GLOBAL MARKETS

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Although the global economy remains relatively healthy, 2005 saw a deceleration in world growth as a result of higher energy prices and a series of natural disasters. The outlook remains favourable for 2006, with GDP growth remaining above 4.0%. However, the continued rise of energy prices, or a faster rise in interest rates, could potentially soften global demand, further fuelling inflationary fears.

Global real estate investment has been on the rise and this trend is expected to prevail throughout 2006. Globally, there is a large pool of capital in the hands of investors looking for less risk and higher returns. The current historically low interest rate environment, coupled with an emerging middle class in countries such as China and India, an aging population, increased pension savings, and increasing property fundamentals in many markets is accelerating real estate investment. Cap rates, in general, have been declining around the globe with asset prices hitting record highs in many markets.

North American institutional investors are gradually looking to other areas of the globe to invest their capital, including Mexico, Brazil, Russia, Central and Eastern Europe, as well as the emerging markets of China and India. Why are they moving abroad? Investors are looking to further diversify as a way of mitigating risk and finding opportunity. The weak US dollar has resulted in an increasing attractiveness of the US real estate market to offshore investors, notably European and Australian, increasing the competition for available product in the marketplace.

Investors are also diversifying into infrastructure investment as a means of acquiring unique assets with favourable risk return. This includes airport and air cargo facilities; roads, highways, toll roads and bridges; railway and port facilities; water and sewer; power transmission; energy equipment and real estate. Australian investment bank, Macquarie Bank, has been investing in infrastructure in both the US and Canada, including Highway 407 in Toronto.

REITs are also widening the global real estate market by offering a more highly liquid way of investing in real estate than direct property investment. The number of REITs continues to grow with this type of investment vehicle now operating in over 20 countries around the world. Other countries, including those in Asia, are now seriously considering putting in place legislation for the creation of REIT vehicles where they do not already exist.

Real estate is becoming very important to China, with housing the fastest growing real estate sector, driven by demographic and economic trends. As the population continues to accrue more personal wealth, the emergence of a middle class and the growth of cities are fuelling the need for capital investment in housing, infrastructure, retail, office, and industrial facilities. In addition, China's entry into the WTO, the 2008 Olympics in Beijing, and the 2010 World Expo in Shanghai should continue to fuel growth in China's real estate sector.

China is slowly opening up to foreign investment as the transparency in its property market improves. High profile investors have recently made their way to the Chinese market, including Morgan Stanley and Goldman Sachs. Prologis, the world's largest provider of distribution facilities has been very active, establishing eight logistics parks in the last two years.

Similar to China, the growth of the domestic economy in India has created more job opportunities. This in turn has led to increased urbanization of the population, increased personal wealth, and the emergence of a growing middle class. Outsourcing activity from the West, particularly major corporations in the United States, has created a booming job market in a number of major cities in India resulting in increased demand for facilities and housing. Recognizing the need for foreign investment, India is gradually changing its foreign investment regulations to encourage more direct investment, including real estate and much needed infrastructure improvements.

In Europe, much of the investment activity is coming from a growing sale/leaseback environment, where large corporations and governments are looking to restructure their portfolios to free up capital and reduce real estate costs, disposing of non-core assets and/or consolidating to use their real estate more efficiently. This activity is providing a significant amount of investment opportunity.

Although interest rates are forecast to rise in many countries around the globe the question remains – how fast, how high, and for how long? After holding at 2.0% for two years, the European Central Bank moved on interest rates in December 2005 raising them by a quarter of a percentage point for the first time in five years. The US Federal Reserve began raising interest rates in June 2004 and is expected to be near the end of its tightening cycle in early 2006, with interest rates leveling off at 4.5%. The Bank of Canada is expected to continue tightening its monetary policy through 2006 with overnight rates expected to reach 4.0% in the fall.

While real estate continues to see efficient cash flow delivery at rates of return greater than other investment opportunities, expect to see continued cross border capital flows into real estate. The levels of activity experienced during 2006 will be significantly influenced by the magnitude of interest rate hikes.