

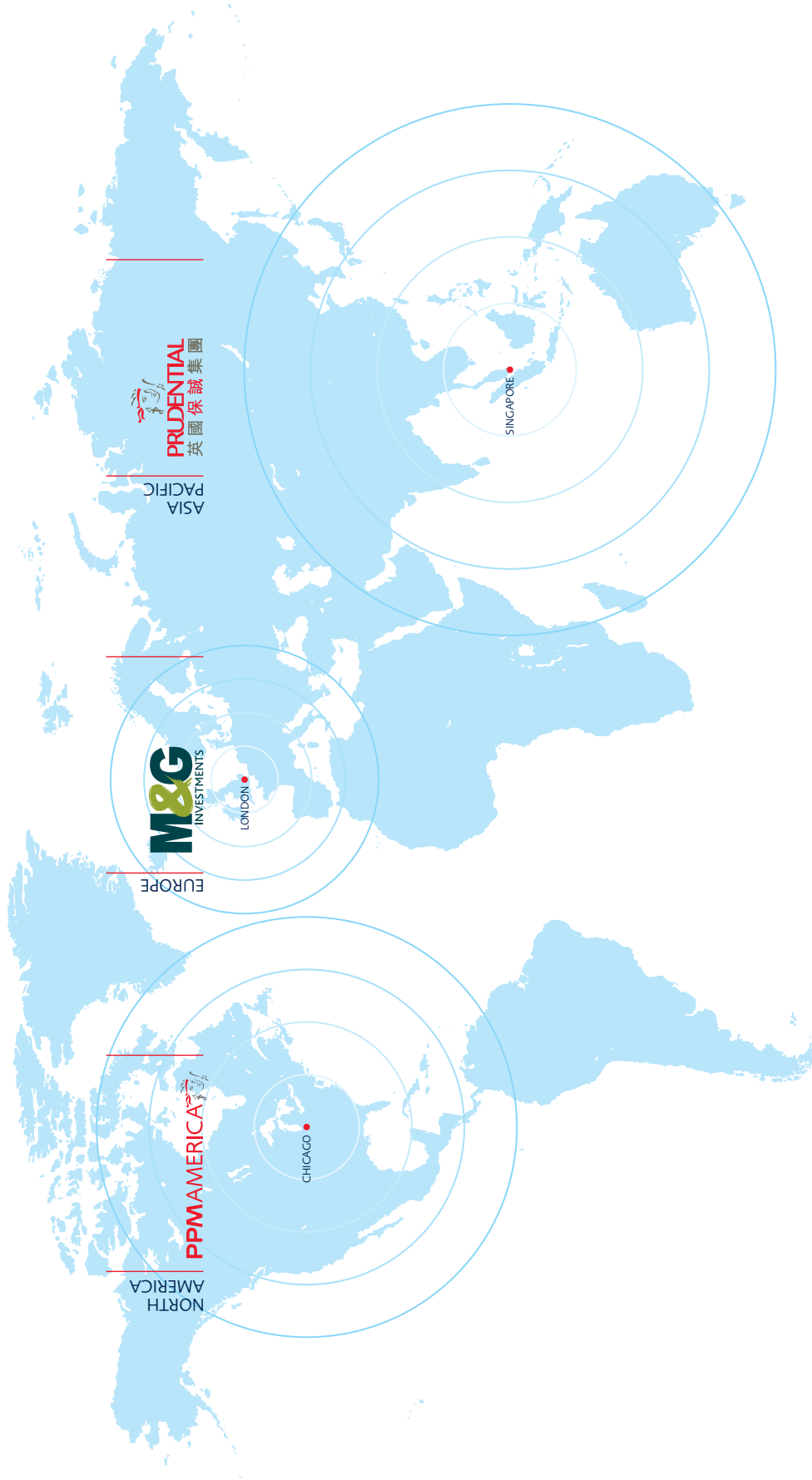
REAL ESTATE
INVESTMENT
MANAGEMENT

INTERNATIONAL
REAL ESTATE PERSPECTIVE
4TH QUARTER 2008



GLOBAL PRESENCE

PRUPIM is a significant force in UK real estate investment management and its global influence is growing rapidly.



Cities directly invested in			
Cannes	Los Angeles	Milan	Paris
Chicago	Lyon	New Jersey	San Francisco
Hong Kong	Metz	New York	Seattle
London	Miami	Ottawa	Seoul
			Singapore
			Sydney
			Toronto
			Vancouver

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ABOUT PRUPIM

PRUPIM is one of the leading real estate investment managers in the United Kingdom. We form part of the M&G Group of Companies which is the asset management arm of Prudential plc in the UK and Europe.

We manage over US\$37 billion of real estate assets, of which over US\$6 billion is invested internationally in North America, continental Europe and Asia Pacific. We are invested in over 1,000 properties with more than 6,000 property occupiers.

We manage real estate investments for a wide variety of clients, providing core services and expertise in fund management, asset management and property management. These services are offered individually, or on a fully integrated basis.

Our major activities are driven by powerful research, managed by the Global Property Research Team. Our considerable scale and diversified activities allow us to draw on our own multi-dimensional inputs which give us an unrivalled information advantage.

We evaluate the macro-economic environment working as part of the global research capability of Prudential. We receive detailed property related data generated by our on-the-ground surveyors. This is fed into proprietary modelling systems which form the basis of our analysis.

The nine-strong Global Property Research Team was formed in 1987 and is comprised of property economists and performance measurement analysts who work together to provide quality property analysis and commentary on the UK and international property markets.

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Unless otherwise specified all data and commentary is as at end September 2008.

For further information please visit our website: www.prupim.com



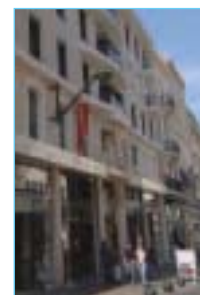
Seattle



Sydney



Los Angeles



Cannes

EXECUTIVE SUMMARY

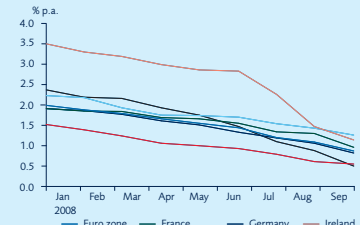
EUROPE

- Across all sectors, occupier demand is waning as most countries experience a marked economic slowdown. Unemployment levels are beginning to rise and inflation remains high, despite easing back from its record peak.
- Increased food and fuel prices are squeezing profit margins and disposable incomes alike. A sharp decline in confidence is beginning to impact on retail spending and prospects for both retail and industrials are weakening. For offices, troubles in the banking industry are exacerbating already softening demand, especially in regions

where take-up has been largely dominated by the financial sector.

- Investors remain gloomy about most European markets. Weakening rents, rising yields, a dearth of buyers and uncertainty over bank lender intentions on current loan stock are undermining confidence. Transaction volumes remain low as vendors balk at the prices that investors, who have an appetite to buy, will pay. In general, office markets are the least favoured by investors. Everywhere, there is a "flight to quality".

Evolution of European GDP Forecasts for 2009



Source: Consensus Economics (January 2008 to September 2008)

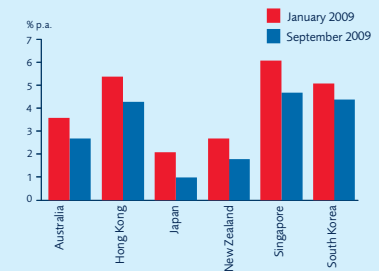
ASIA PACIFIC

- Asia is now experiencing a similar reversal in investment sentiment as other regions. Rental growth is expected to continue to slow – partly through supply delivery, but also through softening demand as Western demand for exports declines and domestic consumer and economic confidence weaken.
- That said, this weakening is more a second order effect since it has been transmitted from the West. The financial crisis itself has been felt less keenly in Asia which operates more conservative banking business

models: lending is still available, but restricted. However, the ultimate effect on the real economy will be the same, although maybe at a lesser extent.

- Australian property yields have shifted out more sharply than elsewhere in Asia. The country's economic and financial model is similar to the West and hence similar effects have been felt. Many of the Listed Property Trusts (LPTs) have property exposure in Europe and the US, which have also helped to transmit the problems to the domestic markets.

Changing GDP Forecasts for 2009 in the Asia Pacific Region



Source: Consensus Economics (January 2008 to September 2008)

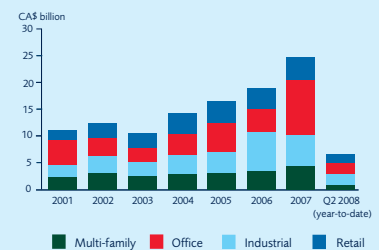
NORTH AMERICA

- The US economy has been through a very rocky time recently, with the fallout from the credit crisis intensifying to almost unprecedented levels. Many economists are now expecting at least a couple of quarters of contraction and, therefore, a recession for the US. On the positive side, inflationary pressures are waning and the (eventual) approval of the Treasury's bail-out plan should go a long way to alleviating the capital markets and thawing the freeze on lending.
- The lack of financing available to real estate investors has been the determining

factor in the commercial property downturn, although the rental market has also recently deteriorated as the economy has slowed.

- Canada's property market has also seen substantially lower transaction volumes this year, and yields have begun to move out marginally. Rental growth is moderating as demand weakens, as the economy is hit by the global financial turmoil and the US slowdown in particular.

Canadian Property Investment



Note: Only includes closed transactions of CA\$1 million+ in Vancouver (Q1 2008 only), Toronto, Calgary & Edmonton (Q1 & Q2 2008)

Source: RealNet, CB Richard Ellis, LaSalle Investment Management (September 2008)

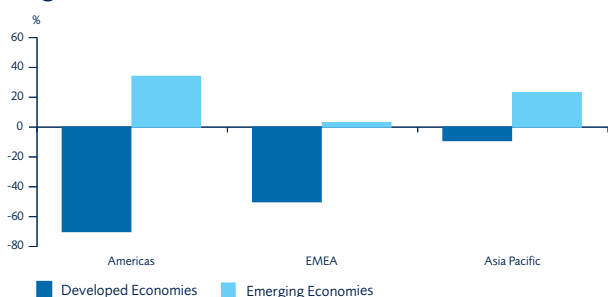
GLOBAL REVIEW

Now seen as a victim of the "credit crunch", the fortunes of commercial property markets globally are intimately tied-up with the unravelling of the financial crisis. However, over recent years, the boom in commercial property markets helped to contribute to the origins of the "credit crunch".

Loose and cheap lending practices helped inflate asset prices beyond levels justified by underlying letting fundamentals. Worse still, through appearing to deliver high and stable returns, commercial property attracted yet more capital, creating a self-fulfilling and self-energising price surge.

However, this surge was based on continuing yield compression, not on improving rentals. In mid-2007, the "music" stopped in the UK, followed shortly by Europe, North America and now Asia, and markets began to retrench. Just as institutional investors exited property, believing it to be expensive, lending for property also seized. This meant a desire to sell property was met with a much diminished appetite for buying and certainly not at the prevailing high prices. Retail investors also began to retreat from the market, forcing managers to place yet more stock on the market.

Change in Transaction Volume



Source: Real Capital Analytics (September 2008)

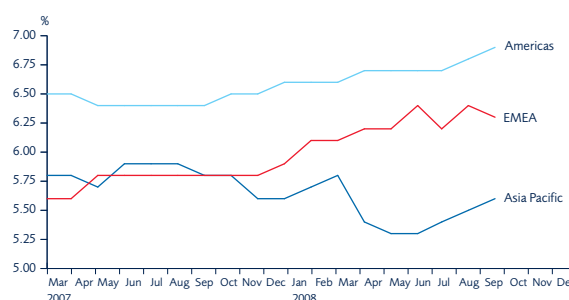
Not surprisingly, prices began to fall. This was seen first in the overstretched UK market but has since spread. Although the timing, the pace and severity of market retrenchment varies around the world, the downwards shift is universal. The UK is most way through its fall and sentinels watch eagerly for signs of life returning. Meanwhile, European and North American markets are in the midst of their correction, and the Asian markets are softening noticeably.

"The UK is most way through its fall and sentinels watch eagerly for signs of life returning. Meanwhile, European and North American markets are in the midst of their correction, and the Asian markets are softening noticeably."

Vendors everywhere seem shocked by the speed and scale of price falls and are readjusting mentally to significantly lower price regimes. Juxtaposing this against the relatively modest number of predatory

opportunists looking to drive hard bargains means transaction volumes globally are a mere fraction of 12–18 months ago; down 70% in some markets. All sellers are being treated as if they were distressed, whilst buyers using their own equity can acquire assets at discounts to those needing to first persuade their banks to lend.

Transaction Yields



Source: Real Capital Analytics (October 2008)
Note: Figures are average 90-day rolling transaction yields for office, retail and industrial properties (not consistent samples)

Not surprisingly in this environment, there is a flight to quality assets with better locations and leases: the obvious preferences for investors in a letting market beginning to feel the real economic effects of the "credit crunch". As a result, secondary or "blemished" property is now being shunned and the yield gap between quality and secondary assets is returning to its natural level and could well go further.

"...secondary or "blemished" property is now being shunned and the yield gap between quality and secondary assets is returning to its natural level and could well go further."

With the exception of the UK, which now appears fairly priced, most commercial property markets globally still seem priced to deliver returns that are not commensurate with their intrinsic risks. In the light of other demonstrably "cheap" investment opportunities, it seems natural that capital will be diverted away from global real estate markets for the next few quarters at least.

The one piece of good news is that the "credit crunch" began to unfold just at the time that investors, desperate for quality stock, began to develop their own. As such, in North America and most markets in Europe, construction pipelines did not become excessive with markets hit mainly by issues of "under-demand" rather than "over-supply". There are exceptions – mainly world office centres like London, Hong Kong and Singapore – but, overall, supply remains reasonably under control and may help foster a more timely return to rental growth in the medium term.

EUROPEAN MARKET DYNAMICS

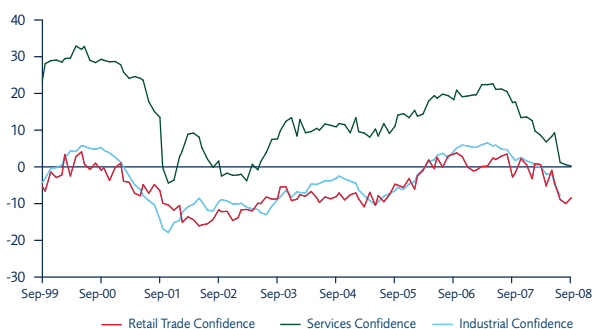
	RENTAL	INVESTMENT
Office	<ul style="list-style-type: none"> Amid the banking troubles and slowing economic activity, office employment levels are falling and demand for office space is waning, particularly in CBD office markets where take-up is dominated by the financial sector. This said, constrained supply in most markets is providing some cushioning and net stock absorption, though falling, remains positive. Spain, however, is exposed to a large supply pipeline and rental growth here has slowed substantially. 	<ul style="list-style-type: none"> Investment sentiment is generally very poor towards the office sector at present. Transaction levels have fallen dramatically. Investable stock on the market is increasing and, in the absence of many buyers, yields are rising in almost every market measured. "World city" financial centres, and markets that have seen particularly rapid yield compression in recent times, are suffering most. While these prime centres are experiencing price falls, secondary centres are suffering from an observable "flight to quality".
Retail	<ul style="list-style-type: none"> Both consumer and retailer confidence have declined rapidly. Sentiment generally has turned negative, especially in countries where residential markets are under-going a rapid pricing correction, such as Spain and Ireland. Additionally, a large shopping centre development pipeline is due to complete just as occupier demand weakens. Rental growth is slowing markedly, albeit from the high levels recorded in recent years. While prime shop rents stall, shopping centre rents are beginning to decline. 	<ul style="list-style-type: none"> Retail competes with industrials in most commentators' views of which sector might be the best performing in the next few years. However, it is not immune from market circumstances. High street units are managing to keep their prices reasonably well, but both shopping centres and retail warehouses are seeing material yield rises at present. This is not only in recently "hot" markets like Spain, but also in France, Sweden and Germany.
Industrial	<ul style="list-style-type: none"> The declining fortunes of the consumer market are impacting on trade growth, which, so far, has outstripped GDP growth but is now falling. This, combined with high fuel costs, is seeing occupier demand moderate. For now, regions supported by strong infrastructure are maintaining stable take-up and rental levels. Additionally, the sector benefits from an elastic pipeline that is able to respond swiftly to changes in demand, helping to limit the extent of rental decline. 	<ul style="list-style-type: none"> Despite remaining valued for its defensive high-yield qualities, yields are now rising in industrial property markets across Europe. In general, yield increases over the year are expected to be around 25 to 30 basis points. However, in line with its other sectors, Norwegian industrial yields have risen significantly, as they have in Spain too. Trading remains thin for European industrials with approximately €1–2 million transacted per month.
Residential	<ul style="list-style-type: none"> Housing markets across the region are decelerating with house sales slumping and mortgage approvals plunging. Spain and Ireland are most at risk as their housing markets undergo a rapid pricing correction, whilst suffering from excess supply. On the upside, with banks restricting mortgage lending and expectations for house prices downbeat, short-term prospects for the rental market are improving as potential buyers opt for rental accommodation until signs of a recovery start to emerge. 	<ul style="list-style-type: none"> The reversal of several years of strong house price inflation is seeing house price growth fall sharply in Spain while, in Ireland, house prices are now in freefall. In contrast, Germany, having seen very little house price growth, is least at risk to the pricing correction. With a "flight to safety" approach, banks are tightening their lending conditions, demanding larger deposits at the same time as pushing mortgage rates up.

EUROPEAN OUTLOOK

The impact of the financial crisis deepened further over the third quarter of 2008 as banks collapsed and government bail-outs reached unparalleled levels. Fortis and Glitnir were part nationalised, while Dexia was rescued by a government cash injection. Meanwhile, Germany's second largest property lender, Hypo Real Estate, received €35 billion in credit guarantees from their government and banks.

Investors' confidence plunged amid uncertainty over Europe's unified rescue approach after governments agreed to a co-ordinated response, but followed with individual actions. Germany unilaterally announced that it would guarantee all retail deposits, following Ireland's earlier move to guarantee all deposits in six of its banks. Other governments are quickly following suit, amid fears of a cross-border flight of capital to more secure banks.

Confidence Weakens in All Areas



Source: Bloomberg (September 2008)

With a tighter squeeze on financial market conditions, the repercussions for corporate investment, consumer spending and household borrowing have become gloomier. The effective closure of the money markets and the housing markets' universal slowdown, have sapped all confidence out of the economy. Economic growth in Europe has slowed substantially and there are growing concerns that the economy is teetering on the brink of a recession. With downside risks to growth being a primary concern, the European Central Bank loosened its hawkish stance on interest rates and cut rates by 50 basis points to 3.75%, the first rate cut in more than five years.

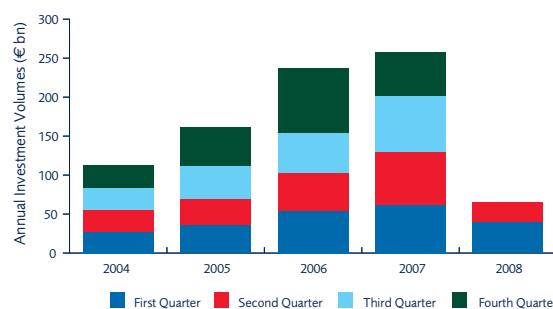
"The CMBS market effectively remains seized. There is evidence of some new funds being raised to invest in property. However, the reluctance of vendors to sell for the prices at which such opportunists might consider buying has meant that the level of market transactions has diminished dramatically."

Against this backdrop, occupier demand has weakened across all sectors. Offices, in particular, are exposed to the rapid demise of the financial sector, whilst retail is vulnerable to a consumer slowdown linked to falling housing markets, especially in Spain and Ireland. Industrials, meanwhile, are at risk from slowing manufacturing and

industrial output. As such, demand is falling from high levels. While offices and industrials will be cushioned by relatively modest supply, retail will be hit by a glut of shopping centre space coinciding with slowing demand. Rental growth is expected to ease back from high levels. In the short term, offices will suffer the largest rental decline, whilst industrial rents will stall. Only modest rental decline is expected in some retail locations, such as Spain.

Investment market conditions are also continuing to weaken across the mature property markets of Western Europe. The scarcity of debt, and the high costs of the limited amount that is available, have dramatically reduced the involvement of leveraged buyers in the markets. The CMBS market effectively remains seized. There is evidence of some new funds being raised to invest in property. However, the reluctance of vendors to sell for the prices at which such opportunists might consider buying has meant that the level of market transactions has diminished dramatically. The numbers vary by both country, sector and, indeed, market commentator, but transaction volumes are now 35–50% lower than last year in most markets across Western Europe. Both domestic and cross-border investment levels are down dramatically on recent levels.

European Investment Volumes (2004 to 2008)



Source: Cushman & Wakefield, KTI and PropertyData (September 2008)

Without question, secondary markets are suffering larger yield rises than prime markets. Investors with capital have more choice and are now much more selective about what they buy. They can buy good assets, with limited risk, at prices that have not been seen for some time. As such, they have no need to involve themselves with secondary assets. If they do, they are demanding material discounts.

Investor sentiment remains gloomy with concerns about whether a reluctance to roll over bank loans could lead to material levels of new stock being placed onto an already anaemic market. Furthermore, the existence of better priced alternative investments to direct property may lead to capital being diverted away from the market for some time to come.

ASIA PACIFIC MARKET DYNAMICS

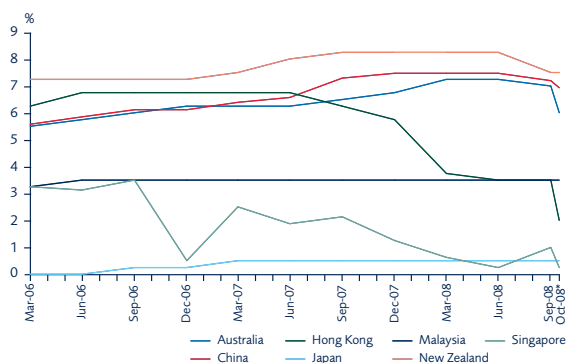
	RENTAL	INVESTMENT
Office	<ul style="list-style-type: none"> Rents are softening in the once booming markets of Tokyo and Singapore as the expansion plans of financial and business services firms are being postponed or abandoned. Secondary space, particularly in Singapore, is expected to suffer the most as occupiers will be able to trade up at little cost once supply of new space comes on line. Whilst activity is being scaled back in response to greater uncertainty and risk aversion, it is unlikely that we will see the level of failure and redundancies seen in the West due to better corporate capitalisation in Asia. 	<ul style="list-style-type: none"> Rental growth in most office markets is expected to fall over the next couple of years: lack of affordability and oncoming supply has been exacerbated by the problems in the financial markets. Prime assets are holding up reasonably well in Tokyo, but those in secondary locations have suffered from a reversal in banks appetite for lending on non-prime assets. In Singapore, the financial crisis is coinciding with delivery of a large amount of supply in the near future, which is denting investor interest in the market.
Retail	<ul style="list-style-type: none"> Consumer confidence is weakening across the region in reaction to the ongoing financial crisis. In Australia, Hong Kong and Tokyo, residential property prices are falling – a particularly potent leading indicator of negative consumer spending. Employment markets are still relatively tight, which is helping to provide a counter balance. Despite this, retailers are becoming more cautious about their expansion plans and there are growing signs of resistance to accept rental increases. 	<ul style="list-style-type: none"> Yields have shifted out strongly in the retail sector in Australia: falling house prices, weakening consumer confidence, rising finance costs and general uncertainty have led to a huge turnaround in investment sentiment. To a lesser extent, similar trends have been felt elsewhere in Asia. The Japanese market has probably felt the effects most keenly after Australia. Highly leveraged investors have suffered from tightening credit conditions and there have been some fire sales of off-prime assets.
Industrial	<ul style="list-style-type: none"> High energy costs, falling exports and generally weaker demand have affected industrial occupiers in Asia, leading to a reduced capacity for tenants to afford rental increases. However, a lack of quality logistics space in certain developing markets, and a structural shortage in more developed markets, should provide sound long-term fundamentals, although weaker demand conditions will dominate in the short term and lead to more muted rental growth. 	<ul style="list-style-type: none"> Yields are beginning to drift out in the industrial sector. Less certain rental growth prospects, and the problems with finding financing, have softened investment demand. Activity is drying up in the REIT sector in Singapore and Japan. In Singapore, the business park sector may look exposed over the next couple of years as a significant delivery of prime office supply comes on stream in the near future, removing this utility as office overspill.
Residential	<ul style="list-style-type: none"> With the Hong Kong economy weakening, demand for mass residential units has softened. This market is, however, dominated by sales rather than rentals. In the high end residential market, leasing demand remains fairly robust as multinationals still seek to place high level executives in Hong Kong. The Singapore market is looking weaker. There is a significant amount of supply expected in the next couple of years. The volume of lease renewals has weakened, particularly for smaller units. 	<ul style="list-style-type: none"> The Singapore and Hong Kong markets were trading at very low yields after they experienced a strong run up in prices based on robust consumer confidence. Investment sentiment in the residential sector has now started to turn sharply, both in these market and others across the region. House prices in Australia are starting to fall after a sustained bull run and, in Tokyo, Singapore and Hong Kong, residential prices are moving in the same direction.

ASIA PACIFIC OUTLOOK

Far from easing, the impact of the "credit crunch" seems to be worsening. The levels of corporate failure in the financial sector and government bail-outs are unprecedented since the Great Depression. However, although Asia is by no means immune to the effects of the "credit crunch", the effects do seem to be less severe than in the West.

Asian banks have suffered write-downs over the past year, but the level of corporate failure in the sector has been lower than elsewhere in the world. Asian financial institutions seem better capitalised than their Western counterparts and appear to be more liquid. Therefore, the risk of failure seems lower. That said, banks have restricted their lending criteria, requiring much more conservative loan to value ratios and applying higher margins on lending rates. Loans are now rarely made outside of well established relationships or outside of core/vanilla assets. This means that the level of funding available is much lower and hence, there are far fewer players in the property investment market. Some areas of the market are suffering more than most: lending on secondary assets or development funding has dried up almost completely.

Central Bank Rates



Source: Bloomberg (October 2008)
* Note: The latest data point is 15 October 2008

Under these conditions, yields are drifting out and property prices are falling. The reversal in investment sentiment has been most profound in Australia where yield shift has been significant. It is not surprising that the reaction of the Australian property market to the credit crisis has been most like that of the UK, given the similar structural features of high-levels of gearing and significance of unitised funds and LPTs. Heavy reliance on debt, and a requirement to mark-to-market frequently, creates a heady mix under these conditions.

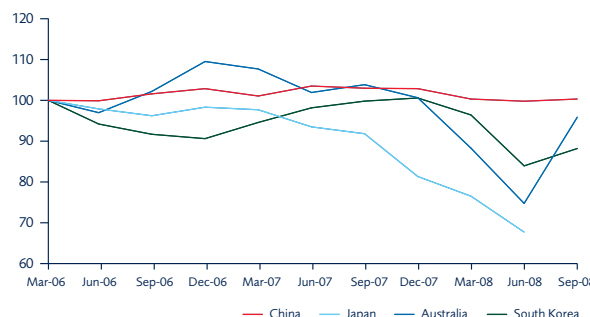
Against this backdrop, it seems difficult to identify the factor that will eventually act as the stabiliser in this unbalanced market. Investment demand has to come from one of two areas; debt funded investors or those lucky enough at the moment to be equity-backed. For debt based investors to return, either lending rates, and/or wider lending criteria, need to be relaxed, allowing current pricing to stand up as attractive, or prices must continue to fall until required returns can be achieved under such lending criteria.

The other alternative is that a wave of demand from equity-backed investors enters the market. There has been much talk of war chests of equity from Sovereign Wealth Funds, and other equity based investors, waiting on the sidelines. There seems to be little evidence of these investors actually committing funds to direct property though. Following massive sell-offs in equity and fixed income markets, property looks expensive in comparison. It seems more likely that this money would be targeted to listed equity to fill their property allocations in the short term. For these investors too, it seems prices will have to fall further to tempt them back to the market.

"Following massive sell-offs in equity and fixed income markets, property looks expensive in comparison."

Prospective returns into the long run look to be stable over the last quarter, as weakening growth expectations have been offset by yield shift meaning that the future, although expected to be worse, can be bought more cheaply. However, in these uncertain times, there is more uncertainty over those growth forecasts. Although supply conditions remain on the whole favourable, the demand side of the equation does appear to be weakening. This phenomenon is only just appearing in official data and so, up until now, growth expectations have been downgraded on the back of sentiment rather than hard facts. With sentiment worsening with each stockmarket slide, and each new piece of economic data looking more gloomy than the last, it seems likely the growth side of the investment equation will weaken further, leading to still weaker sentiment.

Consumer Confidence Surveys



Source: Bloomberg (September 2008)

NORTH AMERICA MARKET DYNAMICS

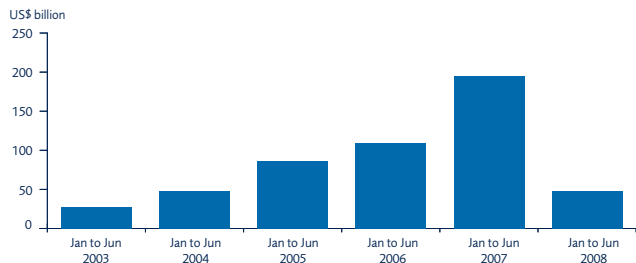
	RENTAL	INVESTMENT
Office	<ul style="list-style-type: none"> ■ The financial turmoil, and associated job losses, have contributed to falling demand for office space in the US. While vacancy rates are rising, the supply of space is relatively constrained as construction has been fairly subdued. Dramatic rental declines are not expected. ■ The Canadian office market remains relatively resilient, with stable demand and modest supply. Rental growth is expected to remain positive in the short term but may weaken by 2010 when new supply hits the market. 	<ul style="list-style-type: none"> ■ "Trophy" prime assets in the best markets in the US have seen the least falls in pricing, while cap rates for more secondary assets have risen much further. Offices continue to see the most transactions of the sectors. ■ Offices continue to be the strongest performing sector in the IPD Canadian Index, providing an annualised total return of 17.4% over the first half of 2008. Nevertheless, the edging up of yields in some sub-markets suggests weakening investment sentiment.
Retail	<ul style="list-style-type: none"> ■ With US consumers cutting back on spending, retailers are suffering. Take-up of space has weakened while delivery of new supply has continued, albeit at fairly moderate levels. Vacancy rates are rising fairly rapidly, and rental growth is expected to halt, with some strip centres already seeing falling rents. ■ Canada's retail fundamentals remain fairly healthy, with vacancy rates broadly stable. However, softening consumer confidence and weakening economic growth are taking their toll, implying moderating rental growth going forward. 	<ul style="list-style-type: none"> ■ Investor sentiment has deteriorated for US retail assets, as fundamentals have weakened. With the outlook for the housing market still poor, and the squeeze on consumers set to continue, rental growth prospects, particularly for open-air retail, have worsened; this is being priced in by investors. ■ Canadian retail yields are now edging up marginally as retail sales weaken. However, sound fundamentals will continue to support market sentiment and yield expansion is expected to be subdued.
Industrial	<ul style="list-style-type: none"> ■ Though new supply of US warehousing is slowing, vacancy rates have continued to rise as demand for space has fallen due to imports weakening. Rents are not expected to keep pace with inflation, with some markets seeing negative rental growth. ■ In Canada, industrial fundamentals continue to soften. Vacancy rates are slowly rising as new supply has exceeded absorption, especially in the manufacturing-driven Eastern markets. In general, rents are expected to remain flat in the short term. 	<ul style="list-style-type: none"> ■ Industrial assets in the US have seen cap rates rise as investor sentiment has weakened and financing has been harder to source. As such, smaller assets are currently being targeted more. ■ The Canadian industrial property market has been affected by constrained export activity and slowing economic growth. In general, yields are rising slowly, with the Western markets expected to hold up better than the Central and Eastern markets.
Residential	<ul style="list-style-type: none"> ■ Despite the housing slump in the US, it remains more economically attractive to rent accommodation rather than buy. Long-term prospects for rental growth remain, with population growth continuing and one million new households being formed each year. ■ Less favourable economic conditions and lower affordability for Canadian homebuyers are pushing people to stay in rented accommodation, helping to boost rental market demand. Rents are expected to rise, especially in the Western provinces. 	<ul style="list-style-type: none"> ■ The housing slump continues, although it is hoped that the US Treasury's financial rescue plan will put a floor under the market and prices will bottom out. Long-term value continues to improve, though investors are yet to re-enter the market. ■ The Canadian residential market continues to soften, mainly due to tighter credit conditions and weakened buyer demand, rather than significant oversupply. Many of the previously "hot" markets have become more balanced as buyers' worries of overheating have grown.

NORTH AMERICA OUTLOOK

The third quarter of 2008 has been extremely rocky for the US economy as the fallout from the credit crisis intensified to almost unprecedented levels during September. A torrent of bad financial news dominated the headlines almost daily: the government bail-outs of mortgage lenders Fannie Mae and Freddie Mac and insurance company AIG; the collapse of the investment bank Lehman Brothers and the buyouts of Merrill Lynch and Wachovia; the failure of Washington Mutual bank; the initial rejection of the US Treasury's \$700bn financial rescue package; and plummeting stockmarkets.

The impact on the wider economy from the financial crisis is still far from clear, although sentiment has certainly deteriorated. With so much bad news, it is easy to gloss over the fact that economic growth for the second quarter of 2008 was very robust, being 2.8% on an annualised basis. The government's one-off tax rebates to households boosted spending, but exports really drove growth, helped by the weak US dollar and relatively strong global economy. This said, growth throughout the second half of the year and into 2009 is expected to be far weaker as these forces diminish, the housing slump continues and the financial turmoil impacts on job losses and investment. Many economists are expecting at least a couple of quarters of contraction and, therefore, a recession for the US.

US Sales Volume (Transactions > US\$25m) January to June (2003 – 2008)



Source: Real Capital Analytics (September 2008)

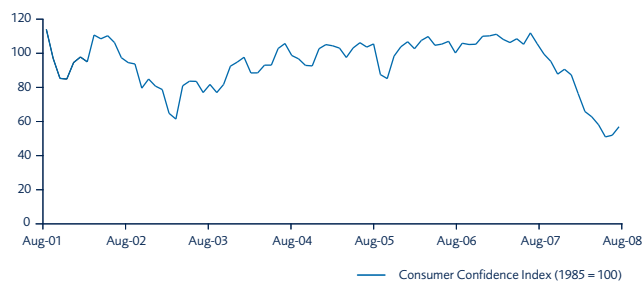
On the positive side, inflationary pressures are waning as the price of oil, and other commodities, falls from record highs, reducing the squeeze on consumers and businesses. This gives the Federal Reserve more room for manoeuvre in their efforts to stimulate the economy. The (eventual) approval of the Treasury's bail-out plan should also go a long way to alleviating the capital markets and thawing the freeze on lending.

"...the "credit crunch" is now regarded as the biggest, most influential event impacting commercial real estate investment of the last 20 years..."

The lack of financing available to real estate investors over the last year has been the determining factor in the commercial property downturn, with transaction volumes sharply down as buyers have been forced to withdraw from the market. A survey conducted by

DLA Piper reveals that the "credit crunch" is now regarded as the biggest, most influential event impacting commercial real estate investment of the last 20 years, overshadowing 9/11, the dotcom crash and the Savings and Loans crisis of 1989–1991. Prices have fallen, by less than 10% in the best markets but more in secondary ones, as cap rates have moved up. However, as many investors are not motivated to sell, many deals simply aren't happening and values are hard to pin down. On the occupier side, demand for space is clearly weakening as the economy slows, although constrained supply is supporting rents. Cap rates are expected to drift outwards rather than shift sharply, and a large amount of capital that is currently waiting in the wings is expected to enter the market once investor confidence is restored.

The US Consumer Confidence



Source: Bloomberg (September 2008)

North of the border, following a contraction of 0.2% in the first quarter of 2008, Canada's GDP grew a marginal 0.1% in the three months to June. Hit by global economic turmoil and the US slowdown, export volumes have declined and the manufacturing and primary sectors continue to struggle. Nevertheless, with the Canadian financial system relatively less exposed to debt and risky investments, a healthy labour market and still growing domestic demand, the economy is expected to perform well going forward. However, with the recent financial mayhem, there is considerable downside risk to growth in the short term.

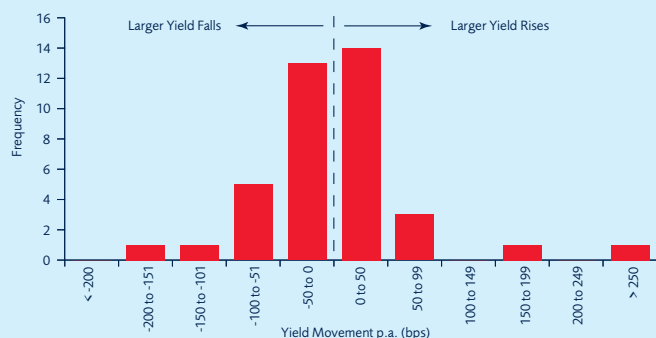
Canada's property market has seen substantially lower transaction volumes over the last year. In general, yields have started to move out marginally, although capital growth is expected to remain positive into 2009, as rents continue to rise, albeit at a moderating rate.

The recent downturn in property markets across the globe was widely expected to happen. After years of stellar performance, yields had been driven down to unsustainably low levels and property was so overpriced that many felt that a correction was inevitable. However, what has been surprising is the sharpness of that correction, particularly in the UK, which has led the rest of the world in the downswing of the property cycle. While some markets have seen yields begin to drift upwards steadily, the UK has, since the summer of 2007, seen yields shift up at a rapid pace, causing capital values to plummet.

How extreme have these yield movements been, and what were the causes? How does the current downturn compare to others that we have seen in the past? Are we witnessing a property crash?

Over the five years between 2001 and 2006, investor demand drove down UK equivalent yields by a total of more than 240 basis points to record low levels, with IPD recording an all property average of 5.37% at the end of 2006. However, a reversal of this trend around the summer of 2007 saw yields begin to rise rapidly, reaching 6.05% by the end of 2007 – a movement upwards of 68 basis points over the year. After three years of 18% plus total returns, 2007 saw the performance of the UK property market pushed into negative territory, with a -3.4% return, despite rental growth adding 4.6%. The impact on capital values from the rise in yields amounted to -11.1%.

Distribution of Annual Yield Movements (1968–2007)



Source: IPD, Jones Lang LaSalle (September 2008)

Comparing this yield movement of 68 basis points over 2007 to movements seen in the past reveals that smaller movements have been more frequent over the last 40 years, with larger movements of +/-100 basis points or more occurring on only four separate occasions. Indeed, the distribution chart above shows that movements appear to be distributed normally, resembling a bell curve with a peak frequency around zero/very little movement. With a standard deviation of 72

basis points, statistically there has been roughly 68% probability of seeing a movement between +/-72 basis points, and a 95% probability of seeing one between +/-144 basis points. In this respect, if normally distributed, 2007's yield rise of 68 basis points has not been extreme, although it has been the third highest rise seen over the last 40 years, with only the crashes of 1974 and 1990 experiencing greater shifts upwards.

"Previous periods with extreme yield movements were generally during times of very volatile rental growth..."

It is when comparing the current downturn with these two previous downturns that a question arises – are we witnessing another crash today? To answer this, we need to define what a crash entails. Unfortunately, while it is generally regarded to be a dramatic fall in a market's value, an agreed specific numerical definition does not appear to exist. If we take the definition given by Investopedia.com, "the market decline must be evidenced as a 20% drop in an index's total value", then the UK commercial property market is now technically in the throes of a crash, with capital values at the end of September 2008 (the most recent data published by IPD at the time of writing) more than 20% lower than 12 months earlier, and still falling. Of course, the UK equity market has fallen far faster in recent times, with the FTSE 100 Index recording a drop of 21% in just a single week (3rd to 10th October).

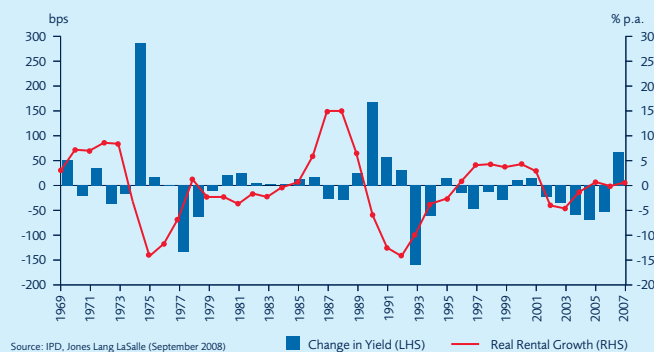
If we look at property yields so far in 2008, we see that the upward shift has extended far further than the 68 basis points over 2007. On a rolling 12-month basis, the period of September 2007 to September 2008 has seen a rise of 169 basis points, equalling the shift during 1990. In fact, due to the lower level of yields today, the last 12 months have actually seen a sharper decline in capital values due to yields rising (a yield impact of almost -24%) than during the early 1990s (-17% yield impact over the worst 12 months).

With the benefit of hindsight, it is easy to understate how unprecedented the recent dramatic rise in yields has been. Certainly yields were expected to correct, but few expected them to correct at a rate even approaching that of the early 1990s.

Previous periods with extreme yield movements were generally during times of very volatile rental growth, like in 1974 and 1990, when rental growth has peaked and begins to fall as investor demand reacts to poorer future cashflows. Conversely, when rental growth swings up from a deep trough, yields have fallen significantly (1977

and 1993). The last few years have seen relatively stable rental growth. Previous property cycles have been marked by a surge in demand for space being met by a boom in development, resulting in oversupply when demand falls back as the economy weakens. This process has resulted in a pronounced rental growth cycle, with booming rents as demand grows, followed by plunging rents during the economic downturn and period of oversupply. The last few years have seen not only a more stable economic environment, with less "boom and bust", but also a relatively constrained amount of development. As such, rents have not been particularly volatile, displaying far more stability than past cycles. Despite this, fairly significant yield movements have occurred so there seems to have been a disconnection between rental growth signals and yield movements recently.

Yield Movements and Real Rental Growth



Since the turn of the millennium, rental growth appears to have been overshadowed by the state of the capital markets in influencing investor demand for property and its pricing. In the few years before the "credit crunch" hit, capital poured into property as a "wall of money" (fuelled by increased globalisation of capital and property markets, cheap debt, and a rise in retail funds offering property investment to "the man on the street") drove down yields year-by-year.

"There seems to have been a disconnection between rental growth signals and yield movements recently. Since the turn of the millennium, rental growth has been overshadowed by the state of the capital markets in influencing investor demand for property and its pricing."

With a broader investor base today, it could be argued that the greater spread of investor requirements and motivations should have helped to provide more stability in the market. However, we have also seen larger flows of "hot money" which, combined with herding behaviour, has contributed to making the market less stable and more prone to pricing swings. In addition, with higher frequency of property valuation, improved analysis and transparency of the property market and increased prevalence of marking-to-market, there is arguably less lag in valuation indices, potentially making re-pricing sharper and quicker than historically.

"It was the arrival of the "credit crunch" that provided the driving force behind the extent of the recent rise in yields, causing extreme shifts in a relatively stable rental growth environment for the first time."

It was the arrival of the "credit crunch" that provided the driving force behind the extent of the recent rise in yields, causing extreme shifts in a relatively stable rental growth environment for the first time. Debt availability dried up, leaving many would-be property investors without financing. Debt-backed buyers withdrew from the market, unable to enter into deals, while equity-backed buyers refused to buy at such high prices. As such, demand for property fell away and yields began to rise. The continuation, and indeed intensification, of the credit crisis has meant that this trend has persisted, not helped by the natural reluctance of investors to "catch a falling knife" and re-enter the market as prices still drop.

Few people, particularly within the property market, anticipated the "credit crunch". Furthermore, with the few extreme yield movements seen historically being restricted to times of volatile rental growth, it is not surprising that many originally expected yields to correct only gradually.

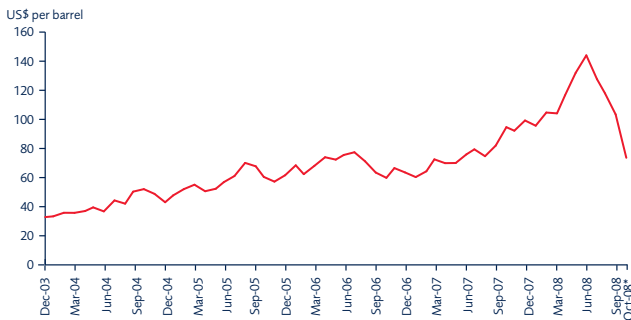
By the time the "credit crunch" struck, the UK was perhaps the most overpriced property market. Yield compression had already ended; indeed yields were beginning to edge up. Other markets globally were generally less overpriced, and were still seeing yields being driven down. Initially, in most of these markets, the "credit crunch" seemed merely to slow or halt yield compression. As the UK has corrected so much since the summer of last year, it is now priced attractively relative to other markets. Indeed, we are now beginning to see some evidence of dramatic yield rises in more countries, following Britain's lead. The UK's experience over the last year has made global property investors more aware of what they could expect.

GLOBAL OUTLOOK

Over the third quarter of 2008, the global financial crisis has gone from bad to worse, exemplified by the extraordinary events of September seeing a number of top financial institutions brought down to their knees. The "credit crunch" has entered a new phase in which credit has almost dried up in many markets, and lenders with large exposure to property debts face vital challenges.

The economies of Europe and the US are struggling and the risk of recession has increased in recent months. In contrast, though clearly affected by the current crisis, Japan – the biggest economy in Asia – came to this crisis in a much less exposed position, and like most other Asian economies, it finds itself distanced from the eye of the storm. Supported by still strong growth from economies like China and India, Asia is expected to remain relatively stable and attractive in the short term.

Easing Oil Price (US Light Crude Oil)



Source: Bloomberg (October 2008)
* Note: The latest data point is 17 October 2008

The impact of the financial crisis on the wider economy is becoming more noticeable, with rising unemployment, house price falls and lower consumer confidence taking their toll on sales. However, on the positive side, inflationary pressures are now expected to ease, as commodity prices have fallen back, and central banks may have more room to cut interest rates to support economic growth. In addition, quick and determined actions from governments should also help to stabilise the turmoil and regain economic confidence. Nevertheless, economic prospects remain gloomy: the latest forecasts by Consensus Economics in September have seen GDP growth for 2009 downgraded to less than 1% for most developed economies.

"...most markets are not suffering from oversupply, and the development pipeline is set to moderate further going forward."

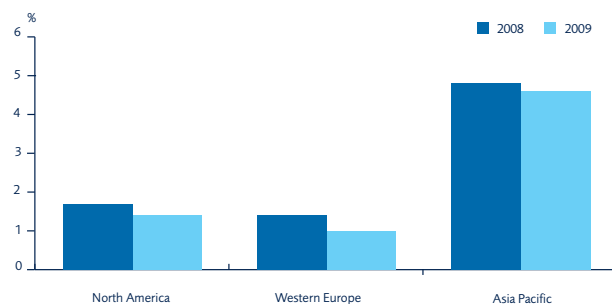
Under more pressure from declining economic conditions, especially rising unemployment and shrinking household consumption, demand for rental space is expected to further weaken. Many major markets are seeing rental growth moderating and in some cases falling. Generally, occupier markets seem to have become more favourable to

tenants, with landlords having to offer lower rents or more concessions to fill their properties.

Against the market's darkening prospects in the short term, there is some positive news. In comparison to the last downturn at the beginning of 1990s, where occupier market fundamentals were struck by both weak demand and high supply, most markets are not suffering from oversupply, and the development pipeline is set to moderate further going forward. This will certainly support rental growth, and the plunging rents seen in the early 1990s are less likely to be repeated today.

As credit market conditions worsen and lenders further reduce their risk appetite, capital available for property investment is becoming even scarcer and some debt markets have almost completely dried up. In addition, cheap investment opportunities have arisen in other asset classes, diverting capital away from property. In such an environment, transaction volumes in property are expected to remain low over the next few quarters, even in previously "hot" markets, like Singapore and Hong Kong. Clearly, with market uncertainty and economic risks appearing to be on the downside, many investors will remain on the sidelines of the property market, waiting for signs of price stabilisation before investing.

Consensus GDP Forecasts



Source: Consensus Economics (September 2008)

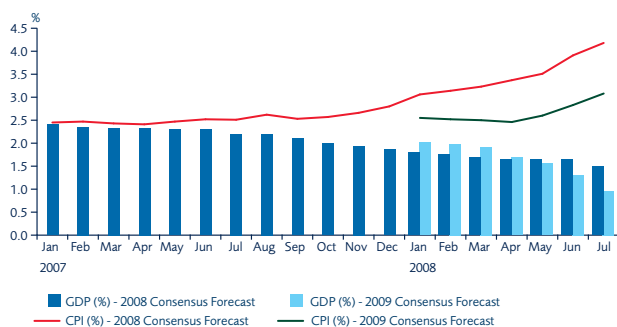
In conclusion, yields are expected to continue rising in most major markets. As the "flight to quality" phenomenon remains prevalent among investors and the prices of prime assets in core markets, such as the UK, become more attractive, secondary assets are under greater risk of re-pricing.

UK PROPERTY OUTLOOK

The second quarter of 2008 saw GDP growth stall, ending the UK's extraordinary run of 63 consecutive quarters of economic expansion. Expectations of growth have been revised downwards, with the IMF downgrading their forecasts to 0.7% for 2008 and -0.3% for 2009, significantly lower than the 1.1% it was forecasting in August, and suggesting at least a technical recession (two consecutive quarters of contraction). Slowing consumer spending, a battered financial sector and weak construction and production output are all likely to contribute to the deceleration in growth. Inflation is also a major concern, having climbed to 4.7% in September, well above the target rate. As a result, the Bank of England finds itself tasked with steering the economy through a very narrow course between inflationary pressures and lower economic growth. As global financial turmoil has intensified recently and prospects for economic growth have weakened, the likelihood of further interest rate cuts in the coming months has risen, though the Bank of England doesn't have much room to play with.

For the property market, the downturn has continued steadily throughout the year so far, and the most recent IPF Consensus forecasts, published in September, have also seen significant downgrades to returns. For 2008 and 2009, total returns now stand at -10.6% and 0.3% respectively. However, with economic and financial market sentiment having worsened in recent weeks, these forecasts already seem behind the curve. Fears are growing that banks may move against poor lending covenants to strengthen their balance sheets, which could eventually lead to a further surge of stock entering an already weak market. The property market survey, published by RICS in July, showed that market confidence is at the lowest level since the survey started in 1998. As such, analysts have downgraded their forecasts swiftly and many are now expecting total returns significantly worse than -10%, or even -15%, for 2008, before a recovery in the following couple of years. The implied returns from the derivative markets also suggest a total return of -15% for this year and -5% for the following year.

Evolution of GDP and Inflation Forecasts



Source: Consensus Economics (July 2008)

Against the potential of a prolonged economic downturn, rental market prospects have also been weakening. Negative rental growth for all property is now forecast for both this year and next. The office sector, which outperformed other sectors in terms of rental growth in recent years, is likely to be the worst occupier market along the five-year forecast horizon. Clearly, being hit hard by weak fundamentals due to significant increase in supply and sharp deterioration in demand, the Central London office, especially the City, is the major force behind the overall fall.

In the retail and industrial sectors, rental fundamentals are also weakening. Though supply, in general, isn't posing too much of a problem, it is clear that downside risks lie on the state of demand. This said, the combination of high fuel and material costs and substantially weakening retail sales will take its toll on retailers and, henceforth, rental growth prospects.

Surveyor Confidence in Occupier Sales and Lettings for the Next Quarter



Source: RICS Commercial Market Survey (Q2 2008)

In summary, evidence is mounting that, rather than being driven solely by investment sentiment, the current cycle will be more significantly impacted by the occupier market than previously thought. Nevertheless, it is worth noting that the rental market fundamentals remain better than those experienced in previous downturns.

With little sign so far of a recovery in either the economy or investor confidence, looking forward we expect yields to continue to rise before stabilising by the second half of next year. Across the board, the industrial sector looks the most attractive over the longer term, due to yields having already substantially corrected. In contrast, the Central London office segment remains gloomy, having suffered from both heavy downgrades in rental growth forecasts and adverse market sentiment. However, given the already substantial yield correction, the UK property market is now among the most attractive relative to other international markets.

GLOBAL ECONOMIC AND MARKET OUTLOOK

During the third quarter, two major developments had a big impact on global financial markets. The first was an escalation in the credit crisis which resulted in the demise of several major banks. Governments were forced to bail-out financial institutions, through massive cash injections and, in some cases, nationalisation, to help stave off a collapse in the US financial system. The impact was felt across the Atlantic Ocean when, following the failure of Lehman Brothers, barometers of financial stress rose to the highest levels in decades and lending between banks virtually ceased. In response, global stockmarkets fell significantly over the quarter as risk aversion rose and investors expected the financial crisis to plunge the world economy into a deep recession.

This gloomy outlook undermined commodity prices, the other major influence over the quarter, which fell sharply as weaker growth prospects reduced the anticipated level of future demand. This hurt the performance of mining and oil & gas shares, which, along with financial stocks, were the worst performing sectors over the quarter. However, it helped boost the returns from government bonds since it offered hope that inflation, which had been running at elevated levels in most economies, would finally decline, opening the door to interest rate cuts. In comparison to government bonds, which were seen as a safe haven amidst the stockmarket turmoil, corporate bonds suffered since default rates were expected to rise. Commercial property was also harmed by the tightening in credit, and valuations fell further during the quarter.

As we enter the last quarter of 2008, the most pressing task for governments and central banks is to restore confidence in the financial system. October has already seen significant progress on this front as governments both boosted banks' capital bases and guaranteed bank deposits. Furthermore, central banks around the world, including the Bank of England and the ECB, surprised the markets when they announced an unscheduled and coordinated series of interest rate cuts, in an effort to steady the faltering global economy.

Nonetheless, interbank lending has continued to operate at substantially higher levels than official interest rates as banks remain extremely reluctant to lend to one another. Following the authorities' moves, the first small signs of an improvement have been seen. However, there remains a long way to go before the money markets can be considered to operate in anything near a "normal" way.

With valuations in most major markets down to multi-year lows, equities are undoubtedly looking highly attractive. Most investors are

expecting the worst profit recession in 20 years – an event that is possible though unlikely. In most economies, worries about higher inflation should fall away in the coming year on the back of the fall in commodity prices. Moreover, in a number of Asian countries, governments are in a strong fiscal position, and may increase public sector spending to boost economic growth.

The downside risk for equities, therefore, is not inflation, but rather the possibility of a worse-than-expected global recession. The key is resolving the serious issues within the global banking system. Therefore, even though equities are good value at present, the worry is that earnings might still fall below expectations. From current depressed valuations, this should not necessarily be bad news as long as interest rates are falling; policymakers are taking action to get credit markets functioning again and equity markets can see "light at the end of the tunnel" for next year and beyond.

UK and European bonds are also attractive. The economic situation in both the UK and on the continent is as weak as in the US, but with inflationary pressures from commodities prices receding, there is a lot of room for policymakers to cut interest rates which should be positive for their bond markets. Furthermore, corporate bonds offer better value than government bonds, given the considerable rise in their risk premium.

Turning to commercial property, returns across the industrial, retail and office sectors are expected to converge, meaning that stock specific performance will be the central driver of returns. Commercial property yields, which rise when property prices fall, are expected to peak in 2009.

10-Year Government Bond Redemption Yields



Source: Datastream (September 2008)

FTSE World Index



Source: Datastream (September 2008)

DATA AND STATISTICS

PRIME RENTS

Region	Residential	Industrial	Office	Retail
Belgium	↔	↑	↓	↓
France	↑	↓	↓	↑
Germany	↑	↔	↔	↓
Italy	↑	↔	↑	↑
Netherlands	↑	↔	↓	↔
Spain	↑	↓	↓	↓
Sweden	↑	↓	↑	↓
Australia	↔	↔	↔	↔
Hong Kong	↑	↔	↑	↑
Japan	↔	↔	↓	↔
Singapore	↓	↔	↔	↔
South Korea	↔	↔	↔	↔
USA	↑	↔	↑	↔
Canada	↑	↑	↑	↑

Source: PRUPIM research drawing on various sources based on data available at end September 2008, reflecting recent trends

PRIME INVESTMENT YIELDS

Region	Residential	Industrial	Office	Retail
Belgium	↔	↑	↑	↔
France	↑	↑	↑	↑
Germany	↓	↑	↑	↔
Italy	↑	↑	↑	↑
Netherlands	↑↑	↑	↑	↑
Spain	↑↑	↑	↑	↑
Sweden	↑	↑	↑	↑
Australia	↑	↑	↑	↑
Hong Kong	↑	↔	↔	↔
Japan	↑	↑	↑	↔
Singapore	↑	↑	↔	↔
South Korea	↔	↔	↔	↔
USA	↑	↑	↑	↑
Canada	↑	↑	↑	↑

Source: PRUPIM research drawing on various sources based on data available at end September 2008, reflecting recent trends

Key				
Up ↑	Down ↓	Strongly up ↑↑	Strongly down ↓↓	Stable ↔

CONTACTS

CONTACTS

PRUPIM

Governor's House (Registered Office)
Laurence Pountney Hill
London EC4R 0HH

City Place House
55 Basinghall St
London EC2V 5DU

Tel 020 7548 6600

Fax 020 7548 6999

Web www.prupim.com

Sarah Chan 020 7548 6861

(Team Administrator)

KEY PEOPLE

Paul McNamara, Director, Head of Research, BSc (Hons) PhD ASIP FRSA OBE

Scott Girard, Director, Research and Strategy, PRUPIM Singapore, B.Comm MAF

Will Robson, Analyst, BA (Hons.) MSc

Richard Gwilliam, Analyst, BSc (Hons.)

Henri Vuong, Analyst, BSc (Hons.) MSc

Cuong Nguyen, Analyst, BSc (Hons.) MSc PhD

Nick Blakemore, Director, Performance Measurement

Katie Smith, Performance Analyst

Sarah Chan, Team Secretary, BA (Hons.)

ABOUT THE GLOBAL PROPERTY RESEARCH TEAM

PRUPIM's well known and widely respected Global Property Research Team, based in London and Singapore, comprises of nine staff including six property economists and two performance measurement analysts. The team engages in three main types of work namely; assessing the attractiveness of UK and international property markets, providing strategic recommendations and risk control measures for clients' funds, and conducting ad-hoc property related analyses on key issues as they emerge. The research team also assists in buy, sell and hold decisions by working closely with colleagues across PRUPIM to create a holistic approach to asset management.

BIOGRAPHIES

Paul McNamara, Director, Head of Research BSc (Hons) PhD ASIP FRSA OBE

Paul is responsible for the overall direction of property research within PRUPIM. He is also a member of the PRUPIM Board. Paul joined Prudential in 1987. He is a Visiting Professor with the Centre for Estate Management at Oxford Brookes University. Paul was appointed Chairman of the Investment Property Forum (2005-6). He is Honorary President and a past Chairman of the Society of Property Researchers and a non-executive director of IPD Holdings Limited. In June 2003, Paul was awarded an OBE in the Queen's Birthday Honours List for services to the property industry.



Scott Girard, Director, Research and Investment Strategy, PRUPIM Singapore, B.Comm MAF

Scott has been active in Asian real estate capital markets since 2002. Previously based in Korea and Japan for Jones Lang LaSalle, he has been involved at senior levels in investments, corporate finance, research and property advisory for a wide range of clients. Scott started his career in Australia in 1995 with ANZ Funds Management before moving into the consultancy business. He graduated from Curtin University of Technology with a Bachelor in Commerce and holds a Master of Applied Finance and Investment from Macquarie University.



REGULATORY INFORMATION

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Past performance is not a guide to future performance and the value of investments can fall as well as rise. Property is valued by an independent valuer. However, valuations are subjective and may vary between valuers. Commercial Property is a specialised sector and has different characteristics to investments in equities, bonds or residential property.

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PRUPIM'S GLOBAL EXPERTISE

- PRUPIM takes a disciplined approach to real estate investment management, supported by high quality research and analysis.
- We have a long history of investing directly in international property markets, which provides a depth of experience to our current operations.
- Our international operations have been built on tried and tested processes that have made us one of the UK's leading real estate investment managers.
- We benefit from the local presence of Prudential's international asset management businesses by working closely with M&G, PPM America and Prudential Corporation Asia.
- As part of Prudential, we are recognised worldwide and share a reputation for size, strength and integrity. This is a considerable advantage in developing relationships and initiating deals.
- We have established a worldwide infrastructure, partnering with the best regional advisers who bring expert local knowledge and exceptional asset management skills.
- The size of the assets we manage makes us a significant and recognised participant in the markets we invest in.
- We have developed a considerable in-house strength in structuring property deals and tax planning; processes which are critical in maximising the returns available.



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INVESTMENT
MANAGEMENT**

Prudential Property Investment Managers Limited

Governor's House (Registered Office), Laurence Pountney Hill, London EC4R 0HH
City Place House, 55 Basinghall St, London EC2V 5DU
Tel 020 7548 6600 ■ Fax 020 7548 6999

www.prupim.com