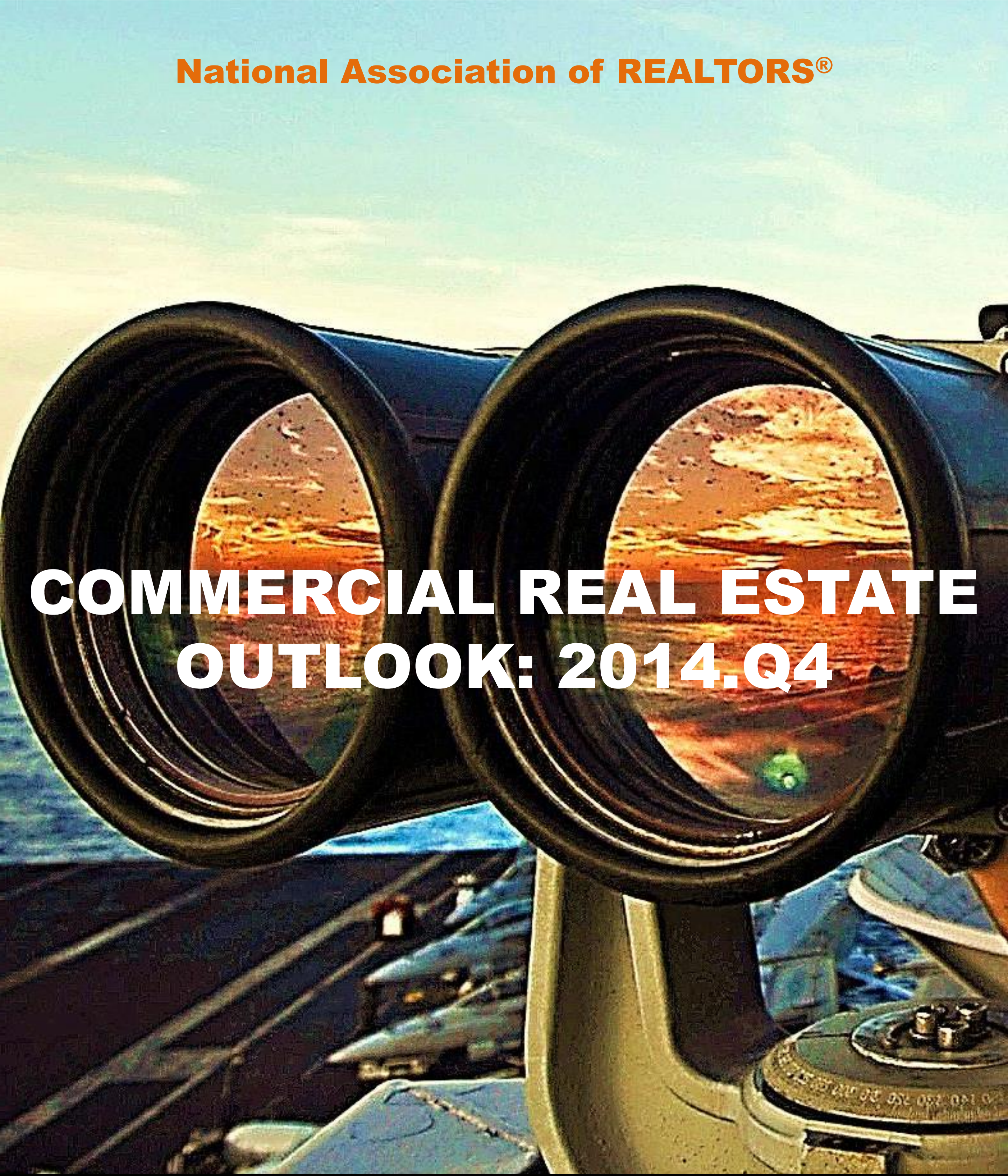
National Association of REALTORS®



COMMERCIAL REAL ESTATE OUTLOOK: 2014.Q4

COMMERCIAL Real Estate

REALTOR®

NATIONAL ASSOCIATION of REALTORS®

ECONOMIC OVERVIEW

Commercial Demand Gets Boost from Economic Momentum in Q3

George Ratiu
Director, Quantitative & Commercial Research

Amid worries of a global economic slackening, U.S. gross domestic product (GDP) increased at an annual rate of 3.6 percent during the third quarter 2014. The pace of growth exceeded economists' expectations, and it provided forward momentum to commercial real estate markets.

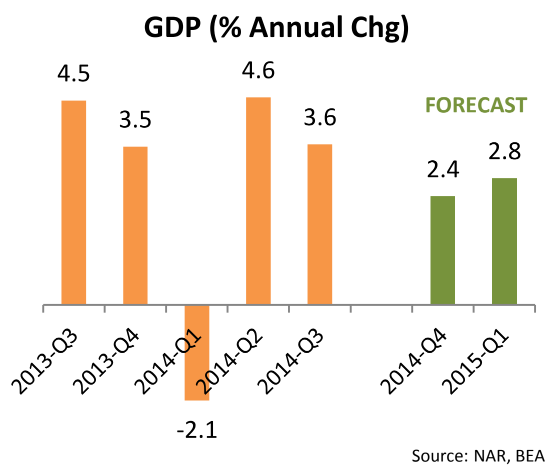
Gains in international trade along with positive government spending were the main engines of growth for third quarter GDP. After a double-digit annual rate of growth in the second quarter, U.S. exports rose at a 7.8 percent rate in the third quarter. Export sector growth was boosted by U.S. goods leaving for foreign shores at a pace which was 11.0 percent higher. Meanwhile, imports of goods and services declined at a 1.7 percent rate over the period, due mainly to a drop in imported goods.

Government spending—which has acted as a drag on GDP growth over the past few years—rose at a 4.6 percent annual rate during the third quarter. The increase came from federal spending, specifically national defense consumption, which advanced at a 15.9 percent rate during the quarter. Government spending at the state and local levels was also positive—1.3 percent higher on an annual basis.

Consumer spending—the largest GDP component—also rose, but at a more modest 1.8 percent annual rate.

Consumers spent more on both goods and services, by 3.1 percent and 1.1 percent annual rate, respectively.

Consumers purchased more cars, furniture and household appliances, recreational vehicles, as well as clothing and shoes. The quarter also bode well for transportation providers, along with financial services and insurance companies, which experienced higher sales.



Business spending increased at a 5.5 percent annual rate, driven by spending on equipment upgrades. Spending on industrial equipment increased 24.9 percent, while investments in transportation equipment rose 30.2 percent in the third quarter. Commercial construction continued, with investments in commercial structures rising 3.7 percent. Business investments in intellectual property products—software, R&D, entertainment, literary works—increased at a 4.2 percent annual rate.

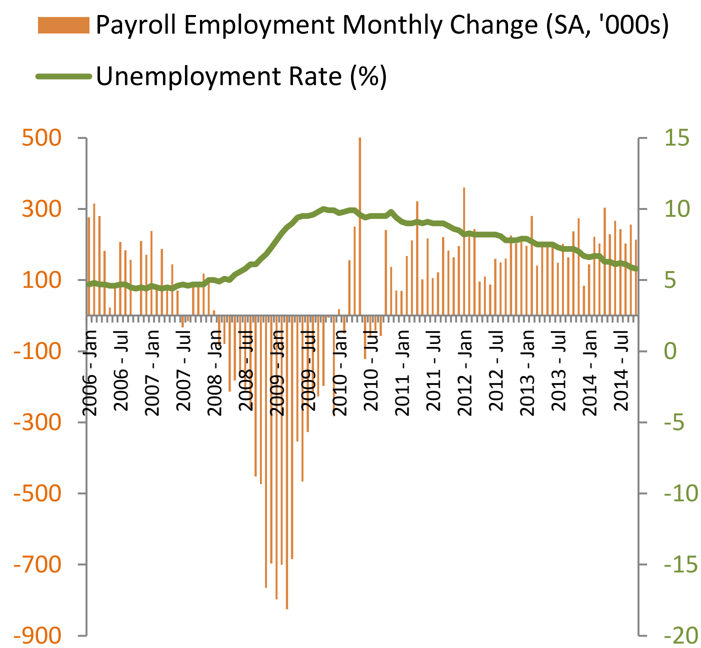
The economic picture was positive across most major indices. Manufacturers' new orders rose at an annual rate of 15.9 percent in the third quarter, on the strength

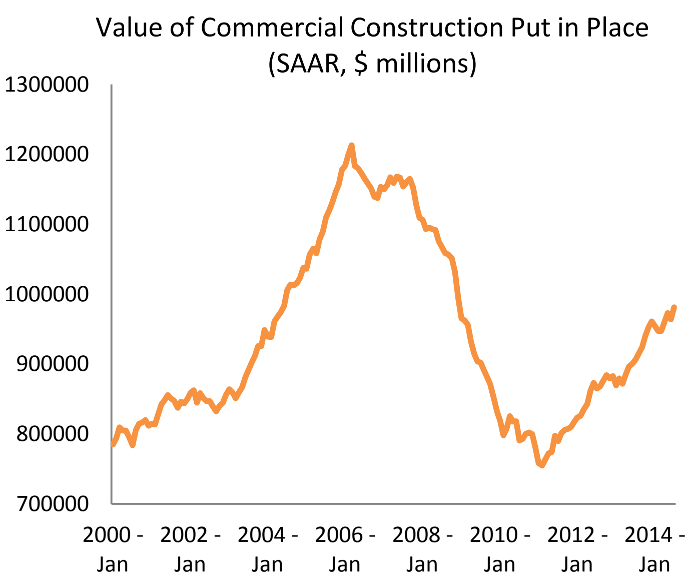
ECONOMIC OVERVIEW

of transportation equipment orders, especially large orders of nondefense aircraft in July. Manufacturer's shipments increased at a 4.8 percent annual rate during the quarter, taking pressure of inventories, which increased at 1.4 percent, the slowest advance of the year so far. The Institute for Supply Management's Composite Index of manufacturing and nonmanufacturing activity rose at a 23.3 percent annual rate, reaching a value of 58.8 in the third quarter (values above 50 denote increasing activity).

As businesses felt more confident during the period, employment advanced. Payroll employment gained a total of 702,000 net new jobs during the third quarter. The start of the fourth quarter in October reinforced the trend, with an additional 214,000 jobs generated during the month.

The third quarter figure was the third largest quarterly increase since the first quarter of 2006, prior to the Great Recession. Goods-producing sectors provided 121,000 new jobs, while service industries added an additional 562,000 net new positions. The government sector contributed 19,000 new positions.





Professional and business services along with the financial industry added 193,000 new jobs, while the information industry contributed 37,000 new jobs. Continued advance in office-using employment was reflected in demand for office space over the period.

Employment in wholesale trade also gained, adding 13,800 new jobs during the quarter. When combined with the additional 37,700 new positions in transportation and warehousing industries, the figure offered a positive signal about the health of the industrial real estate sector.

The unemployment rate declined from 6.2 percent in the second quarter 2014 to 6.1 percent in the third quarter. The labor force participation rate remained unchanged at 62.8 percent. Employee compensation—adjusted for inflation—increased at a 1.0 percent annual rate during the third quarter.

ECONOMIC OVERVIEW

Consumer confidence rose in tandem with the economic gains during the quarter. The Conference Board's index rose to a value of 90.9 in the third quarter, the highest value since the fourth quarter2007. The University of Michigan's Consumer Sentiment index also hit its highest point since 2007, reaching a value of 83.0 in the third quarter.

The GDP outlook for 2015 and 2016 project GDP growth rates of 2.7 and 2.9 percent, respectively. Payroll employment growth is expected to remain steady at 1.9 percent in 2015 and 2.0 percent in 2016. With the Fed's closing of the quantitative easing program, expectations of interest rate increases are rising. While inflation remains contained, with the Eurozone concerned about deflation, price pressures in the U.S. are being felt. Inflation is expected to reach 2.7 percent in 2015 and 3.3 percent in 2016.

NCREIF PROPERTY INDEX RETURNS: 2014.Q3

NATIONAL	2.63%
OFFICE	2.78%
INDUSTRIAL	2.92%
RETAIL	2.33%
APARTMENT	2.53%

Source: National Council of Real Estate Investment Fiduciaries

U.S. ECONOMIC OUTLOOK: NOVEMBER 2014

	2013	2014	2015	2016
Annual Growth Rate, %				
Real GDP	2.2	2.2	2.7	2.9
Nonfarm Payroll Employment	1.7	1.9	1.9	2.0
Consumer Prices	1.5	1.6	2.7	3.3
Level				
Consumer Confidence	73	87	95	98
Percent				
Unemployment	7.4	6.2	5.7	5.5
Fed Funds Rate	0.1	0.1	0.4	1.6
3-Month T-bill Rate	0.1	0.1	0.7	1.9
Corporate Aaa Bond Yield	4.3	4.2	4.8	5.8
10-Year Gov't Bond	2.6	2.6	3.2	4.3
30-Year Gov't Bond	3.4	3.4	4.2	5.4

Source: National Association of REALTORS®

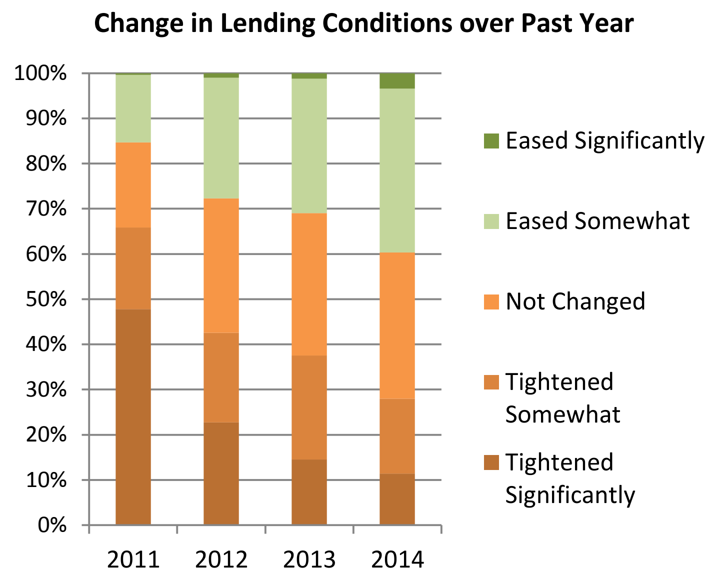
NOVEMBER
2014

COMMERCIAL SPOTLIGHT: 2014 REALTORS® LENDING SURVEY

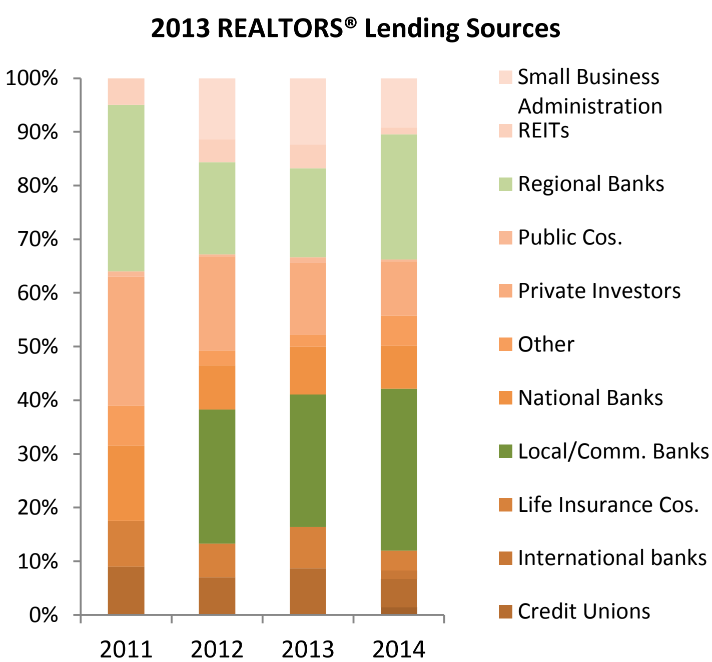
Five years after the Great Recession, lending conditions in REALTOR® markets show signs of recovery. With commercial real estate fundamentals and investment prices on a solid upward trend, lending conditions eased as financing sources broadened in 2014.

The changes in capital liquidity are a welcome sign, pointing to improvements across a wider geographical range. While cash accounts for a third of sales, the main sources of capital for commercial REALTORS®' clients are local and regional banks, along with private investors.

The incidence of failed transactions due to lack of financing diminishes with each passing year, yet lenders' underwriting standards remain the principal obstacle to sales. REALTORS® cite the uncertainty brought about by existing and proposed legislative and regulatory initiatives as the most relevant cause of bank capital for commercial real estate.



During 2013, commercial real estate witnessed broad-based increases in capital availability.



The trend accelerated during 2014, as most major capital providers returned to the markets and actively competed, leading some investors to express concern about an overabundance of capital chasing too few deals in some markets. Both listed and non-listed REITs notched record capital raising levels during 2013. Meanwhile, sovereign wealth funds, institutional funds and private investors funneled ever-growing amounts into commercial assets.

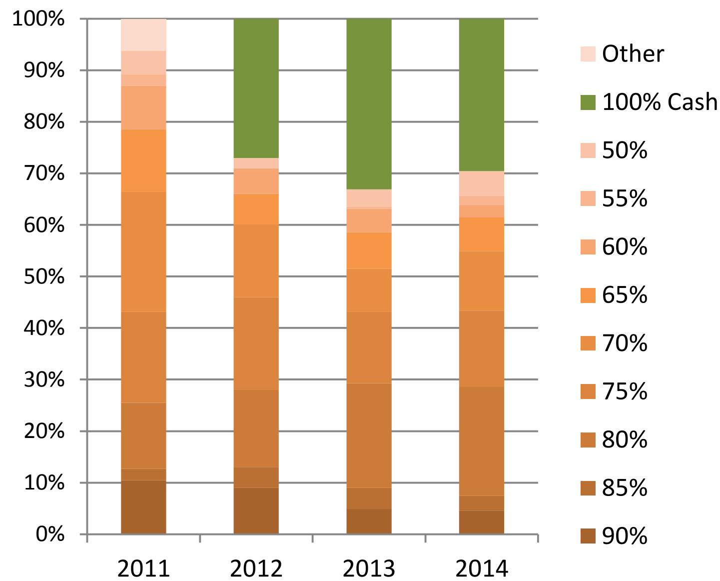
Private investors accounted for the largest portion of acquisitions, making up 41 percent of the market in 2013, based on data from Real Capital Analytics. With $146.4 billion in deals, private investors increased their acquisitions by 20 percent year-over-year. Publicly-listed companies were the second largest group of investors, with deals totaling $66.2 billion, a 50 percent jump on a yearly basis. Institutional funds closed $45.9 billion in commercial deals during 2013, the only group to show a decline from 2012. With Asian investors, national pension funds, and sovereign wealth funds chasing the stability and returns of U.S. assets, cross-border acquisitions rose 39 percent in 2013 compared with the prior year, totaling $35.6 billion.

NOVEMBER
2014

COMMERCIAL SPOTLIGHT: 2014 REALTORS® LENDING SURVEY

- **75%** of respondents closed deals in 2013/14
- **93%** of sales were valued at or below **$5 million**
- Sales composition:
  - Office CBD: 18%
  - **Office Suburban: 32%**
  - **Industrial Warehouse: 36%**
  - Industrial Flex: 20%
  - Multi-family: 30%
  - Retail Strip Center: 26%
  - Retail Mall: 4%
  - **Land: 40%**
  - Hotel: 6%
  - Other: 18%
- **Capital** availability **eased** in **39%** of markets
- Top **sources** of capital:
  - **Local/community banks**: **56%**
  - **Regional banks: 43%**
  - Private investors: **19%**
  - Small Business Administration: 17%
  - National banks: 15%
  - Credit unions: 10%
  - Life insurance companies: 7%
  - International banks: 3%
  - CMBS: 3%
  - REITs: 2%
  - Public companies: 1%
- **Cash** comprised **30%** of all transactions
- **27%** used the **Small Business Administration** refinance program
- Debt-to-service coverage ratio (**DSCR**) was **1.4**.

Average Loan-to-Value for CRE Transactions



- **47%** of sales **failed** due to **lack of financing**
  - Loan **underwriting** standards caused **63%** of financing failures
  - **20%** caused by **appraisals/valuation**
  - **17%** due to financing availability
- **20%** of deals **failed** to secure **re-financing**, compared with 50% in the 2012 report
- Causes of insufficient CRE bank capital:
  - Legislative/regulatory initiatives: **27%**
  - U.S. Economic uncertainty: **22%**
  - Reduced NOI, values & equity: 19%
  - Financial regulatory uncertainty: 19%
  - Disposition of distressed assets: 6%
  - Global economic uncertainty: 4%
  - Pooling/packaging of CMBS:4%
- **18%** of respondents had **international** clients/investors

COMMERCIAL FORECAST

OFFICE	2014 IV	2015 I	2015 II	2015 III	2015 IV	2016 I	2016 II	2014	2015	2016
Vacancy Rate	15.7%	15.8%	15.7%	15.7%	15.6%	15.7%	15.6%	16.2%	15.7%	15.6%
Net Absorption ('000 sq. ft.)	13,855	12,002	11,851	12,865	12,123	13,522	13,352	35,586	48,841	55,026
Completions ('000 sq. ft.)	8,663	10,095	12,079	9,857	10,122	10,530	12,086	27,073	42,154	44,460
Inventory ('000,000 sq. ft.)	4,134	4,144	4,156	4,166	4,176	4,186	4,198	4,134	4,176	4,220
Rent Growth	0.7%	0.8%	0.8%	0.8%	0.9%	0.8%	0.9%	2.6%	3.3%	3.6%

INDUSTRIAL	2014 IV	2015 I	2015 II	2015 III	2015 IV	2016 I	2016 II	2014	2015	2016
Vacancy Rate	8.8%	8.7%	8.5%	8.5%	8.4%	8.3%	8.1%	8.9%	8.5%	8.1%
Net Absorption ('000 sq. ft.)	25,450	18,443	25,616	30,739	27,665	19,040	26,445	110,652	102,463	105,780
Completions ('000 sq. ft.)	15,666	14,983	22,118	20,691	13,556	13,040	19,250	81,009	71,349	62,097
Inventory ('000,000 sq. ft.)	8,466	8,480	8,503	8,523	8,537	8,550	8,569	8,466	8,537	8,599
Rent Growth	0.7%	0.6%	0.7%	0.8%	0.8%	0.7%	0.8%	2.4%	2.9%	3.1%

RETAIL	2014 IV	2015 I	2015 II	2015 III	2015 IV	2016 I	2016 II	2014	2015	2016
Vacancy Rate	9.7%	9.7%	9.6%	9.6%	9.5%	9.6%	9.4%	9.8%	9.6%	9.4%
Net Absorption ('000 sq. ft.)	3,879	5,096	4,341	3,486	5,949	6,424	5,472	11,350	18,871	23,792
Completions ('000 sq. ft.)	3,719	2,940	2,567	2,941	3,264	4,162	3,596	7,747	11,711	15,924
Inventory ('000,000 sq. ft.)	2,050	2,053	2,055	2,058	2,061	2,066	2,069	2,050	2,061	2,077
Rent Growth	0.6%	0.5%	0.6%	0.7%	0.7%	0.6%	0.7%	2.0%	2.5%	3.0%

MULTI-FAMILY	2014 IV	2015 I	2015 II	2015 III	2015 IV	2016 I	2016 II	2014	2015	2016
Vacancy Rate	4.0%	4.0%	4.0%	4.1%	4.3%	4.1%	4.2%	4.0%	4.1%	4.2%
Net Absorption (Units)	76,152	43,855	39,723	37,479	50,110	36,799	33,332	216,296	171,167	143,626
Completions (Units)	47,123	41,919	55,952	54,433	58,364	35,473	45,058	180,796	210,669	165,339
Inventory (Units in millions)	10.2	10.3	10.3	10.4	10.5	10.5	10.5	10.2	10.5	10.6
Rent Growth	1.0%	1.0%	1.0%	1.0%	0.9%	1.0%	0.9%	4.0%	3.9%	3.5%

Sources: National Association of REALTORS® / Reis, Inc.

COMMERCIAL FORECAST: METRO VACANCY RATES – 2014.Q4

Source: NAR, Reis, Inc.		Office	Industrial	Retail	Multifamily
Albuquerque	NM	17.3		11.6	3.3
Atlanta	GA	19.4	13.6	13.1	5.8
Austin	TX	15.8	11.0	6.5	6.1
Baltimore	MD	16.4	11.6	6.3	4.0
Birmingham	AL	13.7		13.8	6.5
Boston	MA	12.9	17.9	6.3	4.5
Buffalo	NY	15.8		13.2	3.1
Central New Jersey	NJ	21.6		9.7	2.8
Charleston	SC	13.8		11.0	6.2
Charlotte	NC	17.5	12.7	9.8	5.6
Chattanooga	TN	16.2		15.2	5.1
Chicago	IL	18.6	8.6	12.2	3.5
Cincinnati	OH	20.4	8.7	12.3	3.3
Cleveland	OH	22.8	8.9	14.6	2.8
Colorado Springs	CO	18.2		14.9	3.6
Columbia	SC	17.6		10.5	6.3
Columbus	OH	18.6	9.3	15.9	5.0
Dallas	TX	23.1	12.5	12.9	5.3
Dayton	OH	26.6		16.2	5.0
Denver	CO	16.6	7.7	10.6	4.5
Detroit	MI	25.1	11.4	11.6	3.0
District of Columbia	DC	9.3			7.0
Fairfield County	CT	21.9		3.9	5.6
Fort Lauderdale	FL	19.6	8.6	10.0	4.3
Fort Worth	TX	16.5	9.9	12.1	4.6
Greensboro/Winston-Salem	NC	21.5		11.4	5.9
Greenville	SC	19.2		14.2	5.4
Hartford	CT	19.9		10.1	2.4
Houston	TX	14.6	8.1	11.7	5.8
Indianapolis	IN	19.7	9.6	15.3	6.1
Jacksonville	FL	21.1	7.8	13.0	6.6
Kansas City	MO	17.1	10.3	11.5	4.5
Knoxville	TN	14.7		11.6	4.4
Las Vegas	NV	25.7		12.0	5.1
Lexington	KY	16.7		7.9	4.9
Little Rock	AR	11.6		11.4	6.4
Long Island	NY	13.2		5.3	2.8

COMMERCIAL FORECAST: METRO VACANCY RATES – 2014.Q4

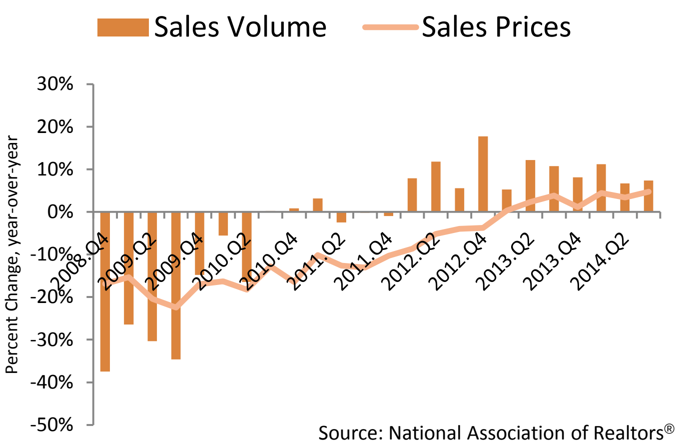
Source: NAR, Reis, Inc.

		Office	Industrial	Retail	Multifamily
Los Angeles	CA	14.7	3.7	5.7	3.2
Louisville	KY	15.1		9.1	5.5
Memphis	TN	23.5	14.6	11.7	8.7
Miami	FL	15.6	6.0	7.0	3.8
Milwaukee	WI	18.9		12.8	3.5
Minneapolis	MN	16.6	7.1	11.0	3.1
Nashville	TN	14.0	7.9	8.2	4.8
New Haven	CT	16.9		13.8	2.3
New Orleans	LA	13.0		11.8	5.7
New York	NY	9.6			2.7
Norfolk/Hampton Roads	VA	16.3		9.6	5.2
Northern New Jersey	NJ	18.7		5.5	4.4
Oakland-East Bay	CA	17.4	8.8	6.2	2.6
Oklahoma City	OK	17.1		13.4	4.8
Omaha	NE	14.7		8.9	3.0
Orange County	CA	17.0	3.6	5.2	2.2
Orlando	FL	17.2	10.9	12.0	5.3
Palm Beach	FL	17.1	6.5	10.2	5.1
Philadelphia	PA	13.8	9.8	9.2	3.4
Phoenix	AZ	25.3	11.0	10.2	5.0
Pittsburgh	PA	16.6	8.8	7.7	3.4
Portland	OR	13.4	7.9	8.1	3.1
Providence	RI	15.8		11.8	2.3
Raleigh-Durham	NC	14.8	14.6	9.1	7.1
Richmond	VA	14.5	11.5	9.8	4.7
Rochester	NY	17.1		12.5	2.8
Sacramento	CA	20.6	11.6	10.9	2.2
Salt Lake City	UT	17.3		12.1	4.0
San Antonio	TX	17.4	7.2	11.0	5.7
San Bernardino/Riverside	CA	23.3	7.2	10.1	3.0
San Diego	CA	15.8	6.8	6.2	2.6
San Francisco	CA	12.2	10.8	3.5	3.3
San Jose	CA	17.7	16.5	4.6	2.7
Seattle	WA	12.8	5.8	7.0	4.4
St. Louis	MO	17.2	6.6	12.2	4.4

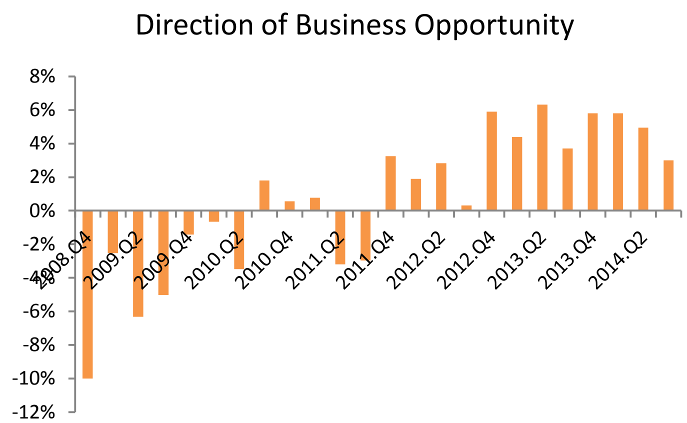
COMMERCIAL FORECAST: METRO VACANCY RATES – 2014.Q4

Source: NAR, Reis, Inc.		Office	Industrial	Retail	Multifamily
Suburban Maryland	MD	16.1	11.0	8.2	4.0
Suburban Virginia	VA	17.4	10.6	5.4	4.8
Syracuse	NY	14.5		14.0	3.1
Tacoma	WA	15.2		13.1	3.3
Tampa-St. Petersburg	FL	21.1	7.9	10.9	4.6
Tucson	AZ	17.0		10.2	5.6
Tulsa	OK	16.8		15.4	5.5
Ventura County	CA	18.2		8.7	2.6
Westchester	NY	18.9		7.9	3.0
Wichita	KS	17.4		14.3	3.5

INVESTMENT TRENDS AT A GLANCE



Source: National Association of Realtors®



Source: National Association of Realtors®

2014.Q3 Investment Conditions	
Office	2.8
Multifamily	4.0
Industrial	3.6
Retail	3.2
Hospitality	3.2

Scale: 1 – 5

2014.Q3 Investment Value vs. Price Ratio	
Office	2.9
Multifamily	2.9
Industrial	3.2
Retail	3.0
Hospitality	2.9

Scale: 1 – 5

2014.Q3 Cap Rates by Property Type and Region(%)	Canada & Mexico	East	Midwest	Other	South	West
Apartment	5.0	6.8	7.8	6.4	7.2	5.7
Office CBD	5.0	6.9	8.6	6.8	7.8	6.8
Office Suburban	6.0	7.4	8.9	7.4	8.4	7.5
Warehouse	7.0	7.9	8.1	7.6	8.3	7
Flex		8	8.4	7.5	8.3	7.1
Retail	6.0	6.8	8.5	6.5	7.7	6.9
Hotel		7.7	9.4	7.9	7.9	6.8
Development		9.8	12.3	8.7	11.9	13.7
Land		12.5	12.7	11	8.4	7.5

Sources: NAR, The CCIM Institute

REALTOR® RESEARCH

The Research Division of the National Association of REALTORS® monitors and analyzes monthly and quarterly economic indicators, including retail sales, industrial production, producer price index, gross domestic product and employment data which impact commercial markets over time. In addition, the Research Division provides several products covering commercial real estate:

- Commercial Real Estate Quarterly Market Survey
- Commercial Real Estate Lending Survey
- Commercial Member Profile
- Expectations and Market Realities in Real Estate 2014
- CCIM Quarterly Market Trends
- SIOR Commercial Real Estate Index

CONTACT

Lawrence Yun, PhD
Chief Economist, Sr. Vice President, Research
lyun@realtors.org

George Ratiu
Director, Quantitative & Commercial Research
gratiu@realtors.org

Although the information presented in this report has been obtained from reliable sources, NAR does not guarantee its accuracy, and such information may be incomplete. This report is for information purposes only. All opinions, assumptions and estimates constitute NAR's judgment as of the date of this publication and are subject to change and evolving events. Actual results may vary from forecast results.

For more information:

REALTOR.org — REALTOR.org/research-and-statistics

Economists' Outlook — economistsoutlook.blogs.realtor.org

www.facebook.com/narresearchgroup

twitter.com/#!/NAR_Research

CCIM Institute — www.ccim.com/resources/itq

professional report — www.siorprofessionalreport-digital.com