TIMING IS EVERYTHING

INVESTING IN SECONDARY REAL ESTATE MARKETS

Thursday November 6 24 2014 Tulsa Trends Conference
National Association of Industrial and Office Properties

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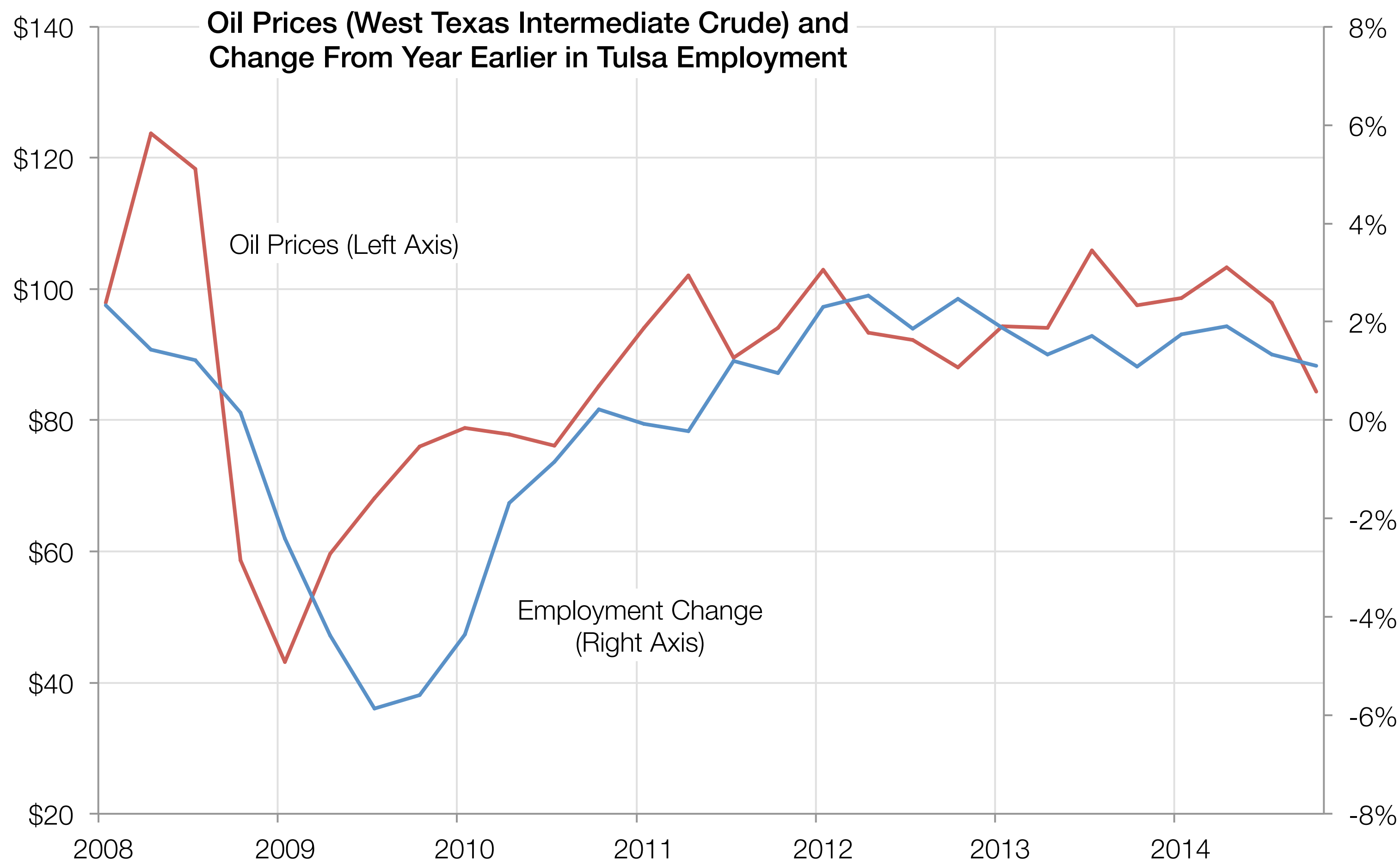
CHANDANECONOMICS

DISCLAIMER

ENERGY PRICES AND THE TULSA ECONOMY



Source: Federal Reserve, Energy Information Administration, Bureau of Labor Statistics

SECONDARY MARKET QUESTIONS FOR 2015

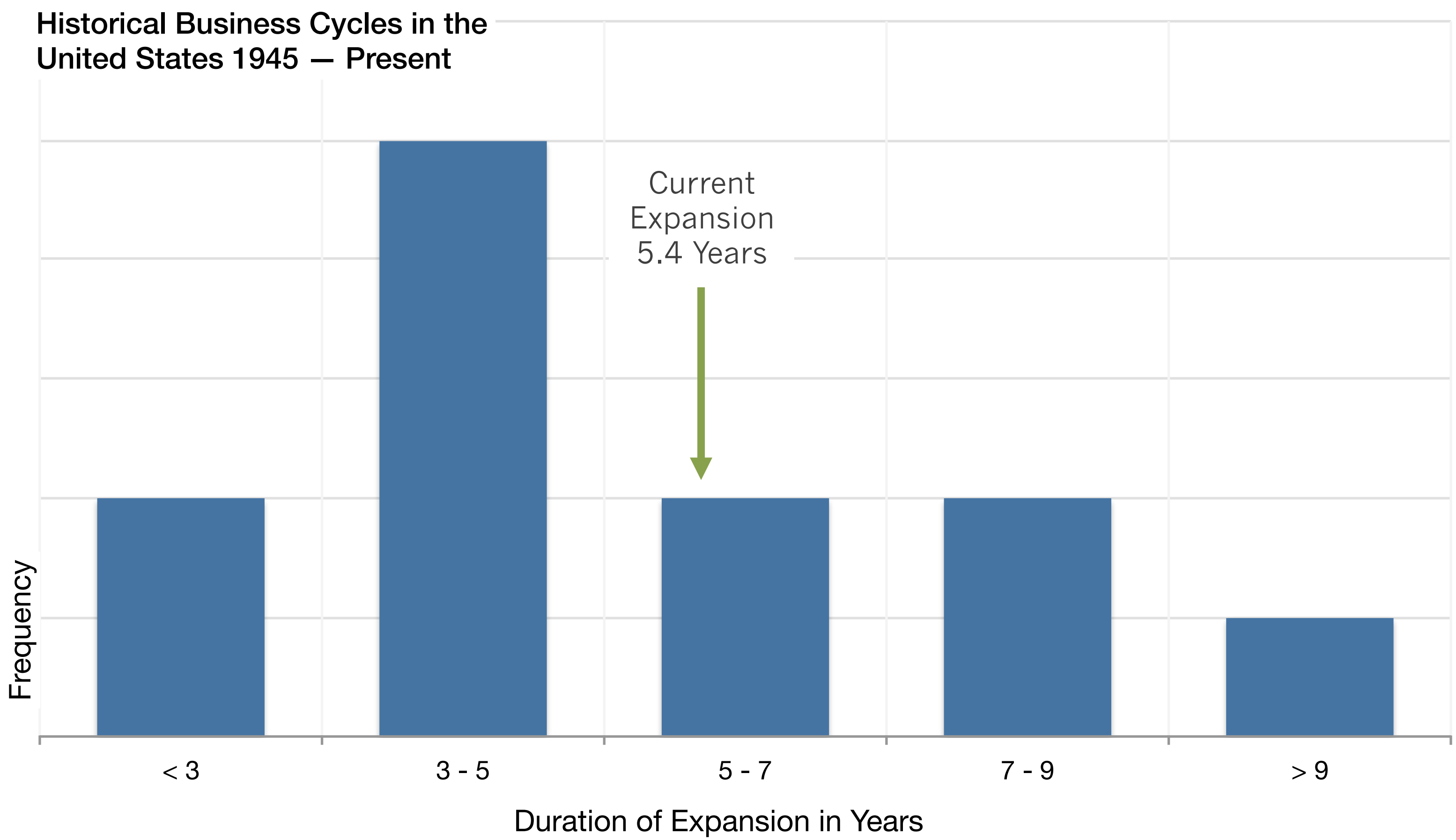
1 **LOCAL ECONOMIES** HEADWINDS OR TAILWINDS

2 **INTEREST RATES** ASKING THE WRONG QUESTION

3 **FUNDAMENTALS** BUILDING MOMENTUM

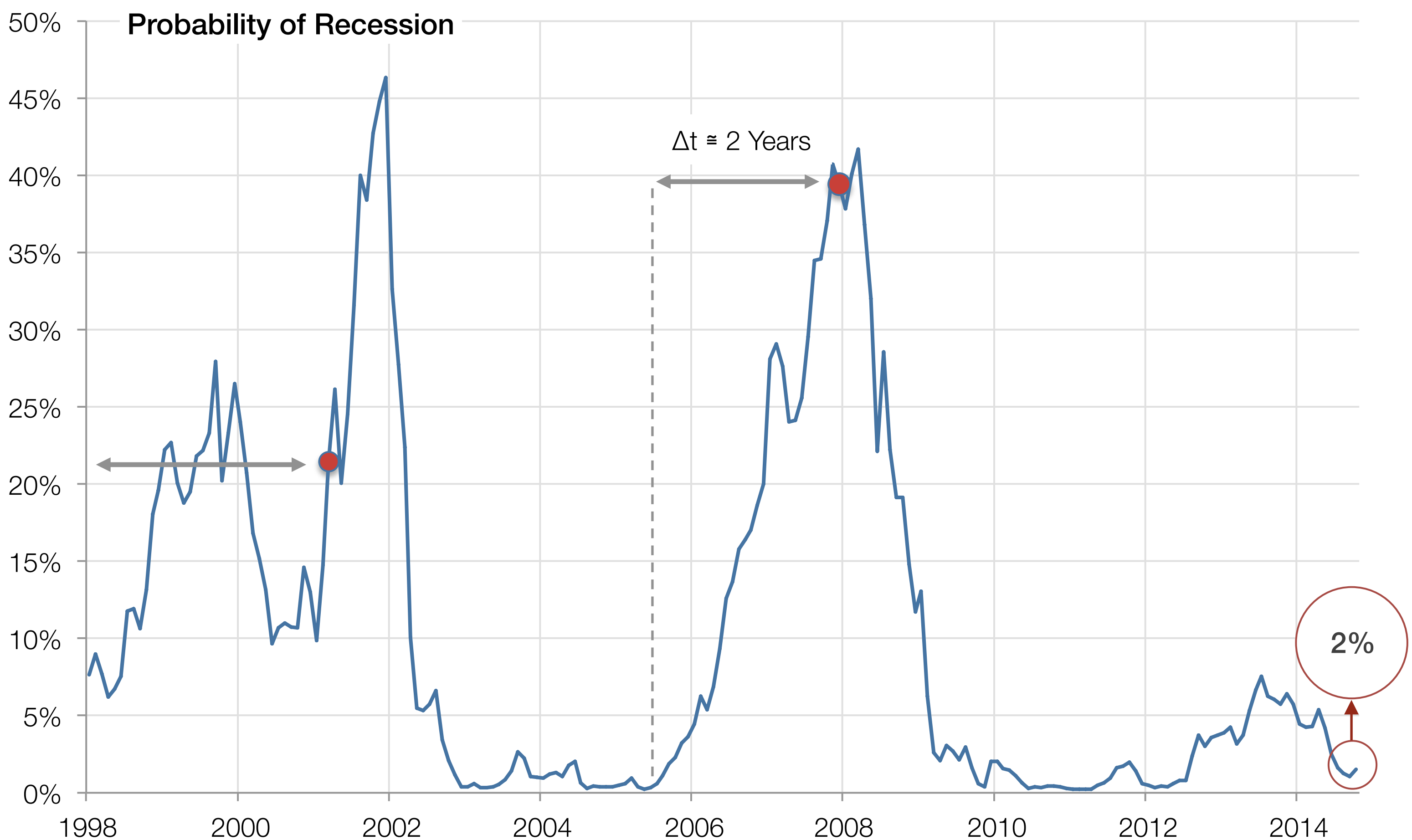
4 **CAPITAL** ARE WE PEAKING

ANTICIPATING THE BUSINESS CYCLE



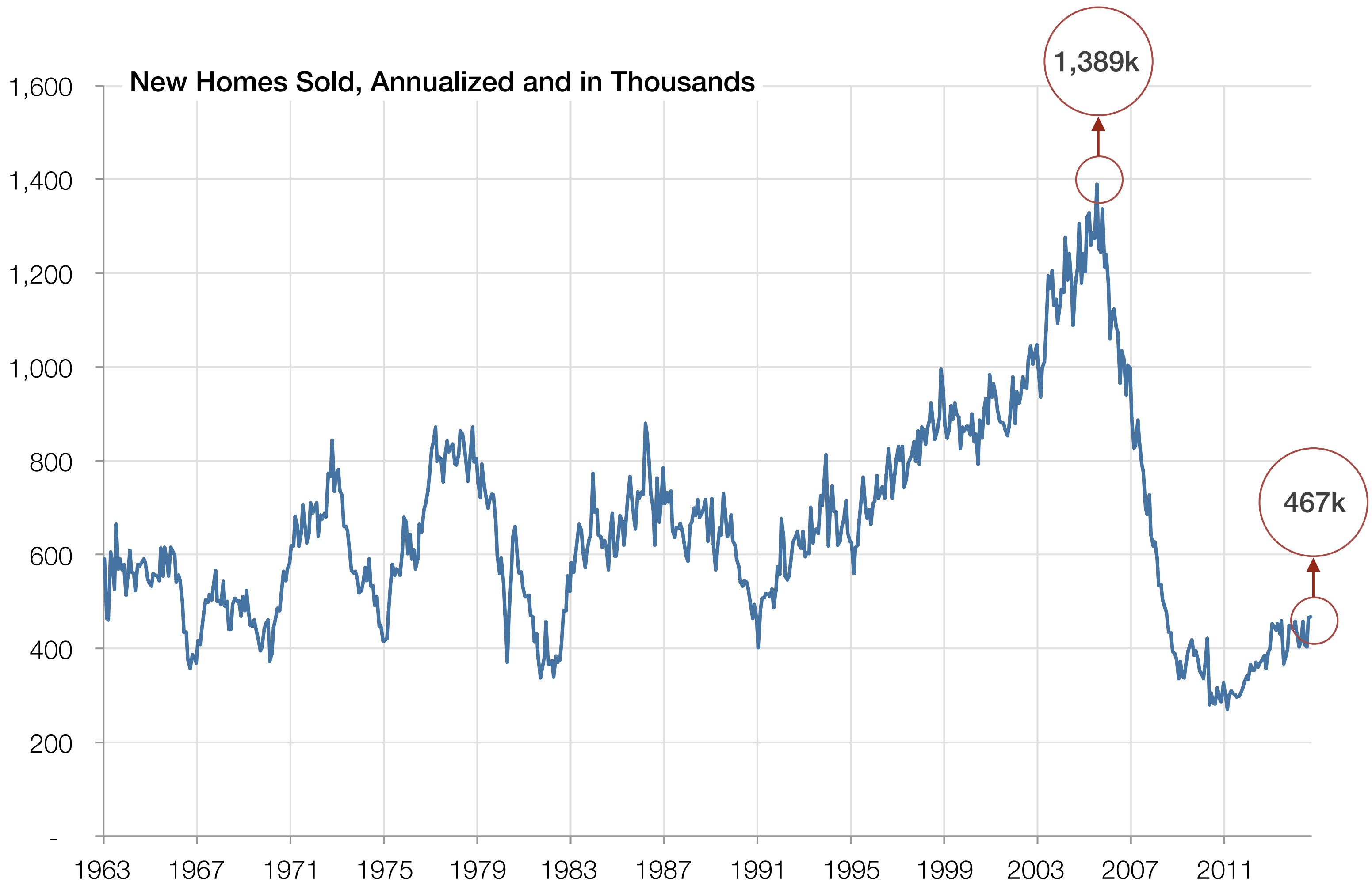
Source: Chandan Economics; National Bureau of Economic Research

THE BUSINESS CYCLE



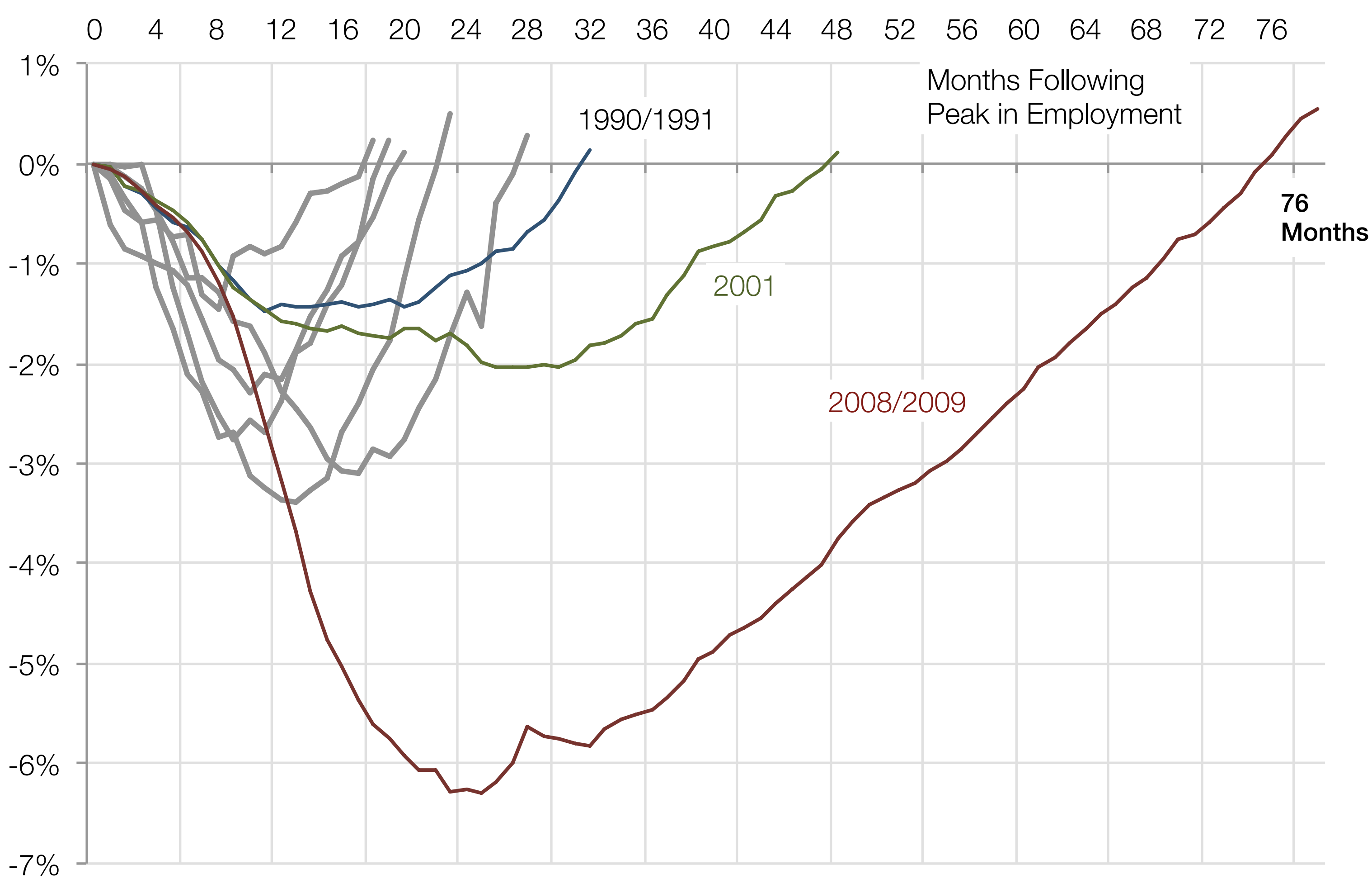
Source: Federal Reserve Bank of New York

THE ECONOMY AND HOUSING



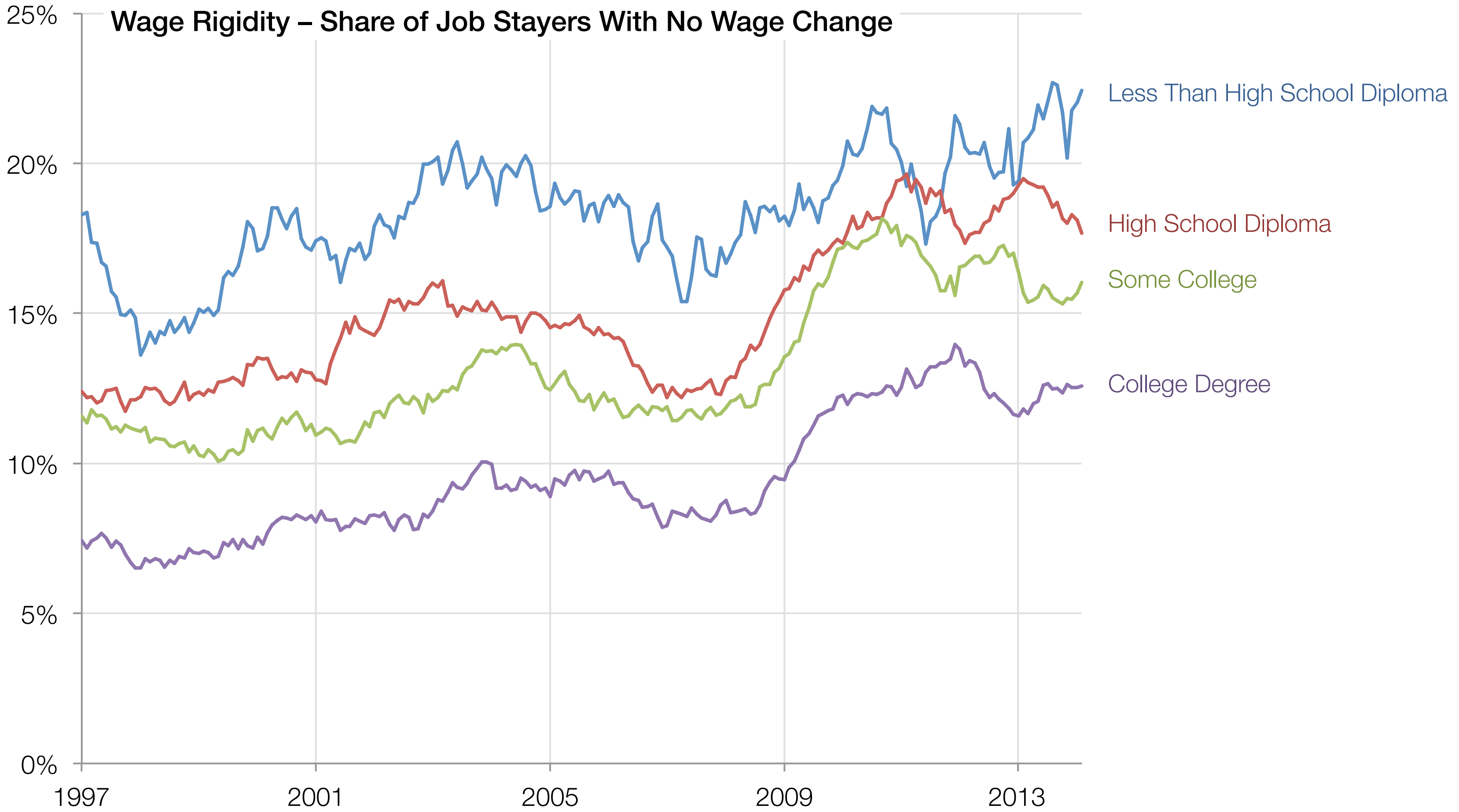
Source: Commerce Department

LABOR MARKET



Source: Chandan Economics; Bureau of the Labor Statistics

LABOR MARKET



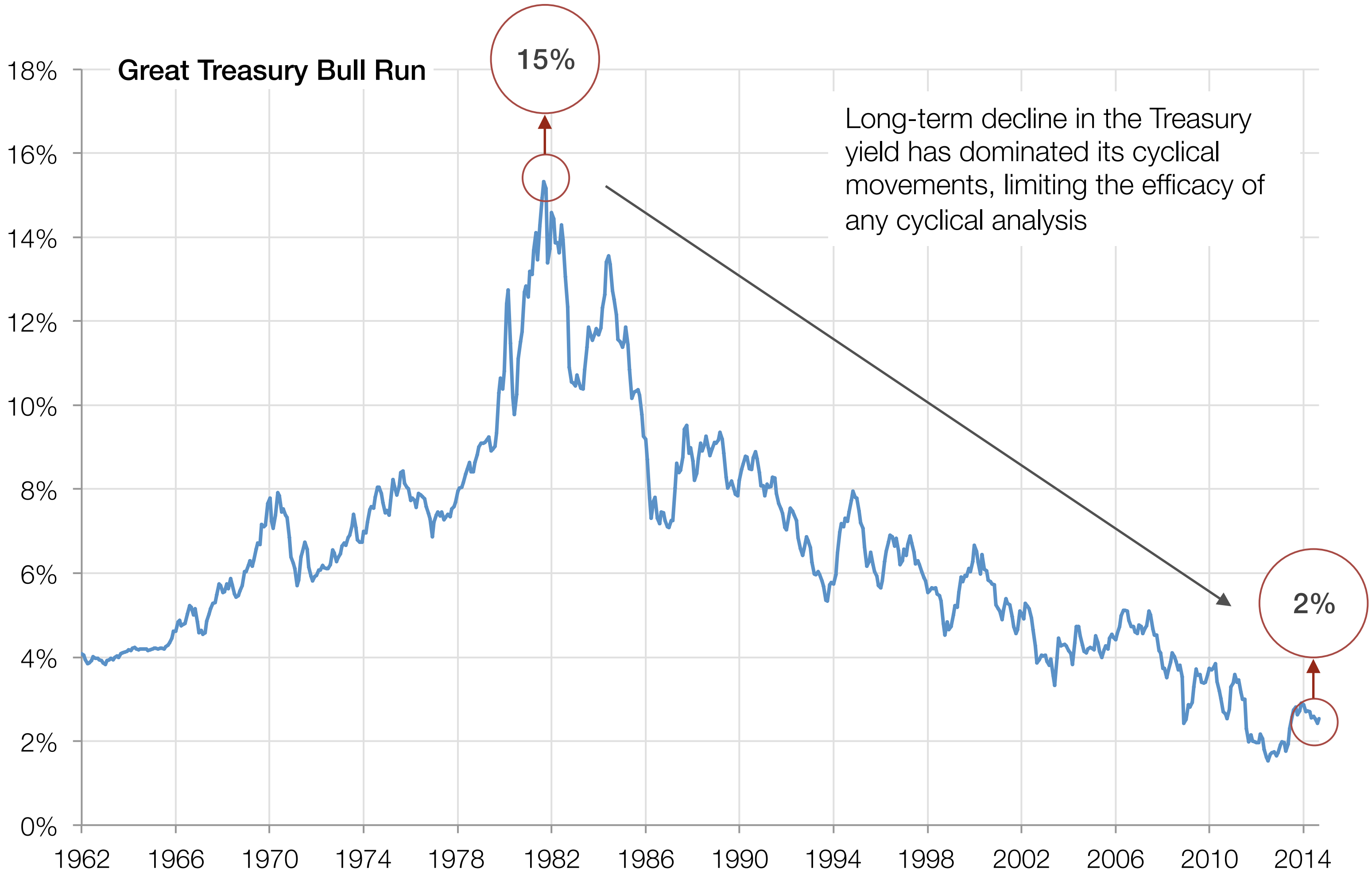
Source: Federal Reserve Bank of San Francisco

SIX KEY OBSERVATIONS

Asset Markets

1. Investor and lender density are important differentiators for primary and secondary markets
2. Secondary markets' risk-reward tradeoff is not always efficient
3. Flexibility in timing acquisitions and dispositions is critical in secondary market returns; buy early, buy long, or have an uncanny sense of timing

INTEREST RATES



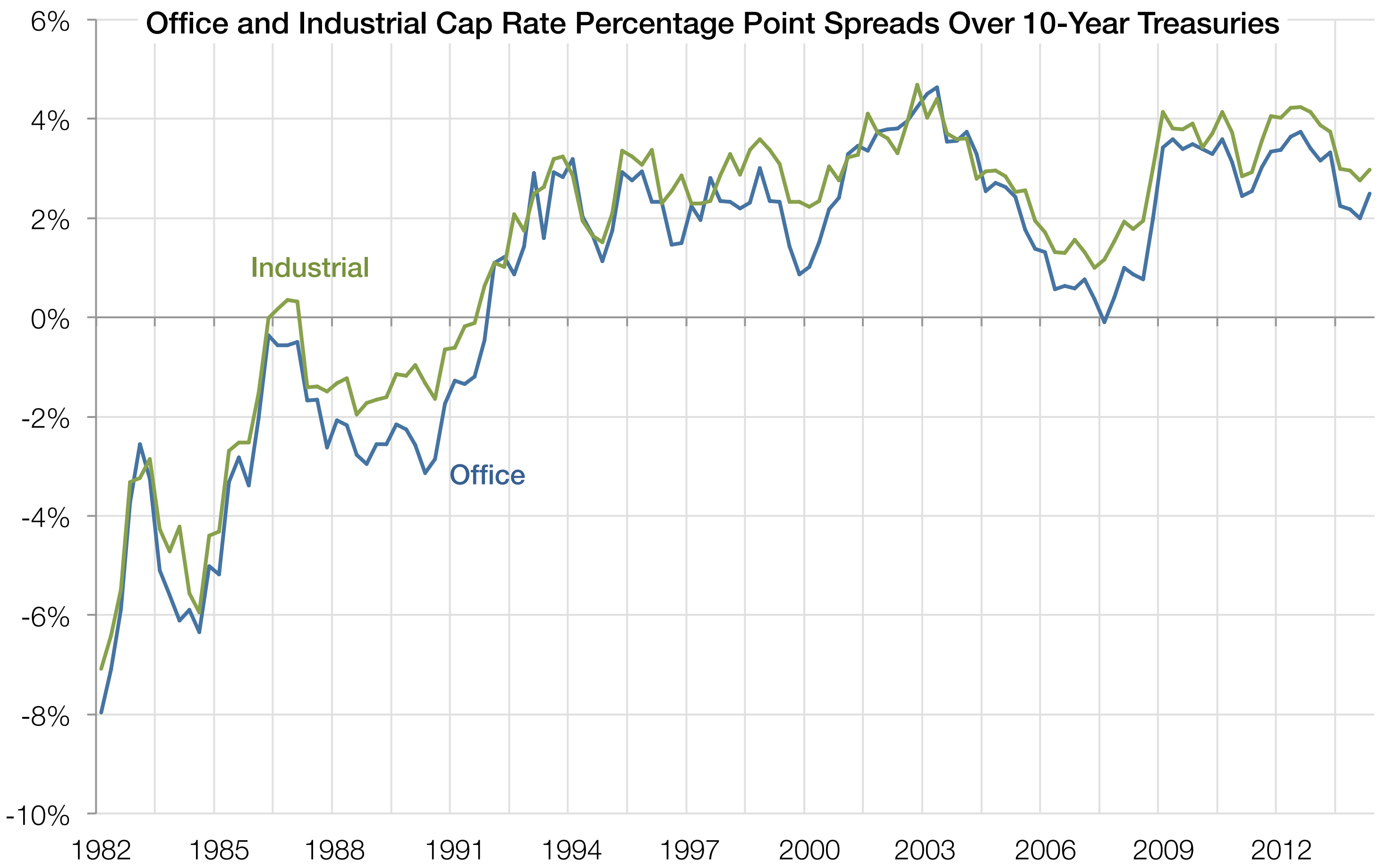
INTEREST RATES

The right question for our industry is not the timing of the interest rate shift but the resilience of prevailing asset prices and current loan structures in higher risk-free yields

	2014	2015	2016
CPI Inflation (EOY YOY)	**1.8%**	**2.3%**	**2.2%**
WSJ Consensus	1.9%	2.0%	2.3%
10-Year Treasury Yield (EOY)	**2.5%**	**3.4%**	**3.8%**
WSJ Consensus	2.8%	3.5%	3.9%
Fannie Mae	2.6%	2.9%	—
Freddie Mac	2.4%	3.4%	3.8%*
Cumulative Recession Probability	< 5%	10 – 15%	25% – 30%

Source: Chandan Economics, WSJ Consensus, Fannie Mae, and Freddie Mac Projections as of October 2014

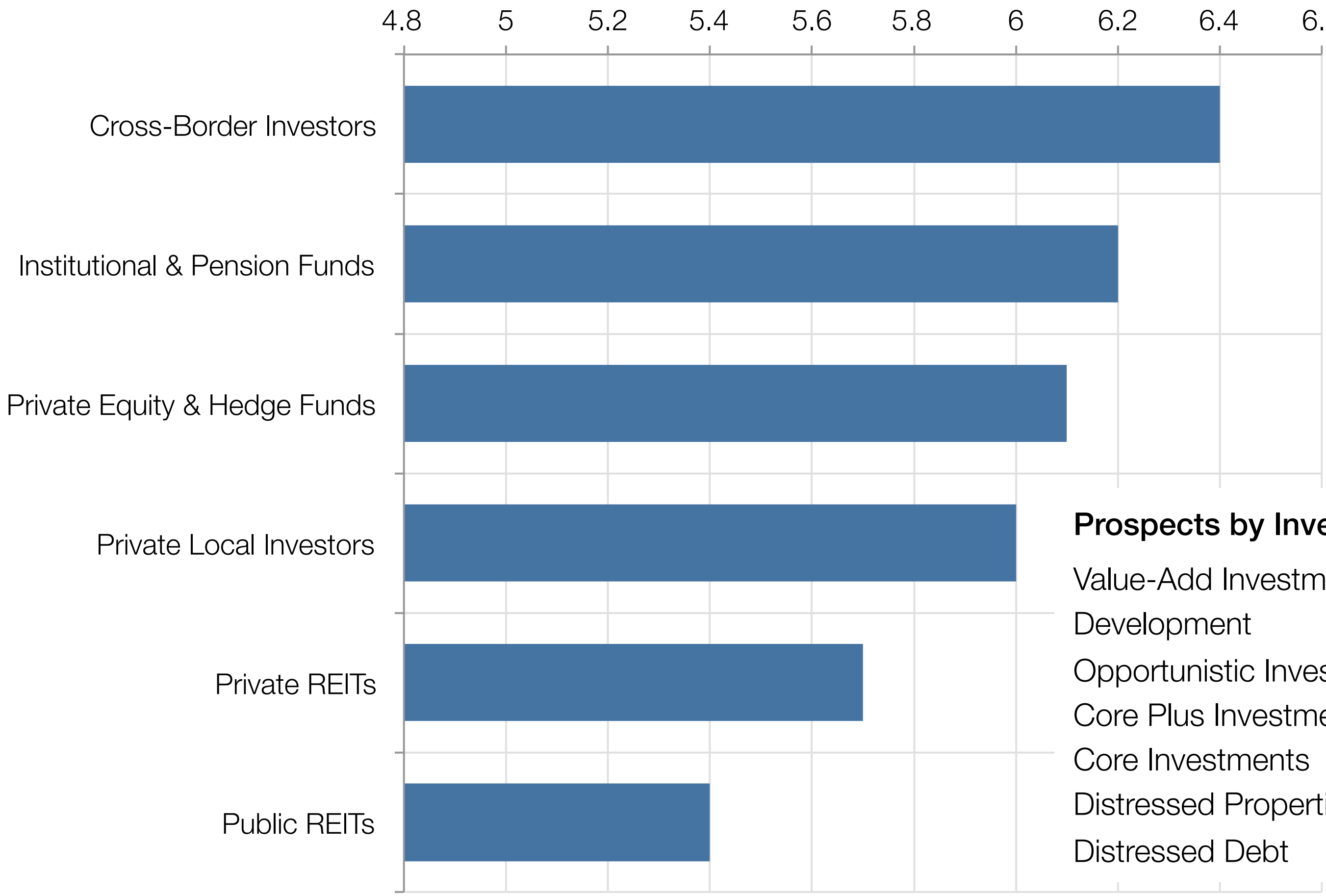
ASSET PRICING TRENDS



Source: Federal Reserve, NCREIF, Chandan Economics

SOURCES OF NEW INVESTMENT

Change in Availability of Capital by Equity Source

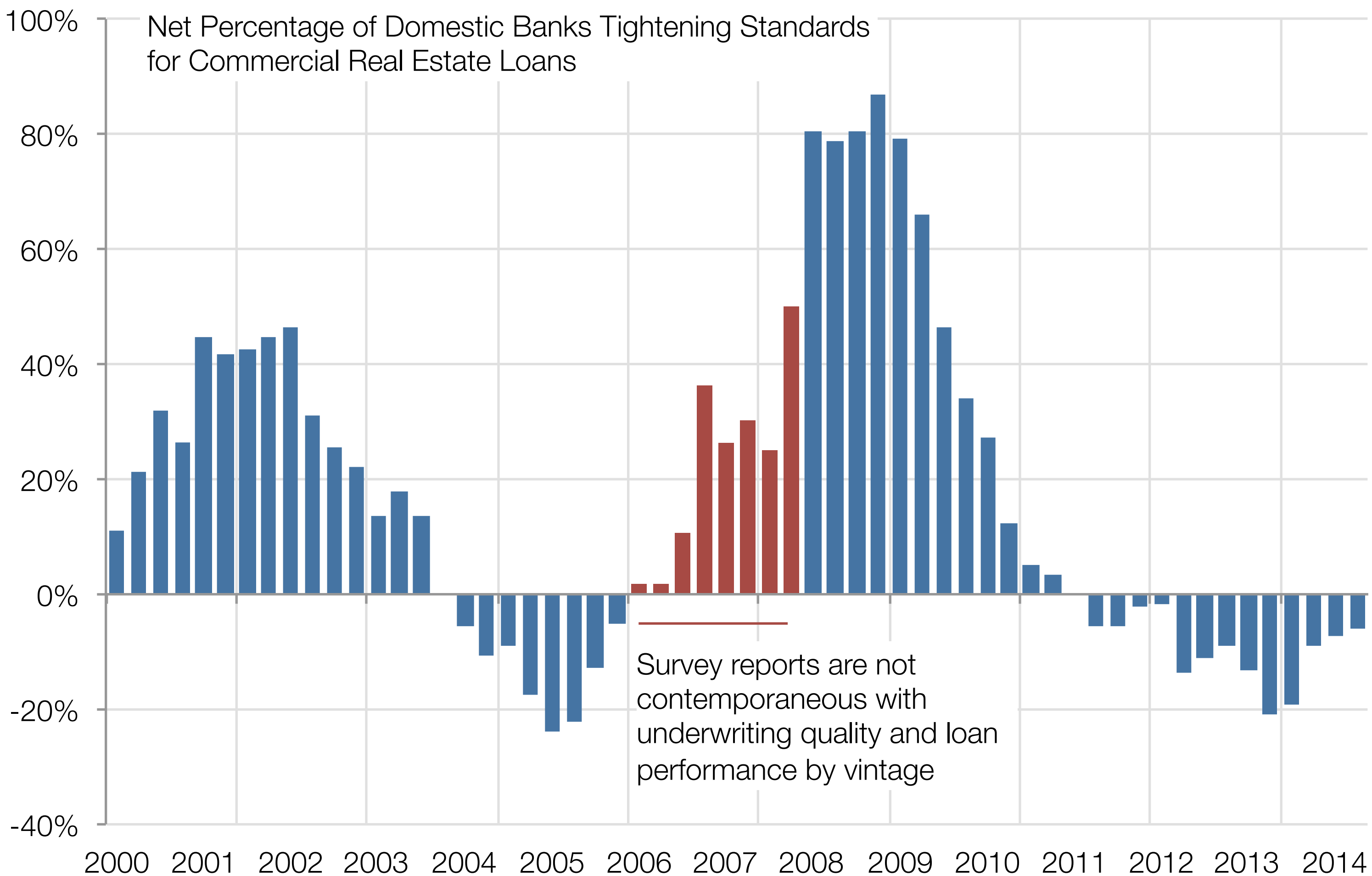


Prospects by Investment Category

Value-Add Investments
Development
Opportunistic Investments
Core Plus Investments
Core Investments
Distressed Properties
Distressed Debt

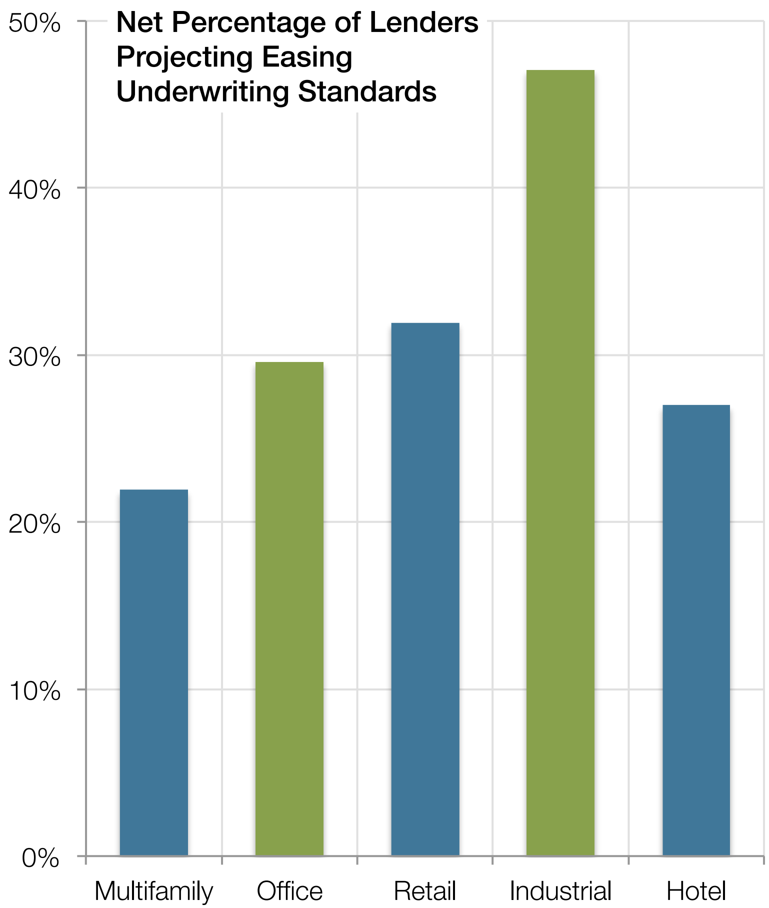
Source: PwC Emerging Trends in Real Estate 2014

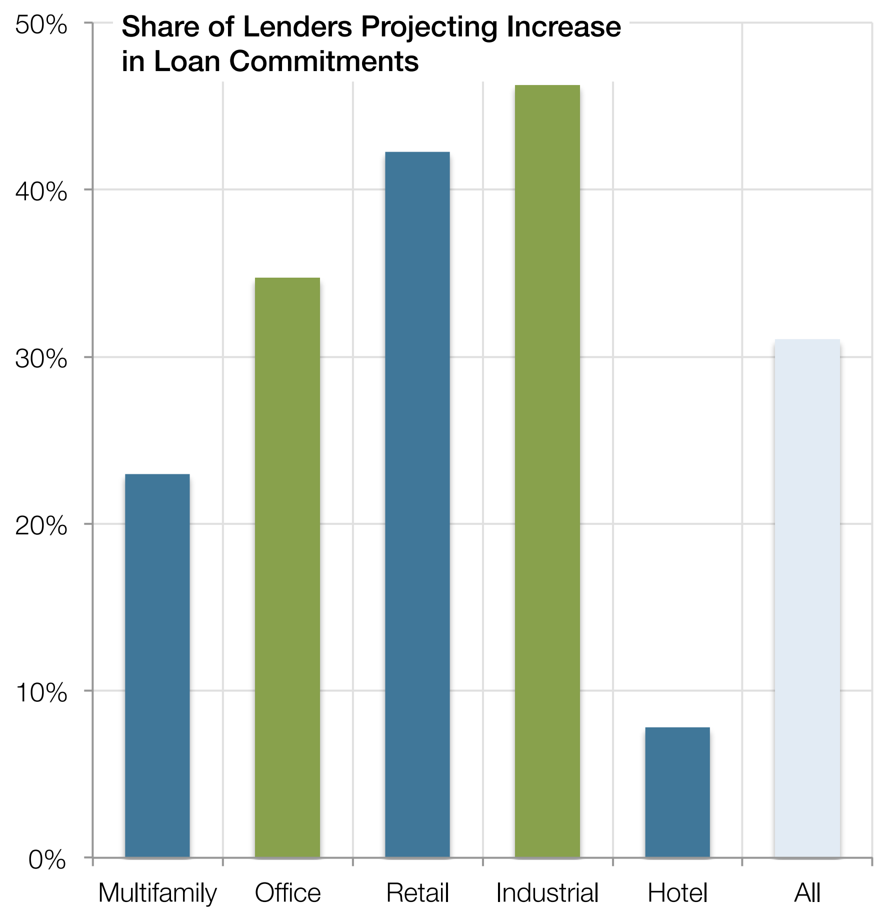
UNDERWRITING STANDARDS



Source: Federal Reserve, Chandan Economics; Note: As of Q4 2013, value is average for construction, commercial, and multifamily loans

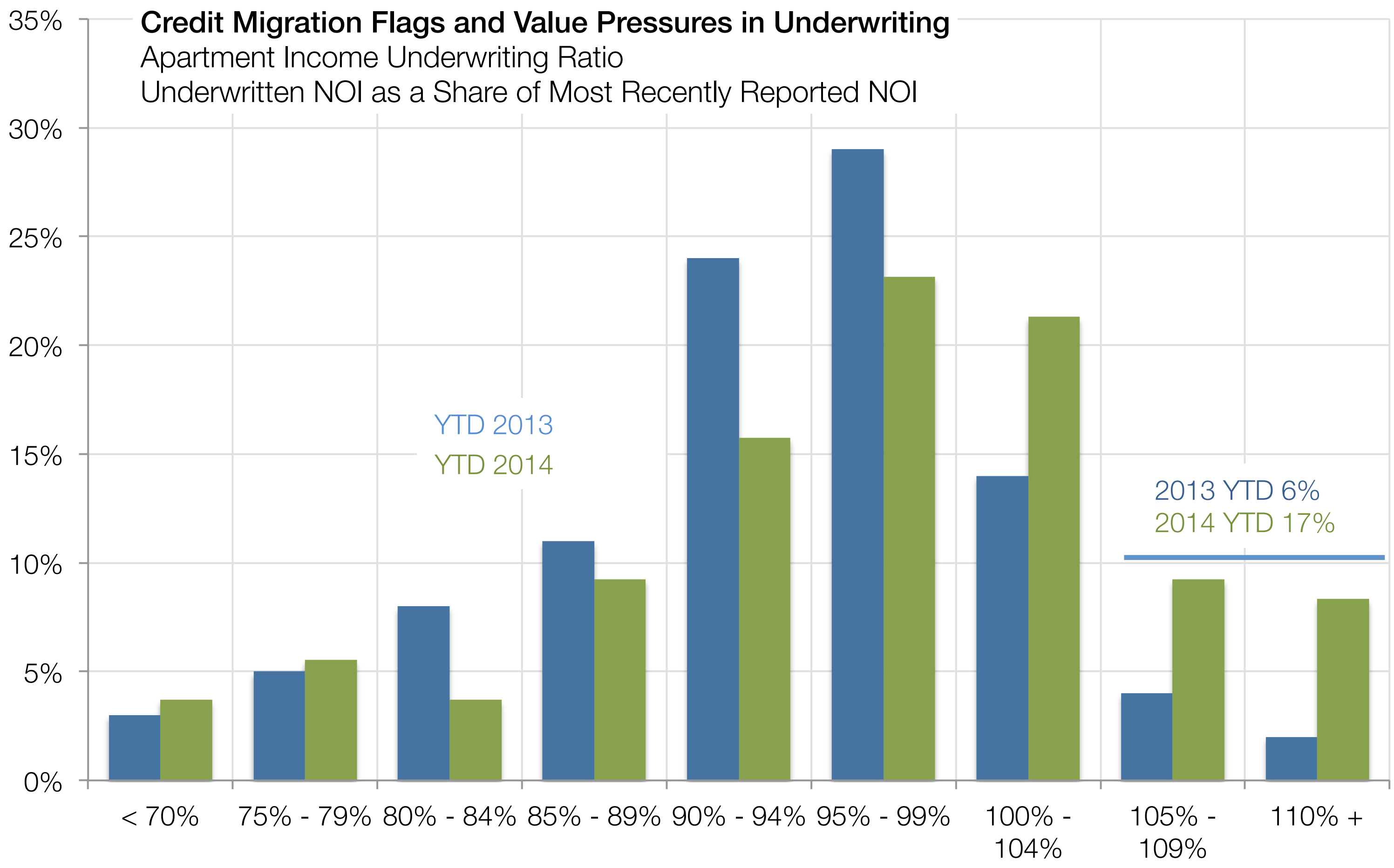
FINANCING TRENDS





Source: RELA-Chandan Survey of Commercial Real Estate Lender Sentiment 2014

APARTMENT CREDIT TRENDS



Source: Chandan Economics; Note: YTD through mid-August 2014; Based on properties with secured financing $1M+; actual and underwritten NOI observed for a subset of transactions only

SIX KEY OBSERVATION

Space Markets

4. Secondary market values are more dependent on property fundamentals
5. Inflexions in secondary markets are no easier to anticipate
6. Industry concentration exaggerates the upside **and** downside of the most coveted secondary markets

(LEADING) CANARIES IN A COAL MINE

1. NET INFLOWS OF CROSS-BORDER CAPITAL
2. INCREASE IN TRANSACTION VELOCITY
3. LOWER AMORTIZATION ON LOWER DEBT YIELDS
4. INCREASE IN LENDER DENSITY AND OVERLAP
5. ASSET-BASED LENDING ON STABILIZED PROPERTIES

FORWARD LOOK

- Adaptation to **changing space use patterns** across all property types, including smaller apartment units with more common spaces

- **Lenders giving ground** on underwriting as competitive overlaps increase. Growth in available debt outpacing growth in qualified borrower pool

- **More lending in more places to more borrowers**, benefiting construction, secondary markets, and non-core, non-stable properties

FORWARD LOOK

- Stable short-term **growth outlook subject to exogenous shocks**; long-term growth challenges remain largely unaddressed

- Moderate economic growth, improving labor markets, and marginally higher interest rates imply **more limited appreciation rates**; capital costs offset by income gains

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