LaSalle Investment Management

Real estate experience. Investment expertise.

European Regional Economic Growth Index E-REGI 2010

The outcome of the 2010 E-REGI reflects the aftermath of the global financial crisis, which is characterised by a sluggish economic recovery and sharp regional disparities.

London is back at the top of the ranking. With the trough passed in 2009, the city's dynamic economy is bouncing back strongly. E-REGI further favours wealthy locations with strong fundamentals, such as Paris and Munich, which outperform in a low-growth environment.

After making a spectacular entry into the E-REGI in 2009, Moscow continues to score strongly and now ranks second. The result clearly reflects the size and exceptional growth platform of the city region, but fails to conceal deficiencies in other, risk-related aspects of the ranking.

In the highly selective and fragile recovery of 2010, it becomes clear that uncompetitive locations are falling behind as they can no longer rely on national momentum to sustain their growth. Therefore, weak locations even in traditionally strong countries, such as Germany, France and the UK, clearly suffer in this year's ranking.

Conversely, emerging regions catching up from a low base perform relatively better in an environment where economic growth in more mature countries tends to be below trend.

Executive Summary

European Regional Economic Growth Index (E-REGI) identifies those cities across Europe where demand for real estate is likely to be strongest in the medium term. As such, E-REGI provides investors, developers and occupiers with a guide to the likely medium-term winners and losers in Europe. Our analysis complements more qualitative approaches and is a valuable tool when combined with detailed real estate knowledge, notably on the supply side, and relative pricing.

Headline Results

- The E-REGI 2010 covers 297 regions across 32 countries in Europe with a total population in excess of 660 million. Five Ukrainian city regions have been added to the model to reflect their growing importance in Europe. The analysis focuses on a subset of 104 major cities (locations with ≥500,000 inhabitants) plus all national capitals.
- The outcome of the 2010 E-REGI reflects the aftermath of the global financial crisis, which is characterised by a sluggish economic recovery and strong regional discrepancies. E-REGI continues to favour wealthy locations, such as the Swiss and Nordic cities, and those city regions that benefit from strong fundamentals, allowing them to outperform in a low-growth environment.
- London, which had lost its top position and slipped to rank no. 8 in 2009, is back at the top of the ranking. The financial crisis had a serious impact on Europe's largest financial centre, resulting in dramatically lower GDP and employment growth expectations. With the trough in 2009 now behind us, this dynamic city is bouncing back strongly.
- After making a spectacular entry into the top 10 in the E-REGI in 2009, Moscow continues to score strongly and now ranks second. This result clearly reflects the size and exceptional growth platform of the city region, notwithstanding a challenging business environment.
- As a result, Munich has lost its position at the top of the ranking and is now on rank 3. The city outperformed its competitors on the back of sustained growth forecasts, owing to a competitive and diverse economy with a strong commitment to innovation. Germany is also the country with the highest number of city regions in the top 20 (four), highlighting the relative robustness of the economy.
- Paris maintains its position in the top 5, only marginally behind Munich. This was achieved through its diverse economy and high wealth levels, which offset any relative slowdown in growth in the aftermath of the crisis. France is generally well represented in the top 20 with three locations, albeit largely in the south of the country, highlighting the selective nature of this nascent economic recovery.
- The 2009 E-REGI penalised Spanish and CEE locations for the excesses in their respective countries in the recent past. In 2010, it becomes clear that uncompetitive locations are falling behind in a weak growth environment as they can no longer benefit from national momentum.
- As a result, weaker locations even in traditionally strong countries such as Germany, France and the UK clearly lose in this year's ranking.
- It has become possible to include a number of Tier-1 Ukrainian locations in the E-REGI 2010. As is typical for emerging markets, the Ukrainian scores are almost entirely driven by growth – not dissimilar to Russia. However, their growth platform clearly reflects the secondary nature of these locations in a CEE context and they score exclusively in the lower half of the ranking.

Top 20 E-REGI Rankings 2010

1.	London	↑
2.	Moscow	↑
3.	Munich	↓
4.	Paris	↓
5.	Stockholm	↓
6.	Oslo	↓
7.	Gothenburg	↑
8.	Copenhagen/Oresund Region	↑
9.	Zurich	↑
10.	Luxembourg	↓
11.	Toulouse	↑
12.	Vienna	↑
13.	Stuttgart	↓
14.	Helsinki	↓
15.	Bern	↓
16.	Geneva	↑
17.	Mannheim-Karlsruhe	↓
18.	Utrecht	↓
19.	Lyon	↑
20.	Frankfurt	⇔

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E-REGI

LaSalle Investment Management has developed a quantitative model, the European Regional Economic Growth Index or E-REGI[1], to help identify the cities and regions across Europe that have the greatest economic growth potential over the short-to-medium term, and hence where demand for real estate is likely to be strongest. E-REGI complements more qualitative approaches and is a valuable tool when combined with detailed real estate knowledge.

This paper presents the latest results from the E-REGI model, and is the twelfth consecutive annual iteration of the service. The coverage of the model is continually updated to take into account current and anticipated market developments. The 2010 model covers 297 regions across 32 countries in Europe with a total population in excess of 660 million. As data availability is improving, it has now become possible to add five Ukrainian city regions to the model in order to reflect their growing importance in Europe.

The analysis is focused on a subset of 104 major cities, representing the locations with ≥500,000 inhabitants, plus all national capitals. The full ranking is set out on page 9.

[1]Prior to 2007 E-REGI was produced jointly by the European research teams of Jones Lang LaSalle and LaSalle Investment Management.

The E-REGI Model

E-REGI is a multi-factor model that ranks each city based on the weighted average score of 15 variables. The variables contained in the model together with their respective weights are set out in the Technical Note (Page 10). In summary, the model combines economic growth factors, the overall level of wealth, and measures of the relative attraction of the business environment, as follows:

- **Growth measures** (accounting for 60% of the model) include change in overall regional output and service employment, as the principal sources of real estate demand. We have used the recent trend in growth (to capture momentum), as well as forecasts of future growth, in both absolute and relative terms. A measure of research & development (R&D) expenditure has been included to capture innovation potential, an important driver of growth.
- **Wealth measures** (accounting for 20% of the model) act as a further screen so that cities that are merely catching up from a low base are not unduly represented. Furthermore, market expertise suggests that wealth levels are correlated with demand for real estate.
- **Business operating environment measures** (accounting for 20% of the model) have been included, as future economic strength is likely to be substantially determined by the attractiveness of the business environment, particularly to foreign investors. Best prospects are likely to be in those cities that can offer the most flexible labour markets, a favourable tax regime, and those that are least regulated.

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E-REGI 2010 Results

Europe is cautiously emerging from the downturn and most countries are expected to return to positive GDP growth in 2010. The competitive economies of Sweden, Germany and France are forecast to fare better in this early recovery, while Southern Europe is likely to lag. The CEE countries have generally experienced a more torrid downturn but are expected to revert to their pre-crisis trend growth rates by 2013/14, following the global recovery.

The E-REGI 2010 results reflect that the disparity between winning and losing cities will be particularly marked over the next few years. This highlights that some locations will be leading the still fragile economic recovery while others will be followers relying on the ripple effects from the winners. One of the reasons for these disparities is the reduced ability of governments to even out growth through regional stimuli because of general fiscal constraints.

European governments have provided extensive fiscal support during the downturn and successful public debt management is crucial to the recovery. The Greek sovereign debt crisis contributes in a considerable way to the risks surrounding the Eurozone recovery. The imbalance in the bail-out burden, mainly at the expense of Germany, puts the future of the Eurozone at risk. On the upside, the recently released results of the “stress tests” for European banks suggest more resilience within the EU banking system than some expected.

In Q2 2010, direct commercial real estate investment in Europe totalled a24bn, representing a 19% increase on Q1 2010 (a20bn) and 92% growth year-on-year. Transaction volumes remained broadly stable at a43bn in H1 2010 (a45bn in H2 2009). More specifically, German investment volumes totalled a4bn in Q2 2010 (+120% year-on-year), the corresponding figures being a2bn (+21%) in France and e1.4bn (+185%) in Sweden.

Capital values have declined as a result of the strong outward shift in yields during the downturn. During the nascent recovery since late 2009, prime office and warehousing yields have compressed by 30bps to date (Q2 2010) and retail by 20bps. Going forward, the downside risks include a delay of the rebound in corporate demand and scarcity of financing. Larger, more liquid markets are expected to see a growing share of activity.

The E-REGI provides guidance as to what can be expected of the European property markets, identifying the cities that look set to provide the best medium term prospects for real estate demand. As Europe is emerging from the recession of 2008/2009, dynamic economies such as London perform more strongly while less competitive locations, even in otherwise robust countries, fall behind.

London (UK)

- **London** (1/+7) is back at the top of the E-REGI ranking. As the trough of the economic crisis appears to have been passed in 2009, the dynamic and flexible economy is bouncing back strongly. With the trough year in 2009 having come out of the forecast component of the analysis, London’s growth score is now largely unmatched again, even by emerging economies. This renewed success highlights London’s role as the major European business hub.
- More specifically, going forward, the effects of the 2012 Olympic Games in London are expected to provide at least a boost to investment and activity. The Games are also expected to speed up development in the Lower Lea Valley, one of the priority areas for regeneration in London. The Games themselves will provide numerous job opportunities and the influx of spectators will offer a boost to the local hospitality industry. Moreover, work has started on Cross Rail, a long planned project, which will improve east-west communications across the London area significantly.

Rest of the UK

- Britain’s general election in May 2010 has delivered a coalition government whose task it will be to tackle the mounting public debt burden. In addition, the UK’s economic recovery is surrounded by risk factors stemming from the over-exposure of banks and the highly indebted households. This cautious outlook exacerbates the polarisation between Tier-1 and regional cities. In fact, the UK is the most polarised Western European economy, with one city (London) at the top of the ranking and all other cities close to or in the bottom half of the table.
- Against this background, regional competitiveness is becoming more and more important as weaker regions can no longer rely on national momentum and increased public expenditure to help sustain their growth. Most of the UK regional and mainly former industrial cities that struggle with the structural transition to a service-based economy lose ground in this year’s ranking, including **Liverpool** (94/-40), **Edinburgh** (59/-11), **Sheffield** (95/-19), **Leeds** (74/-14), **Nottingham-Derby** (45/-7), **Newcastle** (80/-2) and **Manchester** (36/-1).

Moscow (Russia)

- **Moscow** (2/+4) made a spectacular entry into the E-REGI analysis in 2009. This successful result is repeated in 2010 and continues to be due to the size and exceptional growth platform of the city.
- However, Moscow’s wealth score continues to be below average and highlights the fact that the economy is still at an emerging stage and catching up with more mature locations. In line with this characteristic, especially the business environment score continues to detract from the city’s overall ranking. Growth potential alone is not sufficient to qualify a city region as a suitable investment target market.
- Overall, Russia has to deal with a weak banking sector burdened with non-performing loans and persistently high unemployment that is likely to keep domestic demand restrained and to dampen the impetus from higher oil prices and fiscal stimulus. However, the economy is catching up from a low base, and as a result its main city regions benefit from stronger growth prospects. From a political point of view, Russia is set to maintain its renewed ties with the West. Large

bail-out packages have left the state with control of c. two thirds of the economy and a large debt burden, which has triggered the privatisation of 5,500 businesses. The key issue going forward is to take steps to restore confidence amongst foreign investors in the safety of investing in Russia.

- Against this background, the other Russian cities featuring in this year's E-REGI mostly improve their positions: **Nizhny Novgorod** (49/+45), **Yekaterinburg** (77/+14), **St. Petersburg** (97/-5). Despite their shrinking populations, these cities have above average growth prospects as they attract workers and businesses from the rural regions. However, their relatively stronger growth forecasts cannot conceal deficiencies in wealth levels and serious operational risks in the business environment.

Rest of Central & Eastern Europe

- A large number of the Central and Eastern Europe (CEE) city regions improve in this year's ranking, as their economies have either been less affected by the downturn or have more momentum as they are catching up from a lower base in an otherwise low-growth environment. Notably Poland can benefit from trade links to stronger economies such as Germany.
- **Warsaw** (22/-5) slightly loses ground in this year's E-REGI as its growth score deteriorates. As it has largely been spared by the downturn, the recovery is expected to be less buoyant than in other emerging regions that are developing more dynamically from low levels.
- In general, the growth scores of the Polish city regions are underpinned by the country's strong ties to Germany, which is performing relatively more strongly in a European context. As a result, many of these locations can improve their rankings as compared to last year, e.g. **Lodz** (78/+7), **Krakow** (57/+9), **Katowice** (69/+2), **Poznan** (44/+19), **Wroclaw** (50/+33), and **Tricity** (43/+36).
- Several countries in the CEE region are facing a protracted recovery due to high current account deficits, extensive foreign currency borrowing and deficient fiscal policy. These factors are forcing a number of CEE regions to introduce painful retrenchments in return for bail-out measures offered by the IMF, e.g. Hungary and Romania. Consequently, the majority of CEE locations remain near or in the bottom half of the ranking, such as **Budapest** (83/-1) and **Bucharest** (52/+32).
- **Prague** (38/-17) continues to be one of the few CEE locations that achieve an above average ranking. GDP growth has recently been boosted by strong gains in manufacturing, but forecasts remain cautious as the country's economic results strongly depend on external demand. The risk score is weaker as the inauguration of the new government introduces uncertainty. Going forward, key challenges include cutting the fiscal deficit, fighting corruption and reforming the welfare systems.
- **Bratislava** (35/+15) occupies an above average position in this year's E-REGI. The Slovakian economy has recovered in early 2010, driven by rising industrial output and exports. The new centre-right government is likely to bring improvements in the business environment and the country is now expected to have a better chance of meeting the Maastricht deficit criteria (3% of GDP) by 2012. Going forward, the main risks are weak domestic demand and high unemployment. On the upside, the city benefits from increased integration with Vienna.
- **Ljubljana** (70/-24) loses ground relative to last year's ranking. However, in an attempt to boost growth, the Slovenian Trade and Investment Agency has outlined a new programme for 2010/11 to attract foreign direct investment. This project is mainly aimed at manufacturing, services and R&D, with individual projects eligible for state aid if they generate a set number of new jobs.
- **Kiev** (56/N/A), a new entrant into the E-REGI 2010, achieves a slightly below average position. While its score is almost entirely driven by growth, which is typical for emerging locations catching up from a low base, the wealth component is very low and the difficult business environment detracts from the overall rating. This pattern can be observed for all Ukrainian locations that have been added to the E-REGI 2010.
- Unlike in previous years, the Baltic locations show a more heterogeneous performance in the E-REGI 2010: **Vilnius** (98/-1), **Riga** (101/-3) and **Tallinn** (62/+34). This fact highlights strong regional discrepancies based on differing levels of competitiveness, an important characteristic of this early European recovery. Estonia shows the strongest performance. Recovery chances are likely to improve further when the country will enter the Eurozone in 2011 as the first Baltic state member of the currency union.

Munich (Germany)

- **Munich** (3/-2) loses its position at the top of the ranking in 2010, but continues to occupy a place in the top 3. The location benefits from strong economic growth prospects, fostered by a balanced mix of strong global players and a diverse range of SMEs, an ongoing commitment to R&D and high levels of wealth. Munich's success is all the more impressive as it does not compete on scale – it is significantly smaller than London, Moscow and Paris.
- However, Munich is partially dependent on the car industry (BMW) and the severe recession in 2009 has slightly reduced wealth levels (measured as GDP/capita in 2009).

Rest of Germany

- After a severe recession in 2009, Germany is expected to outperform the Eurozone in the short to medium term. The government's short-term work scheme successfully supports the labour market which represents an encouraging sign for the consumer sector, particularly when taken together with the recent increases in confidence. However, the expiry of the short-term work scheme later in 2010 might cause second-round increases in unemployment. Nevertheless, based on strong competitiveness and a weaker Euro currency, Germany is expected to bounce back strongly. As a result, it is again the country with the highest number of locations in the top 20 (four).

- Traditionally strong locations such as **Frankfurt** (20/0), **Stuttgart** (13/-4) or **Mannheim-Karlsruhe** (17/-2) remained virtually stable in 2010. This success highlights the robust and competitive structure of these economies that manage to achieve top 20 rankings in this emerging economic recovery phase Europe undergoes in 2010.
- A number of established locations move up the table in this beginning recovery; e.g. **Berlin** (55/+9), **Hamburg** (24/+7), **Dusseldorf** (28/+6) and **Cologne/Bonn** (26/+4). This strong result shows the clear divide between those locations that have the economic strength to lead the nascent recovery and those that follow only once a certain national momentum has been achieved.
- For the time being, the national growth momentum is not strong enough to support otherwise less competitive regions.
- Consequently, a number of German locations have lost ground in this year's ranking, e.g. **Saarland** (84/-44), **Leipzig-Dresden-Halle** (73/-24), **Hannover** (48/-16), **Nuremberg** (33/-6), and **Bremen** (41/-5).

Paris (France)

- **Paris** (4/-2) continues to occupy a top 5 ranking, mainly on the back of sustained growth prospects and high wealth levels. As a result of the centralised political system, Paris is a major hub of administrative, economic and financial activity in France. It also serves as an important transport and logistics centre in France.
- The Paris region is Europe's biggest employment base with 53% of French executives living in the area. This high proportion of senior personnel is due to the density of company headquarters located in the region. The success and economic diversity of the city are driven by vigorous R&D activity, boosted by the creation of competitiveness clusters which have opened up new opportunities for cooperation between the public and private sectors.

Rest of France

- France is expected to show a solid performance, outperforming the Eurozone in 2010/11, based on high levels of diversification. This positive outlook is due to the greater sector balance in the structure of the French economy and the significant share of the traditionally stable public sector. French consumers are in a relatively good position to weather the crisis due to lower levels of household debt and increasing levels of real disposable income.
- Consumption is further aided by ample government support. In an attempt to consolidate public finances, the French government is planning unpopular measures to cut the pension burden on the state e.g. by increasing the retirement age, which is unusually low at 60 in the public sector for instance.
- A number of French locations slip down the ranking meaningfully in 2010, mainly due to lower growth forecasts as a result of the generally sluggish pace of the recovery. Examples are **Rouen-Le Havre** (75/-33), **Lille** (71/-18), **Strasbourg** (85/-46) and **Basel-Mulhouse** (37/-9).
- On the other hand, **Nantes** (23/+14), **Bordeaux** (32/+1), **Toulouse** (11/+11) and **Lyon** (19/+4), improve their relative ranking, mainly based on the fact that the outlook for employment has improved as compared to last year. Toulouse is positively affected by the improved outlook for Airbus in 2010. France still features prominently in the E-REGI 2010 with four cities in the top 25.

Stockholm (Sweden)

- **Stockholm** (5/-2) maintains a position in the top 5 of the E-REGI 2010, reflecting both its strong growth platform and comparatively high levels of wealth. Stockholm is the largest Scandinavian city economy and thus its natural business and financial centre. The city has the highest regional GDP and the highest growth rate among Scandinavian capitals.
- The Swedish economy is expected to recover strongly in 2010/11. The main drivers of the recovery are likely to be exports and livelier consumer markets, despite concerns of unemployment and high indebtedness having elevated household savings rates. Nevertheless, consumer spending is recovering, underpinned by a sharp rebound in sentiment and positive income developments arising from a stream of tax cuts in recent years. Furthermore, consumers still enjoy record-low interest rates and muted inflation. Moreover, Sweden's business-friendly attitude is a competitive advantage.

Rest of Nordics

- **Oslo** (6/-2) is Norway's premier business centre and benefits from one of the highest wealth levels in Europe. Further, Oslo ranks high on innovation. Its competitive strength is based on a service-oriented economy with more than 80% of the workforce employed in services. However, the Oslo economy relies heavily on revenues from the oil sector. The Norwegian economy emerged from a very mild recession in mid-2009, and the recovery is projected to evolve steadily during 2010 and 2011. The main development will be a stronger consumer spending profile, helped by record-low interest rates, falling inflation, and a relatively resilient labour market.
- **Helsinki** (14/-7) loses its long-standing position in the top 10. While the area expanded as a business location in the recent past due to connections to the Russian and Baltic markets, these links caused it to suffer severely in the financial crisis. The sharp downturn in Finland appears to have bottomed out, but solid growth has not quite returned to Helsinki yet. This is partly due to the fact that one of the most important local businesses, Nokia, lost some of its market share to new competitors.

Zurich (Switzerland)

- Against the background of sustained growth and high levels of wealth, the Swiss cities perform strongly in the E-REGI 2010, and all achieve positions in the top quintile of the scale: **Bern** (15/-1), **Geneva** (16/+9), **Zurich** (9/+3).

- Swiss exports will be hampered by currency appreciation, meaning that expansionary fiscal and monetary policies are likely to be sustained for the remainder of 2010.
- Financial sector stability has improved, but cautiousness about lending remains a restraint. Overall, the Swiss economy has weathered the global downswing of 2008–09 quite well, with domestic demand resilience limiting GDP contraction in 2009. Leading sentiment indicators and the purchasing managers' manufacturing index have shown a sustained rebound until mid-2010, with the latter even reaching an all-time high in spring.
- The double-tax agreements signed in 2009 to secure Switzerland's removal from the Organisation for Economic Co-operation and Development's tax haven "grey list" are likely to go ahead after planned referendum initiatives were dropped by the Swiss People's Party and the Ticino League.

Luxembourg

- **Luxembourg** (10/-5) drops down moderately as compared to the E-REGI 2009, but maintains a position in the top 10. While the city achieved a strong ranking in 2009 on the basis of high wealth levels, this cushion is no longer sufficient to sustain the region as growth – albeit modest – returns to Europe.
- Notwithstanding the economic rebound since mid-2009, GDP growth will remain more subdued than during 2004–07 as financial institutions' operations – notably corporate lending and capital flows to investment funds – are impaired by the damage inflicted on their balance sheets. Furthermore, the detrimental impact of the crisis affecting the public finances of many Eurozone countries will restrain exports, as well as foreign interest in doing business with financial institutions in Luxembourg.

Rest of Benelux

- As the Belgian regions are drifting apart, **Brussels** (29/-10) loses ground in the E-REGI 2010. Belgian exports of goods and services account for some 80% of GDP. The global recovery and the weaker Euro should help Belgium's export sector in the near term, but competition from emerging markets is edging up. Further, the government's efforts to boost employment and growth are stalling. For instance, in January 2010, U.S. vehicle manufacturer General Motors (GM) decided to close its plant in **Antwerp** (40/-11), resulting in up to 2,600 job losses.
- The **Dutch** locations also lose ground in the E-REGI 2010: **Utrecht** (18/-7), **Amsterdam** (30/-12), **Rotterdam/The Hague** (27/-1). The Dutch economy expanded modestly in early 2010, driven by improving net exports. Nevertheless, household consumption and business investment remain muted. Private consumption contracted in early 2010, while the labour market situation deteriorated further.
- On the bright side, the Dutch economy is strongly dependent on exports, especially to Germany. The Netherlands should thus be able to benefit from the relatively stronger recovery there. Particularly Rotterdam benefits from the improved outlook for world trade and now outranks Amsterdam.

Austria

- **Vienna** (12/+1) has remained largely stable in the E-REGI 2010, mainly due to high wealth scores, and has thus also achieved a top quintile ranking.
- The helpful Austrian export rebound observed in early 2010 may lose momentum in late 2010 and in 2011, given fiscal consolidation needs in most parts of the world and a bumpy recovery in most Eastern European economies, which are of particular importance to Austria. More specifically, the city benefits from increasing integration with Bratislava. Banking sector problems appear to have diminished following the publication of satisfactory results of the bank stress tests, but ongoing cautiousness about lending to the non-financial sector will continue to have a restraining effect on the pace of the recovery.

Iberia

- In line with the pattern observed in many established Western European economies, there are sharp discrepancies between the performance of the Spanish city regions as the severe decline in 2009 that affected all regions to a similar extent is over and the recovery depends very much on local robustness and competitiveness: **Bilbao** (86/-35), **Zaragoza** (96/-27) and **Madrid** (46/-2) lose ground while **Barcelona** (51/+17), **Valencia** (53/+9) and **Seville** (72/+14) improve their rankings.
- The economy is still struggling to cope with excessive levels of private debt, a creaking property market, and an over-extended construction sector, coupled with recovering but still muted demand from key export markets. In addition, the government has implemented tough austerity measures, despite the economy still being wounded. Consumers remain insecure about the economy and the labour market, with deep-rooted concerns over the stuttering housing market and high personal indebtedness.
- In terms of competitiveness, the Spanish economy needs to re-orientate itself in order to generate sustainable growth going forward. Until Spain can credibly signal to investors it has the potential to turn this corner, the country remains threatened by contagion effects from Greece.
- **Lisbon** (54/-2) and **Porto** (100/-11) both occupy positions in the bottom half of the ranking in 2010. High unemployment, reduced credit availability and tighter fiscal policy are squeezing Portuguese private consumption.
- Spare capacity, reduced profit margins and depressed confidence are likely to decrease investment expenditure. Global demand is expected to improve modestly in 2010, which should help Portuguese exports. However, the economy suffers from a fundamental lack of competitiveness. Given the mounting public debt burden and a high level of foreign ownership, the country put at risk through contagion from the Greek crisis. Portugal has strong ties to Spain as a trading partner, a country with a particularly vulnerable economy and difficult prospects. On the upside, links to the vibrant economy of Brazil are improving.

Ireland

- **Dublin** (21/+52) improves significantly in the E-REGI 2010. This is almost exclusively due to higher growth scores. The trough year (2009) has come out of the forecasts and the outlook has improved as the Irish economy has rebounded strongly in early 2010. Also, Dublin is driven by the financial services sector, which has regained strength.
- In general, expectations are for Irish GDP to rise modestly in 2010 following a sharp fall in 2009. However, the recovery is forecast to be laboured. Unemployment is expected to remain high for some time to come. Tight credit conditions, falling house prices, and excess capacity are likely to limit growth in the short to medium term. The public finances appear to be stabilising and an overall funding requirement of about **e**20 billion for 2010 remains a valid target. Ireland has now completed 90% of its long-term borrowing programme of **e**20 billion for 2010. In March 2010, the long-awaited "bad bank" scheme was finally launched in Ireland to take ownership of banks' loans arising from the property market.

Italy

- As the fragile economic recovery is very selective and based on local competitiveness, the north-south divide in Italy intensifies. For instance, **Milan** (34/+23) and **Turin** (39/+38) improve in this year’s ranking while **Rome** (82/-26), **Naples** (102/-14) and **Palermo** (103/-10) lose ground.
- The latest economic data and survey evidence have been appreciably firmer and suggest that the Italian economy is likely to expand in 2010. Nevertheless, the pace of recovery is likely to be gradual, with the country still facing significant obstacles to a stronger growth profile. In particular, consumers are expected to spend cautiously against a backdrop of higher unemployment and rising energy costs. The government has pledged to implement painful austerity measues to prevent contagion effects from the Greek crisis.
- Businesses remain under significant pressure from shrinking profit margins, muted sales, and modest sentiment. Demand for labour is projected to cool further in 2010 as the pace of economic recovery is likely to be uneven.
- The business environment continues to be a major drag for the Italian locations. Legislation passed in early 2010 allowed Prime Minister Berlusconi to suspend three ongoing corruption trials. Moreover, Italian politicians, public servants and judges are once again battling against corruption allegations.

Greece

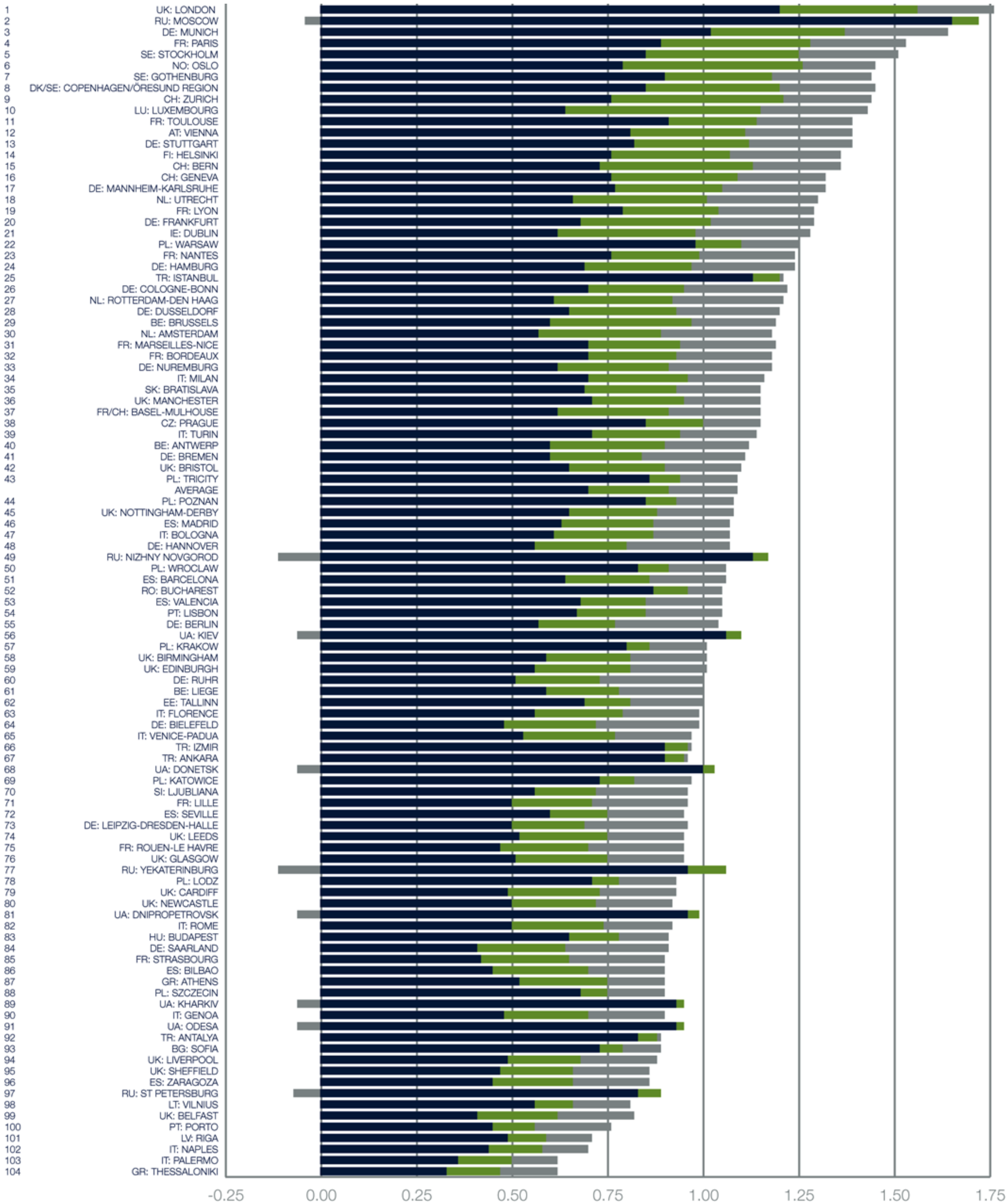
- The two Greek cities featuring in this E-REGI ranking, **Athens** (87/-44) and **Thessaloniki** (104/-23), both lose ground as compared to last year’s analysis, as they suffer from the Greek sovereign debt crisis.
- The **e**750bn package unveiled by the European Union, alongside the European Central Bank and the International Monetary Fund, gives Greece an opportunity to improve its fiscal situation but the scale of consolidation required is likely to prove very difficult.
- Greek GDP is expected to contract in 2010. Private consumption will come under intense pressure as a result of higher unemployment, weaker wage growth, and significantly tighter fiscal policy, including a higher value-added tax (VAT) rate. Moreover, reduced credit availability and concerns about the economic outlook will not only deter households from consuming, but will also weigh down on investment expenditure. There are several scenarios surrounding the ultimate outcome of the Greek crisis, including exiting the Eurozone and devaluing the local currency. Irrespective of the exact political scenario, the next few years will be difficult for Greek cities.

Turkey

- The Turkish Tier-1 locations, **Istanbul** (25/+50), **Ankara** (67/+23) and **Izmir** (66/+29) have all improved their rankings as compared to last year, almost exclusively on the basis of stronger growth scores. Moreover, **Antalya** (92/N/A) has been included in the ranking for the first time.
- Especially Istanbul performs strongly in the E-REGI 2010. It is the leading commercial centre in Turkey. More than a third of Turkish imports and exports pass through Istanbul. It is still largely an industrial city, accounting for nearly half of the national production and broadly the same percentage of jobs. The city is also a major banking and insurance centre.
- The Turkish financial sector appears to have weathered the global downturn of 2008/09 and the Euro crisis of 2010 in relatively good shape, allowing it to continue to expand credit. This increased lending helps fuel a strong rebound in domestic demand, even as the government tightens fiscal policy and labour markets are weak. The domestic market appears to be willing to spend even in this difficult environment and GDP growth will be among the strongest in Europe over the next couple of years.
- However, debt-servicing obligations are not set to ease significantly before 2011. Until then, financing demands remain substantial, particularly given that the country's current account deficit is anticipated to return to high levels.
- As far as the legal environment is concerned, the Justice and Development Party (AKP) presses ahead with constitutional reform plans. The proposal has overcome a major hurdle by being passed in parliament in May 2010. However, it has reinforced the divisions between the proposal’s supporters and its often staunchly secular opponents. The next key step is a September referendum. A yes-vote would give the AKP a great platform from which to fight its campaign for the parliamentary election in 2011.

E-REGI 2010 – City Coverage

E-REGI 2010 – City Scores



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Technical Note

Coverage

The analysis has been undertaken on regions defined by Eurostat, which acts as the central statistical bureau for the European Union. Eurostat has adopted a classification system, the "Nomenclature of Territorial Units for Statistics", referred to as 'NUTS'. This classification provides a breakdown of territorial units for the production of regional statistics within the EU. NUTS is a hierarchical classification. The country level is referred to as NUTS 0. NUTS 1-NUTS 3 are regional levels.

The E-REGI model uses the NUTS 2 level classification, which we believe is the best equivalent to the Standard Metropolitan Areas (SMAs) in the USA. However, in formulating the NUTS-level classification, Eurostat has attempted to standardise a disparate set of national classification systems, and as a result the NUTS classification sometimes lacks consistency on a pan-European scale. Therefore, NUTS 2 regions do not always provide the most appropriate definition of a city region, and in some instances we have assembled a combination of NUTS 1, 2 and 3 areas that better correspond with the physical and economic extent of those cities.

E-REGI Model

The model is a weighted average of 15 sets of data, which can be expressed as a function set out in Figure 1. The variables used in the model are set out in Figure 2. The model is constructed by assigning scores for each variable relative to the average across inputs for all NUTS 1/2 locations. Thus an average location has a score of unity.

Data Sources

Data for the E-REGI model is drawn from several sources. Experian has supplied the Eurostat NUTS 1, 2 and 3 historic data and provided 5-year forecasts for GDP and employment growth. (Except for Russia, Turkey and the Ukraine; in these cases, GDP forecasts have been obtained from Global Insight as these seem to better reflect the most recent economic developments).

The R&D data is sourced from Eurostat. Business operating environment measures have been obtained from Global Insight, which provides national business environment rankings.

Figure 1

E-REGI = *F*[GDP, EMP*m*, R&D, WEALTH, BEnv, EMU]

Where:	GDP	Change in Regional GDP
	EMP*m*	Change in number of Employees in Market Services
	R&D	Expenditure on Research & Development
	WEALTH	Level of GDP per Capita
	BEnv	Quality of Operating Environment for Business
	EMU	EMU/EU Participation

Figure 2

1.	**Growth Components:**	**60%**
	A. Absolute Growth (15%)	
	Forecast Employment Growth 2010-14	7.5%
	Forecast GDP Growth 2010-14	7.5%
	B. Percentage Growth (30%)	
	Forecast Employment Growth 2010-14	12.5%
	Forecast GDP Growth 2010-14	12.5%
	Employment Growth 2007-09	2.5%
	GDP growth 2007-09	2.5%
	C. Research & Development (15%)	
	Spend on R&D as a % of GDP (latest)	15%
2.	**Wealth / Level of Development**	**20%**
	GDP per Capita 2009	
3.	**Business Environment Components:**	**20%**
	A. Country Business Environment	
	Tax	5%
	Operational Environment	2%
	Political Environment	2%
	Economic Environment	2%
	Legal Environment	2%
	Security	2%
	B. EMU/EU Participation	**5%**
	TOTAL	**100%**

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