

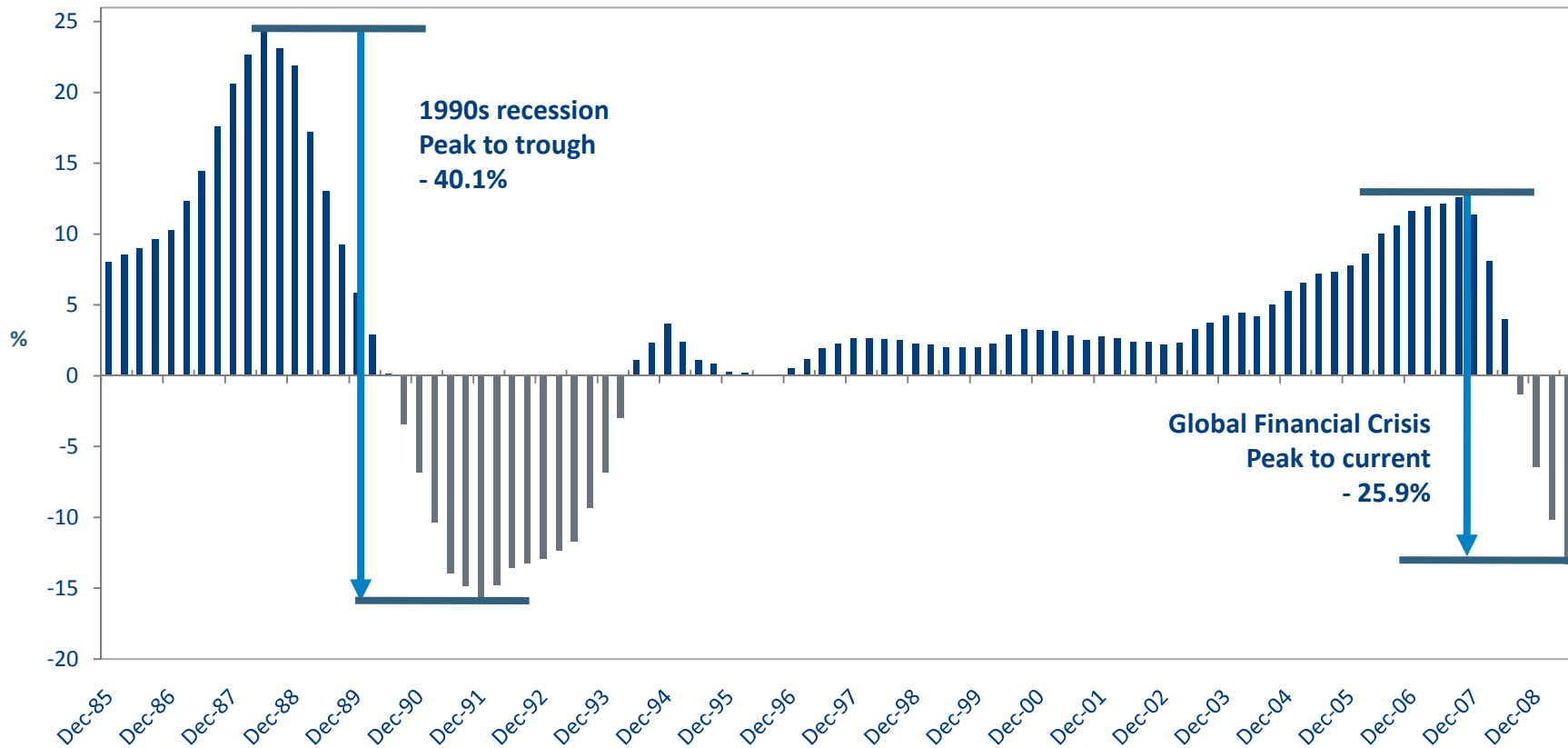
“Why ‘Back to Basics’ is the new mantra in the commercial property sector”

PCA Perth – November 2009



Downturn – not that bad?

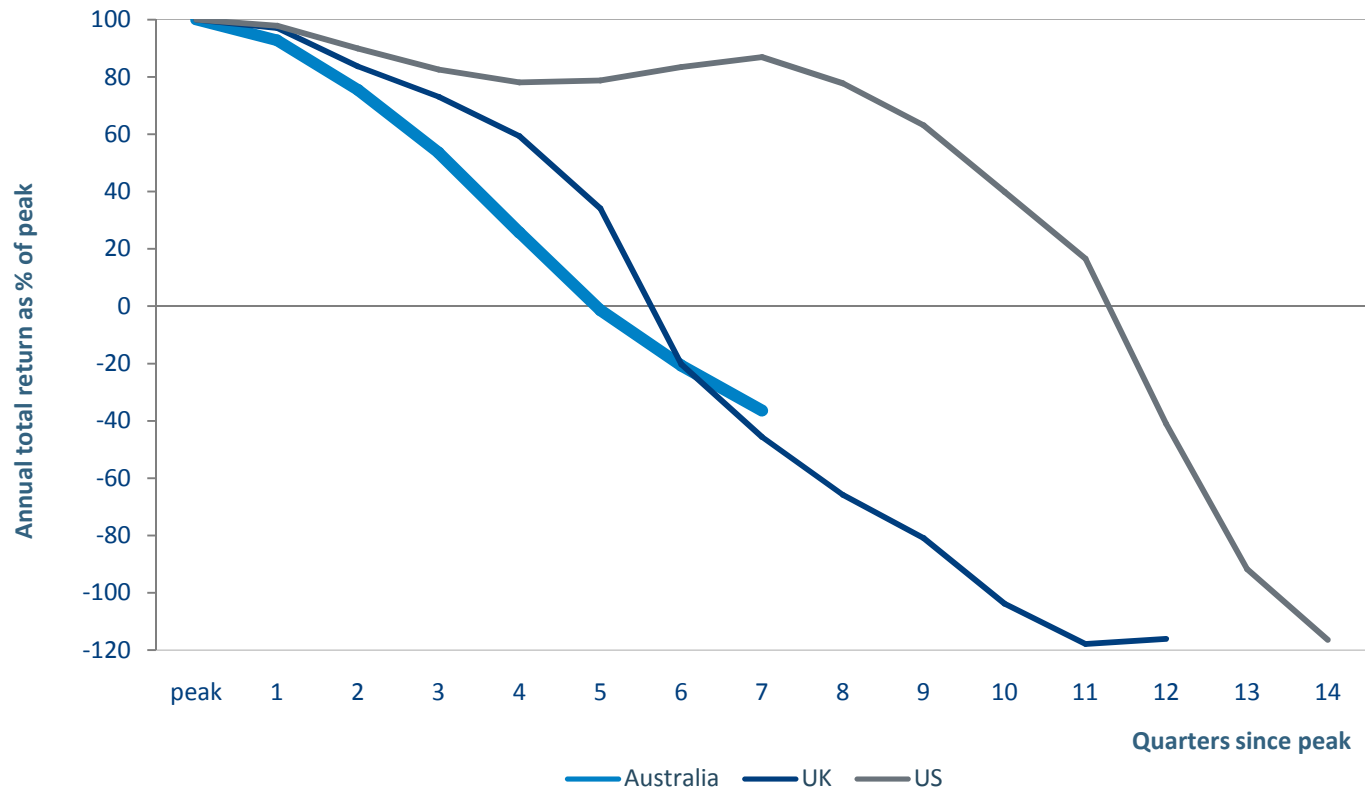
Annual capital growth cycle



Source: PCA/IPD

Global cycle – Australia holding up?

Relative falls in annual total returns since peak to June 09



Source: PCA/IPD

Distressed asset sales – surprisingly low

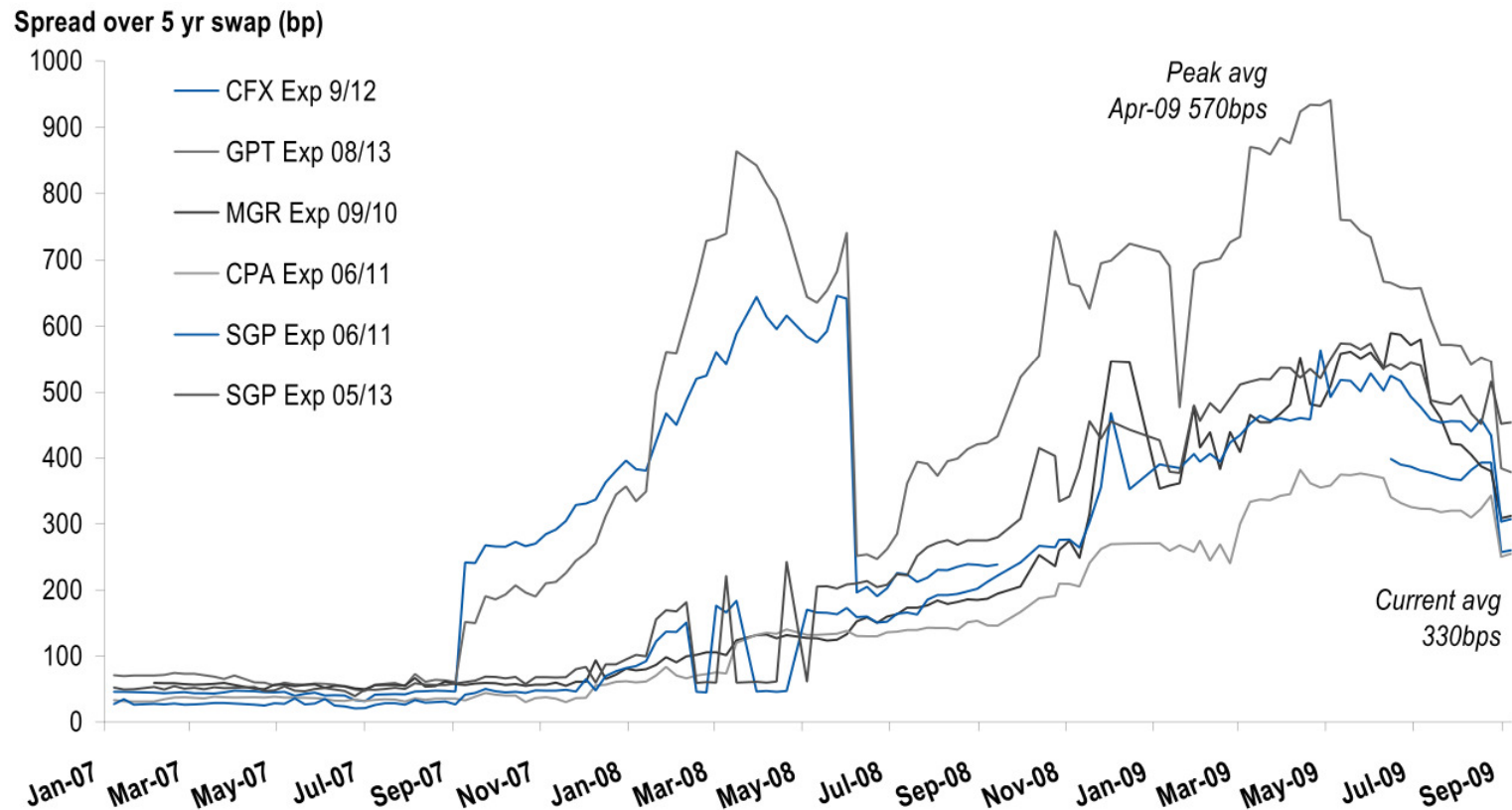
- ◆ Banks have not forced sales this time around
- ◆ Australian real estate market held up better than UK & US
- ◆ Bank focus was getting borrowers to re-capitalise early
 - ◆ REITs lead charge - \$12bn in re-capitalisations
 - ◆ Unlisted funds – still have issues - re-caps more difficult
- ◆ LTV loan covenants have been breached in many cases
 - ◆ But banks have focused on cashflow and debt servicing ratios
- ◆ Expect banks to move more assets off books as market recovers

Asset values – near the bottom?

- ◆ Low transaction volumes since GFC started
 - ◆ Only one regional retail centre sold – 1/6th of Highpoint - 6% cap rate
 - ◆ Only one office building >40,000 sq.m. – 15 William St, Melbourne – 8.8% cap rate
- ◆ Change in sentiment – sellers now pulling assets off market
- ◆ Banks have not flooded the market with forced sales
- ◆ Economic recovery – assisting real estate recovery
- ◆ Further re-pricing correction between prime and secondary
 - ◆ Secondary asset values to remain under pressure

Debt remains expensive

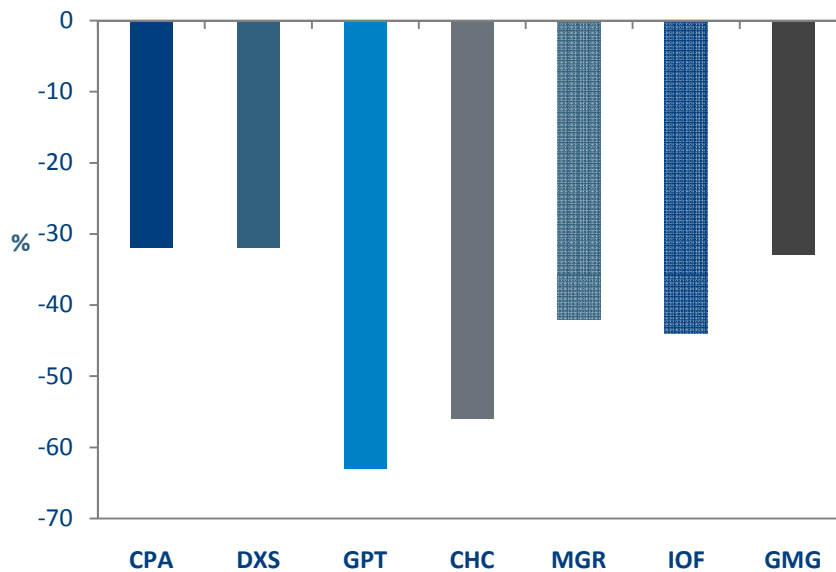
Medium term note's issued by REITs



Source: Reuters, JP Morgan

Capital raisings – at what price?

REITs – discount to pro-forma NTA



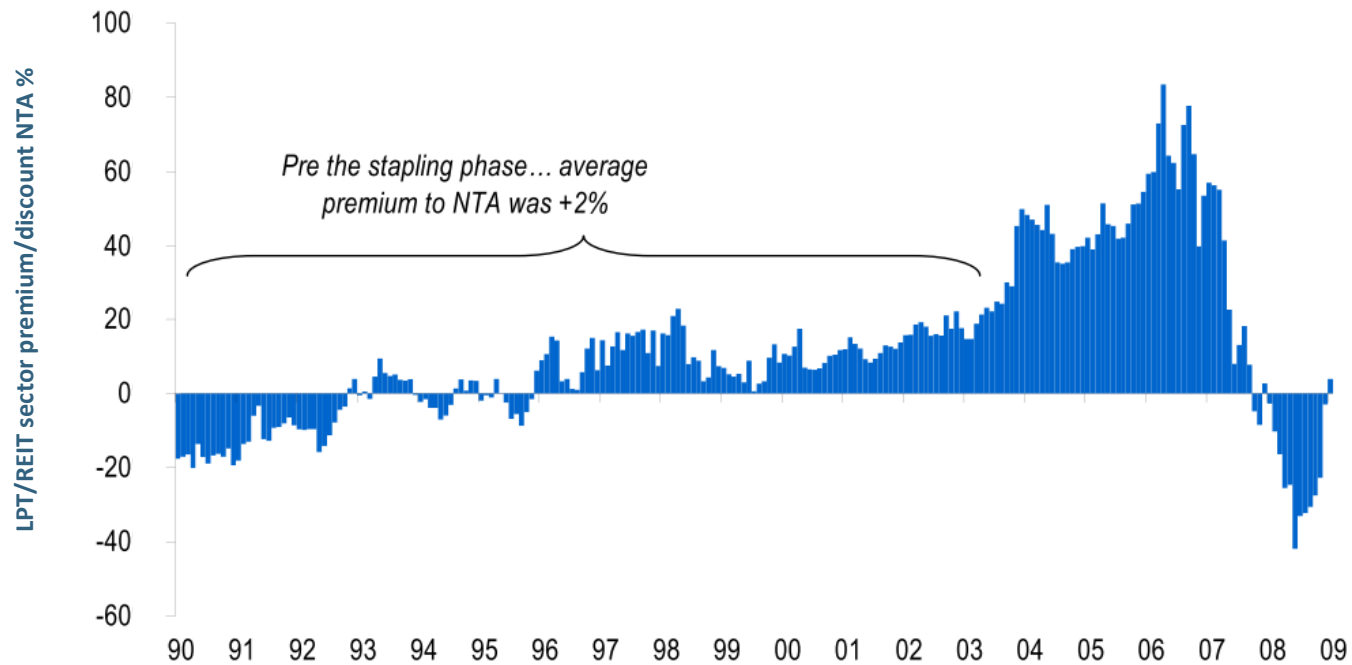
Source: Company reports

Debt refinancing and availability:

- ◆ Record issuance of REIT capital - \$12bn in 2009
- ◆ REIT issues at large discount to NTA
- ◆ Unlisted funds (esp retail funds) – harder to raise capital quickly and at large discounts
- ◆ REITs are now stronger, well placed
- ◆ Some unlisted funds still have issues still to work through

REIT pricing – back in the game?

Property trust sector premium/discount on NTA

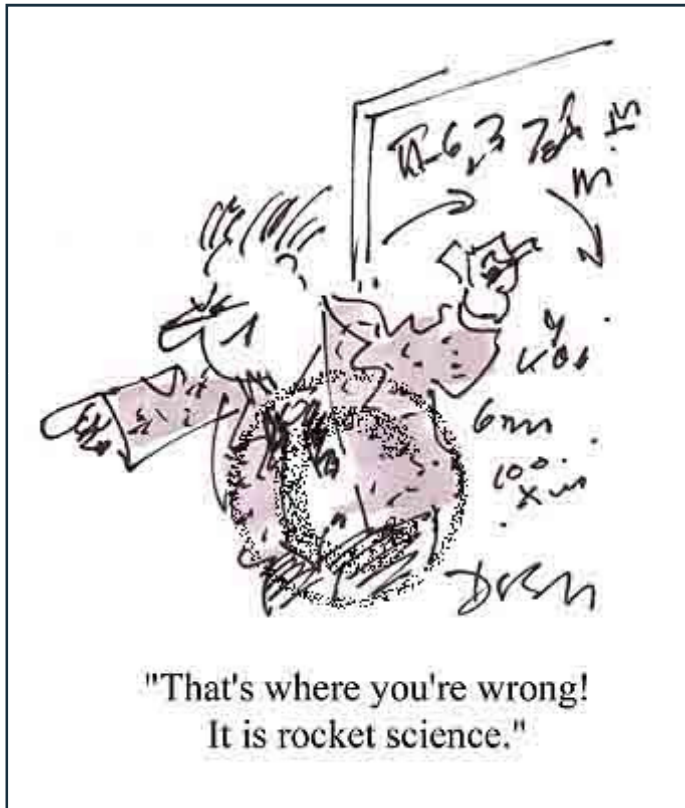


Source: J.P. Morgan

Surviving the future

Issues going forward

Issues the Industry must address



Back to basics – Investors want:

- ◆ less and better mgt of leverage
- ◆ focus on sustainable income
- ◆ sustainable payout ratios
- ◆ simpler structures
- ◆ greater transparency
- ◆ changes to fee structures and greater alignment
- ◆ independent oversight

Issues the Industry must address



Public perception & trust

- ◆ Industry needs to win back investors
- ◆ We've let many investors down – especially retirees
- ◆ Managers must remember investors come first
- ◆ Need clear and transparent message – no surprises
- ◆ Some manager brands are damaged, some terminally

“This is what we call a ‘true to label’ issue...A-REITs engaged in much more risky activities than was realised... these are lessons that must be taken on board”

Jeremy Cooper, Deputy Chairman, ASIC, 11/03/09

Issues the Industry must address



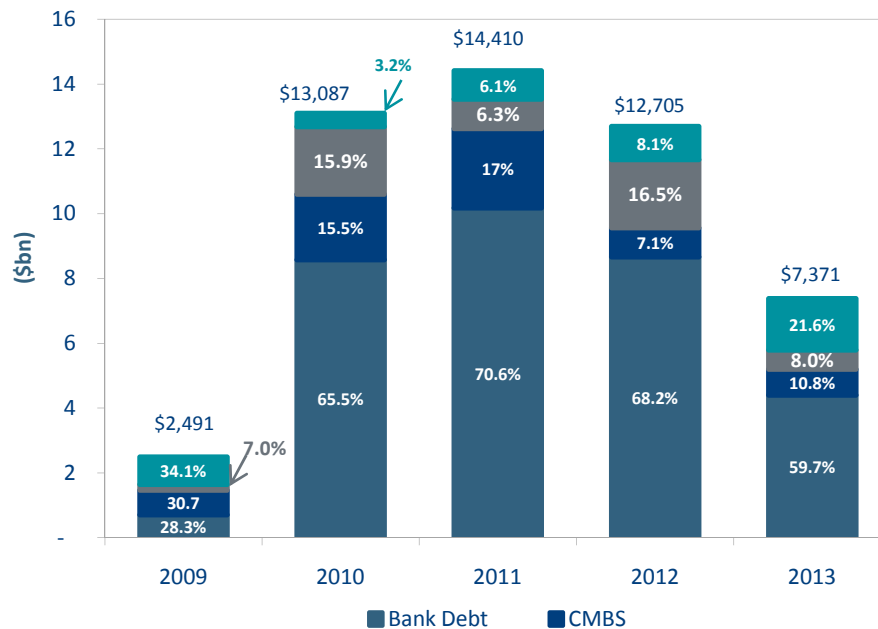
Good old-fashioned asset management – the key to generating alpha

- ◆ Real estate markets inefficient – take advantage
- ◆ Ensure assets are being operated on the most efficient and economical basis
- ◆ Maintain an appropriate tenant mix with the goal of maximising rental revenue and managing risk exposure
- ◆ Foster exceptional tenant relationships
- ◆ Refurbishment, re-positioning or redevelop existing assets

Performance driven by skill rather than just market movement

Issues the Industry must address

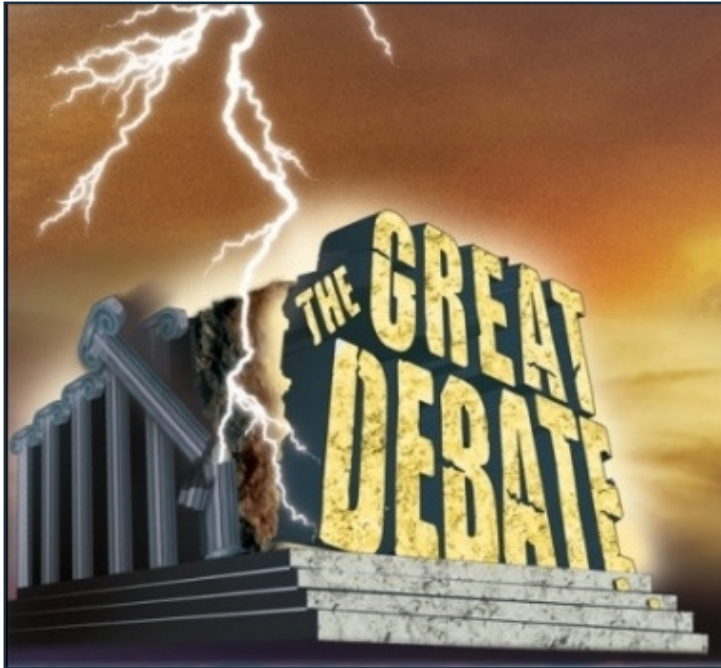
A-REIT debt expiries by type: 2009 - 2013



Debt refinancing and availability:

- ◆ Underwriting standards tough, margins high, more emphasis on recourse
- ◆ Sector will continue to de-lever
- ◆ Super funds/SWF's could be a potential new source of debt
- ◆ Australian property needs to broaden debt sources beyond big four banks

Issues the Industry must address



REITs vs direct – ongoing debate?

- ◆ Industry must support both forms of investment
- ◆ REITs will return to more historical long-term performance
- ◆ REITs will continue to be used as liquid form of real estate
- ◆ Short-term pricing arbitrage between REITs and direct property will continue – driven by lag in direct property valuations
- ◆ For many investors – both will have a place in their portfolio

The next cycle?



What rules must we remember?

- ◆ Capital flows at certain times in the cycle will overwhelm real estate fundamentals
- ◆ Property survives on equity and debt capital – but a balance is needed
- ◆ Risk matters – allocating capital efficiently is about paying attention to relative value – are you being properly compensated for the risk being taken on?

PCA Blueprint

Blueprint

for the Property Investment Industry

Property Council members have developed a *Blueprint for the Property Investment Industry*.

The goals that guide the *Blueprint* were developed at a workshop of senior property executives held in April 2009.

The draft *Blueprint* was discussed at the Capital Markets Leaders Summit 09 held in Canberra in June 2009.

The six point plan of action arose from the Summit deliberations.

The *Blueprint* envisages a future where:

1. Property would be a **distinct asset class**
2. Property would be a magnet for **stable equity and debt flows**
3. The property asset class would be **domestically and internationally relevant, competitive and attractive**
4. The property asset class would be a **trusted, safe and reliable investment choice**
5. Property would be subject to **fair taxes and rational regulation**
6. The property asset class would offer a **diverse menu of investment choices**
7. Property would be an **attractor of talent** – the best and the brightest
8. Property would be underpinned by **strong underlying user demand**
9. The property asset class would be **socially and environmentally responsible**



Six Point Plan of Action

Action One – Secure deep and liquid debt markets

- Lobby the Australian Government (in alliance with key stakeholders) to:
 - Improve the operation of the Basel II framework in Australia
 - Extend its guarantee to AAA rated asset-backed securities
 - Equalise the fee it charges for the banking guarantee rollover relief fund
 - Establish a government-backed emergency deeper, more diverse secondary debt markets
 - Remove regulatory barriers and promote deeper, more diverse secondary debt markets

Action Two – Engage regularly with key stakeholders and customers

- Establish a regular dialogue with banks at the most senior level
- Establish a specific home within the Property Council for the unlisted property investment community
- Establish a P20 group and meetings: the 20 key decision-makers within the asset consultant, research and superannuation and retail investor communities
- Hold a 'Davos-style' event that attracts the top 20 super/pension fund CEOs/heads of property
- Establish an event for rising stars within the investment property community
- Develop stronger alliances with key industry bodies – ABSI, ASFA, FPA, IFSA.
- Strengthen alliances with global property industry bodies

Action Three – Prepare a voluntary guide to leading industry practices

- Prepare guidelines that outline world class principles and practices for financial and corporate responsibility performance reporting, including standard property industry definitions and a supporting resource kit
- Agree on common labels for different property investment products and vehicles
- Modernise real estate valuation practices in consultation with regulators, accounting professions, the API and RICS

Action Four – Implement a market and customer outreach campaign

- Regularly publish comprehensive data on key property industry metrics, in association with information alliance partners
- Launch an online version of *Build Your Wealth*, based on the www.REITsafe.com or www.REIT.org sites, that will educate investors and advisors on the four quadrants of property investment opportunities
- Conduct property investment road shows in conjunction with ASIC, ASFA, ASX, FPA and IFSA
- Promote the Property Council's corporate responsibility reporting guidelines and the industry's positive news stories

Action Five – Advocate for fair taxes and rational regulation

- Ramp-up the Property Council's core reform agenda – lower taxes, less red tape and increased nation-building investment
- Commission a credible econometric model that calculates the contribution of the property industry to the community and assesses the impact of legislative proposals
- Negotiate legislation to modernise Australia's managed investments regime
- Improve the international tax competitiveness of investment management regimes
- Develop a model easy-to-use PDS, endorsed by ASIC and recognised internationally
- Reform international accounting standards relevant to the property industry
- Promote tax incentives for green buildings

Action Six – Invest in professional development

- Facilitate the establishment of at least one international standard graduate school in property investment finance
- Work with professional societies to establish dedicated 'homes' for property-related capital markets professionals
- Revise our Property FPA's vocational guidance primer for students
- Update the Property Council's suite of professional development programs

Conclusion

Conclusion

- ◆ Worst behind us in Australian real estate market - cautious optimism prevails
- ◆ Investors will support listed and unlisted real estate funds that offer:
 - ◆ Quality management with clear investment strategy
 - ◆ Lower and better management of leverage
 - ◆ Sustainable income with appropriate pay-out ratios
 - ◆ Simpler structures
 - ◆ Greater transparency
 - ◆ Greater alignment of fees based on management and performance
 - ◆ Independent oversight
- ◆ The industry is responding and will adapt
 - ◆ REITs are getting house in order
 - ◆ Listed and unlisted managers are looking to restructure and become more transparent
 - ◆ PCA's BluePrint for Property Investment Industry step in right direction
- ◆ There will be winners and losers

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