

The logo for RCLCO, with 'RCL' in black and 'CO' in white on a grey background.

RCLCO

A stylized illustration of a cityscape. The left side is purple with dark silhouettes of buildings and trees. The right side is a bright, colorful scene with a blue sky, a yellow sun, a green tree, and a tall white building with many windows.

Investing in a Volatile Market

RCLCO Institutional Advisory Services

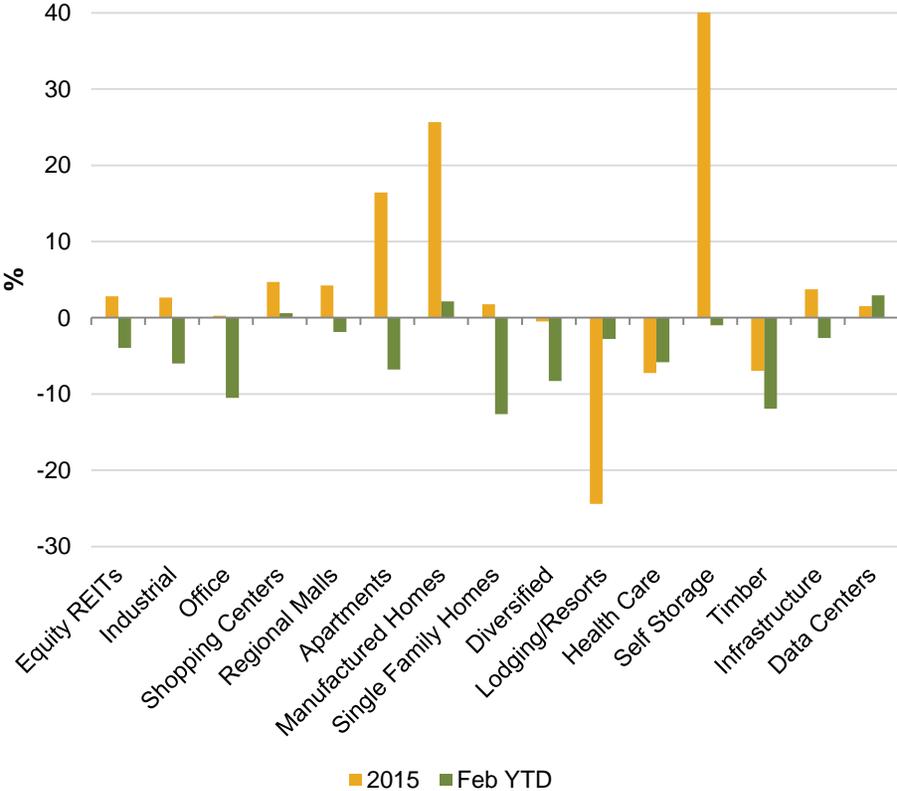
March 2016

REIT Markets are Recently Volatile: Are Private Markets Next?

**REIT Prices
Jan 1994-Jan 2016**



**REIT Total Returns
2015 vs. Feb 2016 YTD**

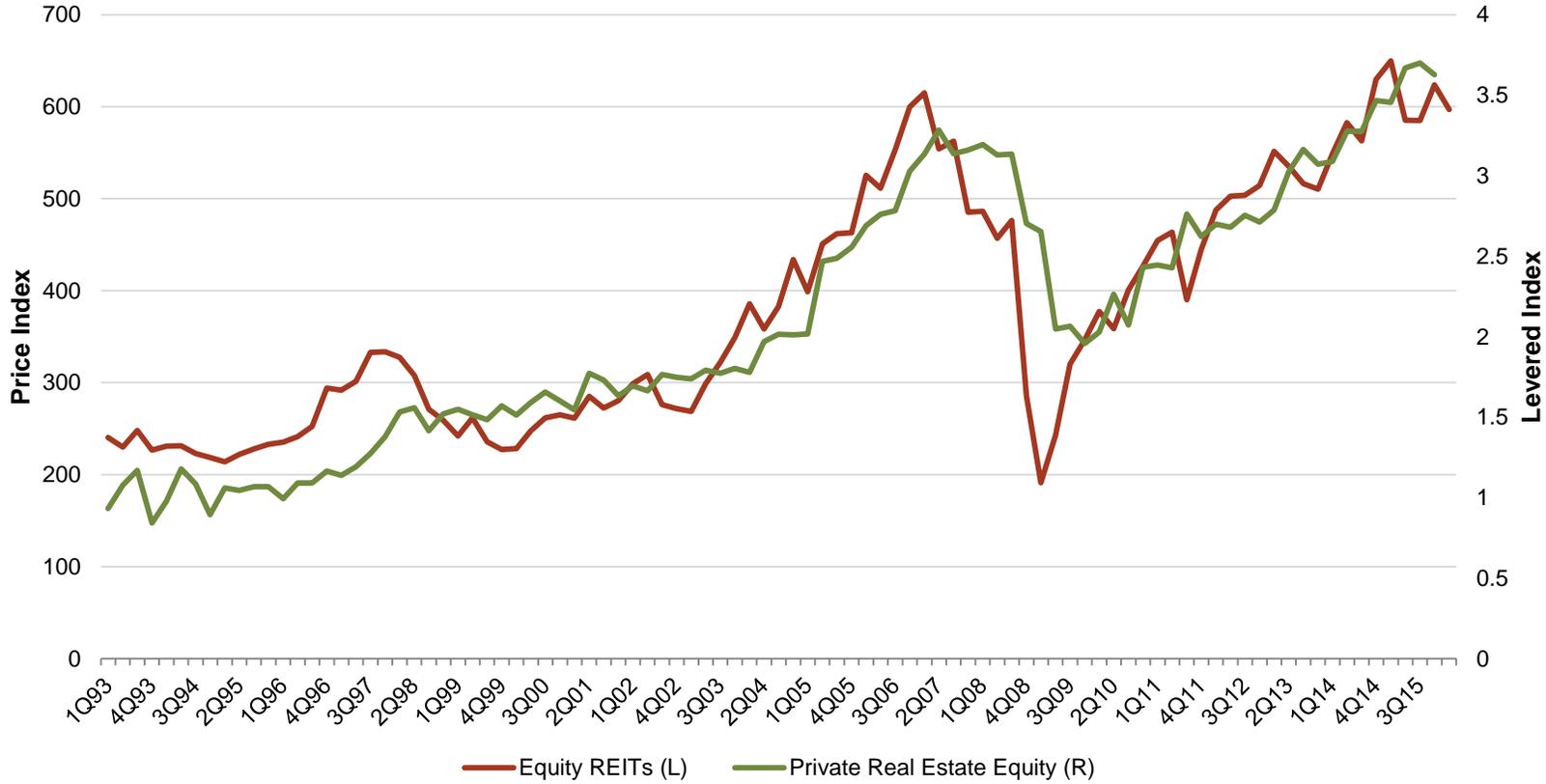


Source: NAREIT



Public REIT Pricing is Highly Correlated With—and Sometimes Leads—Private Real Estate Pricing

**Public & Private Real Estate Pricing
1Q 1993-Feb 2016**

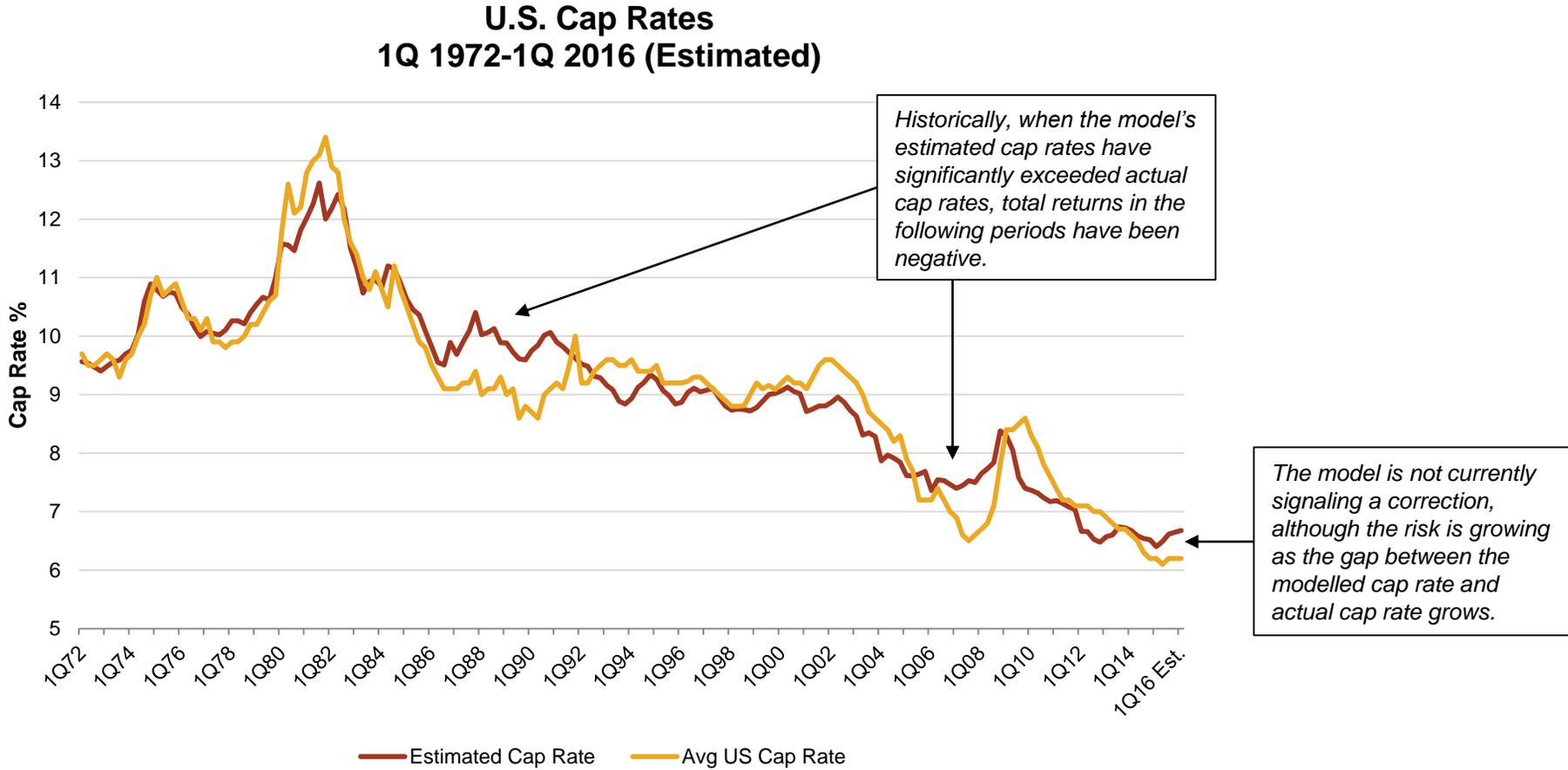


Source: NAREIT; NCREIF – TBI, estimated adjustment for 40% leverage



RCLCO's Pricing Model is Not Yet Showing Stress, but Risk is Increasing

Our pricing model compares pricing for private market real estate to other asset types and general capital market conditions. The model estimates average U.S. commercial cap rates over a long time period.



Source: RCLCO; NREI; RCA; Moody's



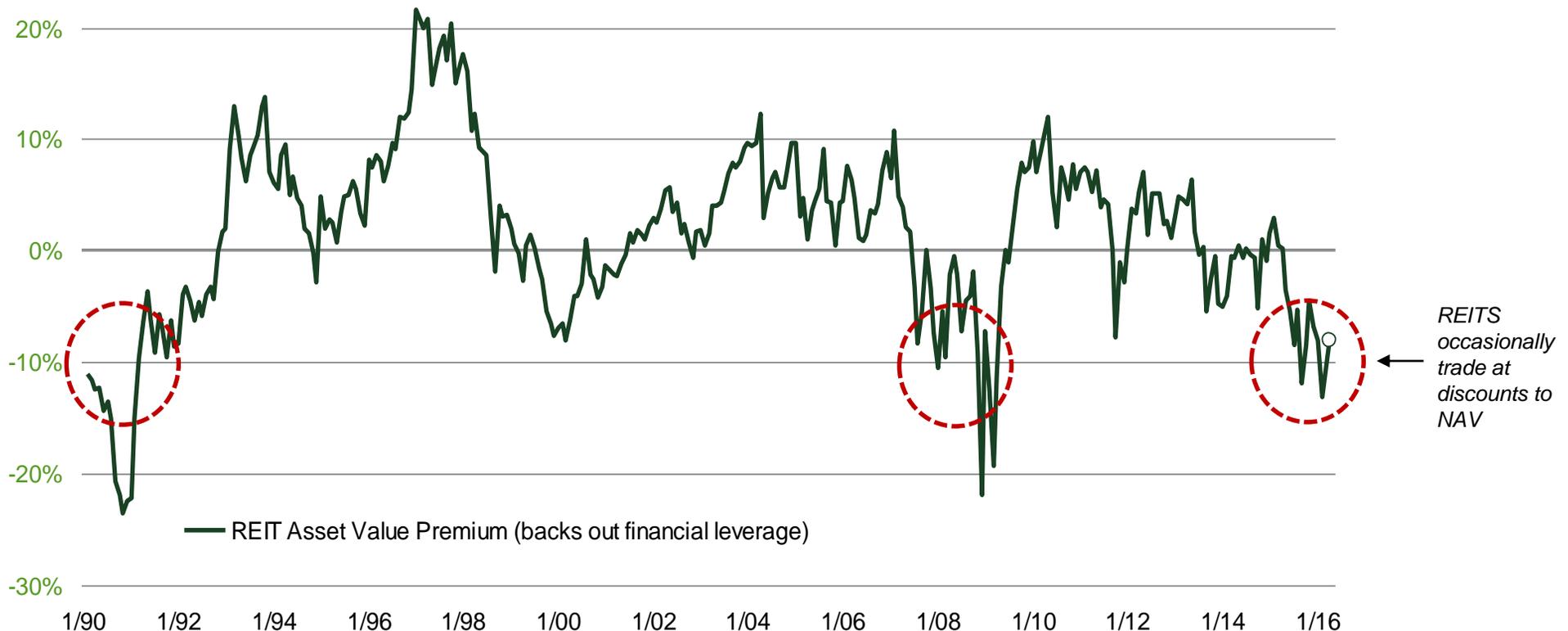
(Capital Market-Driven) Things to Do Now

- Watch for “point of entry” opportunities created by volatility in public markets.
- Develop a target market strategy to enable swift action if short-term pricing opportunities arise.
- Manage existing portfolios to minimize risk and maximize performance.
 - Manage leverage
 - Exposure to interest rate risk in variable rate loans.
 - Exposure to refinancing risk.
 - Use scenario analyses to understand debt coverage risk.
 - Manage portfolio structure
 - Does the portfolio structure allow forward liquidity if needed?
 - As the sector cycle matures, manage vintage and risk exposure, e.g. from leverage, lease-up, and construction.
 - Conduct prudent hold/sell analyses. Consider selling properties that are likely to experience volatility in the near term.

Watch for “Point of Entry” Opportunities: Volatility Can Create Short-Term Mispricing in Public and Private Markets

Watch for differences in pricing between public and private markets. REIT pricing could be an indication of private market pricing changes to come. Or, it could be a short-term opportunity to enter the market at a better price point than on the private side. Watch for REITs with strong property fundamentals. Pricing volatility could create short-term opportunities for go-private transactions, REIT share investing, or investing with private equity real estate funds that can move between public and private markets.

REIT Premiums and Discounts to Underlying Asset Value



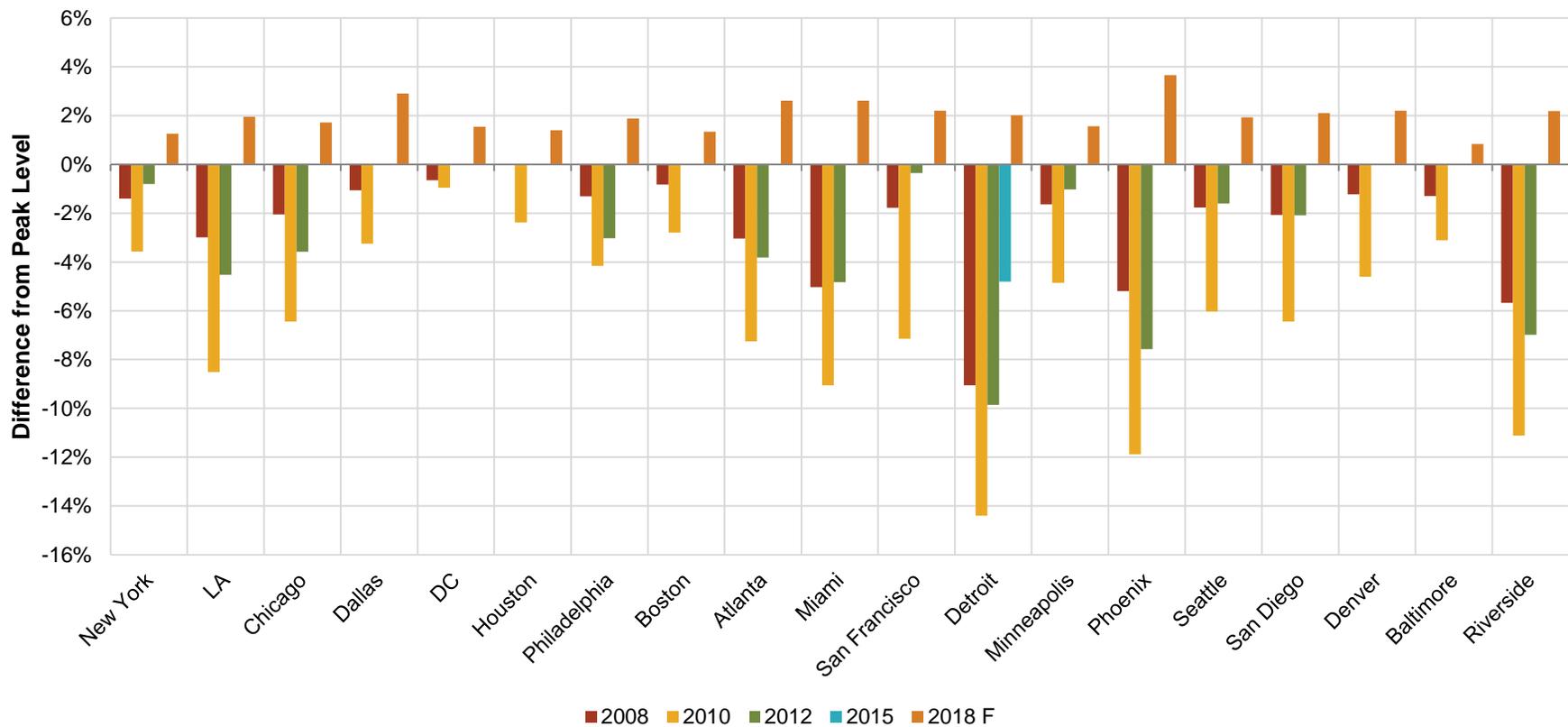
Source: Green Street Advisors. Data as of March 1st, 2016.


Green Street Advisors

Target Markets: Watch for Diverse, High-Growth Markets That Experience Less Volatility in Downturns—and Come Out of Recessions Sooner

Economic growth varies considerably at the local level—and some markets experience shallower and shorter recessions than others. While Washington, D.C., and Houston, TX came out of the last recession after shallow and short downturns, their dependence on a single industry (government and energy respectively) creates forward risk. Thus it is important to understand the economic structure of each market. Dallas, Boston, and Denver also experienced shallower downturns and recovered from the recession sooner. Conversely, markets such as Detroit, Phoenix, Riverside, and even Los Angeles and Miami were volatile and slow to recover from the last recession.

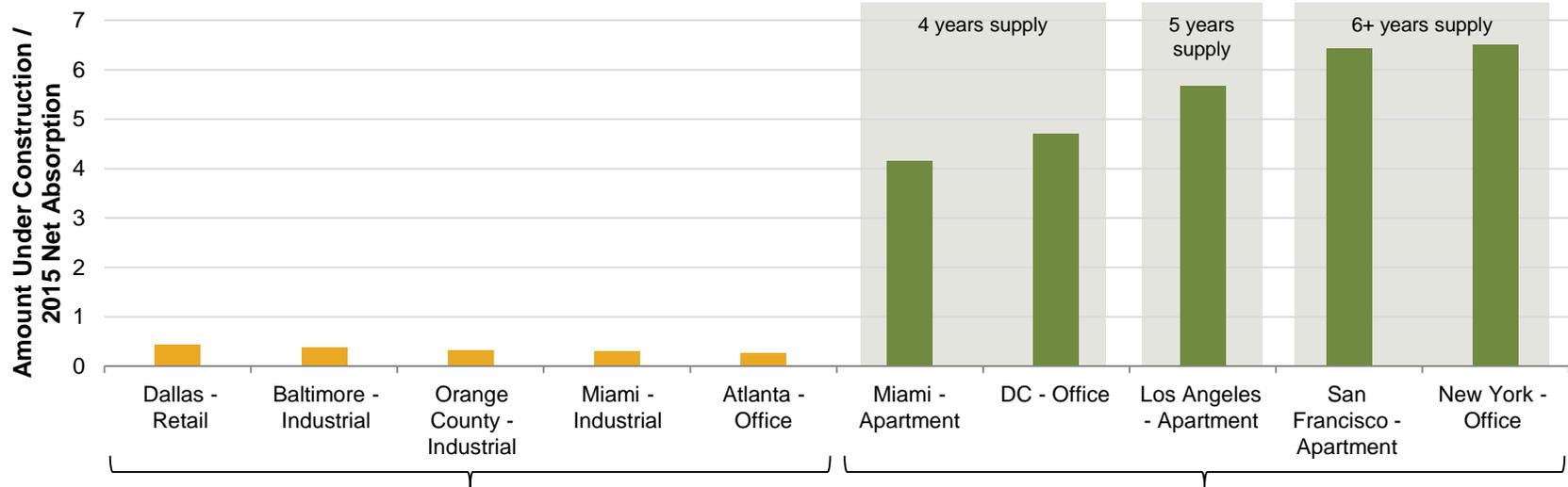
Total Employment as Compared to Peak



Note: Cities that do not display a value for 2015 (blue bar) have returned to peak employment.
 Source: Moody's Economy.com

Target Markets: Favor Good Forward-Looking Supply-Demand Balance

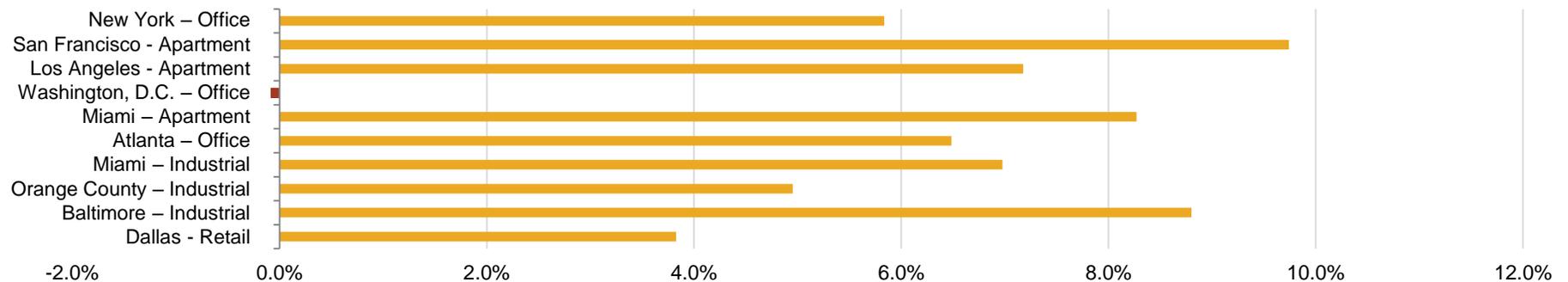
Construction Pipeline Compared to Demand



Watch for markets that have strong demand, but smaller construction pipelines. These markets are less likely to experience excess supply in the near future.

While these markets have generally been hot (see the historical rental growth graph below), construction pipelines are large as compared to recent absorption. While not all construction is scheduled to be delivered in the next year, these markets are reaching a more mature phase of the cycle. Watch for signs of excess construction such as slowing occupancy gains or rental growth.

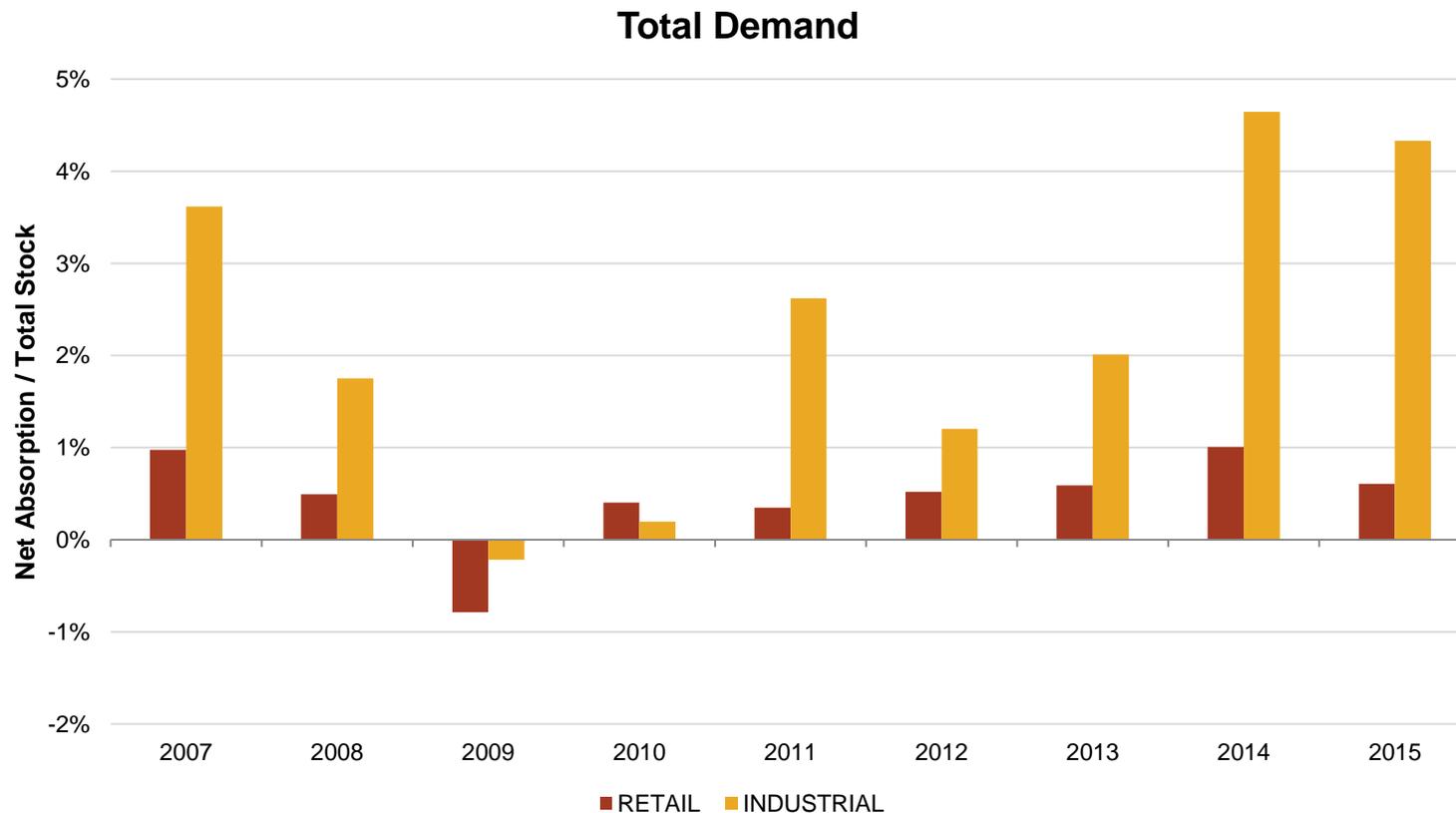
Y-o-Y Rent Growth 2015



Source: CoStar; RCLCO

Target Markets: Watch Subtypes and Secular Changes in Property Use

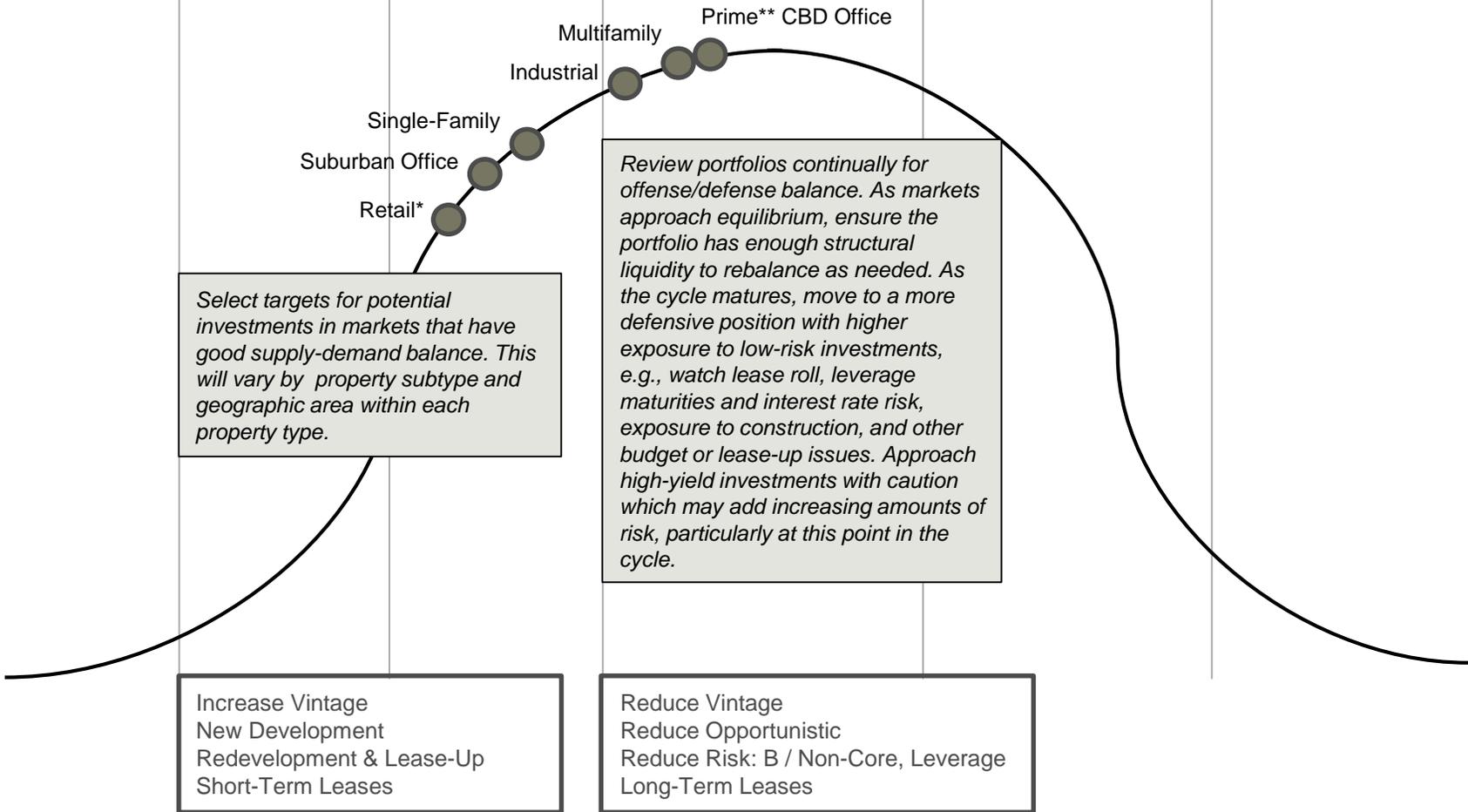
Changing retail patterns continue to create a drag on overall neighborhood and community shopping center retail demand, while growth in e-commerce sales creates continued demand for industrial properties closer to population bases. While some retail properties are performing very well (and in fact have been leading some total return indices), it is important to understand the secular factors impacting retail subtypes. Similar secular changes impact other property types.



Source: CoStar

Manage Existing Portfolios

Occupancy Low	Occupancy Rising	Occupancy Rising	Occupancy High	Occ. Above Average	Occupancy Low
Demand Improving	Demand Improving	Demand Improving	Occupancy Flattening	Occupancy Falling	Occ. Flat to Down
Rents Flat to Down	Rents Rising	Rents Rising	Rents Flattening	Rents Falling	Rents Flat to Down
No Construction	Limited Construction	Construction	Construction	Construction	No Construction



*neighborhood & community centers

**includes New York, Washington, D.C., San Francisco, Seattle, Los Angeles, and Boston

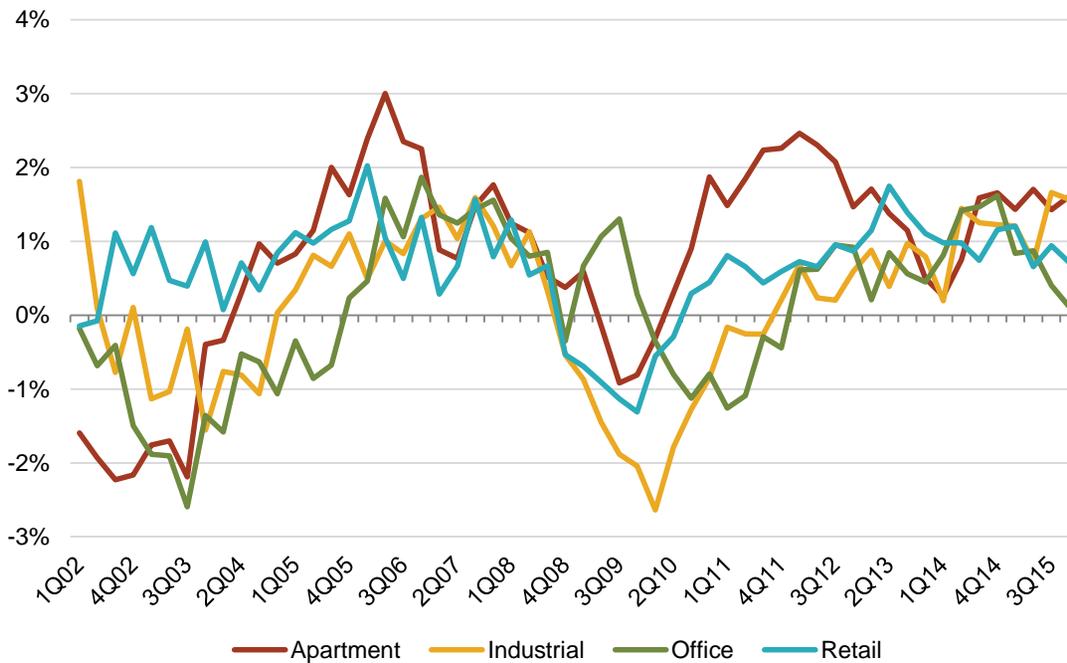
Source: RCLCO



Target Markets: Watch the Cycle—is Leasing an Opportunity or a Risk?

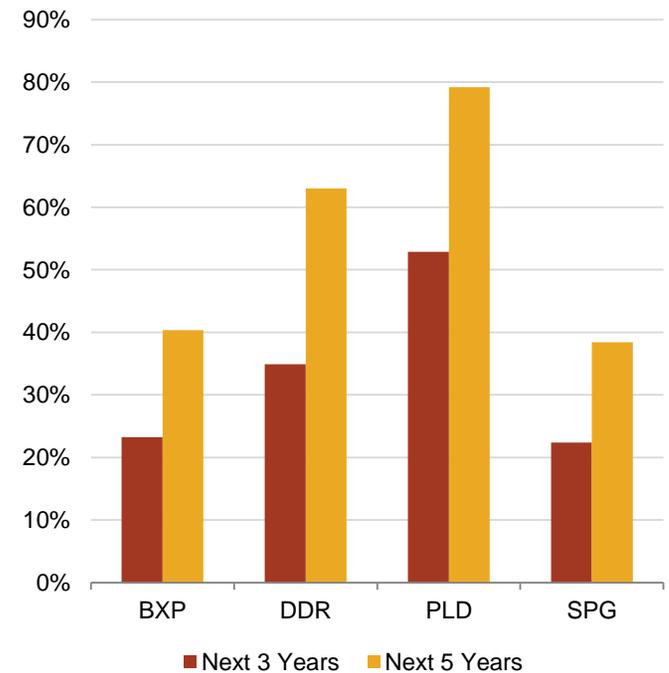
The apartment sector benefited from the demise of the single-family market in the last recession. However, absent unusual conditions, properties with short lease terms such as apartments, industrial, and hotels can experience higher cash flow volatility than sectors with longer-term leases. Watch exposure to forward lease roll at the property and portfolio level in respect to market conditions.

**NOI Growth
2002-2015**



Source: NCREIF and 2014 annual reports

Total Leases Rolling



Next 3 years represents approximate total annual rental revenues under leases expiring in 2015-18; next 5 years is 2015-2020.

Source: NCREIF and 2014 annual reports

Critical Assumptions

Our analysis depends on the correctness and completeness of data available as of the date of this report. The future performance of the global, national, and local economy and real estate market, and other factors similarly outside our control may vary. Given the fluid and dynamic nature of the economy and real estate markets, as well as the uncertainty surrounding particularly the near-term future, it is critical to monitor the economy and markets continuously. Stable and moderate growth patterns are historically not sustainable over extended periods of time; the economy is cyclical; and real estate markets are typically highly sensitive to business cycles. Further, it is very difficult to predict when an economic and real estate upturn will end.

Our analysis can not predict unusual economic shocks on the national and/or local economy, potential benefits from major "booms" that may occur, or the residual impact on the real estate market and the competitive environment of such a shock or boom. Also, it is important to note that it is difficult to predict changing consumer and market psychology.

As such, we recommend the close monitoring of the economy and the marketplace, and updating this analysis as appropriate.

General Limiting Conditions

Reasonable efforts have been made to ensure that the data contained in this study reflect accurate and timely information and are believed to be reliable and comprehensive. This study is based on estimates, assumptions, and other information developed by RCLCO from its independent research effort and general knowledge of the industry. No responsibility is assumed for inaccuracies in reporting by any data source used in preparing or presenting this study. This report is based on information that to our knowledge was current as of the date of this report, and RCLCO has not undertaken any update of its research effort since such date.

Possession of this study does not carry with it the right of publication thereof or to use the name of "Robert Charles Lesser & Co." or "RCLCO" in any manner without first obtaining the prior written consent of RCLCO. This study may not be used for any purpose other than that for which it is prepared or for which prior written consent has first been obtained from RCLCO.

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