

## Real Estate Capital Markets Update – February 21, 2005

### Volume 7, Number 2

Welcome to the update of ULI's Real Estate Capital Markets Web site. Updates are divided into four sections: public real estate securities markets, public real estate debt markets, private real estate equity markets, and private real estate debt (mortgage) markets. In each section, we feature Real Estate Capital Markets Scoreboards detailing selected performance indices for each of the real estate capital markets.

To expand site users' knowledge and understanding of the real estate capital markets, we will publish "knowledge" papers describing underlying market mechanics. In addition, we have provided links to other Web sites that provide related and relevant information. [Click here for links to other Web sites.](#)

Frequently Asked Questions (FAQs): In addition to knowledge papers, we have published answers to FAQs about the real estate capital markets. To go to FAQs, [click here.](#)

Glossaries of frequently used terms are available for readers' use. To go to the glossary section, that includes selected Web sites that provide glossaries and/or real estate term search engines, [click here.](#)

We want this site to be both useful and responsive to users, and we encourage you to e-mail comments and suggestions. If you want to send me an e-mail, click [stephen@uli.org](mailto:stephen@uli.org), add your comments, and click "Send".

### Special Comment: Note from the Editor

In response to suggestions from our readership, we have modified the format of ULI's Real Estate Capital Markets Update by moving the Real Estate Capital Markets Scoreboards previously interspersed in each section to the end of each section. We believe this will enhance the readability and clarity of the publication and welcome additional suggestions from readers on ways we can improve the utility of this publication.

Interest Rate Monitor					
Date	Federal Funds Rate	Prime Rate	10-Year Treasuries	3-Month Libor	Date of Federal Reserve Board Meeting
2/18/05	2.50%	5.50%	4.26%	2.85%	March 22, 2005

### Special Comment: Alice Connell, Group Managing Director, TIAA/CREF, to be Guest Speaker at 3<sup>rd</sup> ULI Real Estate Capital Markets Conference Call

We are pleased to announce that Alice Connell, Group Managing Director of TIAA/CREF, will be the next guest speaker on ULI's Real Estate Capital Markets Conference call. The call is scheduled for April 5, 2005, from 11:00 to 11:45 am, Eastern Standard Time. If you would like to suggest a question for the call, please e-mail [blank@uli.org](mailto:blank@uli.org).

The call-in number will be: 1-719-785-9359

The participant code will be: 508131

The call will be recorded and available for playback for 30 days.

The replay call-in number will be: 1-719-457-0820

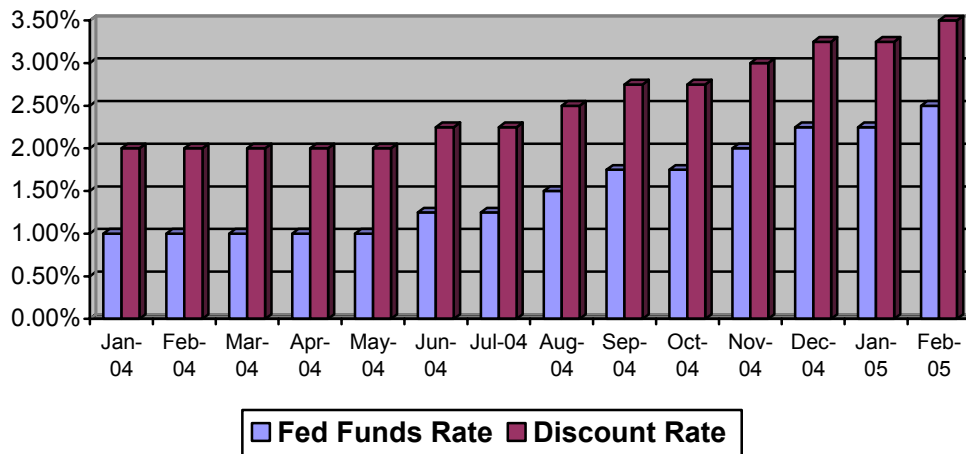
The replay pass code will be: 64743601

**Special Comment: Notes from “The PunchLine...”**

“No Easy Sailing in 05”

“The world economy enjoyed one of the strongest and most balanced performances in decades during 2004. No major region faces a downturn, but growth is obviously centered primarily on the U.S. and China. The U.S. Federal Reserve is now clearly concerned that rates have been held artificially low for too long, and the normalization of interest rates and possibly credit spreads may turn out to be one of the linchpin development of 2005-6. Despite the growth momentum, gross imbalances remain, including the U.S. trade imbalance, the awkward nature of international money flows, currency market developments, and the powerful search for yield that has kept the technical bid for credit amazingly robust. It is noteworthy that correlation among markets may turn out to be stronger than widely appreciated, as so many of the growth engines or performance factors are interrelated.”

**Federal Funds Target Rate and Discount Rate**



## Special Comment: Federal Reserve Board Raises Federal Funds Rate; Chairman Greenspan Testifies Before Congress

As projected, expected, anticipated, and discounted (by the markets), the Federal Reserve Board (FRB) increased the Federal Funds Rate 25 basis points (0.25%) to 2.50% at its meeting held on February 2, 2005. Simultaneously, the FRB increased the Discount Rate 25 basis points to 3.50% and major money center commercial banks increased their Prime Lending Rate 25 basis points to 5.50%. If you have not been keeping count, this is the sixth rate increase by the FRB since June 2004. Analysts consensus is that there will be a minimum of four additional 0.25% rate increases during the balance of 2005.

In his semi-annual report to Congress, FRB Chairman Alan Greenspan made it abundantly clear that the FRB would continue its campaign of increasing short term interest rates, stating: “The cumulative removal of policy accommodation to date has significantly raised measures of the real federal funds rate, but by most measures, it remains fairly low.”

Chairman Greenspan noted that he was “puzzled” by the recent decline in long-term interest rates as it is more common for short-term and long-term rates to move in tandem. (In the two trading sessions following his testimony before Congress, the yield on 10-year Treasury bonds increased 10 basis points (0.10%), assumedly in response to Chairman Greenspan’s remarks).

<b>Real Estate Capital Markets Scoreboard: Money Rates</b>	<b>February 18, 2005</b>
Prime Rate (Base rate on corporate loans by the largest commercial banks)	5.50%
Federal Funds Rate (Rate banks charge other banks for overnight loans)	2.50%
Discount Rate (Rate charged banks who borrow overnight from the FRB)	3.50%
Dealer Commercial Paper (Rate for high grade unsecured notes sold by major corporations)	2.52% - 30 days 2.65% - 60 days 2.76% - 90 days
London Inter-bank Offered Rate (LIBOR) (Rate on deposit-based transactions between banks in the Eurocurrency market)	2.60% - 1-month 2.85% - 3-months 3.08% - 6 months 3.42% - 1 year
U.S. Treasury Securities	4.26% - 10-year

### Public Real Estate Securities Capital Markets

While 2004 was a banner year for real estate investment trust investors, 2005 is off to a rocky start with January’s results showing significantly volatility. According to the National Association of Real Estate Investment Trusts ([www.nareit.com](http://www.nareit.com)), publicly-traded real estate investment trusts (REITs) finished January down 8.4%.

The following chart details total returns by property sector as well as dividend yields by property sector for January 2005:

Property Sector	Total Return	Dividend Yield
Office	-8.34%	5.21%
Industrial	-10.01%	4.42%
Office/Industrial	-8.55%	5.79%
Shopping Center	-8.95%	4.86%
Regional Mall	-9.37%	4.51%
Freestanding Retail	-5.54%	4.84%
Apartment	-10.13%	5.36%
Manufactured Home	-5.85%	4.94%
Diversified	-7.40%	5.43%
Lodging/Resort	-6.23%	2.98%
Healthcare	-8.01%	6.58%
Self-Storage	-5.75%	4.15%
Specialty	-7.16%	4.74%
<b>NAREIT Equity REIT Index</b>	<b>-8.40%</b>	<b>5.04%</b>
Source: National Association of Real Estate Investment Trusts.		

There are lots of explanations for January's rout, ranging from profit taking after 2004's spectacular performance to changes in the interest rate environment to sector rotation to REITs trading above net asset value to REITs trading at historically high multiples to...you get the idea. Suffice it to say, one month does not a market make.

What is clear is that there is a wide divergence in real estate securities analysts' estimates of projected REIT performance for 2005 with the performance range bracketed between -18.0% to +10.0%, including dividends.

Real Estate Capital Markets Scoreboard: Public Securities and Real Estate Performance Indices as of February 18, 2005						
	Dow Jones Industrial Average	S&P 500 Stock Index	NASDAQ Composite Index	Russell 2000 Index	Morgan Stanley REIT Index	NCREIF All Property Index
2005	+0.02%	-0.85%	-5.37%	-3.29%	-3.91%	+14.5%*
* Trailing 12-months ended December 31, 2004.						

Real Estate Capital Markets Scoreboard: Market Capitalization of REITs (number of shares multiplied by share price in \$ millions) as of January 31, 2005								
	# of REITs	Market Cap	Equity REITs	Market Cap	Mortgage REITs	Market Cap	Hybrid REITs	Market Cap
2005	193	307,894	153	275,291	33	25,964	7	6,639
Source: National Association of Real Estate Investment Trusts (NAREIT).								

Real Estate Capital Markets Scoreboard: Offerings of Securities by REITs (in \$ millions) as of January 31, 2005				
	2004		2005	
	# of Offerings	\$ Value	# of Offerings	\$ Value
Initial Public Offerings	29	\$8,271	1	\$350
Follow-on offerings-Common Shares	79	7,338	4	291
Follow-on Offerings-Preferred Shares	61	5,858	1	80
Unsecured Debt	97	17,306	2	375
Secured Debt	0	0	0	0

Source; National Association of Real Estate Investment Trusts.

### Public Real Estate Debt Capital Markets

Issuance of commercial mortgage-backed securities (CMBS) continued apace in January with \$12 billion in CMBS issued in the U.S. markets and \$1.3 billion in CMBS issued in the international markets.

As the chart below indicates, trading spreads continued to narrow across the entire rating spectrum, evidence of continuing and significant institutional investor interest in the sector. Rates in the CMBS lending market remain extremely attractive with originators reporting applications for both newly originated loans as well as re-financings as “brisk”.

In a recently published analysis of global issuance of CMBS in 2004, *Commercial Mortgage Alert* reported that approximately 66% of the collateral underlying CMBS was from the office (35.4%) and retail (30.5%) sectors, followed by multifamily (12.3%), warehouse/industrial (7.6%), hotel (7.0%), mobile home park (2.6%), nursing home/retirement (0.7%), and “other” (3.8%).

Issuance of Commercial Mortgage-Backed Securities January 1, 2000 through February 18, 2005(in \$ Millions)			
	U.S. Assets	Non-U.S Assets	Total Issuance
2000	46,849.4	12,116.4	59,010.8
2001	67,149.9	22,713.8	89,863.7
2002	52,073.3	28,705.9	80,779.1
2003	77,848.1	20,802.9	98,651.0
2004	93,838.2	33,746.0	127,584.2
2005	12,000.00	1,300.0	13,600.0

Source: Commercial Mortgage Alert.

Real Estate Capital Markets Scoreboard: Commercial Mortgage-Backed Securities Trading Spreads above 10-Year Treasury Bonds (in Basis Points)						
	Trailing 12-Months			12/29/04	2/18/05	YTD +/-
	Low	High	Average			
10-Yr. Treasury Bonds	3.71%	4.81%	4.26%	4.32%	4.15%	+0.07%
AAA	+60	+85	+74	+70	+60	-10
AA	+67	+92	+81	+77	+67	-10
A	+76	+103	+90	+85	+76	-9
BBB	+114	+143	+128	+127	+123	-4
BBB-	+154	+176	+167	+167	+163	-4
BB	+310	+415	+367	+325	+310	-15
B	+750	+950	+841	+770	+750	-20

### Private Real Estate Equity Capital Market

The National Council of Real Estate Investment Fiduciaries (NCREIF) recently reported the performance of its property index (which is comprised of 4,152 properties having a market value of approximately \$145.4 billion) for the fourth quarter 2004 as well as for the trailing 12-months ended December 31, 2004.

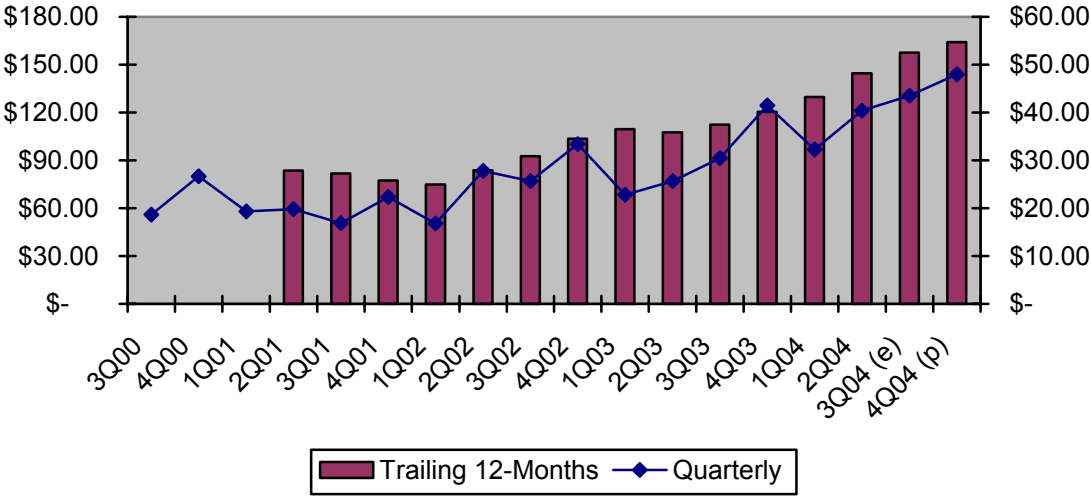
The Index noted an average total return (income plus appreciation) of 4.69% for the fourth quarter 2004 as compared to 3.42% for the third quarter 2004.

The following charts details the results for the fourth quarter 2004 as compared to the third quarter 2004 as well as for the trailing 12-months ended December 31, 2004. As indicated, the retail sector was the best performing property sector (as it has for the entire year) on both a quarter-over-quarter as well as trailing 12-month basis. All sectors provided total rates of return above 10.0% in calendar year 2004.

	4Q2004			3Q2004		
	Total	Income	Appreciation	Total	Income	Appreciation
Multifamily	4.00%	1.47%	2.53%	2.88%	1.46%	1.42%
Hospitality	3.37%	2.06%	1.31%	2.23%	2.20%	1.83%
Industrial	3.75%	1.83%	1.93%	2.74%	1.95%	0.79%
Office	3.74%	1.81%	1.93%	3.17%	1.87%	1.30%
Retail	7.83%	1.89%	5.94%	5.08%	1.83%	3.25%
<b>Total</b>	<b>4.69%</b>	<b>1.77%</b>	<b>2.92%</b>	<b>3.42%</b>	<b>1.80%</b>	<b>1.63%</b>

Trailing 12-Months Ended December 31, 2004			
	Total	Income	Appreciation
Multifamily	13.22%	6.08%	6.83%
Hospitality	10.16%	8.05%	1.99%
Industrial	12.07%	7.90%	3.94%
Office	12.02%	7.76%	4.03%
Retail	22.95%	7.71%	14.43%
<b>Total</b>	<b>14.52%</b>	<b>7.46%</b>	<b>6.70%</b>

**Sales of Office, Industrial, Retail, and Apartments**



Real Estate Capital Markets Scoreboard: Survey of Initial Capitalization Rates								
	Multi-Family	CBD Office	Suburban Office	Retail-Mall	Retail-Neighborhood	Retail-Power	Industrial-Warehouse	Industrial-R & D
2Q98	8.5%	8.5%	8.6%	8.3%	9.1%	9.2%	8.7%	8.8%
4Q98	8.8%	8.7%	8.9%	8.6%	9.5%	9.6%	8.9%	9.1%
4Q99	8.8%	8.9%	9.0%	8.5%	9.2%	9.6%	9.0%	9.3%
4Q00	8.7%	8.6%	9.3%	8.9%	9.4%	10.1%	8.9%	9.3%
4Q01	8.6%	9.2%	9.8%	8.9%	9.5%	10.2%	9.1%	9.7%
4Q02	8.0%	9.0%	9.7%	8.7%	9.2%	9.5%	8.9%	9.7%
4Q03	7.6%	8.4%	9.0%	7.9%	8.2%	8.4%	8.4%	9.2%
4Q04	7.2%	8.1%	8.5%	7.6%	7.7%	8.0%	8.0%	8.9%
<b>YTD</b>	<b>-0.4%</b>	<b>-0.3%</b>	<b>-0.5%</b>	<b>-0.3%</b>	<b>-0.5%</b>	<b>-0.4%</b>	<b>-0.4%</b>	<b>-0.3%</b>
Source: Real Estate Research Corp. ( <a href="http://www.rerc.com">www.rerc.com</a> ).								

### Private Real Estate Debt (Mortgage) Capital Markets

Interest rates for “prime” 10-year commercial mortgages remain within striking distance of historic lows with capital availability described as “plentiful” and “highly competitive”.

Real Estate Capital Markets Scoreboard: “Prime” 10-Year Commercial Mortgages						
	12/31/01	12/31/02	12/31/03	12/31/04	1/31/05	Year-to-Date
Prime Mortgages	7.33%	6.05%	5.80%	5.51%	5.42%	-0.09%
10-Year Treasuries	5.05%	3.81%	4.25%	4.22%	4.10%	-0.12%
Spread	2.28%	2.23%	1.65%	1.29%	1.32%	+0.03%
Source: Barron’s/John B. Levy and Company Survey.						