

July 2011

RREEF Global Real Estate Investment Outlook & Market Perspective 2011

Introduction

Recovery is upon us globally and parts of the world are even well into expansion. Global recovery in the property market began in late 2009, with certain markets in the Asia Pacific region and parts of Europe leading the way, and the majority of markets including those in the United States participating during 2010. Capital inflows as well as improving fundamentals led to significant appreciation in 2010 as evidenced in the returns of several real estate indices globally. Appreciation was so swift in certain markets that speculation of overheating even appeared in a few headlines. As return expectations improved across the globe, transaction volumes increased throughout 2010 and this trend is expected to accelerate throughout 2011. While much of this information is positive for the near term, the speedy and sharp recovery has caused investors to view real estate in a new light. Improved transparency and integration between the capital and fundamental operating markets is providing proof that real estate is susceptible to greater volatility now than in past cycles and not unlike that experienced by other asset classes.

Real estate fundamentals are improving globally and, with only a few exceptions, all property types and regions are in recovery. Retail assets in Asia Pacific and apartment properties in the United States are all moving into the growth part of the cycle as well. Risk to our forecasts is now balanced between the upside and downside for all regions and sectors. The recovery is expected to continue in 2011 and 2012, with expansion taking hold thereafter for most sectors and regions.

In this report, we discuss RREEF's outlook for the global core real estate market over the next five years. Aimed at the institutional investor pursuing a global core real estate investment strategy, we provide a portfolio perspective, taking into account return forecasts and, importantly, our views of risks and correlations across the three main regions highlighted within this report. Real estate investment is available in almost every region, but we have selected just a few global markets in Asia Pacific, Europe and the United States. The selected global markets are widely regarded as principal destinations for institutional real estate investors who have liquidity and transparency requirements for their investment targets. Investors will find outsized returns in many parts of the Asia Pacific region, but these investments come with greater risks, particularly given that the universe of properties is not as deep or transparent as that in Europe or the United States. European economic growth will likely slow until the future of sovereign debt becomes clearer providing some near term risk, but over time there will be attractive opportunities in its troubled economies as the crisis subsides. The United States will continue to produce appealing risk-adjusted opportunities in the near term and benefit from having a deeper investable universe. In addition to office and shopping center properties, institutional investors can invest in the industrial warehouse, R&D space and multifamily sectors in the United States.

Building a global real estate portfolio requires a view of the opportunity set by region, markets and property types. Per DTZ's Money into Property report, the current mix of the real estate invested stock across the globe is 31 percent in Asia Pacific, 32 percent in the United States and 37 percent in Europe. Throughout the report, we look at each of these regions by both market and property type. Additionally, we split Japan and Australia out from the rest of Asia Pacific, due to substantial differences between the economies and real estate markets of these two countries and the rest of Asia, creating five geographical areas for analysis - Asia, Japan, Australia, United States and Europe. The result of the analysis of the regions, sub-regions and property sectors is the framework for a global, core-oriented model real estate portfolio.

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1. Executive Summary

- **Global Portfolio Considerations and Risks:** Between the regions, global investor allocations should overweight the Asia Pacific region, neutral weight the United States and underweight Europe relative to invested stock as reported by DTZ. Although outperformance is more difficult to achieve in slower growing economies, it is possible to get outsized risk-adjusted returns and so these areas should not be ignored by global investors. Additionally, property selection is crucial to garnering outperformance. The top assets in underperforming markets will, with few exceptions, outperform lower quality assets in outperforming markets. Although Asia Pacific is set to outperform and Europe is likely to lag, a global portfolio would still benefit from significant investing in all three regions.
- **Economic Outlook:** The global economy is bifurcated between those countries that had a financial crisis and those that entered recession purely due to falling demand. Nations that experienced the financial crisis (much of Europe and the United States) are currently in a slow recovery, while those with only a demand driven recession (most of Asia Pacific, including China, Central and Eastern Europe, including Russia India and Brazil) are bouncing back more quickly and entering expansion.
- **Mega Trends:** Investors generally hold core real estate assets for long periods, and as such, major, slow moving trends can have large impacts on returns. Two major mega trends are highlighted in this paper.
 1. **Urbanization of emerging economies:** Urbanization is a trend that is accelerating in emerging markets as rural workers seek opportunities in the city. Increased education throughout the globe will have more people working in offices by the end of the current decade than ever before.
 2. **Aging societies globally:** The developed world will have large populations entering retirement during the next 10 years, and this has implications for the size of the workforce (office), discretionary spending (retail and warehouses) and housing trends. Europe and Japan will experience this trend fully, while the United States will be buffered from aging demographics by immigration and a larger younger generation known as the Echo Boom. Additionally, emerging markets will see a larger workforce during the next decade as their workforces grow due to the younger generation. However, although China's working population is growing rapidly, the one-child policy enacted in the early 1980s will limit the previously experienced exponential growth as we move into the next decade.
- **Capital Market Trends:** Capital flows into real estate were greatest for the office sector in the top markets in Europe and the United States, the multifamily sector in the United States, and office and retail sectors in emerging Asia. Capital will be looking further along the risk spectrum going forward as returns have compressed in many major markets.
- **Real Estate Fundamentals:** Market fundamentals are following in line with growth rates of local economies. Rapidly growing Asia Pacific economies and top tier U.S. and European markets are experiencing a quicker rebound in property fundamentals than mid-tier U.S., European and Japanese markets. Financing for new construction remains tight and most new supply is occurring in only a handful of markets.
- **Real Estate Performance Outlook:** Returns will likely average 8 percent to 11 percent globally from 2011 to 2015, although returns will vary substantially. Asia Pacific properties will likely outperform, with greatest risk in this region. Properties in the United States will perform on average, with lower risk. Europe will likely lag the global real estate market, with lower growth and moderate financial risk.

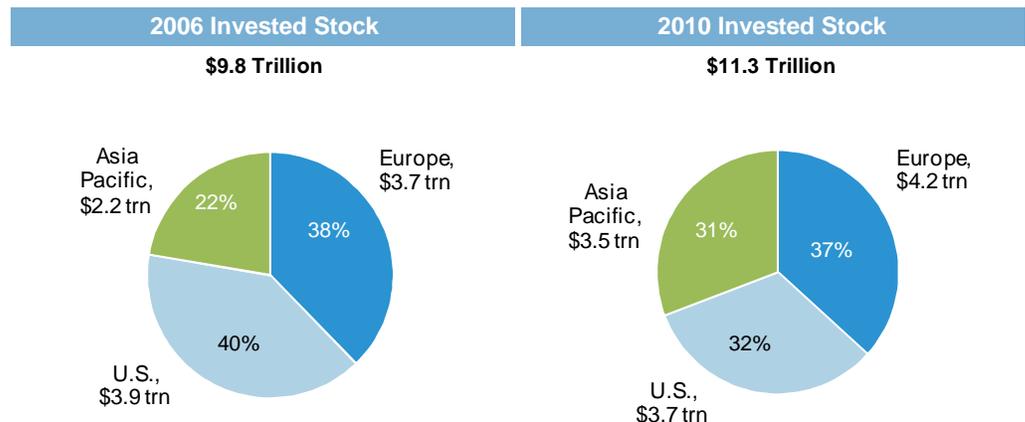
2. Global Portfolio Considerations and Risks

Global investors should look to allocate significant capital across all three regions to core assets during the next five years, but should underweight Europe, overweight Asia Pacific, and market weight the United States according to the investable universe in 2010 as defined by DTZ. Real estate total returns will likely average between 8 percent and 11 percent during the next five years in global core portfolios, and the returns will vary by region with Asia Pacific outperforming, Europe underperforming and the United States performing at the global average. Although the Asia Pacific market is likely to outperform on the whole, a prudent global investor should not overallocate heavily to this region. Unlike areas with deep real estate markets, outsized returns in this less mature region come with risks, and a core investor should look to match investment profiles across markets. The historical benefits of diversification across regions were strong. While correlations of investment total returns between the United States and Europe are relatively high, the correlations between these two and Asia Pacific are much weaker. Thus, diversifying among the three regions can mitigate some risks. While the correlations of total returns in the presented table are for office assets only, we believe these would hold for other property types as well¹. Finally, allocation by property types and regions is only a part of the investment process, and several other market and property specific factors should be examined in any investment decision.

Correlations of Total Returns Among Regional Office Markets (1989 to 2010)				
	Global	Americas	Europe	Asia Pacific
Global	1.00			
Americas	0.89	1.00		
Europe	0.93	0.70	1.00	
Asia Pacific	0.58	0.53	0.36	1.00

Sources: JLL, CBRE, PMA, Miki Shoji, JREI and RREEF Research. As of May 2011.

The following will suggest the allocation by both property sector and market of a model portfolio for an investor without home nation bias. This portfolio will be created by looking at the return and investment risk, as defined by return volatility, profile of each region, market and property type. During the recovery phase of the cycle, it should be noted that some of the markets with the highest returns are inherently volatile, as they move from a negative return to a larger positive return. This is true of some of the most 'core' global markets including New York and London, which have historically outperformed, and are considered low risk when looking at other factors, such as limited supply and greater transparency, but have average to high risk when examining total return volatility.



Sources: DTZ, 2011 Money into Property.

As of May 2011.

¹Data history for other property types (apartments, industrial and retail) is unfortunately too short for correlations to have meaningful results.

Regionally, the current neutral portfolio of real estate invested stock across the globe, per DTZ's Money into Property report, presents that 31 percent of stock is in Asia Pacific, 32 percent of stock is in the United States and 37 percent of stock is in Europe. Investable and invested stock is expected to grow more quickly in the emerging markets and maturing markets, than in the fully matured markets and, as Asia Pacific hosts more markets in the first group it is likely that share of the investable universe will expand for that region during the next decade. Moreover, its virtuous cycle between high foreign investment levels and increasing governance and transparency is set to continue in that region.



Sources: Jones Lang LaSalle, Real Capital Analytics.

As of May 2011.

Forming a global portfolio from a regional perspective based on local excess return and volatility outlook, using the current DTZ data as the market weight, RREEF would suggest a market neutral weight to the United States, an overweight to Asia Pacific, and an underweight to Europe. The United States is a transparent and liquid market, and will exhibit moderate economic growth over the next few years. The combination of these factors makes the region an anchor for a core portfolio. Asia Pacific should be strongly considered for any global investor, as the economic growth and investment return potential is large. Investment in this region also varies, from the established and transparent markets of Japan and Australia, to the other extreme of the relatively new and opaque markets of China and India, with many opportunities in between. Both types of markets, and those in-between, should be considered by investors, with higher risk properties to balance against lower risk ones. An underweight to Europe is prudent for a number of reasons. Lower economic growth forecasts forebode lower total returns. Additionally, capital has rushed into the best properties early in recovery, causing yield underwriting to be lower than what would normally be expected in comparison to the outlook. However, investment in Europe is still encouraged, even with a lower return outlook. Investment in this established and highly transparent region can provide diversification benefits and property specific opportunities can provide outsized returns.

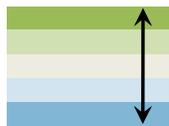
Region	Descriptions
United States <i>Neutral Weight</i>	<ul style="list-style-type: none"> Strong nominal and excess returns with high transparency and recovering liquidity. Even sector weighting among the four property types results in active overweight to industrial and retail, and active underweight to apartment and office relative to NCREIF Property Index sector weights.

Region	Descriptions (<i>continued</i>)
Asia Pacific <i>Overweight</i>	<ul style="list-style-type: none"> Highest nominal and excess returns with virtuous cycle of improving scale, liquidity and transparency/governance compensate investors for the region's higher volatility; also has lowest correlation to U.S. and European regions. Industrial sector is expected to have the highest total return outlook over next five years, driven by external trade supported by recovering economies in developed countries. Mixed but strong overall performance in office sector due to significant yield compression in some markets and tenant preference for upgraded space versus obsolete space. Strengthening domestic consumption and increasing net absorption continues to support retail performance.
Europe <i>Underweight</i>	<ul style="list-style-type: none"> Lowest nominal and excess returns in addition to most significant long-term demographic and short-term cyclic headwinds. Focus on more stable (core) economies in the early years, currently troubled markets in subsequent years. Late recovery markets may offer some current opportunities to acquire core product at relatively attractive yield levels. Europe's demographics, forward growth and capitalization rates favor retail over office.

The table below presents five-year excess investment returns and risks forecasts by metro and property sector. Market and property types are grouped, with risk rated from low on the left to high on the right, and excess returns rated from underperformance on the bottom to outperformance on the top in terms of excess total return above sovereign debt yields. As we are looking at returns, we judge risk based on return volatility. This is different than operational risk, and a property that is financially risky may be operationally low risk. As this approach relies heavily on historical and forecast data, markets and sectors with few data points are not included.

Global Real Estate Excess Return and Risk Profiles of Forecasts, 2011 - 2015

		Low Risk			Average Risk			High Risk		
		USA	Europe	Asia-Pacific	USA	Europe	Asia-Pacific	USA	Europe	Asia-Pacific
Relative to Average Excess Return	Outperform	R-Miami-Ft. Lauderdale R-Seattle		R-Kuala Lumpur	I-Los Angeles I-NYC (Northern N.J.) I-Seattle O-Boston O-NYC (Northern N.J.) O-San Francisco R-Los Angeles R-San Jose	O-Paris: La Défense	I-Hong Kong I-Shanghai O-Tokyo R-Hong Kong R-Taipei	I-San Jose O-San Jose O-Seattle	O-London: City R-Poland	I-Beijing I-Singapore O-Beijing O-Hong Kong O-Shanghai O-Singapore R-Beijing R-Shanghai
	Average	O-Washington D.C. R-San Francisco R-Washington D.C. R-NYC-NorthernNJ	O-Brussels R-Germany	R-Singapore	A-Boston A-Chicago A-Miami/Ft. Lauderdale A-San Francisco A-Seattle A-Washington D.C. I-Boston I-Miami/Ft. Lauderdale I-Washington D.C. O-Chicago O-Los Angeles O-Miami/Ft. Lauderdale R-Boston R-Chicago	O-Amsterdam O-Milan O-Paris: CBD O-Stockholm R-France R-Italy R-Sweden	I-Melbourne I-Seoul I-Tokyo	A-Los Angeles A-NYC (Northern N.J.) A-San Jose O-Atlanta O-Dallas I-Atlanta I-Dallas R-Atlanta R-Dallas	O-London: West End O-Madrid O-Warsaw R-UK	
	Underperform	I-Chicago	O-Hamburg O-Munich	I-Kuala Lumpur O-Kuala Lumpur R-Sydney R-Melbourne	A-Atlanta A-Dallas	O-Frankfurt R-Netherlands	I-Sydney I-Taipei O-Melbourne O-Seoul O-Sydney O-Taipei R-Tokyo R-Seoul		R-Spain	



Markets with the highest ratio of the expected excess return to risk

Markets with the lowest ratio of the expected excess return to risk

A: Apartments
I: Industrial
O: Office
R: Retail centers

Source: RREEF.

As of May 2011.

United States

The United States real estate market is among the most transparent and liquid in the world. This is especially true for tier one markets, where international investors are most likely to place capital. Within the United States, property type selection should have an overweight to industrial and retail properties and underweight to the apartment and office sectors relative to the NCREIF Property Index² and a moderate overweight to the East and West regions with corresponding underweight to the Midwest and South. Coastal, supply constrained, markets tend to have higher volatility than those in the interior, but will also tend to outperform during the next five years. It will be longer before meaningful amounts of construction commence in the supply constrained markets and so vacancy will be able to compress further in these markets. Seattle and Miami-Ft Lauderdale retail will outperform, with lower volatility. Office space in San Francisco, New York and Boston will also likely outperform, as will industrial space in Los Angeles, New York and Seattle.

Europe

Real estate performance over the next five years will be mixed in Europe and global investors should focus on more stable economies in the early years while waiting for trouble to shake out in the more challenging markets. The London office sector, which was one of the hardest hit and recovered rapidly, will continue to outperform. However, as a volatile metro and property sector, it will be a timing play and investors need to be watchful of the next crisis. Core Europe had a boost in 2010, but the capital markets may have jumped too far ahead of the potential growth. Eurozone growth is likely to be soft, as well positioned member countries are forced to absorb losses from the others. Office markets of Paris and Milan will likely perform on the market average when measured by excess returns during the near term, with average volatility. Retail markets in Germany and the office market of Brussels will also likely perform on average, but with lower risk.

Late recovery markets may offer the opportunity to acquire core product at relatively attractive yield levels in light of the uncertainties. A primary example of this strategy is Spain which will likely offer attractive investment opportunities over the medium term as it recovers, but risks during the near term require close monitoring. The implication of these trends for real estate investors is the uncertainty regarding which sectors of the economy will drive the recovery and thus, which real estate sector is best poised to benefit and reward investors.

Asia Pacific

Asia Pacific has substantial variation between markets, as it hosts both well established and mature real estate markets and relatively new markets that are just now becoming available for core investment. Demographic trends and economic growth will support the region for the next five years. Real estate will be the recipient of these trends and rentals should continue to grow, although not evenly in strength, during the forecast period.

Asia

Asia is likely to have the highest returns over the next few years, but with some risks. China has the highest returns forecasted, but with the highest volatility and potential downside risk. Industrial, office and retail properties are likely to have tremendous growth, but economic and operational risks commensurate with possible returns. Meanwhile, the high expected returns in Hong Kong and Singapore are accompanied by their cyclical features where historical rental decline happened fast and sharp. The high volatility in Hong Kong and Singapore contrasts sharply with Seoul, Kuala Lumpur and Taipei markets which are more resilient. Yet these markets would also offer investors a below-average return.

Assets in these markets are likely to have higher than average volatility to match their higher than average total returns. This is likely to be most true for the rapidly expanding markets of China. Although core investors tend to shy away from volatility, these markets are still investable for a global core portfolio through diversification. A global core investor will be able to match assets in this region with assets in regions with lower volatility and, with prudent

² The NCREIF Property Index (NPI) is an equity, asset level index of operating properties within the United States.

investing, receive higher risk-adjusted returns than otherwise.

Australia

Australia benefits from having one of the most transparent real estate markets, where information cost is low, and surprises are less frequent. It also benefits from economic growth from Asia. Consequently Australia is forecasted to perform well during the next five years. In general, the Australian markets would yield attractive absolute return, however will likely be less attractive on an excess return over the local government bond which is relatively high. Most domestic markets are likely to have lower returns with average or low risk. The largest concern for Australian real estate investment for international investors is currency risk, as the Australian dollar appreciated considerably against other currencies since the beginning of the recovery against other currencies. Additional upside risk comes from domestic investors. The REITs and superannuation funds are refocusing away from cross-border investing, and this will bring additional investor demand to Australia.

Japan

The Japanese economy continues to have many unknowns associated with the Great Tohoku Earthquake, and the resulting tsunami and nuclear power plant crisis, and in the near term wary investors will create softer capital values eventually creating attractive buying opportunities. RREEF Research has downgraded its forecast, and recovery will now likely occur in 2012 due to uncertainties about the capital value component of total return. Investors may also find opportunities as Japan's public sector (both national and local governments) falls under increasing pressure to privatize assets.

Total excess returns in Tokyo will likely perform on average in comparison to the local risk-free rate during the next few years with average volatility. Tokyo retail has the lowest prospects of the Japanese property types, with industrial having average risk-adjusted returns and average risk. Tokyo office will likely have average risk but outperform on a risk-adjusted basis.

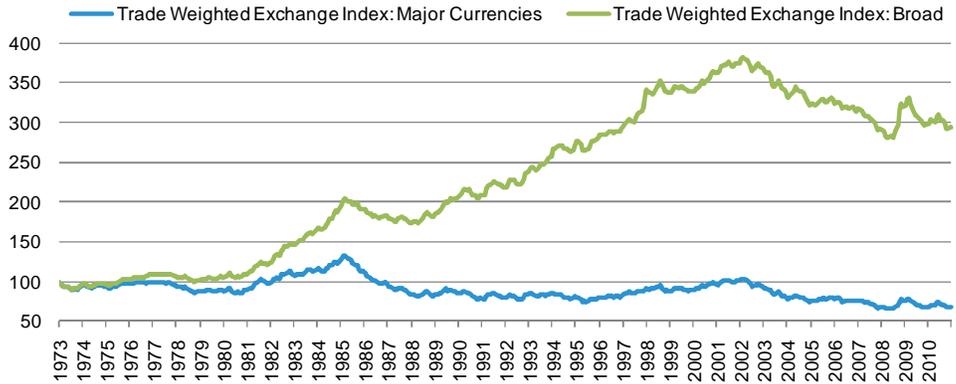
Risks of Global Investment

While RREEF suggests that a core portfolio should be invested in all three regions and in both developed and emerging economies, there is risk to investing so broadly. Currency fluctuations, supplementary costs and capital regulations, and transparency and liquidity issues add to the more often expected risks of domestic core real estate investing. Local market risks are more wide-spread to global investors, but as portfolios are diversified across regions, there is a hedge to local exogenous factors. Investors need to weigh the added returns and diversification benefits of investing globally against the associated risks.

Long-term, direct real estate investment on a global scale must consider currency effects. Risk of changes in foreign exchange prices exist for international investors of any asset class, but real estate investors should focus on the medium- to long-term trends, and spend less time on the short term. The U.S. dollar will likely remain the reserve currency during the next cycle and beyond. However, the dollar has lost value against other currencies during the last decade and as the economy is on a slower recovery it should continue to depreciate against emerging market currencies as global capital flows and trade rebalance. This will be a slow process as major trading partners in the global economy have their currencies on a managed peg. Against the euro and other European currencies, the dollar is likely to remain balanced or possibly appreciate, as recovery is likely to be stronger in the United States than in the eurozone and European Union. This is unlikely to be true during the short term, as interest rate differentials between the eurozone and the United States will likely increase, but should invert over the long run.

Trade Weighted Dollar Indices

January 1973 = 100



Note: Major currencies are euro, Canadian dollar, Japanese yen, pound sterling, Swiss franc, Australian dollar and Swedish krona.

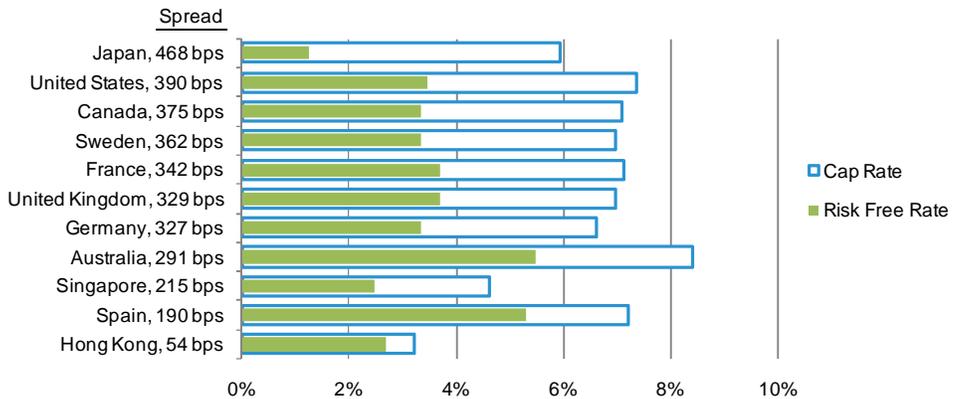
Source: Board of Governors of the Federal Reserve System.

As of May 2011.

Investment in new, less transparent areas can result in outsized returns; however it may be difficult to successfully secure core investments. While the number of institutional quality properties is expanding quickly in these markets, available investments are still rarer than in more transparent and liquid markets. Additionally, stricter government controls in emerging markets can result in higher transaction costs, lower investment control and the need to establish a joint venture with a local investor.

Capitalization and Risk-Free Rates

First Quarter 2011



Note: Includes all commercial properties.

Source: Real Capital Analytics.

As of May 2011.

Yield premiums to the risk free rate vary substantially globally. Capitalization rate spreads range from nearly 500 basis points in Japan and the United States to only 25 basis points in Asia. Accounting for income growth, investors should look for properties with a wide enough spread to justify the risk associated with the cash flow.

Additionally, it becomes difficult to apply accretive financing to assets where the spread between risk free rates and capitalization rates is small, as interest rates become difficult to cover. However, larger spreads make financing attractive.

Debt maturities and troubled assets are a continuous risk in the current environment. Properties purchased at the top of the market with five-year, interest only financing are coming due this year and this could lead to additional value declines for the broader market. However,

risk also clears the way for opportunity and refinancing capital will be in demand in the form of mezzanine debt and preferred equity opportunities.

Local exogenous risks will play a part in global investing. Risks to global investing in 2011 include the political upheaval in the Middle East and North Africa, the fallout from the Japanese earthquake, and the ongoing European sovereign debt crisis. The civil war in Libya and other political upheaval in the region is contributing to higher oil prices globally. This is having a near term effect on economic growth, but the effects will abate as other producers increase output. The earthquake that hit the coast of Japan will have a near term negative effect on the economy. Fears of nuclear radiation and substantial electrical production problems reduce business confidence overall. Lastly, the European sovereign debt crisis continues to weigh on growth in that region. Austerity measures and bailouts may not be enough to keep member states from defaulting on their debt, and the risk is the failure of the system. Problem countries garnered cautious support from the International Monetary Fund (IMF) and the German populous, but another major shock to the system could put the European Monetary Union (EMU) further at risk for dissolution.

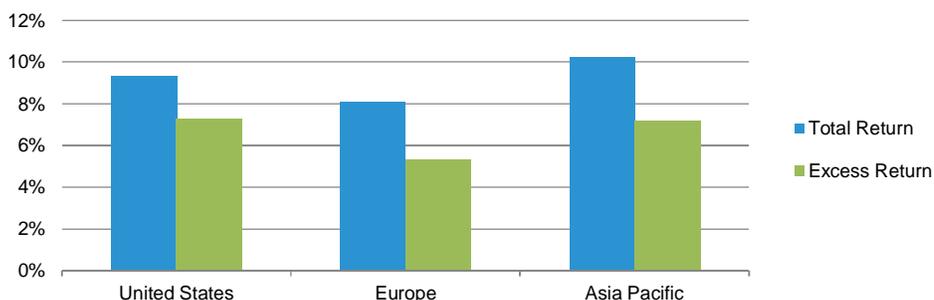
3. Real Estate Performance Outlook

Unlevered total returns performed well across the globe in 2010 and, in many countries, in 2009, especially in the wake of the large contraction in 2008. However, the robust results in 2010 were largely due to capital returning to the market, increasing demand for assets and compressing capitalization rates. In most real estate markets, future returns will come from income yields and growth rather than changes in the capital markets. Some markets, especially in Europe, are at risk for rising capitalization rates as local government bonds rise. If this risk becomes reality and capitalization rates rise, growth in operating income will have to be strong to counter depreciation from the capital markets.

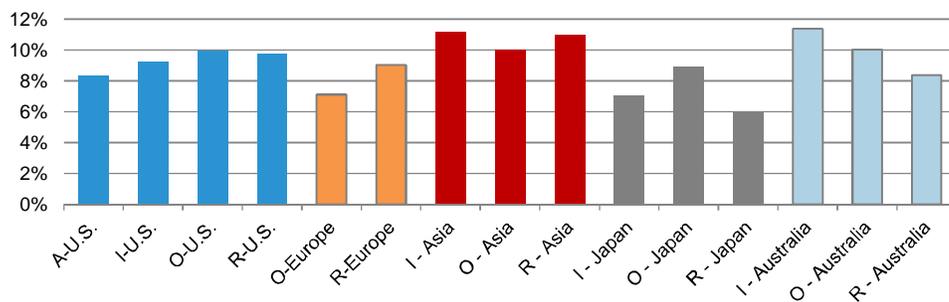
Total return forecasts by region are based on the equal-weighted forecasts by global city-property type and are in line with the expected outlook of both economic growth and real estate fundamentals. General equity and fixed income capital markets have so far predicted the real estate recovery well, rushing first to Asia and core Europe and then to top performing markets in the United States. As property fundamentals recover further, Asia is expected to lead, although risk remains relatively larger in this region than in Europe and the United States. The United States is expected to lead Europe over the next five years as the euro area deals with the sovereign crisis engulfing several member states.

Forecasted Average Annual Regional Returns, 2011 - 2015

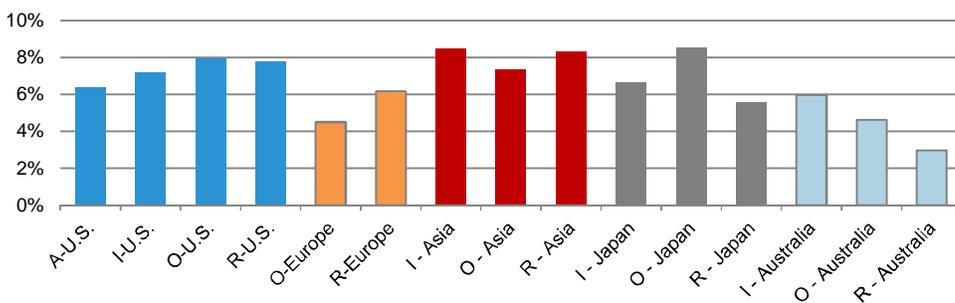
Regional Total and Excess Return



Regional and Property Total Returns



Regional and Property Type Excess Return



Source: RREEF.

As of May 2011.

Although growth in the Asia Pacific region is expected to be stronger than in the United States and Europe over the next five years, total returns are likely to be within 1 percentage point of U.S. returns, and 2 percentage points of Europe. This is mainly due to pricing in Asia Pacific, which was strong in 2010, and remains at higher levels in 2011, bidding down returns.

The relative ranking of the three regions based on unlevered excess return forecasts, above the local government bonds, are relatively in line with the rankings of the absolute total return forecasts, with Asia Pacific and the United States leading Europe. Lower government bond rates are not necessarily correlating with better absolute returns on an unlevered basis but could result in more attractive financing opportunities.

4. Economic Outlook

Economic growth globally is running at two different speeds. Countries that were hit hardest by the financial crisis and entered a deep recession have exited into a slow recovery. These countries include Western Europe and the United States. Japan, which has not yet fully recovered from the recent financial crisis, would have been part of this group, but recently entered recession following the earthquake. Alternatively, countries that did not experience the financial crisis

directly, those that entered a recession because of a drop in global demand, are experiencing a much stronger recovery. Countries with a higher rate of growth include Australia, Brazil, China, much of Asia, and portions of Eastern Europe.

Global economic growth is expected to accelerate at various rates in the next few years. The emerging economies of Asia, South America, and Eastern Europe all rebounded quite quickly and worries of slow economic growth have moved aside of fears of overheating economies. These markets will spend the next couple years managing growth rather than stimulating a recovery. Developed economies, such as the Benelux, Germany, Scandinavia, and the United States, are accelerating out of recovery and into expansion, but, these countries remain on a tenuous foundation and could move back into recession after a major exogenous shock. Finally, a sluggish recovery is expected for the rest of Europe, where deeper, more immediate risks remain in the form of sovereign and household debt issues leading to austerity measures and a focus on debt service over consumption and investment.

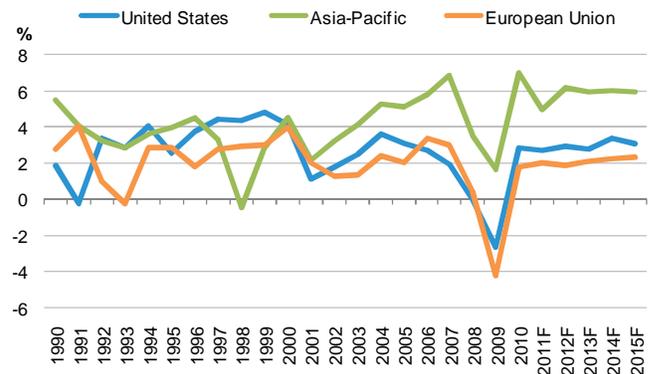
Despite higher oil and food prices (due to demand) and economic growth, global inflation will likely remain under control as central banks across the world have worked over the past 20 years to anchor inflation expectations in order to lower rates. Expectations of inflation beget actual inflation and the anchoring of this outlook helps mollify price increases. Anchoring is further aided by the end of wage indexation, preventing people from assuming inflationary wage increases and thereby not forcing firms to assume inflationary price increases.

United States

The U.S. economy is firmly in recovery and on the verge of expansion, but the pace of economic and job growth continues to be slower than desirable. The economy grew 2.9 percent in 2010, producing fewer than 1.5 million new jobs, a small fraction of the 8.6 million lost during the previous two years. Recessions coupled with financial crises tend to recover with slower rates of growth, and the current recovery is true to form. Consumers are prioritizing debt service over spending, while lenders are just now in a position to originate new loans, slowing overall economic growth. Fiscal constraints at the national, state and local levels will also provide drags on economic growth, and significant budget cuts and layoffs are anticipated. Healthy corporate profits, increasing demand, and rising exports will cause business investment and spending to drive growth early in expansion. Due to excess capacity, wages should remain restrained over the next few years, increasing the competitiveness of workers in the United States as compared to the rest of the world.

A little job growth can go a long way, and consumer spending, which improved in the first quarter of 2011, should continue to expand in anticipation of jobs. Additionally, consumers and businesses that have held out on capital spending (vehicles, computers, appliances, etc.) during the first half of 2010 will expand spending for these goods in 2011 as they did in the second half of last year. However, the expansion of credit availability will be sluggish as the financial sector is only now beginning to recover. Typical of recoveries from a financial crisis,

Real GDP Growth of Major Economies



Source: IHS Global Insight.

As of May 2011.

this slower credit expansion on both the consumer and business sides will cause near-term employment growth to be slower than what normally would occur after a deep recession.

More robust growth is forecast between 2013 and 2015, when GDP growth should average between 3.0 percent and 3.5 percent annually. Employment growth should average between 2.5 million and 3.0 million new jobs annually, pushing the unemployment rate down to between 6 percent and 7 percent by late 2015. RREEF also expects roughly 2.5 percent average annual inflation between 2011 and 2015.

Given highly favorable trends, the economy is more likely to outperform than underperform these forecasts; however, inflation pressures would be stronger under this optimistic scenario.

Europe

For the whole of Europe, economic activity slowed during the second half of 2010. GDP growth of 0.3 percent during the third quarter followed 1.0 percent growth in the second quarter. Performance across countries varied markedly, with Germany and the Nordics outperforming and Southern Europe underperforming. In part, the modest growth for euro land was due to fiscal tightening as well as the recent turnaround in the exchange rate of the euro and pound against the dollar and their impact on respective exports. Europe's slowing growth also mirrors the continuing uncertainty surrounding the timing, structure and associated impact of policy normalization within the EMU.

The sovereign debt crisis resulted in fiscal tightening across the region and this will continue to restrict economic growth prospects in the near term. Furthermore, sudden, periodic loss in confidence by investors and temporarily increasing interest rates continue to weigh on regional economic growth. In contrast, despite implementing major policies, deficits increased in Ireland and Portugal during the year with both countries now preparing for a second wave of austerity measures. In May, eurozone finance ministers agreed to a €78 billion bailout for Portugal with further discussions underway as to how the Greek problems can best be resolved. While still running one of the highest deficits among EMU members, the government deficit in Spain is falling sharply, and Spanish banks are largely solvent. Relative to GDP, public debt in Spain is not on the same scale as Greece or Portugal and the Spanish prospects are equally reflected in the relative low spread of government bonds over the German Bund compared with that of Greece, Portugal and Ireland.

The European economic outlook falls into three broad categories. First, markets where both governments and households are over-indebted, which include Ireland, Portugal, Spain, Hungary and the United Kingdom, have the weakest prospects in the near term. Second, markets are subject to fiscal constraints as governments reduce large deficits through austerity measures, including France and the Netherlands. These markets have better prospects in the near term, but will experience muted growth upon a full recovery, limiting the prosperity phase of the expansion. Third, economies with limited debt, such as Scandinavia, Germany, Poland and Czech Republic, are already in an economic expansion and have strong near term prospects.

The economic recovery in Europe will likely continue to face significant economic and financial sector headwinds within the eurozone, while non-eurozone economies may grow faster in the coming year. Even without another Greek-style crisis erupting in 2011, fiscal realism in general will compound economic pressures and stifle growth in southern and peripheral Europe. Economic growth for the eurozone is forecast to be 1.5 percent in 2011 and 1.6 percent in 2012. The Nordics and Central and Eastern European markets of the Czech Republic, Poland and Hungary are all on better fiscal ground and experienced stronger growth in 2010. These countries will grow at a relatively higher rate, aided by growing demand for advanced manufactured goods in the rest of the world.

Inflationary pressures became more pronounced in the eurozone towards the end of 2010 and early 2011, driven predominantly by rising food and oil prices. While the labor markets and consumer confidence across Europe remain too weak to induce increasing consumer prices, exogenous cost factors – in particular energy costs, a key factor of production – could also contribute to rising prices. This would put the European Central Bank (ECB) in a difficult position. Maintaining its main goal of ensuring euro stability would force the ECB to tighten monetary policy earlier and more sharply than would be the case to support its second objective of economic stability and growth across the eurozone. The ECB rate increase of 25

basis points in early April is the first increase after nearly two years, and further steps are expected later this year. While the main scenario is still that of low inflation and low interest rates in the near term, the risk of higher interest rates as the ECB reacts to higher inflationary pressures exists, which, in turn, could impact the broader economic recovery.

Asia Pacific

Asia

The Asian economies are expected to grow faster than other major economies. Corporate profitability and deepened integration between Asian economies have translated into growing demand for commercial real estate. While Asia was not immune to the global downturn, the lack of a substantial financial crisis enabled this region to be the first to recover. Now that recovery is fully set and most economies in the region are in expansion mode, fears of a slow recovery have changed to trepidation of overheating and inflation. Governments have the challenge now of controlling growth with macroeconomic policy tools. Despite this, it is likely that the Asian economies will continue to be a major source of global GDP growth during the next five years and are expected to outperform both Europe and the United States during the next decade.

China, which creates 37 percent of Asia's output, is expected to maintain 8 percent economic growth per annum in the coming decade despite the recent risk of overheating. Policy risk to reign in inflationary pressure is expected to remain in the near term in order to maintain stable price levels, and thus, social stability. The Chinese government therefore is likely to continue its tightening bias towards the real estate industry, especially the residential sector, amid an abundance of capital in the economy. Yet, with gradual internationalization of the renminbi, the Chinese government is expected to have more tools in keeping economic growth on track.

Australia

While other developed nations are struggling to keep their economies growing, Australia is benefiting from increased global demand for raw materials, especially from nearby emerging markets. It is good to be long in what China needs and Australia is benefiting from this situation. Australia has raw materials, rare commodities and high skilled services, all of which are, and will continue to be, in high demand from China.

Increased inflation caused the central bank to raise key rates sooner than other countries, and right now, Australia has the highest interest rates of all developed nations. Higher rates and stronger growth is appreciating the Australian dollar and policy makers are hoping the elevated dollar will govern the speed of economic growth.

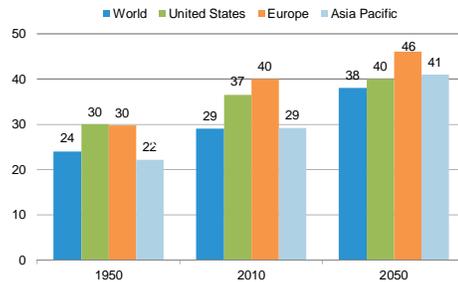
Japan

The exception to the Asia Pacific growth story is Japan, which continues to experience slower than desirable economic and job growth and is faced with contracting demographics. The reconstruction after the earthquake, tsunami and radiation fallout adds risk to this outlook. Nevertheless, Japan managed to grow 4.4 percent in 2010, fuelled by external demand and waning ripples of government stimulus. But after the earthquake shook the country in March, significant constraints on economic activity became apparent, including shorter business hours and the closure of stores and plants. Even Tokyo and other cities not directly hit by the earthquake or tsunami are experiencing lower levels of economic activity. The sources of these disruptions - electric power shortages - are expected to last for the remainder of the year. Deutsche Bank's economists have incorporated these impacts and lowered Japan's real GDP forecasts for 2011 to negative 2.1 percent, followed by a slightly stronger rebound in the 2 percent range in 2012 and 2013 as reconstruction moves into higher gear.

5. Megatrends and Themes³

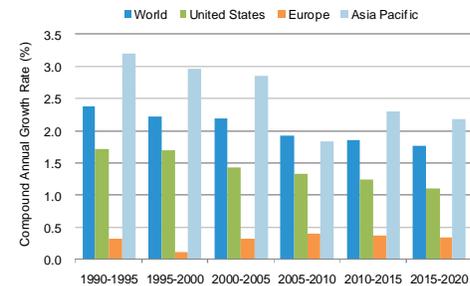
While economic cycles are driven by changes in production and employment, structural economic growth is also shaped by longer term shifts in macro trends and the results have significant implications for real estate. While the impact of longer term structural trends has always been a factor in considering real estate prospects, the accelerated pace of change has increased their importance for even near-term outlooks. Many such trends are pervasive on the global scale, but there are major differences in how they impact the economy, society and, more specifically, real estate markets at the regional, country and local levels.

Median Ages of World Population



Source: UN World Population Ageing 2009 report. As of 2010

Annual Growth Rate of Urbanization



Source: United Nations.

As of May 2011.

- The Asia Pacific region is expected to have the fastest urban growth among the major economies, leading to accelerated real estate demand. Furthermore, increased urbanization should lead to greater barriers to entry.
- The world is growing older. Median age across the world is increasing, and some of the countries with the oldest median aged populations host large core real estate markets. Japan, Germany, Italy and Hong Kong all have median ages over 40 years, and most of Europe is not far behind. The proportion of the European Union population over 50 is forecasted to grow to over 40 percent by 2020. While this problem is not quite as acute in China, the one child policy enacted in the early 1980s is resulting in a smaller younger generation. The government is considering removing the policy in phases, but the effects on demographics are real and could have a subtle impact on demand for future space. Markets with aging populations should result in decelerated real estate demand growth, but an increase in demand for certain types of real estate such as senior living facilities.
- Unlike many of the other mature markets, the United States⁴ has a comparatively lower median age, at 36.5 years. Among the developed countries, the post-World War II baby boom is aging and in many countries in Europe, Baby Boomers had fewer children, with birth rates well below replacement leaving a demographic hole. In the United States, this is not true due to the children of the Baby Boom generation. Known as the Echo Boom, the youngest of the generation is 18 right now, and the eldest are in the junior ranks of the work-force. This demographic will be driving the business force during the next decade in the United States. This cohort is also creating greater demand for urban real estate.

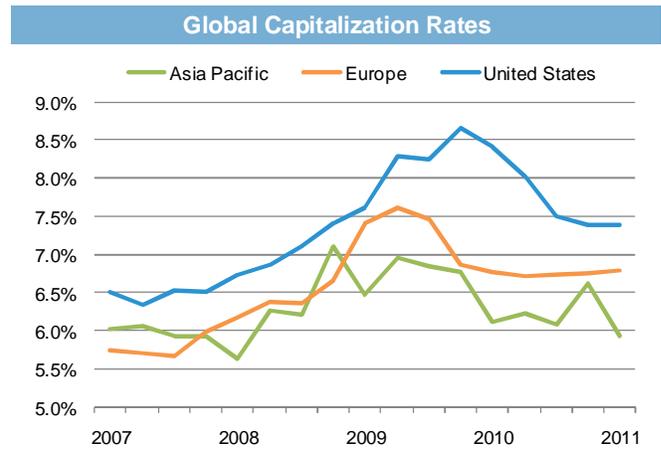
³ Demographic information sourced to the World Population Ageing 2009, Economic & Social Affairs, United Nations

⁴ For more information on demographic and structural changes in the United States, see the RREEF Research paper "Boomers, Echos and X's: Generational and other structural shifts and their impacts on future demand for real estate in the coming decade"

Asia, for the most part, is younger and growing, while Europe is aging and shrinking in population, and the U.S. Baby Boomer cohort will be replaced by the Echo Boom. Global investors will be moving capital in step with economic growth, increasing their allocation to Asia, and decreasing allocations to the United States and Europe during the next 10 years. Transparency will increase in Asia's emerging markets as the real estate industry matures. Core investors will need to watch demographic patterns to find outsized returns.

6. Capital Markets Outlook

Improvement in global stock markets, evidence of improving fundamentals, and increasing amounts of fresh equity and debt promoted real estate investment in 2010. However, an abundance of investment opportunities in 2009 quickly turned to an undersupply in 2010, and increased demand resulted in capitalization rate compression globally. Pricing for core assets in prime markets jumped in 2010 as a result of increasing transaction volume with limited supply. Asia Pacific continues to be the region with the highest real estate transaction volume

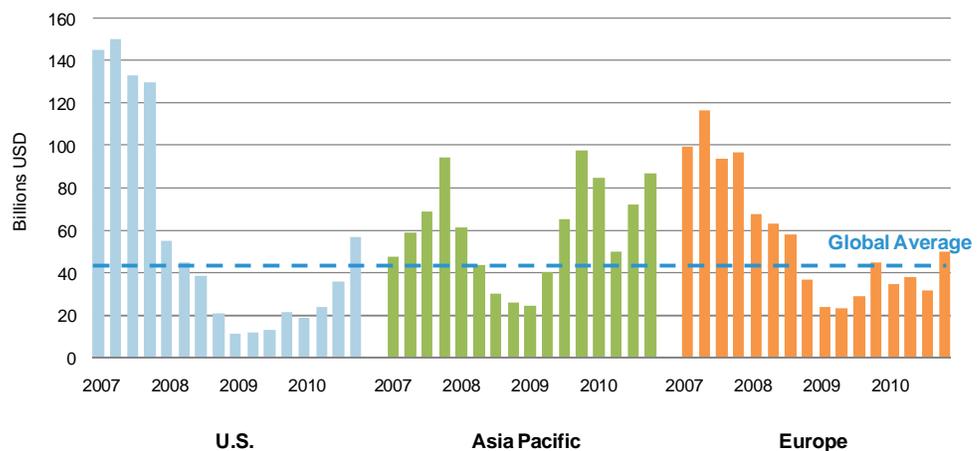


Source: Real Capital Analytics. As of May 2011.

since 2009, but volume in the United States is increasing as well. While capitalization rates peaked first for prime assets in Europe, transaction volume growth is still stagnant.

Global real estate transaction volume should continue to increase in 2011. The United States and Europe will likely see more year-over-year growth than in the Asia Pacific region on core properties, as those regions are starting at lower levels relative to core stock. Capitalization rate compression, which was broad based in 2010, will likely stall in 2011.

Quarterly Transaction Volume by Region All Property Types USD 10 Million and Above



Note: Does not include land. Source: Real Capital Analytics.

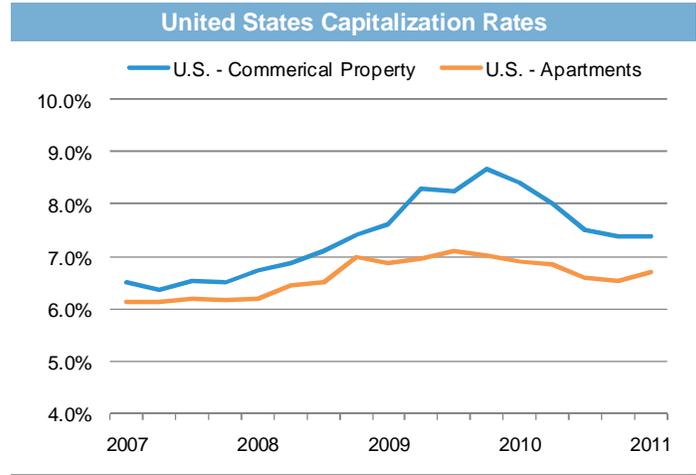
As of May 2011.

United States

Commercial real estate capital markets are recovering in the United States. Total volume doubled from 2009 to 2010, totaling \$109 billion. However, transactions are still at low levels. Volume in 2010 only achieved a level comparable to that achieved in 2002, when the real estate market was last in recovery.

Investor demand early in the year begot further demand later, but supply for higher quality core product remained stable and capitalization rates compressed as a result. Demand appeared first for apartments, which were supported by the government-sponsored enterprises (GSE), as well as burgeoning operating income growth. Core central business district (CBD) office properties soon followed in compression. Retail, suburban offices and industrial properties began to feel the effects of recovery only in late 2010 and early 2011.

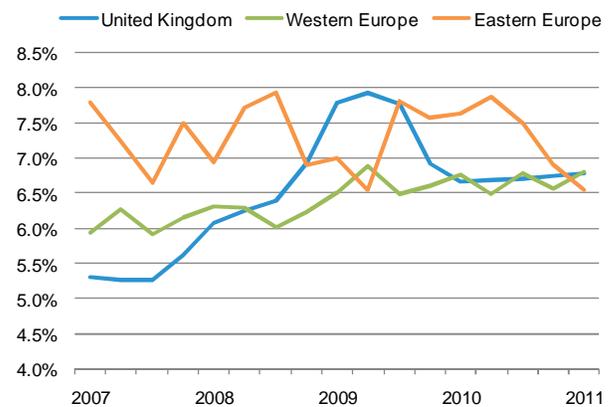
Transaction volumes should continue to increase further in 2011 in the United States, and although capitalization rates may not compress further, the spread to 10-year U.S. Treasuries will at least narrow. Where 4.5 percent capitalization rates seemed exorbitant in early 2010, they are now the norm in the top markets for apartments, and income growth is supporting this pricing for at least the near-term. Although interest rates are off their lows, all lenders are back in the market with even the most conservative looking to place capital as debt again. Investors entering the market will need to be cognizant of interest rate risk, as short-term Treasuries are historically low. Although RREEF is currently forecasting Treasuries to increase only moderately over the next decade, any underwriting should consider the risk of larger jumps.



Europe

Transaction volume in Western Europe and the United Kingdom totaled \$105 billion in 2010, an increase of 23 percent over the low levels of 2009. While the improvement in transaction activity has been evident in 2010 across many national markets, the absolute investment volumes have varied. Investors largely remained focused on markets in Western and Northern Europe. The United Kingdom accounted for over 40 percent of the total volume for the year and Germany and France followed in rank. Investors returned to core Western European markets in 2010 though they largely remained averse to investing in peripheral European markets⁵.

European Capitalization Rates



Note: Data based on transactional yields of available deals.
Source: Real Capital Analytics. As of May 2011.

Transaction volume in Central and Eastern Europe (CEE) totaled \$11.1 billion in 2010, an increase of 51 percent over 2009 levels. Russia attracted the highest interest followed by Poland then the Czech Republic.

Within the CEE, it should be noted that institutional investors tended to invest mostly in Poland, Czech Republic and Hungary in 2010 as these are the more transparent markets within the area, and demand is focused on core real estate.

The demand for prime properties led to further yield compression in Poland, Czech Republic and Hungary. Future development will be similar to Western Europe with the expectation that more opportunistic investors might come back to CEE as improving market fundamentals make room for opportunities.

Transaction volumes will likely increase in 2011. Capitalization rates compressed in the most prime markets in 2010 and investors are incentivized to sell. However, demand for investments will likely continue to exceed supply during the year, and new investment will likely move outward on the risk spectrum. Investors will search for yield in secondary markets and be willing to take more operating risk in terms of vacancy. Just as in the United States, many investments made during the boom years were secured against high loan-to-values (LTV), and given the significant value write downs of the last three years, it is likely this might provide an increasing source of deal flow through 2011 and beyond.

During the medium term, it is likely that there will be minor upward pressure on real estate yields. In the face of rising interest rates, investors may be incentivized to sell at the low capitalization rates, if buyers are continuing to offer higher prices. However, capitalization rates will not likely increase in lockstep with interest rates, and the spread will narrow further along in the forecast period.

⁵ RCA March & May 2011

Asia Pacific

Asia

Investors increased their allocation to real estate in the Asia Pacific region in 2010. Total transaction volume in dollars, excluding development site transactions, increased 40 percent from 2009 to 2010 according to data from Real Capital Analytics. Transaction volume in Japan totaled \$17.7 billion, or 28 percent of the Asia Pacific total. Australia and Hong Kong followed, with \$10.9 billion and \$10.0 billion, respectively. Transaction volume in China exceeded \$8.3 billion, not to mention that development site transactions in this rapidly modernizing country totaled an astonishing \$187 billion.

Asia, excluding Japan, is a diverse investment universe where yield movement diverges among markets. Capitalization rates for more mature markets such as Hong Kong and Singapore will remain low, despite forecasts for capitalization rates to expand gradually as interest rates normalize. Meanwhile, capitalization rates in the Seoul office market peaked in early 2009 and compressed since late 2009, as low interest rate attracted domestic institutional capital to re-enter the market. Nonetheless, with interest rates on the rise and abundant supply in the next five years, capitalization rates in the Seoul office market are expected to gradually expand.

In the meantime, an influx of international capital and the emergence of domestic capital brought to China a structural shift in commercial property markets. Capitalization rates fell during the past two years to levels comparable to developed economies. India, where capitalization rates are still around 10 percent, will be the next candidate for such a structural shift during the coming decade as the investable universe expands and the market becomes more transparent.

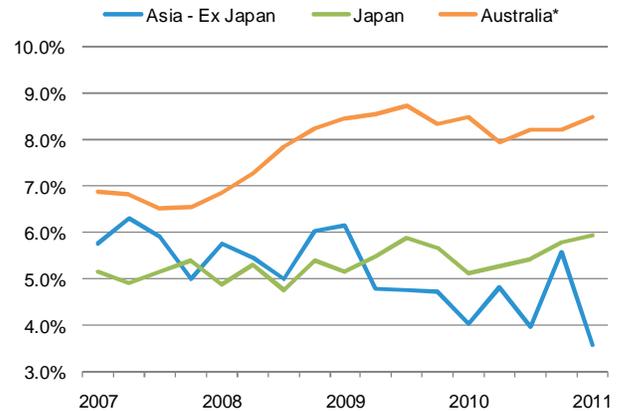
Australia

The Australian commercial real estate market is featured by its depth, transparency, liquidity and a well-developed REIT system. Capitalization rates moved out during the global financial crisis but have started to compress again since late 2010, as foreign investors searched for quality assets amid the recapitalization of the distressed REITs. A Jones Lang LaSalle survey shows that offshore investors accounted for 20 percent of total commercial transactions in 2010, the highest since 1994. Additionally, the latest revision of the Australian Managed Investment Trust scheme in June 2010 provides investors with a more favorable tax structure which is expected to lure more overseas investors.

Australian REITs (AREITs) underwent a strong recapitalization exercise in 2009 in response to the sharp decline in values in 2008. Fundraising totaled AUD 11.9 billion in equity, putting capitalization levels higher than the previous peak in 2007. With distressed REITs recapitalized and restructured, sales of quality assets at attractive prices is expected to wane. Despite healthier balance sheets, acquisitions by AREITs are still tiny when compared with the volume achieved during the peak years. Nonetheless, transaction volume should increase in 2011.

The recapitalized AREITs and the rebalanced superannuation funds, as well as the domestic institutional investors, are expected to re-enter the market, and therefore competition for investments is expected to intensify. Transaction volume should increase in 2011 and capitalization rates will likely compress.

Asia Pacific Capitalization Rates



*Australia data is inclusive of New Zealand, however, this only makes up a small portion of transaction volume in this sub-region.

Data based on transactional yields of available deals.

Source: Real Capital Analytics.

As of May 2011.

Japan

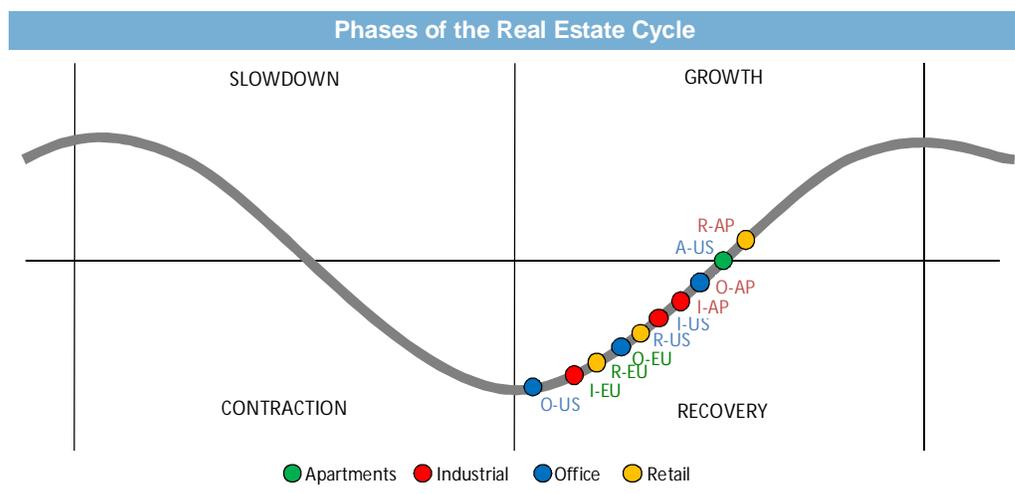
Credit conditions continued to ease in the Japanese real estate markets, at least until the earthquake occurred. New lending by banks for real estate projects grew by 14 percent in the fourth quarter 2010 compared to the same period the previous year⁶, marking four consecutive quarters of increase. The Bank of Japan's Diffusion Index (DI) for the lending attitudes of banks improved in the first quarter 2011 for the eighth consecutive period. This upward momentum, however, may be curtailed as banks might be required to reallocate resources toward post-quake reconstruction.

Real estate capitalization rates were already showing a recovery trend in Japan at the beginning of 2011, but we expect them to remain flat (or perhaps slightly wider for low-grade buildings) through the fourth quarter of 2011. Foreign capital is expected to stay on the sidelines for new investment at least until the nuclear radiation issue appears to be firmly under control. Fundraising activities became inactive, leaving less capital available for investment activities. Also, finance conditions for non-reconstruction-related sectors could be affected during the year.

7. Real Estate Fundamentals

Real estate fundamentals are improving globally. Economic growth is giving businesses reason to expand and although this is occurring slowly in many markets, recovery is expected to accelerate through 2011. Improvement in market fundamentals is partially due to the lack of new supply coming online within the next couple years, enabling increased demand to push vacancies down quicker than otherwise. Market conditions and conservative lending standards prevented new construction during 2009, and therefore any new supply not planned before the recession will not likely come online within the next two years

While there are substantial differences between the regions, there are a few similarities within commercial real estate investing that all markets share. As the global recession was coupled with a financial crisis, debt financing was difficult to find in most markets, preventing meaningful amounts of new construction. There are a few metros that have had large amounts of supply come online in 2009 and 2010, but the majority of these projects were planned before the downturn. The largest supply risks are currently in emerging Asia where demand seems continuous. However, national governments are becoming incentivized to moderate growth during the near term as worries of overheating persist.



Source: RREEF

As of May 2011.

Real estate fundamentals are improving globally and all property types and regions are in recovery. Retail assets in Asia Pacific and apartment properties in the United States are all moving into the growth part of the cycle as well. Supply risk will be highest for these two

⁶ Back-to-back quarterly increases in new bank lending according to the Bank of Japan.

sectors and regions going forward. Fundamentals in Europe are in recovery, but the rate of growth is still weaker than in other parts of the world. Office space in the United States remains at risk, although this is less true for prime properties in the top markets. Risk remains biased to the upside for all regions and sectors, and recovery is expected to continue in 2011 and 2012, with expansion taking hold thereafter for most sectors and regions.

United States

Vacancies topped out in 2010 and absorption turned positive in all property sectors. Rents also bottomed in all sectors, while small increases are evident in the strongest markets. Apartment properties are experiencing an exceptional comeback due to pent-up household formations and lower homeownership rates, and following strong occupancy gains, rents are nearly to the previous peak levels. Lease structures and terms are playing a role in the recovery of each sector. Apartment NOI is growing as the short lease terms allow landlords to raise in-place rents to market rates annually, but other property types will lag in income growth as tenants roll out of leases made during the cycle peak. However, many industrial, office and retail property owners agreed to blend-and-extend leases during the downturn, causing NOI to decline earlier than it would otherwise.

U.S. Vacancy Rate Trends

	Actual				Projected				
	2007	2008	2009	2010	2011	2012	2013	2014	2015
Apartment	5.8%	6.8%	8.2%	6.7%	5.9%	4.8%	4.1%	4.5%	5.5%
Industrial	9.7%	11.4%	13.9%	14.0%	13.4%	12.2%	10.9%	10.3%	10.2%
Office	12.6%	14.0%	16.3%	16.7%	16.1%	14.8%	13.4%	12.3%	12.2%
Retail	7.2%	8.7%	10.3%	10.8%	10.8%	10.4%	10.0%	9.5%	8.9%

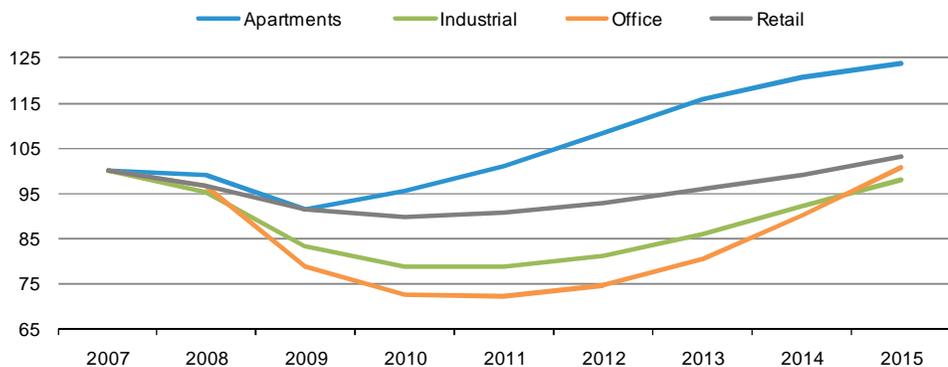
Sources: REIS, CBRE-EA (History) and RREEF (Forecast).

As of May 2011.

New supply should not be a risk for several years for industrial, office and retail properties, and only those buildings planned before the downturn will come into the base during the next year. The apartment sector has a slightly different story. Multifamily permits increased slightly early in 2011 and announcements of new projects under construction are spreading. However, construction that begins today will not be ready for another 18 months for occupancy, so even this product type will have some time to recover before a risk of new supply hits the market.

RREEF Indexed Rent Forecast

2010 = 100



Note: Apartments and Office rent growth are converted to NNN in this chart. Retail and Industrial are normally quoted as NNN Rents in the United States, while Apartments and Office are normally gross of expenses.

Sources: REIS, CBRE-EA (History); RREEF Research (Forecast).

As of May 2011.

Rent increases will come early for apartments, but later and stronger for the other sectors. Occupancy gains and nascent job growth are pumping up rents for multifamily properties, but rent growth will cool as net absorption slows later in the forecast. On the other hand, retail will have only slow rent growth until retailers begin expansion in 2012, leading to stronger rent growth in 2013. Office and industrial, which will have slower growth early on as vacancy is much higher for these sectors, will outperform in the later years when job growth accelerates. The five-year average rent growth will be highest for office and industrial properties, while retail and apartments, on average, will have slower rent growth. Note, however, that our property market operating outlook is somewhat different from our real estate return outlook, which reflects strong capital returns for industrial and retail in the early years, as capital is moving into the sector in anticipation of improving income growth.

Cycles are moving faster than ever and the upside of higher rents and lower occupancy are matched with downside risks of excess new supply after 2015. If property markets are able to reach a cyclical low by 2015, capital will continue to move along the risk spectrum. Excess equity and debt could lead to inflated property values and additional supply. This risk should be monitored by both domestic and international real estate investors.

U.S. Apartments

The apartment sector in the United States recovered impressively over the past 12 to 18 months, exceeding investor expectations. Vacancy rates declined an unprecedented 140 basis points in 2010 amid record absorption and modest new supply. Effective rents posted sizable gains as landlords significantly reduced market-bottom concession packages. Investor exuberance for the sector continues as capitalization rates for premium apartment communities recompressed to pre-recession levels. Debate over the future of the GSEs will continue to make headlines in 2011. However, final legislative reform is unlikely until after the 2012 elections, creating continued risk. This asset class is expected to remain the preferred sector for institutional investors in 2011, given the widely held belief that a recovering economy and favorable demographic trends will continue to drive occupancy gains and strong near-term rent growth. However this sector seems fully priced, particularly in the top-tier markets. Supply risks are also emerging, with multifamily permitting on the rise again as re-energized developers are getting back in the game. Fortunately, the quantity of new deliveries is unlikely to curb strong rent growth before 2014.

U.S. Industrial

After two years of distress, industrial market fundamentals in the United States stabilized in the second half of 2010. The national vacancy rate peaked at 14.6 percent in the second quarter, nearly five percentage points higher than the low watermark level from the past cycle. Positive net absorption of 40.1 million square feet in the third and fourth quarters, and only modest new development, helped push vacancy down to 14.3 percent at year-end. Oversupply conditions persisted in most markets but leasing activity increased.

The economic and property market landscape is growing more favorable. First quarter evidence suggests that initial positive momentum achieved in 2010 is carrying over into 2011, with vacancy falling to 14.1 percent. Warehouse space in global gateway markets and warehouse and flex space in technology centers are early beneficiaries.

It will take several years before the broad U.S. industrial market enjoys a full recovery. Even though we expect that strong demand will begin in 2012, the current oversupply is large, so it will likely take several years before a majority of metro markets achieve equilibrium availability rates. High barrier markets and submarkets are expected to recover ahead of American averages.

U.S. Office

Net absorption turned positive in 2010 as the office sector finished with 17 million square feet in occupancy gains for the year, a surprising reversal of momentum from the negative demand carried into the beginning of the year. Tenants took advantage of rock bottom rents, companies stepped off the sidelines to sign deals, and large users flexed their muscles to negotiate favorable blend-and-extend terms well in advance of expirations.

Limited new deliveries kept supply only a small step ahead of demand, and vacancy ticked up

only 10 basis points to 16.4 percent during the year. While vacancy increased slightly, sublease space declined during the year, but has not been as significant a problem as during the dot-com bust. Despite the increased leasing activity, underlying fundamentals are still struggling as the market scrapes bottom.

Deliveries in 2011 will recede further on their way to an historical low in 2012. Most markets will see a virtual shut-down of construction. Demand is likely to pause in the first half of 2011, as the market takes a breather from overly optimistic growth during late 2010. Nonetheless, absorption in the United States in 2011 is expected to surpass 2010, but remain lukewarm, totaling between 20 million to 30 million square feet.

By the end of the five-year forecast, the average rent for the U.S. office market is expected to return to its last peak in 2008. Leading metros are expected to recover to levels beyond their last peak, while markets affected most by the housing bust and/or overbuilding are expected to require until after 2015 to return to peak rents.

U.S. Retail

Retail vacancy rates began to stabilize in 2010 in the United States, with better markets and centers seeing the start of recovery. At the same time, the downturn has pushed many retail centers nationally into failure, with tenants vacating weaker centers, often to the benefit of stronger centers. As a result, retail centers in top locations with strong tenancy will improve their performance in the coming years, while weaker centers will continue to struggle.

The worst is behind us. Vacancy rates likely peaked and are trending down due to fewer new additions to the supply as well as nascent and growing demand. For the first time since the onset of the recession, actual and announced store openings exceed store closings and this trend will likely accelerate beginning in 2012. Construction is likely to remain moderate for at least the near term, setting the foundation for occupancy gains. Stabilization will continue in 2011 and vacancies will likely begin to fall in earnest starting in 2012. Vacancy rates will likely fall below 9 percent by the end of 2015, about 200 basis points below the current level. Rent growth will likely moderate as well, averaging 3 percent, with much of the growth coming in the later years.

Malls are emerging as the first retail sub-sector to recover in the United States, after being the first into recession, as this type relies heavily on apparel, electronics, and near-luxury goods. Grocery-anchored neighborhood and community centers maintained relative stability in terms of both increased vacancy and rent losses during the downturn, and are now ready to resume growth. Unanchored centers and poorly-located lifestyle centers fared badly during the downturn, as well as secondary malls. Power centers that house many of the nation's big-box retailers performed the worst during the downturn. However, those well located power centers that retained or attracted the dominant surviving discount retailers are extremely well positioned for the future. When vacancies occur, these centers will likely have competing bids from retailers who have found themselves in failing locations.

Europe

Europe Industrial

The European logistics sector stabilized in 2010, in line with global economic trends. Trade in Europe is recovering quickly, but growth remains well below the heady levels experienced between 2002 and 2007. The outlook for trade volume growth is relatively strong during the next five years, which is about half the level experienced in the years leading up to the market peak in late 2007. In addition to positive trade growth, the outlook for eurozone industrial production is promising, which should further support a recovery in industrial real estate demand.

Over the broader European context, the generally favorable trends of improving take-up and limited new supply have led to the beginning of what will likely be looked back upon as the stabilization period of the European logistics rental market during the second half of 2010. Modern logistics absorption remains heavily dominated by demand from third party logistics operators with total take-up trends continuing to show signs of modest improvement. This dynamic is particularly noticeable in the Central European markets of Warsaw and Prague as well as the port-based markets in the Benelux and in Hamburg. While demand trends are

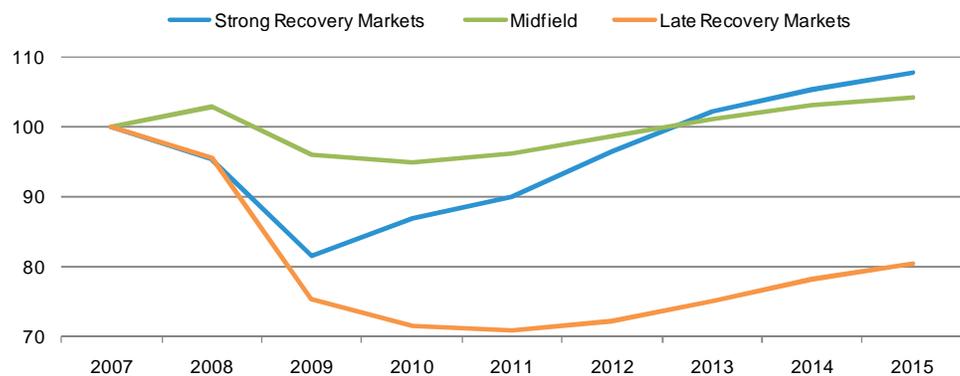
improving, space under construction has essentially come to a halt. The Central European countries and the United Kingdom continue to suffer from high vacancy rates due to the supply overhang from speculative development completed during the peak years. Spain also remains oversupplied as the economic uncertainties continue to hamper a recovery in demand.

RREEF is forecasting prime headline industrial rental growth to be relatively small as modest declines during the correction limit the upside and we believe a fully fledged recovery in logistics demand will be delayed. It is worth noting that this sector has seen significant use of incentives and although asking rents did not see massive declines, the effective rent growth story is far more dynamic through this cycle.

Europe Office

The impact of the economic downturn on the European office market proved to be milder than originally expected. On average, rents declined by about 10 percent, although the variation was significant ranging from over 40 percent in Dublin and London West End to relatively flat in regional France. The majority of markets stabilized or entered the recovery phase during 2010. The relatively resilient labor market led to net absorption turning positive by the end of the year and the overall increase in vacant space was less than in the previous two cycles. This cautiously optimistic aggregate picture masks significant disparity between markets across the continent.

European Office Market Rental Growth Rates



Note: Growth rates are in reference to prime rents.
Sources: RREEF Research, PMA.

As of May 2011.

Variation between markets continued to widen in early 2011. Several markets, most notably London, are already in the advanced stages of recovery while others remain on a downward path. The latter group is driven largely by the level of distress of national economies and, not surprisingly, markets in Spain and Ireland are lagging the rest of the continent. Between these two extremes, a large group of important office markets have reached the bottom of the cycle and are moving towards a slow but steady recovery from 2011. The near future will likely see a slow but accelerating recovery across most of Europe driven by returning tenant confidence and space demand as well as limited supply, which is expected to reach a 20 year low in 2011 and 2012. While this should lead to stronger rent growth in 2013 and 2014, the pace will likely slow in 2015 or later as construction activity returns. However, the current fragile economic situation in a number of over-indebted European economies creates significant downside risks for the recovery path assumed in our main scenario. A major fundamental shock could significantly prolong the cyclical downturn or even lead to a double dip.

In general, the office sector in the CEE has responded strongly to the economic recovery with several markets clearly emerging from the bottom of the cycle and well positioned for growth. Occupier demand is driven mainly by lease renewals and negotiations, and landlords (as in the Western European markets) remain under pressure to offer incentives to secure tenants. Rents have bottomed in several markets but individual countries are at different points of the cycle. Poland's office markets reached the recovery stage early due to the healthy underlying fundamentals and the positive market outlook. Rising demand combined with low completions led to a further decline in vacancy, and rents bottomed out during 2010. The office markets of Prague and Budapest are in the consolidation stage, with both having suffered from weak

demand in 2009 and 2010. Although market fundamentals seem to be fragile, prime rents remained stable through 2010 in Prague, although there were further declines in Budapest. In the near future we will see continuing recovery in Warsaw and Prague due to the positive economic outlook and we expect strong rental growth with rising completions combined with lowering growth of the economy smoothing rental growth after 2013. The office market in Budapest will see another year of weak market fundamentals as a result of the relatively fragile economic environment with positive rental growth forecast beyond 2012.

European Vacancy Rate Trends

	Actual				Projected				
	2007	2008	2009	2010	2011	2012	2013	2014	2015
Europe - Office	8.4%	8.8%	10.7%	11.3%	10.6%	9.9%	9.4%	9.0%	8.8%
Western Europe - Office	8.5%	8.9%	10.6%	11.2%	10.5%	9.8%	9.4%	9.0%	8.8%
UK - Office	9.4%	11.4%	13.3%	13.1%	12.0%	11.1%	11.0%	10.2%	9.2%

Sources: PMA (History) and RREEF Research (Forecast).

As of May 2011.

Europe Retail

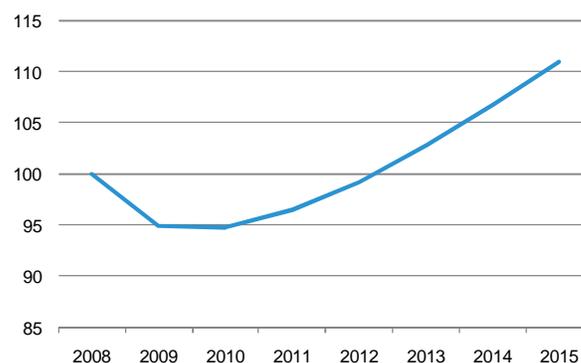
Prospects for the European retail property sector are highly diverse. Western European retail sales growth remains weak both in absolute terms and relative to GDP. However, individual market prospects deviate sharply from average outlook, reflecting important differences throughout the region. Drivers of the differences in spending include the degree of deleveraging pressure on both governments and households and the innate consumer culture of the people within each market. As a result the degree and timing of rental growth varies widely across the European region.

Risks from new product entering the market are largest in some of the weakest markets, while some markets with large pipelines of potential supply are actually hosting little new construction. Total supply pipeline figures for Europe are ostensibly large, but mask low completion expectations given the continuing wave of cancellations, postponements and even stoppages of schemes under construction. Given a lagged supply response, this will assist in rental stabilization in the short term and will be an important component of both rental sustainability and growth in the medium term for all markets. Moreover, it will help to restore the European retail sectors' defensive investment qualities.

As a result of the weaker retail environment combined with the lower availability and higher cost of capital, retailers store expansion plans remain at less than 50 percent compared to the peak of the market. This manifests itself in a polarization of primary and secondary shopping centers along the multiple dimensions of location, scale and quality. Across all markets, there will be winning and losing retail locations reflecting the strength of the micro-market, the quality of the scheme and its retail offer, and its positioning within the wider competitive market. Stock selection is critical.

Prime shopping center nominal rents stabilized in most markets by the end of 2010, with the exception of the weakest markets which may see further, but limited, decline in 2011. While economic growth has returned earlier than expected and supply will remain constrained, it is not likely to translate into strong rental growth. The ongoing pressure to deleverage and rebuild savings across economic sectors, together with weak retailer confidence with respect to expansion, will result in modest growth in even the strongest markets. Given the strong difference in the underlying drivers of the retail economy across markets, the speed and strength of recovery will differ markedly.

European Retail Market Growth Rates



Note: Growth rates are in reference to prime rents.

Sources: RREEF Research, PMA.

As of May 2011.

The impact of the financial crisis for the CEE markets was marginal compared to Western Europe. Retail sales were negative in all markets within the sub-region in 2010 with the exception of Poland. As a consequence retailers are more cautiously implementing new store opening programs. In Hungary and the Czech Republic new market entries were quite limited in 2010. In both countries competition between the existing centers is strong and only the most prime centers are proving successful in attracting new retailers. On the other hand both countries have high street retail, which stand in competition to the shopping centers. Even in the current environment, retailers still find it challenging to secure new locations in prime markets. In 2010, rents continued to decline in Hungary as a result of the weak underlying economy, while rents stabilized in the Czech Republic. The impact of the economic crisis on Polish retail was marginal, as retail sales turning slightly negative in 2009, but rose by 3.5 percent in 2010, the result of strong demand and a muted supply pipeline and new brands seeking to secure prime locations. The outlook from 2011 onwards is strong especially in Poland and the Czech Republic. Both countries will see the highest rental growth within Europe, while Hungary still suffers from structural problems. Rental growth expectations in Hungary are slightly under the European average of 2.6 percent over the next five years.

Asia Pacific

Asia Pacific Vacancy Rate Trends

	Actual				Projected				
	2007	2008	2009	2010	2011	2012	2013	2014	2015
Industrial	8.2%	6.6%	8.1%	8.7%	8.8%	8.4%	6.9%	5.4%	5.5%
Office	3.7%	8.8%	11.8%	10.2%	10.8%	8.4%	7.7%	9.0%	8.2%
Retail	3.0%	3.2%	4.1%	3.6%	3.2%	3.7%	3.6%	4.2%	3.7%

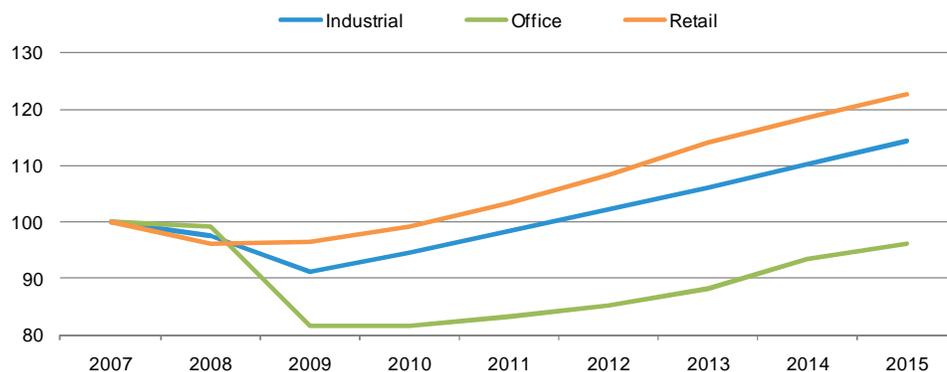
Note: Asia Pacific is inclusive of Japan and Australia in this chart.

Sources: JLL (History) and RREEF Research (Forecast).

As of May 2011.

Asian Rent Growth Rate (%)

2011 - 2015



Source: RREEF.

As of May 2011.

Asia Industrial

External trade in Asia, excluding Japan, rebounded considerably in 2010, supported by a recovering economy in developed countries and a deepening intra-regional economic integration where division of labor among different markets has promoted intra-regional trade flows. Rising household income also contributed to increased demand for warehouses and logistic facilities through increased retail sales.

The expected continued recovery of developed economies will lend support to industrial properties in China. Meanwhile the rise of the middle-class has translated into higher demand for retail sales and therefore demand for quality logistics facilities. Beijing and Shanghai would remain the major beneficiaries as they serve as the gateways to the most developed regions in the countries.

The rise of the Chinese economy and the deeper integration of Hong Kong into China's economy will underpin demand from trading and logistic companies for industrial space. The solid demand growth, however, will be matched with a reduced longer-term supply as the government rezones more industrial lands into residential use. Rents are therefore expected to maintain healthy growth in the next three to five years.

Meanwhile in Singapore, the global economic recovery has also brought back demand for high tech products, helping the industrial market to stage a strong rebound. Rents rose by 50 percent from the trough in 2010 and are now approaching the level of the last peak. As manufacturing, especially in the high tech space, is expected to remain competitive in the region, the export sector will likely remain buoyant and the industrial market favorable to investors.

Australia Industrial

The rising demand for commodities around the world, especially from China, underpins the demand for industrial properties in Australia, especially in resources-driven metros such as Perth and Brisbane. The industrial markets in Sydney and Melbourne benefited from a recovery in both labor market and consumer sentiment. Rent is starting to increase while supply is limited especially in Perth and Adelaide. However, speculative construction emerged in Sydney and Melbourne and both markets will have slightly slower rent growth during the near term.

With rising household income, which helps buoyant retail sales, the Australian industrial market is expected to grow steadily. Demand for commodities will likely remain strong in the near future amid strong economic growth in Asia Pacific. Limited supply yet strong demand growth should continue to underpin rental growth. In the meantime, yields are expected to tighten as both domestic and international investors are chasing for yield assets.

Note to reader: Japanese Industrial will not be discussed in this issue.

Asia Office

The rapid restoration of investor confidence by expansionary policies, as well as the strong rebound in financial markets and global trade activities, has limited corporate layoffs. Unemployment peaked in 2009 in most Asia Pacific countries and trended down thereafter, recently reaching the pre-crisis level. Strong economic growth, especially in China, continues to create jobs in the region, translating into solid office demand. In the meantime, closer economic ties among the Asian economies, especially with China, have prompted businesses to expand hiring.

Hong Kong outperformed all other Asian markets and capital values surpassed the pre-crisis level in 2010 and rent levels are approaching the previous peak. Strong demand from the financial sector contributed to the revived absorption in the market-place. Being the international financial center of the second largest economy in the world, Hong Kong now serves not only foreign investors entering into China but also Chinese investors looking to invest abroad. Against this backdrop, office demand will likely remain strong, although capital values possibly will lag behind rentals due to potential capitalization rate expansion.

The expansion of both domestic and international corporations has also led to a strong rebound in office demand in Beijing and Shanghai. The two cities have gradually evolved into key financial centers in the region, with Shanghai challenging Hong Kong as the leading international financial center in China. Financial companies and trading companies continue to cluster in key CBD areas where land supply has become increasingly limited. Rentals are therefore expected to remain on an upward trend while capitalization rates will likely remain tight due to strong investment demand.

Singapore has also witnessed a gradual recovery in rentals and capital values. Expansion in both financial and professional services sectors have contributed to positive net absorption and corporate hiring is turning more positive. Being the international financial center in Southeast Asia, the financial and professional services in Singapore are expected to benefit from the rise of the neighboring economies, especially Indonesia. The coming large supply would limit near-term growth, however the longer term prospect remains bright.

The Seoul office market is starting to recover in line with the decline in the unemployment rate. However, the Seoul market, especially in CBD and Yoido, is witnessing a new wave of supply which has international specifications. Migration of corporate demand from lower quality buildings to higher quality buildings is expected in the near term, which would result in a below-trend rent growth. Nonetheless, pressure from abundant supply would be alleviated by expansion of the traditional small workstations and growing white-collar employment.

Australia Office

The Australian economy unemployment rate has recovered to the pre-crisis level after a short-term increase. Office demand has also recovered and rentals have started to grow across major cities. Similar to the Australian industrial market, the office market is witnessing a near-term supply trough at a time when demand recovers, especially in the key national economic centers of Sydney and Melbourne.

With the Australian economy expected to maintain a healthy growth of around 3.0 percent to 3.5 percent per annum during the next five years, white-collar employment is expected to expand steadily, which helps office rent growth positive. Longer term supply risks, especially in Sydney CBD, exist, however the realization of supply will likely be limited by the level of pre-commitment.

Japan Office⁷

In March 2011, the vacancy rate for newly developed buildings⁸ in Central Tokyo⁹ rebounded above the 20 percent level for the first time in five months. Similarly, the overall office vacancy rate in Central Tokyo reached 9.2 percent in March, its highest point thus far in the cycle. Deutsche Bank's economists expect unemployment to continue to rise further due to the earthquake, indicating that soft office demand will persist during the year. Overshadowing the already weakening fundamentals is a surge of new office supply expected in 2011 and 2012 in Tokyo. Because of weak demand and new supply, a significant recovery is not expected in the vacancy rate in Tokyo until 2012.

The average asking rents for benchmark properties have declined for the 31 consecutive months through March 2011, falling 23.5 percent from their peak. With a surge of new supply on the way by 2012, demand will soften further, causing asking rents for benchmark buildings to come under pressure. These changes in market fundamentals, however, will occur unevenly and may vary across unique building specifications going forward. Old, low-grade buildings will suffer more than new, high quality, quake-resistant, energy efficient buildings.

Asia 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 from 2011 to 2015, is widely anticipated to steer China toward a more consumption oriented economy. A few of Asia's major shopping center markets had already edged into recovery by late 2009 and more markets joined them in recovery in 2010.

For the mature Asian markets, the downturn in rent growth was relatively tame. Economic growth from China translated into tourism for Hong Kong while new casinos in Singapore became a saving grace for the city-state. Neither Australia nor Seoul suffered from too much distress and will likely expand at a rate of 3 percent to 4 percent per year through the end of the forecast period. New supply should not be a major issue in the near term.

Rising levels of affluence in emerging Asian markets, especially in China and India, have lured retail developers who anticipate a continuously expanding pool of new consumers. During the recent downturn Shanghai's retail market proved particularly adept at minimizing disruptions to shopping center fundamentals. Construction delays and postponements prevented supply from being a risk, and Shanghai's retail rents continued to rise marginally in 2009. While Chinese markets only declined in rents marginally, this was not the case in India.

Ample construction undermined Indian retail fundamentals during this cycle, especially in Mumbai and Delhi, where rents were cut by as much as 50 percent. Initially, the global economic crisis created an atmosphere of uncertainty that put many retailers on the sidelines. With India's economy now growing again at record pace, several chains, including Carrefour and Cartier (France), Gap (United States), Godrej (India) and Yishion (China) are beginning to expand again.

⁷ For a closer look at the Japanese real estate market, see the Japan Real Estate First Quarter 2011 report from RREEF Research, available at www.rreef.com in early May.

⁸ Newly developed buildings are those completed within the last 12 months.

⁹ Central Tokyo is defined here as the central five wards (or "ku") of Chiyoda, Chuo, Minato, Shinjuku, and Shibuya.

Australia Retail

The Australian retail market has traditionally been resilient and it exited the global financial crisis relatively unscathed. Occupancy has been rising steadily with vacancy rates of regional and sub-regional centers in major cities maintained at low levels.

Supply is expected to trend down again in the next three to five years. Coupled with recovered consumer sentiment, the retail market is expected to maintain its trend growth. Vacancy is expected to hover at the historical low levels.

Japan Retail

Soft consumer spending is resulting in demand problems for the shopping center sector. Before the earthquake, RREEF was forecasting recovery in 2012 with modest rental growth through 2015, 2 percent to 4 percent growth per annum. This forecast assumed growth from tourism, but it is too early to tell if fears will dissipate quietly or remain for some time.

The average asking retail rents for major high streets rebounded in Tokyo in the Omotesando, Shinjuku, and Shibuya submarkets in the fourth quarter when consumer confidence showed signs of a recovery, while it has been stable at around JPY 30,000 per tsubo in Ginza for the last 15 months. Early reports indicate that high street retail sales plummeted after the quake, and this weak trend in retail sales in Tokyo is expected to persist at least for a short period of time, causing rents to resume a downward trend again in 2011.

Sales at shopping centers, department stores, and chain stores in January and February 2011 (on an existing store basis) were relatively flat compared with the same period in the previous year. Nikkei RIM's consumption forecasting indicator (CFI)¹⁰, a survey that predicts future consumption trends six months in advance, remained above the 80-point index value for the eighth consecutive month in February 2011, but as indicated by the Economy Watcher Survey, retail sales are expected to plummet during at least the near term. Western Japan, such as Osaka, is expected to be less affected than Eastern Japan.

¹⁰ The CFI is based on a weighted monthly survey of up to 600 working-age adults (age 20 to 69) in the Tokyo metropolitan area. December 2004 = 100.

8. Appendix I: Return & Risk Table Metros

Metros Included in the Return-Risk Table			
Atlanta	A,I,O,R	Amsterdam	O
Boston	A,I,O,R	Brussels	O
Chicago	A,I,O,R	Frankfurt	O
Dallas	A,I,O,R	Hamburg	O
Los Angeles	A,I,O,R	London: City	O
Miami / Fort Lauderdale	A,I,O,R	London: West End	O
NYC (Northern N.J.)	A,I,O,R	Madrid	O
San Francisco	A,O,R	Milan	O
San Jose	A,I,O,R	Munich	O
Seattle	A,I,O,R	Paris: La Defense	O
Washington, D.C.	A,I,O,R	Paris: CBD	O
		Stockholm	O
		Warsaw	O
Beijing	I,O,R		
Hong Kong	I,O,R	France	R
Kuala Lumpur	I,O,R	Germany	R
Melbourne	I,O,R	Italy	R
Seoul	I,O,R	Netherlands	R
Shanghai	I,O,R	Spain	R
Singapore	I,O,R	Sweden	R
Sydney	I,O,R	Poland	R
Tokyo	I,O,R	U.K.	R

Appendix II: Definitions

Capitalization Rates: The ratio between net operating income (annualized) and the property value.

Equivalent Investment Yield: The percentage return on sale price or estimated value derived from the net passing income and increases or decreases to current market rents.

Initial Yield: The percentage return on property investment assuming (i) the property is leased immediately with the prevailing effective rent, and (ii) a full occupancy. Transactions costs of purchasing or leasing of space are not included.

Passing Yield: The percentage return on property investment assuming (i) the property is leased with the average effective rent over a usual rental review period, and (ii) a full occupancy. In the case of a two year rental review period, for example, the average effective rent is calculated by averaging the effective rent of current quarter and the effective rents of the past seven quarters. Transaction costs of purchasing or leasing space are not included.

1 Square Meter ~ 10.8 Square Feet ~ 0.3 Tsubo

Total Return: Total return for years in the period is the sum of (i) capital value change in the year, and (ii) the average of initial yields (assume 100% occupancy) of the current year and the previous year. Transactions costs, leverage and hedging costs, operating expenses, capital expenditures, and depreciation are not included.

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