April 2010

Latin American Quarterly

Market Perspective

Executive Summary

- An economic recovery is underway in Latin America, although the pace and pattern varies widely among countries. While activity in property markets is gradually increasing, it will not gain full strength until later this year. Transaction volume is expected to pick up in the second quarter.
- Capital markets in Latin America rallied in 1Q10 on positive global economic news and improving investor sentiment. Foreign direct investment in Latin America is expected to increase this year as multinational corporations take advantage of the recovery in the region and expand their local operations.
- Buoyed by the improving landscape in local and global economies, industrial companies in the region are gradually resuming expansion plans. For example, auto production is increasing rapidly in both Mexico and Brazil due to growing demand in local and external markets.
- Latin America's retail sector is being enhanced by the stronger employment market, expanding access to consumer credit and the growing buying power of the middle class. Mexico is seeing signs of stabilization in rents and vacancies in more mature markets, although transaction activity remains slow.
- New housing supply is increasing in Mexico for the first time since the onset of the credit crisis, reflecting greater confidence among local construction companies. Supply is expanding particularly fast in Brazil, where the government has doubled the size of the Minha Casa Minha Vida housing program.

Regional Economies

Full-year GDP figures in Latin America in 2009 were mostly negative as a result of the global recession. Economic activity contracted in Mexico (-6.5%), Venezuela (-3.3%), Chile (-1.5%) and Brazil (-0.2%), while the economies of Peru (0.9%) and Colombia (0.1%) expanded. However, fourth-quarter GDP numbers were much improved from 3Q09, which is widely seen as evidence that a recovery is well underway across the region.

In fact, property professionals in Latin America are more upbeat about the commercial real estate market than their peers from any other region of the world, according to the Royal Institute of Chartered Surveyors' (RICS) 4Q09 Global Commercial Property Survey. Latin American countries topped the survey in terms of expectations for rental rates and capital values in 1Q10.

Prudential Real Estate Investors
8 Campus Drive
Parsippany, NJ 07054
USA

Tel +1 973.683.1745
Fax +1 973.734.1319
Web www.prei.com

The recent faster-than-expected growth of the U.S. economy has played a key role in supporting Mexico's rebound. The growth recovery in Mexico was led by the industrial sector, which expanded 3.6% year-over-year in January, after contracting 7.3% in 2009, according to government institute INEGI. The rebound in industrial activity appears to be spreading to services, which expanded 1% in 4Q09 over the previous quarter. The increase in productivity prompted Mexico's unemployment rate to decline to 5.2% at the end of February on a seasonally-adjusted basis, down from 5.4% in December and 6% in September.

Brazil's GDP grew by 2% in the fourth quarter from 3Q09 and 4.3% from the year-ago quarter, backed by expansions in both industry and services, according to government institute IBGE. Brazil's resilient economic performance in 2009 supported a strong employment climate. During the year, nearly 1 million new jobs were created in Brazil, the most among all G-20 countries, according to the Brazilian Labor Ministry. Brazil's unemployment rate in February stood at 7.4%, down from 8.5% a year ago. The improved employment outlook has been reflected in the growing buying power of Brazil's middle class, leading to robust retail sales. The International Monetary Fund (IMF) estimates Brazil's economy will grow 5.5% this year, the second-highest in Latin America after Peru.

According to the RICS survey, Brazil led the world in the rate of increase in real estate transaction activity in 4Q09, while available space declined at the fastest pace. The number of professionals expecting rents to rise during 1Q10 climbed to its highest level since mid-2008.

Brazil will elect a new president in October. Sao Paulo governor Jose Serra, a centrist candidate, leads early polls, although his margin over current President Lula da Silva's chief of staff Dilma Rousseff has narrowed since last year. Rousseff, a leftist, may be helped by the improving economy and support from da Silva, who maintains a high approval rating. Neither candidate is expected to implement major shifts to economic policy.

Chile's economy is in flux as a result of the 8.8-magnitude earthquake that struck the southern coast of the country on February 27, causing in an estimated US$30 billion of damages. The earthquake temporarily disrupted the job market, although the reconstruction efforts are expected to create 60,000 jobs, according to the Chilean government. President Sebastian Pinera, who was inaugurated on March 11, has announced plans for employment subsidies for private companies, construction training for the unemployed and subsidized home repair or rebuilding for lower-income families.

Chile's GDP was negative in 2009, the first annual decline in 10 years, according to the Chilean Central Bank. However, fourth-quarter GDP was up 5.9% from 3Q09 and 2.1% from 4Q08. In January, the month before the earthquake, Chile's monthly economic activity indicators were positive due to growth in the retail sector and automobile industry. The effects of the earthquake will begin to be reflected in March data.

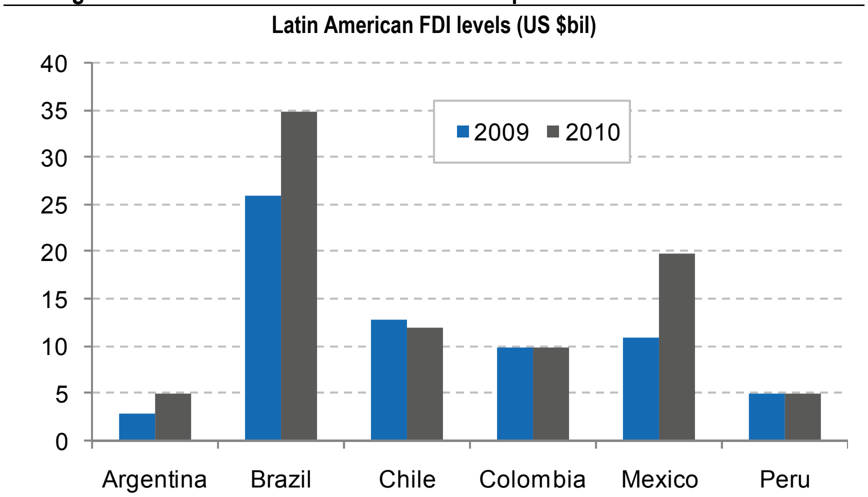
Capital Markets

Public real estate and related companies in Mexico, Brazil and Chile raised US$2.2 billion of equity in the first quarter, out of US$5.2 billion total raised in those countries. Equity market indexes in Latin America in the first quarter rallied behind signs of an economic rebound, and bond index spreads fell 26 bps amid declining risk aversion. Central banks across the region kept rates constant during the first quarter but signaled that they would hike rates to avoid inflation.

Brazil's fiscal and monetary policies remain expansionary despite the strong economy, due in part to the upcoming presidential elections in October. As a result, Brazil's CPI rose 0.78% in February, bringing the one-year inflation rate to 4.83%, or 33 bps above the central bank's target. Bank analysts continue to raise their inflation expectations for this year, and the latest forecast put projected 2010 inflation at 5.2%. The central bank is expected to raise the current 8.75% benchmark interest rate by 50 bps in April and 250 bps for the year. Mexico and Chile are expected to follow Brazil's lead with rate hikes beginning in the third quarter.

Foreign direct investment (FDI) in Latin America is expected to increase this year as multinational corporations take advantage of the recovery in the region and expand their local operations. The IMF forecasts that FDI in the region will increase to US$85 billion this year, up from US$67 billion in 2009, although it will remain below the 2008 level of US$92 billion.

Foreign Direct Investment to Latin American Expected to Rise in 2010



Economist Intelligence Unit (2010 forecast)

The IMF in March approved the Mexican government's request for a one-year renewal of the country's US$48 billion credit line, originally set to expire on April 16, sending the message that it believes that Mexico is in a strong financial position. The Mexican government does not intend to draw on the line. Citigroup announced that the Mexican Government Bond Index is eligible for inclusion in the World Government Bond Index (WGBI). If Mexico continues to meet all WGBI criteria for three consecutive months, it will become the first Latin American government bond market to enter the WGBI. The announcement prompted the Mexican peso to rise to a 17-month high.

Property Markets

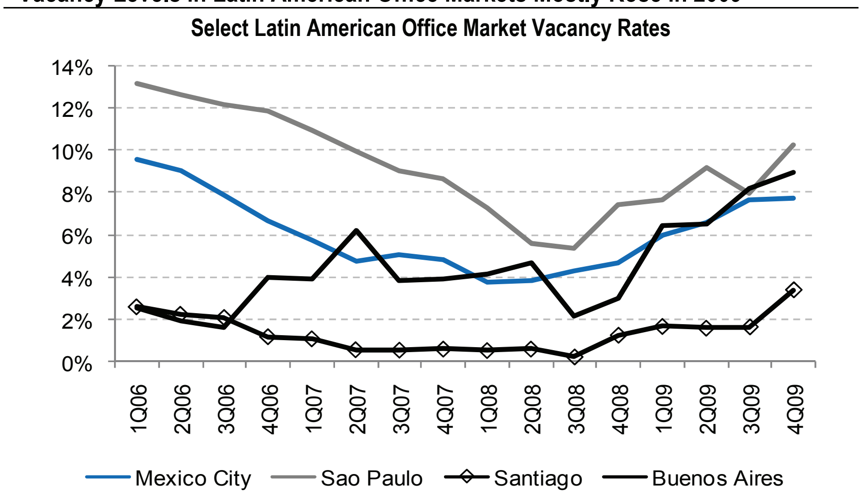
Industrial: Improving global demand, coupled with the rising purchasing power of Latin America's growing middle class, is leading local industrial companies to expand. After nine consecutive positive months, Mexico's main manufacturing expectations index, as measured by the Institute of Finance Executives (IMEF), rose to its highest level since November 2006, indicating that Mexico's industrial sector will continue to grow in the next few months.

Mexico's auto production posted steep increases from year-ago levels in January (102.4%) and February (55.6%), according to Mexican auto industry association AMIA, reflecting the economic recovery and the severity of last year's market decline. Auto exports rose in January (123.6%) and February (96.8%). Mexico's manufacturing employment index fell 3.9% in December, the smallest decline since August 2008, according to INEGI. The recovery trend in the U.S. and Mexico has boosted the confidence of industrial companies, which are starting to think about expanding in Mexico again.

Brazil's industrial production in February increased 1.5% from January and 18.4% from the year-ago month, boosted by strong consumption goods and auto production, according to IBGE. Auto sales rose 27.2% from the year-ago month, according to national automakers association Anfavea. Brazil's industrial confidence index, compiled by the private Getulio Vargas Foundation (FGV), rose to its highest level since November 2007 and the second-highest level since the survey started in 1995. Two-thirds of industrial companies surveyed expect the business climate in Brazil to improve in the next six months, while only 1.6% expects it to worsen. New industrial investments announced during the quarter include: Philips will invest US$116 million to produce televisions in Brazil, Peugeot Citroen (US$708 million) and Ford (US$347 million) will expand auto production facilities and Fiat will hire 1,000 new workers before the end of May. Plus, the government announced in March the second phase of its Growth Acceleration Program, or PAC 2, which includes plans for investments of up to US$800 million in infrastructure and public works projects. March also saw the opening of the south portion of the Rodoanel, a 57-kilometer road that encircles the city of Sao Paulo and is designed to reduce traffic congestion in Brazil's largest city. Brazil is also preparing for its role as host of the 2014 World Cup of soccer and 2016 Summer Olympic Games.

Office: The improving economic climate has led to a more positive outlook for office markets. Increasing demand in some markets has helped vacancy rates to stabilize, although it also may lead to acceleration in the delivery of new space.

Vacancy Levels in Latin American Office Markets Mostly Rose in 2009



CBRE

In Mexico City, the vacancy rate in 4Q09 remained at 7.8%, despite the delivery of 41,000 square meters of new class-A office space, according to CBRE. The average rental rate of class-A space declined to US$23.88/sqm from US$24.91/sqm in 3Q09.

Sao Paulo's office market rebounded strongly during the second half of 2009 due to positive economic data and strong 2010 growth projections. Several stalled projects were restarted, bringing the total new supply in 2009 to 227,000 square meters, according to CBRE. The increase in supply prompted the vacancy rate to rise to 9.2%, up 220 bps from 3Q09, even though net absorption grew 53% in the second half of 2009 compared to the first half of the year. Office rents in Sao Paulo were stable in 2009 at about US$50/sqm.

New supply prompted the vacancy rate of class-A properties in Santiago, Chile, to double to 3.4%, according to CBRE. The vacancy rate is expected to continue to rise this year, due to the steady stream of supply and tepid demand. Construction has resumed on the US$700 million Costanera Center, a mixed-use development which will be the tallest building in South America when it is completed. One of the effects of the earthquake will be increased interest in high-quality buildings with superior construction and design features.

The vacancy rate of class-A office space, in Buenos Aires, Argentina, rose slightly to 9% in 4Q09. According to CBRE, demand for space rose dramatically during the quarter, but vacancy rates might still rise because an even larger amount of new space was delivered.

Retail: A stronger employment climate, expanding access to consumer credit and the growing buying power of the middle class all contributed to the expansion of Latin America's retail sector during the first quarter. Multinational retail companies announced investment in the region, while local retailers remained active players in the capital markets and issued debt and equity to fund expansion plans.

Mexico's consumer confidence index rose in January and February after dropping for a year, according to INEGI. Although the index remains well below 2008 levels, improved confidence has started to reflect in retail sales. Mexico's retail sales broke into positive territory in December for the first time since August 2008, according to INEGI. Meanwhile, same-store sales of members of retail organization ANTAD rose 3.1% in February from the year-ago month, while department store sales increased by 13%. Still, demand for space remains relatively weak. More mature markets are seeing stability in rents and vacancy levels, but it is hard to lure tenants to less developed markets, even with significant tenant perks. The biggest news in the retail sector this quarter came from Wal-Mart, which announced it will open 300 new stores across its various formats, creating about 7,000 permanent jobs in Mexico in 2010. Meanwhile, home-improvement retailer Lowe's opened two stores in Monterrey, its first foray into Mexico.

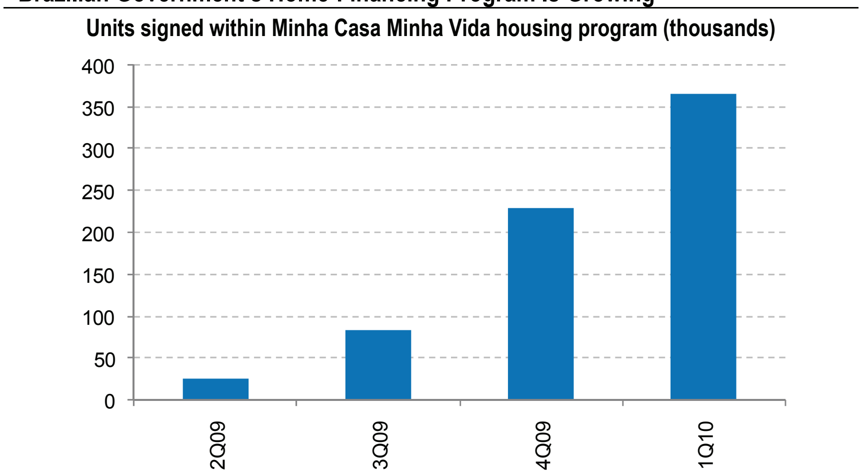
Retail sales in Brazil in January were up 10.4% year-over-year and 2.7% from December, according to IBGE. Brazilian retailer CBD (US$2.8 billion) and French retailer Carrefour (US$1.4 billion) have announced aggressive investment plans for the next two years. Both firms cited Brazil's expanding middle class and expectations for strong economic growth in years ahead. Real estate companies also announced expansion plans. Brazilian homebuilders Gafisa and Rossi signed agreements with Carrefour to construct homes for lower- and middle-income households near Carrefour stores. Brazilian shopping center company Iguatemi recently announced the construction of a US$75 million shopping center in the state of Sao Paulo. Brazilian shopping mall operator Aliansce raised US$315 million in an IPO to build and acquire properties. Large Brazilian retailers Insinuante and Ricardo Eletro merged in March. The resulting company, Maquina de Vendas, is the second-largest non-food retailer in the country and operates more than 500 stores with combined 2009 sales revenue of roughly US$2.9 billion.

Retail sales in Chile grew 0.8% in 2009 and 9.3% in January year-over-year, according to government institute INE. Retail sales are not expected to be too harshly affected by the earthquake, and thus far retailers have been able to meet demand for emergency goods. Many Chilean retailers and real estate companies have recently committed to expanding their presence in Peru. For example, retailer Falabella will invest US$60 million to open 15 new stores in Peru over the next four years, while Chilean shopping mall operator Parque Arauco agreed to pay US$36 million for an 82.5% stake in the Larcomar shopping center in Lima, Peru. The IMF estimates Peru's economy to grow at a 6.3% pace this year, the highest rate in Latin America.

Residential: Homebuilders in Mexico and Brazil posted sales increases in 2009, reflecting the strong demand generated by government housing programs and an expanding middle class. Although the focus remains on low-income housing, in Mexico gains were also seen in the mid- to high-income housing segments due to a recent expansion in credit availability. In both countries, local homebuilders remain active in the equity and debt markets.

Infonavit, the Mexican government's largest mortgage originator, wrote 103,229 mortgages in the first quarter, putting it at 20% of its full-year goal. New housing supply rose 44% year-over-year during the first two months, according to Infonavit, reflecting greater confidence among construction companies and the expansion of credit. Last year Infonavit fell short of its goal in part due to the lack of available construction financing. Infonavit (US$391 million) and Fovissste (US$358 million), the government's second-largest mortgage originator, issued mortgage-backed securities in March. Homebuilders Urbi (US$300 million) and Javer (US$30 million) also issued debt during the quarter.

Brazilian Government's Home-Financing Program Is Growing



CEF, Valor Economico

The Brazilian government in March announced plans to expand its Minha Casa Minha Vida program to finance 2 million homes by 2014, up from its original goal of 1 million. The program aims to spur financing of housing by lowering costs and cutting red tape. The announcement encouraged several Brazilian homebuilders to launch plans for low-income housing units. Homebuilder Gafisa issued US$598 million of equity during the quarter, while MRV floated US$287 million of debt, mainly to finance their growth plans.

Hotel: Buoyed by expectations of rising tourism and the business generated by the upcoming World Cup and Olympics, some large hotel firms launched expansions in Latin America during the first quarter. Paris-based Accor announced plans to invest US$667 million to open 75 new hotels in Latin America by 2012, with the majority concentrated in Brazil. UK-based International Hotel Group plans to invest US$421 million to double its portfolio in Latin America, including 50 new hotels in Brazil over the next 10 years. Hotel occupancy levels in Mexico are starting to pick up after a year of record lows. The number of foreign tourists that travel to Mexico is expected to reach 22.8 million this year, up 6.7% from 2009 and 0.7% from 2008, according to Mexico's Confederation of National Tourism (CNC). This is a positive development for Mexican builders, as the growing number of tourists should increase the potential pool of vacation-home buyers.

Closing Thoughts

During the first quarter, the positive performance of Latin American economies further confirmed that a regional recovery is well underway. Economic growth is on the rise, prompting companies to begin to hire again. Leasing and transaction activity is expected to increase in Latin American property markets, although some sectors and countries are reacting faster than others. The combination of the improved economic environment, increasing availability of debt and positive investor sentiment has just started to translate into higher transaction activity.

The recovering demand has led to the resumption of some stalled commercial real estate projects. In the office sector, that means vacancies may continue to rise as completions add to supply in upcoming quarters. In the retail sector, strong consumer demand has led to the resumption of expansion plans by retailers in Brazil, although in Mexico the environment remains subdued. Low-income housing continues to lead activity in the real estate market, being particularly strong in Mexico and Brazil. We expect development activity, notably housing construction, to gain momentum in Chile in the aftermath of the earthquake. The market for high-end and tourist housing is in full force in Brazil, but in Mexico its progress is dependent on an improvement in credit conditions and confidence among developers.

The Investment Research Department of PREI publishes reports on a range of topics of interest to institutional real estate investors. Individual reports are available by e-mail or via the Web at www.prei.com. Reports may also be purchased in quantity for use in conferences and classes. To receive our reports, change your contact information, or to be removed from our distribution list, please e-mail us at prei.reports@prudential.com, or telephone our New Jersey office at 973.683.1745.

Important Disclosures

These materials represent the views, opinions and recommendations of the author(s) regarding the economic conditions, asset classes, securities, issuers or financial instruments referenced herein. Distribution of this information to any person other than the person to whom it was originally delivered and to such person's advisers is unauthorized, and any reproduction of these materials, in whole or in part, or the divulgence of any of the contents hereof, without prior consent of Prudential Real Estate Investors is prohibited. Certain information contained herein has been obtained from sources that PREI believes to be reliable as of the date presented; however, PREI cannot guarantee the accuracy of such information, assure its completeness, or warrant such information will not be changed. The information contained herein is current as of the date of issuance (or such earlier date as referenced herein) and is subject to change without notice. PREI has no obligation to update any or all of such information; nor do we make any express or implied warranties or representations as to the completeness or accuracy or accept responsibility for errors. These materials are not intended as an offer or solicitation with respect to the purchase or sale of any security or other financial instrument or any investment management services and should not be used as the basis for any investment decision. Past performance may not be indicative of future results. No liability whatsoever is accepted for any loss (whether direct, indirect, or consequential) that may arise from any use of the information contained in or derived from this report. PREI and its affiliates may make investment decisions that are inconsistent with the recommendations or views expressed herein, including for proprietary accounts of PREI or its affiliates.

The opinions and recommendations herein do not take into account individual client circumstances, objectives, or needs and are not intended as recommendations of particular securities, financial instruments or strategies to particular clients or prospects. No determination has been made regarding the suitability of any securities, financial instruments or strategies for particular clients or prospects. For any securities or financial instruments mentioned herein, the recipient(s) of this report must make its own independent decisions.

Conflicts of Interest: Key research team staff may be participating voting members of certain PREI fund and/or product investment committees with respect to decisions made on underlying investments or transactions. In addition, research personnel may receive incentive compensation based upon the overall performance of the organization itself and certain investment funds or products. At the date of issue, PREI and/or affiliates may be buying, selling, or holding significant positions in real estate, including publicly traded real estate securities. PREI affiliates may develop and publish research that is independent of, and different than, the recommendations contained herein. PREI personnel other than the author(s), such as sales, marketing and trading personnel, may provide oral or written market commentary or ideas to PREI's clients or prospects or proprietary investment ideas that differ from the views expressed herein. Additional information regarding actual and potential conflicts of interest is available in Part II of PIM's Form ADV.

PREI is a business unit of Prudential Investment Management, Inc. (PIM), an indirect wholly-owned subsidiary of Prudential Financial, Inc.

Prudential Real Estate Investors
8 Campus Drive
Parsippany, NJ 07054
USA

Tel 973.683.1745
Fax 973.734.1319
Web www.prei.com
E-mail prei.reports@prudential.com

© Copyright 2010