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MEMORANDUM

TO: SELECT ADDRESSES

FROM: GEORGE LIVINGSTON

DATE: OCTOBER 5, 2007

RE: **REAL ESTATE OUTLOOK**

The following points are from the recent Orlando RealShare Conference and from the Trends and Strategy Conference held by the University of Florida's Graduate Real Estate School, as well as other sources.

The general consensus was that the commercial real estate market has slowed, but that there are real differences in activity and opportunities by property types and among geographic locations.

ECONOMY

There is a 40% chance that our economy will slip into a recession. While a full-blown recession is not likely, it will feel like one. The press will overplay the decline, which will negatively affect confidence and demand. Positive momentum is not likely to occur before year end. The job market will show modest weakness, inflation will remain low, the dollar will weaken further, and interest rates will only increase modestly. The commercial real estate market should firm by year end.

STOCK MARKET

The Dow Jones is trading near a new high. The strong market is a leading indicator for the economy. This is a significant positive for the economy and for the real estate industry.

HOUSING MARKETS

The slowdown in the housing market will continue over the foreseeable future. Recovery may not occur until late 2008 or early 2009. This has, and will, impact the commercial markets, title and mortgage companies going out for example, as the demand and need for space is reduced.

The multi-family segment should benefit as fewer families and individuals can qualify for loans.

Foreclosures are more common in some markets, Phoenix and Las Vegas, and by property type, condos in Miami for example. The more there was a bubble and speculation, the higher the rate.

Inventory of new residences stands at 16 or more months for single family and more than 30 months for residential condos. This will retard new construction. A large inventory of existing homes also exists.

One or more large national home builders are expected to go bankrupt.

POPULATION GROWTH

The rate of growth in Florida is likely to slow, but remain at a high level, as compared to other states. Florida will remain the fastest growing state in the southeast.

Workers will come to the jobs spawned from population growth and from companies growing and relocating in Florida. Retirees will continue to move to Florida also.

Florida is not as affordable as it once was, so we will lose some retirees to other states, North Carolina and Tennessee for example.

INVESTMENTS

The demand for all types and qualities of investment properties remains strong. This trend is likely to persist.

CAPITAL MARKETS

The subprime meltdown has affected liquidity in the market. The spread over Treasuries has widened and the LIBOR rate has increased. Capital is more expensive. There is a flight to qualify by lenders to strong buyers and developers as well as to projects, and more equity will be required. The Federal Reserve is expected to reduce their overnight loan rate by another fifty bonus points by year end.

CAPITALIZATION RATES

The consensus was that cap rates are generally up between 20 and 50 basis points. In some cases, there is no change, based on fair pricing, location, and demand for product type. Cap rates are expected to increase modestly, say 50 basis points, by year end.

RETRADING

Buyers are retrading in some cases because they feel they can, based on the market turmoil. Sometimes they win, and in other cases, they are rebuffed. There are other buyers out there, just fewer of them. Buyers are still seeking properties, so worst case scenario is that you start over – at least for now.

STABILIZATION

Investment analysts typically assume stabilization at 5% vacancy. In the recent past, 7% was often used. The question was asked, should the rate more reflect the market's long-term norm, say 10% or more in the case for offices?

The consensus was that the rate should reflect the newness of the product with new being better, quality of the building and tenant mix, as well as the market. New quality buildings tend to have higher occupancies.

RENTAL RATES

Rental rates have generally stabilized, but incentives such as free rent have modestly increased.

COST TO CONSTRUCT

The cost to build new homes has declined. The cost of commercial construction has also started to decline.

ABSORPTION AND OCCUPANCY

While it varies by property type, absorption has in general slowed. Offices are doing the best while condos, residential and commercial, are doing the worst. Retail was perceived as flat, and industrial was down modestly. Occupancies remain high.

REITS

The REIT market segment has been significantly battered over the recent past by the market, but has largely recovered. Historically REITs typically had an all in return of 13% to 15% from dividends and appreciation. After beating the broad market for most years over the recent past and enjoying much higher returns, REITs seem to be reverting to their normal performance range.

Select REITs are clearly preferred, as measured by market valuations, Prologis for example, with the others arrayed to reflect Wall Street's view of their business model and performance. I judge REITs to be a leading proxy indicator for the commercial real estate market. That makes their quick recovery a positive event.

LAND

Land prices are likely to decline in the short to intermediate term and sellers likely will be more permissive as to due diligence and terms.

ISSUES

There are many risks in the current real estate market:

1. Hometown Democracy limiting the ability to increase land use densities and to permit new developments that require land use changes.
2. The length and extent of the housing decline.
3. Liquidity squeeze in the capital markets.
4. Land availability for commercial development, especially industrial.
5. Costs to achieve concurrency.
6. Lack of infrastructure, sewer and water for example, in edge markets.
7. Time to permit.
8. Assurance of development approvals.

PORTS

Port expansion continues to foster growth as imports increase and we continue to offshore manufacturing. Exports are a plus now too. Coastal shipping to avoid road and rail congestion and reduce costs is expanding. Consider Florida as one port with wharfs in Jacksonville, Miami, Tampa, and other locations. Shippers can choose where to offload based on where the containers are going.

OPPORTUNITIES

Buy entitled land. Buy discounted notes from banks and then foreclose on properties. Build apartments.

GL:kap