2013 Marquette University
Real Estate Strategies Conference
Economic Forecast

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Is the Midwest a value proposition or structurally out of favor?

CoStar Commercial Repeat Sales Price Index, August 2013.
Which property type provides the greatest opportunity?

CoStar Commercial Repeat Sales Price Index, August 2013.
Or should one forgo the Midwest markets for the lower cap rate prime markets?

CoStar Commercial Repeat Sales Price Index, August 2013.
The Fundamentals: Growth
GDP Growth

Real Gross Domestic Product (GDPC1)
Source: U.S. Department of Commerce: Bureau of Economic Analysis

Shaded areas indicate US recessions.
2013 research.stlouisfed.org
Economic growth in Wisconsin and Illinois has lagged that of the U.S.


Source: Federal Reserve and Marquette University.
Nationally, jobs are making a slow recovery

Source: WSJ, September 6, 2013.
The U.S. has recovered about 2/3rds of the jobs lost in the recession.
While the unemployment rate has dropped to 7.3%, how do we account for labor force participation rates?
What part of the drop labor force participation rates is retiring baby boomers?

Source: WSJ, September 6, 2013.
The potential for increased hiring looks promising.
Wisconsin and Illinois employment growth has lagged that of the U.S.

Source: U.S. Department of Labor and Marquette University.
Expected population growth for Wisconsin and Illinois is well below the 29% national average 2000-2030

<table>
<thead>
<tr>
<th></th>
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</thead>
<tbody>
<tr>
<td>New Mexico</td>
<td></td>
<td>280,662</td>
<td>15.4</td>
<td>26</td>
</tr>
<tr>
<td>Missouri</td>
<td></td>
<td>834,962</td>
<td>14.9</td>
<td>27</td>
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<tr>
<td>Wisconsin</td>
<td>787,089</td>
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<td>14.7</td>
<td>28</td>
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<td>Oklahoma</td>
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<td>462,597</td>
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<td>Connecticut</td>
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<td>8.3</td>
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<tr>
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<td>Michigan</td>
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<td>755,728</td>
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<tr>
<td>Louisiana</td>
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<td>333,657</td>
<td>7.5</td>
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Source: U.S. Census Bureau.
Inflation
Recently, inflation has been well-behaved . . . .
.... with ample labor, unit labor costs are also well-behaved ....
and commodity prices appear to be stable, which should keep inflation in check.
Housing
Existing home inventories are low and shrinking.
Real house prices bottomed out in 2012
Wisconsin homes sold and median prices up, but lagging national price statistics

<table>
<thead>
<tr>
<th>REGION</th>
<th>HOMES SOLD</th>
<th>% CHANGE</th>
<th>MEDIAN PRICE</th>
<th>% CHANGE</th>
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<tbody>
<tr>
<td></td>
<td>2012</td>
<td>2013</td>
<td></td>
<td>2012</td>
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<tr>
<td>Southeast</td>
<td>2,241</td>
<td>2,711</td>
<td>+21.0</td>
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<tr>
<td>South central</td>
<td>1,362</td>
<td>1,626</td>
<td>+19.4</td>
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<td>West</td>
<td>605</td>
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<tr>
<td>Northeast</td>
<td>1,070</td>
<td>1,141</td>
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<td>$123,600</td>
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<tr>
<td>Central</td>
<td>369</td>
<td>413</td>
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<td>North</td>
<td>548</td>
<td>609</td>
<td>+11.1</td>
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Note: Region totals don't match state totals.

Source: Wisconsin Realtors Association

Source: Milwaukee Journal Sentinel, August 13, 2013, page D1
U.S. homeownership reverts to the historic mean.
Real Median Household Income

Source: NYT, August 21, 2013.
Freddie and Fannie continue to maintain tight underwriting standards for mortgage loans

Source: Federal Reserve Flow of Funds.
Keeping first-time homebuyers out of the market

New Home Sales by Price

Percent of Sales

<$150K  $150K to $200K  $200K to $299K  $300K to $399K  $400K+

Jan-02 Jan-03 Jan-04 Jan-05 Jan-06 Jan-07 Jan-08 Jan-09 Jan-10 Jan-11 Jan-12

http://www.calculatedriskblog.com/
Commercial Real Estate
It appears as if commercial real estate transaction volume is back, what do you see?
The commercial real estate debt markets remain tepid for non-multifamily product.
Banks are easing standards and commercial real estate loan demand is growing.

Source: Federal Reserve Flow of Funds.
Property Markets
Retail
Real retail sales fundamentals are solid but the consumer has headwinds with payroll and affordable healthcare taxes with new limits on unemployment benefit.
Real average wage increases have fallen and most all wage growth is concentrated in upper income levels.

Household debt service levels provide dry spending powder

Household Debt Service Payments as a Percent of Disposable Personal Income (TDSP)
Source: Board of Governors of the Federal Reserve System

Shaded areas indicate US recessions.
2013 research.stlouisfed.org
Spending has shifted to durable goods, which signals consumer confidence.
Multi-channel retailing the new normal (internet sales for Walmart $7.7B/$473B and for Best Buy $3.3B/$48B)

Source: WSJ, August 28, 2013, page A1..
Apartments
Multifamily starts averaged 360,000 since 1956, in July 2013 there were 290,000 starts.
Pent-up household growth not yet tapped

Source: Joint Center for Housing Studies, State of the Nation’s Housing: 2013.
Another look at pent up household demand

Household Growth has Lagged Adult Population Growth Since the Downturn

Annual Growth Rate (Percent)

Source: Joint Center for Housing Studies, State of the Nation’s Housing: 2013.
Lower real income growth generate greater renter demand

Most Types of Households Have Seen Their Real Incomes Decline over the Past Decade

Source: Joint Center for Housing Studies, State of the Nation's Housing. 2013.
Minorities and seniors will drive most all household growth in the coming decade

Source: Joint Center for Housing Studies, State of the Nation’s Housing: 2013.
Midwest has among the best multifamily occupancy rates

Rental Markets in Most Large Metro Areas Are Tight or Tightening

Source: State of the Nation’s Housing Market, 2013, Joint Center for Housing Studies of Harvard University.
Office and Industrial
Capacity utilization remains solid, which is comforting to industrial space owners.
Manufacturing hours worked a solid signal for industrial markets.

The U.S. labor continues to be highly competitive

Source: Economist, May 4, 2013, page 89..
Boston Consulting Group projects that U.S. manufacturing increase by $70-115 billion annually by the 2020

Oil boom shrinks trade deficit 22%

Corporate profits remain strong . . . .
However, demand drivers remain weak.
Office fundamentals remain challenged

• During the second quarter of 2013 office occupancy increased by 7.2 million square feet (0.2%). . . . that was the biggest increase since the economy began slowing in 2007.

• Overall U.S. vacancy rate stayed flat at 17% in the second quarter of 2013, down from a post-recession peak of 17.6% reached in mid-2010.

Source: WSJ, July 8, 2013, page B3.
What’s your strategy?

So what’s your strategy given:

• Equity capital market preferences
• Debt capital market preferences
• Growth fundamentals
• Demographic shifts
• Property type fundamentals
Equity Investment Strategies

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September 12, 2013
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