Investment Market Briefing

INVESTMENT | MID-YEAR 2009

Confidence (n.)
Full trust; belief in the markets.

-Websters Dictionary

MARKET INDICATORS

	MID YEAR 2008	MID YEAR 2009	MID YEAR 2010
SALES VOLUME	▼	▼	◀▶
SALES COUNTS	▼	◀▶	◀▶
CAP RATE	▲	▲	▲

HIGHLIGHTS

Hawaii Total Mid-Year $1M+ Commercial Investment Transactions:

57

Total Mid-Year $1M+ Commercial Investment Sales Volume:

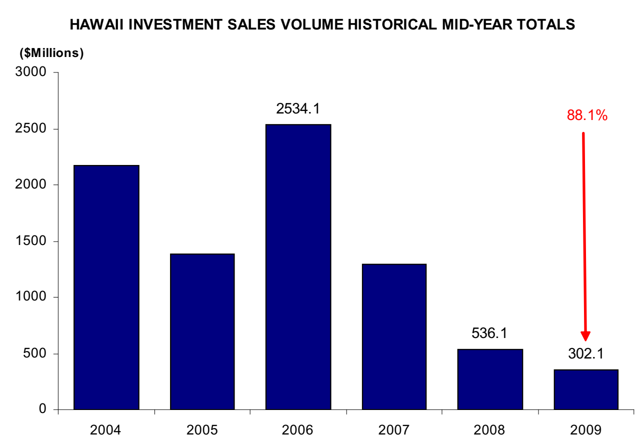
$301,998,100

Trials and Tribulations

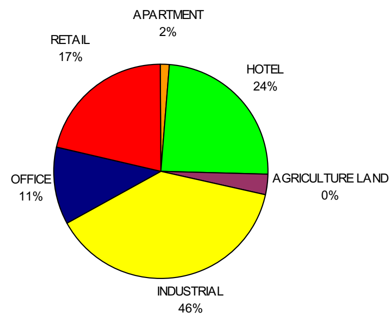
Dramatic declines in commercial real estate transaction volume continue to persist as a combination of the global financial crisis and the recession's impact on real estate dynamics further aggravate the current tenuous market. The inability to find an alternate source of funding for properties with loans expiring is proving to be problematic. The demise of the CMBS ("commercial mortgage backed securities") market and the consolidation of investment banks and institutional lending sources have resulted in a severe contraction in financing capacity.

Additionally, major property sectors are affected by the downturn in the economy. As job losses mount, foreclosures rise, and retail sales drop, demand for commercial space is being affected. Throughout the country, planned commercial developments have been shelved and partially built projects are being heavily discounted for "fire" sales. Vacancy rates have risen precipitously and rents have begun to sag, ultimately affecting the value of the property. Until the "bottom" of the market is recognized, apprehension among the investment community will continue to reign. Purchase and development decisions are postponed and many projects remain in limbo.

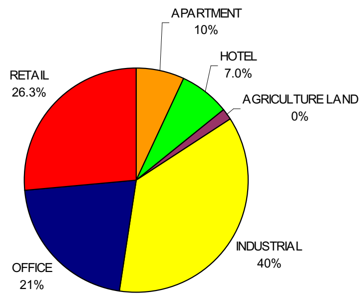
Nationally, with markets in a tailspin, the lack of transaction activity coupled with a downward trend in values, compounds the difficulty of determining a property's worth. Banks and lending institutions, which have increasingly become more risk averse, appear to have tightened their purse strings, only to offer loans to the "cleanest, highest credit worthy" clients. Even if you qualify under



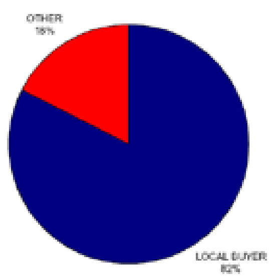
2009 MID-YEAR SALES VOLUME PERCENTAGE BY PROPERTY TYPE



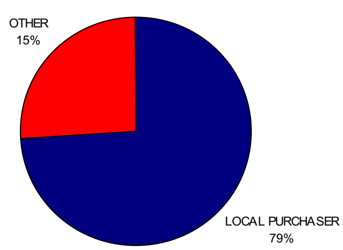
2009 MID-YEAR SALES TRANSACTION COUNT BY PROPERTY TYPE



2009 MID-YEAR PURCHASERS PROFILE BY PERCENT OF TRANSACTIONS



2009 MID-YEAR PURCHASER PROFILE BY PERCENT OF SALES VOLUME



their stringent underwriting criteria, the terms of the loans are restrictive. Loan to value ratios, historic cash flow and operating profits, personal net worth and collateral, etc…are all reviewed as property investors are faced with increased scrutiny. Costs to borrow money have risen, resulting in investors needing to obtain a corresponding increase to capitalization rates and investor target yields.

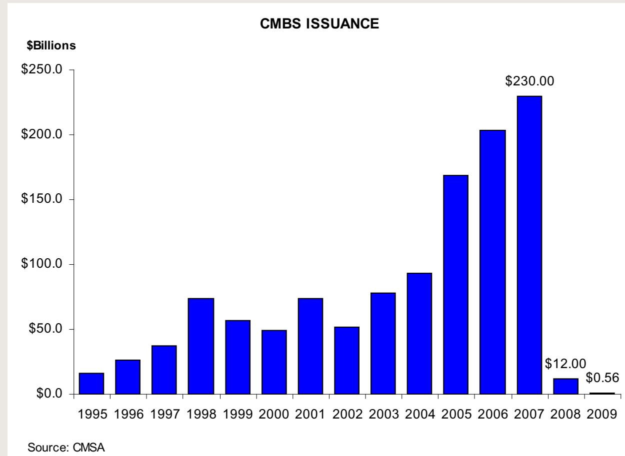
Similarly for Hawaii's commercial real estate investment market, conditions reflect the national sentiment. High priced multi-million dollar prime properties like hotels and shopping centers are lacking from the list of notable sales. Transaction volume continued to decline with an estimated $302 million for the first six months of the year, a 43.7% decline from 2008 figures and a dramatic 88.1% decline from the record peak set in 2006. The average sales price per transaction increased to $5.3 million from $5.2. The majority of the transactions fell in the under $5 million range. Owner user transactions have become the "bread and butter" of the current market, as investor sales have dropped off. Local investors constitute the majority of the ownerships, as local banks have provided the funding for most of the purchases.

CMBS Market Negligible

CMBS served as one of the primary financing sources that flourished during the 2003 to 2008 time period. Nearly a trillion dollars of securitized debt was offered on commercial real estate during this time period. The CMBS market grew from $41.6 billion in 1990 and 3.8% of the mortgage debt outstanding to $907 billion and 28% of the debt outstanding in 2009.

Rapid growth of securitization of these loans resulted in a division of low-risk, low-return to high-risk, high-return debt tranches of AAA, AA, BBB paper. As these tranches were sold off, investors believed that they were minimizing their risk by buying a mixture of risk levels. Loan-to-value ratios rose as investors were enticed with low equity requirements, low interest rates, and non-recourse loans. Frenzied buying supplanted critical thought as investors tried to maximize returns for properties with limited equity. Very little concern was raised that the underlying properties would have to generate enough operating cash flow to service the rising levels of debt.

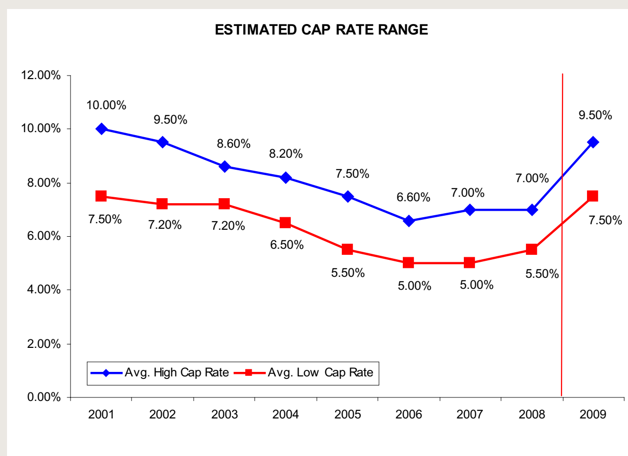
By September 2008, capital markets succumbed to the subprime fiasco and resulted in increased scrutiny for any debt secured by real estate mortgages. CMBS issuance for 2007 was roughly $230 billion. By the end of 2008, only $12 billion was issued. For the first half of 2009, $559 million of CMBS debt was issued. This is less than 5% of that issued in the first half of 2008.



Looming Loan Defaults

Of those that purchased properties in the 2003 to 2007 timeframe with CMBS funds, many utilized five-year term loans that will need to be refinanced or sold over the next few years. Both options appear increasingly difficult, as commercial real estate market dynamics continue to deteriorate and available capital sources tighten restrictions. Loan defaults appear inevitable as properties purchased at the height of the market with overly optimistic rental rate projections are destined to under perform and fail to meet their debt obligations.

In a presentation to the Senate's Joint Economic Committee, experts commented that there are $400 billion in outstanding commercial loan expirations for 2009 and an additional $300 billion for 2010. Washington-based Real Estate Roundtable projected that by 2012, $1.8 trillion dollars in commercial loans will become due. The biggest hurdle has been the lack of capital sources and available loan capacity with the loss of the CMBS market and a number of investment firms (i.e. Fannie Mae, Freddie Mac, Bear Stearns, Wachovia, Lehman Brothers, Countrywide, Chase, Merrill Lynch). Currently, delinquencies among commercial real estate loans doubled over last year's figures to roughly 7% of all the CRE loans outstanding. Concerns are that this level will rise markedly as the $1 trillion dollars of loans come due.



Using debt to purchase a property is beneficial as long as the market continues to appreciate. What better way to make money than to borrow someone else's for the purchase of a property, pay a low or minimal interest rate and when you sell, keep the profits! Unfortunately, this formula for success also penalizes the mortgagee if rents start to sag, or financing costs increase, or the underlying market dynamics worsen. As a part of most financing packages, if a property's value declines, the mortgagee is responsible for maintaining the loan to value ratio and as a result, will have to fund additional equity if the property's value declines. If this ratio is not maintained, the loan technically goes into default.

Real Capital Analytics, a commercial real estate transactions data source, notes that Hawaii's troubled assets have risen dramatically. The properties on this list include those that are delinquent or in default on their loans, those where the owner is bankrupt or financially challenged, or foreclosure efforts have been initiated. The General Growth portfolio (which includesAla Moana Center,Ward Centers.) and Brian Andersen's Anekona Real Estate Development portfolio (which includes Ilikai Hotel, Coconut Grove,Shopping Center, andHilton Kauai Beach Resort) constitute a large percentage of those listed. An estimated total of more than $3.8 billion in loans are categorized as part of Hawaii's troubled assets classification.

"This market is clearly risk adverse, with lenders and investors seeking realistic income projections and commensurate value estimates. Over the last 8 to 12 months, appraisal and consulting assignments related to litigation, bankruptcy, and portfolio review purposes have meaningfully increased as the ability to retain properties is strained."- ***(Stephen Stadlbauer, Lesher Chee Stadlbauer. LLC)***

Banker's Lament

Although problem loans are increasing in Hawaii, local banks have historically been fairly traditional in their commercial real estate lending. The pendulum of loan underwriting for local lenders, which runs from restrictive to lax, remained fixed in the conservative mode throughout most of the 2000 to 2007 time period. Most of the negligent loans were originated by mainland lenders. For commercial real estate brokers, who are principally paid when a transaction is closed, the apparent change in underwriting dictum has increased the difficulty consummating a deal. While a broker could have previously gone to an offshore lender, that option is no longer available. Local banks have become one of the few remaining sources of financing.

Assuming that a broker goes through a hundred prospects and gets ten interested in purchasing their property. Of the ten that go to a banker to get a loan, only 10% receive a bank's term sheets. Of the one that obtains financing, only 80% actually close a deal. This creates a selling ratio of less than 1% for a broker. This is quite a change from the previous market conditions where an agent would get multiple offers for a property and financing firms had aggressively provided funding.

For loan underwriting and property valuation, a property's cash flow becomes integral in a banker's decision to fund a transaction's purchase. Discounted cash flow models using realized income based on the past 12 months of performance has become the norm. In an attempt to get a better handle on a property's worth, the seller's offering memorandum is thoroughly reviewed and overly optimistic net operating income projections are replaced with more conservative models.

Additionally, the purchaser's financial capacity is analyzed. For an owner-user purchase, the owner's net worth and consolidated corporate cash flow statements are evaluated. Bankers now tout "relationship" banking as a way to expand services to new and existing clientele.

Mid-Year 2009 Oahu Investment Market Statistics

	Sales Volume	Transactions	Avg. Transaction Size	Korpacz USA Cap Rate 4Q08	RCA Cap Rate Hawaii 12/08	Colliers Estimated Hawaii Cap Rate
Apartment	$4,493,000	4	$1,123,250	6.88%	6.50%	7.00% to 8.00%
Hotel	$73,066,000	4	$18,266,500	---	---	9.00% to 10.00%
Agriculture Land	$8,448,961	1	$8,448,961	---	---	---
Industrial	$115,944,342	21	$5,521,159	7.13%	8.05%	8.00% to 9.00%
Office	$35,496,588	12	$2,958,049	7.52%	7.60%	8.00% to 9.00%
Retail	$64,549,289	15	$4,303,286	6.99%	7.75%	8.00% to 9.00%
Totals	**$301,998,180**	**57**	**$5,298,214**	---	---	---

Source: Korpacz USA, Emerging Trends 2009, Real Capital Analytics, Colliers Monroe Friedlander, Inc.
NOTE: Cap Rates estimates are for fee simple properties.

Appraiser Dilemma

Property valuation continues to prove problematic in a period where few sales occur. The lack of sales comparables is not a unique situation for Hawaii, where there are typically few major office, retail or hotel sales in a year. Despite this fact, Hawaii's appraisers utilize trending data that helps them to estimate the appreciation or decline in a property's value. In a period of transition, the appraiser has to not only determine the direction of a property's value but how severe of an adjustment is needed to identify the pace of the increase or decrease that is occurring.

Banks reviewing loan applications have placed an increasingly critical eye to any materials submitted by the seller and the buyer of a property. The appraisal becomes paramount in the decision process to whether a bank provides the funds for the purchase, refinance or development of a property.

"Valuing commercial properties in the current investment climate has been challenged by the lack of recent transactions that normally serve as primary indicators. Consequently, interviews with knowledgeable parties, developers, and brokers as to market perceptions are taking on greater importance. Additional analyses of macroeconomic data, investor surveys, and competitive returns in the capital markets also help to bridge the gap." - ***(Fernando Buenavente, The Hallstrom Group, Inc.)***

Investment Forecast

The mention of "green shoots" raises eyebrows as skepticism remains high among the commercial real estate investment community. As an economic indicator, commercial real estate tends to lag the rest of the economy. Until other factors begin to improve such as S&P 500 Index, residential home sales, retail sales, manufacturing production, job growth and so on, the commercial real estate sector will wallow in the proverbial mud of a weakened economy.

For investors with cash, the opportunity to purchase heavily discounted real estate may be in the mid-term time horizon. Looming on the horizon is the specter of the potential for over $1 trillion in CMBS loans with expiring terms. Unless these loans can be refinanced, foreclosures and loan defaults are very likely. The commercial real estate industry needs an alternative funding source to replace CMBS to cover upcoming loan expirations. For those who are unable to find alternative funding sources, joint venture partnerships, workout specialists, hedge and opportunity funds are waiting to capitalize on investing in exchange for large equity positions.

Historically, job growth lags the initial improvement in the economy by as much as 12 months. It usually takes 12 to 18 months of job growth to impact the commercial real estate market. This lag period between the start of economic growth and the resulting improvement to the commercial real estate sector could be up to two years or even longer. Forecasts anticipate 2012 as the likely year for commercial real estate markets to show improvement and growth.

Market Sector Overview

Office
Hawaii's unemployment rate has more than doubled over the past year, the direct result of layoffs among the island's hospitality, construction, retail, finance and real estate sectors. With negative net absorption beginning during the second half of 2007 and continuing through to mid-year 2009, Honolulu County lost nearly 300,000 square feet of occupancy. For the first time in five years, vacancy rates hit double digits as the market posted a 10.15% island-wide vacancy rate and the Central Business District jumped to 10.92%. Net average asking rents fell for the first time to $1.68 per square foot per month ("psf/mo").

Business optimism has continued to wane as many are forced to embrace conservative strategies to weather the downturn in the economy. Since job growth tends to lag behind other economic indicators, layoffs are likely to continue with negative net absorption forecasted for 2010.

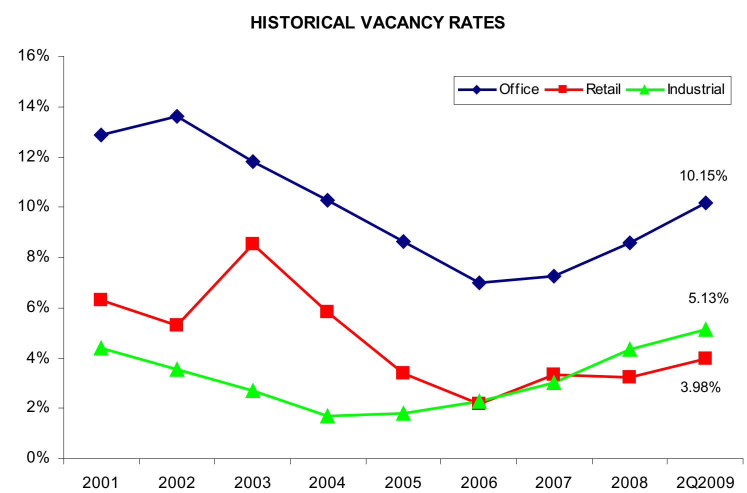
Retail
For the first six months of 2009, Honolulu's retail marketplace posted positive absorption and stable market conditions. Contrary to the sizeable declines in occupancy faced by many major U.S. metropolitan markets, Hawaii has been resilient. Vacancy rates remain among the lowest in the country with a 3.98% recorded at mid-year 2009. Despite the closure of several mid-box retailers such as Circuit City, Comp USA and USA Babies, neighborhood shopping centers and regional malls remained between 97% and 98% occupied. Rents posted their first decline in nearly six years having fallen from an average asking rent of $3.74 psf/mo to $3.52 psf/mo over the past six months. The most significant declines in asking rents occurred in the resort /specialty category.

Hawaii's vulnerability to downturns in the travel sector is being reflected in drastic declines in retail sales expenditures. For Honolulu County, first quarter retail sales have fallen by 7.7% or $429 million. Contributing to this decline has been the drop in air passenger arrivals and the resultant fall in sales, for May a 15% decline in tourism expenditures was reported, or roughly $133 million. Many resort area retailers are reporting 30% to 40% drops in sales and are struggling to meet their rent and payroll obligations.

Industrial
At mid-year 2009, Honolulu's industrial sector posted 314,091 square feet of negative net absorption continuing the trend of lost occupancy for the third consecutive year. Vacancy rates rose to 5.13%, its highest level in over six years. The financial crisis and the subsequent loss of CMBS funding contributed to several planned industrial parks falling into default with their lenders. Additionally, recently constructed industrial condominiums faced difficulty in sales, as many prospects encountered more stringent credit underwriting for their purchase loans.

The decline in construction activity coupled with downturns in both residential home sales and tourism, contributed to reduce the level of demand for warehouse distribution space. Industrial sales activity also reflects the poor business environment, having fallen by 11% for the first quarter.

Rental rates, which had risen to record levels, began their descent by falling from an average asking level of $1.31 psf/mo to $1.15 psf/mo over the past 18 months. CMFC anticipates rents to continue as available space becomes more prevalent due to an increase in business bankruptcies, foreclosures and downsizing.



Hotel

Declining hotel occupancy, falling air passenger arrival counts and dropping hotel room rates placed increased pressure on hotel operators to squeeze margins out of difficult market conditions. For Hawaii, hotel occupancy rates fell to 62%, its lowest ever recorded level since Hospitality Advisors began compiling records in 1987. Additionally, RevPAR declined by 21.1% to $103.

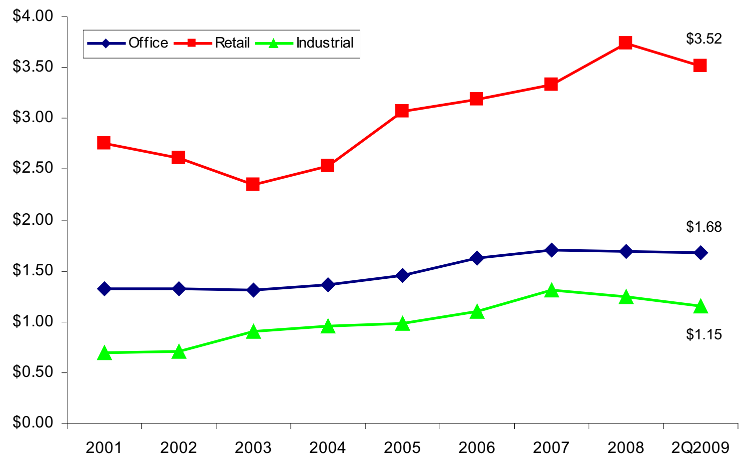
Nationally, hotel loan defaults and foreclosures have nearly doubled from $9 billion in the first quarter of 2009 to $17.3 billion as reported by Real Capital Analytics. Smith Travel Research reported that for luxury hotels, revenue has fallen for 12 consecutive months and by 28% since last April. Being a discretionary expenditure reliant upon favorable market conditions, vacation travel has suffered due the recession's impact on consumer confidence. Over the past five years, a large number of hotel transactions fueled by CMBS and institutional money traded hands. If an alternative source of funding is not found when these loan terms expire, many of these properties will likely go into default.

Multi-family

Over the past few years apartment capitalization rates fell to extremely low levels. Many transactions reported sub-4% return levels. The lack of supply and the extreme shortage of rentable apartment buildings contributed to the strong demand created for residential multifamily apartment investments. Falling into the $1 million to $3 million price range, these properties appealed to many entry level investors.

Over the past six months, CMFC recorded only four apartment transactions, reflecting a tremendous change in the activity for multi-family properties. The likely deterrent has been the dramatic drops in value encountered by small investors to the stock market, personal residential properties, and their businesses. Available funds were drastically depleted as alternative investment vehicle values dropped.

HISTORICAL AVERAGE ASKING RENTAL RATES



2009 Notable Transactions

Propety Type	Location	Buyer	Sales Price	Transaction Date
Golf/Resort	Kapalua Golf Course	Ty Management Corp	$49,800,000	3/27/2009
Industrial	Weyerhaueser Bldg	Thanh Lam, et al	$20,000,000	5/29/2009
Industrial	Pearl City Industrial Park	Fergus & Company	$13,040,000	6/23/2009
Industrial	94-1489 Moaniani St	A&B Properties, Inc.	$12,310,400	3/4/2009
Commercial Land	Kona Land	Kaiser Foundation Health Plan	$11,300,000	3/13/2009
Commercial Land	4390 Nuhou St	Property Development Centers (Safeway)	$11,000,000	4/30/2009
Industrial	94-547 Ukee St	WDCI	$9,560,000	3/4/2009
Office	2411 King Street & 931 Isenberg St	SLAA, LLC	$8,640,000	6/30/2009
Retail	802 Front Street	SMK Inc.	$8,000,000	6/1/2009

Featured Properties For Sale

DEVELOPMENT LAND

Kapolei BMX Sites
Largest Commercial Parcel Available in West Oahu
Land Area: 16.429 acres (4 lots) Zoning: BMX-3
(Individual lot sizes range from 3.688 to 5.020 acres)
Tenure: Fee Simple Asking Sales Price: Submit Offer
Contact: Mark Bratton (B) CCIM, VP

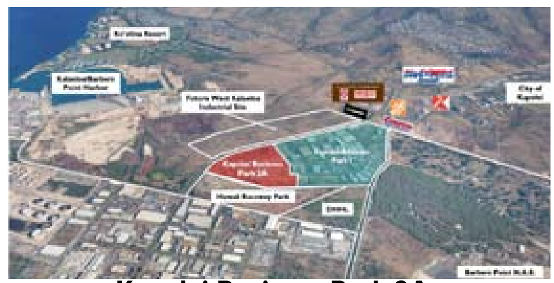
INDUSTRIAL BUILDING

2676 Waiwai Loop
Honolulu, HI
Land Area: 24,738 sq. ft. Zoning: I-2
Building Area: 22,735 sq. ft. Asking Sales Price: $5,500,000
Tenure: Fee Simple
Contact: William R. Froelich (S) JD, Associate

COMMERCIAL BUILDING

2879 Paa Street
Honolulu, HI
Land Area: 31,316 sq. ft. Zoning: B-2
Building area: 16,742 sq. ft. Tenure: Leasehold
Asking Sales Price: $699,000
Contact: Ronald C. Ward (S), VP / Alika Cosner (S), Associate

INDUSTRIAL LAND



Kapolei Business Park 2A
Kapolei, HI
Land Area: 53.71 Acres Zoning: I-2
Lots Available (size): 1 to 20 Acres Asking Sales Price: Undisclosed
Contact: Scott L. Mitchell (B) SIOR, EVP / Guy V. Kidder (S) CCIM SIOR, VP

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1800 Central Pacific Plaza
220 South King Street
Honolulu, HI 96813
Tel: 808-524-2666
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www.collierhawaii.com
www.colliershawaiiblog.com

Consulting & Research

Mike Y. Hamasu
Consulting & Research Director
Tel: 523-9792
mike@collierhawaii.com

Nanette C. Macapanpan (S)
Research Consultant/Project Manager
Tel: 523-9764
nanette@colliershawaii.com

Property Management

Bobbie Lau (S) CPM
Senior Vice President

Investment Services Group

Andrew D. Friedlander (B) SIOR
Principal Broker
Tel: 523-9797
andrew@colliershawaii.com

Scott L. Mitchell (B) SIOR
Executive Vice President
Tel: 523-9702
scott@colliershawaii.com

Jon-Eric Greene (B)
Senior Vice President
Tel: 523-9700
jeg@colliershawaii.com

Mark D. Bratton (R) CCIM
Vice President
Division Manager
Tel: 523-9708
mark@colliershawaii.com

Kim F. Scoggins (B)
Vice President
Co-Division Manager
Tel: 523-9762
kim@colliershawaii.com

Sean G. Tadaki (S) CCIM
Vice President
Office Division Manager
Tel: 523-9745
sean@colliershawaii.com

Nathan A. Fong (B)
Vice President
Tel: 523-9740
nathan@colliershawaii.com

Guy V. Kidder (S) CCIM SIOR
Vice President
Tel: 523-9735
guy@colliershawaii.com

Ronald Ward (S)
Vice President
Tel: 523-9747
ronald@colliershawaii.com

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If you would like additional information, please contact mike@colliershawaii.com