

NCREIF Summer
Conference 2019

STAYING ON TRACK

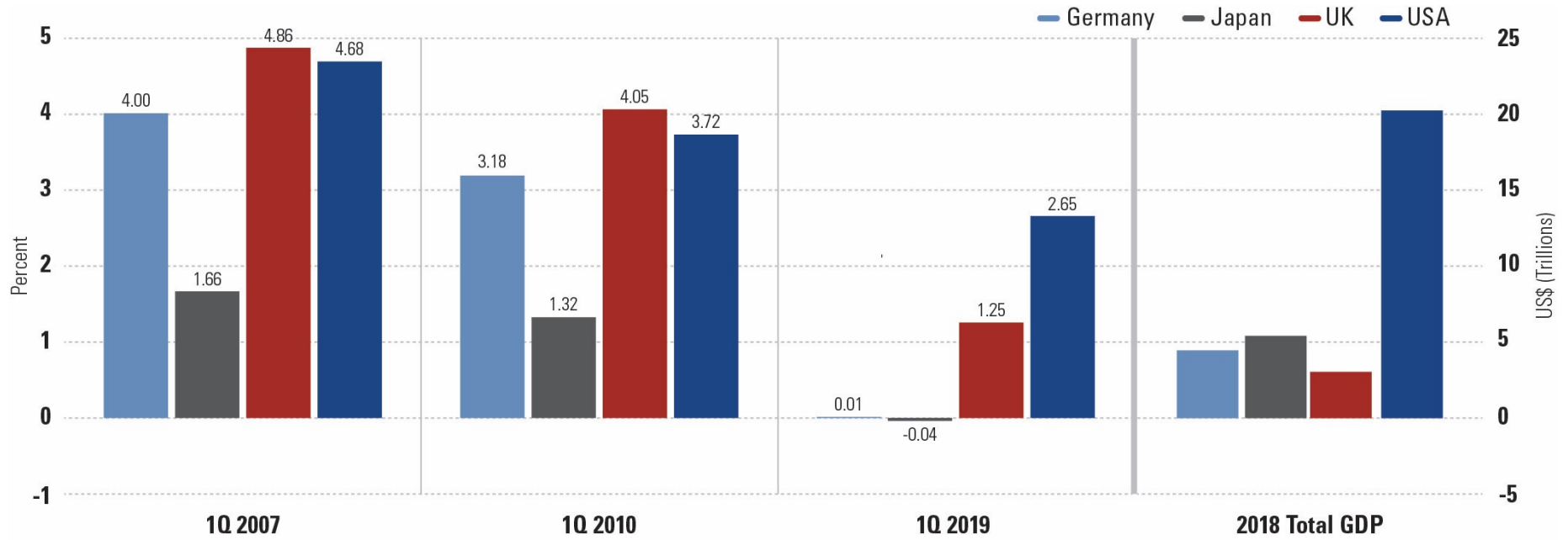


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- **Economy:** GDP grew at an annual rate of 3.2% in 1Q 2019 (advanced estimate), the best first quarter since 2015. About 263,000 jobs were added in April and the unemployment rate fell to 3.6%, a 50-year low. The current U.S. economic expansion phase is on track to become the longest in history at the beginning of the third quarter.
- **Treasury Rates:** The quarterly average U.S. 10-year Treasury rate dropped from 3.04% in 4Q 2018 to 2.65% in 1Q 2019. Situs RERC forecasts the rate to end 2019 around 2.7%. Long-term interest rates relative to GDP are expected to remain low. The 10-years as of June 11, 2019 was 2.14%.
- **Capital Universe:** There continues to be a huge amount of capital availability and dry powder amid . Private equity funds are expected to find it more difficult to place capital as the market comes closer to fair value. Private equity funds are taking longer to close – about 18 months.
- **CRE Returns:** Although NPI-ODCE returns have been strong over recent years, it is important to note that annual returns have been decreasing since 2015. With the economy on the verge of entering its longest expansion in US history, CRE returns are expected to gradually regress. With capital appreciation expected to decline over the forecast period, and cash flow hitting a steady but slower level of growth, CRE will rely on income to drive total returns moving forward.



Sources OECD, 1Q 2019.

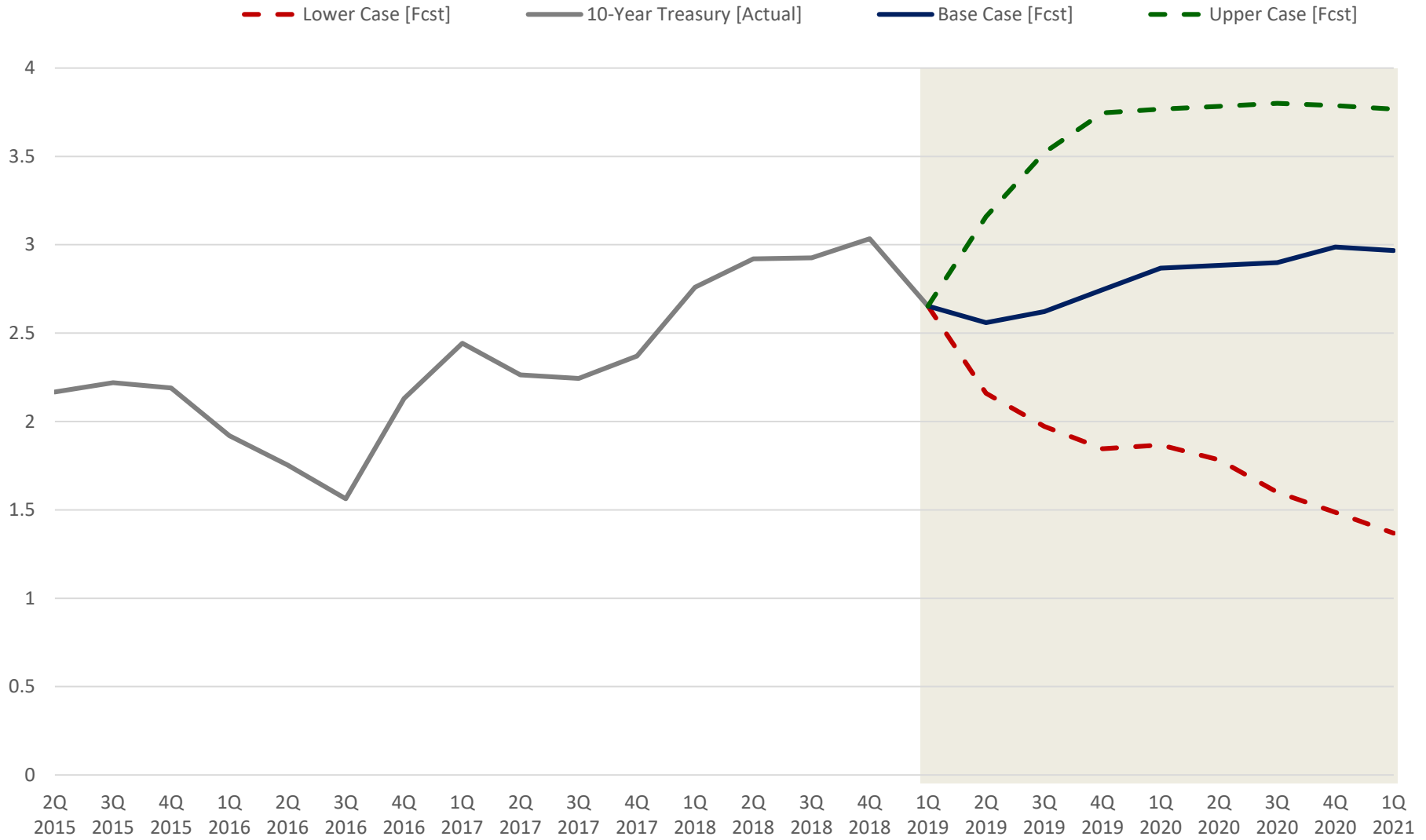
HISTORICAL U.S. 10-YEAR TREASURY RATES



Note: 10-year Treasury data are based on quarterly averages.

Source Federal Reserve, current as of 1Q 2019.

ACTUAL 10-YEAR TREASURY RATES VS. SITUS RERC TREASURY FORECAST



Note: Data based on quarterly average. Shaded area indicates forecast.

Sources Situs RERC, Federal Reserve, 1Q 2019.

Market Indexes	YTD ⁶	1-Year Trailing	3-Year Trailing	5-Year Trailing	10-Year Trailing	15-Year Trailing
NCREIF NPI ¹	1.80%	6.83%	7.07%	9.13%	8.51%	8.81%
NCREIF NFI ODCE ¹	1.20%	6.55%	7.01%	9.18%	7.73%	7.17%
NAREIT Index (Equity REITS) ²	17.17%	20.46%	7.84%	10.00%	18.80%	8.84%
Consumer Price Index ³	0.05%	1.63%	2.13%	1.46%	1.78%	2.05%
Dow Jones Industrial Average ²	13.10%	11.26%	16.37%	12.39%	15.97%	9.02%
NASDAQ Composite ⁴	16.49%	9.43%	16.65%	12.98%	17.59%	9.45%
NYSE Composite ⁴	12.64%	2.76%	7.55%	3.91%	9.81%	4.46%
S&P 500 ²	13.65%	9.50%	13.51%	10.91%	15.92%	8.57%
	1Q 2019	1Q 2018	1Q 2016	1Q 2014	1Q 2009	1Q 2004
10-Year Treasury Bond ⁵	2.65%	2.76%	1.92%	2.76%	2.74%	4.02%

¹NCREIF NPI is a property-level (unleveraged) total return index, gross of fees; NCREIF NFI-ODCE is a fund-level (leveraged equity) total return index, net of fees.

²Based on total return index, and includes the dividend yield.

³Based on the published data from the Bureau of Labor Statistics (seasonally-adjusted).

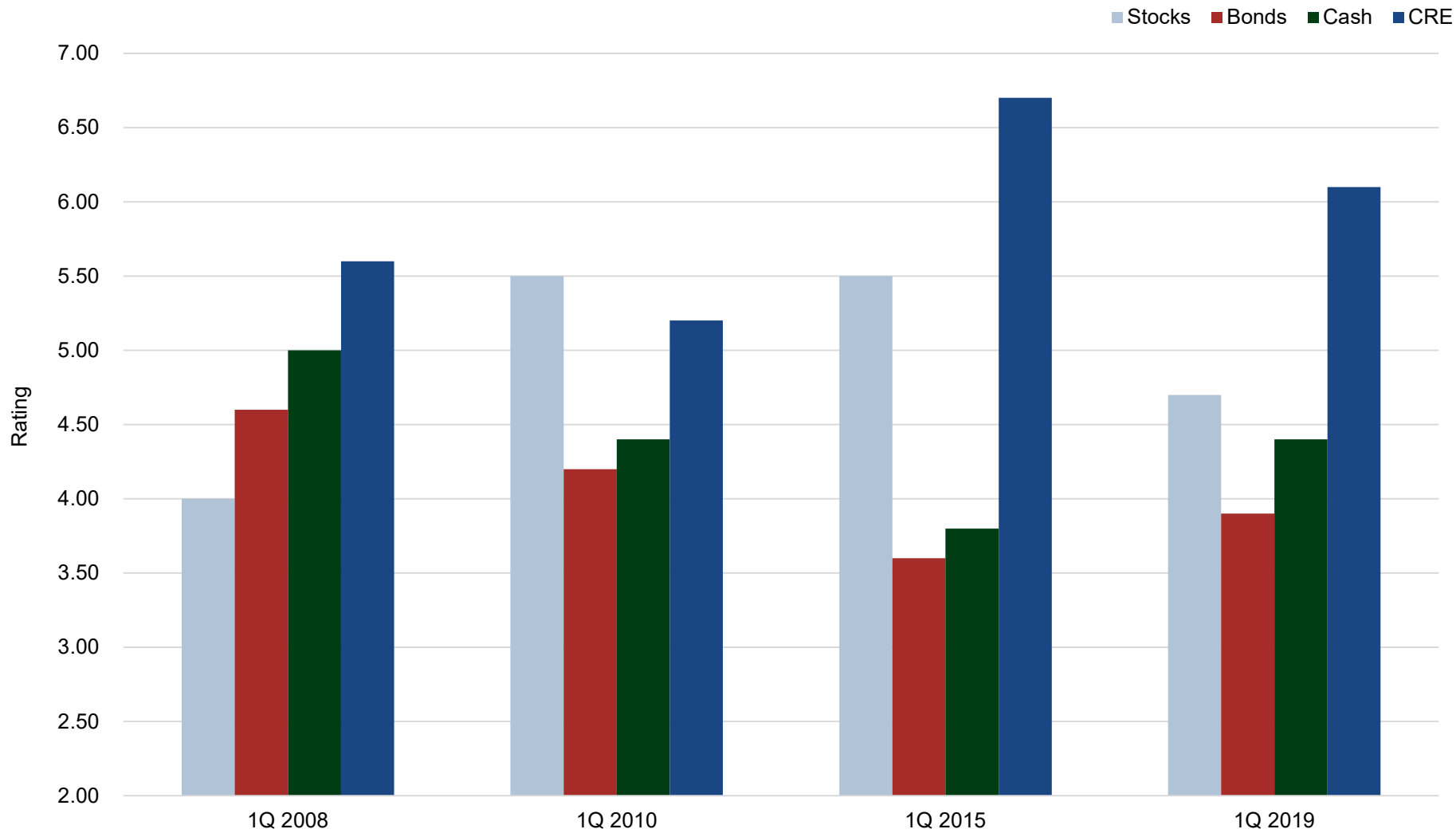
⁴Based on price index, and does not include the dividend yield.

⁵Based on average quarterly T-bond Rates.

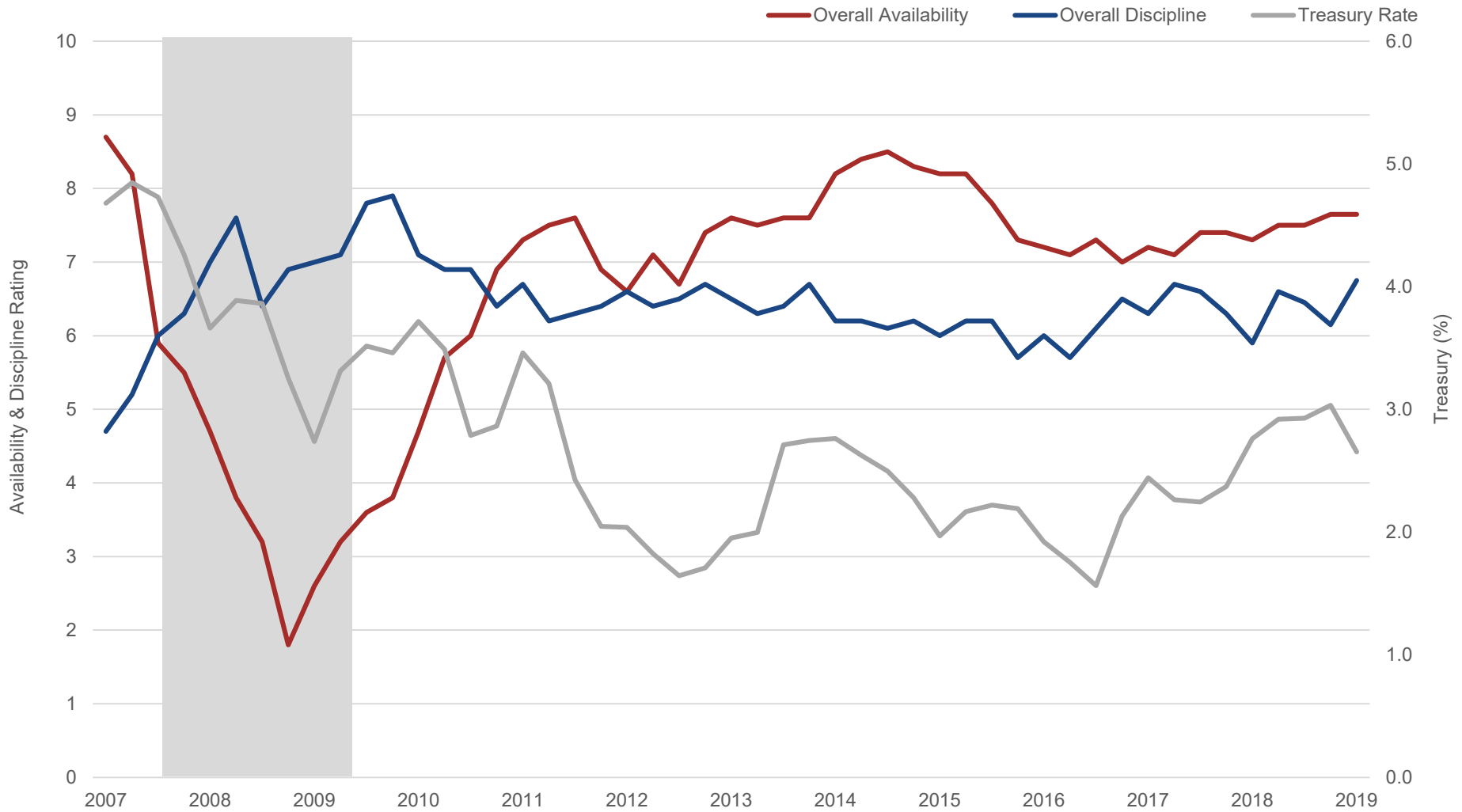
⁶Year-to-date (YTD) averages are not compounded annually except for CPI and NAREIT.

Sources BLS, Federal Reserve Board, S&P, Dow Jones, NCREIF, NAREIT, compiled by Situs RERC, current as of 1Q 2019.

SITUS RERC RATINGS OF INVESTMENT ALTERNATIVES



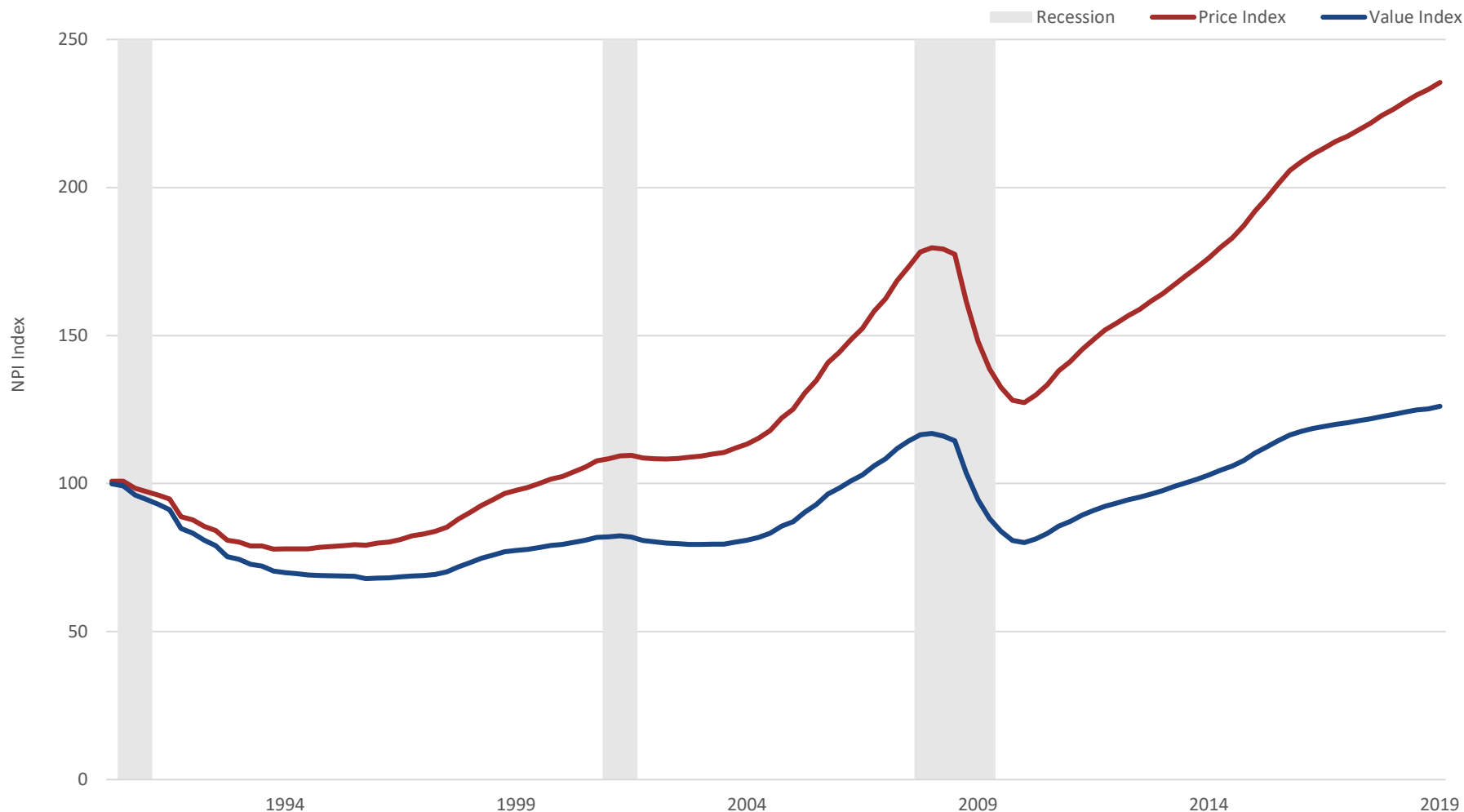
Source Situs RERC, 1Q 2019.



Ratings are based on scale of 1 to 10, with 10 being excellent. Shaded area indicates recession.

Source Situs RERC, 1Q 2019.

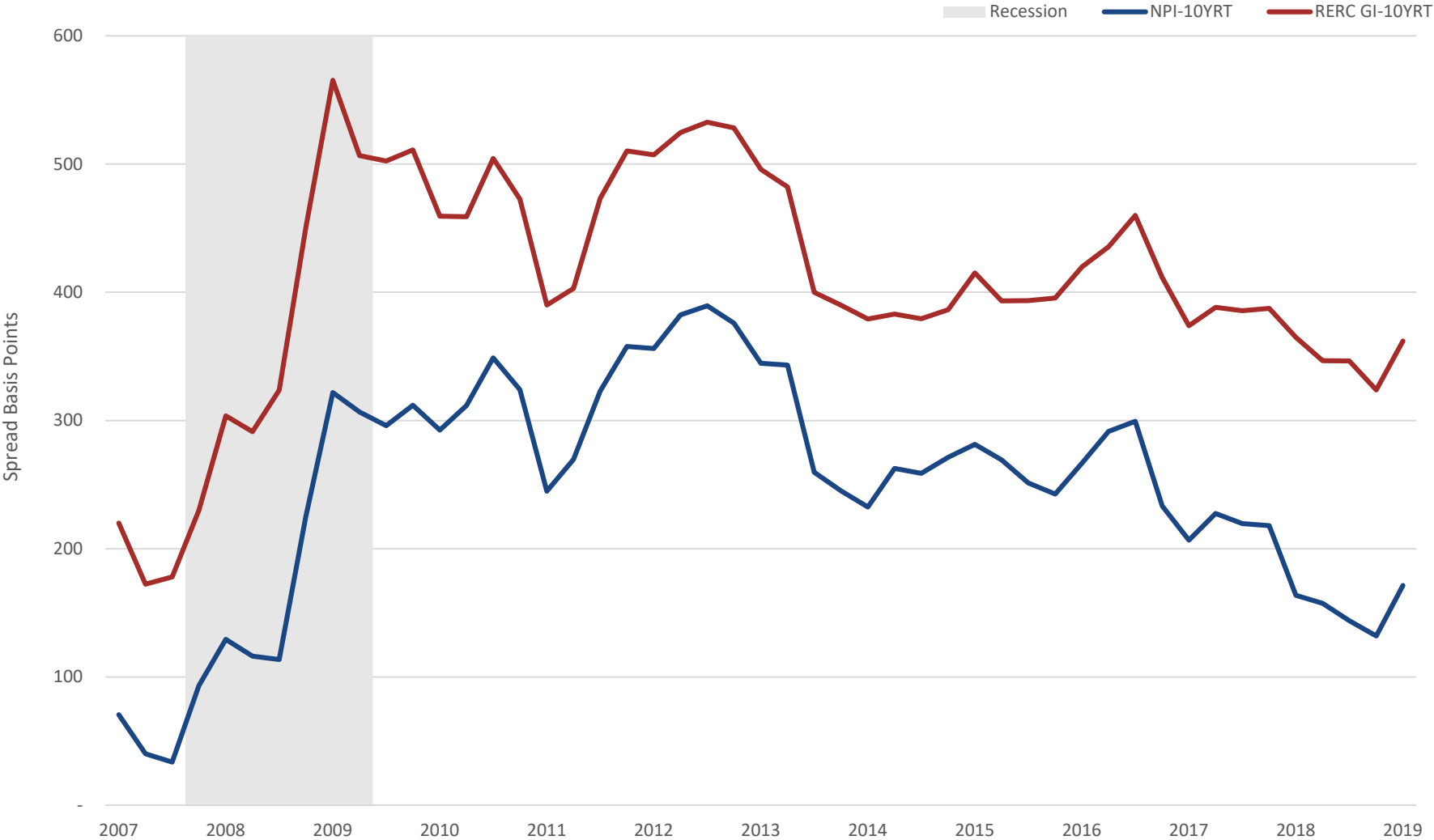
SITUS RERC PRICE AND VALUE INDEXES



Note: Price index combines capital expenditures and capital returns. Value index represents capital returns only. Price Index from 1Q 1990 to 1Q 2019 = 135.46%. Value Index from 1Q 1990 to 1Q 2019 = 26.08%. Shaded area indicates recession.

Sources Situs RERC, NCREIF, 1Q 2019.

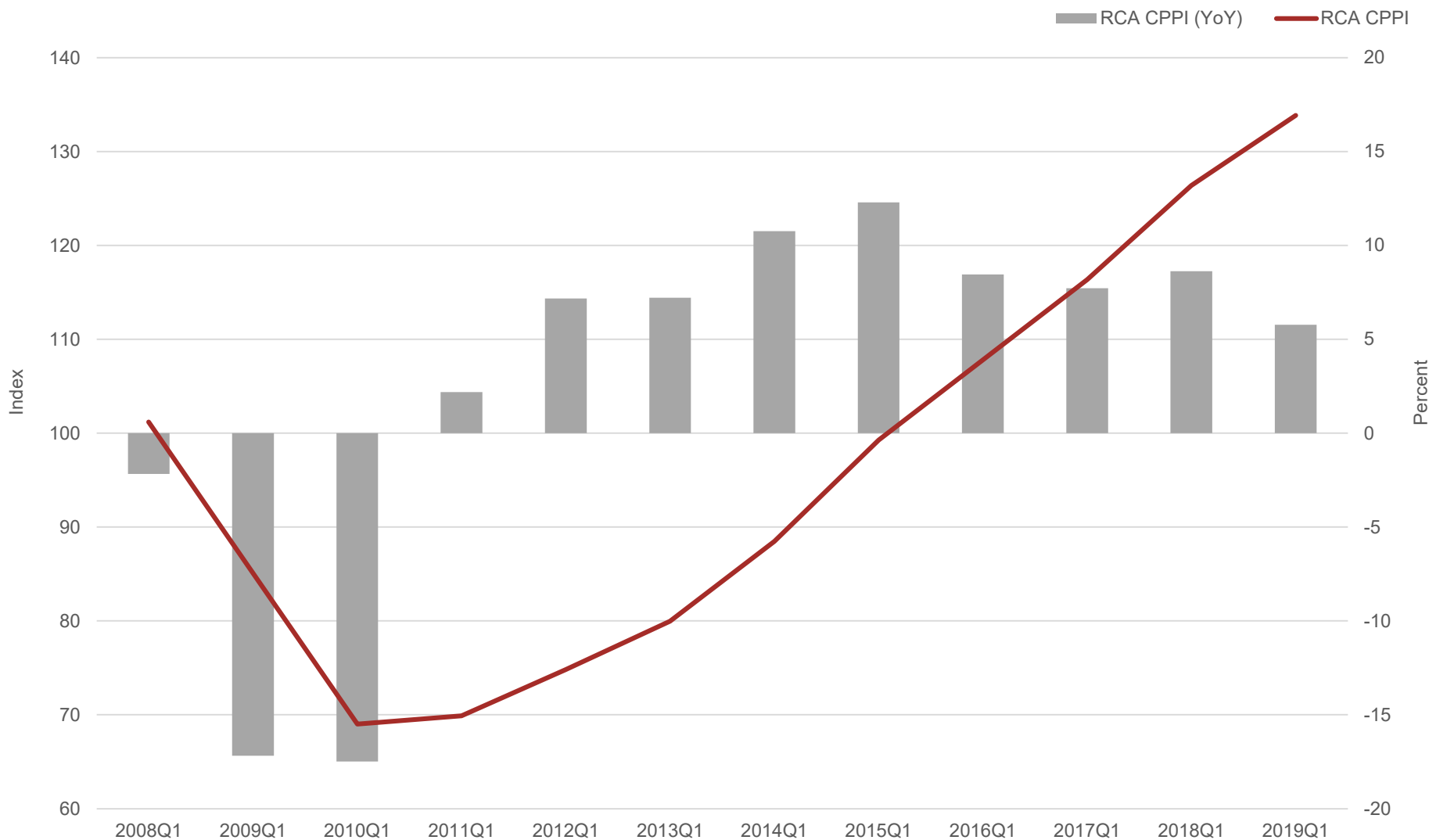
SITUS RERC RATE SPREADS OVER 10-YEAR TREASURY



Note: 10-year Treasury data are based on quarterly averages. Shaded area indicates recession.

Sources Situs RERC, Federal Reserve, current as of 1Q 2019.

CRE PRICING: NATIONAL ALL-PROPERTY



The RCA CPPI is based on repeat-sales (RS) transactions that occurred at any time up through the month of the current report.

Source Real Capital Analytics, 1Q 2019.

PROPERTY TYPE OVERVIEW

Industrial

- Most favorable near-term fundamentals of all the main property types
- Vacancy rates expected to remain near record lows for warehouse and data centers
- A rise in new business formation of small manufacturing companies that sell their goods via e-commerce will likely increase demand in the flex sector
- Industrial still has pricing power amid continued investor interest

Apartment

- Outlook appears to be steady in the short term, with continued investor appetite and rising property values
- As housing shortages continue in major markets, supply and demand characteristics will remain favorable
- Overall average cap rates expected to stabilize or possibly increase in 2019
- Given the transaction volume and pricing, apartments will likely continue to be a preferred property type for investors
- A shift on the demand side with renters turning into homebuyers could have a major impact on this sector

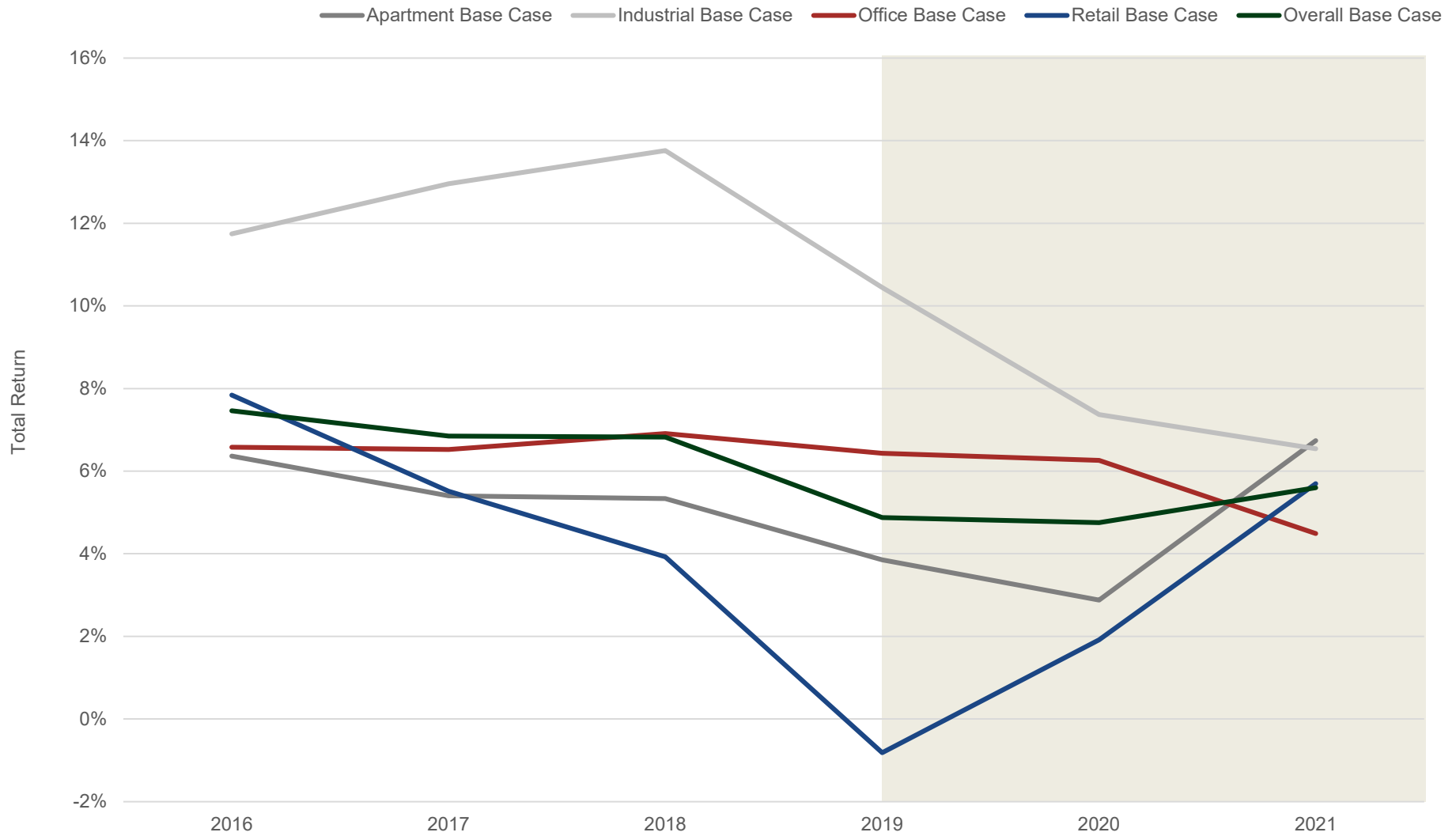
Office

- Steady employment continues to support the office sector; however, it is likely that tenants will reduce their space needs as technology transforms the way work is done
- Lack of newer, first-tier properties and nominal new construction may lead to slightly increasing rents in desired submarkets
- It will likely be more challenging to find the best-valued office markets
- Structural changes to the office market (space optimization, technology) present headwinds for the sector
- Newly constructed office space is still in high demand. Investors should be wary of the large expenses that are required to modify existing buildings.

Retail

- Structural changes to the sector, including e-commerce, oversupply of space, shifting consumer shopping patterns and grocery delivery chains, present long-term challenges across all types of retail
- Capital appreciation is expected to decrease over the next two years
- Modest growth, with rents increasing by about 1.5% over the year
- Technology and customer demands will change the retail landscape as service and experiential space becomes key for the retail industry

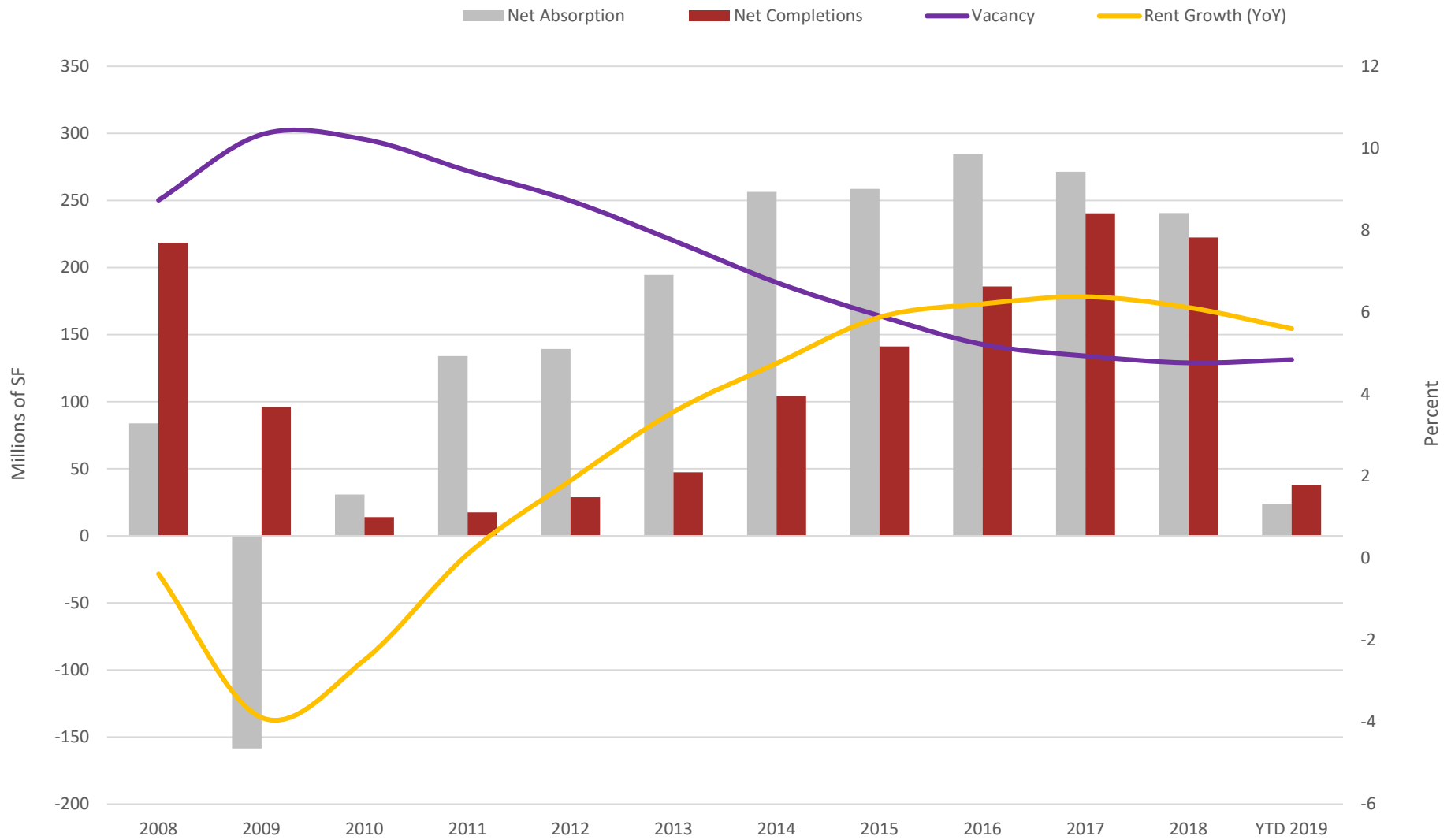
SITUS RERC TOTAL RETURN FORECAST BY PROPERTY TYPE (BASE CASE)



The total return forecast is Situs RERC's proprietary model based on Situs RERC data and data from NPI-ODCE, and is for leveraged, institutional-grade properties. Total returns are derived from an income component and a capital appreciation/depreciation component. Shaded area reflects forecast.

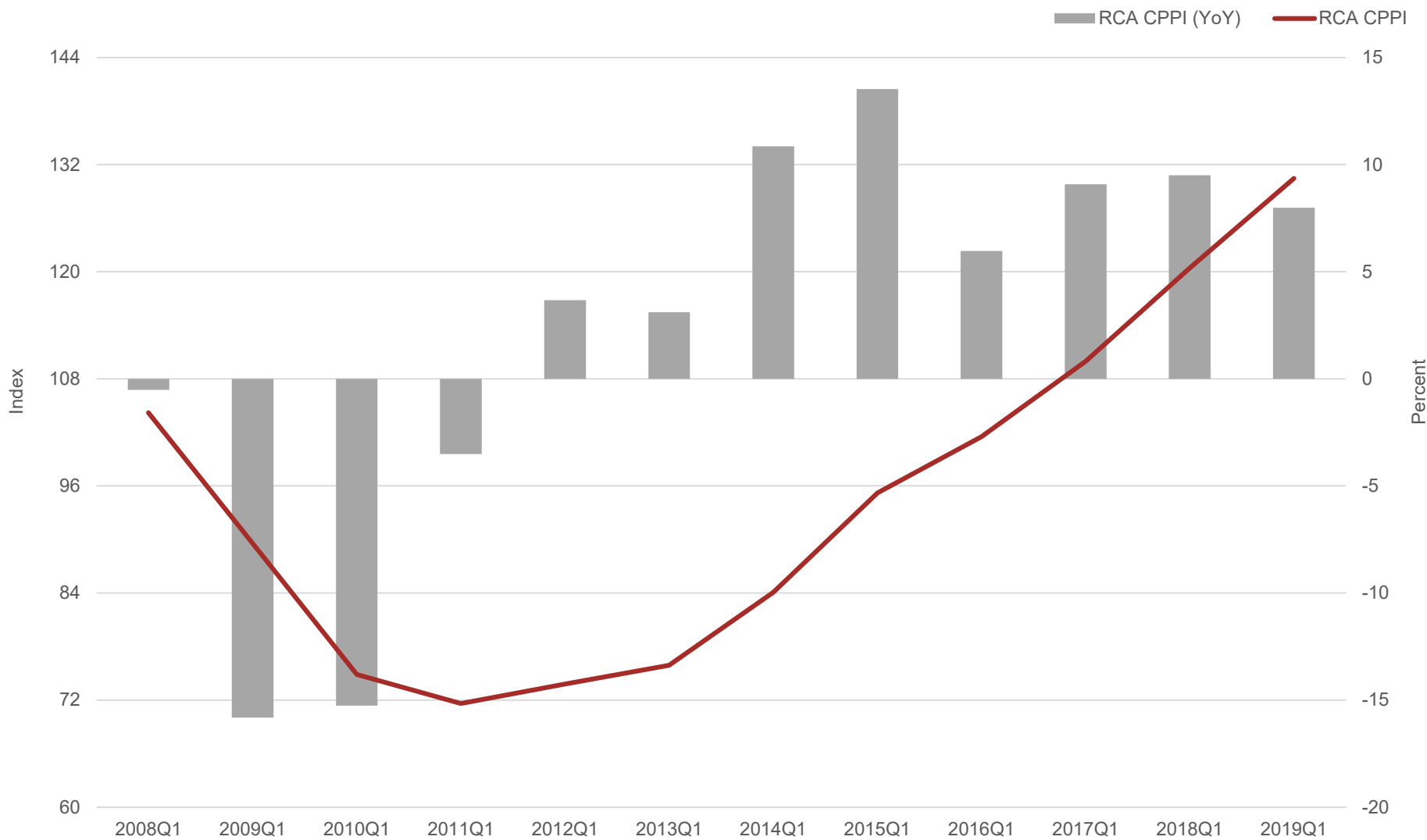
Source Situs RERC, NPI-ODCE, 1Q 2019.

INDUSTRIAL PROPERTY TYPE FUNDAMENTALS



The information is provided "As Is" and without any representations, warranties or guarantees.

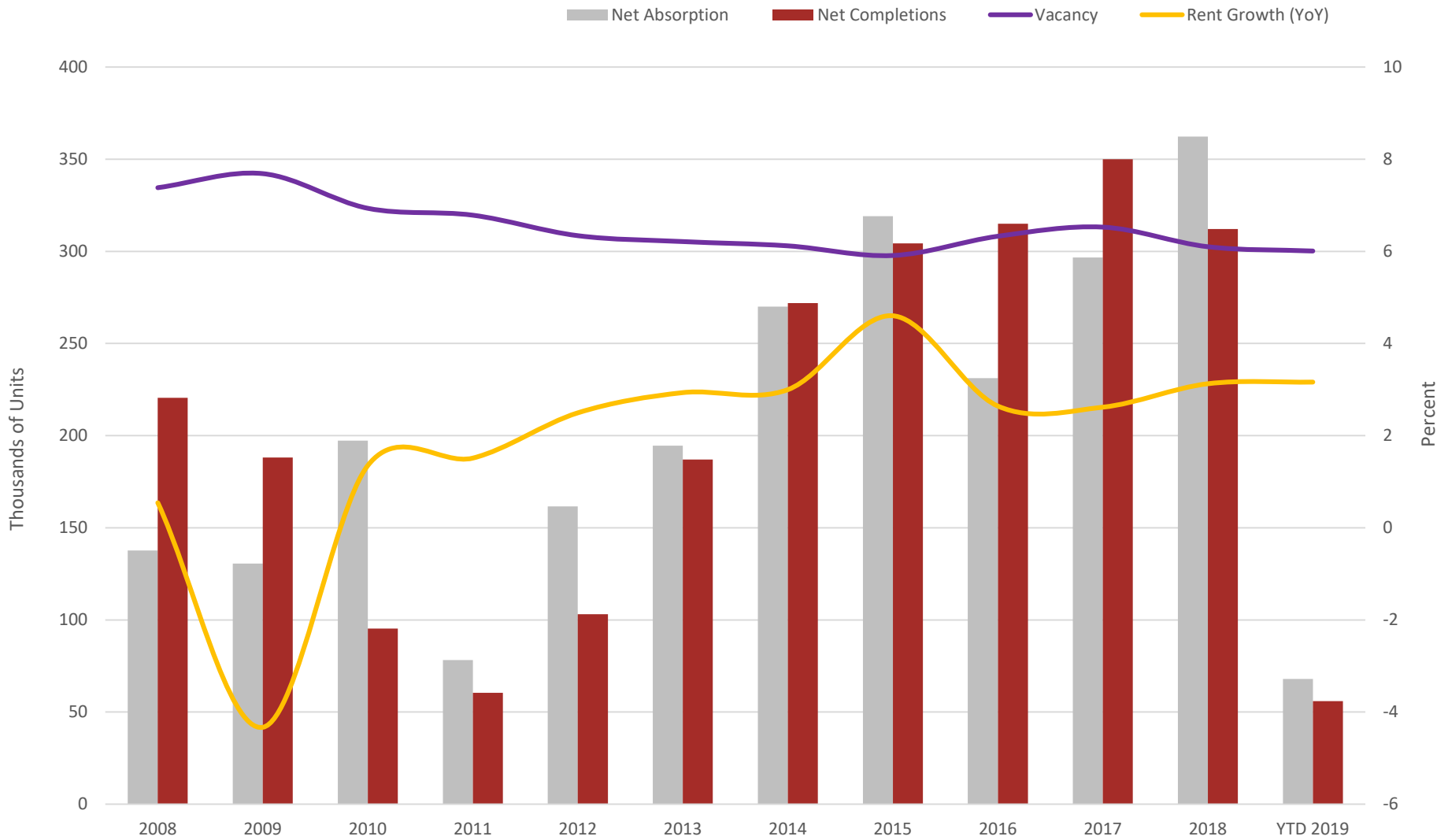
Source CoStar Market Analytics (www.costar.com), 1Q 2019.



The RCA CPPI is based on repeat-sales (RS) transactions that occurred at any time up through the month of the current report.

Source Real Capital Analytics, 1Q 2019.

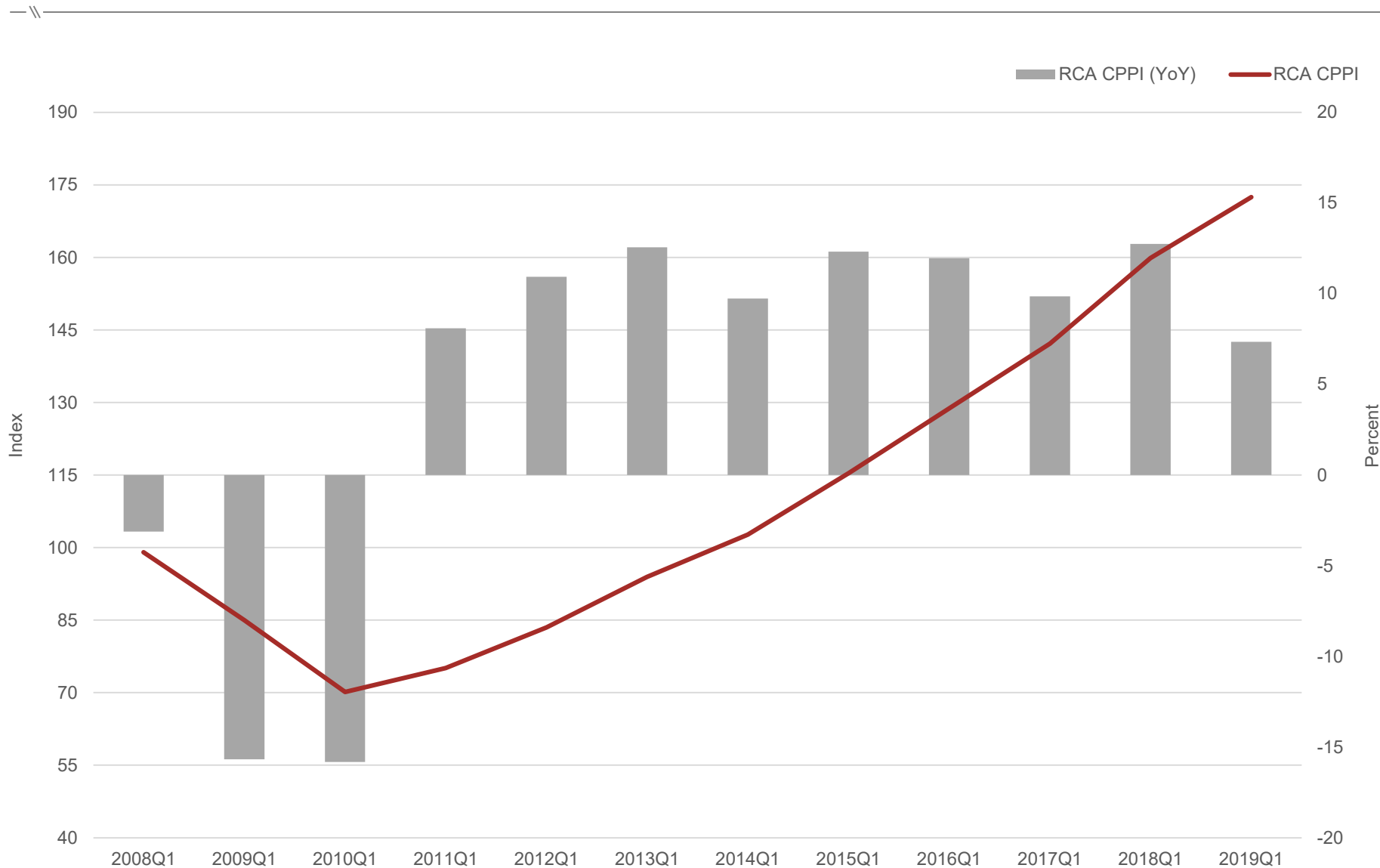
APARTMENT PROPERTY TYPE FUNDAMENTALS



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Source CoStar Market Analytics (www.costar.com), 1Q 2019.

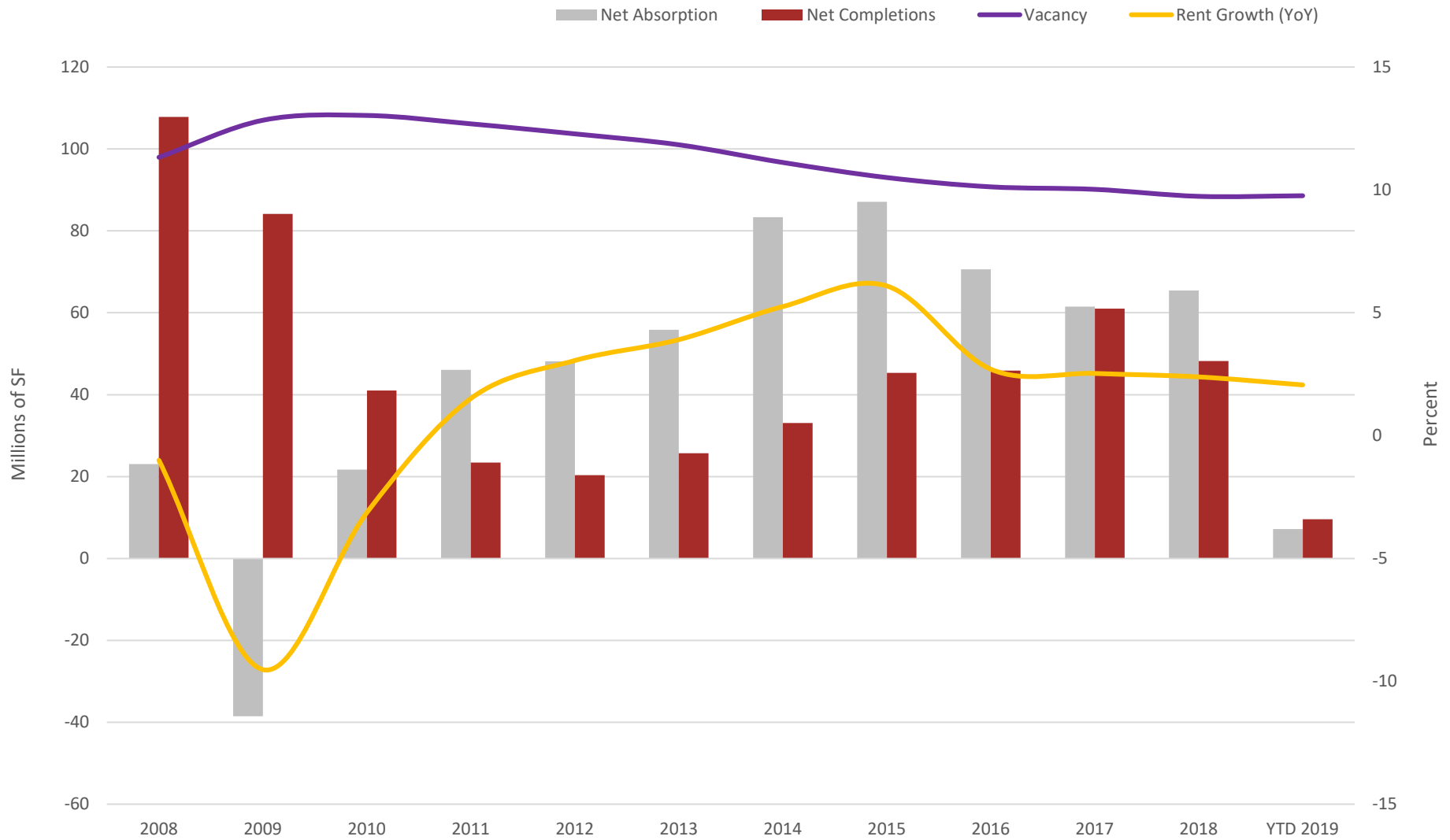
CRE PRICING: APARTMENT



The RCA CPPI is based on repeat-sales (RS) transactions that occurred at any time up through the month of the current report.

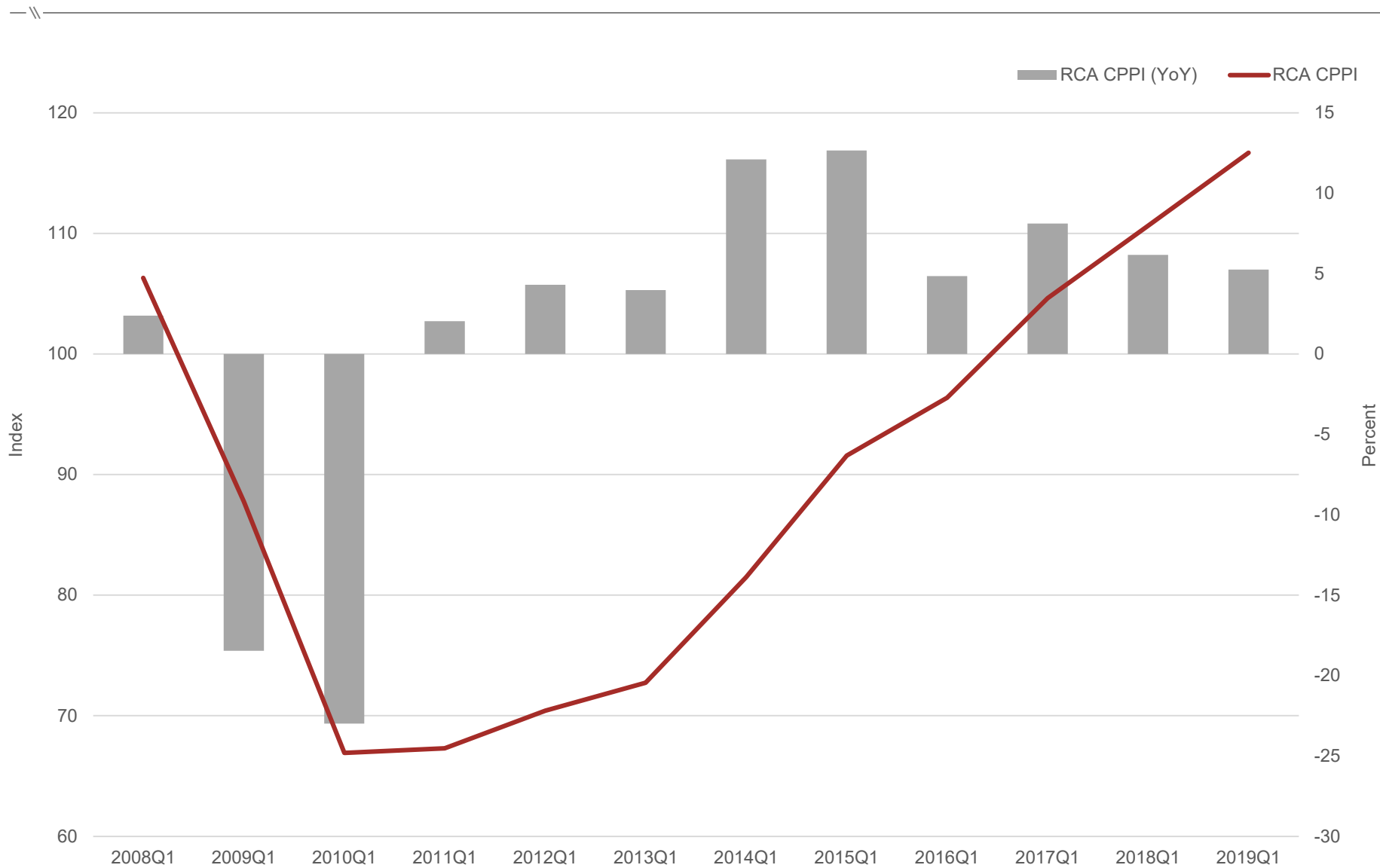
Source Real Capital Analytics, 1Q 2019.

OFFICE PROPERTY TYPE FUNDAMENTALS



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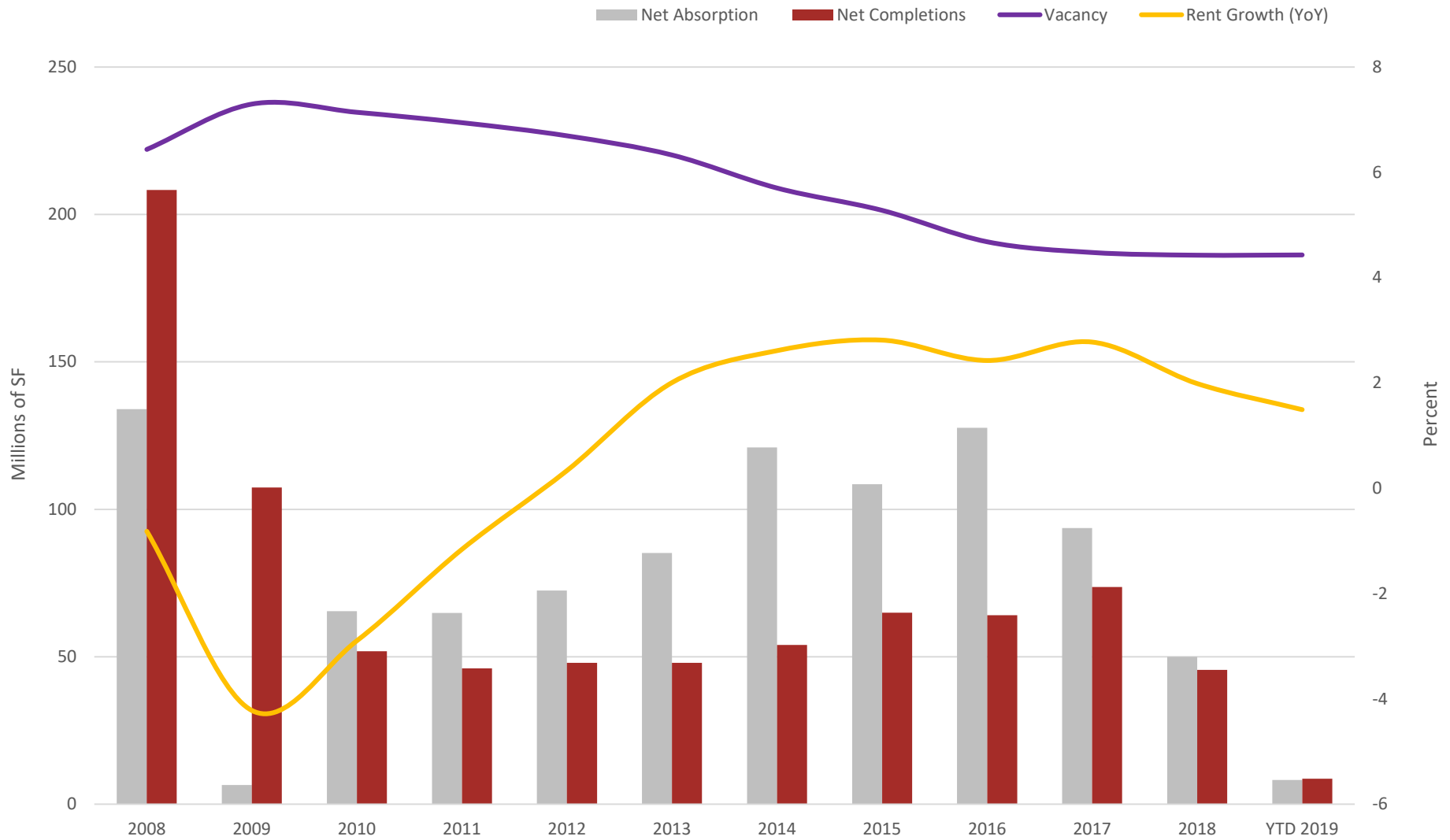
Source CoStar Market Analytics (www.costar.com), 1Q 2019.



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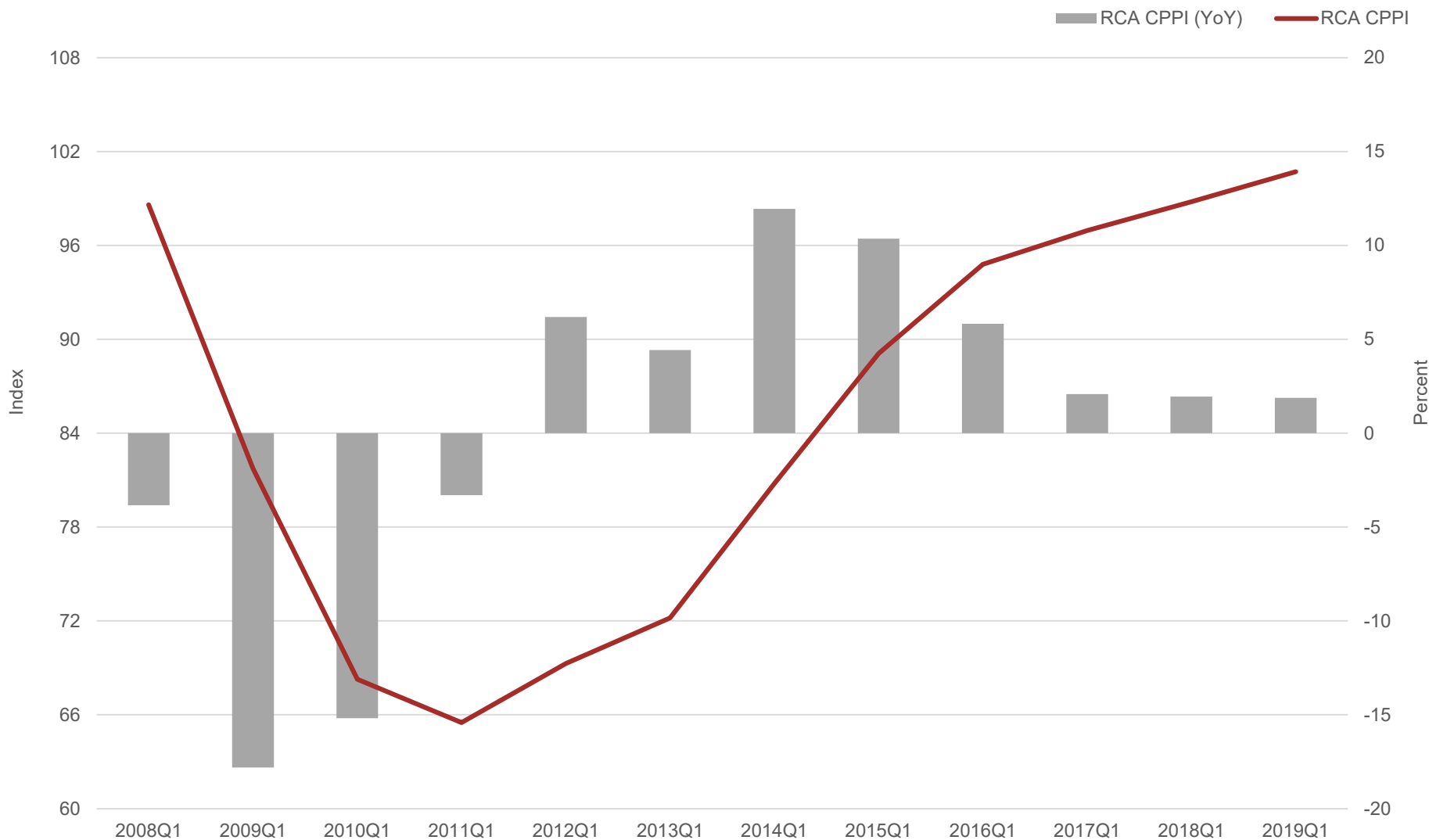
Source Real Capital Analytics, 1Q 2019.

RETAIL PROPERTY TYPE FUNDAMENTALS



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Source Real Capital Analytics, 1Q 2019.

REGULATORY FOCUS

Continue to watch for the impact of fiscal policies, including tax policies, in certain areas:

- California Prop 13: On the ballot for 2020. This would dramatically increase taxes for commercial properties, some of which under the original Prop 13 have not had their values reassessed since 1978. According to the San Francisco Chronicle, It could cost commercial property owners an additional \$11 billion a year in property taxes.
- San Francisco Prop C: Currently in effect, the imposed tax is on businesses that receive income from the lease or sublease of commercial space in San Francisco county. It is observed that many new leases pass the expense through to the tenants, though long-term in-place leases could have a bigger impact on the bottom line.
- Seattle Taxes: In King County (Seattle) for any portion of a sale over \$3.0M, beginning in 2020. For Seattle, if a 3% cost of sale was typical in the past, it will be common to see a 5% cost of sale applied to valuations. This will start being captured in 2Q 2019 valuations.
- Hawaii Tax for Rental Income: The statewide tax rate is 4.0% on all gross rents, but starting in 2019, Oahu and Kauai have a 0.5% surcharge, and Maui has a 0.25% surcharge.
- Chicago Fiscal Health: Chicago's poor fiscal health could result in significant tax hikes. With a new Cook County assessor in office, Fritz Kaegi, changes are expected, particularly to commercial properties. The assessor is also looking for legislative change that would require income-producing properties to disclose rent, income and expense information.
- New York City's pied-à-terre tax: A new tax on real estate transfers will take effect on July 1 (except for sales with signed contracts as of April 1). While mostly targeting buyers of high-priced houses and condos, the Wall Street Journal estimates that nearly 40% (approximately \$160 million per year) will be paid by owners of commercial properties.

THANK YOU!