



Business Review Day Economic Trends in Commercial Real Estate

May 17, 2006

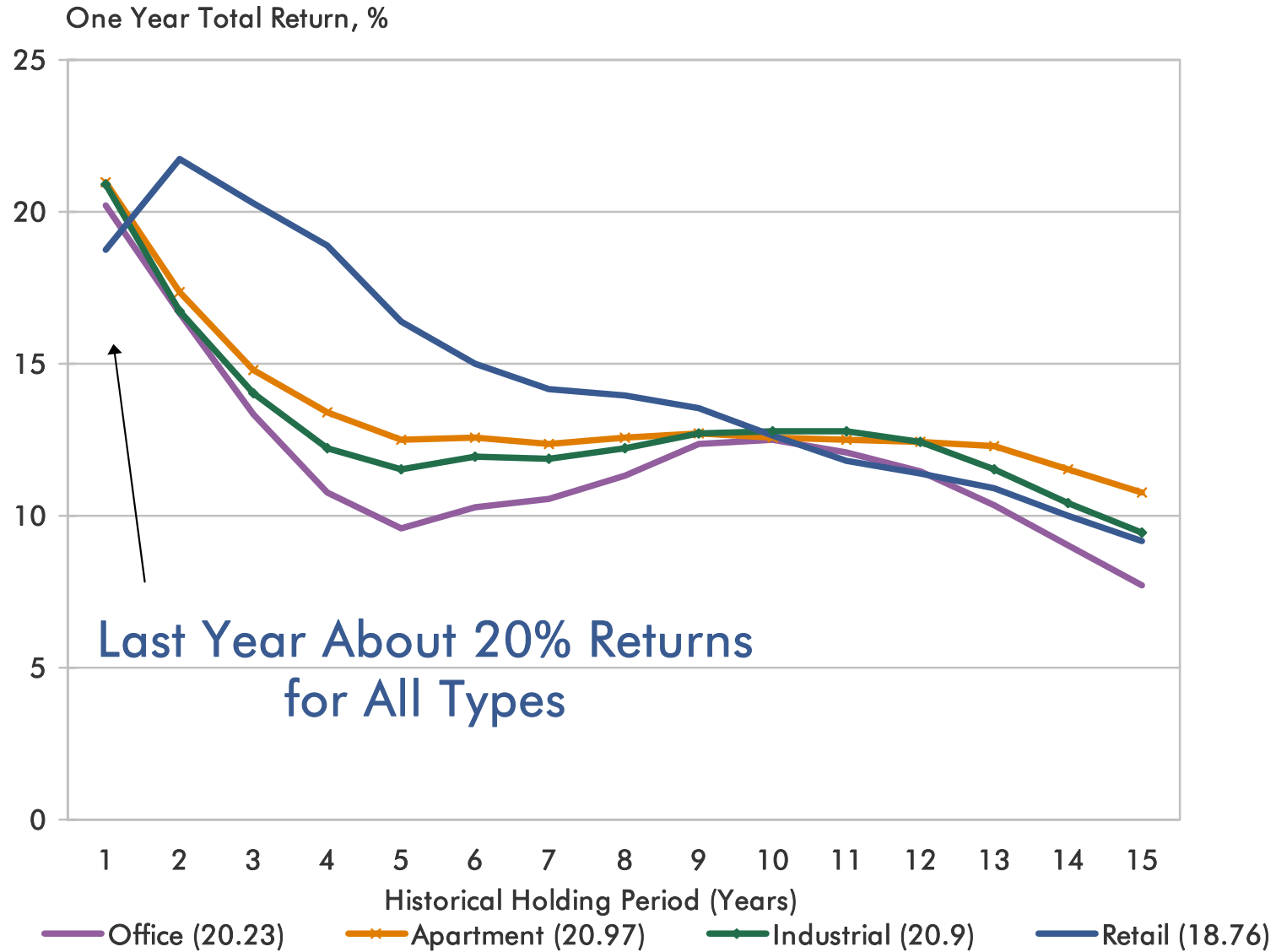
Raymond G. Torto, Ph.D., CRE

100 A CENTURY OF SERVICE
1906 | 2006

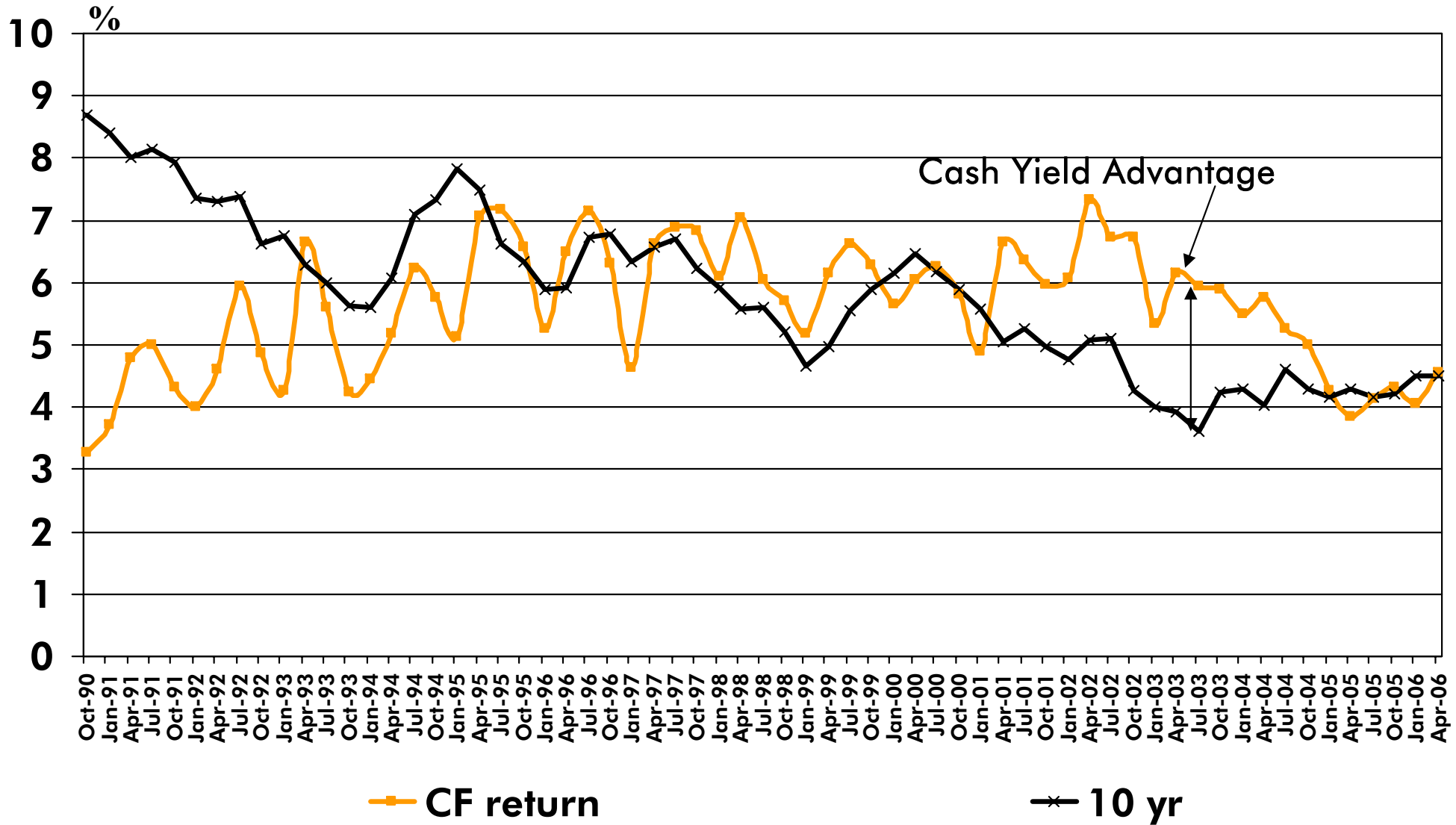
CBRE
CB RICHARD ELLIS

Recent Returns

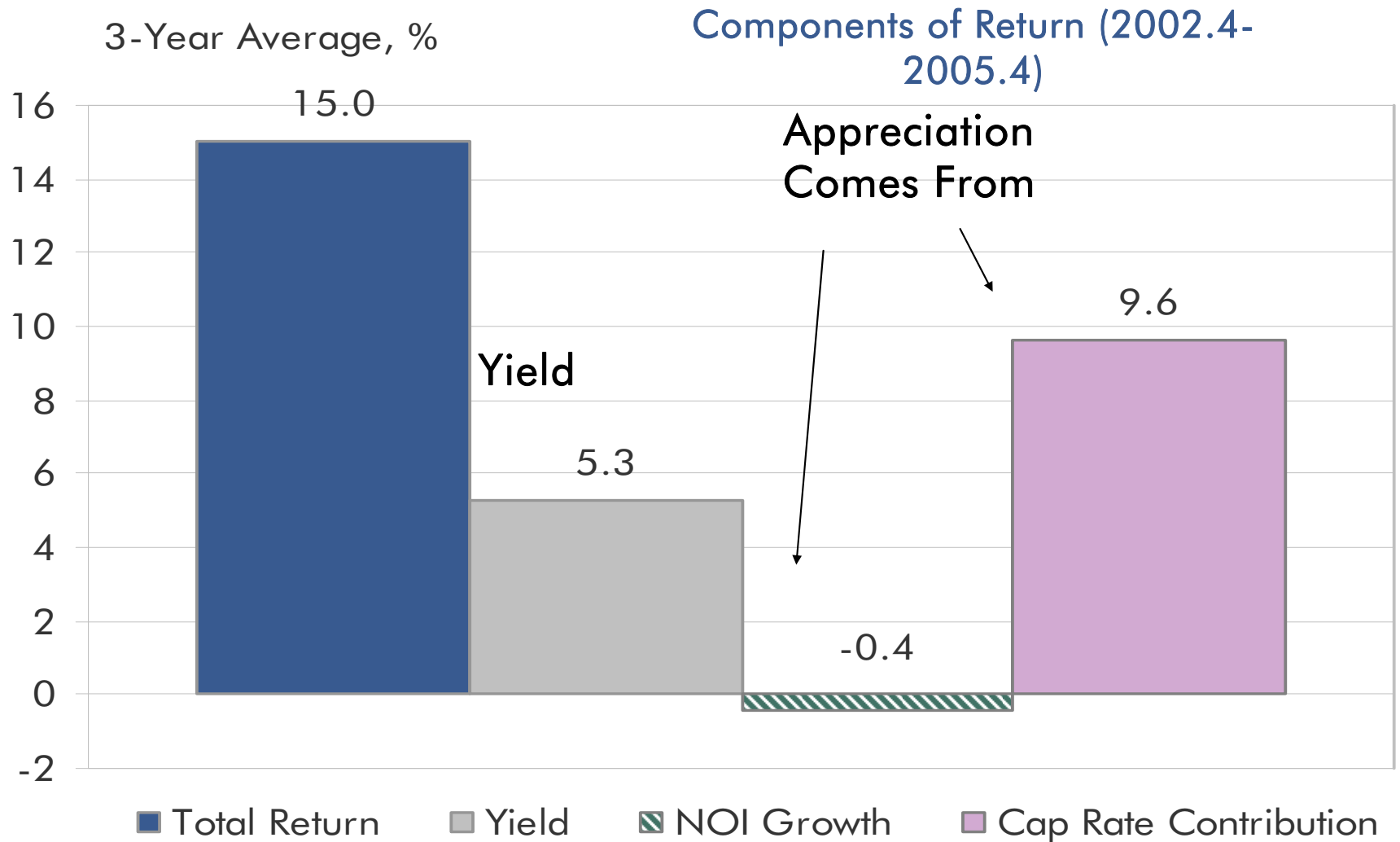
NCREIF Holding Period Returns 2006.1



The Cash Yield Advantage of Recent Years Has Been Competed Away

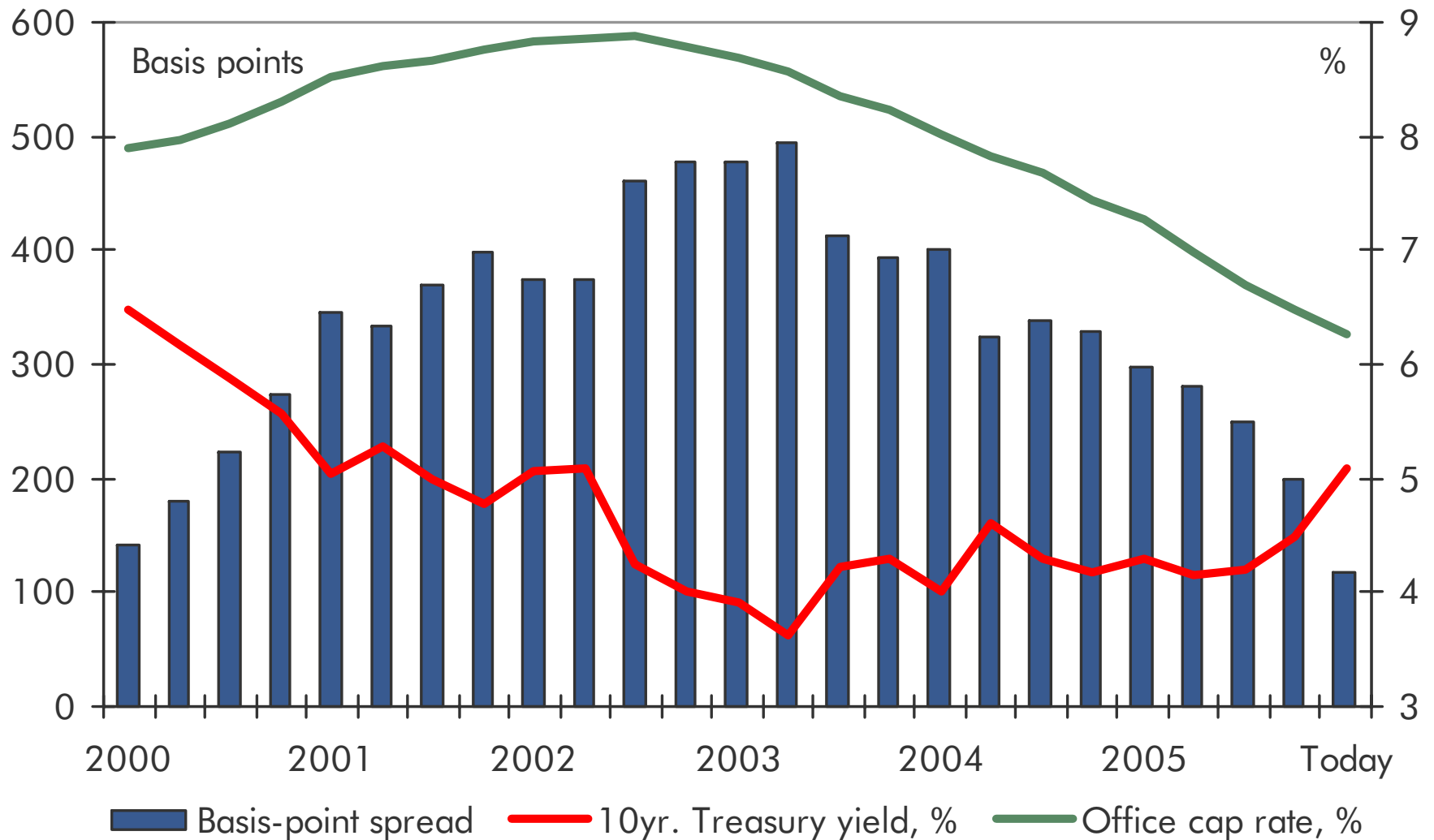


Doing It With Smoke & Cap Rates



NCREIF-weighted returns for Office, Industrial, Multi-Housing, and Retail.

Cap Rates Are Unlikely to Go Lower

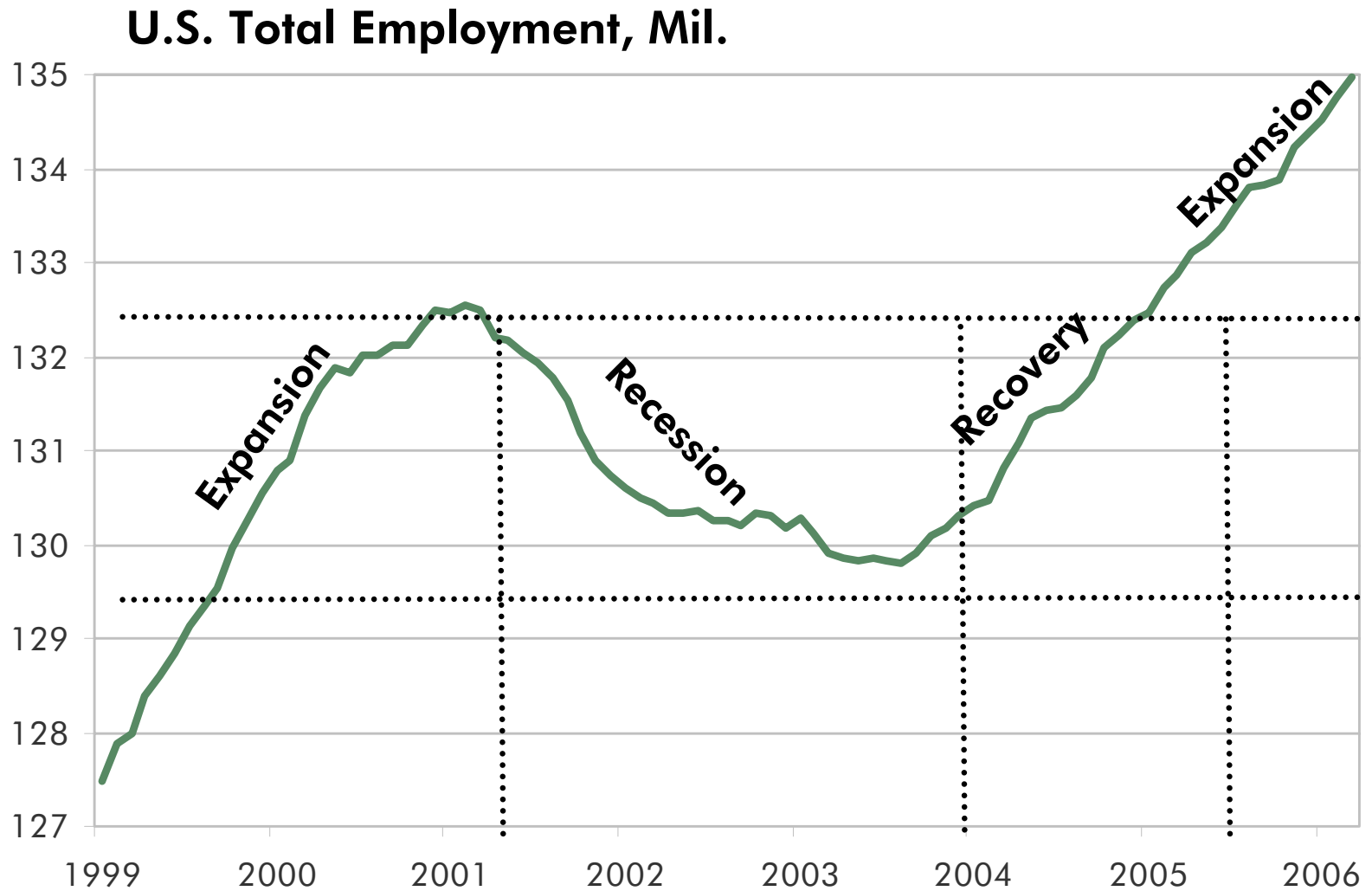


TWR's View: Property Markets

Nothing Happens In a Vacuum. The Economy Is Moving Forward

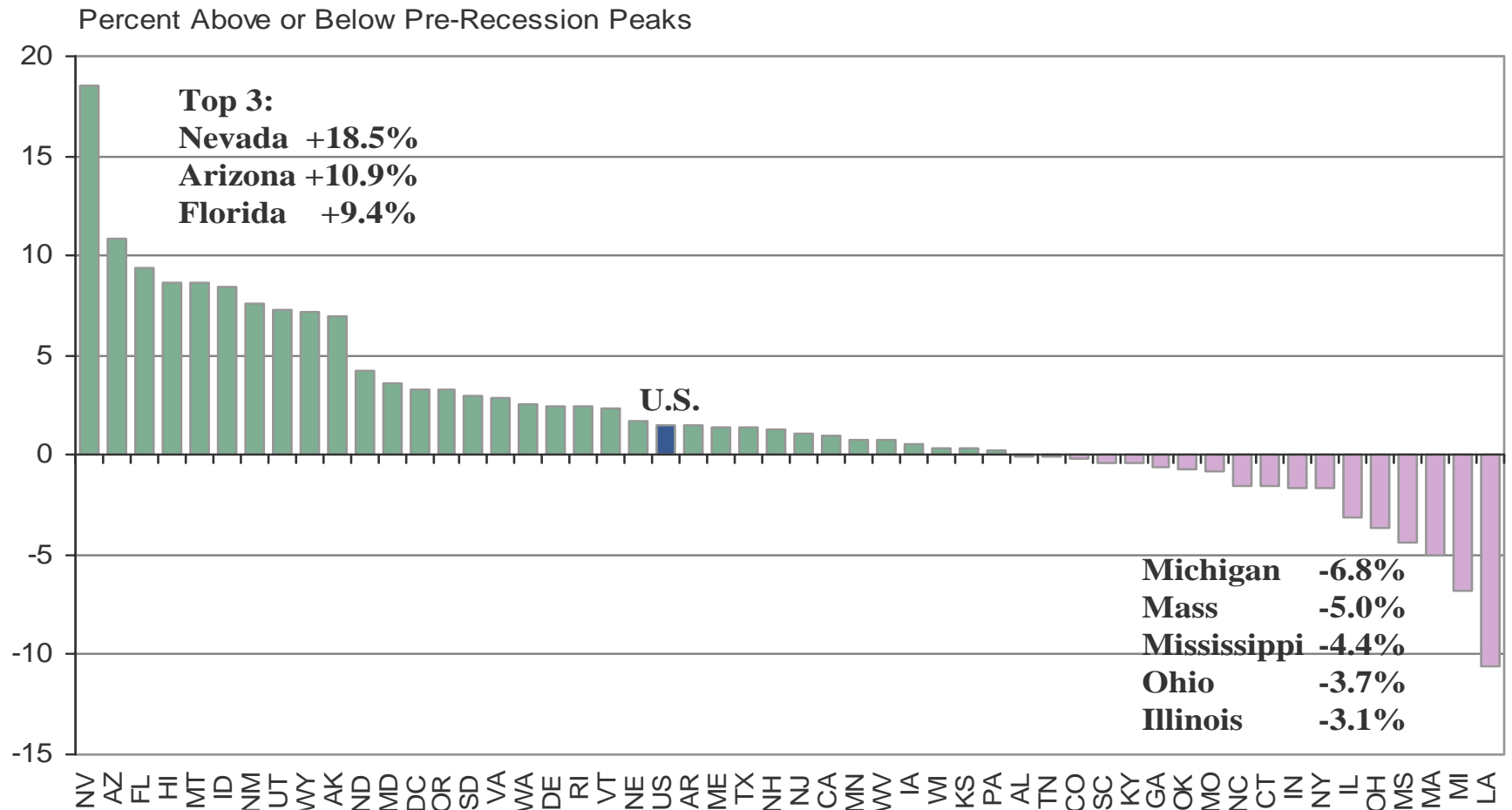
- Industrial capacity utilization at 81.2%
 - Manufacturing capacity utilization at 80.4%
 - Business sales rising by 8.5% year over year
 - Inventories-to-sales ratio extremely low at 1.24
 - Corporate profits are rising at 21.3% year over year
 - Commercial & Industrial lending up 12.3% year over year
 - Exports are rising at a clip of 13.5%
-
- And on and on and on....
 - We're doing well. Don't worry

Second Year of Expanding Jobs



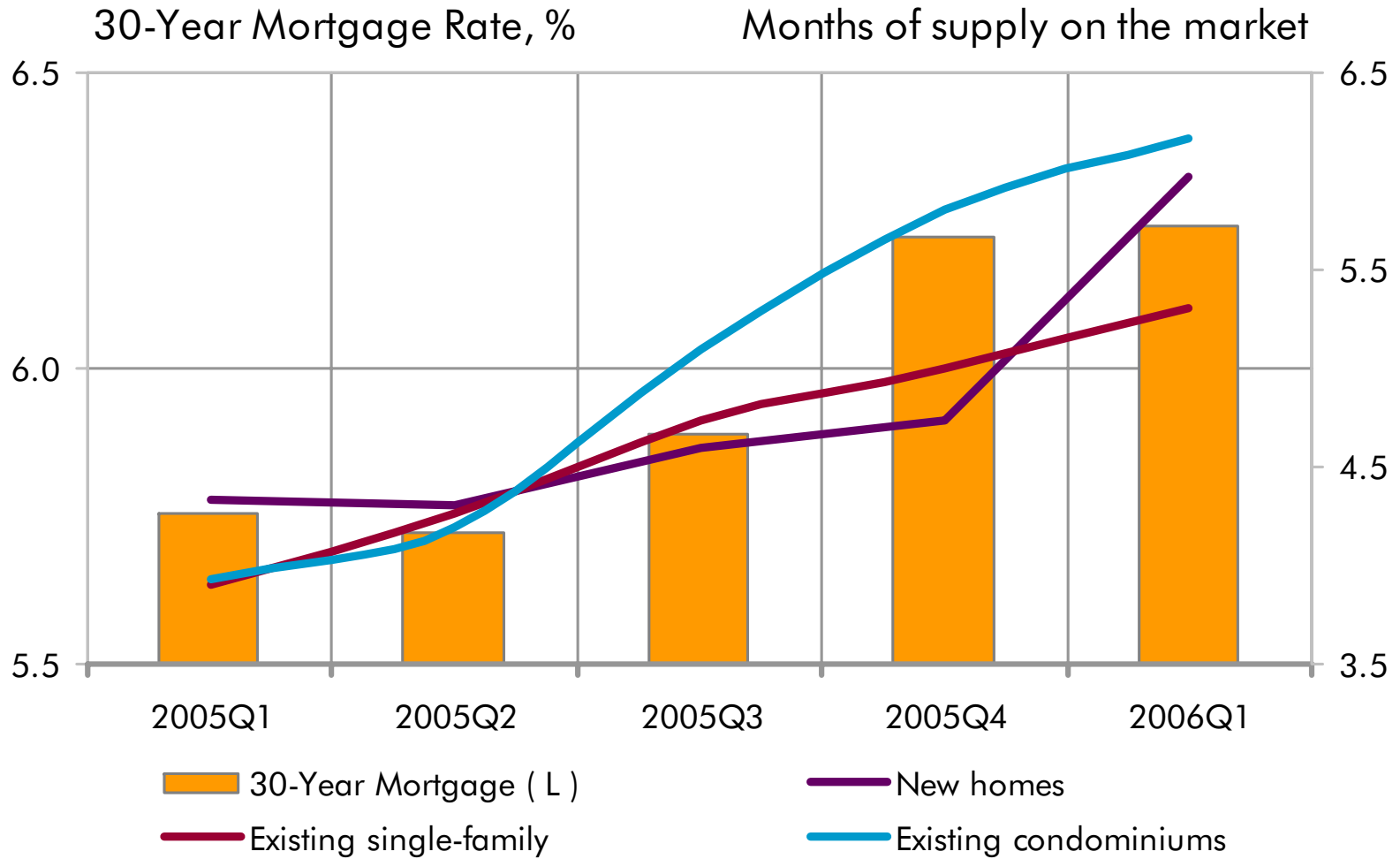
Wide Job Growth Variance!

Today's Jobs Relative to Pre-Recession Peak (2001)

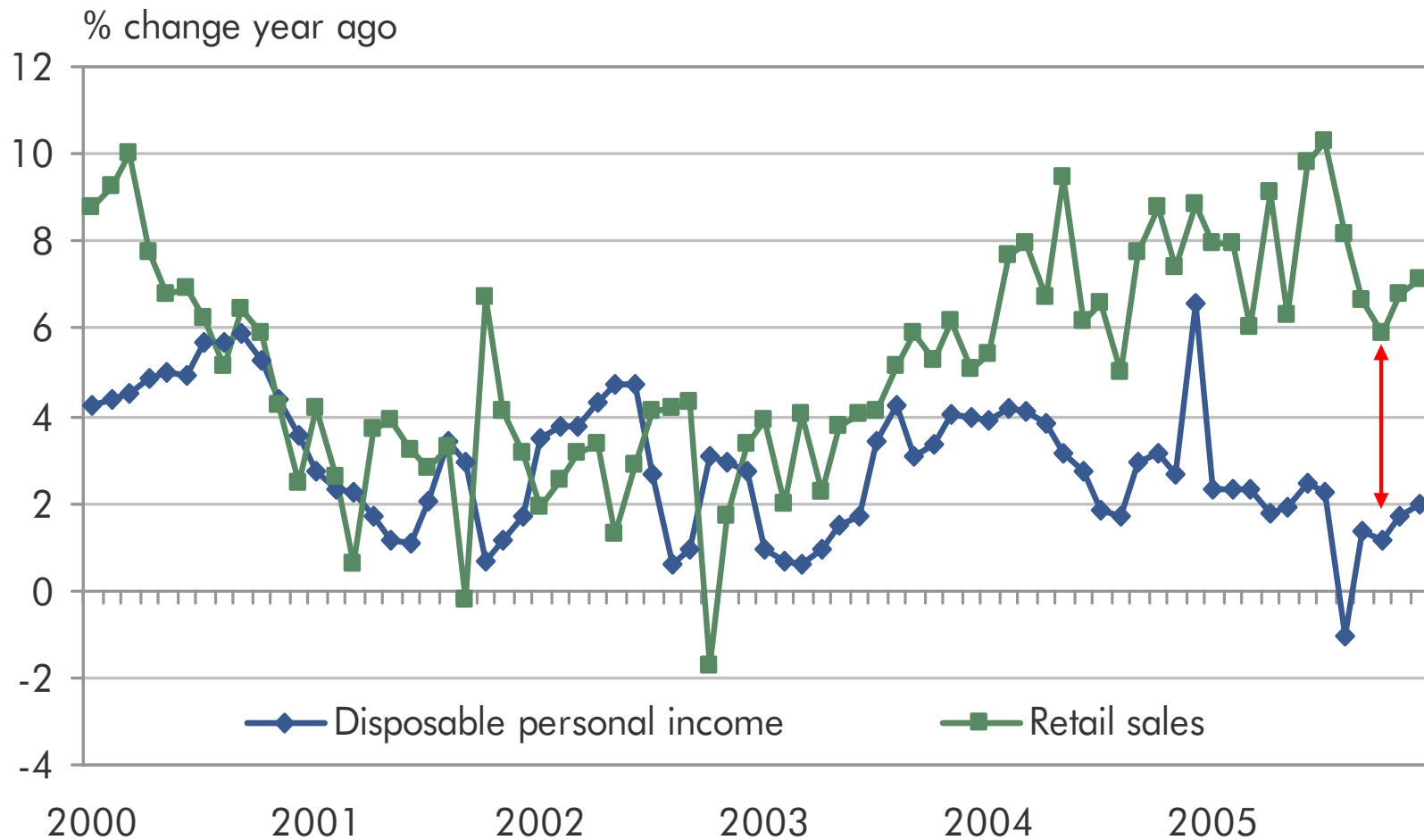


Source: BLS. Data ending December 2005

Rates Rise and Here's a Troubling Trend!



And, This is Going to Hurt, as Well!



However...Fundamentals Are Improving for All Types

Percentage Increase in Rents by Property Type

	2005	2006F	Last High (2000)
Multi-Housing	3.4%	3.2%	7.3%
Office	5.2%	4.5%	13.5%
Industrial	2.9%	3.6%	4.8%
Retail	2.8%	4.0%	5.0%
Hotel	8.0%	6.5%	11.0%

Rents are a good performance measure because they reflect the balance between supply and demand.

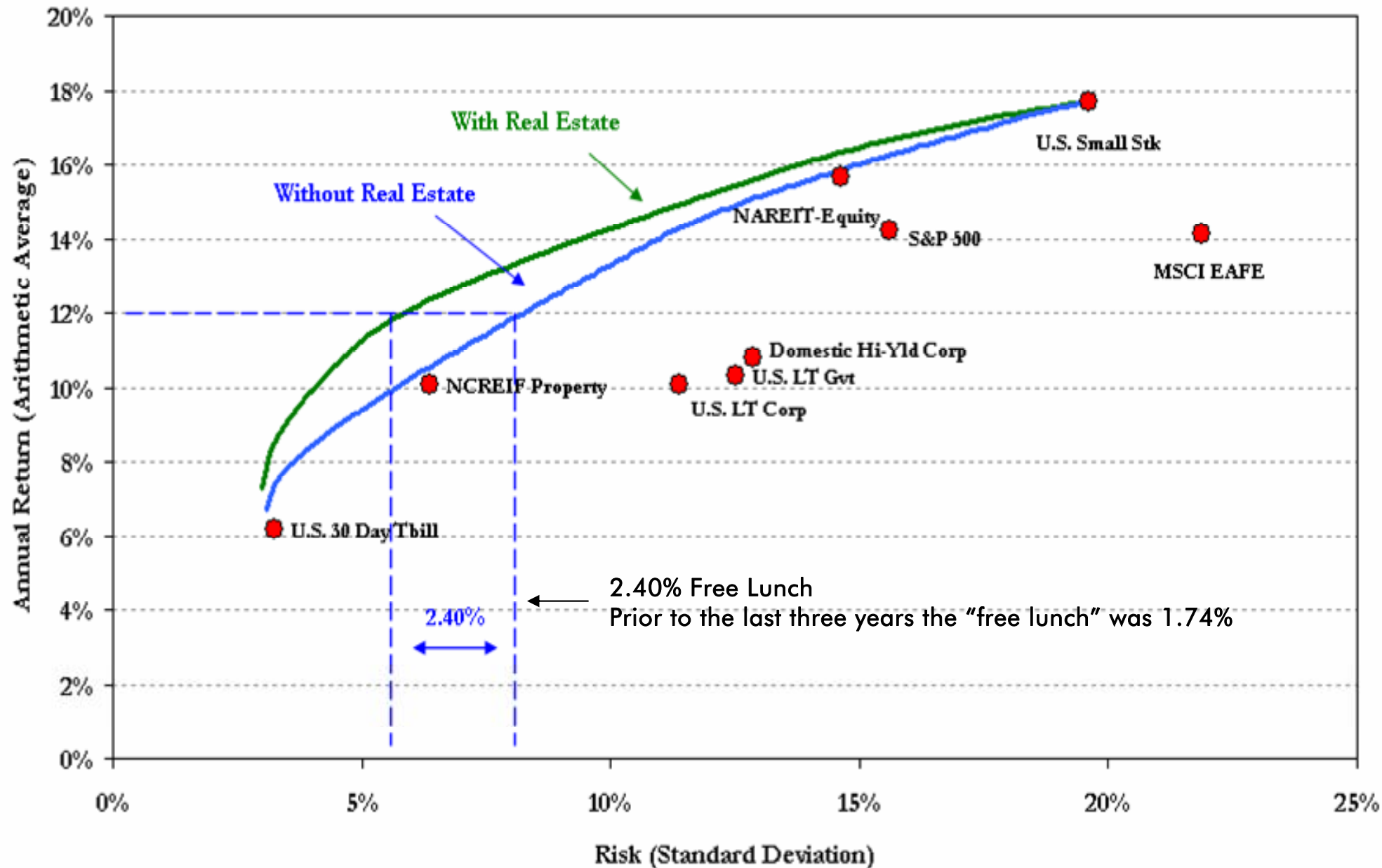
TWR's View: The Capital Markets

Why Real Estate? Why Now?

- There Are Still Opportunities in Real Estate for:
 - Cash Flow
 - Appreciation
 - Diversification
 - Alpha
 - Gamma
- Past Results Are Not Indicative of Future Performance!

Efficient Frontiers with and without Real Estate Selected Asset Classes for the Twentyeight-Year Period 1978–2005

An Illustration of “Free Lunch”



Cap Rate Composition

- Cap rate is composed of:
 - + Risk free rate
 - + Risk premium
 - + Cap X
 - - Expected appreciation

- Appreciation =
 - % chg income - % chg in cap rate
 - Bottom line: fundamentals matter!

Pricing and Fundamentals

"Fooled by Randomness:

the Hidden Role of Chance in Life and in the Markets" by Nassim N. Taleb

- Book's Thesis:
 - It's plain dumb luck, or randomness, not skills, hard work, etc, etc,
- Book's Implication:
 - Forecast don't work: Big events not known
 - » e.g., 9/11. Long Term Capital, 1987 market crash
 - » "Even a broken clock right twice a day"
- Book's Shortcoming
 - If didn't anticipate future, how can we function?
 - Role of econometrics: what is known vs. what is unexplained!