THE QUARTERLY

TRUST REPORT

MULTI-EMPLOYER PROPERTY TRUST

INSIDE:

- **A Discussion with Doug Poutasse, Head of Strategy and Research, Bentall Kennedy: *Commercial Real Estate in a Rising Interest Rate Environment***

SECOND QUARTER | JULY 2013 | VOLUME 28, NUMBER 2

MULTI-EMPLOYER PROPERTY TRUST (MEPT) closed the second quarter of 2013 with a unit value of **$7,006.98** up **2.64 percent** (net of fees) from the previous quarter. For the trailing four quarters, MEPT's net return is **5.69 percent**.

U.S. ECONOMIC AND REAL ESTATE OVERVIEW

In the second quarter, the U.S. economy continued to steadily recover as employment and consumer confidence rose, U.S. corporate profit margins reached record highs, and inflation remained low. Furthermore, the housing market showed signs of continued recovery with higher home prices (11 percent year-over-year increase), increased construction activity, strong existing home sales, and lower inventory. U.S. consumers benefitted from the stronger housing market, low interest rates and a stronger U.S. dollar. At the same time, the widely-anticipated U.S. government sequestration was a modest drag on the economic recovery, but had a significantly lower impact than expected in the second quarter.

There was volatility in the capital markets during the quarter mostly as a result of uncertainty about the U.S. Federal Reserve's plans to reduce quantitative easing, in particular its bond buying program. This concern also drove investor fears of rising interest rates. (See In-Depth Report: *Commercial Real Estate in a Rising Interest Rate Environment*.)

Job growth helped spur the recovery and remained strong in the second quarter with the average monthly increase through the first six months of the year above 200,000 jobs. Private service sector job growth continued to offset job losses in the government sector and weak growth in goods-producing sectors.

In particular, the professional and business services recovery has expanded office-using employment and driven the office sector vacancy lower. The overall office vacancy rate in U.S. central business districts (CBD) at the end of the second quarter decreased by 10 basis points to 10.8 percent, and suburban office vacancy decreased 20 basis points to 11.9 percent, according to CoStar Group. National industrial availability decreased by 30 basis points during the quarter to 12.0 percent. The industrial sector has had vacancy declines for 12 consecutive quarters, with the three most recent quarters showing the largest drops in availability, according to CBRE-EA. As demand has improved for both asset classes, limited new construction of office and industrial space has constrained supply. Overall, technology and energy-oriented markets continued to experience the strongest growth, but the recovery is expanding to other markets.

The national vacancy rate for the multi-family sector was at 4.3 percent at the end of the second quarter, according to REIS, Inc. **At less than five percent, the apartment vacancy is at a level that is lower than most landlords choose to operate — most owners target a 95 percent operating**

(continued inside)

News Briefs

475 SANSOME STREET

IN APRIL, MEPT OBTAINED $81 MILLION IN FINANCING FOR 475 SANSOME STREET. MEPT purchased the 90 percent-leased, 353,686 square foot office building in San Francisco in the fourth quarter of 2012 for $162.8 million. MEPT secured the fixed-rate, 10-year loan at a rate of 3.25 percent with Prudential Insurance Co. MEPT's debt maturity ladder is staggered by maturity date to avoid large refinancing requirements, and borrowings are structured to minimize interest rate exposure.

IN THE SECOND QUARTER, MEPT SECURED $55 MILLION IN SHORT-TERM FINANCING TO FUND THE SECOND PHASE OF DEVELOPMENT AT ELAN UPTOWN. Phase II of this multi-family project in Minneapolis includes 387 units and complements the 203 units currently under construction in Phase I. Phase II broke ground in the second quarter. In keeping with the Fund's commitment to responsible property investing, Elan Uptown is designed to achieve U.S. Green Building Council® Leadership in Environmental and Energy Design Silver certification. Additionally, the project will generate over 1.5 million "green" job hours for members of the local Building Trades.

ELAN UPTOWN

MEPT SOLD RIVER RUN, A 374-UNIT SUBURBAN, MULTI-FAMILY PROPERTY FOR $54.5 MILLION IN GROSS PROCEEDS IN JUNE. The Chicago-area apartment complex was acquired by MEPT in 2002, one year after completion. As part of MEPT's strategic goal to reduce the Fund's allocation to assets in suburban markets, MEPT targeted the 97 percent-leased asset for sale. River Run was purchased by an owner/operator of commercial real estate who has been an active buyer in the Chicago market.

DURING THE QUARTER, MEPT SOLD WESTBROOK CORPORATE CENTER FOR TOTAL GROSS PROCEEDS OF $49.7 MILLION. The 187,653 square foot, suburban office building in the Philadelphia market was built by MEPT in 1998 and fully leased to Teva Pharmaceuticals USA, the largest FDA-approved generic pharmaceutical manufacturer in the U.S. In line with MEPT's strategic goal of reducing its allocation to suburban office assets, MEPT targeted the asset for sale. After securing a 10-year lease extension from the sole tenant, MEPT was able to command a premium price for the asset. Westbrook Corporate Center was sold in an all cash purchase to a subsidiary of CapLease, Inc., a publicly-traded real estate investment trust.

IN JULY, MEPT SOLD THREE INDUSTRIAL ASSETS IN THE ST. LOUIS MARKET FOR TOTAL GROSS PROCEEDS OF $26.1 MILLION. MEPT built West 70 Commerce Center I, III and V, totaling over 527,000 square feet, in 1996 and 1999. The assets are fully leased to multiple tenants. MEPT targeted the assets for sale due to anticipated capital expenditures at the properties. MEPT sold the properties in an all cash purchase to Exeter Property Group, a real estate private equity group.

AT THE END OF THE SECOND QUARTER, MEPT RECEIVED TOTAL GROSS PROCEEDS OF $23.3 MILLION FOR THE SALE OF CHEYENNE CORPORATE CENTER IN LAS VEGAS. The 420,000 square-foot, fully-leased distribution facility was built by MEPT in 2004. Anticipating future leasing risk since the submarket has high vacancy and negative absorption, MEPT marketed the asset for sale. Prologis, a $22 billion, publicly-traded industrial real estate investment trust, purchased the asset in an all cash transaction.

(continued inside)

Second Quarter Results

Net Return, Second Quarter

2.64%

Net Return, 07/1/12–6/30/13

5.69%

Net Asset Value

$5.42 billion

Performance

In the second quarter, MEPT produced a total gross return of 2.87 percent, composed of 1.51 percent income and 1.36 percent appreciation. Year-to-date, MEPT's performance has resulted in a total gross return of 5.16 percent, composed of 2.86 percent income and 2.27 percent appreciation. MEPT is positioned to exceed the Fund's 2013 return expectation of 7.5 percent to 8.5 percent (gross of fees) set by the Management Team at the start of the year due to strong income performance and higher than anticipated appreciation. **The team has reevaluated its outlook for the balance of 2013 and revised the 2013 performance target upwards to a range of 10.0 percent to 11.0 percent (gross of fees).**

Income: The Fund continues to benefit from stable income generated by the 38.4 million square foot operating portfolio. **Income growth has been the result of strong operating fundamentals, leasing activity and rent growth at MEPT properties.** The same-store portfolio (operating assets in the portfolio owned for the past 12 months) had income growth of 11.8 percent over the past 12 months and 6.5 percent for the first six months of the year, compared to the same period last year. Supporting the income growth, the operating portfolio is approximately 91 percent leased with manageable rollover over the next four years — less than 12 percent on average per year — and controllable tenant retention was 90.6 percent for the trailing four quarters.

Yield

	SECOND QUARTER 2013	TRAILING FOUR QUARTERS (COMPOUNDED)
NET	**2.64%**	**5.69%**
INCOME	1.28%	4.71%
APPRECIATION	1.36%	0.95%
GROSS	**2.87%**	**6.63%**
INCOME	1.51%	5.64%
APPRECIATION	1.36%	0.95%

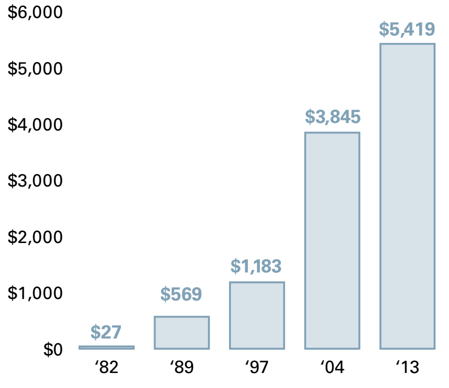
Appreciation: Construction progress at several multi-family projects as well as significant leasing ahead of pro forma at the recently delivered Via6 in Seattle produced a value increase of 4.97 percent. The 654-unit, Via6 was 71.6 percent leased at June 30, 2013 — 456 units have been leased since the leasing center opened approximately nine months ago. Two MEPT urban, multi-family operating assets — McClurg Court in Chicago with apartment leasing of 97.0 percent and The Octagon in New York that is 93.6 percent leased — had outsized appreciation as a result of strong rent growth.

Furthermore, rising market rents and recent leasing activity positively impacted the valuation of CBD office buildings including 200 West Madison in Chicago, 1900 16th Street in Denver, 475 Sansome Street in San Francisco, and 777 Sixth Street in Washington, D.C. Yield compression in the industrial portfolio due

Net Asset Value Growth

June 30, 1982 – June 30, 2013

Based on Market Value ($Millions)

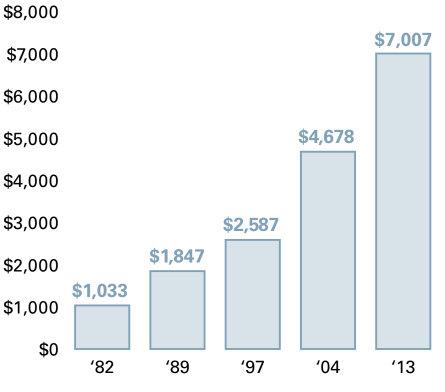


Values shown are for June 30 in each year.
Date of inception April 1, 1982.

Unit Value Growth

June 30, 1982 – June 30, 2013

Based on Market Value



Values shown are for June 30 in each year.
Date of inception April 1, 1982.

Fund Overview

Inception Date	**April 1, 1982**	Average Age of Properties	**13.0 years**
Investments Held	**129**	Markets	**29**
Number of Buildings	**310**	Net Asset Value	**$5.42 billion**
Total Operating Square Footage	**38.4 million**	Unit Value	**$7,006.98**
Operating Occupancy	**90.8%**	Participating Plans	**343**

Performance *(continued from previous page)*

VIA6

to increased sales activity resulted in strong appreciation at Gateway Commerce Center in St. Louis and Rivergate Corporate Center in Portland, OR.

Additionally, Springbrook Prairie Pavilion, a grocery-anchored retail center in the Chicago market, also had a significant increase in value as a result of changes in appraisal assumptions that reflected recent sales activity in the market. Rising interest rates resulted in a modest positive debt-to-market adjustment, excluding joint venture debt, of $7.3 million or a 0.14 percent contribution to the Fund's overall appreciation.

During the quarter, MEPT explored several potential investment opportunities. The Fund sold six assets as well as one land parcel and received a loan payoff for total gross sale price of $164.9 million, thereby contributing positive appreciation. **The Fund's allocations are aligned with the target weightings outlined in its Strategic Plan and 2013 sales represent assets that were inconsistent with the Fund's long-term strategy. MEPT was pleased with the pricing that these well-leased assets received from buyers in the market.** Current institutional investor demand for core assets has provided MEPT with an opportunity for upside potential and MEPT expects to be a net seller in the near-term and generate liquidity in the Fund through asset sales given this favorable market environment.

In Appreciation and Recognition of Our 25 Year Partnership MEPT Salutes:

Deferred Salary Plan of the Electrical Industry

Office and Professional Employees International Union, Local #153 Pension Fund

Projects Sold

Cheyenne Corporate Center
Las Vegas, NV

Hamilton Lakes E. Land Note Receivable (Loan Payoff)
Chicago, IL

River Run Apartments
Chicago, IL

West 70 Commerce Center I, III, V
St. Louis, MO

Westbrook Corporate Center
Philadelphia, PA

SPRINGBROOK PRAIRIE PAVILION

Cover Story *(continued from front page)*

occupancy. With such low vacancy in the apartment sector, effective rents have continued to rise. Additionally, the retail availability rate also fell 30 basis points to 12.2 percent. This marks the second consecutive quarter that availability has dropped 30 basis points, and consumer spending continues to rebound. Sales growth at retail centers across the U.S. has gained momentum over the past couple of months. CBRE-EA reported that both discretionary and necessity retailers have already reached and surpassed their pre-recession sales highs.

News Briefs *(continued)*

MEPT RECEIVED $11.4 MILLION IN GROSS PROCEEDS FROM THE PAYOFF OF A MORTGAGE LOAN ON THE HAMILTON LAKES EAST LAND ASSET. Located in suburban Chicago, Hamilton Lakes East is a 53.1 acres site located in the Hamilton Lakes Business Park, a mixed-use development. In early 2005, MEPT provided a $13 million loan to Hamilton Partners for a planned development in the park and the remaining balance was paid off on April 30, 2013.

Commercial Real Estate in a Rising Interest Rate Environment

Doug Poutasse
Executive Vice President
Head of Strategy and Research
Bentall Kennedy

The recovery in the U.S. economy raises the possibility that the U.S. Federal Reserve Bank may wind down its quantitative easing program sooner than expected, which would likely lead to rising interest rates. Doug Poutasse, Head of Strategy and Research at Bentall Kennedy, shares his thoughts below on the possibility of rising interest rates and the potential impact on U.S. commercial real estate and MEPT.

Should investors expect interest rates to rise? How high and how fast?

It is reasonable to expect that interest rates will rise, but it is not clear how high they will go and how quickly. While Moody's Analytics recently projected that the rate on a 10-year U.S. Treasury bond would close 2013 near current levels at 2.5 percent, reach 3.5 percent by the end of 2014, and hit 4.5 percent in late 2015, many investors are concerned interest rates will rise higher and far more rapidly. These concerns are driven by the uncertainty surrounding the future of the U.S. Federal Reserve Bank's quantitative easing program, which currently involves the monthly purchase of about $85 billion in Treasuries and mortgage-backed securities. This program has played a critical role in the U.S. economic recovery by keeping interest rates extraordinarily low and many now fear that a premature unwinding of this program will lead to rapidly rising interest rates, which could jeopardize economic growth.

Investors should expect to see interest rates fluctuate in the near term. Guidance from the Fed on its plans has been mixed, which has contributed to investor concerns and uncertainty. Those concerns impacted capital markets in May and June when the 10-year Treasury rate rose by over 60 basis points, albeit from historically low levels. However, it's important to note that, in today's volatile financial markets, interest rate fluctuations are a normal occurrence and a rate increase in one month or two can often be followed by a decline in rates in subsequent months. This occurred in early 2012 when rates rose over 24 basis points during February and March only to give back all of that increase in April and continue to fall in May and June. That being said, the rise in May and June of this year was more substantial than we have seen in some time.

While the Fed's extraordinary efforts to keep long-term rates low could wind down later this year, their accommodative stance on short-term rates is unlikely to change anytime soon since the unemployment rate is holding in the mid-seven percent range and inflation remains extremely low.

How will rising interest rates impact commercial real estate?

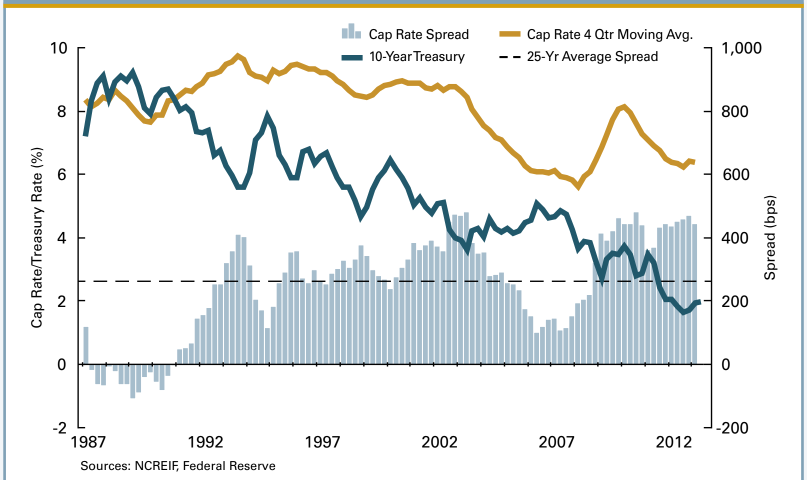
Commercial real estate should remain an attractive asset class even as interest rates rise over the next few years. There is a significant spread between Treasury and real estate yields (or capitalization rates)[1]. The difference between the average cap rate and, the 10-year Treasury, a proxy for a risk-free rate, represents the additional return an investor requires to compensate for the risk of investing in commercial real estate.

As yield-conscious investors have sought out higher-yielding alternatives relative to Treasury bonds, real estate has attracted investors. Even with the recent increase in interest rates, the 10-year Treasury rate is in the 2.5%-range. The spread to Treasuries is at an historic high. The four-quarter moving-average of the transaction-based NCREIF[2] cap rate as of the end of the first quarter of 2013 was 6.4 percent, offering a spread over the 10-year Treasury rate that is about 130 basis points higher than the 25-year average spread of 263 basis points. So Treasury rates could rise by well over a percentage point before spreads relative to current cap rates begin to return to more normal ranges. **While it is true that real estate capitalization rates have compressed from their highs during the recession due to the relative attractiveness of the asset class, cap rates still offer a considerable spread to Treasuries.** (*See chart below: Treasury to Cap Rate Spread.*)

Rising interest rates can negatively impact real estate returns, but in this environment, the rising rates are reflective of the stronger economic growth and easing of Fed intervention. With stable job growth, the economic recovery is

(continued on back page)

TREASURY TO CAP RATE SPREAD



Sources: NCREIF, Federal Reserve

[1] For real estate, the capitalization rate ("cap rate") represents the expected income return of a property, and is often compared to the yield on a U.S. Treasury bond with an equivalent maturity, or "hold".

[2] NCREIF, the National Council of Real Estate Investment Fiduciaries, is a trade association of institutional real estate professionals. NCREIF collects and disseminates real estate performance information, most notably the NCREIF Property Index (NPI) and NCREIF Fund Index – Open - End Diversified Core Equity (NFI-ODCE).

Management Fee—The Trustee of MEPT charges an annual investment management fee based on the net assets of the Fund. The current annual MEPT fee is approximately 0.89%. The fee is determined as follows: 1.25% on the first $1 billion of MEPT total net assets, 1.0% on the second $1 billion of MEPT total net assets, and 0.75% on MEPT total net assets above $2 billion. Cash balances in excess of 7.5% of Property Trust net assets are excluded from the above fee calculation and will be subject to an annual fee of 0.15%. Therefore, the fee decreases as MEPT grows. There are no charges for entry or exit, and the Trustee charges no additional investment management fees to its investors.

IN-DEPTH REPORT *(continued from inside)*

benefiting commercial real estate fundamentals and property values. In fact, most major markets have experienced falling vacancy rates and rising rents, and property income should continue to rise as market conditions improve, supporting solid real estate yields. In the short-term, the strengthening fundamentals should offset downward pressure on real estate yields from rising interest rates. **Given past trends and expectations for future growth, the current spread appears wide enough to absorb meaningful additional increases in interest rates without a material negative impact on property values.**

It is important to note that higher interest rates do not always mean that cap rates will rise. Between 2003 and 2006, the 10-year Treasury rate rose by 150 basis, yet cap rates fell. **This being said, given the leveling out of cap rates in recent quarters, rising interest rates most likely signal an end to cap rate compression driven by pricing.** It is our expectation that it is more likely that future real estate performance will be driven by underlying fundamentals and net operating income (NOI) growth than it has been during the U.S. economic recovery to date.

There will be some impact on the cost of borrowing for commercial real estate investors, but it is not expected to be a dramatic increase, especially for short-term debt. Unlike in past cycles, because of the nature of Fed actions, long-term commercial real estate debt pricing is likely to rise before short-term debt pricing. Short-term borrowing rates are unlikely to change until central banks globally make the conscious decision to move short-term interest rates higher. Eventually, however, both long and short-term borrowing costs will rise.

How will rising interest rates impact MEPT?

MEPT's strong and growing income stream is expected to help mitigate the impact of increasing cap rates caused by rising interest rates. Through its well-positioned portfolio, which is composed of high-quality properties in markets with favorable economic prospects, MEPT expects to drive NOI expansion through occupancy and rental rate improvements as the economy strengthens. MEPT's $1 billion development pipeline, which is starting to deliver best-in-class multi-family properties in top urban markets, will further enhance NOI growth due to initial leasing and, subsequently, expected rental rate growth in these markets.

Additionally, the MEPT strategy does not rely heavily on borrowing and approximately 80 percent of MEPT's debt portfolio is currently financed with fixed-rate loans. Therefore, the Fund has limited direct exposure to a rise in commercial real estate borrowing rates. **In fact, as benchmark interest rates rise, the value of MEPT's liabilities will decrease as its fixed-rate loans are marked-to-market, resulting in equity appreciation.**

The Trust Report is published by Multi-Employer Property Trust (MEPT), a commingled open-end real estate equity fund that invests in a diversified portfolio of institutional-quality real estate assets and 100% union-built new construction properties in major metropolitan markets around the country. MEPT's primary investment strategy is to create top-quality, income producing assets through development, rehabilitation or acquisition and repositioning of under-valued assets. MEPT's investor base is diverse and is composed of Taft-Hartley and public employee pension plans.

For more information, please contact Landon Butler & Company, LP at 202.737.7300, or through the Web site, **www.mept.com**.

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