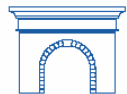


# **The US Real Estate Market:** Issues and Opportunities for Islamic Investors

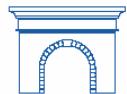
Craig Friedman  
Managing Member  
Arch Street Capital Advisors, L.L.C.



Arch Street Capital  
Advisors, L.L.C.

# Overview

- Patriot Act III – “Know Your Customer”
- Islamic Finance in the U.S.
- Issues Facing Islamic Finance
- Opportunities for Islamic Investors in the U.S.
- Case Studies



# Patriot Act III

*(“Know Your Customer”)*

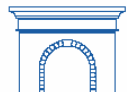
*\*A law passed by the U.S. Congress in 2001 as a response to the September 11, 2001 attacks aimed to facilitate the prevention, detection and prosecution of international money laundering and the financing of terrorism.*

## **Provisions:**

- Requires financial institutions to observe due diligence standards, including procedures for customer identification for accounts they open and maintain for their non U.S. based customers.

## **Implications for Foreign Investors:**

- **Identifies the Investor to Lenders, Joint Venture Partners and Institutional Sellers.**



# Patriot Act III

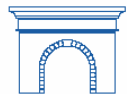
*("Know Your Customer")*

## **Satisfying the Patriot Act**

- Publicly traded companies provide transparency
- Companies owned in part by Sovereign Nations
- Regulated by Central Bank or Governmental Regulator
- Syndication Strategies

## **Maintaining Investor Privacy:**

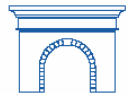
- Investors' Privacy can be maintained through the delivery of a certificate from the foreign financial institution or their legal counsel confirming that appropriate diligence has been conducted on such investors and their sources of funds.



# **Patriot Act III**

*("Know Your Customer")*

**For a well sponsored Investor with an experienced U.S. based advisory team the Patriot Act is not an impediment to investing in the U.S.**

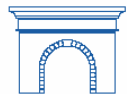


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# Islamic Finance in the U.S.

Although reliable industry data is not available, based on our experience and that of our clients, we are confident that Islamic Finance for U.S. commercial real estate is growing:

- Any commercial real estate asset can be financed in a Shari'a compliant manner.
- In today's market the pricing for Shari'a compliant financing is comparable to conventional financing of the same asset.
- Now that more lenders are aware that Shari'a compliant loans can be securitized the industry will continue to grow.
- The U.S. Government is encouraging Shari'a compliant activity:
  - In 2005 the U.S. Treasury launched the “Islamic finance scholar in residence program” to promote broader awareness of Islamic Finance.
  - In 2006 the U.S. interagency group on Islamic banking was formed to address outstanding regulatory issues.



# Islamic Finance in the U.S.

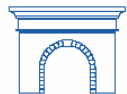
## Institutional Lenders Providing Shari'a Compliant Financing:

### Banks/ Investment Banks

- Bank of America
- Credit Suisse
- Deutsche Bank
- ING
- JP Morgan/Chase
- Key Bank
- LaSalle Bank
- Lehman Brothers

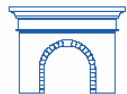
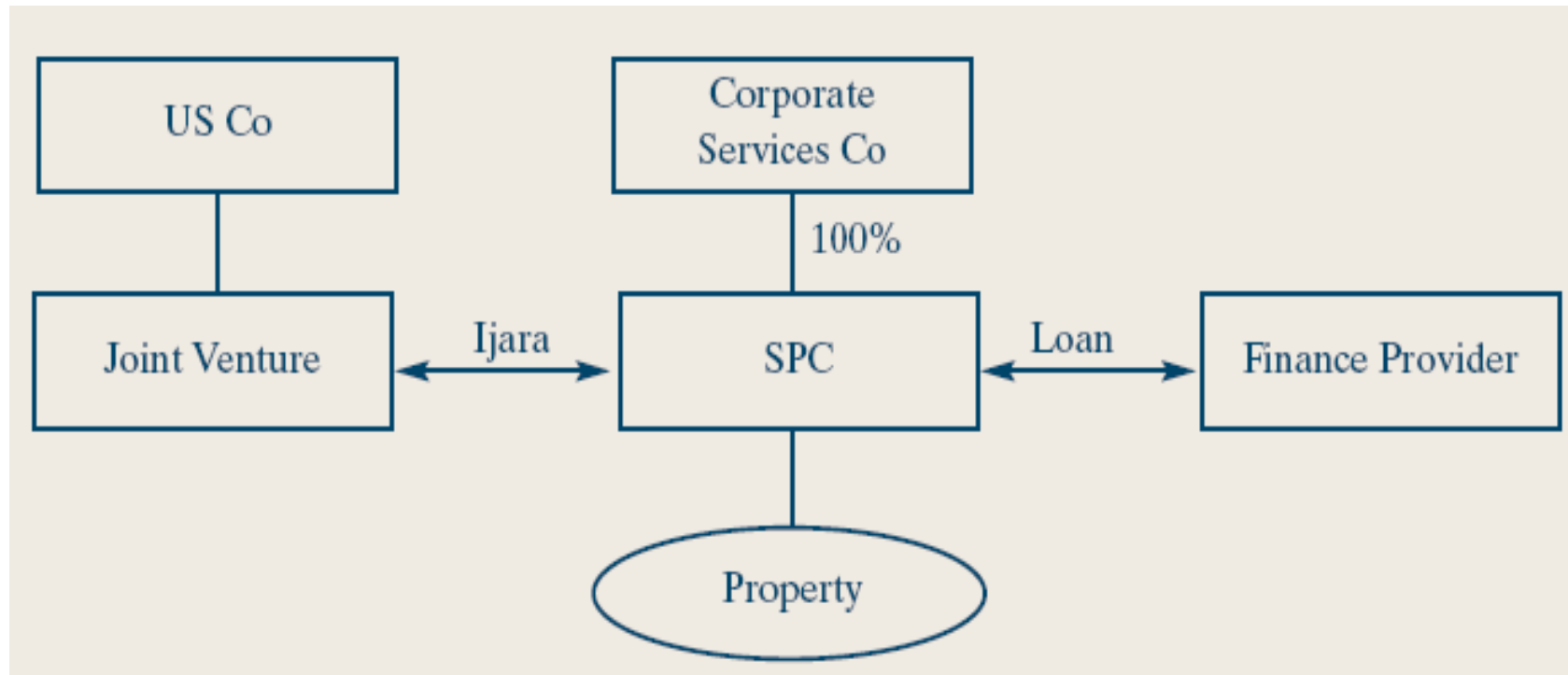
### Life Insurance Companies

- All State Life Insurance Company
- Cigna Real Estate Services
- Jackson National Life Insurance
- Principal Life Insurance Company



# Islamic Finance in the U.S.

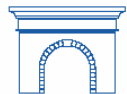
## Shari'a Compliant Financing Structure (*ijara*):



# Islamic Finance in the U.S.

## Issues Facing Islamic Investors in the U.S.

- Informational transparency required by the Patriot Act
- Misconceptions by U.S. operators
- Complexities associated with structuring Shari'a compliant financing
- Negotiation of joint venture / operating agreements in accordance with Islamic Law
- Establishment of U.S. bank accounts
- Maintaining U.S. based books and records for audits
- Obtaining periodic valuations
- Tax structuring to minimize U.S. tax obligations
- Sourcing attractive investment opportunities in competition with U.S. capital sources
- Identifying, hiring, and/or partnering with local operating expertise
- Overseeing investments separated by geographic distance and multiple time zones

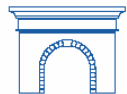


# Islamic Finance in the U.S.

## Solutions / Mitigants:

- Work with knowledgeable third parties with expertise in Islamic Finance including: Tax Advisors, Legal Counsel, Mortgage Brokers, Lenders, and Operators
- Form operating partnerships with well regarded companies in the U.S.
- Engage U.S. based advisor to provide on-the-ground oversight of transactions
  - Benefits:
    - Ability to source both broadly marketed and off market transactions
    - Intimate understanding of U.S. capital markets
    - Direct interaction with Operators / Sponsors
    - Ability to oversee legal, tax, and accounting functions
    - Ability to respond / react in a timely manner to operating issues

**By aligning with an experienced team of advisors your U.S. real estate investment goals can be achieved.**



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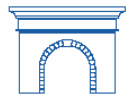
# Opportunities for Islamic Investors in the U.S.

## **Benefits of Investing in the U.S. :**

- Geographic/political diversification
- Currency diversification
- Relatively low volatility
- Liquidity: ability to sell into a deep market of investors
- Transparency of information
- Advanced legal structures - allow for more diverse transactions in the marketplace to be Shari'a compliant
- Investment community's familiarity with Shari'a compliant investing

## **Competitive Advantages of Islamic Capital vs. U.S. Based Capital:**

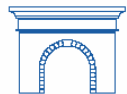
- Responsiveness and Agility- ability to act quickly and in an entrepreneurial way
- Structural flexibility
- Exchange rates: weakness of U.S. dollar
- Capitalization: Ability to complete acquisitions using moderate, rather than maximum financing amounts
- Tax efficiencies associated with being a foreign investor (Murabaha)



# Opportunities for Islamic Investors in the U.S.

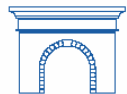
## Reasons to Invest in the U.S. Today

- Relative weakness of the \$US Dollar against foreign currencies.
- As capital moves globally, U.S. real estate is inexpensive when compared with other major global cities.
- In light of other benefits (information transparency, liquidity, etc.) relatively inexpensive pricing should ensure that funds continue to flow to U.S. commercial real estate.
- Rising yields offer more attractive risk adjusted returns.



# Opportunities for Islamic Investors in the U.S.

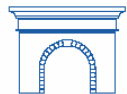
*Appreciation of the GBP against the USD*



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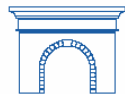
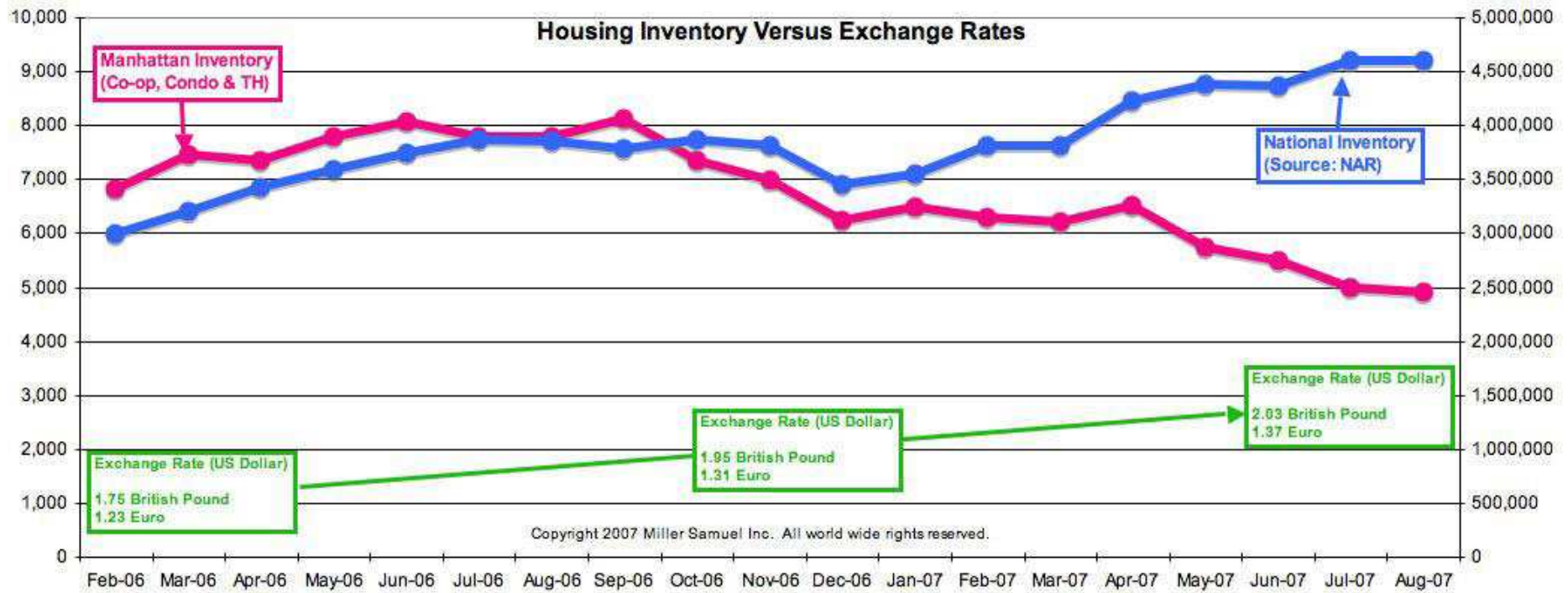
# Opportunities for Islamic Investors in the U.S.

*Appreciation of the Euro against the USD*

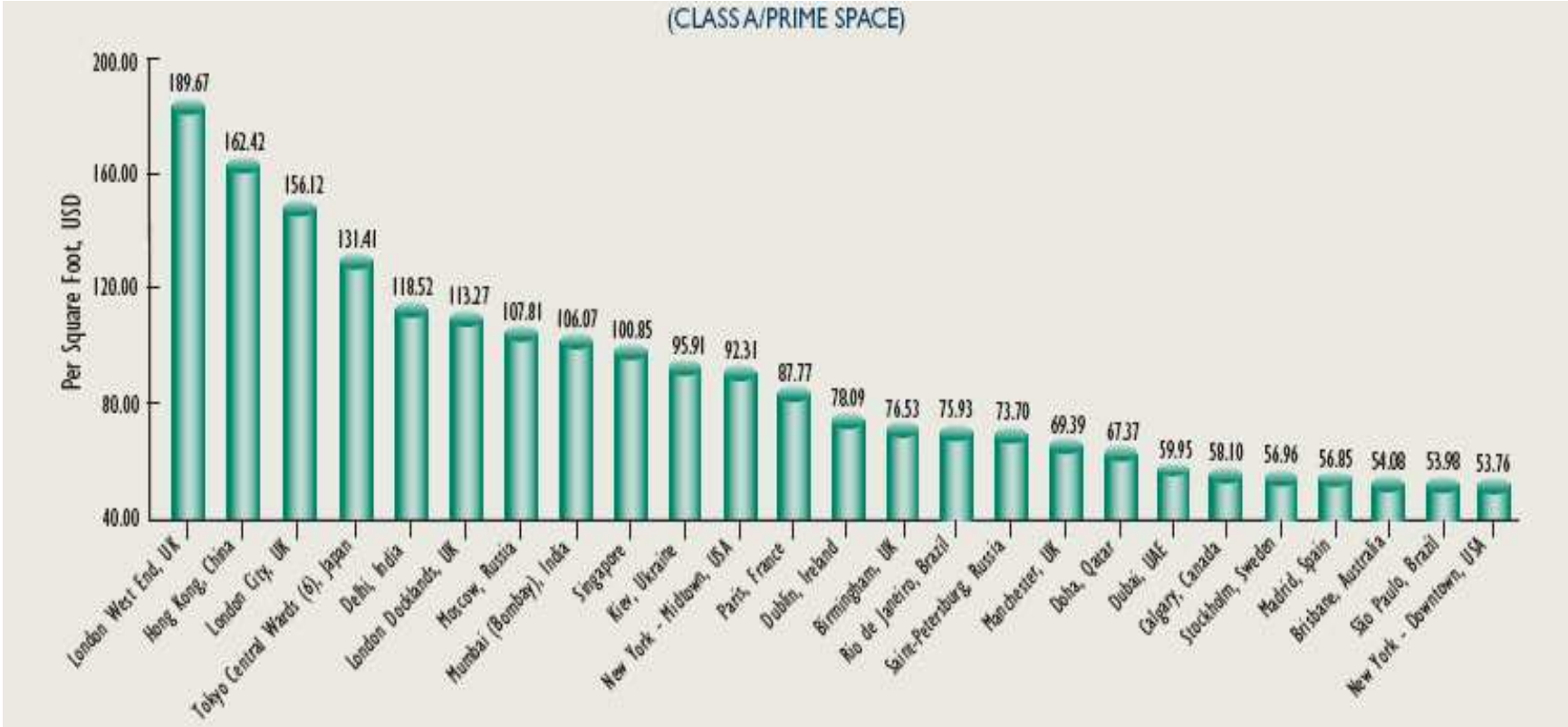


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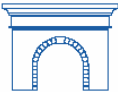
# Opportunities for Islamic Investors in the U.S.



# Global Office Occupancy Costs- Top 25



Source: Colliers International



# Global Capitalization Rates/Initial Yields-25 Lowest

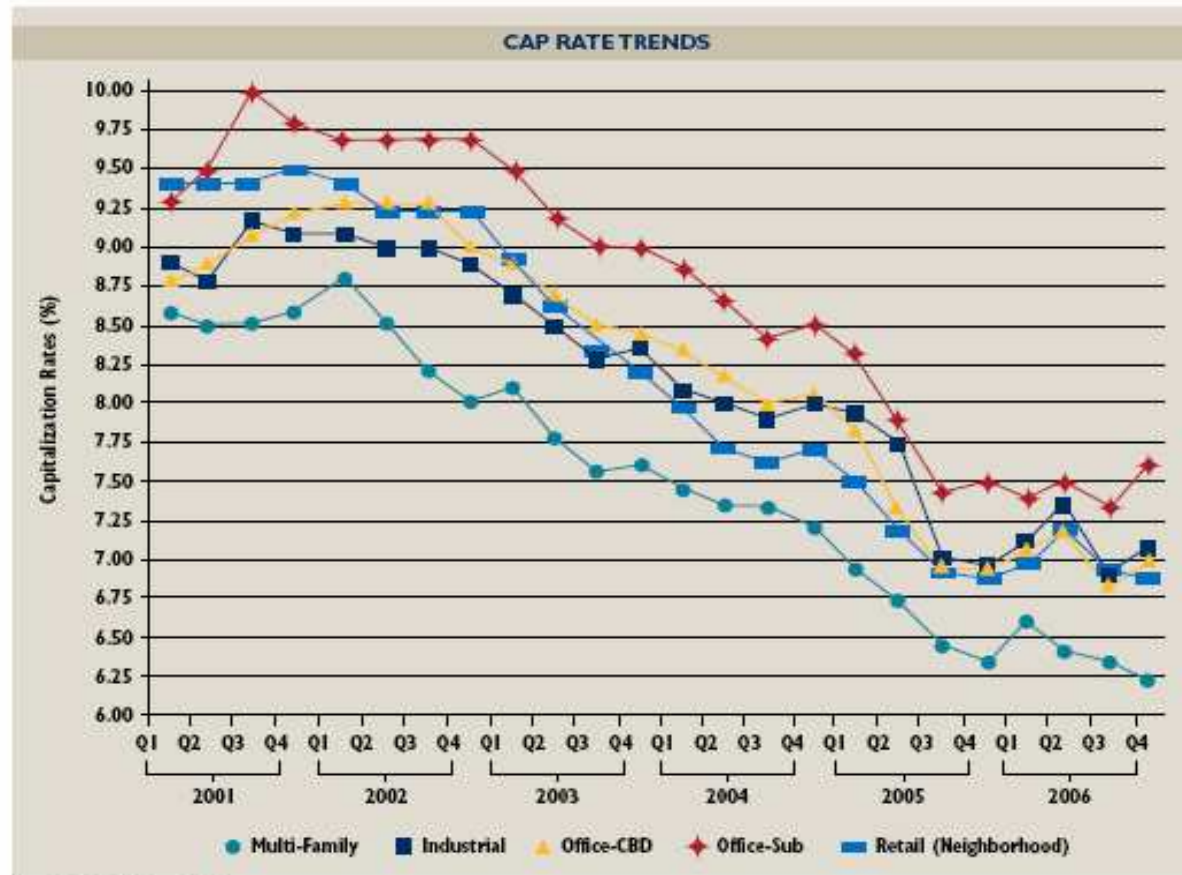


Source: Colliers International

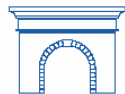


# Opportunities for Islamic Investors in the U.S.

## U.S. Capitalization Rate Trends



Source: Real Estate Research Corp.

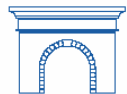


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# Opportunities for Islamic Investors in the U.S.

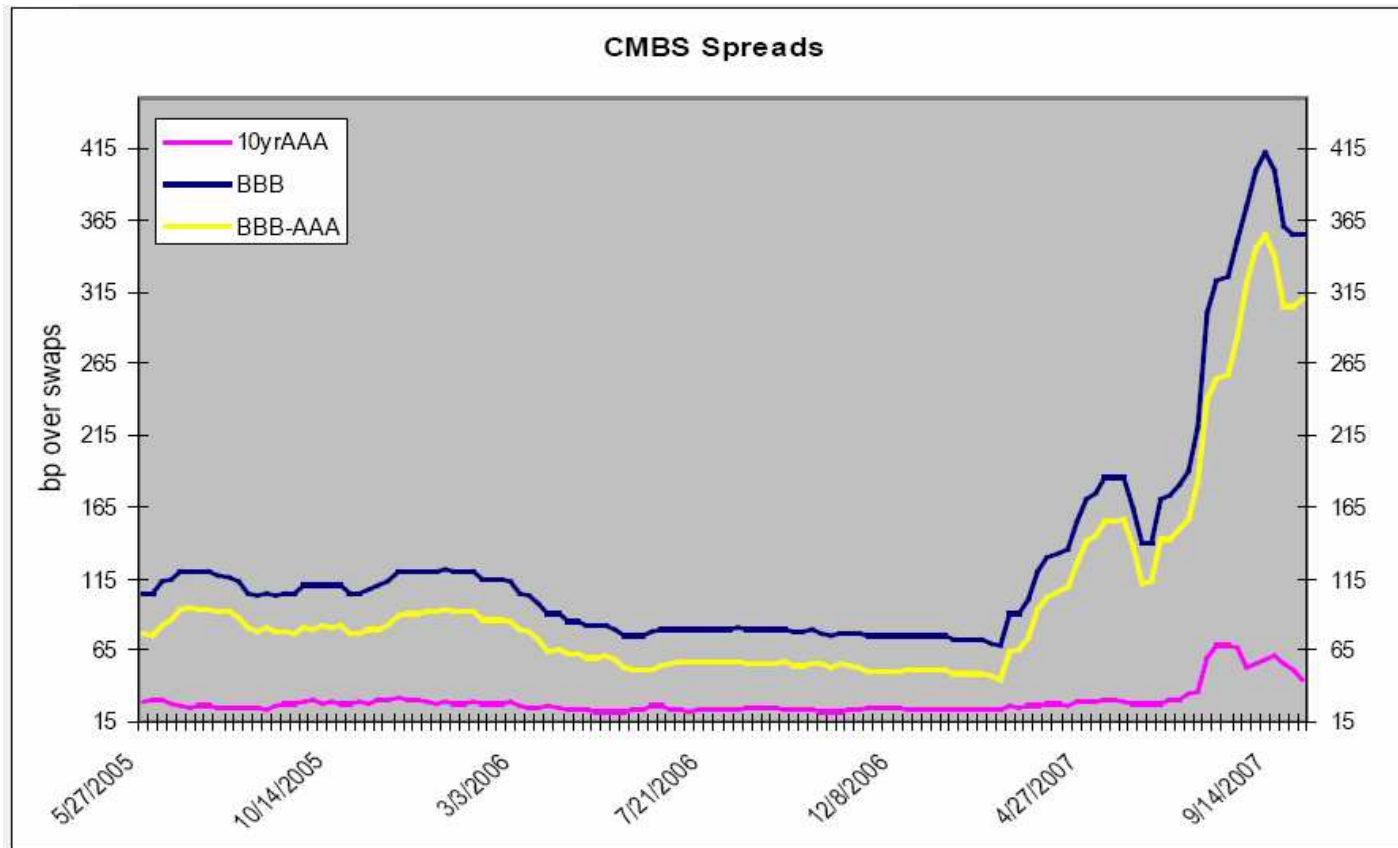
## Current State of the U.S. Market:

- “Credit Crunch”: financing markets are no longer providing aggressive financing terms available over the past few years.
- CMBS Issuance has decreased dramatically:
  - \$8.2 bn issued in Sept. '07 versus \$23.4 bn of Sept. '06
  - Securitization programs have reported originations have dropped in excess of 50%
  - \$36 bn of Issuances in the pipeline for the fourth quarter versus \$72.4 bn in '06
- Lenders cautiously re-entering the market with stricter underwriting standards
  - Lower loan to value ratios
  - Amortization requirements
  - Higher debt service coverage required

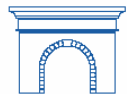


# Opportunities for Islamic Investors in the U.S.

*Increase in CMBS Spreads*



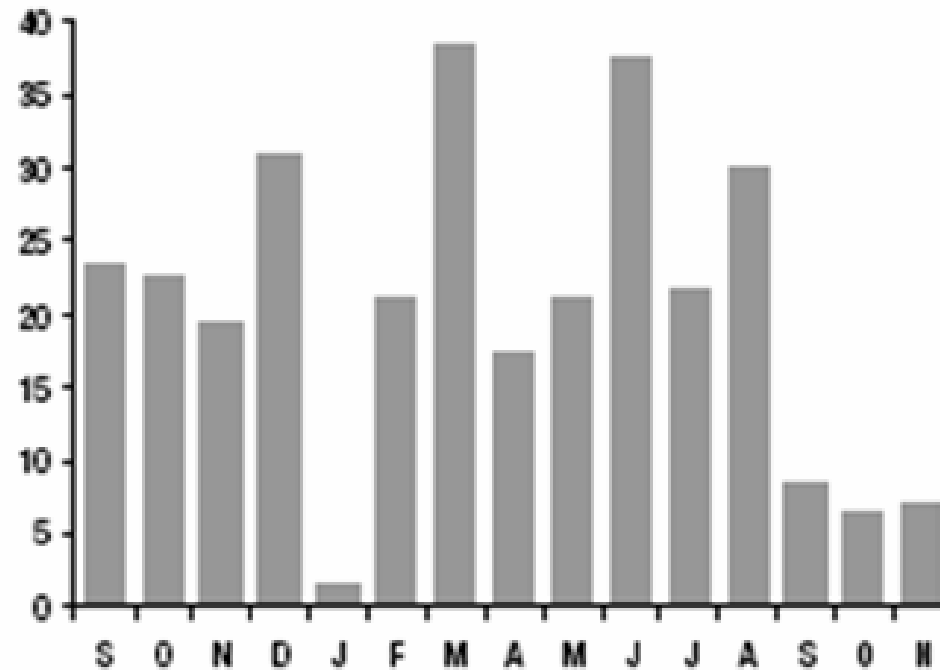
Source: Commercial Real Estate Weekly



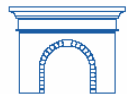
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# Opportunities for Islamic Investors in the U.S.

## U.S. CMBS (9/06- Present) Monthly Issuance (\$ Bn)



Source: Commercial Mortgage Alert

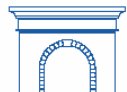


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# Opportunities for Islamic Investors in the U.S.

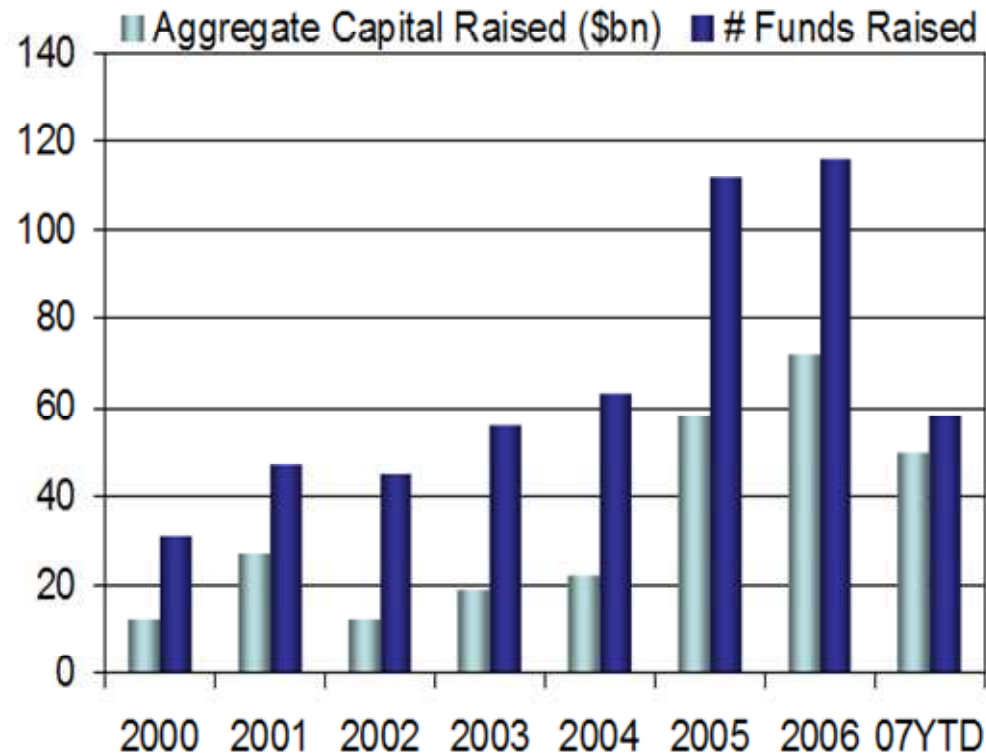
## Current State of the U.S. Market:

- Underlying real estate fundamentals of primary markets remain strong, such as: New York City, Washington D.C., San Francisco.
- Cap rates remain low, but in some markets have increased ~100 bps from last year
- Fund flows remain robust
  - Foreign investment in the U.S. remains high
  - Significant 4<sup>th</sup> quarter 2007 closings may result in real estate funds raising more than the \$40+bn raised in 2006
  - Most fund investors expect to increase real estate allocations over the long term

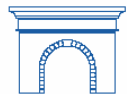


# Growth of Private Equity Real Estate Fundraising

2000 – 2007



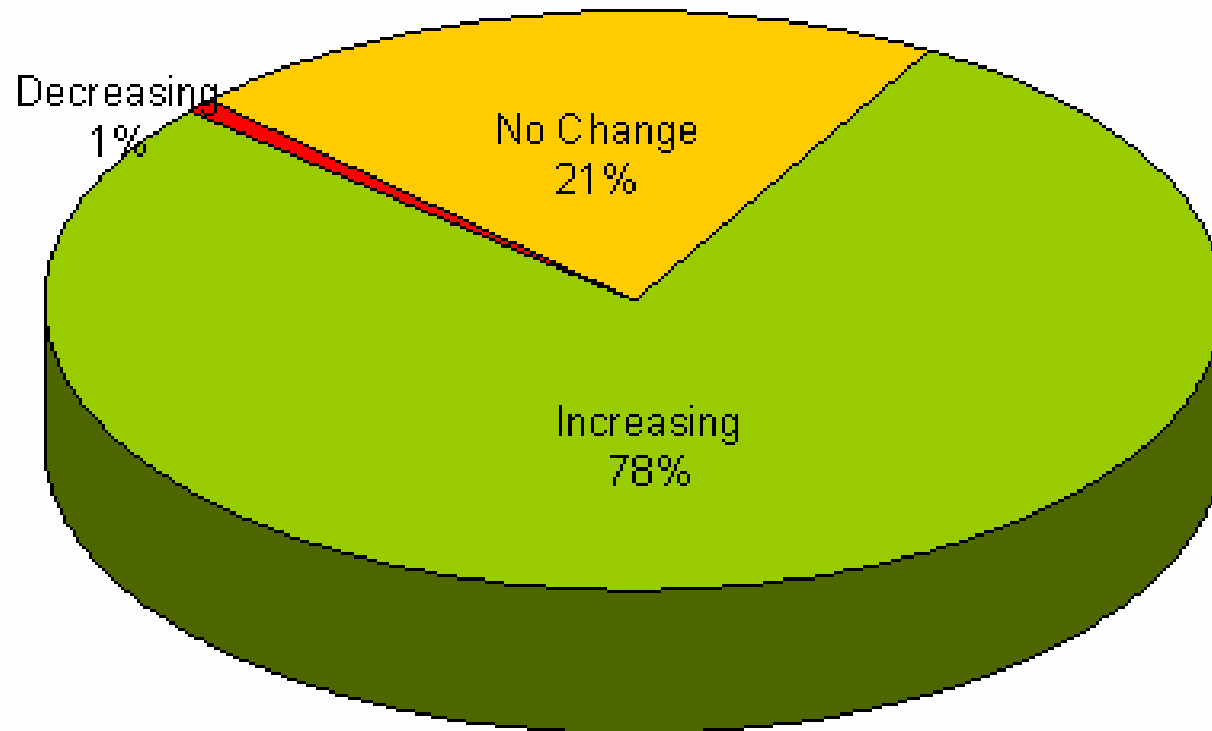
Source: Preqin 2007 Private Equity Real Estate Review, C&W Capital Markets Group



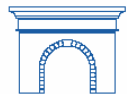
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## Long-term Real Estate Target Allocation Intentions of Limited Partners

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Source: Preqin 2007 Private Equity Real Estate Review, C&W Capital Markets Group

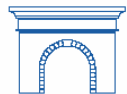


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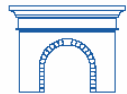
# Opportunities for Islamic Investors in the U.S.

## Investment Opportunities Today:

- High Growth Sectors (example: Healthcare Real Estate)
- Discounted Land Acquisitions
- Alternative Assets / Distressed Opportunities
- Mezzanine / Preferred equity positions
- Recapitalizations
- Issuance of Sukuks
- Entity Investments (through partnership in operating businesses)



# Recent Case Studies



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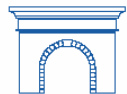
# Case Study I

## Property Information:

- **Asset Type:** Skilled Nursing Facility
- **Location:** Harrisburg, Pennsylvania
- **Operating History:** Operated by municipality at a significant loss
- **Source:** Off market transaction based on relationship
- **Investment Strategy:** Turnaround situation  
Aging of the population

## Execution of Investment Strategy:

- Purchased property at a significant discount to replacement cost
- Established bridge financing upon acquisition
- Stabilized property within 6 months and refinanced out bridge financing and investors' equity
- Property is generating substantial cash flow to investors without equity risk
- Working with partners on another similar off market transaction



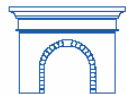
# Case Study II

## Property Information:

- **Asset Type:** Mixed Use Entitlement/Development
- **Location:** San Francisco, California
- **Operating History:** Commercial Office Building fully occupied
- **Source:** Controlled by close relationship with local developer
- **Investment Strategy:** Entitle and upzone land, to be sold to a developer  
City looking to create urban core and improve adjacent transportation capacity

## Execution of Investment Strategy:

- Work closely with the city to satisfy transportation objectives and “Green” building goals
- Corresponding benefit in award of increased height and density



# Conclusion

- The U.S. commercial real estate market continues to attract foreign investors, including Islamic investors, for many reasons including attractive risk adjusted returns, diversification, liquidity, opportunities for currency appreciation, and others.
- For Islamic investors considering U.S. commercial real estate investment, financing is available for all property types on terms and conditions equal to those available to conventional borrowers.
- Attractive opportunities in U.S. commercial real estate can be sourced today more than in any time in recent memory.
- To ensure that Islamic investors have the greatest opportunity to meet their U.S. real estate investment objectives and to efficiently satisfy all requirements imposed on non-U.S. investors, it is advisable to utilize the skills of advisors with deep experience in these areas.

