



resolution**CAPITAL**
real estate securities solutions

RESOLUTION CAPITAL GLOBAL PROPERTY SECURITIES FUND

DECEMBER 2010
QUARTERLY INVESTMENT REPORT



GLOBAL REAL ESTATE SECURITIES

Fund Investment Performance

The Resolution Capital Global Property Securities Fund underperformed the UBS Global Investors Index (AUD Hedged Net TR) by 82 basis points for the quarter ending 31 December 2010.

Period Ending 31 December 2010*

	Quarter %	1 Year %	2 Year %	Since Inception [#] %
Portfolio	5.96	20.04	28.64	7.13
Benchmark (UBS Global Investors Index)	6.78	22.54	24.95	-1.70
Difference	-0.82	-2.50	3.69	8.83

*Returns are expressed after deducting investment management costs.

[#] 30 September 2008

Resolution Capital Global Property Securities Fund Unit Price - Class A

	Entry	Exit
31 December 2010	\$1.0151	\$1.0091
30 September 2010	\$0.9676	\$0.9618

Market Performance

Market Overview

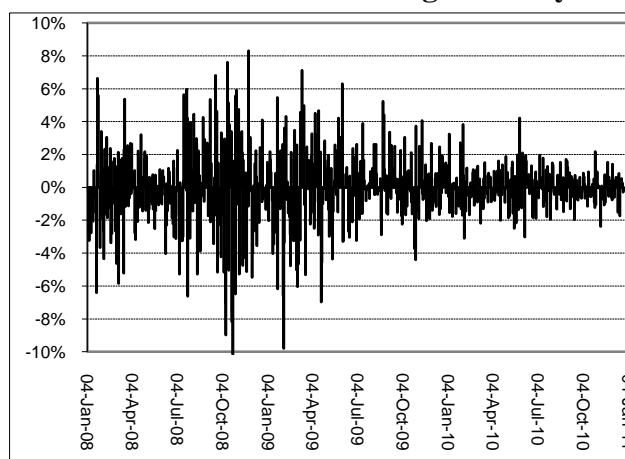
	31 Dec 2010	30 Sep 2010	Quarterly Accumulation Return
UBS Global Investors Index AUD (Hedged)	1,192	1,116	6.8%
UBS Global Investors Index AUD (Unhedged)	919	910	1.0%
S&P/ASX 300 (GICS) Australia Property	19,175	19,402	-1.2%
S&P/ASX 300 Index	34,560	33,023	4.7%
10 Year Bonds	5.51%	4.97%	
90 Day Bills	4.96%	4.89%	
AUD/USD	\$1.02	\$0.97	5.2%

Commentary

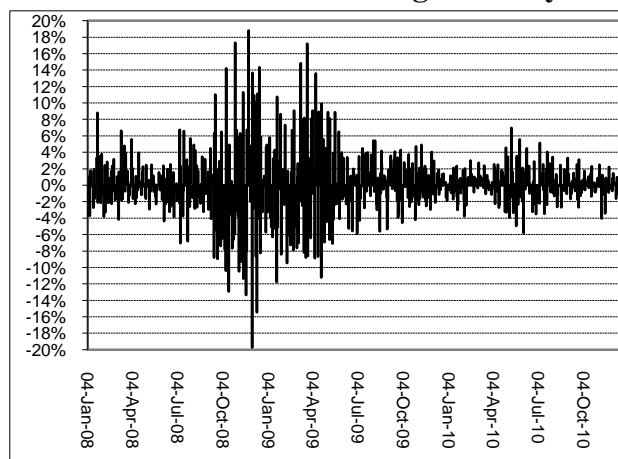
The UBS Global Investors Accumulation Index (Hedged) produced a total return of 6.8% for the quarter ended 31 December 2010. For the calendar year the global REIT benchmark produced a total return of 22.54%. In comparison, AREITs produced a total return of -1.2% and -0.7% for the respective periods.

As the charts below highlights, the appreciable reduction in REIT price volatility continued during the December quarter. Among other factors, this partly reflects stabilised debt markets and consequent improving liquidity in real estate markets, thereby alleviating pressure on REITs as a source of liquidity within real estate exposures.

AREIT % Price Change Per Day



US REIT % Price Change Per Day



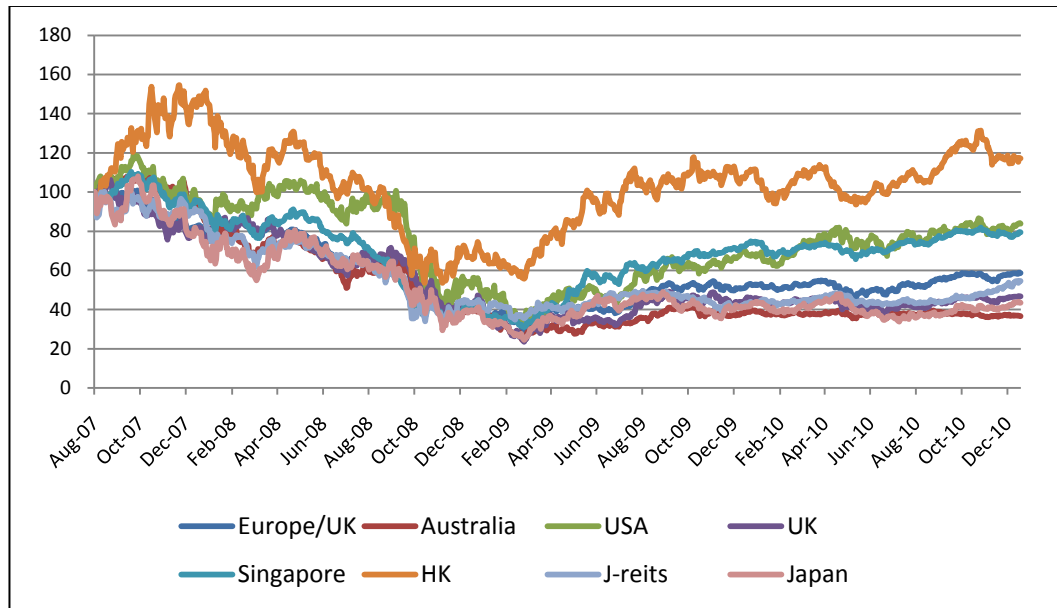
Source: Bloomberg

Real estate markets, including REITs, are gradually adjusting to the stabilising capital market and economic conditions although, based on AREIT's dismal 2010 performance, some better than others. In this more assured environment, REIT management focus has shifted from the challenge of debt refinance, including survival, to growth strategies.

At most levels, activity within the real estate universe is increasing. This is reflected in: REIT equity issuance including IPOs, property transactions, leasing activity, mergers and acquisitions as well as tentative signs of new property development in select areas.

Whilst REIT prices remain below bloated peak levels, generally they have recovered strongly from the trough which most experienced in early 2009.

Indices Graph – REIT Market Recovery



Source: Bloomberg

Of course it is important to recognise that overall economic and investment conditions, particularly in the west, are underpinned by significant artificial stimuli. Budget deficits and loose monetary settings including “quantitative easing” and the “lower for longer” interest rate policy of the US and UK are arguably having the desired effect of bolstering asset prices including real estate, particularly in the northern hemisphere developed markets.

Various stimulus programs continue to roll-out in some markets. Consistent with the short term boost from central planning stimulus, J-REITs were the strongest performing REIT market for the December quarter which followed the Bank of Japan’s decision to buy ¥5 trillion (circa A\$60bn) of financial assets including ¥50 billion (A\$600m) of J-REITs in order to stabilise land prices and boost corporate confidence. The J-REIT buying would represent approximately 1.4% of the current equity market capitalisation of the sector.

By way of contrast, residential real estate markets in South East Asia and those strongly tied to China’s burgeoning economy were subject to a number of central planning cooling measures during the quarter. The Reserve Bank of Australia continued to increase official interest rates whilst China increased interest rates on 25 December to target stubborn inflation. Furthermore, the Governments of China, Hong Kong and Singapore implemented a number of measures including taxes and policies targeted at curbing speculative residential investment activity (significantly reducing the risk of a repeat of the US residential crisis).

Singapore REITs produced the weakest return for the quarter of -2.6%. The market was impacted by the Government’s cooling measures coupled with a raft of equity capital raisings with the promise of more to come in 2011.

Australia’s REITs continue to languish due to poor capital management combined with local economic factors discussed later in the report.

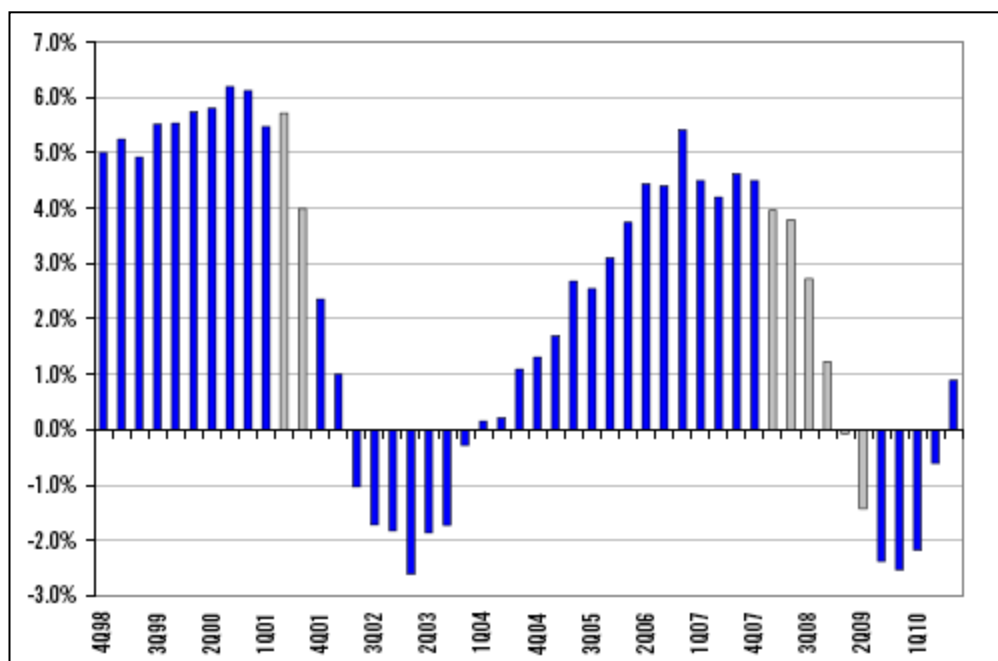
Real Estate Operating Conditions

Most commercial real estate markets experienced improving operating conditions during the period with upward pressure on market rent levels, particularly in the major cities.

With limited supply of new space, commercial real estate operating conditions are beginning to trend positive with signs of a sustained improvement in tenant demand and generally low levels of vacancy.

Significantly, there are signs that the US commercial real estate market is turning the corner. US REIT property portfolio occupancy continues to rebound, Same Store Net Operating Income growth (broadly rental income) turned positive during the September quarter of 2010 versus the previous corresponding period, the first positive number since 2008.

US REIT Same-Store NOI Growth (Rental Income) Turned Positive in 3Q10



Source: Company Reports & Citi Investment Research & Analysis, as of 9/30/2010

Market rents are recovering with office rents generally increasing most. London office rents are believed to have increased by 25% in 2010 whilst Hong Kong rents increased 30%. Meanwhile, during the December quarter, Manhattan landlord SL Green reportedly increased asking rents by 15%.

Nevertheless, REITs do not necessarily benefit immediately from the pick-up in spot market rents. Commercial rental income (particularly in office, industrial and retail), is typically characterised by lease contracts of between 2 and 20 years (most are 5 -10 years) which fixes a minimum income for the duration of the lease. During the lease, rents may be periodically reviewed by predetermined amounts (fixed or inflation linked) whilst some include market reviews which typically include ratchet clauses (i.e. upward only reviews) which prevent rental income falling during the lease period. Hence, property leases signed or reviewed in the market peak period between 2005-07 are, in most cases, producing income streams above current GFC impacted market rental rates. Hence, short term “organic” income upside is generally limited particularly as few REIT portfolios have significant occupancy upside.

As a consequence, real estate with shorter term lease structures such as US hotels and apartments, carried investor favour in the December quarter as they were best placed to capture the improved economic conditions.

Real Estate Transactional Activity

It is worth noting that vacancy levels, notably in prime office markets, are generally lower than has previously been the case after periods of economic and or financial turmoil. Much of this has to do with the relatively low levels of speculative commercial property development during the asset price bubble between 2004 & 2007. As a consequence, unlike the early 90's, banks are not lumbered with non-performing commercial real estate loans which in turn generally results in generous tenant lease deals and fire sales at depressed prices. Hence, combined with the low interest rate environment, distressed quality property at prices well below replacement cost is hard to secure. The bargain buying window created by the GFC was not open very long.

Buyers now appear increasingly willing and able to cross the buy/sell spread for quality property. This comes from increased confidence that rental income streams are robust, whilst lower borrowing costs and improved capital availability has resulted in improving property transactional activity.

During the quarter demand for high quality real estate was evident in a number of major transactions. The most significant buyers include the REITs together with Sovereign Wealth Funds including those from China, Norway, Singapore, Korea and Canada which require minimal debt to fund the acquisitions. As an example, transactions in Central London amounted to £9.9bn in 2010 versus £6.6bn in 2009. Demonstrating the bounce back in values from trough levels, the sale of Bishops Square in London in December 2010 was at an equivalent price 25% higher than a partial interest sold in June 2009 and only 7% below the peak valuation in 2007. In another notable transaction, a partial interest in Doncaster Shopping Centre in Melbourne re-traded at approximately 5% lower than the price paid close to the peak in August 2007. Assuming no hedging of the initial Australian dollar investment, the vendor (LaSalle's Asia Property Fund) likely realised a profit on its investment.

Westfield sold a 50% interest for A\$1.425bn in its London Stratford City development to two pensions funds. This transaction will result in a A\$490m valuation uplift (partly upon completion) and highlights a remarkable development profit from a project commenced on the eve of the financial crisis and which will not be completed until the end of 2011.

We have listed several of the quarter's major global real estate transactions in Appendix 1.

Nevertheless, improved real estate investment and operating conditions are not being experienced by all. Compared with pre-GFC activity, credit for real estate investment is more discerning, imposing higher borrowing margins and more equity for lower quality real estate. As a consequence of more discerning buyers and their generally more disciplined capital providers, we believe markets are undergoing a reversal of the yield compression evident in much of the decade up to 2007. For want of a better term, we are seeing "yield decompression" – the gap between low and high grade real estate is widening. This trend is being exacerbated by the bifurcation in tenant demand as tenants gravitate to better grade, better located property.

Development Joint Ventures

Signalling broader investor appetite for risk through development exposure, two London office construction projects were re-started during the quarter after their respective owners found 50% joint venture partners.

Land Securities had announced earlier in the year that it would proceed with the development of 20 Fenchurch Street (aka “The Walkie Talkie”) and during the quarter sold a 50% interest in the project to Canary Wharf Group for £45.1 million. The 690,000 sqft speculative office development is expected to be completed in mid 2014, with a total development cost of £500 million (100%).

Meanwhile British Land also dusted off its plans to develop 122 Leadenhall Street (aka “The Cheese grater”) when it sold a half interest in the project to the Ontario Municipal Employees Retirement System (OMERS) for £45 million. The 610,000 sqft speculative office development is expected to be completed in mid 2014 with a total development cost of £340 million (excluding interest).

Both these projects had been mothballed during the financial crisis after initially having demolished existing buildings and completing preliminary basement works. While no pre-leasing deals have been announced for either, British Land reported strong interest from a broad range of occupiers.

In Australia, Charter Hall Office REIT (CQO) secured a 12,000 square metre pre-commitment to its 50% owned development project at 171 Collins Street Melbourne. BHP Billiton will take a 10 year lease on the upper floors of the building from completion in mid 2013. Notably, BHP will vacate its current space in one of the buildings recently acquired by Commonwealth Property Office Fund (CPA) which rubs salt into the wound of this poorly executed acquisition by CPA referred to later in our report.

Corporate Activity

The dearth of large scale direct buying opportunities is encouraging merger and acquisition activity within the REIT sector.

Having failed to capture US rival General Growth Properties earlier in the year, Simon Property Group (SPG) turned its attention to London listed, UK mall owner, Capital Shopping Centre Group (CSC). SPG had acquired a 5% position in CSC in 2009 and in November 2010 Simon made an informal indicative £2.9 billion take-over bid. This bid was triggered by CSC’s proposal to issue up to 24.7% of its stock to Peel Group as consideration for the purchase of Trafford Centre, located in Manchester, for £1.6bn. Simon's proposed offer represented a significant premium to NAV, but CSC management refused to open its books for due diligence and we believe sensibly, on 11 January 2011 Simon decided not to proceed with a formal bid.

Consistent with SPG’s bid for CSC, it also is worth noting the increased level of cross border investment interest from the US REITs with SL Green and Host Hotels also making investments outside the US in recent months.

In continental Europe, Nieuwe Steen Investments expressed interest in Vastned Office. The merged entity would own €2.4bn of Dutch and Belgian assets.

Meanwhile in Australia, Goodman Group (GMG) confirmed its bid for ING Industrial but at a price below its initial indication. With GMG controlling almost 20% of the stock, and with the likely support from ING which is being paid an additional AUD\$22.5 million to help facilitate a smooth

transition, we believe minority interests stand little chance of achieving fair value. Not only is it at a discount to the stated NTA of \$0.56, the bid price of \$0.53 per unit fails to recognise the significant stamp duty savings for Goodman, the quality of the portfolio (which would be challenging to replicate within a short to medium period of time) and the fact that the asset values are arguably at a cyclical low (the average cap rate used in the NTA is 8.43%).

The continued clean-up of smaller AREITs continued with take-over bids launched for ING Healthcare and Challenger Wine Trust. Centro also announced that it has called for expressions of interest in its businesses and assets.

Most AREIT takeovers have occurred at discounts to NTA highlighting, among other factors, investors do not believe the individual property valuations and lack of confidence in incumbent management: Better to take a slight discount now than wait for management to destroy more value in the future.

AREIT M&A at a Discount

Target	Buyer	Date*	Takeover Price	NTA	Discount / Premium to NTA
MRZ	MGR	Nov-09	0.594	0.850	-30.1%
CKT	Challenger Life Company Ltd	Feb-10	1.150	1.800	-36.1%
WOT	MGR	Apr-10	0.860	0.820	4.9%
IHF	NorthWest Value Partners	2011	1.000	0.980	2.0%
IIF	GMG	2011	0.53	0.56	-5.3%
CWT	CK Life Science International	2011	0.240	0.410	-41.5%

Source: Company data

*Deals dated 2011 are yet to be completed

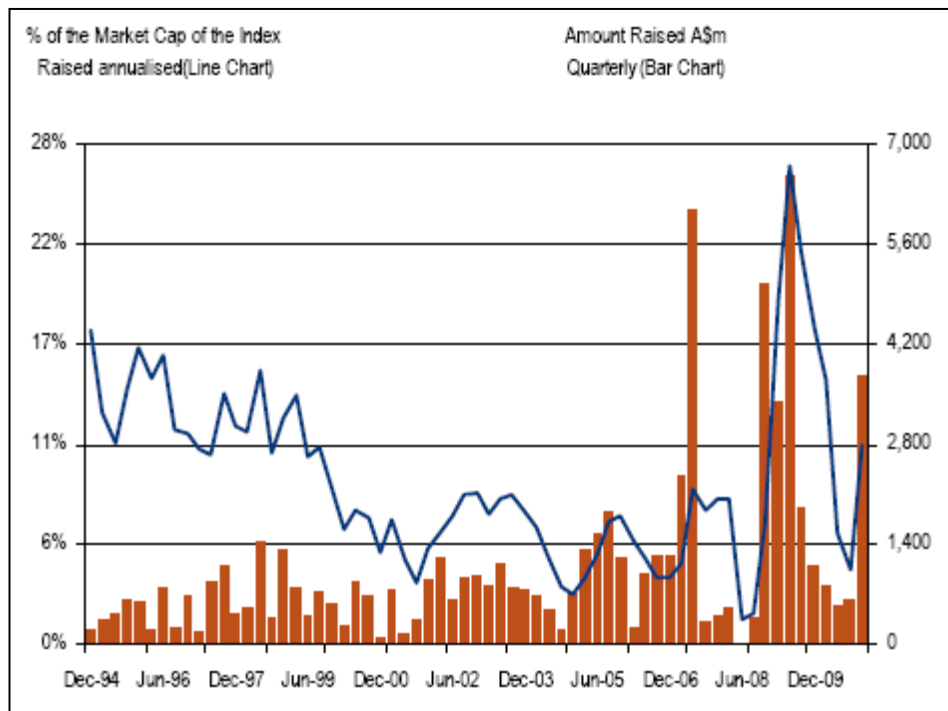
Equity Issuance

Increasing equity issuance by REITs and real estate companies is beginning to weigh on some markets.

Singapore's poor quarter return was in response to, among other factors, the launch of several IPOs (Global Logistic Properties and Mapletree Industrial) and secondary equity capital raisings (Suntec REIT) in recent months and plans for several more in 2011. New IPOs flagged for the new calendar year include Mapletree Commercial as well as a China retail portfolio managed by the former CapitaMall chief executive.

Australia also experienced further secondary raisings. During the quarter the AREITs raised over AUD\$2.3 billion equity which was simply too big an ask for a sector out of favour and not in need of equity. As we explain below the nature of the raisings helped contribute to the ongoing lacklustre performance of the AREIT market.

Australian REIT Capital Raisings



Source: Merrill Lynch

In Hong Kong Hang Lung Properties (101) raised HK\$ 11bn, after the stock hit an all time high the day before. Even though the company has a net cash position it has a huge development pipeline of Chinese malls to fund, with appetite for more.

The US REIT market is experiencing relatively high levels of equity issuance but was able to digest the transactions more comfortably. While smaller scale IPOs continue, secondary offerings by existing vehicles are more significant.

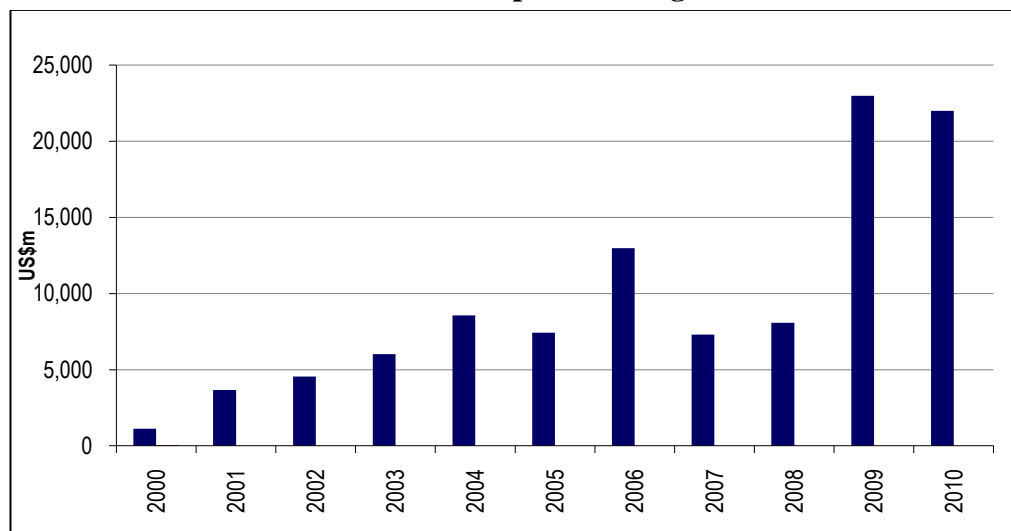
HCP undertook a major US\$1.5 billion public capital raising to fund the purchase of HCR Manor Care Inc for a total purchase price of US\$6.1 billion.

ProLogis continued efforts to restore its balance sheet and portfolio, as well as selling assets, it raised US\$1 billion of equity during the quarter.

It also is worth noting that General Growth Properties emerged from bankruptcy during the quarter following a successful US\$6.9 bn equity raising which effectively recapitalises the stock. GGP was the largest real estate failure on record when it filed for bankruptcy protection in April 2009, symbolically marking the bottom of the real estate cycle.

US REIT IPOs continue to be of a relatively modest scale. However, like several Asian markets, the US also may see significant REIT IPO's in 2011 with speculation that the apartment giant Archstone (previously known as Archstone Smith) could return to the NYSE after being taken private in early 2007 by interests associated with Lehman Bros.

US REIT Capital Raisings



Source: SNL Financial

AREITs – when will they learn?

Not even significant corporate activity (e.g. IIF) could spark a better performance from the AREITs. The local market continues to languish from increasing interest rates, investor preference for mining sector exposures within the local bourse and, most disappointingly, more questionable capital management and corporate governance issues.

Indicative of the corporate governance issues, we believe management remuneration across the Australian sector is excessive, particularly in the context of the poor performance of the listed REIT market over the past 5 years. The Annual General Meeting season gave us the opportunity to demonstrate our displeasure. Within our ASX focussed Core Plus AREIT mandate, we voted against 53% of AREIT resolutions related to Remuneration Reports in stocks which we have invested. The lack of opposition from the majority of other unit holders was puzzling.

REIT AGM – Remuneration Report Resolution

	CHC	MGR	WDC*	GPT*	SGP	DXS	GMG
% voted Against	36.1%	24.8%	16.2%	14.2%	8.3%	2.9%	0.6%

*AGM was held in May 2010

Commonwealth Property Office Fund's (CPA) acquisition of the Grollo office portfolio in November exemplified the capital management problems inherent in the AREIT market. To fund the acquisition, CPA raised \$377 million of equity at 86c per security versus an NTA of \$1.14 per unit and a preceding trading price range of 90-97c per unit.

Hence, management was prepared to issue equity at a significant discount to both the stated NTA and the recent market trading price in return adding assets which are, generally speaking, of moderate value and quality. Nor did the transaction enhance short term income returns, which is but one, albeit sometimes misleading, indication of value creation. A better strategy for CPA would have been to finance the acquisition with asset sales or simply not do the transaction at all. The portfolio has no exposure to CPA.

Moreover, it is worth noting that earlier in 2010 the vendor, Grollo, had explored an IPO of a vehicle which contained at least some of the assets but failed to garner investor support for a float at

NTA. Ultimately the same assets were sold at NTA to CPA which diluted its own equity base to fund the transaction.

CPA was one of the worst performing stocks for the quarter (-6.6% total return), representing a significant fall from grace by one of the few AREITs that had survived the GFC with a reasonable reputation derived from its low leverage and pure domestic asset focus. The lack of discipline and respect for unit holder value was a slap across the face of investors and market commentators who have been asking why many AREITs have been trading at a substantial discount to written down NTAs.

Investors are now accustomed to management issuing equity too often and at too great a discount to fair value (whether that be NTA or market price) which creates a lasting discount mentality.

Therein lies the great flaws in the motivation of some AREIT management who appear to view the primary reason for being listed as a means of extracting exorbitant fees and salaries as well as raising capital to buy more assets without clearly adding value.

The major reason for being listed should be for the benefit of investors, theoretically the owners and beneficiaries of the entity, principally to provide them with liquidity when needed. It is management's role to act in capital providers best interests, outline a strategy and ensure that the stock trades as close to fair value as possible for as long as possible by being disciplined, whilst keeping the market fully informed. Capital should be treated as a scarce commodity, secondary capital raisings undertaken judiciously when it can add value. Clearly, based on the events of the past 5 years, many AREIT managers fail to grasp this basic concept.

We were also puzzled by Westfield Group's decision to spin-off a half share of its Australia and New Zealand portfolio into a separately managed vehicle called Westfield Retail Trust (WRT). Like CPA, WRT also issued equity at a discount to NTA, albeit a meaningful capital raising was required to reduce stamp duty on the transaction.

We have no qualms with WDC disposing of interests in its properties but would prefer that it be done with external capital rather than an in-specie and entitlement issue of the new vehicle – the resulting conflict is undesirable. We were heartened by the Lowy family's decision to participate, oddly something they did not do in the last equity raising by WDC.

Perhaps the spin-off was a lapse in WDC management's otherwise exemplary judgement although it is too early to tell. We have appreciated and benefited from the superior capital and asset management skills demonstrated by WDC over the longer term (once again demonstrated by the profit achieved on the Stratford disposal) and so were prepared to support the transaction as it did not appear to be materially value destroying. However, the market's response to the deal could be described as underwhelming to say the least, the anticipated extent of demand for quality Australian assets failing to materialise in the short term at least, nor the immediate earnings or balance sheet benefits to WDC obvious.

Meanwhile Goodman Group unit holders voted in favour of the transaction involving the purchase of Greg Goodman's (the CEO of GMG) private real estate holding at Moorabbin Airport in Melbourne. Overlooking the huge profit that Mr Goodman achieves on the transaction, in principal we do not believe this type of related party transaction should be encouraged.

This was followed by news that together with other senior executives, the CEO of Valad, Peter Hurley was stepping aside in order to be part of a management buy-out of Valad's European business. Little wonder AREITs in general are earning a dubious reputation.

The other notable feature of the quarter was the number of poorly performing AREITs that completed share consolidations during the quarter. Whilst management can point to liquidity as a primary reason, we believe it is as much to do with masking the sins of the past.

Internet Retail – What is the threat to bricks and mortar shopping centres?

During the quarter, the Australian media was filled with discussion on the impact of internet retail on traditional retailers and bricks and mortar shopping centres. This was heightened by retailer lobby groups calls to remove the GST exemption on offshore internet transactions of less than \$1,000. This sudden awakening of domestic retailers towards online competition was no doubt stimulated by disappointing retail sales growth in the second half of calendar year 2010 and the rapid appreciation of the Australian Dollar.

With all the media and industry hype around online retailing, it should be recognised that its estimated market share is still quite limited; around 5 to 6% of non-food retail sales in Australia (source: Citigroup), compared with around 9% in the United States. Whilst it is reasonable to say that the longer term impact remains open to debate, it is likely to be profound in the way that shopping centres are developed and tenanted.

Having abandoned its previous short lived attempt during the dot-com bubble a decade ago, Westfield's new effort to create its own internet shopping portal during the quarter (www.westfield.com.au) is at the very least an acknowledgement of the threat. Although we don't believe that the 1998 Time magazine cover below is correct, we do agree with former American baseball player Yogi Berra: "The future ain't what it used to be".

The internet makes shopping more transparent and allows consumers to more easily search for value. A search online quickly confirms that many goods are much cheaper abroad and the overall offer better. This begs the question: why are goods in Australia so much more expensive? We think the differences can be explained by a lack of purchasing power with suppliers, higher labour costs, not always passing through the benefits of a rising Australian dollar and (until recently) limited offshore competition. Some might argue that rents in Australia are relatively high, but we note that sales productivity per square metre is also very high compared with offshore markets which might be explained by high urbanisation levels and low retail space per capita.



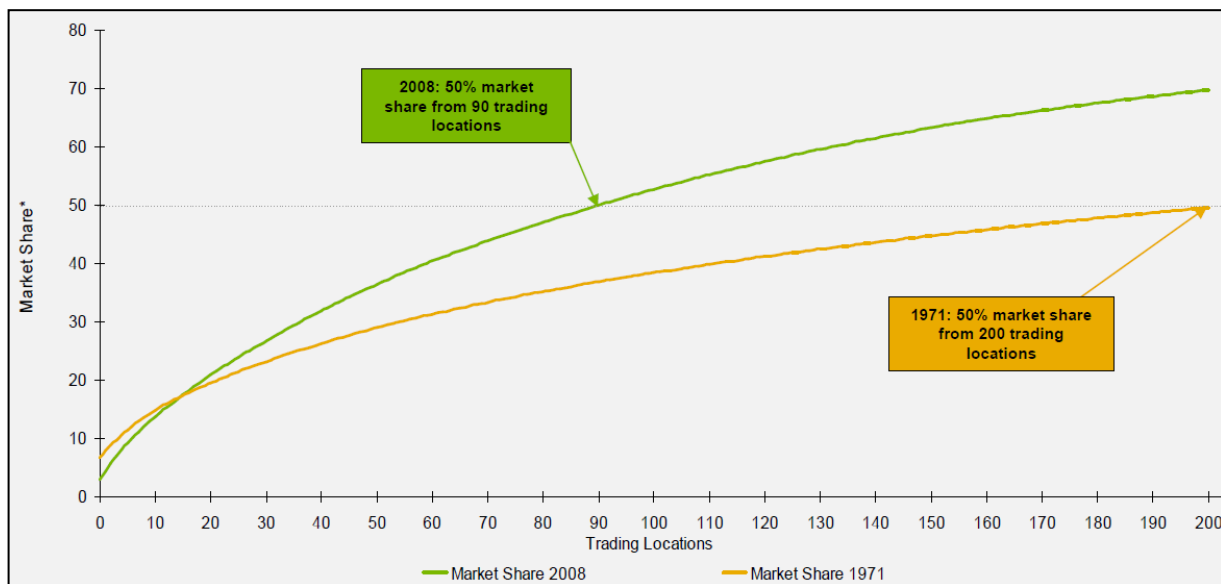
Source: cover Time magazine 20 July 1998

Whilst pure online retailers like Amazon and ASOS (UK apparel retailer) are now significant, seven of the top 10 online retailers in the US actually have a bricks and mortar presence. Apple is a prime example of a company which successfully combines online sales with a (quite impressive) bricks and mortar presence. US department store Nordstrom's online sales are 9% of its total while Best Buy, a US consumer electronics retailer, generates 7% of sales from online channels. Australian bricks and mortar retailers will beef up their online presence (David Jones recently relaunched their mothballed site), but they will face increased competition from retailers abroad, even though these retailers may not have a physical presence in Australia.

We continue to believe in the power of quality shopping centres to attract shoppers and tenants. Shopping centres provide an intimate environment for retailers to engage directly with their customers and demonstrate the benefits of their products and suitability to their individual needs. Entertainment, food and services together with timeliness and return policies are powerful drivers for well located properties in high population density catchment areas.

Continued success of shopping centres has always depended upon the ability of landlords and their retailing occupants to adapt to the changing needs of consumers. Those centres that do not will become obsolete, further strengthening the more powerful shopping centres. This migration to better centres has been the case for some time as the graph below clearly shows.

Market Share – Top UK Retail Locations



Source: CBRE NSLSP / Capital Shopping Centres

Some people simply like to go shopping – to explore and socialise.

One should not overlook the possibility that the internet will increase the consumers' ability to spend and therefore increase total retail spending. As an example, internet gambling has not destroyed casinos, merely expanded the gaming pie. That said, we continue to carefully monitor the situation, which we believe will have a profound impact on retailing and shopping centre tenancy mix.

Our Travels

London Calling

We visited London in early December coinciding with unusually cold weather but critically ahead of Australia's Ashes defeat. Our visit involved attending a global REIT conference, visiting local management teams as well as physical property inspections including time on the road with management of Derwent London and Big Yellow in which we have substantial exposure.

Having survived the financial crisis, London is alive and well, the mood is buoyant, in fact more optimistic than Sydney. The mood of local REIT management was definitely upbeat, surprised by the speed of the turnaround as tenants are considering long term plans rather than short term survival. London is improving on various fronts, as well as the fact that you now can even get a decent coffee and the coalition government is working, getting more done than expected as evidenced by the student riots. Do not misconstrue these comments, the London economy is far from booming but it is certainly expanding which is major improvement compared with the bleak environment just 18 months ago.

The city is enjoying investment in infrastructure associated with the Olympics (now largely complete under David Higgins oversight, with whom we met), and other longer term transport initiatives such as Crossrail (crossing London from east west) and Thameslink (north south). Crossrail in particular will be a major positive for international travellers, continuing the Heathrow Express directly into the city (rather than terminating at Paddington) through Canary Wharf and Stratford in the east.

Pre-empting better economic times, investment in London property is rolling in from offshore, particularly from Russia and the Middle-East. As well as office buildings, middle-east buyers are reportedly behind a couple of recent record prices for apartments with off the plan purchases at £120 million (A\$200m) and £140 million (\$230m, or over \$110,000 sq m). Apart from Simon's bid for CSC, US REITs are now active with SL Green buying a mortgage over a London office building. The Chinese are expected next.

Foreigners are attracted by London's safety, rule of law and tax regime together with the urbanisation trend toward the bigger cities. London, as opposed to the rest of the UK, is the focus of investment activity.

Despite the improved outlook, rent growth is still hard to achieve for most REITs. Rental income of many UK REITs still reflect the heady days of 2005-2007 with income ratcheted at peak levels. To put it in perspective, spot office rents have fallen by 30-40% from the peak but are now showing signs of increasing albeit partly due to lower incentives.

That said, London office vacancy is relatively low (around 7%) and office development is underway, principally designed to take advantage of the amount of obsolete stock experiencing lease expiries over the next 5 years. The commencement of large office development, mostly spec built, is itself remarkable given some speculated about the end of London as a finance hub less than 2 years ago. It seems to be the SMEs that are doing best.

As an example, Derwent London (in which the fund has a significant exposure) has an impressive track record of adding value to older office buildings, principally in London's west end, whilst not raising equity at dilutive prices.

UK retail sales are growing with many retailers reporting a strong start to Christmas trade. Shopping centres are experiencing renewed tenant demand (UK malls were particularly hard hit by retailer

defaults as a consequence of the Western Financial Crisis). Ugg boots are the must-have fashion item.

Once again we visited Westfield London which is proving to be a home-run, proving wrong claims that people prefer high street shopping on Oxford and Regent Streets (which still seem to be doing just fine). We visited on a Sunday and it was as busy as any centre we have visited, the food court booming with lines 10 and 20 long after 3pm at various outlets. Within 2 years of opening, in terms of tenant's retail sales, it is the most successful shopping centre in the UK and sales are growing at 30%, albeit this is helped by the recent opening of the cinema complex.

Top UK Malls

	Name	Location	Owner(s)
1	Westfield London	London	Westfield / JV
2	Bluewater	Greenhithe	Lend Lease / JV
3	Meadowhall	Sheffield	British Land / JV
4	The Trafford Centre	Manchester	Peel Holdings
5	Lakeside	Thurrock	Capital Shopping Centres
6	The Mall at Cribbs Causeway	Bristol	Capital Shopping Centres / JV
7	Metrocentre	Gateshead	Capital Shopping Centres / JV
8	Cabot Circus	Bristol	Hammerson / Land Securities
9	Brent Cross	London	Hammerson / JV
10	Liverpool One	Liverpool	Grosvenor / JV

Source: PMA

Like our trips to the US, it is apparent that the bamboo curtain remains in place from an Anglo-Saxon perspective – the understanding of China is shallow, it is conveniently fobbed off by some as experiencing a bubble. India and Russia are seen as no go areas – largely due to corruption issues.

November NAREIT

During the quarter we also attended the NAREIT conference in New York, where the tone was almost apologetic by some REIT managers who have thus far failed to deliver on earlier promises of plentiful bargain acquisitions from distressed vendors. Indeed many in the US are surprised at the strong prices being paid for the few transactions that have occurred as low interest rates drive down investor hurdle rates. IRR's on the better quality core real estate transactions have been reported to be in the 8% to 9% range. Under-bidders claim that the buyers must be factoring in higher rental growth expectations than their own, or lower capital expenditure requirements.

Somewhat reassuringly, Host Hotels and Resorts (in which the fund has a major exposure) pointed to their preference for quality acquisitions rather than entering “a pie-eating contest”.

Operating fundamentals in the US appear to be bottoming, with residential rents best placed for near term growth. Office and industrial properties remain over-rented but market rents in select CBD markets are beginning to turn around. National chain retailers are looking to expand, while hotel operators are beginning to increase room rates.

New construction remains subdued, although build-to-suit industrial development is beginning to occur in select markets where tenants have no other options. Offshore expansion was downplayed by those who had raised it in the earlier profit reporting season.

Among a number of other property inspections, we also toured the medical office building assets of Cogdell Spencer Erdman in Charlotte, North Carolina. Our investigations did not allay our concerns about the leasehold nature of the land and the relative bargaining power of the tenant/landowner and so we decided to overlook the inclusion of this stock in the portfolio. Our hunt for new opportunities continues.

Fund Performance

The J-REITs strong performance has negatively impacted the alpha performance of the Fund. We expect the magnitude of the J-REIT outperformance will prove to be abnormal and short lived due to the flawed management and fee structure of these vehicles. We do not consider ourselves particularly adept at market timing, particularly for stocks which we do not believe can sustain long term superior returns. Hence, we have chosen to continue to avoid this category favouring instead internally advised Japanese property companies such as Mitsubishi Estate and Aeon Mall, both of which outperformed global benchmarks during the quarter, but not to the same extent as J-REITs.

We remain confident that the Japanese property companies, such as Mitsubishi Estate, provide the prospect of better long term investment returns. These vehicles generally control better quality investment portfolios and have the ability to sell selectively and opportunistically to the JREITs, several of which they manage, as is likely to be the case following the BoJ's JREIT buying initiative. Furthermore, the Japanese Government's plan to reduce the corporate tax rate from 40% to 35% will further enhance returns from the corporate entities.

Our ongoing exposure to Unibail, which we believe is Europe's premier real estate company, detracted from performance. Unibail failed to maintain investor support following its special €20 per share dividend ruled off in October. This was partially offset by our avoidance of lesser quality European retail owners, including Corio, which also performed poorly for the quarter.

Given the continuation of poor performance from the Australian REITs, our decision to stand by our significant AREIT exposure has cost us. Whilst we could be accused of suffering from home market bias, in our defence we had only limited exposure to the sector in 2008 and into 2009 when we could see the magnitude of the problems facing the industry and the sector's performance was in free fall. Having cleaned up balance sheets, recalibrated dividends we believed the sector looked relatively good value in light of the strength of the Australian economy and the fact that higher interest rates had been factored into the market. For many reasons we were wrong in 2010 but we continue to believe there is value in select names.

Whilst we have largely avoided the worst examples of poor corporate governance, and hence stock selection was satisfactory, the stench of the poor corporate governance by many participants is weighing on the entire sector. Furthermore, the strength of the resources sector is driving up interest rates further than we felt necessary while the flow on from the resources boom is not flowing strongly through to tenant demand where most AREITs have much of their exposure.

We will endeavour to cull the number of AREITs in the portfolio but may not significantly reduce our nominal exposure as the local market continues to screen as relatively attractive.

The Fund benefited from its select exposure to the office sector, particularly Hong Kong Land and Mitsubishi Estate. Our avoidance of hitherto market darling Digital Realty also generated positive alpha, the stock suffering during the quarter from concerns of overcapacity in its segment of the data warehouse sector. Exposure to hotel stocks, particularly Host, benefited performance.

Portfolio Changes

Generally speaking we made limited changes to the portfolio.

We divested exposure to stocks we did not believe will produce competitive returns principally Kimco Realty and Public Storage compared with similar stocks Regency Centres and Big Yellow respectively.

We introduced positions in Soho China, Cromwell (Australia), Capital & Counties (UK) as well as Westfield Retail Trust (largely as a consequence of the in specie distribution).

Whilst the AREIT market has been impacted by poor corporate governance and capital management, not all of the Australian market deserves to be tarred with the same brush. During the quarter we added ASX listed Cromwell Property Group (CMW) to the portfolio. Management remuneration is a bargain, particularly when one considers the performance of the vehicle over the past 5 years. Management seems to be at least trying to create value, disposing of property in 2007 and acquiring in weakness of 2008 and 2009. Furthermore, despite higher than average leverage, they did not conduct knee jerk dilutionary equity raisings during the crisis. Its recent capital raising was broadly in line with NTA and at slight premium to its recent trading price. It recently announced that it is undertaking due diligence to purchase the syndicate business of Centro.

In Hong Kong, we reduced exposure to Hong Kong Land (Singapore listed) which has produced impressive returns during our period of investment. We remain attracted to China's economic growth and consequent impact on land prices but we are sceptical of commodity type residential developers which appear expensive on our metrics and are subject to ongoing efforts of the Chinese government to cool the underlying residential market.

For this reason we have sought alternative, non-residential developer opportunities. This interest was further heightened by the Chinese Government's decision earlier in the year to permit local insurance companies to directly invest in real estate. SOHO China (410) is a developer of office and retail strata units for sale to high-net-worth investors. We were attracted to the company due to its focus on downtown locations in Beijing and Shanghai, its focus on commercial rather than residential development and its strong balance sheet (net cash). SOHO has outlined a strategy to retain approximately 25% of developed stock as investment property going forward which we view favourably given the dearth of quality commercial investment exposure available in China to date. Subsequent to our initial investment, the company was reported to have achieved a record sale price for the last remaining strata office floor in The Exchange SOHO in Shanghai of RMB 100,000 per square metre compared with the average price of 67,000 per square metre for earlier sales in that project.

In the UK we added Capital and Counties Properties plc (CapCo), which was formed following the break-up of Liberty International in early 2010. CapCo owns an impressive portfolio of London properties including Covent Garden shopping centre and Earls Court & Olympia which is a medium term residential conversion land play.

Conclusion

The impact of dwindling stimulus packages is likely to impact the pattern of returns from the real estate sector, particularly relative to other investment categories.

The major risk is that REIT prices are moving ahead of long term valuations thanks to the reversionary risk of income streams which remain above current market levels. New equity issuance, particularly IPO's, is becoming an appealing option for unlisted property participants. Internet retail provides an unusual means of competition which will likely have a profound, although not yet fully understood, longer term impact on shopping centres and retail trade.

The expectation that the economic recovery path in the West is likely to be arduous provides an attractive backdrop for real estate investment given the relatively secure and high upfront income returns. Strong REIT balance sheets and the lack of new property supply, particularly speculative development, provide the basis for continued investor confidence in the sector.

By and large we remain comfortable with the key drivers for REITs. Continued exposure to select REITs remains an appropriate method of effective investment portfolio diversification.

Portfolio Top 10 Stocks

Top 10 Portfolio Holdings* – December 2010

Stock	Sector	Country
Link REIT	Retail	Hong Kong
Mitsubishi Estate	Diversified	Japan
Hong Kong Land	Office	Singapore
Home Properties	Residential	USA
Host Hotels & Resorts	Specialized	USA
Land Securities	Diversified	UK
SL Green Realty Corp	Office	USA
Simon Property Group	Retail	USA
Unibail	Retail	France
Westfield	Retail	Australia

Top 10 Portfolio Holdings* – September 2010

Stock	Sector	Country
Essex Property Trust	Residential	USA
Home Properties	Residential	USA
Hong Kong Land	Office	Singapore
Land Securities	Diversified	UK
Link REIT	Retail	Hong Kong
Mitsubishi Estate	Diversified	Japan
Simon Property Group	Retail	USA
Sun Hung Kai	Diversified	Hong Kong
Unibail	Retail	France
Westfield	Retail	Australia

*In alphabetical order

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Appendix 1

Major transactions:

The quarter saw a number of large-scale transactions, demonstrating increased liquidity in real estate markets.

Property	Vendor/Purchaser	Price	Cap rate
USA			
HCR ManorCare Inc	Carlyle Group etc/ HCP Inc	US\$ 6.1 billion	7.7%
US Industrial portfolio	Prologis / Blackstone	US\$ 1 billion	8.0%
US diversified portfolio	ProLogis / TPG	US\$ 505 million	n/a
John Hancock Building, Boston	Normandy & 5 Mile / Boston Properties	US\$ 930 million	4.3%
510 Madison Avenue New York	Macklowe / Boston Properties	US\$ 317 million	6.25% (<i>stabilised</i>)
State of California Portfolio	State of CA / Hines & Antarctica	US\$ 2.33 billion	n/a
New York City freehold portfolio	Gramercy Capital / SL Green	US\$ 390.8 million	
Midwest suburban office portfolio	Duke Realty / CBRET	US\$ 516.7 million	
South Florida office/industrial portfolio	Premier / Duke Realty	US\$ 450 million	
UK			
Westfield Stratford City	Westfield Group /APG of The Netherlands and Canada Pension Plan Investment Board (CPPIB)	£871.5 million (50%)	5.5% (estimated)
Trafford Centre	Peel / Capital Shopping Centres	£1.6 billion	5.0%
Bishops Square, London	Hammerson & OIF / JPMorgan Funds	£ 557 million	6.3% (last sale 6/09 7.3%)
25 Bank Street, Canary Wharf	Canary Wharf Group / JP Morgan	£ 495 million	Owner-occupier
Rolls Building, London	Delancey & Invista / Legal & General	£ 305 million	4.5%
Australia			
Melbourne office portfolio	Grollo / Commonwealth Property Office Fund	A\$ 581 million	7.6%
Doncaster Shopping Centre, Melbourne (25%)	LaSalle / ISPT	A\$ 350 million	5.7%
Brisbane Square, Brisbane	Westscheme / Charter Hall fund & Telstra Super	A\$ 300 million	7.7%
Australian Industrial property portfolio	Colonial fund / Dexu Wholesale Property	A\$ 232 million	9.0%
Singapore			
Marina Bay Financial Centre (33%)	Cheung Kong / Suntec REIT	S\$ 1.5 billion	4.0% <i>related party transaction</i>
Marina Bay Financial Centre (33%)	Keppel Land / K-REIT	S\$ 1.5 billion	4.0% <i>related party transaction</i>
Keppel Towers & GE Tower	K-REIT/ Keppel Land	S\$573 million	Residential redevelopment
Continental Europe			
OpernTurm office tower Frankfurt	Tishman Speyer & UBS / JPMorgan Fund & GIC	€550 million	
Blåmannen 20 city block in Stockholm	HausInvest / Vasakronan	SEK 4.35 billion (A\$ 650 million)	5.0%
Swedish/Nordic office & industrial portfolio	NR Nordic & Russia Prop / Kungsleden	SEK 3.6 billion (A\$ 537 million)	7.0%
German retirement portfolio	Kungsleden / Hemso	SEK 1.3 billion (A\$ 194 million)	7.0% (similar to acquisition price in 2006/7)