

Low-beta markets favoured as medium-term performance is reassessed

Key Highlights

- Our ranking provides a timely reassessment of **medium-term** risk-adjusted property market performance prospects
- We continue to favour large, liquid and relatively mature property markets that are underpinned by stable or improving economies, particularly **Germany, Benelux and France**
- Despite the disappointing GDP data reported in Q2 2008, Germany's economy remains well positioned to deliver above-trend growth over the next five years, and consolidate its position as a **key investment target** for diversified property investors

Reassessing the relative attractiveness of European property markets

We believe property investors should look beyond volatile short-term data and take a medium-term view of key factors such as the economic growth outlook and property market liquidity, transparency and risk-adjusted performance. Our favoured countries provide opportunities to access diversified investment performance across a wide range of cities, regions and sectors in an environment where returns can be enhanced through asset management.

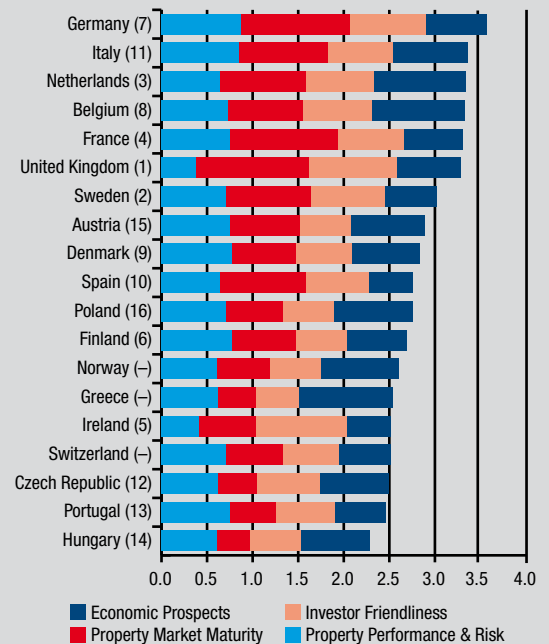
Germany, Italy, Benelux and France feature at the top of our updated European Property Market Relative Attractiveness ranking, which scores countries on the basis of key medium-term investment decision-making factors (refer to Figure 1).

Over the past year, the onset of the global credit crunch has amplified economic risks and caused investors to reassess future performance expectations based on a slower economic growth environment. The reduced ability of banks to lend to consumers and corporates, triggered by the credit crunch, is forecast to have a more pronounced impact on Europe's 'credit-intensive, housing-boom' economies.

Previous European economic out-performers, such as Ireland, Spain and Greece are therefore forecast to experience exaggerated slowdowns in economic growth over the next five years. In these economies future domestic demand growth is likely to be constrained by worsening government budget balances and relatively high levels of consumer debt (see Figure 2).

We believe that in light of greater economic and capital markets related risk, investors are reassessing their attitudes towards property pricing and risk. This process is likely to entail capital value declines in the short-term, with smaller, less liquid markets expected to experience higher levels of volatility in pricing. By contrast, volatility in Western Europe's largest and most mature property markets is expected to be less pronounced, resulting in a more attractive risk-adjusted performance profile.

FIGURE 1 : Germany, Italy, Benelux and France at the top of our medium-term ranking



Sources: Invista REIM, Datastream, OECD, IMF, Experian, ECB, PMA, CWHB, CBRE, DTZ, JLL
 Note: Ranking reflects the weighted sum of eighteen individually scored factors, based on Invista's detailed knowledge of local market conditions. Previous year ranking in brackets.

FIGURE 2 : Key European economic indicators

	GDP Growth 2008-12 relative to 2003-07	Budget Balance % of GDP 2007	Consumer Credit % of GDP 2005-07 avg
Portugal	+99%	-3.5	7.4
Germany	+54%	0.0	7.3
Italy	+11%	-4.0	3.3
France	+1%	-2.5	8.3
Norway	-8%	+17.0	7.2
Hungary	-9%	-6.2	7.6
Poland	-11%	-3.2	6.3
Switzerland	-13%	-0.1	7.2
Austria	-15%	-0.8	10.1
Czech Rep.	-19%	-3.3	3.6
Belgium	-22%	-0.1	2.8
Netherlands	-22%	+1.0	4.6
UK	-22%	-2.4	10.9
Sweden	-26%	+3.0	4.1
Finland	-27%	+3.9	6.2
Denmark	-29%	+4.2	7.5
Greece	-30%	-2.7	11.5
Spain	-49%	+1.1	9.3
Ireland	-52%	+0.5	11.2

Sources: Eurostat, EIU, European Central Bank
 Note: Countries are ranked according to GDP growth in 2008-12 relative to 2003-07

Decentralised Germany offers opportunities

Over the past few years, the German property market has benefited from a stable economic environment and improvements in transparency and liquidity, partly driven by an influx of foreign investment capital. It is now considered an important investment target for most pan-European property investors.

Germany is unique amongst Europe's major property markets due to its decentralised economy which supports a high number of densely populated cities and investable property markets. We identify at least fifteen cities with more than 500,000 inhabitants spread across the sixteen German Federal States.

The three largest States (listed below) account for around 55% of national economic output and 50% of the population, and have been focal points for property investors. However, we also highlight smaller States with positive or stable population dynamics and above-average wealth (see Figure 3):

- **Nordrhein-Westfalen:** With a population of 18 million, this region contributes over 20% of German economic output and is a focal point for manufacturing, trade and financial service sector companies. The Rhine-Ruhr urban agglomeration incorporates several major cities including Düsseldorf, Bonn, Cologne, Dortmund and Essen.
- **Bayern:** The largest State by area contributes 18% of German economic output. Financial & business services companies account for nearly one third of the Bavarian economy, making the State capital Munich one of Germany's most important commercial centres.
- **Baden-Württemberg:** A major hub for manufacturing, science and research & development, with a significant representation of domestic small and medium-sized enterprises (Mittelstand).
- **Hamburg/Bremen:** These 'City-States' are characterised by above-average economic output per head and feature important seaport infrastructure. They are therefore strategic locations for logistics operators.

We expect Germany to benefit from the European Union 'open-borders' policy which encourages the free flow of labour between EU countries. It has a strategic position between western and eastern Europe and future immigration growth could help to offset population declines over the longer-term caused by low birth rates. Demographic projections do however vary across Germany (see Figure 4): in the key States highlighted above, working age populations are forecast to remain broadly stable over the next twenty years, in contrast with former East German States which are expected to see declines.

In summary, we believe that despite recent economic data the German economy remains well positioned to deliver above-trend growth over the next five years. This is due to progress being made on important tax and labour market reforms, improvements in productivity and competitiveness, and the relaxation of immigration laws in order to alleviate skills shortages. Cities and States offering above-average wealth, positive or stable population dynamics and important regional or national infrastructure supporting manufacturing, trade, engineering, science and technology based companies are best placed to provide relatively attractive, low-beta investment returns over the medium term.

All data included is sourced to Destatis unless otherwise stated

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FIGURE 3: German economic output is dominated by the 'Big 3' Federal States

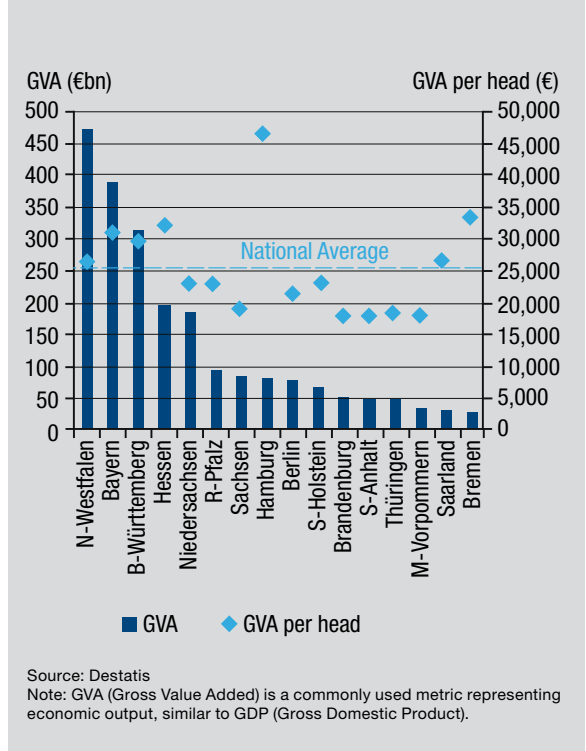


Figure 4: Working-age population is forecast to decline most sharply in Eastern States



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