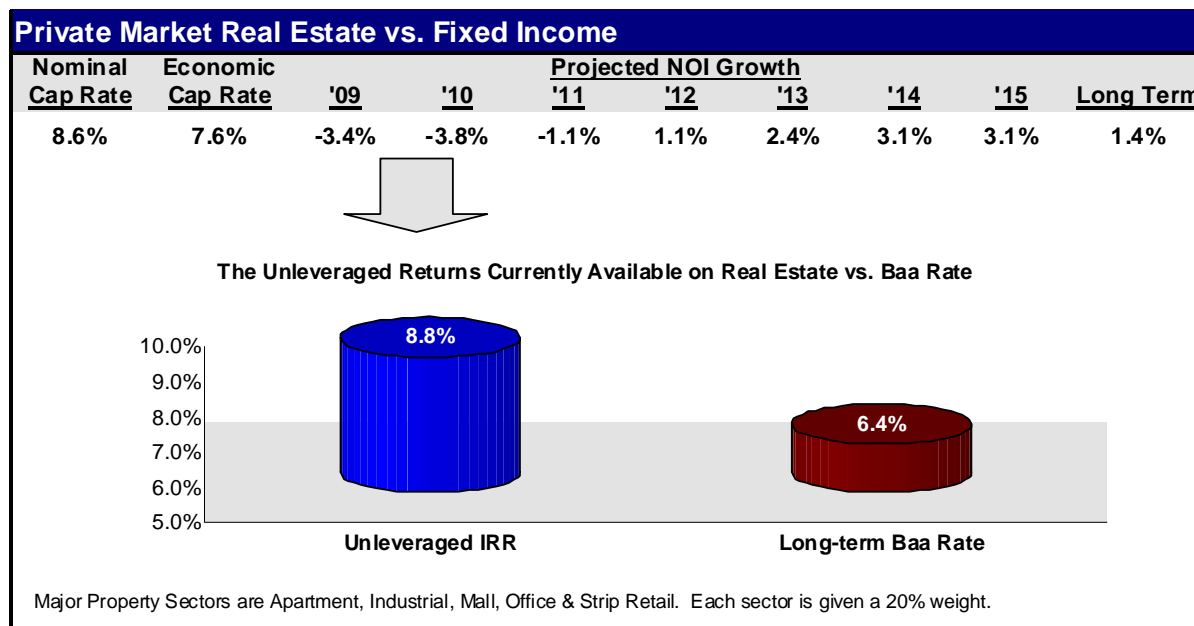


*Wisconsin Real Estate Trends Conference*

**Commercial Real Estate: Distress & Opportunity**

# Expected Unleveraged Returns

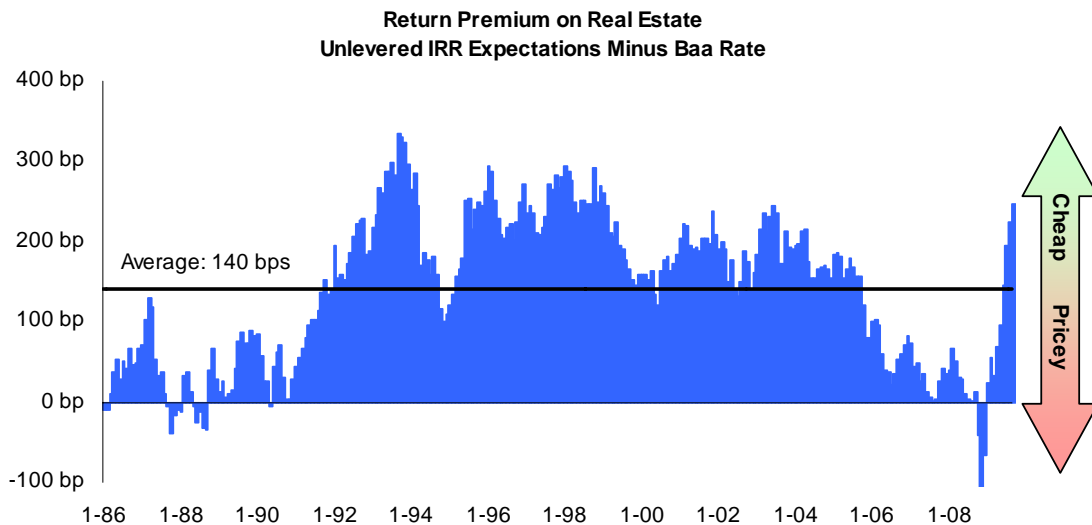
- Based on the weighted average major-property-sector cap rates and growth rates shown below, it is possible to calculate the expected unleveraged returns (IRRs) that real estate investors can currently expect to achieve.



As of 9/1/09

# Return Premium on Real Estate – IRRs less Baa Bonds

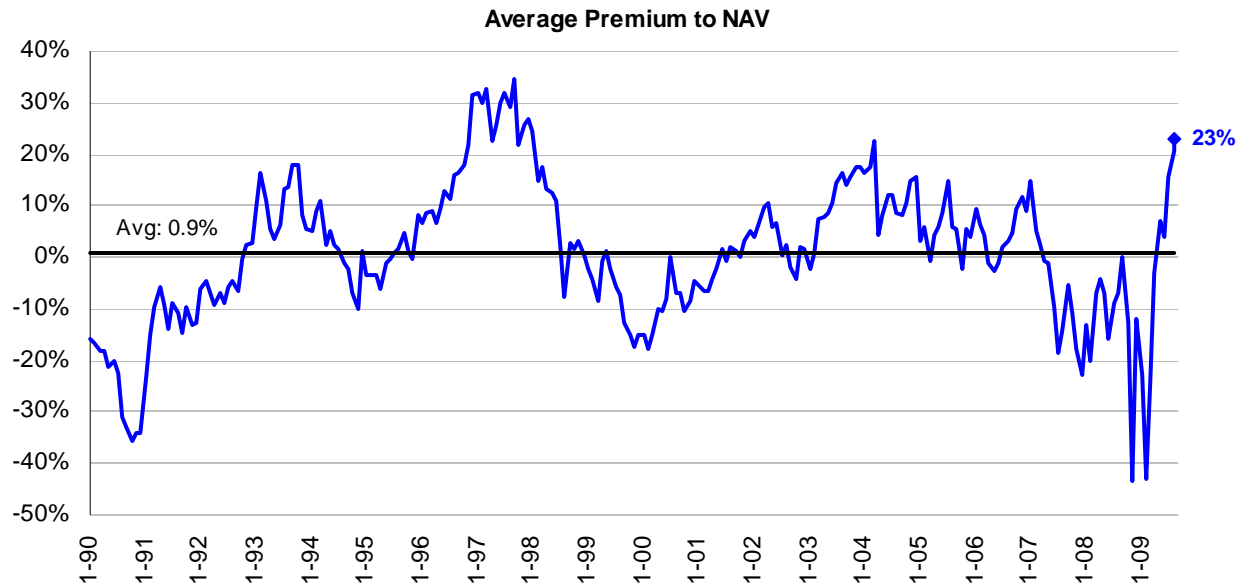
- Current valuation levels can be assessed by comparing prevailing return premiums (i.e. expected IRRs less Baa rates) vs. historic norms. Risk premiums that have been higher than the historic norm have typically preceded periods of outsized appreciation in real estate values, and vice versa. The current spread of 247 bps suggests that private market real estate is cheap compared to long-term bonds.



As of 9/1/09

# Average Premium to NAV

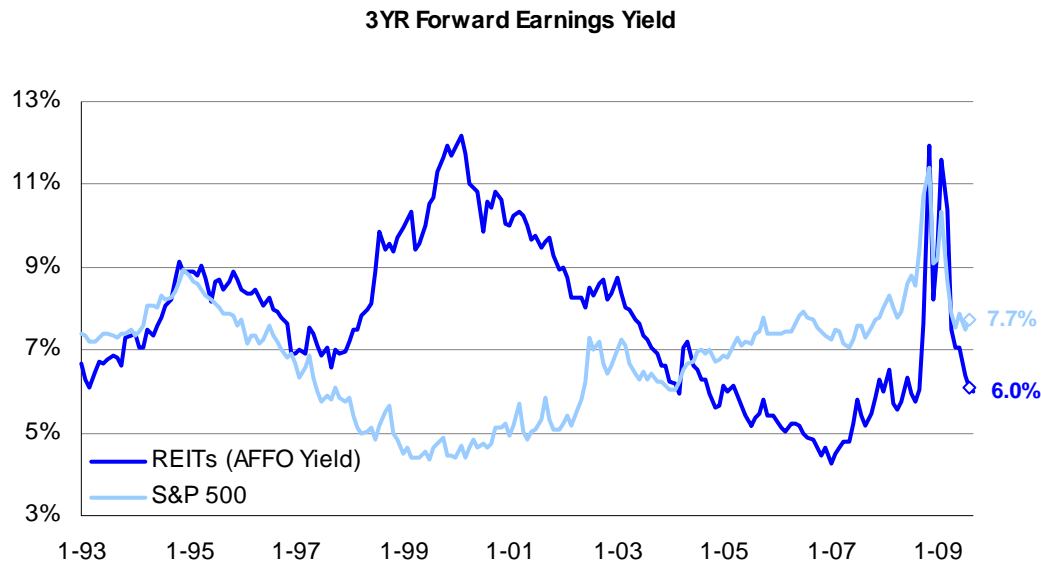
- Observed NAV premiums/discounts in the public market have historically been reliable predictors of future changes in private-market prices. While false signals can occur, large premiums usually precede rising property values, and vice versa.



As of 9/10/09

# Three Year Forward Earnings Yield

- AFFO yield is the REIT industry's proxy for the earnings yield on the broad market. Despite wide swings, earnings yields on REITs and stocks have been about equal. Currently REITs are priced to yield 170 bps less than the broader stock market, suggesting that public real estate is pricey compared to the S&P.

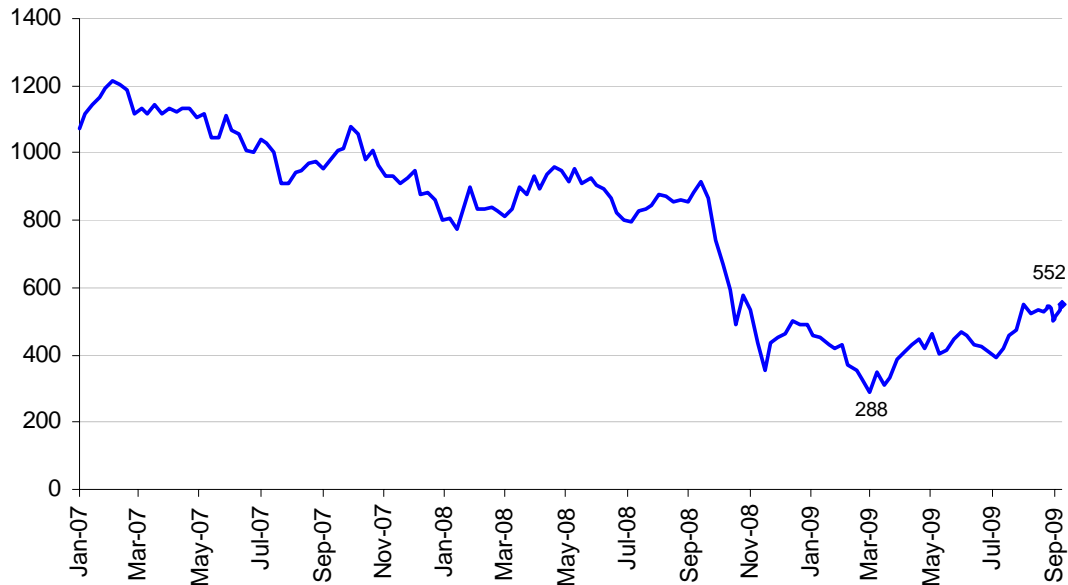


As of 9/4/09

# RMZ Index

- After reaching an all-time high in early March '07 the RMZ lost a staggering 76% of its value over the next two years before bottoming out in early March '09. Since then the market has rallied 92%.

**MSCI US REIT Index (RMZ)**

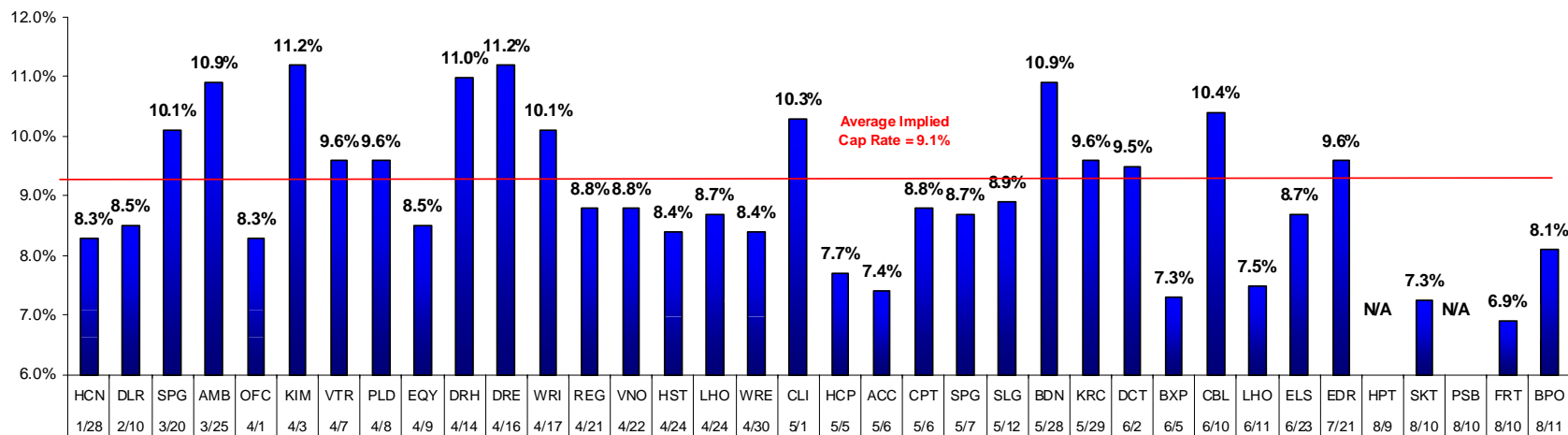


As of 9/10/09

# 2009 Equity Offerings

- In 2009, U.S. REITs have raised nearly \$15 billion of new equity, inducing a virtuous cycle of balance sheet repair and rising share prices. While many of these offerings have been costly based on implied cap rates, they have been a step in the right direction for reducing leverage and improving liquidity positions.
- Equity raises earlier in the year were at significantly higher implied cap rates than more recent offerings, as the REIT market has rallied over 90% from its March '09 low.

Implied Cap Rates on Recent Equity Offerings



As of 9/1/09

## Unsecured Debt Markets

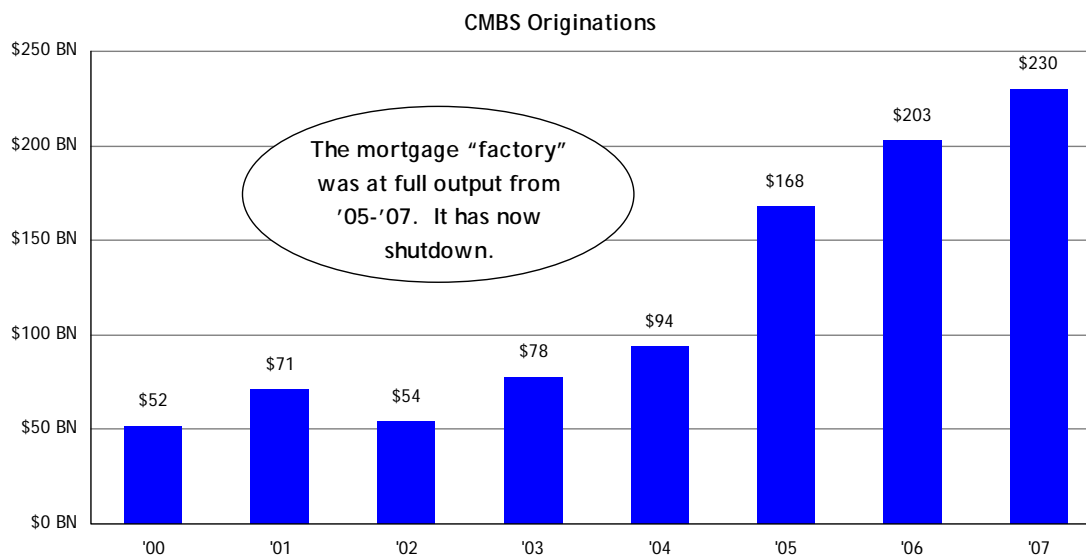
- In August the unsecured debt market for REITs began to thaw.
- REITs raised \$2.55 billion in unsecured debt last month.

Ticker	Date	Amount (\$000's)	Rate	Effective Maturity	Type	Convert Price
Simon Property Group	3/20/2009	\$650,000	10.4%	4/1/2019	Unsec.	
Ventas	4/7/2009	\$200,000	6.50%	6/1/2016	Unsec.	
Digital Realty Trust	4/14/2009	\$260,000	5.5%	4/15/2014	Convertible	\$43.00
Alexandria RE Equities	4/21/2009	\$225,000	8.0%	4/15/2014	Convertible	\$41.40
Starwood Hotels	4/30/2009	\$500,000	7.88%	5/15/2014	Unsec.	
Host Hotels	5/5/2009	\$400,000	9.0%	5/15/2017	Unsec.	
Simon Property Group	5/11/2009	\$600,000	6.75%	5/15/2014	Unsec.	
Mack-Cali Realty	8/5/2009	\$250,000	7.88%	7/15/2019	Unsec.	
Simon Property Group	8/6/2009	\$500,000	6.75%	5/15/2014	Unsec.	
Duke Realty	8/6/2009	\$250,000	7.38%	2/15/2015	Unsec.	
Duke Realty	8/6/2009	\$250,000	8.25%	8/15/2019	Unsec.	
ProLogis	8/11/2009	\$350,000	7.63%	8/15/2014	Unsec.	
Weingarten Realty	8/13/2009	\$100,000	8.10%	8/15/2019	Unsec.	
Federal Realty	8/17/2009	\$150,000	5.95%	8/15/2014	Unsec.	
Westfield Group	8/19/2009	\$700,000	7.50%	8/15/2014	Unsec.	
<b>Total</b>		<b>\$5,385,000</b>				

As of 8/19/09

## CMBS Problems

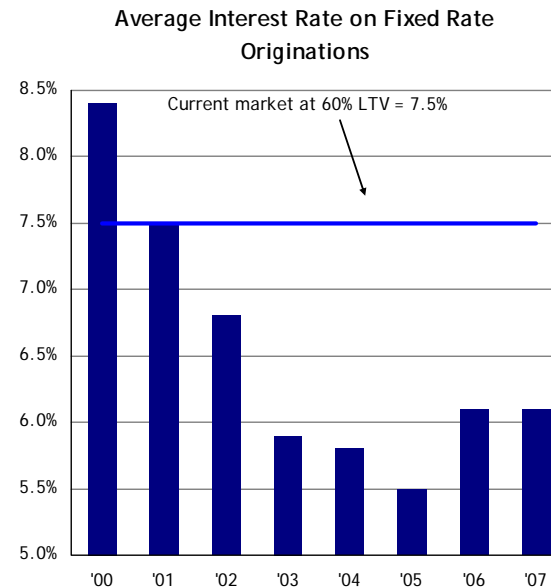
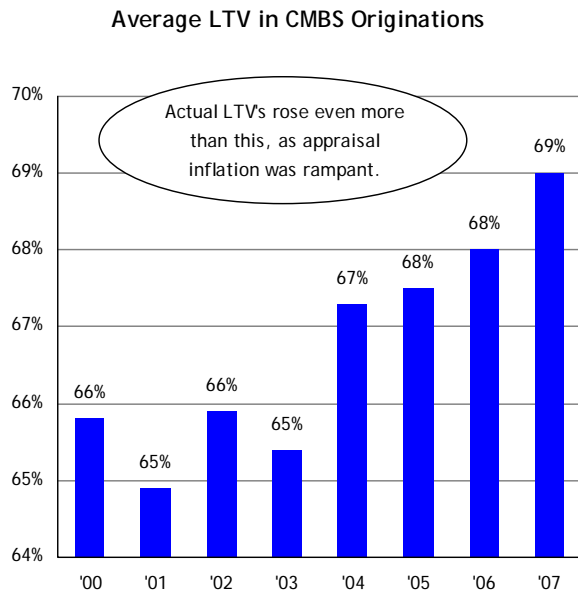
- The making of a mess: the pace of commercial mortgage originations exploded between '05 and '07 at the same time that underwriting standards became extraordinarily loose. Think of this as commercial real estate's version of sub-prime lending.



Sources: Mortgage Bankers Association, Wells Fargo, Eastdil Secured

# CMBS Problems

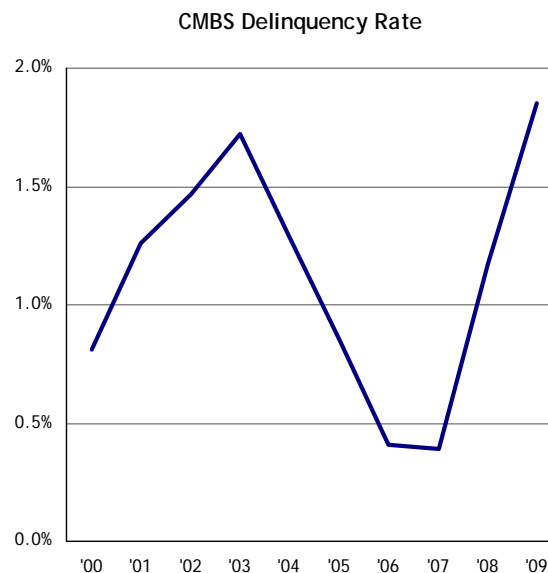
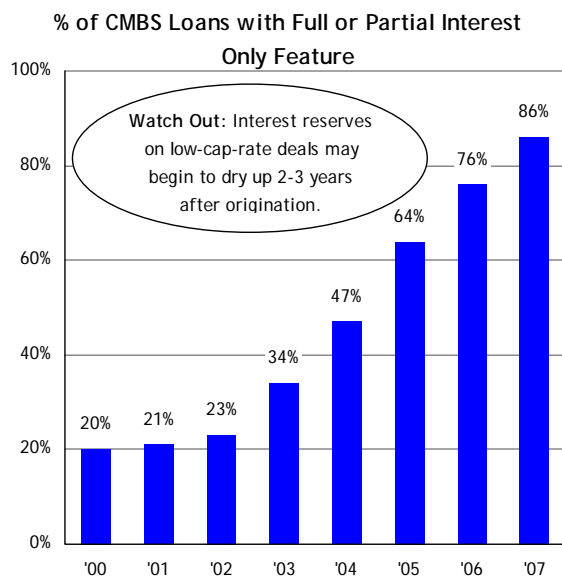
- The '05-'07 CMBS vintages were underwritten at very aggressive loan-to-value ratios amidst an environment where appraisals were often inflated and borrowing costs were well below current levels.



Sources: Mortgage Bankers Association, Wells Fargo, Eastdil Secured, Green Street

# CMBS Problems

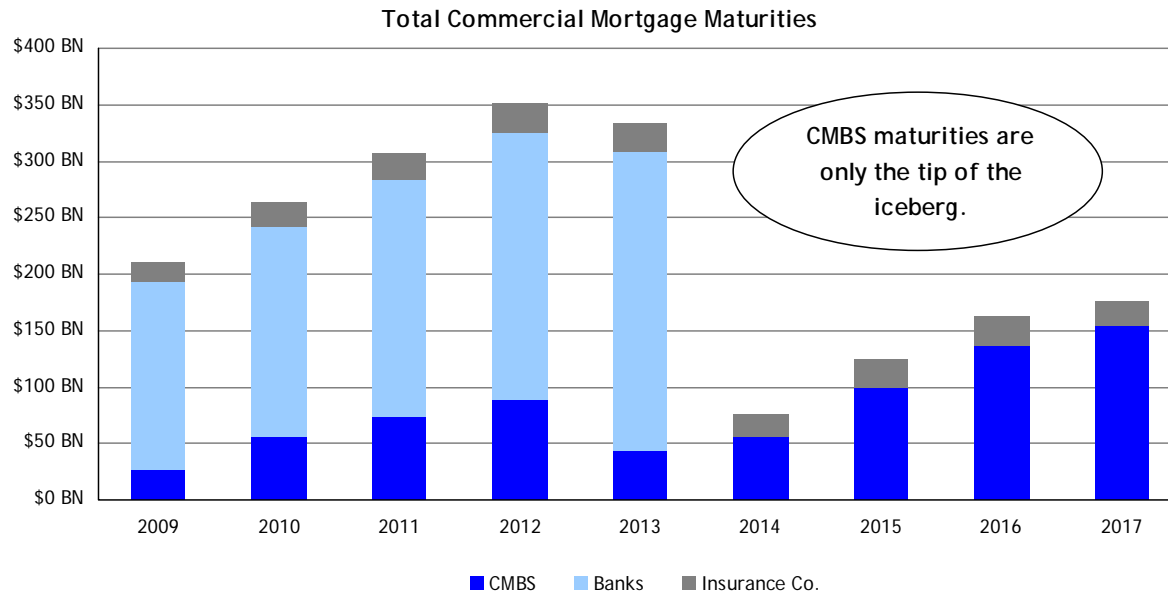
- Defaults have recently picked up, despite loose terms that called for little, if any, pay-down of principal. They will soon go “off the chart”.



Sources: Mortgage Bankers Association, Wells Fargo, Eastdil Secured. Delinquency rates as of the end of the year; '09 is end of 1Q.

# CMBS Problems

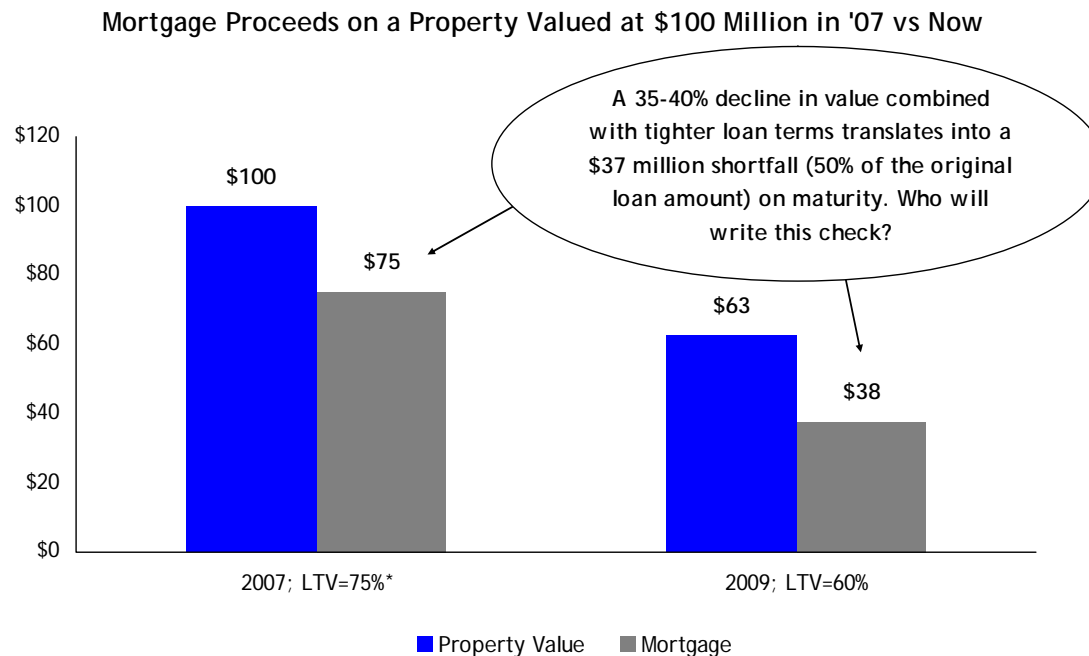
- CMBS maturities will be ugly, but they're only the tip of the iceberg. Over \$1 trillion of maturities occur by '12.



Sources: Mortgage Bankers Association, Wells Fargo, Green Street, Trepp, Bank of America, Deutsche Bank

# Where Will Real Estate be Priced?

- Maturities will be a mess: refinancing will require huge checks.



\* LTV calculated off the appraised value would have been lower. Appraised values were often inflated during the boom.

## Contact

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**Green Street Advisors**  
**567 San Nicolas Drive, Suite 200**  
**Newport Beach, CA 92660**

**Contact:**

**Adam Markman, Managing Director**

**[amarkman@greenst.com](mailto:amarkman@greenst.com)**

**949.640.8780**

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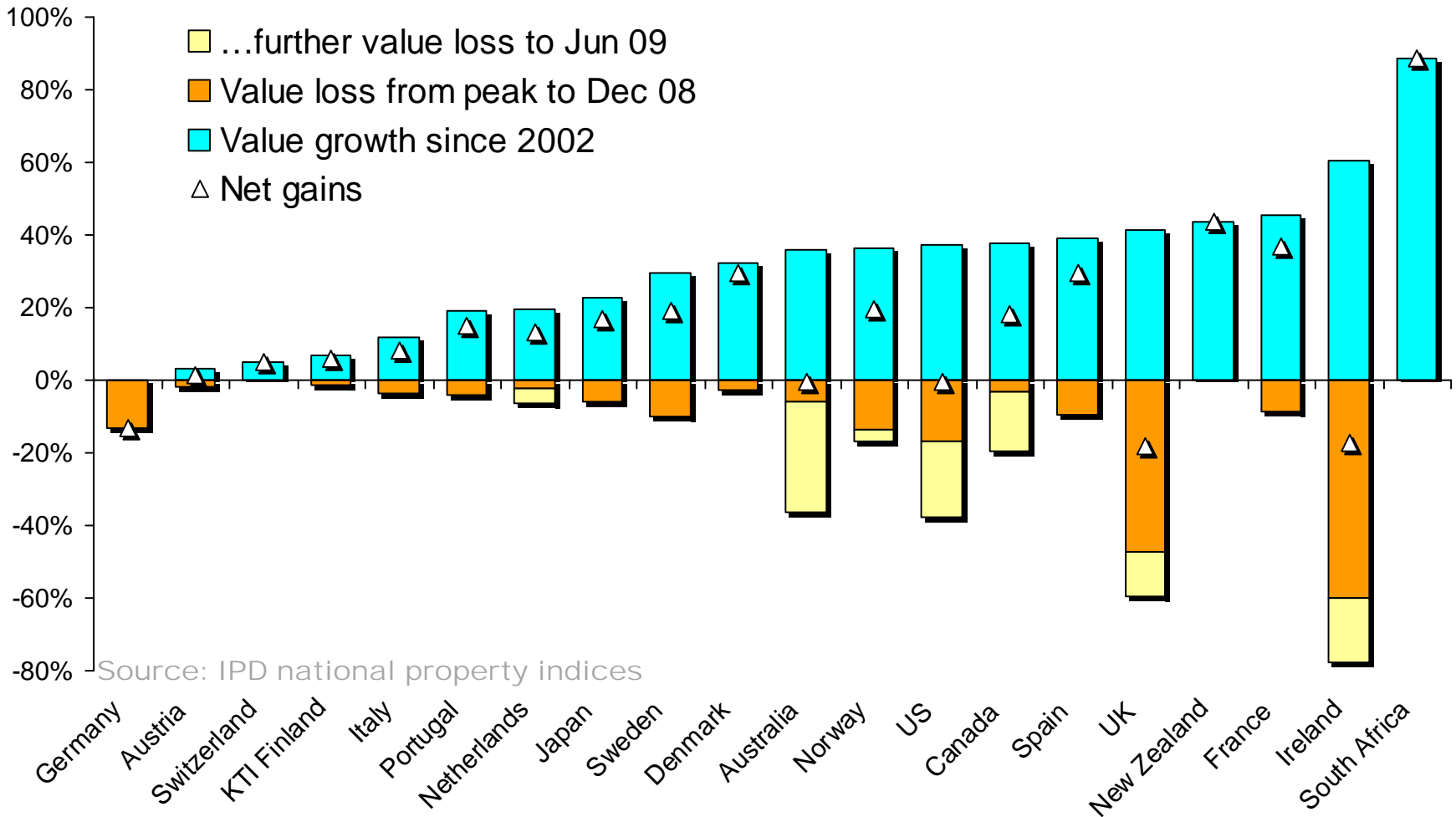
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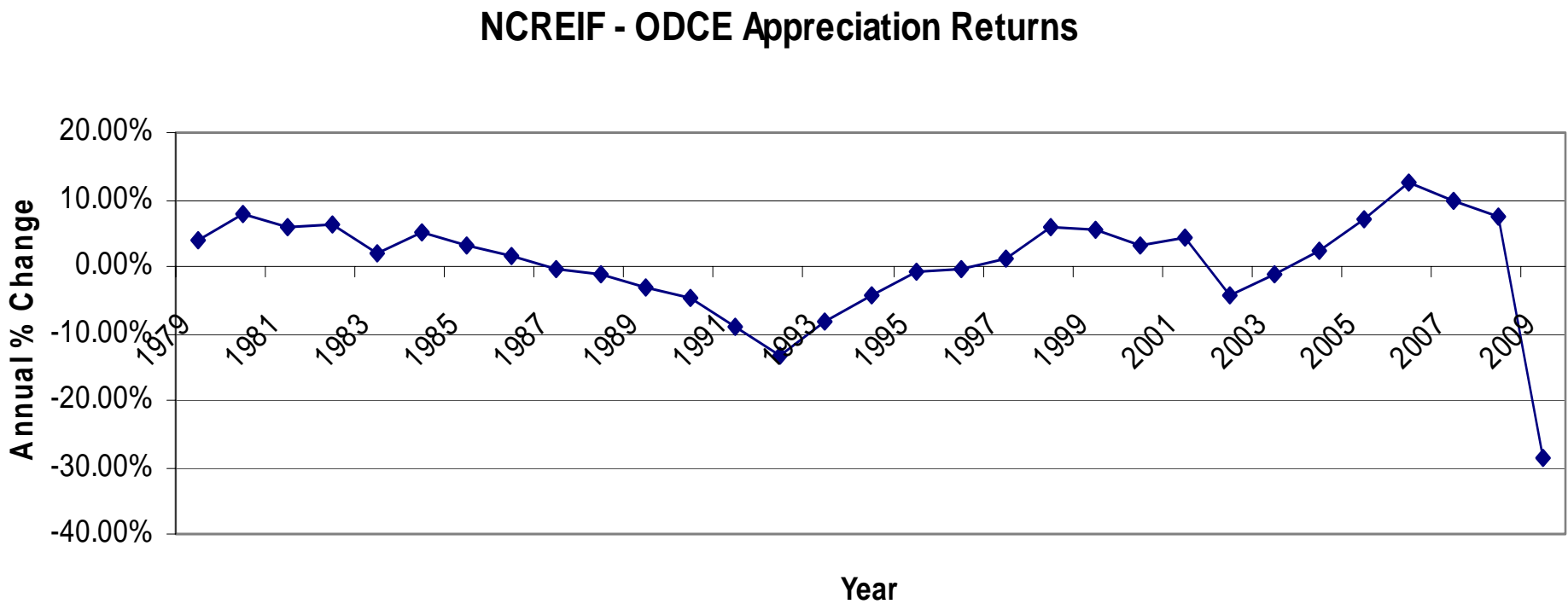
# Boom and Bust...



Growth in direct property capital values since 2002, and subsequent value fall since peak %



# NCREIF Historic Appreciation Returns



# NCREIF – Average Historical Cap Rates

- The long term median transaction cap rate since 1983 is 8.51% (current 7.3%).

