MARKETBEAT

U.S. Capital Markets

Q4 2017

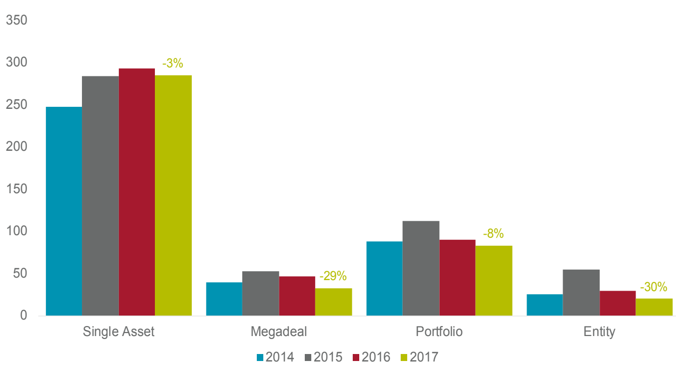
Fourth Quarter Reversal of Fortunes

Transactions volumes totaled $113 billion (B) in the fourth quarter of 2017, bringing the annual total to $422B—down 8.0% from 2016.[1] The anticipated acceleration in deal activity at the end of the year was muted due primarily to a sharp decline in M&A activity. Uncertainty surrounding the recent tax reform legislation could also explain the deceleration in investment sales. With that legislation signed into law, there is reason to believe that there could be a pick-up in the first half of 2018.

Meanwhile core single asset sales exhibited strong momentum, increasing 14% quarter-over-quarter (QoQ). Megadeal volumes, which had been largely absent from the market in the middle half of the year, nearly doubled.[2]

INVESTMENT SALES VOLUMES 2014 - 2017

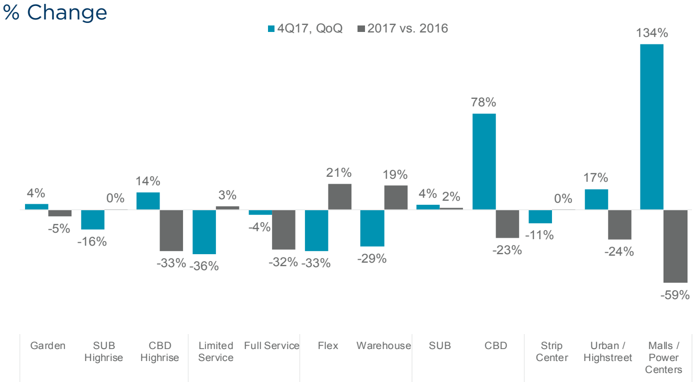
$ Billions, YOY % Change



Source: Real Capital Analytics, Cushman & Wakefield Research
Deals over $5 million

QUARTERLY AND ANNUAL INVESTMENT VOLUME

% Change



Source: Real Capital Analytics
Deals over $5 million

Key Themes of 2017

Smaller Transactions Drove the Market

Despite its comeback in the fourth quarter, megadeal volumes nonetheless ended the year down 29% from 2016. Entity-level transactions were down 30% during the same timeframe and together **megadeals and entity-level transactions accounted for two-thirds of the overall decline in volumes.** Single asset transactions under $250 million (M) were down only 3% in 2017 compared to 2016. Portfolio sales were between these two extremes, down 8% YoY.

Investors Looked Beyond the Major Metro Markets

The decline in megadeal volumes was symptomatic of the broader deceleration in major metro market transaction activity, which fell 14% in 2017. Of the $28B decline in volume, $22B—roughly three-quarters—was attributable to the New York City metropolitan area. It should be noted, however, that New York metro volumes accelerated in the fourth quarter of 2017, ending the year down 32%. In contrast, Washington, D.C. metro volumes were up 13% for the year, driven by strong multifamily, industrial and CBD office sales. Volumes in the Boston and Los Angeles metros were largely flat.

Secondary markets ended the year down only 4% compared to 2016, and tertiary markets down only 3%, although the fourth quarter saw tertiary market volumes 17% QoQ. Houston was the top performing market with volumes up 45% compared to 2016 across industrial, office and retail. The second-best performing market was Orlando where volumes increased 23% as a result of strong multifamily and suburban office activity. Baltimore rounds out the top three with volumes up 40% YoY, driven by industrial and office activity.

Capital Rotated Towards the Suburbs

Urban property sales have been decelerating—from 29% of investment sales volumes in 2015 and 27% in 2016 to 21% in 2017. The decline in absolute sales volume was most evident in office and multifamily. Hotel and retail, however, experienced the largest percentage declines. In the suburbs, industrial, office and development site volume growth nearly offset declines in apartment, hotel and retail.

Fourth quarter activity suggests that urban transactions may be finding a floor. Urban volumes increased 37% QoQ on a pick-up in CBD office and urban development site sales. On the other hand, suburban volumes declined 8% QoQ; growing office volumes failed to offset sharp declines in sales of industrial properties, hotels and development sites, but ended the year largely flat compared to 2016 levels.

Industrial Flourished

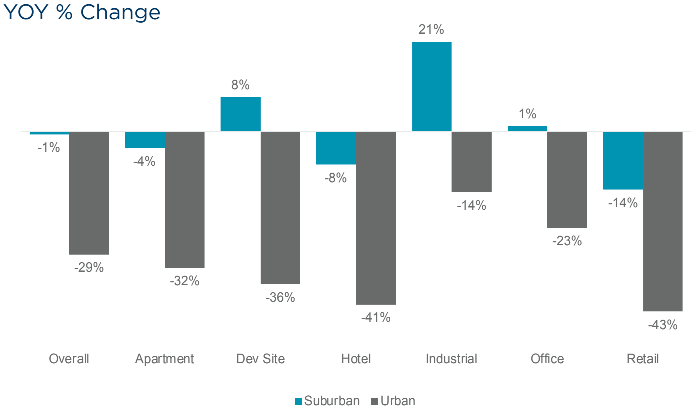
2017 was the first year since 2008—and only the fourth year since 2000—in which industrial overtook retail in volume traded. Industrial volumes increased 20% YoY—to $61B—while retail declined 19% to $54B, reflecting the divergent effects of eCommerce on investor demand for the respective product types.

[1]*Deals over $5 million.*

[2]*Core single asset sales market defined as transactions between $5 and $250 million. Megadeals includes single asset sales $250 million and above.*

INVESTMENT SALES VOLUME: 2017 VS. 2016

YOY % Change



Source: Real Capital Analytics
Deals over $5 million

Within industrial, both flex and warehouse properties experienced comparable increases in sales. **While the major industrial markets continued to attract the majority of transaction activity, capital shifted towards the secondary and tertiary markets on the margin** where volumes were up 25% and 23%, respectively, compared to 15% in the major markets. The top performing markets were Sacramento (+350%), Las Vegas (+215%), Washington, D.C. metro (+137%), Houston (+123%) and Charlotte (+85%).

Notwithstanding the above, industrial transaction sales slowed in the fourth quarter—down 31% QoQ—after a particularly blistering pace of activity in the third quarter—and 5% YoY. The deceleration was greater in the secondary markets than in the major industrial ones. Given the underlying drivers, this seems to be more of a pause than the beginning of a reversal in the recent trend.

Retail Continued Its Reformation

The decline in retail sales volumes has been driven by malls and power centers, which together were down 59% in volume for the year, and by urban/high street retail (down 24%). Competition from eCommerce, combined with an overbuilt retail sector, has resulted in many properties becoming functionally obsolescent. This has translated into lower values and volumes. On the other hand, marquee product has remained in high demand but is also highly priced, resulting in a gap between buyers and sellers that has also contributed to lower transaction volumes. By contrast, **strip center volumes ended the year flat overall, reflecting strong demand for what investors perceive to be eCommerce-resistant product,** notably grocery-anchored centers.

Fourth quarter activity seemed to challenge the trend in retail activity. Strip center volumes declined 11% QoQ, while high street (+17%), power center (+56%) and mall (+343%) sales all increased substantially. **This may mark the point where transaction volumes have found a floor and capital has begun to see value in available properties.** The pending Unibail-Westfield merger and Brookfield's ongoing effort to acquire the remainder of GGP point in this direction.

Private Capital and REITs Led the Way

Private investors accounted for 50% of acquisitions in 2017, up from 47% in 2016. **Private capital has shown itself to be the most adaptive to the maturing cycle environment, focusing on smaller transaction sizes, non-major markets, suburban subtypes and industrial.**

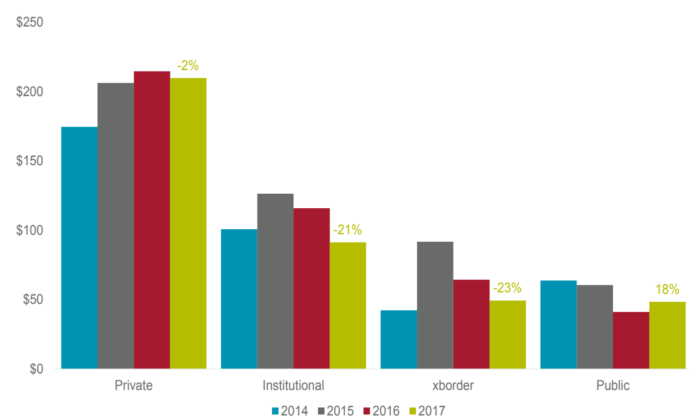
REITs were the only investor group to increase acquisition activity in 2017—up 19% YoY. Yet that figure understates the contribution of development to REIT capital deployment strategies. The increase in acquisitions was almost entirely attributable to purchases of industrial properties in the major markets, which rose from $2.6B in 2016 to $9.5B in 2017. In addition, major market retail acquisitions doubled from $2.7B to $5.4B during the same timeframe. The pace of purchases slackened, however, in the fourth quarter of 2017, down 33% QoQ, coincident with the broader slowdown in industrial sales.

Institutions and Foreign Capital Hesitated

Acquisitions by institutional investors declined 21% in 2017 from 2016, led primarily by an 84% fall-off in purchases in the first quarter with activity escalating through the remainder of the year. Institutional volumes shifted on the margin towards secondary markets for the year overall (-16% vs. -25% in the major metros) but this was likely to due to lack of product in the major markets. In the fourth quarter, major market acquisitions spiked 49% on increased purchases of CBD office and apartment properties (although the latter were mostly suburban properties).

ACQUISITION VOLUME BY INVESTOR TYPE 2014-2017

$ Billions



Source: Real Capital Analytics
Deals over $5 million

The cross-border share of acquisitions declined from 14.0% of transactions in 2016 to 11.7% in 2017 as purchases fell 23% YoY. Much of the slowdown (70%) was due to a lack of investors from China and Hong Kong as the effect of capital controls became evident in the second half of the year. This is not the complete story, however. Cross-border acquisitions excluding China/Hong Kong were still down

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10% YoY as investors from Qatar, Saudi Arabia, Kuwait, Germany and South Korea were less active than they had been previously. On the other side of the ledger, Canadian investors ($16.6B / +22% YoY) were highly acquisitive as were those from Singapore ($4.7B / +150%) and the Netherlands ($3.2B / +920%).

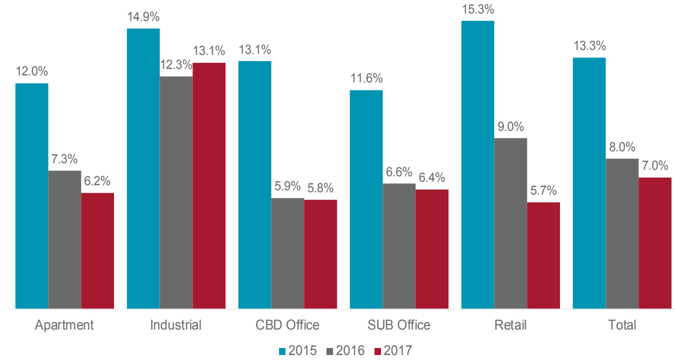
Amid this decline in cross-border sales, foreign investors were increasingly willing to invest in smaller markets. The share of secondary market acquisitions, as a percent of transactions, rose to 33% compared to 30% in 2016 and 23% in 2014. **Activity has also been shifting away from CBD apartment and retail and towards industrial and suburban multifamily** where transactions shares have increased to 19% (from 13% in 2016) and 11% (from 5% in 2016), respectively.

Returns Moderated

According to RCA, **prices across all property types increased 7.1% in 2017 compared to the 8.6% increase in 2016**. This moderation was seen across all property types, most significantly office. **Apartment and industrial properties experienced the greatest price increases**, rising 10.6% and 6.1%, respectively.

The **NCREIF property index of institutional returns registered a 7.0% total return in 2017, down from 8% in 2016,** as returns from capital appreciation slowed. Industrial continued to be the top performing product type and the only one to realize a greater total return in 2017 (13.0%) than in 2016 (12.3%). Office registered a total return of 6.0% (unchanged from 2016) and suburban office continued to outperform CBD office as higher income returns in the suburbs more than offset slightly lower capital appreciation. Multifamily returns decelerated to 6.2% with garden product outperforming high-rise again (as it has in recent years) with an 8.9% return compared to only 4.7% for high-rise. Retail returned 5.7% overall—down sharply from 9.0% in 2016. Returns fell across all retail subtypes, but most acutely for regional and superregional centers (by a ~500 basis points [bps]) and comparatively less for neighborhood and community centers (200-300 bps) and high-end fashion centers where returns were flat. Not surprisingly, these subtypes also boasted somewhat higher returns (community: 6.1%; fashion: 6.4%; neighborhood: 6.5%).

NCREIF NPI TOTAL RETURNS



Source: NCREIF, Cushman & Wakefield Research

What's in Store for 2018?

Our forecast calls for investment sales volumes to rise 2.0% in 2018. We expect a broad continuation of the themes that have been active in 2017, including relatively fewer megadeals in the major metro markets and, by extension, fewer trophy office, hotel and multifamily transactions than earlier in the cycle. Those transactions are to be replaced by smaller deals in the secondary and to some extent tertiary markets as well as a shift towards industrial and multifamily and suburban subtypes broadly where the combination of yields, pricing and fundamentals are more attractive at this point in the cycle.

As interest rates rise modestly, we could start to see more owners of trophy product in the major metros begin to realize the value of their properties through sales as opposed to refinancing. This creates an upside risk for an increase in large deals in 2018.

Conversations with institutional investors reveal significant improvement in sentiment and a strong desire to deploy capital. As we have documented in these reports, these investors have a tremendous store of dry powder: $165B at the time of this writing (end of January 2018). **2018 is the year that the weight of capital drives institutional transaction activity; the year will be characterized by a flexibility in terms of product and market that up to now has been more typical of private investors.**

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