



resolution**CAPITAL**
real estate securities solutions

RESOLUTION CAPITAL CORE PLUS PROPERTY SECURITIES FUND

MARCH 2011
QUARTERLY INVESTMENT REPORT



AUSTRALIAN REAL ESTATE SECURITIES

Fund Investment Performance

The Resolution Capital Core Plus Property Securities Fund underperformed the S&P/ASX 300 AREIT Accumulation Index by 28 basis points for the quarter ending 31 March 2011.

Period Ending 31 March 2011*

	Quarter %	1Year %	2Years % p.a.	Since Inception [#] % p.a.
Fund	3.46	5.38	22.55	-6.95
Benchmark	3.73	4.74	21.95	-10.70
Difference	-0.27	0.64	0.60	3.75

*Returns are expressed after deducting investment management costs.

[#] 30 September 2008

Resolution Capital Core Plus Property Securities Fund Unit Price

	Entry	Exit
31 March 2011	\$0.7375	\$0.7331
31 December 2010	\$0.7223	\$0.7179

Market Performance

Market Overview

	31 Mar 2011	31 Dec 2010	Quarterly Total Return
S&P/ASX 300 (GICS) A-REIT Accumulation Index	19,891	19,175	3.7%
S&P/ASX 300 Index	35,640	34,560	3.1%
UBS Global Investors Index AUD (Unhedged)	959	919	4.3%
UBS Global Investors Index AUD (Hedged)	1,256	1,192	5.3%
10 Year Bonds	5.50%	5.51%	
90 Day Bills	4.89%	4.96%	
AUD/USD	\$1.03	\$1.02	1.0%

Commentary

We apologise for our delay in reporting to you for the quarter ended 31 March 2011.

The S&P/ASX A-REIT Property Accumulation Index produced a total return of 3.7% for the quarter ended 31 March 2011.

The RCL Core Plus Fund underperformed the benchmark by 27 basis points for the quarter (after fees) principally due to its underweight exposure to stocks subject to corporate activity, particularly CharterHall Office REIT and Centro Retail Trust. Exposure to Tokyo Stock Exchange listed AEON Mall Co also detracted from performance. Positives included our over benchmark weight exposure to ING Office (since renamed Investa Office) and Ardent Leisure.

Several external events influenced global investment markets during the quarter including devastating earthquakes in Japan and New Zealand, rising oil prices emanating from unrest in the Middle-East/North Africa and ongoing sovereign debt concerns in parts of Europe. On the positive side, the US economy showed tentative signs of steady improvement albeit the Federal Reserve continues to espouse a “lower for longer” approach to interest rates until the economic recovery firmly takes hold particularly in relation to lowering the unemployment rate. The RBA’s hawkish stance on interest rates seemed to pause during the quarter, the rapid rise of the A\$ reducing pressure to do so. These events provided some support for A-REITs given the greater level of income security offered by the underlying, high quality, real estate.

During the quarter, A-REITs prices benefited from relatively low equity capital issuance, which impacted returns in the preceding quarter. In addition we expect at least some of the proceeds of the \$1.2 billion ING Industrial Trust takeover, finalised during February, together with quarter and half year cash distributions were re-invested back into other REITs in the sector.

A-REIT news of major significance included:

Centro – moving toward resolution?

The saga around Centro Properties Group (CNP) and its affiliates came closer to being finally untangled when the debt-laden group entered into contracts to sell its portfolio of 588 U.S. shopping centres to Blackstone group for US\$9.4bn, only marginally below the group’s latest book value. The disposal will leave CNP with 112 Australian and New Zealand managed retail assets. The sale reduces Centro Retail Group’s (CER) gearing from 75% to around 43% whilst CNP still has *negative* equity of \$2.51 per share.

In simple terms the majority of CNP’s senior debt holders have proposed to wipe out all junior security holders, including unitholders, for \$100m. Included in this payment is the settlement of the class actions against Centro. Furthermore various Centro entities are in talks to amalgamate different portfolios into a new listed fund. This new vehicle would have Australian regional and

sub-regional shopping centres worth around \$4.6bn. CER had a strong performance this quarter, up 43.8%, but CNP lost 63.8%.

It's significant that Blackstone was willing to acquire US\$9.4bn of real estate in one swoop. Not long ago investors were lining up to exit real estate private equity vehicles. The line is still there, but these days it's with investors wanting to get in. (Subsequent to quarter end, another of Blackstone's funds launched a takeover offer for Valad Property Group).

IOF / Investa

ING Group's drawn-out strategic review of its real estate funds management platform entered its next chapter when ING Management (IML) agreed to transfer the management of ING Office Fund (IOF) to Investa Property Group for an undisclosed price with Investa also acquiring a 2.5% stake in IOF currently owned by ING.

ING Group was understood to have received a number of offers, including a management buyout as well as an offer from Cromwell Group (CMW) to acquire all IOF units and internalise management, however these were rejected by the ING board. Perhaps the most perplexing aspect of the deal relates to the intention initially to only partially internalise IOF at some point in the future. The new manager has offered IOF unitholders the option to acquire a 50% interest in the management platform of IOF and Investa once IOF's Australian assets reach \$3.5 billion (Australian AUM is currently \$1.6bn and total AUM is \$2.6bn). The timing has not been indicated and whilst a unitholder meeting will be required, A-REIT investors have rarely done well from these transactions.

While we hold Investa's property team in high regard, we are at a loss at how little attention has been drawn to the inherent conflicts of interest with the new manager. Investa has a large Australian office portfolio, high leverage with short term maturities and is partly owned by Morgan Stanley private equity funds which at a certain point want to exit.

We have been assured that there are no poison pills in place and the board of IOF will remain majority independent. Nevertheless in our view this deal does little to resolve the future of IOF – it adds complication where simplicity and alignment should be the outcome. Disappointingly, once again, stewardship of investors' capital has been passed from one manager to another without a vote.

Charter Hall Office REIT

In early 2010 the Charter Hall Group (CHC) bought the management rights for what is now called the Charter Hall Office REIT (CQO). At the time we were disappointed that the new management basically announced a continuation of the existing strategy, which hadn't been very beneficial for unitholders in the past. At the full year results in August 2010 CQO mentioned that it was exploring investor demand for a CHC managed private equity fund to co-invest in its U.S. assets. During the first quarter of 2011 a U.S. hedge fund and 5% shareholder in CQO agitated against this proposed related party transaction, arguing amongst other things that a higher price might be achieved in the open market. After an exchange of letters back and forth CHC increased their stake in CQO to 10% and announced they had appointed BoAML to explore a range of options including an outright sale of the U.S. portfolio. CQO outperformed the A-REIT sector strongly during the quarter on the back of the above news.

Buy backs

During the quarter Charter Hall Retail Trust (CQR) announced that it would buy back up to \$20m worth of its own units. Management stated that it would only do so if the discount to NTA was large

enough. CQR is releasing a significant amount of equity by selling U.S. and New Zealand properties. In our view this buyback should be viewed as a token, because it represents only around 2% of the units on issue.

Later in the quarter GPT, Mirvac Group (MGR), Challenger Diversified Property group (CDI) and Commonwealth Property Office Fund (CPA) flagged buybacks as possibilities to reduce their persistent discount to NTA.

Recently CPA sold a call option to GDI Property Group to buy three Perth assets for a combined value of \$152 million. This option is exercisable between 1 and 15 July 2011. If exercised, CPA would contemplate a buyback with the sale proceeds if the metrics made sense. Readers would recall that CPA's discount to NTA increased considerably in November 2010 after they issued shares at a large discount to NTA to buy three office buildings in Melbourne.

Some A-REIT managers clearly struggle with the capital allocation decision of when to buyback or issue stock. At a recent AFR real estate conference we presented our views on some of these issues in detail. A transcript of this presentation is included in Appendix I.

Remuneration

In response to shareholder backlash Mirvac Group CEO Nick Collishaw took a voluntary 25% reduction in his fixed remuneration. Disappointingly, in return the company granted Mr Collishaw a one-off cash award linked to Mirvac's performance. A threshold to any payment will be Mirvac delivering average annual Total Shareholder Return (TSR) of 12% over the period from April 2011 to December 2014. If a minimum target security price of \$1.60 is achieved, the award payment will be \$702,000. A maximum entitlement of \$1.23 million will be payable if the closing share price is \$1.95. The company's last reported Net Tangible Assets (NTA) per unit was \$1.56, which makes the share price hurdle above somewhat unambitious.

GPT – not drowning, waving goodbye

GPT announced that it had disposed of its last significant offshore real estate exposure associated with its ill-fated global real estate ambitions. GPT was able to exit the remaining investment on a positive note, disposing of its US healthcare properties at a substantial premium to the previous valuation. GPT now is focused on Australian real estate investment and funds management within the retail, office and industrial property segments.

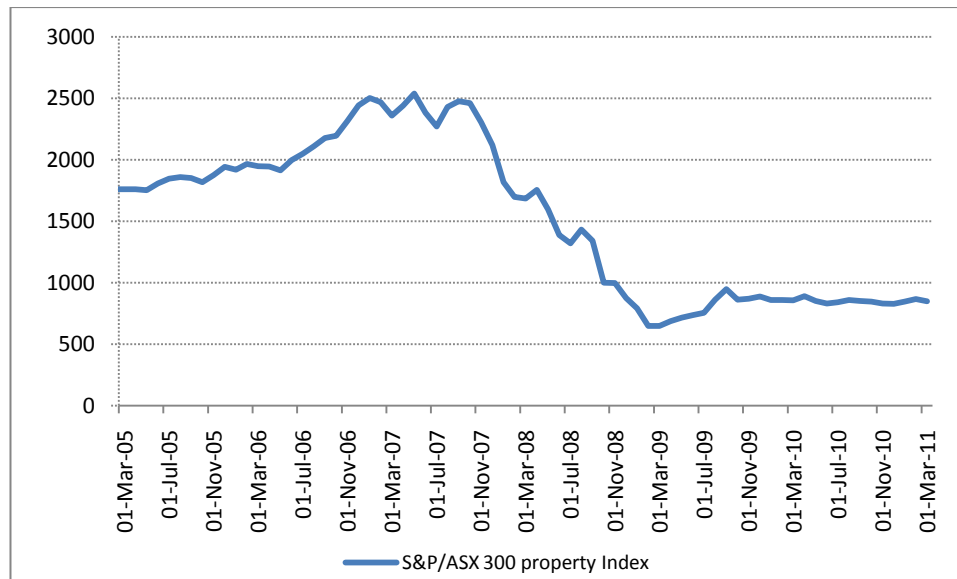
Frank Lowy - End of an Era

In March, Westfield Group (WDC) announced that Frank Lowy will step down from Executive duties at Westfield's May AGM after more than 50 years. Mr Lowy will remain Chairman of the company whilst Peter and Steven Lowy will assume the roles of joint Chief Executive Officers (previously joint managing directors) whilst David Lowy has resigned from the position as Non-Executive Director of WDC.

Reporting Season

The A-REIT Reporting season was bereft of major surprises. Most vehicles reported stable or increasing occupancy levels and evidence of increasing market rents. A-REIT managers reconfirmed previous distribution forecasts with many expecting to achieve real distribution growth in the short term at least.

S& P/ASX 300 A-REIT Price Index



Source: Bloomberg

A-REIT Market Comment

Whilst the March 2011 quarter return of 3.7% was respectable, in our opinion sentiment toward A-REITs remains glum. Whilst the sector had a reasonable quarter it should be put in the context of a lack lustre total return for the year of 4.7%. A-REITs appear to be afflicted by a more chronic malady caused by a number of factors including:

- Upward pressure on interest rates. Whilst there are encouraging signs of improvement, compared with offshore REITs, A-REITs are still confronted with high interest rates and borrowing margins. The latter being due to the relatively uncompetitive/shallow traded debt market. High finance costs are making it difficult for A-REITs ability to enhance returns through acquisitions or developments.
- The sector's recent poor performance and relatively modest dividend yield (circa 6%) is insufficient to tempt Mums & Dads away from the safety of government guaranteed bank deposits yielding 6% or franked industrial stock dividend yields.
- A lack of interest from domestic institutional investors. It would seem these investors have a renewed fervour for direct/unlisted real estate thanks to the perceived lower volatility of the large, well capitalised wholesale funds which generally are perceived to have less agency risk compared with A-REIT management. Associated with this, the demise of dedicated domestic A-REIT funds means that the growing superannuation pool is largely by-passing A-REITs.

With the A-REIT sector trading on average at NTA there is limited compelling headline data to entice general equity investors back into the space, particularly given the boom conditions in the resources sector.

Concerns about aspects of the real estate market do not help the mood. For example, the impact of internet retail on the sector's shopping centres, which forms the backbone of the A-REIT sector, is not instilling confidence. Furthermore, the elevated level of residential prices is impacting sentiment toward REIT majors such as Stockland and Mirvac which derive 20-30% of their earnings from residential trading.

- The significant rise of the A\$ is working against foreign investor interest in the sector. Indeed the following table highlights that from an unhedged US\$ perspective, returns from

the A-REIT market have been more competitive, particularly over a 2 year period, for many offshore unhedged investors because of considerable gains on currency exchange.

- Investors are increasingly concerned about the offshore exposure of Westfield Group (WDC), still the sector's largest stock with an index weighting of circa 30%, the A\$ value of which is eroded by the strength of the local currency. Approximately 64% of WDC's owned assets are located in US, UK and New Zealand.
- Ongoing concerns about A-REIT corporate governance issues, most recently focused on Charter Hall Office Fund and ING Office Fund which we discussed earlier.

It is indeed a powerful blend of negatives. However, we believe many of these factors have largely played out or are cyclical and beyond the control of the REIT participants. It may be the antithesis of the resource sector's super cycle.

UBS Investors Index – Annual Compound Returns (calculated in USD)

	Returns For the Period Ending March 31, 2011								
	YTD	One Mth	Three Mths	Six Mths	One Year	Two Years (1)	Three Years(1)	Five Years(1)	Ten Years(1)
Global	5.5%	-0.6%	5.5%	13.0%	23.9%	53.6%	-1.2%	0.8%	11.8%
US & Canada	6.9%	-1.2%	6.9%	14.8%	25.3%	62.7%	2.4%	1.7%	11.7%
Cont Europe	8.9%	4.4%	8.9%	10.8%	22.5%	47.6%	-2.9%	3.1%	16.4%
UK	8.7%	-3.3%	8.7%	17.3%	20.2%	41.8%	-18.8%	-12.9%	4.9%
Hong Kong	-1.6%	1.0%	-1.6%	12.0%	37.2%	55.6%	18.0%	12.3%	15.2%
Japan	-8.2%	-6.4%	-8.2%	13.5%	25.2%	23.4%	-0.7%	2.9%	n.a.
Australia	4.5%	-0.4%	4.5%	9.1%	18.0%	48.1%	-9.6%	-0.9%	11.8%
Singapore	-1.6%	2.0%	-1.6%	-1.6%	22.4%	54.3%	3.2%	9.3%	n.a.
New Zealand	-0.5%	3.7%	-0.5%	9.6%	16.8%	24.9%	-1.0%	7.1%	n.a.

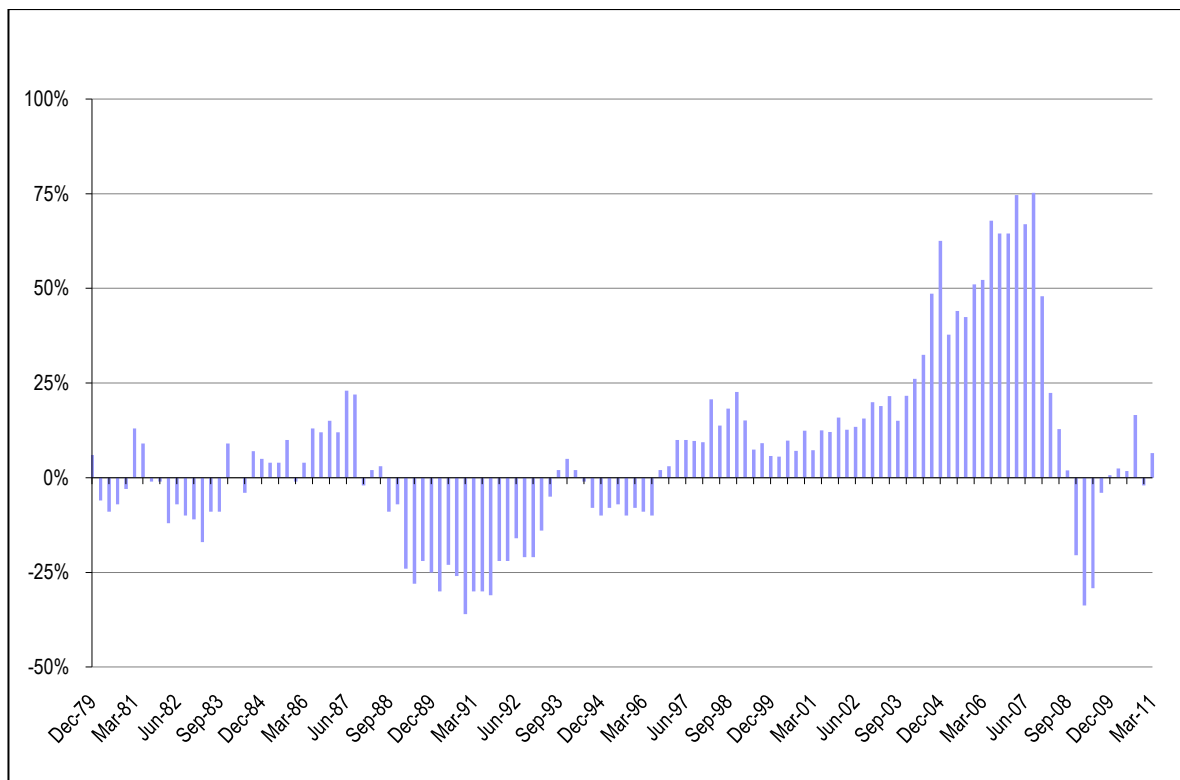
Source: UBS, S&P

Goldilocks Scenario - the A-REIT sector seems just right

For reasons we will discuss, we believe A-REIT values are fair and that, arguably, the sector now provides true diversification. We note this is in contrast with our view of the 2000-2007 period when we witnessed the sector introducing more and more risk without the market seeming to be overly perturbed.

The Price to NTA chart below of the A-REIT sector demonstrates that over the past 25 years the sector has traded at well above and below NTA. Whilst we don't believe price to NTA is necessarily always equilibrium, it is at least a useful reference point.

Premium to NTA

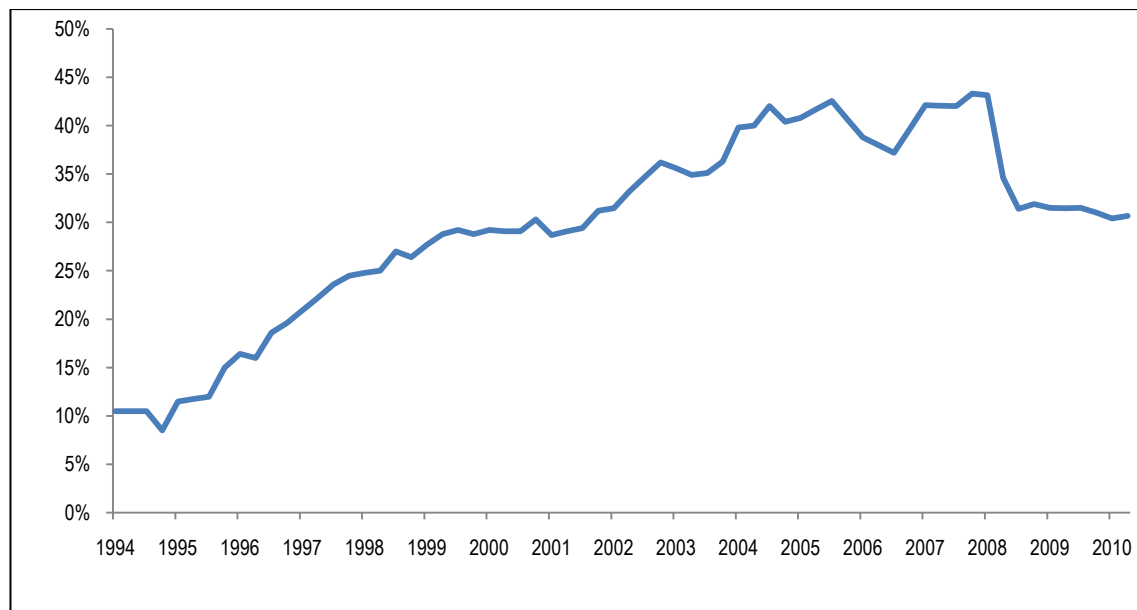


Source: BoAML

We could consider two distinct periods when the sector traded at a significant premium to NTA between 2001 to 2007, and at a significant discount between 1988 and 1993.

Many would like to believe that we will soon return to the heady days of trading at a sustained premium to NTA as was the case in the decade or so up to 2007. However it is crucial to put this period into perspective and the changing nature of the sector. It is important to recognise this was a period of falling interest rates and rising property values, when A-REITs leveraged up, expanded into offshore markets and funds management which allowed greater financial engineering, were subject to elevated M&A activity (which often resulted in a shift from external to internal management) and when dedicated REIT funds were the favoured means of channelling compulsory superannuation into real estate.

Gearing (Debt to Assets)



Source: JP Morgan

Conversely, we do not believe there is a high risk, in the next 12 months at least, that we could return to the period 1988 to 1993 when REITs regularly traded at a significant discount to NTA. Whilst initially, investors fled listed REITs (known then as listed property trusts) in favour of unlisted vehicles post the 1987 the stock market crash, there was consequently a wave of over development (exacerbated by lax bank lending practices) which resulted in a major property downturn. Today the market does not face an oversupply threat and once again many non-institutional unlisted property trusts have again made the same mistake of over-leveraging resulting in significant asset price declines, and unlike listed REITs, frozen redemptions.

Stockland Trust Group – A case study

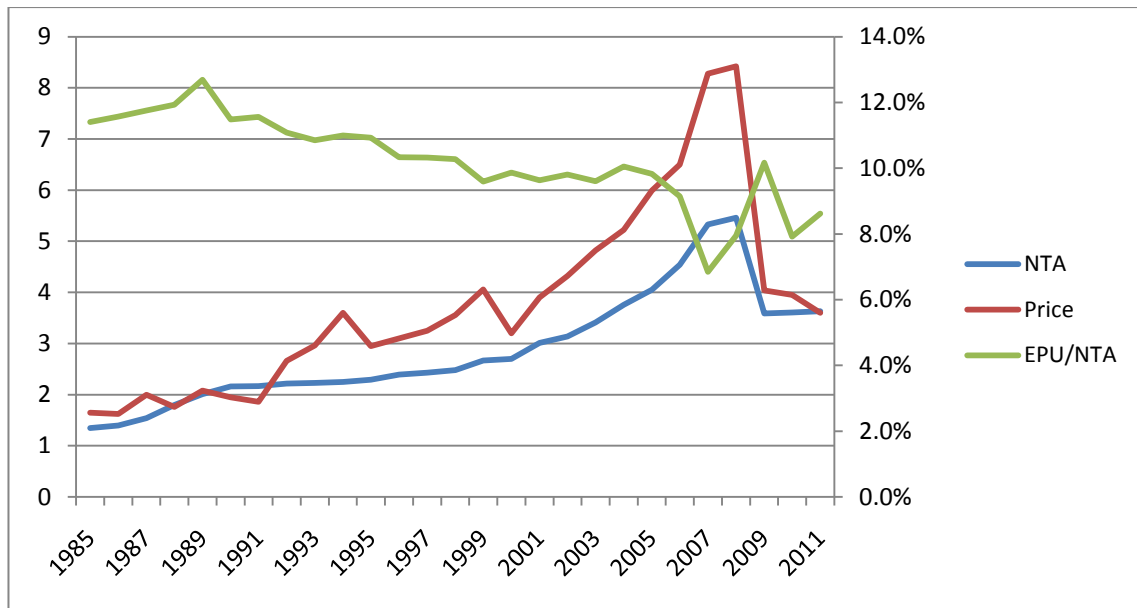
At this point it might be of interest to consider a case study.

As a consequence of M&A activity, few vehicles have a history that goes back to the last economic recession and major real estate downturn in Australia. Because of its long history and relatively stable business and capital structure, Stockland Trust Group (SGP) provides an interesting case study for understanding the long term pricing patterns of A-REITs.

The structure and nature of Stockland today is not dramatically different to how it looked in the late 1980s: internally managed, focused on leading sub-regional shopping centres and residential development albeit the quality of the investment portfolio quality is arguably much improved. The major differences are that SGP has added retirement village investment as a core business (currently representing 10% of earnings) and, unlike its cash positive balance sheet up to the early 90s it now is levered with debt to assets of approximately 20%, having peaked at around 30% in 2006. The dividend pay-out ratio has recently been cut from 95% in the decade up to 2007 to now around 75%. This is close to its pay-out ratio policy up to the early 90s.

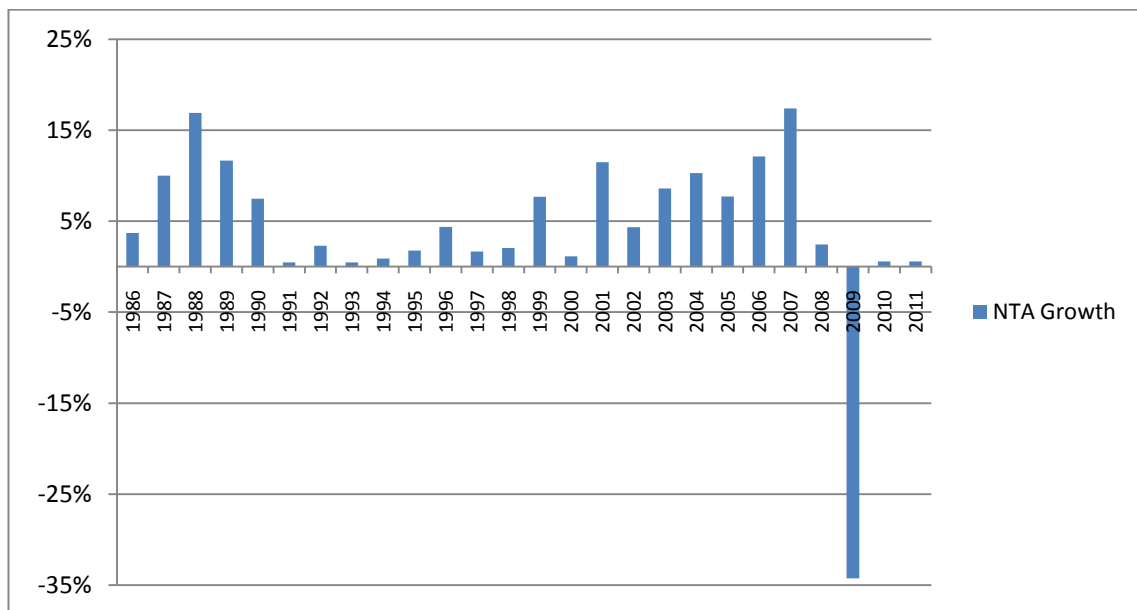
The charts below capture the long term NTA and price of Stockland as well as its earnings yield. Since 1985, Stockland has achieved NTA growth in all years bar one, 2009. This NTA growth track record is remarkable as it captures the last property crash of the early 90's.

Stockland Trust Group



Source: RCL, IRESS

Stockland NTA Growth



Source: RCL

Its price to NTA trading pattern is not too dissimilar to the A-REIT sector over the long term, albeit its superior growth resulted in a greater premium in the decade up to 2007.

Although SGP did undertake dilutionary equity raisings in 2008-09, as evidenced by the sharp decline in stated NTA and EPU, these were far from the worst in the sector.

It does however highlight the agency issue that many observers are grappling with – can A-REIT management be trusted? This contrasts with the high regard for management only a couple of years ago and highlights the transient nature of investor sentiment. It seems risk is best judged through the rear view mirror and investors become complacent about agency risks emerging in other areas. For these reasons, we do not see any of these differences as reasons to substantially discount our valuation performance observations.

Today, Stockland's securities trade on an earnings yield of around 8.75% and close to or just under its stated NTA of \$3.63 – arguably representative of the A-REIT sector pricing at this point. The market is paying no premium for the value of the property management and development platform of one of Australia's leading residential land development enterprises.

Given the stock has traded at an average 25% premium to NTA since 1985, one could suggest that at current prices SGP is good value. However, as we noted earlier in relation to the sector, we believe the late 90s/early 2000s was an exceptional period which should be discounted.

We believe a similar trading pattern of the period of late 1988 to 1993 is likely to emerge when Stockland ordinarily traded at close to its appraised book value. This period has some interesting parallels with the current environment, namely a listed real estate sector out of favour with most institutions and retail investors preferring unlisted forms of real estate – either direct or unlisted property trusts. It was also a period where investors were dealing with a stock market bubble and crash and a banking system under duress, again not dissimilar to the current environment except that real estate markets are today in much better shape largely thanks to the absence of over development.

Up until the early 90s, there was the concern that SGP's sub-regional shopping centres were vulnerable to the competitive forces of the dominant regional malls which proved to be unfounded. Today there is widespread concern about retail in general due to the perceived risk from internet retail. Similarly, in the early 90s investors also had concerns about the state of the residential market due to high interest rates (mortgage loans reached 20% compared with around 7% today albeit drifting higher) again not unlike today's environment. The major differences were the absolute levels of interest rates, inflation and unemployment.

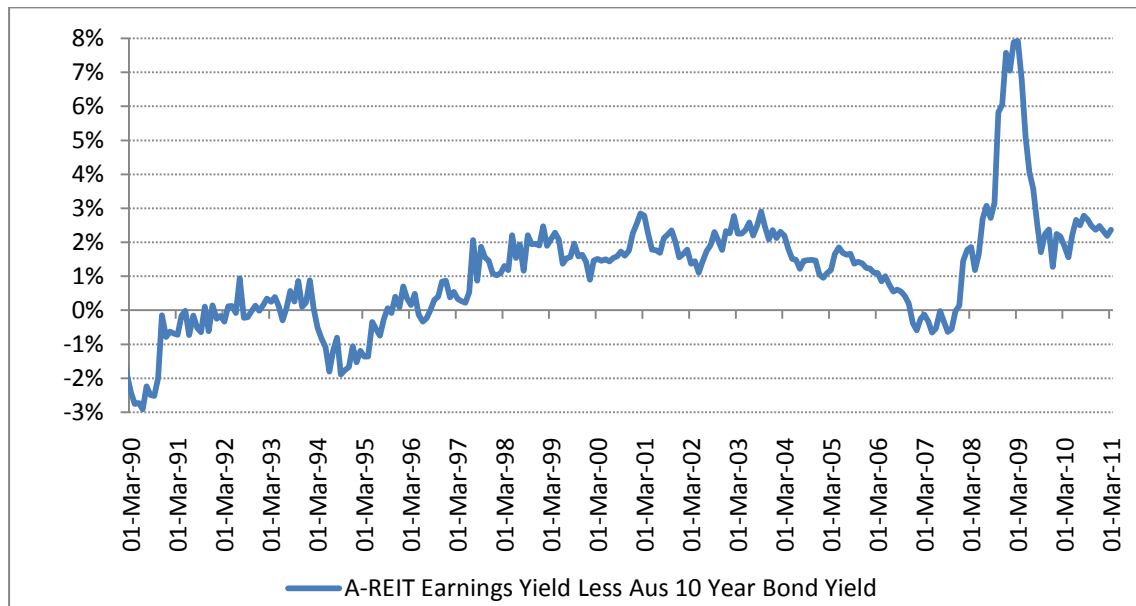
That said, history also suggests downside appears limited unless we enter into a prolonged period of declining asset prices in which case one should also be cautious about investment in unlisted real estate.

Conclusion – the sector looks “Just Right”

Hence, we believe value is slowly emerging in the A-REIT space.

- Commercial real estate fundamentals remain sound, vacancies are low by historic standards and construction activity is subdued. Given the generally high quality of their portfolios, A-REITs are well positioned to benefit from any upswing in tenant demand.
- Relative to bonds, A-REIT valuations do not look stretched.

A-REIT Earnings Yield Less Aus 10 Year Bond Yield



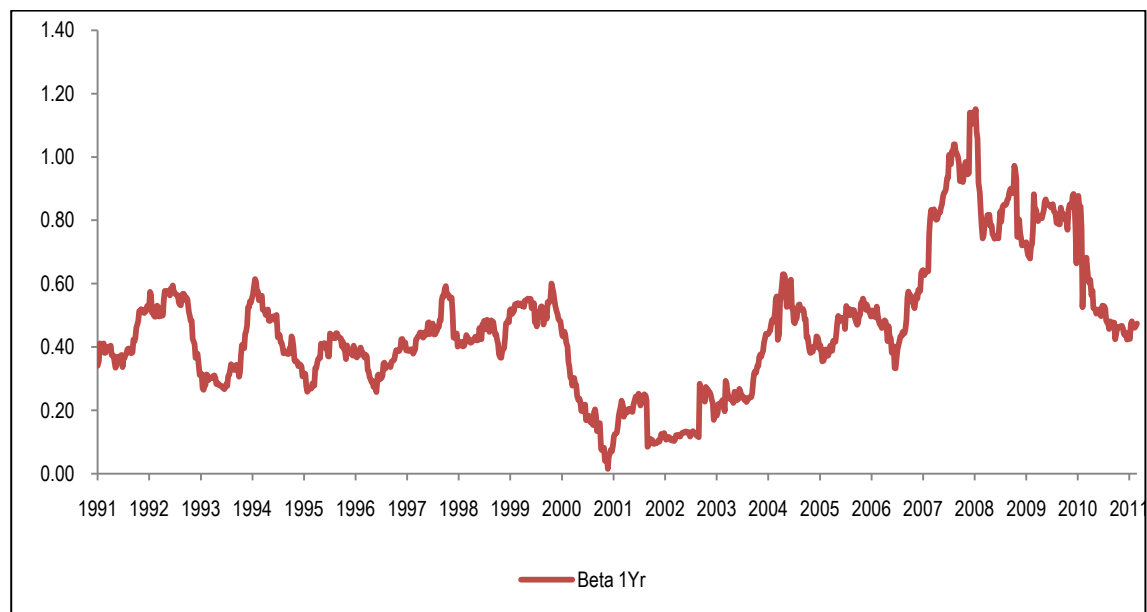
Source: Bloomberg

- Many A-REITs are trading at a discount to Net Tangible Assets (NTA), which is contrast with many unlisted funds of a similar quality which are trading in the secondary market, and raising capital, at NTA. Limited value is ascribed to the potential value creation of the management platforms of many of the vehicles.
- Takeover potential of a number of A-REITs underpins the sector if discounts to NTA persist.
- The potential for significant equity capital raisings, which has constrained the sector’s recovery, appears limited (we have learnt from painful experience that it remains a risk). Indeed the suspension of Dividend Reinvestment Programs, reduction in dividend payout ratios and increasing number of share buy-backs suggests the sector can well and truly fund its immediate capital needs without resorting to capital raisings.
- There are tentative signs of improving, and less costly, debt capital availability.
- Many A-REITs continue to rate highly on environment sustainability initiatives. This should place them in a strong position to attract and retain tenants leading to superior performance relative to others in the real estate market.
- Funds management and commercial property development represent a small part of the overall earnings and value of the sector. Financial engineering such as inappropriate distribution of foreign exchange hedging gains (in conjunction with high debt levels) has largely desisted. Offshore investment by those ill-equipped to do so has all but ceased. Acquisitions, typically debt fuelled, are absent and as such are not boosting short term

earnings growth. Bottom line, the sector now is focused on producing relatively secure returns from real estate, largely domestic and moderately levered.

- The benefits of liquidity appear to have been all but forgotten.
- Volatility has reduced and the sector's trading pattern appears to have decoupled from the equity market.

A-REIT Beta vs S&P/ASX 200 (Equities)



Source: JP Morgan

Hence, we believe the sector has redeemed itself and currently macro factors, ie largely outside management's control, are largely responsible for the direction of the market. Management will have to work hard to create value by disposing of lower return exposures and reinvesting in superior assets, including developing existing properties. It can enhance these activities with capital management initiatives such as selling property and using the proceeds to buy back shares if they are trading at a discount to the market value of the underlying real estate.

In summary, we expect the direction of REIT prices will be more closely related to the direction of property markets and rental growth. Management's task is to remain disciplined and add value. The sector is generating an earnings yield of 7.5% from the nation's leading real estate. Whilst by itself the dividend yield headline number of 6% is not outstanding, it should be recognised that this is based on an 80% pay-out ratio and hence is sustainable. In fact investors should reasonably expect this to grow by at least inflation over the medium to long term.

Apart from liquidity, naturally A-REITs must provide a point of difference and be capable of delivering competitive, risk adjusted returns. We believe A-REITs pricing is now at level which warrants attention relative to global REITs and direct property. Agency risk, whilst still present, is diminished by the greater scrutiny under which management finds itself. With most in strong financial shape and with refined strategies, many A-REITs are now credible investment propositions.

We continue to believe that A-REITs do not have the scale or quality of global REITs to be a permanent solution to Australia's superannuation needs, hence this is largely a tactical recommendation.

Given the significant changes to the sector combined with its pricing, perhaps it may be time to reconsider what role A-REITs can play in your portfolio.

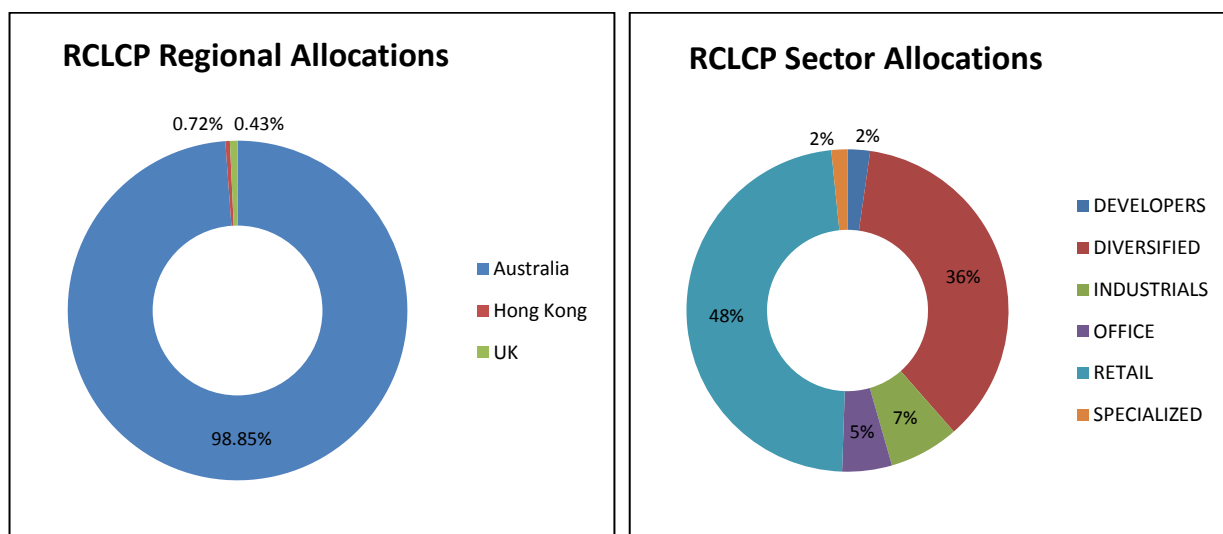
Portfolio Top 10 Stocks

Top 10 Portfolio Holdings* – March 2011

Stock	Sector	Country
CFS Retail Property Trust	Retail	Australia
Charter Hall Retail REIT	Retail	Australia
Goodman Group	Industrials	Australia
Dexus Property Group	Diversified	Australia
GPT Group	Diversified	Australia
ING Office Fund	Office	Australia
Mirvac Group	Diversified	Australia
Stockland	Diversified	Australia
Westfield Group	Retail	Australia
Westfield Retail Trust	Retail	Australia

*In alphabetical order

Allocations – March 2011



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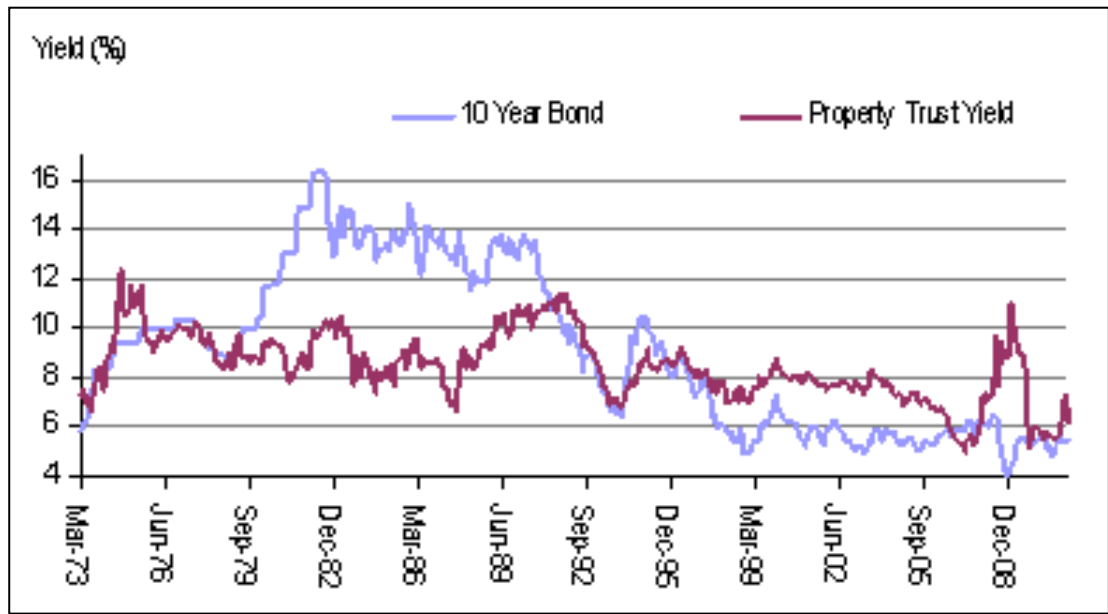
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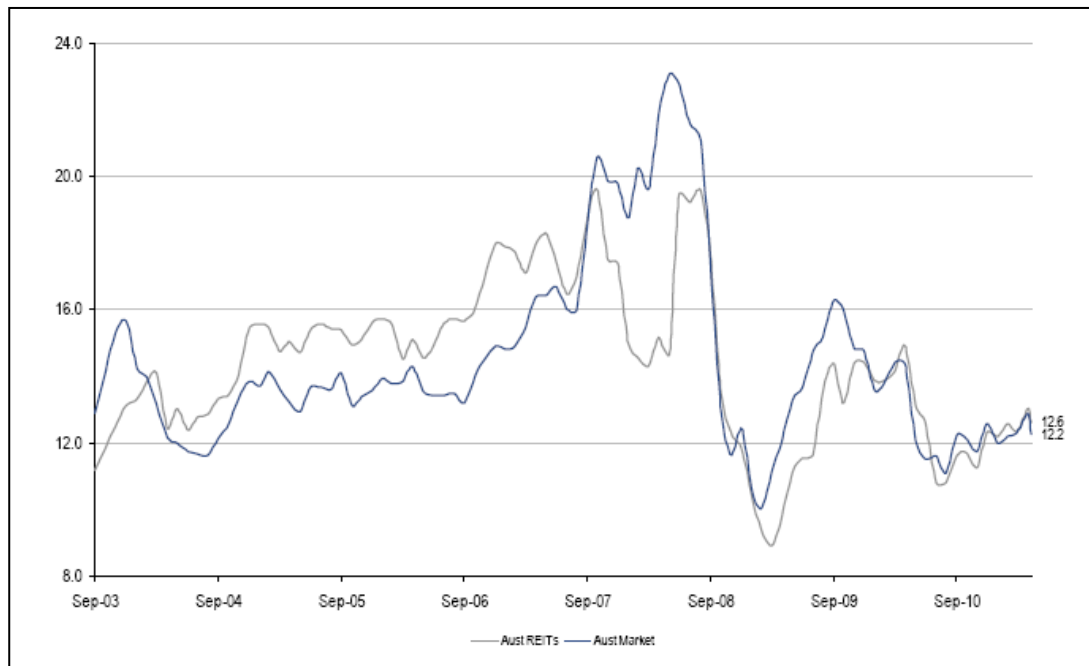
Appendix I

A-REIT Dividend Yield Relative to Bonds



Source: BoAML

A-REITs Relative to Equities



Source: IBES, Citi Investment Analysis & Research

LPT vs. Median Market PE



Source: IBES Data, Credit Suisse estimates

Appendix II: The future of REITs

Presented by Andrew Parsons at the AFR Real Estate Conference 8 March 2011

Today I want to talk about the state of the local A-REITs and the fundamental issues driving investment in global real estate investment trusts.

Before addressing my topic, a disclaimer. I am involved in the business of funds management focused on investing in listed real estate securities. As the saying goes, to a tradesman who only has a hammer – everything looks like a nail. Whilst it is not my intention, the risk is that I am the REIT sector's cheerleader, so please make your own judgements about my comments with this in mind. Nevertheless, I would encourage you to visit www.resolutioncapital.com.au to find my previous presentations.

Let me begin by saying last week I was disheartened to see the Financial Review sponsored Morningstar REIT Manager of the year Award was given to an index fund. Index funds ultimately promise mediocrity and offer little else. The REIT sector's corporate governance standards are not being helped by their growth as they do little to add to the debate within the industry or undertake normal due diligence which is in effect outsourced to active managers. To be fair I will open up the floor to representatives of the index funds now to respond [*our presumption of silence proved to be correct*].

Perhaps index managers would care to come to a real estate industry day and participate in a discussion with more than some bland statistics put together by a broker, or provide their own view on real estate investment best practice and corporate governance rather than outsourcing it to a third party Corporate Governance nanny. If the judging panel believed no active manager deserved it – and this could be the case – then I would suggest it would be better not giving the award at all.

So back to the topic at hand.

Over the past 2 years of presenting at this forum, Resolution Capital has focused on best practice principles within global REITs and what A-REITs could do to restore confidence and competitiveness within the global environment. Today, I'm prepared to report that A-REITs are in the best fundamental shape for perhaps a decade. So I will use this time to reinforce a couple of issues and highlight some of the current market dynamics.

From a macro perspective, the resources boom combined with the anglo financial crisis has resulted in imbalanced capital flows, creating a shortage of capital for Australian commercial real estate, particularly development.

Needless to say, whilst it may be a super cycle, the resources boom will not last forever. Hence, it is vital that investors are offered a range of quality investment alternatives that can at least partially offset the fallout from the inevitable resources bust. Real estate, particularly global REITs, should be part of the solution.

However, the heightened price volatility and equity like returns experienced by global REITs over the past 5 years has left superannuation funds and their asset consultants struggling to interpret the meaning. Two important questions have emerged:

- Are listed REITs a surrogate for direct real estate; and associated with this
- Do investors need to have a separate allocation to listed REITs?

These are the major issue confronting the sector today.

In search of investments that offer the promise of lower volatility, we are witnessing many institutional investors return to unlisted wholesale real estate funds. At the moment core strategies are in fashion, a trend not just in Australia but also overseas as evidenced by CALPERs recent decision to terminate listed REIT and opportunistic real estate mandates in favour of core unlisted strategies. A number of sovereign wealth funds appear to be on the same tack. Apart from the obvious question about timing, this trend has major implications for Australian superannuation for reasons I will elaborate on later in my presentation.

Unfortunately, the behaviour of a small number of A-REITs continues to do REITs in general no favours. Having stabilised the sinking ship in 2008-09 with emergency capital raisings, some recent unnecessary, ill-conceived equity raisings and related party transactions have served to further test the local market's already stretched credibility. I'm not going to name and shame, suffice to say they are an embarrassment and a blight on the reputation of Australia's stewardship standards for publicly listed enterprises. Whilst some of these transactions may have been entirely legitimate, the industry is in no condition to be undertaking transactions with even the slightest sense of impropriety. As the saying goes, not only must it be clean, it must be seen to be clean.

Despite evidence of recidivism on the part of some and uncharacteristic lapses of judgment by others, the optimist in me survives. Overall much of the hard work has been done to restore the investment proposition of many A-REITs as part of equities and global REIT mandates.

Recapping the current state of play, A-REITs have recapitalised balance sheets and recalibrated dividends, the A-REIT dividend pay-out ratio is 80% compared with over 100% 3 years ago. As for balance sheets, the average Loan to Value Ratio is approximately 25%, well within banking covenants of 40-60%. Management also is working on improving the structure and duration of its debt; GPT's 7 year Australian bank debt was a major breakthrough in the local market.

The combination of these factors means that investors can budget with a great deal of confidence on the reliability of the A-REIT income stream and should have limited concern about the prospect that their capital will be permanently impaired through A-REITs breaching debt covenants.

More importantly, the financial crisis has been a catalyst for A-REIT managers to think about the value proposition of their real estate platforms. Today's management has recognised the need for targeted investment strategies such as geographic or sector focus and capital recycling. Furthermore, A-REITs are among the world leaders in environmental sustainability.

Hence, by and large, there has been encouraging progress by A-REITs to provide a sound investment case. With prices barely recovering from their lows, A-REITs currently represent a credible investment proposition. For these reasons, a limited number of A-REITs currently represent a disproportionate exposure in Resolution Capital's global fund.

Having wiped the slate clean, the greatest headwinds for local REITs seems to relate to our elevated A\$ and interest rates, and a matter of trust that management will deliver on promise of this new found mojo. There is a sense of déjà vu with the current conditions. I've been around long enough to know that sentiment changes but over the long term fundamentals triumph. In 1999 I felt like I was wasting my time talking about REITs as most investors only wanted to hear about the latest internet story that they were sure would go up 30% over the next 12 months.

In light of the current sentiment, I think a fundamental question should be considered: why be listed?

If we accept protecting and growing the value of an investment should be the motive of any management, public or private, the primary motive for listing on a stock exchange should be for the benefit of shareholders in terms of liquidity and transparency. Bottom line, management should seek to ensure that the shares trade as close as possible to underlying value of the investments for as long as possible.

Unfortunately history suggests that many managers seem to believe that being listed is a means of raising more capital. Due to the relative ease of tapping the market for equity, management is vulnerable to various temptations: to allay their anxieties, relieve pressure or to increase their own bank accounts and egos. In these circumstances, the long term interests of investors can easily be explained away which manifests itself in raising equity at discounts to both market price and underlying asset values.

Naturally this reduces shareholder wealth and creates a discount mentality for investors: why buy now when I know management do discounted issues. Sellers bargaining power is similarly compromised. The discount becomes ingrained when management regularly undertake such raisings and have no demonstrable track record in adding value to the underlying assets.

It's not unconnected that investment banks love discounted issues. There is a myth being perpetuated in some circles that rights issues don't hurt, even when deeply discounted, because existing shareholders don't get diluted. This supposes that investors have spare cash sitting around. The fact is that most investors will need to sell other assets to fund the commitment, thereby triggering opportunity and transaction costs. Often the stock takes time to soak up the excess supply giving bargain hunters the opportunity to exploit the weakness at the expense of long term investors. Hence, rights issues should never be undertaken lightly.

As well as the risk of poor capital management, being a closed end listed vehicle comes with the risk of sudden changes in investment as well as capital management strategy. We should never forget the decision by a number of previously domestic focused REITs to suddenly lever up to invest offshore, seriously altering the nature of shareholder returns. This had important consequences for those investors that had targeted securities with Australian assets and cash flows to match their own Australian liabilities. Perhaps this was a major motivation for Westfield's recent decision to spin-off a low leverage, moderate fee Australia and New Zealand portfolio on the ASX.

Whilst a sudden change of strategy is an ongoing risk, currently I would rank it low on the current list of things that keep us awake at night.

If that's the case, many A-REITs seem to be underappreciated by the market. This is apparent in reference to three benchmarks.

One, several A-REITs are trading at significant discounts to stated NTA. Two, they trade at discounts to offshore listed peers and three, and most bizarre of all, A-REITs are trading at discounts to Australian unlisted wholesale vehicles. This third point is particularly significant as several of the unlisted wholesale funds have raised significant capital at NTA over the past 12 months despite having very similar property portfolios and capital structures to their listed counterparts which are trading at discounts.

When A-REIT price deviates from value for a prolonged period it is time for boards to consider if current management is in fact capable of generating a satisfactory return on the assets and shareholders equity?

Put simply, not all REITs are born equal. A discount should be factored into the price of some vehicles because appraised valuations are wrong or management are serial value destroyers. Boards either don't understand this or are unable to exert control over management. That being the case, we hope more investors will join us in voting against the overly generous remuneration levels of some executives at next year's AGMs.

On the other hand, where boards and investors have cause for confidence and faith in management, they must wait for normal market forces to take effect and refrain from doing silly deals.

Nevertheless, there are some initiatives currently being considered to more quickly close the gap to fair value.

For example, some investors are calling for A-REITs to lift dividends through increasing the pay-out ratio. I do not believe this is appropriate. Dividends and dividend yields are an outcome of value, dividends don't determine value. The dividend pay-out ratio today of 80% allows for necessary reinvestment in keeping the properties attractive to tenants. Indeed the current 60% dividend pay-out ratio of U.S. REITs has not constrained performance or rating of the sector.

Meanwhile some A-REIT Boards are considering whether it might be in the best interests to downsize REITs by selling assets. This provides evidence of the underlying value of the portfolio and might facilitate using the sales proceeds to pay special dividends and or buy back shares without resorting to gearing up the fund. If carried out in this fashion we believe it is sensible but we are concerned that the arbitrage may not be that great to make it meaningful. The time to consider share buy-backs was 2 years ago when of course few managers had the financial capacity to do so.

If A-REITs continue to trade at discounts, it may then be worth considering the old maxim, if you can't beat em join em. In a nut shell, some A-REITs should delist and become unlisted wholesale funds and/or retail syndicates. I do not believe it will come to this for the majority of the sector but it does highlight the value buffer that underpins A-REITs provided management remain disciplined. Perhaps then people might stop talking about volatility and focus on the more important issue of liquidity.

In relation to liquidity and unlisted real estate, I discussed this issue last year in great detail. I'm not going to repeat what I said, it's on our website. However, I firmly believe many in the superannuation industry dodged a bullet during the financial crisis. Under the fund choice framework, in effect today's superannuation funds are promoted as open ended funds from which investors can change their mix or withdraw at anytime, with the discreet proviso, subject to liquidity. Unlisted real estate often experiences significant volatility of liquidity. Thankfully, in an operational sense, commercial real estate generally performed quite strongly in the latest crisis due to limited new building supply flooding the market, which no doubt took some pressure off investors decisions to reduce exposure to unlisted property. The recent challenges facing members of MTAA and Bookmakers Superannuation are perhaps a taste of things to come.

We continue to believe that the superannuation industry should at least have a balanced approach to its real estate exposure by investing in select, and I stress select, global listed REITs. The extreme price volatility of the recent financial crisis was a relatively short term aberration through which all markets remained open. Volatility in listed markets often represented liquidity and this short term volatility did not change the long term fundamentals of the underlying investments of global REITs. Compared with investment in offshore unlisted real estate, global REITs are transparent in many ways - including fees and taxes as well as pricing and liquidity. They provide exposure to dynamic economies and deep capital markets. For example U.S. REITs are currently securing 10 year finance at an all-in cost of circa 4%, with no LTV covenants, from a range of debt providers.

We continue to argue that Australian investors remain cautious about global REITs because of a fear of the unknown. They are unfamiliar with skilled listed operators such as Simon, Link, Avalon Bay, Unibail, Federal Realty, Boston Properties, Derwent London and Shaftesbury. The strategy and performance of these vehicles is exemplary.

These vehicles provide exposure to portfolios containing some of the world's best real estate experiencing a deep and expanding pool of tenant demand. It would be extremely difficult to replicate these portfolios in an efficient manner through unlisted products.

Indicative of the quality of the platforms, listed global REITs dominate the ownership of the world's fortress malls in the U.S., U.K., western Europe, Brazil, Singapore, Australia and New Zealand. REITs and listed real estate companies own large parts of key global cities including Marunouchi in Tokyo, west end and the city of London, mid-town Manhattan, Hong Kong and Singapore. REITs are now among the major providers of space to logistics companies that are being called upon to service the expanding e-tailing sector. REITs own apartments in major cities which continue to benefit from urbanisation.

It may be a surprise to some of you to know that U.S. apartment REITs have been among the strongest performing property stocks in the world over the past couple of years. The reason is that the majority of U.S. apartment REITs own property in cities like New York, Washington DC, Boston and San Francisco, cities which were not subject to overbuilding that brought about the housing induced finance crisis. The lack of building combined with declining home ownership rates and migration of people to these vibrant 24 hour cities has created an accommodation shortage that has led to relatively strong rental growth. Combined with ongoing access to relatively cheap debt provided by Freddie and Fannie, the multi-family REIT share prices have grown strongly and are now within sight of record highs.

As evidence of the strength of demand for REITs in offshore markets, we expect to see the biggest REIT IPO in history during 2011. Archstone, an apartment stock taken private in 2006 by interests associated with Lehman Bros, is expected to raise more than \$5bn to refloat the platform on the New York Stock Exchange. Blackstone also is working toward major U.S. REIT IPOs of office, industrial and, following the Centro transaction, retail platforms.

To be fair, the greatest challenge to offshore REIT investment at this point is pricing. Unlike A-REITs, many U.S. REITs currently are trading at premium valuations thanks to low interest rates and historically low levels of new supply. U.S. construction activity is at 40 year lows. Low construction activity, a feature of many real estate markets, also is underpinning the outlook for Hong Kong real estate stocks. Even U.K. REIT prices are doing well, not least of which is due to spending on infrastructure projects that go beyond the 2012 London Olympics.

Finally, and quickly, over the next decade we expect to see REITs will be responsible for proportionately more development activity given increased constraints on bank lending and REITs will continue to increase their control of real estate markets globally.

In conclusion, it is both a challenging and exciting time for REITs.

A-REITs are striving for a sustainable improvement in performance which means they are well placed to compete with their global peers. Nevertheless, there is frustration that these improvements are not being appreciated by the market. This is not the time for management to panic into ill-timed capital raisings or deviate from their long term investment plan. Ultimately fundamentals will count.

It is important that the Australian superannuation industry is provided with long term investment strategies suitable to the current framework which promotes liquidity. Local investors must put aside their perceptions of volatility to recognise the liquidity and quality of select Global REITs is a sensible means for Australians superannuation funds to effectively diversify portfolios to achieve superior long term investment outcomes.

Thank you and I'd now be pleased to take questions.

Andrew Parsons

Resolution Capital

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