PARAMOUNT CAPITAL CORPORATION

VIEW OF THE MARKET NEWSLETTER

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Strategy and Insight for the Commercial Real Estate Industry

Inside This Issue:

Real Estate Focus:

- **New CRE Book by Our Editor, Joseph Ori.**
- **Prudential Real Estate Investors Trends for 2016.**
- **Booming Self Storage Industry.**
- **New Lease Accounting Rules Will Create Havoc for CRE.**
- **CRE Financing Rates, Courtesy of Berkadia Commercial Mortgage, LLC**

Economic/Investment Focus:

- **16 Rules of Investment from One of the World's Greatest Investors, John Templeton**
- **Lincoln's Greatness**

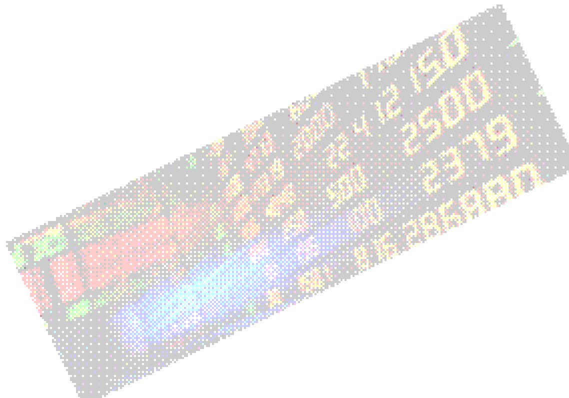
REIT Focus:

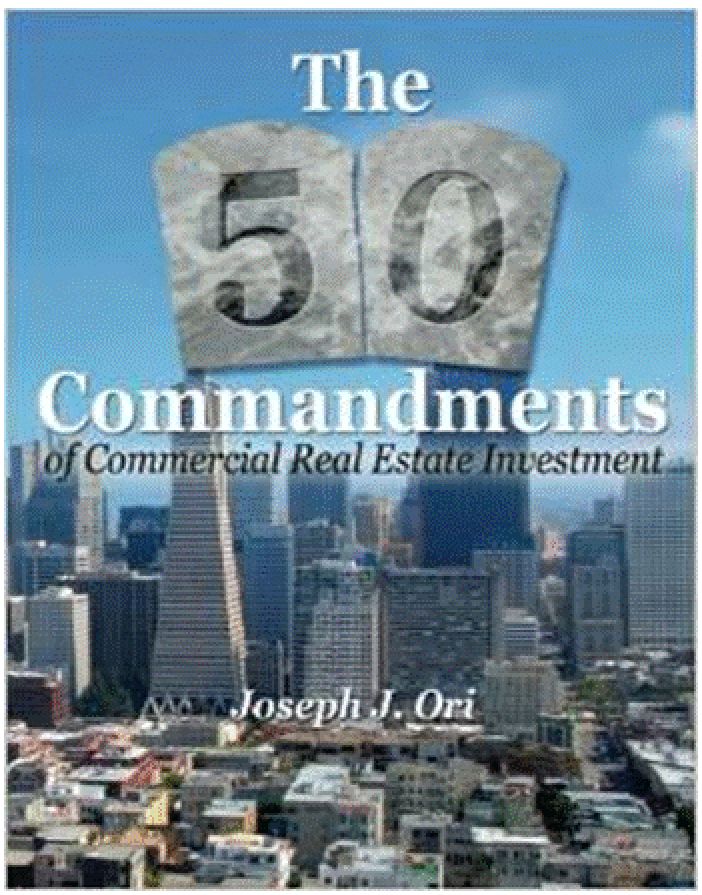
- **REIT Statistics.**
- **REIT Review: Franklin Street Properties Corp., an office REIT.**

REAL ESTATE FOCUS

New CRE Book by Our Editor, Joseph Ori

The editor of this newsletter, Joseph Ori, is pleased to announce the publication of his first book, “The 50 Commandments of Commercial Real Estate Investment”. The book is being published through Amazon and is available to purchase for only $15.99, on its web site at this link: http://www.amazon.com/Commandments-Commercial-Real-Estate-Investment/dp/1508859175/ref=sr_1_3?s=books&ie=UTF8&qid=1434055234&sr=1-3&keywords=50+commandments





The 50 Commandments of Commercial Real Estate Investment compiles the choice pieces of advice Mr. Ori has amassed over 35 years in the CRE industry.

Mr. Ori lists essential dos and don'ts, mistakes, and successful strategies with a mixture of critical analysis and a keen sense of satirical humor—reinforced by his encyclopedic knowledge of the commercial real estate environment.

Mr. Ori covers all areas of the industry. Commercial real estate investment, finance, development, capital markets, and management tactics are all given his full attention—as are leasing, financial analysis, and institutional investments. He applies his commandments to all property types, including apartments, office buildings, shopping centers, industrial warehouses, lodging properties, and senior housing.

Prudential Real Estate Investors Trends for 2016

Prudential Real Estate Investors has just published its CRE Trends for 2016 and below are some of the highlights (all charts are per Prudential Real Estate Investors).

1. Transaction Volume Increases

Global CRE transaction volumes have increased substantially during the past six years with $880 billion in 2015 as compared to the peak volume of $1,070 billion in 2007. According to real estate consultant, Preqin, $91 billion in capital has been raised by private real estate funds during 2015 with an additional $240 billion ready to be invested. Global CRE market fundamentals continue to improve, which will result in increased transaction volume.

EXHIBIT 1: GLOBAL TRANSACTION VOLUME ($ BILLION)

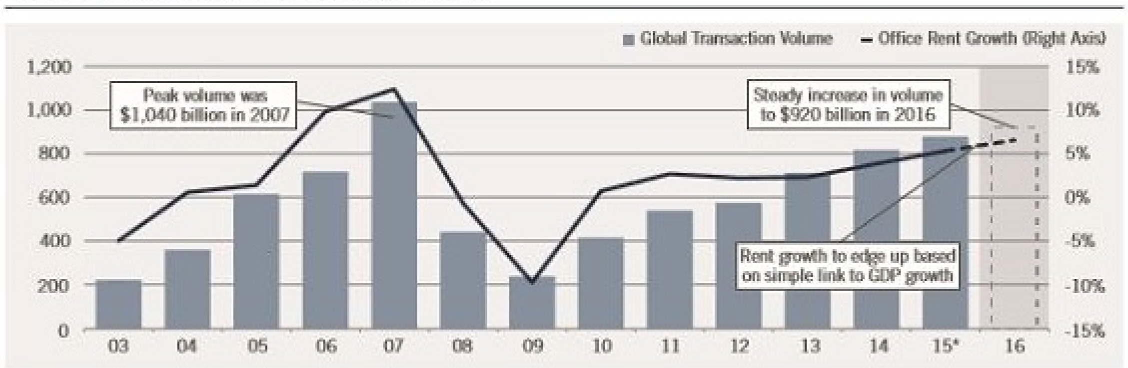
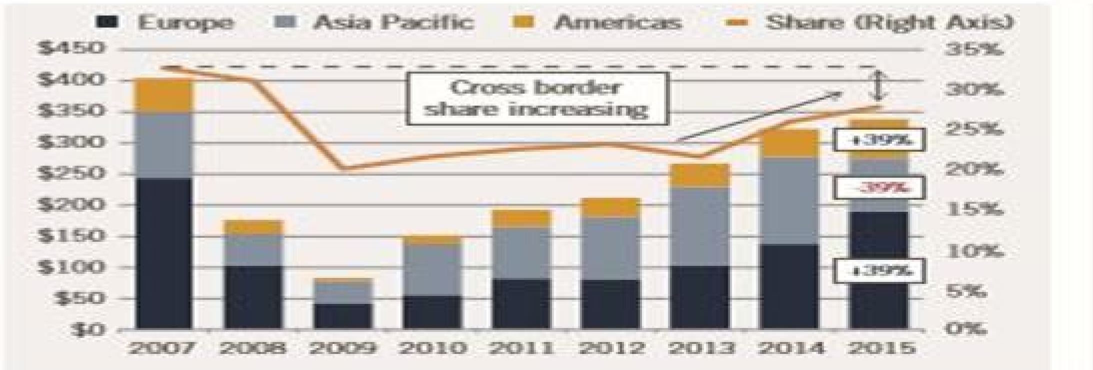


*Figure for 2015 based on four quarter total to 3Q15; Total volume excludes land transactions.
Sources: Real Capital Analytics, Prudential Real Estate Investors; As of December 2015.

2. Investment Horizons Broaden

Global real estate markets are awash in liquidity as investors have a lot of capital to deploy around the world. The challenge in today's overpriced CRE market is to deploy that capital in a manner that generates high risk adjusted returns. During the past year, there have been $340 billion in cross-border transactions

EXHIBIT 2: GLOBAL CROSS BORDER INVESTMENT VOLUME ($ BILLION)

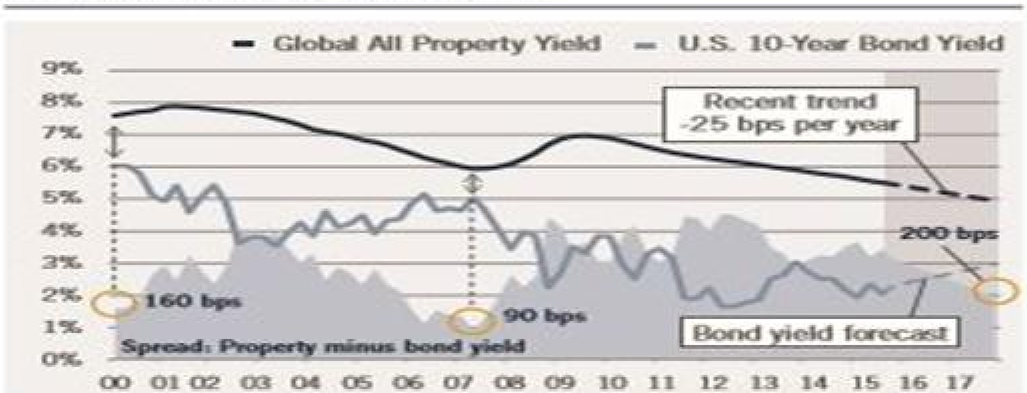


Sources: Real Capital Analytics, Prudential Real Estate Investors; As of Decemb

3. Yield Compression Continues

CRE cap rates and yields are at record lows and are expected to fall even further in 2016. This is due to the abundance of capital, high demand and favorable market momentum. Cap rates in the 24 hour cities like New York, San Francisco and London are already at nose bleed single digits and may go even lower as the spread between shrinking cap rates and yields on government bonds still remains high.

EXHIBIT 4: GLOBAL ALL PROPERTY PRIME YIELD & U.S. GOVERNMENT BOND YIELD

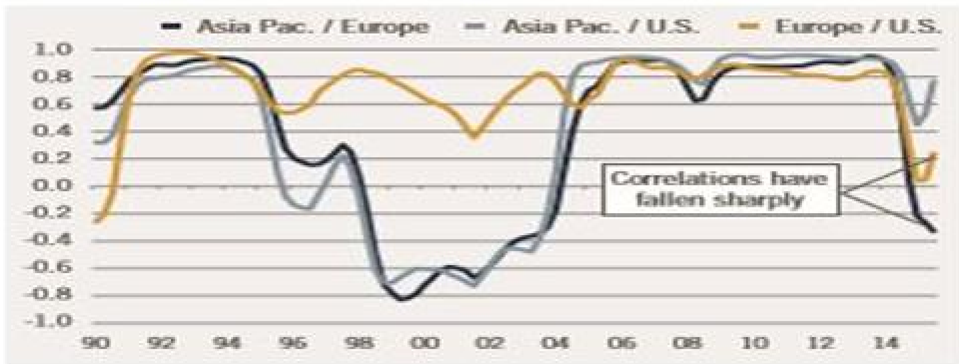


Sources: Oxford Economics, CoStar, Cushman & Wakefield, JLL, CBRE, Prude
Investors; As of December 2015.

4. Diversificaation Makes a Comeback

The correlation of global CRE markets has fallen sharply during the last few years and diversification efforts can lower risk and increase return. With low cap rates and falling yields, CRE supply and demand fundamentals have become misaligned due to contrasting economic conditions and policies.

EXHIBIT 6: ROLLING 5-YEAR ALL PROPERTY CAPITAL VALUE GROWTH CORRELATION (LOCAL CURRENCY BASIS)

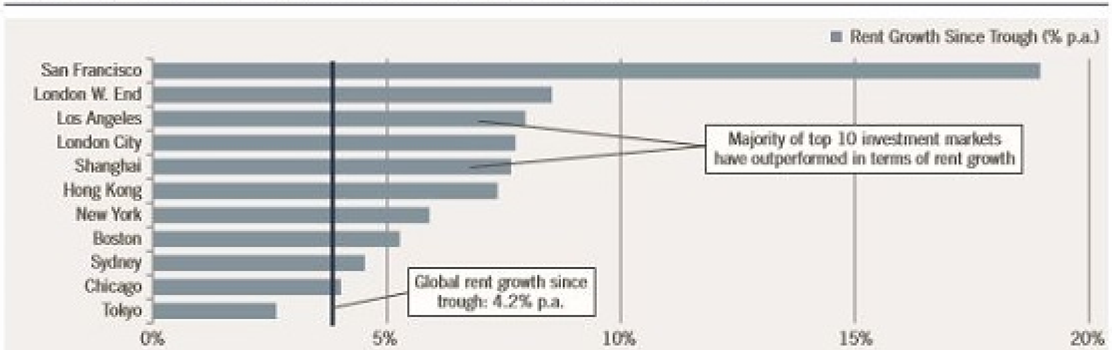


Sources: NCREIF, Cushman & Wakefield, JLL, Prudential Real Estate Investors; /

5. Relocation Away from Gateway Markets

Institutional investors are beginning to shy away from investments in the 24 hour gateway cities where they were most successful in making investments and attracting tenants. Cities such as Boston, Los Angeles, New York and San Francisco have seen a huge influx of investors and capital, driving down cap rates and increasing prices to unsustainable levels. These investors will begin rotating their capital to smaller cities and markets.

EXHIBIT 8: OFFICE RENT GROWTH SINCE TROUGH – TOP 10 INVESTMENT MARKETS

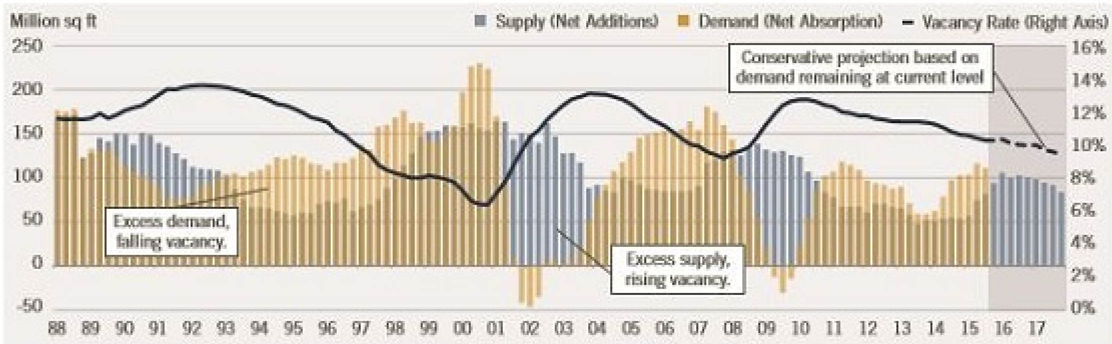


Sources: CBRE, Cushman & Wakefield, JLL, Colliers, Prudential Real Estate Investors; As of December 2015.

6. Vacancy Falls Further

The supply of new space is tepid at best and tenant demand will remain constant. This will result in vacancy rates falling, especially in the gateway markets.

EXHIBIT 9: GLOBAL OFFICE SUPPLY, DEMAND & VACANCY (ROLLING 4Q)

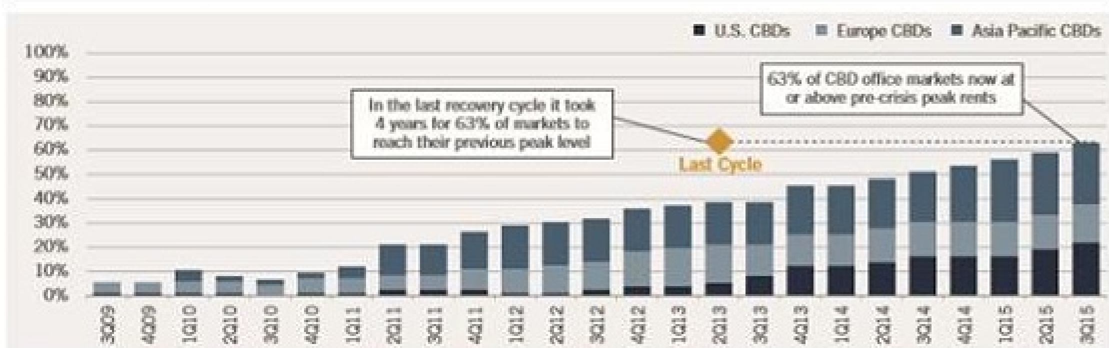


Sources: CoStar, Cushman & Wakefield, JLL, Prudential Real Estate Investors; As of December 2015.

7. More Markets Reach Peak Rents

With robust demand and low supply additions, rents in many markets are above previous peaks. Historically, when rents reach high absolute levels, tenants look to relocate to lower rent areas. One market where this is evident is the Bay Area of CA. Class A office rents in San Francisco are more than $75 per sq. ft. gross with some newer buildings over $100 per sq. ft. Many tenants have left the San Francisco office market for cheaper locales like Oakland, CA and East Bay cities like Walnut Creek, Concord and San Ramon.

EXHIBIT 10: CBD OFFICE MARKETS WITH PRIME RENTS ABOVE PRE-CRISIS LEVELS



Sources: CBRE, Cushman & Wakefield, JLL, Prudential Real Estate Investors; As of December 2015.

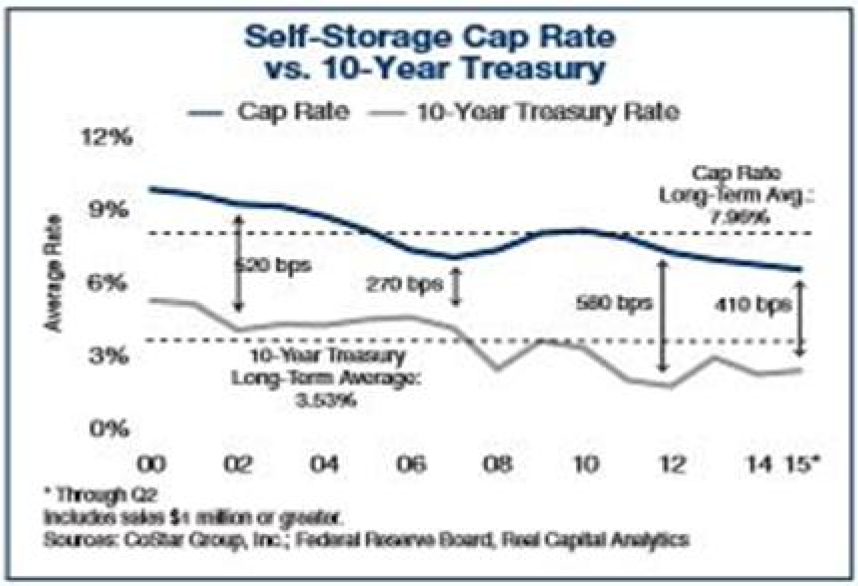
Booming Self Storage Industry

One of the niche sectors of the CRE business is the self-storage industry. The self-storage sector is in a mini-boom with high growth, increasing rents and lofty values. The industry is booming for a number of factors as listed below:

- Improvements in the economy and job market correlate with higher demand for storage units.
- The increased demand for apartments, especially in urban areas where space is limited, leads to higher demand for storage space.

- 10,000 baby boomers are turning 65 every day and many downsize their living situation, which creates demand for storage facilities.
- Although the development of new storage facilities has increased, it is not enough to satisfy increase demand.

Nationwide, the average price of self-storage facilities has risen 8% to $76 per sq. ft. and asking rents average $1.60 per sq. ft., an increase of 5.8% in 2015. Occupancies have risen above 94% in many markets and cap rates, which typically are in the 7.5% to 10% range, have been compressed to an average of 6.5% as shown in the chart below from Marcus & Millichap.



New Lease Accounting Rules Will Create Havoc for CRE

The International Accounting Standards Board (IASB), an independent organization that sets international accounting standards and the Financial Accounting Standards Board (FASB), the U.S. organization that sets U.S. accounting standards, have finally issued on January 13, 2016, new accounting standards for the treatment of leases. This new lease standard must be used by public companies on or before 1/1/19 and will create havoc for the CRE industry.

Prior to this new standard, leases were segregated into two types; operating leases and capital leases. Most CRE space leases are operating leases and some equipment leases are capital leases. An operating lease is a typical 3, 5 or 10 lease for office, retail or industrial space. A capital lease is a lease that meets any of the following requirements:

- *Ownership*-The ownership of the asset is shifted from the lessor to the lessee by the end of the lease period.
- *Bargain purchase option*-The lessee can buy the asset from the lessor at the end of

the lease term for a below-market price.

- *Lease term*-The period of the lease encompasses at least 75% of the useful life of the asset (and the lease is noncancellable during that time).
- *Present value*-The present value of the minimum lease payments required under the lease is at least 90% of the fair value of the asset at the inception of the lease.

These lease classifications into operating and capital leases have worked very well and have been easy to understand and implement. Companies that lease real estate space as an operating lease are only required to record rent expense on their financial statements and disclose in the notes to the financial statements the future minimum lease payments required under the lease.

The above rules have worked well since they were issued by the FASB 13 in 1976. The new IASB/FASB lease accounting standard will require the following draconian accounting changes for leases of more than one year in length:

- Eliminates the classification from FASB 13 of leases into operating and capital leases.

- All leases with terms over one year will be capitalized on a company's balance sheet as a leased asset and leased liability. The leased asset will be the present value of the lease payments at the lessee's incremental borrowing rate, the lease liability will be the total payments due under the lease and the difference will be charged to interest expense over the term of the lease.

- Leased assets will be depreciated on a straight line basis over the lease term.

This new standard will be very bad for the CRE industry and companies that have large lease portfolios in the retail, restaurant, bank, gas station and corporate industries, will be especially hard hit. The IASB/FASB estimates that public companies have $3.3 trillion in lease commitments on their books and this new lease standard will force these companies to place this amount on the balance sheet, which will increase liabilities and negatively affect leverage ratios and bank loan agreement covenants.

The sale-leaseback industry will be especially hard hit as the typical seller lessee like retail and restaurant companies will be reluctant to sign long term lease and load their balance sheets with significant lease liabilities. Many CRE and business organizations have been fighting these new lease rules including the Chamber of Commerce, International Council of Shopping Centers, Retail Federation and others and maybe with a new administration in Washington in 2016, they can be tabled for good.

CRE Financing Rates

The Fed quarter point rate hike of last month, the first in nearly a decade, shows resilience of the American economy. In fact, domestic investment rates have been near-zero since 2008. The insatiable demand by foreign investors and institutional players for domestic real estate properties will continue unabated this year as safe-haven of funds is of tantamount importance. Real estate is a clear winner in this environment, despite higher mortgage rates as follows:

- 10-yr UST @ 2.21% + 150 to 250 bps = 3.71% to 4.71%
- 5-yr UST @ 1.7% + 170 to 275 bps = 3.4% to 4.45%
- 10-yr Swap @ 2.14% + 220 to 300 bps = 4.34 % to 5.14% (while swap rates are inverted, conduit lenders widen pricing to maintain yields)
- Rising benchmark rates are tempered by high-quality mortgage debt demand as bond investors find few alternative yield plays
- Balance-sheet lenders, in particular, have a nearly unstoppable hunger for more mortgage investments keeping down pricingg for high quality loans.

The above financing rates and data are courtesy of John Oharenko, Senior Vice President, Berkadia Commercial Mortgage, LLC, john.oharenko@berkadia.com, 312-845-8565 and feel free to contact John for your real estate financing needs.

ECONOMIC/INVESTMENT FOCUS

16 Rules of Investment from one of the World's Greatest Investors, John Templeton

John Marks Templeton, the pioneer global investor who founded the Templeton Mutual Funds and for the past three decades devoted his fortune to his Foundation's work on the "Big Questions" of science, religion, and human purpose, passed away on July 8, 2008, at Doctors Hospital in Nassau, Bahamas, of pneumonia. As a pioneer in both financial investments and philanthropy, John Templeton spent a lifetime encouraging open-mindedness. If he hadn't sought new paths, he once said, "he would have been unable to attain so many goals." The motto that Templeton created for his Foundation, "How little we know, how eager to learn," exemplified his philosophy in the financial markets and his groundbreaking methods of philanthropy. Below are John Templeton's 16 rules for investment success.

1. INVEST FOR MAXIMUM TOTAL REAL RETURN

This means the return on invested dollars after taxes and after inflation. This is the only rational objective for most long-term investors. Any investment strategy that fails to recognize the insidious effect of taxes and inflation fails to recognize the true nature of the investment environment and thus is severely handicapped. It is vital that you protect purchasing power. One of the biggest mistakes people make is putting too much money into fixed-income securities. Today's dollar buys only what 35 cents bought in the mid-1970s, what 21 cents bought in 1960, and what 15 cents bought after World War II. U.S. consumer prices have risen every one of the last 38 years. If inflation averages 4%, it will reduce the buying power of a $100,000 portfolio to $68,000 in just 10 years. In other words, to maintain the same buying power, that portfolio would have to grow to $147,000— a 47% gain simply to remain even over a decade. And this doesn't even count taxes.

2. INVEST—DON'T TRADE OR SPECULATE

The stock market is not a casino, but if you move in and out of stocks every time they move a point or two, or if you continually sell short… or deal only in options…or trade in futures…the market will be your casino. And, like most gamblers, you may lose eventually—or frequently. You may find your profits consumed by commissions. You may find a market you expected to turn down turning up—and up, and up—in defiance of all your careful calculations and short sales. Every time a Wall Street news announcer says, "This just in," your heart will stop. Keep in mind the wise words of Lucien Hooper, a Wall Street legend: "What always impresses me," he wrote, "is how much better the relaxed, long-term owners of stock do with their portfolios than the traders do with their switching of inventory. The relaxed investor is usually better informed and more understanding of essential values; he is more patient and less emotional; he pays smaller capital gains taxes; he does not incur unnecessary brokerage commissions; and he avoids behaving like Cassius by 'thinking too much.'

3. REMAIN FLEXIBLE AND OPEN-MINDED ABOUT TYPES OF INVESTMENT

There are times to buy blue chip stocks, cyclical stocks, corporate bonds, U.S. Treasury instruments, and so on. And there are times to sit on cash, because sometimes cash enables you to take advantage of investment opportunities. The fact is there is no one kind of investment that is always best. If a particular industry or type of security becomes popular with investors, that popularity will always prove temporary and—when lost—may not return for many years.

Having said that, I should note that, for most of the time, most of our clients' money has been in common stocks. A look at history will show why. From January of 1946 through June of 1991, the Dow Jones Industrial Average rose by 11.4% average annually—including reinvestment of dividends but not counting taxes—compared with an average annual inflation rate of 4.4%. Had the Dow merely kept pace with inflation, it would be around 1,400 right now instead of over 3,000, a figure that seemed extreme to some 10 years ago, when I calculated that it was a very realistic possibility on the horizon.

Look also at the Standard and Poor's (S&P) Index of 500 stocks. From the start of the 1950s through the end of the 1980s—four decades altogether—the S&P 500 rose at an average rate of 12.5%, compared with 4.3% for inflation, 4.8% for U.S. Treasury bonds, 5.2% for Treasury bills, and 5.4% for high-grade corporate bonds.

In fact, the S&P 500 outperformed inflation, Treasury bills, and corporate bonds in every decade except the ’70s, and it outperformed Treasury bonds—supposedly the safest of all investments—in all four decades. I repeat: There is no real safety without preserving purchasing power.

4. BUY LOW

Of course, you say, that’s obvious. Well, it may be, but that isn’t the way the market works. When prices are high, a lot of investors are buying a lot of stocks. Prices are low when demand is low. Investors have pulled back, people are discouraged and pessimistic.

When almost everyone is pessimistic at the same time, the entire market collapses. More often, just stocks in particular fields fall. Industries such as auto making and casualty insurance go through regular cycles. Sometimes stocks of companies like the thrift institutions or money-center banks fall out of favor all at once.

Whatever the reason, investors are on the sidelines, sitting on their wallets. Yes, they tell you: “Buy low, sell high.” But all too many of them bought high and sold low. Then you ask: “When will you buy the stock?” The usual answer: “Why, after analysts agree on a favorable outlook.” This is foolish, but it is human nature. It is extremely difficult to go against the crowd—to buy when everyone else is selling or has sold, to buy when things look darkest, to buy when so many experts are telling you that stocks in general, or in this particular industry, or even in this particular company, are risky right now.
But, if you buy the same securities everyone else is buying, you will have the same results as everyone else. By definition, you can’t outperform the market if you buy the market. And chances are if you buy what everyone is buying you will do so only after it is already overpriced. Heed the words of the great pioneer of stock analysis Benjamin Graham: “Buy when most people…including experts…are pessimistic, and sell when they are actively optimistic.” Bernard Baruch, advisor to presidents, was even more succinct: “Never follow the crowd.” So simple in concept. So difficult in execution.

5. WHEN BUYING STOCKS, SEARCH FOR BARGAINS AMONG QUALITY STOCKS

Quality is a company strongly entrenched as the sales leader in a growing market. Quality is a company that’s the technological leader in a field that depends on technical innovation. Quality is a strong management team with a proven track record. Quality is a well-capitalized company that is among the first into a new market. Quality is a well-known trusted brand for a high-profit-margin consumer product.
Naturally, you cannot consider these attributes of quality in isolation. A company may be the low-cost producer, for example, but it is not a quality stock if its product line is falling out of favor with customers. Likewise, being the technological leader in a technological field means little without adequate capitalization for expansion and marketing.

Determining quality in a stock is like reviewing a restaurant. You don’t expect it to be 100%

perfect, but before it gets three or four stars you want it to be superior.

6. BUY VALUE, NOT MARKET TRENDS OR THE ECONOMIC OUTLOOK

A wise investor knows that the stock market is really a market of stocks. While individual stocks may be pulled along momentarily by a strong bull market, ultimately it is the individual stocks that determine the market, not vice versa. All too many investors focus on the market trend or economic outlook. But individual stocks can rise in a bear market and fall in a bull market. The stock market and the economy do not always march in lock step. Bear markets do not always coincide with recessions, and an overall decline in corporate earnings does not always cause a simultaneous decline in stock prices. So buy individual stocks, not the market trend or economic outlook.

7. DIVERSIFY. IN STOCKS AND BONDS, AS IN MUCH ELSE, THERE IS SAFETY IN NUMBERS

No matter how careful you are, you can neither predict nor control the future. A hurricane or earthquake, a strike at a supplier, an unexpected technological advance by a competitor, or a government-ordered product recall—any one of these can cost company millions of dollars. Then, too, what looked like such a well-managed company may turn out to have serious internal problems that weren’t apparent when you bought the stock. So you diversify—by industry, by risk, and by country. For example, if you search worldwide, you will find more bargains— and possibly better bargains—than in any single nation.

8. DO YOUR HOMEWORK OR HIRE WISE EXPERTS TO HELP YOU

People will tell you: Investigate before you invest. Listen to them. Study companies to learn what makes them successful. Remember, in most instances, you are buying either earnings or assets. In free-enterprise nations, earnings and assets together are major influences on the price of most stocks. The earnings on stock market indexes—the fabled Dow Jones Industrials, for example—fluctuate around the replacement book value of the shares of the index. (That’s the money it would take to replace the assets of the companies making up the index at today’s costs.)

If you expect a company to grow and prosper, you are buying future earnings. You expect that earnings will go up, and because most stocks are valued on future earnings, you can expect the stock price may rise also. If you expect a company to be acquired or dissolved at a premium over its market price, you may be buying assets. Years ago Forbes regularly published lists of these so-called “loaded laggards.” But remember, there are far fewer of these companies today. Raiders have swept through the marketplace over the past 10 to 15 years: Be very suspicious of what they left behind.

9. AGGRESSIVELY MONITOR YOUR INVESTMENTS

Expect and react to change. No bull market is permanent. No bear market is permanent. And there are no stocks that you can buy and forget. The pace of change is too great. Being relaxed, as Hooper advised, doesn’t mean being complacent. Consider, for example, just the 30 issues that comprise the Dow Jones Industrials. From 1978 through 1990, one of every three issues changed—because the company was in decline, or was acquired, or went private, or went bankrupt. Look at the 100 largest industrials on Fortune magazine's list. In just seven years, 1983 through 1990, 30 dropped off the list. They merged with another giant company, or became too small for the top 100, or were acquired by a foreign company, or went private, or went out of business. Remember, no investment is forever.

10. DON'T PANIC

Sometimes you won't have sold when everyone else is buying, and you'll be caught in a market crash such as we had in 1987. There you are, facing a 15% loss in a single day. Maybe more. Don't rush to sell the next day. The time to sell is before the crash, not after. Instead, study your portfolio. If you didn't own these stocks now, would you buy them after the market crash? Chances are you would. So the only reason to sell them now is to buy other, more attractive stocks. If you can't find more attractive stocks, hold on to what you have.

11. LEARN FROM YOUR MISTAKES

The only way to avoid mistakes is not to invest—which is the biggest mistake of all. So forgive yourself for your errors. Don't become discouraged, and certainly don't try to recoup your losses by taking bigger risks. Instead, turn each mistake into a learning experience. Determine exactly what went wrong and how you can avoid the same mistake in the future. The investor who says, "This time is different," when in fact it's virtually a repeat of an earlier situation, has uttered among the four costliest words in the annals of investing. The big difference between those who are successful and those who are not is that successful people learn from their mistakes and the mistakes of others.

12. BEGIN WITH A PRAYER

If you begin with a prayer, you can think more clearly and make fewer mistakes.

13. OUTPERFORMING THE MARKET IS A DIFFICULT TASK

The challenge is not simply making better investment decisions than the average investor. The real challenge is making investment decisions that are better than those of the professionals who manage the big institutions. Remember, the unmanaged market indexes such as the S&P 500 don't pay commissions to buy and sell stock. They don't pay salaries to securities analysts or portfolio managers. And, unlike the unmanaged indexes, investment companies are never 100% invested, because they need to have cash on hand to redeem shares. So any investment company that consistently outperforms the market is actually doing a much better job than you might think. And if it not only consistently outperforms the market, but does so by a significant degree, it is doing a superb job.

14. AN INVESTOR WHO HAS ALL THE ANSWERS DOESN'T EVEN UNDERSTAND ALL THE QUESTIONS

A cocksure approach to investing will lead, probably sooner than later, to disappointment if not outright disaster. Even if we can identify an unchanging handful of investing principles, we cannot apply these rules to an unchanging universe of investments—or an unchanging economic and political environment. Everything is in a constant state of change, and the wise investor recognizes that success is a process of continually seeking answers to new questions.

15. THERE'S NO FREE LUNCH

This principle covers an endless list of admonitions. Never invest on sentiment. The company that gave you your first job, or built the first car you ever owned, or sponsored a favorite television show of long ago may be a fine company. But that doesn't mean its stock is a fine investment. Even if the corporation is truly excellent, prices of its shares may be too high. Never invest in an initial public offering (IPO) to "save" the commission. That commission is built into the price of the stock—a reason why most new stocks decline in value after the offering. This does not mean you should never buy an IPO.

Never invest solely on a tip. Why, that's obvious, you might say. It is. But you would be surprised how many investors, people who are well-educated and successful, do exactly this. Unfortunately, there is something psychologically compelling about a tip. Its very nature suggests inside information, a way to turn a fast profit.

16. DO NOT BE FEARFUL OR NEGATIVE TOO OFTEN

And now the last principle. Do not be fearful or negative too often. For 100 years' optimists have carried the day in U.S. stocks. Even in the dark '70s, many professional money managers—and many individual investors too—made money in stocks, especially those of smaller companies. There will, of course, be corrections, perhaps even crashes. But, over time, our studies indicate stocks do go up…and up… and up.

With the fall of communism and the sharply reduced threat of nuclear war, it appears that the U.S. and some form of an economically united Europe may be about to enter the most glorious period in their history. As national economies become more integrated and interdependent, as communication becomes easier and cheaper, business is likely to boom. Trade and travel will grow. Wealth will increase. And stock prices should rise accordingly.

By the time the 21st century begins—it's just around the corner, you know—I think there is at least an even chance that the Dow Jones Industrials may have reached 6,000, perhaps more. Chances are that certain other indexes will have grown even more. Despite all the current gloom about the economy, and about the future, more people will have more money than ever before in history. And much of it will be invested in stocks.
And throughout this wonderful time, the basic rules of building wealth by investing in stocks will hold true. In this century or the next it's still "Buy low, sell high."

Lincoln's Greatness

Abraham Lincoln is considered one of our greatest Presidents, however, his path to success was littered with failures. A common list of the failures of Abraham Lincoln (along with a few successes) is shown below:

- 1831 - Lost his job
- 1832 - Defeated in run for Illinois State Legislature
- 1833 - Failed in business
- 1834 - Elected to Illinois State Legislature (**success**)
- 1835 - Sweetheart died
- 1836 - Had nervous breakdown
- 1838 - Defeated in run for Illinois House Speaker
- 1843 - Defeated in run for nomination for U.S. Congress
- 1846 - Elected to Congress **(success)**
- 1848 - Lost re-nomination
- 1849 - Rejected for land officer position
- 1854 - Defeated in run for U.S. Senate
- 1856 - Defeated in run for nomination for Vice President
- 1858 - Again defeated in run for U.S. Senate
- 1860 - Elected President **(success)**

That looks like a pretty glum résumé, making you wonder how he ever made it to the top. But when you really think of it, to run for office or high positions so many times, you have

to have something on the ball and have more successes than meet the eye. Lincoln's rocky road to greatness illustrates that one should never give up and if you fail at something, get up, dust yourself off and try again.

REIT FOCUS

REIT Statistics

Current REIT statistics through November 2015 per NAREIT are included in the table below:

Period	***All REITs***	***All Equity REITs***	***S&P 500***	***Dow Jones Industrial Average***	***NASDAQ Composite***
2015 YTD (11/15)	1.08%	1.50%	3.01%	.006%	9.05%
1-Year	2.19%	2.77%	2.75%	.22%	7.86%
5-Year	12.34%	12.64%	14.4%	12.41%	16/76%
10-Year	6.73%	7.22%	7.48%	7.64%	9.73%
20-Year	10.55%	11.1%	8.38%	8.81%	8.18%
FTSE NAREIT Market Capitalization	$935B	$875B	NA	NA	NA
Dividend Yield	4.23%	3.77%	2.14%	NA	NA

REIT Review

Summary

This month's REIT Review is on Franklin Street Properties Corporation ("FSP"), a publicly traded REIT that owns and operates a portfolio of institutional quality office properties in major U.S. markets.

Property Information

As of Q3 2015, FSP owned and operated 36 office properties containing 9.6 million rentable sq. ft. FSP also manages nine sponsored REITs and held five promissory notes secured by real estate mortgages. FSP's office properties are primarily located in the five core markets of Atlanta, Dallas, Denver, Houston and Minneapolis. Portfolio occupancy was 88% and average rent per sq. ft. was $26.81 for Q3 2015. The yoy NOI decreased 6.7% for Q3 2015.

Major Events

FSP sold an office property located in Plano, Texas on February 23, 2015 at a $1.5 million gain, an office property located in Eden Prairie, Minnesota on March 31, 2015 at a $9.0 million gain and an office property located in Charlotte, North Carolina on May 13, 2015 at a $0.9 million gain.

Corporate Data

FSP went public in 2005, is incorporated in Maryland and is located in Wakefield, MA. FSP's debt is rated Baa3 by Moody's.

Management

George J. Carter, 67, President and CEO

Mr. Carter has been a director since 2002 and is responsible for all aspects of the business of FSP, with special emphasis on the evaluation, acquisition and structuring of real estate investments. Prior to the conversion of Franklin Street Partners Limited Partnership into FSP in 2002, Mr. Carter was President of the general partner of the Partnership and was responsible for all aspects of the business of the Partnership and its affiliates. From 1992 through 1996 he was President of Boston Financial Securities, Inc. Prior to joining Boston Financial, Mr. Carter was owner and developer of Gloucester Dry Dock, a commercial shipyard in Gloucester, Massachusetts. From 1979 to 1988, Mr. Carter served as Managing Director in charge of marketing at First Winthrop Corporation, a national real estate and investment banking firm headquartered in Boston, Massachusetts. Prior to that, Mr. Carter held a number of positions in the brokerage industry, including positions with Merrill Lynch & Co. and Loeb Rhodes & Co. Mr. Carter is a graduate of the University of Miami (B.S.).

Mr. Carter's son, Scott H. Carter, serves as Executive Vice President, General Counsel and Assistant Secretary of FSP and Mr. Carter's other son, Jeffrey B. Carter, serves as Executive Vice President and Chief Investment Officer of FSP.

Jeffery B. Carter, 44, EVP and CIO

Mr. Carter was appointed to this position in February 2012. Previously, Mr. Carter served as Senior Vice President and Director of Acquisitions of FSP from 2005 to 2012 and as Vice President – Acquisitions from 2003 to 2005. Mr. Carter is primarily responsible for developing and implementing FSP's investment strategy, including coordination of acquisitions and dispositions. Prior to joining FSP, Mr. Carter worked in Trust Administration for Northern Trust Bank in Miami, Florida. Mr. Carter is a graduate of Arizona State University (B.A.) and The George Washington University (M.A.).

John G. Demeritt, 55, EVP and CFO

Mr. Demeritt has been Chief Financial Officer since March 2005. Mr. Demeritt previously served as Senior Vice President, Finance and Principal Accounting Officer since September 2004. Prior to September 2004, Mr. Demeritt was a Manager with Caturano & Company, an independent accounting firm, where he focused on Sarbanes Oxley compliance. Previously, from March 2002 to March 2004 Mr. Demeritt provided consulting services to public and private companies. During 2001 and 2002, Mr. Demeritt was Vice President of Financial Planning & Analysis at Cabot Industrial Trust, a publicly traded real estate investment trust, which was acquired by CalWest in December 2001. From October 1995 to December 2000, Mr. Demeritt was Controller and Officer of The Meditrust Companies, a publicly traded real estate investment trust (formerly known as the La Quinta Companies, which was then acquired by the Blackstone Group), where Mr. Demeritt was involved with a number of merger and financing transactions. From 1986 to 1995, Mr. Demeritt had financial and accounting responsibilities at three other public companies, and was previously associated with Laventhol & Horwath, an independent accounting firm from 1983 to 1986. Mr. Demeritt is a Certified Public Accountant and holds a Bachelor of Science degree from Babson College.

Top Institutional Holders:	Shares	%
Vanguard Specialized REIT Index	6,460,424	6.45
Blackrock Fund Advisors	5,201,185	5.19
Fuller and Thaler Asset Management, Inc.	4,253,758	4.25
Undiscovered Managers Behavioral Value Fund	3,877,232	3.87
Forward Management LLC	3,849,400	3.84

Ownership

Financial Analysis and Valuation

Select financial data for FSP as of the Q3 2015 10Q and supplemental information

(in millions where applicapable)

Financial Data	
Real Estate Assets, Gross	$1,899
Total Assets	$1,926
Property Debt (weighted average interest rate of approximately 2.4 %)	$920
Common Stockholders' Equity	$934
Revenue	$182
Net Income	$19
Net Income Per Share	$.20
Cash Flow from Operations	$72
Unsecured/Secured Credit Facility ($500 million with $300 million used)	$200
Market Capitalization	$986
Property Debt to:	
Gross Real Estate Assets	48%
Market Capitalization	93%
Enterprise Value	48%
Dividend and Yield ($.76/sh.)	7.7%

Valuation Methodology	
Q3 2015 Revenue Annualized	$248
Less: Q3 2015 Operating Expenses Annualized (excluding depreciation, amortization, interest expense and less G&A expenses)	116
Annualized Net Operating Income 2015	132
Projected Inflation Rate at 3.5%	x1.035
Projected Forward NOI for Next Year	$137
Projected Average Cap Rate	7.5%
Projected Value of Real Estate Assets	1,827
Add: Net Operating Working Capital (at book value)	150
Investment in Non-Consolidated REITs (at book value)	77
Related Party Mortgage Loan Receivables (at book value)	93
Total Projected Asset Value of Company	2,147
Total Debt Per Above	(920)
Projected Net Asset Value of the Company	$1,227
Common Shares Outstanding-100M Shares	
Projected NAV Per Share	**$12**
Market Price Per Share on 1/15/16	**$9**
Premium (Discount) to NAV	**(25%)**

Financial Metrics

The gross real estate assets, property debt, revenues, net income, funds from operations, return on invested capital and dividends per share for the years 2010 through Q3 2015 are shown in the table below:

(millions except per share amounts)	2010	2011	2012	2013	2014	Q3 2015
Gross Real Estate Assets	$1,074	$1,245	$1,396	$1,870	$1,868	$1,899
Property Debt	$283	$449	$616	$926	$888	$920
Revenues	$117	$139	$161	$213	$249	$182
Net Income	$22	$43	$7	$19	$13	$19
Funds from Operations (FFO)	$66 $66	$71	$80	$100	$112	$79
Return on Invested Capital (1)	4.3%	4.4%	4.7%	4.7%	5.5%	NA
Dividends Paid Per Share	$.76	$.76	$.76	$.76	$.76	$.57(2)

(1) This is the ratio of cash provided by operations divided by stockholder's equity plus property debt, less cash and measures the return the REIT is earning on its invested capital.

(2) Dividend is currently $.19 per quarter.

The total return of FSP year to date and through five years is show in the chart below per NAREIT:

	FSP Total Return	YTD (11/15)	1-Yr	3-yr	5-Yr
		-9.21%	-7.32%	2.74%	2.13%

As shown above, our net asset value per share for FSP is $12/sh., compared to a market price of $9/sh. Current average cap rates for office properties per our industry

experience and CBRE's Cap Rate Survey are in the 5% to 8% range, depending on the location, occupancy, quality and age of the property. We have used an average cap rate of 7.5% due to FSP's portfolio being primarily well-located Class A/B suburban office properties.

Valuation Analysis

FSP's strengths, concerns and recommendation are as follows:

Strengths:

- Solid portfolio of Class B office assets.

- Investment grade credit rating.
- Attractive stock price at $9/sh. and 9X FFO.
- Attractive dividend yield of 7.7%.

Concerns:

- Dividend at $.76/sh. has been the same since 2009 and cash flow from operations for Q3-15 was $72M versus $57M in dividend payments to shareholders, which provides excess cash flow for a dividend increase.
- Management's strategy of repositioning the portfolio by selling high cap rate and high occupancy suburban assets and reinvesting the proceeds into low cap rate and low occupancy value-added urban assets.
- Minimal growth in revenue and FFO since 2012.

Recommendations:

FSP is a small capitalization REIT with a Class B portfolio of office properties and our recommendations are as follows:

- FSP needs to increase the stock dividend as it has been the same since 2009.
- FSP is too small to be a public company and should be taken private or sold with its large discount to NAV.
- We like the reasonable valuation of FSP, however, are skeptical of their repositioning program as they are reinvesting into high priced urban office assets at the peak of the market and at compressed cap rates, while the trend of urban office occupancy is beginning to reverse, as rent increases have hit ceiling levels in many markets. Therefore, we are not recommending the purchase of the stock, even though the valuation and dividend are attractive.
- When a REIT changes its investment strategy, that is a signal that the exiting strategy is flawed or the implementation was poor. There is nothing wrong with owning suburban office buildings, if they are purchased at proper risk adjusted cap rates, the acquisitions are underwritten properly and they are in the best locations. Many suburban office buildings are 75% to 90% leased and will never get to a 95% stabilized lease level due to slower suburban job growth. However, many investors believe they can increase the occupancy to the 95% level and underwrite the acquisition as such and overpay for the asset.

A five-year price chart of FSP is shown below:

REIT FOCUS REVIEWS IN PRIOR ISSUES OF VOM ARE AS FOLLOWS:

1. Kilroy Realty Corporation, December 15, 2013

2. Cedar Realty Trust, Inc., January 15, 2014

3. Brandywine Realty Trust, February 15, 2014

4. Associated Estates Realty Corporation, March 15, 2014

5. Weingarten Realty Investors, April 15, 2014

6. EastGroup Properties, Inc., May 15, 2014

7. Spirit Realty Capital, Inc., June 15, 2014

8. Parkway Properties, Inc., Jul 15, 2014

9. Equity Residential, August 15, 2014

10. Boston Properties, Inc., September 15, 2014

11. The Macerich Company, October 15, 2014

12. Essex Property Trust, Inc., November 15, 2014

13. First Industrial Realty Trust, Inc., December 15, 2014

14. Avalon Bay Communities, Inc., January 15, 2015

15. Corporate Office Properties Trust, February 15, 2015

16. Post Properties, Inc., March 15, 2015

17. Liberty Property Trust, April 15, 2015

18. General Growth Properties, Inc., May 15, 2015

19. Cousins Properties, Inc., June 15, 2015

20. Saul Centers, Inc., July 15, 2015

21. Duke Realty Corporation, August 15, 2015

22. Apartment Investment and Management Co., September 15, 2015

23. Kimco Realty Corporation, October 15, 2015

24. Taubman Centers, Inc., November 15, 2015

25. Mid-America Apartment Communities, Inc., December 15, 2015

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