



LONG: DUKE REALTY (DRE)
SHORT: ISHARES US REAL ESTATE (IYR)

Industrial – “If you believe that the economy will keep recovering, then this is the sector to own.” - CNBC

TODAY WE WILL SHOW THAT:

1. U.S. industrial real estate will outperform all U.S. commercial real estate over next two years
2. Duke Realty will outperform its peers in the industrial real estate sector over the next two years
3. Therefore, buying Duke Realty while selling the U.S. real estate market (via IYR) will yield over a 17% return to the Carnelian Fund over the next two years

AGENDA

- Proposed Trade
- U.S. Industrial Outlook
- Company Overview
- Valuation
- Short Trade
- Summary



PROPOSED TRADE

Long: DRE

Short: IYR

TRADE OVERVIEW

		Beta Neutral						
	Ticker	Beta	Shares	Share Price	Total Value	Portfolio Weight	Weighted Beta	
Long	DRE	1.04	6,899	\$19.43	\$ 134,043	44.7%	0.46	
Short	IYR	-0.84	-2,220	\$74.75	\$ (165,957)	55.3%	-0.46	
					\$ 300,000		0.00	

- Investment Period: 18 – 24 months
- DRE Target Price: \$22.95
 - Duke Realty (DRE) Dividend Yield: 3.55%
 - iShares U.S. Real Estate (IYR) Dividend Obligation: 3.34%
- Projected Return: **17%**



U.S. INDUSTRIAL OUTLOOK

Strong Industrial Fundamentals
The Ecommerce Story
Panama Canal Expansion

U.S. INDUSTRIAL MARKET SNAPSHOT — 3Q 2014*

Economy

Domestic industrial production, foreign trade grew in 3Q 2014
U.S. GDP grew 4.6% during 2Q 2014

60.3 million sq. ft. of positive net absorption in Q3 2014
U.S. industrial market expanded for 18th consecutive quarter

Demand

Supply

30.7 million sq. ft. of new supply added in 3Q 2014
Development activity still below long-term average

Availability dropped to 10.6%, a post-recession low
Secondary markets posting greatest quarterly declines

Availability

Rents

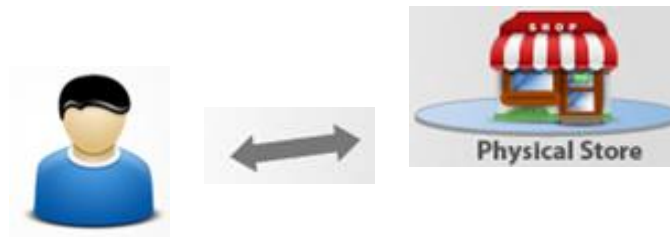
U.S. average net rent up 3.1% YTD to \$5.92 psf
Rents up in 57% of markets tracked by CBRE

* Source: CBRE US Industrial MarketView Snapshot – 3Q 2014

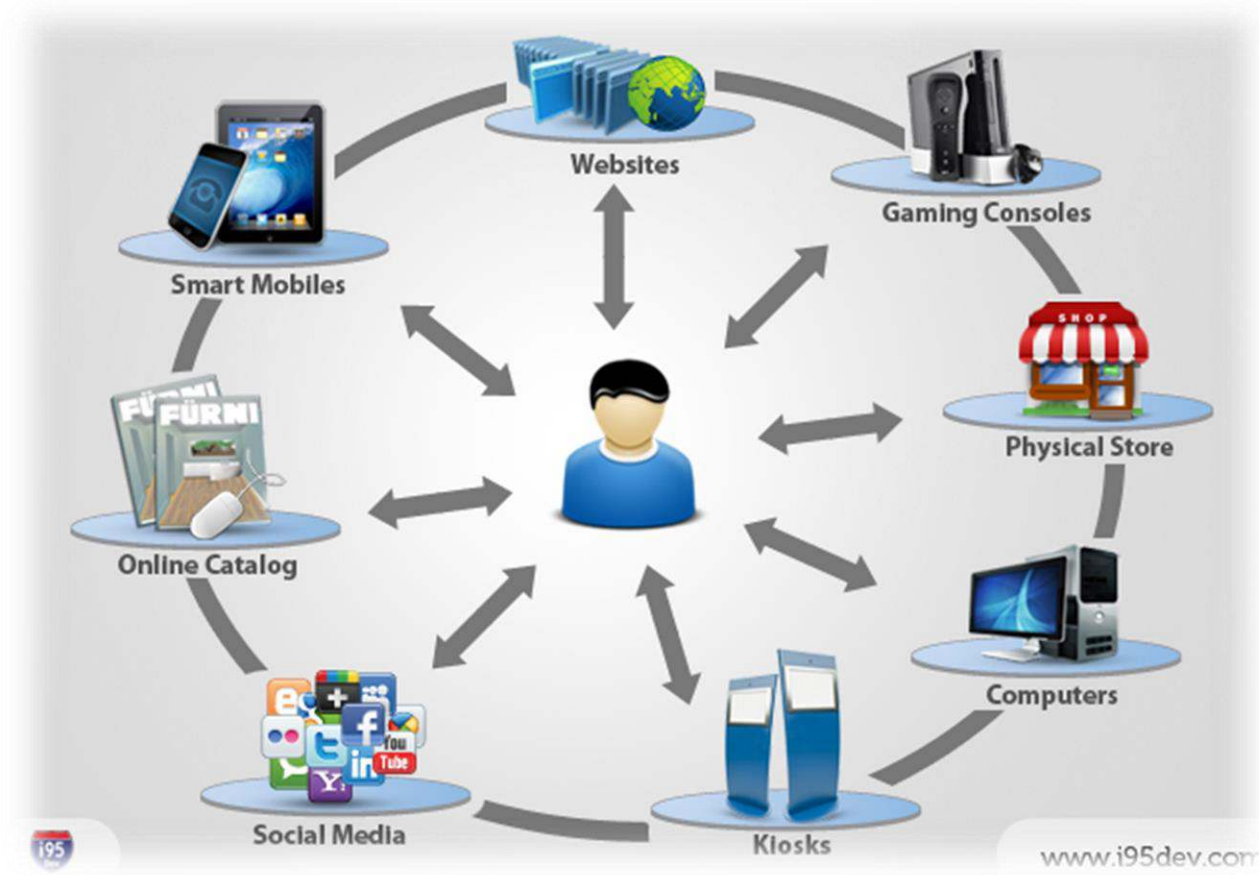
INDUSTRIAL DEMAND DRIVERS

- E-Commerce is on fire
- Seaports investing heavily in infrastructure
- Lower energy costs boost U.S. factory output

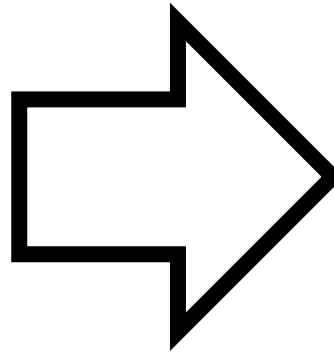
UNI-CHANNEL DISTRIBUTION MODEL



OMNI-CHANNEL DISTRIBUTION MODEL



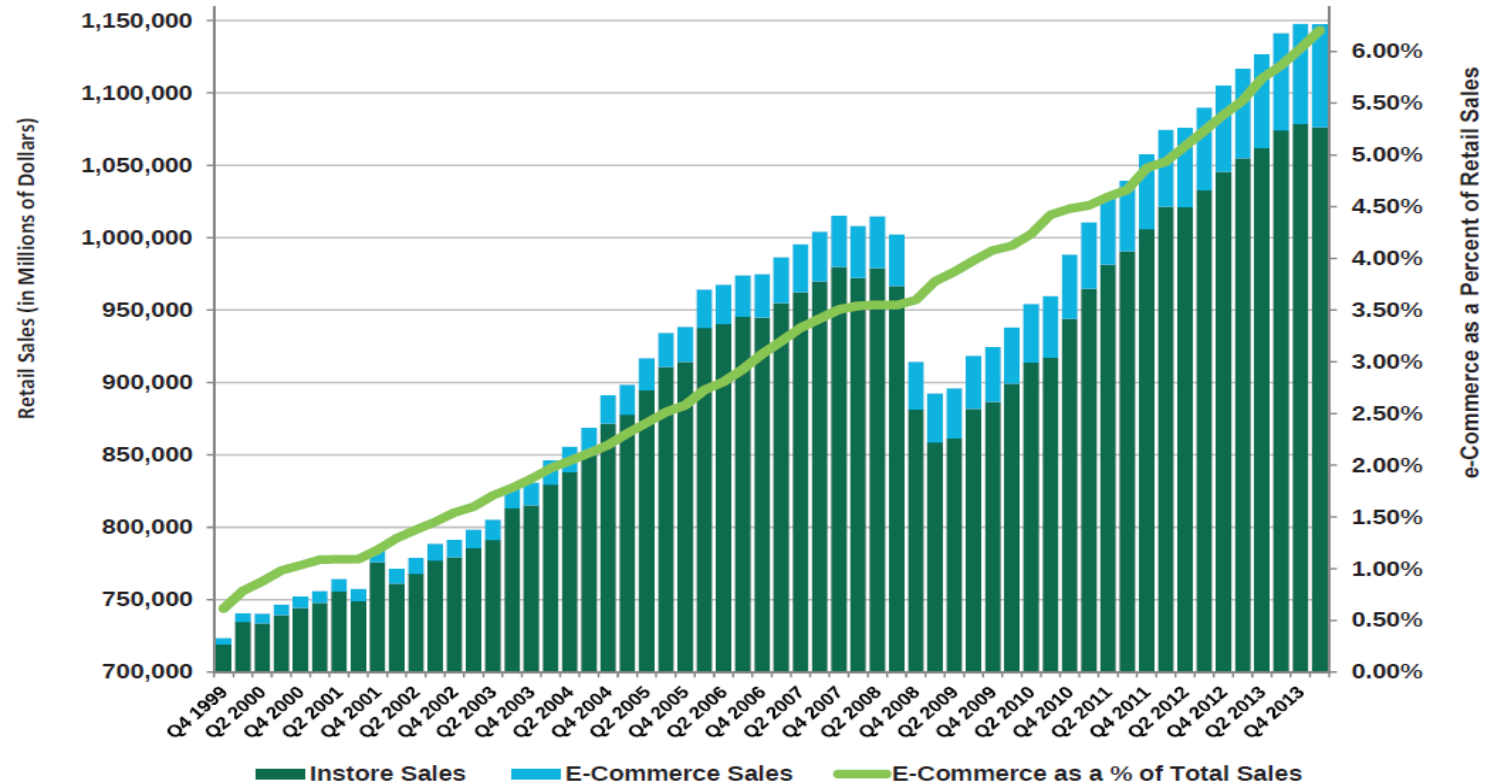
SHIFT FROM STORES TO DISTRIBUTION CENTERS



CENTERS OWNED BY COMPANIES LIKE DUKE REALTY



METEORIC RISE IN ONLINE SALES



Source: Census Bureau

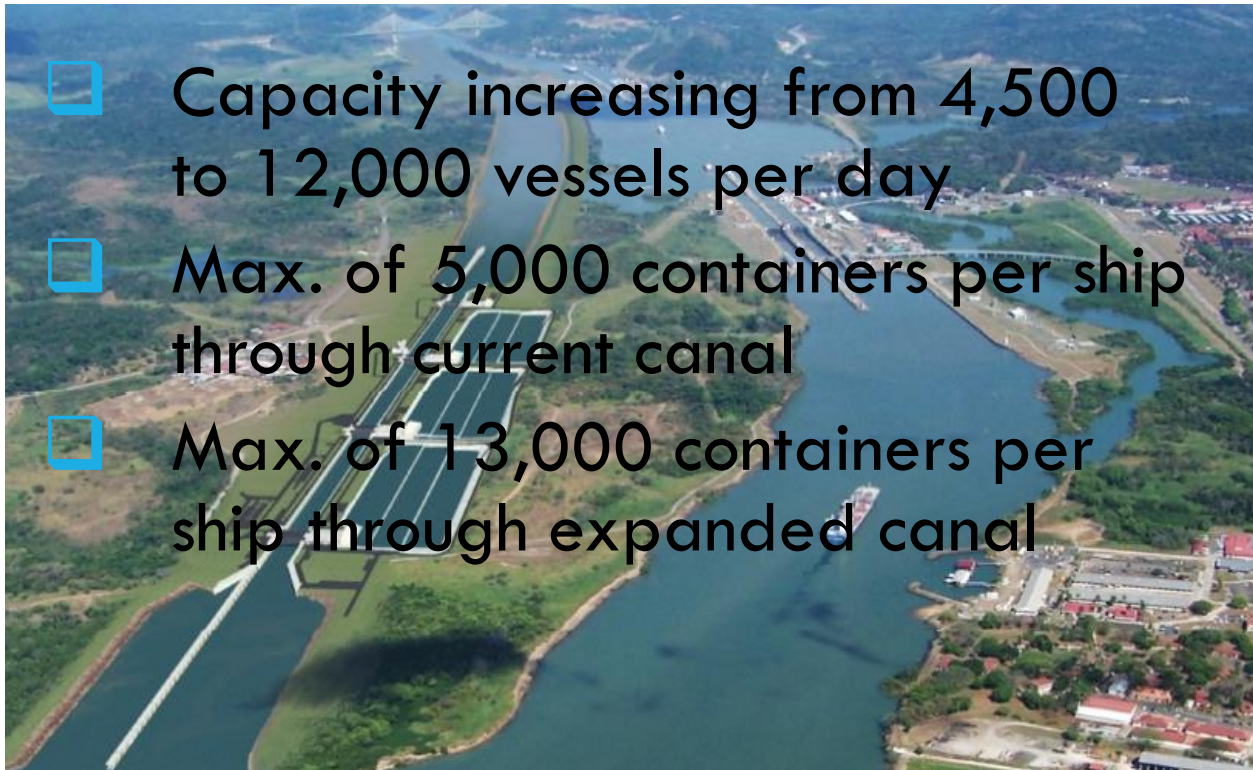
E-COMMERCE STILL ONLY REPRESENTS 6.2% OF OVERALL RETAIL SALES

E-COMMERCE = DRAMATIC EFFECT ON INDUSTRIAL RE

- ❑ E-Commerce sales growing at 20% annually
- ❑ E-Commerce uses now represent 10% of all new leasing worldwide
- ❑ E-Commerce users require 3x the logistics space as brick-and-mortar retail
- ❑ Currently 30 million SF of active E-Commerce requirements in U.S.

Source: CBRE 2Q Industrial Capital Markets Overview

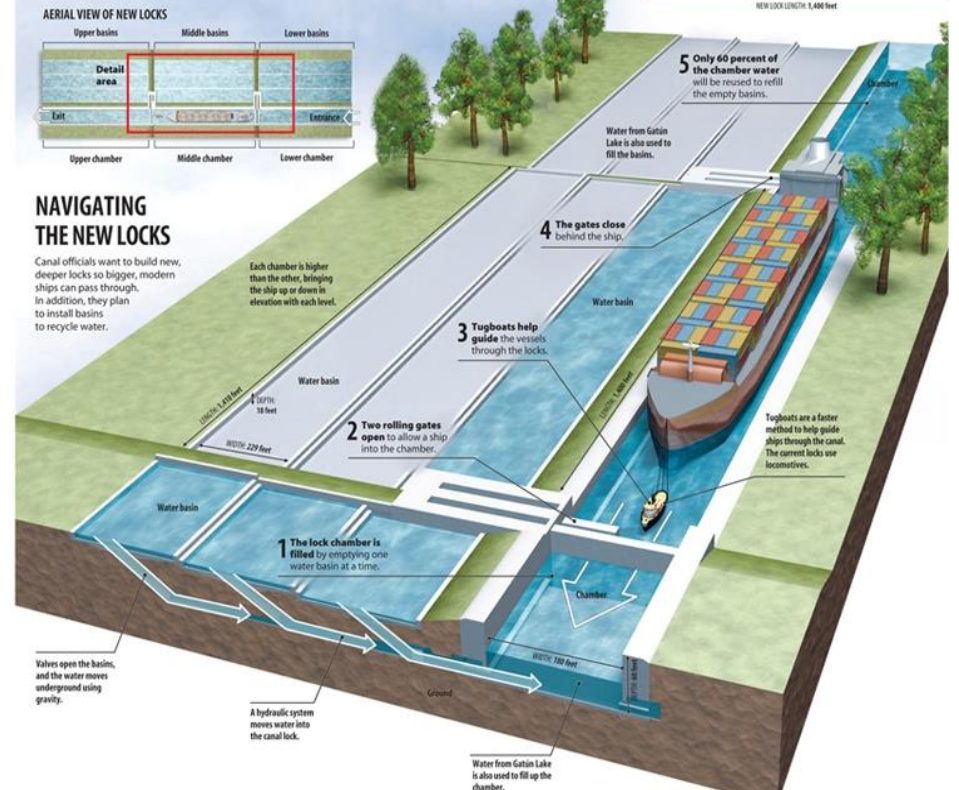
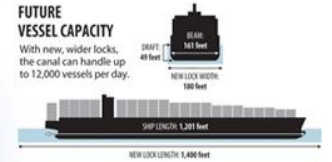
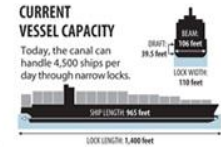
PANAMA CANAL EXPANSION



NEWS ILLUSTRATED

Expanding the PANAMA CANAL

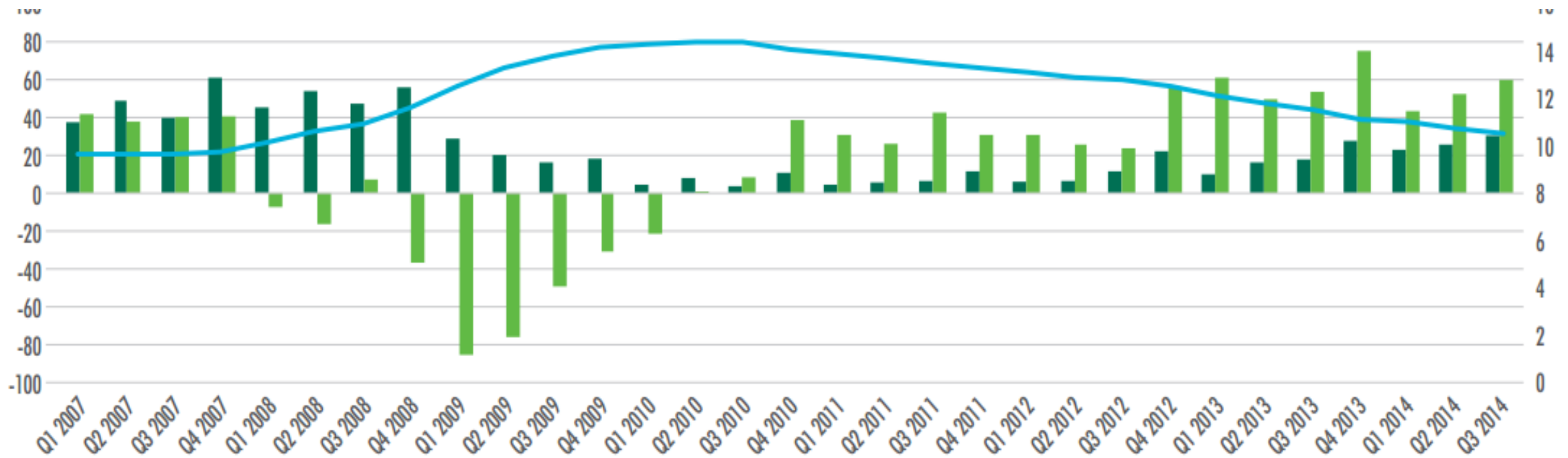
Operating since 1914, the Panama Canal is poised to undergo a \$5.2 billion expansion to keep the aging waterway competitive in today's shipping industry.



EFFECT OF PANAMA CANAL EXPANSION

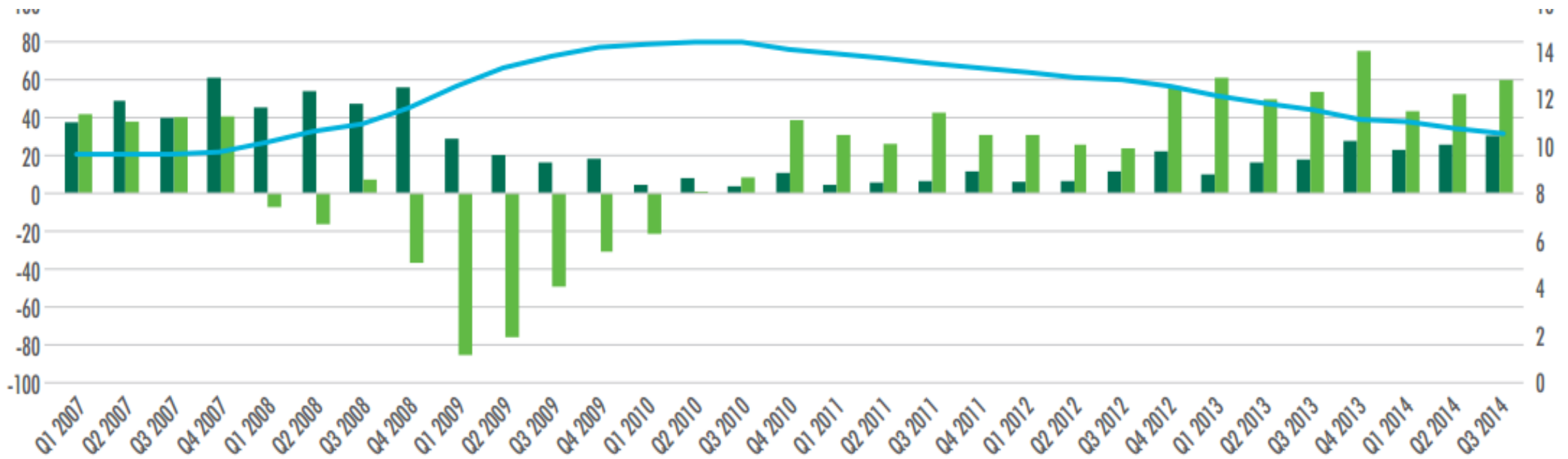
- ❑ Expansion will bring larger, more container ships to ports on both U.S. coasts
- ❑ Prompting substantial investment in port infrastructure/surrounding areas
- ❑ Increasing demand for industrial space in port-centric locations

U.S. INDUSTRIAL SUPPLY AND DEMAND



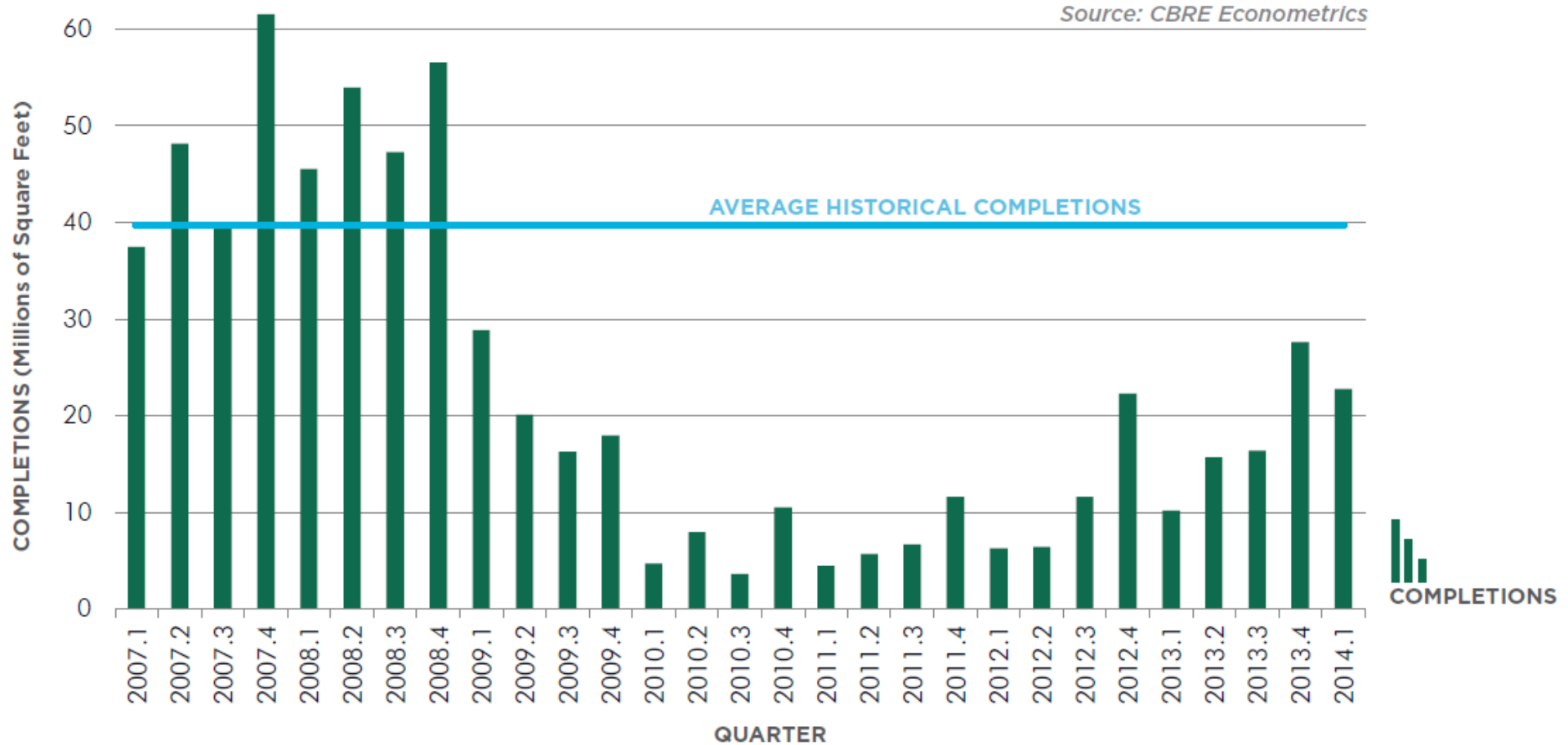
Source: CBRE Econometric Advisors, Q3 2014.

U.S. INDUSTRIAL SUPPLY AND DEMAND



Source: CBRE Econometric Advisors, Q3 2014.

INDUSTRIAL DEMAND OUTPACES SUPPLY 2 TO 1



CONDITIONS RIPE FOR RENT APPRECIATION

- ❑ Market rents still below pre-recession levels in many markets
- ❑ Many industrial markets now below long-term average vacancy rate
- ❑ Demand far outstripping supply
- ❑ Industrial rents up 3.1% YTD – 5% projected rent growth for 2014
- ❑ Accelerated rent growth likely in second half of 2014 and 2015
- ❑ Duke Realty's rent roll well-positioned to benefit from rent growth

Source: CBRE 2Q Industrial Capital Markets Overview



COMPANY OVERVIEW

Narrowing Focus
Strong Leadership
Positive Analyst Outlook

HISTORY

1972 – Founded in Indianapolis, Indiana

1993 – IPO listed on NYSE

- 10 million square foot portfolio

1999 – Merger with Weeks Corporation

- Expanded geographic reach across the South

2009 – Initiated strategic shift to industrial

2011 – Sale of \$1 billion in suburban office to Blackstone

2013 – Further geographic expansion into Pacific NW and along East Coast

- Over 150 million square foot portfolio

Source: Duke Realty; WSJ

EXECUTIVE MANAGEMENT

Dennis Oklak (Chief Executive Officer) – Mr. Oklak has served as CEO of Duke Realty since 2004 and has been with the company since 1986. He has guided Duke’s resurgence from the depths of the financial crisis, and its current strategic initiatives.



James Connor (Chief Operating Officer) – Mr. Connor is responsible for the company’s nationwide real estate operations, including its industrial, office, and medical office portfolios. Mr. Connor also oversees Duke Realty’s development activities. He joined the company in 1998, before which he was a senior executive with Cushman & Wakefield.

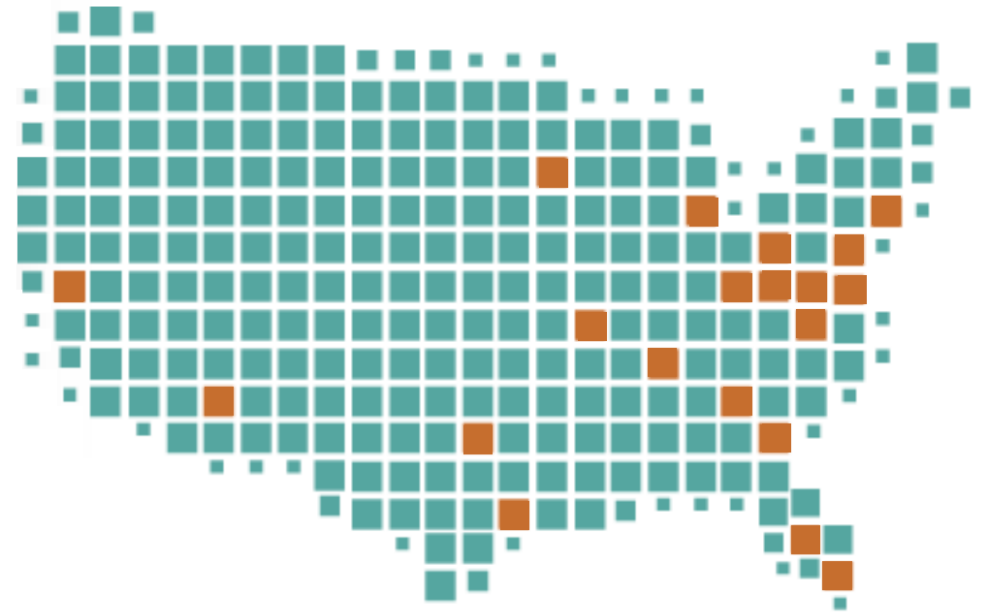


Source: Duke Realty

GEOGRAPHIC REACH

- ❑ Nationwide portfolio with growing presence in industrial strongholds like the Inland Empire and New Jersey
- ❑ Nine markets each generate greater than 4% of Duke's industrial NOI
- ❑ Industrial:
 - Indianapolis - 11.47%
 - Chicago - 10.35%
 - Dallas - 8.57%
- ❑ Office:
 - Indianapolis - 22.51%
 - Raleigh - 19.53%
 - St. Louis - 11.57%

Source: Duke Realty



ASSET STRATEGY

1. **Increase investment in quality industrial properties in existing markets and select new markets**
2. Managing medical office portfolio nationally to focus on hospital system relationships and capitalize on demographic trends
3. Increase investment in markets where management believes greatest potential for asset growth exists
4. **Reducing investment in suburban office properties located primarily in Midwest as well as reducing investment in other non-strategic assets**
5. Monetizing land inventory through development activity as well as sales of surplus land

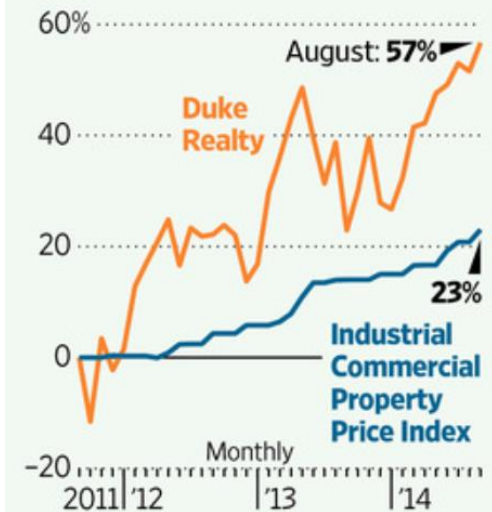
Source: Duke Realty 10-K

PORTFOLIO SHIFT

- Since 2009, Duke Realty has undergone a strategic repositioning away from a diversified, but office-focused portfolio to an industrial-focused portfolio
- This shift is in response to many factors
 - Pure-play REITs favored by investors and analysts
 - Suburban office badly impacted by financial crisis and changing workplace preferences
 - Strong industrial fundamentals
 - Industrial is significantly less capital intensive than office

Simpler Is Better

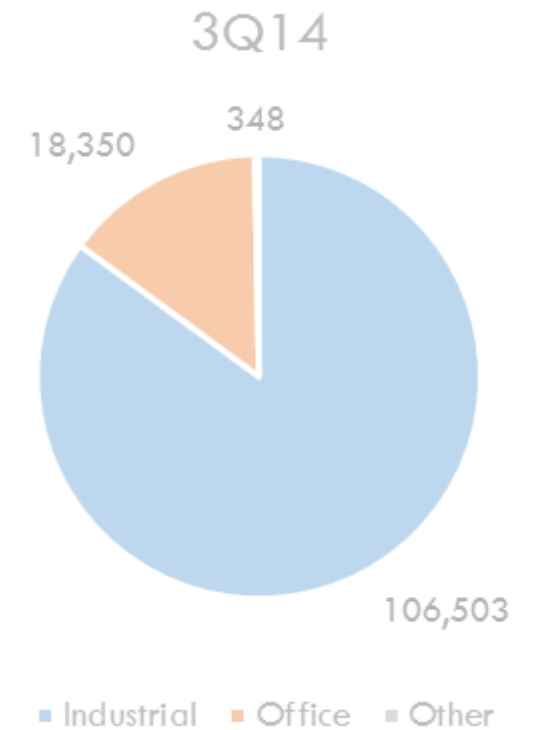
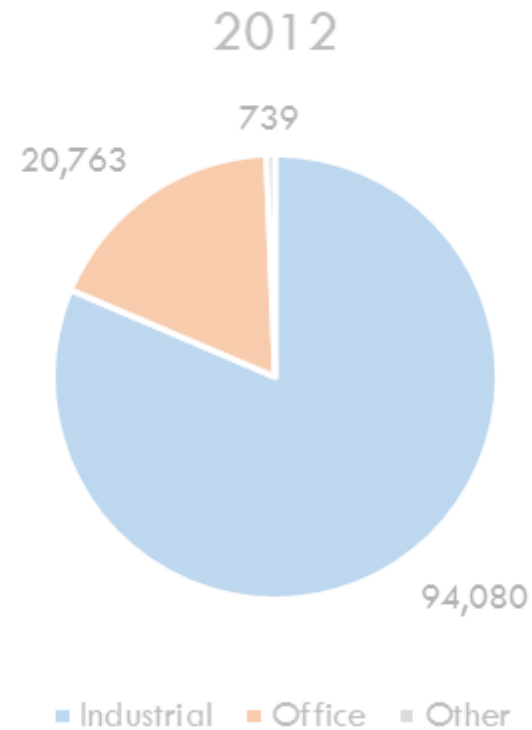
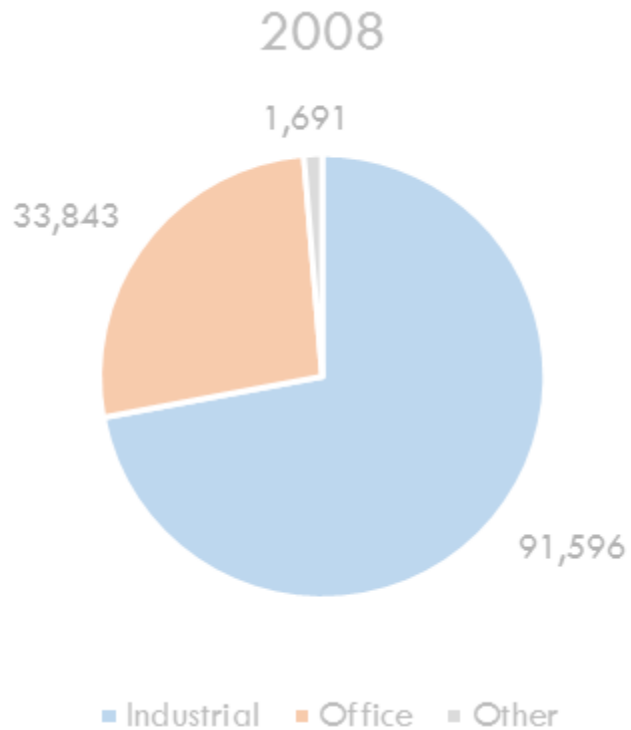
Duke's shares have beaten the broader industrial-property market as the company has streamlined. Performance over past three years:



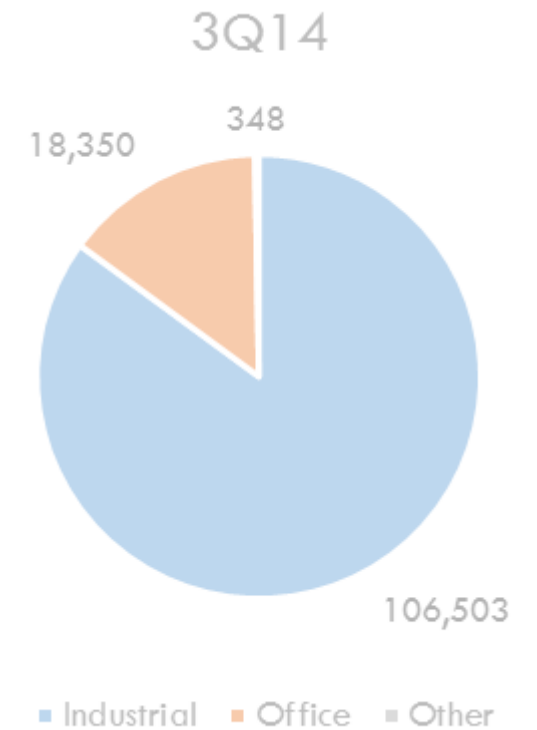
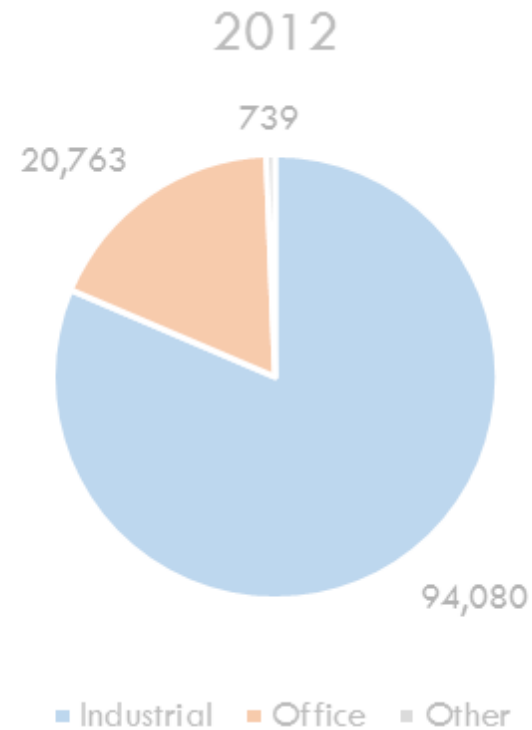
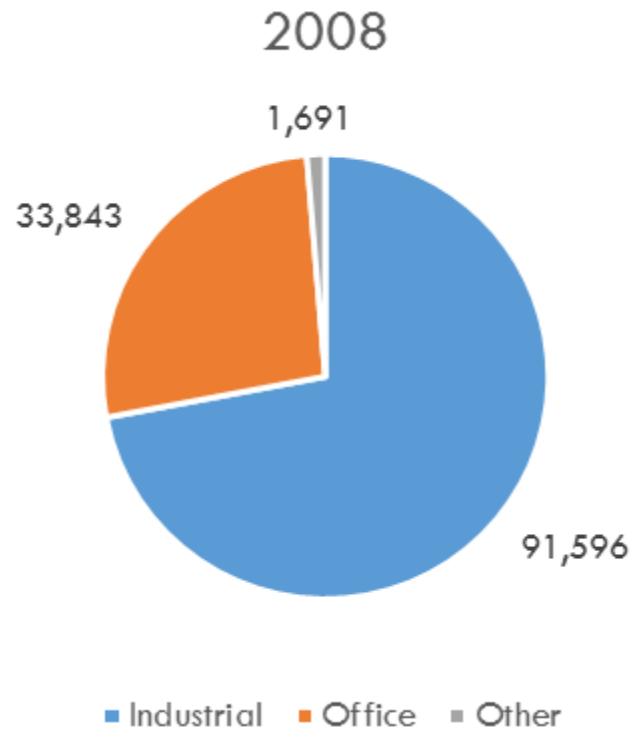
Sources: WSJ Market Data Group (shares);
Green Street Advisors (index)

The Wall Street Journal

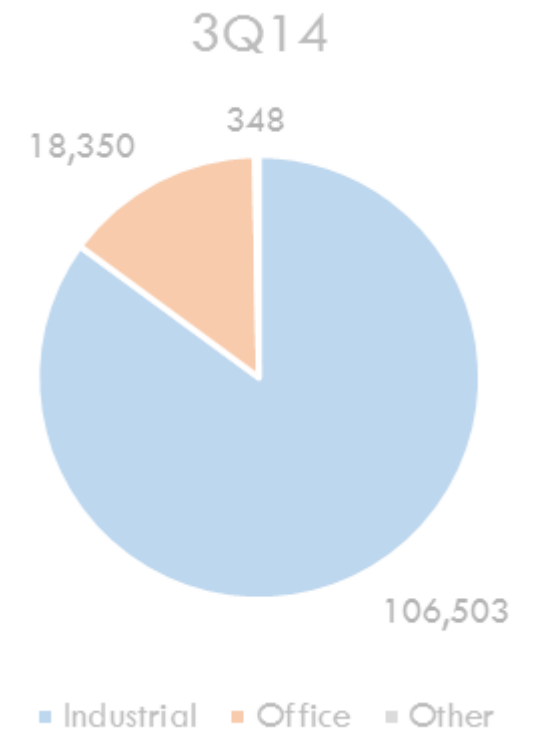
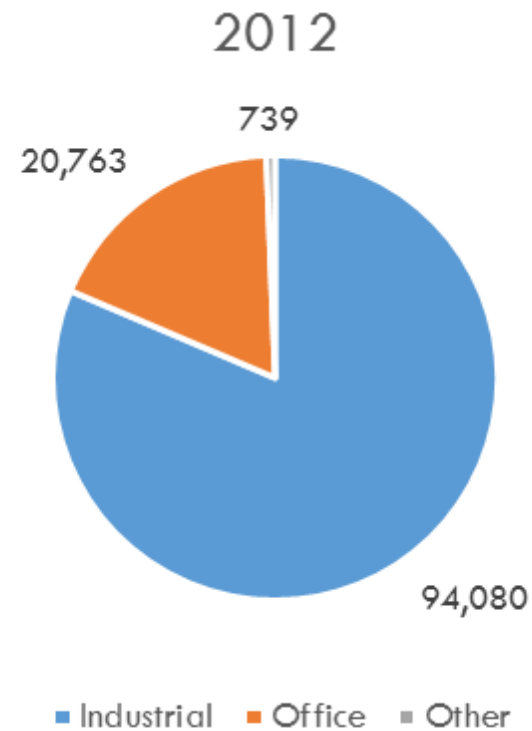
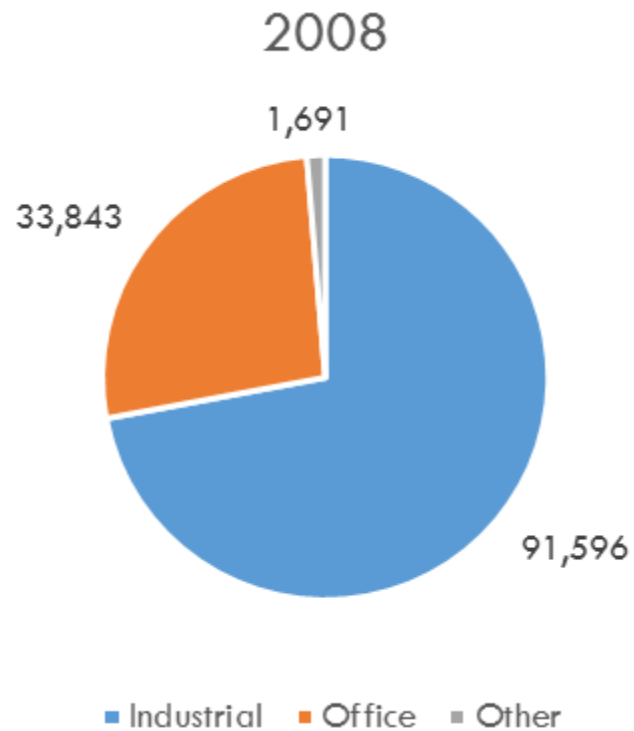
PORTFOLIO COMPOSITION - 2008



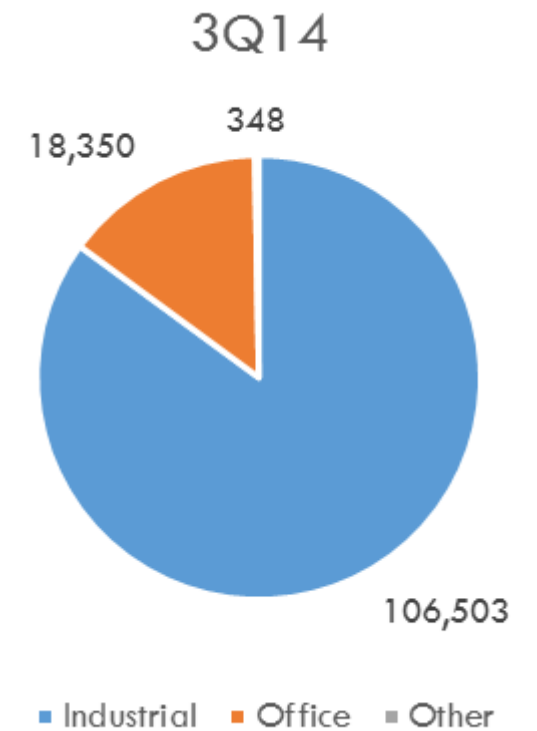
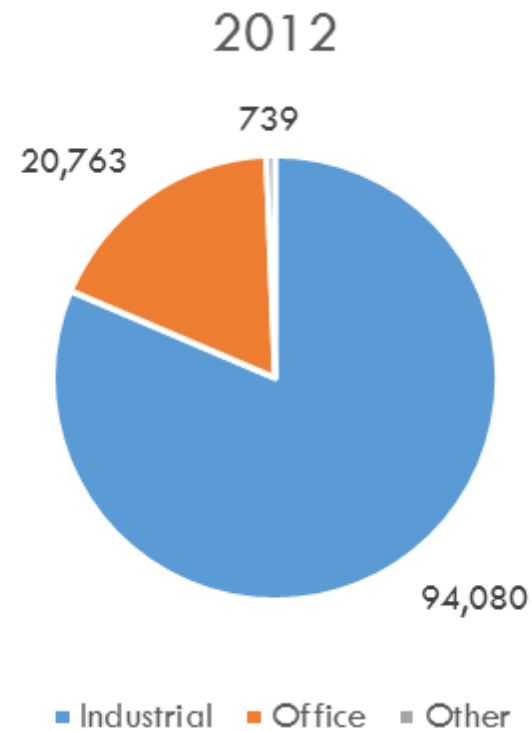
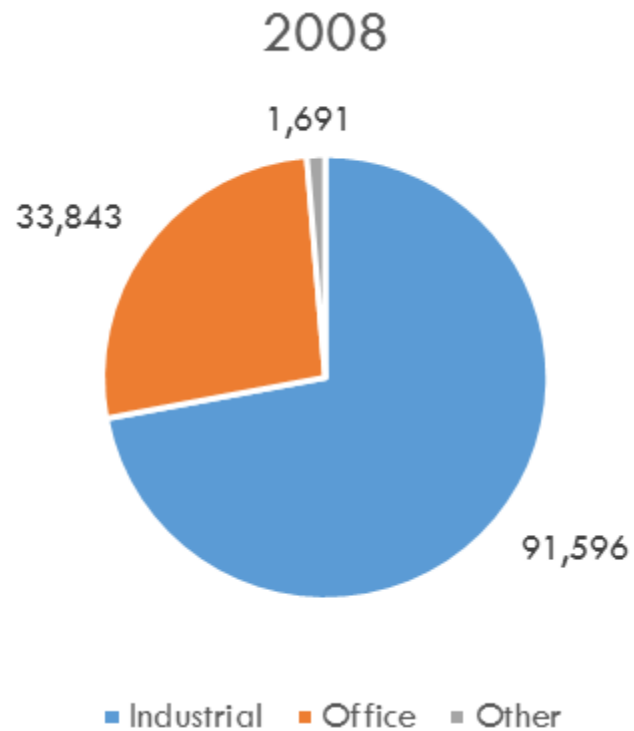
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PORTFOLIO COMPOSITION - 2008



PORTFOLIO COMPOSITION - 2008



CASE STUDY: RIVERVIEW

- ❑ **Who would want to work here?**
- ❑ Duke Realty sold 86,676 square foot building in Nashville market to a local real estate investment firm for \$4.8 million in October 2014
- ❑ 64% leased at disposition
- ❑ Originally acquired in 1999 for \$1.5 million

Source: SNL; The Tennessean



FOCUS ON DEVELOPMENT

- ❑ Duke Realty executives believe that opportunities for value creation exist more in development than in acquisition
- ❑ The company is backing this up with significant development activity, focused on industrial generally, and build-to-suit specifically
- ❑ 2013 - 19 wholly owned developments placed into service; total cost \$481.7 million
 - 4.4 million square feet
 - 90.5% leased by year-end 2013
- ❑ Third quarter 2014 - 3.6 million square feet placed into service

Source: REIT.com; Duke Realty 10-K and 10-Q

CASE STUDY: LEGACY COMMERCE CENTER

- ❑ Speculative redevelopment of former GM assembly plant in Linden, NJ
- ❑ 5 miles from Port Newark and Port Elizabeth
- ❑ Building 12 is complete and Building 13 is under construction
- ❑ Building 12 Specs:
 - 495,000 square feet
 - Delivered October 2014
 - 50 x 50 column spacing
 - 36' clear heights

Source: CoStar, New York Times



LEASES

- ❑ Retention rates
 - 68.3% in 2013
 - 62.4% in first three quarters of 2014
- ❑ Careful management of rent rolls across portfolio prevents concentration of lease expirations and reduces rollover risk
- ❑ Largest group of expirations in 2017 only represents 11.03% of rental revenue

Year of Expiration	Square Feet	Annual Rental Revenue	No. of Leases	Percentage of Rental Revenue
4Q2014	1,412	\$ 7,848	120	1.16%
2015	10,701	\$ 53,701	307	7.92%
2016	14,264	\$ 68,746	334	10.14%
2017	15,425	\$ 74,812	325	11.03%
2018	11,808	\$ 69,699	292	10.28%
2019	13,497	\$ 74,322	286	10.96%
2020	12,438	\$ 71,488	164	10.54%
2021	8,882	\$ 47,694	136	7.03%
2022	6,950	\$ 34,584	81	5.10%
2023	2,783	\$ 22,597	55	3.33%
2024 and Thereafter	21,143	\$ 152,760	142	22.52%
Total Leased	119,303	\$ 678,251	2242	100.00%
Total Portfolio	125,201			

Source: Duke Realty 10-Q

STRONG TENANT BASE

Tenant Name	% of Revenues
Baylor Scott & White Health	3.0%
Amazon.com Inc.	2.3%
United States Government	1.8%
Ascension Health Alliance	1.2%
Lenovo Inc.	1.2%
Crate & Barrel	1.0%
Home Depot Inc.	1.0%
Harbin Clinic LLC	0.9%
Catholic Health Initiatives	0.8%
Interactive Intelligence	0.8%
NFI Industries Inc.	0.8%
Schneider National Inc.	0.7%
Mercy Healthcare North	0.6%
Tenet Healthcare Corp.	0.6%

Source: SNL



SHORT INTEREST

- ❑ 2.79%
- ❑ Absolute level of short interest and recent trend support market confidence in Duke Realty story
- ❑ Fourth quarter has seen short interest decline as share price has increased



Source: Bloomberg

INSTITUTIONAL OWNERSHIP

- ❑ Institutional ownership: 94.59%
- ❑ Top 10 Institutional Owners: 49.08%
- ❑ Reported recent activity shows net increase in institutional holdings of over 11 million shares
- ❑ Insiders own 0.29% of outstanding shares

Institutional Ownership Information - Total Positions

Holder	Position	PositionChange	Shares Out(%)
Vanguard Group Inc.	45,065,770	1,064,278	13.19
BlackRock Fund Advisors	25,931,306	789,830	7.59
Fidelity Management & Research Co.	14,654,248	5,267,500	4.29
CBRE Clarion Securities LLC	14,421,831	(494,177)	4.22
Morgan Stanley Investment Management Inc.	13,038,238	1,266,987	3.82
SSgA Funds Management Inc.	12,261,329	608,443	3.59
RREEF America L.L.C.	11,975,210	861,935	3.50
PGGM Vermogensbeheer B.V.	10,785,816	0	3.16

Source: SNL

PERFORMANCE



ANALYST COVERAGE

Date	Research Firm	Action	From	To
May 6, 2014	Oppenheimer	Initiated		Outperform
February 4, 2014	RBC Capital Mkts	Upgrade	Sector Perform	Outperform
January 15, 2013	Robert W. Baird	Initiated		Outperform
October 5, 2012	Miller Tabak	Upgrade	Sell	Hold
October 24, 2011	Robert W. Baird	Upgrade	Neutral	Outperform
October 24, 2011	Stifel Nicolaus	Upgrade	Hold	Buy
July 20, 2011	Deutsche Bank	Upgrade	Hold	Buy
June 21, 2011	RBC Capital Mkts	Upgrade	Sector Perform	Outperform
November 11, 2010	Barclays Capital	Initiated		Equal Weight
July 16, 2010	Robert W. Baird	Upgrade	Underperform	Neutral

Strong Buy

Buy

Hold

Underperform

Sell

Current Month

	3
	4
	8

Source: Yahoo! Finance

Company Overview

Proposed Trade

Industrial Overview

Company Overview

Valuation

Short Trade

Summary



VALUATION

Relative
Absolute
NAV

NET ASSET VALUE

GAAP NOI Cap Rate	7.58%
Economic Cap Rate	6.05%
GAAP NOI	\$ 650,856
Less: Recurring Capital Expenditures	\$ (84,545)
Adjusted NOI from Owned Properties	\$ 566,311
Divide by Economic Cap Rate	6.05%
Market Value of Owned Properties	\$ 9,360,508
Management Income	\$ 9,000
Management Cap Rate	20%
Implied Benefit of Management Income	\$ 45,000
Cash, Cash Equivalents, Securities	\$ 66,132
Receivables	\$ 194,071
Recent Acquisitions	\$ 94,032
Investments in Non-Consolidated REITs	\$ 316,015
Land Held for Future Development	\$ 542,490
Development Projects (110%)	\$ 423,288
Other Assets	\$ 692,451
Gross Market Value of Assets	\$ 11,733,987
Less: Total Liabilities	\$ 4,654,985
Less: Preferred Stock	\$ 332,794
Net Market Value of Assets	\$ 6,746,208
Divided by: Total Shares/OP Units	341,714,410

Net Asset Value per Share

\$ 19.74

Source: Duke Realty 10-Q; CBRE

COST OF CAPITAL

	Total	Weight
Total Debt Outstanding	\$ 4,208,547	37.6%
Value of Common Stock Outstanding	\$ 6,639,511	59.4%
Value of Preferred Equity	\$ 332,794	3.0%
Cost of Debt	1.7%	
Cost of Preferred Equity	8.3%	
Beta	1.04	
10 Yr. UST	2.37%	
Market Return	8.00%	
Cost of Equity	8.23%	
WACC	5.78%	

Source: Duke Realty 10-Q; Bloomberg

DISCOUNTED CASH FLOW

Five-Year Horizon
Discounted Cash Flow (\$000)

	Actual	Forecasted	Planning Period					
	2013	2014	2015	2016	2017	2018	2019	2020
AFFO	\$ 300,245	\$ 305,381	\$ 347,757	\$ 386,145	\$ 426,452	\$ 458,114	\$ 490,566	\$ 502,831
Growth Rate from Development			6.9%	6.0%	5.4%	4.9%	4.6%	0.0%
Growth Rate from Rental Increases			7.0%	5.0%	5.0%	2.5%	2.5%	2.5%
FCFF from SNL FactSet (Reference)			\$ 367,200	\$ 409,200				

Terminal Value in 2019

\$ 15,353,316

Price as of 11/10/2014	19.43
Shares outstanding as of 11/10/2014	341,714,410
Weighted Average Cost of Capital	5.78%
Terminal Growth Rate	2.50%
Annual AFFO Growth from Development	\$21,000

NPV of FCFF for years 2015-2019	\$ 1,770,708
+ NPV of Terminal Value	\$ 11,595,400
Total Present Value of FCFF	\$ 13,366,108
Less: Debt (Book Value)	\$ (4,208,547)
+ Cash	\$ 66,132
Less: Preferred Equity	\$ (332,794)
Less: Minority Interests	\$ (27,003)
= Value of Common Equity	\$ 8,863,896
Divided by # Shares Outstanding at 11/10/2014	341,714,410

Value per Share

\$ 25.94

Source: Duke Realty 10-Q and 10-K; SNL; Bloomberg

RELATIVE VALUATION



Company Name	Share Price	Price/FFO 2011	Price/FFO		Price/FFO 2014
			2012	Price/FFO 2013	(Estimated)
Duke Realty	\$19.43	12.6	13.9	13.4	16.6
Liberty Property Trust	\$35.30	12.3	14.2	13.4	14.4
EastGroup Properties	\$68.54	14.1	17.2	17.2	19.8
Prologis	\$41.41	24.6	N/A	22	22.4

	Historical Price/FFO	Current Price/FFO	Weight
Duke Realty	13.3	16.6	
Liberty Property Trust	13.3	14.4	0.4
EastGroup Properties	16.2	19.8	0.4
Prologis	23.3	22.4	0.2
Weighted Average Comparable	16.4	18.2	
Duke Realty	13.3	16.6	
= Ratio	1.24	1.09	
* Duke Realty Share Price	\$19.43	\$19.43	
Target Price	\$24.03	\$21.26	

Source: SNL



TARGET PRICE RECONCILIATION

- Weighting reflects relative confidence in valuation approaches, with slight overweight to DCF value given depth of analysis and strength of assumptions
- Analyst target prices in \$19.50 to \$20.00 range; Stifel Nicolaus increased target to \$21.00 in August 2014

	Price/Share	Weight
Relative - Historical	\$24.03	0.1
Relative - Current	\$21.26	0.2
Absolute DCF	\$25.94	0.4
NAV	\$19.74	0.3
Current Share Price	\$19.43	
Target Price	\$22.95	
Premium/Discount	-15.35%	



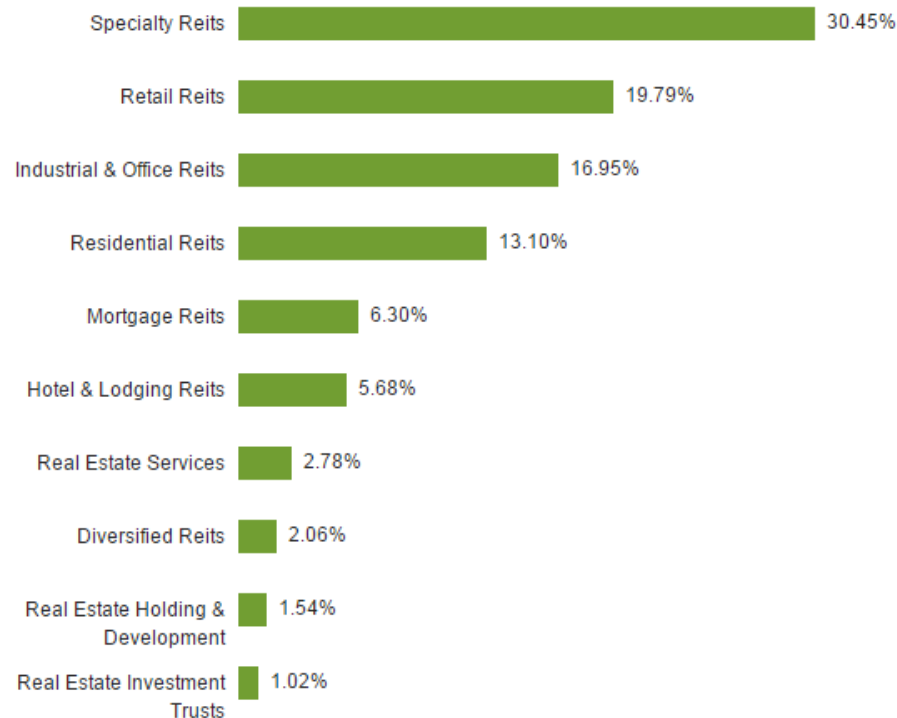
iShares[®]
by BLACKROCK[®]

SHORT TRADE

U.S. Real Estate (IYR)
Hedge Out Market Risk

ISHARES U.S. REAL ESTATE (IYR) BY BLACKROCK

Exposure to U.S. real estate companies and REITs



Top Holdings (%)

Simon Property Group REIT Inc -	7.12%
American Tower REIT -	5.17%
Crown Castle Intl. REIT -	3.75%
Public Storage REIT -	3.35%
Equity Residential REIT -	3.11%
Health Care REIT Inc -	2.82%
Prologis REIT Inc -	2.63%
AvalonBay Communities REIT -	2.58%
HCP REIT Inc -	2.54%
Ventas REIT Inc -	2.54%

DRE VS. IYR – SHARE PRICE SINCE NOV. 2011





SUMMARY

You Are What You Eat

TRADE SUMMARY

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- ❑ Projected Return: **17%**

SUMMARY OF CONCLUSIONS

1. U.S. industrial real estate will outperform all U.S. commercial real estate over next two years
 - E-Commerce
 - Trade/Infrastructure Spending
 - Supply/Demand imbalance
2. Duke Realty will outperform its peers in the industrial real estate sector over the next two years
 - Focus on bulk industrial, disposition of suburban office
 - Rent growth by raising rents to market rates as leases roll
 - NOI growth via build-to-suit development
3. Therefore, buying Duke Realty while selling the U.S. real estate market (via IYR) will yield over a **17%** return to the Carnelian Fund over the next two years

THANK YOU