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ØRESTAD – SUCCESS OR FAILURE ?

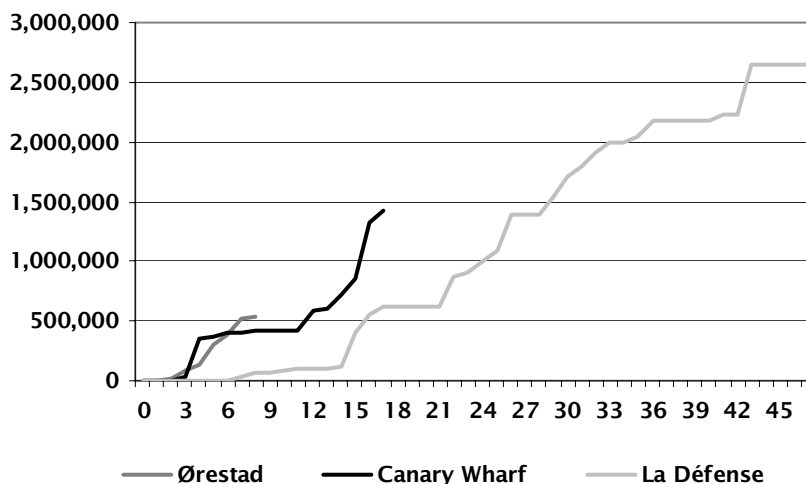
Has Ørestad developed successfully?

Planning for Copenhagen’s new major urban district, Ørestad, was initiated some ten years ago. The area has a potential for up to around 3 million sqm of floor space, of which 500,000 sqm has already been committed, and construction commenced 3 or 4 years ago.

We have analysed the rate of development in Ørestad compared with two other very important new urban districts in major European cities, La Défense in Paris and Canary Wharf in London, where developments were initiated much earlier.

The figure below shows the volume of committed floor space in each of the three districts as a function of the number of years passed since the respective planning phases were completed.

Accumulated committed floor space as a function of the relevant development period



Source: Sadolin & Albæk

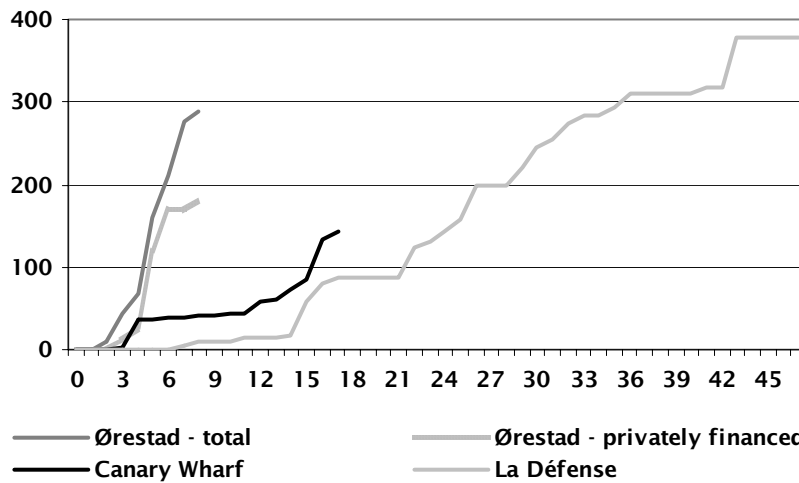
It is important to note that the majority of such projects grow in leaps, as building activity progresses faster during an economic upswing as compared with periods of economic downturn. This applies in particular to Canary Wharf, which is dominated by office developments, whereas a more stable trend is expected in areas combining commercial and residential projects.

Nonetheless, we conclude that the development rate in Ørestad matches that of Canary Wharf, while being significantly higher than what was seen in La Défense. We therefore believe that the

development of Ørestad over the next 10-20 years will render it as successful as Canary Wharf and La Défense – which were both termed failures during their early years of building activity.

Adjusting the figures to reflect that Greater Copenhagen is a much smaller urban area than both London and Paris, the rate of development becomes even more impressive.

Committed floor space per 1,000 capita as a function of the relevant development period



Source: Sadolin & Albæk

Developments in Ørestad not borne exclusively by public-sector projects

So far, public-sector projects represent just under 50% of the floor space in Ørestad. Based on the above figure, we conclude, however, that privately financed urban developments in Ørestad exhibit a quite impressive growth rate taking into account the size of Copenhagen.

THE INVESTMENT PROPERTY MARKET

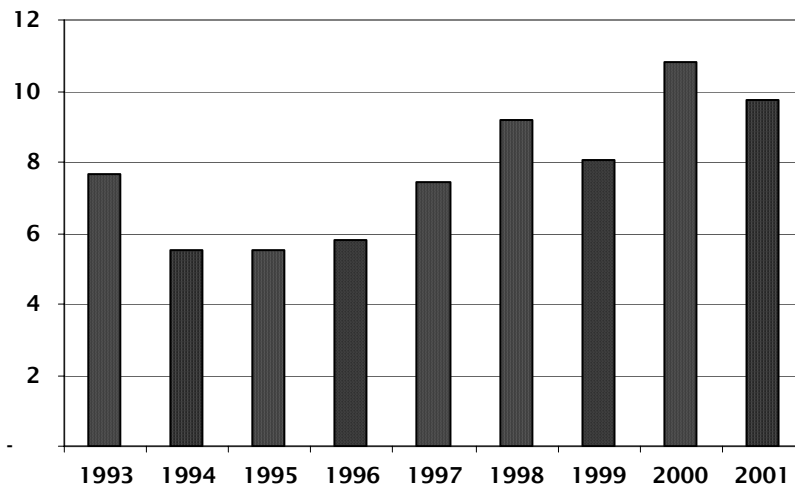
Stable turnover in the commercial property market

Jitters in the financial markets in recent months caused by sluggish economic developments have spurred some uncertainty in the market for investment property, leading to reluctance among a number of investors.

Despite this trend, investment property turnover has been quite good, thanks in part to a few, very significant transactions relating to property or property portfolios and in part to high turnover of small and medium sized urban property to private investors.

The figure below shows turnover of commercial property in Greater Copenhagen from 1993-2001.

Turnover of commercial property (in DKK billion) in Greater Copenhagen



Source: Statistics Denmark

As appears from the figure, turnover from 1998-2001 ranged from DKK 8 billion to DKK 11 billion. Figures for 2002 are not yet available, but we forecast that turnover in 2002 remained at around DKK 10 billion.

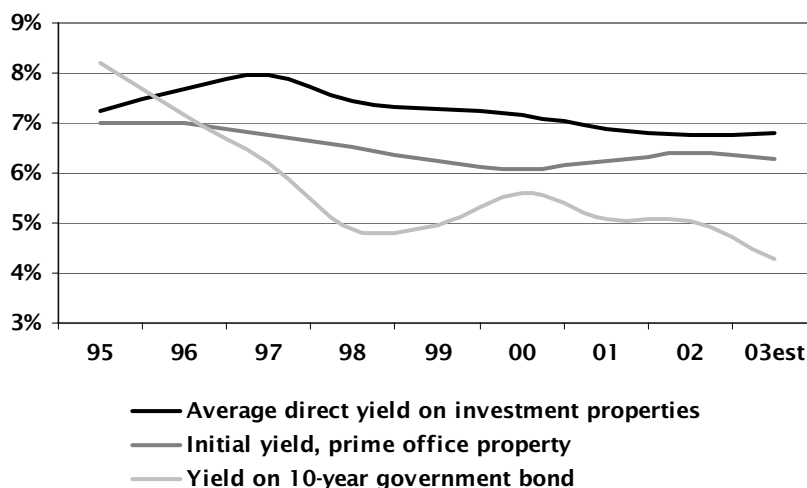
We should add that these figures do not include the total volume of property projects under construction. That figure has generally been some DKK 2 billion higher in recent years.

We would not rule out, though, that turnover in 2003 may prove to be even higher, seeing especially as a number of very large transactions have been carried through this year, including the DKK 1.7 billion sale by *Nordea* of a portfolio of properties to a consortium of institutional investors, the anticipated sale by *Magasin* of the *Illum* high street property on *Strøget* as well as *CGI's* purchase of 50% of the *Field's* shopping centre in *Ørestad*.

Investor interest largely driven by low interest rate levels

In our opinion, investor interest in property is not spurred by expectations of a significant economic recovery in the short term that would lift the market for commercial leases. The incentive to invest in property can rather be traced to the low level of interest rates.

Current return on property and benchmark bond yield to maturity



Source: Sadolin & Albæk

The figure above shows the yield to maturity for 10-year government bonds relative to (1) the average direct yield on investment property in Greater Copenhagen, and (2) the prime yield, the first year's net initial yield on prime office property let on a 10-year interminable lease.

The yield spread, the difference between the prime yield and the yield on 10-year government bonds, is currently more than 200 bp, whereas the direct excess return on an average property portfolio outperforms the bond yield by more than 250 bp.

The direct excess return on property, that is, excess return excluding value adjustments, is at the highest level recorded in recent memory. The decline in interest rates has not resulted in any appreciable drop in investors' required return on property investments.

Declining net initial yields on mixed-use city property

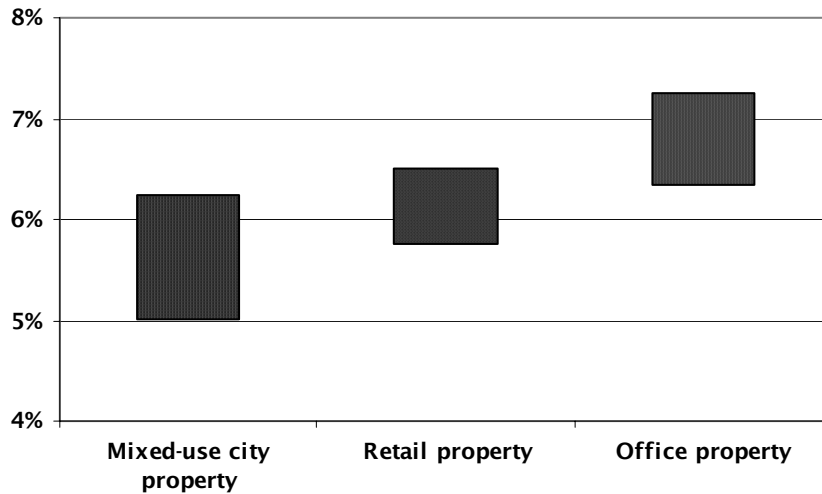
In a market characterised by significant vacancy risk, investors naturally attach considerable importance to the letting probability of a property.

This has increasingly made private investors in particular demand mixed-use city property in an effort to diversify tenant risk through a combination of retail, commercial and residential property.

As a result, initial yield requirements for such property are sub-

stantially lower today than the requirements for “pure” retail and office property without a similar degree of risk diversification.

Current net initial yield requirements for Copenhagen CBD property

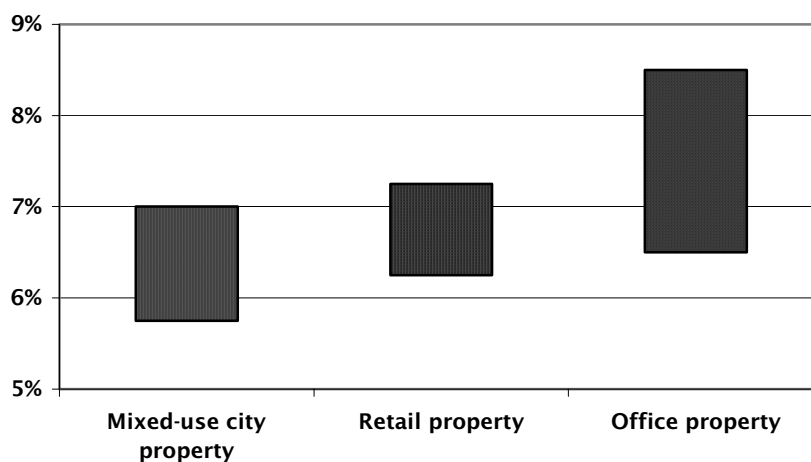


Source: Sadolin & Albæk

As can be seen from the above figure, today’s market displays significantly lower requirements for direct yields on mixed-use property as compared with retail and office property.

This reflects that investors are willing to pay more for the low vacancy risk of residential tenancies. Therefore, yield requirements largely depend on the proportion of residential property and whether property is let at a low cost-driven rent.

Current net initial yield requirements for non-CBD property in Copenhagen



Source: Sadolin & Albæk

As appears from the above figure, a similar pattern applies to non-CBD property in Copenhagen, although it is not as pronounced as in Copenhagen CBD property.

Distribution and hotel property let on long-term leases generating extremely competitive yields

Institutional investors have retained their strong interest in office property let on long-term leases to tenants of good financial standing. Conversely, specialised property, such as distribution and hotel property, rarely attract institutional investors despite extremely competitive initial yields.

In today's market, modern prime location distribution property let on, say, a 15-year interminable lease to a tenant of good financial standing typically generates a net initial yield of around 7.5%. Hotel property generates a yield of some 7.0%, whereas office property let on a similar long-term lease would probably generate a net initial yield of 6.0-6.25%.

Due to the current excess return provided, distribution and hotel property generates a total return corresponding more or less to the total return on office property - even despite significantly weaker value growth rates as compared with office property. This applies particularly to private investors who may benefit from the tax allowances in distribution and hotel property but also to institutional investors, although they do not have such benefits.

In the figure below we have calculated the total return on distribution, hotel and office property investments, respectively, as a function of the property value after 15 years (end-of-period value) as a percentage of the acquisition price.

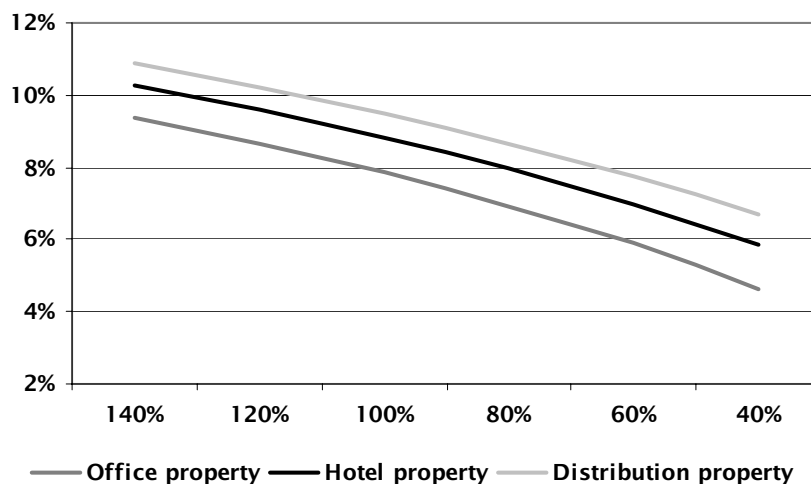
We have assumed that distribution property is acquired at a net initial yield of 7.5%, hotel property at 7.0% and office property at

6.25%. Furthermore, we have assumed an annual rent review of 2.0% p.a.

As appears from the figure, office property would generate a total return of 7.85% p.a. without any increase or decline in value over the 15-year period, whereas hotel property and distribution property would generate total returns of 8.82% p.a. and 9.49% p.a., respectively, under similar conditions.

For an investor targeting an overall return that outperforms the benchmark yield by, say, more than 300 bp or currently about 7.5%, the office property value after 15 years must be at least 92% of the acquisition price. Comparable hotel property generates the same total return if the property value after 15 years is 70% of the acquisition price, whereas the end-of-period value of distribution property only needs to be 55% of the acquisition price to achieve a similar total return.

Total return on property as a function of end-of-period value as a percentage of initial value



Source: Sadolin & Albæk

It is therefore surprising that institutional demand remains focused almost entirely on office property and that we have hence not recorded any portfolio strategies seeking a more diversified sector allocation. This may to some extent indicate a force of habit.

RETAIL PROPERTY SUPPLY IN GREATER COPENHAGEN

Restrictive planning regulations in the retail property area hampering competition

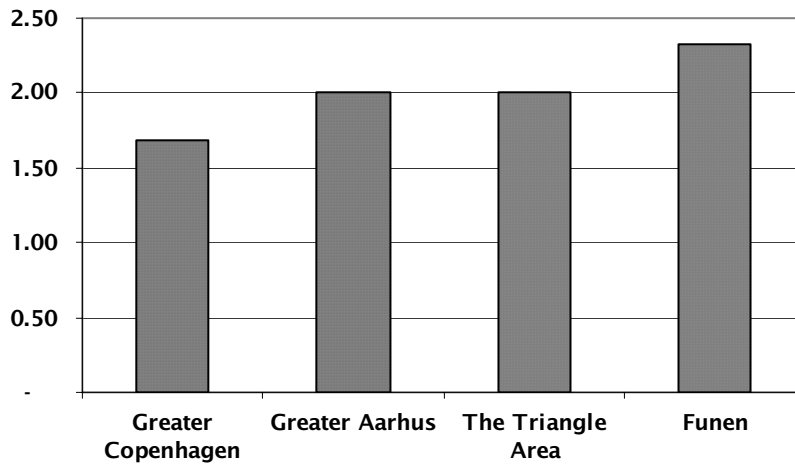
The potential for developing new retail property areas and shopping centres are subject to Denmark's quite restrictive planning regulations. Although a certain amount of regulation may be expedient to retain bustling and attractive environments in central Copenhagen, Danish planning regulations hamper the development opportunities of the retail trade and at times even weaken the prospects for expansion of new retail chains and concepts.

Recently, there has been considerable debate about the inexpediency of the City of Copenhagen not having any current plans to increase the amount of retail space, not even in high street areas where space vacated by former bank branches cannot be converted into retail space under current regulations. Fortunately, we have reason to expect that these restrictions will soon be eased to set off more dynamic developments for retail trade in the Copenhagen CBD.

Shortage of retail space in Greater Copenhagen

In a wider perspective, however, there is still a shortage of retail space in Greater Copenhagen as compared with other parts of the country.

Retail space per capita in selected areas



Source: Sadolin & Albæk

Retail space per capita in Denmark averages just under 2.0 sqm which is not much different from other countries of Western Europe.

As appears from the above figure, however, there is a considerable

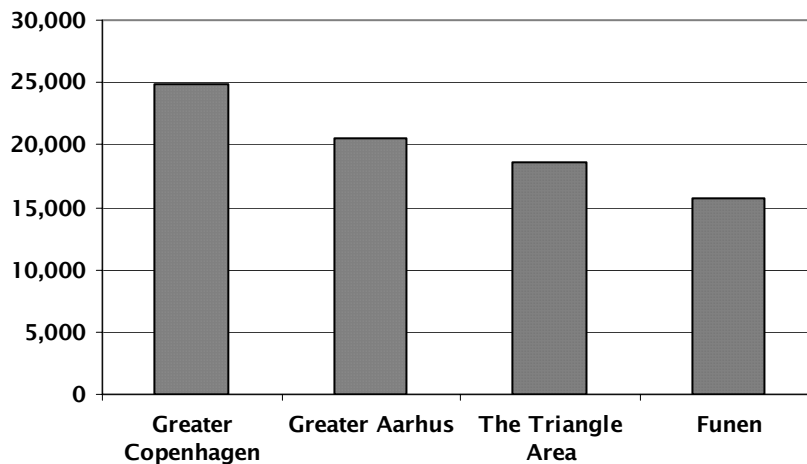
shortage of retail space in Greater Copenhagen as compared with other parts of the country. The establishment of the *Field's* shopping centre in Ørestad will naturally contribute new retail space but it will amount to only some 0.04 sqm per capita in Greater Copenhagen.

Retail sales per capita in Greater Copenhagen is about 10-15% higher than the national average. This is due partly to the relatively high income levels and resulting consumption potential and partly to the fact that a significant share of retail sales in the Copenhagen CBD can be attributed to Danish and foreign tourists.

Due to the combination of moderate retail space and strong retail sales per capita in Greater Copenhagen, sales per sqm of retail space are significantly higher than in the rest of the country.

As can be seen from the figure below, average retail sales in Greater Copenhagen totalled around DKK 25,000 per sqm of retail space in 2000. This is 17% higher than the corresponding figure for Greater Aarhus, 25% higher than the so-called Triangle Area (region constituted by the towns of Vejle, Fredericia and Kolding in Jutland), and no less than 36% higher than the figure for Funen, which has the largest amount of retail space per capita.

Average sales in DKK per sqm of retail space (year 2000)



Source: Sadolin & Albæk

Greater Copenhagen lacking around 600,000 sqm of retail space to match

Calculations reveal that Greater Copenhagen would need no less than another 600,000 sqm of retail space to match the national average. Current projects in the retail area, including the shopping centre projects *Field's* in Ørestad and *Ro's Torv* in Roskilde, are expected to contribute approximately 150,000 sqm of new retail

the national average

space. However, new retail space is also underway outside Greater Copenhagen, for example *Bruuns Galleri* in Aarhus, and the current projects will therefore not change the existing situation.

Although we expect some easing of planning regulations in the retail area, there is nothing to suggest that Greater Copenhagen will experience developments of new retail areas to counterbalance this trend within a foreseeable period.

Retail vacancy in Greater Copenhagen 50% lower than the national average

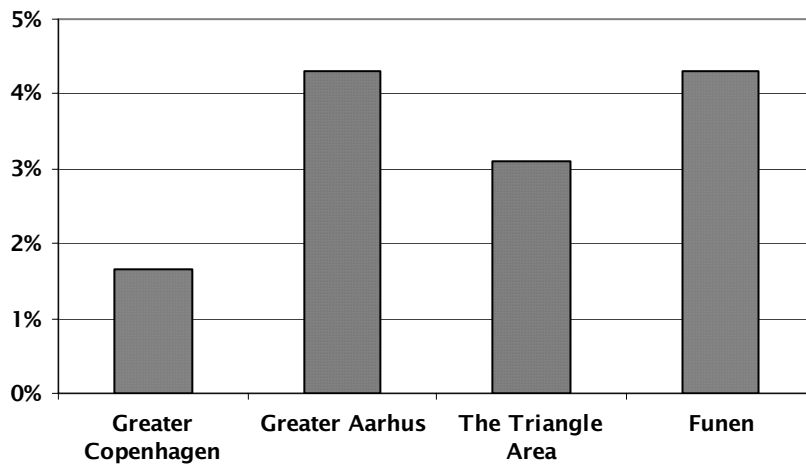
Because Greater Copenhagen has significantly less retail space per capita as compared with the rest of Denmark, the letting probability is higher.

Retail vacancy rates in Denmark currently average around 3.1%.

As appears from the figure below, the vacancy rate in the Triangle Area is in line with the national average, whereas rates in Greater Aarhus and on Funen are somewhat higher, around 4.3%.

Conversely, the current retail vacancy rate in Greater Copenhagen is only around 1.6%, or about half the national average.

Retail vacancy rates in selected areas



Source: Sadolin & Albæk

The high letting probability of retail space in Greater Copenhagen has undoubtedly contributed to investors' initial yield targets for prime retail property being 50 bp lower today than the prime yield for office property, for which the statistical vacancy risk is somewhat greater.

EUROPEAN PROPERTY MARKETS

Sweden – one of the most liquid property markets in Europe

In this issue of the Sadolin & Albæk NewsLetter we have chosen to focus exclusively on current developments in the two Nordic property markets that, together with the Danish market, are the most attractive to foreign investors, namely Sweden and Finland.

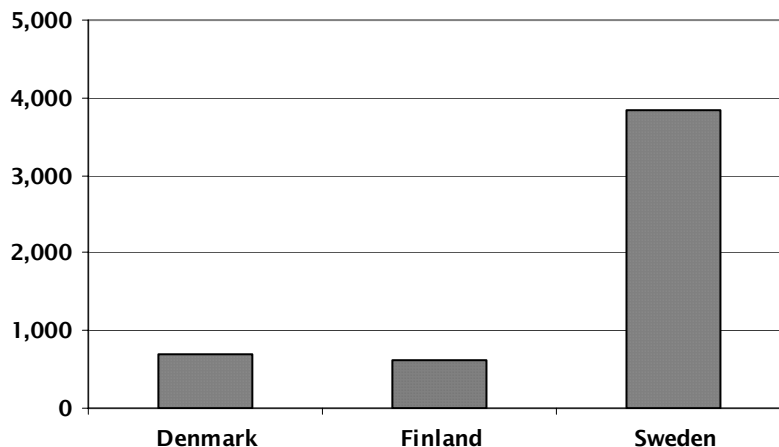
The Swedish market is the largest and by far the most liquid market in Scandinavia, recording some of the strongest activity from international investors among the European markets.

In 2002-2003, there were 6 individual transactions concerning properties or property portfolios exceeding EUR 50 million in Denmark. Only one of these involved a foreign purchaser: DEKA's acquisition of law firm Plesner Svane Grønberg's new headquarters at Nordhavnen – a waterfront district north of the Copenhagen CBD.

During the same period, around 25 transactions each worth more than EUR 50 million were carried out in Sweden. Out of this number, 14 transactions involved foreign purchasers.

The figure below shows that individual transactions in Sweden exceeding EUR 50 million translate into property sales totalling almost EUR 4 billion. During the same period, the corresponding figures for Denmark and Finland were approximately EUR 700 million and EUR 600 million, respectively.

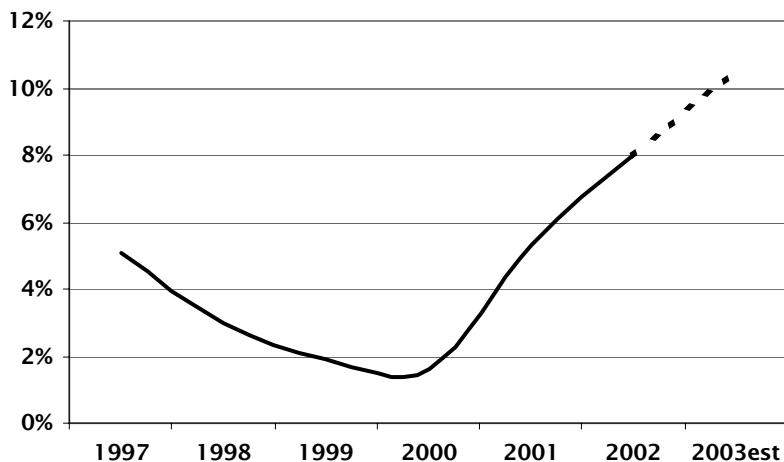
Total transaction volume in millions of euro for transactions exceeding EUR 50 million



Source: Sadolin & Albæk

This considerable investment activity took place during a quite turbulent period for the Swedish property market, with falling rent levels and rising vacancy rates.

Office vacancy in Greater Stockholm



Source: Sadolin & Albæk

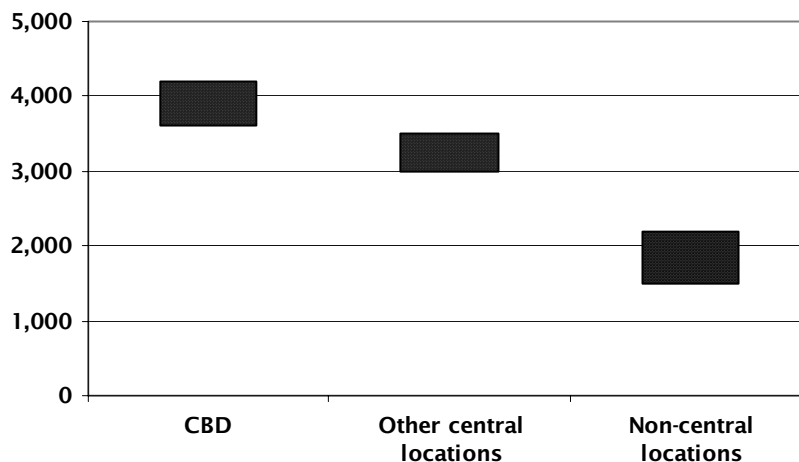
As appears from the above figure, the office vacancy rate in Greater Stockholm was approximately 8.0% at year-end 2002. This marked a significant increase relative to 2000, when the vacancy rate was only about 1.6%.

The forecasts for this year are subject to considerable uncertainty, ranging from the most optimistic forecasts predicting that vacancy rates will stabilise at around 8.0% to the most gloomy ones calling for a rate of more than 12% by year-end 2003.

Stockholm office rental market still under pressure

Office rents in the Stockholm CBD peaked in the first half of 2000 at around SEK 5,500 per sqm per year. Since then, rent levels have declined significantly in line with falling demand and rising vacancy rates.

Current office rents in Stockholm (SEK per sqm per year)



Source: Sadolin & Albæk

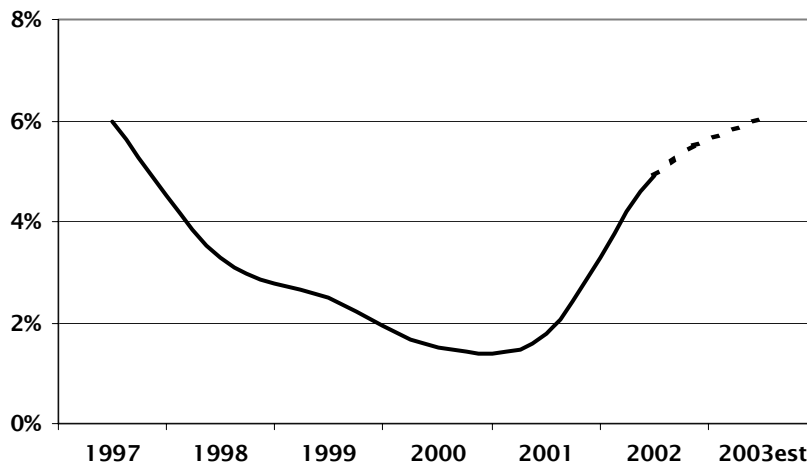
Prospects for the Swedish market, and for the office market in Stockholm in particular, are currently characterised by considerable uncertainty. However, the substantial turnover of property evidences the confidence of a number of Swedish and international investors that the market will soon bottom out. It is worth noting that particularly the market in Stockholm traditionally reacts quite swiftly and with steep increases to signs of an economic upswing.

However, we believe that especially investments in office property let on short-term leases are subject to substantial risk, as economic conditions are somewhat uncertain in the short term due to the weaker global economic trends, the US dollar depreciation and the resulting impaired competitiveness of Swedish industry.

Finland – a euro market dark horse?

Like the market in Stockholm, the Helsinki office market is characterised by growing, albeit not as dramatically, vacancy rates.

Office vacancy in Helsinki



Source: Sadolin & Albæk

However, due to a sharp decline in new developments from approximately 220,000 sqm in 2002 to an estimated 85,000 sqm in 2003, we see no imminent risk of continued high vacancy rates.

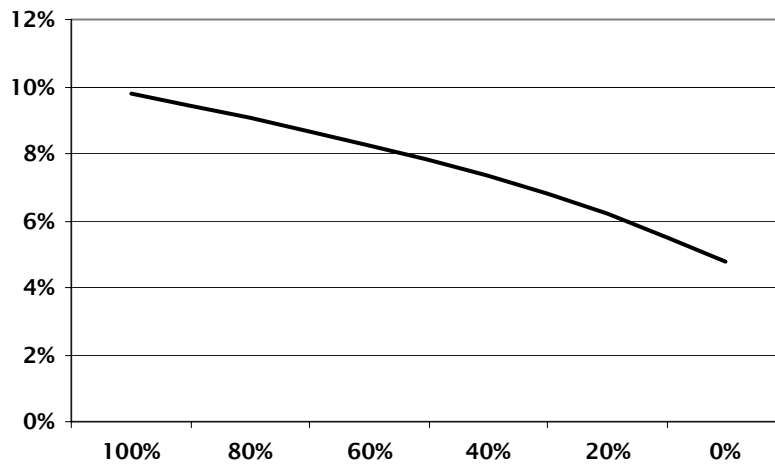
The Finnish property market offers some quite attractive investment opportunities. Finland is a member of the euro zone and is therefore likely to benefit from low interest rate levels for some time yet. In this light, the net initial yields offered by the market on property investments would seem attractive.

The prime yield, that is, the net initial yield on prime investment property let on long-term leases, is currently around 6.5%. Net initial yields on secondary location office and retail property are substantially higher. For example, secondary location retail property let on 10-year or 15-year leases to tenants of good financial standing can often be obtained at a net initial yield of approximately 8.0%.

Property let on a 15-year fully indexed lease obtained at a net initial yield of 8.0% will, provided the property value is maintained, generate a total return before tax of 9.8% p.a. at an annual indexation rate of 2.0%.

As can be seen from the figure below, such property investments will generate a pre-tax return of some 4.8% even though the property has no value when the lease expires.

Total annual return on property as a function of end-of-period value as a percentage of initial value



Source: Sadolin & Albæk

Accordingly, we believe the current yield targets for investments in Finnish property largely reflect that this is traditionally a very illiquid market in which yield targets have been driven largely by sluggish property sales.

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