Real Estate Derivatives

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PRRES UTS Sydney 20 January 2009

On the pulse of
the property world

IPD

Why the initial difficulties in the UK?
… the problems

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- A lack of knowledge
  - Real Estate people about derivatives
  - Derivative people about Real Estate
- Index availability
- Timing of past pushes and strong one-way capital flows
- The Life Fund 'Catch 22'

  "The market is illiquid so life funds can't invest in derivatives… and ... because life funds can't invest in derivatives, the market is illiquid"
- Lack of clarity over tax treatment
  - Which regime, capital or income?
- A mismatch of knowledge and utility?
  - 'all property' contracts for multi-asset decisions
  - The link made through property fund managers
- Mandates

Source: Paul McNamara, Prudential Property Investment Managers (UK)

The advantages of going 'synthetic'?
...for UK property investors

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- Speed
    - Hours versus months
- Reduced cost
    - 1% versus 10%
- 'Accuracy'
    - Target allocation levels
- Flexibility
    - Moving in and out of real estate, sectors and segments
- Lack of hassle
    - Less people involved in the chain

Source: Robin Goodchild, LaSalle Investment Management

Notional Traded £m

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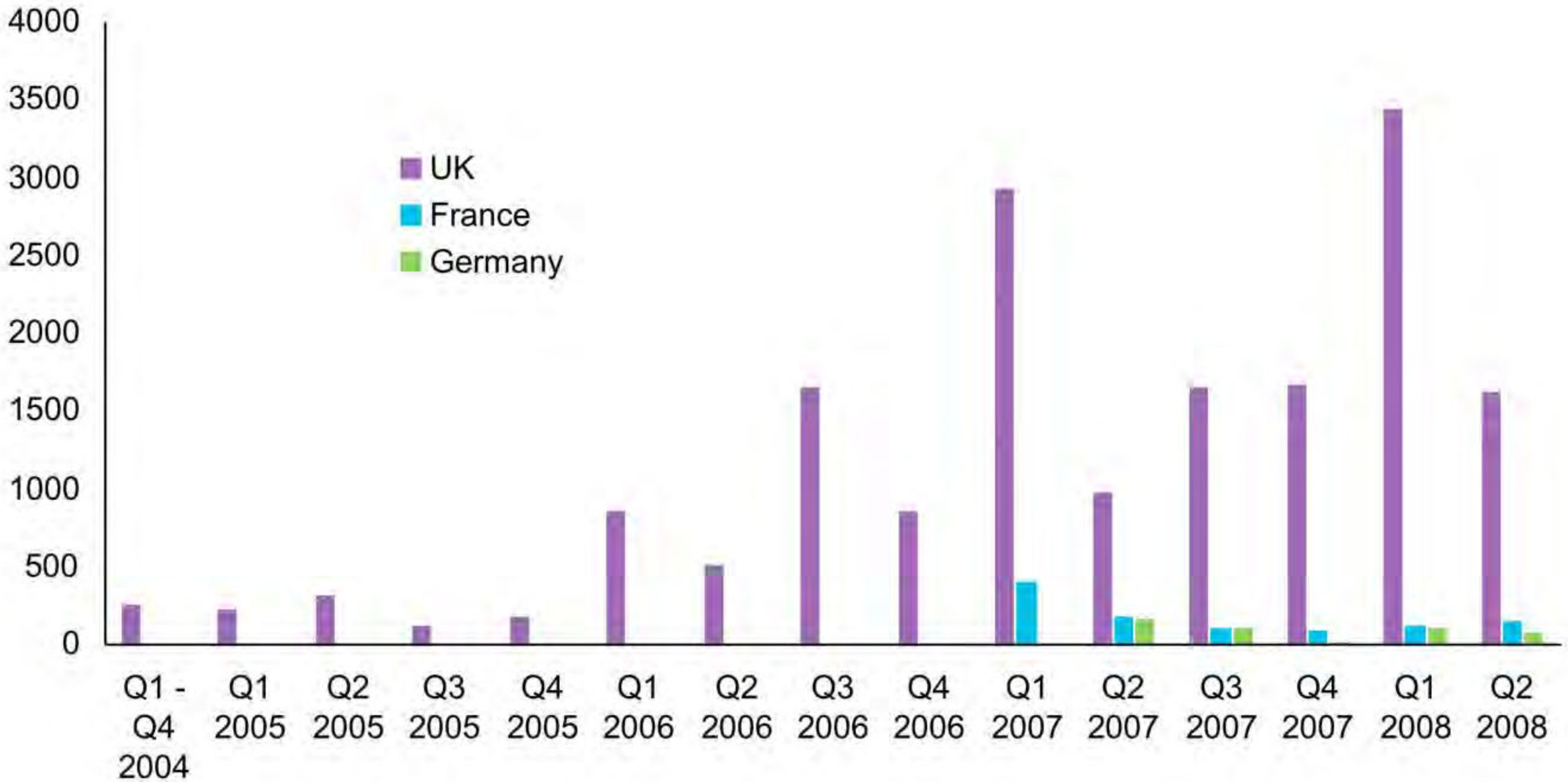

UK Interbank vs End User

Outstanding Notional £m

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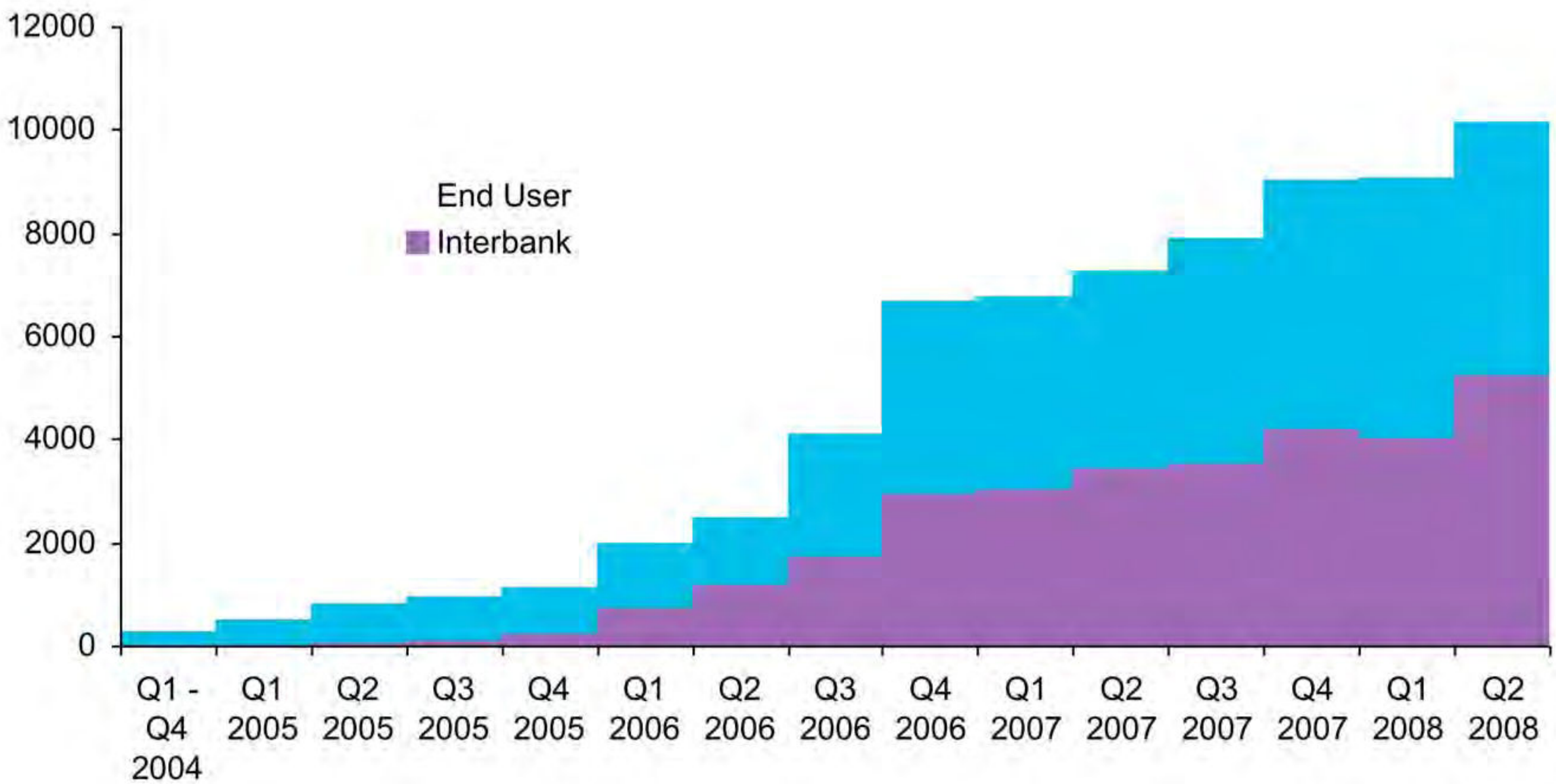
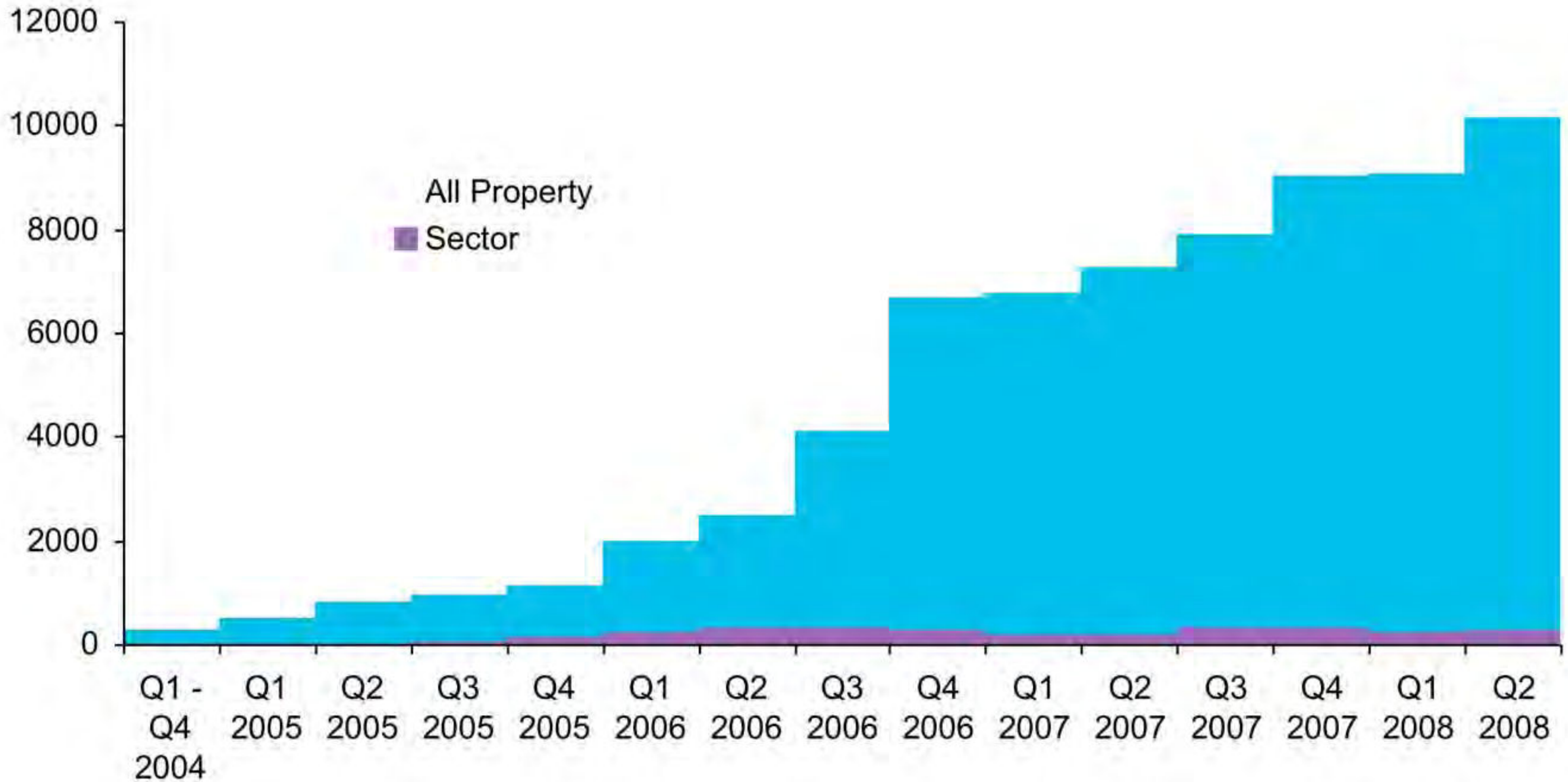


UK Sector vs All Property
Outstanding Notional £m



Survey respondents

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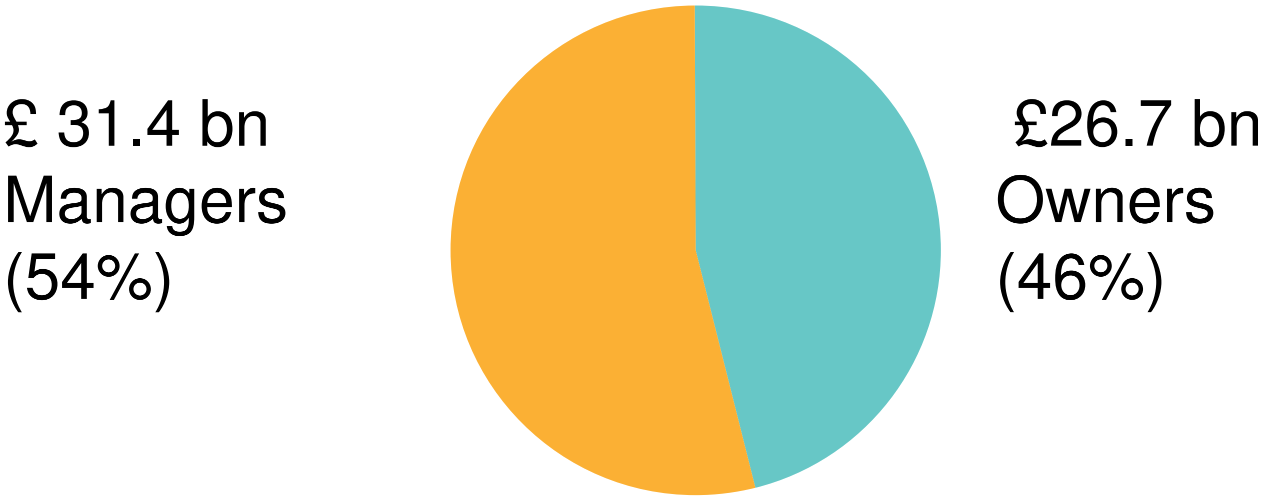

- Sent to 100 IPD contributors
- Replies representing £58 bn of capital
- 48% of the IPD UK Universe

Readiness Survey – Main Points

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- Investors feel they know about derivatives and are highly supportive of the market
- Keen to go beyond ‘all property’ contracts
- 3 out of 4 have a mandate to trade and the vast majority of the rest are willing to recommend their use
- Main concern – liquidity

Main Uses of Property Derivatives

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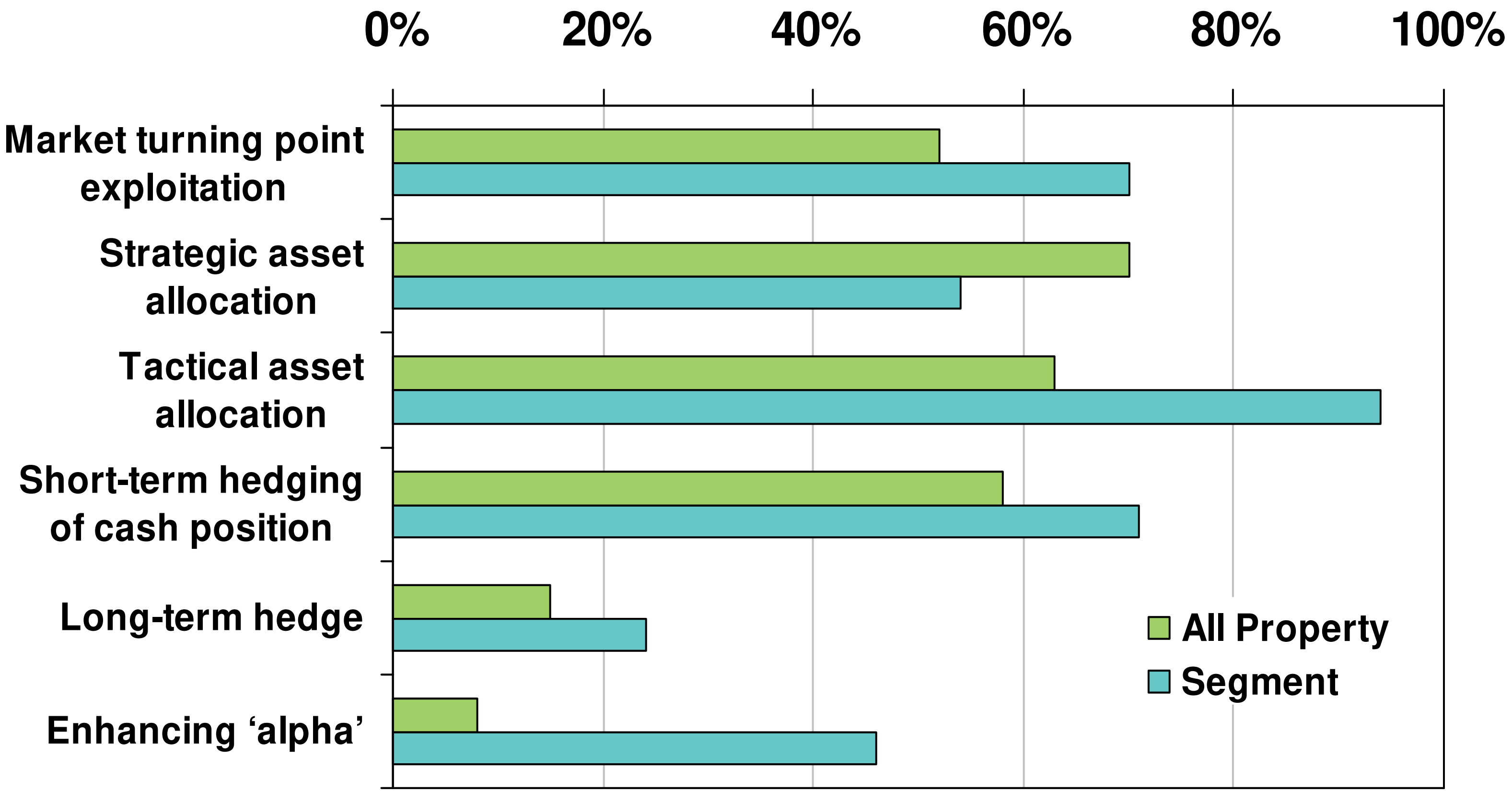

Remaining Barriers to using derivatives

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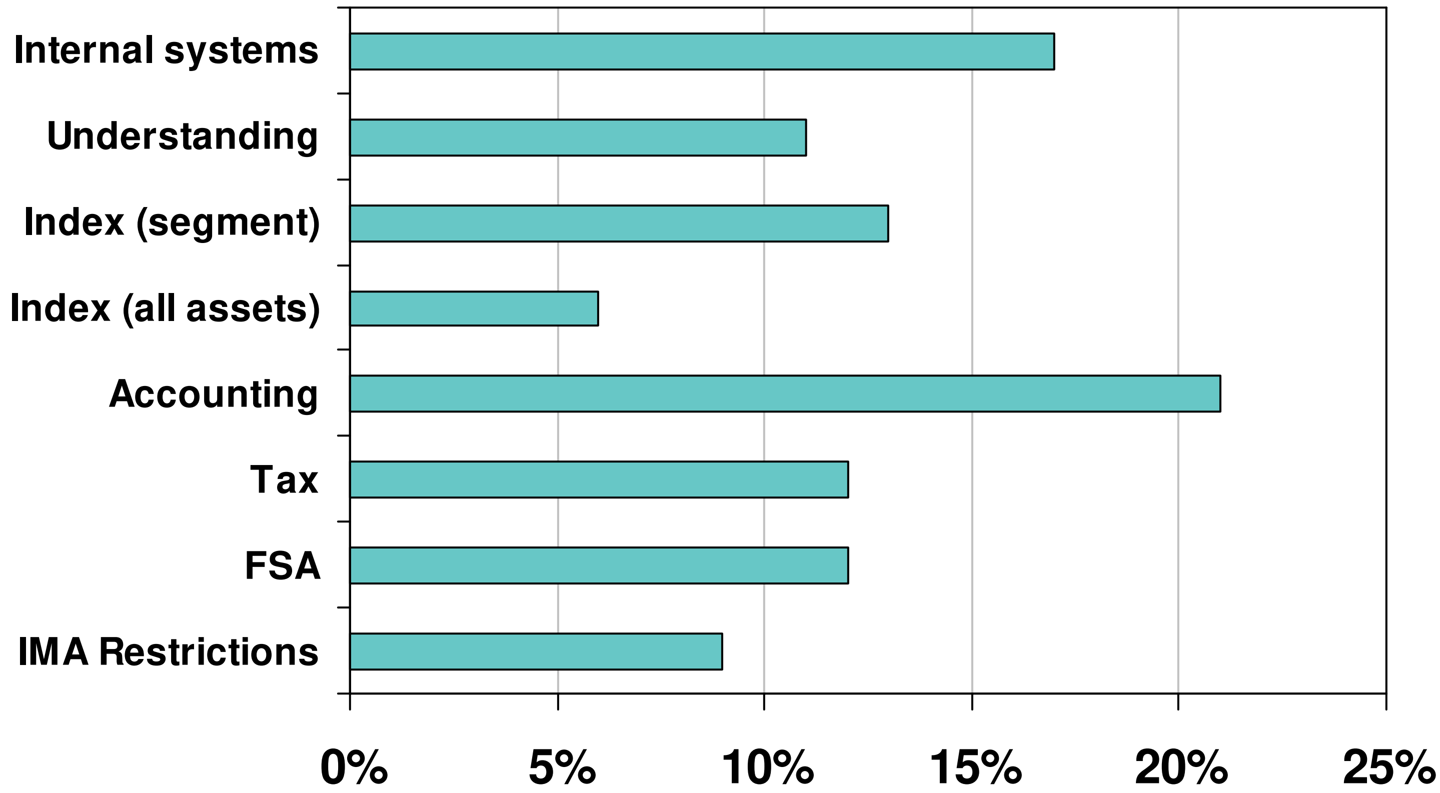

The Australian Experience

2006 Exuberance

2007 Practicalities

2008 Ready, Get Set,

CRASH

2009 ?

Other Observations

"Catch 22"

Tertiary Education

Trust Confidence

A question for discussion

In the current Economic Climate does anyone think that there is a role for Property Derivatives this year in their portfolio or investment strategies?

Futures Curves.

Exploiting inadequate knowledge

Thank you for your time

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Example of recent CD deal
… Prudential & British Land

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Buyer	Agent	Seller
	Pay IPD All Property Index	
The British Land Company plc	Euro Hypo & Deutsche Bank	Prudential Prop. Investment Managers
	Pay Interest Rate (LIBOR + Premium)	
£20m		£20m

- Maturity of 3 years with annual settlement
- The agent charges a small fee on the notional value of the contract

The UK experience
… A potted history

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- Early 1980s – era of PINCs, SPOTs & SAPCOs
- Since the 1990s – four attempts to establish an index based derivatives market based on IPD indices
    - London FOX 1991 x
    - Property Index Forwards (PIFs) 1994 +
    - Real Estate Index Markets (REIMs) 1998 +
    - Property Index Certificates (PICs) 1999 +
- Other attempts
    - Abbey National plc residential derivative based on Halifax residential price index