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CHICAGO BOOTH REAL ESTATE

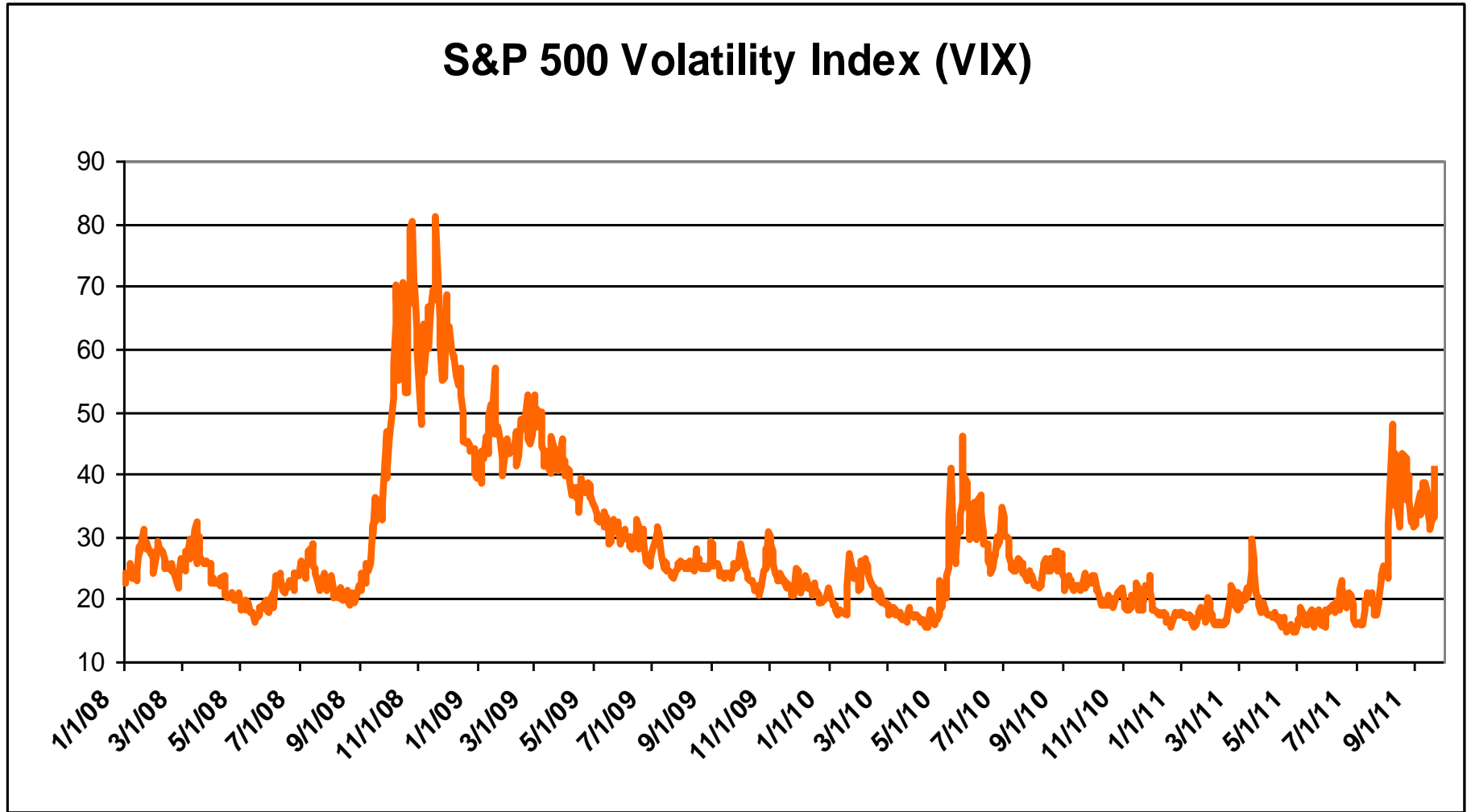
CONFERENCE

**THE RETURN
OF
SYSTEMIC
RISK**



NOVEMBER 10, 2011

Systemic risk and volatility returns...



SOURCE: CHICAGO BOARD OF EXCHANGE, OCTOBER 2011

- ❑ ***SLOWDOWN IN EARLY 2011 STARTED WITH EXOGENOUS AND IDIOSYNCRATIC EVENTS***
- ❑ ***BUT HAS COME FULL CIRCLE TO ENDOGENOUS AND SYSTEMIC EVENTS***
- ❑ ***SPECIFIC ISSUES DIFFER ACROSS DEVELOPED AND DEVELOPING ECONOMIES...***
- ❑ ***...BUT MOST OF THE VOLATILITY IS LINKED IN SOME WAY TO MARKET RESPONSE TO SIGNIFICANT GOVERNMENT POLICY UNCERTAINTY***

Sources of concern

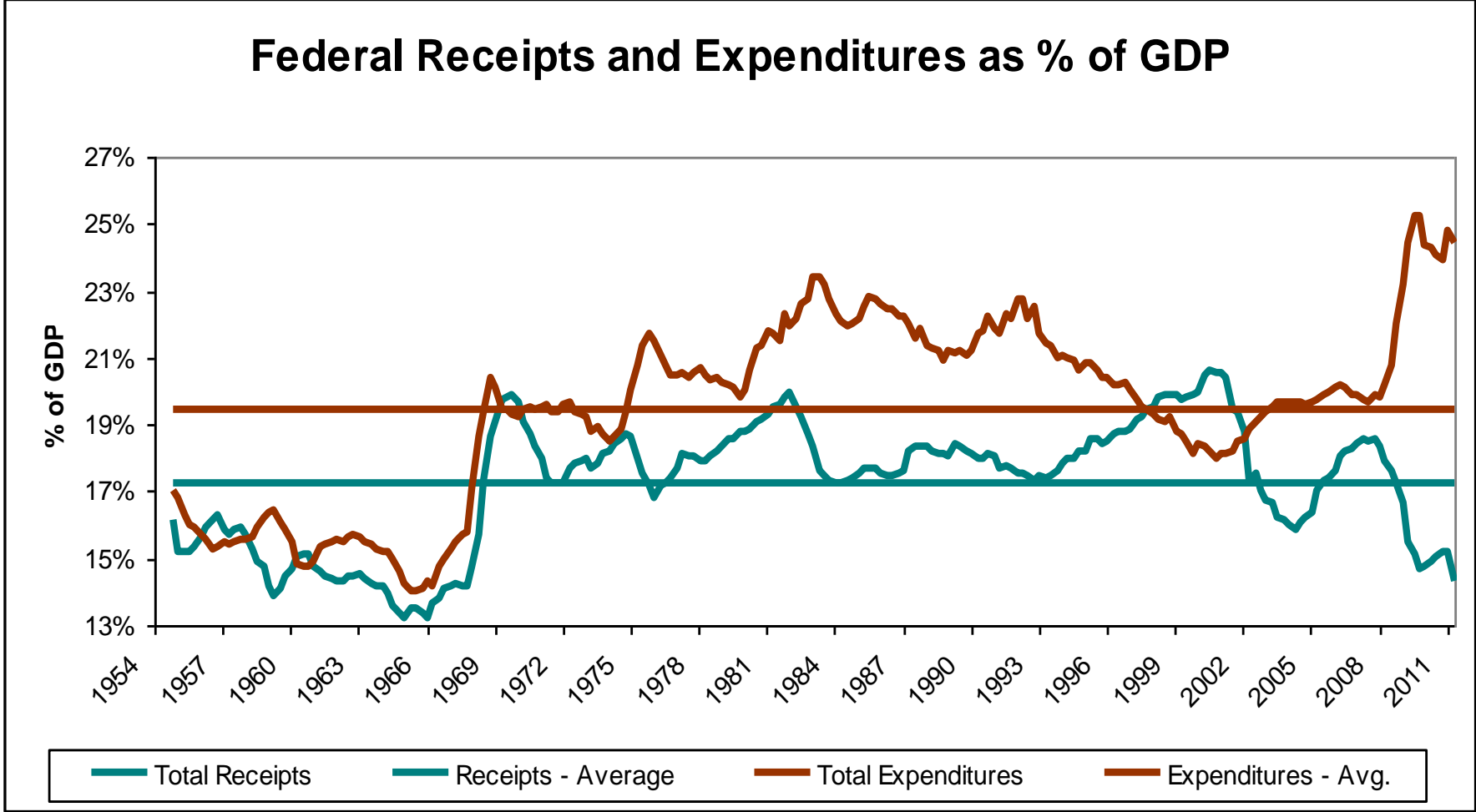
- ❑ **REALIZATION THAT CREDIT CRISIS NOT REALLY OVER**
 - **TRANSFERRED FROM PRIVATE SECTOR TO PUBLIC SECTOR IN DEVELOPED ECONOMIES**
 - **INCREASING CREDIT RISKS IN DEVELOPING ECONOMIES (INCLUDING SHADOW BANKING)**

- ❑ **EPICENTER OF SYSTEMIC RISK IS EUROPE**
 - **REACTIVE MEASURES, NOT PROACTIVE → CONTAGION STILL AN ISSUE**

- ❑ **BUT EVEN IF RESOLVED, PLENTY OF POLICY UNCERTAINTY IN U.S. AS 2012 ELECTION LANDSCAPE UNFOLDS**
 - **WELL CAPITALIZED PRIVATE SECTOR, BUT RELUCTANT TO EXPAND**
 - **REGULATORY ENVIRONMENT**
 - **BUDGET DEFICIT RESOLUTION**
 - **TAX POLICY**
 - **OVER-RELIANCE ON MONETARY POLICY?**

A big gap to close

Federal Receipts and Expenditures as % of GDP



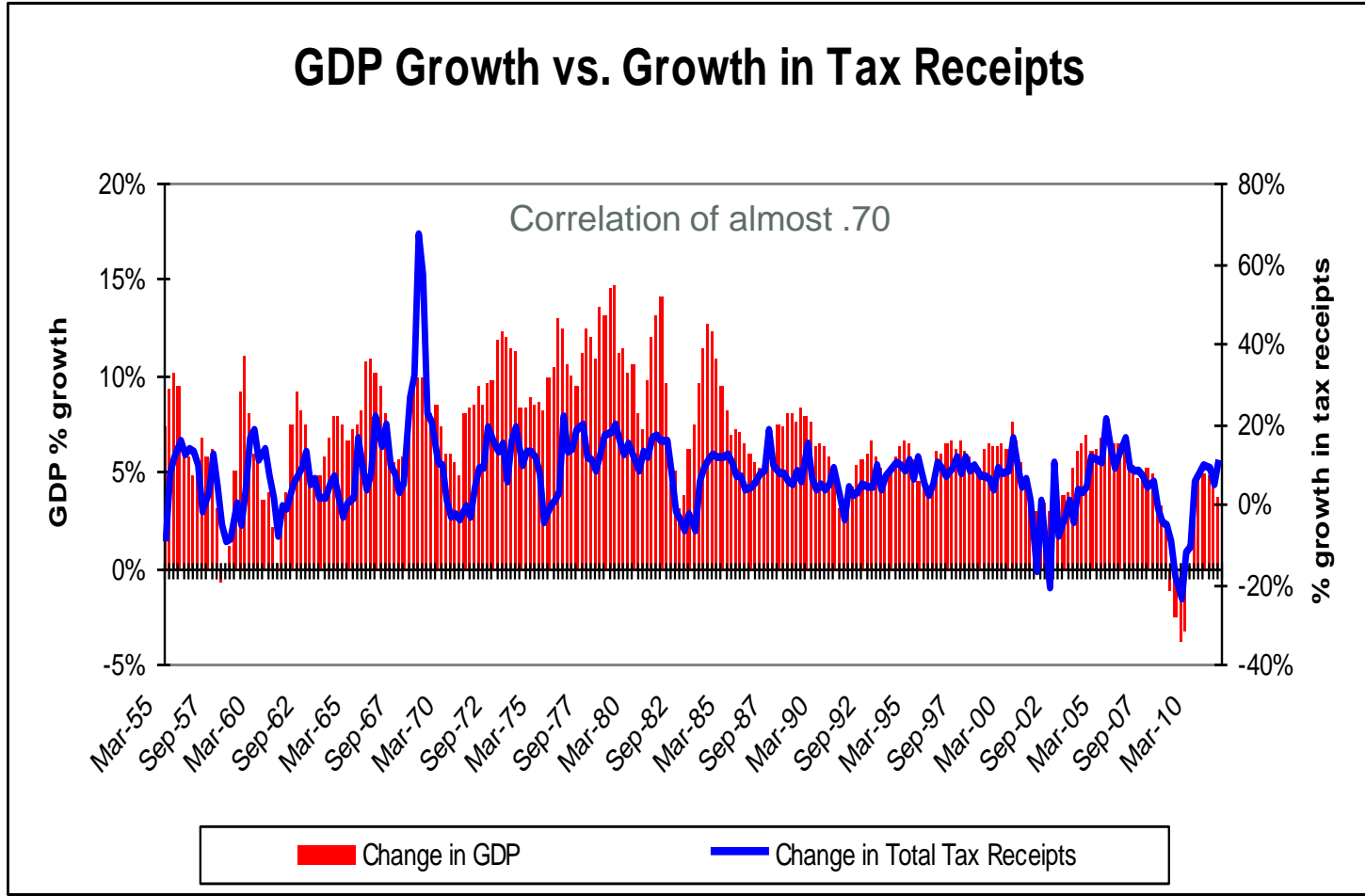
SOURCES: BUREAU OF ECONOMIC ANALYSIS, US TREASURY, SEPTEMBER 2011

Observations on policy and budget deficits

- ❑ **CLARITY NEEDED ON GOAL OF TAX POLICY: REDISTRIBUTE EXISTING WEALTH OR PRO-GROWTH TAX POLICY TO CREATE ADDITIONAL WEALTH?**

- ❑ **PRIVATIZE GOVERNMENT OWNED ASSETS TO RAISE CASH?**

- ❑ **CONSIDER U.S. SOVEREIGN WEALTH FUND FOR MORE EFFECTIVE USE OF**

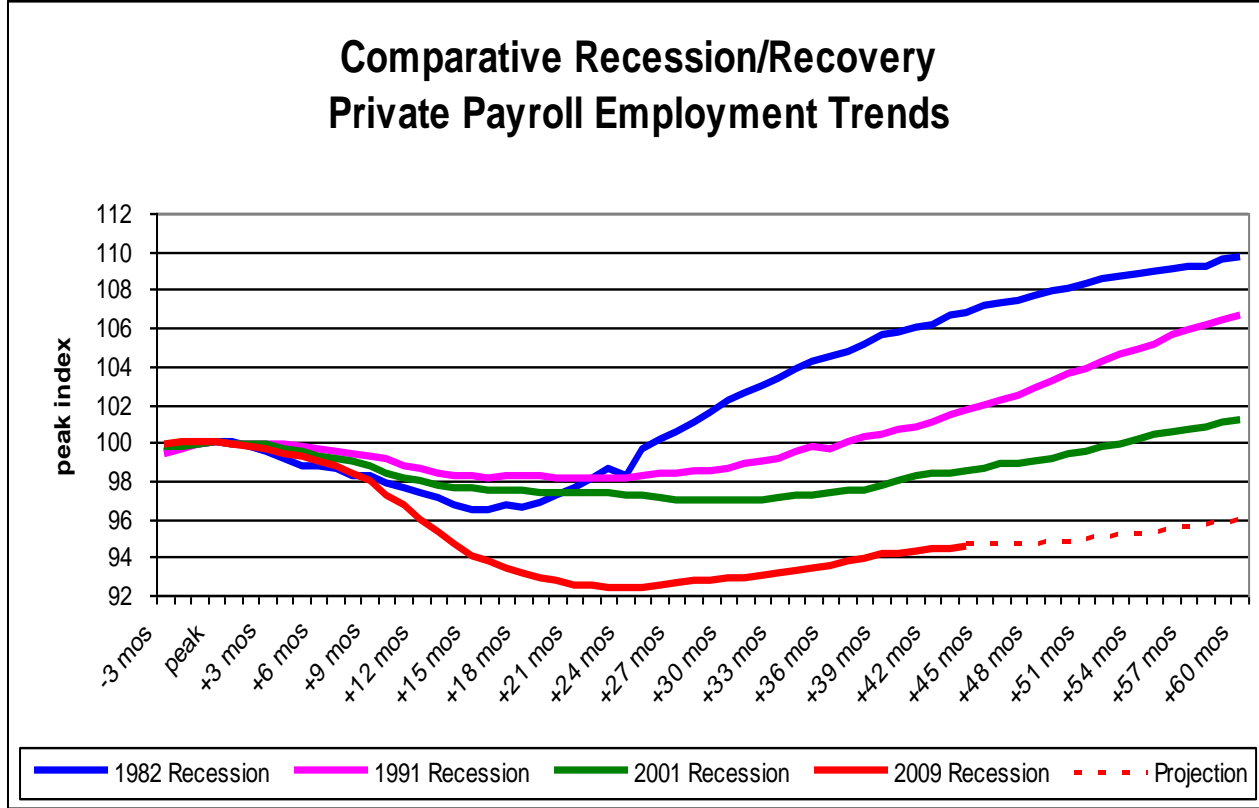


SOURCES: BUREAU OF ECONOMIC ANALYSIS, US TREASURY, TAX POLICY CENTER
SEPTEMBER 2011



OVERALL, SLOWER ECONOMY ADVERSELY IMPACTS SPACE MARKET RECOVERY

- EXCEPT FOR APARTMENTS, EQUILIBRIUM HAS BEEN PUSHED FURTHER INTO FUTURE AS ECONOMIC CONCERNS INCREASE
- SUPPLY NOT AN ISSUE EXCEPT FOR APARTMENTS, WHICH ARE NEAR PEAK LANDLORD PRICING POWER
- SOME BIG BOX INDUSTRIAL SUPPLY ALSO UNDERWAY

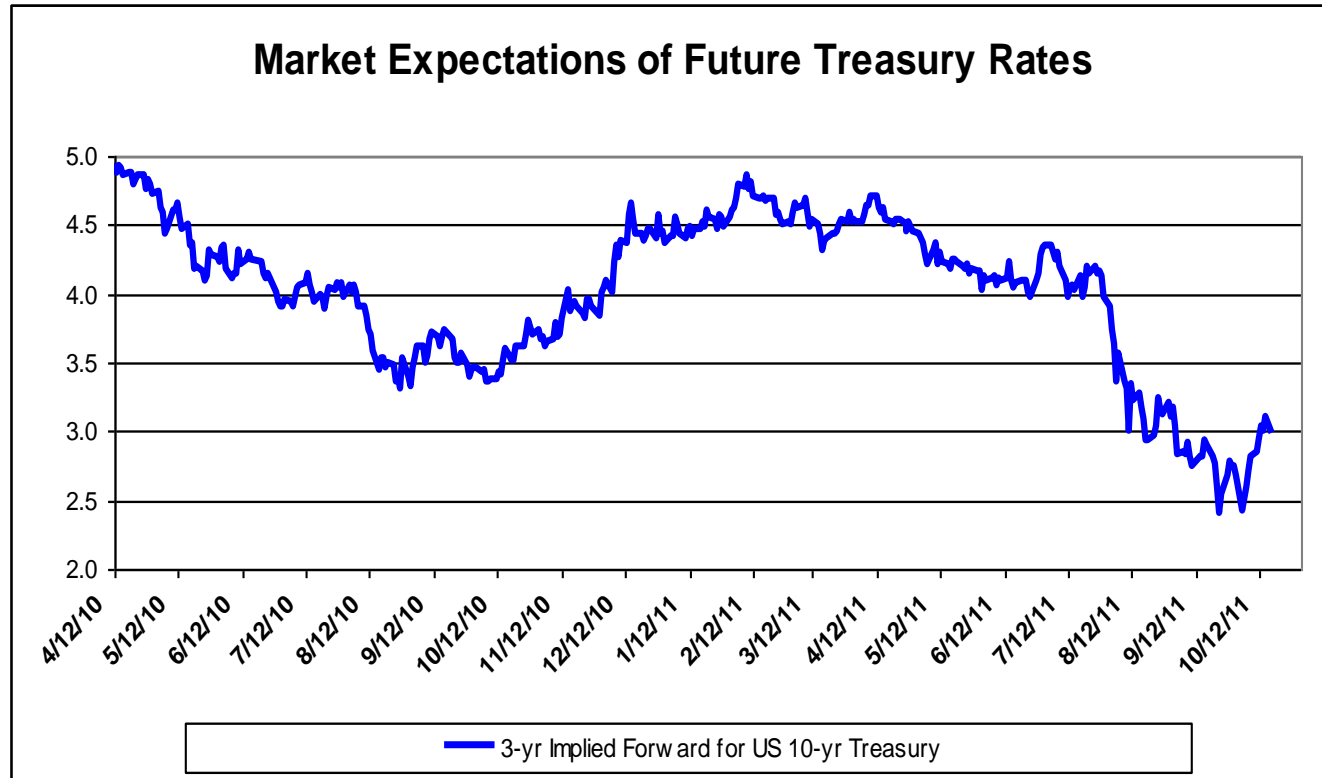


SOURCES: BUREAU OF LABOR STATISTICS, PRINCIPAL GLOBAL INVESTORS, NOVEMBER 2011



IMPACT OF VOLATILITY ON REAL ESTATE PRICING ACROSS QUADRANTS

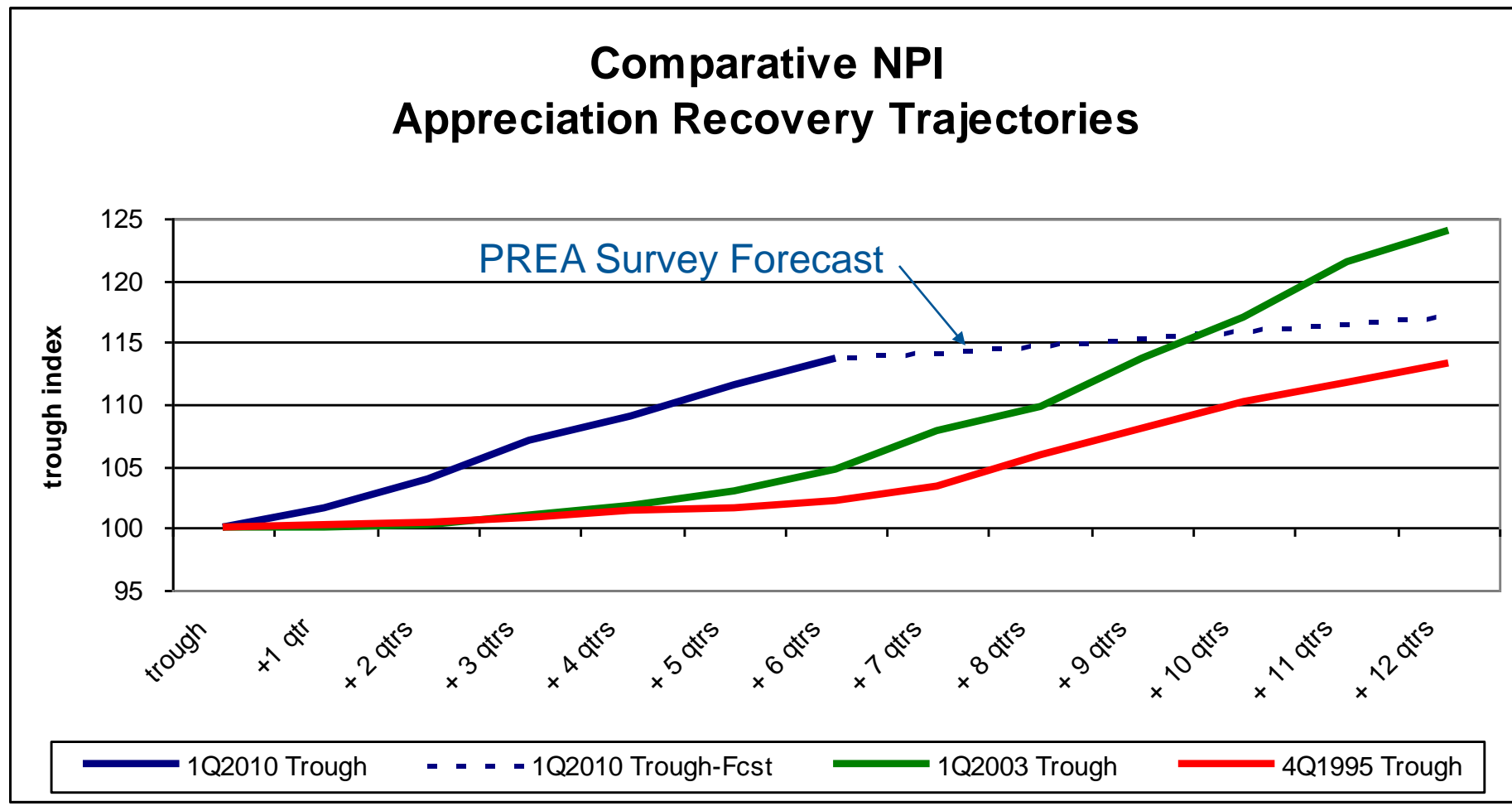
- THE RELATIVE VALUE EQUATION HAS CHANGED
- REITS DOUBLE BEAR MARKET, BUT WITH SUBSEQUENT REBOUNDS
- CMBS PRICED FOR RECESSION
- MORE CONSERVATIVE SENIOR SECURED LENDERS AND ABSENCE OF CMBS OPENS DOOR FOR MEZZANINE LENDERS
- TREASURY RATES SUPPORTIVE OF



SOURCE: US TREASURY, OCTOBER 2011

Rate of appreciation expected to flatten, but not necessarily turn negative

Comparative NPI Appreciation Recovery Trajectories



SOURCE: NCREIF, PREA, OCTOBER 2011

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