



SIIC II will drive the French market further **By Fraser Hughes & Jorrit Arissen**

The introduction of the French SIIC structure has been positively received both by specialist real estate sector investors and by the broad market. Since the introduction of the new regime, the French real estate sector has significantly out-performed the market, with exceptional results from existing companies and the arrival of new players in the sector.

SIIC Legislation

At the end of 2003, the French Government introduced their version of REIT legislation – les Sociétés d'Investissements Immobiliers Cotées (SIIC). The underlying motives for introducing the SIIC regime were several. The listed sector in France wanted to align its competitive position in its domestic market against that of non-resident investors, by adjusting the French tax regime to match the tax flow-through regimes applicable in neighbouring countries (Benelux, Germany, USA...). Moreover, the French industry was able to demonstrate to the Ministry of Finance that such a move would generate resources to help reduce the French government budget deficit, by way of the 'exit tax' to be paid by property companies on un-realised capital gains, as they opted to convert into the SIIC structure.

The listed sector in France was also reacting to a persistent and structural discount by the market to the value of their underlying assets, and was able to demonstrate that a listed tax-transparent vehicle, with a corporate income tax exemption for specific areas of activity¹ and an obligation to distribute cash-flow, had enabled the absorption of this discount elsewhere.

SIIC II²

At the end of November 2004, the government announced that it had approved an amendment to the existing SIIC legislation (SIIC II), covering the contribution of assets to SIIC entities in exchange for equity. The legislation was proposed as an amendment to the 2005 finance bill and is applicable for the calendar years 2005 - 2007. During this period, a party can contribute (transfer) a property or property portfolio to a SIIC structure and receive shares in the SIIC in return. The tax liabilities on the difference between the historic value of assets in the balance sheet and their value on the open market will be settled at the reduced exit tax rate of 16.5% (payable in four annual instalments) rather than at normal corporation tax rates (34%).

The SIIC will undertake to hold any such property for at least five years after the transfer. The new legislation does not however impose such conditions on the contributor of such property, and this could give rise to an important new source of equity in encouraging divestment by existing holders of property through this tax-efficient route. There are few examples at present (Accor – Foncière des Régions) but it is expected that the legislation will be of interest to corporates wishing to outsource, to institutional owners wishing to diversify, as well as an exit opportunity for non-listed funds.

¹ EPRA Tax Transparency Committee - European REIT regimes and the impact of the EC Treaty freedoms, August 2005.

² Tête de la Course - Kempen & Co Research, June 2005.



Growth of the SIIC market

Since the introduction of the SIIC structure, the re-rating of the sector in France has provided investors with an exceptional return (figure 1). The FTSE EPRA/NAREIT France has returned 127% since the end of 2002, or SIIC introduction, significantly outpacing both the European and Global indices.

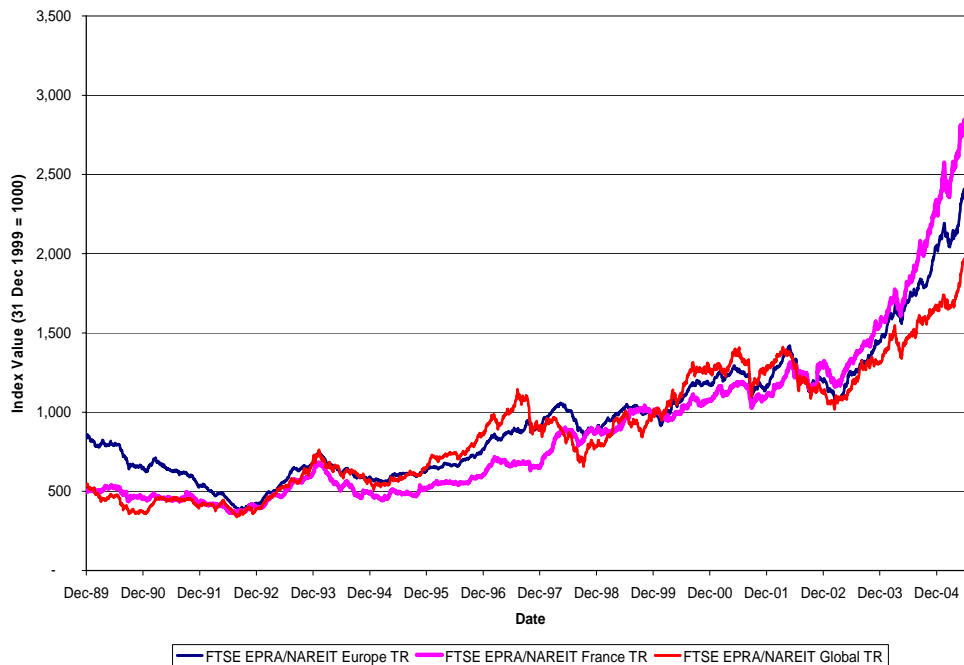


Figure 1: FTSE EPRA/NAREIT France against the European and Global Indices.

Source: EPRA

Figure 2 provides an overview of the current SIIC market. The size of the SIIC market has grown phenomenally since the legislation became effective in 2003. Total market capitalisation has risen from €10 billion to over €25 billion in July 2005 translating not only exceptional individual performances (particularly from the larger, well known companies who have achieved returns well in excess of the broad European market) but an extension of the sector as well.

According to Max Berkelder, Property Analyst at Kempen & Co, "As a result of SIIC I, a number of listed property companies have been de-listed from the stock exchange or have seen their free float market caps been reduced due to bids (i.e. Sophia, Bail Investissement, SFL and Gecina). The hopes are high for SIIC II to change this trend and bring new blood - listed companies to the market such as Casino's subsidiary Mercialys. Other retailers like Carrefour and Lafayette are named in this respect as well. Another viable option for increasing size of the sector is sale of portfolios by opportunity funds to small listed SIICs in return for shares. The benefit of this 'kiss of life' by an opportunity fund is that a small SIIC can grow substantially and the free float of this company rises over time when the opportunity fund sells its stake. This can all take place in a relatively short period of time, and is probably quicker than an IPO process. Some successful new kids on the block are Foncière des Régions, Société de la Tour Eiffel and Altaréa."

Liquidity or traded value has also increased significantly (244%) demonstrating the improved ability to trade the stock in the market. Paradoxically, volatility of



the FTSE EPRA/NAREIT France index has fallen from over 19% at the end of 2002 to 12.5% today.

Company Name	Total return 31 Dec 2002 to 29 July 2005	Market capitalisation in mln as at 31 Dec 2002	Market capitalisation in mln as at 29 July 2005	Percentage change in market capitalisation	Value traded in 2002 mln	Value traded in mln 31 July 2004 through 29 July 2005	Percentage change in traded value
Gecina	107.83%	€1,943	€6,114	215%	€ 393.68	€ 2,839.01	621%
Unibail	131.41%	€3,188	€5,269	65%	€ 1,592.54	€ 3,487.20	119%
Klepierre	103.59%	€1,926	€3,682	91%	€ 357.91	€ 1,057.49	195%
Societe Fonciere Lyonnaise	71.63%	€1,049	€2,035	94%	€ 98.91	€ 618.57	525%
SILIC	127.73%	€743	€1,464	97%	€ 113.97	€ 230.68	102%
Fonciere des Regions	335.92%	€193	€1,524	688%	€ 0.98	€ 94.07	9493%
Bail Investissement	144.46%	€165	€1,354	722%	€ 17.82	€ 418.05	2246%
ICADE EMGP	109.74%	€341	€798	134%	€ 1.29	€ 12.56	873%
Fonciere des Murs	577.19%	€7	€555	7456%	€ 0.27	€ 2.92	978%
Altaera	319.35%	€10	€559	5467%	€ 0.13	€ 3.71	2783%
SIIC de Paris	87.06%	€230	€430	87%	€ 13.43	€ 4.22	-69%
ICADE Fonc des Pimonts	99.04%	€179	€371	107%	€ 0.19	€ 0.63	234%
Acanthe Developpement	60.17%	€163	€240	47%	€ 2.05	€ 37.41	1721%
Soc de la Tour Eiffel	118.99%	€5	€228	4586%	€ 0.47	€ 48.57	10337%
Affine	179.50%	€89	€211	138%	€ 4.60	€ 21.74	373%
SIIC de Paris 8eme	96.21%	€50	€90	79%	€ 0.58	€ 0.69	18%
ADT SIIC	-44.24%	€10	€75	660%	€ 0.47	€ 51.28	10890%
Fonciere Massena	-30.17%	€45	€43	-3%	€ 0.11	€ 3.10	2819%
Mines de la Lucette SA	37.47%	€17	€40	132%	€ 0.45	€ 4.77	952%
ADC SIIC	-95.40%	€31	€34	10%	€ 0.02	€ 3.26	13526%
Total		€10,385	€25,116	142%	€ 2,599.88	€ 8,939.93	244%
FTSE EPRA/NAREIT France TR	126.71%						
FTSE EPRA/NAREIT Europe TR	98.40%						
FTSE EPRA/NAREIT Global TR	82.88%						

Figure 2: French listed SIICs ranked by market capitalisation at 29 July 2005.

Source: EPRA, Bloomberg.

Matadors on the French market

France's largest SIIC is currently Gecina - at the head of a diversified portfolio valued at €8.8 billion³. The portfolio is spread between office and retail property (60%) and 40 percent residential property (40%). Recently, Spanish developer Metrovacesa acquired 68.5 percent of Gecina through a public bid and indicated its intention to implement a more aggressive asset management strategy. Metrovacesa plans to redevelop part of the commercial portfolio to realize higher rental values, and to divest a significant part of the residential portfolio.

The fourth largest French SIIC, Société Foncière Lyonnaise (SFL), is also majority owned by a Spanish company after a successful public offer in July 2004. Although Inmobiliaria Colonial acquired 95.1 percent of SFL at that time (to gain exposure and management in the French market) they have, since the acquisition, reduced their holding to below 80%. In April this year, Juan-Jose Brugera, CEO of Inmobiliaria Colonial, stated that they would further reduce their stake in SFL in order to demonstrate to the market that SFL would continue as an autonomous company within the group, with appropriate governance and a free-float which would enable index-inclusion.

Probably the best known SIIC internationally are Unibail and Klépierre (second and third largest in the sector respectively). Unibail focuses on three distinct business lines: offices, shopping centres and exhibition-convention complexes. Klépierre owns more than 220 shopping malls in Continental Europe with a lettable floor area totalling over 1.5 million square meters. Both of these

³ As at 31 December 2004.



companies have demonstrated management skills in their sector, an enviable track record and a large and liquid free float.

Non-French companies also benefit from the SIIC regime

Besides these French companies, a number of other companies have opted for the SIIC structure for the French portion of their cross-border portfolio. These include Dutch companies Rodamco Europe, Corio, Vastned Retail and Eurocommercial Properties and UK companies Hammerson and CLS Holdings. Due to the existence of the SIIC status, the French subsidiaries of these companies are exempt from tax on income and capital gains provided that the distribution criteria are respected.

Summary

Since introduction in 2003, the French listed real estate sector has benefited significantly. From being viewed as more competitive with its neighbours, to eradicating persistent and structural discounts to net asset value. The EPRA/NAREIT France Index has returned approximately 130% since SIIC introduction, with the market capitalization of the sector ballooning from €10 to €25 billion. Foreign investors have also been attracted into the market, with namely Spanish companies taking large holdings in their French counterparts. In addition, non-French companies have also opted for the SIIC structure. It is envisaged that the updated SIIC II structure, applicable for the calendar year 2005-2007 will further develop the market in the form of new blood.