From: Sellers, R Scot [RSellers@archstonesmith.com]. Sent:1/19/2008 7:40 PM.

To: Augarten, David [DAUGARTE@TishmanSpeyer.com]; Speyer, Rob [RSpeyer@TishmanSpeyer.com]; Packard, Coburn J [cpackard@lehman.com]; Walsh, Mark [mawalsh@lehman.com]; Ashmun, Robert [rashmun@lehman.com].

Cc: Mueller, Chaz [CMueller@archstonesmith.com]; Callison, Jack [jcallison@archstonesmith.com].

Bcc: .

Subject: RE: .

This isn't a complete "rebuttal" to the article, but rather a compilation of talking points that should be helpful in addressing many of the allegations in the article. We can provide more detailed information on several of the issues addressed below, including share repurchases, replacement costs, purchase of stock in another public company, etc. Please let me know what else you would like me to address, or how else I/we can be helpful. Thanks, here are some thoughts:

The principal mistake in the article is the assumption that public market share prices are in any predictive of real estate values, or represent an "efficient" market. I learned efficient market theory in business school, and it didn't take long as the CEO of a publicly traded company to realize just how wrong the public market gets valuations and even directionality from time to time. For instance, we purchased over 20% of our common stock back from 1998 through 2001 at an average price of less than $20/share, at a time when our stock traded at in excess of a 30% discount to the value of our assets. This period of time began with a similar (though not as significant) period of illiquidity in the markets (LTCM failure and Russian debt crisis) and the market overreacted by punishing real estate stocks.

Then, as now, the operating fundamentals were solid, and replacement costs were increasing, and the implicit per unit value of our portfolio (using our publicly traded share price) was at least 40% below replacement costs. Replacement costs are an especially important benchmark in supply-constrained markets, because of the difficulty of adding new supply. By definition, as demand increases in these markets, it can only be met by developing new units at replacement costs, which in turn requires rents that produce a market rate of return on these costs.

In addition to the strong operating fundamentals that exist today, we are heading into a market where very few new single family homes will be built, and the home ownership rate is likely to decrease, all of which will produce stronger fundamentals for apartments. Yes, there are some markets where there are too many condos that need to be sold (Florida, Vegas, Phoenix), but the markets we operate in have minimal "shadow" condo inventory, because it is so difficult to develop here. As a result, sharply diminished home purchases will strengthen the apartment market in the cities we operate in, and the growth rates for rents should increase significantly in coming years.

Investors understand the incredible difficulty of amassing a significant portfolio of assets in the sub-markets we operate in, and therefore, place a very high value on the ability to acquire these types of assets, at any point in the real estate cycle. There may be points in time when transactional volume is limited (due to the unavailability of debt), but this will change, and the implicit value of the assets will become obvious to the market. We are in a period of more limited transactional volume today, but there is still significant demand to purchase the assets we own at very attractive prices, and we will continue to consummate transactions with qualified buyers and partners as we move forward.

Using a comparison of public market pricing to value our portfolio may seem intuitive to someone who doesn't understand the public markets well, but it is flawed for several reasons. First, you simply could not purchase these companies today at anywhere close to current share prices. In addition to repurchasing our own common shares during the last cycle of inefficient public market prices of apartment companies, we also purchased 4.9% of another apartment company, and approached them with an overture to purchase them for cash, at a material premium to existing market pricing. The Board turned us down repeatedly, despite a very credible cash offer. Our Board was comfortable making a sizable investment in this public apartment company, because we were confident that the existing share price represented a discount of 45 to 50% compared with the true private market value of the assets. Ultimately, we sold our stake in this company for a profit of tens of millions of dollars.

Frankly, the same situation exists today, which is why even an unsubstantiated rumor about a company like Post Properties has caused its stock to trade up in the midst of a down market, because of the tremendous gap between current share prices and private market values. In addition, if you calculate the implicit per unit values of the portfolios of AVB and EQR, you will find that they are 35 to 50% below the replacement costs of their assets. Replacement costs are unlikely to come down much, if at all, due to the tremendous demand for raw materials from large construction initiatives around the world. In addition, available land is so limited in the markets we operate in, and the locations we own are equally desirable for office, retail or residential development, that land prices are unlikely to change much either.

The other thing that the article missed is the value of our platform, and our development franchise. Private real estate investors understand the tremendous value of this platform/franchise, and are willing to pay for it (whether to "rent" it, or to own it), but the public markets don't get this for some reason. When you look at the consistent value creation that a company like ASN, or AVB, has been able to create through the development of high quality assets in these supply constrained markets, over the course of many years, there is clearly tremendous value here, yet public market investors have never been willing to recognize this. That may change over time, but not only is the value of these franchises not recognized today, but the market's implicit value of these platforms is actually significantly negative today (the large discounts to NAV that exist).

The important thing to remember when faced with a situation like this is to look at longer term fundamentals. Investors who have rushed to liquidate anything in the face of an illiquid market, have always regretted these decisions. Fortunately, we have an investor group who understands long term value, and all you need to do is look at the successful NY real estate families to understand the tremendous value creation realized through long term ownership of assets in the markets we operate in. Periods of slowness are opportunities to acquire great assets at attractive prices, which we intend to do, as opportunities present themselves. Although, having said that, we don't anticipate seeing a lot of distress in the markets, due to the strong operating fundamentals in our business. In addition, as interest rates come down, this reduces the pressure on owners to sell, and since they have an understanding of replacements costs, they are more likely to just hold the assets.

From: Augarten, David [mailto:DAUGARTE@TishmanSpeyer.com]
Sent: Saturday, January 19, 2008 12:58 PM
To: Sellers, R Scot
Subject: Fw:

Here it is

----- Original Message -----
From: Altberg, Elliott
To: Galiano, Paul; Siebers, Kevin; Augarten, David; Kubiak, Riggs
Sent: Sat Jan 19 11:05:33 2008
Subject: RE:

The Barron's article...

Apartment-House Blues

By ANDREW BARY

A TOP-OF-THE-MARKET LEVERAGED BUYOUT of Archstone Smith, a leading real-estate investment trust, could prove disastrous for Wall Street firms and other equity investors in the $22 billion transaction, which closed three months ago.

What differentiates Archstone from other potentially troubled LBOs, including Chrysler, Linens 'n Things, Swift Transportation and Claire's Stores, is that Street firms could be stuck with a good chunk of the equity in the deal. In most LBOs, private-equity firms like Apollo and Blackstone provide the equity while banks and investment banks offer financing guarantees.

The Archstone situation is murky because key participants, including Tishman Speyer and Lehman Brothers <http://online.barrons.com/public/quotes/main.html?type=djn <http://online.barrons.com/public/quotes/main.html?type=djn&symbol=leh> &symbol=leh> (ticker: LEH), are saying little about the transaction other than that the company had 5%-plus rent growth in 2007 and that two property sales were completed recently at high prices. When Archstone, a leading REIT focused on the apartment market, went private, Lehman, Banc of America Strategic Ventures and Barclays Capital provided a $4.6 billion bridge-equity loan to get the deal done. Real-estate funds operated by Tishman Speyer, a prominent New York property firm, and Lehman Brothers each put up $250 million for control of the private Archstone.

It's unclear now how much of the bridge-equity loan has been sold to institutional investors. Prior to the closing of the deal, Lehman and Tishman Speyer said on a conference call that only $500 million of the bridge-equity loan was likely to be sold at closing. The duo looks to sell all the equity within a year.

Heavy Load: Privately held Archstone has five times the debt of AvalonBay, a comparable publicly traded real-estate investment trust. As a result, it faces a tougher challenge in a rocky real-estate market.

Soon after the deal got done, prices of apartment REITs, including AvalonBay Communities <http://online.barrons.com/public/quotes/main.html?type=djn <http://online.barrons.com/public/quotes/main.html?type=djn&symbol=AVB> &symbol=AVB> (AVB) and Equity Residential <http://online.barrons.com/public/quotes/main.html?type=djn <http://online.barrons.com/public/quotes/main.html?type=djn&symbol=EQR> &symbol=EQR> (EQR), fell. With apartment REITs down 30% since October, it may have proven difficult for Lehman and Tishman Speyer to sell the equity, leaving Lehman, Banc of America Strategic Ventures and Barclays stuck holding much of the bridge loan. AvalonBay, a comparable REIT, has seen its shares drop to 83 from 125 in October.

Archstone has an attractive portfolio of apartments in good markets, including Washington, Manhattan, southern California and the San Francisco Bay area. It owns a mix of desirable garden apartments and high rises.

Wall Street is concerned, however, that rent increases will slow, even in relatively strong markets. Apartment REITs also face pressure as large numbers of unsold single-family homes get rented out. Several Street analysts have cooled on apartment REITs, cutting stock-price targets and financial projections for the group.

Archstone has staying power because it raised a substantial amount of money when it went private, including $9 billion of secured loans from Fannie Mae <http://online.barrons.com/public/quotes/main.html?type=djn <http://online.barrons.com/public/quotes/main.html?type=djn&symbol=FNM> &symbol=FNM> (FNM) and Freddie Mac <http://online.barrons.com/public/quotes/main.html?type=djn <http://online.barrons.com/public/quotes/main.html?type=djn&symbol=FRE> &symbol=FRE> (FRE). Yet, based on current REIT prices, the value of the Archstone equity could be zero.

Archstone is a classic example of a good company with a bad balance sheet. It has more than $16 billion of debt, and its interest expense is running at more than $1 billion annually. Cash flow from its properties was running at just a $700 million rate in the second quarter of 2007, meaning the company is burning cash. The LBO sponsors told potential lenders in September that Archstone actually was covering its interest expense -- but that was only because of a pre-funded $500 million interest reserve.

The Bottom Line:

Archstone is burning cash and could face slowing rent increases. It may also feel pressure as unsold single-family homes are rented out. Its equity may now be zero.

In the real-estate world, properties and companies often are valued based on a capitalization rate, which essentially is the return that an all-cash buyer would get. The cap rate is calculated by taking annual net operating income and dividing it by the purchase price. Archstone's buyers accepted a low capitalization rate of about 4.3%, below the 6% interest cost on its debt.

With the selloff in REIT shares, cap rates on apartment REITs have risen to an average of 7%. The highly-regarded AvalonBay has a cap rate of around 6.3%. The lower the cap rate, the higher the value of a company.

With rising cap rates, Archstone's value probably is going down, imperiling the equity in the deal. Assume a 6% cap rate and the company would be valued at $14 billion, based on an optimistic $850 million of net operating income for this year. This would imply a wipe-out of the $5 billion of equity since the company has that $16 billion-plus in debt that takes precedence. Even the use of an aggressive cap rate of 5.5% results in no equity value.

Things could break right for Archstone if the economy recovers and apartment-REIT shares come back into favor. But those are big ifs. Archstone may end up being one of the biggest casualties of the LBO mania.

-----Original Message-----
From: Galiano, Paul
Sent: Saturday, January 19, 2008 11:00 AM
To: Siebers, Kevin; Augarten, David; Kubiak, Riggs; Altberg, Elliott
Subject: Re:

Riggs I suggest you and Elliott call Keith Cyrus now to try and schedule a call or meeting for the banks with the model team. Keith was on the bank call this morning.

----- Original Message -----

From: Siebers, Kevin

To: Augarten, David; Kubiak, Riggs; Altberg, Elliott

Cc: Galiano, Paul

Sent: Sat Jan 19 10:53:30 2008

Subject: RE:

Ok. The same article was also referenced by Barry Vinocur's REIT Wrap newsletter this morning.

From: Augarten, David

Sent: Sat 1/19/2008 7:50 AM

To: Siebers, Kevin; Kubiak, Riggs; Altberg, Elliott

Cc: Galiano, Paul

Subject:

there was a negative article in barrons this am about archstone. The banks are trying to prepare for ques from sr mgmt and want to run sensitivity analsis etc. Will be setting up a call to figure out logistics