

Emerging Trends in Real Estate®

2014



Emerging Trends in Real Estate® 2014

A publication from:



Emerging Trends in Real Estate®

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Notice to Readers

Emerging Trends in Real Estate® is a trends and forecast publication now in its 35th edition, and is one of the most highly regarded and widely read forecast reports in the real estate industry. *Emerging Trends in Real Estate® 2014*, 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® 2014 reflects the views of over 1,000 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 377 individuals and survey responses were received from over 694 individuals, whose company affiliations are broken down below.

Private property company investor, or developer	33.5%
Real estate service firm	26.1%
Institutional/equity investor or investment manager	17.6%
Bank, lender, or securitized lender	8.0%
Publicly listed property company or equity REIT	7.7%
Homebuilder or residential land developer	7.1%
Other	1.0%

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 who chose to be identified appears at the end of this report, but it should be noted that all interviewees are given the option to remain anonymous regarding their participation. In several cases, quotes contained herein were obtained from interviewees who are not listed. Readers are cautioned not to attempt to attribute any quote to a specific individual or company.

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.



Gaining Momentum

“Recovering from the **recovery.**”

Commercial real estate is reaching an inflection point where “valuations will no longer be driven by capital markets.” In 2014, *Emerging Trends* interviewees expect “space market fundamentals and property enhancements to emerge as the primary drivers of total returns,” reducing the reliance on falling capitalization rates and high amounts of leverage.

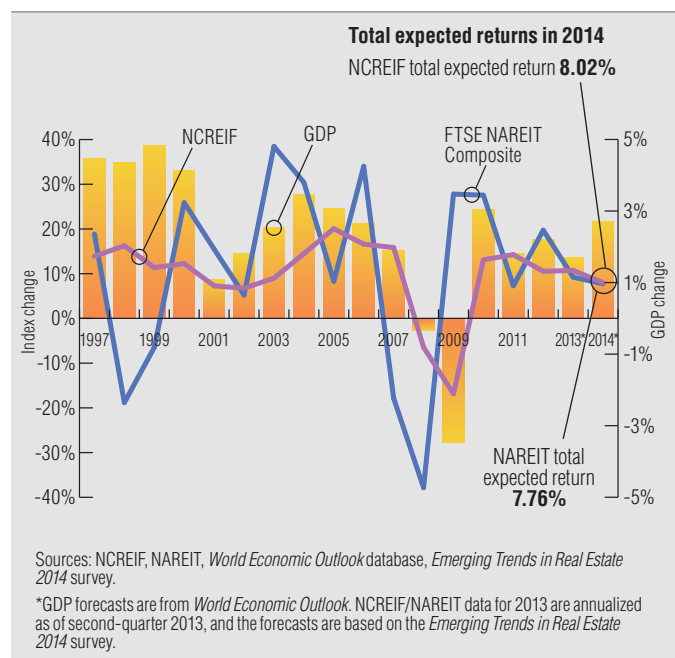
The real estate recovery will gain momentum in 2014. This should be good news to an industry that has experienced a recovery of fundamentals that has been much slower than it is used to after a recession. In fact, the pace of the recovery can make it difficult to spot the signs of improvement until they are in full swing. At first glance, many of the trends identified for 2014 are similar to those identified in previous years. These trends were relevant when originally identified, but the slower pace of this economic recovery prevented them from coming to fruition in the expected time frame. The difference for 2014 is that the market has progressed further through the economic and real estate cycles and we are now seeing real evidence that the trends have the momentum to finally make an impact on the real estate market.

The real estate market continues to move through the recovery phase of this cycle. The trends identified for 2014 portend both opportunities and challenges for investors in 2014. Economic and demographic changes will drive demands for real estate that are familiar and some that will require the industry to adapt. Equity and debt capital will continue to be attracted to the asset class, and the deployment of this capital will include more investment strategies that will involve a wider set of markets and property types. The economic recovery is projected to continue in 2014—and with it rising interest rates. The expected impact of rising interest rates ranges from little to

potentially leading capital to flow into alternative asset classes. Despite the wide range of opinions, everyone is convinced that the search for returns through cap rate compression will become the search for returns through improving fundamentals and/or operational improvements.

The year 2014 may well be the year that the real estate markets “recovers from the recovery.” Real estate professionals

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



interviewed for *Emerging Trends* expect growth to be sufficient to generate consistent and growing demand for commercial real estate across all property types. As one fund manager says of the moderate 2.5 percent gross domestic product (GDP) growth in the second quarter of 2013, “That is not huge, but it is enough to create demand for real estate product—that is, demand for

space and improving rent—because at the same time there’s almost no new supply. It’s a sweet spot for real estate.” An economist notes, “We have a new paradigm here. It is not the kind of recovery we have seen before with 250,000 new jobs a month. It’s a recovery with 100,000-plus jobs a month.”

“With the economy in a position where the tailwinds are now stronger than the prevailing headwinds, 2014 should be a year when we see real estate fundamentals improve in sectors beyond the already very healthy multifamily sector—and in a number of markets—to a point where we could see above-inflation-rate rental growth,” says a fund manager. According to *Emerging Trends* 2014 interviewees, the tailwinds include “good if not great” job growth—in industries that are, by no small coincidence, magnets for commercial real estate investment (energy, technology, health care and biological research, and, to some extent, education and financial services)—solid corporate profits, and a recovery in the housing market. These tailwinds are expected to trump the headwinds, which include a “stubbornly high” unemployment rate, uncertainty over government regulation and fiscal policy, and concern about the rising cost of debt capital.

The expected breadth of the recovery is illustrated by the view of *Emerging Trends* survey respondents toward the outlook for real estate business prospects. Prospects for almost all types of real estate businesses were rated more optimistically for 2014 than in last year’s survey for 2013. The improvement in business outlook was most significant for homebuilders, for whom prospects are not only expected to be significantly better than last year but whose prospects have more than doubled in the

EXHIBIT 1-2
2014 Issues of Importance for Real Estate

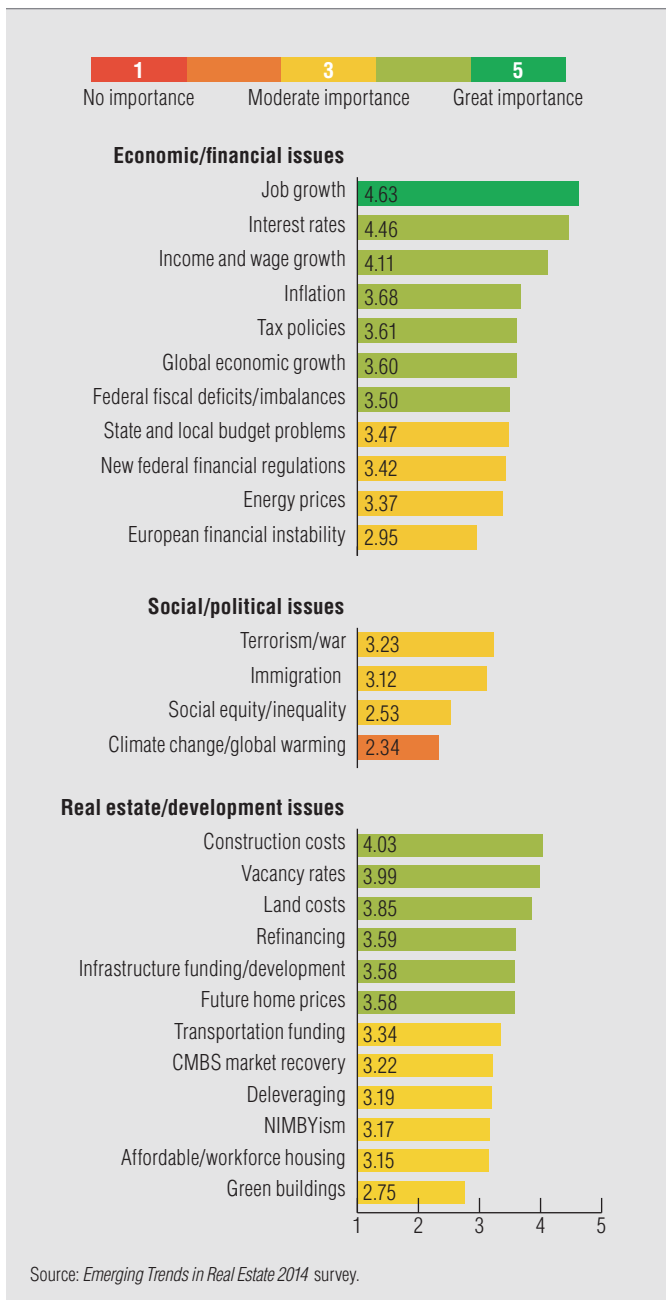


EXHIBIT 1-3
Emerging Trends Barometer 2014

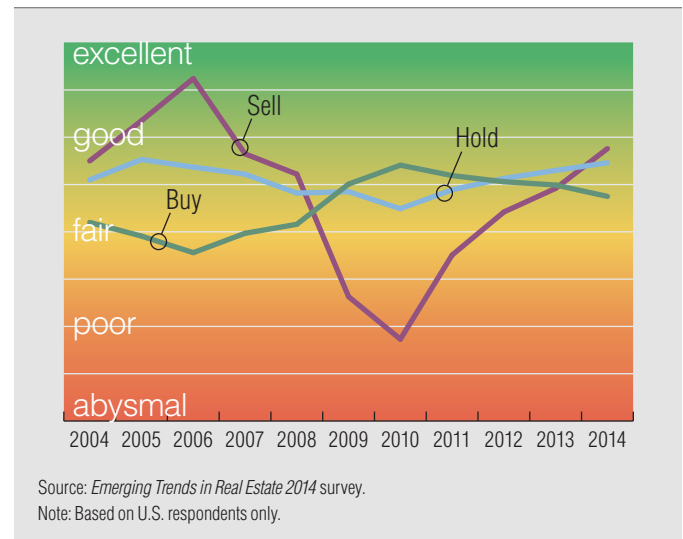


EXHIBIT 1-4
NCREIF Cap Rates vs. U.S. Ten-Year Treasury Yields

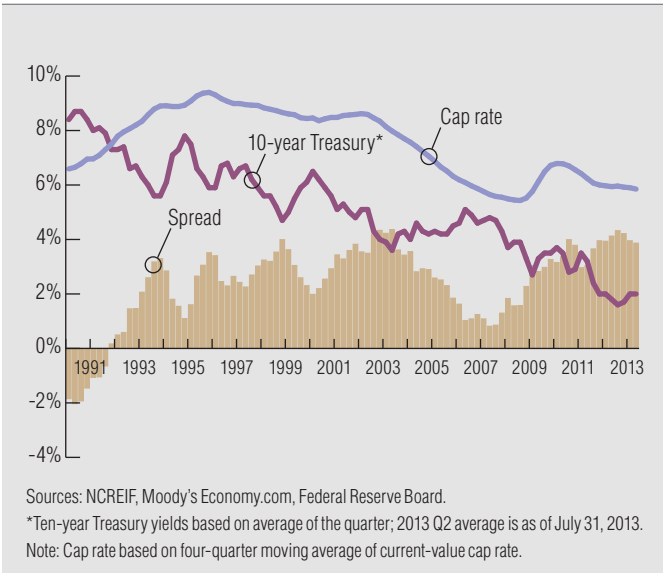
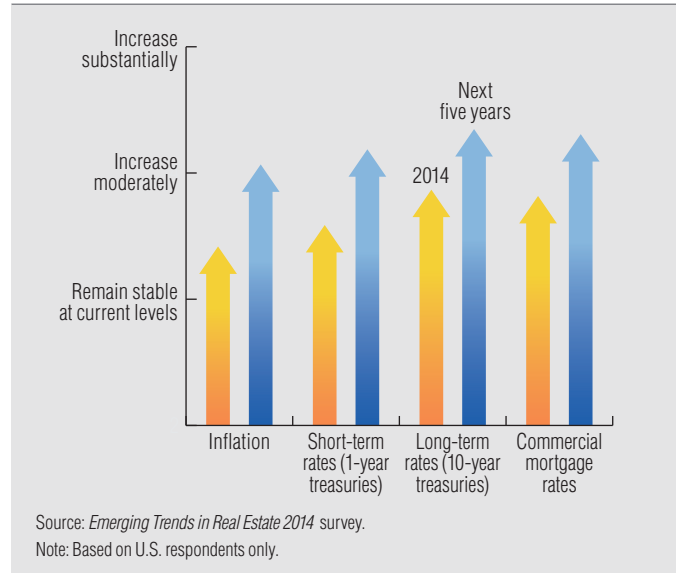


EXHIBIT 1-5
Inflation and Interest Rate Changes



past two years. As a result, homebuilders have moved from the weakest real estate businesses in 2012 to one of the strongest in 2014. Business prospects for commercial bank real estate lenders and commercial mortgage-backed securities (CMBS) lenders and issuers also improved noticeably.

Emerging Trends: Key Drivers for 2014

Prospects for Profitability Continue to Improve

Real estate market participants continue to do an excellent job of making money despite the slow recovery. Survey respondents are feeling more optimistic about their ability to be profitable in 2014 (see Exhibit 1-6). If market participants can feel good about profitability in a slow-growth recovery, they should be ecstatic if the recovery gains momentum. In 2010, only 18 percent of respondents felt the prospects for profitability were at a good or better level. This has improved steadily each year, with 68 percent of respondents now feeling that profitability will be at least good in 2014.

Increasing Interest Rates

Interview subjects and survey respondents agree that interest rates are going to rise just moderately in 2014. And it is widely believed that the market can handle an orderly increase in interest rates without serious disruption to the recovery. But the potential for rising rates leaves a lingering shred of uncertainty and discomfort over higher interest rates, which will muddle the exit strategy for investors if cap rates rise. “The question on everybody’s mind is how long interest rates are going to stay low. What happens when, five years from now, rates are up? What is your exit strategy? It is a crapshoot thinking about whether rents are going to go up in the next five years,” says a real estate service provider.

Ten-year Treasuries are expected to rise just moderately in 2014, as are commercial mortgage rates, according to the *Emerging Trends* survey respondents. This will bring to an end a six-year-long period of low interest rates and will mark a “return to more of a normal market.” But several interviewees commented that rising interest rates will not derail real estate investment—either debt or equity. If higher interest rates are a function of the Fed’s response to an improving economy in 2014, the increased borrowing cost will be offset by greater demand and thus higher rents. The key risk remains the timing and pace of interest rate increases.

Back to Fundamentals

Space market fundamentals have slowly improved to the point where, even with slow demand, real income growth is likely to occur over the next two years. With interest rates expected to rise, the market will begin to look at improving cash flows to drive returns. This transition from cap rate compression to fundamental performance will increase the emphasis on asset management to enhance returns.

As this new phase in recovery takes hold, investors will see income growth through rising occupancy or rising rents. This marks a significant shift from a dependence on cap rate compression for appreciation growth that has become ingrained in investment strategies across property types. Investors will

recognize the “good old common sense” behind the new rules of this game immediately. “If cap rates go up, you don’t have the financial engineering opportunity you had over the last couple of years,” says an investor. The result is that the more attractive properties may be those with more upside potential—a shift from recent trends where buying occupancy and safety was the primary criterion. And investors will learn to live with less leverage.

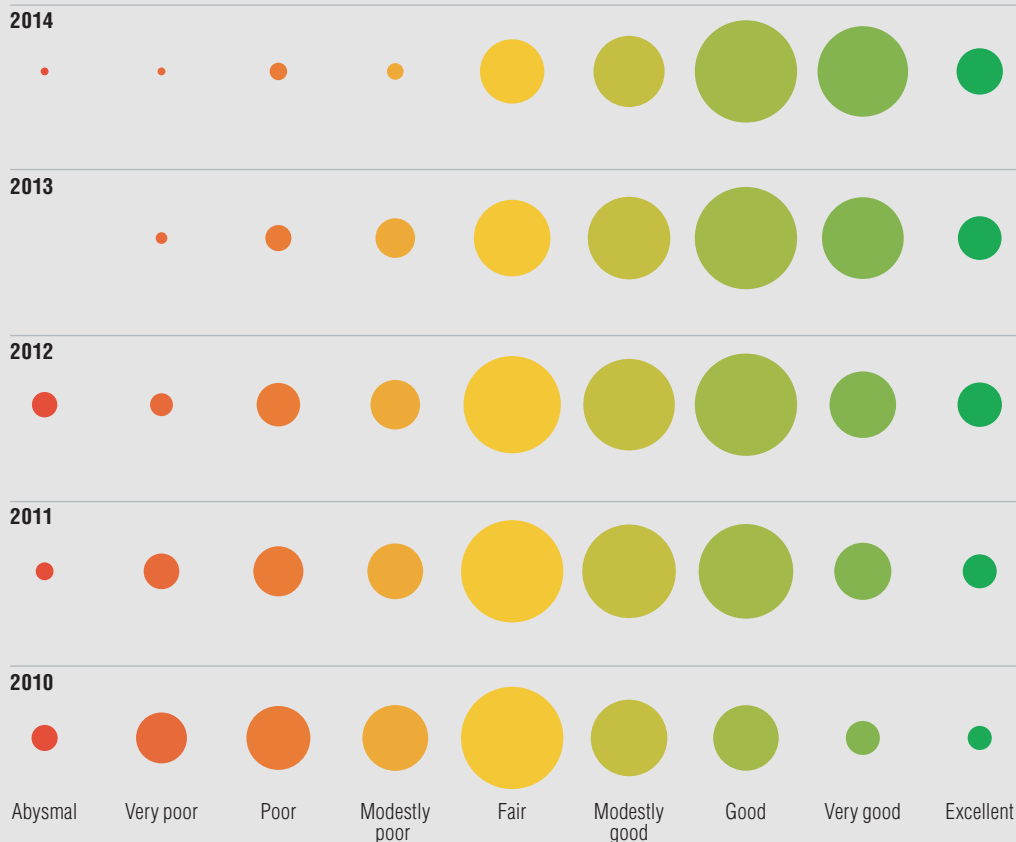
Capital Goes Wide

The availability of debt and equity capital is on the rise in 2014. Sources of capital are becoming more comfortable with the improving conditions in the market and are willing to invest in more markets and in a wider set of investment strategies. The

EXHIBIT 1-6

Firm Profitability Forecast

Prospects for profitability in 2013 by percentage of respondents



Source: *Emerging Trends in Real Estate* surveys.
 Note: Based on U.S. respondents only.

sources of capital are not all new. Equity capital will come from wealthy investors, institutional investors, global investors, sovereign wealth funds, real estate investment trusts (REITs), and family offices. Active debt capital players will include insurance companies, banks, mortgage REITs, global real estate funds and mezzanine lenders, and the commercial mortgage-backed securities (CMBS) market. The difference in 2014 is that providers of capital are looking to increase their allocation or are willing to look at investments that they have previously avoided.

An economist observes: “Nobody is talking about interest rates. They talk about availability of credit.” In fact, both interviewees and survey respondents agree that the markets will be awash in both equity and debt. According to survey respondents, availability of equity capital will increase the most from foreign investors; on the debt side, the CMBS market rose to the top of the survey of expected changes in capital availability.

Development Goes Beyond Multifamily

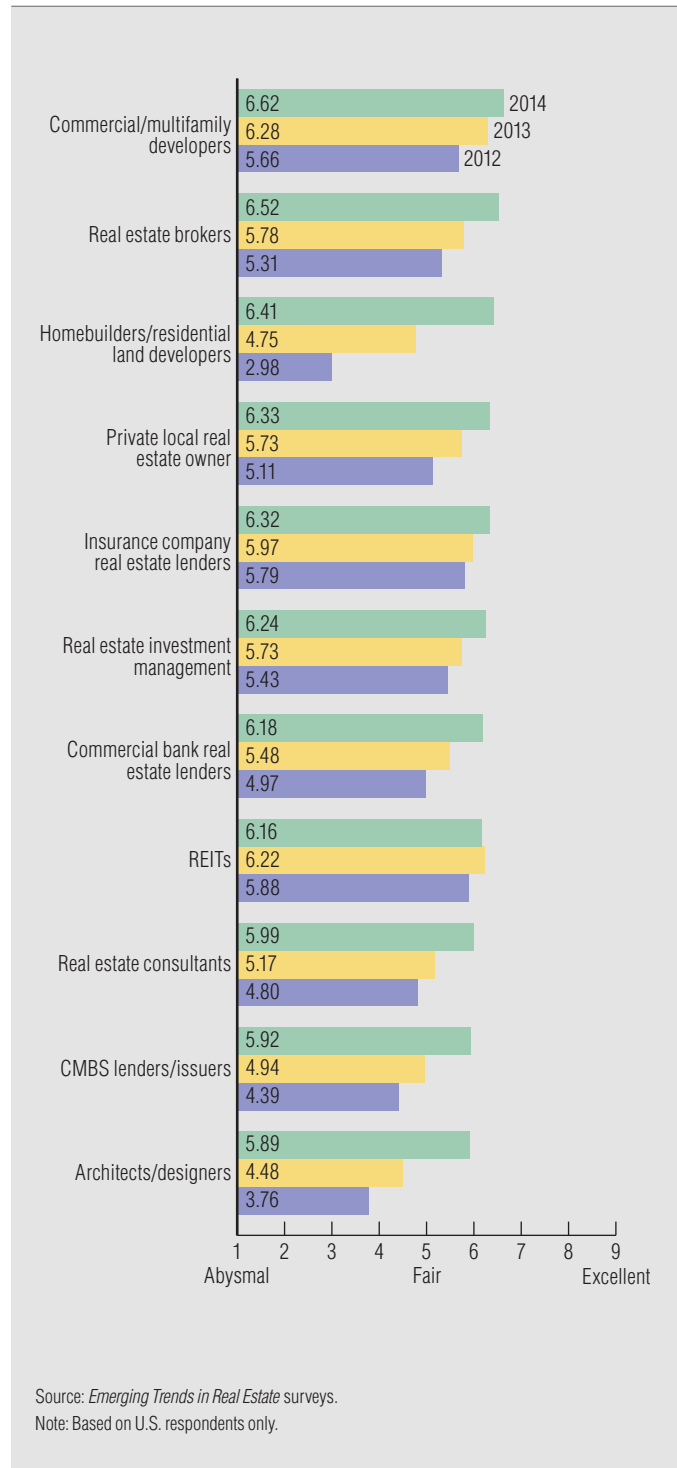
Survey respondents’ interest in development is up in 2014, and it isn’t the multifamily sector that lands at the top of the list. Industrial development is where respondents feel the best opportunities exist for development in 2014. Development over the past several years has been dominated by multifamily and build-to-suit opportunities, but the improvement in market vacancy rates is driving improved rent growth forecasts. The result is that development will be viable in select markets and property types. The office sector could see an increase in re-development as building owners look to reposition properties to meet changing tenant demands.

Survey respondents are comfortable that the recovery will continue even with slow growth in demand because new supply delivered remains at very low levels. In 2007, real estate data providers reported that new supply of commercial real estate was ramping up but had begun fairly late in the real estate cycle. With little new construction in the post-recession years, one economist predicts: “In 2014, we could start to see some tightening as we continue to absorb space with very little new supply at all. We might see landlords push rents a little higher than you might expect.”

Demographic Shifts

The growth of generation Y and its impact on all sectors of commercial real estate could be the singular most dominant trend for many years. This group lives, works, and plays in different ways than previous generations. The impact will be felt by all real estate sectors. This generation will be more urban and less suburban; they won’t want to drive as much but will want

EXHIBIT 1-7
Real Estate Business Prospects

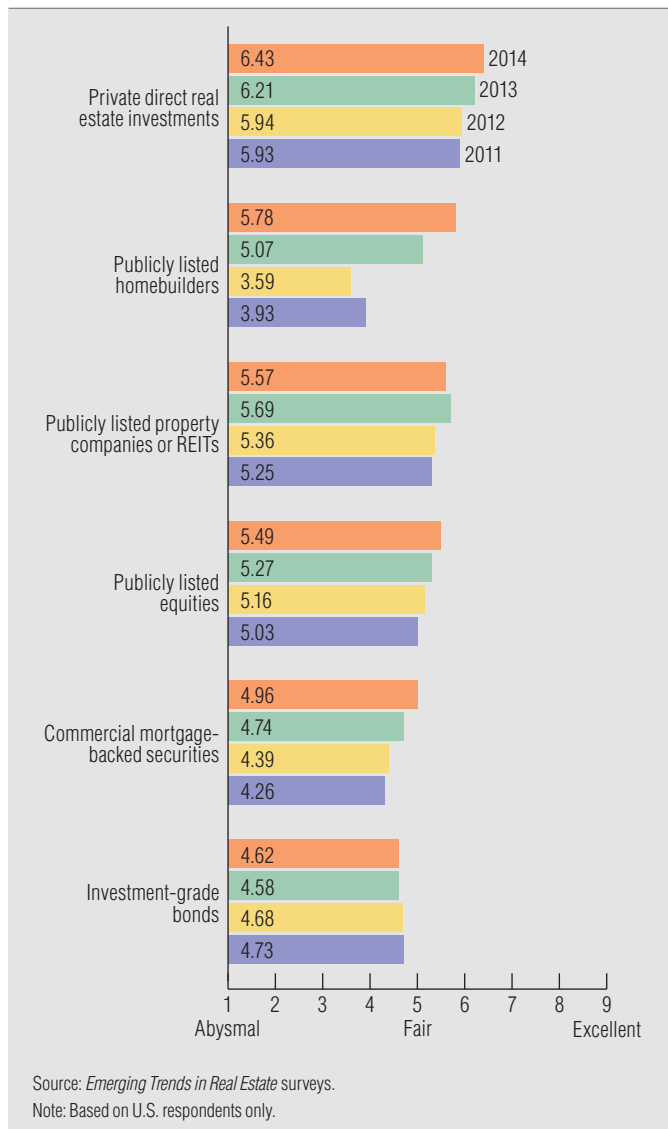


to be mobile. From intown rental housing to collaborative office space to close-in warehousing to ensure same-day delivery from online retailers, gen Y will be a noticeable force in shaping commercial real estate. All of these trends will have a significant impact on real estate. Referred to as a “powerful engine” by an investor, this generation “will be very good for real estate.”

On the other side of the demographic shift, the baby boomers also will drive change as they age; many will sell their homes and move to urban locations with similar amenities as those desired by gen Y (but with the added amenity of convenient health care).

EXHIBIT 1-8

Investment Prospects by Asset Class



The Changing Face of Space

All real estate property sectors are making changes going forward. Office users are demanding less space per worker as they reconfigure for more collaboration, and retailers are looking for urban formats that will be able to serve city dwellers more efficiently. Industrial space is being designed and located where it can meet the needs of online retailers with ever faster delivery times. And multifamily space is adapting to provide less space per unit, but increased common areas.

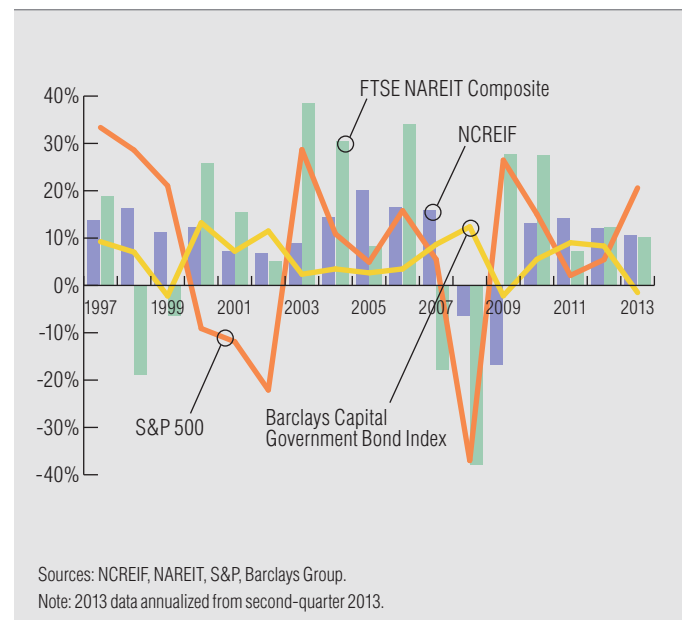
Housing Market Recovery

The housing market is no longer a drag on most local economies. The recovery to date has set up markets to experience growth going forward. The housing market recovery will be strong enough to be an unexpected boost to a number of local economies, allowing them to outperform expectations.

A number of local housing markets have seen prices return to levels comparable to the peak from the previous cycle. In most markets, activity has reached a level that is supportive of economic growth. In a number of markets hit particularly hard by the bursting of the housing bubble, investors have purchased distressed homes in bulk over the past several years. This has helped to stabilize these markets.

EXHIBIT 1-9

Index Returns: Real Estate vs. Stocks/Bonds



Gen Y Shifts America

Generation Y—those people born between 1979 and 1995—is an urban and urbane generation. There are 72 million gen Yers in the United States—approaching the size of the baby boom generation of 73 million—and, through immigration, gen Y is growing. This generation is the most ethnically and racially diverse of all the generations and stands out as the most urban, multicultural, and transient generation in America today.

Gen Yers are already changing the marketplace due to their preferences and large size—and they have the potential to continue having that impact as they age. Gen Y's preferences often stand in sharpest contrast to those of older generations.

Gen Y's preferences are profiled in *America in 2013: A ULI Survey of Views on Housing, Transportation, and Community* and *Generation Y: Shopping and Entertainment in the Digital Age*. These statistically representative surveys provide insight into their choices.

Preference for City Living

Of all the generations, gen Y is the most likely to live in a medium-sized or big city, and to express the preference to live in a medium-sized or big city in five years.

Current and desired size of community	Gen Y	Gen X	Baby boomers	War babies/silent generation
Currently in medium-sized or big city	39%	30%	30%	22%
Want a medium-sized or big city in five years	40%	23%	14%	25%

Source: ULI. *America in 2013*.

The *Generation Y: Shopping and Entertainment in the Digital Age* survey asked how gen Yers view themselves. In an exact match with findings published in *America in 2013*, 39 percent of gen Yers said that they were city people. Furthermore, 14 percent of gen Yers said they live either downtown or near downtown, 34 percent said they live in a city neighborhood outside of downtown, and 13 percent said they live in a dense, older suburb. That amounts to a significant 61 percent of gen Y now living in urban environments.

Preference for Compact Development

When asked about the importance of specific community features, gen Yers ranked the following characteristics highly: a short distance to work and school (ranked highly by 82 percent), walkability (76 percent), proximity to shopping and entertainment (71 percent), and convenience of public transportation (57 percent).

Percentage ranking at top (6–10)	Gen Y	Gen X	Baby boomers	War babies/silent generation
Short distance to work and school	82%	71%	67%	57%
Walkability	76%	67%	67%	69%
Distance to family/friends	69%	57%	60%	66%
Distance to shopping/entertainment	71%	58%	67%	69%
Convenience of public transportation	57%	45%	50%	56%

Source: ULI. *America in 2013*.

Gen Y takes transit, walks, and bikes. Of all the generations, generation Y is the most likely to use transit daily, or at least once per week. Americans of all generations are frequent walkers, but gen Y walks and bikes the most.

Percentage doing nearly every day or at least once per week	Gen Y	Gen X	Baby boomers	War babies/silent generation
Driving	90%	95%	94%	85%
Taking public transit	20%	7%	10%	4%
Walking to a destination	47%	46%	43%	31%
Biking	19%	16%	12%	6%

Source: ULI. *America in 2013*.

Gen Y Is on the Move

Far more gen Yers say they expect to move in the next five years than the adult population overall—63 percent and 42 percent, respectively. About 38 percent of the gen Yers expecting to move think they will end up in an apartment or a duplex, a townhouse, or a rowhouse—higher than the U.S. average of 29 percent. And compared with 49 percent of gen Yers who currently live in a single-family home, 60 percent of those who plan to move within five years expect to move to a single-family home. Still, this is lower than the current and expected single-family housing preference among all adults (66 percent and 67 percent, respectively).

Enduring Preferences?

Whether or not gen Y's preferences and habits will endure is an interesting question that no one can answer definitively right now.

An important question is: Will they be able to afford the lifestyle they want, in the locations they want? This will be determined by the ability of metropolitan areas to provide a range of affordable, appealing, and high-quality options—not just for gen Y, but for other generations as well.

Dealing with Uncertainty

The majority of survey respondents certainly had something to be optimistic about when considering 2014. This level of optimism, however, continues to be muted to some extent by a nagging feeling of uncertainty. The source of this lack of commitment to a sustainable recovery is almost universally blamed on the federal government.

The level of uncertainty surrounding regulatory, fiscal, and monetary policy is on the rise and is not likely to be resolved anytime soon. The market will need to deal with this uncertainty as it relates to job creation, capital pricing, and the cost of doing business.

Uncertainty Cuts Expectations for Washington, D.C.

Washington, D.C., was a favorite of survey respondents during the economic downturn and the early stages of the recovery. The consistency provided by the federal government sector supported the market while other markets dealt with falling employment. Unfortunately, what was once viewed as an asset

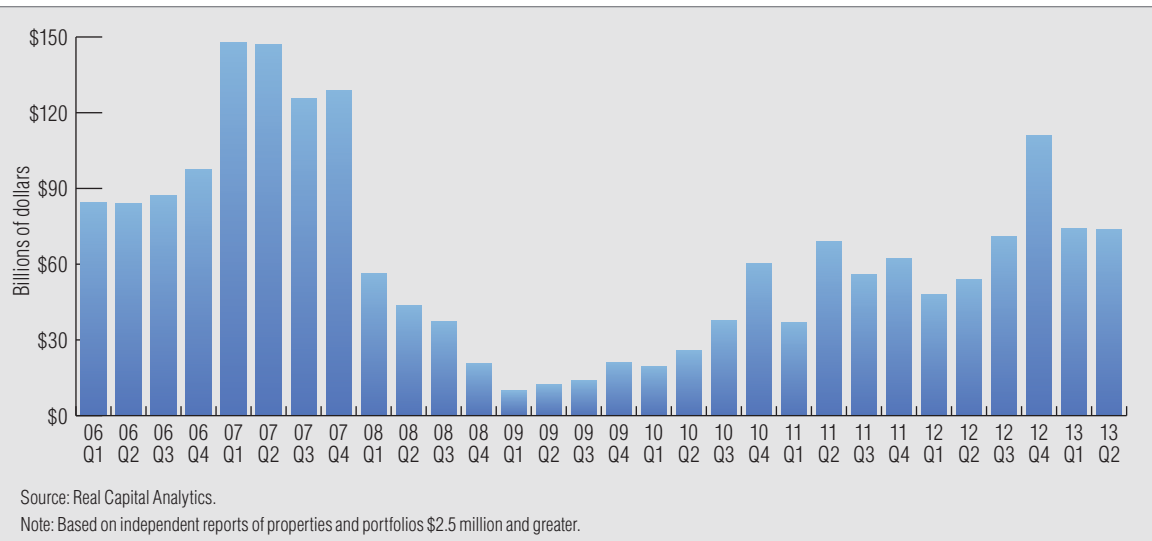
is now viewed as a liability. The Washington, D.C., market may well be suffering from “fed fatigue” as weariness sets in over government shutdowns and uncertainty persists over the future of government spending; even when these concerns are combined with a healthy supply pipeline, market participants are cautious about the prospects for returns. The potential for rising rates will change how investors enter into new investments.

2014 Condensed

In 2014, as the real estate industry enters the “middle innings” of the “recovery from the recovery,” industry participants note that this year’s opportunities do not come from financial structuring or the application of a “bit too healthy dollop” of leverage. Rather, successes in 2014 will emerge where an improving economy with strengthening fundamentals meets an investor’s property operating skills. Whether it’s a focus on overlooked markets and/or property types or a focus on repositioning, re-leasing, re-tenanting, or the like, *Emerging Trends* interviewees and survey participants agree that success and profits in 2014 will, as form follows function, come to those with real estate operating and management skills.

EXHIBIT 1-10

Sales of Large Commercial Properties in the United States





Real Estate Capital Flows

“All of a sudden, the banks are comfortable with real estate, which scared the daylights out of them from 2007 to 2009.”

As the U.S. economic recovery takes hold, the breadth of investors' and lenders' interest in commercial real estate is increasing. Participants in the real estate capital markets are now willing to consider investments and mortgage loans with increased risks as compared with last year's investment and lending models.

Thus begins the stage in the recovery where real estate investors—finding fewer and fewer opportunities in the primary markets—return to previously ignored secondary markets and less than perfectly positioned assets, as a steady stream of capital stands ready to be invested. *Emerging Trends* survey respondents agree with an institutional real estate adviser who notes, “The markets will be awash in both equity and debt... and foreign capital will be on the rise.” Survey respondents foresee increases in capital availability from almost all sources in 2014.

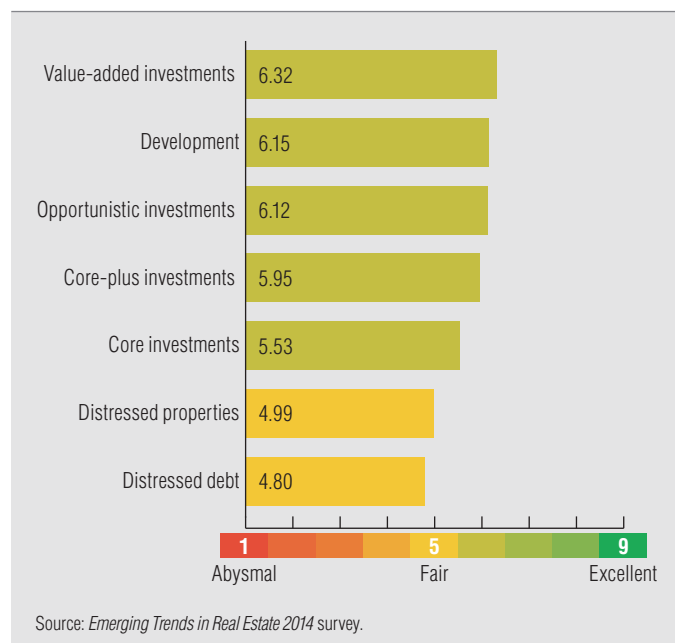
The search for yield through cap rate compression is becoming the search for increases in value through rent growth, vacancy decreases, and/or operational improvements. Online survey respondents support the observations by interviewees that 2014 is forecast to be the year that institutional investors reduce their emphasis on core properties. In the expectation that core investments with fixed-income-like streams might struggle with valuations as exit cap rates begin to rise, their future equity investments should reflect a search for higher returns in value-added and opportunistic investments in secondary locations, with development focused in only the strongest markets.

No longer will investors look only to the “big six” markets—Boston, Chicago, Los Angeles, New York City, San Francisco, and Washington, D.C.—to protect the value of their assets. In 2014, new investments could demonstrate a rising level of confidence in the economics of secondary markets for investment.

Investors in the coming cycle may create value by repositioning assets rather than solely through financial structuring. The head of a large property management firm opines, “There is a fair amount of space in markets today that could struggle indefinitely in its current position, but, with a new look or purpose, could be a significant competitor to new development.”

And, in an indication of the risk that institutional investors may come to accept in the years to come, one Wall Street fund

EXHIBIT 2-1
Prospects by Investment Category/Strategy



manager, when asked where he plans to invest his “next \$500 million,” replied, “I would put the risk trade on. I would build into growth. I would be doing construction of speculative office. You can be outside of the top 12 markets, and you can do it.”

But the key risk remains the timing and pace of interest rate increases. As one real estate investment adviser observes: “Everybody believes interest rates will continue to rise, but I don’t know if [they] will be dramatic or not. When interest rates go up, cap rates start to go up. Then rental rates tend to go up when there is no construction to compete with and supply is constant. So the earnings on a property will go up. That will offset some of the increase in cap rate increases. So the values

won’t be hit as if you got a fixed income stream with a rising cap rate. How that relationship plays out, I don’t know. But it will mitigate the increase to some degree that everyone is expecting in cap rates.”

Lenders Increase CRE Exposure

“Now there is starting to be some financing available—not back to where it was, but starting to trend that way,” notes a real estate investment adviser. “Pools of capital are being put together to make loans. Financial organizations that are not traditional banks are starting to make loans again in a significant way. Private equity funds are pooling capital from pension funds. They are making the case that they can get yields from CRE debt lending at rates that are competitive with Treasuries and bonds. We are moving back into a normalized real estate cycle where debt and equity may be available and in the short term people may be very cautious about how they underwrite their deals. There will be rational capital structures. There are significant opportunities. CRE can support the debt that will be put on it. Yields will look competitive in the current environment. Money should flow to those investments. Then, banks that are now being paid to do nothing [i.e., to hold balance on their balance sheet at the federal funds rate] will have to come back and compete in the marketplace for investments.”

EXHIBIT 2-2

Change in Availability of Capital for Real Estate in 2014

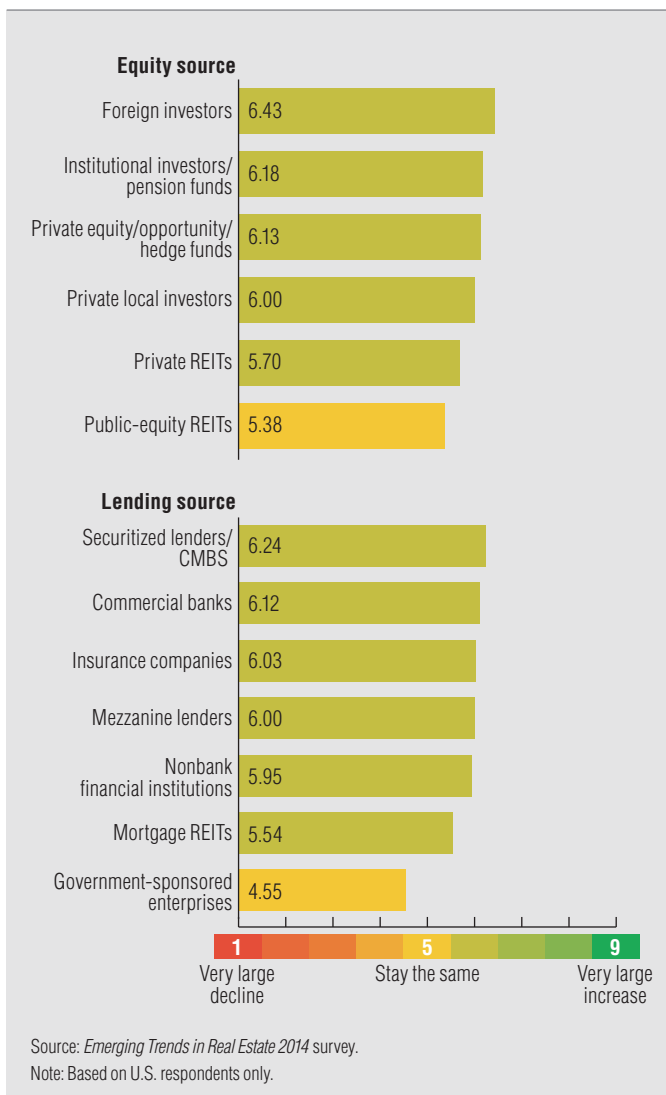
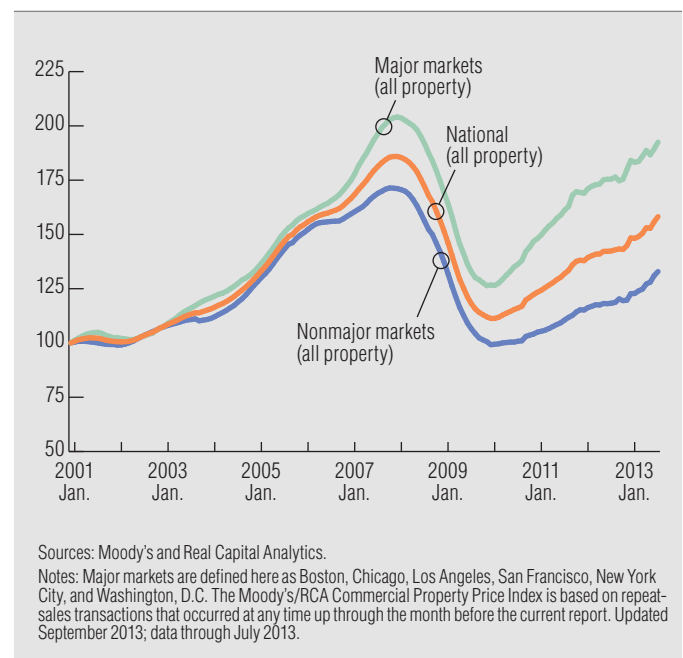


EXHIBIT 2-3

Moody’s/RCA Commercial Property Price Index



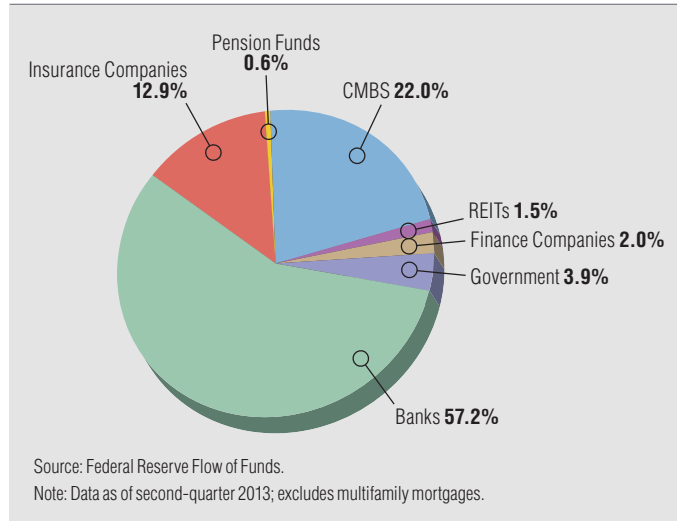
Respondents to the *Emerging Trends* survey expect an increase in the availability of debt capital from five principal sources: the commercial mortgage-backed securities (CMBS) market, commercial banks, insurance companies, mezzanine lenders, and nonbank financial institutions. The CMBS market, though far from historic peak volumes, has recovered from its trough and has grown over the last several years. Expectations of its continued growth brought it up from third place last year to its current first place.

Commercial banks rose to second place in the survey in terms of expected availability of debt capital, from fourth place a year earlier. Notwithstanding the expected increase in interest rates, as the Fed tapers its QE initiatives, commercial banks should retain their ability to be very competitive in 2014. To some extent, lending by banks and insurance companies could absorb any reduction in capital provided by Fannie Mae and Freddie Mac, should the federal government follow through on revamping these agencies. But, as one real estate analyst says, “Nothing will happen next year. All thought of reforming Fannie and Freddie is still on hold, despite the occasional glimmer of a proposal or a hearing.”

CMBS Revival

Rising to the top of the survey of expected change in capital availability, from third place a year earlier, is the CMBS market,

EXHIBIT 2-5
Commercial Mortgage Debt Outstanding, by Source



which several interviewees estimate could originate \$100 billion or more in 2014, easily exceeding the 2013 estimate of \$80 billion. An increasing number of CMBS issuers will be available to pick up the slack if commercial banks, insurance companies, pri-

EXHIBIT 2-4
U.S. Buyers and Sellers: Net Capital Flows, by Source and Property Sector

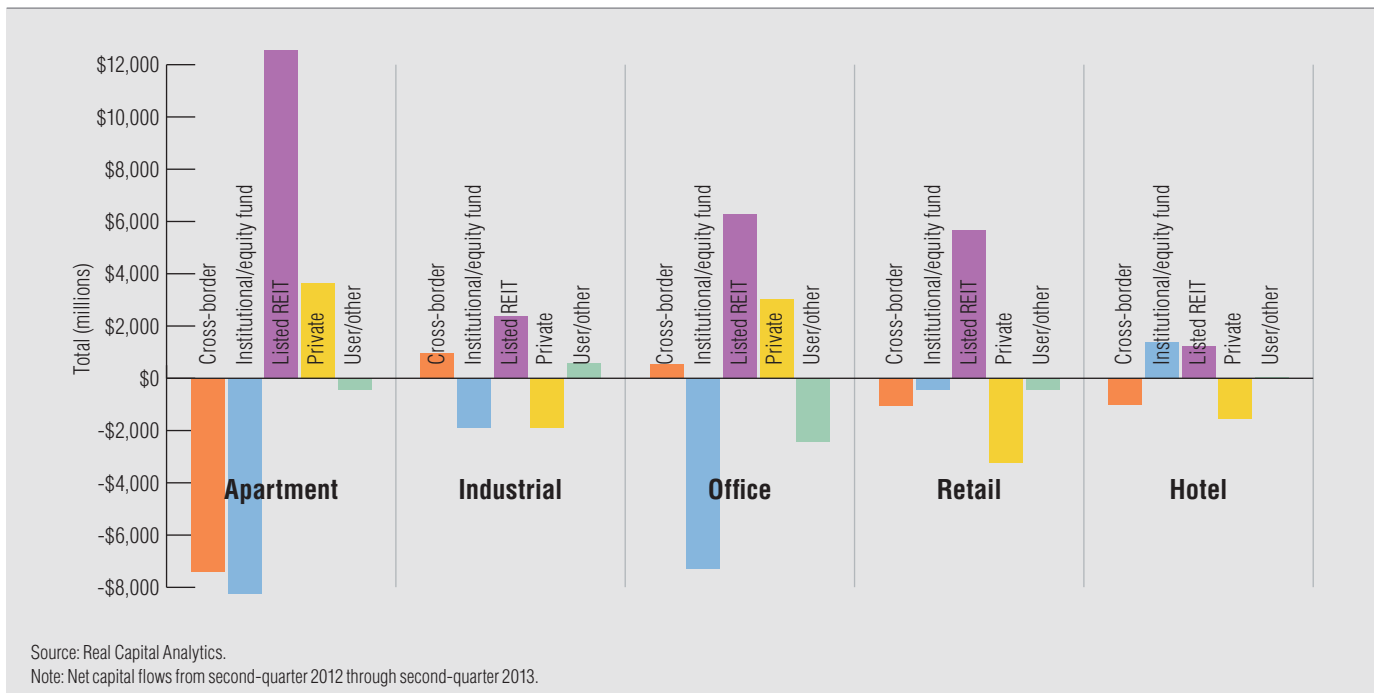
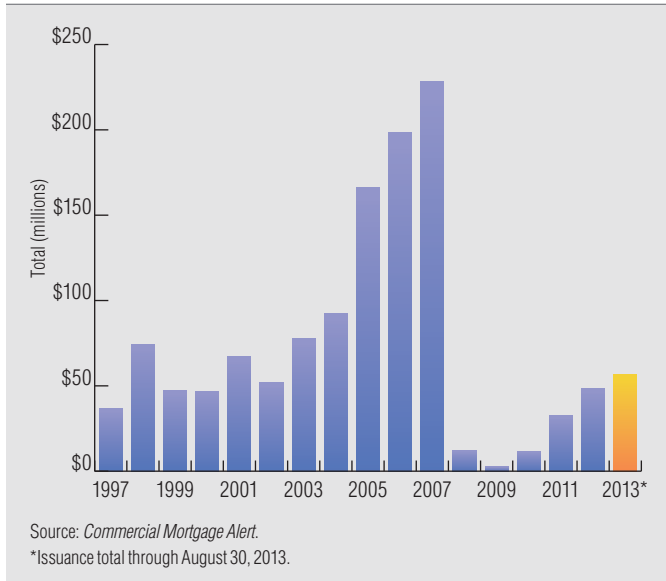


EXHIBIT 2-6
U.S. CMBS Issuance



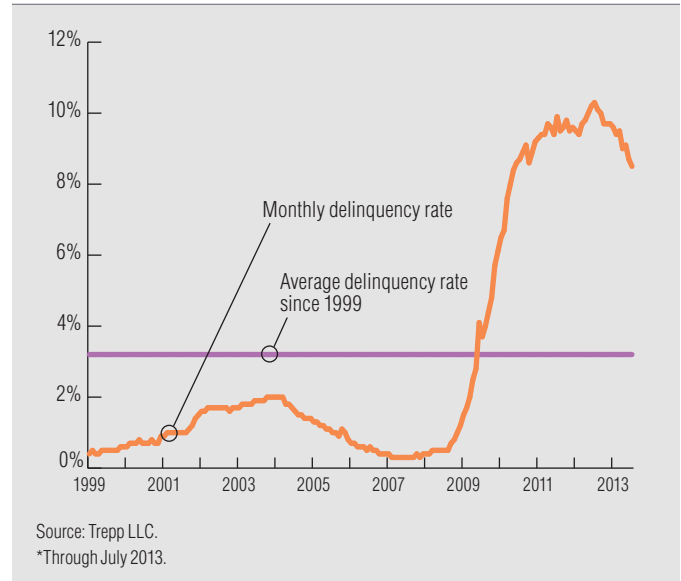
vate equity players, and mortgage real estate investment trusts (REITs) cannot keep pace with new demand for debt capital.

While this segment of the U.S. fixed-income market is not expected to return to its precrisis peak, it is still expected to stabilize at “a healthy level” and “remain steady going forward,” according to several interviewees. In a sign of improving health, CMBS delinquency rates have fallen, reaching 8.14 percent in September 2013, down from 9.99 percent in September 2012, according to Trepp LLC.

“CMBS is an important and needed piece of the capital structure for commercial real estate. This could be even more necessary if commercial banks find their ability to lend influenced by [Dodd-Frank] guidelines that could set real limits on real estate lending. You will see the need to expand beyond commercial banks if we are going to meet the capital needs of the commercial real estate market,” says a banker.

One reason for interviewees’ optimism about the CMBS market is that it has proved surprisingly resilient since it effectively shut down for three years after peaking at about \$230 billion in annual issuance in 2007. The first eight months of 2013 saw the issuance of about \$56.4 billion in CMBS despite a spike in ten-year Treasury rates in June. Now, investors are crowding into the below-investment-grade tranches as CMBS provide a higher-yielding alternative. “Whereas a year ago they had only one or two investors for the B-piece, they now have more than 20 investors in the B-piece,” says a senior financial officer. “Everyone thought the limited number of B-piece buyers would

EXHIBIT 2-7
CMBS Mortgage Delinquency Rates



be a constraint, but it hasn’t been,” says an institutional investment adviser.

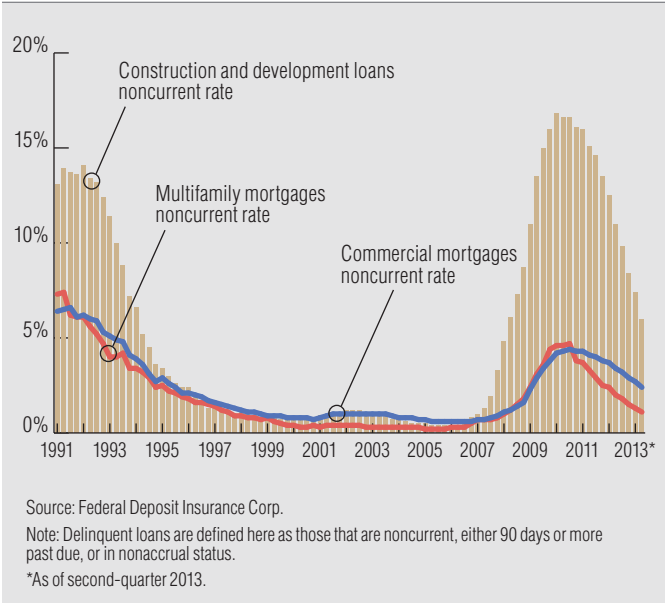
Among the most active CMBS borrowers could be equity REITs, typically for deals under \$25 million, according to one analyst. “There is definitely an uptick. Deals are getting financed. It is not the same as it was, but then again it should not have been what it was,” the analyst says.

Commercial Banks

In another emerging trend, expected higher interest rates may incentivize banks, which now hold about half of the commercial real estate loans in the United States on their balance sheets, to once again pursue more loans in the expectation that lending could become more profitable at higher rates. “They still have loans on their books that they have not written down. Their balance sheets have started to improve. They have had some gains, so they will be able to take some losses. They will be able to sell off some of their assets,” says one real estate investment adviser. In addition, real estate loan delinquencies for banks and CMBS lenders are declining and as loans mature, they will free up room on bank balance sheets to make new loans in an era when perceived risk has diminished for this asset class.

In their rush to finance real estate transactions, banks could tighten spreads on loans to become more competitive. “A lot of banks are being quite aggressive in terms of what they are comfortable with in underwriting risk in transactions, and are prepared to compete very heavily on pricing in the market. So

EXHIBIT 2-8
Bank Real Estate Loan Delinquency Rates



spreads have gone down. In the absence of the economy taking a backward step, I can certainly see that continuing in 2014,” says a banker.

Banks may also undercut each other to refinance floating-rate loans to fixed rates. “Regional banks and large money-center banks have been really competitive this year,” says a banker, referring to 2013. “They have been swapping out floating-rate business for five-, seven-, and ten-year fixed business at very competitive rates.” And it’s not just American banks. “Canadian banks have been very aggressive in pricing and Asian banks are starting to ramp up lending in the U.S.,” the banker adds.

Forty-three percent of survey respondents expect that debt underwriting standards “will be less rigorous.” Though lenders are now “far more cautious of the sponsorship” than they were in the first half of the last decade, “lending rules are trending to [those seen in] pre-recession times,” says a commercial real estate manager.

These developments may mark “the first expansion in bank lending since the first quarter of 2008,” says an industry association executive. Since 2007, all but a few large banks with clean balance sheets have been fairly conservative regarding new lending while trying to get as many loans repaid as possible.

“All of a sudden, the banks are comfortable with real estate, which scared the daylight out of them from 2007 to 2009, and they are looking for opportunities,” says an investment fund manager.

EXHIBIT 2-9
Real Estate Capital Market Balance Forecast

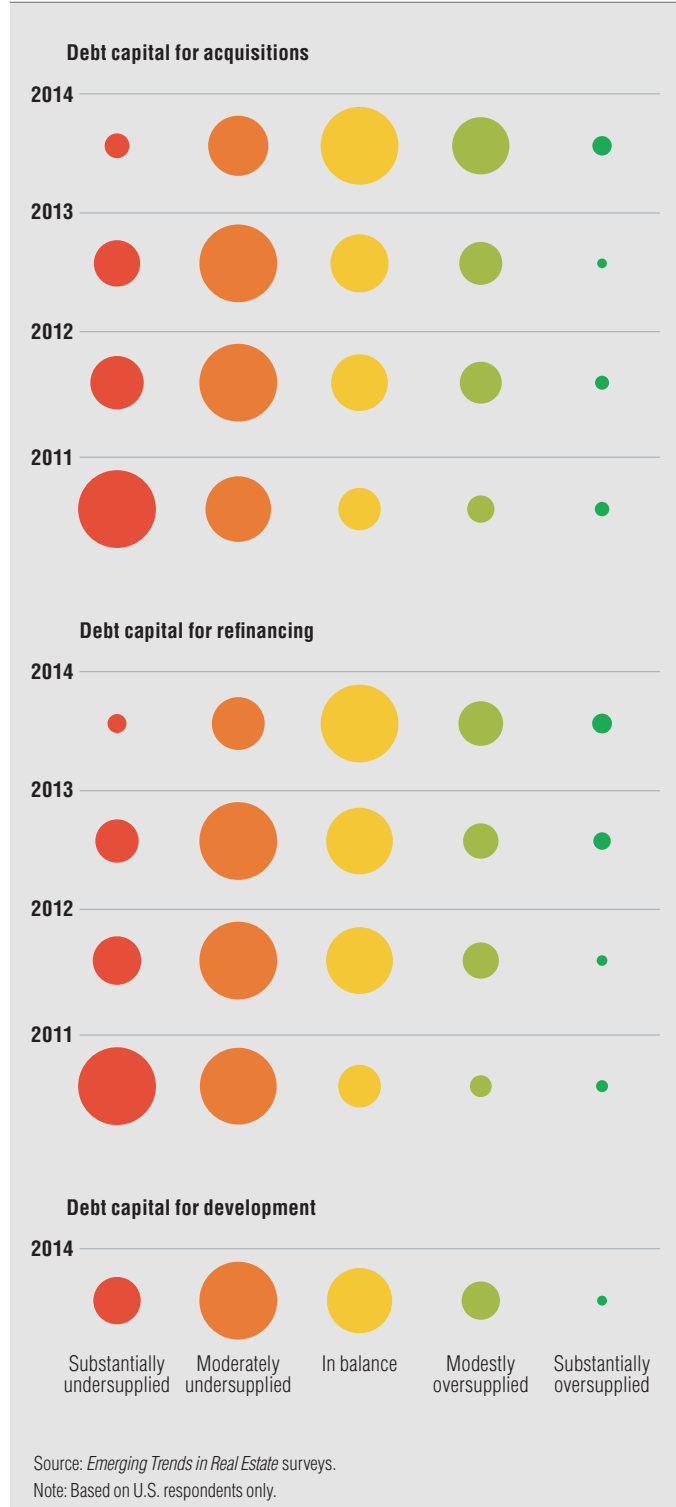


EXHIBIT 2-10

Debt Underwriting Standards Forecast for the United States

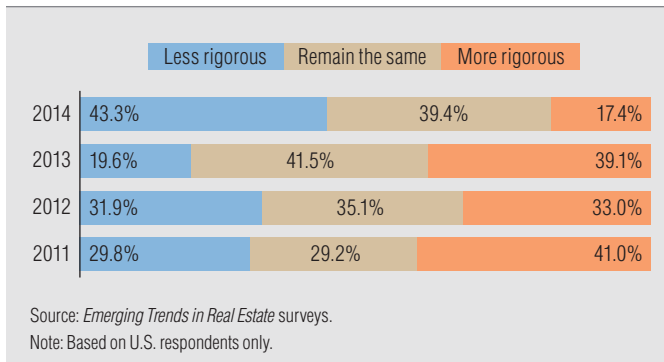
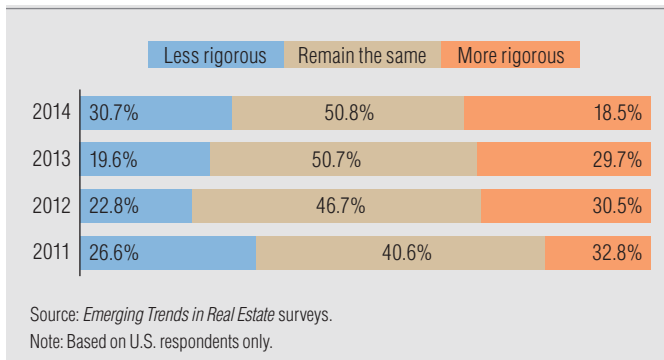


EXHIBIT 2-11

Equity Underwriting Standards Forecast for the United States



For regional and community banks, the motivation is generally that they “are healthier now and have turned the corner over the past 12 months and are aggressively trying to grow their assets in a defensive manner,” says a fund manager. The improvement in bank balance sheets should free up lending capacity for new deals, providing additional capital for projects in secondary markets. “Community and regional banks are increasingly eager to lend and have lots of capital to do it in their own backyards,” says a commercial real estate fund manager. Continuing to focus on local borrowers, they will “help smaller developers get the small projects going” while those who want to invest on a national scale will continue to keep their loan origination costs down by taking out larger loans from national banks. This trend of increasingly more active community and regional banks in commercial real estate “is coming here in 2013 and will be bigger in 2014 and 2015,” says an investment fund manager.

Banks could start issuing types of loans from which they have abstained since the recession, such as construction and development loans. “Requests for development financing will be up. There will be more focus on new development rather than redevelopment,” says a commercial banker. Though “new development deals will still require 50 percent equity and significant preleasing,”

Higher interest rates should make it easier to convince borrowers to take out shorter-term loans. The increase in ten-year Treasury rates in June “had a big impact” in that “it changed borrower behavior and it changed the underwriting of deals,” says a banker. “Sponsors will settle for shorter-term debt to lock in a cheaper rate rather than fixing it at a ten-year level. Now they are looking at seven-year or five-year deals.”

The availability of financing could make it easier to rationalize higher-risk projects. Thus, banks may slide down the quality scale on the assets they lend against because borrowers could be more inclined to accept a higher interest rate regime. “Sponsors are prepared to take the risk of less certainty during their investment window. Banks will start lending on more secondary or ‘value-add’ assets,” says a banker. “I can see more banks and investors start to chase more Class B assets going forward. I can see the spreads tightening a bit.”

Life Insurers

While life insurers fell to third place in the survey of expected change in availability of debt capital, from first place a year earlier, they still are expected to grow their commercial real estate lending in 2014, according to an investment fund manager.

EXHIBIT 2-12

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

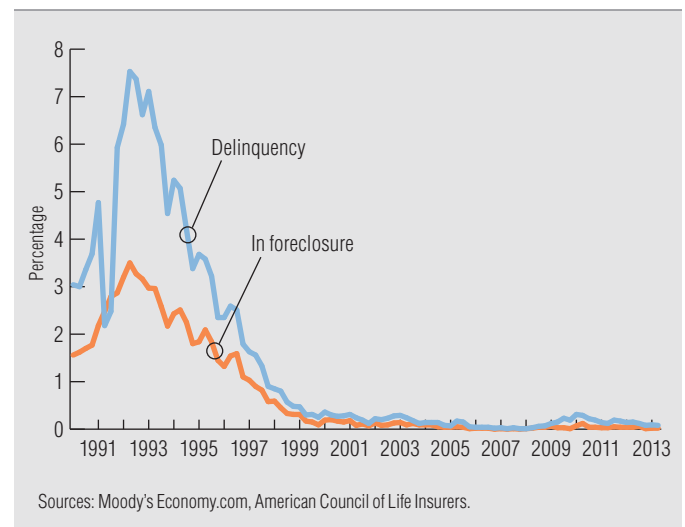
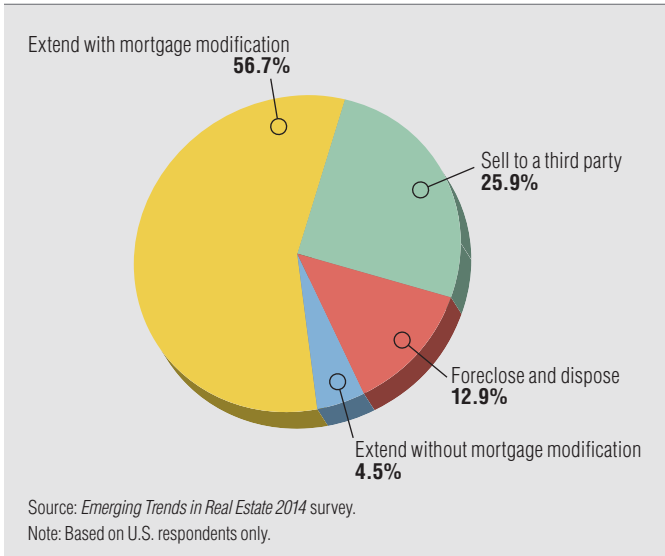


EXHIBIT 2-13

Maturing Loans: Preferred Strategy for Lenders

Having aggressively managed their loan portfolios since the global financial crisis, they should continue to focus on very high-quality loans. The one factor that could reduce demand for loans would be if corporate bonds of comparable ratings were to start offering more attractive investment spreads. “As rates go up, you will see insurers continue to be active in providing financing to the real estate industry,” says a commercial real estate firm executive.

Mezzanine Debt

“The mezzanine capital raised will be invested in positions ranging from additional equity to preferred equity to mezzanine positions to help rationalize current debt. New to the game are investors coming in with new debt to take out old debt. The overhang of bad investments will eventually be eaten up,” said a real estate investment adviser. Mezzanine debt fell to fourth place in the survey of debt capital availability in 2014, from second place a year earlier. “The biggest question on mezzanine is where the returns are going to be,” says an investment banker. “If mezzanine rates don’t increase enough and we don’t feel we’re getting paid enough, we’ll stop. At a 200-spread [basis points] difference, we don’t think we are getting paid for the risk.”

Still, some interviewees see mezzanine debt becoming more prevalent in 2014, not less so. “Mezzanine will be more competitive in the future because there is more and more capital available,” says an investment adviser. Other interviewees predict an “increase in B-piece, mezzanine, and debt funds available to fill gaps in the transaction structure” and

“an increase in the use of mezzanine financing combined with higher-cost senior debt.”

Mezzanine debt could play a critical role in the refinancing of approximately \$1 trillion in precrisis loans that are scheduled to mature in 2014 through 2016. A manager of a high-yield fund predicts that this debt will be refinanced with a combination of senior and structured debt, including about \$200 billion in mezzanine loans. Although “the low-hanging fruit has already been taken,” if this refinancing occurs, it will prove that the practice of lenders to “extend and pretend” real estate loans that matured after 2008 will have had the desired effect of stabilizing the debt capital market, says an investment adviser. As for loans that will not be refinanced, “extend and pretend” could remain in effect, possibly demonstrating that fundamentals have improved to a point where lenders are comfortable with retaining a certain portion of those loans.

Shadow Banking

Such demand for debt capital could remain great enough for opportunities to proliferate in the so-called shadow banking industry. In a secular trend, shadow banking—that is, the commercial lending market outside of the regulated universe of insured depository institutions and life insurance companies—may continue to shape up as “a force to be reckoned with,” says a fund manager. Widely considered an inevitable response to concerted efforts by regulators to constrain a wide range of

EXHIBIT 2-14

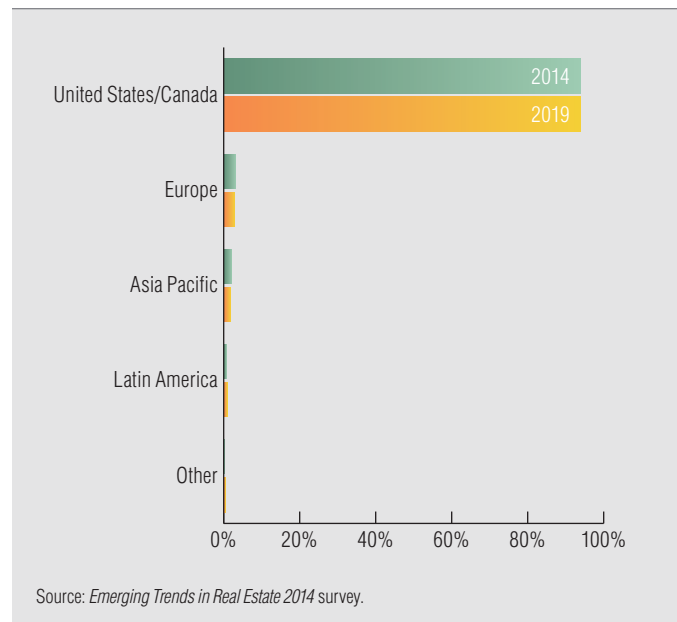
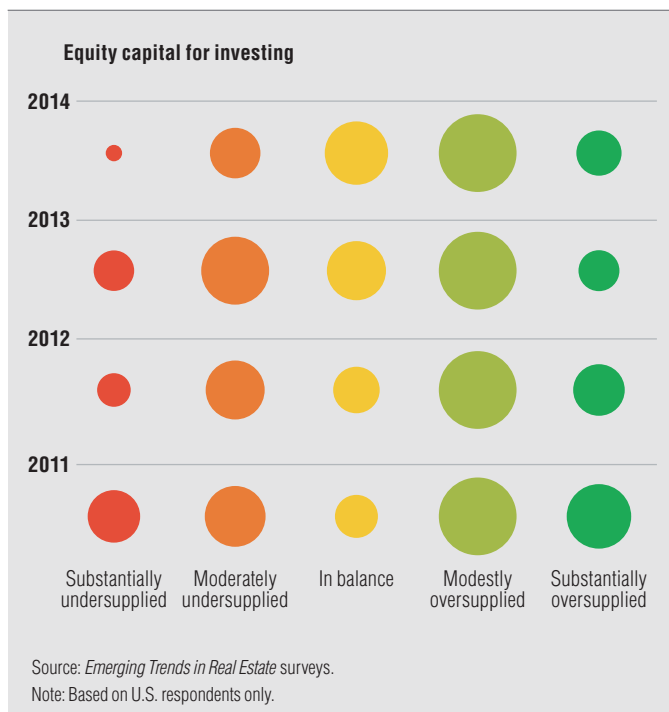
Percentage of Your Real Estate Global Portfolio in World Regions

EXHIBIT 2-15

Real Estate Capital Market Balance Forecast



operations by financial institutions, the growth of the shadow banking market should continue to accelerate. While its size remains impossible to estimate, many interviewees agree that the shadow banking market will serve to direct borrowers who need capital away from traditional lenders and toward the growing number of private equity funds, REITs, and other entities that will increasingly step forward to meet the demand for capital that is expected to grow in 2014.

Private equity companies have been “taking much more exposure to the debt market” since mid-2012, says a global investment manager. “They are raising phenomenal amounts of money. So it’s going to be a much more competitive marketplace.” As of April, there were 37 solely debt-focused closed-end private real estate funds operating worldwide, and they had raised a total of \$35 billion since 2007, according to Preqin.

“Financial organizations that are not traditional banks are starting to make loans again in a significant way,” says a fund manager. “It’s not back to where it was, but starting to trend that way.”

Equity Sources Expand

The outlook for capital availability from a wide range of equity sources is expected to improve in 2014. According to the survey respondents, availability of equity capital will increase the most from foreign investors, followed closely by the following: pension funds and other large institutions; private equity funds, hedge funds, and opportunistic funds; and private local investors.

Many interviewees expressed the opinion that commercial real estate will get a lot more “institutional” in 2014 and the years beyond. “Availability of capital will be good,” explains a fund manager. “It’s dramatically better than it was three or four years ago, and a little better than a year ago. But as people rotate out of the bond market and into equities, where does the capital go? Real estate ownership is becoming more institutional. It will become more routine, more liquid, more accurately priced.”

Foreign Investors

A recent survey of foreign investors by the Association of Foreign Investors in Real Estate (AFIRE), which is made up of nearly 200 “investing organizations” in 21 countries, found that 81 percent of respondents “intend to increase their portfolio of assets in the U.S.,” which “is perceived to provide a stable environment in which to invest and is the best market for capital appreciation.” Specifically, 71 percent “believe economic fundamentals had improved to the point that makes secondary cities [as opposed to ‘core’ gateway cities] in the U.S. worth looking at for new real estate acquisitions.”

In what some interviewees interpret as a secular trend, foreign investors are clearly on a shopping spree. From January to August 2013, they acquired \$22.8 billion in U.S. real estate, which accounted for 13 percent of all real estate transactions in the country, up from 9 percent in 2012, according to Real Capital Analytics. Over the last three years, the biggest investor was Canada, followed by China and countries in the Middle East. “Over the next ten years, we will see a continuing trend toward more foreign capital coming in,” says an investment manager. As an example, two unrelated South Korean investment funds bought two office buildings in Houston in early 2013, one of which a real estate service provider described as a “double A Class property” for its location and other attributes.

Foreign capital, whether from sovereign wealth funds, high-net-worth individuals, or other sources, should continue to increase. The irony is that foreign investment is pouring into the United States despite delays in long-awaited reform of the Foreign Investment in Real Property Tax Act (FIRPTA). “This would increase further if FIRPTA were changed. Yet even in the absence of such changes in those foreign investment tax laws, there is evidence of a lot more foreign capital coming into the U.S.,” says an investor and builder in a secondary market.

EXHIBIT 2-16

Foreign Net Real Estate Investments in the United States, by Buyer Origin, 2009–2013

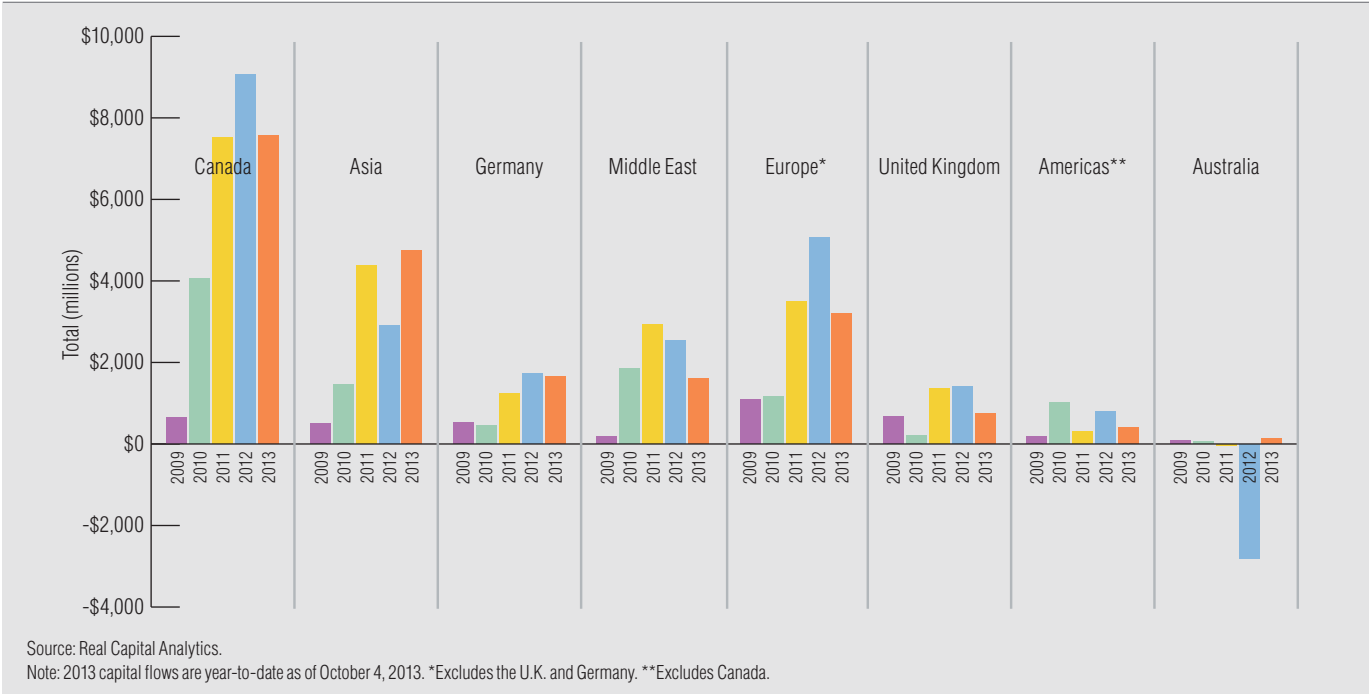
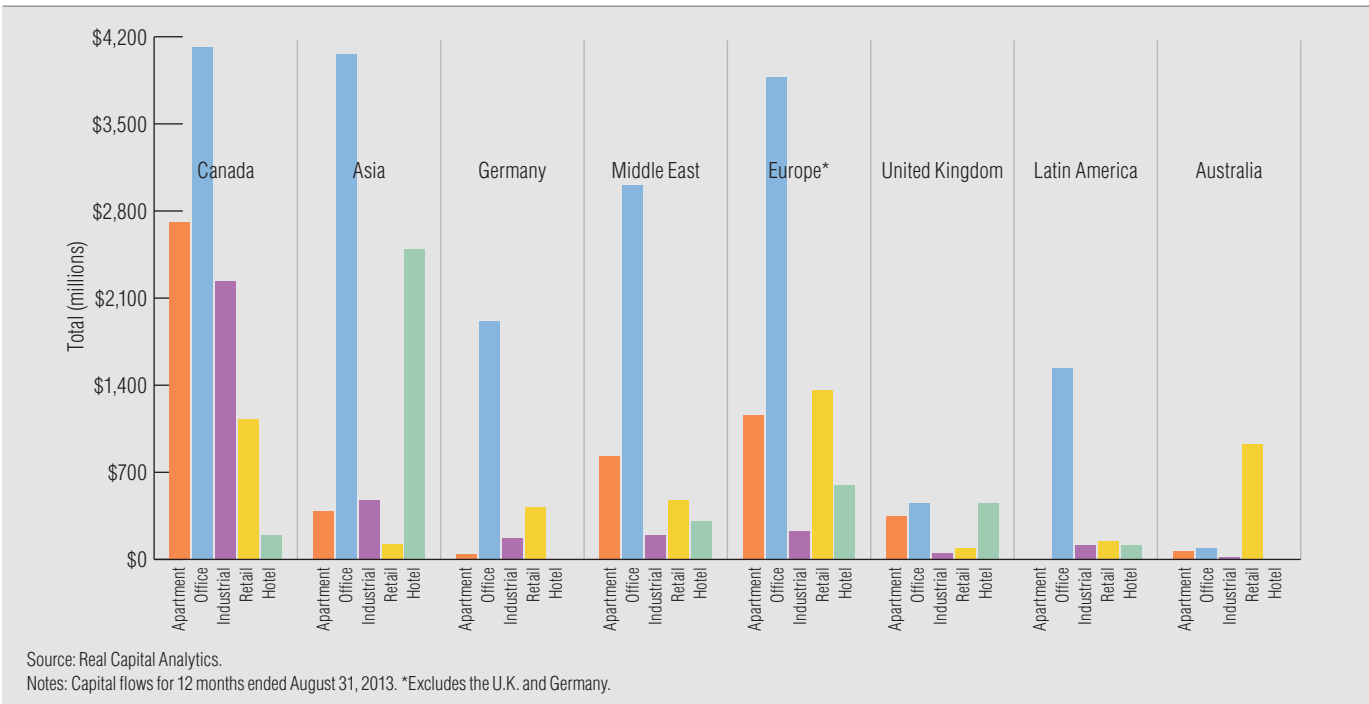


EXHIBIT 2-17

Foreign Real Estate Investments in the United States, by Buyer Origin and Property Type



In the eyes of some American investors, however, the grass will look greener on the other side of the Atlantic Ocean. In 2014 and 2015, U.S. investors may adopt a new pattern of investing in real estate in Europe, where bids for the highest-quality core properties have risen so high that they have been “temporarily priced out of core,” says an investment manager. When Europe’s economic crisis bottoms out, it could “give investors the courage to say, ‘I’m going to stop bidding on the highest-quality stuff, and I’m going to bid on these properties that used to be core in the expectation that they may return to core pricing in the next several years.’”

Private Equity

In domestic U.S. investments, private equity investors should still be able to afford to leverage their investments heavily—even as interest rates rise—while structuring deals with about 30 percent equity, says a global investment manager. “We are seeing more participation in the real estate market on the part of traditional private equity firms,” says a real estate investment manager. Some investors could pursue a strategy of “platform buying” in which they will buy operators to serve as a launch pad for a funded investment strategy. But an investment manager says, “more of them are expanding their existing mandate and participating directly in the purchase of property through joint ventures with operating companies as opposed to buying the company.”

After having spent billions of dollars to buy tens of thousands of foreclosed single-family houses in 2012 and 2013, private equity shops may emerge among the largest categories of rental landlords. Such assets “are so completely accepted as an asset class by the same institutional investors who abhorred

the idea of collecting rent from people before the financial crisis that they are even investing in secondary markets,” says a fund manager. In what amounts to the institutionalization of the U.S. single-family rental housing market, private equity shops look to grow income by leasing to individuals who would have bought homes before the recession but are now delighted to be renters, having learned that “it’s a fallacy that paying rent is throwing away money” in the domestic context of servicing a mortgage, explains the fund manager. As few investments have gone full cycle, it is too early to determine whether this is a long-term business opportunity or a short-term trade.

Overall, the private equity market appears to be bifurcating between the global private equity funds that appear to be able to raise significant amounts of capital and the more local or regional firms who appeal to investors seeking smaller allocations to the asset class.

Pension Funds

Among pension funds, growth in real estate investing may not come solely from defined-benefit plans, however. According to *Pensions & Investments*, defined-benefit plans invest about 6.5 percent of their \$3.8 trillion worth of assets in direct real estate, but they are shrinking every year as corporate plan sponsors “soft-close” or shut them down altogether. A potential new player for real estate is defined-contribution plans, which grew to reach \$3.8 trillion—on a par with defined-benefit plans—at the beginning of 2013 as plan sponsors launched new ones. Defined-contribution plans currently invest only \$11 billion in direct real estate.

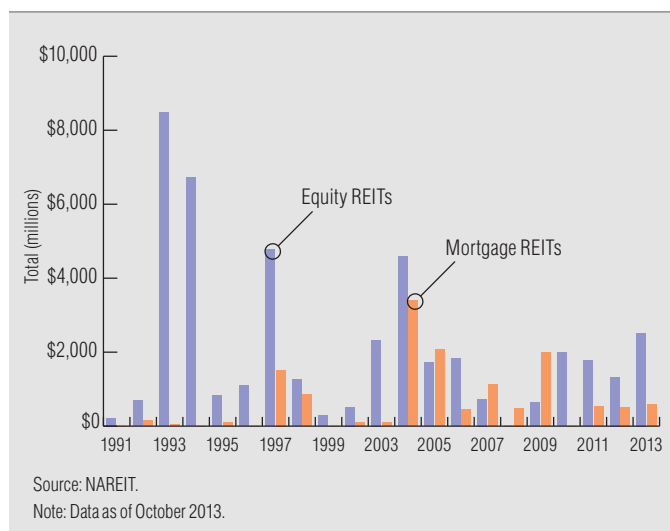
In May, the firms formed a new consortium—the Defined Contribution Real Estate Council (DCREC)—with a mission to “more than double” defined-contribution plans’ allocation to direct real estate, according to several interviewees. “Defined-contribution plans are coming alive. Target date funds will play a big role,” says a fund manager.

Equity REITs

Public equity REIT capital could be very active in 2014 as REITs deploy the unprecedented amount of capital that they have raised in less than two years. Equity REITs raised \$51.3 billion in 2011, \$73.3 billion in 2012, and another \$40.5 billion in the first five months of 2013 before the REIT market corrected this past summer. To hear one fund manager tell it, the selloff was triggered by Federal Reserve Board Chairman Ben Bernanke’s discreet hints that the end of quantitative easing was near, which scared away yield chasers. “REITs had such a run because a lot of people were buying just for dividend yield. It was not necessarily anything to do with real estate,” says one REIT executive.

The number of publicly listed equity REITs increased from 128 in July 2012 to 143 in September 2013 thanks to a flurry of

EXHIBIT 2-18
REIT IPOs Capital Raised, by Sector



initial public offerings (IPOs). The new REITs are highly innovative, investing in income streams no less exotic than cellular telephone towers and parking spaces, thereby redefining what qualifies as real estate. “REITs continue to do all the right things: deleverage, sell underperforming property, cautiously develop new property, raise equity, and improve lines of credit,” says a commercial real estate developer.

As a result, higher interest rates would likely have no impact on the credit ratings of REITs because “their metrics have been consistently getting better,” an analyst explains. “Some might have their fixed charges go up, but their net debt to EBITDA [earnings before interest, taxes, depreciation, and amortization] is going to go down.” So they are expected to continue to raise debt in the bond market in 2014. “There is an incredible amount of bond issuance going on in anticipation of companies’ thinking interest rates will go up,” the analyst noted. REITs raised \$14.94 billion in 43 unsecured debt issuances from January 1 to July 31, 2013, compared with \$25.73 billion for the full year of 2012, according to the National Association of Real Estate Investment Trusts (NAREIT).

The question is whether the market for direct real estate investments will follow the REIT market in 2014. For the last two decades, the NCREIF Index has directionally followed the FTSE NAREIT U.S. Real Estate Index in broad brushstrokes with a time lag of less than a year. “It is scary how the REIT index forecasts the NCREIF index,” says a fund manager. “The REIT index has dropped off this year. That would suggest the NCREIF [index] could drop off next year.”



Markets to Watch

“Find the right market and the right partner, execute quickly, don’t miss an opportunity—and **invest one deal at a time.**”

The pace of the economic and real estate recovery remains uneven across U.S. metropolitan-area markets. The recovery has clearly had more momentum in markets with favorable demographics, exposure to growing industry sectors, and those with an attractive cost of doing business. These trends have been in place since the recovery began, but to the benefit of the overall market, they are now expanding to a larger market set. Survey respondents in 2013 expressed a desire to move into secondary markets in search of higher yields. The desire was clearly there in 2013, but 2014 may well be the year when we will see these plans come to fruition. One fund manager notes, “The focus is now on top 25 markets, not the top six. We like markets that have the potential for growth.”

The growing number of investors will be looking for investments to place a growing amount of capital. The top investment markets of the past few years are still attractive and will continue to appeal to investors with certain return targets, but the desire to place capital and earn a higher return has investors even more willing to explore opportunities in a wider swath of potential markets. While this was the same sentiment as last year, what makes it more likely to occur in 2014 is that the pace of market fundamental improvement is now viewed as being sustainable, so the economics of the investments are now meeting more investor risk/return metrics. A national portfolio manager stated that “the outlook for a broader number of markets is that improved demand will create the kind of leasing momentum that will allow landlords to push rents.”

2014 Market Ranks

Throughout this report, we have talked about this being the year when investors finally get serious about increasing investment

levels in secondary markets. The overall rank of markets by survey respondents shows some changes that would seem to indicate that this will happen in 2014.

The top five markets remain virtually unchanged with only some moderate reshuffling. San Francisco maintains the number-one position in the overall rankings. This tech-influenced market is also attractive to young workers, and with meaningful supply constraints in place, its location at the top is no surprise. Houston jumped three spots to number two in 2014. Houston’s booming energy economy has fueled an active real estate market over the past few years, and survey respondents expect that to continue in the coming year. Two Texas markets switched places in the top five from 2013. Dallas/Fort Worth jumped up four spots to number five, while Austin slipped three spots to a still-respectable number seven. It is possible that survey respondents see these two markets enjoying many of the same economic drivers, but the much larger investable universe in Dallas/Fort Worth was enough to make it slightly more attractive.

Other notable moves driven by trends for 2014 is the move of Miami into the top ten at number eight. Survey respondents moved Miami up from number 12 in 2013. This is a significant improvement for a market that was hard hit by the bursting of the housing market bubble. Miami is an attractive destination for foreign capital and remains a very appealing destination for younger residents. Other positive moves were made by markets that were hit by the housing meltdown. Las Vegas jumped 12 spots to move from near the bottom in 2013 to number 38, and Phoenix improved eight spots to number 25.

Perhaps the only possible sentiment that could have removed San Francisco from the number-one spot would have been survey respondents’ feeling that the market had peaked. This may have been behind a few markets making negative

EXHIBIT 3-1

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

	Investment	Development	Homebuilding
1 San Francisco (2/1/1)	6.98	6.88	7.74
2 Houston (1/3/2)	7.00	6.64	7.48
3 San Jose (5/2/3)	6.78	6.75	7.40
4 New York City (3/4/6)	6.84	6.58	7.19
5 Dallas/Fort Worth (6/6/4)	6.76	6.37	7.36
6 Seattle (4/7/7)	6.83	6.36	7.19
7 Austin (7/10/5)	6.69	6.25	7.34
8 Miami (10/5/8)	6.57	6.38	7.06
9 Boston (8/8/9)	6.64	6.35	6.87
10 Orange County, CA (9/12/10)	6.60	6.17	6.85
11 Denver (13/14/11)	6.46	6.15	6.84
12 Nashville (14/11/15)	6.46	6.18	6.75
13 Los Angeles (15/13/17)	6.45	6.15	6.70
14 San Antonio (19/16/12)	6.28	6.10	6.79
15 San Diego (12/19/16)	6.47	5.91	6.71
16 Charlotte (17/18/13)	6.37	5.92	6.79
17 Raleigh/Durham (18/20/14)	6.31	5.90	6.79
18 Salt Lake City (16/17/19)	6.42	6.03	6.54
19 Portland, OR (11/21/25)	6.53	5.88	6.28
20 Minneapolis/St. Paul (20/9/26)	6.27	6.27	5.91
21 Chicago (22/15/27)	6.11	6.11	5.89
22 Washington, D.C. (26/26/18)	5.88	5.46	6.54
23 Tampa/St. Petersburg (24/22/23)	5.97	5.59	6.30
24 Orlando (25/23/21)	5.89	5.56	6.40
25 Phoenix (21/28/24)	6.14	5.41	6.29
26 Atlanta (23/27/22)	6.05	5.43	6.33
27 Northern New Jersey (28/31/20)	5.85	5.25	6.40
28 Inland Empire (27/24/28)	5.87	5.53	5.73
29 Honolulu/Hawaii (29/25/30)	5.68	5.46	5.56
30 Philadelphia (30/33/31)	5.56	5.04	5.56
31 Indianapolis (34/29/35)	5.33	5.33	5.40
32 Pittsburgh (31/37/37)	5.55	4.90	5.29
33 Westchester/Fairfield (33/39/33)	5.48	4.82	5.43
34 Virginia Beach/Norfolk (36/36/29)	5.21	4.91	5.58
35 Kansas City (35/30/43)	5.28	5.28	5.11
36 St. Louis (37/32/42)	5.18	5.18	5.13
37 Baltimore (38/40/36)	5.15	4.74	5.31
38 Las Vegas (32/43/41)	5.49	4.44	5.15
39 Jacksonville (42/42/34)	4.96	4.64	5.42
40 Sacramento (40/44/32)	5.05	4.43	5.53
41 Cincinnati (41/34/44)	4.98	4.98	4.92
42 Columbus (43/35/46)	4.94	4.94	4.81
43 Oklahoma City (45/41/39)	4.82	4.67	5.18
44 Tucson (39/47/38)	5.14	4.28	5.19
45 Milwaukee (44/38/47)	4.83	4.83	4.70
46 Albuquerque (46/45/40)	4.65	4.33	5.18
47 New Orleans (48/46/45)	4.49	4.30	4.83
48 Memphis (47/49/48)	4.52	4.07	4.49
49 Cleveland (50/48/50)	4.20	4.20	4.00
50 Providence, RI (49/50/49)	4.30	3.66	4.30
51 Detroit (51/51/51)	3.12	3.12	2.96

Source: *Emerging Trends in Real Estate 2014* survey.

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

moves from 2013. Washington, D.C., and northern New Jersey recorded the largest decline in rankings in 2014. Each of these markets fell 14 spots. This is a particularly sharp drop for Washington, D.C., given that only a few years ago it was the number-one market in the survey. Washington, D.C., was a favorite of survey respondents during the economic downturn and the early stages of the recovery. The consistency provided by the federal government sector supported the market while other markets dealt with falling employment. However, what was once viewed as an asset is now viewed as a liability. The Washington, D.C., market may well be suffering from “fed fatigue” as weariness over a government shutdown and uncertainty over the future of government spending, even when combined with a healthy supply pipeline, have made market participants cautious about the prospects for returns.

Investment Prospects Continue to Improve

Survey respondents and interviewees alike have an improved outlook for the 2014 performance of a growing number of markets. Exhibit 3-2 illustrates the improvement that survey respondents see in the investment prospects for the market set. At the depth of the Great Recession, no market was scored high enough by respondents to warrant a rating of “good or better.” The recovery began slowly in 2011 and has steadily improved each year during the recovery. In fact, 2014 will again be a year when more survey respondents see the investment prospects

EXHIBIT 3-2

Historic Real Estate Prospects: Good or Better vs. Poor or Worse Ratings for 2004–2014

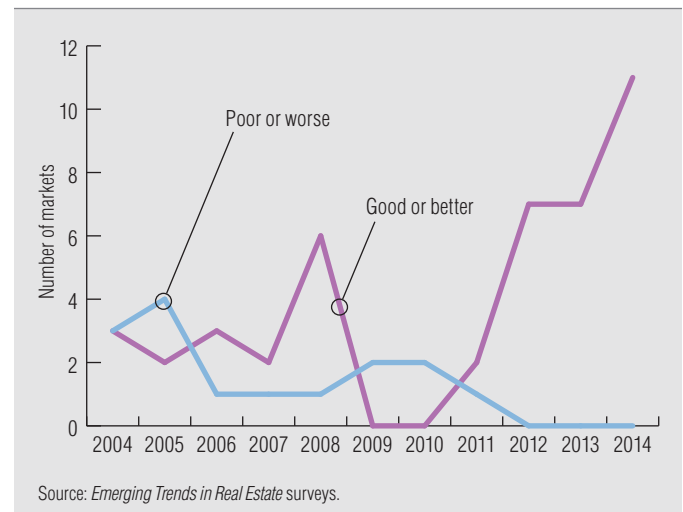
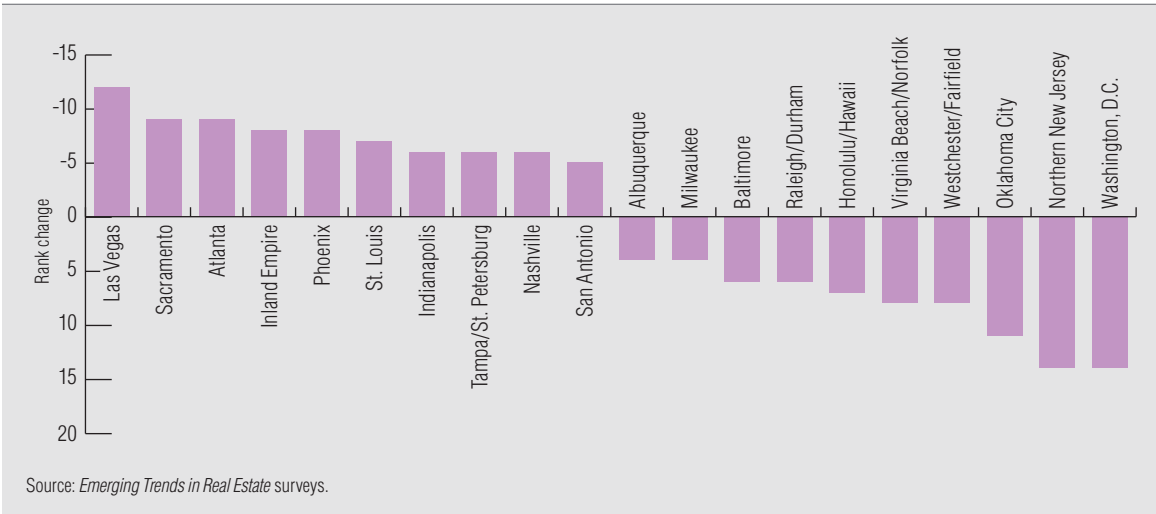


EXHIBIT 3-3

Emerging Trends Overall Real Estate Prospects Rank, Change from 2013



as “good or better” in nearly twice as many markets as was the case at the most recent peak in 2008.

Survey respondents not only have a better view of the investment prospects for a larger set of markets, they are also starting to look at markets that are clearly outside the core set favored during the early years of the recovery. A look at the progression of markets over the past four surveys in Table 1 reveals how sentiment has moved from only preferring the ultra-core New York and Washington, D.C., to a broader set of core markets that includes San Francisco and Boston along with tech- and energy-centric markets Austin and Seattle. In 2014, the set of markets with a “good or better” outlook for investment prospects includes representatives from each of the aforementioned categories, but becomes more diverse. Dallas/Fort Worth, with its strong economic recovery that is driving real estate activity, makes the list. Markets previously beaten down by the housing market collapse—Miami and Orange County, California—have improved expectations for 2014. Portland, Oregon, represents a couple of emerging trends by making the list. Portland represents a market that not only has a technology component, but also is very attractive to residents who are in search of the urban lifestyle.

An Increase in Development May Be on the Horizon

The outlook for development improved for the second straight year, and perhaps more important the average outlook for development is considered “fair” and barely misses being considered “modestly good.” The current rating is an improvement from two years ago, when the average outlook was “modestly poor.” The improvement in the development outlook is distributed across a

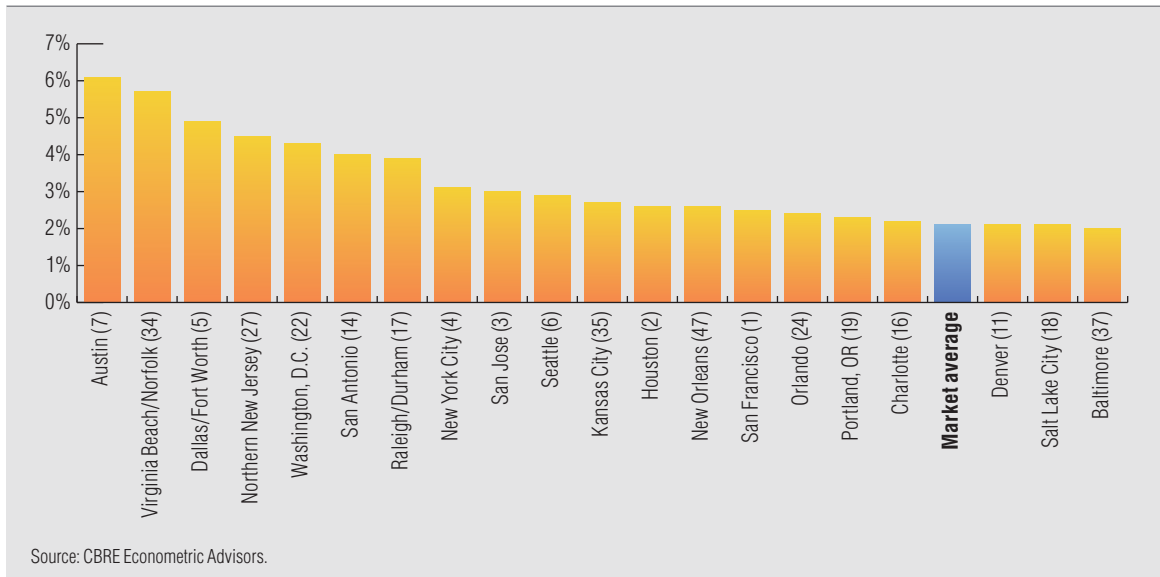
number of markets, with 40 markets reporting an improvement in development prospects for 2014. The uptick in the outlook for development, however, does not mean that the market will be flooded with new supply in the near future. In a number of markets the sentiment did improve, but the overall rating still remains below fair. For example, Las Vegas saw the largest score increase, but the overall rating is still considered to be “modestly poor.” Conversely, a negative change in development sentiment may actually be a good indicator. Austin recorded a slightly negative change in the prospects for development, but the overall rating remains one of the highest in the survey and is

TABLE 1
Markets with Investment Prospects Good or Better

2011	2012	2013	2014
New York	Austin	Austin	Austin
Washington, D.C.	Boston	Boston	Boston
	New York	Houston	Dallas/Fort Worth
	San Francisco	New York	Houston
	San Jose	San Francisco	Miami
	Seattle	San Jose	New York
	Washington, D.C.	Seattle	Orange County
			Portland
			San Francisco
			San Jose
			Seattle

EXHIBIT 3-4

2013 Space under Construction as a Percentage of Inventory



considered “modestly good.” The decline in the development outlook for these markets could mean that survey respondents are being more cautious about future activity.

Market fundamentals have improved to a point where new supply is underway in a rising number of markets. Exhibit 3-4 lists the top 20 markets ranked by the amount of new supply as a percentage of total inventory under construction. With the exception of a few outliers, new supply is concentrated in the top 20 markets. The rise in new supply in these markets is not surprising, as fundamentals have improved or are expected to reach a level where they can support these higher levels of new supply. One developer notes, “When supply ramps up, it may well catch the market by surprise. We could see real shortages of labor and commodity inputs to keep up with the higher levels of building.”

Housing Market No Longer a Drag on Growth

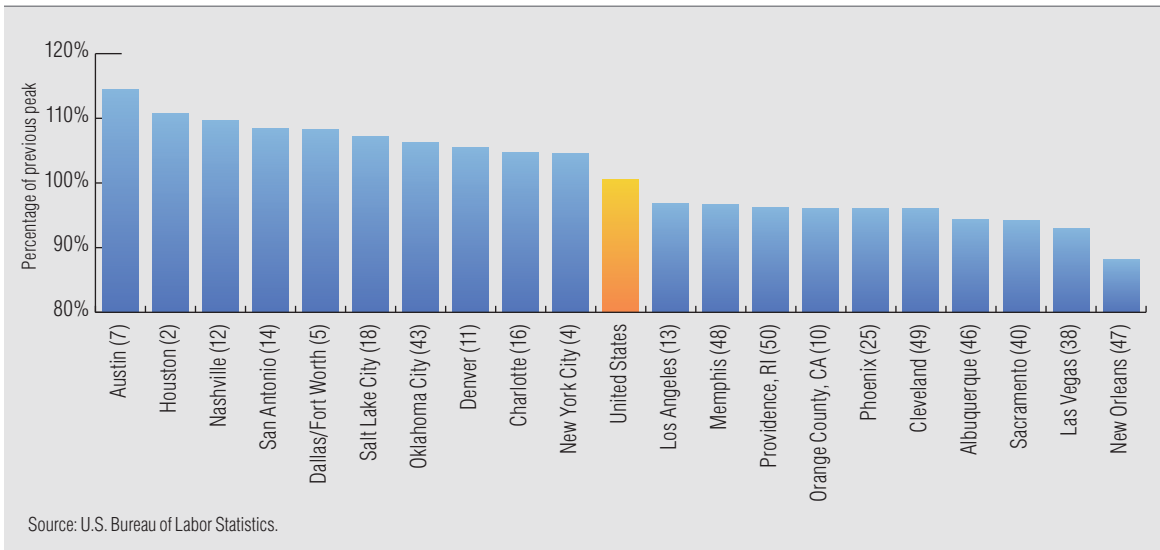
Single-family housing is no longer a drag on most market economies, and the prospects for homebuilding in 2014 improved in all 51 markets. The average outlook improved from fair to modestly good over the past year. Two years ago, survey respondents saw the single-family market outlook as modestly poor and it was a definite headwind to economic recovery. The top markets in our survey are also those where respondents see the best potential for homebuilding. The heavily

tech-oriented markets—San Francisco and San Jose—are at the top of the homebuilding outlook. A national condominium developer notes, “The demand for housing in the Bay Area has improved with a vengeance. The improvement in the tech market is causing a surge in demand.” The improvement in the outlook for homebuilding is not just limited to higher-cost housing markets. A strong local economy is also driving expectations in more affordable markets such as Dallas/Fort Worth, Houston, and Austin.

The breadth of the recovery in the single-family market has moved beyond a simple rebound in prices to include rising demand based on household formations to an expected increase in the construction of new homes. Thirteen markets will have fully recovered to peak price levels by the end of 2014, according to Federal Housing Finance Agency (FHFA) conventional and conforming mortgage data. These data remove the influence of distressed home sales and cash buyers and point to a diverse set of markets, including those with more stable economies, like Pittsburgh and Columbus, Ohio, to those that have faster economic growth, such as Denver and San Antonio. Strong household growth is again expected in a familiar set of markets led by several in the state of Texas along with Las Vegas, Charlotte, and Portland. The result is that housing starts are projected over the next five years to rebound back to levels similar to those seen in the previous cyclical peak.

EXHIBIT 3-5

Employment Recovery from Previous Peak through 2014



Employment

By the end of 2014, employment levels in over half of the markets in the survey will be back to their pre-recession peak. What this means is that additional employment from this point could be accretive to positive real estate demand. Exhibit 3-5 shows the correlation between market position in the survey and employment recovery. The top markets in regard to employment recovery, with the exception of Oklahoma City, are all ranked near the top of this year's survey. The markets at the bottom of the survey show that a lack of employment is typically a deterrent to real estate performance. The exception to this group is Phoenix, which has recently shown signs of improvement and is ranked number 25 in this year's survey.

Employment growth is projected to continue to improve. A similar analysis shows that by 2016, only a handful of markets will still have employment levels below the pre-recession peak. With employment now growing from peak levels and the limited amount of new supply that has been delivered during the recovery, it is easy to see why the outlook for real estate fundamentals is positive. A portfolio manager notes, "The current condition of the real estate market sets up well for any type of upside surprise in employment growth."

Population and Demographics

Population will continue to play a role in how the recovery plays out in a number of markets. Total population growth, net migration, and growth in influential age cohorts will all shape the future

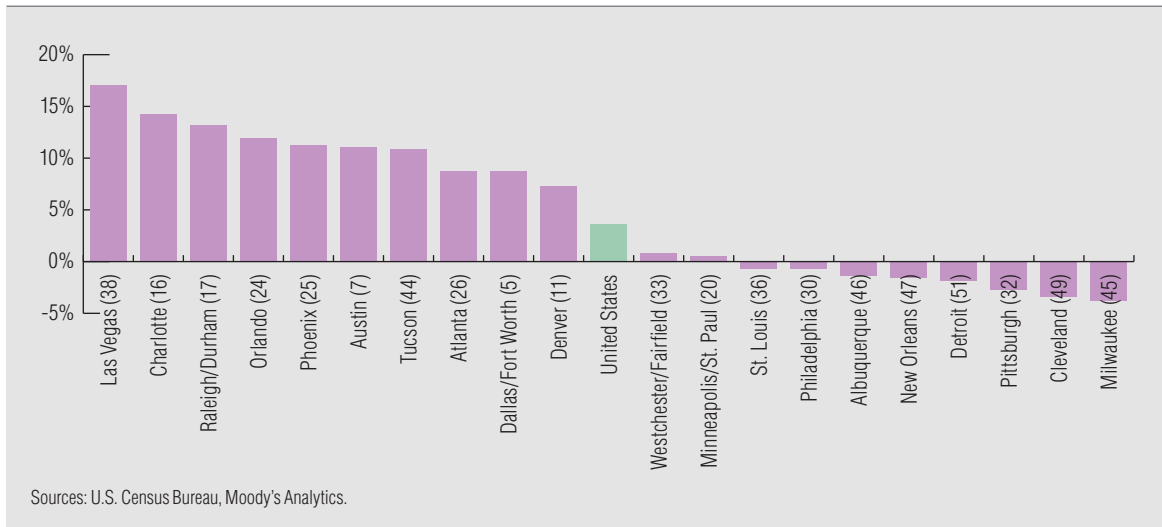
real estate recovery. Cleveland, Pittsburgh, and Detroit are the only markets projected to experience negative total population growth in 2014. The highest rate of population growth is expected in the Texas markets, where population growth is again expected to occur at a rate more than double the national average. The recovery in Las Vegas and Phoenix will get a boost from strong population growth as these two markets will have the highest rate of growth in the survey.

Net migration will benefit a number of markets over the next few years. The recovery in the single-family housing market should make it easier for workers to be more mobile. If you are confident you can sell your house without taking a devastating loss, you are going to be more willing to move for employment reasons. The ability of markets to attract workers from other places could really boost employment growth. Dallas/Fort Worth and Phoenix are projected to benefit the most from net migration, with each market projected to attract more than 78,000 new residents each year.

The real estate industry is clearly interested in the impact of the millennial generation, the largest generation since the baby boomers. "The growing influence of this generation and their impact on how business is conducted and where it is conducted could well be the most significant trend in real estate for many years," notes an institutional investment adviser. It is projected that this group will affect not only how space will be used, but also where it will be used. Exhibit 3-6 shows where this age cohort will see the largest rate of growth over the next five years. It is not a coincidence that being attractive to this age group is occurring in markets that rank near the top of the survey.

EXHIBIT 3-6

Five-Year Projected Growth in Population Age 20–34



A market does not necessarily need to be in the top ten in terms of growth to benefit from the impact of the millennial generation. A number of markets that are projected to have lower rates of overall population growth will still see a significant increase in millennial population growth. Markets such as San Francisco, New York, Chicago, Washington, D.C., and Atlanta are projected to have average to below-average total population growth, but will see much stronger growth in the 20-to-34-year-old population.

Low-Cost and High-Production Markets Continue to Outperform

“Even as the economy improves, look for companies to remain extremely focused on costs,” observes a national real estate service provider. A number of interviewees expressed the opinion that firms are going to be very cost conscious even after the economy improves. A focus on costs is believed to be part of the reason why the Texas markets have

been steadily improving in the survey. The comparatively lower cost of doing business and perceived business-friendly environment are making Texas an attractive alternative for companies looking to either expand or even relocate.

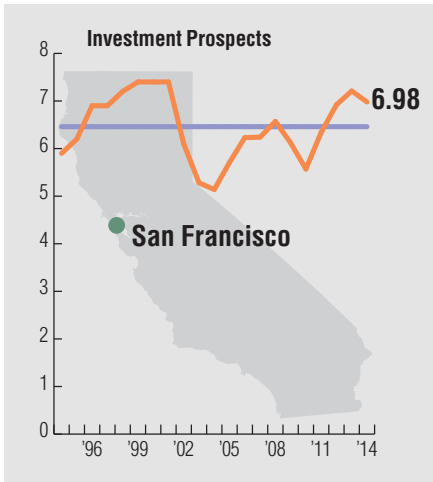
Low cost is not the only factor influencing real estate market improvement. Eight of the top ten markets in this year's survey have some of the highest costs of doing business. These high costs are offset by higher levels of productivity that can be achieved in these markets. Seven of these markets have gross metro product-per-capita rates that are significantly above the U.S. average. As long as there are benefits in either more efficient production or higher workforce retention, markets such as those in northern California, New York, and Boston will remain attractive to real estate investors.

The Top 20 Markets

San Francisco (1). For the second year in a row, San Francisco is the top-ranked market in the survey. The number-one ranking isn't dependent on one variable, as San Francisco was ranked first

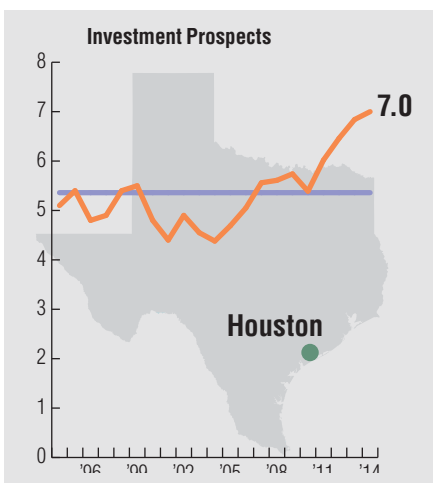
for homebuilding prospects, third for development, and first for investment. Survey respondents find the prospects for this market to be “good” for investment and development and “very good” for homebuilding prospects. San Francisco was one of the most mentioned markets in this year's interviews. A portfolio manager of a large state pension fund sums it up: “Capital is plentiful and money is even available for new projects, [with] a lot of due diligence. We really like the big cities—New York, San Francisco are the top markets for all investment types.”

Despite being one of the most expensive markets in which to live and do business, San Francisco will see its economy continue to thrive in 2014. The economy is projected to add jobs at a 2.0 percent rate for the year. The thriving economy is boosting net migration, with 36 percent of new residents moving into the metro area. San Francisco's high costs are offset by high productivity levels, with gross metro product projected to grow at a 4.2 percent rate next year. Stronger production is expected to contribute to a growth of 5.5 percent in personal income.



According to survey respondents, San Francisco is a solid “buy” for all property types. The “buy” recommendation for each property is higher than the average for each of the major markets. Respondents feel particularly good about hotels in San Francisco.

Houston (2). The second-highest market in this year’s survey, Houston improves from its number-five position in last year’s survey. Investment and homebuilding prospects are responsible for Houston’s number-two ranking. Houston is the top-rated market for investment and the second-highest-rated market for homebuilding prospects. Respondents find the prospects for all three components to be “good.” An institutional investor sums up



the benefits of Houston: “Houston is on fire right now; we don’t see it letting up.”

Houston will continue to expand at a strong and steady pace in 2014. Housing, nonresidential construction, and a revival in exploration industries will be the key economic drivers. Employment gains are projected to come from related manufacturing and professional services, as large companies relocate more of their headquarters operations to Houston. Over the longer term, above-average population growth and expansion in energy, health-related, and distribution industries will help propel above-average economic growth.

Houston is an overwhelming “buy” based on survey respondents. The Houston buy recommendations for all five property types are well over the average

for the top markets. The buy ratings put Houston in the top three out of 15 markets for all property types.

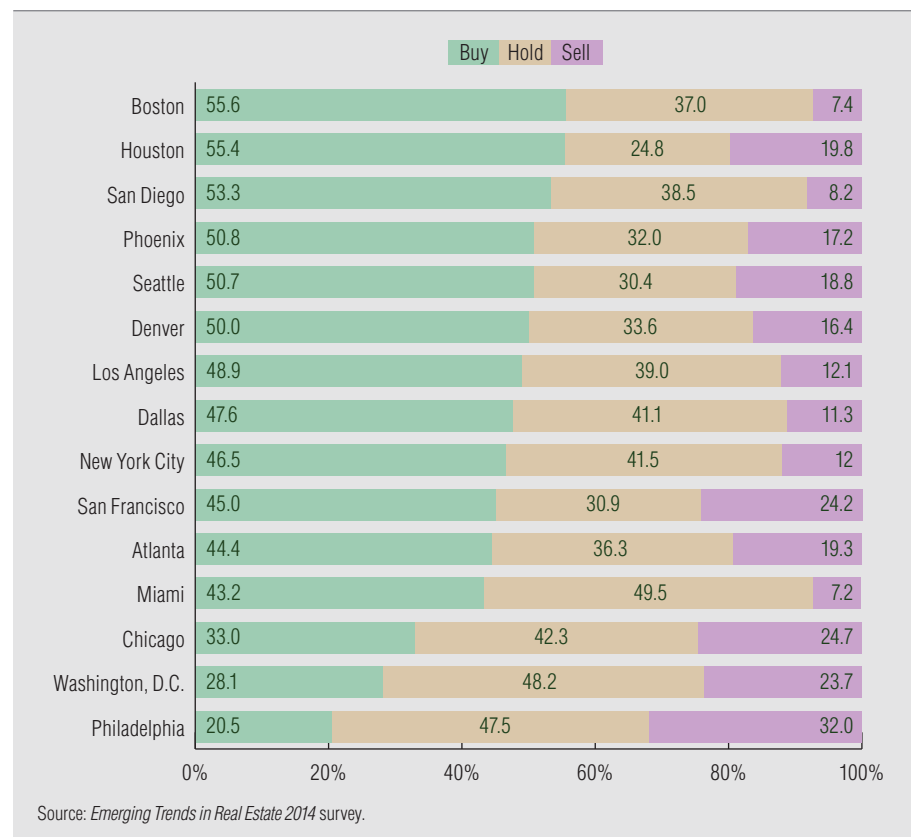
San Jose (3). San Jose is the third-ranked market for the second year in a row. It scores well in all three components, with the investment and development prospects both ranked fifth and the homebuilding prospects third. Respondents see the outlook for each component to be “good” in 2014.

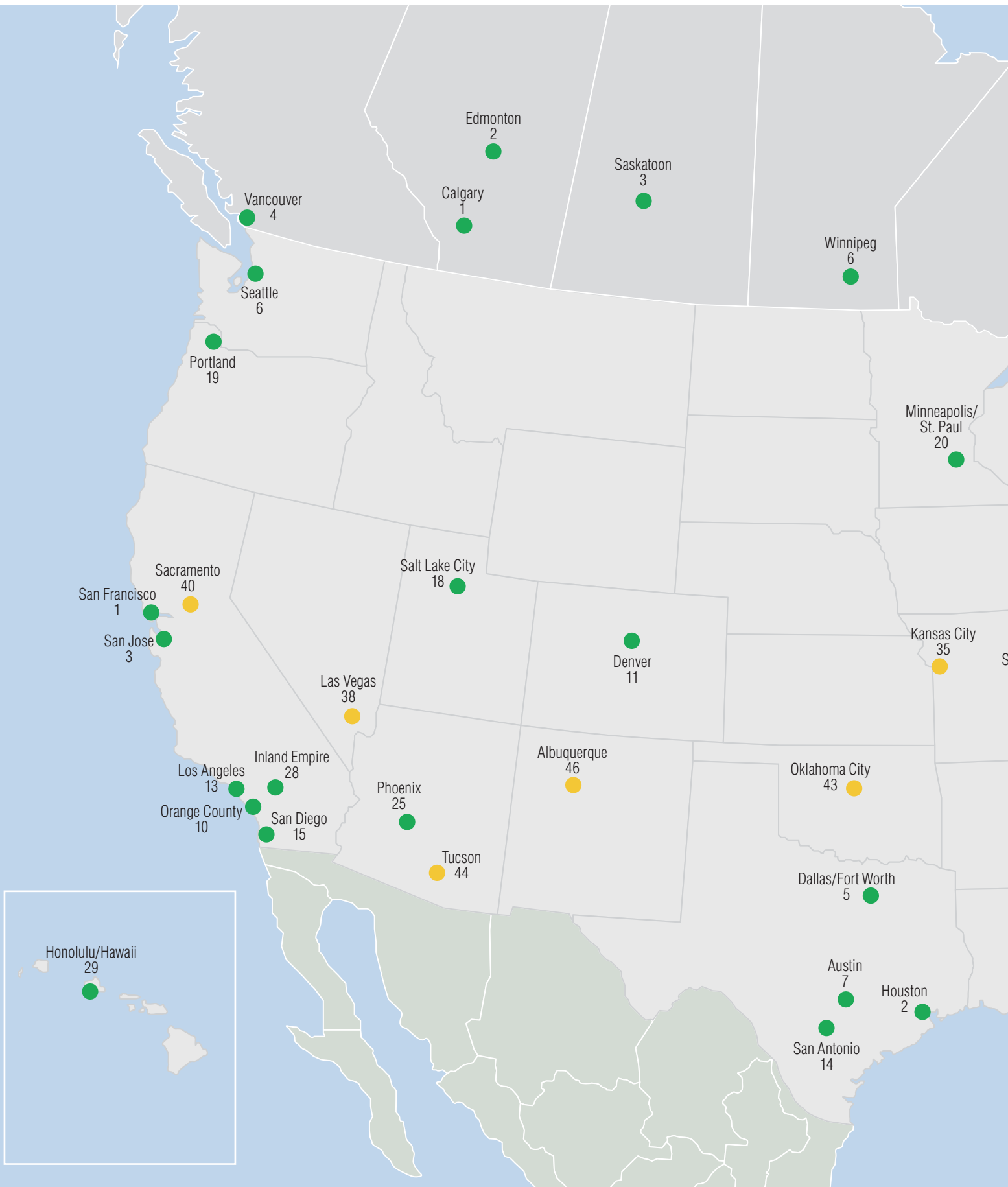
This year’s interviewees are all attracted to San Jose’s technology industry. They feel that the job and income growth generated will support rising real estate demand. They are, however, very aware of the potential risks of the market overbuilding.

The breadth of San Jose’s economic growth should broaden in 2014. Despite

EXHIBIT 3-7

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





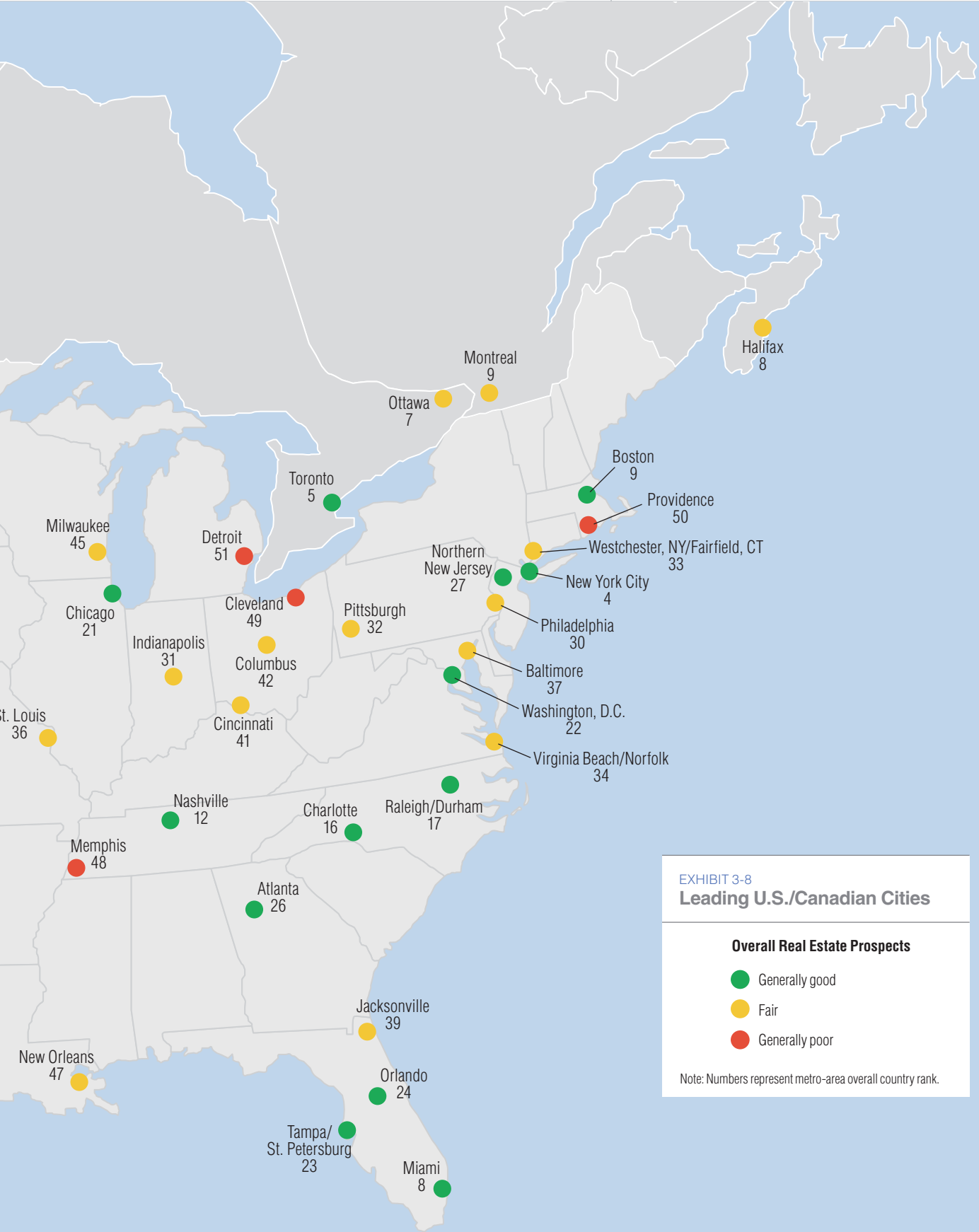


EXHIBIT 3-8
Leading U.S./Canadian Cities

Overall Real Estate Prospects

- Generally good
- Fair
- Generally poor

Note: Numbers represent metro-area overall country rank.

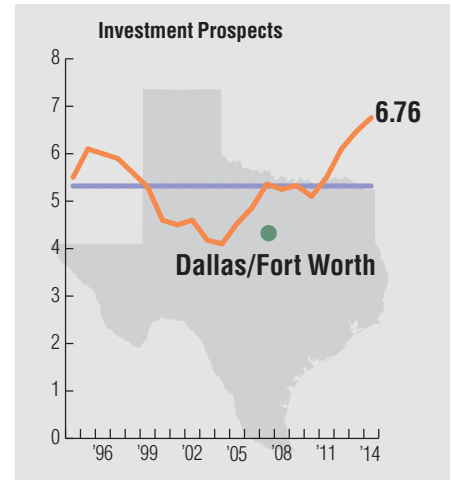
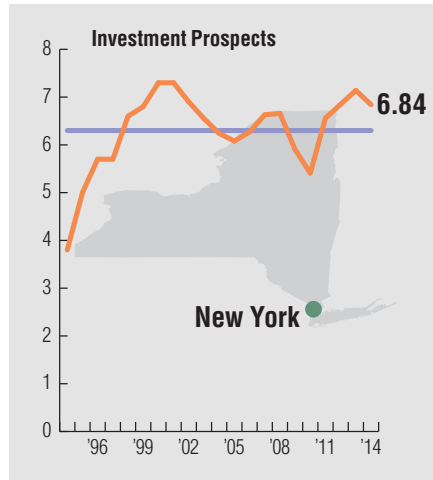
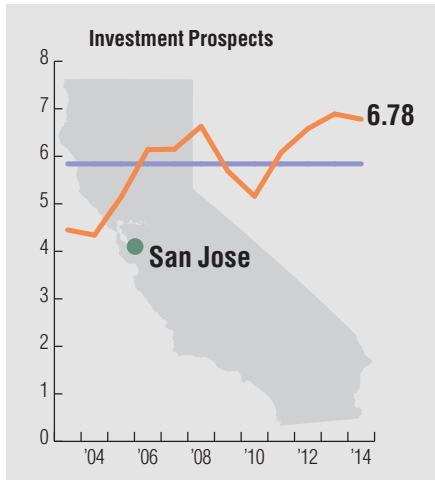
TABLE 3
Housing

2014 Rank	Market	Households		Median Home Prices			2014 Single-Family Home Year-to-Year Change					Multifamily Metrics			
		2014 Total (000s)	3-Year Projected Growth	2014 Price (\$ 000s)	2013-2014 % Change	2014 as % of Peak	Affordability Index*	Permits	Starts	Completions	Sales	Walk Score	Rent/Cost of Ownership**	Rent as % of HH Income	Space under Construction as % of Inventory
	Total U.S.	121,412	3.7%	205,140	3.7%	92.4%	169.50	68.8%	69.6%	77.5%	6.6%	55.87	0.8	19.4%	3.7%
1	San Francisco	1,690.83	3.7%	783.21	2.3%	93.0%	58.54	79.3%	71.5%	26.7%	6.2%	84.90	0.5	31.0%	4.6%
2	Houston	2,253.98	6.6%	190.49	3.9%	125.3%	164.41	25.2%	21.0%	14.7%	6.0%	49.80	0.8	16.0%	3.2%
3	San Jose	643.53	3.2%	785.43	1.9%	94.0%	66.38	57.8%	53.6%	27.1%	5.7%	54.50	0.4	22.0%	5.4%
4	New York City	4,385.95	1.4%	478.51	1.9%	89.0%	69.50	56.5%	40.9%	11.0%	4.4%	85.30	1.0	61.5%	9.5%
5	Dallas/Fort Worth	2,513.48	7.5%	183.84	4.4%	123.2%	179.02	59.1%	53.1%	24.1%	9.0%	46.90	0.8	15.9%	3.7%
6	Seattle	1,425.91	5.0%	356.54	4.9%	92.6%	117.85	14.0%	4.6%	-24.0%	5.8%	73.70	0.6	19.1%	6.4%
7	Austin	734.24	9.0%	234.16	4.2%	127.3%	156.70	58.4%	53.1%	28.0%	8.5%	46.70	0.7	17.4%	8.3%
8	Miami	897.23	4.0%	228.16	-0.3%	60.4%	106.30	81.1%	73.5%	51.6%	4.1%	72.50	0.9	30.7%	5.5%
9	Boston	1,812.35	2.8%	381.19	3.9%	93.3%	130.86	40.9%	34.2%	23.9%	3.1%	79.20	0.8	29.7%	4.9%
10	Orange County, CA	1,032.76	3.9%	649.39	1.9%	91.7%	65.02	55.0%	47.1%	18.3%	9.4%	60.70	0.5	25.5%	2.1%
11	Denver	1,078.58	5.6%	282.65	1.4%	113.2%	133.79	68.9%	63.8%	23.7%	12.1%	60.40	0.6	17.2%	6.1%
12	Nashville	660.04	4.2%	179.96	4.5%	98.4%	169.30	54.0%	49.2%	44.0%	4.6%	36.40	0.7	17.2%	4.1%
13	Los Angeles	3,362.78	3.2%	401.68	2.6%	71.9%	72.38	61.2%	45.5%	-10.0%	-1.2%	65.90	0.7	31.0%	1.8%
14	San Antonio	831.30	7.0%	182.58	5.5%	119.4%	156.84	85.9%	81.7%	59.9%	7.5%	40.80	0.7	17.3%	4.9%
15	San Diego	1,135.80	3.9%	474.47	3.8%	78.7%	75.19	100.1%	94.4%	45.3%	7.4%	55.70	0.6	26.7%	2.5%
16	Charlotte	741.05	8.7%	182.11	5.1%	116.7%	175.32	52.7%	50.3%	53.4%	3.7%	34.30	0.6	17.5%	7.9%
17	Raleigh/Durham	696.97	7.3%	203.07	3.5%	100.7%	175.78	44.6%	42.3%	44.9%	3.7%	41.40	0.6	8.5%	9.0%
18	Salt Lake City	395.91	4.7%	246.26	5.6%	106.3%	143.38	43.1%	40.9%	17.4%	3.8%	58.00	0.6	14.9%	4.0%
19	Portland, OR	938.37	7.1%	274.79	3.7%	93.3%	124.69	63.8%	57.8%	21.8%	5.4%	66.30	0.6	18.2%	5.7%
20	Minneapolis/St. Paul	1,348.80	4.3%	194.77	1.9%	83.7%	200.73	47.4%	47.5%	27.8%	3.8%	69.30	1.0	17.8%	5.1%
21	Chicago	3,555.22	2.4%	201.14	6.0%	73.6%	173.34	18.6%	17.8%	2.7%	4.5%	74.30	0.9	21.3%	2.1%
22	Washington, D.C.	2,196.03	4.8%	384.31	1.4%	89.3%	133.21	52.9%	46.1%	32.6%	9.3%	73.20	0.7	18.8%	7.4%
23	Tampa/St. Petersburg	1,186.91	3.7%	150.32	6.0%	66.7%	195.88	33.5%	30.8%	39.7%	1.6%	51.10	1.0	22.1%	3.2%
24	Orlando	857.83	7.9%	161.81	3.3%	60.2%	163.65	38.1%	32.0%	19.7%	2.6%	47.00	1.0	21.0%	5.6%
25	Phoenix	1,666.38	8.8%	178.93	0.4%	67.0%	170.03	96.7%	98.3%	80.0%	-0.6%	45.40	0.9	16.5%	2.4%
26	Atlanta	2,064.01	6.6%	146.02	6.7%	85.3%	215.78	-2.3%	-7.7%	-13.6%	5.7%	52.90	1.2	16.9%	1.5%
27	Northern New Jersey	1,641.88	1.8%	360.43	6.3%	87.8%	131.46	76.5%	67.2%	43.4%	8.4%	74.00	0.7	24.7%	4.9%
29	Honolulu/Hawaii	323.14	3.7%	711.21	7.2%	111.1%	56.99	54.9%	48.8%	22.8%	-0.5%	63.00	N/A	N/A	N/A
30	Philadelphia	2,294.06	2.0%	231.65	5.3%	99.3%	169.71	55.9%	45.1%	12.1%	4.2%	74.10	0.8	20.3%	2.5%
31	Indianapolis	720.47	4.8%	141.05	4.7%	114.6%	229.06	69.5%	69.5%	42.7%	4.3%	37.40	0.8	15.9%	3.0%
32	Pittsburgh	1,012.26	1.7%	141.53	5.0%	118.7%	232.63	36.6%	29.0%	4.9%	2.8%	64.10	1.0	20.6%	2.1%
33	Westchester/Fairfield	692.10	1.7%	520.44	3.1%	87.9%	103.85	33.5%	20.8%	108.0%	7.8%	45.00	0.6	28.4%	1.2%
34	Virginia Beach/Norfolk	649.39	3.4%	208.95	5.3%	85.7%	161.31	50.3%	46.6%	39.0%	4.7%	40.80	0.7	20.1%	7.7%
35	Kansas City	836.23	3.7%	158.64	4.1%	102.3%	212.34	101.4%	105.5%	98.3%	5.8%	38.10	0.8	14.7%	2.9%
36	St. Louis	1,157.17	2.5%	139.69	8.0%	94.9%	230.12	68.4%	74.0%	88.3%	4.5%	61.40	0.9	16.4%	1.5%
37	Baltimore	1,065.37	3.2%	267.69	4.9%	94.0%	151.77	56.9%	54.5%	45.0%	-2.1%	63.90	0.7	18.0%	4.7%
38	Las Vegas	772.40	9.6%	176.31	4.8%	55.6%	163.25	93.4%	86.8%	37.3%	6.5%	49.20	1.0	18.2%	0.5%
39	Jacksonville	549.37	5.3%	161.71	2.3%	84.0%	187.13	9.1%	6.0%	17.6%	1.2%	32.60	0.9	17.9%	3.6%
40	Sacramento	820.51	3.6%	237.17	2.6%	63.3%	142.69	76.8%	78.4%	62.2%	6.7%	49.30	0.8	18.8%	1.5%
41	Cincinnati	853.53	3.1%	141.92	3.6%	97.8%	233.78	96.2%	91.9%	42.7%	5.2%	58.90	0.9	16.1%	1.2%
42	Columbus	753.20	3.8%	155.79	7.8%	103.9%	221.90	92.8%	85.8%	42.7%	4.9%	47.00	0.8	15.3%	4.2%
43	Oklahoma City	517.42	4.9%	156.13	2.5%	118.0%	189.65	27.4%	22.9%	20.3%	5.7%	35.60	0.6	13.5%	1.8%
44	Tucson	407.50	8.3%	182.68	7.2%	74.7%	158.45	96.8%	97.9%	63.8%	3.5%	48.20	0.7	17.3%	1.4%
45	Milwaukee	634.24	2.6%	223.93	8.1%	101.7%	148.49	88.3%	84.1%	32.0%	4.6%	60.60	0.7	19.1%	1.7%
46	Albuquerque	354.84	2.4%	183.71	5.1%	92.6%	147.04	102.8%	84.2%	-8.5%	2.6%	47.50	0.6	17.8%	3.9%
47	New Orleans	468.14	2.6%	182.84	6.9%	106.0%	150.90	49.0%	52.1%	76.8%	-0.4%	55.60	0.9	21.9%	2.1%
48	Memphis	513.56	4.0%	137.73	6.5%	96.9%	197.00	87.4%	89.2%	124.6%	8.1%	39.40	0.9	17.8%	2.0%
49	Cleveland	839.53	0.1%	123.03	2.6%	88.4%	252.76	73.7%	68.1%	13.7%	5.0%	58.30	1.1	18.6%	0.6%
50	Providence, RI	623.74	1.4%	236.35	3.3%	80.8%	147.82	73.1%	64.5%	33.8%	0.2%	73.00	0.8	27.1%	0.4%
51	Detroit	1,689.97	1.5%	74.49	4.0%	45.5%	428.06	-8.1%	-5.0%	17.8%	9.2%	49.90	2.2	18.7%	0.5%

Sources: U.S. Census Bureau, Moody's Analytics, Reis.

*Affordability is the percentage of households with a median income that can afford to buy a median-priced home.

**Market apartment rent/median mortgage payment.



growth in all sectors of the economy, technology will remain the biggest contributor to the economy. Longer term, the San Jose economy will continue to benefit from the cluster of leading tech firms, its ability to cultivate and attract innovative companies, and its highly educated population—all of which will remain major drivers. High costs, however, will continue to be a concern.

New York City (4). New York slips two spots to number four in this year's survey. The investment and development components are still rated "good," but are down from last year's scores. Despite their decline in scores, the investment and development components are ranked number two and three in this year's survey. Along with San Francisco, New York is probably the top-mentioned market by this year's interviewees. New York comes up in conversation related to business and professional employment growth and its exposure to tech employment. In general they all like New York, but some real concerns exist that the pricing is once again getting too high. A national banker expresses his concerns: "Cap rates are lowering to levels that do not make sense in cities like New York."

New York City is on the verge of a self-sustaining expansion: employment has surpassed its prior peak well ahead of other

large metro areas. In 2014, total employment will get more support from goods industries as construction hiring ramps up. Further out, job growth in New York City will approximate the national rate, but gross metro product (GMP) and income growth will be higher, owing to the region's highly productive and well-educated workforce.

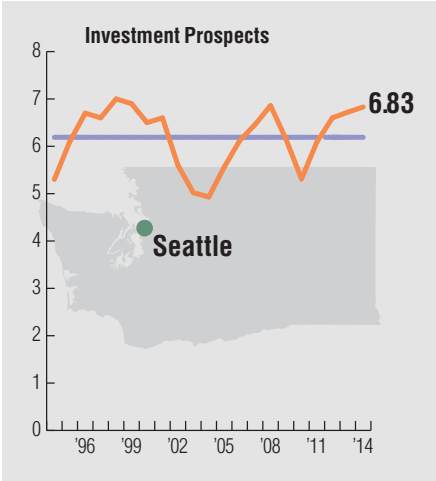
Survey respondents recommend "buy" for all property types in New York. The recommendations exceed the average of the top markets. Rental apartments and hotels are the property sectors that respondents feel offer the best opportunity in 2014.

Dallas/Fort Worth (5). In the 2014 survey, Dallas/Fort Worth moved up four spots to number five. Survey respondents rated Dallas/Fort Worth in the top ten for investment, development, and homebuilding prospects, but it was a particularly strong jump in homebuilding prospects that moved the market up in this year's survey. The prospects for all three components are considered "good" by respondents for 2014. The Dallas/Fort Worth economy has a number of interviewees very attracted to this sometimes-volatile market. One institutional adviser observes, "We see strong opportunities for new speculative industrial development in the Southwest and Pacific; lots of new development going on in Dallas."

Housing and manufacturing are projected to keep the Dallas/Fort Worth economy expanding in 2014. The Dallas/Fort Worth economy will continue to benefit from high concentrations of technology, corporate headquarters operations, excellent distribution infrastructure, and above-average population gains. Dallas/Fort Worth remains attractive to employers and employees alike due to its highly competitive cost of living and doing business.

Industrial/distribution is the property type that survey respondents most recommend as a "buy" in this year's survey. Apartment, retail, and office all have buy recommendations above the comparative average, but respondents feel that it would be better to hold Dallas/Fort Worth hotels in 2014.

Seattle (6). Seattle is up one spot to number six in this year's survey. Prospects for all three market components—investment, development, and homebuilding—improved in 2014, with homebuilding prospects posting the largest gain. Survey respondents rated each component as offering "good" prospects for 2014. A national real estate consultant expresses the following view of the market: "Seattle is enjoying good job growth due to the tech industry. It is also becoming a core market for foreign investors."



Seattle-Bellevue-Everett’s near-term fortunes are more upbeat than most because the expansion in commercial aerospace manufacturing will stretch into 2014. In addition, projected hiring in tech industries will keep wage income growth above average. Seattle’s high rate of educational attainment and global connections will keep the economy viable in the coming year.

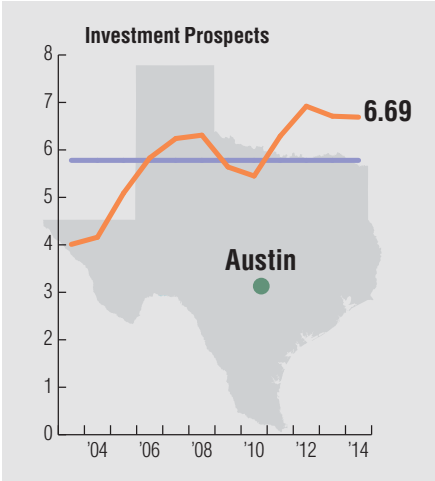
Respondents say they feel good about industrial/distribution, office, and retail in Seattle. The “buy” rating for each of these property types is ranked in the top five among the competitive market set. The outlook for hotels is not as sanguine, with respondents giving Seattle hotels a “sell” recommendation well above the market average.

Austin (7). Austin remains in the top ten for 2014, but actually slipped three spots from last year’s position. The metro area’s drop in this year’s survey is due to a slight decline in investment and development prospects. Despite the decline, the outlook for both components is still considered “good” by respondents and they are in the top ten compared with all markets. The outlook for homebuilding prospects improved for 2014. The Texas state capital metro area continues to be a favorite of interviewees; interest in it is now at a point where investors are willing to take on more risk. “We have made

several investments in value-add office assets in Austin. We see vacancy as an opportunity in these markets.”

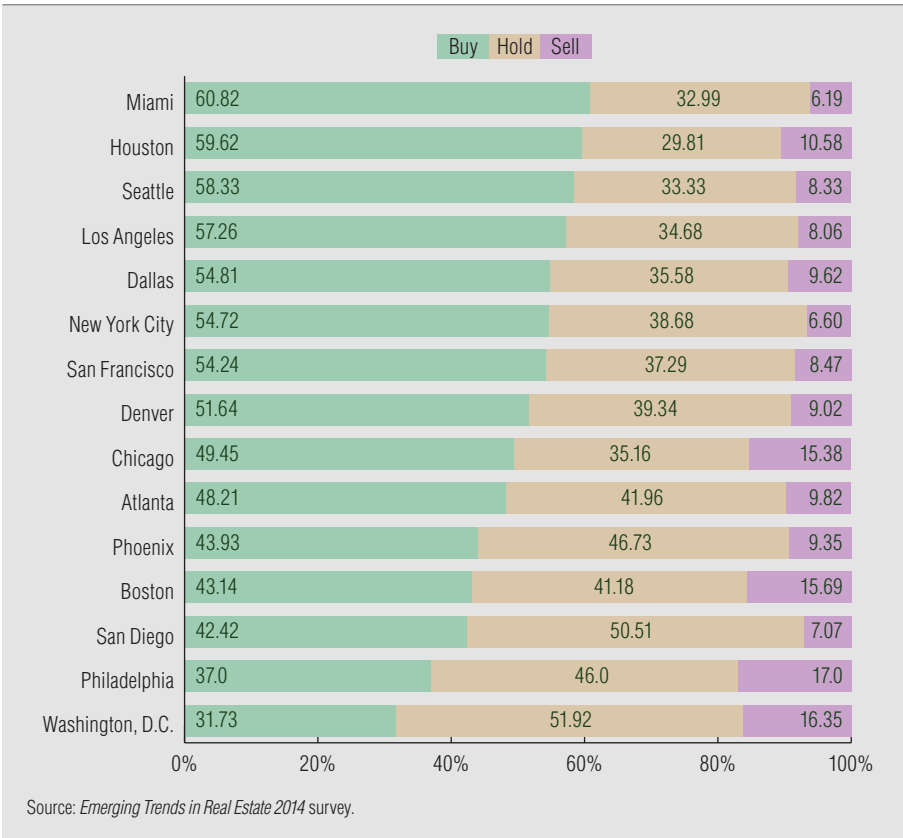
Austin’s expansion will lead the state over the coming year, driven by solid growth in housing construction and technology-related industries. In-migration of professionals in those industries will lift multifamily and subsequently single-family construction. Austin will continue to attract relocating companies aiming to take advantage of relatively lower business costs, lower taxes, and a highly trained workforce. Longer term, the metro area’s well-educated workforce, high concentration of technology businesses, and population gains double to triple the national pace will keep the Austin economy growing.

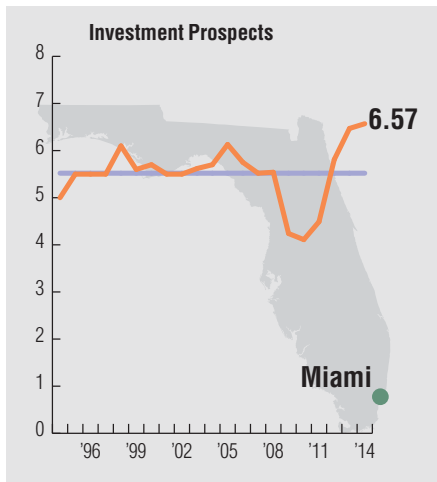
Miami (8). Miami breaks into the top ten for 2014 by moving up four spots to num-



ber eight. It is up 17 spots from 2012. Each of the three components of performance increased for 2014, with investment prospects and homebuilding prospects both

EXHIBIT 3-9 U.S. Industrial/Distribution Property Buy/Hold/Sell Recommendations



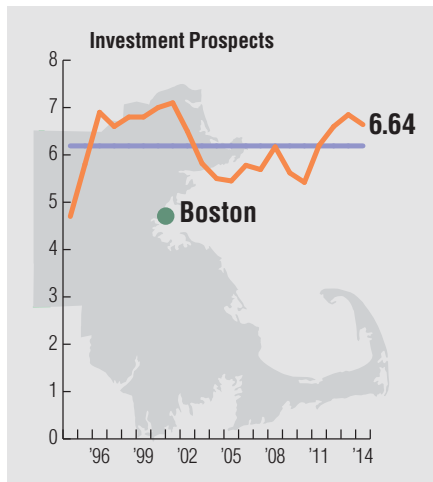


in the top ten. The outlook for development is up from 2014, but ranks only 26th compared with all of the markets in the survey. Miami's jump this year is largely due to a significant increase in the 2014 outlook for homebuilding prospects. Miami has rebounded nicely from the recession, and this has not escaped the notice of interviewees. An international real estate law firm notes that "Miami is still the 'South American playground.'" An executive with an institutional investor describes the uniqueness of Miami: "Miami is a market that doesn't operate off of real estate fundamentals like other markets. It operates in its own universe."

Over the next two years, growth in the Miami economy will track national economic growth as the upscale economy compensates for slower population growth. Longer term, Miami will benefit from its expanding infrastructure, strong international trade ties, and stature as an international tourist destination.

Miami is a strong "buy" for industrial/distribution, retail, and hotels. Miami actually has the highest percentage of respondents recommending "buy" for these three property types. Respondents see Miami office as a "hold" market.

Boston (9). The 2014 survey puts Boston down three spots to number nine. The metro area's investment prospects declined slightly in 2014. Despite the



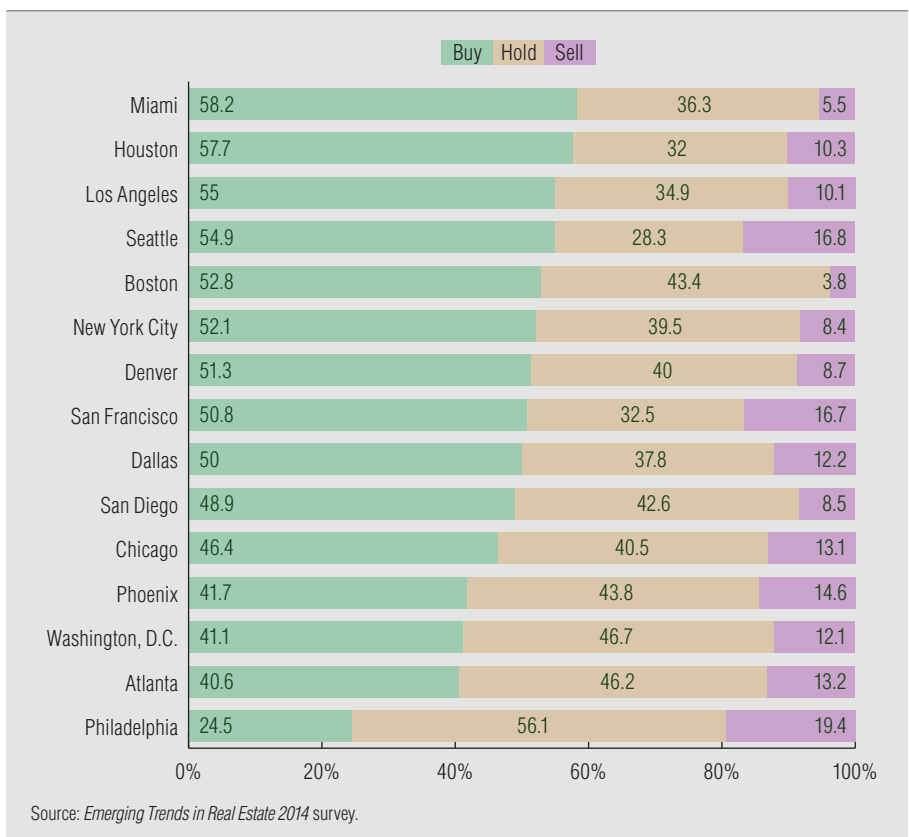
decline, investment prospects are still considered "good" by respondents. Development and homebuilding prospects are considered "good" by

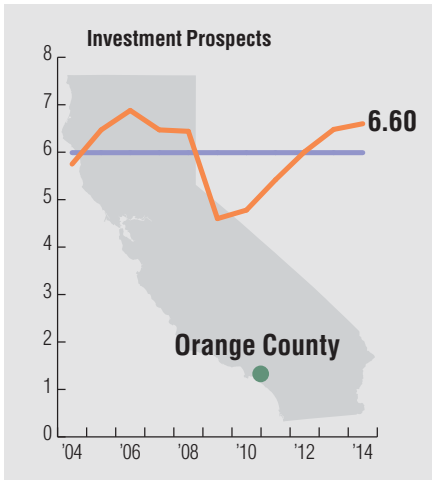
respondents and are up slightly from 2013. Boston has several things going for it that make it attractive to investors. A Boston-based institutional investor sums up his thoughts on Boston: "Boston is a 24-hour knowledge-based economy. It is hard to build in Boston; there is a transition happening there because tenants are moving away from the financial district and toward Cambridge."

Strong gains in health care, construction, and high tech will help Boston outperform the nation in job growth in 2014. Boston will benefit from a concentration of high-skill, well-paying jobs in health care and technology. However, high business and living costs and below-average population growth could cause the market to underperform the national economy in the long run.

EXHIBIT 3-10

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

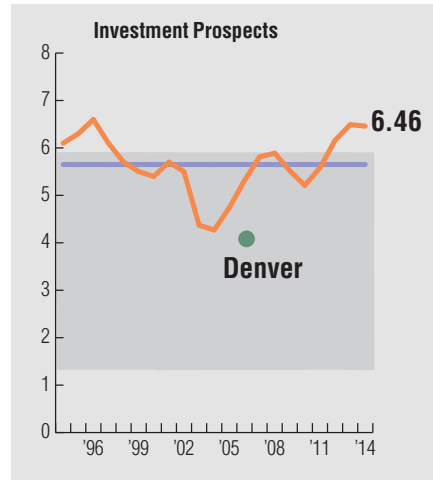




Despite the metro area's decline in overall ranking, survey respondents still see apartment, office, retail, and hotel as "buys" in 2014. Boston industrial/distribution is viewed as a "hold" by survey respondents.

Orange County, California (10). At number ten, Orange County remains unchanged from 2013. The outlook for investment prospects in 2014 increased slightly and is ranked number nine among all markets. According to the survey, the outlook for development and homebuilding prospects is up significantly from 2013. Survey respondents see the 2014 outlook for each component to be "good." The recovery in Orange County may be taking some people by surprise. A local real estate investor doesn't think this will last long. "In Orange County, the unemployment rate is low and wage pressure is increasing. There is a lot of multifamily under construction, which could lead to problems in the future. In the office sector, the Fashion Island area is hot and in demand and rents have increased substantially, but there is still a lot of vacancy near the airport, and rents there are much lower."

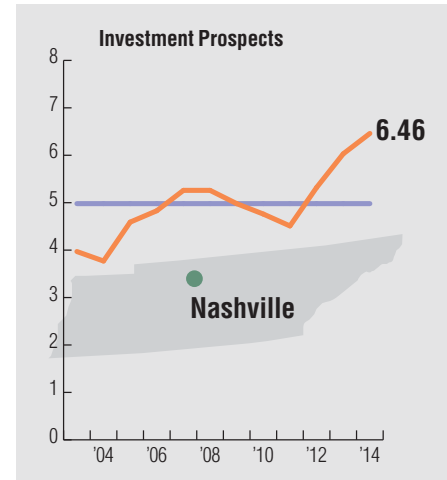
Denver (11). Colorado's largest city moves up three spots from 2013 to number 11. Survey respondents see the outlook for investment, development, and



homebuilding prospects to be "good" for 2014. The outlook for development and homebuilding prospects is up from 2013, while the investment outlook remains unchanged from last year. Denver is intriguing to a number of interviewees. Some see it as an established core market, while others see it as more of an opportunistic location. A hedge fund executive opines, "Secondary cities, or 'institutional core cities,' are the markets to invest in for up-and-coming funds. Examples are Denver, Houston, Dallas, and Seattle. These 'core' markets are ideal for development, as that will be the way to make money in 2014. With the higher risk, they could earn a higher return."

Denver is positioned to be an above-average performer in the coming years. High industrial diversity and a well-educated workforce provide numerous avenues for growth. Denver International Airport will be a boon to the economy by offering easy access to national and global markets. In-migration will be robust because of plentiful job opportunities, supporting strong long-term growth.

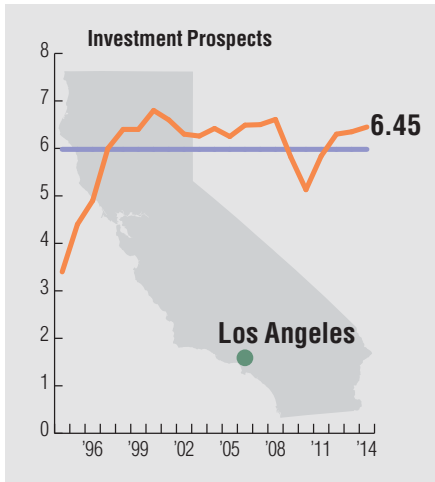
Industrial/distribution, office, and retail are considered "buys" by this year's survey respondents. The results of the survey indicate that respondents think 2014 might be a year to think about selling apartments and hotels in Denver.



Nashville (12). The state capital of Tennessee moves up six spots in 2014 to number 12. The metro area's move in the rankings can be attributed to survey respondents' seeing definite improvement in investment, development, and homebuilding prospects. All three of these components are rated in the top 20 in this year's survey. Homebuilding prospects saw the largest increase from 2013 to 2014. Nashville is quickly moving onto the national investment radar. A number of interviewees now see it as a viable location for development. A representative of a foreign investor notes the following: "More investors are attracted to cities where job-growth engines such as state capitals, major universities, or major medical centers are located such as Nashville."

Nashville's short-term growth prospects are the best in years. The release of pent-up demand for homes will soon propel homebuilding, just as auto demand is already propelling manufacturing. Longer term, Nashville's skilled workforce and diverse economy support a positive outlook, and the metro area will grow faster than the country as a whole over the long term.

Los Angeles (13). California's largest city improved to number 13 in this year's survey, up three positions. Investment, development, and homebuilding pros-



the largest gains in this year's survey. The industrial market in Los Angeles is doing very well, but other property types are starting to benefit from the improved economy. As one local investor describes, "Out in Los Angeles, things are going very well; we are seeing the housing market rebound and the office sector is coming along—not great, but steady; we haven't seen a lot of new construction. Rental rates in L.A. haven't moved much, so we likely won't see too much new supply here."

L.A.'s recovery will strengthen in 2014 because of housing, visitor-dependent industries, and increased spending on entertainment production and advertising. Spending and payroll cuts by cash-strapped local and federal governments remain a near-term risk. High business

and housing costs and net domestic out-migration will dampen job and output growth over the long run.

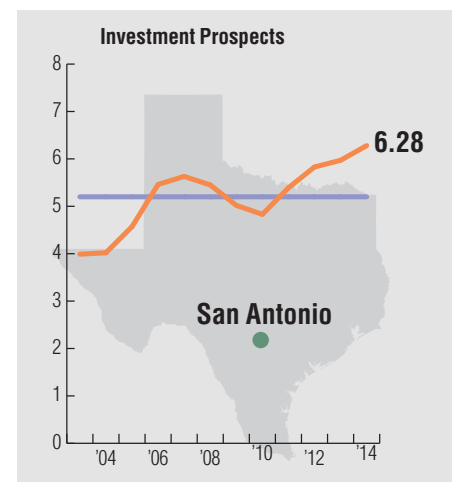
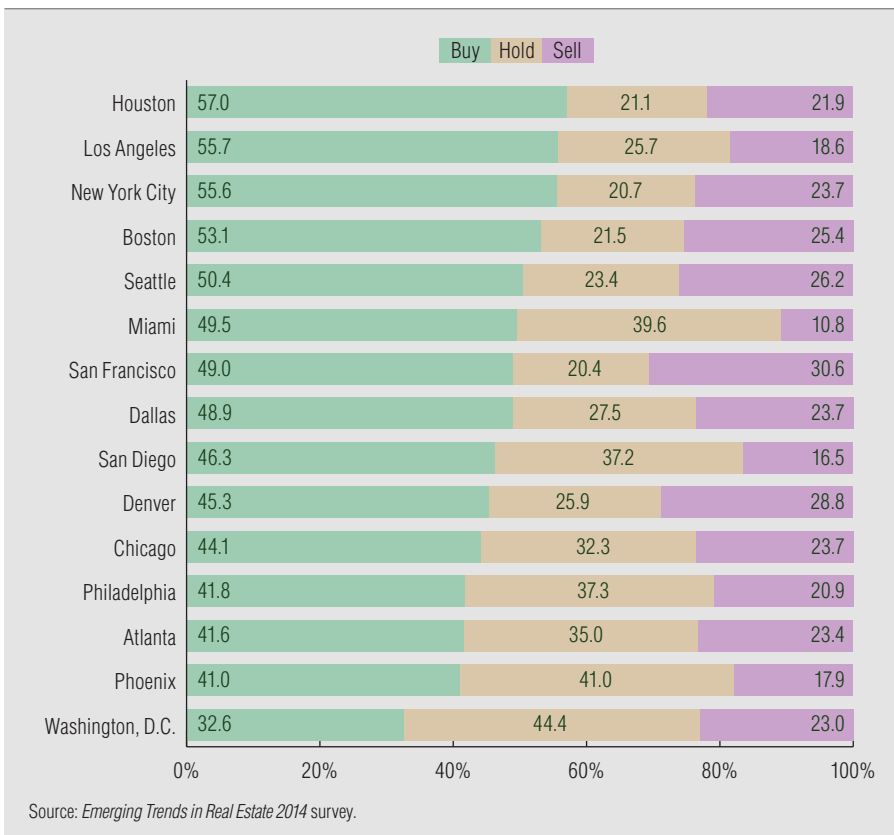
Survey respondents rate Los Angeles as a "buy" for all property types. The buy rating for apartments, industrial/distribution, and retail are in the top five of the competitive set. Respondents see 2014 as a year to hold office and hotel.

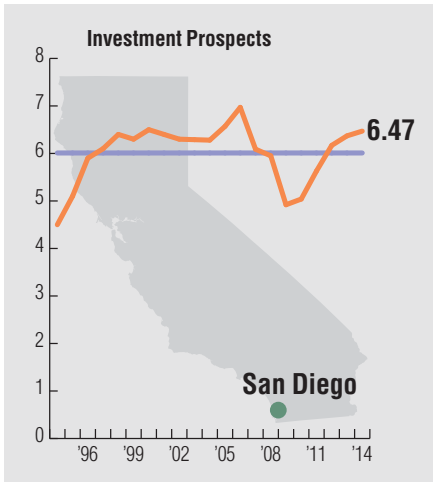
San Antonio (14). Remaining in the top 20 in 2014, San Antonio has moved up from number 19 to 14. The metro area's investment and development prospects rankings improved in this year's survey, and remain in the "modestly good" range. Respondents feel better about homebuilding prospects in San Antonio as the rating moved from "fair" to "modestly good" in 2014. San Antonio is a relatively new market to the top 20, but it has enough going on to keep investors interested. The manager of a real estate fund describes the benefits of San Antonio as follows: "San Antonio is a very diverse and balanced economy with the effects of Eagle Ford shale as well as manufacturing, and it's also under the influence of Austin, only 50 miles away."

San Antonio's expansion should reaccelerate over the coming year, supported by a variety of industries, including housing, manufacturing, local government, and development in Eagle Ford shale. However, further federal fiscal contrac-

pects all improved in the eyes of survey respondents. Each component is ranked "modestly good" to "good." The outlook for development and homebuilding had

EXHIBIT 3-11
U.S. Apartment Buy/Hold/Sell Recommendations





tion will remain a downside risk. Longer term, the concentration of military cybersecurity and medical activity, growth in commercial aerospace, low costs of doing business, and above-average population gains will contribute to above-average overall performance.

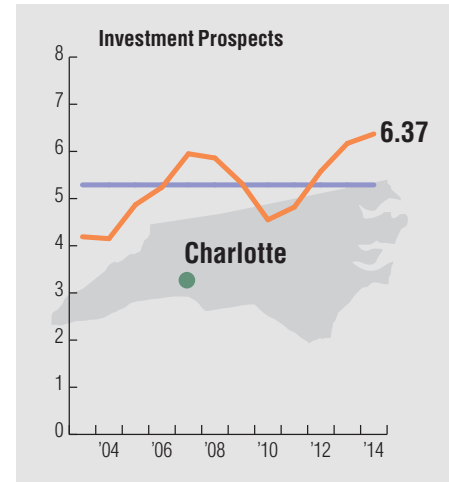
San Diego (15). At number 15, San Diego remains unchanged in this year's survey. Development and homebuilding prospects both improved in 2014's survey. Respondents see the outlook for investment and development prospects as "modestly good" in 2014, while the outlook for homebuilding increased to a "good" rating. San Diego is a West Coast center for life sciences. A research and development fund investor describes the life-sciences market: "Cambridge/Boston is the best market for life science. Then San Francisco and San Diego in that order, based on tenant base. However, San Francisco and San Diego have sufficient supply to handle growth."

San Diego's recovery is forecast to strengthen in 2014 and 2015, though it faces the largest downside risk among California's metro areas from federal budget austerity. Weakness in military- and visitor-dependent industries would offset growth in technology, trade, and real estate. Employment will surpass its previous peak in late 2014, slightly later than the country as a whole. In the

long term, San Diego is well positioned to take advantage of high-value-added tech research and development and the Pentagon's reorientation toward the Pacific Rim. Longer term, high business and living costs will remain a concern.

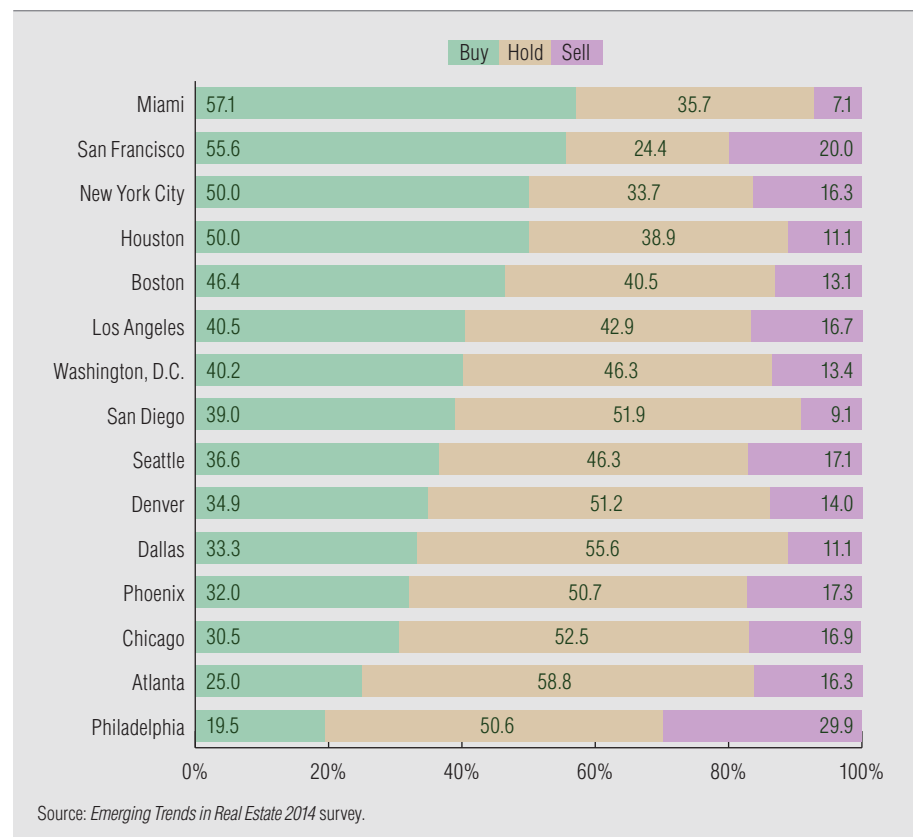
Office is the San Diego property type that respondents feel is a "buy" in 2014. The survey shows apartments, hotels, and retail as being a toss-up between "buy" and "hold." Respondents see industrial/distribution as a solid "hold" for the coming year.

Charlotte (16). Remaining in the top 20 for the second year in a row, Charlotte moved up one position to number 16. In 2014, investment and development prospects in Charlotte were up slightly. Respondents see the outlook as "modestly good" to "good" for the coming year.



The outlook for homebuilding prospects had the largest increase in this year's survey. Homebuilding prospects moved from "fair" to "good" this year. Interviewees

EXHIBIT 3-12
U.S. Hotel Buy/Hold/Sell Recommendations



expressed concern about consolidation in the financial services industry when discussing Charlotte, but the metro area's strong demographic trends continue to keep them very interested.

The recovery of the Charlotte-area economy will outpace that of the United States through 2014, due to the former's broad mix of drivers. Growth next year will be faster as the large service sector, including professional and business services, expands consistently. Well above-average population growth bodes well for gains in health care, consumer industries, and housing. Charlotte will outperform the country as a whole in the near term.

Raleigh/Durham (17). Slipping six spots to number 17, Raleigh/Durham is still in the top 20 this year. The decline is attributable more to other markets improving than the outlook for Raleigh/Durham deteriorating. Investment prospects improved slightly in the 2014 survey and remain in the “modestly good” range as did the outlook for development prospects. The outlook for homebuilding prospects moved from “modestly good” to “good,” but slipped when compared with the improvement in other markets. It isn't just jobs—it is high-quality jobs that seem to be supporting growth in Raleigh/Durham. “For the first time in a number of years, we are seeing office

developments announced. The new development seems to be driven by creation of new jobs. A national financial services and a technology firm both announced the creation of high-paying jobs. Raleigh alone is creating 12,000 jobs a year. Though still only half of what it used to be, it is still clear that job creation is starting to come back.”

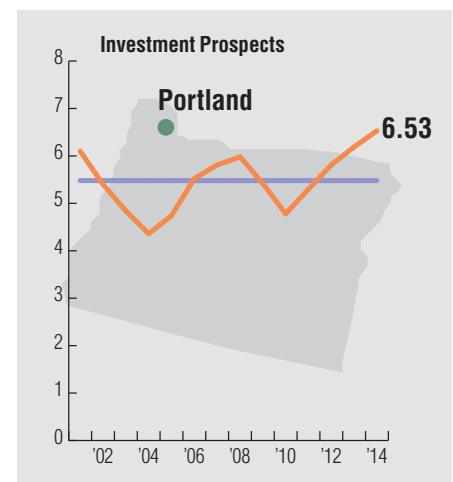
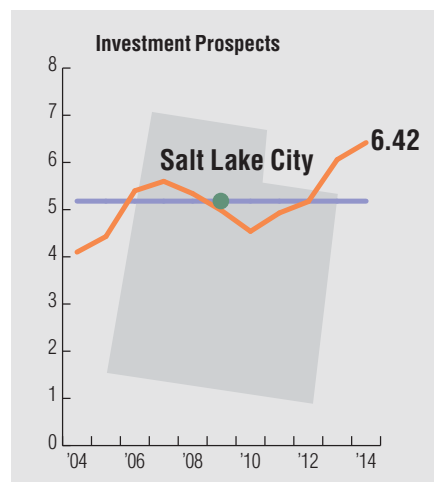
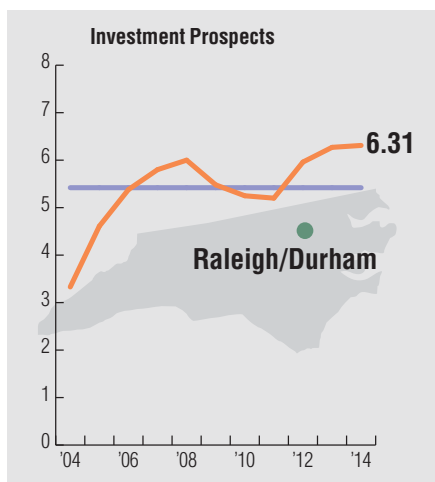
Job growth in private services will keep Raleigh/Durham recovering slightly faster than the country as a whole through 2014. The outlook for Durham is bright thanks to its concentration in education and health care, and the Triangle's science- and tech-based cluster. Over the longer term, strong population growth, household income gains, investment in high technology, and pent-up housing demand will drive above-average job growth.

Salt Lake City (18). In this year's survey, Salt Lake City moved into the top 20, moving up three spots to number 18. The metro area's improvement can be traced to survey respondents' feeling more optimistic about the outlook for investment prospects in 2014. Salt Lake City's investment prospects ranked 30th in 2013, but moved all the way to number 16 this year. Investment prospects in Utah's largest city are considered “modestly good.” The ranks for development and homebuilding remained virtually unchanged and

are both considered “modestly good.” Salt Lake City is new to the top 20, and is fairly unfamiliar to a number of interviewees. The metro area's demographic and employment story will likely pique national investors' interest in 2014.

Salt Lake City will be one of the nation's strongest performers in 2014, with rapid gains in high tech, finance, and leisure. Construction will pick up as the area's housing shortage is addressed and higher prices make building more attractive. The outlook for consumers is similarly rosy, as strong job and income gains, along with rising wealth and easier credit conditions, drive above-average increases in spending. Longer term, solid demographics, including a highly skilled workforce, along with low business costs, will help facilitate growth. Salt Lake City is expected to comfortably outperform the nation over the next several years.

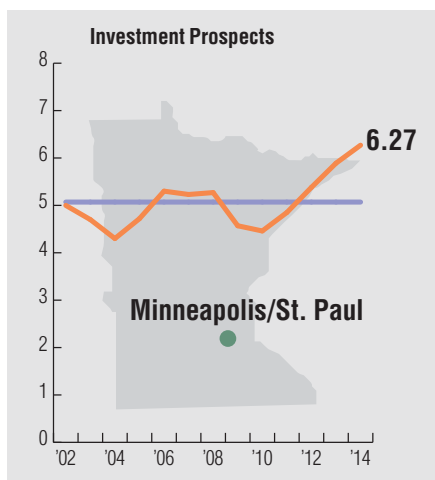
Portland, Oregon (19). Portland moved up one spot to number 19 in this year's survey. Respondents see investment prospects in Portland improving in 2014 from “modestly good” to “good.” Development prospects remained unchanged at “modestly good” this year, but homebuilding prospects improved from “fair” to “modestly good.” Interviewees are drawn to Portland due to its attractiveness to younger workers. Virtually all references to Portland are



based on the quality of life it offers. One institutional investor describes how he views these markets: “The countertrends include markets that offer alternative lifestyles such as college towns and tech-attractive cities such as Boulder, Colorado; Portland, Oregon; and Austin, Texas.”

Benefiting from a broad improvement in the U.S. and global economies, Portland’s economy should grow over the coming year. The metro area’s basic industries are well linked to business investment spending that is due to rise in the coming two years, and any improvement in global demand will be a bonus. Further, slow hiring recently among nonbasic service industries means payrolls are not bloated and will respond to stronger income growth.

Minneapolis/St. Paul (20). Moving up three spots, Minneapolis/St. Paul rounds out the top 20 in this year’s survey. The outlook for investment and development prospects improved in 2014, with both sectors moving up in the rankings. Survey respondents see the outlook for both to be “modestly good.” Respondents see the outlook for homebuilding prospects up from “fair” to “modestly good” this year. Minneapolis has typically been viewed as a regional city, but it is starting to get more attention as investors look at other alternative opportunities.



A REIT analyst notes, “We have already seen from clients an interest in looking at higher-volatility properties in places like Seattle and Minneapolis.”

Minneapolis/St. Paul faces relatively few obstacles as the economy moves toward expansion. Major commercial construction projects and a healthy housing market will have far-reaching impacts. The long-run outlook remains positive, as a diversified economy, a strong workforce, and the presence of key anchors—both institutional and private sector—will power growth.

Other Markets

Chicago (21). The largest city in Illinois remains outside the top 20 again in 2014, but did improve three positions from last year. The metro area’s improvement is attributable to survey respondents’ view that the homebuilding prospects will be better in 2014. The outlook for homebuilding prospects improved four spots and is now considered “modestly good,” up from last year’s “fair.” The investment and development outlook remained virtually unchanged from 2013 to 2014. Interviewees speak about Chicago as two cities—the urban center and the suburbs. Clearly, the action is in the former. A local investor and service provider states: “Urbanization is the key in Chicago; we are seeing the trend of movement back into the city. People want to be in a [denser] environment, convenience as more of what you need and need to do is close at hand, don’t want to deal with traffic. This is resulting in office users’ move back in from the suburbs to be closer to workers.”

Survey respondents feel like 2014 will be a year to hold assets in Chicago. No property type recorded a strong percentage of respondents recommending “buy.” Chicago office received a comparatively strong “sell” rating, indicating that some market participants think it may be time to exit the Chicago market.

Washington, D.C. (22). The nation’s capital tumbles all the way to number 22 in this year’s survey, dropping 14 positions from last year. Washington’s decline is *the* story of this year’s survey. The drop is a combination of survey respondents’ seeing a less favorable outlook for D.C. in 2014, while feeling better about a number of other markets. The investment and development outlook for Washington, D.C., declined in 2014, but is still in the “modestly good” category. These measures now rank 26th, down from first and ninth, respectively. The outlook for homebuilding did improve slightly; but when compared with the other markets, the rank slipped from fourth to 18th. Uncertainty is surrounding the federal government and also affecting the Washington real estate market. A fund portfolio manager sums up the D.C. market thusly: “There is still uncertainty in a few markets such as Washington, D.C., where sizable supply is coming, which would suggest it’s not going to be great.”

Despite the drop in the rankings, survey respondents don’t think 2014 is the year to exit Washington, D.C. The only property type with a relatively high “sell” recommendation is industrial/distribution. Office, apartment, and retail all have a solid “hold” recommendation. Hotels have a slightly above-average recommendation toward “buy.”

Tampa/St. Petersburg (23). Tampa/St. Petersburg rebounded six positions in this year’s survey to number 23. Survey respondents feel better about the investment and development prospects in Tampa/St. Petersburg in 2014. Each measure improved in total score and comparative rank, although the outlook for development remains “modestly poor.” The outlook for homebuilding saw the largest increase, moving from “modestly poor” to “fair.”

Orlando (24). In this year’s survey, Orlando is ranked number 24, up four spots from 2013. Survey respondents feel that the investment, development, and

homebuilding prospects in Orlando will be better in 2014. Each category is rated as “modestly good.” The respondents also feel that Orlando will outperform more markets this year as the rank for each category improved over last year.

Phoenix (25). Arizona’s capital city moved up eight spots in the 2014 survey and now stands at number 25. While survey respondents feel that the investment outlook will be better in 2014, it is the outlook for development and homebuilding that really boosted Phoenix’s overall rank. The development outlook moved from “modestly poor” to “fair,” while the outlook for homebuilding moved from “modestly poor” to “modestly good.”

Survey respondents see Phoenix office as a “buy” in 2014. They tend to see next year as a good time to hold apartment, industrial, and hotel properties. The respondents are mixed on retail, with some thinking it may be the year to sell and others to hold.

Atlanta (26). The state capital of Georgia improved significantly in the 2014 survey, rising nine spots to number 26. The rise in Atlanta’s rank is attributable to improvement in all three performance categories. Investment, development, and homebuilding prospects all moved from being considered “modestly poor” in 2013 to “modestly good” in 2014. More important, Atlanta made double-digit improvement compared with the other markets in the survey for investment and homebuilding.

Survey respondents think that the outlook for Georgia’s largest city is much improved in 2014, but they aren’t ready to buy just yet. The results of this year’s survey put Atlanta near the bottom of markets with “buy” recommendations by property type. It seems like Atlanta will be a market to hold in 2014.

Northern New Jersey (27). Northern New Jersey fell from number 13 to number 27 in this year’s survey. This decline rivals that of Washington, D.C., for the most surprising finding. The decline in

northern New Jersey’s position in the survey is due to the outlook for investment and development. Each category declined in both overall score and in the rankings comparing it to other markets.

Inland Empire (28). California’s Inland Empire improved in the 2014 survey, rising to number 28 from 36 last year. The improvement in the Inland Empire’s position is attributable to survey respondents’ feeling better about development and homebuilding prospects in 2014. Respondents consider the outlook for development and homebuilding to have improved to “modestly good” from last year’s “modestly poor.”

Honolulu/Hawaii (29). In this year’s survey, Honolulu/Hawaii slipped to number 29. This represents a decline of seven spots from last year. Survey respondents see little change in the investment, development, and homebuilding prospects for Honolulu/Hawaii in 2014. The decline in overall position is largely due to improvement in other markets.

Philadelphia (30). Philadelphia came in at number 30 in this year’s survey, down slightly from number 27 in 2013. Survey respondents don’t see a lot of change in the outlook for investment, development, and homebuilding for 2014 in Philadelphia. Each of these categories continues to be ranked from “fair” to “modestly good.” Philadelphia’s loss of ground in 2014 is attributable to the number of markets that have a stronger outlook.

Survey respondents see Philadelphia as a market to either hold or sell. It had the top “sell” ranking for industrial/distribution, office, retail, and hotel. Not all respondents feel like it is time to sell in Philadelphia as the market also ranked near the top for “hold” recommendations by property type.

Indianapolis (31). Indianapolis increased by six places in the 2014 survey and now stands at number 31. Survey respondents’ outlook for Indianapolis did not

change significantly in 2014. The survey shows that the outlook for investment, development, and homebuilding are all in the “fair” range.

Pittsburgh (32). Pittsburgh remained fairly stable in 2014 and its ranking of 32 is down only two from last year’s survey. Survey respondents reported a modest improvement in the outlook for investment, development, and homebuilding in 2014. They see the potential for these categories as “fair” to “modestly good.” Pittsburgh’s comparative rank for investment remained unchanged, but the city did lose some ground to other markets in the outlook for development and homebuilding.

Westchester/Fairfield (33). In this year’s survey, Westchester/Fairfield slipped eight positions to number 33. The 2014 survey respondents lowered their expectations for investment and development returns, although both remain in the “fair” range. Respondents, however, do see an improved outlook for homebuilding next year.

Virginia Beach/Norfolk (34). Virginia Beach/Norfolk came in at number 34 in the 2014 survey; this is down eight spots from the 2013 survey. The decline in Virginia Beach/Norfolk’s position was largely due to survey respondents’ lowering their outlook for development prospects in 2014. The outlook for investments also declined slightly, but the impact on Virginia Beach/Norfolk’s overall position was minimal. Survey respondents do see better prospects for homebuilding next year, but the improvement was not enough to keep up with improvement in other markets.

Kansas City (35). Down only one position from 2013, Kansas City’s position in this year’s survey is 35th. Survey respondents were consistent with last year’s outlook for investment, but feel better about the prospects for development. The outlook for homebuilding improved slightly in this year’s survey, but the

increase was not enough to keep up with improvement in other markets.

St. Louis (36). In this year's survey, St. Louis improved seven spots, ranking 36th. The 2014 survey revealed widespread improvement in the outlook for St. Louis. Respondents raised the outlook for investment, development, and homebuilding. The level of improvement was enough to keep pace with other markets, leading to St. Louis's overall improvement.

Baltimore (37). Maryland's largest city declined by six positions in this year's survey to land at number 37. Survey respondents lowered their expectations for investment and development in Baltimore for 2014. While the decline still leaves the outlook in the "fair" range, the decline lowered Baltimore's competitive rank by category. The outlook for homebuilding did improve, however, going from "modestly poor" to "fair."

Las Vegas (38). Near the bottom in the 2013 survey, Las Vegas rose to number 38 in this year's survey. The driver of Las Vegas's improved ranking is the stronger outlook by survey respondents to investment, development, and homebuilding. The improvement in these outlooks was significant enough to raise the comparative ranking by category. While Las Vegas did show a significant improvement, it is important to note that the overall outlook still remains "modestly poor" to "fair."

Jacksonville (39). For the third consecutive year, Jacksonville remains at number 39. Survey respondents see the outlook for 2014 as being very similar to that for last year. The outlook for investment, development, and homebuilding improved to the "fair" range. The improvement in each category was sufficient enough to keep pace with overall market changes.

Sacramento (40). Up nine positions from 2013, California's capital city stands at number 40 in this year's survey. Sacramento's improvement is attributable to survey respondents' projecting a

better outlook for all three performance categories in 2014. The survey reveals that the outlook for 2014 moved each category up one position. Investment and homebuilding are now considered "fair," up from "modestly poor" and "poor," respectively. The development outlook also improved in the survey and now stands at "modestly poor," up from "poor." These improvements were stronger than those in a number of other markets, resulting in Sacramento's improvement in overall rank.

Cincinnati (41). In this year's survey, Cincinnati declined three spots to number 41. Survey respondents increased their outlook for the market in 2014, but the outlook for investment and homebuilding was not enough to keep up with other markets. The survey did show that the outlook for development did improve when compared with the rest of the markets. The outlook for each category remains in the "fair" range.

Columbus (42). Columbus slipped two spots to number 42 in this year's survey. The good news for the state capital is that 2014 survey respondents see the outlook improving next year. Respondents gave Columbus higher scores for investment, development, and homebuilding. The current outlook for each category remains in the "fair" range. The improved development outlook is supporting the city's overall market ranking.

Oklahoma City (43). In this year's survey, Oklahoma City dropped 11 spots to number 43. The 2014 survey respondents have a less favorable outlook for Oklahoma's largest city. The outlook for investment and development is down in this year's survey, but remains in the "fair" range. The outlook for homebuilding did rise, but the increase was not enough to keep pace with other markets.

Tucson (44). Unchanged from its ranking in 2013, Tucson remains at number 44 this year. The 2014 survey respondents raised their outlook for investment, devel-

opment, and homebuilding in Tucson. The 2014 outlook for investment and homebuilding remain "fair." Next year's outlook for development improved, but remains "modestly poor."

Milwaukee (45). Moving down four spots from 2013, Wisconsin's largest city stands at number 45 in this year's survey. Survey respondents have an improved outlook for Milwaukee in 2014, but this improvement hasn't been enough to keep up with the outlook in other markets. The outlook for investment, development, and homebuilding remains "fair."

Albuquerque (46). New Mexico's largest city continues to slip in the survey, falling four positions to number 46. Survey respondents this year see an improved outlook for Albuquerque in 2014. The improvement is modest for investment and development but more substantial for homebuilding. The outlook for investment and homebuilding remains "fair," while the outlook for development is "modestly poor." The decline in Albuquerque's overall rank is attributable to a failure of this improvement to keep pace with other markets.

New Orleans (47). In the 2014 survey, New Orleans stands at number 47—the same position it occupied in 2013. The city received a slightly improved outlook for 2014. Respondents to this year's survey see the outlook for investment, development, and homebuilding being better next year. The outlook for investment and development remains "modestly poor," and "fair" for homebuilding. This improvement was strong enough to keep New Orleans's overall position unchanged.

Memphis (48). Memphis declined three spots in the 2014 survey to number 48. This year's survey shows that respondents feel somewhat better about Memphis for 2014. The survey shows that the outlooks for investment, development, and homebuilding all improved for 2014, although they remain in the "modestly poor" range.

Cleveland (49). Dipping slightly this year, Cleveland fell one spot to number 49. The 2014 survey respondents slightly raised their outlook for investment, development, and homebuilding in Cleveland. The improvement keeps the outlook in the “modestly poor” range, and with the exception of the development outlook, Cleveland lost ground to other markets in the survey.

Providence, Rhode Island (50). This year, the capital city of Rhode Island drops four spots to number 50. Survey results were not enough for Providence to keep pace with the other markets in the survey. The outlook for development in 2014 actually declined, but remains in the “modestly poor” range. The 2014 outlook for investment and homebuilding did rise, but these categories also remain “modestly poor.”

Detroit (51). At number 51, Detroit remains at the bottom of the survey—the same position it occupied in 2013. The weakness in the outlook for Detroit is universal. Survey respondents interpret the outlook for investment, development, and homebuilding as being at the bottom of all the markets in the survey. If there is a bright spot, it is that respondents did raise the overall score for development and homebuilding. Unfortunately, respondents still see the outlook as “poor.”



Property Type Outlook

“If you are a long-term investor, the industrial sector just keeps doing better, even if it’s not glamorous.”

Healing Properties

Survey results and interviews with industry participants note growth in demand sufficient to improve fundamentals in 2014, opening up investment and development opportunities even with the prospect of increasing interest rates. The ability of the U.S. commercial real estate market will improve across the full spectrum of property types.

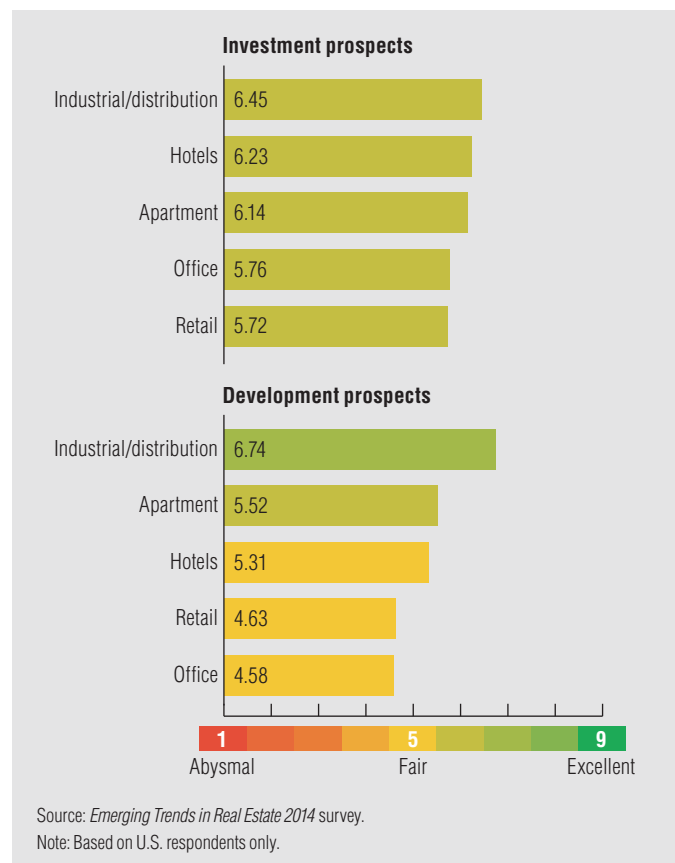
“Overall, we’re in the fifth inning,” says a commercial banker, “but it feels like this cycle is happening much faster than the last cycle.” And millennials are leaving their imprint on almost every sector. In addition to urban rental housing and more collaborative office configurations, “Technology demand for the millennials has been a game-changer, and this has positively impacted the retail and industrial sectors,” says a real estate investment adviser.

The industrial and distribution sector leads the way for both investment and development prospects in 2014, according to *Emerging Trends* survey respondents, with expected prospects rising to almost the same level as the apartment sector last year. “If you are a long-term investor, the industrial sector just keeps doing well, even if it’s not glamorous,” says an industrial real estate investor.

Hotels are a strong second to industrial and distribution investment prospects. Development prospects for hotels are expected to strengthen but remain third in the overall rankings. As a real estate adviser notes, “Hotels continue to do well primarily because not many are being built, and demand is coming back from [an increase in] business travel and tourism.”

Apartment development prospects are expected to decline significantly in 2014 over 2013, according to the ratings provided

EXHIBIT 4-1
Prospects for Major Commercial Property Types in 2014



by survey respondents but remain second to the industrial and distribution sector. “The peak of supply is coming next year,” says a mortgage banker. Apartment investment prospects are expected to slip and are ranked third behind the industrial and distribution and hotel sectors.

As job growth continues, activity in the retail and office sectors is expected to step up with development prospects in both sectors strengthening noticeably, although, in relative terms, they remain the lowest-rated sectors. “The retail store is not going away. But its place in the whole mix has changed and will continue to evolve,” declares a shopping center developer. Investment prospects are not expected to change much, with the retail sector improving modestly and office investment prospects just inching up.

Housing prospects for almost all residential property types showed at least moderate improvement in this year’s survey,

with strong jumps in expected prospects for single-family moderate- and high-income housing. The attraction of urbanization is again reflected in the high rating received by infill and intown housing. This perennial first-place choice for best prospects is followed by seniors’ housing and the single-family sector. Even condominiums and second/leisure homes made great strides in improved prospects, although they remain among the lower-rated housing types.

Respondents expect cap rates to move up slightly by the end of 2014. Warehousing and research and development (R&D) industrial are the only property types for which respondents don’t expect to see much of an increase in expected cap rates.

EXHIBIT 4-2
Prospects for Commercial/Multifamily Subsectors in 2014

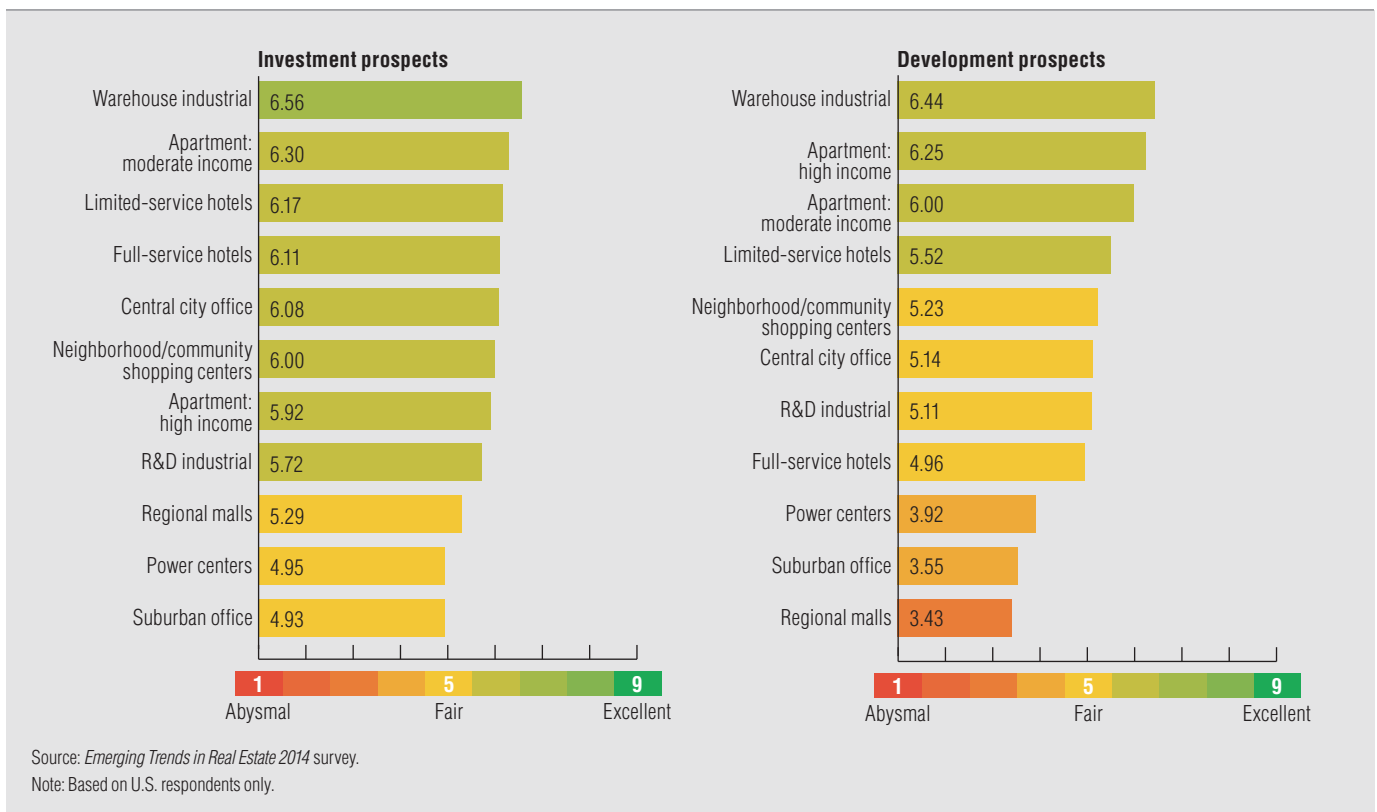
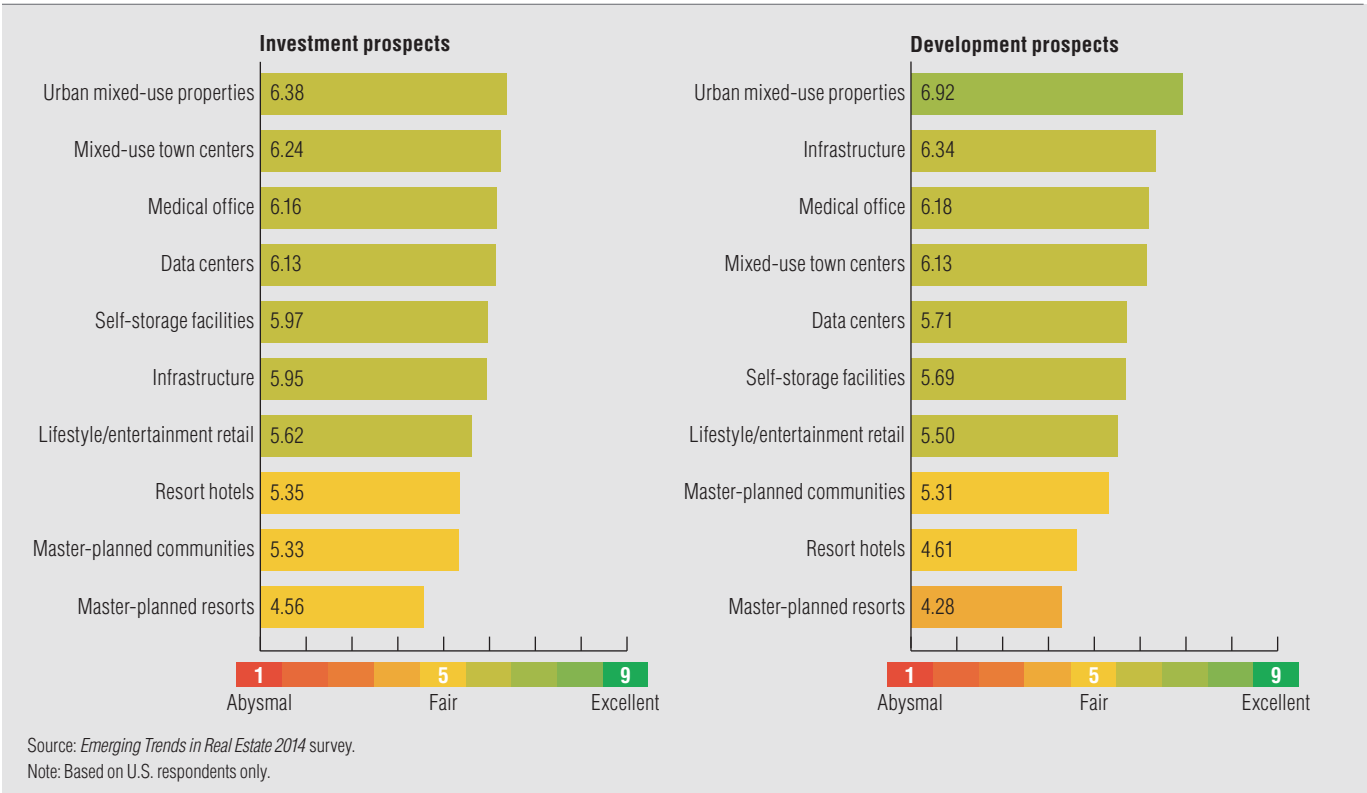


EXHIBIT 4-3

Prospects for Niche and Multiuse Property Types in 2014



Industrial

Industrial real estate will get a boost in 2014 as the U.S. economy continues to improve and as retailers and manufacturers have made the shortening of the supply chain their top priority for the foreseeable future.

Warehousing stands out as the strongest prospect in both investment and development in 2014—not only among industrial subsectors and niche markets, but across all types of subsectors and niche markets. (Only development prospects for urban mixed-use properties are rated more highly.) Warehousing is a clear favorite when survey respondents recommended action: this subsector received the most “buy” recommendations of all sectors—almost 64 percent of survey respondents made this recommendation, with 27 percent saying “hold” current assets and less than 10 percent recommending “sell.”

The strength of warehousing reflects the expanding influence of e-commerce distribution networks. For online retailers, this means building vast fulfillment centers near major cities to compete for same-day delivery capacity. “Electronic retailing is impacting the whole distribution program. Facilities are being built to enable same-day delivery—huge buildings, fulfillment centers in areas where we’ve never seen warehouses before,” says a logistics executive.

Investment and development prospects for the R&D industrial subsector, though not among the top rated, nonetheless are expected to improve, likely fueled by growth in the medical and technology fields. Respondents were more cautious about

the prospects for this subsector, with only 36 percent making a “buy” recommendation.

Self-storage and data centers also are expected to improve for both investment and development. Says one investment adviser, “Three years ago, no one would touch a self-storage property. Now, self-storage is one of the darling property types. That is really because investors have chewed down other types of properties.” Another adviser observes, “Self-storage is doing well, partly because of the recession, when people had to move out and put their stuff somewhere.”

In making buy/hold/sell recommendations for the total industrial sector by metropolitan area, respondents put Miami at the top of the list, with over 60 percent of respondents rating the city as a “buy.” The next top four industrial markets—Houston, Seattle, Los Angeles, and Dallas—are all global distribution hubs with healthy local economies.

The Return of Manufacturing

Industrial space in general will also benefit from the shortening of supply networks through the “reshoring” of factories to the United States and the elimination of a long supply chain across the Pacific Ocean, for example, which many companies have concluded is no longer worthwhile as labor costs in China rise. “Manufacturing is coming back to the U.S., and it’s coming back faster than we thought. Back in 2011, no one thought we would see anything until 2015. Now, we are seeing dozens of

EXHIBIT 4-4

U.S. Industrial Completions and Availability Rates

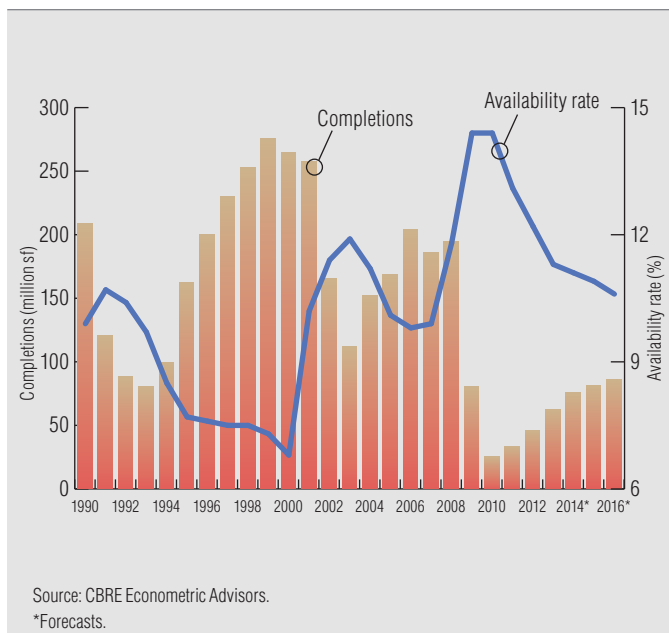
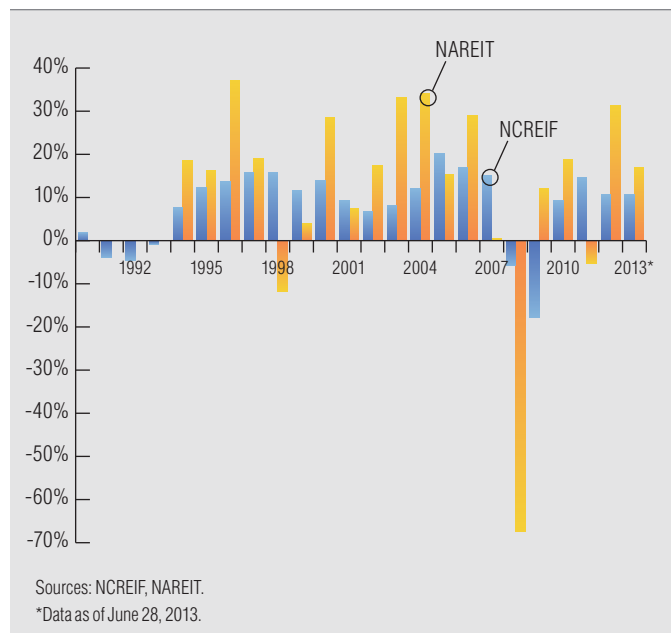


EXHIBIT 4-5

U.S. Industrial Property Total Returns



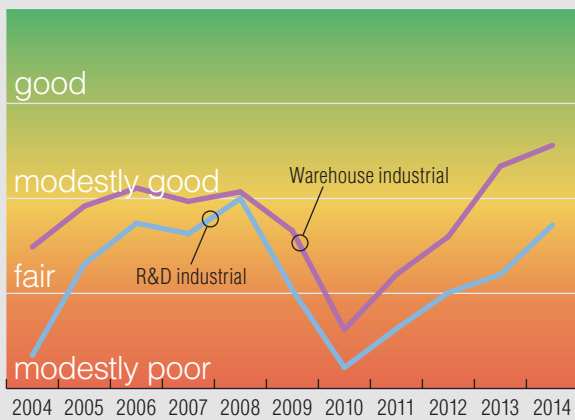
companies moving back to the U.S. because the economics are shifting,” says a labor economist. “A key driver of this trend is that labor costs in China are rising, with wages increasing by about 15 to 20 percent a year and the steady appreciation of the Chinese yuan against the dollar. Manufacturers are seeing very long supply chains, and there are increasing concerns about intellectual property. They were willing to accept all that before, but no longer because there’s less of an advantage in labor costs.”

New factories are also opening up in some surprising locations—and in some unexpected industries. In January 2013, a semiconductor manufacturer announced plans to build a facility in Saratoga County, New York, to support technology development and manufacturing activities. And it’s not just American manufacturers that are looking to shorten their supply chain. In June 2013, an Asian computer producer opened a personal-computer assembly plant in Whistett, North Carolina. Low U.S. energy costs are fueling this trend as well.

Upcoming: The Panama Canal

Finally, in anticipation of the opening of the Panama Canal expansion in 2015, “ports along the East and West Gulf coasts are all reacting, trying to make themselves ports of call for the much bigger ships that will be able to get through the canal,” says an industry association executive. Intermodal rail and trucking companies that serve those ports are also investing. By 2014, this interviewee expects to see “some impact on warehouse and factory location, and more so once the canal reopens in 2015.”

EXHIBIT 4-6
Industrial/Distribution Investment Prospect Trends



Source: *Emerging Trends in Real Estate* surveys.

U.S. warehouse industrial

2014	Prospects	Rating	Ranking
Investment prospects	6.56	Good	1st
Development prospects	6.44	Modestly good	1st
Buy		Hold	Sell
63.5%		26.9%	9.6%
Expected capitalization rate, December 2014		6.7%	

U.S. R&D industrial

2014	Prospects	Rating	Ranking
Investment prospects	5.72	Modestly good	8th
Development prospects	5.11	Fair	7th
Buy		Hold	Sell
36.0%		41.6%	22.4%
Expected capitalization rate, December 2014		7.5%	

Source: *Emerging Trends in Real Estate 2014* survey.

Note: Based on U.S. respondents only.

Hotels

The trajectory of the hotel sector is favorable, especially for limited-service hotels. Some interviewees even say that hotels are “almost back to peak levels,” or are seeing “tremendous activity.” In the 2014 *Emerging Trends* survey, both limited-service and full-service hotels moved up in investment ranking among the commercial and multifamily subsectors to third and fourth place, respectively, just behind warehousing and moderate-income apartments. This boost parallels the nation’s economic recovery, and as travel increases the hospitality industry will continue to expand and benefit from the increased demand. This sustained recovery is likely to come in part from “corporate travel—the bread and butter of the industry,” according to a manager of a portfolio of hotels.

Limited-service hotels are expected to perform better than their full-service counterparts. As one fund manager opines, “High-quality ‘select-service’ hotel brands where the interior design, look, touch, and feel tend to mimic full-service hotels will continue to proliferate.” Conversely, there will be “a continued dramatic decline in development of new classic ‘full-service’ hotels,” asserts a financial adviser specializing in commercial real estate. “Some of the higher-end hotels [and] resorts will suffer due to lower levels of discretionary spending.” However, brands will adapt to consumer needs “by providing an ‘experience’ that customers are willing to pay for,” states the president of a luxury hotel firm.

Another concern is that although “the sector is performing well, it is likely that growth is slowing and the upside will be limited in the future,” according to an investor. A hospitality company’s chief executive officer remarked that supply may come back more quickly than demand, and “new hotels in high-performing markets can really hurt the market.” Other worries are a rise in interest costs and regulation. Ultimately, however, in the words of a fund manager, “In an environment of an improving economy, there is more demand for offices, hotels, self-storage, etc., so you get an improvement in both volumes and pricing,” offsetting potential issues.

With 48 percent of survey respondents making a “buy” recommendation on limited-service hotels, this subsector ranks second to warehousing, although, unlike in the warehousing sector, the remaining recommendations are almost equally split between “hold” and “sell.” Forty-one percent made a “buy” recommendation for full-service hotels.

Recommendations for the total hospitality sector by metro area put Miami at the top of the list, up from fifth place last year, with 57 percent of respondents rating the city as a “buy.” San Francisco and New York City follow, with Houston in fourth place for “buy” recommendations. Houston moved up from tenth place last year and the percentage of respondents recommending “buy” increased from 30 percent to 50 percent. Boston is in fifth place.

EXHIBIT 4-7
U.S. Hotel Occupancy Rates and RevPAR

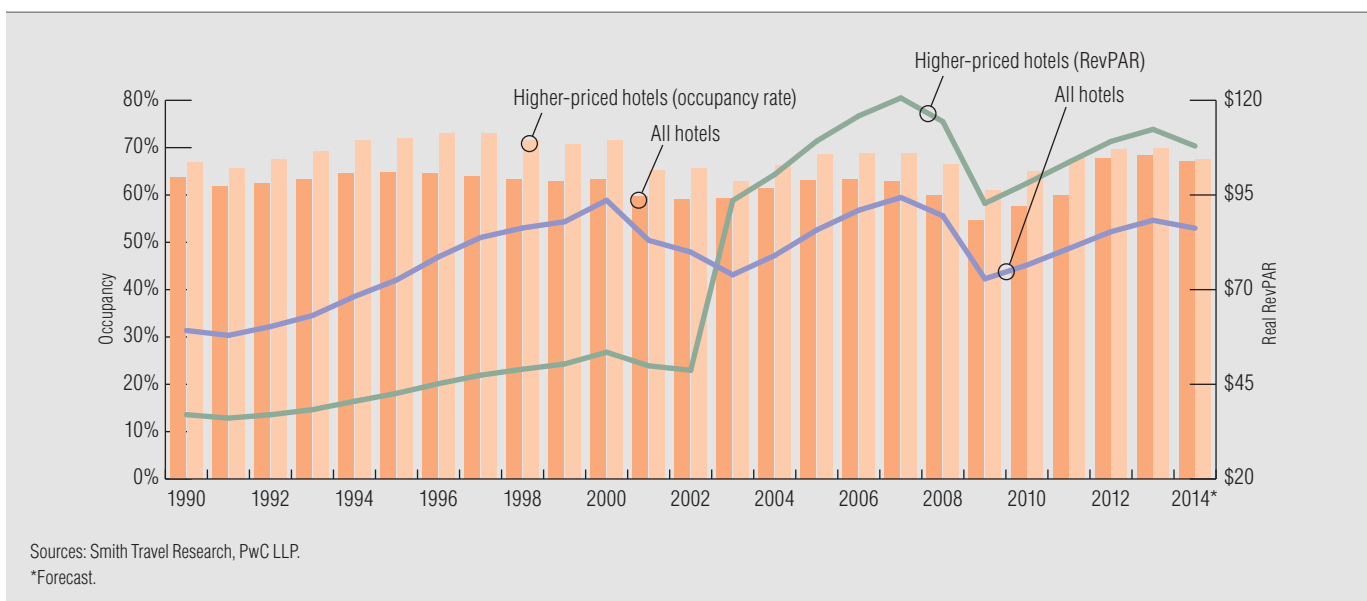
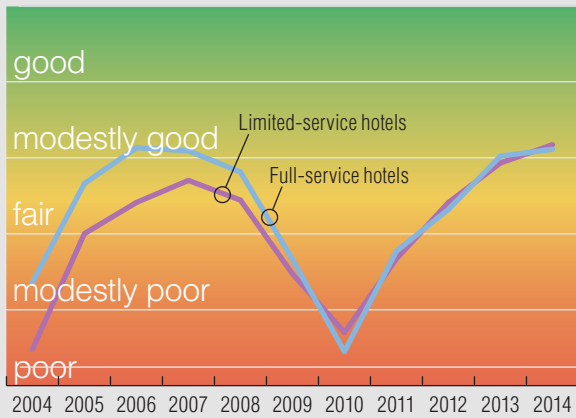


EXHIBIT 4-8

Hotel Investment Prospect Trends



Source: *Emerging Trends in Real Estate* surveys.

U.S. hotels: limited service

2014	Prospects	Rating	Ranking
Investment prospects	6.17	Modestly good	3rd
Development prospects	5.52	Fair	4th
Buy		Hold	Sell
48.1%		28.6%	23.4%
Expected capitalization rate, December 2014		8.3%	

U.S. hotels: full service

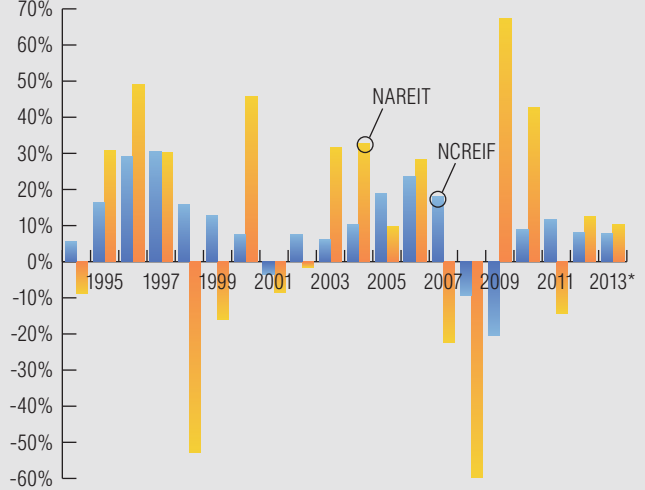
2014	Prospects	Rating	Ranking
Investment prospects	6.11	Modestly good	5th
Development prospects	4.96	Fair	6th
Buy		Hold	Sell
40.8%		36.8%	22.4%
Expected capitalization rate, December 2014		7.5%	

Source: *Emerging Trends in Real Estate 2014* survey.

Note: Based on U.S. respondents only.

EXHIBIT 4-9

U.S. Hotel/Lodging Property Total Returns



Sources: NCREIF, NAREIT.

*Data as of June 28, 2013.

Apartments

Moderate- and high-income apartment development prospects, as well as moderate-income investment prospects, remain among the strongest of all sectors rated for 2014 by the *Emerging Trends* survey respondents. But, unlike last year, when apartment prospects outshone the prospects of all other sectors, these apartment ratings are slightly lower this year, placing them behind warehousing. And investment prospects for high-income apartments are lower than those for a wide range of commercial subsectors.

The declining appetite for investing in high-income apartments is reflected, in part, in the sharp drop in “buy” recommendations from 44 percent in 2013 to 21 percent in 2014. Moderate-income apartments show their strength with an increase in “buy” recommendations for 2014 over 2013—38 percent versus 28 percent, respectively.

Does New Supply Pose a Risk?

Many interviewees expressed a sentiment similar to the one expressed by a real estate analyst who said that apartments will be “fully supplied, not oversupplied” in 2014. The apartment sector may “flirt with overbuilding, but this industry can lay off the gas pedal fairly quickly.” Even with a strengthening of the single-family housing market, many interviewees are optimistic that multifamily will adjust appropriately.

That’s not to say there won’t be isolated pockets of overbuilding, particularly in the luxury market. “The peak of supply is coming this year and next year,” says a REIT executive. “Then what happens? If interest rates move up, can we get the rent to justify new supply? At some point, if costs are going up, how much farther can we push the rents?”

Overall, even with a slight uptick in vacancy rates projected as additional units come on the market, rates are projected to remain relatively low in 2014 and for even several years beyond, according to REIS.

Multiple Sources of Demand

Millennials (or ‘gen Yers’), who show a preference for living in a walkable, urban area, regardless of the size of the city where they live, will continue as a strong source of demand. They are less likely to buy their own homes, according to *America in 2013: A ULI Survey of Views on Housing, Transportation, and Community*. Drawing from a statistically representative sample, the study indicates that 54 percent of gen Yers rented their primary residence in 2013, compared with 32 percent of all adults in the United States. Of those gen Yers who are very likely to move within five years, 69 percent expect to rent, compared with 25 percent of all adults.

At the same time, baby boomers are selling their houses to rent apartments within walking distance of downtown areas or moving into centers for active seniors. “There is a growing demand for projects that target residents who are 55 and older. They want high ‘walk scores’ and access to entertainment, amenities, and quality health care,” says the CEO of a commercial real estate firm.

At the lower end of the age spectrum, some investors favor student housing “because it is not cyclical,” says an institutional real estate adviser. “Because most colleges no longer build new dorms, the sector will remain strong.”

EXHIBIT 4-10
U.S. Multifamily Completions and Vacancy Rates

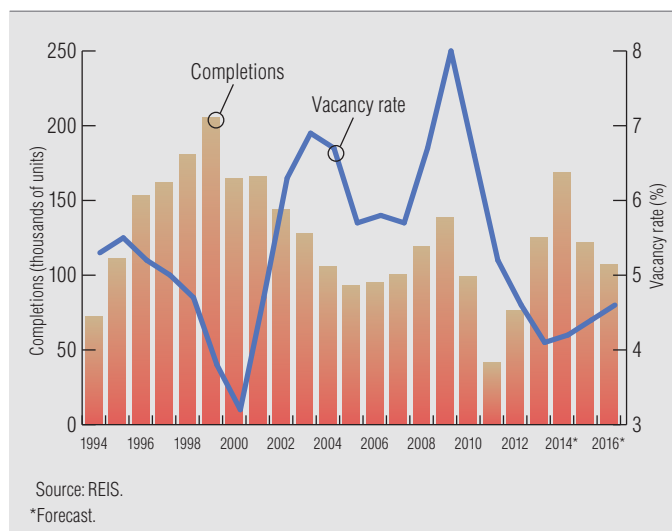


EXHIBIT 4-11
Multifamily Units under Construction

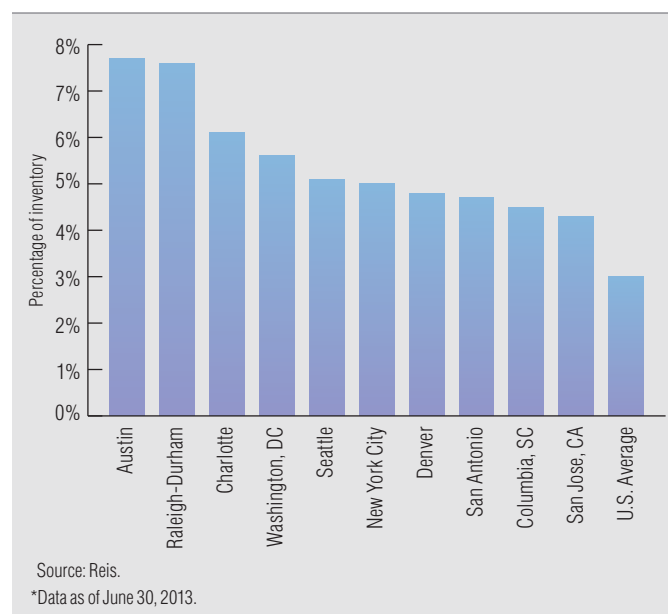
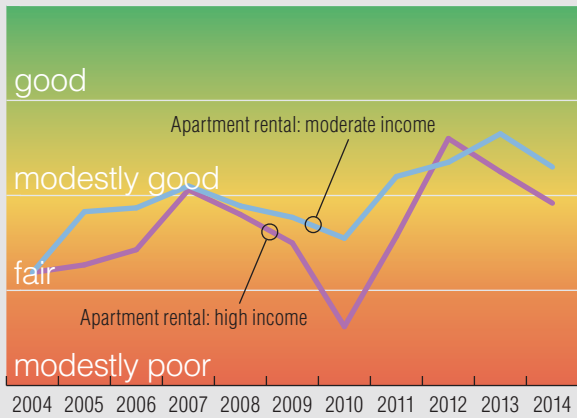


EXHIBIT 4-12

Apartment Investment Prospect Trends



Source: *Emerging Trends in Real Estate* surveys.

U.S. high-income apartments

2014	Prospects	Rating	Ranking
Investment prospects	5.92	Modestly good	7th
Development prospects	6.25	Modestly good	2nd
Buy	Hold		Sell
21.3%	35.2%		43.5%
Expected capitalization rate, December 2014		5.4%	

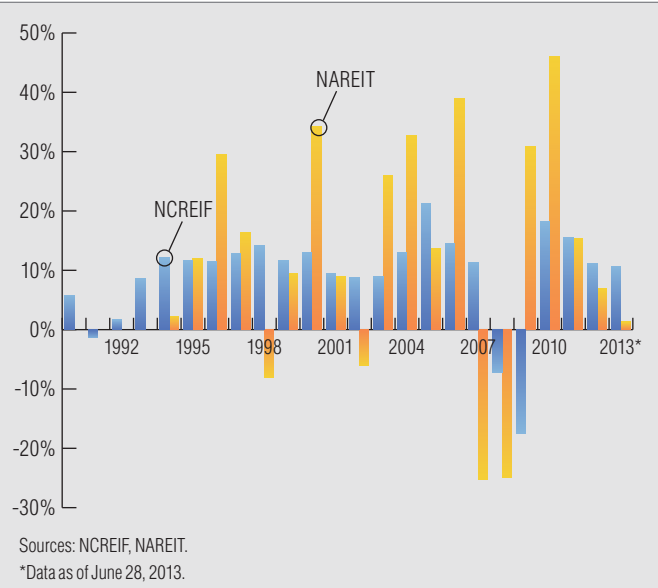
U.S. moderate-income apartments

2014	Prospects	Rating	Ranking
Investment prospects	6.30	Modestly good	2nd
Development prospects	6.00	Modestly good	3rd
Buy	Hold		Sell
37.6%	34.3%		28.1%
Expected capitalization rate, December 2014		6.2%	

Source: *Emerging Trends in Real Estate 2014* survey.
 Note: Based on U.S. respondents only.

EXHIBIT 4-13

U.S. Apartment Property Total Returns



Sources: NCREIF, NAREIT.
 *Data as of June 28, 2013.

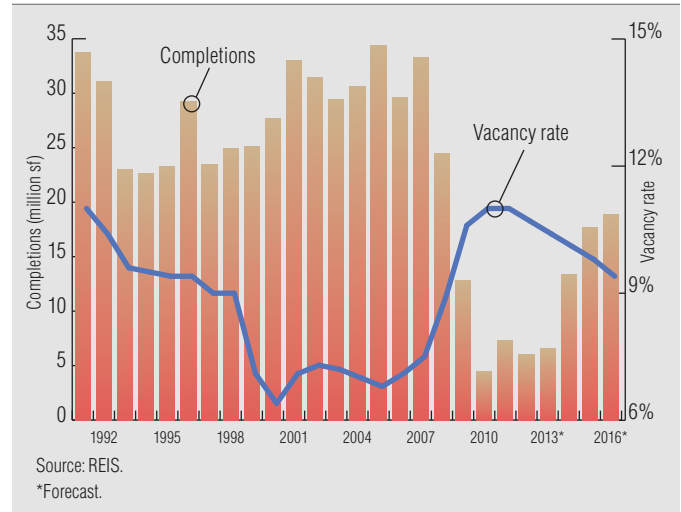
Retail

“Retail has been slower to rebound than other property types,” explains a commercial banker, and a real estate adviser adds, “With improved GDP and steady employment growth, 2014 marks the first time that retailers are expanding.”

Because of increased levels of e-commerce, retail is expected to become leaner in the future. “Technology is enabling merchants to get by with much less inventory, [which] means they need less space,” a real estate service provider points out. “At the other end of the supply chain, the buyer’s journey [has] changed a lot.” As a result, “Retailers continue to rethink size requirements,” says the CEO of an investment firm. Less square footage per site and the gradual decline of big-box stores is where many interviewees predict retail is headed in the near future. One investor believes, “The need for big department stores is declining, and the end of their world may occur in five years.”

On the other hand, a shopping center developer notes that while “retailers are running out of opportunities in suburbs, urban environments [retail alone or with residential on top] will continue to be attractive.” Multiple firms are “seeing [the] millennial generation focusing on urbanism, plus a combination of private developers and government programs [is] pursuing the redevelopment of infill locations,” according to the president of a retail REIT. Prospects for mixed-use urban developments are high, tied as they are to these changing demographics. One shopping center owner further observes, “The path of growth for retail is no longer out toward the suburbs. Everyone is looking to move back into the city and to find an adaptable business model that can tap this underserved segment.” In fact, urban mixed-use properties were a clear favorite among survey

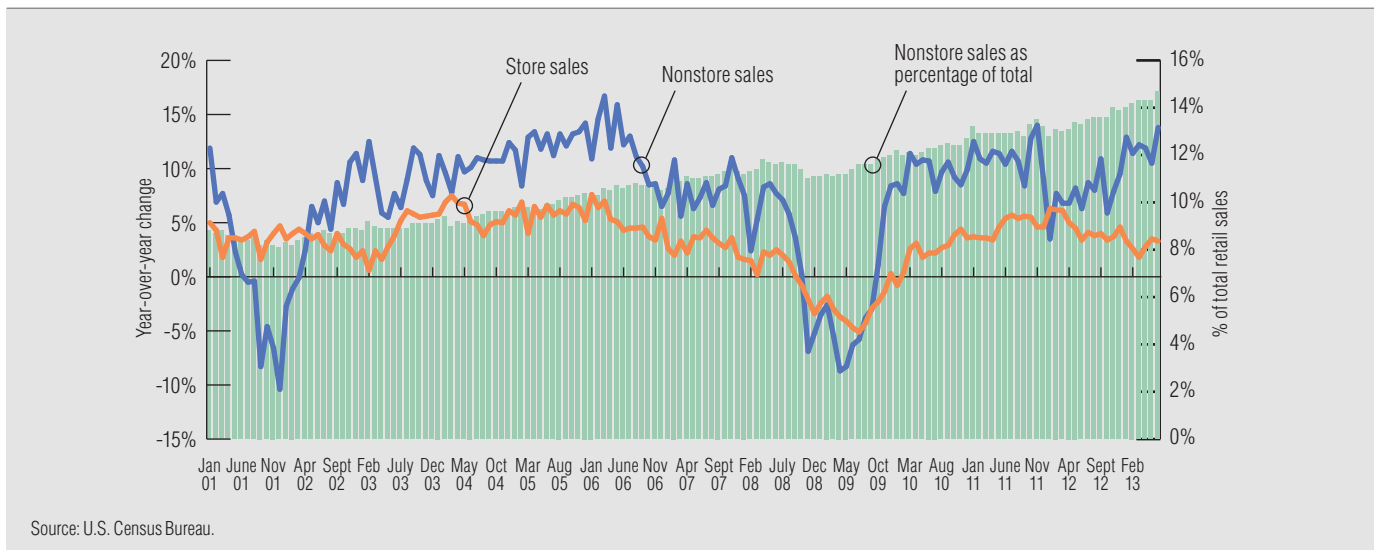
EXHIBIT 4-15
U.S. Retail Completions and Vacancy Rates



respondents, who rated this sector the highest of all sectors for expected development prospects in 2014. Prospects for investment in urban mixed-use properties were expected to be almost as strong.

In addition, “High-end is holding up well,” says an investment manager. This submarket is profiting because of its low probability of substitution with other mediums as well as location of this type of retail in entertainment districts. However, the middle range is suffering, as it is “most susceptible to internet competition.”

EXHIBIT 4-14
Retail Sales: Year-over-Year Change



“Overall, retail is showing itself to be resourceful and is bouncing back,” concludes a shopping center owner, reiterating a sentiment shared by multiple interviewees. “Consumer confidence is increasing,” notes a banker, and retail—especially in urban infill areas—is expected to improve along with it.

Neighborhood/community shopping centers were the most highly rated among retail sectors for investment prospects, rising slightly from last year’s rating. Close to 50 percent of respondents recommended “buy” for this sector, as compared with only 18 percent who recommended “buy” for power centers. Development prospects for neighborhood/community shopping centers stepped up but remain just fair.

Some interviewees see what they describe as a long-needed renovation of shopping malls that lost tenants during the recession and are now in the process of being spruced up. “Retail needed that in the worst way,” says a fund manager.

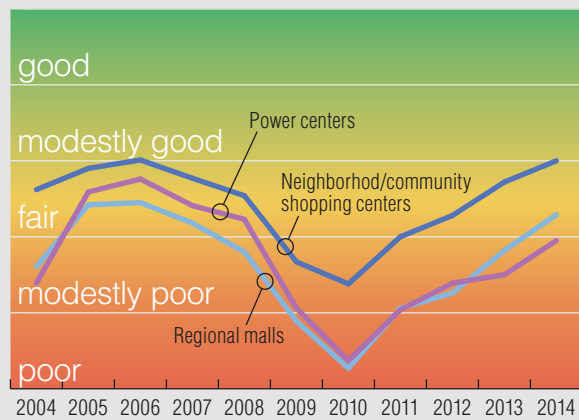
The Online Challenge

To adjust to the increase in online shoppers, retailers are looking at a variety of approaches ranging from using stores more as showrooms to using them as quasi-distribution centers. “Brick-and-mortar” retail will continue to converge with online shopping as all retailers become progressively drawn into competition with Amazon to deliver goods to customers on the same day they are ordered. Stores will increasingly fill online orders from their own shelves, effectively blurring the line between retail and warehouse space.

“We will see more subtle, if not more dramatic, ways in which retailers use real estate to facilitate a bichannel approach

to retail to adapt to an economy that has a large percentage of its commerce going on over the internet. While one retailer decreases its footprint from 14,000 to 9,000 [square] feet, another opens up more distribution warehouses for same-day delivery. Those lines are converging,” says a logistics executive.

EXHIBIT 4-17
Retail Investment Prospect Trends



Source: *Emerging Trends in Real Estate* surveys.

U.S. neighborhood/community centers

2014	Prospects	Rating	Ranking
Investment prospects	6.00	Modestly good	6th
Development prospects	5.23	Fair	5th
Buy		Hold	Sell
47.1%		35.8%	17.1%
Expected capitalization rate, December 2014		6.9%	

U.S. power centers

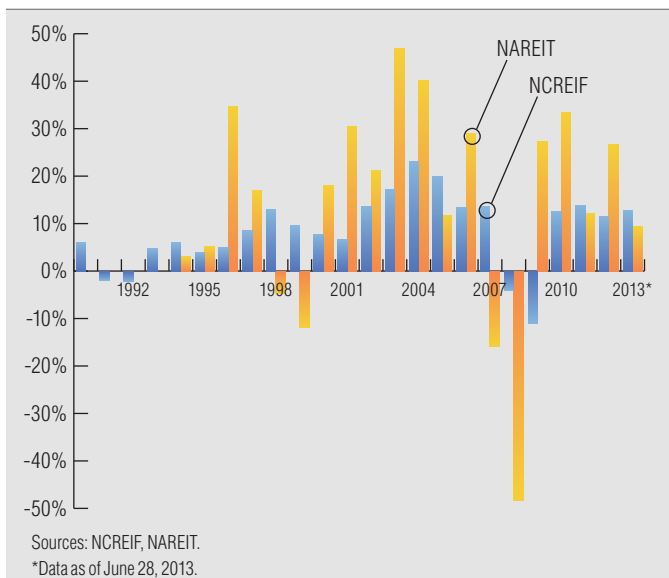
2014	Prospects	Rating	Ranking
Investment prospects	4.95	Fair	10th
Development prospects	3.92	Modestly poor	9th
Buy		Hold	Sell
18.0%		42.7%	39.3%
Expected capitalization rate, December 2014		7.3%	

U.S. regional malls

2014	Prospects	Rating	Ranking
Investment prospects	5.29	Fair	9th
Development prospects	3.43	Poor	11th
Buy		Hold	Sell
20.0%		52.6%	27.4%
Expected capitalization rate, December 2014		6.2%	

Source: *Emerging Trends in Real Estate 2014* survey.
Note: Based on U.S. respondents only.

EXHIBIT 4-16
U.S. Retail Property Total Returns



Sources: NCREIF, NAREIT.
*Data as of June 28, 2013.

Office

Perhaps more than any other property type, office space will struggle to find pockets of new demand in 2014. In the *Emerging Trends* survey, respondents continue to rate central city offices among the better sectors for investment but only fair for development; suburban office is the lowest rated of all sectors for investment and among the lowest for development.

Still, some *Emerging Trends* survey respondents see potential for office space in general in 2014, with 42 percent of them rating the central city office sector as a “buy” and 30 percent rating suburban office as a “buy.” Boston still tops the survey, but none of the five cities immediately following is among the half-dozen cities that have dominated office space in recent years. Four of them—Houston, San Diego, Seattle, and Denver—derive their economic growth from technology or energy. Phoenix, which is also in the top five, may well be considered a recovery play.

Efficiency in Demand

Companies are learning to get by with fewer employees while taking up less space per employee as they allow more employees to work at home and squeeze others into denser office layouts. “There is this constant trend to get more productivity and efficiency out of office space. It will lead to a slower tightening of the office market,” says a leasing broker. “We are seeing more people being put in less space than ever.” A case in point is a new office building that is under construction in Boston that is designed for nine people per 1,000 square feet. “That is unbelievable density,” says an institutional investment adviser who is familiar with the project. “The highest [density] I have ever heard was five people per 1,000 square feet.”

EXHIBIT 4-18

U.S. Office New Supply and Net Absorption

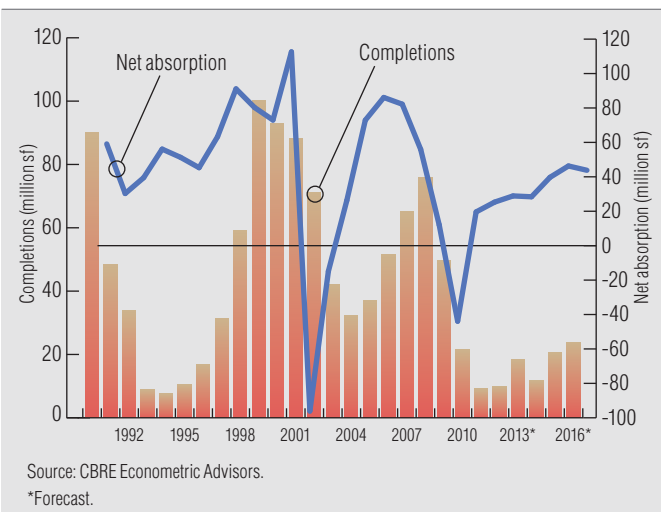
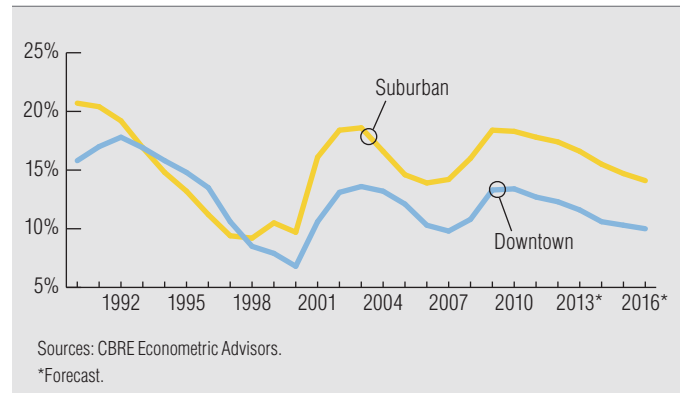


EXHIBIT 4-19

U.S. Office Vacancy Rates



The pressure of densification on the office market will have sobering implications for rents in 2014. “Some of the larger corporate occupiers are rolling over leases, with more employees than when they originally signed the lease. So they are able to keep the same amount of space at less space per employee, increase the number of employees, and therefore become more efficient. So it is not that they are spending less money. They are just increasing density and improving their efficiencies and lowering their cost per employee,” says a real estate service provider.

“Companies have some reluctance about making permanent hires. Companies want to remain short so they can adjust and use contractors, temporary employees, and part-time employees. It may stunt growth in jobs overall. The cost of health care is the number-one reason,” says a real estate investment adviser. Office workers can work at home “because of what the smartphone has done. It lets you work out of the house,” says a developer.

Yet, office space will still fare better in 2014 than its reputation would lead one to believe. One factor working to the advantage of the sector is that it did not build into oversupply. “In office space, bankers and developers have not allocated that money toward speculative office development, which we think is very constructive. We are glad to see that level of discipline. Given that job growth is still suffocated, we would not expect there to be a sea change in the volume of speculative development starting any time in the near term. Maybe in deliberate small doses, but not a sea change,” explains a commercial developer and property manager.

In addition to workspace efficiencies, an office developer notes that “there will continue to be a relentless pursuit of more efficiency in utilities, quality of mechanical systems, and LEED certification. It is just a matter of time before the same thing happens with LEED that happened with ADA requirements, which used to be voluntary. But now you can’t get a building permit

without meeting those criteria. We will migrate toward 'not a choice anymore,' " says an office developer.

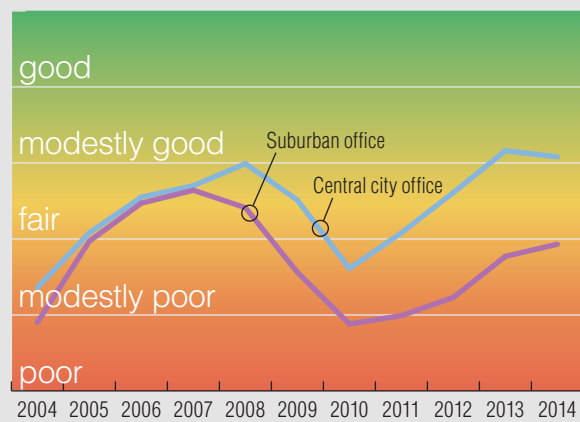
Secondary Market Attractiveness

In secondary and tertiary markets, where many of the new investments will be made in 2014 by investors with an increasing appetite for risk, densification will not be as high on the agenda of developers as in first-tier markets. "In bigger markets where rents, cost of business, and cost of living are higher, there is tremendous pressure for more densification in office space. In a mid-tier market, you don't save much at all if you save 20 percent on \$25 per square foot versus 20 percent of \$85 per square foot in New York." In smaller markets where office workers tend to drive to work, office buildings are required to provide enough parking spaces for them. That poses a limit on the extent to which an office building can densify—leading to a potential lack of parking space—as one developer explains.

As banks ease lending requirements and become more amenable to construction and development loans, office space will expand in some surprising markets. "Some of the strongest markets in the Southeast will be Greenville, Charleston, Charlotte, Raleigh, Birmingham, Nashville, and even Chattanooga. Spec industrial and office development is now feasible in certain markets. Office rents in Greenville are now around \$27 to \$28 per square foot—the first time they have reached these levels. With low vacancies, these rates can now justify new construction in downtown locations," says a commercial real estate developer.

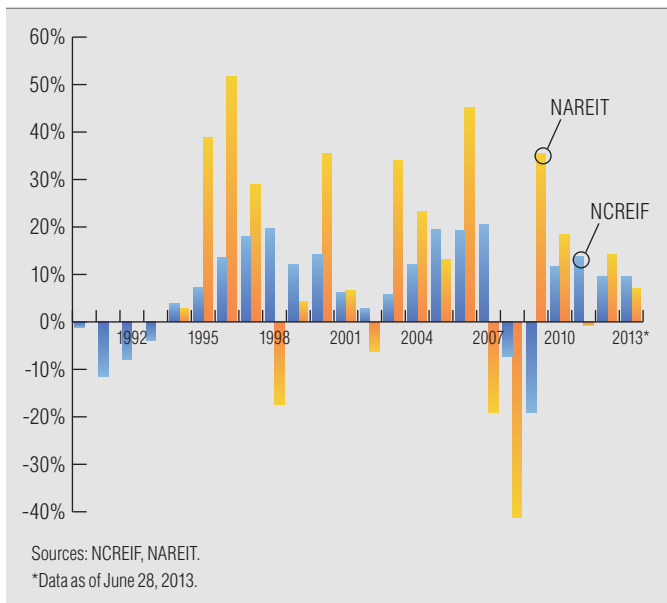
Raleigh, for example, is seeing the creation of 12,000 jobs a year, which local developers point out is only half the rate they saw before the recession. Yet many of the jobs are high-quality ones at financial services firms and technology companies. "The Class A office market has tightened," says a developer in Raleigh. "There are not many available blocks of space. Everybody who could move up has done so. The B Class space is still available, and we are finally starting to see that market tighten up. Rents are back up. We are starting to see a real rebound of well-located office properties. But the far-range suburbs are still struggling."

EXHIBIT 4-21
Office Investment Prospect Trends



Source: *Emerging Trends in Real Estate* surveys.

EXHIBIT 4-20
U.S. Office Property Total Returns



Sources: NCREIF, NAREIT.
*Data as of June 28, 2013.

U.S. central city office

2014	Prospects	Rating	Ranking
Investment prospects	6.08	Modestly good	5th
Development prospects	5.14	Fair	6th
Buy	Hold	Sell	
41.5%	19.9%	38.7%	
Expected capitalization rate, December 2014		6.4%	

U.S. suburban office

2014	Prospects	Rating	Ranking
Investment prospects	4.93	Fair	11th
Development prospects	3.55	Modestly poor	10th
Buy	Hold	Sell	
30.0%	35.5%	34.5%	
Expected capitalization rate, December 2014		7.8%	

Source: *Emerging Trends in Real Estate 2014* survey.
Note: Based on U.S. respondents only.

Housing

The survey results indicate an improved outlook for all types of residential property investment in 2014, as ratings of prospects improved across all sectors.

Infill and intown housing continues to strengthen and remains the top-ranked favorite this year for both investment and development. Housing for seniors also remains near the top with improved ratings. “The national penetration rate of seniors’ housing could double in the next 15 years from the current level of just 8 percent. We will now see more development across the country. We have an aging population and a functional obsolescence of older independent living facilities. The newer ones are more resortlike,” says an institutional real estate adviser.

The most significant changes in prospects for 2014 are expected in the single-family sector—both moderate-income and high-income housing. Investment prospects for both jumped and are now ranked just behind infill/intown housing and seniors’ housing. Development prospects also jumped for both, with moderate-income housing ranked second only to infill/intown housing and high-income single-family housing following development prospects for seniors’ housing.

This trend is illustrated in Florida markets where demand for the full spectrum of residential property types is sizzling. “Miami has clearly come back from the time when 25 cranes had all stopped in the air while building high-rise residential,” says a commercial real estate developer. “That inventory has been nearly depleted. They have gone back to building things again.” A commercial banker observes, “Single-family residential is coming back. There will be 8,000 single-family residential units built in Orlando in 2013. This sector will get stronger and stronger. There is a lot of for-sale property being built.”

Fueled by Cash

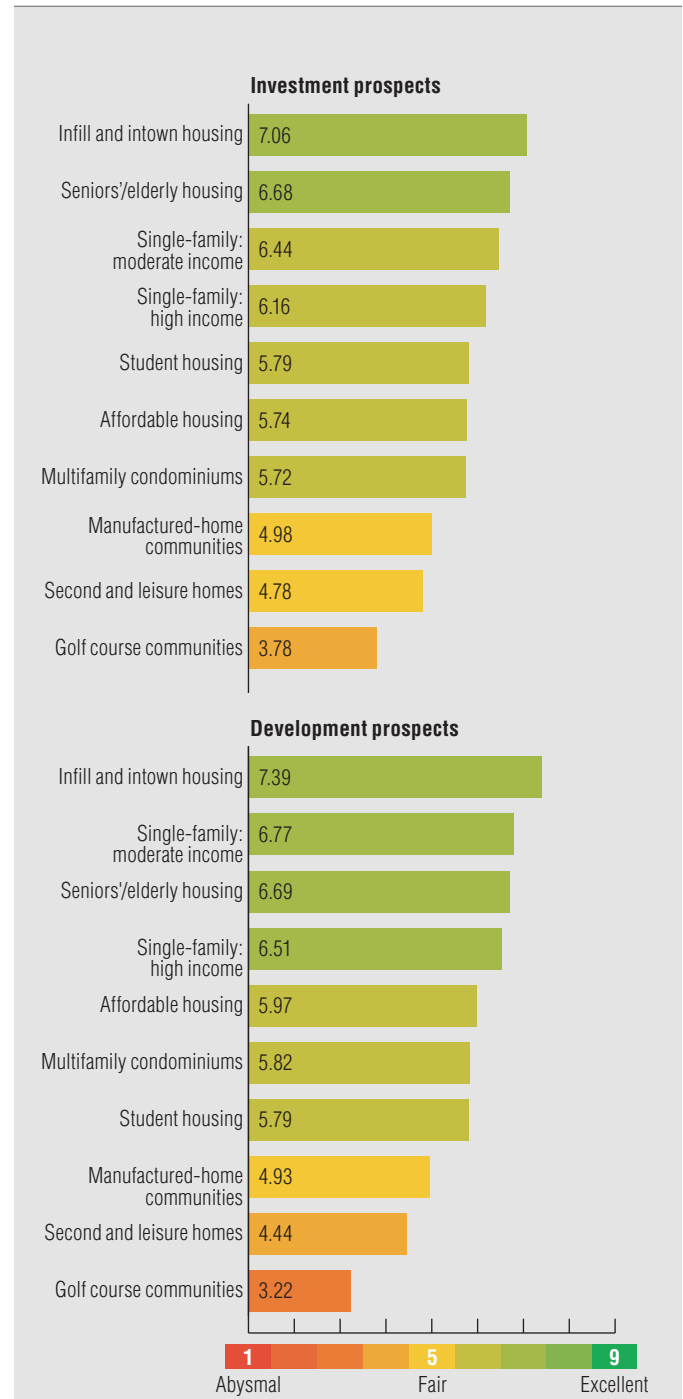
All-cash purchases represented an average of 45 percent of all residential sales in August 2013, up from 39 percent in July 2013 and 30 percent in August 2012. Miami had a higher percentage of all-cash sales—69 percent of total sales—than any other city with a population of 1 million or greater, followed by Detroit (68 percent), Las Vegas (66 percent), Jacksonville, Florida (65 percent), and Tampa, Florida (64 percent), according to RealtyTrac.

Among the investors in single-family homes are large private equity firms. “They are buying a lot of the vacant inventory and now moving into new construction. I see that as a strong trend,” says a residential developer.

Foreign investors also are playing a role in the residential market, and nowhere is this trend more evident than in Florida. “Foreign investment in single-family homes, condos, and multifamily apartments has been propping up the real estate market in Florida for the last four years, largely in the form of flight capital from Latin Americans and money from Europeans looking for second homes with a better value per square foot,”

EXHIBIT 4-22

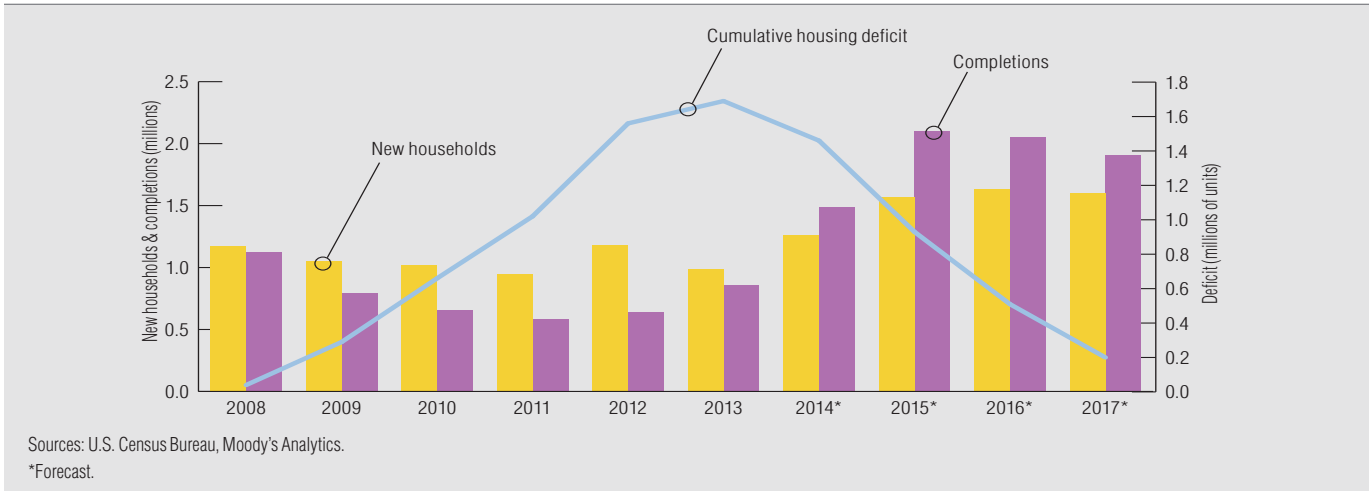
Prospects for Residential Property Types in 2014



Source: *Emerging Trends in Real Estate 2014* survey.

Note: Based on U.S. respondents only.

EXHIBIT 4-23
Housing Supply



say a commercial banker. “I see that continuing as long as the economies of the countries they come from become less of a place to keep their money. Florida is a very pro-business state,” says a residential developer.

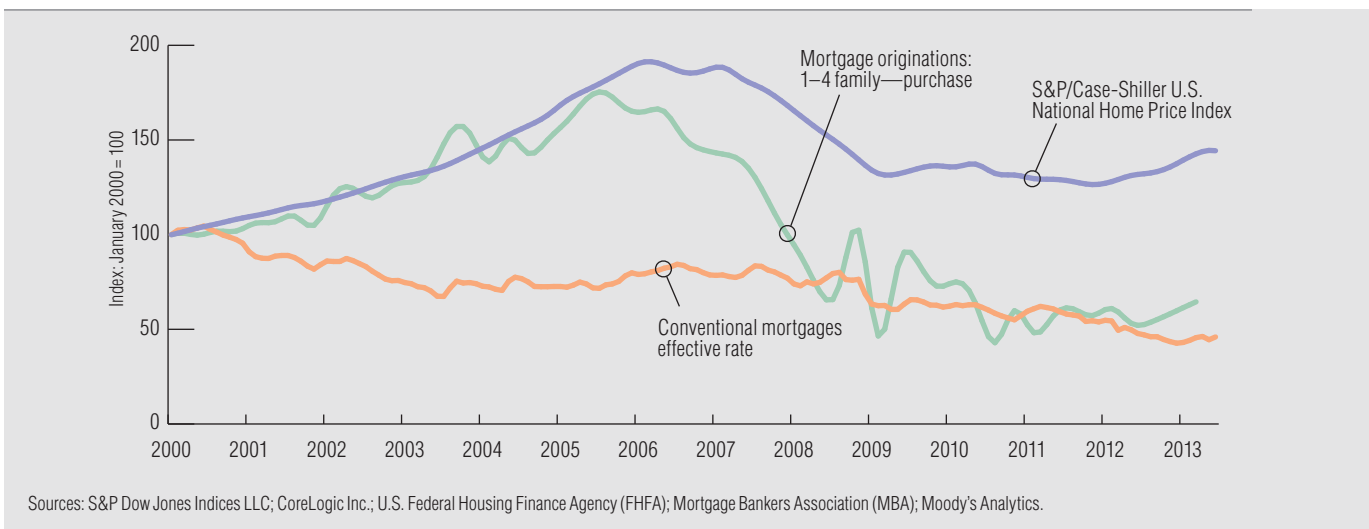
Looking Up

By midyear 2013, home prices had reached 77 percent of peak levels from a trough of 65 percent just 1.5 years before, according to the S&P/Case-Shiller U.S. National Home Price Index. And total housing construction is projected to continue to

increase in 2014, after being severely depressed for the last six years, according to Moody's Analytics' forecast (August 2013).

Still, one real estate analyst notes, “While the housing market has had a remarkable rebound, it is off a very low base and is being driven, to a significant extent, by the investor market. This may be a temporary phenomenon and will slow down as prices keep rising. What will happen to this growing inventory? Will it be sold all at once or held for the long term? Only when households are buying homes for the first time in large numbers and others are moving up, will there be a strong, stable housing market.”

EXHIBIT 4-24
Home Prices, Rates, and Originations





Emerging Trends in Canada

“The Canadian real estate market must be looked at as
a market within a market.”

The stability of the Canadian real estate market continues to attract positive attention from domestic and international investors. These market participants range from sovereign wealth funds to experienced local market investors. While the overall market could easily be described as “healthy,” the current real estate and capital market environment requires that each investment be carefully evaluated on its own merits. As one fund manager puts it: “The real estate market must be looked at ‘as a market within a market’—submarkets within cities must be reviewed to locate prime/central markets, all of which have different dynamics. The averages [e.g., cap rates, vacancies, IRRs (internal rates of return), etc.] can be meaningless within cities. The challenge is to understand the submarket in each area.”

Canada’s real estate market avoided the worst of the 2008 global financial crisis, and due to steady economic growth and a lack of oversupply it remains in a good position. The current level of economic growth will support the expansion of the real estate market across all property types. The Canadian real estate market could also get a boost from improvement in the U.S. economy. A stronger U.S. economy will continue to spur economic activity between the two countries, benefiting multiple industries across Canada.

The strength of the Canadian real estate market has made it very appealing to domestic real estate investors, but these investors are not limited to local investment. Canadian real estate investors are now the largest nondomestic investors in U.S. real estate. According to Real Estate Analytics, Canadian investors purchased \$10.7 billion of U.S. properties over the last 12 months. This represents 28 percent of all nondomestic investment in U.S. real estate. Canadian institutions, pension funds, and private investors are also active in Latin America,

Europe, and Asia. The move to nondomestic investments is not due to any dissatisfaction with the local market, but reflects the sophistication of these investors as they search for diversified investment opportunities.

“Canada came out of the global financial crisis better than any other industrialized country in the world. Every office building, every warehouse is effectively full. It’s a pretty nice place to be,” says an interviewee.

Yet there are signs that Canada’s real estate market will reach a plateau in 2014. “Canada is in a holding pattern,” says one portfolio manager. “Going into the downturn, there was very little construction. We were already seeing rents at near-record levels, and seeing vacancy rates at rock-bottom levels. So it is very difficult to see substantial improvement in fundamentals.”

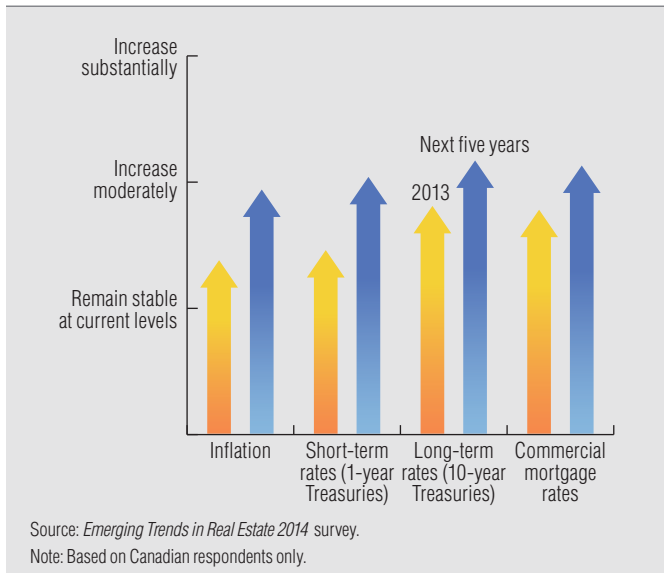
This year will be the year that investors in Canada look to the fundamentals of commercial property for “pure” yield in the form of cash flow, rather than relying on capital markets to boost real estate values. “Things will be tougher next year, but not a pitfall. It will be more of a ‘normal’ cycle. We’ll have to work the assets, [and] focus on fundamentals and adding value,” says an interviewee. “While there will still be opportunities to acquire older properties and add value, competition for good assets will get tougher in 2014 along with increased competition for capital.”

Economy in Full Bloom

Some interviewees doubt that job growth in Canada will be sufficient to support continued demand for commercial real estate. Canadian jobs are tied largely to prices for commodities such as oil, potash, and precious and semiprecious metals like gold and copper—prices which have come down with a slackening of

EXHIBIT 5-1

Inflation and Interest Rate Changes



demand in China. Though the country has more than replaced all of the jobs it has lost since the recession, an average of only 12,000 jobs were created per month during the first half of 2013. “Job growth does not bode well for real estate right now. We are running at half of last year’s rate,” says an interviewee.

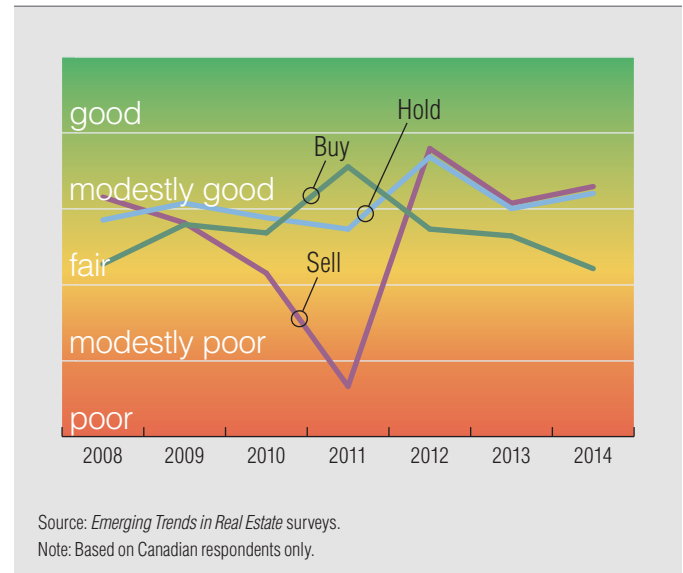
Canadian real estate investors hope to get a boost from the U.S. economy in 2014. Canada’s economy is tied to the U.S. economy through bilateral trade and investment. “We are waiting to see if the recovery in the U.S. is real. If it is, we will almost certainly benefit, and we will ride that tailwind,” says an interviewee. Canadians will benefit not only from the knock-on effect of U.S. economic growth, but also from the resulting rise in U.S. property values. Canadian investors who regard prices as climbing too high at home will invest in the United States, where they remain the largest foreign buyers of real estate.

Market Will Remain Strong in 2014

The *Emerging Trends* survey, a survey of Canadian real estate participants and service providers, indicates that participants expect Canada’s real estate market to improve in 2014. The average “buy” rating is projected to slip slightly, from “modestly good” to “fair.” While this may seem to reflect falling confidence, it actually indicates that strength in the market has pushed up prices for the last two years to a level where investors are beginning to approach each transaction with a heightened level of caution.

EXHIBIT 5-2

Emerging Trends Barometer 2014

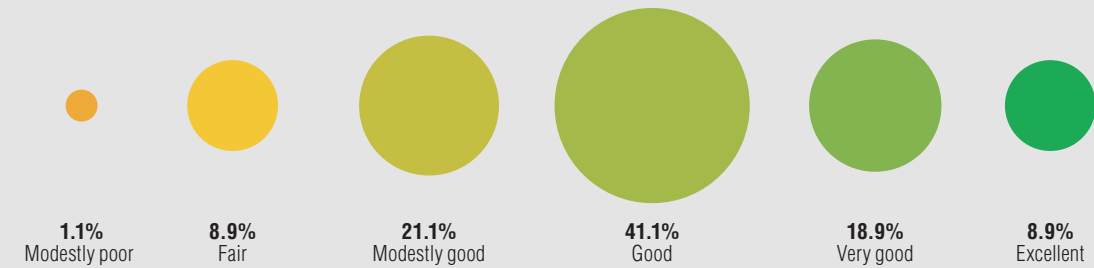


The 2014 “sell” recommendation for the Canadian market remains in the “modestly good” range, suggesting that 2014 will be a year when investors could try to sell select properties. The combination of the buy and sell rankings suggests it may be a year when the market will function efficiently enough for investors to sell properties if they so desire. Finally, the “hold” rating nudged upward slightly, indicating that 2014 will still be a “modestly good” time to hold properties. This survey result would appear to reflect the general mind-set of most market participants. These indicators are consistent with sentiments expressed by our interviewees, many of whom felt that 2014 would still see a good number of transactions, but volumes will likely be down from last year. Buyers could be more discerning, paying top dollar only for the best properties. With prices strong, many interviewees also view this as a good time to reposition portfolios. It is timely to sell assets that may not be in line with current investment objectives.

Profitability Scenario without Losers

An efficient market across the full spectrum of property types in all major Canadian cities would clearly be good for business in 2014. The outlook for the profitability of companies will build on strong performance in 2013, with 69 percent of survey respondents predicting “good” or “higher” prospects for profitability. Even more impressive, more than one-quarter of the respondents see the prospects for profitability as “very good” or “excellent.” There would appear to be no losers in this scenario,

EXHIBIT 5-3

Firm Profitability Forecast**Prospects for profitability in 2014 by percentage of respondents**

Source: *Emerging Trends in Real Estate 2014* survey.
Note: Based on Canadian respondents only.

with only 10 percent of respondents seeing the prospects for profitability as “modestly poor” or “lower.”

Such confidence is a strong indication that Canada’s real estate market will benefit a wide range of market participants, from lenders to fund managers to developers. In particular, the outlook would appear to be good for anyone who benefits directly from real estate investment.

Local operators scored the second-highest rating for profitability, which reflects a transition in the market from dependence on capital market movements for returns to more traditional asset performance. These Canadian investors indicate that they

will continue to work with local partners as they explore new opportunities in search of higher returns.

The business prospect outlook for other types of market players is somewhat mixed. Commercial/multifamily developers are expected to have “slightly better” prospects than homebuilders. The outlook for lenders ranges from “strong” for banks to “lower” for insurance companies and commercial mortgage-backed securities (CMBS) lenders.

Among lenders, banks that are positioned to take advantage of higher interest rates have “slightly better” prospects than insurance companies and CMBS lenders as spreads on debt start to widen across the board in expectations of higher interest rates. The ability of banks to attract low-interest deposits that can be put to work at higher rates will boost their profitability. But CMBS lenders, who operate in a higher-risk loan environment, will be challenged by rising rates.

EXHIBIT 5-4

Prospects for Capitalization Rates

Property type	Cap rate September 2013 (percent)	Expected cap rate December 2014 (percent)	Expected cap rate shift (basis points)
Central city office	5.70	5.89	19
Suburban office	6.51	6.87	36
Regional malls	5.33	5.42	9
Power centers	5.91	6.01	10
Neighborhood/community shopping centers	6.25	6.43	18
Apartment: moderate income	5.17	5.25	8
Apartment: high income	4.95	5.19	24
Warehouse industrial	6.22	6.39	17
R&D industrial	6.46	6.70	24
Full-service hotels	7.10	7.10	0
Limited-service hotels	7.90	8.15	25

Source: *Emerging Trends in Real Estate 2014* survey.
Note: Based on Canadian respondents only.

Top Trends for 2014

Cap Rates on the Rise

Survey respondents agree that capitalization rates will stabilize or rise in 2014 depending on specific assets. To some extent, this will be a function of higher borrowing rates. “We have seen an increase of 50 basis points across the board in response to increased interest rates,” says an interviewee.

Across the 11 property sectors surveyed, cap rates are projected to increase by less than 25 basis points in 2014. Suburban office space is likely to see the largest increase, at 25 to 50 basis points, followed by high-income for-rent apartments and research and development (R&D) industrial property. Expectations of softer demand for these property types are behind the projected increase in cap rates as investors demand a higher return.

The smallest increases in cap rates are expected to be seen in full-service hotels, moderate-income for-rent apartments, and regional malls. These assets are perhaps seeing the smallest increases due to their specific attributes. Full-service hotels and moderate-income for-rent apartments can raise their rents in a shorter time frame, allowing them to take advantage of a stronger market. Regional malls don't have the same level of rent adaptability, but they do tend to offer a bondlike income stream. Survey respondents may be seeing the advantage to both these characteristics going into a faster economic growth environment.

"Cap rates are starting to focus on quality and make distinction between good and bad properties," an interviewee explains.

Capital Continues to Move into Balance

Based on 2014's survey respondents, the availability and cost of capital for real estate investment are coming more into balance and the competition for capital will be robust. "There is debt and equity capital available. People will accept slight yield reductions," says an interviewee. At the same time, there will be more "institutionalization of real estate" in deals that are likely to be structured with an eye toward managing loan-to-values by being conservative with the loan proceeds and valuations.

Equity capital for investing from a variety of sources is considered by over 38 percent of the respondents to be in balance. This percentage is up from 32 percent of respondents in 2013. While a rising number of respondents see the market as in balance, what may be even more significant is the percentage of respondents who view the amount of capital available being oversupplied has declined to 37 percent from nearly 50 percent two years ago. A balance of capital in the market will keep pricing more dependent on individual fundamentals and less on excess capital influence.

REITs Recede as Buyers, but Other Participants Eager to Take Their Place

In 2014, Canadian real estate investment trusts (REITs), which represented about three out of ten buyers as recently as July, may choose to be more selective about the assets they pursue. One of the reasons for their previous dominance in the acquisition market was that the number of REITs in the market increased significantly over the past three years. "They are no longer the dominant buyers," says an interviewee. The reason is that REITs are sensitive to rising interest rates. "Their cost of capital has gone up so much, from about 4.5 percent to 6.5 percent. They were buying at cap rates of 5.25 percent to 5.5 percent, but now it's hard for them to be accretive."

The once-dominant, but now reduced, role of REITs as acquirers is quickly being filled by pension funds, which "never really went away but now are in full position," the interviewee says. At the same time, private buyers, which historically were not as aggressive as REITs and not as exposed as REITs to interest rate increases, are becoming more active as acquirers. They tend to operate in different markets. "REITs get marked to market every hour," he says. Pension funds, which are driven by actuarial assumptions and are thus not forced to confront the impact of interest rates until year-end, were competing directly with REITs to buy the highest-institutional-grade properties.

Well-capitalized REITs will not have trouble accessing additional capital, but may choose not to due to the expected higher cost. Any additional capital raised must be redeployed at an expected rate that is accretive to unit-holder (i.e., shareholder) value. If REITs have decided to be more selective in the assets they pursue, they could need less capital in 2014. Consolidation could occur among small and mid-sized REITs, but consolidation will need to add to unit-holder value. There is some concern about the potential impact on REITs if valuations soften in 2014. "Weaker REITs may not have a choice, and will have to sell into a softer market to make distributions," says an interviewee.

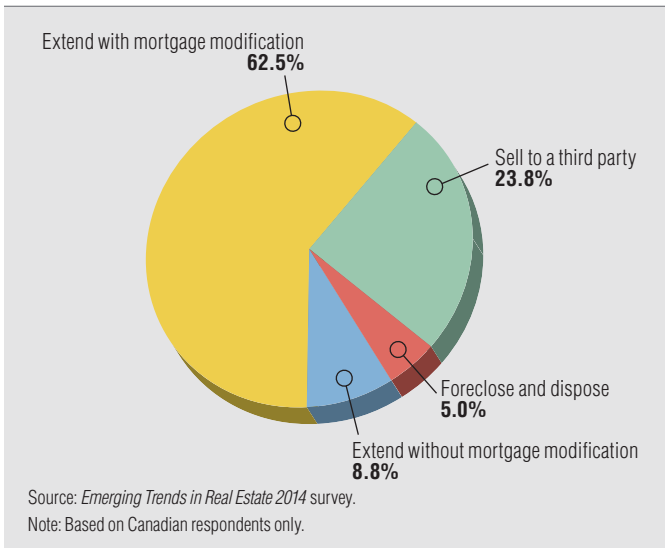
Retailers Spinning Off CRE Holdings as REITs

In what could emerge as a secular trend, some publicly listed retailers are spinning off their commercial real estate holdings as separately listed REITs in the hope that the value of those holdings will be realized in the form of higher securities prices on the stock market. The first such deal was struck by a major Canadian grocer, which in July raised \$400 million in the REIT initial public offering (IPO) while raising another \$600 million in bonds. In October, another Canadian retail chain that sells car parts and consumer goods raised \$253 million in an IPO. While retailers that are in a position to launch such IPOs represent "a limited universe," says an interviewee, it will be interesting to see if similar deals are cobbled together by Canadian companies in other industries that have sizable real estate holdings across the country.

Debt Capital Readily Available

Banks may be incentivized by higher interest rates to make debt capital available. Both acquisitions and refinancing, debt capital is viewed as being over 70 percent "in balance" or "moderately oversupplied." Nevertheless, 62 percent of respondents indicate that the preferred strategy for lenders that have problem loans on their books will be to extend them with mortgage modifications.

EXHIBIT 5-5
Maturing Loans: Preferred Strategy for Lenders



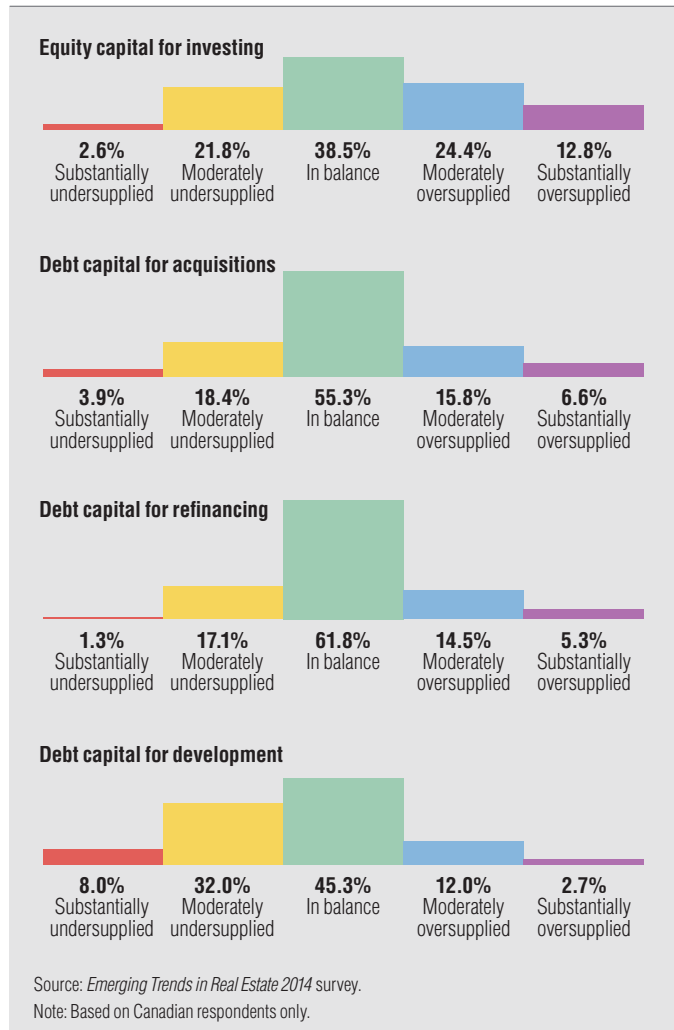
Development Will Remain Well Funded

Development is likely to be well funded, with 45 percent of respondents seeing debt capital for 2014 development as being on the rise. In an indication that any project that receives development financing will still need to meet reasonable underwriting criteria, 40 percent of the respondents see this category of debt capital as “undersupplied.” It should be noted that capital is expected to be available for high-quality projects that meet stricter lender requirements for both the project and the borrower. For example, high-rise condominium projects, and their sponsors, are now getting a higher level of scrutiny from traditional lenders. The best projects to the best borrowers will get capital, while those that do not meet these criteria will need to look for capital from alternative sources. Alternative sources of capital do exist, but will typically have a higher cost.

Borrowing Strategies

The expectation that borrowing will become more expensive does not appear to discourage real estate investors. Interviewees say they expect Canadian interest rates to increase 100 to 200 basis points by 2015. “Changes in the economy will likely result in change to the cost of debt,” explains an interviewee. The increase in rates, however, is not expected to lower demand for debt capital. “If you have a good strategy for long-term growth, regardless of the cost of borrowing, debt at today’s rates will still have a positive impact on bottom line,” says an interviewee. In response to higher rates, one interviewee

EXHIBIT 5-6
Real Estate Capital Market Balance Forecast for 2014



believes that investors “should consider utilizing as much debt as possible” to lock in low interest rates while they still can. “There are signs that some pension funds are now taking this precaution,” he says.

This is an opportunity for lenders to segregate borrowers more aggressively, using credit quality as the main distinguishing factor. “To make sense of aggressive pricing, you need to have aggressive debt financing,” says an interviewee. “There is aggressive debt around for the right borrowers, who are easier to stratify in Canada than in Europe, where the difference between a creditworthy borrower and the next tier is almost indistinguishable.”

Capital Plays Hard to Get

Although survey respondents see both debt and equity capital as being available in 2014, they don't expect capital to be easier to obtain. Our interviewees expect that owners of capital will only be looking to invest in the best projects and that they will be risk-adjusting their return expectations more so than in the last few years. "There is lots of cash available, but there is no place to put it. Mortgage lenders are going crazy," says an interviewee. "Lots of cash is available for good projects, but banks are increasingly lending only to established builders with good balance sheets," says another.

It is unclear whether equity underwriting standards are getting stricter in Canada. In 2014, 44 percent of respondents expect equity underwriting standards to remain unchanged, while 44 percent expect them to become more rigorous, which would keep capital from flowing into ill-conceived transactions. Only 11 percent of respondents expect equity capital underwriting to be less rigorous.

But it is clear that debt underwriting standards are getting tougher. The survey reveals that debt capital will be at least as difficult to obtain in 2014, with 50 percent of respondents predicting that debt underwriting standards will be "more rigorous" and with 90 percent of respondents predicting that they will be either "the same" as a year earlier or "more rigorous."

EXHIBIT 5-7

Equity Underwriting Standards Forecast for Canada

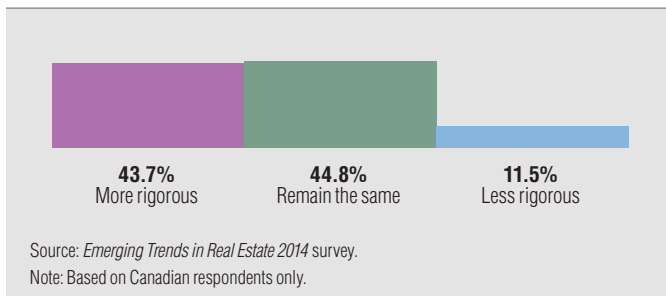


EXHIBIT 5-8

Debt Underwriting Standards Forecast for Canada

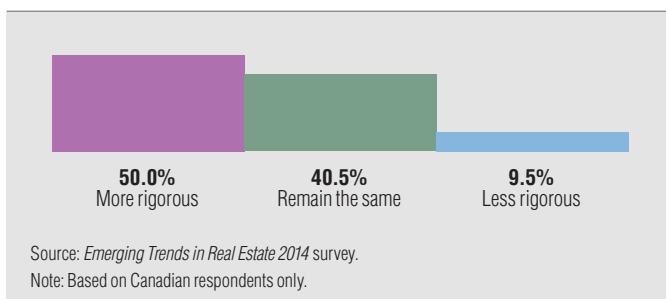
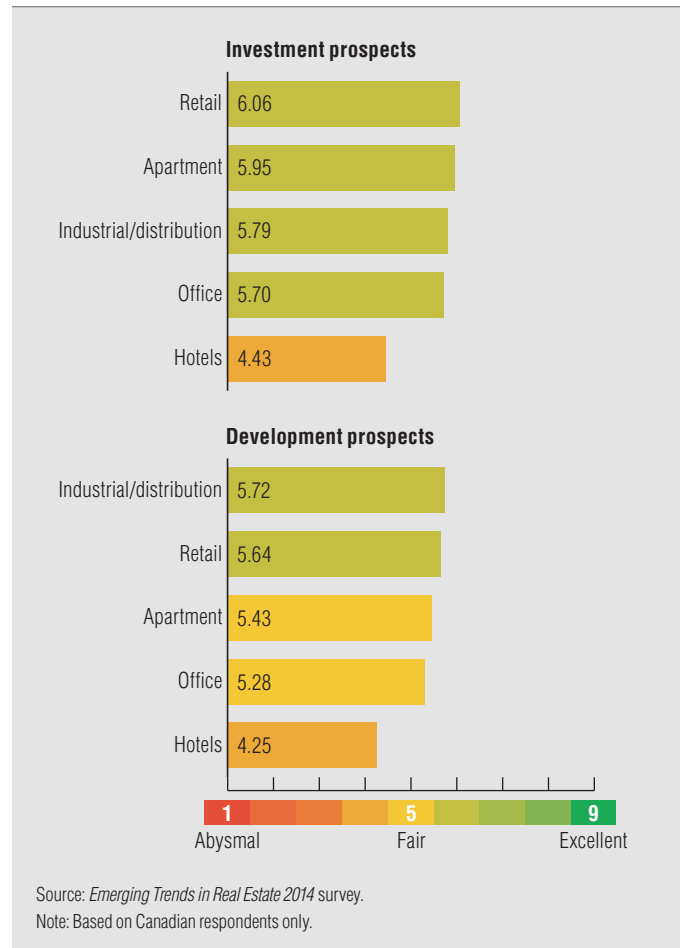


EXHIBIT 5-9

Prospects for Major Commercial Property Types in 2014



Financing for new condominiums is a case in point. In general, Canadian lenders will not approve a new project until it is at least 70 percent presold. The buyers are usually investors, and presale requirements are rigidly enforced. But in 2013, the stakes were raised even higher as banks started favoring established builders with track records and healthy balance sheets. Smaller developers—even ones that have established track records and were able to borrow as recently as two years ago—are increasingly being forced to seek alternative lenders.

"Bank underwriting has dried up for condo lending except for established relationships with strong, experienced local builders," says an interviewee, predicting that banks will wait until the end of 2014 or mid-2015 to "loosen up" construction lending for condominiums. "They are concerned that it will be two to three years before the existing pipeline is absorbed, even

though there is no real concern on absorption as rental demand is strong and rents are increasing,” the interviewee adds.

Only 9 percent of respondents expect debt underwriting standards to be less rigorous, up from 6 percent a year earlier.

Institutional Investors Will Become More Active

Survey respondents are expecting the majority of buyers and sellers of real estate who were active in the Canadian market in 2013 to remain in the market in 2014, except for an expected drop in activity by REITs. Perhaps there will even be a “small increase” in the number of players, the survey predicts. Institutional investors, including pension funds and foreign investors, are expected to be slightly more active in 2014.

Private acquirers of real estate will be about as active as they were in 2013, or slightly more active, according to the survey. “Private investors will drive the market in 2014 as REITs are likely to be more discerning purchasers in 2014 due to their return requirements,” explains an interviewee. The survey identifies public equity REITs as the only group of market participants that is likely to show a “slight decline” in activity.

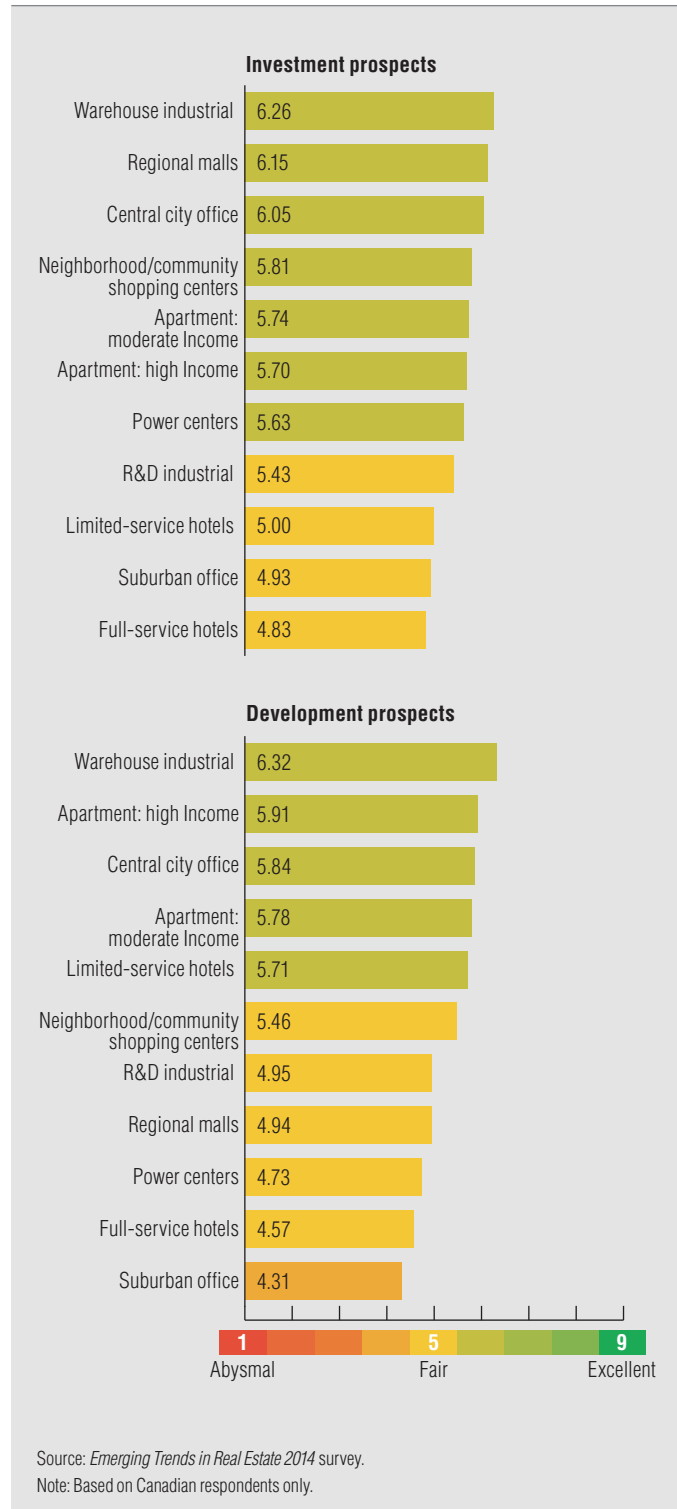
Nonbank Financial Institutions to Become Active as Lenders

Except for government-sponsored entities (GSEs), all active providers of debt capital are expected to remain at least as active in Canada’s real estate market in 2014 as they were a year earlier. Nonbank financial institutions and mezzanine lenders are expected to see a small increase in activity due to improved market fundamentals, which will allow them to move toward higher risk/return strategies that can be enhanced with leverage in the form of debt and also as a response to tighter lending by banks to high-rise condo builders. Traditional players, such as securitized lenders, mortgage REITs, and insurance companies, will be as active as they were in 2013 or show a “slight increase,” according to the survey. The level of debt provided by commercial banks is expected to stay the same. GSEs are expected to provide “slightly lower” levels of debt capital as private players become more active.

Opportunities Arise across Property Types

There will be no shortage of opportunities for investors to earn a decent return in Canadian real estate in 2014. According to the survey, retail, for-rent residential, industrial distribution, and office space will all offer “modestly good” investment prospects in 2014. Hotels, however, are viewed as offering “moderately poor” investment prospects. Indicating an improvement in sentiment, development prospects for all major property types are

EXHIBIT 5-10
Prospects for Commercial Subsectors in 2014



expected to improve in 2014, with survey respondents placing them in a range from “fair” to “modestly good.”

Office Boom in Toronto and Vancouver Raises Concerns

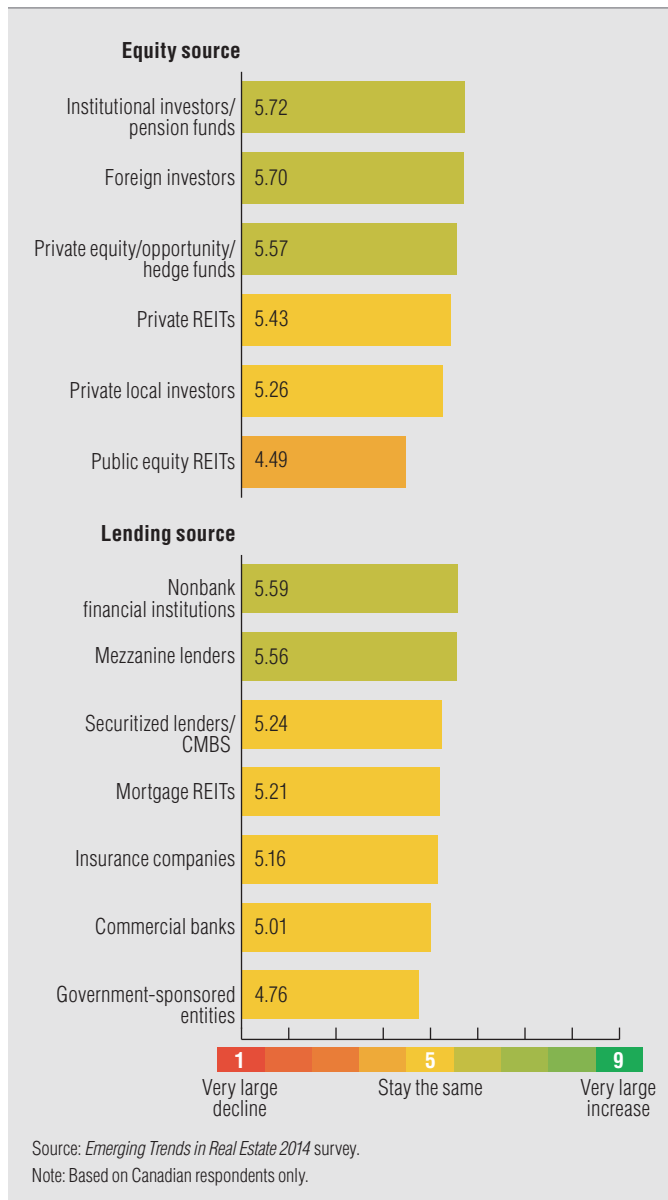
Canada is in the midst of a commercial office boom. About 4 percent of inventory was still under construction in mid-2013, which was about four times the level in the United States. “We

have started another office development cycle. What’s different about this cycle is that we have more downtown development. We’ve never seen so much office construction in downtown Vancouver or downtown Toronto,” says a fund manager.

Although prices are expected to remain at record levels in 2014, there are some concerns. “Tenants are leaving more space than they are leasing. The good news is all the new buildings are full. The bad news is 25-year-old buildings have huge chunks of vacancy. That could be a big negative,” says an interviewee.

Survey respondents are nearly equally split between these positive and negative signals, with 25 percent of respondents indicating that 2014 will be a good time to buy office property and 26 percent saying it will be a good time to sell. The survey also indicates that central city offices are more in favor than suburban offices. While the former are considered “modestly good” from an investment and development perspective, the latter are considered “fair” for investment and “modestly” poor for development. Central city offices compare well with other subsectors, ranking in third place for both investment and development, under community shopping centers but above moderate-income apartments.

EXHIBIT 5-11
Change in Availability of Capital in 2014



Redevelopment Will Trump Development

In some Canadian markets, a cyclical trend will favor redevelopment over development for several years. In Montreal, for example, more office buildings are expected to be redeveloped than built from the ground up in 2014. Owners of owner-occupied buildings who plan to move to new ones in 2014 are expected to redevelop the old ones as apartment complexes or for other uses. “There is no oversupply of office inventory even with new construction given the redevelopment plans for existing buildings. Old tenants vacate and move to new construction,” says a national investor. Suburban and Class B office space will need to redevelop in all markets to stay competitive. A leading real estate service provider notes that older space and

EXHIBIT 5-12
Central City Office

2014	Prospects	Rating	Ranking
Investment prospects	6.05	Modestly good	3rd
Development prospects	5.84	Modestly good	3rd
Buy 38.6%		Hold 45.5%	Sell 15.9%
Expected capitalization rate, December 2014		5.9%	

Source: *Emerging Trends in Real Estate 2014* survey.
Note: Based on Canadian respondents only.

less favorable suburban locations will need to transform to meet the needs of the market.

Redevelopment will also play a role in any market looking to increase urban density. Municipalities aiming to maintain the vitality of urban cores could be inclined to favor redevelopment of existing projects. A Toronto developer expressed an interest in redevelopment: “We are buying for future redevelopment sites. We don’t see a large future in developing office space now or in near future. We are willing to buy existing office buildings, hold [them] for five to ten years, then redevelop the site into mixed-use, high-rise residential/retail.”

Mixed-Use Projects Will Proliferate in Downtown Areas

A similar trend will soon take shape in Toronto where, an interviewee explains, “All land available for low-rise [development] within the greenbelt will be built out in ten years. Therefore, remaining opportunities will be for redevelopment only. They will favor higher density and mixed use.” In line with the increasing preference among downtown residents and office workers to live, work, and play within walking distance if not near mass transit hubs, there is an increasing trend toward urban core mixed-use development. A prime example is the new multiuse space in downtown Toronto, which combines condominiums with offices and retail stores. Several other downtown Toronto projects combine hotels with condominiums and retail stores. Going forward, it is likely that this mixed-use trend in development will continue. The desire of tenants to be able to live, work, and play in an urban location will drive further demand for projects that could offer residential, retail, and office. In addition, municipalities may begin to see the advantage of such projects and will look for policies that will incentivize their development.

Intensification, Reverse Migration Continue to Take Hold

Intensification of downtown areas of cities is continuing in Canada’s major centers to combine with reverse migration from the suburbs to downtown areas as one of the most forceful and rapidly emerging secular trends in both corporate office and residential real estate. In southern Ontario, for example, a greenbelt restriction against developing in certain areas, combined with government intensification policies, is precipitating the development of both office and residential property along subway lines and near mass transit hubs in Toronto, resulting in markedly higher density. A powerful factor that is driving reverse migration is that both residents of suburbs and employees of companies in suburban offices have grown tired of their long commutes and are reacting by moving into downtown areas, which is stimulating new demand for office space in the cities and resulting in an increase in infill development.

High absorption rates for new office space, which tends to be preleased, pose the question of what will happen to the old stock. To hear commercial real estate industry sources in Toronto tell it, the old buildings will have to be refurbished in a manner that will bring them up to current environmental and energy efficiency standards. Significant investments will continue to be made in well-located buildings in core downtown areas. The challenge for the owners of these buildings will be to keep post-renovation rents low enough to remain competitive. In addition to remaining competitive on a cost basis, refurbished buildings will need to meet changing tenant demands. Newer properties may have an advantage due to more flexible floor plates that can be adjusted to a wider set of floor layouts. Many tenants today are looking for more collaborative space with less private space. Office layouts that facilitate workers who may work in the office only on a part-time basis are also becoming more desirable. These office finishes allow tenants to fit more workers into less space, thus lowering the required space per employee. The downside to this transition is that a refurbished building may need to attract either larger or more tenants than were previously required to keep the building fully occupied. An international service provider notes: “There is a new workplace strategy”—tenants are focused on managing and reducing real estate costs—reconfiguring to use less space per employee. This push has been led by the banks and financial institutions as they focus on managing costs.”

Suburban Offices Left Out in the Cold

As office workers and residents gravitate toward the urban core of major cities across Canada, suburban offices face dimmer prospects, particularly in suburban areas that are not easily reachable by mass transit. For investment and development, suburban offices ranked tenth and 11th, respectively. “Related to the trend of urban intensification, suburban office is a declining commodity that has no staying power,” says an interviewee. Suburban office is becoming less competitive as companies

EXHIBIT 5-13
Suburban Office

2014	Prospects	Rating	Ranking
Investment prospects	4.93	Fair	10th
Development prospects	4.31	Modestly poor	11th
Buy 22.2%	Hold 40.0%		Sell 37.8%
Expected capitalization rate, December 2014		6.9%	

Source: *Emerging Trends in Real Estate 2014* survey.
Note: Based on Canadian respondents only.

EXHIBIT 5-14

Neighborhood/Community Centers

2014	Prospects	Rating	Ranking
Investment prospects	5.81	Modestly good	4th
Development prospects	5.46	Modestly good	6th
Buy		Hold	Sell
48.6%		32.4%	18.9%
Expected capitalization rate, December 2014		6.4%	

Source: *Emerging Trends in Real Estate 2014* survey.
Note: Based on Canadian respondents only.

return to the urban core and companies take less space. As this space becomes vacant and needs to be refurbished to be competitive, the suburban market softens even further.

Suburban office performance could get some positive momentum by the expected improvement in the U.S. economy. Improving economic conditions at home could lead to expansion by U.S. companies into Canadian markets. These companies' needs are adequately met by suburban locations that are significantly less expensive than urban core locations. This type of tenant demand, however, will still be influenced by the amenities that the property has to offer. Locations near transit hubs, retail amenities, and worker housing will still outperform. In addition, these companies are likely to still require the amenities mentioned earlier that allow tenants to use less space per worker. It remains to be seen if the activity generated by the expansion of U.S. firms will be enough to offset the move toward the urban core.

Retail Is a "Buy"

Survey respondents view Canada's retail market as one to invest in during 2014. Across the major markets, an average of 38 percent of respondents rate retail as a "buy." Calgary and Toronto are at the high end, with over 42 percent of respondents recommending buying retail property in these markets. Not surprisingly, only 13 percent of respondents anticipate that 2014 will be a good year in which to sell retail property, and 48 percent suggest that it would be best to hold retail investments for the entire year.

These recommendations are related to the difficulty that a seller of an attractive piece of brick-and-mortar retail real estate would face in finding another attractive one to buy later. Inflation-adjusted retail sales in Canada were unchanged in mid-2013 from a year earlier. "This is not a huge risk because we are not building that much retail," says an interviewee. "But you can't ignore what is going on with online sales, which is continuing to chip away at retail. Retail sales have gotten pretty sluggish despite a fairly robust economy."

EXHIBIT 5-15

Power Centers

2014	Prospects	Rating	Ranking
Investment prospects	5.63	Modestly good	7th
Development prospects	4.73	Fair	9th
Buy		Hold	Sell
25.7%		45.7%	28.6%
Expected capitalization rate, December 2014		6.0%	

Source: *Emerging Trends in Real Estate 2014* survey.
Note: Based on Canadian respondents only.

EXHIBIT 5-16

Regional Malls

2014	Prospects	Rating	Ranking
Investment prospects	6.15	Modestly good	2nd
Development prospects	4.94	Fair	8th
Buy		Hold	Sell
41.7%		55.6%	2.8%
Expected capitalization rate, December 2014		5.4%	

Source: *Emerging Trends in Real Estate 2014* survey.
Note: Based on Canadian respondents only.

Canada is seen as "under retailled" in terms of square footage of retail floor space per capita, so Canadian investors are backing foreign retailers who are eager to sell their wares in a safely recovered economy. They are leading shopping malls and other retail buildings to renovate, expand their floor plates, or otherwise reformat. In July 2013, for example, a Canadian retailer announced plans to purchase a U.S.-based department store and open seven new locations in Canada. This expansion will consist of converting existing stores or building new ones. In September, a Canadian pension fund purchased another U.S. department store for \$6 billion. In January, a U.S.-based discounter took over nearly 220 outlets of a Canadian discount department store chain across Canada. Other prominent U.S.-based retail chains have announced plans to open Canadian locations by either converting or renaming existing locations through the end of 2013 and into 2014.

The survey respondents see other disparities in the retail market as well. Regional malls are seen as the second-best investment option despite the fact that institutional ownership of high-quality malls in Canada makes them difficult to acquire. Neighborhood and community centers are considered attractive from an investment perspective, ranking in the top five among subsectors of retail and other property types covered by the

EXHIBIT 5-17

Warehouse Industrial

2014	Prospects	Rating	Ranking
Investment prospects	6.26	Modestly good	1st
Development prospects	6.32	Modestly good	1st
Buy		Hold	Sell
66.7%		29.2%	4.2%
Expected capitalization rate, December 2014		6.4%	

Source: *Emerging Trends in Real Estate 2014* survey.
Note: Based on Canadian respondents only.

EXHIBIT 5-19

Hotels—Limited Service

2014	Prospects	Rating	Ranking
Investment prospects	5.00	Fair	9th
Development prospects	5.71	Modestly poor	5th
Buy	Hold	Sell	
14.3%	57.1%	28.6%	
Expected capitalization rate, December 2014		8.2%	

Source: *Emerging Trends in Real Estate 2014* survey.
Note: Based on Canadian respondents only.

EXHIBIT 5-18

R&D Industrial

2014	Prospects	Rating	Ranking
Investment prospects	5.43	Fair	8th
Development prospects	4.95	Fair	7th
Buy	Hold	Sell	
29.2%	54.2%	16.7%	
Expected capitalization rate, December 2014		6.7%	

Source: *Emerging Trends in Real Estate 2014* survey.
Note: Based on Canadian respondents only.

EXHIBIT 5-20

Hotels—Full Service

2014	Prospects	Rating	Ranking
Investment prospects	4.83	Fair	11th
Development prospects	4.57	Fair	10th
Buy	Hold	Sell	
14.3%	71.4%	14.3%	
Expected capitalization rate, December 2014		7.1%	

Source: *Emerging Trends in Real Estate 2014* survey.
Note: Based on Canadian respondents only.

survey. Respondents expect power centers to lag as attractive investments in 2014, with prospective investments rated “modestly good” and development prospects rated “fair.” The investment prospects for power centers fall to the bottom quartile of all real estate investment alternatives. Power centers’ development prospects fare slightly worse, rated “fair” and a ranking of nine out of 11.

America’s Industrial Recovery and Canada

The “reshoring” of manufacturing in the United States will come, to some extent, at Canada’s expense. Ford Motor Co., General Motors, and Chrysler are in the process of moving their Canadian production back to the United States, where costs are lower, along with a host of auto parts manufacturers. Interviewees cite the strength of the Canadian dollar, which they say they expect to remain at about 95 cents to the U.S. dollar through 2014. “The strong Canadian dollar makes it difficult to compete,” says one interviewee.

“Manufacturing is struggling,” says an interviewee. “The big concern is that manufacturing is well below the peak of 2007 and 2008,” says an interviewee.

Yet survey respondents are still bullish on warehouse/industrial property, with 67 percent assigning a “buy” rating to the property type in major cities. Only 4 percent of respondents believe that 2014 will be a good time to sell. A substantial 29 percent recommend holding onto it. There is significant diversification within the industrial/warehouse sector and the potential investment decisions. Modern multipurpose logistics space with the desired ceiling height and amenities is in high demand by both investors and owner-occupiers. On the other end of the spectrum are older and perhaps less functional industrial space. The investment choices for this type of space seem to appeal to users and investors looking for a steady income stream, a user serving a local market need, or someone looking for a redevelopment opportunity. “Expect to continue to see opportunities to acquire older properties and add value, but competition for good assets has increased and will stay difficult in 2014,” observes a Canadian industrial investor.

The outliers are Montreal and Calgary. Only 17 percent of respondents indicate they would buy industrial/distribution property in Montreal, and 37 percent believe it will be the right time to sell. For Calgary, 38 percent of respondents rate industrial/distribution as a “hold.” But that does not appear to reflect dis-

satisfaction, because 51 percent of respondents—more than in any other Canadian city—rate it as a “buy.”

Warehouses have the greatest potential in industrial real estate, according to the survey, which ranked them in first place for both investment and development for 2014. R&D industrial, with its higher office component, does not fare as well, considered merely “fair” for both investment and development. R&D falls below most subsectors, just above limited-service hotels.

Hotels

If survey respondents are correct, 2014 may be a quiet year for hotel transactions. In the four major markets, an average of 64 percent of respondents would hold hotel assets. Respondents recommend buying over selling in Calgary and Montreal, while selling over buying in Toronto and Vancouver.

No particular type of hotel seems to stimulate optimism, however. Development prospects are described as “modestly poor,” but because some other property subsectors receive even less enthusiastic reviews, hotels land in the middle. Investment prospects are “weak” for both limited-service and full-service hotels. Still, survey respondents are not recommending wholesale liquidation. A high 57 percent of respondents say they would hold limited-service hotels and an even higher 71 percent make the same recommendation for full-service hotels.

Rental Apartments

For-rent apartments are still an extremely attractive investment choice. The average “buy” recommendation for Canada’s major markets is 46.2 percent, while only 8 percent of survey respondents expect 2014 to be a good time to sell for-rent apartments. In the country’s three largest markets—Calgary, Toronto, and Vancouver—39 percent of respondents recommend that investors buy apartments. Similarly, 46 percent of respondents recommend holding—not selling—rental apartments in the major markets. The fourth-largest market, Montreal, has the lowest “buy” rating but still has a higher “hold” rating than the other three major cities.

Survey respondents are apparently confident that a large supply of condominiums in at least two major cities will not put undue pressure on the rental market. In Canada, condominiums are often bought by investors and then rented out, which can put pressure on other rentals. In Calgary, an oversupply of condos has reached the point where one interviewee expects them to flood the rental market. But in Toronto, such properties are seen as serving a necessary purpose as “the only real source for more rental stock” to meet “still-strong rental demand,” says another interviewee. Concern about the overbuilding of the condominium market, particularly in Toronto and Vancouver, has been a popular topic of conversation, with a level of con-

EXHIBIT 5-21

Apartments—Moderate Income

2014	Prospects	Rating	Ranking
Investment prospects	5.74	Modestly good	5th
Development prospects	5.78	Modestly good	4th
Buy 46.2%		Hold 46.2%	Sell 7.7%
Expected capitalization rate, December 2014		5.3%	

Source: *Emerging Trends in Real Estate 2014* survey.
Note: Based on Canadian respondents only.

EXHIBIT 5-22

Apartments—High Income

2014	Prospects	Rating	Ranking
Investment prospects	5.70	Modestly good	6th
Development prospects	5.91	Modestly good	2nd
Buy 30.8%		Hold 53.8%	Sell 15.4%
Expected capitalization rate, December 2014		5.2%	

Source: *Emerging Trends in Real Estate 2014* survey.
Note: Based on Canadian respondents only.

cern that the condominium market could be heading toward a bubble. Fortunately, the underlying strength of demand from natural household growth and immigration illustrated in the 2014 Net Migration Forecast chart (Exhibit 5-25) has been enough to absorb the units being delivered. If the amount of new units being delivered begins to slow, this could lead to a shortage, which may result in rising rents.

Rising rents in condominium rentals could help improve the economics of purpose-built for-rent apartments. Purpose-built for-rent apartments could become a more significant part of the housing stock going forward. If fewer condos become available for rent, tighter mortgage rules make purchasing a home more difficult, and more households make the lifestyle choice to rent rather than own, purpose-built for-rent apartments could help meet the need for more housing stock. However, there remain significant obstacles preventing the large-scale development of built-for-rent units. In addition to rent controls, development sites are difficult to obtain, development charges are increasing, approval processes are lengthening, and the longer time horizon for returns limits the number of investors who have an interest in this type of development.

EXHIBIT 5-23

Prospects for Residential Property Types in 2014

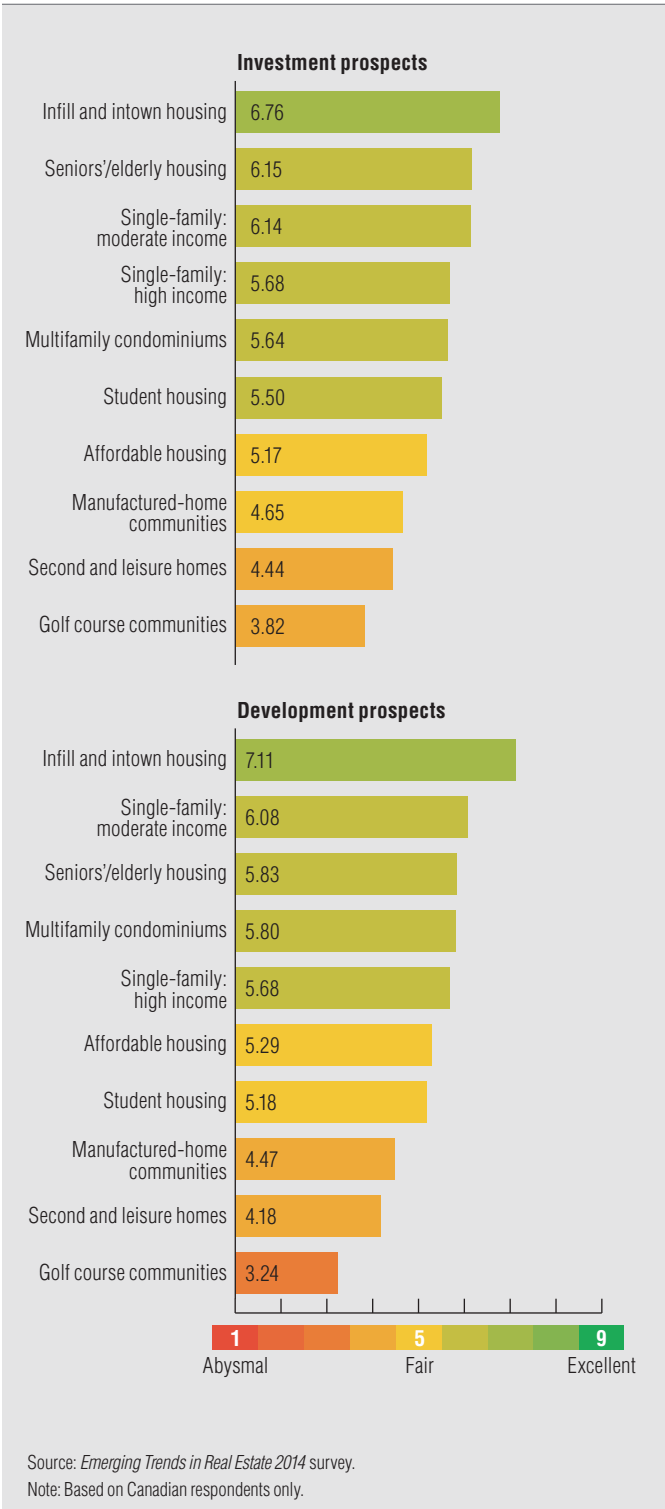
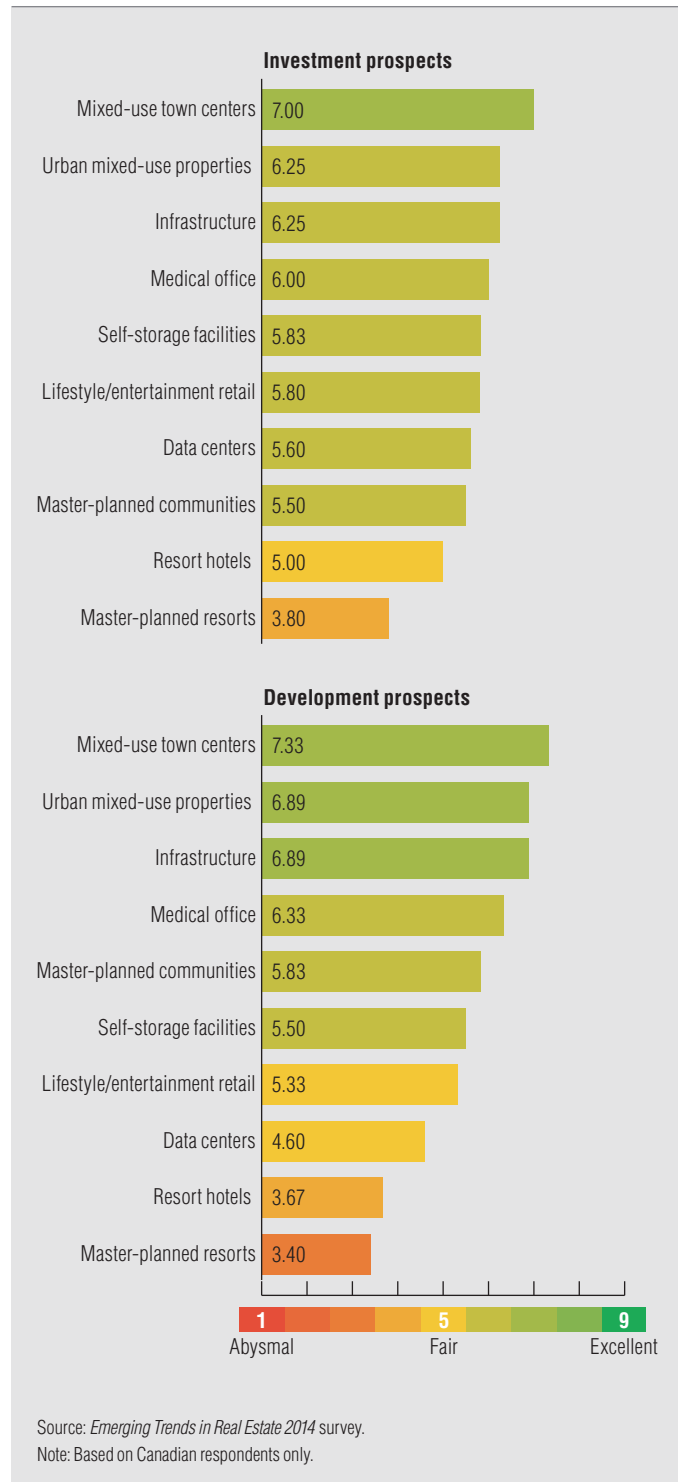
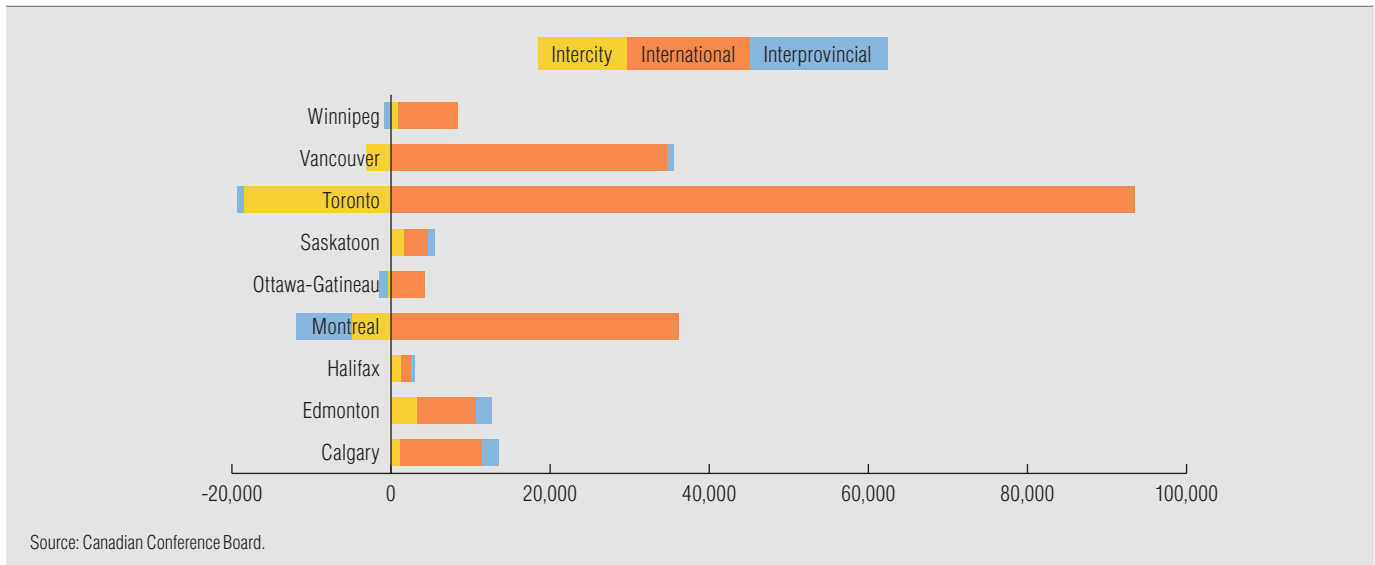


EXHIBIT 5-24

Prospects for Niche and Multiuse Property Types in 2014



2014 Net Migration Forecast



Survey respondents view moderate-income and high-income apartments in a fairly even light for 2014, predicting “modestly good” investment prospects for each of them in 2014. They rank in fifth and sixth place, respectively, among other subsectors of property types, below community shopping centers but above R&D industrial property. From a development perspective, respondents put high-income apartments as the second-most-attractive option for the year.

Urbanization and Intensification Continue to Take Hold

Residential development within city limits will be increasingly prevalent in 2014. Reflecting a secular trend toward urbanization and intensification, infill and intown housing easily have the highest investment and development prospect scores for the year to come. The outlook for both types of housing is “good.”

If there is a limit to this trend, it’s that prices for single-family homes in Canada’s major markets are rising faster than personal income. “You can’t be in the business when the average man can’t afford the average house. We’re at that point now,” says an interviewee. The average price of a home in Canada increased to \$385,906, according to the Canadian Real Estate Association. This is an 8.8 percent year-over-year price gain. This trend could push “more development outside of the greenbelt to address affordability,” another interviewee predicts. The impact of rising house prices is not isolated to major markets. Home prices are up 4.3 percent year over year, in all markets outside of Toronto, Vancouver, and Calgary.

Development at more distant locations, however, comes with a different set of costs. As previously discussed, the population has clearly shown a desire to move back to the urban core. This reverse migration is intended to eliminate commuting costs and to allow for access to a live/work/play environment. Suburban development will require more investment in infrastructure to attempt to efficiently move workers to and from employment centers. Housing development outside the urban core also requires a lengthy and increasingly difficult and expensive

Markets to Watch: Overall Real Estate Prospects

	Investment	Development	Homebuilding
1 Calgary (1/1/1)	6.40	6.25	6.91
2 Edmonton (2/4/3)	6.18	6.06	6.45
3 Saskatoon (3/3/4)	6.12	6.12	6.43
4 Vancouver (4/2/5)	6.10	6.17	6.39
5 Toronto (5/5/2)	6.03	5.88	6.46
6 Winnipeg (7/6/6)	5.50	5.32	5.71
7 Ottawa (6/7/6)	5.52	5.07	5.71
8 Halifax (8/8/9)	5.36	5.04	4.95
9 Montreal (9/9/8)	5.21	4.82	5.30

Source: *Emerging Trends in Real Estate 2014* survey.
 Note: Numbers in parentheses are rankings for, in order, investment, development, and homebuilding.

2014 Forecast Economic Indicators

	Calgary (1)	Edmonton (2)	Saskatoon (3)	Vancouver (4)	Toronto (5)	Winnipeg (6)	Ottawa (7)	Halifax (8)	Montreal (9)
Real GDP growth (%)	3.4	3.2	3.5	3.1	2.7	2.1	1.6	2.6	2.1
Total employment growth (%)	2.8	1.6	0.8	2.5	1.6	1.5	1.6	1.6	0.6
Unemployment rate (%)	4.6	4.6	4.2	6.2	8	5.5	6.1	6	7.9
Personal income per capita growth (%)	2.8	2.1	1.3	3.3	2.5	2.8	3.1	2.9	2.1
Population growth (%)	2.1	1.9	2.6	1.6	1.7	1.2	0.7	0.9	1
Total housing starts	13,239	11,734	2,842	16,391	40,847	3,953	6,225	2,289	15,392
Retail sales growth (%)	5.2	5	5.3	3.8	3.6	4.6	3.4	3.6	3.4

Sources: Statistics Canada, CMHC Housing Time Series Database, the Conference Board of Canada.

process to obtain the proper entitlements and install the required infrastructure. The infrastructure issue may become an emerging trend in the Greater Toronto, Calgary, and Edmonton areas and perhaps in other markets. Municipalities seeking new and creative ways to finance infrastructure are increasingly pushing costs and risks down to developers. For example, in addition to ever-increasing development charges, one regional authority in Ontario is requiring developers to finance upfront infrastructure costs for subdivisions that have historically been funded directly by the local government and covered through development charges. This increases costs to developers and also leaves them with the risk of cost recovery from continued downstream development. If other municipalities adopt this approach, it will further drive up housing costs, making homes even less affordable.

Moderate-income single-family housing is seen as an attractive investment in 2014. Respondents see the prospects for other areas of the residential market as less attractive, with the investment and development prospects rated from “modestly poor” to “modestly good.”

As part of the urbanization trend, the growing attractiveness to investors of work/live/play developments will lead the outlook for 2014. Survey respondents give niche and multiuse property “mod-

estly good” to “good” ratings. Other niche investments that are likely to attract interest in 2014 are infrastructure and medical offices, which both have higher ratings than other sectors. Respondents remain cool on niche products at the luxury end of the spectrum, reflecting concerns that job growth is too slow to build demand for them.

Markets to Watch

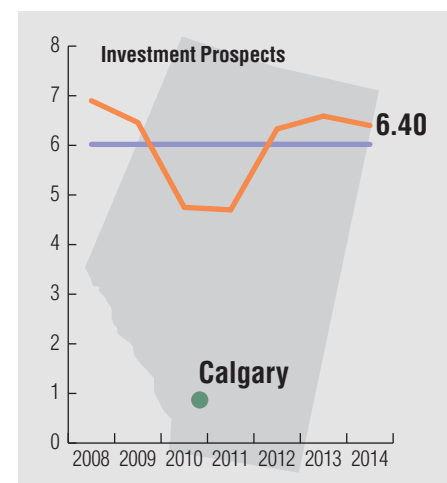
Survey respondents see the average overall rating for Canada’s nine largest commercial real estate markets as “modestly good” for investment and development in 2014. Average prospects for homebuilding are rated as “fair.” Calgary is their unanimous choice for “top market” for prospects in three categories: investment, development, and homebuilding.

Results for the other eight cities are diverse. Edmonton, Saskatoon, and Vancouver are in the top five ranks for each of the three categories. Toronto has only a mediocre score for investment and development prospects, but it’s the second-highest-rated market for homebuilding. The remaining four markets all score in the bottom half of the three categories. Secondary markets received higher marks than a year earlier, rising closer to parity with primary ones. Respondents’ views on the prospects for

2014 appear to be more related to the specifics of individual markets than in previous years—and less motivated by a search for yield.

Calgary (1). For the second year in a row, Calgary is the number-one-rated market by survey respondents. “Calgary marches to a different drum. It’s tied to energy, so it keeps on building,” explains an interviewee. “In Calgary, developers are getting innovative by profit-sharing with builders to provide exclusivity to those builders,” says another interviewee. Holding the top spot for both investment and development, Calgary moved into first place for homebuilding as well.

The Calgary economy continues to post solid gains, despite the disruption



caused by summer flooding. The energy industry, primarily oil, remains strong and will continue to benefit from economic growth around the world. Locally, energy and energy service companies have dominated office demand. Economic activity is being supported by growth in both the goods and services sectors. Manufacturing and construction will lead the goods sector, and personal services and transportation and warehousing are the key drivers on the service side.

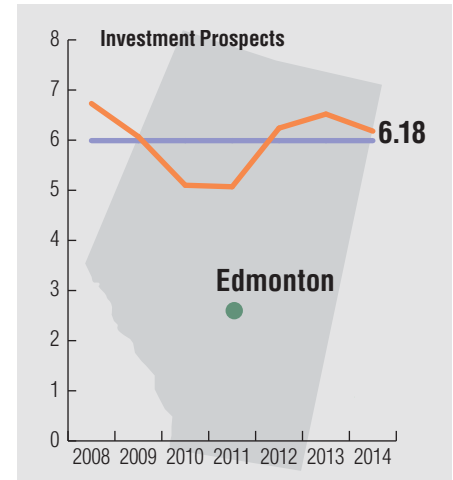
Economic activity is projected to grow at a 3.3 percent rate in 2013 and at a 3.4 percent rate in 2014. Employment growth is expected to slow but remain good through the end of this year and into 2014, growing at a 2.4 percent and 2.8 percent, respectively.

With improved job growth and personal income gains, 2014 is projected to be another good year. This should support consumer spending, which will support the wholesale and retail trade sector. Stronger business and personal services and a rise in transportation and warehousing activity should support stronger levels of service growth. Housing starts are expected to drop in 2013, although this decline could reverse

in 2014. Overall, housing starts are projected to decline to match slightly slower demographic growth. Population growth is projected to rise at a 3.1 percent rate in 2013, but slow to 2.1 percent in 2014. "As Calgary looks for more urbanization, look for condos to turn into rental stock."

"Calgary offers some unique opportunities. It is one of the fastest-growing western markets where it is possible to find assets." By property type, survey respondents see Calgary as a market where it is still attractive to buy for-rent apartment, retail, and industrial/distribution property. The enthusiasm for office and hotel properties is slightly less in Calgary, with respondents feeling that now may be a good time to sell. Overall, the survey reveals that if you already own these property sectors, then it may be a good time to hold.

Edmonton (2). The 2014 survey once again leaves Edmonton behind Calgary. Edmonton claimed second place by being rated number two for investment prospects, number four for development prospects, and number three for homebuilding. "Land development in Edmonton is really going ahead. Partners are acquiring land. Developers are full out



with good velocity in Edmonton, where the pricing is steady and not climbing as fast as in Calgary," says an interviewee.

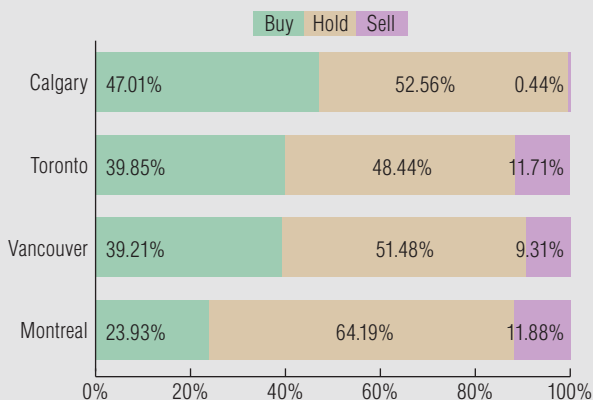
Real gross domestic product (GDP) grew considerably in the first half of 2013 at 4.2 percent, and growth is expected to remain strong through the rest of the year. The goods sector, mainly driven by the energy industry, is growing at an extremely fast rate. This is likely to continue, barring a severe economic disruption such as a recession in the United States. Service sector growth is projected to slow this year before rebounding slightly in 2014. Domestic demand remains strong supporting the wholesale and retail trade sectors, but most other service-producing industries are experiencing slower growth. Employment growth is projected to slow in 2014 to 1.6 percent.

Population growth remains strong in 2013, but is projected to slow in 2014. The demand for new homes has stayed strong in 2013, but starts are expected to slow in the second half of the year. Even with this, builders will still start more than 14,000 units. Housing starts are projected to average closer to 11,300 units over the next several years. "With the growth in Edmonton, it is a great place to buy land."

Saskatoon (3). There was nearly a three-way tie for second place. Saskatchewan's largest city scores just one basis point

EXHIBIT 5-27

Apartment Buy/Hold/Sell Recommendations



Source: *Emerging Trends in Real Estate 2014* survey.
Note: Based on Canadian respondents only.

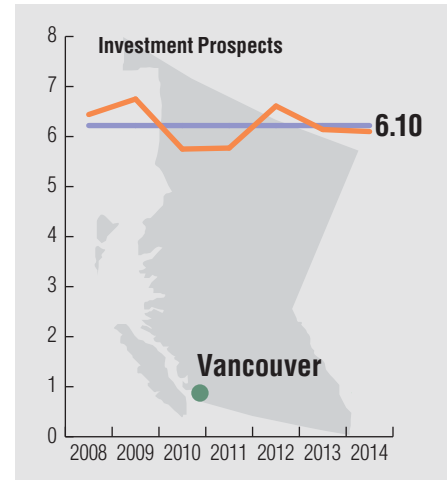
behind Edmonton, landing in third place. Saskatoon is consistently rated in this year's survey, with a three for investment and development prospects and a four for homebuilding. The smallest of the nine Canadian markets covered, with an estimated population of 285,000, reported absorption of 18,000 square feet of suburban and CBD office space during the first half of 2013.

The Saskatoon economy is growing at a robust pace. GDP growth is projected to be 5.2 percent in 2013. Manufacturing and construction are the main drivers of this economic growth, with services being the trailing sector. Potash production continues to drive economic growth in Saskatoon. A multinational energy company is moving its headquarters to Saskatoon to be closer to its potash mine. Employment growth is projected to rise at an astounding 6.1 percent in 2013 before slowing in 2014. The strong labor market is attracting new residents, and population growth is projected to be 3.5 percent in 2013 before slipping to 2.6 percent in 2014. Strong population growth has kept the residential construction industry busy. Housing starts hit a high in 2012 at 3,753 units. Starts will remain strong, but will

slow to a more sustainable level of around 2,800 units over the next several years.

Vancouver (4). This year's survey puts Vancouver in fourth place, just one basis point behind Saskatoon and 20 basis points behind Edmonton. Vancouver scored very highly for development prospects, rated number two, but trailed behind Edmonton and Saskatoon in the investment and homebuilding sectors. Vancouver is rated four for investment prospects and five for homebuilding. Interviewees express concerns over the liquidity of Vancouver's multifamily apartment market, though they see the city as reliable for long-term investments in large shopping malls.

Economic activity is projected to moderate in 2013, with the slowdown widespread through all sectors of the economy. The goods sector will be slower due to lower levels of manufacturing and construction activity. Service sector growth is also expected to be slow due to a lack of support from the goods-producing sector and lower levels of public administration spending. Employment growth is expected to be very slow in 2013 at only 0.5 percent but is projected to bounce back in 2014, growing at a 2.5 percent rate.

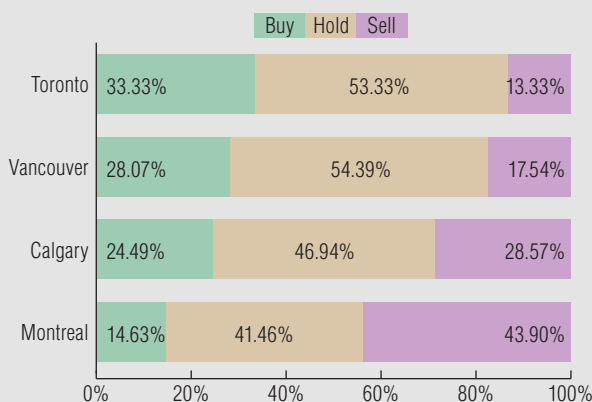


Population growth is projected to remain stable at 1.6 percent in 2014. The combination of higher population and employment growth is expected to boost personal income growth, allowing for faster consumer spending growth. This should drive an increase in retail sales of around 3.7 percent in 2014. Developers are projected to start 17,000 houses this year and in the next several years.

From a "buy" perspective, Vancouver is in the bottom half of the markets by property type. The hotel sector is the only one where respondents feel like it is better to sell than to buy in Vancouver. In general, respondents see 2014 as a market to hold for all property types, with over 50 percent of respondents making this recommendation.

Toronto (5). The survey places the Toronto market at number five for investment and development prospects, falling two rungs from number three a year earlier. Yet survey respondents still like the prospects for Toronto's homebuilding market, which was ranked as number two. The best real estate bets for 2014, says another interviewee, will be Greater Toronto area downtown office, condos in the right locations, and urban retail. They also see opportunities to place debt or equity capital in projects that are not yet financed.

EXHIBIT 5-28
Office Buy/Hold/Sell Recommendations



Source: *Emerging Trends in Real Estate 2014* survey.
Note: Based on Canadian respondents only.

Toronto's economic growth is expected to slow in 2013, but by 2014, with global economic conditions improving overall, economic activity will strengthen. This should give consumers the confidence to increase their spending. Real gross domestic product growth is forecast to reach 2.7 percent. Manufacturing, construction, and services are all expected to experience positive growth in 2014. Employment growth is projected to grow at a 1.6 percent rate next year.

Demand for new homes in Toronto has benefited from foreign investment, the improvement in the economy, low interest rates, and good population growth. With inventories rising, starts in 2013 are expected to slow. The decrease in starts is expected to be a short-term event, with starts ramping back up in 2015 to meet an expected rise in demand. Population growth in 2014 is projected to be 1.7 percent.

Toronto remains near the top of the buy, sell, or hold analysis. Ontario's largest city is the top "buy" market for office and is the number-two market for each of the other property types. Survey respondents feel strongly that Toronto is a market where you should either buy or hold. Retail and rental apartments are the only property sectors with higher "sell" recommendations, but even these are low compared with the other two choices

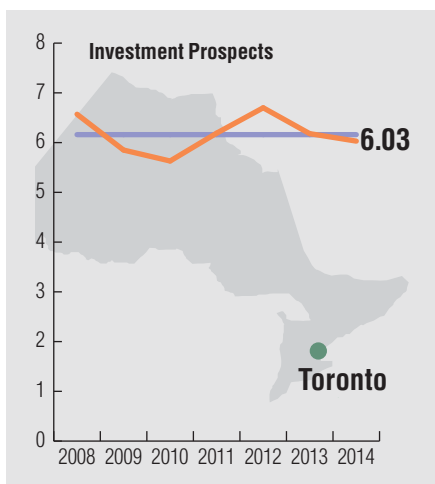
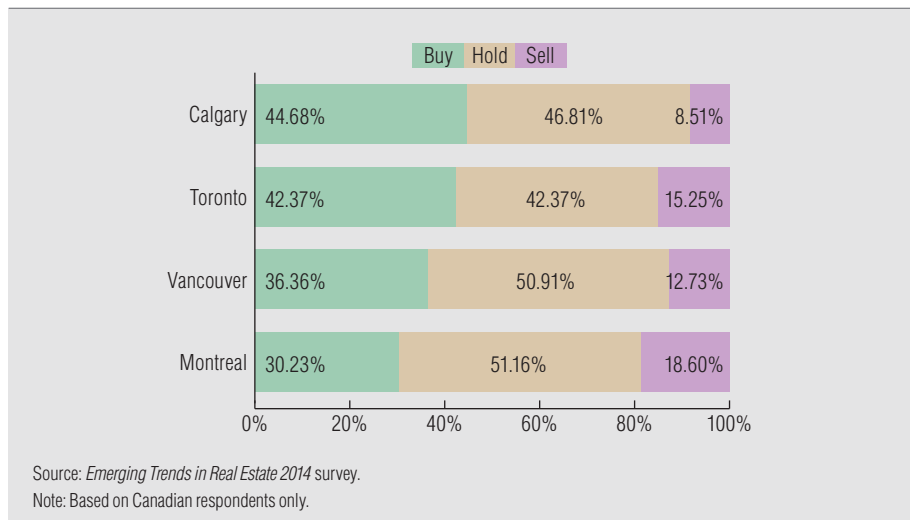


EXHIBIT 5-29

Retail Buy/Hold/Sell Recommendations



by property type. "Toronto is a great retail market, but the deals that are available are really competitive."

Winnipeg (6). The provincial capital of Manitoba climbs two rungs in this year's survey. While investment prospects are ranked seventh, development prospects and homebuilding are both ranked sixth. Winnipeg is the first of what could be considered a "second level" of markets due to a 250-basis-point difference between Winnipeg's score and that of Toronto. Interviewees say they are worried about the liquidity of the city's multifamily apartment market. "In Winnipeg, there is no pipeline for office despite constant growth," an interviewee adds.

Winnipeg's economic growth is projected to rebound in 2014 to 2.1 percent. Several factors are expected to support this stronger growth; manufacturing output, construction spending, and a growing service sector should all contribute to higher levels of economic activity. The manufacturing sector should see a boost in transportation equipment, public project construction is on the rise, and the service sector will benefit from better employment gains. Total employment is projected to rise at a 1.5 percent rate in 2014.

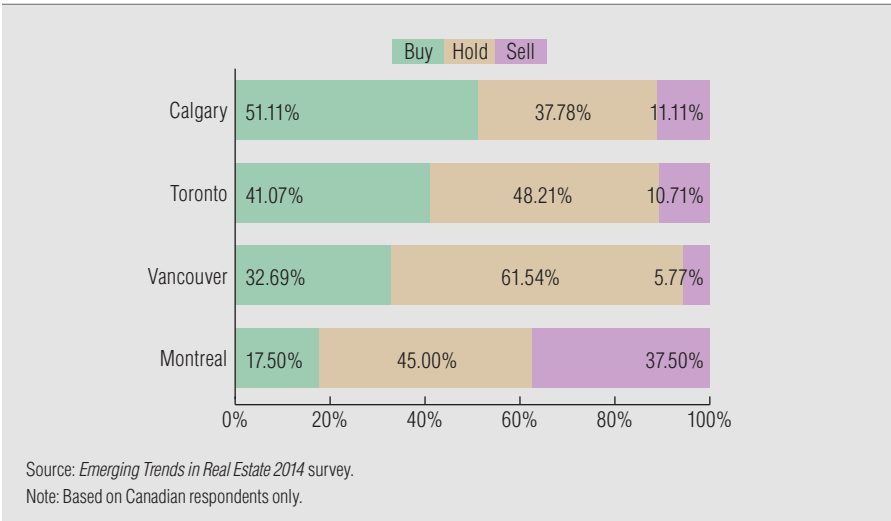
Housing construction has been boosted by both single-family and multi-family starts. Housing starts are expected to peak in 2013 and then decline in 2014 due to slower population growth and a tightening of mortgage rules that are slowing demand. Starts could rebound in 2015 if the economy continues to recover. "Winnipeg is a smaller market, which makes buying office difficult, but it is a great market for retail."

Ottawa (7). Survey respondents place Ottawa at number seven, two rungs lower than a year earlier. Canada's capital city outperforms Winnipeg in investment prospects, but trailed in development and homebuilding. Ottawa takes sixth place for investment prospects, seventh for development prospects, and sixth for homebuilding prospects. "Ottawa is soft if not shrinking," says an interviewee. Another interviewee cites recent movement out of the downtown core as another issue.

The Ottawa economy will continue to deal with federal government austerity in 2014. The public administration sector may begin to stabilize, however, which will help growth. The high-tech sector outlook is also mixed, with manufactur-

EXHIBIT 5-30

Industrial/Distribution Buy/Hold/Sell Recommendations



ing expected to continue to struggle while related services are showing some growth and are adding employees. Employment growth is projected to grow 1.6 percent in 2014.

Housing starts are projected to fall to levels not seen since 1999. The decline in jobs, tighter mortgage rules, and a balanced resale housing market are cooling demand for new housing. Housing starts are projected to remain at lower levels over the next few years.

Halifax (8). The 2014 survey places Halifax at number eight, slightly ahead of Montreal. Halifax’s prospects for investment, development, and homebuilding were all near the bottom. Investment and development prospects are both rated eighth while homebuilding is ranked ninth. One interviewee expresses concern that the Nova Centre, a 1 million-square-foot mixed-use project that is under construction, “will have significant negative impact” on the city’s commercial real estate market, while an oversupply of multifamily apartments “is already leading to rent squeeze and rental incentives.”

Economic growth in Nova Scotia’s provincial capital is projected to rise in 2014. Utilities tied to natural gas produc-

tion are projected to lead the higher level of economic activity. Nonresidential building activity will also contribute to positive economic growth. Finance, insurance, and real estate services are projected to grow as Halifax becomes a back office service center. The manufacturing sector will get a boost as production is slated to begin on a multidecade contract to build ships for the Royal Canadian Navy.

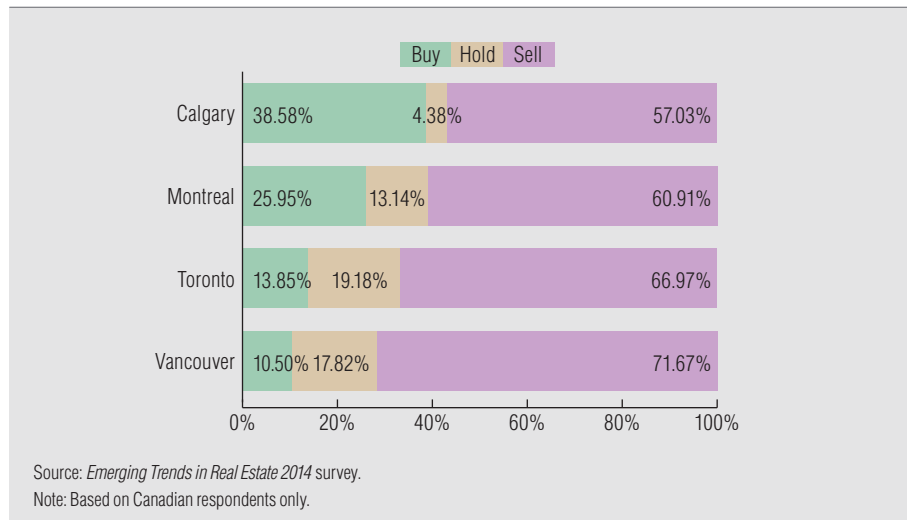
Employment growth is projected to rise 1.6 percent next year.

Housing starts have been rising in 2013, with the strength in starts coming from multifamily units. Single-family housing starts have actually been declining. The decline is a response to the number of condominiums that have recently been delivered. Housing starts are expected to remain at lower levels over the next few years.

Montreal (9). Quebec’s largest city scored just below Halifax, with a particularly low rating for development prospects, which lowered its composite score. Whether it is related to construction, corruption, or politics, interviewees expressed uncertainty about investment in Montreal. One interviewee says, “Montreal faces major risks because of uncertainty relating to politics,” referring to an anticipated election in the spring of 2014. Economic growth is projected to rebound to 2.1 percent in 2014. This level of growth is near the median of all markets. The economy has been dealing with weakness in the goods-producing sector, while the services sector has been showing steady growth. Total employment growth is expected to be slow in 2014 at only 0.6 percent.

EXHIBIT 5-31

Hotel Buy/Hold/Sell Recommendations



The Montreal office and multiresidential property markets all have some unique characteristics that will affect performance in 2014. There hasn't been a boom in office construction in decades. Some developers have land in the right location to build, but they need to have a significant tenant before they would announce a project. The few projects that were announced will go to market, but very little construction or development is expected over the next two to five years. The multiresidential inventory in Montreal is old and requires redevelopment. As one interviewee notes, a deterrent to new multiresidential construction remains rent control in Quebec. There is little incentive to invest in older inventory of multiresidential: "You never know what you'll get," and it is hard to get returns back.

The condo and industrial markets have enjoyed relatively strong performance. The condo market is vibrant; however, interviewees question whether the velocity with which presales have occurred on new-construction projects can possibly continue as banks continue to increase their presale requirements. Interviewees have mixed views on whether all projects announced will go to market, but good urbanized locations will continue to be good investments. The higher "sell" rating for industrial/distribution properties likely reflects the general age of the stock. The industrial/distribution market is in a relatively healthy condition, and owners may be able to attract premium prices by selling to investors with redevelopment plans.

Best Bets in 2014

Urban and Infill Retail Development

The outlook for retail is strong nationwide, but urban and infill retail could be exceptionally attractive in 2014. Retailers go where the customers are, and with the continuing trend toward urbanization more of those customers are moving to the urban core. Urban residential growth in multiple markets is well ahead of urban retail development. This has created a shortage of retail to serve a population that increasingly wants to live, work, and play without using transit. Retailers see this as a growth opportunity not unlike the opening of the suburbs. As they develop formats to meet the demands of the urban market, retailers will need to find attractive locations. These locations are likely to be a combination of new development and redevelopment of existing properties.

Build mixed use downtown. Mixed-use projects are soaking up investment dollars in one of the most rapidly emerging investment opportunities in Canada's major urban downtown areas. Combine condominiums with offices and retail stores to take advantage of a growing preference among reverse migrants and millennials to live, work, and play within walking distance

of downtown areas. These investments are in line with the *Emerging Trends Canada* survey, which finds that retail, for-rent residential, industrial distribution, and office space will all offer "modestly good" investment prospects in 2014.

Invest in commercial/multifamily developers. Commercial/multifamily developers are expected to have "slightly better" prospects than homebuilders in 2014. Multifamily developers may see more attractive opportunities in neighborhoods that are seeking to increase the density of development within the urban core.

Lock in or refinance at low rates. Borrowers are locking in low interest rates on loans before they climb higher—and are negotiating longer-term loans. The cost of capital is expected to increase to 4 percent from 3.5 percent in 2014. Market participants could benefit from longer borrowing terms at fixed rates.

Look for underperforming or mismanaged assets. In a strong market, look for investments that are underperforming due to poor management. Use operational skills to improve the profile and attractiveness of the asset to take advantage of strong market fundamentals and growth.



Emerging Trends in Latin America

Cross-border investment is **growing in both directions** at dramatic rates.

Two rapidly emerging trends may link the fortunes of the U.S. and Latin American commercial real estate markets more closely than in the 20 years since the U.S. Congress passed the North American Free Trade Agreement. First, Latin Americans are growing as major foreign investors in real estate in the United States—particularly in office buildings, single-family homes, and condominiums—because they regard the United States as the safest and most secure investment environment in the world. Second, U.S. investors are discovering opportunities in Latin America.

Cross-border investment is growing in both directions at dramatic rates. Investors from Latin American countries have invested a total of \$1.78 billion in real estate in the United States in 2013 thus far (through October 18)—almost double the \$855.3 million they invested during 2012, according to Real Capital Analytics (RCA). Concurrently, RCA reports that U.S. investors have invested a total of \$1.11 billion in real estate in Latin American countries in 2013 (through October 18), compared with the \$693.5 million they invested during 2012.

Latin Americans Investing in the United States

There appears to be no impediment to the flow of Latin American investment into real estate in the United States. According to fund managers and developers, Latin American investors in U.S. real estate are driven by concerns about political stability and economic policy, particularly in Argentina, Brazil, and Venezuela. They have confidence in the slow, steady

pace of economic growth and view the United States as “the safest place” in the world to “park their money” in properties that will offer strong cash flow opportunities. While Latin American investors in general have become inured to the sticker shock of high interest rates, hyperinflation, and International Monetary Fund bailouts in Latin countries over the last couple of decades, they still prefer the United States, which, they believe, is the last country in the world where they would expect to suffer any such impact to their real estate investments.

During the 12 months through August 31, 2013, \$1.54 billion of commercial real estate investment from Latin America went into U.S. office property, while the remaining \$377 million was divided fairly evenly between hotels and industrial and retail property, according to RCA.

“Most of the investors are from Brazil and Argentina. They want to put their capital in a safer place, and they want diversification,” says one fund manager.

Latin American investors are looking to single-family homes and condominiums as well. Demand from Latin American investors has cleared an inventory of tens of thousands of condos across southwest Florida, according to developers and fund managers. Now, developers from Argentina, Brazil, Mexico, and Venezuela are building new homes in Miami for Latin American buyers. A survey conducted by the National Association of Realtors shows that buyers from Mexico ranked third, after Canada and China, in foreign purchases of residential property during the 12 months through March 31, 2013. Among purchases by Mexicans, 61 percent were in California and Texas and 91 percent were of single-family detached homes.

U.S. Investors in Latin America

At the same time, U.S. investors are becoming more open to the idea of investing in real estate in Latin America. Opportunistic real estate fund managers in the United States who focus on Latin America say they are achieving internal rates of return of about 20 percent. Their investments reflect a bet on an emerging middle class of young consumers who are starting to spend in a discretionary manner.

Implications for growth are also strong in the warehousing and manufacturing sectors. “Once societies achieve middle class, they go from spending most of their money on food and shelter to spending it on more discretionary items. So whole supply chains are just being created to service that new consumerism. We are seeing that in spades in Brazil, where the industry is building out a modern supply chain for the first time. It’s very different from what you see in Los Angeles, where there already is an infrastructure,” says a U.S. fund manager who invests in Latin America.

To some extent, a similar story is being told in the emerging markets of Asia, Africa, and eastern Europe. But U.S. investors who were interviewed for *Emerging Trends* emphasized that Latin America offers greater transparency, more reliable rule of law, and less government interference than emerging markets in other regions offer. Also, some U.S. investors say they consider the cultural and language barriers in Latin America easier to cross than those in other emerging markets.

Perhaps the largest impediment to the growth of U.S. investment in real estate in Latin America is the repatriation of capital and currency depreciation. Investors interviewed for *Emerging Trends* described complex legal structures that they complained had failed to allow them to repatriate their capital, and they complained that currency depreciation had wiped out most of their gains over the last couple of years. One U.S. investor said the value of his company’s real estate investments in Brazil is “up dramatically” over the last two years in local currency terms but that currency depreciation has “taken away all of those gains.” Still, they explained, they expect their investments to deliver robust returns over the long term.

Brazil

The investment destination of choice in Latin America is Brazil, which, with nearly 200 million people, is the region’s biggest country. A recent survey by the Association of Foreign Investors in Real Estate found that, despite large protests against the government in the first quarter of 2013, foreign investors still consider Brazil more attractive than any other emerging market in the world for the second year in a row for real estate acqui-

sitions. China took first place in the survey, but Mexico—the second-largest country in Latin America—came in fifth. The survey also found that foreign investors consider Brazil second best (after the United States) in “providing the best opportunity for capital appreciation.”

A key driver of commercial real estate development in Brazil is government spending on infrastructure projects for two of the world’s most widely watched sporting events over the next three years. The government is upgrading stadiums, roads, ports, airports, and other infrastructure for the World Cup soccer tournament in a dozen Brazilian cities in 2014. It plans to undertake similar projects for the 2016 Summer Olympics in Rio de Janeiro. New hotels, restaurants, stores, and other forms of accommodation and related retail services are being built around the new stadiums and airports in anticipation of the millions of visitors that these sport events will draw to the region.

Mexico

The next Latin American country that is likely to fall into the crosshairs of U.S. real estate investors is Mexico. Multiple industry participants noted that they were encouraged by signs of reform in Mexico, where drug-related crime and violence are declining and businesses are starting to expand under a new government that came to power in 2012. So, in 2014, Mexico’s real estate industry will tap the public market for capital. In an emerging trend, the number of new real estate investment trusts (REITs) is increasing in Mexico, where the first public REIT was listed in March 2011. Many of the new REITs are apartment or mortgage companies. Still, several U.S.-based developers and fund managers who were interviewed for *Emerging Trends*, including those who currently invest in Latin America, say they will continue to avoid investing in Mexico because security concerns related to drug-related violence remain, as well as difficulty in finding skilled local partners.

“Mexico is on the [uptick] and starting to get its act together. It will be a country of the future, but in the distant future,” says a U.S. industrial developer.

Interviewees

Abu Dhabi Investment Authority

Thomas R. Arnold

Ackman-Ziff Real Estate Group LLC

Gerald S. Cohen
Simon Ziff

Aegis Property Group

Jim Kinzig

AEON USA Realty Advisors Inc.

Donald P. Guarino Jr.
Lyndsay Schumacher

AEW Capital Management

Michael Acton
Dan Bradley
Marc Davidson
Jeff Furber
Robert Plumb

Agellan Commercial REIT

Frank Camenzuli

AIMCO

Ernie Freedman

Alcion Ventures

David Ferrero

AllianceBernstein

Neil Abraham
Eric Franco

Allied Properties Real Estate Investment Trust

Michael Emory

The Alterra Group of Companies

Robert Cooper

Amacon Group

Bob Cabral

American Realty Advisors

Scott Darling
Lee Menifee

Amstar

Doug Wiley
Paul Zarian

Angelo Gordon

Reid Liffmann
Adam Schwartz
Gordon Whiting

APG Asset Management US Inc.

Steven Hason

Apollo Global Management

Joseph Azrack

ARA Finance

Tom MacManus

The Armour Group Limited

Scott McCrea

Artemis Advisors LLC

Dale Anne Reiss

Aspac Developments Ltd.

Gary Wong

Associated General Contractors of America

Kenneth D. Simonson

Ballard Spahr

Michael Sklaroff

Bank of America Merrill Lynch

Jeffrey D. Horowitz
Daniel G. Walsh

Barclay Street Real Estate

David Wallach

Barclays Capital

P. Sheridan Schechner

Baruch College

David Shulman

Basis Investment Group LLC

Mark K. Bhasin

Bay Hollow Associates

Alice Connell

Beacon Capital Partners

Jeffrey D. Brown
Kevin Whelan

Bedrock Real Estate Services

Eric Larson

Bentall Kennedy (Canada) LP

Gary Whitelaw
Paul Zemla

Bentall Kennedy (US) LLP

Chuck Burd
Douglas Poutasse

BioMed Realty Trust Inc.

Greg N. Lubushkin

Boston Consulting Group

Harold L. Sirkin

Boston Properties

Michael LaBelle
Owen Thomas

Brandywine Realty Trust

George Hasenecz
Howard Sipzner

BRE Properties

Constance B. Moore

The Bristol Group Inc.

James Curtis

Brixmor Property Group

Michael V. Pappagallo

Brookfield Office Properties

Mitchell Rudin

Bucksbaum Retail Properties

John Bucksbaum

Buzz McCoy Associates Inc.

Bowen H. "Buzz" McCoy

Cadillac Fairview Corporation

Cathal O'Connor

Canadian Apartment Properties Real Estate Investment Trust

Thomas Schwartz

Canderel

Daniel D. Peritz

CapRidge Partners LLC

Steve LeBlanc

Capright Property Advisors LLC

Jay Marling

Carey Watermark Investors Incorporated

Michael Medzigian

The Carlyle Group

Robert G. Stuckey

Carmel Partners

Ron Zeff

CBRE Group Inc.

Gil Borok
Bob Sulentic
Ray Torto
William C. Yowell
Ross Moore (Canada)
Tom Frye

CBRE Econometric Advisors

Jon Southard

CB Richard Ellis Limited

John O'Bryan

Champion Partners Ltd.

Jeffrey L. Swope

Charles River Realty Investors

Brian H. Kavogian

Charter Homes & Neighborhoods

Robert P. Bowman

Cigna Realty Advisors

Bill Carlson
John Clark
Nando Parete

Citi Private Equity Services

Michael Dwyer

CitiStates Group

Peter Katz

City Center Lehigh Valley

J.B. Reilly

Claridge Homes

Neil Malhotra

Clarion Partners

Stephen J. Furnary
Tim Wang

Colony Capital

Richard B. Saltzman

Columbia Property Trust

E. Nelson Mills

Commercial Properties Limited

John K.F. Irving

Compatriot Capital

Paul E. Rowsey III

The Concord Group

Richard M. Gollis

Connecticut Retirement Plans and Trust Funds (CRPTF)

Cherie Santos-Wuest

Cornerstone Real Estate Advisers

Jim Clayton
David J. Reilly

Cousins Properties

Lawrence Gellerstedt

CRE Finance Council

Stephen M. Renna

Crescent Communities

Margaret Jenness

Crescent Real Estate Holdings

John C. Goff

CRL Senior Living

Douglas Cameron

Crow Holdings International

Harlan Crow
Anne Raymond

Crown Realty Partners

Michael A. Pittana

Cushman & Wakefield

Bill Hartman
Steven A. Kohn
Maria Sicola

DCT Industrial

Philip Hawkins
Tom Wattles

DDR Corp.

Dan Hurwitz

Deloitte

Robert O'Brien

Desjardins Asset Management

Michel Bédard

Deutsche Asset & Wealth Management

Scott Koenig

DiamondRock Hospitality Company

Mark W. Brugger

DivCore Real Estate Asset Management LLC

Michael Carp

Dividend Capital Group, University of Denver

Glenn Mueller

DLC Management Corp.

William Comeau

DLJ Real Estate Capital Partners LLC

Chip Andrews

Donahue Schriber

Lawrence P. Casey
Patrick S. Donahue

Dorsay Development Corporation

Geoffrey Grayhurst

DRA Advisors

Paul McEvoy Jr.

DREAM Unlimited Corporation

Jason Lester

Dundee International Real Estate Investment Trust

Jane Gavan

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