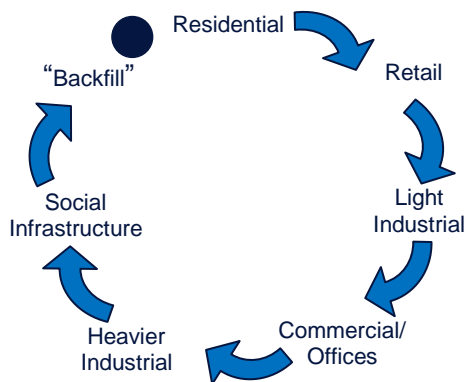


Residential Market Outlook - 2011

Following the relatively strong and active residential property markets in Melbourne especially the inner urban sector during 2009 and into early 2010, the market did slow detectably in the second half last year, as high interest rates in combination with record price levels caused some hesitation. This was however more pronounced in the First Home Buyer and “fringe” market, the relatively inner urban and higher priced market above \$1.0M, still performing well. The apartment market, more than any other sector, remained strong, the new releases of quality well located projects being well subscribed, a trend expected to continue into 2011.

It is important for investors to appreciate that residential investments in various forms, whether houses, townhouses, apartments or land, or even from a construction and development perspective, is of all categories, the lowest risk real estate. This is well demonstrated by the following diagram and explanation.

Development Progression / Relative Risk



This chart demonstrates that development begins and is sustained by a residential nucleus, which as the lowest risk real estate, determines the subsequent sub-markets, which establish in the order of progression demonstrated. As the cycle evolves, each subsequent category relies upon the vibrancy of the preceding markets in consequence of which the risk progressively.

Source: Charter Keck Cramer - Research

Residential property is the most liquid of all real estate classes, it is in demand in some form or another by every individual and is not dependent on immediate association with other property categories such as retail, commercial or industrial, for it to have a buoyant market. At the urban fringe, regionally and at coastal resorts, residential communities have established markets and well evidenced values. Although relatively modest in terms of net income return on an annual basis, when capital growth is taken into account, the combined “Internal Rate of Return”, competes strongly with other property classes.

Investors need to understand, that if they have modest funds, and invest “indirectly” into commercial property through Trusts and Funds, that they will lose a considerable share of return to the Managers. Alternatively, direct investment into residential real estate, can provide a better net result.

The strongest fundamental, strong population growth, will underpin Australia’s residential property markets particularly Melbourne, into the foreseeable future.

Investors should concentrate on establishing a core portfolio of residential real estate before moving to other property classes. Excluding their own residence, a portfolio of \$10.0M makes good sense, if on a wholly residential basis, but perhaps varied to include some established housing, apartments, land, a residential development site, or some sub-division, refurbishment, or construction propositions. The more inner urban the better. Townhouses provide an attractive price alternative to more expensive houses at the same location, and in the opinion of many, a better amenity to apartments in the same locality. It is expected, that townhouses will experience strong capital growth over the next decade.

In Melbourne, sections of South Yarra, now represent the city's highest value residential precinct. In South Yarra, over the decade 2000 - 2010, capital values increased by an average of 10.2% per annum (p.a.), or as may otherwise be expressed, from \$490,000, to \$1.3M. This was better than metropolitan Melbourne as a whole, which grew by around 9.7% over the same period, from \$190,000 - \$480,000.

Highlighting the strong preference for South Yarra, it can be noted that its growth was even stronger than some of the nearby areas which are also considered very select. Compared with South Yarra's outstanding growth of 10.2% p.a., Prahran reflected 9.7%, Toorak 8.9%, and Windsor 9.9% (*Source: Charter Keck Cramer - Research*).

In conclusion, with the prospect that interest rates have now peaked in the current cycle with purchasers becoming relaxed that increases are not on the horizon and with continued population growth, and the pressure of demographic change, Melbourne residential real estate remains a low risk, affordable, liquid, medium to long term investment, to which any prudent investor should give high priority.

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