

THE SIGNIFICANCE OF CAPITAL FLOWS INTO THE AUSTRALIAN COMMERCIAL PROPERTY MARKETS

GRAEME NEWELL

University of Western Sydney

VALERIE KUPKE

University of South Australia

STANLEY McGREAL

University of Ulster and University of South Australia

ABSTRACT

Capital flows to Australian commercial property have been US\$67 billion over the 2007-2011 period. This places Australia as the sixth most active property market globally. Using the extensive Real Capital Analytics database, this paper examines these Australian property capital flows in a local, Asia-Pacific and global context. The dynamics of these property capital flows are also assessed by major cities, property type and investor type. Overall, Australia is found to be an important commercial property investment market at both a local, Asia-Pacific and global level, with strong investor support from both domestic and international property investors as part of their property investment strategies.

Keywords: Australian commercial property, capital flows, global significance, Asia-Pacific significance, international investors, property investment strategy

INTRODUCTION

The case for commercial property as an important asset class in an institutional portfolio has been well established. This includes both domestic and international property in a mixed-asset portfolio (Bond et al 2003; Hoesli et al 2004; Ling and Naranjo 2002). This has seen major property fund managers establish commercial property portfolios in excess of US\$1.6 trillion in total (for example, CBRE Global Investors, RREEF, Pramerica, LaSalle) (I&P RE 2012). Major players in commercial property investment have included REITs, pension funds, sovereign wealth funds, private equity funds and high wealth investors in both a local and international context. For example, property typically comprises 5-10% of a pension fund portfolio in the mature economies (Newell, 2010).

In an Australian context, the Australian property funds management sector has over \$300 billion in assets under management, including major commercial property portfolios for Westfield (\$50 billion), AMP (\$25 billion) and Colonial First State (\$20 billion) (PIR, 2011). Similarly, superannuation funds in Australia have an average of 10% property in their portfolios, comprising 7% unlisted property and 3% listed property, compared with only 8% property in their portfolios in 2004 (APRA 2012b).

The strategic benefits of commercial property in a mixed-asset portfolio include portfolio diversification, inflation-hedging, low risk and strong risk-adjusted returns (Newell 2005). Numerous studies have shown these benefits to be evident for Australian commercial property (eg: Higgins 2010, 2011; Lee and Higgins 2009; Leung 2010; Newell 1996, 2005, 2007c,d; Newell and Lee 2011a,b), as well as for various international markets (eg: Hoesli et al 2004; Lee 2005; Lee and Stevenson 2006; Stevenson 2004). These benefits of Australian commercial property have been further enhanced by Australia having one of the most transparent commercial property markets globally (JLL 2012a).

Social profile:

Population:	22.0 million
Urban population:	89%
Major cities:	Sydney (4.4 million), Melbourne (3.9 million), Brisbane (2.0 million), Perth (1.6 million)

Economic and financial profile:

Labour force:	12.1 million
GDP:	\$1.5 trillion; #13 globally
GDP per capita:	#5 globally
GDP growth:	2.9%
GDP sectors:	Agriculture (4%), industry (25%), services (71%)
Unemployment:	5.1%
Inflation:	2.3%
Global business competitiveness:	#20 globally
Corruption perception:	#9 least corrupt globally
Stock market:	US\$1.2 trillion; 2.5% of global market cap; 10 th largest stock market globally
Superannuation fund assets:	\$1.4 trillion; 5 th largest globally
Sovereign wealth fund:	Australian Future Fund: US\$80 billion; #13 globally

Social, Economic and Financial Profile of Australia: 2012
Sources: APRA (2012a), CIA (2012), EPRA (2012), JLL (2012b), SWFI (2012), TI (2011), WEF (2011), WFE (2012)

Table 1

In this overall context, Australian commercial property is seen as an attractive investment for local and international property investors. This is particularly so, given the strong economic climate and positive market fundamentals in Australia in recent years post-GFC compared to the ongoing economic uncertainty in the US and the major sovereign debt issues in Europe. As such, it is important to understand the dynamics and significance of Australia in a commercial property context. This paper examines the significance of Australian commercial property capital flows over 2007-2011 in a local, Asia-Pacific and global context by assessing over 72,000 global commercial property transactions at US\$3.3 trillion in transaction value from the Real Capital Analytics (RCA)

database. The dynamics of these property capital flows are also assessed by major cities, property type and investor type to further highlight various strategic property investment issues.

SIGNIFICANCE OF COMMERCIAL PROPERTY IN AUSTRALIA

To highlight the stature of Australia in an investment context, Table 1 provides a general social, economic and financial profile of Australia in 2012.

Overall, Australia is seen to provide a strong economic framework to underpin the commercial property sector, with sustained GDP growth and global business competitiveness. The Australian stock market is the tenth largest globally, with the superannuation sector being the fifth largest globally.

Table 2 provides the commercial property profile of Australia in 2012. High levels of investible property and significant property market transparency (#3 globally) (JLL 2012a) are supported by a clearly defined property investment environment regarding property tenure, taxation and legal structure (JLL 2011), as well as an active and robust property funds management sector (PIR 2011).

Investible property:	US\$656B; 2.5% of global property; #11 globally
Property market transparency:	#3 globally; “high transparency” rating
Office stock:	23.8 million sqm; comprising CBD office (16.3million sqm) and non-CBD office (7.5million sqm); vacancy rate = 7.9%
Property funds management:	Over 550 property funds with \$302 billion in property assets
Major property fund managers:	Westfield (\$50billion), AMP (\$25billion), CFS (\$20billion), Goodman (\$19billion), Stockland (\$15billion), GPT (\$15billion), DEXUS (\$14billion), Lend Lease (\$10billion)
Listed property sector:	#6 globally; 4.4% of global market cap
REITs:	#2 globally; 9.9% of global market cap
Listed property sector:	19.7% of total property; #2 globally
IPD property index:	1985-2012; 1700 properties valued at \$135billion; 73 property funds
Leading property professional associations:	Australian Property Institute, Property Council of Australia, RICS, Urban Development Institute of Australia

Property Profile of Australia: 2012

Sources: EPRA (2012), IPD (2012), JLL (2012a), Macquarie Securities (2011), Pramerica REI (2012), PCA (2012), PIR (2011)

Table 2

The securitized property market includes A-REITs which is the second largest REIT market globally (only exceeded by US REITs), with Australia also having the second highest level of listed property (versus total property) globally (only exceeded by Hong Kong). Superannuation funds in Australia have seen commercial property as a key asset class in their portfolios, utilising a range of listed and unlisted property investment vehicles to achieve this property exposure (Newell 2007a,b, 2008; Newell and Lee 2011b) including unlisted wholesale property funds and property securities

funds. High levels of property professionalism are also achieved by the active role of the API, PCA, RICS and UDIA, as well as international standard commercial property performance indices provided by IPD. This sees Australia as one of the most mature and sophisticated commercial property markets globally.

The engine room for this strong economic and financial environment and activity is the Australian office market. With 23.8 million sqm of office space in Australia, the significant role of the Sydney CBD office market (30% of Australian CBD office market), Melbourne CBD (26%), Canberra (14%), Brisbane CBD (13%) and Perth CBD (9%) is clearly evident in the CBD office markets. The Australian office market vacancy rate of 7.9% (January 2012) has reduced from 9.0% in July 2011 (PCA 2012).

The above social, economic, financial and property profile has provided a strong, positive environment for commercial property investment in Australia for both local and international property investors. This has recently been driven by increasing capital values, rental growth, transparency, economic growth, positive market fundamentals, improved market confidence and a strong Asia connection (JLL 2012c). A full analysis of global commercial property transactions over 2007-2011 will be presented in the subsequent sections of this paper to highlight this Australian commercial property transaction activity in a local, Asia-Pacific and global context.

METHODOLOGY

Global commercial property transactions were assessed over 2007-2011 using the Real Capital Analytics (RCA) database. RCA is an independent US-based property research organisation who track the sale of commercial property value (and development sites) of at least \$10 million each for over 75 countries in the Americas, Europe, Middle East and Africa and Asia-Pacific (including Australia). Over the 5-year period of 2007-2011, this extensive RCA commercial transactions database comprised 89,345 transactions at US\$3,295 billion (\$3.3 trillion) in transaction value, representing the largest and most comprehensive commercial property transactions database available globally. Data prior to 2007 is not available. The RCA database has been used previously for research involving transaction activity during the GFC in Asia (Newell and Razali 2009) and during the GFC in Europe (Newell et al 2010).

For the analyses in this paper, only commercial property transactions (ie: office, retail, industrial, hotel, other) were considered, with development sites excluded. This resulted in 72,191 commercial property transactions at US\$2,342 billion (\$2.3 trillion) being analysed. This saw a comprehensive coverage across the various countries, enabling a rigorous analysis of commercial property transaction activity in Australia to be effectively placed in an Asia-Pacific and global context. The analyses of the RCA database in this paper go well beyond just reporting the transactions data, there is a strong value-adding element of critical analysis to articulate the significance of the investment trends for commercial property transaction activity in Australia over 2007-2011. As such, the scale and depth of this analysis of the Australian commercial property transactions sees this paper as the most rigorous and incisive analysis of the Australian commercial property investment landscape yet conducted. Because international comparisons are needed in the analyses, all transaction volumes are given in US\$.

COMMERCIAL PROPERTY TRANSACTIONS IN AUSTRALIA: 2007-2011

Table 3 provides summary details of this commercial property transaction activity over the five-year period of 2007-2011 for Australia, Asia-Pacific and globally. Overall, this saw over 72,000 transactions at over \$2.3 trillion globally. The impact of the GFC in 2009 is clearly evident, with global transaction activity reducing by 57% (by number) and 77% (by value) compared to pre-GFC activity in 2007. Whilst some post-GFC recovery is evident, global transaction values in 2011 are still only 49% of the 2007 pre-GFC transaction value.

	2007	2008	2009	2010	2011	2007-2011
Number of transactions:						
Australia	385	189	202	265	394	1,435
Asia-Pacific	1,584	1,335	1,097	1,419	2,105	7,540
Global	19,375	15,086	8,427	13,764	15,539	72,191
Value of transactions (US\$ billion):						
Australia	\$28.0	\$6.9	\$6.2	\$11.8	\$14.2	\$67.1
Asia-Pacific	\$102	\$74	\$56	\$75	\$96	\$403
Global	\$921	\$409	\$210	\$350	\$452	\$2,342
Percentage of global transactions:						
Australia	2.0%	1.3%	2.4%	1.9%	2.5%	2.0%
Asia-Pacific	8.2%	8.8%	13.0%	10.3%	13.5%	10.4%
Global	100%	100%	100%	100%	100%	100%
Percentage of global transaction value:						
Australia	3.0%	1.7%	3.0%	3.4%	3.1%	2.9%
Asia-Pacific	11.1%	18.1%	26.7%	21.4%	21.2%	17.2%
Global	100%	100%	100%	100%	100%	100%

Commercial Property Transaction Activity: 2007-2011

Source: Authors' Analysis of RCA Database

Table 3

With 1,435 commercial property transactions over this period accounting for over \$67 billion in transaction value, Australia accounted for 2.0% of global transactions and 2.9% of global transaction value, with this percentage of global transaction value for Australia being in the range of 1.7% - 3.1% annually. The impact of the GFC in 2009 on Australia saw transaction value decrease by 78%, comparable to the global GFC decrease. Post-GFC, transaction value is still only 51% of the pre-GFC activity, marginally above the global recovery level.

The increasing significance of the Asia-Pacific region sees this region accounting for 17% of commercial property transactions over this period, reflecting the significant role of Japan, China, Hong Kong and Singapore. In comparison, North America accounted for 43% of global transaction activity (\$1,000 billion) and Europe accounted for 38% of global transaction activity (\$892 billion) over this five-year period. The impact of the GFC was less evident in the Asia-Pacific region, with transaction value dropping by 45% compared to North America (90% decrease) and Europe (67% decrease). Similarly, the post-GFC recovery in the Asia-Pacific region (94% of the pre-GFC levels)

is more significant than that seen in North America (36% of pre-GFC levels) and Europe (55% of pre-GFC values).

	2007	2008	2009	2010	2011	2007-2011
Transaction value (US\$ billion)	\$28.0	\$6.9	\$6.2	\$11.8	\$14.2	\$67.1
Global %	3.0%	1.7%	3.0%	3.4%	3.1%	2.9%
Global rank	#6	#14	#8	#8	#8	#6
Asia- Pacific %	27.5%	9.3%	11.1%	15.7%	14.8%	16.7%
Asia-Pacific rank	#2	#4	#4	#3	#3	#2

Significance of Australian Commercial Property Transaction Activity: 2007-2011

Source: Authors' Calculations from RCA Database

Table 4

Table 4 positions this Australian commercial property transaction activity more fully in a global and Asia-Pacific context over 2007-2011. In a global context, Australia accounted for 3% of transaction value and was the sixth most active international market over this period, only exceeded by US (#1), UK (#2), Germany (#3), Japan (#4) and France (#5). Australia consistently ranked #6 - #8 annually at this global level. At an Asia-Pacific level, Australia accounted for 17% of transaction value and was ranked #2, only exceeded by Japan, with Australia consistently ranked at #2 - #4 annually at an Asia-Pacific level.

Rankings and market shares for the transaction activity in the various leading countries are given in Table 5. At a 40% market share, the US is the dominant global market, although this market share reduced significantly in the GFC, with some recent recovery of the US global market share. The two leading markets of the US (40% market share) and UK (12% market share) account for over 50% of global transaction values, reflecting their significance as major international markets and destinations of both domestic and international property capital flows. Whilst Australia was the sixth most active international market, to put Australia in this global context at a relative level, Australia only accounted for 7% of US transaction levels, 24% of UK transaction levels, 40% of German transaction levels and 60% of France transaction levels (see Table 5).

At an Asia-Pacific level, Japan was the dominant market with a 31% market share, although the market share has reduced in more recent years with the growth in the other Asian markets. The 17% Asia-Pacific market share by Australia saw Australia only accounting for 53% of Japan transaction levels, with this Australian market share exceeding those of the other major Asia markets namely China (20% higher activity for Australia), Hong Kong (42% higher activity) and Singapore (71% higher activity).

	2007	2008	2009	2010	2011	2007-2011
Global significance:						
US	#1: 53%	#1: 31%	#1: 20%	#1: 31%	#1: 37%	#1: 40%
UK	#2: 11%	#2: 11%	#2: 17%	#2: 13%	#2: 11%	#2: 12%
Germany	#3: 7%	#4: 7%	#4: 7%	#3: 7%	#3: 8%	#3: 7%
Japan	#5: 4%	#3: 7%	#3: 8%	#5: 6%	#4: 6%	#4: 5%
France:	#4: 4%	#5: 4%	#5: 6%	#4: 6%	#5: 5%	#5: 5%
Australia	#6: 3.0%	#14: 1.7%	#8: 3.0%	#8: 3.4%	#8: 3.1%	#6: 2.9%
Asia-Pacific significance:						
Japan	#1: 32%	#1: 41%	#1: 31%	#1: 29%	#1: 26%	#1: 31%
Australia	#2: 28%	#4: 9%	#4: 11%	#3: 16%	#3: 15%	#2: 17%
China	#4: 9%	#2: 12%	#2: 20%	#4: 14%	#2: 18%	#3: 14%
Hong Kong	#5: 8%	#3: 10%	#3: 14%	#2: 16%	#4: 12%	#4: 12%
Singapore	#3: 13%	#5: 9%	#7: 4%	#5: 10%	#5: 11%	#5: 10%

**Global and Asia-Pacific Significance of Australian
Commercial Property Transactions (\$): 2007-2011**
Source: Authors' Calculations from RCA Database
Table 5

INTERNATIONAL SIGNIFICANCE OF MAJOR AUSTRALIAN CITIES

Based on commercial property transaction activity, Table 6 ranks the leading Australian cities in a global and Asia-Pacific context. In a global context, Sydney is the only top 20 ranked Australian city, being eighteenth globally in 2011 with \$6 billion. At an Asia-Pacific level, Sydney is currently ranked #6, followed by Melbourne (#9), Brisbane (#10), Perth (#12) and Adelaide (#17), seeing five Australian cities ranked in the top 20 Asia-Pacific cities. These rankings for the top Australian cities have improved in more recent years.

At a global level, New York (#1; \$34 billion), London (#2; \$29 billion) and Tokyo (#3; \$22 billion) were the major cities as destinations for domestic and international property capital flows in 2011. To put Sydney more fully in this global context, Sydney only accounted for 17% of New York transaction levels and 20% of London transaction levels.

At an Asia-Pacific level, Tokyo (#1; \$22 billion), Hong Kong (#2; \$11 billion), Singapore (#3; \$11 billion) and Shanghai (#4; \$8 billion) were the major cities for commercial property transactions. Sydney only accounted for 26% of Tokyo transaction levels, 50% of Hong Kong transaction levels, 53% of Singapore transaction levels and 74% of Shanghai transaction levels.

	2007	2008	2009	2010	2011
Global significance:					
New York	#1	#2	#5	#3	#1
London	#2	#3	#1	#2	#2
Tokyo	#6	#1	#2	#1	#3
Washington	#5	#7	#8	#6	#4
Paris	#7	#4	#3	#4	#5
Los Angeles	#3	#5	#9	#8	#6
San Francisco	#4	#12	#12	#9	#7
Sydney	#18	#48	#22	#16	#18
Asia-Pacific significance:					
Tokyo	#1	#1	#1	#1	#1
Hong Kong	#4	#2	#2	#2	#2
Singapore	#2	#3	#7	#3	#3
Shanghai	#10	#7	#4	#4	#4
Seoul	#6	#4	#3	#6	#5
Sydney	#3	#10	#9	#7	#6
Taipei	#11	#8	#5	#11	#7
Beijing	#5	#6	#6	#5	#8
Melbourne	#7	#12	#10	#8	#9
Brisbane	#9	#13	#11	#12	#10
Perth	#12	#14	#12	#13	#12
Adelaide	#18	#21	#16	#17	#17

International Significance of Major Australian Cities Transactions (\$): 2007-2011

Source: Authors' Analysis of RCA Database

Table 6

LOCAL SIGNIFICANCE OF MAJOR AUSTRALIAN CITIES

Table 7 highlights the contribution and local significance of the major Australian cities over 2007-2011. The dominant role of Sydney (\$22 billion over 2007-2011) sees Sydney accounting for 32% of transaction activity, with Sydney and Melbourne accounting for over 50% of total Australian commercial property transaction activity. Sydney has regained its market share, following a major loss of market share during the GFC. To further reinforce the dominant role of Sydney over this period, Melbourne only accounted for 63% of Sydney transaction levels, Brisbane only 49% and Perth 28%.

	2007	2008	2009	2010	2011	2007-2011
Value of transactions (US\$ billion):						
Sydney	\$10.1	\$1.4	\$1.0	\$4.4	\$4.8	\$21.7
Melbourne	\$5.3	\$1.3	\$1.3	\$2.2	\$3.6	\$13.7
Brisbane	\$4.3	\$1.1	\$1.0	\$2.2	\$2.1	\$10.7
Perth	\$1.8	\$0.6	\$0.8	\$0.9	\$1.9	\$6.0
Other	\$6.5	\$2.4	\$2.0	\$2.3	\$1.8	\$15.0
Percentage of total Australian transaction value:						
Sydney	36%	22%	17%	37%	34%	32%
Melbourne	19%	18%	21%	18%	25%	20%
Brisbane	15%	17%	16%	19%	15%	16%
Perth	6%	8%	13%	7%	13%	9%
Other	23%	35%	33%	19%	13%	22%
Ranking on transaction value:						
Sydney	#1	#1	#2	#1	#1	#1
Melbourne	#2	#2	#1	#2	#2	#2
Brisbane	#3	#3	#3	#3	#3	#3
Perth	#4	#4	#4	#4	#4	#4

Significance of Commercial Property Transactions in Major Australian Cities: 2007-2011
Source: Authors' Calculations from RCA Database

Table 7

SIGNIFICANCE OF PROPERTY SUB-SECTORS

The role of the property sub-sectors in these Australian commercial property transactions over 2007-2011 is shown in Table 8. With over \$39 billion in transaction value, office property was the leading property sector, accounting for 59% of transaction activity. This office market share decreased during the GFC, but has subsequently recovered its market share. Office and retail transactions accounted for over 80% of this transaction activity.

At an international level, 2011 saw Sydney as the twelfth most active office market globally, with Melbourne being the twenty-ninth most active office market globally. Amongst the other property sub-sectors, Melbourne retail was ranked #22 globally, compared with retail in Hong Kong (#1), London (#2), New York (#3) and Tokyo (#4). For the industrial sub-sector, Sydney industrial was ranked #5 globally, compared with industrial acquisitions in LA (#1), San Francisco (#2) and Chicago (#3).

	2007	2008	2009	2010	2011	2007-2011
Value of transactions (US\$ billion):						
Office	\$17.6	\$3.9	\$3.2	\$6.7	\$7.9	\$39.3
Retail	\$6.0	\$1.4	\$1.9	\$2.9	\$2.4	\$14.6
Industrial	\$2.5	\$0.6	\$0.6	\$1.4	\$2.1	\$7.2
Hotel	\$1.6	\$0.7	\$0.6	\$0.9	\$0.7	\$4.5
Other	\$0.3	\$0.3	\$0.0	\$0.1	\$0.2	\$0.9
Percentage of total Australian transaction value:						
Office	63%	56%	51%	56%	59%	59%
Retail	21%	20%	30%	24%	18%	22%
Industrial	9%	9%	8%	12%	16%	11%
Hotel	6%	10%	10%	7%	5%	7%
Other	1%	4%	0%	1%	2%	1%
Ranking on transaction value:						
Office	#1	#1	#1	#1	#1	#1
Retail	#2	#2	#2	#2	#2	#2
Industrial	#3	#4	#4	#3	#3	#3
Hotel	#4	#3	#3	#4	#4	#4
Other	#5	#5	#5	#5	#5	#5

**Significance of Commercial Property Types in Australian
Property Transactions: 2007-2011**

Source: Authors' Calculations from RCA Database

Table 8

SIGNIFICANCE OF DOMESTIC AND INTERNATIONAL INVESTORS

The strong economic climate and property market fundamentals have seen a positive property investment climate in Australia for both domestic and international investors. This has seen a high demand for core assets (eg: office), even given the strength of the Australian dollar for international investors (Brown 2011; JLL 2012c)

	2007	2008	2009	2010	2011	2007-2011
Office	66%	16%	35%	20%	41%	45%
Retail	82%	1%	28%	12%	47%	56%
Industrial	46%	6%	0%	15%	34%	30%
Total	68%	10%	29%	18%	41%	45%

Level of Cross-Border Investment in Australian Commercial Property: 2007-2011

Source: Authors' Calculations from RCA Database

Table 9

Table 9 highlights the significant contribution by cross-border investors in 2007-2011, accounting for approximately \$30 billion or 45% of transaction activity; particularly in the office and retail property sectors. Major property investors from Singapore, Canada, Germany, US, Malaysia and

South Korea have been active over this period, including major pension funds, sovereign wealth funds, private equity funds and property funds managers. This has included leading property investors, such as GIC, CIC, LaSalle, Deka, Brookfield, Canada Pension Plan, RREEF, Prudential, K-REIT, KWAP and NPS.

This Australian commercial property exposure has been achieved via a range of property investment vehicles including unlisted property funds, separate accounts and club deals. Club deals have recently taken on increased importance, as major investors seek alignment of interest and more control in the property investment process. This has included the privatising of the ING Industrial REIT portfolio in 2011 via a club deal involving Goodman (20%), Canada Pension Plan (43%), APG (25%) and China Investment Corp (12%), including two pension funds (Canada and Netherlands), one sovereign wealth fund (China) and a major Australian property investor. This trend has been further continued in 2012 with the privatising of the Charter Hall Office REIT using a club deal involving GIC and Canada Pension Plan.

PROPERTY INVESTMENT IMPLICATIONS

Australia is a significant commercial property investment market for both domestic and international property investors, reflecting its size, transparency, maturity, investor base, property market fundamentals and economic/property outlook at a local, Asia-Pacific and global level. Using a rigorous and incisive analysis of over \$2.3 trillion in transactions from the Real Capital Analytics database over 2007-2011, this research has enabled major research insights regarding the dynamics of commercial property transactions in Australia over this period in a local, Asia-Pacific and global context. This has seen Australia account for over \$67 billion in commercial property transactions over 2007-2011; being 3% of global transactions and seeing Australia as the sixth most active market globally over this period.

Importantly, this paper has highlighted the significant contribution of commercial property investment in Australia over recent years. This has seen Australian commercial property as an important investment for a wide range of investors including pension funds, sovereign wealth funds, private equity and property fund managers, having a key strategic role in the property portfolios for many domestic and international property investors.

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Email contact: g.newell@uws.edu.au