

# Property research paper

## Global REITs: key features and recent trends

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### Executive summary

- *REITs have exhibited a period of strong growth.* Over the last decade REITs have been growing rapidly due to: i) the emergence of securitised real estate markets; ii) increasing capital flows into alternative investments, particularly in property; iii) and favourable space market fundamentals.
- *REITs are distinctly different from listed equities.* REITs differ from listed equities both in terms of investment characteristics and structure. REITs offer a relatively high and stable income yield and (until recently) relatively lower volatility. Also, through their status of non-taxable flow-through entities, REITs avoid the double-taxation problem linked to distribution of dividends for corporations.
- *Favourable investment performance against competing asset classes.* Over the long-term, REITs have outperformed both listed general equities and fixed interest asset classes in terms of absolute return performance and risk-adjusted returns. In comparison to fixed interest, REITs have delivered a solid yield supported by a favourable capital return. However, the unfavourable performance of REITs over the short-term is considered to be cyclical in nature as it is largely associated with the recent credit crisis.
- *REITs offer a high level of liquidity for real estate investment.* REITs became very attractive in the 1990's, offering greater liquidity as opposed to the illiquid nature of direct investment.
- *REITs offer the potential for diversification benefits.* REITs provide diversification due to the heterogeneous nature of property assets in terms of sector, asset grade and geographical location. This offers investors a wide range of product diversity across the risk-reward space. Also, REITs were found to generally have low correlation with both bonds and shares. However, with the recent market downturn, correlations with these asset classes have tended to rise.

- *REITs are considered to enhance portfolio investment performance.* REITs were found to enhance global investment portfolios, comprising of shares and fixed interest, via improved risk-adjusted returns. This tended to rise with increase allocation to REITs. Furthermore, a global REIT portfolio was found to deliver better investment performance than investing in a single geographical REIT market.
- *The short-term outlook for REITs. Return performance for REITs is likely to soften.* Underlying property earnings growth is likely to slow, underpinned by weakening space market conditions. Furthermore price support for REITs is expected to be subdued with uncertainty plaguing equity and capital markets with the unfolding of the credit crisis. With the end of cap-rate compression, the emphasis on delivering performance will be on active (asset) management.
- *Risks associated with investing in REITs.* While REITs offer many favourable attributes, they also carry many risks. Firstly, against direct property, REITs exhibit greater return volatility over the short-term. Secondly, the level of gearing in many REIT markets has tended to expose them to greater market volatility. This has recently been reflected in a rise in risk-premia for such REITs. Hence, exposure to REITs with lower gearing levels is considered to be relatively attractive. Another risk relates to the state of space markets, which are likely to experience further deterioration if the global economy slows significantly.

## 1. Introduction

Recently, many listed stock markets have experienced significant downturns spurred on by the credit crisis. Accordingly, the Real Estate Investment Trust (or REIT) sector globally has also experienced a similar downturn. To many investors the synchronised downturn in REITs along with general listed equities has surfaced questions surrounding the defensive nature of REITs, and consequently, the problematic nature of diversification benefits in light of high correlations in price returns between the two asset classes. An important aspect of this debate relates to the distinction between cyclical versus structural characteristics exhibited by these asset classes. While asset classes may exhibit distinct characteristics in terms of key investment parameters, such as return and risk, they tend to often show disparities in these parameters with cyclical departures from long-term trend behaviour.

This report aims to add clarity to this debate by outlining the investment value proposition of REITs in terms of fundamental characteristics and investment features. Moreover, it reviews these characteristics in the context of the recent cyclical downturn in return performance.

This report is organised as follows. Section 2 provides an overview of the global REIT market in terms of size, market composition, and growth profile. Section 3 reviews investment performance in terms of absolute and risk-adjusted returns. In this section attention is also given to the relationship between returns and interest rates. Section 4 considers the case for diversification by gauging return correlations between REITs and other asset classes. Section 5 discusses key product attributes; specifically income yield and product offering. Section 6 discusses the investment structure of REITs, focusing on the management model, gearing levels and tax. Section 7 examines the value of REITs in a balanced portfolio.

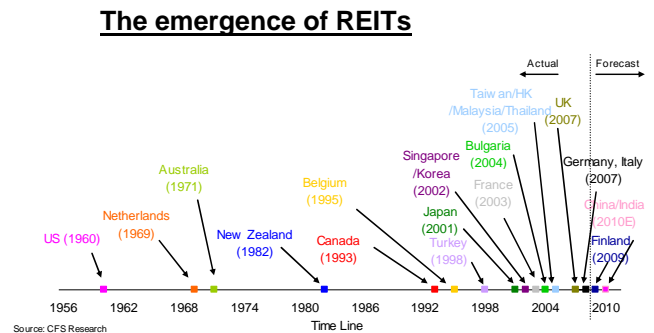
## 2. Global proliferation of REITs

### Global emergence of REITs

Public REITs offer investors exposure to property investment via a listed public exchange. While not new, REITs became very attractive in the 1990's, offering liquidity as opposed to the illiquid nature of direct investment.

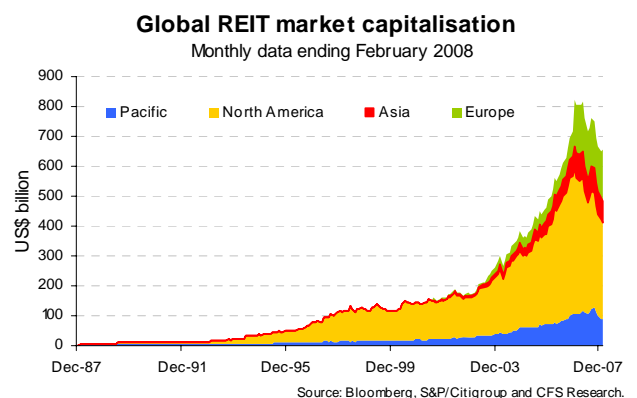
The proliferation of the REIT structure globally, as noted in Figure 1A, represents a structural change in terms of global investment in real estate. Since the Asian crisis there was a rapid development of REIT markets across Asia and, in more recent years, across Europe with the introduction of UK and German REITs.

Figure: 1A



Currently, there are 436 REITs with a combined market cap of around US\$661.0 billion. The rapid emergence of REITs has been matched by their growth in market capitalisation (cap). Figure 1B clearly highlights the exceptional growth in the market cap for REITs over the last ten years ending February 2008. Notably, after reaching a peak in 2007, the decline in market cap in recent times reflects the downward valuation in REIT markets in conjunction with the credit crunch and a delisting of REITs (largely reflecting M&A and regulatory considerations in the US).

Figure: 1B



The composition of the global REIT market, in terms of market cap and number of trusts, is highlighted in Figures 2A and 2B respectively. Focusing on market cap, North America is the largest REIT market with a share of 49%, (which is dominated by the US with a share of 45%). Europe has a share of 26% with the main countries being France (with a global share of 13%) and UK (with a share of 8%). The Asian region has a share of 12% (comprised mainly of Japan and Singapore) while Australia has a share of 13%. The share and ranking of REIT markets by country is also similar when based on the number of REITs.

Figure: 2A

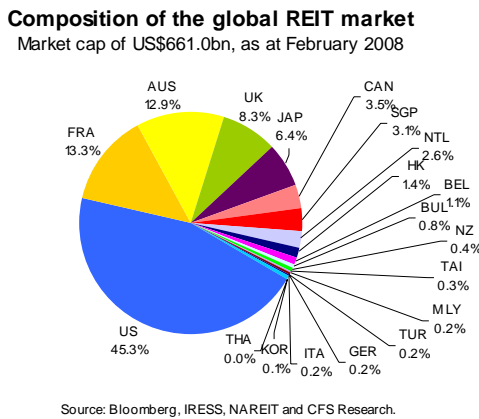
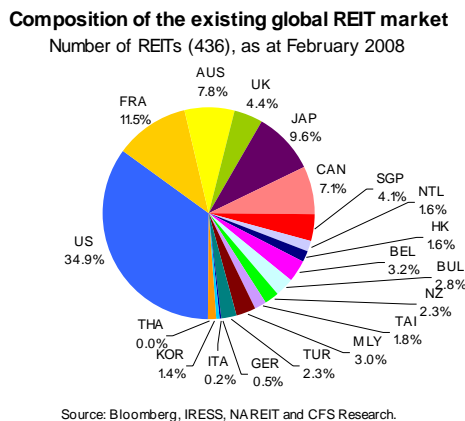


Figure: 2B



In gauging the size of the global REIT sector, Table 1 reports the size of individual REIT markets by country against the size of the economy and stock markets. Overall, investments in REITs represent about 2% of the global economy and about 1.7% of the listed equity market. While these percentages vary across country, REITs are particularly

significant in Bulgaria, Australia, New Zealand and Singapore with shares above 5%.

Table: 1

Global Market Size as at February 2008							
Country	Size of Economy (GDP) \$US bn	Stock Market (Market Cap) \$US bn	REIT Market (Market Cap) \$US bn	Share of REITs to Economy	Share of REITs to Stock Market	Number of REITs	Average Market Cap(\$US bn)
US	\$14,195	\$14,449	\$299	2.11%	2.07%	152	1.97
Netherlands	\$863	\$702	\$17	1.97%	2.42%	7	2.42
Australia	\$1,047	\$1,129	\$85	8.16%	7.57%	34	2.51
New Zealand	\$146	\$40	\$3	1.75%	6.31%	10	0.26
Canada	\$1,571	\$1,636	\$23	1.46%	1.40%	31	0.74
Belgium	\$507	\$344	\$7	1.41%	2.08%	14	0.51
Turkey	\$748	\$197	\$2	0.21%	0.80%	10	0.16
Japan	\$4,867	\$4,124	\$42	0.86%	1.02%	42	1.00
Korea	\$999	\$782	\$1	0.06%	0.08%	6	0.10
Singapore	\$185	\$382	\$20	10.98%	5.32%	18	1.13
France	\$2,843	\$2,297	\$88	3.09%	3.82%	50	1.76
Taiwan	\$409	\$508	\$2	0.46%	0.37%	8	0.24
Hong Kong	\$222	\$1,504	\$9	4.05%	0.60%	7	1.28
Malaysia	\$208	\$253	\$2	0.78%	0.64%	13	0.12
Germany	\$3,653	\$2,739	\$1	0.03%	0.04%	2	0.55
United Kingdom	\$2,833	\$6,804	\$55	1.93%	0.80%	19	2.88
Bulgaria	\$49	\$17	\$5	10.27%	29.30%	12	0.42
Italy	\$2,330	\$979	\$1	0.05%	0.11%	1	1.06
<b>Total</b>	<b>\$37,676</b>	<b>\$38,886</b>	<b>\$661</b>	<b>1.75%</b>	<b>1.70%</b>	<b>436</b>	<b>1.06</b>

Source: Bloomberg, Datastream, IMF, IRESS, NAREIT and CFS Research.

A summary of existing REIT markets and their key characteristics is provided in Table A1 of the Appendix.

**Growth prospects**

The global real estate investment landscape is changing fast as more countries adopt legislation for the REIT structure and foreign property companies establish their presence in other jurisdictions.

**Asian region**

There are five countries in Asia where the REIT structure is either in legislation planning or in a REIT development phase. These are China, India, Pakistan, Indonesia and the Philippines. It is believed that once China and India introduce their REIT systems (by 2010) these markets will dominate the region.

The markets of Japan and Singapore should continue to attract future capital, yet an increased capital allocation is expected in emerging markets. The Japanese REIT market is the largest in Asia. Currently the Japanese government is considering lifting restrictions for J-REITs so that they can invest in overseas real estate. This will increase regional activity and underpin the Japanese investors' external growth. In contrast, Singapore is considered to be a favourable cross-border REIT centre due to its regulations, business policy and tax measures.

Hong Kong REITs began in 2005, but had a sluggish start due to government barriers which banned offshore real estate investments. While the removal of this obstacle has assisted the market, it is disadvantaged by the REIT's partially tax transparent system. The market could benefit if it establishes itself as a potential cross-border platform.

## European region

The development across Europe has been much slower than Asia, reflecting a lack of ideal and common investment structures (in a region with independent legal and fiscal frameworks across countries) as well as unfavourable market dynamics.

UK REITs were introduced on 1st January 2007. Within the European region, the UK REIT market has an estimated share of 31.4%. After U.K. REIT legislation was introduced, many property companies converted into REITs. Since January 2007 prices for UK REITs have generally moved down. This is due to a variety of factors, including: the dilution of net asset values with the conversion charge; rises in interest rates and concerns about higher bond rates; uncertainty surrounding the short-term outlook for the macroeconomy and turnaround in real estate markets; and investors taking capital out of the sector. Furthermore, the credit crunch caused a drying up of liquidity in the direct property markets, exacerbating the fall in asset values with the selling of property assets in the unlisted fund space.

In Germany, legislation was passed on 23rd March 2007 for a REIT regime, with retrospective effect to 1st January 2007. At present only 2 REITs have been established in the market, however, research from UBS has estimated the German REIT market could be worth €127 billion (in asset value) by 2010.

Italian REITs are following the French model (referred to as SIIQ) with REIT legislation introduced in mid-2007. Currently, only Immobiliare Grande Distribuzione is trading as a REIT with a market cap of US\$1.06bn as at February 2008. To date only a few property companies have shown interest to convert to a REIT status. IMMIT Immobili Italiani, the

€1.3bn property division of Bank Intesa Sanpaolo, postponed its plans to list as a REIT in May 2008. Aedes Immobiliare plans to launch a €1.2bn REIT by the end of 2008. Over the short-term we expect an increased activity in this sector with conversions of existing public and private property companies or establishment of new REITs through Initial Public Offerings.

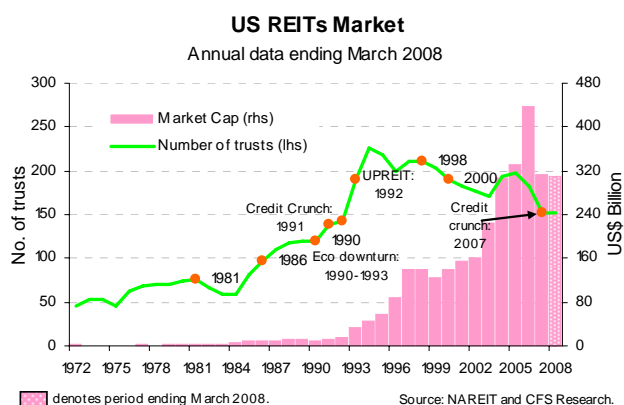
## North America

North America has experienced a considerable decline in REIT numbers, on the back of private equity deals in both the US and Canada.

As noted in Figure 3A, the number of REITs listed in the US has fallen in 2007, mainly as a result of two trends: i) strong privatisation activity from private equity players; and ii) the effect of the Sarbanes-Oxley legislation in the US, making it less attractive for companies to list due to the increased burden of compliance.

Similar to the US, Canadian REITs are currently going through the privatization and consolidation stage, despite interest from large Canadian pension funds and overseas institutional buyers in recent years.

Figure: 3A

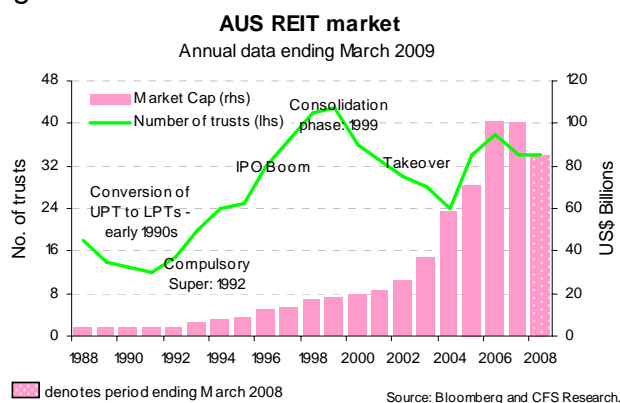


## Australasia

The Australian REIT market is one of the most sophisticated and mature listed real estate investment markets in the world. Over the last two decades the Australian REIT sector has experienced exceptional growth with market cap growing by an average rate of 20% per

annum. This growth profile is shown in Figure 3B.

Figure: 3B



The strong growth can be attributed to a variety of factors which include: the growth in superannuation investment (via the government compulsory pension scheme) into property, the growing popularity of annuity style investment funds, strong capital raisings as a result of a sector shift and rotation of investment funds from general equities, the access to liquidity relative to direct property offerings, and the transfer of property from corporate balance sheets.

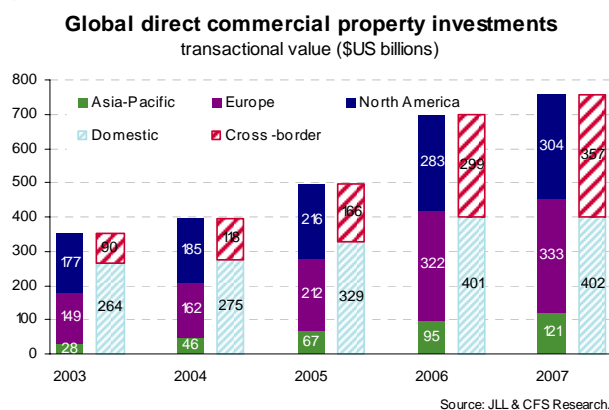
As at February 2008, the number of REITs within the ASX 200 Index stood at 34 with a combined market capitalization of US\$85.5bn. It is worth noting that the sector's market capitalization declined by around 30% with the unfolding of the credit crisis.

The NZ REIT market is relatively small by world standards. As at the end of February 2008, the market capitalisation was approximately US\$2.4bn across 10 trusts.

### Real estate investment transactions

Globally, the proliferation of REIT markets has driven a significant increase in the amount of cross-border investments. Figure 4 highlights this feature by showing the increasing value of commercial real estate transactions since 2003 split by region and by type. In 2007, these regions accounted for a total of US\$121bn, US\$304bn and US\$333bn, respectively.

Figure: 4



A large proportion of the European transactions arise from the UK, followed by Germany and France which altogether accounted for 63% of total volumes in 2007. United States accounts for 93% of transaction volumes in North America. In the recent past, the Asian region has received significant interest from the international investors which were chasing higher returns. The main impetus for an increase in investments is seen in the increase of intra-regional trade. The majority of the Asian transactions arise from Japan (50%), Australia (15%), and Hong Kong, China and Singapore with 7%.

Impact from the global crisis has been felt in the region by the reduction in the volumes of transactions in the second half of 2007. However, the strong 1H2007 has counterbalanced this poor performance. Over the year France and Germany have experienced increased volumes by 34% and 15% respectively. In contrast, real estate agent Savills reports that the UK market experienced a 58% decline in transaction volume in Q42007 to US\$14.8bn.

In the current investment environment many investors are holding off from allocating capital to the property sector as they reassess their investment strategies. At the same time there are many pro-active players, seizing on global opportunistic investments which include: Sovereign wealth funds (SWF), German open-ended funds, North American institutions, Middle East investors and Australian investors. SWF have included: Singapore Government Investment Corp. (SGIC), Qatar Investment Authority, the Abu Dhabi Investment Authority, Temasec (Singapore) and China Investment Corp.

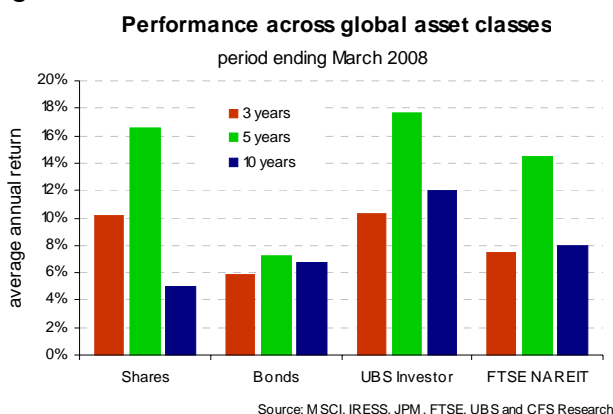
### 3. REIT investment performance

This section discusses the performance of REITs. Specifically, it examines global REIT performance against global shares and bonds, briefly discusses the relative performance of REITs against listed shares for selected country markets, examines the movement between REIT returns and interest rates, and finally considers performance in terms of risk-adjusted returns.

#### Return performance: a global perspective

Figure 5A shows the return performance of global REITs to global listed shares and fixed interest (or bonds). Global shares are proxied by the MSCI World index, a commonly used benchmark for global shares comprising of 23 countries. Global REITs are proxied by the FTSE EPRA/NAREIT Global Real Estate (FTSE) Index and the UBS Global Real Estate (UBS) Investor Index. Both indices track the performance of listed real estate companies and REITs globally. The UBS series can be considered to be a subset of the FTSE series as it excludes real estate development companies - which tend to be more volatile. The J.P. Morgan Global Index is a well known benchmark for global bonds. All indices are expressed in US dollars.

Figure: 5A

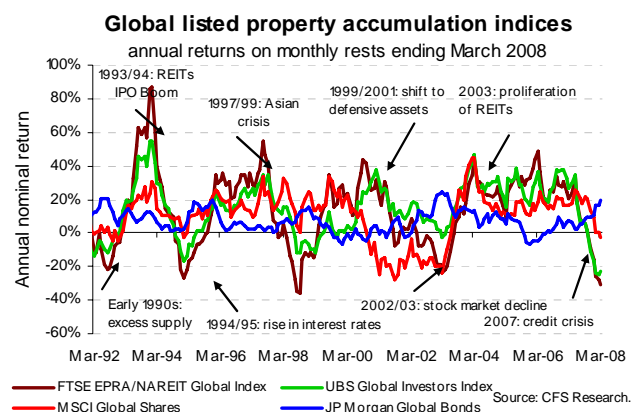


Notably, return performance over recent years has been substantially lower than over the medium term (5 years), reflecting the severe downturn associated with the recent credit crisis. This is particularly highlighted for REITs where the sluggish short-term performance is below their long-term (ten year) average. This suggests that the recent poor returns by

REITs reflect an over reaction against longer term performance. It is also worth noting that over the longer time frame REITs have outperformed both shares and bonds.

Figure 5B highlights the historical profile of asset returns since the early 1990's. Over this period REIT performance was influenced by a combination of changing space market fundamentals, movements in interest rates and equity markets. With the passing of the Asian crisis in 1997, there was a greater emphasis on securitising real estate, especially in Asia. With the aftermath of the tech wreck in early 2000, there was a growing interest by investors towards alternative investments (including direct property and REITs) in search of high yielding investment products and greater absolute return. In 2003, improving space market fundamentals (on the back of favourable macroeconomic conditions) delivered positive rental growth which further provided uplift in property returns. This uplift in return was further supported by aggressive use of leverage with the relatively low cost of debt. Overall, the combination of favourable space market and capital market conditions contributed to property's strong performance during this period.

Figure: 5B



#### Return performance: REITs versus listed shares

The following section takes a closer look at the return performance between REITs and listed shares across selected markets: namely the United States, Australia, Japan and Singapore. All these markets experienced a consistent sharp decline in price returns in line

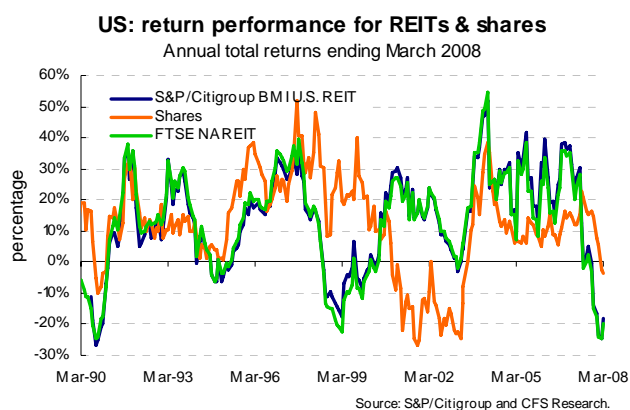
with the unfolding of the credit crisis over the last six months.

### United States

Figure 6A shows annual US-REIT total returns, (based on the FTSE NAREIT All REITs index and the S&P/Citigroup BMI REIT index), versus shares (based on the S&P500 share index).

US-REITs have experienced three major downturns since 1989. Between August 1989 and October 1990, REITs fell as much as 36% and 30% between March 1998 and November 1999. More recently, the decline in REIT prices by around 28% is in line with previous downturns. Currently, REITs are trading around a 20% discount to the value of the underlying assets.

Figure: 6A

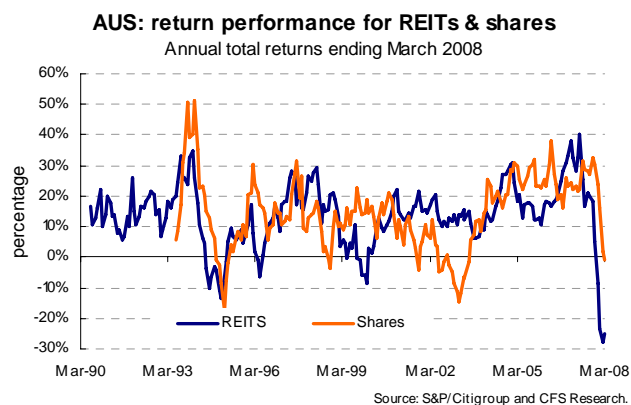


Furthermore, REITs have outperformed shares between 2000 and 2006. Since late 2006 both asset classes exhibited a sharp decline in their price returns, a reflection of the credit crisis. Importantly, shares outperformed REITs with REITs experiencing a much sharper decline. For instance, over the 12 months ending March 2008 REITs lost 17.9% of their value, compared to only 9.1% decline for shares. The erosion in relative performance of REITs is a combination of an upward re-rating of risk in the sector and a downgrade in earnings expectations with a cooling in the macroeconomy. It is worth noting that the debt re-pricing will be of ongoing concern for highly geared trusts.

### Australia

Figure 6B shows annual A-REIT total returns, (S&P/Citigroup BMI REIT index) versus shares (based on the S&P/ASX 200 equities index). A-REITs have outperformed shares during the past seven years. In the period from December 2000 to March 2008, A-REITs delivered an average annual total return of 16.0% while the S&P/ASX200 index delivered 14.5%. As with the US-REITs, A-REITs have experienced a major downturn since late 2007. The REIT index fell by 24.8% over the year to March 2008. The fall in index was triggered by the credit crisis, causing an upward repricing of risk to reflect highly leveraged and financially structured REITs.

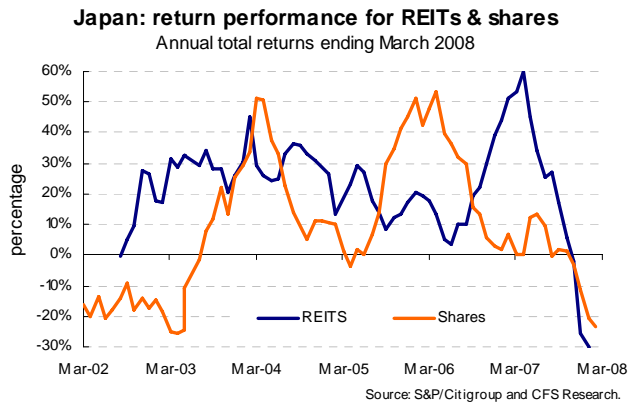
Figure: 6B



### Japan

Figure 6C shows annual J-REIT total returns, (S&P/Citigroup Japan REIT index) versus shares (based on the Topix Index) since 2002. From its inception in 2001, the J-REITs market has grown rapidly in market capitalisation and outperformed the Japanese share market in terms of return, delivering 22.8% versus 11.5% pa. Around November 2006, J-REIT share prices surged on the back of increased demand by international investors. The unfolding of the credit crisis has triggered a slide in J-REIT prices. Over the last 12 months ending March 2008, the REIT market fell by 39.4% with foreign funds selling J-REIT holdings to cover their losses in other investments.

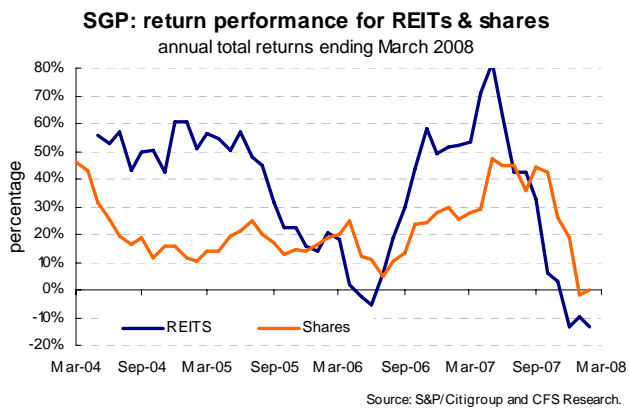
Figure: 6C



**Singapore**

Figure 6D shows annual S-REIT total returns, (S&P/Citigroup Singapore REIT index) versus shares (based on the Straits Time Index) since 2004. Over the period May 2007 to March 2008 the S-REIT posted a negative return of 19.3%. Currently, investors are focused on defensive style assets with the prospect of persistent share market volatility in the short-term.

Figure: 6D



Finally, all Figures from 6A to 6D, tell us the same story i.e., that the recent poor returns by REITs are cyclical, not structural, in their nature. Thus, those long-term oriented investors should consider investing in REITs market as they have outperformed other asset classes over the longer time frame. While REITs can be considered to be a 'good buy' with prices currently trading at a discount to net asset value (NAV), there is the potential for further falls in prices within the current uncertainty in investment markets.

**REITs versus interest rates**

Given that REITs are a relatively high yielding investment, movements in interest rates are considered to be a key driver of return performance. Rises in interest rates tend to correspond with periods of strong economic growth and rising inflation. While such periods tend to support rental income cash-flows, the higher inflation feeds through into longer-term bond maturities. Given that the bond rate is commonly used as a proxy for the risk-free rate, it forms part of the discount rate in DCF valuations. Consequently, increases in the bond rate tend to dampen asset prices.

Figures 7A, 7B and 7C depict movements in REIT annual returns against annual changes in the bond rate for the US, Australia and Japanese markets respectively. Note that the axis for the bond series is inverted. For all three markets there appears to be a relatively strong inverse correlation between the two series. It is worth noting that this relationship appears to weaken over the last few years. The divergence in the two series for the US and Australia over the last few years reflects the strong influence of M&A activity. Recently, the widening disconnect between the two series reflects the 'fall-out' associated with the credit crisis.

Figure: 7A

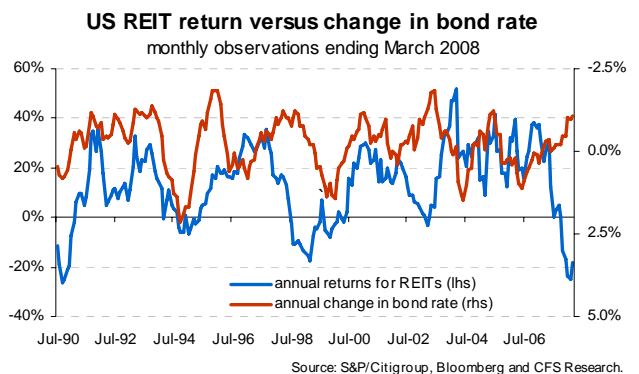


Figure: 7B

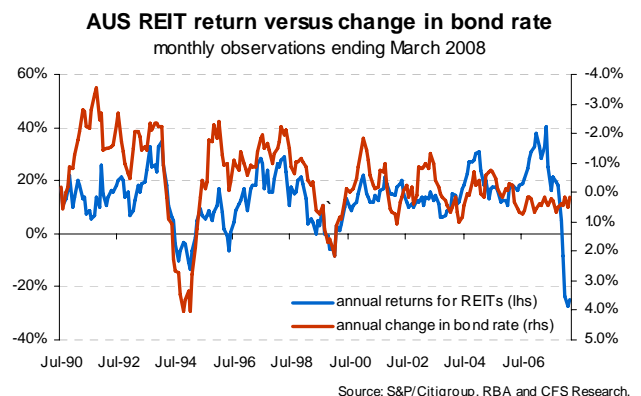
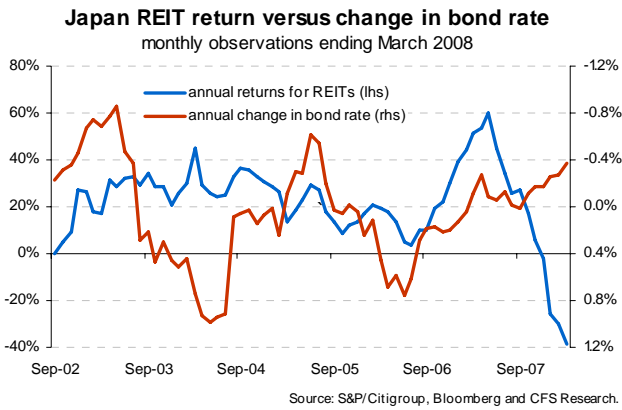


Figure: 7C



In summary, the charts highlight that historically there is a close inverse relationship between interest rates and REIT price returns. As such, gaining an insight into the future movement of interest rates would offer a basis for gauging the outlook on price growth.

The outlook on global interest rates is mixed, while rates have been moving down in the US and Europe, they have been climbing in Australia and NZ. Australia is likely to experience a peak in the interest rate cycle within 12 months and then start easing. Japan has kept the interest rate steady and may even lower rates, while China is on a path of raising rates.

**Risk-adjusted returns**

Apart from absolute total return another key investment performance is risk-adjusted returns. Figures 8A and 8B show estimated risk-adjusted return performance for REITs against competing asset classes. Note that global REITs are represented by both the UBS Investor index (referred to as core REITs) and FTSE EPRA/NAREIT index series.

Looking at Figure 8A, global REITs compare unfavourably to global shares over the last 3 and 5 years ending March 2008. However, they outperform shares over the longer 10 year period. It is interesting to note that a very different scenario arises when the sample period is rolled back to June 2007 as depicted in Figure 8B. In this instance, core global REITs outperform global shares and bonds over five and ten-year time horizons. While this is a reflection of the recent sharp declines in price returns, it also reflects a substantial rise in equity market volatility. This is partly

illustrated in Figure 8C which show that REIT return volatility for both the US and Australian markets has rapidly increased over the last twelve months relative to listed shares. This recent upsurge in volatility appears to represent an overshoot position from that experienced since 2000. As such, we expect volatility to subside going forward which implies an improvement in the risk-adjusted return profile of REITs.

Figure: 8A

**Risk-adjusted total returns**  
period ending March 2008

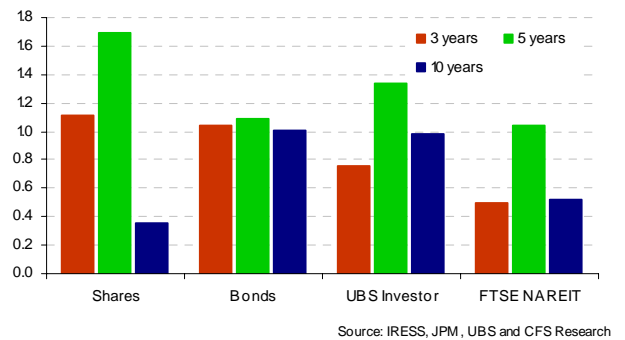


Figure: 8B

**Risk-adjusted total returns**  
period ending June 2007

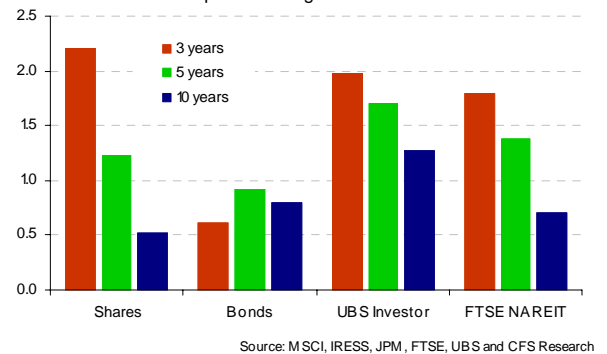
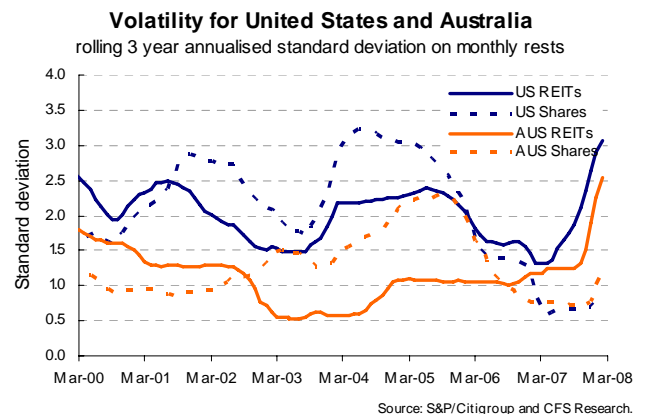


Figure: 8C



## Short-term outlook on return performance

In formulating a short-term view on the performance of REITs, consideration is given to earnings growth and capital market conditions.

In many of the mature markets, earnings growth and property asset prices have been relatively strong, underpinned by improving space market conditions and favourable capital markets. In contrast, the short-term outlook is likely to be less favourable due to: i) a sluggish macroeconomic environment mainly associated with the slowdown in the US and its ripple effect across the globe; ii) the uncertainty surrounding the future direction of equity markets, reflected in increased market volatility and an upward re-rating of risk; iii) the increased cost of finance, and iv) over-weight in capital allocation to property. With regards to property allocations, while current allocations are over-weight in this asset class from a tactical perspective, they are considered not to be over-weight from a strategic perspective if the current performance across asset classes is deemed to be temporary in nature.

All this is likely to see demand for space slow and vacancy rates rise. Also, as mentioned earlier, prices are likely to moderate with valuations factoring in higher discount rates. Indeed, we are already seeing investment yields soften on the back of these factors. Furthermore, with the end of cap-rate compression, the emphasis on delivering performance will switch to active (asset) management. Furthermore, the current environment offers opportunity for longer-term players (managers) to reposition their growth strategies.

While the easing of interest rates in the US and Europe should provide some support to prices, this is most likely to be offset by deteriorating economic conditions and tightening financial conditions.

## 4. Diversification benefits

This section explores the potential for diversification benefits via REITs. Diversification benefits can take the form of a

reduction in the portfolio risk, an increase in the risk-adjusted return or a hedge against potential losses. The first part discusses ways of obtaining diversification. The second part examines this more formally in the context of return correlations.

### Seeking diversification

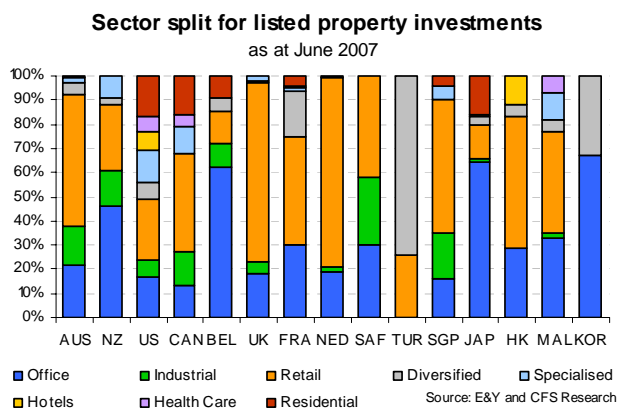
Property investment offers a diverse range of investment type, differentiated by asset sector and sub-sectors, asset grade or quality, asset geographical locations, tenancy types (such as tenancy lease structures and security of tenancy income), trust structures, tax regulations and market conditions. As such, investing in global REITs offers investors a level of diversity which is multi-dimensional.

As mentioned, two common ways is by either having exposure to different property sectors or by having exposure to markets which exhibit different property cycles. Both of these diversification drivers are discussed further below.

### Exposure to different property sectors

Figure 9 shows the sector diversity of listed property trusts across country markets. Clearly, sector exposure varies greatly across market. However, property exposure tends to be highly concentrated in the core property sectors of office and retail. Minor exposures are present for industrial and the residential sectors.

Figure: 9



According to Ernst & Young (E&Y), Asia is the second leading region with exposure to the global office market. Although, its office sector concentration has become increasingly diluted

with more REITs coming to market. In Europe, REITs have mainly concentrated on retail and office assets. The UK, Netherlands and France are oriented towards the retail sector. While US REITs also have a high concentration to retail, it also has the greatest sector diversity. The top three sectors include retail (25.6%), residential (17.1%) and office (16.3%).

**Exposure to markets with different property cycles**

Property markets are driven by macroeconomic factors, but also by local market factors and prevailing conditions. As such, property markets are likely to display different cycle patterns, both in terms of duration and amplitude. Indeed, such disparities in market cycles are likely to be more apparent in the absence of strong global common trends.

Figures 10A and 10B show property market cycles for Asian and European industrial markets for selected countries, respectively, while Figure 10C show all property markets cycles for Australia. Notably, markets are positioned in different phases of the property market cycle, both currently and in one year's time. This suggests that diversification benefits are possible by exploiting market cycles.

Figure: 10A

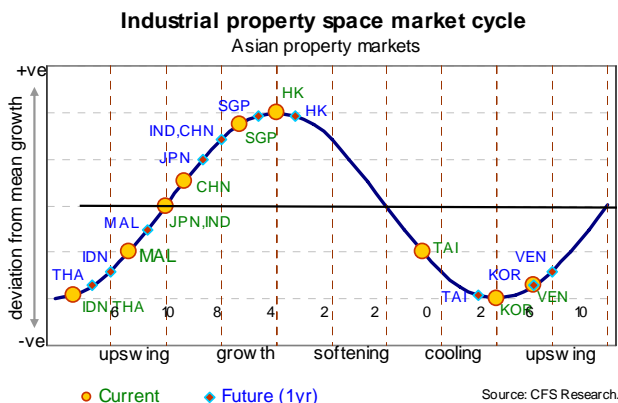


Figure: 10B

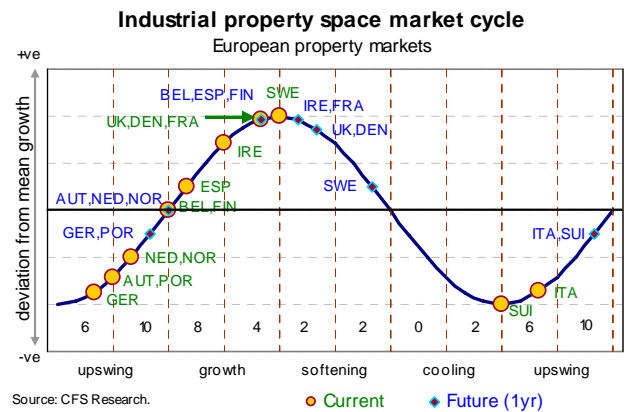
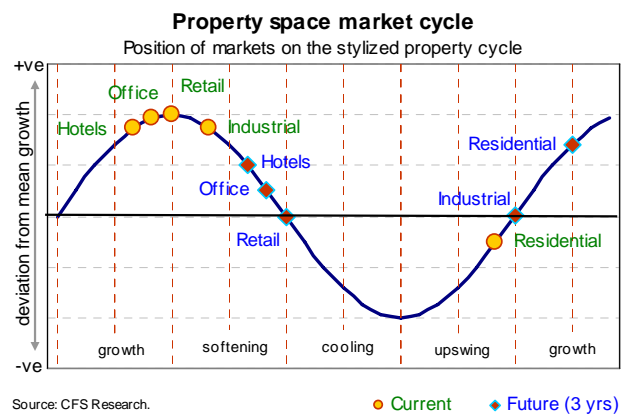


Figure: 10C



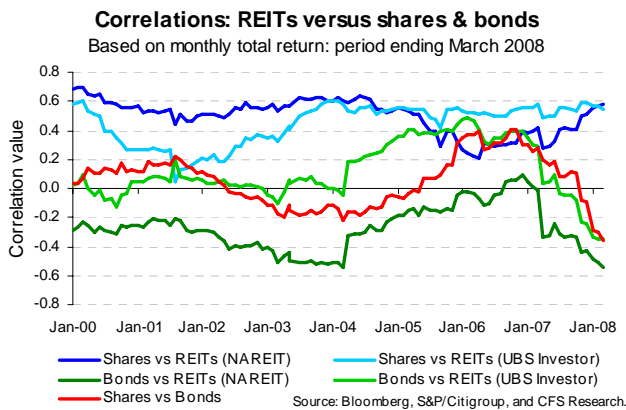
**Correlation**

Examining pair-wise return correlations is a formal way to gauge co-movement between any two investment markets. Low and negative correlation values indicate that markets tend to move counter-cyclical to each other, thus offering diversity across return profiles.

**Global asset classes**

Figure 11A shows return correlations between global REITs (based on the FTSE EPRA/NAREIT Global Real Estate Index and the UBS Global Real Estate Index), global shares (based on the MSCI World index) and global fixed interest (based on the JP Morgan government bond index) asset classes. The correlations are based on a 3 year sample period and rolled back through time to examine correlation stability.

Figure: 11A

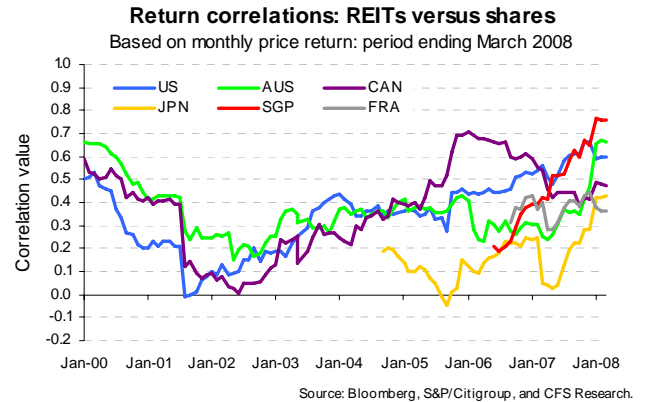


The correlation between global shares and global REITs is positive and moderately high. Correlation values over recent periods have hovered up towards 0.60. In contrast, the correlation between global bonds and global REITs has tended to be negative in recent times with values ranging between -0.3 to -0.55. More importantly, the chart displays that correlation values are not stable through time, but rather cyclical. Notably, over the last 12 months correlation values have tended to strengthen, partly a reflection of a synchronised downturn in investment markets due to the credit crisis. Overall, the relatively moderate and variable nature of correlation values hints at the potential for diversification benefits.

**Correlations for selected country markets**

Figure 11B shows price return correlation profiles between REITs and listed shares for selected countries. In line with the global series, correlations between REITs and share price returns have been strengthening recently. The lower correlation values around 2001 reflects the aftermath of the tech-wreck on investment markets which saw shares tumble and REIT markets rise as investors rotated capital towards defensive income yield-oriented investments.

Figure: 11B



**Correlations between listed and direct property markets**

Apart from examining correlations between REITs and other assets classes, it's also worth examining the co-movement between REITs and direct property. In gauging the correlations between listed and direct property markets, we focused on Australia and the US as being mature markets. Figure 11C and 11D show rolling annual returns for the Australian and the US direct property and REIT markets respectively. Notably, while the two series display significant disparity of the short-term, over the long-term both investment property markets display a convergence in returns. In this context, investment in REITs can be considered to be a surrogate for direct property exposure, but with the added benefit of offering liquidity.

Figure: 11C

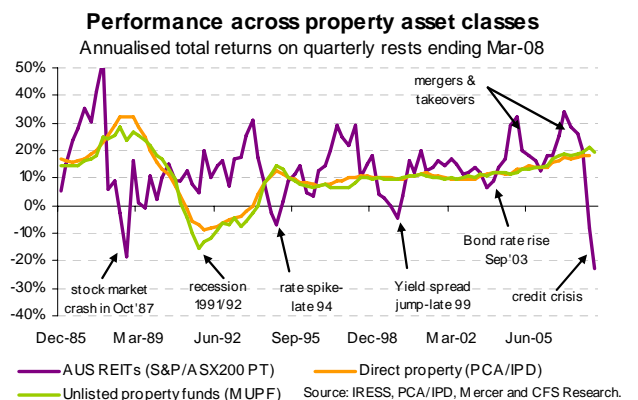
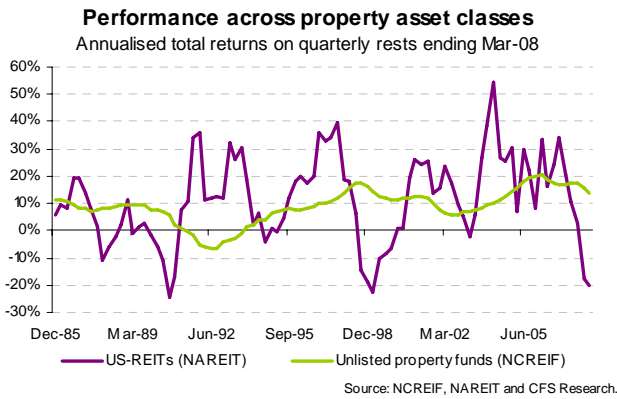


Figure: 11D



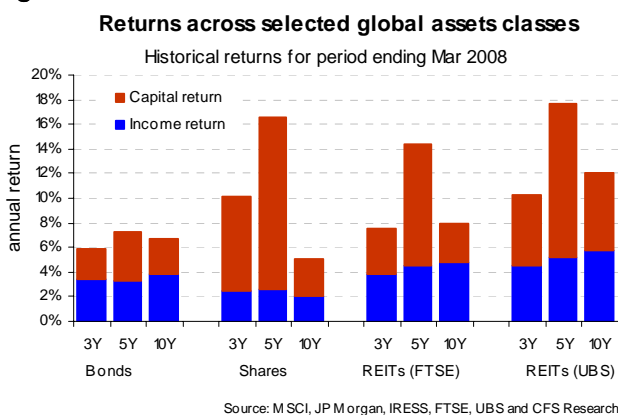
## 5. Product attributes

This section briefly outlines some of the key product attributes of REITs. Specifically, we focus on various key attributes: high income yield; a wide product range across the risk-reward space, and high liquidity. It is worth noting that the delivery of these features requires management with solid expertise and experience. As such, investors get access to professional experienced management teams.

### Return composition: yield focus

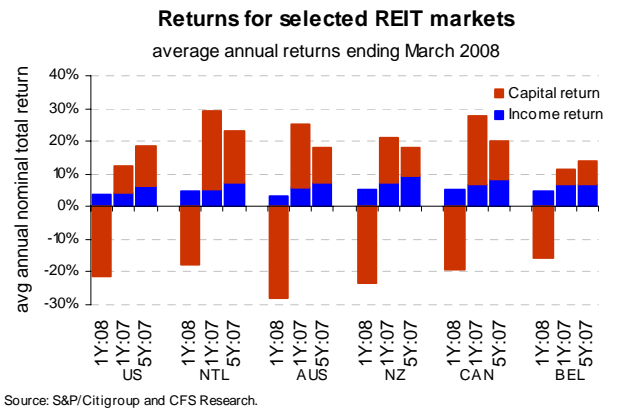
Figure 12A shows historical average annual returns for selected global indices over various time frames ending March 2008. [Note that income yield is an implied yield, calculated as the difference between total return and price return]. Notably, the return profiles for REITs deliver a higher income yield across all time frames relative to global bonds and listed shares. Furthermore, while the total return of REITs has underperformed shares over short time frames - the 3 and 5 year periods – it has outperformed over the longer time frame of ten years.

Figure: 12A



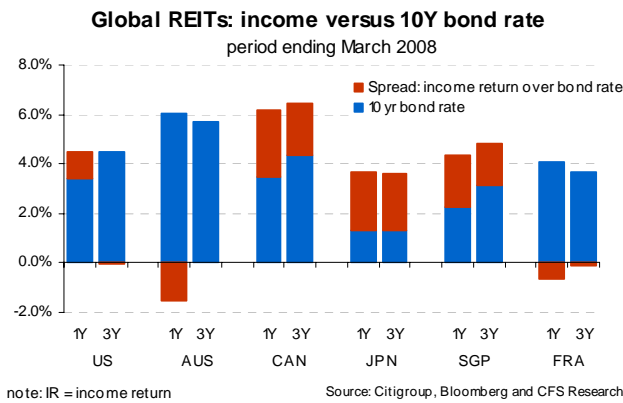
Focusing solely on REIT markets, Figure 12B shows returns for selected REIT markets split between income and capital. Notably, REIT markets deliver a relatively high income component (when compared with general equities), but the income component remains relatively stable even in times of market turmoil. For instance, with the recent downturn, while capital return has turned negative consistently across REIT markets; investors can take comfort in a stable income yield. However, note that while some markets, such as the UK, have experienced relatively low income return (during the recent credit crisis period), other markets (such as Canada, New Zealand and Australia) have delivered relatively higher income returns.

Figure: 12B



The income yield of REITs is commonly compared to the bond rate in gauging pricing. Figure 13 shows that REITs generally deliver an income return premium over the bond rate. The discount in income spread for Australian REITs reflects relatively tight yields; a reflection of strong investor demand against limited quality product, and on-going rises in the bond rate in line with tightening monetary policy. French REITs have also delivered a negative spread to the bond rate; largely a reflection of strong share price movements as underlying income growth is strong, running at c5% over the past year. [Note that returns for French REITs should be viewed as indicative only as the index only includes 12 constituents as opposed to the 50 trust reported in Table 1].

Figure: 13



**Population dynamics**

The relatively high income stream offered by REITs is a key attractive feature for investors. The attraction of REITs is part of a broader push by investor demand towards investment products with higher and stable income components. This stems from an aging population which will demand higher-dividend-paying investments to fund (i.e., sustain the cost of living) in their retirement.

A glimpse of this trend towards an aging global economy is highlighted in Table 2. It shows that almost 15% of total global population consist of people on the brink of retirement.

Table: 2

	Share (%) of Population above 65 years				
	2000	2005	2010	2015	2020
United States	12.4	12.4	13.0	14.5	16.3
United Kingdom	15.8	16.0	16.7	18.4	19.5
EU 15 Total	16.4	17.4	18.1	19.5	20.8
France	16.1	16.4	16.7	18.6	20.3
Germany	16.4	18.9	20.0	20.6	21.9
Italy	18.3	19.6	20.6	22.1	23.3
Netherlands	13.6	14.2	15.2	17.5	19.1
Spain	16.8	16.8	17.4	18.6	20.0
Australia	12.4	13.1	14.3	16.4	18.3
Japan	17.4	20.0	23.1	26.9	29.2
<b>OECD Total</b>	<b>13.0</b>	<b>13.8</b>	<b>14.7</b>	<b>16.2</b>	<b>17.8</b>

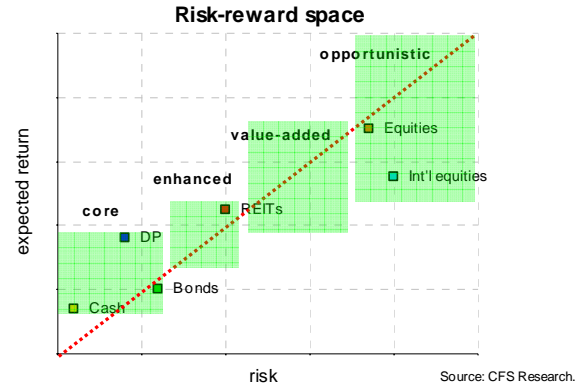
Source: UBS and CFS Research

**Proliferation in investment products**

This diversity in property assets offers investors a wide range of real estate investment products which caters for their differing risk tolerance levels. Figure 14A highlights the stylised investment segments in terms of the risk-return profile. They range from core products, which offer low risk and low return, to opportunistic products, that offer a higher level of risk associated with a wider range of return profiles. As shown on the

chart, direct property resides in the core space, A-REITs reside in the value-added space and shares reside in the opportunistic space.

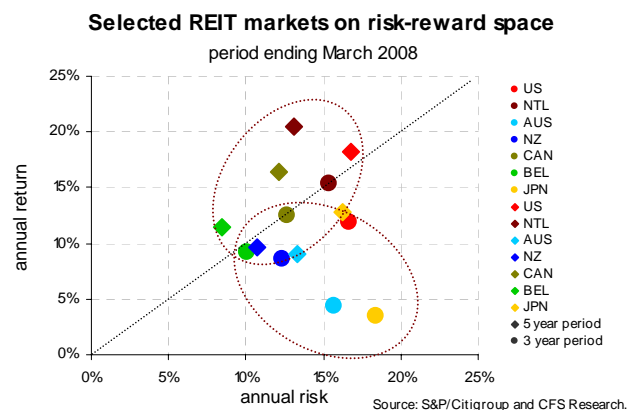
Figure: 14A



With the global expansion of the property investment market, the product offering has expanded beyond the core region in an effort to seek alpha (enhanced risk-adjusted) returns. REITs with exposure to core sectors typically reside in the enhanced region, exposure to non-core sectors generally reside in the value-added region, and exposure to international and (residential) development tend to reside in the opportunistic region.

It is also of interest to gauge how the various country REIT markets are positioned on the risk-reward space. Figure 14B plots selected markets with risk-reward estimates based of historical 3 and 5 year returns ending March 2008. Notably, the shorter time frame shows a general movement towards greater risk; a reflection of the sharp downturn in prices recently. The longer 5 year time frame generally highlights a more balanced trade-off between risk and return (i.e., markets tend to hover around the risk-reward locus).

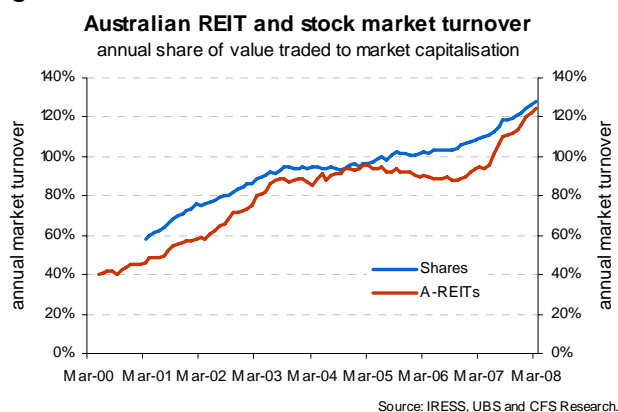
Figure: 14B



## Liquidity

A key appeal of REITs to investors is the ability to invest in a typically illiquid asset class through an efficient and liquid structure (via the stock exchange). In conjunction with a rising market capitalisation, liquidity (turnover) has also grown strongly in the sector. More importantly, liquidity for REITs has been in line with general equities. This is illustrated in Figure 15 for the Australian market.

Figure: 15



## 6. Investment structure

This section briefly discusses some key elements pertaining to the investment structure of REITs. Investment structures for REITs vary across country markets; however, they generally include three key entities: investors; the responsible entity or trust; and the manager. An important consideration is the treatment and engagement (or inter-relationship) between these three entities. One aspect of this relates to the type management model employed for management functions.

### Management model

A key feature of the REIT model is the type of management structure adopted; either the stapled trusts (unique to Australia due to a different tax treatment of trusts and corporations) or internally managed trust (IMT) or the externally managed trusts (EMTs).

IMTs are where REIT units and shares in a corporation are stapled together. Each stapled security comprises one unit in the trust stapled with one unit in the corporation. Such

corporations engage in a range of property service, management, development and construction activities. Distributions from the trust typically include a tax-advantaged component and dividends from the corporation may be franked. While IMTs don't have fee leakage (in terms of external management fees) they have company overheads (based on a percentage of gross asset value (or GAV)).

EMTs are where management of the assets is out-sourced to a third party. Under this arrangement, the asset manager receives a fee from the trust (on behalf of unit holders). Importantly, trust distributions to unit holders are net of management fees (leakage) and are typically tax advantaged.

In the US, publicly-traded REITs were initially externally managed, using external advisors and property managers (usually from the same company) to make investment decisions and to manage REITs' assets. Currently, many REITs are vertically integrated and efficiently internally managed corporations.

In the European region a variety of REIT management models are employed. For instance, UK REITs can choose their management business model to be either external (via the use of Special Purpose Vehicles) or internal. In Italy, REITs must adopt the corporate governance model (which have internally managed structures) as used by Italian joint-stock companies (known as SpA or Società per Azioni). French REITs use corporate structure and all REITs (known as SIIC) are internally managed. Furthermore, in both Belgium and Netherlands, REITs employ the corporation structure and both external and internal management structures exist.

In Asia, REITs generally adopt the external management model, using external managers and property managers for management services and purchase and management of assets.

Overall, both structures have advantages and disadvantages. However, it can be argued that overall performance is not dominated by the management structure but depends on the quality of the management team, its strategy and ability to execute the strategy.

## Gearing levels

Another important consideration of the investment structure relates to the level of gearing, measured as Net Debt over Enterprise Value. Leverage for Global REITs is around 33%; however it varies widely across country REIT markets. This is partly driven by different gearing conditions on investment structure as reported in Table 3, as well as prevailing market conditions and the cost of debt.

Table: 3

Gearing across selected REIT markets		
Net Debt / Enterprise Value (%)		
REIT markets	Gearing condition	Gearing Level (as at May-08)
US	No restrictions	42%
Netherlands	60% of property assets	39%
Australia	No restrictions	32%
New Zealand	Generally no restrictions	34%
Canada	No restrictions	NA
Belgium	65% of total assets	52%
Turkey	No restrictions	NA
Japan	No restrictions	26%
Korea	Limit to 200% of equity	NA
Singapore	35% of total assets	29%
France	No restrictions	38%
Taiwan	35%	NA
Hong Kong	45% of total assets	24%
Malaysia	35%	15%
Thailand	Prohibited	15%
Germany	55% of its real estate assets	NA
United Kingdom	1.25x interest cover test	49%

Source: E&Y, UBS and CFS Research.

For instance, leverage levels in A-REITs have increased strongly since 1994 from 10% to stand around 32% at present, although it varies across sub-sectors. The increased gearing is attributable to: i) a gradual reduction in the level and volatility of market interest rates; ii) greater use of capital management to expand and generate enhanced returns (strong distribution per unit growth); and iii) historical low levels of (perceived) risk in property investment.

In addition, since REITs can be highly leveraged they perform well in a growing market, but losses can be amplified in the falling market. Thus, going forward fund managers will be more conservative in gearing levels, in light of credit crisis and high interest rates.

## Taxation

An important element of REIT investment structures relates to taxation. This section briefly discusses the tax treatment of profits (both income and capital gain) and withholding tax regimes (related to distributions to its shareholders) for REITs. The full overview of the tax treatment across for selected REIT markets is provided in Table A2 of the Appendix.

REIT structures are characterised as non-taxable flow-through entities. In general, REITs have a favourable tax treatment in exchange for distributing the majority or all of their income to shareholders. This minimum dividend distribution requirement usually varies between 80% and 100%. When REITs distribute income to investors (shareholders) they are exempt from paying income tax; the income tax is borne by investors (based on their individual marginal tax rate). Payout ratios are usually high as any undistributed income held by the REIT will be subject to tax. Importantly, through their status of non-taxable flow-through entities, REITs avoid the double-taxation problem linked to distribution of dividends for corporations.

Globally, while REITs are usually exempt from capital gain taxes, in some countries they receive a similar treatment to current income or they form part of taxable profit. However, if 100% of taxable income is distributed as dividends capital gains are normally fully exempt from taxation.

Since investing directly in real estate is generally considered to be tax inefficient, REITs offer additional tax benefits to foreign investors. Generally, various treaties significantly reduce withholding tax on distributions to foreign residents if their individual share is less than 10% of the value of REIT. Since the REITs landscape is rapidly evolving, countries try to retain the competitive advantage over their competitors on the back of the taxation rate that applies to the investor. That is why withholding tax for foreign investors becomes an important component of country competitiveness.

## 7. Portfolio construction

This section presents various types of portfolio constructions in an attempt to gauge the value of mixing REITs across markets and adding REITs to portfolios of traditional assets classes.

### Global REIT portfolio

In constructing a global REIT portfolio we have restricted our universe of REIT markets to only a handful of markets; five in total. These five markets were selected to reflect regional exposure (i.e., North America, Australasia, Asia and Europe) but also include markets with adequate time series on returns and significant global market size.

In this study six stylised portfolios were constructed to reflect different weighting schemes across regional REIT markets. Portfolio 1 (P1) applied equal weighting across the four regions. [Note that Japan and Singapore are each given a weight of 12.5% as they are part of the Asian region]. Portfolio 2 (P2) assigns weights based on each individual's share of the global REIT market in terms of market capitalisation. Portfolios 3, 4, 5, 6 consider different scenarios in terms of regional dominance. As such, the dominant region is assigned a weighting of 50% with the remainder of the 50% equally weighted across remaining regions.

Return and risk metrics for the five individual REIT markets and six portfolios are reported in Table 4. We have also computed a risk-adjusted return measure based on the Shape Ratio (SR).

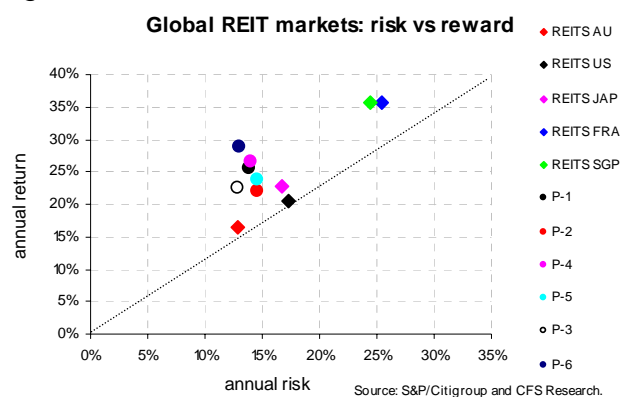
Table 4 clearly shows that the global REIT portfolio heavily weighted towards Europe (essentially French REITs) outperforms. This is not surprising since the French REITs have considerably outperformed their global counterparts in terms of total returns, offering an average annual return of 35.6% over the past five years while delivering a relatively low level of risk.

Table: 4

Global Portfolio Construction										
Nominal Total Returns 5 years ending March 2008										
Regions	return	stdev	SR	Portfolio						
				Equal Weight	Market Cap	AU centric	Asia Centric	US centric	FRA-centric	
				P-1	P-2	P-3	P-4	P-5	P-6	
REITS AU	16.4%	12.9%	1.27	25.0%	16.0%	50.0%	16.7%	16.7%	16.7%	16.7%
REITS US	20.6%	17.3%	1.19	25.0%	56.0%	16.7%	16.7%	50.0%	16.7%	16.7%
REITS JAP	22.7%	16.7%	1.36	12.5%	16.4%	8.3%	25.0%	8.3%	8.3%	8.3%
REITS SGP	35.6%	24.4%	1.46	12.5%	3.8%	8.3%	25.0%	8.3%	8.3%	8.3%
REITS FRA	35.6%	25.5%	1.40	25.0%	7.9%	16.7%	16.7%	16.7%	50.0%	50.0%
combined				100.0%	100.0%	100.0%	100.0%	100.0%	100.0%	100.0%
Return (annual)				25.5%	22.0%	22.4%	26.7%	23.8%	28.8%	
Std dev rate (annual)				13.8%	14.6%	12.9%	14.0%	14.6%	13.0%	
SR				1.84	1.51	1.74	1.90	1.63	2.22	

Figure 17A graphically presents the six portfolios against the five REIT markets on a risk-reward diagram. Notably, the six portfolios represent better risk-adjusted returns than the individual country REIT markets.

Figure: 17A



### Balanced global portfolio augmented with REITs

In this next exercise we construct a simple global portfolio consisting of global shares and fixed interest assets and add global REITs. Global shares are represented by the MSCI World Index, global REITs are represented by the S&P BMI World REIT Index and global bonds are represented by the JP Morgan Government Bond Index.

The analysis makes use of return, risk and correlation estimates based on historical total return data over the last five years ending March 2008.

Five stylised portfolios were constructed to reflect different weighting schemes across the global portfolio. Portfolio 1 (P1) consists solely of traditional assets classes, applying equal weight to shares and bonds. Portfolios 2, 3, 4 and 5 give increasing weight to global REITs, starting with a weight of 5% and rising by increments of 5% to a maximum weight of

20% in portfolio 5 (P5). This increase in weight to REITs comes at the expense of an equal down-weight to shares and bonds.

Table 5 shows that as the global portfolio gives increasing weight to global REITs, not only does the portfolio return increase, but the SR metric also increases. This highlights that augmenting a global portfolio of listed shares fixed interest with REITs delivers enhanced risk-adjusted returns.

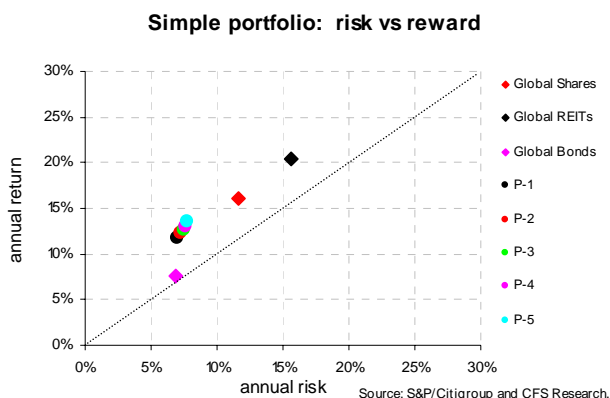
Table: 5

Global Portfolio Construction									
Nominal Total Returns 5 years ending March 2008									
Regions	return	stdev	SR	Portfolio					
				P-1	P-2	P-3	P-4	P-5	
Global Shares	16.0%	11.7%	1.37	50.0%	47.5%	45.0%	42.5%	40.0%	
Global Bonds	7.6%	6.9%	1.10	50.0%	47.5%	45.0%	42.5%	40.0%	
Global REITs	20.4%	15.7%	1.30	0.0%	5.0%	10.0%	15.0%	20.0%	
combined				100.0%	100.0%	100.0%	100.0%	100.0%	100.0%
Return				11.8%	12.2%	12.7%	13.1%	13.5%	
Std dev				7.0%	7.3%	7.5%	7.7%	7.8%	
SR				1.69	1.68	1.69	1.71	1.74	

Source: CFS Research.

Figure 17B graphically presents the five portfolios (denoted by the circles) against the three asset markets (denoted by the diamond symbols) on a risk-reward diagram. Notably, the five portfolios represent better risk-adjusted returns than the individual country REIT markets. The best case scenario, indicated by the light blue circle, is P5 comprising of 40% shares, 40% fixed interest, and 20% REITs. Such a portfolio would increase returns by 170 basis points and risk by only 80 basis points, compared to P1.

Figure: 17B



### Balanced country-specific portfolios augmented with REITs

In this final exercise we undertake a similar portfolio analysis to the previous section – we construct simple three asset class portfolios,

comprising of listed shares, fixed interest and REITs, but for selected country markets. The country markets include: Australia, United States, Japan, Singapore and France.

Once again the analysis makes use of return, risk and correlation estimates based on historical total return data over the last five years ending March 2008. For each country portfolio five stylised portfolios are constructed with REIT allocations from zero (for P1) to 20% (for P5).

Portfolio results are reported in Tables 6A, 6B, 6C, 6D and 6E. Generally, with increasing weight to REITs, the overall portfolio return and risk-adjusted ratio are improved for all country-specific portfolios.

While we proved that the real estate is a successful diversifier in country centric mixed portfolios, extensive research still has to be completed to provide an answer on optimal amount of properties needed to create a well diversified real estate portfolio.

Table: 6A

Portfolio Construction for Australia									
Nominal Total Returns 5 years ending March 2008									
Regions	return	stdev	SR	Portfolio					
				P-1	P-2	P-3	P-4	P-5	
Shares	19.8%	11.0%	1.80	50.0%	47.5%	45.0%	42.5%	40.0%	
Bonds	15.1%	10.3%	1.47	50.0%	47.5%	45.0%	42.5%	40.0%	
REITs	16.4%	12.9%	1.27	0.0%	5.0%	10.0%	15.0%	20.0%	
combined				100.0%	100.0%	100.0%	100.0%	100.0%	100.0%
Return (annual)				17.4%	17.4%	17.3%	17.3%	17.2%	
Std dev rate (annual)				5.1%	5.0%	5.0%	5.2%	5.3%	
SR				3.44	3.47	3.44	3.36	3.23	

Source: CFS Research.

Table: 6B

Portfolio Construction for US									
Nominal Total Returns 5 years ending March 2008									
Regions	return	stdev	SR	Portfolio					
				P-1	P-2	P-3	P-4	P-5	
Shares	11.5%	10.4%	1.11	50.0%	47.5%	45.0%	42.5%	40.0%	
Bonds	4.6%	3.9%	1.19	50.0%	47.5%	45.0%	42.5%	40.0%	
REITs	20.6%	17.3%	1.19	0.0%	5.0%	10.0%	15.0%	20.0%	
combined				100.0%	100.0%	100.0%	100.0%	100.0%	100.0%
Return (annual)				8.1%	8.7%	9.3%	10.0%	10.6%	
Std dev rate (annual)				3.7%	3.8%	4.1%	4.5%	4.9%	
SR				2.19	2.27	2.27	2.23	2.16	

Source: CFS Research.

Table: 6C

Portfolio Construction for Japan									
Nominal Total Returns 5 years ending March 2008									
Regions	return	stdev	SR	Portfolio					
				P-1	P-2	P-3	P-4	P-5	
Shares	13.5%	20.9%	0.65	50.0%	47.5%	45.0%	42.5%	40.0%	
Bonds	2.7%	7.8%	0.34	50.0%	47.5%	45.0%	42.5%	40.0%	
REITs	22.7%	16.7%	1.36	0.0%	5.0%	10.0%	15.0%	20.0%	
combined				100.0%	100.0%	100.0%	100.0%	100.0%	100.0%
Return (annual)				8.1%	8.8%	9.6%	10.3%	11.0%	
Std dev rate (annual)				5.5%	5.3%	5.2%	5.2%	5.4%	
SR				1.47	1.67	1.84	1.97	2.05	

Source: CFS Research.

Table: 6D

Portfolio Construction for Singapore								
Nominal Total Returns 5 years ending March 2008								
Regions	return	stdev	SR	Portfolio				
				P-1	P-2	P-3	P-4	P-5
Shares	19.1%	16.9%	1.13	50.0%	47.5%	45.0%	42.5%	40.0%
Bonds	7.4%	5.3%	1.40	50.0%	47.5%	45.0%	42.5%	40.0%
REITs	35.6%	24.4%	1.46	0.0%	5.0%	10.0%	15.0%	20.0%
combined				100.0%	100.0%	100.0%	100.0%	100.0%
Return (annual)				13.3%	14.4%	15.5%	16.6%	17.7%
Std dev rate (annual)				6.6%	6.8%	7.1%	7.5%	7.9%
SR				2.02	2.11	2.18	2.22	2.24

Source: CFS Research.

Table: 6E

Portfolio Construction for France								
Nominal Total Returns 5 years ending March 2008								
Regions	return	stdev	SR	Portfolio				
				P-1	P-2	P-3	P-4	P-5
Shares	17.5%	11.2%	1.56	50.0%	47.5%	45.0%	42.5%	40.0%
Bonds	12.6%	10.6%	1.19	50.0%	47.5%	45.0%	42.5%	40.0%
REITs	35.6%	25.5%	1.40	0.0%	5.0%	10.0%	15.0%	20.0%
combined				100.0%	100.0%	100.0%	100.0%	100.0%
Return (annual)				15.0%	16.1%	17.1%	18.1%	19.2%
Std dev rate (annual)				3.5%	4.4%	4.7%	5.3%	6.0%
SR				4.34	3.65	3.67	3.40	3.18

Source: CFS Research.

## 8. Research Team

**Did you know CFS Research has a global reach and the expertise to tailor research to your needs?**

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# 9. Appendix

Table: A1

Summary of existing world REIT markets

February 2008																			
	1960	1969	1971	1982	1993	1995	1999	2001	2001	2002	2003	2005	2005	2005	2005	2007	2007	2004	
No of REITs (February 2008)	152	7	34	10	31	14	10	42	6	18	50	8	7	13		2	19	12	
REIT Mkt Cap US\$bn (February 2008)	\$299.3	\$17.0	\$85.5	\$2.6	\$22.9	\$7.1	\$1.6	\$42.0	\$0.6	\$20.3	\$67.8	\$1.9	\$9.0	\$1.6	\$163.8	\$1.1	\$53.9	\$5.1	
Equity Mkt Cap US\$bn (February 2008)	\$14,448.7	\$702.2	\$1,128.8	\$40.5	\$1,635.7	\$344.3	\$197.0	\$4,123.7	\$782.2	\$362.0	\$2,296.9	\$507.5	\$1,504.1	\$253.0	\$1,638.8	\$2,739.2	\$6,893.7	\$17.3	
% of REIT to Equity Market	2.1%	2.4%	7.6%	6.3%	1.4%	2.1%	0.8%	1.0%	0.1%	5.3%	3.8%	0.4%	0.6%	0.04%	0.04%	0.04%	0.8%	29.3%	
Management	Internal/External	Internal	Internal/External	Internal/External	Internal	Internal/External	Internal/External	External	Internal/External	External	Internal/External	Internal/External	Internal/External	External	External	Internal/External	Internal/External		
Legal Structure	Most are UPREITs structure	When structured with a holding company sitting above a number of subsidiaries	Trust	Trust	Closed-ended mutual fund trusts	Closed-ended company	Trust or Corporation currently formed as Corporation	Trust or Corporation currently formed as Corporation	Trust or Corporation currently formed as Corporation	Trust or Corporation currently formed as Corporation	SA (corporation) or SCA (limited partnership)	Trust	Trust	Property Trust Funds	Mutual fund				
Location of Investments			Unrestricted. Currently holding mainly in Aust, NZ, US, UK and Continental Europe	Unrestricted. Current holdings mainly in NZ				Unrestricted. Current holdings mainly in Japan	Unrestricted. Current holdings solely in Korea.	Unrestricted. Current holdings mainly in Singapore and HK		Unrestricted. Current holdings in Taiwan only.	Unrestricted. Holdings of assets expected to be mainly in Hong Kong and China.	Unrestricted. Current holdings in Malaysia only.	Thailand only				
Min number of shareholders	min 100 shareholders, any 5 certificate holders = 50% of total value		min 500 before listing		min 150 shareholders		min 1,000 before listing			min 500 before listing		min 50 holders, any 2 certificate holders = 50% of total value		No less than 250 holders					
Mandatory listing	No	No	No	No	No	No	No	No	Generally no	Yes	No	No	No	No	No	No	No	No	No
Minimum initial investment			No requirement	No minimum requirement	No less than \$500			JPY 5bn (USD45m) total assets before listing	KRW500n (circa USD50m) before listing	SGD20m or 25% of units held by >500 public holders		No minimum requirement	No minimum requirement	RM100m (circa USD26m)	8500m (circa USD 12.5m)				
Investment Restrictions											15% share capital to be held by shareholders owning less than 2% shareholding must be 60%								
Real Estate Investment	75%+	100%	>50% of revenue from property		80%+	100%	50%+	75%+	70%+	70%+	Flexible	75%+	100%	50-75%	75%+	75%+	75%+	75%+	75%+
Overseas Assets	OK	OK	OK	OK	OK	OK	OK	Restricted	OK	OK	OK	OK	OK	OK	Restricted	OK	OK	OK	OK
Development	OK	Minimal	OK	OK	OK	OK	OK	Restricted	OK	OK	OK	OK	OK	Prohibited	Prohibited	Prohibited	Prohibited	OK	OK
Geared Limit	No restrictions	80% of property	No restrictions	Generally no	No restrictions	80% of total assets	No restrictions	No restrictions	OK (max 80%)	20% of total assets	No restrictions	30%	30%	Prohibited	Prohibited	Prohibited	Prohibited	OK	OK
Payout	>90% of taxable income (post depreciation)	100% of fiscal earnings	100% of taxable income (post depreciation)	Generally no	80% of distributable cash earnings (pre depreciation)	80% of taxable income and net pay down	No legislation to distribute income	>90% of taxable income (post depreciation)	>90% of equity less capital and reserves	100% of taxable income (no depreciation)	80% of taxable income from rentals, 50% of capital gains	100% of net income (post expense and reserve)	100% of net income after tax (no depreciation)	No restrictions but undistributed earnings taxed at 25%	>90% of profit	>90% of profit incl. half of gains	50% of profit incl. half of gains	50% of net assets	50% of net assets
Closed ended	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Closed ended fully listed and need government's approval	Yes	Yes	Yes	Yes	Closed
Foreign Ownership restrictions	Allowed	Max 25% by single investor	Allowed	Allowed	No limit	No limit	No limit	No limit	No limit	No limit	No limit	Approval required	No limit	Minimum 30% Bumiputera equity, max 49% foreign equity participations in REIT	Rest to LN40%	Rest to LN40%	10% holding rule	10% holding rule	
Tax Transparency	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	No*	Yes	Yes	Yes	Yes	Yes	Yes
<b>Tax Treatment - Distribution at Trust level</b>																			
Local Institution								Tax free	n.a	Tax free	Tax free	Tax free	17.5%	Tax free	Tax free	Tax free	Tax free	Tax free	Tax free
Foreign Institution	Partial exemption	25% may be reduced pursuant to a double taxation treaty	Partial exemption		25% withholding tax on income paid to non-resident unit holder	15% dividend withholding tax, may be reduced with tax treaty		Partial	n.a	10% 1% stamp duty/overseas	25% dividend withholding tax, may be reduced with tax treaty	Tax free	17.5% (corp tax) 15% property tax	28% (corp tax), 15% withholding tax on offshore interest payments	Tax free			25% dividend withholding tax, may be reduced with tax treaty	
<b>Tax Treatment - At recipient level</b>																			
Local Institution								Income tax	n.a	Tax free	subject to diff treatment if paid out of exempt or taxable profit and gain	6.0%	Net of above	Marginal tax	Tax free	Final withholding tax, capital gains may be exempt	subject to diff treatment if paid out of exempt or taxable profit and gain		
Foreign Institution								Corp tax	n.a	20.0%	standard income tax	6.0%	Net of above	Corp tax	Corp tax		standard income tax		
<b>Other taxes and duties</b>																			
	Overseas withholding tax of 15%	Overseas withholding tax 15% but not on stock dividend	Limited trust: no stamp duty, overseas withholding tax					Acquisition, registration and various surcharges levied, although at a reduced rate	Reduced tax and duty on acquisition of real estate assets for the period 2005-2010		Exemption of stamp duty on acquisition of real estate assets for the period 2005-2010	Overseas withholding tax of 15%	Disposal of REIT certificate is exempt from income tax	Stamp duty of up to 3.75% in transfer of real estate into a REIT	RPG tax on regressive scale		Overseas withholding tax of 15%		

Source: EAV, IBS, NAREIT, Datastream, IRESS and CFS Research.

Note: \* not needed as there is no tax on dividends in HK

Table: A2

Comparison of Tax structures across REIT markets			
Country	Income	Capital Gain	Withholding Tax
<b>Europe</b>			
France SIIC	Exemption from CIT for eligible activities. Non-eligible activities are taxed at the rate of 33.33% increased to 35.43% by surcharges.	Capital gains resulting from disposal of assets or participations belonging to the eligible activities and duly distributed are exempt from Capital Income Taxes.	25% dividend withholding tax which may be reduced pursuant to tax treaties to 15%, 5% or 0% (substantial participation held at the rate of by a corporation)
Belgium SICAFI	In principle subject to the standard corporation tax rate (33.99%), but the qualifying real property income is excluded from the taxable basis.	Capital gains are not included in the taxable profit provided they are at arm's length.	15% dividend withholding tax, which may be reduced pursuant to the application of tax treaties.
Netherlands BI	Real property income forms part of the taxable profit and is taxed at a 0%-rate (a de facto full exemption)	Capital gains / losses are allocated to a tax-free reserve and are, therefore, exempt from tax.	25%, which may be reduced pursuant to a double taxation treaty. The amount of the tax-free capital gain reserve is considered "capital" for withholding tax purposes, which is in principle, not subject to withholding tax.
Italy FII	Tax exempt	Tax exempt	12.5%, which may be reduced to 0% in case of distribution to qualified resident or non-resident unit holders.
<b>Australasia</b>			
Australia	Not taxable in the hands of the trustee provided the unitholders are presently entitled to the trust's income. Certain types of income may be subject to tax in the hands of the trustee where the income is attributable to nonresident unitholders and is Australian sourced.	Tax treatment of capital gains similar to that of ordinary income. 50% CGT discount may be available.	Dividend and interest paid to non-resident unitholders is subject to withholding tax in accordance with domestic rules/treaty rules, as dividends or interest.
Hong Kong	REIT is ordinarily subject to property tax for property held directly, dividend income from SPVs is tax exempt from profits tax	No capital gain tax	None
Japan	JREIT is subject to tax but distributions are deductible.	Tax treatment similar to current income.	Withholding income tax rate for public JREITs is 7%, local tax rate: 3%, for details see sect. 2.4.
Korea General REIT	Property income forms part of the taxable profit and is taxed at 14.3% on income up to KRW 100 million and 27.5% on income above KRW 100 million.	Capital gains form part of the taxable profit and is taxed at 16.5% or 29.7%.	16.5% to Korean individual shareholders. Dividends to offshore shareholders may be reduced pursuant to the application of tax treaties
Korea CR-REIT	Property income forms part of the taxable profit but a full exemption is applicable if 100% of taxable income is distributed as dividends	Capital gains form part of the taxable profit but a full exemption is applicable if 100% of taxable income is distributed as dividends	16.5% to Korean individual shareholders. Dividends to offshore shareholders may be reduced pursuant to the application of tax treaties
Singapore	Not taxable at trustee level to the extent of taxable income distributed	No capital gains tax	70% on distributions to non qualifying unit holders, e.g. nonresident corporate unit holders
<b>North America</b>			
US REIT	Dividend distributions for tax purposes are allocated to ordinary income, capital gains and return of capital, each of which may be taxed at a different rate. Dividends are deductible from taxable income. A REIT pays corporate income tax to the extent it retains income.	Capital gains follow the same system as ordinary income: to the extent the capital gains are distributed to the REIT's shareholders in the form of dividends, these may be deducted from taxable income.	No withholding to US shareholders. 30% rate applied to ordinary dividends to non-US shareholders unless a lower treaty rate applies (usual case). 35% withholding rate on REIT capital gain distributions to non-US shareholders.
Canada MFT	An MFT, like any trust resident in Canada, is taxed as individual on its worldwide income from all sources including capital and gains computed under the ITA. It is entitled to deduct when in computing its income for a taxation year all income determined for purposes of the ITA was paid or payable to unit holders in the year thereby reducing its net income to zero.	Capital gains follow the same system for income except only 50% of a capital gain (a "taxable capital gain") is included in income and 50% of a capital loss can be applied to offset taxable capital gains.	There is no withholding on distributions made to residents of Canada. There is a 25% withholding tax on income paid to a unit holder that is non-resident of Canada subject to reduction under a tax treaty. Prior to the proposal 2004 federal budget (discussed below), distributions in excess of income and distributions of capital gains from the disposition of "taxable canadian property" did not attract withholding tax.