

Real value in a changing world

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U.S. 2008 Capital Markets Transaction Volume Down 70 Percent to \$125 Billion; Distressed Property and Loan Asset Opportunities Expected in 2009

Mortgage risk emerging as major borrowers face balloon hurdles in 2009

CHICAGO, JAN. 23, 2008 — Jones Lang LaSalle expects 2008 year-end U.S. capital markets total transaction volume, hindered by the global credit crisis and a recessionary economy, to have closed at approximately \$125 billion^[1], down some 70 percent from 2007. According to Jones Lang LaSalle's new U.S. Capital Markets 2009 research report, the rate of transaction decline increased significantly over the last few months of 2008 as the commercial mortgage-backed securities (CMBS) market virtually disappeared and dramatically waylaid new transactions. CMBS issuance effectively came to a standstill in 2008, plunging by 95 percent from 2007 to just \$12.1 billion, with zero new CMBS issuances since June. Given the likelihood the CMBS market will not return in a meaningful fashion in the near-term, investment transaction activity in 2009 may further decline by up to 20-25 percent. Further complicating the investment sales market will be the fierce competition for capital and a buyer-seller standoff that won't likely break until true distress hits a broad swath of owners beginning in late 2009.

According to Jones Lang LaSalle, the global economy is in the midst of a necessary broad de-leveraging that transcends political boundaries, industries and asset classes. While the contraction in debt availability in the financial markets is expected to extend through 2009, private equity funds and foreign investors should gain traction in 2009 as they continue to amass large pools of opportunistic equity poised to purchase distressed assets and mis-priced commercial loans.

"It may take another three to four quarters for broad-based distress to reach the sales market, but there is no question there is capital waiting to invest in real estate once opportunities arise¹. The delay is coming from owners and investors who are just now coming to grips with the new realities of today's market that includes a 30+ percent decline in asset values. Few investors are rushing to sell currently unless they're facing imminent loan maturities or redemptions," said Earl Webb, CEO of Jones Lang LaSalle Capital Markets. "While we are seeing transactions occur, "true" pricing benchmarks will not be clear until a large-scale, forced-selling of distressed assets occurs and sets a new value range. It is unclear where cap rates will settle, but if going-in, un-levered yields rise above eight percent for quality properties in 2009, opportunistic investors will begin to seize these once-in-a-

¹ JLL estimates \$300 billion of capital is targeting U.S. real estate

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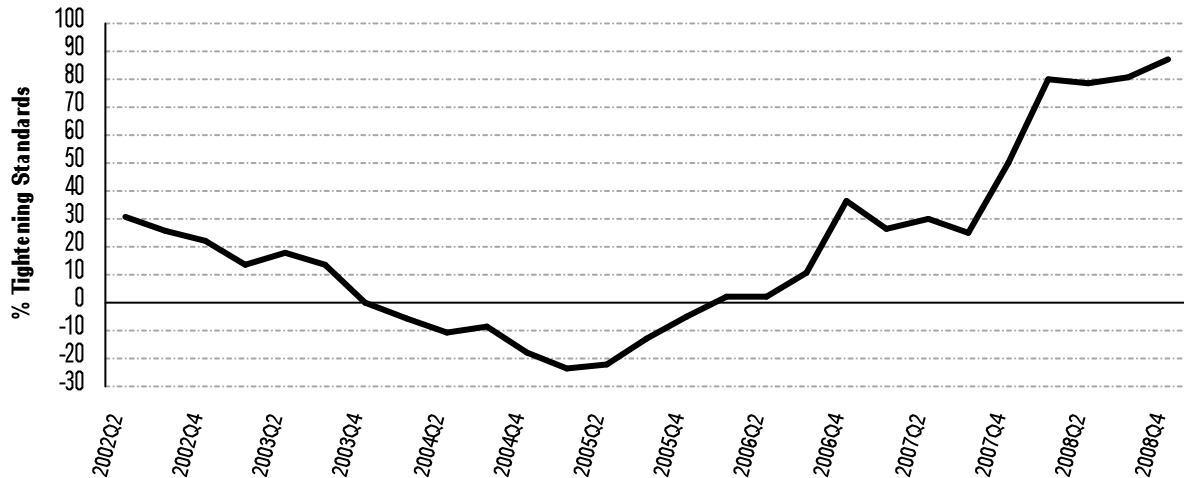
lifetime yield opportunities. Additionally, as market fundamentals continue to weaken in 2009, values may continue to erode in spite of a gradual stabilizing of cap rates and return expectations.”

Jones Lang LaSalle also indicated the Federal Reserve and Treasury are expected to aggressively counter the financial crisis by introducing various new tools to promote liquidity, directly purchasing debt instruments and injecting financial institutions with capital. Combined, these measures should reduce market volatility during 2009.

Despite the continuing unprecedented efforts of the federal government to utilize creative new liquidity measures, banks continue to rein in lending. In the fourth quarter 2008, a record high percentage of senior loan officers reported to the U.S. Federal Reserve that their banks were tightening standards for commercial real estate loans. Commercial lending will likely tighten even further in 2009, given deteriorating fundamentals and continuing financial turmoil.

Banks Continue to Rein in Lending; 87% Tightening in Q4 Highest in Fed Survey History

Net % of Banks Tightening Standards for Commercial Real Estate Loans



Source: Economy.com, Jones Lang LaSalle, Federal Reserve

“The beginning of a new presidential administration and new aggressive monetary policies should increase certainty into the debt markets by mid- 2009, but the CMBS market as we knew it in 2006-2007 is gone,” said Bart Steinfeld, Managing Director of Jones Lang LaSalle’s Real Estate Investment Banking practice. “The resultant lack of liquidity in the transactions market will continue to create challenges for owners and developers in 2009. That will produce an exponential rise in the number of troubled first mortgage and mezzanine loans that will need to be repositioned in the coming year.”

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Many of the loans underwritten from 2005 to 2007 contained aggressive rent growth assumptions that will be unsupportable in 2009. In today's market, commercial rents are declining and will continue to do so into 2010. A further drop in rental rates, combined with a much more conservative financing environment, is expected to have a direct impact on the increasing number of delinquencies and defaults in 2009.

"Given the unprecedented reduction of liquidity and global de-leveraging, balloon payment risk has quickly emerged as one of the major hurdles facing borrowers with maturing loans in 2009 and 2010," said Steinfeld. "Servicers have increasingly indicated that they anticipate a growing number of borrowers to have trouble refinancing maturing mortgages, even if the underlying properties are performing well."

According to Jones Lang LaSalle, the growing number of troubled mortgages is ushering in an escalation in secondary loan sales activity. That activity is a product of the bid-ask gap narrowing, as loan sellers have begun to acknowledge the deflated values of their assets and begin to accept the realities of current market pricing. As evidence of this trend, the firm has seen an increasing demand for the firm's Value Recovery Services, specialized services that assist clients affected by the current financial crisis. These services address:

- the new operational and occupancy needs of banks and insurance companies; assist financial institutions with challenged assets and liabilities;
- provide receivership services to lenders, loan servicers and financial institutions;
- help public-sector entities raise cash to meet budget shortfalls from assets they have acquired from financial institutions;
- assist owners of distressed properties with leasing and recapitalization strategies; and
- assist occupiers with identifying ways to create value with their occupancy requirements and manage the negotiation risks in this challenging environment.

"We're seeing an increasing number of global financial institutions and loan servicers turn to intermediaries looking for help. We're currently providing valuation, asset strategy and management and loan disposition services for a major commercial bank on a loan portfolio in excess of \$1 billion. This portfolio includes whole loans, b-notes and mezzanine positions, which are all secured by various forms of income and non-income producing real estate. There are still buyers for these assets today," confirmed Steinfeld. "We're also selling a \$220 million portfolio of b-notes backed by U.S. assets for a European financial institution."

On the bright side, Jones Lang LaSalle reports that while lending activity has markedly diminished in the past year and spreads have risen accordingly, the drop in market indices has created an

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opportunity for borrowers who are actually able to get financing from traditional lenders to lock in financing rates at reasonable coupons. As of January 12th, LIBOR dropped to an astonishing 0.34 percent, down from 4.6 percent in January 2008 and 5.32 percent in January 2007; while the 5-year Treasury yield sank below 1.5 percent, compared to 3.08 percent in January 2008 and 4.76 percent in January 2007. Clearly, those investors with capital will be “king” in 2009.

“As more owners face upcoming maturities that cannot be refinanced, an unprecedented opportunity is emerging for investors in distressed debt and CMBS where the super-senior 10-year, AAA class continues to yield unprecedented returns (approximately 12.4 percent as of mid-December),” added Webb.

International Investor Outlook

“The increase in loan sale activity is spreading across the globe,” said Steve Collins, Managing Director of Jones Lang LaSalle’s International Capital Group. “As the debt bubble deflates in 2009, opportunities will emerge for private and foreign equity funds to make substantial gains in market share while many highly-leveraged private funds will be forced to shrink and consolidate in the face of redemptions.”

Both foreign and institutional buyers have been the only net buyers in 2008. However, international investors, who had once taken advantage of the dollar’s decline against the euro, are expected to slightly pare back and focus their investments on core markets in 2009.

“With yields at nine to 10 percent on senior level debt, first mortgage loans are becoming an attractive return on investment for international players,” added Collins. “In 2009, we expect to see increased market participation by foreign entries into all levels of the capital stack.”

Corporate Capital Chase

Jones Lang LaSalle also reports an increasing number of corporations are exploring the benefits of sale-leaseback transactions to maximize value and access affordable capital through the non-core assets.

Jay Koster, Managing Director of Jones Lang LaSalle’s Corporate Capital Markets practice, predicts a significant increase in corporate appetite to execute sale-leasebacks in 2009. “Corporations are looking for capital capacity to operate their businesses and position themselves to take advantage of opportunities that will arise through this market cycle,” said Koster. “We’re seeing more corporations looking to trade property to raise capital, and we expect that appetite will be matched by heightened demand from investors that recognize inherent value in real estate leased to strong-credit corporations. The inquiries from our corporate clients are up by 300 percent, versus 18 months ago.”

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Kenneth Rudy, Jones Lang LaSalle's President & COO agrees with Koster. "We foretold an increase in corporate sale-leasebacks last year and that trend will absolutely continue as corporations remain challenged in securing new sources of capital," said Rudy. "Transactions will start to close in 2009 as investors are more willing to commit capital to acquire companies' owned assets tied to long-term, credit leases. We also expect to see more corporate dispositions to come from downsizing in 2009 as corporations mark-to-market the value of surplus real estate inherited in acquisitions at market clearing prices."

Jones Lang LaSalle Capital Markets is composed of a broad range of real estate investment debt and equity specialists, and corporate finance experts, working on all property types and in all the major national markets on behalf of major institutional and local investors and developers, as well as corporations. The firm's Capital Markets professionals are highly skilled at pinpointing and tailoring the right capital solutions for each of these client's needs. The Investment Sales teams assist investors in developing and executing asset recapitalization strategies for office, industrial, retail, multifamily, healthcare and seniors housing product. The firm's Real Estate Investment Banking experts raise debt and joint venture equity for investors and developers, and provide secondary loan sale advisory services. The Corporate Capital Markets professionals help corporations develop and execute strategies that bridge their occupancy, capital deployment and financial reporting objectives for their facility portfolios. Collectively, the firm's Capital Markets team handled \$82 billion in annual transaction volume in 2007.

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About Jones Lang LaSalle

Jones Lang LaSalle (NYSE:JLL) is a financial and professional services firm specializing in real estate. The firm offers integrated services delivered by expert teams worldwide to clients seeking increased value by owning, occupying or investing in real estate. With 2007 global revenue of \$2.7 billion, Jones Lang LaSalle serves clients in 60 countries from 750 locations worldwide, including 180 corporate offices. The firm is an industry leader in property and corporate facility management services, with a portfolio of approximately 1.2 billion square feet worldwide. LaSalle Investment Management, the company's investment management business, is one of the world's largest and most diverse in real estate with \$53 billion of assets under management. For further information, please visit our Web site, www.joneslanglasalle.com.

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