

August 2010

Asia Pacific Property Cycle Monitor

Table of Contents:

1. Economic context	2
2. Office	4
3. Retail.....	9
4. Industrial	13
5. Appendix.....	16

Executive summary

During the past six months, Deutsche Bank's forecast for global economic expansion in 2010 climbed from 4.0% in January to 4.4% at mid-year. Yet the 2010 outlook for major economies such as the US (3.3%), Japan (2.8%), and the UK (1.2%), all lag the overall global forecast while prospects for the Eurozone slipped from 1.5% to 1.0% during the same period. Pulling the global economy forward is Asia (ex-Japan), where improving consumer and business sentiments have underpinned a robust mid-year forecast of 8.5% growth in 2010, up from 7.7% at the beginning of the year. Even with China and India excluded, emerging Asian countries remain on track for a brisk 6.3% expansion this year. The post-crisis economic landscape has repositioned Asia as a source for capital to be invested in property markets abroad while Asia's domestic and intra-regional investors have displaced foreigners as the dominate investors within the Asia Pacific real estate markets. Timing is the main factor that clouds Asia's current economic outlook since much of the year's growth lies front-loaded in early 2010. As Asia's export-oriented economies struggle to find new demand in Europe and North America, the region's pace of growth will decelerate as the remainder of the year unfolds.

A swift economic start in 2010 added buoyancy to **Asia's office markets**, allowing volatile cycles like those in Hong Kong, Singapore, Shanghai, and Beijing to shift quickly into recovery. Less volatile markets like Seoul, Sydney, and Melbourne that manoeuvred through the downturn with limited construction and only modest demand disruption, have also moved into recovery. This contrasts with Tokyo and other Japanese cities where rents continue to fall. Japan remains the region's only market experiencing distressed investment transactions. In India, despite otherwise dynamic economic growth, the extensive construction pipeline in the major cities has delayed recovery prospects for at least another year in Mumbai, and perhaps longer in Delhi, Bangalore, and Chennai. Elsewhere in the Asia Pacific region, office fundamentals in Taipei, Kuala Lumpur, Manila and Bangkok point to delayed recoveries with modest to moderate rental growth.

Performance continues to improve across most of **Asia's retail markets**, especially those in Hong Kong and Shanghai where the retail cycle turned quickly and a burst of new rental growth seems likely this year. Sydney, Melbourne, Beijing, and Seoul also eased through this property cycle with less volatility than originally feared. Singapore remains a wildcard with good upside potential. Though its retail market took a sharp blow in the downturn, Singapore's supply pipeline is limited and new tourist attractions appear increasingly likely to energise demand. Substantial oversupply (Mumbai, Delhi), stagnant demand (Tokyo), and political uncertainty (Bangkok) will delay recoveries in a few markets. Looking ahead, China's 12th Five-Year Plan which will cover the years 2011 to 2016 is widely anticipated to steer the country toward a more consumption-oriented economy, which could provide a substantial boost to the region's retail demand in the coming years.

Fundamentals in **Asia's industrial markets** stabilised in early 2010, with rents down significantly from peak in a few gateway industrial markets like Singapore. The first signs of the regional industrial market's revival began to appear in the first half of 2010 as tenant demand picked up in the major markets of China and Australia. Meanwhile, softer fundamentals still linger in the industrial markets of Bangkok, Kuala Lumpur, and Tokyo.

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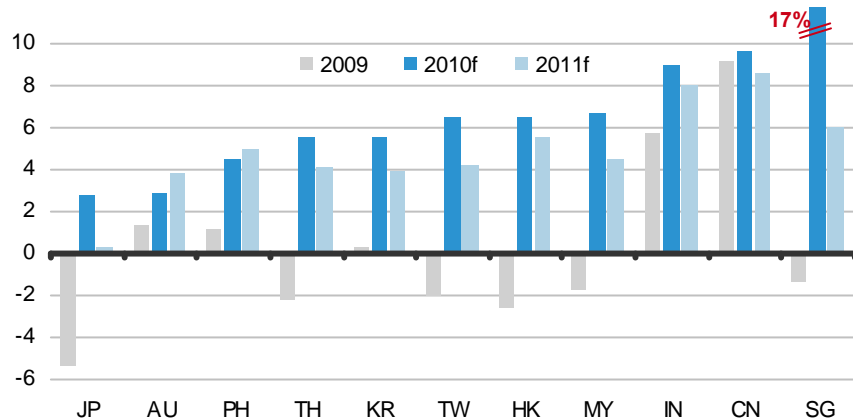
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1. Economic context

Over the past six months the outlook for global economic expansion in 2010 climbed from 4.0% in January to 4.4% at mid-year. Yet Deutsche Bank's latest 2010 forecasts for perennial economic heavyweights like the US (3.3%), Japan (2.8%), and the UK (1.2%), all lag the world outlook, and prospects for the Eurozone slipped from 1.5% to 1.0% during the first half of the year. Pulling the global economy forward is Asia (ex-Japan), where improving consumer and business sentiments have underpinned a robust mid-year forecast of 8.5% growth, up from 7.7% at the beginning of the year. Even with China and India excluded, Emerging Asia is still on track for a robust 6.3% expansion in 2010. The downside of Asia's outlook, however, is timing. Frontloaded growth in early 2010 is likely to be followed by deceleration as Asia's export-oriented economies struggle to find new demand in Europe and North America.

Exhibit 1: Real GDP growth (%)



Source: Deutsche Bank, "Asia Economics Monthly". Data as of 22 July 2010; Deutsche Bank, "Global Economic Perspective". Data as of 21 July 2010; "f": forecast

China's economy is on track to match or exceed last year's 9.1% pace. The most recent Deutsche Bank forecasts put the growth rate at near 9% for 2010 and 2011. Most economists expect significant wage inflation over the next few years, positioning China for a structural shift toward consumer-led growth. Meanwhile, China tightened restrictions on real estate lending practices earlier this year in an effort to reign in liquidity in property markets, but the actions were not fast enough to choke a supply pipeline that was already well progressed. Construction completions in May were double the levels of a year earlier even as early anecdotal evidence suggested transaction volumes may have already peaked, thus putting property markets in general at risk of oversupply as the year progresses.¹

India continues to surprise on the upside. Six months ago, forecasters expected 7.5-8.0% growth for 2010-2011, but subsequent upward revisions have shifted to the 8-9% range. The Reserve Bank of India (RBI) continues to grapple with an elevated inflation rate. Though upward price momentum has eased somewhat this spring, the risks of continued high levels of inflation will weigh on the RBI's next rate decision.

At the other end of Asia's economic spectrum lies Japan, where GDP decreased by -5.1% in 2009, a faster contraction than the Eurozone (-4.1%) and double the rate of the US. (-2.4%). A heavily front-loaded 2.8% bounce is expected for Japan in 2010, with steady economic deceleration through the remainder of the year. Japan's tenuous economic recovery has put its property market at odds with the rest of Asia and left it the only country in the region to see distressed investment transactions.

Australia will be the only major country in the region to scrape through 2010 with growth rate as slow as Japan's. The upside for Australia will be accelerating momentum that will bring its economy closer in line with other Asia Pacific countries by 2011.

¹ Deutsche Bank, Global Markets Research "Asia Economics Monthly" 15 June 2010, page 8.

Singapore is the only country in the region whose economic growth in 2010 that is likely to surpass that of China and India. Singapore, along with Hong Kong and its neighbour Malaysia, has staged an impressive recovery this year. Economic growth will approach 17.0% in Singapore in 2010 as compared to 6.5-7.0% in Malaysia and Hong Kong. With economic prospects for Europe and the US weakening, a significant reliance on exports will limit the ability of Singapore and Malaysia to sustain their recent levels of growth. This leaves Hong Kong, with its more diversified economy and its orientation toward China, positioned to emerge in 2011 with relatively strong economic performance.

While Asia experienced strong economic growth in early 2010, many countries are expected to struggle to keep up that momentum. Exports helped push Taiwan's GDP up by 13.3% over year-ago levels in the first quarter of 2010, and this unleashed a wave of private investment in the economy. While overstocked inventories may drag on the economy going forward, Taiwan could still manage to turn in 6.5% GDP growth for 2010, but this should slow further to a 4.2% pace by 2011.

The Philippines and Thailand also experienced strong first quarter economic performance of 7.3% and 12.0%, respectively. Despite a strong start to the year, Thailand's economic performance is particularly vulnerable. A resurgence of political unrest this spring will deter tourism, and drought conditions in the country's north threaten the agricultural sector in the short term. The Philippines will be better positioned to avoid a significant slowdown. It is one of only two countries in the region (Australia is the other) where forecasts point to an economic acceleration from 2010 to 2011. Across a range of indicators, including investment, consumption, inflation, and trade, the Philippines have recently delivered balanced performance.

Favourable exchange rates propped up South Korea's export sector in 2009 just enough for the country to narrowly avoid economic recession, but the country missed the bounce in momentum that many countries in the region experienced in the first quarter of 2010. According to Deutsche Bank forecasts, South Korea's economic performance for this year should still be a respectable 5.5%.

2. Office

The rousing economic start in 2010 provided a powerful boost to Asia's office markets. Most of the region's major markets have already bottomed, though a few still struggle. Distressed investment transactions in the region have been confined largely to Japan, which is the only Asian market where tenant demand is still a serious disruption to fundamentals. The Indian markets still grapple with extensive supply pipelines, and to a lesser extent so do Guangzhou, Beijing, Singapore, and Seoul.

Economic shocks can often reshuffle the roster of investors, and the financial crisis of 2008-2009 was no exception. Before the crisis, opportunities in Asia lured foreign investors into the region's property markets. The post-crisis landscape has repositioned Asia as a source for capital to be invested in property markets abroad. Meanwhile, Asia's domestic and intra-regional investors have displaced foreigners as the dominate investors in the Asia Pacific real estate markets.

Among the **Mature Asian Markets**, Hong Kong and Singapore faced the sharpest downturns in 2009. Peak-to-trough, Hong Kong's office rents fell by a third while Singapore's were cut in half. Yet sharp cycles also can turn quickly and present new upside opportunities. Initial yields have been squeezed in both markets – to below 4.0% in Hong Kong and under 4.5% in Singapore. Hong Kong's rents have already bottomed out and the recovery could come even sooner in Central, the core submarket, where supply is tighter. Much of Hong Kong's major construction activity has occurred in areas peripheral to Central, especially in West Kowloon, where significant reclamation and redevelopment efforts offer a tempting alternative for Central's financial services tenants. Despite the drop in rents, Hong Kong's vacancy rate never broke out of the single digits during the downturn, and this will ease the path to recovery. Rents are likely to resume double-digit growth this year.

Singapore's recovery seems to be lining up in tandem behind Hong Kong. Improving corporate demand and high rates of pre-commitment could well contain the vacancy rate at around 10%, moderately lower than most forecasts initially predicted. A trend toward converting existing office properties to residential use will help offset stock additions. Rents should resume growth this year, but unlike Hong Kong, double-digit growth may not kick in until 2011.

Australia narrowly avoided recession in 2009, and it is one of the few economies that is likely to gain momentum going into 2011. This will benefit the Central Business District (CBD) of Sydney and Melbourne where vacancy rates never slipped out of the single-digits. Differences in tenant demand, however, will likely cause these two markets to diverge slightly during the recovery period. Melbourne, which draws more from a diversified tenant base of a mix of international and domestic firms, is likely to outperform Sydney where tenants tend to be weighted more toward banking and financial services. Melbourne's slimmer near-term supply pipeline further positions it for rental growth that is faster and more front-loaded than Sydney's relatively steady, moderate recovery.

Among Asia's mature office markets, Seoul experienced the softest landing, with rents in the three core submarkets declining only 4-6%. Before the global financial crisis took hold, Seoul's office market was near full occupancy with a vacancy rate below 2% in 2008. Additions to stock through 2014 will add just over 1 million square meters to the market, mostly in the CBD and Yoido. Steady, secular demand growth for office space, driven by ongoing economic expansion, workforce growth, and increasingly larger workstations, should provide the basis for incremental office absorption. The balance of supply and demand should keep the vacancy rate manoeuvring within a relatively narrow band over the next three to four years. While this would leave little room for a robust recovery, it is nonetheless unlikely to negate the prospects for rental growth entirely. RREEF Research expects overall prime office rents to grow at no more than 5% p.a. from 2011-2014. Despite its low volatility, Seoul's stable, resilient demand carries the prospect for steady income returns.

Relative to the rest of the Asia Pacific region, Japan's economy took an unusually severe blow in this cycle. This put significant pressure on office rents in Tokyo, and to a lesser extent, impacted the country's secondary cities, too. Tokyo's recent era of limited construction and steady rental growth hit a crescendo in 2007. Market fundamentals began unravelling in 2008 and have yet to reach a balance. In 2010, Tokyo's office vacancy rate is on track to level off at a record 9%. Rental levels tumbled by approximately 14% in Tokyo last year and are likely to continue to soften this year and into 2011 before regaining balancing. With fundamentals in disarray, prime modern properties have shown a competitive advantage in tough market conditions.

At the peak of this cycle, offices in Tokyo commanded rents as much as double those of secondary cities. Because these secondary cities lacked significant upward momentum during the last expansion, rents in these markets now face somewhat milder corrections than Tokyo. By the time the Japanese office market bottoms out in 2011, rents in Tokyo are likely to be down more than 20% peak-to-trough compared with less than 10% in Osaka and Nagoya. Yokohama, with relatively close proximity to the Tokyo market, is likely to experience a decline of 10-15%. Ample supply pipelines in some of these secondary cities will also limit opportunities for anything more than modest rental growth in the outer years of the forecast. The Kita Yard redevelopment adjacent to Osaka Station, for example, broke ground this spring will add more than 500,000 square meters of phased office and retail space through 2013. Such projects leave Tokyo, despite its near-term demand challenges, in a better position for rental rebound when the market turns.

Most the office markets in **Emerging Asia** have begun to move into their recovery phases. Only in Guangzhou and the major Indian cities, will recovery hold back until 2011.

Tenant demand has resumed in both Beijing and Shanghai. Leasing activity picked up first in Shanghai in late 2009, with a strong rebound in Pudong, where vibrant demand will be needed to absorb the supply pipeline. Pudong draws much of its tenant strength from firms, especially financial institutions, which serve the booming Yangtze River Delta area. The Pudong and Puxi submarkets together will add nearly 2.9 million square meters between 2010 and 2014, posing a potential near-term challenge to Shanghai's otherwise vigorous rental growth.

With just over 1 million square meters of new Grade A office supply expected in 2010, Beijing's recovery may be slower to warm up than Shanghai's. Still, tenant demand has been solid with much of the strength coming from state-owned enterprises (SOEs) relocating their head offices to newer, more modern buildings in the capital city. Beijing's tenant demand should prove resilient over the forecast. As the supply pipeline slows down, rental growth should gradually accelerate toward double-digit levels by 2014.

New construction puts the timing of Guangzhou's office market recovery in jeopardy. The pipeline of new supply will peak in 2011 as more than 900,000 sqm are delivered in a market where absorption is not expected to exceed 400,000 sqm per year through 2014. The vacancy rate has already risen sharply, and could top out as high as 30% in 2011, thus holding rental growth to modest levels until late in the forecast.

Even as economists in early 2010 have kept busy continuously upgrading India's economic outlook, disarray still persists within the country's office fundamentals. A pause in India's tenant demand during the global financial crisis created an awkward opening: it allowed a rampant pipeline of office construction to take a wide lead over absorption. As prospective tenants curtailed pre-leasing of under-construction projects, backed out of pre-leases, or renegotiated existing leases, office rents quickly plunged. This disruption of demand would have been less resonant had the construction pipeline not been so sizable. In Mumbai and Delhi, rents have been cut in half from the pre-crisis peak of 2007 while rents in Bangalore and Chennai are down by 20%. Even though each of these markets will need to absorb significant construction pipelines, India's economy and political stability continue to surprise on the upside. Fundamentals should begin to realign first in Mumbai's office market, with rents to resume growth as early as 2011. The other major Indian office markets are likely to follow by 2012.

Emerging Asia's other office markets – Taipei, Kuala Lumpur, Manila, and Bangkok – have all eased through their cycles without the drama of India's supply shocks or China's resurgent demand. As a result, the timing of cyclical recovery in these markets lags Shanghai and Beijing but could well lead the Indian cities. Taipei's centrally located Xin-Yi district remains a highly favoured location with a large share of the city's Grade A stock, and at least half of the overall market's annual absorption. Tenant demand resumed in early 2010, and rents have stabilised. From 2011-2014, RREEF Research expects Xin-Yi, as well as the overall Taipei market, to manage 3-4% annual rental growth.

Kuala Lumpur's office market plans to add about 1.3 million square meters between 2010 and 2014, with two-thirds of the new stock destined for KL (city) and the remainder in the decentralised areas. Although leasing remains sluggish, the cumulative rental correction in this cycle is likely to be held below 10%. RREEF Research expects Kuala Lumpur to experience average annual rental growth of 2-5%, beginning in 2010 and continuing through the forecast window of 2014.

In Manila, developers have scaled back plans and delayed construction deliveries, thus paving the way for a speedier recovery. The Philippines is one of the few economies in Asia in which GDP growth is anticipated to accelerate in 2011. Brokers in Manila have already reported an uptick in foreign business process outsourcing (BPO) activity, which comprises a large share of the market's tenant base. Rents have already stabilised in early 2010, and RREEF Research expects the market to regain growth of 5-6% p.a. from 2011 onward.

Domestic political and economic turmoil disrupted Bangkok's office market while most of its Asian peers were still booming. Rents peaked in 2006 and only recently have they stabilised. While the supply pipeline remains modest, so does demand. Brokers reported sluggish activity in the first quarter. By the second quarter, political unrest had resurfaced again, threatening to repel both tourists and potential foreign investors. RREEF Research estimates that modest rental growth of 2-4% p.a. could be possible, barring further political or economic setbacks. Under such a scenario, rents could regain their 2006 peak toward the end of the forecast period.

Exhibit 2: Asia Pacific office market cycle

Office Market Cycle						
Emerging Markets		Forecast Years				
YE09	YE10	YE11	YE12	YE13	YE14	
GRW		GRW	GRW	GRW	GRW	GRW
PGW						
REC	REC					
CON						
GDP Growth*	6.9%	9.7%	8.1%	7.8%	8.0%	8.2%
% Vacant	17.5%	20.9%	22.0%	20.4%	16.9%	15.8%
Rent Momentum	Decrease+	Stable	Increase	Increase	Increase	Increase
Mature Markets		Forecast Years				
YE09	YE10	YE11	YE12	YE13	YE14	
GRW			GRW	GRW	GRW	GRW
PGW						
REC	REC	REC				
CON						
GDP Growth*	-3.6%	3.0%	2.1%	2.4%	2.5%	2.6%
% Vacant	8.7%	9.6%	8.8%	8.1%	7.0%	6.2%
Rent Momentum	Decrease+	Stable	Stable	Increase	Increase	Stable

* Weighted by the size of GDP at the national level in US dollar

Key: REC = Recovery GRW = Growth PGW = Post Growth CON = Contraction

Source: RREEF Research, Deutsche Bank Research, and Global Insight. Data as of August 2010

Office sector outlook

Drivers

- Tenant demand recovers as unemployment rates drop across the Asia Pacific region.
- Large yield spreads (after taxes) make Tokyo more appealing than fundamentals might suggest.
- Postponed or cancelled construction in some markets could hasten recovery.

Constraints

- Supply remains an issue throughout India as well as issue in Beijing, Singapore, and Seoul.
- Likelihood of a weaker recovery increases in major economies.
- Macroeconomic forces push long-term interest rates higher than currently expected.
- Sluggish demand persists in the lagging markets (Bangkok, Tokyo, and secondary Japanese cities).

Implications: Timing of changes

- The window of opportunity in the Australian and Singapore markets is closing fast.
- Attractive yield spreads in Japan and a steady market outlook in Korea offer investors opportunities for stable returns.

Exhibit 3: Asia Pacific Office market performance

Out-Perform	Average	Under-Perform
Singapore	Tokyo	Mumbai
Melbourne	Osaka	New Delhi
Sydney	Yokohama	Bangalore
Shanghai	Nagoya	Chennai
Beijing	Taipei	Manila
Seoul	Kuala Lumpur	Guangzhou
Hong Kong		Bangkok

Source: RREEF Research. Data as of August 2010

Exhibit 4: Asia Pacific Office market table

			Forecast				
YE 2009			2010	2011	2012	2013	2014
Emerging Markets	Stage	Contraction	Recovery	Grow th	Grow th	Grow th	Grow th
	Rent Momentum	Decrease+	Stable	Increase	Increase	Increase	Increase
Beijing	Stage	Contraction	Recovery	Grow th	Grow th	Grow th	Grow th
	Rent Momentum	Decrease+	Increase	Increase	Increase	Increase+	Increase+
Shanghai (Pudong)	Stage	Contraction	Recovery	Grow th	Grow th	Grow th	Grow th
	Rent Momentum	Decrease+	Increase+	Increase+	Increase	Increase	Increase
Shanghai (Puxi)	Stage	Contraction	Recovery	Grow th	Grow th	Grow th	Grow th
	Rent Momentum	Decrease+	Increase	Increase+	Increase	Increase	Increase
Guangzhou	Stage	Contraction	Contraction	Recovery	Grow th	Grow th	Grow th
	Rent Momentum	Decrease+	Stable	Stable	Stable	Increase	Increase
Mumbai	Stage	Contraction	Contraction	Recovery	Grow th	Grow th	Grow th
	Rent Momentum	Decrease+	Decrease	Stable	Increase	Increase+	Increase+
New Delhi	Stage	Contraction	Contraction	Recovery	Grow th	Grow th	Grow th
	Rent Momentum	Decrease+	Decrease	Stable	Increase	Increase	Increase
Bangalore	Stage	Contraction	Contraction	Recovery	Grow th	Grow th	Grow th
	Rent Momentum	Decrease+	Stable	Stable	Increase	Increase	Increase
Chennai	Stage	Contraction	Contraction	Recovery	Grow th	Grow th	Grow th
	Rent Momentum	Decrease+	Stable	Stable	Increase	Increase	Increase
Kuala Lumpur	Stage	Contraction	Recovery	Grow th	Grow th	Grow th	Grow th
	Rent Momentum	Decrease	Increase	Increase	Increase	Increase	Increase
Bangkok	Stage	Contraction	Recovery	Grow th	Grow th	Grow th	Grow th
	Rent Momentum	Decrease	Stable	Stable	Increase	Increase	Increase
Manila	Stage	Contraction	Recovery	Grow th	Grow th	Grow th	Grow th
	Rent Momentum	Decrease+	Increase	Increase	Increase	Increase	Increase
Taipei	Stage	Contraction	Recovery	Grow th	Grow th	Grow th	Grow th
	Rent Momentum	Stable	Increase	Increase	Increase	Increase	Increase
Mature Markets							
	Stage	Contraction	Contraction	Recovery	Grow th	Grow th	Grow th
	Rent Momentum	Decrease+	Decrease	Stable	Increase	Increase	Stable
Hong Kong	Stage	Contraction	Recovery	Grow th	Grow th	Grow th	Grow th
	Rent Momentum	Stable	Increase+	Increase+	Increase+	Increase	Increase
Seoul	Stage	Contraction	Recovery	Grow th	Grow th	Grow th	Grow th
	Rent Momentum	Stable	Stable	Increase	Stable	Increase	Increase
Tokyo	Stage	Contraction	Contraction	Contraction	Recovery	Grow th	Grow th
	Rent Momentum	Decrease+	Decrease+	Stable	Stable	Increase	Stable
Yokohama	Stage	Contraction	Contraction	Contraction	Recovery	Grow th	Grow th
	Rent Momentum	Decrease	Decrease+	Stable	Stable	Increase	Stable
Nagoya	Stage	Contraction	Contraction	Contraction	Recovery	Grow th	Grow th
	Rent Momentum	Stable	Decrease	Stable	Stable	Stable	Stable
Osaka	Stage	Contraction	Contraction	Contraction	Recovery	Grow th	Grow th
	Rent Momentum	Stable	Decrease	Stable	Stable	Stable	Stable
Singapore	Stage	Contraction	Recovery	Grow th	Grow th	Grow th	Grow th
	Rent Momentum	Decrease+	Increase	Increase+	Increase+	Increase+	Increase
Sydney	Stage	Contraction	Recovery	Grow th	Grow th	Grow th	Grow th
	Rent Momentum	Decrease+	Increase	Increase	Increase	Increase	Stable
Melbourne	Stage	Contraction	Recovery	Grow th	Grow th	Grow th	Grow th
	Rent Momentum	Decrease	Increase+	Increase+	Increase+	Increase	Increase

Source: RREEF Research. Data as of August 2010

3. Retail

Asia's retail property markets benefit from a convergence of positive growth factors, including rising incomes, middle-class populations, retail sales, job opportunities, and tourism flows. China could also give a boost to the region's demand in the coming years. The country's 12th Five-Year Plan which will cover the years 2011-2016 is widely anticipated to steer China toward a more consumption-oriented economy. A few of Asia's major shopping centre markets had already edged into recovery by late 2009 and more markets have now joined them in recovery in 2010.

The retail outlook for **Mature Asian Markets** has improved further in the past six months, with Hong Kong bouncing back with particular strength. Hong Kong's cumulative peak-to-trough rental losses proved marginal during the downturn. In 2010, those losses will likely be recaptured as retail rents rise by more than 10% to surpass their previous 2007 peak. Improvements in the economy, consumer sentiment, retailer interest, and tourist arrivals (especially from mainland China) should continue to boost retail demand amid a manageable construction pipeline. Rents could continue to rise by as much as 10% p.a. through 2012, but will inevitably throttle back to a slower pace.

While Hong Kong depends on China to keep tourist arrivals buoyant, Singapore must draw its tourists from farther afield. Casinos have become part of Singapore's tourism strategy and in early 2010 it introduced its first two on a massive scale. The first phase of Resorts World Sentosa opened in February with 1,350 hotel rooms and it was followed in April by Marina Bay Sands, which is adding 2,560 rooms in phases over the next year. Just ahead of these new casinos, Singapore also spruced up the Orchard Road shopping district in 2009 to welcome new visitors. The government reported in May that tourist arrivals had soared by 30% from year-ago levels. Despite a substantial dent to its economy in 2009, Singapore's retail vacancy rate never nudged above 4%. With little new supply in the pipeline, Singapore is well positioned to resume moderate, steady rental growth of 3% p.a. through 2014.

The downturn for retail property proved relatively mild in Sydney and Melbourne, where low vacancy rates, modest (and mostly pre-committed) construction, and restrictive planning laws have kept the retail markets constrained. But structural shifts are afoot as the country's two dominant supermarket chains, Coles and Woolworths, have boosted market share at the expense of smaller stores. Both domestic chains plan to add more stores over the next few years, with foreign discount chains like Costco and ALDI also reportedly interested in carving out a niche in the Australian retail food market. With Australia's economy expected to continue improving, retail rents in Sydney and Melbourne may post solid gains of 3-4% p.a. in 2010 and beyond.

Like Australia, rents in Seoul's retail market look set to grow at a similar pace of 3-4% p.a. in 2010 and beyond. While foreign fashion retailers have shown recent interest in Seoul's trendy Myeongdong shopping district, foreign property investors may find Seoul a bit more challenging to navigate. The retail stock tends to be either owner-occupied or controlled by conglomerates, and base rents closely track CPI.

Japan's retail market suffers largely on the demand side, especially at shopping centres. Tokyo's retail shopping centre rents should continue their downward slide through 2010 and into 2011. RREEF Research expects the market to recover by 2012 with the opportunity for moderate rental growth in the range of 2-4% p.a. On the other hand, rents at major high streets in Tokyo are showing signs of levelling off, due partly to the increase of Chinese tourists. In Ginza, one of the main shopping districts in Tokyo, the prime high street rents increased for the first time in seven quarters while the average rents kept dropping marginally in the first quarter 2010. RREEF Research expects high street rents in Tokyo to recover by 2011 with healthier rental growth, 4-6% p.a., than suburban shopping centres.

Rising levels of affluence in **Emerging Asian Markets**, especially China and India, have lured retail developers who anticipate a continuously expanding pool of new consumers. During the recent global downturn Shanghai's retail market proved particularly adept at minimising disruptions to shopping centre fundamentals. Construction delays and postponements kept the supply pipeline at bay through the crisis, and Shanghai's retail rents continued to rise marginally in 2009. The strength of the market continues to attract major foreign chains, including Lotte (South Korea),

Wal-Mart (US), and Carrefour (France); meanwhile the Chinese supermarket chain Lianhua has plans for 500 new stores in the Yangtze River Delta region. With a boost from the World Expo, Shanghai's rents could feasibly rise by up to 10% this year, but after 2010 rental growth will ease back to a rate of 5-7% p.a. In Beijing, a glut of new space was expected to cut rents as much as 10% from their 2008 peak. Indeed, the retail vacancy rate has shot up from a low of less than 3% during the Olympics to 15% in 2010, but rental levels have lost less ground than expected. As a result, Beijing's retail market has already stabilised. RREEF Research estimates that the market could see rental growth of 5-8% p.a. from 2010-2014.

Ample construction in India's major cities undermined fundamentals during this cycle, especially in Mumbai and Delhi, where rents have been cut by as much as 50% since peaking in 2007. Initially, the global economic crisis created an atmosphere of uncertainty that put many retailers on the sideline, waiting to see how it would all shake out. With India's economy now growing again at a record pace, several chains including Carrefour and Cartier (both of France), Gap (US), Godrej (India), and Yishion (China) have reportedly begun dusting off their expansion plans. Even with a heavy supply pipeline, demand will be strong in Delhi and Mumbai. RREEF Research expects that by 2012 rents in both markets could revert to annual growth rates near 5%. Initial yields, however, will remain among the highest of Asia's major retail markets.

Retail fundamentals in the rest of Asia show neither the volatility of Mumbai and Delhi nor the resilience of Shanghai. Fundamentals instead lie somewhere in between. Taipei saw rents peeled back about 20% from their 2007 peak amid weak domestic demand. But as the Taiwanese economy has roared back to life, retail rents have stabilised. Taipei's rental growth will be marginal this year but a gradual acceleration over the forecast could push rental growth to 5% or more by 2013. In Kuala Lumpur, a moderate supply of new suburban shopping centre space and modest consumer demand will likely keep rental growth in the range of 3-4% p.a. in the years ahead. Bangkok's retail market has stabilised and rents are unlikely to lose any further ground in 2010, but the chances for a boost in tourism arrivals this year were probably dashed by the political unrest this spring. As a result, retail rents are unlikely to rebound until 2011, and growth will likely be held below 3% p.a. for the next few years.

Exhibit 5: Asia Pacific Retail market cycle

Retail Market Cycle						
Emerging Markets		Forecast Years				
YE09		YE10	YE11	YE12	YE13	YE14
GRW	PGW		GRW		GRW	
REC	CON	REC				
GDP Growth*	6.9%	9.7%	8.1%	7.8%	8.0%	8.2%
GDP Per Capita *	5,635	6,407	7,106	7,938	8,733	9,566
Rent Momentum	Decrease+	Stable	Increase	Increase	Increase	Increase+

Mature Markets		Forecast Years				
YE09		YE10	YE11	YE12	YE13	YE14
GRW	PGW		GRW		GRW	
REC	CON	REC				
GDP Growth*	-3.6%	3.0%	2.1%	2.4%	2.5%	2.6%
GDP Per Capita *	34,108	39,084	41,226	43,890	46,362	48,587
Rent Momentum	Stable	Stable	Increase	Increase	Increase	Increase

* Weighted by the size of GDP at the national level in US dollar

Key: REC = Recovery GRW = Growth PGW = Post Growth CON = Contraction

Source: RREEF Research, Deutsche Bank Research, and Global Insight. Data as of August 2010

Retail sector outlook

Drivers

- Above-average GDP growth continues to expand middle-class populations in China, India, and parts of Southeast Asia.
- Intra-regional tourism surprises on the upside in Taiwan, Singapore, and Hong Kong.
- International retailers continue to expand their presence across the Asia Pacific markets.

Constraints

- Income growth and retail demand languish in Japan.
- Floundering economic recoveries in Europe and the US place a drag on Asia's performance.

Implications: Timing of changes

- Peak-to-trough rental levels decline most in Mumbai and Delhi, giving these markets good upside potential for later recoveries.
- Early, rapid rental recoveries in Hong Kong and Shanghai to decelerate after 2010.
- Singapore rolled the dice in 2010, opening two new resort/casino complexes in a bid to boost tourism.
- China's 12th Five-Year Plan which will cover the years 2011-2016 is widely anticipated to steer the country toward a more consumption-oriented economy in the years ahead.

Exhibit 6: Asia Pacific Retail market performance

Out-Perform	Average	Under-Perform
Hong Kong	Taipei	New Delhi
Singapore	Beijing	Mumbai
Sydney	Kuala Lumpur	Tokyo
Melbourne	Bangkok	
Shanghai	Seoul	

Source: RREEF Research. Data as of August 2010

Exhibit 7: Asia Pacific Retail market table

			Forecast				
		YE 2009	2010	2011	2012	2013	2014
Emerging Markets	Stage	Contraction	Recovery	Growth	Growth	Growth	Growth
	Rent Momentum	Decrease+	Stable	Increase	Increase	Increase	Increase+
Beijing	Stage	Recovery	Growth	Growth	Growth	Growth	Growth
	Rent Momentum	Decrease	Stable	Increase+	Increase+	Increase+	Increase+
Shanghai	Stage	Recovery	Growth	Growth	Growth	Growth	Growth
	Rent Momentum	Increase	Increase+	Increase+	Increase+	Increase+	Increase+
Mumbai	Stage	Contraction	Contraction	Recovery	Growth	Growth	Growth
	Rent Momentum	Decrease+	Decrease	Stable	Increase+	Increase+	Increase+
New Delhi	Stage	Contraction	Contraction	Recovery	Growth	Growth	Growth
	Rent Momentum	Decrease+	Decrease+	Stable	Increase+	Increase+	Increase+
Kuala Lumpur	Stage	Contraction	Recovery	Growth	Growth	Growth	Growth
	Rent Momentum	Decrease	Increase	Increase	Increase	Increase	Increase
Bangkok	Stage	Contraction	Recovery	Growth	Growth	Growth	Growth
	Rent Momentum	Decrease	Stable	Increase	Increase	Stable	Stable
Taipei	Stage	Contraction	Recovery	Growth	Growth	Growth	Growth
	Rent Momentum	Decrease+	Stable	Increase	Increase	Increase+	Increase+
Mature Markets	Stage	Contraction	Recovery	Growth	Growth	Growth	Growth
	Rent Momentum	Stable	Stable	Increase	Increase	Increase	Increase
Hong Kong	Stage	Contraction	Recovery	Growth	Growth	Growth	Growth
	Rent Momentum	Decrease+	Increase+	Increase+	Increase+	Increase+	Decrease
Seoul	Stage	Recovery	Growth	Growth	Growth	Growth	Growth
	Rent Momentum	Increase+	Increase	Increase	Increase	Increase	Increase
Tokyo	Stage	Contraction	Contraction	Contraction	Recovery	Growth	Growth
	Rent Momentum	Decrease+	Decrease+	Decrease	Stable	Increase	Increase
Singapore	Stage	Contraction	Recovery	Growth	Growth	Growth	Growth
	Rent Momentum	Decrease+	Increase	Increase	Increase	Increase	Increase
Sydney	Stage	Growth	Growth	Growth	Growth	Growth	Growth
	Rent Momentum	Stable	Stable	Increase	Increase	Increase	Increase
Melbourne	Stage	Growth	Growth	Growth	Growth	Growth	Growth
	Rent Momentum	Stable	Increase	Increase	Increase	Increase	Increase

Source: RREEF Research. Data as of August 2010

4. Industrial

Fundamentals in the Asian warehouse and logistics market stabilised in early 2010. The recent global economic crisis swept through the gateway industrial markets of Singapore and Shanghai with particular intensity, cutting peak rents by double-digit levels. While demand has picked up again this year in the major cities of China and Australia, softer market conditions still linger in Tokyo.

The timing of industrial recovery in the **Mature Asian Markets** has diverged, with rents rising in some markets but still struggling in others. A favourable exchange rate worked to South Korea's advantage during the downturn and kept exports moving and distribution activities flowing. This cushioned Seoul's industrial properties with a relatively flat rent cycle. RREEF Research expects industrial rents in Seoul to resume moderate, but steady growth of up to 3% from 2010 onward. The Australian economy's soft landing has also positioned its industrial markets for relatively quick recoveries. Current construction pipelines in both Sydney and Melbourne appear manageable, with high levels of pre-commitment from industrial tenants. After peak-to-trough rental corrections of less than 10%, both cities are likely to see a moderate bounce of 3-4% rental growth in 2010 with that pace appearing sustainable through 2014.

Industrial properties in Singapore and Hong Kong are still stabilising in 2010, and rents in both markets should begin to grow again in 2011. Singapore's industrial market took the region's worst hit, with rents off by more than 40% from peak levels. Prior to the downturn, Singapore's business parks picked up spill over demand as office space became unusually tight and office rents soared. But with plenty of more competitively priced office space now available, Singapore must once again rely primarily on industrial tenants to fill its parks. Thus, the timeline for recovery is pushed out. RREEF Research expects rental growth to resume in this market by 2011 at a modest 2-3% pace that is more likely to carry through 2014.

As the primary transshipment centre for the Pearl River Delta, Hong Kong's industrial market draws its tenants from freight forwarders active throughout the region. Recent leasing activity from this tenant base helped stabilise rents by year-end 2009. But even as this was occurring, the market was already experiencing some degree of cap rate compression (as was Singapore). Even though tenant demand has begun to revive in early 2010, RREEF Research still projects that Hong Kong's industrial rents will stay mostly flat this year. Rental growth should resume by 2011 and continue through the next few years at a 2-5% p.a. pace.

Japan's industrial market has struggled with unbalanced fundamentals recently. Even though industrial production has risen 25% over year-ago levels, most forecasts predict a more sluggish economy going into 2011, and this will likely keep new demand from industrial tenants at bay, at least for a while. Over the longer term, there are reasons for hope. Construction levels are modest and structural changes – prompted by outsourcing, consolidation, and new environmental regulations – should eventually channel demand toward new, modern logistics facilities. For now, RREEF Research expects that Tokyo's industrial rents are more likely to lose ground in 2010 before eventually flattening in 2011. Modest growth of 2% p.a., is likely to resume by 2012.

Industrial rents have begun to improve in some of the **Emerging Asian Markets**, namely Shanghai and Beijing where tenant demand picked up briskly in the first half of 2010. Shanghai's inherent advantage as a logistics hub is its position in the Yangtze River Delta. From this location, Shanghai captures airborne and seaborne trade flowing into and out of rapidly developing areas in central China. Nevertheless, China's resilient domestic retail consumption growth provides significant opportunities for both cities. Over the longer term, the prospects for China's industrial markets is looking up. Rising levels of domestic consumption and industrial production point toward significant long-term demand for logistics and distribution facilities. This growth would be further supported by China's commitment to upgrade and expand its transportation infrastructure to a state-of-the-art status. RREEF Research projects industrial rents to begin rising this year in both Shanghai and Beijing. Net effective industrial rents in both cities are likely to expand over the next few years at a 4-6% p.a.

Among other industrial centres in Emerging Asia, rents in Bangkok continue to fall, while rents in Taipei and Kuala Lumpur have stabilised. None of these markets are likely to resume rental growth until next year, and in Kuala Lumpur, where fundamentals are relatively stagnant, industrial rents could stall in a holding pattern until as late as 2012. Rental growth in Kuala Lumpur and Bangkok is unlikely to break above a 2% p.a. pace over the next few years. Taipei, however, holds promise for a slightly stronger recovery. US-based retailer Costco, for example, announced plans in the first half of 2010 for a major expansion in Taiwan that will include a new distribution facility. As Taipei's industrial market recovers in 2011, RREEF Research estimates that rents could gradually accelerate to a 3-4% p.a. pace by 2013.

Exhibit 8: Asia Pacific industrial market cycle

Industrial Market Cycle						
Emerging Markets		Forecast Years				
YE09		YE10	YE11	YE12	YE13	YE14
GRW	PGW		GRW			
REC	CON	REC				
GDP Growth*	6.9%	9.7%	8.1%	7.8%	8.0%	8.2%
Industrial Production Growth*	8.0%	14.8%	11.3%	11.0%	10.4%	10.4%
Rent Momentum	Decrease+	Stable	Increase	Increase	Increase	Increase

Mature Markets		Forecast Years				
YE09		YE10	YE11	YE12	YE13	YE14
GRW	PGW		GRW			
REC	CON	REC				
GDP Growth*	-3.6%	3.0%	2.1%	2.4%	2.5%	2.6%
Industrial Production Growth*	-15.8%	14.5%	4.7%	5.2%	4.3%	2.2%
Rent Momentum	Decrease+	Stable	Stable	Increase	Increase	Increase

* Weighted by the size of GDP at the national level in US dollar

Key: REC = Recovery GRW = Growth PGW = Post Growth CON = Contraction

Source: RREEF Research, Deutsche Bank Research, and Global Insight. Data as of August 2010

Industrial sector outlook

Drivers

- Long-term growth and development trends underscore increasing demand for modern logistics facilities throughout the region.
- Lack of good quality warehouse and logistics properties push rental values upwards in many cities as the economy recovers.
- Limited supplies of industrial land (Singapore, Hong Kong, Tokyo) enhance the recovery prospects for a few major markets.

Constraints

- Relatively weak economic recoveries in Europe and North America delay the rebound for export-led demand in Asia.
- Lacklustre demand in Tokyo lingers longer than anticipated.
- Supply pipeline in China revives too quickly.

Implications: Timing of changes

- Tokyo expected to be the last major market to recover, but future fundamentals look solid, i.e., limited construction with structural demand for more modern product.

- Upside potential for strong recoveries in supply constrained markets with sharper cycles (Hong Kong, Singapore).

Exhibit 9: Asia Pacific Industrial market performance

Out-Perform	Average	Under-Perform
Shanghai	Kuala Lumpur	Tokyo
Beijing	Seoul	Bangkok
Sydney	Singapore	
Melbourne	Taipei	
Hong Kong		

Source: RREEF Research. Data as of August 2010

Exhibit 10: Asia Pacific Industrial market table

			Forecast				
		YE 2009	2010	2011	2012	2013	2014
Emerging Markets	Stage	Contraction	Recovery	Grow th	Grow th	Grow th	Grow th
	Rent Momentum	Decrease+	Stable	Increase	Increase	Increase	Increase
Beijing	Stage	Contraction	Recovery	Grow th	Grow th	Grow th	Grow th
	Rent Momentum	Decrease+	Increase+	Increase+	Increase	Increase	Increase
Shanghai	Stage	Contraction	Recovery	Grow th	Grow th	Grow th	Grow th
	Rent Momentum	Decrease+	Increase	Increase	Increase	Increase	Increase
Kuala Lumpur	Stage	Contraction	Recovery	Recovery	Grow th	Grow th	Grow th
	Rent Momentum	Decrease+	Stable	Stable	Stable	Stable	Stable
Bangkok	Stage	Contraction	Contraction	Recovery	Grow th	Grow th	Grow th
	Rent Momentum	Decrease+	Decrease+	Stable	Stable	Stable	Stable
Taipei	Stage	Contraction	Recovery	Grow th	Grow th	Grow th	Grow th
	Rent Momentum	Decrease+	Stable	Stable	Increase	Increase	Increase
Mature Markets	Stage	Contraction	Recovery	Grow th	Grow th	Grow th	Grow th
	Rent Momentum	Decrease+	Stable	Stable	Increase	Increase	Increase
Hong Kong	Stage	Contraction	Recovery	Grow th	Grow th	Grow th	Grow th
	Rent Momentum	Decrease+	Stable	Stable	Increase	Increase	Increase
Seoul	Stage	Contraction	Recovery	Grow th	Grow th	Grow th	Grow th
	Rent Momentum	Stable	Increase	Increase	Increase	Increase	Increase
Tokyo	Stage	Contraction	Contraction	Recovery	Grow th	Grow th	Grow th
	Rent Momentum	Decrease+	Decrease	Stable	Stable	Stable	Stable
Singapore	Stage	Contraction	Contraction	Recovery	Grow th	Grow th	Grow th
	Rent Momentum	Decrease+	Stable	Stable	Increase	Increase	Increase
Sydney	Stage	Contraction	Recovery	Grow th	Grow th	Grow th	Grow th
	Rent Momentum	Decrease+	Increase	Increase	Increase	Increase	Increase
Melbourne	Stage	Contraction	Recovery	Grow th	Grow th	Grow th	Grow th
	Rent Momentum	Decrease+	Increase	Increase	Increase	Increase	Increase

Source: RREEF Research. Data as of August 2010

5. Appendix

The existence of property cycles provides an opportunity to forecast performance based on fundamental demand and supply drivers. As with other regions, our forecasting process in Asia Pacific is based on a thorough “top-down” and “bottom-up” approach. However, data limitations and the immaturity of many markets means less reliance can be placed on econometric techniques than in the more mature markets of the US and Europe.

In addition to the limited amount of consistent, reliable market information and the low level of market maturity, the fundamental structural changes occurring in many markets also limit the relevance of econometric techniques. For these reasons, our top-down approach is based on a combination of quantitative and qualitative assessments to provide an initial projection of demand and supply drivers, vacancies and rents.

These top-down forecasts are discussed in detail with our local experts and advisors to arrive at a well-grounded “real world” view of market prospects. Such a “real world”, rather than a purely “econometric” approach, is entirely appropriate for these opaque and less mature markets. The systematic analysis of the fundamental drivers of performance for such markets produces a series of forecasts which are helpful in understanding broad trends in relative performance.

The analysis reveals that different cycles pervade across geographies in terms of degree and timing. These reflect the economic fundamentals driving demand and specific supply characteristics at the local level. This Asia Pacific Property Cycle Monitor includes forecasts for 21 cities across 11 countries in the region in the office property sector, 13 cities for the retail sector and 11 cities for the industrial sector. These markets are classified according to their respective stages in the cycle and their prospects over the coming five years.

In our European Property Cycle Monitor, geographic location is the main criteria used in distinguishing broad trends in market performance, with significant differences being experienced in “Western” and “Central/Eastern” Europe. In Asia Pacific, this approach is less suitable given the wider range in levels of market maturity across the region. As a consequence, we distinguish broad trends in performance according to the level of market maturity rather than geography.

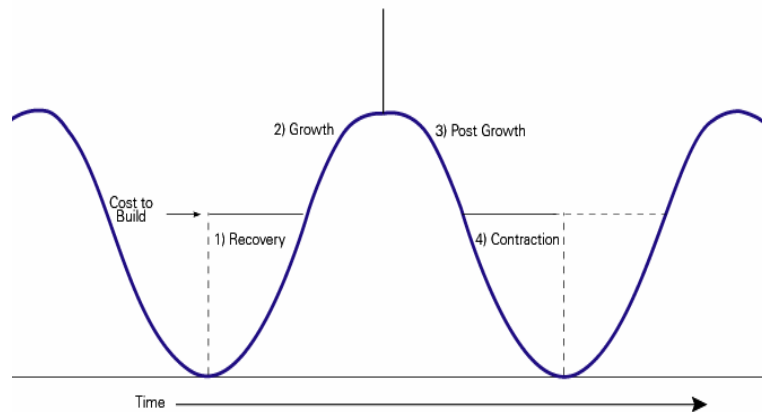
On this basis, the “Mature Asian Markets” group covers Australia, Hong Kong, Singapore, South Korea and Japan. It is clear that South Korea and Japan fall well short of the other markets in terms of their maturity, but recent changes in both markets and improvements in the institutional environment mean they are more similar to the “Mature” markets than the “Emerging” ones across the rest of the region. In contrast, China, India, Malaysia, Taiwan, Philippines and Thailand are clearly emerging markets and their behaviour, as well as the confidence that can be placed on any forecasts, need to be distinguished from the Mature group.

Given the different levels of economic maturity in Asia Pacific, two distinct market cycles are apparent. A separate cycle and overview is presented for mature and for emerging markets, together with an economic overview of the current and future prospects for each market.

Classifying the markets

Each property sector has a clearly identifiable cycle with four main phases: Recovery, Growth, Post Growth and Contraction (see Exhibit 1). The office market has the greatest volatility of the three main commercial sectors. The retail and industrial sectors are less volatile due to the relatively high levels of owner-occupation with less investment activity and limited modern supply, particularly in the industrial sector.

Exhibit 11: Property market cycle



Source: RREEF Research. Data as of August 2010

Property market cycle

Stages	General conditions
1 Recovery	High but declining vacancy rates – stable to rising rents
2 Growth	Low and declining vacancy rates – rising rents supportive of construction
3 Post Growth	Low but increasing vacancy rates – rising/flattening rents
4 Contraction	High or increasing vacancy rates – falling rents

The position in the property market cycle is based on a combination of factors including the vacancy rate relative to the individual market’s historical average, change in vacancy rate and rate of rent growth. It is important to recognise that our analysis is based on movements in “headline” prime rents as data limitations prevent the systematic comparison of effective rents across markets. In general terms, effective rents will lead the recovery of headline rents, as a reduction in incentives tends to occur a number of months ahead of any movement in headline rents.

Rent cycle

In addition to its stage in the cycle, a “rent momentum” category is assigned to each of the markets for every year of the forecast period. This rent momentum, which helps establish the rate of growth at different stages of recovery, is based on the typology displayed in Exhibit 2 (page 6). It is intended to show the general momentum behind potential changes in rent, not an absolute variation in rates.

Exhibit 12: Rent categories and the property cycle

Momentum Category	Cycle Stage			
	Contraction	Recovery	Growth	Post Growth
Increase+			√	
Increase		√	√	√
Stable	√	√	√	√
Decrease	√			√
Decrease+	√			

Source: RREEF Research. Data as of August 2010

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