

Commercial Real Estate
Capital Markets Update
First Quarter 2008

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Sources:

Federal Reserve Bank
Globe Street
National Council of Real Estate Investment Fiduciaries
Real Capital Analytics
U.S. Department of Commerce
U.S. Department of Labor

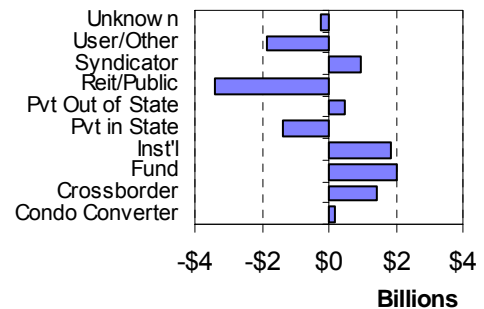


Overview

The good news is that the worst of the credit market turmoil appears to be past. Investors have been reassured by the bold and unprecedented actions of the Federal Reserve, which included the deliverance of Bear Stearns into the arms of JP Morgan, lending to investment banks as well as commercial banks while encouraging them to boost capital reserves to maintain liquidity, and reducing the federal funds rate from 5.25 percent last September to 2.0 percent at present. The Fed has come under a lot of criticism because its actions weakened the dollar, encouraged speculation in oil and commodities, stoked gas prices and threatened to ignite inflation. But it appears that the Fed also averted a collapse of the credit markets that could have triggered a full-blown credit crisis and a deep recession. Chairman Bernanke, a student of the Great Depression, most likely was the right person for his job at the right time.

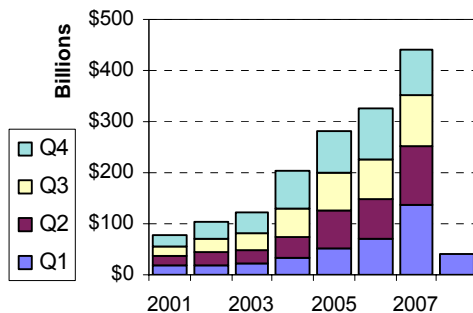
percent of the large banks surveyed tightened standards for commercial real estate loans during the first quarter. Interest-only periods are rare, debt coverage ratios are up, loan-to-value ratios are down, and recourse has increased.

CRE Buyers & Sellers by Net \$ 2008-Q1



Source: Real Capital Analytics, Grubb & Ellis

Commercial Real Estate Investment



Source: Real Capital Analytics, Grubb & Ellis

The bad news is that the credit markets remain in disarray. Securitized lending is incapacitated, and that includes commercial mortgage backed securities, which account for about one-quarter of all commercial real estate debt outstanding and about one-third of the debt issued last year. Portfolio lenders such as banks, insurance companies and pension funds that hold the loans on their books remain active but are far more cautious. The latest Fed survey of senior loan officers indicates that 79

With leverage playing a key role in commercial real estate values, it's no wonder that the dollar volume of investment transactions is off 71 percent in the first quarter compared with the first quarter of 2007. Average capitalization rates have drifted a bit higher, but not as much as might be expected because there are few distressed property sales as yet. That could change when recently issued floating rate loans come up for refinancing. The owners will not be able to get terms nearly as generous as were available a year or two ago, and they will need to come up with more equity or figure out some other course of action with their lenders. In the worst case, that could include defaults and foreclosures, though the level of distress won't be anywhere near the troubles plaguing residential real estate. A deterioration of leasing market fundamentals could aggravate delinquencies by reducing net operating incomes, dealing a one-two punch to owners who need to refinance.

But there is a silver lining to the economic downturn (not defined as a recession just yet) ignited by the credit market problems: The labor market has been holding up remarkably well compared to the last six

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Table 1: Key Investment Market Indicators by Property Type

	Apartment	Industrial	Office	Retail
Capitalization Rate¹				
2007-Q1	6.07%	6.92%	6.60%	6.57%
2007-Q4	6.23%	7.37%	6.62%	6.74%
2008-Q1	6.18%	7.05%	6.94%	6.88%
Direction	▲	▲	▲	▲
Total Sales (billions)¹				
2007-Q1	\$20.4	\$11.2	\$79.4	\$26.5
2007-Q4	\$36.9	\$9.8	\$28.8	\$11.0
2008-Q1	\$12.0	\$7.1	\$14.4	\$6.5
Direction	▼	▼	▼	▼
Investment Return²				
2007-Q1	2.91%	3.47%	4.14%	2.97%
2007-Q4	3.26%	5.14%	5.93%	3.42%
2008-Q1	2.93%	3.19%	4.76%	2.41%
Direction	▼	▼	▼	▼
Vacancy Rate^{3,4}				
2007-Q1	6.0%	7.7%	13.3%	7.1%
2007-Q4	5.7%	7.7%	13.0%	7.5%
2008-Q1	5.9%	7.9%	13.5%	7.7%
Direction	◀▶	▲	▲	▲
Asking Rent^{3,4,5}				
2007-Q1	\$991	\$4.55	\$33.28	\$19.11
2007-Q4	\$1,026	\$4.69	\$36.38	\$19.49
2008-Q1	\$1,035	\$4.67	\$35.63	\$19.57
Direction:	◀▶	◀▶	▼	▼

1. Source: Real Capital Analytics; transactions above \$5M
2. Source: National Council of Real Estate Investment Fiduciaries (NCREIF)
3. Source: Grubb & Ellis (office and industrial data); Reis (retail and apartment data)
4. Retail data is for neighborhood and community centers
5. Office rent is for Class A space, full service
Industrial rent is for warehouse/distribution space, triple net
Retail rent is for neighborhood and community centers, triple net

recessions. Since peaking last December, payroll employment has fallen 0.2 percent through the first four months of 2008, half the rate of decline at the onset of the prior two recessions and less than half the decline at the onset of the four recessions before that. The reason behind the shallow job losses is

that employers were cautious adding jobs during the 2001-2007 expansion cycle, and now they are being cautious in eliminating them. The inventory of office space on the sublease market corroborates this trend. Since bottoming in the second quarter of 2007, the supply of sublease space across the U.S.



has increased 12 percent. During the comparable three-quarter period at the onset of the 2001 recession, sublease space more than doubled. There are other reasons to expect that the downturn may be shallow. Global growth and the weak dollar are boosting exports, benefiting manufacturers. Corporate debt levels are low, suggesting that companies will feel less pressure to implement layoffs and delay capital spending plans. Finally, the \$112 billion economic-stimulus package will provide one-time payments to more than 131 million households, though much of that may go for food and gas.

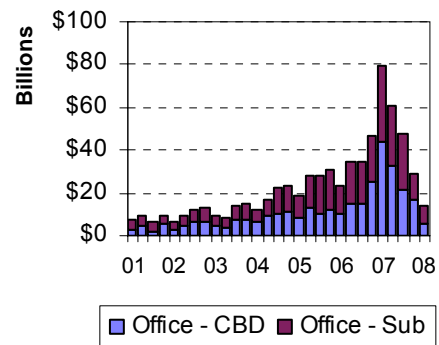
Expect leasing market fundamentals such as vacancy and rental rates to deteriorate modestly during the remainder of 2008 for office, industrial, retail and hospitality properties. For apartments, the increase in the renter pool resulting from rising residential foreclosures will be offset by an increase in shadow supply (unsold condos and foreclosed houses being offered for rent) and by the softening labor market, which will push some of this summer's crop of graduates to find roommates or move in with relatives to conserve cash. Thanks to the labor market's slow motion downturn, leasing market fundamentals are likely to hold up better than they did during and after the 2001 recession. But the economic recovery, when it comes, could be equally shallow. Foreclosures will remain a problem into 2009, lenders will remain risk-averse, and there isn't much in the way of "animal spirits" to drive a recovery worthy of the name.

Office Market

Cap rates: 6.1 percent for CBD properties sold in the first quarter, unchanged from the year-ago quarter; and 7.1 percent for suburban properties, up 40 basis points from a year ago. *Direction: up, but not until more distressed properties come to market; stable in the meantime.* **Total sales:** \$14.4 billion in the first quarter, down 82 percent from the year-ago quarter, which was supercharged by the \$39 billion sale of Equity Office Properties to The Blackstone Group and the subsequent resale of many former EOP properties to third-party investors. *Direction: lower compared with year-ago sales. Buyers and sellers are at an impasse, the CMBS market remains frozen, and portfolio lenders are being cautious.* **Investment return:** 1.96 percent (unleveraged) in

the first quarter compared with 4.60 percent in the year-ago quarter for institutional grade properties tracked by the National Council of Real Estate Investment Fiduciaries (NCREIF). *Direction: down. Cap rates are poised to rise, and rental rates are poised to sink. But owners who are renewing leases signed three to five years ago should still be able to capture some nice gains.* **Vacancy rate:** 13.5 percent in the first quarter, up 20 basis points from the year-ago quarter. *Direction: up as the construction pipeline continues to deliver the 94 million square feet still under way just as tenants are turning more conservative.* **Class A average asking rental rates:** \$49.87 per square foot per year, full service, for available CBD space and \$28.45 for suburban space, up by 11.3 percent and 3.8 percent, respectively, from the year-ago quarter. *Direction: flat in 2008, though effective rates will fall as landlords amp up their concession packages to keep existing tenants and attract new ones.* **Greatest risk:** The economic downturn, shallow so far, could devolve into a deeper recession, taking the labor market and demand for office space with it.

Office Investment By Location



Source: Real Capital Analytics, Grubb & Ellis

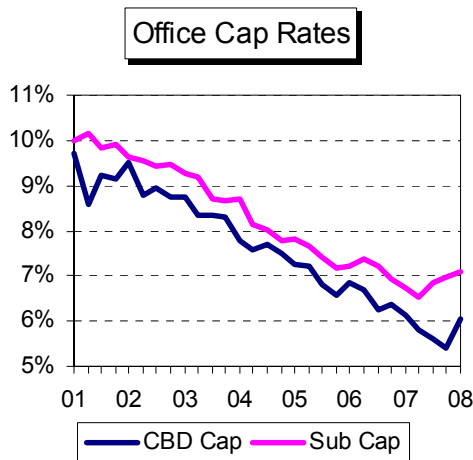
Major office transactions announced or concluded late in 2007 or early in 2008 include the following:

- Gramercy Capital Corp. completed its \$3.3-billion acquisition of American Financial Realty Trust, adding 29.2-million square feet to its portfolio. AFR is made up of buildings housing Bank of America, Wachovia and other large financial institutions.

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- Inland Real Estate Acquisitions Inc. purchased two portfolios from SunTrust Bank, paying \$736 million for a total of 433 triple-net lease properties comprising 2.3 million square feet. The majority of the assets are retail bank facilities located in the Southeast that will be leased by SunTrust.
- In New York City, Ashkenazy Acquisition Corp. and The Carlyle Group acquired 650 Madison Avenue, a 27-story, 600,000-square-foot trophy tower, from Hiro Real Estate Co. for \$680 million. SL Green Realty Corp. sold 1250 Broadway, a 39-story, 670,000-square-foot building, to Murray Hill Properties for \$310 million.
- Vico Capital is the new owner of 2099 Pennsylvania Ave. in Washington, D.C. Vico paid Wealth Capital Investments \$172.5 million for the 206,000-square-foot building. The \$837 per square foot price set a new record in the market.



Source: Real Capital Analytics, Grubb & Ellis

- In Chicago, Apollo Real Estate Advisors sold the three-building, 600,000-square-foot Citicorp Plaza to Parkway Properties Inc. for \$100 million, while a subsidiary of Hines paid \$540 million for the 51-story UBS Tower at 1 N. Wacker Dr. The 1.4-million-square-foot UBS asset was acquired from a German investment fund managed by Rreef.
- In Phoenix, Hines closed on the 966,000-square-foot One and Two Renaissance Square

for \$270.9 million. The seller of the CBD property, which is situated on a full city block, was the Pauls Corp. and GE Asset Management.

- Hines was also active in California, acquiring the 551,000-square-foot Raytheon and DirectTV complex in El Segundo from Newkirk Segair LP. The REIT paid \$120 million for the property, which consists of two 11-story Class A buildings and a 10-story parking garage.
- In another LA-area transaction, Douglas Emmett Inc. purchased 1.4 million square feet in six Class A buildings in West Los Angeles and the San Fernando Valley, paying Arden Realty Inc. \$610 million for the properties.
- In the medical office arena, Nationwide Health Properties closed on six of 15 properties that it plans to acquire from Pacific Medical Buildings this year for a combined total of \$460 million. This is part of a \$2-billion, seven-year deal between NHP and Pacific Medical for existing and planned properties. The existing space totals approximately 2 million square feet.
- Medical Properties Trust Inc. acquired seven assets in locations around the country for \$138 million from HCP Inc. The REIT expects to purchase another 14 properties from HCP later this year.
- In Florida, Grubb & Ellis Realty Investors LLC acquired the two-building Jacksonville Medical Plaza on behalf of tenant-in-common investors. The 11-acre property contains 132,000 square feet of medical offices.

Industrial Market

Cap rates: 7.0 percent for warehouse properties, up by 10 basis points from the year-ago quarter; and 7.1 percent for flex properties, also 10 basis points above the year-ago quarter. *Direction: up.* **Total sales:** \$7.1 billion in the first quarter, off by 36 percent from the year-ago period. *Direction: down versus year-ago comparisons; flat compared to the first quarter.* **Investment return:** 1.44 percent (unleveraged) in the first quarter for institutional grade properties compared with 3.22 percent in the year-ago quarter, according to NCREIF. *Direction: down.* **Vacancy rate:** 7.9 percent in the first quarter, up from 7.7 percent in the year-ago quarter. *Direction: higher as the construction pipeline continues to deliver new space during a period of*

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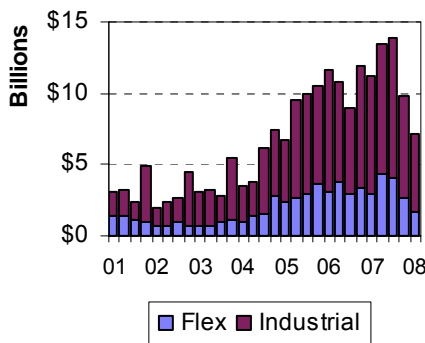


reduced tenant demand for space. **Asking rental rates:** \$4.67 per square foot per year, triple net, for warehouse/distribution space – up 2.7 percent from the year-ago quarter; and \$10.71 for R&D/flex space – up by 6.5 percent from the year-ago quarter. *Direction: stable in 2008, up one quarter and down the next with little change by year-end. However, landlords will offer more aggressive concessions packages to keep their properties leased up.* **Greatest risk:** Legislation discouraging the growth of international trade.

Major industrial transactions announced or concluded in the second quarter include the following:

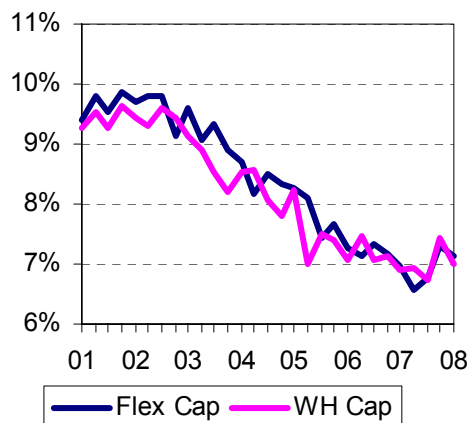
- Lighthouse Real Estate Ventures Inc. acquired 25 warehouse/flex assets in the Northeast from Baker Properties for \$209 million. The portfolio, which totals 2 million square feet, was part of a 1031 exchange.
- A joint venture between Wentworth Property Co. and the Utah State Retirement Investment Fund will pay more than \$150 million for 2.5 million square feet of distribution space in three Phoenix properties currently under development by Buzz Oates Group of Cos.
- In the largest transaction in Chicago's I-55 Corridor in the past decade, Panattoni Development Company and LaSalle Investment Management sold a four-building, 1.9-million-square-foot portfolio to Heitman American Real Estate Trust for more than \$100 million.
- KTR Capital Partners purchased two fully-leased distribution buildings totaling 1.1 million square feet in Carteret, N.J., for \$79.3 million.

Indust. Investment By Product



Source: Real Capital Analytics, Grubb & Ellis

Industrial Cap Rates



Source: Real Capital Analytics, Grubb & Ellis

Retail Market

Cap rates: 7.2 percent for strip centers in the first quarter, up by 60 basis points from the year-ago quarter; and 6.5 percent for malls and other centers, up by 10 basis points from the year-ago quarter. *Direction: up. Shopping centers are the least favored of the major property types.* **Total sales:** \$40.0 billion in the first quarter, off by 71 percent from the year-ago quarter. *Direction: down.* **Investment return:** 1.44 percent (unleveraged) in the first quarter compared with 3.14 percent in the year-ago quarter for institutional grade properties, according to NCREIF. *Direction: stable to slightly lower.* **Vacancy rate:** 7.7 percent for neighborhood and community centers in the first quarter, up from 7.1 percent in the year-ago quarter (source: REIS). *Direction: higher. The housing slump has been a drag on retail sales for the past two years. Retailers are closing stores and curtailing expansion plans.* **Asking rental rates:** \$19.57 for neighborhood and community centers in the first quarter, up by 2.4 percent from the year-ago quarter. *Direction: stable to slightly lower, although demand is holding up for the best locations.* **Greatest risk:** The labor market,

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which has shed a surprisingly small number of jobs this year, begins to lose them in greater chunks.

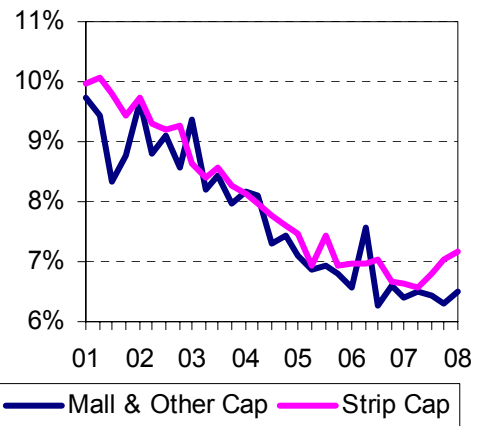
Major retail transactions announced or concluded in the second quarter include the following:

- Starmount Co. sold \$540.8 million worth of assets in North Carolina and Virginia to CBL & Associates Properties Inc. and Teachers' Retirement System of the State of Illinois. A joint venture between the buyers, valued at \$356.6 million, includes the Friendly Center and the Shops at Friendly Center in Greensboro and the Renaissance Center in Durham, as well as six office buildings. CBL also acquired a 100 percent interest in eight other community centers and a 12-asset office portfolio.
- Weingarten Realty Investors sold an 85 percent stake in a 2.1-million-square-foot portfolio, forming a joint venture with AEW Capital Management for the \$229-million recapitalization of 18 Texas assets. The properties, all of which are located in infill locations, include 13 grocery-anchored centers, one regional power center and four neighborhood centers.
- In the Washington, D.C., region, Principal Real Estate Investors and McCaffery Interests acquired six shopping centers and an office building from Fried Properties for \$126 million. The total portfolio is 529,000 square feet.

million. The seller, CRE Master JV Holdings, is an affiliate of UBS. The branch buildings are located mainly throughout the Northeast.

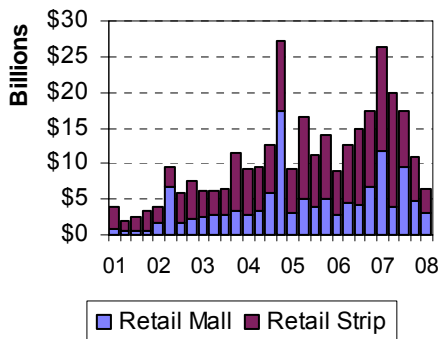
- Pacific Coast Capital Partners LLC and Dunhill Partners Inc. paid Kimco Realty Corp. more than \$100 million for Fountains on the Lake, an open-air power center near Houston. The new owners plan to expand the project, which currently consists of 589,000 square feet in 25 buildings.
- In suburban Cincinnati, Regency Centers acquired the Sycamore Plaza/Sycamore Crossing shopping center from RP Properties for \$93.3 million.

Retail Cap Rates



Source: Real Capital Analytics, Grubb & Ellis

Ret. Investment By Product



Source: Real Capital Analytics, Grubb & Ellis

- Net Lease Capital Advisors purchased 114 properties net leased to Citizens Bank for \$135

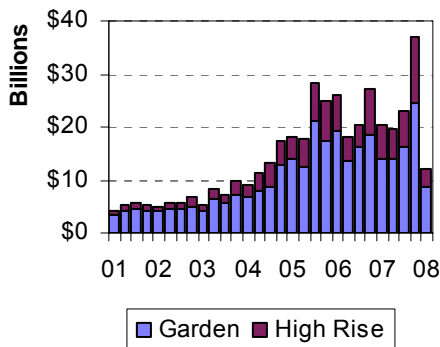
Apartment Market

Cap rates: 6.2 percent for garden apartments, unchanged over the past four quarters; and 6.3 percent for mid- and high-rise properties, a sharp increase of 90 basis points during this period. *Direction: up. The increase for mid- and high-rise properties may relate to the drying up of the condo conversion market.* **Total sales:** \$12.0 billion in the first quarter, off by 41 percent from the year-ago period. *Direction: down from year-ago comparisons, though Fannie Mae and Freddie Mac are putting a floor under apartment sales compared with other property types.* **Investment return:** 1.26 percent (unleveraged) in the first quarter for institutional grade properties, down from 2.87 percent in the



year-ago quarter according to NCREIF. *Direction: stable to slightly lower depending on the depth of the economic downturn.* **Vacancy rate:** 5.9 percent in the first quarter, down slightly from 6.0 percent in the year-ago quarter. *Direction: stable as demand from foreclosed households offsets the increase in shadow supply from unsold condos and homes being converted to rentals.* **Asking rental rates:** \$1,002 per unit, up by 4.2 percent from the year-ago quarter. *Direction: moderately higher.* **Greatest risk:** More layoffs and dim employment prospects for graduating seniors could send would-be renters in search of roommates or to live with relatives until the worst blows over.

Apt. Investment By Product

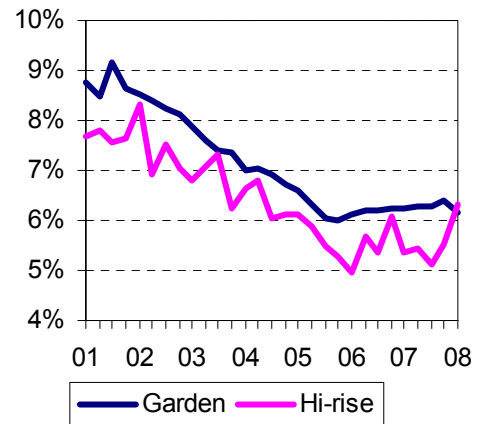


Source: Real Capital Analytics, Grubb & Ellis

Major apartment transactions announced or concluded in the second quarter include the following:

- UDR Inc. sold 25,684 units for \$1.7 billion to a joint venture of DRA Advisors LLC and Steven D. Bell & Co. The portfolio consists of 86 communities in Arkansas, Delaware, Florida, North Carolina, Ohio, Oregon, South Carolina, Tennessee, Texas, Virginia and Washington.
- Trimarchi Management and Capri Capital Partners acquired 10 Texas complexes from Internacional Realty Inc. for close to \$300 million. The portfolio totals 3,041 units.

Apartment Cap Rates



Source: Real Capital Analytics, Grubb & Ellis

- Apartment Investment and Management Co. sold a minority stake in three of its West Los Angeles properties. A fund of JP Morgan Asset Management paid \$202 million for a 47 percent interest in the 1,382-unit portfolio.
- BPG Properties Ltd. acquired Boston Capital Real Estate Investment Trust in a \$260 million transaction. BPG added 11 properties comprising 3,098 units in Seattle, Portland, Salt Lake City, Dallas and Jacksonville, Fla.
- In Chicago's Lakeview and Lincoln Park neighborhoods, a seven-property, 896-unit portfolio traded for \$122.5 million. Newcastle Ltd. purchased the buildings, the majority of which were constructed in the 1920s, from an affiliate of Wexenthaller Realty Management.

Hospitality Market

Cap rates: 8.1 percent for full service hotels, up by 60 basis points over the past four quarters; and 10.6 percent for limited service properties, up sharply by 210 basis points. *Direction: stable to moderately higher.* **Total sales:** \$5.2 billion in the first half, off by 47 percent from the year-ago period. *Direction: lower versus the year-ago totals.* **Investment return:** 1.35 percent (unleveraged) in the first quarter for institutional grade properties, down from 3.56 percent in the year-ago quarter according to NCREIF. *Direction: stable to slightly lower.* **Greatest risk:** A global recession would chill business and

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liesure travel. A stronger dollar would diminish the wave of overseas travelers streaming into the U.S. for bargains.

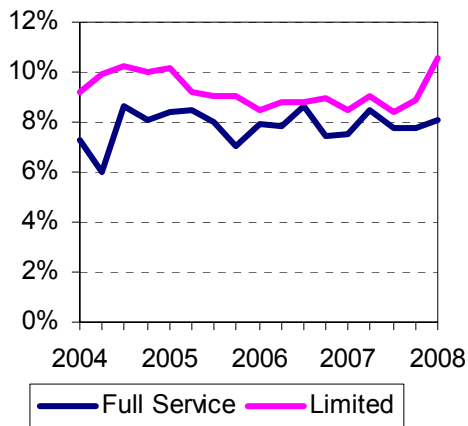
Major hotel property transactions announced or concluded in the second quarter include the following:

- Sam Zell acquired 14.8 million shares of Starwood Hotels & Resorts Worldwide for \$737 million, giving him a 7.7 percent stake in the company.
- HBE Corp. sold its five-property Adams Mark portfolio to Chartres Lodging Group for an estimated \$500 million. The new owner plans to spend an additional \$240 million to renovate and rebrand the properties, which total 4,867 rooms in Dallas, Denver, St. Louis, Indianapolis and Buffalo.

Wyndham Worldwide brands. The portfolio, which is spread throughout the Midwest, totals 2,397 rooms.

- In another joint venture transaction, Interstate teamed with Ireland's Harte Holdings to purchase a four-asset portfolio comprising 892 rooms from Blackstone Group LP. The properties, which are located in Pennsylvania, New Jersey, Washington, D.C., and Louisiana, traded for an aggregate \$207.8 million.

Hotel Cap Rates



Source: Real Capital Analytics, Grubb & Ellis

- FeiCor Lodging Trust Inc. acquired two Renaissance-branded AAA Four-Diamond assets from Walton Street Capital, Rockpoint Group and SCS Advisors for \$225 million. The properties include the 560-room Renaissance Esmeralda Resort & Spa in Indian Wells, Calif., and the 361-room Renaissance Vinoy Resort & Golf Club in St. Petersburg, Fla.
- A joint venture between Interstate Hotels & Resorts and FFC Capital Corp. acquired 22 Exel Inn properties, which it will convert to various