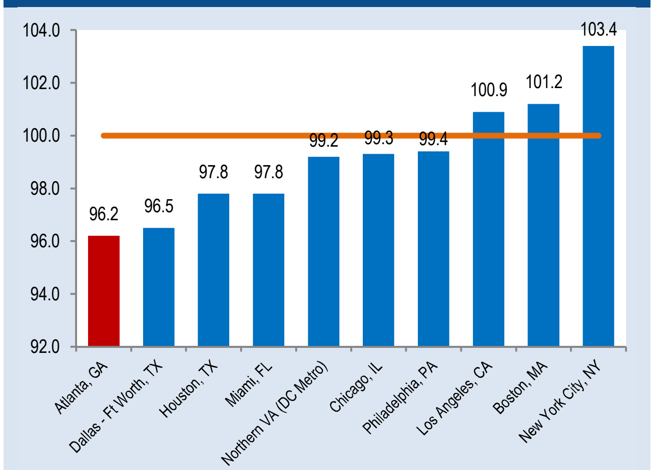
PCCP Market Commentary

Thinking About Unloved U.S. Markets

Fourth Quarter 2013

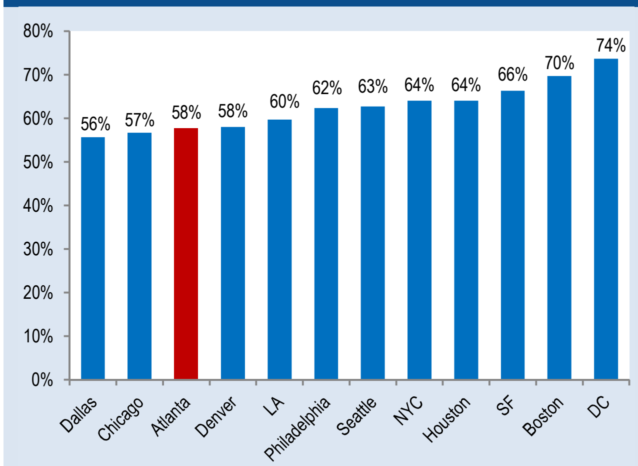
PCCP looks for attractive, mispriced investments. To make sure we cover the market, we proactively evaluate the performance of top MSAs and primary asset types to combine a "top-down" investment thesis with our "bottom-up" deal analysis. This approach leads us to the markets that have not yet been overrun by investment capital. (They can be hard to find!) In particular, we are intrigued by a top-10 U.S. city that has experienced economic recovery and significant job growth, but where CRE pricing lags fundamental improvements. We also find compelling another city that has had an annual population growth rate more than four times the average over the last 40 years, and yet prices for multifamily properties in the city remain less than 50% of peak values. Have you guessed the answers? Atlanta and Las Vegas. Here's our breakdown.

COST OF DOING BUSINESS INDEX – 10 LARGEST MSAS



Source: KPMG Competitive Alternatives: Guide to International Business Location, 2012

ATLANTA INSTITUTIONAL INVESTMENT: 2010 - 2012



Source: RCA

Atlanta became the seventh largest office market in the U.S.[1] without experiencing severe vacancies due to major corporate expansions. Atlanta ranks third in the U.S. in Fortune 500 headquarters.[2] Over 34% of residents have a college degree (which ranks the city 16th in the country[3]). Atlanta benefits from a self-reinforcing corporate activity cycle that attracts college graduates, creates high paying jobs, and keeps real estate well occupied. Additionally, Atlanta possesses the rare combination of infrastructure of a major city and low costs of the suburbs. KPMG ranked Atlanta as the lowest-cost business environment among the 10 largest cities in the country.[4]

Despite corporate demand drivers, supply is expected to remain constrained. Conservative office development costs of $375/SF demand $40/SF office rents. But the most prestigious submarkets currently command rents in the high $20s with only a few buildings north of $30. Institutional capital flows, both debt and equity, are also projected to stay restrained over the medium term, further limiting supply additions. Atlanta hasn't been discovered (yet) by global equity looking for core real estate opportunities. So we are still interested.

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[1] PPR Research Fourth Quarter 2012
[2] Fortune 500
[3] The Brookings Institute 2010
[4] KPMG Competitive Alternatives, Guide to International Business Location, 2012

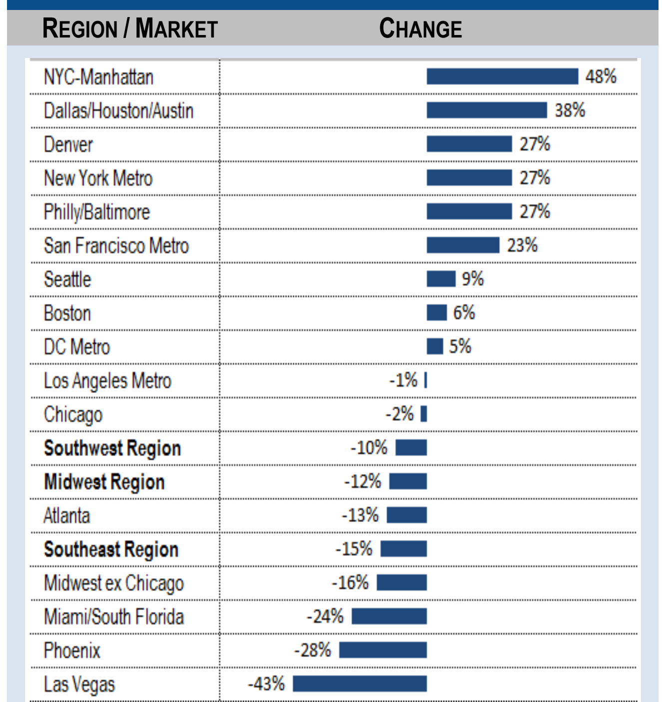
Job creation was very positive last year, with an addition of 51,600 new jobs (of which 40% were in the professional and business services sector - prime users of office space). Capitalizing on this, we have made two equity investments in Atlanta (a Class A suburban office complex purchased at foreclosure and a Class A- apartment recap averting a foreclosure.)

Las Vegas was one of the metropolitan areas most impacted during the downturn. Home prices declined 62%[5], unemployment skyrocketed to a high of 15.1% (U.S. peak: 10.0%)[6], and hotel & gaming revenue, essential to the local economy, fell 20%. The Las Vegas multifamily market experienced 30-year high vacancies at the end of 2009 of 9.3%, up from a low of 3.4% in 2006[7]. While these factors may appear to be a deterrent, let's remember that GDP is growing and travelers are on the road again. Recent momentum has started an apparent dramatic recovery in Las Vegas, with the unemployment rate decreasing 2.5 percentage points in just the last 12 months and the metro attracting 39.7 million visitors in 2012, breaking the 2007 record![8] As travelers once again return to Las Vegas and job growth rebounds from its lows, we expect annual population growth to return, fueling continued demand across all product types.

But let's focus on multifamily. Average asking rents have remained relatively low despite the strength of other fundamentals, increasing only 2.1% from recent lows and still 12.7% below the 2008 peak. In comparison, the PPR54's rents are now 4.5% *above* the prior record of 2007.[9] Occupancy has recovered swiftly (from 9.3% vacancy at the trough to 6.0% today), and rents must surely follow. On the supply side, Las Vegas has seen net additions of only 1,087 units over the last four years. In comparison, there were 1,080 net additions in the *single quarter* before the start of the recession (4Q 2007)[9]. Given the lack of new supply coupled with growing demand, we believe the Las Vegas apartment market is primed to outperform. So we are actively pursuing apartment deals in the region and if our pipeline holds, we'll be making investments.

We continue to believe that U.S. commercial real estate distress and de-levering is an on-going process. Opportunities remain for investors who are willing to dig in on fundamentals and avoid markets overheated by investors bidding up core real estate.

MULTIFAMILY PRICING – PEAK VALUES TO NOW



Source: Real Capital Analytics

William R. Lindsay
wlindsay@pccpllc.com
(310) 414-7868

Yon Cho
ycho@pccpllc.com
(646) 308-2103

Greg Eberhardt
geberhardt@pccpllc.com
(310) 414-2004

K.C. Boback
kboback@pccpllc.com
(646) 308-2102

[5] *S&P/Case-Shiller Home Price Index*
[6] *US Bureau of Labor Statistics*
[7] *PPR Data Genie*
[8] *Las Vegas Convention and Visitors Authority*
[9] *PPR Data Genie*