



RESOLUTION CAPITAL GLOBAL PROPERTY SECURITIES FUND

MARCH 2010

QUARTERLY INVESTMENT REPORT



GLOBAL REAL ESTATE SECURITIES

Fund Investment Performance

The Resolution Capital Global Property Securities Fund under-performed the UBS Global Investors Index (AUD Hedged Net TR) by 257 basis points for the quarter ended 31 March 2010.

Period Ending 31 March 2010*

	Quarter %	6 Month %	1 Year %	Since Inception [#] %
Fund	3.91	11.05	73.13	0.73
Benchmark	6.48	11.88	79.71	-11.26
Difference	-2.57	-0.83	-6.58	11.99

*Returns are expressed after deducting investment management costs.

[#] 30 September 2008

Resolution Capital Global Property Securities Fund Unit Price - Class A

	Entry	Exit
31 March 2010	\$0.9269	\$0.9213
31 December 2009	\$0.8920	\$0.8866



Market Performance

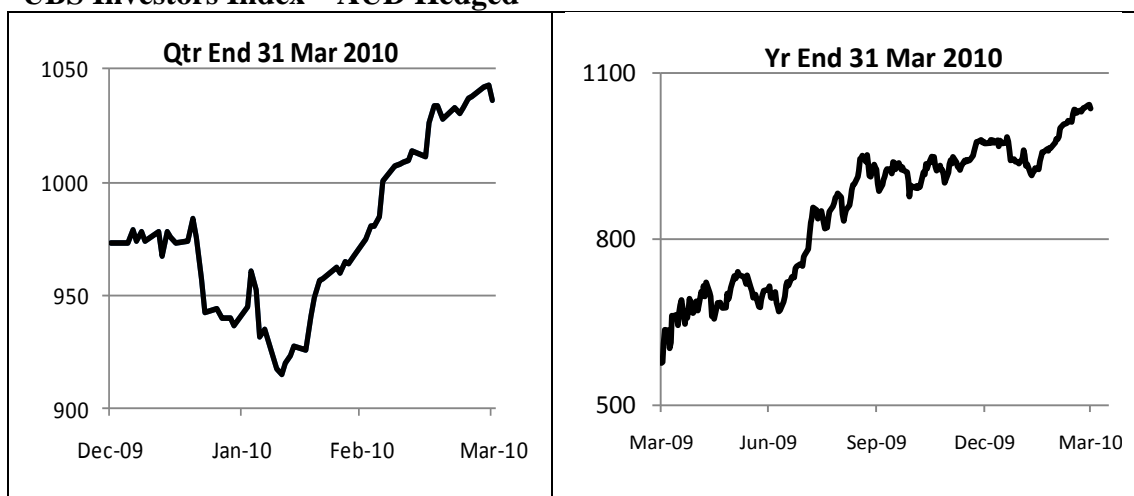
Market Overview

	31 March 2010	31 December 2009	Quarterly Accumulation Return
UBS Global Investors Index AUD (Hedged)	1,036	973	6.5%
UBS Global Investors Index AUD	881	857	2.7%
S&P/ASX 300 (GICS) Property	18,990	19,306	-1.6%
S&P/ASX 300 Index	34,340	33,916	1.3%
10 Year Bonds	5.76%	5.72%	
AUD/USD	\$0.917	\$0.8973	2.2%

Commentary

Global REIT markets weakened in the first half of the March quarter as a lacklustre reporting season and renewed sovereign default risk highlighted by Greece's position weighed on sentiment. At its low point the market had fallen 6.0% by early February but a combination of M&A activity and the US Federal Reserve's stated intention to keep interest rates low, despite some signs of improving economic conditions, ignited a rally which saw the market rebound back into positive territory to deliver a 6.5% total return for the quarter (hedged).

UBS Investors Index – AUD Hedged



Source: UBS

The US was the strongest performing region, with the rebound triggered by Simon Property Group's US\$10 billion takeover bid for General Growth Properties (GGP) which was announced on 16 February 2010. This was followed by an alternative US\$6.5 billion equity recapitalisation proposal from a group of investors which, if successful, would see GGP emerge from bankruptcy. The competitive bidding for GGP and lack of other significant transactions highlighted that the volume of distressed selling to emerge from the financial crisis has so far been less than many had expected. In fact many REITs had positioned themselves to take advantage of distressed selling opportunities by raising equity but have since found that the few assets that have been put to market have been well bid. As one US REIT manager told us, "this is the greatest buying opportunity never to happen".

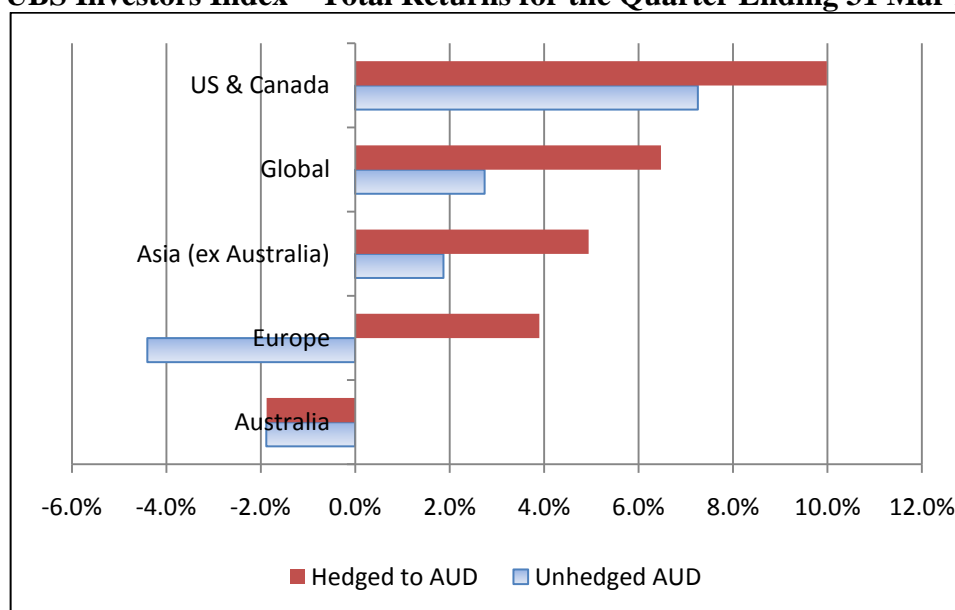
UBS Investors Index Total Returns – AUD Hedged

	Quarter	1 year	3 year
Global	6.5	79.7	-16.0
US & Canada	10.0	107.6	-14.3
Europe	3.9	68.9	-18.4
Asia (ex Australia)	4.9	42.8	-12.4
Australia*	-1.9	38.6	-22.0

Source: UBS

* Constituents may differ from S&P/ASX 300 (GICS) Property

UBS Investors Index – Total Returns for the Quarter Ending 31 Mar 2010



Source: UBS

Australia was the weakest performing region with rising interest rates and a strong AUD continuing to act as headwinds on the sector.

Importantly, the quarter saw a number of real estate players around the world kick-start their development pipelines as the outlook for real estate markets have improved enough to stimulate new supply.

Real Estate Operating Conditions

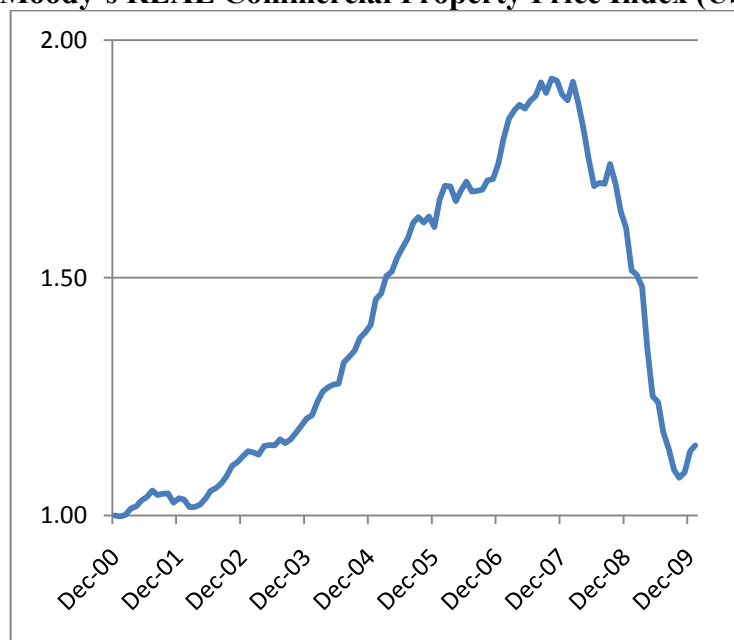
Reporting season was lacklustre across most regions except Chinese developers who reported strong 2009 EPS growth following a lean 2008. China's stimulus initiatives led to a massive spike in lending, fuelling strong price and volume growth for the mainland residential developers. Subsequent fears of a property bubble has seen a reversal of government policy to reign in speculation, continuing the push-pull cycle of Chinese government policy impacting residential real estate. Elsewhere, 2009 results and 2010 earnings guidance reflected the impact the financial crisis has had on economic drivers which are delaying space absorption and consequent rental growth. Higher share counts from equity recapitalisations of 2009 plus elevated tenant incentive capital expenditure combine to act as a drain on growth. "Flat is the new up" was how Simon Nyilassy, President/CEO of Canadian REIT Calloway, described the environment.



Notably, two global property heavyweights disappointed the market with lower than expected 2010 guidance. Australian based Westfield forecast distribution for 2010 of A\$0.64, which based on 70% - 75% payout implies earnings per share of A\$0.85 to A\$0.91 in 2010. This compares to A\$0.94 per share in 2009, with \$0.02 of that from hedging (offshore earnings will no longer be hedged). Meanwhile French-based Unibail-Rodamco forecast earnings growth to be 0% - 2%, well below the high-single-digit annual growth to which the market has become accustomed from Continental Europe's benchmark stock.

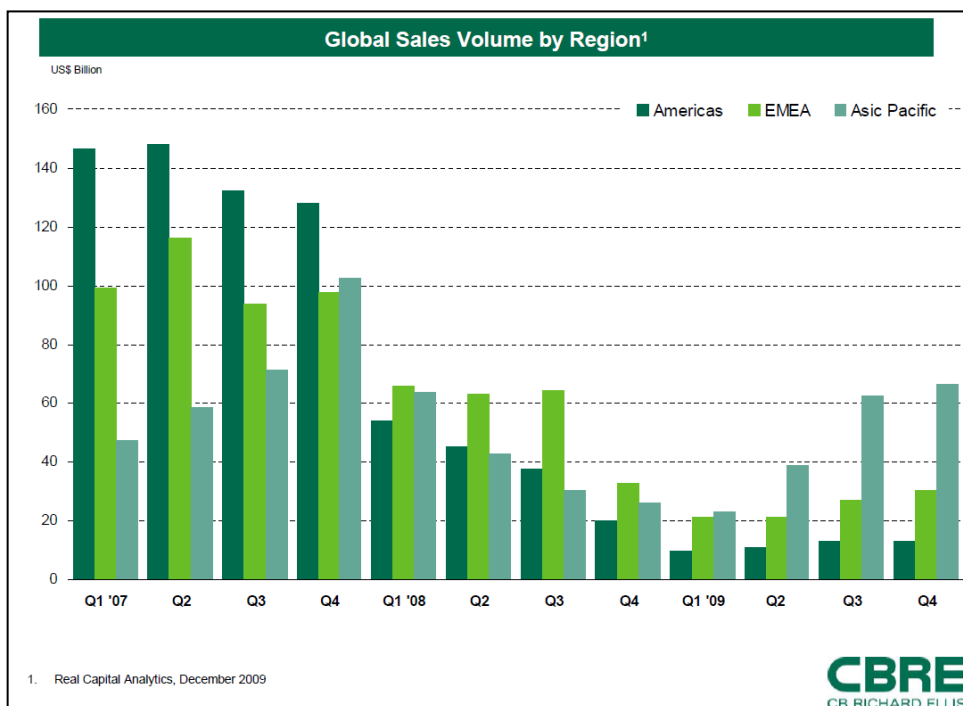
Most IFRS reporting companies announced a stabilisation of asset valuations and opined that asset prices had bottomed. In the US this was evidenced by Moody's REAL Commercial Property Price Index beginning to turn positive after troughing at a level 44% below its peak. Japan was one of the few markets where write downs continued with Mitsubishi Estate announcing a well-anticipated further ¥120 billion impairment charge on office and residential assets including two office developments for which it had acquired the land in 2007.

Moody's REAL Commercial Property Price Index (US)



Source: Moody's

Real estate capital market transaction activity has remained well below levels experienced in the preceding 5 years, with the exception of the Asia-Pacific region. Lower than expected distressed selling appears to have led to a pent-up demand for investment opportunities by those who have positioned themselves in advance. Some REITs, particularly in the US, found themselves struggling to find areas to deploy the cash that was raised throughout 2009, evidenced by Vornado Realty Trust announcing that its dividend would be paid entirely in cash after paying the previous amount partially in stock over the last year to bolster its firepower.



Source: CBRE

Hence the relatively few opportunities that have been put to market have been well bid. Significant transactions during the quarter included:

- US multifamily REIT Equity Residential bought three luxury apartment towers in Manhattan from troubled New York real estate investor Harry Macklowe. The US\$475m purchase price reflects a relatively firm 5.5% cap rate and was funded with proceeds from previous asset sales.
- It was also reported that Macklowe, who failed to refinance a multi-billion dollar loan to Deutsche Bank in 2008, sold the former Drake Hotel site at Park Avenue and 56th Street in New York for US\$305 million. The transaction was significant in that land purchases, particularly of this magnitude, have been rare during the financial crisis. The purchaser was an entity affiliated with California-based investment firm CIM Group.
- Unibail-Rodamco sold five Dutch shopping centres above book value to local rival Wereldhave for EUR235m and subsequently acquired stakes in seven malls in France and Poland from Simon Property Group (SPG) for EUR715m. Proceeds from SPG's sale boosted the acquisitive US REIT's firepower to fund its earlier acquisition of Prime Outlets as well as its bid for GGP.
- Corio announced a EUR1.3bn acquisition of a portfolio of new German shopping centres and developments from European developer Multi Corp. The deal is roughly split 50:50 between operating assets and developments, with Corio sharing development profits with Multi on about 40% of the developments. The operating shopping centres will be acquired at a net initial yield of 6.5%.
- Singaporean REITs ventured to Australia to acquire property including:
 - K-REIT Asia acquired a 50% stake in 275 George St in Brisbane from Charter Hall.
 - Starhill Global REIT acquired the David Jones Building in Perth from Centro for A\$114.5m.



- CDL Hospitality REIT acquired five hotels in Brisbane and Perth for A\$175m.
- They join a number of foreign property investors who have recently entered Australia, most significantly from South Africa and South Korea.
- Singaporean office REIT, CapitaCommercial Trust sold Robinson Point for SGD203.25 million to AEW. The sale price was an 11% premium to the December 2009 valuation and is a rare example of a sale by an externally managed Asian REIT. Management have stated it intends to re-invest the proceeds into higher growth opportunities.
- Victoria House, Bloomsbury Square in London's West End was purchased by M1 Real Estate for £175 million. This was the largest office deal in the West End since 2007. The vendor was Moritz Group.
- The acquisitive South Korean Pension Fund purchased a 12 per cent stake in Gatwick airport.

There were also significant leasing transactions in London including one example where competing tenants out-bid each other in order to secure a large block of space. Blackrock prevailed in leasing 300,000sqft of space in Drapers Gardens at £49psqft for 25 years, trumping earlier plans by Macquarie Bank to occupy the space for a reported £45psqft. Macquarie subsequently agreed terms to lease 217,000sqft at British Land's Ropemaker Place development.

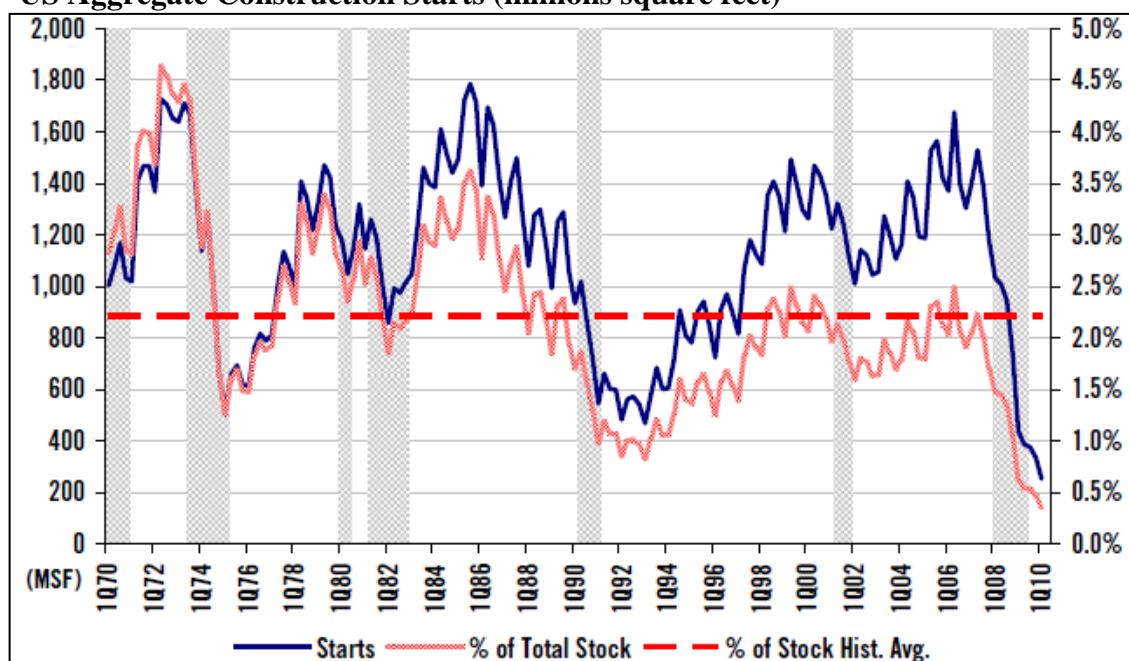
Perhaps the most notable feature of this quarter was the return of real estate development activity. Importantly this includes speculative development as some real estate players begin to position themselves for the next up-cycle recognising the lead time required to complete new projects.

- US multifamily REIT Avalon Bay, said it will start US\$400m of construction this year after a nine month hiatus from development.
- Land Securities announced it would re-start £655m worth of speculative developments in the West End in addition to possibly resurrecting its "walkie talkie" project in London City.
- Great Portland Estates triggered an 80,000 square metre speculative project in London's Bishopsgate by selling a 50% stake to Brookfield Properties who will joint venture the re-development starting in 2011-12. Brookfield paid £42.975 million for their 50% interest.
- Lend Lease signed a project development agreement on the 490,000 square metre stage 1 of the Barangaroo site on the Sydney CBD's western foreshore. Construction of the first commercial building is anticipated to commence by December 2010 with Lend Lease indicating tenants had already expressed interest. The total Barangaroo project is expected to deliver a mix of office, retail, residential and hotel space over the next 10-15 years with an end value of A\$6 billion.
- Grocon will build a 58,000 square metre office tower in Sydney after having earlier secured 75% conditional pre-leasing to ANZ Banking Group and Freehills. By selling 75% of the project (50% to GPT Wholesale Office Fund and 25% to LaSalle) Grocon effectively kick-started the A\$660 million project.
- Aspen also said it will go ahead with a A\$200m, 35,000sqm office development in the Adelaide CBD following a 30,000sqm pre-lease with the ATO for a 15 year initial term.



- Aeon Mall informally announced plans to develop 10-15 shopping centres in China by the end of FY16. Seven are planned for suburban Beijing with a total capital cost to be circa ¥20.0 billion.
- Westfield announced that it had successfully preleased the proposed new office component of its Pitt St mall redevelopment. JP Morgan will occupy 16,700 square metres in the new tower to be known as 85 Castlereagh Street.
- Charter Hall Office REIT sold a 50% interest in 171 Collins Street in the Melbourne CBD for A\$15.5m to Cbus Property who will joint venture the re-development project.
- Also in Australia Westfield, Goodman Group, CFS Retail Trust and Stockland all announced that they would resume commercial development activity.

US Aggregate Construction Starts (millions square feet)

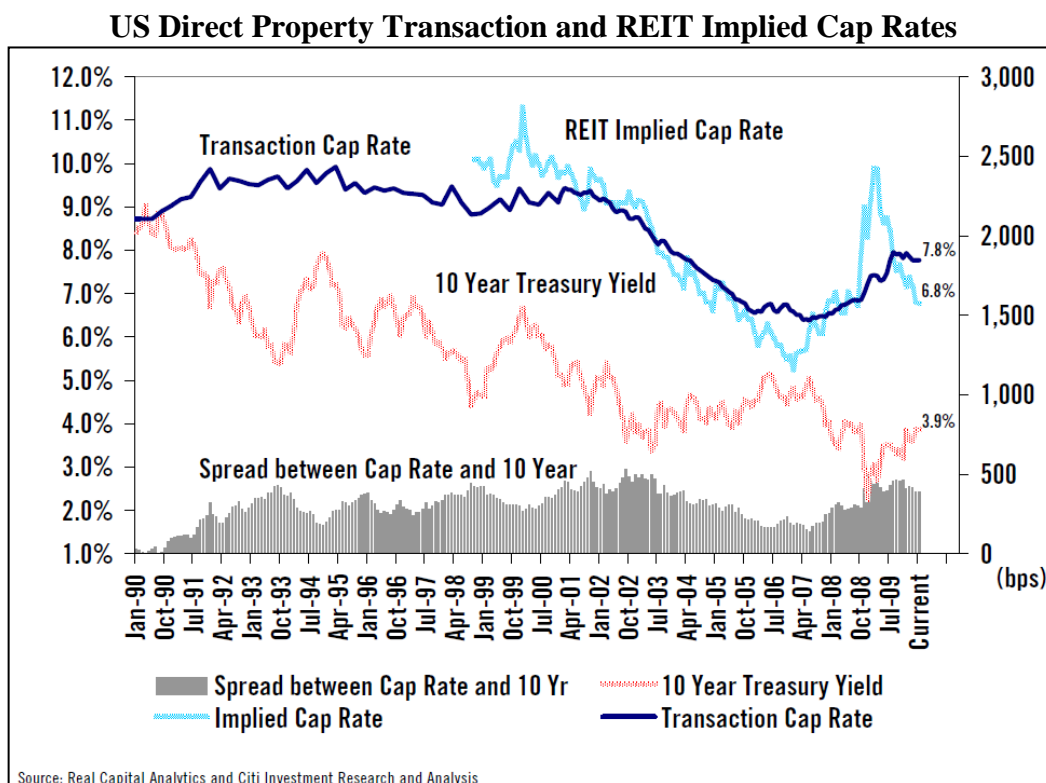


Source: Citi Investment Research and Analysis

REITs and Real Estate Capital Markets

Simon Property Group (SPG) made an unsolicited bid for competing mall owner General Growth Properties (GGP). Simon's offer valued GGP at US\$9 per share for the equity (US\$6 cash and US\$3 implied for the land business through a spin off) and par plus accrued interest and dividends for all the unsecured debt. GGP initially countered the offer with a plan to exit bankruptcy proceedings by splitting the company in two, with Brookfield Asset Management pledging US\$2.63bn to that effort. The plan called for creating one company that owns roughly 180 of General Growth's higher-quality malls and a smaller one that owns riskier real-estate holdings, geared to investors willing to gamble on higher returns. The General Growth-Brookfield plan values General Growth at US\$15 per share. It was subsequently announced that Fairholme Capital Management (one of GGP's largest unsecured creditors) and Pershing Square Capital Management (one of GGP's largest equity investors) had offered an additional US\$3.9 billion to Brookfield's offer, bringing the total equity commitment to US\$6.5 billion. Amid the competition, Westfield (WDC) was reported to have signed a nondisclosure agreement to begin discussions with General Growth about a possible offer.

The prospect of M&A activity and firming property values spurred a rally across the US REITs. The following chart shows that the implied cap rate of US REITs is now 100 basis points firmer than average direct market cap rates.



Meanwhile Liberty International (LII) is proposing to demerge into two listed entities, one composed of £5bn of shopping centres and the other £1.2bn of London properties. The latter will not retain its REIT status due to its development exposure and exhibition business. The Capital Shopping Centres portfolio includes 13 UK malls which would include assets attractive to Westfield and Simon Property Group who both acquired stakes in LII in 2008. The spin-off of its London estates potentially makes the remaining shopping centre portfolio more attractive to such suitors. More-over, if the demerger proves successful it could spur UK diversified REITs to consider demerging into sector specialist entities. Land Securities toyed with this concept a few years ago but ultimately rejected it after selling its Trillium unit in a trade sale. For a further discussion on the merits of diversified property entities please refer to the appended text of a speech presented by Andrew Parsons to the 2010 AFR Commercial Real Estate Conference.

M&A in the JREIT sector continued with Japan Rental Housing and Prospect REIT Investment Corp announcing a merger in March, the fifth merger in the past year.

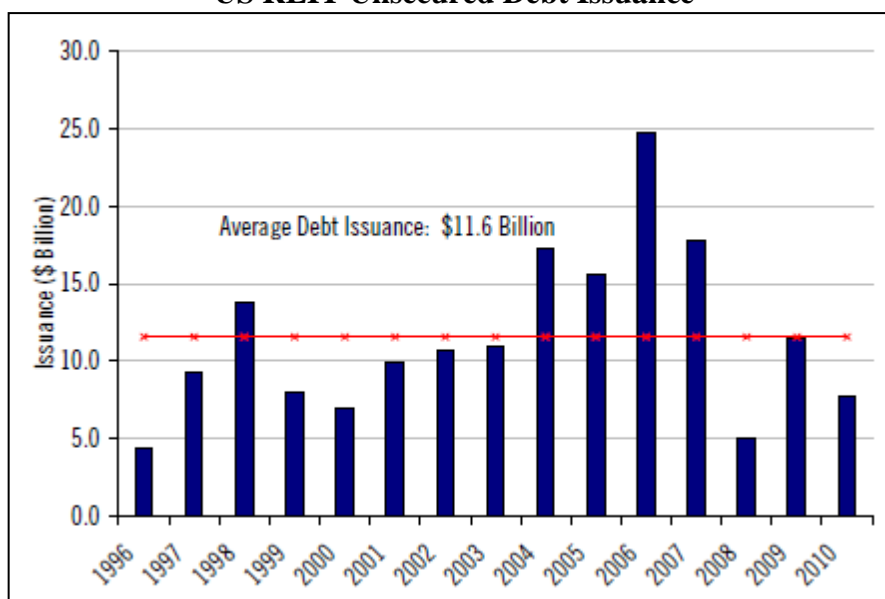
Equity raisings were relatively subdued during the quarter and included:

- Piedmont Office Realty Trust, an unlisted REIT with multiple classes of shares, raised US\$174 million via an IPO of its Class A shares on the New York Stock Exchange. The shares closed the period at US\$19.85, a 37% premium to the IPO price.
- Metric Property Investments raised £175 million via an IPO on the London Stock Exchange. It listed in late March and closed the period at £1.025, a 2.5% premium to its IPO price.

- In contrast, Terreno Realty Corp of the US shelved its US\$200m planned IPO in late January due to a lack of interest. The REIT intended to use the proceeds to buy unidentified industrial properties in US coastal markets.
- Charter Hall Group (CHC) raised A\$305 million to fund the acquisition of Macquarie Bank’s real estate platform and co-investment stakes (referred to later in this report). The average price of the placement and rights issue was A\$0.69.
- Lend Lease raised A\$806 million at A\$8.60 per share to fund a string of recent acquisitions and developments wins.

Meanwhile debt capital markets activity has begun to recover. In the first quarter of 2010 US REITs issued over US\$6 billion of unsecured and convertible debt, putting it on track to exceed the average of the last 14 years. This was achieved after many REITs had bought back large amounts of short-dated debt at discounts to par, allowing them to extend maturities while in many cases lowering the cost of debt. Notable issuers included Simon Property Group’s US\$1.25billion 10 yr note issued in January at a coupon of 5.65% and Vornado’s US\$500m 15 year issue in March at a coupon of 4.25%.

US REIT Unsecured Debt Issuance



Source: Citi Investment Research and Analysis and SNL

Singapore REITs were also active in the debt capital markets extending maturities at a lower average debt cost. Ascendas REIT and CapitaCommercial Trust both issued convertibles at coupons of 1.6% and 2.7% respectively with conversion premiums of 25%.

CMBS issuance remains relatively low, with some industry commentators predicting that up to US\$30 billion could be issued in the US in 2010. While this would be a 3-fold increase on 2009, it is still only a fraction of US\$230 billion issued in 2007.



Management Changes

Investment banks appear to be exiting the property funds management business perhaps reflecting higher returns available elsewhere or regulatory and capital pressures triggering divestment of non-core businesses.

In Australia Macquarie Bank sold its real estate funds management platform to Charter Hall Group (CHC). The business included management rights on two listed A-REITs (Macquarie Office Trust and MacquarieCountryWide Trust) as well as three smaller unlisted funds. The \$108 million sale price (excluding co-investment stakes) equated to a 7.7x multiple on 2011 forecast EBITDA and 1.5% of assets under management. The transaction also included CHC purchasing 7.5% equity stakes in the two listed vehicles from Macquarie, with a first right of refusal to purchase the remaining 6% and 4% of each respective vehicle still owned by Macquarie. Highlighting the conflicts of interest in the external management model, Macquarie agreed to vote its remaining units (effectively a blocking stake) in-line with CHC on any resolution to remove the manager for 12 months. Furthermore, we note that unitholders in the underlying vehicles were not given an opportunity to vote on the change in stewardship of their capital nor vote on any other alternative proposals.

Meanwhile press reports suggest that Citigroup had agreed to sell its Citi Property Investors unit to private equity firm Apollo Management and ING is close to offloading its global real estate platform to Blackrock.

In Hong Kong, further management changes at The Link REIT were revealed, with CEO Ian Robbins saying he would not renew his contract that expires in November 2010, with the current CFO to succeed him. The change comes after the resignations of fellow Australians COO Ross O'Toole earlier in the month and Project & Development Director Scott Nugent in December 2009. All three are expected to return to Australia. We continue to monitor our position in this stock carefully in light of these changes, in particular the pace and success of its efforts to maximise value from the existing portfolio via active asset management.

Resolution Capital Travel Insights

During the quarter the Resolution Capital team toured the NSW Central Coast – Newcastle region, visiting shopping centres and residential projects owned by Westfield, Stockland, GPT, CFX and Mirvac. Retail conditions appear to generally be solid with most reporting sales increases in the range of +3% to 6% driven by supermarkets and mini majors. Stockland Greenhills and Glendale were both trading very strongly, the latter a unique asset in the Australian market due to its open-air design. GPT's massive cap-ex program in the Newcastle region is of some concern for us, particularly the mooted redevelopment of the Newcastle CBD site. It is an ambitious project which could potentially re-invigorate the city and with many community benefits. However in our view the significant cost, competition and nature of the trade area gives us cause for concern. Meanwhile Mirvac's residential development on the site of the former Newcastle Hospital appears to us to have too many high-priced penthouse apartments for the size of this market.

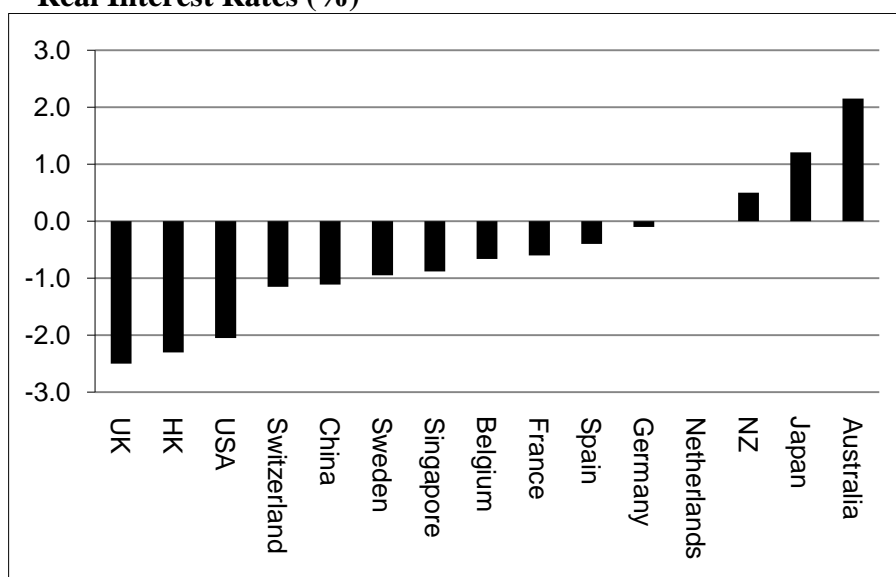
Outlook

Better quality REITs are well positioned to capitalise on weaker real estate owners and lenders who remain over-leveraged. The emergence from bankruptcy of General Growth Properties (GGP) is currently playing out. Simon Property Group's take-over bid, and competing recapitalisation proposals indicate strong demand for distressed real estate opportunities. If direct market transaction activity remains subdued we expect to see REIT-to-REIT or REIT-to-private M&A activity.

Meanwhile, relatively subdued construction supply outlook, low interest rates and lender forbearance on problem loans acting to defer large-scale distressed selling looks to underpin the near term outlook for asset prices. We have under-estimated the effect such a powerful cocktail would have on US REITs which have outperformed strongly this quarter.

The question is how long can the sweet-spot last where real interest rates are being held low while successfully reflating asset prices and economic growth. Much rests on the timely shifting of current policy settings (as it did after the dot-com crash, where the US arguably kept rates too low for too long which sowed the seeds for a housing bubble). The widening of interest rate differentials and the prospect of currency appreciation in Asia are likely to impact capital flows.

Real Interest Rates (%)



Source: Bloomberg, RCL

We believe there is a high probability of new equity issuance including IPO's, re-listing of previously privatised REITs (including Archstone in the US, Investa and Brookfield/Multplex in Australia), and placements to fund acquisitions (including whatever happens to GGP), new developments or debt re-financing.

Financial market regulation may yet impact all asset classes as shifting ground rules alter the availability and cost of capital. More particularly for real estate the impact is mostly likely to be felt on office market dynamics. If proposals succeed to break-up the 'too-big-to-fail' investment banking goliaths we could see a shift in the size, type and locational requirements driving office space demand in the larger financial hubs. New York landlords have already reported leasing activity to newly established investment boutiques set up by former employees of larger investment banks.



Longer term the REIT sector will need to see sustained earnings growth. Rebounding GDP growth is a positive driver. However the overhang from the financial crisis including lower rents, higher vacancy rates, higher tenant incentive cap ex and higher share counts are likely to be a drag on earnings for some time.

We remain focussed on investing in good quality real estate with strong recurring cash flows where management has the capability and capacity to exploit both internal and external growth opportunities.



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Appendix 1

AFR Commercial Real Estate Conference 2010

16 Mar. 10

The Future of the Listed Property Sector

I am pleased to have been asked back to once again discuss the future of REITs. I am keen to see if I could predict last year what I would say about the future in the future. The major themes that I outlined last year included:

- The problems that beset a number of A-REITs were primarily due to capital mismanagement;
- For the majority of A-REITs, leverage should be low principally due to management limitations and the lack of depth of local debt markets;
- The Listed REIT remains relevant as an efficient structure for real estate ownership;
- Investors must set reasonable risk/return expectations from the A-REIT sector, particularly given the natural limitations of the domestic physical market and REIT management talent pool; and
- The ongoing importance of liquidity.

I stand by what I said and, for the sake of consistency, it is my intention to elaborate upon some of these issues with a clearer view from today's vantage point.

As the 19th century UK Prime Minister Benjamin Disraeli once said "How much easier it is to be critical than to be correct". I appreciate that from the REIT investor's side of the fence one could underestimate the challenges for any public entity in executing a sensible long term strategy, whilst listening to the seemingly ever changing whims of investors and corporate advisors. However, as the listed REIT relies upon public capital this comes with added responsibility and scrutiny.

For much of the past 10 to 15 years, A-REITs have provided the backbone of institutional real estate exposure thanks to the quality of the real estate, transparency, liquidity and, up till 2007, impressive return history. Crucially, poor returns and the extraordinary volatility over the past 5 years has triggered a realisation that the local REIT industry alone is insufficient in providing a high quality, high volume solution to the substantial needs of the Australian superannuation industry. Asset allocators now are taking a holistic approach to real estate. This is the critical issue confronting what is termed the A-REIT industry.

I should note the term industry is somewhat fallacious. The industry is the collective outcome of disparate management teams and strategies. In reality the A-REIT industry includes a range of products, some good, others developed to exploit investor appetite for what they thought was a foolproof investment. To those that held that expectation, let's be clear, real estate is cyclical and has never been a foolproof investment!

Nevertheless, having survived the latest Financial Crisis, investors and A-REIT management are dusting themselves off, surveying the damage and trying to set a course for the future. REITs are scurrying for property acquisitions, some M&A activity has already occurred, REITs are buying funds management businesses and development is back on the agenda. It seems we've learnt our lessons, balance sheets have been restored and dividend pay-out ratios set at sensible levels. The equity raised, clumsy as it was, has washed away the sins of the past, redemption is at hand. In the year to 28 February 2010 the A-REIT index produced a total return of over 40%. It would be easy to believe the worst is over and REITs will regain their prominence, their reputations restored.

However, focusing on a short and extraordinarily positive return period such as the past 12 months is self serving and misrepresentative. Asset allocators take a far longer perspective that



incorporates a full market cycle to indicate what we might expect from the A-REIT sector in the future.

For many investors, real estate serves as a store of wealth which should be expected to produce a total return of at least the risk free rate, somewhat lower than equities but with lower volatility and typically a higher income yield. REITs are capable of delivering to this objective, the overlay of responsible capital enhancing initiatives, for example modest amounts of debt, should enhance the returns to unit holders.

Investors now have a suitable long term history to judge whether in reality A-REITs meet this objective and the results are not flattering. An appropriate long term time frame is provided by measuring risk and returns over like with like market conditions. Hence, we can now look back from the 2009 bottom of the market to the previous property downturn which bottomed in 1992 to look at trough to trough returns. In this 17 year full investment cycle, the A-REIT produced a compound total return of approximately 5% per annum. Whilst nominally this is unacceptable, the volatility of these returns has severely dented the sector's credentials forcing dedicated supporters to lose confidence.

This long term return profile warrants further explanation. In the past 17 years and beyond, the A-REIT industry has experienced a multitude of varied and competing forces – including a significant growth phase involving the listing of previously unlisted vehicles in the early 90's, forays into overseas real estate markets, external to internal management, the dalliance with development trusts, the growth of funds management income streams, mergers, acquisitions and privatisations, unleveraged to highly levered balance sheets, tight equity issuance to the recent flood of emergency equity capital raisings.

Not only have the markets changed, so too has the nature of the A-REIT investor altered. For 20 years after its inception in the 1970's A-REITs, or LPTs as they were then known, were largely the domain of retail mum and dad investors. With institutions burned by their unlisted and direct holdings in the early 1990's, isn't that ironic, over the subsequent decade A-REITs enjoyed favoured sector status and an arm chair ride provided by the compulsory superannuation inflows together with plentiful cheap credit.

Whilst not dismissing the importance of recognising your constituency, REIT managers must appreciate that there is a danger of complicating a long term real estate investment strategy with the ever changing moods of investors and interests of corporate advisors. Too much emphasis continues to be placed on short term earnings accretion rather than long term value creation. Investment banks continue to prosper by exploiting the anxieties of weak management and need for instant gratification. Over time investors, or was it investment banks, have demanded: high yield, growth, security, yield accretion, dividend recalibration, specialisation, diversity, simplicity, balance sheet leverage, share buy backs, hedging, asset light funds management models and recapitalisation. Fundamentally, many of these themes conflict and it is difficult to interchange real estate portfolios and capital structures as quickly as these terms change.

From this it is reasonable to observe that markets and sectors are rarely, if ever, efficient or in equilibrium. The only constant is change. Alternatively, in a nutshell, you can't be all things to all people all of the time.

It is important to recognise that a number of A-REITs have delivered credible strategies and resultant investment performance. Unfortunately these sound A-REIT operators have been tarred with the same brush as those that failed investors and the perception of the REIT structure.

That said, I repeat, whilst there are a number of examples of quality A-REITs, their numbers are too few and their combined size too small for a reasonably large investor, such as the super industry, to use A-REITs alone as the primary form of real estate exposure.



With the structural flaws of the industry and performance shortcomings of a real estate exposure focussed on A-REITs laid bare, debate has consumed investors on various fronts: listed versus unlisted, global versus domestic, volatility - perceived or real, is it a real estate investment or a subset of the equities market?

Bottom line, Australian superannuation funds are voting with their cash by switching from A-REIT dominated portfolios into a mix of domestic unlisted real estate and global REITs.

As a consequence, A-REIT unit registers now are far more broad-based including general equities investors, hedge funds, mums and dads as well as global REIT funds. Whilst broad based, the problem is that much of this money is transitory. The implications of this change are significant and far reaching. Having lost the support of previously patient dedicated investors, A-REITs now must compete harder for capital against a far broader range of alternate investments from an often fickle and discerning group of investors. Hence, it is likely that for the foreseeable future the sector's relative cost of capital will be considerably more expensive.

Now that they truly appreciate that capital is scarce and precious, A-REITs must confront the following questions: What is my fundamental value proposition; and: How can an A-REIT be globally competitive?

Being prescriptive about what form the sector should take is pointless – it is up to the individual market participants. There is no foolproof or one size fits all formula. Nevertheless, there are some basic principles.

One area that A-REITs should address is the notion of diversification. Indeed in my opinion, diversification must be one of the most abused terms in the industry's lexicon. Many managers have hidden behind mediocrity by extolling the virtues of different levels of diversification. Diversification can justify just about anything but generally means in effect adding to a portfolio. I would like to pause on this point to make an observation that the recent round of extraordinarily dilutive equity raisings makes a mockery of those management teams that now claim they are in a position to take advantage of current property bargains.

Most A-REITs have sufficient size and liquidity to be on most investor's radar screens and a critical mass of assets for management to stay above the poverty line. Hence they do not need to accumulate assets. As Warren Buffett recently said, we operate in "a world where size tends to correlate with both prestige and compensation".

I have no qualms with the theory of diversification and the increasing trend toward mixed use development appears to add merit to certain real estate groups being across sectors. In practice, few A-REIT managers appear to understand some basic principles and concepts including tactical versus passive asset allocation or the risk of over diversification which leads to diseconomies of scale or losing critical points of difference. Furthermore, many managers destroyed any risk minimisation benefits of diversification by over leveraging. Diworsification is perhaps more apt.

Global diversification, as pursued by many of the A-REITs, has now been abandoned in favour of the all new and improved strategy of "simplification". It is ironic, and an indication of how flawed the strategy of many was, that at a time when the Australian dollar is making highs against many currencies and the local buoyant economy is heavily dependent upon our ability to dig rocks out of the ground, that many local REITs are disposing of offshore investments in cyclically weak economies. Looking at the evidence, one could argue there has been a strategy pursued by some groups of buy high sell low and the "best of breed" jvs could be renamed "best of greed".

Whilst Resolution Capital believes it is possible for A-REITs to successfully invest globally, we acknowledge it is extraordinarily difficult to execute. As I said last year, few A-REITs have the necessary resources to effectively establish on the ground, high calibre property investment



and management teams in different countries with the multitude of challenges that this brings including issues surrounding culture, politics, law and currency. Those that have succeeded appear to be focussed on particular locations and sectors on which they can apply a transferable skill set.

Instead, there are plenty of studies that prove that global REIT investors can more efficiently diversify sectorally and geographically. It seems the superannuation industry's increasing allocation to global REITs supports this view, Mohammad is now going to the mountain.

What I now want to highlight are some examples of success and factors that Resolution Capital has found around the world that demonstrate true best of breed REITs stand out through a commitment to quality and end results. These stocks now represent the benchmark for the A-REIT.

First thing to note is that size is not the issue in delivering performance.

London listed Shaftesbury plc is a UK REIT with an enviable track record and total assets of approximately \$2 billion. The REIT has maintained a patient strategy over the last 25 years of assembling clusters of buildings in busy areas of London's West End including Carnaby Street, Covent Garden and Chinatown. It employs just 19 people and focuses on driving significant earnings growth through reconfiguration to higher uses and incremental amenity improvements that benefit the entire area. Its strategy to attract unique and innovative retailers provides a distinctive retail destination for consumers.

Federal Realty is a US shopping centre REIT with a successful long term track record including 42 consecutive years of dividend increases. Its strategy is built on three simple premises: restricting investments to only top quality real estate, fiscal conservatism both from a balance sheet and operating perspective and a selective approach to acquisitions and developments. In practice it is focussed on shopping centres located in wealthy high barrier to entry markets. Management is conservative in acquisitions; the number of properties acquired each year can be counted on one hand. Since 2002 they have bought 15 properties and own only 84 in total. They shun portfolio deals, because these inherently include weaker centres.

French REIT Silic is another example of a targeted, value-add, strategy. It has remained focussed on four districts in and around Paris where it is gradually improving the value of the land. It owns what were previously industrial estates close to Paris's airports where it is gradually replacing aged warehouses with highest and best use office buildings.

This doesn't mean you have to be small to be focussed. With assets valued over \$33 billion, Unibail Rodamco is one of the world's largest and is arguably continental Europe's premier REIT. Despite its size it is run on the mantra of being a small vehicle, driving each asset hard. Although diversified, its strategy is to supplement returns from its European fortress malls with earnings from its Paris convention centres as well as value adding opportunities in the office market. It regularly reviews the return prospects of each property, disposing of the assets where it has maximised value creation, reinvesting the proceeds in other properties in the portfolio or selectively acquiring new properties where it can add value.

Meanwhile, US REIT Boston Properties has demonstrated the benefits of a disciplined strategy operating in a cyclical sector. Boston Properties is focussed on key office markets in North America. Supplementing its stable office investment portfolio, it bought land in the early 90's TMT crash, developed it, sold it at record prices in 2006 and maintained low leverage against the advice at the time to lever up. Because of its prudent capital management, in 2008 it was able to purchase the GM Building, arguably the best office building in Manhattan from a distressed vendor.



These stories demonstrate what it takes to successfully compete for capital. Each of these vehicles operate within highly competitive markets that have not necessarily demonstrated particularly strong underlying economic growth. Because of the quality of their portfolios and strategy, they trade at a price that gives them a cost of capital advantage which they exploit judiciously.

I challenge anyone to identify quality real estate opportunities of the scale, transparency and efficiency of those available in the global listed REIT market. This is why Australian institutions are moving down this path and why Resolution Capital has been promoting this avenue for several years.

Which brings us to the other great industry debate of listed versus unlisted property. Ongoing discussion surrounding the perceived low volatility of unlisted real estate is of limited benefit for long term investors if the quality of the underlying assets and capital structure is broadly similar. Nevertheless, there remains an undeniable perception that only unlisted real estate provides real estate like returns. Quoting from Benjamin Graham's *The Intelligent Investor*, which was first published in 1949, "it is self-deception to tell your-self that you have suffered no shrinkage in value merely because your securities have no quoted value". Bottom line, as I said last year, if being listed is that bad, the sensible thing for REITs to do is delist.

Unlisted real estate provides its own set of challenges and some in common with its listed rivals. The listed sector was not alone in overleveraging. Unlike REITs today, debt refinance remains an unresolved issue of large parts of the unlisted market. Many funds remain frozen and debt maturity issues loom large on the horizon. Quality control also is a challenge.

Whilst in theory long term the difference in returns of each should not be fundamentally different, it is essential for successful investment outcomes to choose the best exposures and be cognisant of liquidity issues. Too much exposure to markets and products with limited depth and liquidity creates unnecessary dislocation from time to time which has been evident in both domestic listed and unlisted real estate over the past 20 years.

The reality is that liquidity and transparency are critical issues for the Australian superannuation industry under the fund and investor choice regime. A significant ill-disciplined move by the super industry back into unlisted domestic real estate would be a retrograde step. We call upon regulators to clarify the position of unlisted investments in super funds before there are major catastrophes.

If there is one immediate measure that A-REIT management can pursue to garner investor support it is to bolster ESG credentials. Institutional investors are placing far greater emphasis on this area which is beginning to have a greater influence on how they will direct investment mandates.

In relation to the Environment, the REIT sector is in a strong position to benefit from this issue and I would commend many in the sector for the efforts and achievements thus far. The REIT sector has the scale and resources necessary to lead this movement and I believe investors will ultimately be rewarded. However, as a point of interest, could someone explain to me why on our property inspections solar power facilities are more prominent on UK and European buildings compared with Australian developments?

In relation to Governance we continue to encourage managers to eradicate conflicts. Fiduciary duty means that it is near impossible to serve more than one master successfully. As soon as you introduce conflict, that duty is seriously jeopardised. Those people that have best explained how they manage conflicts, particularly in closed end vehicles, are now retired and living a fine life indeed whilst the investors continue to battle.

In conclusion, whilst it is important to recognise that the only constant is change, it is fair to say that the game for A-REITs has changed dramatically.



Whilst not all vehicles should be tarred with the same brush, the A-REIT sector has lost a dedicated place in institutional investment portfolios and must now compete directly against powerful alternatives in the real estate space, namely unlisted real estate and global REITs.

A-REITs management teams must produce strategies that have an investment case that is compelling globally. Such a strategy should be designed to weather the inevitable storms that impact markets from time to time, not forcing management to radically alter its portfolio or capital structure when there is a wind change in markets or investor profiles.

Resolution Capital continues to advocate that a portfolio of select global REITs will provide the most effective means of delivering diversification within most superannuation portfolios. A reliance upon the relatively small quality opportunity set of A-REITs and an Australian economy based on a highly cyclical low value add resources sector is a far from ideal.

The noise created by short term volatility distracts attention from the fact that the leading global REITs, which include select A-REITs, produce superior long term total returns with the added benefit of liquidity.

The hard part is execution, to avoid distractions and stay true to your investment objectives for the ultimate benefit of long term investors.

Andrew Parsons
Resolution Capital



Appendix 2

Resolution Capital Team
Property Tour 04/02/2010

