Research Report

Asia Pacific Real Estate Strategic Outlook

February 2017

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1 Executive Summary

Macroeconomic conditions in Asia Pacific moderated in 2016, as headwinds remain in light of tapering growth in China and fragile trade activities in the region. Volatility intensified in global capital markets after the U.K.’s referendum and the U.S. presidential election in 2016. The direction of trade policies under new U.S. President Trump will particularly be a key concern for the APAC region given anxieties over potential shifts towards protectionism policies. Job growth in the region continues to hover above the historical ten year average particularly in Japan and Australia, and to some extent in China. Meanwhile, the slower growth and low inflation environment have given central banks more leeway to maintain looser monetary policies as evident in Japan, Korea and Australia. Barring any shocks or unexpected shifts in the baseline, the regional economy is expected to remain broadly stable at 5.3% in 2017\(^1\).

Real estate performance across much of the Asia Pacific region continues to strengthen on the back of strong capital markets and healthy occupier fundamentals. Across the region, key cities in Japan, China, Hong Kong and Australia continued to see healthy office leasing demand in 2016 while the weight of capital targeting quality assets have contributed to further cap rate compression in core markets. The outlook of property returns which have been heavily front loaded in our previous forecast could flatten over our forecast horizon through 2021 and returns in coming years are likely to be driven mostly by income yields as the impact of yield compression recedes. Near term returns are capped in Tokyo given the strong competition with REITs for quality assets while in Seoul, subdued tenant demand coupled with shadow space in developers or owner occupied buildings are expected to weigh on rental growth prospects. Nevertheless, in our view, Asia Pacific commercial real estate markets are expected to deliver healthy core unlevered total returns ranging between 5.8% - 8.1% per annum over the next five years with industrial returns outperforming office and retail returns\(^2\).

<table>
<thead>
<tr>
<th>Asia Pacific Real Estate target markets:</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Theme</strong></td>
</tr>
<tr>
<td>Main Target Market with High Asset Liquidity</td>
</tr>
<tr>
<td>Focus on Cash Flows</td>
</tr>
<tr>
<td>Recovery Market</td>
</tr>
<tr>
<td>Mid-Term Opportunities</td>
</tr>
<tr>
<td></td>
</tr>
<tr>
<td></td>
</tr>
</tbody>
</table>

| **Theme** | **Sector** | **Countries/Cities** | **Main Rationale** |
| Active Asset Management | Office | Japan, Korea, Australia, Shanghai, Beijing | Utilize asset management specialty and local knowledge to enhance asset performance and improve cash flows. |
| Attractive Excess Return | High street retail/Shopping centres | Japan, Korea, Australia, Shanghai, Beijing | Improvement of foot traffic and a fresher tenant mix for underperforming high street retail and shopping centres. |
| | Office/High street retail/Neighbourhood centres/Logistics | Regional cities in Japan | Ten year government bond yields remain near zero levels with borrowing costs among the cheapest in the region. |
| | Logistics/Hotel | Japan, Korea | Structural undersupply of good quality hotels. |

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\(^1\) IMF Regional Economic Outlook, Asia Pacific, as at Oct 2016.

\(^2\) No assurance can be made that projected returns will be achieved.

\(^3\) See chapter 3 for further discussion on Core Strategy and Core Plus and Value Added Strategy.
2 The Economy

Macroeconomic conditions in Asia Pacific moderated in 2016. China’s growth continued to moderate gradually and remain underpinned by infrastructure investment and domestic consumption. Australia saw a recovery in the non-mining sectors especially in the main Eastern states, while Western Australia continued to struggle on the back of the commodity price slump. Domestic consumption remained slow in Japan and South Korea.

The region’s growth momentum is generally subdued but partially supported by accommodative monetary policies in major economies. Uncertainties are intensifying on the other hand amidst ongoing volatility in global capital markets after the U.K.’s referendum to leave the European Union and also the U.S. presidential election in 2016. The direction of trade policies under new U.S. President Trump will particularly be a key concern for the APAC region given anxieties over potential shifts towards protectionism policies. Barring any shocks or unexpected shifts in the baseline, the regional economy is expected to remain broadly stable at 5.3% in 2017 as per latest IMF projections.

Exhibit 1: Real GDP growth & unemployment rates

![Graph showing Real GDP growth & Unemployment rates in various countries (Australia, China, Hong Kong, Japan, Malaysia, Singapore, South Korea)]

Note: f = forecast. There is no guarantee the forecasts will materialise
Source: Bloomberg, Oxford Economics, Deutsche Asset Management, as at Jan 2017. Past performance is not a reliable indicator of future performance

External demand:
In the developed west, the U.S. economy remains on a recovery track supported by consumer spending and healthy labor market. Financial markets remain buoyant as the Dow Jones Industrial Average and S&P 500 index soared to all-time highs in the weeks following the conclusion of the U.S. presidential election as investors price in likelihood of increased budget expenditures in U.S. economic policies, notwithstanding lingering uncertainties regarding the pace of interest rate hikes. Europe’s economy appeared set on a firmer footing although concerns remain following the U.K.’s referendum to leave the European Union in June 2016 and increased geopolitical tensions.

While a recovering U.S. economy generally bodes well for the rest of the world, the direction of trade policies under new president has become unclear and any increase in protectionism could reduce import demand for the products manufactured in China or other Asian nations. China is the largest trading partner for many countries in the Asia Pacific region, while its trade volumes have been declining over the past two years to 2016 amidst ongoing structural reforms. The intricate linkage in the Asian economies to China is most acutely demonstrated in South Korea where exports have been declining continuously since the start of 2015.
Monetary policy:

In support of domestic and export demand, major central banks in Asia have largely adopted loose and accommodative monetary policies in 2016. The Bank of Japan (BoJ) first adopted an unprecedented negative interest rate policy followed by a subsequent modification towards yield curve control policy in the same year to combat persistent deflation concerns. The Bank of Korea (BoK) and the Reserve Bank of Australia (RBA) also lowered policy rates to all-time lows in efforts to stimulate their respective domestic economies. Going forward, Asian policy makers should remain accommodative to support growth though any further easing measures are unlikely to be aggressive given the increasing domestic debt levels and prospects of higher interest rates in the United States.

Inflation:

In light of the lower energy prices, overall inflation is expected to remain muted across Asia Pacific, especially in the larger economies including China, Japan, South Korea and Australia. 10-year government bond yields in these developed core countries are expected to rise gradually in 2017-2018, albeit at varying degrees. Bond yields are expected to rise very marginally in Japan, and between 1.0 – 2.2 percentage points across Singapore, Australia, Malaysia, South Korea, China and Hong Kong over the next five years. Deutsche Asset Management (Deutsche AM) anticipates a risk of cap rates increase in some markets, especially in the trade dependant economies of Hong Kong and Singapore. (Our view is in line with the interest rate level anticipated in the forward market.)

Note: f = forecast. *Based on the Singapore domestic interbank overnight rate as Singapore does not have a central bank policy rate. There is no guarantee the forecast returns shown will materialize.


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6 Bloomberg. Data as at July 7, 2016.
2.1 Economic Outlook

— **Japan**: Based on latest government projections\(^5\), Japan’s GDP is expected to grow 0.9%-1.0% in 2017 and 2018, as economic performance remains uneven with recovery in exports affected by currency volatility while domestic capital and consumer expenditure remains slow. BoJ had announced in September 2016 it would shift its monetary policy focus away from a monetary base expansion target to controlling long-term interest rates, in renewed efforts to meet its ambitious inflation target of 2%. Recovery in consumer sector remains stagnant with sustained inflation unlikely in the near-term.

— **South Korea**: Korea’s export-driven economy is estimated to have slowed down to 2.7% in 2016\(^6\) and a further slowdown is expected in 2017, in contrast to the historical average of 3.4% over the last ten years. The country has suffered from the downturn of its export industry to China, the country’s biggest trade partner, as well as the domestic political turmoil which led to the impeachment of the president in office, and investigations into bribery allegations of large Chaebol (conglomerate) owners.

— **China**: Given the more challenging external picture, China’s export growth is expected to remain tepid. The slowdown in the property market and construction activity will likely put a drag on growth. Household consumption supported by rising incomes should hold up better while fiscal policy will likely remain expansionary, allowing for infrastructure investment to remain a key growth driver. GDP growth is expected to moderate to 6.3% in 2017\(^7\). The USD is also expected to be relatively strong owing to the higher prospects of U.S. interest rate hikes in 2017. This could exert renewed pressure on RMB and concerns about the potential for large-scale capital outflows could mean that capital account restrictions are likely to be tightened in 2017.

— **South East Asia**: Growth in key South East Asian economies is expected to be generally modest in 2017. Sluggish external conditions continue to weigh on export demand though growth remains supported by relatively resilient domestic consumption and investment. Notwithstanding, risks abound from lingering weakness in export demand and potential capital outflows atop currency weakness triggered by prospects of higher U.S. interest rates. Latest projections by IMF\(^7\) forecast GDP growth of 5.1% for the ASEAN region in 2017.

— **Singapore**: Singapore’s economy continues to face challenging market conditions driven by global economic headwinds, weak manufacturing and export demand, and subdued business investment though growth momentum remains in select industries such as the wealth, insurance and healthcare sectors. Economic growth is projected to rebound slightly to c.2% in 2017\(^8\), in line with the government’s forecast of 1-3% growth amidst expectations for a gradual improvement in the external trade environment.

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\(^6\) Oxford Economics. Data as at December 13, 2016.

\(^7\) IMF Regional Economic Outlook, October 2016

\(^8\) Oxford Economics. Data as at December 13, 2016.
— **Australia:** The Australian economy has continued its gradual transition away from the mining investment led growth to domestic demand drivers. Household consumption remained resilient while the lower Australian dollar has continued to provide support for tourism, services and other trade-dependant sectors. Labour market conditions remained stable, although the pace of growth has moderated. Following the weak inflation environment in the first half of 2016, the RBA has trimmed the cash rate twice in 2016 by a total of 50 basis points to an all time low of 1.5% in August 2016⁵. This is consistent with the decline in cost of business inputs such as fuel and lower growth in labour costs, in-line with the movement of workers from highly paid mining-related jobs to other employment. In its meeting in November 2016, RBA has signaled that interest rates are likely to remain on hold in the near term.

### 2.2 Risks to the Forecast

— **Slowdown in China:** Risks to the Asia Pacific region center around the outlook for China’s growth and the implications for commodity demand. Moreover, rising corporate leverage levels if unchecked, could lead to further economic vulnerability. Growth in resource-led economies such as Australia remain undermined by the weakening of Chinese import demand while exports of Korea have been declining since the start of 2015. Being the largest trading partner for many other APAC nations including Japan and Singapore, a sharper-than-expected slowdown in China’s economy would see trade flow and economic growth decline in the region.

— **Impact of the U.S election on trade and capital markets:** Growing concerns over protectionism policies could lead to higher tariffs and nullification of international trade agreements such as the TPP, in turn adversely impacting export and trade volumes and limiting economic growth around the region. The growing possibility of successive rate hikes in the United States affects the currency exchange rates and could trigger capital flight from emerging markets.

— **Interest rate volatility and cap rate widening:** Prospects of successive rate hikes by the U.S. Fed could affect key REIT markets such as Australia, Hong Kong, Singapore and Japan, which are structurally sensitive to the long term interest rate volatility. These REIT markets could impact the broader direct real estate markets in terms of transaction volume, yields, capital value and more importantly the market sentiment. We have reflected this in our cap rate assumptions in the base case scenarios for each market although risks remain that cap rates might widen more significantly than anticipated.

— **Impact of the U.K. referendum on E.U. membership ("Brexit"):** In light of the U.K.’s referendum result to leave the European Union, we expect further capital market volatility and a possible reweighting of capital away from Europe to top gateway cities in Asia Pacific. Prolonged uncertainty could derail global economic growth and weigh on occupier demand. From the currency perspective the South Korean and Australian markets could be affected by increased hedging costs while the Japan market can be expensive in dollar terms in the event of renewed yen strength.

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⁵ Reserve Bank Of Australia, Press Release dated 2 August 2016
3 Strategic Real Estate Outlook

Real estate performance across much of the Asia Pacific region has been resilient notwithstanding early indications of slowdown on the back of already compressed cap rates in key core markets. Japan, China and Australia’s top cities have continued to experience healthy office leasing demand in 2016, and the recovery is expected to continue in coming quarters for these key markets while real estate fundamentals are likely to remain subdued in other markets including Singapore, Perth, Seoul and Hong Kong due to either a surge in new supply or subdued tenant demand in 2017.

The weight of capital targeting quality assets in the region has contributed to further cap rate compression, especially in key Japanese and Australian cities. The trend was compounded by active investments by sovereign capital, pension funds and insurance firms which have increased their real estate allocation. As such, much of the capital growth was front loaded and realized in the earlier years till 2016, leading to diminished prospects of capital growth over coming years in the forecast horizon. Therefore, returns in coming years are likely to be driven mostly by income yields.

Core unlevered total returns are expected to range between 5.8% - 8.1% annually over the next five years with the industrial sector performing better than office and retail, while near term returns are capped in Tokyo and Seoul given the strong competition for good quality assets and subdued tenant demand, respectively. Nevertheless, potential widening of cap rates in the medium term could create good entry opportunities for investors seeking increased exposure within the region.

3.1 Strategic Investment Themes

Since summer 2016, we have witnessed further tightening of cap rates in Japan, Australia and South Korea in line with interest rate cuts, while cap rates remained tight in Singapore and Hong Kong. It has become increasingly challenging for investors seeking income producing core-type opportunities in these markets to achieve their target returns, with some opting to move up the risk curve and/or diversify their target sectors.

We hold the view that while part of the cap rate compression was driven by anticipation of a recovering rental cycle, other structural factors were also at play: (1) geographical diversification needs as evident from the gradual increase in cross-border transactions and (2) continuous amount of capital available to invest as data from Preqin11 which showed that Asia-focused real estate funds have raised an aggregate capital of over US$10.6 billion in 2016, topping the US$7.5 billion raised in 2015.

Note: f = forecast. There is no guarantee the forecasts will materialise. Total return is calculated based on the weighted average of investable stock in each market according to Cushman & Wakefield Money into Property 2016. As such, the performance and forecast shown represent hypothetical and simulated performance, which has many inherent limitations. Please see “Important Information” for additional disclosure regarding the use of simulated, hypothetical performance. No assurance is made that forecasted returns will be achieved.

Source: Cushman & Wakefield Money into Property May 2016, Deutsche Asset Management, as at Jan 2017
We favour markets with relatively good yield spreads to mitigate risks arising from widening of cap rates, and healthy leasing fundamentals to provide rental income growth to drive returns going forward. In addition, we believe there are alternatives for cross border diversification trends, and as such we prefer gateway cities with deep markets and greater appeal to foreign investors.

**Core Strategy**

— **Main Target Market with High Asset Liquidity:** Good income producing assets providing meaningful returns in key gateway cities, i.e. Osaka, Sydney and Melbourne, have continued to attract global capital. Although returns appear more modest compared to last year, this strategy offers investors the potential for income stability and higher liquidity given the depth of the market and stable corporate occupier demand. High street retail in major shopping destinations with access to high footfall as well as neighbourhood retail centres with large catchments in Osaka, Sydney and Melbourne also remains attractive. Supply is tight across major high street locations while neighbourhood centres provides a cushion against fluctuations in discretionary spending.

— **Focus on Cash Flows:** For investors looking for higher income returns, attractive opportunities exist in the logistics sector given the steady income stream nature and higher yields of logistics properties – typically in excess of 6% (4.5% for greater Tokyo). We recommend focusing on prime logistics centre in key transportation hubs including Japan, Korea, Singapore and Australia.¹²

— **Recovery Market:** For investors with slightly lower risk profiles and preferences for stabilized assets, markets in mid to late-recovery offer an attractive combination of higher entry yields and potential for market-driven returns. We see opportunities in the Brisbane office market where rental growth is in a mid to late recovery cycle and could accelerate with rising demand set against a backdrop of low development pipeline and shortage of Grade A space.

— **Mid-term Opportunities:** Monitor progress and look out for optimal entry timing in core investable markets with near-term returns capped by intense competition for assets with domestic REITs i.e Central Tokyo or facing short-term vacancy issues i.e Seoul and Singapore. Despite current weak rental prospects at the latter markets, demand supply dynamics are expected to improve gradually in favour of landlords on the back of recovering occupier demand leading to cyclical rental uplifts in later years.

**Core Plus and Value Added Strategy**

— **Active Asset Management:** We see opportunities in key cities in mature North Asian and Australia markets by taking on leasing risks for vacant office properties or refurbishment/re-positioning of older but well-located properties. High street and shopping centres are also strong candidates for a value-add proposition including improvements in retail footfall and repositioning of tenant mix. In China, opportunities could arise from repositioning underperforming office assets and improving tenant mix for retail assets in prime locations such as Beijing and Shanghai. Strong local network and deep market knowledge are crucial for successful value enhancement.

— **Attractive Excess Return Markets:** The ten-year Japanese government bond is yielding at around 0% and borrowing costs are extremely cheap. Japanese regional cities are expected to provide one of the best excess returns over the risk free rate, indicating good investment returns when local finance is secured.

— **Forward Commitments:** In some markets, entering into joint ventures with strong local operating partners for forward commitments provides a viable route to access good real estate assets. We see selective opportunities in the hotel and logistics sectors both in Japan and South Korea, given the structural undersupply in these sectors. Construction risk and lease-up risk should be mitigated.

¹² Deutsche Asset Management. This information is subject to change at any time, based upon economic, market and other considerations and should not be construed as a recommendation. Past performance is not indicative of future returns. Forecasts are based on assumptions, estimates, opinions and hypothetical models that may prove to be incorrect.
3.2 Capital Markets

Transactions:
Commercial real estate transaction volumes (excl. land transactions) in Asia Pacific hit peak levels exceeding US$150 billion both 2014 and 2015. However, volumes started to taper off in 2016 due to tight markets and rich valuations, declining by a preliminary 18% in the first three quarters of 2016. Japan continued to host the largest transaction volume with c.27% market share, followed by China (21%) and Australia (18%) in the period, while domestic investors accounted for over 80% of transactions in Japan and China. Office transactions accounted for 54% of total transaction volumes in the first three quarters in 2016, an increase from 48% in 2015, while the retail sector accounted for 20%, down from 28% in 2015.

REITs:
The aggregate amount of equity fundraising by REITs in the region was muted in Singapore and Australia in 2016, while the negative interest rate policy in Japan helped stable capital inflow. Being structurally sensitive to volatilities in long term interest rates, REIT stock indices in major markets in the region were supported by a low interest rate environment in the first half of 2016, followed by subdued price movements driven by the increases in long term interest rates in the United States and other countries.
Investor Profile:
Data from Real Capital Analytics indicates continued active participation from cross-border investors whose share of transactions in Asia Pacific rose from 29% in 2015 to 32% in the first nine months of 2016. A couple of multi-billion dollar transactions by cross border investors were observed in the region, including Seoul, Singapore and Shanghai while overseas investors accounted for over half of total transactions in Sydney, Melbourne and Singapore in the period. Listed corporations and REITs form the next largest buyer group in the region, accounting for 23% of transaction volumes, lower than the 28% share in 2015.

Note: f = forecast. There is no guarantee the forecast returns shown will materialize.
Source: Real Capital Analytics, Deutsche Asset Management, as at Jan 2017.

Office:
The trend of global and domestic capital chasing income producing office assets has contributed to cap rate compressions in 2016 in the majority of countries across the region including Japan, South Korea, Singapore and Australia, while cap rates remain broadly flat in other markets such as China and Hong Kong, in line with interest rate movements. The tight conditions were supported by active investments by sovereign capital, pension funds, insurance firms and cross border investors chasing large deals while domestic REITs became the most dominant investor group in Japan. Cap rates are expected to remain at current tight levels in most markets in 2017 before unwinding modestly in 2018, with the anticipated impact of widening cap rates on capital values likely to be strong in Hong Kong followed by Singapore over the next few years.

Note: f = forecast. There is no guarantee the forecast returns shown will materialise.
Retail:
Sizable institutional grade assets in the retail sector remain tightly held by local developers and REITs in markets like Hong Kong, Singapore and Australia, capping deal volumes. High street retail sales have benefited from increasing tourist arrivals in Japan, South Korea and Australia, while private wealth capital is more dominant in transactions in prime high street areas in Hong Kong, Shanghai, Tokyo Ginza and Seoul Gangnam where cap rates are extremely tight. Institutional investors have been observed to be exploring suburban assets in Japan, Australia and to a lesser degree in Korea, where investors and REITs have tried to reshuffle existing portfolios.

Investor interest in the industrial and logistics sector remains strong due to the relatively higher yields and the recent evolution and gradual maturity of the sector, though acquisition opportunities of institutional grade assets remains limited. The supply of modern facilities is catching up to increasing demand with multiple large assets currently in the development pipeline in major metros in Japan, South Korea and China in 2017 and ahead. Further yield compression (albeit marginal) could occur in Japan, while yields have stabilized in other markets.

Exhibit 10: Retail sector: Initial yields and 10Y government bond yield

Exhibit 11: Industrial sector: Initial yields and 10Y government bond yield
Credit markets:
The financing environment still remains accommodative due to the favorable monetary policy and supportive measures. Base rates have started to increase in some markets in the region, by around 10 basis points in Japan or 20-40 basis points in Hong Kong, Singapore and South Korea while spreads remained at similar levels to a year ago. With the exception of Hong Kong, cap rate spreads over financing costs remain positive across core markets with the highest positive carry of circa 200-300 basis points in Australian and Japan markets.

Nonetheless, there are signs that lenders are becoming sensitive to high valuations especially for assets with weaker leasing covenants or in inferior locations. This could lead to moderate cap rate widening in 2017 or 2018 onwards.

Exhibit 12: Typical commercial lending terms

<table>
<thead>
<tr>
<th>Market</th>
<th>LTV (%)</th>
<th>Base Reference rate</th>
<th>Spread (bps)</th>
<th>Financing Cost (bps)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Australia</td>
<td>50%</td>
<td>3M BBSW Rate: 1.80%</td>
<td>150 - 225</td>
<td>330 - 405</td>
</tr>
<tr>
<td>China</td>
<td>50-60%</td>
<td>1-5 year base lending: 4.75%</td>
<td>300 - 500</td>
<td>775 - 975</td>
</tr>
<tr>
<td>Hong Kong</td>
<td>50%</td>
<td>1 year HIBOR: 1.55%</td>
<td>200 - 300</td>
<td>355 - 455</td>
</tr>
<tr>
<td>Japan</td>
<td>50%</td>
<td>5Y JPY Swap rate + TL spread: 0.2%</td>
<td>40 - 60</td>
<td>60 - 80</td>
</tr>
<tr>
<td>Singapore</td>
<td>60%</td>
<td>3M Swap Offer Rate: 0.95%</td>
<td>120 - 180</td>
<td>215 - 275</td>
</tr>
<tr>
<td>South Korea</td>
<td>50-60%</td>
<td>5Y KTB: 1.8%</td>
<td>160 - 200</td>
<td>340 - 380</td>
</tr>
</tbody>
</table>

Source: Bloomberg, Deutsche Asset Management, as at Jan 2017
For illustrative purposes only
4 Property Sectors and Returns

4.1 Office

Current Conditions: Office markets in core cities across Asia Pacific generally performed relatively well in 2016, underpinned by steady occupier demand trends. Sydney led the region in effective rental growth, driven by a broad base recovery in tenant demand led by business services, followed by Tokyo where vacancy rates remain very tight and Hong Kong where demand was underpinned by financial services firms from mainland China. On the other hand, some markets such as Singapore, Brisbane and Perth remain in cyclical downturn weighed down by subdued demand and significant short-term supply pressures.

Looking back a decade since the global financial crisis, office rents across the region have mostly recovered to levels above or near their pre-crisis peak in 2007/2008, underlining the ongoing recovery effected in the region. Falling interest rates contributed to the ongoing yield compression and growth in asset values which led to the significant outperformance of capital value growth to date compared to rental growth in the past decade.

Outlook: For the five year forecast period till 2021, vacancy rates across key office markets in the region are generally expected to improve or remain stable at the current healthy levels. The recovery in occupancy rates will likely be the strongest in Australia, especially in the regional cities of Brisbane, Perth and Adelaide where vacancy rates should improve gradually from current elevated levels in excess of 15%. Markets currently undergoing a supply surge this year such as Singapore are expected to see a cyclical recovery in the medium term. Exceptions are Kuala Lumpur, Beijing and Hong Kong where large development pipelines are underway.

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Correspondingly, a divergence in rental growth trend is expected in 2017 with continued rental growth momentum in the core cities of Australia, China and Tokyo (albeit at varying degrees), while significant rental declines are expected in Singapore, Hong Kong, and other cities such as Perth and Guangzhou due to short-term supply pressures. Flattish rental growth is expected in Seoul, Yokohama and Osaka against the backdrop of a patchy outlook in the corporate sector.

Looking ahead in the longer term, we expect to see modest rental growth given the still healthy fundamentals in the region, led by Sydney and Melbourne through recovery in tenant incentives, followed by Shanghai and Tokyo. In Singapore, having seen significant correction in 2015 and 2016, rental growth should turn positive in a year or so followed by strong recovery in the outer years of the forecast period. Cyclical rental declines expected in Guangzhou, Adelaide and Hong Kong during 2017 should see gradual rental recovery in later years. Lower but steady growths are expected in other cities including Seoul and Brisbane where current elevated vacancy rates should recover gradually, and Japanese regional cities where occupier demand is more moderate compared to Tokyo.
Historically, an inverse relationship has been observed between the expected vacancy rate and rental growth forecast in most cities. A healthy demand supply balance is expected to persist in most key markets though weak leasing conditions are expected in Kuala Lumpur and Perth. Forecast average five-year rental growth is also projected to be negative in Hong Kong (overall) where a cyclical downturn is expected in 2017-18.

Performance: Mid to high single digit returns are expected in most cities in the APAC office sector over the next five years through 2021, on the back of healthy demand and moderate supply. Chinese Tier-1 and Australian cities are projected to be among the top performers, followed by Seoul and regional second tier cities in Australia, China and Japan. Japanese regional cities are expected to provide good excess returns over the local risk free rate, indicating good investment returns when local finance is secured, while total return will be lowest in Tokyo due to the highly tight entering cap rates. Forecast five-year performance in highly volatile markets such as Hong Kong and Singapore are projected to come in relatively weaker though good entry points should arise particularly for Singapore following the beginning of anticipated market recoveries occurring sometime around 2018.
4.2 Retail

Current conditions: The rise in e-commerce has redefined the retail landscape in Asia Pacific. Multi channel or ‘Omni-channel’ retailing as well as the emergence of mobile-based transactions have seen retailers changing their retail operating models and increasing the selection of goods and services available online often at lower prices than in-store. As a result, this could undermine profit margins for physical retail stores and consequently turnover rent leases at retail centres. Notwithstanding, anecdotal evidence have also showed that some pure play e-commerce companies are merging their online and high street presence and have setup physical store space for brand building as well as showrooms.

Diverging trends have developed in the retail environment across the region. Retail sales continue to underperform in some major markets in the region including Hong Kong, Singapore and Malaysia due to soft domestic consumption and subdued inbound tourist arrivals. Rents have declined in Singapore and Kuala Lumpur, while no rental growth is expected in Hong Kong until 2018. The environment appears tough particularly for prime retail in Singapore and Hong Kong where retailers face margin pressures resulting from the combined effects of weaker tourist spend and elevated rental and labour costs.

On the other hand, key cities in China, Australia, South Korea and Japan continue to see healthy, moderate rental growth underpinned by stable domestic consumption trends and strong tourist arrivals, despite competition from the ongoing proliferation of online retail. Nonetheless, given the structural shifts in consumer shopping behavior, and the need for retailers to divert resources from traditional bricks-and-mortar sales towards building up Omni-channel marketing strategies, the retail environment continues to be in favour of tenants with landlords offering better incentives. Vacancy rates could start to inch upwards in decentralized areas on the back of growing supply while occupier demand from retailers are likely to remain stable in the majority of locations in 2017.

Outlook: Over the five-year forecast horizon, Shanghai and Australian top cities are expected to experience the strongest growth in retail rents in the region, although growth should be more moderate in suburban, decentralized areas even in these cities. In Seoul and Tokyo, retail rental growth is likely to be more modest below 2% p.a., due to slower domestic consumption and subdued inflation expectations. Rental growth is projected to be minimal in Singapore and Kuala Lumpur with rents affected by diminished tourist arrivals especially in the near future.

Note: f = forecast RC= Regional Centres SRC= Sub-regional centres. * Projected returns are based on compounded basis. There is no guarantee the forecasts will materialise.

Source: Deutsche Asset Management, as at Jan 2017.
Performance: Given the emergence of online retailing, there is a preference among investors toward long term leases in the retail sector. The impact from online retail is expected to be felt more keenly in the discretionary retail segments such as apparel and electronics, compared to the non-discretionary segments such as staple food and daily necessities.

Looking ahead, the performance of neighbourhood centres in Australia appears more attractive due to higher yields than larger-sized formats, such as regional centres (RC). Healthy excess returns (i.e. annual total returns minus bond yields) of about c.3%-5% are expected in most key retail markets in the region except for Singapore and Guangzhou where excess returns are expected to come in at 2% or below.

<table>
<thead>
<tr>
<th>Excess Return</th>
<th>Projected compounded annual return and excess return between 2017f – 2021f</th>
</tr>
</thead>
<tbody>
<tr>
<td>Sydney - SRC</td>
<td>7.4%</td>
</tr>
<tr>
<td>Sydney - Neighbourhood</td>
<td>3.7%</td>
</tr>
<tr>
<td>Melbourne - SRC</td>
<td>3.6%</td>
</tr>
<tr>
<td>Kuala Lumpur - KLCC</td>
<td>2.5%</td>
</tr>
<tr>
<td>Sydney - RC</td>
<td>3.2%</td>
</tr>
<tr>
<td>Seoul</td>
<td>3.9%</td>
</tr>
<tr>
<td>Melbourne - RC</td>
<td>2.9%</td>
</tr>
<tr>
<td>Shanghai - Prime</td>
<td>2.9%</td>
</tr>
<tr>
<td>Beijing - Core</td>
<td>2.8%</td>
</tr>
<tr>
<td>Hong Kong - Overall</td>
<td>2.9%</td>
</tr>
<tr>
<td>Guangzhou - Prime</td>
<td>1.5%</td>
</tr>
<tr>
<td>Singapore - Suburban</td>
<td>2.3%</td>
</tr>
<tr>
<td>Tokyo</td>
<td>4.7%</td>
</tr>
<tr>
<td>Singapore - Prime</td>
<td>1.8%</td>
</tr>
</tbody>
</table>

Note: f = forecast RC= Regional Centres SRC= Sub-regional centres. There is no guarantee the forecasts will materialize. Excess return is determined by projected income return plus capital appreciation over the local 10 year sovereign bond rate.

Source: Oxford Economics, Deutsche Asset Management, as at Jan 2017

4.3 Industrial

Current Conditions: Despite the slowdown in China, prime logistics space across the region continues to see healthy take-up driven by e-commerce and third party logistics providers, resulting in positive rental growth trends across the region. The availability of prime development land and quality modern warehousing facilities is critical for logistics markets undergoing modernization changes coupled with rising domestic consumption, particularly for locations such as Seoul and tier-one cities in China.

Exhibit 20: Industrial sector: Net rent index (Base Year 4Q2006 = 100)
Outlook: In the industrial sector, e-commerce and third party logistics companies are expected to drive leasing demand in the modern logistic space across the region. Rental growth is expected to be moderate in the region at around 1-3% p.a, broadly in line with each country’s inflation as tenants, third party logistics companies, retailers and consigners remain mindful of logistics costs. Ample logistics supply is expected in cities like Tokyo in 2017, capping rental growth while rents in Singapore are likely to remain in decline this year before staging a recovery on the pretext of improving global trade conditions.

Performance: Owing to higher yields, increased transparency and strong underlying occupier demand, the industrial sector has provided consistently higher returns than the office and retail sectors, and is expected to remain attractive in the next five years (see Exhibit 5 on page 8). Five-year return forecasts for the key cities in Australia, China, Singapore and Seoul look favourable at high levels in excess of 7%, though investors could be constrained by the limited deal flow of high quality completed assets in Chinese cities, Seoul and Singapore. Tokyo is expected to provide good excess returns in the forecast period, while excess returns are forecast to be the lowest in Hong Kong at 3.3% where industrial cap rates are anticipated to rise in the forecast period.
5 Required Returns (office sector)

It is insufficient to compare property-level total returns on a stand-alone basis without factoring the associated risks, especially in the Asia Pacific region with the huge divergence in market maturity. A number of factors were considered in the computation of required returns and associated risks related to each submarket such as volatility, liquidity, transparency and the accumulated effect of obsolescence. The required returns were formulated using both quantitative and qualitative modeling which was integrated in our House View. The following table summarizes the components for the required returns.

Exhibit 23 highlights the positioning of the various markets in reference to this framework. The total forecast returns on the vertical axis are plotted against required returns on the horizontal axis for each office market. The returns are based on the same office sector forecasts as outlined on Exhibit 17. We categorize the major office markets into the following three groups:

— **Core Target Market**: The core target markets include major cities in Japan and Australia as well as Seoul where total return forecasts look favorable compared to their required returns. These are among the most established and mature markets in the region and core investors focused on income yields should center their portfolio investments mainly in these markets. This is broadly in line with the “Main Target Market” in Core Strategy in the Strategic Investment Themes outlined on page 9, while some other regional markets in Australia and Japan are included as well.

— **Late Recovery**: Markets experiencing a cyclical downturn due to supply surge and subdued demand such as Singapore and Perth. A cyclical market recovery is expected in the medium-term. This is similar to the “Medium-term Opportunities” in Strategic Investment Themes outlined on page 9.

— **High Risk High Return**: Top tier markets in China are expected to provide attractive returns in the next five years, though the required returns are partly higher due to the high risk free rate and lower market transparency. These markets should be more suitable for core-plus or value added strategies in line with “Active Asset Management” in Strategic Investment Themes on page 9.

Exhibit 23: Forecast Returns vs Required Returns in APAC Office Market:

Note: F = forecasts. There is no guarantee the forecasts will materialise.
Source: Deutsche Asset Management, as at Jan 2017
Despite favourable performance expectations in some markets there are other challenges and constraints that should be factored for commercial real estate investments which cannot be fully captured in the required return calculations above, especially for cross border investors.

Hedging costs are expensive in Australia and South Korea for Euro investors and this can be an impediment for cross border investors when competing with domestic investors, even though total return forecasts may look attractive. In Japan, local investors and developers hold the upper hand due to extremely cheap borrowing costs in the local debt market, while access to cheap capital is limited for foreign investors.

Regulatory and compliance risks exist for foreign investors. Onshore holding structures in China with equity investments from foreign parties require the formation of foreign-invested enterprises (FIEs) or wholly owned foreign enterprises (WOFEs). Conversion of structures is required if the existing holding structure is not in either of these forms and is subjected to regulatory approval, which introduces regulatory uncertainties.

Therefore, it is critical for investors to find capable investment managers who have a good foothold in each of these markets when making investments.
6 Overview of Key Asia Pacific Markets

Strategic Outlook: Japan

- Real GDP growth estimated at c.1% in 2016, as the unfavorable currency rate unwound following the U.S presidential election in November enhancing the performance of the manufacturing industry.
- While BoJ’s new fiscal policy involving yield curve control turned out to be effective in inducing government bond yields to hover around 0%, cap rates remained extremely tight for core assets while transaction volumes almost halved in a year.
- The leasing market presents a mixed picture as office vacancy rates continued to recover in all major cities, yet rental growth softened in newly developed buildings. The rental growth of Central Tokyo retail remained healthy thanks to robust growth in inbound tourist arrivals, while the vacancy rates of the industrial sector rose amidst the unprecedented large supply in Tokyo and Osaka.
- Despite their strong appetite for further investment, foreign investors find it more difficult to make core investments in the office and retail sectors, due to lower total returns as cap rates tightened as well as the harsh competition with the J-REITs dominating more than 60% of transactions in 2016.

Occupier

- With labor markets staying tight, the office vacancy rate in Central Tokyo compressed to 3.8% in November 2016, 0.4% lower than a year ago. Vacancy rates are expected to remain tight until 2018 when a large supply of new office buildings come onstream.
- Rental markets remained broadly healthy in the retail sectors in Central Tokyo, boosted by the modest growth of inbound tourists.
- The unprecedented large supply in the industrial sector exerted upward pressure on vacancy rates in Tokyo and Osaka, though demand for good quality assets remains robust.

Investment

- Continued strong investment demand saw office appraisal cap rates in Tokyo decline to a preliminary 3.5% in the third quarter of 2016, a fall of c.40 basis points from a year ago.
- On the other hand, preliminary data indicates commercial real estate transaction volumes fell 46% year on year to JPY 2.9 trillion in 2016.
- Transaction volumes declined especially in Central Tokyo due to a lack of assets for sale in the market and fully priced valuations, while other non-core transactions or investments in the decentralized region are not strong enough to fill the gap.

Exhibit 24: Real Estate Transaction Volume in Japan

Exhibit 25: Office Supply and Vacancy Rate in Central Tokyo

Note: There is no guarantee the forecasts will materialise. F = forecasts.
Source: Deutsche Asset Management, Real Capital Analytics, Bank of Japan, Miki Shoji, Mori Trust, Jan 2017
Strategic Outlook: Korea

- Korea’s export-driven economy is estimated to have slowed down by 2.7% in 2016 and a further slowdown is expected in 2017. The country has suffered from the downturn of its exports to China, the country’s biggest trade partner as well as the domestic political turmoil leading to the impeachment of its president in office and investigation into bribery allegations of large Chaebol (conglomerate) owners.

- Weakening demand continued to favour tenants in 2016, and the trend is expected to start easing only after 2018 with no strong signs of demand recovery in the near future.

- Record-high transaction volumes in 2016 proved real estate investment is still being regarded as attractive in terms of yield spreads. Some investors became less active in core assets with concerns around tightening cap rates and bond yield hikes towards the end of 2016.

- We remain positive on the logistics sector underpinned by high income yields, particularly assets with exposure to domestic non-disccretionary consumption.

Occupier

- Weak demand brought by the sluggish economy kept the CBD office vacancy rate at elevated levels of 11.1% in the fourth quarter of 2016, slightly higher than 10.8% a year ago.

- Given additional vacancies coming on by some big tenants’ moving out to owner occupied or fringe buildings and the shadow vacancy originated from master lease guarantees by the construction companies, office vacancy rates in major districts is expected to hardly recover in 2017 and may do only after 2018.

- Declining domestic consumption kept occupancy rates soft in high street retail, while industrial rental growth remains healthy on the back of fast-growing e-commerce and 3PL markets.

Investment

- Preliminary data indicates transaction volumes in 2016 hit a record high of KRW 13 trillion, led by the record high transaction of Brookfield’s IFC acquisition for KRW 2.5 trillion.

- Investors continued to show keen interest owing to relatively higher yield spreads as well as deregulations lowering threshold for smaller investors; however some sizeable deals have been delayed or cancelled as tight office cap rate and bond yields soared since November.

- More investors have been seen switching to higher yielding strategies such as lease ups, forward commitments, asset conversions and investment in decentralized regions.

Exhibit 26: Real Estate Transaction Volume in Korea

Exhibit 27: Office Supply and Vacancy Rate in Korea

Note: There is no guarantee the forecasts will materialise. F = forecasts. Source: Deutsche Asset Management, Real Capital Analytics, Colliers, Jan 2017
Strategic Outlook: China

- China’s growth outlook is expected to remain subdued given the more challenging external picture. The slowdown in exports and the weaker property market will put a drag on growth. Notwithstanding, resilient domestic consumption supported by rising income has helped to offset the weakness in external trade.

- Office leasing activities in Beijing and Shanghai moderated amid the slower economy. Rental growth will face downward pressure as newly completed buildings enter the market especially in Shanghai (Pudong).

- Investment markets continue to be dominated by domestic institutional investors, most notably insurance companies. Good prospects for modern industrial space underpinned by demand from by 3PLs and retailers (e-commerce & traditional).

Occupier

- Overall leasing demand remained muted as foreign MNCs occupiers remained generally cautious. Given the notable amount of new supply in decentralized Shanghai particularly in 2017, the vacancy rate is anticipated to rise.

- Leasing demand in Beijing has also remained weak on the back of the slower economy. Rental growth at existing buildings will be capped as landlords remain cautious during rental negotiations. Rents are expected to soften in Beijing from 2018 onwards given the strong competition from high-quality projects in decentralized markets.

- In the retail sector, rents will likely remain largely stable and landlords have been actively adjusting tenant mix and putting more emphasis on F&B and kids’ brands.

- Leasing activities in the industrial sector continues to be dominated by 3PLs, e-commerce and traditional retailers.

Investment

- Investment activities continued to be dominated by domestic capital, most notably from insurance companies. Based on preliminary figures, total transaction volumes in 2016 remained largely stable from the RMB 200 billion recorded in 2015.

- Overall, office and retail accounted for over 74% of total transaction volume while the apartment sector accounted for another 15%. Meanwhile, transaction volumes in the industrial sector remained thin given the limited availability of assets for sale.

- Foreign investors continued to retain a strong interest in China although many have been priced out of the market given the low yields.

Exhibit 28: Real Estate Transaction Volume in China

Exhibit 29: Office Supply & Vacancy Rate in Beijing and Shanghai

Note: F = forecasts. There is no guarantee the forecasts will materialise.
Source: Real Capital Analytics, Deutsche Asset Management, as at Jan 2017
Strategic Outlook: Hong Kong

- Tenant decentralisation continues to gain momentum as rental gap widens between core and non-core areas. Completions of high-quality supply in decentralised area are expected to pull down rents especially in 2017 and 2018.
- The slowdown in China’s economy continues to have an impact on Hong Kong’s tourism sector. This coupled with the weaker Yuan have continued to impact retail sales.
- Office investment remains predominantly driven by end-users
- Higher yield expectations may cap capital value growth

**Occupier**

- Widening rental gap between core and non-core areas have encouraged more tenants to decentralize. Completions of high quality office development along with attractive rents in non core areas could draw more international financial institutions out of the traditional CBD areas and put a cap on rents especially in 2017 and 2018.
- Challenges in the Hong Kong retail sector remain significant with slowing visitor arrivals, falling tourist expenditure and a strong Hong Kong dollar. Landlords are adjusting to the changing market conditions, exploring new business models, and catering its services towards the local population.
- 3PLs and retailers remain cautious towards leasing warehouse space amid ongoing weakness in retail market and subdued external trade environment.

**Investment**

- Mainland Chinese companies have been active in Hong Kong and have elected to purchase office building for self-occupation.
- Local investors continue to retain a strong interest in retail properties located near local residential catchments.
- Investment demand for industrial properties has weakened considerably given the expiry of industrial buildings revitalization policies in March 2016.
- Corporate end-users seeking to have a long term presence in Hong Kong particularly Chinese companies are expected to continue to dominate the investment market. However, tighter capital controls by the Chinese government could cap investment activities in the coming quarters.

**Exhibit 30: Real Estate Transaction Volume in Hong Kong**

<table>
<thead>
<tr>
<th>Year</th>
<th>Office (HKD bn)</th>
<th>Retail (HKD bn)</th>
<th>Industrial (HKD bn)</th>
<th>Apt (HKD bn)</th>
<th>Hotel (HKD bn)</th>
</tr>
</thead>
<tbody>
<tr>
<td>2007</td>
<td>70</td>
<td>30</td>
<td>10</td>
<td>20</td>
<td>10</td>
</tr>
<tr>
<td>2008</td>
<td>80</td>
<td>40</td>
<td>15</td>
<td>25</td>
<td>15</td>
</tr>
<tr>
<td>2009</td>
<td>90</td>
<td>50</td>
<td>20</td>
<td>30</td>
<td>20</td>
</tr>
<tr>
<td>2010</td>
<td>100</td>
<td>60</td>
<td>25</td>
<td>35</td>
<td>25</td>
</tr>
<tr>
<td>2011</td>
<td>110</td>
<td>70</td>
<td>30</td>
<td>40</td>
<td>30</td>
</tr>
<tr>
<td>2012</td>
<td>120</td>
<td>80</td>
<td>35</td>
<td>45</td>
<td>35</td>
</tr>
<tr>
<td>2013</td>
<td>130</td>
<td>90</td>
<td>40</td>
<td>50</td>
<td>40</td>
</tr>
<tr>
<td>2014</td>
<td>140</td>
<td>100</td>
<td>45</td>
<td>55</td>
<td>45</td>
</tr>
<tr>
<td>2015</td>
<td>150</td>
<td>110</td>
<td>50</td>
<td>60</td>
<td>50</td>
</tr>
<tr>
<td>2016E</td>
<td>160</td>
<td>120</td>
<td>55</td>
<td>65</td>
<td>55</td>
</tr>
</tbody>
</table>

**Exhibit 31: Office Supply and Vacancy Rate in Hong Kong**

<table>
<thead>
<tr>
<th>Year</th>
<th>New supply (000 sqm)</th>
<th>Net absorption (000 sqm)</th>
<th>Vacancy rate (RHS)</th>
</tr>
</thead>
<tbody>
<tr>
<td>2004</td>
<td>300</td>
<td>200</td>
<td>5%</td>
</tr>
<tr>
<td>2005</td>
<td>310</td>
<td>210</td>
<td>4%</td>
</tr>
<tr>
<td>2006</td>
<td>320</td>
<td>220</td>
<td>3%</td>
</tr>
<tr>
<td>2007</td>
<td>330</td>
<td>230</td>
<td>2%</td>
</tr>
<tr>
<td>2008</td>
<td>340</td>
<td>240</td>
<td>1%</td>
</tr>
<tr>
<td>2009</td>
<td>350</td>
<td>250</td>
<td>0%</td>
</tr>
<tr>
<td>2010</td>
<td>360</td>
<td>260</td>
<td>0%</td>
</tr>
<tr>
<td>2011</td>
<td>370</td>
<td>270</td>
<td>0%</td>
</tr>
<tr>
<td>2012</td>
<td>380</td>
<td>280</td>
<td>0%</td>
</tr>
<tr>
<td>2013</td>
<td>390</td>
<td>290</td>
<td>0%</td>
</tr>
<tr>
<td>2014</td>
<td>400</td>
<td>300</td>
<td>0%</td>
</tr>
<tr>
<td>2015</td>
<td>410</td>
<td>310</td>
<td>0%</td>
</tr>
<tr>
<td>2016E</td>
<td>420</td>
<td>320</td>
<td>0%</td>
</tr>
</tbody>
</table>

Note: F = forecasts. There is no guarantee the forecasts will materialise.
Source: Real Capital Analytics, Deutsche Asset Management, as at Jan 2017
Strategic Outlook: Singapore

- Economic growth slowed below 2% in 2016 but cyclical recovery is expected on base case scenario of gradual improvement in global trade conditions.
- Real estate demand-supply dynamics generally remain pro tenants though supply pressures are expected to ease significantly after 2017.
- Office rental growth capped in the short term given the large supply CBD office pipeline, but cyclical rental recovery over the next few years should present good opportunities for investors looking at long-term capital growth.
- We remain positive on the logistics space underpinned by high income yields, particularly assets with exposure to domestic non-discretionary consumption.

Occupier

- Overall office leasing demand remained muted with businesses delaying expansion plans in view of the slowing economy while the financial sector continues to tackle restructuring challenges. Flight-to-quality trends are likely to continue as tenants attracted to lower rentals relocate to newer buildings with higher grade specifications.
- Office rental growth and occupancy levels remain pressured by a supply surge this year though a significant pullback in supply pipeline after 2017 could set the stage for a medium-term cyclical rental recovery.
- Retailing environment faces challenges with operating costs and weaker consumer spending, though prime suburban malls underpinned by local non-discretionary spending are likely to outperform.
- Industrialists likely to see further headwinds this year though rentals are expected to see some recovery from next year in an improving global trade environment.

Investment

- Preliminary data indicates investment sales have rebounded 25% year on year in 2016 to a three-year high, spurred by foreign acquisitions of prime office assets including Qatar Investment Authority’s purchase of Asia Square Tower 1 for SGD 3.4 billion.
- Keen investor appetite for quality core assets combined with strong balance sheet positions of real estate owners to underpin stability in prime yields.

Exhibit 32: Real Estate Transaction Volume in Singapore

Exhibit 33: Office Supply and Vacancy Rate in Singapore

Note: F = forecasts. There is no guarantee the forecasts will materialise.
Source: Real Capital Analytics, Deutsche Asset Management, as at Jan 2017
Strategic Outlook: Australia

- Tightening vacancy to be accompanied by reduced incentives particularly in the Grade A office segment in Sydney and Melbourne.
- Industrial assets remained keenly sought after given the comparatively higher returns.
- Commercial properties in Australia provide higher excess returns relative to the 10-year government bond yield which provides a margin of safety should interest rates rise faster than expected.

Occupier

- Tenant demand in Sydney and Melbourne has been broad based and mainly driven by organic growth from businesses particularly from the financial and business services sector. Limited new supply in 2017 and 2018 coupled with increasing withdrawals of office stock is expected to lead to a tightening in vacancy.
- Tenant incentives in Sydney and Melbourne are expected to decrease from its cyclical peak in 2015 to 27 months and 34 months respectively by 2018 while incentives in Brisbane are expected to remain comparatively flat at 43 months’ rent free (for 10-year leases). Meanwhile, incentives in Perth have increased sharply from 50 months’ rent free in 2015 and are forecasted to remain elevated, extending to circa 59 months’ rent free before trending down gradually from 2018 onwards.
- Leasing demand in the regional shopping centres remained firm supported by international retailers seeking to expand. Neighbourhood shopping centres despite being more resilient have been under pressure given the lower growth in food spending and strong competition between supermarkets.

Investment

- Preliminary data indicates investment volumes falling by 36% year on year in 2016 as owners held on to stock given limited reinvestment opportunities. Investors continued to retain a strong preference for office sector, accounting for close to 50% of total investment volumes.
- Interest from both domestic and international investors remained strong given the relatively high spreads, and prospects of rental growth particularly in Sydney and Melbourne has attracted buyers.
- Portfolio transactions have continued to gain favour given the competition for industrial assets.

Exhibit 34: Real Estate Transaction Volume in Australia

Note: F = forecasts. There is no guarantee the forecasts will materialise.
Source: Real Capital Analytics, Deutsche Asset Management, as at Jan 2017
Exhibit 35: Office Net Supply and Vacancy Rate in Sydney and Melbourne

Note: F = forecasts. There is no guarantee the forecasts will materialise.
Source: Real Capital Analytics, Deutsche Asset Management, as at Jan 2017
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