Market Intelligence Report:

Commercial Property Market Intelligence Report: *Status and Business Opportunities*

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Second Quarter 2013

Executive Summary

After growing at a solid pace in the first quarter, economic growth appears to have slowed somewhat during the second quarter, reflecting continuing difficulties in the Eurozone and more modest growth in Asia and Latin America. With the exception of the apartment sector, the unusually sluggish economic recovery has made for a painfully slow improvement in commercial real estate operating fundamentals and new construction activity.

On a positive note, the commercial real estate market continues to benefit from increasing liquidity and attractive financing rates. The low interest rate environment has played a major role in rising commercial property prices. To investors, the combination of lower interest rates and higher property values has made commercial real estate more attractive. Operating fundamentals continue to improve, at least slowly, across all property types with vacancy rates continuing to trend lower and rent growth higher.

Apartments remain the strongest market sector as vacancy rates continue to decline. Asking and effective rents are still increasing, but there are signs that improvements in fundamentals may be decelerating. Market conditions are tightening, with inventory constraints becoming evident due to strong demand and low supply. This has fueled the construction boom, with builders and developers seeking to take advantage of today's supply constraints.

Office Sector Crawls Back

Though the office sector has witnessed 13 quarters of positive demand for space, its metrics have generally been sub-par during this stage of market recovery, in part because of the way that businesses' use of space has changed. Office employment growth has been quite modest through the first four years of the economic recovery and has actually slowed somewhat in recent months, although there have been some notable exceptions, such as in the energy sector and select technology sectors (including mobile internet, cloud computing and social networking). The moderate improvement in the labor market has not been strong enough to strengthen the office sector, despite some improvement in vacancy rates.

New construction remains a shadow of its former self with current activity still near record lows. The construction pipeline, however, is beginning to show signs of life. Looking ahead, the relatively slow office employment growth rate is expected to accelerate over the next few years, driven in part by the financial services sector, which is benefiting from the rebound in home sales, and the professional and technical services sector, which is also gaining strength. It is interesting to note that more than

continued on page 2

60% of the 80,000 office buildings nationwide are at least 20 years old, representing a significant retrofit opportunity for real estate investors and developers to potentially earn higher yields.

Retail, Industrial Continue to Improve

Recovery in retail fundamentals has been the slowest of all key property types. Vacancy rates have fallen only slightly from their peak in late 2011, and rent growth has risen only modestly. Sales growth has been uneven, with much of the activity at low end "dollar" and high end "luxury" stores. The nation's top tier malls continue to fare better, with higher rent growth and lower vacancy rates. Due to still-struggling retail sales, competition from online retailers, and a muted demand for space, new construction remains anemic.

Industrial fundamentals continue to improve with vacancy rates continuing to decline. However, the improvement is now at a slower rate than exhibited in the second half of last year. Demand for warehouse and distribution space, driven by gains in international trade, e-commerce and the energy boom, continues its slow but steady improvement. The on-going revival in manufacturing activity and the continued influx of foreign direct investment are also fueling gains in many markets. The expected slightly faster pace of improvement during the rest of the year has already resulted in some speculative construction, with REITs responsible for the vast majority of this activity.

Strong Forecast in Hospitality Sector

The hospitality sector has, until recently, lagged other commercial property types during the market recovery. However, this asset class has recently started coming back in vogue as demand is spiking up just as the supply growth has plummeted to record lows. Significantly, hotel transaction volume is 50% higher this year compared to the same period of 2012 as room demand heats up in a market that has seen little new construction over the last five years. Average room rates are on the rise in most markets, making the sector a more desirable asset class for investors.

The historically low level of new supply, combined with rising hotel pricing and the relative scarcity of properties available for sale in the largest metros, is causing investment activity to spill into secondary markets. The sector is expecting to see significant gains next year, including a healthy increase in revenue per available room and net operating income. Investors are also expected to do well with strong property value growth and increasingly favorable debt terms.

Construction Fueled by Foreign Investment

Commercial construction overall in the market is improving, although from an extremely low base. Construction of new factories and R&D centers has increased with the help of foreign investment. Warehouse and distribution construction is also ramping up, and the construction of data centers remains strong. Office and retail development is proceeding, albeit cautiously. Speculative office development has been essentially limited to major energy hubs and tech centers. Retail development is beginning a turnaround, with the strongest growth at the lower end of the market. Grocery-anchored centers and projects feeding off mass transit links are also beginning to make some headway for the first time in several years.

Flow of Capital Gains Traction

Capital markets continue do well and are anchoring the recovery in commercial real estate. The commercial mortgage market is growing as demand strengthens and lending standards loosen. Notably, borrowers have more financing alternatives than at any time in the last five years. As such, transaction volume is increasing across all major debt capital sources, including banks, CMBS, life insurers and GSEs, and should continue as the year progresses. Commercial real estate prices appear to be resuming broad-based gains, shaking off the effects of a seasonal slowdown in the first quarter. Notwithstanding, much of the capital markets' liquidity must still be credited to the Federal Reserve's continued quantitative easing, which may be changing over the near term forecast.

Lenders

The second quarter of the year finds commercial real estate lenders doing well. Provisions for loan losses continue to fall, and a growing number of banks have cleared through their distressed assets and are ready to return to actively lending again. And for the first time in a long time, underwriting criteria on some lending is beginning to loosen. At the same time, demand in the marketplace is increasing, driven in large part by the low interest rate environment and the expanding need for refinancing. However, economic growth is now threatening the Fed's monetary easing program, which will result in a gradual rise in interest rates. This will adversely impact borrowing for commercial real estate transactions and the operating income of highly leveraged properties. It likely will also slow the pace of asset price increases unless underlying economic conditions improve much more than they have to-date.

continued on page 3

Commercial Property Market Intelligence Report *(continued from pg. 2)*

Commercial banks and savings institutions insured by the FDIC continue to get stronger. The FDIC's *First Quarter 2013 Quarterly Banking Profile* reported an increase in both bank profits and lending volumes as well as a continued decline in the number of problem banks. The FDIC reported an aggregate profit for the banking industry of $40.3 billion in 1Q13, an all-time high. This is the 15th consecutive quarter that earnings have registered a year-over-year increase. The number of FDIC-insured institutions reporting financial results fell to 7,019 in 1Q13 from 7,083 in 4Q12. In 2007, prior to the last fiscal crisis, there were 8,559 FDIC-insured banks reporting. During the first quarter of the year, four insured banks failed, the smallest number of bank failures in a quarter since 2Q08. Commercial real estate exposure continues to be the main driver behind problem loans at failed banks.

The number of institutions on the FDIC's problem list in 1Q13 fell for the eighth consecutive quarter, after increasing for 19 quarters (since 3Q06). The number of "problem" institutions declined from 651 in 4Q12 to 612 in 1Q13.

The Federal Reserve's April 2013 *Senior Loan Officer Opinion Survey on Bank Lending Practices,* found that 27 of the 67 banks (40%) surveyed indicated that they experienced "moderately stronger demand" for commercial real estate loans in 1Q13. The remaining banks (60%) indicated the demand "stayed about the same as in the previous quarter." Thirteen of the 36 large banks (36%) responding (with total domestic assets of $20 billion or more as of December 31, 2010) indicated that commercial real estate loan demand was "moderately stronger." This compares to 14 of the 31 smaller banks (45%) responding to the survey.

This same survey found that lending requirements for approving commercial real estate loans were beginning to loosen at more and more banks. Although the majority of banks (76.1%) surveyed have not changed their bank's credit standards, almost one-quarter (25% of the large banks and 20% of the smaller banks) were found to have eased their standards.

According to the Mortgage Bankers Association's (MBA) *Quarterly Survey of Commercial/Multifamily Mortgage Bankers Originations*, *Q1 2013*, commercial and multifamily mortgage loan originations experienced their usual seasonality, decreasing by 46% compared to the fourth quarter of last year. Nevertheless, originations were still up (9%) compared to a year ago. The low interest rate environment and improving property markets were helping more deals underwrite successfully.

Distress Levels Falling

Real Capital Analytics (RCA) tracks the distressed asset market and recently reported $158.7 billion in distressed loans associated with 11,566 properties in 1Q13, down from $167.5 billion (associated with 12,116 properties) reported the prior quarter. The size of the distressed asset market peaked at $191.5 billion in October 2010. The $158.7 billion total consists of $106.6 billion in troubled loans associated with 7,646 properties (down from $113.9 billion associated with 8,184 properties in the last quarter) and $52.1 billion in lender REO associated with 3,920 properties (down slightly from $53.5 billion in lender REO associated with 3,932 properties in the last quarter). Of the $394 billion of mortgages that became troubled since the 2007 market peak, approximately 60% have been resolved, and new instances of distress continue to decline. In another sign of market strength, the percentage of commercial properties selling at distressed prices dropped to 16.4% in March from 25.5% in March of last year.

CMBS/CDOs

Commercial mortgage-backed securities issuance has been a cornerstone of commercial real estate financing and thus far, 2013 has been a very good year. Issuance reached $39 billion in the first four months of this year, more than double $15 billion during the same period last year. This puts the sector on pace to shatter the $48 billion in originations for all of 2012. Credit spread tightening has resulted in CMBS becoming more competitive with insurance companies for the highest quality loans, driving competition within the capital markets to the benefit of borrowers. Originations are now forecast to reach between $70 and $100 billion this year. Delinquencies have also reached a post-recession low. The market recovery has resulted in underwriting standards slipping somewhat, with borrowers able to increase leverage, and interest-only loans becoming more prevalent.

REITs

Real estate investment trusts continue to have good access to the capital markets, as demonstrated by debt and preferred issuance of approximately $7.6 billion through April of this year. While some of the money raised is being used to refinance debt and deleverage, much of it is targeted for property acquisition and development. Good property fundamentals and low cost capital continue to enable REITs to upgrade their portfolios as they sell lower-quality assets and re-invest in higher-quality core assets. While a limited amount of

continued on page 4

development is taking place, principally in the apartment and healthcare sectors, most REITs are expected to continue to grow through moderately sized acquisitions.

Life Insurance Companies

Life insurance companies emerged from the last downturn in a good position due to their strict discipline in maintaining the most conservative underwriting practices. However, they now are facing new challenges resulting from increased competition, principally from banks and CMBS, and depressed interest rates. The FHFA's plan to shrink the role of GSEs in the multifamily space is expected to provide opportunity to life insurance companies that have already been aggressively pursuing high quality properties in the apartment sector. Loan originations are expected to increase this year, as is investment in high-quality properties in core markets.

Property Transaction Market

Property transactions in terms of both "number of transactions" and "dollar sales volume of transactions" declined in the first quarter of the year (each by approximately one-third) compared to the relatively robust fourth quarter of last year. This is attributed principally to seasonality. However, a number of interesting highlights are noted below:

- There are now 436 private real estate funds targeting aggregate commitments of $157 billion. Twenty of these funds raised approximately $5.2 billion in the first quarter of the year. Rockpoint Group raised $1.4 billion for Rockpoint Real Estate Fund IV. Prime Finance Partners raised $621 million for Prime Finance Partners III. Also particularly active in raising funds this quarter is Starwood Capital Group (for its Starwood Distressed Opportunity Fund IV). Others include:

  — Blackstone Group

  — Cabot Properties

  — Paulson & Company

  — Edge Principal Advisors

  — Invesco Real Estate

  — Noble Investment Group

  — Henderson Global Investors (London based)

  — Pembrook Capital Management

  — Velocis Fund

  — Adler Kawa Real Estate Advisors

  — Sitex Group

- Foreign investors continue to invest in U.S. commercial real estate. Last year, almost $27 billion was invested in the U.S., with two-thirds of the investments concentrated in nine major markets and principally focusing on office properties. They are now expanding their horizon into secondary markets. In the first four months of this year, they made up 8.8% of U.S. commercial transactions (on a dollar volume basis). Singaporeans, South Koreans, Israelis and Norwegians, in particular, are accelerating purchases of U.S. real estate, attracted to America's growing economy and rebounding prices.

  Recent foreign buyers include:

  — Norwegian Government Pension Fund Global

  — UBS (Switzerland)

  — Investcorp International, Inc.

  — Agellan Commercial REIT (Canada)

  — Independencia Asset Management (Chili)

  — IRSA Investments and Representations, Inc. (Argentina)

  — AMP Capital Investors (Australia)

  — Ivanhoe Cambridge (the real estate arm of Caaisse de Depot et Placement du Quebec, Canada's largest pension fund manager)

  — Harel Insurance Investments and Financial Services, Ltd. (Israel)

  — Menora Mivtahim Insurance Ltd. (Israel)

  — Overseas Union Enterprises Ltd. (Singa pore)

  — Government of Singapore Investment Corp. (GIC)

  — Mirae Asset Global Investments (Seoul, South Korea)

  — Family of Chinese real estate developer Zhang Xin

  — Family of Brazilian banking billionaire Moise Safra

continued on page 5

Commercial Property Market Intelligence Report *(continued from pg. 4)*

- The top commercial/multifamily loan originators in 2012 were:
  - — Wells Fargo – top originator for CMBS
  - — Bank of America – top originator for commercial bank loans
  - — MetLife – top originator among the life companies
  - — Wells Fargo and Walker & Dunlop – top originators for Fannie Mae
  - — CBRE Capital Markets – top originator for Freddie Mac
  - — Red Mortgage Capital – top originator for FHA/Ginnie Mae
  - — TIAA-CREF – top originator for pension funds
  - — KeyBank Real Estate Capital – top originator for REITs
  - — Cohen Financial – top originator for specialty finance
  - — Top 5 lenders overall:
    - Wells Fargo,
    - BofA,
    - PNC,
    - Prudential, and
    - KeyBank.

Italics indicates this buyer has acquired additional properties beyond what was reported in last quarter's Property Intelligence Report.

Bold indicates a buyer newly added to the list in the last quarter.

Regular font indicates no change from last quarter's report.

Where the Action is…

Most Active Buyers of High Quality Properties ($10 Million or Greater) in the Past 12 Months (in order of dollar volume acquired):

All Property Types	
1. Lehman Brothers – 564 properties	6. Starwood Capital– 205 properties
2. Equity Residential – 91 properties	7. **TIAA-CREF**– 44 properties
3. Blackstone Group – 1,376 properties	8. *Realty Income*– 585 properties
4. AvalonBay Communities – 76 properties	9. **RXR Realty**- 6 properties
5. **Caisse de Depot (Quebec)** – 87 properties	10. **JP Morgan** - 28 properties
Multifamily	
1. Lehman Brothers– 559 properties	6. American Campus Communities– 50 properties
2. Equity Residential – 86 properties	7. *Goldman Sachs*– 34 properties
3. AvalonBay Communities– 70 properties	8. **Caisse de Depot (Quebec)** – 28 properties
4. Greystar Real Estate Partners– 41 properties	9. **Fairfield Residential** – 36 properties
5. *TIAA-CREF* – 8 properties	10. **American Invesco Realty** - 14 properties
Office	
1. *RXR Realty*– 6 properties	6. Comcast Corp– 2 properties
2. Clarion Partners– 12 properties	7. **Zhang Xin (China)**– 1 property
3. **JP Morgan**- 10 properties	8. **M. Safra & Company** – 1 property
4. MetLife – 6 properties	9. **Crown Acquisitions** – 2 properties
5. **Caisse de Depot (Quebec)** – 3 properties	10. **Highgate Holdings** - 1 property
Hotel	
1. Blackstone - 1,169 properties	6. *Summit Hotel Properties*- 2 properties
2. GIC (Government of Singapore Investment Corp.) - 4 properties	7. **Host Hotels & Resorts** - 2 properties
3. **Omni Hotels** - 6 properties	8. DiamondRock Hospitality - 5 properties
4. Starwood Capital - 158 properties	9. Abu Dhabi Investment Authority - 2 properties
5. Sahara India Pariwar - 2 properties	10. **Chesapeake Lodging Trust** - 7 properties

continued on page 6

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Where the Action is…

The Most Active Buyers of High Quality Properties ($10 Million or Greater) in the Past 12 Months (in order of dollar volume acquired):

Retail

1. DDR - 51 properties	6. **Kimco** - 59 properties
2. *Starwood Capital*- 16 properties	7. **TIAA-CREF** - 8 properties
3. Macerich - 4 properties	8. The Inland Real Estate Group of Companies - 48 properties
4. Blackstone Group - 62 properties	9. **QIC Properties** - 8 properties
5. *Realty Income Trust*- 434 properties	10. Vornado Realty Trust - 4 properties

Industrial

1. *Blackstone* –98 properties	6. TPG Capital– 55 properties
2. Industrial Income Trust (IIT)– 45 properties	7. **Caisse de Depot (Quebec)** - 55 properties
3. Realty Income Trust– 64 properties	8. Brookfield Asset Management – 62 properties
4. **BioMed Realty** – 17 properties	9. Exeter Property– 45 properties
5. DivcoWest Properties –56 properties	10. Westcore Properties– 82 properties

Senior Housing & Care*

1. **HCP, Inc. -** 127 properties	6. **Harrison Street Real Estate Capital -** 11 properties
2. **Formation Capital** - 72 properties	7. **CNL Financial Group -** 31 properties
3. **Safanad** - 69 properties	8. **Engel Burman Group** - 6 properties
4. **Health Care REIT** - 29 properties	9. **Brookdale Senior Living (BKD)** - 21 properties
5. **Omega Healthcare Investors REIT** - 49 properties	10. **TPG Capital -** 210 properties

Development

1. **Hines**	6. City University of New York
2. **Genting Group**	7. Amazon
3. ProLogis	8. Irvine Company
4. **Boston Properties**	9. JDS Development
5. Memorial Sloan-Kettering	10. **Baupost Group**

**New category added this quarter.*

Most Active Sellers of Commercial Real Estate (over last 12 months)

1. Lehman Brothers	6. Equity Residential
2. Bank of America	7. **Goldman Sachs**
3. Barclays Group	8. **Beacon Capital Partners**
4. Blackstone	9. TIAA-CREF
5. **Hines**	10. **Carlyle Group**