some of the projects will not be realized or only years later because of a lack of investors, financing, or potential tenants.

Population trend: back into the city

Population number, 1992 = 100



Sources: Feri, Statistical Office Hesse, Helaba Research

Residential construction
not to be neglected

The population in the Rhein-Main area has steadily increased over the last twenty years. In spite of declining population numbers in Germany, this should not change within the conurbation in the coming years. However, within the region, the city of Frankfurt was for a long time unable to participate in this population growth. This has changed only over the last few years, thanks to the marked increase in residential construction activity (especially in the new Riedberg quarter). For the development of the city it will continue to be of great importance to mobilize sufficient space for residential construction. Since the next years in Frankfurt will presumably see more demand for additional living space than new office space, the planned projects we have mentioned should be kept as flexible as possible with regard to the property types. ■

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