

INTER news



January 2014 Edition

**What is happening
in the Real Estate
Market in the Sharon
area and why now**

**How will our Silicon
Valley continue to
thrive**

**What will happen
in the Office Market
through 2016**

Recipe for Success

**The Man Who Established Commercial Real
Estate in Israel – past, present and future**



**Dear Readers,**

Haifa's southern industrial parks continue the path of continuous growth. Adjoining the original Matam Park, a similar, new Life Science Park is planned by Industrial Buildings Corporation. Melisron's Sha'ar HaCarmel as well as adjacent buildings in Tirat HaCarmel, continue to benefit from the attractiveness of the Matam Park site. In our article, we have tried to explain why so many international companies coming to Israel establish their R&D center at this location.

We have seen volatile prices in the Sharon area over the past half year, especially in Kfar Saba and Netanya. In this newsletter we have analyzed the business parks in the Tel Aviv area and we have worked to clarify the reasons for pricing movement in the Sharon in respect to price stability in the Gush Dan area.

Also in this newsletter - a review of the expected three year demand in office space in the Tel Aviv area. At this moment, prices and occupancy rates remain unchanged.

And a personal "blowing our own trumpet": our lead article follows the career of Adrian Blumenthal, who 40 years ago established a professional commercial real estate market in Israel.

Enjoy your read!

Yoram Blumenthal
Partner, Inter-Israel

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Senior Editor: Yair Kachel
Managing Editor: Avriël Ben-Dor
Researcher: Marissa Kerzner
Production: Naama Ochanun
Language Editor: Danny Geva
Graphic Designer: Studio Orna Cohen
Statistical Oversight: Rami Yulazri
Production Editor: Yair Kachel PR Ltd.
Translator: Ari Itzkowitz, Lion H.I. Consulting Ltd.

Inter Israel Real Estate Consultants

15 Abba Hillel Silver
Ramat Gan
research@inter-israel.co.il
www.inter-israel.co.il

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The Stormy Sharon

Falling prices in Netanya, rises in Kfar Saba, new deals in Herzlia • A summary of the office rental market in the second half of 2013

In this report, we have analyzed supply and demand for office space in different geographic areas for the entire second half of 2013 and expectations for the coming year. We have collected data on rental pricing and occupancy rates among offices in nine individual areas, from Netanya in the North-Central Coastal Region to Ness Tziona and Rehovot in the South-Central Coastal Region. Our data indicates continued overall stability in the office space market, with a slight 2% decline in average office rental prices from NIS 49.7/sq.m. to NIS 48.8/sq.m. The slight decline in rental prices has not had any real effect on the balance between supply and demand for these areas.

Areas where rental price changes stood out include Netanya, with a sharp fall of 9%, Rosh Ha'ayin, declining by 5%, and Petach Tikva and Rana'ana with falls of 5% each. In contrast, we observed in Kfar Saba a 4% rise in the past six months (completing an 18% rise in the past year). We observed no real change in the areas of Ness Tziona – Rehovot, the Ben-Gurion Airport area, Herzlia and Hod Hasharon.

Occupancy analysis by area:

Petach Tikva – Petach Tikva has been exposed to rising levels of competition from Kfar Saba and Hod Hasharon for the past year. In addition, heavily aggressive marketing, both from Amot and local developers, to increase interest in their Petach Tikva projects, have come to fruition in the current half, and is reflected in a number of significant deals: Occupancy of the area formerly occupied by Lucent Alcatel in Park Azorim, and noteworthy advances in occupancy of the Amot Platinum Building. On the other hand, there are a number of projects where occupancy has failed to advance for many months.

Rosh Ha'ayin – Occupancy rates continue to decline, with rental prices falling a further 5%. Though there are initial signs of life with some deals underway, the local Park Afek business district is still best categorized by companies in distress with heavy layoffs (each employee is equivalent to 15 sq.m. of gross space, and therefore the layoffs of hundreds or thousands of employees is a huge strain on the real estate market). Closing of Better Place released about 10,000 sq.m. to the market, with 2,000 sq.m. now occupied.

Ness Tziona – Rehovot – These areas continue to enjoy stability and very high occupancy rates. Collaboration between the Weizmann Institute and the Science Park continues to attract medical research companies to the area, driving the overall attractiveness of the area. Rental prices have remained steady at NIS 48/sq.m./month for the past six months.

The Ben-Gurion Airport Area:

Airport City - underwent two dramatic changes. HOT vacated a building of 10,000 sq.m. and moved to Yakum. Egged will shortly vacate a similar sized building and relocate its management to Beit Dagan.

Or Yehuda - El Al has completed relocation of its call center to the local Terminal Park Project and the entire Stage A has been fully marketed. Marketing of Stage B is commencing.

Lod - The area continued to stagnate this half, continuing its decline on the list of desirable locations in the center of the country.



The Oshira Project, Kfar Saba

The Sharon Region:

Herzlia - continues to be stable, with high occupancy rates and high levels of demand. In the six months under review, there were a number of large transactions and an increase in the number of global players with locations in the area. These deals reflect the demand and prestige value of the area.

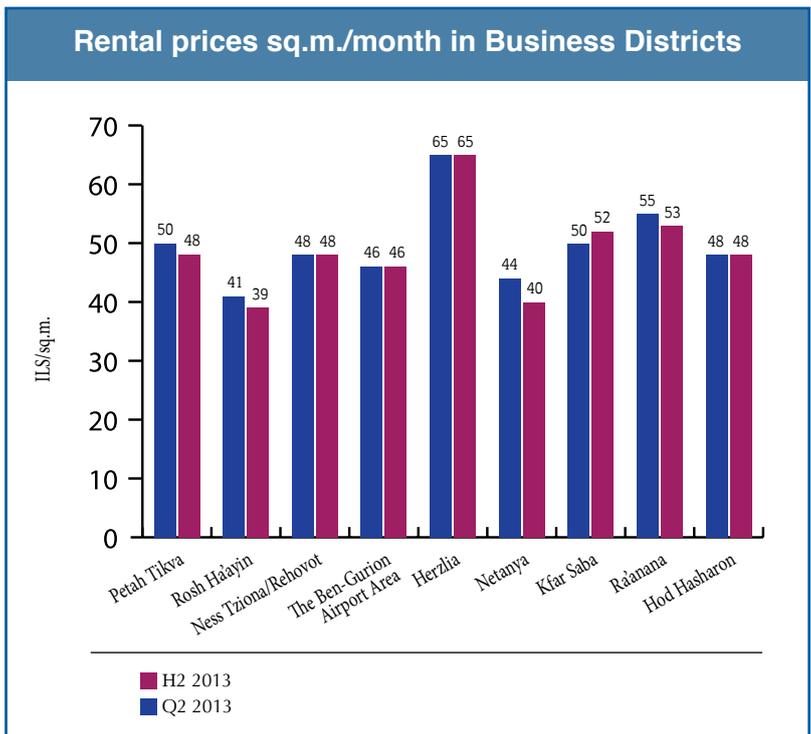
The Netanya market continues to gain interest especially with falls in prices which have led to the closing of a number of transactions over the past six months - for example, Cost 365 of the Hamashbir Group, occupying 2,800 sq.m. in Park Ogen. Other deals include Gadot Chemicals, Telram, SMEG, and SCR, which is renting 7,000 sq.m. in Ramat Poleg.

Ra'anana - A slight fall in prices in this city that benefits from its "big sister" Herzlia Pituach and is slowly beginning to feel competition from Hod Hasharon and Kfar Saba.

Hod Hasharon - Prices were stable in the second half of the year, and we expect a rise in the rank of Hod Hasharon in the list of general demand in Central Israel. As witness to this, Ashtrom has decided to construct a third tower in its industrial park in Hod Hasharon.

“Figures point to continued overall stability in the office rental market, with a slight decline of around 2% in average office rental prices”

Kfar Saba - In the second half of 2013, rents rose from NIS 50/sq.m./month to NIS 52/sq.m./month on average. The price rise was driven by high demand and the area's rising attractiveness as an industrial location and a serious alternative for corporates considering relocation or expansion in Ra'anana or Herzlia Pituach.



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Years of Commercial Real Estate in Israel

Israel's oldest and most important real estate consultancy is celebrating its fortieth anniversary of partnering with all leading high-tech and industrial corporations, most leading local institutes, global players, foreign governments, and a strategic alliance with the leading international real estate firm Cushman & Wakefield. It all began with a clerk at the absorption ministry who said to Adrian Blumenthal, our founder, when he immigrated to Israel, "real estate is not a serious profession in Israel"



The year: 1967, prior to the outbreak of the Six Day War, Adrian was still living in London. BBC television documentaries were showing scenes of Tel Aviv discos with the caption to viewers: "look well – this place may not be around in two weeks-time."

Like many young people, this scenario had a profound influence on Adrian, who shortly after was en route to Israel and a job in the export department of Osem – one of Israel's principle food producers, with a branch office in London.

When later on in his career, Adrian

decided to move to the Real Estate field and needed to process his immigrant visa, a clerk at the Absorption Ministry reacted that "Real Estate in Israel was not a serious profession". Adrian's Father recommended otherwise, explaining that Real Estate was the engine that drove modern, Western economies and undoubtedly as Israel's population and modernization grew, so would the sophistication of its economy.

In 1971, Adrian joined a large residential Real Estate firm, setting up within the Company a commercial department. Two years later, Adrian had left this Firm and established

Inter Israel, specializing in commercial real estate. That year marked another significant turning point in Israel's history, the Yom Kippur War.

Inter Israel established its first office in the El Al House, the most modern building of its time, where we remained for 14 years. "The main problem was receiving telephone lines. We were promised three lines and just when the office was ready for opening, found we had none. Fortunately our friendship with the International Red Cross and the Pilz Concern, both tenants in the Building who generously gave us phone lines from their bank of lines, enabled

us to set up shop on the seventh floor on time in March 1973.”

“When we started in business, a leading Tel Aviv law office would typically be located on a third floor walkup with no elevator. How things have changed!”

The need for a business-oriented agency proved itself and the office soon became the industry leader. The first clients were foreign embassies and overseas airlines such as Air France, British Airways, Lufthansa, Swissair, Singapore Airlines and Olympic. Technology companies were scarce at the time.

“At that time, apart from Shalom Meir Building, referred to as the Shalom Tower, also widely known as Israel’s first skyscraper, there were hardly any office buildings in Israel”, tells Blumenthal.

“The face of the market changed completely with the advent of Asia House, built by the Eisenberg Concern, one of the early flagship projects marketed by Inter Israel. It all started with our negotiating a rental of 220 sq.m in the building to the International Committee of the Red Cross. As a result of this anchor tenant, we negotiated on behalf of many other Embassies space in the Building.”

Unfortunately some of the other older office buildings such as the El Al House, have deteriorated and aged. In New York and London, vintage buildings such as the Empire State Building, which retains its prestige even today, are restored and renewed.

“A preference to allow the decline of long-standing buildings in favor of new projects”

However, with the shortage of land in Israel, iconic, long-standing structures are allowed to decline in favor of new, modern, “green” and “user-friendly” officer towers.

“In 1978, following the peace accords with Egypt, many Governments required embassy premises, particularly

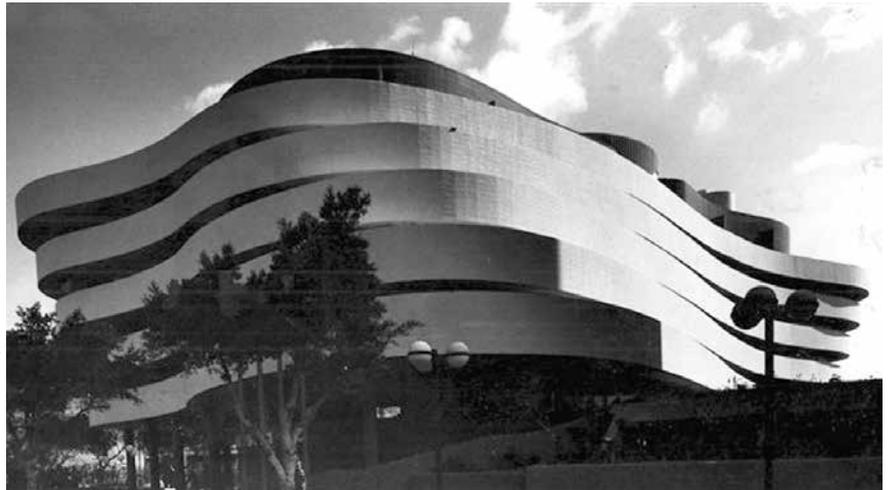


Photo courtesy of the Late Pavel Gross

Asia House, 1970

along Tel Aviv’s Hayarkon Street, with the Egyptian Embassy establishing temporary premises, followed by Jordan and others. On meeting with the Jordanians after they crossed the Allenby Bridge, we began searching for embassy premises in Israel. On a tour of Tel Aviv one of the members of their delegation was insulted when I didn’t recognize him – apparently he was the news anchor for Jordanian TV news in Hebrew!” reminisces Adrian.

Before the construction of the Ayalon Highway Ben-Yehuda and Dizengoff Streets were Tel Aviv’s Central Business Districts. Prices were measured in millions of lirot. “Inter Israel was very active in the diplomatic sector because the global institutions were not yet present. Israeli entities were only beginning to recognize the added value of utilizing a real estate advisor, and the market was rather immature and not yet in need of such a service as today.”

Blumenthal: “Inter Israel continued its market expansion throughout the 80’s while Israel’s economy went for a wild ride. During the ‘Merry Aridor

Days’ when former MK Yoram Aridor’s financial policies led to skyrocketing inflation, the real commercial estate market continued to rise and Israel

Inter Israel established its first office in the El Al House, the most modern building of its time

began to make its mark on the global high-tech scene. We were chosen to represent Cisco’s vast expansion plans in Israel, leading to a significant increase in our operations.”

During the 90’s, Yoram Blumenthal, the next generation, joined the office and Inter Israel joined up for the first time with an international real estate firm, Healey & Baker, which afterwards merged with Cushman & Wakefield (our partner today) to become a leader and best-in-class in the commercial

real estate field. Yoram joined Inter Israel in 1995, three years following his discharge from the Israel Defense Forces and following his studies in economics and management and time spent in the London office. The Company was highly successful, offering a high level of advisory services.

“When Cushman & Wakefield acquired Healey & Baker, we in turn became their associate office and subsequently Alliance Partner in Israel. This is a Company with activities on every continent. It became a prerequisite to align our services with the firm, such as a complete involvement with every real estate transaction of our clients,” says Adrian, adding, “including organizational support for all accompanying real estate processes, negotiating return of leased areas to landlords, space reduction, office relocation, subletting, sale and leasebacks, lease admin, financial modeling, integration of the global corporation with the local staff and many other areas of involvement.”

With the transition of Israeli companies to the international marketplace, Inter Israel has also seen a reverse trend – to provide the headquarters of Israeli corporations with the ability to manage their global

property portfolio. Inter Israel counts among its international clients HP, Cisco, Teva, Analog Devices, Akamai, GE, Qualcomm, Credit Suisse, Goldman Sachs, Boeing, the Azrieli Group, Gav Yam, Morgan Stanley, Deutsche Bank, Migdal, Clal, Kardan and Dell.

“Inter Israel’s secret of success is comprised of human capital and professionalism. The company has a low



Before the construction of the Ayalon Highway, Ben Yehuda and Dizengoff Streets were the central business districts. Prices were measured in millions of lirot

rate of employee turnover. Many of our consultants have been with us for 16-17 years. Their motivation, attention to client needs, attention to detail, depth of understanding and of the clients’

real need – sometimes even better than that of the client themselves, is what has transformed us into a leading real estate service company,” explains Adrian.

“The real estate service sector still has a way to go to achieve real professionalism. Unfortunately, there are many entrepreneurs in Israel who do not effectively rely on real estate consultants and believe they know best. Foreign companies in developed markets have understood for decades the need for professional help in this area. There will be greater integration with global markets and we will incorporate further levels of service as this sector develops. We already utilize services provided by Cushman & Wakefield that are not yet available in Israel. We see our clients reducing or closing their asset management departments and outsourcing these functions, especially in areas of A-Z consulting, including economic analysis, component valuation, future asset needs, market evaluations, etc. We have become part of companies’ decision-making processes and not only at the advisory level. Today, the name of the game is saving and optimizing and our clients see us as a vital component in this creation of value,” summarizes Adrian.

Our Own Silicon Valley

What is the secret of success of Southern Haifa's industrial parks, which are prospering and which are declining

● Why does every international name insist on establishing a center there and do they have an alternative

It appears that the secret of success of the Southern Haifa's high-tech areas is similar to that developing in Beersheba: a combination of proximity of leading academic institutions (The Technion and Haifa University), government incentives (formerly listed as a National Priority Area A), excellent access to transportation such as the national railway and the central bus station, and near a metropolitan center. These anchors bolster the attractiveness of all the companies in the area and assist in recruitment of relevant quality manpower whilst also attracting other

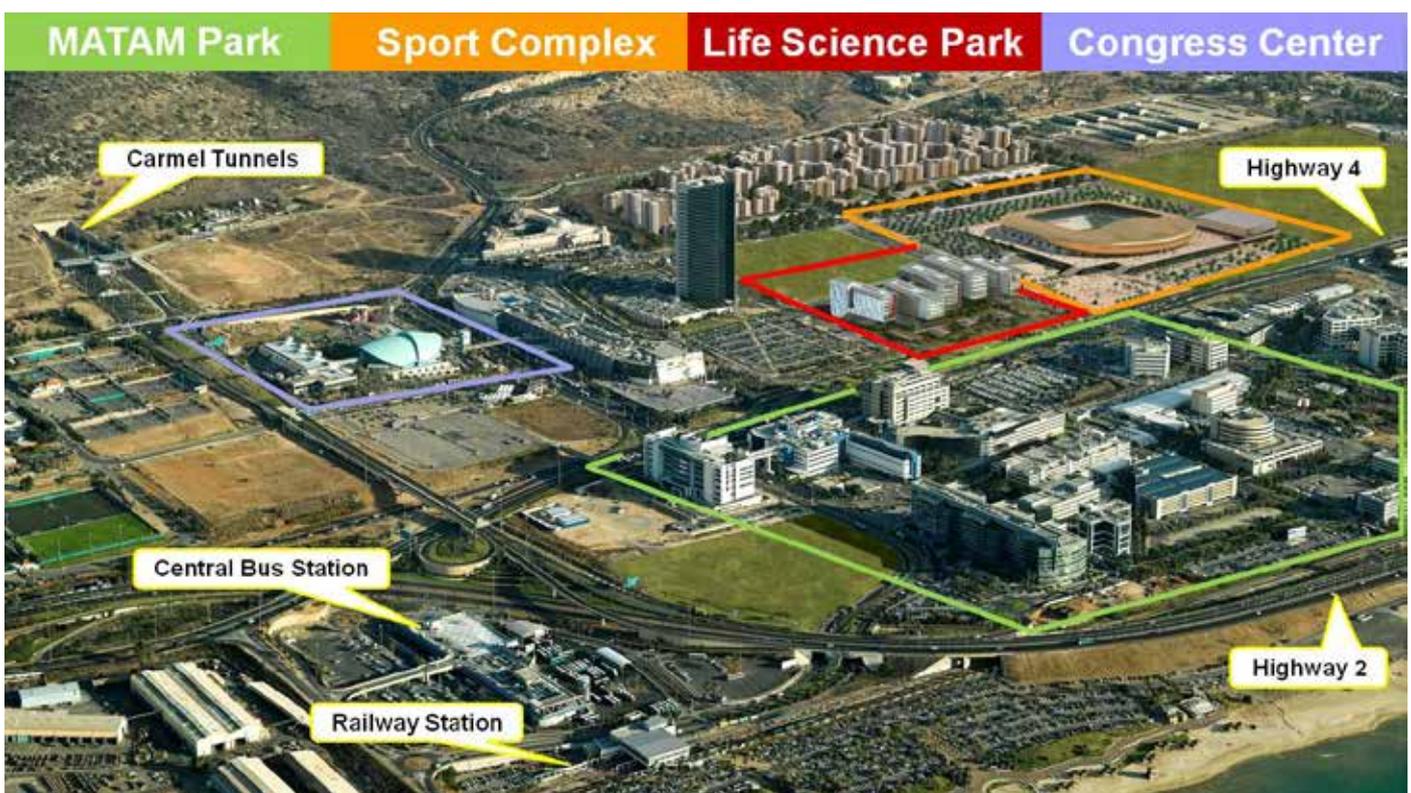
dominant players and research and development centers in technology and sciences. The popularity of the Haifa area seems to have snowballed and created its own attraction: every significant institution already on site, mainly at the Matam park acts as a magnet, with many newcomers to Israel also feeling the need to be there.

The first to rush to set up business in the South Haifa area were the giant internationals such as Microsoft, Intel, Elbit (Israel), IBM and Philips, all in the Matam Park belonging to Gav Yam and the Haifa Development

Company. GE set up in Tirat Carmel, a nearby smaller center, also housing MED-1, specializing in technology and communications and the starting point of Israel's undersea internet cable.

The Israel Electric Corporation also set up its office headquarters in southern Haifa, across from the Matam Park. A new adjacent industrial park is due to be set up by Industrial Buildings Corporation, which will at least initially specialize as "A Life Sciences Park", though it is no longer certain that this will be its sole area of activity.

Other principle anchors that have assisted in Haifa's regional development include proximity to the Carmel Tunnels, allowing easy access to residents of the Carmel and the surrounding Krayot suburbs, as well as the development of a convention center planned to include a business hotel. As Matam has become crowded,



Matam Park

Illustration: Moshe Zur Architects



A new project, Matam, Haifa

individual firms have relocated to a smaller area south of Matam called Sha'ar HaCarmel, under the ownership of Melisron.

The southern Haifa area has seen the establishment of many joint projects between international corporates and Israeli science institutions. These include Qualcomm and Intel with The Technion, and IBM with the University of Haifa where it established an R&D center within the campus grounds on the Carmel. Over the past ten years, other significant corporations including Yahoo, Google, Apple and Zoran, have set up shop in the southern Haifa area, allowing for easy access to high quality engineers.

Whether on purpose or not, the Matam Park, jointly owned by Gav Yam, who manages the park, and Haifa's Economic Development Company, owned by the Haifa municipality, has become the leading industrial park in the area even though only half of the permitted development of the site has already been completed. International technology companies do not really have an alternative site in the area with the same standard of construction or developed areas, such as access to childcare, synagogues, shopping, postal services, banks, well maintained green areas, lighting, cleanliness and administration. The entry of the Industrial Buildings Corporation to the

area will be a major change and it will be interesting to follow developments over the next few years.

Matam is undoubtedly the lead industrial park in the southern Haifa area, leading nearby companies to advertise themselves as if they were also located at Matam in order to bolster their image, even if not in the park itself. This has transformed Matam into a unique business park in south Haifa as other parks in the area cannot yet match its quality of services and infrastructure. In addition to the companies previously mentioned, other companies located at Matam include CSR (previously Zoran), Philips Medical and Microsoft. Occupancy rates reach 95%, with only 2,000 to 3,000 sq.m. currently available.

According to our data, Matam covers 270,000 sq.m. of land and rental prices in new buildings range from NIS 50-55/sq.m. while existing buildings reach NIS 60-65/sq.m. Gav Yam has recently announced the expansion of Microsoft to an additional 7,400 sq.m. in a new building. Gav Yam currently has two new buildings under construction. The first building will be ready for occupancy in November 2014 while the second building will be ready in the summer of 2015. Monthly rental prices are currently NIS 52/sq.m.

While the area no longer qualifies as a National Priority Area, it continues

Yokneam is a National Priority Area and a great example to governmental decisions that have proven themselves. There is practically no available commercial or industrial space and construction of new projects continues unabated

to develop and thrive. We can credit government assistance for positively promoting this area. The result – once development reached a critical mass, government assistance was no longer required.

Another mini-park located to the south of Matam is Sha'ar HaCarmel. This is an area comprising three buildings, built to the south of Matam but within the municipal boundaries of Tirat HaCarmel. At the entrance to Tirat HaCarmel are several additional buildings to which the Municipality is trying to attract high-tech companies, but as yet without much success. Infrastructure in the area, including

Illustration: Lir Architects



The Crytek B project in Yokneam

these buildings, is not sufficiently developed for the high-tech industry. The almost singular exception is GE, located in the Tirat Carmel industrial park, 1.5 km south of Matam and Sha'ar HaCarmel. Although this area also houses the MED-1 transatlantic internet anchor, controlling Internet traffic from Israel to the world, the location is not considered relevant for other high-tech or major companies.

The Life Sciences Park (Industrial Buildings Corporation) is planned to be constructed by Haifa's Municipal Development Company in partnership with the Industrial Buildings Corporation in the southern region of Haifa adjacent to Matam. The Park will cover 31 dunams (31,000 sq.m site area) and is expected to include 85,000 sq.m. of construction, customized to the companies leasing the space. The Park is planned to specialize in life sciences and infrastructure will be tailored accordingly.

Companies have no attractive alternative in the area of Matam both in terms of the level of construction as well as the level of development of the area

The Closest Alternative – the Yokneam Industrial Park

- Yokneam is the main regional alternative for high-tech and biotech companies, at a distance of only 22 km from Haifa. It is also a short distance from the Trans-Israel Highway 6.
- The largest companies present are: Syneron Medical, occupying 37,000 sq.m., Marvell, with 30,000 sq.m., Lumenis, with 16,000 sq.m., Dexcel Pharma, with 15,000 sq.m., and Given Imaging (recently acquired for \$860 million by the medical device giant Covidien), occupying 12,000 sq.m.
- A number of companies are located at the old Mordot HaCarmel Industrial Park, focused more on manufacturing and including the Osem and Keter plants. There is much less of a “high-tech” atmosphere in the infrastructure, layout and landscaping and the area is littered with old-fashioned facilities.
- The new park, the Mevo Yokne'am Industry Park, located closer to Tivon, is much more developed with a more “high-tech” feel. Organizations located here include Syneron, Lumenis, Dexcel and Given Imaging. Occupancy rates exceed 90% with very limited remaining available space.
- Yokneam currently has three projects under construction, totaling 27,000 sq.m. The largest is Crytek B from Industrial Buildings Corporation and all three projects are located at the Mevo Yokne'am Industry Park. Initial occupancy is scheduled for the first quarter of 2014. Monthly rental prices in existing buildings in the new industrial area are around NIS 60/sq.m. and in new projects under construction, between NIS 42 to NIS 50/sq.m. Yokneam is a National Priority Area and a great example of successful governmental policy. There is practically no available commercial or industrial space and construction of new projects continues unabated.

Office Rental Market Maintains Stability

In the second half of 2013, the office rental market in the Central Business Districts continued to show stability in demand, occupancy rates and rental prices; will forecasts of price drops from an expected large increase in inventory from new buildings be realized and what are our forecasts for the next three years

Our survey for the second half of 2013 encompasses office space “stock” totaling 2.2 million sq.m. in 129 office buildings in the greater Tel Aviv area, of which 62 buildings were analyzed in depth. Tel Aviv includes 6 business district – Rothschild, Shaul Hamelech, the Coast, Menachem Begin, Yigal Alon and Ramat Ha’hayal. In addition, we have analyzed the Diamond Exchange area and the BBC (Bnei Brak Business Center) area which is adjacent to Ramat Ha’hayal.

Continued Market Stability

During the third and fourth quarters of 2013, occupancy rates have remained practically unchanged at 97.5% on average. Also, average monthly rental prices remained at NIS 97/sq.m./month, excluding Bnei Brak and Ramat Ha’hayal (where the calculated price falls to about NIS 91/sq.m./month).

Rothschild Boulevard retains the highest rental prices, maintained for the current period at NIS 111/sq.m./month. Following this is Shaul Hamelech, maintaining a similar NIS 110/sq.m./month on average. The Menachem Begin area has fallen by a negligible 1% to NIS 99/sq.m. from NIS 100/sq.m. on average. Yigal Alon remains without change from the second quarter at NIS 98/sq.m./month. The Diamond Exchange area also remained unchanged at NIS 85/sq.m./month while in Bnei Brak, there was a slight drop from NIS 74 to NIS 73/sq.m./month. Along the Coast rentals remained unchanged at NIS 78/sq.m. similarly Ramat Ha’hayal at NIS 72/sq.m. on average.

Growth in occupancy rates during the second half of 2013 declined to 5,000 sq.m. from 33,000 sq.m. in the first half of the year. Therefore the annual rate stood at 38,000 sq.m., a

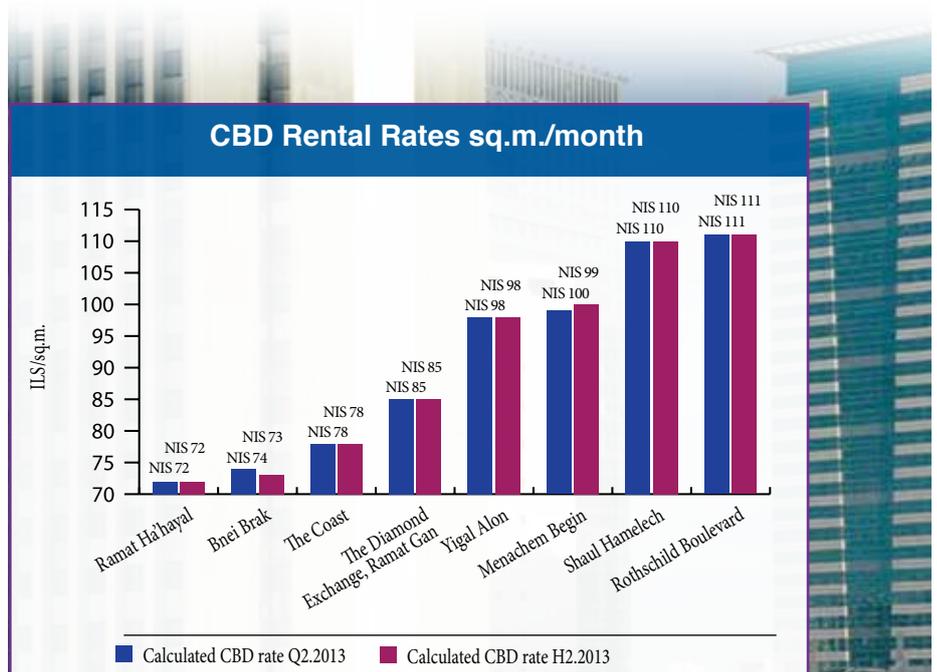
Growth in occupancy rates during the second half of 2013 declined to 5,000 sq.m. from 33,000 sq.m. in the first half of the year

significant decline from the multi-year rate of 95,000 sq.m. It is still too early to decide whether this marks a trend change.

Overall, we can say the office rental market continues to maintain stability, with high levels of occupancy. The business districts of Ramat Ha’hayal and the BBC have increasingly become an attractive alternative to the central business districts of Tel Aviv and are attracting significant business institutions.

Our Forecast Upto 2016

In addition to analyzing the central business districts, we have also analyzed expected market developments for the period 2014 to 2016, with interesting results. During 2014, we expect office completions of 64,000 sq.m., a relatively modest increase in office space inventory. When calculating the multi-year average for 2013 and 2014,



we find an average addition of 104,000 sq.m. of office space per year for these two years.

During 2015, we expect an additional increase of 95,000 sq.m. in office space inventory. The main thrust of office space completions is expected to occur in 2016, with the addition of 200,000 sq.m. of office space, largely (about 85%) in Tel Aviv and the remainder in Bnei Brak.

Thus throughout the three years of 2014 to 2016, about NIS 360,000 sq.m. in office space will be added, or an average of 120,000 sq.m. per year. As the Take-Up rate from a macro viewpoint averages only 90,000 sq.m., we expect to see a surplus of around 90,000 sq.m. of office

space by the end of 2016. It is important to point out that future occupancies are based on analysis of expected trends in the market and not based on any knowledge of specific demand.

Consequently, we expect 2017 to begin with a surplus of 90,000 sq.m. in the office rental market. Still, the large challenge will actually arrive during the course of the year as an unprecedented 400,000 sq.m. of space enters the market. Marketing of such a large quantity of space, from our experience, will require about four years of take-up, if accounting for an assumed reasonable rate of market growth similar to the previous decade.

The result of these numbers means

that in the next three years, there will be many pricing pressures, reaching a peak in 2016–2017, if projects are not delayed or cancelled. We expect intense fighting over the marketing of new projects, with many incentives to be offered to lessees (upgrades to infrastructure, terms, etc.) as well as discounts, as a function of the differential of supply and demand according to location.

We expect prices to gradually decline by 15% as we arrive at 2017, providing opportunities in the coming years for lessees and upgraders. We fear that developers without proper financial planning and aggressive marketing skills could find themselves in an unpleasant situation.

