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Possible Indicators of a Market Recovery

September 2008

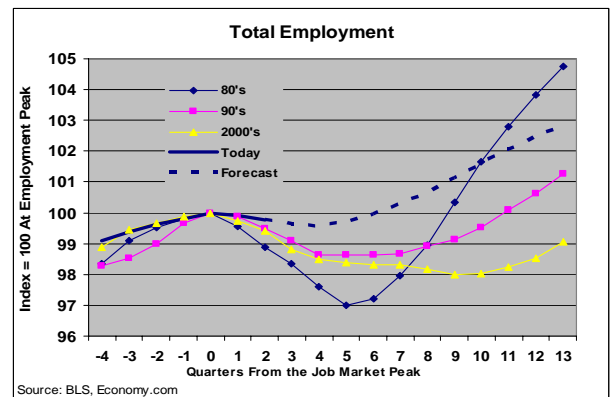
In this newsletter, we will discuss which indicators are likely to help lay the foundation needed to recover from the current market slowdown. Additionally, we will discuss how investments made during similar periods of market stress have fared and what risks exist that could delay or slow the recovery.

What are the Signs to Watch for Indicating a Market Recovery?

The current market environment has convinced many investors to sit on the sidelines due to uncertainty about where income and values for real estate are headed. Although investors should not try to time the real estate market, in order to make an informed investment decision, it is important that one understands where we are in the market cycle. We have found that over the past three downturns, (1) employment growth, (2) housing sales growth and (3) housing price increases have tended to be strong indicators of future economic growth and commercial real estate market conditions. Recoveries are parabolic in nature and no bell is rung at the bottom; but we have found that the stabilization of these three factors are indicative of a recovery. In addition, in the current market, we are going to pay particular attention to the increase in the number of home sales, as we believe this will be a key determinant of the turnaround.

JOB GROWTH

The fuel for real estate demand is job growth, so until employment numbers turn positive, net positive absorption of real estate is not likely to return. Significant job growth typically trails corporate profit growth, as firms need to make sure profits can be sustained prior to hiring additional personnel. We expect that out-sourcing and a rise in consultant usage will be an early indicator for future employment growth. At present, total employment is down 0.4% from the peak and is expected to hold up significantly better than in prior recessions. The question is, "Will this trend continue, resulting in a relatively mild slow down or will it get worse?"



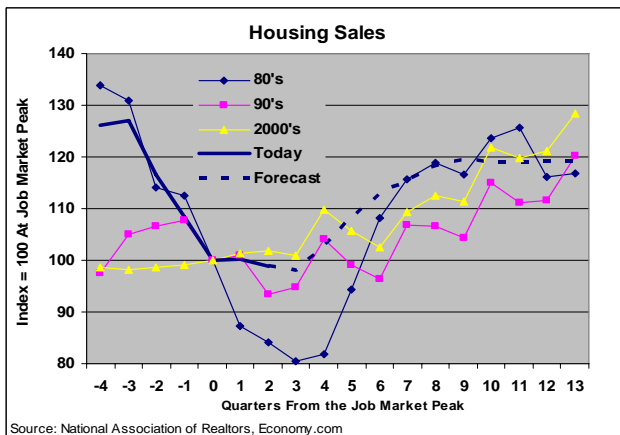
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HOUSING SALES

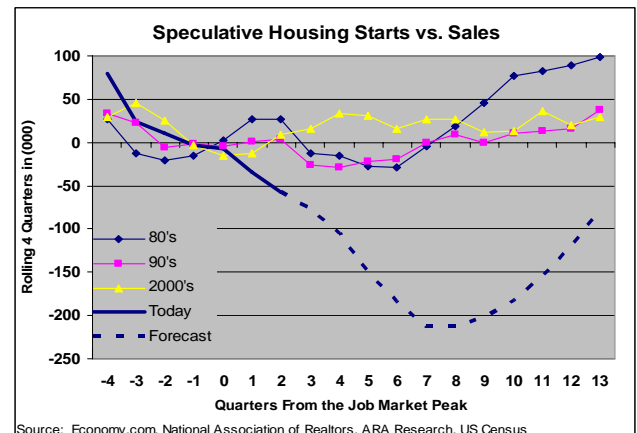
In the three previous downturns, an increase in housing sales volume was either the first indicator to turn positive or it slightly lagged corporate profit growth. A rise in housing sales helps fuel the entire economic recovery, as buyers of homes also tend to spend money on consumer goods, such as appliances and furniture. In the current cycle, housing sales are down 22% from 1Q07, but have recently started to rise, in some of the most depressed markets such as Las Vegas, NV and Ft. Myers, FL.



HOUSING PRICES

Generally, the lag from job growth to housing price growth is approximately one year, as the housing market needs to reduce supply levels before values can rise. Since new housing competes with resale housing, the first phase of this reduction is to reduce the supply of speculatively built new homes on the market. In fact, an unprecedented reduction in inventory is occurring, as new home sales are exceeding new starts by 50,000 units. We are expecting this to expand to a record of nearly 200,000 units within the next year. Corresponding to the expected reduction in new housing inventory levels, the national resale housing supply level should start to decline. Based on historical trends, a fall in the resale housing inventory from a current level near 11 months to eight months, is

normally associated with solid housing price increases. Given the overhang that now exists, we do not see that occurring over the next year, but clearly the shift in this metric would be one of the strongest indicators of a market recovery.



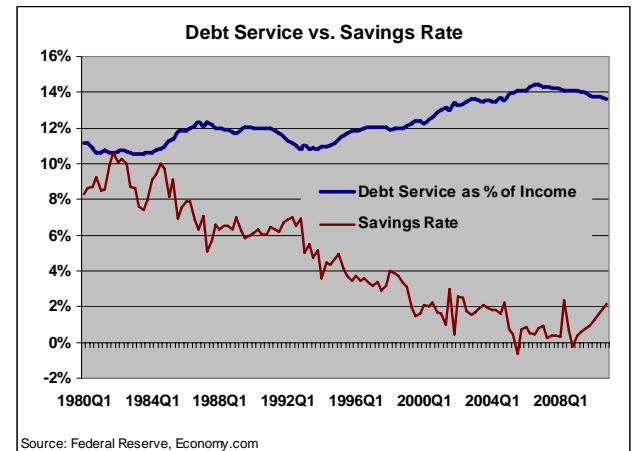
While it is difficult to be precise in predicting the future, these three factors have historically proved to be strong indicators that the economy and the associated real estate markets are beginning to recover. The recent growth in housing sales, even in some of the nation's most depressed markets, is the first of many indicators suggesting a positive turning point in the economy and commercial real estate.

Potentially helping to support a decline in housing supply is the high level of housing sales as a percentage of the market stock, with the sales volume holding at about 6.5% of total inventory. In comparison, this property sales volume is significantly higher than in the 1980s and 1990s when housing sales slowed to 4% and 5.5% of inventory, respectively. This higher level of sales activity suggests that while the supply of housing is elevated, the high sales rate should help to support a rapid reduction in housing inventory once this turning point is reached.

Risks to Recovery

CONSUMER DEBT SERVICE BURDEN

Longer term, the growing level debt service burden is likely to continue to constrain the economy and result in a higher level of debt default than has occurred in the past. Supporting this view, debt service levels as a percentage of income have risen from 11% in the 1980's to over 14% currently. This rise is due in large part to: 1) the historically low cost of borrowing, 2) increased willingness of lenders to make credit available to the full range of consumers, not just the most creditworthy, and 3) easy access to home equity and other housing related debt tied to values that are now starting to turn downwards. Overall, this liberal lending policy has supported a rise in liabilities to 20% of household income compared to only 13% in the 1980's, although lower interest rates are offsetting some of the effect of this increase.

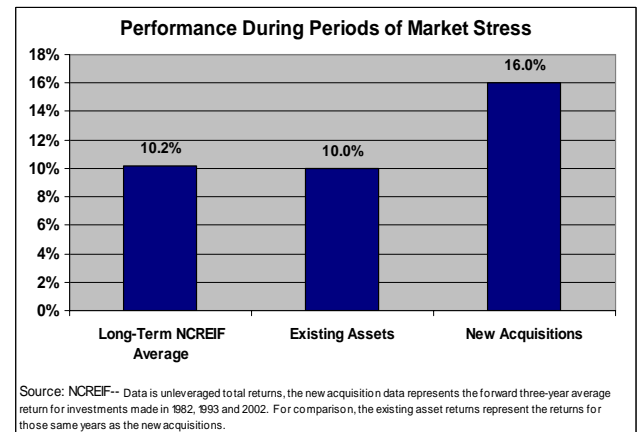


LOW SAVINGS RATE

The US personal savings rate has fallen to nearly zero, compared to a 9% average in the 1980s and much higher savings rates in other countries. Although some of this traditional savings has been diverted to retirement plans and other tax deferred vehicles, thereby increasing overall wealth, the limited amount of savings and restricted access to retirement vehicles means that when the economy enters rough periods with declining employment and reduced incomes, the ability of the household sector to continue spending at previous levels will be curtailed. We believe that an increase in the traditional savings rate is essential to a market recovery.

Investments During Periods of Stress Perform Well

Studies of past weak points in the market (1982, 1993, and 2002) shows that returns for existing investments over the subsequent three years have nearly matched the long-term NCREIF Property Index return of 10.2%. Furthermore, for new acquisitions made during these periods of market stress, the returns for these investments over the next three years have averaged a cumulative 18% more than the NCREIF Index during this same period. In total, this suggests that investors willing to take a well-researched risk during a period when others are shying away from the market, may be handsomely rewarded. We think that 2009 is likely to present this opportunity.



Conclusion

In light of the current economic cycle, several factors, specifically rising housing sales, job growth and rising housing prices, are typically the indicators of a market recovery. While these indicators have not yet turned positive, we expect the commercial real estate market to follow with these broader market trends. While investors wait for the anticipated recovery, the lower level of job loss during this downturn compared to past downturns suggests that real estate fundamentals of occupancy, rent and NOI should perform equal to or better than during prior downturns. Additionally, history has shown that for investors willing to take some risk during this period of stress, the rewards have historically been strong for both existing investments and new investments.

Key Indicators			
Interest Rates	9/4/2007	8/4/2008	9/4/2008
10-Year Treasury Yield	4.6%	4.0%	3.6%
CMBS AAA Yield	5.4%	6.9%	7.5%
CMBS BBB Yield	8.9%	23.5%	27.6%
Cap Rates	2Q2007	1Q2008	2Q2008
Office	6.4%	7.0%	6.8%
Industrial	6.8%	7.2%	7.4%
Multi-family	6.1%	6.2%	6.4%
Retail	6.6%	6.9%	6.7%
12 Mo. Private Real Estate Returns	2Q2007	1Q2008	2Q2008
NCREIF - All Properties	17.3%	13.6%	9.2%
Office	22.1%	17.5%	11.5%
Industrial	16.9%	13.0%	8.5%
Multi-family	13.3%	9.6%	6.5%
Retail	13.6%	11.6%	8.7%
Vacancy	2Q2007	1Q2008	2Q2008
Office	12.5%	12.9%	13.2%
Industrial	9.7%	10.2%	10.7%
Multi-family	4.7%	5.4%	5.6%
Retail	10.2%	11.3%	11.8%
Employment	Aug '07	July '08	Aug '08
Unemployment	4.7%	5.7%	6.1%
Total Employment Monthly %	0.1%	-0.1%	-0.1%
Total Employment Yr/Yr	1.0%	0.0%	-0.2%

Source: Lehman, NCREIF, TWR, PPR, Real Capital Analytics, Economy.com, US Treasury

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