Asia Quarterly Property Snapshot

Aberdeen

The economy

Recent performance

- The global economic environment began to stabilise over Q2 after a period of sharp quarterly contraction. Large fiscal stimuli and very loose monetary policy, along with a recent cyclical inventory recovery have assisted in this stabilisation. Economies most open to global trade were the hardest hit as trade and manufacturing activity collapsed, but these are also expected to benefit from this current restocking process.
- Asia Pacific economies benefited from all these global trends. Some countries, such as China, Singapore and South Korea, announced higher than expected economic growth in Q2 due to these factors. Manufacturing business confidence has improved markedly, in particular in China, where firms have realigned production to cater for the domestic rather than export market. Consumer confidence has also improved.
- Planned government spending is focusing on containing unemployment growth and stimulating domestic consumption which has typically lagged behind expectations. Inflation is not an immediate concern with some countries such as China and Japan currently in deflation mode. However, over the medium term there is some concern of inflation returning, particularly in food, energy and commodities. How central banks react to this threat will be key to long term prospects.
- Asia Pacific banks remain in a generally healthy state and have been willing to work with clients who have breached their LTV covenants. Chinese banks increased their lending substantially over H109 which has fuelled a housing and stock market rally with the latter's share prices above their 12 month lows. It is likely the pace at which these banks lent will slow over H209 which along with various monetary policy changes will help to control any potential overshooting.

Economic outlook

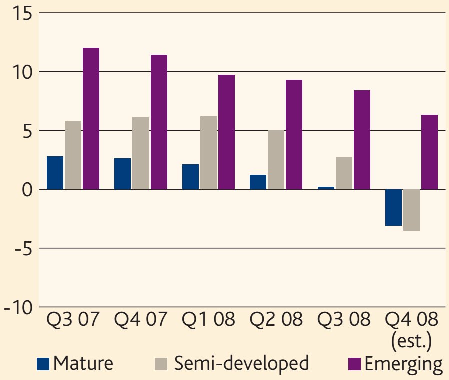
- By the end of next year it is expected countries in Asia Pacific will have had three years of sub-trend economic growth. A sustained recovery in Asia's trading partners, namely the US and Western Europe, will be needed before above trend growth can materialise. This recovery is forecast to start from mid 2010.
- Unemployment will peak next year but the wealth effect from improving conditions, including an equity market rally and housing recovery will potentially see urban, middle class consumers return to trend spending patterns. Apart from China and Indonesia consumer spending will be below trend this year, but may reverse next year as recovery takes hold.
- The economic outlook looked dim at the beginning of the year and got darker over Q1. However, surprise has been to the upside, with better economic growth than first thought and global stabilisation. Though conditions will remain tough for the balance of the year, Asia Pacific is well placed to benefit quickly from growth in the advanced economies, when (not if) they recover.

Economic forecasts

	2008	2009	2010
Real GDP growth (%)			
Mature*	0.2	(4.9)	1.3
Semi-developed*	1.9	(3.3)	4.3
Emerging*	8.0	6.2	7.7
Consumer spending growth (%)			
Mature	1.1	(0.9)	0.9
Semi-developed	1.4	(1.6)	3.5
Emerging	6.8	7.0	8.6
Employment growth (%)			
Mature	0.4	(0.7)	(0.6)
Semi-developed	0.4	(0.9)	1.0
Emerging	1.2	0.5	0.8
Unemployment rate (%)			
Mature	4.1	5.2	5.9
Semi-developed	3.5	4.6	4.5
Emerging	5.0	5.0	5.6

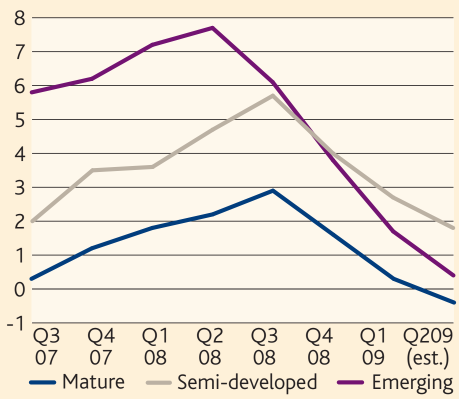
* Mature – Japan, Hong Kong, Singapore and Australia
Semi-developed – South Korea, Malaysia and Taiwan
Emerging – China, India, Thailand and Philippines
Source: Aberdeen Property Investors

Quarterly real GDP growth year-on-year (%)



Source: Thomson Datastream

Inflation (%)



Source: Thomson Datastream

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Property market overview

Recent performance

The downturn in Asia Pacific commercial property markets continued over Q2 though the speed of the decline abated. The leasing market saw further easing as landlords dropped asking rentals, increased rent free allowances and competed on non-financial terms such as lease flexibility. Though most markets saw capital values fall over the quarter, conditions in the investment market improved as easing credit markets, increased liquidity, lower interest rates and improved optimism about the outlook lead to greater investor confidence, particularly from domestic investors which were previously priced out of the market. This lead to a quarter-on-quarter increase in investment volumes, though levels remain sub-trend and global investors continue to sit on the sidelines. All Property capital values have eased YTD by some 9% since the start of the year, led by the office sector with retail and logistics following.

Offices

- Demand still exists for well located, prime, high occupancy office buildings. The bid ask spread between vendors and purchasers has reduced sufficiently that investment volumes improved over Q2. Though the outlook remains far from clear, capital value declines stabilised over Q2, declining by only 2%. Initial yields are a mixed bag, reacting to the speed of both the rental and value declines.
- Asian prime office rents fell 5.8% over Q2, bringing the year to date decline to just over 15%. Developed market rents declined the most as they continued, albeit at a slower rate, to adjust after reaching their peak in 2008. True tenant demand continued to be weak with brokers reporting activity being driven by renewal rather than expansion or relocation decisions. Jones Lang LaSalle reported net absorption recovering from a very low Q1. However, most of this was driven by precommitted supply and volumes still remain below trend levels. Vacancy continued to increase for the eighth consecutive quarter.

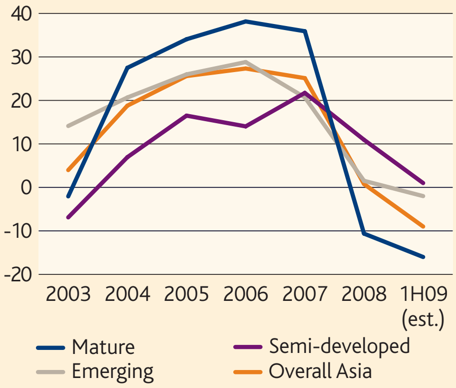
Retail

- Prime retailer demand trended down over Q2 as trading conditions were tough and the outlook uncertain (rents fell 1% quarter-on-quarter). Their prime focus at the moment is improving operational performance rather than expansion or new store openings. However, regional consumer confidence has recently rebounded, and there is some expectation that prime retailers will return to the new letting market in preparation for a possible recovery.
- Retail capital values were stable over the quarter, leaving yields to rise slightly. To date capital values have decreased 6.7% across the region, with most of the falls coming from emerging markets such as China and India where supply is greatest.

Logistics

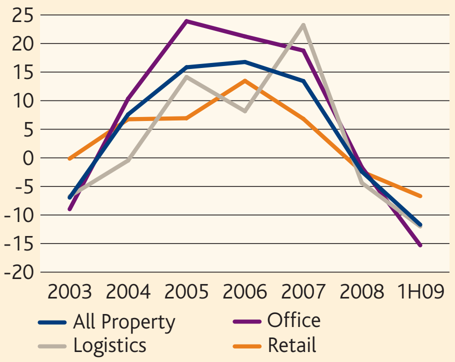
- Logistics rents fell across the region over Q2, but, as with the other sectors, at a slowing rate of decline. Tenant demand was concentrated from domestic orientated firms rather than those exposed to the export market.
- Capital values were down 3.8% over Q2 bringing year to date decline to 12%. Yields were mixed but overall were fairly stable.

All commercial property prime total return (%)



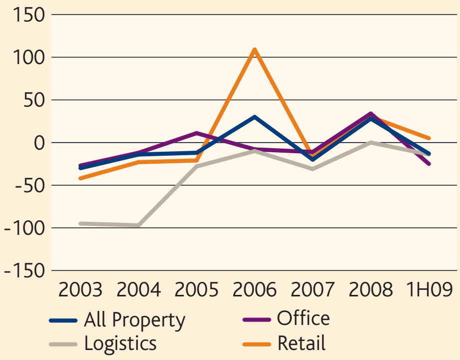
Source: Aberdeen Property Investors

Asia prime rental growth by sector (%)



Source: Aberdeen Property Investors

Asia prime yield shift by sector (bps)



Source: Aberdeen Property Investors

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Sector prospects

Outlook

This 2009 correction is significant and even severe in some markets, but for the Asia region it is shaping up to be less difficult than the Asian Financial crisis of 1997. The regional investment market will deliver an overall negative total return this year, though the year end outlook has improved as key property market indicators have slowed their rate of decline over the past quarter.

Though the outlook for the rest of the year is not much better than the performance over Q2, we now expect most of the declines to have been factored in to H109. We see total returns returning into positive territory in 2010 on the back on much more moderate year-end capital value declines and continuing strong income returns. However, this view is based on an economic outlook that is uncertain at this stage, and there are realisable risks to both the upside and downside.

Bank lending continues to be available for most completed projects with a secure income stream, but debt funding for development projects remains very tight. Capital flows across the region were up on Q1 volumes, and the Asia region showed further resilience with more deal flow than either Europe or the Americas as reported by RCA.

Mature markets, with perhaps the most room to adjust from their peak, will have further to move through to the end of the year. When the recovery does arrive, expected during the course of 2010, it will be uncharacteristically mild for these markets as a whole. Semi-developed markets have been comparatively stable during this downturn, and we expect their dip to be less severe than the previous cycle.

Offices

- Generally unemployment will continue to rise over the next 12 months, pressuring the office markets further. Rents will fall and vacancies will rise before markets reach their trough. However, the speed of this cyclical movement will differ between markets depending on their individual demand/supply balance. The investment markets will likely lead an occupational market recovery, and the bid ask spread has already begun to reduce. Though value declines are still expected, the rate of their decline will slow.

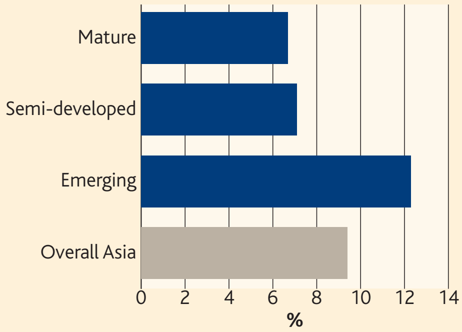
Retail

- Improving consumer confidence, continuing governmental stimulus packages and a likely steadying of tourism arrivals will ease pressure on retail rents, with values rising to reflect an improved outlook. Retailers are expected to continue to concentrate on their operational performance before investing in an expanded footprint, though opportunities to tap emerging market growth remain a priority for some.

Logistics

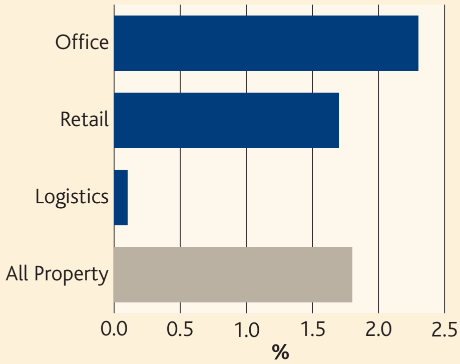
- Though a recent inventory rebuilding has supported the trade markets, a recovery in the Asian logistics sector is still tied closely to a consumer recovery in both Europe and the US. Further near term declines in values are expected, with a pick up by the end of the five year outlook.

Five year annualised total returns* prime 'All Property' (to June 2014)



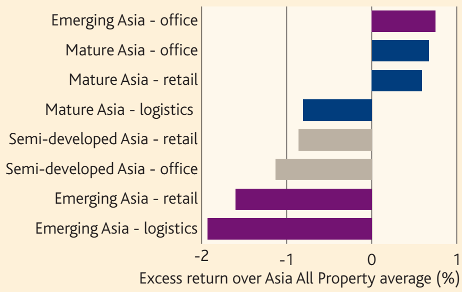
* Unleveraged returns in local currencies
Source: Aberdeen Property Investors

Five year annualised prime rental growth (to June 2014)



Source: Aberdeen Property Investors

Market pricing over five year horizon



Source: Aberdeen Property Investors

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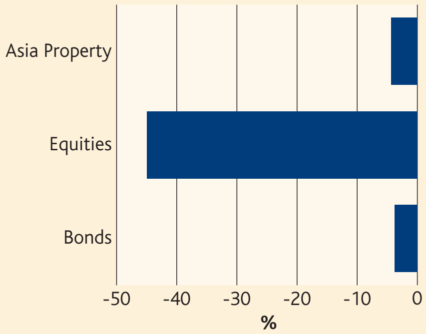
Aberdeen market view

The table below shows Aberdeen's market view, relative to the All Property benchmark (defined as the simple average of all the markets included in our analysis).

Sector	Strategy
Australia - office	Overweight
Australia - retail	Underweight
Australia - logistics	Neutral
China - office	Neutral
China - retail	Neutral
China - logistics	Neutral
Hong Kong - office	Overweight
Hong Kong - retail	Overweight
Hong Kong - logistics	Neutral
India - office	Overweight
India - retail	Overweight
Japan - office	Underweight
Malaysia - office	Underweight
Malaysia - retail	Overweight
Singapore - office	Underweight
Singapore - retail	Underweight
Singapore - logistics	Underweight
South Korea - office	Underweight
Taiwan - office	Underweight

Source: Aberdeen Property Investors

Asset classes – 12 month return performance to June 2009



Asia Property – Commercial Property return excl. Japan
Equities – MSCI Asia excl. Japan
Bonds – JPM Emerging Market Index

Source: Aberdeen Property Investors, Thompson Datastream

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