

Real estate in Europe: Back to *Basics* !



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Back to *Basics*

- Erosion in economic fundamentals (at this point)
- Erosion in total property returns
 - Cash returns are now key
 - Appreciation (capital) returns often negative
 - Gross initial yields (capitalization rates) still expanding, although at a slower pace

Back to *Basics*

- Tight debt market
 - Reduced access to debt finance
 - But the situation is improving
 - More opportunities for equity investors

Back to *Basics*

- “Wait and See” attitude
 - With emerging bid-ask spread
 - Lives of property funds are extended

Back to *Basics*

- This marks a clear change after a decade of double-digit returns
- Property investments will be based:
 - More on a thorough investigation of the individual property characteristics
 - Less on past market characteristics and pricing

Are we not too pessimistic ?

- As evidenced by the listed markets? “Irrational exuberance”?
- Assets priced far below net asset values
 - 34% on average world-wide, 27% for Continental Europe, 40% for the UK
 - Anticipating lower intrinsic value ?

Are we not too pessimistic ?

–Irrational exuberance ?

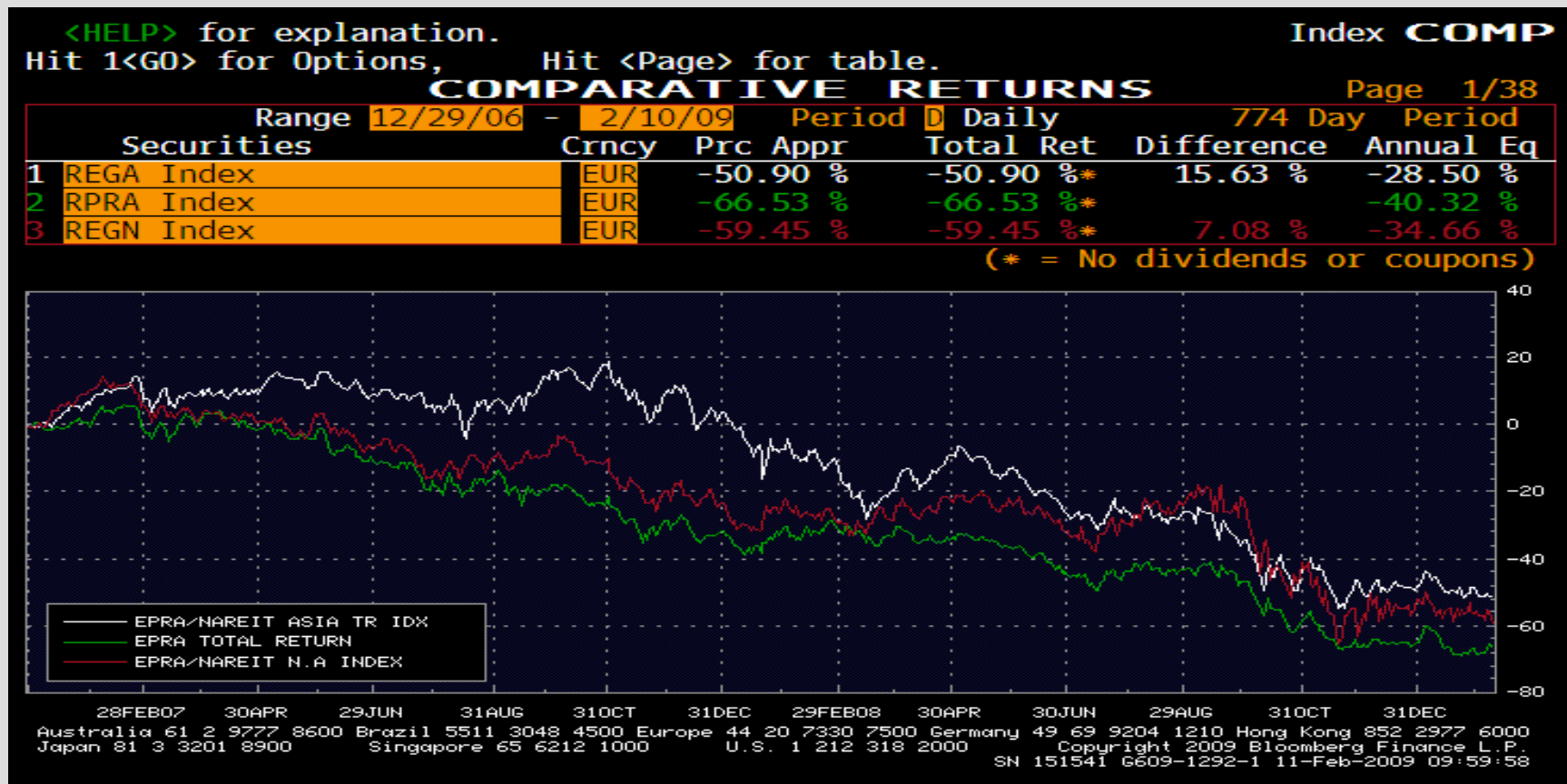
–Dividend yields far above 10 yr government bond yields

- A dividend yield of 6% on average vs. government yields below 4%
- Risk premiums asked for by investors are probably adequate now

Are we not too pessimistic ?

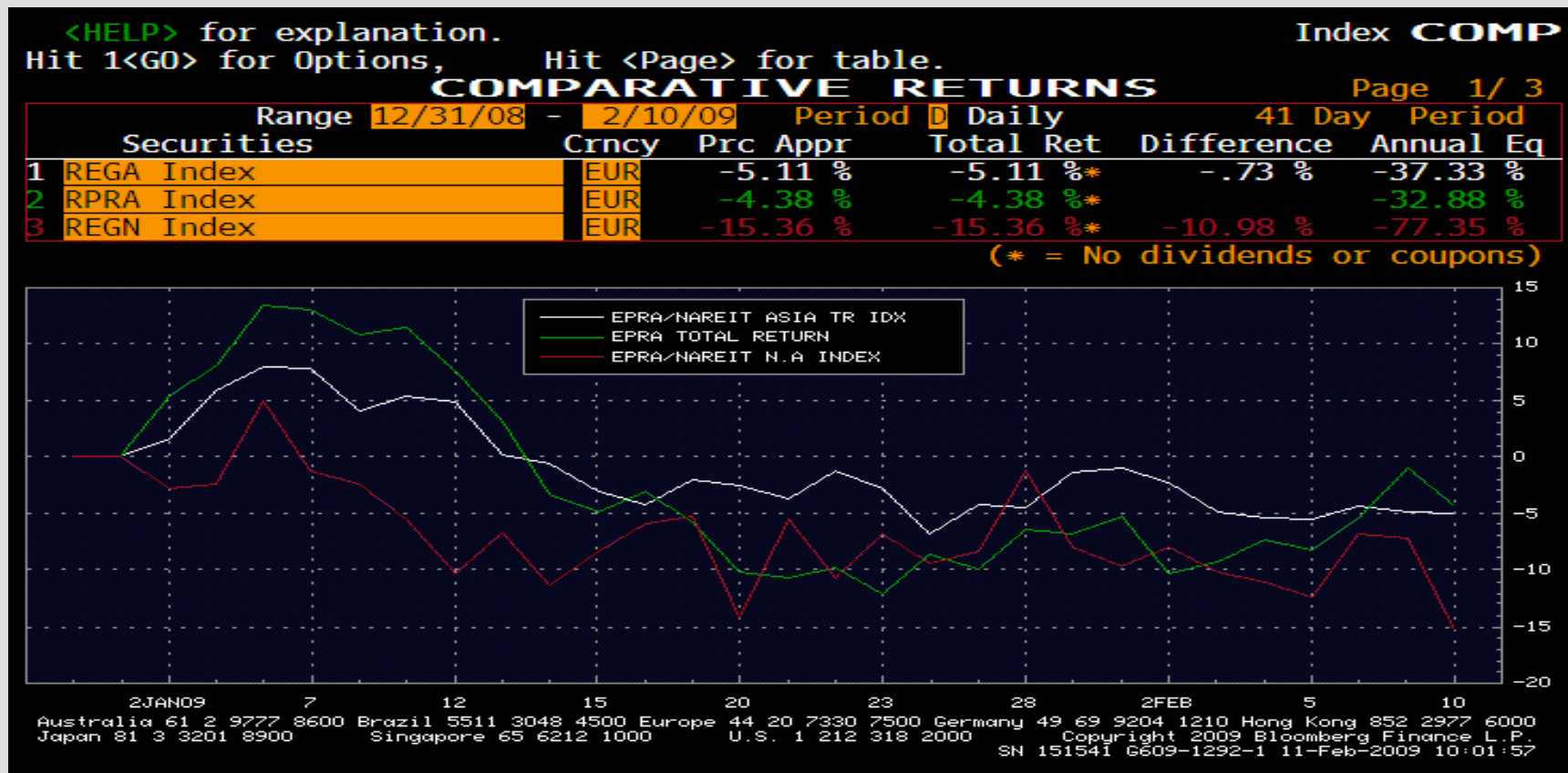
- Real estate anticipates (partly) inflationary pressures
 - In contrast to cash like instruments

Are we not too pessimistic ? (REITs 01/01/07-10/02/09)



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Are we not too pessimistic ? (REITs year-to-date)



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Real estate and inflation

- Real estate offers a *partial* protection against inflation
 - Depending on lease characteristics, regulation,...
 - Depending on the interlease risk

Real estate and inflation

- But the partial inflation hedging quality of real estate *equity* is magnified by the use of fixed rate debt

So, How is Europe ?



	02 February 2009	short-term < 1 year	Assessment
Macro-economic data			
Real GDP growth (%)	1.1	-1.2	-
Inflation (%)	3.3	1.1	0
EUR/USD	1.26	1.38-1.43	0
10-year government bond yields (%)	3.05	2.75-3.25	0/+
Money market rates	2.08	1.50-2.00	0/+
Long-term real interest rates (10-year, %)	2.11	1.90	+
Short-term real interest rates (3-month, %)	0.48	0.65	+
Property data			
Gross initial prime yields (GIYs) (%)	5%-8%	5.5%-8.5%	-
Spread GIYs/borrowing costs	Widening	Widening	+
Value growth	Declining	Stable or slightly declining	0/-
Rental growth	Marginal (if any)	Marginal (if any)	0/-
Occupier demand	Eroding	Eroding	0/-
Supply	No-industry-wide overbuilding	Supply limited	+
Other features			
Sub prime crisis	Direct impact	Direct impact	-
Availability investment money	More selective	More selective	0
Overall assessment			Slightly negative
Source: MEA Dubai 16-18 February 2009 Source: Fortis Private Real Estate. Macro-economic data: Prognosis by Fortis Private Banking February 2009 + : positive stance / 0 : neutral stance / - : negative stance			

Diversification away from domestic markets ?

- Theoretical case for investing outside the home markets
 - Economic cycles do not move in a similar way
 - Property markets do not move in a synchronised way

- Offering diversification benefits in terms of risk and return

Diversification away from domestic markets ?

- But is globalisation (of capital markets) not ignoring local characteristics ?
- Tempering return-enhancing and risk-reducing international investment opportunities?

Unique opportunities ?

- Bricks in the Euro zone, generating cash
 - Property/asset management strategy
 - Portfolio value creation

- Acquisitions from “distressed” sellers?
 - Property portfolios facing pressure from banks (near or at breach of loan-to-value covenants)

Thank you !

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