$25.00

Italian Real Estate For Sale

International Real Estate Institute

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Preface

This writing is a follow-up to the Year 2000 World Congress of the International Real Estate Institute that was held in Rome in May, 2000. The Year 2000 Jubilee finds many new offerings of investment real estate on the Italian market in response to Italian corporate restructurings and Italian government progress toward meeting European Union membership requirements and European Central Bank requirements for adoption of the euro.

Introduction

In international real estate circles, Italian real estate has assumed significance as the previous millennium came to a close. As Italian pension funds, companies, and the government have placed some investment-type properties on the market to start the new Italian real estate era, even more real property offerings are proposed in 2001 and during the next few years.

The Significance of Italian Real Property Today

International real estate investors note the significance of Italian investment real estate. First, Italian real estate may represent opportunities for portfolio diversification. Second, Italy's membership in the European Union and its adoption of the euro implies the availability of good investment properties with more transactional transparency with a more stable currency. The Italian government - even though subject to instability from frequent changes in the government leadership - is following policies and programs to reduce government debt and reduce earlier levels of inflation. Such policy implementation and program administration are part of the requirements for European Union membership and European Central Bank requirements for Italy's adoption of the common European currency, the euro. At the same time, Italian companies are restructuring to meet changing European and global market conditions and for greater profitability from operation in the integrated European marketplace. Some large Italian companies are selling assets to invest more funds outside of Italy in their corporate diversification efforts. For example, Telecom Italia acquired recently Entel, a Chilean telecommunications company, for $905 million.

The adoption of the euro promises a stronger currency for the transaction of business and investment. As a long-term government policy, the Italian lira has constantly been devalued over time to increase the competitiveness of Italian businesses and their products in the global marketplace.

Italian Property Within the International Scene

International real estate analysts continually look the world over for good investment opportunities. From whatever vantage point - London, New York, Amsterdam - they view the changing scenes in countries of all continents. Since property prices tend to be relatively high and rates of economic growth relatively low in Western Europe, the United Kingdom, Scandinavia, the United States, and Canada, the analysts tend to look for better opportunities outside these developed area. Recently investors have studied opportunities in Asia as a result of the Asian financial crisis of the late 1990s. Property prices have fallen significantly in such locations as Bangkok, Jakarta, Hong Kong, and Tokyo. As Africa was featured by U.S. President Bill Clinton on a tour of Africa in 1999, investment analysts turned some of their attention to the Republic of South Africa, the most developed country of the continent. The heightening of the tensions and military deployment of the continuing Israeli-Palestinian conflict has generally cooled any scrutiny of Middle Eastern investments in general. The continuing financial and social problems of Latin America generally preclude investigation of such advanced countries as Brazil, Mexico, Argentina, and Chile. But, as a result of the continuing international property analyses, many have turned to the Italian property market and focused on the continuing business and government changes to view the possible yields from various possible types of real estate investments. Italy may be one of the Western European countries that may hold promise for profitable real property investments: Property prices are relatively low, more investment-grade properties are being offered for sale by government agencies, businesses, and pension funds; the Italian currency tends to strengthen; and the transparency of transactions and equity in tax administration are increasing with political and government reform.

Forms of Italian Property Investment Alternatives

Italian property interests are available in multiple forms to Italian and foreign investors. Three of the available forms include (1) real estate company stock listed on the exchanges, (2) direct investment in the partial or total equity of a single or multiple properties, and (3) investment participation in a real estate fund composed totally or partially of Italian real properties. Much of Italian property has not been available in any investment form to local and foreign investors due to government direct ownership of Italian real estate, state-owned

company direct ownership of Italian real estate, and insurance company and pension fund ownership of Italian real estate. The pension funds who own large amounts of Italian property are both publicly- and privately-owned funds. Today these large Italian real estate owners may be acquiring Italian real estate and/or disposing of Italian real estate. For example, the Perilli corporate real estate subsidiary, Milano Cantrell Company, is seeking to acquire certain properties while many partially government-owned companies such as Telecom Italia, Enel, the partially state-owned electric utility, and Eni, the partially state-owned oil and gas company, are seeking to dispose of certain properties.

The Government Privatization Movement

The government of Italy has had pervasive ownership of corporate stock of major Italian companies that has included large real estate holdings. In order to reduce the government debt to satisfy European Union and European Central Bank requirements, the various government agencies are selling at least a part of their Italian company stock holdings. As the state-owned companies sell blocks of their stock, a participation in large company holdings of real property may be acquired indirectly.

The various levels of Italian government - municipal, state, federal - have also owned property, sometimes through the medium of government pension funds. To reduce total government debt and to reduce the Italian debt percentage of Italian gross domestic product, some of these properties are being sold. These holdings include many types and qualities of properties from vacant or largely vacant inefficient and less functional buildings that are registered and protected as historically significant properties to Class A residential, office, retail, and industrial buildings that fit current business needs. The same things tend to be true of the large insurance company holdings. The large Italian real estate funds may have extreme property types within their long-term property holdings.

Corporate Disposition of Property Portfolios

Italian corporations have been setting up separate real estate subsidiaries - many listed on exchanges - to hold their corporate real estate. In many instances the spin-off of the corporate real estate into listed subsidiaries has presaged future corporate sale of owned and leased real property, in part or in total. Banks, for example, have accumulated real property as a tax-efficient way of building up reserves. Today changed Italian legislation discourages corporate buildup of reserves in this manner.

The Italian corporate real estate spin-offs into separate corporate subsidiaries may have started with the Instituto Nazionale delle Assicurazoni or INA spin-off of 85 percent of its property portfolio into the separate property company, UNIM, in a $2.9 billion deal in November of 1998. INA had just moved from being a private company to being a public company. As a public company, the company management thought that property assets made up far too high a percentage of the INA total investment portfolio. As UNIM was listed on the Milan stock exchange, it may have become the largest listed real estate company in Italy and the second-largest property company in Europe. The government still holds 1.1 percent of the INA insurance group.

Eni, the Italian oil and gas group, has completed its disposal program of non-core business including $960 million of property assets. These property assets were sold to Goldman Sach's Whitehall property fund in early December, 2000; other property assets of Eni that are valued about $117 million will be sold to other buyers. Eni's listed property company in which it holds 90 percent of the equity is called Immobiliare Metanopoli. Before Immobiliare Metanopoli shares dropped about 40 percent at the end of year 2000, this property company attained a stock market value of approximately $1.1 billion. As part of the total euro 1.1 billion deal between the Goldman Sach fund and Eni, the 90 percent stake in Immobiliare Metanopoli that was held by Eni was sold to the Goldman Sach fund. The Italian government still owns 35 percent of Eni.

The real estate subsidiary of the industrial company Gruppo Comparr-Montedison, Iniziativa Ediliazia, was bought in 2000 by a partnership comprised of an Italian property firm and Real Estate Fund III created and managed by Morgan Stanley Dean Witter. Previously the Morgan Stanley Real Estate Fund II bought a portfolio of distressed property loans from Instituto San Paolo di Torino in 1997 and, a year later, a portfolio of Turin office buildings from the Fiat Group.

In November, 1999, Telecom Italia spun off some of the most valuable properties of the group into an independent real estate subsidiary called IM.SER. Now Beni Stabili, Lehman Brothers, the U.S. investment bank, and Telecom Italia hold various shares in IM.SER that is valued through the transaction at euro 2.9 billion (about $2.6 billion). Beni Stabili, perhaps now the biggest property company in Italy, holds a 45 percent share, Lehman Brothers a 15 percent share; and Telecom

Italia, a 40 percent share. The three partners have joined together to manage and enhance part of the Telecom Italia's property assets. Beni Stabilia, is the property offshoot of San Paolo-IMI. San Paolo-IMI, the result of a merger between Instituto San Paolo di Torino bank and IMI bank, is Italy's biggest bank group. This large bank merger was encouraged by the requirements for Italy's admission to the European Union. Since the Italian banking industry was seen as too fragmented, banking mergers were encouraged.

In the fall of 1999 Deutsche Bane Alex Brown's head of Southern European real estate, stated that between $13 billion and $15 billion of real estate assets were due to be offered over the years 2000 and 2001 . A part of this amount has reached the market by early 2001. Italian real estate companies including Gabetti Group are creating special departments and divisions to assist with the proposed property disposals that are expected over the coming five years.

Demand and Supply for Investment Property Space

The demand from local and foreign investors and property occupiers for Class A property tends to far surpass the supply of Class A space available. This imbalance of demand and supply has existed for some time. The imbalance has been accentuated by the recent period of economic prosperity. The Italian economy has thrived during the last half of the 1990s as has the rest of Western Europe as represented by the European Union. During the less economically prosperous periods this imbalance was not as momentous perhaps.

The Impact of Historic Property Preservation and Tourism Encouragement

As the demand for functional and efficient office, retail, and industrial space has reflected the economic prosperity of any particular year, the supply of functional and efficient investment property has been influenced by the public-private consensus that the historic buildings of many areas should be preserved and protected. Italians are proud of their heritage. They are also aware that tourism is a large component of the national government and business revenue and personal and business incomes. Certain areas are more affected by the revenue derived from tourist sites than other areas. The need for modern, up-to-date commercial, industrial, and residential space particularly exists from the center of Italy to the northern boundary where the majority of the historic preserved buildings attract high volumes of tourists each year.

The Impact of the North-South Divide

The south of Italy, in contrast, requires less high-quality property due to the lower levels of business and industry and continuing high-levels of unemployment. There are few tourist attractions south of Rome, that lies in the west central portion of Italy, with the exceptions of Naples and Capri; little industrial growth has been exhibited in the south of Italy for many years. During the 1990s the Italian government- business establishment has tried to encourage high-technology development in the less economically viable south of Italy.

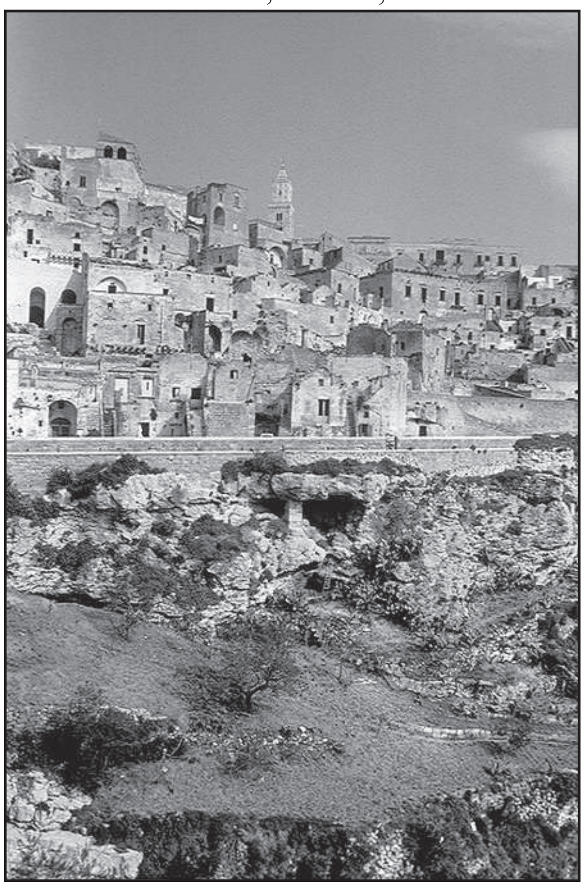
General Corporate Requirements for Space

Multinational and Italian corporate demand for high-quality commercial, industrial, and residential space has tended to focus on the Milan and Turin areas for business operational and distribution purposes. Multinational and Italian corporations continue to need office locations in Rome that cater to governmental and public relations functions. The top multinational and Italian corporate executives need access to Italian government officers as well the consular and embassy officers and staff of the country of their official corporate domicile. Large amounts of office space are absorbed by the various local and foreign government-related offices. Much of this space needs refurbishment and reconstruction for modern government and business purposes. Industry does not tend to seek operating spare in the Rome metropolitan area.

Availability of Business Services

in Rome and Milan

Commercial interests are well served in Rome as in Milan by the presence of many business services such as legal, accounting, marketing, and management-consulting services. For example, the international accounting firms including Reconta Ernst & Young and PricewaterhouseCoopers have offices in Milan to serve Italian and multinational companies. The many international law firms of Rome include Alegi & Associates, Brosio, Casati a Associati, Dobson & Pinci, and Pavia Ansaldo a Verusio. In Milan the international law firms include Baker & McKenzie, Brosio, Casati a Associati, Dobson & Pinci, Foster & Associates, Graham & James, Katten, Muchin & Zavis, Pavia Ansaldo a Verusio, Avv. Thomas R. Mitchell, and Avv. Massimo Sanguineti. Some of these service firms desire better quality office space in appropriate locations for their current and future needs.



Space for the Growth Industries

The growth industries of most countries of the world tend to be the telecommunications and high technology sectors. This is true of Italy, also. While these economic sectors tend to require more appropriate space than is available, at the same time, the government who is a major shareholder in many of these companies is pursuing programs of real property disposition in order to reduce its debt. Some of these growth industries need more functional space than they now enjoy. As a result of the current real property disposition era, high-tech growth companies are hoping for more appropriate new or refurbished space for their needs as a result.

The Impact of Transportation

Since traffic congestion is intense in such major Italian urban areas as Rome and Milan, business space is sought in locations accessible to key rail and subway stations. For example, every day two million cars and 600,000 motor scooters traverse Rome's streets. Due to this heavy traffic congestion, both Rome, the religious and government capital, and Milan, the business center, have subway and bus lines and railroads that link business and industry centers with residential space and other urban centers in Italy and outside the country. A portion of the EuroStar rail system in Italy, Euro Italia, serves the Italian need for links between principal cities of Italy and, on an extended basis, serves the Italian need for links to other principal cities of Europe.

The subway lines are important locational considerations for building occupants in both Milan and Rome. The "new Rome" suburban development called "EUR" is vitally accommodated by several subway stations that link the Exposition Universal Roma (the meaning of "EUR") and the international airport on the coast to the west of Rome. Local residents point out, though, that the 20-mile length of the Rome subway system is less than the length of the 60 underground catacomb walkways of Rome. As the engineers and administrators prepared for the Year 2000 Jubilee that was expected to attract 30 million visitors (60 percent Italian and 40 percent foreign), they realized that adding even a half mile of the Metro subway line would be incredibly difficult. Since Rome is essentially a museum of the early history of mankind, by digging down only

two feet for subway excavation one might easily run into the ruins of a early Roman villa or other such momentous discovery. Planned excavations unrelated to the Metro (subway) continue to unearth important discoveries about the early Roman civilization.

Multinational companies' locational preferences are particularly sensitive to the locations of existing international and general aviation airports of the major Italian cities. In Rome, government and business executives whose offices and homes are located near the subway stations are advantageously linked on a direct line basis to the Rome international airport. Milan government and business officials are served by two airports that lie to the north of the metropolitan area. The Malpeesa International Airport, the most recently built airport that seeks to relieve the traffic pressure from the closer original international airport, is still talked about in terms of its long distance from the Milan business center. The new international airport, which is located approximately 30 miles from the city line, requires too much time for its access even in today's terms, according to the current press.

Other Characteristics of Italy That Influence the Demand-Supply Balance

The demand and supply of real property is closely associated with population characteristics, the properties of the Vatican estate, gross domestic product relationships, inflation, unemployment, the balance of trade, the government debt position, and the currency relationships.

Population Characteristics

The total population of Italy approximates 60 million. The earlier 1996 population census produced a count of 57.5 million. The majority of the population inhabits five principal urban areas that encompass four of the 18 provinces of Italy proper and the island of Sicily: Rome in Lazio Province with a population of roughly 3 million, Milan in the Lombardia Province with a population of roughly 1.5 million, Naples in the Campania Province with a population of roughly 1.1 million, Turin in the Piemonte Province with a population of three quarters of a million. Generally the more affluent part of the population inhabits the north including Rome in the west center of Italy. The large percentage of elderly citizens depends on government pensions primarily. The current government leadership seeks to enhance the pension programs that would have an effect of increasing the capital of the Italian financial system and reduce the government indebtedness with the development of more private pension plans.

The preponderance of Catholic citizens, in comparison to Protestant citizens, generally means a respect for the Catholic history of the country. There is a strong regard for the preservation and enhancement of the Catholic basilicas and other churches who do not house religious relies of great significance. Of course, there is also respect for the preservation and enhancement of barbarian and heathen structures and art, such as Hadrian's tomb, because this also is an important part of the long history of Italy and the world.

The Vatican Properties

The Vatican is a separate political and governmental body within the national boundaries that define Italy. The Vatican lands cover approximately 44 hectares that surround St. Peters Basilica plus the lands covered by additional Rome basilicas outside the formal Vatican-St. Peter's estate including St. Paul's Cathedral and St. Mary Maggiore's Cathedral. The formal, integrated Vatican estate that surrounds St. Peters Basilica contains significant amounts of office and residential space that includes the private apartments of Pope John Paul. Several museums make up a large part of the Vatican estate. They contain immense amounts of statuary - in addition to the immense amount of sculptured religious art in St. Peter's Cathedral - wall and ceiling frescos, and silk and woolen tapestries.

The Geography of the Country and Building Material Problems

In many areas of Italy, the construction of structures for any purpose is arduous due to the geography. Of the two principal urban centers, Milan and Rome, the construction of buildings in the Milanese metropolitan area is much easier than the construction of buildings in the Rome metropolitan area. While Milan rests on a rather level plain that borders the Italian Alps to its north, Rome lies about 25 miles back from the coastline formed by the Tyyrrhenian Sea and contains many sharply rising hills. In the Roman era before and after the birth of Christ, Rome was said to exist on seven hills. Even though the "seven hills of Rome" presented many construction difficulties, the Roman Empire that encompassed much of the known world was headquartered in marble and granite buildings arranged on these "seven" hills. Even the difficult procurement of clean water impelled the invention of the early Roman aqueducts that brought clean water from the mountainous areas of the central part of Italy to what continues to be Italy's largest city.

Quality building materials were so scarce in the eras of building and reconstruction of the Roman Empire that heavy building materials were borrowed from previous buildings for new structures desired by the new government leaders. For example, the marble from the many lower levels of the sports field of the Coliseum was borrowed for the construction of the Roman Forum and then marble from these two spectacular historic building complexes was borrowed for the construction of the later large public buildings including the multiple large basilicas and the Pantheon. At that time, the builders were already recognizing the scarcity and expense of procuring high-quality and long-enduring building materials for new construction projects.

Gross Domestic Product Relationships

The gross domestic product of Italy rose from \$1.1 trillion in 1998 to a forecasted \$1.3 trillion in 1999 which reflects a 2.6 percent change in real gross domestic product (often abbreviated "GDP") growth. Looking at GDP per capita we see that the per capita productivity rose from \$20,300 in 1998 to a forecasted \$22,700 in 1999. Wage rates were expected to rise 3.4 percent from 1998 to 1999. These figures reflect the economic prosperity of Europe in general and Italy in particular as a major country within the highly populated, affluent region.

Inflation and Unemployment

The Italian inflation rate remains less than two percent which is in line with the low inflation rate of many developed countries. The change in the money supply was reduced by more than half by the Bank of Italy between 1998 and 1999. This financial move underlies the reduction in inflation from earlier years. Industrial production rose on an annual basis from a 2.6 percent rate of change from 1997 to 1998 to a forecasted 2.9 percent rate of change from 1998 to 1999, according to the June 15, 1998 Financial Times. Unemployment, on a average basis, was expected to decline from 11.9 percent in 1998 to 11.6 percent in 1999. But the unemployment situation is very unbalanced in Italy. In the south, the rate of unemployment is estimated at roughly 20 percent while that of the north of Italy is estimated as low as six percent.

Balance of Trade

Exports continue to exceed imports which gives Italy a positive trade balance. The country's chief trading partners are the European Union members. The principal EU trading partners are Germany, France, and the United Kingdom. A positive trade balance is maintained only with the United Kingdom. A positive trade balance has recently been generated with the United States, also. Italy exports 7.9 percent of its goods and services to the United States and imports only 5 percent of its products from the United States.

Government Debt Position

The relatively high level of Italian government debt is reflected in its government debt as a percent of the country's gross domestic product. The percentage, 118.7, for 1998 was expected to decline to 114.7 percent in 1999. The government, encouraged by the European Union, is expected to reduce this debt position even further in the near future with its privatization plan for its assets.

Currency Relationships

The euro has been adopted for government and commercial transactions, but the Italian lira remains the currency for retail and smaller transactions. As of January 1, 2002, the euro must be used in accounting and the presentation of financial statement.

Investment is encouraged by the recent strengthening of the euro against the U.S. dollar and the Japanese . The Italian lira has continually declined in value over prior decades. The continual devaluation of the lira has encouraged the international sale of Italian goods and services. The investor normally benefits from the strengthening of the foreign currency in which investments are made. For currency management purposes, hedging instruments such as forward, futures, and options contracts have been developed for the euro just as they exist for the Italian lira, pound sterling, the French franc, the Deutschemark, and the Swiss franc. As the various separate European currencies are totally replaced by the euro, the derivatives used for hedging will be confined to the euro and the other European Union currency derivatives will be discontinued. As a case in point, the Italian lira derivatives will be phased out as all future Italian business is done using the euro.

Some Characteristics of the Italian Real Estate Market

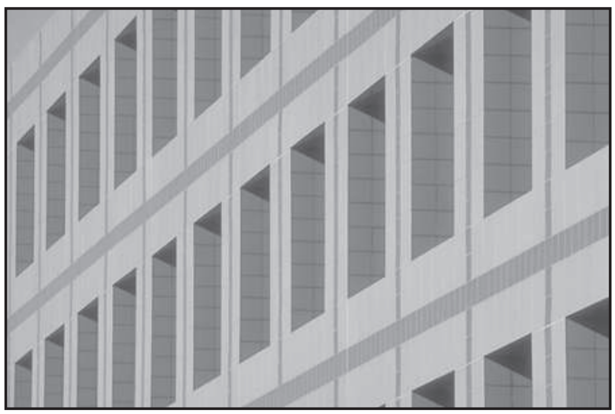
We now turn to the licensing of real estate brokers and agents, property sale and leasing patterns, trends in rents, terms of lease contracts, public property and cadastral registers, and taxation.

Licensing of Real Estate Brokers and Salespersons

According to a full-time real estate person who is employed full time for an international real estate firm whose branch is located in Italy, real estate brokers and agents (otherwise called "salespersons" in the United States) do not have to be licensed or meet government licensing requirements in Italy. They have to be registered with the local Chamber of Commerce though. In effect, anyone can pursue real estate activities that lead to compensation from the real estate owner and/or buyer or lessee in the form of real estate commissions. But international real estate firms based in the United Kingdom, at least, expect their employees to fulfill the professional requirements that are normally expected of United Kingdom estate agents and surveyors. Those requirements are established by the three large professional real estate associations of the United Kingdom. Quite often the Italian and other foreign branches of the large international real estate firms based in the U.K. are staffed with people who have met the requirements for the professional designations of the Royal Institution of Chartered Surveyors - which is a long-standing association among the three prominent estate management associations of the U.K. - or aspire to fulfill those requirements in the near future.

Property Sale and Leasing Patterns

The highest proportion of the total number of Italian property sales - 90 percent - lies in the residential sector. The second ranked sector for property sales falls in the retail and industrial building sector - approximately 4.5 percent of total property sales; the third ranked sector falls into the “other typologies” sector - approximately 3.5 percent - which does not include the office sector. The fourth ranking sector for property sales - 1.3 percent of total property sales - is the office/office building sector, according to the latest figures compiled by the Gabetti Group Research Department. The latest Gabetti property sales figures cover 1999 and the expectations for year 2000. Looking only at the sales of land, sales of agricultural land have recently comprised more than 70 percent of total annual land sales; building land sales, over 15 percent; and sales of other types of land, a little over 10 percent.



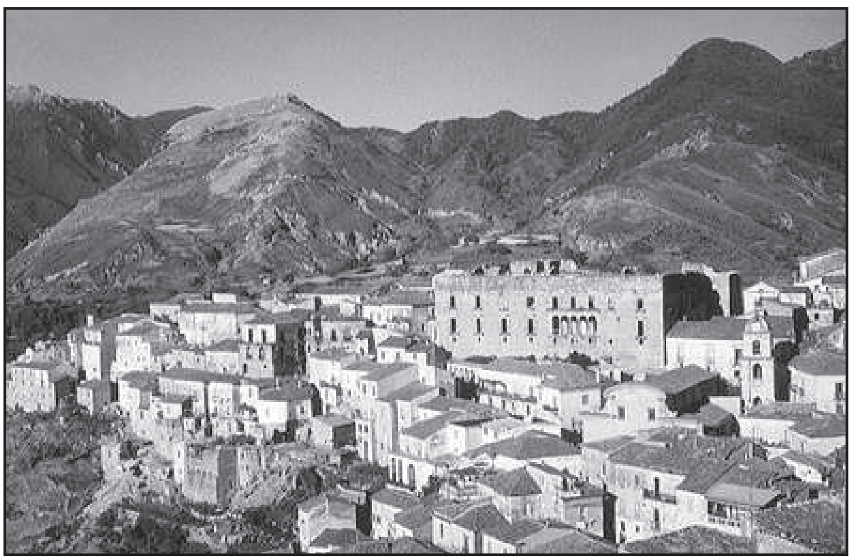
On the basis of sales volume, the proportions of total sales volume differ from the proportions of number of sales by sector. In 1999 residential sales accounted for 80 percent of the total Italian property sales volume; retail and industrial sales volume, 11 percent; offices, 5 percent, and other types of properties, 4 percent. About 60 percent of the residential market was concentrated in the northern portion of Italy since 35 percent was associated with the northwest section and 21 percent with the north east, 18 percent of total 1999 sales were associated with the center of Italy and 20 percent, with the south.

At all monthly household income levels with the exception of the lowest group, there is significantly more demand for housing ownership than for lease of housing. The lowest income group - that representing net monthly family income of less than Lira 2 million - the demand for leased housing is about three times stronger than the demand for owned housing. For households with over Lira 5 million in net monthly income, the demand for owned housing is about twice that of the demand for leased housing. At the same time, the percentage of leased housing for all income levels probably surpasses the percentage of owned housing in the three major cities of Italy - Rome, Milan, and Turin. This pattern tends to be true no matter what the country due to the traffic congestion, the preference for residential locations closer to major city workplaces, and the lack of housing for ownership generally in the center city. Where the number of sales of residential space in Italy have increased about 25 percent from 1995 to and including 1999, the number of lease contracts signed for residential space has increased 35 percent. Therefore, the Italian property companies have seen increasing business in both residential unit sales and leases, but the strongest growth has been in leasing, according to the Gabetti Research Department.

To approach the topic of office space ownership and lease, we need to look at the distribution of Italian companies by type of activity by geographical region of Italy. While companies associated with agriculture, hunting, forestry, and fishing comprise roughly 23 percent of total Italian businesses, industrial, energy, and construction companies make up 25 percent of total Italian businesses, Service companies comprise a little more than half of all Italian companies, and they are spread rather evenly across Italy with some concentration in the northwest and center areas of the country. All types of businesses need office space for their administrative functions, but service businesses generally require only office space. Therefore, office space demand is a little stronger in the northwest and in the center of the country than it is in the northeast and the south. The major cities of Rome, Milan, and Turin generally accommodate the most office space for administrative headquarters.

Trends in Rents

When the rent control law was changed in 1992, rents became negotiable between the landlord and the tenants. Provisions for renewal of expiring lease contracts were part of Italian Law 359 of 1992, Article 11 Contracts in Derogation.



As of early 2010, office and retail rents are expected to rise in all major Italian cities in general, according to Gabetti Group, while industrial rents should rise in all cities with the exception of in industrial rents in Turin and declining industrial rents in Genoa. Office rents are expected to strongly rise in Milan, Florence, and Naples with only moderate increases in Genoa, Bologna, and Rome. Retail space rents are expected to strongly rise in Genoa, Bologna, Florence, and Naples and only rise moderately in Turin, Milan, and Rome, according to Gabetti Group.

At the end of year 2000, we can review some generalized office rents and their trends in three principal areas of Rome. Office space in prime central business district locations of Rome rents for approximately $300 per square meter per year or approximately $30 per square foot per year. In the EUR (abbreviation for “Exposition Universal Roma”) district, office rents approximate $220 per square meter per year or approximately $22 per square foot per year. Healey & Baker estimate that 70 percent to 80 percent of Rome’s multinational corporations are situated in the EUR district for several reasons. In the periphery of Rome, office rents approximate $120 per square meter per year or approximately $12 per square foot per year. Since it is difficult to find a large, well-located construction site for a large, modern office building in the center business district of Rome and the existing CBD office buildings generally need renovation and reconstruction, most multinational company office occupiers must seek more modern and efficient office space in the EUR district or more peripheral locations of the city.

Terms of Lease Contracts

We need to review general lease contract terms for both residential and nonresidential space since the terms vary measurably. Lease contracts are governed by the Civil Code of Italy where the leased property is located.

Residential Lease Terms. Residential leases where the *rent is unrestricted* run for four years with automatic renewal for a further four years. If the contract terms permit or if any serious reasons should exist, the tenant may leave the premises by giving the landlord notice six months prior to the expiration of the residential lease. The landlord may refuse to renew the original lease if conditions explicitly covered by the lease exist. Where residential rents have been *prearranged by local agree-*

ments between parties in special categories, the lease contract may run for three years and automatically renew for a two-year period. *Temporary* residential leases may have a maximum term of 18 months and must identify the temporary requirements of the parties to the lease. If no proof is given of the temporary nature of the lease, the lease may be extended to four years in length.

Nonresidential Lease Terms. The nonresidential non-hotel lease may run for a period not to exceed six years. Hotel leases, as an exception to the general rule, may run for a maximum term of nine years. If the conditions of the lease contract permit or if serious conditions exist, the tenant may withdraw from the contract before the lease term ends. The lease automatically renews unless the lessee gives notice at least twelve months before the end of the contract. The rent may be increased annually up to 75 percent of the ISTAT (assumed to be a government-maintained index such as the Consumer Price Index.). If the tenant engages in an activity that involves direct contacts with consumers, the lessor is entitled to a pre-emptive right if the landlord offers the property for sale.

Public Property and Cadastral Registers

When a property right is transferred, it must be registered in the Public Property Register. The person who first registers the property purchase in the Public Property Register is given legal priority over the person who later registers his purchasing documents. This helps settle conflicts between two or more people who think they have acquired the same property right. In case of conflict, priority is established by the date of registration. Registration of the title transfer gives public notice of the circumstances and transparency to the transaction.

According to Law 47 of 1985, the documentation of all purchases and sales transactions must give the number and date of the building permit or data concerning the associated administrative measures. Evidence of amendments or authorizations that permit change to the structure of the properties must be included.

The Cadastral Register (Registri Catastali) includes properties subject to taxation on the income from the land and buildings. The focus is on the income accruing to the property ownership. Construction plans are filed in the Cadastral Register, This register is referred to in contracts for the transfer of land for the legal description of the property. The Land Register (Registri Immobiliari), in contrast, focuses on the names of individual landowners. The index of the Land Register contains the names of individual landowners rather than individual plots of land. Both registries are maintained by the Provincia or district and are names Conservatorie dei Registri Immobiliari. The Ministry of Finance is liable for any damages that stem from errors in the information in the land register.

The information recorded in the land register includes:

- contracts transferring ownership
- contracts creating, transferring or modifying usufructs, surface rights or enfiteusi
- contracts creating or modifying servitudes
- contracts creating or extinguishing rights to use or inhabit land
- preliminary sales contracts lease contracts of more than nine years
- contracts creating companies, consortia or associations which confer property rights
- court judgments which create, transfer or modify any of such rights

Taxation of Italian Property

Three types of taxes affect the ownership of real property: real property taxes, corporate federal and local income taxation, and taxation at the time of property transfer.

Real Property Taxes. Since 1993, real property taxes are levied annually by municipalities on income from real property and based on the property's cadastral value. The rate varies from 0.4 percent to 0.7 percent, according to Ernst & Young. The Technical Tax Office applies the property assessment tariffs to the cadastral income associated with the property registered on the cadastral register to determine the amount of tax due. For properties that are not yet registered in the Land Register, the income of similar buildings already registered in the Land Register are applied on a comparison basis. Cadastral income is usually calculated by adjusting assessment tariffs, that are established by cadastral law, to the size of the property unit. The assessment tariff takes into account the municipality where the property is located, the locational zone within the municipality, the category of property within the municipal census zone, the class of property that refers to the income capacity of the properties with equal levels of value or quality, and the size of the property unit. If the property is rented to third parties, the gross income is assumed to be the larger of the two following amounts: rent resulting from the lease contract or the cadastral income. Then 15 percent of the income is treated as a non-fixed deduction for building operating expenses. Taxable income from special purpose buildings such as workshops and buildings built for the special requirements of industrial or commercial businesses is estimated from direct assessment of value by the Technical Tax Office.

•**Corporate Federal and Local Income Taxation.** The corporate income tax (abbreviated "IRPEG") rate is 37 percent. The local income tax (ILOR or imposta locale sui redditi) rate is 16.2 percent on the amount of income earned. The amount of the ILOR cannot be deducted from the amount of IRPEG paid. Therefore, the total corporate income tax rate for resident and non-residence companies is 53.2 percent, according to the Ernst & Young international accounting firm.

The approved method for calculating depreciation for income tax purposes is the straight-line method. Land is not depreciable. For the first three years of a land improvement's life, accelerated depreciation of up to two times the ordinary rate per year may be claimed.

Taxation at the Time of Property Transfer. Property transfers are subject to value-added, mortgage, and/or registration taxes. The value-added tax (abbreviated "VAT") rates depend on the types of transactions. If a residence is transferred by a building company, the VAT rate is 4 percent if a home is purchased for the first time and under special conditions; the rate is 10 percent for the purchase of non-luxurious homes; and the rate is 20 percent for the purchase of luxurious homes. If an entire building that does not have an exclusively residential nature is transferred by a building company or a company that has carried out renovation work, the VAT rate is 10 percent. The standard VAT rate is 20 percent, according to Ernst & Young.

If land upon which a building may be placed is transferred by a company, the transaction is subject to the value-added tax and the registration tax at the fixed amount of Lira 250,000 or approximately $110. If non-building land and non-agricultural land is involved, the value-added tax is not payable, but an 8 percent registration tax is payable. In contrast, the transfer of agricultural land by a company is subject to a registration tax of 8 or 15 percent depending on the purchaser. The transfer of buildings by a company is subject to VAT and a registration tax of Lira 250,000 which is roughly equivalent to $110. Transfers of buildings by private individuals in general are not subject to VAT, but are subject to registration tax of 7 percent, 3 percent if it is the purchase of a first home, and 3 percent if the properties reflect special historical, artistic, and archeological interest with a declaration of the special conditions by the purchaser. The registration tax is paid on the value of the transferred property.

Financing Italian Property

Italian property is usually financed by loans, leases, equity from real estate funds, exchange-listed securities, and syndicated equity offerings. The Banking Law of 1993 that followed the Second Banking Directive of the European Economic Community (EEC) of 1989 changed many banking aspects. All credit institutions are authorized to provide all types of credit services. All banking and finance activities are controlled and supervised by the Bank of Italy. Special provisions of the 1993 Banking Law apply to property financing or mortgage financing. For example, the medium or long-term mortgage loans should represent as a maximum 80 percent of the value of the mortgaged property or the construction costs associated with the property. Such a loan-to-value ratio may be raised to 100 percent when additional security such as a bank or insurance guarantee or a pledge of government bonds is provided. The mortgage loan terms range from 7 to 10 years, the repayment schedule has fixed and equal installments that provide for decreasing interest payments and increasing principal payments. Both fixed and variable interest rates are offered the customers. The loan interest rate may be indexed on the banks' prime rate or another similar rate. A number of German and U.K. mortgage lenders have entered the Italian mortgage market in recent years and have been successful in their lending.

Sale-leasebacks are used by businesses who occupy properties whose titles have been sold to investors and the space leased back. Usually the sale-leaseback may have provisions for the purchase of the property by the lessee at or before the end of the lease.

Both foreign and domestic real estate equity funds may provide property financing. For example, recently DTZ estate agents whose company headquarters is located in London sold Citta Mercato shopping center in Bussolengo, Verona to the new property fund of Credito Italiano. Other closed-end Italian real estate funds are:

•Valore Immobiliare Globale, sponsored by Deutsche Bank, 155 million euros, 15-year duration, that started up in 1998

•Piramide Globale, sponsored by Deutsche Bank, 258 million euros, 15-year duration, that started up in 1999

•Securfondo, sponsored by San Paolo IMI, 155 million euros, 15-year duration, that started in 1999

•Unicredito Immobiliare Uno, sponsored by Unicredito, 300 million euros, 15-year duration, that started in 1999

•Polis, sponsored by Banche Popolari, 258 million euros, 12-year duration, that started in 2000

•Portafoglio Immobiliare, sponsored by BNL, 250 million euros, 10-year duration, that started in 2000

•Alfa, sponsored by INPDAP-Mediocredito Centrale, 460 million euros, 10-year duration, that started in 2000

The Gabetti Group Research Department has estimated that the potential for real estate funds in

Italy for the full-year 2000 was 1.033 billion euros; the potential for 2001, 2.066 billion euros.

A number of real estate companies have listed shares; sale of the shares to Italian and foreign investors raises funds for property finance. Many of these companies have recently been spun off by Pirelli, Ent, Enel, Sao Paulo IMI Bank, and other large companies.

At the end of 2000, the supreme court of Italy decided that all fixed-rate mortgages with interest rates over 9.75 percent that were set before 1997 were usurious. The banks must cancel the contracts and pay back all interest payment received. About 70 percent of the mortgages negotiated by home-owners and banks are drawn up on a fixed-interest-rate basis. Many home mortgages had rates set between 10 and 18 percent until the mid-1990s when interests fell. To alleviate the financial alarm felt by the banks, on December 28, 2000 the Italian government cabinet decreed, as an emergency measure, that noone in Italy should be required to service a fixed-rate mortgage above 12 percent following the steep decline in interest rates in recent years.

Appraisal of Italian Real Property

Traditionally real property has been valued using the market comparison and the cost approaches. Some use of the income approach has been made particularly in recent years by the international estate managers and surveyors who have been valuing property in Italy. The use of discounted cash flow methods is becoming more widespread.

There are generally no laws covering property valuation in Italy except for case law related to the compulsory purchase of land and buildings. Only three professions that are associations with real property and construction are recognized: architects, engineers, and design technician/surveyors. Each of these professions have their own professional body. The professional associations (ordini) are associations that were instituted by Royal Decree in 1925. In the early 1990s, there were approximately 50,000 architects, 90,000 engineers, and 80,000 design technicians/surveyors (geometri). The surveyors (geometri) conduct real property valuations, certify real estate development projects, and may request building permits for property owners.

The real estate brokers are less well developed as a profession. From 60,000 to 70,000 active brokerage firms exist; their number tends to depend on the current stage of the real estate market cycle. In 1989 a law required six months attendance at a course including real estate valuation techniques in order for a person to perform the activities of a real estate agent. Only recently though has the appraisal instruction covered valuation of investment properties as well as the valuation of individual properties, i.e., houses and apartments.

The training and qualification of real property valuers tends to be at a beginning stage in comparison with the other advanced countries of the world. A number of valuation courses are offered at undergraduate and graduate schools including a Masters Degree program at Turin Polytechnic University.

An obstacle to appraisal work - non-transparency of real estate transactions - confounds real estate investment yield analysis, too. Italy has long been associated with tax-avoidance and corrupt societies. In recent years, with great governmental efforts, that association has been weakening. For example, tax collections have improved during the last few years; as the Italian government has strived to meet the European Union financial requirements, it has had to bear down on taxpayers for payment of legally required amounts of taxes. Another obstacle to efficient and timely appraisal practices has been appropriate data banks of timely and reliable information that is sponsored by real estate-related groups. Sources of construction cost, market prices, vacancy rates, insurance and management expenses, maintenance expenses, and income data are scarce and appropriate data limited.

Indications of Real Estate Investment Yields

Various international real estate sources indicate some generalized yields for the Milan and Rome office, retail, and industrial markets for recent periods. Some general conclusions might be reached first: Real estate prices have generally risen with average Italian employee purchasing power since 1963. The rise in real estate prices has far exceeded the cost of living since the early 1980s. There have been increasingly higher peaks in real estate prices over the real estate cycle since the early 1970s. The recent peaks in Italian real estate prices have been realized in 1991-1992, 1981-1982, and 1974-1975.

Evidence of increased professional in real estate investment analysis is the current existence of the Italian Society of Real Estate Counselors and Investment Advisors whose leadership is international in nature. Other evidence is the work of the international real estate agents in the major Italian markets.

Office Building Yields

Since office buildings are the prime investment property type that is continually under scrutiny by international real estate investors, let us turn to revealed yields in this sector. In mid-1999 office yields in Rome and Milan were estimated to range from 6 percent in the central business district to 7.5 percent in the outlying areas. In early 2000 Milan office yields were estimated to be 5.25 to 5.5 percent. Similar office yields were estimated for the Vienna, Geneva, and Berlin markets. The growth rate of the prime office rent index was relatively low in comparison with the prime office rent growth rate of the 1990-1992 period, according to Healey & Baker.

Retail Property Yields

As of mid-1999 retail property yields of Rome were roughly 5 percent in the central business district and 6.5 percent in the locations further out from the city center. At the same time, the retail yields of Milan's central business district were approximately 4.75 percent and 6 percent in the outlying areas. Then in early 2000, the Milan total retail market yields were estimated between 4.5 percent and 5 percent. Milan's retail yields, at the same time, approximated those of Vienna and Dublin. The Milan's yields were half of the retail yields experienced at the same time in Prague and Warsaw.

Industrial Property Yields

Since industrial property yields often generate higher yields than office and retail property yields, we may note that, in mid-1999 the industrial yield was estimated at 9.5 percent in Rome and 9 percent in Milan. In Milan's industrial market, yields had dropped to 8 percent to 8.5 percent by early 2000. At the same time, industrial yields were similar in Stockholm, Barcelona, Brussels, Copenhagen, and Frankfurt, according to the combined research of several leading international real estate companies. According to Healey & Baker, the prime industrial rent growth rate was relatively high in the late 1990s based on the Healey & Baker index of prime industrial rental growth for annual periods.

Conclusions

Due to its real estate growth potential and its rising international country credit rating, Italian real estate is an excellent candidate for investors who are seeking diversification within the European Union. This 17th ranked country among the 145 countries whose country credit ratings are published by the editors of Institutional Investor magazine - exhibits relatively low office rents, promise of rising office rents, scarce modem commercial and industrial buildings, a strengthening currency as the Italian lira changes to the euro in January, 2001 and relatively low interest rates and inflation. There is a continuing stream of property offerings from large multinational and local companies who are diversifying their portfolios based on recent legislative actions and continuing privatization programs.

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About the Author
and
Background for the Manuscript

ITALIAN REAL ESTATE FOR SALE

Dr. M.A. Hines

International investors are scrutinizing the Italian real estate market as they are attracted to the economic development of Europe. As they analyze world real estate markets for potential opportunities, they may want to notice the new attractions of the Italian market. The author, Dr. M.A. Hines, the Clarence W. King Endowed Professor of Real Estate and Finance of the Washburn University School of Business, Topeka, Kansas has traveled again to this advanced economy to review the international real estate potential of this country of 60 million people, that is a member of the European Union and the European Monetary System. As the country changes to total use of the euro in year 2002, the currency risk diminishes within the European Union.

As a long-term member of the International Real Estate Institute, Dr. Hines has contributed numerous manuscripts for articles, books, and monographs for the worldwide membership since 1983. At the 1986 World Congress in Vienna, the IREI leadership gave Dr. Hines an award for service to the Institute.

Her book, INTERNATIONAL INCOME PROPERTY INVESTMENT, and her monograph, JAPANESE SHOPPING CENTERS: FINANCIAL AND INVESTMENT FEATURES, were published by the Institute in 1985. The monograph, AN OVERVIEW OF GLOBAL REAL ESTATE FINANCE, was originally published in 1989 and revised in 1995 and 1999. Recently the Institute published two of her manuscripts in monograph form: BRAZILIAN REAL ESTATE, in 1999, and MOROCCAN REAL ESTATE: NORTH AFRICAN PROPERTY, THE IMPACT OF &PROPERTY ON INTERNATIONAL REAL ESTATE, and INVESTING IN JAPANESE REAL ESTATE: LINKS TO INTERNATIONAL TRADE, in 2000.

Dr. Hines is the author of 45 books and monographs including four major real estate textbooks. Seventeen books and monographs of the total deal with international real estate topics. In addition, about 75 of her 112 refereed and professional articles involve international real estate, international trade, and international business in general.

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