



RREEF Alternative Investments

Real Estate

Infrastructure

Private Equity



Lambda Alpha International  
Golden Gate Chapter

## RREEF Research: Economic and Real Estate Market Forecast 2010

January 12, 2010

*Presented by:*

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## Section I

# Macroeconomic and Capital Market Outlook

## Labor Productivity Should Slow...So Employment Bottoms in the First Quarter

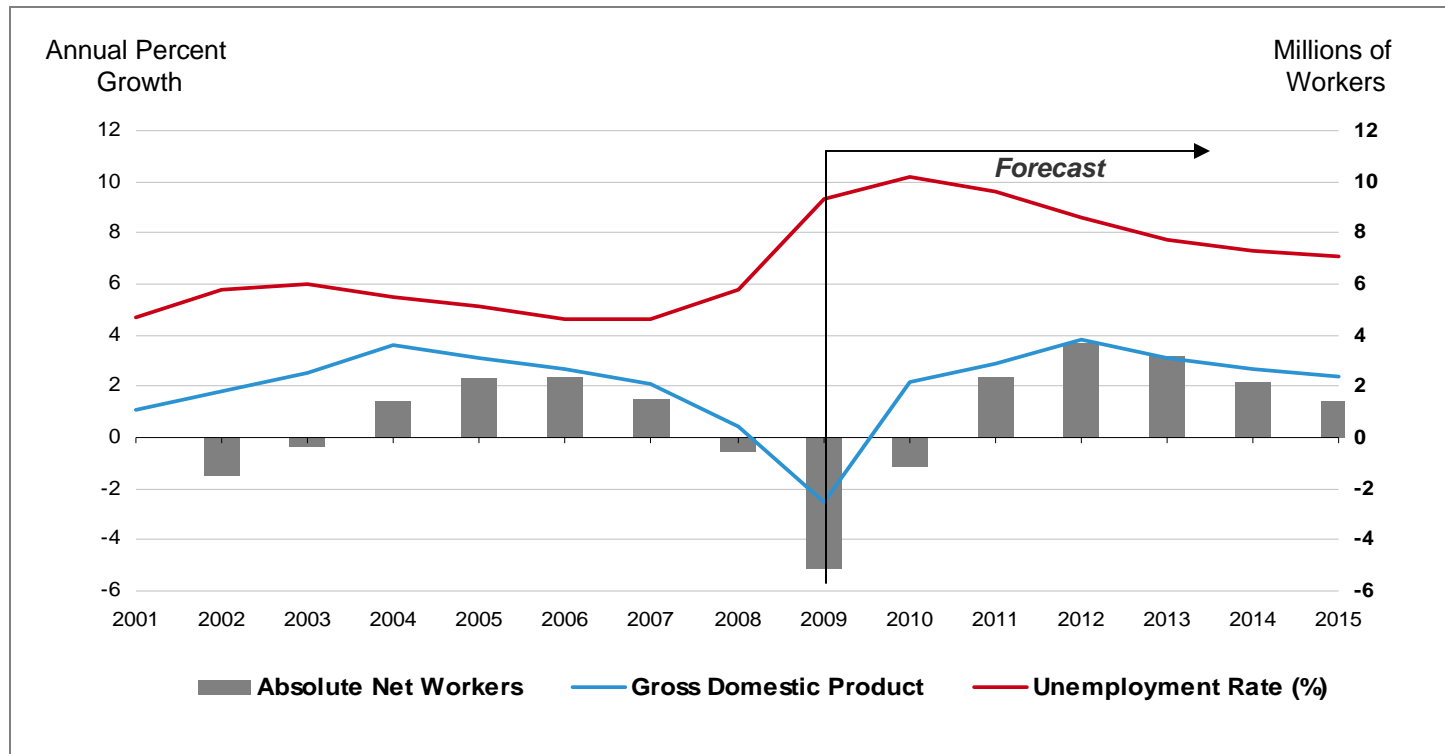


### Case for Recovery in U.S. Job Market

- Pent-up demand for labor
- Pace of job cuts easing
- Surge in temp hires
- Jump in the private work week
- A partial reversal in the jump in the unemployment rate
- Fall in new claims for unemployment benefits

Sources: Global Insight, RREEF Research.  
As of December 2009.

## Employment Growth will Lag Economic Recovery

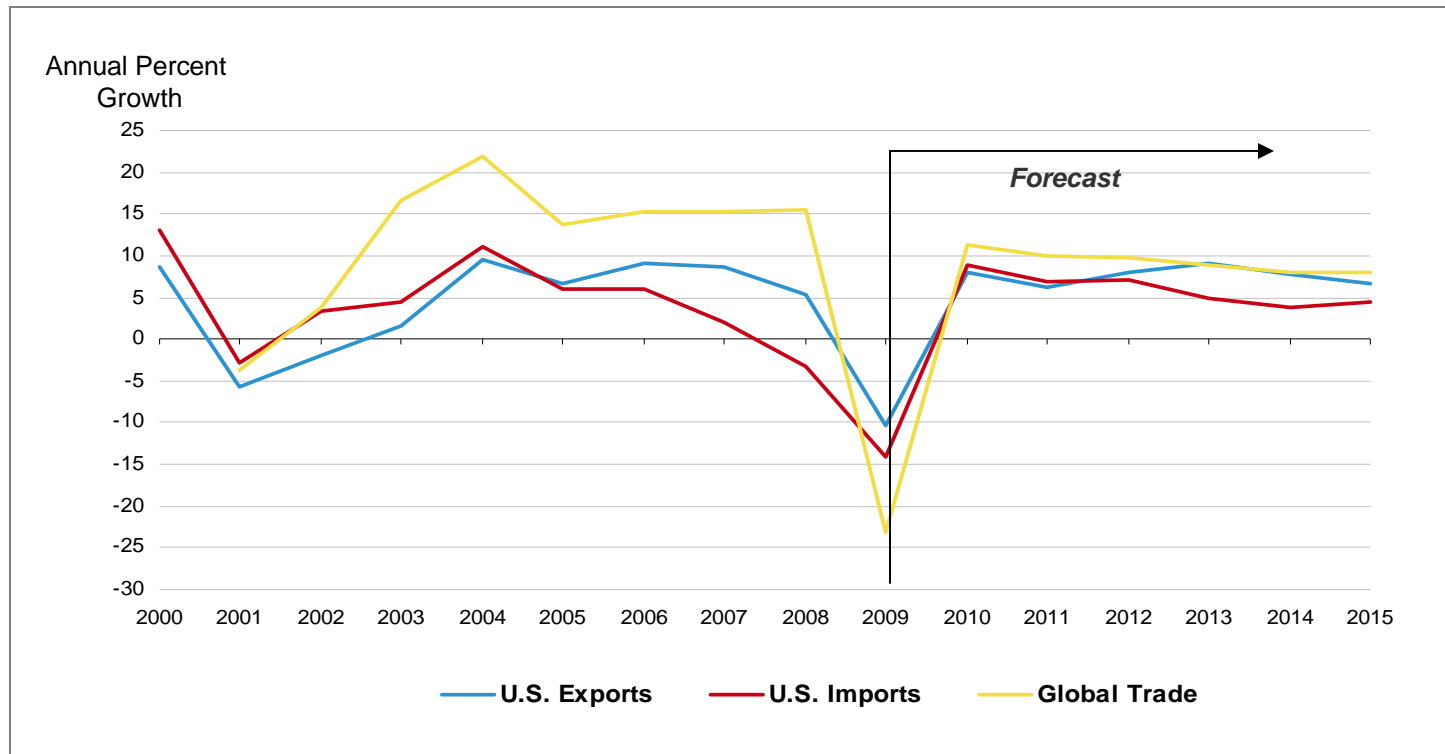


Source: BEA, BLS and Global Insight  
As of December 2009

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## International Trade will Resume Growth and Rebalance



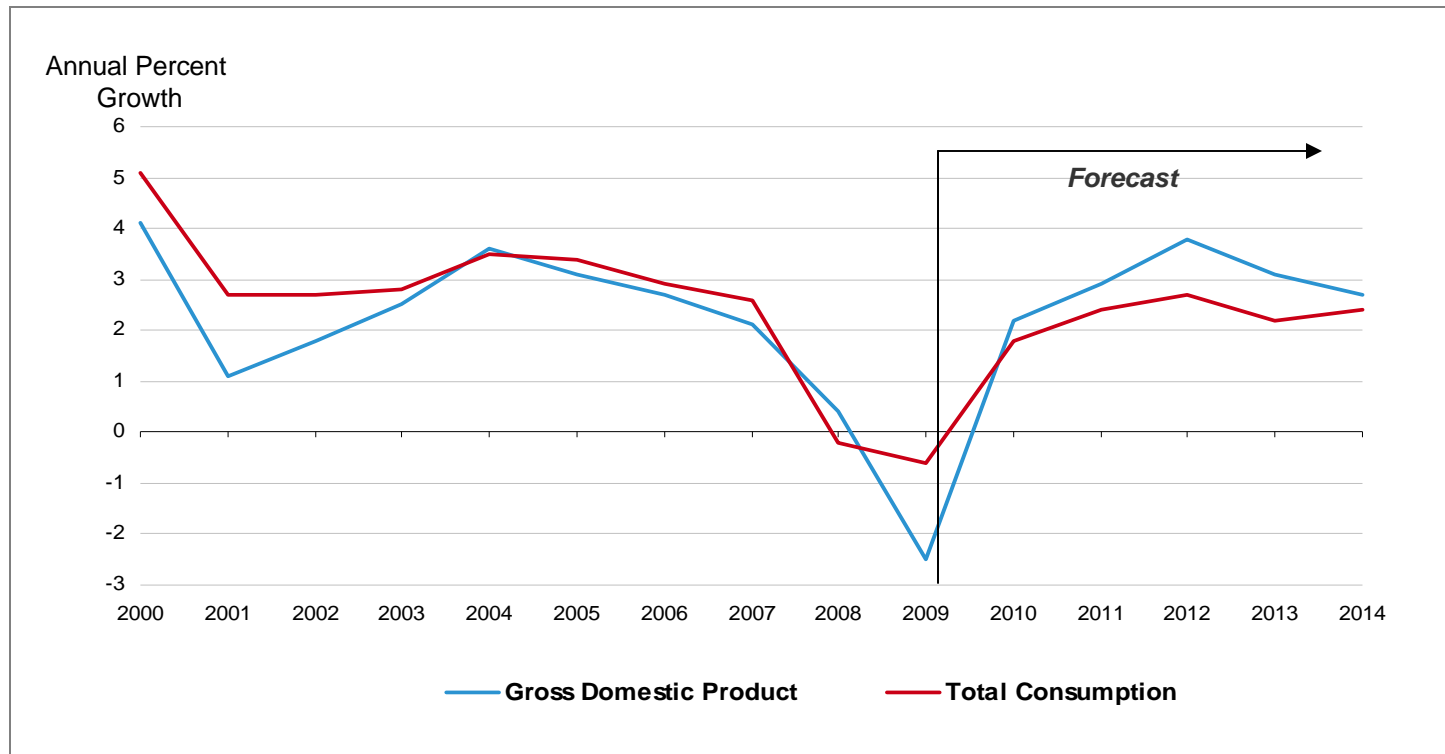
Source: BEA and Global Insight  
As of December 2009

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## Economic Recovery will begin in 2010

Consumption will Lag Overall Recovery



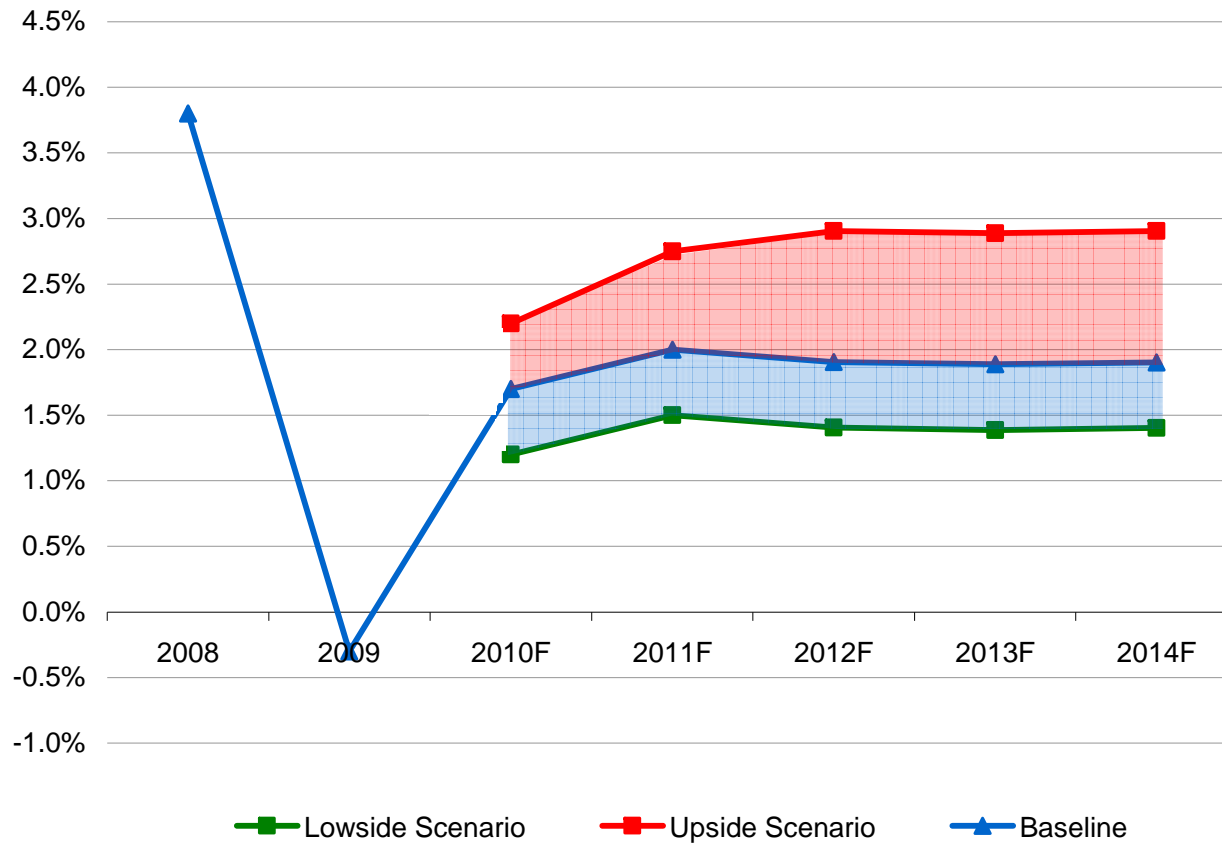
Source: BEA and Global Insight  
As of December 2009

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## Future Inflation is a Worry

Consumer Price Inflation Forecast



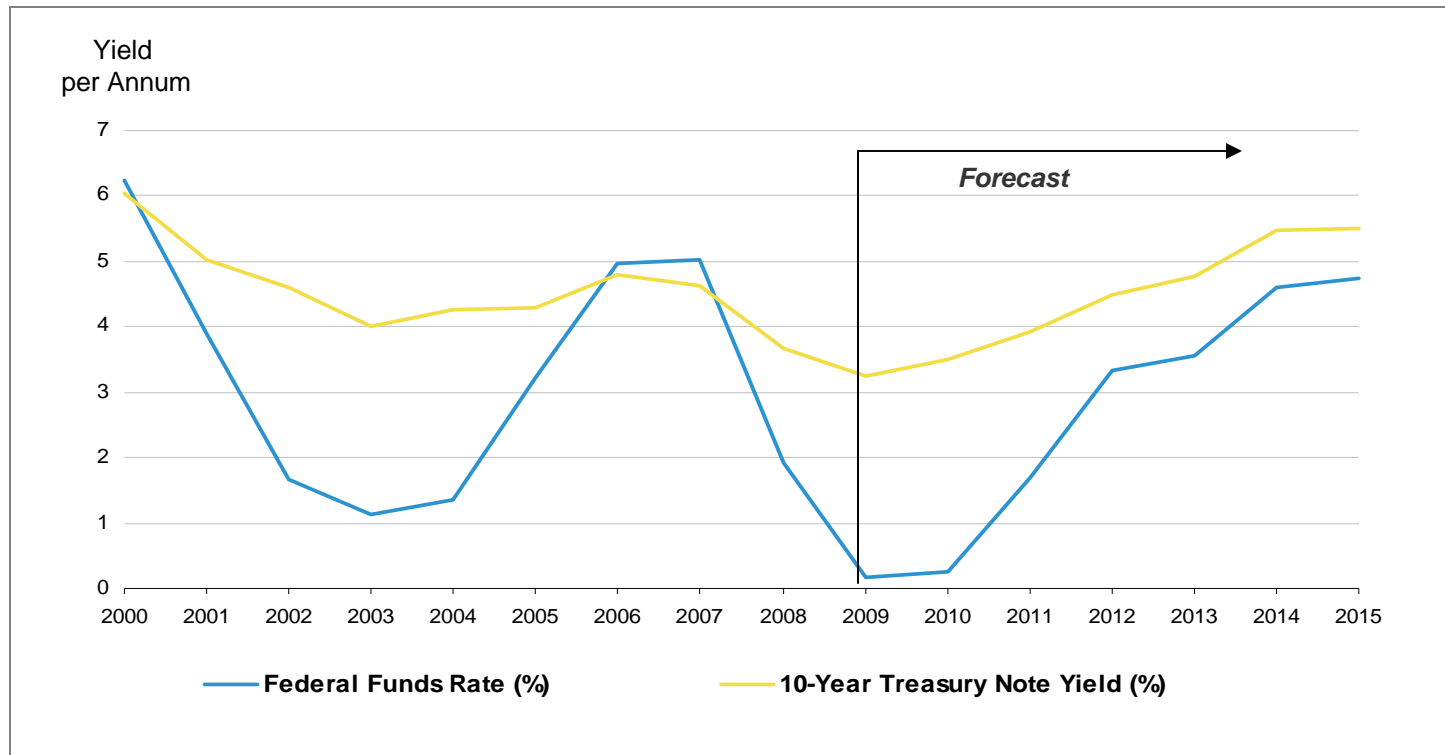
F = Forecast

Sources: Global Insight, RREEF Research.

As of December, 2009.



## Fed Funds Rate will Increase Against Inflation



Source: Federal Reserve, US Treasury and Global Insight  
As of December 2009

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## Employment Growth in Northeast and Midwest will Lag the South and West\*



\* Size of "star" reflects relative population size of metro area.  
Source: Economy.com.  
As of November 30, 2009.



## Significant Risks and Recovery

- ❑ **Inflation:** Feds efforts insufficient to control inflation in other years
- ❑ **Distressed Real Estate:** Large volume of distressed properties pushed onto market depressing values
- ❑ **Political:** Dysfunctional Congress fails to balance timely need for growth with need for deficit reduction
- ❑ **Business Expansion:** Global and U.S. business fail to replace the consumer as key driver of this recovery
- ❑ **Geopolitical:** Mounting protectionism





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## Section II

# Real Estate Market Summary Outlook

## Property Type Expectations: 2010-2014

### Apartments well poised for future

- First sector to achieve healthy occupancy (2012)
- “Echo Boom” (20-35 years old) household formation increases
- Supply constrained markets – not overbuilt with for sale housing should outperform
- Urban and inner suburban transit-oriented locations with employment and/or retail amenities nearby are preferred

### Industrial will weather downturn

- Industrial markets should stabilize more quickly than office
- Occupancy should stabilize in 2010 and steadily improve in 2011 and 2012
- Rents likely to decline another 10 percent nationally
- Warehousing for imports and retailers will be weakest

### Office most volatile and sensitive to recession

- Vacancy expected to peak in 2010 at 600 basis points above 2007
- Declining rents in all metros during 2010 average  $\pm$  5%
- Peak-to-trough rental declines nationally expected at 25 percent or more
- Occupancy not healthy until 2013
- Risk of underutilized space dampening absorption during recovery

### Retail hardest hit

- US consumption growth negative in 2008, first time since 1990
- Consumption expected below long term averages for several years
- Weak retailers have or will liquidate
- New store openings slow to resume
- Discounters performing better than upscale stores
- Neighborhood/community grocery anchored centers are favored

*This information is a forecast and due to a variety of uncertainties, and assumptions made in our analysis, actual events or results or the actual performance of the markets covered may differ from those presented.*

## For Real Estate, Recovery not Expected to Start Until 2011

- 2010 expected to be the trough for most property sectors.
- Recovery expected to begin in 2011 with modest rent growth.

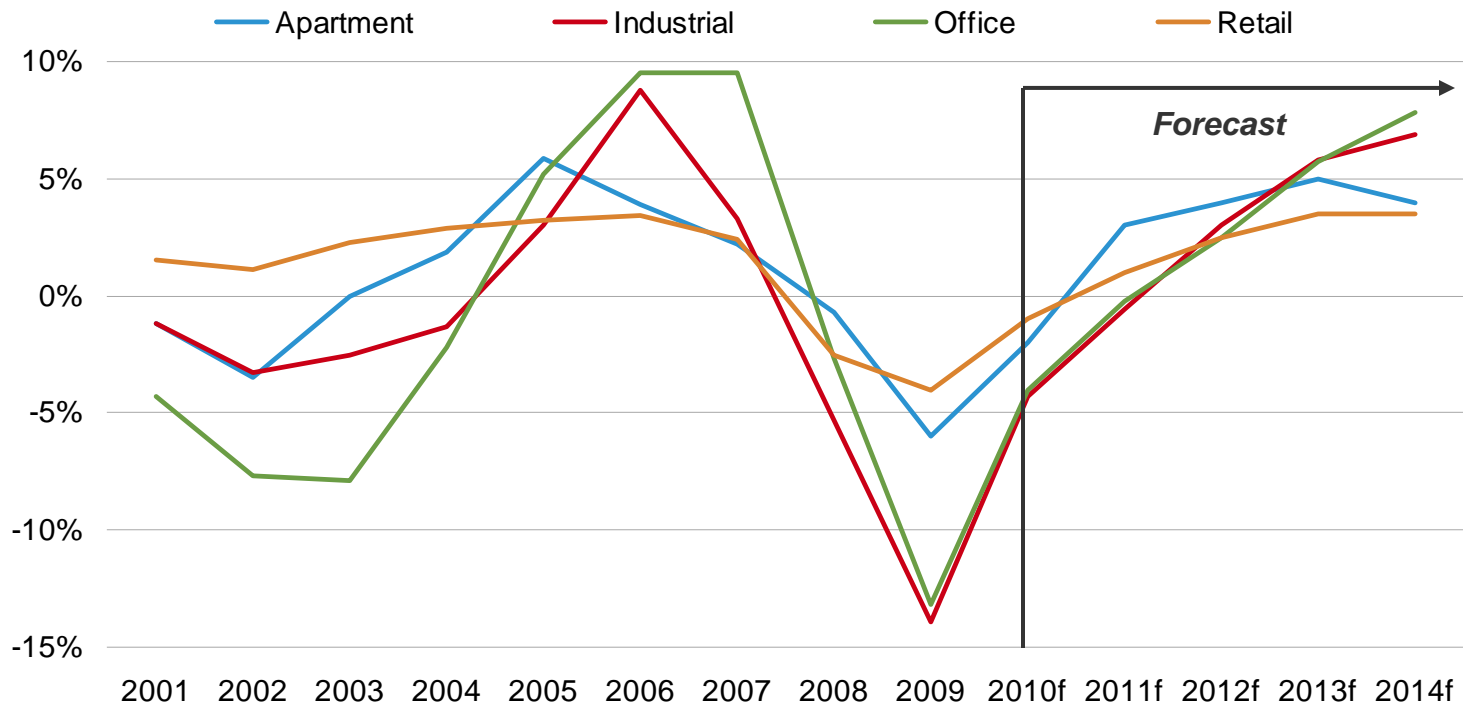
National Vacancy Rate Trends								
	2007	2008	2009	Forecast 2010	Forecast 2011	Forecast 2012	Forecast 2013	Forecast 2014
Apartment	5.7%	6.7%	8.3%	8.6%	7.5%	6.2%	5.6%	5.5%
Industrial	9.4%	11.3%	14.0%	14.4%	13.4%	11.9%	10.8%	10.2%
Office	12.6%	14.0%	17.3%	18.5%	17.8%	15.9%	14.0%	13.1%
Retail	7.2%	8.7%	10.4%	10.9%	10.5%	9.8%	9.1%	8.3%

Forecasts are of the market and not of a RREEF product.  
Sources: REIS Reports, CBRE-EA, RREEF Research.  
As of December 2009.

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## U.S. Average Rent Growth by Sector, 2001 – 2014

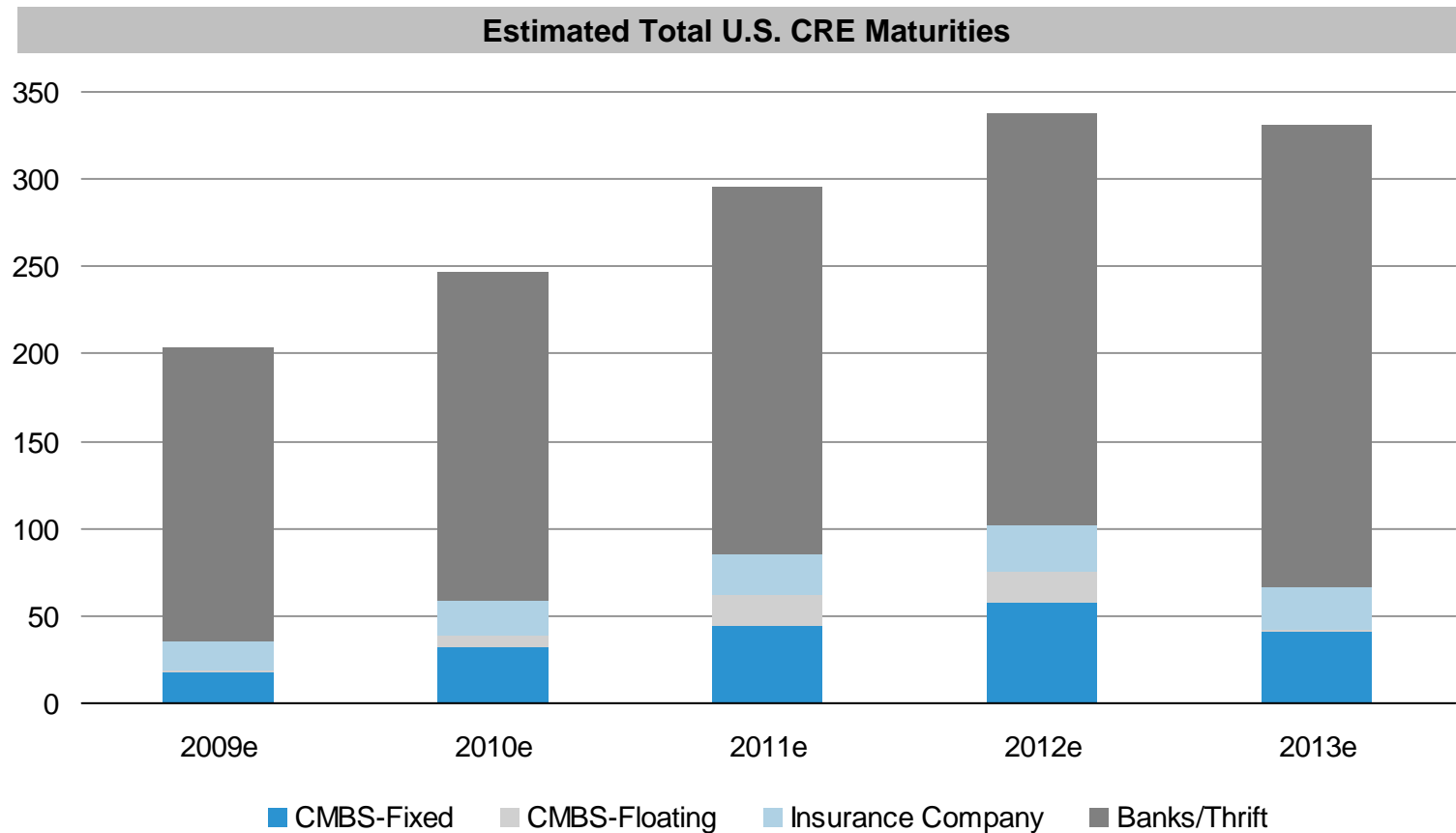


Source: Axiometrics, CBRE-EA, REIS, Torto Wheaton, RREEF Research  
As of December 2009.

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## U.S. Commercial Real Estate and CMBS Refinancing is a Big Risk



*This information is a forecast and due to a variety of uncertainties, and assumptions made in our analysis, actual events or results or the actual performance of the markets covered may differ from those presented.*

*Source: Deutsche Bank, Intex, Trepp, Mortgage Bankers Association, Federal Reserve.*

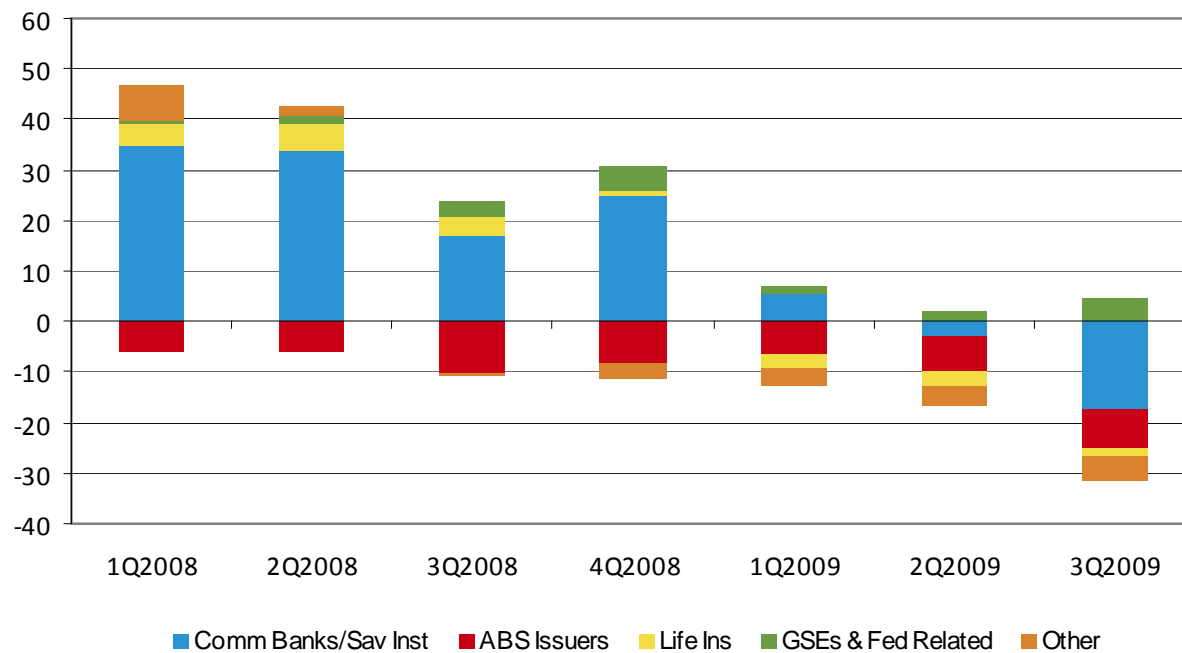
*As of August 2009.*

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## CRE Debt Issuance has been in Free-fall

Quarterly Change in US CRE Mortgage Debt by Lender (USD, Bn)

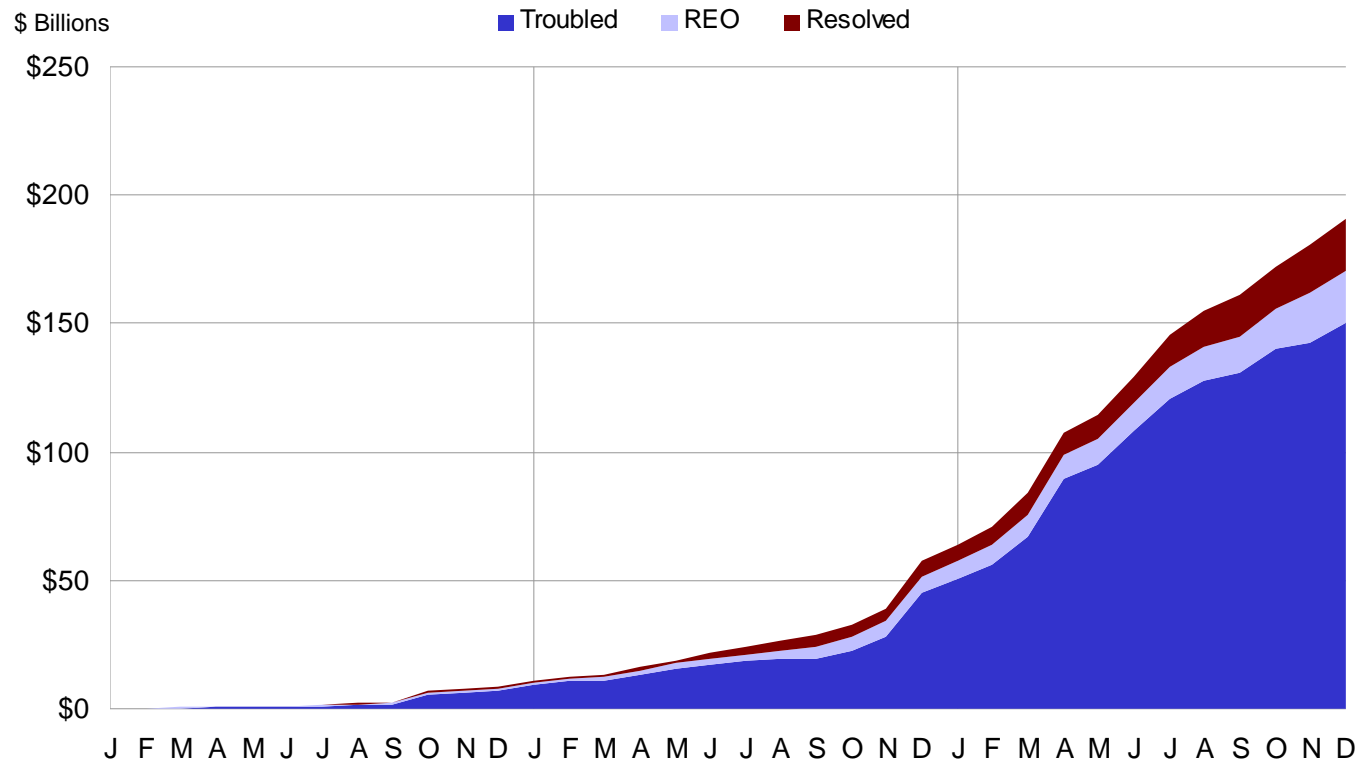


Source: Federal Reserve Flow of Funds  
Released on December 10, 2009.

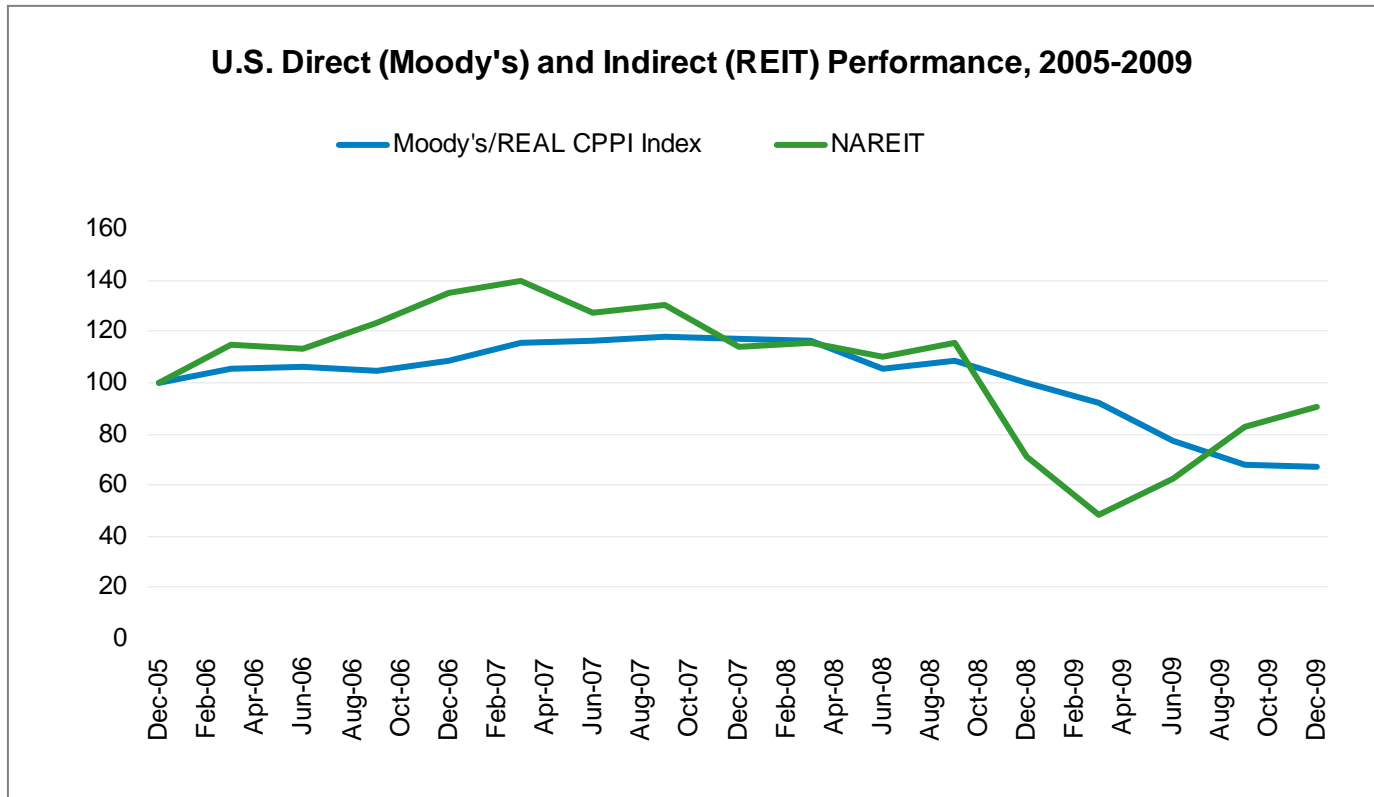


## Distressed CRE Debt is Spiking!

Monthly Cumulative Distress across U.S. Markets by Property Type, 2007-2009



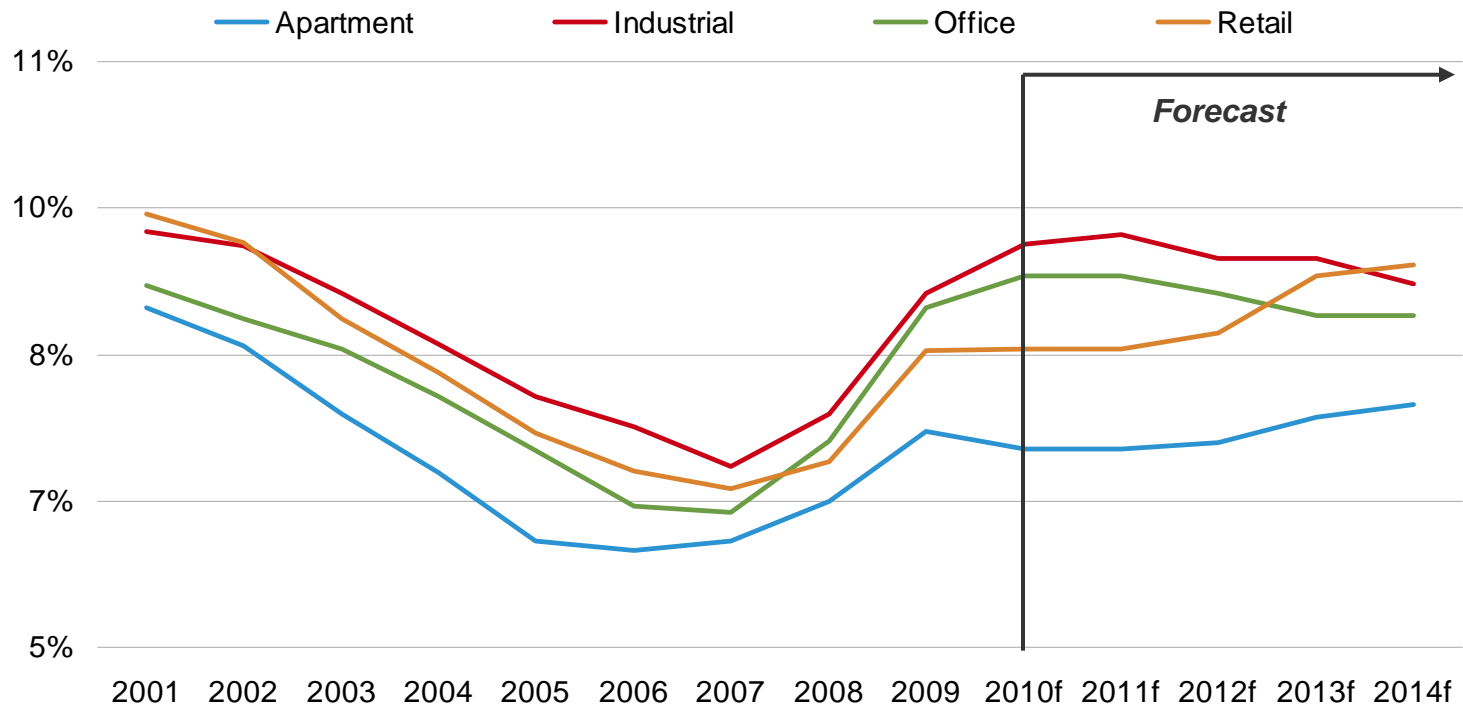
## Public Markets are Forecasting a Rebound in Commercial Real Estate



Returns indexed at 100 as of December 31, 2005.



## U.S. Average NCREIF Cap Rates by Sector, 2001 – 2014



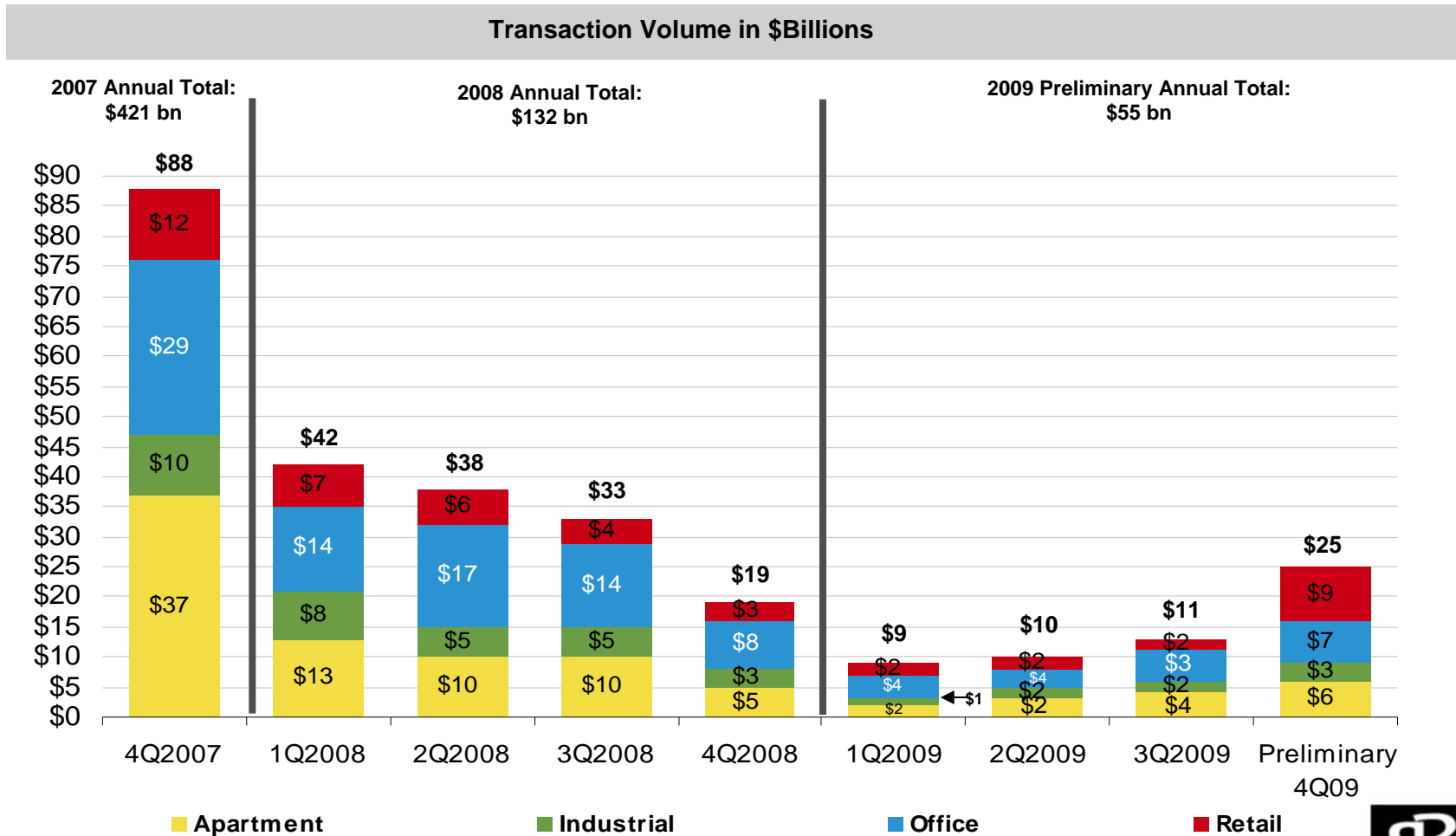
f=Forecast

Source: CBRE-EA, PMA, Torto Wheaton, RREEF Research  
As of December 2009.

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## Quarterly Transaction Volumes: 4Q2007 – Preliminary 4Q2009



Source: Real Capital Analytics.

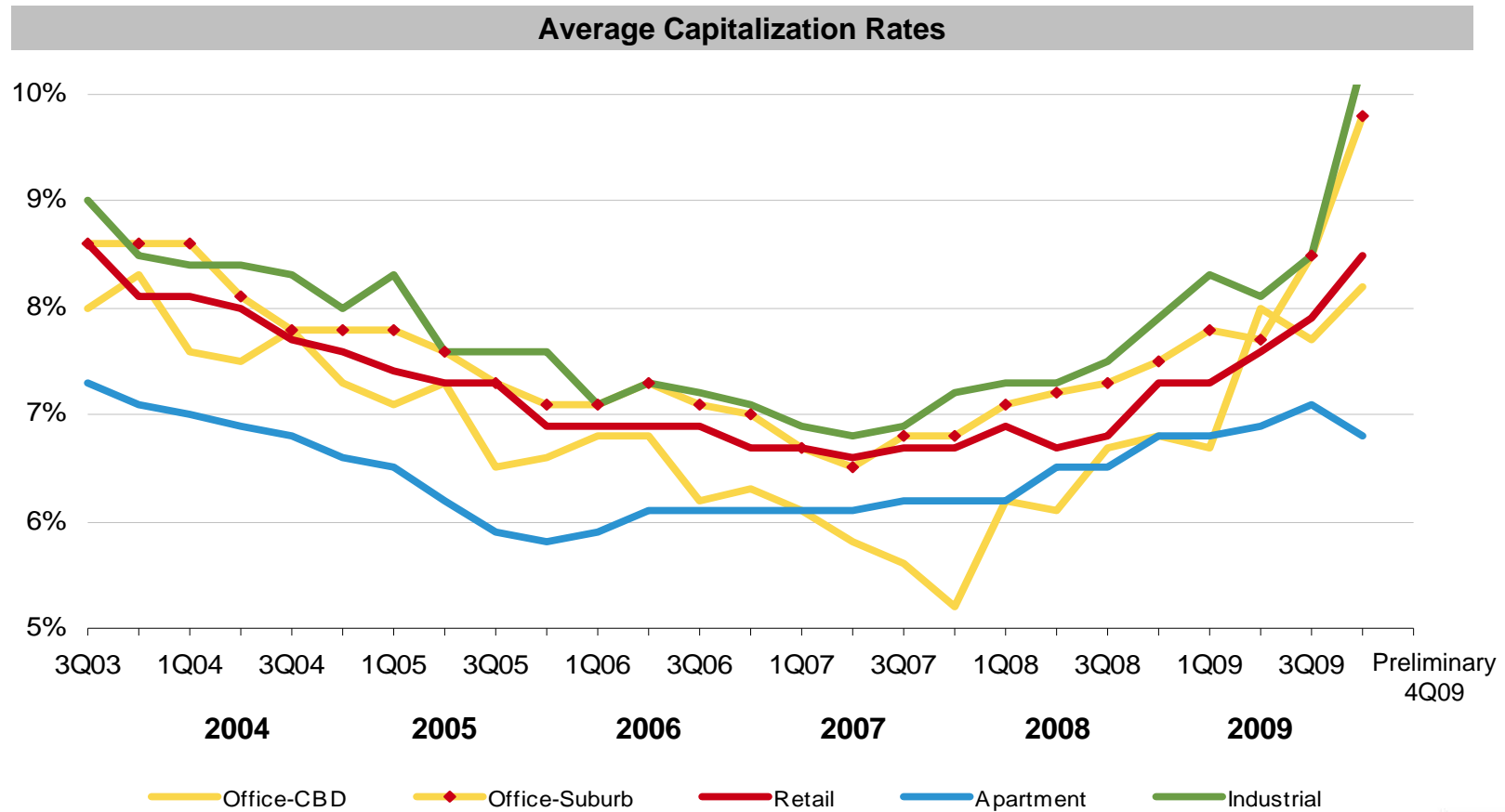
Preliminary as of December 31, 2009.

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## Capitalization Rate Trends: Modest Increase in 2007- 2009

But Cap Rates Are Adjusting ... and spreads on equity returns are increasing for Real Estate



Source: Real Capital Analytics and RREEF Research.  
Preliminary as of December 31, 2009.



## Property Values Have Already Fallen Further than in the 2000's Recession, But Still Less than in the 1990's

1990's					
	Total	Apartments	Industrial	Office	Retail
Appreciation	-32.3%	-16.7%	-33.7%	-50.2%	-26.4%
No. of Quarters	23	14	19	38	27
Dates	1Q1990 – 4Q1995	2Q1990 – 3Q1993	4Q1989 – 3Q1994	4Q1987 – 4Q1995	3Q1990 – 2Q1997

2000's					
	Total	Apartments	Industrial	Office	Retail
Appreciation	-3.5%	-0.3%	-3.7%	-10.5%	-2.7%
No. of Quarters	6	1	7	9	6
Dates	3Q2001 – 1Q2003	4Q2001	3Q2001 – 2Q2003	3Q2001 – 4Q2003	3Q2000 – 1Q2002

Late-2000's					
	Total	Apartments	Industrial	Office	Retail
Appreciation	-28.2%	-28.7%	-28.9%	-30.6%	-22.5%
No. of Quarters	6	6	6	6	6
Dates	2Q2008 – 3Q2009	2Q2008 – 3Q2009	2Q2008 – 3Q2009	2Q2008 – 3Q2009	2Q2008 – 3Q2009

Source: NCREIF.  
As of September 30, 2009.

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## Office and Retail Likely to be Hit Worst, Industrial to Recover Most Quickly

- Substantial valuation adjustments in 2009.
- Valuation declines forecast to exceed that of early 1990s.

Property Type	Apartment	Industrial	Office	Retail	Total
<b>Actual NPI Total Return</b>					
2008	-7.3%	-5.8%	-7.3%	-4.1%	-6.5%
<b>Forecast NPI Total Return</b>					
2009	-18% to -16%	-18% to -16%	-21% to -18%	-16% to -12%	-18% to -16%
2010	2% to 4%	2% to 4%	-5% to 0%	-4% to 0%	-2% to 2%
<b>Peak to Trough Appreciation Returns for current cycle (Peak – Trough)</b>					
	-40% to -36% (2Q08 – 1Q10)	-42% to -38% (1Q08 – 2Q10)	-52% to -48% (2Q08 – 2Q10)	-44% to -40% (2Q08 – 3Q11)	-45% to -40% (2Q08 – 2Q10)

Sources: RREEF Research and NCREIF (for history).  
As of October 31, 2009.

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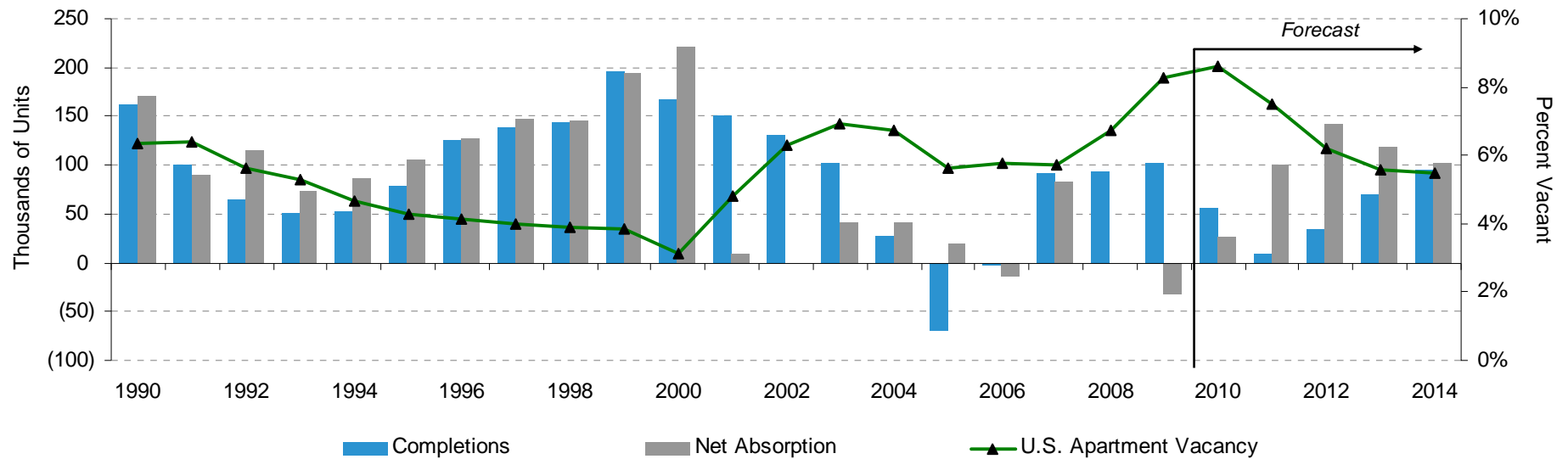
Private Equity

## Section III

# Apartment Sector Outlook

## Apartments: The Worst is Past – Early Recovery in Core Markets

U.S. Apartment Supply and Demand, 1990-2014

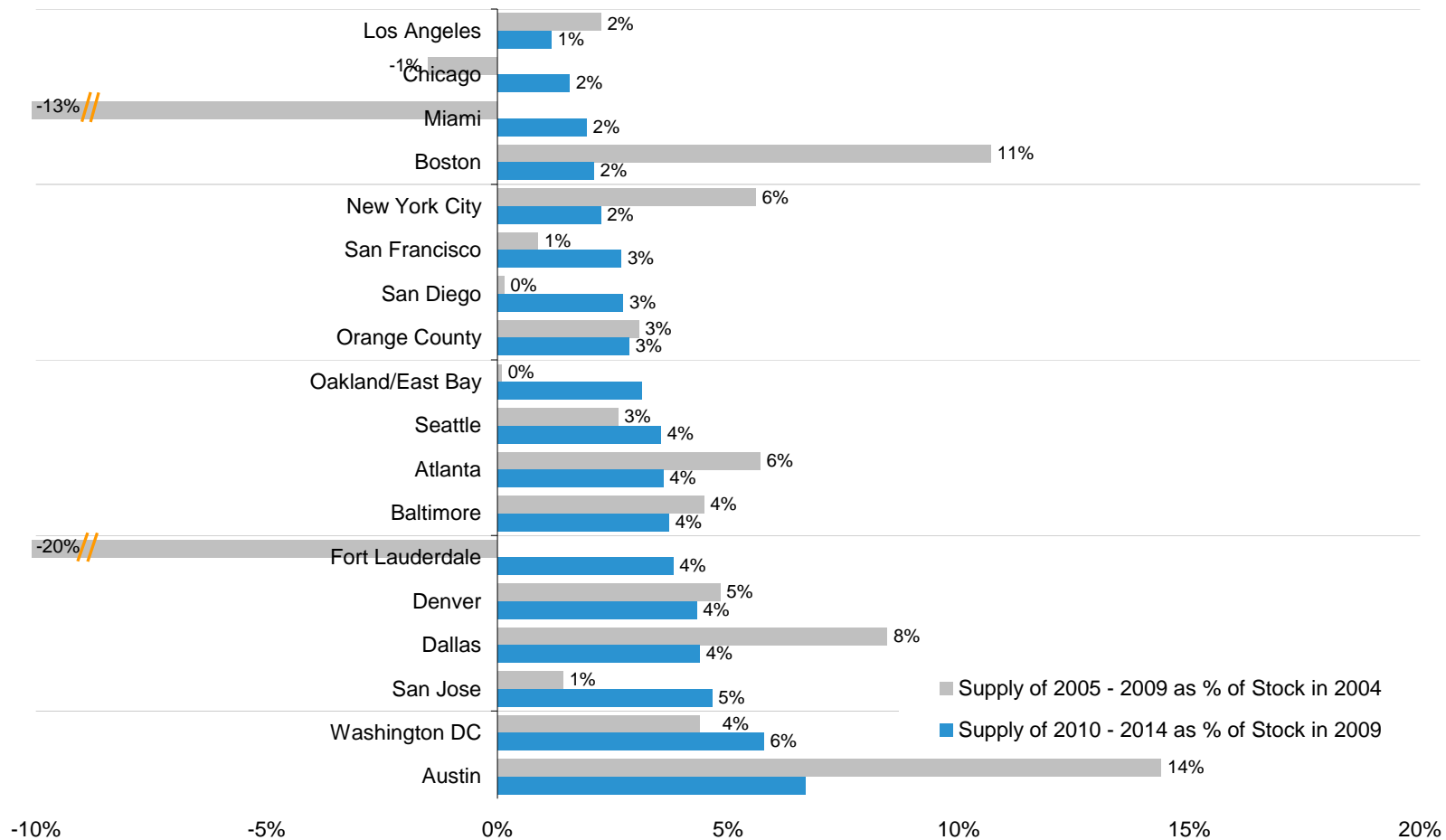


Source: RREEF Research, REIS  
As of December 2009.



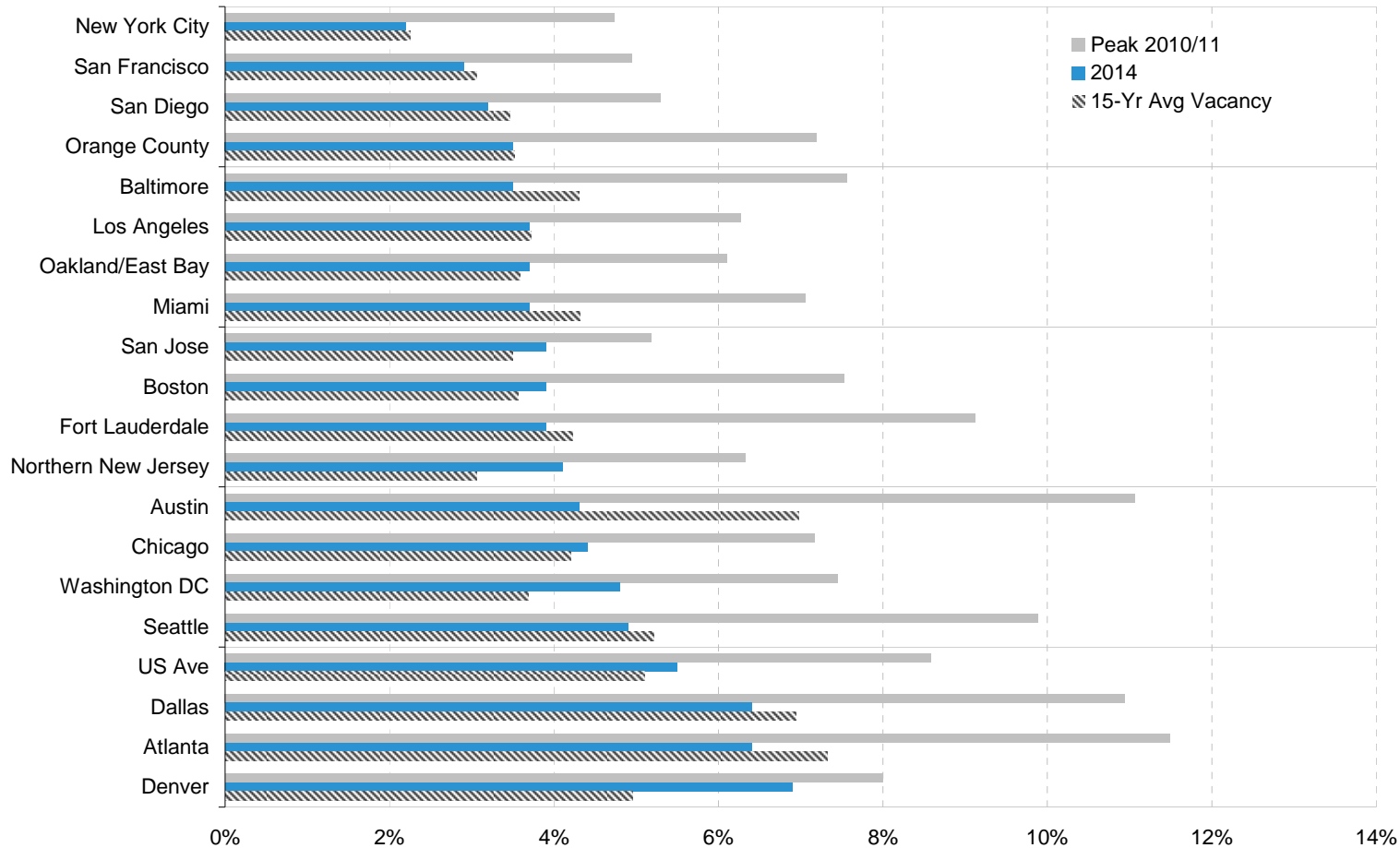
## Apartments: The Sector Where Supply Has Accelerated

Apartment Supply as % of Stock, 2010 - 2014



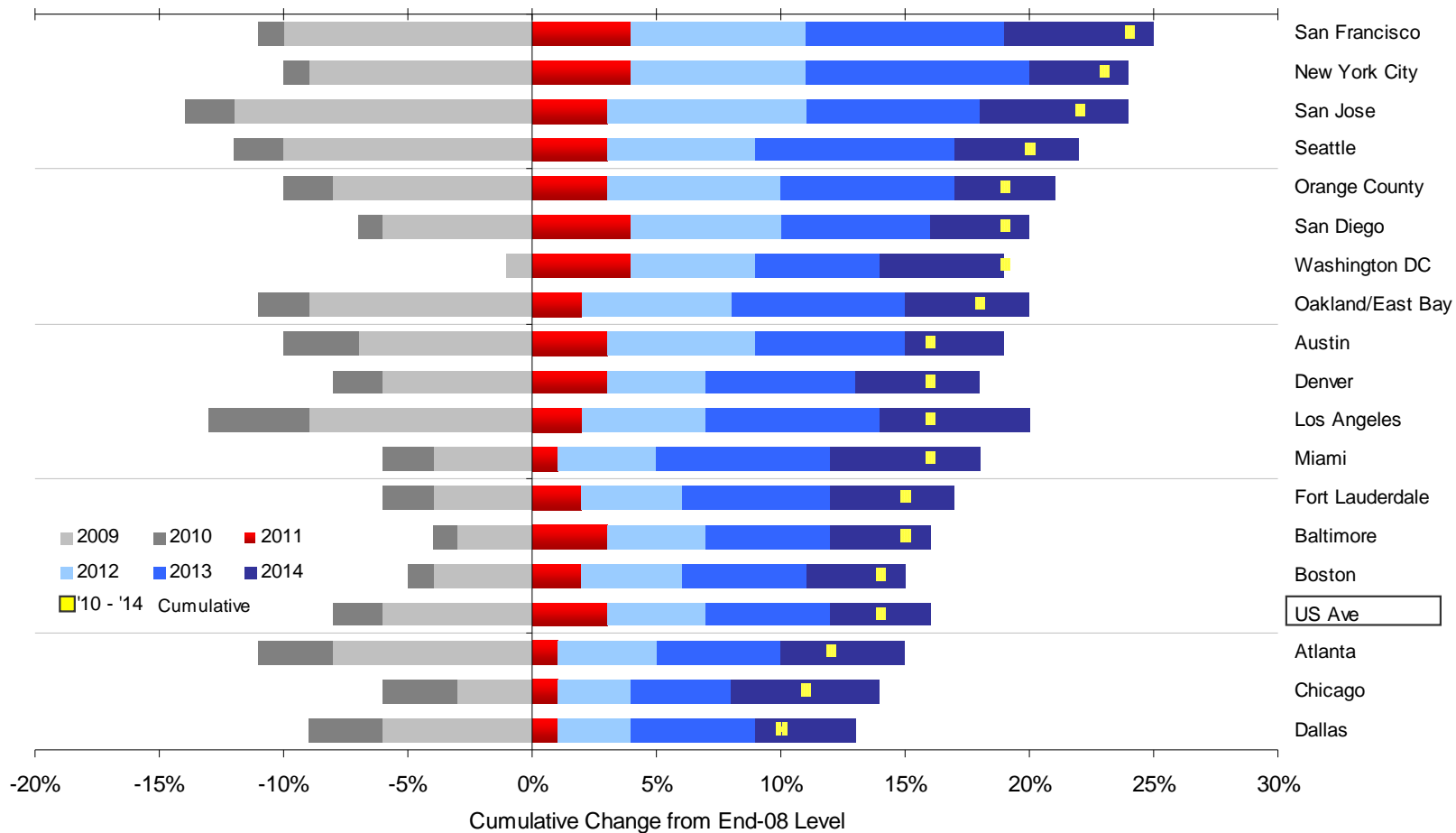
## Apartments: Vacancy Rates Will Approach Historic Norms in 2014

### U.S. Apartment Vacancy Rates



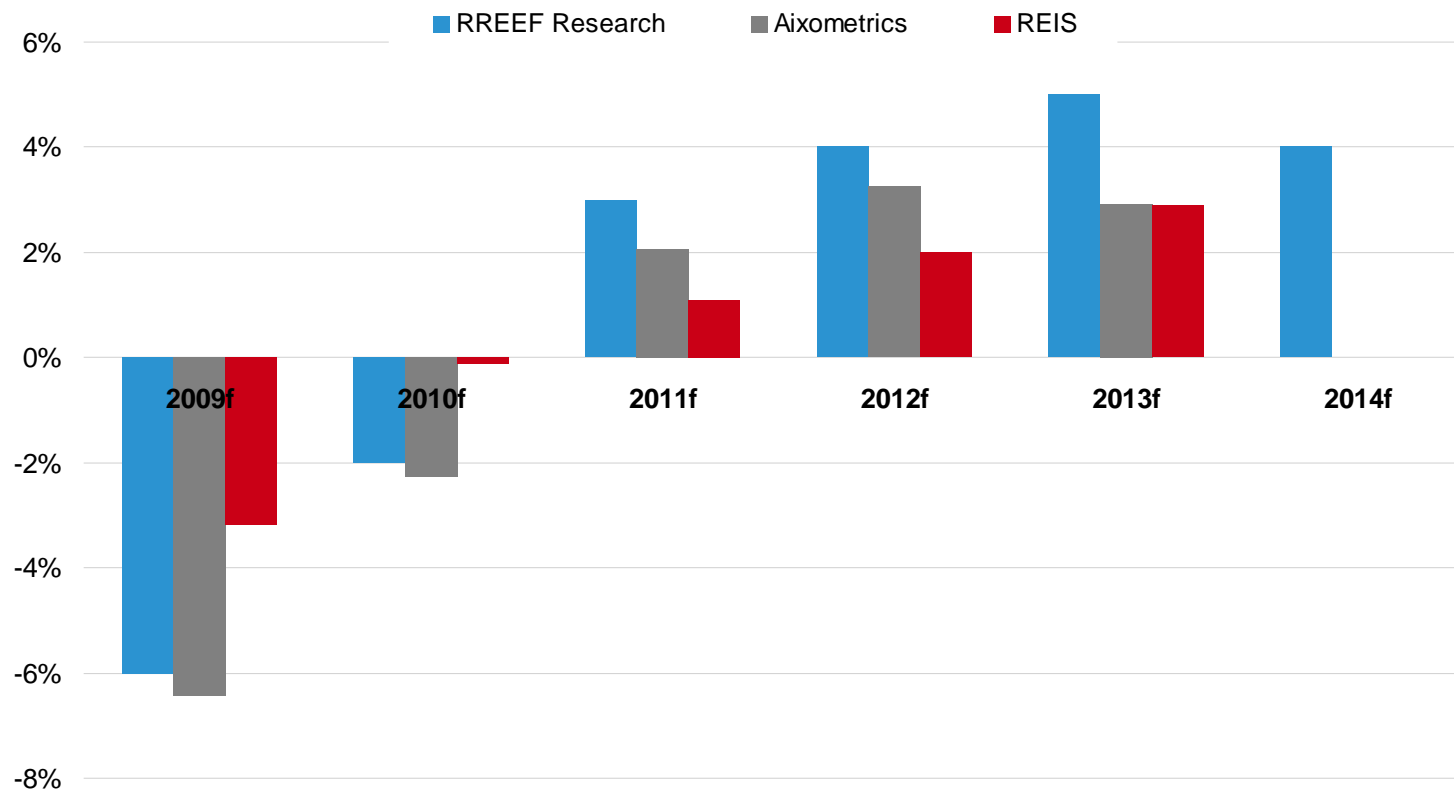
## Apartments: Rents Stabilize in 2010 and then Turn Positive

Apartment Cumulative Rental Growth Rate (%), 2010-2014



## Apartments: RREEF Research Optimistic on Apartment Recovery

Average Apartment Rental Growth Comparison 2009-2014f

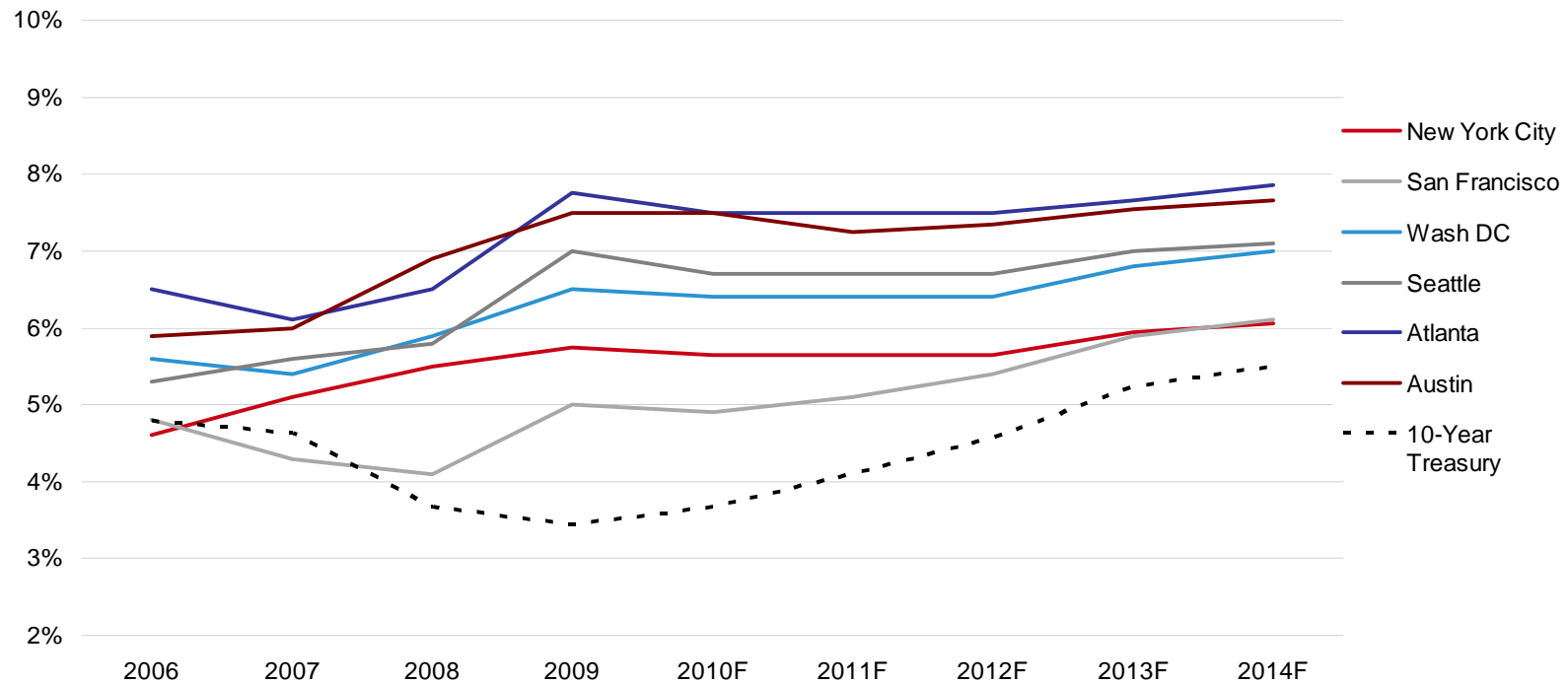


f = Forecast  
 Source: RREEF Research  
 As of December 2009.



## Apartments: Cap Rates Stabilizing Due to Better Fundamentals and Agency Debt

Metro Apartment Cap Rates 2001-2014f

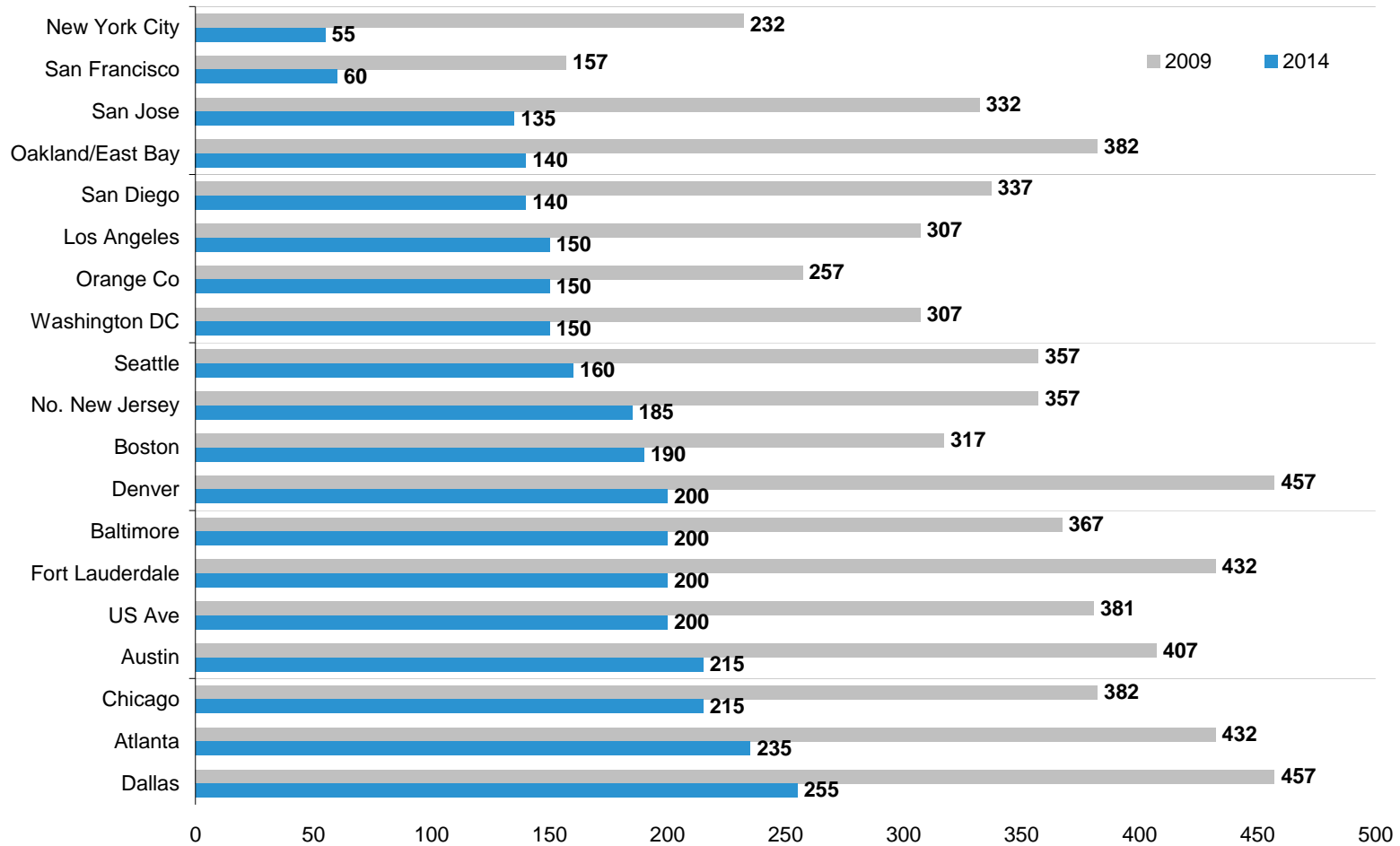


f = Forecast  
 Source: CBRE-EA  
 As of December 2009.

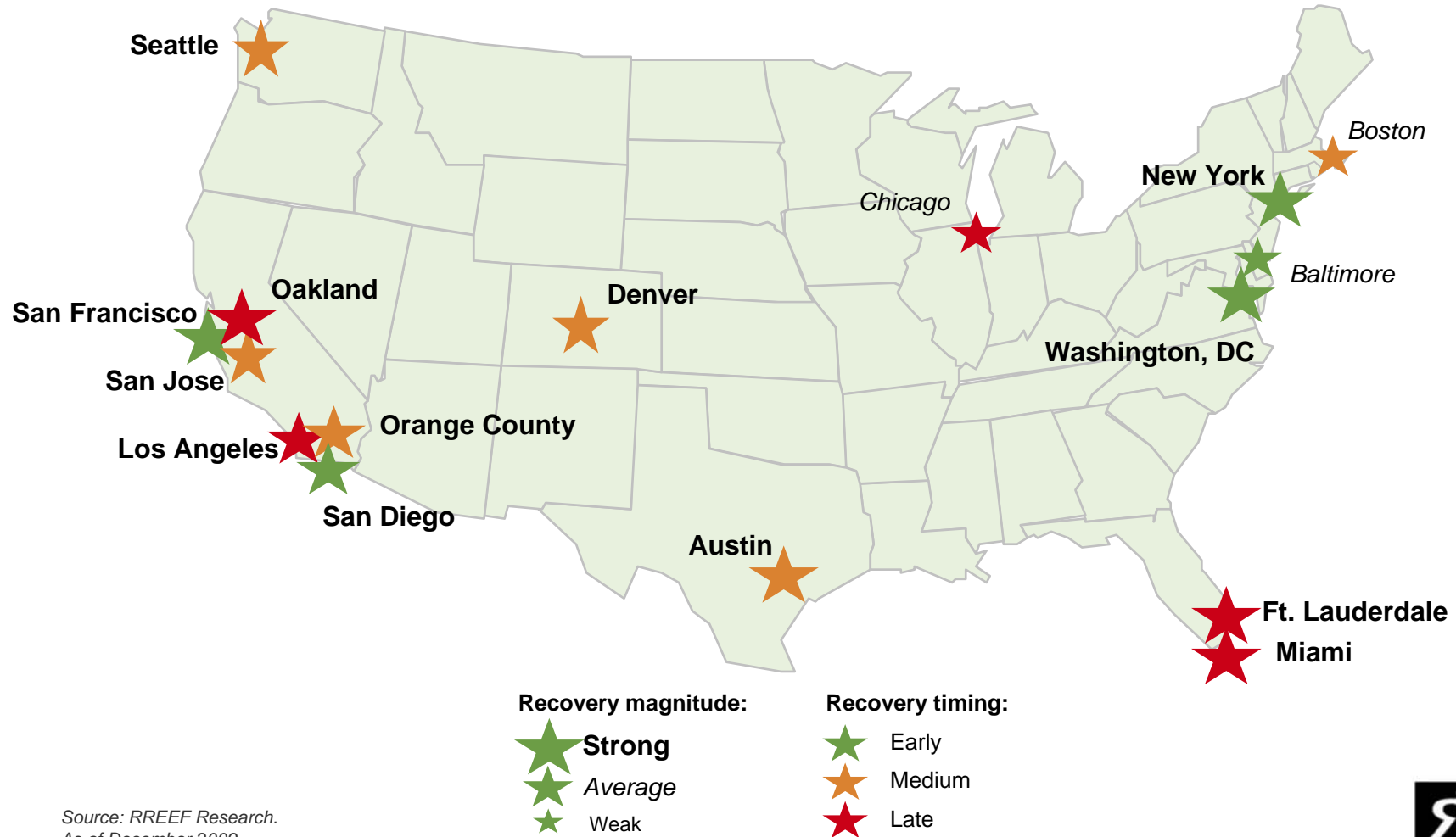


## Apartments: Cap Rate to T-Bill Spread Forecast to Compress

**Apartments Yield Spread, 2009 - 2014**



## RREEF Target Apartment Investment Markets



Source: RREEF Research.  
As of December 2009.





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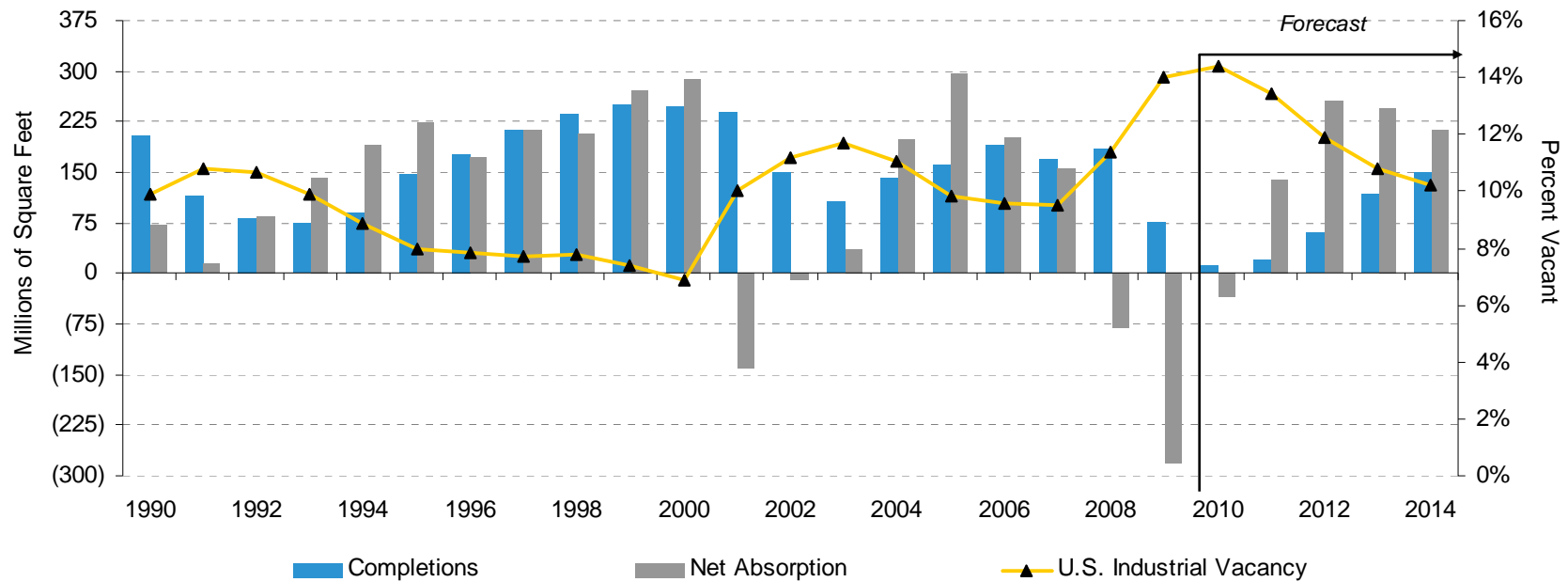
Private Equity

## Section IV

# Industrial Sector Outlook

## Industrial: Weak through 2010, then Recovery with Supply Gap and Occupancy Gain

U.S. Industrial Supply and Demand, 1990-2014

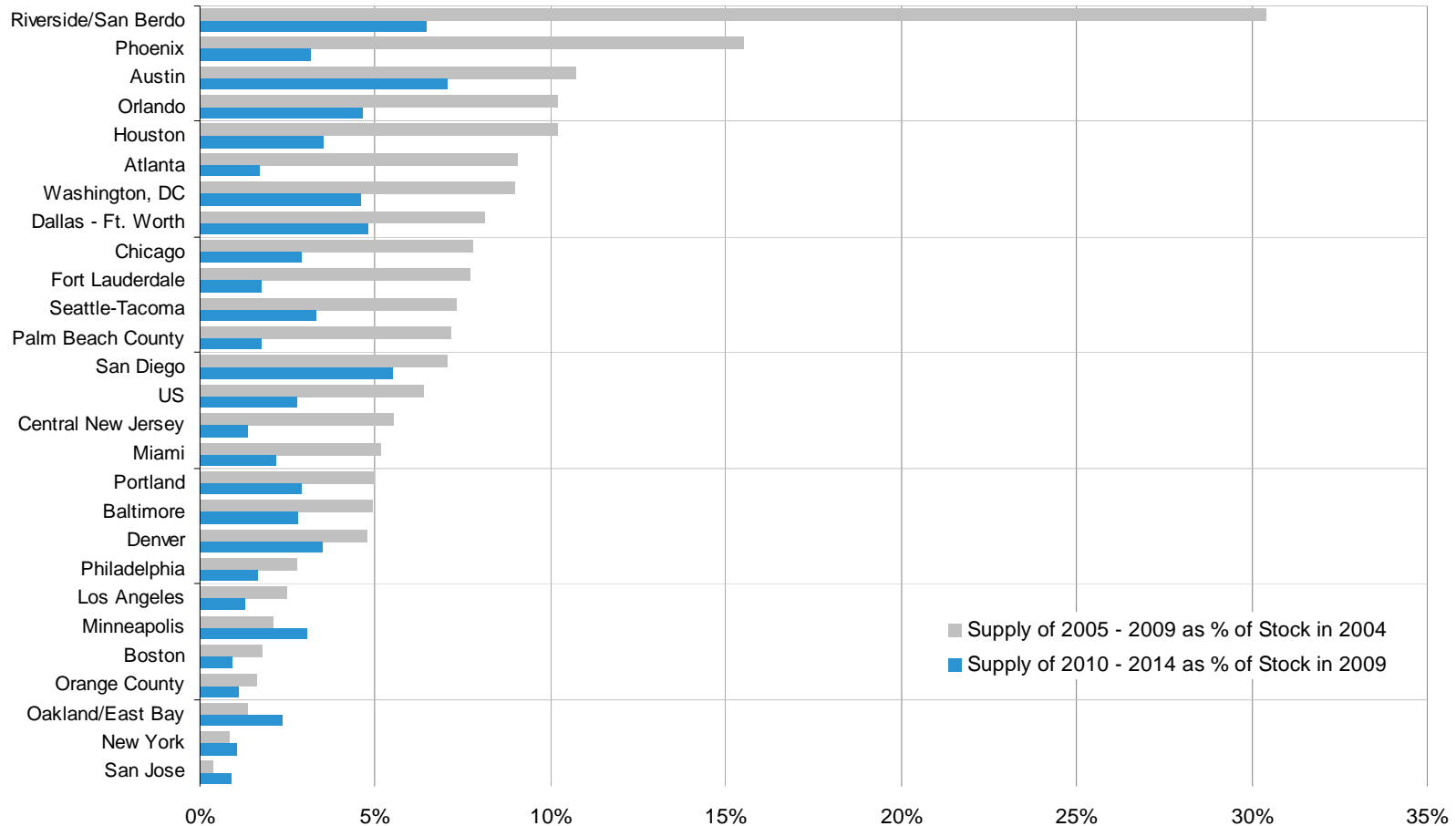


Source: RREEF Research, CBRE-EA.  
As of December 2009.



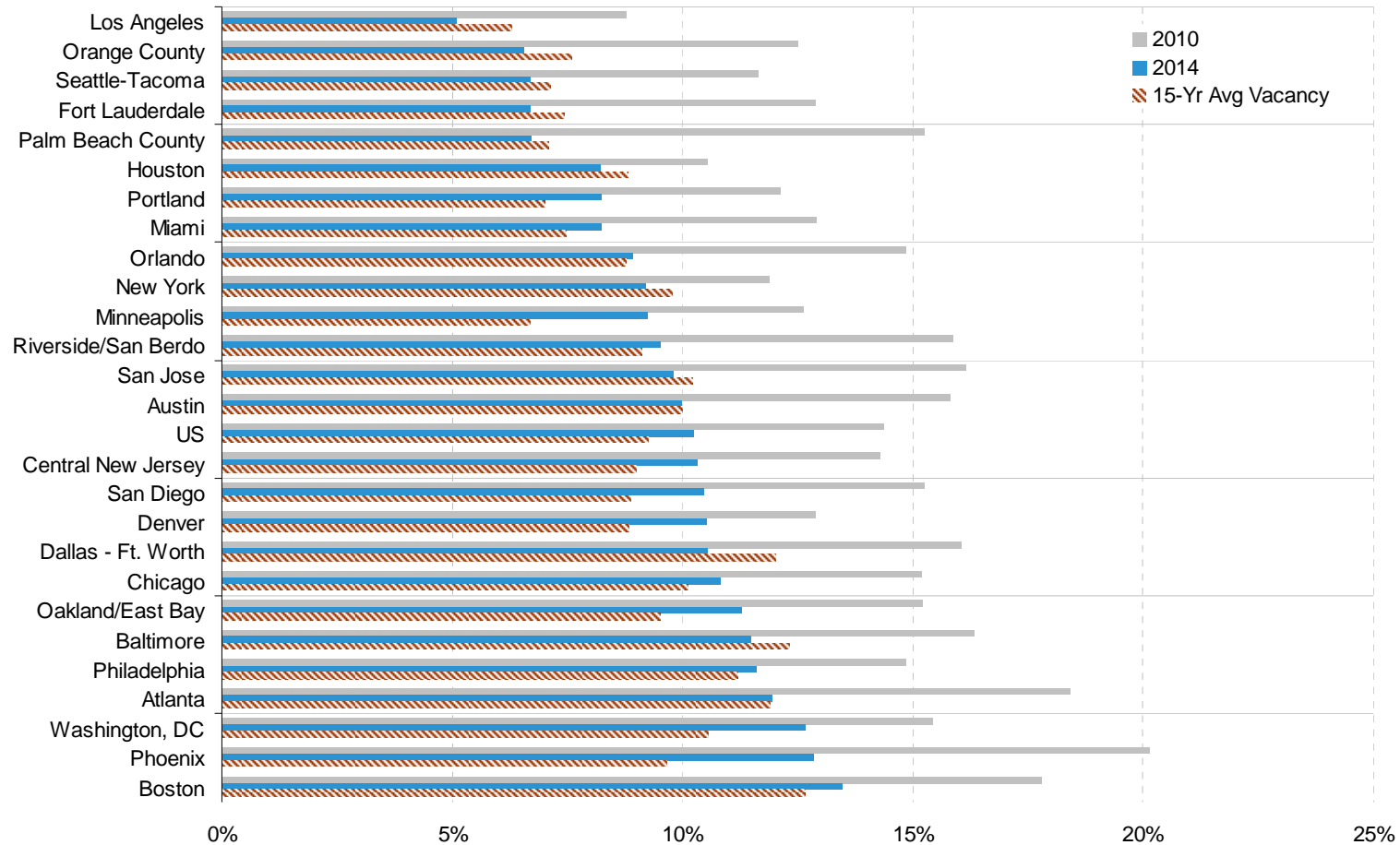
## Industrial: All Markets will Have Protracted Fall-Off in Supply

Industrial Supply as % of Stock, 2010 - 2014



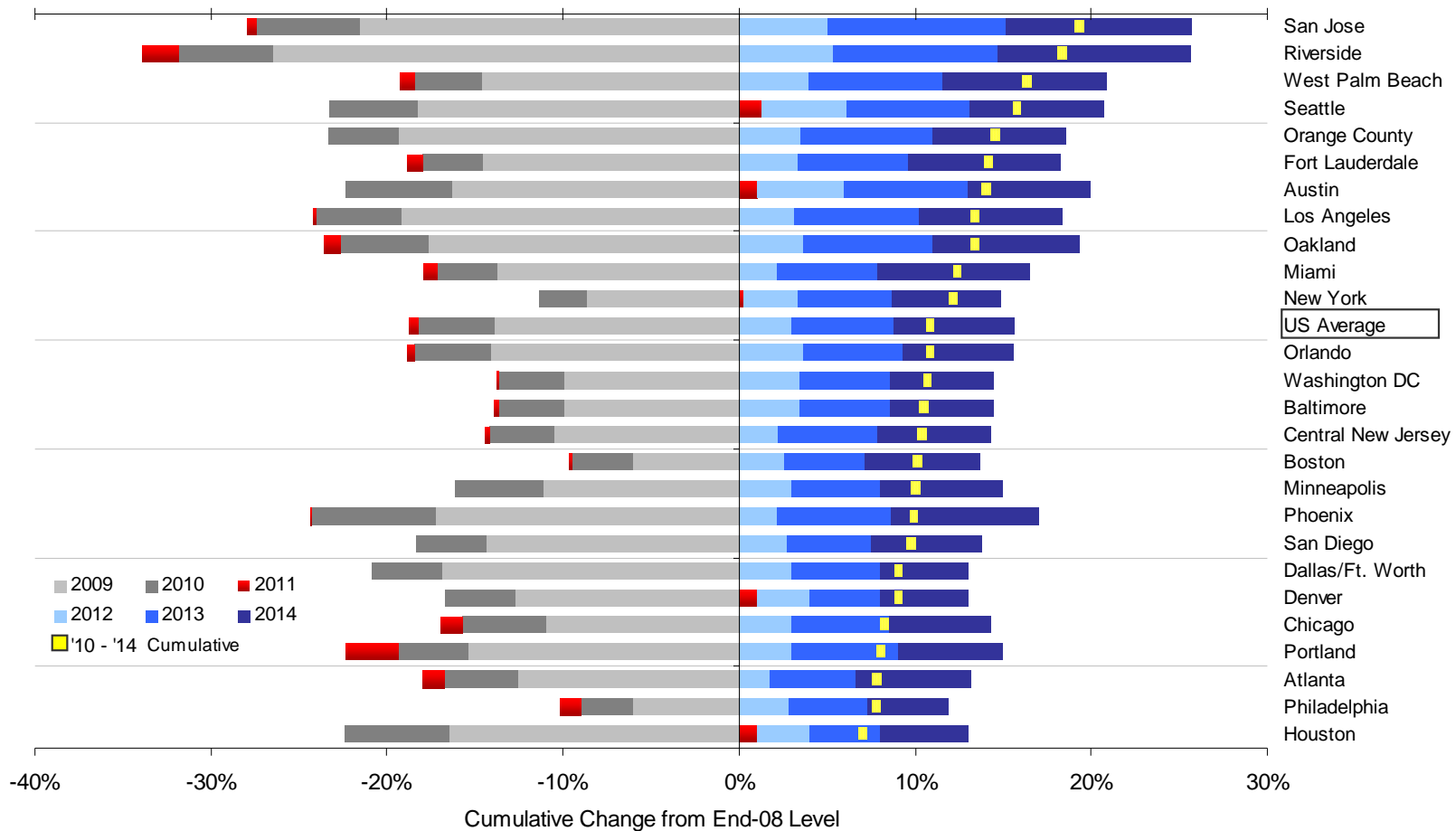
## Industrial: Renewed Demand in 2012 Feed into Occupancy Gains

### U.S. Industrial Vacancy Rates

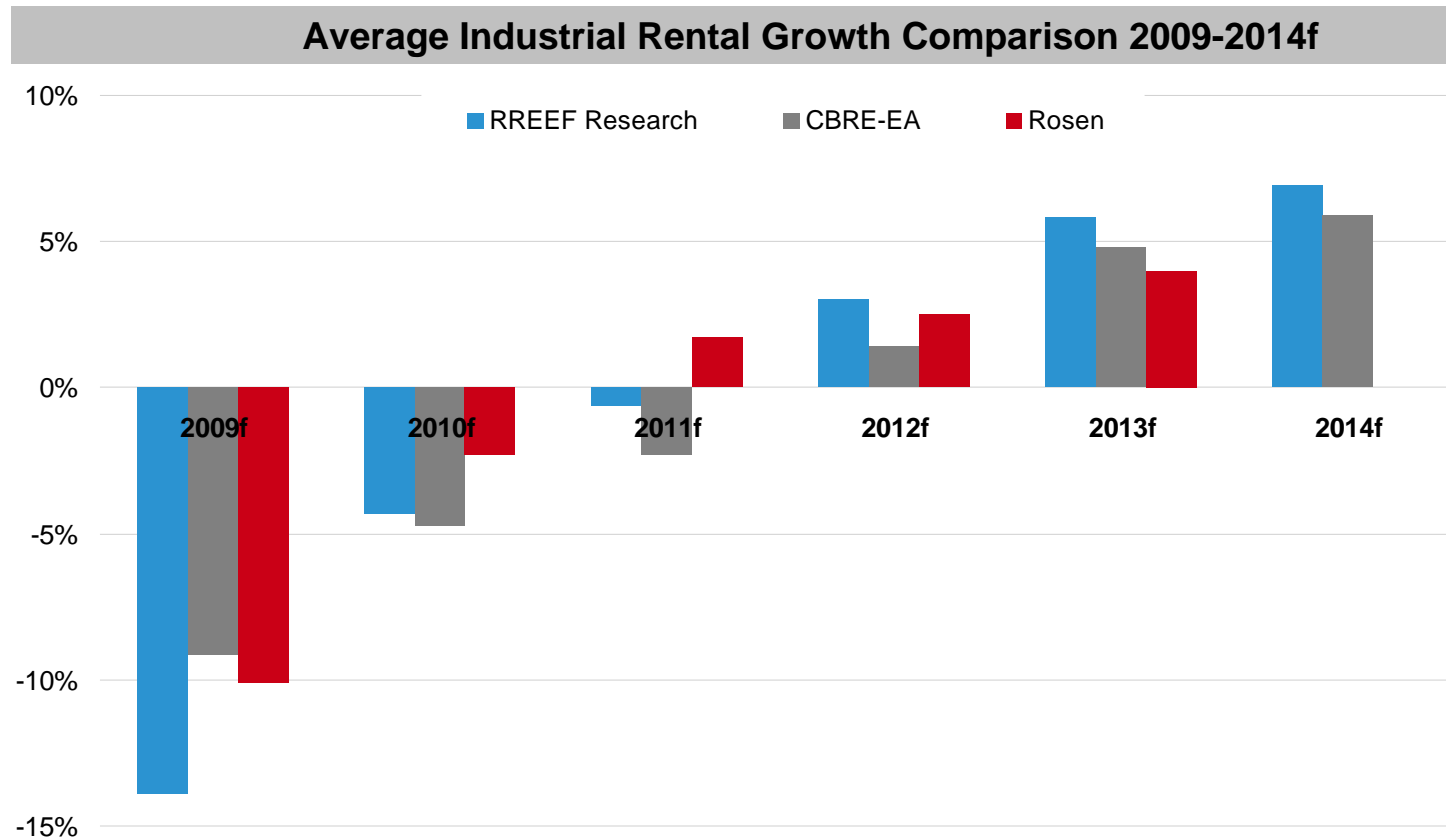


## Industrial: Strong Out-Years, but Full Rent Recovery Incomplete in Year Five

Industrial Cumulative Rental Growth Rate (%), 2010-2014



## Industrial: RREEF Measures Greater Declines and Stronger Rent Recovery

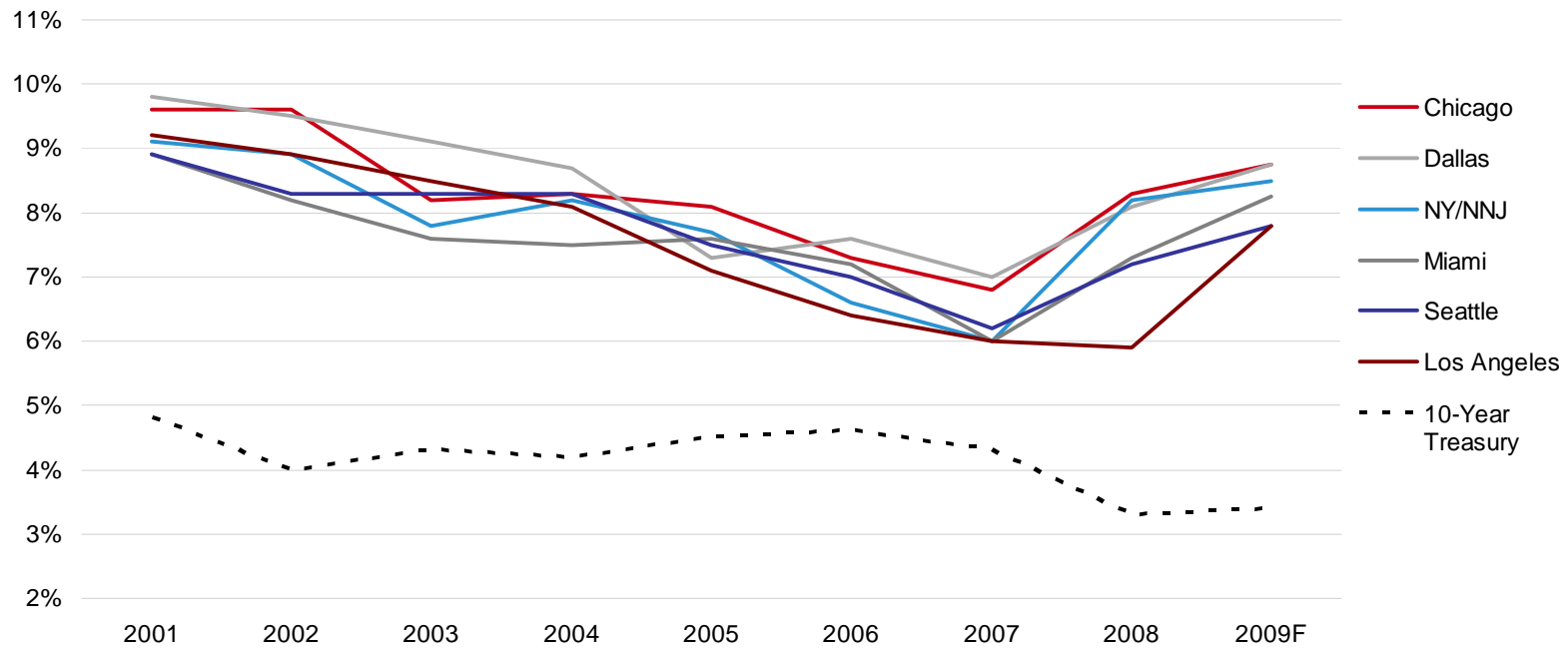


f = Forecast  
 Source: RREEF Research  
 As of December 2009.c



## Industrial: Cap Rate Correction Started Much Earlier Than Other Sectors

Metro Industrial Cap Rates 2001-2009

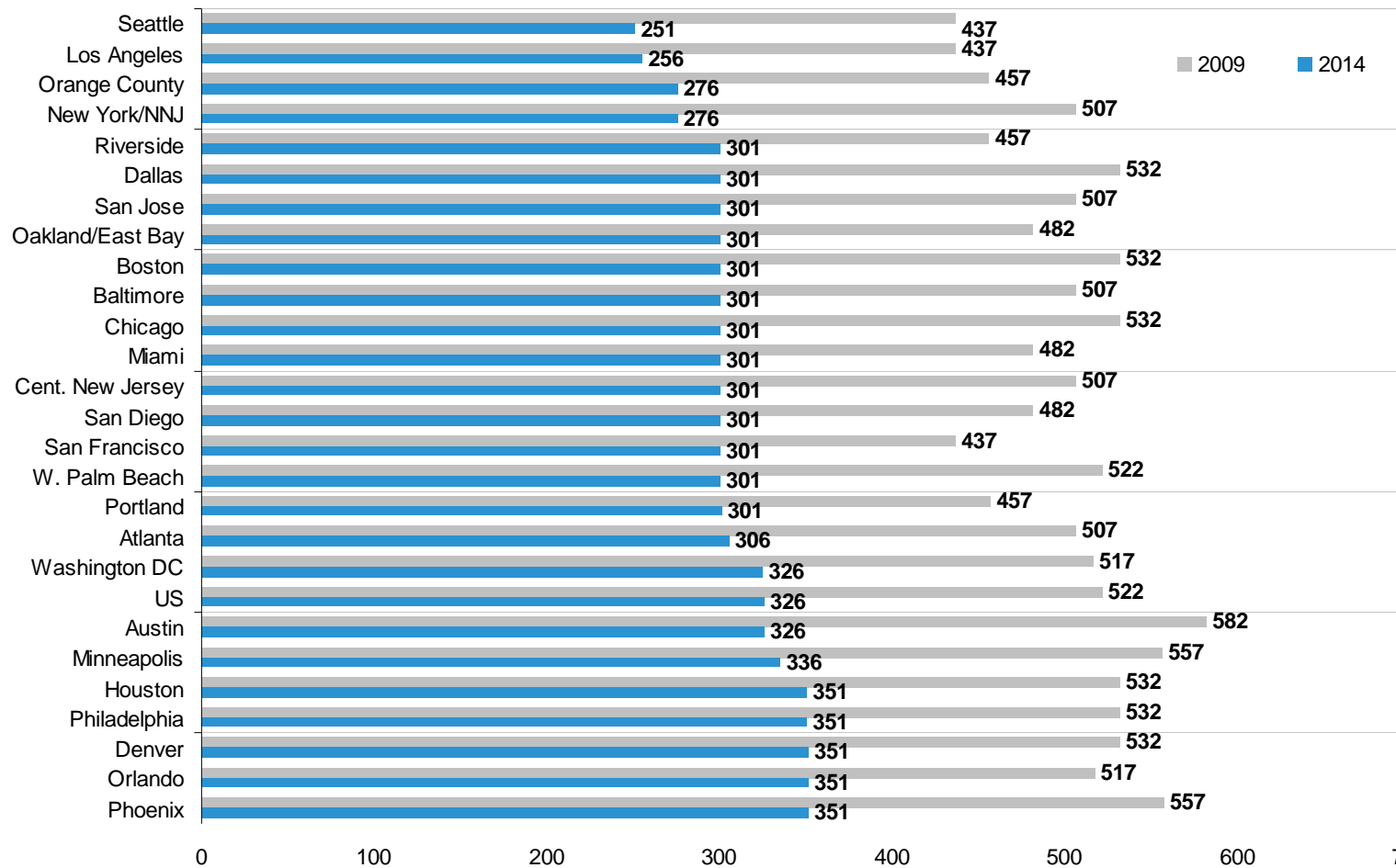


Source: CBRE-EA  
As of December 2009c



## Industrial: Three Tiers in Outlook with Preferred Markets at 300 bps or Less

Industrial Yield Spread, 2009 - 2014



## RREEF Target Industrial Investment Markets



Recovery magnitude:

- ★ Strong
- ★ Average
- ★ Weak

Recovery timing:

- ★ Early
- ★ Medium
- ★ Late

Source: RREEF Research.  
As of December 2009.





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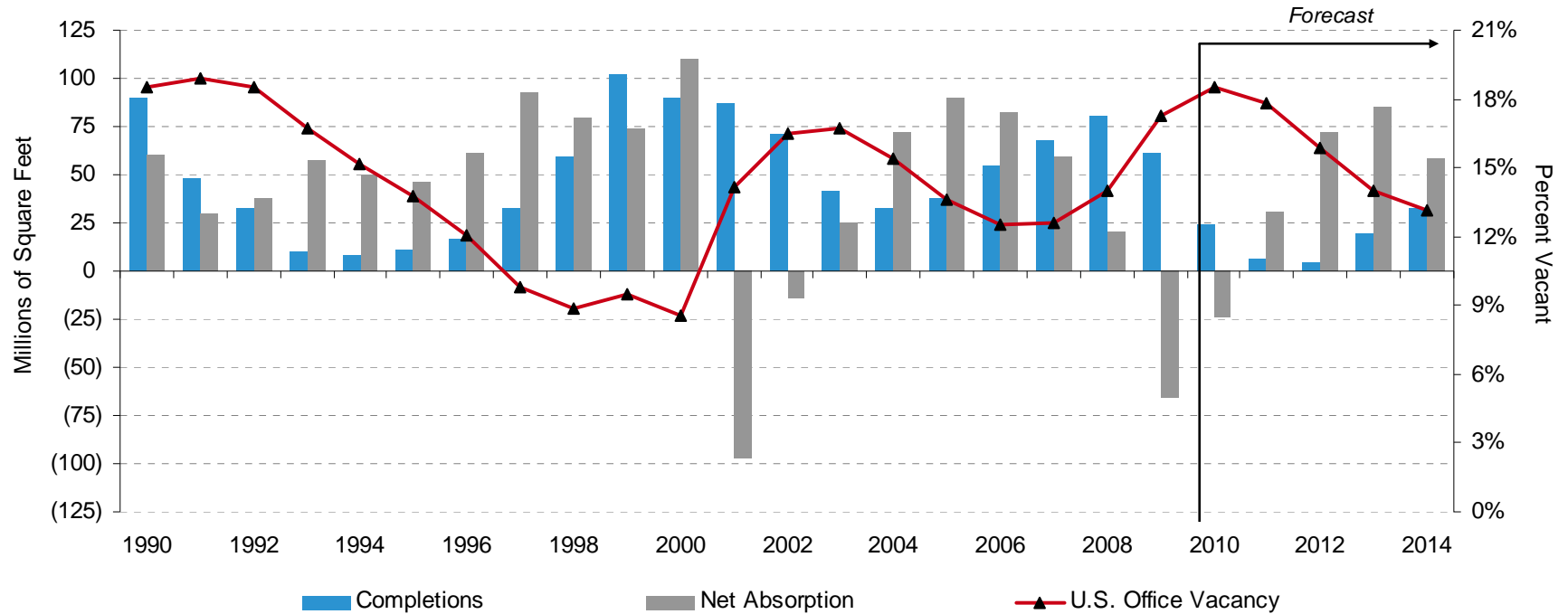
Private Equity

## Section V

### Office Sector Outlook

## Office: Mid-term at Risk with Weak Job Recovery

U.S. Office Supply and Demand, 1990-2014

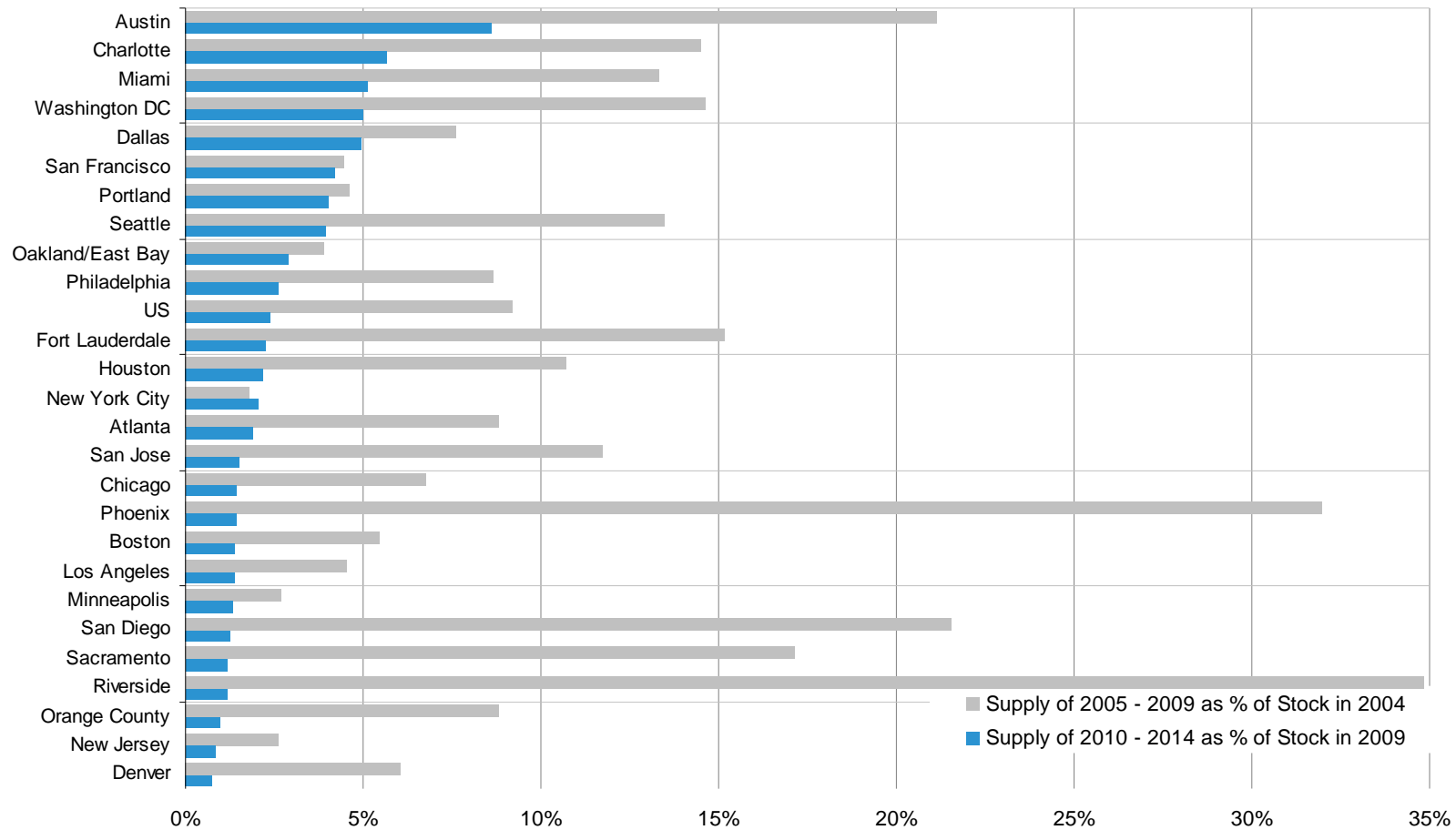


Source: RREEF Research, CBRE-EA  
As of December 2009.

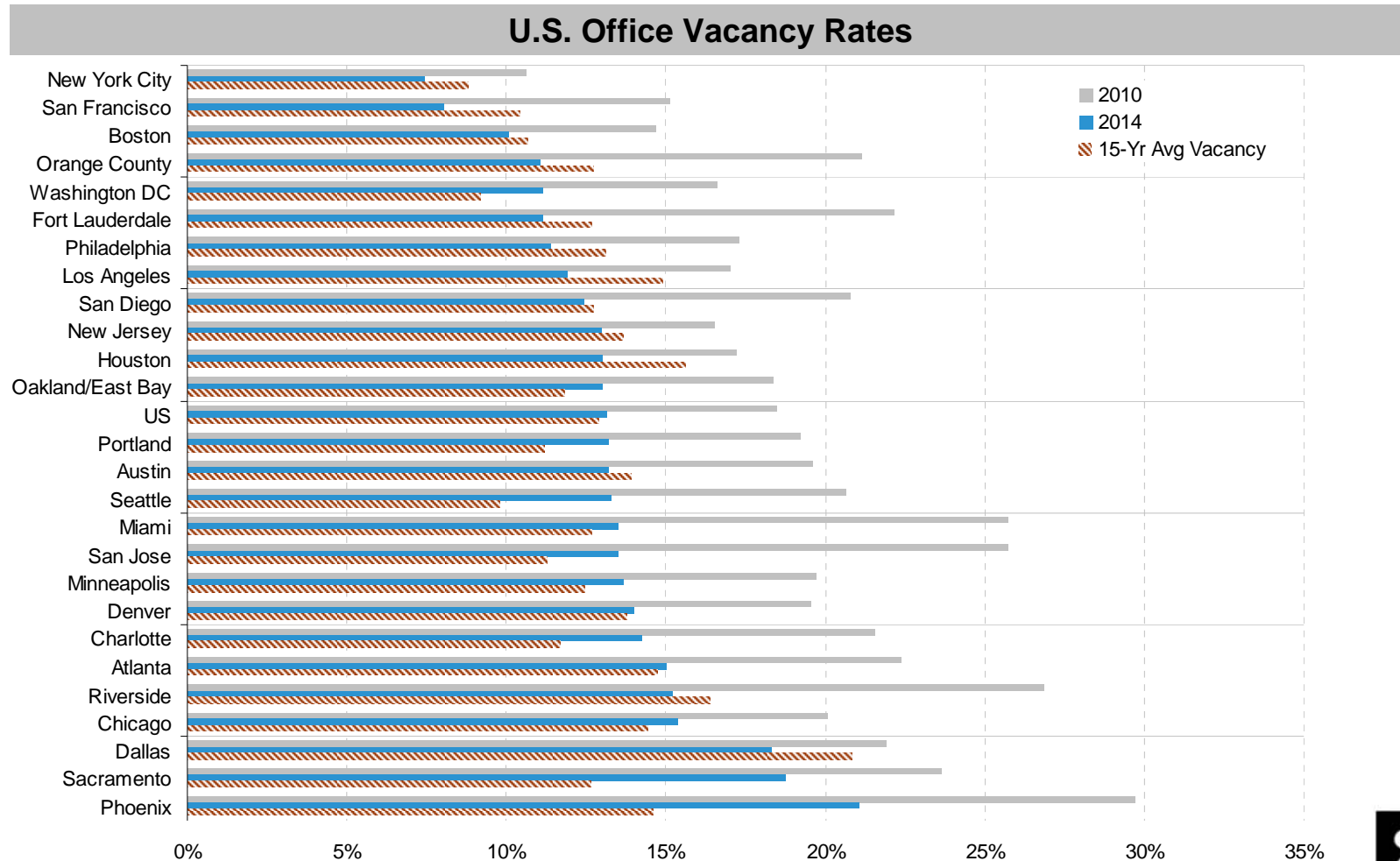


## Office: Future Supply Risk in Limited Metros, but Supply Overhang in Many Others

Office Supply as % of Stock, 2010 - 2014

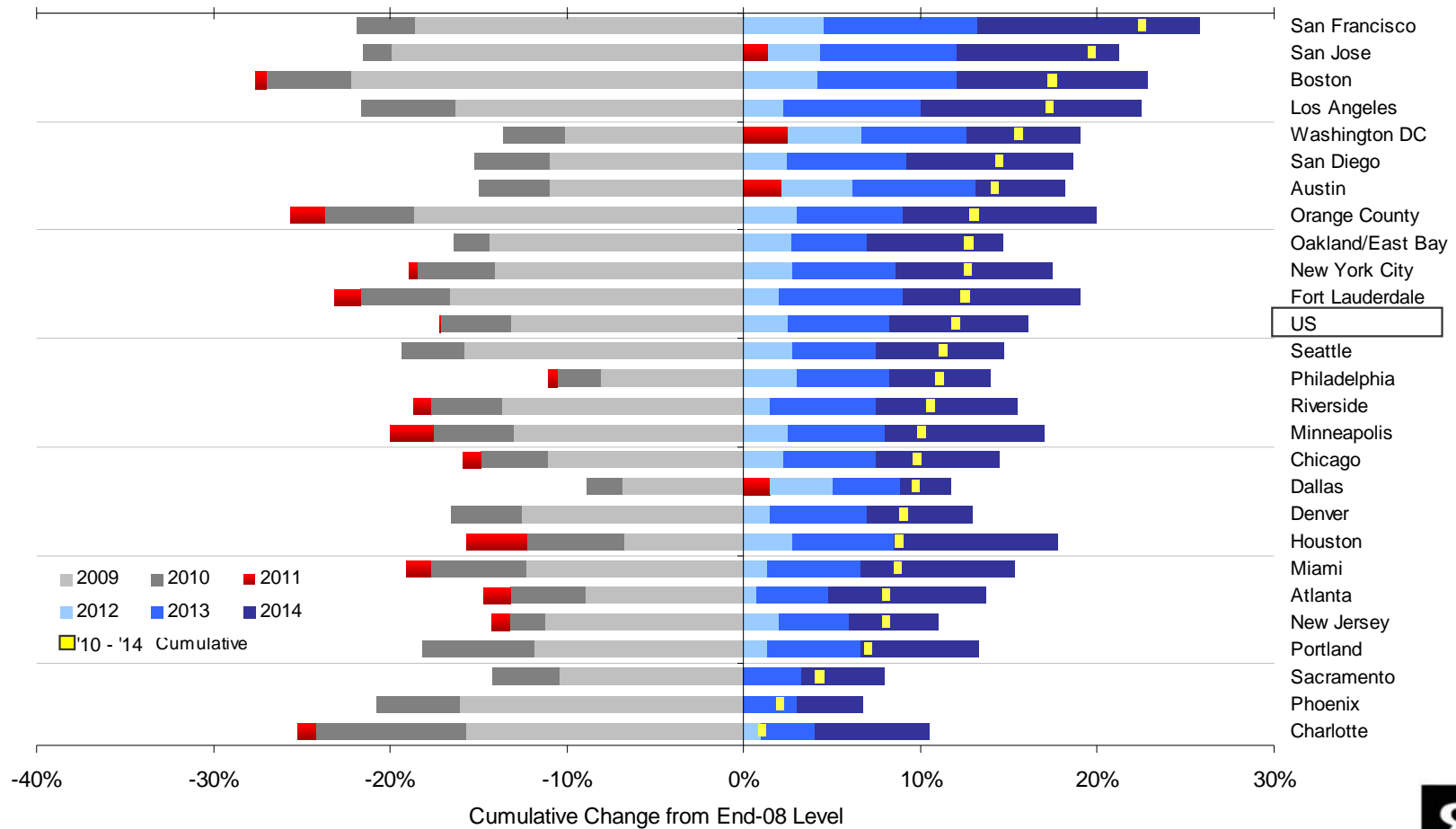


## Office: Supply-Constrained Metros Generally Outperform on Vacancy Rates

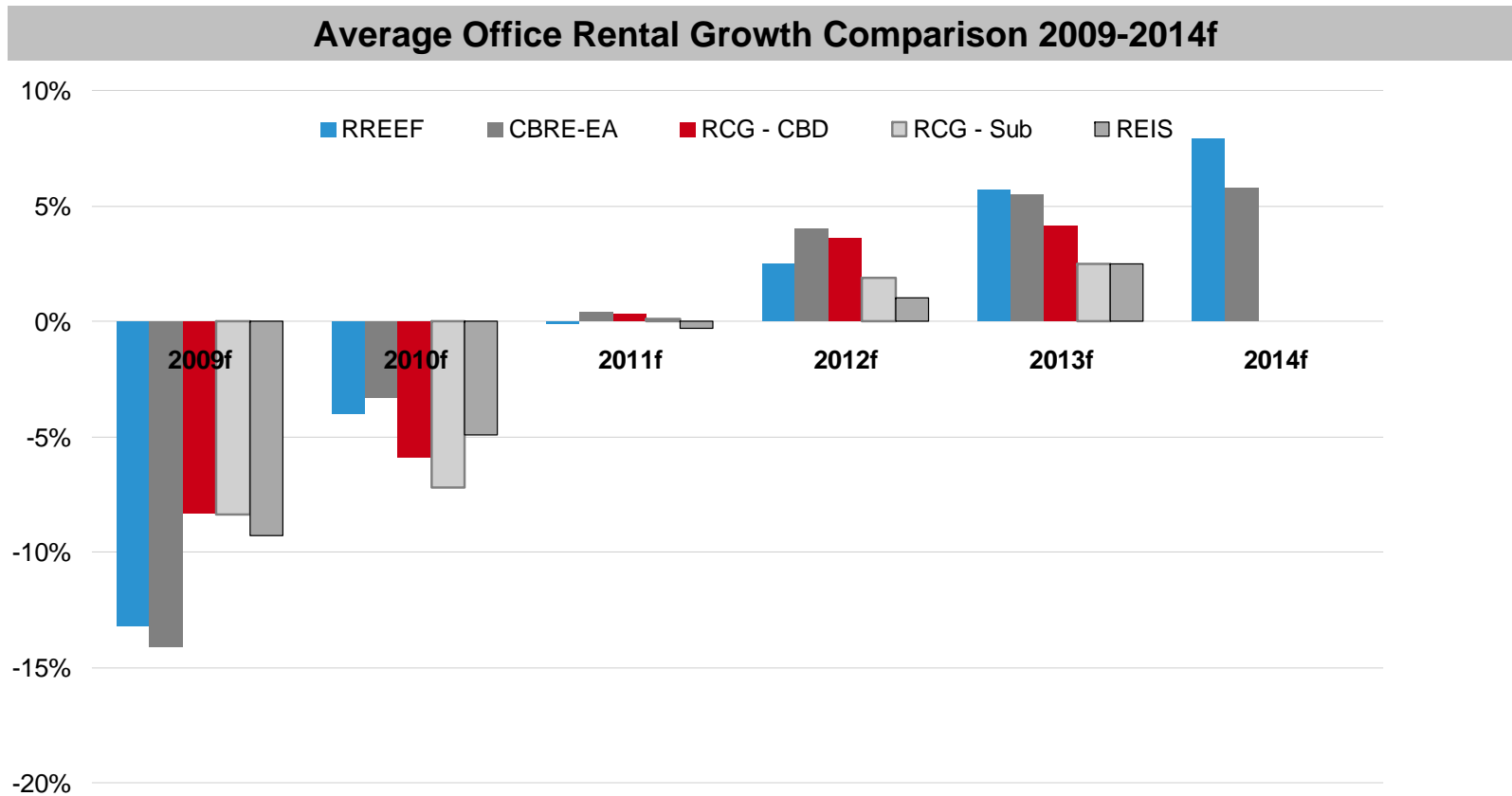


## Office: Rent Growth Strongest in Coastal Core Markets

Office Cumulative Rental Growth Rate (%), 2010-2014



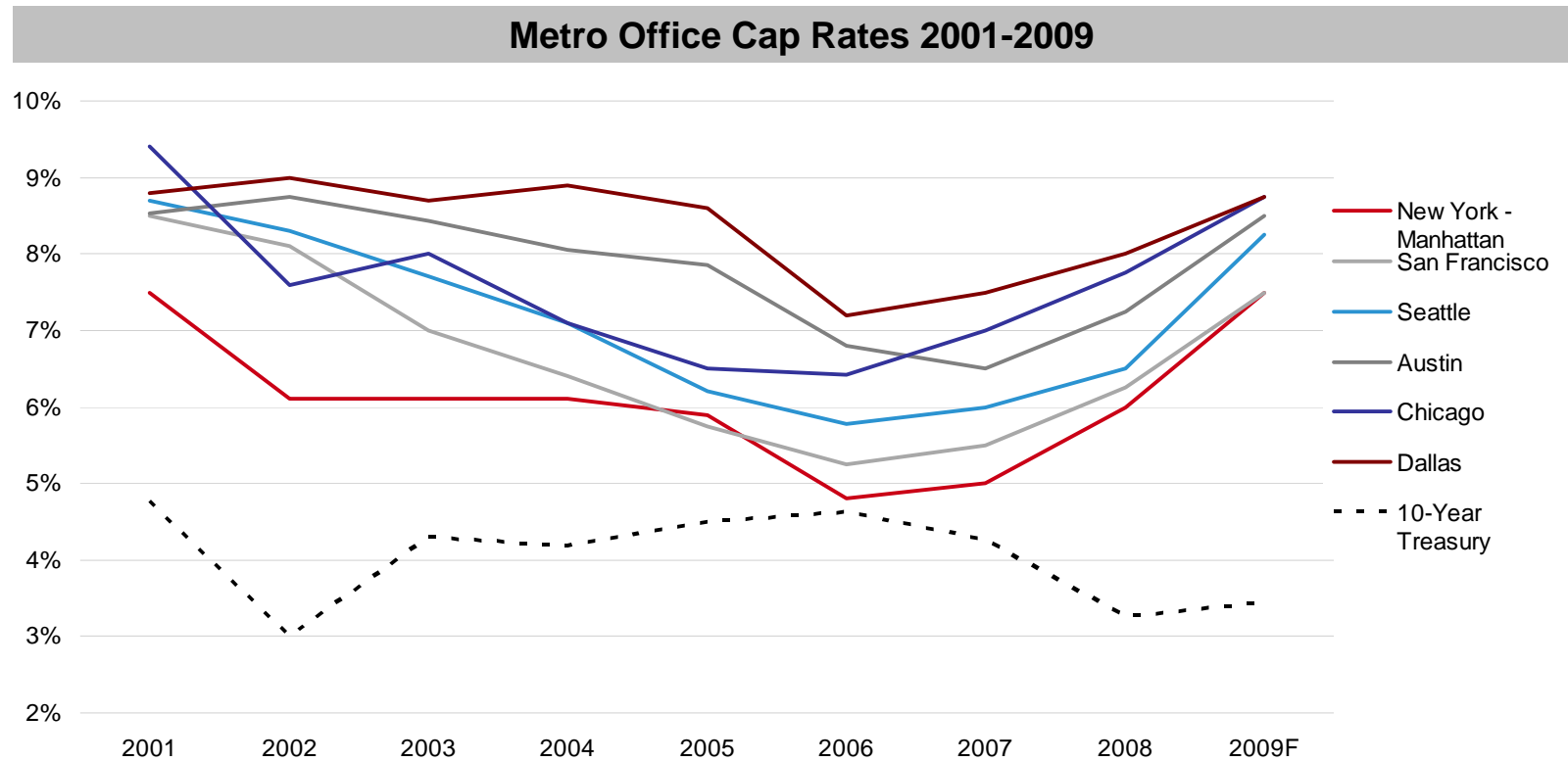
## Office: RREEF Research More Bearish in the Near Term; More Bullish Long Term



f = Forecast  
 Source: RREEF Research  
 As of December 2009.c



## Office: Cap rates Returned to Historic Norms

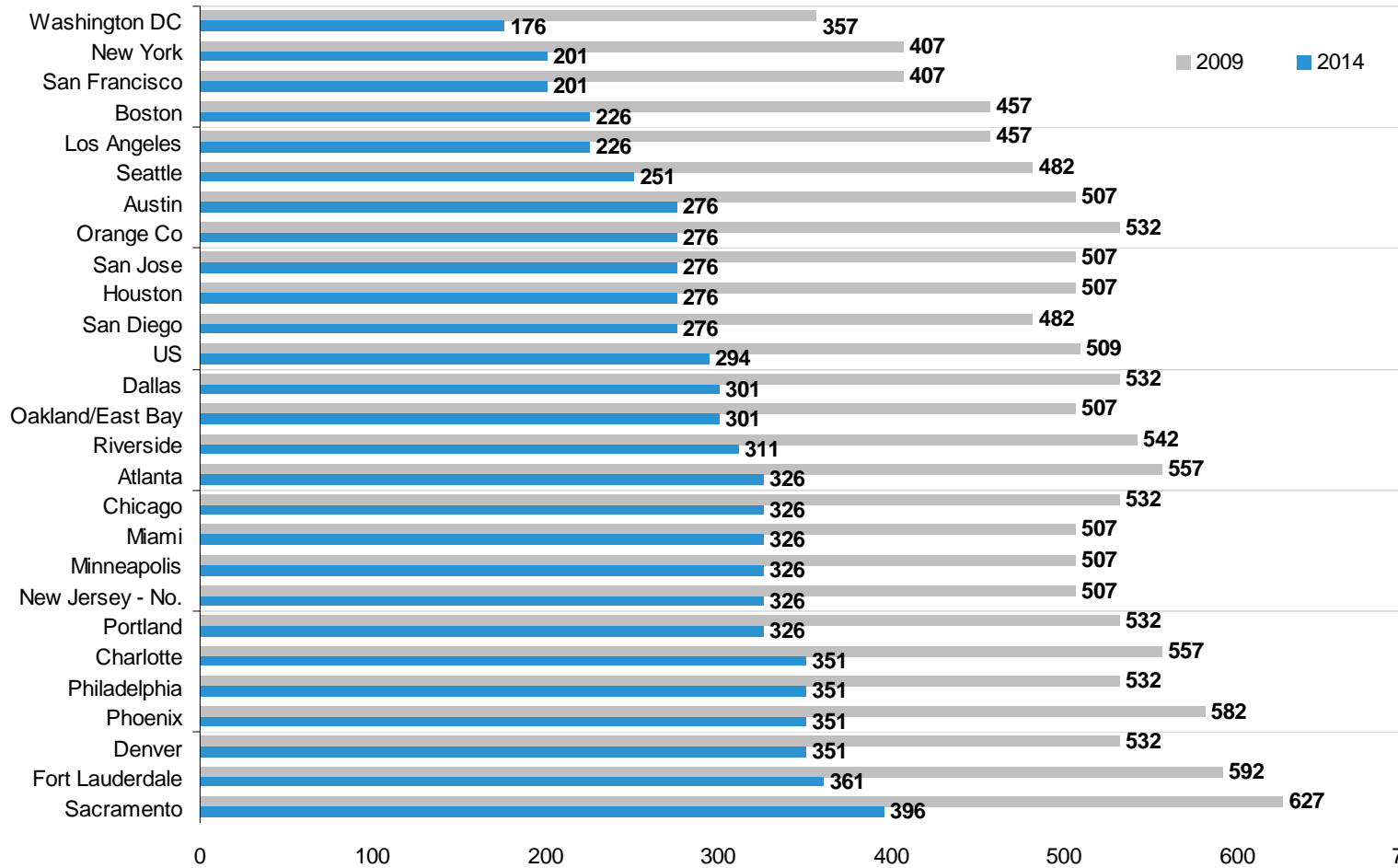


Source: CBRE-EA  
As of December 2009.

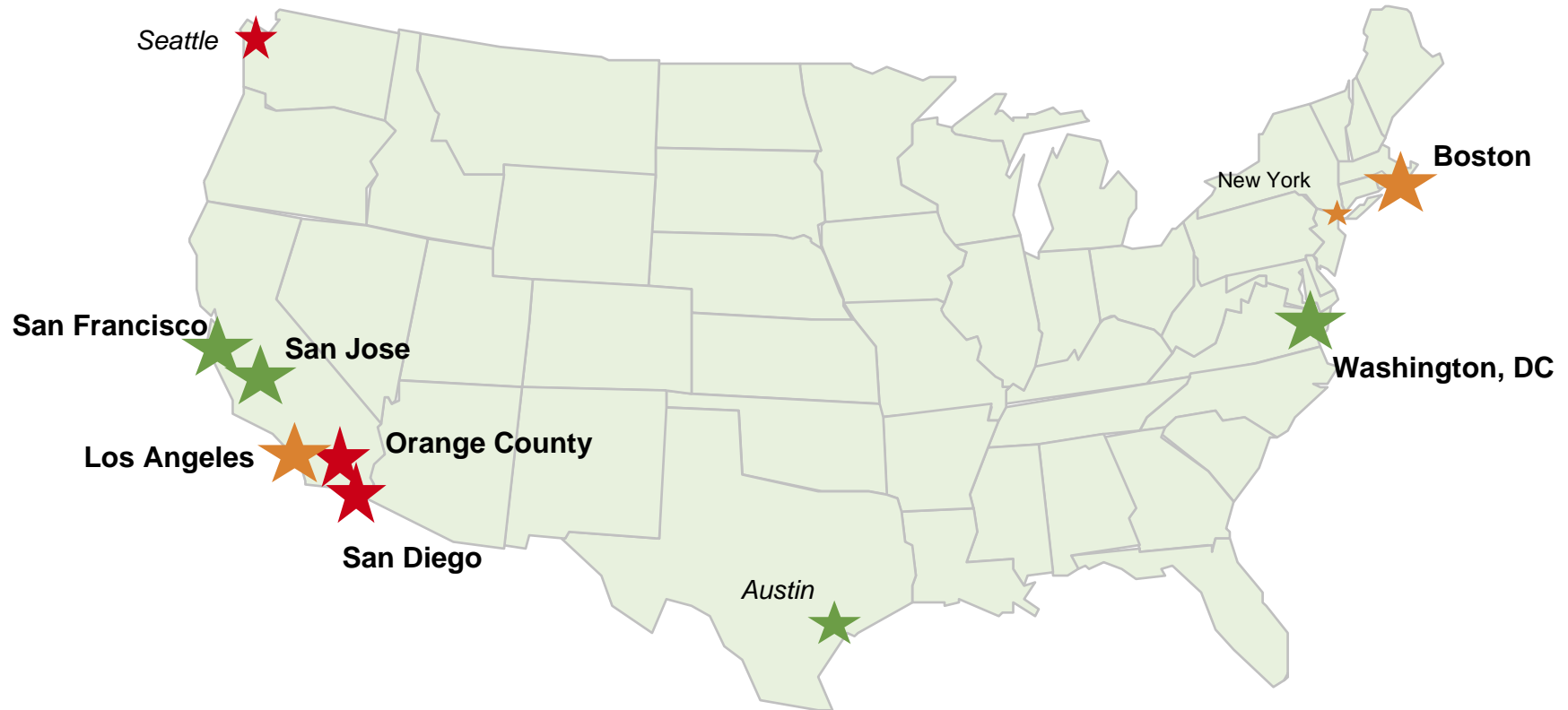


## Office: Cap Rates to T-Bill Yield Spread Forecast to Compress

Office Yield Spread, 2009 - 2014



## RREEF Target Office Investment Markets



Recovery magnitude:

- ★ Strong
- ★ Average
- ★ Weak

Recovery timing:

- ★ Early
- ★ Medium
- ★ Late





## Section VI

### Retail Sector Outlook

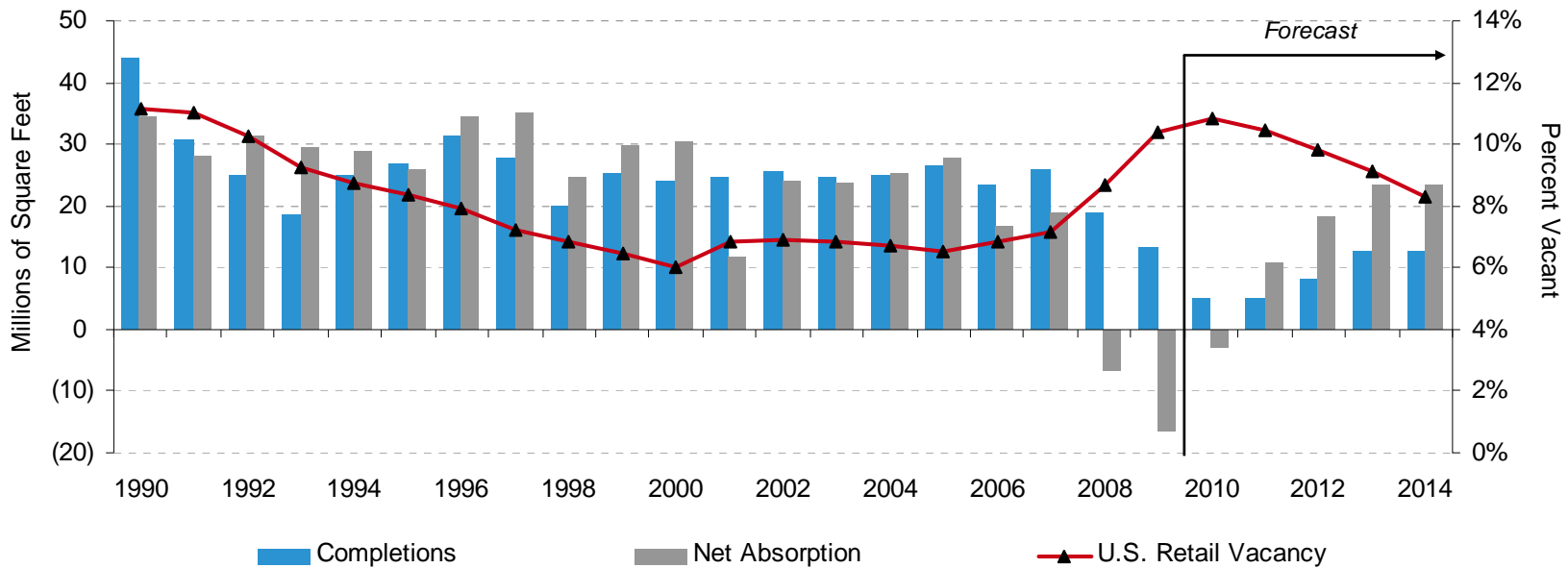
## Retail: A Different Rent Model

- ❑ Top-down model, rather than the bottom-up forecasting for the other sectors
  - Forecast national rent growth baseline based on macro retail conditions
  - Adjust for each metro and product type based on key drivers
  
- ❑ Regression model to determine drivers of “rent growth consistency”
  - Most important factors: (1) vacancy rate and (2) per-capita sales growth
  - Also: (3) HH income growth and (4) net supply growth relative to HH growth
  - Top performing metros are those we traditionally favor: denser, more affluent metros with significant physical or regulatory constraints to new supply
  
- ❑ Metro level occupancy and rent-growth drivers more based on economic growth
  - Most important factors for near term: (1) current market conditions and (2) current economic conditions
  - Most important factors for longer term: (1) competitive supply threat (2) likely economic growth



## Retail: Grappling with Unprecedented Demand Declines

U.S. Retail Supply and Demand, 1990-2014

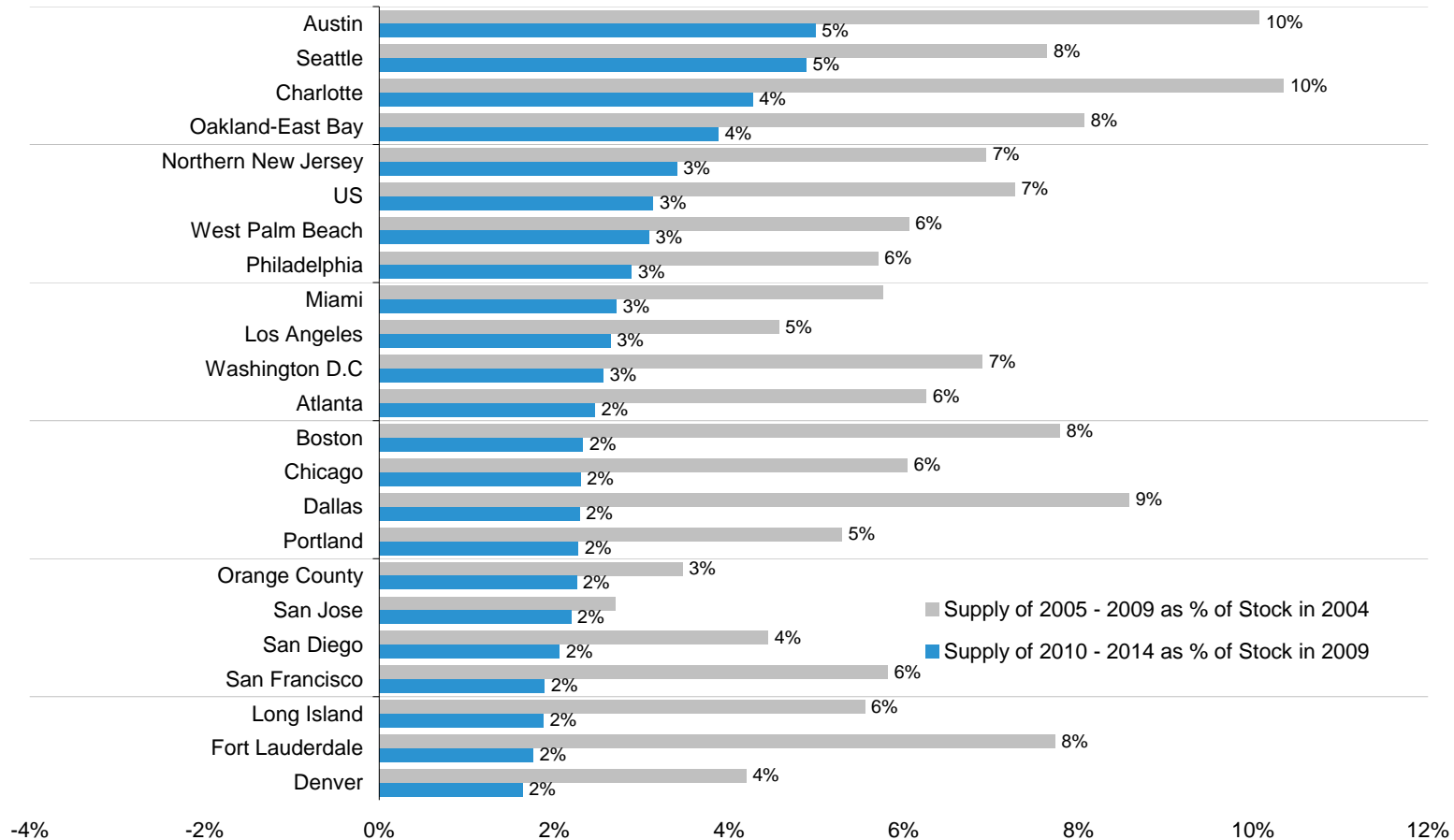


Source: RREEF Research, REIS.  
As of December 2009.

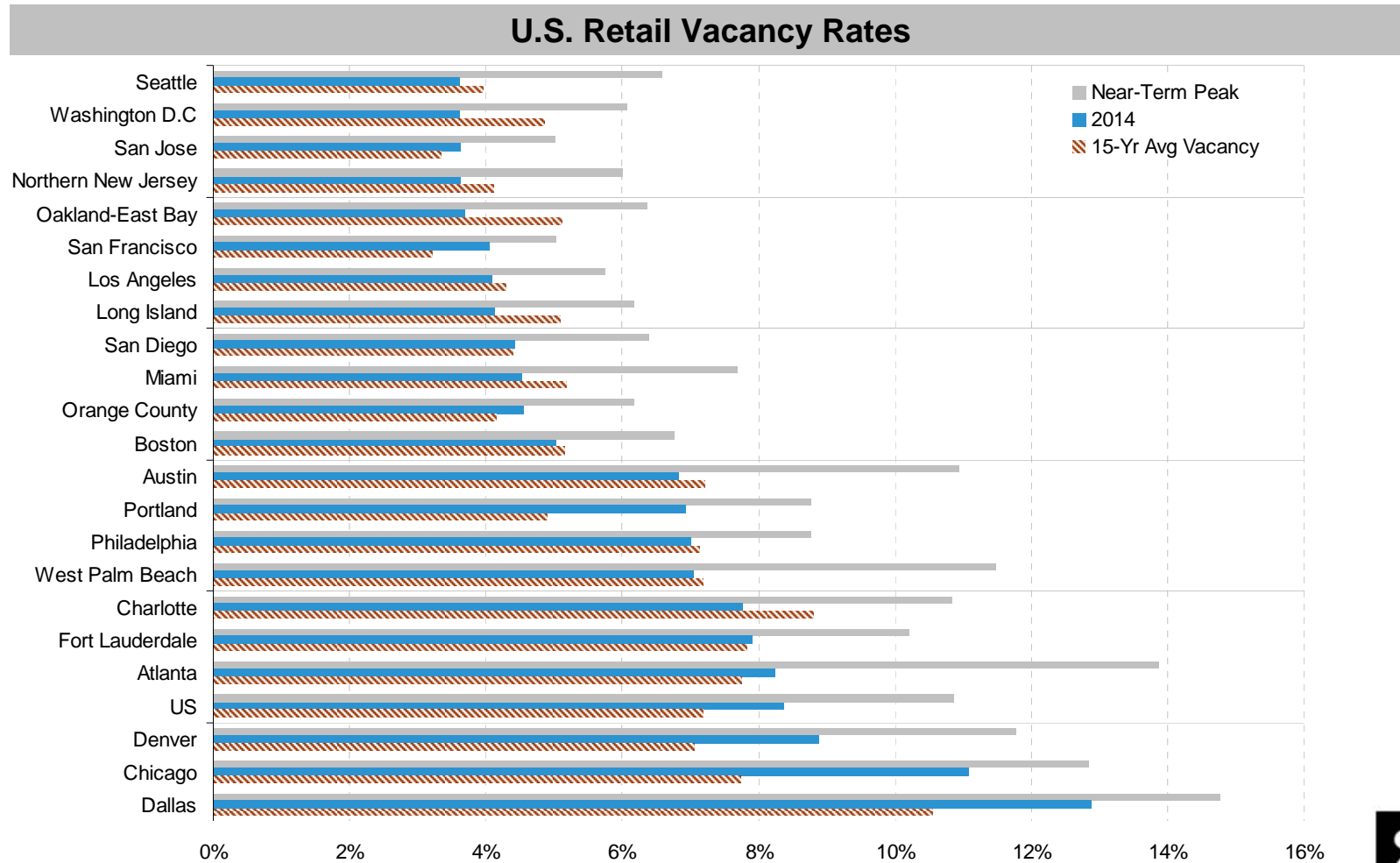


## Retail: A Dramatic Drop in Deliveries...

Retail Supply as % of Stock, 2010 - 2014

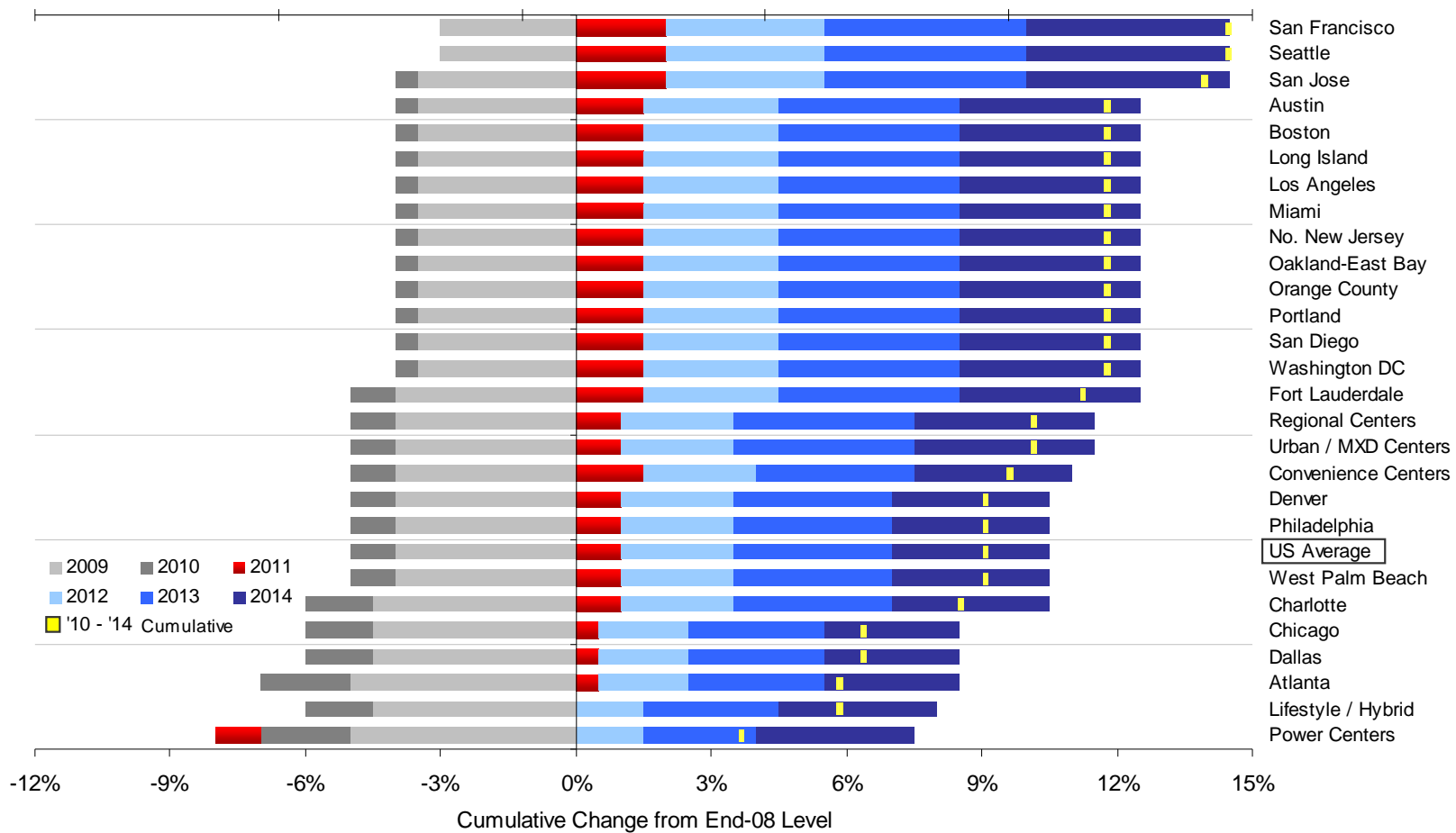


## Retail: Helps Drive Down Vacancies Going Forward

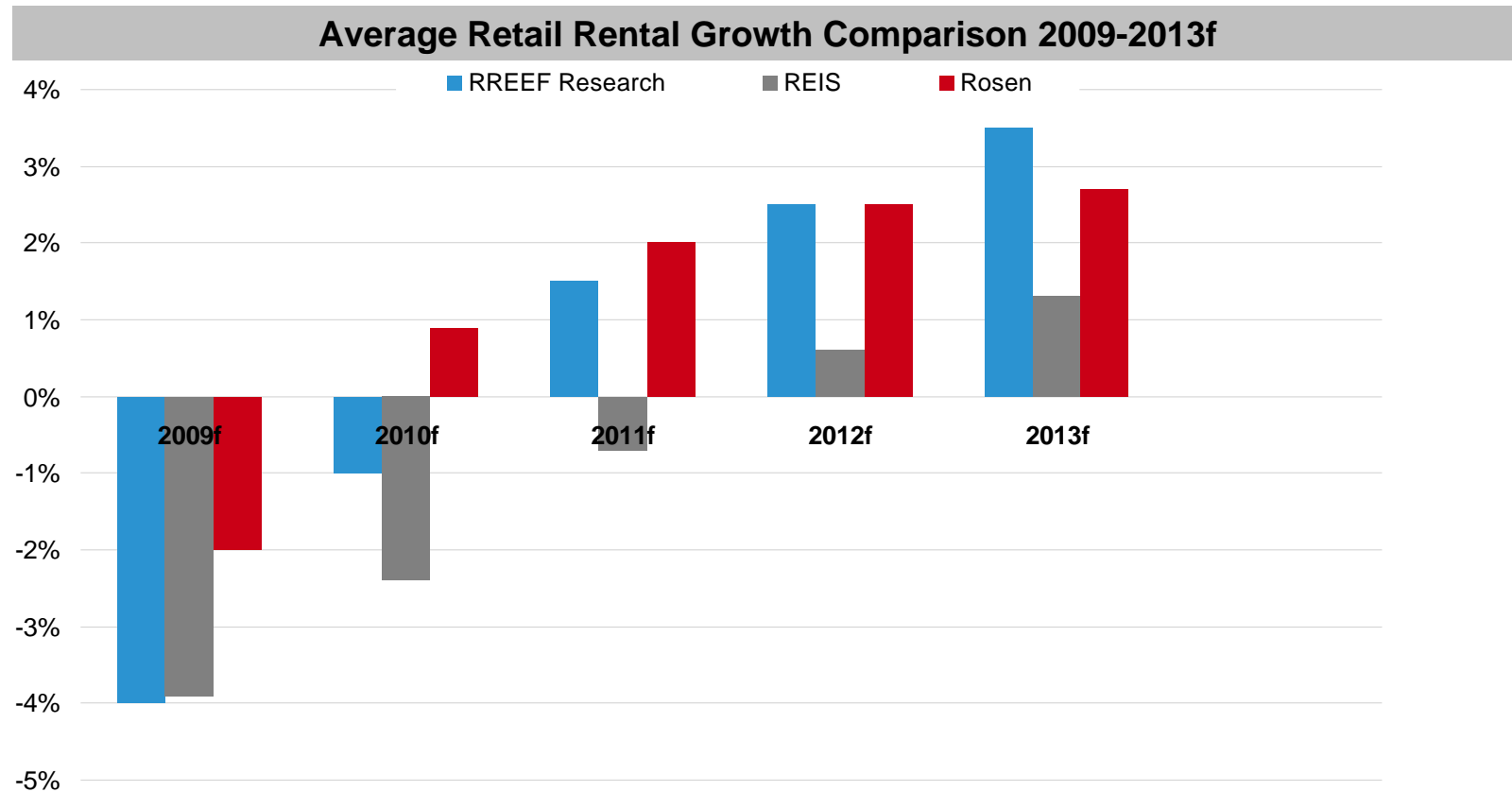


## Retail: Worst of Rent Declines Are Now Behind Us, But Future Growth Will be Moderate

Retail Cumulative Rental Growth Rate (%), 2010-2014



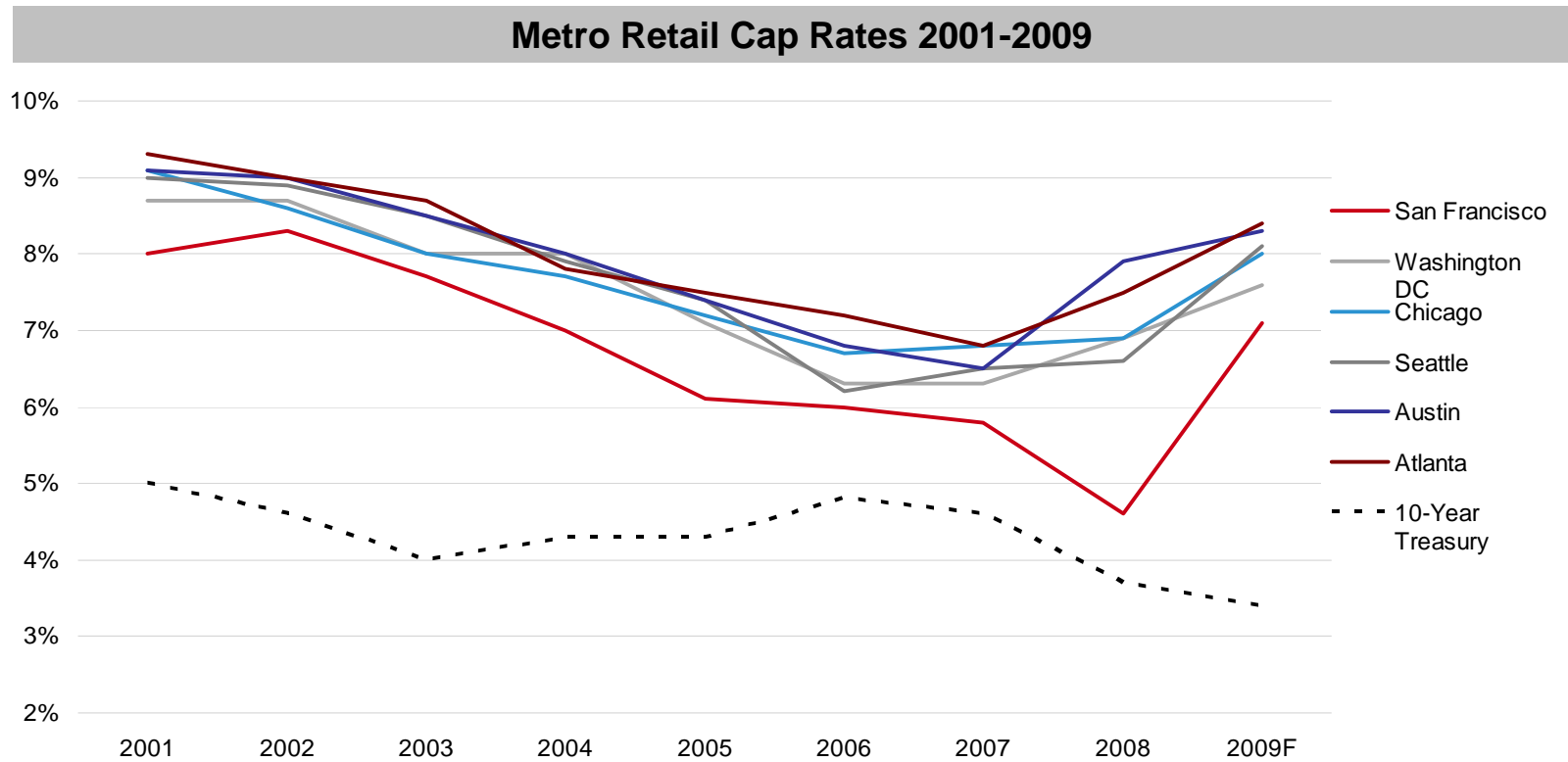
## Retail: RREEF Research Somewhat Optimistic on Retail



f = Forecast  
 Source: RREEF Research  
 As of December 2009.c



## Retail: Cap Rates Returning to Historic Norms

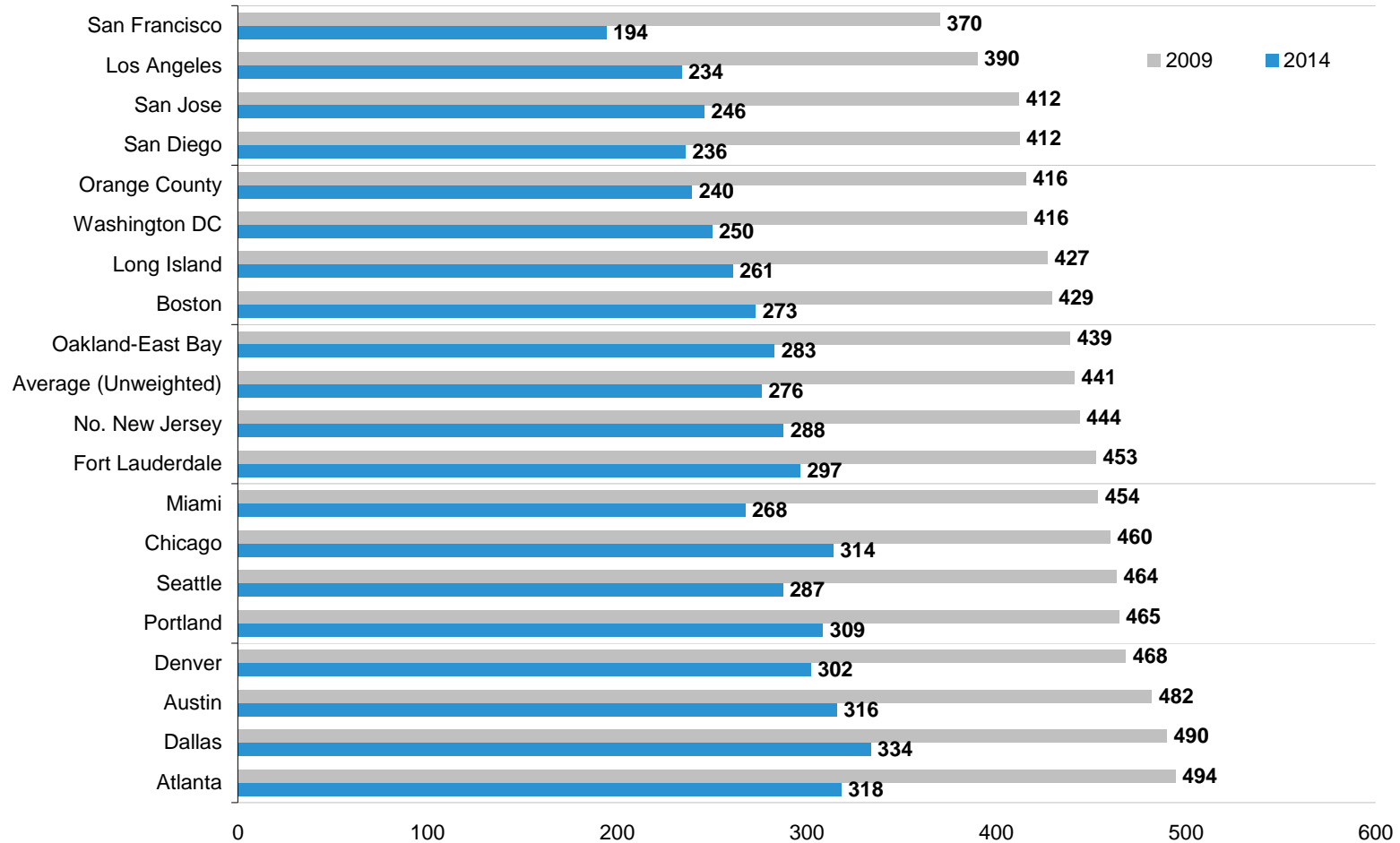


Source: CBRE-EA  
As of December 2009.

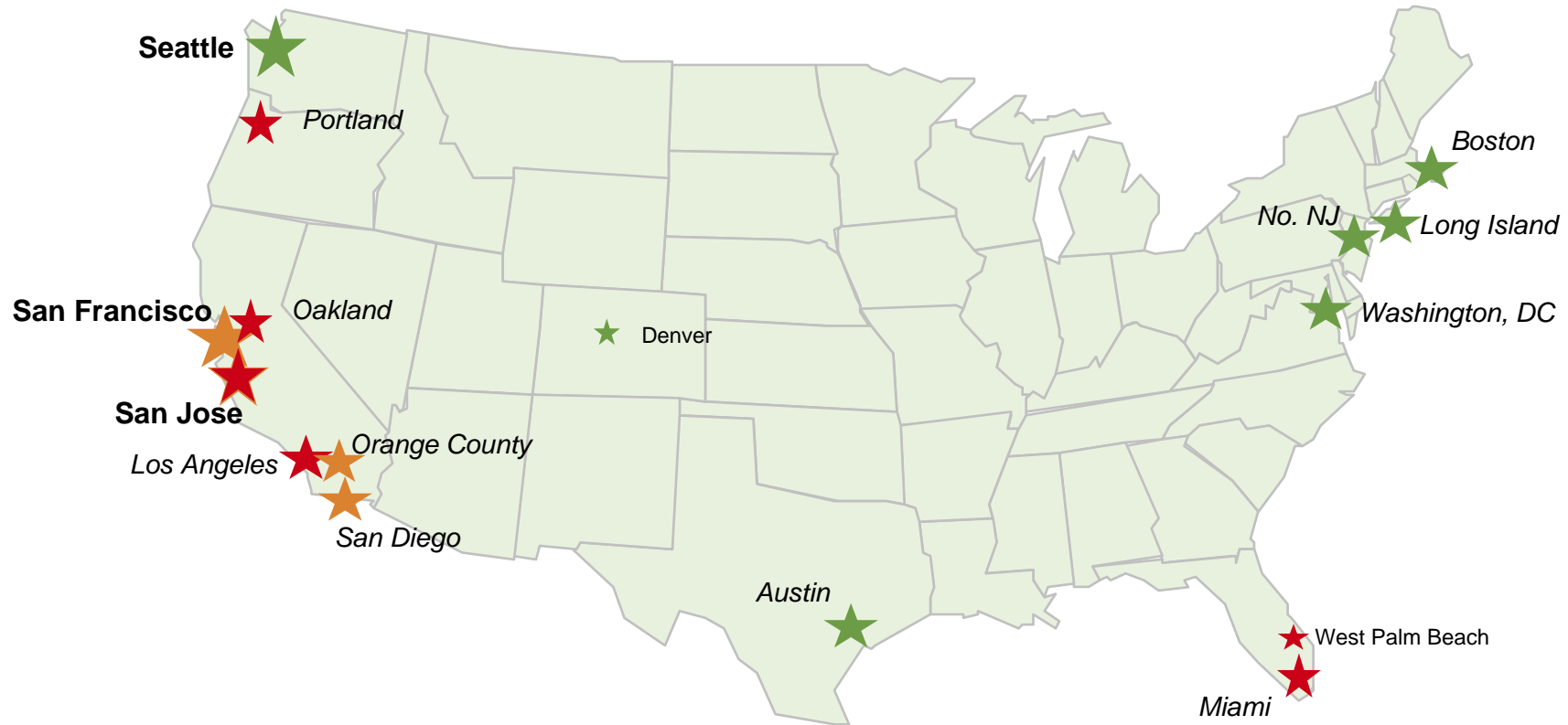


## Retail: Cap Rate to T-Bill Yield Spread to Compress

Retail Yield Spread, 2009 - 2014



## RREEF Target Retail Investment Markets



Recovery magnitude:

- ★ Strong
- ★ Average
- ★ Weak

Recovery timing:

- ★ Early
- ★ Medium
- ★ Late



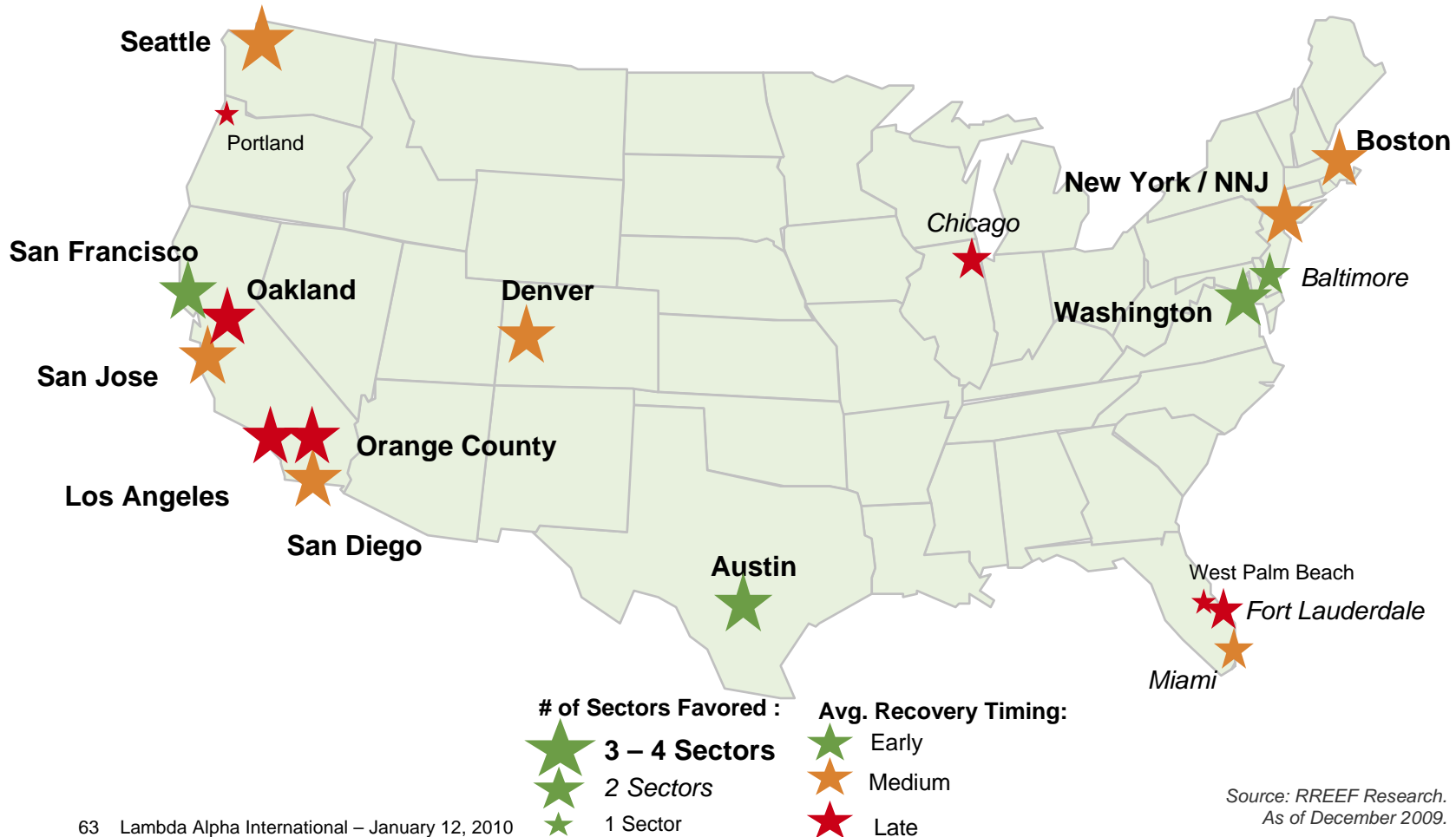


## Section VII

### Summary Market Conclusions

## Near-Term Acquisitions Should Concentrate On “Quick Recovery” Markets

### Real Estate Market Recovery Roadmap



## Investing in 2010-2011

- Primary Investment focus should be core
- Prime submarkets in primary target markets
- Apartments should be favored given earliest recovery
- Industrial in favored markets should also be given strong consideration
- Strength of near term rent roll is key, especially in industrial, office and retail sectors
- Secondary submarkets and secondary target markets should be considered “Value-Added”



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