



Outlook for Australian Property Markets 2010-2012

Brisbane

Update August 2010



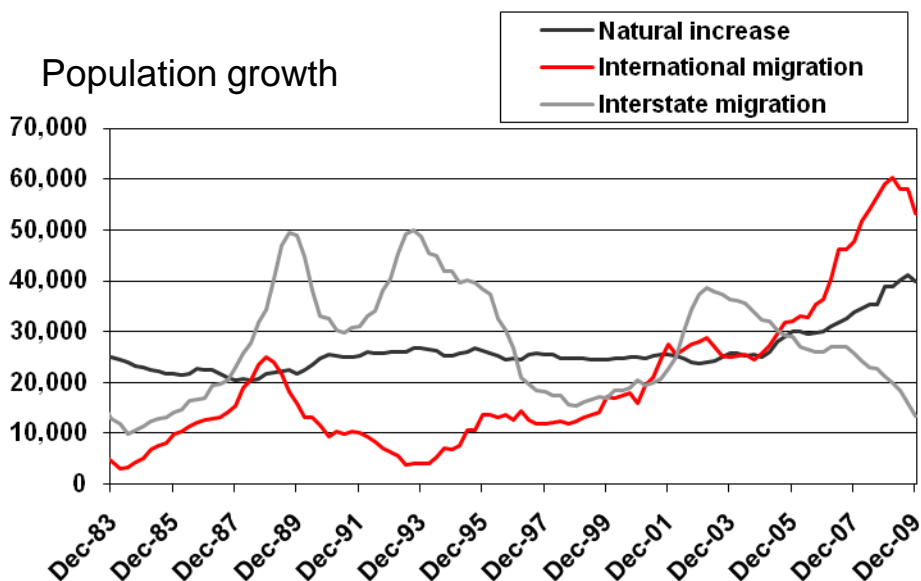
Outlook for Australian Property Markets 2010-2012

Brisbane Residential

Update August 2010

Population growth slowing, but still above average

Population growth – yearly rolling total

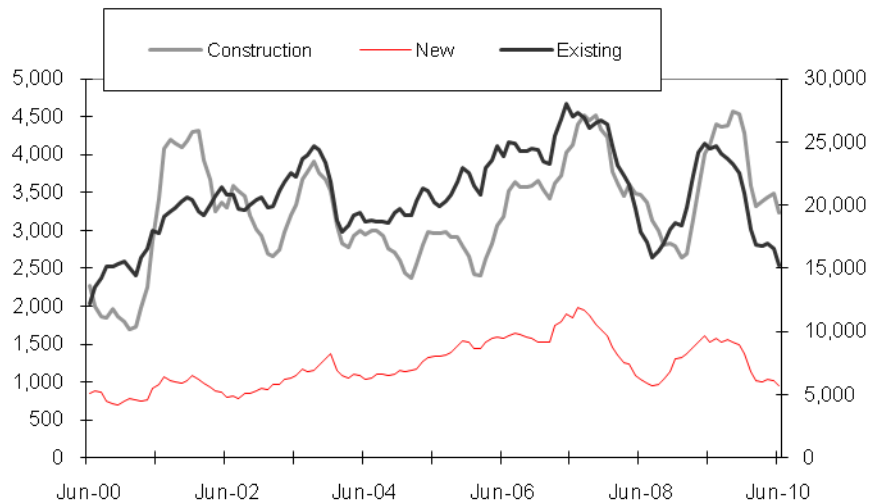


Source: ABS

- Queensland's population growth rate slowed in 2H 2009 as international migration and interstate migration eased. However, at 2.4% in the year to December 2009 it remained above the longer term average of 2.3%. There were a total of 106,560 new residents to Queensland in 2009, well above the 73,110 average since 1982.
- Despite slowing, net international migration remained very strong at 53,265 people. Natural growth also remained very strong at almost 40,000 people, again well above average.
- The one area for possible concern is the declining numbers of interstate migrants. While still the highest of any State in the country, at 13,519 it is the lowest in over 16 years.
- While expectations are for immigration numbers to continue to slow, the population growth may well be buoyed by increasing interstate migrants as the mining sector takes off again. However, this is more likely from 2011.

Finance plummets, but construction holds better than others

Finance commitments for owner occupiers and investors - 3MMT

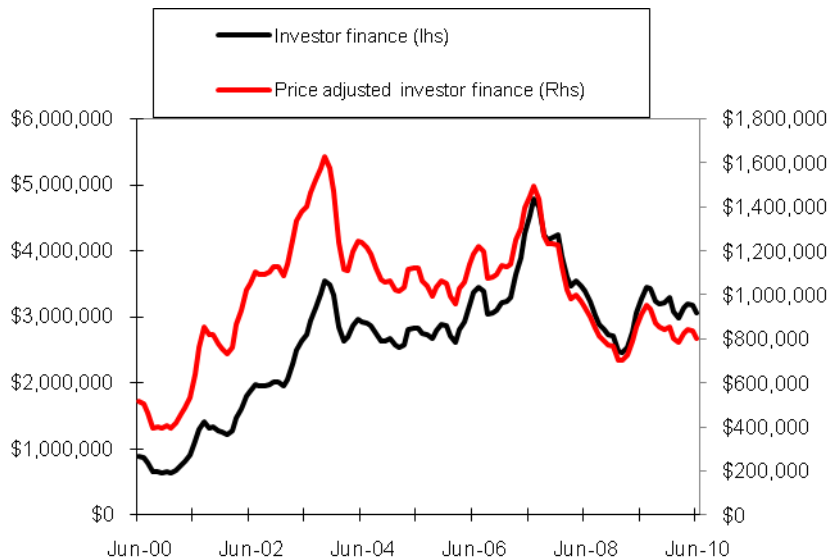


Source: ABS, REIA
Analysis: Westpac Property

- The impact of the fiscal and monetary stimulus was noted in February. However, as the stimulus was removed, finance commitments plummeted in 1H 2010.
- Finance commitments to construct a new dwelling fell by 25% between December 2009 and June 2010, while finance to buy new fell 31%. There was evidence that this market was slowing in Q4 2009, but the speed of decline has surprised. Finance levels for construction are back to mid 2008 levels, while finance for new dwellings are at early 2000 levels.
- The development market was expected to slow as first home buyers declined, but the decline of finance for existing dwellings was the biggest surprise. These fell 27% in 1H 2010.
- While confidence in Queensland was largely positive in 1H 2010, high volatility was evident which may explain the extent of the downturn. Should economic fundamentals improve as expected, activity in the housing market should follow.

Investors slow, but not as much as owner occupiers

Finance commitments for investors - 3MMT

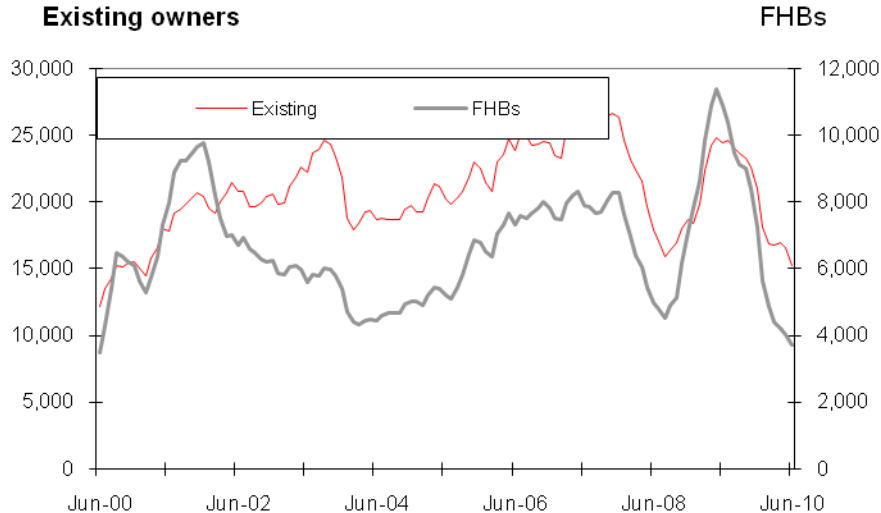


Source: ABS, REIA
Analysis: Westpac Property

- Investor activity does not appear to have been as affected as owner occupier activity. While slowing from the mid 2009 highs, the investors appear to have more confidence than owner occupiers.
- Investor finance slowed by some 10% during the first half of the year, while price adjusted finance fell by a lesser 6%.
- While nominal investment value is around pre-2007 boom levels, price adjusted is at early 2000s levels.
- Expectations are for this sector to remain active into 2H 2010, with the potential of a slowdown in 2011, should rates rise as expected.

First home buyers falls as expected, upgraders surprisingly follow

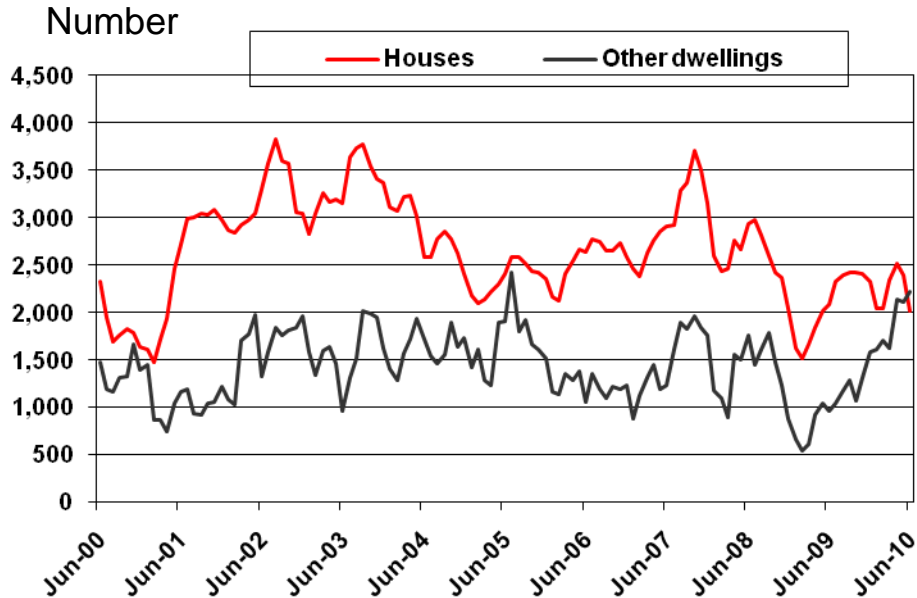
First homes buyers tumble - Qld 3 monthly moving totals



- The number of first home buyers (FHB) continued to decline, although at faster rate than expected in 1H 2010. FHBs were some 50% lower in June 2010 than in December 2009 and are at their lowest level in 10 years.
- We expect this group of buyers to remain relatively weak over 2H 2010, with many having been pulled forward to 2009. However, the rate of decline should slow.
- As mentioned the existing owner occupiers were the biggest surprise in terms of decline. While interest rate hikes were expected, we considered that the creation of new jobs would counter the negative from higher interest rates. Full time jobs in Queensland rose by almost 35,000 in the six months to June, a growth rate of 2.2%. Total jobs were up 44,700 over the same period. As mentioned previously, volatile consumer confidence may have resulted in major decisions being put off. With continued improvement expected we expect this market to improve in 2H 2010.

Under supply continues despite lift in other dwelling approvals

Dwelling approvals – Brisbane 3 monthly moving totals

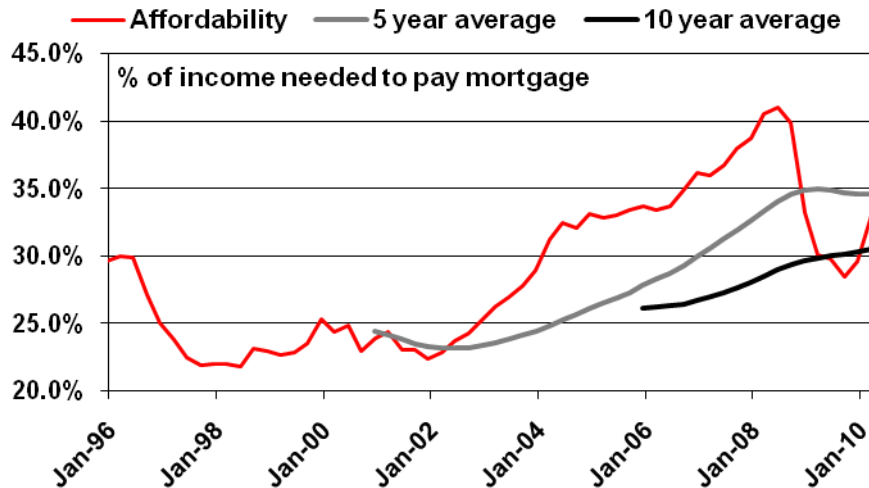


Source: ABS

- Dwelling approvals remained weak in 2010, despite signs of a recovery in activity. At 8,200 dwellings approved figures were the highest for almost three years and generally above the levels of the late 2000s. The growth was attributable to other dwellings, with house approvals falling in the half year.
- Brisbane's population grew at 52,100 in the year to June 2009. The highest level in at least nine years of ABS data.
- Dwelling approvals of 12,645 in 2009 or even the higher 15,837 in the year to June 2010 would not meet the requirements for this level of population growth. Allowing 2.6 persons per dwelling (Census 2006), some 20,038 dwellings would be required, before the consideration of demolitions and non starts are taken into account.

Affordability bottomed out in Q3, rose as expected in 2010 but sits around 5 year average

Home loan affordability - Queensland



Source: REIA

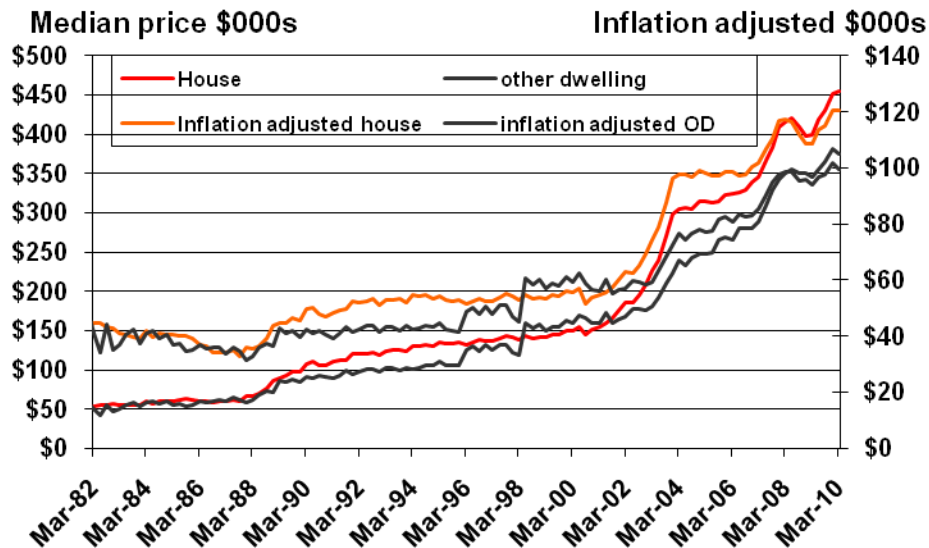
- As expected, rising interest rates and an increased loan size has led to a decline in the affordability of Queensland's residential markets. The proportion of average household income needed to pay an average mortgage rose to 33% in Q1 2010. With further interest rate hikes in April and May we consider this will have risen to 34.4% by end Q2 2010, assuming limited growth in loan size.
- At 34.4% the repayment proportion will be around the average level of the past five years, but above the 10 year average.
- Should prices rise in line with household income (which grew at 6.7% in the year to March 2010) and interest rates rise as Westpac Economics believe in 2011, the proportion would rise to 35.6%. While above the five year average it would be below the 41% proportion evident in mid 2008, which made Queensland the least affordable State.



Australia's First Bank

Price growth slows, confidence the key to future growth

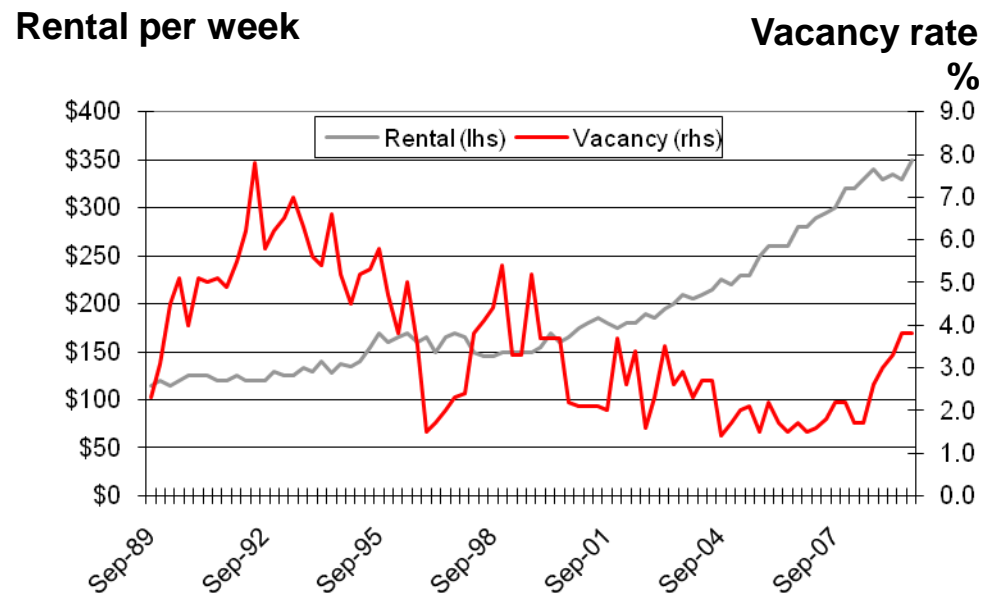
Brisbane median house & other dwelling prices



- In February we anticipated a slowing of price growth but no falls in 2010. Following growth of 13% for houses and 9% for other dwellings in 2009, we anticipated around 5% for 2010.
- House price growth in Q1 was a low 0.9%, while other dwellings fell by 1.7%. With weak demand in Q2 there is little to suggest any different in this quarter.
- Although expectations are for a pick up in demand in 2H 2010, the market appears cautious. Although affordability is around the 5 year average, a pick up in local market confidence is needed to drive prices up. This may now not come until 2011, although interest rate hikes may impact on this.

Vacancy continued to rise despite under supply, but rents rose

Rental and vacancy

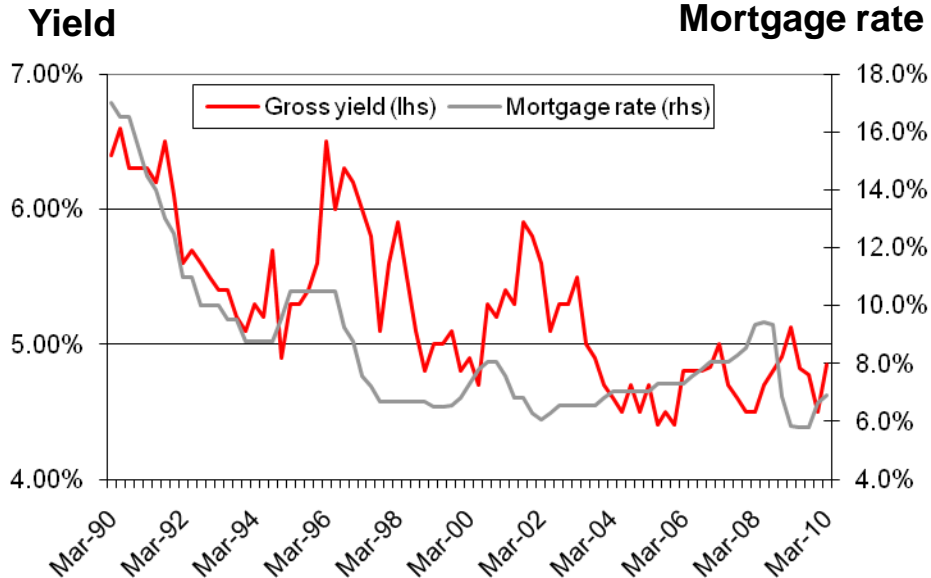


Source: REIA

- Strange things are happening in the Brisbane market!. Vacancy continued to increase in the six months to Q1 2010, despite continued undersupply and the slowdown of FHBs moving into ownership. REIQ data suggests that vacancy reached 3.8% in Q1 2010, up from 3.3% in Q3 2009. Rule of thumb is equilibrium would be around 3%.
- However, our expectations of rental growth have eventuated, driven we expect by higher interest rates and, despite the vacancy rate, supposedly a lack of choice. Rents rose by 6.1% in Q1 2010, after falling in Q4.
- Our expectations are that vacancy should start to fall in 2H 2010 given population growth, placing further pressure on rents. This should continue into 2011 as interest rates rise, although the level of vacancy could mute some of the growth.

Yields forecast changed, now above 5% by year end as rental growth outstrips prices

Gross residential yields against mortgage rate – Brisbane other dwellings



- Investment yields rose to 4.9% in March 2010 as a combination of falling 'other dwelling' prices and rising rents impacted. Our forecast was for yields of around 4.7% by year end, but with the lack of strong activity being shown in the buyers market we have adjusted our price growth forecasts.
- Similarly we have adjusted our yield forecast to over 5% by year end.



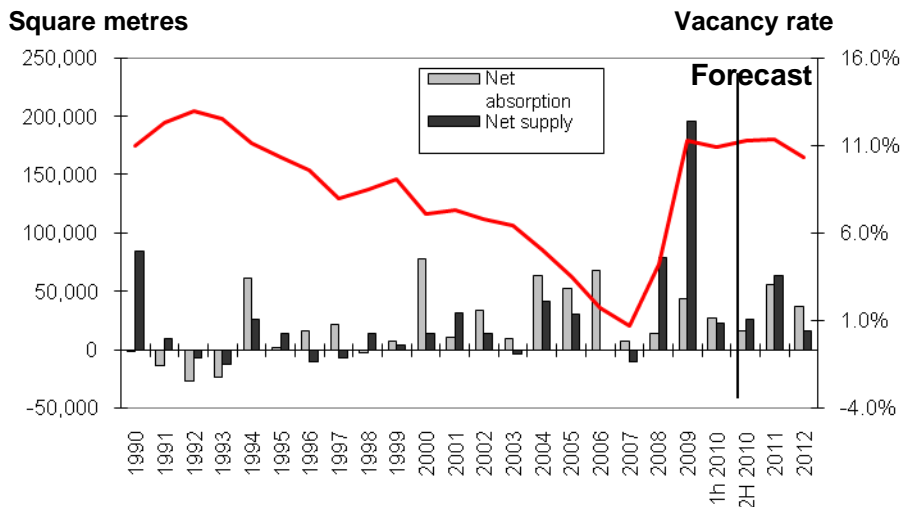
Outlook for Australian Property Markets 2010-2012

Brisbane Office

Update August 2010

Brisbane CBD office market near peak, but supply continues

Supply, demand and vacancy in Brisbane CBD



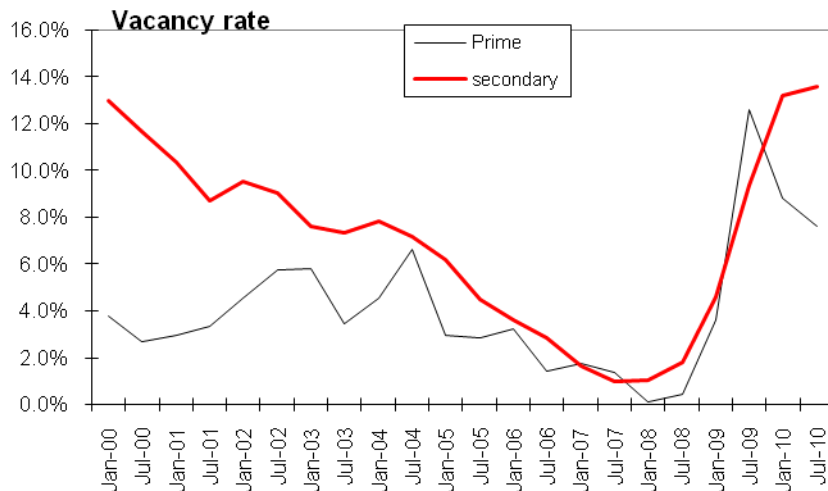
- Vacancy fell to 10.9%, from 11.3%, as net absorption exceeded supply in 1H 2010. Stronger than expected net absorption of 27,500 square metres drove the vacancy down.
- While the current development cycle is nearing an end, two major projects, Albert Street at 38,000 square metres and One One One Eagle street at over 60,000 square metres will affect the market. Added to this is the relocation from the CBD of Energex later this year.
- As indicated in February the risk is to the upside for demand as the resources boom takes off. Accordingly, we have increased our net absorption figures.
- Our forecasts now have vacancy lifting slightly in 2H 2010 before plateauing in 2011 and falling into 2012. However, at 10.3% by end 2012 it will remain well above the longer term average of 6.7%.
- To reach the long term average vacancy rate, net absorption will need to match that of 2004 to 2007 at an average of almost 62,000 square metre per annum. Long term average is 37,600 square metres.

Source: Historical data: PCA Office market report July 2010

Forecasts: Westpac Property

Shift to quality continues into 2010

Vacancy by grade – Brisbane CBD



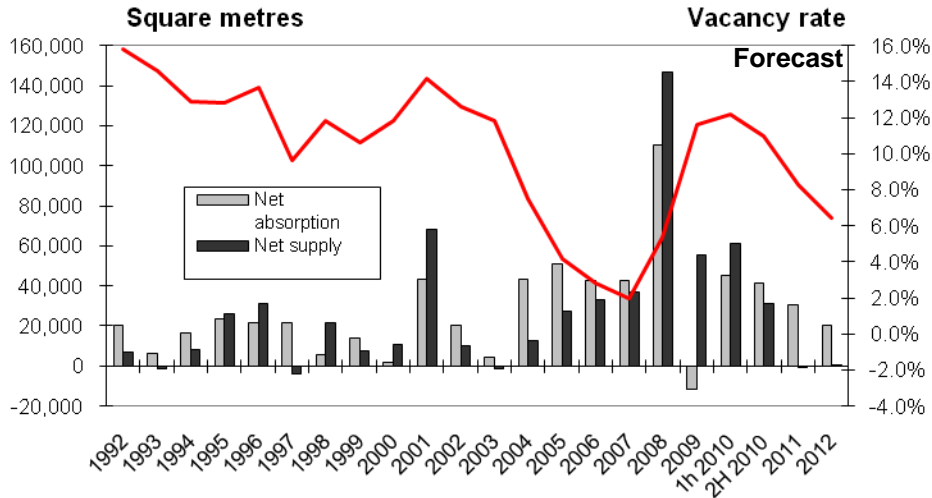
- Vacant prime office stock amounted to 69,200 square metres at July 2010, down from 73,000 square metres at the start of the year. The vacancy rate fell to 7.6% from 8.8%.
- Secondary vacancy rose during the same period, with the vacancy rate rising to 13.6%.
- The flight to quality, noted in February's forecast, continues as expected. Although prime space is under construction, the low level of pre-commitment should result in a continued competitive environment for tenants.

Source: Historical data: PCA Office market report July 2010

Forecasts: Westpac Property

Brisbane 'near city' vacancy peaked, but stock still to complete

Supply, demand and vacancy in 'Near City' Brisbane



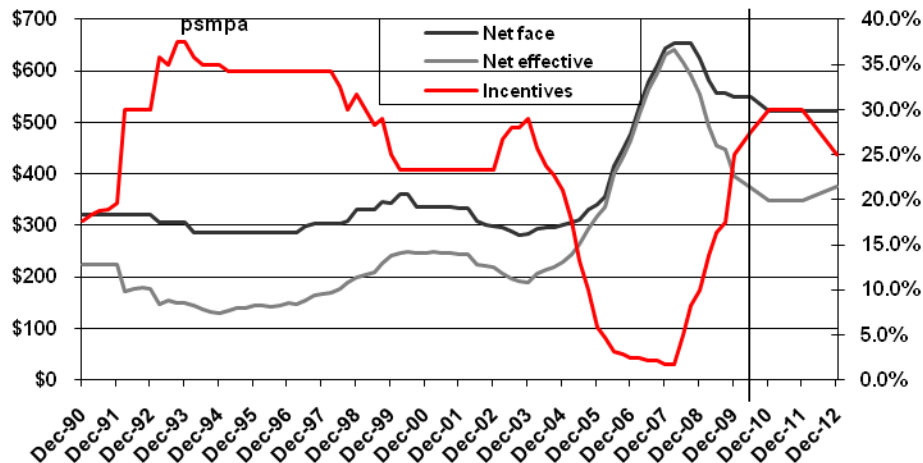
- In the stronger economic climate expected over the forecast period we have adjusted our peak vacancy rate from 13.9% by year end to the consideration that vacancy peaked in July 2010 at 12.2%.
- Future supply is still high but is largely pre-committed to Energex. Although projects with a DA amount to 42,500 square metres, the current high level of vacancy, combined with the high vacancy in the CBD is unlikely to see projects start and complete before end 2012.
- However, we do anticipate a pick up in tenant demand which with a lack of supply will help reduce vacancy to around 6% by end 2012.
- By this time new projects are likely to have commenced.

Source: Historical data: PCA Office market report July 2010

Forecasts: Westpac Property

Brisbane CBD rents near, if not at, bottom

Prime net effective rents – Brisbane CBD



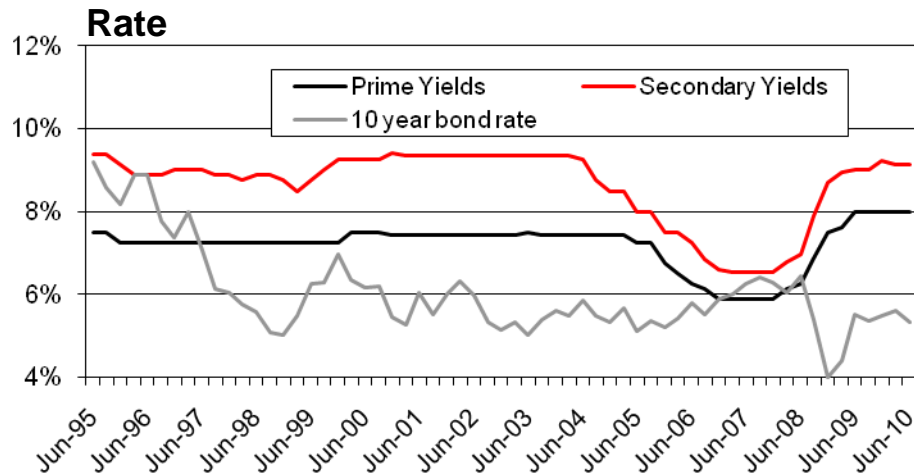
Source: CB Richard Ellis historic data to July 2010

Forecast: Westpac Property

- In February we suggested that incentives could peak at 30% over the next year, but that an improving level of demand may well fill prime vacancy faster than expected, enticed by the incentives. In February further declines of 11% in effective rents were expected in 2010, with a peak to trough fall of over 45% by the second half of the year.
- In the first half of 2010 net effective rents fell by almost 6% as incentives rose to 27.5%. Although there is potential for stronger than forecast demand, the level of uncommitted new supply means we maintain our February forecasts, for now.
- Q2 2010 data suggested a stabilising in rents and incentives according to CBRE. If this is the case, it is difficult to forecast any uplift in rents given supply levels.

Yields stabilise, little change expected

Prime and secondary yields against the 10 year bond rate



- Our forecast of limited change in yields is proving correct with no movement in the Brisbane market in 1H 2010. However, prime and secondary values fell by around 2% over the six months as rents fell.
- We continue to forecast limited movement in yields, with investors still concerned about the level of vacancy. As this improved, pressure on values and yields will increase.
- Yields are well above their ten year averages and risk premium to the 10 year bond rate. This may well attract the speculative buyer, looking for long term gain for a market at bottom.
- Near City yields firmed by around 20 basis points over the half year, but remain above their ten year average. Prospects for capital growth in this market should improve from 2011 as vacancy falls.



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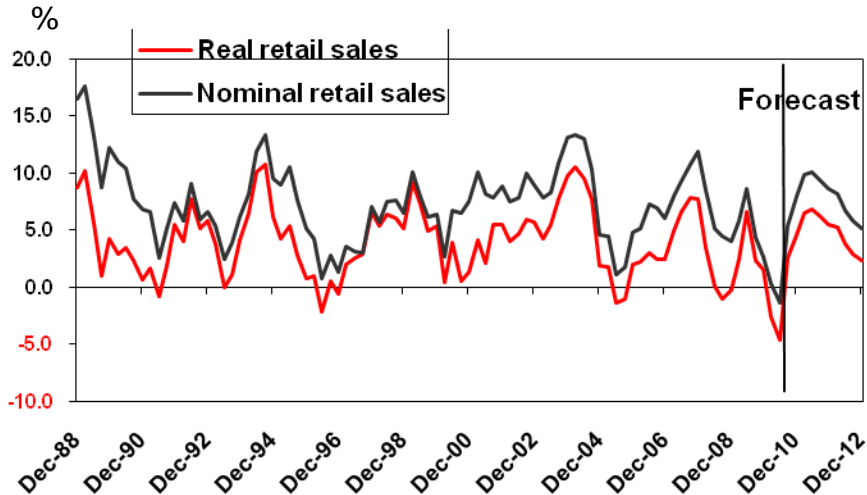
Brisbane Retail

Update August 2010

Retail sales fell in Q2 2010, strong pick up predicted

Change in retail sales

Change on same qtr in previous year



- The removal of the stimulus in the form of low interest rates and cash handouts impacted Queensland more than most in 1H 2010. In the year to the June quarter ABS data suggests retail sales fell.
- However, after a negative view in February, Access Economics have become more bullish on Queensland, forecasting strong retail sales growth. While much of the 10% forecast for the next twelve months will be a recovery from current levels plus growth, it is high.
- They forecast a slowing back towards average by 2012.

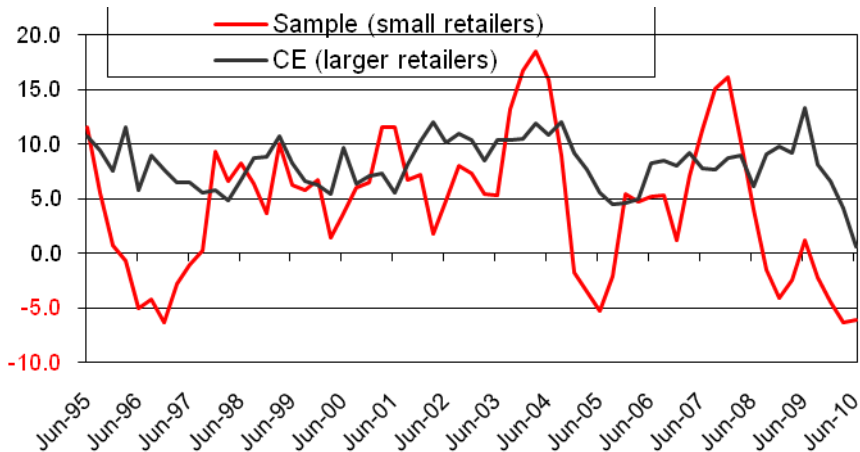
Source: ABS

Forecast: Access Economics

Both large and small retailers hit by slowdown

Change in retail sales - Queensland

% change on same qtr in previous year



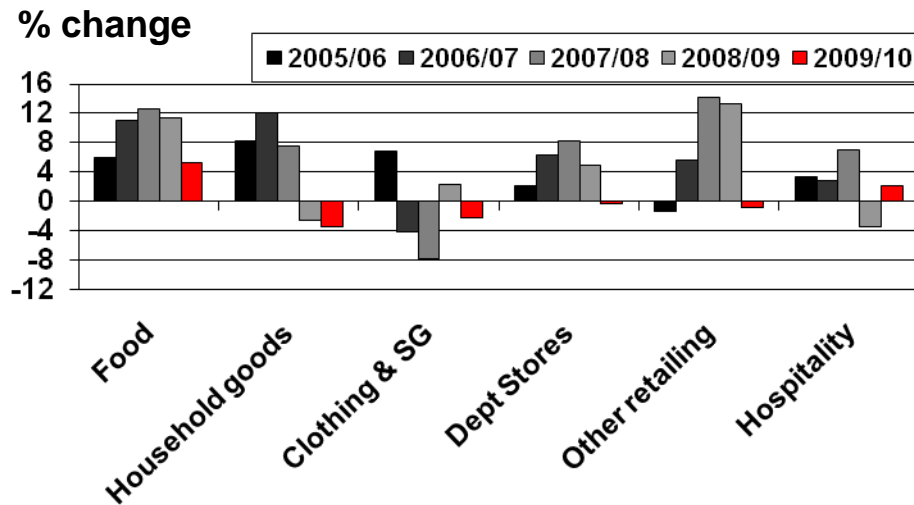
- The breakdown of retail spending by smaller retailers, where the ABS takes a sample of retailers, and larger retailers who are completely enumerated (CE) shows who has benefitted from the cash handouts in Queensland.
- Smaller retailers continue to be impacted by the removal of stimulus in 1H 2010, with sales some 6% lower than a year earlier. This should pick up if Access Economics forecasts for total retail sales are correct.
- However, the normally steady larger retailers were also impacted, with annual sales growth slowing to virtually nothing. The pick up in retail sales should ensure stronger turnover into 2011.

Source: ABS

Analysis: Westpac property

All sectors impacted by the retail sales slowdown

Annual change in retail spending by sector - Queensland

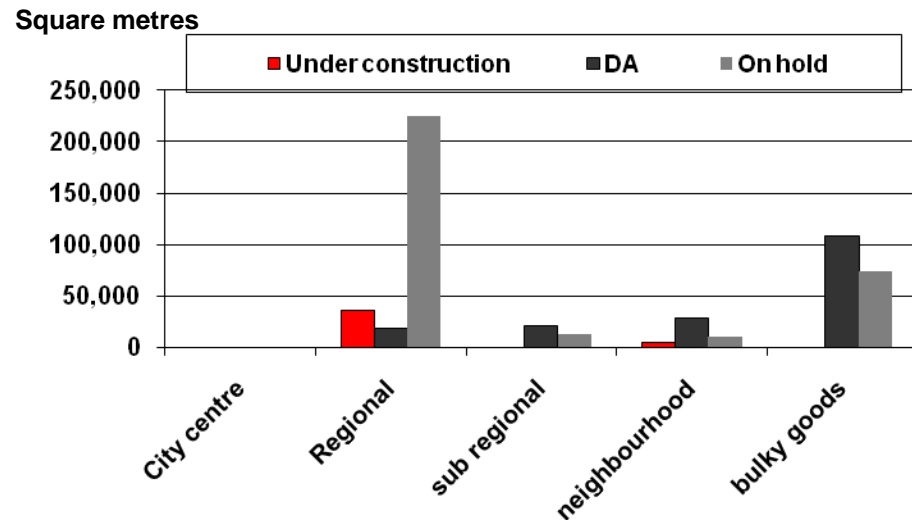


Source: ABS

- Analysis of sales by sector type reveals areas where tenant security or expansion is likely to emanate.
- The slowdown in spending in the year to June has impacted on all sectors. As usual food has been one of the strongest sectors, with growth of over 4%.
- Of the other sectors, only hospitality posted a positive result, with household goods sales falling for the second consecutive year.
- Clothing and soft goods also fell and have delivered only one positive year in the past four.

Retail supply stays minimal

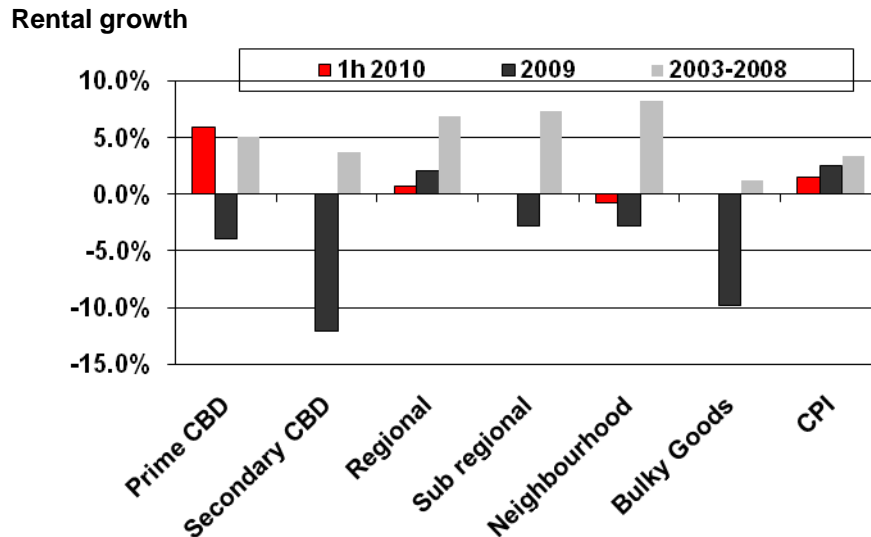
Future and possible retail stock Brisbane



- Retail construction remains sluggish in South East Queensland, which is not surprising given the growth in retail sales.
- Although there are around 500,000 square metres with a DA or on hold, the likelihood of these commencing soon is low. However, as sales growth picks up development should follow in a stronger economic environment

Rents mixed in 1H 2010

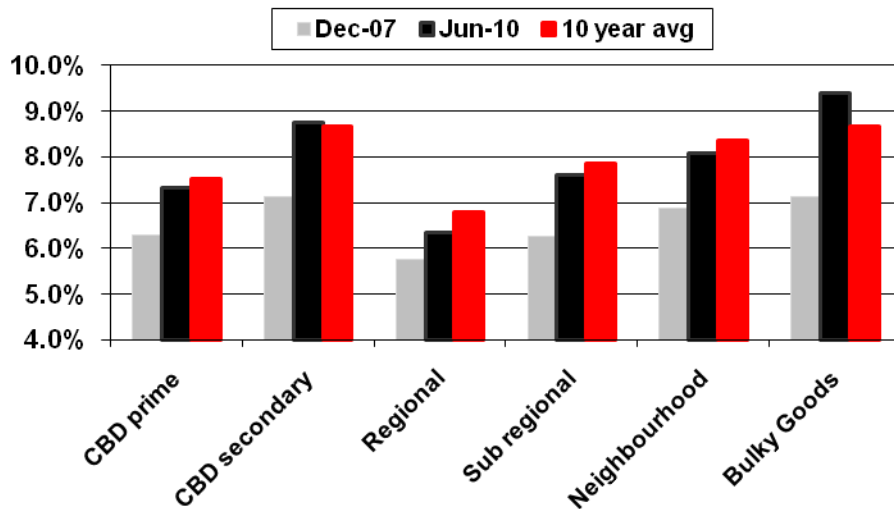
Rental growth – Brisbane retail



- With the exception of prime CBD retail rents were largely on hold in 1H 2010. This continued the trend of stabilisation experienced in Q4.
- This is not surprising given the lack of sales growth, although if Access economics are correct and sales growth surges into next year, a lack of any new supply could result in rents lifting again into 2011.

Yields stabilisation continues

Average yields – Brisbane retail



- The stabilisation in retail property yields identified in Q4 2009 has continued into 2010, as expected. The only movement has come from Bulky Goods centres with a minor firming of 10 basis points.
- However, with the exception of CBD secondary centres and bulky goods centres yields remain slightly below their ten year averages.
- Should retail sales pick up as forecast, rising rents may well result in stronger investor interest into 2011 and pressure on yields to firm.



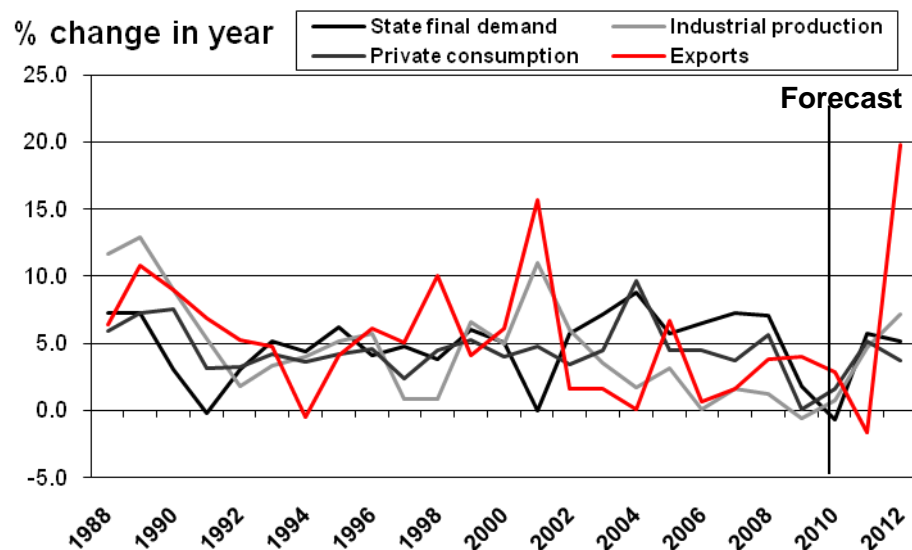
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Brisbane Industrial

Update August 2010

Demand to rise as economic recovery gathers pace in 2011

Industrial drivers Queensland

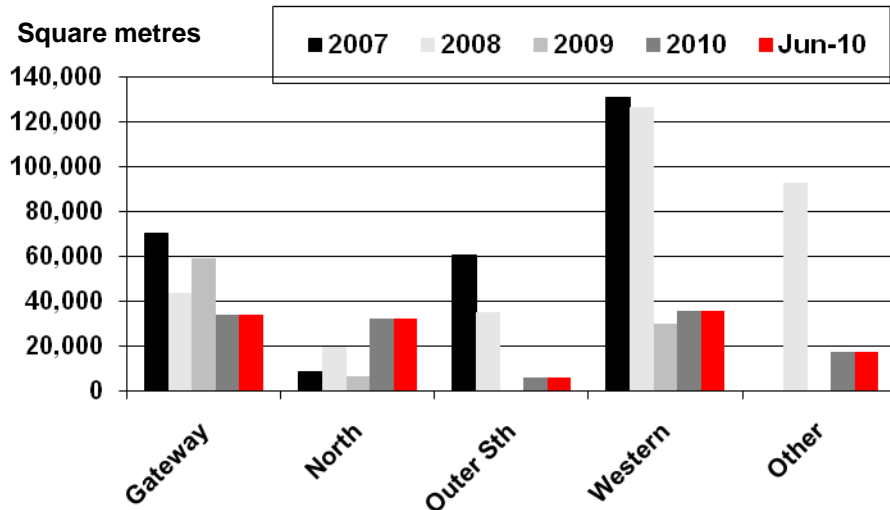


Source: Access Economics

- The economic slowdown experienced in 2009, which dragged into 1H 2010 for Queensland's industrial drivers is expected to end over the remainder of the forecast period.
- Ignoring the surge in exports in 2012, largely from mining production, all indicators are expected to improve over the next three years.
- This should help lift demand from industrial tenants.

Supply remains low

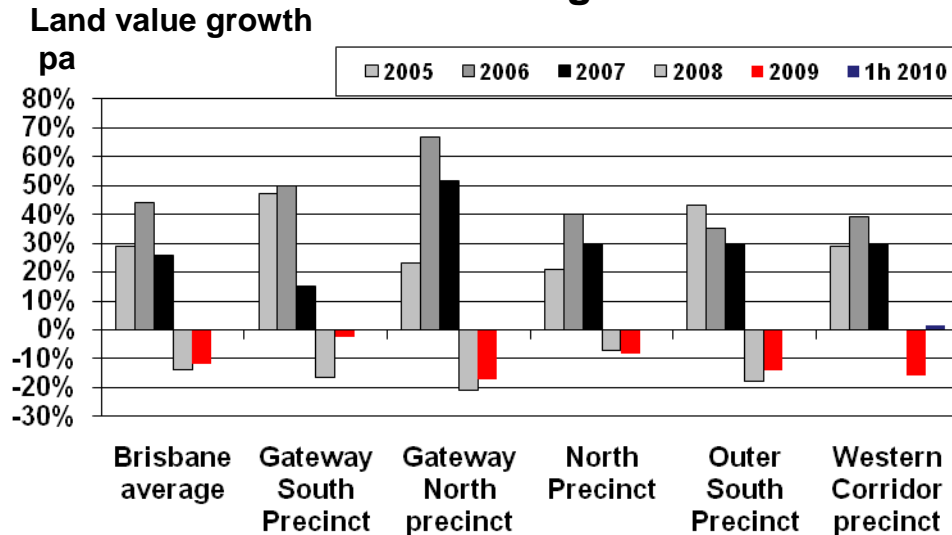
Industrial supply under construction Year start



- The level of new industrial property under construction rose slightly in 1H 2010 to around 125,000 square metres. However, it remains well below the levels of 2006-8.
- The supply is evenly divided between major regions, with only the outer south and M1 Corridor showing little new major construction.
- The level of confidence remains quite low in this sector, as evidenced by the 680,000 square metres that CBRE consider to have been abandoned and a further 380,00 square metre on hold.
- Projects with development approval amount to 540,000 square metres. As such, there is no shortage of potential space that can be built once confidence and demand returns.

Land values plateau

Land value growth

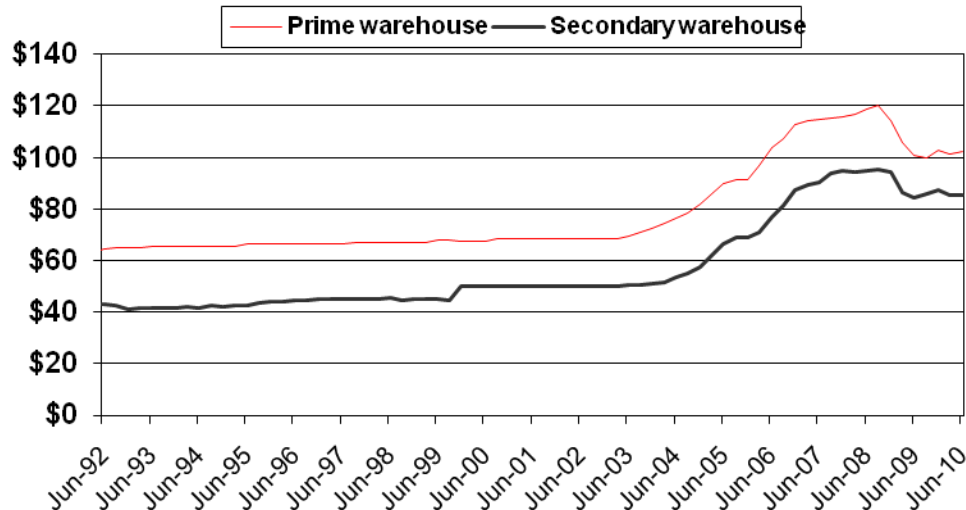


- As expected land values plateaued in 1H 2010. The exception was in the Western Corridor where minor growth was shown, according to CBRE.
- The low level of industrial construction, plus the high level of projects either on hold or with a DA suggests that pressure on land prices is unlikely to lift over at least the short term.

Rentals stabilise, limited growth until at least 2011

Net effective rents – Brisbane

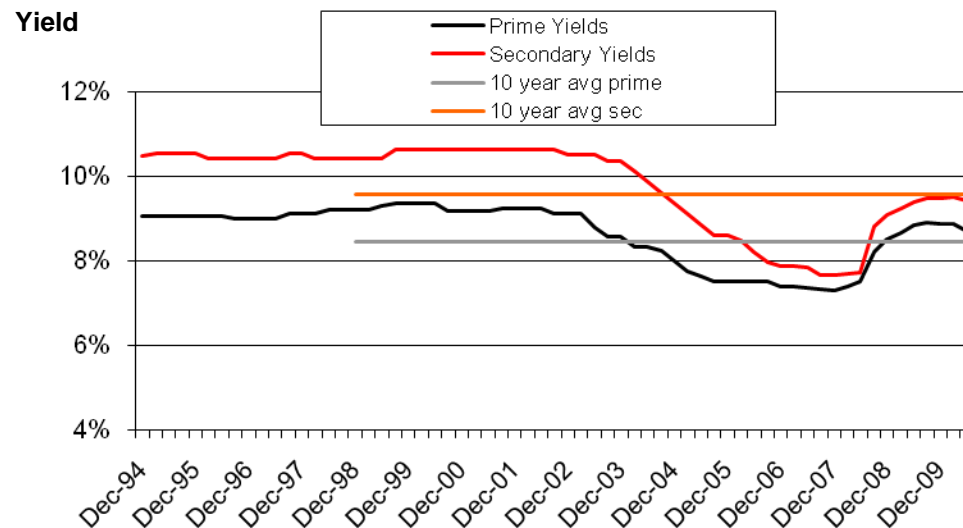
Rental psmpa



- As expected both prime and secondary net effective rents remained largely unchanged in 1H 2010.
- Rents have been stable since Q3 2009 and are back to around 2004/5 levels.
- As forecast in February we expect little change in rents during 2H 2010, but as demand picks up in 2011 falling vacancy should help rental growth commence again.

Yields stabilise, with minor firming, pressure to lift from 2011

Prime and secondary yields against the 10 year average



- Industrial yields recorded a minor firming in 1H 2010, according to CBRE. Prime yields firmed by around 20 basis points, while secondary firmed by around 6 basis points.
- While prime yields remain above their ten year average, secondary have fallen below it.
- With limited rental pressure in 2H 2010, yields should stay on hold. However, for well leased prime properties, yields of around 8.5% may prove attractive and could attract investors, resulting in some pressure on yields over the next six months. This pressure should increase into 2011.
- Secondary yields should remain stable.

Disclaimer

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