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MAY 31, 2018



SIX MYTHS THAT ARE SHAPING OUR MARKETS

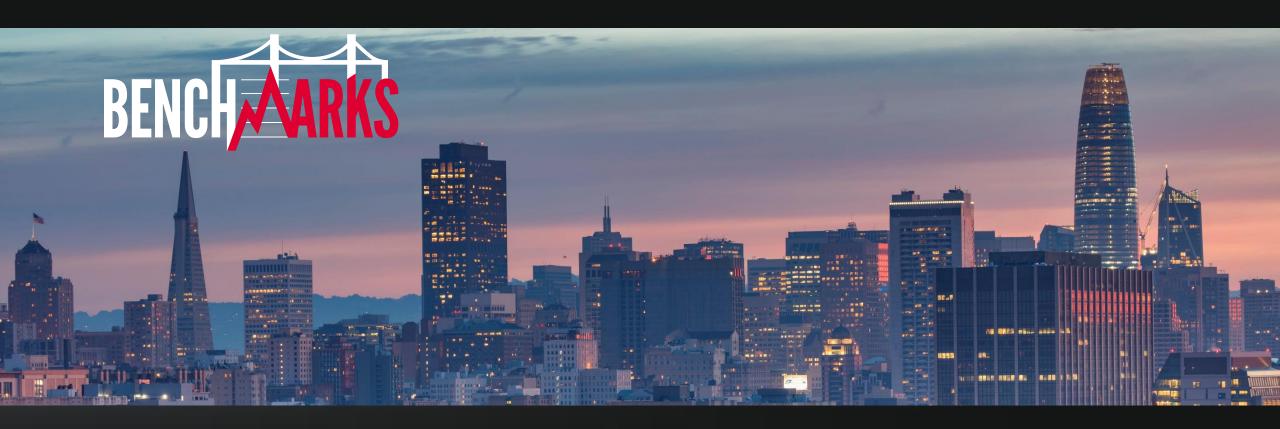
- (1.) Foreign investors have soured on U.S. commercial real estate
- 2.) Millennials are the future of apartment demand
- 3. Brick-and-mortar retail is being replaced by e-commerce
- 4. Workplace design is primarily about efficiency and cost control
- 5. Older, close-in industrial product is often vacant and obsolete
- 6. Suburban office locations are no longer desirable



Available for download soon at ngkf.com





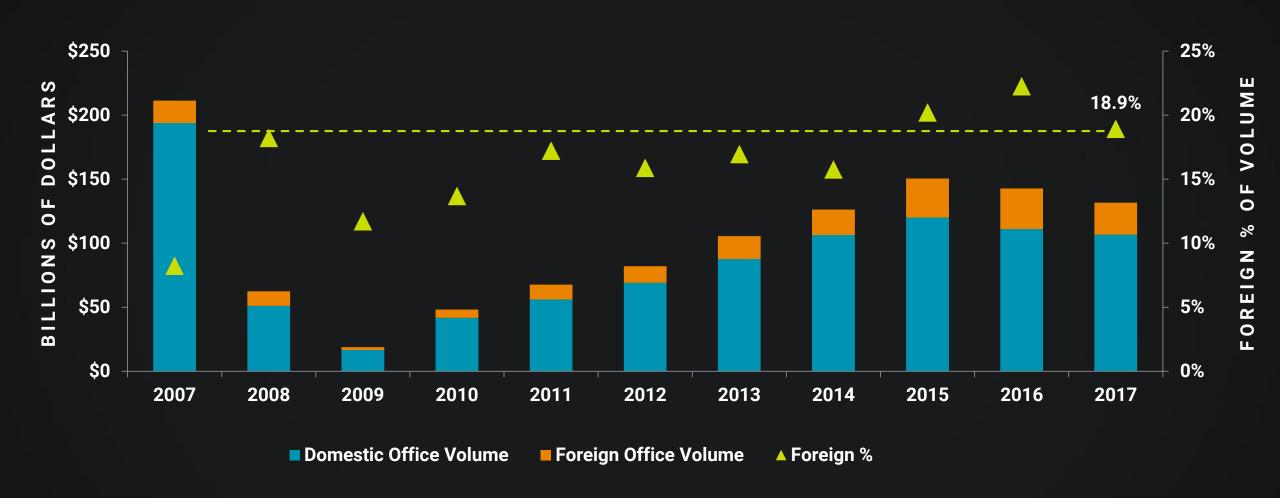


MYTH #1:

FOREIGN INVESTORS

HAVE SOURED ON U.S. COMMERCIAL REAL ESTATE

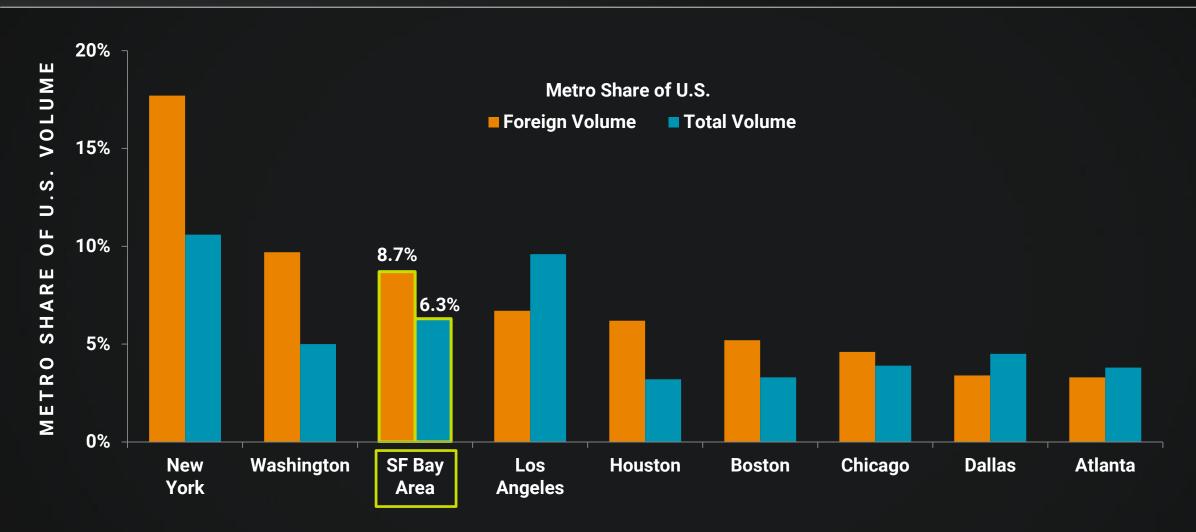
Foreign vs. Domestic Office Volume | United States



Source: Data provided by Real Capital Analytics, analysis by NKF Research; May 2018



Share of Foreign and Total U.S. Sales Volume | Major U.S. Metro Areas | All Property Types | 2017



Source: Data provided by Real Capital Analytics, analysis by NKF Research; May 2018



Investment Opportunities Still Abound in the Bay Area

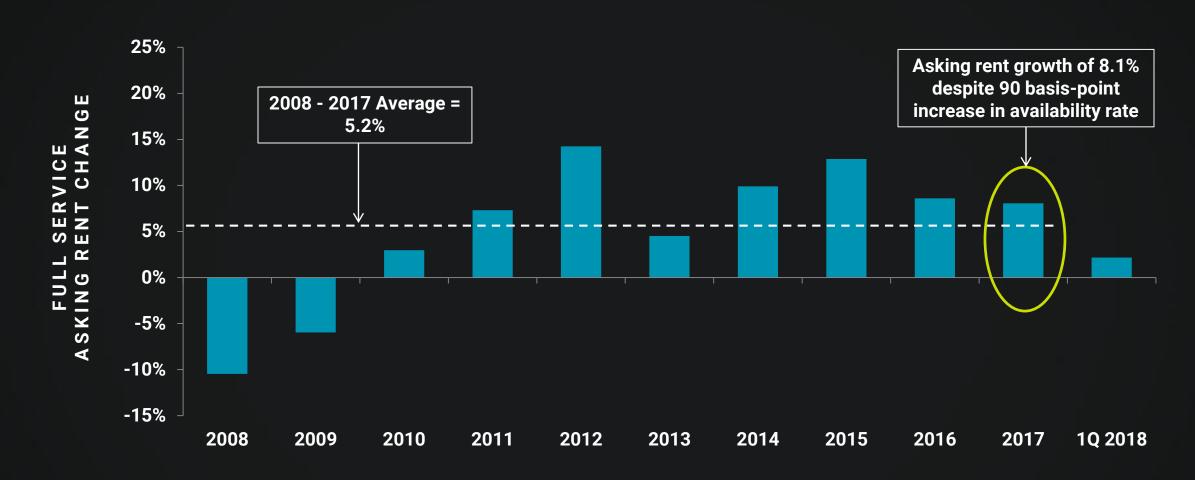
RERC Value vs. Price Index Top Investment Opportunities for 2018 Among Primary Markets

Office		Apartments	
1. Seattle	6. Washington	1. Seattle	6. Boston
2. Denver	7. Los Angeles	2. Atlanta	7. Washington
3. San Jose	8. Chicago	3. Denver	8. Los Angeles
4. Atlanta	9. New York	4. San Jose	9. Orange County
5. San Francisco	10. Boston	5. San Francisco	10. New York

Source: RERC, NKF Research; May 2018



Bay Area Office Asking Rent Change Rent Growth Present Even With Rising Availability





The "Smart Money" and Bay Area Capital Markets

- Smart money is continuing to invest in U.S. commercial real estate, particularly in gateway markets like the Bay Area, because of its superior investment potential over stocks (notwithstanding Chinese capital controls)
- Last year, West Coast markets surpassed East Coast markets in total sales volume; investors are recognizing the strength in this region's fundamentals, even late in the cycle
- With a lot of prime assets having traded already during this cycle, investors
 are migrating toward the suburbs in a search for yield

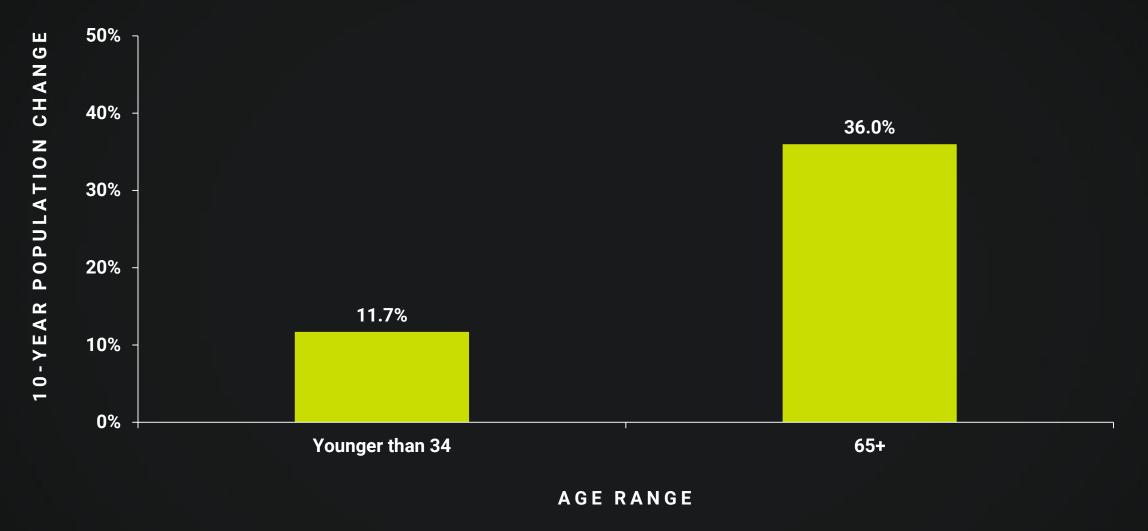




MYTH #2:

MILLENNIALS ARE THE FUTURE OF APARTMENT DEMAND

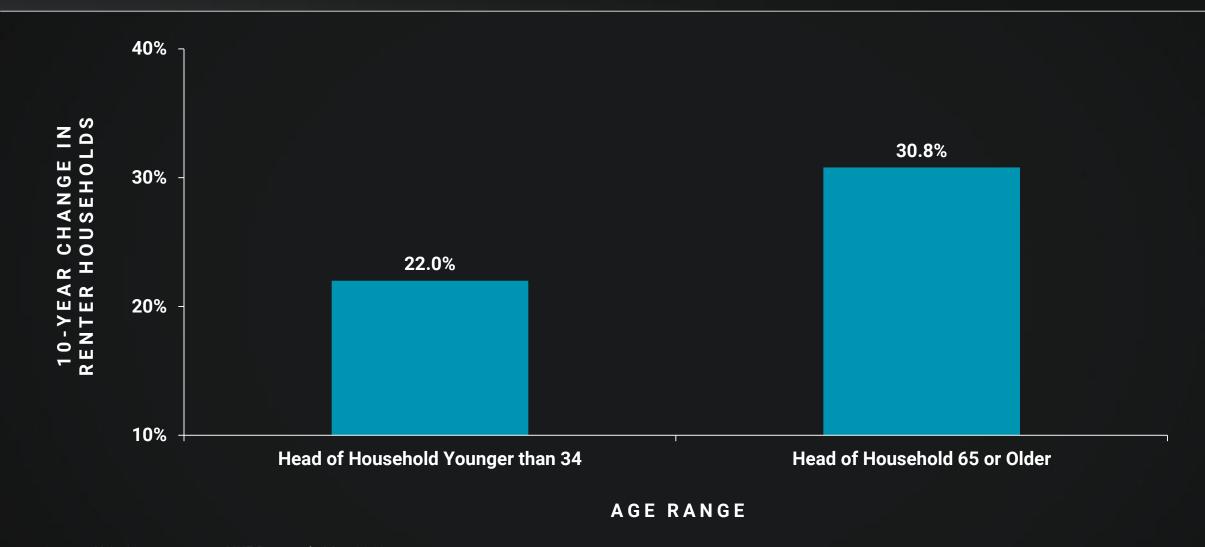
Population Change by Age Group | Bay Area | 2006 - 2016



Source: U.S. Census Bureau, NKF Research; May 2018



Change in Renter Households by Age Group | Bay Area | 2006 - 2016



Source: U.S. Census Bureau, NKF Research; May 2018



Baby Boomers and Seniors are Trading Landscaping for Lifestyle



VS.



Source: Zacs Garden, Vi at Palo Alto, NKF Research; May 2018

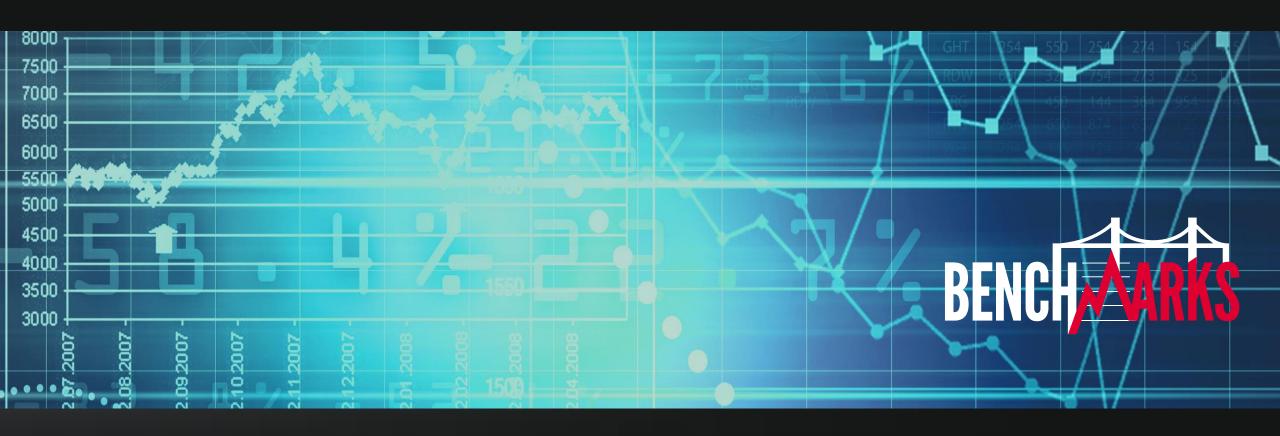


The "Smart Money" and Bay Area Multihousing

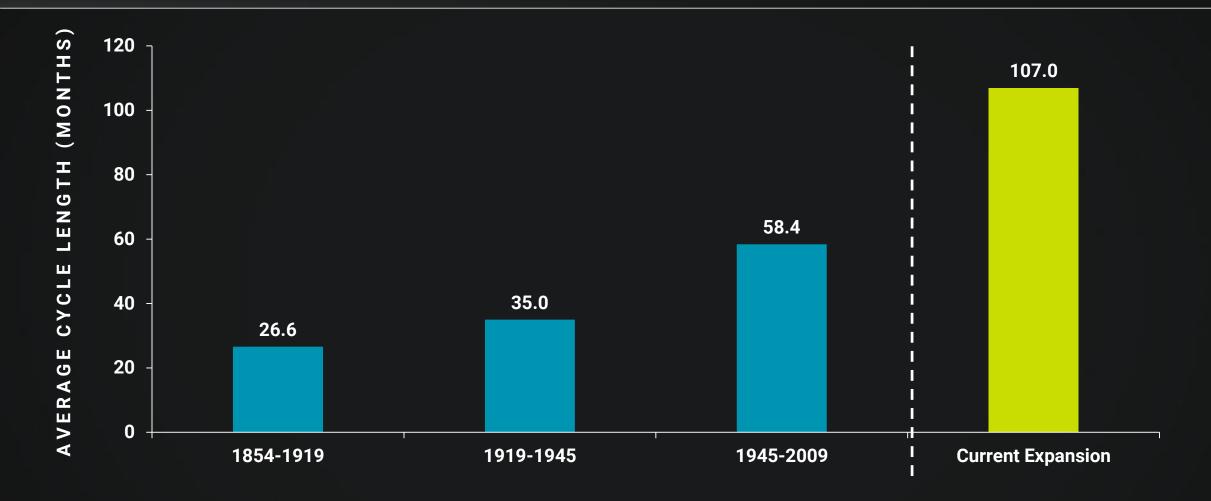
- Design larger units that can accommodate big furniture, more storage, extra bedrooms for the grandchildren
- The luxury market is strong but also consider affordability some retirees
 are seeking to make their resources go a long way
- Focus on flexibility today's popular micro-units may require retrofitting as tenant demand undergoes a generational shift







Average Length of U.S. Expansion Cycles



Source: National Bureau of Economic Research, NKF Research; May 2018



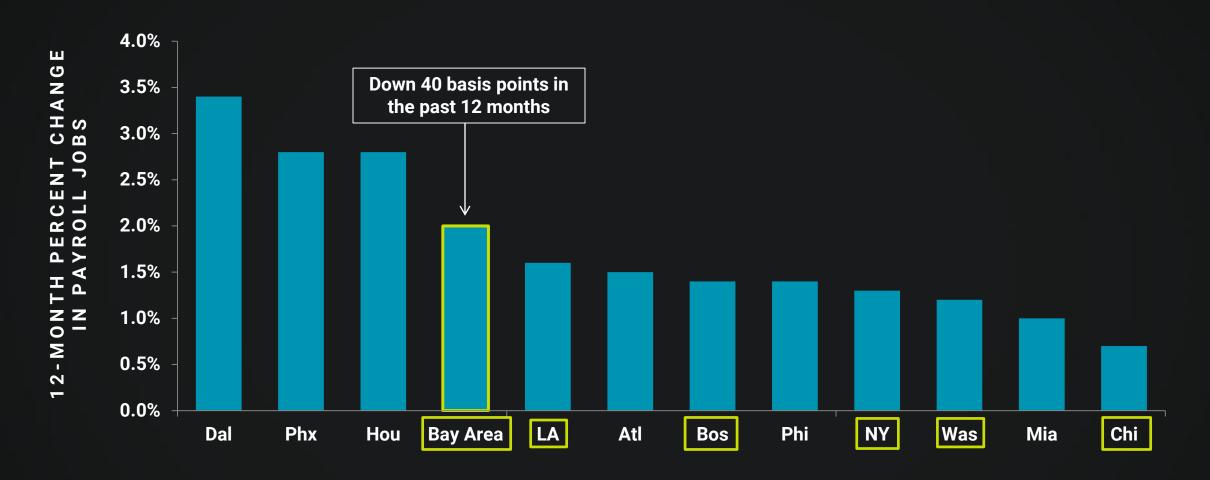
Potential Causes of the Next Recession | United States

- Over-tightening by the Fed (too many interest rate hikes too quickly)
- Energy or financial crisis
- Geopolitical crisis (war or terrorist attack)
- Insufficient productivity growth to increase corporate profitability
- Insufficient wage growth to keep up with inflation
- Sharp increase in deficit spending
- Tariff war breaks out

Source: MIT Technology Review, Brookings, NKF Research; May 2018



Payroll Job Change for Major U.S. Metro Areas | 12 Months Ending April 2018



Note: Bay Area includes San Francisco/East Bay and San Jose metro areas Source: U.S. Bureau of Labor Statistics, NKF Research; May 2018



Sample of 2017-2018 Office Expansions in the Bay Area



2.4+ MSF of Bay Area leases since start of 2017



1.3 MSF of Bay Area leases since start of 2017



736,000 SF The Exchange on Sixteenth



594,000 SF Chase Center



554,000 SF of Bay Area leases since start of 2017

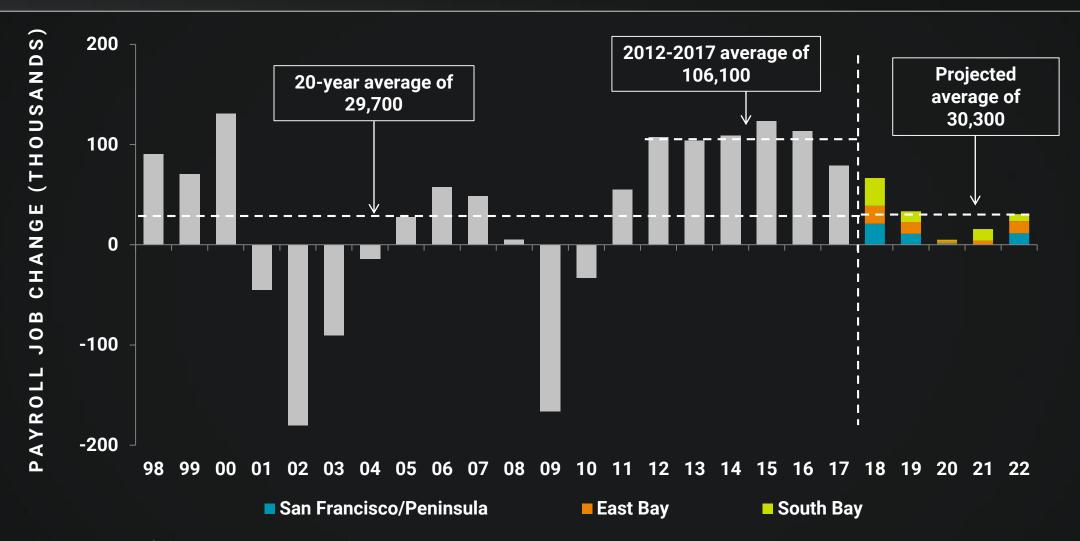


287,000 SF 650 Townsend

Source: Bisnow, The Mercury News, Stick PNG, NKF Research; May 2018



Bay Area Job Growth Likely to Remain Sturdy but Decelerate



Source: Moody's, U.S. Bureau of Labor Statistics, NKF Research; May 2018



The "Smart Money" and the Bay Area Economy

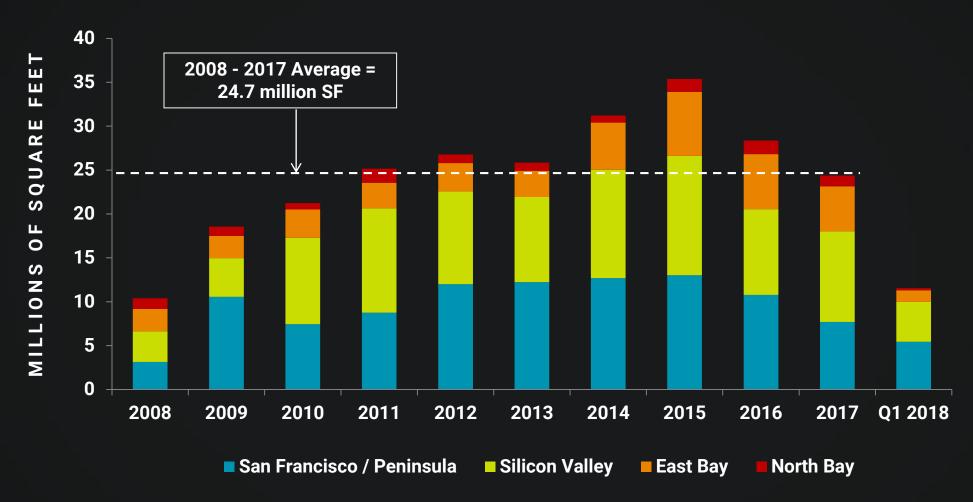
- Tech sector will help insulate Bay Area from next recession; technology is now more of a need than a want
- The smartest companies are creating superior workplaces to differentiate themselves at a time when qualified labor is hard to find
- The Bay Area has some of the lowest unemployment rates in the nation, but housing affordability continues to be a concern; smart money is focused on increasing productivity and work-life balance in order to retain talent

Source: Moody's, NKF Research; May 2018





Gross Absorption | Major Jurisdictions

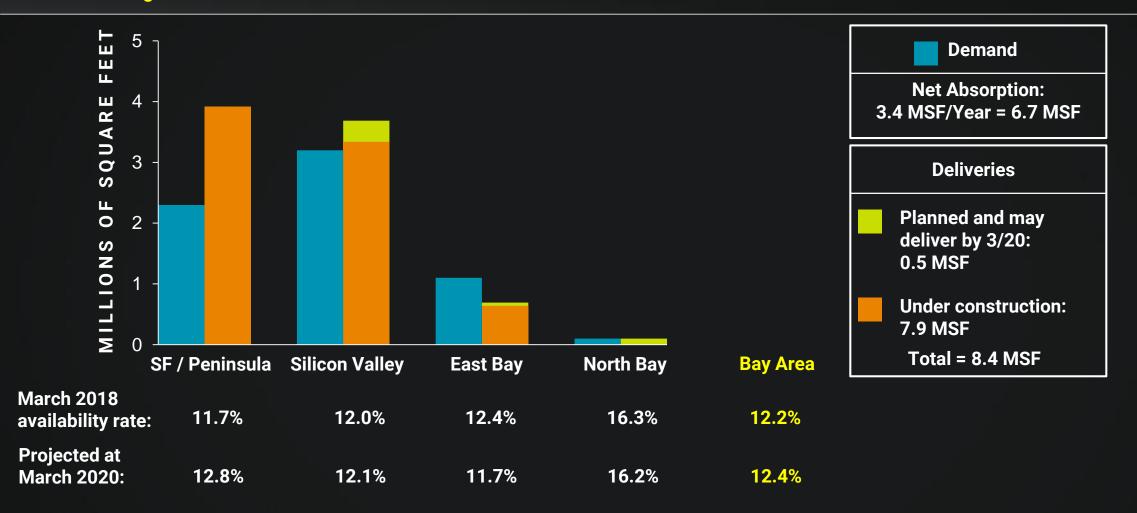


Note: Silicon Valley includes South Peninsula and South Bay

Source: CoStar, NKF Research; May 2018



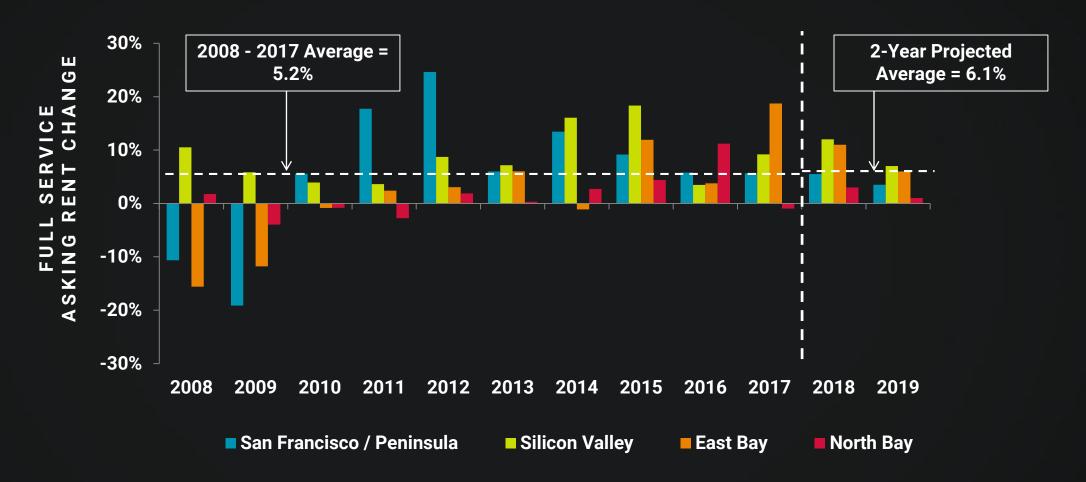
Projected Demand and Deliveries | Major Jurisdictions 2 Years Ending March 2020



Note: Demand projections take into account projected employment growth, changes in space utilization, current tenant requirements in the market, and historical trends. Net absorption represents the net change in occupied space, not gross demand. Deliveries exclude projects built for owner-occupancy. Source: NKF Research; May 2018



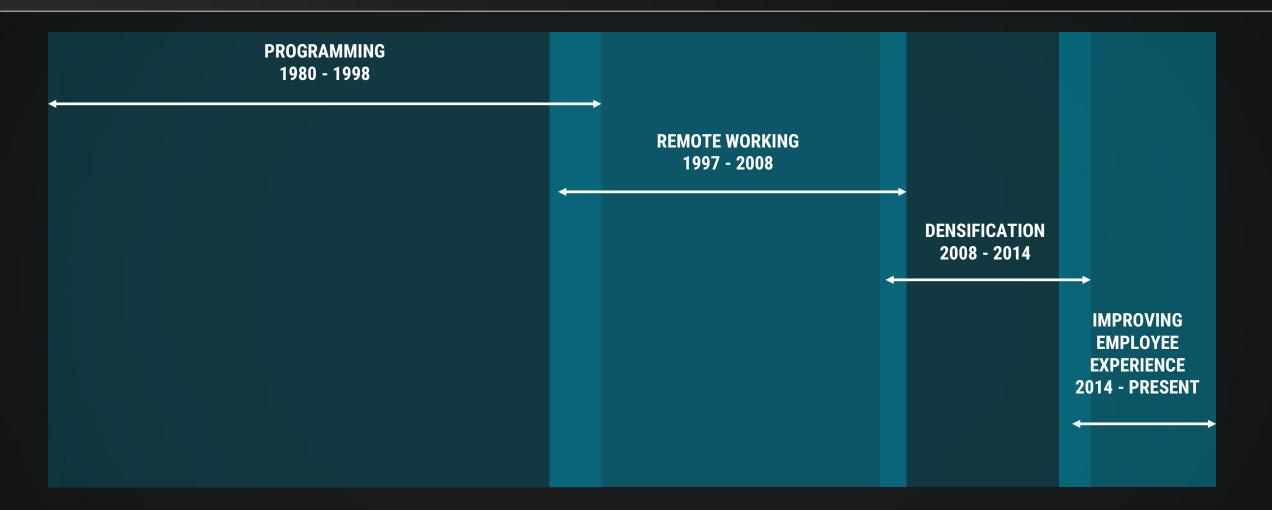
Projected Asking Rent Change | Major Jurisdictions



Note: Silicon Valley's average asking rent rose in 2008 and 2009 due to delivery of new product after a period of few deliveries Source: NKF Research; May 2018



U.S. Employment and Dominant Workplace Trends





The "Smart Money" and the Bay Area Office Market

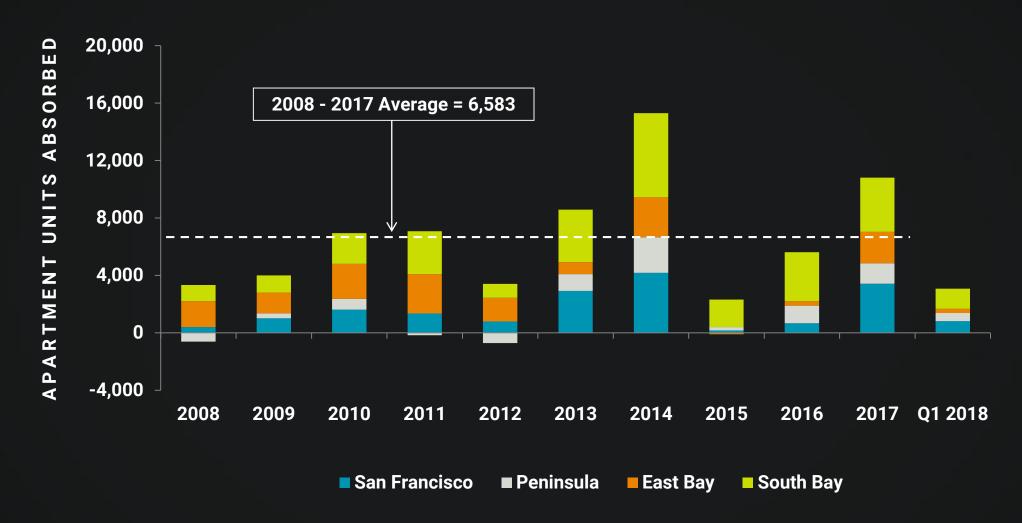
- Enhance asset performance by helping tenants improve their productivity;
 design space with the employee experience in mind
- Mixed-use, amenity-rich suburban product is gaining favor with tenants who do not want commutes to downtown but are seeking an activated environment
- Focus on infill in tight markets and transit-oriented development







Net Absorption | Major Jurisdictions



Source: Axiometrics, NKF Research; May 2018



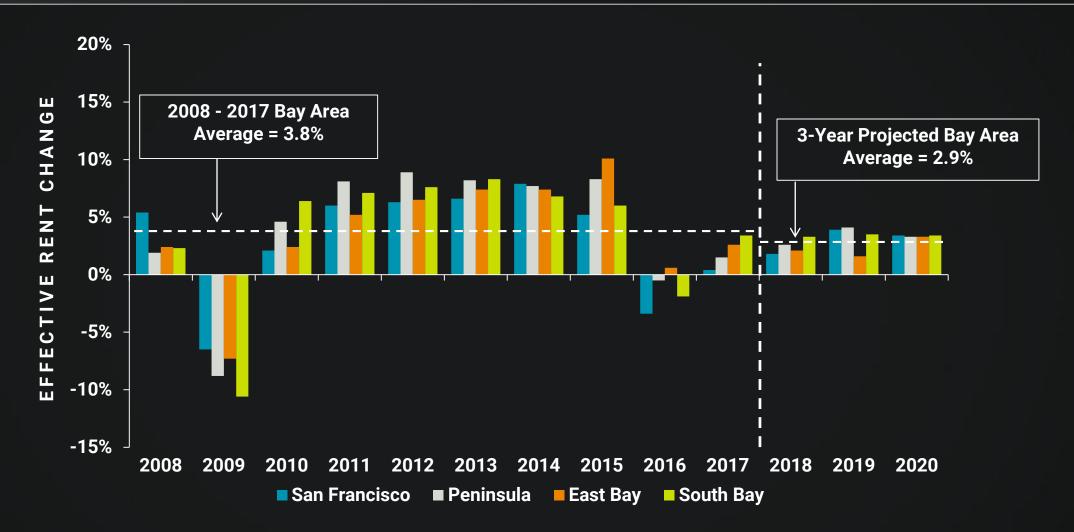
Projected Demand and Deliveries | Major Jurisdictions 3 Years Ending March 2021



Note: Net absorption represents the net change in occupied space, not gross demand. Includes market rate units at projects of 50 or more units. Source: Axiometrics, ARA Newmark, NKF Research; May 2018



Projected Effective Rent Change | Major Jurisdictions



Source: Axiometrics, ARA Newmark, NKF Research; May 2018



The "Smart Money" and the Bay Area Apartment Market

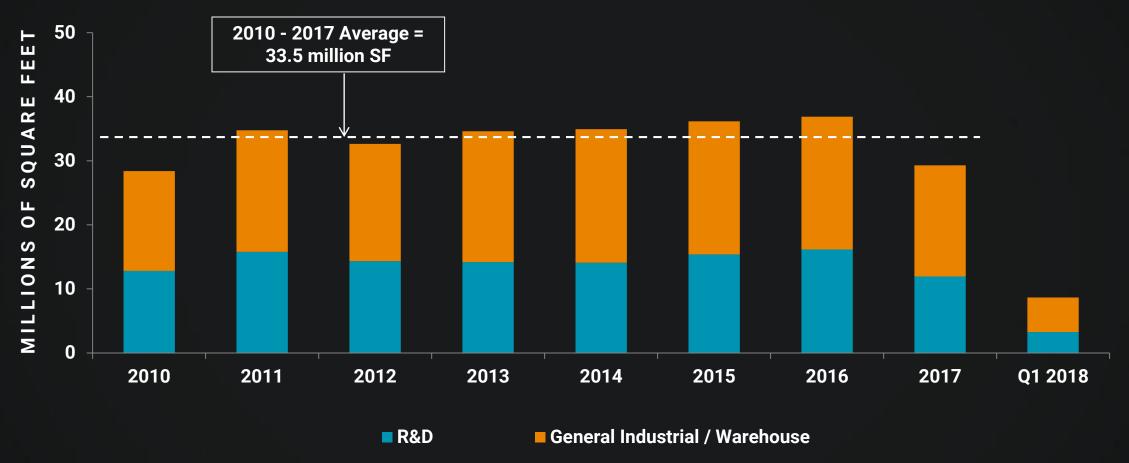
- Target both millennials and boomers/seniors to maximize potential demand in an evolving market
- Provide service amenities that improve productivity of work-at-home tenants
- Capitalize on the need for quality workforce housing renovate well-located
 Class B assets where projects will pencil







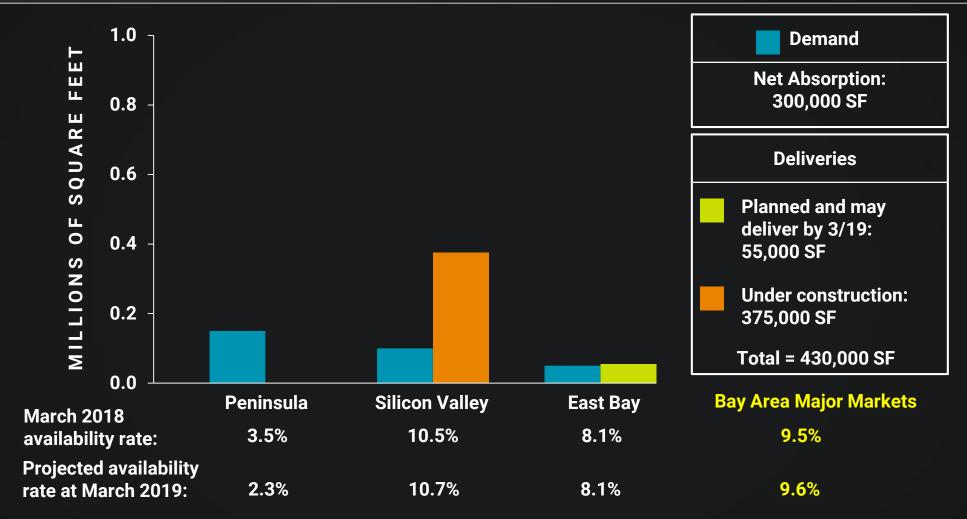
Gross Absorption - All Industrial Space



Note: Absorption data for all types of industrial space includes Peninsula, Silicon Valley, and East Bay Source: NKF Research; May 2018



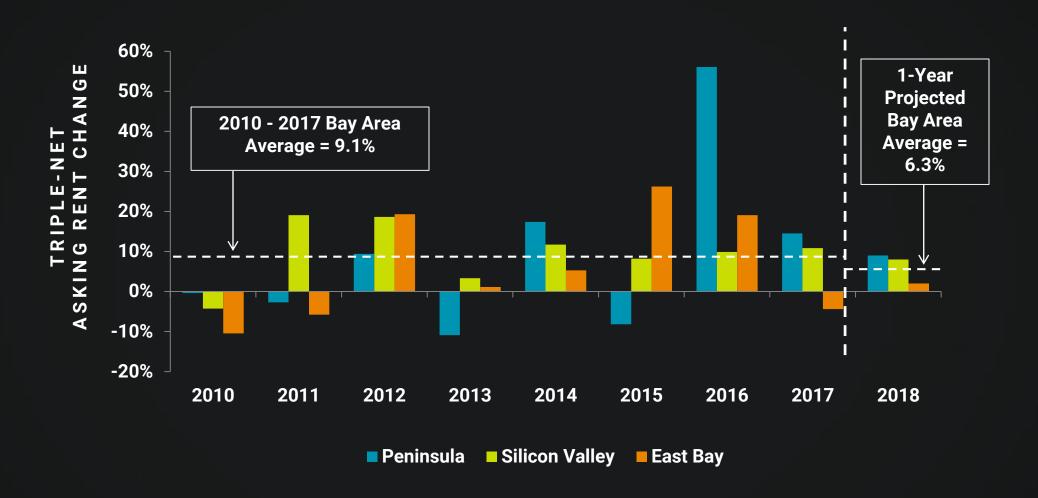
Projected Demand and Deliveries for <u>R&D</u> Space | Major Jurisdictions 1 Year Ending March 2019



Note: Demand projections take into account projected employment growth and historical trends. Net absorption represents the net change in occupied space, not gross demand. Source: NKF Research; May 2018

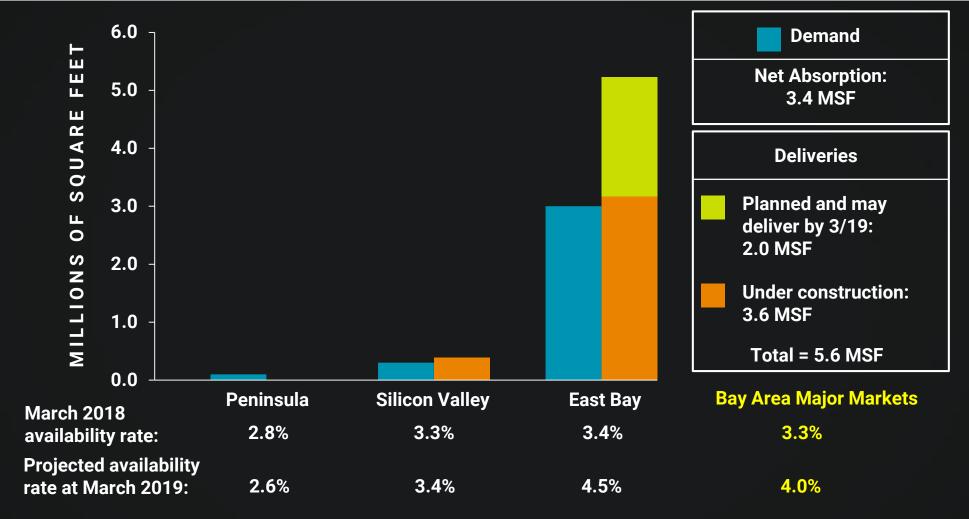


Asking Rent Change for R&D Space | Major Jurisdictions





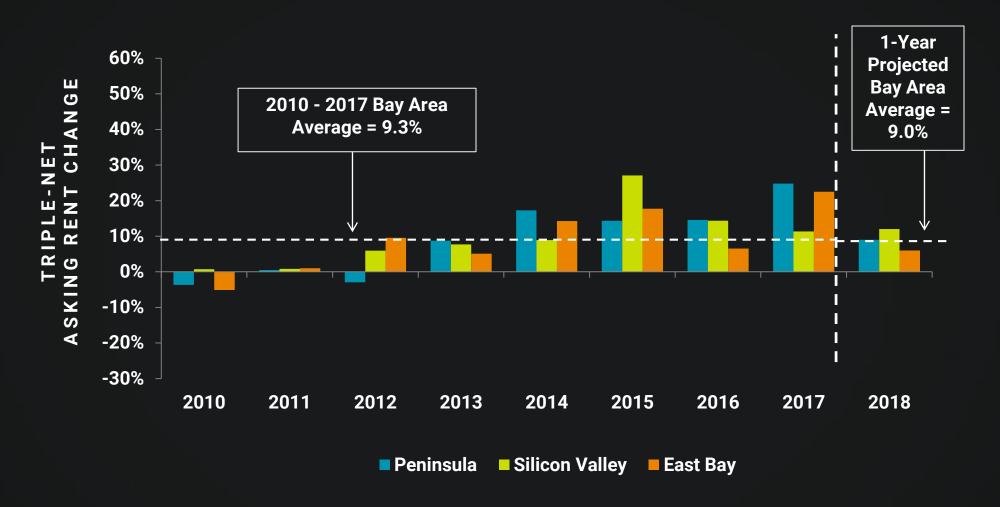
Projected Demand and Deliveries for <u>General Industrial / Warehouse</u> Space | Major Jurisdictions 1 Year Ending March 2019



Note: Demand projections take into account projected employment growth and historical trends. Net absorption represents the net change in occupied space, not gross demand. Source: NKF Research; May 2018



Asking Rent Change for General Industrial / Warehouse Space | Major Jurisdictions





The "Smart Money" and the Bay Area Industrial Market

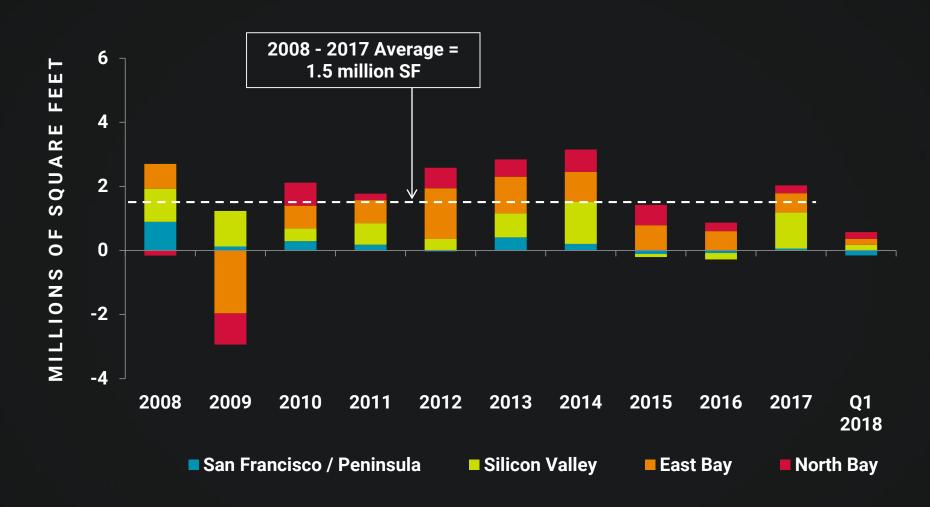
- With e-commerce rapidly expanding, consider purchasing distribution product close to population centers to support last-mile connectivity, even if modernization is required
- Close-in warehouses near urban centers often command a rent premium over exurban product, presenting opportunities for infill development and redevelopment at higher rents. Some occupiers may even invest their own capital to enhance less functional buildings in appealing locations.
- Multistory warehouses, such as those found in land-constrained Asian markets, may be a development opportunity in the Bay Area







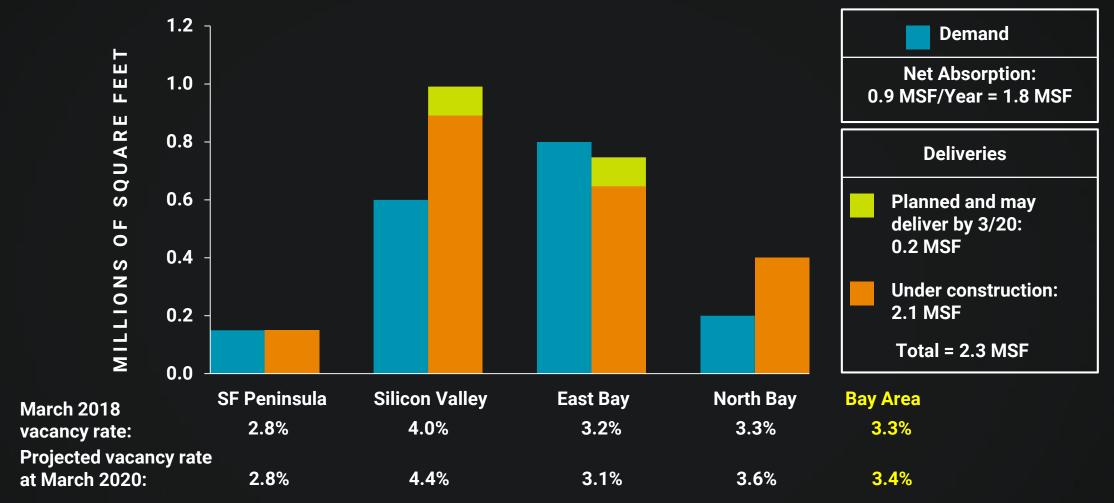
Net Absorption | Major Jurisdictions



Source: CoStar, NKF Research; May 2018



Projected Demand and Deliveries | Major Jurisdictions 2 Years Ending March 2020

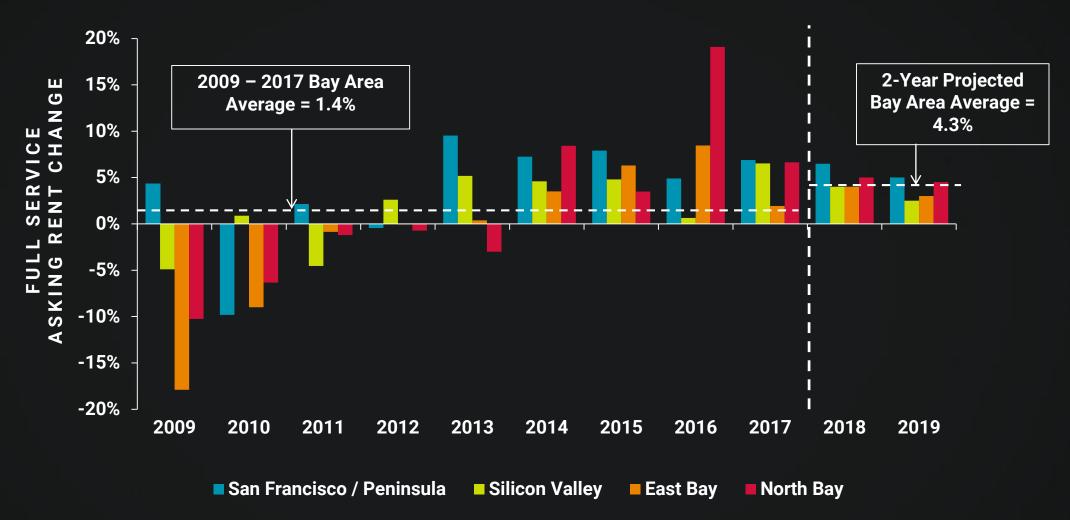


Note: Vacancy rate includes space that is physically vacant. Demand projections take into account projected employment growth and historical trends. Net absorption represents the net change in occupied space, not gross demand.

Source: CoStar, NKF Research; May 2018



Asking Rent Change | Major Jurisdictions



Source: CoStar, NKF Research; May 2018



The "Smart Money" and the Bay Area Retail Market

- Target new, experiential concepts that draw foot traffic and require substantial space, such as rock climbing, bowling centers, virtual reality, fitness concepts, food halls, and restaurant/cinema concepts
- Market to discount retailers such as Ross, TJ Maxx, Marshalls, and Nordstrom Rack. Also target grocery stores, which are recession-resistant and are reinventing themselves with customer pick-up and two-hour delivery.
- Seek retailers who started online and are now branching into brick-and-mortar, such as Amazon (with books and groceries). Consider hosting pop-up stores for online retailers who are experimenting before committing to brick-andmortar space.