

Moody's/REAL Commercial Property Price Indices, November 2008

AUTHORS:

Nick Levidy
Managing Director
(212) 553-4595
Nick.Levidy@moodys.com

Andrea Daniels
VP-Sr Credit Officer
(212) 553-4416
Andrea.Daniels@moodys.com

Connie Petruzzello
AVP-Analyst
(212) 553-4894
Concetta.Petruzzello@moodys.com

CONTACTS:

David Little
Managing Dir-Mktg&Prod
Strat
(212) 553-1627
David.Little@moodys.com

Mike DiCristino
Associate Product Strategist
(212) 553-4411
Michael.Dicristino@moodys.com

MOODY'S CLIENT SERVICES:

New York
+1-212-553-1653

Tokyo
+81-3-5408-4100

London
+44-20-7772-5454

Hong Kong
+852-3551-3077

Sydney
+61-2-9270-8100

Singapore
+65-6398-8308

WEBSITE:

www.moodys.com



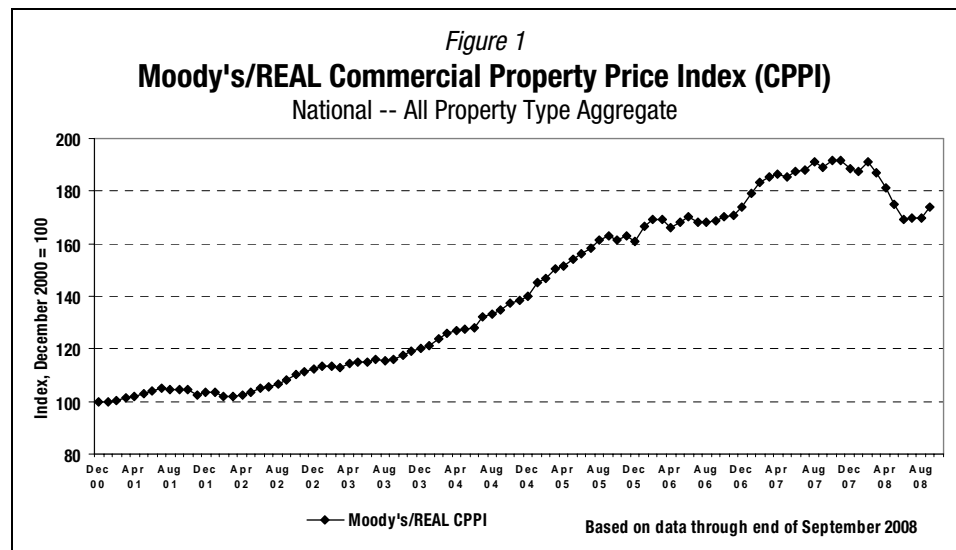
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OVERVIEW

In this report, the Moody's/REAL National All Property Type Aggregate Index for September measures 173.92, an increase of 2.5% over the previous month. This represents a decrease in prices of 7.9% from September 2007 and is 9.4% below the peak in October 2007. The index is 3.2% higher than it was 2 years ago. This report is based on data through the end of September.



November 18, 2008

Figure 2
Current Moody's/REAL CPPI and Change from Earlier Periods

New This Period: National All Property Type Aggregate
National – Four Property Types
Top 10 MSAs – Four Property Types
West – Four Property Types

Repeated This Period: East – Four Property Types
South – Four Property Types
Southern California – Four Property Types
MSA Office Markets – New York, San Francisco, and Washington DC
MSA Apartment Market – Florida

	Current Index ^M	1 Month Earlier	1 Year Earlier	2 Years Earlier
National All Property Type Aggregate	173.92	2.5%	-7.9%	3.2%
	Current Index ^Q	1 Quarter Earlier	1 Year Earlier	2 Years Earlier
National - Apartments	178.57	2.3%	-7.2%	2.5%
National - Industrial	171.37	0.4	-10.1	0.6
National - Office	162.08	-1.0	-8.3	3.5
National - Retail	175.84	0.1	-9.9	-4.5
Top Ten MSAs ¹ - Apartments	212.35	0.5	-4.7	7.5
Top Ten MSAs- Industrial	189.18	0.9	-4.4	4.3
Top Ten MSAs- Office	170.00	2.2	-0.6	7.9
Top Ten MSAs- Retail	188.01	0.4	-4.3	5.2
West - Apartments	180.72	2.9	-5.6	4.5
West - Industrial	174.50	2.1	-3.3	7.0
West - Office	155.20	-5.5	-10.6	7.8
West - Retail	186.25	-1.4	-6.2	-3.2
	Current Index ^A	1 Year Earlier	2 Years Earlier	
East - Apartments	194.10	-4.8%	2.1%	
East - Industrial	170.18	-3.0	3.8	
East - Office	173.92	-1.8	13.0	
East - Retail	196.32	-2.9	4.2	
South - Apartments	148.60	-8.0	-5.9	
South - Industrial	192.04	2.4	14.1	
South - Office	175.43	0.1	-0.8	
South - Retail	175.88	-3.0	2.2	
So. California - Apartments	206.22	-4.0	-2.3	
So. California - Industrial	197.25	-5.8	8.6	
So. California - Office	196.03	6.1	13.0	
So. California - Retail	256.22	5.1	12.6	
New York - Office	228.17	1.6	20.7	
San Francisco - Office	133.97	5.3	21.7	
Washington DC - Office	177.27	2.6	8.0	
Florida - Apartments	185.22	-14.1	-16.7	

M Monthly series. Most recent data is through September 30, 2008.

Q Quarterly series. Most recent data is through the end of the 3rd quarter 2008. Analysis is based on data from that 3rd quarter.

1 Top Ten MSAs refers to the ten MSAs with the most transactions by dollar volume, in each property type.

A Annual series. Most recent data is through the end of the 2nd quarter 2008. Analysis is based on data from four quarters (3Q07, 4Q07, 1Q08, and 2Q08). Given that the measure is of a rolling four-quarter period, data as of the end of the 2nd quarter can not be compared with that from the end of the previous quarter.

The Moody's/REAL Commercial Property Price Indices (CPPI) measure the change in actual transaction prices for commercial real estate assets based on the repeat sales of the same assets at different points in time.¹

Notable Observations and Themes

- The September aggregate price index experienced a 2.5% gain in prices over August. An increase in prices at this time may seem counterintuitive. However, we believe this result can be explained by continued loss avoidance on the part of sellers and by the fact that many September closings occurred pursuant to contracts entered into in the summer, before the market turmoil of September and October.
- Three of the four national property type series saw modest price increases this quarter, although prices in all four property types are down significantly from their peaks.
- The Top 10 series saw modest gains in all property sectors. Office prices in the top ten cities in particular are faring quite well, with a 2.2% price increase this quarter and dropping only 1% from the peak level overall.
- Western office underperformed the nation, with a decrease in prices of 5.5%, the largest drop in the report. The index now stands 10.6% below its peak, in stark contrast to the performance of office properties in the top ten cities.

¹ A summary or short version of the repeat sales methodology is available in a Moody's Special Report. [US CMBS: Moody's Publishes the First Commercial Property Price Indices Based on Commercial Real Estate Repeat Sales Data](#). Sept. 19, 2007. This is available on Moodys.com > Structured Finance > Commercial MBS > CRE Indices. A very detailed and complete explanation of the methodology is available in a White Paper from MIT. David Geltner and Henry Pollakowski. A Set of Indexes for Trading Commercial Real Estate Based on the Real Capital Analytics Transaction Prices Database. MIT Center for Real Estate. Sept. 26, 2007.

NATIONAL – ALL PROPERTY TYPE AGGREGATE INDEX: PRICE INCREASE LIKELY DUE TO LOSS AVOIDANCE AND CONTRACTS FROM LAST SUMMER

The National – All Property Type Aggregate is a monthly series, and this report is based on data through September 2008. Refer back to *Figure 1*, page 1.

At first glance, this month's positive return of 2.5% is counterintuitive in view of the lack of liquidity in the markets, recent increases in cap rates for commercial real estate as part of the ongoing adjustment of risk premiums for all asset classes around the world, and the general turmoil in the financial markets and broader economy over the past few months. Last month, we attributed the flattening of prices in part to decreased transaction volume and loss avoidance by sellers. We continue to believe these factors have contributed to this month's index results.

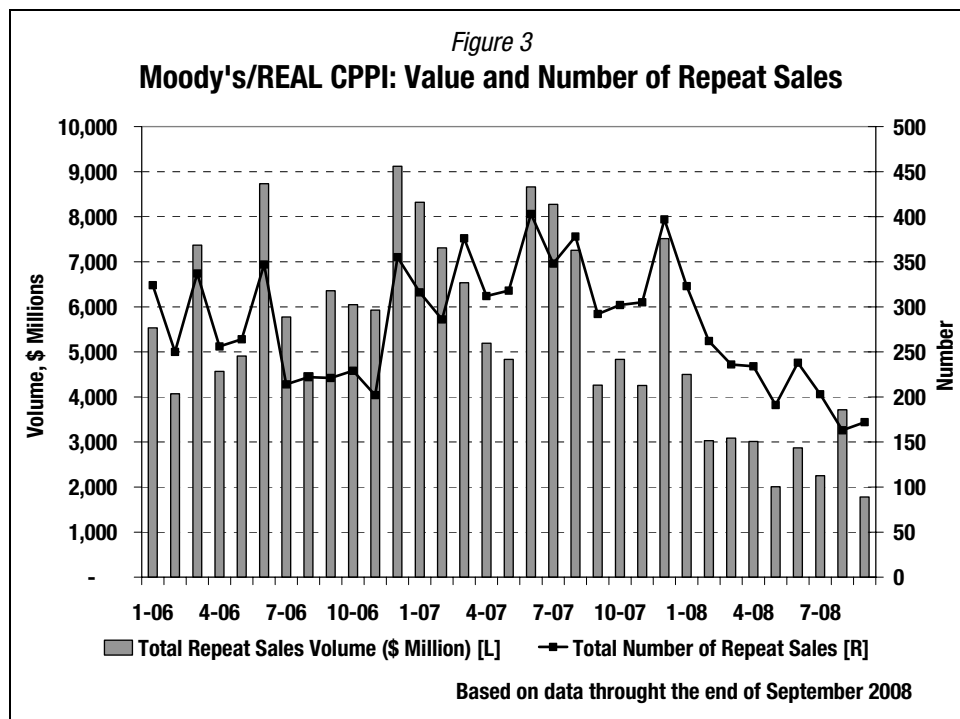
In addition, we note that the positive returns are based on actual sales data through the end of September. Deals that closed in September were likely agreed to at some point during the summer. It may seem like a distant memory now, given the turmoil in the markets this fall, but last summer it appeared that we just might avoid a major recession. Of course, starting in September, we saw major layoffs (over half a million jobs lost in September and October), the disintegration of Lehman Brothers, the federal bailout of AIG, the federal takeover of Fannie Mae and Freddie Mac, and one of the biggest stock market declines in recent history. The deals that closed in September likely reflected the relatively positive outlook of just a few months ago.

Furthermore, the results in the quarterly national property type indices lead us to believe that the aggregate increase in prices in September is due in part to relative strength in the apartment sector (see Page 9). In fact, if we exclude apartment properties from the set of repeat sales observations used to calculate the National – All Property Type Aggregate Index, the aggregate monthly return for the remaining three property types is less than 1%.

We continue to believe that commercial property prices have not yet reached a bottom. As pressure continues to build in the sector, owners will begin selling into a deteriorating market at lower prices. Assuming transaction volume is near a bottom, then we would expect the index returns to resume a downward track soon.

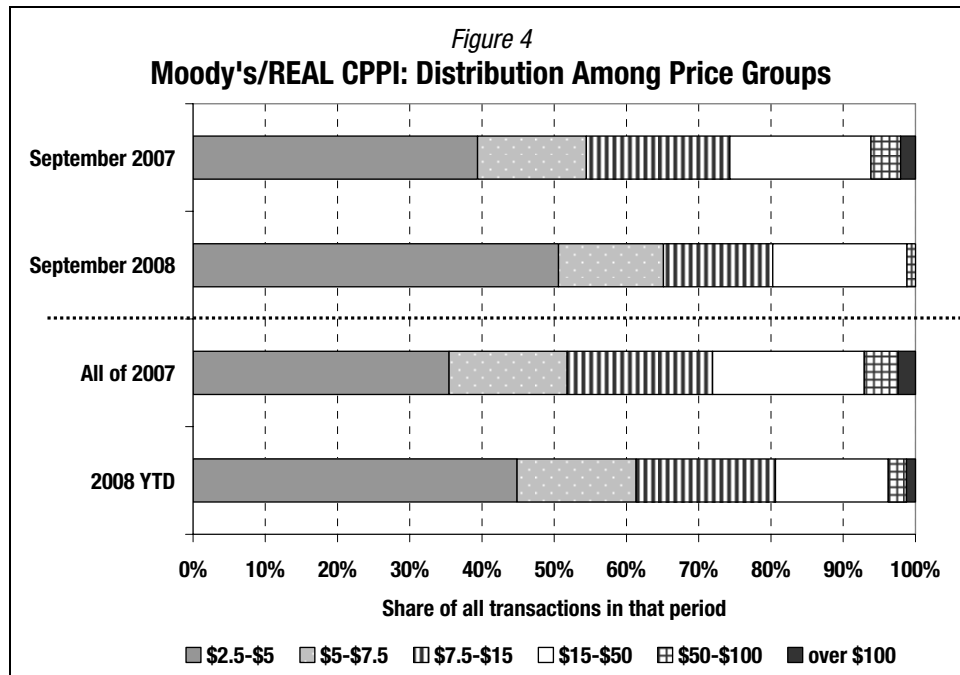
Transaction Volume and Average Prices

There were 172 repeat sales observations recorded in September, a slight increase over the month before. The increase was fairly evenly spread among the four property types. Transaction volume is well above the minimum required to calculate the index.



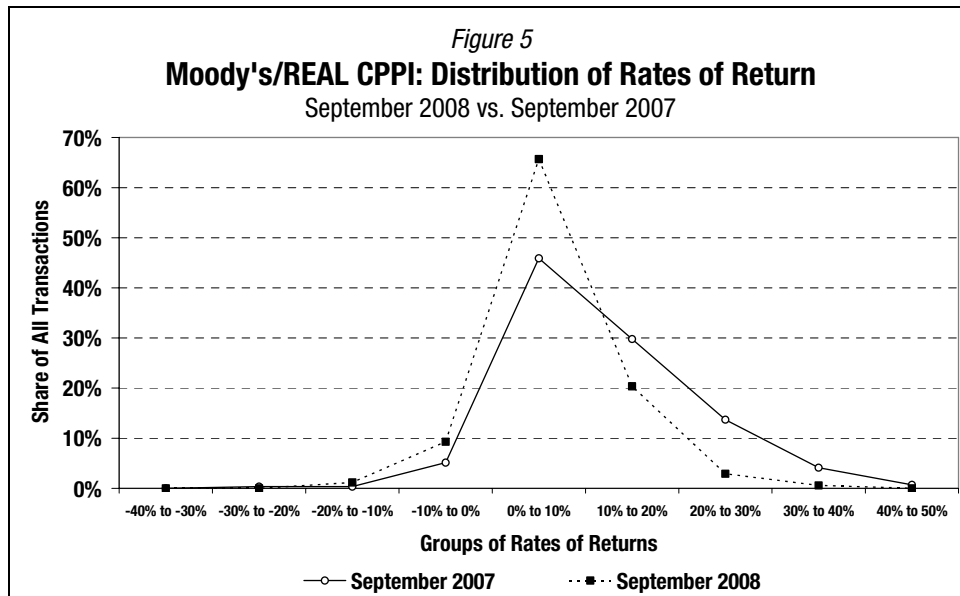
By dollar value, September's transaction volume was less than half the level seen in August. However, August's total dollar volume appears to have been something of an anomaly when compared to the number of transactions occurring that month. The average transaction size was substantially higher in August than in the other months of this year. When compared to transaction volume from May, June and July, September's dollar volume drop off is not so steep. Nevertheless, we do note that the total transaction volume of \$1.7 billion recorded this month is the lowest the index has experienced since early 2004. Also, bear in mind that transactions are often scheduled to close in the last month of the quarter. In this context, September's low volume may be viewed as further indication of reduced liquidity, pointing to continued seller loss avoidance and uncertainty among buyers.

The average price of the property trades that form the basis of the index scores also reveal some interesting trends. After prices peaked in October 2007, we began to see the average transaction price decrease as well, with sales activity moving away from high-end and trophy assets and toward lower priced properties. This trend continues, with over 65% of sales this month occurring in assets priced \$7.5 million or less, compared to slightly more than 50% in September of last year. Comparing 2008 year-to-date versus all of 2007 also shows a similar trend toward lower priced sales (see *Figure 4*).



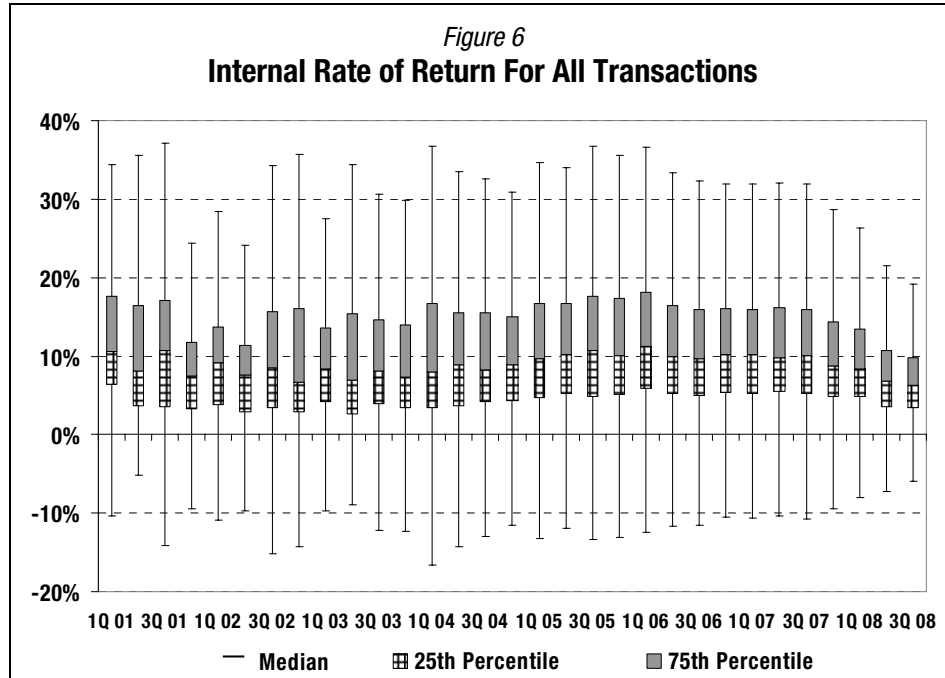
The Spread in Round-Trip IRRs: Dispersion Tightening as Prices Drop

Another interesting metric to examine is the overall round-trip price-change IRR achieved by the investors who have sold properties during the current period. While the index return reflects only the component of that IRR that occurred within the current period, the investors' overall "cradle-to-grave" price-change experience reflects the entire time between when the investor bought the property and when they sold it (in the current period). With property prices generally falling for almost a year, we have seen the average round-trip IRRs on the deals tracked by the index decline as well, shifting away from higher returns in the recent past toward flat or negative returns².



² Of course, Moody's/REAL CPPI tracks only the asset price-change component of the total IRR; investors would also have received net cash flow from property operating earnings, which would raise the complete IRR above the price-change-only component.

Further analysis shows that, as prices have fallen, there is also less dispersion around those rates of returns, with fewer frothy returns in excess of 20% but also fewer highly negative returns.

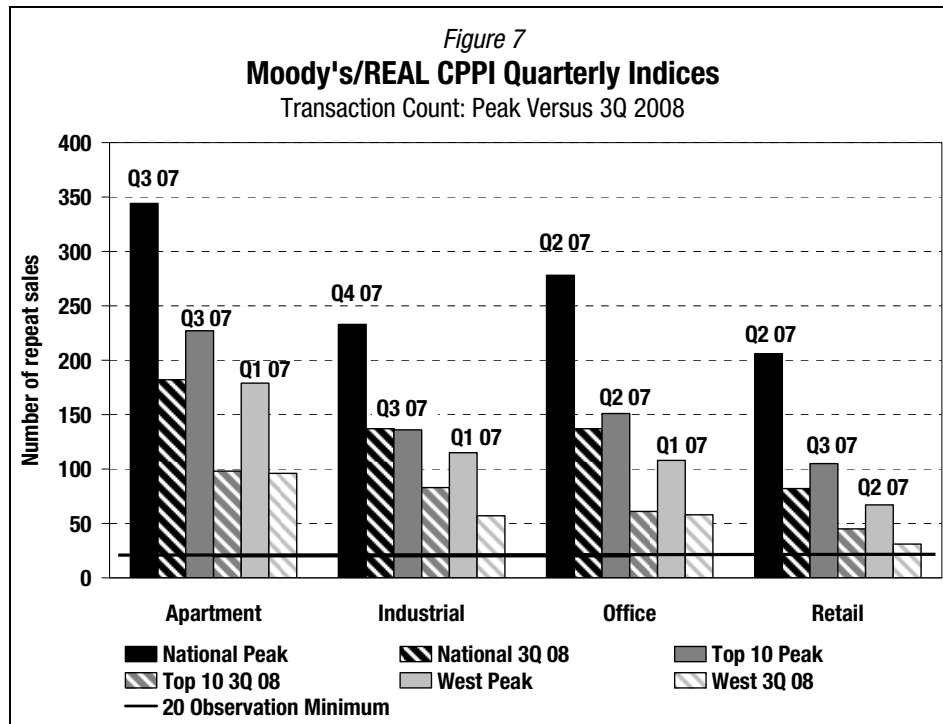


One interpretation of the reduction in the down-side tail of the IRR distribution is that this is additional evidence of loss avoidance on the part of sellers, as the drop in highly negative rates of return corresponds with the drop in transaction volume. In the near future, if transaction volume increases in a down-market we may see even fewer highly positive returns, and a lengthening of the lower-end bar due to an increase in highly negative returns (see *Figure 6*). Another (related) explanation for the tightening of the IRR spread has to do with the average holding period, the length of time the properties have been held between the buy and the sell. With the decline in volume as the market has fallen, investors are holding onto properties longer. IRRs computed over longer holding periods naturally tend to show less spread, as IRRs are quoted on a *per annum* basis, and the resulting averaging of many periods' returns together tends to mitigate extreme returns. Of course, lengthening average holding periods is just the other side of the coin reflecting reduced volume that in a down-market reflects seller loss avoidance to at least some degree.

Transaction Volume in the Sub-Indices: Down Significantly From Their Peaks

The number of repeat sales observations fell by about 20% in the third quarter as compared to the second for all three of the quarterly series: National, Western Region, and the Top 10 Markets. By both number and dollar value, the level of transaction volume is the lowest seen since late 2004.

The height of repeat sales transaction volume varied by series; the peak was mid to late 2007 for the nation, early 2007 for the West, and mid 2007 for the Top 10—but all have since seen transaction volume cut in half (as measured by number, or down 65% as measured by dollar).

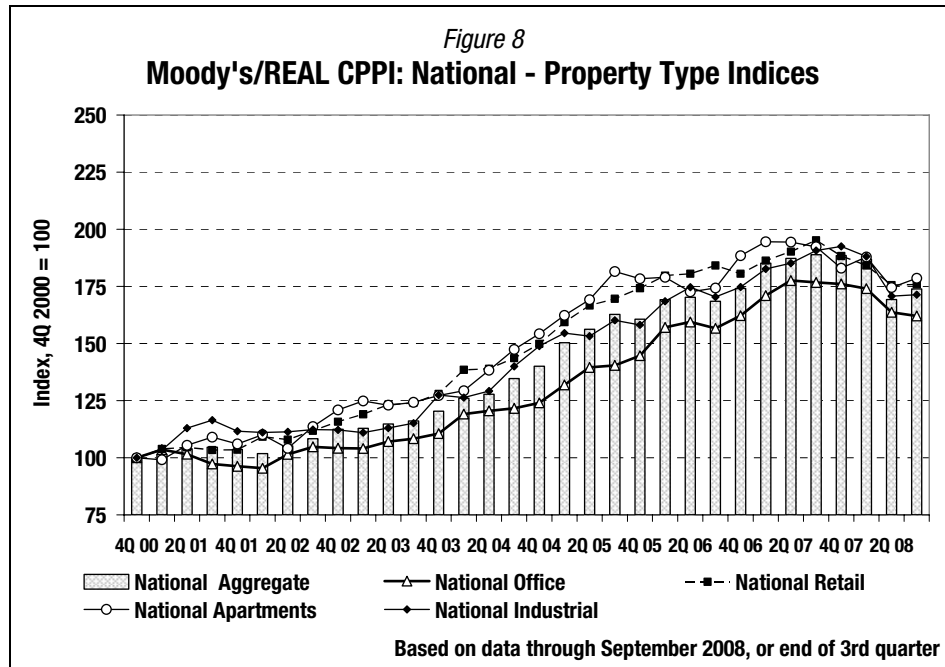


Across all series, apartment and retail volume has suffered the most, with the number of transactions down by about 60% in each. Retail is down slightly more in the West, by 65%, while apartment is down 65% in the top ten cities. Nationally, and in the West, the number of repeat sales transactions of office properties is down 50% overall, and in the top ten cities, the number of office transactions has fallen by 60%. Transaction volume for industrial has fared slightly better for the nation and the top ten cities, down 40% overall, and in the West, repeat sales of industrial properties are down by 50%.

NATIONAL – PROPERTY TYPE INDICES: APARTMENT PRICES GAIN

The National – Property Type Indices for the four major property types are a quarterly series, and this report is based on data through the third quarter 2008.

As noted previously, part of the 2.5% monthly gain seen in the aggregate price index can be attributed to the apartment sector, which posted a positive quarterly gain in national apartment prices of 2.3% in the third as compared to the second quarter. This gain partially offsets the 7.1% drop in prices seen last quarter, resulting in an overall drop of 8.2% from the peak measured in 1Q 07. Prices in the national apartment sector have been declining the longest of the four national property types, but the overall drop has also been the mildest. (It is worth noting that apartments had already taken some correction in 2005-06 with the bursting of the condo-conversion boom.)



National industrial fared second best of this series in the third quarter, with a slight increase in prices of 0.4%. Overall however, even though industrial prices began falling in the last quarter of 2007, the latest of the four property types, they have fallen the furthest, down 11% from the peak.

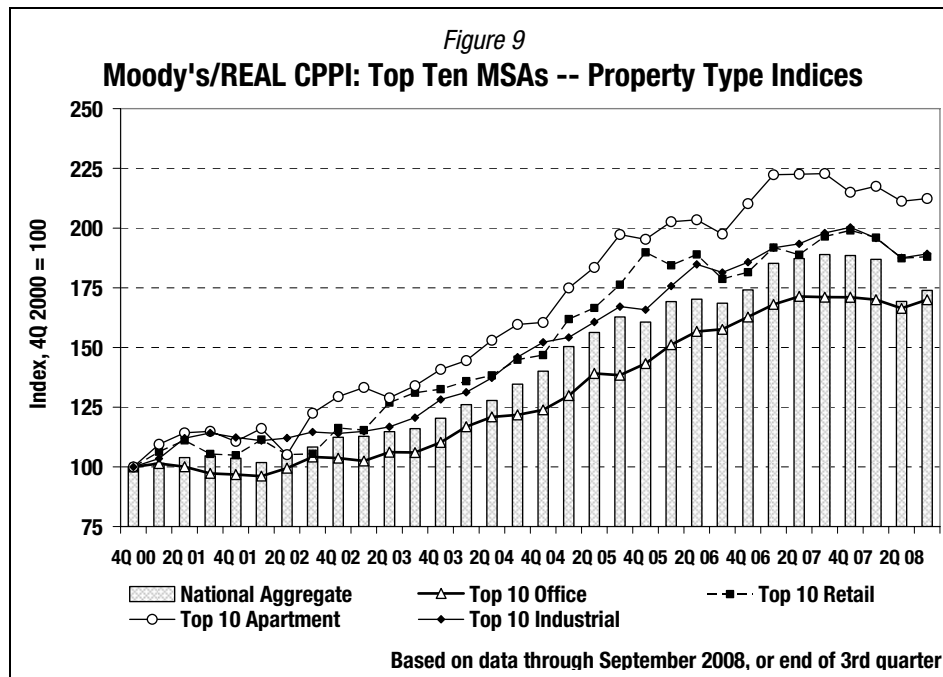
The national retail sector is right behind the industrial sector in terms of total decline from peak, with an overall decline in prices of almost 10% since 3Q 07. This quarter, prices stopped falling, but could not offset the declines seen so far, since this quarter's change in prices was virtually flat.

The office sector was the only property type nationally to continue to fall in the third quarter, with a decline in prices of 1.0%. Office has been the least volatile of the four property types, slowly and steadily declining since its peak in 2Q 07, for an overall decline of 8.7%.

TOP TEN MSAS – PROPERTY TYPE INDICES: PRICE INCREASES IN ALL PROPERTY TYPES

This series is based on the ten MSAs which are home to the most transactions by dollar volume in each property type.³ Approximately 50%-80% of the national index is driven by the performance of assets in only ten cities, although that ratio varies by property type and over time. This is also a quarterly series, based on data through the third quarter of 2008.

All four property types in this series saw price increases, with three of the four outpacing the nation this quarter. Top 10 office fared the best, with prices increasing 2.2% in the third quarter, in contrast to the nation which saw a decline of 1.0%. This increase takes back the losses the Top 10 office sector experienced last quarter, which leaves it just 1% below the peak seen in the second quarter of 2007. Thus far, the Top 10 office sector has been the least impacted by the turmoil in the financial markets.



Top 10 industrial and retail saw similar gains this quarter. Industrial prices in the top ten cities increased just shy of 1% in the third quarter of 2008. This gain slightly outpaced the nation, which increased almost half a percent in prices over the same time period. However, this slight increase in the top ten industrial cities follows two consecutive quarters of significant drops in prices, leaving the Top 10 industrial sector almost 6% below the peak seen in the fourth quarter of last year.

Similarly, growth in retail prices in the top ten cities this quarter slightly outpaced the growth seen in the nation overall, 0.4% versus 0.1%. This very mild growth in Top 10 retail, like industrial, comes after two quarters of price declines. Retail prices in the top ten cities now stand 5.5% below the peak reached at the end of last year.

The gain of 0.5% in Top 10 apartment prices was the only sector in this series to fall short of the nation, which saw growth in the apartment sector of 2.3%.

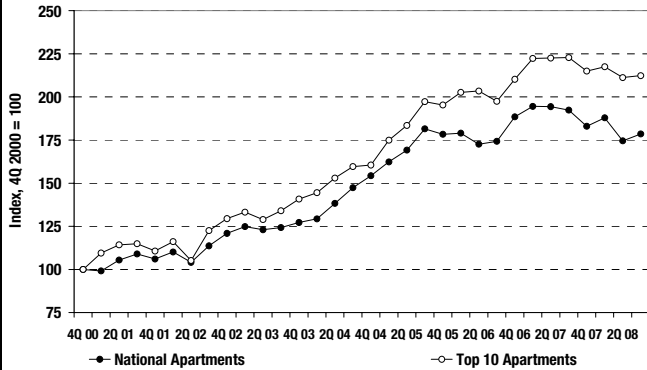
It is important to note that, although in general, prices in the top ten cities for all property types peaked at the same time as the nation and have been falling ever since, they have not fallen as sharply and appear to be faring better than the nation overall.

³ A list of the top ten cities in each property type can be found in a Moody's Special Report. [Moody's/REAL Commercial Property Price Indices, May 2008](#). May 19, 2008. This is available on Moody's.com > Structured Finance > Commercial MBS > CRE Indices.

Figure 10
Moody's/REAL

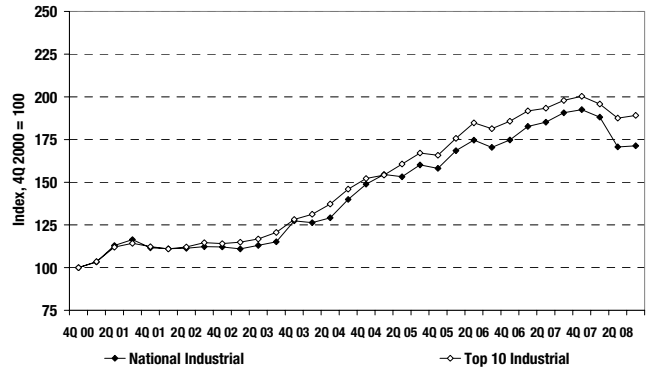
Prices in the Top 10 Cities Compared to the Nation

Apartment



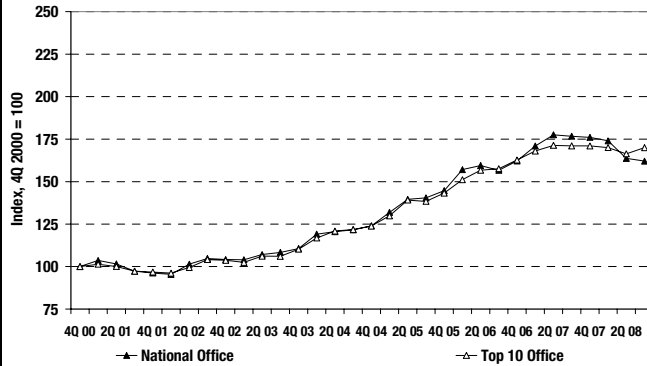
Based on data through September 2008, or end of 3rd quarter

Industrial



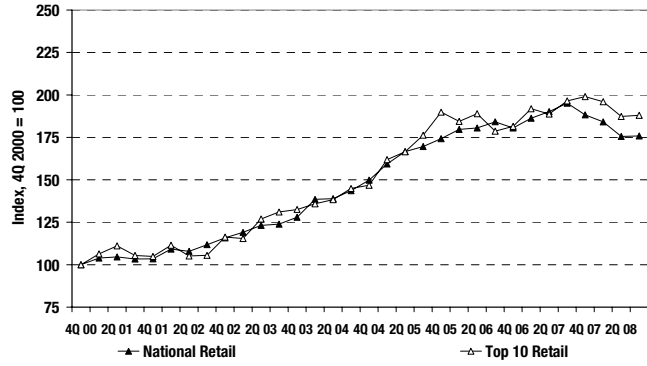
Based on data through September 2008, or end of 3rd quarter

Office



Based on data through September 2008, or end of 3rd quarter

Retail



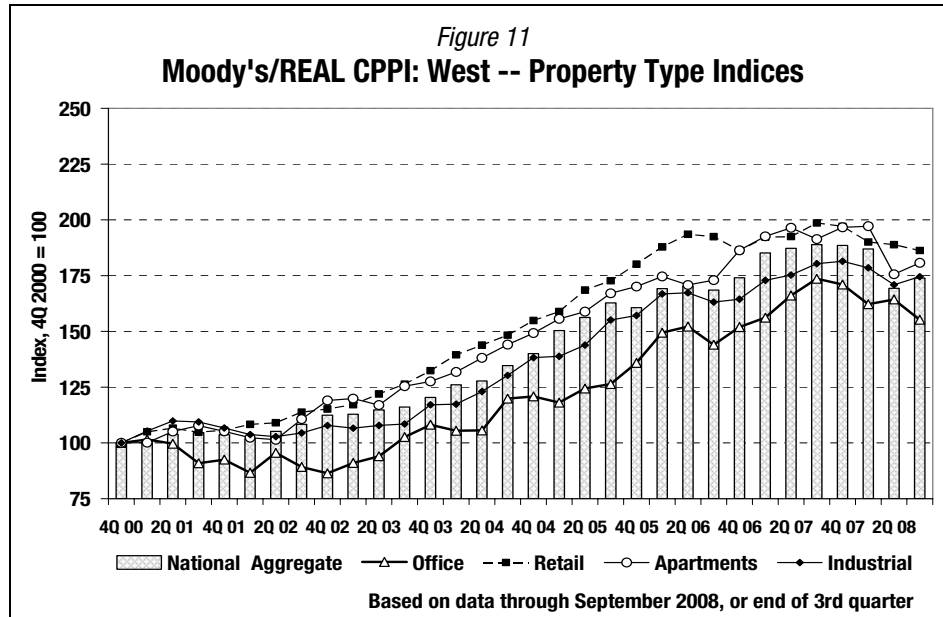
Based on data through September 2008, or end of 3rd quarter

In all but the office sector, the run up in prices was higher over the past several years in the top ten cities, and the recent fall in prices has been relatively gradual, as compared to the nation. For office, growth in prices in the top ten cities did not reach the peak seen in the nation, and the Top Ten office index score shows very little in the way of price declines thus far.

WESTERN REGION – PROPERTY TYPE INDICES: OFFICE MARKET LAGS

The Western Region – Property Type Indices for the four major property types are a quarterly series, and this report is based on data through the third quarter of 2008.⁴

The four property types in the West generally followed the trajectory seen in the nation as a whole, though its gains in prices were higher, and its losses steeper. In the West, the apartment sector saw an increase in prices on the order of 2.9% which is the largest increase seen in any of the indices reporting this month. However, last quarter, western apartment saw the largest decrease of any sector: 10.9%. Thus, overall, this sector is down 8% from its peak in 2Q 07. Western industrial property prices saw an increase as well, with a gain of 2.1%. Industrial is the strongest performing sector in the West overall, falling less than 4% from the peak in 4Q 07.



The Western retail sector saw a modest drop in prices of 1.4% this quarter. Retail has been falling steadily over the last few quarters, with an overall drop of 6.2% in prices since its peak in 3Q 07. The western office sector measured the largest decline in prices of any index this month, with a decrease of 5.5%. The movement in western office has been quite volatile since it peaked in 3Q 07, and with an overall decline in prices of 10.6%, it is the worst performer of the western region.

On the whole, although the price declines in the West (in office and retail) were steeper than the declines in the nation this quarter, none of the four property types in the West have fallen as far from their peak as compared to the individual property sectors for the nation overall.

The attached Appendix includes the following:

- A calendar summarizing the report cycle, i.e., which indices are recalibrated in which month. The calendar also indicates the precise release dates for Moody's/REAL Indices for the next year (*Figures 12, 13, and 14*).
- Charts for the 16 sub-indices that were not recalculated for this report. These are repeated from the previous report so that both data and charts for all indices, whatever the most recent calculation, are included here in one document for investors' convenience (*Figures 15 – 19*).

⁴ The regions are the same as those defined by NCREIF. A list of each of the states included in each region is provided in the CPPI Primer: [Moody's Publishes the First Commercial Property Price Indices Based on Repeat Sales Methodology](#).

APPENDIX

Figure 12
CPPI: Report Release Cycle, 2008 - 2009

	OCTOBER	NOVEMBER	DECEMBER
	Oct. 20, 2008	Nov. 19, 2008	Dec. 22, 2008
Report to be released:	Aggregate	Aggregate	Aggregate
For period:	August	September	October
Based on data through:	August 31	September 30	October 31
Report to be released:		12 Quarterly Indices (A)	16 Annual Indices (B)
For period:		3rd Quarter	3rd Quarter
Based on data through:		September 30	September 30
	JANUARY	FEBRUARY	MARCH
	Jan. 20, 2009	Feb. 19, 2009	March 19, 2009
Report to be released:	Aggregate	Aggregate	Aggregate
For period:	November	December	January
Based on data through:	November 30	December 31	January 31
Report to be released:		12 Quarterly Indices (A)	16 Annual Indices (B)
For period:		4th Quarter	4th Quarter
Based on data through:		December 31	December 31
	APRIL	MAY	JUNE
	April 20, 2009	May 19, 2009	June 22, 2009
Report to be released:	Aggregate	Aggregate	Aggregate
For period:	February	March	April
Based on data through:	February 28	March 31	April 30
Report to be released:		12 Quarterly Indices (A)	16 Annual Indices (B)
For period:		1st Quarter	1st Quarter
Based on data through:		March 31	March 31
	JULY	AUGUST	SEPTEMBER
	July 20, 2009	Aug. 19, 2009	Sept. 21, 2009
Report to be released:	Aggregate	Aggregate	Aggregate
For period:	May	June	July
Based on data through:	May 31	June 30	July 31
Report to be released:		12 Quarterly Indices (A)	16 Annual Indices (B)
For period:		2nd Quarter	2nd Quarter
Based on data through:		June 30	June 30

Figure 13

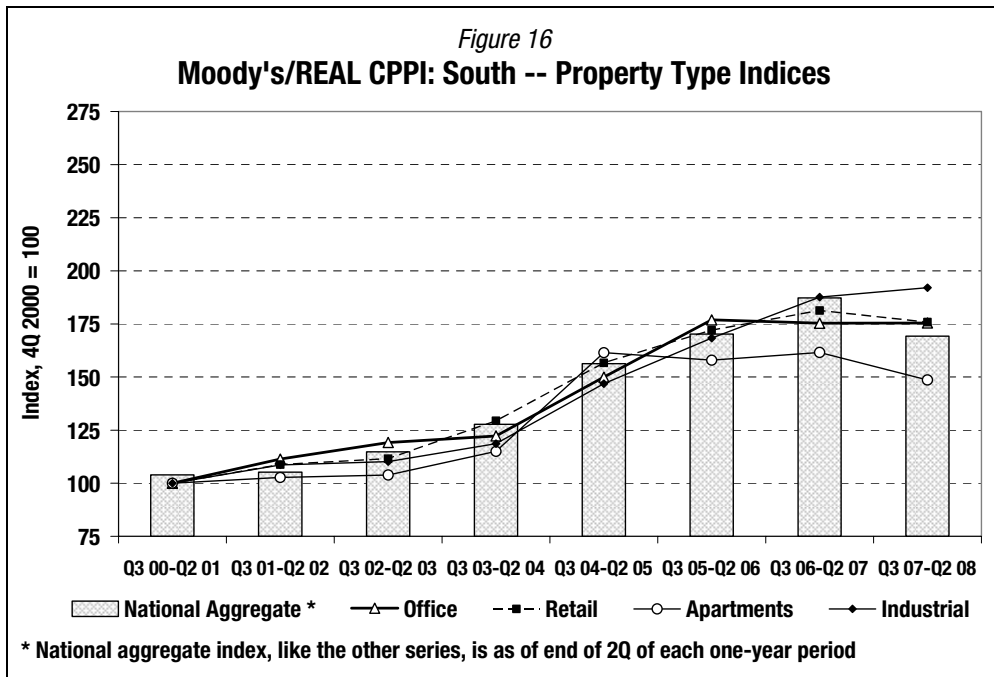
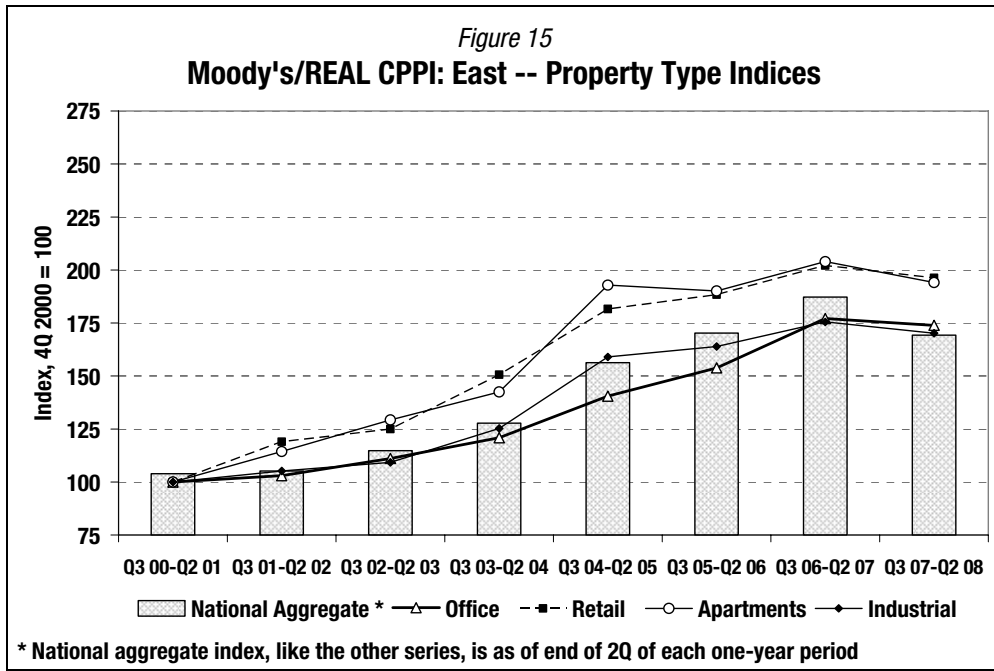
(A) 12 Quarterly Indices include the following:

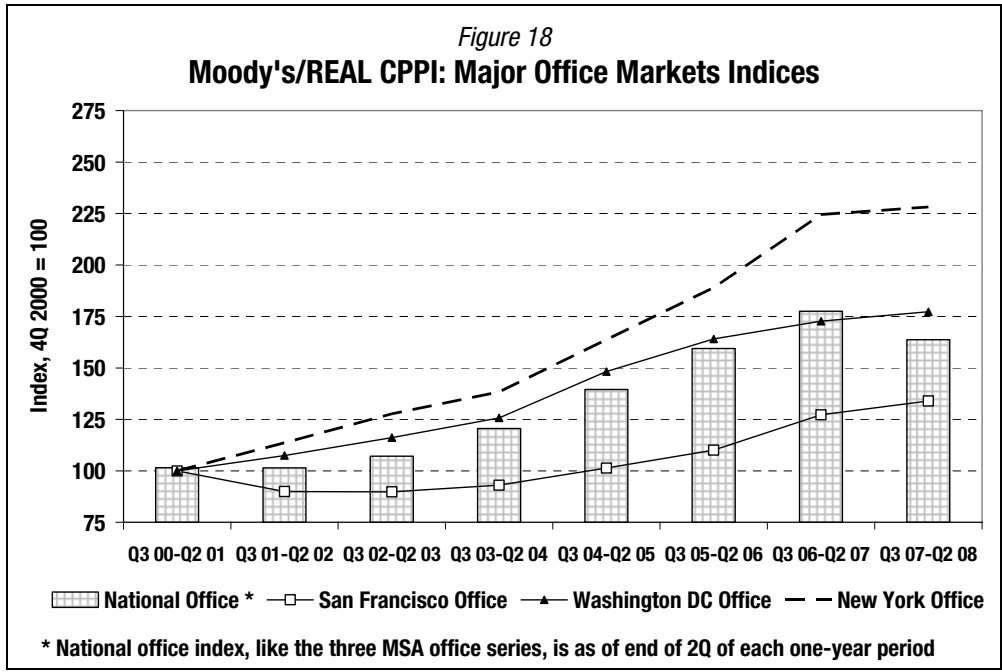
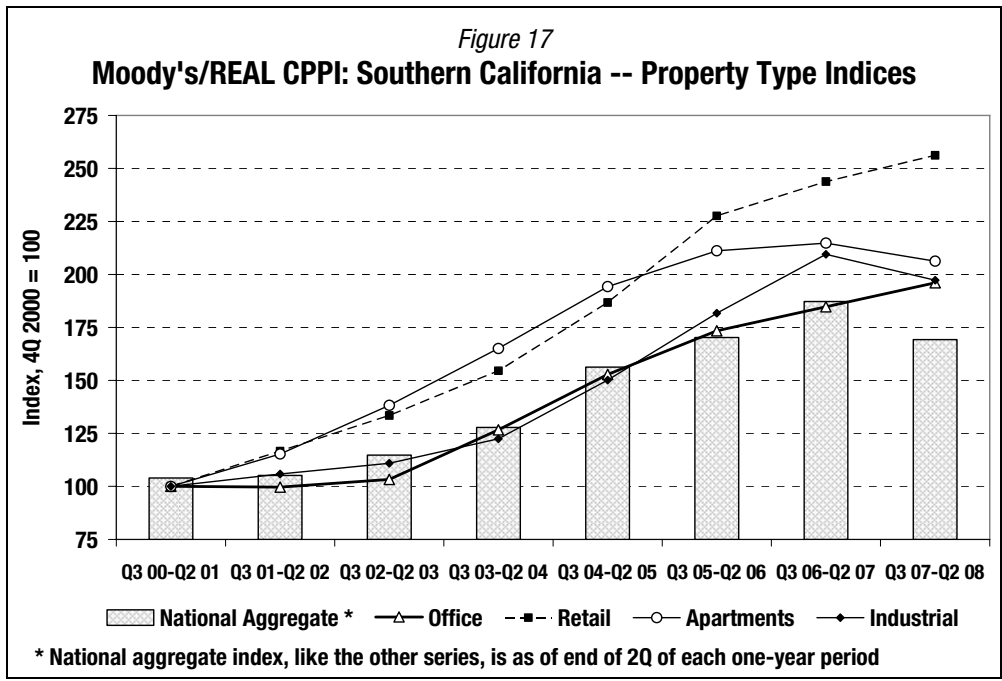
APARTMENT	RETAIL	OFFICE	INDUSTRIAL
National Apartment	National Retail	National Office	National Industrial
Top 10 MSAs Apartment	Top 10 MSAs Retail	Top 10 MSAs Office	Top 10 MSAs Industrial
West Apartment	West Retail	West Office	West Industrial

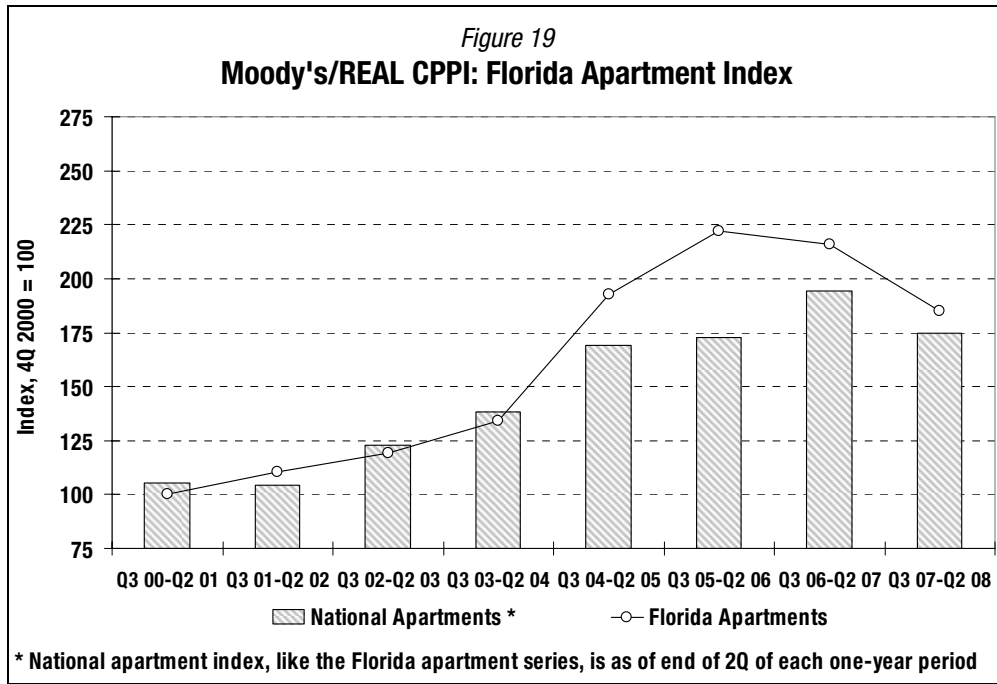
Figure 14

(B) 16 Annual Indices with Quarterly Releases include the following:

APARTMENT	RETAIL	OFFICE	INDUSTRIAL
East Apartment	East Retail	East Office	East Industrial
South Apartment	South Retail	South Office	South Industrial
So. California Apartment	So. California Retail	So. California Office	So. California Industrial
Florida Apartment		New York Office	
		San Francisco Office	
		Washington DC Office	







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