Stamford Insights – February 2012

Key Points

- **Weak sentiment from Q4-2011 has carried over to the new year**
- **Some concern over liquidity but there is currently reasonable supply of capital, both local bank/non-bank and foreign**
- **Whilst there is evidence of bank margins increasing, we believe quality investment debt facilities will continue to attract price tension in the market**
- **Non-bank capital has become more price competitive**
- **Equity & junior debt supply available for deals**
- **We recommend clients consider financing well ahead of impending maturity or project requirement**

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2012 Outlook, the last little while……………

The early part of 2012 has seen weak sentiment in the commercial real estate market carry through from the later part of 2011. General business confidence is also low, particularly in those parts of the economy not benefitting from the strength in the resources sector.

The newspapers are certainly not helping the general mood, some headlines from a single recent weekend business section included;

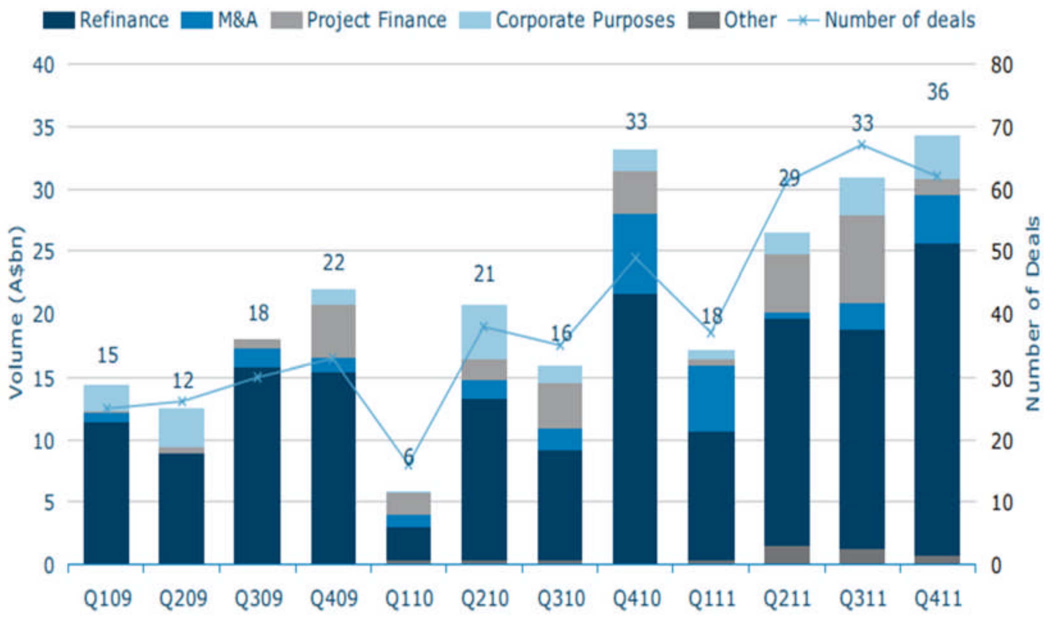
"Company Liquidations Rise…….."
"Fashion in rags…….."
"Dark days for investment banks"
"Slow earnings growth in the aisles"
"The Banks space odyssey" (comment on banks reducing office footprint commensurate with staff reductions)
"Lean times for bulky goods"

Adding to this we have a high profile construction company falling over and a Reserve Bank wrong footing most interest rate forecasters by leaving the cash rate on hold in its first meeting of the year (the banks then increased their lending interest rates for good measure).

Current landscape…………

The market landscape for commercial real estate debt has been influenced by broader economic sentiment as well as direct concerns for increased pricing pressure (see *Stamford Insights October 2011 –B on our website http://www.stamfordcapital.com.au/current-news*) and reduced liquidity given the state of the wholesale finance markets.

It is clear however that borrowers are acutely aware of finance risk post GFC and typically moving ahead of time to deal with impending facility maturities.



(Source: ANZ)

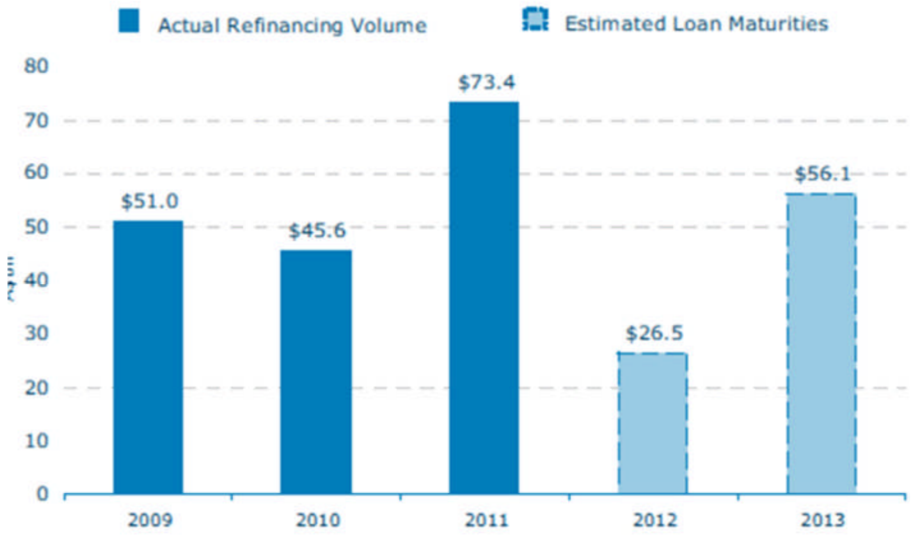
Q4 2011 saw a spike in finance activity in the syndicated debt market (which in 2011 represented ~76% of total Australian loan market), as borrowers anticipated worsening conditions for 2012. Approx 71% of the Q4 loan volume in this market was related to refinance of existing facilities.

Liquidity

Whilst we have seen some non-bank lenders pause, the local lending market remains generally open for business, particularly good quality investment property loans. In fact we believe the amount of capital available in the non-bank market grew in net terms over the second half of 2011.

On the foreign front, 2011 saw debt capital ex-Europe largely depart the market, there was some offset with Asian capital becoming increasingly more active, particularly in transacting directly with sub-institutional market. The foreign capital that is now available is typically seeking a yield premium to local bank pricing but is prepared to provide leverage.

Again looking at the syndicated debt market we see relatively low forecast loan maturities for 2012 off the back of the large volumes set Q4 2011.



(Source: Thomson Reuters LPC)

Given capital availability and lower relative forecast maturities we believe that good quality transactions, particularly for investment assets, will continue to attract capital and competitive pricing.

There remains less depth of capital for development finance and this market will remain open only to proven borrowers having projects with strong dynamics (ie significant pre-sales, quality builder, sound underlying market). This is particularly acute for transactions $10mill plus where the private lending market tends to fall away and options outside the local banks are limited, but they do exist!

Pricing

This year has seen the local banks look to increase pricing, with movements in the order of 10-20bps. This trend looks more likely to continue than not as the wholesale markets remain unsettled and the banks continue to strive for profit growth.

We have however noticed non-bank capital become more price competitive and as noted above we expect such capital to become more attractive to the market on 2012.

Other capital (Equity & Junior Debt)

Equity and junior debt remains available for projects showing appropriate risk/return metrics and investment assets.

Sponsors and providers do however need to be cognisant of senior lenders view on such capital and how it is structured into a transaction.

Closing thoughts…………

The debt market for real estate remains volatile, lenders and continuously entering and exiting the market. We recommend clients allow as much time as they can afford to assess and deal with maturing facilities or project finance requirements.

Stamford prides itself on having market best knowledge of capital for real estate and welcomes the opportunity to work with and assist clients.

Regards,

Stamford Captial Australia.