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Office Real Estate

2006 Forecast

Our View of the Office Market -

- On the back of a robust domestic and global economy, demand for office space continues to surprise on the upside
- Job growth, a key driver of office space, is continuing to register solid if not spectacular gains
- Headwinds include; labor shortages, offshoring, space efficiencies, energy costs, short term interest rates
- Vacancies are declining, new construction while increasing is still low
- Leasing velocity, while improving, is still not back to pre-recession levels

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Top 10 Trends

- Financial services, health services and professional and business services fueling the office market
- Call centers/data centers staged to make a bit of a comeback
- A handful of markets are going to be the catalyst to push rents significantly higher
- These markets will be characterized by rent spikes (bidding for space in highly sought after buildings will become more common)
- Early renewals to continue again next year
- Acute shortages of large blocks of space will increasingly be reported
- Class B space will enjoy a renaissance in 2006
- High demand for investment properties will push prices above replacement cost (even after taking into account rising construction costs)
- Construction activity will pick up substantially as the year progresses
- Residential conversions will continue to erode office stock

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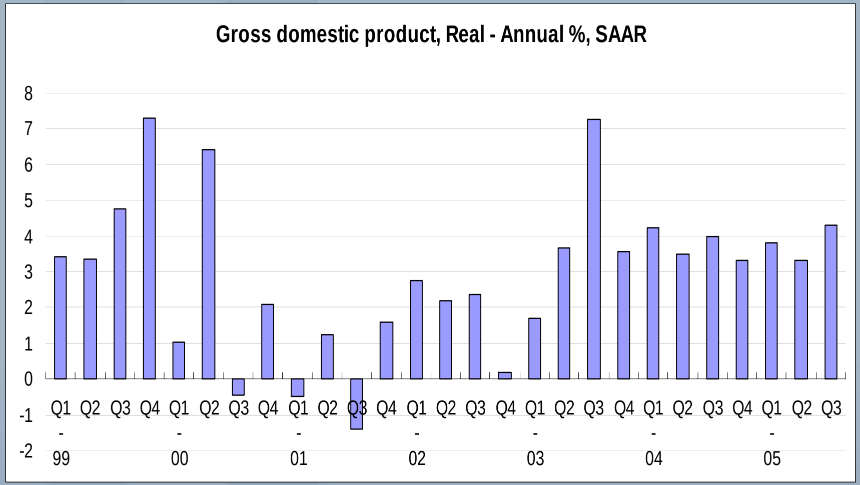
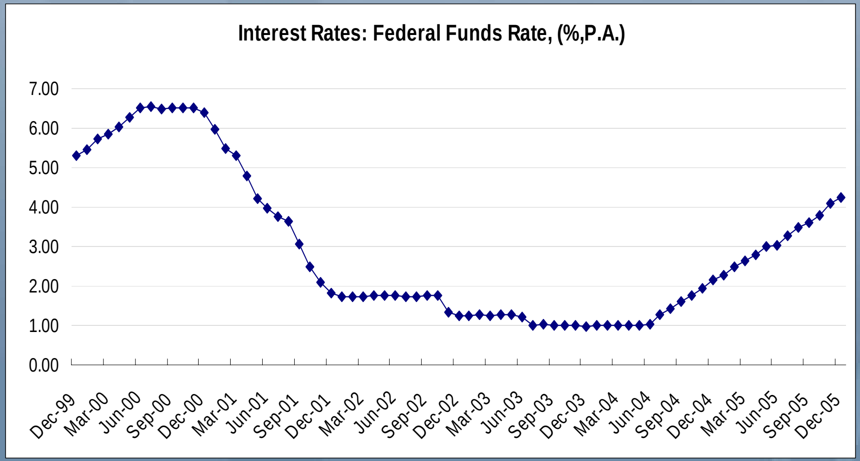
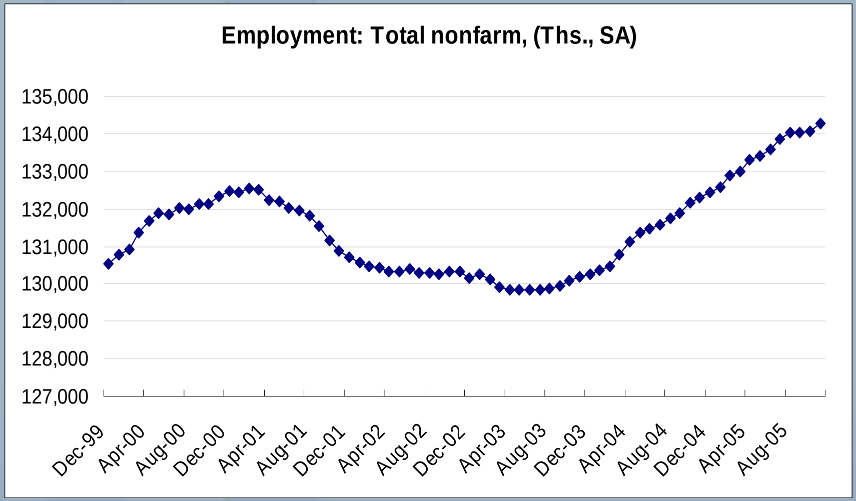
Office Real Estate – Key Demand Drivers

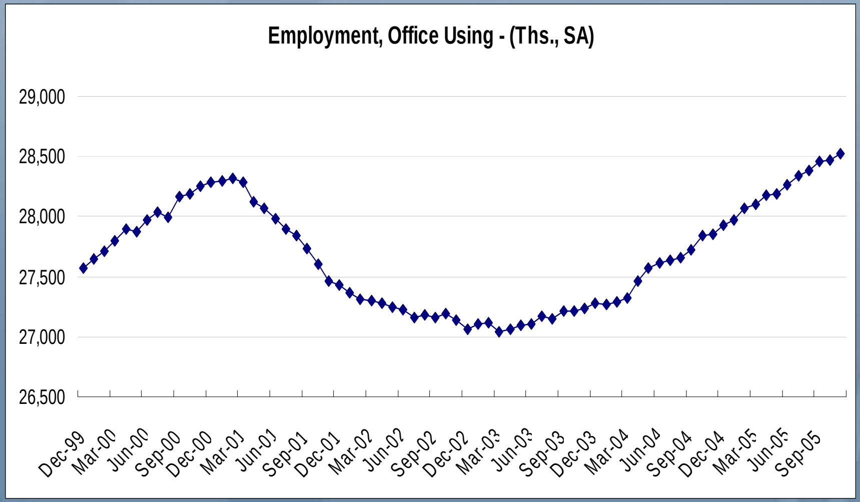




- US economy staying strong with Q3 growth of 4.3% - robust growth anticipated for Q4 and 2006
- Federal funds rate at 4.25%, up from 1.00% 18 months ago – 4.5% by January 06

Office Real Estate – Key Demand Drivers





- After two soft months, job market picked up steam. Total new jobs for 2005 approx 2.0 million, 1.5% growth

  Office using employment on track to increase 646,000 in 2005, 2.3% growth

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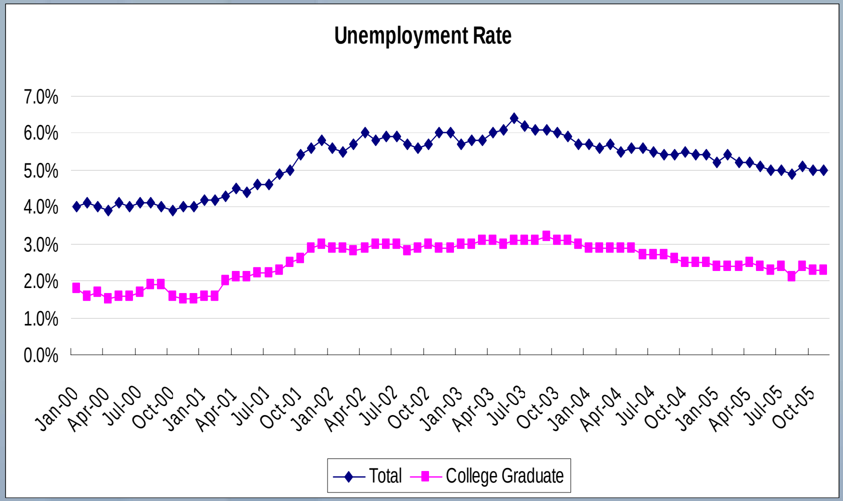
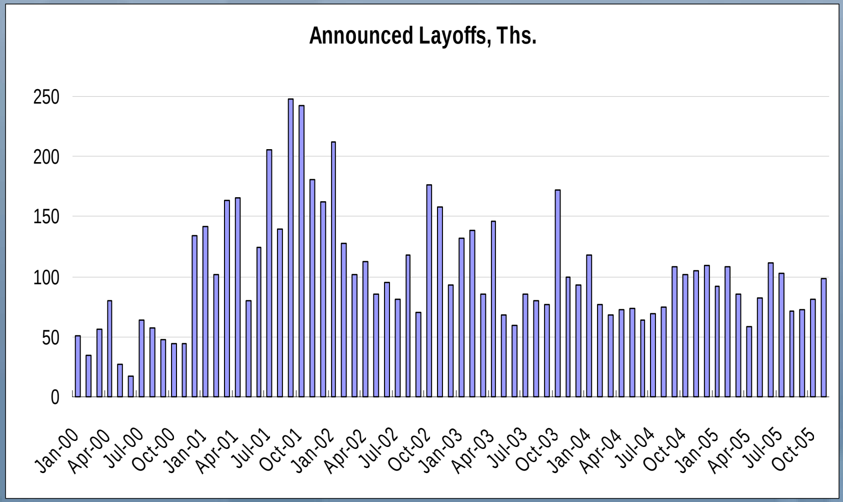
Office Real Estate – Key Demand Drivers





- Unemployment levels reflect tightening labor market, particularly true for college graduates.
- Layoffs continue to trend down, although November up after three good months

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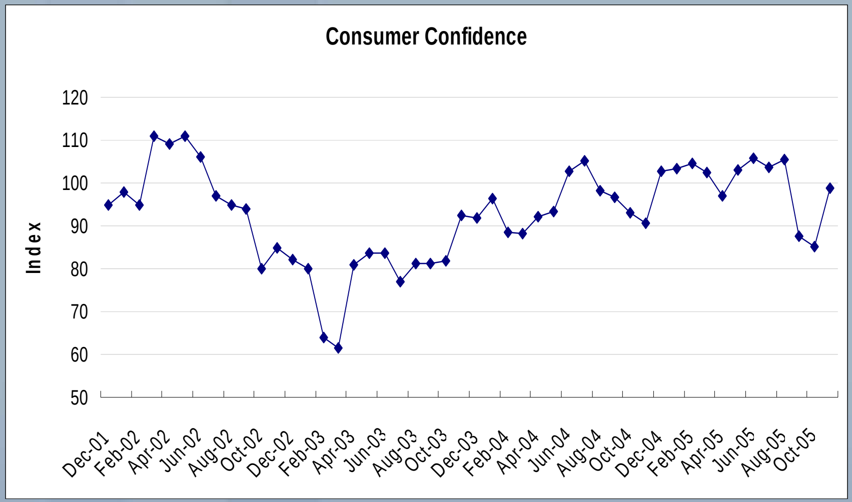
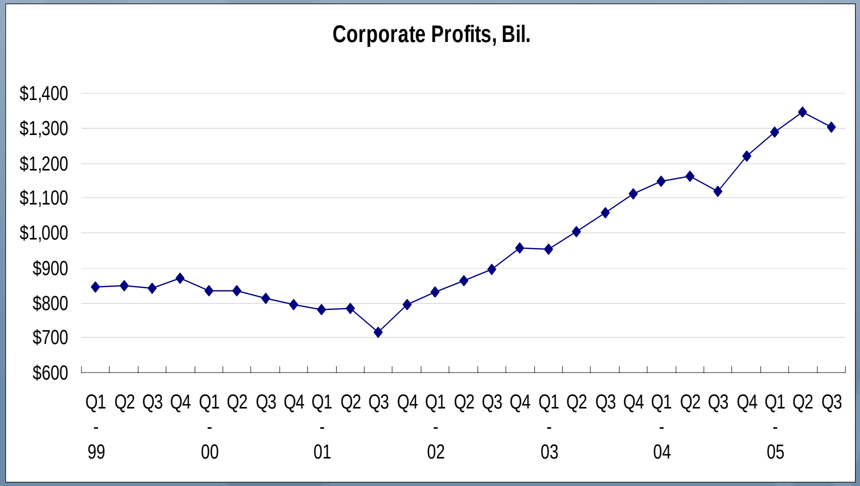
Office Real Estate – Key Demand Drivers





- After plunging in September and October, November reading above "90" – energy costs remain a concern

- While Q3 profits fell, the trend is up as corporations continue to accumulate significant cash balances

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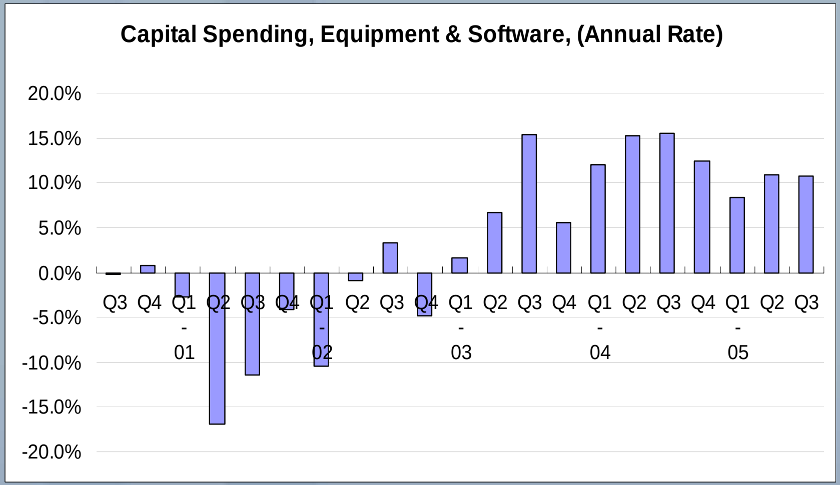
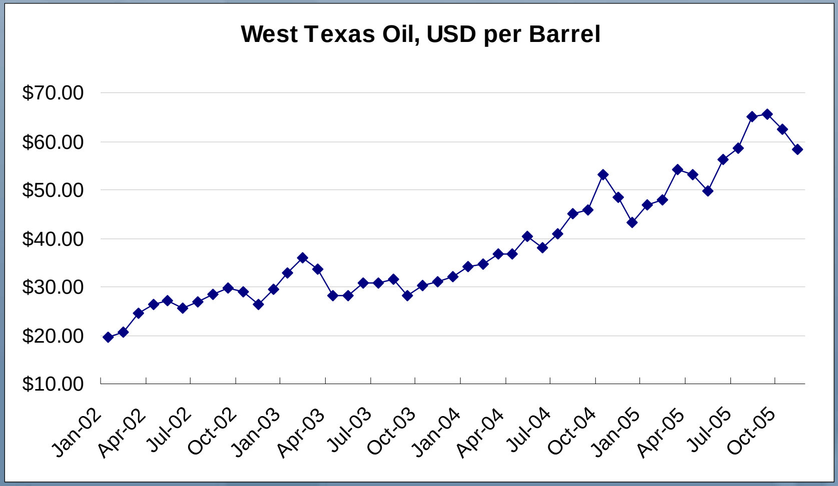
Office Real Estate – Key Demand Drivers





- Capital spending still posting double digit growth suggesting expansion for many firms
- The biggest unknown for 2006 remains oil - after peaking at $70, oil has settled at $60 with little change anticipated until the Spring

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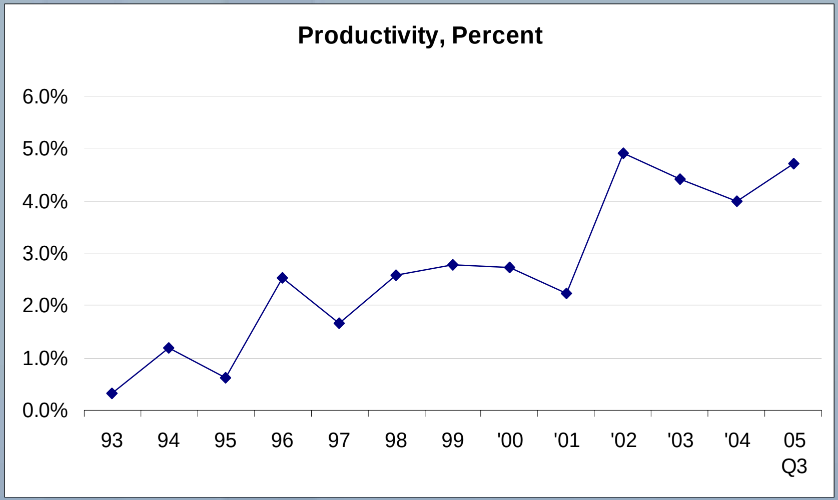
Office Real Estate – Key Demand Drivers



- Productivity levels remain very high – long term higher productivity will keep inflation and interest rates low, but will lower the demand for office space

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Office - Snapshot

- Office vacancy rate decreased by 52 basis points during Q3 to 14.1% (DT – 13.7%, Sub – 14.3%)
- Vacancy rate to landlords 12.5% (excluding sublease space)
- Q3 absorption registered 33.6 MSF, (26.3 in Q2) – 29.6 in Q3 2004
- Q3 new construction registered 9.4 MSF (12.0 in Q2) 11.6 in Q3 2004
- Sublease space down to 11.7% of vacant space
- Rents up – CBD 3.7% and suburban 2.2% YTD

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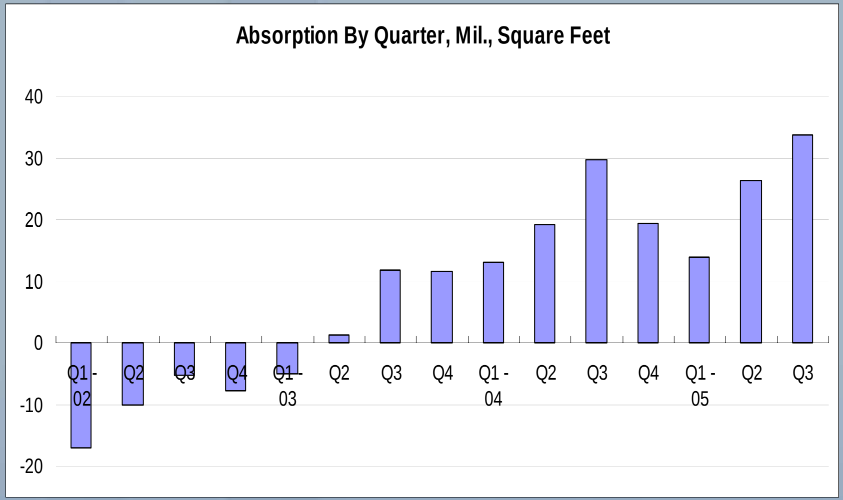
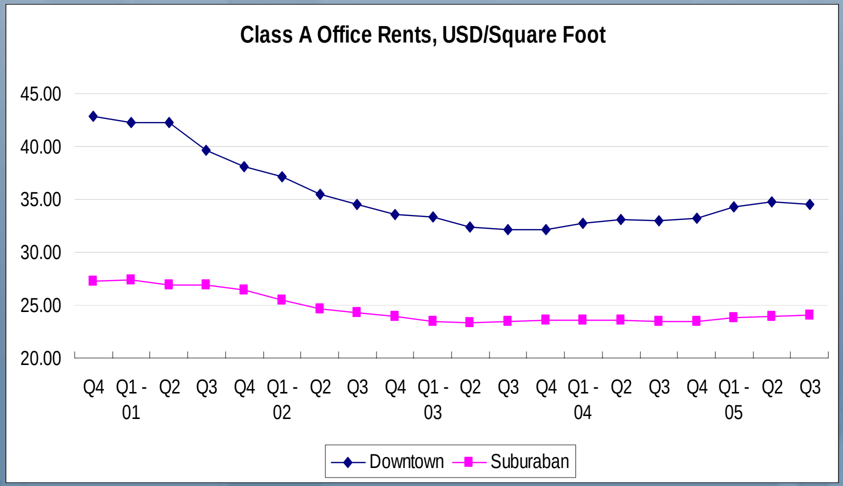
Office Real Estate – Market Fundamentals





- Demand for office space surged to a recent high in Q3 - for Q4 and 2006 leasing activity will be somewhat restricted by ever increasing efficiencies in space utilization

- In a handful of markets supply crunch anticipated in 2007 – 2009, rents will spike in late 2006, Downtown Class A buildings take 4-5 years to bring to market, Class C buildings being converted to other uses

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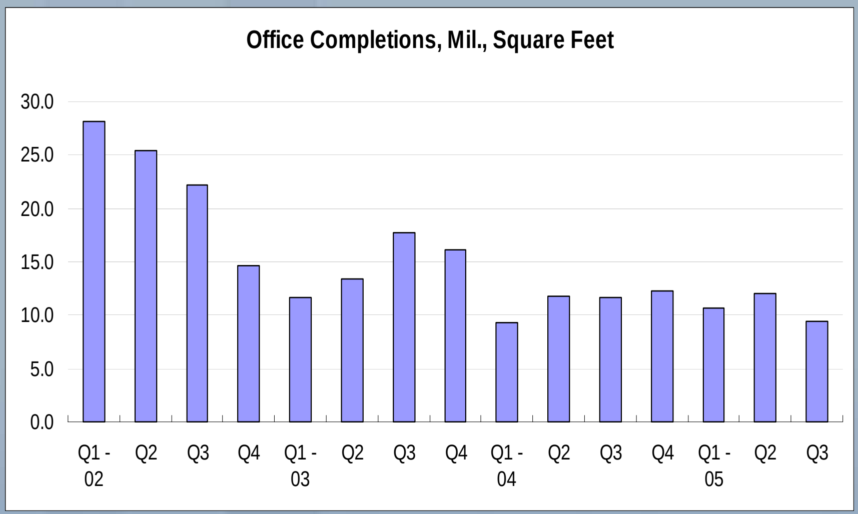
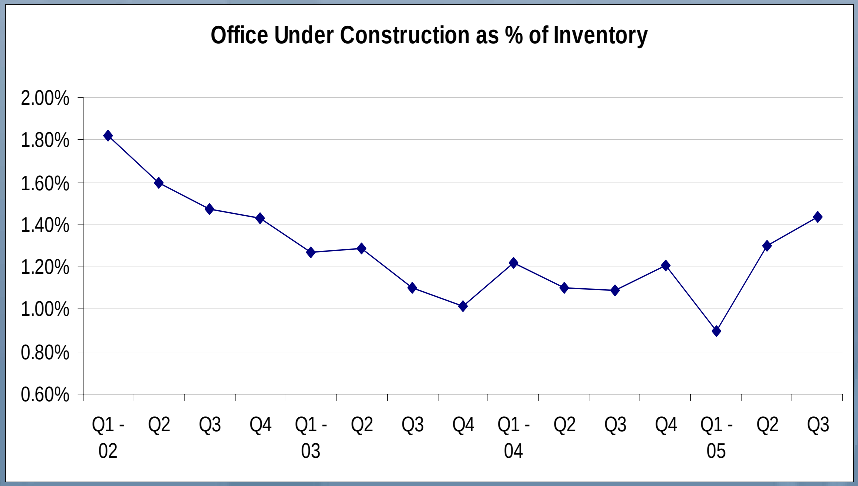
Office Real Estate – Market Fundamentals





- Increases in supply will be kept in check by; high land costs, extended entitlement periods, restraints on financing speculative development and rising material costs
- 2005 almost certainly marks a cyclical low as demonstrated by construction activity which is back above 1.4% of existing inventory

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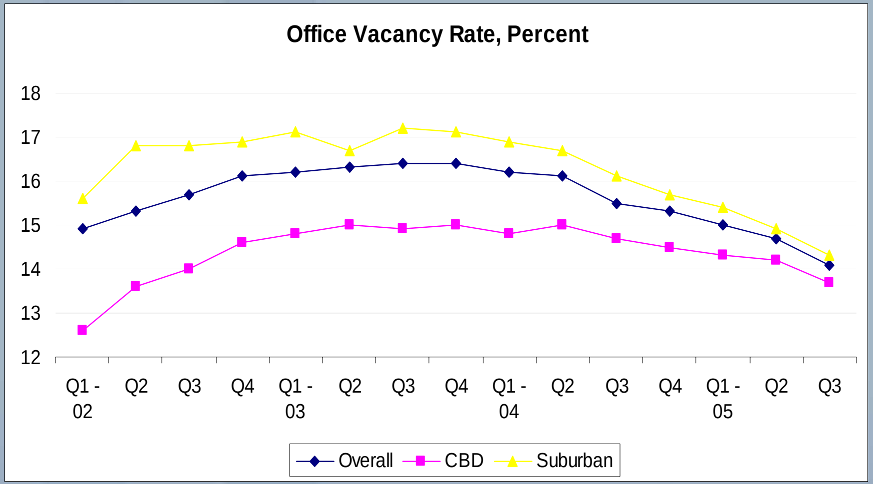

- Office vacancy rates continue to arc lower, with suburban vacancy rates declining by almost 300 basis points over the past 24 months

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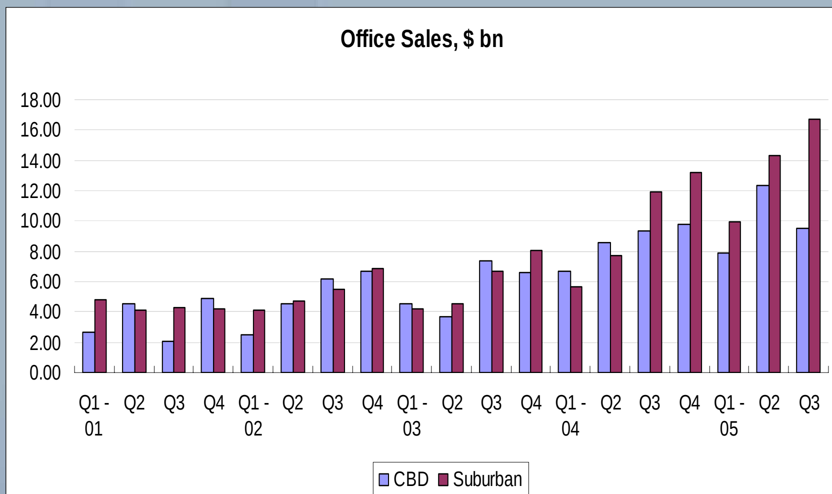
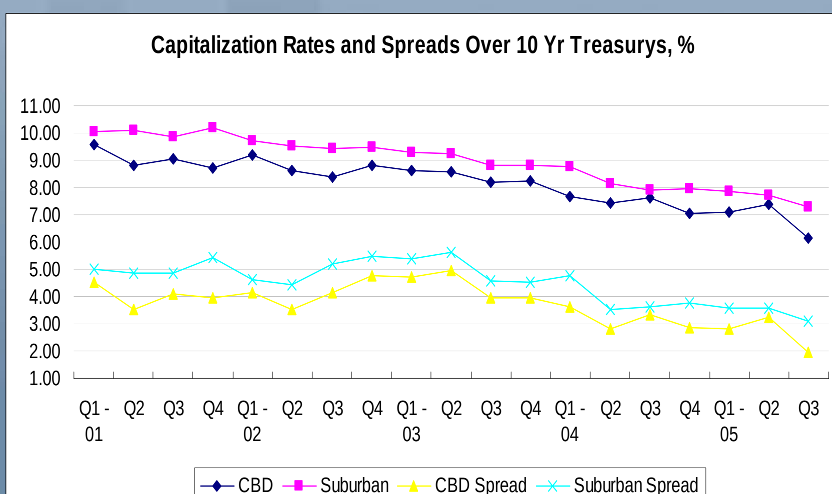
Office Real Estate – Market Fundamentals





- Office investment sales activity continues to be well above normal - particularly suburban

- Cap rates and spreads continue to go lower for both CBD and suburban properties

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Office – Investment Market Summary

- Stronger market fundamentals will cancel out rising short-term interest rates (as long as they do not increase by more than 100 basis points)
- Real estate values will go higher driven by improving fundamentals not by cap rate compression
- Improving fundamentals make vacancy valuable
- Core buyers will pursue Class A real estate
- Value-add buyers will pursue Class B real estate
- Class C real estate will disappear for adaptive re-use
- We are in the midst of the strongest sellers market ever
- Private capital, which has been one of the most active buyer groups, will be less dominant in 2006 as they shift their focus to secondary and tertiary markets

Office – Investment Market Summary – continued

- Institutional buyers (pension funds) will be much bigger buyers in tier one markets in 2006
- Small value-add investors will be attracted to smaller suburban and tertiary markets
- Small value-add investors will also be attracted to Class B product in Class A markets
- Cap rates for the very best office real estate will remain in the 5.0-5.5% range
- Unleveraged IRR's for the very best real estate will remain in the low 7's
- The improving risk/return profile of real estate will continue to put downward pressure on cap rates
- With alternate investment returns still stagnant coupled with the lag effect of capital flows, real estate will again be the recipient of significant investment capital
- Higher replacement costs boosting values

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Office - 12 Month Forecast

- Office markets on target to register another robust year, at least on par with 2005
- Tech firms returning to the market could be the "big surprise" in 2006
- New office development to increase by 30% but still well below normal levels
- Vacancy levels to drop another full point to just over 13.0%
- Reports of "critical shortages" will be reported in certain sub-markets
- Office rents for top tier markets to increase by up to 25% in 2006
- Even in the face of rising interest rates, cap rates and prices to hold steady

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