Lessons within Financial Distress: Public or Private?

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Real estate investment characteristics

- Long duration asset – typical hold period 5 to 10 years
- Income earning power tied to local market dynamics, depreciation and replacement costs
- Valuation and pricing tied to global capital markets
- Unlevered returns of leased buildings: between Bonds and Equities.
- Deep debt markets
- Asset class status acknowledged by most asset allocation studies.

### Significant asset class
- Size of market
- Diverse owner base
- Institutional and Retail depth

### Active management
- Asset selection and asset management are both sources of “alpha”
- Vintage Year matters
- Derivatives markets are not mature

### Unique risk-return characteristics
- Hybrid of a bond (contractual income)…
- … And a Stock (non-contractual residual)
- Returns exhibit low correlations with other asset classes

### Risks
- Direct investing: High levels of specific risk & transaction costs
- Listed Real Estate: Track broader stock market over the short run.
Real Estate – A Significant Asset Class

- Investable real estate universe is estimated at $6.9 trillion

Source: Bloomberg, EPRA/NAREIT, LaSalle Investment Management Research As of 3Q 2011
Global Real Estate Universes by Region 2012

Listed Real Estate
Total = $2.4 trillion

- Asia Pacific: 43.2%
- Europe: 16.7%
- Americas: 37.0%
- Middle East and Africa: 3.1%

Institutional Real Estate
Total = $6.9 trillion

- Asia Pacific: 30.5%
- Europe: 31.8%
- Americas: 34.2%
- Middle East & North Africa: 3.5%

Source: Investment Property Databank, LaSalle Investment Management
As of 3Q 2011
Note: The Listed Real Estate Universe includes all publicly listed property companies, primarily REITs and REOCs. Diversified development companies are included in emerging markets, but homebuilders are excluded. The Institutional Real Estate Universe includes all institutional investor-owned property, public and private.
European Real Estate Universes by Country 2012

Listed Real Estate Total = $0.4 trillion

- UK: 25%
- France: 27%
- Germany: 9%
- Spain: 4%
- Sweden: 5%
- Switzerland: 5%
- Italy: 3%
- Other W. Europe: 14%
- Turkey: 0%
- CEE: 2%
- Other W. Europe: 14%

Institutional Real Estate Total = $2.2 trillion

- UK: 17%
- France: 13%
- Germany: 17%
- Italy: 5%
- Spain: 2%
- Sweden: 6%
- Switzerland: 8%
- Netherlands: 7%
- Other W. Europe: 14%
- Turkey: 3%
- CEE: 8%
- Other W. Europe: 8%

Source: Investment Property Databank, LaSalle Investment Management As of 3Q 2011
Note: The Listed Real Estate Universe includes all publicly listed property companies, primarily REITs and REOCs. Diversified development companies are included in emerging markets, but homebuilders are excluded. The Institutional Real Estate Universe includes all institutional investor-owned property, public and private.
Two Tales of A Financial Crisis

Private Markets

Public Markets

IPD UK Monthly Capital Value Index: 1986 = 100

EPRA/NAREIT Developed Europe Price Index

Sources: IPD, EPRA/NAREIT
2011 RE Transaction Volume Up Across All Regions

$750 Billion Traded in 2011, with Americas Showing the Most Growth

Source: Real Capital Analytics, includes land sales, which comprise about 75% of transactions in Asia-Pacific but less than 10% in Europe and the Americas
Latest data as of 29 February 2012
YTD Capital Raising Picks Up
Nearly As Much Raised YTD as in all of 4Q 2011

Capital Raised by Region

Global Capital Raised by Type

Source: SNL Financial. Data includes public and private REITs and non-REIT real estate operating companies.

As of 24 February 2012
Private RE in Europe: 4 stories of a ‘different’ crisis

Source: IPD
RE Characteristics and Valuation, Liquidity & Volatility

- Low correlation of RE with other asset classes is based on private market data
- Private market returns are smoothed by appraisals (though extent varies)
- Trade-off between liquidity and price volatility:
  - obvious in public markets
  - also in private markets, cf. Germany & UK
- Debt always increases volatility……...
  - Optimum level up to 40% LTV?
- .... and affects correlations
  - Returns from higher risk strategies more highly correlated with stocks than private unlevered RE
Option One: Direct Property Ownership

Products

- Domestic
- Collection of national portfolios
- Regional portfolios
- Global portfolio

Positives

- Maximum diversification benefits
- Maximize control
- Flexibility on leverage levels including none
- National & regional benchmarks

Negatives

- Scale, specific risk / portfolio size
- Low liquidity
- Management
- Administration
- Tax and legal
Option Two: Unlisted/Private Indirect Property Funds

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<thead>
<tr>
<th>Global Funds</th>
<th>Targeted Funds</th>
<th>JVs/Clubs</th>
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<tbody>
<tr>
<td>Investment banks</td>
<td>Specialist managers/investment banks</td>
<td>Specialist managers</td>
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<tr>
<td>Opportunistic</td>
<td>Open or closed end</td>
<td>Usually closed end</td>
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<tr>
<td>No control over regional</td>
<td>Sector/country/regions</td>
<td>Varying risk profiles</td>
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<td>weights</td>
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<td></td>
<td>Availability</td>
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**Positives**
- Diversification retained
- Utilize expert management
- Range of styles and higher returns
- Defined strategies
- Improving benchmarks

**Negatives**
- Low liquidity and control
- Availability?
- Administration of draw downs
- Management of employing capital

**Fund of funds or individual investments**
Option Three: Listed/Public Property Company Securities

Real Estate Investment Trusts (REITs)
- Property owning vehicle
- Distributes 80% to 100% of taxable income
- Limited ability to generate reserves for investment
- Country opportunities
  - Americas: US, Canada, Brazil, Mexico
  - Europe: Belgium, Netherlands, France, UK, Germany, Greece, Bulgaria, Finland, Spain, Italy, Lux., Lithuania
  - Australasia: Australia, Singapore, Japan, Hong Kong, Philippines, South Korea, New Zealand, Malaysia, Taiwan, India, and Pakistan
  - Other: Dubai, Turkey, Israel, and South Africa

Conventional Listed Real Estate Operating Companies (REOCs)
- Lower income/dividend yield
- Higher correlation with general equities
- Often development focus. Real estate may be one of several businesses.

Positives
- Established benchmarks
- Liquidity and transparency
- Utilize expert management
- Investment period: immediate

Negatives
- Volatility - influence of general equity markets
- Relatively immature market in some countries
Real estate securities – REITs are a global market

- The tax transparent Real Estate Investment Trust (REITs) vehicle exists in many countries
- Much of the highest quality commercial property in Australia, USA and Europe is owned by REITs
- The requirement to distribute about 90% of earnings encourages a high dividend yield; returns are more direct property like than equities
- Public market liquidity gives ready exposure and management of allocation
- Regional and global benchmarks, e.g. EPRA/NAREIT, UBS & GPR
- $100 bn in global REIT portfolios through specialist managers
Dealing with the Debt Overhang – Threat & Opportunity

European commercial real estate debt maturity profile

Over €350bn of Debt Maturing in 2012 & 13

Source: De Montfort University, CBRE (Q4 2010)
Sources of Capital in the ‘Teens’ for Real Estate

Expanding

Private Markets
- Sovereign wealth funds

Public markets
- Global managers
- DC pension plans
- Private savers

Contracting

Private markets
- Insurance companies
- DB pension plans (as they mature)

Public Markets
- Discontent with volatility of stocks
The benefit of investing between big cycles

Total Real Return %

-20%
-10%
0%
10%
20%

71 72 73 74 75 76 77 78 79 80 81 82 83 84 85 86 87 88 89 90 91 92 93 94 95 96 97 98 99 00 01 02 03 04 05 06 07 08 '09 10 11

USA Long-run real average 5.4% pa

UK Long-run real average 4.2% pa

Source: IPD, NCREIF, LaSalle Investment Management

1977-1988 8.0%
1978-1988 7.6%
1979-1988 6.8%
1980-1988 6.4%
1981-1988 7.1%
1988-1993 8.6%
1993-1994 8.3%
1994-2006 9.3%
1995-2006 9.4%
1996-2007 10.2%
1997-2007 9.7%
1998-2007 7.9%
1999-2008 7.7%
2000-2008 7.3%
2001-2007 9.5%
2002-2007 8.8%
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2005-2007 8.6%
2006-2007 8.7%
2007-2008 9.4%
2008-2009 8.0%
2009-2010 6.0%
2010-2011 6.7%
2011-2012 7.3%

Source: IPD, NCREIF, LaSalle Investment Management

1994-2006 9.3%
1993-2006 9.9%
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1998-2007 7.9%
1999-2008 7.7%
2000-2008 7.3%
2001-2007 9.5%
2002-2007 8.8%
2003-2007 7.6%
2004-2007 8.3%
2005-2007 8.6%
2006-2007 8.7%
2007-2008 9.4%
2008-2009 8.0%
2009-2010 6.0%
2010-2011 6.7%
2011-2012 7.3%

Source: IPD, NCREIF, LaSalle Investment Management
RE is part of the volatile global capital markets
  - Greed & Fear rule
- Debt availability: the most important influence on RE equity pricing
- Disciplined investors adhere to:
  - Required Return
  - Cost of Capital
  - Mean Reversion concepts
- Public markets tend to lead in pricing; private markets tend to lag
- The value of communicative, reliable partners become most evident in a down-market
- Real estate remains a cyclical business
- Buying after a steep price correction is almost always a winning strategy