

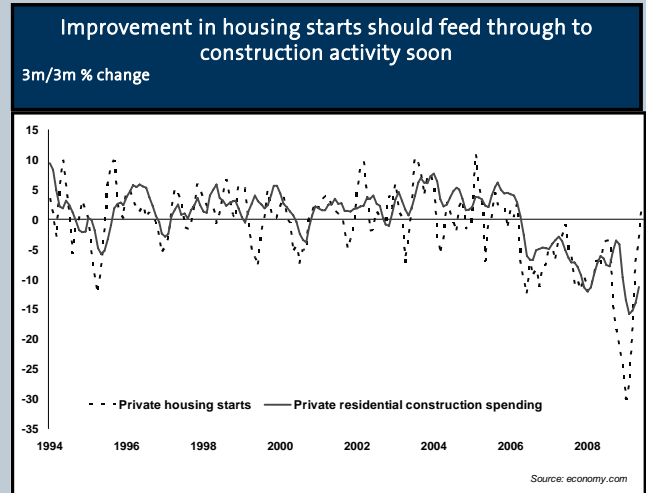
US residential construction spending likely to improve

- The next update on the US construction sector will be the release of construction spending data for June on Monday 3rd. This information is divided into public and private spending, with private spending accounting for almost 70% of the total.
- Total construction sector spending has shown modest signs of stabilisation in recent months although the 0.5% monthly increase recorded in April was more than reversed by a 1% fall in May. That left construction spending 12% lower than in May 2008. Private non-residential construction was the only sector to report a monthly increase in spending but, looking beyond monthly volatility, there has been very little substantial expansion in that sector since October 2007. However, construction spending in the weak commercial property sub-sector fell by 32% in the 12 months to May 2009. Given the dearth of new construction planned (as noted in the Fed's Beige book released on Wednesday 29th), non-residential construction spending is likely to deteriorate in the next few months.
- Private residential construction, which had shown recent signs of improvement, fell by 3.5%/m in May. Unlike non-residential construction, however, the bulk of the downturn has already been seen in this sub-sector. And

recent data have yet to reflect the recent surge in housing starts, which increased by 15% between April and June. The lag between starts and construction spending suggests that the increase in activity should feed through into more positive construction spending numbers in June or July. Stabilisation at a slightly higher level, rather than further expansion, is the likely outlook for the rest of 2009.

“Construction spending has shown signs of stabilisation”

“A rise in residential spending is expected in June or July”



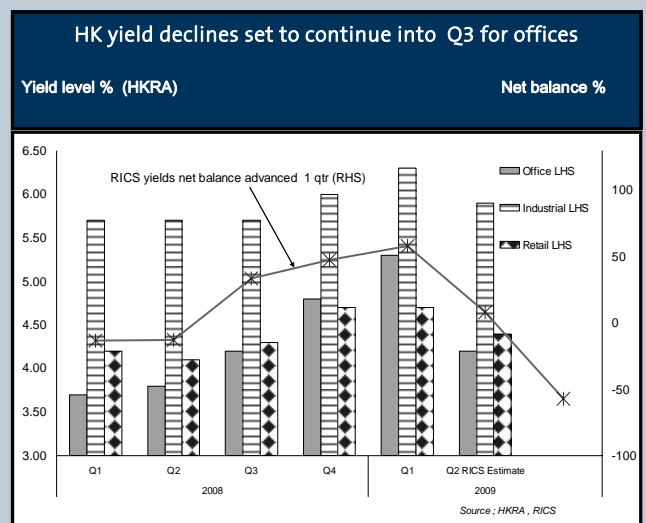
HK property rebounds despite ongoing rental declines

- The latest RICS Global commercial property survey for Q2 2009 revealed some improvements in the emerging Asia property market. At a global level, lettings demand remained in decline across most sectors and regions in Q2 although some markets have bucked the trend. Emerging Asian offices, Australasian industrial and the Latin American office sector have all shown a return to modest growth in demand.
- Improvements in activity in the commercial property market in emerging Asia broadly reflect an upturn in economic activity across the region. Interestingly, Hong Kong saw a notable improvement in the investment market with purchasing activity moving up sharply for offices and retail although less so in the industrial market. This may reflect the injection of a massive monetary stimulus in China since the turn of the year.
- The uptick in investment interest has occurred despite rapid declines in rents which continued into the second quarter. Indeed, the lettings market continued to see marginal declines in activity compared to Q1 although confidence indicators have perked up markedly. Agents expect retail lettings activity to rise in Q3 possibly reflecting the pick up in new retail enquiries reported in Q2. It appears that the low interest rate environment coupled with the

rebound in activity in China has boosted investor sentiment towards the property sector. The latest figures from the Hong Kong Rating Agency (HKRA) show that yields for Grade A offices stood at 4.1% in May down sharply from 5.4% during January. This compares to 4.7% for retail and 5.9% in the industrial market. The latest RICS survey suggests that yield declines will continue into Q3.

“ This week’s RICS Survey revealed a sharp turnaround in Hong Kong ”

“..with yields set to move lower still into Q3”



Australian house prices set to rebound

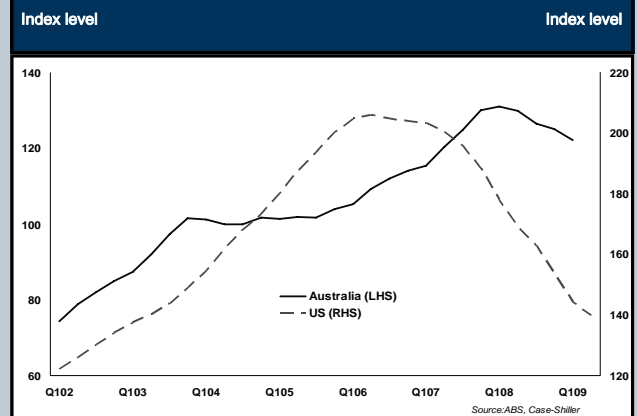
“Residex suggests house prices may have risen by more than 3% in Q2”

“There is increasing concern at the RBA over the risk of another housing bubble”

- Official data on Australian house prices for the second quarter of the year are due for release on Tuesday 4th. The last set of numbers showed that, across the whole country, prices fell by 2.2% in the first three months of the year. The high water mark for the housing market in Australia was the first quarter of 2008. Since then, prices have dropped by a little short of 7% on average. The headline figure masks widely varying regional trends with Darwin and Hobart still relatively firm and Perth very much in the eye of the storm.
- More timely data from Residex, the residential property data gathering company, suggests that the official numbers will show an increase in the second quarter. Residex indicate that prices may have risen by 2.3% for the whole quarter; in June alone, it posted a 3.6% gain. If the official figures come out anywhere near this, it will leave house prices not far away from last year’s peak. This is in marked contrast to the US where, even given the stabilisation seen in this week’s Case-Shiller index, prices are still one-third down on the high.
- The significance of a firm set of numbers will not be lost on the Reserve Bank of Australia (RBA) which meets on the same day as the housing release. Governor Glenn Stevens

only last week warned about the risks of another bubble emerging if housing supply does not respond to higher demand. Some comfort may be drawn from the 9.3% jump in approvals to build new homes in June. Even so, the likelihood is that the RBA will move to begin reversing the 425 basis points of interest rate cuts sooner than previously expected.

House prices remain more resilient in Australia than the US

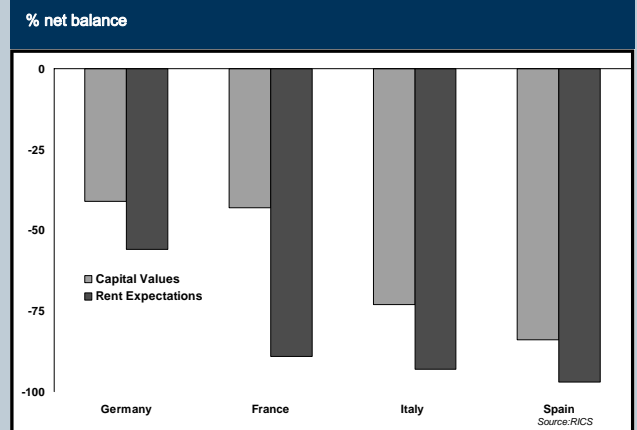


PMIs to signal further improvement in euro area

- The publication of a raft of (final) PMI surveys for July over the coming week will provide further confirmation of the improving tone to the euro area economy. The manufacturing report will be released on Monday 3rd followed by the services report on Wednesday 5th. Provisional figures showed manufacturing sentiment comfortably beating expectations, climbing to its best level for 11 months, while confidence in the service sector also edged upwards. Significantly, although the output indices remain below the 50 level they are approaching the point that would be consistent with a more stable trend in GDP.
- By individual country, the improving picture has been fairly broadly based although in relative terms the turnaround in Germany has been rather more marked than elsewhere on the continent. Significantly, the RICS Global Commercial Property Survey released this week shows Germany ahead of its main partners in the euro area on all the key indicators. While the net balances remain negative on both the outlook for capital values and rent expectations, it is less so in Germany than in France, Italy or Spain. The rise in yields in Q2 has also been rather more modest.
- The ECB will make its monetary policy announcement on Thursday 6th facing increasing evidence of deflation in the headline CPI price measure. Meanwhile, the latest euro

area bank lending survey shows that lenders are on balance continuing to tighten credit standards albeit in a less marked way than was the case earlier in the year. Specifically, the net balance of banks toughening up further on lending conditions for either businesses or housing finance has diminished. Against this backdrop, interest rates are likely to remain on hold at 1% for most if not all

RICS Global Commercial Property Survey



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