

## General Indicators

|                 |   |
|-----------------|---|
| Nr. of Licenses | ↓ |
| Interest Rates  | ↑ |
| Market Value    | ↔ |

## Lisbon Indicators (Q1 11)

|   |       |
|---|-------|
| Housing supply (Q1 11 vs. Q1 10)          | ↓     |
| Average asking price (€/sq m)             | 2,500 |
| Average prime asking price – new (€/sq m) | 3,950 |

## Porto Indicators (Q1 11)

|   |       |
|---|-------|
| Housing supply (Q1 11 vs. Q1 10)          | ↔     |
| Average asking price (€/sq m)             | 1,700 |
| Average prime asking price – new (€/sq m) | 3,200 |

## Trends

- The present crisis of sovereign debt is not only affecting the loan conditions of the banks, a mechanism essential for the functioning of the economy and for the development of a sustained growth, but is also considerably reducing the purchasing capacity of the Portuguese, due to the Austerity Measures imposed by the Government. This scenario has led to an anticipated significant decrease in the acquisition of first residences aggravated by the increasingly limited access to bank financing.

## SUMMARY

### • Access to bank financing increasingly limited

The instability in Portuguese public finances is leading to restrictions in the access to bank financing, including diminishing loan to value ratios, increasing bank margins (spread) and the application of rigorous risk and valuation analysis criterions.

### • Lease Market as an effective alternative for the Portuguese

Despite the fact that interest rates stand at historically low levels, the increase in restrictions on bank financing, together with the ever increasing mobility by families, have been contributing to the resurgence of the leasing market, a traditionally secondary market in Portugal. In addition to the fact that the current economic scenario favours this market, the Government is to implement the measures foreseen in the Memorandum of Understanding (MoU) signed with the EU/IMF/CEB, that clearly defends the incentive to lease in detriment to acquisition.

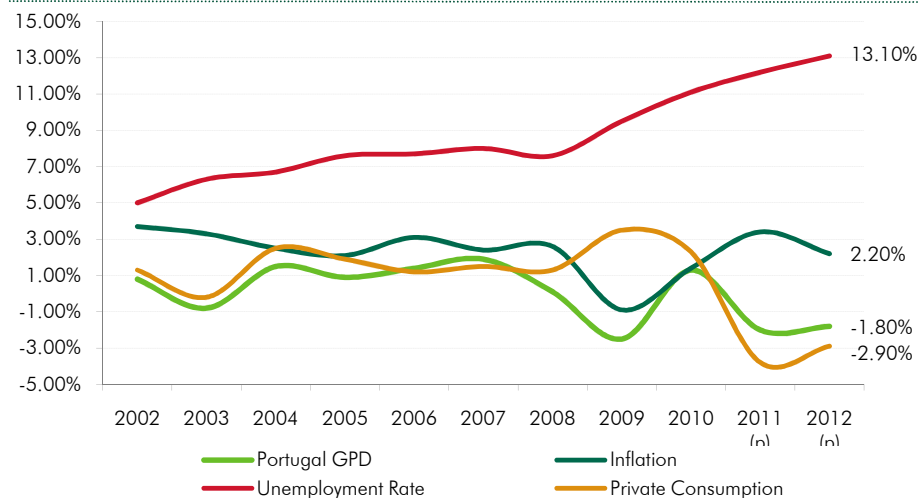
### • Urban Renewal to help contribute towards the recovery of the Portuguese Property Market

The MoU and the program of the new Government promote and incentive urban renewal, considered fundamental for the revitalisation of the cities and for the recovery of the sector. A change in the legislation is thus foreseen, in order to simplify, in general, the processes of such a nature. However, more important than the measures, is the influence that this will have on the change of the lease law and the maximum functioning of the residential lease market.

### • Funds for the Lease of Residential Property ("FIIAH") currently with low level of success

The "FIIAH" were created by the State to assist families with the financial effort aggravated by the increase in mortgage rates, whereby the future owners become tenants, selling their homes to the "FIIAH", with the option to reacquire the property. However, to date these funds have not achieved the success expected, as interest rates have remained relatively low, and in the majority of the situations, the applicable market rent is higher than the monthly mortgage value.

## Key Economic Indicators



Source: Bank of Portugal; IMF; CB Richard Ellis Analysis

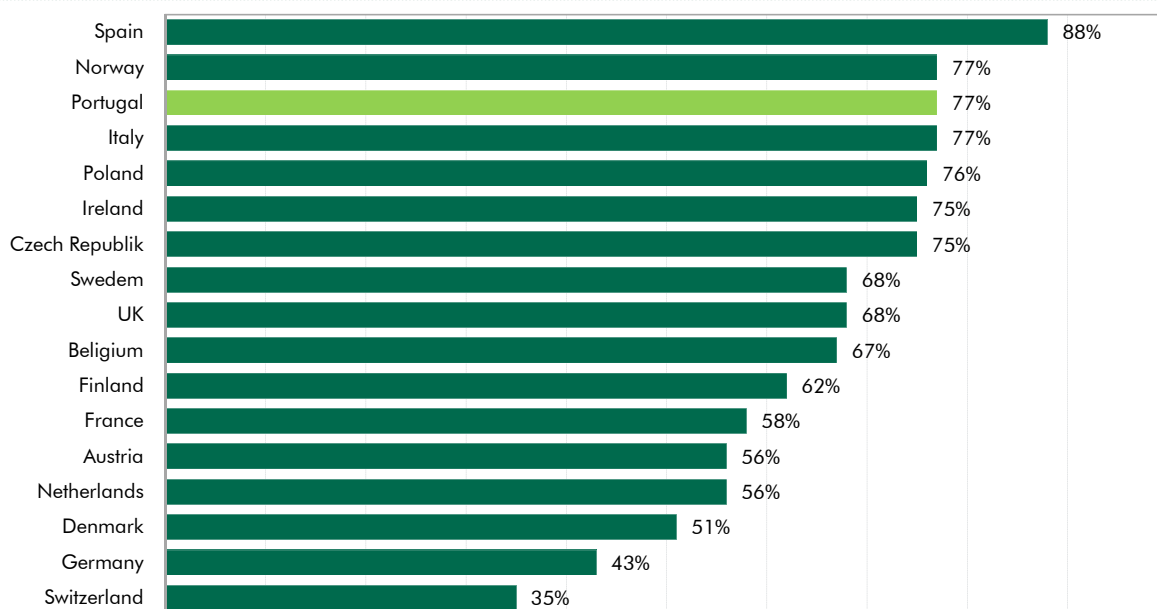
## LEASE MARKET

At the end of the 40's, rents in Lisboa and Porto were frozen. This measure was generalised throughout the rest of the country following the revolution in 1974. The effects resulting from the freeze in rents were extremely serious, as landlords no longer had the right to freely negotiate rental levels. This situation continues to have an impact on the sector, as a number of contracts signed under these terms (old rents with no termination date) are still in force, and, consequently do not allow the market to function freely.

The problem with the lack of supply in the lease sector was resolved by families resorting to mortgage loans and becoming home owners. The systematic reduction in interest rates and the facilitation in access to credit and in the measures allowing for new construction (concentrated essentially in the periphery zones) sustained this strategy, strongly targeting the Portuguese residential market towards home ownership.

Portugal is one of the European countries with the highest percentage of home ownership, comprising 77% of the residential sector. In countries with a high economic capacity, such as Germany, this proportion drops to almost half, revealing a strong dynamics of the lease market.

### Home ownership international, 2009



Source: Euroconstruct; Info-institute; CB Richard Ellis Analysis

The Urban Lease Law has in fact not been favourable to landlords, namely in the eviction of tenants in case of unfulfillment by the latter, and, therefore, in a considerable number of situations this has led landlords to chose not to place buildings on the lease market opting to maintain the building vacant. Consequently, this has resulted in a significantly reduced supply in the number of residential units, whereby demand is currently well in excess of supply.

Notwithstanding, the international crises and the subsequent instability of the Portuguese public finances have forced a drop in the rating, making it difficult for Portuguese banks to obtain financing from international banking institutions. Although interest rates continue to be low, the process allowing for the acquisition of a home has become more difficult due to the criteria used in risk analysis and the increased rigour in the valuation of property, the decrease in the loan to value levels and the increase of bank spreads.

This new paradigm has "resuscitated" the residential market theme, having been a priority issue in the MoU signed between the Portuguese Government and the EU/IMF/CEB. The objectives clearly expressed in the referred document and in Government program presented thereafter include the maximum functioning of this market, considered to be essential, not only to allow for a more dynamic property sector but also to permit the mobility of the families, the urgent reduction in the level of family debt and the revitalisation of the cities through urban renewal.

According to the documents in question, the solution lies in changing the present legislation and taxation in force, as demonstrated below. The changes foreseen in the Lease Law are expected to increase landlord confidence, reducing their risk and consequently the asking rent values, allowing for the expansion in supply, thus permitting a wider access to residential lease by families.

In summary, the residential lease market is expected to undergo exponential growth in the near future, due to (1) the increasing difficulty in access to bank financing and (2) the changes in the legislation and taxes publicised in the MoU. As a result, the number of vacant houses will increase, allowing tenants more margin to negotiate, undoubtedly leading to an adjustment in rents, with a subsequent professionalization of this sector.

## FUNDS FOR THE LEASE OF RESIDENTIAL PROPERTY

The Funds for the Lease of Residential Property ("FIIAH") were created in 2009, at the initiative of the Government, to assist families with difficulties in paying monthly mortgage loans and to create an additional stimulus for the residential sector. These funds represent an important tool for banks, helping to find a solution for mortgage bad debt.

The "FIIAH" allow families with bank mortgages to sell the respective residential property and become tenants of their homes, benefiting from the option to reacquire the property.

However, whilst interest rates remain low and market rents high, there is no advantage for the families to become tenants instead of owners, as the rent payable would probably be significantly higher than the monthly mortgage value. However, due to the current situation where many families have reached the limit of their financial efforts, and with the expected increase in interest rates, this scenario is likely to invert in the short/medium term.

This conjuncture does not represent, for the time being, a significant success for these funds. There are currently only 6 "FIIAH", of which two are owned by Caixa Geral de Depósitos, and one respectively by BES, Caixa de Crédito Agrícola, Banif and Montepio. The properties placed in these funds include, to date, plots of land and other uses other than residential, and not all of the properties have been sold by the future tenants, as the management companies may acquire for these funds properties to be subsequently leased, or may transfer residential units already included in the fund portfolio (as is the case of property seized due to mortgage bad debt).

The table below summarises the principal rules for the incorporation and functioning of the "FIIAH".

| "FIIAH" RULES                    |  |
|----------------------------------|--|
| <b>Incorporation</b>             | <ul style="list-style-type: none"> <li>Until 2014, by any public or private entity, including property investment companies</li> <li>After 1 year, asset value <math>\geq</math> 10 M€</li> </ul>  |
| <b>Requisites</b>                | <ul style="list-style-type: none"> <li>75% of the properties to be located in Portugal and destined for first residence.</li> <li>Private; or</li> </ul>   |
| <b>Subscription</b>              | <ul style="list-style-type: none"> <li>Public – minimum of 100 participants, which individual participation may not exceed 20% of the total value of the fund</li> </ul>   |
| <b>Distribution of dividends</b> | <ul style="list-style-type: none"> <li>Annual minimum of 85% of the net results of the fund</li> </ul>   |
| <b>Sales Value</b>               | <ul style="list-style-type: none"> <li>Market Value (<math>\leq</math> valuation value)</li> </ul>   |
| <b>Rent Value</b>                | <ul style="list-style-type: none"> <li>Market value and subject to annual indexation</li> </ul>  |
| <b>Reacquisition Value</b>       | <ul style="list-style-type: none"> <li>Value of sale to fund, subject to annual indexation according to the IPC</li> <li>Should the reacquisition occur within 2 years after the property is included in the fund, the cost resulting from the sale, valuation, assignment and register will be added to the sales value.</li> </ul> |
| <b>Reacquisition Option</b>      | <ul style="list-style-type: none"> <li>Until 2020 and at any given moment, with a prior notice of 90 days</li> </ul>   |

Source: Applicable legislation ; CB Richard Ellis Analysis

We point out the main fiscal advantages for this type of funds, both for the owner/tenant, as well as for the fund:

| Fiscal Advantages of FIIAH |  |
|----------------------------|--|
| <b>Fund/ Participants</b>  | <ul style="list-style-type: none"> <li>Exempt from Corporate and Income Tax for income obtained by the "FIIAH" and participation units</li> <li>Exempt from Annual Municipal Tax and Property Transfer Tax and Stamp Duty</li> <li>Exempt from the payment of supervision tax</li> </ul>   |
| <b>Owner/ Tenant</b>       | <ul style="list-style-type: none"> <li>Exempt from Income Tax on the capital gains resulting from the sale of the property (payable should the lease contract be terminated and the reacquisition option not exercised)</li> <li>Income Tax deduction on the rents paid.</li> <li>Exempt from Property Transfer Tax and Stamp Duty on the reacquisition</li> </ul> |

Source: Legislação aplicável; CB Richard Ellis Analysis

## IMPACT OF THE MEMORANDUM OF UNDERSTANDING ON THE PROPERTY MARKET

The program presented by the Government guarantees the careful and rigorous fulfilment of the Memorandum of Understanding signed between the Portuguese State and the EU/IMF/CEB. The execution of this MoU is absolutely essential in order to regain the confidence of international investors and, consequently, the recovery of external credit, and increased growth and employment.

We therefore summarise below the conclusions reached from the analysis of the document, in parallel with the Government program, in relation to the property market in general, and particularly to the residential sector, and point out the 4 principal targets:

- Improve households' access to housing;
- Foster labour mobility;
- Improve the quality of housing and make better use of the housing stock;
- Reduce the incentives for households to build up debt.

In order to fulfil these objectives, the referred documents foresee changes at 3 levels:

- (1) Revitalise the residential lease market;
- (2) Incentivise urban renewal; and
- (3) Modify property taxation.

### Revitalise the lease market

The Government proposes to undertake a series of measures in the short term, in order to revise the contractual terms and create conditions to increase the confidence of the landlords, to ensure balanced rights and obligations of landlords and tenants, considering the socially vulnerable. We would like to draw attention to the following changes foreseen in the New Urban Lease Law:

- Provide for an extrajudicial eviction procedure for breach of contract;
- Allow for the convergence of rents to more updated values through mechanisms for the control and increase in rent (dependant on the residential conditions of the property);
- Consider the termination of binding contracts within a maximum period of 15 years;
- Limit the possibility of transmitting the contract to first degree relatives;
- Reinforce the contractual freedom between the parties.

### Incentivise property rehabilitation

Urban Renewal is not only strategically important for the recovery of the property sector, considered to be essential for the economic growth of the country, but also for the repopulating of the cities that have somewhat been abandoned due to the development of the peripheries resulting from new construction. In order to promote property rehabilitation, the Government is aiming to adapt the legislation to:

- Simplify administrative procedures for renovation works;
- Stimulate the incorporation of Urban Renewal Property Funds;
- Simplify the urban renewal regime, with regards to the delimitation of Urban Rehabilitation Areas and the inclusion of isolated urban renewal processes.

At the same time, the Government is looking to simplify the institutional model for urban planning, which is currently considerably complex.

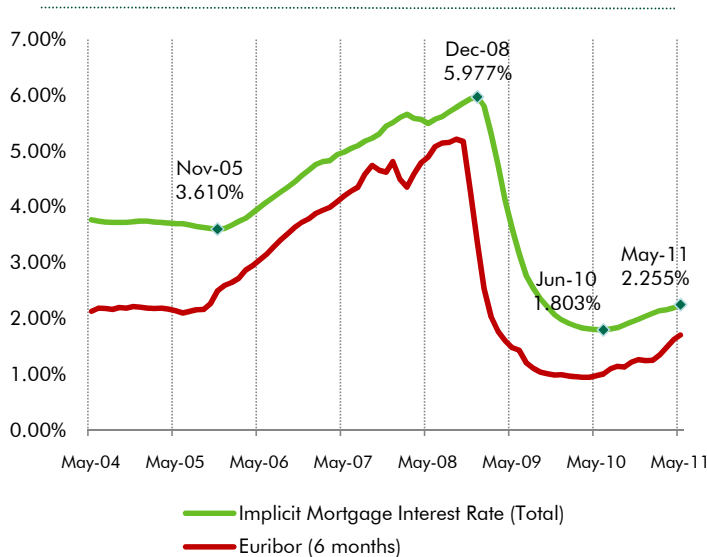
### Increase in property taxation

At this level, the Government foresees changing property taxation so as to boost lease incentives in detriment to the acquisition of residential property, simultaneously increasing State income. This will be achieved by:

- Increasing Annual Municipal Tax ("IMI") income :
  - Ensure that by end 2012 the taxable value of all property is close to the market value. Property valuation should also be updated regularly (every year for commercial real estate and once every three years for residential real estate);
  - Temporary exemptions of "IMI" for owner-occupied dwellings will be considerably reduced and "IMI" of vacant property increased;
- Limit, or even eliminate, income tax deductibility of rents and mortgage interest payments;
- Restructure Property Transfer Tax ("IMT") to increase market liquidity and transparency.

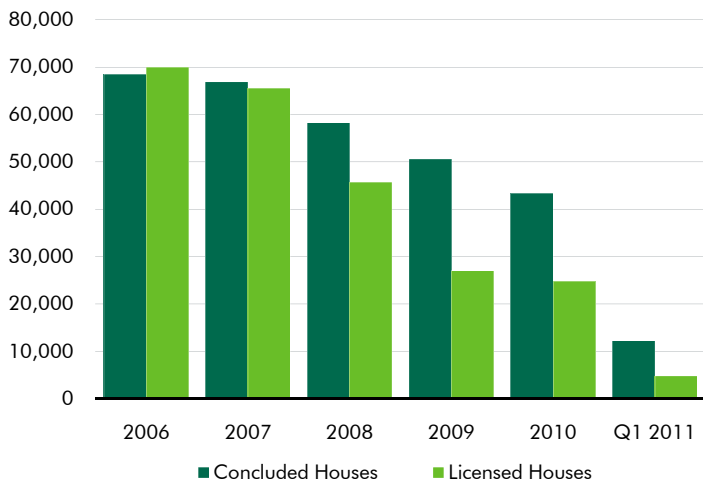
KEY MARKET INDICATORS

Evolution of Implicit Mortgage Interest Rate



Source: INE; CB Richard Ellis Analysis

Evolution of Number of Housing Licenses and Concluded in Portugal



Source: INE; CB Richard Ellis Analysis

Confidencial Imobiliário Index



Source: Confidencial Imobiliário; CB Richard Ellis Analysis

- According to recent census data, between 2001 and 2011 the number of households in Portugal increased by 11.6%, to 4,079,577. This boost is due to, on the one hand, the increase in population, with a variation of 1.93% during this same period, but on the other mainly as a result of the reduction in the average of number of family members, that reduced from 2.8 in 2001 to 2.6 individuals in 2011.
- The number of lodgings stated in the 2011 census stood at 5,879,845, which is equivalent to an increase of 16.3% when compared to 2001. Currently the number of dwellings is 1.4 times superior to that of the quantity of families, clearly reflecting an excess of residential units in Portugal.
- The implicit mortgage interest rate, applicable to all contracts in force reached its lowest value of the last decade in June 2010, standing at 1.803%. Since then rates have begun to increase gradually. In May 2011, INE registered a rate of 2,255% in mortgage financing. However, if we analyse the more recent contracts, this value is incremented by 3.146% and 3.321% for contracts signed in the last six and three months respectively, reflecting a significant influence in the increase of bank spreads.
- The construction sector has been considerably affected by the unstable economic scenario, with a continued decrease in the number of licenses granted for housing construction.
- During the first quarter of 2011 around 4,800 residential units were licensed, which when compared to 2010, represents a drop in the region of 25%. In the last 5 years, the number of units licensed reflected an annual average drop of over 20%.
- The residential dwellings completed accompanied the same downward trend as that of the licensed units, representing an average annual negative variation of 11%, in the past 5 years.
- An analysis of the *Confidencial Imobiliário Index* (ICI) which measures the evolution of the value of residential supply over a period of time, shows that despite all the turbulence and instability which has occurred, property in Portugal has not suffered an accentuated drop, but has been subject to slight adjustments. The average year-on-year growth of the ICI, reflects this scenario and despite the slowing down registered since the beginning of 2011, always shows positive growth.
- However, we refer that used stock reflects a reduction in prices and a greater flexibility by landlords in closing transactions.

## LISBON RESIDENTIAL MARKET

The Lisbon Residential Market can be subdivided into 10 well defined zones, as illustrated on the map on the last page of this report, namely: Baixa/Castelo, Chiado, Santos/São Paulo, Lapa, Campo de Ourique/Amoreiras, Avenidas Novas, Western Zone (Alcântara, Ajuda, Belém and Restelo), Eastern Zone (including Parque das Nações), Campolide/Benfica and Lumiar.

### Supply

During the 1<sup>st</sup> quarter of 2011, according to data available from Confidencial Imobiliário /Lardocelar.com, the residential supply available in the Lisbon Metropolitan Area (LMA) was of around 128,000 dwellings (new and used). When compared to the same period in 2010, this reflects a decrease in supply of approximately 3.7%. The councils of Lisbon, Sintra and Cascais are clearly dominant in terms of total stock available in the LMA, representing a share of around 15%, 12% and 11%, respectively.

In the council of Lisbon, the supply of dwellings during the first quarter of the year stood close to 19,300 units, a decrease of approximately 3.4% when compared to the same period in 2010.

Around 31% of the houses comprising the supply in the capital city are new, and are mainly concentrated in the areas of Avenidas Novas, Eastern Zone, and Campolide/ Benfica, with quotas of 21%, 16% and 15%, respectively. On the opposite end stand the areas of Santos, Lapa, Chiado and Campo de Ourique/ Amoreiras, where each zone registers around 3% of the total stock.

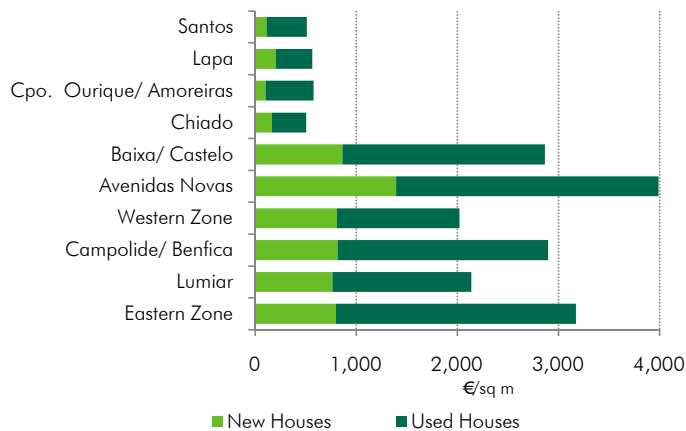
### Residential Prices

While analysing the evolution of asking prices in the city of Lisbon, we conclude that there is a valorisation trend over the years. However, there has been a frank deceleration during 2010, and the 1<sup>st</sup> quarter of 2011 reflects a slight drop in prices.

In Lisbon, the average asking prices for new houses were in the region of 3,000 €/sq m, while the asking prices for used houses stood at around 2,350 €/sq m. An analysis per zone shows that Lapa registered the highest average asking price, namely circa 3,950 €/sq m for new units. The Eastern Zone registered the lowest values, where the average price for the supply of new products was situated at around 2,450 €/sq m, influenced by the low values at the parishes of Beato and Marvila.

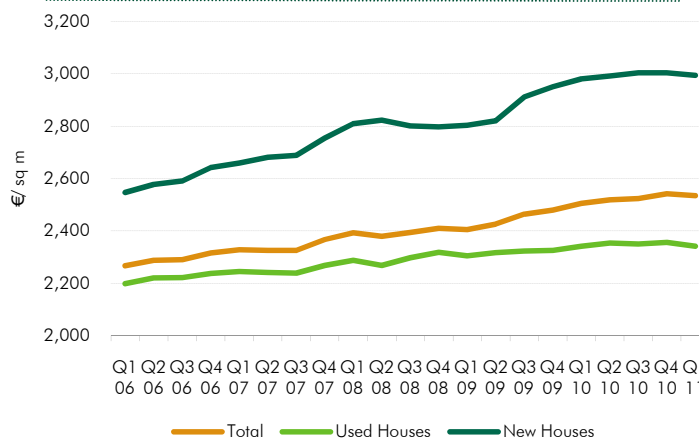
According to the data referent to sales registered and published by the SIR – *Sistema de Informação Residencial* (Residential Information System) 2010 witnessed higher values in the areas of Chiado and Santos, with new units achieving an average value of 3,300 €/sq m.

### New and Used Houses Supply, per Lisbon Zone, Q1 2011



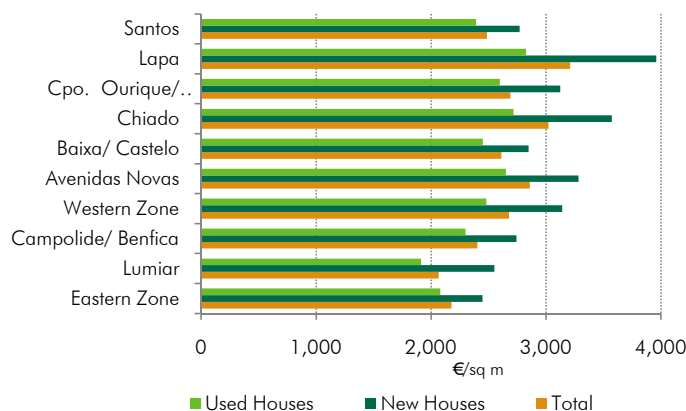
Source: Confidencial imobiliário/ Lardocelar.com; CB Richard Ellis Analysis

### Average Asking Price Evolution in Lisbon



Source: Confidencial imobiliário/ Lardocelar.com; CB Richard Ellis Analysis

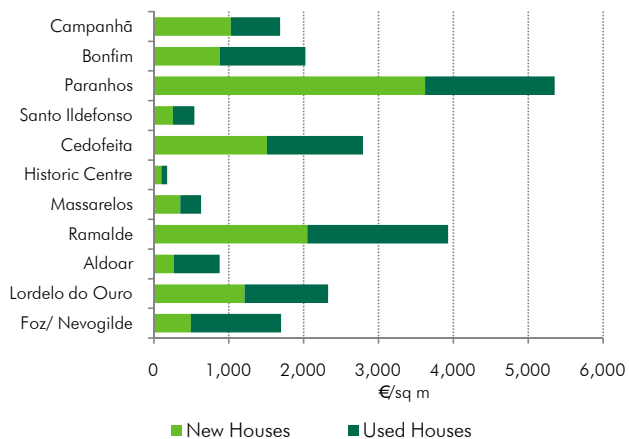
### Average Asking Price per Lisbon Zone, Q1 2011



Source: Confidencial imobiliário/ Lardocelar.com; CB Richard Ellis Analysis

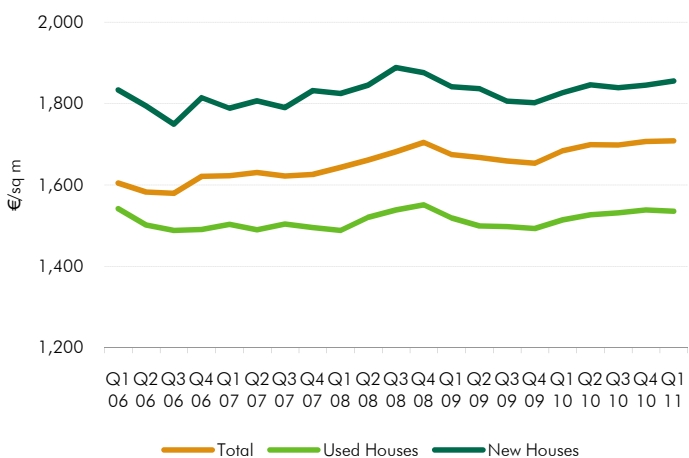
Analysing the values registered in the residential lease market published by Confidencial Imobiliário /Lardocelar.com, we verify that the asking prices in Lisbon reach an average of 11€/sq m/month. In the Baixa/ Castelo, Chiado and Avenidas Novas zones the average asking rents are in excess of 13,5 €/sq m/month.

**New and Used Houses Supply, per Porto Zone, Q1 2011**



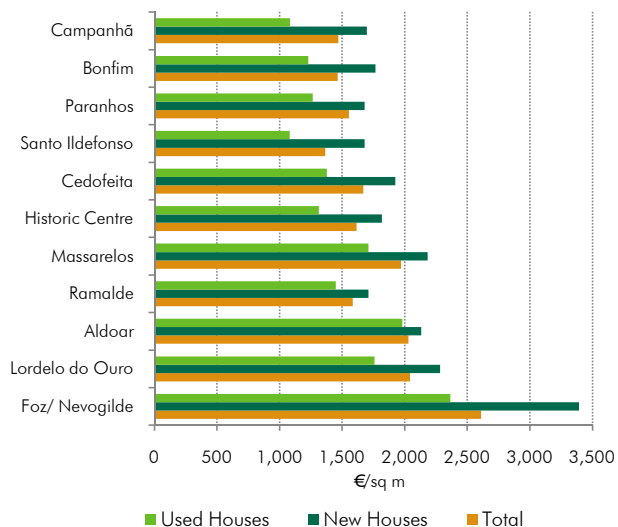
Source: Confidencial imobiliário/ Lardocelar.com; CB Richard Ellis Analysis

**Average Asking Price Evolution in Porto**



Source: Confidencial imobiliário/ Lardocelar.com; CB Richard Ellis Analysis

**Average Asking Price per Porto Zone, Q1 2011**



Source: Confidencial imobiliário/ Lardocelar.com; CB Richard Ellis Analysis

**PORTO RESIDENTIAL MARKET**

The Porto Residential Market is subdivided into 11 well defined zones, as illustrated on the map on the last page of this report, namely: Foz/ Nevogilde, Aldoar, Lordelo do Ouro, Ramalde, Massarelos, Historic Centre, Cedofeita, Santo Ildefonso, Bonfim, Campanhã and Paranhos.

**Supply**

During the 1<sup>st</sup> quarter of 2011, and according to data published by Confidencial Imobiliário/ Lardocelar.com, the residential supply available in the Porto Metropolitan Area (PMA) was of approximately 85,500 dwellings. When compared to the same period in 2010, the level of supply remained almost unchanged. The councils of Porto and Vila Nova de Gaia are clearly dominant in terms of total stock available in the PMA, representing a share of around 26% and 25%, respectively.

The supply of residential dwellings available in the council of Porto stood close to 22,000 units during the first quarter of the year, representing an increase in the region of 7% in comparison to 2010.

Approximately 53% of the available stock in Porto is comprised by new dwellings, and the highest share, which stands at around 31%, is situated in the Paranhos zone. The Historic Centre registers less than 1% of new houses available, but this share is expected to increase in the future, due to the policy to regenerate the city of Porto.

**Residential Prices**

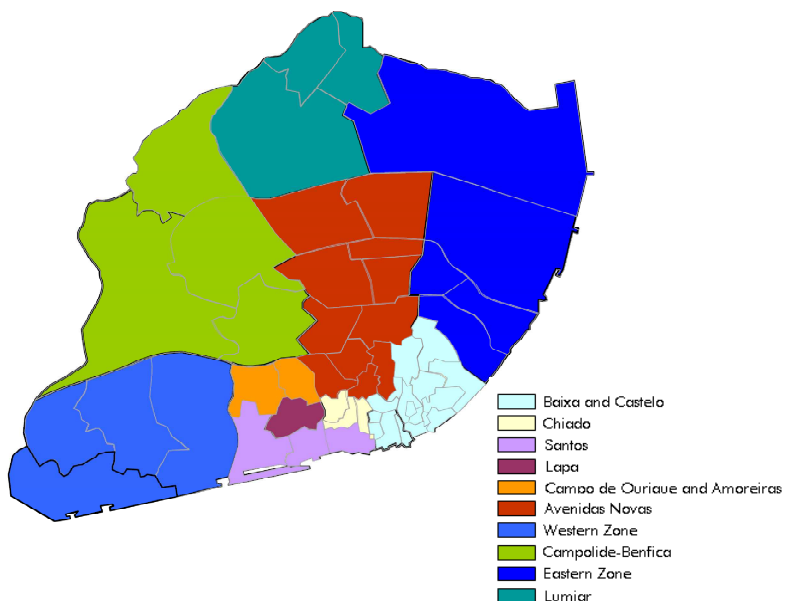
With respect to the evolution of asking prices, the PMA registered an increasing trend over the past years, although this was not as accentuated as in Lisbon. Despite the unstable economic situation, values in Porto continue to increase, and only the used houses reflect a slight decrease in numbers during the first quarter of this year.

In 1<sup>st</sup> quarter of 2011, average asking prices for new houses in the city of Porto stood at around 1,900 €/sq m, and prices for used homes at 1,550 €/sq m. The Foz zone continues to be the most attractive area of the city, with a higher average price for new dwellings, of around 3,200 €/sq m. In Campanhã and Santo Ildefonso, on the other hand, average values for new products stood at 1,700 €/sq m.

Regarding sales indicated during 2010 by the SIR, the highest values were registered in Foz, reaching an average of 3,100 €/sq m.

With regards to the city of Porto lease market, the average values stand at 7.4 €/sq m/month. In the Foz zone, average values are above 9.5 €/sq m/month.

## LISBON MAP



## PORTO MAP



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