

# Property

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## \$14bn gone and there's worse on way

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and Shannon Nicholls

In arguably their toughest reporting season, Australian property companies have written down more than \$14 billion in property values and most observers expect there is worse to come.

The deteriorating outlook is reflected in the continuing sell-down of listed real estate investment trusts, which fell another 6.1 per cent yesterday.

UBS analyst John Freedman expects property values to drop by up to 30 per cent from their 2007 peak as the capital market upheaval churns its way through the system. To date those values have fallen 10 per cent from their peak. In the six months to December 31 they fell 6.8 per cent on average.

"This has been driven by the lack of credit, not by supply and demand fundamentals," Mr Freedman said. "This is not a real estate market crisis — it's a credit market crisis."

"You look around the street and you don't see massive amounts of developments under way with no tenants. This is the big difference from the 1992 crash."

The top 19 property trusts in the S&P/ASX 200 REIT counted for more than \$10.8 billion in devaluations in the past six months, with an average decline of 6.8 per cent. Some analysts believe this is a more realistic result than was expected from this round of valuations.

Goldman Sachs JBWere analyst Simon Wheatley estimates cap rates on average rose 48 basis points over the past six months. "[That] cap rate movement should have represented a 6.8 per cent decline in values and that's pretty much in line," he said.

"The cap rate move is very transparent. It was good to see the hit sooner rather than later because the market knew it was coming. We thought people might have been a bit lighter in this period — around 5 per cent."

Westfield topped the chart with a \$3.3 billion write-down on its US shopping centre portfolio. Centro Retail Group showed a decrease of 6.4 per cent over its portfolio. Its values have fallen 16.2 per cent in the past 18 months.

By value, the best performer was CFS Retail Property Trust which

### Crash course

Performance of S&P/ASX 200 real estate investment trusts Six-months to December 31

	Property write-downs (\$m)	Devaluation (%)	Weighted avg cap rate (%)	Net tangible assets (\$)	Last close (\$)	Total assets (\$m)	Total debt (\$m)	Gearing (Total debt/assets) (%)	Total loss (\$m)
Westfield	3,300	6.0	6.20	12.63	9.92	57,673	19,955	34.6	2,200
GPT	1,400	18.0	6.50	1.43	0.27	13,030	4,391	33.7	3,253
Dexus	773	9.3	7.40	1.33	0.69	9,575	3,457	36.1	954
Centro Retail	760	6.4	7.20	0.72	0.03	4,471	2,709	60.6	2,060
Macquarie Office	717	10.5	7.00	0.63	0.09	5,487	2,694	49.1	1,086
Stockland	700	6.2	7.10	4.86	2.56	13,390	4,151	31.0	366
Macquarie CountryWide	598	10.0	7.40	1.48	0.12	5,647	3,320	58.8	714
Goodman	486	7.0	7.20	1.05	0.19	9,651	3,976	41.2	466
Macquarie DDR	358	8.9	7.20	0.92	0.03	2,811	1,687	60.0	221
ING Industrial	327	5.1	7.30	1.66	0.06	4,678	2,110	45.1	450
Tishman Speyer	315	10.0	6.30	1.88	0.06	2,067	1,162	56.2	223
ING Office	277	6.6	6.80	1.30	0.22	3,619	1,368	37.8	446
Mirvac	236	6.2	7.00	2.44	0.80	7,143	2,264	31.7	646
C'wth Property Office	203	5.8	7.00	1.41	0.93	3,593	1,121	31.2	299
CFS Retail	139	-1.8	6.10	2.14	1.61	7,693	1,977	25.7	226
Babcock & Brown Japan	126	4.7	5.00	1.75	0.20	2,695	1,463	54.3	215
Valad	73	5.0	7.10	0.95	0.03	3,756	1,311	34.9	821
Bunnings Warehouse	44	4.6	7.60	1.88	1.66	968	344	35.5	23
Abacus	17	4.0	7.75	1.24	0.28	1,498	548	36.6	52
<b>TOTAL</b>	<b>10,849</b>								<b>14,720</b>
<b>Average</b>		<b>7.0</b>	<b>6.90</b>					<b>41.8</b>	

SOURCE: AFR, GOLDMAN SACHS JBWERE, UBS

had a devaluation of only 1.8 per cent or \$132 million.

CFS Retail fund manager Michael Gorman expects independent valuers' assessments on capitalisation rates will remain bearish. "We see valuers struggling to find evidence of cap rates given lack of sales evidence," he said. "Given that, though, they might find that cap rates for regional malls soften by another 50 basis points."

Such a decline in values has pushed gearing out to 40.8 per cent (excluding Centro Retail) for the 19 REITs and this is expected to have an impact on the way banks tighten credit. Commonwealth Bank chief credit officer Ross Griffiths said REITs could expect lenders to ask for more detailed information.

"Falls in property valuations will see lenders focus even more closely on cash flow," he said. "Realistic forecasts which recognise that income from tenants may be under stress is expected. Future cash flow is now even more important than valuations."

Mirvac and Valad have seen the

change in banks' attitude. Both have had reductions in the amount of debt refinanced. Mirvac had a \$400 million drop and the cost of its main facility went up. It was also hit when four of its 13 financiers exited the syndicated arrangement. All four were foreign banks.

"If your bank knows your business well it will probably support you," Mr Freedman said. "If you have a syndicate with some foreign banks it might be a bit harder to

### Future cash flow is now even more important than valuations.

renew and if you have CMBS, well, that market is closed."

He believes banks were most concerned with gearing, then interest coverage. They would then move deeper into the amount of debt coming up for renewal in the next 12 to 24 months.

It was not only property valuations that fell.

More than \$3.8 billion in financial instruments such as bets on interest rates were written down. Westfield again led the charge with \$1.3 billion written down because of its presence in the US.

Westfield is the second-largest US shopping-mall owner and as the Australian dollar lost 35 per cent against the US dollar after climbing to its highest level since floating, the group shipped back a \$4.7 billion gain on the currency movement.

Some weren't so lucky on the exchange rate. GPT Group — which closed sharply down at a new low of 27¢ yesterday — lost \$545 million on foreign currency and \$839 million in interest rate hedging.

GPT chief executive Michael O'Brien said the losses were unrealised. "Under AIFRS, the rate volatility flows to the P&L but doesn't affect the underlying cash flow of the business," he said.

"The losses are artificial. We can't actually access the lower interest rates as spreads have widened so much, therefore the rates are probably similar anyway.

"Our hedging policy is designed to provide stability and certainty to cash flow and the operating income of the company.

"Hedges provide interest rate and foreign exchange certainty."

Shares in GPT, which is seeking a new chairman and chief executive, have almost halved since it unveiled a \$3.25 billion loss last Friday.

The sharp sell-down is partly driven by fears the group will not be able to exit its offshore property joint venture with Babcock & Brown, even though loans within the joint venture are non-recourse.

On Tuesday, UBS downgraded its rating to neutral, from buy, and Morgan Stanley has halved the stock's target price to 40¢ from 80¢.

One broker said yesterday that with little equity left in the vehicle, local institutions were looking to "get out while they can".

One fund manager described GPT as "a highly leveraged vehicle, end of story. It's sad."

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