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Commercial Real Estate Fundamentals Slip Sliding Away

With the U.S. unemployment rate now projected by Moody's to peak at 10.1% by the end of 2009 and credit still hard for investors to secure, there was little to cheer about during a quarterly media briefing Wednesday on the capital markets conducted by real estate research firm Reis. In short, vacancies in commercial real estate are likely to increase over the next 18 to 24 months with positive rent growth absent from the scene until 2012, or even later. "Investors will have to think longer about hold periods," Reis director of research Victor Calanog concluded, "and give up aspirations of a quick flip at triple the price in two to four years." Reis forecasts that the national office vacancy rate will reach 18% by year-end, the highest level since 1992, when overbuilding in the sector was rampant. The national office vacancy hit 16.3% in the first quarter, up from 15.5% in the previous quarter. Meanwhile, transaction volume measured across property types dropped 40.2% in the first quarter compared with the fourth quarter of 2008, and fell 74.2% year-over-year. In contrast to the 40.2% drop in transaction volume across all property types, office fared a bit better. By dollar volume, the value of the deals fell by just 7% in the first quarter. However, when excluding distressed sales — the John Hancock Tower in Boston, the former Bertelsmann building at 1540 Broadway and The New York Times headquarters and 10 Universal City Plaza in San Fernando Valley, Calif. — dollar volume actually dropped by 48%, not 7%. The drop-off in deal volume is much more pronounced in central business districts, where transactions occurred in just 11 of the 79 markets. In contrast, 40 out of 79 markets in non-CBD locations recorded office property deals. In short, investors have less tolerance in the current market to pay for relatively more expensive properties, said Calanog. For instance, 2008 transaction data shows that CBD office properties traded for \$366 per sq. ft. while non-CBD properties changed hands for \$193 per sq. ft. On a positive note, the price per square foot in the office sector increased 4.8% year-over-year, with three out of five regions registering positive growth, according to Reis. "It would be unwise to extrapolate these results across time and call a recovery, given continuing uncertainty in financial markets and near-term expectations of performance declines in the office sector," said Calanog. The national apartment vacancy rate is less alarming, but is still projected to peak at 8%, a level not seen since the late 1980s, according to Reis. The average capitalization rate, or initial return to the investor based on the purchase price, for multifamily hit 7.6% at the end of the first quarter nationally. That average includes deals with cap rates ranging from 10.8% to approximately 5% for gateway cities such as New York and San Francisco. While the decline in transaction volume in the apartment sector across all regions is in line with the office sector's 60% to 80% drop, Calanog noted that the apartment sector likely will recover sooner than the office sector. "With multifamily properties transacting at even lower prices this quarter, and possible recovery by 2010," he says, "investors willing to take the risk may want to use the remainder of 2009 to look for opportunities. In the retail sector, the news was grim for sellers. Reis projects that the average vacancy rate for neighborhood and community centers will rise to 10.8% by year's end, 11.8% in 2010 and more than 12% in 2012. In the first quarter, retail property cap rates ranged from 4.1% to 11.5% with Midwest neighborhood centers yielding an average cap rate of 9.9%. Nationally prices fell 20% in the first quarter from \$208 to \$167 per sq. ft. "The Southwest is the only region that registered positive growth [in sales prices]," said Calanog, "but once again we need to take this with a grain of salt." The caveat is that only 64 retail properties changed

hands in all of 2008 in the Southwest, and only nine traded in the first quarter of this year. By dollar volume, the decline in deals was more than 70% year-over-year. With the dearth of transactions, the federal government has introduced new programs such as the Term Asset-Backed Securities Loan Facility, or TALF, to ease liquidity and stimulate investment in commercial mortgage-backed securities. "Firms may either benefit from TALF via debt financing, or they might actually be able to raise money through equity offerings," said Calanog. "But will they use that money to invest in income-generating assets, or will they pay down debt? If it's the latter, then is deleveraging more about lack of faith in the recovery of credit markets in the near-term?" **(National Real Estate Investor/Sibley Fleming)**

NABE: Economists Forecast Modest Rebound Beginning in 3rd Quarter

A panel of 45 U.S. economists expects a "modest" economic rebound to begin in the second half of 2009, picking up steam in 2010, the National Association for Business Economics said Wednesday. "The panel ... [predicts] positive, albeit modest, growth in the third quarter, followed by steady improvement thereafter," the NABE outlook report said. "On the whole, however, the economic rebound lacks luster. Real GDP growth over the second half of 2009 is expected to average a well-below-trend 1.2 percent pace." The forecasters surveyed said growth in 2010 "is slated for a return to near its historical trend, with real GDP rising 2.7 percent on a fourth-quarter-to-fourth quarter basis. ... [But] next year's expected growth in GDP would be considerably more moderate than the typical rebound following a steep decline." The economists said that labor conditions nationwide "are expected to deteriorate further, with additional, but decreasing job losses through year-end." They predicted that the nation will have lost 4.5 million jobs by the end of 2009, driving the unemployment rate to 9.8 percent, but that the rate should ease to 9.3 percent by the end of 2010. In Colorado, unemployment has been trending between one and 1.5 percentage points lower than the national rate of 8.9 percent. The "NABE Outlook" report presents a consensus of macroeconomic expectations from a panel of 45 professional forecasters. The survey was taken Apr. 27-May 11. One of the forecasters on the panel -- although not necessarily agreeing with all of its conclusions -- is Colorado economist Jeff Thredgold of Thredgold Economic Associates and Vectra Bank. **(Denver Business Journal)**

Colo. Jobless Rate Down Slightly to 7.4 Percent

State labor officials say the seasonally adjusted unemployment rate in Colorado slipped a tenth of a percentage point to 7.4 percent in April, the first drop since October 2007. But Colorado Department of Labor and Employment Executive Director Donald Mares said Friday he expects continued job losses to push the rate up in coming months. One year ago, Colorado's jobless rate was 4.7 percent. The national unemployment rate was 8.9 percent in April. Labor officials say an estimated 2.5 million Coloradans were employed in April, down 62,900 from a year earlier. About 201,300 were looking for work, up 74,000 from April 2008. First-time filings for unemployment insurance through April have doubled compared with the first four months of last year, the labor department said. Not including seasonal shifts in the labor force, nonfarm employment in April was down 3.8 percent compared with a year ago to about 2.26 million jobs. The leisure and hospitality

sector lost about 4,600 jobs as ski season was winding down. The 900 jobs added in construction in April represented the first increase in the sector since June, but it was only about one-fourth of the number of jobs the sector usually adds in April, labor officials said. **(Denver Post)**

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Kidney-Care Giant DaVita Moving Executives to Denver

View Larger DaVita Inc., a Fortune 500 company and one of the largest kidney care providers in the United States, said Wednesday its CEO and several other top executives will relocate to the Denver area from its California headquarters. The move involves DaVita chairman and CEO Kent Thiry and an unspecified number of other top company officials currently based in El Segundo, Calif. DaVita said it does not currently plan to move any of its other 32,000 employees to Colorado, but said it will consider Denver its corporate headquarters. "We're very pleased to announce our search is over and we've selected the Denver area to make our home," Thiry said in a statement. DaVita (NYSE: DVA) operates about 30 outpatient kidney dialysis centers in Colorado and more than 1,400 nationwide in 43 states serving 700 hospitals. It already has about 800 employees in Colorado. DaVita in 2005 acquired Lakewood-based competitor Gambro Healthcare US, a unit of Gambro AP, which expanded the company's Colorado footprint. The date of the move and the exact location of the new office were not announced. In a statement, the company said it chose the Denver area for its executive relocation based on four factors: "The city's geographic location is ideal for a nationwide company with facilities and operations spread across nearly every state in the country; "The relative costs in the area are less expensive for families and companies alike; "Denver is widely considered to be a highly desirable place to live and work; and DaVita's significant existing presence in the region provides a solid foundation upon which the company can continue to grow." The company said it expects to save millions of dollars "over time" because of the move. DaVita ranks No. 433 on the 2009 Fortune 500 list. The magazine said it had 2008 revenues of \$5.7 billion and profits of \$374.2 million. Colorado currently is home to 11 companies on the latest Fortune 500 list, led by Qwest Communications International Inc. at No. 197. **(Denver Business Journal)**

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U.S. Consumer Confidence Up Dramatically

U.S. consumer confidence jumped in May to its highest level since September. The Conference Board Consumer Confidence Index now stands at 54.9, up from 40.8 in April. The index is based on a representative sample of 5,000 U.S. households. "Looking ahead, consumers are considerably less pessimistic than they were earlier this year, and expectations are that business conditions, the labor market and incomes will improve in the coming months," said Lynn Franco, director of the Conference Board Consumer Research Center. "While confidence is still weak by historical standards, as far as consumers are concerned, the worst is now behind us." Consumers' appraisal of the job market was also more favorable. Those claiming jobs are "hard to get" decreased to 44.7 percent from 46.6 percent in April. Those saying jobs are "plentiful" edged up to 5.7 percent from 4.9 percent. The employment outlook was also less pessimistic, with the percentage of consumers expecting more jobs in the months ahead increasing to 20 percent from 14.2

percent, while those anticipating fewer jobs decreased to 25.2 percent from 32.5 percent. **(Denver Business Journal)**

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	CURRENT	1 MONTH PRIOR	1 YEAR PRIOR
FED FUNDS RATE	.25	.25	2.00
3 MONTH LIBOR	.66	1.03	2.68
PRIME RATE	3.25	3.25	5.00
10 YEAR TREASURY	3.47	3.11	4.06
30 YEAR TREASURY	4.34	4.03	4.75

