CORNERSTONE

U.S. RESEARCH quarterly

June 2014

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The U.S. Economy

- The U.S. economy temporarily contracted in the first quarter, impacted by severe winter weather. Real GDP declined at an annualized rate of 1.0% (second estimate) in Q1 2014, dragged down by declines in private investment and net exports. On the positive side, consumption expanded to a 3% annualized rate and real GDP was up 2% on year-over-year basis.

- Second quarter economic releases portray a resilient and strengthening economy, albeit one that still face challenges (housing and long-term unemployment), that we expect to grow at 3% or above the rest of the year. Job growth is picking up, household wealth is rising, and policy uncertainty has essentially vanished from the news headlines.

- Despite Federal Reserve "tapering" of QE asset purchases, yields on 10 year Treasuries are down more than 50 bps this year through late May, supporting higher stock prices, lower mortgage rates and a rally in corporate and high yield bond prices. We expect 10 year Treasury yields to begin to slowly trend upward as the economy accelerates and global deflation concerns ease later this year. With the Fed shifting its policy stance away from targeted 6.5% unemployment and 2.5% inflation rates towards a more qualitative consideration of broad economic conditions, the Fed is not likely to raise policy (short-term) interest rates until at least this time next year.

Real Estate Investment Markets

- Real Capital Analytics reports property sales volume of almost $90 billion in 1Q 2014, up 15% over 1Q 2013. The Moody's/RCA Commercial Property Price Index (CPPI) increased 2.4% in the first quarter and 15% over the past year, with gains across all property sectors.

- Pricing and investor interest in core assets, and in major coastal markets, remains strong, though there is also increasing interest in core-plus and value added strategies, and non-coastal markets as the investment market recovery continues to mature.

Real Estate Benchmark Returns

- At 2.74% (1.31% income, 1.44% appreciation) 1Q 2014 NCREIF Property Index (NPI) returns surprised on the upside, 21 bps higher than in 4Q 2013. Retail (4.3%) strongly outperformed by a wide margin, driven by super-regional (6.79%) and regional (5.39%) malls, followed by industrial (2.75%).

- NCREIF Open End Diversified Core Equity (ODCE) fund index returns were 2.62% in 1Q 2014, down from 3.30% in 4Q 2013. ODCE returns trailed NPI, an odd outcome in an up-market, explained in large part by differences in frequency of NPI separate account property appraisals compared to ODCE properties. ODCE returns (14.24%) exceeded NPI returns (11.18%) over the past year.

- The NAREIT Equity REIT total return index was up 9.98% in 1Q 2014 and is up 4.99% in 2Q 2014 through May 23rd. Year to date the index is up 15.46% vs. 3.86% for the S&P 500.

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U.S. Economy & Real Estate Trends

U.S. economic fundamentals are strengthening, despite first quarter challenges from winter weather disruptions and continuing stresses from overseas events in Europe and China. With real GDP declining by 1 percent in the first quarter, the slowdown was dramatic but temporary, as more recent economic releases portray a resilient domestic economy with good prospects for accelerating and well aligned with our forecast for moderate growth this year. Corporate and household balance sheets are healthy, policy uncertainties which plagued confidence in previous years have diminished, and preconditions for Fed tightening have yet to be satisfied. Consumer confidence surveys from the University of Michigan and the Conference Board have both rebounded strongly, the latter reaching a six-year high in March. While consumers express concern regarding near-term prospects, expectations for the longer term economy continue to improve, buoyed by improving job prospects, rising home values, and low interest rates.

In contrast to the weak GDP report, and supporting our view that the first quarter pause was temporary, monthly U.S. employment gains have accelerated above expectations in recent months, vaulting to an estimated 288,000 in April, the largest monthly gain in over two years. Concerns regarding the implications of long-term unemployment, a falling labor force participation rate, and the lack of wage growth are all well-founded and are evidence of structural changes beneath the top-line employment numbers. Nevertheless, aggregate employment should finally move ahead of pre-recession peak level in the next few months

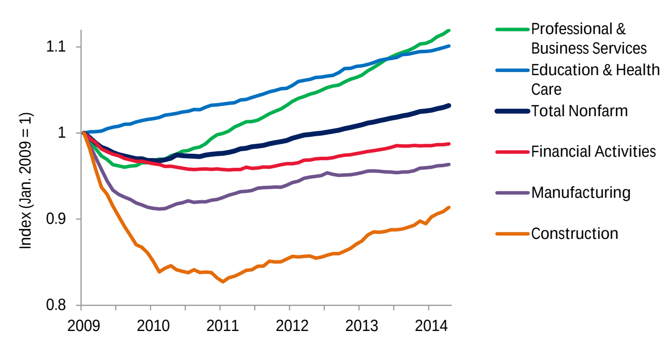
Commercial real estate space markets are in full recovery or expansion mode with some local supply imbalances evident. Overall space market conditions are broadly improving with more markets and sectors seeing vacancies at or below equilibrium levels supporting real rent growth. Capital market support for the asset class is expected to remain strong, with recent transaction and pricing trends reflecting an expanding investor base and an evolving investor appetite for real estate as interest rates bottom and both leasing fundamentals and access to debt financing improve.

U.S. Forecast Economic Performance

%	2013	2014	2015
Change in Real GDP	1.9	2.6	3.0
Employment Growth	1.6	1.9	2.2
Unemployment Rate	6.7	6.4	5.9
Change in Inflation (CPI)	1.5	1.8	2.0
Housing Starts (000s units)	930	1,000	1,250
Core Retail Sales Growth	4.5	5.0	5.1
10 Year Treasury	2.8	3.1	3.5
1 Month Libor	0.2	0.2	0.4

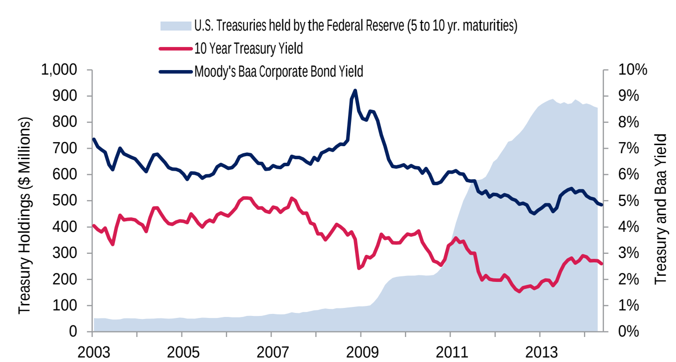
forecast [1]

Employment Picture is Improving
Lagging construction sector joining the recovery



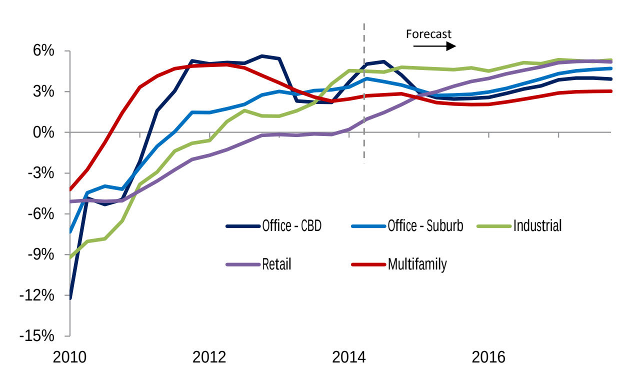
Source: Cornerstone, BLS (monthly data as of April 2014).

Despite "Tapering" QE Will Continue to Pressure Interest Rates
Recent decline in Baa corporate yields points to uptick in GDP growth rate



Monthly data through April 2014 plus average of daily May values through 5/20/14 for Treasury and Baa yields.
Source: Cornerstone, Federal Reserve Board.

Stage Set for Sustained and Broad-Based Rent Growth



Year to year % change in quarterly rent index (actual) and forecasts, 2010:1 - 2017:4
Source: Cornerstone based on data and forecasts from CBRE-EA (as of May 2014)

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Property Type Fundamentals & Capital Markets

Office: 1Q vacancy ↓10 bps to 14.8% [2]

Slow but broadening recovery continues, led by a 20 bp decline in CBD vacancy to 12.1%, pushing national vacancy back down to its long-run level. Suburban office vacancy held steady at 16.3%. Rent indices are rising nationally, and construction activity remains relatively quiet with just four million square feet of multi-tenant space delivered in the fourth quarter. About half the nation's major markets have recovered to pre-recession vacancy rates, and with the majority of new supply concentrated in a few markets, the office sector is well-positioned for near term occupancy and rent gains.

Apartment: 1Q vacancy ↓10 bps to 4.9% [2]

Robust demand kept pace with the increasingly active supply pipeline that saw more than 160,000 new units completed nationally in the past year. Even in some of the most active markets for new development (Austin, Seattle, and San Francisco) vacancy declined year-over-year. Investor interest in apartments remains strong with several recent transactions attracting prices above estimated replacement cost. While rents continue to rise in most markets, the pace of growth has slowed with expectations for a moderate increase in vacancy later this year.

Hotel: Occupancy ↑ 160 bps year to date [3]

Hotel markets shrugged off first quarter GDP weakness with gains across all chain scales, price tiers, and in most major markets. Overall national occupancy rose to 56.0%. Full service upscale and luxury chain scales occupancies ranged from 67% to 71%, approaching new peak levels in many cases. "Top 25" markets averaged 73.9% occupancy in March and RevPAR grew 6.2% (trailing 12 months) for top tier chain scales. With new supply coming off a ten-year low, we expect the sector may well outperform consensus' view for 5% to 6% RevPAR growth in 2014.

Industrial: 1Q availability ↓ 20 bps to 11.1% [2]

Strong, broad-based recovery continued with availability declining in 41 of 61 markets surveyed by CBRE-EA this quarter, and in all markets over the past year. To date only 16 metros have recovered to pre-recession occupancy rates, indicating room for further gains. With occupancies recovering and rents rising in most markets, supply activity is accelerating but remains relatively limited with Riverside and Dallas/Ft. Worth accounting for over one third of all supply activity nationally. In both cases, supply is aligned with strong demand growth, and our favorable near-term outlook for this sector is improving.

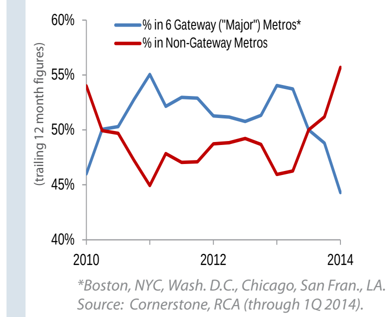
Retail: 1Q availability ↓10 bps to 11.9% [2]

While recovery in shopping center occupancies continues to lag other property sectors, prospects are improving. Occupancy gains were reported in 44 of 63 markets surveyed by CBRE-EA in the first quarter, and nationally availability is down 60 bps over the past year. New supply activity is essentially dormant, though the sector faces a rising and largely unmeasured obsolescence factor as retail chain formats evolve. While top line retail metrics are uninspiring, though having a more favorable outlook, investor interest and transaction pricing is very competitive for assets in proven locations with fundamentally sound trade area demographics.

Capital Market Focus

A strengthening and evolving investor appetite for real estate from both domestic and overseas capital sources continues to drive robust gains in transaction activity and broadening of investment market recovery. Property transactions volume totaled $87 billion in the first quarter, up 15% over last year, with price gains across all property sectors. Retail property transactions led with almost $23 billion in total volume. Office volume followed closely, with both CBD and suburban properties attracting more capital. April saw nearly $26 billion in transactions, up 23% over last year, although gains were attributable to a number of large portfolio sales, a theme that is likely to continue owing to the weight of capital looking to invest. We expect the pace of offerings and transactions to continue through 2014, and the ULI Consensus Forecast projects an 11% increase in sales volume this year to $400b.

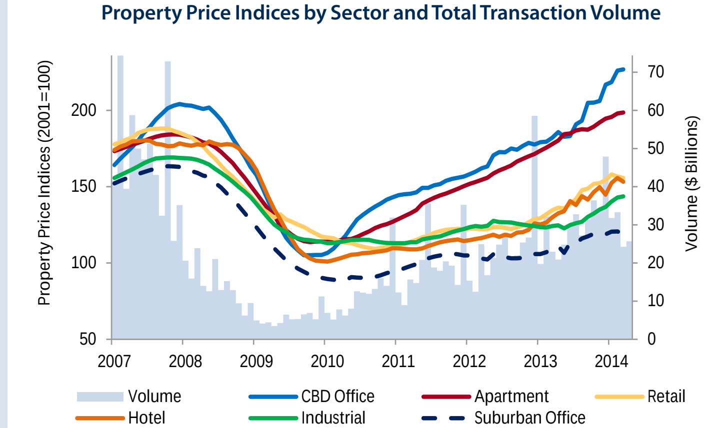
Investment Scope Broadens
Share of dollar transaction volume



**Boston, NYC, Wash. D.C., Chicago, San Fran., LA.*
Source: Cornerstone, RCA (through 1Q 2014).

The national, transaction-based Moody's/RCA Commercial Property Price Index (CPPI) increased 2.4% in 1Q 2014 and 15% over the past year. The aggregate index is now 6.3% below its November 2007 peak, although significant variation in recovery across both markets and property sectors remain. Recovery in the aggregate index has been led by the CBD office and apartment sectors, particularly in the major "Gateway" Markets, that have more than fully recovered. Suburban office, and to a lesser extent industrial, retail and hotel, price recoveries have lagged. We expect the gap in performance across the various sectors to narrow as the economic and real estate cycles mature and investment strategies and valuations adapt, with growing participation by private investors, as evidenced by more transactions and improved pricing of smaller properties, as well as volume gains in secondary markets taking market share from Gateway metros.

Property Price Indices by Sector and Total Transaction Volume



Monthly through March 2014 for Moody's/RCA Commercial Property Price Index (CPPI) data and April 2014 for transaction volume.

Capital Markets

Market Return Comparison

Total Returns	Q1 2014	1-year	3-year	5-year	10-year
NCREIF Property Index	2.7%	11.2%	11.7%	7.9%	8.7%
FTSE NAREIT-Equity Index [7]	10.0%	4.2%	10.7%	28.2%	8.2%
BofA/ML U.S. Corp/Gov't Bond Aggregate Index [6]	2.1%	-0.4%	4.2%	5.2%	4.4%
MSCI EAFE Gross USD Index [6]	0.8%	18.1%	7.7%	16.6%	7.0%
Russell 2000 Index [6]	1.1%	24.9%	13.2%	24.3%	8.5%
S&P 500 Index	1.8%	21.9%	14.7%	21.2%	7.4%
Wilshire 5000 Index	2.0%	22.4%	14.4%	21.7%	7.9%

Market Yields and Rates

Market Yields and Rates (%)	Q1 2014	Q4 2013	1-year
10-year Treasury Yield [5]	2.8%	2.7%	2.6%
LIBOR - 3 month [5]	0.2%	0.2%	0.3%
BofA/ML U.S. Corp /Gov't Bond Aggregate [6]	2.1%	2.1%	2.1%
NCREIF Potential Distribution (12-mo trailing) [1,4]	3.6%	3.7%	3.7%
FTSE/NAREIT-Equity Dividend Yield (12-mo forward) [7]	3.9%	3.9%	3.8%

Private Real Estate Performance Summary

NCREIF Property Sector Index Total Returns [4]	Q1 2014	1-year	3-year	5-year	10-year
Apartment	2.2%	10.0%	11.9%	9.1%	8.3%
Hotel	0.8%	7.3%	8.2%	4.5%	6.9%
Industrial	2.8%	12.6%	12.3%	7.3%	8.2%
Office	2.2%	10.2%	10.7%	6.6%	8.2%
Retail	4.3%	13.5%	13.0%	9.4%	10.2%
NCREIF Property Index	2.7%	11.2%	11.7%	7.9%	8.7%

Public Real Estate Performance Summary

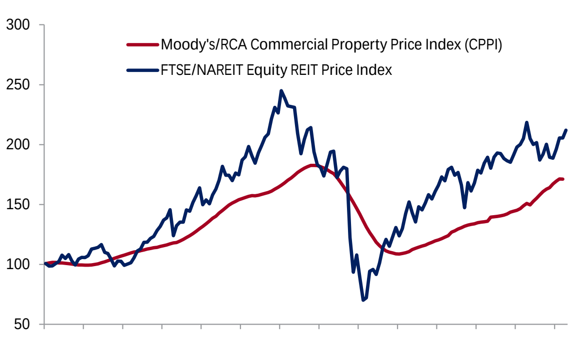
NAREIT Equity Sector Index Total Returns [7]	Q1 2014	1-year	3-year	5-year	10-year
Office/Industrial	11.1%	7.0%	8.4%	26.0%	4.6%
Retail	8.9%	3.8%	14.7%	33.4%	7.1%
Residential	13.7%	6.5%	7.5%	29.1%	11.1%
Lodging	5.8%	18.4%	9.3%	38.0%	5.4%
Healthcare	9.4%	-11.3%	9.0%	23.4%	11.0%
Diversified	7.0%	2.6%	6.3%	26.2%	6.6%
FTSE/NAREIT Equity Index	10.0%	4.2%	10.7%	28.2%	8.2%

Real Estate Pricing

Endnotes and Data Sources

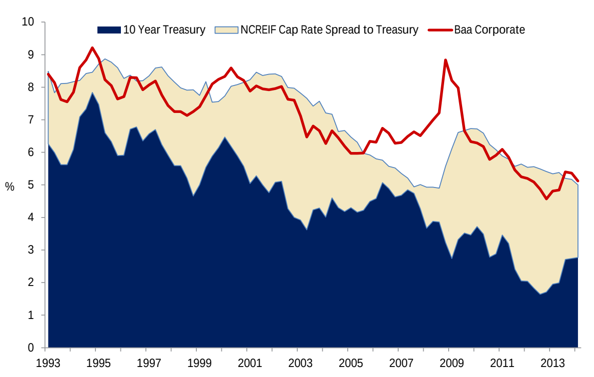
1 Cornerstone Research
2 CBRE Econometric Advisors
3 Smith Travel Global
4 NCREIF
5 Moody's Economy.com
6 Morningstar
7 NAREIT

Property and Equity REIT Price Indices



Monthly data. CPPI extends through March 2014, REIT index through April 2014.
Source: Moody's Investor Services, RCA, NAREIT, Cornerstone.

NCREIF Cap Rate vs 10 Yr Treasury & Baa Corporate Bond Yields



Quarterly data through 1Q 2014
Source: Cornerstone, NCREIF, Federal Reserve Board.