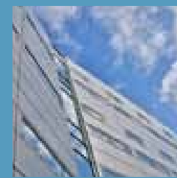
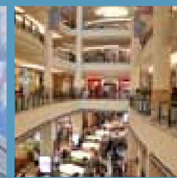
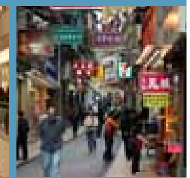
Global Real Estate Trends Review

2011







A series from Russell Reynolds Associates' Global Real Estate Practice, highlighting hiring trends in the industry

It is difficult to identify "trends" in a time as dynamic as the one we live in today. In fact, the only consistent sustained trend seems to be macro-level turbulence.

The European debt crisis hangs over the global economy like a black cloud. Stock market fluctuations in August sparked unease and generated fear of the dreaded "double dip" recession. Entering into an election year, it is clear domestic and global political dysfunction will continue to feed economic uncertainty.

With no real job growth on the horizon, it is no wonder that the fragile recovery of the last few years seems to have faltered, if not ground to a halt. Growth in the U.S. economy, the world's largest, averaged less than 1% in the first half of the year. Unemployment has hovered just above 9% for several months and long-term joblessness is at a record high.

Within real estate, we see conflicting signs.

The once red hot public markets have plummeted. For much of the past two years, real estate stocks outperformed the broader stock market, but that ended dramatically in September as investors feared that a weak global economy would sap demand for commercial space. The Dow Jones All Equity REIT Index posted a negative 15% total return during the third quarter, the largest drop since the first quarter of 2009.

In particular, the mortgage REIT sector was a casualty due to potentially impactful SEC regulations and the direct hit taken in access to capital due to ripple effects from the EU crisis. In one recent two day stretch, aggregate losses among leading mortgage REITS had reached as much as 11.1%, the biggest drop in almost three years.

The debt markets have dried up, with the resurgence of CMBS in particular put on indefinite hold. In the fourth quarter, the pipeline of commercial mortgage securities is expected to fall to about $3 billion, according to analysts at J.P. Morgan, less than half the volume seen in the first half of the year. The rate of loans delinquent by 30 days or more has continued to rise over the last five months.

Meanwhile, actual property values enjoyed a continued growth throughout the end of July, with the Moody's/REAL Commercial Property Index reporting a 5% advance in July alone. Early indication of a "leveling off" included plateau pricing in markets such as Washington, D.C. multi-family and New York office. According to Green Street, values have fallen since May of this year.

From a human capital standpoint, the points highlighted above seem to have had very little impact on hiring within commercial real estate. For seven straight quarters, hiring has been consistent at the senior most levels within commercial real estate. Activity seems to hover somewhere equidistant from the peaks of 2007 and the troughs of 2009. Specifically, we continue to see:

- Heightened demand for marketing / investor relations talent within the fund management sector.
- Consistent need for Chief Financial Officers.
- CEO/COO hires to take over distressed, broken, or recapitalized / revamped businesses.
- Continued surplus of mid level real estate talent, meaning an oversupply of acquisitions, development and asset management professionals.

- Rebuilt lending teams on Wall Street, in particular the “re-potting” of senior and mid-level talent from Lehman Brothers.
- Rapid fire growth and reduction in force for CMBS teams.
- A pullback in hiring within the REIT sector, on the heels of robust C-suite level activity in 2010 and the first half of 2011.

Given the overall uncertainty in the capital, property, and employment markets, the question we are most often asked is “What do you think will happen with compensation this year?”

Based on our own observations and the more in-depth knowledge of Kevin Christenson, Founder and CEO of Christenson Advisors, a leading compensation consulting firm within commercial real estate, we believe that most real estate companies expect overall compensation to increase. While compensation for 2010 was, on average, near target, many companies expect to achieve target or above target performance this year. However, while sentiment in the market was very strong the first half of 2011, the economic struggles and debt ceiling crisis this summer have more real estate companies worried about the future. The resulting uncertainty may place downward pressure on those pieces of compensation that are more discretionary.

Compensation will vary widely by product offering and asset class, as well as between public and private companies. Overall, on the commercial side, compensation is a long way from the halcyon days of 2006/2007. For stable companies, both private and public, base salary increases should again average in the (3% to 4% range). Companies that are in a restructuring mode continue to keep base salaries frozen and provide more upside as it relates to incentive compensation.

For some public companies, particularly those that have raised capital and are doing deals, compensation in 2010 and 2011 is higher than 2007. Clearly there is lower delta and greater stability in compensation in the public arena, particularly as it relates to those companies that have raised capital. In particular, select C-Suite positions (CEO, COO and CIO executives) who have moved the needle in this market (raised capital and executed transactions) have experienced material increases.

Within private equity/investment management, compensation remains at a steep discount to peek. With respect to cash bonuses, some have increased targets at a greater rate than the public companies due to limited or non-existent long-term incentive opportunities. For instance, investment managers have increased bonus pools in order to retain key executives, given that past promotes are gone or underwater, and current fund raises/closings to provide additional promote/carry will take may years to deliver a payout. While there are many funds in the market, very few have been closed. This restricts the ability of firms to provide promote/carry to the team. While many companies have looked to increase the bonus pool relative to overall cash flow, very few are changing promote structure and/or forgiving any underwater promote obligations of management.

At a micro level, top flight asset managers, portfolio managers, capital raising professionals and sophisticated finance executives continue to be in high demand and experiencing material increases. Depending on the company, transactions and development are starting to come back, but it is very early. Within the debt side, a significant barbell exists - platforms that have sprung up or enjoyed a resurgence filling the void left by large commercial banks are seeing peak activity and should compensate as such. In most cases, however, the peaks of 2007 are unlikely to be seen again in the near or mid terms.

According to Christenson, firms are moving methodologically toward programs that “keep it simple”. Cash bonuses are tied to the annual performance (cash flow) of the company and long-term incentive compensation derived from long-term value creation. With the new Dodd Frank legislation there continues to be a lot of pressure on Boards/ Compensation Committees to make certain that compensation is clear and understandable, performance based, and reasonable. There is intense scrutiny/downward pressure on tax gross-ups, change-in-control payments or golden parachutes, multiples with respect to severance, and perks.

Track Record

Recent Completions Include:

- **Board Members** for one of North America's largest investors and owners of commercial real estate
- **Chief Executive Officer** for a private equity-backed, privatized triple net lease REIT
- **Managing Director, Asset Management** for a large multi-strategy private equity firm
- **President** for a private equity-backed, equity-backed, privatized triple net lease REIT
- **President** of a large industrial portfolio backed by a prominent private equity firm
- **President, Retail Division** of a premier real estate investment Company, with fully integrated operations
- **Principal, Investments** for a debt fund platform within a large multi-strategy private equity firm
- **Senior Vice President/Chief Accounting Officer** for a pre-IPO industrial REIT
- **Vice President of Acquisitions** for a large opportunity fund
- **Vice President of Marketing** for an urban-focused, multi-strategy fund manager

About Russell Reynolds Associates

Leadership for a Changing World. In today's global business environment, success is driven by the talent, vision and leadership capabilities of senior executives.

Russell Reynolds Associates is a leading global executive search and assessment firm with more than 300 consultants based in 40 offices worldwide. Our consultants work closely with public and private organizations to identify, assess and recruit senior executives and board members to drive long-term growth and success. We value teamwork, serving our clients with a collaborative approach that spans our international network of sector and functional experts.

Our in-depth knowledge of major industries and our clients' specific business challenges, combined with our understanding of who and what makes an effective leader, ensure that our clients secure the best leadership teams for the ongoing success of their businesses. For more information, please visit us at www.russellreynolds.com.