



Emerging Trends in Real Estate® 2013

A publication from:



Emerging Trends in Real Estate®

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Executive Summary

The enduring low-gear real estate recovery should advance further in 2013: *Emerging Trends* surveys suggest that modest gains in leasing, rents, and pricing will extend across U.S. markets from coast to coast and improve prospects for all property sectors, including housing, which finally begins to recover. Most developers and investors who seek quick wins will remain frustrated as return expectations continue to ratchet down to more realistic but relatively attractive levels providing income plus some appreciation. In fact, real estate assets will almost certainly continue to outperform fixed-income investments in the ultralow-interest-rate environment induced by the Federal Reserve, as well as offer a familiar refuge from ever-seesawing stock markets.

Systemic global economic turmoil, hobbled credit markets, and government deficits, meanwhile, will continue to restrain anxious industry leaders who downplay chances for a faster-tracked upturn amid uncertainty. Investors discouraged about stratospherically priced core properties in gateway markets inevitably will “chase yield,” stepping up activity in secondary markets and acquiring more commodity assets. These players will need to focus prudently on current income-producing investments and avoid the surfeit of properties edging toward obsolescence, especially certain suburban office parks and some half-empty second- or third-tier shopping centers.

Most areas can sustain little if any new commercial construction, given relatively lackluster tenant demand and the generally weak employment outlook. Only the multifamily housing sector continues to offer solid development opportunities, although interviewees grow more concerned about potential overbuilding in markets with low barriers to entry—probably occurring by 2014 or 2015.

The real estate capital markets maintain a turtle's pace for resolving legacy-loan problems as the wave of maturing commercial mortgages gains force over the next three years. Low interest rates have bailed out lenders and underwater borrowers, but interviewees warn against complacency and recommend preparation for eventual rate increases. Under the circumstances, low rates and high core real estate prices lead investors to find the best risk-adjusted returns in the middle of the capital stack—mezzanine debt and preferred equity. Equity pipelines will have ample capital

from well-positioned, cash-rich REITs; yield-hungry pension funds; and foreign players parking money in safe North American havens. These investors will need to remain disciplined and sidestep risk outside of major markets, probably partnering with local operators who have an edge in ferreting out the best deals.

The industry must continue to grapple with unprecedented changes in tenant demand driven by technology and a relentless pursuit to temper costs in a less vibrant economy. Office users squeeze more people into less square footage, preferring green buildings with operating efficiencies, while retailers reduce store size in favor of various integrated e-commerce strategies. The large generation-Y demographic cohort orients away from the suburbs to more urban lifestyles, and these young adults willingly rent shoebox-sized apartment units as long as neighborhoods have enticing amenities with access to mass transit. And more intergenerational sharing of housing occurs to pool resources among children (seeking employment), their parents (reduced wages and benefits), and grandparents (limited pensions and savings).

Overall metro-area market ratings display significant improvement from 2012. Investors still show strong interest in top properties in primary coastal markets, as San Francisco, New York City, Boston, and Washington, D.C., remain in the top ten. However, inflated prices remain a top concern in those areas, with many investors starting to adjust their market investment strategies, showing increased interest in secondary markets as many chase tenants. Some of the top secondary cities mentioned include Austin, Houston, Seattle, Dallas, and Orange County, all in the top ten and most with significant increases in ratings. Improving prospects in cities like these are mostly driven by consistent job growth in strong, sustainable industries such as technology, health care, education, and energy. “American infill” locations offering walkability and strong transit systems continue to outshine the others. These locations offer advantages to the echo boomer generation, which in itself is a key demographic in the real estate investor's eye. Other metro areas scoring well include San Jose, Miami, Raleigh/Durham, Denver, San Diego, Charlotte, and Nashville.

In general, the economy should generate enough momentum to push greater leasing activ-

ity and increase occupancies. *Emerging Trends* respondents continue to favor apartments over all other sectors, although pricing has probably peaked and rent growth will subside in markets with an upsurge in multifamily development activity. Industrial properties and hotels will show the biggest improvement in 2013, and downtown office space in gateway markets also registers solid prospects, but power centers and suburban office space score the lowest marks for investment and development among survey respondents. Homebuilders will need to keep activity in check, but should gain confidence from stabilizing housing markets. Any uptick in single-family construction by 2014 and 2015 should buoy the overall economy and help other property sectors.

Canada will maintain its relative wealth island status, free of the debilitating government debt and credit market dislocation hamstringing most other countries. Its real estate markets enjoy a seemingly durable equilibrium, helped along by concerted investor discipline, lender controls, and government regulation motivated to ensure steady growth and dodge disagreeable corrections. Recently frothy condo markets in the nation's dominant cities take a breather even as the country's urbanization wave continues. Prices may level off or decline slightly for upper-end residences, but interviewees expect housing to circumvent any significant downturn, helped by ongoing immigration trends and a history of relatively stringent mortgage underwriting. Tight office markets in Toronto, Vancouver, and Calgary offer the opportunity for select office development projects, and U.S. retailers entering the country will help keep occupancies high in shopping centers. Apartment investments remain highly favored, and even hotels rebound from an anemic period. Canada's biggest concern focuses on the condition of the U.S., European, and Chinese economies; its prospects could suffer if other regions cannot boost their outlooks.

Latin America's growth track probably hits some speed bumps as its export markets slow down, but expanding middle-class populations in Brazil, Mexico, Colombia, and Peru offer significant opportunities to developers in for-sale housing, apartments, and shopping centers.

Notice to Readers

Emerging Trends in Real Estate®, a trends and forecast publication now in its 34th edition, is one of the most highly regarded and widely read forecast reports in the real estate industry. *Emerging Trends in Real Estate*® 2013, undertaken jointly by PwC and the Urban Land Institute, provides an outlook on real estate investment and development trends, real estate finance and capital markets, property sectors, metropolitan areas, and other real estate issues throughout the United States, Canada, and Latin America.

Emerging Trends in Real Estate® 2013 reflects the views of over 900 individuals who completed surveys or were interviewed as a part of the research process for this report. The views expressed herein, including all comments appearing in quotes, are obtained exclusively from these surveys and interviews and do not express the opinions of either PwC or ULI. Interviewees and survey participants represent a wide range of industry experts, including investors, fund managers, developers, property companies, lenders, brokers, advisers, and consultants. ULI and PwC researchers personally interviewed more than 325 individuals and survey responses were received from over 575 individuals, whose company affiliations are broken down here:

Private Property Company Investor or Developer	35.9%
Real Estate Service Firm	19.6%
Institutional/Equity Investor or Investment Manager	16.1%
Other	9.5%
Bank, Lender, or Securitized Lender	9.0%
Publicly Listed Property Company or Equity REIT	6.2%
Homebuilder or Residential Land Developer	3.6%

Throughout the publication, the views of interviewees and/or survey respondents have been presented as direct quotations from the participant without attribution to any particular participant. A list of the interview participants in this year's study appears at the end of this report. To all who helped, the Urban Land Institute and PwC extend sincere thanks for sharing valuable time and expertise. Without the involvement of these many individuals, this report would not have been possible.



Recovery Anchored in Uncertainty

“It’s three yards and a **a cloud of dust.**”

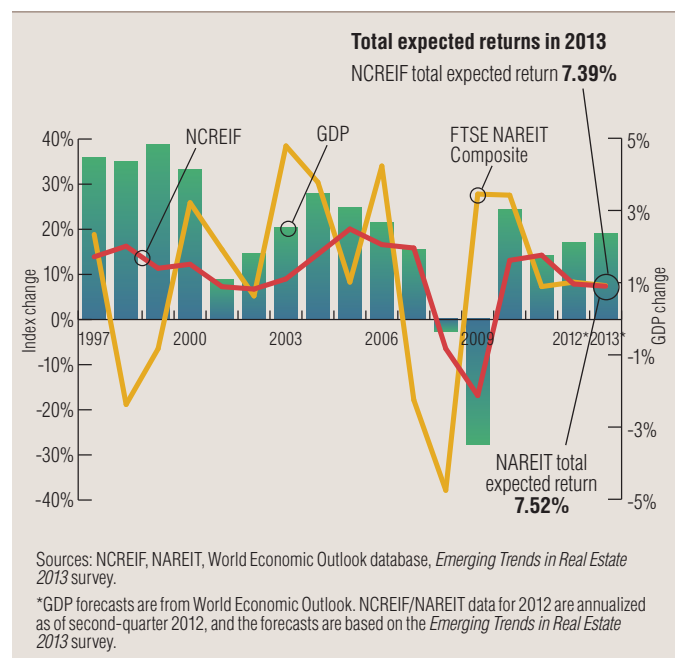
Real estate continues to meander along a slower-than-normal recovery track, behind a recuperating U.S. economy, dogged by ongoing world economic distress. But for the third-consecutive year, *Emerging Trends* surveys indicate that U.S. property sectors and markets will register noticeably improved prospects compared with the previous year, and the advances now gather some measure of momentum across virtually the entire country and in all property types. “Decent” though “relatively disappointing” job creation should be enough to coax absorption higher and nudge down vacancy rates in the office, industrial, and retail sectors, helped by “next to no” new supply in commercial markets. Robust demand for apartments holds up despite ramped-up new construction, and even the decimated housing sector “turns the corner” in most regions. Improving fundamentals eventually should prod rents and net operating incomes onto firmer upward trajectories, building confidence about sustained—albeit tame—growth and buttressing recent appreciation.

Although these gains seem modest and out of step with recent boom/bust cycles, restrained progress ultimately fits real estate’s income-oriented profile. Even though “it’s easy to be cynical: everybody seems to want what they can’t have” (“rent spikes,” “high yields with safety,” and “fully leased buildings”), interviewees seem to come to terms with the market’s “muddling-along pace,” expressing “cautious optimism” while abandoning hopes for “a big bounce.” Real estate’s “make-things-happen” entrepreneurs will stay “frustrated” and hamstrung in creating value—“the IRR [internal rate of return] model isn’t what it used to be”—but buying, holding, managing, and bumping up property revenues usually wins the real estate game. What’s that story about tortoises and hares? “We’re the

dull sister of the investment world; earning a 5 percent to 7 percent return is what we do best.”

Lingering doubters need to ease up just a bit: the world’s problems “actually benefit [U.S.] real estate, even though we don’t deserve it.” Low interest rates give the real estate industry breathing space, and money “pours in from overseas” seeking refuge. Real estate assets, meanwhile, continue to command

EXHIBIT 1-1
U.S. Real Estate Returns and Economic Growth



attractive spreads over fixed-income investments and offer considerably more stability than stocks.

Still, caution reasonably should rule decision making, given significantly greater potential for economic skids than any chance for an accelerating property market rebound. And chastened credit markets, still grappling with bloated portfolios of legacy problems, wisely and necessarily stick to reinstituted, rigorous underwriting standards. Although anxious investors feel more compelled “to chase yield” as core properties in the gateway markets reach for gulp-hard price points, “there’s no premium for taking risk” when Europe bounces from crisis to crisis, China ebbs into an export slowdown, and the United States delays in dealing with its own debt conundrum. In considering solutions, worrying about what will happen “is perfectly appropriate.” The “uncertainty” about global economics and government policy is “the industry’s biggest issue, because we

are so capital intensive, and it’s totally out of anyone’s control.” All the improving signs can appear “offset by the unknown,” weighing down sentiment.

This uncertainty may inhibit “exciting big-ticket projects” and constrict enthusiasm over scaled-down profitability compared with the precrash days, but the industry still can find plenty of roll-up-your-sleeves enterprises to bolster recently capital-starved properties and ensure enhanced future performance, including renovation, rehabilitation, repositioning, releasing, and refinancing. Successful players “continue to adapt”: what worked last year may not work next year. Tenants continue to shrink space requirements to improve efficiency, relying on technology rather than extra square feet. Office landlords should consider embracing flexible design features, green technologies, and Leadership in Energy and Environmental Design (LEED) systems or face the consequences. Obsolescent suburban office space now follows nearby left-for-dead regional malls into value-loss oblivion: many of these properties will be converted into something else over coming decades. Surviving shopping centers appear ripe for reinvention to integrate better with e-commerce and logistics supply chains, which continue their headlong transformation to accommodate less storage and more direct shipping to end users.

Promising signs of green shoots in desiccated and oversupplied housing markets should not tempt homebuilders into new projects too soon. But the potential for some measure of new housing construction over the next two to three years is real and would be a welcome boost for the economy and other real estate sectors.

Indeed, industry players must not lose sight of recent progress while steeling themselves for an ambiguous future, requiring new visions and tamped-down expectations. “We need patience.” Liquidity returns, but deleveraging takes much longer than expected, and weighty global problems will be a persistent drag. The world debt crisis took decades to create, the housing bubble followed 15 years of unimpeded growth, and the commercial real estate collapse derived from years of easy credit.

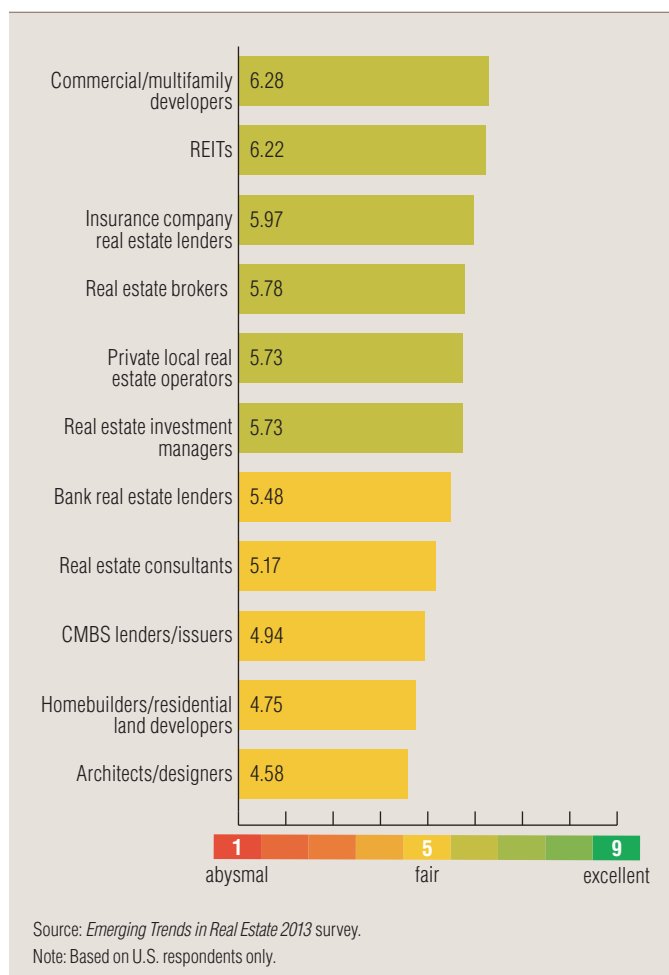
“It’s only reasonable [a full-blown] recovery will take more time”—a process less than firmly anchored in all that confounding uncertainty.

Emerging Trends: The Key Drivers for 2013

The following are the most important trends and issues that will affect U.S. real estate markets in 2013, according to an analysis of *Emerging Trends* interviews and surveys.

EXHIBIT 1-2

Real Estate Business Prospects for 2013



Chasing Yield: Not Enough Product for Prudent Investment

As investors tentatively advance further along the risk spectrum in 2013 chasing yield, they suffer queasiness about the limitations of U.S. real estate markets: there is just “not enough product” to get the yields they want. Core real estate seems overpriced: plowing money into top properties at sub-5 percent cap rates looks unproductive, especially if and when interest rates “inevitably” go up. “It’s not the smartest thing to do” and “could get ugly out there,” except for buyers and long-term holders of the best properties in the best locations. The number of truly trophy assets remains somewhat static: typical markets can sustain only so many fortress malls or Class A office buildings as prime tenants shrink space requirements and willingly play leasing musical chairs. Many lodestar properties become irreplaceable holds unless managers undertake transactions for fees where they can command top dollar.

No one can count on tenant demand to boost the prospects significantly for the surfeit of below-prime commercial real estate, and the highly favored apartment sector borders on overheated in some places with development well underway. In the current recovery, asset managers already teeter on “a high wire,” “feeling pressure from clients to put money out” but not finding “prudent yields” in underwriting future rents on these more commodity, B and C class properties. Banks, institutional investors, and real estate investment trusts (REITs) “spin out” more Class B and C product they want off their books, trying to entice bites from the unsated equity capital wave, straining to maintain underwriting discipline. “Watch for assumption creep: buying at 9 percent or 10 percent cap rates might make sense, but at 7 percent or 8 percent in these markets, there could be a problem when you want to exit.” In the right management and leasing hands, some of these vanilla properties may throw off decent income returns, but realizing much appreciation seems like a stretch.

And can anyone find a lender to help leverage performance on these “higher beta” properties? It may become somewhat easier in 2013, but not much, given rationally tight financing standards. What is the advantage for bankers in taking outsized chances when their portfolios continue working off legacy problems?

Traders always get in trouble when they price real estate “as a commodity.” And that is the ongoing issue for today’s chastened buyers: too much product looks no better than that—commodity.

EXHIBIT 1-3

Investment Prospects by Asset Class for 2013



Localization and the Move into Secondary Markets

Money slowly wends its way beyond the highly favored global gateways into “long-neglected” secondary markets where “tighter pricing will be a true trend in 2013.” Investors “concentrate on higher-quality assets” in “search of higher rates of return,” but pickings are relatively slim. “You need much more compelling reasons to go into secondary and tertiary markets, focusing on niches” and particular local strong suits.

For the big institutional investors, venturing out of the top-ten major markets where they have concentrated their activity “can be filling but not very satisfying”—historically return expectations do not always pan out, and exit strategies prove more difficult to execute. Because they have eliminated most regional staffing, the major money management advisers and investment banks typically lack the depth and reach to understand internally the idiosyncrasies of most medium-sized and smaller metropolitan areas. And smaller investment companies mostly rely on third-party research reports. As they move farther afield in 2013 hunting for yield, these investors must depend on local operating partners to make wise investment calls in addition to managing and leasing decisions, or they risk major stumbles.

Expected stepped-up institutional activity aside, second- and third-tier markets increasingly “become the province” of local high-net-worth operators, supported by regional and local bank capital. “It’s happening, but you don’t hear about it.” The locals “look at the micro” (tenant moves and market drivers); “nobody is talking about the macro” (the global economy). They “take more risks,” “buy at low bases,” “invest more of their own money,” and they are willing to bet on their communities for the long term rather than focus on some unachievable short-term investment return for investors who may never set foot in town. “These are more buy-and-hold, get-rich-slow investors.”

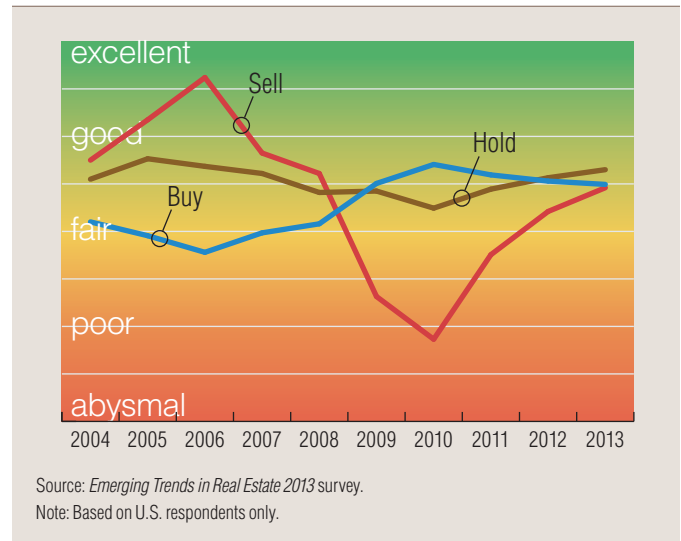
Restrained absorption and lack of tenant depth in many of these markets will force locals to think out of the box and about change of use. Outside of a handful of tech- or energy-dominated markets, “they cannot expect much growth.”

Transaction Volume Will Tick Up

Forlorn deal makers find hints of more action in 2013. Pricing continues to strengthen, but increases are “muted” until credit markets return to more normal states and transaction volume stays relatively “anemic.” The *Emerging Trends* barometer reflects lack of clear market direction. Buy/hold/sell sentiment continues to track in a narrowing range with purchase appetites losing some vim in the face of higher prices, while selling interest increases for the same reason (exhibit 1-4). Without pressure from lenders, “truculent” owner/borrowers continue to hold out for “top dollar”

EXHIBIT 1-4

Emerging Trends Barometer 2013



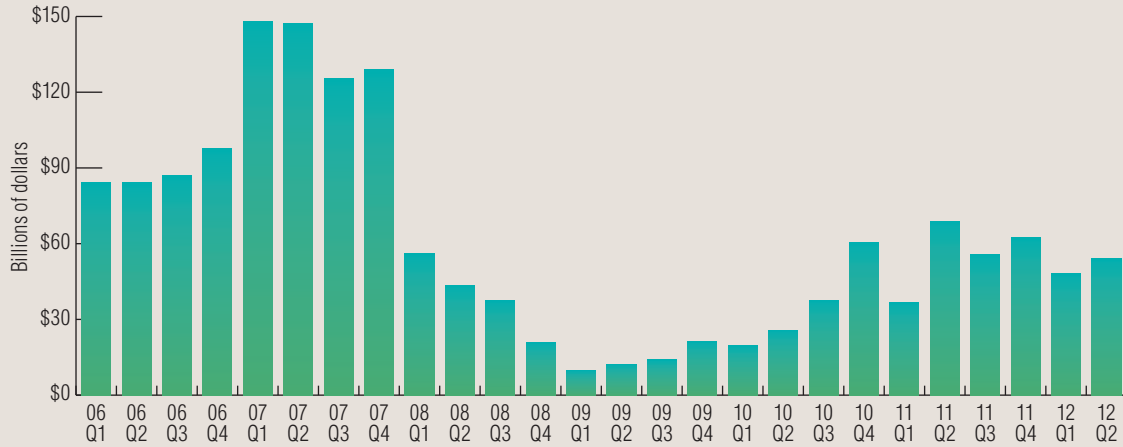
while investors expect bargains. Intensified bank balance sheet clearing should “provide [more] opportunities for well-capitalized” buyers, but “very little will be available in institutional-class real estate.” “If you don’t have to sell, it’s better to hold,” although hungry investors will pay above replacement cost for pricey, well-leased core properties. Those buyers will have no choice except “to sit on [these acquisitions] for a while. Conditions aren’t right for flipping, and there will be no easy plays.” Action picks up in \$20 million-and-under properties located in suburbs and second-tier markets “as long as the income is there.”

Perplexing Interest Rates: “the Biggest Risk”

Many real estate players wonder if they have been lulled into complacency after consistently predicting wrongly in *Emerging Trends* for most of the past decade an increase in interest rates over a five-year time horizon and perfunctorily doing so again in this year’s survey (exhibit 1-7). Lurking ominously in their future, rates must begin to revert to the mean, and cap rates will eventually follow. “How long can they stay down?” But the low-growth economy forces the Federal Reserve to print money and keeps rates at unprecedented low levels, probably at least through 2015. And rock-bottom rates continue to be a boon for real estate, providing exceptionally low and attractive financing for borrowers with good credit at a time of a huge refinancing surge in commercial mortgage-backed securities—“it makes the tidal wave less serious”—in addition to turning properties into a more compelling investment relative to fixed-income vehicles. “It’s

EXHIBIT 1-5

Sales of Large Commercial Properties



Source: Real Capital Analytics.

Note: Includes transactions in the Americas for properties \$10 million or greater.

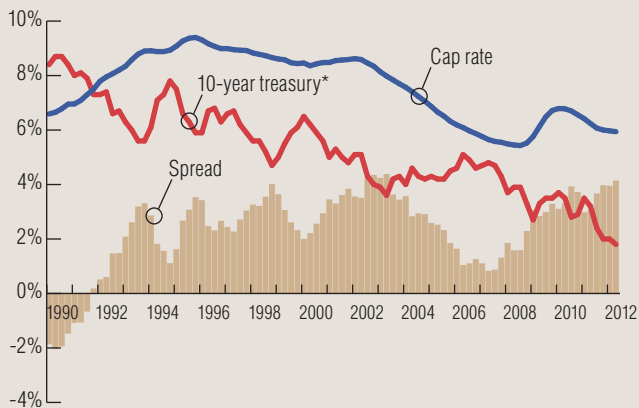
the most important trend—changing the investment environment with different rate-of-return expectations.” Asset pricing is “modest; repricing debt is where funds will go. A 4 percent to 5 percent mortgage is a pretty good deal, relieves owners with cash flow issues, and provides a decent return for lenders.”

As more investors inevitably chase yields in secondary markets during 2013, doubts about where rates are headed

perplex interviewees, especially in view of ballooning government deficits. They prefer to think any increases “could be four or five years out: just look at Japan” where rates have remained in the cellar for close to two decades (along, not coincidentally, with the Japanese economy). But how long can the Fed keep buying up treasuries when other investors back off because of low returns and U.S. debt issues? And what happens if some

EXHIBIT 1-6

NCREIF Cap Rates vs. U.S. Ten-Year Treasury Yields

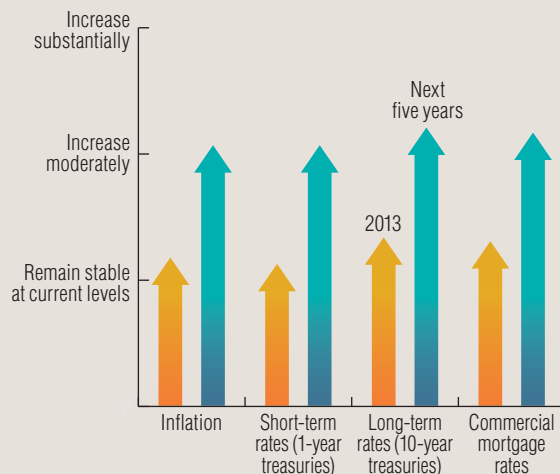


Sources: NCREIF, Moody's Economy.com, Federal Reserve Board, PricewaterhouseCoopers LLP.

*Ten-year treasury yields based on average of the quarter; 2012 Q2 average is as of July 31, 2012.

EXHIBIT 1-7

Inflation and Interest Rate Changes



Source: *Emerging Trends in Real Estate 2013* survey.

Note: Based on U.S. respondents only.

exogenous event occurs to force rates up? Can anyone be sure the Fed is the master of holding down rates indefinitely? “We’ve been living off artificially managed cheap debt when we really need demand and rental growth. Any crisis in confidence about the United States, and interest rates on treasuries could escalate,” notes an interviewee. Simply, normalizing rates “are the biggest risk” to the industry.

If rates increase suddenly, many borrowers “will be disintermediated, unable to refinance unless property income has grown sufficiently to support value and repayment of an existing mortgage.” And investors would be wise not to assume exit cap rates based on today’s low interest rate levels. “It could bite us.” Investors should lock in low mortgage rates, assume long-term mortgages, and hedge against rising T-bill rates. “It’s tempting to stay short because there is so little cost, but this will not last.”

While interest rates remain collapsed, inflation stays under control mostly because of high unemployment, low wage growth, deleveraging, and a resulting lack of pricing power. “We continue to buy time, but don’t seem to be making much progress.” Many real estate pros would like to see inflation increase, boosting net operating incomes and hard asset values while helping them eliminate the burden of their mortgage and cash flow constraints. “That’s probably the only way out of the debt problems.” The “sweet spot” scenario holds for some inflation and continuing low financing rates; “it’s hard to mess up if you have good assets.”

Overbuilding Multifamily?

Developers rush into multifamily, the only sector where demand “of historical proportions” and undersupply combine to justify new construction. Lender interest and low borrowing rates (including from Fannie Mae and Freddie Mac) facilitate project financing to leverage returns, and plunging cap rates on existing apartments give developers a positive spread. Smart developers who bought and entitled land at the recent market bottom really score. Bullish players forecast continued upward pressure on rents from the eventual release of pent-up demand from generation Yers living with parents; many will find jobs and move out on their own. In addition, tens of thousands of apartments demolished each year will need replacing.

But some interviewees raise cautionary notes and contend “it’s time to start shutting down” the construction pipeline. “There’s much more development coming on than people are admitting. They also ponder all the funds investing in single-family housing, which will add to rental supply and compete against apartments. Clearly, hidden inventory exists that people aren’t focusing on.” Other nervous Nellies point to office developers shifting into the apartment space, “because they can get financing.” “It’s hard to keep discipline and prevent overbuilding.”

Cooler heads distinguish between infill markets with few developable sites, especially near mass transit stops, and traditional hot growth areas where new commodity, garden-style product can mushroom and often overshoot demand. “You see too much construction in easy-to-build markets. Construction is needed where you have a 2 percent vacancy rate and it’s hard to build.” At the very least, multifamily development will “change the tilt of the game board, moderating growth in rents and ultimately returns.” When rent increases become tempered and construction prices increase, developers will start to back off. “You don’t want to play the game too long.”

For the longer term, gen-Yers may not want to live in apartments indefinitely: “They will move back to the ‘burbs with the backyard and dog, renting since they may not be able to buy. NOI [net operating income] growth in apartments could tail off.”

Housing Resuscitation: Lifting Other Sectors

Battered homebuilders finally may register a pulse in 2013. Most interviewees expect a long, hard slog to recovery for the U.S. housing industry, but prices increase in more areas, the foreclosure process begins to be resolved in earnest, and institutional investors help firm up markets by buying inventory. At some point, the sheer force of the expanding population (at 2 million to 3 million annually) will create demand for single-family homes, and any upsurge in housing will likely ripple positively through the rest of the real estate industry and the entire economy. Homebuyers may then head to shopping centers to furnish and appoint their houses, and distribution facilities will need to support increased movement of goods. Suburban office markets could benefit, too: mortgage and sales brokers, title companies, and construction firms will all need to expand as lawyers and appraisers could also get a boost. Marginal improvements in 2013 set the course for better days ahead.

Playing It Safe

The unprecedented global financial dislocation prolongs an unwelcome hunkering down. “Everybody is operating on yellow and red flashing lights,” and “managing risk and selectivity will be the key to any success.” Entrepreneurial tendencies remain mostly harnessed amid conditions borne of debt-related “drift” and “uncertainty.” This means investors cluster in the world’s perceived safest markets—the United States and Canada are at or near the top of their lists—and shun other places. Lenders continue to open doors for their highest-credit clients but place hurdles in front of other borrowers. With a few exceptions in the handful of 24-hour cities and energy/tech markets, developers cannot make a case for construction loans; only multifamily

builders manage to line up financing. Retail tenants want into Class A malls and leave second-class centers, while just about everyone avoids half-empty strips and office parks. Interviewees expect little relief from evident market “bifurcation” “until the economy recovers,” and most resign themselves anxiously to “no huge change.”

Getting a Grip on Return Expectations: Debt Beats Equity

“I roll my eyes if a manager claims he can get more than a 15 percent annualized return” on a commercial real estate fund, says an interviewee. “They’re picking numbers to try to meet the market.” Such optimistic—bordering on fanciful—projections cannot play out in the current environment “without a lot of leverage [hard to come by] and a lot more [downside] risk.” Individual investments may pan out, but added value and opportunistic returns pegged to precrash-era expectations just do not appear viable, and that is bad news for all the general partners and high-growth managers trying to resurrect their fund management businesses and earn generous promotes off their optimistic appreciation scenarios. “Getting used to less can take a long time.”

If they have not already, real estate players reorient to reality, understanding what property investments are built to deliver. “Remember, over time three-quarters of real estate returns derive from income, only one-quarter from value gains.” Any return in the 6 to 10 percent range looks particularly attractive in 2013 when compared to interest rates and inflation, not

to mention against stocks and bonds, and well-leased real estate should produce those levels of returns for the next several years (exhibit 1-8). “It’s the best horse in the glue factory.”

As deleveraging and refinancing continue to “suck up a lot of capital,” at least through mid-decade, yield expectations are changing, and real estate looks more like “the income vehicle” it was meant to be. Within the capital stack, debt investments should earn better risk-adjusted returns than equity, thanks to significant loan-to-value ratios and realistic valuations that combine to provide excellent downside protection. Smart lenders “should not depend on a lot of growth and [should] underwrite based on current fundamentals.”

Operating in a Slow-Growth Environment: Decent Profitability

Like other businesses, real estate firms boost profitability at the margins by keeping lean, and *Emerging Trends* respondents anticipate 2013 will be a reasonably good year for bottom lines (exhibit 1-9). “Staffing-wise they’re doing nothing” after cutting back a bit; incomes inch back toward 2007 levels. Better-capitalized firms should continue to gain market share at the expense of other failing companies, but “the overall size of the industry will not change.” Compensation relative to the 2007 peak remains “more modest.” Only a select number of investment managers secure “equity programs that will pop value” after “a lot of equity washed out.” Compensation is no longer determined by peer-group comparisons but by individual company profitability, with cash awards approaching about 70 percent of peak levels and equity opportunities offering only about 50 percent. “Everything had been out of balance.”

Top leasing and property management executives get paid premiums for keeping buildings filled and finding ways to reduce operating costs. Proven marketing professionals who can raise capital also remain in high demand, given ravenous competition for skittish client dollars. Deal makers continue to suffer in lackluster transaction climes and freshly minted MBA job seekers will have better success with some past bricks-and-mortar credentials. Office developers shift into apartments, and homebuilders gear up for new activity, but in a slow-growth mode. “It’s not very exciting.”

More CEOs keep themselves up at night figuring out scenario planning, and many executive teams add risk strategists to prepare for potential bolt-out-of-the-blue crises. Cushioning against problems takes precedence over ambitious new ventures. At the same time, changing demographics, “Era of Less” realities, and technology effects force developers and operators to do business differently in meeting altered demand trends. From retail and warehouse to office and apartments,

EXHIBIT 1-8
Index Returns: Real Estate vs. Stocks/Bonds

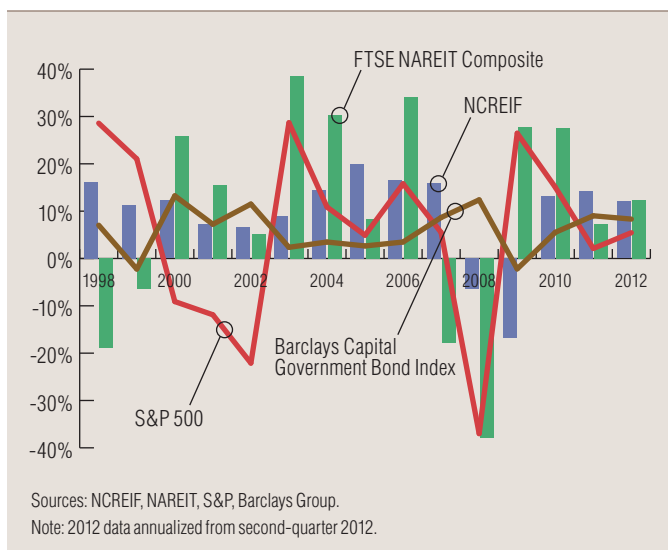
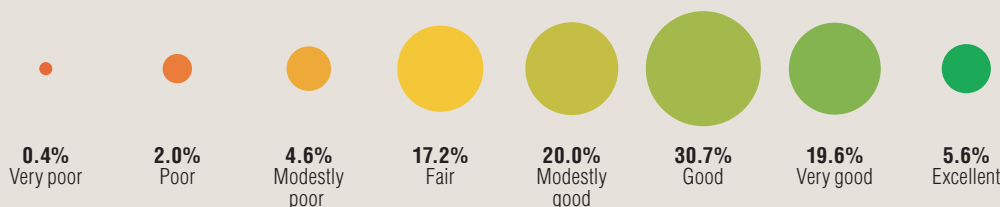


EXHIBIT 1-9

Firm Profitability Forecast 2013

Prospects for Profitability in 2013 by Percentage of Respondents

Source: *Emerging Trends in Real Estate 2013* survey.

Note: Based on U.S. respondents only.

tenants do not necessarily settle for old-school layouts and designs. Understanding and “staying close to the customer” becomes more important than ever.

Evolving and Ongoing Trends

Technology, Job Growth, and Reduced Demand

Emerging Trends interviewees remain flummoxed about job growth and give up on reflexive optimism about how the U.S. economy always finds its way.

Some pockets of high-quality job growth do exist in energy markets where the natural gas boom and upward-trending oil prices lift prospects, the familiar high-tech bastions, and “eds and meds” corridors around hospital centers and near major education institutions. Anyplace offering a combination of these employment drivers and attracting a highly educated workforce, including the global gateways, positions itself relatively well at least for the near to medium term. Also, “don’t count out” financial centers (with greater regulatory certainty, banking institutions can stabilize), and manufacturing “makes a comeback.”

Aside from the few bright spots, the overall jobs outlook appears chronically “sluggish,” hindered in part by recent government cuts and the comatose construction industry. A majority of new jobs created in the recovery are low paying, a continuation of the longer-term national trend of decreasing wages and benefits. Interviewees increasingly place more blame on technology-related productivity gains, which also shrink tenant space requirements in a painful double whammy, keeping vacancies higher than desirable in commercial real estate.

On the office front, companies shoehorn employees into less space—workbenches replace cubicles—and let more people work from home (avoiding commuting time and expenses) or out of the office with their laptops and smartphones in tow, reducing rents and operating expenses. Businesses relying on wi-fi can slash space once needed for filing cabinets, computer hardware, and credenzas—all that paper stuffed into manila folders evaporates into data clouds—as fretting office landlords just hope they can renew leases somewhere close to existing square-footage requirements. Web-embracing retailers, meanwhile, “kick in” internet selling strategies that dovetail with liberally shrinking store sizes and inventories, which also means they hire fewer store clerks. Fortress malls may stay full, but lesser retail locations lose tenants and value.

“It’s an eye-opener what’s happening to the workplace and shopping habits”; “technology has gone from experimental to here to stay.” Or put another way, interviewees contend constrained job growth and reduced space per capita look like prolonged realities.

Compactness

People and businesses seek smaller spaces. They realize they do not need as much room to live and work, and want to reduce rents and operating expenses as they deleverage or try to enhance bottom lines in the less-than-robust economy. Gen-Y career builders forsake suburban lifestyles and willingly move into “shoebox”-sized city apartments; nearby public amenities like retail districts and parks can make up for the lack of personal space. In the “Waltons effect,” more grandparents, parents, and young-adult offspring live together to pool resources; they each put up with less personal room, too. Companies gravitate to flexible office layouts, which facilitate cramming staff into smaller work areas, and retailers rely on smaller store formats, selling more products through web-based channels. For

real estate owners, the move to less means slackened overall demand growth, whereas homebuilders and apartment developers need to consider new, more efficient models and related amenities (wi-fi is a must) for projects.

Shortfalls in municipal budgets—from increasing pension costs, reduced federal aid, and resistance to higher taxes—forces local officials to come to terms with the economics of planning schemes and zoning. In retrospect, sprawl has turned into a loser for many suburbs; officials begin to realize how denser development generates greater revenues at lower per capita infrastructure costs. The realization finally dawns that “creating something high quality and compact produces a greater yield for any land asset.” Sewer lines and roads servicing sprawling subdivisions, originally subsidized decades ago by the then-more-revenue-rich federal and state governments, now require extensive upgrades or replacements as they approach the end of their life cycles. But insufficient local tax revenues from single-family homeowners will not cover the repair bills in most cases, and cash-strapped states and the feds just do not have enough funds to help out.

Unprecedented Transformation in Tenant Demand

Never before has the real estate industry been so whipsawed by such rapid transformation in tenant requirements. Whereas only a few years ago, office users placed a premium on scale and quality, today they want space that can “provide efficiency” and “encourage productivity.” Practicality and collaborative environments in open-space plans make more compelling brand statements than marble finishes and skyscraper views as flexibility and ease in moving teams within layouts take precedence over boardroom amenities and corner offices. “CEOs get compensated for cutting costs, not expanding,” and their corporate real estate underlings get the message “about figuring out ways to use less real estate.” Tellingly, even some white-shoe law firms lose windowed offices and adopt more functional space schemes.

Everybody caters to echo boomer tastes: “their sheer size deserves attention and can’t be underestimated.” These multi-tasking younger professionals crave interconnectedness and mobility, value the most up-to-date communications devices so they can operate from just about anywhere, and downplay physical space as well as privacy; for them social cacophony can be energizing. They also favor green amenities. If they must work in close quarters, they want more fresh air and natural light, and they like the idea of working in cutting-edge buildings that manage energy loads to reduce environmental impacts. For now and at least until they start families, proximity to stimulating urban action—living and working within reasonable distances and using mass transit—holds more attraction for the 20-

something crowd than spending time and money commuting by car to quiet suburban lanes. Apartment developers home in on echo boomers’ socialization penchant; they can build smaller units if they supply wi-fi and provide common space like roof decks or event rooms for texting-inspired get-togethers.

The housing bust may not have destroyed homeownership dreams, but more people across the age spectrum now feel greater peace of mind renting while many others have no other choice; saddled by bad credit or lacking enough equity, they cannot afford to buy. The renter surge extends well beyond multifamily and back into suburban single-family residential neighborhoods.

Adapting the ‘Burbs

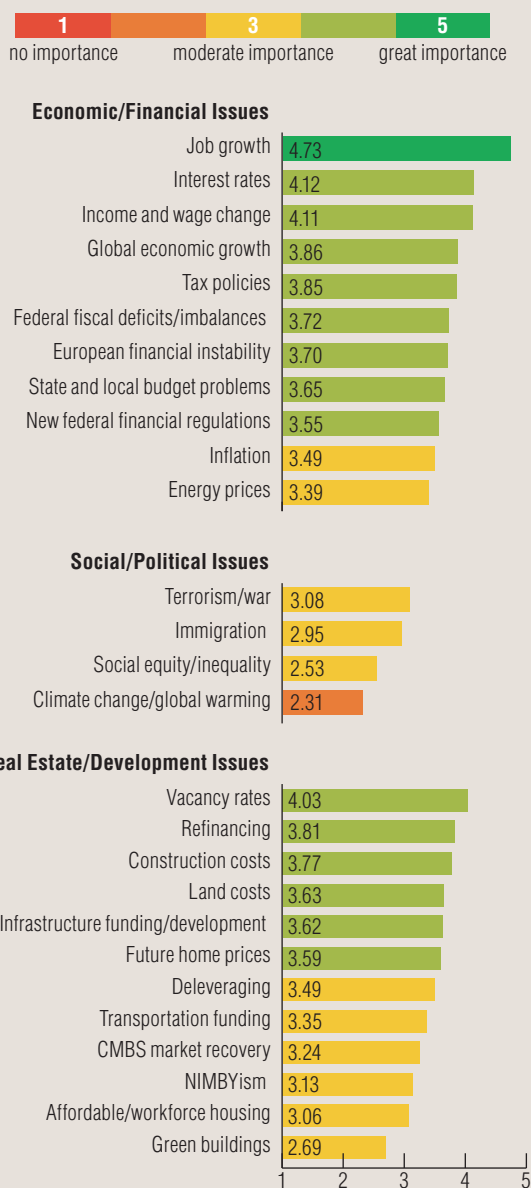
The world “rethinks the suburbs” in the wake of population gains in the major gateway markets and growth in urbanizing suburban nodes at the expense of fringe areas. “It’s a secular trend driven by where many young people want to live,” and it will have a “very material impact on how real estate is used.” Some “biotech and pharmaceutical companies break up their suburban campuses and move back into cities because they can’t convince PhDs to go to the suburbs.”

Despite “suburban office: who wants it!” scorn, “everyone isn’t going back to the cities,” and aside from the prominent 24-hour meccas, many long-forsaken downtowns continue to struggle. The majority of Americans, meanwhile, still live outside urban cores or in suburban agglomerations. But developers and investors need to realize future success may rest in identifying prime locations suitable for densification in suburbs and linking into transit-oriented hubs as more communities seek car alternatives to relieve traffic congestion “and avoid choking to death.” “Anything near suburban rail is gold. We’re seeing superior rent growth compared to buildings away from light rail; it’s no longer hypothetical.”

Separating land uses from each other—housing, retail strips, office campuses and regional malls—loses traction to more compact development with mixed-use, urban concepts. Many suburban parcels stand ready for makeovers—whether a ghost mall, an empty formerly grocery-anchored neighborhood center, or that nearly vacant office park or low-density business park.

Under any circumstances, investors wisely bet on infill, especially around the 24-hour cities where most of the nation’s economic activity concentrates. The housing crisis pushes more families into apartments from houses, spurring suburban multifamily projects. Real rental growth and population gains occur “on a more broad-based level” in the major metropolitan areas and urbanizing suburbs embedded around them. The localized exceptions occur where urban gentrification effectively transfers endemic poverty into inner-ring suburbs.

EXHIBIT 1-10

2013 Issues of Importance for Real EstateSource: *Emerging Trends in Real Estate 2013* survey.

Best Bets 2013

Emerging Plays

These investment and development sentiments from *Emerging Trends* interviewees deserve particular attention in 2013.

Concentrate acquisitions on budding infill locations. Top 24-hour urban markets outperform the average, bolstered by move-back-in trends and gen-Y appeal. But the top core districts in these cities have become too pricey. "Find buildings where tenants want to be," typically in districts where hip residential neighborhoods meet commercial areas and "not necessarily the top, most expensive buildings." "You can't get enough of anything near mass transit stations," especially apartments.

Construct new-wave office and build to core in 24-hour markets. Major tenants willingly pay high rents in return for more efficient design layouts and lower operating costs in LEED-rated, green projects. These new buildings can lure tenants out of last-generation "brown" product. Other build-to-core gambits will work, too. "Better to develop at a seven cap rate than buy an existing building at a five." Completed medical office and apartments should sell at nice spreads into ever-present capital demand. Rental apartment projects provide solid income with the potential for future condominium conversions.

Develop select industrial facilities in major hub distribution centers near ports and international airports. In these markets, "the industrial sector is where the apartment sector was two years ago," driven by tremendous demand by large-scale users looking for specialized space and build-to-suit activity.

Use caution investing in secondary and tertiary cities.

Focus on income-generating properties, and partner with local operators who understand tenant trends and can leverage their relationships. If you feel uneasy about overpaying, listen to your gut and back off. Markets grounded in energy and high-tech industries show the most near-term promise (but can be volatile), while places anchored by major education and medical institutions should perform better over time. Leading secondary markets include Austin, Charlotte, Nashville, Raleigh-Durham, and San Jose.

Begin to back off apartment development in low-barrier-to-entry markets. These places tend to overbuild quickly, softening rent growth potential and occupancy levels probably by 2014 or 2015.

Consider single-family housing funds. Housing markets finally limp off bottom, and major private capital investors make a move into the sector. Concentrate investments with local players who know their markets and can manage day-to-day

property and leasing issues. Be prepared to wait a while before rentals can be converted into a revived sales market. In the meantime, investors should earn good income returns.

Repurpose the surfeit of obsolescent properties. Whether abandoned malls, vacant strip centers, past-their-prime office parks, or low-ceilinged warehouses, a surfeit of properties requires a rethink, a teardown, and in many cases a new use. Creative planners and developers have myriad opportunities to reconsider how sites can tie into future growth tracks and integrate into more efficient and desirable models. Many capital-depleted hotels are ripe for renovations, too.

Enduring Favorites

These investment bets have been highlighted in recent *Emerging Trends* reports and continue to be among interviewees' leading recommendations for 2013.

Recapitalize well-leased, good-quality assets, owned by overleveraged borrowers, who are upside down financially. This ongoing "feast of opportunities" has plenty of legs because banks continue to engage in "extend and pretend" loan strategies as more mortgages reach their maturities. "Lots of real estate has income-generation potential but has been compromised by distressed capital structures." "Look for distressed borrowers, not distressed properties." Mezzanine debt and preferred equity positions will offer particularly good risk-adjusted returns.

Lock in long-term, low-interest-rate mortgage debt. Why tempt the inevitable? "There's no way the low-interest-rate environment lasts," and your low-rate mortgage could be "a huge future asset" as soon as interest rates begin to pop. The surge in mortgage maturities seems perfectly timed for some struggling borrowers who may be able to refinance at lower costs. Back off floating-rate debt before you look stupid. The Fed cannot keep printing money forever.

Hold core properties in 24-hour cities. Whether office towers, prime hotels, apartments, or skyscraper condominiums, pricing tests limits, and these markets either have peaked temporarily or could level off for a while. But premier assets should continue to outperform over time; if sold, how would you replace them? Boston, New York City, San Francisco, and Washington, D.C., can come off the boil, but they always stay near or at the top of investor lists. The Bay Area reaches the *Emerging Trends* ranking pinnacle for 2013.

Buy or hold public REITs. Given their dividends and embedded growth, these stocks should continue to perform well. Focus on sector-dominating companies that have assembled blue-chip portfolios of the best income-producing assets in

multifamily housing, regional malls, strip centers, office buildings, and distribution facilities.

Buy nonperforming loans, and work out discounted payoffs from borrowers. Banks and special servicers tend to shed mortgages on weaker assets, "but you can hit a lot of singles and doubles" at the right price.



Real Estate Capital Flows

“Plenty of capital is available
for people who can earn it.”

For 2013, the real estate capital markets throw off confusing, mixed signals amid significant pent-up investor demand, sluggish but mending fundamentals, and low interest rates, as lenders continue to hold on to a slew of underperforming loans in a glacial deleveraging and hundreds of billions of commercial mortgages reach maturities. Four years after the cyclical bottom, “many markets have not been allowed to clear and prices have not been reset,” except in the dominant 24-hour cities and a handful of tech and energy regions.

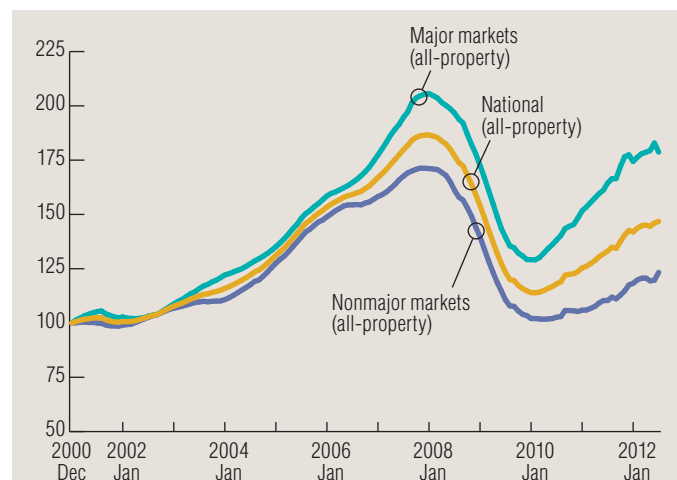
Expectations for returns decrease on paper, but investors still push for higher yields than may be possible or reasonable, especially given the insipid economy and ongoing political intransigence. “It’s easy to get ahead of yourself, and some [investors] will lose control of discipline.” “A crazy search for yield” in a low-interest-rate environment leads some interviewees to argue that sub-5 percent cap rate purchases are rational given spreads to treasuries. But they ignore what may happen to exit cap rates when interest rates inevitably increase, as well as the extremely checkered and unhappy history of compressed cap rate purchases in past market cycles. *Emerging Trends* survey respondents predict a moderate oversupply of equity capital and a moderate undersupply of debt capital during the year (exhibit 2-2).

Inevitably in a measured recovery more equity capital will creep into the higher-cap-rate strata—riskier secondary markets and lower-quality assets—unable to stomach high pricing and minimal yields in core real estate. But the prime gateway markets will continue to benefit from increased flows from foreign investors looking for secure wealth islands to protect assets.

In the debt markets, it will be “more of the same”—good assets with solid income streams and good credit borrowers will

have no trouble attracting financing from life insurers and banks eager to choose from the pick of the litter. As markets improve, more properties will enter this worry-free zone, and rich-can-get-richer mortgagors easily lock in “exceptionally cheap money.” But players with bad credit and/or marginal assets, who need capital infusions to keep afloat, continue to find themselves cast aside or placed in extend-and-pretend limbo. “It’s still the

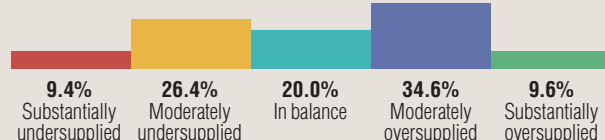
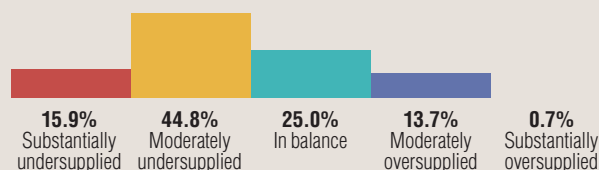
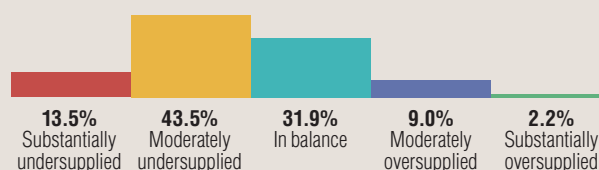
EXHIBIT 2-1
Moody’s/RCA Commercial Property Price Index



Sources: Moody's and Real Capital Analytics.

Notes: Major markets are defined here as Boston, Chicago, Los Angeles, San Francisco, New York, and Washington, D.C. The Moody's/RCA CPPI is based on repeat-sales transactions that occurred at any time up through the month before the current report. Updated August 2012; data through June 2012.

EXHIBIT 2-2

Real Estate Capital Market Balance Forecast for 2013**Equity Capital for Investing****Debt Capital for Acquisitions****Debt Capital for Refinancing**Source: *Emerging Trends in Real Estate 2013* survey.

Note: Based on U.S. respondents only.

best—and all the rest.” According to *Emerging Trends* respondents, stringent underwriting standards will harden into practice in 2013: more than 80 percent say tough loan terms will stay the same or become even more rigorous (exhibit 2-3).

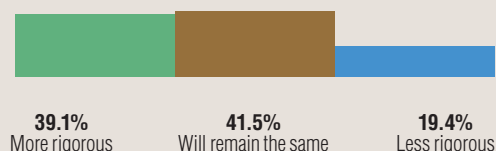
Compromised CMBS issuers stagger back, unable to offer much help to their formerly bread-and-butter Class B and C-asset borrowers; the securitized debt markets still “look like a question mark” and show few signs of reclaiming much more market share in 2013. Most leftover CMBS quandaries remain unresolved from the crash: “They had lowered costs and spread risk tolerances around, but bond investors didn’t know what they were buying and the underwriting and risks were not clearly understood. None of that has been rectified yet,” an interviewee said.

Complicating matters, the estimated \$300 billion of refinancing required for maturing loans over each of the next three years will decrease lenders’ ability to write new commercial mortgages and force a continuation of extend-and-pretend strategies on existing debt. Lenders also remain extremely disciplined about commercial construction lending: developers “have an easier time finding equity investors” than financing.

Further clouding analysis, the metrics of risk-adjusted investments get turned somewhat on their heads: usually safe senior debt yields fall toward uncomfortably low levels for lenders with an eye on future interest rate moves. At the same time, low yields for core real estate pricing look less appealing than the risk-adjusted returns for the mezzanine debt and preferred equity. Effectively, investors in these middle-of-the-capital-stack tranches can obtain “a higher-than-equity cap rate with higher cash-on-cash returns and lower risk.” Interviewees expect the pricing differential to narrow between senior and mezzanine debt during 2013.

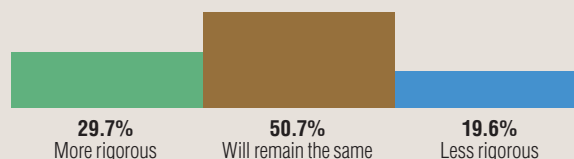
Under any circumstances, real estate attracts the attention of enough—that is, considerable—capital activity, which helps deleverage fractured legacy investments and move markets in the direction of regaining equilibrium. Financial-institution balance sheets “avoid taking hits,” and low interest rates help preserve capital and encourage a deliberate, if admittedly protracted recovery. Frustration about limited opportunities and lowering returns logically should be tempered by evident investor appeal for the asset class as an income generator and potential inflation hedge. Why else would so much capital prop it up? Simply, U.S. real estate, properly underwritten, remains as good a place as any for husbanding assets in an unsettled world.

EXHIBIT 2-3

Debt Underwriting Standards Forecast for the United StatesSource: *Emerging Trends in Real Estate 2013* survey.

Note: Based on U.S. respondents only.

EXHIBIT 2-4

Equity Underwriting Standards Forecast for the United StatesSource: *Emerging Trends in Real Estate 2013* survey.

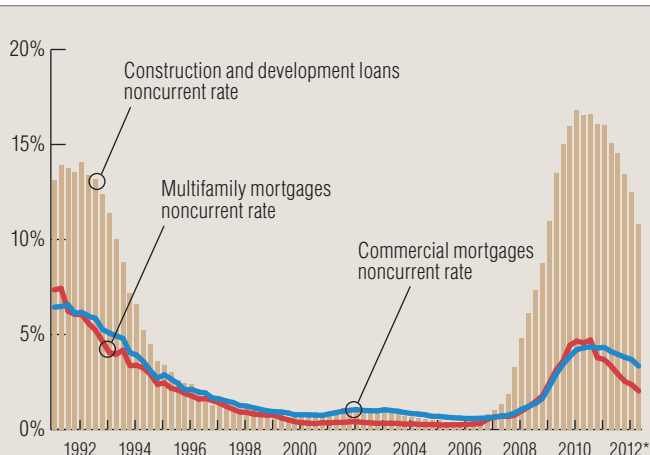
Note: Based on U.S. respondents only.

Banks Will Bide Their Time

The take-it-gently deleveraging beat goes on. Buyers wait aimlessly for banks to shed commercial property assets at cheap prices; banks maintain a slew of problem assets on their books while values ratchet slowly up, reducing their potential losses; borrowers with sterling credit have no problem securing financing; troubled borrowers who need refinancing capital most of all get the cold-shoulder treatment or, more likely, receive an extend-and-pretend pass; and Federal Reserve-engineered low interest rates “save everyone.” The kabuki theater performance plays out ever so slowly with no one sure exactly what’s happening in the bowels of these financial institutions. But more than four years after Lehman, banks apparently have not bolstered their balance sheets enough to clear the market, or the government wants them to hold back (in the case of home foreclosures especially) for fear of shocking prices into a further decline—a politically and economically risky bet. As a result, banks feel “no intense pressure” to do much of anything: many mortgages even on underwater assets may be among “their highest-yielding assets.” As long as loans are current, lenders are better off to extend than sell loans at discounts, foreclose and recognize losses when markets have further room to improve, or refinance at lower rates. Under the circumstances, the same beat essentially goes on for another year at least, although bankers selectively will dribble “a little more from inventory” onto the market “and take some additional [manageable] hits.”

EXHIBIT 2-5

Bank Real Estate Loan Delinquency Rates



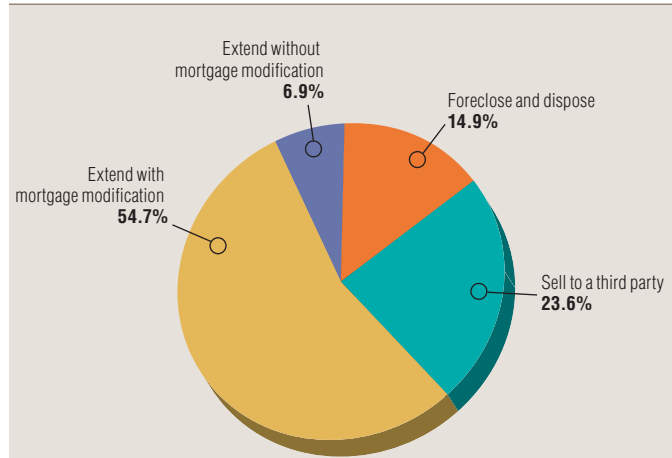
Source: FDIC.

Note: Delinquent loans are defined here as those that are noncurrent, either 90 days or more past due, or in nonaccrual status.

*As of Q2 2012.

EXHIBIT 2-6

Maturing Loans: Preferred Strategy for Lenders

Source: *Emerging Trends in Real Estate 2013* survey.

Note: Based on U.S. respondents only.

Fewer Banks Drive Harder Bargains

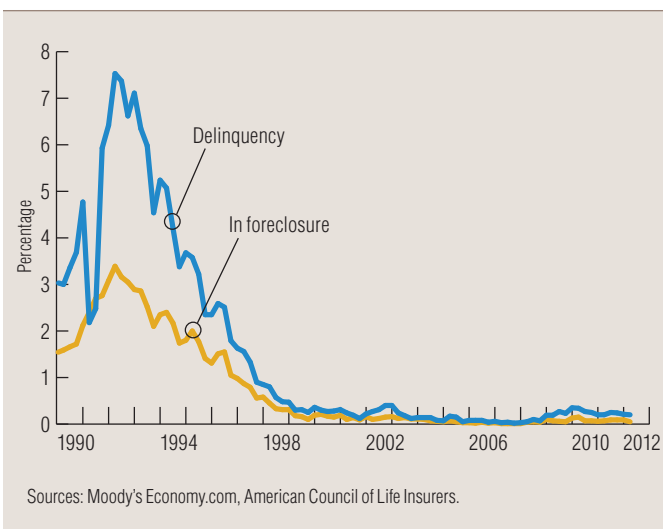
The credit debacle has shrunk the banking community into “a smaller group” of active lenders. Interviewees count only two major U.S. money-center banks willing to lend on larger deals, and hobbled European banks, once influential players “are out of the picture.” Regional and local banks have been winnowed down, and survivors may consolidate and merge to find economies of scale needed to comply with new banking regulations. Finding fewer choices, borrowers will continue to confront tough lending terms; banks require “a lot of equity” and some recourse. Perhaps not surprisingly, bankers appear more willing to keep these better-underwritten loans on their balance sheets than try to securitize them. Notes an interviewee, “Banks now do business the way they should have been doing business all along—actually thinking about real estate and not about debt getting flipped or getting paid for origination.” Refinancing takes the breath away from the origination market; the bulk of lending across all sources will continue to focus on dealing with the \$300 billion in loans maturing annually through 2015.

Insurers Cream the Top of the Market

After retreating from the precrash overleveraging binge and, not coincidentally, avoiding the portfolio problems of banks and CMBS originators, shrewd life insurers still “have the pick”

EXHIBIT 2-7

U.S. Life Insurance Company Mortgage Delinquency and In-Foreclosure Rates



of the best senior loan deals in the absence of much competition. They originate record volumes, usually with high-credit clients, and on a risk-adjusted basis conservatively achieve a considerable cushion with loan-to-value ratios of 65 percent or lower and “a lot of real equity ahead of us” on high-quality assets. Interviewees claim insurers are not pushing values and base underwriting on current cash flows. “That’s how they have stayed out of trouble” all along. Uncharacteristically, they move into multifamily housing and even do some mezzanine lending and construction to permanent loan deals to get higher yields; given current markets, these risks seem reasonable. Making their mark in avoiding commodity properties, insurers will not fill the lending void in helping troubled borrowers owning Class B or C properties. But in 2013, insurers will try to limit the terms of loans and offer more floating-rate debt to hedge against the low-interest-rate environment. Some new insurers may also enter the real estate lending space, but this will not be a game changer for borrowers.

CMBS Lurching Forward

New regulatory restrictions on traditional lenders—including Basel III and Dodd-Frank—could open the way for private equity and hedge funds, as well as start-up lending shops, to fill some of the void or step in to resuscitate the still-flagging conduit business. “Sputtering to life” from “a shadow of what it was,” CMBS may have a chance to lurch back into the financing spotlight “once transaction activity increases.” Without enough

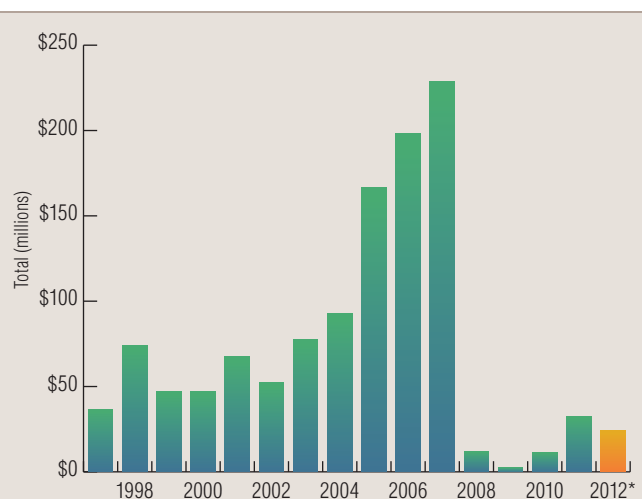
“good product, you cannot create pools, and there hasn’t been enough [good product].” The market also requires more B-piece buyers to invest in the riskiest tranches, so originators have held back, unwilling to warehouse loans.

But the CMBS industry may need to confront bigger obstacles in order to rebound fully. Although most interviewees contend that a properly functioning mortgage securities engine is necessary for liquidity in the real estate capital markets, they also express serious concerns about failures to address evident problems in CMBS underwriting, regulation, ratings, and servicing since the market collapse at the depths of the credit crisis. “The problem for bond buyers remains”: the people running CMBS shops have “shuffled around,” underwriting is only marginally better,” originators and issuers “don’t have enough skin in the game” for an alignment of interests, the ratings agencies still get paid by the issuers, and “attitudes haven’t changed.” In short, “nothing meaningful has happened” to correct the problems, which sent bond buyers running to the exits.

Some interviewees say regulatory changes—like requiring holding a portion of each loan or delays in realizing fees and promotes—could lower industry profitability and limit the number of players willing to enter the business. Some interviewees remain skeptical, “At first B-piece buyers will be reasonably disciplined. Then they will gradually loosen credit standards as transactions and money come into the market” until it’s time to “revisit underwriting problems” and their consequences. In the meantime, “bond buyers cannot get the same level of detail and disclosure we did pre-2007,” and more hedge funds, not real

EXHIBIT 2-8

U.S. CMBS Issuance



Source: Commercial Mortgage Alert.

*Issuance total through August 30, 2012.

estate-oriented players, work the B-piece space, raising questions about the quality of due diligence.

In spite of continuing concerns, interviewees continue to expect that CMBS issuance can return to a \$75 billion to \$90 billion level over the next several years—well below its \$250 billion peak, but a rational market share.

Another CMBS Roadblock: Special Servicer Questions

Who watches out for bondholders once CMBS loans go into default? It was supposed to be special servicers, even though CMBS pioneers in the mid-1990s privately had questioned how servicers could handle a deluge of problem mortgages working off complex loan documents without any previous connections to borrowers. The early promoters conveniently dismissed potential problems by predicting only a small chance of mass defaults. Unfortunately, interviewees say, now-evident problems involving some special servicers and their handling of tens of billions of dollars in troubled CMBS loans raise questions and further reinforce market doubts about CMBS structures and relationships. Disparate and disaggregated, “senior bond holders complain, but take no [concerted] action [yet]; something will bubble up.”

At the same time, borrowers continue to face hurdles in pursuing work-outs: “They have nobody to talk to.” In addition, some interviewees highlight questionable special-servicer practices, including holding back on resolving loans to feed fee machines, side dealing, profitable trades at the expense of

EXHIBIT 2-9

CMBS Mortgage Delinquency Rates

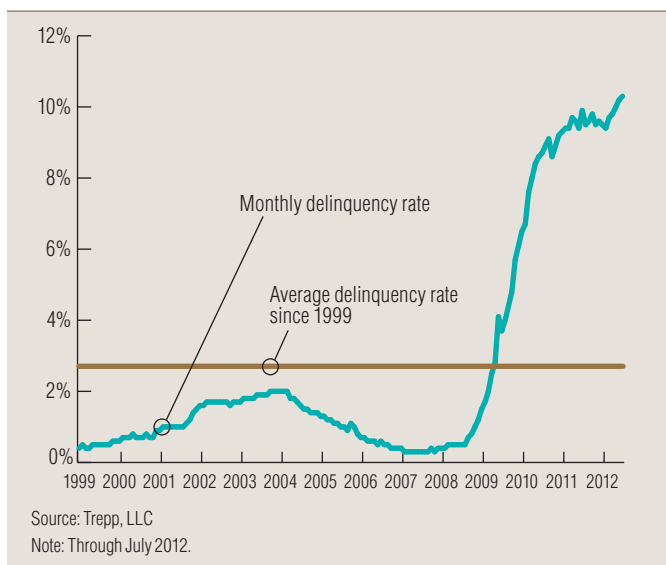
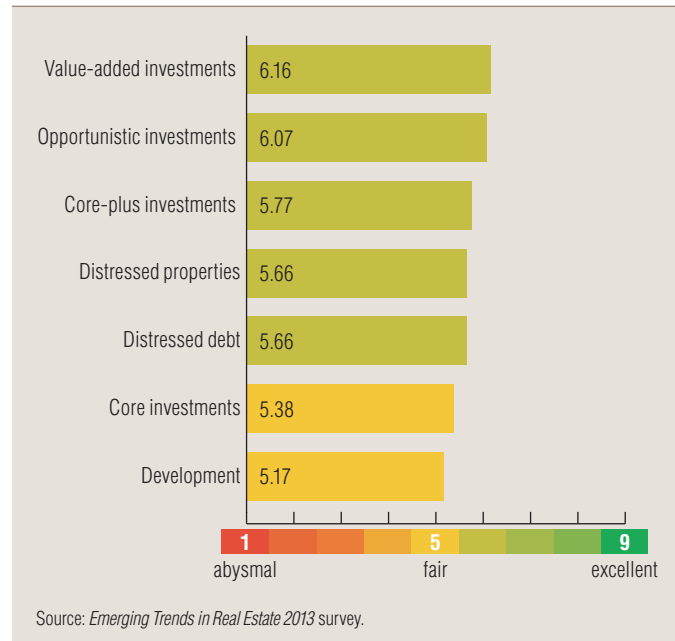


EXHIBIT 2-10

Prospects by Investment Category/Strategy



trusts, and self-serving abuse of document loopholes, according to interviewees. If so, these servicers take advantage of the lack of any ready oversight since mechanisms were never put in place over them to protect bondholders beyond caveat emptor. Besides the potential for lawsuits, interviewees suggest that the industry and/or regulators must address these special-servicing issues or “the CMBS world will continue to flounder.” Some borrowers, meanwhile, just wish they had “taken a higher rate” through a traditional lender. Expect servicers to increase auctions on their worst assets; they have reached the point of diminishing returns and will take almost “any price to avoid paying property taxes.”

Searching for Yield in the Capital Stack

Investors will continue to jockey for position in the capital stack to achieve the best risk-adjusted returns, hoping for as much upside as possible. A ton of dollars “looking for a home,” rock-bottom interest rates, and resulting low cap rates push down mezzanine debt quotes on core real estate into the high single digits (they remain in the low to mid-teens for secondary markets). Although disappointing for the yield hungry, these deals still promise a core-plus return with a downside cushion ahead of core equity. Recapitalizing a high-quality, overleveraged property and taking a preferred equity position may turn

out even better. In either case, core equity owners face lesser prospects: they assume the first loss position when cash flows and potential future interest moves could leave them with less generous return expectations unless rents escalate ahead of most predictions.

The Squeeze-Down of Opportunity Funds

As investment banks retreat from funds management in the wake of the expensive regulatory “compliance maze,” super-sized private equity and hedge funds—“the new nonbank banks”—vacuum up pension fund allocations, which characteristically seek safety in the security of what everybody else is doing. Managers of these multibillion-dollar funds then “push out dollars promising big returns, which could be hard to realize” in current commercial markets compromised by improving but still questionable tenant demand. With tremendous buying power, they target large portfolios and entities, looking to improve performance and then sell down the line.

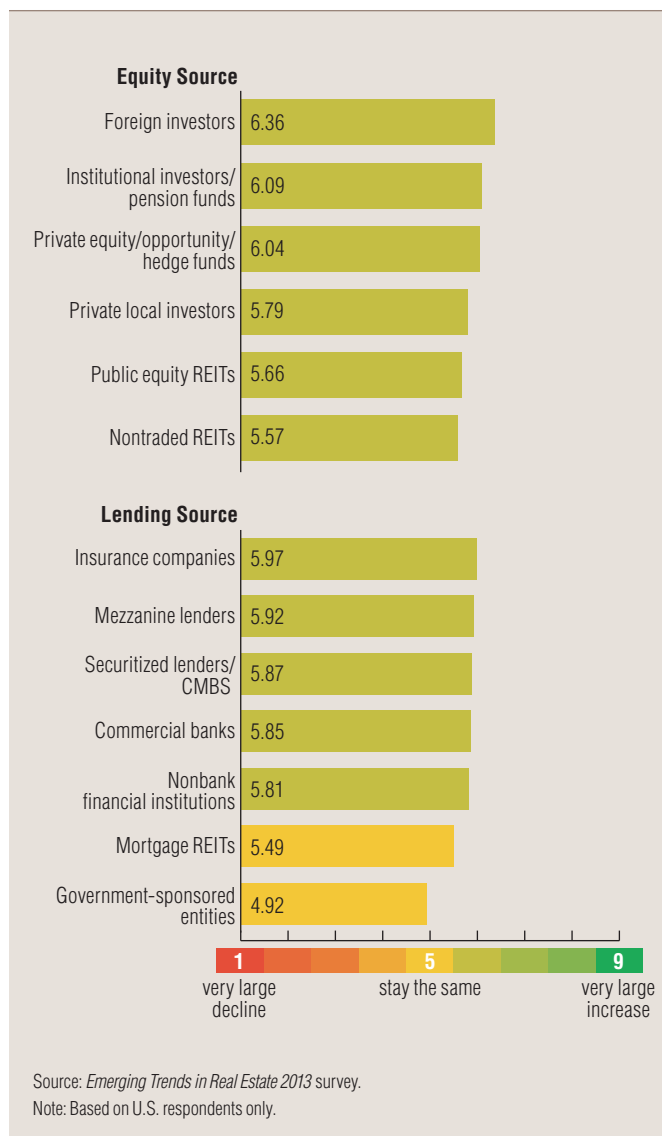
In these markets where promotes will be more difficult to achieve, the megafunds can earn “huge fees on their volumes” alone, leaving hundreds of smaller “opportunity fund” competitors, who need promotes to profit, grasping for leftovers and vulnerable to failure. “The simple math proposition of organizational expenses for smaller general partners is that without scale and unless you get promotes, you cannot make the businesses work.” And very few can be successful consistently. They may time taking advantage of a narrow window for acquisitions at or near the bottom of a cycle and ride a recovery, but the cycle may not cooperate for subsequent funds, which will miss on any significant value gains once recovery has played itself out. In the worst-case scenario, late-to-the-game funds buy too close to the top and sink in any market correction. Because finding good opportunistic investments in the current environment is difficult, more opportunity funds “will be forced into development” to have any chance of realizing satisfactory performance bonuses, and many of these fund managers lack development expertise unless they are fronted by experienced local operators. Plan sponsors and other investors become hip to the square: they favor existing managers with good operating histories and without legacy problems. Other managers “will struggle to raise peanuts.”

REITs Corner the Top-Tier Market

Sitting pretty at the top of the real estate food chain, public REITs consolidate their holdings in core, institutional-quality real estate and reap the benefits of cap-rate compression on well-leased properties as well as ongoing solid income genera-

EXHIBIT 2-11

Change in Availability of Capital for Real Estate in 2013



tion. Generally strong management teams can scale operations, leading to expense savings over portfolios, and leverage national tenant relationships, especially in retail and industrial space. They continue to sell weaker assets, deleverage higher-cost debt, grow unencumbered assets, get investment-grade ratings, and float cheaper unsecured financings. Insurance companies and banks, meanwhile, fall all over themselves to extend credit to these public companies: “They chase the people who need it the least.”

The stock market understandably looks favorably on all these moves. “REITs stack up as a defensive asset with good earnings and dividend growth”—hard to find amid otherwise choppy equities’ performance. If worse comes to worst, many of these companies look well positioned to ride out any problems: prime holdings inevitably perform better in most market scenarios, losing less value in down markets and appreciating more in recoveries. But companies concentrated in certain weak sectors like suburban office face tough sledding, and the overall industry pushes up against the limits of supply in top-tier properties. There are only so many to go around. When Class A assets come to market, expect well-heeled REITs to pounce on any opportunities.

High-Net-Worth Hesitation

Hungry for capital gains and less motivated by income, high-net-worth investors temporarily display less enthusiasm for commercial real estate. They tend to recoil from all the negative “never-in-my-life-have-I-seen” economic indicators and stockpile cash. Exceptions are entrenched local real estate families, who have built up fortunes over time developing, owning, and managing properties for the long term. They remain very much in the game and look to take advantage of any bargains, especially in secondary markets where big players have been relatively scarce. They will try to use their marketplace knowledge and considerable local connections, including tenant relationships, to best advantage.

Pensions in Flux

On the front burner for pension funds, “serious underfunding” plagues public plan sponsors, potentially upending retirements of aging baby boomers. “In a pure numbers game,” states and local governments move toward a reality check: taxpayers ultimately may not be able to afford the current public pension fund system. Over time they likely must follow the lead of corporate plan sponsors and transform defined-benefit plans into defined-contribution programs self-managed by the beneficiaries, and 401(k)s, whose liquidity requirements make investment in equity real estate unwieldy and “could diminish real estate’s role.”

In the meantime, some plan sponsors downgrade real estate from “its own little province” into an asset-allocation category lumped together with other real assets like infrastructure, natural resources, and farmland. These plan sponsors “look for greater efficiency and pricing; in theory, if timber offers better returns, then allocations to real estate may be reduced.”

For pension fund managers, the handwriting is on the wall, though the ramp-down of defined-benefit plans will happen gradually and not begin immediately. “With mixed results,” they

continue to wrestle with how to put day-to-day valuation and liquidity mechanisms—cash and public REIT allocations, limitations on investment rights—in place for private equity real estate options in 401(k) plans. Then marketing real estate to beneficiaries presents its own challenges, competing among all the various stock, bond, and cash options.

For now, pension funds tie themselves in knots over strategies and return expectations after securing “relatively good” recent real estate performance and wondering if it can continue. They need alpha to fill funding gaps, but also require steady income to meet current payout requirements. For most pension fund investment managers, fundraising has been “brutal” and should remain difficult in 2013. Uncertainty leads plan sponsors to “write fewer and bigger checks to bigger, safer [brand] names.” And although overall allocations remain up, “getting invested remains an issue with queues into core funds just about everywhere” and other managers struggling to find product to meet ambitious return parameters. “A lot of pension fund money was attracted into real estate by promises of 15 percent or better returns, and that’s not happening.” The biggest public funds “grow more conservative” and bring direct investment capabilities in house after a past round of cost cutting and shedding staff experts.

“Open questions” abound.

EXHIBIT 2-12

Percentage of Your Real Estate Global Portfolio in World Regions

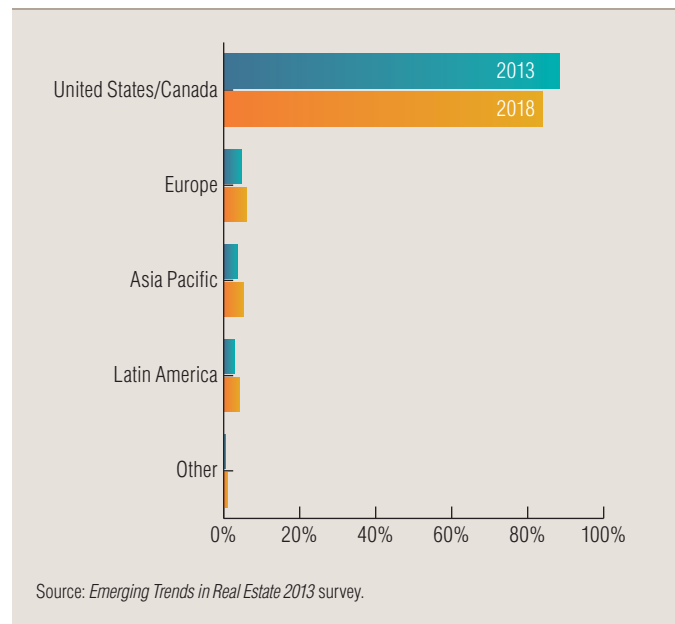
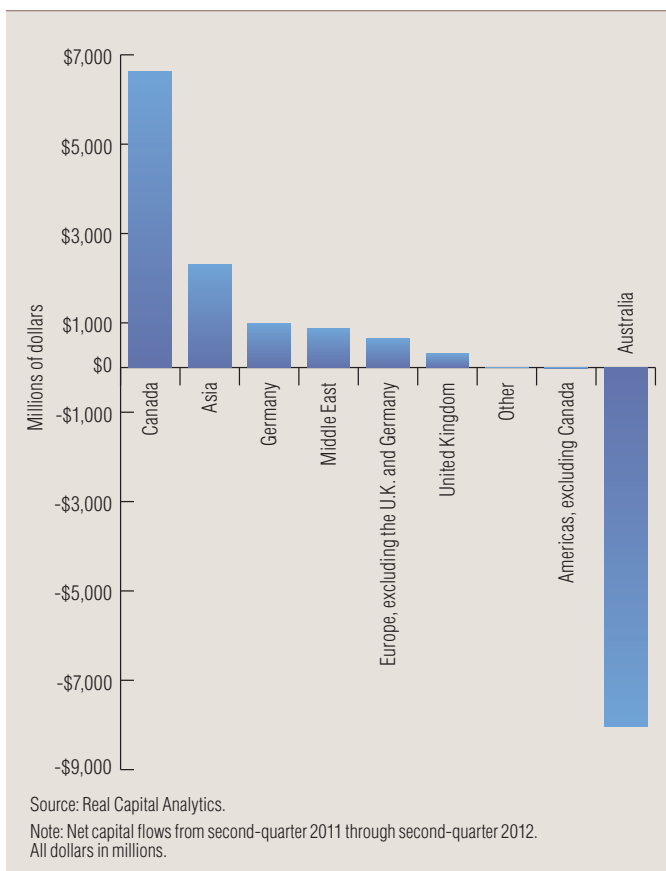


EXHIBIT 2-13

Foreign Net Real Estate Investments in the United States by Buyer Origin



Safe Haven Influx

In a world of economic hurt and fear, the United States still “represents good relative value” and ranks internationally as the “premier” safe real estate investment haven. Europeans cope uneasily on shaky domestic turf and seek relative stability and some measure of yield across the pond, while wealthy Chinese and Russians park assets outside of their countries. Middle East investors and affluent Israelis play smart by offshoring wealth away from backyard hotspots, and nouveau riche Latin Americans diversify fortunes into south Florida condos. Asian sovereign wealth funds are flush with cash and could pick up any slack if domestic pension funds pull back. Anticipate that foreign money will continue ample inflows into American property markets from all compass points unless the federal government fails to address the fiscal cliff. Concentrating their activities in the *très chère* gateways, most foreign sources “may not get great returns, but with low interest rates, they’ll take their

chances.” The amount of foreign capital in New York City and Washington, D.C., is “breathtaking”; San Francisco, Miami, Los Angeles, and Boston also draw attention, but not much heads elsewhere.

Europe. “Scared to death” about the euro crisis and concerned about China’s slowdown, Germans, Dutch, and the Brits especially seek safe U.S. harbors and see good relative value. “They will be very active.” Some veteran players may even venture tentatively beyond the gateway investment model given high pricing in the 24-hour cities.

Asia. The region’s bulging sovereign wealth funds view the United States “positively.” They like its size and stability in contrast with Europe’s problems and the volatility of emerging markets. And U.S. real estate certainly compares favorably with T-bill yields or other alternative investments. Chinese institutions just begin to look offshore under new government rules. “They will concentrate in the most familiar coastal markets, the one’s they know and feel safe in.” Wealthy Chinese individuals “are recreational investors willing to make high-risk investments” in fancy homes and skyscraper condos. Chinese banks “can be extremely competitive if they choose” as Japanese and South Koreans also “keep their hands in the game.”

Canada. Buoyed by their strong fiscal condition, Canadians look south of the border after running out of real estate opportunities in their relatively constrained markets where institutions buy and hold on to the best properties. “The grass is always greener,” and the amount of Canadian capital trying to find its way into the United States “is mind-boggling.” The big public pension funds have been joined by public vehicles and some private funds in the hunt for returns. Investment banks and money managers “crank out” new funds “like cookie cutters” with stretched yield promises and may buy inferior properties.” There’s just a ton of pent-up capital that needs to get invested.” But the institutions know the markets: “They won’t be reckless.”

Middle East. Oil money focuses on “the four food groups and hotels,” but has no interest in niche or specialized property strategies. Business is conducted quietly with longtime partners. “They are willing to take outsized risk for outsized returns.” Israelis have always had close ties to the United States and increase their activity. “It’s the most secure place for them to invest.”

Latin America. As South American economies comparatively flourish and a wealthy class emerges, the United States naturally attracts increasing amounts of Latin American capital. South Florida pieds-à-terre or New York apartments not only make good investment candidates for securing assets, but also are status builders. Expanding Hispanic demographics also make the United States an increasingly comfortable place to invest as well as do business.

EXHIBIT 2-14

Foreign Net Real Estate Investments in the U.S. by Property Type

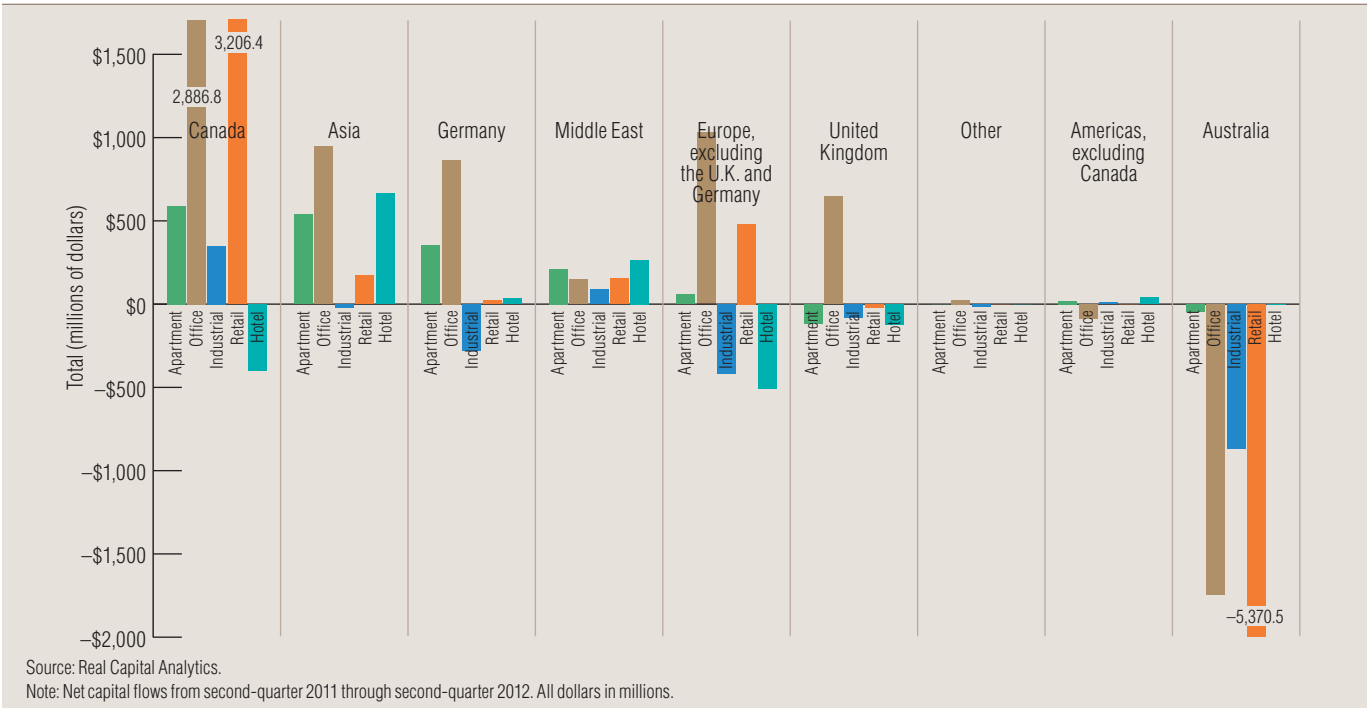
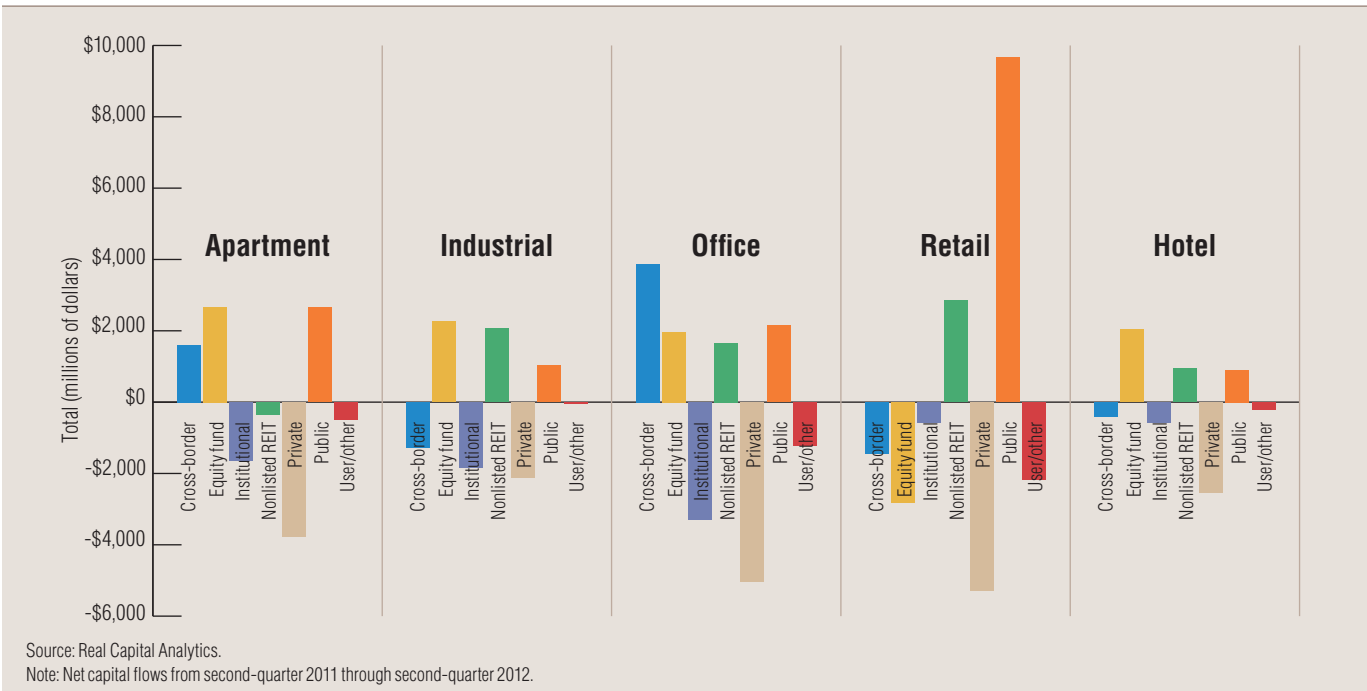


EXHIBIT 2-15

U.S. Buyers and Sellers: Net Capital Flows by Source and Property Sector





Markets to Watch

“Look where other people aren’t, and smart money will follow micro-fundamentals.”

In 2012, the *Emerging Trends* “Markets to Watch” chapter opened with the following interviewee quote: “Capital will search for yields beyond the overbought gateways and the few jobs-growth markets, taking on considerably more risk.” Investment strategies conformed with *Emerging Trends* forecasts through the first half of 2012, but investment slowed at the start of the second half. This slowdown was just a sign of apprehension over stepping outside the prime market/prime property investment strategy. The acceptance of additional real estate risk did not seem feasible to many in view of other concerns on the horizon. This “wait and see” approach is understandable because investors must reevaluate the global economic uncertainty, a limited increase in U.S. employment, continuing problems with housing, and a presidential election.

Even though these troubles linger, the 2013 *Emerging Trends* forecasts display strong signals that investors will return to accepting more risk in their portfolios in an attempt to “chase more yield.” Overall, interviewees have a positive tone, stating, “Yield is in the secondary markets,” “We like safe bets; but secondary markets are the focus now,” and “The idea is to start moving into second-tier markets where there’s better pricing relative to the top-tier markets.” Secondary real estate markets were mentioned repeatedly, comments focusing mostly on their price and yield advantages. “The chasing of yield started in the gateway cities [and] is now spreading to the other markets. . . . There is quite a lot of activity in the secondary city markets.”

Even as riskier secondary markets show up on investors’ radar, many believe the move cannot be made without concentration on leasing to high-quality tenants within growth industries that are sustainable. “Location, location, location” will always be the key driver in real estate. However, as property prices meet

or exceed prerecession levels in the “big six”—San Francisco, New York City, Boston, Washington, D.C., Los Angeles, and Chicago—the focus of markets and property investors has shifted more to the lessee’s value, various market demographics, a city’s economic production, diversification, job growth, and basically on where people want to be. As one investor states, “Corporate occupiers may do better by following their employees.” Real estate investors might want to reflect on that strategy.

Market Trends

Survey Says . . .

Because other asset classes continue to offer minimal returns or too much volatility, investment capital’s interest in commercial real estate continues to increase. The 2013 *Emerging Trends* survey results confirm this trend: only six of the 51 markets covered exhibited a decline in investment prospects. This year, 57 percent, or 29 cities, received a rating of “modestly good” or better, followed by 27 percent with a rating of “fair,” and only 16 percent were rated “modestly poor” or lower. Compared with last year, investment prospect values for the big six rose by an average of only 0.48 points, but the rest of the field improved its values by an average of 0.62 points. Those cities making the biggest moves in the values, and rated “generally good” or better, were generally secondary markets and included Salt Lake City, Charlotte, and Miami. On the other end of the spectrum, Washington, D.C., and Austin, two of the top-rated markets in last year’s report, saw their rating values decline, as did New Orleans.

EXHIBIT 3-1

U.S. Markets to Watch: Overall Real Estate Prospects

	Investment	Development	Homebuilding
1 San Francisco (1/1/1)	7.21	6.87	6.80
2 New York City (2/2/3)	7.14	6.76	6.42
3 San Jose (3/3/2)	6.89	6.58	6.58
4 Austin (7/4/5)	6.71	6.40	6.26
5 Houston (5/5/6)	6.84	6.36	6.15
6 Boston (4/6/8)	6.85	6.31	6.05
7 Seattle (6/8/7)	6.72	6.16	6.14
8 Washington, DC (12/9/4)	6.43	6.11	6.30
9 Dallas/Fort Worth (10/7/10)	6.47	6.20	5.86
10 Orange County, CA (9/19/9)	6.48	5.57	5.91
11 Raleigh/Durham (15/10/11)	6.27	5.93	5.72
12 Miami (11/11/16)	6.47	5.89	5.44
13 Northern New Jersey (16/12/12)	6.26	5.89	5.65
14 Denver (8/14/15)	6.49	5.77	5.45
15 San Diego (13/17/13)	6.37	5.60	5.61
16 Los Angeles (14/15/14)	6.35	5.69	5.49
17 Charlotte (18/16/19)	6.17	5.67	5.26
18 Nashville (21/13/21)	6.03	5.79	5.16
19 San Antonio (22/18/17)	5.97	5.59	5.40
20 Portland, OR (17/20/23)	6.19	5.52	5.09
21 Salt Lake City (19/21/20)	6.06	5.39	5.20
22 Honolulu/Hawaii (24/22/18)	5.79	5.37	5.33
23 Minneapolis/St. Paul (23/25/25)	5.89	5.06	4.82
24 Chicago (20/24/31)	6.05	5.12	4.54
25 Westchester, NY/Fairfield, CT (28/23/26)	5.59	5.14	4.78
26 Virginia Beach/Norfolk (31/27/22)	5.36	5.00	5.14
27 Philadelphia (27/26/24)	5.61	5.05	4.83
28 Orlando (26/28/27)	5.64	4.97	4.77
29 Tampa/St. Petersburg (25/29/29)	5.66	4.90	4.64
30 Pittsburgh (33/32/28)	5.32	4.66	4.66
31 Baltimore (32/30/33)	5.36	4.78	4.40
32 Oklahoma City (36/31/30)	4.98	4.76	4.55
33 Phoenix (29/37/34)	5.56	4.24	4.26
34 Kansas City (34/33/32)	5.27	4.37	4.42
35 Atlanta (30/34/38)	5.40	4.32	3.96
36 Inland Empire, CA (35/36/36)	5.20	4.26	4.05
37 Indianapolis (38/35/35)	4.83	4.31	4.20
38 Cincinnati (37/38/40)	4.96	4.18	3.88
39 Jacksonville (39/39/41)	4.80	4.16	3.88
40 Columbus (42/41/37)	4.56	4.04	4.00
41 Milwaukee (41/40/42)	4.59	4.04	3.88
42 Albuquerque (44/44/39)	4.48	3.88	3.90
43 St. Louis (40/42/46)	4.61	4.00	3.65
44 Tucson (43/47/44)	4.53	3.71	3.83
45 Memphis (47/43/45)	4.23	3.94	3.80
46 Providence, RI (48/46/43)	4.23	3.77	3.83
47 New Orleans (50/45/47)	4.16	3.85	3.65
48 Cleveland (49/48/48)	4.19	3.39	3.65
49 Sacramento (45/49/49)	4.31	3.30	3.43
50 Las Vegas (46/50/50)	4.30	3.00	2.94
51 Detroit (51/51/51)	3.38	2.16	2.33

Source: *Emerging Trends in Real Estate 2013* survey.

Note: Numbers in parentheses are rankings for, in order, investment, development, and homebuilding.

Expectations have risen not only for investment, but also for development prospects for 2013. Of the 51 markets covered, 20 were rated “modestly good” or better for development, 12 were rated “fair,” and 19 scored a “modestly poor” or worse. Development rating values were up across the board, but the big six scored much better than rest of the field, registering an average 6.14, compared with the field’s 4.82 average. Says one interviewee, “Replacement costs are better than market prices in larger markets, so now might be the time to build.” According to survey participants, market movers in the development arena include Charlotte, San Francisco, and Chicago. Less interest in building was found in the Washington, D.C.; Westchester County, New York; and Detroit areas.

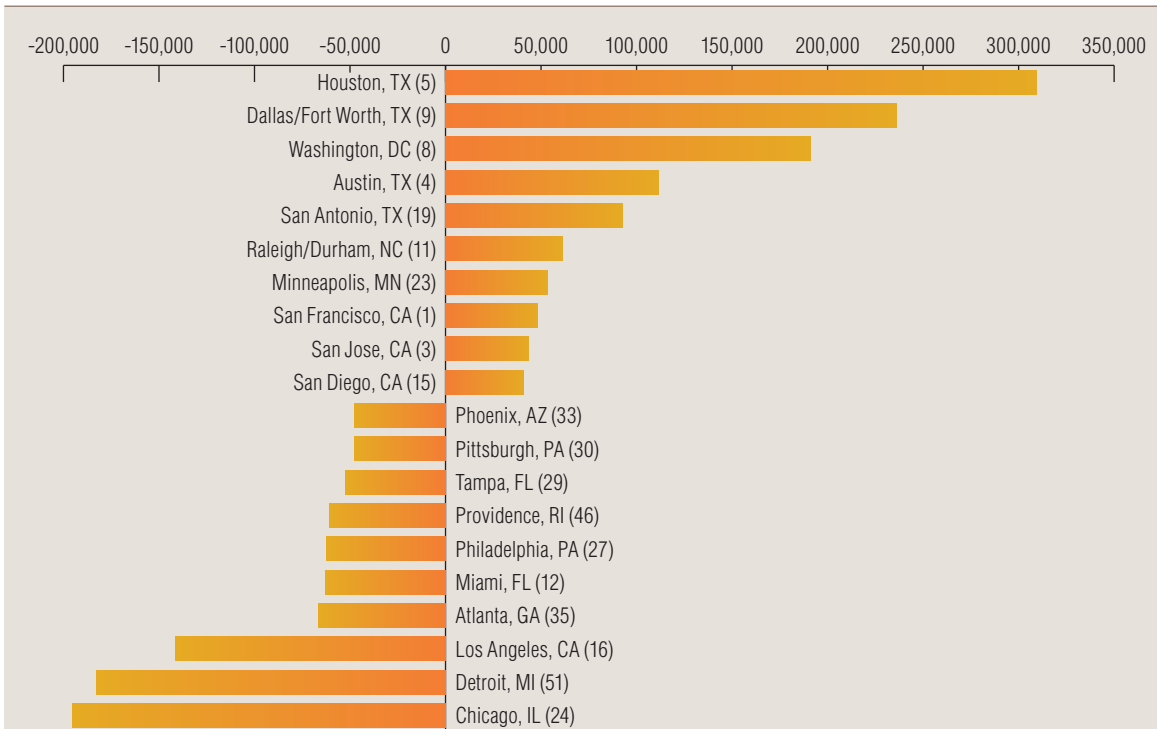
Homebuilding has started to see the light, a view documented by survey results: the number of markets rated “modestly good” or better increased to 14 from only three last year. “The housing market has finally bottomed, and now real estate growth should follow,” says a developer. This might be true, but homebuilding prospects will be best in the larger markets, according to survey results. All big-six markets except Chicago received a rating of “modestly good” or better for homebuilding. As a total, the average value for larger markets was 5.93, compared with an average of 4.71 for the rest. Housing may have bottomed out, but the markets that offer the best homebuilding prospects are the larger ones. According to survey results, top areas for homebuilding in 2013 include San Francisco, San Jose, and New York City. The areas with the least attractive prospects include Detroit, Las Vegas, and Sacramento.

“Employment Please”

Slow and limited job creation continues to be a concern in 2012, and according to *Emerging Trends* interviewees, the topic will be one of the top issues in 2013. Interviewees believe, “jobs are getting better, but won’t accelerate in 2013,” “limited job creation isn’t increasing demand,” and “we’re not sure what the engine is that will drive job growth.” Moody’s Analytics forecasts slow growth—a 1.1 percent increase in employment for the coming year. Even with these modest projections, there have been signs of continuous job growth. Since the “technical” end of the recession in July 2012, the United States has added 2.66 million nonfarm jobs. However, that constitutes only 36 percent of the 7.4 million jobs lost during the recession. Even with those statistics, one optimistic interviewee forecasts “6 million new jobs by the end of 2014, or about 250,000 a month.”

Service-type positions show strong growth in numbers, but goods-producing employment continues to struggle, down 18.7 percent since the peak in 2006 (see appendix). The number of government positions in 2013 is still expected to be down

EXHIBIT 3-2

Employment Change (2007–2013)

Source: Moody's.

Note: Employment for 2013 is a forecast as of September 2012. Numbers in parentheses are overall rank.

from the 2009 peak, mostly driven by state, regional, and local reductions. Federal positions remain a concern because budget issues may lead to major cutbacks. “Government employment and even subcontractors should be concerned,” says one participant. Even though overall job growth is questionable, some industries—including technology, energy, health care, and education—show strong signs of growth. “Energy, tech, and health are going to do much better than people think.”

Emerging Trends survey results show a strong correlation between jobs and survey rankings. Some markets with strong 2013 employment growth projections fared well, including any city in Texas, New York City, Raleigh, and San Jose, to name a few. Not surprisingly, several of these markets also have a large concentration of work in those few industries showing growth. For example, Houston has energy, which represents 3.6 percent of the city’s employment; 16 percent of Raleigh’s jobs are in education; and the technology sector constitutes 25 percent of San Jose’s employment. These numbers show some positives, but real estate’s future is still uncertain. As an interviewee states, “It’s a horse race between NOI increases, job growth, and interest rate hikes.”

Diversity, Production, and Rank

As expected, the majority of markets with higher overall economic production scored better in this year’s survey. Measuring gross metro product (GMP) per capita—the size and production of a metropolitan area by population—the projected average growth is 1.4 percent for all of the markets covered in the report. Survey results show that 24 cities will exceed that average, and 27 will fall below it next year. Comparing that to survey market ranks, seven of the top ten *ET* markets are considered above average producing cities, while three fall below average expectations. Austin (4), San Jose (1), and Dallas (9) top the GMP per capita list at 5.3 percent, 3.1 percent, and 3.0 percent growth, respectively. Economic production is a driver of real estate—and obviously of interest to interviewees and survey participants. As one states, “Economic production and revenue are influential in our investment decisions.”

A little more unexpected is the comparison of survey rank to Moody’s industrial diversity scale. Industrial diversity is a 0-to-1 scale that measures a market’s business diversity compared with that of the United States as a whole, which is assigned a

EXHIBIT 3-3

Gross Metro Product per Capita

Best	Worst
1. Austin (4)	1. Detroit (51)
2. Salt Lake City (21)	2. New Orleans (47)
3. Houston (5)	3. Cleveland (48)
4. San Jose (3)	4. Providence, RI (46)
5. Raleigh/Durham (11)	5. Northern New Jersey (13)

Sources: Moody's forecast for 2013; *Emerging Trends in Real Estate 2013* survey.

Note: List based on *Emerging Trends* markets only. Number in parentheses represents *Emerging Trends 2013* total market rank.

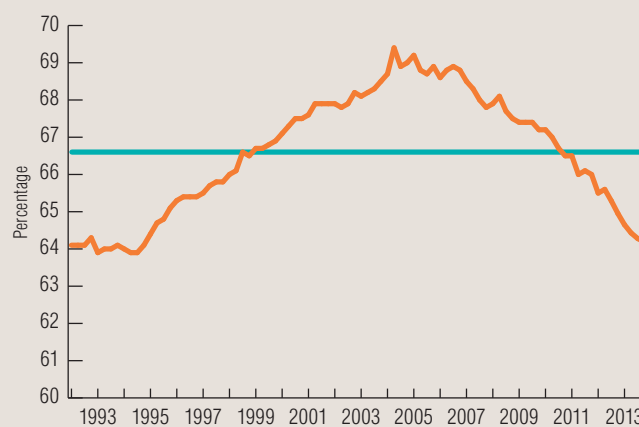
value of 1. Employment diversity should be a benefit to market risk and output. However, when compared with survey ranks, the answers are slightly unexpected. Out of 51 *Emerging Trends* markets, 23 received a 0.75 industrial diversity rating or better, signifying that those metropolitan areas possess a rather diverse base. Of those 23 diverse markets, however, only one, Dallas, scored a top-ten ranking in the 2013 *Emerging Trends* report. Of the remaining nine, six received a mark of 0.5 or higher, and three were below 0.5. Asks one interviewee, "Diversity is a sign of stability, but will stable be enough in a slow-growing economy?" Recessionary times might spark investors to look to more diverse markets to weather job losses and declines. However, now, in a time of slight economic uptick, results indicate that investor sentiment is focused on job-producing industries and those markets that contain them, such as San Jose and Seattle, regardless of how diverse the businesses are that are producing those jobs.

The Housing Impact

Even as many professionals feel more comfortable saying the housing market has bottomed out, statistics might lead to doubts about that conclusion. At the end of August, the U.S. Census Bureau reported that the homeownership rate was 65.5 percent, the lowest rate in the past 50 years (exhibit 3-4). This value does not even include the 3.9 million borrowers who are 90 days or more delinquent on house payments and at risk of default. Analysts often state that true homeownership is closer to 62 percent. Either way, the lending and homeownership crisis continues to put a big strain on commercial real estate and many commercial real estate markets. Many interviewees agree; one says, "If the housing sector recovers, more jobs, banks freed up, and a multiplier effect ensues."

EXHIBIT 3-4

Homeownership Rates



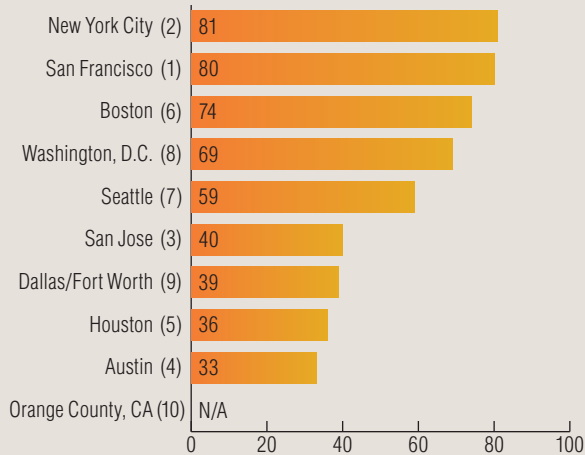
Sources: U.S. Census Bureau; Moody's Analytics (forecasts).

Even if home prices have "bottomed" in places or are "starting to see a little bit of life in terms of pricing," the road to recovery will be slow and difficult. According to Moody's Analytics forecasts, in 2013 only six housing markets will be in the black compared to their peak prices. Trends data show that these markets either did not experience such steep price declines during the recession or are in areas that have big expectations for job growth next year. A few markets with minimal price movements include Pittsburgh (30) and Oklahoma City (32). But even more interesting is the boost given home prices by increased hiring in areas such as Houston (5), Raleigh (11), and San Antonio (19).

"You're going to see the best housing markets provide better commercial real estate options." This statement stands true when looking at the survey's list of the top-ten investment prospects and various housing statistics. For the survey's top-ten markets, delinquency rates of 90-plus days are 30 basis points lower than the average for those in the other 41 cities in the survey, and delinquent loans are processed 27 days quicker in those same markets. In 2013, home completions will be 3.9 percent higher in the top-ten markets than in the other markets covered, and home sales will be 1.7 percent higher. "You're going to see the best markets get new housing," says an interviewee. Finally, comparisons of house price declines from peak levels are not even close: prices in the top-ten markets are down 17.3 percent, compared with 23.7 percent for the rest of the field.

The housing market might see another uptick in the near future because many large investment groups have started to enter the housing hunt. Investors have put up large amounts of

EXHIBIT 3-5

Public Transit System ScoresSource: Walk Score®, www.walkscore.com.Note: Number in parentheses represents *Emerging Trends 2013* total market rank.

capital to take advantage of low-priced and foreclosed homes available in markets such as Florida, California, Nevada, and Arizona. The investment strategy is to purchase these types of homes and then rent them to new residents. Though this approach is still fairly new and on a small scale, a private REIT has been created to follow this home purchase and rent strategy. Apartment rentals have risen, followed by increased development, but if an abundance of rental homes is entered into the game, overbuilding could become a concern for the apartment sector.

American Infill and Chasing Echo Boomers

Even though the housing market is starting to improve, demand and interest in apartments in “American infill” locations remain hot. “People want to live in areas where walking and transit is all that’s needed.” High transit and walkability scores are found in high-ranking *Emerging Trends* cities, including San Francisco (1), New York City (2), and Boston (6) (exhibits 3-5 and 3-6). This trend has led to a boom in apartment development: completions as a percentage of total inventory in 45 markets exceeds ten-year averages. This increased demand for infill apartment rentals is overwhelming: the vacancy rate in every market is well below the ten-year average. “People need to find a place to live, and we see a cyclical move away from homeownership in metropolitan markets.”

EXHIBIT 3-6

Walkability Rankings

Best	Worst
1. New York City 85.3 (2)	1. Jacksonville 32.6 (39)
2. San Francisco 84.9 (1)	2. Charlotte 34.3 (17)
3. Boston 79.2 (6)	3. Oklahoma City 35.6 (32)
4. Chicago 74.3 (24)	4. Indianapolis 37.4 (37)
5. Philadelphia 74.1 (27)	5. Kansas City 38.1 (34)

Sources: Walk Score®, www.walkscore.com; *Emerging Trends in Real Estate 2013* survey.Note: On a scale of 0 to 100, with 100 representing a walker’s paradise. List based on *Emerging Trends* markets only. Number in parentheses represents *Emerging Trends 2013* total market rank.

Leading this cyclical move is the echo boom generation, which has pushed the American dream of homeownership to the rear. As one interviewee states, “The echo boomer generation is a key demographic we are focused on.” This trend is strongly exhibited in a comparison of various markets’ demographic makeup with survey results: echo boomers as a percent of the population in the top ten ranked markets totaled 15.3 percent, but only 13.6 percent in the bottom ten markets (exhibit 3-8). This difference is evident in both primary and secondary markets: New York City (2), Austin (4), Seattle (7), and Salt Lake City (21), all have an echo boomer population that constitutes over 15 percent of the total for the metropolitan statistical area. Another key trend involving commercial real estate and echo boomers is education (exhibit 3-7). In the top five markets in terms of educational achievement, echo boomers make up 15.4 percent of the population, compared with only 13.8 percent in markets with less educational achievement.

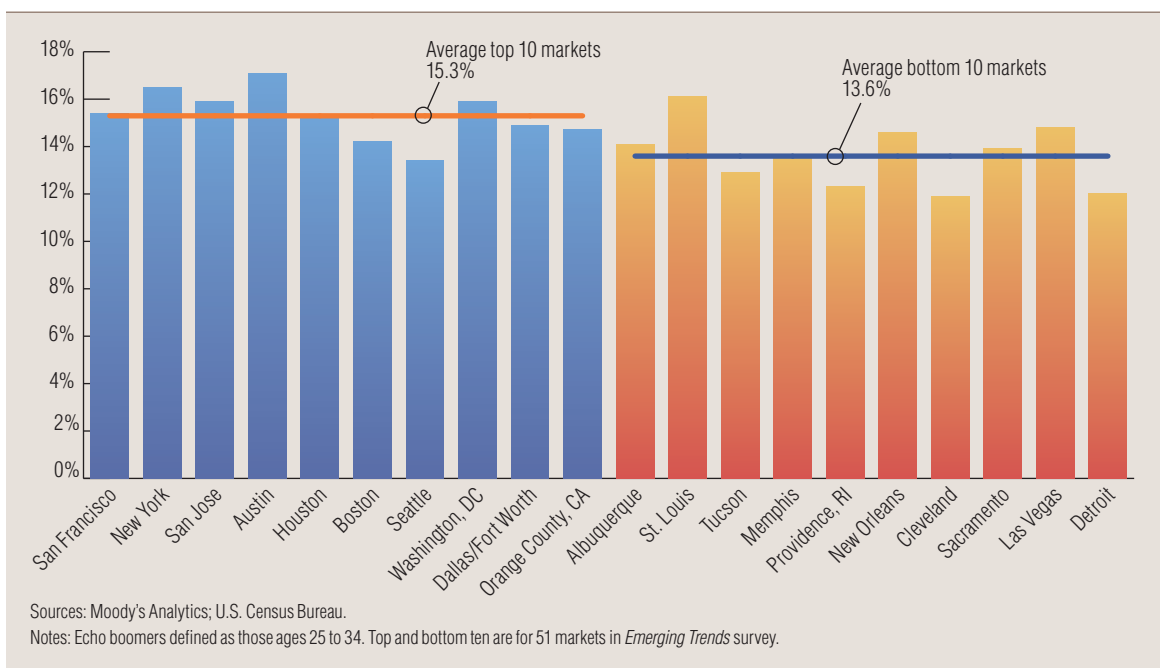
EXHIBIT 3-7

Metro Area Education Rankings

Best	Worst
1. Washington, DC (8)	1. Inland Empire, CA (36)
2. San Jose (3)	2. Las Vegas (50)
3. Boston (6)	3. Tampa (29)
4. San Francisco (1)	4. Jacksonville (39)
5. Baltimore (31)	5. Memphis (45)

Sources: Brookings Institution; U.S. Census Bureau; *Emerging Trends in Real Estate 2013* survey.Notes: Rank based on percentage of population age 25 or older with a graduate degree. List based on *Emerging Trends* markets only. Number in parentheses represents *Emerging Trends 2013* total market rank.

EXHIBIT 3-8

Echo Boomer Percentage of Population

Migration: Will Real Estate Follow?

A look at net migration as a percentage of total population produces some unexpected results and possibly a vision of what is to come. Raleigh (11), Phoenix (29), Tucson (44), Las Vegas (50), and Austin (4), in that order, make up the top five destination markets for in-migration, whereas negative net migration can be found in Cleveland (48), Detroit (51), and Chicago (24) (exhibit 3-9). A few interviewees expressed the importance of migration: "[We are] starting to focus on second-tier markets that have good in-migration," and "We like cities that have good education centers and are magnets for migration." Even so, higher-migration areas did not excel in survey rankings. Therefore, even if individuals move to certain markets for a job, a lower cost of living, or lower home prices, to name a few draws, institutional capital might not be ready to risk investing in those markets because of the current economic uncertainty. However, with an improving housing market possibly on the horizon, household mobility might return.

Big Six versus the Field

Over the last few years, the commercial real estate market has continued to see a division of market interest between major and non-major cities for investment. Many investors classify market

size using different standards; however, in the end the split comes down to the "big six" versus "the field." Even with pricing concerns, the big six—San Francisco (1), New York City (2), Boston (6), Washington, D.C. (8), Los Angeles (16), and Chicago (24)—continued to score well in the 2013 survey. "Regardless of prices, institutions seem to be staying in major markets," an investor says. This ongoing trend has affected prices substantially. Since the 2007 peak, commercial real estate prices in major metropolitan areas are down only 11.4 percent on average, compared with 29.4 percent in other metropolitan areas (exhibit 2-1). This major market price movement and cap rate compression has elicited mixed reviews from interviewees. Some express concern, saying: "Gateway cities are fully priced with too much capital chasing too few properties," and "Prices and fundamentals don't add up in the major markets." Others, though, still believe "good prime properties will always be good prime properties, and capital will flow."

While major markets remain the dominant force in commercial real estate and the main attraction of capital, participants and data show that non-major markets—the field—might not be a "bad play" moving forward. A comparison between the big six and the field in terms of certain macroeconomic elements reveals some strong areas for these markets. For example, averages of GMP, industrial diversity, and ten-year echo boomer growth all point to strength for secondary metropolitan areas.

EXHIBIT 3-9

Net Migration as a Percentage of 2013 Population

Survey results regarding investment prospects agree: some of the largest gainers in rating values compared with 2012 are Salt Lake City, with a 0.89 increase; Tampa/St. Petersburg, 0.87; and Nashville, 0.71. Even more surprising is the limited growth or actual decline in rating values in big-six markets such as Washington, D.C., down 0.50, and Los Angeles, up only 0.05. “Everything we’re looking at is incrementally better, meaning incrementally more capital for secondary markets as it spills out of the larger markets,” says one interviewee; says another, “Secondary market fundamentals haven’t been lagging substantially.” Secondary markets are in the crosshairs of many investors looking for return and ready to take on more risk, but the economic future as well as the availability of capital to those markets will determine the final outcome.

Develop or Buy

There has not been a positive outlook for development in an *Emerging Trends* publication in five years. Nonetheless, one key trend for 2013 is that some construction will return. As a whole, 12 more markets, for a total of 20, received a rating of “modestly good” or better as compared with 2012. Even though secondary or tertiary markets were the largest rating value gainers, interviewees were much more focused on developing in the big-six markets. Say interviewees: “Besides apartments, only select larger markets show signs of development”; “limited development outside of core markets”; and “build-to-suit and prelease is the way to go.” Because, apartments aside, market development has remained stable and prices in core locations are often

overvalued, replacement costs are often below bidding prices. Therefore, selective building can be expected within the big six, whereas controlled-cost acquisitions will be the trend in secondary markets. Survey results indicate that not much of either will take place next year in tertiary locations.

Although development will be somewhat limited, trends point to more environmentally friendly, sustainable buildings and a more efficient use of space. Green developers continue to embrace this pursuit and to adapt and conform to new demands from consumers. Owners believe “green building is often a good investment from a ROI [return on investment] perspective and adds to the bottom line.” In addition to sustainability, the amount of space provided continues to be adjusted, specifically in the office and apartment arenas. Say interviewees: “Office buildings are exhibiting anemic real growth and are getting serious about downsizing space per employee”; “Tenants are accepting smaller space [smaller units] to keep amenities, quality, and location”; and “People will be looking for smaller spaces generally, both commercial and residential. There will be an emphasis on reducing real estate operating costs.”

A Few Other Trends

Two additional market trends worth noting are organic versus inorganic growth, and the future for small deals. From a commercial real estate perspective, organic growth, except in apartments, is limited as corporations continue to sit on profits without adding employees. However, more inorganic growth in commercial real estate is being seen. Owners continue to look for tenants to

“steal,” offering newly structured space, often with better leases and concessions, in order to continue to show absorption in their locations. “We can move into another building across the street and take the same amount of space, but with a more efficient layout,” says one lessee. An owner agrees: “Often the tenant you need might be right in front of you.”

Interviewees also spoke of looking at much smaller deals—\$50 million or less—that are often of no interest to larger institutional capital players. “There is the perception that they are too small, but there are opportunities,” says one investor; adds another: “\$50 million and less is a very attractive place.” Equity for smaller deals is a bit easier to obtain and, even with the additional risk, might provide good returns at current lending rates. Some areas of interest in deals like these might be ancillary markets near stronger markets with job growing industries—for example, Bellevue, Washington, a smaller, growing city only a 16-minute drive from the booming city of Seattle. Ancillary markets might not be for all investors, but opportunities exist in many areas similar to Bellevue.

The Top 20 Markets

San Francisco (1). In 2013, San Francisco steals the triple crown from Washington, D.C., receiving top billing in the *Emerging Trends* investment, development, and housing categories. “San Francisco is driven by growth and a strong jobs outlook, led by technology and a structural change away from suburban and toward downtown.” Continued infill interest is supported by one of the best transit systems in the country and a city center with walkability that is number two only to New York City. “This around-the-clock city has someone pushing paper, shopping, shipping, or sightseeing all the time.”

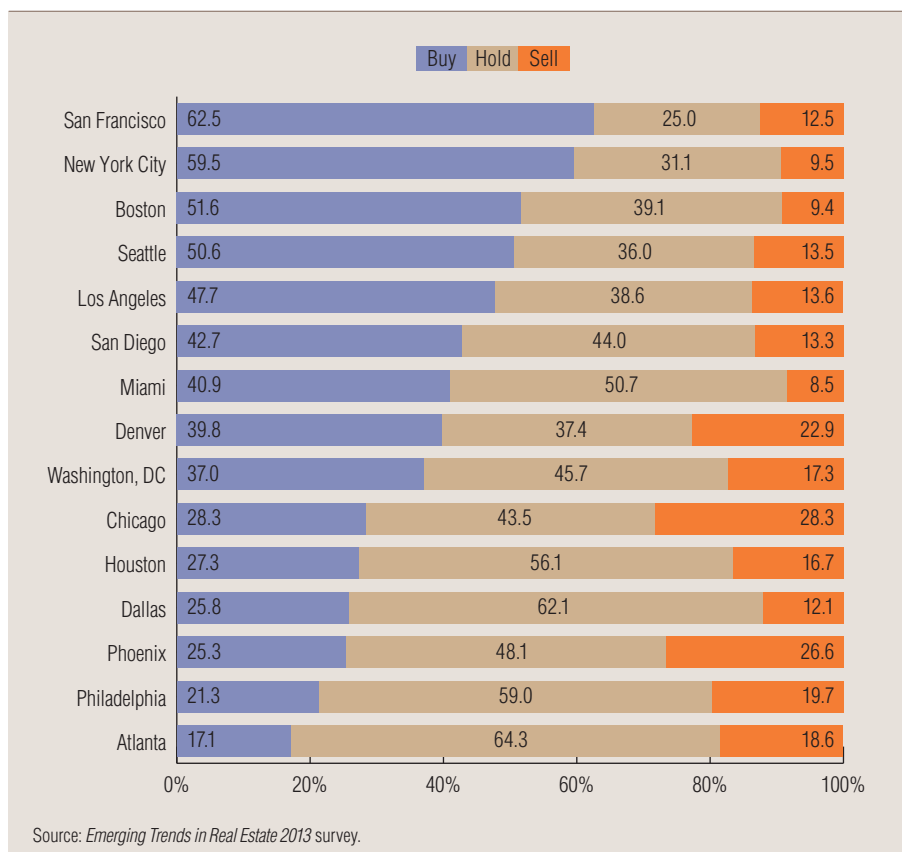
According to 2013 forecasts from Moody’s, San Francisco’s GMP growth will reach 1.7 percent, and the city will add almost 50,000 jobs from the 2007 peak. This pair of growth indicators should open investors’ eyes even wider to this global city. Even though industrial diversity seems weak here, investors still savor its skilled personnel and the facts that high tech accounts for 10 percent of the city’s jobs and the young demographic represents over 15 percent of the population. Even with a questionable business climate at times, San Francisco has a mix that draws many corporations now and will draw them in the future. Next year, higher commercial real estate prices and supply constraints might restrict the number of deals, but PwC’s pipeline analysis (exhibit 3-14) shows

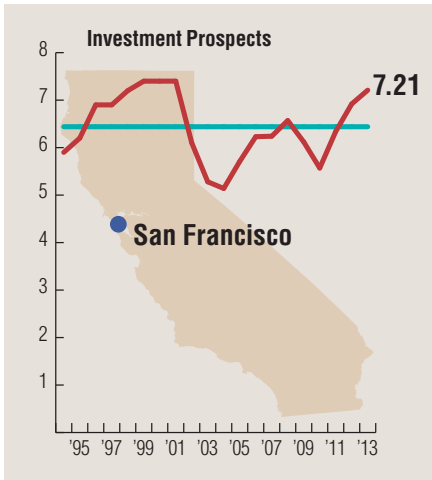
commercial real estate completions totaling near 1 percent of total stock. “The great fortunes in real estate have always been made by having long-term vision.”

A look at the *Emerging Trends* buy, hold, and sell projections shows retail space in San Francisco to be a good buy, according to 62 percent of survey participants. Buy opportunities continue in apartments, though rating values for that sector declined almost 20 percentage points from 2012. The majority of survey participants still see buying potential in the other three sectors; however, the sell rating for office space hovers around 31 percent, up 20 percentage points from the last report. Even with some concerns over pricing, San Francisco is still a market to watch. As one buyer says, “We have been and

EXHIBIT 3-10

U.S. Retail Property Buy/Hold/Sell Recommendations



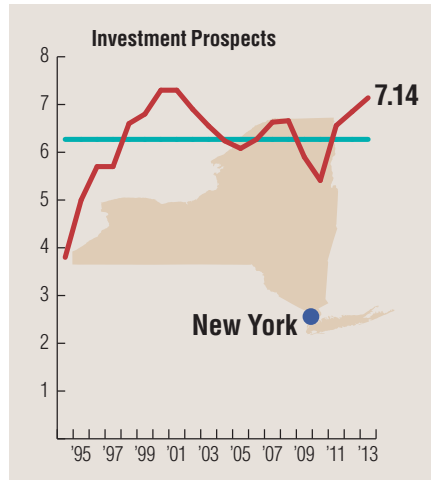


expect to continue to be very active in San Francisco.”

New York City (2). New York City makes a small move this year, stepping up two spots to second-best investment prospect. Rating values for development and homebuilding rose, but the city remained in the same position for each, ranked second and third, respectively. Even with the strong results, investors still seem concerned about the run-up in prices: “It’s no longer a safe haven of parking capital by chasing compressing cap rates in New York City,” and “New York markets are too expensive to support the rental price.”

Macro fundamentals for the financial capital of the world look secure because employment is expected to be back in the black next year, topping prerecession peak job numbers in the latter 2000s by almost 14,000. Demographics for the city prevail, with 20 percent of jobs being in the growing education and health care sectors and an important echo boomer population that represents 16.5 percent of the population. Service-type jobs continue to develop, but a lag in goods-producing jobs is a concern.

Though one interviewee calls New York City an overpriced market, survey participants disagree in regard to buy, hold, and sell suggestions for next year. Over 53 percent of interviewees give the city a top buy rating for office space.



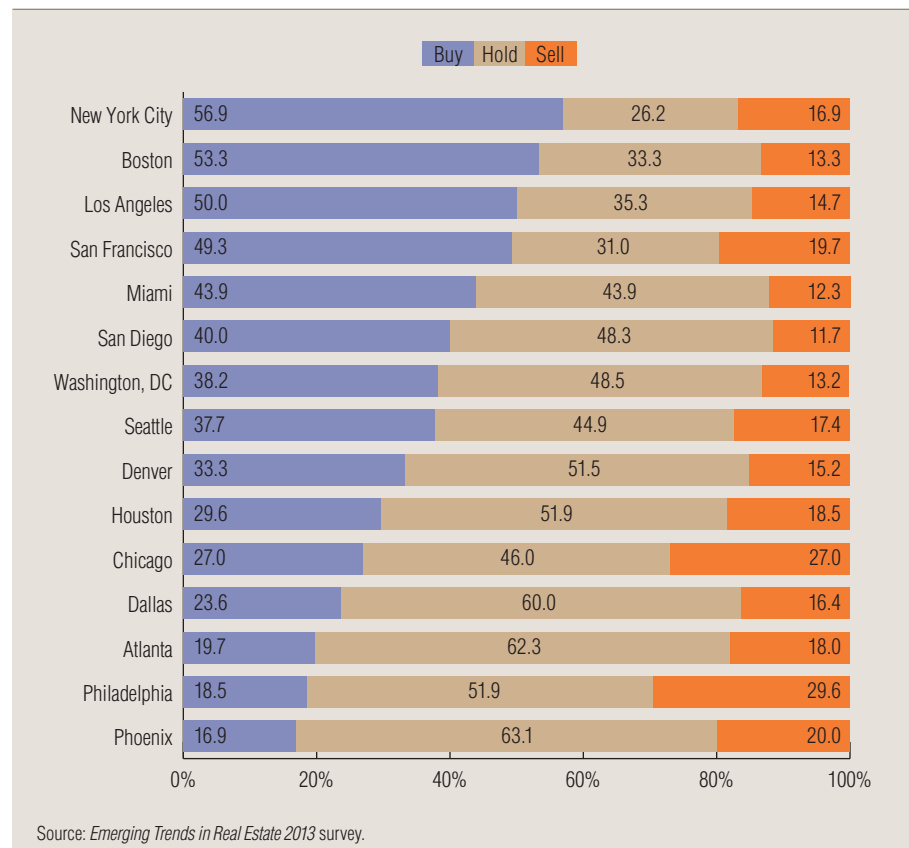
Only 14 percent believe it is time to sell office properties, some believing “there will continue to be a negative impact by financial services fallout and shrinking

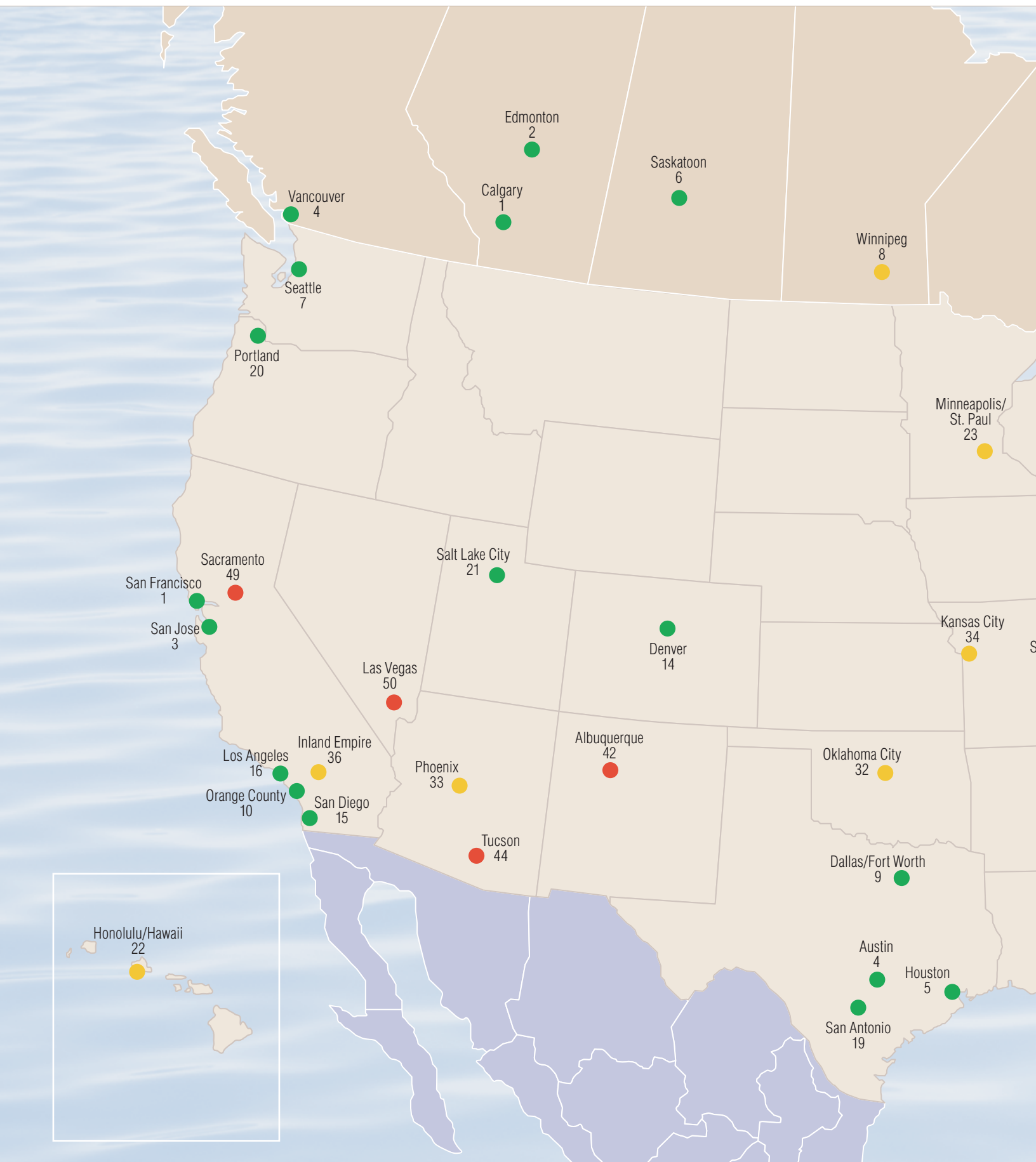
head count.” Hotels are the sector of most interest, receiving the highest buy rating from 57 percent of those surveyed. One interested investor notes, “The New York hotel market has absorbed 5,000 rooms and it is still very tight, so there is opportunity there for more development and growth.” Even with the spike in commercial real estate prices, investors seem to have the same level of interest in New York City, possibly attempting to “take on lease-up risk.”

San Jose (3). Only an hour’s drive south of San Francisco, the San Jose technology corridor continues to be a market to watch, according to results. In 2013, San Jose and the broader Silicon Valley will continue to generate jobs in a variety of fields, but most will be in high technol-

EXHIBIT 3-11

U.S. Hotel Buy/Hold/Sell Recommendations





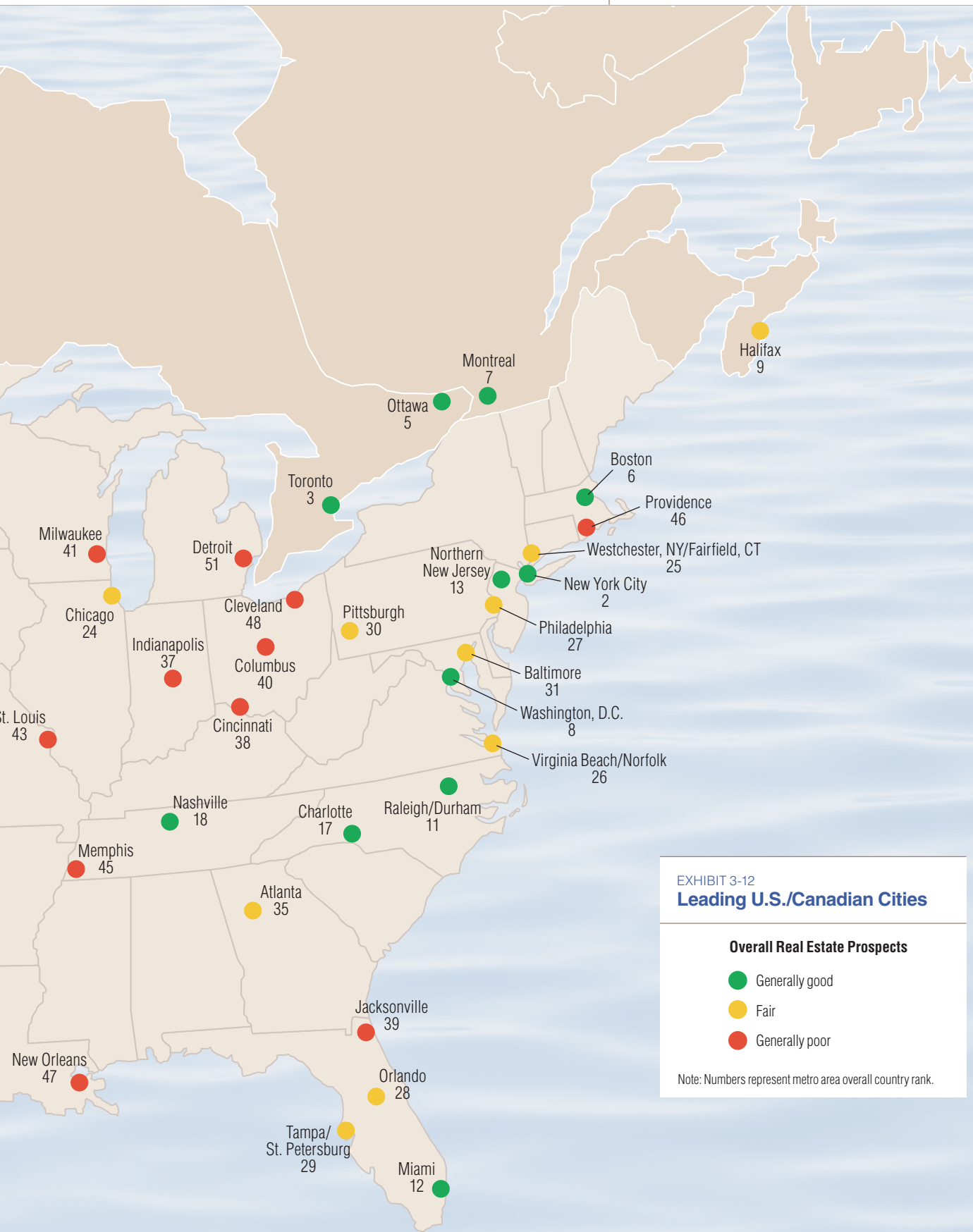
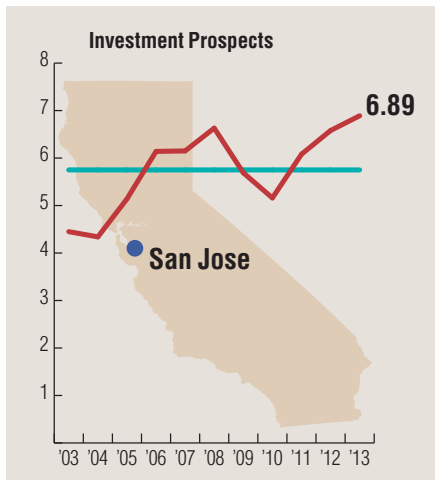


EXHIBIT 3-12
Leading U.S./Canadian Cities

Overall Real Estate Prospects

- Generally good
- Fair
- Generally poor

Note: Numbers represent metro area overall country rank.



ogy. Based on 2013 projections, the San Jose area will generate close to a total of 50,000 jobs since 2007, mostly in the high-tech industry that makes up over 25 percent of its total employment. Industrial diversity is limited in San Jose and could be a concern for investors (see appendix). However, the more than

6,600 technology companies based here employing over 255,000 people make it an area of interest. “There is risk in San Jose and technology, but established tenants with growth potential are a big draw.”

The city improved its investment prospect rank from seventh to third and scored its highest historical value of 6.89. Its higher ranking in development and homebuilding is consistent with its core of young, well-educated, and highly paid employees. San Jose is a fairly supply-constrained market (exhibit 3-13). However, institutional capital will be moving toward this smaller market in an attempt to beat competitors. As one interviewee says, “We’re on the upswing, and the early bird catches the worm.”

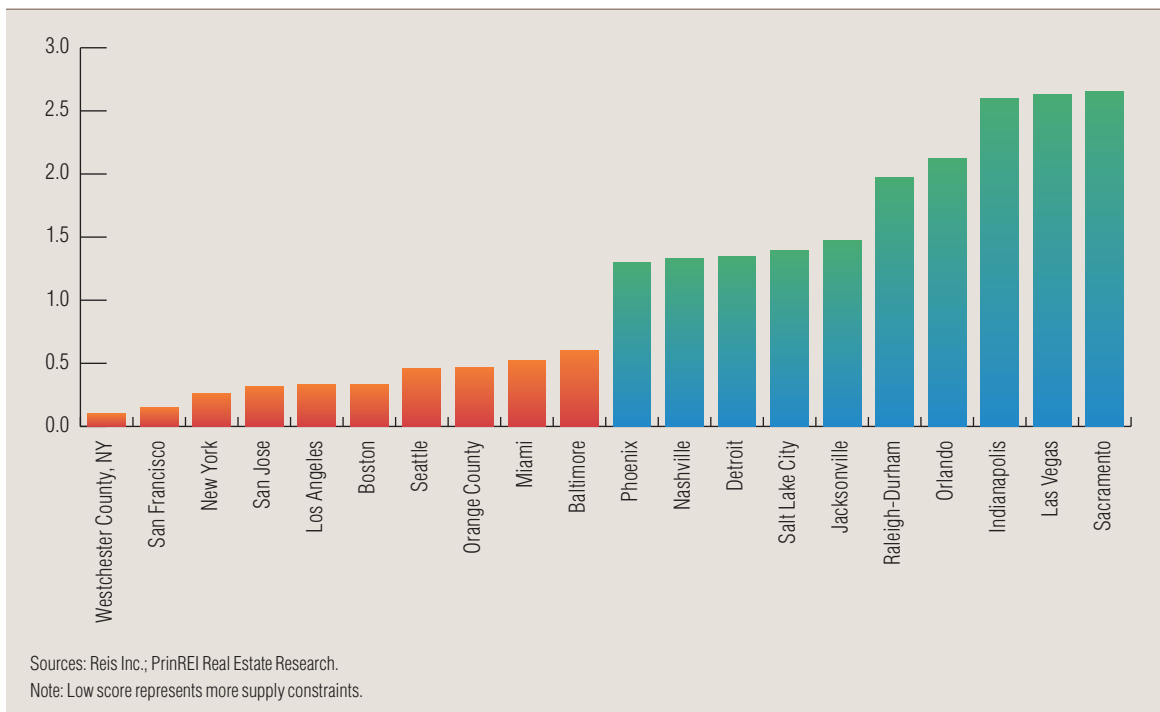
Austin (4). In 2013, Austin looks set to continue to impress individuals and attract institutional investors. “Austin will be a winner next year,” and “Austin, Texas, offers a lot more job growth and possible increase in income,” are

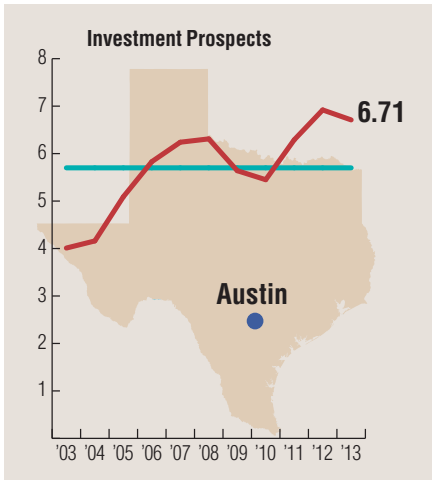
among the comments from interviewees. In the 2013 results, Austin took a few steps back in its ranking for investment prospects, from second to seventh, and in homebuilding, from second to fifth. The rating value for development rose, but the city remained fourth in rank. “Cranes are all over the place in the city,” and “Technology remains a key driver” are comments signaling that Austin will continue to grow.

Expansion of commercial real estate in Austin looks likely with a population increase of 2.3 percent anticipated next year, pushed by the echo boomer demographic that makes up 17.3 percent of the total population and has increased in number by over 25 percent during the past ten years. Completions in 2013 are expected to represent 2.8 percent of Austin’s total real estate stock (exhibit 3-14). Growth is good, but Austin’s past volatility should be a concern. According to CBRE Econometrics, office vacancy

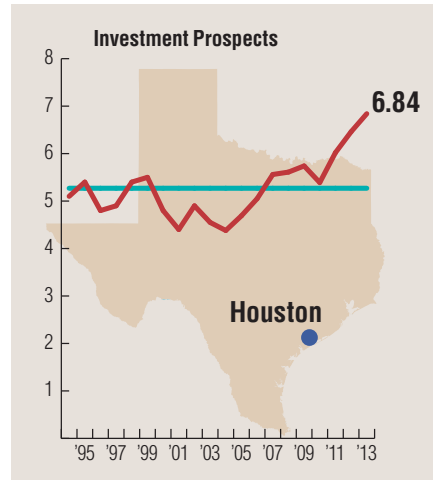
EXHIBIT 3-13

2013 Supply Constraints: Most and Least Constrained Metro Areas





rates that hovered around 5.0 percent during the dot-com bubble had jumped above 20 percent by 2002 after the bubble burst. Predictions place office vacancies closer to 10 percent in 2013 and 2014. Even with a booming technology market, a great university, and the state capital, Austin has an industrial diversity rating of 0.68, only average compared with its peers. Great opportunities exist in Austin, but reviews are much more mixed than they were last year. “Austin has good components but is just considered somewhat risky.”



Houston (5). “Energy, energy, energy.” Not only is energy-related employment one of the driving forces behind the Houston market, but the amount of energy expended by interviewees expressing their enthusiasm for the city’s real estate outlook is overwhelming. “You can buy now at a higher cap rate and benefit from growth over the hold period”; “We love the demand coming from the service industry in the energy renaissance”; and “Houston is a winner.” Survey results support these statements: the city’s investment prospect rank jumped from eighth to fifth, registering a value of 6.84, far exceeding the city’s 20-year survey average of 5.27. Development prospects for the area look good as well, the rating value rising, but the city’s ranking only advanced one position. The ranking for homebuilding prospects, however, fell back one place: housing starts, completions, and sales seem minimal compared with those of other Texas markets. This slower movement might be caused by a bust in apartment interest. Multifamily vacancies are forecast to be 6.8 percent in 2013, 2.3 percentage points below the city’s ten-year average. The cost ratio of renting vs. owning a home in Houston is 1.23, signaling that it is still cheaper to purchase a house. It is no real surprise, but survey participants believe the main buying

opportunities are in the industrial sector. Fifty percent believe that space in Houston is worth taking a chance on. “Houston ports are very attractive” and “Panama Canal widening should help” are a few outlooks on the industrial and manufacturing arenas. Office space received a buy rating from 43 percent of survey respondents, but some question those results: “I would be careful about putting office dollars there.” Apartments are still rated a buy overall, but 30 percent of survey participants say, instead, that now might be the time to sell. Survey results confirm that the Houston market is worth a look in 2013: “Houston has endured better than we thought.”

Boston (6). An increase in high-technology and biomedical research and development employment continues to take the lead, increasing investor interest in the Boston market. Part of the city’s stability occurs because 20 percent of its jobs are in health care and education (see appendix). Even after combining the third-best walkability and transit scores with some of the best colleges and universities in the nation, the city has shown only a limited ability to attract echo boomers, with that demographic constituting only 14.2 percent of its population. Boston’s appeal may be limited by its high business and living costs. Still, survey results are great for the Boston

EXHIBIT 3-14

PwC Pipeline Analysis 2013**Total Completions as a Percentage of Total Real Estate Inventory****Top 10**

Austin	2.8%
Charlotte	2.0%
Boston	1.8%
Salt Lake City	1.7%
Seattle	1.6%
San Antonio	1.6%
Inland Empire, CA	1.6%
Raleigh-Durham	1.5%
Albuquerque	1.3%
Denver	1.3%

Sources: PwC; CBRE; REIS.

Note: Apartment unit size is estimated at 850 square feet; hotel room size is estimated at 500 square feet.

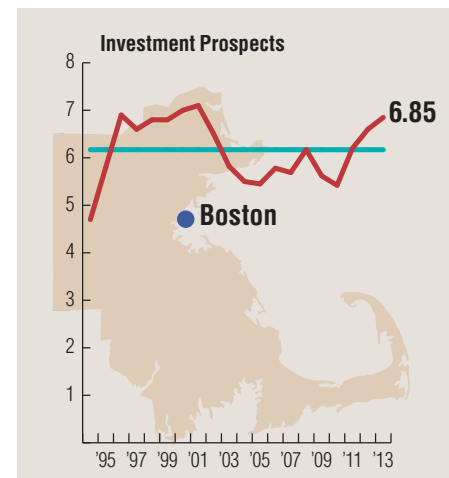
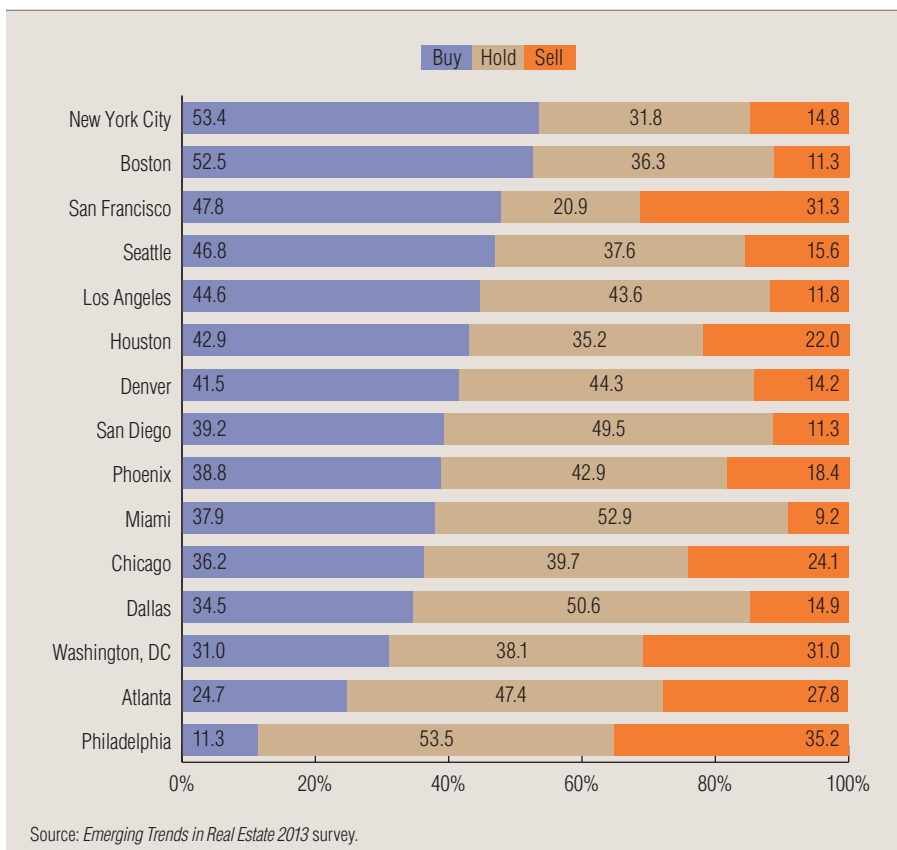


EXHIBIT 3-15

U.S. Office Property Buy/Hold/Sell Recommendations

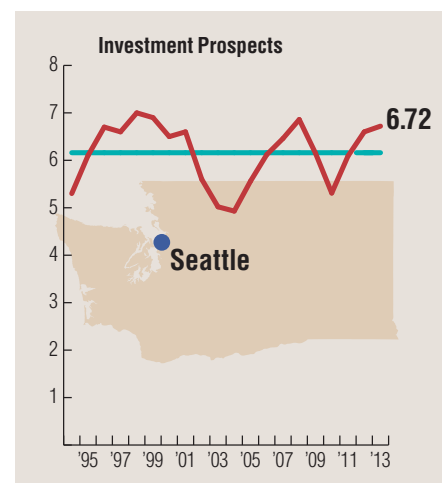


metro area. Investment prospects posted a 6.85 value, the highest since 2001, and the city's rank jumped one position. Its rankings in development and homebuilding each advanced two spots, to sixth and eighth, respectively. "We consider the major cities, and Boston is one of the best we're looking at."

According to *Emerging Trends* interviews and survey results, extreme interest exists for a variety of buying opportunities in Boston. The majority of participants now believe the time has come to buy in the apartment, hotel, office, and retail sectors. Comparing these results with those from 2012, sell recommendations are slightly up, but nonetheless investors want Boston apartments. Apartments in Boston scored the highest of all 15 markets covered, with 59.7 percent of

respondents thinking 2013 is the time to buy. "Boston for office," states one investor, and 52 percent of participants agree, making office space a buy. Like last year, industrial is considered a hold.

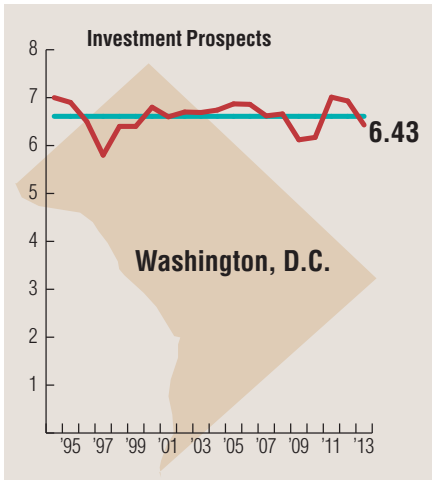
Seattle (7). "Seattle for the risk/reward ratio; it has diverse economies and good quality of living." As the global center for the software industry, Seattle continues to be the focus of many domestic and global investors. "Seattle belongs in the primary market category," one investor states. Rankings for investment and homebuilding remain at the sixth and seventh spot, respectively. Homebuilding might struggle as apartment interest increases, with "a definite suburban-to-urban movement taking place." However, the city's ranking for development



dropped one place to eighth. Even with some ranking declines, rating values for each of the categories improved. "Seattle is experiencing terrific momentum in job growth, with tech companies taking up most of the well-located vacant space." For 2013, job growth is projected at 1.2 percent, 50 basis points above its ten-year average. The echo boomer population has expanded 20 percent over the past ten years, making Seattle one of the best markets for younger adults. "Strong companies such as Amazon, Starbucks, Boeing, Microsoft, Nordstrom, Gates Foundation, and Costco have all been hiring and absorbing space of late."

With this employment and office absorption, 47 percent of survey respondents recommend the purchase of office space in 2013, while those recommending sales fall below 38 percent. Interest is also very strong in industrial space, with over 51 percent indicating now is the time to buy. Investors favor Seattle industrial space for a few reasons, including the "industrial-to-mixed use transition taking place for many suburban industrial and business park sites," as well as the city's position "serving as the main corridor to Asia."

Washington, D.C. (8). "I think that, long term, D.C. is going to continue to be a super-strong market," one interviewee says—though survey participants did not seem to agree. For 2013, declines were



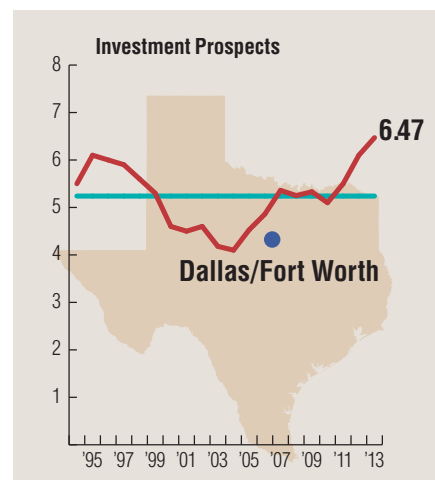
found in the investment, development, and homebuilding rankings. The nation's capital has a lot on its plate in the last quarter of 2012 with the presidential election, and the outcome will be a key determinant of what follows. Practically since the recession, commercial real estate prices have risen, with investors regarding D.C. investments as "recession-proof." However, concerns about overbuilding and costs continue to lead discussions about interest in D.C. Investors believe "institutional demand has fallen in the D.C. metro due to a politically ambiguous environment," and "Washington, D.C., has lost demand for high-end space."

Only a 50-basis-point increase in the number of jobs is expected next year, falling below D.C.'s ten-year average of 1.1 percent growth. Washington's unemployment rates are far lower than the national average, but the outlook after the election for direct government employment and subcontracting jobs remains in question. Washington, D.C., combined with the Maryland and northern Virginia suburbs, has seen technology and energy-related employment increase; however, that growth may not be enough to offset what might occur in the near future. Nevertheless, the market continues to be a hub for well-educated echo boomers. Its infill-focused neighborhoods, combined with walkability and extensive

transit service, are a draw for many; say interviewees: "We will stay active in D.C.," and "Prices won't turn us away from Washington, D.C."

Buy rating values in all five property sectors were down this year when compared to last year's survey. In addition, the majority of survey respondents gave hold recommendations for the office, industrial, retail, and industrial sectors. An interesting trend was that the majority of participants recommended selling in the hot, pricey apartment sector even though D.C. home prices are still down 24 percent from their peak and apartment rents have continued to rise. Still, some owners believe the time is right to move on from the city's multifamily sector and take advantage of current gains. Based on results, it is safe to say that D.C. "has cooled a little."

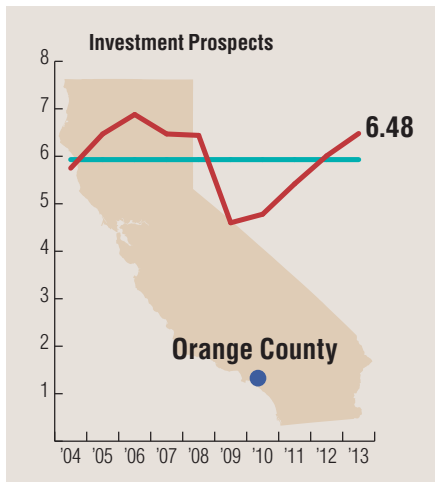
Dallas/Fort Worth (9). "What our economy needs is employment, and Dallas has been a great market in providing it." Through the end of 2013, Dallas is expected to have added over 230,000 jobs since 2007. Of the markets included in the survey, it ranks behind only its Texas neighbor, Houston, as a job provider. Next year unemployment rates are forecast to fall to 7.2 percent, 1.2 percentage points lower than the U.S. rate of 8.4 percent. The Dallas/Fort Worth industrial diversity index of 0.81



shows that its job base is one of the most diversified of the 51 markets covered. With employment leading the way, survey participants believe in Dallas, ranking its investment prospects tenth with a value of 6.47. Its development ranking jumped as well, by two spots, but its value for homebuilding did not gain as quickly as other indicators and the city's ranking dropped two positions. A relatively low 3.2 percent delinquency rate on home mortgages and a quick judicial process on foreclosures make distressed homes more accessible for purchase if financing is available. Combine this source of housing supply with estimated apartment vacancy rates of 5.2 percent next year, and a decline in the homebuilding outlook is easier to understand despite the strong market.

Even with projections of continued growth, "hold" seems to be the word regarding hotel, retail, and office space. One investor states, "Rents in Dallas have not moved in 25 years, and efficiency in office space doesn't increase development." Similar to other markets, over 51 percent of survey participants would still suggest buying apartments in the coming year: "Dallas multifamily looks good to us," and "would consider acquiring land to flip to developers."

Orange County, California (10). With total population of more than 3 million, Orange County comprises 34 cities. Some of the largest are Santa Ana, Anaheim, Irvine, and Huntington Beach. California's economy continues to struggle, and home prices will still be down more than 27 percent in 2013 from their prerecession peak. Even with that decline, median home prices throughout the county are about \$513,000. At this level, the rental/homeownership ratio is 0.78, suggesting that people prefer to rent and causing a projected decline in apartment vacancy rates to 5.8 percent next year—2.6 percentage points below the ten-year average. Employment throughout Orange County continues to

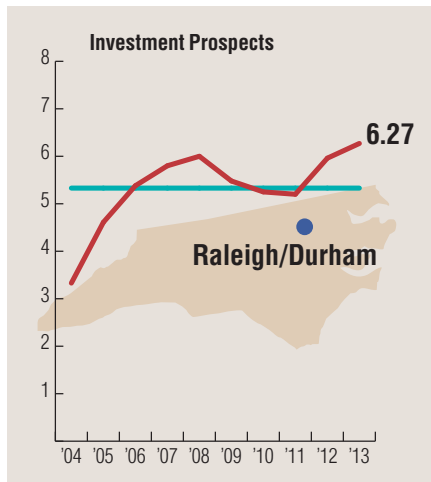


put a strain on markets, with employment remaining below the prerecession level. The unemployment rate is 2 percentage points above the ten-year average.

Investors still believe in investments in Orange County, however: survey results show increases in the county's rating value and ranking as an investment prospect. It ranks ninth in the investment and homebuilding categories, both improvements from last year. However, its ranking for development prospects dropped two spots to 19th overall.

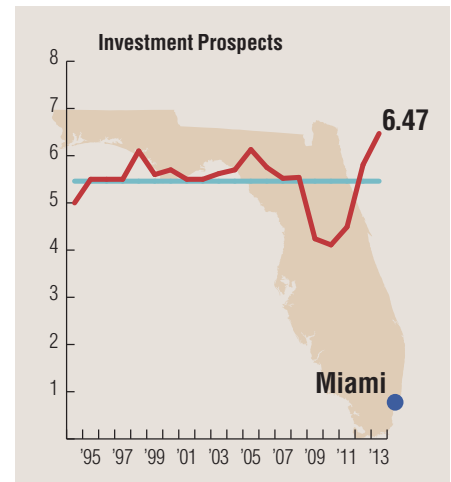
Raleigh/Durham (11). "All things are looking good for the Raleigh area," says one investor. Survey participants could not agree more: the cities' development prospect ranking moved up five spots to tenth, and homebuilding jumped four spots to 11th overall. Supply constraints for commercial real estate play a factor in the development bump (exhibit 3-13). The metro area's investment prospect value rose, but its ranking stayed at 15th.

This eastern-seaboard, centrally located area continues to be a hub of education: the city ranks fifth overall in that field. "[Raleigh/Durham is] one of our top markets to watch next year," states an investor. A very affordable cost of living, substantial job growth, and a diverse employment base have continued to stimulate the economy here. For 2013, Raleigh tops the survey's forecast



for highest ratio of net migration to total population (exhibit 3-9) and is one of the top five in GMP per capita, indicating to investors that this market is "one to watch." The importance of the housing market as a backbone for commercial real estate is visible here, as home prices are expected to increase another 1 percent next year, and Raleigh/Durham is one of the few metro areas out of the red since the recession. This situation, combined with a foreclosure rate just shy of 4 percent, puts the area in a good position for future growth.

Miami (12). Cranes are back in south Florida, and the condominium market has moved from bust to boom. After suffering from overdevelopment and cheap credit in 2007, the popular Miami condominium market collapsed. Five years have passed and the demand is back again, not only from domestic capital, but also from foreign investors who are swooping in to take advantage of the demand. Financing does not seem to be an issue this time around because many investors are offering all cash. Investment plans include leasing to tenants who may have lost homes in a city where foreclosure forecasts exceed 18 percent. Since the start of the recession, median home prices are down more than 50 percent, and apartment vacancies should slip below 3.5 percent soon. With continued housing troubles, investments in apart-

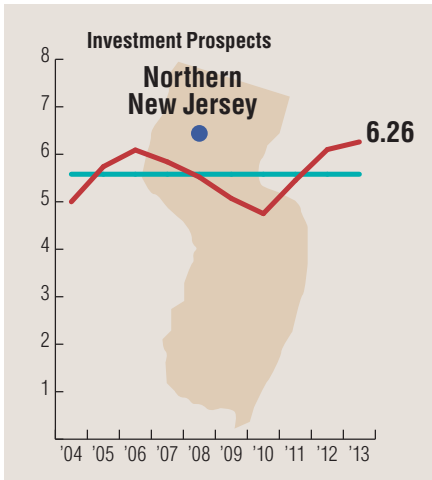


ment and condominium rentals seem like a wise move. "We like the pace and direction of rentals here," claims an investor.

This improvement in the housing outlook, combined with an interest in industrial space, has sparked a new enthusiasm for Miami commercial real estate. Survey results display significant increases in investor prospects for 2013, with the city's ranking jumping from 17th to 11th, but even greater improvement in development prospects, with the city's ranking moving from 26th and "modestly poor" to 11th and "modestly good" this year. The city still ranks 16th for homebuilding, but the industry's rating has gained some ground from last year.

Half those surveyed recommend buying apartment properties as this sector tries to compete with condominiums for tenants. Of even more interest is industrial space, with 52 percent of participants believing now is the time to make a move in this sector. "Facilities around Miami airport will serve well for the large volume of perishable goods that are traded between the U.S. and Latin America." Office and retail remain a hold because high unemployment and lack of job growth remain a concern.

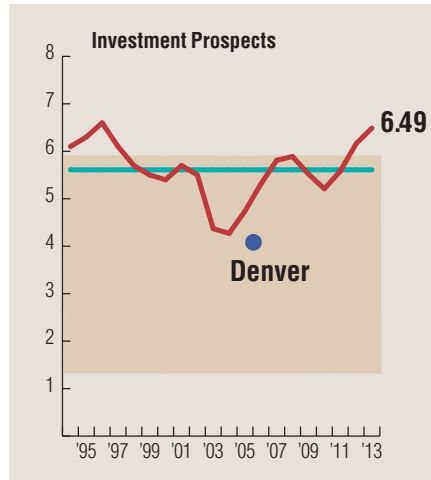
Northern New Jersey (13). The northern New Jersey market consists of a handful of counties, with Newark being the largest city in the market. A huge asset for the



area is a diverse and growing number of professions, including high technology, financial services, and health care. With this diversity, GMP forecasts are set to increase 1.5 percent in 2013. Even with growth in employment slowing, northern New Jersey is in a prime market location that, combined with robust infrastructure, should make it a target for real estate investors. Growth in household numbers remains minimal, but housing prices have not been as hard hit as those in other markets. Even with controlled prices, homeownership makes more economic sense than renting, as seen by a cost ratio of homeownership to rentals that slightly tops 1.0.

Survey results show that northern New Jersey's ranking for investment prospects has fallen three positions to 16th. Development prospects moved in the opposite direction, up four to 12th, and rating values for homebuilding rose, but the market remained stable in the rankings.

Denver (14). With only 4 percent of homes in foreclosure and 2.5 percent of homes sitting at 90-plus days delinquent, "Denver wasn't directly in the crosshairs of the housing downturn." The city's homebuilding rating value and rank in the survey demonstrates the validity of this opinion, rising 0.94 and one spot, respectively. Denver's economy has



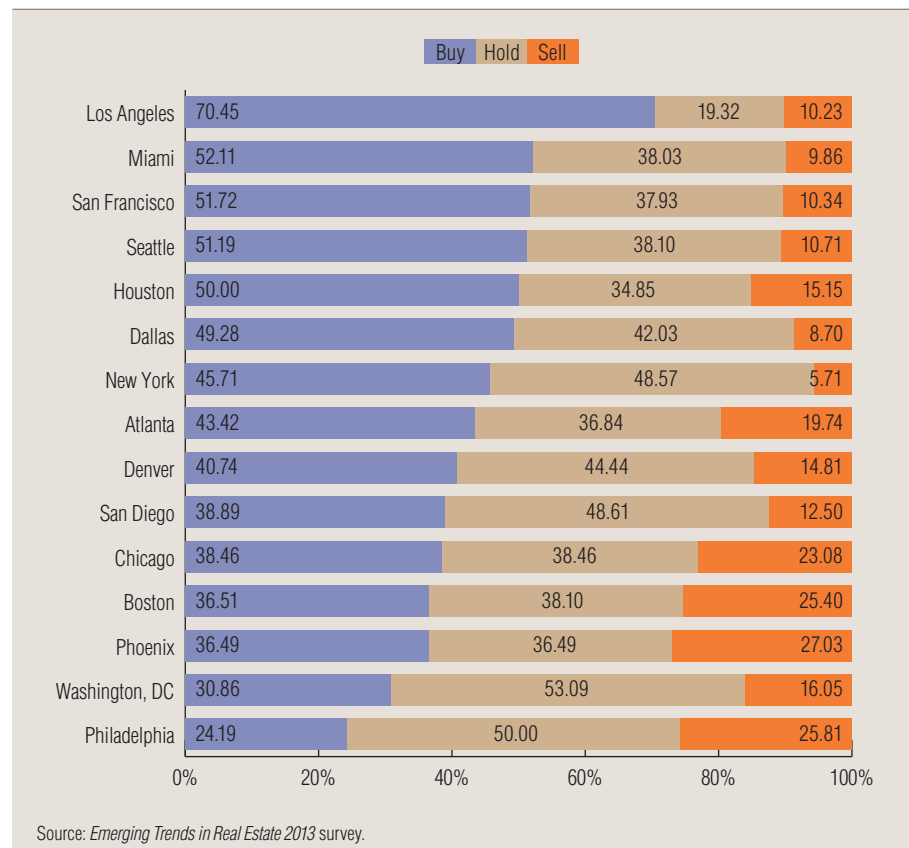
remained healthy, maintaining the ability to absorb a diverse employment base. The city's industrial diversity rank, 0.83, is one of the highest among all metro-

politan areas. A big benefit for Denver is its educated workforce, which is concentrated in growing industries such as high technology (6.7 percent) and energy (0.4 percent). "Denver is attracting attention with energy industries," an investor notes.

From an investment perspective, "Denver has strong growth potential." Results show the city moving up three spots in the investment prospects rankings. An attraction is the city's central location in the country's southern and western regions, as well as Denver's ever-expanding international airport, which offers access to national and global destinations. With growing sophistication, Denver offers "good quality of living." Although survey results show Denver growing in appeal for investment,

EXHIBIT 3-16

U.S. Industrial/Distribution Property Buy/Hold/Sell Recommendations

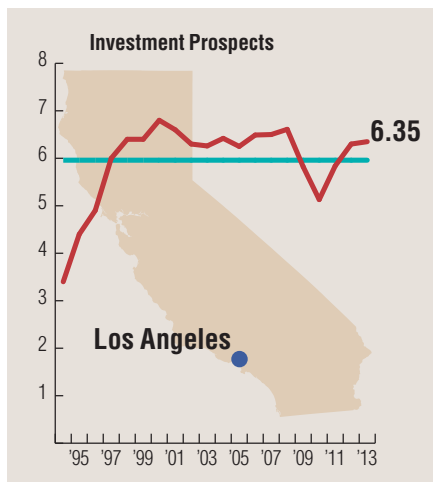


development prospects declined three notches.

San Diego (15). The fourth of five California cities/regions to make the *Emerging Trends* top 20, San Diego shares characteristics with the others. Home prices continue to be considerably lower, even though foreclosure rates are somewhat stable. The percentage of echo boomers in the population, 15.8 percent, is worth noting; however, much of this echo boomer population consists of lower-paid military personnel stationed in the area. The developing high-tech sector is significant, but unemployment levels are still above the national average.

Even though San Diego is not an overly diverse city in terms of employment, more than 40,000 jobs have been filled since the peak. Also, the city's tourist traffic continues to improve, increasing revenue for the area. With these and other attributes, investment prospects moved up three positions. Even with these gains, however, the city's ranking for development prospects fell four spots. The only sector to receive a buy rating is apartments, with 54 percent of survey participants still seeing some opportunities there. Some light interest in the retail arena also exists, but most respondents suggest a hold in 2013.

Los Angeles (16). Interviewees' comments and survey results were very mixed



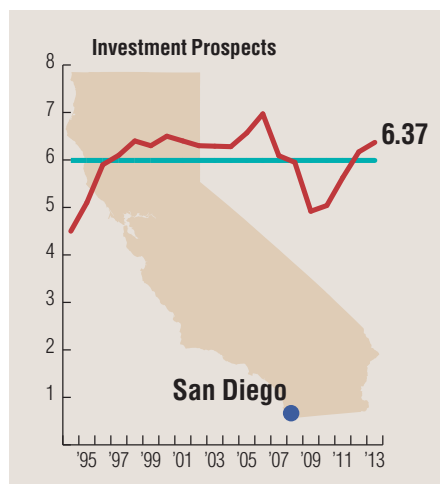
on the Los Angeles market. On the positive side, the number of households in the area is projected to rise by over 1 percent in the coming year, and over 15 percent of the population is made up of up-and-coming echo boomers. Interviewees provide quotes such as, "L.A. is bulletproof," "we are completely positive on L.A.," and "opportunities abound in the city." Los Angeles's constant flow of capital through tourism and entertainment always helps create interest in commercial real estate, as can be seen in the buy, hold, and sell recommendations. The Los Angeles industrial market dominated the buy column: over 70 percent of survey participants suggest buying industrial space next year—18 percentage points higher than that for Miami. The majority, 59 percent, suggest buying in the apartment sector as well. The recommendations for office space were almost exactly split between buy and hold.

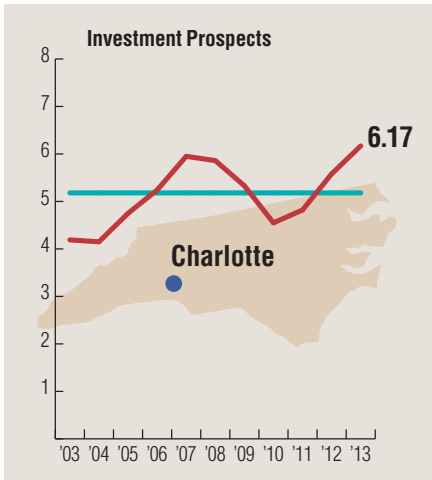
Although this all sounds good, other numbers must have been a concern for survey participants. Los Angeles's job growth is projected to be minimal next year—only a 30-basis-point increase over 2012. Compared with totals from 2007, Los Angeles is still projected to be over 140,000 jobs in the hole through next year. These factors and others (see appendix) might be the reason the city did not perform well in investment, development, and

homebuilding prospect rankings and rating values. The investment prospects rose only 0.05, compared with a 0.32 average increase for all cities in the survey. This result caused Los Angeles to fall five spots in the investment rankings. Development had a larger rating value decline and fell five spots as well. Homebuilding was the only sector to rise in the rankings, climbing from 17th to 14th. Home starts are projected to increase 27 percent next year, with completions hovering around 13 percent.

Charlotte (17). "Going into secondary markets, but only with safe bets—Charlotte." The interest in Charlotte's investment, development, and homebuilding prospects posted significant improvement compared with 2012 results. Mostly understood as a big banking and financing town, this market has continued to expand, with a variety of businesses relocating to Charlotte for its high quality of life, low cost of business, and world-class international airport. Since 2011, 37 companies have moved to the area, creating more than 8,000 jobs. From the last peak through 2013, Charlotte is forecast to add nearly 30,000 jobs, making it one of the stronger secondary markets to watch. Businesses are not the only thing coming to Charlotte: net migration as a percentage of population is expected to be 1.5 percent in 2013, and forecasts show a 2.5 percent increase in households. Even with these growth numbers, some interviewees still have concerns: "Charlotte is subject to what banks do," and "We see Charlotte as a risky metro in spite of a relatively strong economy, due to its dependence on two large banks."

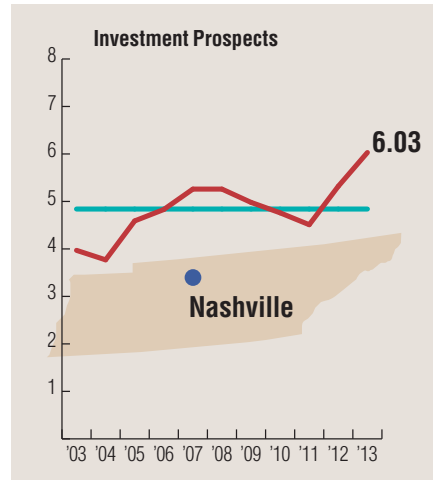
Nashville (18). Vanderbilt University and a Nissan North America manufacturing plant are only two of a large set of diversified employers found in the Nashville area. These varied forms of employment help the market score an industrial diversity index of 0.80. Growth in this market looks to remain slow and steady, with 2013 employment growth forecast at 1.3 percent. "The market looks good in Nashville,





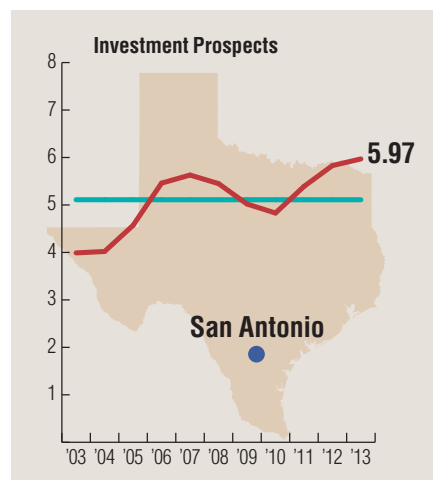
with both population and job growth.” Retail spending in the city continues to increase at a greater pace than in most markets. Limited housing losses might stimulate that number: prices are down only 13 percent from their peak, and expectations are for an additional increase of 1.5 percent in median home prices next year. Even with housing remaining somewhat stable, “there are a lot of apartments under construction in Nashville, about half in the core or close.” PwC analysis shows that multifamily completions will constitute 1.8 percent of the total stock in 2013. Similar to the continued trend of “American infill,” “there has been a huge shift toward the more urban areas of Nashville for the apartment sector.”

This growth can be seen not only in the macro trends, but also in the investment, development, and homebuilding numbers. Investor sentiment improved, raising Nashville’s investor prospect ranking to 21st from 27th. A more significant leap was found in the development arena, where the city moved up five spots to 13th. PwC’s pipeline analysis indicates that over 1 percent of Nashville’s stock is being added next year. Besides an influx of apartments, “a new convention center is coming on line, along with four new hotels, which will boost tourism next year.” Tourism is a key component of Nashville’s economy, and according to interviews and survey results,



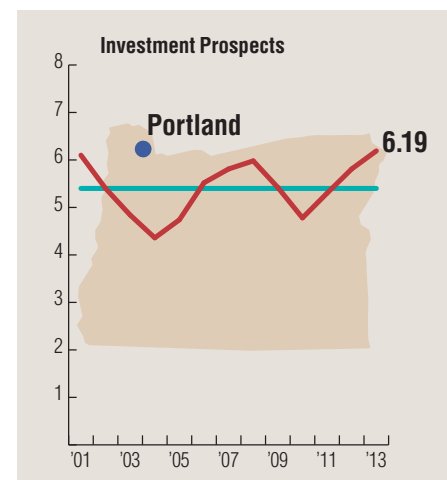
many investors may be packing their bags to check out this city.

San Antonio (19). It’s official, and as expected: all four major Texas markets make the 2013 *Emerging Trends* top 20. San Antonio had the lowest total rating values of the four, and its investment, development, and homebuilding numbers reflect why. This year’s values for investment prospects showed a minimal gain, but not enough to keep pace with the other cities, pushing the city’s ranking down six spots. Development dropped four places, and homebuilding fell eight positions. Even with declining development rating values, San Antonio continues to be a growing market. PwC’s forecasts show over 1.5 percent of total stock being completed



next year. San Antonio should have no problems filling that space because job growth is forecast to increase 2.5 percent, and close to 100,000 jobs have been filled since 2007. Overall economic growth looks healthy for the city because GMP will rise 2.6 percent, a slightly slower pace than the ten-year average of 2.9 percent. A strong military base combined with over 15 percent employment in health and education is a good formula for future expansion in this market.

Portland, Oregon (20). Portland’s economy displays stability but few signs of quick improvement. Employment diversity is limited, with jobs concentrated mainly in manufacturing, health, education, and government work. Even with rising numbers of younger adults, Portland is still composed mostly of a limited-growth, aging population. With a home foreclosure rate of 4.8 percent and median prices still 20 percent below their peak, regional consumer spending might still suffer. In 2013, apartment vacancies are expected to reach 1.9 percent, with 1.0 percent of the entire multifamily inventory added to the mix that year. Therefore, commercial real estate opportunities exist in Portland, but investors will have to take on more risk in their search. As for investment prospects, Portland advanced one spot to 17th. Declines are forecast in the other two categories next year.



Other Major Markets

Chicago (24). “Chicago has been pretty slow to come back.” One of the big six, Chicago’s recovery cannot compare with that of the other five. Still a major industrial and business area, Chicago’s economy seems to have stalled. In 2013, population growth will be minimal, and many current Chicago residents are migrating away from the city. Job forecasts are negative, and the losses will total close to 200,000 since the last peak (exhibit 3-2). Manufacturing and government jobs make up over 20 percent of employment, but both will struggle in the near future. As in most markets, the majority of participants rate apartments a buy. However, the other four property sectors should be put on hold next year. Even with those results, one interviewee is “looking to buy or develop industrial in Chicago.” Despite macro concerns, survey participants rank Chicago one position higher for investment and development opportunities. Commercial real estate prices might not have pushed as high here as in the other major markets, but taking on this amount of risk should be the bigger concern.

Philadelphia (27). Survey results indicate that 2013 will be a hold period for all property sectors. Even though the apartment sector is a hold, some disagree, stating “Philadelphia is the market for multifamily.” Sell recommendations outnumbered buy calls for office, industrial, and hotel space, but a hold strategy still prevails. Similar to the case in Chicago, next year’s population forecast is nominal and even 60 basis points lower than the national forecast. Job growth remains flat, with only a 0.6 percent increase expected. With a lack of jobs, no population growth, and negative net migration, Philadelphia offers few of the macro trends real estate investors seek. The city’s ranking for investment prospects fell to 27th from 24th in 2012. Surprisingly, development took two steps forward to 26th, even though PwC’s pipeline analyses show minimal completions scheduled, representing only 0.8 percent of total inventory.

Phoenix (33). This volatile market continues to make strides, but survey and interviewee results are mixed. For example, optimism—“We also think Phoenix is a market to watch”—is followed by pessimism—“We do not plan on investing in Phoenix.” Results indicate that opportunities exist, but doubts remain as to whether the risk-adjusted returns are worth it. Investment prospect values rose, but the city’s ranking dropped six spots to 29th. The ranking for development prospects moved up six spots, and homebuilding prospects did even better, jumping ten positions. There are still fewer jobs than during the prerecession peak, but next year’s projected job gains are 50 basis points above the national estimate. “Phoenix economics are starting to recover.” Strong metropolitan production is contributing to the recovery, but a housing market with a 50 percent price decline

continues to weigh heavily on investors. Of those surveyed, 49 percent believe the apartment sector presents buying opportunities. Views on the industrial sector are equally split between buy and hold, but hold is the dominant call for all remaining sectors. One interviewee has no interest right now: “I don’t think it will ever be a primary market—its downtown is fractured.”

Atlanta (35). Similar to the case for the other three major markets that failed to make the top 20, Atlanta’s loss of employment and the housing collapse affect interest in commercial real estate. Median home prices in the metro area have sunk below \$100,000 and are projected to decline another 60 basis points next year. Even with these difficulties, job growth is showing improvement and is projected to increase 2.6 percent. GMP looks strong as well and is projected to rise 2.9 percent in 2013, far exceeding the city’s ten-year average. Concludes one investor, “We will see more activity in Atlanta in 2013 as job growth emerges.”

With signs of improvement, investment, development, and homebuilding all make positive moves in overall rank. “Atlanta’s size is something you have to look at for investments.” As in many markets, apartments are one of the sectors suggested for purchases in Atlanta. The industrial sector registered a buy as well because increases in manufacturing, warehousing, and shipping are expected in the near future. Hold is the recommendation, however, for offices, hotels, and retail space.

Other Market Outlooks

Strong production, population, and migration are just a few of many positive signs for **Salt Lake City (21)**. “Salt Lake City is tertiary by size, but the recovery is far along and impressive.” A large gainer for investment prospects, Salt Lake moved from 30th to 19th. “Lots of high-tech companies are looking at SLC.”

Honolulu (22) provides a great quality of life, with a slow, steady recovery. “Job growth has stabilized,” states an interviewee. Honolulu’s housing remains expensive, but the market is not forced to battle significant loss of value. “Honolulu tourism isn’t going away anytime soon.” With that, Honolulu moves up in development but takes a few steps back in investment prospects. **Minneapolis/St. Paul (23)** provides well-educated and skilled labor in research and high technology. Unemployment has not been a concern for the city, because employment has escalated; the unemployment rate will be nearly 3 percentage points lower than the U.S. rate next year. “Peripheral opportunities are not getting much attention here.” Continuing to move up in the investment ranks is **Virginia Beach/Norfolk (26)**. The market does not have great job diversity, but stabilized growth makes this tertiary market worth a peek.

Next are two Florida cities: **Orlando (28)** and **Tampa/St. Petersburg (29)**. Survey results have both cities' investment prospect improving in 2013, but Tampa gained slightly more ground, edging out Orlando for the 25th spot. The opposite is true for development: participants believe Orlando has more opportunities. To settle the tie, homebuilding goes to Orlando. Both markets continue to deal with the many economic issues Florida has faced. Housing continues to be in the hole, but Tampa's recovery in median prices is a bit better. However, job losses have not been as harsh in the entertainment capital of the world for tourists. Because Orlando wins the battle, it gets the quote: "We see it in Orlando . . . those markets are back."

Pittsburgh (30) and **Baltimore (31)** are two originally blue collar-oriented towns that have been transformed in many ways over numerous decades. The *Emerging Trends* total ranking shows Pittsburgh edging out Baltimore by one spot this year. Baltimore has had an influx of echo boomers over a ten-year period and has an industrial setting that has been great for job growth. Pittsburgh's appeal is not as strong to a younger generation, but housing stability has helped the city's economy. Investment prospects for both cities are lower than last year's, with Baltimore taking a bigger plunge. Development prospects have also fallen, with Baltimore having a slightly higher rank at 30th. Finally, homebuilding is all Pittsburgh, which moved forward two spots compared with an 11-spot loss for Baltimore.

"We will see a push in one tertiary market—Oklahoma City," and "we are seeing many companies moving from the West Coast to Oklahoma." As an energy industry location, **Oklahoma City (32)** moved up four spots in the investment prospect ranks.

Not much change was seen in **Jacksonville (39)**, but resurgence may be on the horizon because the city's young people are moving into a diverse set of industries. The lack-luster housing market in **Albuquerque (41)** weighs heavily on this recession-ridden market; survey results show concern, as investment and development decline. **Memphis (45)** takes steps backward in all three categories, with limited industrial diversity and questionable future growth. **New Orleans (47)** may have seen some slight movement; nonetheless, government and service job numbers are in decline, and the city remains stagnant in investment and development. Economic dependence on the state government and homes at half their precrash value continue to hurt the **Sacramento (49)** market. **Las Vegas (50)** is still mired in the quicksand of foreclosures and home prices declines. Problems in key Vegas industries are also taking their toll, with education, health care, and service-related employment levels below average.

Chicago and Minneapolis are top performers for the Midwest in 2013, but many cities in this region will continue to face economic and real estate challenges. "We'd be way out in front, maybe even Middle America investing, but we

haven't gotten near that level." **Kansas City (34)** shows slight movement, up in investment and development as a result of a number of industrial opportunities. **Indianapolis (36)** shows signs of attracting interest with low business costs and solid demographics. However, the city's dependence on a limited number of employers might be a concern. **Cincinnati (38)** makes a considerable jump, rebounding with a multitude of industries involved in manufacturing, and wholesale and retail businesses. **St. Louis (43)** shows strong industry diversification but still struggles with job growth. The declining population in **Cleveland (48)** is causing all sectors to struggle, with only education and health services seeing any improvement. The economic woes for **Detroit (51)** persist, with no youth contingency, little diversity in employment, high unemployment, low job growth, and migration from the city. "The auto industry has come back somewhat, but you can only be interested in the top buildings in Detroit."



Property Types in Perspective

“Demand for space slowly but steadily comes back.”

In 2013, commercial and multifamily property sectors regain generally solid *Emerging Trends* investment ratings. Categories hold their relative rankings from 2012 in the survey, with perennial leader apartments in the catbird seat again, though noticeably leveling off, and retail continuing to lag, but recovering. Interviewees predict “Demand for space slowly but steadily comes back,” exhibiting “decent growth.” Industrial/warehouse and hotels show the biggest survey improvements, trailed closely by downtown office. Power centers and suburban offices remain investors’ least-favored subcategories. Except for apartments and industrial space, development prospects remain challenging. Interviewees note that “Despite one of the longest stretches of basically no construction” in commercial markets, “pent-up demand does not exist except in select cities.” Interviewees show mixed concerns about apartment construction on a market-by-market basis, but generally concur that “overdevelopment” will happen, just not in 2013. They also anticipate “more big-box industrial” development after a long postcrash hiatus.

Significantly, after the \$6 trillion loss in housing values during the recent recession, respondents begin to express hints of optimism about for-sale residential properties, especially infill and in-town housing, which score modestly good ratings. They also signal the need and opportunity to invest in infrastructure development and redevelopment across the country because facilities—roads, mass transportation systems, public buildings, sewage and water mains, airports, and rail stations—require substantial overhauls, expansions, or new construction.

EXHIBIT 4-1

Prospects for Major Commercial Property Types in 2013

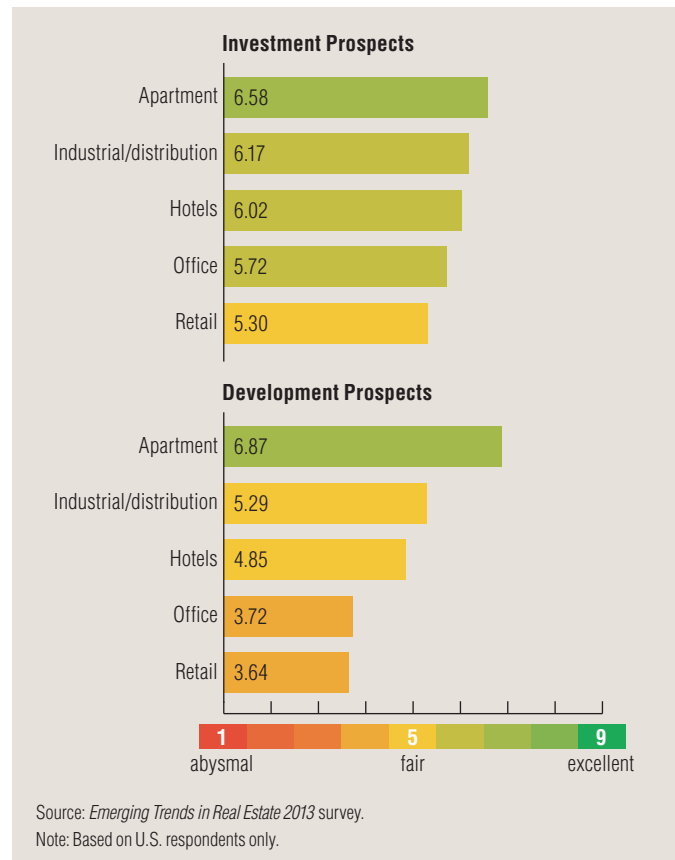
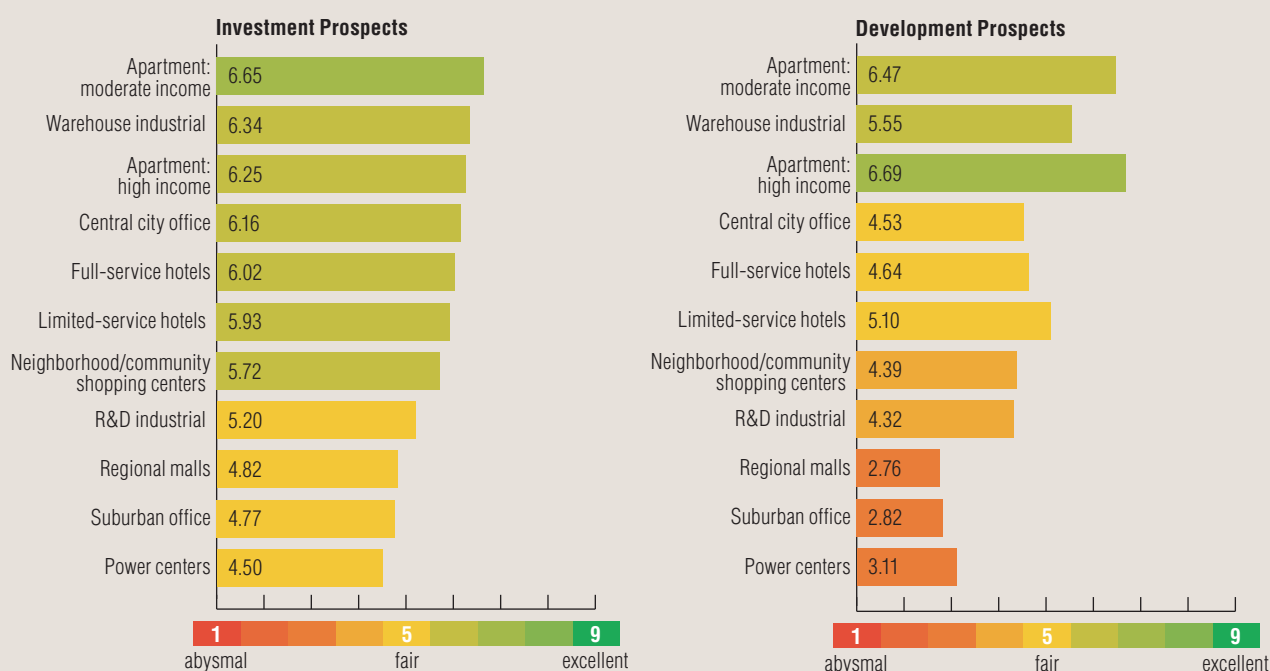


EXHIBIT 4-2

Prospects for Commercial/Multifamily Subsectors in 2013

Source: *Emerging Trends in Real Estate 2013* survey.

Note: Based on U.S. respondents only.

EXHIBIT 4-3

Prospects for Capitalization Rates

Property type	Cap. rate August 2012 (percent)	Expected cap. rate December 2013 (percent)	Expected cap. rate shift (basis points)
Apartment: high income	5.67	5.85	18
Central city office	6.15	6.17	2
Apartment: moderate income	6.11	6.27	16
Regional malls	6.37	6.51	14
Warehouse industrial	6.92	6.87	-5
Neighborhood/community shopping centers	6.97	7.05	8
Full-service hotels	7.27	7.38	11
Power centers	7.42	7.63	21
R&D industrial	7.62	7.64	2
Suburban office	7.90	7.94	4
Limited-service hotels	8.16	8.24	8

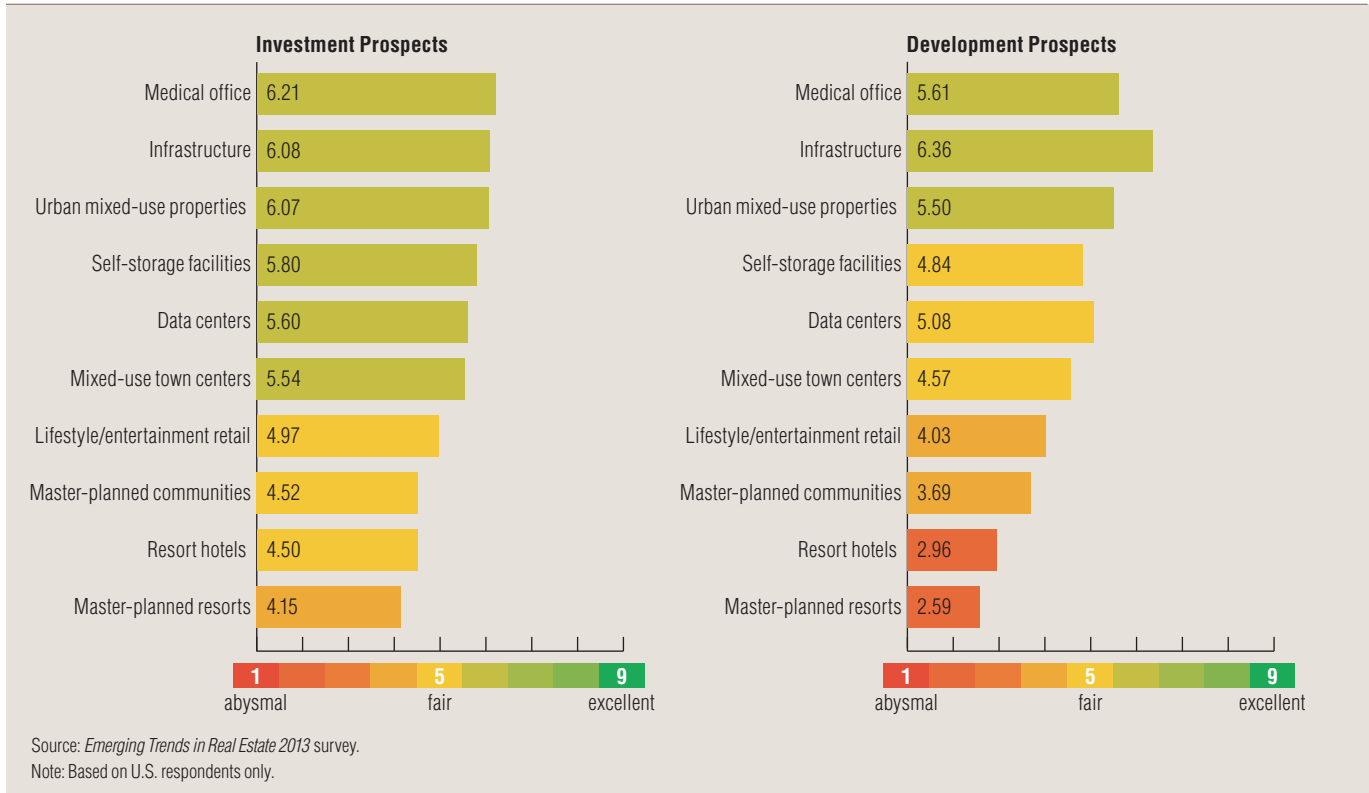
Source: *Emerging Trends in Real Estate 2013* survey.

Note: Based on U.S. respondents only.

Core properties reach or approach pricing zeniths—apartments look “past peak,” central business district office space appears “at peak, and prime industrial may be within 10–20 percent of peak.” Respondents predict cap rates will remain in a narrow range between now and year-end 2013, with most sectors experiencing slight increases and only industrial/warehouse showing further tightening (exhibit 4-3). High vacancies and limited expansion interest by tenants will likely result in leases still rolling off to lower market rents in offices, retail space, and some warehouses. Demand pickup should improve, but stay in second gear. “Commodity properties, except apartments, will continue to struggle to establish pricing power with tenants.”

Investors like “bite-sized specialty types.” Medical office, student housing, and self-storage benefit from above-average tenant demand drivers. The aging population requires more health care services—doctor visits, lab tests, and rehab facilities. The very large generation-Y demographic cohort should continue to support student housing in the near term. And

EXHIBIT 4-4

Prospects for Niche and Multiuse Property Types in 2013

public storage fits into the move-back-into-the-cities trend where people live in less space and need solutions for where to keep possessions they cannot fit into their apartments.

The following is a digest of major trends affecting the major property sectors.

Apartments

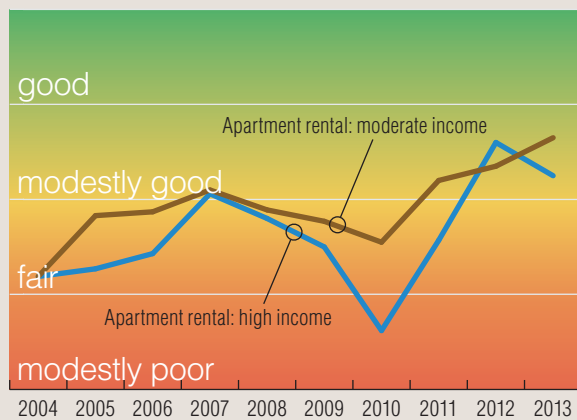
Strengths

The multifamily bandwagon rolls on. “It’s such a good story you have a hard time resisting making investments,” says an interviewee. Positive demographics—the bulge of young adult renters and downsizing baby boomers—supplemented by homeownership displacement from the housing bust create significant demand drivers. Population shifts into infill areas and urbanizing suburbs, especially locations near mass transit stops, favor multifamily, too. More people willingly forsake space and yards for greater convenience and avoiding car dependency. On the

supply side, some fallow development years have further tightened many markets as developers only now begin to catch up. In high-barrier-to-entry places, particularly in metropolitan areas along the coasts, new projects may have trouble keeping up with demand, resulting in mid- to low-single-digit vacancy rates, rent spikes, and “extremely solid” appreciation (exhibit 4-6). So long as these trends continue, over the long term apartments should continue to outperform all other property types on a risk-adjusted basis, with excellent cash flow components. Whereas other sectors must weather impacts from technology buffeting and slackened demand growth, future population increases suggest a vibrant and expanding apartment market.

EXHIBIT 4-5

U.S. Apartment Investment Prospect Trends



Source: *Emerging Trends in Real Estate* surveys.

U.S. High-Income Apartments

2013	Prospects	Rating	Ranking
Investment prospects	6.25	Modestly good	3rd
Development prospects	6.69	Good	1st
Buy 43.8% Hold 35.8% Sell 20.4%			
Expected capitalization rate, December 2013		6.3%	

U.S. Moderate-Income Apartments

2013	Prospects	Rating	Ranking
Investment prospects	6.65	Good	1st
Development prospects	6.47	Modestly good	2nd
Buy 28.1% Hold 33.1% Sell 38.8%			
Expected capitalization rate, December 2013		5.9%	

Source: *Emerging Trends in Real Estate* 2013 survey.

Note: Based on U.S. respondents only.

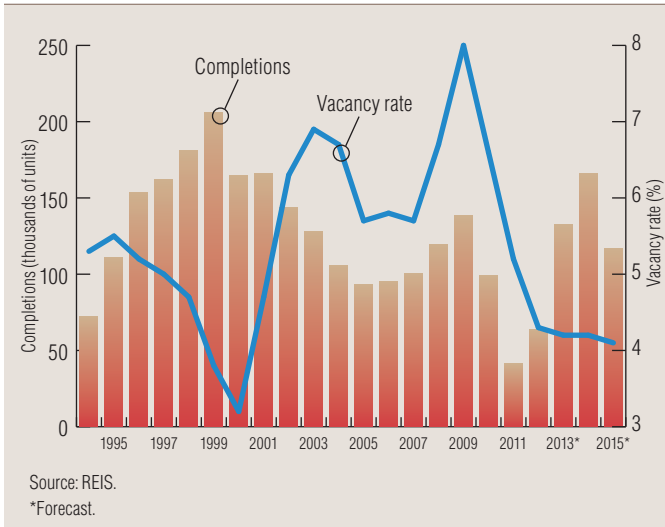
Weaknesses

“Inordinately large” capital flows course into the apartment sector and raise concerns among some investors despite the solid fundamentals. The best deals “have been picked over” and what is left has become just “too pricey.” Some interviewees warn to back off: “Without job creation, this [performance] growth cannot continue.” Some “scary” loan underwriting does not compute: “Exit caps at 4 in ten years when interest rates could be much higher” will require “a good run of value creation.” New projects, meanwhile, could get out of hand in traditional hot-growth, easy-to-build Sunbelt markets, as well as in suburban areas where apartments traditionally tend to underdeliver. Shut out of much activity in the office and retail sectors, developers of all stripes “pile into the sector” as lenders offer construction loans. If the housing market starts to recover and homebuyers gain confidence, apartment demand could slacken; at some point purchasing may begin to look like a better deal than leasing if rents keep increasing. And new investment funds scarf up single-family homes for rental properties, which could compete with multifamily units.

Development

Developers find some solace—“a lot of [apartment] supply is needed to keep up with obsolescence as well as natural growth”—and banks and insurers eagerly boost construction financing volumes. Even with stepped-up activity, interviewees say unit deliveries in 2012—about 200,000—“will come up short” of the roughly 300,000 mark typically needed to maintain equilibrium in markets nationwide. High-barrier-to-entry urban infill markets around 24-hour cities cry out for new projects. Developers who can secure scarce sites and overcome typical entitlement hurdles should score winners, catering to the wave of echo-boomer career builders and their empty-nester parents. Development approaches “hinge on location and quality: at the high end, developers must provide amenities inside and outside” of projects. At the lower end, neighborhoods and convenience count more. For younger, less-affluent rent-

EXHIBIT 4-6

U.S. Multifamily Completions and Vacancy Rates

ers, “developers can meet price points providing less space” as long as the surrounding area offers “a quality experience” defined by shops, restaurants, parks, and, most important, access to workplaces or mass transit to get to work. As light rail and bus rapid transit service is expanded in many markets, construction opportunities will likely present themselves around new

transit stations. The “continuing urbanization” wave underway should give developers at least “a three- to four-year” window in major markets.

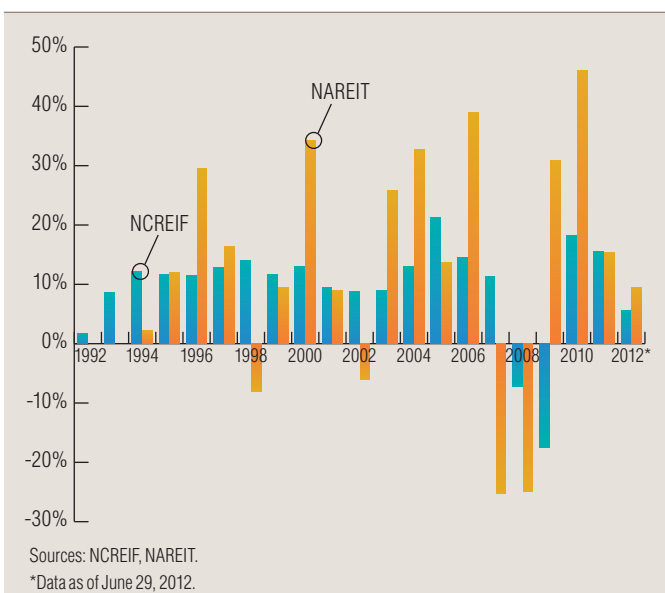
Best Bets

At this point in the cycle, sellers under pressure and some banks shedding assets will settle for the most dependable buyer, not necessarily the biggest offer. “Position yourself” to make deals because many assets are still overleveraged. Focus on apartments “in the big cities with jobs growth.” Even though “a lot of money is headed” into urban infill, “[renter] demand will be there” to support future appreciation. Value-add plays in multifamily can still be attractive. Again, concentrate on buying good assets in good markets, then driving yields by providing modest capital for improvements and hiring a capable property manager to lease up the space into renter demand. Yield chasers should become more selective about development—centering activity on popular urban districts and densifying suburban nodes. Anything transit oriented should hit pay dirt.

Avoid

Back off the sub-6 cap rate deals on existing properties, “where you have much less room for error” should interest rates increase, and steer clear of garden apartments in suburban areas where new development can spring up easily and soften returns on older product. Some of these low-barrier-to-entry places could suffer from oversupply by 2014 or 2015: “Multifamily is almost guaranteed to overdevelop,” according to one interviewee. Particularly watch out in high-foreclosure markets where speculators will turn single-family homes into rentals and compete directly against apartment owners for tenants.

EXHIBIT 4-7

U.S. Apartment Property Total Returns**Outlook**

The “rah-rah” multifamily story seems “a little long in the tooth” and will eventually “lose some steam” as housing rebounds, but expect the run of increasing rents and values to continue in most markets at least through 2013 and probably well into 2014. Cap rates—although not out of range compared with other sectors with higher capital costs and risks—probably have nowhere to go but up, and rent growth should moderate after a boom in infill locations. Car-access suburban markets “will do okay, but underperform.”

Industrial

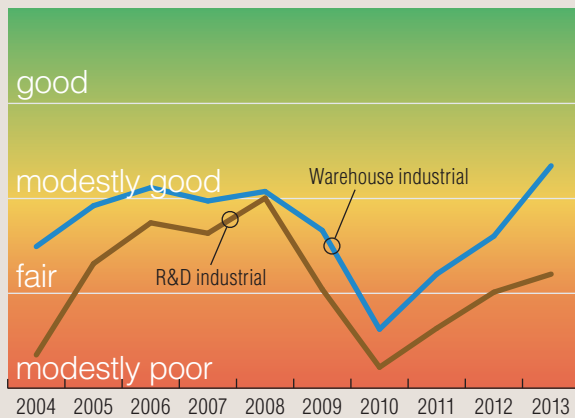
Strengths

The nomenclature has changed from warehouse to distribution and now logistics, but according to one interviewee the industrial supply chain “will always be there since it’s infinitely flexible.” Worries about e-commerce may be overblown: some space turns obsolete faster, but the web retailers still want facilities mostly in the same places “where the bricks-and-mortar guys put [them] near population centers” around the gateways. Recovering at a snail’s pace and “lagging most other sectors,” top industrial markets finally experience good absorption and

moderating vacancies; rents should continue to trend “slightly positive” or better in 2013, especially if global business accelerates. Big blocks of space will be harder to find, leading to new projects. Institutional investors maintain strong interest in major-shipping-hub, big-box space: they like the steady income returns, and long-term holders register solid if unspectacular appreciation. Although they continue to struggle to “scale” portfolios—morsel-sized portions of acquisitions never seem to satisfy capital appetites—at least exit strategies pose no problems to execute. What’s wrong with a classic “get-rich-slowly business”? Not much.

EXHIBIT 4-8

Industrial/Distribution Investment Prospect Trends



Source: *Emerging Trends in Real Estate* surveys.

U.S. Warehouse Industrial

2013	Prospects	Rating	Ranking
Investment prospects	6.34	Modestly good	2nd
Development prospects	5.55	Fair	3rd
Buy 67.9% Hold 23.6% Sell 8.5%			
Expected capitalization rate, December 2013		6.9%	

U.S. R&D Industrial

2013	Prospects	Rating	Ranking
Investment prospects	5.20	Fair	8th
Development prospects	4.32	Modestly poor	8th
Buy 23.1% Hold 45.2% Sell 31.7%			
Expected capitalization rate, December 2013		7.6%	

Source: *Emerging Trends in Real Estate* 2013 survey.

Note: Based on U.S. respondents only.

Weaknesses

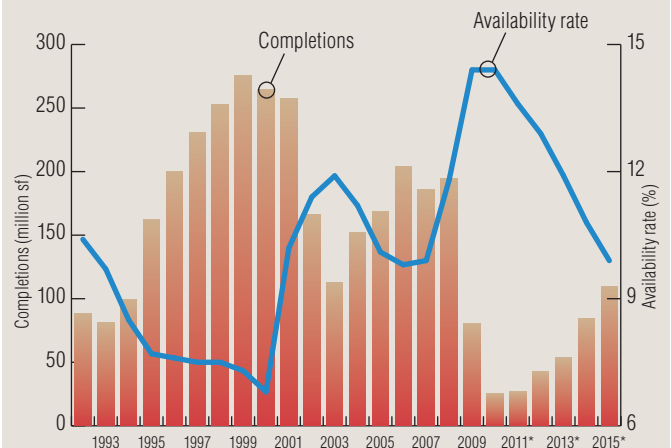
Worldwide economic malaise stunts the rebound at key ports and international airports; some investors “underweight industrial due to reduced exports.” Although “fundamentally not changing the business,” e-commerce slows growth in overall demand for logistics facilities: retailers tend to store less at intermediate points between manufacturers and customers, hurting secondary and tertiary locations. Demand for specialized space tailored to distributor needs forces more old product into obsolescence in key midcountry gateways like Dallas, Chicago, and Atlanta.

Development

Developers latch on to significant demand for build-to-suits from e-commerce companies willing to pay for customized space with elaborate stacking systems to accommodate pick-and-

EXHIBIT 4-9

U.S. Industrial Completions and Availability Rates



Source: CBRE Econometric Advisors.

*Forecasts.

pack operations, increasingly using robots and automated equipment. A far cry from old-fashioned storage facilities, these buildings may require upgraded HVAC and power systems, as well as parking for large numbers of workers. REITs are well positioned to grab this business because they often have better access to capital than the average developer. Otherwise, most U.S. markets cannot sustain much speculative construction—although the pace picks up during 2013.

Best Bets

Owners should hold on to their hub gateway portfolios; these markets will continue to tighten, slowly pushing up rents and returns to healthy levels. Look for opportunities to upgrade and redevelop older product into big-box space in these same “usual suspect” markets. These projects could come on line in time to meet the steadily improving demand, and institutions inevitably will line up to buy them.

Avoid

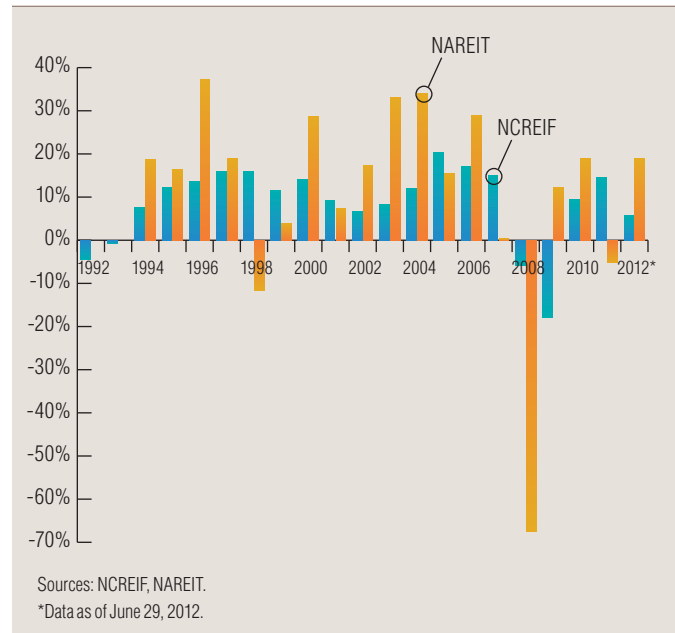
Some smaller markets may retain demand for old-style storage space, serving local trades and merchants, but properties in many secondary and tertiary locations lose out as distributors sidestep them for more direct channels; “Demand won’t come back.” It’s the industrial “equivalent of suburban office parks.”

Outlook

In an ongoing free-for-all, East and Gulf Coast ports will compete against each other for a share of Pacific shipping traffic slated to come through a widened Panama Canal, scheduled to open by year-end 2014. These markets include Houston, New Orleans, Mobile, Miami, Jacksonville, Savannah, Charleston, Norfolk, Baltimore, and New York–New Jersey. The winners will draw enough government funds and private capital to help dredge harbors and build new facilities for offloading containers from massive, deep-hulled post-Panamax ships. Tens of billions of dollars in infrastructure needs extend to expanding freight rail hubs and widening interstate highway connections. Lacking a national infrastructure strategy, the federal government lets states, cities, and regions battle for funding. “The jury is still out, but wild-card factors in decision making could be rail access, local labor costs, taxes, and timing to key inland distribution markets.” Most players avoid “taking any bets.” The victors will either expand or transform into major industrial centers, boosting their economies and providing significant new development and investment opportunities. Stay tuned: it is the biggest contest affecting the future of U.S. industrial markets.

EXHIBIT 4-10

U.S. Industrial Property Total Returns



Research and Development

Relatively buoyant tech enterprises boost prospects for familiar R&D markets in and around brainpower centers like San Francisco–San Jose, Austin, Seattle, Boston, and the North Carolina Research Triangle; major companies expand and startups proliferate. Reversals in stock prices for social-media companies might give some pause, and R&D is notoriously volatile: startups can quickly turn into shutdowns. How many apps do we really need?

Retail

Strengths

The industry sidestepped a full-bore, over-the-cliff “death spiral.” Now, more “optimistic” investors and owners exhale in relief, crediting a significant “limitation on new supply for making the difference.” Upscale retail roars back, especially along downtown streets in 24-hour urban districts and at the leading fortress malls. Affluent Americans continue to shop, and chains gravitate to these most-favored shopping destinations where rents increase and vacancies decline precipitously. Some stressed power centers manage to recoup by filling empty stores with new big-box tenants, and basic bread-and-butter, grocery-anchored retail in established infill markets registers solid income-oriented performance, too. An interviewee said, “The worst is over, and we’re seeing more upside than expected.” The big mall REIT companies “are all doing fine”; they continue to consolidate their positions in the top regional centers, shedding their remaining stinker properties, and hold considerable leasing leverage over retailers who crave premier locations. Chains and specialty retailers, including some offshore brands, “cannot find enough space in the [select] places [New York primarily] where they want to showcase their brands.” Progress on taxing internet sales also offers some promise to dull inexorable e-commerce incursions.

Weaknesses

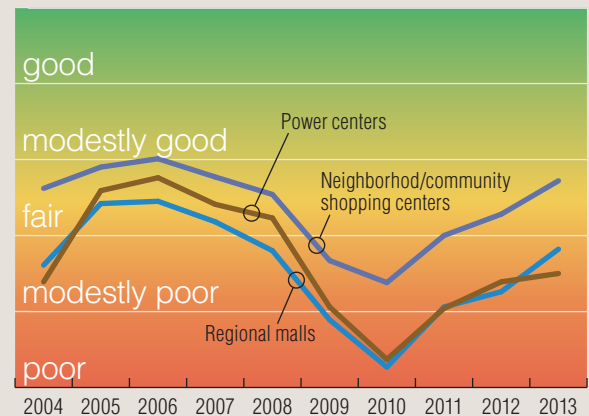
Without a strong economic recovery, evident bifurcation splits the few strong centers from many more vulnerable ones in a “rapidly evolving” and “oversupplied” retail real estate universe. Most interviewees gird for continued industry contraction in the face of competition from web retailers. The 99 percent “have less discretionary money,” controlling consumption appetites, and “the middle market struggles” because many cash-strapped shoppers “go down a notch” in their spending. Operators find a dearth of creditworthy tenants, whether mall anchors, supermarkets, drugstores, local hair salons, or pizza guys. Consolidating major chains increasingly abandon Class B and C regional centers; financially challenged mom-and-pop stores leave half-empty strips along suburban boulevards; and many other “dead dog” commodity properties, suffering from physical deterioration, face repurposing into churches, light manufacturing facilities, or whatever—just not stores. As for e-commerce, web sales nibble away at bricks-and-mortar margins; retailers reduce store square footage and rely more on clicks-and-bricks strategies than bricks alone. In a rapidly evolving marketplace, retail flavors of the day “lose luster” more quickly, consumer preferences become “harder and harder to pin down,” and profit margins become more difficult to maintain.

Development

Forget about suburban development: no new malls or strips required, and lenders restrict access to capital to only their

EXHIBIT 4-11

Retail Investment Prospect Trends



Source: *Emerging Trends in Real Estate* surveys.

U.S. Neighborhood/Community Centers

2013	Prospects	Rating	Ranking
Investment prospects	5.72	Modestly good	7th
Development prospects	4.39	Modestly poor	7th
Buy 52.7%		Hold 28.0%	Sell 19.3%
Expected capitalization rate, December 2013		7.1%	

U.S. Power Centers

2013	Prospects	Rating	Ranking
Investment prospects	4.50	Fair	11th
Development prospects	3.11	Poor	9th
Buy 11.9%	Hold 38.5%	Sell 49.7%	
Expected capitalization rate, December 2013		7.6%	

U.S. Regional Malls

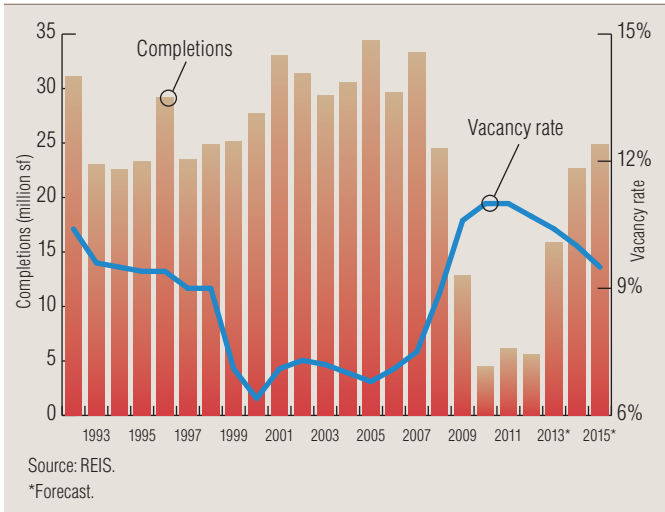
2013	Prospects	Rating	Ranking
Investment prospects	4.82	Fair	9th
Development prospects	2.76	Poor	11th
Buy 16.0%	Hold 54.9%	Sell 29.2%	
Expected capitalization rate, December 2013		6.5%	

Source: *Emerging Trends in Real Estate* 2013 survey.

Note: Based on U.S. respondents only.

highest-credit clients—advantage the REITs once again. But retail real estate could use a heavy dose of redevelopment, particularly older (30 years plus) fortress malls, which need reconfiguring to handle retailers’ morphing in-store/online marketing schemes—smaller stores, more showroom and promotion space, and less storage. Some new, nontraditional

EXHIBIT 4-12

U.S. Retail Completions and Vacancy Rates

tenants will lease display space for promotions in higher-traffic locations and orient shoppers to make purchases or contacts directly off their mobile devices as they pass by. Restaurants, movie theaters, and entertainment features will become more important enticements to the mall mix as landlords “figure out how best to compete against online selling.” Big-box formats continue to wrestle with how to shrink into urban streetscapes to capture business from move-back-in trends, and multifamily developers similarly accommodate necessity retail components—supermarkets, drugstores, and cleaners—into their infill projects. “Urban retail development has major potential.”

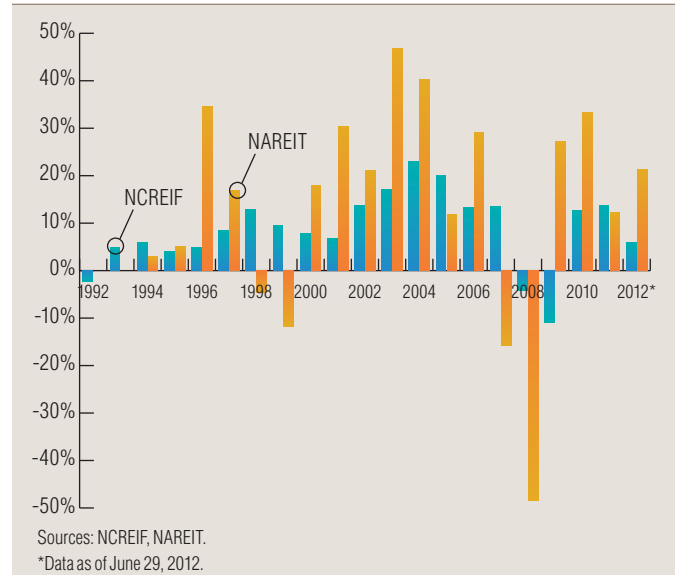
Best Bets

Investments in mall REITs, which monopolize ownership of Class A/A+—quality malls, may be the only way to get a piece of these top centers. These publicly traded operators would be crazy to dispose of any of their fortress centers, given firmly established locations in the most advantageous retailing hubs and “huge sales” volumes. Outlet mall companies also turn “very hot.” Economizing shoppers can buy specialty brands at half price and “get a better bang for their buck.” Flagging Class B and C regional malls feel the heat as outlets make incursions into their home turf, expanding from locations near tourist resort destinations closer to suburban backyards. The warehouse clubs also draw crowds looking for bargains. Neighborhood centers in good residential neighborhoods with barriers to entry will do well as long as they are anchored by a dominant supermarket chain.

Avoid

Questionable retail properties litter the suburban scene from coast to coast. Many need bulldozing and transforming into

EXHIBIT 4-13

U.S. Retail Property Total Returns

alternative uses, including parks and light-rail stations or possibly warehouse space to support e-commerce. Power centers look more like “a crapshoot,” considering how much big-box commodity merchandize ultimately could be bought online. Watch out for neighborhood centers exposed to Whole Foods/Trader Joe’s or Walmart/SuperTarget forays. According to an interviewee, “Between high-end specialty food stores and discount superchains, the typical grocery anchored strip is at significant risk. If you lose the grocery anchor, you’re sunk.”

Outlook

Retail real estate appears positioned to endure a very long, slow, but dramatic transformation in how and where people shop. Online approaches turn retailing into an “omnichannel” business: the winners will embrace technology and integrate it into bricks-and-mortar platforms, realizing that e-commerce/in-store combinations beat stand-alone formats. “If you can touch it in the store, you’ll buy more of it online.” Mall shoppers manned with apps will know what’s on sale, get coupons for discounts, and find out about new products—potentially driving more business. Landlords and tenants need to adjust how space is priced as marketing and promotion become more important to retailers than just direct in-mall sales. The big-box stores all look at how to downsize, too; they may move from power centers into smaller fortress mall configurations or inner-city formats. Prime neighborhood retail survives: necessity shopping endures for groceries and pharmacy items, but just about everywhere in America could use less store space per capita.

Office

Strengths

Lagging behind other commercial property sectors, office finally benefits from a severe, necessary, and now extended construction slowdown. Absorption increases and rents tick up in the stronger 24-hour downtowns and other markets harboring expanding high-tech and energy businesses. Investors must focus more than ever on location. “That means urban, dense, vibrant places,” preferably with diversity provided by universities and medical centers. Buildings win if they can offer tenants flexibility allowing cost-effective layout changes to accommodate open-space plans and wi-fi technologies. Green buildings with high ratings under the Leadership in Energy and Environmental Design (LEED) program and energy-efficient systems leapfrog

the competition: tenants calculate operating savings and find they can attract young talent who favor “cool space” and nods by their employers to environmental correctness.

Weaknesses

“Secular headwinds” buffet office markets. Tenants continue to downsize space-per-capita requirements, and technology enables more people to work away from the office or spend less time there. “Vacancy rates are too high nationally—low double digits for downtown and midteens for suburban office” (exhibit 4-16) as tenant credit quality has turned “much more suspect.” Many new high-flying companies “can be here today, gone tomorrow.” Landlords “must be careful even with law firms” (whose billable hours are down from what they used to be), while other blue-chip tenants cannot be counted on to expand their space requirements; financial companies and accountants continue to offshore and outsource. “Value-conscious” businesses “want hyper-efficiencies, looking to take 80 percent of the space they used to lease and stuffing more people in.” They “seek density and less cost per employee,” making it extremely difficult to achieve “pricing power even in the best markets.” Investors increasingly worry about “how much rental growth you can expect to offset higher cap rates down the road.” Office problems increase CMBS delinquencies as leases written at market peaks in 2006 and 2007 burn off at lower rental rates and often for less space, if tenants renew at all. Some landlords should be “scared to death” about any pending rollovers in their tenant base.

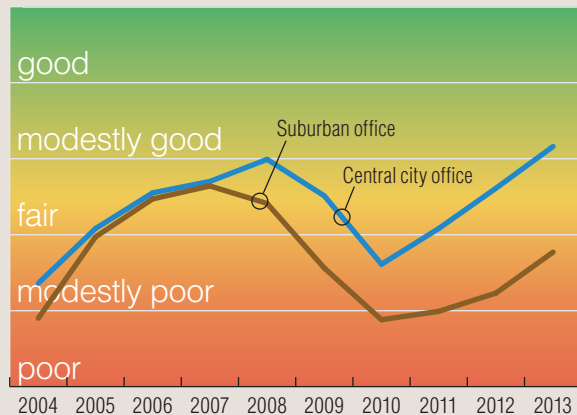
Development

Contraction in space use and chronically high vacancies will continue to mothball most projects in many markets. In tighter 24-hour cities, new green developments, featuring layout efficiencies and “healthy” interiors, can charge premiums in siphoning big space users away from existing buildings. “At a macro level, office vacancies won’t get much better, but this new product will sell.” In fact, any new office building will be “some version of green,” and these projects will render “hard-to-retrofit” brown buildings, including some ten- and 20-year-old vintage towers, “increasingly obsolete.” Prospective tenants now “check the boxes” for lower energy bills, better windows for more natural light, cleaner/fresher air, raised floors for under-floor wiring and HVAC systems, as well as high-tech conference centers. “It’s like a fancy, new car: everybody wants to be in a LEED building.”

Where possible, re-adapting space “will become a common undertaking” as owners try to install new energy-efficient systems and create more open spaces. They need to appeal to tenant mind-sets, which “rationalize” the notion of “increasing worker productivity and wellness while reducing square footage per employee.” Some big corporations—typically e-commerce firms and manufacturers—“sit on lots of money” and may be willing to entertain build-to-suits.

EXHIBIT 4-14

Office Investment Prospect Trends



Source: *Emerging Trends in Real Estate* surveys.

U.S. Central City Office

2013	Prospects	Rating	Ranking
Investment prospects	6.16	Modestly good	4th
Development prospects	4.53	Fair	6th
Buy 47.4%		Hold 35.1%	Sell 17.5%
Expected capitalization rate, December 2013		6.2%	

U.S. Suburban Office

2013	Prospects	Rating	Ranking
Investment prospects	4.77	Fair	10th
Development prospects	2.82	Poor	10th
Buy 25.1%		Hold 45.5%	Sell 29.4%
Expected capitalization rate, December 2013		7.9%	

Source: *Emerging Trends in Real Estate* 2013 survey.

Note: Based on U.S. respondents only.

EXHIBIT 4-15

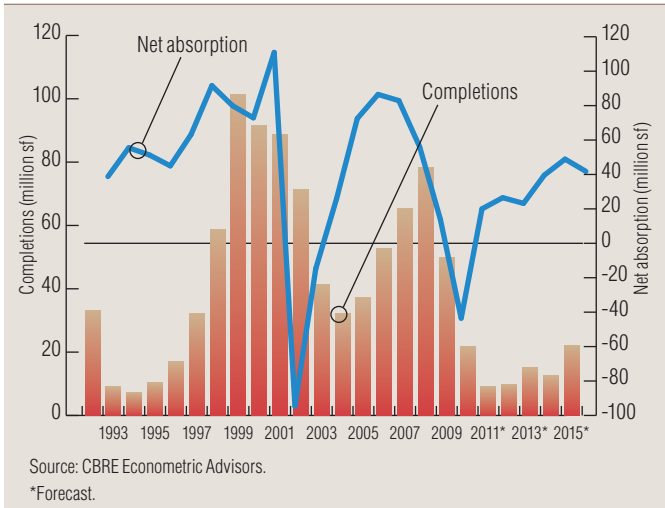
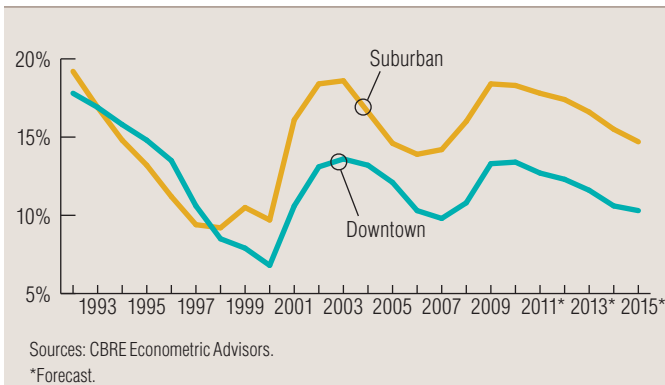
U.S. Office New Supply and Net Absorption

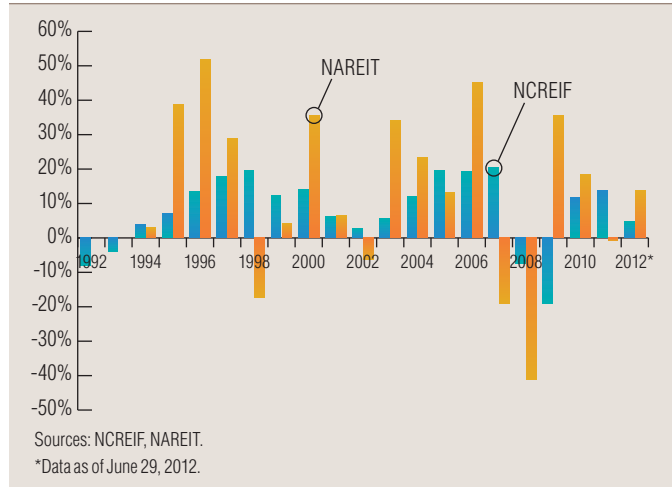
EXHIBIT 4-16

U.S. Office Vacancy Rates**Best Bets**

Focus on well-leased buildings in top markets and protect against functional obsolescence. Favor LEED buildings or buildings that can be economically adapted to meet LEED standards. Tune in to work attributes favored by younger hires, who place emphasis on connectivity and social interaction over privacy and their own space. Also, pay more attention to the neighborhoods where the gen-Y crowd wants to live and work; “Their influence cannot be underestimated.” A minority view suggests that once unemployment drops, “all the old-style, high-finish amenities will make a comeback.” “It’s an employer’s market right now, so workers will put up with less space as long as they get a paycheck.” But don’t bet on it.

Although a niche sector, medical office space presents compelling investment opportunities as the nation’s health

EXHIBIT 4-17

U.S. Office Property Total Returns

care industry balloons to take care of graying baby boomers. Undersized properties may “make it hard to put money out,” but the demand from doctors, clinics, labs, and rehab providers is “crazy to ignore.” Landlords should not have problems leasing space anywhere near hospital centers and medical complexes.

Avoid

“Severely handicapped” suburban office space remains “a trap.” Generation Y resists working in isolated office-park campuses, which require a car for the commute. Models for repurposing outmoded suburban retail space may offer ideas on “what to do about some of this old crappy [office] space.” Resist buying cheap Class C or off-location buildings with the idea of riding back an eventual market rebound. Investors underestimate the capital expenditure requirements for maintaining these buildings, and long-term leasing and value trends point to subpar results. Rents have flat-lined or worse in many suburban districts for decades.

Outlook

Aside from modestly bullish forecasts for gateway trophies and the few new green projects in these same markets, the office sector promises a tough road for investors, given decreased demand, dictated and enabled by morphing work styles and technology. The office as work center has become less essential as more bosses choose to let more of their workers spend more of their time operating from elsewhere. These approaches not only register bottom-line savings, but also can encourage greater productivity. Multinational companies can be expected to continue shifting work to lower-cost overseas markets, moderating expansion appetites in the United States. And most obvious, today’s office users require less space than in the past to get the same amount of work done: businesses now operate with fewer administrative personnel and need less storage. It’s a new age.

Hotels

Strengths

The hospitality sector—especially in major markets (“New York pulls up everything”)—performs “quite well.” Helped by “little new development,” investors and operators realize “solid growth” in occupancies, with rates tracking right behind, and remain “cautiously optimistic” as long as the economy holds together. “More people stay in hotels than ever before” and “the frenzy of cutting [staffing] and lopping off expenses has ended.” The upscale and luxury categories revive in style: wealthy travelers and business elites book cushy resorts and prime business center suites as

operators hope guests do not notice reduced manpower levels and the absence of certain “runaway-cost” service amenities. Bulk-buying corporate customers accept year-over-year increases in negotiated rates, and “modestly” loosen purse strings on food and beverage–related events. Full-service hotels have pared expenses by eliminating multiple restaurants, and “menu engineering” brings back more profitable margins.

Weaknesses

Operators put a brave face on “revolutionary changes” wrought by web-based pricing transparency and internet reservation sites. Value-conscious customers can surf the web for the best prices and secure favorable deals, hamstringing the ability to advance rates. In a battle fought on websites and through social media, the big chains try to gain an edge through rewards programs and have an advantage over weaker flags or independents using less-sophisticated systems and technologies. Price shopping “forces hourly revenue management like the airlines” with “inventories controlled like bond traders.” Hotel chains have all migrated to off-property, centralized sales and marketing functions. “It’s now a science, not an art.” While the meeting business has recovered “after taking the pipe [during the recession], it’s not where it was.” The total size of group catering per head stays down and events remain “less elaborate.”

Development

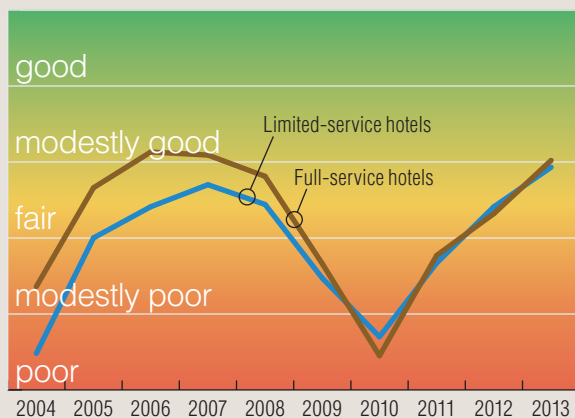
Given plenty of troubled legacy loans in portfolios and multiple cycles of burned development transactions, lenders show no inclination to bankroll hotel projects, except extremely select deals in prime global gateways. “The universe of locations strong enough for new development will remain extremely limited”—“New York, Miami, D.C., Boston, L.A., San Francisco, and maybe energy markets.” After five years of bankruptcies, cost cutting, and holding on, many properties require overhauls. The industry will need to concentrate on upgrades and renovations rather than ground-up construction.

Best Bets

Investors need to “change their metrics” and realize that few bargains exist; yields and margins will no longer satisfy “opportunistic” expectations. Opportunity players try to ferret out “really attractively priced,” “broken deals” that need a “white knight” and “a new flag”—“maybe a resort in Florida or Arizona.” Special servicers hold “lots of product” in need of renovation from deferred maintenance; at some point they will try to clear these properties from their books. Buyers will need to be selective, especially in secondary and tertiary markets where revenue per available room (RevPAR) growth lags. Clean and comfortable, low-frills suites with oatmeal and scrambled eggs or muffins included in a complimentary breakfast draw

EXHIBIT 4-18

Hotel Investment Prospect Trends



Source: *Emerging Trends in Real Estate* surveys.

U.S. Hotels: Limited Service

2013	Prospects	Rating	Ranking
Investment prospects	5.93	Modestly good	6th
Development prospects	5.10	Fair	4th
Buy 45.9% Hold 31.2% Sell 23.0%			
Expected capitalization rate, December 2013		8.2%	

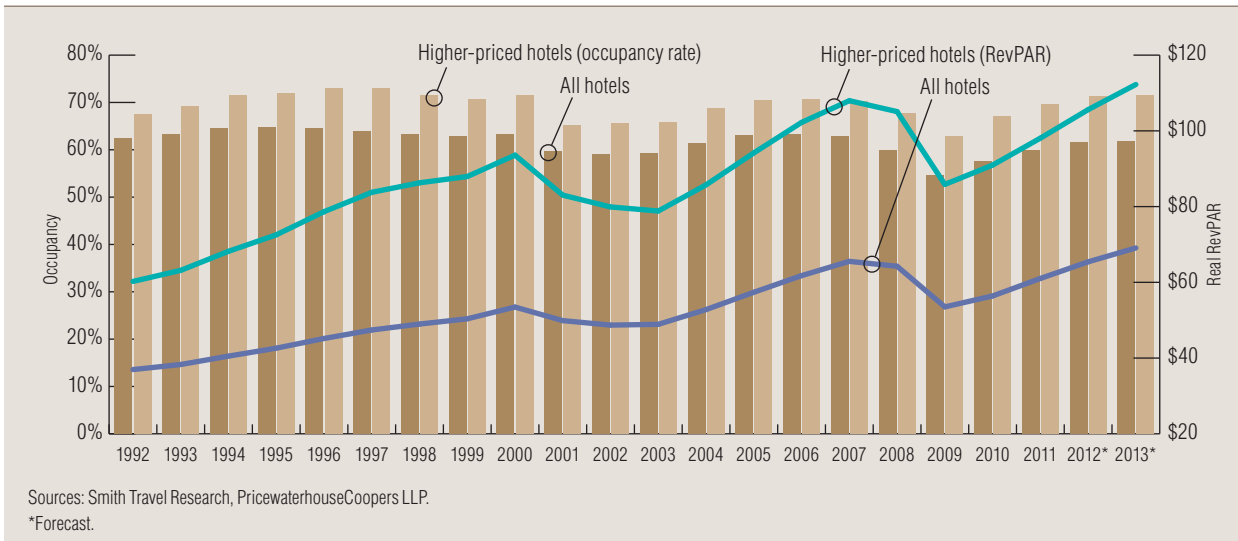
U.S. Hotels: Full Service

2013	Prospects	Rating	Ranking
Investment prospects	6.02	Modestly good	5th
Development prospects	4.64	Fair	5th
Buy 30.7% Hold 45.2% Sell 24.2%			
Expected capitalization rate, December 2013		7.4%	

Source: *Emerging Trends in Real Estate* 2013 survey.

Note: Based on U.S. respondents only.

EXHIBIT 4-19

U.S. Hotel Occupancy Rates and RevPar

budget-conscious business travelers in droves to limited-service hotel formats like Hilton Garden Inn, Courtyard by Marriott, and Residence Inns. Less dependent on group and catering/restaurant business, these hotels avoid costly overheads, including large food and beverage staffs. For “uncertain times, it’s the surest bet,” and despite decent cash flows, “a lot of [local] owners won’t be able to refinance maturing loans,” paving the way for attractive recapitalization plays at lower cost bases.

Avoid

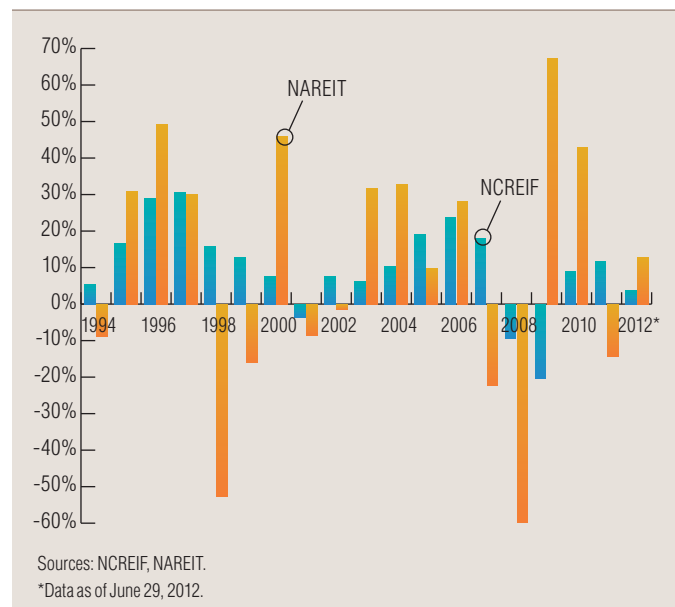
Travel increasingly concentrates in the top 25 or so population and business centers. Hotels a step or two removed from primary transportation hubs register weaker outlooks and will have trouble sustaining strong revenue gains. Although investors may find some reasonable deals, they should be extremely selective.

Outlook

Quietly hotels edge back into favor “and can’t be ignored. They’ve been in rocket mode.” Expect profit growth to flatten in the healthy mid- to high single digits as long as development remains sedated. Winners will find ways to burnish their brands and fend off online travel agencies, which effectively commoditize pricing among the leading flags. So far the typical hotel boom-after-bust cycle in transaction pricing has been short-circuited by slow-to-foreclose lenders, tepid debt availability, and a wide gap in bid/ask spreads. Transaction volume should gain momentum finally as buyers capitulate in the face of strong revenue growth and lenders dispose of more foreclosed assets. The industry keeps its fingers crossed that momentum can be sustained: any economic

reversals would strike operating margins quickly. The major hotel companies view the United States as a mature market with relatively few expansion opportunities outside the familiar global gateways. Their attention has shifted to overseas markets—especially Asia, India, and Latin America—where more attractive development prospects beckon.

EXHIBIT 4-20

U.S. Hotel/Lodging Property Total Returns

Housing

Strengths

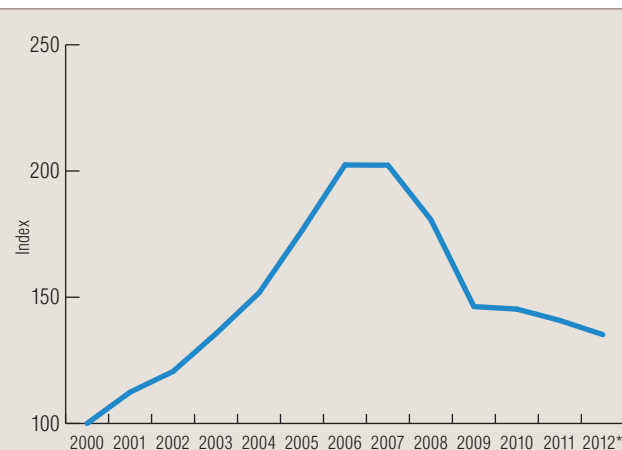
Down for so long in an excruciating bump-along-the-bottom trough, housing finally advances and markets gain some real traction, although struggling along the way. In a classic buyers' market, institutional managers and savvy high-net-worth investors take the plunge with conviction. They opportunistically try a "pioneering" gambit, raising hundreds of millions of dollars in capital for funds to vacuum up single-family product at depressed prices, rent it for income, and eventually sell in any full-bore recovery. Smaller players have already put together localized ventures, and prices should firm up further in markets that are drawing attention. Some prime neighborhoods in affluent enclaves escaped much damage and register modest gains, while "accelerating prices" for condominiums in "better" markets like south Florida could be "a leading indicator for recovery." Skyrocketing apartment rents in certain infill and gateway markets also provide incentives to buy. Banks finally allow more short sales and convert delinquent owners into renters, helping dent the inventory of problem loans, which weighs down many commodity markets.

Weaknesses

Even with relatively low mortgage rates, home sales have languished and the homeownership rate has dropped to 50-year lows, revealing lack of pent-up demand and the depths of many Americans' shaky personal finances in a problematic jobs market; they simply cannot afford to own homes. Others just do not want to venture the risk or deal with homeownership headaches,

EXHIBIT 4-21

The S&P/Case-Shiller Home Price 20-City Composite Index

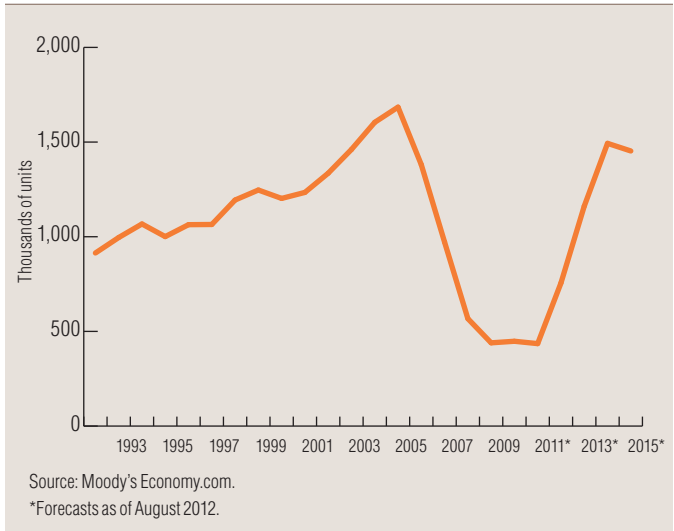


Source: Standard & Poor's.

*As of June 29, 2012.

EXHIBIT 4-22

U.S. Single-Family Building Permits



Source: Moody's Economy.com.

*Forecasts as of August 2012.

amply documented in reams of housing-bust publicity. Rational credit standards, which require reasonable downpayments and good borrowing histories, shut out some potential buyers who would have had no trouble scoring a mortgage in the precrash lending environment. More than 10 million homeowners, meanwhile, remain underwater on mortgages worth more than actual house values. Any distressed selling will continue to dampen prices—and what happens if interest rates increase?

Development

New construction levels have never been lower in 50 years, and if the market has any chance to recover more quickly, homebuilders and lenders would be wise to show continued discipline. Expected population gains will eventually lift demand and push housing starts, and builders should find some opportunities in markets with better employment growth. They retreat from traditional greenfield subdivisions at the suburban fringe and seek more infill opportunities. Instead of building cavernous McMansions, they downsize models, consider more energy-efficient designs, and look to accommodate extended families in units comfortable for grandparents running out of retirement savings and adult gen-Y children unable to cut financial ties.

Best Bets

For anyone who wants to own and has the means, now is a good time to buy and lock in low long-term financing. Prices should continue to edge up, and mortgage rates are not expected to get better absent an economic reversal. Speculators, including the new housing fund ventures, should

concentrate on securing low acquisition prices on rentable properties, which can deliver steady cash flows. “Expensive housing markets won’t work. Rents do not support the purchase prices,” and anyone expecting to score rapid value gains likely will be disappointed. Fund investors need assurance that their advisers/general partners have the organizational infrastructure to manage and lease scores of disparate houses in different places and deal with the inevitable myriad renter-related issues, from leaks and broken appliances to household damage and security deposits. “There’s no playbook”; scaling up these funds may be “a challenge” and “could be a crapshoot.” Local investors, focused on a manageable number of properties in familiar districts and neighborhoods, may be better positioned to deliver on performance objectives. Buying land cheap, getting entitlements to add value, and holding until markets strengthen still makes sense, too.

Avoid

Watch out for older commodity suburbs in decline. For any location, a substandard school district and a falling tax base could signal an unfortunate downward home price spiral. Weekend, summer, and resort homes still can compute for folks with significant disposable incomes, but “do they make economic sense” for most potential buyers? “You’re so much better off renting for three weeks” or vacationing at places where you have never been before and escaping the ownership hassles.

Outlook

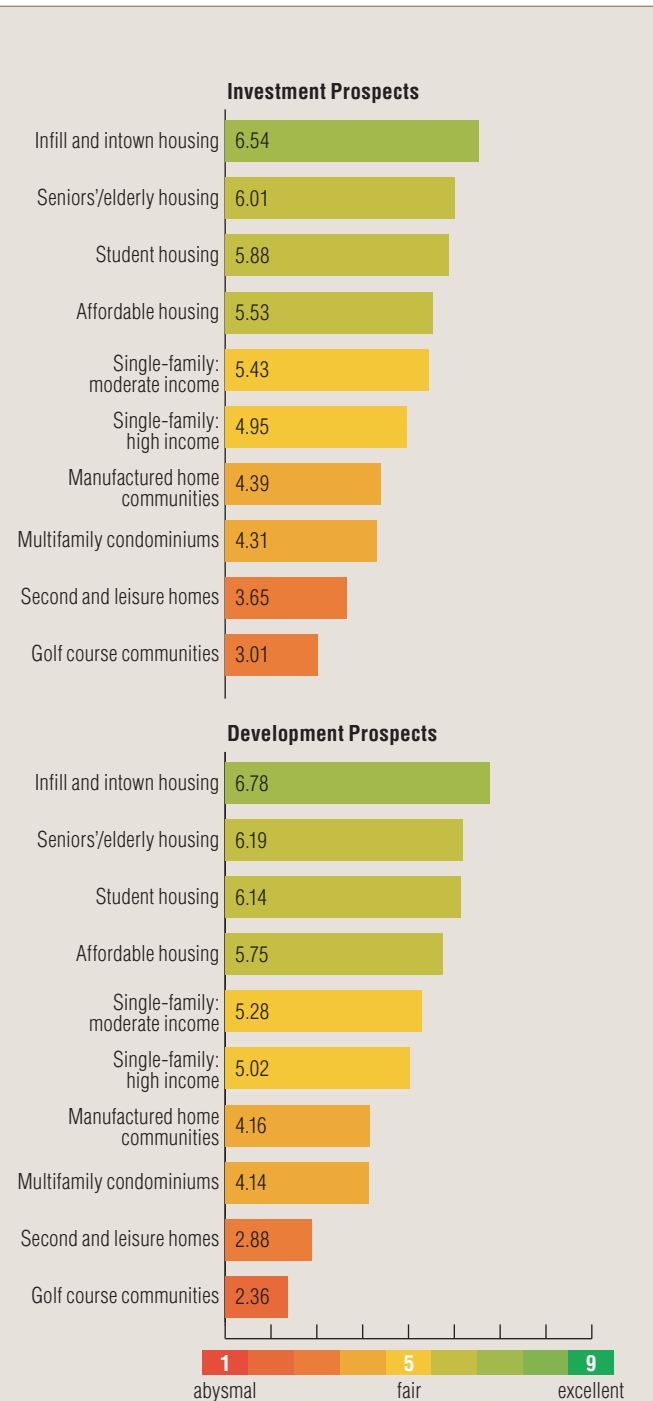
Housing will remain troubled until unemployment rates fall, worker earnings power recovers, the market clears its foreclosed/defaulted properties, and banks loosen up credit standards just a bit. No one holds his or her breath, but a recovery finally appears underway in fits and starts. In 2013, more buyers should gain confidence about acquisitions, and high rental rates in some markets should encourage more house hunting. The nascent upswing remains extremely susceptible to any economic reversals or interest rate hikes. Given housing’s significance to the overall economy, the country will be back on track when homebuilders can get back in gear. But what comes first?

Niche Housing Sectors

Seniors’ housing. The sheer number of Americans aging into retirement promises steady demand for seniors’ housing over the next decade. At the same time, smart players realize the market dynamics may be changing because fewer seniors will have the savings or pensions they might have expected only a few years ago. Stock market reversals, companies abrogating retirement plans, and losses in home values all conspire to put

EXHIBIT 4-33 (4-23)

Prospects for Residential Property Types in 2013



Source: *Emerging Trends in Real Estate 2013* survey.

Note: Based on U.S. respondents only.

many seniors in dicey financial straits. Developers start to orient projects toward a “private-pay population” with “less income in the midst of a weak economy.” Some “disappointed” investors expect “slow growth for years, with little opportunity to raise rents.” They also worry about “political uncertainty over health care, moves to cut health care costs, and the changing insurance environment.” At the same time, the desire for generational separation is upended by harsh economic realities: more grandparents may be forced to move in with their children and scrap plans to live independently either in seniors’ housing projects or their own homes.

Mobile home parks. The same demographics and income issues work in favor of mobile home park owners, who can sit on land and earn solid income until development opportunities resurface. In these constrained times, trailer living fits the lifestyle budgets of more people, old and young.

Student housing. The sector remains compelling, given the sheer demographic numbers of college-age young people.



Emerging Trends in Canada

“We’re not a bad place to be.”

In a world struggling with managing unprecedented debt levels and economic upheaval, Canada enjoys “boring” stability, its real estate markets following along in a seeming state of near-perpetual equilibrium, at least compared with other volatile regions, including most obviously the United States. As uncertainty continues around the globe, “Canada sits in a sweet spot of low interest rates with [the benefit of] a natural resource/commodity-based economy.” “People live under the assumption that we have a profound safety net which provides confidence that things won’t go upside down.” From Vancouver’s Pacific gateway and Alberta’s oil sands in the west to Toronto’s global financial center and Halifax’s shipbuilding in the east, Canada is well positioned to sustain its economic consistency. The rest of the world has taken notice. U.S. retailers are expanding into the dependable Canadian market, immigration waves stoke growth in housing and condominium sales,

and foreign investors try to gain footholds (most unsuccessfully) in property sectors against difficult odds: Canadians tend to buy and hold long term.

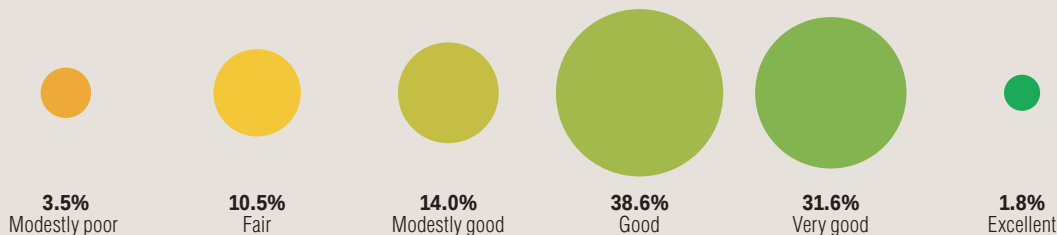
But “cautiously exuberant” Canadians also struggle against complacency and must remain focused on the reality of how the world’s tenth-largest economy can be dragged down by everyone else. “We cannot continue to outperform economies awash in debt. The huge deficit of our largest trading partner, the U.S., will restrain growth; energy markets and the resource sector [will] slow down.” In other words, Canada “cannot assume we’re immune” from the “gray cloud” hovering over the world’s major markets.

For 2013, a balanced outlook is expected. “Compared to everyone else, we will do very well, but growth trends will be pretty mediocre.” In fact, “mediocre” should be viewed as “the new ‘good,’” as real estate players “need to scale back expectations.” Canada has entered “a post-adrenaline phase after only

EXHIBIT 5-1

Firm Profitability Forecast

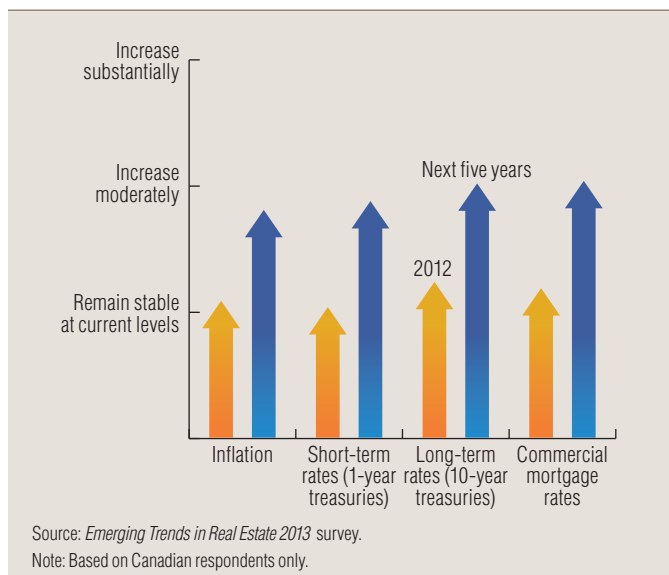
Prospects for profitability in 2013 by percentage of respondents



Source: *Emerging Trends in Real Estate 2013* survey.

Note: Based on Canadian respondents only.

EXHIBIT 5-2

Inflation and Interest Rate Changes

a mild recession,” the economy bounced back quickly, helped by looser-than-normal monetary policy and sales of natural resources. “Our base is pretty solid, but we’re no longer on fire.”

Interviewees point to some of the concerns threatening the Canadian economy in 2013. “Commodities can get beaten up, especially the natural gas sector.” Household debt has increased to near-record levels, and home valuations are level or have declined in some places. It is nowhere near a U.S.-style melt-down, but “higher interest rates could create problems.” The housing slowdown affects the construction industry and retailers; fervent consumer buying quiets down from recent peaks. The government also “winds down” stimulus and tries to make fiscally responsible cuts. “Growth will depend on the private sector” alone. As a result, the unemployment rate hovers north of 7 percent and wage growth has been “limited”—better than most global competitors, but not indicative of a vibrant jobs forecast. Call the economy and job growth “slow and steady.” There is an apparent disconnect in job opportunities and employee resources, as increasingly new jobs are concentrating in the commodity-rich west while the largest population centers are east, mostly in Ontario and Quebec. The nation’s continuing immigration surge shifts gradually toward Alberta and Saskatchewan, heading to where the jobs are, and will continue to spur local real estate markets in coming years—not just in Calgary and Edmonton, but also around Saskatoon and Winnipeg.

All in all, “we expect nothing spectacular, but if the world turns around, we are in an excellent position”—and not a bad position under any circumstances.

Top Trends for 2013

Equilibrium Maintenance. Year in year out, vacancy rates help tell the commercial real estate story in Canada. They average in the mid-single digits across virtually all property types, keeping most markets in a healthy, near steady state, which gives landlords the opportunity to push rents and enjoy measured, ongoing appreciation. A small group of institutional investors dominates office markets in the largest cities and owns the best retail properties, enjoying solid income returns from their holdings. Like their U.S. neighbors, asset-rich Canadian public pension funds wrestle in a low-interest-rate environment with how to meet a widening gap in funding their long-term liabilities as more beneficiaries retire. On a risk-adjusted-return basis, they see real estate and infrastructure investments as a solution for finding stability and low volatility with significantly better yields than fixed income. But exercising significant discipline, they also “resist firing up the domestic development cycle” in an attempt to boost performance and understand that any overbuilding would only undermine values on their existing portfolios. Everyone seems to benefit from the resulting relative balance in supply and demand: “They all want to see 2 to 3 percent rental growth and wait for increased demand for space to build before they fund development, resulting in pressure on rental rates.” Although investors and developers may miss out on some opportunities, they avoid painful busts: the country’s commercial mortgage defaults remain minimal, and markets have avoided a U.S.-style collapse. All signs point to more of the same in 2013, with the Canadian market expected to continue to linger in this comfortable zone.

Interest Rate Benefits. As long as interest rates hold near rock-bottom lows, commercial real estate will continue to prosper: “It’s the attractive” alternative. “If I put dollars in the bank, I’ll get next to nothing, and bonds, not much more, so I’ll load up on real estate and get a 7 to 8 percent return in markets that are generally not oversupplied,” notes one interviewee. Not surprisingly, REIT stocks benefit from the same thinking: their dividends lure a strong following of both retail and institutional investors, and refinancing at low rates should help their profit margins. Interviewees expect rates to increase only marginally, heavily influenced by U.S. and European central bankers who engage in further monetary intervention to help their ailing economies, which need to produce more jobs.

Uncomfortable Household Debt. On the flip side, cheap money has had its negative impacts, relaxing the average Canadian’s usually well-served, conservative fiscal tendencies. Suddenly, “everyone is up to their eyeballs in debt; when interest rates went to zero, they loaded up [on credit] and fueled homebuying with inexpensive mortgages.” Homeownership

approaches a possible saturation point near 70 percent and prices in some markets began declining in 2012 as federal regulators applied the brakes and imposed stricter lender guidelines, such as limiting amortizations to 25 years, resulting in increased monthly mortgage payments. Both house hunters and condo speculators have backed off buying sprees, and discretionary sellers decide to pull back.

Interviewees say a minor correction could be healthy for markets and appear confident that anything approaching U.S. heartache will be avoided. They point to significant differences in the two countries' mortgage markets: Canadian banks have always required downpayments; never engaged in "NINJA" (no income, no job, and no assets) lending practices, let alone offered subprime rate financing; and hold mortgages on balance sheets. Therefore, the ingredients for a subprime-driven mortgage-backed securities environment never developed. Strict underwriting weeds out most compromised borrowers, and buyers take out insurance against defaults. Although new supply has not outstripped demand trends, thanks to immigration flows, all signs suggest the condo market needs a further cool-down, especially for luxury units. In the meantime, low interest rates should help recent borrowers make payments and "hold on," even though values could edge down further.

Urbanization Continues Apace. Canadians gravitate to the "urbanization model. It's everywhere," extending beyond central business districts to reach interconnecting urban nodes in once-suburban expanses not only around Toronto, Vancouver, Calgary, and Montreal, but also "reaching every part of the country," including the smaller cities. "People make

a choice of where they want to live, and the shift has been quite profound." They increasingly choose in-town living and high-rise apartments or townhouses over suburban subdivision, house-and-yard lifestyles. The trend is "generational," "cultural," and "not just economical." Cities are more convenient and concentrate 24-hour amenities for business, recreation, and entertainment. Aging baby boomers get tired of shoveling snow and navigating roads during harsh winters, gen-Yers are attracted to better job opportunities and a glamorous city life,

EXHIBIT 5-4

Change in Availability of Capital in 2013

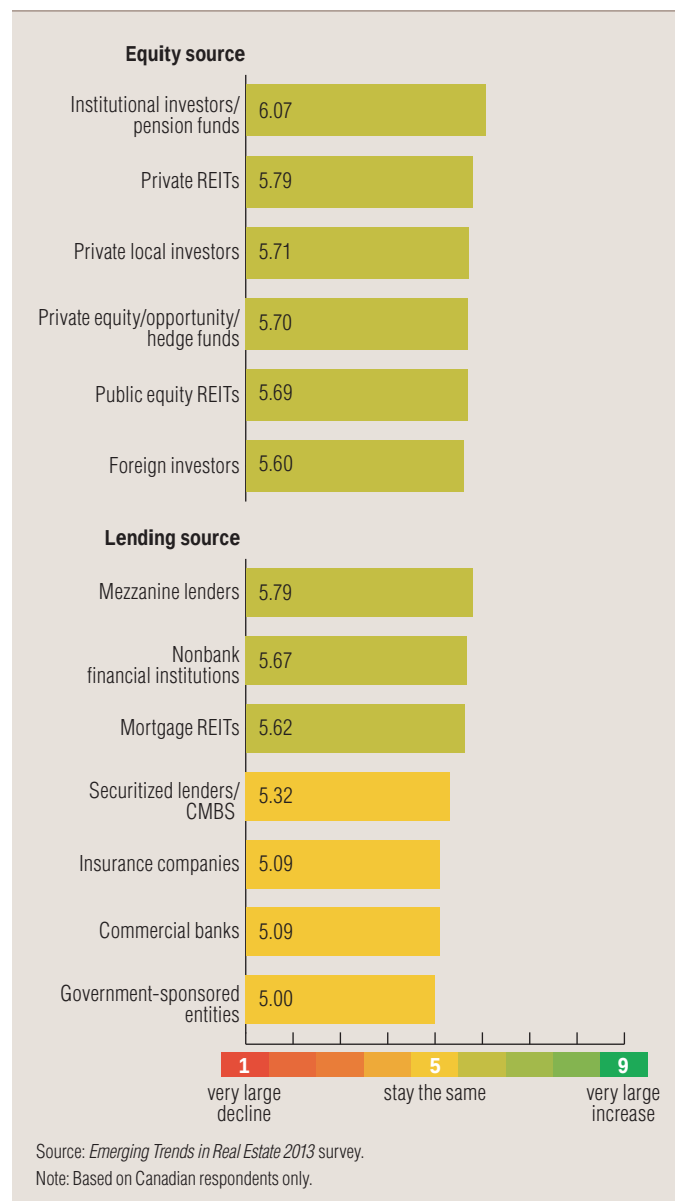
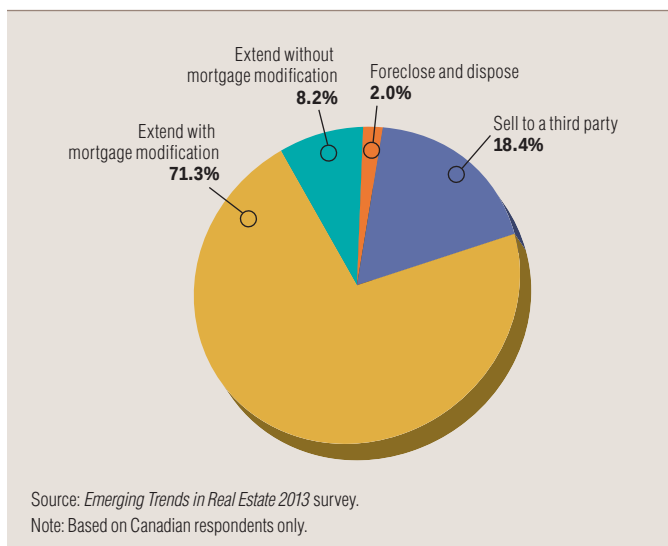


EXHIBIT 5-3

Maturing Loans: Preferred Strategy for Lenders



and everyone wants to limit time lost in increasing suburban congestion. Retailers “start to support” the high-rise residential boom, working with developers and planners to integrate streetscape shopping into new condominium projects.

Land values for “scarce” infill sites continue to increase after having skyrocketed, as local governments encourage densification and developers look to maximize returns by building as high as zoning allows. Any location near mass transit stations significantly increases in value, and developers and the business community call for increased light rail and subway funding to expand or build systems and support densification. They worry that most municipalities lack the resources to finance infrastructure projects adequately and need support from the federal government, which shies away from major outlays. Existing infrastructure, meanwhile, nears the end of life cycles, requiring expensive upgrades or replacements. As a result, concerns grow about how urbanizing nodes will connect to cores and each other. Dense development patterns require mass transit to reduce traffic gridlock and attract city dwellers to urban attractions. Ironically, regions moved to densification planning partly because of unsustainable costs related to sprawl development, including expenses for extensive road and sewer systems. “It’s time for the federal government to get more involved,” says an interviewee.

Condo Wave Curls. Toronto, North America’s largest condominium market, sees new apartment towers sprouting like weeds “everywhere” in an “absolute boom.” Developers have been “building where they shouldn’t.” In recent years Vancouver’s waterfront and hillsides underwent similar skyline makeovers, and more recently Montreal and Calgary have experienced strong condo building sprees. Condo mania has extended to other Canadian cities like Halifax and St. Johns as well—all part of urbanization and densification trends, encouraged by local governments and driven by significant buyer and renter demand.

All the activity finally raised alarms at the Bank of Canada, and 2013 should answer the question as to whether the bank’s actions to temper demand, including establishing higher hurdles for foreign buyers to obtain mortgages, were too aggressive or helped restore a balanced market. Many interviewees wonder whether the restrictions were necessary. “Everything seems to be bought.” If buyers choose not to occupy, they find renters: either young professionals or immigrants help fill units and support relatively low mortgage carrying costs, and continued strong immigration should enable more development, some interviewees argue. Others suggest that buying had progressed to unsustainable levels, especially for high-end units, driven by an “if I don’t buy now, I’ll lose out” mentality. Concerns also grow about the staying power of offshore investors should they experience financial reversals back home.

Increasingly “cautious” banks received their regulator’s message loud and clear, scrutinizing developers’ track records and project quality more closely. Greater weight is placed on loan requirements for reaching significant presales and downpayments before construction starts. “More projects will be deferred or pulled back” with possible “value flatness for the next two to three years.” The biggest threat to the market would be higher interest rates. That’s when buyers would walk away from prepayments and some unit owners would have trouble keeping up with mortgage bills. However, interviewees see low risk of that scenario in 2013.

Reasonable Development Pipeline. Even though condo developers prepare for a slowdown after the robust pace of high-rise construction, cranes are expected to remain visible along major city skylines. A steady stream of projects in the development pipeline will not be delivered for several years, and with most interviewees expecting continuing buyer demand over the medium term, this should contribute to a reasonable ongoing market for new projects in “a more normalized cycle.” Any pullback in new construction should tighten already “good supply/demand dynamics,” based on encouraging urbanization trends, which support an increase in buying and renting as jobs and businesses cluster in and around city centers. If more stringent underwriting weeds out speculators and borderline borrowers, this can only translate into a more favorable balance that will support stable or increasing values over time. Recent sticker shock on downtown projects, especially in the Greater Toronto area (GTA)—and the Greater Vancouver area—have spurred mid-rise condo construction in infill areas, as well as homebuilding outside the greenbelt. “People want larger, more affordable units suitable for families,” whereas much of the new downtown construction features small layouts marketable to young professionals and couples, or empty nesters. What happens when gen-Y residents in these buildings decide to have kids?

Development charges, passed on to buyers, become “a massive issue—up to \$16 or \$17 per square foot” in some jurisdictions as local governments tap into the building boom to fill their coffers. The GTA municipalities charge homebuilders up to \$60,000 a door because “demand allows for it.” Interviewees also continue to complain about “needless” government red tape in the zoning and permitting process, which “unnecessarily” adds to costs and can stymie projects. Slowing construction activity in some markets should help “stabilize” construction costs, which escalated during the building boom. But budgets could face offsetting increases from tariffs on imported construction materials.

Typical Commercial Building Restraint. Always under relative control, activity on the commercial side remains more constrained. Any new construction keeps up with increasingly

measured demand and does not race ahead of it. Few prime development sites remain in either Toronto or Vancouver and “stay in a few hands.” Calgary, with more available building sites, can generate a semblance of boom/bust cycles, but the market never seems to stay out of kilter very long because of growing energy markets. Potential approvals of controversial pipeline projects from Alberta to the United States and into British Columbia would boost real estate construction prospects further. Although pension funds and other institutional investors resist speculative development, they selectively seek expansion and renovation opportunities in existing portfolio holdings in an effort to increase yields and maintain a competitive edge in aging buildings.

Transforming Tenant Demands. Office developers take notice of how changing tenant requirements—open layouts, shrinking space use per capita, hoteling and other technology impacts, as well as operating and energy efficiency preferences—spread from the United States and force altered approaches to projects. They realize the need to deliver green product to attract prime space users, while institutional owners continue to focus on upgrading existing stock to LEED standards in order to remain competitive. “Green is huge in office. It’s become an intrinsic core value for tenants and fundamental for their business in attracting talent.” But some interviewees raise a familiar complaint: “Tenants want it, but aren’t willing to pay more for it.” Retail development orients away from the suburbs to densifying city center residential areas—particularly integrating supermarkets, other service retail space, and smaller versions of big-box chain store space into apartment complexes or convenient sites nearby. And every commercial developer wants to be as close to transit corridors as possible; businesses place an increasing premium on proximity to rail and subway lines.

Essential Immigration Drivers. “The trend of ‘the west is best’ will continue.” Eastern Canada gains from its “depth” of population and diversity of businesses, including Toronto’s powerful financial industry, but western Canada benefits from the “dynamics” of the jobs-generating industries of oil, gas, and commodities. Flows of about 250,000 immigrants annually from overseas—mostly from Asia and the Middle East—begin to redirect to Edmonton, “the staging ground for oil sands” work. The federal government and provinces collaborate better to identify hiring needs and bring people to satisfy them. As the profile for nonimmigrant Canadians ages into graying demographic cohorts, immigration will remain the lifeblood for housing demand, commercial and multifamily development, and retail sales, especially in expanding relatively high-growth western cities. Traditional immigration magnets—Toronto and Montreal—will continue to prosper from flows of newcomers along established international pathways. Newer areas of

economic activity, such as the Maritime Provinces, will attract greater immigration as a result of the coastal energy boom that will undoubtedly create new jobs.

“Leveling” Cap Rates. Investors’ proclivity to secure income over long-term holding periods tends to sedate deal making and helps insulate markets from volatility, although commercial markets registered record transaction volumes during 2012. Again, the *Emerging Trends Canada* barometer settles in a familiar positive zone for 2013 with buy/hold/sell sentiment essentially aligning (exhibit 5-5). Survey respondents expect little further downward movement in “low-as-you-can-go” cap rates, especially for apartments, regional malls, and downtown office space (exhibit 5-6). The exceptions will be for prime development sites in and around downtowns, especially for stores. “Land values in core districts will keep going up.” If anything, it may be a slightly better time to sell than buy, but then given limited investment alternatives, owners probably are better off holding. And as noted, that “is just what most successful Canadian investors do out of habit anyway.”

Plenty of Capital, Not Enough Deals. “The stars could not be better aligned” for attracting capital into Canada’s reliably solid real estate markets: they look as good as any place to invest in the world. Rational leverage levels, extremely low default rates, high occupancies, and low interest rates all combine to reinforce investor and lender confidence in an asset class generating attractive yields. For 2013, *Emerging Trends* respondents expect balance in debt availability—meaning debt will neither

EXHIBIT 5-5
Emerging Trends Barometer 2013

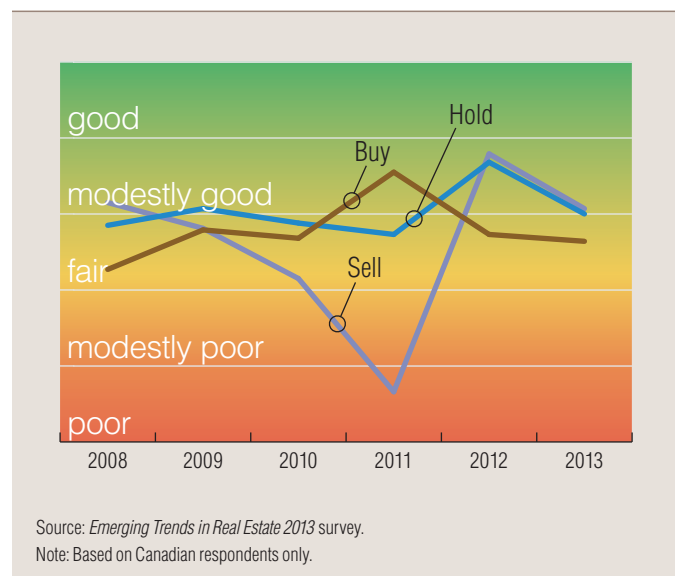


EXHIBIT 5-6

Prospects for Capitalization Rates

Property type	Cap. Rate August 2012 (percent)	Expected cap. rate December 2013 (percent)	Expected cap. rate shift (basis points)
Regional malls	5.22	5.15	-7
Apartment residential (rental)	5.14	5.18	4
Apartment: moderate income	5.38	5.36	-2
Central city office	5.48	5.43	-5
Warehouse industrial	6.07	6.00	-7
Power centers	6.13	6.21	8
Full-service hotels	6.25	6.25	0
R&D industrial	6.60	6.45	-15
Neighborhood/community shopping centers	6.54	6.54	0
Suburban office	6.55	6.62	7
Limited-service hotels	8.00	8.00	0

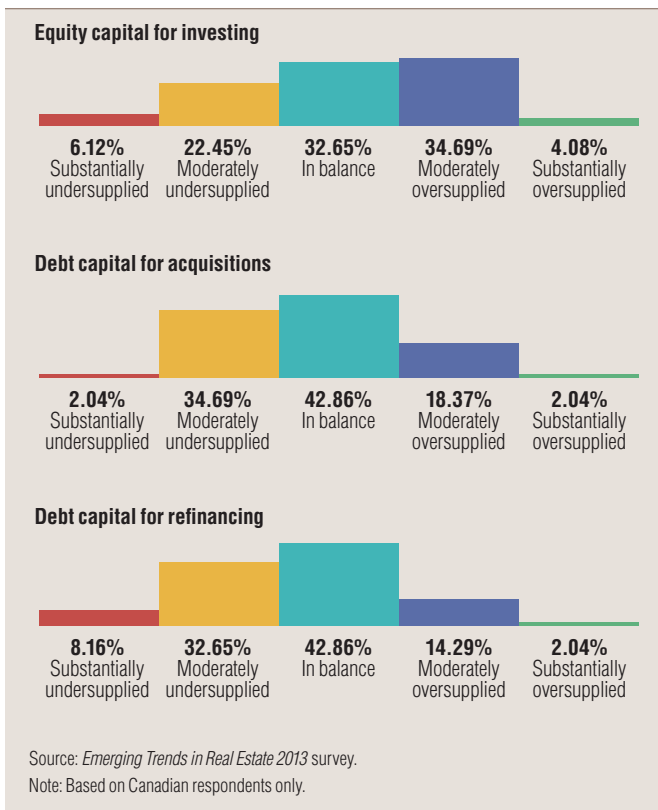
Source: *Emerging Trends in Real Estate 2013* survey.
Note: Based on Canadian respondents only.

be over- or undersupplied, although high-credit borrowers will have better access, especially for condo-related construction loans where lenders will be more discriminating and reject less-experienced developers (exhibit 5-7). Already-rigorous underwriting standards promise to turn stricter. “Adventurers and amateurs will be eliminated” in the condo arena, and ten-year financing is tough to secure because life insurers want to avoid getting caught with liability mismatches should interest rates rise as expected over the medium to long term.

Ample cash positions search for yield but tend to find few opportunities in private equity real estate: both pension funds and “more aggressive” REITs “have capital to invest, but haven’t been able to achieve their investment goals.” As a result, institutional investors will continue to look outside the country, and REITs may muscle into pension-fund turf, bidding on available higher-profile trophies, as exemplified by the recent Scotia Plaza transaction in Toronto. Foreigners wish to enter Canadian markets “looking for a safety net,” although the Canadian dollar offers no currency advantages. Foreign investors are confronted with various legal hurdles, which only make it more difficult to compete with domestic players, who are naturally more adept at maneuvering on their home turf. New sources of capital—private REITs, boutique real estate funds structured as trusts or limited partnerships, and various other money manager vehicles—sprout up to attract high-net-worth investor interest in the asset class. Searching for product, and marketing five- to seven-year holding periods similar to U.S. value-add or opportunity funds, these nascent vehicles may keep returns lower

EXHIBIT 5-7

Real Estate Capital Market Balance Forecast for 2013



in secondary markets and “the nontrophy asset tiers.” These vehicles could also get involved in development deals, financing borderline projects rejected by traditional lenders.

Markets to Watch

“Canada’s real estate market has an appetite for transactions, but it is difficult to find deals.” Even during a questionable global economy, the Canadian commercial real estate market continues to grow and attract capital. “Real estate concerns are reducing, even with global economic uncertainty,” an investor says. Even with that attitude, investors still have their eyes wide open on the European debt crisis, China’s decline, Middle East conflicts, and the struggling U.S. economy. In 2013, Canada’s stable economy, job growth, and alluring assets will continue to be an attraction to both domestic and foreign capital. Equity is in abundance, and debt for acquisitions looks to be in balance. Investors need to allocate this capital, and “instead of keeping cash, they look for great assets—real estate.” Without a correction in sight, there is anticipation in the industry that transactions

will continue to be based on sharper, more aggressive moves. It has turned into a “professional’s market,” in which those with exceptional skills to complete deals will succeed. However, looking for and acquiring real estate might be slightly more difficult next year as the hunt for quality assets continues. “Investors are more yield challenged, and searching for good assets is tough,” states a potential buyer.

The large institutional owners of high-quality assets in prime markets make the search difficult due to their long-term investment strategy. In addition, prices might seem high, but most interviewees think they will still rise a little more—if you can “get the deal done.” With those struggles, and still the appetite and desire for real estate, investors have focused on strong tenant-based properties in secondary markets, or “Class B space in Class A markets.” Supporting this trend, interviewees are quoted as saying, “there is a demand for quality property in all markets,” “flight to quality for purchasers,” and “we’re moving into secondary markets.” However, not all investors are ready to take on additional risk in secondary markets at this stage of the game. Some interviewees state, “shy away from the secondary markets,” and “we tend to stay away from secondary markets as liquidity is an issue.”

As investors look for quality, through investment or development assets, other “older properties” continue to wait in limbo. A quality-based division is forming as capital continues to shy away from aged assets. Growing urbanization, transit challenges, creative and efficient space design, and a growing demand for green, energy-efficient buildings continue to shape the real estate landscape. Interviewees note, “sustainability and green: it’s here forever,” “tenants continue to become more space efficient,” and “LEED certification, more contemporary design; access to transit corridors is essential.” As these trends grow, new and next-generation companies will continue to use these features to attract and retain their best employees. Landlords looking to compete and grow should follow this direction to attract valuable tenants.

Overall Results

Even with this product chase and a possible need to change investment strategy, *Emerging Trends in Real Estate* survey results for investment, development, and homebuilding prospects managed to improve for most metro areas. Of the nine markets covered for commercial/multifamily investments, one was ranked “good,” six were “modestly good,” and two were “fair.” This performance is far better than 2012, when markets were basically split between “modestly good” and “fair.” The average rating value for all markets improved as well, moving from a 5.85 to 5.95, with only three markets seeing declines. The top movers were Montreal and Winnipeg, a primary and a secondary market. The larger markets such as Toronto, Montreal, Vancouver, and Calgary prevailed with an average value of 6.21, but still showed a decline from last year. Smaller markets averaged a score of 5.73, a year-over-year increase in value of 0.18 points. This is a modest indicator that investors are ready to make some moves into secondary markets.

Development prospects were even more impressive, showing positive movement with a jump to 5.74 from 5.29, or to “modestly good” from “fair.” The increase in the prospect value was good for both primary and secondary markets. The primary market average was 5.99, compared with a score of 5.55 for secondary markets. Even so, similar to investment results, the secondary markets had a larger increase over last year, up 0.54, compared with an increase of 0.35 for primary markets. Top gainers in development included Calgary, Edmonton, and Montreal. One interviewee agrees with survey results, adding, “Development will continue to grow with ‘cross-pollination’—office/retail/residential.”

The biggest mover of the three *Emerging Trends* categories was the homebuilding arena, where average metro-area scores increased 0.65 points year-over-year to 6.20, an overall rating of “modestly good.” “The Canadian homebuilding industry needs to be building on a continual basis, as capacity is needed.” Results and sentiment like those are indications that strong home construction activity will be here for a while.

EXHIBIT 5-8

Equity Underwriting Standards Forecast for Canada

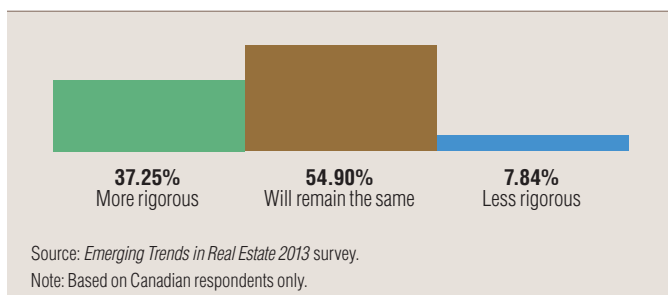


EXHIBIT 5-9

Debt Underwriting Standards Forecast for Canada

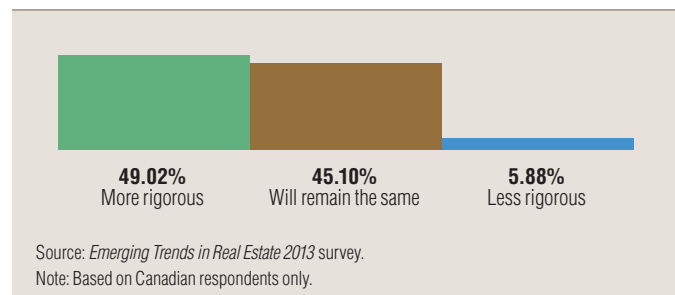


EXHIBIT 5-10

Markets to Watch: Overall Real Estate Prospects

	Investment	Development	Homebuilding
1 Calgary (1/1/2)	6.59	6.77	7.07
2 Edmonton (2/2/1)	6.52	6.35	7.08
3 Toronto (3/3/4)	6.18	5.95	6.19
4 Vancouver (4/5/6)	6.14	5.83	6.00
5 Ottawa (6/4/5)	5.88	5.92	6.15
6 Saskatoon (7/7/3)	5.70	5.37	6.47
7 Montreal (5/6/7)	5.93	5.41	5.77
8 Winnipeg (8/8/8)	5.41	5.05	5.67
9 Halifax (9/8/9)	5.16	5.05	5.44

Source: *Emerging Trends in Real Estate 2013* survey.

Note: Numbers in parentheses are rankings for, in order, investment, development, and homebuilding.

Markets to watch include Edmonton, Calgary, and Saskatoon. Primary markets beat the others again, scoring on average 6.26 and 6.16, respectively, for homebuilding. However, secondary markets saw a larger increase in their ratings values, jumping 0.92, compared with 0.30 for the primary markets. The trend of secondary markets scoring larger increases in rating values has been consistent for all three categories. The focus on secondary markets will substantially increase this year as investors continue to “chase yield” and find it more difficult to find product in primary markets.

Employment and Housing

Interviewees expressed mixed reactions regarding the future of certain macroeconomic drivers, such as employment, housing, and income. Optimists stated, “employment is stable,” and employment will be “slow and steady.” Pessimists counter, “unemployment is too high and will ultimately impact us,” and “higher unemployment is in the future.” The mix in responses is interesting in view of Canada’s overall economic performance. Since 2007, the nine Canadian markets covered will have added 720,000 jobs, in contrast with the United States, which will continue to show a net loss of 3 million jobs from pre-crisis levels. Next year’s job forecast for the same markets shows growth in Canada exceeding 2.4 percent, while the United States is forecast to see only a 1.0 percent increase. Finally, unemployment rates in Canada are below ten-year averages in five of the nine markets and the aggregate average is lower as well. The evidence indicates that unlike the United States, Canada has seen stable and slow growth in most economic indicators. A possible

explanation for the mixed outlook in the interviews is the fear of a negative shift in the global economy. If this were to happen, it would certainly hurt Canada’s economy and the commercial real estate market. However, overall interviewee consensus indicates “slow and steady” growth for the economy and the real estate market in Canada.

According to consensus forecasts, the housing market looks to maintain pace in the coming year. Forecasts from the Conference Board of Canada for overall housing starts in 2012 were 207,200, compared with 193,100 in 2013. Declines are usually considered a negative, but the 7 percent drop is viewed as a positive sign because Canadian housing and condo markets continue to see price movements that have a few saying the gloomy word “bubble.” One interviewee’s contrasting sentiment is reflected by his comment that “the market has come off, and the balance of sellers to buyers is healthy.” Projections show that housing resales will increase less than 1 percent at prices 2.5 percent higher than 2012. Another interviewee’s call is similar, stating “With continued low interest rates, housing prices will continue to rise.” The breakdown between eastern and western provinces shows interesting projections for 2013, as housing starts are projected to contract in the east and to expand in the west, excluding Saskatchewan. These forecasts are strongly supported by job growth expectations, as western cities show average increases of 2.1 percent, compared with 1.4 percent in the east. “Employment equals housing.”

Emerging Trends results support these statements. A comparison of city investment rankings to jobs shows the top four investment markets with 2013 job growth of 2.5 percent, compared with 2.3 percent for the other five markets. A comparison of prospective development markets yields conflicting results, with the top four markets projected to see 2.2 percent job growth, 40 basis points less than the five remaining markets. Prospects for homebuilding are just as would be expected: more jobs, more homes. The top four scoring markets show job increases of 3.0 percent, while the other five are anticipated to grow by 1.9 percent. Job growth and housing are two key drivers of commercial real estate success, and for Canada, both appear to be in balance, as stated by an investor: “We do not have any U.S.-style dead zones.”

Immigration, Migration, and Population

The need and chase for employment has led to an upward trend in immigration, a shift in migration between Canadian provinces and cities, and an increase in general population. The trend of a migratory increase in population over natural growth has been consistent as the country’s birth rate declines. In 2013, net immigration to Canada (the total number of immigrants minus the annual number of emigrants) is expected to range from 209,600 to 316,700, according to Statistics Canada. If one assumes the

higher estimate, Canada's total population is estimated to grow 1.4 percent next year, and the nine markets covered in *Emerging Trends* will average growth of about 1.7 percent. As the European recession lingers and U.S. economic growth remains slow, the flow of individuals remains a concern. "More immigration is going to Saskatchewan and Alberta, bringing in more skilled labor from Ireland and Europe." At first, increases in population are a positive sign for real estate; however, without enough job support to handle the increases, the economy could falter.

Migration (the flow of permanent residents from one Canadian market to another) was often discussed in interviews. Calgary looks to have the biggest jump in population, 2.3 percent, as many move to take advantage of Calgary's projected 2.8 percent increase in jobs next year. This trend is consistent across the top four markets with the largest job growth in 2013, which together show population increases of 1.9 percent, above the national average of 1.4 percent. "There is a mismatch in location of jobs versus where people are. This will change migration patterns." The west versus east matchup shows similar trends. Western markets' population looks to increase 1.8 percent, and eastern growth is 50 basis points behind at 1.3 percent. Finally, contrary to the investor demand shift toward secondary markets for investment-grade commercial real estate, lifestyle preferences will continue to drive population growth in the four primary markets, which are expected to grow by 2.0 percent, compared with an average of 1.4 percent growth in the five remaining markets. Even with a flow west, "Toronto will always retain the number-one position for immigration and migration."

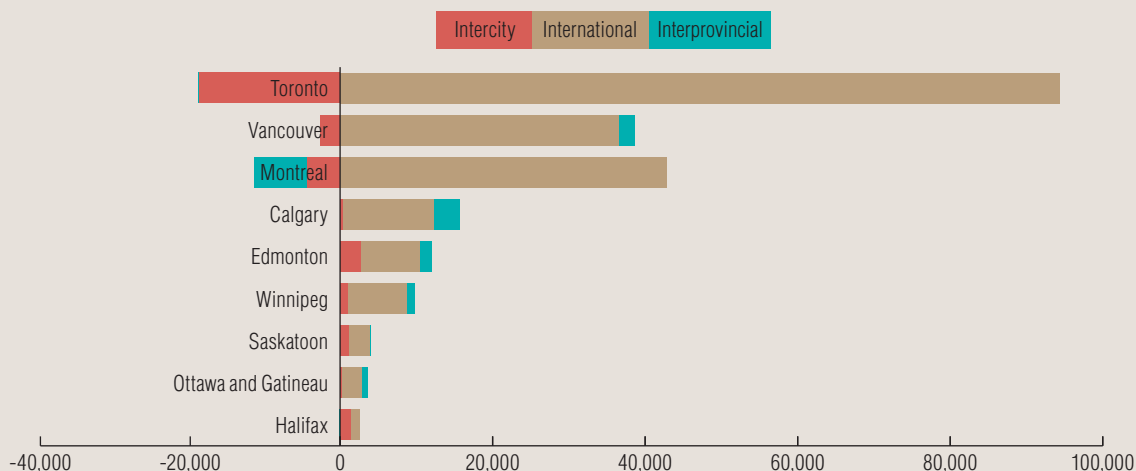
Urbanization and Transportation

With immigration and migration flows, a continuing trend is increasing "urbanization" of metropolitan areas, as Canada's workers prefer to live closer to where they work. "Major urban areas will see most of the investment capital as areas encourage the intensification of an urban culture." "New generations want to walk to work" in major urban centers like Vancouver, Toronto, and Montreal. "The choice to live in cities is no longer economic, but has now become cultural." Moving forward, each city will serve as the focus, creating and preserving an "identifiable" community. Commercial real estate will follow that trend, and "small-box retailers will move to where the people live." This tendency will not stop at major markets, though, as "urbanization will continue and will spread to smaller cities." At least one interviewee notes, "Urbanization, for two or three successive years, is still continuing, and it's everywhere, including midsized cities." Urban growth is not necessarily stimulated by natural population increases, but driven by larger city benefits that draw investments and an educated workforce. Corporate real estate is all about strategic locations for success, and these urban attributes offer everything the workforce desires.

Even with capital flow to urbanized locations and an increase in density, without proper infrastructure and transit, these locations will suffer. There are "inevitable requirements for improved infrastructure in all major cities." Ridership on conventional transit services has continued to increase year-over-year, supporting the additional need for "more contemporary transit corridors." As urban density pushes out to additional locations, the "need

EXHIBIT 5-11

2013 Net Migration Forecast



Source: Canadian Conference Board.

for good connectivity to downtown” is going to intensify. Many interviewees say they will follow: “We will be building more residential rental buildings on high-public-transit locations,” and “[We will see] continued urbanization and building near existing transit lines and future transit lines.” Whatever way you look at it, “tenants want to walk or be near public transit.” Markets that offer both options will succeed.

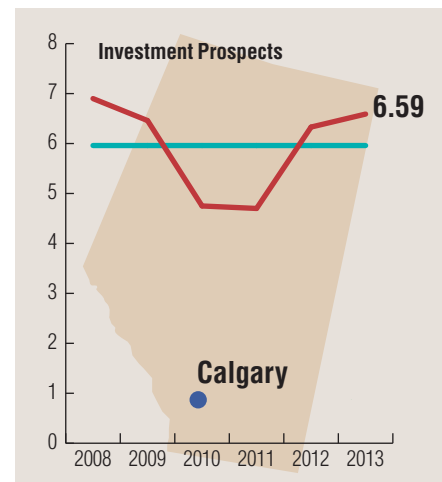
Metro Market Trends

Calgary (1). Growth, growth, growth is in Calgary’s future, as evidenced by economic fundamentals, commercial real estate volume, and *Emerging Trends* survey results. An expanding economy is requiring a larger and more highly skilled workforce, and numbers show that this trend will continue. Employment forecasts indicate growth of 2.8 percent next year and 2.9 percent in 2014. This growth, driven mostly by the oil and gas industry, has made it challenging to acquire high-quality real estate in this market. Absorption of prime properties has reached record levels, and rents are continuing to be pushed due to limited supply. “It’s harder to bid on local Calgary-area ‘A’-quality assets.” In 2013, this absorption and lack of space looks to continue, especially within office-type and industrial employment space because job numbers in these areas are expected to increase 3.6 percent and 2.6 percent, respectively. Construction will increase in the housing and nonresidential arenas, but will be nowhere near pre-crisis levels.

Calgary has impressive results and rankings in this year’s survey, registering first in investment prospects, first in development prospects, and second in homebuilding prospects. This is not a surprise for many participants, who maintain that “Calgary is heating up” and “Calgary is the best.” The city’s investment prospect ranking moved from third to first in 2013, receiving the only “good”

designation of the nine markets in the survey. High-quality opportunities might be difficult to find in this area, but investors will continue to hunt regardless of price. Calgary development had the largest gain in its rating value, up 1.1 points, moving into first as well. Demand will remain high and development is needed: total construction output will increase only 3.0 percent this year and 4.7 percent next. Calgary could not get the trifecta this year, though, as homebuilding in the market placed second to its northern neighbor, Edmonton. Housing starts should crack 10,000 in 2013, registering a marginal 4.4 percent increase year-over-year.

The buy, hold, and sell strategies show a majority of participants recommending a buy in three of the five property sectors. With over 56 percent of respondents recommending purchasing, industrial leads the focus, a 12 percentage point increase in this market over last year’s results. Apartments are a sector to buy as well, according to 55 percent of survey participants. One interviewee disagrees, though, stating “Calgary: not so good for residential sectors. It is a city

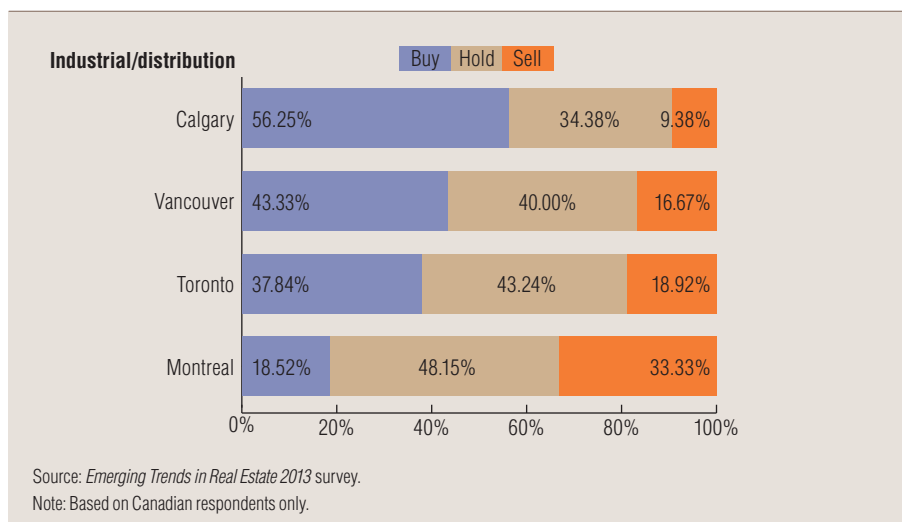


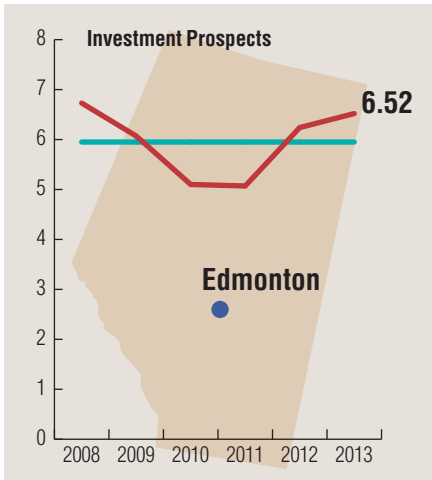
of homeowners.” Retail properties chalk up a buy, too, as retail sales increased close to 10 percent this year, and a 7.0 percent increase is expected next year. Results for office look great for owners, as 45 percent of interviewees recommend a hold for now. The lack of space, climbing rents, and anticipated cap rate compression put landlords in control in Calgary’s office environment.

Edmonton (2). Only about a three-and-a-half-hour drive from Calgary, Edmonton “is looking great” as well.

EXHIBIT 5-12

Industrial/Distribution Buy/Hold/Sell Recommendations





Strong consumer spending pushes the city's expected increase in 2012 gross domestic product slightly over 3.0 percent, increasing in 2013 to 4.0 percent. Employment growth has been continuous, as around 100,000 jobs have been created or filled since 2007. Unemployment forecasts predict a respectable 4.7 percent next year, but still 30 basis points below the ten-year average. With over 1.2 million residents, Edmonton continues to see population growth as many see the city as "the place to be." As Edmonton's energy-rich sector thrives, manufacturing follows with future expansion. Confidence in current and future oil prices provides a nice outlook for this oil-rich area. Say investors, "the world believes that oil is up for good," and "Edmonton is so small, and the oil industry finds it attractive."

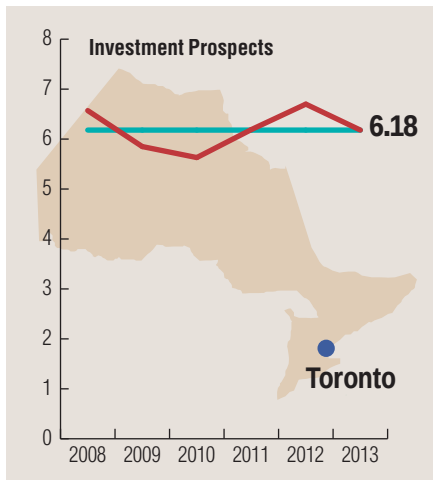
Emerging Trends survey results and real estate investors predict a good 2013 for Edmonton investment prospects: its rating value added 0.28 points, moving this market up two spots to second. Edmonton is an example that supports the trend to secondary markets in search of high-quality real estate investments in strong economic locations. "As a result of hard-to-purchase, quality 'A' properties, we have more willingness to go to another market such as Edmonton, Saskatoon, and Regina." With this growth

comes development, and Edmonton had a 0.87 increase in its rating value, moving to second from fourth. Nonresidential construction dominated, as projects like expansion of the Edmonton International Airport and Commonwealth Stadium's recreation center were completed. Housing starts statistics and survey results send mixed messages, as only a 1.1 percent increase in the number of new homes is forecast, but participants rank Edmonton as the number-one homebuilding area. Homebuilding prospects in Edmonton jumped three positions, and the city had the highest change in rating value of all nine markets. Regardless of the homebuilding outcome, Edmonton is a market on investors' radar. "Edmonton will outperform the others."

Toronto (3). The number-one market to watch in the 2012 *Emerging Trends* report, Toronto delivered mixed results and responses for 2013. Overall, this international market is still a top-three city, and capital will continue to flow to the area. "Toronto was my choice. People are renting by choice, occupancy rate is always good, employment is stable." Forecasts support this statement, as job growth is expected to increase 3.0 percent, gross domestic product should gain 3.5 percent, and the city's educated workforce is expected to see its personal income grow another 3.6 percent. Lower interest rates and continued interest in high-quality assets drove residential and nonresidential construction higher over the past two to three years. Construction output in those sectors looks to be slightly lower this year, but government infrastructure support should continue to add value to the Toronto market. As is the case in other primary markets, high-quality assets are difficult to obtain, and prices still look likely to escalate. Foreign capital will continue to focus on Toronto's assets, but, an interviewee predicts, "Sovereign funds will come to Canada when Europe gets worse. And when they do, they will focus on Toronto."

Survey results show Toronto taking steps back in all three categories this year. Investment prospect values fell 0.52 points to 6.18, and the city's rank went from first to third among the nine markets. Interestingly, the investment prospect value for 2013 is exactly equal to the *Emerging Trends* historical average for Toronto. Even though *Emerging Trends* values are survey driven, this may be a sign that the Toronto market as a whole is in a state of equilibrium. Development is the only category where Toronto improved its prospects, but not enough to keep the second spot, and the city dropped to third. Still, many large projects are set for completion in 2012 and in the years to come. Building makes sense because "it's the Toronto international market; everything can be sold quickly." Homebuilding continues to be a hot topic, but survey results forecast a slowing in 2013, landing the market in fourth. Toronto's rising home prices continue to be a concern, as expressed by many interviewees. "The Toronto and Vancouver housing markets, especially condos, have come off a bit, but interest rates are low, and the Bank of Canada and the Canadian government have introduced some fear, but not panic." "Multifamily starts will slow, but vacancy rates will continue to decline, reaching 1.3 percent in 2013. Mixed use-style properties, combining residential, commercial, and especially retail space, are a trend to watch for as additional properties are added to Toronto's inventory.

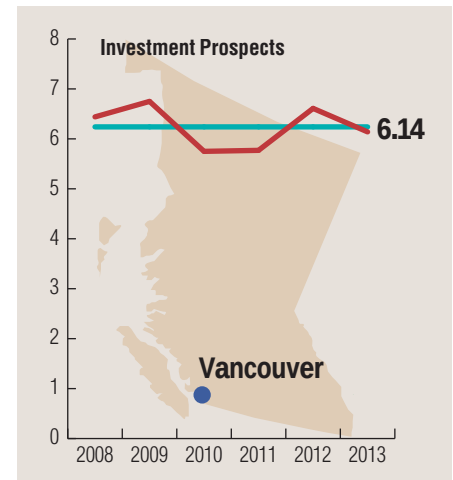
The decline in apartment vacancy rates and need for additional units is seen in the buy, hold, sell results. The only buy recommendation is found in the apartment sector, where the largest share of interviewees—48 percent—will continue to look at multifamily investments. "Toronto equals 'oversupplied' in high-rise development, but 'undersupplied' in low rise." Hold suggestions dominate in the remaining four property types. Even though the largest share of participants



24 months,” suggest that the city still has strong positive investor sentiment.

Vancouver (4). Vancouver’s economy has sharpened up and will look to continue that trend into 2013. Gross domestic product forecasts show growth of 2.5 percent in 2012, followed by a spike of 3.7 percent in 2013. The increase in production is driven by an expected increase in employment of 2.3 percent, exceeding ten-year average growth by 36 basis points. More than 72,000 jobs have been added to this market since the employment slowdown in 2009. With a slightly lower cost of living (with the exception of housing) than the country, Vancouver has seen consumer spending be a key driver of the economy. This trend looks to continue, with retail sales projected to increase another 4.8 percent in the coming year. These statistics are all great support for real estate, as some interviewees believe, “Vancouver is still positive and the place to be,” and “Vancouver is attractive.”

Some interviewees still believe in opportunities in Vancouver, but *Emerging Trends* survey results show declines in all three categories. The investment

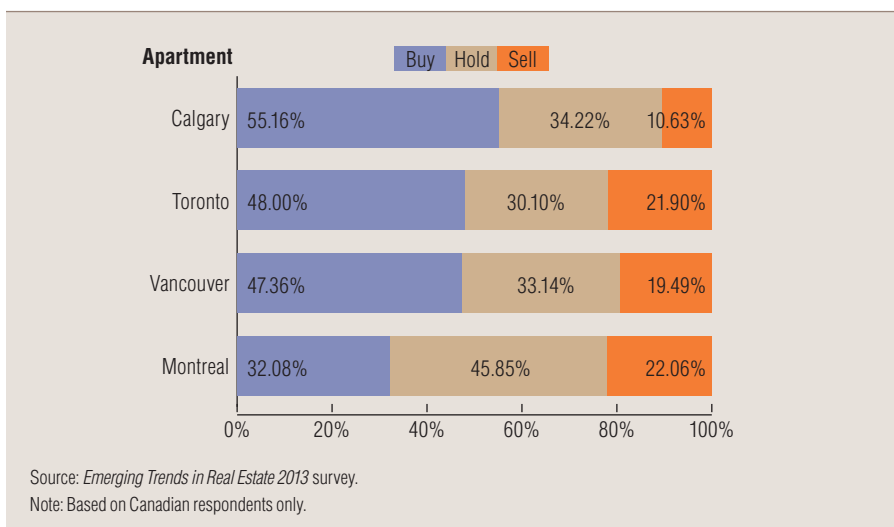


suggests hold, over 37 percent would buy retail commercial real estate in Toronto. Say interviewees: “new retailers need extra development capacity, especially around the Toronto area,” and “retail underserved by urban retail [i.e., malls] in Toronto; it is a closed market [i.e., a few developers controlling urban retail space] so retailers are being pushed away.” Toronto may have taken a few steps back in survey results, but comments such as “the city has strong fundamentals” and “it is a landlord’s market over the next 12 to

prospect value for Vancouver declined 0.47 points, and the rank dropped from second to fourth. An interviewee notes, “overbuilt Vancouver is flat. Lots of supply.” Development prospects showed similar movement—down in value and rank, falling from first last year to fifth in 2013. Vancouver’s government red tape continues to make it more difficult to develop real estate every year. Homebuilding prospects also do not look as strong year-over-year—down by a value of 0.50 points, from first to sixth. Housing start forecasts look to be just shy of 18,000 next year. “Less high-end product is moving in Greater Vancouver. Sellers are dropping prices. Lower-priced product continues to move.”

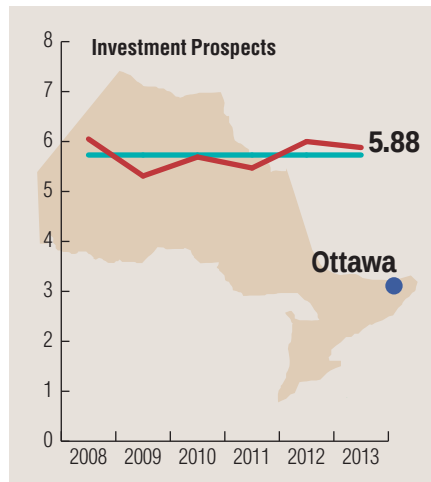
Even with a decline in rating values, prospects still exist in Vancouver. Buy/hold/sell recommendations suggest buying office, apartment, and industrial, in that order. Interviewees agree: “multiresidential is strong in Vancouver,” and “my personal choice is to live in Vancouver.” Office and apartment results are similar to 2012, but industrial saw a 6.5 percent spike in buy suggestions. The gradual sign of manufacturing growth is a key contributor to the increased interest in industrial space. The 2012 forecasts for manufacturing suggest 2.5 percent growth, marking the third-straight positive year.

EXHIBIT 5-13 Apartment Buy/Hold/Sell Recommendations



Ottawa (5). In 2013, the economic outlook for Ottawa looks weak. Population will increase only 0.8 percent, 90 basis points less than the average of the markets included in this report. Employment change does not look strong either, as projections show only a 1.0 percent increase, 35 basis points below the city's ten-year average. One buyer recommends, "stay out of Ottawa." The future of Ottawa's large number of government employees is questionable as federal cuts to balance the budget are underway. Employment in the public administration sector will decline 2.4 percent this year and an additional 1.5 percent next year. Economic slowdowns will affect residential and nonresidential construction, as declines in both areas are expected. With this decline in development, an investor says the "Ottawa market is very tight and will be difficult to enter."

Yet despite the challenging economic times, survey participants still believe in some opportunities in this market. Development prospects were rated "modestly good," up from "fair" last year, and moved from sixth to fourth overall. Even with a continuing slide in hous-



ing starts expected to last until 2015, homebuilding remained stable in fifth position, with a slight increase in rating value. Investment prospects for Ottawa declined, dropping one position to sixth. Responses covering various sectors seemed uninviting: "vacancies have been high due to impact of technology sector's poor performance," "Ottawa: seeing some consolidation of office space," and "the industrial market is expected to be fair at best."

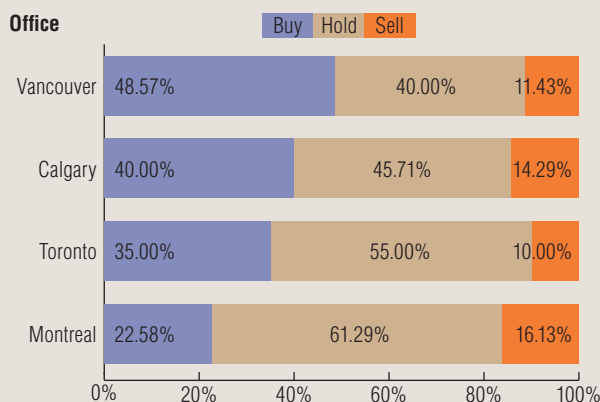
Saskatoon (6). A large amount of interest is heard from interviewees and survey participants regarding the smallest market of the nine covered. With an estimated population possibly reaching 285,000, based on a 2.0 percent growth rate, Saskatoon is continuing to attract interest from commercial real estate investors and developers. Investment prospects for the city increased to "modestly good," from "fair," but its rank dropped one spot to seventh. Employment statistics show continued growth driven by strong mining and housing construction sectors, as well as an improving manufacturing sector. This expansion is attracting capital, as "many are starting to participate in investments in the Saskatoon area."

Still, as the market strengthens, the future of further development remains questionable. Development prospects declined, but remain "fair." The city dropped from fifth to seventh rank on this measure, according to 2013 results. One interviewee disagrees, though, and plans on "land banking throughout Saskatoon for future development." Housing starts are forecast to slow in 2013 and beyond. However, homebuilding survey results differ, as Saskatoon jumps from sixth to third, receiving a "modestly good" rating. "Small growth in these areas is big growth."

Montreal (7). "Montreal's outlook is good, but maybe not very good." *Emerging Trends* survey results recommend a hold strategy in all five property sectors. Apartment and hotel were the only two sectors where some participants are looking to buy, as both cracked 30 percent, but the majority of respondents still suggest investors sit on what they have. Sell signals are fairly strong in the industrial sector, as one-third say it might be time to exit this area.

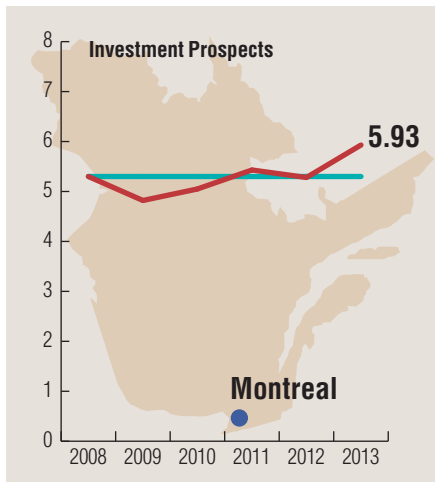
In 2013, economic development is moderate as gross domestic product forecasts display only 2.2 percent growth. Employment gains this year were zero, but some expansion—around 2.0 per-

EXHIBIT 5-14

Office Buy/Hold/Sell Recommendations

Source: *Emerging Trends in Real Estate 2013* survey.

Note: Based on Canadian respondents only.



cent—is projected for next year. “Major projects in infrastructure will continue and have an impact on availability of skilled workers.” Population in the market looks to remain consistent, increasing around 1.3 percent. However, interviewees say, “Montreal’s immigrants are not as wealthy as they may be in other Canadian cities,” and “Montreal does not benefit as much as it could from this influx of population.”

In spite of moderate economic drivers, the city’s investment prospects rank moved two spots higher to fifth overall.

Development prospect results were similar, shifting from eighth to sixth this year. A developer notes, “We are involved in a large number of prestigious Montreal development projects.” Homebuilding prospects improved, but settled into the seventh spot for the second year in a row. “Montreal benefits from a diversified economy [e.g., sectors health care, universities, life sciences/pharmaceutical, video, professional firms, aerospace, etc.], and outlook is optimistic over the long term.”

Winnipeg (8). In 2013, Winnipeg’s manufacturing sector looks to grow after having two years of severe declines. The economy has produced a steady recovery since contraction in 2009, as gross domestic product should increase 2.6 percent next year. With an increase in manufacturing and production comes an increase in employment, which is expected to gain 2.0 percent, exceeding its ten-year average by 80 basis points. With these components in place, “to us Winnipeg seems like a steady market of opportunities.” The city has outperformed the other covered markets in job change since 2007, as 229,000 positions were

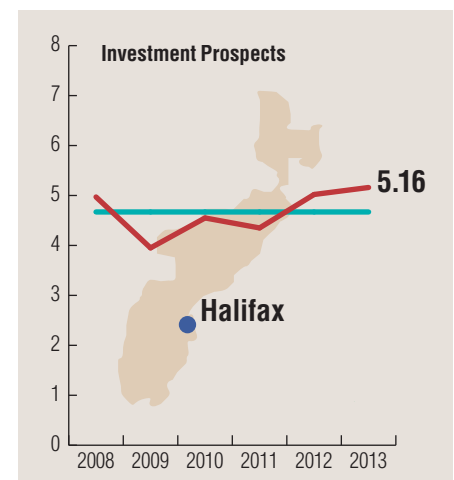
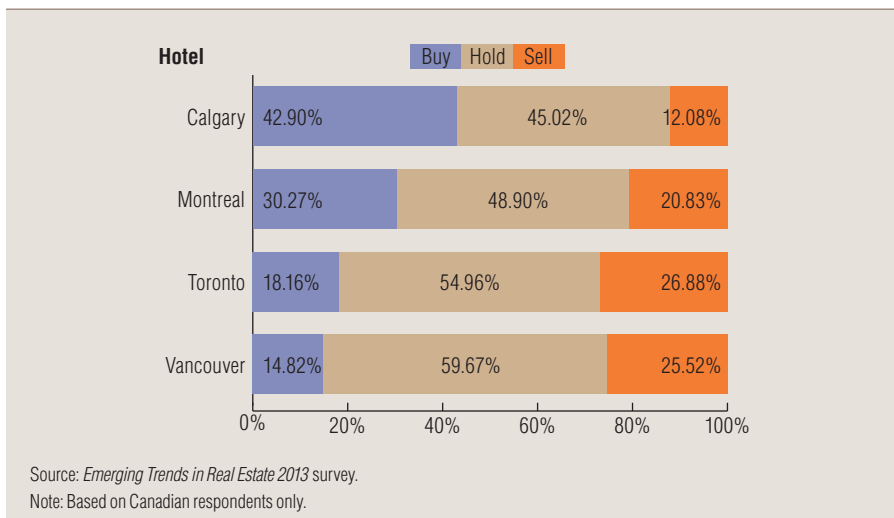
filled over those five years. However, population growth is minimal, only increasing 1.3 percent, 40 basis points below the average of the other markets. “We think the market is good, but it really depends on price,” states an investor.

Winnipeg’s favorite number must be eight, as it managed to secure that position in all three categories. With manufacturing and job-growth drivers increasing, investment prospects for the market increased as well. Winnipeg received the eighth position in investment prospect rank, moving up 0.41 points in value. Development showed the same movement, up one spot to eighth. Homebuilding, which was eighth in 2012, stayed in that position in 2013. Housing starts have displayed continuous increases, and that trend will continue, with a jump of 6.7 percent expected. Construction output has strengthened, both in residential and nonresidential, as absorption and inventories remain in check. Says one investor, “Winnipeg will outperform in the retail sector,” but another claims, “the city will underperform in the industrial sector.”

Halifax (9). “[For] commercial real estate in Halifax, lease rates continue to be depressed.” Economic drivers are positive, but slower than many of the other Canadian markets. Gross domestic product and employment projections show 2.2

EXHIBIT 5-15

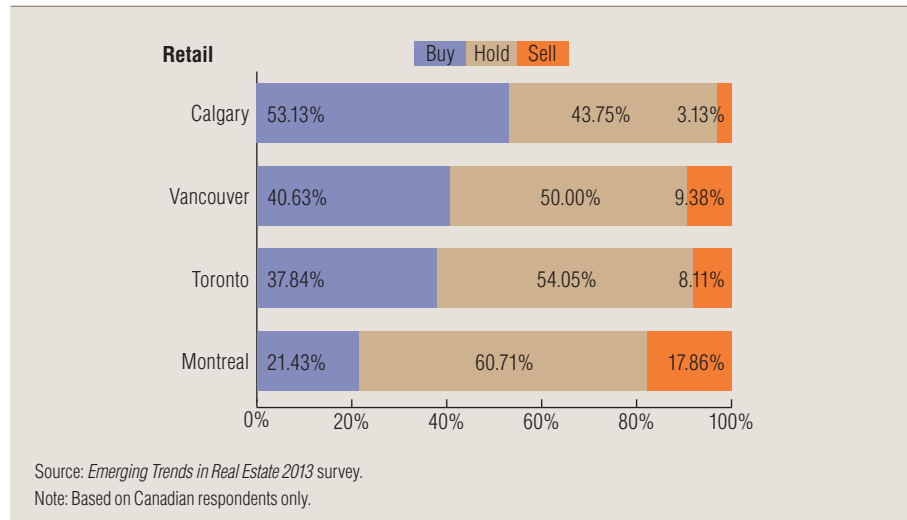
Hotel Buy/Hold/Sell Recommendations



percent and 2.1 percent growth, respectively. Population is just over 400,000 and growth is only 1.1 percent, 60 basis points lower than the nine-market average. Manufacturing growth should pick up next year, as a \$25 billion contract for supplying combat ships is underway. Says an interviewee, “Halifax will be a very strong location for investment for the next five years due to the shipbuilding contract.” Still, it is difficult to buy assets in this market due to its small size.

Investment, development, and homebuilding prospect values all increased in year-over-year comparisons. However, the gain in investment prospects was not enough to get Halifax out of ninth place. Development fared a little better, moving to eighth in a tie with Winnipeg, up from ninth in 2012. A decline in housing starts looks likely to continue in 2013, as only 2,235 are projected. *Emerging Trends* survey results agree, as Halifax stays in last position for homebuilding. Halifax is an attractive market, due to cost. However, one interviewee believes “the layers of bureaucracy and time needed to get buildings constructed and occupied make it a very difficult location to do business.”

EXHIBIT 5-16

Retail Buy/Hold/Sell Recommendations

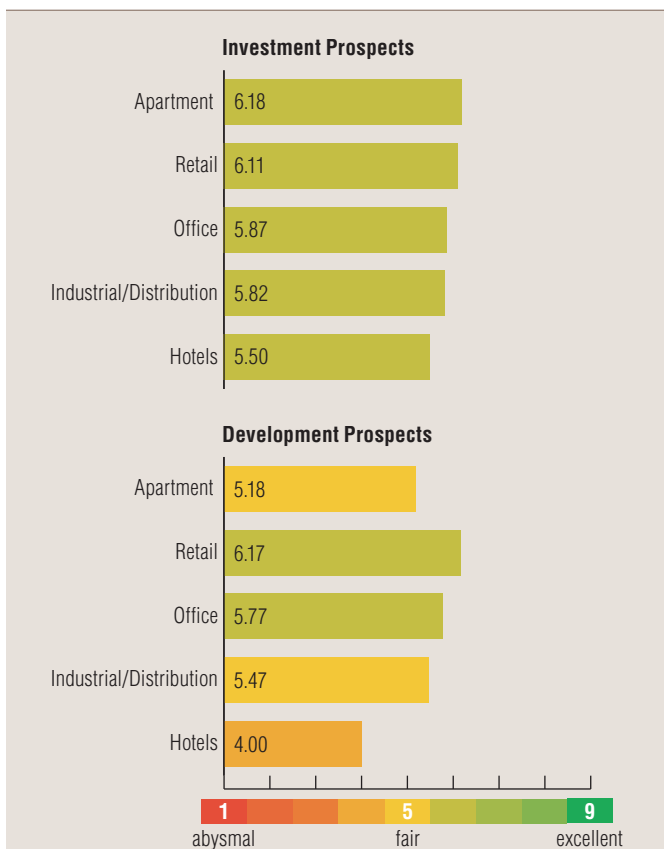
Property Types in Perspective

Emerging Trends surveys highlight “modestly good” investment and development prospects across most property sectors for 2013 (exhibit 5-17), reflective of expected solid supply demand fundamentals in commercial categories. Housing sectors also score favorable marks, except for second and leisure homes.

Apartments. The recent condo buildup has not softened multiresidential markets; “they’re stronger than ever.” Like “bond investments,” landlords reliably can increase rents, supported by high occupancies and steady appreciation. Confident lenders extend financing “for next to nothing,” and cap rates reach “shockingly low levels” in some markets. With development concentrated on units in higher-end-market condo towers (which many buyers rent out), existing apartment stock in middle-market urban neighborhoods meets ample leasing demand for

EXHIBIT 5-17

Prospects for Major Commercial Property Types in 2013

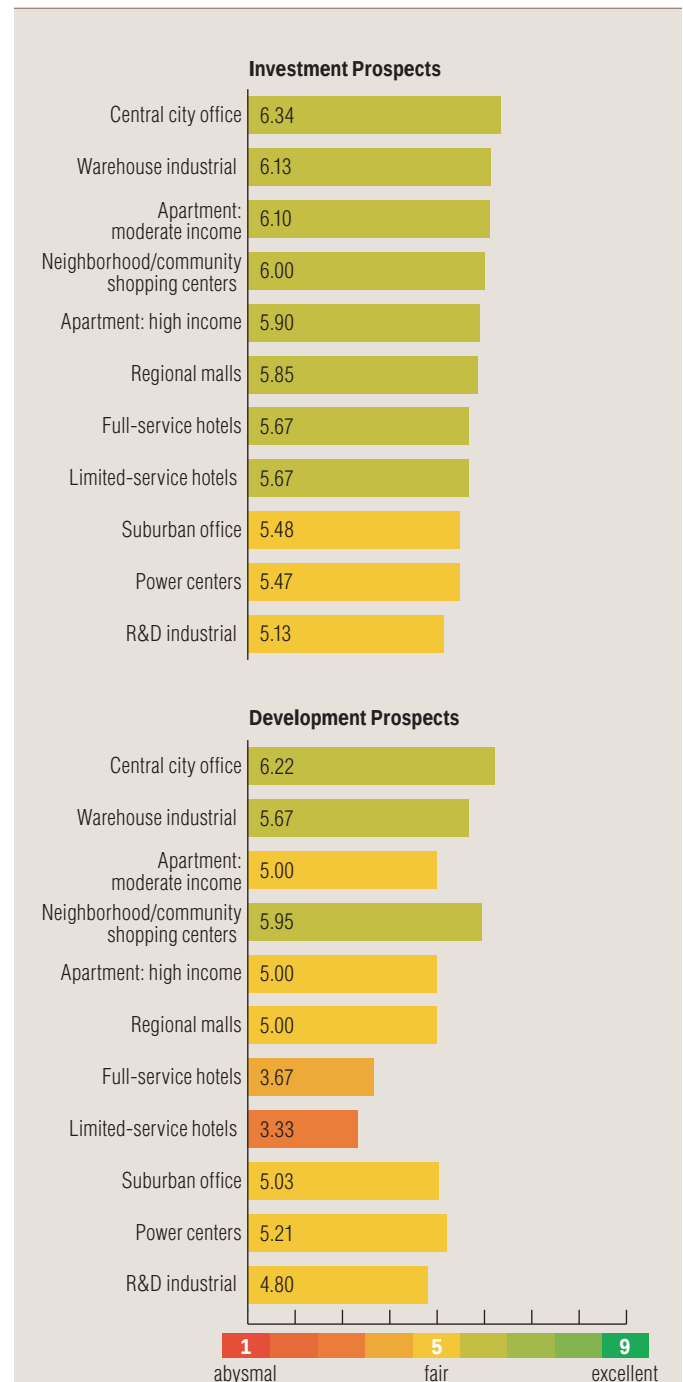


Source: *Emerging Trends in Real Estate 2013* survey.

Note: Based on Canadian respondents only.

EXHIBIT 5-18

Prospects for Commercial Subsectors in 2013



Source: *Emerging Trends in Real Estate 2013* survey.

Note: Based on Canadian respondents only.

EXHIBIT 5-19

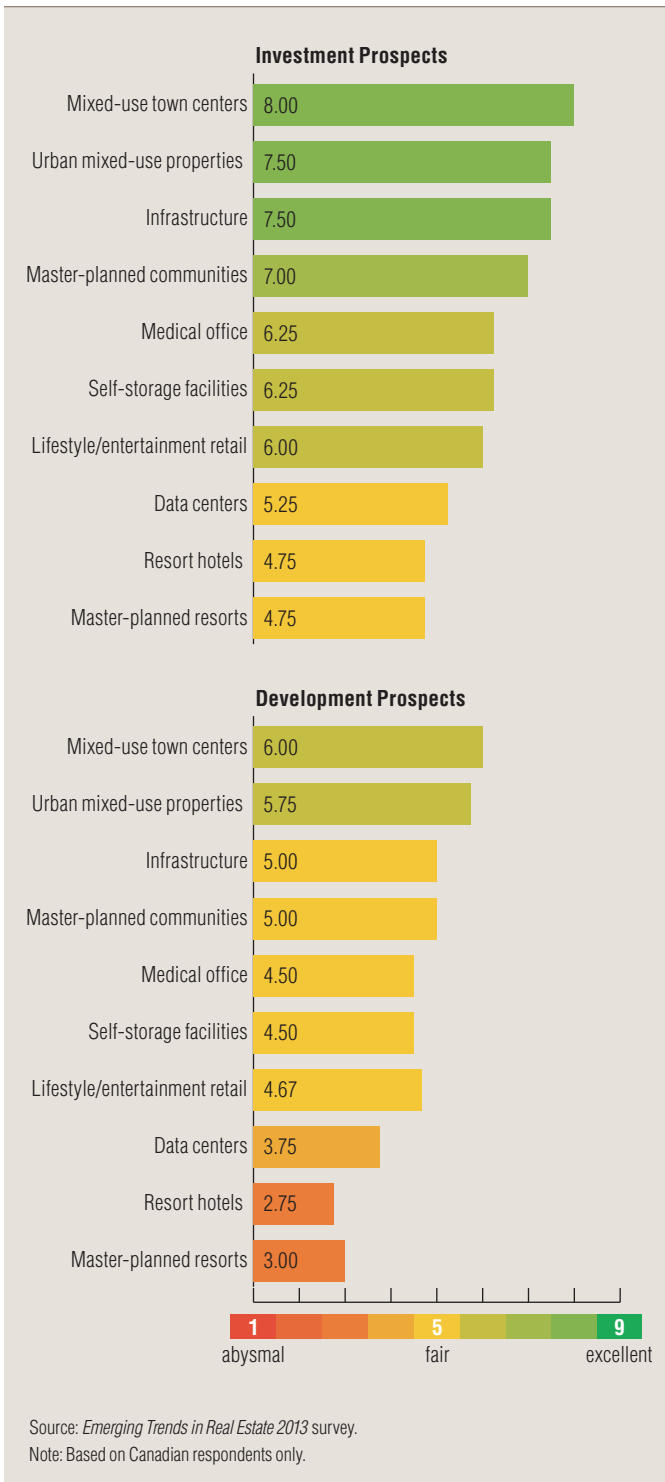
Prospects for Niche and Multiuse Property Types in 2013

EXHIBIT 5-20

Apartments—Moderate Income

2013	Prospects	Rating	Ranking
Investment prospects	6.10	Modestly good	3rd
Development prospects	5.00	Fair	6th
Buy 33.3%	Hold 33.3%	Sell 33.3%	
Expected capitalization rate, December 2013		5.4%	
Source: <i>Emerging Trends in Real Estate 2013</i> survey.			
Note: Based on Canadian respondents only.			

EXHIBIT 5-21

Apartments—High Income

2013	Prospects	Rating	Ranking
Investment prospects	5.90	Modestly good	5th
Development prospects	5.00	Fair	6th
Buy 33.3%	Hold 41.7%	Sell 25.0%	
Expected capitalization rate, December 2013		5.2%	
Source: <i>Emerging Trends in Real Estate 2013</i> survey.			
Note: Based on Canadian respondents only.			

lower-cost options, especially from career starters and newly arrived immigrants. In older districts, many buildings require overhauls or replacement. Investors looking for value-add opportunities can upgrade units. “It’s a broken record: multires is always a good bet.”

Office. Rents and values “keep going up,” reaching replacement-cost levels as a handful of new towers readily lease up in major markets, paving the way for additional new construction. Developers will look to take advantage of strong tenant appetite for efficient layouts in sought-after green projects, which house more workers in less space and can reduce operating costs. “They are head and shoulders above older buildings.” Brokers are starting to make headway on sales pitches for higher rents in these new-generation towers, highlighting offsets from lower expenses. “Everybody wants to maximize everything. They like more output for less space.” This “inexorable” march toward efficiency is “a normal course of business”; it is as important to office markets as urbanization trends, and more owners of existing skyscrapers must undertake “surprisingly” expensive retrofits to stay competitive or risk dropping to B-quality status. In the unlikely event overbuilding occurs, “it will be at the

EXHIBIT 5-22

Central City Office

2013	Prospects	Rating	Ranking
Investment prospects	6.34	Modestly good	1st
Development prospects	6.22	Modestly good	1st
Buy 43.3%	Hold 33.3%	Sell 23.3%	
Expected capitalization rate, December 2013		5.4%	

Source: *Emerging Trends in Real Estate 2013* survey.
Note: Based on Canadian respondents only.

EXHIBIT 5-24

Neighborhood/Community Centers

2013	Prospects	Rating	Ranking
Investment prospects	6.00	Modestly good	4th
Development prospects	5.95	Modestly good	2nd
Buy 55.0%	Hold 30.0%	Sell 15.0%	
Expected capitalization rate, December 2013		6.5%	

Source: *Emerging Trends in Real Estate 2013* survey.
Note: Based on Canadian respondents only.

EXHIBIT 5-23

Suburban Office

2013	Prospects	Rating	Ranking
Investment prospects	5.48	Fair	9th
Development prospects	5.03	Fair	5th
Buy 16.1%	Hold 54.8%	Sell 29.0%	
Expected capitalization rate, December 2013		6.6%	

Source: *Emerging Trends in Real Estate 2013* survey.
Note: Based on Canadian respondents only.

EXHIBIT 5-25

Power Centers

2013	Prospects	Rating	Ranking
Investment prospects	5.47	Fair	10th
Development prospects	5.21	Fair	4th
Buy 20.0%	Hold 75.0%	Sell 5.0%	
Expected capitalization rate, December 2013		6.2%	

Source: *Emerging Trends in Real Estate 2013* survey.
Note: Based on Canadian respondents only.

expense of older buildings with obsolete space.” A transformation in medical practice and an aging population in need of increased health care services lift prospects for medical office space. Hospitals “decant nonessential services,” and more doctors are forming multiple-practitioner clinics. Space near hospital centers commands a premium; cap rates in some markets decline to 6 percent. Doctors and lab operations seek “large floor plates” and “flatter buildings” that provide patients with dedicated medical environments.

Retail. Already-tight markets will tighten further as U.S. retailers expand into Canada, led by Target, Nordstrom, and Lowe’s. The entry of new chains precipitates “a dynamic moving around of tenants” and “sounds the death knell” for some weaker domestic brands in “the most Darwinian of property sectors.” Owners revel in the activity as the U.S. interlopers find difficulty securing sites and force out struggling competition by taking their space, often at higher rates. The sector’s small club of developers, meanwhile, continues to work “hand in glove” with retailers to meet their needs and “keep supply from getting out of whack.” Zoning restrictions and ever-vigilant lenders also

EXHIBIT 5-26

Regional Malls

2013	Prospects	Rating	Ranking
Investment prospects	5.85	Modestly good	6th
Development prospects	5.00	Fair	6th
Buy 30.0%	Hold 60.0%	Sell 10.0%	
Expected capitalization rate, December 2013		5.2%	

Source: *Emerging Trends in Real Estate 2013* survey.
Note: Based on Canadian respondents only.

keep a check on new development. But owners must begin to contend with integrating e-commerce platforms and dealing with retailers’ locational strategies. Given high occupancies and strong demand, the expected preference of tenants for smaller store layouts should not undermine property revenue streams or values. All the chains fight for good sites in undersupplied urban centers. The wave of new condo residents demands convenient

shopping at familiar brand-name stores, and developers look to accommodate: they pay up for land, but can charge premium rents. Older suburban centers make prime candidates for redevelopment into new shopping formats. Unlike the United States, Canada is not oversupplied with retail space. Interviewees register only minor concern about whether more subdued housing markets and high household debt could affect store sales.

Industrial. Warehouse vacancies have declined and investors like the steady cash flows, but the sector seems mired in comparatively “slow growth,” hampered by the strong currency and related exchange-rate issues, especially around Toronto and Montreal. Import/export flows remain somewhat compromised by south-of-the-border turbulence. “It’s difficult to find pockets of real growth with auto and aerospace industries still off.” At least supply is not an issue because developers have backed away in the face of generally “weak leasing markets,” with rents below replacement cost, but “creeping up.” Not surprisingly, smaller western distribution markets perform considerably better, boosted by commodities activity; owners can register rent “leaps” on new leases. Generally, a widening gap in the level of investor demand develops between more favored new, high-

ceilinged distribution space—where tenants tend to concentrate leasing activity—and increasingly obsolete older warehouses, which suffer noticeably higher vacancies.

Hotels. Prospects for hotels should continue to improve.

Occupancies and room rates crawl back to 2007 peaks in the big cities, and RevPAR is not far behind. Outside of Calgary, interviewees see little room for much new development, with the exception of adding popular all-suite limited-service brands, catering to business travelers, in certain downtown markets.

Housing. Housing markets appear primed to hold relative values, and population inflows from overseas almost guarantee steady future demand for new homes. Respondents appear modestly bullish about prospects for condo (high rise and mid rise) and home construction, especially in urban and infill areas, as well as town centers. Increasingly steep prices for housing closer to urban cores should create greater demand for more affordable single-family homes in outer suburbs. Expensive high-end condo units lose some luster as demand tails off; affluent offshore buyers become less active.

EXHIBIT 5-27

Warehouse Industrial

2013	Prospects	Rating	Ranking
Investment prospects	6.13	Modestly good	2nd
Development prospects	5.67	Modestly good	3rd
Buy 37.5%		Hold 56.3%	Sell 6.3%
Expected capitalization rate, December 2013		6.0%	

Source: *Emerging Trends in Real Estate 2013* survey.
Note: Based on Canadian respondents only.

EXHIBIT 5-29

Hotels—Limited Service

2013	Prospects	Rating	Ranking
Investment prospects	5.67	Modestly good	7th
Development prospects	3.33	Poor	11th
Buy 33.3%			Hold 66.7%
Expected capitalization rate, December 2013		8.0%	

Source: *Emerging Trends in Real Estate 2013* survey.
Note: Based on Canadian respondents only.

EXHIBIT 5-28

R&D Industrial

2013	Prospects	Rating	Ranking
Investment prospects	5.13	Fair	11th
Development prospects	4.80	Fair	9th
Buy 12.5%		Hold 62.5%	Sell 25.0%
Expected capitalization rate, December 2013		6.5%	

Source: *Emerging Trends in Real Estate 2013* survey.
Note: Based on Canadian respondents only.

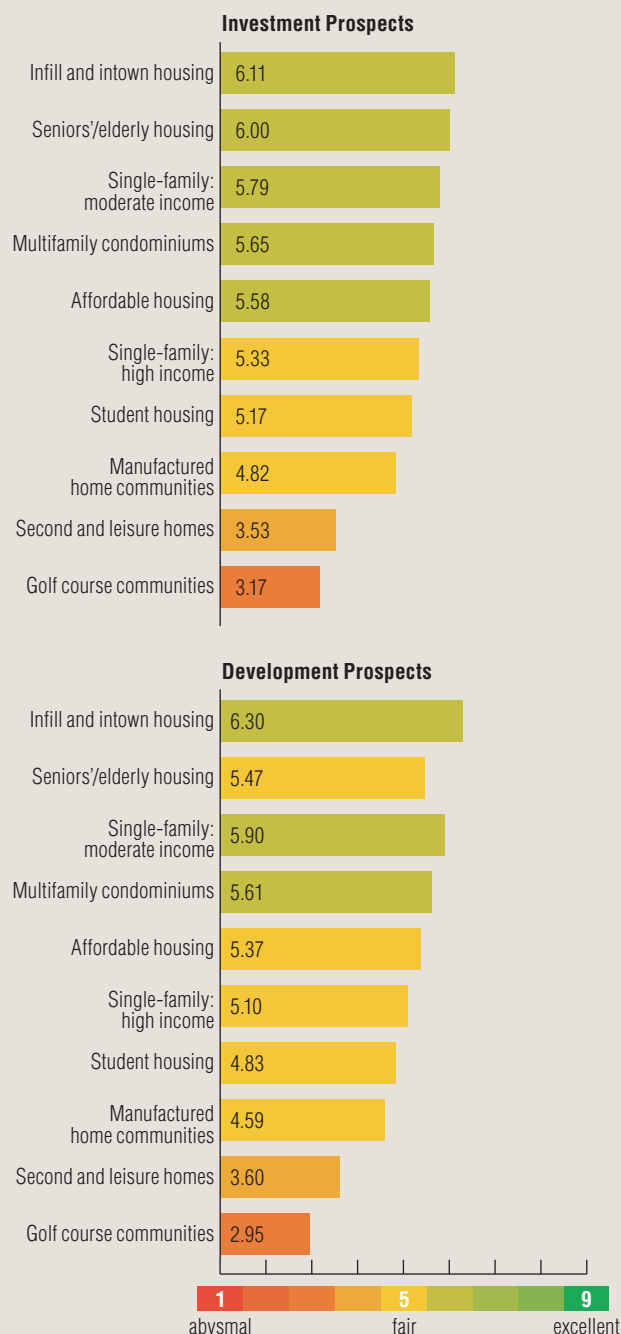
EXHIBIT 5-30

Hotels—Full Service

2013	Prospects	Rating	Ranking
Investment prospects	5.67	Modestly good	7th
Development prospects	3.67	Modestly poor	10th
Hold 66.7%			Sell 33.3%
Expected capitalization rate, December 2013		6.3%	

Source: *Emerging Trends in Real Estate 2013* survey.
Note: Based on Canadian respondents only.

EXHIBIT 5-31

Prospects for Residential Property Types in 2013Source: *Emerging Trends in Real Estate 2013* survey.

Note: Based on Canadian respondents only.

Best Bets

Hold Core Real Estate in Major Markets. For institutions, only five or six cities—"the traditional suspects"—offer opportunities to place money, and they happily dominate these markets, enjoying consistent payoffs from solid income-producing trophy properties across all property categories.

Develop Green Office in Downtowns. Major tenants want this more efficient space and will move from older buildings into layouts with operating-system advantages.

Land Bank in Western Markets. In Canada, the beckoning of "go west, young man" (and women, too) still applies, and opportunities for real estate investors and developers to take advantage of escalating inflows of workers for available jobs will continue, with an obvious caveat to unexpected reversals in energy and commodity markets. Buy and hold sites in and around the larger cities should see values escalate nicely, and infill sites will score development projects more quickly.

Secure Infill Sites. Any low-rise inner-city real estate "has got intensification written all over it," especially if located anywhere near mass transit. "Go for the sure-shot redevelopment capital play."

Develop Housing Away from Urban Cores. Soaring condo pricing and family-unfriendly units create an opening for homebuilders to meet the underserved market for larger layouts, which can better accommodate children.

Buy Luxury Condos in the Dip. With urbanization baked into future demand, upscale space in the best downtown locations will reclaim any lost value quickly.



Emerging Trends in Latin America

These countries “cannot decouple”
from the rest of the world.

Latin American countries—led by Brazil, as well as Mexico, Colombia, Peru, and Chile—provide continuing opportunities for real estate developers and investors if they can manage to master local markets and find suitable local partners. Three key trends drive growth:

- **Favorable demographics.** Young populations should propel markets for the foreseeable future. “All these 20- to 30-year-olds entering the workforce are reminiscent of the leading edge of baby boomers in the U.S. after World War II,” and fuel a prodigious housing boom.
- **Diversifying economics.** Expanding middle-class populations also help broaden business activity beyond exports into service-based industries, which focus on domestic consumption.
- **Increasing access to capital.** Strengthened economic footings, firmer government credit ratings, and augmented foreign investments lead to development of more sophisticated financial systems and greater availability of mortgage capital, which foster increasing real estate investment.

But in 2013, enduring global recessionary impacts will continue to dampen previously outsized growth, lowering regional economic expansion from the mid- to high single digits to the mid- to low-single-digit range. These countries “cannot decouple” from the rest of the world “and they will not do as well.” Lagging transportation infrastructure also hampers development activity outside of major cities. “Roads are bad,” intercity rail is limited, and secondary airports are sketchy. “It’s hard to get from point A to point B, and that gums up the works.” As a result, capital tends to steer clear of “underserved” smaller markets, where pent-up demand and “micro-opportunities” exist.

In the near term, unmet housing demand and retail expansion will dominate the attention of real estate developers and

investors. Builders have no trouble finding buyers for apartments as an “exploding middle class” absorbs units. In turn, residents hunger to furnish homes and head to stores. The international shopping center industry “wakes up to the potential” and launches major retail development projects. Leading U.S. mall companies shut out of activity back home compete against or join forces with Brazilian and Chilean companies, who also export their project skills into neighboring nations. “Regional malls attract a lot of capital,” including from U.S. and Canadian pension funds that see they can capture “a low-volatility premium and outsized returns” on long-term holds, especially for well-located centers in Brazil and Mexico.

Lack of transparency, frustrating government “idiosyncrasies,” and a dose of underlying corruption can pose ongoing

EXHIBIT 6-1

2013 Latin America General Indicators

	Unemployment (%)	Inflation (%)
Argentina	10.3	6.3
Brazil	5.0	6.5
Chile	3.0	6.9
Colombia	3.1	10.5
Ecuador	4.5	6.2
Mexico	3.1	4.6
Peru	2.3	7.5
Uruguay	6.0	6.0
Venezuela	28.7	8.1

Sources: International Monetary Fund, *World Economic Outlook* database, April 2012; Moody's Economy.com.

challenges in some jurisdictions; that is why partnering with “reliable,” “well-connected” locals remains “essential” for foreign investors. But relative to bedraggled Western economies and other volatile emerging markets, many Latin American countries look downright dynamic. Some—Brazil in particular—hold potential for world leadership as the 21st century continues to unfold and they energetically leave third world vestiges behind them.

Brazil

South America’s powerhouse hits the brakes after a heady run. Commodity and natural resource exports to Europe and Asia slow, and the country settles into a more tepid growth mode, helped along by expanding domestic consumer spending and a relatively modest government debt load. Compared with many global alternatives, Brazil looks like “a safe haven,” and the country seems “easier to invest in than either India or China.” The few institutional-grade office and residential properties in site-constrained São Paulo and Rio de Janeiro have been “priced to perfection,” while all asset categories remain under-supplied across the country. “The consensus is 15 to 20 years of growth lie ahead.”

Offshore investors will continue to want exposure to this emerging market that may have already arrived. But to realize the pop of an emerging-market return, they will probably need to “move beyond Rio and São Paulo to 20 other cities with 1 million or more in population”; these places need everything from apartment buildings and tract housing to shopping centers and offices. “They can provide decent risk-adjusted returns,” if investors can get comfortable outside the familiar places. On the housing front, where a huge supply deficit exists at the middle- and lower-income levels, the government works with banks to encourage the availability of 30-year mortgage capital for buyers and provide development incentives. But commercial projects require “substantial equity”: capital markets have not evolved to provide much financing. That is where major international mall companies and offshore institutional capital can make inroads with Brazilian mall operators looking for funding. They can join forces to “go after the expanding consumer base as disposable incomes rise.” Logistics properties to support retail expansion “lease up immediately.” Virtually no Class A industrial space is available. “You build even in a halfway-decent location and they [tenants] will come.” Cap rates for office space in the top markets “can’t compress further,” and rents hit the stratosphere. “Tenants may start to push back” and seek alternative options in secondary locations where developers can find sites.

Meanwhile, the country focuses on completing construction for the World Cup in 2014 and the Summer Olympics in 2016.

“It won’t be perfect; a lot rides on getting it done.” New related infrastructure—roads, high-speed rail, and airports—should help support future economic growth.

Mexico

Drug-violence headlines “scare” away foreign capital. “Institutional investors won’t take a hard look at Mexico.” But fundamentals should continue to improve as long as the U.S. economy does not move sideways. Manufacturing led by the auto industry “makes a comeback,” boosting prospects for border cities especially. Internal capital from pension fund allocations helps pick up some of the financing slack, stabilizing property markets in the absence of outside investments. Because competitors have pulled out, remaining players can benefit from a “more open playing field.” The market is “not booming, but you can selectively find good projects.”

Mexico City, the country’s mainstay citadel, and other large cities appear “more insulated” from the gangster-related warfare. Developers move to fill a housing deficit—trying to meet the expanding middle-class demand for units with modern amenities, particularly security. “People move back from the suburbs into mid- and high-rise apartments that can provide a greater sense of safety.” Resort areas suffer “significant distress” from a glut of second homes. The one-two punch of tapped-out U.S. buyers and constant news of drug-cartel mayhem turns off demand despite low prices for choice locations. “Every master-planned resort on the Mexican coast still has hair on it, and it may take a long time to turn around.”

Institutional-quality office space remains in short supply, whereas industrial space is overbuilt in many areas. Retail property presents considerable opportunity: many markets lack small to medium-sized shopping centers.

Other Countries

Colombia is a “coming attraction” and positions itself as the next Brazil with a boost from a new U.S. trade agreement. The country has “come a long way” since its drug-war days. More institutional investors make trips to Bogotá to check out the landscape, discovering a severe housing and office shortage, which hearkens back to Brazil a decade ago, with many of the same compelling demographic drivers in place. Although some interviewees point to “a better business climate than Brazil”—the government is less bureaucratic and labor laws are less demanding—others say “it’s hard to break in,” and there are still relatively few opportunities and “not as many available partners.”

Peru looks like another “up-and-comer,” with recent economic growth topping 6 percent. “The middle class increases [in size], and that fuels real estate opportunities.” An undercur-

EXHIBIT 6-2

Latin America Economic Growth

Percentage real GDP growth									
	2007	2008	2009	2010	2011*	2012*	2013*	2014*	2015*
Argentina	8.7	6.8	0.8	9.2	8.9	4.2	4.0	4.2	4.3
Brazil	5.7	5.1	-0.6	7.5	2.7	3.0	4.2	4.0	4.1
Chile	4.7	3.7	-1.7	6.1	5.9	4.3	4.5	4.5	4.5
Colombia	7.5	2.4	1.5	4.0	5.9	4.7	4.4	4.5	4.5
Ecuador	2.5	7.2	0.4	3.6	7.8	4.5	3.9	3.7	3.5
Mexico	3.3	1.5	-6.1	5.5	4.0	3.6	3.7	3.8	3.3
Peru	8.9	9.8	0.9	8.8	6.9	5.5	6.0	6.0	6.0
Uruguay	7.6	8.5	2.6	8.9	5.7	3.5	4.0	4.0	4.0
Venezuela	8.4	4.8	-3.3	-1.5	4.2	4.7	3.2	3.1	3.2

Sources: International Monetary Fund, *World Economic Outlook* database, April 2011.
* Projections.

rent of “political uncertainty” and lingering “banana republic feel” deter many investors for now. They take the safer route to Rio or São Paulo, not Lima.

Argentina struggles to attract interest, caught in Brazil’s shadow. Investors fret about a lack of political and monetary stability. Institutional investors generally steer clear: the country registers a bad rap for inflation, hostility to business, currency controls, and difficulty in taking money out. “Buenos Aires needs everything new. They have trouble maintaining old buildings,” but financing any deal proves difficult.

Foreign investors find **Chile** difficult to penetrate and “not worth the effort.” It’s a relatively small market with most real estate held by locals—long-term owners interested in capturing traditional income-oriented core returns. Offshore players seeking emerging market-style payoffs must look elsewhere.

Appendix A: Economy

2013	MSA	2013 Population		Echo Boomers (25-34)		2013 GMP per Capita			2013 Jobs			Unemployment		% Employment – Key Industries					Job Types Changes Peak to 2013			
Rank		Total (Million)	Change	% of Total Population	10-yr Growth	2013 GMP per Capita	10-year Avg Change	Industrial Diversity	2013 Change	10-year Avg Chg	Chg Since 2007	2013	10-Year Avg	Bus. & Pro. Svcs.	Educ. & Health	Energy	Const.	Goods Prod.	Service Jobs	Gov't		
	U.S.	314.2	1.0%	13.6%	9.7%			1.00	1.1%	0.2%	(2,998,495)	8.4%	6.5%	13.6%	15.5%	0.6%	4.1%	-18.7%	1.7%	-2.6%		
16	Los Angeles, CA*	13.2	1.0%	15.2%	1.5%	1.2%	1.6%	0.55	0.3%	-0.4%	(141,144)	9.7%	7.2%	15.4%	13.6%	0.1%	3.1%	-31.0%	-2.0%	-9.2%		
2	New York, NY	11.8	0.6%	16.5%	8.1%	1.1%	1.9%	0.62	1.2%	0.5%	13,432	8.5%	6.7%	16.0%	19.8%	0.0%	3.0%	-32.1%	2.0%	-5.8%		
24	Chicago, IL	9.6	0.6%	14.5%	2.9%	-0.3%	0.9%	0.81	-0.4%	-0.3%	(195,405)	9.7%	7.0%	16.8%	15.6%	0.0%	2.7%	-31.8%	-1.1%	-3.7%		
9	Dallas/Fort Worth, TX	6.8	2.1%	14.9%	13.6%	3.0%	3.1%	0.81	2.3%	1.0%	235,934	7.2%	6.1%	15.4%	12.6%	0.4%	4.9%	-15.1%	2.3%	2.1%		
5	Houston, TX	6.3	2.0%	15.2%	21.3%	2.2%	3.1%	0.61	2.3%	1.6%	309,508	7.5%	6.1%	14.3%	12.8%	3.6%	6.4%	-1.7%	2.3%	0.6%		
27	Philadelphia, PA	6.0	0.4%	13.4%	8.0%	0.2%	1.2%	0.75	0.6%	-0.1%	(62,195)	8.4%	5.9%	15.7%	21.5%	0.2%	3.3%	-30.1%	1.3%	-5.2%		
8	Washington, DC	5.9	1.2%	15.9%	19.2%	1.0%	2.9%	0.45	0.5%	1.1%	190,939	5.7%	4.2%	22.8%	12.8%	0.1%	4.7%	-21.8%	0.7%	0.4%		
12	Miami, FL	5.8	1.3%	13.1%	9.1%	1.1%	1.3%	0.63	0.2%	0.2%	(62,781)	9.3%	6.5%	15.4%	16.1%	0.0%	3.3%	-42.6%	-1.9%	-5.7%		
35	Atlanta, GA	5.5	1.4%	14.3%	5.7%	2.9%	1.6%	0.81	2.1%	0.4%	(66,282)	9.2%	6.2%	18.0%	12.7%	0.1%	3.7%	-26.6%	1.7%	-5.4%		
6	Boston, MA	4.6	0.6%	14.2%	7.2%	1.7%	2.0%	0.65	1.0%	0.1%	(1,101)	7.0%	5.4%	17.6%	20.2%	0.1%	3.1%	-31.1%	1.6%	-2.3%		
1	San Francisco, CA	4.5	0.9%	15.5%	7.6%	1.7%	1.3%	0.60	0.4%	-0.5%	48,248	8.4%	6.4%	19.3%	13.4%	0.1%	4.0%	-30.5%	-2.4%	-8.9%		
33	Phoenix, AZ	4.4	2.7%	14.2%	13.7%	2.7%	2.5%	0.79	1.6%	1.0%	(47,825)	8.0%	5.8%	16.4%	15.0%	0.2%	4.9%	-33.8%	-0.5%	-8.2%		
36	Inland Empire, CA	4.4	1.2%	14.2%	9.4%	1.7%	2.2%	0.80	1.0%	0.8%	(41,239)	12.7%	8.1%	12.0%	12.6%	0.1%	4.7%	-41.1%	-2.6%	-6.3%		
51	Detroit, MI	4.3	0.0%	12.0%	-12.6%	0.4%	-1.1%	0.55	0.4%	-1.4%	(182,707)	11.2%	8.8%	18.7%	16.4%	0.1%	3.1%	-40.7%	-5.2%	-21.1%		
Quartile 1 & 2 Avgs		6.7	1.1%	14.5%	8.2%	1.5%	1.7%	0.67	1.0%	0.3%	(187)	8.8%	6.5%	16.7%	15.4%	0.4%	3.9%	-29.3%	-0.3%	-5.6%		
7	Seattle, WA	3.6	1.2%	15.9%	20.2%	2.7%	2.6%	0.39	1.2%	0.7%	31,917	8.3%	6.4%	14.1%	13.1%	0.0%	4.7%	-11.7%	1.0%	-0.4%		
23	Minneapolis, MN	3.4	1.1%	15.0%	13.5%	0.8%	1.4%	0.78	1.6%	0.1%	53,301	5.5%	5.1%	15.4%	16.9%	0.1%	2.8%	-23.9%	2.5%	-3.8%		
15	San Diego, CA	3.2	1.4%	15.8%	14.1%	1.3%	2.1%	0.64	0.9%	0.1%	40,863	9.0%	6.2%	17.5%	12.6%	0.0%	4.3%	-23.9%	-0.1%	-2.1%		
10	Orange County, CA	3.1	1.1%	14.7%	20.1%	1.0%	2.1%	0.67	0.8%	-0.1%	(19,470)	7.6%	5.6%	18.4%	11.7%	0.0%	4.5%	-23.2%	-2.6%	-9.7%		
29	Tampa, FL	2.9	1.3%	12.5%	13.3%	1.3%	1.2%	0.86	0.4%	0.2%	(52,431)	10.1%	6.5%	17.1%	16.7%	0.0%	4.0%	-38.5%	-2.6%	0.7%		
43	St. Louis, MO	2.9	0.4%	13.4%	8.7%	0.1%	0.6%	0.86	0.0%	-0.3%	(29,413)	8.6%	6.6%	15.3%	18.1%	0.1%	4.2%	-31.0%	-0.1%	-5.1%		
31	Baltimore, MD	2.8	0.6%	14.3%	16.3%	0.6%	2.3%	0.84	0.1%	0.4%	11,043	7.7%	5.3%	15.3%	20.0%	0.1%	5.2%	-21.8%	0.7%	0.5%		
14	Denver, CO	2.7	1.2%	15.6%	14.2%	1.3%	1.7%	0.83	1.3%	0.6%	1,666	8.7%	6.0%	17.6%	12.7%	0.4%	5.6%	-21.3%	1.7%	-0.8%		
30	Pittsburgh, PA	2.4	-0.1%	12.2%	5.8%	0.8%	1.2%	0.78	0.7%	0.1%	(47,825)	8.0%	5.8%	14.6%	21.8%	0.8%	3.9%	-22.8%	2.0%	-5.3%		
20	Portland, OR	2.3	1.8%	15.2%	14.5%	1.7%	6.5%	0.68	0.9%	0.6%	36,051	9.1%	7.4%	13.6%	14.8%	0.1%	4.7%	-14.6%	0.4%	-0.1%		
19	San Antonio, TX	2.3	2.0%	14.1%	23.3%	2.6%	2.9%	0.82	2.5%	1.4%	92,672	7.3%	5.6%	11.6%	15.6%	0.4%	5.1%	-5.4%	2.6%	1.0%		
28	Orlando, FL	2.3	2.2%	14.4%	18.5%	2.3%	2.9%	0.30	1.4%	1.3%	(20,893)	9.7%	6.2%	15.3%	12.3%	0.0%	4.1%	-41.2%	-0.4%	0.8%		
Quartile 3 Avgs		2.8	1.2%	14.4%	15.2%	1.4%	2.3%	0.70	1.0%	0.4%	8,123	8.3%	6.0%	15.5%	15.5%	0.2%	4.4%	-23.3%	0.4%	-2.0%		
49	Sacramento, CA	2.2	1.3%	13.9%	14.0%	0.7%	1.2%	0.68	0.7%	-0.3%	(27,553)	10.3%	7.2%	12.9%	13.5%	0.1%	4.0%	-38.7%	-6.2%	-6.2%		
13	Northern New Jersey	2.2	0.3%	12.3%	-1.0%	1.5%	0.6%	0.74	0.6%	-0.5%	(27,493)	9.4%	6.1%	17.2%	15.4%	0.1%	3.2%	-33.8%	-0.9%	-5.8%		
38	Cincinnati, OH	2.2	0.5%	13.1%	3.3%	-0.5%	0.5%	0.83	0.4%	0.0%	(31,444)	8.5%	6.2%	15.7%	15.1%	0.1%	3.4%	-19.9%	-0.1%	-6.0%		
34	Kansas City, MO	2.1	1.0%	14.2%	10.9%	0.3%	1.3%	0.86	0.4%	0.3%	16,875	7.2%	6.3%	16.0%	13.8%	0.1%	3.0%	-21.9%	1.2%	-2.7%		
50	Las Vegas, NV	2.1	2.5%	14.8%	17.1%	2.3%	3.0%	0.23	2.7%	1.2%	13,637	12.4%	7.4%	12.1%	9.0%	0.0%	4.4%	-59.4%	-2.4%	-9.1%		
48	Cleveland, OH	2.1	-0.3%	11.9%	-4.2%	-1.4%	-0.2%	0.77	0.0%	-0.8%	(21,312)	8.1%	6.5%	13.4%	19.6%	0.1%	2.9%	-30.1%	-3.6%	-12.5%		
25	Westchester/Fairfield	2.0	0.4%	N/A	N/A	2.5%	1.5%	N/A	1.2%	0.0%	N/A	N/A	N/A	14.9%	19.2%	0.0%	3.8%	N/A	N/A	N/A		
3	San Jose, CA	1.9	0.9%	15.4%	5.0%	3.1%	4.4%	0.23	1.2%	-0.1%	43,598	9.0%	7.4%	19.6%	13.7%	0.0%	3.8%	-31.9%	1.6%	-12.5%		
40	Columbus, OH	1.9	0.8%	15.0%	6.2%	0.1%	0.6%	0.75	0.8%	0.2%	4,168	7.5%	5.8%	16.5%	15.2%	0.1%	2.6%	-33.2%	1.6%	-4.8%		
4	Austin, TX	1.9	2.7%	17.1%	25.7%	5.3%	4.7%	0.68	3.2%	2.2%	111,734	6.5%	5.3%	15.1%	11.7%	0.2%	4.8%	-19.7%	3.3%	3.2%		
17	Charlotte, NC	1.9	2.3%	14.3%	15.4%	2.9%	2.2%	0.77	1.4%	0.8%	29,970	10.1%	7.1%	17.0%	10.6%	0.1%	4.4%	-31.6%	1.9%	-1.6%		
37	Indianapolis, IN	1.8	1.4%	14.2%	9.4%	1.2%	1.8%	0.80	0.8%	0.4%	(7,973)	7.4%	5.6%	15.2%	14.8%	0.1%	4.9%	-18.2%	1.0%	-0.6%		
11	Raleigh/Durham, NC	1.8	2.8%	13.9%	20.2%	2.7%	4.3%	0.76	1.7%	1.5%	61,301	15.3%	11.1%	16.1%	16.0%	0.2%	4.2%	-22.9%	2.3%	-3.7%		
26	Virginia Beach, VA	1.7	0.5%	14.7%	12.0%	1.1%	1.5%	0.37	0.7%	0.1%	23,512	6.6%	4.7%	13.3%	13.7%	0.1%	4.4%	-22.6%	-1.8%	0.1%		
18	Nashville, TN	1.7	1.4%	14.8%	16.5%	1.7%	2.7%	0.80	1.3%	1.0%	40,514	7.6%	5.6%	14.9%	16.1%	0.1%	4.2%	-19.6%	1.4%	-1.5%		
46	Providence, RI	1.6	0.3%	12.3%	-3.2%	0.5%	0.8%	0.76	0.4%	-0.5%	(60,594)	11.8%	7.1%	11.0%	21.8%	0.1%	3.0%	-37.6%	-2.8%	-6.5%		
41	Milwaukee, WI	1.6	0.3%	13.7%	7.5%	1.5%	1.1%	0.67	0.2%	-0.3%	(21,730)	7.6%	6.1%	13.8%	18.6%	0.0%	3.1%	-23.5%	-2.6%	-6.5%		
39	Jacksonville, FL	1.4	1.3%	13.8%	15.0%	0.1%	1.5%	0.79	0.6%	0.6%	(5,762)	9.0%	6.0%	16.0%	15.1%	0.0%	3.9%	-39.9%	-0.7%	-2.0%		
45	Memphis, TN	1.3	0.8%	13.6%	4.0%	1.2%	1.2%	0.55	0.7%	-0.2%	(1,957)	9.7%	6.9%	14.0%	14.5%	0.1%	3.5%	-22.8%	-3.9%	-2.6%		
32	Oklahoma City, OK	1.3	1.2%	14.7%	20.1%	1.6%	2.3%	0.73	1.3%	0.8%	18,809	5.9%	4.8%	13.6%	13.4%	3.3%	4.2%	-2.6%	1.6%	-1.2%		
47	New Orleans, LA	1.2	0.3%	14.6%	-4.5%	1.1%	0.4%	0.62	0.3%	-1.2%	16,908	7.9%	5.6%	13.3%	14.9%	1.3%	5.1%	-24.2%	-10.0%	-21.3%		
21	Salt Lake City, UT	1.2	1.5%	16.1%	11.0%	2.4%	3.5%	0.73	0.9%	1.3%	(5,475)	6.1%	5.1%	16.3%	10.7%	0.3%	6.4%	-7.0%	1.4%	-0.2%		
44	Tucson, AZ	1.0	2.2%	12.9%	11.0%	1.9%	1.8%	0.63	1.7%	0.5%	842	8.4%	5.9%	13.4%	16.1%	0.5%	5.1%	-19.2%	-1.8%	-7.2%		
22	Honolulu, HI	1.0	0.7%	14.9%	14.9%	0.7%	2.1%	0.47	1.2%	0.7%	14,226	5.8%	4.0%	13.8%	13.5%	0.1%	4.6%	-20.0%	-0.6%	0.4%		
42	Albuquerque, NM	0.9	1.1%	14.1%	20.2%	2.0%	2.5%	0.68	1.5%	0.3%	(16,780)	8.4%	5.5%	15.3%	15.9%	0.1%	4.9%	-31.7%	-2.4%	-2.4%		
Quartile 4 Avgs		1.7	1.1%	14.2%	10.3%	1.5%	1.9%	0.66	1.0%	0.3%	7,005	9.1%	6.6%	14.8%	14.9%	0.3%	4.1%	-26.3%	-0.9%	-4.7%		

Sources: PwC, Moody's Analytics, Bureau of Economic Analysis, U.S. Census Bureau.

Notes: Quartiles based on MSA total population. * Quartile 1 (Los Angeles) combined with quartile 2. 2013 calculations based on forecasts acquired September 2012.

Appendix B: Housing

2013 Rank	MSA	Households		Median Home Prices			2013 Single-Family Homes Changes			Rent/ Home	State System		Foreclosures			Apt. Vacancy		Apt. Completions	
		2013 Total	Change	Prices	2013 Change	From Peak	Starts	Completions	Sales	2013 Ratio	Judicial	Non-Judicial	Process Time (Days)	Rate	90+ Days Delinquent	2013	10-year Avg	2013 Comp/ Inv.	10-yr Avg Comp/ Inv.
	U.S.	41,639.0	0.9%	\$416,390.00	0.9%	0.9%	0.9%	0.9%	0.9%	1.59						4.2%	6.4%	0.6%	1.1%
2	New York, NY*	4,397.7	0.5%	\$437.3	0.6%	-18.6%	17.7%	5.7%	19.2%	1.75	*		445	8.2%	3.5%	1.8%	2.7%	2.3%	1.2%
16	Los Angeles, CA	4,389.8	1.2%	\$349.0	-0.2%	-41.1%	27.0%	13.5%	21.0%	1.04	*	*	117	4.8%	3.6%	3.1%	3.9%	0.7%	0.4%
24	Chicago, IL	3,545.6	0.6%	\$179.1	0.7%	-34.5%	39.5%	4.1%	11.2%	1.55	*		300	9.1%	3.4%	3.6%	5.4%	1.1%	0.3%
9	Dallas/Fort Worth, TX	2,474.7	2.2%	\$152.1	-0.8%	-0.8%	39.0%	29.9%	14.0%	1.43	*	*	27	3.6%	3.2%	5.2%	8.2%	1.8%	1.1%
27	Philadelphia, PA	2,290.6	0.5%	\$212.3	1.0%	-9.0%	45.4%	15.3%	25.6%	1.27			270	6.0%	3.7%	3.5%	4.6%	1.2%	1.1%
5	Houston, TX	2,223.0	2.1%	\$165.5	0.1%	0.1%	18.9%	17.0%	10.3%	1.24	*	*	27	3.2%	2.9%	6.8%	9.1%	1.3%	1.2%
8	Washington, DC	2,171.5	1.3%	\$326.5	-2.1%	-24.2%	32.5%	14.3%	21.3%	1.16		*	47	3.5%	3.5%	3.9%	4.6%	3.3%	0.7%
12	Miami, FL	2,167.4	1.3%	\$179.5	-4.1%	-52.1%	31.0%	-8.7%	8.5%	1.56	*		135	18.7%	4.3%	3.4%	4.8%	0.5%	1.1%
35	Atlanta, GA	2,040.9	1.8%	\$92.4	-0.6%	-46.0%	72.8%	56.4%	8.9%	2.33	*	*	37	5.4%	4.9%	6.1%	9.1%	1.1%	0.4%
6	Boston, MA	1,807.5	0.9%	\$337.1	-0.3%	-17.4%	42.7%	13.7%	11.7%	1.33	*		75	3.6%	3.3%	3.4%	5.1%	2.1%	0.7%
51	Detroit, MI	1,693.5	0.3%	\$61.0	8.9%	-62.7%	34.3%	33.4%	37.6%	3.55		*	60	5.2%	4.6%	3.9%	6.6%	0.4%	0.2%
1	San Francisco, CA	1,682.5	1.1%	\$589.6	0.7%	-30.0%	28.2%	30.3%	22.1%	0.86	*	*	117	3.7%	2.6%	2.8%	4.2%	1.6%	0.4%
33	Phoenix, AZ	1,634.7	2.7%	\$129.5	-1.6%	-51.5%	42.8%	38.9%	-10.3%	1.53	*	*	90	5.8%	3.7%	5.6%	8.6%	1.2%	0.5%
Quartile 1 & 2 Avgs		\$2,501.5	1.3%	\$247.0	0.2%	-29.8%	36.3%	20.3%	15.5%	1.58			134	6.2%	3.6%	4.1%	5.9%	1.4%	0.7%
7	Seattle, WA	1,415.7	1.4%	\$291.4	2.8%	-24.3%	2.1%	4.9%	13.3%	0.94	*	*	135	3.5%	5.9%	4.4%	5.6%	3.3%	0.5%
36	Inland Empire, CA	1,367.2	1.6%	\$176.9	-1.6%	-55.9%	137.3%	136.8%	20.7%	1.53	*	*	117	6.5%	5.3%	4.7%	8.5%	1.7%	0.9%
23	Minneapolis, MN	1,339.6	1.5%	\$158.5	-1.2%	-31.8%	34.4%	29.4%	33.2%	1.61	*		95	3.3%	1.8%	2.6%	4.5%	1.3%	0.7%
29	Tampa, FL	1,191.2	1.2%	\$139.4	0.0%	-38.2%	31.7%	41.3%	4.4%	1.56	*		135	16.2%	3.8%	5.2%	7.2%	1.4%	0.7%
43	St. Louis, MO	1,158.4	0.9%	\$124.8	1.2%	-15.2%	15.0%	0.9%	16.3%	1.51	*	*	60	4.6%	3.2%	4.9%	7.5%	0.2%	0.4%
15	San Diego, CA	1,131.5	1.5%	\$371.4	-0.4%	-38.4%	55.7%	10.4%	23.4%	0.93	*	*	117	4.2%	3.2%	2.3%	3.8%	0.7%	0.6%
31	Baltimore, MD	1,062.1	0.9%	\$235.6	0.0%	-17.2%	26.1%	1.0%	15.8%	1.11	*		46	4.8%	5.0%	3.6%	4.9%	1.7%	0.9%
14	Denver, CO	1,060.1	1.5%	\$228.2	-2.1%	-8.6%	29.7%	18.4%	14.7%	1.05	*	*	145	4.0%	2.5%	3.8%	7.5%	1.7%	0.7%
10	Orange County, CA	1,028.7	1.2%	\$513.8	0.3%	-27.4%	48.3%	46.9%	33.1%	0.78	*	*	117	4.8%	3.6%	5.8%	8.4%	0.7%	0.6%
30	Pittsburgh, PA	1,008.1	0.3%	\$128.9	1.7%	1.7%	28.7%	-1.7%	19.2%	1.69	*		270	5.0%	2.7%	3.0%	5.6%	0.8%	0.8%
20	Portland, OR	927.1	2.0%	\$230.1	3.0%	-21.9%	26.4%	16.8%	18.8%	0.97	*	*	150	4.8%	3.0%	1.9%	5.0%	1.0%	0.8%
38	Cincinnati, OH	849.8	0.8%	\$125.6	0.1%	-13.5%	10.2%	-18.3%	16.4%	1.49	*		217	6.6%	3.3%	4.1%	7.4%	0.8%	1.0%
Quartile 3 Avgs		\$1,128.3	1.2%	\$227.1	0.3%	-24.2%	37.1%	23.6%	18.8%	1.26			134	5.7%	3.6%	3.9%	6.3%	1.3%	0.7%
25	Westchester/Fairfield	873.6	1.2%	\$873.6	1.2%	-2.3%	N/A	N/A	N/A	0.54	*		N/A	N/A	N/A	3.0%	4.0%	1.1%	0.7%
28	Orlando, FL	845.6	2.1%	\$124.0	-3.1%	-53.9%	21.7%	-0.2%	6.3%	1.83	*		135	15.7%	4.3%	5.2%	7.4%	1.9%	1.2%
48	Cleveland, OH	843.9	-0.3%	\$101.2	0.4%	-27.3%	-22.4%	-31.2%	16.2%	1.86	*		217	8.4%	4.3%	3.1%	6.0%	0.0%	0.3%
34	Kansas City, MO	834.3	1.4%	\$136.1	-0.4%	-12.3%	36.5%	3.8%	23.7%	1.34	*	*	60	4.3%	3.1%	4.7%	7.3%	0.9%	0.7%
19	San Antonio, TX	819.1	2.1%	\$161.0	0.0%	0.0%	45.0%	39.2%	10.3%	1.17	*	*	27	3.1%	2.8%	6.0%	7.5%	2.4%	1.4%
49	Sacramento, CA	818.2	1.2%	\$173.0	0.4%	-53.8%	84.6%	61.0%	23.2%	1.39	*	*	117	5.2%	3.9%	3.1%	5.6%	0.5%	0.7%
13	Northern New Jersey	777.7	0.1%	\$366.8	3.4%	-17.2%	39.6%	8.5%	22.7%	1.06	*		270	8.2%	3.5%	3.1%	4.0%	0.8%	0.6%
50	Las Vegas, NV	761.3	2.5%	\$115.4	-6.2%	-63.6%	12.3%	8.8%	15.9%	1.76	*	*	116	10.7%	8.4%	5.4%	6.8%	1.1%	1.1%
40	Columbus, OH	748.1	1.0%	\$129.6	-0.7%	-13.6%	31.9%	9.0%	18.1%	1.38	*		217	6.7%	3.6%	5.2%	7.9%	0.7%	0.7%
17	Charlotte, NC	727.1	2.5%	\$211.0	-0.3%	-0.3%	53.0%	34.0%	10.9%	1.00	*	*	110	5.1%	3.2%	3.4%	5.1%	2.1%	0.7%
4	Austin, TX	719.4	2.8%	\$205.7	-0.3%	-0.3%	24.3%	24.6%	13.1%	1.13	*	*	27	1.9%	1.9%	4.8%	7.7%	3.7%	1.5%
37	Indianapolis, IN	713.0	1.6%	\$124.7	-1.3%	-1.3%	25.9%	0.3%	13.4%	1.44	*	*	261	6.8%	3.2%	4.7%	8.5%	1.7%	0.9%
11	Raleigh/Durham, NC	689.3	2.7%	\$411.0	1.0%	0.5%	46.2%	42.8%	12.2%	0.52	*	*	110	3.7%	2.5%	3.2%	5.5%	1.0%	0.5%
18	Nashville, TN	653.7	1.7%	\$158.9	1.5%	-13.0%	36.1%	25.0%	18.3%	1.23	*	*	45	4.5%	3.5%	4.2%	6.5%	1.8%	0.8%
26	Virginia Beach, VA	644.3	0.8%	\$195.2	3.2%	-20.0%	44.8%	21.6%	15.8%	-	*	*	45	3.6%	3.1%	N/A	N/A	N/A	N/A
3	San Jose, CA	643.0	1.2%	\$583.7	0.4%	-30.2%	28.2%	40.7%	18.9%	0.72	*	*	117	3.5%	2.5%	2.8%	4.3%	2.0%	0.6%
41	Milwaukee, WI	633.3	0.7%	\$192.6	2.7%	-12.5%	-0.7%	-0.6%	19.8%	1.13	*	*	290	5.8%	3.2%	3.0%	4.8%	1.0%	0.4%
46	Providence, RI	625.8	0.0%	\$226.2	2.0%	-22.6%	40.7%	3.0%	3.5%	1.36	*	*	62	6.2%	4.6%	3.1%	6.0%	1.1%	0.7%
39	Jacksonville, FL	546.2	1.7%	\$123.0	3.0%	-36.1%	-0.3%	-21.5%	5.0%	1.66	*		135	12.5%	4.7%	7.4%	8.6%	0.9%	1.2%
32	Oklahoma City, OK	513.3	1.5%	\$148.2	1.8%	1.8%	6.5%	11.9%	17.6%	0.98	*	*	186	4.4%	2.5%	5.8%	8.4%	0.7%	0.6%
45	Memphis, TN	509.6	1.2%	\$117.1	1.5%	-17.6%	80.4%	85.1%	36.5%	1.51	*	*	40	8.6%	6.8%	7.8%	10.5%	1.0%	0.5%
47	New Orleans, LA	465.7	0.6%	\$158.1	0.5%	-8.3%	47.9%	38.1%	13.2%	1.41	*	*	180	5.9%	3.9%	6.4%	6.7%	1.2%	1.1%
44	Tucson, AZ	407.1	2.3%	\$146.1	2.3%	-40.3%	46.4%	27.4%	8.5%	1.17	*	*	90	4.6%	3.0%	4.2%	7.2%	0.3%	0.3%
21	Salt Lake City, UT	393.9	1.5%	\$198.8	4.3%	-14.2%	28.3%	28.9%	16.3%	0.98			142	4.9%	3.6%	3.8%	5.7%	2.8%	0.7%
42	Albuquerque, NM	358.4	1.1%	\$178.6	1.9%	-10.0%	-8.4%	-13.1%	19.1%	1.02	*		180	5.2%	2.3%	3.7%	5.7%	1.4%	0.7%
22	Honolulu, HI	321.9	1.2%	\$655.5	0.8%	0.8%	-6.8%	-15.3%	6.5%	-	*	*	220	5.1%	2.1%	N/A	N/A	N/A	N/A
Quartile 4 Avgs		\$649.5	1.4%	\$239.0	0.8%	-18.0%	26.4%	17.8%	15.3%	1.14			136	6.2%	3.6%	4.5%	6.6%	1.3%	0.8%

Sources: PwC, Moody's Analytics, Bureau of Economic Analysis, U.S. Census Bureau, RealtyTrac.

Notes: Quartiles based on MSA total population. * Quartile 1 (New York) combined with quartile 2. 2013 calculations based on forecasts acquired September 2012.

Interviewees

Abu Dhabi Investment Authority
Thomas R. Arnold

Ackman-Ziff Real Estate Group LLC
Gerald S. Cohen
Patrick Hanlon
Russell Schildkraut
Simon Ziff

AEW Capital Management
Richard Brace
Marc Davidson

AIMCO
Ernie Freedman

Allied Properties Real Estate Investment Trust
Michael Emory

The Alterra Group of Companies
Robert Cooper

Amacon Group
Bob Cabral
Patrick Uy

American Realty Advisors
Stanley Iezman

APG Asset Management US Inc.
Steve Hason

Apollo Global Management
Joseph Azrack

ARA Finance
Thomas MacManus

Armco Capital Inc.
George Armoyan
Rob MacPherson

The Armour Group Limited
Scott McCrea

Artemis Advisors, LLC
Dale Anne Reiss

ASB Real Estate Investments
Robert Bellinger

Aspac Developments Ltd.
Gary Wong

Aspen Properties Ltd.
Scott Hutcheson
Greg Guatto

AXA Equitable
Timothy Welch

Ayer Capital
V. Raja

Bank of America Merrill Lynch
Jeffrey D. Horowitz

Bank of Montreal
Greg Vriend

Barclays Capital
P. Sheridan Schechner
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Baruch College
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Basis Investment Group LLC
Mark K. Bhasin

Bay Hollow Associates
Alice Connell

Bentall Kennedy (Canada) LP
Paul Zemla

Bentall Kennedy (US) LLP
Chuck Burd
Douglas Poutasse

BioMed Realty Trust Inc.
Greg N. Lubushkin

Borden Ladner Gervais LLP
Mark Lewis

Boston Properties
Mike LaBelle

BPG Properties, Ltd.
Daniel M. DiLella Sr.
Arthur P. Pasquarella

Brandywine Realty Trust
George Hasenecz
Jerry Sweeney

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