Lar España Real Estate SOCIMI, S.A. and subsidiaries

Consolidated Directors' Report for the year ended 31 December 2014

(Free translation from the original in Spanish. In the event of discrepancy, the Spanish-language version prevails.)

1 Situation of the Group

1.1 Situation in the real estate market

Office market

- **Madrid**

At 31 December 2014 the office rental market in the centre of Madrid has seen an improvement in the level of rentals in the central business district (CBD), with an increase of 5.15% with respect to the same period of the prior year. Rental levels in the secondary CBD have remained constant.

The gross take-up for 2014 is up 3% compared with 2013, standing at 390,000 m2 at the 2014 reporting date.

At 31 December 2014 the vacancy rate is 12.1%.

The rental price of prime properties in Madrid is Euros 25.5/m2/month.

- **Barcelona**

Rental prices in Barcelona have risen 3.38% in 2014. Paseo de Gracia and Diagonal have seen an increase of 1.42% compared with the same period of the prior year.

The gross take-up in 2014 was 281,700 m2, reflecting an increase of 51% on 2013 figures.

At 31 December 2014 the vacancy rate is 12.5%.

The rental price of prime properties in Barcelona is Euros 17.75/m2/month.

Logistics market

The volume of investment has increased from approximately Euros 100 million in 2013 to over Euros 600 million at the 2014 reporting date as a result of investments from large institutional investors and recently created SOCIMIs (listed corporations for investment in the real estate market - Spanish “REITs”).

Returns have ranged from 7.25% to 8.25%.

Take-up has risen with respect to 2013, although to a lesser extent than investment volume.

Residential market

According to the latest statistical data published by the Spanish National Statistics Office (INE), prices in the residential market have climbed 1.6% in 2014.

It should be noted that this includes a 2% increase in the price of new homes and a 1.5% rise in the price of second hand homes.

New real estate developments have been undertaken in Madrid and Barcelona, where the offering of residential property is limited.

Commercial premises

According to the latest report published by the INE, at 30 December 2014 the national occupancy rate was up 0.9% compared with 2013.

This improvement has been supported by the 1.2% rise in sales in shopping centres at 31 December 2014 with respect to the same period in 2013.

The general retail trade index has improved by 1.9% in 2014, with the personal accessories (0.9%), household accessories (6.6%) and other (1.4%) sectors performing particularly well.

Consumer spending in Spain is currently recovering and has improved with respect to 2013.

Investment market

The investment market has become more competitive, due primarily to the following factors:

- The appearance of new SOCIMIs competing for certain types of assets.
- Growing interest in the Spanish market among international investors looking for opportunities.
- Financing has improved in terms of LTV and cost.
- There has not been a particularly extensive market of real estate available for sale in 2014, especially in the office sector.

Asset management capacity and access to the market will be the key elements for predicting the behaviour of the Spanish real estate sector in the coming months.

These trends have not altered the initially planned investment schedule or the expected returns therefrom.

1.2 Organisational structure and functioning

The Group comprises a group of recently incorporated companies that outsource their management functions. It has assigned Grupo Lar Inversiones Inmobiliarias, S.A. to be the sole manager. This company has over 40 years' experience in the real estate market and a long history of generating value over the course of various real estate cycles spanning recent decades and has alliances with some of the most renowned international investors.

The main responsibilities of the Parent's board of directors include establishing an investment strategy, allocating resources, managing risks and corporate control, as well as bookkeeping and preparing the financial reports.

The Group's activity focuses primarily on three types of assets:

- Shopping centres: the lease of commercial premises and of single-tenant commercial properties.

  The Group's strategy is based on seeking out shopping centres with high growth potential and deficiencies in asset management, particularly where there are opportunities for replacement or expansion.

  The Group intends to continue investing in single-tenant commercial properties in favourable locations and with good transport links.

  The Group's investment approach is to evaluate the possibility of entering into joint venture agreements in order to limit asset concentration risk and be able to access larger commercial premises.

- Office: office rental business.

  The Group focuses primarily on the Madrid and Barcelona markets, which attract the greatest interest from institutional investors and have the highest levels of liquidity. The Group's strategy is to invest in refurbishment and the improvement of installations and occupancy rates of existing buildings.

- Logistics: logistics centre rental business.

  The Group seeks to invest in large centres located in logistics platforms with good land transport connections and high-profile tenants. It also seeks out assets and locations where rental prices are projected to grow.

The Group is planning to invest in the residential market, with a particular focus on first homes located in the most consolidated areas of the largest cities in Spain. (See note 31 to the annual accounts).

The Group's investment policy principally encompasses:

- Investment opportunities in medium-sized assets that offer significant opportunities for management, avoiding segments with higher levels of competition.

- Risk diversification, expanding throughout Spain with the primary focus being on investments in commercial premises. With respect to offices and logistics centres, the focus is on Madrid, Barcelona and, to a lesser extent, certain large cities such as Valencia, Seville etc., while in the residential market (first homes) the focus is on the main cities and market segments with a limited offering. This will give the Group a portfolio that is diverse in terms of both asset type and location.

The Group has a robust pipeline that will enable it to comfortably achieve its investment plans as forecast.

For further information on lines of business and geographical areas see note 6 to the consolidated annual accounts.

2 Business outlook

2.1 Introduction

At the 2014 reporting date the Group's revenues amount to Euros 8,606 thousand derived from the Group's activity, i.e. the rental business.

The Group's other operating expenses for 2014 amount to Euros 7,231 thousand and primarily relate to advisory services for the acquisition of assets (commercial, technical and legal due diligence etc.) provided by entities not related to the Parent (Euros 2,597 thousand) and the fees for management services provided to the Parent by Grupo Lar Inversiones Inmobiliarias, S.A. (Euros 2,083 thousand).

Operating profit before revaluations, provisions and interest (EBITDA) totals Euros 1,926 thousand.

The independent appraisal performed by Cushman & Wakefield and Jones Lang LaSalle at the reporting date revalued the Group's real estate investments by Euros 442 thousand.

At the 2014 reporting date the Group's rental business was valued at Euros 357,740 thousand by the same independent appraisers mentioned in the previous paragraph. The appraisal values are updated every six months in line with market best practices (see note 7).

Net finance income is Euros 1,872 thousand excluding the profit/(loss) on equity-accounted investees.

The Group made a profit of Euros 3,456 thousand in 2014.

By area of activity is should be noted that:

- A significant percentage of the Group's revenues comprises rental income from shopping centres, which represents 73% of total revenues, compared with rental income from offices and logistics, which accounts for 13% and 14%, respectively.

- Over 67% of rental income from shopping centres is earned through the Txingudi and Anecblau shopping centres.

At 31 December 2014 the Group's entire business has an occupancy rate of 89.75% of the gross lettable area (GLA), with occupancy rates of 90.2% in shopping centres, 83.1% in offices and 91.7% in logistics.

At the 2014 reporting date the Group has a portfolio of rental property projects that includes seven shopping centres (84,904 sqm), four office buildings (41,732 sqm) and two logistics centres (119,147 m^2), with a total gross lettable area of 245,783 sqm.

2.2 Other financial indicators

At 31 December 2014 the Group presents the following financial indicators:

- Working capital of Euros 52,380 thousand.
- Liquidity ratio of 11.8.
- Solvency ratio of 1.1.

These ratios are high, indicating that the Group has sufficient liquidity and a substantial security margin to meet its payment obligations.

The ROE (Return on Equity), which measures the return obtained by the Group on its equity, is 0.89%; the ROA (Return on Assets), which measures the efficiency of the Group's total assets irrespective of the sources of financing employed, i.e., the capacity of the assets of a company to generate income, is 0.79%.

2.3 Environmental and personnel issues

Environmental issues

The Group takes measures to prevent, reduce and repair the damage caused to the environment by its activities. However, due to its nature, the Group’s activity does not have a significant impact on the environment.

Personnel

See note 29 to the consolidated annual accounts.

3 Liquidity and capital

3.1 Liquidity and capital

In what has been the Group's first year of activity, the Parent has obtained its liquidity primarily by issuing 40,030,000 shares of Euros 2 par value each plus a share premium of Euros 8 per share.

The Group's outstanding financial debt totals Euros 37,822 thousand at 31 December. This level of debt is due to the acquisition of the Egeo office building and the Nuevo Alisal shopping centre during the year.

The Group aims for the maturity of its debt to be in line with its capacity to generate cash flows to service this debt.

See section 1.2 of this report for details of how the Group expects to fund its future investments.

3.2 Analysis of contractual obligations and off-balance sheet transactions

At 31 December 2014 the Group does not have any contractual obligations that would give rise to future cash outflows.

At 31 December 2014 the Group does not have any off-balance sheet transactions that have had, or will foreseeably have, a significant effect on the Group's financial position, income and expense structure, results of operations, liquidity, capital expenses or equity.

4 Main risks and uncertainties

See note 22 to the consolidated annual accounts and section E of the Corporate Governance Report for 2014.

5 Events after the reporting period

See note 31 to the consolidated annual accounts.

6 Outlook for the Group

The outlook for the Spanish rental market is as follows:

- 2015 is expected to be the year of consolidation and subsequent upturn in activity in the Spanish real estate market in general.
- There will be divergences in price, returns and availability between different areas.
- The offering in the rental market is predicted to grow as a result of assets that were acquired by investors when prices in the sector were at their lowest point now becoming available on the market.
- Prices are expected to increase, while returns in prime areas in Madrid and Barcelona will decline as a result of the scant offering of premium assets coupled with rising demand, especially from institutional investors.

Given the current level of reserves, we are confident that the Group will be able to continue making good progress in 2015 and subsequent years.

See section 1.2 of this report for information on the investments that the Group expects to carry out in the future.

7 R&D&i activities

Given the characteristics, activities and structure of the companies comprising the Group they do not usually engage in research, development or innovation activities.

8 Acquisition and disposal of treasury shares

See note 14.c.iii) to the consolidated annual accounts for information on treasury share transactions.

These purchases were carried out in the framework of a discretionary treasury share management agreement that was reported to the CNMV in compliance with the recommendations published by that entity on 18 July 2013.

At 31 December 2014 the share price is Euros 9.18.

At the 2014 reporting date the Parent holds 531,367 shares, which represent 1.3% of the total shares issued.

9 Other significant information

9.1 Stock market information

The IPO share price was Euros 10 and the par value of the Parent's shares at the reporting date is Euros 9.18. The average share price for the year has been Euros 9.59.

The Group does not currently have a credit rating from the main international ratings agencies.

9.2 Dividend policy

See note 5.e) to the consolidated annual accounts for information on the dividend policy.

9.3 Average payment period for suppliers

The average payment period for suppliers stood is 31 days.

10 Annual Corporate Governance Report

For the purposes of article 538 of the Spanish Companies Act, it should be noted that the 2014 Annual Corporate Governance Report forms part of this Directors' Report.