

Australian REITs Continue on Strong Growth Path

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Australia is the most securitized real estate market on the globe, with approximately 70% of its investment grade commercial real estate assets being owned by listed and unlisted REITs. Australia first introduced REITs in the early 1970s and further expanded the offerings to property securities and mortgage funds in the mid 1980s. Unlisted REITs (unlisted property trusts) suffered a severe setback in the early 1990s due to the commercial property market collapse combined with economic recession; many funds were frozen for several years, leaving most private investors very disillusioned with the whole REITs concept. The real leap forward for listed REITs (LPTs) came in the mid 1990s when most of the frozen unlisted funds were forced to list for liquidity reasons, this introduced approximately 300,000 new investors and their advisers to actively participating in the listed REITs market.

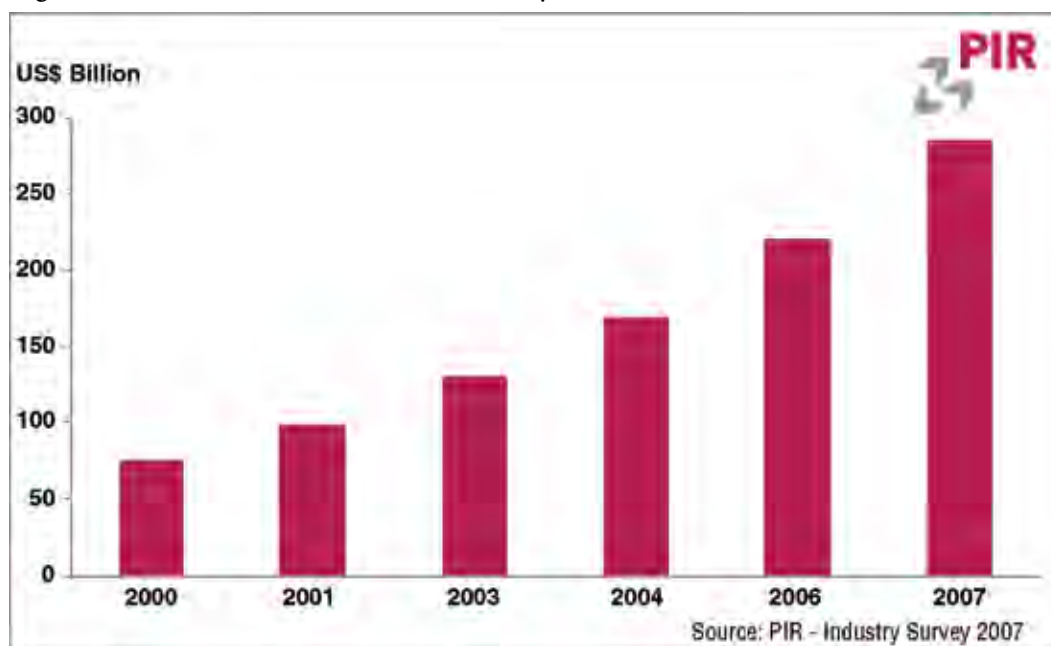
The key growth drivers of Australia's REITs market have come about through several factors; most

institutions/pension funds came to realise in the late 1990s that they did not have sufficient scale to own and manage direct property, Australian's traditional love affair with real estate (70% home ownership), and a wall of money accumulating from the introduction of compulsory pension contributions introduced in 1992.

The wall of money from pension contributions is now rapidly approaching US\$1 trillion. This has caused considerable undersupply of investable product, causing Australia to be a disproportionate investor in offshore markets. REITs were one of the main beneficiaries, having subsequently invested close to US\$50 billion in off shore real estate in the past decade, the bulk of this investment is in the USA (predominately retail) we are now seeing a very distinct shift in focus towards Europe and Asia. This trend is also being taken up by the unlisted REIT sector, which has committed US\$2.5 billion to date.

The Australian REITs industry continues to grow at a rate that has exceeded a compound annual

Figure 1: Growth of Australian REITs Industry 2000–2007



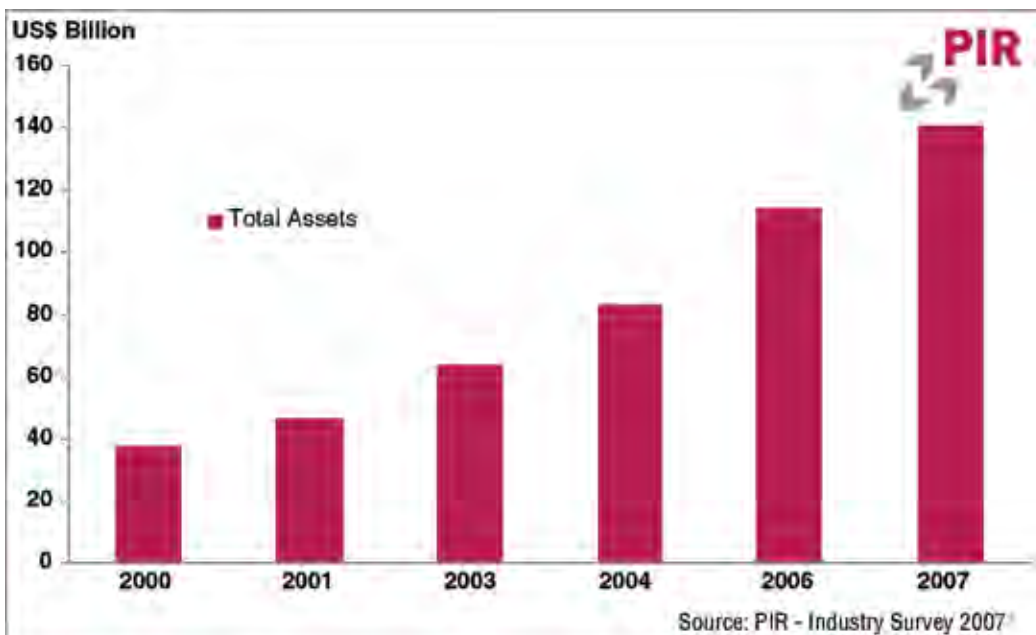
growth rate of 20% since Property Investment Research (PIR) commenced formal monitoring of investment statistics/funds in 2000 (Figure 1 on page 15). Looking at the past 12 months, the quantum of listed and unlisted REITs under management has increased by 29% to reach US\$285 billion, now approximately 1.3 million investors, an increase of 8%. The rapid industry expansion has continued to be fuelled by the weight of investable funds, driven by compulsory pension and retirement savings seeking exposure to real estate and met by price inflation as yields continue to tighten across the board, with some testing levels not seen since the 1980s boom.

While the consensus view is that things really are “different” this time, significant yield compression in real estate markets has placed increased reliance on even further capital growth and continued rental escalation to achieve total returns commensurate with the attendant level of risk associated with any acquisitions of both securitized and “direct” assets. While the weight of funds seeking a home in securitized real estate has enhanced competition for assets and contributed to this yield compression (and therefore often yield dilution to existing funds), it is not certain that this trend is sustainable. There may be some compression left yet, however, based on investment fundamentals, it is quite possible (in fact, likely) that some subsequent reversal

(unwinding of yields) will undo some of the capital value gains made to this point. It is at that time that the performance of some acquisitions across the broader property market — without discrimination across sectors, funds or managers — may no longer be masked by the current benign environment.

If the current Australian REITs growth rate continues, PIR would expect the industry to exceed US\$400 billion in two years. The substantial growth in the industry is reflected by the expansion in real estate assets. The listed REITs sector has increased assets under management by 23% to reach US\$140 billion in the past year. This growth is, however, overshadowed by the unlisted REITs — retail sector, which from a small base has grown at an annual rate of 30% per annum since 2001. Similarly, property securities funds (mainly invested in listed REITs/LPTs) have also enjoyed considerable growth in assets. Over the past year, the property securities wholesale sector has increased in size by 42%. The reason for this rapid rise can initially be attributed to the growth in underlying listed REITs/LPTs (Figure 2). However, the excess growth is primarily due to the weight of pension contributions looking for managed exposure to this industry, which has enjoyed increasing returns for six years and, according to research from both PIR and Russell Investment Group, listed REITs have achieved

Figure 2: Listed REITs (LPT) Growth 2000–2007



returns ahead of competing investments (Figure 3).

As the Australian REITs market expands, the leading fund managers continue to maintain their dominance. The top 10 fund managers collectively control 57% of the overall REITs industry (Figure 4). Overall, the top 10 are responsible for real estate assets totalling US\$163 billion, an increase of 27% on last year's figure of US\$128 billion. Westfield on its own controls US\$39 billion (14% of the industry), the next biggest being AMP with US\$21 billion (7%), followed by Centro; both of whom have overtaken Macquarie from last year. While there has been movement within

the top 10 fund managers last year, there have been no new entrants or exits from the rankings.

Just as the top 10 fund managers dominate the property funds industry, listed REITs/LPTs are the dominant vehicle in property investment. As indicated by Figure 3, the listed REITs segment represents 49% of the overall property funds under management with over 4,300 properties, an increase of 40%. This growth can be attributable to the demand for direct property and in particular a 75% increase in international property assets over the past year. There were 66 listed REITs trading on the Australian Securities Exchange

Figure 3: Total Assets of all Australian Real Estate Funds

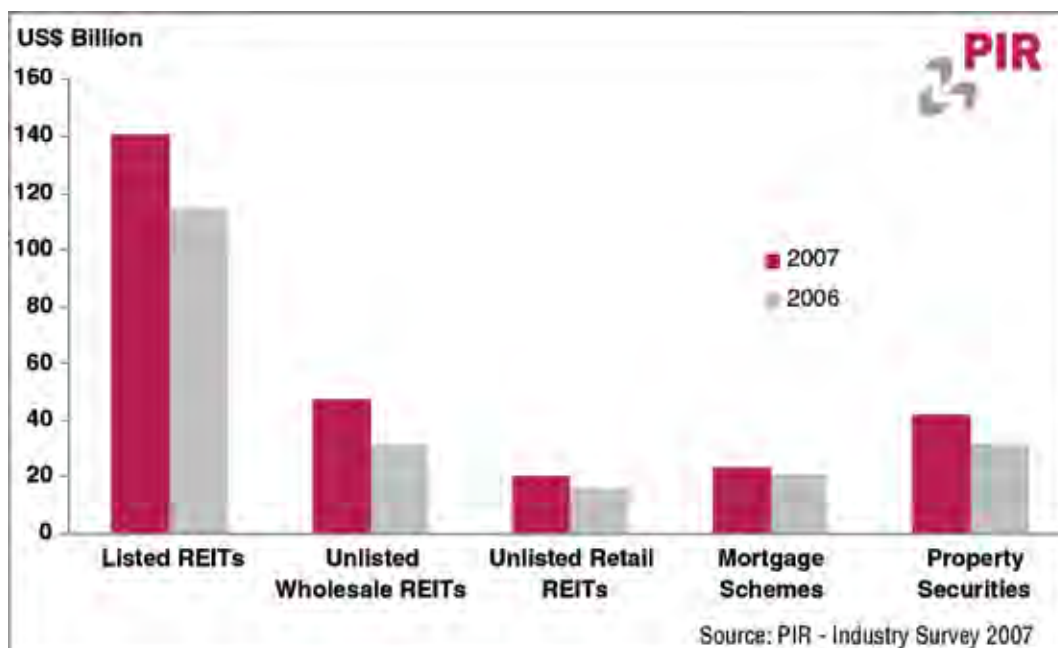


Figure 4: Australia's Top 10 Fund Manager — All Categories

Fund Manager	2007 Ranking	2006 Ranking	Total Assets (US\$m)
Westfield Group	1	1	39,432.8
AMP Capital Investors Limited	2	4	21,130.8
Centro Properties Group	3	5	18,386.7
Macquarie Bank Limited	4	2	16,856.6
Colonial First State Group	5	3	16,623.7
GPT Group	6	8	10,769.5
DB RREEF Funds Management Limited	7	6	10,670.0
ING Group	8	7	10,535.8
Stockland Trust Management Limited	9	10	9,349.8
Mirvac Group	10	9	9,017.7
Total			\$162,773.7

THE TOP 10 REITS MANAGERS BY FUND CATEGORIES

Figure 5: The Top 10 Listed REITs Managers

Total Assets of Listed REITs: US\$140.48 billion

Fund Manager	2007 Ranking	2006 Ranking	Total Assets (US\$m)	% of Total listed REITs
Westfield Group	1	1	39,432.8	28.5%
Macquarie Bank Limited	2	2	12,908.6	9.2%
GPT Group	3	3	8,881.5	6.2%
Stockland Trust Management Limited	4	5	8,624.1	6.2%
DB RREEF Funds Management Limited	5	6	7,224.0	5.2%
Colonial First State Global Asset Management	6	4	7,196.0	5.1%
ING Management Limited	7	10	6,810.0	4.9%
Mirvac Group	8	8	6,788.0	4.9%
Centro Properties Group	9	7	6,706.7	4.8%
Macquarie Goodman Funds Management Limited	10	12	6,196.0	4.4%
Total			\$110,768.2	79.1%

Figure 6: The Top 10 Unlisted Wholesale REITs Managers

Total Assets of UWF: US\$47.28 billion

Fund Manager	2007 Ranking	2006 Ranking	Total Assets (US\$m)	% of Total Wholesale
AMP Capital Investors Limited	1	1	9,277.4	19.6%
QIC Real Estate Funds Pty Ltd	2	2	7,194.4	15.2%
ISPT Pty Limited	3	4	4,514.2	9.5%
Lend Lease Corporation Limited	4	5	3,604.0	7.6%
Colonial First State Global Asset Management	5	3	3,324.2	7.0%
Centro Properties Group	6	new	2,880.0	6.1%
Eureka Funds Management Limited	7	7	2,252.9	4.8%
Macquarie Bank Limited	8	8	1,920.8	4.1%
GPT RE Limited; GPT Funds Management Limited	9	new	1,888.0	4.0%
DB RREEF Funds Management Limited	10	6	1,564.2	3.3%
Total			\$38,420.2	81.2%

Figure 7: The Top 10 Property Securities Fund Managers

Total Assets of Property Securities: US\$41.60 billion

Fund Manager	2007 Ranking	2006 Ranking	Total Assets(\$m)	% of Total Securities
AMP Capital Investors Limited	1	1	8,064.4	19.4%
Colonial First State Investments Ltd	2	4	2,843.8	6.8%
Vanguard Investments Australia Ltd	3	5	2,728.1	6.6%
BT Funds Management Limited	4	3	2,603.3	6.3%
Centro Properties Group	5	20	2,565.6	6.1%
APN Funds Management Limited	6	8	1,952.2	4.7%
MLC Investments Limited	7	7	1,834.2	4.4%
UBS Global Asset Management (Australia) Ltd	8	10	1,571.2	3.8%
Russell Investment Management Limited	9	12	1,497.8	3.6%
Franklin Templeton Investments Australia Limited	10	14	1,413.8	3.4%
Total			\$27,074.4	65.1%

(ASX) as at the end of March, compared with 62 a year earlier and 52 in March 2004. Among these are trusts who own solely US, Japanese and European real estate in addition to trusts who have diversified holdings across numerous countries and jurisdictions. The top 10 listed REITs managers control 79% of total listed assets under management — almost unchanged from last year.

Analysis of property funds by sub-sector highlights the more subdued growth of retail property which topped the table last year. This year, it was residential development which grew the fastest (albeit off a relatively low base), bouncing back from a decline in the previous year (indicating the volatile nature of this asset class). Substantial growth was also seen in retirement (160%) and healthcare (90%) — all “alternative” asset sub-classes which are likely to become mainstream as investor acceptance, liquidity, and availability raise their profile.

In 2006, we saw the increasing emergence of “hybrid” funds, where the portfolio comprises a mix of direct and indirectly held property assets. These funds have continued to grow in popularity with retail investors, as they generally offer greater liquidity and diversification than pure direct property trusts, with growth in FuM of 142% over the past year alone.

Finally, it is worth highlighting the movements in the gearing levels for certain categories. An overall increase in gearing from 26.9% to 28.9% was recorded, with growth particularly noticeable in unlisted REITs from 48.1% to 51.5%, driven largely by newer funds with higher gearing (reflecting the closed risk premium gap between the risk free rate and real estate yields) more than existing funds increasing gearing. In order to maintain investor momentum in the retail investor market, gearing has had to increase to keep

yield offers at an acceptable level — and, anecdotally, management fees have also been pared back. Average gearing in listed REITs also increased from 40.5% to 42.7%, fuelled largely by overseas acquisitions taking advantage of larger risk premia available in countries such as Japan and Spain.

It seems that unless investor sentiment becomes unhinged or an extraneous factor serves to mitigate the rate of growth of funds under management in the sector, that when PIR revisits the Property Funds Industry Survey in 2008, total FuM seems likely to be close to US\$336 billion. ★

*This article was produced by **Property Investment Research (PIR)**, Australia’s leading independent specialist research organization, providing full coverage of real estate funds and markets.*

For those organizations seeking more involvement with the Australian REITs industry, PIR provides several options:

- *Comprehensive research and statistical analysis on the Australian REITs market, including a complete directory of all funds, managers and key executives*
- *Online independent research covering listed and unlisted REITs and markets*
- ***The Australian Property Funds Industry Forum, the key annual REITs industry event, held between October 21–23, 2007 (Jim Fetgatter, AFIRE, 2007 Chairman)***

For further information, please visit www.pir.com.au



PIR was established in 1989. Richard Cruickshank was its architect and founder. He has held senior roles in the finance, investment, share broking and advisory disciplines in Australia and UK for the past 30 years and has maintained a pre-eminent role in property trust investment and research for more than 20 years.