



Emerging Trends in Real Estate 2009

Bob Gardner, Managing Director

RCLCO

ULI Los Angeles District Council | November 18, 2009

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ROBERT CHARLES LESSER & CO. REAL ESTATE ADVISORS

AGENDA



Where We Are Today

- ▶ The Recap
- ▶ Recent Market Performance

Where We Are Headed

- ▶ Sentiment Survey Results
- ▶ Economic Forecasts

What's It Mean For Real Estate

- ▶ Key Considerations
- ▶ Product opportunities



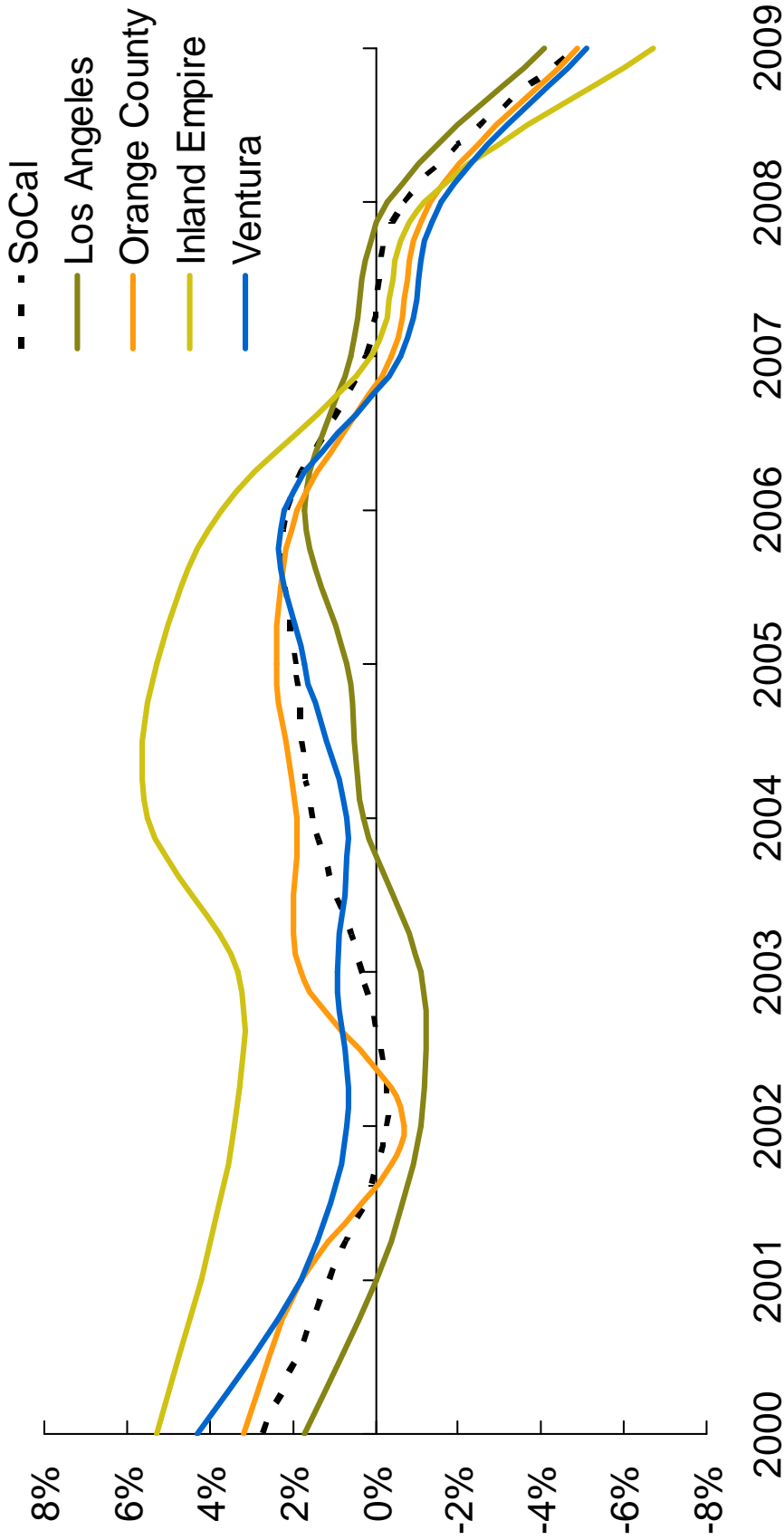
The Recap

2000 – 2009: THE RECAP FOR LA REGION MORE PEOPLE AND HOUSING, NO GAIN IN REAL INCOME

- ▶ **Population**
 - 2009 population in five-county region -- 18.5 million, up 12% over the 2000 population of 16.5 million
 - LA County – 10.3 million in 2009, up 8.5% over 2000 population of 9.6 million
- ▶ **Residential Permits**
 - 575,000 total permits through 2008; two-thirds were single-family
 - Half of total permits in IE
- ▶ **Commercial Space**
 - Industrial space supply increased to 1.15 billion sf, an increase of 15%; two-thirds in IE
 - Office space supply increased to 519 million sf, up 7%.; 50% of increase located in OC
- ▶ **Employment**
 - Sept 2009 employment at 6,700,000, virtually unchanged since 2000.
 - Peak during decade was 7,219,000 in Sept 2007; jobs have fallen nearly 8% from peak
- ▶ **Per Capita Personal Income**
 - 2008 per capita income ranged from a high of \$49,000 in OC to a low of \$28,000 in IE
 - Adjusted for inflation, per capita income in 2008 is no different than 2000 – no real income gain!

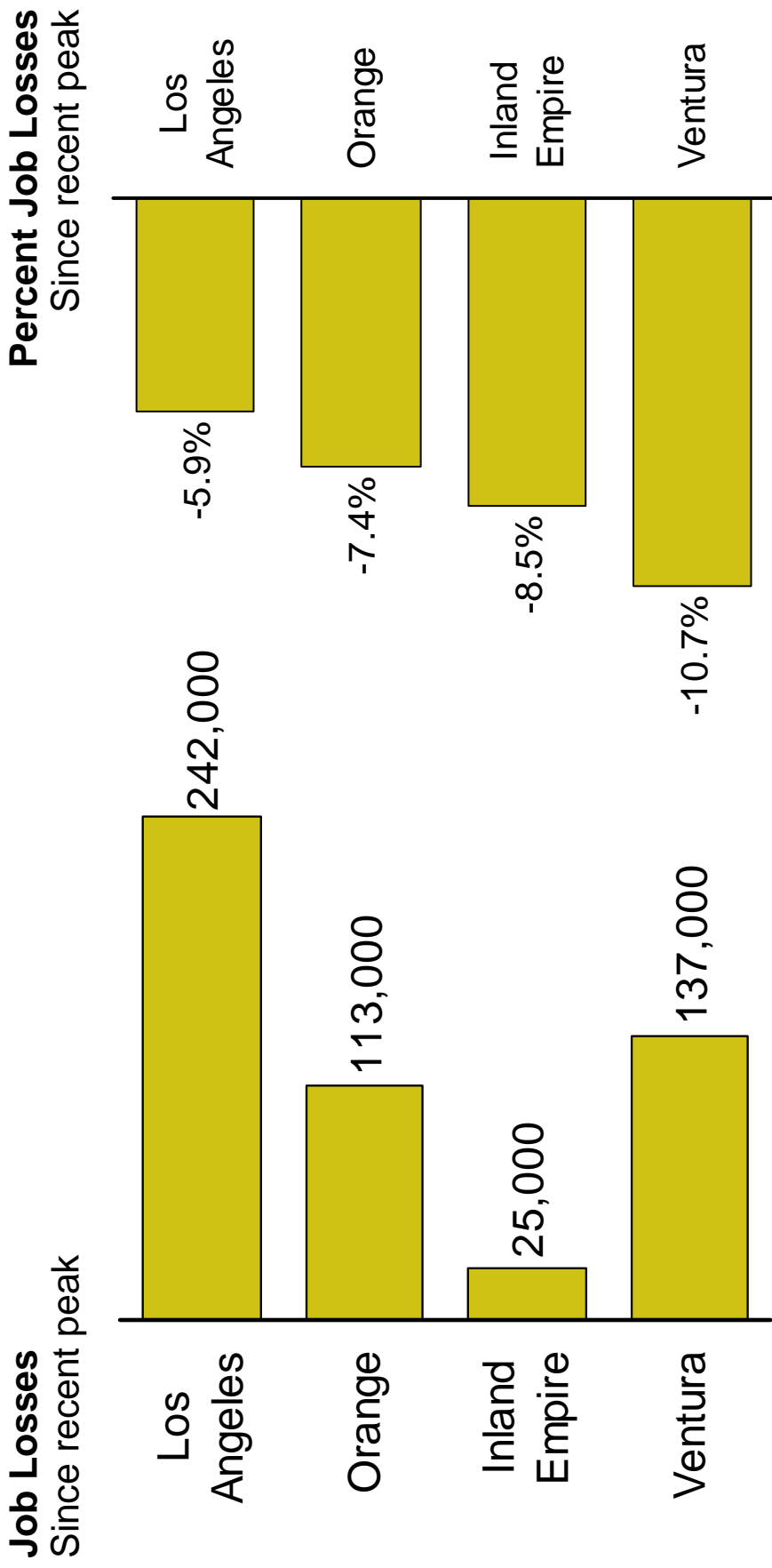
JOB LOSSES ACCELERATED IN 2009 FOR LA REGION, 2009 JOB TOTAL SAME AS 2000 TOTAL

Employment Growth Rate
Southern California (by county)



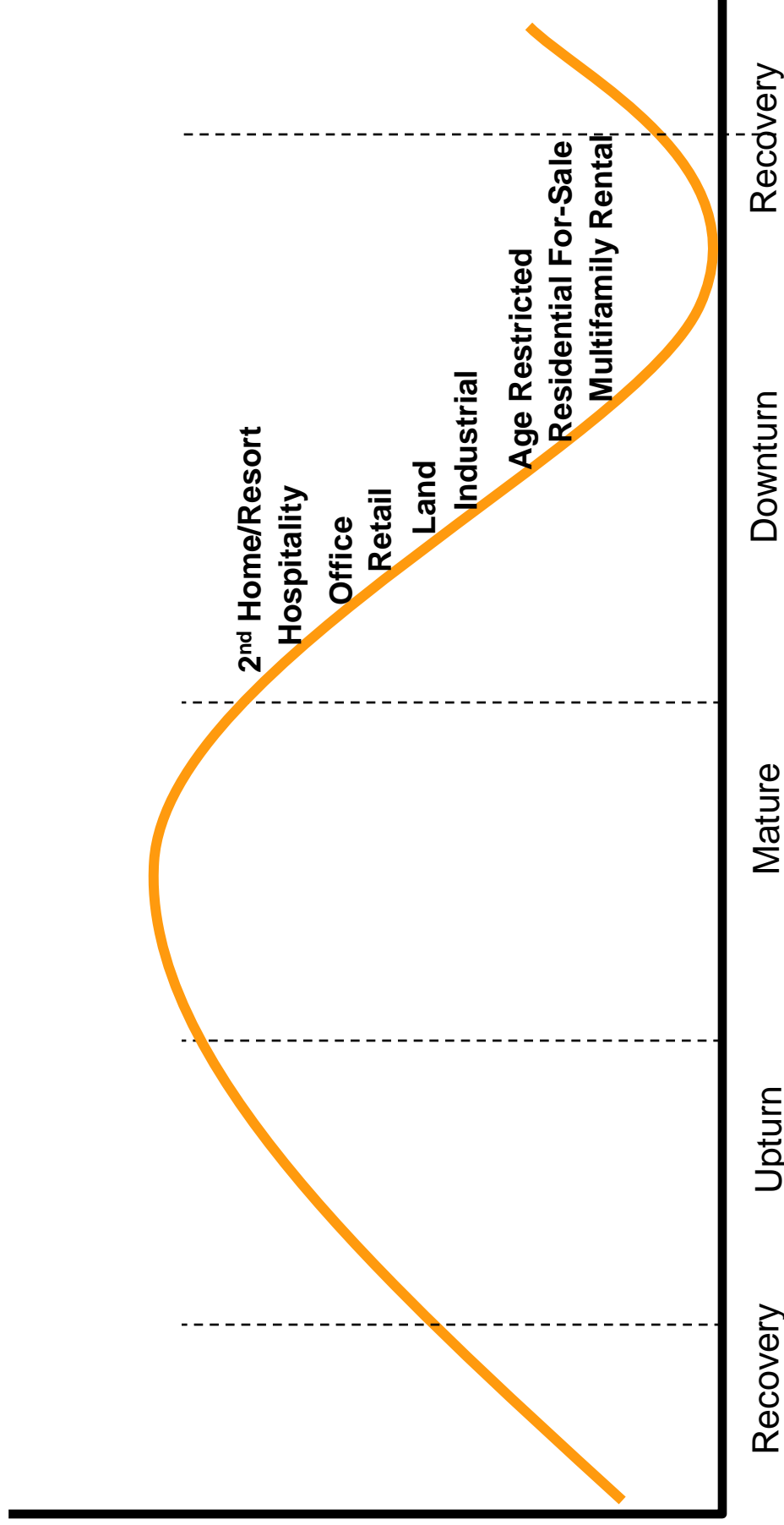
SOURCE: U.S. Bureau of Labor Statistics, LAEDC

STUNNING EMPLOYMENT LOSSES SINCE 2006/07 LA TOTAL NOW BELOW 2000; OTHER COUNTIES ABOVE



SOURCE: Bureau of Labor Statistics; National Bureau of Economic Research; RCLCO

WHERE WE ARE TODAY THE REAL ESTATE CYCLE – STILL IN THE DOWNTURN

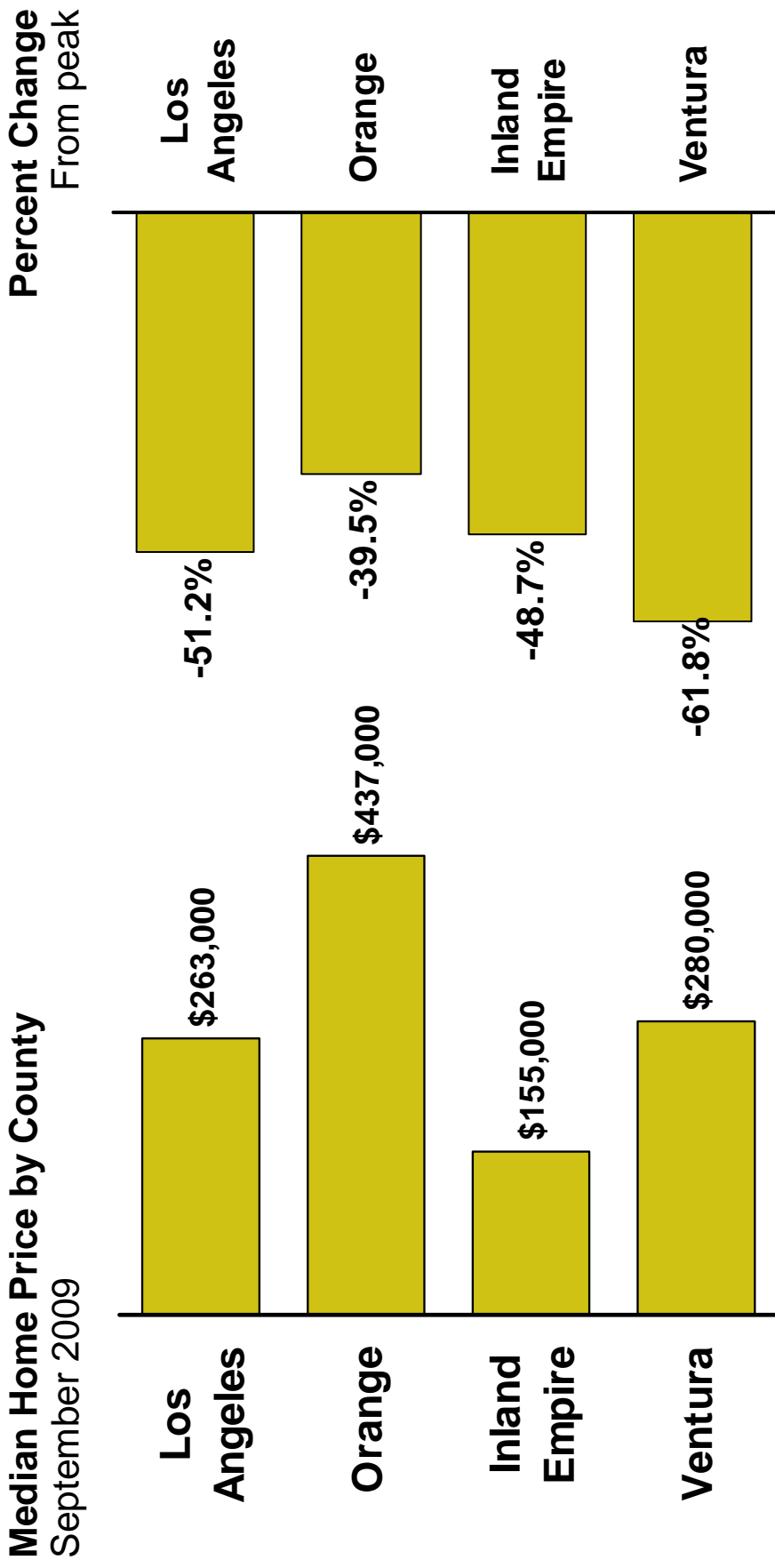


SOURCE: RCLCO Market Sentiment Survey September 2009



Recent Real Estate Product Performance

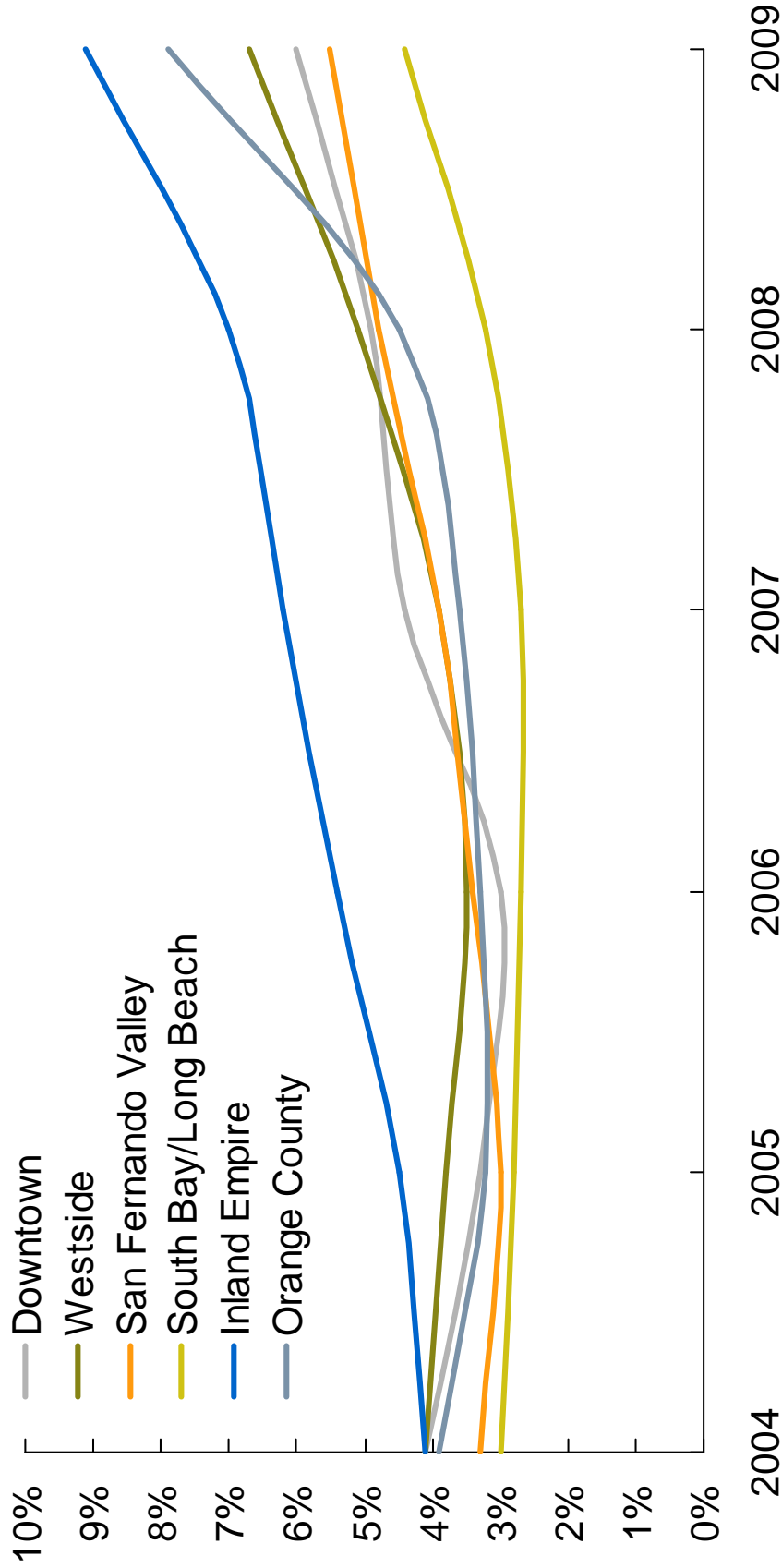
HUGE DECLINES IN HOUSING PRICES BACK TO PRICES SEEN IN 2002 AND 2003; PEAKED IN 06/07



SOURCE: Economy.com

APARTMENT MARKETS WEAKENED FURTHER RENTAL RATE DECLINES ACCOMPANY RISING VACANCY

Apartment Vacancy Rate
Southern California (by submarket)

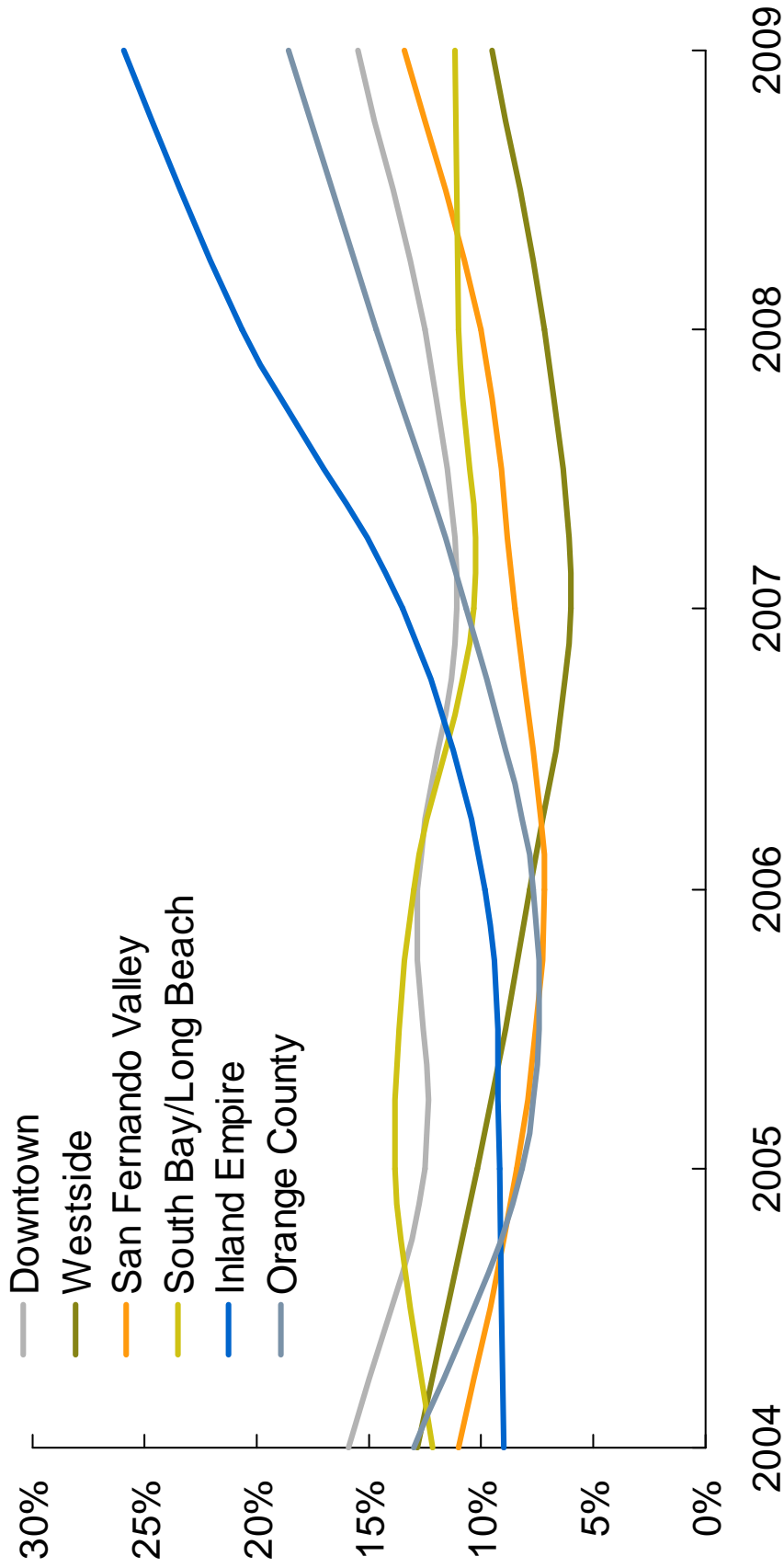


NOTE: 2008 reflects year-end forecast as of Third Quarter 2008.

SOURCE: Marcus & Millichap; REIS

OFFICE MARKETS SOFTENED ACROSS REGION ALL MARKETS NOW OVERSUPPLIED

Office Vacancy Rate
Southern California (by submarket)

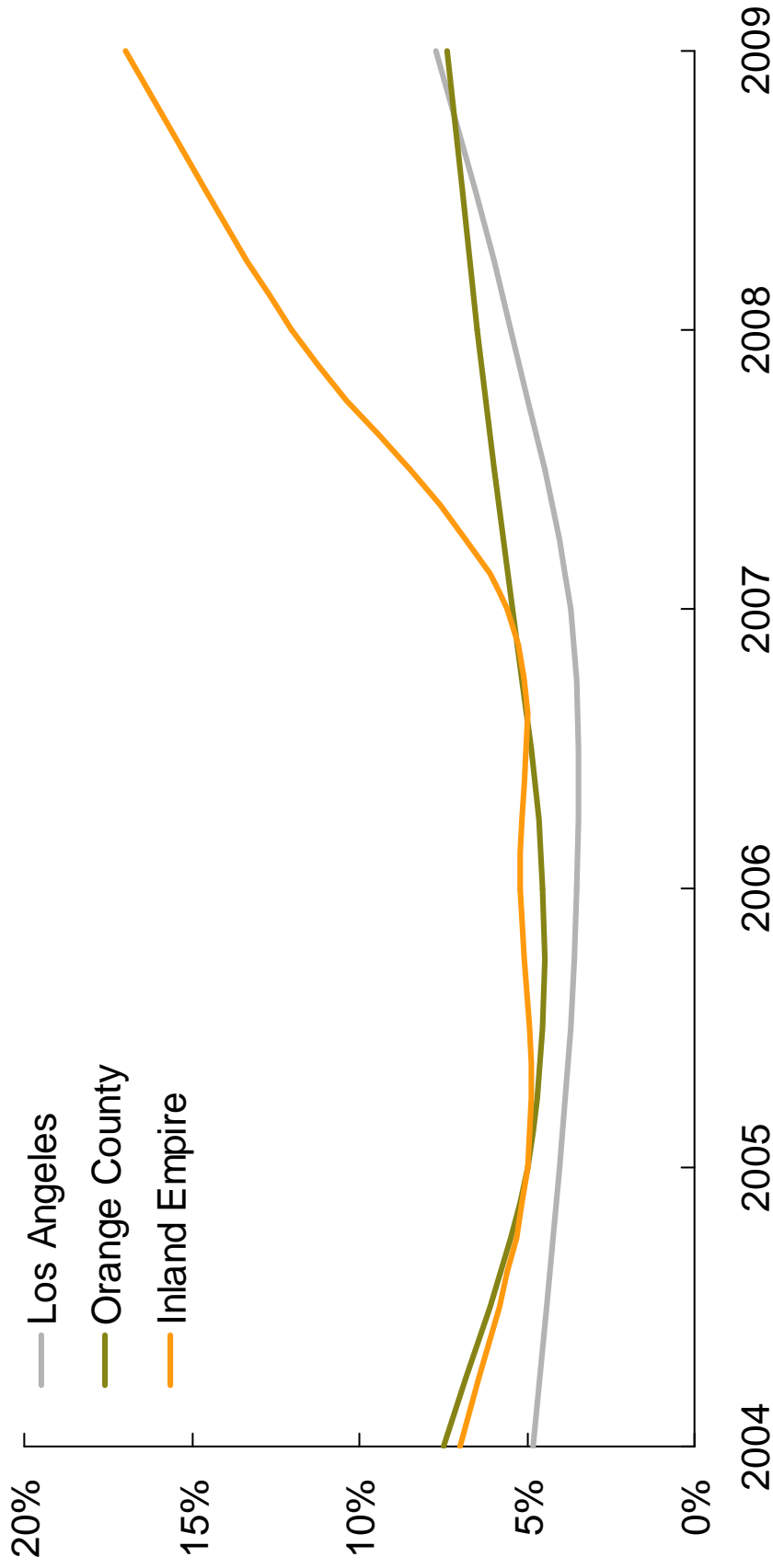


NOTE: 2008 reflects year-end forecast as of Second Quarter 2008.

SOURCE: Marcus & Millichap; REIS

INDUSTRIAL MARKETS SHOW FURTHER DECLINE IE SUBSTANTIALLY OVERSUPPLIED

Industrial Vacancy Rate
Southern California (by submarket)

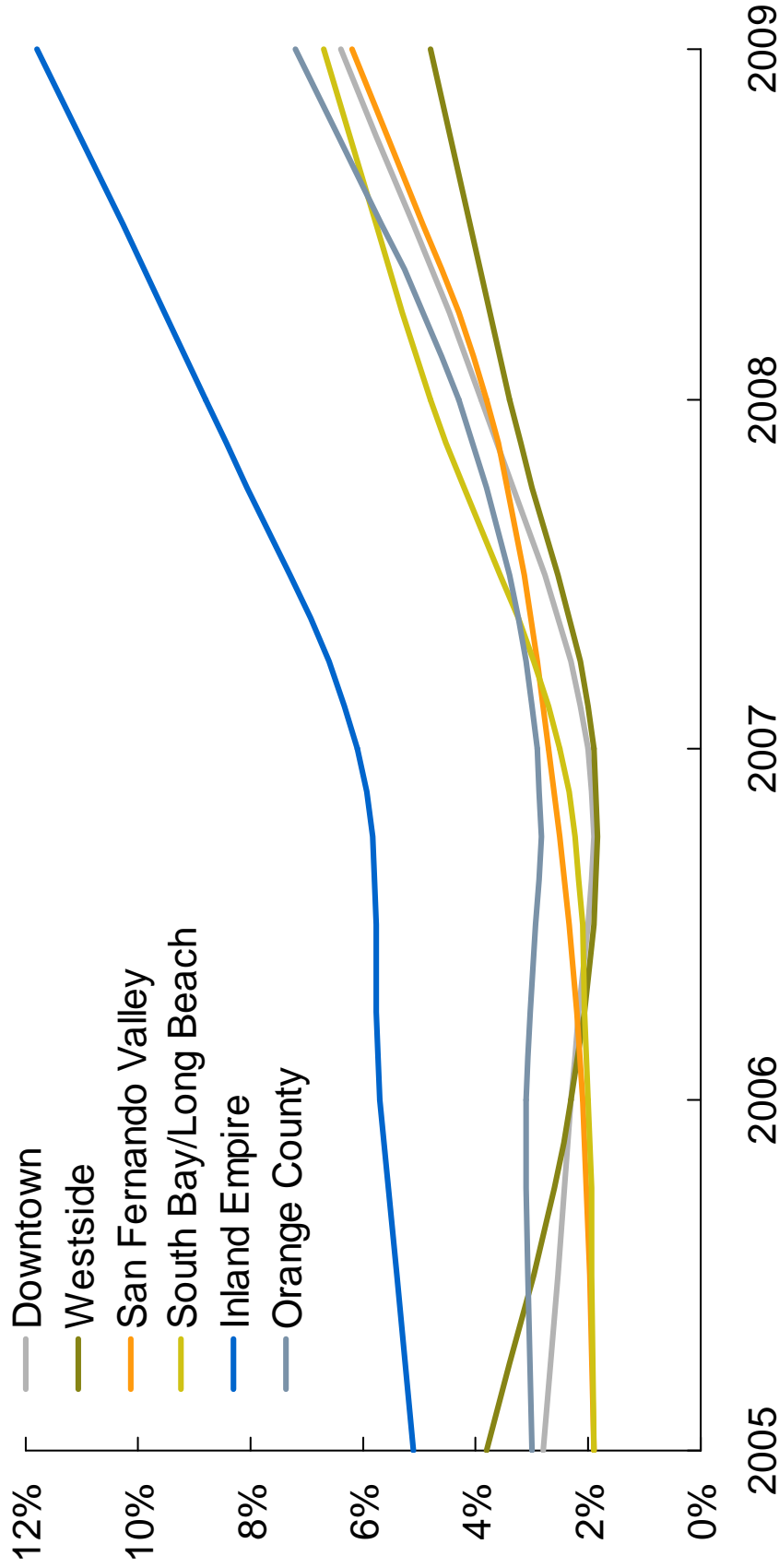


NOTE: 2008 reflects year-end forecast as of Third Quarter 2008.

SOURCE: Marcus & Millichap; REIS

RETAIL MARKETS CONTINUE WEAKNESS CONSUMER RETRENCHMENT – NO SURPRISES HERE

Retail Vacancy Rate
Southern California (by submarket)



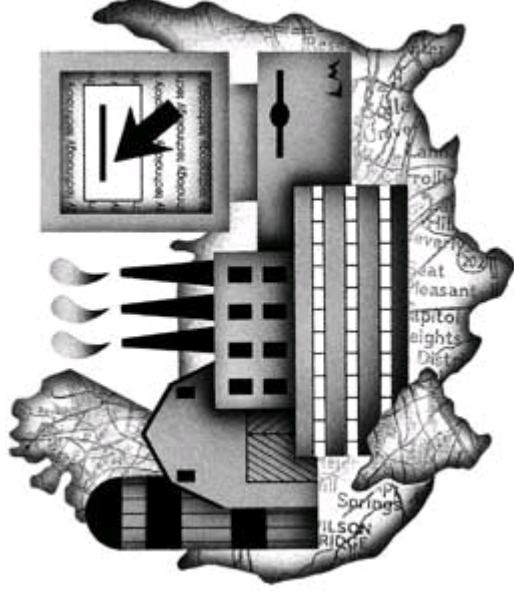
NOTE: 2008 reflects year-end forecast as of Third Quarter 2008.

SOURCE: Marcus & Millichap; REIS

OFFICE TRENDS, 2000 - 2009

EXPANDED SUPPLY; NOT EXCITING PERFORMANCE

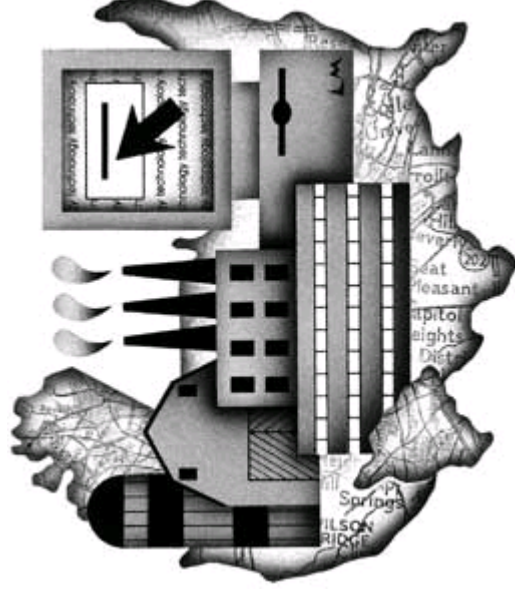
- ▶ **2009 occupancy rates across all five counties ended below 88%; all oversupplied**
 - IE and OC showed occupancy at about 84%
 - LA County at slightly less than 88%
 - Highest occupancy levels during 2000 - 2009 at 92% to 94%
 - More years below 90% than above
- ▶ **From 2000 – 2009, developers added to the supply inventory in each county.**
 - Lowest nine-year increase was LA County at 4%
 - Highest was 34% in IE
- ▶ **2009 rents vary widely across the region**
 - Low of \$22 psf per year in IE
 - High of \$31 psf per year in LA
- ▶ **In general, office rents in 2009 are lower than rents in 2000, adjusted for inflation**
 - LA's current rents are slightly lower; OC 16% less
 - Only the IE shows higher rents in 2009 than 2000, about 13%



INDUSTRIAL TRENDS, 2000 - 2009

BETTER OCCUPANCIES; WORSE ON ADJUSTED RENTS

- ▶ **2009 occupancy rates across all five counties differed dramatically**
 - IE at 84%, highly overbuilt market
 - LA County was the high at 95%
 - OC and Ventura at 93% to 94%
- ▶ **From 2000 – 2009, IE was the location for most industrial space added in five-county region**
 - IE's nine-year inventory expanded by 75%
 - Next was Ventura County at 17%
- ▶ **2009 rents vary widely across the region**
 - Low of \$5 psf per year in IE
 - High of \$8 psf per year in OC
- ▶ **All industrial rents in 2009 are lower than rents in 2000, adjusted for inflation**
 - Ventura County rents at about 20% below 2000 adjusted rents
 - IE at 15% below
 - OC current rents performed best, 5% below 2000 rents



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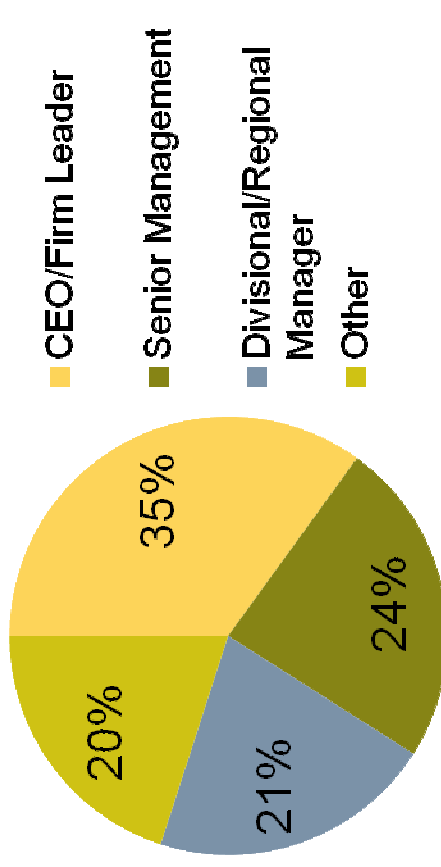


RCLCO Sentiment Surveys

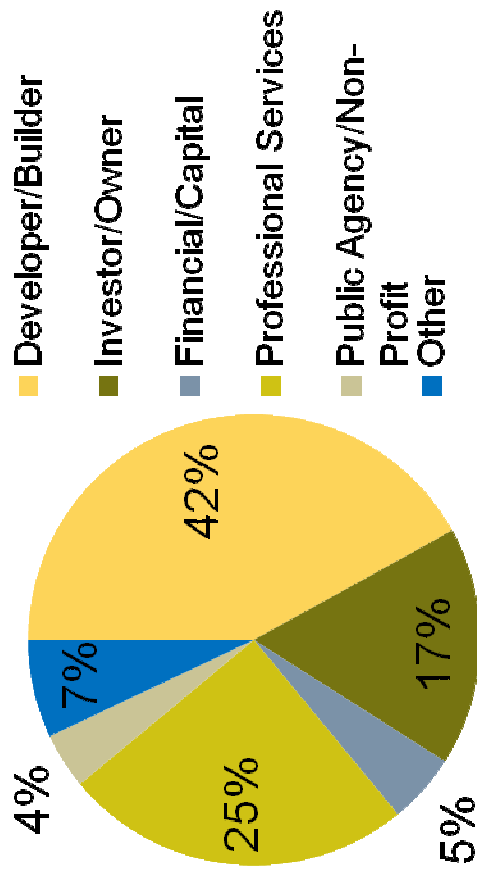
RCLCO MARKET SENTIMENT SURVEY FALL 2009 (Total Responses = 581)

Real estate executives believe the worst may be behind us, but fragile economic conditions, weak credit markets, and looming commercial defaults are conspiring to push the real estate recovery well beyond 18 months in most markets.

Individual Respondent Roles



Firm/Organization Roles



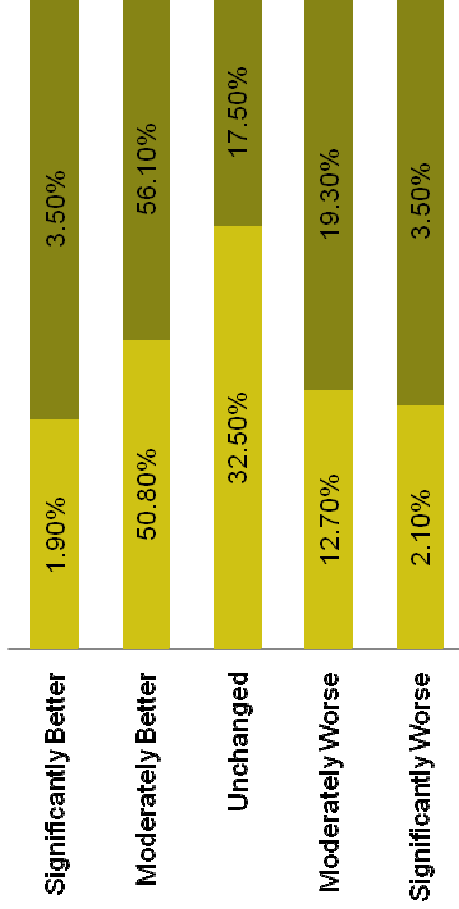
SOURCE: RCLCO Market Sentiment Survey – September 2009

LA REGION MORE PESSIMISTIC ABOUT OUTLOOK FOR RECOVERY THAN OTHER REGIONS

How do you expect U.S. and regional/local economic conditions to be in six months?

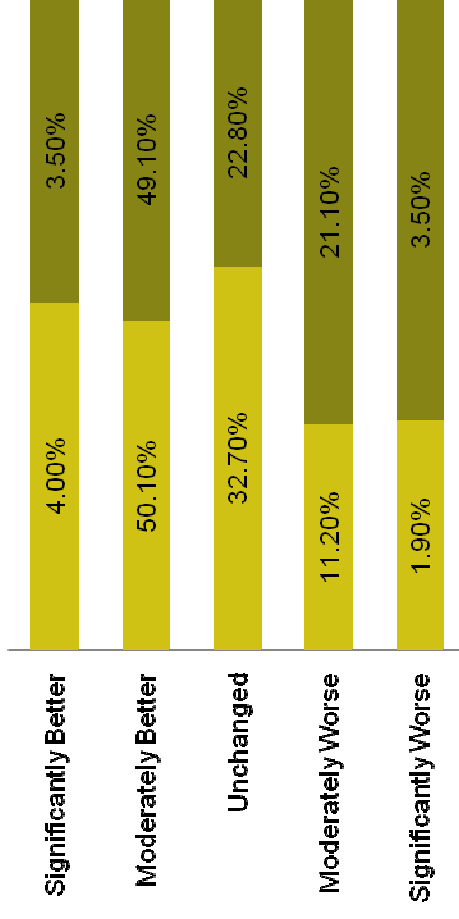
National Economy

■ Nation ■ LA



Local Economy

■ Nation ■ LA



REAL ESTATE PROFESSIONALS WARY AS SERIOUS CONCERNS REMAIN

"I am deeply concerned that there is a significant amount of "bad" commercial real estate loans (both traditional financing and CMBS) that have to be dealt with (i.e., losses taken) before we can clear the decks and move on.... I foresee huge amounts of bad commercial real estate loan defaults. This will create a great deal of pain to those on the borrowing and lending sides, but great opportunity for buyers with cash."

"There will be a second wave of mortgage defaults forcing residential prices downward. Commercial property values will drop throughout 2010. All of this will put more pressure on banking system. No decent recovery until 2011, if then."

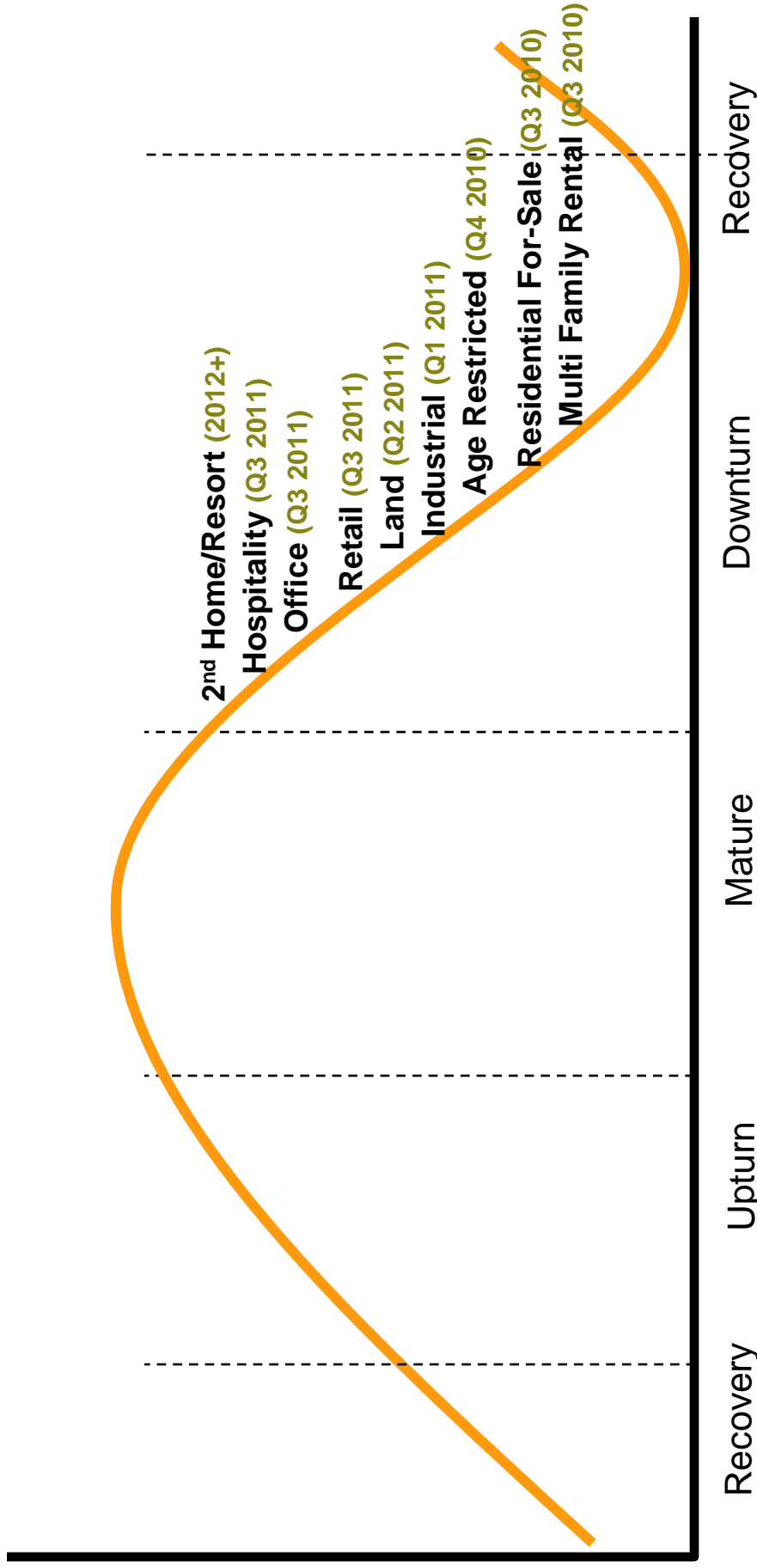
"People seem to think a correction is something we all deserve. I think there are a lot of economic sins yet to be atoned for. Where is it written that after so much hanky panky -- everything will turn out just fine in the end. That happens on television and in bedtime stories, maybe not in the long term US economy. Stay tuned."

SOURCE: RCLCO Market Sentiment Survey September 2009

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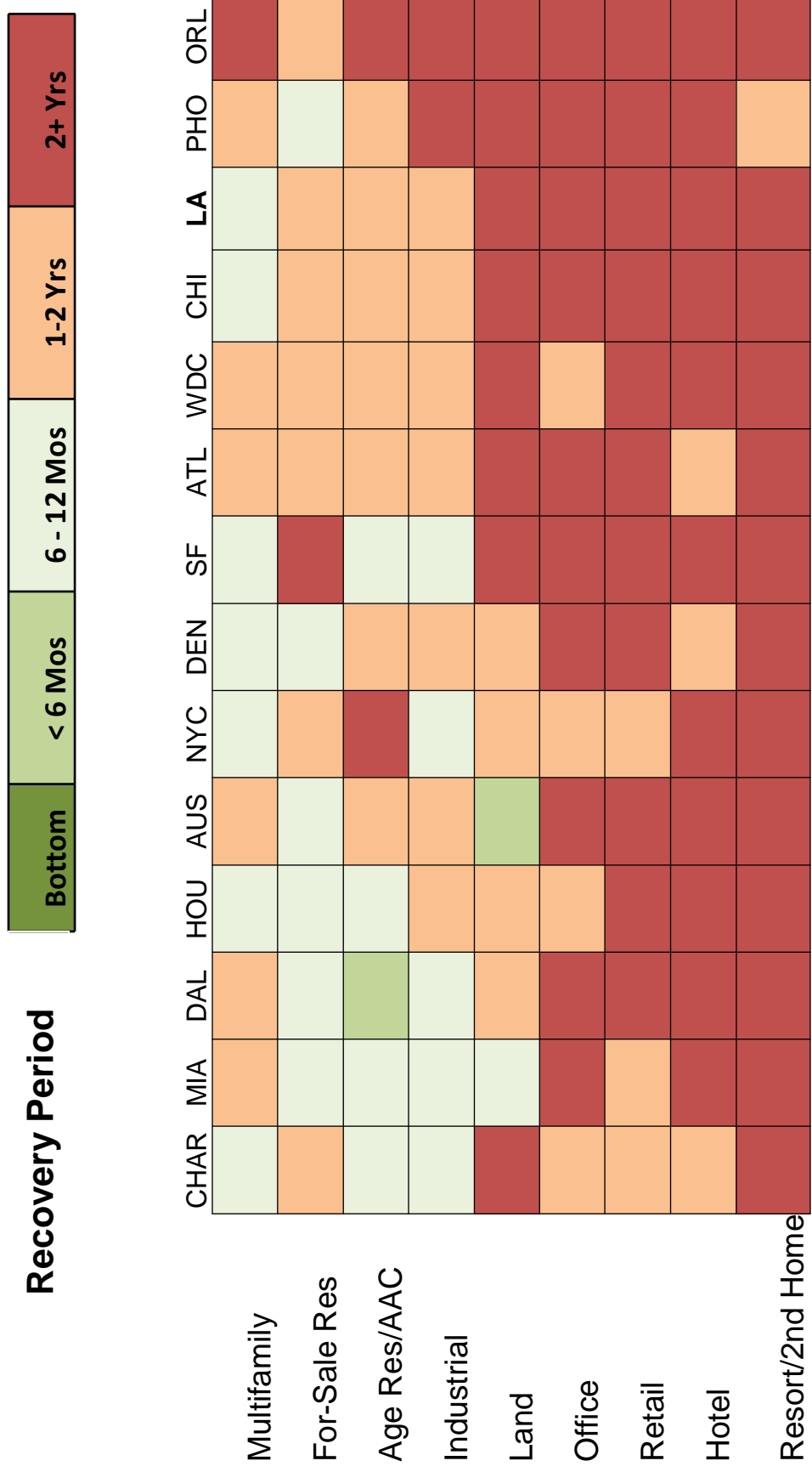
REAL ESTATE RECOVERY NOT EXPECTED FOR ANOTHER 12-18 MONTHS

Median Date Predicted for Recovery of Sector



SOURCE: RCLCO Market Sentiment Survey September 2009

RECOVERY IS LIKELY TO BE DISPARATE GEOGRAPHICALLY AND BY PRODUCT TYPE



REAL ESTATE PROFESSIONALS SEE IMPROVEMENT IN RESIDENTIAL MARKETS

"In our region, I think entry level housing is already recovering. High end stuff is just not moving. You can't buy up if you can't sell. You can't sell if the short sale/foreclosure market is not depleted. I think the higher end market is stuck and people aren't moving and are unwilling to lower prices unless they are forced to move due to job or other reasons."

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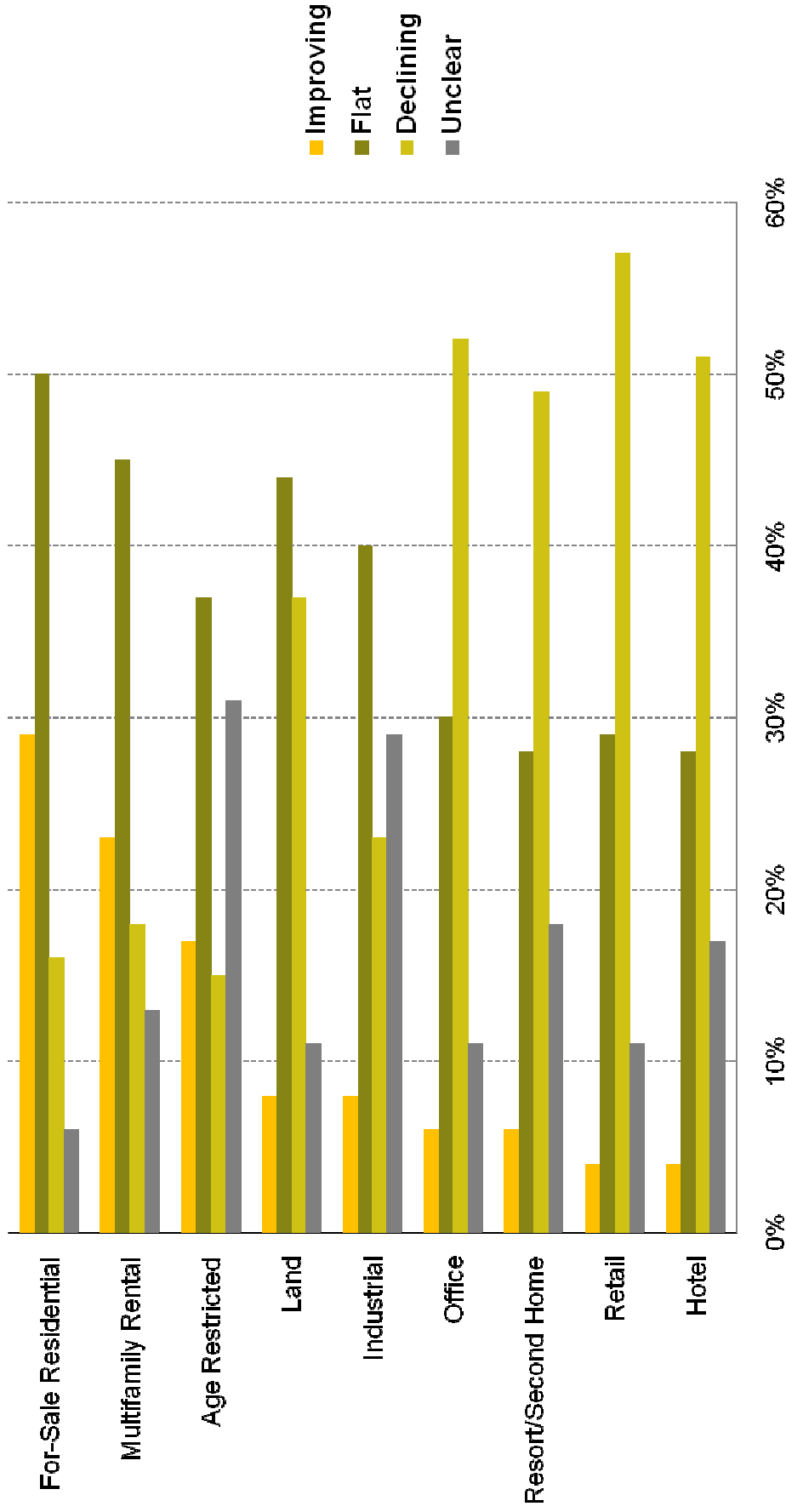
"Residential sales have strengthened, the office market continues to decline. Retail is stable to slightly growing. Very few new projects are even in the pipeline. There will come a time in this market when the hunt/fight for building lots will become brutal, since no one is increasing inventory but that is some time off."

SOURCE: RCLCO Market Sentiment Survey September 2009

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AVAILABILITY OF CAPITAL TO REMAIN LIMITED RESIDENTIAL PROJECTS HAVE BEST PROSPECTS

Which of the following statements best reflects your sentiments concerning the availability of capital for real estate over the next six months?



SOURCE: RCLCO Market Sentiment Survey September 2009

LACK OF CAPITAL A CONSENSUS CONCERN A MAJOR HINDRANCE TO RECOVERY

- *“Access to capital has been and appears to be difficult. Lending is constrained for even the best of firms.”*
- *“The most significant issue today is the lack of investment capital and the unavailability of ADC loans.”*
- *“There will be no recovery without a functioning debt market.”*
- *“Annual bank appraisals and ill-informed appraisers are severely impacting free market reaction to product.”*
- *“There is little hope for growth until credit returns in a significant way. We are worried that will not happen until the job market improves and banks are more confident to lend. We are hopeful for some incremental improvement in residential single family next year, and are concerned that the multifamily segment will sink even further due to credit market inactivity.”*
- *“You should add a nonexistant choice on the capital questions”*

SOURCE: RCLCO Market Sentiment Survey September 2009

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MOST REAL ESTATE FIRMS PLAYING DEFENSE BUT RECOGNIZE OPPORTUNITY IN TODAY'S MARKET

Minimizing expenses is key. Over the next 12 months:

- 84% of surveyed firms plan to reduce overhead expenses
- 47% plan to reduce staff
- 74% plan to delay or defer capital investments

60% plan to be opportunistic buyers of real estate assets/financial instruments.

Other popular strategies include:

- Forming alliances/partnerships
- Acquiring distressed assets, including competing firms
- Offering lower priced product to satisfy changing demand
- Pursuing more public sector work

“Subject to the financial pressures brought to bear, we are in a wait and see posture. With continued declines in the market a hold position looks like progress. Those that survive this downturn with some or most assets in place will stand to do very well in 2-5 years.”

“Opportunistic residential land buys based on 3 yr. holds. Explore multifamily area as it declines in the next 12 months. Watch economy, local job generation, state and federal budgets, and bank failures with implication on values.”

“We’ll do anything for a fee.”

SOURCE: RCLCO Market Sentiment Survey September 2009

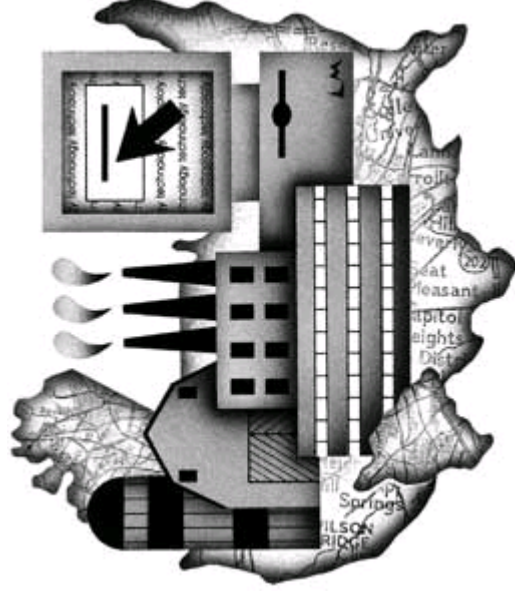
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Economic Forecasts

“GREAT RECESSION IS OVER,” PER NABE SLOW GROWTH FORESEEN

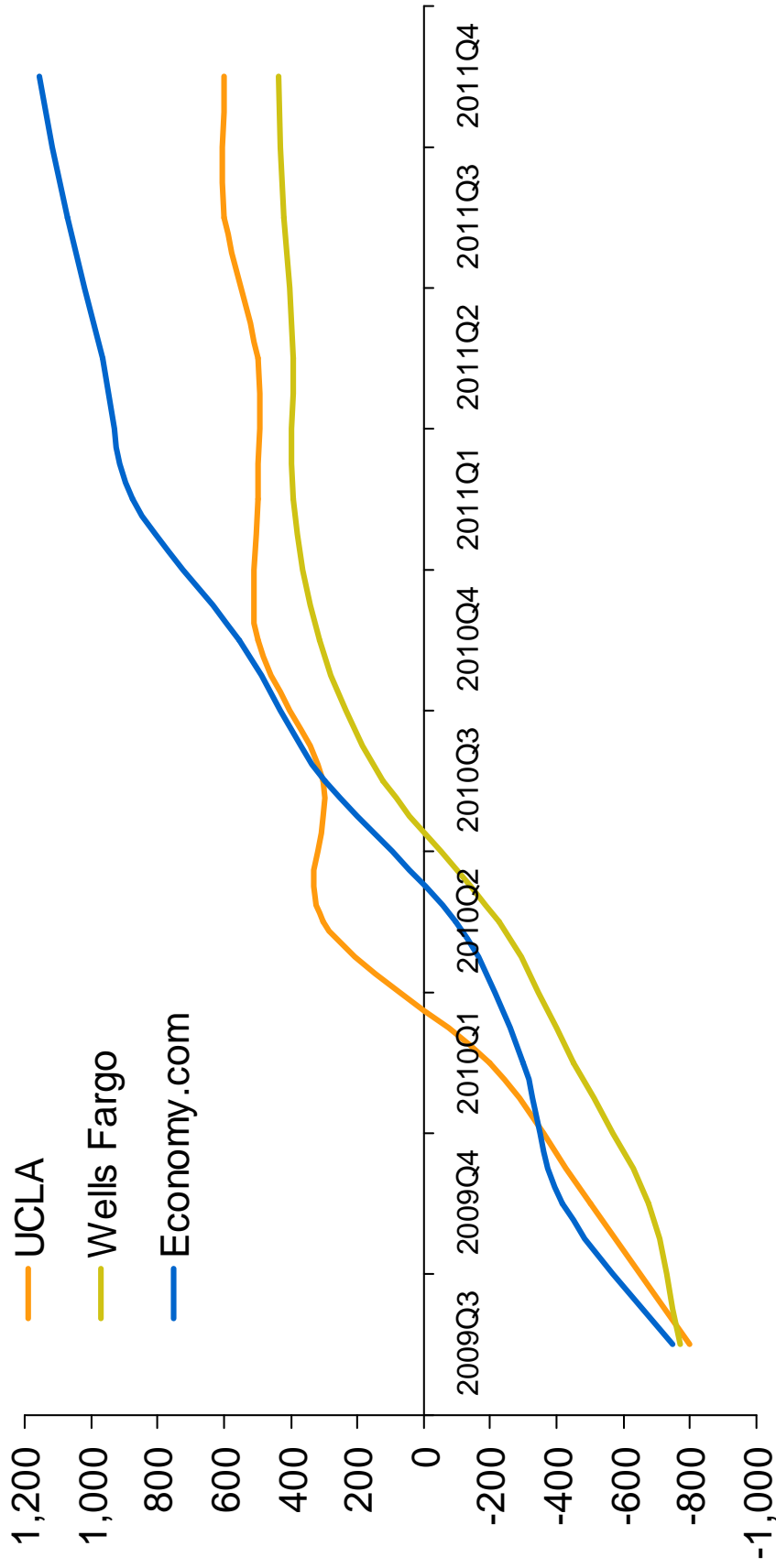
- ▶ Current recession started in December 2007; longest and deepest since 1930s
- ▶ Triggered by collapse of U.S. housing market and ensuing global credit crisis
- ▶ Much of anticipated recovery driven by businesses rebuilding their inventories
- ▶ Three-year housing market downturn coming to an end; housing prices expected to bottom this year
- ▶ GDP growth over second half of 2009 at 2.9%; for 2009 as a whole GDP expected to contract 2.5%. GDP growth for 2010 projected at 2.6%
- ▶ Unemployment rate to rise to 10% in Q1 2010, declining slightly to 9.5% by year-end 2010
- ▶ Jobs lost during recession not recovered until 2012 or beyond



Source: Summary NABE Survey, October 12, 2009

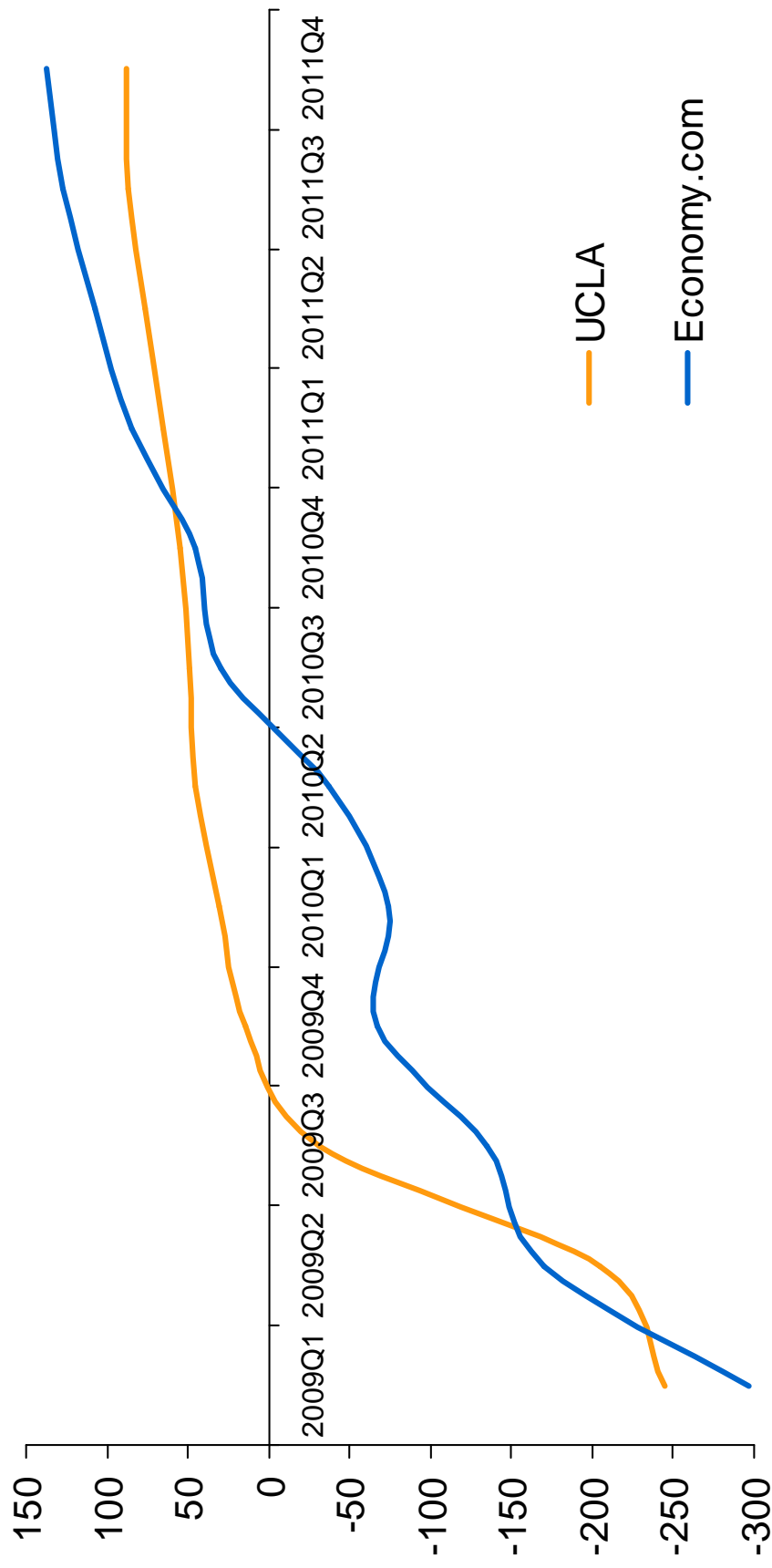
U.S. JOB GROWTH TURNAROUND IN 2010 TOTAL JOBS PEAKED IN 2007; REPLACEMENT BY 2013

Employment Growth By Quarter (in 000s), 2009 Third Quarter - 2011



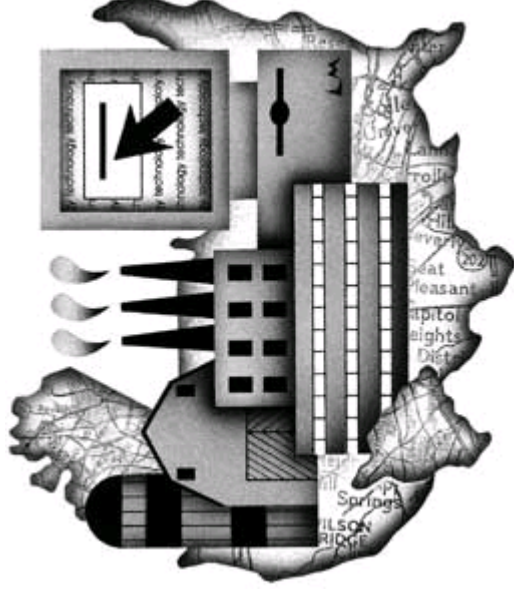
CALIFORNIA JOB GROWTH TURNAROUND IN 2010 TOTAL JOBS PEAKED IN 2007; REPLACEMENT BY 2012/13

Employment Growth By Quarter (in 000s), 2009 - 2011



“CALIFORNIA HOUSE PRICES TO RISE IN 2010” CALIF ASSOC OF REALTORS EXPECT 3.3% GAIN

- ▶ Slight gain of 3.3% after three down years
- ▶ For 2010, median expected price for single-family detached housing at \$280,000 in the state
- ▶ Last year, this same organization had expected 2009 median home price at \$358,000. 2009 median estimate at \$271,000 reflect impact of foreclosures
- ▶ California house prices fell 22% this year on top of 2008's 38% decline
- ▶ Three-fourths of homes now selling in the state at less than \$500,000
- ▶ Huge rebound in lower-end properties; reduction in market share at high end – dragged down the median



Source: Summary of California Association of Realtors 2010 Forecast, Bloomberg.com, October 7, 2009

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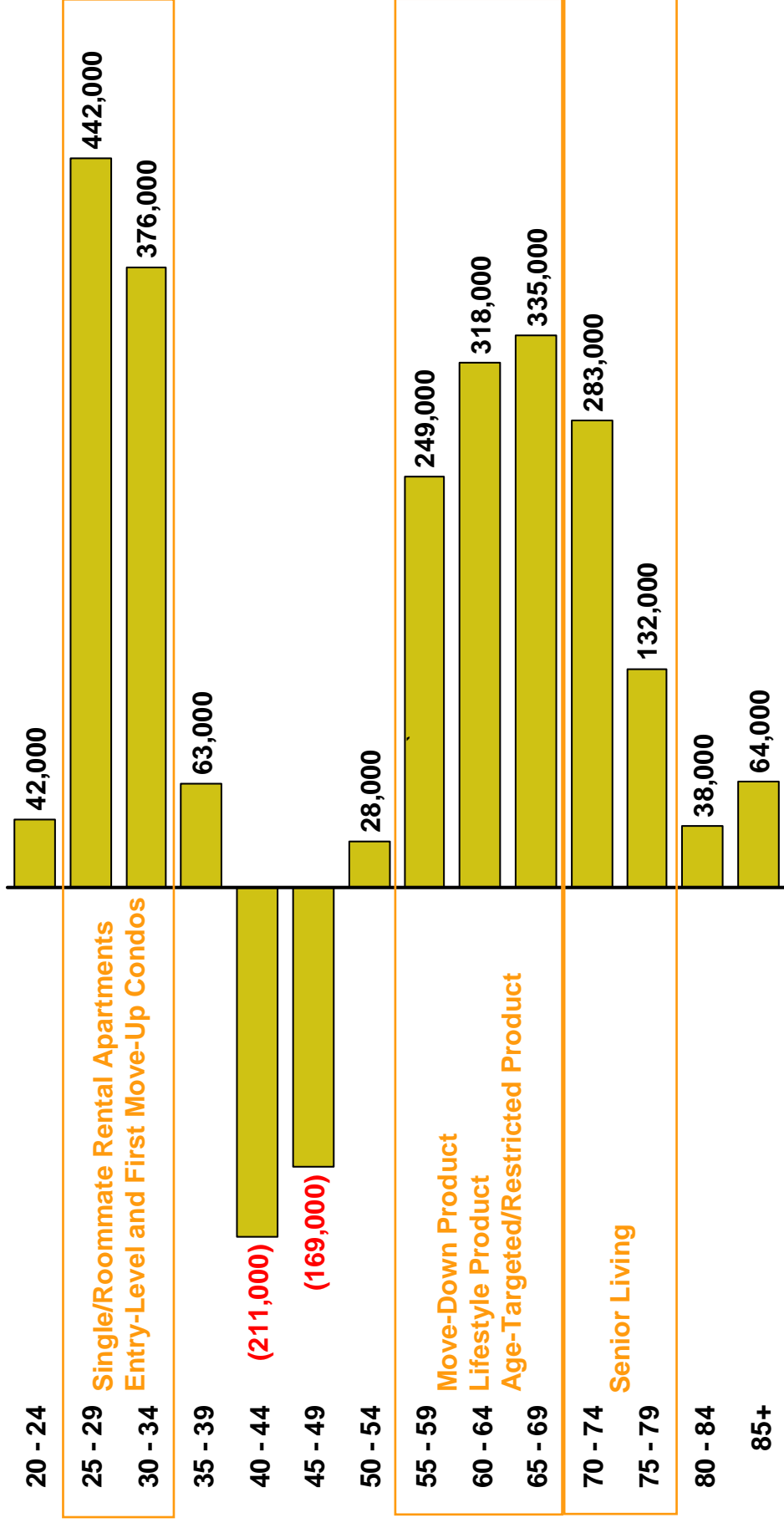




Key Considerations

FUELING RECOVERY – SOCIAL POP EXPANSION CURRENT POP. OF 19 MILLION TO GROW BY 2+ MILLION

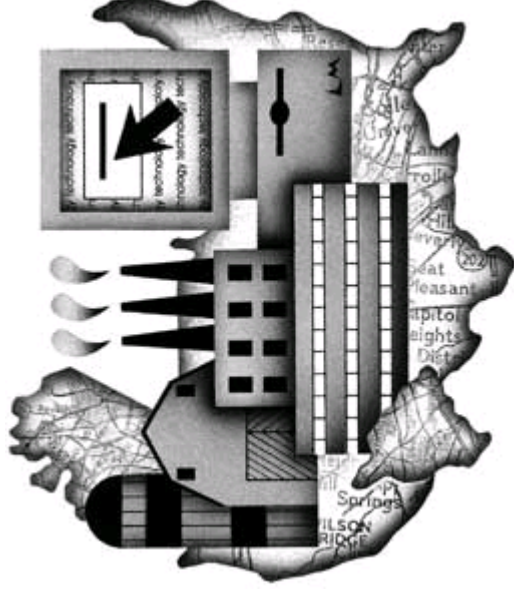
Projected Total Population Growth Rate by Age Southern California, 2010-2020



SOURCE: California Department of Finance; RCLCO

EMERGING RECOVERY – INVESTMENT UPSIDES CONSTRAINED SUPPLY – RISING OCCUPANCIES & RENTS

- ▶ **Commercial real estate looks grim in 2010**
 - Oversupplied markets
 - Rising unemployment
 - Declining NOI
- ▶ **Emerging recovery, plus SoCal’s favorable demographics, underpin future acquisitions of distressed assets.**
 - No new construction coupled with eventual employment growth will improve occupancies.
 - Rising occupancies will push rents
- ▶ **Bottom of the recession is either here now or approaching. *Time to plan for investment, focusing on locations and products that will respond to the coming recovery.***



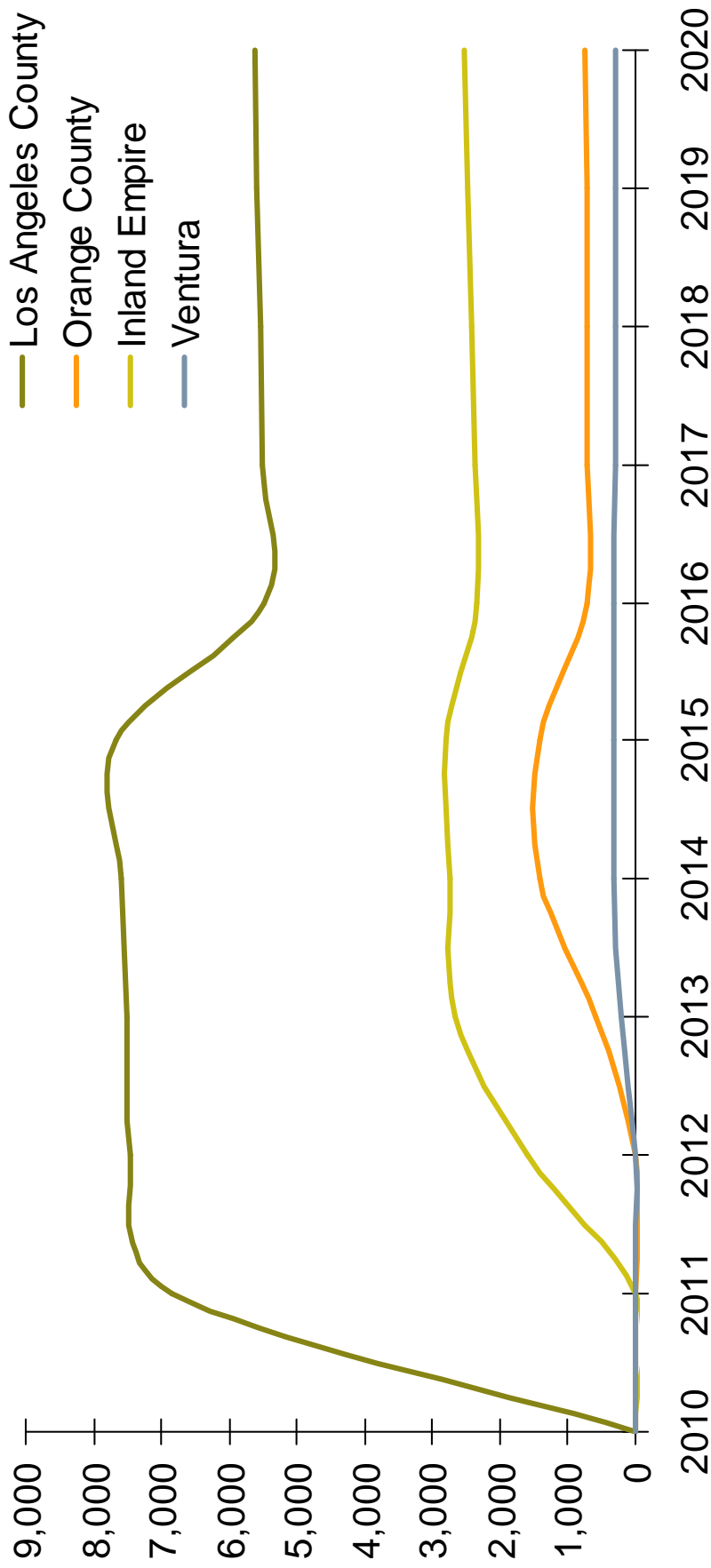


Real Estate Product Forecast – Emerging Demand for New Development

NEW APARTMENTS - IN PLACE BEGINNING 2011/12

CONSTANT 5% MARKET VACANCY

In Units
Southern California, 2010-2020

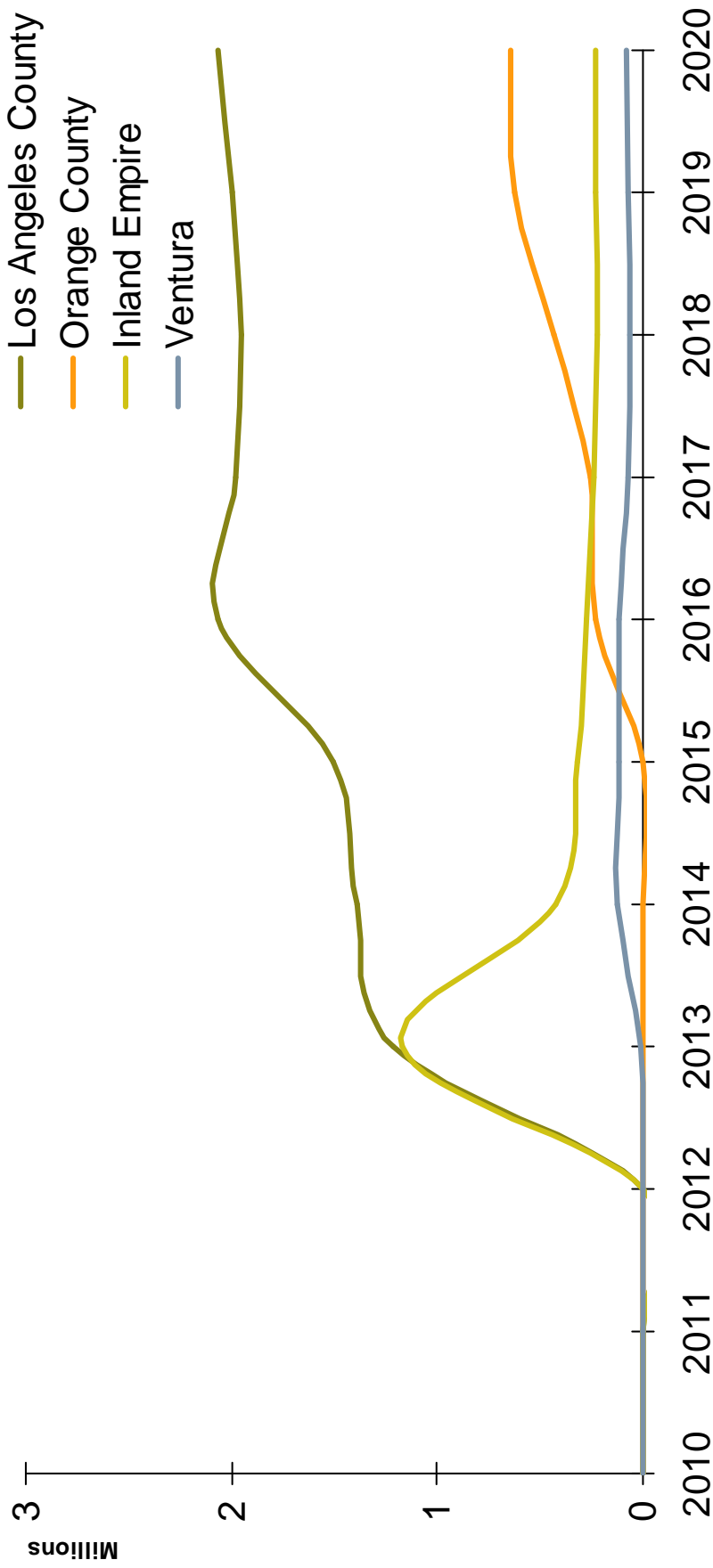


SOURCE: Marcus & Millichap (builds on projected 2009 vacancy) ; modified SCAG population projections

NEW OFFICE SPACE - IN PLACE BEGINNING 2013

CONSTANT 7% MARKET VACANCY

In Millions of SF
Southern California, 2010-2020

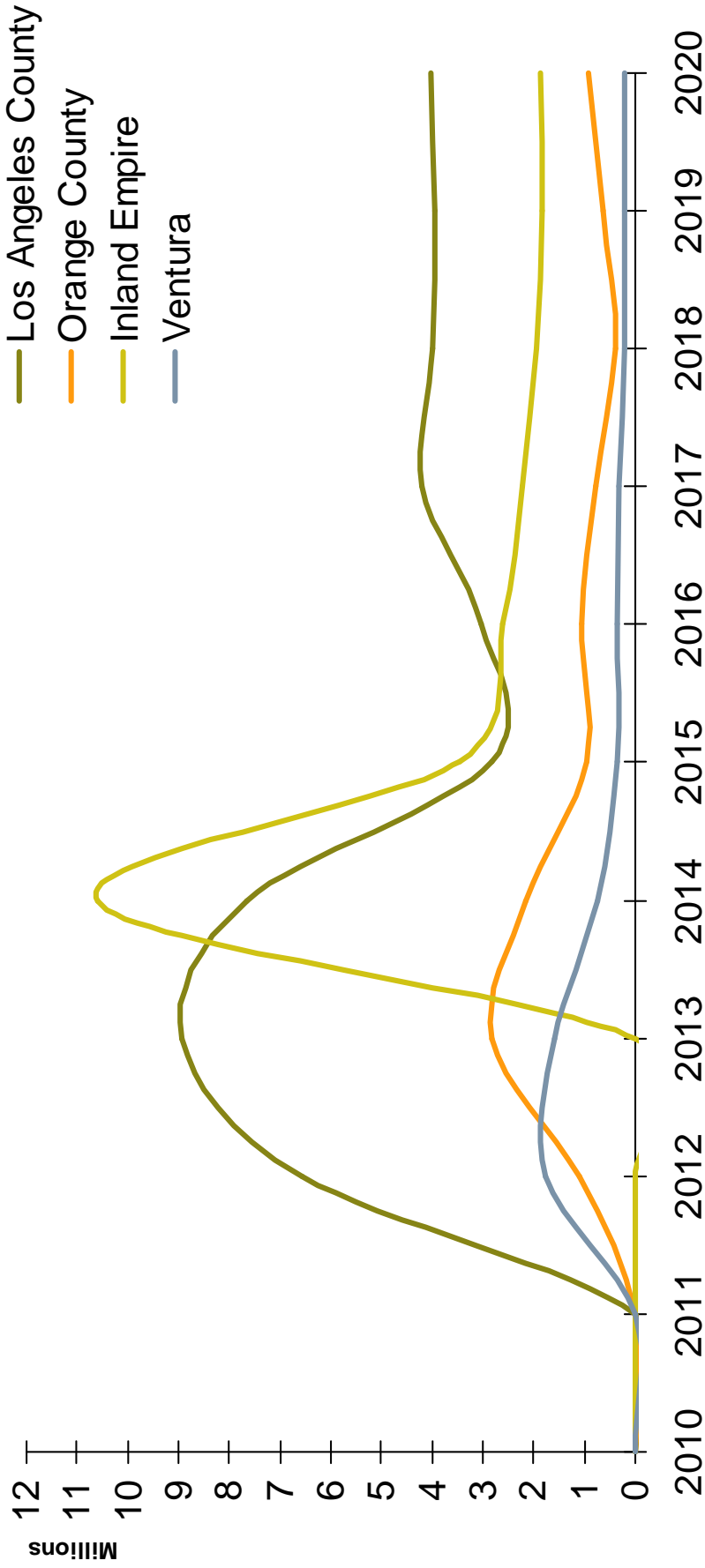


SOURCE: Marcus & Millichap (builds on projected 2009 vacancy) ; modified SCAG population projections

NEW INDUSTRIAL SPACE - IN PLACE IN 2012

CONSTANT 5% MARKET VACANCY

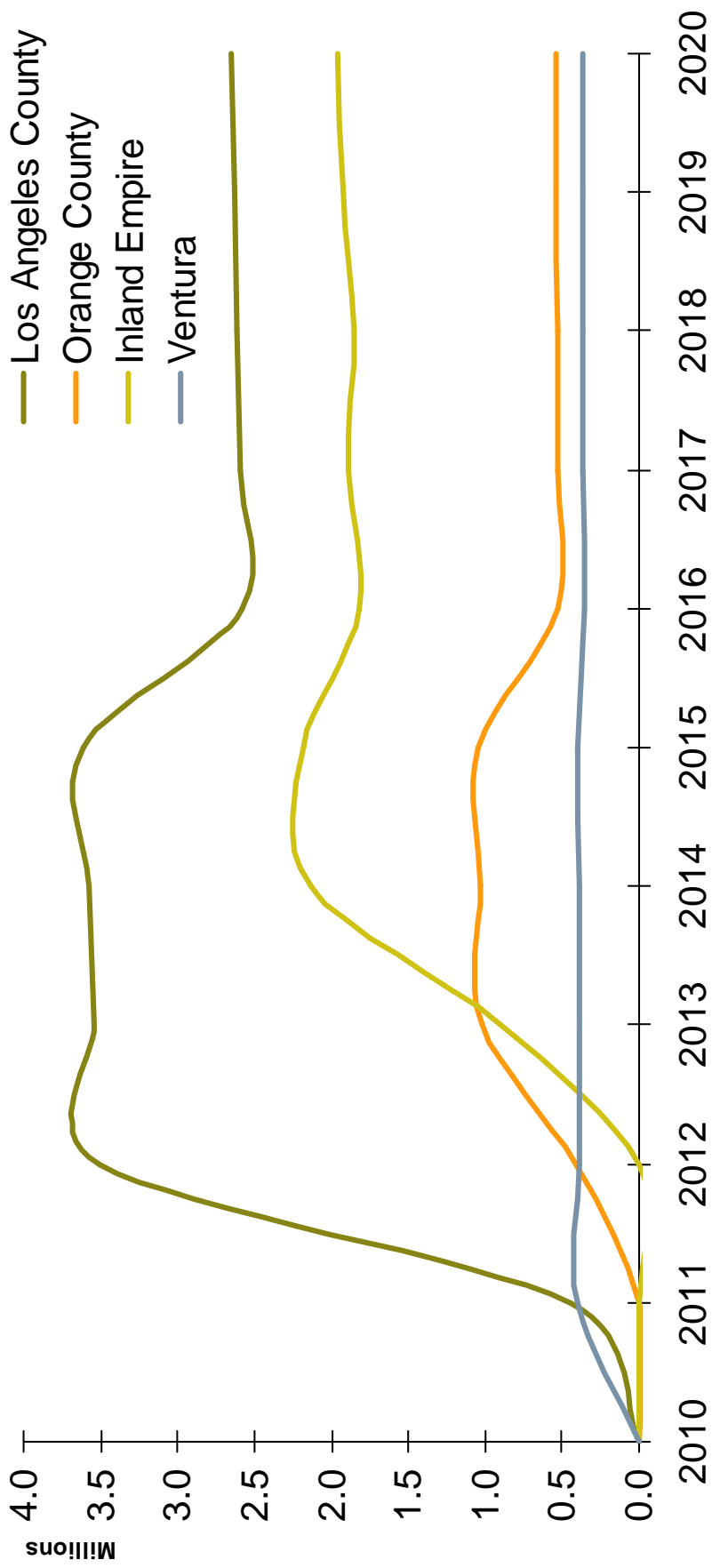
In Millions of SF
Southern California, 2010-2020



SOURCE: Marcus & Millichap (builds on projected 2009 vacancy) ; modified SCAG population projections

NEW RETAIL SPACE - IN PLACE IN 2012 CONSTANT 5% MARKET VACANCY

In Millions of SF
Southern California, 2010-2020



SOURCE: Marcus & Millichap (builds on projected 2009 vacancy) ; modified SCAG population projections



Final Thoughts

CAPITALIZING ON THE EMERGING TRENDS A SLOW RECOVERY BUT A RECOVERY NONETHELESS

**“This time, like all times, is a very good one if we
know what to do with it.”**

- Ralph Waldo Emerson

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“We simply attempt to be fearful when others are greedy and to be greedy only when others are fearful.”

- Warren Buffett

FINAL THOUGHTS -- THE EMERGING TRENDS A SLOW RECOVERY BUT A RECOVERY NONETHELESS

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“I look to the future because that's where I'm going to spend the rest of my life.”

- George Burns

RCLCO CONTACT INFORMATION

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RCLCO: HOW WE ADD VALUE

40+ Years Industry- Leading Firm

- 40+ years experience across all product types and geographies
- Pioneered methodologies in market analysis, consumer research, and financial analysis
- End-to-End solutions

Expertise & In-Depth Knowledge

- Multidisciplinary team of professionals with diverse backgrounds
- Deep bench of specialists by sector, geography, practice area, and client type
- Experts in land and residential development; commercial, multifaceted projects

Advisory Approach

- Independent insight, experience, and fact-based recommendations
- Forward looking strategic advice to minimize risk and maximize opportunities
- Fusion of consulting and “practice”

Scalability

- 500+ engagements per year
- Offices in Washington, DC, Los Angeles, Orlando, Atlanta and Austin
- Systematic approach and strategic alliances to execute large engagements

Specific Services

- Strategic Planning
- Market & Economic Research
- Project Segmentation, Positioning
- Fiscal & Economic Impact Analysis
- Valuation Services
- Acquisition & Disposition Strategies
- Workouts & Restructuring
- Transaction, Structuring & Investment Analysis
- Development Services



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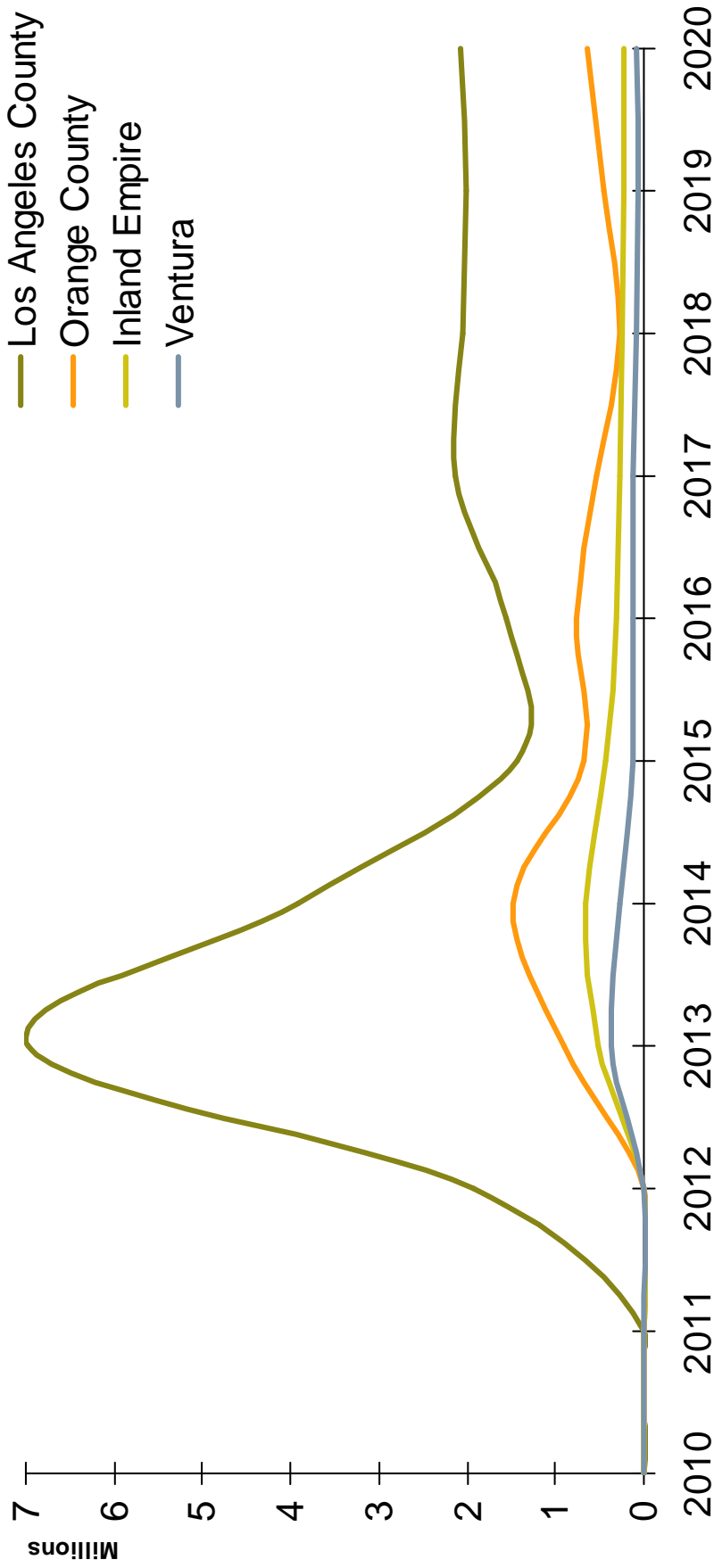
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NEW OFFICE SPACE - IN PLACE IN 2012 AND 2013 CONSTANT 10% MARKET VACANCY

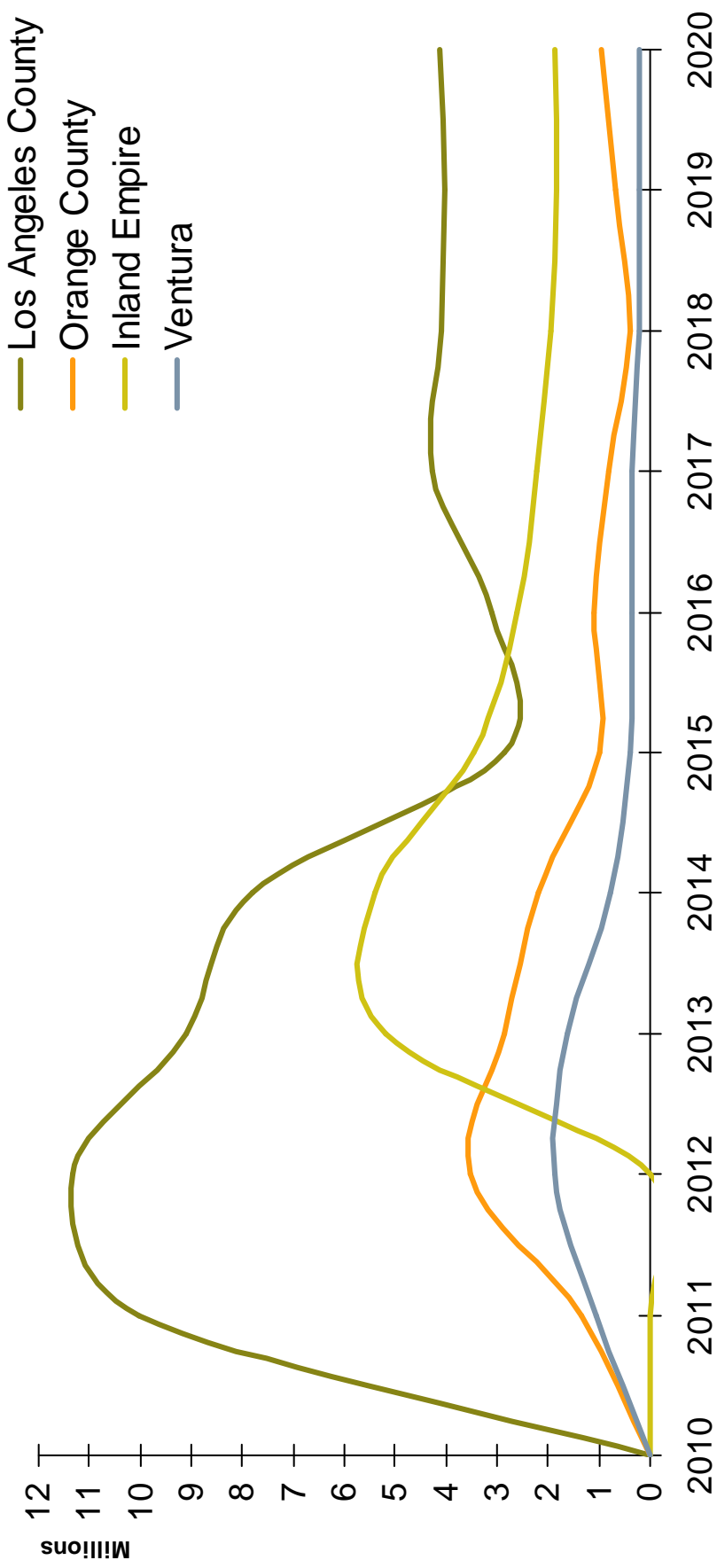
In Millions of SF
Southern California, 2010-2020



SOURCE: Marcus & Millichap (builds on projected 2009 vacancy) ; modified SCAG population projections

NEW INDUSTRIAL SPACE - IN PLACE IN 2011 CONSTANT 7% MARKET VACANCY

In Millions of SF
Southern California, 2010-2020



SOURCE: Marcus & Millichap (builds on projected 2009 vacancy) ; modified SCAG population projections