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Commercial Real Estate in Paris: Yesterday, Today and Tomorrow

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It seems everyone has a vision of Paris (usually romantic) - and an opinion about Parisians (often less so). After 30 years living here I'm beginning to get the hang of the city and life in France, and to highlight some of the changes I've noticed.

In particular, the election of President Macron, who has created a centre ground for politics after the traditional left and right divide collapsed, seems to have liberated the French to believe that change is possible. I have noticed that younger people who have travelled abroad and brought back ideas are excited about staying in France and watching the country become a "can-do" environment. One example is the Station F start-up incubator, the largest in the world with 2,500 workstations and a 10,000 sq ft food court. Another is the Hermitage project in La Défense, Norman Foster-designed 320 m high twin towers with mixed use (office/hotel/residential) for the first time. Planning has taken 6 years!

The Olympic Games, to be held here in 2024, is also a great symbol of confidence and renewal. Oh yes, and the Ryder Cup this year.....well let's leave that out for now.

A little background on the City and its commercial real estate market:

The Paris region has been the heart of a country managed tightly from the centre by the Monarchy, or by the République, after the 1789 Revolution. It's only 2% of the French territory, yet today it's home to 12 million people (a fifth of the population) and generates over 30% of national wealth (660 billion Euros) with an estimated 6 million jobs.



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Comparing Paris with the rest of Europe, it creates 4% of Europe's total GDP (that's more than London or Northern Italy) and is the most densely-populated region.

It's not surprising, then, that this activity needs a lot of real estate to function. The office market is now the largest in Europe (53 million m² or 570 million sq ft) and is broadly split between mostly period buildings in the city and post-1945 stock out of town.

Light industrial / manufacturing are also key components of the economy, and the best estimates are of some 24 million m² / 260 million sq ft of space; while logistics adds a further 19 million m² / 200 million sq ft.

Général de Gaulle made sure that post-war construction did not destroy the historic character of the city. He did this by banning almost all high-rise developments in town (32 m is maximum height in the centre), by pushing development to the suburbs, and by creating five new-build locations, or *Villes Nouvelles*, 30 km distant to house people and provide areas for employment. The high-rise office area of La Défense just west of Paris which comprises 30 million sq ft was also started at that time.

Public transport is efficient and cheap and mass transit is key to defining office locations. It's all very integrated and European; however – as in London – these historic networks have needed major upgrades of late. After all, the first metro line was built in 1889 to move people to see the Eiffel tower and the Universal Exhibition.

Much more exciting than renovation is the Grand Paris initiative, a massive extension of the transit network by 2030 - to link up suburban destinations and thus avoid everyone having to come in to town to change lines. Two hundred km of track and 68 new stations will see 28 billion €uros spent (*want to bet the final bill is higher?*).

Of course, the French still have a love affair with their cars and there is congestion both in the city and on the freeway system, which includes three ring roads circling Paris; driving is dicey, but a lot less scary than Italy!

So what are the realities of the day-to-day commercial real estate market?





Offices are booming; 2017 take-up was 2.6 million m² (28 million sq ft), a record year since 2007, and 2018 has seen 1.8 million m² (19 million sq ft) absorbed. Vacancy rates are now the lowest I have ever seen, maybe 1.5% in the CBD. Any space not leased probably has a major defect - in fact, this is the first time landlords have the leverage in the market since 2000, and they are taking full advantage!

Much of the office stock is obsolete or simply not adapted to modern usage. The converted period apartment buildings have parquet floors and chimneys. Even lawyers now want more flexible space which permits technology to be installed and maintained. Maybe Wi-Fi will replace cabling and save drilling through walls. Still, the structure of buildings makes them inherently difficult to remodel. Paris planning protects the historic façades, so the opportunities for new buildings in town are limited. Development behind retained façades is never efficient – and top floors in those buildings suffer from low ceiling heights.

When a new build is available, there is strong competition from large companies which take entire buildings, leaving only rare sub-lets for smaller tenants. Over 2 million m² of offices are being constructed for 2019 – 2020 in the Paris region, and some 60% is pre-let. Prime rentals in the CBD are quoted at over 800 €/m² per annum exclusive (that's \$80 US per sq ft p.a. NNN). In the La Défense high-rise area west of the City, rentals are nudging up to 600 €/m² (\$60 US per sq ft p.a. NNN). Then there are service charges, property taxes, etc., which add 25% to 30% in occupancy costs.

In this tight office leasing market, I find it's difficult to persuade clients of our added value as tenant advisors, when the market seems stacked against all tenants. But then tenants discover how extremely complex and fragmented the market is, with little collaboration between the brokers, and no centralised listing service such as CoStar as there is in other European countries (e.g. UK or Holland). Technology has not affected the way French real estate brokerage operates, except to speed up communication and make people more accessible.

So to identify available space, we brokers approach landlords directly, and check with each individual agent – time consuming and inefficient. For the tenant who is not represented, there is no way to comprehensively check the market for all the available options.

Brokerage fees are payable by the tenant, and usually quoted at 30% of the first year's rental. In fact, this hides the frequent 'double-dipping' by some brokers- as institutional landlords will pay their brokers a fee, not necessarily disclosed to the tenant. In contrast, our approach is to quote a 15% fee, or a fixed fee, with performance bonuses as appropriate.





French law obliges the landlord to offer a minimum 9-year lease term, and the tenant has break options with no penalty at the end of years 3 and 6 – hence the “3.6.9” pattern you may have heard of. This makes a French lease the most flexible in Europe, and it limits the amount of sub-lets (when a company has a problem they can give notice to get out of it!). Short-term leases are just coming in following new legislation in 2017, and we expect this segment of the market to grow when the market contracts. Negotiating different terms is possible, and with larger blocks of space some clients choose to commit to 4 or 6 years without a break to obtain concessions on rental rates, fit-out, rent-free, etc., if their business plan can sustain it.

Light industrial rentals range from 60 to 120 €/m² exclusive (\$6 to \$11 US per sq ft p.a. NNN) depending on the location, quality of building and office configuration. Rather than asking small businesses or plumbers what they need, developers usually choose to build offices rather than simple industrial sheds wherever possible to increase rental rates.

Logistics rentals vary widely, as recent legislation limits what can be stored if buildings do not reflect the new code – which has made older sheds obsolete. Transporters will pay a big premium for larger new-build Grade A units, where they can install the technology and robotics they need - and those rents are reaching 60 €/m² exclusive (\$6 US per sq ft p.a. NNN). Older facilities will be in the 40 to 50 €/m² range – or may become unlettable without significant investment.

Leasing commercial real estate in Paris is complex, and having an expert on your side will definitely simplify the process for you and yield superior results. Available office and industrial space will continue to be scarce in 2019, so having an expert advisor that represents your interests is the smartest way to secure the most optimal facility for your business - and avoid the pitfalls of obsolete space. Despite advancing technologies in real estate worldwide, the process of sourcing and securing commercial space in Paris remains “old school” - and not accessible with a few keystrokes over the world wide web.

Article submitted by Charles Tatham, SIOR, MRICS / ITRA Global Paris, France

