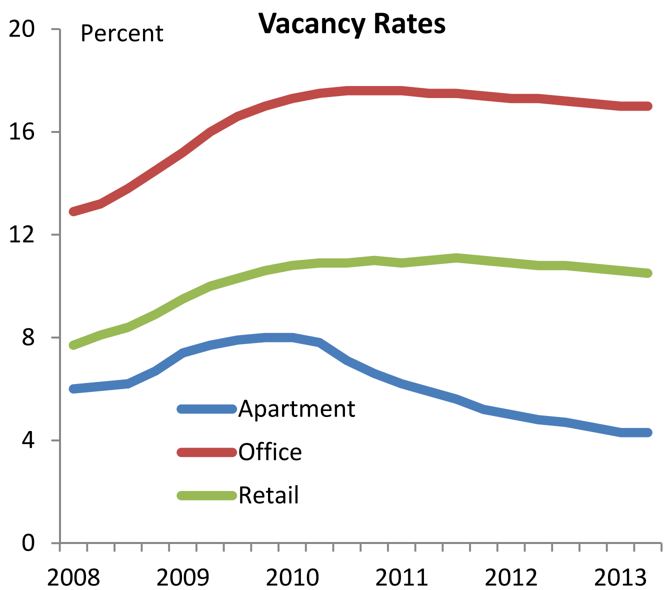
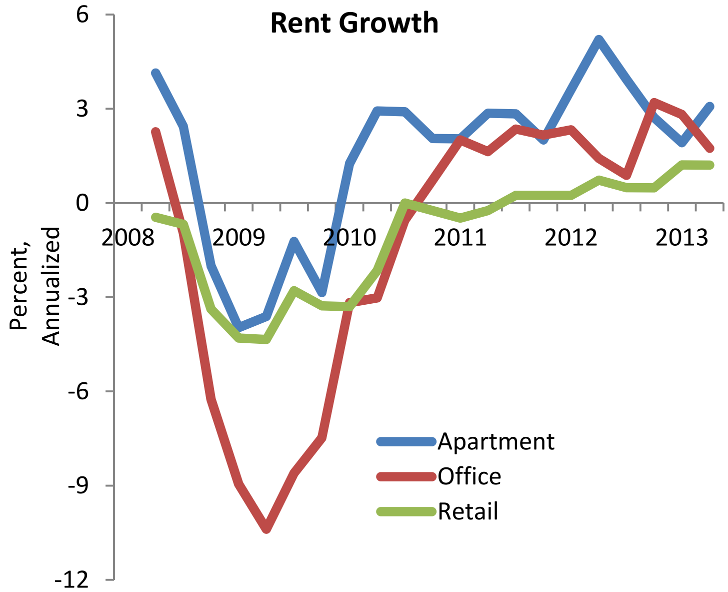
Commercial Property Update 2013:Q2





The apartment sector still enjoys strong demand and tight vacancies, despite concerns that rental markets would suffer as the housing market came back to life (home sales, housing starts and prices are all on an upward path; chart and discussion, next page). New supply of apartments remains modest, although starts continue to rise. Apartment vacancy rates are steady at a low 4.3 percent, and rent growth rebounded after decelerating a bit in Q1.

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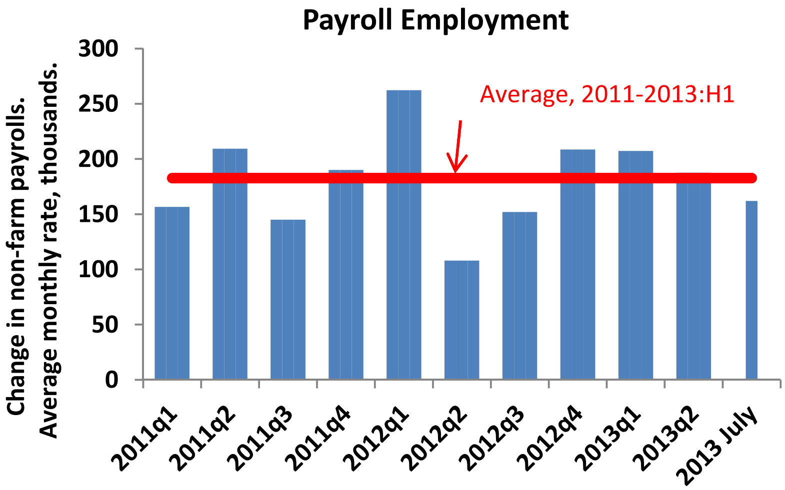
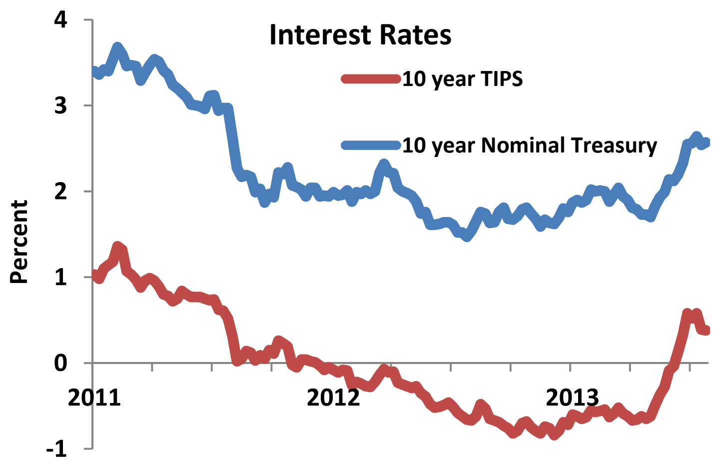
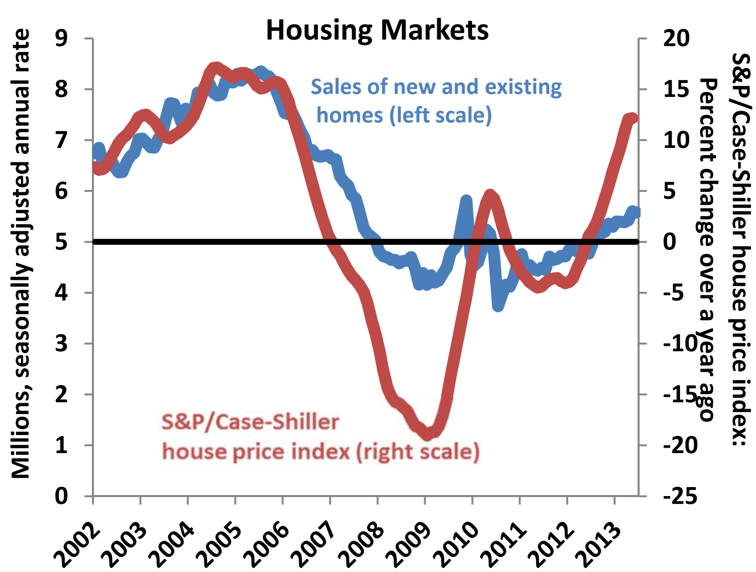
The office sector showed little improvement in the second quarter. Vacancy rates were unchanged at 17.0 percent, only 0.6 ppt below its peak in late 2010-early 2011. Net absorption remains sluggish but there is little new construction to speak of. Rent growth decelerated, and effective rents are still below their levels in 2009. The national average figures reflect a mix of solid improvement in CBD markets but very weak in the suburbs. Second-tier cities are seeing gains in office markets.

The retail sector continued the slow improvement that began late last year. Vacancy rates are drifting down very gradually, but rent growth has firmed a bit. Regional malls continue to lead the way while community and neighborhood centers lag.

Economic Outlook







Economic Fundamentals

Job growth slowed in July to 162,000, considerably below recent trends. Average hourly earnings edged down and the work week also slipped a bit, confirming the relative weakness of the report. The unemployment rate fell 0.2 ppt, to 7.4%; only those actively looking for work are counted, however, and a drop in labor force participation accounted for part of the decline in the unemployment rate.

The July employment report is at odds with other indicators that suggest better labor market conditions, however, including a drop in jobless claims to the lowest since January 2008 and a move up in the ISM employment sub-index.

Interest rates backed up as Federal Reserve officials discussed possible timing of an end to QE3. Rates on the 10 year Treasury note rose 100+ bps but, at less than 3%, remain extremely low by any historical standard. TIPS yields, which subtract inflation, moved slightly positive.

Housing markets are rebounding (finally!), with rising sales, prices and construction. After years of little or no new home building, excess housing stock has been largely worked off, and inventories are tight—in fact, lack of supply is inhibiting sales in many markets. Mortgage rates remain low, despite the recent rise, and should have a minor impact on the housing recovery.