

View of the Market

Volume XVII/Issue

7/July 2025

Strategy and Insight for the Commercial Real Estate Industry

A Publication of Paramount Capital Corporation

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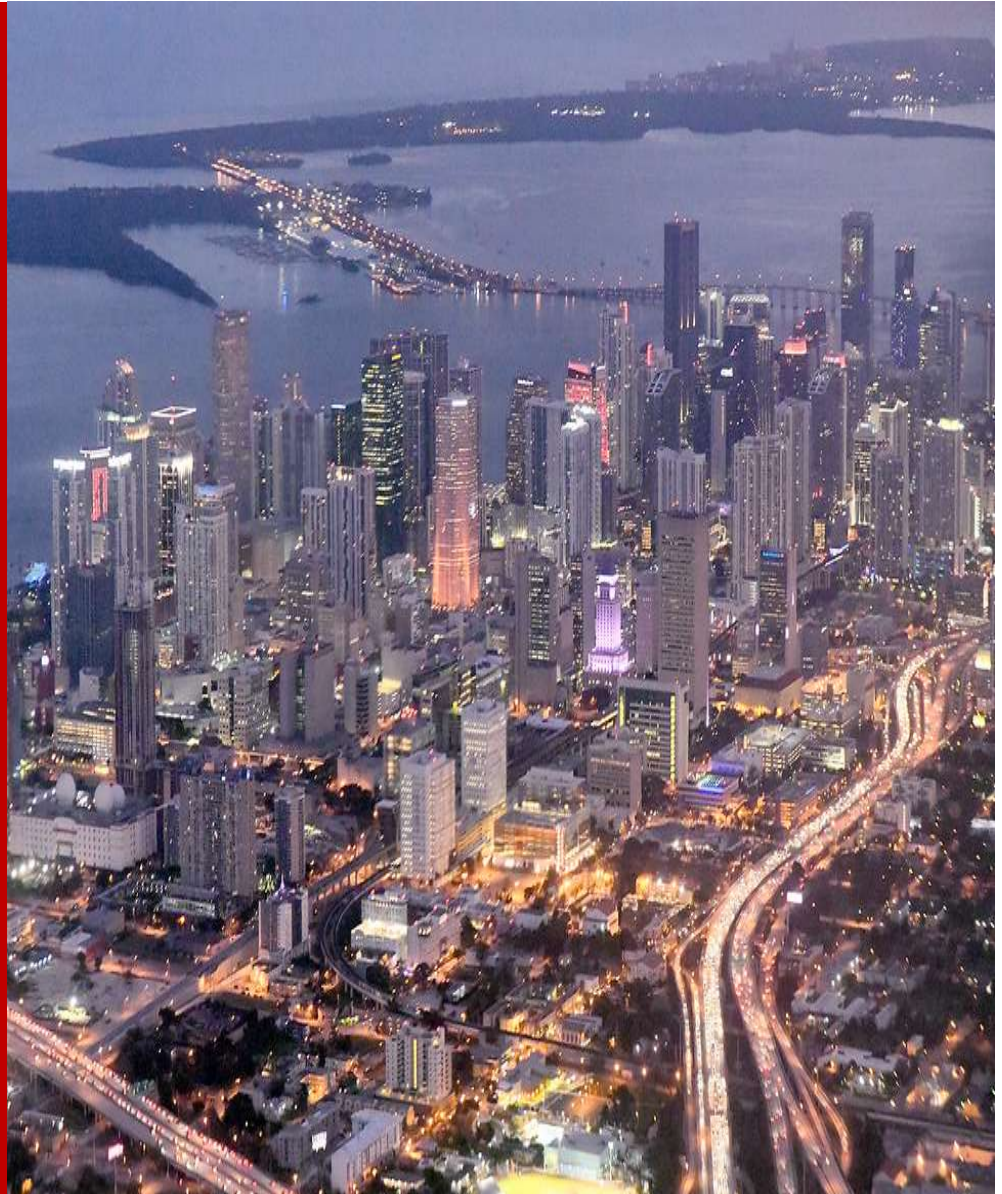
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REAL ESTATE FOCUS

Investing in B & C CRE Properties

CRE investment properties are typically categorized as either A, B or C properties. Class A properties are considered the best-in-class real estate, in the finest locations, fully leased with a high percentage of credit tenants, have higher quality finishes and amenities, require little if any repairs and improvements and are typically newer properties. Class B properties are well-located, with high occupancy, some credit tenants, and may need repairs and improvements, as well as lower-quality finishes and amenities. Class C properties are poorly located assets, with high vacancy, low quality finishes and amenities and typically need substantial repairs and improvements. Class A properties are also considered Core assets; Class B properties are considered Core Plus assets and Class C properties are considered Value-Added (need retenanting or capital improvements) or Opportunistic (need retenanting and substantial capital improvements) assets.

Most CRE investors, especially the large institutions like pension funds, insurance companies, endowments, and sovereign wealth funds, are only interested in investing in Class A assets. These institutions are very conservative and risk-averse and prefer to acquire safety and prestige with Class A assets. Class A assets look great on the cover of a deal sheet or in an investor presentation, but they are very expensive, and cap rates are typically below 5%-6%, depending on the location and asset type. It is also difficult to substantially increase the value of Class A assets through leasing and operations management, as they are already at their peak assessment.

If an investor wants to pay a high price for a low-risk asset, then Class A properties are fine. However, many investors prefer Class B & C assets that are available at much lower prices and higher cap rates, typically in the 6%-8%+ area. Class B & C assets that require repairs and improvements and are being released can be excellent candidates for turnaround and value creation, as discussed above. A Class B asset can become a Class B+ asset with improved

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management and the required improvements, and releasing. Class C assets can also become Class B assets with the same management needed, improvements, and releasing. As a property moves up the Class ladder, valuation increases, and cap rates decrease. This is one way to create value in CRE investment.

A Review of the MetLife 2025 U.S. Commercial Real Estate Chartbook

MetLife Investment Management is one of the largest commercial real estate lenders and investors with over \$102 billion in CRE assets. Their 2025 U.S. Commercial Real Estate Chartbook was issued in June 2025 and a summary of their findings and conclusions are as follows.

I. Key Takeaways:

- The CRE market was a year into its recovery when the Liberation Day broad-based tariffs landed; policy-driven volatility is likely to continue this summer and beyond.
- Valuations remain compelling: over the next twelve months, growth of 4.0% is expected in retail, 2.0% growth in apartments, 2.0% growth in industrial, and 0.5% growth in office. Value growth should accelerate throughout 2026 as the construction completion void accelerates.
- Construction costs have fueled the ten year plus housing affordability crisis; immigration restrictions, NIMBYism, and tariff pressure are likely to make this phenomenon spill into commercial real estate in 2026.
- Highest-conviction recommendations: net-lease retail, independent-living seniors housing, medical office and select residential segments.
- Caution: ground-up development (all sectors), value-add strategies (all sectors), student housing, full-service hotels, grocery-anchored retail.

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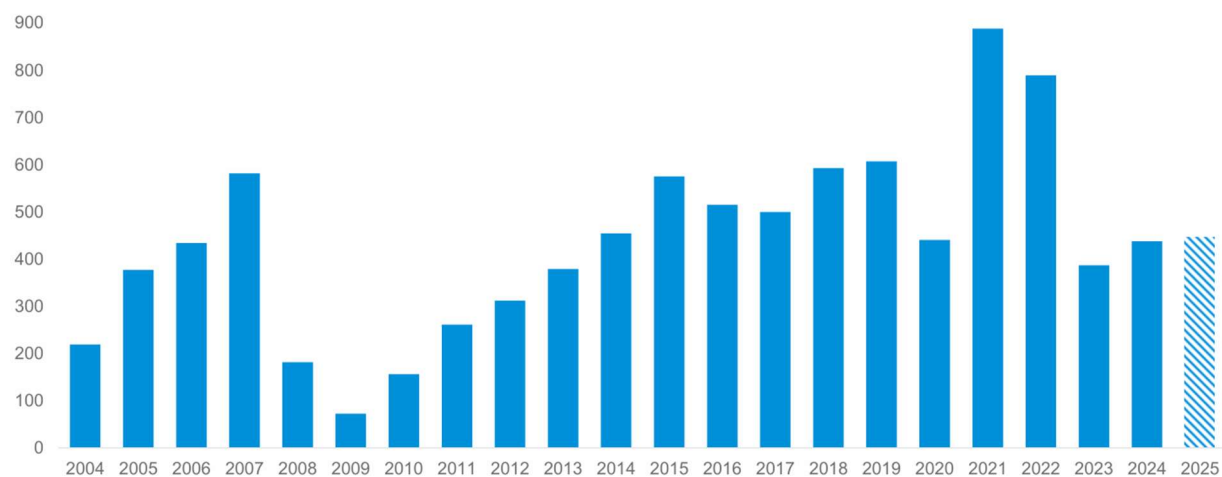
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II. Property Transaction Volume:

- As shown in the chart, transaction volume is down 50%-60% from the 2021 peak.

Policy Uncertainty Will Likely Keep Liquidity Depressed

US CRE Transaction Volume



Sources: MIM, RCA. Data as of 1Q 2025.

III. Policy Exposure by Property Type:

- All property types could benefit from rising construction costs and lower supply (less immigration, tariffs).
- Apartment: Immigration restrictions could dampen demand in markets like Miami, San Diego, Dallas, and Boston.
- Office: Waning CEO confidence could slow the nascent office sector recovery. Potential for rising capital expenditures for tenant improvements.
- Retail: Retail assets in lower-income markets or submarkets face risk due to their reliance on goods imported from Asia, particularly in categories like electronics and apparel.
- Industrial: Port markets could experience lower demand, but sunbelt markets could benefit from onshoring and lower construction activity.

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- **Hotels:** Consumer discretionary spending could slow, reducing domestic travel. A strong dollar and anti-U.S. sentiment could slow international travel to the U.S.
- **Alternative Sectors:** Sectors like data centers, self-storage, medical office, and residential alternatives have a lower exposure to changing federal government policies.

IV. Property Type Scoreboard

MetLife Investment Management Property Type Scorecard

Sector	Stochastic Rank	Capital Markets Rank	MIM Rank	YoY Change	Strategy	Benchmark Allocation	Recommended Allocation
Retail- Net Lease	3	1	1	1	Overweight	2%	3%
Seniors Housing (IL)	4	2	2	3	Overweight	3%	5%
Infill Warehouses	2	7	3	-2	Overweight	10%	13%
Medical Office	7	3	4	8	Overweight	2%	3%
Self Storage	8	5	5	10	Overweight	3%	4%
Manufactured Housing	5	11	6	-2	Neutral+	3%	4%
Data Centers	9	8	7	0	Neutral+	2%	3%
Cold Storage	1	17	8	-5	Neutral+	1%	2%
Retail- Mall	17	4	9	-3	Neutral	4%	4%
Retail- Strip/Neighborhood	15	6	10	1	Neutral	4%	4%
Moderate Income Housing	10	14	11	-3	Neutral	1%	1%
Limited-Service Hotels	6	18	12	-2	Neutral	1%	1%
Regional Warehouses	14	10	13	-4	Neutral	15%	15%
Single-Family Rentals	12	16	14	0	Neutral-	3%	3%
Traditional Apartment	16	13	15	3	Neutral-	21%	19%
Office (Excludes Life Science/Medical)	11	19	16	3	Neutral-	14%	12%
Life Science	18	12	17	0	Underweight	3%	2%
Retail- Grocery Anchored	21	9	18	2	Underweight	4%	2%
Full-Service Hotels	13	21	19	2	Underweight	1%	1%
55+ Housing	19	15	20	-7	Underweight	1%	1%
Student Housing	20	20	21	-5	Underweight	2%	1%

Source: MIM. Based on a June 2025 Delphi consensus survey of MIM's acquisitions staff for current market pricing, aggregated portfolio information, and ratings from vendors including CoStar and Green Street. External sources include REIT and Market information from MIM vendors including CBRE-EA, and Green Street.

Note: Pricing analysis is only focused on Core and Stabilized assets.

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Positive Leverage in CRE Deals is Coming Back

Positive leverage in CRE deals is coming back as the Federal Reserve finally begins lowering interest rates this summer and fall. Since the Fed began raising interest rates in March of 2022, the cost of debt has risen and become higher than cap rates, which creates negative leverage. Negative leverage also occurs when the cash-on-cash return or return on the investor's equity is less than the cap rate and this is a big “No-No” in CRE. This has been happening during the last few years with rising interest rates and firm cap rates. Today, the average cost of permanent debt is about 6.50%, while property cap rates average about 6.0%. Even though negative leverage is risky, many real estate investors, even some of the largest and most astute private equity firms in the business, had no other choice if they wanted to buy a CRE property. They figured that even though negative leverage is bad, rates will eventually come down and the property will be refinanced at a lower rate, which would create positive leverage in the future.

One of the most important axioms of a successful real estate investment and development program is to acquire or build real estate with positive leverage. Positive leverage occurs when the cap rate is greater than the cost of debt, which means the return on equity will be greater than the cap rate. Negative leverage is just the opposite and is defined as when the cap rate on a property acquisition is less than the cost of debt or debt constant and therefore, the cash-on-cash return is less than the cap rate. The debt constant is the annual debt service (principal and interest) payment divided by the amount of the debt.

Let's say an apartment property is purchased for \$50 million, with a net operating income of \$3 million or at a cap rate of 6.0%. If the property is financed with a permanent loan at 70% or \$35 million, with an interest rate of 6.50% interest only, the annual mortgage payment would be \$2.275 million. The annual debt constant is therefore 6.5% ($\$2.275\text{M}/\35M), the same as the interest rate since there is no loan amortization. Since the cap rate of 6.0% is less than the debt constant of 6.5%, the cash-on-cash return falls to only 4.83% (NOI of \$3.0M less the debt payment of \$2.275M, equals the cash flow to equity of \$725K, divided by the equity of \$15M, equals a return of only 4.83%) and this is negative leverage. One of the most important financial

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incentives to invest in CRE are to provide the investors with a high cash-on-cash return or commonly referred to as “levering the equity.” Leveraging the equity is the whole attraction of the CRE investment business. No other alternative investment program, like private equity, venture capital and hedge funds, provides this simple leveraging technique. The levered equity return structure is inherent in CRE investment and development. In the above example, if the interest rate on the debt falls to 5.0% and the cap rate also falls to 5.5%, as they were prior to March 2022, the investment would have positive leverage as the cap rate of 5.5% would be greater than the debt constant of 5.0% and the cash-on-cash return would rise to an attractive 6.67% and this is the yield the investors would receive in year one from positive leverage and substantially higher than the 4.83% in the negative leverage example.

Why do investors continue to buy CRE with negative leverage? I think there are three reasons. One is that they have the capital raised in a fund or private placement and are eager to spend it. Two, they believe that rent increases will be high enough in future years to create positive leverage and three, many investors were sure that the Fed would aggressively lower interest rates in the last half of 2025. However, what if the rent increases don't materialize and interest rates are not lowered and stay the same? It all depends on the Federal Reserve. If the Fed is desirous about reducing the federal funds rate from 4.25% to 3.0% or less, then the new CRE boom will begin. If not, the CRE industry will muddle along and be stuck with negative leverage.

Get Your Copy of Three Great CRE Books by Our Editor, Joseph Ori

The editor of this newsletter, Joseph Ori, is pleased to offer his three CRE books for sale, “The Fifty Commandments of Commercial Real Estate Investment,” Edition I and II and “Commercial Real Estate Investment for Pros (and Dummies Too!).” All books are available on Amazon and other book outlets on Kindle, and soft and hardcover from \$8.99 to \$24.99.

Both editions of The Fifty Commandments of Commercial Real Estate Investment compile the choice pieces of advice Mr. Ori has amassed for over 40 years in the CRE industry. Mr. Ori lists essential dos and don'ts, mistakes, and successful strategies with a mixture of critical analysis and

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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.

Commercial Real Estate Investment for Pros (and Dummies Too!) discusses the history, the various financial players, legal and financial structures, property types, modern portfolio theory and the financial metrics of commercial real estate investment and the commercial real estate industry. The book includes numerous charts and analyses of the industry and a step-by-step breakdown of the commercial real estate analysis and investment process. The book is perfect reading for the experienced real estate pro and also understandable to the real estate novice or someone new to the industry.

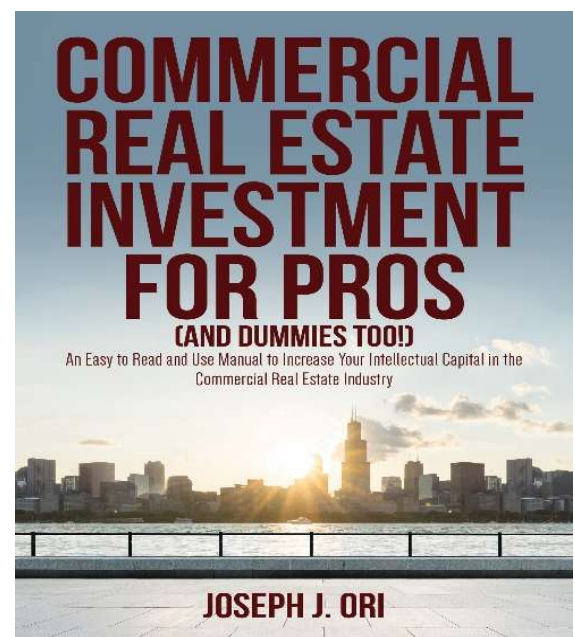
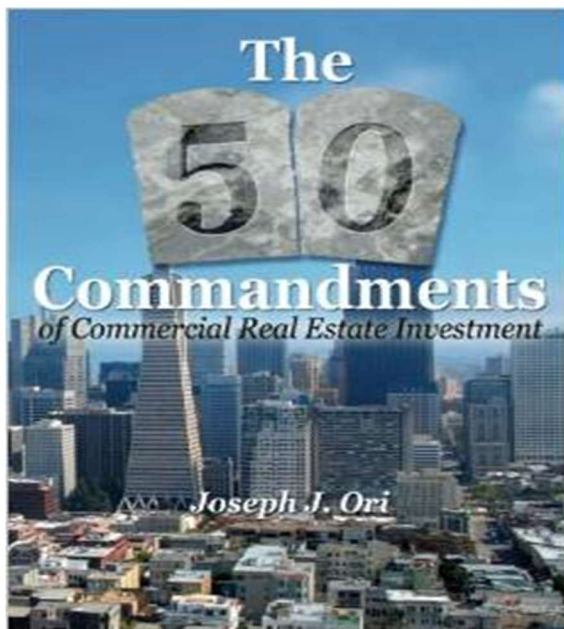
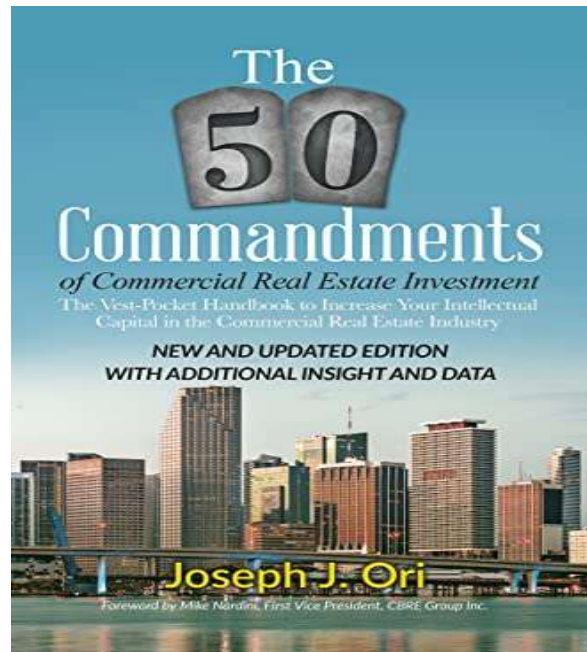
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CRE Financing Rates

Loan Type	Mortgage Rate	Maximum Amortization	Term (years)	Maximum LTV
Permanent Loans	5.63%-9.50%+	30	10	70%
Conduit-CMBS	5.88%-7.49%+	30	10	70%
Bridge Loans	6.50%-13.50%+	Interest Only	1-3	80%
Construction Loans	6.25%-9.50%+	Interest Only	1-4	70%
Insurance Co. Loans	5.38%-7.89%+	30	10	70%
Fannie Mae/Freddie Mac	5.46%-6.26%+	30	10	80%

Commercial Loan Index Rates	
Prime Rate	7.50%
30-Day SOFR (secured overnight funding rate)	4.35%
1 Year Swap	3.81%
10 Year Swap	3.67%
5 Year Treasury	3.86%
10 Year Treasury	4.28%
Federal Funds Rate	4.25%



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Interest rates fell this month, with the 10-year treasury rate at 4.28%. The Federal Reserve's Open Market Committee meets on July 28th and 29th, and we hope they come to their senses and lower the federal funds rate by at least .50%. The above financing rates and data are courtesy of Paramount Capital Corporation and feel free to contact Joseph Ori, Founder and CEO, Paramount Capital Corporation, jjo@paramountcapitalcorp.com, for your real estate capital needs.

CRE Deal Focus

CRE Deals of the Month

Purchaser/ Sponsor	Seller	Property/ Deal	Price	Description
Blackstone	Shorenstein Investment Advisors	Minority Stake in Two Office Towers, Bellevue, WA	\$545M	Minority interest in two six-story office buildings.
NorthPoint Development	High Street Logistics	Industrial Portfolio, Elgin, IL	\$270M	A 2.8 million-square- foot industrial portfolio with 11 properties.

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Plymouth Industrial REIT	NA	Industrial Portfolio, Ohio	\$193M	A 2 million-square-foot industrial portfolio with 21 buildings.
The Hamilton Co.	DiGiovanni Family	Hill Estates, Belmont, MA	\$175M	A 396-unit apartment complex.
NorthPoint Development	Blackston Link Logistics	Las Vegas Logistics Center, Las Vegas, NV	\$175M	A 1 million-square-foot industrial property.
Kennedy Wilson, Kenedix Inc. and Hulic Co., Ltd.	Vanbarton Group	The Danforth, Seattle, WA	\$173M	A 265-unit apartment complex.
Centerspace	Cottonwood Communities, Inc,	Sugarmont, Salt Lake City, UT	\$149M	A 241-unit apartment complex.

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MG Properties	Anton Development	Citron Apartments, Anaheim, CA	\$144M	A 314-unit apartment complex built in 2023.
Griffis Residential	Northwestern Mutual Life Insurance Co.	Anya Apartments, West Palm Beach, FL	\$87M	A 223-unit apartment complex built in 2021.
Pacific Urban Investors	Boston Investor Group	Meadow Creek Apartments, Portland, OR	\$76.7M	A 304-unit apartment complex built in 1985.

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CORPORATE FINANCE FOCUS

The Daily Drucker

One of the most popular corporate thinkers and management consultants in the last hundred years is Peter Drucker. He passed away in 2005 at 92 years old, but during his illustrious career, published over thirty-five books, and his corporate and management ideas have had a profound impact on shaping the modern corporation and management science. For the next twenty-four issues of VOM, we will highlight some of his insights and motivations in corporate management, personnel, and the knowledge worker from one of his last books, *The Daily Drucker*.

I. Harmonize the Immediate and Long-Range Future

A manager must, so to speak, keep his nose to the grindstone while lifting his eyes to the hills, quite an acrobatic feat. A manager has two specific tasks. The first is creation of a true whole that is larger than the sum of the parts, a productive entity that turns out more than the sum of the resources put into it. The second specific task of the manager is to harmonize in every decision and action the requirements of the immediate and of the long-range future. A manager cannot sacrifice either without endangering the enterprise.

II. Compensation Structure

Compensation must always try to balance recognition of the individual with stability and maintenance of the group. People have to be paid, but every compensation system is liable to misdirect. Compensation always expresses status, both within the enterprise and in society. It entails judgments on a person's worth as much as on performance. Develop a compensation system that rewards individual performance while balancing individual rewards with rewards that help maintain the continuity of the entire organization as a whole.

III. Decision Objectives

A decision process requires clear specification as to what the decision has to accomplish. What are the objectives the decision has to reach? In science these are known as "boundary

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conditions.” The more concisely and clearly boundary conditions are stated, the greater the likelihood that the decision will indeed be an effective one and will accomplish what it set out to do. Take a decision you are facing today. Clearly specify what purpose or need you want to fulfill by making the decision.

IV. Decision Making

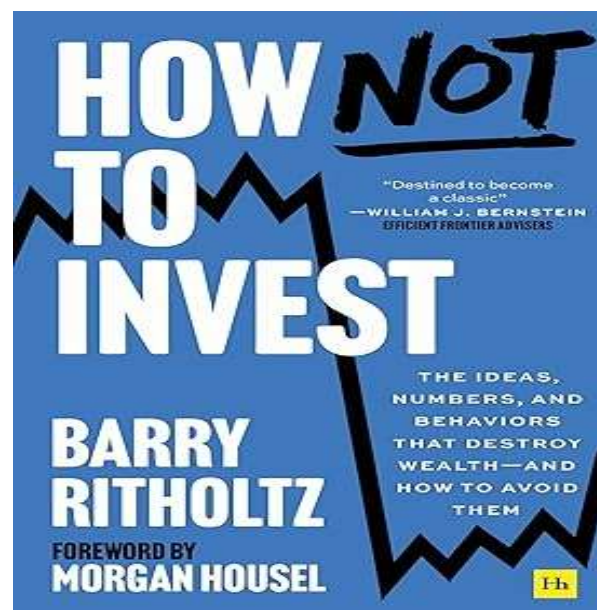
Start with what is right rather than what is acceptable. But if one does not know what is right, one cannot distinguish between the right compromise and the wrong compromise and will end up by making the wrong compromise. And don't you, above all, concern yourself with the compromises that might be needed to make your recommendations acceptable.

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Book Review: How Not to Invest

“How Not to Invest,” The ideas, numbers and behaviors that destroy wealth and how to avoid them, by Barry Ritholtz, Harriman House, 2025.



This is a great read, and if you're tired of reading the same old run-of-the-mill investment books that try to teach you how to beat the market, when less than 1.0% of investors can, then this is the book for you. The author, Barry Ritholtz, is the Co-Founder, Chairman and Chief Investment Officer of Ritholtz Wealth Management, a financial planning and asset management firm that manages over \$5 billion in assets. The book discusses the myriad of bad habits in the investment business, from bad ideas, numbers, behavior, and advice, in an easy-to-read, short chapter format. I recommend this book to anyone who wants to increase their intellectual capital in investments and finance and the return on their portfolio.

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REIT Statistics

Current REIT statistics for 5/31/25 per NAREIT are included in the table below. Please note that the all-equity REIT return over 20 years includes three CRE downturns: the Great Recession, the retail and store closure meltdown and the current higher interest rate regime.

<i>Period</i>	<i>All REITs</i>	<i>All Equity REITs</i>	<i>S&P 500</i>	<i>NASDAQ Composite</i>
<i>5/2025</i>	1.63%	1.88%	1.06%	-.74%
<i>1-Year</i>	10.77%	11.70%	13.52%	1.19%
<i>5-Year</i>	7.10%	7.16%	15.94%	15.91%
<i>10-Year</i>	5.85%	6.17%	12.86%	15.27%
<i>20-Year</i>	6.61%	7.10%	10.47%	11.76%

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<i>Market</i>				
<i>Capitalization</i>	\$1.43T	\$1.37T	\$52.8T	\$33.5T
<i>Dividend Yield</i>	4.32%	3.99%	1.24%	1.17%

REIT Review

Summary

This REIT valuation is on AvalonBay Communities, Inc., (“AVB”), a publicly traded REIT that is engaged in the development, redevelopment, acquisition, ownership and operation of multifamily communities located in New England, the New York/New Jersey metro area, the Mid-Atlantic, the Pacific Northwest, Northern and Southern California, Raleigh-Durham and Charlotte, North Carolina, Southeast Florida, Dallas and Austin, Texas and Denver, Colorado. AVB owns 309 properties with 94,865 units. Occupancy as of 3/31/25 was 96% and the same-store net operating income growth for Q1-25 YoY was 4.6%.

Property Developments

AVB has 19 wholly-owned communities under construction, with 6,595 apartment homes and a projected total capitalized cost of \$2.493 billion.

Corporate Data

AVB is traded on the New York Stock Exchange, is incorporated in Maryland, and is located in Arlington, VA. AVB has 142.3 million common shares outstanding and a market capitalization of approximately \$28.65 billion. AVB is rated A- by Standard and Poor’s and A3 by Moody’s.

Management

Benjamin W. Schall, 50, President and CEO

Ben is the Company’s Chief Executive Officer and President and has been a director of the Company since January 2021. Ben was previously AvalonBay's President, joining the Company

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in January 2021, and prior to that the Chief Executive Officer and President and a trustee of Seritage Growth Properties, a publicly traded real estate investment trust principally engaged in owning, developing, and managing a diversified portfolio of retail and mixed-use properties throughout the United States. Prior to becoming CEO and President of Seritage in May 2015, Ben served as Chief Operating Officer of Rouse Properties, Inc. from 2012 to 2015; Rouse was a publicly-traded REIT (since acquired) that owned and managed regional malls and retail centers in 21 states. Prior to that, Ben was Senior Vice President with Vornado Realty Trust, a publicly traded REIT that owns, manages, and develops office and retail assets concentrated in New York City with additional assets in Chicago and San Francisco. Ben received his Masters of Business Administration from Harvard Business School in 2003 and earned his undergraduate degree from Swarthmore College.

Top Institutional Holders	Shares (millions)	%
Vanguard Group, Inc.	22,670	15.93
Blackrock, Inc.	17,110	12.02
State Street Corporation	9,260	6.51
Norges Bank	6,810	4.79
T. Rowe Price Associates, Inc.	5,520	3.88

Ownership Breakdown	
% of Shares Held by All Insiders and 5% Owners	.36
% of Shares Held by Institutional & Mutual Fund Owners	95.99
Number of Institutions Holding Shares	1,179

All amounts above per Yahoo Finance

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Financial Analysis and Valuation

Select financial data for AVB per the 2025 Q1-10Q, and supplemental information.

(In millions where applicable)

Financial Data	Amounts
Real Estate Assets, Gross	\$26,955
Total Assets	\$21,215
Property Debt (at weighted average interest rates of approximately 3.5%)	\$8,301
Stockholders' Equity	\$11,916
Revenue	\$745
Net Income (Loss)	\$236
Cash Flow from Operations	\$415
Unsecured Credit Facility	\$2,024
Market Capitalization	\$28,650
Property Debt to:	
Gross Real Estate Assets	31%
Market Capitalization	29%
Enterprise Value	22%
Dividend and Yield (\$7.00sh.)	3.44%
Shares Sold Short (in millions per Yahoo Finance)	3,090

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Valuation Methodology	
Q1-2025 Real Estate Revenue	\$745
Q1-2025 Real Estate Operating Expenses (excluding depreciation, amortization, interest expense, impairment charges plus G&A expenses)	<u>\$291</u>
Q1-2025 Net Operating Income	\$454
Proforma Annualized Net Operating Income at 102%	\$1,852
Projected Average Cap Rate	<u>6.0%</u>
Projected Value of Real Estate Assets	\$30,867
Add: Net Operating Working Capital (at book value)	(\$11)
Construction in Progress (at book value)	\$1,198
Land Held for Development (at book value)	\$141
Unconsolidated Investments (at book value)	<u>\$226</u>
Total Projected Value of the Assets of the Company	\$32,421
Less: Total Debt per Above	<u>(\$8,301)</u>
Projected Net Asset Value of the Company	<u>\$24,120</u>
Common Shares Outstanding, 142.3M Common Shares	
Projected NAV Per Share	\$169
Market Price Per Share on 7/15/25	\$201
Premium (Discount) to NAV	19%

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Financial Metrics

The gross real estate assets, property debt, revenue, net income, funds from operations, return on invested capital, dividend coverage, and dividends per share for AVB for the years 2020 through Q1-25 are shown in the table below.

(Millions except dividend and per share amounts)	2020	2021	2022	2023	2024	Q1-25
Gross Real Estate Assets	\$22,550	\$23,799	\$24,619	\$25,462	\$26,729	\$26,955
Property Debt	\$7,564	\$8,103	\$8,315	\$7,981	\$8,076	\$8,301
Revenue	\$2,301	\$2,294	\$2,593	\$2,767	\$2,913	\$745
Net Income (Loss)	\$827	\$1,004	\$1,136	\$928	\$1,081	\$236
Funds from Operations (FFO)	\$1,186	\$1,135	\$1,353	\$1,462	\$1,564	\$403
Return on Invested Capital (1)	7.8%	6.9%	8.4%	8.9%	9.1%	NA
Dividend Coverage (2)	1.34	1.28	1.52	1.58	1.69	1.66
Dividends Paid Per Share	\$6.36	\$6.36	\$6.36	\$6.60	\$6.80	\$7.00(3)

- (1) This ratio is cash provided by operations plus interest expense divided by stockholders' equity plus property debt and measures the return the REIT is earning on its invested capital.
- (2) This ratio is funds from operations divided by common and preferred stock dividends and distributions to noncontrolling interests.
- (3) The dividend in 2025 is \$1.75 per quarter.

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

AVB Total Return	5/2025	1-Yr	3-yr	5-Yr
	-5.23%	10.75%	3.34%	9.47%

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As shown above, our net asset value per share for AVB is \$169/sh., compared to a market price of \$201/sh. Current average cap rates for apartment properties per our industry experience and CBRE's Cap Rate Survey are in the 5.0% to 7%+ range, depending on the location, age and quality of the property. We have used an average cap rate of 6.0% due to AVB's quality portfolio of apartment communities.

Strengths:

- An attractive dividend yield of 3.44%.
- A low debt-to-enterprise value of 22%.

Concerns:

- REIT prices will decline if interest rates increase.
- The dividend has only been increased by 10% since 2020.
- AVB is trading at a 19% premium to our NAV.

Recommendation:

AVB is trading at a 19% premium to our NAV per share and we do not recommend the purchase of the stock.

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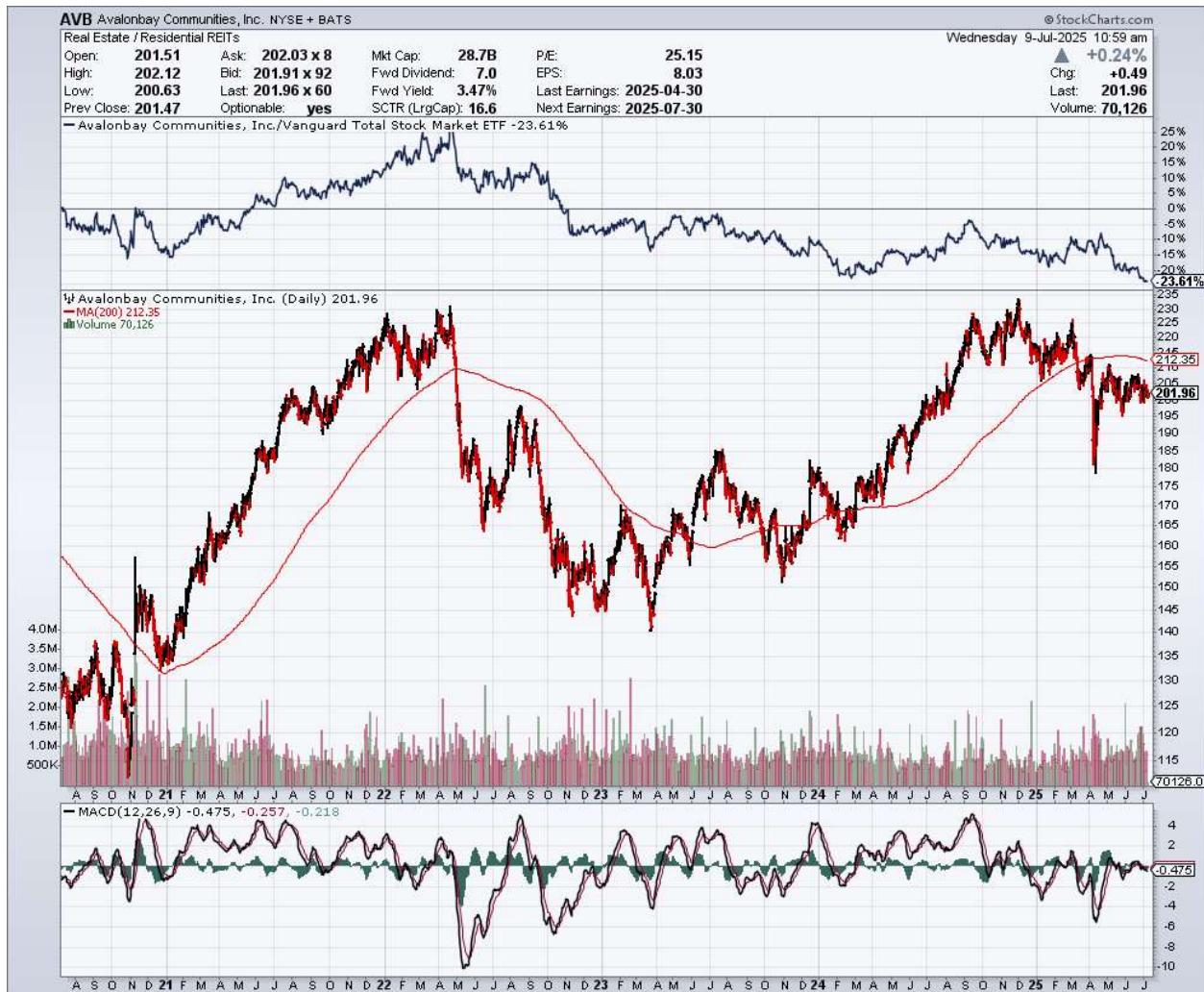
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A five-year price chart for AVB is shown below:



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



1. Camden Property Trust, August 2024
2. Regency Centers Corporation, September 2024
3. Kilroy Realty Corporation, October 2024
4. BXP, Inc., November 2024
5. Realty Income Corp., December 2024
6. Equity Residential, January 2025
7. Douglas Emmett, Inc., February 2025
8. Rexford Industrial Realty, Inc., March 2025
9. Broadstone Net Lease, April 2025
10. Alexandria Real Estate Equities, Inc., May 2025
11. Tanger, Inc., June 2025

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