

UK Monthly Index

JULY 2008

UK Property Returns -4.7% in H1 2008

Falling Capital Values Accelerate in June

- Significant weakness in the Central London office occupier market once again caused rental growth to be negative at the All Property level in June. All other segments remain firm.
- All Property rents fell marginally over the second quarter but remain up on the beginning of the year.
- For the second consecutive month, the decline in All Property capital values reaccelerated to -1.3%. Since the start of the year property values are down 7.4% and are 18.5% lower than their peak in June last year.
- UK Commercial Property has returned -13.9% in the last year, only marginally worse than equities on the FTSE All Share at -13.0% but significantly behind gilts with 7.1%.

Output Slows in All Sectors – GDP Growth Very Low

- Q1 GDP growth was revised down to just 0.3% q-o-q.
- According to the June CIPS PMI, both Manufacturing and Services fell below the neutral level in June. Construction activity plummeted to its lowest level in over 10 years.
- Retail sales surprised on the upside with the fastest monthly growth in more than 20 years. Although, profit warnings from major UK retailers and a large drop in mortgage equity withdrawal suggest this may be an aberration.
- UK CPI rose to 3.3% in May with the Bank of England likely to hold the base rate at 5% in July.

MARKET BACKGROUND

Investment into UK Property fell to a 7 year low in the second quarter; with the lack of transaction evidence resulting in a yield shift of just 20bp over the quarter, half the rate of Q1. Compounding the yield impact, rental values actually fell in the second quarter compared to moderate growth in Q1. Nonetheless, All Property capital values fell only 3.0% in Q2 compared to 4.5% in the previous three months.

Over the first half of the year, All Property values fell by 7.4% compared to 11.9% in the final 6 months of 2007. In the last year, All Property rental values have grown by just 2.2% while total returns plummeted to -13.9%.

Although the pressure of forced sales from retail funds may have eased, the debt environment remains challenging for commercial property. Results from the Q2 Bank of England Credit Conditions survey suggest that this will continue through the next few quarters.

INVESTMENT MARKET RETURNS (END JUNE)

| | % Year-on-Year | |
|----------|----------------|----------------|
| | Total Return | Capital Growth |
| Property | -13.9 | -18.5 |
| Equities | -13.0 | -16.1 |
| Gilts | 7.1 | 1.9 |

Source: CB Richard Ellis, EcoWin

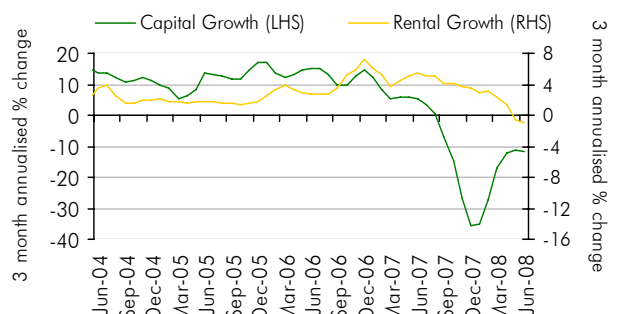
CB RICHARD ELLIS SHORT TERM INDICATORS

| Sectors | Capital % | Rental % |
|------------------------|-----------|----------|
| Offices | -14.0 | -4.5 |
| Central London Offices | -14.8 | -8.2 |
| Standard Shops | -7.0 | 1.3 |
| Retail Warehousing | -12.4 | 0.0 |
| Industrial | -10.6 | 1.4 |
| All Property | -11.6 | -1.0 |

Source: CB Richard Ellis Index June 2008.

The CB Richard Ellis Short Term Indicator is a three-month annualised average of capital and rental growth

ALL PROPERTY SHORT TERM INDICATORS



Source: CB Richard Ellis Index, June 2008

OFFICES

All Offices were once again the worst performing sector in June with falls in both rental and capital values outpacing those of the other sectors. Office rental values have now fallen in three consecutive months and are 0.2% lower than at the beginning of the year. This weakness is entirely driven by the Central London market where rents have fallen 0.7% in the first six months of the year. Outer London/M25 and Rest of UK offices on the other hand, have still seen modest growth of 0.6% and 0.3% respectively in the YTD.

Given the deteriorating occupier outlook for Central London offices, this market suffered the largest negative yield impact in June, resulting in capital values falling by 2.1% over the month – almost twice the rate of May. With falls of 7.3% in the YTD, Central London office values may still be marginally outperforming Outer London and Rest of UK offices, both at c-7.5%, but are catching up quickly.

Offices have returned -4.8% in the first six months of 2008, lower than Retail but stronger than Industrials. On account of their lower income return, Central London office returns are significantly below those in Outer London or the Rest of UK over the first half of the year.

RETAIL

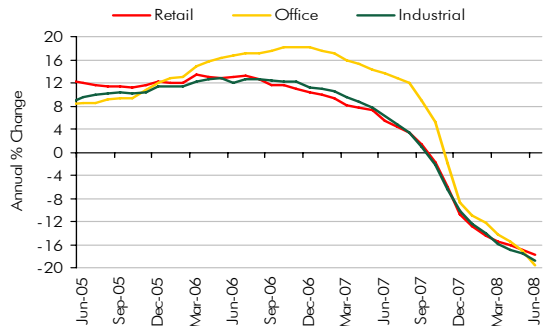
All Retail rental values have risen by 0.6% in the first six months of the year. This figure, however, obscures the underlying differences between subsectors, with 1.1% for Standard Shops and no growth in Retail Warehouses. Retail Warehouse rents have not risen in more than a year, and Shop rents appear to be slowing as Q2 growth was less than half of the previous quarter.

Shops have consistently been the best performing segment this year and have seen values fall by just 6.6% in the YTD, compared to Retail Warehouses which fell 8.2%. Shops actually recorded two months of positive returns in Q2 due to less adverse capital value movements – although June saw a return of -0.7%. Overall, Retail property has returned -4.4% in H1 2008, the strongest of any sector, and Q2 returns were less impacted than offices and industrials.

INDUSTRIAL

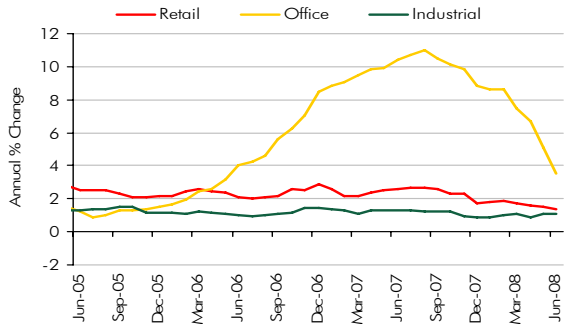
Industrials continue to be strongly affected by current market conditions with only Retail Warehouses performing worse. Rents were muted, growing by just 0.7% in the first six months of the year, although this is still stronger than in H2 2007. Capital values fared much better in Q2 relative to the other sectors, but due to large falls in Q1, are now 8.4% lower than at the beginning of the year. Industrials typically have stronger income returns than other property sectors, offsetting some of the large falls in capital values. Industrials have performed poorly in the first six months of the year with a return of -5.3%, but were stronger than all other segments in Q2 apart from shops.

CAPITAL GROWTH



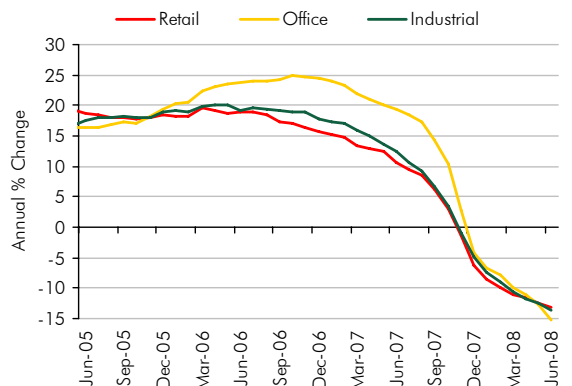
Source: CB Richard Ellis Index, June 2008

RENTAL GROWTH



Source: CB Richard Ellis Index, June 2008

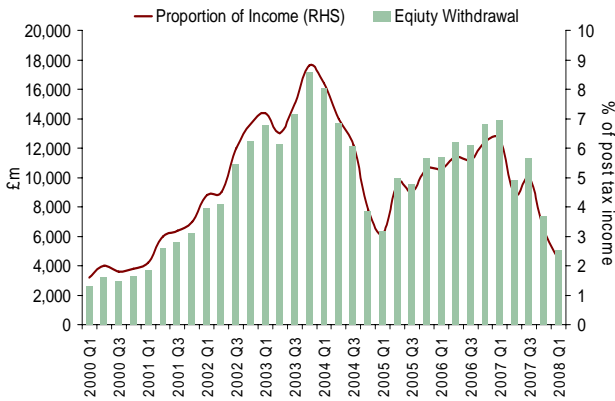
TOTAL RETURN



Source: CB Richard Ellis Index, June 2008

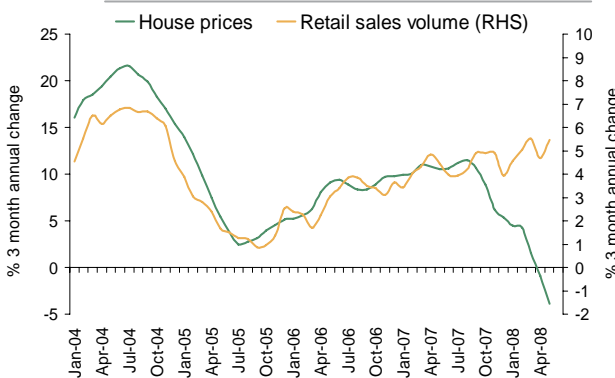
ECONOMICS AND INVESTMENT MARKETS

HOUSING EQUITY WITHDRAWAL



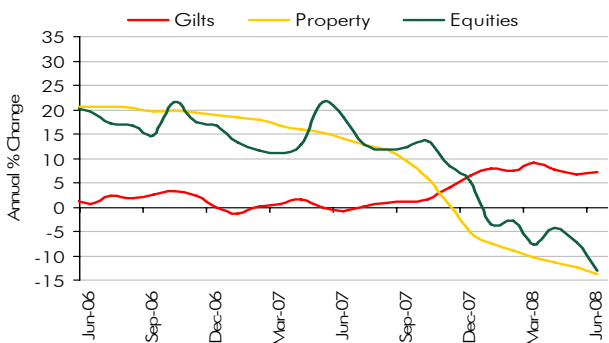
Source: Bank of England

RETAIL SALES AND HOUSE PRICE GROWTH



Source: EcoWin, Halifax

INVESTMENT MARKET RETURNS



Source: Ecwin, CB Richard Ellis

The economic climate continues to deteriorate both in the UK and Globally as central banks are limited in their ability to provide monetary stimulus. UK Q1 GDP growth was revised down to just 0.3% q-o-q, a clear indication of the current slowdown. Survey evidence continues to suggest a stagnant economy with both Services and Manufacturing output falling according to the June CIPS PMI. The same survey showed a severe contraction in the construction sector, unsurprising given the well documented troubles of house builders and commercial developers.

A substantial proportion of UK GDP is dependent on consumers, who have fared surprisingly well in the first half of the year – obstacles, nonetheless, continue to mount against them. Consumer expenditure grew by 1.1% in Q1 2008, consistent with annual growth of more than 3%. This robust growth appears to have continued in Q2, with retail sales soaring by 3.5% in May according to the ONS. However, many retailers, including M&S and John Lewis have issued profit warnings citing dire sales and slow turnover. Other indicators point towards tougher conditions ahead; with mortgage equity withdrawal figures dropping sharply in Q1 to just £5b. This is down from £14b the same quarter in 2007, as the cost of debt rose and house prices fell, removing consumers’ ability to borrow to support consumption.

The price of oil surged past \$145 in early July – a new record – and food costs continue to rise. Combined with rising import costs, and a struggling pound, CPI reached 3.3% in May with further rises anticipated throughout the summer. The Bank of England is widely expected to keep interest rates on hold at 5% in July, but an interest rate rise is not entirely impossible given the Bank’s remit to maintain a target rate of CPI inflation of 2%. This represents a dramatic shift in expectations given the most recent rate cut occurred only in April.

Credit conditions continue to tighten with the Q2 Bank of England survey showing lending intentions for all types are still very weak and LIBOR continuing to hover almost 100bp above the base rate. Mortgage approvals fell once again to a new low of 42k and house prices on the Nationwide are now 3.8% lower annually.

Q2 saw very limited transactional activity in the commercial property investment market; just under £5bn traded hands compared to more than £17bn in Q2 last year.

Property continues to be the worst performing asset year-on-year, but actually outperformed equities on the FTSE All Share in the YTD. So volatile have been the equity markets that they have returned -11.2% in the first six months of the year. Gilts continue to outperform, although they have struggled in recent months with heightened inflation risks.

PROPERTY INVESTMENT YIELDS, JULY 2008

| | Equivalent Yields % July 2008 | Equivalent Yields % July 2008 |
|---------------------------------------|-------------------------------|---|
| Prime Retail | 5.25 | Offices: West End |
| Good Secondary Retail | 6.50 | Offices: City |
| Secondary Retail | 7.25 | Offices: M25/South East |
| Prime Shopping Centres | 5.50 | Offices: Major Provincial |
| Secondary Shopping Centres | 6.85 | Offices: Secondary |
| Retail W/H: Prime – restricted user | 6.50 | Prime: Distribution Unit |
| Retail Parks: Prime – open user | 5.25 | Prime Industrial Estate (Greater London) |
| Retail Parks: Prime – restricted user | 6.25 | Prime Industrial Estate (Ex Greater London) |
| Retail Parks: Secondary | 7.25 | Older Industrial Estate (20 years old) |
| Leisure Centres: Prime | 6.75 | |

Note: Prime yields refer to an equivalent yield for a prime (well specified, well located and rack rented) property let to a financially strong tenant on a lease with a minimum of 15 years unexpired.

CB RICHARD ELLIS MONTHLY INDEX, JUNE 2008

| Sectors | % , 1 Month | | | % , Year-to-date | | | % , 12 Months | | | Index, Dec 1999=100 | | |
|--------------|-------------|------|------|------------------|------|------|---------------|-------|------|---------------------|-------|-------|
| | TR | CG | RG | TR | CG | RG | TR | CG | RG | TR | CG | RG |
| All Offices | -1.1 | -1.6 | -0.3 | -4.8 | -7.4 | -0.2 | -15.2 | -19.5 | 3.5 | 205.4 | 116.7 | 113.6 |
| CL Offices | -1.7 | -2.1 | -0.5 | -5.1 | -7.3 | -0.7 | -14.9 | -18.6 | 5.5 | 208.1 | 122.3 | 117.1 |
| All Retail | -0.5 | -1.0 | 0.1 | -4.4 | -7.1 | 0.6 | -13.2 | -17.7 | 1.4 | 217.1 | 130.8 | 124.0 |
| Shops | -0.7 | -1.1 | 0.2 | -3.9 | -6.6 | 1.1 | -11.4 | -15.9 | 2.7 | 212.8 | 130.6 | 122.5 |
| Retail W/H | -0.5 | -1.0 | 0.0 | -5.5 | -8.2 | 0.0 | -18.2 | -22.4 | -0.2 | 221.1 | 135.8 | 128.1 |
| Industrial | -0.6 | -1.2 | 0.0 | -5.3 | -8.4 | 0.7 | -13.5 | -18.8 | 1.1 | 224.4 | 122.5 | 111.7 |
| All Property | -0.8 | -1.3 | -0.1 | -4.7 | -7.4 | 0.3 | -13.9 | -18.5 | 2.2 | 214.2 | 124.3 | 118.0 |

TR – Total Returns, CG – Capital Growth, RG – Rental Growth

KEY ECONOMIC INDICATORS

| Monthly Data | M-o-M % | Y-o-Y % |
|-----------------------------|---------|---------|
| Retail Sales (May) | 3.4 | 8.1 |
| RPIX (May) | | 4.4 |
| ILO Unemployment Rate (Mar) | -- | 5.3 |
| Manufacturing Output (Apr) | 0.2 | 0.1 |
| Base Rates (June) | -- | 5.00 |

Source: ONS

| Quarterly Data | Q-o-Q % | Y-o-Y % |
|-------------------------------|---------|---------|
| GDP (Q1 2008) | 0.4 | 2.5 |
| Household Spending (Q1 2008) | 1.1 | 3.0 |
| Business Investment (Q1 2008) | -1.4 | 3.7 |

AVERAGE INDEPENDENT FORECASTS FOR UK ECONOMY % change on year earlier, unless otherwise stated

| | 2008 | 2009 |
|-------------------------|------|------|
| GDP | 1.7 | 1.4 |
| Private Consumption % | 1.7 | 1.0 |
| Unemployment Q4, mns | 0.9 | 1.0 |
| Manufacturing output % | 0.6 | 1.2 |
| Employment growth % | 0.5 | 0.0 |
| Inflation % CPI Q4 | 3.2 | 2.2 |
| Official Bank Rate Q4 % | 4.8 | 4.4 |

Source: HM Treasury, Comparison of Independent Forecasts, June 2008

For more information regarding the Monthly Index, please contact:

Michael Keogh
Michael.Keogh@cbre.com

Gary Martin
Gary.Martin@cbre.com

CB Richard Ellis
 St. Martin's Court
 10 Paternoster Row
 London EC4M 7HP
 Tel 020 7182 2000
 Fax 020 7182 2001

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