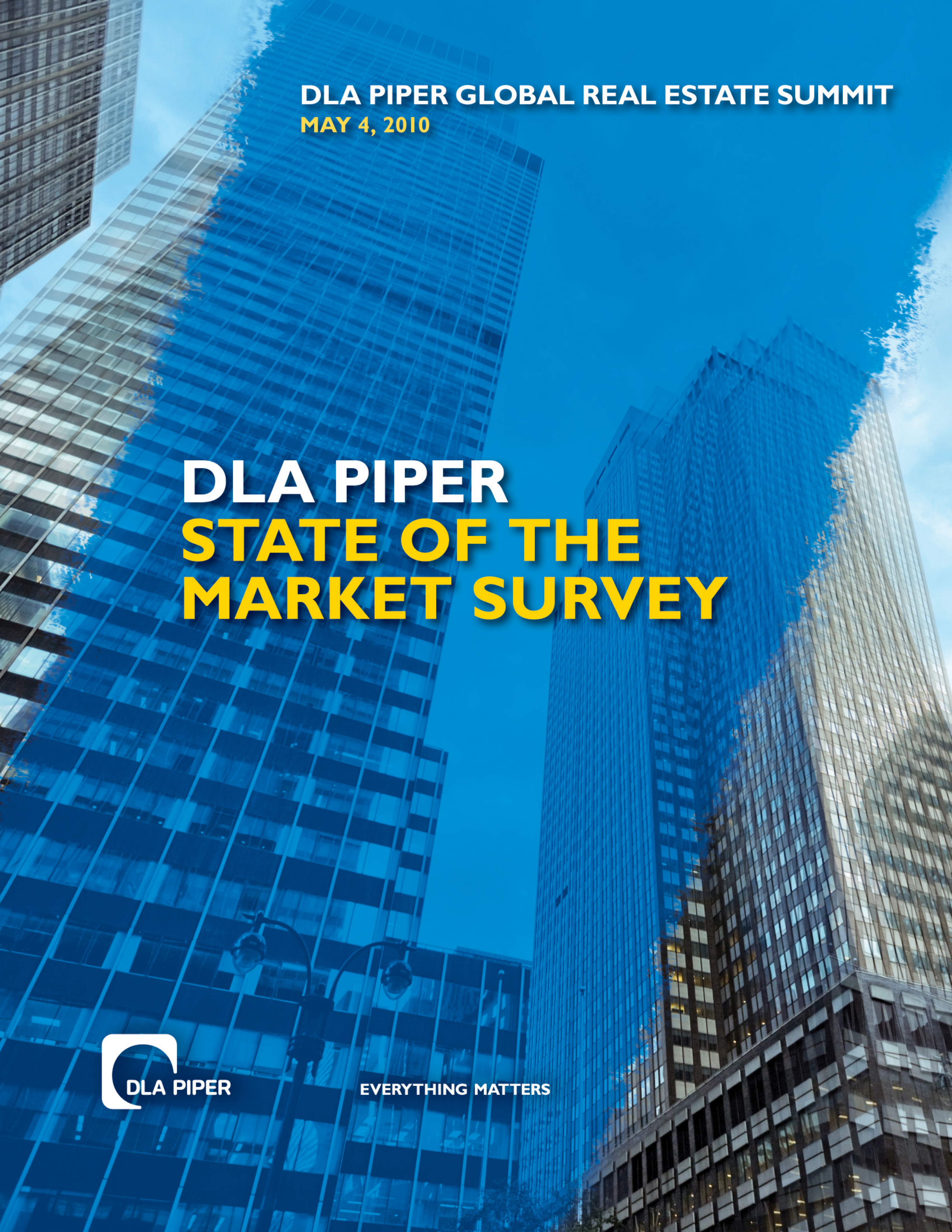

DLA PIPER GLOBAL REAL ESTATE SUMMIT

MAY 4, 2010

DLA PIPER
STATE OF THE MARKET SURVEY

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EVERYTHING MATTERS

EXECUTIVE SUMMARY

“Let the cards fall where they may.”

Faced with billions of dollars in commercial real estate debt coming due, the industry refuses to panic, sensing that the bottom of the cycle is upon us, according to DLA Piper’s *2010 State of the Market Survey*.

Responding to this bottoming out process, the outlook for the US commercial real estate industry remains largely bearish but it is noticeably improving. The bulls among the respondents believe the markets have corrected and that the abundance of equity capital will fuel the comeback. Even among the bears, fears of inflation and a double-dip recession do not appear to be a major concern. This sense of recovery has been buoyed in part by the federal government’s TARP, TALF and other real estate-focused programs.

Moving forward, however, real estate executives report they do not want nor anticipate any further federal assistance as they prepare to workout and wait out maturing loans.

Highlights of DLA Piper’s *2010 State of the Market Survey* include:

- The majority of respondents (60 percent) believe that real estate markets have already reached, or will reach, bottom in 2010.
- 6 out of 10 respondents (60 percent) describe themselves as “bearish,” down from a record high of 90 percent in September 2008 when DLA Piper last surveyed the market. Consequently, “bullish” responses quadrupled from 10 to 40 percent.
- 2 out of 3 respondents believe that the federal government’s TARP, TALF and other real estate-focused programs have done “enough” to stabilize the real estate marketplace.
- Consistent with this view, the majority of respondents (70 percent) do not expect any additional federal legislation focused on aiding the US commercial real estate market.
- 6 out of 10 respondents (60 percent) do not expect the CMBS market to return in time to help refinance the more than $150 billion in CMBS loans coming due in the next two years.
- Respondents named workouts (40 percent) and loan extensions (27 percent) as the two most prominent strategies for owners and lenders trapped by the refinancing crisis.
- Interestingly, respondents do not expect workouts to yield deep discounts with lenders: 61 percent of respondents expect that the **largest** loan write-offs will range between 11 and 30 percent.
- Tempering concerns over inflation, 75 percent of respondents think interest rates are headed up, but only “slightly,” in the next six months while another 21 percent of respondents expect “no change” in interest rates.

- Armed with war chests of new capital, respondents expect private equity and hedge funds (37 percent) and REITS (29 percent) to be the most active investors during the next near.
- Multifamily (37 percent) ranks as the most attractive investment opportunity during the next 12 months, while hotels (25 percent) rebounded from last place in 2008 to finish as the second most attractive investment opportunity.

VERBATIMS

Respondents were asked to share their thoughts on the following questions in an open forum for comment and feedback. The following represent select verbatims received from survey respondents.

What do you think regulators should do to further stimulate the recovery of the US commercial real estate market?

- *Nothing.*
- *Get out of the way.*
- *Stop interfering.*
- *Let the cards fall where they may.*
- *Let some big banks fail. Let the market find its bottom without artificially propping up the very banks that created this mess.*
- *Force banks to stop "kicking the can."*
- *Continue to pressure major banks to make loans.*
- *Face the music, finally, which will be painful but will allow investors to feel confident about values.*
- *Create a government-sponsored rating agency that has "skin in the game."*
- *Make sure banks maintain 5% interest in every tranche of loans they originate.*
- *Modify FIRPTA laws to promote overseas investment.*

What issue do you think remains the key wild card facing the US commercial real estate market?

- *Inflation.*
- *Interest rate fluctuation.*
- *Wall Street's influence on government policy.*
- *Job growth!*
- *Sheer lack of demand – we still have years of shadow vacancy left to absorb.*
- *Job growth. No jobs, no people. No people, no need for space.*
- *Recognize the reality that cap rates have shifted and the current values are going to be the norm.*
- *Billions in CMBS debt coming due.*
- *The "shape" of the recovery.*
- *The number of deep pocketed investors who have bet so heavily on a depression. They keep talking their short book.*

DLA PIPER 2010 STATE OF THE MARKET SURVEY

1. HOW WOULD YOU DESCRIBE YOUR OUTLOOK FOR THE US COMMERCIAL REAL ESTATE MARKET OVER THE NEXT 12 MONTHS?

RESPONSES	COUNT	%	PERCENTAGE OF TOTAL RESPONDENTS
Bullish	123	39.94%	
Bearish	185	60.06%	
Total Responses	308		20% 40% 60% 80% 100%

- 6 out 10 respondents (60 percent) describe themselves as "bearish," down significantly from 90 percent in September 2008 when DLA Piper last surveyed the market just days after the collapse of Lehman Brothers and the sale of Merrill Lynch to Bank of America.
- "Bullish" sentiment, meanwhile, has quadrupled from 10 to 40 percent in 2010, signaling a strong sense of recovery among respondents.

2. WHAT IS THE PRIMARY REASON FOR YOUR CONFIDENCE?

RESPONSES	COUNT	%	PERCENTAGE OF TOTAL RESPONDENTS
Expected rebound of the US economy	28	22.76%	
Foreign investment in US market	3	2.44%	
Investment opportunities created by market correction	49	39.84%	
Abundance of equity capital available for investment	28	22.76%	
Return of credit markets	11	8.94%	
Obama administration and Democratic policies	2	1.63%	
Other (please specify)	2	1.63%	
Total Responses	123		20% 40% 60% 80% 100%

- The majority of respondents (40 percent) who hold a bullish outlook for the US commercial real estate market cite new investment opportunities created by the market correction. This suggests that respondents expect more assets will be coming on the market during the next 12 months and that the bid-ask gap on pricing is also shrinking to more acceptable levels.

- Looking at other bullish factors, an equal percentage of respondents (23 percent) cited the abundance of equity capital available and the expected rebound of the US economy as the reasons for their confidence.

  Note: This question was only made available to those respondents who described their outlook as "bullish." For this reason, the question was not applicable to 185 of our survey respondents.

3. WHAT IS THE PRIMARY REASON FOR YOUR LACK OF CONFIDENCE?

RESPONSES	COUNT	%	PERCENTAGE OF TOTAL RESPONDENTS
Sluggish economic/job growth	87	47.03%	
Continued fallout from credit crisis (e.g. lack of available debt)	62	33.51%	
Inability to bridge the "bid-ask" gap on pricing	21	11.35%	
Obama administration and Democratic policies	8	4.32%	
Other (please specify)	7	3.78%	
Total Responses	185		**20% 40% 60% 80% 100%**

- The majority of "bearish" respondents attributed their outlook to a combination of sluggish economic and job growth (47 percent) and continued fallout from the credit crisis (34 percent).

  Note: This question was only made available to those respondents who described their outlook as "bearish." For this reason, the question was not applicable to 123 of our survey respondents.

4. WHERE DO YOU THINK INTEREST RATES ARE HEADED IN THE NEXT SIX MONTHS?

RESPONSES	COUNT	%	PERCENTAGE OF TOTAL RESPONDENTS
Up Significantly	10	3.25%	
Up Slightly	230	74.68%	
No Change	65	21.10%	
Down Slightly	3	0.97%	
Down Significantly	0	0%	
Total Responses	308		**20% 40% 60% 80% 100%**

- The overwhelming majority of respondents (75 percent) think interest rates are headed "up slightly" in the next six months while another 21 percent of respondents expect "no change" in interest rates.
- Respondents clearly do not expect any surprises in store regarding interest rates, and the data also illustrates a particularly strong belief that there are no near-term inflation concerns in the market.

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5. WHERE DO YOU THINK CAP RATES ARE HEADED IN THE NEXT 6 TO 12 MONTHS?

RESPONSES	COUNT	%	PERCENTAGE OF TOTAL RESPONDENTS
Up	54	17.53%	
No significant change	200	64.94%	
Down	52	16.88%	
(Did not answer)	2	0.65%	
Total Responses	308		**20% 40% 60% 80% 100%**

- The majority of respondents (65 percent) expect no significant change in cap rates, flanked by 18 percent who expect cap rates to rise and 17 percent who expect cap rates to fall.
- Interestingly, when compared with the results of question No. 6, this bell-shaped curve suggests a disconnect between expectations for cap rates and the broader marketplace.
  - With a strong majority of respondents believing that the real estate markets are at or near bottom, we would expect a more dramatic shift in cap rates to reflect an anticipated uptick in activity.
  - Instead, the data suggests uncertainty in the marketplace regarding which direction property values will move when deal flow returns.

6. WHEN WILL THE REAL ESTATE MARKETS HIT BOTTOM?

RESPONSES	COUNT	%	PERCENTAGE OF TOTAL RESPONDENTS
They already have	76	24.68%	
2010	109	35.39%	
2011	88	28.57%	
2012	28	9.09%	
After 2012	5	1.62%	
(Did not answer)	2	0.65%	
Total Responses	308		**20% 40% 60% 80% 100%**

- The majority of respondents (60 percent) believe the real estate markets are at or near the bottom.
  - 25 percent of respondents believe the markets have already hit bottom.
  - 35 percent of respondents expect that the bottom will hit later this year.
- Interestingly, while 60 percent of respondents describe themselves as bearish in question No. 1, possibly suggesting that the bottom of the market has not yet revealed itself, the majority of respondents here (60 percent) claim we are at the bottom. Once again, the uncertainty in the marketplace regarding the strength and velocity of the recovery is apparent from these answers.

- Slightly more than 10 percent of respondents believe that the bottom will not occur until 2012 or beyond.

7. WHICH INDUSTRY DO YOU THINK (PLEASE SELECT ONE):

		HOTEL	INDUSTRIAL	MULTIFAMILY	OFFICE-DOWNTOWN	OFFICE-SUBURBAN	RETAIL	DID NOT ANSWER	TOTAL
(a)	Presents the most attractive opportunity for real estate investors during the next 12 months?	[77] 25.00%	[34] 11.04%	[115] 37.34%	[30] 9.74%	[13] 4.22%	[31] 10.06%	8	308
(b)	Will see the greatest demand for "green" buildings in the next 12 months?	[21] 6.82%	[17] 5.52%	[35] 11.36%	[160] 51.95%	[44] 14.29%	[12] 3.90%	19	308

- While multifamily (37 percent) ranks as the most attractive investment opportunity during the next 12 months, respondents have also turned their attention back to the hotel sector.
  - After hotels took among the biggest hits of any commercial real estate sector during the credit crisis, respondents are now hoping to capitalize and rank hotels as the second most attractive investment opportunity – up from fifth (last place) in 2008.
- Reflecting the new wave of requirements for commercial green buildings in municipalities both large and small, the downtown office (52 percent) and suburban office sectors (14 percent) are expected to see the greatest demand for green buildings.

8. WHICH OF THE FOLLOWING INTERNATIONAL MARKETS OR REGIONS OUTSIDE OF THE US ARE MOST ATTRACTIVE FOR INVESTMENT DURING THE NEXT 12 MONTHS? PLEASE RANK IN ORDER OF IMPORTANCE WITH #1 BEING MOST ATTRACTIVE:

RESPONSES	RANK 1	RANK 2	RANK 3	RANK 4	RANK 5	RANK 6	RANK 7	WEIGHTED RANK (SCORE)
Brazil	90	48	53	21	9	4	6	1 (1308)
China	69	69	38	23	22	7	3	2 (1262)
India	35	60	57	37	26	10	5	3 (1141)
Western Europe	23	21	35	51	38	30	33	4 (873)
Eastern Europe	9	22	26	52	56	37	29	5 (804)
Middle East	3	7	15	27	42	61	76	6 (570)
Russia	2	4	7	19	38	82	79	7 (506)
(Did not answer)								77
Total Responses								308

- Likely responding to opportunities created by the 2016 Summer Olympics and 2014 World Cup, Brazil ranks as the most attractive international market, unseating China and India atop this ranking for the first time in the history of DLA Piper's *State of the Market Survey*.
- After rising to fourth place in 2008, respondents dropped the Middle East into seventh place in favor of opportunities in Western and Eastern Europe as concerns over the uncertainty of the recovery – particularly in Dubai – continue to cloud that region.

  Note: To calculate the weighted rank (score), selections were ranked 1-7 using an inverse weighted scale that valued each response as follows:

  – 1 – 7 points
  – 2 – 6 points
  – 3 – 5 points
  – 4 – 4 points
  – 5 – 3 points
  – 6 – 2 point
  – 7 – 1 point

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9. WHAT TYPE OF INVESTORS DO YOU EXPECT TO BE MOST ACTIVE IN THE US IN THE COMING YEAR?

RESPONSES	COUNT	%	PERCENTAGE OF TOTAL RESPONDENTS
Foreign investors	63	20.45%	
Insurance companies	15	4.87%	
Pension funds	20	6.49%	
Private equity / hedge funds	115	37.33%	
REITs	88	28.57%	
(Did not answer)	7	2.27%	
Total Responses	308		**20% 40% 60% 80% 100%**

- Reflecting the enormous amounts of capital raised during the past 18 months in both the private and public markets, the majority of respondents expect private equity and hedge funds (37 percent) to be the most active investors in the next year, followed by REITs (29 percent).
- In a dramatic spike upward from fifth (last place) in 2008, it is interesting to note that expectations for REITS have never been higher in the history of DLA Piper's *State of the Market Survey* (previous high, fourth in 2005). Now armed with war chests of capital for the first time in years, respondents believe REITS are among the most well-positioned investors. The recent, sustained rally in the share prices of publicly traded REITs supports this sentiment as well.

10. HAS THE FEDERAL GOVERNMENT DONE ENOUGH TO STABILIZE THE MARKETPLACE THROUGH THE TARP, TALF AND OTHER PROGRAMS FOCUSED ON REAL ESTATE?

RESPONSES	COUNT	%	PERCENTAGE OF TOTAL RESPONDENTS
Yes	206	66.88%	
No	99	32.14%	
(Did not answer)	3	0.97%	
Total Responses	308		**20% 40% 60% 80% 100%**

- 2 out of 3 respondents believe that the federal government's TARP, TALF and other real estate-focused programs have done enough to stabilize the real estate marketplace.

11. IN THE NEXT 12 MONTHS, DO YOU EXPECT THAT THE FEDERAL GOVERNMENT WILL ADOPT ADDITIONAL LEGISLATION FOCUSED ON AIDING THE US COMMERCIAL REAL ESTATE MARKET?

RESPONSES	COUNT	%	PERCENTAGE OF TOTAL RESPONDENTS
Yes	94	30.52%	
No	214	69.48%	
Total Responses	308		**20% 40% 60% 80% 100%**

- Consistent with the responses to question No. 10, the majority of respondents (70 percent) do not expect any additional federal legislation focused on aiding the US commercial real estate market.

12. DO YOU THINK THE CMBS MARKET WILL RE-EMERGE IN TIME TO HELP REFINANCE THE NEARLY $150 BILLION IN CMBS LOANS COMING DUE IN THE NEXT TWO YEARS?

RESPONSES	COUNT	%	PERCENTAGE OF TOTAL RESPONDENTS
Yes	124	40.26%	
No	180	58.44%	
(Did not answer)	4	1.30%	
Total Responses	308		**20% 40% 60% 80% 100%**

- Faced with the prospect of refinancing nearly $150 billion in CMBS loans in the next two years, 6 out of 10 respondents expect that the CMBS market will fail to re-emerge in time to help provide refinancing options.
- Notably, the percentage of respondents who are bullish in their outlook for the real estate markets (40 percent) is also the same as those who believe that CMBS financing will return to fuel the resurgence of the industry (40 percent).

13. WHETHER OR NOT THE CMBS MARKETS MAKE A COMEBACK, WHICH OF THE FOLLOWING STRATEGIES DO YOU THINK WILL BE THE MOST PROMINENT AS OWNERS AND FINANCIAL INSTITUTIONS WORK TO ADDRESS THE BROADER REFINANCING CRISIS WITH MORE THAN $1 TRILLION IN COMMERCIAL REAL ESTATE DEBT COMING DUE BY 2014?

RESPONSES	COUNT	%	PERCENTAGE OF TOTAL RESPONDENTS
Refinance existing debt	13	4.22%	
Recapitalize with new money and dilute remaining equity stakes	67	21.75%	
Wait it out (i.e. “kicking the can down the road” with loan extensions)	83	26.95%	
Work it out (i.e. restructure existing loans through a combination of write-downs, new capital and additional collateral)	124	40.26%	
Walk away (i.e. turn over the keys)	12	3.90%	
Sell the property	6	1.95%	
(Did not answer)	3	0.97%	
Total Responses	308		**20% 40% 60% 80% 100%**

- Respondents expect that “working it out” (40 percent) and “waiting it out” (27 percent) will be the two most prominent strategies used to navigate the waves of commercial real estate debt coming due between now and 2014.
- Despite several highly publicized examples of owners “walking away” from their properties and turning over the keys to lenders, respondents do not see a trend developing: Only 4 percent report that walking away will be the most prominent strategy.
- Aside from workouts and loan extensions, the options for owners and financial institutions are limited: While 22 percent of respondents think voluntarily recapitalizations will be the most prominent, the outlook for refinancing (4 percent) and property sales (2 percent) is particularly grim.

14. WHAT IS THE LARGEST PERCENTAGE OF AN INDIVIDUAL, NON-RECOURSE COMMERCIAL LOAN IN EXCESS OF $10 MILLION THAT YOU EXPECT A LENDER WILL WRITE OFF OR DEEPLY SUBORDINATE (E.G. BY SPLITTING THE ORIGINAL NOTE INTO AN "A" NOTE AND A "HOPE" NOTE) AS A PART OF A WORKOUT IN THE NEXT 12 MONTHS?

RESPONSES	COUNT	%	PERCENTAGE OF TOTAL RESPONDENTS
0-10%	17	5.52%	
11-20%	92	29.87%	
21-30%	95	30.84%	
31-40%	40	12.99%	
41-50%	23	7.47%	
51-60%	13	4.22%	
More than 60%	12	3.90%	
(Did not answer)	16	5.19%	
Total Responses	308		**20% 40% 60% 80% 100%**

- The majority of respondents do not expect workouts to yield extremely deep discounts with lenders:
  - 61 percent of respondents expect that the largest loan write-offs will range between 11 and 30 percent.
  - Only 8 percent of respondents expect that the largest loan write-offs will eclipse 50 percent.
- This forecast provides an insiders' look – a roadmap of sorts – regarding the types of likely boundaries and breakpoints of workouts, suggesting again that lenders are generally not willing to take drastic measures to workout loans.

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METHODOLOGY

In April of 2010, DLA Piper distributed a survey via e-mail to top executives within the real estate industry, including CEOs, COOs, CFOs and other senior executives. The survey was completed by **308 respondents** (see below for regional breakdown).

The survey coincides with DLA Piper's 2010 Global Real Estate Summit taking place in Chicago on May 4, 2010 and is attended by many of the executives included in the survey.

Question No. 2 was only made available to those respondents who described themselves as "bullish" in question 1.

Question No. 3 was only made available to those respondents who described themselves as "bearish" in question 1.

Due to rounding, all percentages used in all questions may not add up to 100 percent.

RESPONSES BY REGION	COUNT	%	PERCENTAGE OF TOTAL RESPONDENTS
Atlanta	7	2.27%	
Boston	36	11.69%	
Chicago	128	41.56%	
Dallas/Fort Worth	3	0.97%	
Houston	2	0.65%	
Los Angeles	18	5.84%	
New York	28	9.09%	
San Francisco Bay Area	13	4.22%	
Washington, DC	32	10.39%	
Other (please specify)	39	12.66%	
(Did not answer)	2	0.65%	
Total Responses	308		**20% 40% 60% 80% 100%**

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