Korpacz

REAL ESTATE INVESTOR SURVEY

FIRST QUARTER, 1999 • VOLUME 12 • NUMBER 1

Making News This Quarter

Korpacz Hotel Market Report Pages 27-32

National Highlights

1999 Investment Market Starts Slowly Amid Pricing Uncertainty

The real estate market is orderly. It is also stable, in balance, normal. After the hyperactivity of the past year or two, investors are savoring the tranquility as the 1999 transaction market gets off to a slow start. That will change, of course. Pension funds have their allocated amounts of money to put into real estate, opportunity funds will smell bargains, strong REITs will become larger and stronger, developers will develop.

For now, neither buyers or sellers are reaching for the sky as they were six months ago, and neither is perceived to have the advantage in negotiations. Part of that is because there have not been enough deals since the 1998 price correction to give them a clear sense of where prices ought to be.

"We know intuitively that prices are down, but we don't know how much," says one investor. "So we're taking a harder look at certain assumptions in our analyses and will lean a little on the low side."

Last fall Survey participants believed that the market correction would mean a substantial decrease in prices across the board. At the time, deals were left on the table as cash-strapped buyers walked away, or prices were negotiated down significantly. Now that the air has cleared, the price correction appears to have been modest. A minority of participants believe that price reductions in some property classes and some geographic areas are double digit, but the majority believe that most price reductions are in the 5% to 10% range. Of course, as prices vary by geographic location, property type, and quality, so do price corrections.

There is capital for acquisitions. Pension funds are expected to lead the pack in acquisitions this year. Well-capitalized REITs will be present but are not likely to be as aggressive as REITs in general were last year. They will not have to be because the competition is not expected to be as fierce. Already, there is a noticeable reduction in the number of competitors for a deal. Although most properties attract more than one bid, it is a handful at most. And the bigger the deal, the fewer the bidders. The population of bidders shrank when the REITs pulled out of the market en masse. "They were big bucks bidders," comments one participant. "The deals under $25 million are where the action is now."

Other players are wealthy individuals, partnerships of individuals, developers who are preselling new projects, and some opportunity funds. Opportunity funds now control about $100 billion in assets, according to a recent Critteden report. They will sell about $35 billion in assets over the next two years, cash that will be available for reinvestment. The most prevalent foreign investors are German groups.

As buyers, REITs are most evident as partners in joint ventures with large institutional investors. Such deals are generally 50-50 partnerships.

Debt capital is widely available. Currently, the prominent sources are banks and life insurance companies. When the CMBS market fell off, life insurance companies stepped in. "The underlying risk had not changed," observes

one participant. "The situation brought some lenders who had been dormant back into the market." Wall Street will slowly come back into the real estate market on the debt side. Investors expect that the debt markets will return to "normal."

Market fundamentals are stronger than they have been for years, a condition that is expected to continue. Overbuilding is not a problem. The drop in the REIT activity and the drop in the CMBS market last year were well timed. The Wall Street analysts put the brakes on, which kept the supply and demand dynamic in balance.

PUBLIC MARKET TRENDS

This is the year that investors will come to realize that REITs are income stocks, not growth stocks — and the year that REITs themselves will come to the same realization. The school of hard knocks, Wall Street, is teaching this lesson. On average, REIT stock value declined 25% last year; after dividends, the total return was a negative 17%. Hotel REITs dropped 56% of their value. At the same time, the S&P 500 gained 27%.

Conservative analysts predict that REIT stock prices will remain flat in 1999. Others forecast total return growth between 6.5% and 10.0%. The average dividend is projected to be as high as 6.8%.

While sitting out of the acquisition market, many REITs are refocusing their strategies for long-term growth. And investors will be watching for signs of strength. Among these are excellent management and a strong balance sheet with a low debt ratio. Geographic location of the properties in a portfolio is critical, and REITs whose properties are protected by supply constraints will be more likely to be recommended by analysts. Niche property focus will also be an advantage.

Some REITs of course are still positioned to acquire property. At the time of the fall 1998 price correction, they had low debt and adequate acquisition lines. Many REITs will acquire property this year in joint venture deals with institutional investors.

Growth of the REIT industry in the foreseeable future will not repeat the phenomenal experience of the past five years. Between 1994 and June 30, 1998, the total REIT industry market capitalization skyrocketed 261.0% from $44.3 billion to $159.93 billion. The percentage increase between December 31, 1997, and June 30, 1998, was 80.2%. Then the bubble started deflating. The rate at which the amount of capital raised was growing slowed and the number of securities issued stagnated.

As of October 30, total market capitalization was $139.75 billion, a decrease of 12.6% from the end of June. By year-end 1998, total market capitalization was down to $138.3 billion, a decrease of 13.52% from the midyear peak.

The amount of capital raised through initial public offerings (IPOs), secondary offerings, and unsecured debt was $27.69 billion as of June 30, 1998. By October 30, it had increased to $36.2 billion, which indicates a slower rate of growth than in the first six months of the year. As of December 31, 1998, the amount of capital raised was $39.13 billion.

In the first five months of 1998, 13 IPOs, totaling more than $1.98 billion, were issued. As of October 30, two additional IPOs were added; the total of all 15 was nearly $2.03 billion. There were no IPOs in November and December. In 1997, 26 IPOs were issued; the total was nearly $6.30 billion.

January 1999 saw a further decline in total market capitalization. As of January 31, 1999, it was down 0.36% to $137.8 billion. The amount of capital raised in the first month of the new year was $1.8 billion. There was one IPO, which raised $12.0 million.

CASH FLOW FORECAST ASSUMPTIONS

Cash flow forecast assumptions this quarter indicate that values are declining at least slightly in most surveyed markets. The composite average overall cap rate (OAR) increased 9 basis points over last quarter. The average OAR decreased in only one market; the change is a mere 4 basis points in the national regional mall market. The average OAR increased in 14 markets. The range is from 2 basis points in the Atlanta office market to 33 basis points in the Houston office market. There was no change in the Pacific Northwest and Southeast Florida office markets.

KORPACZ REAL ESTATE INVESTOR SURVEY

VOL. 12, NO. 1
FIRST QUARTER 1999

Korpacz Real Estate Investor Survey™
is published quarterly by
The Korpacz Company, Inc.
7470 New Technology Way
Frederick, MD 21703-9461
E-mail: info@korpacz.com
Web site: www.korpacz.com

Publisher: Peter F. Korpacz, MAI
Editor-in-Chief: Karla L. Heuer
Production Manager: Bernadette T. Korpacz

Subscription Rates. Print: One year U.S. $250, foreign $300. **On-line:** One year $225. Rates are subject to change without notice.
Make checks payable to The Korpacz Company, Inc.

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Table 1
Yield Comparisons
JANUARY 1, 1999

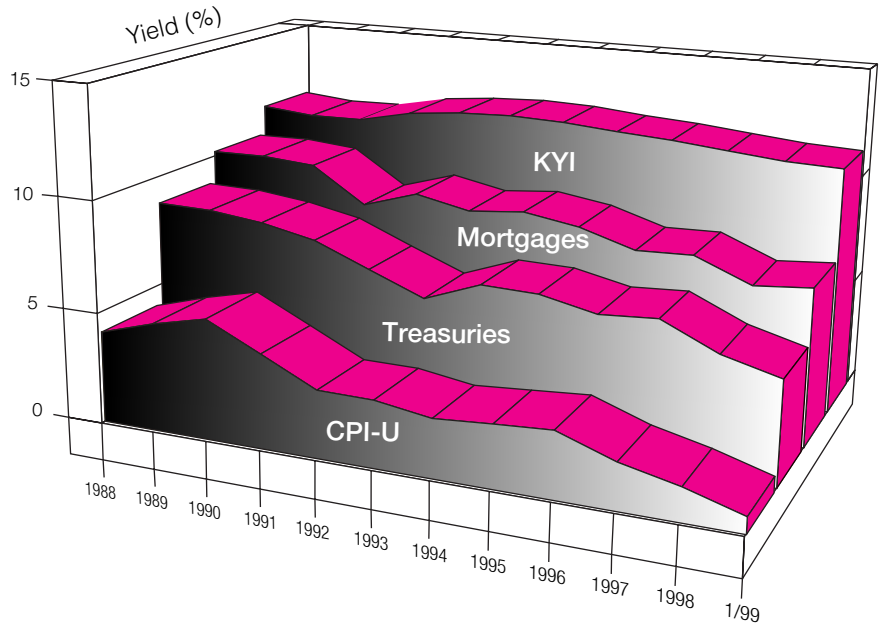
YIELD INDICATORS	1992 AVERAGE	1993 AVERAGE	1994 AVERAGE	1995 AVERAGE	1996 AVERAGE	1997 AVERAGE	1998 AVERAGE	1998 OCTOBER	1999 JANUARY
Korpacz Yield Indicator (KYI)[a]	12.15%	12.25%	12.18%	11.96%	11.82%	11.59%	11.35%	11.26%	11.27%
Long-Term Mortgages[b]	9.26%	8.76%	9.00%	8.61%	7.86%	7.94%	6.93%	6.83%	7.14%
10-Year Treasuries[c]	6.95%	5.98%	6.92%	6.86%	6.33%	6.48%	5.34%	4.61%	4.69%
Consumer Price Index Change[d]	3.01%	2.99%	2.61%	2.78%	2.96%	2.07%	1.48%	1.96%	0.73%
SPREAD TO KYI (Basis Points)									
Long-Term Mortgages	290	349	317	335	396	366	442	443	413
10-Year Treasuries	520	627	525	510	549	511	602	665	658
Consumer Price Index Change	915	926	957	918	886	952	987	930	1054

a. A composite IRR average of the markets surveyed.
b. 10-year or longer term for commercial and industrial property. Source: Research Department, Appraisal Institute and Federal Reserve; beginning October 1994, Crittenden Publishing, Inc.; compiled by The Korpacz Company, Inc.
c. Source: Federal Reserve.
d. Source: U.S. Department of Commerce; quarterly changes are annualized based on the index change from the prior quarter; the year-end change is based on the index change from the prior-year fourth quarter.

The average discount rate (IRR) decreased in 8 markets; the range is from 1 basis point in the Los Angeles office and national industrial markets to 14 basis points in the national regional mall and Pacific Northwest office markets. The average IRR increased in nine markets. The range is from 3 basis points in the national power center and Manhattan office markets to 19 basis points in the Washington, DC office market.

The average initial market rent change rate increased in five markets and decreased in 11. There was no change in the national power center market. Increases range from 2 basis points in the Washington, DC office market to 36 basis points in the Pacific Northwest office market.

Figure 1
Comparative Yields
JANUARY 1, 1999



YIELD COMPARISONS: Real Estate vs. Alternative Investments

The Korpacz Yield Indicator (KYI) increased 1 basis point to 11.27% (see Table 1). The current rate is 8 basis points lower than the 1998 average. The KYI peaked at 12.29% in fourth quarter 1993. For the most part, it has trended downward since.

The average long-term mortgage rate is 7.14%, 31 basis points higher than the rate last quarter. The current rate is 21 basis points higher than the 1998 average.

The 10-year treasury rate increased 8 basis points to 4.69%. The current rate is 65 basis points lower than the 1998 average.

The relationship between real estate yields and inflation is noted by comparing yields to the CPI. From October to January, the CPI change rate decreased 123 basis points from 1.96% to 0.73% (annualized). The spread between the KYI and CPI change rate is 1054 basis points.

The spread between the KYI and long-term mortgage rates decreased 30 basis points to 413 from last quarter's 443 basis points. The current spread is 29 basis points lower than the 1998 average.

The spread between the KYI and 10-year treasuries decreased 7 basis points. The current spread is 56 basis points higher than the 1998 average.

DIVIDEND COMPARISONS:
Public vs. Private Markets

REIT dividend yields can be compared with stock dividend yields, although they are not exactly comparable. As Merrill Lynch cautions: "P/E ratios for most companies incorporate measures of earnings after depreciation, whereas REIT earnings are measured as a function of funds from operation (FFO), which basically amount to earnings before depreciation. Adjustments to FFO for recurring capital expenditures still do not result in adjusted FFO (AFFO) measures which are readily comparable to GAAP [generally accepted accounting principles] earnings in other sectors."

The REIT dividend yield is somewhat comparable to the going-in cap rate (OAR) on an all-cash sale. The OAR is the dividend rate a direct real estate investor receives upon a cash purchase of a property. However, caution must be exercised here as well. The Korpacz Dividend Indicator (KDI) is a composite OAR (initial rate of return in an all-cash transaction) average of the 17 commercial markets surveyed (not including the hotel markets). The average annualized equity REIT dividend yield is for all companies, including for example, health care and manufactured homes, which we do not track.

As a result of such differences among dividends for equity REITs, the S&P 500, and OARs, the comparisons are not perfect. However, they do show trends among these three types of investments.

The KDI, average dividend yields for equity REITs, and the S&P 500, as well as spreads between the KDI and the other investments, are set out in Table 2. From 1991 through 1996, the annual average KDI consistently increased. At the same time, the spread between average annual IRRs and OARs consistently decreased. The narrowing spread is indicative of investors' diminished anticipation of both increased income and property appreciation.

In 1997 the annual average KDI decreased slightly. The spread between average IRRs and average OARs narrowed in three quarters of 1997. It widened slightly in all quarters of 1998. This quarter the spread is 216 basis points, down 8 basis points from last quarter. If prices continue to decline, average OARs will rise. Their relationship to average IRRs will bear watching.

Average annualized equity REIT dividends have fluctuated considerably during the 1990s, due primarily to fluctuations in their stock prices. By comparison, the average annual S&P 500 pattern has been steadier. It declined from 1991 through 1993, increased in 1994, and declined in each of the next four years. This is, in large measure, due to the dramatic increases in stock prices during 1995 through 1998.

As REIT dividends fluctuated between 1991 and 1996 and the KDI consistently increased, the spread between the KDI and REITs climbed from the 1991 annual average of 38 basis points to the historical high of 382 basis points, reached September 30, 1997. This quarter the spread is 164, a 50-basis-point decrease from last quarter. The average annual spread from 1991 through 1998 is 215 basis points.

Changes in the spread between the KDI and the average S&P 500

Table 2
Dividend Comparisons
JANUARY 1, 1999

DIVIDEND INDICATORS	1992 AVERAGE	1993 AVERAGE	1994 AVERAGE	1995 AVERAGE	1996 AVERAGE	1997 AVERAGE	1998 AVERAGE	1998 OCTOBER	1999 JANUARY
Korpacz Dividend Indicator (KDI)[a]	9.09%	9.28%	9.29%	9.31%	9.39%	9.35%	9.08%	9.02%	9.11%
Equity REITs[b]	7.53%	6.30%	7.25%	7.75%	7.09%	6.06%	6.01%	6.88%	7.47%
S&P 500[c]	2.97%	2.74%	2.85%	2.41%	2.11%	1.83%	1.57%	1.59%	1.32%
SPREAD TO KDI (Basis Points)									
Equity REITs	156	298	204	156	230	329	307	214	164
S&P 500	612	654	644	690	728	752	751	743	779

a. A composite OAR (initial rate of return in an all-cash transaction) average of the markets surveyed.
b. Source: National Association of Real Estate Investment Trusts; average annualized dividend yield calculated by The Korpacz Company, Inc.; dividend yields are as of the last day of the prior quarter.
c. Source: S&P 500 Analysts' Handbook Office Series–Monthly Supplements; average annual dividend yield calculated by The Korpacz Company, Inc.; dividend yields are quarterly yields as of the last day of the prior quarter.

from 1991 through 1997 range from a low of 545 basis points in 1991 to a high of 765 reached September 30, 1997. The current spread is a 36-basis-point increase over last quarter. The average annual spread from 1991 through 1998 is 654 basis points.

Average annual real estate dividends, as expressed by the KDI, are higher than REIT dividends and S&P 500 dividends in every year shown in Table 2. The likely reasons that the private market real estate dividends are higher than public market dividends are the burden of management and lack of liquidity in direct private ownership of real estate. In the public market, there is no management burden and the opportunity for liquidity is present daily.

Historically the return on stocks, as represented by the S&P 500, has been considerably lower than the return from all forms of real estate ownership. Stocks have consistently provided the bulk of their return in appreciation of the stock over time.

INSTITUTIONAL vs. NONINSTITUTIONAL RATES

EDITOR'S NOTE: Table 3 shows noninstitutional-grade property discount rates (IRRs) and overall cap rates (OARs) for the surveyed markets for which sufficient data are available.

As with the rates published for institutional-grade property, we do not represent that the survey is statistically accurate for each surveyed market. Analysts are cautioned to test rates in local markets to verify spreads and relationships between institutional-grade and noninstitutional-grade property rates. Despite the survey findings that rates are higher for noninstitutional-grade property, in our appraisal work we have found that the reverse is true in some cases in some markets.

As would be expected, the IRRs in our Survey are higher for noninstitutional-grade property than for institutional-grade property, reflecting the greater risk in owning noninstitutional-grade property.

Average noninstitutional-grade IRRs range from 12.13% (Atlanta office market) to 15.00% (Washington, DC office market). The composite average noninstitutional-grade IRR for all markets is 13.26%. This is 9 basis points higher than last quarter. By comparison, the composite average institutional-grade IRR is 11.27%.

Like the IRRs, the OARs in our Survey are higher for noninstitutional-grade property than for institutional-grade property. Average noninstitutional-grade OARs range from 9.58% (San Francisco office market) to 11.97% (national strip shopping center market). The composite average noninstitutional-grade OAR for all markets is 10.59%. This is 10 basis points higher than last quarter. By comparison, the composite average institutional-grade OAR is 9.11%.

MARKETING TIME

Marketing time, the period from putting a property on the market to closing, has been narrowing over the past several years. This quarter's estimates indicate that the length of time is stabilizing in many markets. Marketing time estimates for retail, office, industrial, and apartment properties are included in the Investor Survey Response tables. Averages are shown in Table 4.

The shortest marketing time is 5.31 months in the national apartment market. The longest is 8.36 months in the national CBD office market.

The average for all surveyed markets is 7.21 months. This is 2.17% lower than last quarter's average and 15.08% lower than one year ago.

VALUATION ISSUES

Reserves for Replacement

Including an appropriate reserve for replacement of building components during an ownership period is important in forecasting the real cash return potential of an acquisition. Large capital costs are usually accounted for separately. The reserve for replacement allocations of individual Survey participants are included in the Investor Survey Response tables. Ranges and averages of current and year-ago assumptions for the surveyed markets are set out in Exhibit 1.

Over the past year, reserves for replacement fluctuated more than they had in previous years. Compared with one year ago, the average reserve increased in eight markets, decreased in four markets, and did not change in five. Decreases range from 4.44% in the national apartment market to 10.81% in the Atlanta office market. Increases range from 4.55% in the Los Angeles office market to 27.78% in the Pacific Northwest office market.

Our experience in analyzing capital expenditures over time for replacement of building components in various property types indicates a disparity between actual expenditures and forecast reserve accounts. Actual expenditures are most often higher. Consequently, it is always surprising to see decreases in forecast replacement reserves in some surveyed markets, especially office markets. As one participant observes, some buyers seem to ignore the continuous reinvestment that buildings require. "Buildings don't get newer, they only get older and more expensive to run."

The decreases are in markets in which there is considerable new construction. The decreases could be a reflection of predevelopment investment, with lower reserves required for new properties.

Table 3
Rates: Institutional-Grade vs. Noninstitutional-Grade Property
FIRST QUARTER 1999

Source: Personal survey conducted by The Korpacz Company, Inc. during January 1999.

	INSTITUTIONAL				NONINSTITUTIONAL				SPREAD TO INSTITUTIONAL	
	IRRs		OARs		IRRs		OARs		AVERAGE IRR	AVERAGE OAR
Market	Range	Average	Range	Average	Range	Average	Range	Average	Basis Points	Basis Points
National Regional Mall	9.50%-12.50%	11.14%	7.00%-10.50%	8.41%	11.00%-16.00%	13.50%	8.00%-12.50%	9.88%	236	147
National Power Center	10.25%-12.50%	11.32%	8.00%-10.50%	9.82%	NA	NA	NA	NA	NA	NA
National Strip Shopping Center	10.00%-14.00%	11.61%	8.25%-11.50%	9.76%	12.00%-18.75%	14.20%	9.00%-15.00%	11.97%	259	221
National CBD Office	9.75%-15.00%	11.28%	7.00%-11.00%	8.82%	11.00%-18.00%	13.69%	8.50%-14.00%	10.56%	241	174
National Suburban Office	9.75%-12.50%	11.11%	7.50%-10.50%	9.17%	11.00%-14.50%	12.73%	9.50%-12.50%	10.83%	162	166
Atlanta Office	9.75%-12.00%	11.08%	8.00%-10.50%	9.23%	11.00%-13.50%	12.13%	10.00%-11.00%	10.63%	105	140
Chicago Office	9.29%-13.00%	10.95%	8.00%-10.25%	9.11%	10.25%-14.75%	12.34%	8.50%-12.00%	10.25%	139	114
Dallas Office	10.00%-13.00%	11.38%	7.50%-12.00%	9.24%	11.50%-15.50%	13.25%	9.00%-14.50%	11.08%	187	184
Houston Office	10.00%-13.50%	11.78%	8.00%-12.00%	9.43%	12.50%-15.00%	13.75%	10.25%-12.00%	10.75%	197	132
Los Angeles Office	10.00%-14.00%	11.63%	7.00%-10.50%	8.74%	12.00%-20.00%	14.90%	8.50%-13.00%	10.38%	327	164
Manhattan Office	9.75%-13.00%	11.09%	7.50%-10.00%	9.00%	10.25%-15.00%	12.96%	NA	NA	187	NA
Pacific Northwest Office	10.00%-13.00%	11.27%	8.00%-11.00%	9.18%	11.75%-18.00%	14.33%	9.50%-15.00%	11.38%	306	220
San Francisco Office	9.25%-12.00%	10.71%	7.00%-11.00%	8.42%	10.25%-14.50%	12.46%	7.50%-11.00%	9.58%	175	116
Southeast Florida Office	10.00%-12.00%	11.14%	8.00%-12.00%	9.39%	11.25%-15.00%	13.30%	9.00%-14.00%	10.80%	216	141
Washington, DC Office	10.00%-13.00%	11.50%	7.00%-11.00%	9.13%	13.50%-18.00%	15.00%	9.00%-14.00%	10.75%	200	162
National Industrial	9.50%-12.50%	11.14%	8.00%-10.25%	9.14%	10.50%-14.50%	12.18%	8.25%-12.00%	10.21%	104	107
National Apartment	10.00%-15.00%	11.48%	7.50%-11.00%	8.83%	11.00%-17.00%	13.01%	8.50%-11.50%	9.83%	153	100

Table 4
Average Marketing Time (months)
FIRST QUARTER 1999

MARKET	CURRENT QUARTER	LAST QUARTER	YEAR AGO
National Regional Mall	8.05	9.55	10.00
CHANGE	—	–15.71%	–19.50%
National Power Center	7.50	7.50	8.30
CHANGE	—	0.00%	–9.64%
National Strip Shopping Center	6.68	6.66	7.46
CHANGE	—	+0.30%	–10.46%
National CBD Office	8.36	8.64	9.25
CHANGE	—	–3.24%	–9.62%
National Suburban Office	8.00	8.08	8.63
CHANGE	—	–0.99%	–7.30%
Atlanta Office	6.50	6.50	6.63
CHANGE	—	0.00%	–1.96%
Chicago Office	7.50	7.50	9.19
CHANGE	—	0.00%	–18.40%
Dallas Office[a]	6.50	6.69	8.65
CHANGE	—	–2.84%	–22.93%
Houston Office[a]	6.61	6.61	8.65
CHANGE	—	0.00%	–24.86%
Los Angeles Office	5.69	6.06	8.75
CHANGE	—	–6.11%	–34.97%
Manhattan Office	7.77	7.86	10.39
CHANGE	—	–1.15%	–25.22%
Pacific Northwest Office	7.29	7.29	8.25
CHANGE	—	0.00%	–11.64%
San Francisco Office	6.25	6.25	7.14
CHANGE	—	0.00%	–12.46%
Southeast Florida Office	8.07	8.07	9.20
CHANGE	—	0.00%	–12.28%
Washington, DC Office	7.22	7.33	8.25
CHANGE	—	–1.50%	–12.48%
National Industrial	6.53	7.03	7.12
CHANGE	—	–7.11%	–8.29%
National Apartment	5.31	4.88	4.50
CHANGE	—	+8.81%	+18.00%
All Markets Surveyed (Simple Average)	7.05	7.21	8.23
CHANGE	—	–2.22%	–14.34%

a. Year-ago quarter times are for combined Dallas-Houston office market.

Management Fees
Property management may be an in-house function, performed by an affiliated company, or contracted for with a third party. In any case, the expense is included in the cash flow analysis. It is an "above-the-line" item, included in property expenses as part of the derivation of NOI. Management fees are usually expressed as a percentage of effective gross income. Ranges and averages of current management fee assumptions for the surveyed markets are set out in Exhibit 2. Average management fees range from 2.50% in the San Francisco office market to 3.92% in the national regional mall market.

Leasing Commissions
Most investors incorporate leasing commissions into a cash flow analysis as a "below-the-line" item. This is the case in two of the three methods used to derive NOI. The third method treats leasing commissions, along with the capital replacement reserve and TIs, as an "above the line" item. Like management fees, leasing commissions are usually expressed as a percentage of effective gross income. Ranges and averages of current leasing commissions assumptions for the surveyed markets are set out in Exhibit 2. Average leasing commissions range from 4.58% in the San Francisco office market to 6.60% in the national industrial market.

Price Corrections and Survey Rates
In the fourth quarter 1998 issue, we reported that the consensus among Survey participants, whom we interviewed during September and early October, was that the real estate market had suffered an abrupt price correction. Numerous deals in contract were at risk and many ongoing negotiations were terminated or revalued downward. Yet this perception was not widely reflected in investors' criteria, specifically, going-in cap rates and discount rates. In fact, the com-

posite average IRR declined a few basis points from the prior quarter, and the average OAR increased only 1 basis point.

This apparent discrepancy brings to the fore some issues regarding changes in cap and discount rates and other assumptions in our Survey. Readers should be aware of the following:

- When there is a perceived abrupt change in market conditions, our market participants are often reluctant to make significant changes to the forecast assumptions and usually wait a quarter until they are more certain of market conditions. Rather than immediately changing their investment criteria, investors are inclined to wait to see if the shift is short term or until there is considerable market evidence of lower (or higher) prices in actual deals closed. This brief lag has been typical over the 10-year history of our Survey.

- It is often not necessary for investors to alter the criteria cap rates they report in our Survey immediately because most participants report a range of rates. In any given quarter, most of the deals they do will be at rates within that range. When prices are rising, it is likely that deals are in the lower end of the range. Even when conditions change (e.g., prices dropping), if the range is still commensurate with their acquisition strategy, they often do not change the range. They may start to buy properties at rates in the middle or top end of the range because of some price decline.

  This issue has arisen many times over the years we have published the Survey. We have no mathematical solution to the problem, since we do not adjust

Exhibit 1. Reserves for Replacement—FIRST QUARTER 1999

MARKET	CURRENT QUARTER	YEAR AGO
National Regional Mall		
RANGE	$0.05-$0.75	$0.10-$0.75
AVERAGE	$0.22	$0.21
CHANGE	—	+4.76%
National Power Center		
RANGE	$0.10-$0.25	$0.10-$0.25
AVERAGE	$0.15	$0.15
CHANGE	—	0.00%
National Strip Shopping Center		
RANGE	$0.10-$0.50	$0.10-$0.50
AVERAGE	$0.19	$0.19
CHANGE	—	0.00%
National CBD Office		
RANGE	$0.10-$0.50	$0.05-$0.50
AVERAGE	$0.24	$0.20
CHANGE	—	+20.00%
National Suburban Office		
RANGE	$0.10-$0.50	$0.05-$0.50
AVERAGE	$0.23	$0.20
CHANGE	—	+15.00%
Atlanta Office		
RANGE	$0.10-$1.05	$0.15-$1.05
AVERAGE	$0.33	$0.37
CHANGE	—	–10.81%
Chicago Office		
RANGE	$0.10-$0.25	$0.10-$0.25
AVERAGE	$0.19	$0.20
CHANGE	—	–5.00%
Dallas Office[a]		
RANGE	$0.05-$0.50	$0.05-$0.25
AVERAGE	$0.21	$0.18
CHANGE	—	+16.67%
Houston Office[a]		
RANGE	$0.05-$0.50	$0.05-$0.25
AVERAGE	$0.20	$0.18
CHANGE	—	+11.11%
Los Angeles Office		
RANGE	$0.05-$1.00	$0.05-$1.00
AVERAGE	$0.23	$0.22
CHANGE	—	+4.55%
Manhattan Office		
RANGE	$0.10-$0.50	$0.10-$0.50
AVERAGE	$0.25	$0.25
CHANGE	—	0.00%
Pacific Northwest Office		
RANGE	$0.15-$0.50	$0.10-$0.25
AVERAGE	$0.23	$0.18
CHANGE	—	+27.78%
San Francisco Office		
RANGE	$0.10-$0.30	$0.10-$0.50
AVERAGE	$0.19	$0.20
CHANGE	—	–5.00%
Southeast Florida Office		
RANGE	$0.10-$0.30	$0.10-$0.30
AVERAGE	$0.20	$0.20
CHANGE	—	0.00%
Washington, DC Office		
RANGE	$0.10-$0.25	$0.10-$0.25
AVERAGE	$0.17	$0.17
CHANGE	—	0.00%
National Industrial		
RANGE	$0.05-$0.30	$0.05-$0.40
AVERAGE	$0.13	$0.11
CHANGE	—	+18.18%
National Apartment		
RANGE	$150.00-$400.00	$50.00-$400.00
AVERAGE	$238.89	$228.28
CHANGE	—	4.44%

a. Year-ago quarter amounts are for combined Dallas-Houston office market

Exhibit 2
Management Fees and Leasing Commissions
FIRST QUARTER 1999

MARKET	MANAGEMENT FEES	LEASING COMMISSIONS
National Regional Mall		
RANGE	3.00%-4.00%	4.00%-6.00%
AVERAGE	3.92%	4.75%
National Power Center		
RANGE	2.50%-4.00%	2.50%-6.00%
AVERAGE	3.38%	4.95%
National Strip Shopping Center		
RANGE	3.00%-5.00%	2.50%-6.00%
AVERAGE	3.67%	4.63%
National CBD Office		
RANGE	1.00%-4.00%	3.60%-8.00%
AVERAGE	2.81%	5.36%
National Suburban Office		
RANGE	2.00%-4.00%	3.00%-8.00%
AVERAGE	3.45%	5.10%
Atlanta Office		
RANGE	2.50%-4.00%	2.00%-7.00%
AVERAGE	3.31%	5.39%
Chicago Office		
RANGE	1.75%-5.00%	3.00%-7.00%
AVERAGE	3.23%	5.13%
Dallas Office		
RANGE	2.00%-4.00%	2.00%-5.00%
AVERAGE	2.80%	5.05%
Houston Office		
RANGE	2.00%-4.00%	2.00%-6.50%
AVERAGE	2.83%	5.25%
Los Angeles Office		
RANGE	1.75%-5.00%	4.00%-6.00%
AVERAGE	2.66%	4.81%
Manhattan Office		
RANGE	2.50%-4.00%	NA
AVERAGE	3.17%	NA
Pacific Northwest Office		
RANGE	2.00%-4.50%	3.00%-6.00%
AVERAGE	3.04%	4.90%
San Francisco Office		
RANGE	1.50%-4.00%	2.50%-7.00%
AVERAGE	2.50%	4.58%
Southeast Florida Office		
RANGE	2.50%-4.00%	3.00%-6.00%
AVERAGE	3.04%	4.75%
Washington, DC Office		
RANGE	2.00%-4.00%	4.50%-7.00%
AVERAGE	3.08%	5.08%
National Industrial		
RANGE	1.00%-5.00%	3.00%-30.00%
AVERAGE	3.12%	6.60%
National Apartment		
RANGE	2.50%-5.00%	NA
AVERAGE	3.73%	NA

any of the participants' investment criteria.

- The range also accommodates variations in pricing across geographic and quality components of investors' strategies. The lower end of the range may represent the rates at which participants buy properties in more expensive geographic markets and especially higher-quality properties. An example is the recent pricing of re-gional malls. Participants report that prices of Class-A malls in general did not decline; in fact, prices may even be increasing. By contrast, prices on some Class-B and C malls are still thought to be down 10% to 20%.

Surveying real estate market participants is certainly an inexact science, as this and other issues attest. We will continue to report on imperfections and idiosyncracies of the real estate investment market so that readers of our Survey will understand the assumptions that underlie the data we present. Our annual report on NOI definitions is an example of this ongoing effort. ■

National Regional Mall Market

One at a time, some regional mall owners are adding centers to their portfolios in states where they already have a significant presence. Their goal is to dominate a large geographic area while achieving economies of scale in marketing, leasing, and management. In a generally quiet transaction market, most trades are single-property sales, although some recent deals involve two to four malls. The malls that are most in demand are those with strong credit tenants in markets with high barriers to entry.

A few well-capitalized REITs are still buying, but they do not dominate the market as was the case a year ago. Currently they are more likely to be joint venture partners with pension funds. In most deals, buyers are pension funds alone or private investors. Sellers include life insurance companies and pension funds divesting property in maturing funds.

The consensus among regional mall participants is that prices did indeed fall off a bit late last year. The effect on Class-A properties seems to have been minimal, and some investors believe that Class-A properties generally retained their values. In fact, prices may even be increasing. By contrast, Class-B and C malls "took the biggest hit, with prices down perhaps 10% to 20%." Participants say, however, that there have not been enough transactions in the new year to verify their sense of current pricing levels.

The majority of regional malls are priced below replacement cost. Participants say that prices in the national regional mall market range from 80.0% to 105.0% of replacement cost. The average price is 88.8% of cost. Estimates of value change over the next 12 months range from 0.0% to 10.0%; on average, values are expected to increase 3.5%.

Key value indicators are shown in Table 5. All indicators moved this quarter. The average discount rate (IRR) decreased 14 basis points to 11.14%. The average overall cap rate (OAR) decreased a minor 4 basis points to 8.41%.

Cap rates for top-tier malls are considerably lower than the average OAR. For A and A+ malls, the range of cap rates is from 7.00% to 9.50%; the average OAR for A+ malls is 7.75%, up 25 basis points from last quarter. The average OAR for A malls is 8.11%, 16 basis points higher than last quarter. For B+ malls, the range is from 7.50% to 10.00%; the average is 8.96%. For B malls, the range is from 8.25% to 11.00%; the average is 9.83%.

Although there is "decent demand" for regional malls and upscale community centers, retail continues to be the least desirable property type. Reasons are concern about overbuilding, changed and changing consumer spending and shopping practices, and a continuous onslaught of competition for consumer dollars. Occupancy in good-quality retail property is at sufficient levels now. But institutional buyers, who are long-term investors, are considering how and by whom retail space will be occupied in the future. Consequently, they are interested in potential competition such as the effect of Internet commerce on retail real estate. Total 1998 Internet sales of approximately $13 billion represent only about 1.0% of total retail sales. However, revenue increased 230.0% over last year, according to Boston Consulting Group and shop.org. A significant portion (59%) of the revenue from on-line sales now goes to retailers who also have physical stores, but if dramatic increases continue, ultimately retailers will rethink their space needs. ■

Table 5
National Regional Mall Market
FIRST QUARTER 1999

KEY INDICATORS	CURRENT QUARTER	LAST QUARTER	YEAR AGO
Discount Rate (IRR)[a]			
RANGE	9.50%–12.50%	10.00%–13.00%	10.00%–13.00%
AVERAGE	11.14%	11.28%	11.50%
CHANGE (Basis Points)	—	–14	–36
Overall Cap Rate (OAR)[a]			
RANGE	7.00%–10.50%	7.00%–11.00%	7.00%–11.00%
AVERAGE	8.41%	8.45%	8.51%
CHANGE (Basis Points)	—	–4	–10
Market Rent Change Rate[b]			
RANGE	0.00%–4.00%	0.00%–4.00%	0.00%–4.00%
AVERAGE	3.03%	3.00%	3.00%
CHANGE (Basis Points)	—	+3	+3
Expense Change Rate[b]			
RANGE	3.00%–4.00%	3.00%–4.00%	3.00%–4.00%
AVERAGE	3.39%	3.60%	3.68%
CHANGE (Basis Points)	—	–21	–29
Residual Cap Rate			
RANGE	7.50%–10.50%	7.50%–11.00%	7.50%–11.00%
AVERAGE	8.56%	8.76%	8.80%
CHANGE (Basis Points)	—	–20	–24

a. Rate on unleveraged, all-cash transactions

b. Initial rate of change

National Power Center Market

The investor pool for power centers is small compared with that of buyers of neighborhood and community centers. This and the fact that power centers are relatively new and have not yet appreciated enough to warrant selling contribute to a generally slow transaction market.

The most prominent buyers are pension funds that want power centers for balance among the retail properties in their portfolios. The most enthusiastic owners are investors who have discovered a profitable niche in this retail format. In many cases they focus on development of power centers to hold for the steady income from long-term quality credit leases.

Among the strategies of successful power center owners is the formation of joint ventures with local partners and ongoing relationships with high-credit tenants. Developing a good network of credit tenants is key. "It is a learning curve through which you become more familiar with the terms that they require and the ways they do business," says one participant. "With each center it becomes easier to sign favorable deals."

Credit drives this market, and a power center is only as good as the credit quality of its anchor tenants. The most frequently stated reason investors give for not investing in power centers is concern about releasing the large space that would be left by a vacating anchor. Often the space is an odd size and has been specially built for the original tenant.

A significant trend in the power center market is the dwindling supply of anchor tenants. Because of intense competition, the industry segment of "category killers" is experiencing serious contraction. Some retailers, such as Toys 'R' Us, are closing stores, while bankruptcy takes its toll on other big-box retailers. In addition, many former anchor tenants, including behemoth Home Depot, are constructing their own properties.

Supply and demand are closer to equilibrium than they have been for a number of years. This is due to a recent construction slowdown.

Prices in the national power center market are at replacement cost, and minimal value change is forecast over the next 12 months. Consequently, fluctuations in value indicators are generally minor, as can be seen in comparing current indicators with those of the year-ago quarter (see Table 6). This quarter the average discount rate (IRR) increased 3 basis points to 11.32%; it had remained at 11.29% for the prior two quarters. The current average is 10 basis points lower than in the year-ago quarter.

The average overall cap rate (OAR) increased 5 basis points to 9.82%. The rate is 8 basis points lower than one year ago.

Because the long-term leases on anchor space generally provide little potential for rent growth, OARs are relatively high. However, in the typical power center deal, as in-line store space increases, the potential for rent growth increases and cap rates usually decline. As a result, OARs tend to be highest on power centers that are 100% big-box space; and they tend to be lowest on power centers that are 75% big-box and 25% in-line stores.

Once again, recent retail sales statistics demonstrate that consumers continue to like the discount and other value-oriented stores that tenant power centers. The largest gains in 1998 holiday and post-holiday retail sales compared with one year ago were among such retailers. January showed Wal-Mart up 16.5%. Other results were Dollar General Corp. plus 22.6%, Ames plus 13.8%, and Kmart plus 5.6%. ■

Table 6
National Power Center Market
FIRST QUARTER 1999

KEY INDICATORS	CURRENT QUARTER	LAST QUARTER	YEAR AGO
Discount Rate (IRR)[a]			
RANGE	10.25%–12.50%	10.00%–12.50%	9.50%–12.50%
AVERAGE	11.32%	11.29%	11.42%
CHANGE (Basis Points)	—	+3	–10
Overall Cap Rate (OAR)[a]			
RANGE	8.00%–10.50%	8.00%–10.50%	9.00%–11.00%
AVERAGE	9.82%	9.77%	9.90%
CHANGE (Basis Points)	—	+5	–8
Market Rent Change Rate[b]			
RANGE	0.00%–4.00%	0.00%–4.00%	0.00%–5.00%
AVERAGE	2.83%	2.83%	2.92%
CHANGE (Basis Points)	—	0	–9
Expense Change Rate[b]			
RANGE	2.00%–4.00%	3.00%–4.00%	3.00%–4.00%
AVERAGE	3.29%	3.38%	3.67%
CHANGE (Basis Points)	—	–9	–38
Residual Cap Rate			
RANGE	9.00%–10.50%	9.00%–10.50%	9.00%–10.50%
AVERAGE	9.83%	9.79%	9.96%
CHANGE (Basis Points)	—	+4	–13

a. Rate on unleveraged, all-cash transactions

b. Initial rate of change

National Strip Shopping Center Market

Transaction activity in the national strip shopping center market is slow, in diametric contrast to the hyperactivity of a year and two ago. The exchange buyers who closed a notable number of deals in the fourth quarter have stepped back, leaving the field open for pension funds, individuals, and, yes, REITs. Not the plethora of REITs that swarmed over the market in their heyday, but more disciplined REITs with continued access to capital.

What is different about some of the REITs that are active now is that, instead of raising capital through the equity capital and unsecured debt markets, they are participating in joint venture deals with institutional investors. Typically, the partners are pension funds. The ventures utilize the REITs' capacity to find and close deals and then to manage the properties. The other REITs that are active are those few that still have the capacity to acquire properties. At the time of the fall 1998 price correction, they had very conservative low leverage balance sheets and more than adequate acquisition lines.

The national strip shopping center market is stronger than it has been in years. Retail in general, and strip centers in particular, recovered more slowly than other property types, but now fundamentals are good. Average vacancy rates are under 10.0%, and centers generally show positive rent growth. For the most part, income streams are satisfactory and tenant sales growth is at or above inflation.

Supply and demand in the grocery- and drugstore-anchored shopping center segment are fairly close to equilibrium. Development has slowed somewhat, but there is always a need for such neighborhood and community centers in housing growth markets. The danger is in misinterpreting growth projections. Development activity may decline further in the coming months because of a lack of capital for development.

On average, prices in the national strip shopping center market are nearly at replacement cost. Participants estimate that they vary from 80.0% to 120.0% of replacement cost. The average is 97.9%. Prices are not expected to rise significantly over the next 12 months; the projected average increase is 1.8%.

Key value indicators are shown in Table 7. The average discount rate (IRR) increased 8 basis points to 11.61%. The average OAR increased 3 basis points to 9.76%, 11 basis points lower than one year ago.

Investors believe that prices have declined — one participant thinks that cap rates are up roughly 50 basis points in his region — but most participants have not changed their criterion rates. Some who have are finding that landing deals at the new rates is tough. "We have raised acquisition cap rates some 10 to 20 basis points but have not been very successful purchasing at this level," says one participant.

Strip shopping centers have traditionally been perceived to pose higher investment risk than regional malls, and both IRRs and going-in cap rates reflected a premium for the higher risk. For the past year, the spread between the average strip center IRR and the regional mall rate has been widening. This quarter the spread is 47 basis points. The strip center OAR has consistently been considerably higher than the regional mall rate. This quarter's OAR premium is 135 basis points.

This market is seen to be a buyers' market for marginal centers. However, sellers have the negotiating advantage in deals for top-quality, high-credit centers. ■

Table 7
National Strip Shopping Center Market
FIRST QUARTER 1999

KEY INDICATORS	CURRENT QUARTER	LAST QUARTER	YEAR AGO
Discount Rate (IRR)[a]			
RANGE	10.00%–14.00%	10.00%–14.00%	10.50%–14.00%
AVERAGE	11.61%	11.53%	11.63%
CHANGE (Basis Points)	—	+8	–2
Overall Cap Rate (OAR)[a]			
RANGE	8.25%–11.50%	8.00%–12.00%	8.00%–13.00%
AVERAGE	9.76%	9.73%	9.87%
CHANGE (Basis Points)	—	+3	–11
Market Rent Change Rate[b]			
RANGE	0.00%–7.00%	0.00%–7.00%	0.00%–5.00%
AVERAGE	3.39%	3.17%	3.15%
CHANGE (Basis Points)	—	+22	+24
Expense Change Rate[b]			
RANGE	2.00%–5.00%	2.50%–5.00%	2.50%–5.00%
AVERAGE	3.25%	3.33%	3.66%
CHANGE (Basis Points)	—	–8	–41
Residual Cap Rate			
RANGE	8.75%–12.00%	8.50%–12.00%	8.50%–12.00%
AVERAGE	10.07%	9.95%	10.04%
CHANGE (Basis Points)	—	+12	+3

a. Rate on unleveraged, all-cash transactions

b. Initial rate of change

National CBD Office Market

The consensus of investors is that CBD office buildings are as good a value as can be found in today's market. Prices on other property types have been bid up to comparatively unprofitable levels. Nonetheless, transaction activity has slowed measurably over the past six months.

There are still deals, and usually more than one contender for each deal, but the multitudes of bidders have disappeared. CBD office transactions tend to be large, generally over $50 million. Consequently, the population of would-be buyers shrank when the majority of REITs pulled out of the market. "They were the big bucks bidders," comments one participant. Today's buyers, primarily pension funds, partnerships, and some foreign entities, are benefitting from the reduced competition as well as the late-1998 price correction.

The most evident sellers are life insurance companies and REITs. Insurance companies have been withdrawing from direct ownership of real estate for the past several years. Some REITs are selling property to raise capital.

CBD office markets are strong, with high occupancy and rising rents. The national CBD vacancy rate is around 11.0%. New construction in most markets is minimal, and tighter credit puts the future of some announced projects in doubt. Still, vacancy rates are likely to rise 1.0% to 2.0% in the next 12 to 24 months.

The excess of supply over demand that will push vacancy rates up is due not so much to the volume of new construction as to diminishing demand. To date, job growth has continued to astound market watchers. Increases in the service sector, which includes office employment, has offset jobs lost in manufacturing due to global financial problems. But the outstanding expansion in new jobs of the past few years is not likely to last indefinitely. At year-end layoffs at corporations such as Boeing and AT&T, which total tens of thousands of jobs, were announced.

More layoffs are likely as a result of the record-setting merger activity last year. In addition, some analysts are projecting that 1999 activity will hit new records. Total dollar amount of 1998 mergers was nearly $1.7 trillion; this included the top seven largest deals in history. The motivation was a drive for pricing power and economies of scale, according to *Fortune*. The inevitable consequence of the mergers among industry's giants is a loss of jobs, perhaps in giant proportions.

Another trend that will affect job growth is the falloff in new businesses. This is the sector that has created thousands of new jobs in recent years. Startups declined 14.0% in 1996 and 4.0% in 1997. Preliminary figures for 1998 project a further drop.

Most CBD office buildings can still be acquired at a large discount to replacement cost, but prices exceed cost in some instances. Participants say that prices in the national CBD office market range from 65.0% to 110.0% of replacement cost. The average price is 91.0% of cost.

Key value indicators are shown in Table 8. For the past two years, values have moved steadily upward. This quarter's changes in rates are indicative of the recent price correction. The average discount rate (IRR) increased 6 basis points to 11.28%. The average overall cap rate (OAR) increased 10 basis points to 8.82%.

Some investors are shying away from markets that were most in demand last year, including San Francisco and Boston, because they think prices are too high. Instead, they are looking at markets that are still rebounding, such as Chicago and Washington, DC. ■

Table 8
National CBD Office Market
FIRST QUARTER 1999

KEY INDICATORS	CURRENT QUARTER	LAST QUARTER	YEAR AGO
Discount Rate (IRR)[a]			
RANGE	9.75%–15.00%	9.50%–15.00%	10.00%–15.00%
AVERAGE	11.28%	11.22%	11.63%
CHANGE (Basis Points)	—	+6	–35
Overall Cap Rate (OAR)[a]			
RANGE	7.00%–11.00%	7.00%–11.00%	7.50%–11.50%
AVERAGE	8.82%	8.72%	9.19%
CHANGE (Basis Points)	—	+10	–37
Market Rent Change Rate[b]			
RANGE	0.00%–8.00%	0.00%–8.00%	0.00%–8.00%
AVERAGE	3.93%	4.00%	3.44%
CHANGE (Basis Points)	—	–7	+49
Expense Change Rate[b]			
RANGE	2.00%–4.00%	2.00%–4.00%	3.00%–5.00%
AVERAGE	3.33%	3.38%	3.67%
CHANGE (Basis Points)	—	–5	–34
Residual Cap Rate			
RANGE	7.50%–11.00%	7.50%–11.00%	8.00%–11.50%
AVERAGE	9.33%	9.32%	9.47%
CHANGE (Basis Points)	—	+1	–14

a. Rate on unleveraged, all-cash transactions

b. Initial rate of change

National Suburban Office Market

"The smaller deals, the ones under $25 million, that's where the action is now that the REITs are gone" reports one participant. In office properties, this means a suburban focus. "Action" is relative, however, and transaction activity is much slower in the absence of the army of REITs. Many buyers are waiting to see if, in the less competitive environment, prices will drop further. At the same time, sellers are taking properties off the market, hoping that prices will rise to last summer's levels.

Investors perceive that prices for suburban office buildings are down, but they are quick to mention that the magnitude of change is highly dependent on quality and geographic area. While the consensus is that suburban office prices were hit harder than those in CBD markets, prices of suburban Class-A buildings in the better submarkets held their value or dipped maybe 5.0%. Estimates of the overall damage are around 10.0%, although in some locations it could be 15.0%.

The underlying fundamentals in suburban office markets are still good. The national vacancy rate is about 11.0%. While construction in some suburban markets over the past couple of years boomed, it has been a pop compared with total inventory. The amount of office space projected to come online in 1999 amounts to less than 4.0% of existing inventory. Tighter capital for new development is likely to keep the overall percentage small.

Concerns about overbuilding are confined to certain markets. Those where near-term demand does not match projected supply additions include Atlanta, Dallas, Orlando, Portland, Salt Lake City, Seattle, and San Jose, according to Donaldson, Lufkin & Jenrette research. Markets where proposed construction is less than projected demand include Las Vegas, San Antonio, New York, and San Diego.

Properties in the national suburban office market are close to fully priced. Participants say that prices range from 85.0% to 115.0% of replacement cost. The average price is 97.8% of cost. Price increases over the next 12 months in some markets may be as high as 10.0%. The average projected price increase is 4.3%, down 50 basis points from last summer.

Key indicators are shown in Table 9. This quarter's changes are indicative of investors' response to the late-1998 price correction. The average overall cap rate (OAR) is up 14 basis points, the greatest increase in any of the national markets. At 9.17%, the rate is nearly identical to the year-ago rate. The average discount rate (IRR) increased 5 basis points to 11.11%.

As new price levels of office buildings settle in, the spreads between value indicators in the national CBD office market and the national suburban office market may widen. Comparisons of value indicators show an average suburban IRR 17 basis points lower than that in the CBD office market. The suburban OAR is 35 basis points higher than the CBD rate. The average initial market rent change rate in the suburban market is 14 basis points lower than in the CBD market. Only two quarters ago the suburban rate was 65 basis points higher.

Although prices are high, many investors believe the suburban market still holds some opportunities. However, this may be primarily because there are few alternatives, with stock prices high and bond rates low. ■

Table 9
National Suburban Office Market
FIRST QUARTER 1999

KEY INDICATORS	CURRENT QUARTER	LAST QUARTER	YEAR AGO
Discount Rate (IRR)[a]			
RANGE	9.75%–12.50%	9.50%–12.50%	10.00%–13.50%
AVERAGE	11.11%	11.06%	11.41%
CHANGE (Basis Points)	—	+5	–30
Overall Cap Rate (OAR)[a]			
RANGE	7.50%–10.50%	7.50%–10.50%	7.50%–10.50%
AVERAGE	9.17%	9.03%	9.18%
CHANGE (Basis Points)	—	+14	–1
Market Rent Change Rate[b]			
RANGE	0.00%–8.00%	0.00%–8.00%	0.00%–8.00%
AVERAGE	3.79%	4.02%	4.04%
CHANGE (Basis Points)	—	–23	–25
Expense Change Rate[b]			
RANGE	2.00%–4.00%	2.00%–4.00%	3.00%–5.00%
AVERAGE	3.10%	3.25%	3.59%
CHANGE (Basis Points)	—	–15	–49
Residual Cap Rate			
RANGE	8.00%–11.00%	8.00%–11.00%	8.25%–11.00%
AVERAGE	9.49%	9.47%	9.57%
CHANGE (Basis Points)	—	+2	–8

a. Rate on unleveraged, all-cash transactions

b. Initial rate of change

Atlanta Office Market

Boasting an unstoppable economy, Atlanta continues to astound investors who expect that the massive amount of new office development will sink the market. "The Atlanta office market is overbuilt on paper," says one participant. He points out that part of the reason for increasing vacancy rates is that some vacant space is new. "It's not occupied but has been leased."

The strong local economy is evidenced in the number of new jobs created annually. The Atlanta MSA will see 46,900 new jobs in 1999, a 2.3% increase over 1998, when the growth rate was also over 2.0%. Atlanta is the regional headquarters for a number of international companies and large U.S. firms, such as Lucent Technology. Although the economy is diversified, the most prominent growth segment is high technology, especially telecommunications and wireless communications. Other growth industries in Atlanta are transportation and tourism. It is the regional center for warehousing and distribution as well as the state's top tourist destination.

Demand for office space increased in 1998 over 1997 levels, albeit not at a sufficient pace that all the new space that came on-line could be occupied. As a result, the vacancy rate at the end of the year was 11.2%, a 50-basis-point increase over year-end 1997. Net occupancy was more than 50.0% higher than in 1997, however. Jamison Research, Inc. reports 1998 net occupancy of 5.6 million square feet, 1.8 million square feet more than in the prior year. During 1999 vacancy rates will no doubt continue to trend upward.

Expectations of the level of new development vary. Although diminished capital lending has slowed the number of projects going into the pipeline, some observers think that development could increase in submarkets in which the amount of new supply has not been great.

Rents in Class-A buildings range from $19.50 to $22.75 per square foot. New construction came on-line at high rents, but some participants report that they have flattened or even dropped slightly in Class-A buildings. Class-B rents have held steady. Some developers are reportedly on the verge of introducing free rent concessions.

Values in the Atlanta office market had increased 30.0% since 1994, according to one report. The average sale price of office properties had been recorded at $112 per square foot, while Class-A buildings generally have been sold at approximately $140 per square foot. However, the shortage of REITs in the marketplace has affected prices. They were conspicuous buyers in the first half of 1998 and accounted for more than 40.0% of the dollar volume of purchases in 1997.

Although prices in the Atlanta office market jumped during the first half of 1998, the price correction in the second half brought them back to year-ago levels. This is demonstrated in an average discount rate (IRR) that is close to the first quarter 1998 rate and an average overall cap rate (OAR) identical to the year-ago rate. The average IRR declined 9 basis points to 11.08% (see Table 10). The rate plunged 43 basis points last quarter. The average OAR is up 2 basis points to 9.23%.

Some buildings in the Atlanta office market are still priced below replacement cost, but most are fully priced. The range of prices is from 90.0% to 110.0% of replacement cost. The average price is 100.0% of cost. Prices are expected to remain fairly flat; the projected average increase over the next 12 months is only 1.9%.

Atlanta is increasingly suffering from the level of demand on its infrastructure as well as environmental problems. Unless corrected, this could be the variable to reduce economic growth in the future. ■

Table 10
Atlanta Office Market
FIRST QUARTER 1999

KEY INDICATORS	CURRENT QUARTER	LAST QUARTER	YEAR AGO
Discount Rate (IRR)[a]			
RANGE	9.75%–12.00%	9.50%–13.50%	9.75%–12.00%
AVERAGE	11.08%	11.17%	11.19%
CHANGE (Basis Points)	—	–9	–11
Overall Cap Rate (OAR)[a]			
RANGE	8.00%–10.50%	8.00%–10.50%	8.00%–10.00%
AVERAGE	9.23%	9.21%	9.23%
CHANGE (Basis Points)	—	+2	0
Market Rent Change Rate[b]			
RANGE	0.00%–3.50%	0.00%–3.50%	2.00%–5.00%
AVERAGE	2.21%	2.29%	3.54%
CHANGE (Basis Points)	—	–8	–133
Expense Change Rate[b]			
RANGE	3.00%–3.50%	3.00%–4.00%	3.00%–4.00%
AVERAGE	3.10%	3.35%	3.55%
CHANGE (Basis Points)	—	–25	–45
Residual Cap Rate			
RANGE	9.00%–11.00%	9.00%–11.00%	9.00%–11.00%
AVERAGE	9.46%	9.44%	9.60%
CHANGE (Basis Points)	—	+2	–14

a. Rate on unleveraged, all-cash transactions
b. Initial rate of change

Chicago Office Market

Last year's hottest office investment markets are giving way to markets that are still on the rebound. Chicago, especially downtown, is high on investors' lists. They are attracted by the upside potential of rising rents in the still-tightening space market. Meanwhile, interest in many suburban submarkets is cooling, due to the amount of new construction that has come on-line.

Greatly due to demand for space downtown, the overall vacancy rate continued to decline last year, to 13.3% in the fourth quarter. Only about 6.0% of Class-A space is available. As a result, average Class-A rents increased to $29.84 gross per square foot, according to Cushman & Wakefield. This is a 20.2% jump over a year earlier. Tenants who could not get into prime space had to be satisfied with Class-B space, which pushed average rents in this tier to $23.57 gross per square foot, a 21.4% increase. Rental rate hikes are expected to moderate to about 10.0% this year, but many leases that will expire in the near future are still below market rent.

Lurking on the horizon, however, is the prospect of lower job growth rates in the metropolitan area, which will hit downtown hardest. The peak of job growth in this business cycle was in 1995, when the number of new jobs was 94,000, a 2.5% increase over 1994. In 1998 approximately 63,000 new jobs were created, an increase just over 1.5%. This is the same number of jobs created in 1996, but 5,000 fewer than were added in 1997. One participant projects that in 1999 only about 31,000 will be added and only 11.0% of them (3,000 to 4,000) will be in downtown Chicago.

Suburban submarkets will need the job growth. More than 2.5 million square feet of office space were brought on-line last year, and at year-end approximately 1 million additional square feet were under construction. At 14.5%, the fourth-quarter vacancy rate was one full percentage point higher than one year earlier. The Class-A rate was 17.6%. Most of the construction has been in the east-west corridor, where in 1998 the vacancy rate increased from 1.0% to 7.0%. Currently, the O'Hare submarket is the tightest suburban submarket.

Prices are thought to have peaked with the sale of the trophy John Hancock Center at somewhere between $200 and $225 per square foot. The Shorenstein Company purchased the office and retail space, which accounts for 860,000 square feet of the 2.8 million-square-foot tower, for an estimated $220 million.

Even as many REITs are noticeably absent in the Chicago transaction market, Prime Group Realty Trust purchased 33 West Monroe, a 28-story Class-A office building. At approximately $94.5 million, the price was $111.60 per square foot. This represents about 51.0% of replacement cost, according to the Prime Group.

While some existing buildings can still be acquired at significant discounts to replacement cost, especially in the CBD, participants say that across the Chicago office market, prices in general range from 80.0% to 110.0% of replacement cost. The average price is 96.1% of cost.

Key value indicators are shown in Table 11. All cash flow forecast assumptions shifted this quarter. Both the average discount rate (IRR) and average overall cap rate (OAR) are up. The average IRR increased 16 basis points to 10.95%. The average OAR is up 6 basis points to 9.11%.

Prices are off 5.0% to 15.0% from last year's peak, according to analysts. This and the potential for near-term rent growth downtown and in certain suburban submarkets are factors that are likely to produce a lively transaction market in the coming months. ■

Table 11
Chicago Office Market
FIRST QUARTER 1999

KEY INDICATORS	CURRENT QUARTER	LAST QUARTER	YEAR AGO
Discount Rate (IRR)[a]			
RANGE	9.29%–13.00%	9.50%–13.00%	10.00%–13.00%
AVERAGE	10.95%	10.79%	11.31%
CHANGE (Basis Points)	—	+16	–36
Overall Cap Rate (OAR)[a]			
RANGE	8.00%–10.25%	8.00%–10.00%	8.50%–10.00%
AVERAGE	9.11%	9.05%	9.25%
CHANGE (Basis Points)	—	+6	–14
Market Rent Change Rate[b]			
RANGE	0.00%–6.00%	0.00%–9.00%	0.00%–6.00%
AVERAGE	4.00%	4.38%	3.04%
CHANGE (Basis Points)	—	–38	+96
Expense Change Rate[b]			
RANGE	2.00%–4.00%	3.00%–4.00%	3.00%–4.00%
AVERAGE	3.09%	3.25%	3.54%
CHANGE (Basis Points)	—	–16	–45
Residual Cap Rate			
RANGE	8.00%–10.50%	8.00%–10.25%	8.50%–10.25%
AVERAGE	9.25%	9.18%	9.42%
CHANGE (Basis Points)	—	+7	–17

a. Rate on unleveraged, all-cash transactions

b. Initial rate of change

Dallas Office Market

"The pipeline has narrowed since the capital crunch hit," says one participant. This is definitely advantageous in a market that is frequently mentioned in discussions of office markets that could become overbuilt. The current difficulty in securing financing is compounded by a slowdown in preleasing of new buildings. As a result, some projects have been shelved, and many announced buildings will not go up.

With more than 11 million square feet of new office space under development, projected supply growth is on the verge of exceeding demand growth significantly. Projections of the magnitude of supply in excess of demand over the next 12 to 18 months range from 4.0% to 7.0%. Suburban Dallas vacancy rates could rise to as high as 19.0%, according to Lehman Brothers.

Dallas has experienced tremendous economic expansion, which brought it back from the excesses of the 1980s building binge. But growth is moderating, and there are some clouds on the horizon that could upset the economy.

Last year's job growth is not likely to meet some early optimistic projections. The probable increase of 77,000 new jobs is down from the annual average of 86,000 since 1994. Threatening existing jobs are announcements of layoffs by several major Dallas metroplex employers.

Although vacancies in the Dallas office market increased last year, rents and occupancies went up as well. Average rent marketwide was over $20.00 per square foot, an increase of nearly 8.0% over the year-ago rate. The average Class-A rent is approximately $24.00 per square foot; it is over $29.00 in the tightest submarkets. Many market watchers expect that rents will level or even fall this year as a result of the new space that will be delivered.

As in other transaction markets, REITs are conspicuous only by their absence. An exception is Equity Office Trust. The acquisition of two office buildings in Irving early this year brought Equity's Dallas office portfolio to 4.2 million square feet.

Prices in the Dallas office market climbed to nearly record heights in the first half of 1998 alone, but the correction in the second half brought them closer to year-ago levels. Participants estimate that properties can be bought for 50.0% to 110.0% to replacement cost. The average price is 88.4% of cost. This is a 190-basis-point decline since fourth quarter 1998.

Key value indicators in the Dallas office market are shown in Table 12. Current and last-quarter indicators are for Dallas alone; indicators for the year-ago quarter are for the combined Dallas-Houston office market. All cash flow forecast indicators shifted this quarter; together, they point to lower values.

The average discount rate (IRR) decreased 2 basis points to 11.42%. The change last quarter 1998 was a 16-basis-point decrease on the heels of a 7-basis-point decline in the prior quarter.

The average overall cap rate (OAR) jumped 27 basis points to 9.24%. This follows a 14-basis-point increase last quarter.

The greatest change in key indicators is the 72-basis-point plunge in the average initial market rent change rate. Clearly, most investors are no longer including large rent increases in their analyses. In at least one submarket, Far North Dallas, there is so much vacant space that landlords are offering concessions.

Investor interest in Dallas continues to be focused on suburban submarkets. "We hesitate to go into downtown markets such as Dallas, where the CBD is the market of last resort," comments one participant. ■

Table 12
Dallas Office Market
FIRST QUARTER 1999

KEY INDICATORS	CURRENT QUARTER	LAST QUARTER	YEAR AGO [c]
Discount Rate (IRR)[a]			
RANGE	10.00%–13.00%	10.00%–14.00%	10.00%–14.00%
AVERAGE	11.38%	11.40%	11.86%
CHANGE (Basis Points)	—	–2	–48
Overall Cap Rate (OAR)[a]			
RANGE	7.50%–12.00%	6.50%–11.00%	7.50%–12.00%
AVERAGE	9.24%	8.97%	9.48%
CHANGE (Basis Points)	—	+27	–24
Market Rent Change Rate[b]			
RANGE	0.00%–10.00%	0.00%–10.00%	0.00%–10.00%
AVERAGE	3.34%	4.06%	3.94%
CHANGE (Basis Points)	—	–72	–60
Expense Change Rate[b]			
RANGE	2.50%–4.00%	3.00%–4.00%	3.00%–4.00%
AVERAGE	3.35%	3.47%	3.83%
CHANGE (Basis Points)	—	–12	–48
Residual Cap Rate			
RANGE	8.00%–12.00%	8.00%–11.00%	8.00%–12.00%
AVERAGE	9.50%	9.44%	9.71%
CHANGE (Basis Points)	—	+6	–21

a. Rate on unleveraged, all-cash transactions
b. Initial rate of change
c. Year-ago quarter indicators are for combined Dallas-Houston office market.

Houston Office Market

"Bullish" is a word investors often use in describing their interest in Houston. Fundamentals in the Houston office market are solid, and development has been limited.

Houston's economy continues to be robust, and despite energy industry problems, the office market has not been adversely affected. "Most oil experts believe that $11 a barrel oil is short lived," says one participant. "Production is being cut so much that by the end of this year we'll start seeing oil prices up to $16 to $18 per barrel." Down the road there may be repercussions from the consolidation in the oil industry, but the outlook for the natural gas industry is relatively optimistic.

One of the tightest office submarkets is the Energy Corridor, where Class-A space is nearly fully occupied; the vacancy rate was less than 1.0% at midyear. Other submarkets in which Class-A space is at a premium are the Far Southwest, Katy Freeway, and Uptown Galleria. Average Class-A rents in these submarkets range from just over $22.00 to over $24.00 per square foot. Class-A space is a small portion of the total office inventory, however, and the gap between Class-A and Class-B rents is considerable, with Class-A rents approximately 40.0% higher. Overall, rents have leveled off in recent quarters, and fewer investors are incorporating rent spikes into their analyses.

Downtown Houston is attractive to investors. It is currently undergoing a renaissance, with construction of the new Ballpark at Union Station and loft conversions to residential use. While there is discussion of new office projects, rents have not increased to a level that would justify construction.

Recent office construction has been confined to suburban markets, most of it in west Houston. While some analysts believe it may have been premature, the volume has not been as excessive as some other markets. Toward the end of 1998, 2.6 million square feet of office space were under way. This represents an increase to total inventory of about 1.0%.

Houston office properties are priced low compared with comparable markets in the nation. Average prices range from approximately $55 to $95 per square foot. The highest price paid to date is approximately $150 per square foot for One Riverway. The largest recent transaction is the sale of Pennzoil Place for $200 million, or approximately $143 per square foot. Although REITs were buyers in most of the largest transactions last year, a German family was the buyer of Pennzoil Place, and CIGNA bought One Riverway.

In general, buildings can be acquired for 50.0% to 105.0% of replacement cost. The average price is 83.5% of cost. This is a 120-basis-point increase over last quarter. Participants expect values to rise over the next 12 months from 3.0% to 15.0%, with an average of 7.3%.

Key value indicators are shown in Table 13. Current- and last-quarter indicators are for Houston alone; indicators for the year-ago quarter are for the combined Dallas-Houston office market. There are large swings in the cash flow forecast assumptions this quarter. This is due more to a change in the Houston survey participant base than it is indicative of significantly declining values.

The average discount rate (IRR) increased 12 basis points to 11.78%. The average overall cap rate (OAR) increased 33 basis points to 9.43%.

Houston's past may be the biggest deterrent to investors. "Some people are scared of Houston because of its past volatility and the lack of zoning constraints," observes one participant. ■

Table 13
Houston Office Market
FIRST QUARTER 1999

KEY INDICATORS	CURRENT QUARTER	LAST QUARTER	YEAR AGO [c]
Discount Rate (IRR)[a]			
RANGE	10.00%–13.50%	10.00%–14.00%	10.00%–15.00%
AVERAGE	11.78%	11.66%	11.85%
CHANGE (Basis Points)	—	+12	–7
Overall Cap Rate (OAR)[a]			
RANGE	8.00%–12.00%	6.50%–11.00%	7.00%–12.00%
AVERAGE	9.43%	9.10%	9.15%
CHANGE (Basis Points)	—	+33	+28
Market Rent Change Rate[b]			
RANGE	0.00%–8.00%	2.00%–10.00%	0.00%–10.00%
AVERAGE	3.48%	4.70%	4.59%
CHANGE (Basis Points)	—	–122	–111
Expense Change Rate[b]			
RANGE	3.00%–4.00%	3.00%–4.00%	3.00%–4.00%
AVERAGE	3.50%	3.45%	3.67%
CHANGE (Basis Points)	—	+5	–17
Residual Cap Rate			
RANGE	8.00%–12.00%	8.00%–11.00%	9.00%–12.00%
AVERAGE	9.58%	9.53%	9.69%
CHANGE (Basis Points)	—	+5	–11

a. Rate on unleveraged, all-cash transactions

b. Initial rate of change

c. Year-ago quarter indicators are for combined Dallas-Houston office market.

Los Angeles Office Market

Regional economic growth above the U.S. average is a strong draw for investors in the Los Angeles office market. Southern California growth is also better than the state as a whole. Job growth in 1998, which was positive in all industries, exceeded the California average, which was 2.5%. In metropolitan Los Angeles, the office market continues to benefit from the influx of new businesses and expansion of existing firms over the past several years. Occupancy is up in most submarkets, accompanied by rising rents. Development is under way in strong submarkets where rent levels indicate that it is warranted.

A surprising amount of interest is focused on the downtown market. Although it is still soft, with vacancies in the high teens, investors are apparently counting on the resurgence momentum to continue. Last year's typical sale prices ranging from $125 to $185 per square foot were eclipsed by the December sale of 801 Tower for an estimated $195 per square foot. The 24-story property is the newest building downtown. Another Class-A building on the corner of Figueroa and Sixth went for approximately $160 per square foot. Buyers of both buildings are private investors. Class-C buildings downtown are drawing telecommunications and other high-tech tenants. As in other cities, a high-tech district is developing.

Prices in the favored West Los Angeles and Tri-Cities areas are considerably higher than in other submarkets. Class-A buildings go for $250 to $300 per square foot. The price for the 21-story trophy tower at 100 Wilshire in Santa Monica was over $360 per square foot. An advisor bought the tower on behalf of an institutional investor; the seller was Japan's Asahi Urban Development, which purchased it during the booming 1980s.

Absorption has slowed in the Tri-Cities due to a decrease in demand from the entertainment industry. Despite this and the new space that has been developed, the submarket is still strong. Demand has increased from the technology and service sectors. The 215,000-square-foot Media Studio was delivered in the fourth quarter, and Glendale Plaza, which is 520,000 square feet, is scheduled to open this quarter.

Office properties in the Los Angeles market offer considerable upside potential since they are generally still available at less than replacement cost. Across the market, prices range from 75.0% to 100.0% of replacement cost. The average price is 86.4% of cost. Prices are expected to increase between 2.0% and 10.0% over the next 12 months. The average projected increase is 7.1%.

Key value indicators are shown in Table 14. All cash flow assumptions shifted this quarter, but changes to the average discount rate (IRR) and average overall cap rate (OAR) are minor. Comparison with the year-ago rates shows much higher values. The average IRR decreased a negligible 1 basis point to 11.63%. The current rate is 22 basis points lower than in the year-ago quarter. The average OAR increased 3 basis points to 8.74%. The average OAR is now 41 basis points lower than it was one year ago. The average initial market rent change rate dropped 44 basis points. The rate is 75 basis points higher than in the year-ago quarter.

The most noteworthy development project under way in the Los Angeles office market is the 10-story office building in the Howard Hughes Center in the Westside submarket. This building will be close to 250,000 square feet and is expected to come on-line early in 2000. Ultimately, the owner plans to add two more office buildings, one four stories and the other 12 stories. ■

Table 14
Los Angeles Office Market
FIRST QUARTER 1999

KEY INDICATORS	CURRENT QUARTER	LAST QUARTER	YEAR AGO
Discount Rate (IRR)[a]			
RANGE	10.00%–14.00%	10.00%–15.00%	10.00%–15.00%
AVERAGE	11.63%	11.64%	11.85%
CHANGE (Basis Points)	—	–1	–22
Overall Cap Rate (OAR)[a]			
RANGE	7.00%–10.50%	7.00%–10.25%	7.00%–12.00%
AVERAGE	8.74%	8.71%	9.15%
CHANGE (Basis Points)	—	+3	–41
Market Rent Change Rate[b]			
RANGE	2.50%–10.00%	2.50%–10.00%	0.00%–10.00%
AVERAGE	5.34%	5.78%	4.59%
CHANGE (Basis Points)	—	–44	+75
Expense Change Rate[b]			
RANGE	3.00%–4.00%	3.00%–4.00%	3.00%–4.00%
AVERAGE	3.42%	3.44%	3.67%
CHANGE (Basis Points)	—	–2	–25
Residual Cap Rate			
RANGE	8.00%–11.25%	8.00%–11.00%	9.00%–12.00%
AVERAGE	9.30%	9.28%	9.69%
CHANGE (Basis Points)	—	+2	–39

a. Rate on unleveraged, all-cash transactions

b. Initial rate of change

Manhattan Office Market

Investors say that Manhattan office building prices are too high for buyers but not high enough to induce owners to sell. Owners seem determined to hold on to properties until prices recover from last year's correction. Some analysts believe that the correction was greater in Manhattan than in most other office markets.

"Prices were so out of control that buyers didn't realize the extent until the competition went away," says one participant. Prices declined then, and cap rates are estimated to have jumped as much as 50 basis points for a short time before they settled. Now investors perceive that they have stabilized, but transaction activity is slow and it is hard to get a handle on price levels. The deals that died last fall when the credit crunch hit and most REITs pulled out were not resurrected, and few deals have been struck yet in the new year.

There is little doubt, however, that activity will pick up in the near future. CBD office buildings offer the best remaining opportunities in this mature real estate cycle, and Manhattan is invariably mentioned as a target market.

Manhattan is one of the tightest office markets in the nation, and demand growth is expected to exceed supply growth over the next 18 months. Despite announced layoffs on Wall Street and expected cutbacks by major banks, the space market should remain tight. An increase of 35,000 new jobs in 1999 is projected. The gains will be in tourism, communications, and media and professional services.

Office development in Manhattan is minimal, with most "new" space the result of rehabbing older buildings. "There's only the Bear Sterns building, which will be occupied by them, and the projects in Times Square — that's why rents are so good," observes one participant.

Leasing activity is excellent; blocks of space over 10,000 square feet are nonexistent, and it is not easy to find 7,500 to 8,000 square feet. Triple-A space on upper floors with a view goes for $60 to $65 per square foot.

Prices for Manhattan office properties are still generally below replacement cost, and discounts of 10.0% to 40.0% are the norm. Those at the greatest discount are Class-B properties, but prices of these buildings are rising. With almost no new construction in Manhattan, buildings that can be renovated are in great demand. Participants estimate that the average price of Class-A and Class-B properties together is 80.0% of replacement cost. Prices are expected to increase from 3.0% to 10.0% over the next 12 months; the average projected increase is 7.9%.

Key value indicators are shown in Table 15. All cash flow forecast assumptions shifted this quarter. The greatest change is a 16-basis-point increase in the average overall cap rate (OAR). It had remained at 8.84% last quarter, following a 30-basis-point plunge in third quarter 1998.

The average discount rate (IRR) increased 3 basis points to 11.09%. The average IRR is now 29 basis points lower than one year ago.

Manhattan and the historic Wall Street district got a psychological boost, albeit an expensive one, when the New York Stock Exchange decided to remain in New York. The city and state agreed to a $560-million package of subsidies and tax breaks to keep the "Big Board" in residence. It is the largest subsidy in New York's history. The NYSE will construct a 60-story tower across from its present building. The project, which will be started in 2001 and completed in 2004, will be the first new Downtown office building since the 1980s. It will contain two 50,000-square-foot trading floors. The exchange will occupy an additional 650,000 square feet. ■

Table 15
Manhattan Office Market
FIRST QUARTER 1999

KEY INDICATORS	CURRENT QUARTER	LAST QUARTER	YEAR AGO
Discount Rate (IRR)[a]			
RANGE	9.75%–13.00%	9.75%–13.00%	10.00%–14.00%
AVERAGE	11.09%	11.06%	11.38%
CHANGE (Basis Points)	—	+3	–29
Overall Cap Rate (OAR)[a]			
RANGE	7.50%–10.00%	7.50%–10.00%	7.50%–12.00%
AVERAGE	9.00%	8.84%	9.14%
CHANGE (Basis Points)	—	+16	–14
Market Rent Change Rate[b]			
RANGE	0.00%–6.00%	0.00%–6.00%	0.00%–10.00%
AVERAGE	3.67%	3.56%	3.44%
CHANGE (Basis Points)	—	+11	+23
Expense Change Rate[b]			
RANGE	3.00%–5.00%	3.00%–5.00%	3.00%–5.00%
AVERAGE	3.56%	3.61%	3.72%
CHANGE (Basis Points)	—	–5	–16
Residual Cap Rate			
RANGE	8.00%–10.50%	7.00%–10.50%	7.00%–11.00%
AVERAGE	9.20%	9.08%	9.11%
CHANGE (Basis Points)	—	+12	+9

a. Rate on unleveraged, all-cash transactions

b. Initial rate of change

Pacific Northwest Office Market

Sentiment is mixed on the potential effect on the Seattle office market of Boeing's announced 12,000-person reduction. The company says that the reduction will be accomplished mostly through attrition. The optimists believe that the ripple effect will be minor, that any slack will be picked up through in-migration of companies that want to take advantage of Seattle's stable workforce. The other side is exemplified by one participant who observes, "So far the Boeing scare has people only talking about weakness in the market, but there is a softening that is not yet fully visible." A few deals have already been affected. The city took Key Tower off the market because it could not achieve the desired price.

The major Pacific Northwest cities, Seattle and Portland, continue to experience strong economic conditions, although the pace of economic expansion has slowed in recent months. As a result, demand for commercial properties has cooled. The Federal Reserve Board reports that two-thirds of the respondents to its Beige Book survey expect economic growth in the Pacific Northwest and Northern California to be at or below the national level this year.

Rents are high in both Seattle and Portland. Top Class-A space goes for approximately $40 per square foot. Both cities are expected to experience rent growth over the next several years that is greatly above the national average. Projected average annual rent growth through 2002 in both Seattle and Portland is 5.7%, according to REIS Reports.

Office prices across the market are perceived to have dropped somewhat from mid-1998 highs. Some buildings in the Pacific Northwest office market are priced higher than replacement cost, but with the recent price correction, more are available at a discount to the cost benchmark. Prices are 85.0% to 110.0% of replacement cost. The average price is 97.6% of cost. This is slightly lower than last quarter's average. However, some participants expect prices to rebound, increasing as much as 10.0% over the next 12 months; the average projected increase is 3.0%.

Key value indicators in the Pacific Northwest office market are shown in Table 16. The greatest change is the 36-basis-point jump in the average initial market rent change rate. It is one of the few increases in this indicator in any of the surveyed office markets, and it is the highest.

The average discount rate (IRR) decreased 14 basis points to 11.27%. The average overall cap rate (OAR) remains at 9.18% for the second consecutive quarter. It declined 9 basis points last quarter.

A block of more than 180,000 square feet of vacated office space is about to hit the Seattle CBD as a result of the dissolution of a major law firm. Their prime space is leased at $30 per square foot, although the market rent for comparable space is $40 per square foot.

Construction in the Seattle and Portland CBDs is just beginning. The first new downtown Seattle office tower since 1991, Millennium Tower, will add 180,000 square feet of Class-A space. The other likely office project is a 308,000-square-foot building at the convention center. The most notable structure under construction in the Portland CBD is the ODS tower. The building is scheduled to come on-line in September. There is enough pent-up demand in both downtown submarkets to almost assure absorption of the new space. By contrast, so much new space has been added in suburban submarkets that at least one analyst forecasts that supply will outstrip demand over the next 18 months. ■

Table 16
Pacific Northwest Office Market
FIRST QUARTER 1999

KEY INDICATORS	CURRENT QUARTER	LAST QUARTER	YEAR AGO
Discount Rate (IRR)[a]			
RANGE	10.00%–13.00%	10.00%–15.00%	10.00%–15.00%
AVERAGE	11.27%	11.41%	11.53%
CHANGE (Basis Points)	—	–14	–26
Overall Cap Rate (OAR)[a]			
RANGE	8.00%–11.00%	8.00%–11.00%	8.00%–11.25%
AVERAGE	9.18%	9.18%	9.41%
CHANGE (Basis Points)	—	0	–23
Market Rent Change Rate[b]			
RANGE	2.50%–8.00%	0.00%–8.00%	3.00%–8.00%
AVERAGE	4.54%	4.18%	4.14%
CHANGE (Basis Points)	—	+36	+40
Expense Change Rate[b]			
RANGE	2.00%–4.00%	3.00%–4.00%	3.00%–5.00%
AVERAGE	3.34%	3.41%	3.65%
CHANGE (Basis Points)	—	–7	–31
Residual Cap Rate			
RANGE	8.50%–10.50%	8.50%–10.50%	8.25%–10.75%
AVERAGE	9.43%	9.43%	9.52%
CHANGE (Basis Points)	—	0	–9

a. Rate on unleveraged, all-cash transactions

b. Initial rate of change

San Francisco Office Market

Some owners may have missed the peak in the San Francisco office market, but they are selling nonetheless. The divestiture of property by Japanese owners, which has been expected for some time, is clearly under way. In two recent downtown transactions the sellers were Japanese entities, and another Japanese-owned trophy property is on the market.

Tao International sold 111 Sutter Street. The historic 22-story landmark was purchased by privately held Ellis Partners, Inc. for approximately $170 per square foot, or $45 million. The asking price was reported to be $60 million to $70 million, still less than the $75 million price tag when Tao bought it in the mid-1980s.

A joint venture between Hines Interests and the CalPERS pension fund is buying 505 Montgomery Street from Mitsui Fudosan (U.S.A.). The price of the 24-story trophy building is estimated at $95 million, or $305 per square foot.

Finally, Dai-ichi Life Insurance Company of Japan is offering the ultra-trophy Citicorp Center for sale. Although there is no asking price, the sale price of the 43-story tower is expected to exceed $300 per square foot.

While the investment market is "hot as a pistol," leasing activity in San Francisco is slow. Tenants are staying put because there is not much attractive space available. This will change over the next few years as a result of additions to supply through renovated space, sublease space, and new construction. For now the city's office market is one of the strongest of all major U.S. markets. Until recently when some rehabbed space came on-line, downtown was virtually fully occupied.

However, the marketwide vacancy rate began to inch upward late in 1998. The amount of new construction in the suburbs is considered by some analysts to be excessive, given the size of the submarkets and their historical demand. Suburban vacancy rates will no doubt spike later this year. A source of concern is the softness of employment in the Silicon Valley. Year-over-year employment growth slowed to less than 1.0% at the end of 1998, considerably lower than the 2.5% increase for California overall.

The perception among participants is that prices have dropped approximately 10.0% since last summer. Still, overall pricing in the San Francisco office market is close to replacement cost. Prices are 70.0% to 110.0% of replacement cost. The average price is 98.0% of cost. Prices are expected to increase as much as 10.0% over the next 12 months; the average increase is projected at 2.8%.

Key value indicators in the San Francisco office market are shown in Table 17. The average discount rate (IRR) dropped 12 basis points to 10.71%. The average overall cap rate (OAR) inched up by 4 basis points to 8.42%. This nearly offsets last quarter's 5-basis-point decrease. The San Francisco OAR remains the lowest of all surveyed office markets.

The greatest change in key indicators again this quarter is in the average initial market rent change rate. This quarter's 83-basis-point drop brings the rate to 4.67%, 175 basis points lower than one year ago. Rents in Class-A buildings downtown had soared in the past two years; they are estimated to be up as much as 40.0%. However, most major rent spikes have already occurred. This quarter only 33.3% of our participants say they are incorporating spikes into their analyses; this is down from 85.7% in third quarter 1998. The range of spikes is from 4.0% to 10.0%; the average is 8.5%.

Most investors remain very high on San Francisco. A few are shying away from this market because they believe that buildings are overpriced. ■

Table 17
San Francisco Office Market
FIRST QUARTER 1999

KEY INDICATORS	CURRENT QUARTER	LAST QUARTER	YEAR AGO
Discount Rate (IRR)[a]			
RANGE	9.25%–12.00%	9.25%–12.50%	10.00%–13.00%
AVERAGE	10.71%	10.83%	11.32%
CHANGE (Basis Points)	—	–12	–61
Overall Cap Rate (OAR)[a]			
RANGE	7.00%–11.00%	7.00%–11.00%	7.00%–11.00%
AVERAGE	8.42%	8.38%	8.82%
CHANGE (Basis Points)	—	+4	–40
Market Rent Change Rate[b]			
RANGE	0.00%–10.00%	0.00%–11.00%	0.00%–10.00%
AVERAGE	4.67%	5.50%	6.42%
CHANGE (Basis Points)	—	–83	–175
Expense Change Rate[b]			
RANGE	3.00%–4.00%	3.00%–4.00%	3.00%–4.00%
AVERAGE	3.50%	3.58%	3.50%
CHANGE (Basis Points)	—	–8	0
Residual Cap Rate			
RANGE	8.00%–10.00%	8.00%–10.00%	8.00%–10.00%
AVERAGE	8.88%	8.96%	8.86%
CHANGE (Basis Points)	—	–8	+2

a. Rate on unleveraged, all-cash transactions
b. Initial rate of change

Southeast Florida Office Market

"The lull *after* the storm" is how one participant characterizes the status of transaction activity in the Southeast Florida office market. Investors often take a bit of a breather at the start of the new year, but this year is extraordinarily quiet because of uncertainty about the direction of prices. "We don't know which way cap rates are going, what is a good sale price or a bad sale price," comments one investor. As a result, not so many would-be buyers are soliciting owners for their property. On the other side, owners are not putting product on the market because they hope that pricing will accelerate again. In an additional change from the recent past, buyers who do bid on properties are more careful and are spending more time doing due diligence.

A relatively small market, the Southeast Florida office market is spread over three counties—from the middle of Palm Beach County, through Broward County, to the end of Dade County. The major office markets are West Palm Beach, Boca Raton, Fort Lauderdale, and Miami. There is not a significant supply of institutional-grade properties outside of Miami. International business is centered in Dade County, but Broward County gets the spillover of Dade County, benefitting from the growth there. Palm Beach County is the weakest area because it has the least amount of commerce and the most available land.

Economic growth in Southeast Florida is fueled by distribution and transportation, tourism, and high-tech industries. Recently there has been a large influx of call centers. The importance of international trade, especially with Latin America, is a cause of concern because of the weakness of the Brazilian economy and the potential for it to spread across Latin America. Nearly half of Florida's exports are to Latin America.

For now, however, Miami and Dade County are strong, partly because the area is nearly fully built out. Its office markets are not overbuilt, and vacancy rates are single digit. The amount of new office construction in some other areas, however, will cause vacancies to rise this year. North Palm Beach and Boca Raton are both likely to see rates over 10.0% before year-end. Still, many developers who had planned to build are going forward.

Survey participants perceive that prices are 10.0% to 15.0% lower as a result of last year's price correction. Still, prices are close to replacement cost and exceed it for many buildings. The range is from 80.0% to 110.0% of replacement cost; the average is 94.6% of cost. Participants expect prices to rise over the next 12 months, but the rate of increase is modest, from 2.0% to 5.0%. The projected average increase is 3.3%.

Key value indicators are shown in Table 18. Uncertainty about near-term pricing could well be the reason for the lack of movement in cash flow forecast assumptions this quarter. Only the average discount rate (IRR) and the average initial market rent change rate shifted. The average IRR decreased 6 basis points, following a 20-basis-point decline last quarter. At 11.14%, the rate is now 24 basis points lower than one year ago.

The average overall cap rate (OAR) remains at 9.39% for the second consecutive quarter. The Southeast Florida office market average OAR is one of the highest of all surveyed office markets.

Although transaction activity will no doubt pick up in the coming months, the number of transactions could be down 25.0% to 30.0% from levels in recent years. Marketing periods will likely stretch from the days when "it was like putting property on a buffet, and hungry buyers would pick it off," as one participant recalls. ■

Table 18
Southeast Florida Office Market
FIRST QUARTER 1999

KEY INDICATORS	CURRENT QUARTER	LAST QUARTER	YEAR AGO
Discount Rate (IRR)[a]			
RANGE	10.00%–12.00%	10.00%–13.50%	10.00%–13.50%
AVERAGE	11.14%	11.20%	11.38%
CHANGE (Basis Points)	—	–6	–24
Overall Cap Rate (OAR)[a]			
RANGE	8.00%–12.00%	8.00%–12.00%	8.00%–12.00%
AVERAGE	9.39%	9.39%	9.46%
CHANGE (Basis Points)	—	0	–7
Market Rent Change Rate[b]			
RANGE	2.00%–7.00%	2.00%–7.00%	2.00%–7.00%
AVERAGE	3.63%	3.69%	4.21%
CHANGE (Basis Points)	—	–6	–58
Expense Change Rate[b]			
RANGE	2.00%–4.00%	2.00%–4.00%	3.00%–4.00%
AVERAGE	3.19%	3.19%	3.43%
CHANGE (Basis Points)	—	0	–24
Residual Cap Rate			
RANGE	9.00%–11.00%	9.00%–11.00%	9.00%–11.00%
AVERAGE	9.72%	9.72%	10.02%
CHANGE (Basis Points)	—	0	–30

a. Rate on unleveraged, all-cash transactions
b. Initial rate of change

Washington, DC Office Market

The Washington, DC office market is thriving and, consequently, is highly attractive to investors. Transaction activity in the new year has slowed from last year, when REITs, foreign investors, life insurance companies, pension funds, and local buyers were storming the market in hot pursuit of properties. The REITs are generally gone now, but the others are expected to heat up the market in the coming months, albeit at a more moderate pace.

Investors could hardly ask for stronger market conditions. While absorption dropped in 1998 from 1997 levels, vacancy rates continued to fall. The overall vacancy rate at year-end was 8.4%. Northern Virginia showed the lowest rate, 7.3%. District vacancy was 7.8%, and it was 11.7% in suburban Maryland. The tight space market has caused rents to rise to a level that supports new construction. The average asking rent in the District is $28.12 per square foot, with the Southwest and East End submarkets supporting the highest per-square-foot averages, $31.86 and $31.33, respectively. For absolute top-of-the-line District office space, rents are as high as $45.00 per square foot. In Northern Virginia, the average asking rent is $22.80 per square foot; it is $19.03 in the Maryland suburban market.

The District continues to suffer a severe shortage of Class-A space. Recent additions to the top-tier inventory have been renovated space, which has generally been preleased. In 1998, supply in the District increased by only 1.1%. The suburban increases were 2.9% in Northern Virginia and 1.4% in Maryland.

Prices for office properties soared early in 1998 but moderated in the wake of the dramatic halt of REIT acquisition activity and the collapse of CMBS market. Nevertheless, at year-end the average sale price in the District was approximately $210 per square foot, up more than 10.5% over the 1997 average. Several late-year purchases were above the per-square-foot average including 1800 M St. NW at $214 and 1155 Connecticut Ave. NW at $216.

Marketwide, prices are nearing replacement cost and exceed it for many buildings. Overall, prices range from 75.0% to 110.0% of replacement cost. The average price is 93.1% of replacement cost. Over the next 12 months, values are expected to increase as much as 10.0%; the average projected increase is 3.6%.

Key value indicators in the Washington, DC office market are show in Table 19. Changes this quarter reflect participants' reaction to last fall's price correction. The average discount rate (IRR) increased 19 basis points to 11.50%. The average overall cap rate (OAR) shot up 25 basis points to 9.13%.

The current DC average IRR is now among the highest of all surveyed markets, considerably higher than average IRRs in both the national CBD office market (11.28%) and national suburban office market (11.11%). The Washington, DC average OAR remains one of the lowest of all surveyed office markets. It compares with 8.82% in the national CBD office market and 9.17% in the national suburban office market.

Investors see upside potential in this office market. Government is a nearly recession-proof space user, but even better, the employment base has diversified in recent years. High-tech computing and communications technology, research, and development; trade, education, and tourism are important sectors of the economy. Northern Virginia boasts two of the largest Internet access providers, and nearly half of all international Internet traffic flows through these and other access providers located there. ■

Table 19
Washington, DC Office Market
FIRST QUARTER 1999

KEY INDICATORS	CURRENT QUARTER	LAST QUARTER	YEAR AGO
Discount Rate (IRR)[a]			
RANGE	10.00%–13.00%	10.00%–13.00%	10.00%–13.00%
AVERAGE	11.50%	11.31%	11.52%
CHANGE (Basis Points)	—	+19	–2
Overall Cap Rate (OAR)[a]			
RANGE	7.00%–11.00%	7.00%–11.00%	7.00%–11.00%
AVERAGE	9.13%	8.88%	8.88%
CHANGE (Basis Points)	—	+25	+25
Market Rent Change Rate[b]			
RANGE	0.00%–10.00%	0.00%–10.00%	0.00%–10.00%
AVERAGE	3.00%	2.98%	2.75%
CHANGE (Basis Points)	—	+2	–25
Expense Change Rate[b]			
RANGE	2.00%–4.00%	3.00%–4.00%	3.00%–4.00%
AVERAGE	3.30%	3.43%	3.71%
CHANGE (Basis Points)	—	–13	–41
Residual Cap Rate			
RANGE	8.00%–11.00%	8.00%–11.00%	8.00%–11.00%
AVERAGE	9.41%	9.33%	9.06%
CHANGE (Basis Points)	—	+8	+35

a. Rate on unleveraged, all-cash transactions

b. Initial rate of change

National Industrial Market

"We've tried to do some industrial deals, but without much success" is a common complaint among investors who have warehouse/distribution facilities high on their property-type target lists for this year. Prices are high and were hardly touched by the late-1998 correction. Deals on industrial R&D and flexible-use properties are easier to land due to the ample supply of relatively low-priced product. They offer significant upside potential but also carry higher risk.

Institutional investors like to balance their portfolios with institutional-grade warehouses because of the nearly constant balance between supply and demand. The balance may shift in the near-term, however. Although construction starts slowed in the second half of 1998, there were already a large number of projects in the pipeline which were near completion. The likelihood of adding a certain number of projects now in the planning stage brings the total of new supply that will hit the industrial market over the next 18 months up to 122 million square feet, according to Donaldson, Lufkin & Jenrette Equity Research. This represents a 3.0% increase to existing stock. DL&J forecasts that the national vacancy rate could rise by as much as 2.0%.

The markets that lead in potential excess of supply over demand include Atlanta, Fort Lauderdale, Nashville, Sacramento, Salt Lake City, and Seattle. The most promising markets, those where demand is greater than supply planned or under construction, include Houston, Phoenix, Richmond, and San Antonio.

Another potential threat to the industrial market is the prospect of further weakening in the global economy. Although areas that depend heavily on international trade have remained strong thus far, if the Brazilian economy deteriorates further and spreads across Latin America, U.S. exports could decline significantly. The states that are at greatest risk of being economically affected are Florida and Texas.

Prices in the national industrial market are relatively stable, albeit at high levels. Through the end of 1998, bulk warehouses held their values, experiencing downward correction of only about 5.0% on good quality product in good markets. Flex and R&D properties were hit harder, with prices dropping by an estimated 10.0%.

Institutional-grade warehouses remain above replacement cost, while lower-grade product is generally at replacement cost. R&D and flex properties are still generally below this marker. Across the market, prices range from 80.0% to 110.0% of replacement cost. The average is 98.0% of cost.

Key value indicators are shown in Table 20. The average discount rate (IRR) declined a negligible 1 basis point after standing at 11.15% for the three prior quarters. The average overall cap rate (OAR) increased 5 basis points to 9.14%.

The risk of ownership of R&D/flex properties is higher than in the warehouse segment. This is evident in comparing rates for R&D/flex space with those for warehouse/distribution facilities. The range of IRRs for warehouses is from 9.50% to 12.50%; the average is 11.02%. The range of OARs is from 8.00% to 10.50%; the average is 9.03%. For R&D/flex properties, the range of IRRs is from 8.00% to 14.00%; the average is 11.56%. The range of OARs is from 8.00% to 12.00%; the average is 9.80%.

The Midwest, especially Chicago, is often named as a preferred market, but participants say that current high prices make acquisitions difficult there. They also like California. Since that market recovered later than others, they believe there are still opportunities for some "pops." ■

Table 20
National Industrial Market
FIRST QUARTER 1999

KEY INDICATORS	CURRENT QUARTER	LAST QUARTER	YEAR AGO
Discount Rate (IRR)[a]			
RANGE	9.50%–12.50%	9.50%–12.50%	10.00%–12.50%
AVERAGE	11.14%	11.15%	11.25%
CHANGE (Basis Points)	—	–1	–11
Overall Cap Rate (OAR)[a]			
RANGE	8.00%–10.25%	8.00%–10.25%	8.00%–10.50%
AVERAGE	9.14%	9.09%	9.08%
CHANGE (Basis Points)	—	+5	+6
Market Rent Change Rate[b]			
RANGE	2.00%–6.00%	2.00%–6.00%	2.00%–6.00%
AVERAGE	3.39%	3.54%	3.65%
CHANGE (Basis Points)	—	–15	–26
Expense Change Rate[b]			
RANGE	1.50%–5.00%	1.50%–5.00%	3.00%–4.00%
AVERAGE	3.28%	3.43%	3.63%
CHANGE (Basis Points)	—	–5	–40
Residual Cap Rate			
RANGE	8.50%–11.00%	8.50%–11.50%	8.00%–11.00%
AVERAGE	9.52%	9.55%	9.50%
CHANGE (Basis Points)	—	–3	+2

a. Rate on unleveraged, all-cash transactions

b. Initial rate of change

National Apartment Market

The national apartment market "just keeps on keeping on." More than a year ago many analysts thought it had peaked, that it would soon be over the top and down the investment curve. Prices were high and there had been an abundance of new development, too much in many markets — all the signs of a market on the brink of a downturn. Prices are still high and there is more development, and the downturn has not happened. The apartment market continues to exhibit amazing endurance.

Despite the large number of new units added to inventory in recent years, absorption has generally been good, and the apartment market is close to equilibrium. There are pockets of concern, but overall nationwide demand is expected to exceed supply slightly over the next 18 months. In addition, some markets that had been perceived as overbuilt or on the verge of overbuilding are coming in line, according to Donaldson, Lufkin & Jenrette Equity Research. These markets include Atlanta, Austin, Charlotte, Las Vegas, Phoenix, and Raleigh-Durham.

Construction has slowed in recent months. According to some participants, this is due to REIT withdrawal from development activity. The squeeze on their capital and its higher cost have limited their participation. There is not a general credit crunch on apartment financing, however. Fannie Mae and Freddie Mac are offering low-cost capital, at rates reported to be as low as 6.25%.

In last year's real estate price correction, apartments were the least affected of all property types. There is less price volatility in the apartment market because of the dollar amount of deals, which are relatively smaller than those for, say, a regional mall or CBD office tower.

Some REITs are still in the apartment market — or back in it. They join the pension funds, private partnerships with access to Wall Street capital, syndicators, and investors with 1030 exchange money who picked up the slack late last year.

There is a wide spread in prices in the national apartment market. Participants say that, overall, prices range from 75.0% to 120.0% of replacement cost. The average price is 96.6% of cost. Projected increases over the next 12 months are not large; the range is from 0.0% to 6.0%, with an average increase of 2.4%.

Key value indicators in the national apartment market are shown in Table 21. Both the average discount rate (IRR) and the average overall cap rate (OAR) increased, which may signal that investors look for a moderation in prices. The average IRR is up 12 basis points to 11.48%. This follows a 10-basis-point hike last quarter. The average overall cap rate (OAR) increased 6 basis points to 8.83%.

Investors are particularly interested in acquiring urban apartments; they believe they offer outstanding investment potential. There is a surge in residential population in the downtowns that were formerly deserted after business hours. Los Angeles and Dallas are among the cities that are encouraging residential development as a catalyst for downtown revitalization. Downtown Manhattan is becoming a 24-hour market as a result of conversions of older office buildings to apartments. One neighborhood in lower Manhattan went from no households to 7,000 households in the past decade, according to one participant. "In New York, time is money for young Wall Street professionals and law associates who are trying to make partner," he says. "They don't really live in their 150-square-foot studios; those are places to put their cleaning and sleep, but they really live at work." ■

Table 21
National Apartment Market
FIRST QUARTER 1999

KEY INDICATORS	CURRENT QUARTER	LAST QUARTER	YEAR AGO
Discount Rate (IRR)[a]			
RANGE	10.00%–15.00%	10.00%–13.00%	10.00%–13.00%
AVERAGE	11.48%	11.36%	11.15%
CHANGE (Basis Points)	—	+12	+33
Overall Cap Rate (OAR)[a]			
RANGE	7.50%–11.00%	7.00%–11.00%	7.00%–11.00%
AVERAGE	8.83%	8.77%	8.88%
CHANGE (Basis Points)	—	+6	–5
Market Rent Change Rate[b]			
RANGE	0.00%–6.00%	0.00%–7.00%	0.00%–6.00%
AVERAGE	3.08%	3.29%	3.20%
CHANGE (Basis Points)	—	–21	–12
Expense Change Rate[b]			
RANGE	2.00%–5.00%	2.00%–5.00%	2.50%–5.00%
AVERAGE	3.16%	3.29%	3.49%
CHANGE (Basis Points)	—	–13	–33
Residual Cap Rate			
RANGE	8.00%–10.50%	8.00%–10.00%	8.00%–10.25%
AVERAGE	9.22%	9.20%	9.26%
CHANGE (Basis Points)	—	+2	–4

a. Rate on unleveraged, all-cash transactions

b. Initial rate of change

National Hotel Market Highlights

After years of significant growth, record-breaking construction starts and profits, and numerous mergers and acquisitions, the national hotel market is entering a period of slower growth and refocused strategies. However, "it is not the doom and gloom often written about," observes one participant. Other participants agree that the general state of the national hotel market remains good. "It's a good time to buy, but if you're a seller, you've missed the boat since REITs can no longer afford to pay top premiums."

REITs took a hard hit on Wall Street last year and are no longer the major hotel buyers. Their lower stock prices mean reduced access to capital. As a result, sale prices are "more realistic," creating more opportunities for private capital. "The fundamentals of a property drives the price, no matter what Wall Street does," comments one participant. Transactions are expected to increase in the months ahead; the major buyers are likely to be pension funds, insurance companies, and private companies.

The fight to become the biggest hotel company has been replaced with becoming the strongest. Increases in competition and decreased occupancy rates are causing hotel operators and owners to concentrate on new business strategies such as property growth, brand loyalty, and management. Frequent-guest programs and "100% Satisfaction Guaranteed" policies are becoming popular at hotels. In addition, several companies such as Meristar, Prime Hospitality, and Felcor have announced new management teams and executives.

INDUSTRY PERFORMANCE

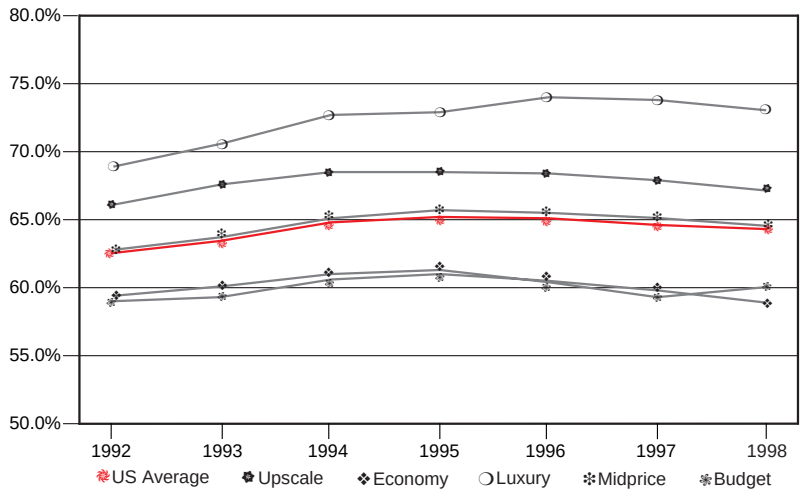
Room supply continues to outpace room demand. Total room supply grew 4.0% during 1998, while demand gained 3.1%, according to Smith Travel Research (STR). Although the room supply growth for 1998 is above the increase realized in 1997 (3.5%), demand in 1998 was much higher than demand in 1997 (2.4%).

Despite increases in demand, STR reports that occupancy levels slipped in most hotel market segments during 1998 (see Exhibit H-1). Overall occupancy declined 0.8%. Luxury hotels continue to maintain the highest occupancy levels at 72.9%. Budget hotels realized a slight gain in occupancy from 59.7% in 1997 to 60.0% in 1998.

Declines in occupancy are affecting even the largest hotel markets. Only six of the 25 largest markets experienced occupancy gains in 1998. The top three markets for occupancy growth were Denver, Norfolk-Virginia Beach, and Washington, DC. The market main-taining the highest overall occupancy level in 1998 was again New York City (77.6%).

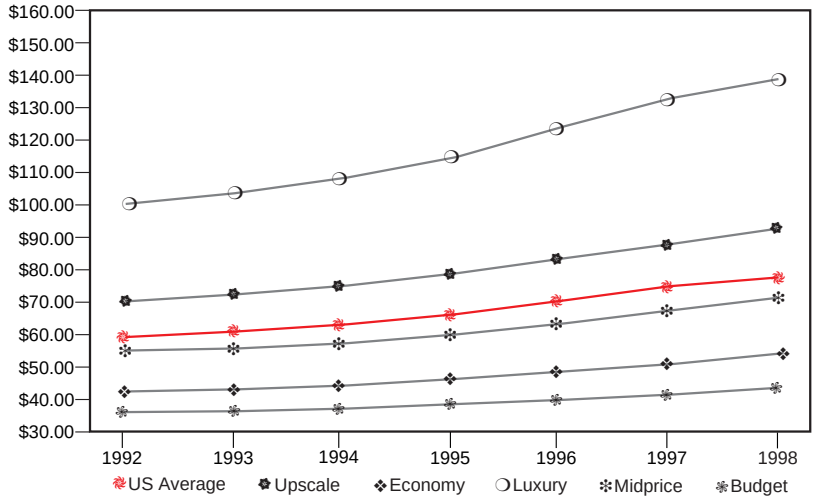
Of more concern to hotel investors than the decline in occupancy is the

Exhibit H-1
Occupancy Trends 1992-1998



Source: Smith Travel Research.

Exhibit H-2
Average Daily Room Rates 1992-1998



Source: Smith Travel Research.

slowdown in ADR growth. Although ADRs continue to increase in each hotel market segment (see Exhibit H-2), ADR growth in 1998 (4.40%) is well below that realized in 1997 (6.10%). This trend is expected to continue. "We are moving toward normal growth levels," comments one investor. The fear, however, is that a decline in ADRs combined with declines in occupancy will diminish profits.

REITS

Stock prices for hotel REITs declined an average of 56.0% last year amid fears of overbuilding. Although the fundamentals of the hotel industry remain relatively unchanged, REITs are "still trying to figure out where they are and what they've created," says one participant.

With stock values so low, many REITs are not able to raise sufficient funds to outbid other buyers and acquire any and every asset they want. As a result, sale prices are likely to decline, which will allow non-REIT hotel investors to become competitive again. This is welcomed by investors who seemed always to be outbid by REITs.

Nevertheless, REITs are certainly not completely out of the market. Furthermore, some of those that are not active now are thought to be out of the market only temporarily, taking a breather. More REITs will return eventually. This is a very important time period for hotel REITs, a time to refocus their strategies for long-term growth.

Some REITs will undoubtedly sell some properties, as Patriot American Hospitality did in the latter part of 1998, or consolidate. A few REITs will convert back to private companies or become C-Corps. This has already been shown by Starwood, which reverted to a C-Corp in early 1999 from paired-share REIT status. Other companies, such as Host Marriott Corp., converted to REIT status.

CONSTRUCTION

The recent shortage of capital has caused a slowdown in new development. In addition, the decline in occupancy and ADR growth rates has resulted in several hotel companies, including Sunburst Hospitality Corp., Extended Stay America, Inc., Prime Hospitality Corp., and Marriott International, to cancel or cut back on planned development.

Construction is forecast to decline 23.0% in 1999 and 35.00% in 2000, according to PricewaterhouseCoopers. These are sharper declines than the firm's earlier projections of 15.0% and 25.0%, respectively.

Participants are slightly more concerned about a downturn in the U.S. economy than about overbuilding. "The outlook for the industry is good if the economy remains stable," states one participant. "If the economy falters, demand and ADRs will decline dramatically and profits will plummet."

Although participants are projecting the pace of ADR growth to slow over the near term, they expect ADRs to continue to increase at above inflation. In addition, the recent slowdown in construction is expected to enable the industry to maintain adequate occupancy levels. As a result, shortfalls in profits, if any, should be minimal.

Lodging Research Network (LNR) projects 1998 hotel industry profits at $17.6 million. For 1999 and 2000, LNR is projecting profits of $19.2 million and $21.0 million, respectively.

MARKETING TIME

Marketing time remains relatively unchanged for full-service and economy/limited-service hotels since third quarter 1998 (see Table H-1). The greatest decrease in marketing time was realized in the luxury hotel market. This is not a surprise since luxury hotels continue to be a preferred property type for investors due to limited new construction, continued increases in ADRs, and high demand. The highest increase in marketing time is in the extended-stay market.

The average marketing time for all hotel segments is 6.50 months. This is 1.40% greater than the third quarter average. Since the Korpacz hotel market reports were first published in third quarter 1998, marketing time estimates from one year ago are not available. ■

Table H-1
Average Marketing Time (months)
FIRST QUARTER 1999

MARKET	CURRENT QUARTER	THIRD QUARTER	YEAR AGO
Full-Service Hotels	5.67	5.64	—
CHANGE	—	+0.53%	—
Economy/Limited-Service Hotels	6.38	6.38	—
CHANGE	—	0.00%	—
Luxury Hotels	6.55	6.83	—
CHANGE	—	–4.10%	—
Extended-Stay Hotels	7.39	6.79	—
CHANGE	—	+8.84%	—
All Markets Surveyed	6.50	6.41	—
(Simple Average)	—	+1.40%	—

National Full-Service Hotel Market

Full-service hotels attract the most investor interest of all market segments. Although the transaction market is fairly quiet now, activity is expected to increase as the capital markets regain confidence in the hotel industry. The better investments will be located in areas with diverse economies that can withstand economic shortfalls, such as Boston, Denver, New York, and Washington, DC.

Market conditions are strong and should remain healthy. Any decline will likely be minor, although growth rates will continue to moderate. Mergers and acquisitions will likely progress at a much slower pace than last year.

The greatest concerns in the full-service hotel market are employment costs and the ability to maintain sufficient workers. With many of the major markets in the United States experiencing unemployment rates below 5.0%, full-service hotel owners are finding it difficult to hire and keep good-quality personnel. Many hotel workers, even managers, view their employment as a job, not a career. In an attempt to minimize the labor problem, some hotel transactions include written stipulations regarding in-place management and workers. Other concerns include the availability of financing, the future role of capital markets, and a sudden negative shift in the economy.

Occupancy in full-service hotels declined in 1998 for the third consecutive year, according to Smith Travel Research (STR). The full-service hotel segment achieved 67.4% occupancy. The average daily rate (ADR) was $91.47. Although continuing to increase, ADR growth dropped dramatically to 3.65% from 5.13% in 1997. Participants expect occupancy and demand to continue the slight downward trend, while ADRs will increase at slower rates. RevPar (revenue per available room) is forecast to increase between 3.0% and 7.0% this year. There is concern, however, that a strong downturn in demand could cause ADR wars.

The overall breakeven occupancy for the national hotel industry is approximately 55.5%, according to Bear, Stearns & Co. and Pricewaterhouse-Coopers. The breakeven point is down significantly from 62.5% in 1992 due to above-average growth in ADRs and lower debt and equity costs. Of all the market segments, full-service hotels operate closest to their breakeven occupancy level of 63.0%.

The Northeast and West, especially California and Arizona, as well as major airport markets are frequently named as good full-service hotel locations. Convention markets such as San Francisco, New York, and Washington, DC are also considered favorable for full-service hotels. Participants are leery of some areas, including the Southeast, parts of Texas, Chicago, and Atlanta.

Key value indicators for the full-service hotel market are shown in Table 22.

This is the second quarter the hotel survey was done by The Korpacz Company, Inc. Therefore, comparisons with year-ago results are skewed due to a different participant base and different methodology. This quarter the average discount rate (IRR) increased 17 basis points. At 13.71%, it is higher than the luxury hotel market IRR. It remains well below average IRRs in the extended-stay and economy/limited-service markets; these are perceived as higher-risk property types. The average overall cap rate (OAR) jumped 46 basis points to 10.02%.

In third quarter 1998, 75.0% of participants believed that the full-service market was a sellers' market. The past six months have brought about a significant change. The percentage of participants who see the full-service market as a sellers' market declined to 59.0%. The remaining 41.0% think it is a buyers' market. ■

Table 22
National Full-Service Hotel Market
FIRST QUARTER 1999

KEY INDICATORS	CURRENT QUARTER	THIRD QUARTER 1998	YEAR AGO
Discount Rate (IRR)[a]			
RANGE	9.00%–16.00%	9.00%–16.00%	10.00%–25.00%
AVERAGE	13.17%	13.00%	14.04%
CHANGE (Basis Points)	—	+17	–87
Overall Cap Rate (OAR)[a]			
RANGE	8.00%–13.00%	8.00%–12.00%	6.00%–12.00%
AVERAGE	10.02%	9.56%	9.88%
CHANGE (Basis Points)	—	+46	+14
Average Daily Rate Chg.Rate[b]			
RANGE	2.00%–10.00%	2.00%–10.00%	3.00%–12.00%
AVERAGE	4.85%	4.88%	4.50%
CHANGE (Basis Points)	—	–3	+35
Operating Expense Chg. Rate[b]			
RANGE	1.00%–10.00%	1.00%–10.00%	2.50%–4.00%
AVERAGE	3.27%	3.31%	3.26%
CHANGE (Basis Points)	—	–4	+1
Residual Cap Rate			
RANGE	8.00%–12.00%	8.00%–12.00%	8.00%–12.00%
AVERAGE	10.54%	10.24%	10.30%
CHANGE (Basis Points)	—	+30	+24

a. Rate on unleveraged, all-cash transactions
b. Initial rate of change

National Economy/Limited-Service Hotel Market

The economy/limited-service hotel market is considered to have the greatest investment risk of all hotel segments. During the past years of robust development, supply outpaced demand significantly. The result is an overbuilt market with declining average daily rate (ADR) growth, slips in occupancy, and declines in sale prices.

The threat of additional new construction appears to be alleviated for now. The capital crunch on Wall Street has put a halt to the majority of economy/limited-service hotel construction. Some developers have completed the first phase of a project but are waiting before going on to phase two. Others have canceled proposed and planned development and are offering sites for sale. Participants expect the capital markets to open up slowly, but they do not believe that developers will be quick to return to a construction. "The hotel industry has learned a lesson," comments one participant. Investors need to work internally to become the strongest player in the market and not be concerned with being the biggest player.

Transaction activity is minimal. There is reluctance on behalf of both buyers and sellers. Investors in economy/limited-service hotels may need to rethink their inventory. Sunstone Hotel Investors, Inc., a hotel REIT, recently sold five of their limited-service hotels as part of a repositioning strategy to concentrate on luxury and upscale hotel investment. Other companies and REITs may soon follow.

There is a lack of available capital for new development. However, refinancing opportunities exist for some economy/limited-service hotels.

Occupancy in the economy/limited-service market declined from 61.3% in 1997 to 60.9% in 1998, according to Smith Travel Research (STR). The ADR increased slightly from $53.74 in 1997 to $56.31 in 1998. Participants are projecting a continued decline in ADR growth, occupancy, and RevPar. The overall breakeven occupancy for the national hotel industry is approximately 55.5%, according to Bear, Stearns & Co. and PricewaterhouseCoopers. Economy/limited-service hotels are operating only slightly above their breakeven occupancy level which is 58.5%. This contributes to the perception that investment in this segment is risky.

Favorable areas for economy/limited-service hotels include the Southeast, Northeast, Texas, Denver, and major middle-market cities with technology corridors. "But it's still a tough product in most markets," comments one participant.

Key value indicators for the economy/limited-service hotel market are shown in Table 23. This is the second quarter the hotel survey was done by The Korpacz Company, Inc. Therefore, comparisons with year-ago results are skewed due to a different participant base and different methodology. This quarter the average discount rate (IRR) jumped 43 basis points to 14.57%. It is now the highest average IRR of all the hotel segments. Although the average overall cap rate (OAR) remained at 11.34% for the second consecutive quarter, it is also the highest average OAR of all the hotel segments.

Despite the slowdown in construction, it will take some time before equilibrium between the demand and the oversupply created in the recent construction boom is reached. Demand is not expected to increase significantly over the near term. If the national economy remains stable, minimal supply increases should prevent further deterioration of occupancy levels. Fundamentals within the economy/limited-service hotel segment will slowly improve, providing more attractive financial rewards for investors. ■

Table 23
National Economy/Limited-Service Hotel Market
FIRST QUARTER 1999

KEY INDICATORS	CURRENT QUARTER	THIRD QUARTER 1998	YEAR AGO
Discount Rate (IRR)[a]			
RANGE	10.00%–18.00%	10.00%–16.00%	11.00%–15.00%
AVERAGE	14.57%	14.14%	13.36%
CHANGE (Basis Points)	—	+43	+121
Overall Cap Rate (OAR)[a]			
RANGE	10.00%–12.00%	10.00%–12.00%	9.00%–14.00%
AVERAGE	11.34%	11.34%	11.44%
CHANGE (Basis Points)	—	0	–10
Average Daily Rate Chg.Rate[b]			
RANGE	2.00%–10.00%	2.00%–10.00%	3.00%–12.00%
AVERAGE	3.44%	3.44%	4.10%
CHANGE (Basis Points)	—	0	–66
Operating Expense Chg. Rate[b]			
RANGE	2.00%–4.00%	2.00%–4.00%	2.50%–4.00%
AVERAGE	3.11%	3.11%	3.19%
CHANGE (Basis Points)	—	0	–8
Residual Cap Rate			
RANGE	10.50%–12.50%	10.00%–12.50%	8.00%–13.00%
AVERAGE	11.72%	11.59%	10.92%
CHANGE (Basis Points)	—	+13	+80

a. Rate on unleveraged, all-cash transactions

b. Initial rate of change

National Luxury Hotel Market

Robust demand and lack of new supply are the primary reasons the luxury hotel market is the strongest segment in the hotel industry. With limited new construction in the pipe-line, luxury hotel investors expect to continue to benefit from lucrative operating leverages. Strong returns are attractive to developers. However, lack of capital and available sites in strong markets as well as the length of time for construction will likely limit additional supply.

Transactions are minimal because it is hard to find willing sellers. Most transactions are for single properties, although there have been some portfolio sales. Host Marriott acquired the Ritz-Carlton in San Francisco and the Ritz-Carlton in Dearborn, Michigan for reported purchase prices of $479,167 and $211,039 per room, respectively. Meristar Hospitality purchased the Forrestal Hotel in Princeton, New Jersey for $240,550 per room. The Westin River North in Chicago was sold for $215,000 per room to Lend Lease Real Estate Investments Inc. Participants expect transaction activity to increase.

As in the full-service market, luxury hotel participants are also concerned about staffing. Low unemployment rates make it increasingly more difficult to attract and keep sufficient personnel.

According to Smith Travel Research (STR), occupancy in the luxury hotel market was 72.9% in 1998. Occupancy in this segment has declined annually since 1995. The average daily rate (ADR) in 1998 was $139. As is the case in the other hotel segments, luxury ADR growth rates continue to decline. However, luxury ADRs appear to be the hardest hit, declining 8.30% in 1996, 6.86% in 1997, and 4.34% in 1998.

Luxury properties have upside potential and record profits are likely to continue, especially in the top metropolitan markets. Participants are keeping a watchful eye on the economy. An economic downturn would likely result in less business and vacation travel. This would negatively affect luxury hotels and especially resort hotels. If the economy remains stable, participants expect to see a pattern similar to that realized in 1998 — slight declines in occupancy and ADR growth rates. RevPar (revenue per available room) is forecast to increase between 3.0% and 7.0%.

Key value indicators for the luxury hotel market are shown in Table 24. This is the second quarter the hotel survey was done by The Korpacz Company, Inc. Therefore, comparisons with year-ago results are skewed due to a different participant base and different methodology. At 12.81%, the average discount rate (IRR) remains the lowest of all hotel market segments. The IRR spread between the luxury and full-service segments increased 11 basis points, suggesting that investments in luxury products are perceived as more favorable. The overall cap rate (OAR) and residual cap rate are also the lowest.

The overall breakeven occupancy for the national hotel industry is approximately 55.5%, according to Bear, Stearns & Co. and Pricewaterhouse-Coopers. Luxury hotels are operating slightly above their breakeven occupancy level of 60.0%. This is well above the economy/limited-service and extended-stay markets, which report breakeven occupancy rates of 41.0% and 49.0%, respectively.

Favorable locations for luxury hotel investment include tourist destinations such as New York, San Diego, San Francisco, Seattle, and Washington, DC. These cities are also popular for conventions and business travel. Other regions of interest are the West Coast, Northeast, and Southwest. Some investors are shying away from Miami because of overbuilding there. ■

Table 24
National Luxury Hotel Market
FIRST QUARTER 1999

KEY INDICATORS	CURRENT QUARTER	THIRD QUARTER 1998	YEAR AGO
Discount Rate (IRR)[a]			
RANGE	9.00%–16.00%	9.00%–16.00%	10.00%–25.00%
AVERAGE	12.81%	12.75%	14.20%
CHANGE (Basis Points)	—	+6	–139
Overall Cap Rate (OAR)[a]			
RANGE	6.00%–12.25%	6.00%–12.25%	6.00%–11.50%
AVERAGE	9.25%	9.19%	9.03%
CHANGE (Basis Points)	—	+6	+22
Average Daily Rate Chg.Rate[b]			
RANGE	3.00%–10.00%	3.00%–12.00%	3.00%–10.00%
AVERAGE	5.23%	5.73%	4.58%
CHANGE (Basis Points)	—	–50	+65
Operating Expense Chg. Rate[b]			
RANGE	1.00%–5.00%	1.00%–5.00%	3.00%–4.00%
AVERAGE	3.17%	3.29%	3.28%
CHANGE (Basis Points)	—	–12	–11
Residual Cap Rate			
RANGE	7.00%–11.50%	7.00%–11.50%	8.00%–12.00%
AVERAGE	9.86%	9.56%	9.86%
CHANGE (Basis Points)	—	+30	0

a. Rate on unleveraged, all-cash transactions

b. Initial rate of change

National Extended-Stay Hotel Market

The recent slowdown in construction is good news for the extended-stay hotel market. "We are over the top with only one place left to go and that's down," comments one investor. Most participants view the low end of the market segment as overbuilt, while the upper end of the market segment ($100 and above average daily rate) is healthy.

Construction in this segment has been spurred by financing that is more readily available for this product than for full-service or luxury hotels. Investors like extended stay hotels because of the low labor requirements.

The first properties built in the extended-stay market achieved ADRs below the average of full-service hotels. However, they were top-tier extended-stay hotels. Currently, the newest niche for hotel investors and developers, such as Marriott International, Inc., is the mid-priced, extended-stay product. Average daily rates (ADRs) range from $45 to $60. With no proven track record, only time will tell if this new product is successful.

Extended-stay properties continue to have higher profit margins than traditional hotels. The overall breakeven occupancy for the national hotel industry is approximately 55.5%, according to Bear, Stearns & Co. and PricewaterhouseCoopers. The national level is down significantly from 62.5% in 1992 due to above-average growth in ADRs and lower debt and equity costs. Extended-stay hotels are operating well above their breakeven occupancy level of 49.0%. As a result, extended-stay hotels are better able to withstand economic adversity.

Once built to compete with transient hotels, extended-stay products have taken on a life of their own, offering a variety of price-points and unique amenities, including dual phone lines, fax machines, large workstations and living areas, and kitchenettes. Over the past few years, supply growth has outpaced demand growth, causing occupancy and ADRs to slip. If profits began to suffer and decline to a point that extended-stay properties start to revert to transient hotels, the underlying dynamics that make the extended-stay market attractive to investors would change dramatically. The entire hotel industry would likely be negatively affected.

Key value indicators for the extended-stay hotel market are shown in Table 25. The extended-stay hotel market was first reported in the third quarter 1998 issue. Therefore, indicators from one year ago are not available. The average discount rate (IRR) increased 39 basis points over third quarter 1998. At 14.43%, it is the second highest of all hotel market segments, reflecting concern about overbuilding and risk in the market. By comparison, the full-service hotel average IRR is 13.17%. It is 14.57% in the economy/limited-service segment and 12.81% in the luxury segment.

The average overall cap rate (OAR) decreased 23 basis points to 10.59%. It is higher than the average OAR in the full-service and luxury hotel segments but considerably lower than that in the economy/limited-service segment.

Participants note Texas, Colorado, Utah, and Florida as preferred states for upscale extended-stay products. Other desirable areas include Denver, Northern California, Pacific Northwest, and Northeast. In addition, major metropolitan areas are becoming increasing popular. However, barriers to entry such as land availability, timing, and cost make development difficult.

The extended-stay hotel market is still new, and there is limited data about which segments within the market are most efficient and in demand. Despite uncertainties, hotel companies are forging ahead with cautious optimism hoping to beat the competition. ■

Table 25
National Extended-Stay Hotel Market
FIRST QUARTER 1999

KEY INDICATORS	CURRENT QUARTER	THIRD QUARTER 1998	YEAR AGO
Discount Rate (IRR)[a]			
RANGE	12.00%–16.50%	12.00%–16.50%	
AVERAGE	14.43%	14.04%	
CHANGE (Basis Points)	—	+39	+68
Overall Cap Rate (OAR)[a]			
RANGE	9.00%–12.00%	10.00%–12.00%	
AVERAGE	10.59%	10.82%	
CHANGE (Basis Points)	—	–23	
Average Daily Rate Chg.Rate[b]			
RANGE	3.00%–10.00%	2.50%–10.00%	
AVERAGE	4.31%	4.00%	
CHANGE (Basis Points)	—	+31	
Operating Expense Chg. Rate[b]			
RANGE	2.00%–5.00%	2.00%–5.00%	
AVERAGE	3.16%	3.18%	
CHANGE (Basis Points)	—	–2	
Residual Cap Rate			
RANGE	10.00%–12.50%	9.50%–12.50%	
AVERAGE	10.97%	10.82%	
CHANGE (Basis Points)	—	+15	

a. Rate on unleveraged, all-cash transactions

b. Initial rate of change

National Regional Mall Market

INVESTOR SURVEY RESPONSES*

FIRST QUARTER 1999

*Representative sample; due to space constraints, not all responses are included.

Source: Personal survey conducted by The Korpacz Company, Inc. during January 1999.

	CHANGE RATES			RESIDUAL		DISCOUNT RATE (IRR)	OVERALL CAP RATE (OAR)	VACANCY ASSUMPTIONS			RESERVE	MARKETING TIME
	Market Rent	Expenses	CPI	Cap Rate	Selling Expense	Free & Clear	Free & Clear	Months Vacant	Tenant Retention	Underlying Vacancy & Credit Loss	Per Square Foot	Months
INVESTMENT ADVISOR ■ Forecast Period: 10 to 15 years Interested in dominant Class-A malls with strong anchored lineups and above-average trade area demographics; major emphasis on DCF but also looks at direct capitalization and price per square foot; uses face rents and reflects concessions as they occur.	Years 1-4 varies per market; 3.0% thereafter	3.0%	3.0%	7.50% to 10.00%	1.0% to 2.0%	10.00% to 12.00%	7.00% to 10.00%	9 to 12	60.0% to 75.0%	5.0% to 7.0% (nonanchor)	$0.15 to $0.25	6 to 12
INVESTMENT BANKER ■ Forecast Period: 10 years Relies on DCF (IRR) and direct capitalization (initial cap rates); does extensive sensitivity analysis on residual cap rates, growth rates, and initial market rents; retail sales based on historical and market analysis; typical sales growth per market per year is at the inflation rate (CPI); analysis of TIs is an important cash flow forecast item; believes market for malls is improving.	2.0% to 4.0%; varies per market	3.0%	3.0%	7.75% to 8.75% (Best); 8.75% to 10.25% (Most)	1.5%	10.00% to 11.00% (Best); 11.00% to 12.50% (Most)	7.00% to 8.50% (Best); 8.50% to 10.50% (Most)	3 to 4	70.0% to 75.0%	2.0% to 5.0%	Varies by mall	6 to 9
DOMESTIC PENSION FUND ■ Forecast Period: 10 to 12 years Buys free and clear; average IRR consists of a 6.5% to 7.0% real rate of return plus the inflation rate; the indicated growth scenarios help to determine sensitivity of investment to inflation; relies on DCF (IRR) and overall cap rates equally; uses face rents and reflects concessions when they are scheduled to occur.	Years 1-3 varies per market; thereafter at inflationary rate	2.0%/ 4.0%/ 6.0%	2.0%/ 4.0%/ 6.0%	7.50% to 8.00%	1.0%	10.50% to 11.00%	7.00% to 8.00%	3 to 4	70.0% to 75.0%	1.0% to 3.0%	$0.15	3 to 4
DOMESTIC PENSION FUND ■ Forecast Period: 10 years Looks at DCF (IRR), direct capitalization (initial cap rates), and price per square foot; uses face rents and reflects concessions when they are scheduled to occur.	3.0% to 4.0%	3.0%	3.0%	9.00% to 10.50%	2.0%	11.50% to 12.50%	9.50%	6	50.0%	5.0%	$0.25	9 to 18
REIT ■ Forecast Period: 5 years Uses both DCF and direct capitalization; in direct cap, capitalizes NOI after capital replacement reserve; applies rollover vacancy of 1.5%; replacement reserve is dollar amount.	4.0%	3.0%	3.0%	8.00%	2.0%	12.00%	8.00%	2	75.0%	0.0%	—	3
REAL ESTATE ADVISOR ■ Forecast Period: 10 to 15 years Retail sales are based on historical and market analysis; typical sales growth initially flat, then increasing 3.0% to 5.0% per year in typical markets; relies on DCF (IRR), direct capitalization (initial cap rates), and price per square foot; strives for realistic cash flow forecast; relationship of price to retail sales (1.0 to 1.5 times sales) is carefully analyzed; uses face rents.	2.0% to 3.0% initially; varies thereafter	3.5%	3.0% to 4.0%	8.00% to 9.00%	1.0% to 2.0%	10.50% to 12.00%	8.00% to 9.00%	4 to 6	60.0% to 70.0%	2.0% to 5.0%	$0.25 to $0.75	9
INVESTMENT ADVISOR ■ Forecast Period: 10 years Retail sales growth is based on historical performance and market analysis; very strong evidence is required to exceed 5.0% per year; spreads between A and B properties getting wider; prefers free and clear properties; uses all valuation techniques and correlates; does not rely on any one technique; looks for sale price to be 100% to 125% of sales volume; looks at components of NOI growth; uses face rents.	0.0% to 4.0%	3.5%	3.5%	7.50% to 9.00%	1.5%	10.00% to 11.00%	7.00% to 9.00%	2	60.0%	3.0% to 10.0%	$0.10	6 to 10

Korpacz

National Power Center Market

INVESTOR SURVEY RESPONSES*

FIRST QUARTER 1999

*Representative sample; due to space constraints, not all responses are included.

Source: Personal survey conducted by The Korpacz Company, Inc. during January 1999.

	CHANGE RATES			RESIDUAL		DISCOUNT RATE (IRR)	OVERALL CAP RATE (OAR)	VACANCY ASSUMPTIONS			RESERVE	MARKETING TIME
	Market Rent	Expenses	CPI	Cap Rate	Selling Expense	Free & Clear	Free & Clear	Months Vacant	Tenant Retention	Underlying Vacancy & Credit Loss	Per Square Foot	Months
REAL ESTATE ADVISOR ■ Forecast Period: 10 years Uses both DCF and direct capitalization; initial growth rates typically are between 0.0% and 3.5%; preference for infill locations with minimum land available and high barriers to entry; seeks very strong leases with "going dark" protection; 80.0%+ of overall return component should be generated by current income.	0.0% to 3.5%	3.5%	—	9.50%	2.0% to 2.5%	10.50% to 11.50%	10.00%	6 to 9 (nonanchors); 9 to 12 (anchors)	40.0% to 60.0%	0.0% to 3.0% (anchors); 6.0% (nonanchors)	$0.10 to $0.15	6 to 12
INVESTMENT BANKER ■ Forecast Period: 10 years Considers power center investments "coupon clipper" deals; uses both DCF and direct capitalization; focuses on West Coast; prefers urban areas with easy access and good anchor tenancy; credit is key; IRR is 10.25% to 11.50% on centers with good credit tenants.	4.0%	3.0% to 4.0%	4.0%	9.00% to 10.00%	2.0%	10.25% to 12.00%	8.00% to 10.00%	3 to 6	65.0% to 75.0%	5.0% to 10.0%	$0.10	6
INSTITUTIONAL INVESTOR ■ Forecast Period: 10 years Primarily interested in high-credit deals; uses both DCF and direct capitalization but focuses on IRR; develops IRR using tenants' bond rate plus 100 to 400 basis points for real estate related risks; lower IRRs are for high-credit deals with "bond" leases; uses present value analysis of effective rents.	2.0% to 3.5%; varies thereafter	2.0% to 3.5%	2.0% to 3.5%	9.50% to 10.00%	2.0% to 2.5%	10.50% to 11.25%	9.25% to 10.00%	3 to 6	50.0% to 60.0%	1.0% to 2.0% (anchors); 4.0% to 6.0% (nonanchors)	$0.15 to $0.25	6 to 9
INVESTMENT ADVISOR ■ Forecast Period: 10 years Uses both DCF and direct capitalization; credit of tenants is major determinant of rate; consolidations among anchors will cause continuing fallout vacancies; sees a smaller pool of investors for power centers than for regional malls.	0.0% to 4.0%	3.5%	3.5%	10.00% to 10.50%	1.5%	11.00% to 12.00%	9.75% to 10.50%	2 to 6	60.0%	5.0% to 10.0%	$0.10	6 to 12
INVESTMENT ADVISOR ■ Forecast Period: 5 to 10 years Uses both DCF and direct capitalization; applies OAR to NOI after capital replacement reserve deduction but before TIs and leasing commissions; views as credit deal; some growth assumed in cap rate; focuses on acquisitions in Florida.	3.0% to 4.0%	3.0% to 4.0%	3.0% to 4.0%	9.50% to 10.50%	2.0%	11.00% to 12.50%	9.00% to 10.00%	4 to 8	70.0% to 80.0%	3.0% to 5.0%	$0.15 to $0.25	4 to 8
INVESTOR-DEVELOPER ■ Forecast Period: 11 years Uses both DCF and direct capitalization; in direct cap, capitalizes cash flow after TIs, leasing commissions, and capital replacement reserve; in analyzing power centers with greater percentage of in-line space compared with big-box space, would likely apply a lower overall cap rate due to potential for increased income.	3.0%	3.0%	3.0%	10.00%	2.0%	12.00%	10.50%	3	66.0%	Actual; 5.0% noncredit tenants	$0.10 to $0.25	6 to 9

National Strip Shopping Center Market

INVESTOR SURVEY RESPONSES*

FIRST QUARTER 1999

*Representative sample; due to space constraints, not all responses are included.

Source: Personal survey conducted by The Korpacz Company, Inc. during January 1999.

	CHANGE RATES			RESIDUAL		DISCOUNT RATE (IRR)	OVERALL CAP RATE (OAR)	VACANCY ASSUMPTIONS			RESERVE	MARKETING TIME
	Market Rent	Expenses	CPI	Cap Rate	Selling Expense	Free & Clear	Free & Clear	Months Vacant	Tenant Retention	Underlying Vacancy & Credit Loss	Per Square Foot	Months
INVESTMENT ADVISOR ■ Forecast Period: 10 to 12 years Concerned about stability of anchor tenants; seeks centers with strong national anchors, low in-line tenant area components, and strong trade market area demographics; major emphasis on DCF, but also looks at direct capitalization and price per square foot; uses face rents.	Years 1-4 varies per market; 3.0% thereafter	3.0%	3.0%	9.50% to 12.00%	2.0% to 3.0%	11.00% to 13.00%	8.75% to 11.50%	6 to 12	50.0% to 70.0%	5.0% to 10.0% (nonanchor)	$0.15 to $0.25	6 to 12
INVESTMENT BANKER ■ Forecast Period: 10 years Does extensive sensitivity analysis on residual cap rates, growth rates, and initial market rents; retail sales based on historical and market analysis; initial cash return is more important than the IRR; TIs are an important cash flow forecast item.	Years 1–3 varies per market; 3.5% thereafter	3.0%	3.0%	8.75% to 11.00%	2.0%	10.50% to 14.00%	8.25% to 11.00%	4 to 8	60.0%	5.0% to 10.0% (noncredit tenants)	$0.15	4 to 12
DOMESTIC PENSION FUND ■ Forecast Period: 10 to 12 years Buys free and clear; average IRR consists of a 6.75% to 7.50% real rate of return plus the inflation rate; the indicated growth scenarios help to determine sensitivity of investment to inflation; relies on DCF (IRR) and overall cap rates equally; uses face rents and reflects concessions when they are scheduled to occur.	Years 1-3 varies per market; thereafter at inflationary rate	2.0%/ 4.0%/ 6.0%	2.0%/ 4.0%/ 6.0%	9.00% to 9.75%	2.0%	10.75% to 11.50%	8.75% to 9.75%	4 to 6	60.0% to 70.0%	5.0% (noncredit tenants)	$0.10 to $0.20	4 to 6
REAL ESTATE ADVISOR ■ Forecast Period: 10 years Relies on DCF, also uses direct capitalization and price per square foot; residual cap rate may be developed through a second 10-year DCF analysis (years 11 to 20).	2.5% to 3.0%	2.5% to 3.0%	2.75% to 3.0%	9.50% to 11.00%	3.0%	10.00% to 12.00%	9.25% to 10.50%	6	50.0% to 70.0%	7.5% (nonanchor)	$0.10 to $0.20	—
REAL ESTATE ADVISOR ■ Forecast Period: 10 to 15 years Retail sales are based on historical and market analysis; typical sales growth is initially flat, then increasing 3.0% to 5.0% per year in typical markets and 7.0% per year in strong markets; relies on DCF (IRR), direct capitalization (initial cap rates), and price per square foot; strives for realistic cash flow forecast, especially in market rent growth rate, retail sales growth rate, and credit loss; greater distinction is being made between A and B centers; great concern over stability of anchors; uses face rents.	0.0% to 3.0% initially; varies thereafter	3.5%	3.0% to 4.0%	10.00% to 12.00%	2.0% to 4.0%	11.00% to 12.50%	9.50% to 10.50%	6 to 8	50.0% to 60.0%	3.0% to 5.0%	$0.50	9
INVESTMENT ADVISOR ■ Forecast Period: 10 years Dominant grocer and other anchors are a must; infill locations with true supply constraints are important.	0.0% to 4.0%	3.5%	3.5%	9.25% to 10.50%	1.5%	11.00% to 13.00%	9.00% to 10.00%	2 to 4	50.0%	5.0% to 10.0%	$0.10 to $0.20	6 to 9
INSTITUTIONAL INVESTOR ■ Forecast Period: 10 years Invests primarily in 200,000- to 500,000-square-foot well-anchored community centers and good credit quality anchored power centers; relies on DCF; market rent growth rates vary according to supply-demand balance in specific market; applies rent spikes as warranted by market conditions and specific property; uses effective rents.	Varies per market until stabilized; thereafter at inflation rate	2.0% to 3.5%	2.0% to 3.5%	9.50% to 10.00%	2.0% to 3.0%	11.00% to 11.50%	9.50% to 10.50%	4 to 6	50.0% to 60.0%	1.0% to 3.0%	$0.10 to $0.20	6 to 9
INSTITUTIONAL INVESTOR ■ Forecast Period: 10 years Buys free and clear; interested in higher quality community centers; relies on DCF (IRR); uses direct capitalization as a check only; may apply rent spike if appropriate based on analysis of leases in place; uses face rents in model that allocates actual concessions when they are scheduled to occur; currently in reduction phase.	3.0%	3.5% to 4.0%	3.0%	9.75% to 10.25%	3.0% + any local tariffs	11.25% to 11.75%	9.75%	4 to 6	70.0%	6.0% to 8.0%	$0.10 to $0.20	6
MORTGAGE BANKER ■ Forecast Period: 10 years Relies on direct capitalization, shifting away from DCF; in DCF focuses on first 5 years of 10-year forecast period; uses face rents.	3.0%	3.0%	4.0%	9.50%	3.0%	11.00% to 13.00%	10.00%	3 to 8	70.0%	5.0%	$0.20 to $0.25	6

Korpacz

National CBD Office Market

INVESTOR SURVEY RESPONSES*

FIRST QUARTER 1999

*Representative sample; due to space constraints, not all responses are included.

Source: Personal survey conducted by The Korpacz Company, Inc. during January 1999.

	CHANGE RATES			RESIDUAL		DISCOUNT RATE (IRR)	OVERALL CAP RATE (OAR)	VACANCY ASSUMPTIONS			RESERVE	MARKETING TIME
	Market Rent	Expenses	CPI	Cap Rate	Selling Expense	Free & Clear	Free & Clear	Months Vacant	Tenant Retention	Underlying Vacancy & Credit Loss	Per Square Foot	Months
INVESTMENT ADVISOR ■ Forecast Period: 10 to 15 years Prefers free and clear properties; uses rent spikes if appropriate based on demand and relationship of current rents to rents required to justify new construction; relies on DCF (IRR), direct capitalization (initial cap rates), and price per square foot; uses face rents and reflects concessions when they are scheduled to occur.	Years 1–5 varies per market; 3.0% thereafter	3.0%	3.0%	8.50% to 10.00%	1.0% to 3.0%	10.25% to 12.00%	7.50% to 10.00%	6 to 12	50.0% to 75.0%	2.0% to 3.0%	$0.15 to $0.25	6 to 12
INVESTMENT BANKER ■ Forecast Period: 10 years Real cash on cash (after capital expenditures) more important than IRR; real interest in newer CBD buildings at 8.0% to 10.0% cash-on-cash rates; investor interest is increasing, more deals are coming to market, and prices are rising as capital seeks these deals.	3.0% to 5.0%	3.0%	3.0%	8.50% to 10.50%	2.0%	10.00% to 13.00%	7.50% to 10.00%	3 to 9	60.0% to 70.0%	3.0% to 5.0%	Varies	6 to 9
DOMESTIC PENSION FUND ■ Forecast Period: 10 to 12 years Buys free and clear; average IRR consists of a 6.0% to 7.0% real rate of return plus the inflation rate; the indicated growth scenarios help to determine sensitivity of investment to inflation; relies on DCF (IRR) and overall cap rates equally; use of face or effective rents varies with market.	Years 1-3 varies per market; at inflationary rate thereafter	2.0%/ 4.0%/ 6.0%	2.0%/ 4.0%/ 6.0%	8.75% to 9.25%	2.0%	10.50% to 11.50%	8.50% to 9.25%	6 to 9	60.0% to 70.0%	2.0% to 5.0%	$0.10 to $0.15	9 to 12
INVESTMENT ADVISOR ■ Forecast Period: 5 to 10 years Seeks a discount to replacement cost in recovering markets; uses face rents; in certain markets may apply rent spike in first three years.	0.0% to 7.0%	3.5%	3.5%	9.00% to 10.00%	1.0% to 3.0%	10.75% to 12.50%	7.50% to 9.00%	6 to 12	50.0% to 75.0%	3.0% to 7.0%	$0.20 to $0.40	6
REAL ESTATE ADVISOR ■ Forecast Period: 10 to 15 years Relies on DCF (IRR), direct capitalization (initial cap rates), and price per square foot; uses face rents and reflects free rent and other concessions when they are scheduled to occur; placing additional emphasis on average cash-on-cash rates for years 1 to 5, 6 to 10, and then the average rate for 1 to 10, coupled with partitioning present values and placing greater weight on cash flow vs. residual; continuing caution.	0.0% to 5.0%	3.0% to 4.0%	3.0% to 4.0%	9.00% to 10.00%	2.0% to 4.0%	10.50% to 13.00%	8.50% to 10.00%	6 to 9	60.0% to 70.0%	3.0% to 5.0%	$0.20 to $0.50	12 to 18
INVESTMENT ADVISOR ■ Forecast Period: 10 years Prefers free and clear proprieties with joint venture partner and preferred return; uses all valuation techniques and correlates; does not rely on any one technique; looks at components of NOI growth; uses face rents.	0.0% to 8.0%	3.5%	3.5%	9.00% to 10.00%	1.5%	11.00% to 15.00%	8.00% to 11.00%	4 to 8	60.0%	5.0% to 10.0%	$0.20	6 to 12
DOMESTIC PENSION FUND ■ Forecast Period: 10 years Relies on DCF (IRR), direct capitalization (initial cap rates), and price per square foot; uses face rents.	3.0% to 4.0%	3.0%	3.0%	8.75% to 10.00%	2.0%	11.00% to 12.00%	8.50% to 10.00%	6 to 8	60.0%	5.0%	$0.15	6 to 12
DOMESTIC PENSION FUND ■ Forecast Period: 10 years Uses both DCF and direct capitalization; in direct cap, capitalizes NOI before TIs, leasing commissions, and capital replacement reserve; uses face rents and reflects concessions when they are scheduled to occur.	3.0% to 3.5%	3.0% to 3.5%	3.5%	8.00% to 9.50%	—	10.00% to 12.00%	7.50% to 9.50%	6 to 12	60.0% to 70.0%	1.0% to 3.0%	$0.10 to $0.25	6 to 12
LIFE INSURANCE COMPANY ■ Forecast Period: 10 years Uses both DCF and direct capitalization; in direct cap, capitalizes NOI before TIs, leasing commissions, and capital replacement reserve; applies a 4.0% to 8.0% rent spike in years 1 to 3 in select markets.	3.0% to 8.0%	2.0% to 3.0%	3.0%	9.00% to 11.00%	1.0% to 4.0%	10.00% to 12.00%	8.00% to 10.00%	3 to 12	50.0% to 70.0%	3.0% to 6.0%	$0.20 to $0.40	3 to 12

National Suburban Office Market

INVESTOR SURVEY RESPONSES*

FIRST QUARTER 1999

*Representative sample; due to space constraints, not all responses are included.

Source: Personal survey conducted by The Korpacz Company, Inc. during January 1999.

	CHANGE RATES			RESIDUAL		DISCOUNT RATE (IRR)	OVERALL CAP RATE (OAR)	VACANCY ASSUMPTIONS			RESERVE	MARKETING TIME
	Market Rent	Expenses	CPI	Cap Rate	Selling Expense	Free & Clear	Free & Clear	Months Vacant	Tenant Retention	Underlying Vacancy & Credit Loss	Per Square Foot	Months
INVESTMENT ADVISOR ■ Forecast Period: 10 to 15 years Prefers free and clear properties; relies on DCF (IRR), direct capitalization (initial cap rates), and price per square foot; total vacancy and credit loss including rollover vacancy is 5.0% to 10.0%; reflects actual rents and concessions.	Years 1-5 varies per market; 3.0% thereafter	3.0%	3.0%	8.50% to 10.00%	2.0% to 4.0%	10.25% to 12.00%	8.00% to 10.00%	6 to 12	50.0% to 75.0%	2.0% to 5.0%	$0.10 to $0.20	6 to 12
INVESTMENT BANKER ■ Forecast Period: 10 years Real cash on cash (after capital expenditures) more important than IRR.	Years 1-3 varies; 3.5% thereafter	3.0%	3.0%	8.50% to 10.50%	2.0%	10.50% to 12.50%	8.00% to 10.50%	6 to 9	65.0%	5.0% to 7.5%	$0.10 to $0.20	6 to 9
DOMESTIC PENSION FUND ■ Forecast Period: 10 to 12 years Buys free and clear; average IRR consists of a 6.5% to 7.5% real rate of return plus the inflation rate; the indicated growth scenarios help to determine sensitivity of investment to inflation; relies on DCF (IRR) and overall cap rates equally; use of face or effective rents varies with market.	Years 1-3 varies per market; thereafter at inflationary rate	2.0%/ 4.0%/ 6.0%	2.0%/ 4.0%/ 6.0%	9.00% to 9.25%	2.0%	10.50% to 11.50%	8.75% to 9.50%	6 to 9	60.0% to 70.0%	2.0% to 5.0%	$0.10 to $0.20	9 to 12
INVESTMENT ADVISOR ■ Forecast Period: 5 to 10 years Seeks a discount to replacement cost in recovering markets; in certain markets may apply spike in first three years; uses face rents.	3.5% to 7.0%	3.5%	3.5%	9.00% to 10.00%	2.0% to 3.0%	10.75% to 12.50%	7.50% to 9.00%	6 to 12	50.0% to 75.0%	5.0% to 10.0%	$0.20 to $0.40	6
REAL ESTATE ADVISOR ■ Forecast Period: 10 to 15 years Relies on DCF (IRR), direct capitalization (initial cap rates), and price per square foot; uses face rents and reflects free rent and other concessions when they are scheduled to occur; placing additional emphasis on average cash-on-cash rates for years 1 to 5, 6 to 10, and then the average rate for 1 to 10, coupled with partitioning present values and placing greater weight on cash flow vs. residual; continuing caution.	2.0% to 5.0%	3.0% to 4.0%	3.0% to 4.0%	9.00% to 10.00%	2.0% to 4.0%	10.50% to 12.50%	9.00% to 10.50%	6 to 9	60.0% to 70.0%	3.0% to 4.0%	$0.20 to $0.50	12 to 18
INVESTMENT ADVISOR ■ Forecast Period: 10 years Prefers free and clear properties with joint venture partner and preferred return; uses all valuation techniques and correlates; does not rely on any one technique; looks at components of NOI growth; uses face rents.	0.0% to 8.0%	3.5%	3.5%	9.00% to 10.00%	1.5%	11.00% to 12.00%	8.50% to 10.00%	4 to 6	70.0%	2.0% to 5.0%	$0.10 to $0.20	6 to 9
DOMESTIC PENSION FUND ■ Forecast Period: 7 years Relies on DCF (IRR), direct capitalization (initial cap rates), and price per square foot; uses effective rents.	3.0% to 4.0%	3.0%	3.0%	9.00% to 10.50%	2.0% to 3.0%	11.00% to 11.50%	9.00% to 10.00%	6 to 8	60.0%	5.0%	$0.15 to $0.20	6 to 12
INVESTOR ■ Forecast Period: 5 to 7 years Relies on DCF and direct capitalization; selling expense capped at $150,000; uses face rents.	4.0% to 5.0%	3.0%	2.5%	8.50%	1.5%	10.00%	8.00% to 8.50%	4 to 6	70.0%	1.0%	$0.50	—
REAL ESTATE ADVISOR ■ Forecast Period: 10 years Relies on DCF, also uses direct capitalization and price per square foot; initial market rent change rate for years 1 to 3 is a spike and is a function of the Torto-Wheaton forecast rent in individual markets; residual cap rate is in part developed through a second 10-year DCF analysis.	Varies per market	2.5% to 3.0%	2.75% to 3.0%	9.00% to 11.00%	3.0%	10.50% to 11.50%	9.00% to 10.50%	6	60.0% to 80.0%	5.0% to 7.0%	$0.10 to $0.20	—
INSTITUTIONAL INVESTOR ■ Forecast Period: 10 years Invests primarily in newer suburban office properties with credit quality tenants; relies on DCF; market rent growth rates vary according to supply-demand balance in specific market; applies rent spikes as warranted by market conditions and specific property; uses effective rents.	2.0% to 4.0%; varies thereafter	2.0% to 3.5%	2.0% to 3.5%	9.50% to 10.00%	2.0% to 3.0%	11.00% to 11.75%	9.00% to 9.75%	4 to 8	50.0% to 60.0%	1.0% to 3.0%	$0.15 to $0.20	6 to 7

Atlanta Office Market

INVESTOR SURVEY RESPONSES

FIRST QUARTER 1999

Source: Personal survey conducted by
The Korpacz Company, Inc. during January 1999.

	CHANGE RATES			RESIDUAL		DISCOUNT RATE (IRR)	OVERALL CAP RATE (OAR)	VACANCY ASSUMPTIONS			RESERVE	MARKETING TIME
	Market Rent	Expenses	CPI	Cap Rate	Selling Expense	Free & Clear	Free & Clear	Months Vacant	Tenant Retention	Underlying Vacancy & Credit Loss	Per Square Foot	Months
DEVELOPER ■ Forecast Period: 10 years Uses both DCF and direct capitalization; in direct cap, capitalizes NOI after capital replacement reserve deduction but before TIs and leasing commissions; uses face rents and reflects concessions when they are scheduled to occur.	2.5%	3.0%	3.0%	9.00%	2.5%	9.75% to 10.50%	9.50%	6 to 9	67.0%	7.0%	$0.15 to $0.20	—
INVESTMENT ADVISOR ■ Forecast Period: 10 years Relies on DCF; does not do a true direct capitalization approach but analyzes the implied year 1 overall cap rate based on NOI divided by value conclusion.	3.5%	3.5%	3.5%	9.50%	1.5% to 2.0%	11.00%	9.20% to 9.60%	2 on weighted basis	60.0%	4.0%	$0.10	—
LIFE INSURANCE COMPANY ■ Forecast Period: 10 years Prefers suburban properties; uses DCF and direct capitalization; uses face rents and allocates concessions when they are scheduled to occur; no longer applies rent spikes.	0.0% to 3.5%	3.0%	3.0%	9.25% to 9.50%	3.0%	11.25% to 11.50%	9.00% to 9.50%	6	65.0%	5.0% to 10.0%	$0.20 to $0.25	3 to 6
INVESTMENT ADVISOR ■ Forecast Period: 10 years Uses both DCF and direct capitalization; in direct cap, capitalizes NOI before TIs, leasing commissions, and capital replacement reserve; uses face rents and reflects concessions when they are scheduled to occur; concerned that construction activity could soften market.	0.0% to 2.0%	$8.00 per square foot	3.0%	9.50%	1.0%	10.00% to 11.00%	8.75%	6	65.0%	7.0%	$0.25	—
LIFE INSURANCE COMPANY ■ Forecast Period: 5 to 8 years Uses DCF and direct capitalization; relies on DCF; in direct cap, capitalizes NOI after capital replacement reserve but before TIs and leasing commissions; uses face rents and reflects concessions when they are scheduled to occur; also considers discount to replacement cost.	0.0% to 3.0%	3.0%	2.0%	9.50% to 11.00%	2.0%	11.00% to 12.00%	8.00% to 10.50%	6	60.0%	4.0%	$0.25	6 to 9
INVESTMENT ADVISOR ■ Forecast Period: 10 years Relies on DCF; typical management fees are 4.0%; typical leasing fees are 5.0% on new leases, 2.0% on renewals; typical TIs are $5.00 for new leases, $3.25 for renewals; uses face rents; structural vacancy	3.0%	3.0%	3.0%	9.25%	2.0%	12.00%	9.25%	0	75.0%	5.0%	$1.05	6 to 9

Chicago Office Market

INVESTOR SURVEY RESPONSES*

FIRST QUARTER 1999

*Representative sample; due to space constraints, not all responses are included.

Source: Personal survey conducted by The Korpacz Company, Inc. during January 1999.

	CHANGE RATES			RESIDUAL		DISCOUNT RATE (IRR)	OVERALL CAP RATE (OAR)	VACANCY ASSUMPTIONS			RESERVE	MARKETING TIME
	Market Rent	Expenses	CPI	Cap Rate	Selling Expense	Free & Clear	Free & Clear	Months Vacant	Tenant Retention	Underlying Vacancy & Credit Loss	Per Square Foot	Months
REAL ESTATE ADVISOR ■ Forecast Period: 10 years Relies on DCF; uses direct capitalization as a check only; real estate taxes are a major issue; prefers suburban markets; uses face rents and reflects concessions when they are scheduled to occur.	3.0%	3.0%	3.0%	8.00% to 10.00%	2.0% to 3.0%	9.29% to 11.80%	8.00% to 9.50%	3 to 6	60.0% to 75.0%	5.0%	$0.15 to $0.20	9 to 12
MORTGAGE BANKER ■ Forecast Period: 10 years Relies on DCF and uses direct capitalization as a test; cost, rent, and value per square foot are true "sanity tests"; real estate taxes are a big issue (usually more than 50.0% of property expenses); uses effective rents; geographic preferences are downtown and north suburban.	3.0% to 5.0%	3.0%	3.0%	9.25% to 9.50%	2.0%	11.00%	9.00%	6	70.0% to 75.0%	5.0%	$0.15	6 to 9
INSTITUTIONAL INVESTOR ■ Forecast Period: 5 years Relies on DCF; forecasts market rent at 6.0% year 1, 5.0% year 2, 4.0% year 3, and 3.0% thereafter; forecasts higher expenses in Cook County; in direct cap, capitalizes NOI before TIs, leasing commissions, and capital replacement reserve.	6.0%	$7.00 to $8.00 per square foot	3.0%	8.50% to 9.50%	1.0% to 3.0%	11.00% to 13.00%	—	3	75.0%	1.0%	$0.20	6
INSTITUTIONAL INVESTOR ■ Forecast Period: 10 years Relies on DCF; market rent growth rates vary according to supply-demand balance in specific submarket; applies rent spikes as warranted by conditions and specific property; uses present value analysis of effective rents.	Varies per submarket until stabilized; thereafter at inflation rate	2.0% to 3.5%	2.0% to 3.5%	9.25% to 9.75% (Suburbs); 9.50% to 10.50% (CBD)	2.0% to 3.0%	11.00% to 12.00%	9.25% to 10.25%	3 to 9	50.0% to 60.0%	1.0% to 3.0%	$0.15 to $0.20	3 to 6 (Suburbs); 6 to 12 (CBD)
REAL ESTATE ADVISOR ■ Forecast Period: 10 years Prefers suburban properties; uses both DCF and direct capitalization; relies on DCF; in direct cap, capitalizes NOI after capital reserve deduction but before TIs and leasing commissions; may apply rent spike on limited basis; uses effective rents.	3.0%	3.0%	2.5% to 3.5%	9.25%	2.5% to 3.0%	10.50% to 11.50%	9.00% to 9.50%	6	50.0%	7.0% to 10.0%	$0.15 to $0.20	9 to 12
LIFE INSURANCE COMPANY ■ Forecast Period: 10 years Buys suburban office properties only; uses DCF and direct capitalization; also looks at average 5-year cash-on-cash returns; applies 5.0% to 8.0% rent spike in years 1 to 3 in suburban markets with supply constraints, strong demand, limited new construction, and rents below level required to support new construction; uses face rents and allocates concessions when they are scheduled to occur; marketing time estimate is for properties that are "priced right."	3.5% to 6.0%	3.0%	3.0%	9.00% to 9.25%	3.0% to 4.0%	10.00% to 11.25%	8.00% to 9.00%	3 to 6	60.0% to 65.0%	5.0% to 10.0%	$0.20% to $0.25%	3 to 6
REAL ESTATE ADVISOR ■ Forecast Period: 10 years Uses both DCF and direct capitalization; occasionally applies 7.0% to 9.0% rent spike for 1, 2, or 3 years on top-quality product in the strongest suburbs; buyers' market; uses face rents.	0.0% to 3.0% (CBD); 2.0% to 5.0% (Suburbs)	4.0%	—	9.25% to 9.50% (Suburbs); 10.00% (CBD)	2.0% to 2.5%	10.00% to 10.75%	10.00%	6 to 9 (Suburbs); 9 to 12 (CBD)	50.0% to 70.0%	3.0% to 7.0% (Suburbs); 5.0% to 10.0% (CBD)	$0.20% to $0.25%	9 to 12

Dallas Office Market

INVESTOR SURVEY RESPONSES*

FIRST QUARTER 1999

*Representative sample; due to space constraints, not all responses are included.

Source: Personal survey conducted by The Korpacz Company, Inc. during January 1999.

	CHANGE RATES			RESIDUAL		DISCOUNT RATE (IRR)	OVERALL CAP RATE (OAR)	VACANCY ASSUMPTIONS			RESERVE	MARKETING TIME
	Market Rent	Expenses	CPI	Cap Rate	Selling Expense	Free & Clear	Free & Clear	Months Vacant	Tenant Retention	Underlying Vacancy & Credit Loss	Per Square Foot	Months
LIFE INSURANCE COMPANY ■ Forecast Period: 10 years Relies on DCF; also uses direct capitalization and sales comparison in CBDs; properties with upside command lower going-in cap rates; uses rent spikes.	3.5% (Suburbs); 0.0% (CBD) years 1 and 2; 3.5% thereafter	2.5%	3.0%	9.00% to 12.00%	1.5% to 5.0%	10.50% (Suburbs) to 12.00% (CBD)	8.00% to 12.00%	4 to 6	70.0% (Suburbs); 60.0% (All others)	10.0% (Suburbs); 15.0% (CBD)	1.0% of EGI	12
INVESTMENT ADVISOR ■ Forecast Period: 3, 5, and 10 years Relies on DCF and direct capitalization; there are no concessions and no free rent in this market; no longer applies rent spikes.	0.0% to 2.0%	4.0%	4.0%	8.50% to 9.50%	2.0%	10.50% to 11.50%	7.50% to 9.50%	6 to 9	60.0% to 75.0%	5.0%	$0.25	9
REAL ESTATE ADVISOR ■ Forecast Period: 10 years Buys all cash; focuses on DCF analysis, then looks at cash-on-cash returns in years 2 to 5; looks at 5-year averages and cash-on-cash returns after leasing commissions, TIs, and reserves; also "goes above the line" to see true capitalization rate.	0.0% to 5.0%	3.0% to 4.0%	3.0% to 4.0%	9.25% to 10.25%	2.0% to 4.0%	11.00% to 13.00%	8.50% to 10.00%	4 to 7	60.0% to 70.0%	2.0% to 3.0%	$0.20 to $0.50	3 to 6
INVESTMENT ADVISOR ■ Forecast Period: 10 and 20 years Criteria for downtown and suburban submarkets vary widely; uses both DCF and direct capitalization; ties most expenses to CPI but projects others (e.g., utilities and real estate taxes) at higher rate; applies a 10.0% rent spike in years 1 through 3; uses effective rents.	4.0% to 10.0%	3.5% to 4.0%	3.5%	8.00% to 9.50%	2.0%	10.00% to 12.00%	8.00% to 11.00%	5	70.0%	5.0%	3.0% to 7.0% of EGI	6
INVESTMENT ADVISOR ■ Forecast Period: 5 to 10 years Interested in both CBD and suburban properties; relies on DCF and direct capitalization; in direct cap, capitalizes cash flow after TIs, leasing commissions, and capital replacement reserve; uses face rents.	4.0%	4.0%	3.5%	9.00% to 9.50%	2.0%	11.00% to 13.00%	8.00% to 9.00%	6 to 9	60.0% to 75.0%	5.0%	$0.05 to $0.15	2
LIFE INSURANCE COMPANY ■ Forecast Period: 10 years Interest is in Dallas suburbs only; uses DCF and direct capitalization; applies rent spikes of 5.0% to 7.0% in years 1 to 3; uses face rents and allocates concessions when they are scheduled to occur; marketing time estimate is for properties that are "priced right."	3.0% to 4.0%	3.0%	3.0%	9.00% to 9.50%	2.0% to 4.0%	11.00% to 11.50%	8.75% to 9.25%	6	65.0%	5.0% to 10.0%	$0.20 to $0.25	4 to 9
LIFE INSURANCE COMPANY ■ Forecast Period; 5 to 8 years Uses DCF and direct capitalization; also looks at discount to replacement cost; relies on DCF; in direct cap, capitalizes NOI after capital replacement reserve but before TIs and leasing commissions; there are few concessions in this market, therefore face rent equals effective rent.	3.0%	2.5%	2.0%	9.00% to 11.00%	2.0%	11.00% to 12.00%	8.00% to 10.00%	6	60.0%	4.0%	$0.25	6

Houston Office Market

INVESTOR SURVEY RESPONSES*

FIRST QUARTER 1999

*Representative sample; due to space constraints, not all responses are included.

Source: Personal survey conducted by The Korpacz Company, Inc. during January 1999.

	CHANGE RATES			RESIDUAL		DISCOUNT RATE (IRR)	OVERALL CAP RATE (OAR)	VACANCY ASSUMPTIONS			RESERVE	MARKETING TIME
	Market Rent	Expenses	CPI	Cap Rate	Selling Expense	Free & Clear	Free & Clear	Months Vacant	Tenant Retention	Underlying Vacancy & Credit Loss	Per Square Foot	Months
LIFE INSURANCE COMPANY ■ Forecast Period: 10 years Relies on DCF; also uses direct capitalization and sales comparison in CBDs; uses effective rents; properties with upside command lower going-in cap rates.	3.0% to 3.5% (Suburbs); 0.0% (CBD)	3.5%	3.5%	8.00% to 12.00%	1.5% to 5.0%	10.50% (Suburbs); to 12.50% (CBD)	8.00% to 12.00%	4 to 6	70.0% (Suburbs); to 60.0% (All others)	10.0% (Suburbs); to 12.0% (All others)	1.0% of EGI	12
INVESTMENT ADVISOR ■ Forecast Period; 3, 5, and 10 years Relies on DCF and direct capitalization; there are no concessions and no free rent in this market; applies 5.0% to 8.0% rent spikes in years 1 to 3 in suburban submarkets.	4.0% to 8.0%	4.0%	4.0%	9.00% to 10.50%	2.0%	10.50% to 12.00%	8.50% to 11.00%	6 to 9	60.0% to 75.0%	5.0%	$0.25	9
REAL ESTATE ADVISOR ■ Forecast Period: 10 years Buys all cash; focuses on DCF analysis, then looks at cash-on-cash returns in years 2 to 5; looks at 5-year averages and cash-on-cash returns after leasing commissions, TIs, and reserves; also "goes above the line" to see true capitalization rate.	2.0% to 5.0%	3.0% to 4.0%	3.0% to 4.0%	9.00% to 10.00%	2.0% to 4.0%	11.00% to 13.00%	8.75% to 10.25%	4 to 7	60.0% to 70.0%	2.0% to 3.0%	$0.20 to $0.50	3 to 6
INVESTMENT ADVISOR ■ Forecast Period: 10 and 20 years Criteria for downtown and suburban submarkets vary widely; uses both DCF and direct capitalization; ties most expenses to CPI but projects others (e.g., utilities and real estate taxes) at higher rate; uses effective rents.	2.0% to 8.0%	4.0%	4.0%	8.00% to 9.50%	2.0%	10.00% to 12.00%	8.00% to 11.00%	5	70.0%	5.0%	3.0% to 7.0% of EGI	6
INVESTMENT ADVISOR ■ Forecast Period: 5 to 10 years Interested in both CBD and suburban properties; relies on DCF and direct capitalization; in direct cap, capitalizes cash flow after TIs, leasing commissions, and capital replacement reserve; uses face rents.	4.0%	4.0%	3.5%	9.00% to 9.50%	2.0%	11.00% to 13.00%	8.00% to 9.00%	6 to 9	60.0% to 75.0%	5.0%	$0.05 to $0.15	2
LIFE INSURANCE COMPANY ■ Forecast Period: 10 years Interest is in Houston suburbs only; uses DCF and direct capitalization; applies rent spikes of 5.0% to 7.0% in years 1 to 3; uses face rents and allocates concessions when they are scheduled to occur; marketing time estimate is for properties that are "priced right"; still some concern over cyclical nature of economy.	4.0% to 5.0%	3.0%	3.0%	9.25% to 9.75%	2.0% to 4.0%	11.25% to 11.75%	9.00% to 9.50%	3 to 6	65.0%	5.0% to 10.0%	$0.20 to $0.25	4 to 9
LIFE INSURANCE COMPANY ■ Forecast Period; 5 to 8 years Uses DCF and direct capitalization; also looks at discount to replacement cost; relies on DCF; in direct cap, capitalizes NOI after capital replacement reserve but before TIs and leasing commissions; uses face rents and reflects concessions when they are scheduled to occur.	2.0% to 4.0%	3.0% to 4.0%	2.0%	9.50% to 11.00%	2.0%	10.50% to 13.50%	8.00% to 10.00%	6	60.0%	4.0%	$0.25	6 to 9

Korpacz

Los Angeles Office Market

INVESTOR SURVEY RESPONSES*

FIRST QUARTER 1999

*Representative sample; due to space constraints, not all responses are included.

Source: Personal survey conducted by The Korpacz Company, Inc. during January 1999.

	CHANGE RATES			RESIDUAL		DISCOUNT RATE (IRR)	OVERALL CAP RATE (OAR)	VACANCY ASSUMPTIONS			RESERVE	MARKETING TIME
	Market Rent	Expenses	CPI	Cap Rate	Selling Expense	Free & Clear	Free & Clear	Months Vacant	Tenant Retention	Underlying Vacancy & Credit Loss	Per Square Foot	Months
PENSION FUND ADVISOR ■ Forecast Period: 7 to 10 years Relies on DCF; looks at value indicated by direct capitalization; uses face rents and applies concessions when projected to occur; does not tie income or expenses directly to CPI.	2.5% to 6.0%	3.0% to 4.0%; taxes 2.25%	2.5% to 3.0%	9.00% to 10.00%	2.0% to 3.0%	11.00% to 13.00%	9.00% to 10.00%	4 to 7	65.0% to 75.0%	5.0% to 8.0%	$0.10 to $0.20	6 to 8
REAL ESTATE ADVISOR ■ Forecast Period: 5, 7, and 10 years Buys turnaround situations as well as rotational plays in suburban markets; uses both DCF and direct capitalization; relies on DCF; applies 4.0% to 10.0% rent spike in years 1 to 2 in submarkets where there is evidence that they will occur; uses face rents in DCF model, net effective rents in direct capitalization.	4.0% to 6.0%	4.0%	4.0%	8.00% to 10.00%	1.5% to 2.0%	11.00% to 13.00%	8.00% to 10.00%	2 to 12	65.0%	8.0% to 10.0%	$0.30 to $1.00	6
INVESTMENT BANKER ■ Forecast Period: 10 years Uses DCF (IRR), direct capitalization (initial cap rates), and price per square foot; does extensive sensitivity analysis and correlates all value indications; uses face rents; IRRs for Class-A properties are 10.00% to 13.00%; investors looking at IRRs again; cash on cash is important, but perceived improvement in market is more important.	4.0% to 5.0%	3.0% to 4.0%	3.0% to 4.0%	9.00% to 10.00%	2.0%	10.50% to 14.00%	7.00% to 10.00%	4 to 6	65.0% to 75.0%	5.0% to 10.0%	Does not use	6 to 12
INVESTMENT ADVISOR ■ Forecast Period: 10 years Uses both DCF and direct capitalization; in direct cap, capitalizes NOI before TIs, leasing commissions, and capital replacement reserve; applies rent spike in years 1 and 2 in certain submarkets; uses face rents and reflects concessions when they are scheduled to occur.	10.0%	3.5%	3.5%	9.00%	2.0%	10.50% to 11.00%	9.00%	6	70.0%	5.0%	$0.20	—
INVESTMENT ADVISOR ■ Forecast Period: 5 to 15 years Buys free and clear; looks for minimum 5.0%+ real IRR; uses face rents; relies on DCF, cash returns after capital expenses, and price per square foot; prefers new buildings with 85.0%+ occupancy.	Spikes in years 1-3	4.0%	3.5%	9.00% to 10.50%	2.0%	10.50% to 12.25%	7.50% to 9.00%	6 to 9	60.0% to 75.0%	5.0% to 10.0%	$0.05 to $0.15	2 to 5
INSTITUTIONAL INVESTOR ■ Forecast Period: 3 to 5 years Uses both DCF and direct capitalization; in direct cap, capitalizes NOI after capital replacement reserve deduction but before TIs and leasing commissions.	3.0% to 5.0%	3.0%	4.0%	8.50% to 9.50%	2.0% to 5.0%	12.00% to 14.00%	8.00% to 9.00%	6	75.0%	5.0%	$0.15 to $0.20	3
INVESTOR ■ Forecast Period: 5 years Uses both DCF and direct capitalization; in direct cap, capitalizes NOI before TIs, leasing commissions, and capital replacement reserve; typically looks for Class-A, 150,000-square-foot and larger properties in Tier 1 locations; likes opportunities for turnaround, repositioning, and select renovation projects.	5.0% to 8.0%	3.0% to 3.5%	2.5%	9.50%	1.5%	12.00%	8.00%	4	70.0%	3.0% to 4.0%	$0.10 to $0.15	4 to 6
LIFE INSURANCE COMPANY ■ Forecast Period: 10 years Relies primarily on DCF; also uses direct capitalization; in direct cap, capitalizes NOI before TIs, leasing commissions, and capital replacement reserve; applies 4.0% to 5.0% rent spike in year 1 and/or 2 in certain West Los Angeles submarkets.	3.0% to 4.0%	3.0%	3.0%	8.75% to 11.25%	1.5% to 4.0%	10.50% to 12.25%	8.50% to 10.50%	6 to 12	50.0% to 60.0%	3.0% to 4.0%	$0.20 to $0.25	5 to 10

Manhattan Office Market

INVESTOR SURVEY RESPONSES*

FIRST QUARTER 1999

*Representative sample; due to space constraints, not all responses are included.

Source: Personal survey conducted by The Korpacz Company, Inc. during January 1999.

	CHANGE RATES			RESIDUAL		DISCOUNT RATE (IRR)	OVERALL CAP RATE (OAR)	VACANCY ASSUMPTIONS			RESERVE	MARKETING TIME
	Market Rent	Expenses	CPI	Cap Rate	Selling Expense	Free & Clear	Free & Clear	Months Vacant	Tenant Retention	Underlying Vacancy & Credit Loss	Per Square Foot	Months
INVESTMENT BANKER ■ Forecast Period: 10 years Strongest interest is in Midtown; criteria are for Midtown.	5.0% years 1-3; 3.5% thereafter	3.0%	3.0%	8.00% to 10.00%	2.5%	10.00% to 12.00%	7.50% to 10.00%	6 to 12	65.0%	3.5% to 7.0%	Varies	6 to 9
DOMESTIC PENSION FUND ■ Forecast Period: 10 to 12 years Buys free and clear; average IRR consists of a 6.5% to 7.5% real rate of return, plus the inflation rate used on market rent. The three indicated growth scenarios help to test the sensitivity of investment to inflation; relies on DCF (IRR); NYC reassessment at 45.0% of sale price with five-year phase-in and 2.0% tax rate increase beginning after phase-in; use of face or effective rents varies by submarket.	2.0% years 1-2; inflation thereafter	2.0%/ 4.0%/ 6.0%	2.0%/ 4.0%/ 6.0%	8.00% to 9.00%	1.0% to 6.0%	10.50% to 11.50%	8.25% to 9.25%	6 to 9	60.0% to 70.0%	2.0% to 5.0%	$0.10 to $0.20	9 to 12
DOMESTIC PENSION FUND ■ Forecast Period: 10 years Reflects NYC reassessment at 40.0% to 45.0% of sale price with tax rate increases of 5.0% per year; looks at DCF, direct capitalization (initial cap rates), and price per square foot.	3.0%	3.0%	3.0%	9.00% to 10.50%	1.0% to 2.0%	11.00% to 12.50%	8.50% to 10.00%	6 to 9	60.0%	5.0%	$0.10 to $0.15	12 to 18
REAL ESTATE ADVISOR ■ Forecast Period: 10 to 12 years NYC reassessment at 38.0% to 45.0% of sale price with five-year phase-in; very concerned about NYC's assessment practices; relies on DCF (IRR), direct capitalization, and price per square foot; emphasis on cash-on-cash rates; more realistic credit loss, downtime, free rent, TIs, and annual capital reserve; uses face rents and reflects concessions when they are scheduled to occur; applies 5.0% to 7.0% rent spike in years 3 to 4 in selected Downtown submarkets; more concerned with the resale estimate.	3.0% to 4.0% (Midtown); 0.0% initially, then 2.0% to 4.0% (Downtown older product)	3.0% to 4.0%	3.0% to 4.0%	8.00% to 10.00%	2.0% to 4.0%	10.50% to 12.50%	8.00% to 9.50%	6 to 12	60.0% to 70.0%	1.0% to 3.0%	$0.20 to $0.50	6 to 12
INVESTMENT ADVISOR ■ Forecast Period: 10 years Prefers free and clear, reflects NYC reassessment at 40.0% to 45.0% of sale price with five-year phase-in and increase of tax rates at 5.0% per year; does not place primary reliance on any technique; uses all and correlates; also looks at components of NOI growth; uses face rents.	4.0%	3.5%	3.5%	8.50% to 9.50%	1.5%	11.00% to 12.00%	8.50% to 10.00%	4 to 6	65.0%	5.0% to 10.0%	$0.10 to $0.20	9 to 12
INVESTMENT ADVISOR ■ Forecast Period: 10 years Uses both DCF and direct capitalization; in direct cap, capitalizes NOI before TIs, leasing commissions, and capital reserve; uses face rents and reflects concessions when they are scheduled to occur; foreign investors continue to have an interest in Manhattan office buildings.	3.5%	3.5%	3.5%	9.00% to 10.00%	1.0% to 3.0%	10.75% to 12.50%	8.00% to 10.00%	9 to 12	50.0% to 70.0%	3.0% to 7.0%	$0.40	9 to 12
REAL ESTATE ADVISOR ■ Forecast Period: 5, 7, and 10 years Uses both DCF and direct capitalization; relies on DCF; uses face rents in DCF model, net effective rents in direct capitalization; prefers Downtown and Times Square.	4.0% to 6.0%	4.0%	4.0%	8.00% to 10.00%	1.5% to 2.0%	11.00% to 13.00%	8.00% to 10.00%	2 to 18	60.0%	8.0% to 14.0%	—	10
INVESTMENT ADVISOR ■ Forecast Period: 10 to 15 years Buys free and clear; uses face rents; prefers Midtown; looks for a 7.0% to 8.0% real IRR; relies on direct cap, DCF, and price per square foot.	4.0%	4.0% to 5.0%	3.5%	9.00% to 10.00%	8.0% to 10.0%	10.00% to 11.00%	8.50% to 10.00%	8	65.0% to 75.0%	5.0%	$0.25	2

Pacific Northwest Office Market

INVESTOR SURVEY RESPONSES

FIRST QUARTER 1999

Source: Personal survey conducted by
The Korpacz Company, Inc. during January 1999.

	CHANGE RATES			RESIDUAL		DISCOUNT RATE (IRR)	OVERALL CAP RATE (OAR)	VACANCY ASSUMPTIONS			RESERVE	MARKETING TIME
	Market Rent	Expenses	CPI	Cap Rate	Selling Expense	Free & Clear	Free & Clear	Months Vacant	Tenant Retention	Underlying Vacancy & Credit Loss	Per Square Foot	Months
REAL ESTATE ADVISOR ■ Forecast Period: 10 years Uses both DCF and direct capitalization; preference for DCF; interested in both CBD and suburban properties in both Seattle and Portland; uses face rents.	5.0%	3.0%	---	9.00% to 9.50%	2.0% to 2.5%	11.50%	9.50% to 10.00%	6	60.0% to 70.0%	5.0%	$0.20 to $0.25	9 to 12
INVESTOR ■ Forecast Period: 10 years Uses both DCF and direct capitalization; in direct cap, capitalizes NOI before TIs, leasing commissions, and capital replacement reserve; there are no concessions in this market; rental rates continue to rise in Puget Sound market area; vacancy rate continues to drop; prefers Puget Sound area and Spokane, Washington.	8.0%	3.0%	3.0%	8.50% to 10.00%	3.0%	10.75% to 12.00%	8.50% to 11.00%	3 to 9	75.0% to 80.0%	0.0% to 4.0%	Does not use	6 to 12
INVESTMENT BANKER ■ Forecast Period: 10 years Uses DCF (IRR), direct capitalization, and price per square foot; does extensive sensitivity analysis; reliance is on projections and IRRs; uses face rents.	4.0%	4.0%	4.0%	9.00% to 10.00%	2.0%	10.00% to 13.00%	8.00% to 10.00%	3 to 6	65.0% to 70.0%	5.0% to 10.0%	Does not use	6 to 9
INVESTMENT ADVISOR ■ Forecast Period: 10 years Uses primarily DCF; in direct cap, capitalizes NOI before TIs, leasing commissions, and capital replacement reserve; applies rent spike in year 1 in certain submarkets; uses face rents and reflects concessions when they are scheduled to occur.	3.0% to 3.5%	3.5%	3.0% to 3.5%	9.00% to 9.50%	2.0% to 3.0%	10.50% to 11.00%	8.00%	6	65.0%	2.0% to 5.0%	$0.15 to $0.20	6
INVESTOR ■ Forecast Period: 5 to 10 years Uses both DCF and direct capitalization; in direct cap, capitalizes NOI before TIs, leasing commissions, capital replacement reserve; dropping rent spikes because the market has already moved.	Varies	2.0% to 4.0%	1.5% to 2.5%	9.50% to 10.50%	3.0% to 5.0%	10.00% to 13.00%	8.75% to 10.00%	6	75.0%	5.0%	$0.20 or 2.0% of EGI	3 to 6
REAL ESTATE ADVISOR ■ Forecast Period: 10 years Uses both DCF and direct capitalization; relies on DCF; in direct cap, capitalizes NOI after capital reserve deduction but before TIs and leasing commissions; uses effective rents.	2.5%	3.0%	2.5% to 3.5%	9.25%	2.5% to 3.0%	10.50% to 11.50%	9.25%	6 to 9	50.0%	7.0% to 10.0%	$0.15 to $0.20	6 to 9
INSTITUTIONAL INVESTOR ■ Forecast Period: 10 years Buys free and clear; interested in attractive, well-located Class-A properties; relies on DCF (IRR); uses direct capitalization as a check only; may apply a 5.0% to 8.0% rent spike if justified by submarket conditions and specific property; uses face rents in model that allocates actual concessions when they are scheduled to occur; underlying vacancy and credit loss may be lower based on current occupancy, leases in place, and rollover risk.	4.0% to 5.0%	3.75% to 4.0%	3.0%	9.25% to 9.75%	3.0% + any local tariffs	11.00% to 11.50%	8.75% to 9.50%	6	70.0%	6.0% to 8.0%	$0.25 to $0.50	6

San Francisco Office Market

INVESTOR SURVEY RESPONSES

FIRST QUARTER 1999

Source: Personal survey conducted by
The Korpacz Company, Inc. during January 1999.

	CHANGE RATES			RESIDUAL		DISCOUNT RATE (IRR)	OVERALL CAP RATE (OAR)	VACANCY ASSUMPTIONS			RESERVE	MARKETING TIME
	Market Rent	Expenses	CPI	Cap Rate	Selling Expense	Free & Clear	Free & Clear	Months Vacant	Tenant Retention	Underlying Vacancy & Credit Loss	Per Square Foot	Months
INVESTMENT ADVISOR ■ Forecast Period: 5 to 10 years Relies on DCF; applies rent spike in years 1 to 3; typical management fees are 3.0%; typical leasing fees are $9.00 on new leases, $4.50 on renewals; typical TIs are $15.00 for new leases, $9.75 for renewals; structural vacancy has been reached in this market.	8.00%	3.0%	3.0%	8.25% to 8.75%	1.0%	10.00% to 10.50%	8.50%	2	75.0%	5.0%	$0.10 to $0.25	3 to 6
PENSION FUND ADVISOR ■ Forecast Period: 7 and 10 years Uses DCF and direct capitalization but relies on DCF; uses face rents and reflects actual concessions when scheduled to occur; market rent growing faster than CPI; no longer applies a rent spike.	4.0% to 6.0%	3.0% to 4.0%; taxes 2.0%	3.0% to 3.5%	8.00% to 9.50%	1.0% to 2.0%	10.50% to 12.00%	7.50% to 8.50%	5 to 8	60.0% to 70.0%	3.0% to 5.0%	$0.10 to $0.20	6 to 9
REAL ESTATE ADVISOR ■ Forecast Period: 5 to 10 years Uses both DCF and direct capitalization; in direct cap, capitalizes NOI before TIs, leasing commissions, and capital replacement reserve; no longer applies rent spike; uses face rents and reflects concessions when they are scheduled to occur; is placing greater focus on rents in place.	4.0%	4.0%	4.0%	8.50% to 9.00%	1.0% to 1.5%	10.50% to 11.00%	7.50% to 9.00%	6	70.0%	5.0%	$0.15 to $0.25	6 to 9
REAL ESTATE ADVISOR ■ Forecast Period: 5 and 10 years Buys turnaround situations as well as rotational plays in suburban markets; uses both DCF and direct capitalization; relies on DCF; applies 4.0% to 10.0% rent spike in years 1 through 3 in submarkets where there is evidence that they will occur; uses face rents in DCF model, net effective rents in direct capitalization.	0.0% to 10.0%	4.0%	4.0%	8.00% to 10.00%	1.5% to 2.0%	9.25% to 12.00%	8.00% to 11.00%	2 to 18	60.0% to 65.0%	0.0% to 6.0%	—	3 to 6
DOMESTIC PENSION FUND ■ Forecast Period: 10 years Prefers CBD; uses both DCF and direct capitalization; projects a 5.0% to 8.0% rent spike for CBD buildings in years 1 and 2; uses face rents and reflects concessions when they are scheduled to occur.	3.0% to 4.0%	3.5%	3.5%	8.50% to 9.50%	1.0% to 2.0%	10.00% to 11.50%	7.50% to 9.00%	8 to 10	60.0% to 70.0%	1.0% to 3.0%	$0.10 to $0.25	6 to 12
LIFE INSURANCE COMPANY ■ Forecast Period: 10 years Uses both DCF and direct capitalization; in direct cap, capitalizes NOI before TIs, leasing commissions, and capital replacement reserve; forecasts expenses at 100% of projected CPI; no longer applies a rent spike.	0.0% to 5.0%	3.0%	3.0%	9.00% to 9.50%	1.5% to 4.0%	10.00% to 11.25%	7.00% to 9.00%	3 to 10	60.0% to 70.0%	1.5% to 5.0%	$0.20 to $0.30	3 to 6

Korpacz

Southeast Florida Office Market

INVESTOR SURVEY RESPONSES*

FIRST QUARTER 1999

*Representative sample; due to space constraints, not all responses are included.

Source: Personal survey conducted by The Korpacz Company, Inc. during January 1999.

	CHANGE RATES			RESIDUAL		DISCOUNT RATE (IRR)	OVERALL CAP RATE (OAR)	VACANCY ASSUMPTIONS			RESERVE	MARKETING TIME
	Market Rent	Expenses	CPI	Cap Rate	Selling Expense	Free & Clear	Free & Clear	Months Vacant	Tenant Retention	Underlying Vacancy & Credit Loss	Per Square Foot	Months
REIT ■ Forecast Period: 5 and 10 years Entrepreneurial buyer looking to buy going-in yield or value-added opportunities; uses price per square foot, stabilized cap, and 10-year DCF as checks; no longer uses rent spikes in this market; uses face rents and reflects concessions when they are scheduled to occur.	2.0% to 3.0%	2.0% to 3.0%	2.0% to 3.0%	10.00% to 11.00%	2.0%	11.00% to 12.00%	10.00% to 12.00%	6	65.0%	5.0%	$0.20	6
INVESTMENT ADVISOR ■ Forecast Period: 5 to 10 years Relies on DCF and direct capitalization; contract rents above market are reduced to market for pricing; market is improving; Miami's Airport West, downtown, and Brickell Class-A markets are very strong; uses effective rents.	5.0% to 7.0% years 1-3; 4.0% thereafter	3.0% to 4.0%	3.0% to 4.0%	9.50% to 10.00%	2.0%	10.50% to 12.00%	8.50% to 10.00%	4 to 8	75.0% to 80.0%	5.0% of noncredit space	$0.15	4
LIFE INSURANCE COMPANY ■ Forecast Period: 10 years Uses DCF only; applies rent spike in years 1 and 2 in most submarkets, amount is determined on a case-by-case basis.	3.0% to 4.0%	3.0%	3.0%	9.25% to 9.50%	2.0% to 4.0%	10.50% to 11.75%	—	3 to 6	70.0%	6.0% to 10.0%	$0.20 to $0.30	6 to 9
DOMESTIC PENSION FUND ■ Forecast Period: 3, 5, 7, and 10 years Uses both DCF and direct capitalization; in direct cap, capitalizes NOI after capital replacement reserve but before TIs and leasing commissions; uses effective rents after all concessions are extracted; applies 5.0% to 10.0% rent spike in early years; target IRR is 12.00%+ on development deals.	3.0% to 5.0%	3.0%	3.0%	9.00% to 10.00%	2.0%	10.50% to 12.00%+	9.00%+	6 to 9	70.0% to 75.0%	5.0%	$0.10 to $0.20	Varies
LIFE INSURANCE COMPANY ■ Forecast Period: 5 to 8 years Uses DCF and direct capitalization; also looks at discount to replacement cost; relies on DCF; in direct cap, capitalizes NOI after capital replacement reserve but before TIs and leasing commissions; uses face rents and reflects concessions when they are scheduled to occur; typical concessions still include three to six months free rent and generous TIs.	3.0%	3.0% to 4.0%	2.0%	9.50% to 11.00%	2.0%	11.00% to 12.00%	8.00% to 10.00%	6	60.0%	4.0%	$0.25	6 to 9
REAL ESTATE ADVISOR ■ Forecast Period: 10 years Interested in properties that are "value added" opportunities; uses both DCF and direct capitalization; occasionally applies 5.0% to 7.0% rent spike in year 3 or 4 in some markets; uses face rents and reflects concessions when they are scheduled to occur.	2.0% to 5.0%	3.5%	—	9.50%	2.0% to 2.5%	10.00% to 10.50%	9.50% to 10.00%	6 to 9	50.0% to 70.0%	5.0% to 7.0%	$0.20 to $0.25	9 to 12
LIFE INSURANCE COMPANY ■ Forecast Period: 10 years Relies on DCF; also uses direct capitalization and sales comparison approaches as secondary analytical tools; uses face rents; use of rent spikes is minimal but may apply in year 1; amount of spike is determined on a case-by-case basis.	3.0%	3.0%	3.0%	9.25% (Class A) to 10.50% (Class B)	2.0% to 4.0%	10.75% to 11.75%	9.00% to 9.50%	3 to 6	70.0%	8.0% to 12.0%	$0.20 to $0.30	6 to 24

Washington, DC Office Market

INVESTOR SURVEY RESPONSES*

FIRST QUARTER 1999

*Representative sample; due to space constraints, not all responses are included.

Source: Personal survey conducted by The Korpacz Company, Inc. during January 1999.

	CHANGE RATES			RESIDUAL		DISCOUNT RATE (IRR)	OVERALL CAP RATE (OAR)	VACANCY ASSUMPTIONS			RESERVE	MARKETING TIME
	Market Rent	Expenses	CPI	Cap Rate	Selling Expense	Free & Clear	Free & Clear	Months Vacant	Tenant Retention	Underlying Vacancy & Credit Loss	Per Square Foot	Months
INVESTMENT BANKER ■ Forecast Period: 10 years Active market; little new construction except for build-to-suit; vacancy rate declining; uses face rents; underlying vacancy and credit loss includes rollover vacancy; prefers Golden Triangle and East End submarkets.	3.5%	3.0%	3.0%	8.00% to 9.00%	2.0%	10.00% to 11.50%	7.00% to 9.00%	8	75.0%	2.0% to 5.0%	$0.10 to $0.20	6
DOMESTIC PENSION FUND ■ Forecast Period: 10 to 12 years Buys free and clear; average IRR consists of a 7.0% to 7.5% real rate of return plus the inflation rate; the indicated growth scenarios help to determine the sensitivity of investment to inflation; relies on DCF (IRR) and cap rates equally; use of face or effective rents varies by submarket.	0.0% for period of years; then 3%, 5% spike + inflation	2.0%/ 4.0%/ 6.0%	2.0%/ 4.0%/ 6.0%	8.00% to 9.00%	1.0% to 2.0%	11.00% to 11.50%	8.00% to 9.00%	6 to 9	60.0% to 70.0%	2.0%	$0.10 to $0.20	6 to 9
INSTITUTIONAL INVESTOR ■ Forecast Period: 10 years Uses both DCF and direct capitalization; in direct cap, capitalizes NOI before TIs, leasing commissions, and capital replacement reserve; prefers CBD and East End.	3.0% to 3.5%	3.0%	3.0%	10.00%	2.5%	12.00% to 13.00%	9.50%	6	70.0%	5.0% to 6.0%	$0.20	5
REAL ESTATE ADVISOR ■ Forecast Period: 5 and 10 years Buys turnaround situations as well as rotational plays in the suburbs; uses both DCF and direct capitalization; relies on DCF; applies 4.0% to 10.0% rent spikes in years 1 and 2 where there is evidence that they will occur; uses face rents in DCF model, net effective rents in direct capitalization.	0.0% to 10.0%	4.0%	4.0%	8.00% to 11.00%	1.5% to 2.0%	11.00% to 13.00%	8.00% to 11.00%	2 to 18	65.0%	8.0% to 14.0%	—	3 to 6
INVESTMENT ADVISOR ■ Forecast Period: 10 years Prefers free and clear properties with joint venture partner and preferred return; uses all valuation techniques and correlates; does not rely on any one technique; looks at components of NOI growth; uses face rents.	0.0% to 3.0%	3.5%	3.5%	8.50% to 10.00%	1.5%	11.00% to 12.50%	8.50% to 10.00%	4 to 6	60.0%	5.0% to 10.0%	$0.10 to $0.20	6 to 9
DOMESTIC PENSION FUND ■ Forecast Period: 7 years Relies on DCF (IRR), direct capitalization (initial cap rates), and price per square foot; uses effective rents.	3.0%	3.0%	3.0%	9.00% to 10.25%	2.0% to 3.0%	11.00% to 12.50%	8.75% to 9.50%	6 to 12	60.0%	2.0% to 3.0%	$0.15 to $0.20	12 to 18
INVESTOR ■ Forecast Period: 3 to 5 years and 10 years Uses DCF and direct capitalization; in direct cap, capitalizes NOI before TIs, leasing commissions, and capital replacement reserve; uses face rents and reflects concessions when they are scheduled to occur.	3.0% to 3.5%	3.0%	3.0%	10.00% to 10.50%	3.0%	11.00% to 13.00%	9.00% to 11.00%	6	60.0% to 70.0%	5.0% to 10.0%	$0.15 to $0.25	6 to 9
INSTITUTIONAL INVESTOR ■ Forecast Period: 10 years Relies on DCF; market rent growth rates vary according to supply-demand balance in specific submarket; applies rent spikes as warranted by market conditions and specific property; uses present value analysis of effective rents.	Varies per submarket until stabilized; thereafter at inflation rate	2.0% to 3.5%	2.0% to 3.5%	9.00% to 10.00%	2.0% to 3.0%	11.00% to 11.75%	9.00% to 9.75%	3 to 6	50.0% to 60.0%	1.0% to 3.0%	$0.10 to $0.20	3 to 9

National Industrial Market

INVESTOR SURVEY RESPONSES*

FIRST QUARTER 1999

*Representative sample; due to space constraints, not all responses are included.

Source: Personal survey conducted by The Korpacz Company, Inc. during January 1999.

	CHANGE RATES			RESIDUAL		DISCOUNT RATE (IRR)	OVERALL CAP RATE (OAR)	VACANCY ASSUMPTIONS			RESERVE	MARKETING TIME
	Market Rent	Expenses	CPI	Cap Rate	Selling Expense	Free & Clear	Free & Clear	Months Vacant	Tenant Retention	Underlying Vacancy & Credit Loss	Per Square Foot	Months
INVESTMENT ADVISOR ■ Forecast Period: 10 to 15 years Prefers free and clear properties; relies on DCF (IRR), direct capitalization (initial cap rates), and price per square foot; total vacancy and credit loss including rollover vacancy is 5.0% to 7.0%; uses actual rents and reflects concessions as they occur.	Years 1-3 varies per market; 3.0% thereafter	3.0%	3.0%	8.50% to 10.00%	2.0% to 4.0%	10.50% to 12.00%	8.00% to 10.00%	6 to 12	60.0% to 70.0%	2.0% to 3.0%	$0.10 to $0.15	6 to 9
DOMESTIC PENSION FUND ■ Forecast Period: 10 years Prefers to buy free and clear; uses all valuation techniques.	3.0%	3.0%	3.0%	9.00% to 10.00%	2.0% to 3.0%	11.00% to 11.50%	8.75%	6 to 9	60.0%	5.0%	$0.15	6 to 9
INVESTMENT ADVISOR ■ Forecast Period: 10 years Prefers free and clear; relies on direct capitalization (initial cap rates), price per square foot, and DCF (IRR) and equity cap rates equally; hard to find in bulk (250,000 square feet or more); uses face rents.	2.0% to 4.0%	3.5%	3.5%	9.00% to 10.00%	1.5%	11.00% to 12.00%	8.50% to 9.50%	4 to 6	65.0%	4.0% to 8.0%	$0.10 to $0.15	6 to 9
DOMESTIC PENSION FUND ■ Forecast Period: 10 to 12 years Strongest market; buys free and clear only; average IRR consists of a 7.0% to 7.5% real rate of return, plus the inflation rate; the three indicated growth scenarios help to determine sensitivity of investment to inflation; relies on DCF (IRR) and initial cap rates equally; use of face or effective rents varies by market.	Years 1-3 varies per market; thereafter at inflationary rate	2.0%/ 4.0%/ 6.0%	2.0%/ 4.0%/ 6.0%	9.00% to 9.50%	2.0%	11.00% to 11.50%	9.00% to 10.00%	6 to 9	60.0%	2.0% to 5.0%	$0.10 to $0.20	6 to 9
REAL ESTATE ADVISOR ■ Forecast Period: 10 to 12 years Good market; continuing interest — more stress on supply/demand, etc.; relies on DCF (IRR), direct capitalization (initial cap rates), and price per square foot; emphasis on average cash-on-cash rates, more realistic; credit loss, downtime, free rent, TIs, and annual capital reserve; a lot of interest in this market but also very cautious; more concerned with the resale estimate — stabilized income, full selling commissions, full legal expenses, and real estate tax adjustment.	3.0% to 5.0%	3.0% to 4.0%	3.0% to 4.0%	9.00% to 10.00%	2.0% to 5.0%	10.50% to 12.00%	8.50% to 10.00%	6 to 12	50.0% to 60.0%	3.0% to 5.0%	—	6
REIT ■ Forecast Period: 10 years Uses both DCF and direct capitalization; in direct cap, capitalizes NOI before TIs, leasing commissions, and capital replacement reserve; uses effective rents after all concessions are extracted.	3.0%	3.0%	2.0%	—	2.0%	10.75%	8.25% to 10.00%	6	70.0%	7.0%	$0.05	5
REIT ■ Forecast Period: 7 years Uses both DCF and direct capitalization; in direct cap, capitalizes NOI before TIs, leasing commissions, and capital replacement reserve.	3.0%	3.0%	3.0%	11.00%	3.0%	11.75%	10.25%	6 to 9	70.0%	5.0%	$0.10 to $0.15	—
PENSION FUND ADVISOR ■ Forecast Period: 10 to 14 years Uses both DCF and direct capitalization; in direct cap, capitalizes NOI before TIs, leasing commissions, and capital replacement reserve; vacancy assumption is 5.0% total including lag on noncredit tenants plus 1.0% to 2.0% credit loss.	3.5%	3.5%	3.5%	9.00% to 9.50%	1.5% to 5.0%	10.50% to 11.50%	8.50% to 9.50%	—	70.0%	1.0% to 2.0%	$0.10 to $0.15	2

National Apartment Market

INVESTOR SURVEY RESPONSES*

FIRST QUARTER 1999

*Representative sample; due to space constraints, not all responses are included.

Source: Personal survey conducted by The Korpacz Company, Inc. during January 1999.

	CHANGE RATES		VACANCY	RESIDUAL		DISCOUNT RATE (IRR)	OVERALL CAP RATE (OAR)	RESERVE	MARKETING TIME
	Market Rent	Expenses	Total Vacancy	Cap Rate	Selling Expense	Free & Clear	Free & Clear	Per Unit	Months
DOMESTIC PENSION FUND ■ Forecast Period: 10 years Strong balanced market; groups leases by expiration dates for DCF analysis; typical NOI ratio is 60.0%; uses face rents since concessions are typically minor; leasing fees are in addition to a 4.0% management fee; relies on direct capitalization; uses DCF as a test.	4.0%	2.0%/ 4.0%/ 6.0%	5.0%	8.75% to 9.50%	2.0%	11.00% to 11.50%	8.50% to 9.00%	$150 to $250	3 to 4
REAL ESTATE ADVISOR ■ Forecast Period: 10 years Continuing positive interest—people represent real demand; strong market; supply and demand in balance; groups leases by expiration dates for DCF analysis; management fee ranges from 3.0% to 5.0%; relies on DCF, direct capitalization, and sales comparison; emphasis on average cash-on-cash rates, more realistic credit loss, downtime, free rent, TIs, and annual capital reserve.	0.0% to 3.0%	3.0% to 4.0%	3.0% to 5.0%	9.00% to 10.00%	3.0%+	11.00% to 12.00%	8.50% to 9.50%	Specific by component, cost & life expectancy	6
DOMESTIC PENSION FUND ■ Forecast Period: 1 and 10 years Uses both DCF and direct capitalization; in direct cap, capitalizes NOI after capital replacement reserve; reflects concessions as they occur; may burn off on new property during lease-up period in *strong* market.	3.0% to 3.5%	3.0% to 3.5%	5.0% to 10.0%	8.00% to 10.00%	—	10.00% to 12.00%	7.50% to 9.50%	$200 to $400	6 to 9
DOMESTIC PENSION FUND ■ Forecast Period: 7 years Strong interest in this product nationwide; applies management fee of 3.0% to 4.0%; uses DCF and direct capitalization; emphasis is on initial returns.	2.0% to 3.0%	3.0%	5.0% to 7.0%	9.00% to 10.50%	2.0% to 3.0%	11.50%	8.00% to 9.00%	$300	6
INVESTMENT ADVISOR ■ Forecast Period: 5 to 10 years Good product for diversified portfolio, groups leases by expiration dates for DCF analysis; uses management fee of 4.0%; average NOI ratio is 40.0% to 50.0%; relies on direct capitalization and uses DCF to calculate yield.	Years 1-3 varies per market; 3.0% thereafter	3.0%	5.0% to 10.0%	8.00% to 10.00%	2.0% to 3.0%	10.50% to 12.00%	7.50% to 9.50%	$200 to $300	6 to 9
REAL ESTATE ADVISOR ■ Forecast Period: 5 and 10 years Relies on DCF, also uses direct capitalization; residual cap rate is 25 basis points over the going-in cap rate on a 5-year holding period, 50 basis points over the going-in cap rate on a 10-year holding period.	3.0% to 3.5%	3.5%	6.0% to 8.0%	9.25% to 9.75%	2.5%	10.75% to 11.50%	8.75% to 9.25%	$200 to $250+ $100 to $150 for capital improvements	6
PENSION FUND ADVISOR ■ Forecast Period: 10 years Uses both DCF and direct capitalization; in direct cap, capitalizes NOI after capital replacement reserve deduction; buys 150- to 400-unit apartment complexes in first-and second-tier markets nationwide.	3.0%	3.0%	5.0% to 7.0%	9.00% to 10.00%	1.5%	11.00% to 12.50%	7.75% to 9.00%	$200 to $250	3
PENSION FUND ADVISOR ■ Forecast Period: 7 to 10 years Specializes in this market; increases annual rent in lieu of lease-by-lease analysis; uses management fee of 4.0% plus leasing costs and reserve (actually funded); relies on direct capitalization primarily; also uses sales comparison and cost; more equity and debt are flowing to this market; sees signs of overbuilding of new deluxe product.	0.0% to 2.0%	3.5%	6.0% to 8.0%	8.25% to 9.00%	2.0%	10.00% to 11.00%	7.75% to 8.50%	$200 to $250	4
INVESTMENT ADVISOR ■ Forecast Period: 10 years Specializes in this market; relies equally on DCF and direct capitalization; IRR may be as high as 12.00% in very weak markets; reserve amount depends on age and/or conditions, typically $150 per unit for new properties, $300 per unit for those over 10 years old.	3.0% to 3.5%	3.0% to 3.5%	5.0% to 10.0%	8.50% to 9.50%	2.0% to 3.0%	11.00% to 11.50%	7.75% to 9.00%	$150 to $300	3
REIT ■ Forecast Period: 10 years Uses both DCF and direct capitalization; in direct cap applies OAR to NOI after capital replacement reserve deduction; acquisitions are in the Western region of the United States.	3.0%	3.0%	5.0%	9.25%	2.0% to 3.0%	11.00% to 12.00%	8.75%	$200	4 to 8
REAL ESTATE ADVISOR ■ Forecast Period: 10 years Prefers newer suburban garden complexes in mature, stable markets; uses both DCF and direct capitalization; relies on DCF; in direct cap, capitalizes NOI after capital replacement reserve deduction.	2.5%	3.0%	6.0% to 8.0%	9.25%	3.0%	10.50% to 11.00%	8.75% to 9.50%	$250 to $400	9 to 12

Korpacz

National Full-Service Hotel Market

INVESTOR SURVEY RESPONSES*

FIRST QUARTER 1999

*Representative sample; due to space constraints, not all responses are included.

Source: Personal survey conducted by The Korpacz Company, Inc. during January 1999.

	CHANGE RATES		RESIDUAL			DISCOUNT RATE (IRR)	OVERALL CAP RATE (OAR)	GROSS ROOM REVENUE MULTIPLIER	MANAGEMENT FEES	RESERVE FOR REPLACEMENT OF FIXED ASSETS	MARKETING TIME
	Average Daily Rate	Operating Expenses	Cap Rate	Year Capped	Selling Expense	Free & Clear	Free & Clear	GRRM	Base Fee	Percent of Total Revenues	Months
REIT ■ Forecast Period: 10 years Focuses on large MSA markets such as New York, Los Angeles, San Francisco, Chicago, Seattle, as well as resort destinations; uses both DCF and direct capitalization; in DCF, forecasts 3.0% to 5.0% initial average daily rate but 5.0% to 10.0% if repositioning; in direct cap, capitalizes both prior 12 months and forecast next 12 months income.	3.0% to 10.0%	3.0%	10.00% to 12.00%	10	3.0%	12.00% to 15.00%	—	—	3.0%	4.0%	—
LIFE INSURANCE COMPANY ■ Forecast Period: 10 years Uses both DCF and direct capitalization; in direct cap, capitalizes forecast next 12 months income.	3.0% to 6.0%	3.0%	10.00% to 12.00%	11	2.0% to 4.0%	10.00% to 11.50%	8.50% to 10.00%	Does not use	3.0% to 6.0%	4.0% to 6.0%	4 to 12
REAL ESTATE ADVISOR ■ Forecast Period: 5 years Buys nationwide; uses both DCF and direct capitalization; relies on DCF but is sensitive to market rates; growth rates are specific to the market; forecasts demand growth from the fundamental demand side based on forecast growth in room rate demand and models the mix of four different sources of business, each of which typically has a different rate.	2.0%	4.0%	9.50% to 11.00%	6	1.0%	12.00% to 15.00%	10.00% to 13.00%	—	Varies	5.0% to 8.0%	2 to 3
REAL ESTATE ADVISOR ■ Forecast Period: 10 years Interested in full-service and luxury due to better opportunity for growth than economy/limited-service product; uses both DCF and direct capitalization; may use base or incentive management fee, with incentive fee very property specific; in direct cap, usually caps forecast next 12 months; prefers hotels in major markets with good job growth, regional and local room demand, major business travel centers, submarkets convenient to major airports.	Varies per market	3.0% to 4.0%	10.00% to 11.00%	11	2.0% to 3.0%	12.00% to 16.00%	9.00% to 11.75%	Does not use	2.5% to 4.0%	3.0% to 5.0%	6 to 12
REIT ■ Forecast Period: 5 years Relies on direct capitalization; capitalizes prior 12 months income.	4.0% to 8.0%	3.0%	9.50% to 10.50%	10 or 11	3.0%	—	12.00%	Does not use	2.0%	3.0%	—
HOTEL OWNER-OPERATOR-FRANCHISOR ■ Forecast Period: 10 years Seeks opportunities nationwide; uses both DCF and direct capitalization; initial average daily rate growth rate in stabilized markets where supply and demand are near equilibrium is close to the CPI; selling expense depends on size and value of the property.	3.5% to 4.5%	3.0%	9.00% to 11.00%	11	2.0%	12.00% to 14.00%	8.00% to 9.50%	Does not use	3.0%; uses base + incentive in some cases	4.0% to 6.0%	3 to 6
LIFE INSURANCE COMPANY ■ Forecast Period: 10 years Prefers well-located properties in growing suburbs and airport markets with potential to turn around and add value.	3.0% to 4.0%	3.0%	10.00% to 10.50%	11	1.0% to 2.0%	13.00% to 14.00%	9.50% to 10.00%	—	2.0% to 3.0%; 0.05% to 10.0% incentive fee	4.0% to 5.0%	1 to 6
PRIVATE HOTEL COMPANY ■ Forecast Period: 10 years Uses both DCF and direct capitalization; in direct cap, capitalizes forecast next 12 months income; prefers West, Northeast, and Southeast.	4.0%	4.0%	10.00%	10	2.0%	9.00% to 10.00%	—	—	3.0%; 10.0% AGOP incentive fee	4.0%	—
PENSION FUND ADVISOR ■ Forecast Period: 7 years Uses both DCF and direct capitalization; in direct cap, capitalizes prior 12 months income; prefers California (both Northern and Southern), Arizona, Seattle, Chicago, New York, and Mid-Atlantic region.	5.0% to 6.0%	3.0% to 10.0%	8.00% to 12.00%	8	2.0% or $ specific	13.00% to 14.50%	8.00% to 9.00%	3 to 4	2.0%; 1.5% incentive fee	5.0%	4

National Economy/Limited-Service Hotel Market

INVESTOR SURVEY RESPONSES*

FIRST QUARTER 1999

*Representative sample; due to space constraints, not all responses are included.

Source: Personal survey conducted by The Korpacz Company, Inc. during January 1999.

	CHANGE RATES		RESIDUAL			DISCOUNT RATE (IRR)	OVERALL CAP RATE (OAR)	GROSS ROOM REVENUE MULTIPLIER	MANAGEMENT FEES	RESERVE FOR REPLACEMENT OF FIXED ASSETS	MARKETING TIME
	Average Daily Rate	Operating Expenses	Cap Rate	Year Capped	Selling Expense	Free & Clear	Free & Clear	GRRM	Base Fee	Percent of Total Revenues	Months
HOTEL OWNER-OPERATOR-FRANCHISOR ■ Forecast Period: 5 to 10 years Criteria are for new mid-scale hotels with restaurants being developed nationwide; uses both DCF and direct capitalization; initial average daily rate growth rate in stabilized markets where supply and demand are near equilibrium is close to the CPI; selling expense depends on size and value of the property.	3.0%	3.0%	11.00% to 12.00%	6 to 11	3.0%	14.00% to 16.00%	11.00%	Does not use	3.0%; uses base + incentive in some cases	4.0%	3 to 6
HOTEL OWNER-MANAGER ■ Forecast Period: 3 years Focuses on direct capitalization; in direct cap, capitalizes prior 12 months income; prefers Midwest, South, and Northwest.	2.0% to 3.0%	60.0% of revenues	12.00%	—	—	—	12.00%	—	3.0%; 10.0% of distribution incentive fee	4.0%	4
PRIVATE HOTEL COMPANY ■ Forecast Period: 10 years Prefers Northeast, Southeast, and Southwest; uses both DCF and direct capitalization; in direct cap, capitalizes forecast next 12 months income.	4.0%	4.0%	11.00%	10	2.0%	10.00%	—	—	3.0%; 10.00% AGOP incentive fee	4.0%	—
PENSION FUND ADVISOR ■ Forecast Period: 7 years Uses both DCF and direct capitalization; in direct cap, capitalizes prior 12 months income; prefers California, Denver, Seattle, Midwest (Chicago), East Coast to New York.	3.0%	2.0% to 4.0%	12.00%	8	3.0% to 5.0%	13.00% to 15.00%	10.50%	2.0 to 2.5	3.0%; 1.0% to 2.0% incentive fee	4.0%	6
HOTEL MANAGEMENT COMPANY ■ Forecast Period: 3 to 5 years Uses both DCF and direct capitalization; in direct cap, capitalizes prior 12 months income; prefers Texas, Florida, and Denver.	3.0% to 4.0%	3.0%	11.00% to 12.00%	5	2.0% to 3.0%	15.00%	11.00% to 11.50%	Does not use	5.0%; 15.0% of cash flow in excess of owner's priority incentive fee	5.0%	6 to 12
MORTGAGE BANKER ■ Forecast Period: 10 years Uses both DCF and direct capitalization; in direct cap, capitalizes forecast next 12 months income; prefers West and Northwest.	2.0% to 4.0%	3.0% to 4.0%	12.00%	11	3.0% to 4.0%	15.00%	11.50% to 12.00%	2.5 to 3.5	3.0% to 4.0%; deal-specific incentive fee	4.0% to 5.0%	6 to 12
HOTEL COMPANY ■ Forecast Period: 5 to 10 years Uses both DCF and direct capitalization; in direct cap, capitalizes forecast next 12 months income; prefers Northeast and West.	3.0% to 10.0%	2.0% to 3.5%	10.50% to 12.00%	6 to 11	2.0% to 4.0%	14.00% to 16.00%	10.00% to 11.50%	Does not use	3.0% to 5.0%	3.0% to 5.0%	3 to 6

Korpacz

National Luxury Hotel Market

INVESTOR SURVEY RESPONSES*

FIRST QUARTER 1999

*Representative sample; due to space constraints, not all responses are included.

Source: Personal survey conducted by The Korpacz Company, Inc. during January 1999.

	CHANGE RATES		RESIDUAL			DISCOUNT RATE (IRR)	OVERALL CAP RATE (OAR)	GROSS ROOM REVENUE MULTIPLIER	MANAGEMENT FEES	RESERVE FOR REPLACEMENT OF FIXED ASSETS	MARKETING TIME
	Average Daily Rate	Operating Expenses	Cap Rate	Year Capped	Selling Expense	Free & Clear	Free & Clear	GRRM	Base Fee	Percent of Total Revenues	Months
REAL ESTATE ADVISOR ■ Forecast Period: 10 years Interested in full-service and luxury due to better opportunity for growth than economy/limited-service product; uses both DCF and direct capitalization; may use base or incentive management fee, with incentive fee very property specific; in direct cap, usually caps prior 12 months; prefers hotels in major markets with good job growth, regional and local room demand, major business travel centers, submarkets convenient to major airports.	3.0% to 5.0%	3.0% to 5.0%	10.00% to 11.50%	11	2.0% to 3.0%	13.00% to 16.00%	9.25% to 12.25%	Does not use	2.5% to 4.5%	3.0% to 5.0%	6 to 12
HOTEL OWNER-OPERATOR-FRANCHISOR ■ Forecast Period: 10 years Criteria are for upscale and resort hotels; seeks opportunities nationwide; uses both DCF and direct capitalization; initial average daily rate growth rate in stabilized markets where supply and demand are near equilibrium is close to the CPI; selling expense depends on size and value of the property.	3.5% to 4.5%	3.0%	9.00% to 10.00%	11	2.0%	12.00% to 14.00%	8.00% to 9.50%	Does not use	3.0%; uses base + incentive in some cases	4.0% to 6.0%	6
LIFE INSURANCE COMPANY ■ Forecast Period: 7 to 10 years Uses both DCF and direct capitaliation; in direct capitalization, may capitalize trailing 12 months income or forecast 12 months on a case-by-case basis.	3.5%	3.0%	9.50% to 10.00%	11	2.0%	11.50% to 13.00%	9.00% to 10.00%	—	2.5% to 3.0%	4.0% to 5.0%	—
LIFE INSURANCE COMPANY-PENSION FUND ■ Forecast Period: 10 years Uses both DCF and direct capitalization; in direct cap, capitalizes forecast next 12 months income; prefers major urban and resort markets.	3.5%	3.0%	10.00% to 10.25%	11	1.0% to 2.0%	11.00% to 12.50%	9.50%	Does not use	3.0%	4.0%	—
PRIVATE HOTEL COMPANY ■ Forecast Period: 10 years Uses both DCF and direct capitalization; in direct cap, capitalizes forecast next 12 months income.	4.0%	4.0%	9.50%	10	2.0%	9.00% to 10.00%	—	—	3.0%; 10.0% AGOP incentive fee	4.0%	4
PENSION FUND ADVISOR ■ Forecast Period: 5 to 7 years Uses both DCF and direct capitalization; in direct cap, capitalizes prior 12 months income; prefers West Coast, East Coast, and Midwest.	6.0% to 10.0%	3.0% to 4.0%	7.00% to 9.00%	6 to 8	2.0%	12.00% to 14.00%	7.50% to 8.00%	3 to 6	1.5% to 2.0%; 1.0% to 3.0% incentive fee	8.0%	4
REIT ■ Forecast Period: 5 years Uses both DCF and direct capitalization; in direct cap, capitalizes both prior 12 months income and forecast next 12 months; OAR is 8.00% to 9.00% on prior 12 months and 10.00% to 11.00% on forecast income; prefers urban resort and convention markets.	4.0% to 6.0%	1.0% to 3.0%	9.50% to 10.00%	6	1.5% to 2.0%	13.00% to 15.00%	8.00% to 9.00%	Does not use	1.0% to 2.5%	4.0% to 5.0%	4
HOTEL OWNER-INVESTOR ■ Forecast Period: 5 to 7 years Uses both DCF and direct capitalization; in direct cap, capitalizes prior 12 months income; prefers top 50 urban MSA markets.	4.0% to 6.0%	3.0%	10.50%	5 to 7	1.5% to 2.0%	13.50% to 14.00%	10.00%	Does not use	3.0%	4.0%	6
MORTGAGE BANKER ■ Forecast Period: 10 years Uses both DCF and direct capitalization; in direct cap, capitalizes prior 12 months income; prefers North and Northwest.	5.0% to 6.0%	3.0% to 4.0%	9.50%	11	2.0% to 3.0%	12.00% to 13.00%	9.00%	Does not use	2.0% to 3.0%	4.0% to 5.0%	6
INVESTMENT BANKER ■ Forecast Period: 1 year Uses direct capitalization based on a one-year pro forma; growth rates depend on market and position of hotel within the market.	Varies	Varies	—	—	—	—	6.00% to 10.00%	Does not use	3.0%	3.0% to 4.0%	6

National Extended-Stay Hotel Market

INVESTOR SURVEY RESPONSES*

FIRST QUARTER 1999

*Representative sample; due to space constraints, not all responses are included.

Source: Personal survey conducted by The Korpacz Company, Inc. during January 1999.

	CHANGE RATES		RESIDUAL			DISCOUNT RATE (IRR)	OVERALL CAP RATE (OAR)	GROSS ROOM REVENUE MULTIPLIER	MANAGEMENT FEES	RESERVE FOR REPLACEMENT OF FIXED ASSETS	MARKETING TIME
	Average Daily Rate	Operating Expenses	Cap Rate	Year Capped	Selling Expense	Free & Clear	Free & Clear	GRRM	Base Fee	Percent of Total Revenues	Months
HOTEL DEVELOPER-MANAGER-OWNER ■ Forecast Period: 3 years All hotels are new construction; uses both DCF and direct capitalization; in DCF expects 15.00% yield upon stabilization; in direct cap, applies a 30.00% OAR to income and capital proceeds from debt and sale over a 3- to 5-year period; prefers Northern California and Pacific Northwest markets with barriers to entry.	5.0%	3.5%	10.50%	3	2.0%	15.00%	—	—	3.5%; 10.00% of incremental cash flow over hurdle	2.0% to 4.0%	12
HOTEL OWNER-OPERATOR-FRANCHISER ■ Forecast Period: 5 to 10 years Uses both DCF and direct capitalization; in direct cap, capitalizes forecast next 12 months income.	3.0%	3.0%	10.00% to 11.00%	6 to 11	2.0% to 3.0%	13.00% to 15.00%	10.00%	Does not use	3.0%; uses base + incentive in some cases	4.0%	6
HOTEL MANAGEMENT COMPANY ■ Forecast Period: 5 years Uses both DCF and direct capitalization; in direct cap, capitalizes prior 12 months income; prefers Texas, Colorado, Utah, Florida; focuses on upscale extended stay not economy products.	4.0% to 5.0%	3.0% to 3.5%	11.00% to 11.50%	5	2.0%	14.00% to 14.50%	11.00%	Does not use	3.0%; 15.0% of cash flow in excess of owner's priority incentive fee	4.0% to 5.0%	6 to 9
MORTGAGE BANKER ■ Forecast Period: 10 years Uses both DCF and direct capitalization; in direct cap, capitalizes forecast next 12 months income; prefers West and Northwest.	3.0% to 4.0%	3.0% to 4.0%	11.50%	11	3.0% to 4.0%	14.00% to 15.00%	11.00% to 11.50%	Does not use	3.0% to 4.0%	4.0% to 5.0%	6 to 9
MORTGAGE BANKER ■ Forecast Period: 5 to 10 years Uses both DCF and direct capitalization; in direct cap, capitalizes forecast next 12 months income; prefers Northeast.	3.0% to 10.0%	2.0% to 5.0%	10.50% to 12.50%	6 to 11	2.0% to 4.0%	14.00% to 16.50%	10.00% to 12.00%	Does not use	3.0% to 5.0%	3.0% to 5.0%	3 to 8
HOTEL COMPANY ■ Forecast Period: 1 year Uses direct capitalization based on a one-year pro forma; growth rates depend on market and position of hotel within the market; prefers major metro areas.	Varies	Varies	—	—	—	—	10.00% to 12.00%	Does not use	3.0%	3.0% to 5.0%	6
INVESTMENT BANKER ■ Forecast Period: 7 years Uses both DCF and direct capitalization; in direct cap, capitalizes prior 12 months income.	5.0%	2.5%	12.00%	7	2.0%	16.00%	11.00%	2.0	4.0%	4.0%	9

Investment and Property Market Characteristics: Office Markets

FIRST QUARTER 1999

Source: Personal survey conducted by The Korpacz Company, Inc. during January 1999.

	FORECAST VALUE CHANGE NEXT 12 MONTHS		PRICE AS % OF REPLACEMENT COST		STRUCTURAL VACANCY		YEARS TO STRUCTURAL VACANCY		TIs - NEW (PSF)		TIs - RENEWAL (PSF)	
Market	Range	Average	Range	Average	Range	Average	Range	Average	Range	Average	Range	Average
National CBD	2.00%-10.00%	5.79%	65.00%-110.00%	91.00%	4.00%-10.00%	7.88%	0-5	2.5	$10.00-$50.00	$27.92	$0.00-$20.00	$10.60
National Suburban	0.00%-10.00%	4.33%	85.00%-115.00%	97.75%	4.00%-8.00%	6.88%	0-3	1.1	$8.00-$30.00	$15.09	$4.00-$20.00	$7.18
Atlanta	0.00%-6.00%	1.92%	90.00%-110.00%	100.00%	6.00%-11.00%	8.00%	0-0	0	$5.00-$15.00	$10.50	$3.25-$7.00	$5.06
Chicago	0.00%-10.00%	3.00%	80.00%-110.00%	96.11%	2.00%-10.00%	6.39%	0-4	0.9	$10.00-$40.00	$22.50	$5.00-$20.00	$10.50
Dallas	0.00%-10.00%	5.33%	50.00%-110.00%	88.44%	5.00%-10.00%	6.40%	0-6	1.7	$8.00-$30.00	$15.17	$2.00-$15.00	$6.67
Houston	3.00%-15.00%	7.25%	50.00%-105.00%	83.50%	3.00%-10.00%	5.81%	0-4	1.3	$10.00-$30.00	$14.86	$2.00-$15.00	$6.36
Los Angeles	2.00%-10.00%	7.08%	75.00%-100.00%	86.43%	5.00%-10.00%	6.50%	1-3	2.5	$5.00-$30.00	$16.19	$0.00-$15.00	$5.81
Manhattan	3.00%-10.00%	7.88%	60.00%-90.00%	80.00%	5.00%-12.00%	8.42%	0-2	0.9	$30.00-$40.00	$36.67	$5.00-$20.00	$11.67
Pacific Northwest	(10.00%)-10.00%	2.95%	85.00%-110.00%	97.58%	3.00%-7.00%	5.20%	0-3	0.9	$5.00-$35.00	$16.64	$0.00-$15.00	$7.08
San Francisco	(5.00%)-10.00%	2.80%	70.00%-110.00%	98.00%	5.00%-10.00%	7.00%	0-0	0.0	$5.00-$30.00	$15.33	$0.00-$10.00	$4.30
Southeast Florida	2.00%-5.00%	3.33%	80.00%-110.00%	94.58%	5.00%-10.00%	6.50%	0-3	1.0	$12.00-$27.00	$16.60	$3.00-$15.00	$6.40
Washington, DC	0.00%-10.00%	3.64%	75.00%-110.00%	93.12%	4.00%-8.00%	6.52%	0-3	1.7	$0.00-$35.00	$18.33	$0.00-$15.00	$9.83

Investment and Property Market Characteristics: National Markets

FIRST QUARTER 1999

Source: Personal survey conducted by The Korpacz Company, Inc. during January 1999.

	FORECAST VALUE CHANGE NEXT 12 MONTHS		PRICE AS % OF REPLACEMENT COST		CLASS-A+ and A MALLS				CLASS-B+ and B MALLS				STABILIZED OCCUPANCY	
					IRRs		OARs		IRRs		OARs			
Market	Range	Average	Range	Average	Range	Average	Range	Average	Range	Average	Range	Average	Range	Average
Regional Mall	0.00%-10.00%	3.50%	80.00%-105.00%	88.80%	9.50%-12.50%	10.88%	7.00%-9.50%	7.94%	10.50%-13.50%	11.98%	7.00%-10.00%	9.35%	92.00%-99.00%	94.60% (Class-B to A+)
Power Center	0.00%-0.00%	0.00%	100.00%-100.00%	100.00%									90.00%-95.00%	93.40%
Strip Center	(3.00%)-10.00%	1.79%	80.00%-120.00%	97.95%									90.00%-98.00%	94.25%

					WAREHOUSE/DISTRIBUTION				R&D/FLEX							
					IRRs		OARs		IRRs		OARs		TIs - NEW (PSF/UNIT)		TIs - RENEWAL (PSF/UNIT)	
					Range	Average	Range	Average	Range	Average	Range	Average	Range	Average	Range	Average
Industrial	0.00%-10.00%	2.17%	80.00%-110.00%	98.00%	9.50%-12.50%	11.02%	8.00%-10.00%	9.03%	8.00%-14.00%	11.56%	8.00%-12.00%	9.80%	$0.00-$15.00	$3.97	$0.00-$8.00	$1.69
Apartment	0.00%-6.00%	2.42%	75.00%-120.00%	96.55%									$35.00-$350.00	$165.00	$0.00-$150.00	$50.00

Survey Process

Survey participants represent a cross section of major institutional equity real estate market participants who invest primarily in institutional-grade property. Initially, each participant is interviewed by telephone or in person regarding the cash flow assumptions used in analyzing real estate investment opportunities throughout the United States. Subsequent quarterly surveys are completed by mail with telephone follow-ups. Information is criteria applied in the quarter in which it is reported.

As a group, the survey participants collectively own, control, or acted as agent in 1998 transactions of institutional-grade real property assets with a total estimated value in excess of $200 billion. The minimum equity investment of the participants is from $5 million to $50 million (excluding hotel participants). Rates and other assumptions presented in this survey indicate participants' expectations from institutional-grade real property investment. They do not reflect performance of such property. The information is not generally applicable to investments that are not institutional grade. Although we do not represent that the survey is statistically accurate, the survey results provide important insight into the thinking of a significant part of the equity real estate marketplace.

Definitions

- **INSTITUTIONAL-GRADE REAL ESTATE**
  Real property investments that are sought out by institutional buyers and have the capacity to meet generally prevalent institutional investment criteria.
- **KORPACZ YIELD INDICATOR (KYI)**
  A composite IRR average of the surveyed markets
- **KORPACZ DIVIDEND INDICATOR (KDI)**
  A composite OAR average of the surveyed markets
- **MARKETING TIME**
  The period of time between the initial offering of a property for sale and the closing date of the sale
- **STRIP SHOPPING CENTER**
  Neighborhood or community center
- **RESPONDENT TYPE**
  Classification of survey participants into descriptive categories (e.g., domestic pension fund, REIT, investment advisor)
- **FORECAST PERIOD**
  Time for projection of anticipated cash flow benefits for discounted cash flow analysis
- **CHANGE RATE**
  Annual compound rate of change

  Market Rent
  Achievable current rent if vacant

  Expenses
  Total property expenses
- **RESIDUAL**
  Estimated total price at conclusion of forecast period

  Cap Rate
  Overall capitalization rate used in calculation of residual price

  Selling Expense
  Transaction expenses (legal, brokerage, marketing, etc.) paid by the seller
- **DISCOUNT RATE (IRR)**
  Internal rate of return in an all-cash transaction, based on annual year-end compounding; formerly termed the *free and clear equity IRR* in the Korpacz Survey
- **OVERALL CAPITALIZATION RATE (OAR)**
  Initial rate of return in an all-cash transaction; formerly termed the *free and clear equity cap rate* in the Korpacz Survey
- **VACANCY ASSUMPTIONS**
  Months Vacant
  The number of months a space remains unleased at the expiration of a vacating tenant lease

  Tenant Retention
  Percentage of leased rentable area that is expected to be re-leased by the existing tenants at lease expiration

  Underlying Vacancy/Credit Loss
  Percentage of total revenue uncollected due to unexpected vacancy or credit loss (in addition to any rent loss from vacancies at lease expirations)
- **NET OPERATING INCOME (NOI)**
  Income remaining after deduction of all property expenses. In direct capitalization, investors capitalize one of the following:
  1. NOI *after* capital replacement reserve deduction but *before* TIs and leasing commissions
  2. NOI *before* capital replacement reserve deduction, TIs, and leasing commissions
  3. Cash flow *after* capital replacement reserve deduction, TIs, and leasing commissions
- **REGIONAL MALL CLASSIFICATIONS**

Class	Retail Sales PSF
A+	$400 and up
A	$300 to $399
B+	$250 to $299
B	$200 to $249
C+	$150 to $199
C	$100 to $149
D	Less than $100

- **RESERVE**
  Amount allocated for periodic replacement of building components during a property's economic life
- **FULL-SERVICE HOTEL**
  Hotel with restaurant and lounge facilities, meeting space, and a minimum service and amenities level; moderate to lower upper-tier pricing; includes all-suite hotels
- **ECONOMY/LIMITED-SERVICE HOTEL**
  Hotel with "rooms only" operation and no food and beverage except possibly continental breakfast; lower-tier pricing
- **EXTENDED-STAY HOTEL**
  Hotel with rooms that generally include work stations with two-line phones, access to fax machines; mid- and upper-price hotels include kitchenettes, separate lounging area; weekly rates.
- **LUXURY HOTEL**
  High-quality hotel offering personalized guest services, typically with extensive amenities; upper-tier pricing; includes four- and five-star resorts
- **OPERATING EXPENSES (HOTEL)**
  The on-going expenditures incurred during the ordinary course of business necessary to maintain and continue the production of gross revenues, not including reserves, debt service, and capital costs
- **GROSS ROOMS REVENUE MULTIPLIER (GRRM)**
  The relationship, or ratio, between sale price and gross rooms revenue
- **MANAGEMENT FEE (HOTEL)**
  An expense item representing the sum paid for or the value of management service, excluding incentives, expressed as a percentage of total revenues
- **RESERVE FOR REPLACEMENT OF FIXED ASSETS (HOTEL)**
  An allowance that provides for the periodic replacement of building components, and furniture, fixtures, and equipment, which deteriorate and must be replaced during the building's economic life
- **RevPar**
  Revenue per available room

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Table H-2. **Average Replacement Reserves** (% of total revenue)
FIRST QUARTER 1999

MARKET	CURRENT QUARTER	THIRD QUARTER	YEAR AGO
Full-service hotels	4.25	4.33	—
CHANGE	—	–1.85%	—
Economy/Limited-service hotels	4.17	4.17	—
CHANGE	—	0.00%	—
Luxury hotels	4.50	4.70	—
CHANGE	—	–4.26%	—
Extended-stay hotels	4.00	4.03	—
CHANGE	—	–0.74%	—
All Markets Surveyed	4.23	4.31	—
(Simple Average)	—	–1.86%	—

Table H-3. **Average Management Fees** (% of total revenue)
FIRST QUARTER 1999

MARKET	CURRENT QUARTER	THIRD QUARTER	YEAR AGO
Full-service hotels	2.90	2.83	—
CHANGE	—	+2.47%	—
Economy/Limited-service hotels	3.61	3.50	—
CHANGE	—	+3.14%	—
Luxury hotels	2.81	2.63	—
CHANGE	—	+6.84%	—
Extended-stay hotels	3.50	3.25	—
CHANGE	—	+7.69%	—
All Markets Surveyed	3.21	3.05	—
(Simple Average)	—	+5.25%	—