2009 Economic and Commercial Real Estate Outlook: Too Much Pain, Too Little Gain

presented to:

Department of Defense Appraisal Conference

August 18, 2009

by

James R. DeLisle, Ph.D.
Runstad Professor of Real Estate,
Director, Graduate Real Estate Studies
Presentation Overview

• Part I: Overview and the Cause of Our Disconnect

• Part II: Economic and Capital Markets

• Part III: Real Estate Capital Markets

• Part IV: Commercial Real Estate Market Update

• Part V. Implications for Real Estate Professionals
# DOD Conference Survey Respondent Profile

Click for annotation

## 1. Please indicate the branch of the service with which you are affiliated.

<table>
<thead>
<tr>
<th>Branch</th>
<th>Response</th>
</tr>
</thead>
<tbody>
<tr>
<td>Army</td>
<td></td>
</tr>
<tr>
<td>Navy</td>
<td></td>
</tr>
<tr>
<td>Other, please specify</td>
<td></td>
</tr>
</tbody>
</table>

View Responses
Three Major Attributes of Real Estate

Three major attributes of real estate . . .

- L,  
- L,  
- L,  
- L.  

The new regime of real estate . . .

- D . . . . . . . istressed,  
- D . . . . . . . istressed,  
- D . . . . . . . istressed.
Commercial Distressed Assets in US

(as of August 2009)

Source: Real Capital Analytics
The Three C’s of our Disconnect

- Credit Crisis
  - Easy Credit
  - Cheap Credit
  - Plentiful Credit

- Crisis of Confidence
  - Consumer Confidence
  - Corporate Confidence

- Crisis of Collateral
  - Value attributable to delinking spatial market/capital market
  - Values correction as “marked to market”
  - Re-pricing of Risk
Real Estate Cycles & Spatial/Capital Disconnect

Key Questions: Where are we? Where is bottom? When?
### Part II: The Economic and Capital Markets

**Survey Results:**
Source: DOD Appraisal Conference Attendees

<table>
<thead>
<tr>
<th>Statement</th>
<th>Strongly Agree</th>
<th>Neither</th>
<th>Strongly Disagree</th>
</tr>
</thead>
<tbody>
<tr>
<td>Emerging from Recession</td>
<td>0%</td>
<td>20%</td>
<td>27%</td>
</tr>
<tr>
<td>Employment Get Better</td>
<td>0%</td>
<td>0%</td>
<td>13%</td>
</tr>
<tr>
<td>Credit Won’t be Problem</td>
<td>0%</td>
<td>0%</td>
<td>20%</td>
</tr>
<tr>
<td>Consumers will be back</td>
<td>0%</td>
<td>0%</td>
<td>67%</td>
</tr>
<tr>
<td>Commercial RE Rebound</td>
<td>0%</td>
<td>0%</td>
<td>40%</td>
</tr>
<tr>
<td>Bailout/Stimulus Focused on CRE</td>
<td>0%</td>
<td>0%</td>
<td>20%</td>
</tr>
<tr>
<td>Housing Bottomed Out</td>
<td>0%</td>
<td>0%</td>
<td>27%</td>
</tr>
<tr>
<td>Fed Work by Year-End</td>
<td>0%</td>
<td>0%</td>
<td>27%</td>
</tr>
<tr>
<td>CRE Not Collapsing</td>
<td>0%</td>
<td>0%</td>
<td>40%</td>
</tr>
<tr>
<td>CRE Bottomed Out</td>
<td>0%</td>
<td>0%</td>
<td>21%</td>
</tr>
</tbody>
</table>

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Employment Losses Slowing, Hours Increasing

Net Employment losses

Hours Worked Rising?

Who’s Next: Who’s Left?

Source: economy.com

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Some Good News: Manufacturing & Autos

Business Spending

Cash for Clunkers….

Source: economy.com
Global and Domestic Business Confidence

U.S. Business Confidence

Some improvement....

G3: Global Confidence

Source: economy.com
Inventories and Capacity Utilization

Inventory Reductions Slowing

Capacity Utilization

Source: economy.com
Consumer Confidence, Spending & Credit

Consumers Contracting

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**Consumers Are Very Jittery...**

*University of Michigan sentiment index, 1966Q1=100*

![Graph showing consumer sentiment over time](graph.png)

**Source:** Univ. of Michigan

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**A Credit Crunch**

*Change year ago in household debt outstanding, $ bil*

![Graph showing changes in household debt](debt_graph.png)

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**Sales Have Barely Bumped Since December**

*Retail sales*

![Graph showing retail sales over time](sales_graph.png)

---

**Obama to prod credit card firms on fee practices**

WASHINGTON, Apr. 23, 2009 (Reuters) — President Barack Obama will weigh in on Thursday on the lending practices of U.S. credit card companies, an issue that has triggered an outcry from consumers hit with high fees and interest rates. ... > full story
Interest Rates, Mortgage Rates

Fed Funds Rate

Recent Mortgage Rates

<table>
<thead>
<tr>
<th>Interest Rate</th>
<th>YIELD/RATE (%)</th>
<th>52-WEEK High</th>
<th>52-WEEK Low</th>
<th>CHANGE IN PCT. PTS 52-Wk 3-Yr</th>
</tr>
</thead>
<tbody>
<tr>
<td>30-year mortgage, fixed</td>
<td>5.32</td>
<td>6.61</td>
<td>5.30</td>
<td>-0.22 -0.39</td>
</tr>
<tr>
<td>15-year mortgage, fixed</td>
<td>4.95</td>
<td>6.22</td>
<td>4.90</td>
<td>-0.09 -0.35</td>
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<tr>
<td>Jumbo mortgages, $417,000-plus</td>
<td>6.75</td>
<td>7.89</td>
<td>6.49</td>
<td>0.16 0.74</td>
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<tr>
<td>Five-year adj mortgage (ARM)</td>
<td>5.66</td>
<td>6.14</td>
<td>5.01</td>
<td>0.40 0.34</td>
</tr>
<tr>
<td>New-car loan, 48-month</td>
<td>7.10</td>
<td>7.14</td>
<td>6.45</td>
<td>0.11 0.63</td>
</tr>
<tr>
<td>Home-equity loan, $30,000</td>
<td>5.18</td>
<td>6.85</td>
<td>4.64</td>
<td>-1.67 -0.81</td>
</tr>
</tbody>
</table>

Mortgage Spreads

FHLMC: 30-Yr. Average conventional commitment rate - Fixed Rate, (%)

Source: economy.com
Housing Activity and Delinquency Rates

**Construction**

New residential construction, mil, SAAR

- Permits
- Starts

**Delinquency & Default**

Year-over-year difference in first mortgage, % of dollar volume, basis points

- 30-day
- 60-day
- 90-day
- 120-day

Sources: Equifax, Moody's Economy.com

**Housing Index**

Modest Gains Suggest New-Home Sales Have Bottomed
NAHB housing market index, SA

- Future sales
- Present sales
- Buyer traffic

**Distress Sales Play a Smaller Role**

Pending home sales, % change year ago

- West
- South
- Northeast
- Midwest

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Single-Family Market: Prices Peak - Current

S&P/Case-Shiller U.S. National Home Price Index

% Change Index

Index

Sources: Standard & Poor’s and Fiserv. Data through 2008Q3.

S&P/Case-Shiller Home Price Indices

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<th></th>
<th>10-City</th>
<th>20-City</th>
<th>National</th>
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<tr>
<td>Peak date</td>
<td>Jun-06</td>
<td>Jul-06</td>
<td>2006Q2</td>
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<tr>
<td>Peak level</td>
<td>226.29</td>
<td>206.52</td>
<td>189.93</td>
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<tr>
<td>Decline since peak</td>
<td>-25.0%</td>
<td>-23.4%</td>
<td>-21.0%</td>
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<tr>
<td>Decline in the last 12 months</td>
<td>-19.1%</td>
<td>-18.0%</td>
<td>-16.6%</td>
</tr>
</tbody>
</table>

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Delinquency and Loan Charge-Off Rates

Loan Charge-Off Rates to Rise

Delinquency Rates

Residential Foreclosures

Source: economy.com
## Business Cycles: An Historical Comparison

### U.S. Business Cycles Since World War II

**Peak-to-trough % change**

<table>
<thead>
<tr>
<th>Peak</th>
<th>Trough</th>
<th>Real GDP</th>
<th>Industrial Production</th>
<th>Nonfarm Employment</th>
<th>Jobless Rate</th>
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<tbody>
<tr>
<td></td>
<td></td>
<td>Low</td>
<td>High</td>
<td>Change</td>
<td>Low</td>
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<tr>
<td>Dec. 2007</td>
<td>Sept. 2009</td>
<td>-3.9%</td>
<td>-19.2%</td>
<td>-5.5%</td>
<td>4.4%</td>
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<tr>
<td>Mar. 2001</td>
<td>Nov. 2001</td>
<td>-0.4%</td>
<td>-6.3%</td>
<td>-2.0%</td>
<td>3.8%</td>
</tr>
<tr>
<td>July 1990</td>
<td>Mar. 1991</td>
<td>-1.3%</td>
<td>-4.3%</td>
<td>-1.5%</td>
<td>5.0%</td>
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<tr>
<td>July 1981</td>
<td>Nov. 1982</td>
<td>-2.9%</td>
<td>-9.5%</td>
<td>-3.1%</td>
<td>7.2%</td>
</tr>
<tr>
<td>Jan. 1980</td>
<td>July 1980</td>
<td>-2.2%</td>
<td>-6.2%</td>
<td>-1.3%</td>
<td>5.6%</td>
</tr>
<tr>
<td>Nov. 1973</td>
<td>Mar. 1975</td>
<td>-3.1%</td>
<td>-14.8%</td>
<td>-2.7%</td>
<td>4.6%</td>
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<tr>
<td>Dec. 1969</td>
<td>Nov. 1970</td>
<td>-1.0%</td>
<td>-5.8%</td>
<td>-1.4%</td>
<td>3.4%</td>
</tr>
<tr>
<td>Apr. 1960</td>
<td>Feb. 1961</td>
<td>-1.3%</td>
<td>-6.2%</td>
<td>-2.3%</td>
<td>4.8%</td>
</tr>
<tr>
<td>Aug. 1957</td>
<td>Apr. 1958</td>
<td>-3.8%</td>
<td>-12.7%</td>
<td>-4.4%</td>
<td>3.7%</td>
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<tr>
<td>July 1953</td>
<td>May 1954</td>
<td>-2.7%</td>
<td>-9.0%</td>
<td>-3.3%</td>
<td>2.5%</td>
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<tr>
<td>Nov. 1948</td>
<td>Oct. 1949</td>
<td>-1.7%</td>
<td>-8.6%</td>
<td>-5.1%</td>
<td>3.4%</td>
</tr>
</tbody>
</table>

**Average**

- Real GDP: -2.0%
- Industrial Production: -8.3%
- Nonfarm Employment: -2.7%
- Jobless Rate Low: 4.4%
- Jobless Rate High: 7.6%
- Change: 3.2%

**Sources:** NBER, BEA, FRB, BLS, Moody’s Economy.com

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**The Future Remains Uncertain**

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Bailout # 1: TARP

- Troubled Asset Relief Program (TARP)
  - When: Early Fall 2008
  - Objectives: stabilize financial institutions & provide liquidity & restore business and consumer confidence
  - Funding
    - $700 billion Bailout (?) Budget
    - $250 b to take equity-like positions in financial institutions
    - Purchase commercial paper; changed to Capital Purchase Program (CCP)

- What Happened?
  - Current Scandals
    - Special Inspector General for the Program
    - On April 20th, announced some 20 Probes of Bailout for Fraud, Trading
Banks Want Out of Tarp

Intend to Stay

How TARP-Funded Warrants Work

Banks that intend to stay in the Troubled Asset Relief Program

The Treasury provides capital to the troubled bank.

When the bank’s shares are trading above the strike price, the Treasury can exercise the warrants. The payoff is the difference between the share price and the strike price.

In exchange, the government gets warrants, or options to buy shares in the company at a fixed price, known as the strike price, some time in the future.

If the share price remains lower than the strike price, the government gets no payoff.

Want to Give Back $

Banks that want to leave TARP

The bank must provide the Treasury with an independent valuation of the warrants.

The Treasury and the bank must agree on the price. If they can’t, Treasury must try to sell the warrants into the private market.

One problem undermining the Treasury’s effort to revamp the TARP program is the limitation of existing oversight. A report issued Tuesday by the TARP’s special inspector general, for example, suggested firms could game a federal program designed to deal with illiquid bank assets. “The significant government-financed leverage presents a great incentive for collusion…whereby, once again, the taxpayer takes a significant loss while others profit,” said the report from Special Inspector General Neil Barofsky.

J.P. Morgan, Goldman Sacks
Bailout # 2: TALF & CMBS….

• When: 2009
  – Expand Term Asset-Backed Security Loan Facility (TALF) to allow the posting of both new and legacy MBS
  – Both commercial MBS (“CMBS”) and residential MBS (“RMBS”) collateral.

• Objectives
  – Consumer: insure the debt if a borrower defaults
  – Backing the backers, the Treasury department will provide $200 b
  – Real-Estate Industry Pushes Fed to Lengthen TALF Terms
Financial Stability Plan: April 2009

• Financial Stability Trust
  – A Comprehensive Stress Test for Major Banks
  – Increased Balance Sheet Transparency and Disclosure

• Capital Assistance Program
  – Public-Private Investment Fund ($500 Billion - $1 Trillion)
  – Consumer and Business Lending Initiative (Up to $1 trillion)

• Initiatives
  – Transparency and Accountability Agenda
  – Affordable Housing Support and Foreclosure Prevention Plan
  – A Small Business and Community Lending Initiative
TALF Safety Net Extended for Commercial RE

• Extension
  – The Federal Reserve is extending its Term Asset-Backed Security Loan Facility, which would have expired this year.
  – Objective: keep safety net up for commercial real estate and help roll over loans

• Size of Market
  – Some $3.5 trillion in commercial real estate loans
  – March 08- August 09: Only $30 billion of $1 trillion lent
  – Commercial RE likely to stress reserves over next several years
IMF Global Financial Stability Report

- Global credit crunch will be “deep and long-lasting”
- More bank writedowns are coming
  - Raised $900 b in new capital since crisis; loses of $2.8 trillion
  - US banks had over $500 billion write-downs, may double by 2010
- The Next Fix: Capital Infusion: by end of 2010
  - US $275 billion
  - Euro area $375 billion
  - UK $125 billion
  - Other Developed $100 billion
- Conclusion
  - Not all banks bad,
  - but a lot of bad banks
Part III: Real Estate Capital Markets

Macro-economic Environment

- Economy tottering with risk of recession
- Businesses struggling, stock market volatile
- Consumers bearish

Real Estate Capital Market

- Wavering, delayed investor demand
- Rising Cap rates, declining values
- Challenge in de-levering asset class
Where on Real Estate Market Cycle?

<table>
<thead>
<tr>
<th>Strongly Agree</th>
<th>Neither</th>
<th>Strongly Disagree</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Commoditized Pricing Out</strong></td>
<td>8%</td>
<td>38%</td>
</tr>
<tr>
<td><strong>No trouble Refinancing</strong></td>
<td>7%</td>
<td>29%</td>
</tr>
<tr>
<td><strong>Sellers Unrealistic</strong></td>
<td>7%</td>
<td>13%</td>
</tr>
<tr>
<td><strong>Fundamentals Declining</strong></td>
<td>20%</td>
<td>6%</td>
</tr>
<tr>
<td><strong>Cap Rates Too Low Yet</strong></td>
<td>13%</td>
<td>6%</td>
</tr>
<tr>
<td><strong>Recent Comm’l RE Bubble</strong></td>
<td>21%</td>
<td>7%</td>
</tr>
<tr>
<td><strong>Dev Back Next Year</strong></td>
<td>13%</td>
<td>40%</td>
</tr>
<tr>
<td><strong>More Erosion in NOI</strong></td>
<td>13%</td>
<td>40%</td>
</tr>
<tr>
<td><strong>Transaction Volume Low</strong></td>
<td>13%</td>
<td>73%</td>
</tr>
<tr>
<td><strong>RE Underperform 2 yrs.</strong></td>
<td>7%</td>
<td>47%</td>
</tr>
</tbody>
</table>

Source: DOD Appraisal Conference Attendees
Economic and Real Estate Turnaround

Economy Turnaround

Real Estate Turnaround

Source: DOD Appraisal Conference Attendees
National Recession and Real Estate

Turning to the economic environment, we can start with some good news that is quickly overwhelmed with some of the bad news. In response to the question of...
Size and Trends in Distressed Assets in US

Trends in Distressed Assets

Magnitude of Distressed Assets

Cumulative Distressed Assets

(as of July 2009)

Source: Real Capital Analytics
Distressed Asset Leakage: Cannibalization

Sources: RCA, WSJ 4/21/2009
Commercial Real Estate: How we Got Here

[Graph showing total return and value change over time with various events labeled, including ERISA, Tax Reform, NCREIF, Tax Recovery: ACRS, RE Collapse, Thrifts Collapse, RTC, UPREITs, CMBS, 9/11, Recession, Defensive Capital $’s, and year markers from 1974 to 2005.]
## Four Quadrant Investing

### Private vs. Public

<table>
<thead>
<tr>
<th>Equity</th>
<th>Public</th>
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<tr>
<td>Individual / Owship</td>
<td>Equity REITS</td>
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<tr>
<td>Pension Funds / Funds</td>
<td>Real Estate Corporations</td>
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<tr>
<td>Partnerships, Ventures</td>
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</table>

<table>
<thead>
<tr>
<th>Debt</th>
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<tbody>
<tr>
<td>Commercial Mortgages</td>
</tr>
<tr>
<td>Residential Mortgages</td>
</tr>
<tr>
<td>Mezzanine Debt</td>
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<table>
<thead>
<tr>
<th>Debt</th>
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</thead>
<tbody>
<tr>
<td>Commercial</td>
</tr>
<tr>
<td>Mortgage-backed</td>
</tr>
<tr>
<td>Securities (CMBS)</td>
</tr>
<tr>
<td>Mortgage REITs</td>
</tr>
</tbody>
</table>

### Second Generation Holistic Portfolio Management

```
Non-Core
International
Commercial Mortgages
REITs
Securitized Products
```

```
Aggregate First Generation Portfolio
Open-end Fund 1
Open-end Fund 2
Closed End Fund 1
Closed End Fund 2
Specialty Fund
Core
```

```
Aggregate Second Generation Portfolio
```

---

*Real Estate Finance*

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What Happened: Commoditization of Pricing

Market Risk/Return Long-Term

Recent: Risk/Return 5 yrs
How We’re Doing: Opportunistic Funds

Not Asset Allocate at these IRRs

Source: NCREIF

Net Assets
Opportunistic $211,622 M
Core $455,317 M
Value-Added Closed-end 9%
Operational 10%

Gross Real Estate
Opportunistic 57%
Core 25%
Value-Added Closed-end 10%
Value Added 8%

Leverage

Source: 2009 Emerging Trends
How We’re Doing: Institutional Real Estate

Recent NCREIF Index

Source: NCREIF

DOD Value Losses

Source: DOD Appraisal Conference Attendees

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# 2009-2010 Cap Rate Expectations

<table>
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<tr>
<th></th>
<th>6.0</th>
<th>6.5</th>
<th>7.0</th>
<th>7.5</th>
<th>8.0</th>
<th>8.5</th>
<th>9.0</th>
<th>9.5</th>
<th>10</th>
<th>10+</th>
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<tbody>
<tr>
<td><strong>Core</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
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<td></td>
<td></td>
<td></td>
<td></td>
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</tr>
<tr>
<td>Current</td>
<td>1</td>
<td>0</td>
<td>1</td>
<td>3</td>
<td>2</td>
<td>2</td>
<td>3</td>
<td>1</td>
<td>0</td>
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<tr>
<td></td>
<td>8%</td>
<td>0%</td>
<td>8%</td>
<td>23%</td>
<td>15%</td>
<td>15%</td>
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<td>8%</td>
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<tr>
<td>Feb 2010</td>
<td>1</td>
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<td>1</td>
<td>3</td>
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<td></td>
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<td>23%</td>
<td>8%</td>
<td>8%</td>
<td>31%</td>
<td>0%</td>
<td>15%</td>
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<td><strong>Value-add</strong></td>
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<tr>
<td><strong>Distressed</strong></td>
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Source: DOD Appraisal Conference Attendees
How Cap Rates & NOI Impact Value

What if Cap Rate Increases From 6.25% to 7.75%?

What Value impact on $100,000 NOI?

What if NOI down 10%?

4.6% NCREIF Apartment Cap in 2008!

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The Global Fundamentals: Cap vs. Vacancy

Cap Rates and Vacancies for Office Properties

Global Trends in Yields/Cap Rates

Source: Real Capital Analytics
Global Capital Flows: Before the Storm

ORIGINS OF PROPERTY BUYERS
PERCENT OF ACQUISITIONS

*GCC (Gulf Cooperation Council): Bahrain, Kuwait, Oman, Qatar, Saudi Arabia, United Arab Emirates

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Risk-Tolerances: Investor Appetites

Merrill Lynch Fund Manager Survey

Goldman Sachs Risk Tolerance Survey

IMF Global Financial Stability Report
Bid/Ask Spread: Trends and Value Pressures

- **Bid/Ask Compression**
  - Distressed Sellers
  - Distressed Assets

- **Mark-to-Market Accounts**
  - NCREIF - 28% w/o Distressed Sales
  - Going Forward: Three Strikes
    - Comps Down as Assets Dumped
    - NOI Erosion, Vacancy & Rents
    - Wcc: Debt & Equity Yields Up
Commercial Leverage: Problems & Implications

• Easy Credit
  – DCRs: lowered; eased via bullets: 3, 5, 10 yrs
  – LVs: Record values, financial engineering
  – Loose, non-recourse debt

• Outlook for Commercial Debt
  – Limited supply; flight to quality
  – Tighter; increased equity and recourse

Coming Attractions
Commercial, Industrial and RE Credit

Commercial and Industrial Loans Tight

Difficult Credit Conditions Will Slow the Recovery

Net % of banks tightening standards for C&I loans (L)

Real GDP, % change year ago (R)

Commercial RE Lending Standards Tightening

Fed Keeping Close Eye on Commercial Real Estate
Net % of banks tightening standards

Commercial real estate loans
Institutional Equity Capital Flows

• **Investment Preferences**
  – Search for Value; eschew risk
  – Fewer products/structures

• **Timing**
  – Patient; waiting for bottom
  – Indecisive; slower to act

• **Decreased capital flows**
  – Rising Return/Yield hurdle
  – Denominator effect

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Source: 2009 Emerging Trends
Trends in Commercial Transaction Activity

Monthly Sales Volume: Pre-Credit, Post-Credit, Post Financial/Recession

Percent Change Sales Volume: Pre-Credit, Post-Credit, Post Financial/Recession
Part IV: The Spatial Market

Macro-economic Environment
- Economy tottering with risk of recession
- Businesses struggling, stock market volatile
- Consumers bearish

Real Estate Capital Market
- Wavering, delayed investor demand
- Rising Cap rates on private side
- Challenge accessing equity and recourse debt

Spatial Market
- Fundamentals continue to weaken mirroring economy
- Vacancy rates rising, rents softening
- Stagnating demand, tempered recovery
Part III: Commercial Market Fundamentals

Vacancy Rates

Source: Torto Wheaton Research, REIS, 2009 Emerging Trends

Development (msf)
Institutional Cap Rate: NCREIF Income Returns

Total Returns by Property Type

Implicit Cap Rates by Property Type

Source: NCREIF
Sales Volume by Property Type

2008 US Sales Volume by Property Type

- OFF CBD
- OFF Suburban
- APT Garden
- APT Mid/High Rise
- IND Warehouse
- IND Flex
- HOT Full Service
- HOT Limited Service
- RET Strip Center
- RET NNN

Click for annotation

Change in Volume vs. 2007

Portfolio
One off

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Distressed Assets by Property Type and Subtype
Growth in Distressed Assets by Property Type

- **Office**
- **Apartment**
- **Retail**
- **Hotel**
- **Industrial**
Part V: Implications for Real Estate Professionals

Opportunities for Investment

- Acquisition
  - Cash Purchases
  - Structured Debt

- Promoted Equity Positions
  - Entitled, not started
  - In Development, not finished
  - Capital Needs: TIs, CapX

- Distressed
  - Properties
  - Debt
  - Owners
  - Tenants

Stalled in Seattle

But we’re number 1……..
Opportunities for Service Providers

• Mortgagees: Outsourced Services
  – REO Management
    • Troubled Asset Dispositions
    • Convertible Loans/Equity Kickers.JVs
  – REO Avoidance
    • Workout Restructured Loans
    • Pre-foreclosure Settlements

• Asset Management Takeovers: Investors
  – Asset/Portfolio Mgmt Holds
  – Asset Liquidation/Disposition

• TIC Counseling Services
  – Workouts/Arbitration
  – Disposition/Liquidation/Refinance
Biggest Risks in Commercial Real Estate

- **Capital**
  - Access to Debt
  - Access to Equity

- **Refinancing**
  - Bullet Mortgages
  - New Loans, Good Real Estate

- **Tenant Disruptions**
  - Panic
  - Waive of Bankruptcies

- **National Economy**
  - Recession
  - Credit Freeze

- **Real Estate Fundamentals**
  - Weakening occupancy
  - Rising Vacancies
  - Overbuilding continues

- **Transactions**
  - Sellers unrealistic
  - Tenants non-committal
  - Buyers on fence

Source: DeLisle's 2008-09 Surveys
What Will it Take to Turn it Around?

• Nothing
  – Buyers & sellers not adjusted
  – Time will cure

• Economy
  – Jobs, employment
  – Economic Growth
  – Consumer Confidence
  – Business Confidence
  – Global Recovery

• Credit
  – Access; get the money out
  – Refinancing Source
  – Healthy Banks

• Clear Distressed Backlog
  – Properties
  – Debt
  – Owners
  – Tenants

• Government Incentives
  – Recapitalization
  – Stabilization

• Perfect Storm (Stars Aligned)
  – Stimulus Money Flows
  – Confidence rises
  – Credit Flows

Source: DeLisle’s 2008-09 Surveys
DOD Respondent Opportunities & Challenges

Opportunities

- **Leases**
  - Lease renegotiations
  - Static or reduced commercial rents
  - Concessions in form of free rent and buildouts
  - Lease rollovers
- **Acquisitions**
  - Lower acquisition prices
  - Opportunities to acquire large tracts near installations

Challenges

- **Valuation**
  - Valuing assets in distressed markets
  - Valuing assets in falling markets
- **Usage Decisions**
  - Determining Highest & Best Use
  - Factoring in anti-terrorism protection
- **Staffing**
  - Hiring and staffing qualified appraisers
  - Reacting to quickly changing workloads
Major Worries for DOD Attendees

• Commercial Market
  – Increasing commercial vacancy rates; oversupply of space
  – Commercial market collapse
  – Deterioration in values
  – Market price declines due to distressed property sales

• Capital Flows
  – Tight commercial finance
  – Bank failures Too much speculation

• Economy
  – Rising interest rates
  – Increasing unemployment National debt to foreign sources

• Residential
  – Blight in residential communities
  – Residential rebound too quick
Topics DOD Attendees Want to Address

• Valuation
  – Commercial property valuation
  – Outlook for commercial market fundamentals
  – Market value vs. liquidation/distressed value

• Economy
  – The economy and impact on real estate
  – Will stimulus programs work?
  – Role of US currency and the Fed in the economy
  – How can deficit spending continue?

• Local Markets
  – Housing value trends
  – Local market conditions: residential and commercial
Lessons Learned

- Recapitalization = Recapitulation
- Reconnection Capital and Spatial Critical to Stability
- Securitization not a Panacea
- Financial Engineering not Sustainable
- Not all Distress is Created Equal
  - Properties
  - Borrowers
  - Markets
- Market Timers: Value-Add vs. Opportunistic vs. Vulture
- Interventions and Unintended Consequences
Where to Turn

"Stress Management: Approaches for preventing and reducing stress" — Learn techniques to reduce the stress in your life with this special report from the experts at Harvard Medical School. 30% off the cover price and free shipping for SmartBrief readers. Click here to order in hard copy or electronic download.

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