

Property Derivatives

Market Overview

May 2009



Over the last fortnight, the frailties of the financial sector have taken a back seat as the incredulous expense claims for hanging baskets, mortgages and industrial cleaners have littered our front pages. The economic woes are still ever-present however, and they have left many fearful that the bear market FTSE rally will come crashing back to the levels experienced at the start of March. There is certainly much data to support this, from the inflation figures last week, to continued lay offs across all sectors.

In the property world, alarm bells were ringing after a report published by DeMontfort University discussed a £225bn 'ticking time bomb' in commercial property. £43bn worth of loans from lenders to the commercial property sector are due for repayment in 2009. Nine out of ten organisations reportedly have loans in breach of financial covenants, double the figure on the previous year. Clearly this could have serious implications for total returns

The IPD monthly estimate of total returns came in at -1.81%, which whilst being less of a decline compared to the previous month, brings us to a 9.44% fall so far in 2009. Against these continuing declines, it was therefore surprising to see front end of the derivatives curve move higher. At the end of April, the mid on the Dec 09 was -17%. Towards the end of May, the Dec 09 was trading up at -16%. We put this down to supply and demand. There remains a healthy appetite for one year structured notes which enable a fund to outperform IPD by as much as 18%. In the last couple of days the price has actually drifted back to a -17% mid.

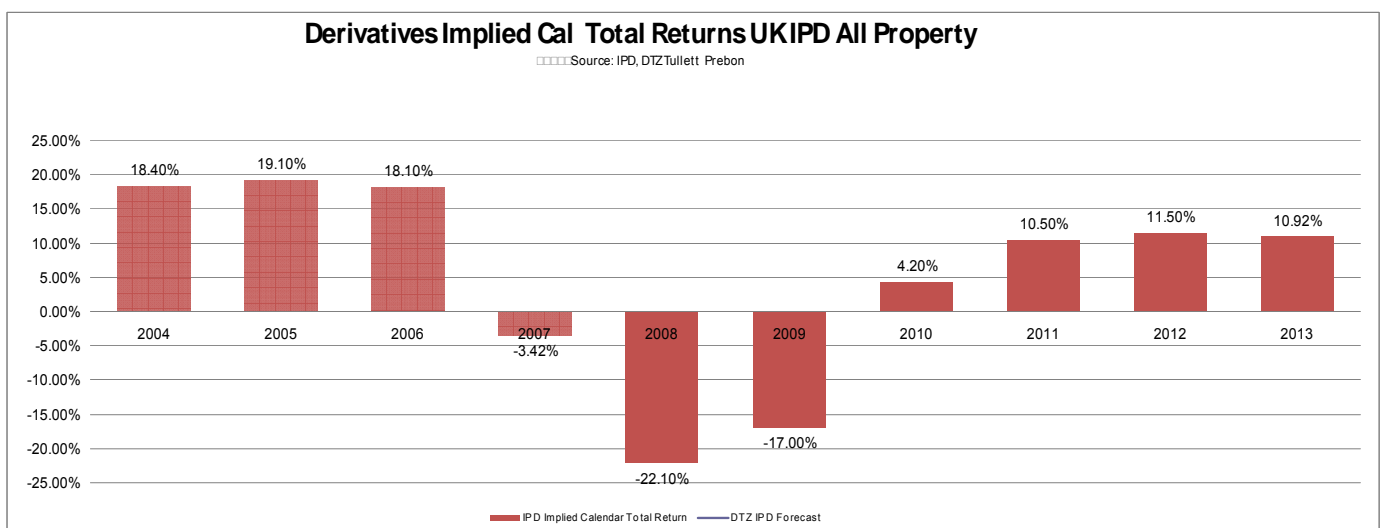
Earlier on in the month there was some buying in the Dec 11, trading as high as -1.0% but this too has subsided leaving the current mid at -0.75%. There has also been continued activity in French All Office IPD in May. Of particular interest was the Dec 09 which has been trading at -20.0%.

The IPD quarterly breakfast at the start of May saw the release of Q1 volumes. Expectations weren't great and a total of £606m traded – an 80% drop off in activity from Q1 2008. However this is very much in line with activity in the physical market. The second quarter has started off in a brighter fashion, and although familiar issues are still apparent, hopes are high for continued growth and greater liquidity as the year rolls on.

UK All Property Indicative Mid Market Prices		
Tenor	Mid Price (pa)	Implied Total Return (pa)
Dec 08 – Dec 09	-17.0%	-16.50%
Dec 08 – Dec 10	-7.00%	4.20%
Dec 08 – Dec 11	-1.50%	10.5%
Dec 08 – Dec 12	1.50%	11.50%
Dec 08 – Dec 13	3.40%	10.92%

Table 1

Tullett Prebon
28.05.09



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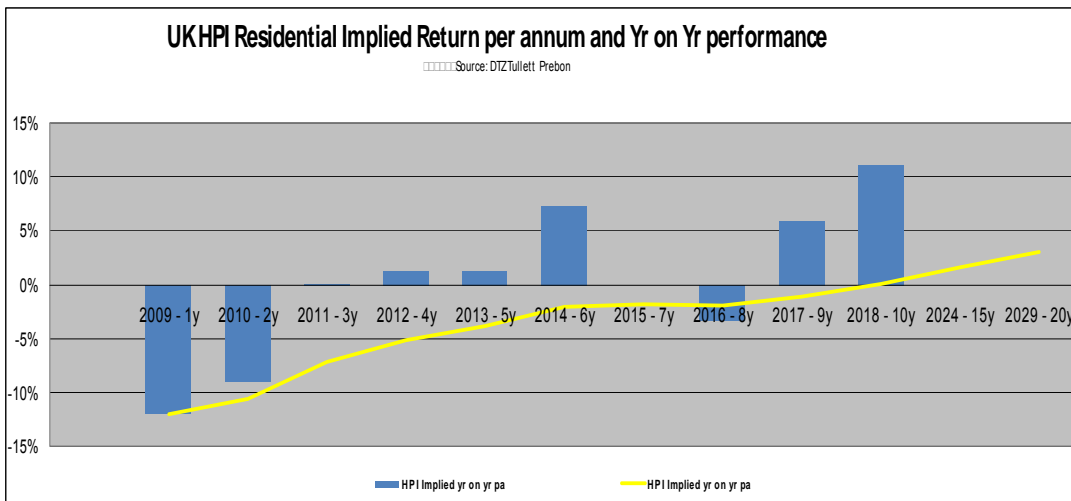
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UK Residential Market

The month of May has, on the whole, seen a step in the right direction for both residential property and the derivatives market alike. Although there were worse than expected CPI and RPI figures, pockets of positive news flow have emanated from the residential world. House prices fell at their slowest rate for over a year in the 3 months to April, whilst new buyer enquiries rose at their fastest pace since 1999, according to RICS. The HHPI non seasonally adjusted figure actually returned a slightly positive number this month of +0.06%. Some may argue that this figure, coupled with the rally in the equity market, should be viewed as evidence that we are nearing the end of the downturn. Others, perhaps more wisely, point to the fact that such a strong number suggests greater falls towards the end of the year. Indeed, the seasonally adjusted figure was actually -1.7%.

The derivatives market has been surprisingly buoyant this month, with trades reported across the curve. There have been strong bids recently which have complemented the bear market FTSE rally. With levels having remained stagnant for a while, that they are drifting higher may mean buyers do not want to miss the boat. On a day of particular frequent activity last week, the 9 year traded at the relatively high level 106. There were also trades in the 6 year at 93, and keen interest in the 2-4 year facets. Consequently, the curve has drifted higher and there are good opportunities for both buyers and sellers. We expect to see continued HPI activity over the coming months.



Tenor Dec08 -	MID Price	Implied pa Return
0y	100	Dec 08 Start
1y	90.0%	-12.0%
2y	85.5%	-9.1%
3y	86.0%	0.0%
4y	87.0%	1.2%
5y	90.0%	1.2%
7y	95.0%	-1.8%
10y	107%	11.1%
15y	122.0%	-
20y	150.0%	-

Table 2 Tullett Prebon 29/04/09

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EUREX

The first trade of significant size was reported this month on Eurex. 100 lots of Cal 10 traded at 102.75. The trade was said to have been a the result of an OTC block trade which had been negotiated off-exchange, and then transacted on screen at this agreed level. All very encouraging.

Indicative pricing available at: **Bloomberg and Reuters – TPPR<GO>**

Historical Publications

For historical newsletter publications, please visit www.tullettprebon.com For further commentary and information, please see our monthly column in Property Week at www.propertyweek.com or contact:

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