FINAL TRANSCRIPT

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BPO - Q2 2010 Brookfield Properties Corp Earnings Conference Call

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PRESENTATION

Operator

Good morning. My name is Lisa, and I will be your conference operator today. At this time, I would like to welcome everyone to the Brookfield Properties second quarter earnings conference call. All lines have been placed on mute to prevent any background noise. After the speakers' remarks, there will be a question-and-answer session. (Operator Instructions) Thank you. Ms. Coley, you may begin the conference.

Melissa Coley - *Brookfield Properties Corp - VP, IR & Communications*

Good morning, and welcome to Brookfield Properties second quarter 2010 conference call.

Before we begin our presentation, let me caution you that our comments and discussion will include forward-looking statements and information, and there are risks that actual results, performance or achievements could differ materially from anticipated future results, performance or achievements, expressed or implied, by such forward-looking statements and information. Certain material factors and assumptions were applied in drawing the conclusion in making the forecast and projections in the forward-looking statements and information. You may find additional information about such material factors and assumptions, and the material factors that could cause our actual results, performance or achievements to differ materially, set forth in our news release issued this morning. I would like to turn the call over to Ric Clark, President and Chief Executive Officer.

Ric Clark - *Brookfield Properties Corp - President & CEO*

Thanks, Melissa.

To accommodate those of you who wish to dial into the Brookfield Homes call, which is at noon, we are up against a hard stop of 12 o'clock today. So, because of that, and in order to talk about the progress that we've made on our strategic initiatives, we're going to dispense with reports from our division CEOs, Tom, Dennis and Alan, who are all on the call, and they'd be happy to field your questions, if you have any at the end of the call. So, I apologize for this, but I also, in order to get to everyone in the Q&A, we're going to have to limit questions to one with follow-ups for clarity. Please hop back in the queue, and hopefully we'll be able to answer everyone's question within the one hour time frame. So with that, Bryan, why don't we jump right into operating results?

Bryan Davis - *Brookfield Properties Corp - SVP & CFO*

Sure, thanks Ric. Good morning, everyone.

This morning, we reported funds from operations totaling $209 million for the second quarter. This compares to $123 million for the same period in 2009, an $86 million increase, or 70%. On a per share basis, FFO was $0.40 per share compared with $0.32 for the same period in 2009.

The current period results include a $53 million realized return on an investment and debt, which Ric will touch on in his comments. In addition to that gain, this quarter benefited from an increase in residential results of $20 million, and in commercial results of $13 million. Compared to the first quarter of this year, FFO is up $76 million, which in addition to the gain was due to an $18 million increase on our residential result, and a $5 million increase in earnings from our commercial operations.

Before I dig into the results, I did want to point out that we have now included in our supplemental, our proportionate earnings, including supporting schedules. The purpose of this is to present our share of earnings from those assets that we are now required to equity account for, under IFRS. With that as background, our commercial property operations earned FFO of $123 million versus $110 million in 2009, representing a 12% increase. We had an active leasing quarter at rents higher than expiring, and were able to maintain occupancy at a high 94.8%. In addition, we reduced our out year rollover exposure. Contributing to the increase in results with same store growth, contribution from property previously under development, higher recurring fee income, and the stronger Canadian dollar. This was offset by slightly higher interest expense, and increased general and admin expenses due to the transaction costs associated with the formation of our Canadian REIT in our recently announced transaction.

Our net operating income for the--for our continuing operations on a proportionate basis is highlighted on page nine of our supplemental, with $265 million for the quarter, compared to $241 million for the same period in the prior year. This increase is a result of the reclassification of Bankers Court in Calgary and Bay Adelaide Center in Toronto, and 1225 Connecticut in Washington, DC to commercial properties, which accounted for $12 million of the increase. We had termination income of $6 million on a take-back of space in Downtown New York. We had an additional $1 million of recurring fee income, and same-store growth of $11 million, or 5.1%. This was offset by a reduction in net operating income from the sale of our two Washington properties in the fourth quarter. Our same-store growth of 5.1% benefit from the stronger Canadian dollar, which accounted for $7 million. In the quarter, we had an average rate of $1.03 versus $1.17 in the same period last year.

We also benefited from increased rental rates on new and modified leases. We had an increase in same-store occupancy of 80 basis points, and a reduction in our operating costs. Our residential development operations earned $33 million in net operating income, which compares favorably to $13 million earned one year ago. As highlighted in our residential slides, which start on page 31 of the supplemental, this increase was due to strong sales volumes on both lot and home sales.

Now shifting to our balance sheet, total assets on a proportionate basis increased to $19 billion, from $18.5 billion at the end of the prior year. The fair value of our commercial office properties totaled $14.8 billion, or $332 per square foot, resulting in a 6.7% going-in cap rate.

Values during the first 6 months of 2010, increased by an aggregate of $426 million, which we've highlighted on page 18 of our supplemental, and this is primarily a result of the acquisition of a 50% interest in 77 K Street, a reclass of 1225 Connecticut from development properties, and valuation adjustments due mainly to increased cash flows, as a result of current period leasing activity and timing adjustments. Commercial development properties decreased $82 million since the beginning of the year to $540 million or $44 per square foot. This decrease is primarily due to reclassification of 1225 Connecticut, offset by our investment in the first quarter in Bishopsgate, a development site in London.

Our common equity increased from $6.5 billion to $6.7 billion, or $13.37 per share. On a pretax basis, so excluding our deferred tax liability, common equity of $7.2 billion, or $14.36 per share.

Now, before I turn the call back over to Ric, I did want to point out a new slide in our supplemental on page 17, called "Components of net asset value." In this slide, we've attempted to highlight the key components in determining our net asset value; including, a normalized net operating income, the calculation of our implied going-in cap rate, and value per square foot based on IFRS values, a summarized balance sheet for our residential development business, and most importantly, the elimination of minority shares of the earnings and net assets of our Canadian REIT and US subsidiary, which I know you all worked through. Hopefully, you'll find this helpful in migrating your models to the new IFRS world, or if you have already done that, then as a helpful and quick reference point. As always, I'd be happy to walk through anything in more detail after this call.

Now, on that, I will conclude my comments on the financial results and turn the call back over to Ric.

Ric Clark - *Brookfield Properties Corp - President & CEO*

Thank you, Bryan.

As Bryan pointed out, our reporting results were strong for the second quarter and for the first half of the year. And I'd say, overall, and in general, the business environment that we're operating in continued to improve, particularly in our three most important and major markets, New York City, Washington DC, and Toronto--where almost 70% of our commercial net operating income comes from. We've seen meaningful core growth in our residential business year-over-year and quarter-over-quarter, and year-to-date versus prior year results, those are up 153%. We've also shown core commercial property NOI growth after stripping out gains and lease termination payments of 7%, with in-place rents 11% below market rent. We think we're well positioned to continue to gain ground as leases mature.

So, here's what we're seeing and hearing regarding the office sector landscape, broken down by the principal business sectors driving the markets that we're invested in. So, first on the financial services side, Q2, as reported by a number of the financial services and banks and investment houses, versus Q1, was a bit more challenging. Consistent concerns were expressed about the near term pace of global growth, about European sovereign credit risks, and domestically, over the impact of financial regulatory reform, and the continuation of consumer deleveraging, and its impact on spending. Notwithstanding all of this, our experience and observations of these firms when it comes to space utilization, and their activity has been that they are hiring. It is a bit modest, and many of the firms are actively engaged in space discussions, many with us, as we speak. Our vacancies in these markets remain low, and we are seeing activity coming from financial services firms.

On the energy sector side, notwithstanding events in the Gulf, activity continues to be pretty good in actually both of our markets, Houston and Calgary. There has been some shuffling of assets between energy sector firms, which is usually good for us. It creates activity, and as we all know, there's been some overbuilding in Calgary, which mitigates the activity that we've seen there. On the government sector side, Ottawa is just kind of steady. I'd say no growth in government, but no shrinkage, and Washington, DC appears to be expanding and that market's performed very well. So, with all that, it's minor high level background, again, we had a good quarter on the leasing side, completing 1.3 million square feet of leasing, and have had a robust first half with 3.6 million square feet of total leasing transaction completed.

As Bryan mentioned, occupancy remains flat quarter-over-quarter, and is down 20 basis points for the year, but I think more importantly, activity within our portfolio continues to be strong, as we are in the middle of serious discussions with about 4.3 million square feet of tenants. So, we expect to exceed last year's overall leasing of 4.6 million square feet by the end of the third quarter, and may well exceed 2008's overall completed leasing of 6.4 million square feet by year end. Although, it's a little bit early to say this with complete confidence.

I think it's worth a look at the performance of the real estate brokerage firms so far this year, particularly those that are publicly listed and had their calls and earnings releases not long ago. Among other things, they are reporting leasing demand fundamentals having turned positive, and for the first time in ten quarters, they are reporting that the US office markets have posted positive overall net absorption. Now, it's modest, but for the first time in ten quarters it has been positive.

Not being economists, we try not to predict where the market is going, but rather to give commentary on what we're seeing within our portfolio, data points and certainly momentum. And in our observations, New York City, Washington, DC, and Toronto---all these markets are major markets appear to be fully in recovery mode with decent and improving activity, improving economic fundamentals, modest job growth, and no competition on the new supply side, at least at the moment. Under these circumstances, these markets typically experience meaningful rental growth once equilibrium is reached, and we're closing in on that in these markets. The balance of our markets appear to be at the beginning of a, what will likely be, a slow recovery, but we're not really expecting major changes, at least in the near term. I didn't intend to get into further detail on any operating achievements, but as I said, Dennis, Tom, and Alan are all on the call, and would be pleased to take questions at the end.

So, for the rest of the call, I wanted to turn our attention to the progress that we've made toward our principal priorities in strategic initiatives, which we've been working on for several quarters. And, just as a reminder, during 2009, our focus was on preparing the balance sheet to address liquidity concerns and to set the stage for future growth. For 2010, we began the year with $2.1 billion of liquidity, which we wanted to put to work both internally, and externally as well.

Our priorities for 2010 were, just to list them here, were to delever and refinance our US Office Fund debt in advance of October 2011 maturity, to address the 4.6 million square feet of October 2013 lower Manhattan lease maturities, and to begin to put liquidity to work on acquisitions. So, the first one of those, the US Office Fund, as our earnings release mentioned, Brookfield Asset Management, through its lending operations, acquired a $570 million of the mezzanine debt of the US Office Fund at a discounted face value. Through an agreement that we have entered to, the net benefit of this will be received and transferred to Brookfield Properties. As a result, we believe we've prefunded the bulk, if not all, or more, of the equity deleveraging required to refinance this portfolio.

And with lending markets improving--continuing to improve, and more and more lenders entering the market and spreads tightening down to about 200 basis points on a 10- year loan, we're seeing this is a great time to do refinancing. So we're seeing all-in rates being somewhere around, or slightly above 5%. Dennis and Mark, have been actively working to refinance the properties in the US Office Fund on a more conventional basis, and to sell a couple of assets as well. So, we hope, next quarter, but certainly by the end of the year, to be able to report meaningful progress on these initiatives, and more to come in the near term.

We said on prior calls that the priorities in this portfolio--sorry the properties in the US Office Fund portfolio have performed well since acquisition, and have experienced a meaningful NOI uplift over the past four years. Largely, it's not completely offsetting any temporary rise in cap rates. With this, and the effect of the deleveraging that we've just set up, and given the current lending environment, we expect that we'll be able to secure investment grade financing for the portfolio.

So the second priority, the 2013 lower Manhattan lease rollovers, and addressing that, we've talked a lot about this on prior calls, but I don't have a lot though to say here. I'll be a bit brief, but I did have a few things that I did want to point out. And the first is, the progress Downtown on the construction front is advancing rapidly, and there are very visible signs of this, for any of you that have been Downtown. The media has picked up on this, and what may be the best kept secret as to lower Manhattan's future, is gaining media attention, and you might have seen a couple of exposes on this over the last week.

We are in, what we hope to be, the final stages of planning for the redevelopment of the public and retail areas of the World Financial Center, and hope to be in a position later this year to announce and commence this work. Of the 4.5 million square feet of 2013 World Financial Center expirees, here is our current status. We have terms settled, and are in the documentation stage for 630,000 square feet of leases. We have another 200,000 square feet of leasing in what we call advanced discussions, which we hope and expect will go to the documentation stage shortly. We also are in a very active dialogue with 3.2 million square feet of potential tenants, including existing tenants, new tenants, and some new tenants, even potentially coming from Midtown Manhattan. So, to sum it up, we have serious interest and activity on 90% of the space maturing at the World Financial Center in 2013.

So, on the final priority, which is putting our liquidity to work, paving the way for future growth, we have three things to report. As you would have seen in the press release and if you heard from Bryan, we booked a $53 million gain, which is about a 160% annual return on the acquisition of debt secured by a portfolio of assets in Washington, DC. We felt that there was no downside on this investment, and as it turns out, got paid back quickly, at a very substantial profit. During the quarter, we also, through a modest investment, gained 100% ownership of a building that we owned a 50% interest in, in Washington, DC, 77 K Street, for a gross price of $39 million, or $237 per foot. We subsequently completed a $94 million refinancing of this property, and are in advanced discussions to bring the leasing from 52% to 90%, so this should turn out to be a good transaction for us.

And finally, in what we believe will be a profitable move for us, we announced this morning a couple of transactions, which will lead the way for Brookfield Properties' next phase. We announced a plan to transform Brookfield Properties into a global pure-play office company, which includes acquiring a high quality portfolio of 16 premiere assets, in Australia from Brookfield Asset Management. It also--we also plan on the divestment of our residential land and housing business, a name change of the company to Brookfield Office Properties. And, just summing it up, these transactions collectively will position Brookfield Properties as the only publicly listed Class A office company that has a presence in four of the world's most important developed countries, and a scalable asset management model to service global tenants.

So, getting into a little bit more detail on these, and starting with the residential divestment, in 2003, we spun off Brookfield Homes to create a pure-play, North American focused premiere office company. At the time, we did retain what was a modest investment in a largely western Canadian based residential land and housing business, which was contributing about $15 million to $20 million a year to our FFO. Through, I think, the hard work of a very skilled management team, additional investment and the economic growth in western Canada, this division grew to again become a very substantial contributor to Brookfield Properties' FFO.

Believing now, like we did in 2003, that this business, the office business, will both be more valuable if operating separately, and to complete the transformation of Brookfield Properties into a global pure play-office company, we have begun initial discussion to the divest of our residential land and housing operations. To this end, we expect to commence initial discussions with Brookfield Homes, the division that we spun off in 2003, to recombine the businesses through a merger. Should a merger proceed, we envision Brookfield Properties' equity interest would be monetized into a listed security in the merged entity, which Brookfield Properties would dispose of through an offering to shareholders. We would also envision obtaining a commitment from Brookfield Asset Management to acquire any shares of the merged entity, that weren't otherwise subscribed for in the offering. This would give each shareholder an opportunity to participate if they like, and for Brookfield Properties to receive full proceeds to reinvest into the global office business.

So, the final part of this repositioning is the acquisition of the Australian office assets from Brookfield Asset Management. And as I said, we have entered into a transaction with Brookfield Asset Management whereby Brookfield Properties will acquire BAM's interest in 16 premiere Australian office properties, comprising eight million square feet, in Sydney, Melbourne and Perth, and these properties are 99% leased, and have a current NOI of AUD206 million, which is about $185 million. The properties have a total growth value of AUD3.8 billion, which is about $3.4 billion and BPO will pay to Brookfield Asset Management AUD1.6 billion, or $1.4 billion.

Now, the funding of this transaction will come from available liquidity and from a $750 million subordinate bridge acquisition facility, which will be provided by Brookfield Asset Management, which will be repaid from by the completion of some or all of the following. Asset sales, including a sell-down of Brookfield Properties equity interest in our publicly listed Canadian office company, Brookfield Office Properties Canada, or other financing or capital activities. This transaction is expected to be completed in third quarter of this year following of the receipt of third party consents and approvals.

Now, I'd say that BAM has been a great corporate sponsor for Brookfield Properties and both Brookfield Properties and Brookfield Asset Management, and each company's Board of Directors recognizes that related parties dealings can be beneficial for all shareholders. However, careful consideration and transparency are obviously required. Accordingly, Brookfield Properties' Board of Directors established an independent committee to assess this transaction. The committee retained Morgan Stanley to help, and to advise it. The independent committee unanimously recommended that the Board of Directors approve this proposed transaction.

So, our investment thesis on this transaction, I'd first make a few points on the Australian economic landscape. The first thing I'd say is that the global financial crisis has been less severe in Australia, and from a technical standpoint, its economy avoided recession. As the world economies begin to emerge from the global economic downturn, I think the Australian economy is in a stronger position than any other advanced economy. Driving the economy is a rich commodity and resource base, and given proximity, a strong trading relationship with Asia. Asia is expected to experience the highest rates of growth over the next several decades, and according to the IMF, within five years, Asia's economy will be about 50% larger than it is today, accounting for more than one-third of global output.

I'd also add that Australia's government entities are amongst the strongest in the developed world with very limited deficits, and the expectations of reaching budget surplus over the course of the next couple of years. Australia also has a strong and growing pipeline, and investment projects will boost investment over the coming years. Now, all of the above should lead to a vibrant growing economy with strong job growth.

I think the last point that I'd make on the investment landscape in Australia, particularly versus Canada, is that the Canadian dollar has meaningfully out performed the Australian dollar in recent months posing an opportune time to decrease exposure to Canadian assets and increase exposure to Australian assets. Now, adding to our investment thesis, I'd say that Brookfield Properties' strategy of owning high quality assets in the world's most dynamic markets can be effectively deployed in select developed economies around the world. Tenant synergies can be leveraged in other gateway cities, such as Sydney, Melbourne, and Perth in Australia. And, we think that investment in these cities will produce more stable return and growing returns than new North American markets for us. Entering new markets and taking on new people in platforms are risky, which is why to minimize this risk, in advance of making this decision, Tom Farley and several others from BPO have been actively involved with Australia's management team for this portfolio, and have been assessing the assets and the team for about a year.

Now, this transaction adds a large complementary property portfolio of high quality assets. It expands our geographic footprint to attractive new markets. It assembles a similar portfolio, well, sorry. I'd make that point that assembling a similar portfolio platform over time would be much more costly and difficult, if not impossible to replicate. It's in our view, an opportune time in the real estate cycle, to acquire an interest in core assets in Australia, and I'd point out that in 2007, a similar acquisition traded at a 5.2% cap, and which is about 26% higher than the price being paid on this transaction. And lastly, what Brookfield Properties intends to do is to use this Australian management team and platform for future growth, and we think that combining the strong operating base and team, there will be ways to expand both into existing markets where these assets are in Australia and possibly into new markets over time. So, I think those are the comments that I wanted to make about this transaction. And at this point, operator, we would be happy to open up the line to questions.

QUESTIONS AND ANSWERS

Melissa Coley - *Brookfield Properties Corp - VP, IR & Communications*

Operator?

Operator

(Operator Instructions) Your first question comes from the line of Ross Nussbaum.

Ross Nussbaum - *UBS - Analyst*

Hello? Can you hear me?

Ric Clark - *Brookfield Properties Corp - President & CEO*

Yes.

Ross Nussbaum - *UBS - Analyst*

Okay. Can you help me get maybe an understanding of, did the independent directors of Brookfield Properties look at the Australian transaction on its own merits, or was there some consideration given to the back stop that's being provided on the housing transaction as well as the transfer of benefits on the US Office Fund mez purchase? I'm struggling with getting to the bottom of what factors they considered the deal to be fair.

Ric Clark - *Brookfield Properties Corp - President & CEO*

This transaction was independent of any other transaction. So, the Australian transaction was reviewed by itself and on its merits.

Ross Nussbaum - *UBS - Analyst*

And why didn't you roll in the UK assets or Brazil assets, or even the assets in say Brisbane or New Zealand that BAM owns? Why Australia?

Ric Clark - *Brookfield Properties Corp - President & CEO*

The thoughts are Sydney, Perth, and Melbourne are markets that are similar to the markets that we'd experienced the most, the best results in North America, and are consistent with strategy of owning high quality assets in markets whose economies are primarily different by tenants in financial services, energy, resource, or government sectors. And, those are the three markets that fit that bill. The assets that were left out, these were -- they were either markets we didn't think were consistent with that strategy, or assets that had other issues that needed to be dealt with. So, those weren't kept within the portfolio. Sorry, Ross. Did I miss part of that question?

Ross Nussbaum - *UBS - Analyst*

Yes, I think the other question was relating to the UK and Brazil. Why Australia? If you're going to become a global office REIT, and you're trying to become a little more focused here, why not just do the whole kit and caboodle, and roll in UK and Brazil, and separate Brookfield from them?

Ric Clark - *Brookfield Properties Corp - President & CEO*

So, in Brazil, BAM doesn't own any office assets, so there was nothing there to consider. And in the UK, it's just not something that was considered at this time. I think that BAM's ownership in the UK is a little bit different than what we have in Australia, which is portfolio of assets, which are actively managed by the management team down there. So, it's not to say there won't be an opportunity to do something in the UK at a later date, but for now, I think this transaction is what made sense for us.

Operator

Your next question comes from the line of Sloan Bohlen with Goldman Sachs.

Sloan Bohlen - *Goldman Sachs - Analyst*

Good afternoon. Jay's on as well. Questions on the Australian portfolio.

Ric Clark - *Brookfield Properties Corp - President & CEO*

Operator?

Operator

I'm sorry.

Ric Clark - *Brookfield Properties Corp - President & CEO*

We seem to be having a little trouble with the line here.

Operator

There's no response from that line. Your next question come from the line of Steve Sakwa with ISI.

Steve Sakwa - *ISI Group - Analyst*

Good morning. Just wanted to, I guess follow up on the Australia. Ric, I'm just trying to understand. One, you're buying this at a 6.7%. The debt comes at 7.4%. There's this negative arbitrage in this market. So, can you help us understand the pricing on this deal? And then secondly, help us understand the global synergies you get from operating in multiple markets. We know Sam Zell tried to build a national office footprint here and ultimately came to the conclusion that bigger wasn't better, and it didn't make it more profitable. So, what do you see on the global front that gives you confidence that you're going to make a global footprint more profitable?

Ric Clark - *Brookfield Properties Corp - President & CEO*

Let's start with the last part of your question, which is comparison to Equity Office, and I'd say the strategies between Brookfield Properties and Equity Office are very meaningfully different. Sam intended to be all things to all people, all throughout North America. So, he had large assets in every, every major city within North America.

Brookfield Properties is a very focused company. We only invest in cities we consider gateway cities, whose economies are dynamic and vibrant, resilient, and are driven by tenants, principally in three market sectors. And his focus, I think he even made that point that he can buy toilet paper cheaper. We're not -- we don't see expense synergies. We actually see revenue synergies. The people that, for major businesses that are involved in real estate decision making, we find are located in one of our major cities, they're located in New York, they're located in Houston, they're located in Toronto, they're located in Calgary, they're located in London, they're located in Sydney, Melbourne, or Perth. And it's typically one person who is in charge of those things, and in our experience, including recently, with the announcement of the 100 Bishopsgate development opportunity in London, we're seeing that we know the people that are making the decisions. So any US bank, for example, the person making the decision is probably located in New York City, and we have a strong relationship with them. So, absolutely on the revenue side, there will be synergies in this strategy.

Steve Sakwa - *ISI Group - Analyst*

And the first part of the question?

Ric Clark - *Brookfield Properties Corp - President & CEO*

Sorry, would you repeat it?

Steve Sakwa - *ISI Group - Analyst*

I'm trying to understand in most markets, in this case, the leverage is upside down in terms of there being negative arbitrage. Normally, you'd want to buy at a higher cap rate, and finance it with cheaper debt. Australia seems to be the reverse. You're buying it at 6.7% cap, you've got higher cost debt, and that market tends to have high cost debt. So, you are sort of upside down, day one, in terms of that situation. There's not a lot of space rolling. So, I'm trying to understand the economics behind this deal, and how you got comfort with a 6.7% yield.

Ric Clark - *Brookfield Properties Corp - President & CEO*

So, the negative arbitrage is actually one of the disadvantages from investing in the Australian market, and there's no question about that, but in our view and in our analysis, that is offset by the upside potential in the market. And I think it's a combination of things. One, is this is a very strong well-positioned economy, which is going to experience very above average growth over the next couple of decades, in our view, given its proximity in trading relationship with Asia, and the growth that Asia's likely to go through. So, and also, it's a market that is well in balance from a supply and demand standpoint, and we think there's huge potential for spiking of rental rates in the near term. And finally, under the leadership and management of Brookfield Properties, by exporting our systems, asset management techniques, and ideas and relationships, there's very meaningful upside to be experienced versus the going-in cap rate. So, I think there's lots of reasons why this is going to be a very valuable, accretive acquisition for us, and will offset the negative arbitrage.

Operator

Your next question comes the line of Sloan Bohlen with Goldman Sachs.

Sloan Bohlen - *Goldman Sachs - Analyst*

Alright, I'll try this again. Basically, just a question, along the same lines as Steve's. Just wondering if you could maybe put some numbers around how you make up for that gap in the negative arbitrage, what you underwrite for rent growth going forward. There isn't a lot of roll in the portfolio over the next basically four years. Maybe walk us through that, and then I've got a question on the sources of liquidity from the deal.

Ric Clark - *Brookfield Properties Corp - President & CEO*

Sloan, can I just ask you a question? We seem to losing people abruptly on the call. Are people hearing the full comments well?

Sloan Bohlen - *Goldman Sachs - Analyst*

We can hear you on our end, or at least I can.

Ric Clark - *Brookfield Properties Corp - President & CEO*

Alright. So, as far as the underwriting and rental growth, I don't have the assumptions with me, but I'd say we were somewhat modest in our rental growth projections. They would have been higher than what we expect in North America over the next couple of years, but not--we did not underwrite large rental rate spikes. I can't tell you exactly on this call what they were, but they probably averaged 3% or 3.5%, or 4%, and not much more than that over a 10- year period. Let's see, sorry. Sloan, what else?

Sloan Bohlen - *Goldman Sachs - Analyst*

Yes, the second question, just on how far along on the sales of the residential division, and your stake in the Canadian listed entity, when can we see that -- I guess that's timed for the third quarter, but how far along in the process are you there?

Ric Clark - *Brookfield Properties Corp - President & CEO*

We're not far along at all on that. That was merely an announcement of our intentions to engage with Brookfield Homes on a transaction. So, it's something that we hope can be completed by year end, or certainly by the beginning the next year, but we're only at the very initial stages of working through that.

Sloan Bohlen - *Goldman Sachs - Analyst*

And I guess the sources of liquidity in the meantime, that's the reason for the total return swap? If you could touch on that a little bit.

Ric Clark - *Brookfield Properties Corp - President & CEO*

The main reason for that was to preserve in-place financing.

Sloan Bohlen - *Goldman Sachs - Analyst*

Okay. Okay. I'll probably follow up offline.

Bryan Davis - *Brookfield Properties Corp - SVP & CFO*

If I could make one comment on sort of the cash, and I think you were getting that at our liquidity position, we do have $1.3 billion. As we sit on our balance sheet, $500 million of that is pure liquidity, $150 million of cash, $280 million of our deposit, and then we also have capacity within our lines, within our Carma division. So, we do still sit, even with our investment in repurchasing through BAM on the US Fund debt, with a fair amount of liquidity that will be allocated to completing and closing out this transaction in the third quarter.

Sloan Bohlen - *Goldman Sachs - Analyst*

Okay. Thank you, Bryan. I'll probable follow up with you.

Operator

Your next question comes from the line of Michael Bilerman with Citi.

Michael Bilerman - *Citigroup - Analyst*

Hi, good morning. Ric, I'm just, a two parter, (technical difficulty)

Ric Clark - *Brookfield Properties Corp - President & CEO*

Michael?

Operator

I'm not sure what happened.

Ric Clark - *Brookfield Properties Corp - President & CEO*

Operator, could you check the status of this line?

Operator

Yes sir, one moment.

Ric Clark - *Brookfield Properties Corp - President & CEO*

Michael? Operator, maybe we should go to the next question. I'm not sure if he got disconnected.

Operator

Okay. Your next question comes from the line of Mario Saric with Scotia Capital. Mario, your line is open.

Mario Saric - *Scotia Capital - Analyst*

Hi, good morning. Just with respect to the Australian acquisition, Ric, perhaps you can talk about the fixed rent review process, and how that works.

Ric Clark - *Brookfield Properties Corp - President & CEO*

Basically, let's see. Tom, are you on the call? Maybe you want to talk about that.

Tom Farley - *Brookfield Properties Corp - CEO - Canadian Commercial Operations*

Yes. Actually, one of the fundamental differences between leases in Australia and what we typically see in North America is that in this portfolio, as an example, 85% of these leases have an automatic escalator once per year, and the average of that increase is 4%. So, to jump in and to just clarify, gross rate of functions, we do have an automatic increase on 85% of the income of 4% per year, and then certain leases, depends on what's been negotiated, would have a market review mechanism at some point through the lease term, and of course, it does vary from lease to lease. However, the automatic escalator and the automatic growth feature is unique to Australia, compared to our North American markets.

Mario Saric - *Scotia Capital - Analyst*

Okay. And then Ric, perhaps just on the acquisition front, when you initially raised $1 billion of capital last August, you became an opportunistic buyer of real estate. These yields are following below initially set target thresholds. So, can you just walk us through how that reconciles to the overall acquisition environment as it stands today? And are you seeing less opportunities elsewhere, or is there going to be more of a focus going forward on core assets?

Ric Clark - *Brookfield Properties Corp - President & CEO*

Couple things, one is, as you know, there hasn't been a lot of transactions in North America at all in the office sector so far. We do still think there will be opportunities. Monetary policy has been such that funders have incentivized to basically delay dealing with the inevitable. So, there will be some opportunities at some points over the course of the next couple of years. How many, remains to be seen. As far as this transaction goes, the initial returns are more core-like, but our intention is, at some point, to bring in partners like we do in North America, either at the asset level or in a wholesale fund or to do some kind of an IPO with the assets at a subsequent date. And we think at that time, it will greatly enhance our returns, and we don't view this to be simply a core investment for us.

Mario Saric - *Scotia Capital - Analyst*

Okay. Thank you.

Ric Clark - *Brookfield Properties Corp - President & CEO*

You're welcome.

Operator

Your next question comes from the line of Michael Bilerman with Citi.

Michael Bilerman - *Citigroup - Analyst*

Alright, well, we'll try this again. Can you hear me?

Ric Clark - *Brookfield Properties Corp - President & CEO*

Yes, we can hear you Michael, sorry.

Michael Bilerman - *Citigroup - Analyst*

Ric, I'm just trying to determine your role in all of this, and when we buy public companies, we expect to see a CEO who's driving strategy, making decisions as to what are the appropriate investments. You, because you're sitting as CEO of Properties, you're the head of BAM's real state. You sit on the Board of Brookfield Multiplex, which actually holds these assets. And at some point, you can't recuse yourself from everything, and then if you do recuse yourself from each part of the transaction, then there's really no one that we as minority shareholders in Brookfield Properties know that we're getting a great deal. So, I'm trying to figure out how, at the end of the day, that you can say this is a win/win effectively for everyone, because on any side of the deal, you've got to be feeling that, especially as you being an opportunistic investor, you want a good deal for your shareholder

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Ric Clark - *Brookfield Properties Corp - President & CEO*

First of all, I think it was a fantastic deal for Brookfield Properties, and yes, I was the major advocate for this international strategy and for acquiring this portfolio of assets. I just would say, although, with the significant investment in Brookfield Asset Management and my dual role as head of Global Real Estate for Brookfield Asset Management. There's certainly, the potential for conflicts, or at the very least appearance of conflict. But, Brookfield Asset Management has been a fantastic corporate sponsor of Brookfield Properties if you just look back in history. And I would remind you of the Trizec transaction where, over the course--which was done over the course of a four-day period, and a dozen acquisition and restructuring professionals were loaned to Brookfield Properties to complete the transaction in addition to $1 billion bridge loan.

So, just the history and experience has been that Brookfield Asset Management has been a very supportive shareholder to Brookfield Properties, and it's benefited all the shareholders. And I think this is a great transaction. But, just to make sure that there was no conflict or self-dealing, or anything like that, an independent committee was formed. There was no BAM related directors involved in that at all. They had expert advice from an outside advisor, Morgan Stanley. The committee met directly with Tom Farley, who has no direct involvement with Brookfield Asset Management, and who had been the man on point down in Australia over the course of last 12 months, assessing management and assessing the assets, so we didn't make any mistakes. And, he reported directly to the committee without my involvement. So, that's probably the best I can do in response to your question.

Michael Bilerman - *Citigroup - Analyst*

Let me ask it a different way. Brookfield Asset Management obviously has interest in Properties, has interest in these assets in Australia, and everywhere. So, at some points, the benefits -- the revenue synergies that you're talking about, could have been garnered without Properties having to go in at a very, very low FFO yield, which you're selling residential likely will result in a lots of dilution, but let's put that aside. The revenue synergies should have been there because all these assets, somehow or not, are already underneath the Brookfield Asset Management empire, where you could be sharing that knowledge and those tenants and things like that.

Ric Clark - *Brookfield Properties Corp - President & CEO*

I think Brookfield Properties' shareholders are going to benefit greatly from this investment. There are great synergies between tenants from place to place, and I think a pure-play global office company, this is a unique investment vehicle. It should attract attention from international investors, anybody wanting to in invest in high quality premiere office properties, in the world's most important developed cities, this will be a very attractive investment vehicle for them.

Michael Bilerman - *Citigroup - Analyst*

Okay. Thank you.

Ric Clark - *Brookfield Properties Corp - President & CEO*

You're welcome.

Operator

Your next question comes from the line of Karine MacIndoe, BMO Capital Markets.

Karine MacIndoe - *BMO Capital Markets - Analyst*

Hi. Thank you. Just wanted to flesh out some of your comments about the Australian market In terms of above average growth, proximity to Asia, I would imagine the buying of commodities, natural resources from Australia. And how that compares, contrasts to your views of the Canadian market, given that we still have meaningfully positive spreads in Canada versus the negative spread investment being made here, and how you can shed light on pulling capital out of Canada, selling down your ownership in BOX and redeploying some capital into the Australian market?

Ric Clark - *Brookfield Properties Corp - President & CEO*

On the case of the Canadian market, as you know, a lot of the high quality assets have transferred into the hands of institutional owners, and there's been very little transactional activity. There's just not the ability to acquire many more assets. At the same time, there's some development going on in western Canada. There will be more development going on in Toronto. And, to us, the prospects for growth over the next 20 years aren't as compelling as they are with Australia. And given the trading relationship with Asia, all the money being spent on infrastructure, we think this market is poised for very meaningful growth over the next couple of decades. So, not to say Canada won't be a good market, but there's been little transactional activity, and very little ability for us to make accretive acquisitions there. At the same time, I made the comment on the ramp up in the Canadian dollar versus the Australian dollar. I think, given that, it's also good time to redeploy capital there,

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Karine MacIndoe - *BMO Capital Markets - Analyst*

Okay, and what do you see that 6.7% implied cap rate for this portfolio being in five years? And is the 7.4% on debt, is that a mark to market rate on this? Is that what you can get on debt at this stage? In that market?

Ric Clark - *Brookfield Properties Corp - President & CEO*

Debt's probably a little bit more expensive than that in this market at this time. And Bryan, I don't know if you have any comment?

Bryan Davis - *Brookfield Properties Corp - SVP & CFO*

Yes, I'd say the debt is fairly close to that rate in this market. It is somewhat of a shorter term, floating rate debt market. Although, on the 7.5%, we fixed 76% of that. But, the rates may be a slightly more expensive, but there in and around that ballpark range.

Karine MacIndoe - *BMO Capital Markets - Analyst*

And what's the weighted average term on this?

Bryan Davis - *Brookfield Properties Corp - SVP & CFO*

I think it's two and a half years.

Karine MacIndoe - *BMO Capital Markets - Analyst*

Okay. So, you've got that exposure coming up. What do you envision the 6.7% being in year three to five?

Bryan Davis - *Brookfield Properties Corp - SVP & CFO*

4% growth annually, at minimum, on 85% of the portfolio.

Karine MacIndoe - *BMO Capital Markets - Analyst*

And occupancy, you're expecting to be maintain the 99%?

Bryan Davis - *Brookfield Properties Corp - SVP & CFO*

Maybe 100%.

Ric Clark - *Brookfield Properties Corp - President & CEO*

We expect it to be high. There are some lease rolls, but the average we apply to is about 8 years, so it's not a lot of churn in the near term.

Karine MacIndoe - *BMO Capital Markets - Analyst*

Okay, thank you.

Operator

Your next question comes from the line of John Guinee with Stifel.

John Guinee - *Stifel Nicolaus - Analyst*

Ric, not to beat a dead horse, but is 6.7% the right number? I thought I heard you say $3.4 billion acquisition against $185 million of NOI.

Bryan Davis - *Brookfield Properties Corp - SVP & CFO*

Ric, I can comment on that. There is one development property that's included in the $3.5 billion that isn't going to be spitting out NOI until partway through 2012. We did sort of highlight that on, I think it was slide five, and that the transactional package is about a $900 million asset. So, if you back that out, multiply it by 6.7%, you get to the slightly less than the $185 million that Ric had alluded to, but that 6.7% is on cash NOI, and there are straight line rents which are included in the number that Ric had alluded to.

John Guinee - *Stifel Nicolaus - Analyst*

Okay. Can you talk through, just for us who don't spend a lot of time in Sydney, Perth, or Melbourne, the overall size of these markets, and just a rough comparison? It's obviously not Midtown Manhattan or west L.A. Is it Houston-esque, is it like Minneapolis, is it like Atlanta? How would you characterize the total square footage replacement cost, what it costs to build in this market, et cetera?

Ric Clark - *Brookfield Properties Corp - President & CEO*

So, just, let's see. Starting with Sydney. So, the Sydney--Tom, do you want to comment on the Sydney market. You want to start, and then I'll--

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Tom Farley - *Brookfield Properties Corp - CEO - Canadian Commercial Operations*

Sure.

Ric Clark - *Brookfield Properties Corp - President & CEO*

It's about--well, go ahead Tom.

Tom Farley - *Brookfield Properties Corp - CEO - Canadian Commercial Operations*

So, the Sydney market, first of all, there's about five million people that live in Sydney. The downtown, well the CBD office market is about 51 million square feet, and there's about 1.9 million under construction. Today, it has a vacancy rate of about 8%, and we consider the market to be very strong. Replacement cost numbers, I don't have right in front of me, but we could certainly get them. Melbourne is a city that is approximately four million people. It has an office market of about 45 million square feet in the CBD, and the vacancy rate is 6.3%. And I should say, by the way, Sydney is, when you look at that market, it's primarily the financial industry that drives that economy. Whereas in Melbourne, it's a combination of government and financial services. When you go to Perth, Perth is -- has a population of approximately 1.5 million people. The CBD is 16 million square feet. It has a vacancy rate today of about 7.7%. And the driver in that economy is natural resources, primarily focused on iron ore, together with oil and gas.

John Guinee - *Stifel Nicolaus - Analyst*

And are hard costs and land costs roughly the same as the Midwest?

Tom Farley - *Brookfield Properties Corp - CEO - Canadian Commercial Operations*

No. You know, they're probably only a little higher. Again, I don't have the exact numbers here, but the rents are higher as well.

Ric Clark - *Brookfield Properties Corp - President & CEO*

So I'd just make a couple comments. Sydney would be like Toronto or New York, Perth would be like Calgary or Houston, and Melbourne is somewhere in between where it has a good combination of financial, resource and government tenants, and it also -- most of the superannuation funds are located in Melbourne. Generally, on average, I'm going to say new replacement costs is probably something like $900 a foot. We can get better clarity for that. We don't have those numbers with us here, but that's sort of the ballpark.

John Guinee - *Stifel Nicolaus - Analyst*

Okay. Great, thank you.

Ric Clark - *Brookfield Properties Corp - President & CEO*

Okay.

Operator

Your next question comes from the line of Alex Avery with CIBC.

Alex Avery - *CIBC - Analyst*

Can you hear me?

Ric Clark - *Brookfield Properties Corp - President & CEO*

Yes.

Alex Avery - *CIBC - Analyst*

Hello?

Ric Clark - *Brookfield Properties Corp - President & CEO*

Yes. Go ahead, Alex.

Alex Avery - *CIBC - Analyst*

Okay. Thank you. Just on the slide five in the Australian supplemental, just looking at the 6.7% going-in cap rate and the 6% levered FFO yield, that's not -- that's on the basis that you just are looking at the $1.4 billion -- the yield on the 1.4 billion? That would be the assumption there?

Bryan Davis - *Brookfield Properties Corp - SVP & CFO*

That's right, Alex.

Alex Avery - *CIBC - Analyst*

Okay. And then, as you look at funding that, you've noted $750 million subordinated acquisition facility from BAM. Is that at a similar rate to the $300 million line that you've got? I think that was last quarter at about 4%?

Bryan Davis - *Brookfield Properties Corp - SVP & CFO*

Slightly lower rate, the market, of course, is come in for corporate sort of credit as you know, and so we have got a rate of LIBOR plus $300 million, so we're closer to the 3.5% rate on the line. But it will be ultimately be priced very similar to, when we go through the process of renewing our bank line, something at around the range where the market is today, not when we renewed them back in early -- or late 2008, early 2009.

Alex Avery - *CIBC - Analyst*

Okay. And you've got a lot of transactions going on right now, Brookfield Homes is big, or the residential Carma Brookfield Homes deal would be a big question mark there. Presumably, if you had the capital, you would prefer to reduce the indebtedness to BAM?

Ric Clark - *Brookfield Properties Corp - President & CEO*

Yes.

Alex Avery - *CIBC - Analyst*

And on that transaction, there's been a little discussion about related party and the perception of conflicts of interest. With Brookfield Homes and Carma, it sounds like it would seem to present an even greater challenge from that perspective. Can you just talk about maybe some valuation goal posts, and perhaps how you plan to manage that process?

Ric Clark - *Brookfield Properties Corp - President & CEO*

At this point, we can't really -- it's early on, so we can't really give valuation metrics, but I would say that it is a similar process to Australia in that the independent committee will have an advisor, it's actually the same advisor, who will work closely with them on values that are presented by management. And they will, reach their own conclusions. But that's -- it's kind of early stages for that, though.

Alex Avery - *CIBC - Analyst*

So, would the valuation process, as you were mentioning, the Australian one was a stand alone valuation process. In the case of the residential developments, would it also incorporate valuations of Brookfield Homes relative to its book value, or relative to what you perceive its value to be, given that you'll be receiving shares instead of cash?

Ric Clark - *Brookfield Properties Corp - President & CEO*

Yes, yes. The valuations of the each entity would have to be done on a consistent basis. So, there's work to be done there.

Alex Avery - *CIBC - Analyst*

Okay. Thanks a lot.

Operator

Your next question comes from the line of Suzanne Kim with Credit Suisse.

Suzanne Kim - *Credit Suisse - Analyst*

Could you provide me with some more detail about your JV you're doing with Great Portland?

Ric Clark - *Brookfield Properties Corp - President & CEO*

Sure. So, we bought a 50% interest in a development site, 100 Bishopsgate in downtown London. At this point, we are working to finalize the planning on the development, and seeking to find anchor tenants in order to kick off the development. The site will be positioned to proceed with the demolition of what's on the site currently on or around March or April of next year. So, at this point, we're just in the planning and advancement stages, and looking to secure anchor tenants.

Suzanne Kim - *Credit Suisse - Analyst*

I guess what I'm trying to get at, is there a larger plan that you're trying to get into London? Is this the beginning of a relationship with Great Portland, or do you anticipate, after going to Australia, that you're going to expand in London in a larger way?

Ric Clark - *Brookfield Properties Corp - President & CEO*

London is a market that we believe there is synergies similar to the Australian synergies with the core strategy and holdings of Brookfield Properties. So, it is a market that we're committed to growing in, and we're working hard at it. As to whether or not we do more things with Great Portland, I think they're an excellent company, have a great management team, and we would be delighted to do more with them, but we're also looking to do things on our own. And at this point, we have nothing really to report as far as things that are imminent, but we have been spending a bunch of time in London, looking for things to do that we think will be complementary and accretive Brookfield.

Suzanne Kim - *Credit Suisse - Analyst*

Are there other Asian cities you are looking at right now to expand to?

Ric Clark - *Brookfield Properties Corp - President & CEO*

At the moment --

Suzanne Kim - *Credit Suisse - Analyst*

Given your comments earlier in the call.

Ric Clark - *Brookfield Properties Corp - President & CEO*

Yes. Look, I think, Asia is obviously an area of the world that is going to go through very substantial growth, and I'm sure there will be opportunities for firms like ours. At the moment, we don't know much about the market, and it isn't a principal area of focus for us.

Suzanne Kim - *Credit Suisse - Analyst*

Okay. Great, thank you.

Operator

Your next question comes from the line of Neil Downey with RBC Capital Markets.

Neil Downey - *RBC Capital Markets - Analyst*

Hi. Good afternoon. Firstly, for Bryan, turning back to the Australian assets, you would seem to have implied that there's maybe a $10 million straight line rent adjustment between GAAP and cash NOI. Could you further on to that, help us think about how we might think about AFFO, in terms of normalized tenant inducements, leasing costs, non- recoverable CapEx, on the $3.4 billion of gross assets?

Bryan Davis - *Brookfield Properties Corp - SVP & CFO*

So, I think you're right as it relates to your estimate on the straight line components and the numbers that we've presented. I don't know if I have in front of me necessarily all the various different things that would otherwise go into the calculation of AFFO in the terms of sustaining CapEx. I don't know if Tom can mention it. It's probably not much different than operating similar properties that we have in the North American market.

Tom Farley - *Brookfield Properties Corp - CEO - Canadian Commercial Operations*

Yes, and I think that the other point is that the agent of this portfolio is, it's a quite young portfolio, the buildings aren't very old. And so, that's another great compelling factor.

Neil Downey - *RBC Capital Markets - Analyst*

Okay. I know it's very early days on the proposal with Brookfield Homes, but presumably, you believe there's the ability to firstly effect a merger with your home building and land development business with Brookfield Homes on a tax deferred basis?

Bryan Davis - *Brookfield Properties Corp - SVP & CFO*

Of course tax is one of the areas that we will definitely look at with respect to this transaction. Ultimately, when, if the intention is to convert our position into cash, once you do that, you can no longer defer. But, at the end of the day we spend a lot of time insuring that we have sufficient losses within the system, so that we could structure transactions in the most tax efficient manner, and we'll continue to focus on that as it relates to this transaction and the evolution of this transaction.

Neil Downey - *RBC Capital Markets - Analyst*

So, I guess that goes to the next part of my question actually, Bryan. Your equity in the home building business is about $1.1 billion at book today. I think you may have hinted in the past, your view, or you certainly articulated that is in effect a historical number. Do you believe that you -- that Brookfield Properties can realize net cash, of at least $1.1 billion, even after some potential tax friction, or is that something you simply can't comment on at this point?

Bryan Davis - *Brookfield Properties Corp - SVP & CFO*

I'd say it's probably something that's too early to comment on.

Neil Downey - *RBC Capital Markets - Analyst*

Okay. Thank you.

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Operator

Your next question comes from the line of John Stewart with Green Street Advisors.

John Stewart - *Green Street Advisors - Analyst*

Thank you. Ric, can you let us know what percent of par BAM paid for the mezzanine debt, and when you say that they are essentially going to transfer the net benefit to you, how does that work? Do you buy it from them at their cost? Can you give us some color there?

Ric Clark - *Brookfield Properties Corp - President & CEO*

Well, to the second part of the question, there's no markup on it. BAM, in this instance, was a facilitator. They have debt operations, so this is kind of a natural for them. They were kind of in the mix on these kinds of things. So, as far as what we paid as a percentage of par, I don't think we can disclose that at this point. So, hopefully in the fullness of time, we'll be able to. But there is no markup -- there is no markup to BAM, if that's what you're asking.

John Stewart - *Green Street Advisors - Analyst*

Yes, that was definitely part of the question. So, essentially, BAM gives up half the upside. But, Bryan, can you give us any color on the total return swap?

Bryan Davis - *Brookfield Properties Corp - SVP & CFO*

Sorry, as it relates to?

John Stewart - *Green Street Advisors - Analyst*

Multiplex.

Bryan Davis - *Brookfield Properties Corp - SVP & CFO*

So ultimately, the transaction is structured in a manner where we are buying an economic interest in the underlying portfolio -- it's BAM's entire economic interest. The total return swap is a mechanism that allows us to receive the earnings underlying the properties as well as any value appreciation or depreciation underlying the properties. I know we put a slide in the package that we had published this morning that attempts to walk through that structure, but it puts us in a position where we make an investment today, and we participate in the economics going forward.

John Stewart - *Green Street Advisors - Analyst*

Okay, thanks.

Operator

Your next question comes from the line of Anthony Paolone with JPMorgan.

Joe Dazio - *JPMorgan - Analyst*

Hello guys. It's Joe Dazio here with Tony. Sorry if I missed this earlier, but can you walk through as it relates to the Trizec debt and BAM buying at a discount, how that equity -- "equity" that was created, but then buying at a discount was transferred to you guys? Is there any costs that you bear in order to do that?

Ric Clark - *Brookfield Properties Corp - President & CEO*

There's no additional costs other than the purchase price for the debt, which I believe is your question. And, the debt has not been transferred at this point. And it's more for technical reasons that I don't really want to get into the details on the call, but I think BAM was a great facilitator of what we were trying to do, which was achieve the early deleveraging of -- for the -- in anticipation of refinancing of this mezzanine debt.

Joe Dazio - *JPMorgan - Analyst*

Thank you.

Ric Clark - *Brookfield Properties Corp - President & CEO*

You're welcome.

Operator

Your next question comes from the line of Jim Sullivan with Cowen and Company.

Jim Sullivan - *Cowen and Company - Analyst*

Thank you. I just wanted to follow up on the issue of the Australian lease profile, particularly the focus on the issue of the so-called fixed rent review. Is the -- this is not in the nature of fixed steps, I believe. Is this something where the rent is actually reviewed and increased every year based on a variety of stated contingencies, and its simply averaged 4% over time?

Tom Farley - *Brookfield Properties Corp - CEO - Canadian Commercial Operations*

No. In fact, it's an automatic escalator. And certain leases may have a subsequent mark to market, partway through, their lease that would be dependent on the variables of that time. But, generally 85% of the portfolio has an average 4% automatic escalator.

Jim Sullivan - *Cowen and Company - Analyst*

Okay. So, that's essentially the driver of the straight line number?

Tom Farley - *Brookfield Properties Corp - CEO - Canadian Commercial Operations*

Yes.

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Jim Sullivan - *Cowen and Company - Analyst*

Okay. And the -- so when we talk about the FFO yield, that FFO yield includes that straight line accrual?

Tom Farley - *Brookfield Properties Corp - CEO - Canadian Commercial Operations*

Yes.

Jim Sullivan - *Cowen and Company - Analyst*

Okay. And, the mark to market currently, per the hand out, I think was about 6% or 7%? Is that right?

Bryan Davis - *Brookfield Properties Corp - SVP & CFO*

The mark to -- can you repeat that?

Jim Sullivan - *Cowen and Company - Analyst*

In terms of the -- I think it indicated in the handout a mark to market of roughly 6%, I think a $3 difference per foot, I want to say. I was trying to calculate the roll, the positive impact on the growth rates from the roll. 10% of the leases rollover the next two years, and in-place, it's about, no, sorry, 6% below market, right?

Bryan Davis - *Brookfield Properties Corp - SVP & CFO*

Right. Correct.

Ric Clark - *Brookfield Properties Corp - President & CEO*

Correct. That's right.

Jim Sullivan - *Cowen and Company - Analyst*

Okay. Okay, shifting to New York, the Downtown market. In your prepared comments, I think the bottom line was 90% of the 4.6 million square feet are in various stages of activity. And, I think the summary language talked about a combination of new and existing, and also made reference to the possibility of some tenants who currently based in Midtown moving Downtown. I just wanted to make sure, to the extent you're including existing tenants in that 90% number, is that -- by that, do you mean tenants who are existing subtenants of Merrill Lynch, the same space?

Ric Clark - *Brookfield Properties Corp - President & CEO*

Yes.

Bryan Davis - *Brookfield Properties Corp - SVP & CFO*

Yes.

Jim Sullivan - *Cowen and Company - Analyst*

Okay. Very good. Thank you.

Ric Clark - *Brookfield Properties Corp - President & CEO*

You're welcome.

Operator

Your next question comes from Sam Damiani with TD Newcrest.

Sam Damiani - *TD Newcrest - Analyst*

Thank you. Just on the mezz loan discount, that benefit being transferred to Brookfield, what is BAM getting in return for giving half of that up?

Ric Clark - *Brookfield Properties Corp - President & CEO*

Nothing. They are getting the benefit of their 50% investment through their ownership in Properties, basically.

Sam Damiani - *TD Newcrest - Analyst*

So, the other 50%, they are just giving it up? They didn't ask for anything in return?

Ric Clark - *Brookfield Properties Corp - President & CEO*

No.

Sam Damiani - *TD Newcrest - Analyst*

That's totally independent of any sort of negotiations on the Carma sale?

Ric Clark - *Brookfield Properties Corp - President & CEO*

You know Sam, this is a little bit tricky. To put a little light around it, as you can imagine, when you do financings, the borrower is not typically permitted to buy back the debt. So, hopefully that explains it. We weren't permitted to buy it. Properties was not permitted to buy it.

Sam Damiani - *TD Newcrest - Analyst*

So, did you effectively lend BAM the money to buy it for you then, or --?

Ric Clark - *Brookfield Properties Corp - President & CEO*

In effect, yes.

Sam Damiani - *TD Newcrest - Analyst*

So, when do you think that loan will be transferred?

Ric Clark - *Brookfield Properties Corp - President & CEO*

Whenever we wrap up the refinancing.

Sam Damiani - *TD Newcrest - Analyst*

So, any time within the next 12 months basically?

Ric Clark - *Brookfield Properties Corp - President & CEO*

Between now and October 2011 is the expectation.

Sam Damiani - *TD Newcrest - Analyst*

Okay. Thank you.

Operator

Your next question comes from the line of Shant Poladian with Canaccord Genuity.

Shant Poladian - *Cannaccord Genuity - Analyst*

Hello?

Ric Clark - *Brookfield Properties Corp - President & CEO*

Yes, Shant?

Shant Poladian - *Cannaccord Genuity - Analyst*

Hi. With respect to that debt on the Australian assets, there's only 2.5 years worth of term. If you guys, you can access debt in multiple markets, obviously you can get debt cheaper in Canada, or you can do prefs, and you can do a crunch swap. How should we be thinking about this debt in a couple years?

Bryan Davis - *Brookfield Properties Corp - SVP & CFO*

Shant, this is Bryan. Again, we don't -- we always say we don't have a crystal ball ahead of us, but that's one of the things we think about. Who knows ultimately what the Australian market looks like from cost to capital perspective going two years out, but as we think through the refi of this underlying debt, we are definitely thinking through some of the other synergies that we may get from this transaction, that may involve the right side of the balance sheet and whether or not we can access capital in other sources against that same security at a cheaper rate.

Shant Poladian - *Cannaccord Genuity - Analyst*

And, what kind of levered IRR are you thinking about this investment, over your time horizon?

Ric Clark - *Brookfield Properties Corp - President & CEO*

I think over a ten year time horizon at a minimum, it should be in keeping with our overall goal of delivering something like a low- teen return to investors. So I think at the minimum, that, but possibly better.

Shant Poladian - *Cannaccord Genuity - Analyst*

So, basically looking at a negative spread on debt in year one is really missing the point, right?

Ric Clark - *Brookfield Properties Corp - President & CEO*

Yes.

Shant Poladian - *Cannaccord Genuity - Analyst*

Okay. Thanks a lot.

Ric Clark - *Brookfield Properties Corp - President & CEO*

Yes.

Operator

Your next question comes the line of Michael Bilerman with Citi.

Michael Bilerman - *Citigroup - Analyst*

Just a follow up. Some of the assets are owned by Prime Property Fund, which is Morgan Stanley. How did that conflict also, in terms of managing that process?

Ric Clark - *Brookfield Properties Corp - President & CEO*

So Michael, it's just unfortunate coincidence that they both have similar names. It's actually not Morgan Stanley. It's a publicly listed vehicle, of which the former Multiplex Group owned the majority of it, and I don't know if I have that percentage in front of me. But it has nothing to do with Morgan Stanley.

Michael Bilerman - *Citigroup - Analyst*

Okay.

Ric Clark - *Brookfield Properties Corp - President & CEO*

We bought BAM's interest in that.

Michael Bilerman - *Citigroup - Analyst*

Okay. And then typically, when companies make large acquisitions, you start talking about how it will impact the numbers, accretion or dilution. I'm just curious, I know there's still a lot of things to get done, but on the surface, when you take all the transactions together would seem to be a pretty dilutive event, just given the FFO yield on the assets you're buying, the high FFO yield of the assets that you plan to sell, and likely still financing that you need to get in place. So, how should we be thinking about how all this nets down to your earnings profile?

Ric Clark - *Brookfield Properties Corp - President & CEO*

I think the goal is to redeploy capital that's being generated at lower cap rates -- at about the same or lower cap rates than what the initial cap rate is for the Australian assets, for one. For two, when it comes to redeploying capital that we take out of the residential division, there's no question that will be dilutive, and the expectation, and at least hope, is that the multiples that are given to the earnings coming out of the residential division are very meaningfully less than the more pure and consistent income you would get from an office asset. So, that's how we're thinking about it.

And we think, just assuming for a second, hypothetically, that we are generating capital at 6.7% cap rate and reinvesting it at a 6.7% cap rate. Our view is that the upside in Australia, at least over the next decade, is greater than what can be achieved in the North American markets.

Michael Bilerman - *Citigroup - Analyst*

And then, one of the things you have in your presentation is that by doing this total return swap, you'll be able to benefit the property level financing, that you can transfer this portfolio to future dates and to a different ownership entity, either through a public or private fund, and lower your stake, which obviously now you're going to use the Toronto, or the Canadian subsidiary -- that equity in there to be able to go buy this. As you sit back, let me say this the right way. What do you want to do when you grow up in terms of Brookfield Properties? What -- how do you envision the ownership of assets, and in the relative geographies, what ultimate do you want to own?

Ric Clark - *Brookfield Properties Corp - President & CEO*

Just looking back to the last decade, we have not been, at all, a static organization. The Company, although it's been around since the early, or late '20s, I think, in it's current form since probably the late '90s, or mid- '90s, has gone -- is the amalgamation of seven portfolio acquisitions, and we're constantly rethinking the strategy and the direction. A the moment, what we envision is owning the, or one of the highest quality collection of office assets in the most important developed countries in the world, and those being Canada, the US, Australia, and ultimately, the United Kingdom. But not in every market -- not the EOP strategy where you want to do be all things to all people, but very focused on the best, most dynamic and resilient markets within those countries. And it would be -- I think that's basically it.

Michael Bilerman - *Citigroup - Analyst*

Just the last one, in terms of this mez debt purchase, you obviously within the Fund have other partners, other capital partners that you have, but there's also Blackstone. How does--when you talk about the $570 million, is it the $570 million converting to effective equity? So, that you're putting all this capital, you're able to get it at some discount, effectively the $570 million converts to equity, in which your ownership take is going out, and how does it also affect your other partners, both your partners in the Fund, but also Blackstone's involvement?

Ric Clark - *Brookfield Properties Corp - President & CEO*

As far as how it affects the other partners, I suppose all the details of that have not yet been worked out. But it won't really be meaningful from an economic standpoint to Brookfield Properties, I think is the important point to make. So --

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Dennis Friedrich - *Brookfield Properties Corp. - President and CEO - U.S. Commercial Operations*

I think we're, Michael, fairly straightforward, we're looking at as an ultimate conversion equity in deleveraging of the US Fund itself, and the $4.1 billion of existing debt that's up against that fund.

Michael Bilerman - *Citigroup - Analyst*

So, you're viewing it as all equity you're putting in? Your effectively paying something in the magnitude of some discounts of the $600 million, so you're putting another $600 million -- we have to think about -- when we think about sources and uses, you have another use of capital somewhere up to $570 million of equity that you're injecting into the Fund, that you'll have to raise somewhere else?

Dennis Friedrich - *Brookfield Properties Corp. - President and CEO - U.S. Commercial Operations*

I don't think we're saying that, Michael.

Ric Clark - *Brookfield Properties Corp - President & CEO*

Sorry, so you're --

Michael Bilerman - *Citigroup - Analyst*

The debt was bought at a discount by BAM, right?

Dennis Friedrich - *Brookfield Properties Corp. - President and CEO - U.S. Commercial Operations*

Right.

Michael Bilerman - *Citigroup - Analyst*

So, and now they are transferring that debt, now you're paying them for that debt. Who is getting the equity? Somebody has to be taking some ownership stake in the portfolio if someone is buying debt. I'm just wondering who that is? Is that Properties taking a bigger stake in the Fund, by converting debt to equity, or is it BAM taking a stake in the fund as an equity --

Ric Clark - *Brookfield Properties Corp - President & CEO*

No, I would view it as Properties -- it's Properties pro-rata share of deleveraging in the Fund.

Dennis Friedrich - *Brookfield Properties Corp. - President and CEO - U.S. Commercial Operations*

The US Fund leverage.

Ric Clark - *Brookfield Properties Corp - President & CEO*

Yes. So, there isn't an incremental -- and some of the details need to be worked out, but I would just look at this as if there's no incremental ratcheting up and equity interest in the fund. It's just simply -- and it's possible we've overfunded. And we won't really know until we finish our work on refinancing, which is underway now. But it's possible that we'll get money back once the refinancing is done.

Michael Bilerman - *Citigroup - Analyst*

But, you're coming out of pocket for money. Is this what it all comes down to?

Ric Clark - *Brookfield Properties Corp - President & CEO*

Yes.

Dennis Friedrich - *Brookfield Properties Corp. - President and CEO - U.S. Commercial Operations*

Yes. That's gross equity in the deleverage.

Bryan Davis - *Brookfield Properties Corp - SVP & CFO*

And Michael the --

Ric Clark - *Brookfield Properties Corp - President & CEO*

Go ahead, Bryan

Bryan Davis - *Brookfield Properties Corp - SVP & CFO*

The other important point is that's not -- we've already included that in the $1.3 billion of liquidity that we've been referencing as it relates to the liquidity position of Brookfield Properties going forward.

Michael Bilerman - *Citigroup - Analyst*

Okay. Thank you.

Operator

Your next question comes from the line of Ross Nussbaum with UBS.

Ross Nussbaum - *UBS - Analyst*

Hi, my follow-ups have been answered, thank you.

Operator

Your next question is from the line of Mario Saric with Scotia Capital.

Mario Saric - *Scotia Capital - Analyst*

One last question, and just on the topic of liquidity. Post all of the proposed transactions, majority of your liquidity that you built up over the past 12 months would have been absorbed at that point in time. How do you look at your liquidity on a pro forma basis, as well as your leverage at this point in time in the cycle? Are you comfortable with it, or what are the thoughts there?

Bryan Davis - *Brookfield Properties Corp - SVP & CFO*

Ric, maybe I can address it. We're very comfortable with our leverage levels as we sit today. A good share of the liquidity that we raised has been deployed, either through our investment in Bishopsgate, what we have been talking about with respect to the debt in the Fund, and with respect to this transaction, but we still have liquidity. We still have our full undrawn bank lines. We also have the ability to refinance a number of assets that are coming due over the balance of this year and into next year that are at loan to value levels in and around the 30% change.

So, I think we feel good about our balance sheet and our liquidity position going forward, as well as the leverage level that we currently sit at. Taking into account that the big thing that influences our leverage is, of course, the US Office Fund, and we're expecting, as we talked about, that this will represent a deleveraging event of the US Office Fund when ultimately that mez debt rolls in 2011.

Mario Saric - *Scotia Capital - Analyst*

And everything that's happened within the US Office Fund, does that impact your ability to sell assets from that fund versus, let's say, 12 months ago?

Dennis Friedrich - *Brookfield Properties Corp. - President and CEO - U.S. Commercial Operations*

In terms of the purchase of the mezz, in relation to that?

Mario Saric - *Scotia Capital - Analyst*

Yes, purchase of the mez, and as well any restructuring that you've potentially done.

Dennis Friedrich - *Brookfield Properties Corp. - President and CEO - U.S. Commercial Operations*

Some of the restructuring will help asset sales, but in general, no. If anything, our view on asset sales would be selling the right assets at the right time.

Mario Saric - *Scotia Capital - Analyst*

Okay, thank you.

Operator

Your next question comes from the line of Neil Downey with RBC Capital Markets.

Neil Downey - *RBC Capital Markets - Analyst*

(Inaudible) billion transactions, Bryan, does that put $3.4 billion of assets and $2 billion of debt on your balance sheet, or is it a one-line item, given that it's a total return swap?

Bryan Davis - *Brookfield Properties Corp - SVP & CFO*

It is $3.4 billion of assets and $2 billion of debt, as we expect. In part, it's control over assets, which is the measured test under IFRS, and we have management and economics, which effectively equal control. Having said that, and as you would have noticed, we did put out the proportionate set of financial statements, so even if it was one-line item, we would have definitely showed you what the financial statements would have looked like on a proportionate basis.

Neil Downey - *RBC Capital Markets - Analyst*

Okay. Thank you.

Operator

Your next question comes from the line of Sam Damiani with TD Newcrest.

Sam Damiani - *TD Newcrest - Analyst*

I just want to clarify the yield there, the City Square property in Perth as the development assets earning no yield today, and does the 6.7% cap and 6% FFO yield, that strips out that investment out of the $3.4 billion? Is that right?

Bryan Davis - *Brookfield Properties Corp - SVP & CFO*

Correct. But it is assumes that the equity that we have invested in City Square as a result of this transaction, we have the ability to capitalize interest associated with that.

Sam Damiani - *TD Newcrest - Analyst*

I see. Okay. So, that's a $900 million asset, I think you had mentioned earlier. Has that money been spent? You're buying it at fully completed cost?

Bryan Davis - *Brookfield Properties Corp - SVP & CFO*

It is in the process of being spent, the equity has been fully committed. There's a construction facility in place that will fund the balance of the construction costs until completion, I think in 2011 or thereabouts.

Sam Damiani - *TD Newcrest - Analyst*

So how much debt does that bring you up from starting -- when you're starting with $2 billion? How much more will be on the balance sheet when that building is completed?

Bryan Davis - *Brookfield Properties Corp - SVP & CFO*

So, $500 million.

Sam Damiani - *TD Newcrest - Analyst*

$500 million. So, the total cost of this is 3.9 --?

Bryan Davis - *Brookfield Properties Corp - SVP & CFO*

Hold on. Yes. Let me get back to you on that. I have to check to make sure we didn't pro forma the full debt level into the $2 billion. We may have done that.

Sam Damiani - *TD Newcrest - Analyst*

That would be great, and just the yield on that development, $900 plus a foot is what I'm seeing here, and the market rents seem to be in the $45 range based on your disclosure. Does that suggest the stabilized yield to be around 5%?

Bryan Davis - *Brookfield Properties Corp - SVP & CFO*

No, I -- yes. That number's --

Ric Clark - *Brookfield Properties Corp - President & CEO*

This property would be the newest, and probably, likely one of the best, if not the best asset, in the portfolio. So, the yield's going to be a bit lower than the yields in the rest of properties, but I think it's a little higher than that.

Sam Damiani - *TD Newcrest - Analyst*

How much, Ric, is it a sub 6% asset, or it's up 5.5% still?

Ric Clark - *Brookfield Properties Corp - President & CEO*

I don't think it is. I think it's -- shoot, I don't have it. Sam, can you give me a second? I don't see it, so let me see if I can find it.

Bryan Davis - *Brookfield Properties Corp - SVP & CFO*

And while Ric's looking, Sam, I confirm that the debt number that we provided on page five pro forma is in the full debt that will be on City Square.

Sam Damiani - *TD Newcrest - Analyst*

So, that money has been spent, or, so you're going to start with a lower debt amount, and its going to creep up to that level over the next year?

Ric Clark - *Brookfield Properties Corp - President & CEO*

Yes. Yes. It creeps up, yes. Sam, unfortunately, I thought I had it, but I don't. So, we'll have to get back to you on it.

Sam Damiani - *TD Newcrest - Analyst*

No worries. Great. Thank you.

Ric Clark - *Brookfield Properties Corp - President & CEO*

Yes.

Operator

Your next question comes from the line of Jimmy Shan with National Bank Financial.

Jimmy Shan - *National Bank Financial - Analyst*

Thanks. Just a couple of quick clarifications. In terms of the liquidity position, after all these transactions are affected, including the sale of the resi business, you still going to have about $1 billion of -- to be deployed. Is that a fair estimate?

Bryan Davis - *Brookfield Properties Corp - SVP & CFO*

Yes, as we look out into 2011, and build in the various different capital initiatives that we are focused on, whether its refinancing of under-levered properties that are coming due in the next little while, when you take that into account with the existing capacity that we have within our bank lines, that's probably a fair number.

Jimmy Shan - *National Bank Financial - Analyst*

And, how does that $1.3 billion of liquidity you referenced on slide five, you mentioned $300 million of that is from credit facilities? The rest are in some form of cash, or short-term investments?

THOMSON REUTERS

Bryan Davis - *Brookfield Properties Corp - SVP & CFO*

No, no. Of the $1.3 billion, it rounds out to about $800 million that relates to credit, and the balance is cash, sort of liquid cash, whether it's our deposit or cash, just cash on our balance sheet.

Jimmy Shan - *National Bank Financial - Analyst*

Okay. And then last question, I think Ric, you made reference to BAM's Canary Wharf. So, should we assume that a transaction -- is out of the question given the management structure of that business?

Ric Clark - *Brookfield Properties Corp - President & CEO*

I wouldn't make that assumption. It's not necessarily out of the question. It's just -- given our overall liquidity, and what BAM owns in Australia, and I think the opportunity, this was the logical thing to do now. Whether or not we do something with them for the UK, just requires further thought, and we just haven't begun to think about it.

Jimmy Shan - *National Bank Financial - Analyst*

Okay, thanks.

Operator

Your next question comes from the line of Suzanne Kim with Credit Suisse.

Suzanne Kim - *Credit Suisse - Analyst*

Hi. I apologize if you already addressed this question earlier, but I'm just wondering how all the shuffling is going to impact your guidance, assuming that you do spin off the residential portfolio.

Bryan Davis - *Brookfield Properties Corp - SVP & CFO*

I think that one of the things that we alluded to is a transaction as it relates to the residential portfolio likely won't be effective until towards the end of the year, if not early next year. So, and we haven't come up with 2011 guidance just yet. So, as it relates to 2010 guidance, depending on the close of this transaction, it's not going to have that meaningful an impact.

Suzanne Kim - *Credit Suisse - Analyst*

Okay. But, in terms of all the other transactions, you're maintain your guidance for the year then, your IFRS guidance?

Bryan Davis - *Brookfield Properties Corp - SVP & CFO*

Yes. Yes. The one big reconciling item is that our IFRS guidance didn't include the $53 million or $0.10 gain that we were able to earn on the investment in the debt underlying the Washington portfolio. So, whether you strip that out or keep that in, you have to just bear that in mind.

Suzanne Kim - *Credit Suisse - Analyst*

Great, thanks.

Operator

And at this time, there are no further questions.

Ric Clark - *Brookfield Properties Corp - President & CEO*

Thank you, operator. I just would wrap up by responding to Sam's question earlier, and the initial yield on the City Square transaction is -- it's in the 6% or solidly, probably mid-6's, and happy to provide more clarity on that for anybody who wants it later. We obviously ran over our 12 o'clock hard stop, but given the level of questions, we felt that it was appropriate, and if anybody has any additional questions they'd like for us to follow-up on, we'd be pleased to do that. So, thanks for your participation today.

Operator

This concludes today's conference. You may now disconnect.
