



Note. This PDF is annotated. Click on the icon to the left on each page to view them. Right click and resize to read them or just scroll down. JRD



2010 Real Estate Outlook: To Walk, To Talk, To Walk the Talk?

presented to:

WASCAR Education Day: 2009

Washington State Commercial Association of REALTORS®

October 22, 2009

by
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Runstad Professor of Real Estate & Director, Graduate Real Estate Studies



Presentation Overview



I: Outlook 2008 Review and New Industry Challenges

II: Economic and Capital Markets

III: Real Estate Capital Markets

IV: Commercial Real Estate Market Update

V: Implications for Seattle Real Estate Market



Part 1: 2008 Outlook Grade and Challenges

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



RUNSTAD CENTER FOR REAL ESTATE STUDIES

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The Risk Management Process

Types of Risks in Real Estate

Political Prognostication: Obama & Rossi

Part I: Economic Growth & Recession?

Rising Unemployment

Falling Business Indicators & Confidence

Global Contagion: Diffusion of Credit

Stock Market: 10,000 + 2yrs

Crisis on Wall Street: East to West Coast

Consumer Confidence, Spending & Credit

Low Inflation & Interest Rates

Continued Housing Crisis & Foreclosures

Part II: Capital Markets & Submerging Trends

Institutional RE Investment: An Historical Look

Valuation: Spatial Balance, Capital Surplus

Capital/Spatial Divide: Commoditization

Institutional Cap Rates: Today 6.5 -2yr 7

Commercial Leverage: Problems & Implications

Institutional Capital Flow Declines

Part III: Real Estate Market Fundamentals

Rise in Vacancies, Decline in Development

Office, Retail, Apartment, Industrial & Hotel Real Estate



2008 Outlook: Issues & Opportunities

Government Intervention

Will Government Intervention Work? Yes, No, Maybe So....

What More Should Government Do? Nothing to Everything

National Real Estate Outlook

Seattle CBA on National Market Trends/Issues; Generally Agree with National Poll

National: Greatest Risks to Commercial RE? Debt, Refinance, Fundamentals, Values

National: Greatest Opportunities? Cash, Debt, Distress, Value Creation

Seattle Real Estate Assessment

Seattle's Economy and Real Estate: Guarded, Many Concerns, Need to Change

Seattle as an Institutional Market: It Matters and Struggles on Price/Performance

Seattle Commercial RE: What's Happening/Not?

Who's Hurting? Who's Not?

Seattle Real Estate Outlook

Biggest Risks in Seattle? Employment, Infrastructure, Economy, Capital, Fundamentals

Biggest Opportunities in Seattle? None, Services, Core, Distress, Cash

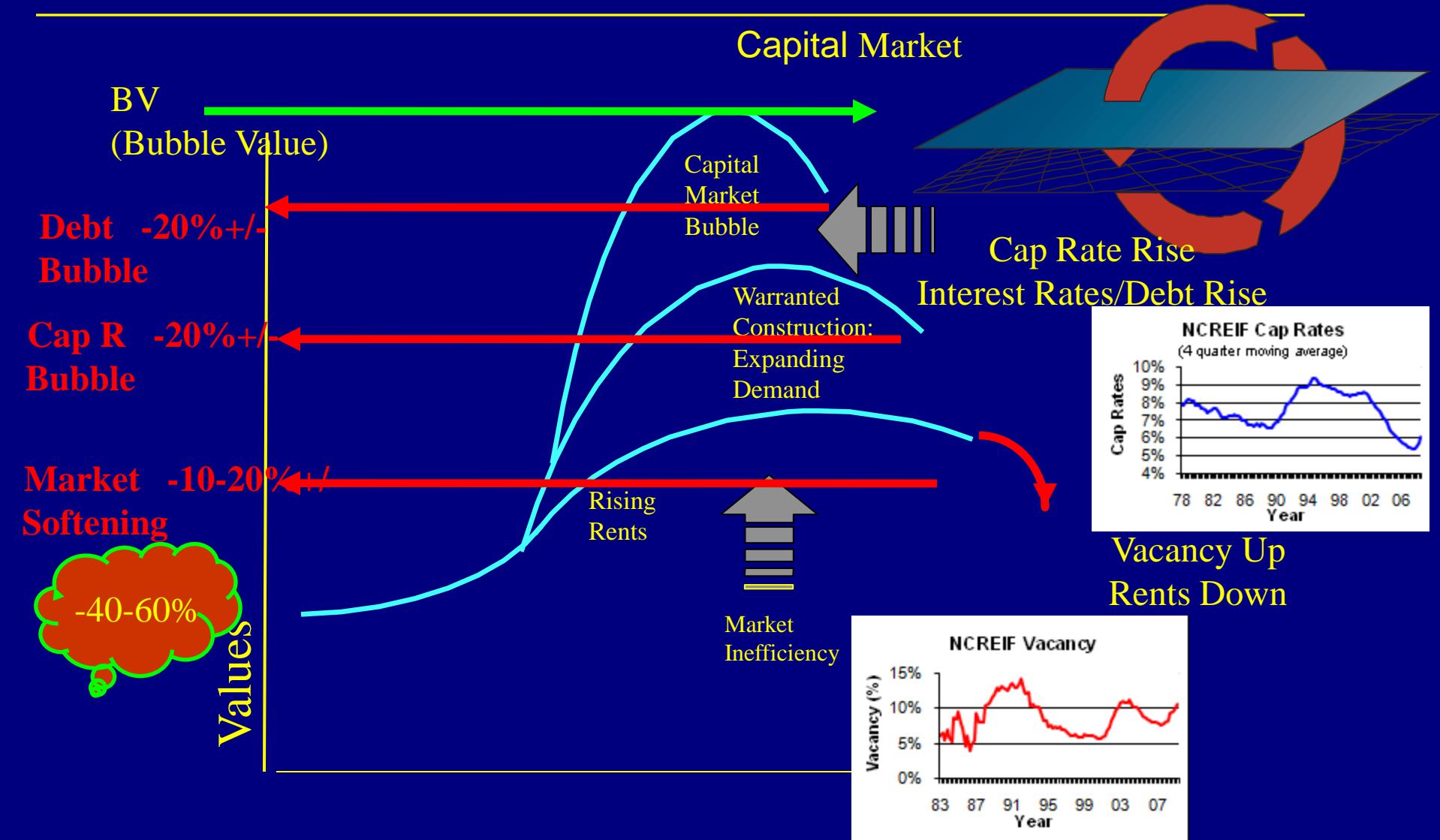
Key Topics of Interest? RE Outlook, Capital Markets, Seattle

Difference? What to do, what learned?



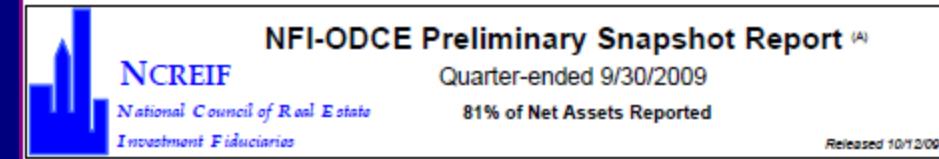
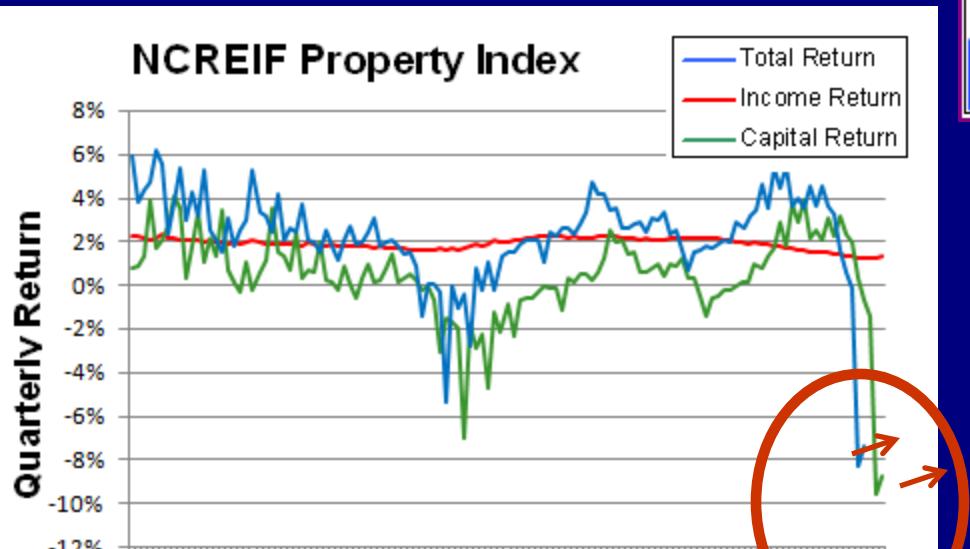
Spatial & Capital Market Re-connect

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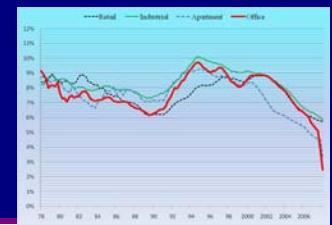
How We're Doing: Institutional Real Estate



The Good News....
It's not as bad as it was

The ‘Bad News’

Implicit Cap Rates
200bp below averages



	Current Qtr Estimate	Previous Qtr Actual	Change	1 Year	3 Years	5 Years	10 Years	SI (B) (31.75 Years)
Income	1.59%	1.53%	0.06%	5.7%	5.3%	5.7%	6.9%	7.8%
Appreciation	-8.96%	-10.53%	1.57%	-39.1%	-12.4%	-3.5%	-1.1%	0.2%
Total, Gross of Fees (C)	-7.41%	-9.03%	1.62%	-35.3%	-7.6%	2.1%	5.7%	8.0%

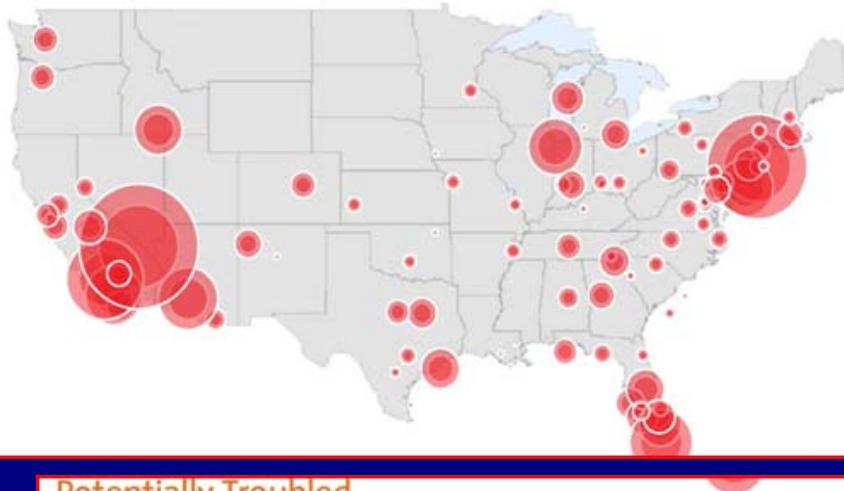


Distressed Real Estate Asset Profile

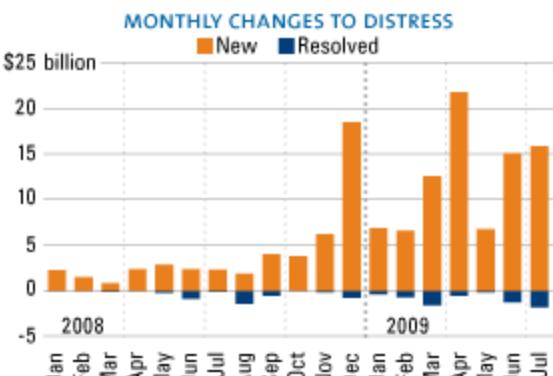


Status and Location

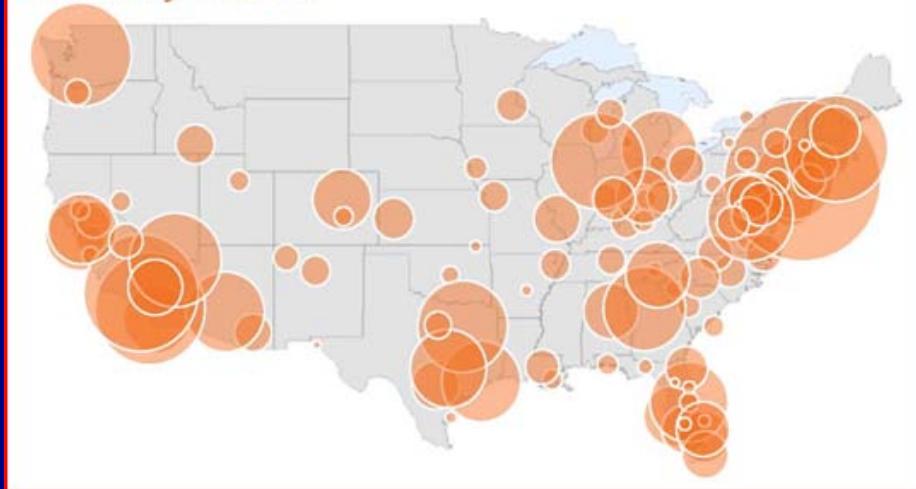
Distressed



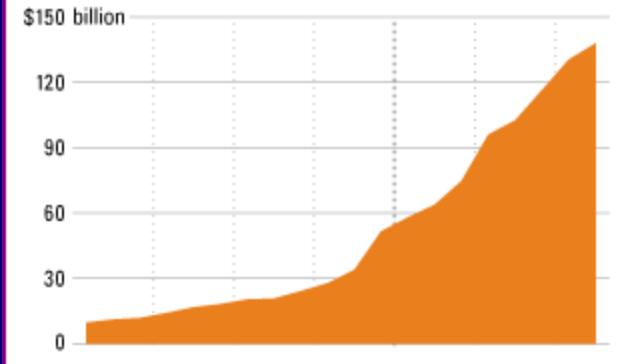
Growth & Build-up



Potentially Troubled



TOTAL OUTSTANDING DISTRESS

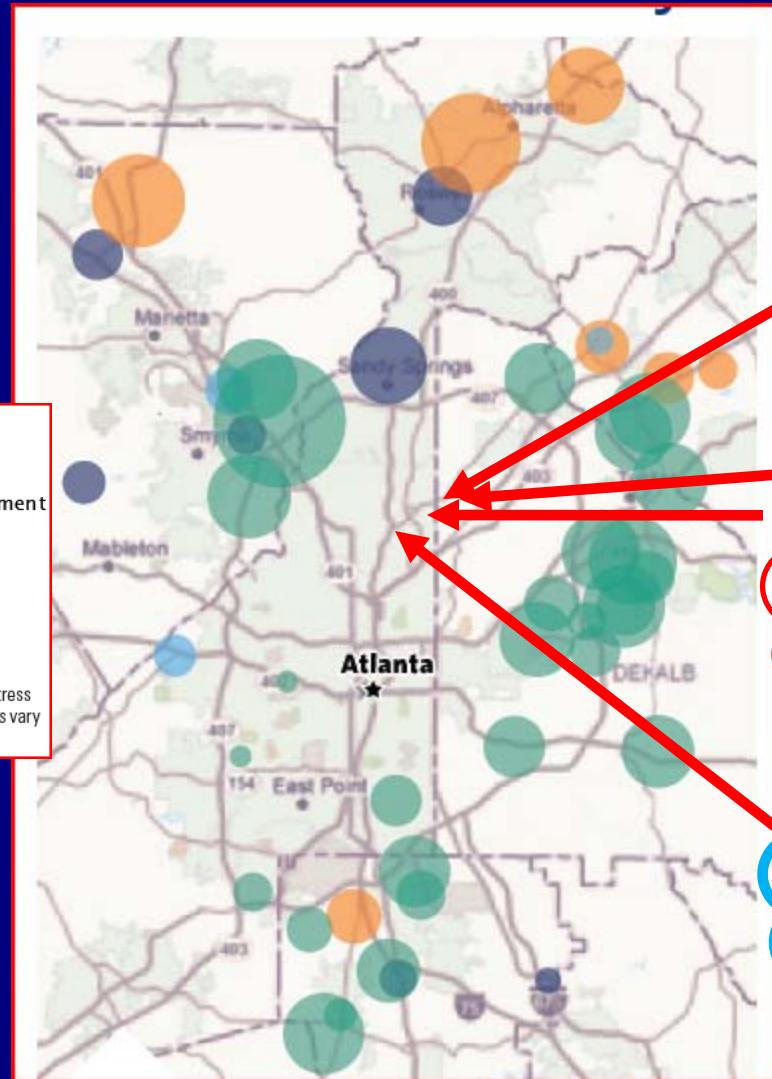


Source: Real Capital Analytics

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Distressed Asset Spillover: Tenant Cannibalization





Challenges & Three Attributes of Real Estate



Three major attributes of real estate . . .



. vulnerable,

- L,
- L,
- L.



. vulnerable,



. vulnerable.

The 2009 regime of real estate . . .

- D stressed,
- D stressed,
- D stressed.

The 2010 + regime of real estate . . . **L, L, L**

Butt, what the “L”?

Liability, Litigation, Liquidity (NOT!)

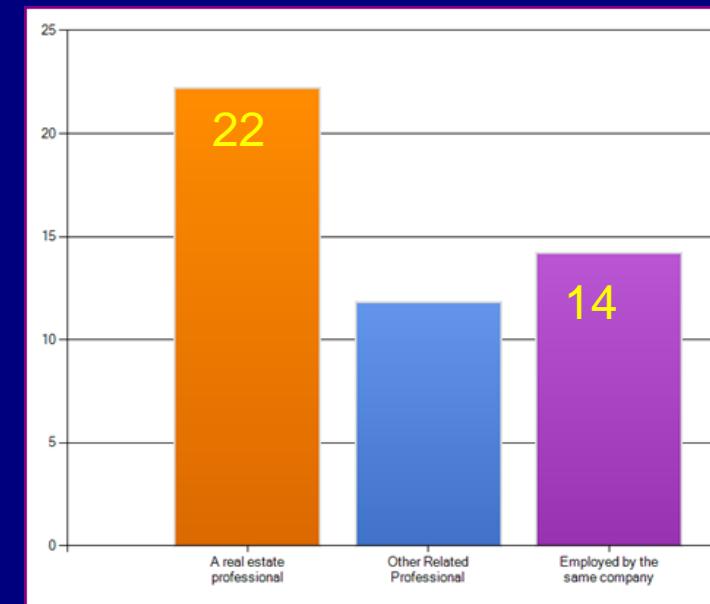


Who Are We?

Who's Here?

		Response Percent	Response Count
Broker: Tenant Rep		12.5%	8
Broker: Owner Rep		26.6%	17
Tenant User		0.0%	0
Corporate Owner/User		1.6%	1
Advisor		3.1%	2
Investor		9.4%	6
Investor Rep		1.6%	1
Investment Sales		9.4%	6
Other		15.6%	10
Developer		4.7%	3
Developer Rep		3.1%	2
Property Manager		4.7%	3
Mortgage Broker/Banker		4.7%	3
Lender		Who's Not?	0.0%
Consultant		1.6%	1
Lawyer		1.6%	1

Experience of Respondents



JRD Prediction

Number with Same Company will decline.....

Who's Not?



When National & Seattle Markets Bottom Out?

	It has already	4th Quarter 2009	1st Quarter 2010	2nd Quarter 2010	3rd Quarter 2010	4th Quarter 2010	1st Quarter 2011	2nd Quarter 2011	3rd Quarter 2011	4th Quarter 2011
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Economy

National Market	24.1% (13)	18.5% (10)	9.3% (5)	13.0% (7)	13.0% (7)	9.3% (5)	3.7% (2)	0.0% (0)	1.9% (1)	5.6% (3)
Seattle Market	9.6% (5)	3.8% (2)	13.5% (7)	30.8% (16)	15.4% (8)	7.7% (4)	7.7% (4)	3.8% (2)	1.9% (1)	3.8% (2)

Housing Market

	It has already	4th Quarter 2009	1st Quarter 2010	2nd Quarter 2010	3rd Quarter 2010	4th Quarter 2010	1st Quarter 2011	2nd Quarter 2011	3rd Quarter 2011	4th Quarter 2011
National Market	26.9% (14)	3.8% (2)	3.8% (2)	26.9% (14)	21.2% (11)	9.6% (5)	0.0% (0)	3.8% (2)	0.0% (0)	1.9% (1)
Seattle Market	26.9% (14)	3.8% (2)	1.9% (1)	17.3% (9)	13.5% (7)	21.2% (11)	1.9% (1)	5.8% (3)	1.9% (1)	3.8% (2)

Commercial RE Market

	It has already	4th Quarter 2009	1st Quarter 2010	2nd Quarter 2010	3rd Quarter 2010	4th Quarter 2010	1st Quarter 2011	2nd Quarter 2011	3rd Quarter 2011	4th Quarter 2011
National Market	3.8% (2)	1.9% (1)	1.9% (1)	9.4% (5)	17.0% (9)	22.6% (12)	17.0% (9)	7.5% (4)	9.4% (5)	3.8% (2)
Seattle Market	3.8% (2)	0.0% (0)	5.7% (3)	1.9% (1)	9.4% (5)	22.6% (12)	20.8% (11)	9.4% (5)	11.3% (6)	7.5% (4)



Part II: A Growing Consensus on Economy

Statement on National Economy	Strongly Agree	Agree	Neither	Disagree	Strongly Disagree
The US economy is on the road to recovery.	3%	44%	26%	21%	5%
Inflation not a concern for 2 years	3%	44%	7%	30%	16%
Employment losses stop by year-end.	2%	12%	5%	62%	20%
GDP Growth will be positive in 2009.	2%	15%	23%	52%	8%
Economic recovery will be very gradual.	42%	53%	0%	2%	3%
Consumer confidence will rebound.	3%	25%	15%	52%	5%
Manufacturing slump will continue.	13%	72%	8%	7%	0%
Interest rates will remain low.	7%	56%	16%	21%	0%
Credit market returns to normal in 6 mo.	2%	5%	5%	50%	38%
Corporate profits will start increasing.	3%	46%	21%	25%	5%

Monday, October 12, 2009

Leading Economists Declare End to Recessions

SAINST LOUIS—The recession, which began in December 2007, has ended but the nation still faces a long slow recovery, according to economists surveyed by the National Association for Business Economics.

Almost all of the panelists (92%) said it would take until at least 2012 to recover all of the jobs lost in the recession. The majority of respondents – 54% – said the jobs lost in the recession – 7.2 million through the employment report for September – would not be recovered until 2012; 33% said the job losses would not be recouped until 2013 and another 5% said it would take even longer.



Breaking News on Real Estate & the Economy

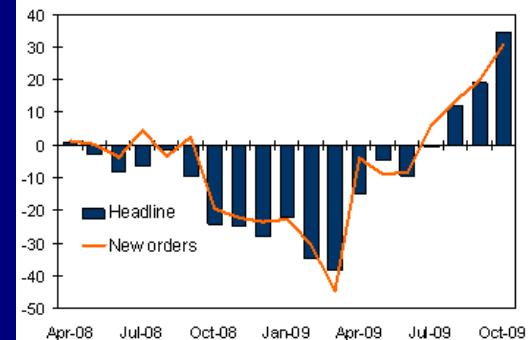
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BUSINESS | OCTOBER 16, 2009

Construction Industry Forecast to Rebound in 2010

The nation's construction industry, nearly paralyzed during the downturn, should see modest gains next year, as a rise in building of single-family houses, apartment buildings, and highways and bridges offsets drops in commercial and manufacturing property, according to a new report.

Broad-based improvement in manufacturing continues
Empire State manufacturing survey, index



DJIA Extends Climb Above 10000

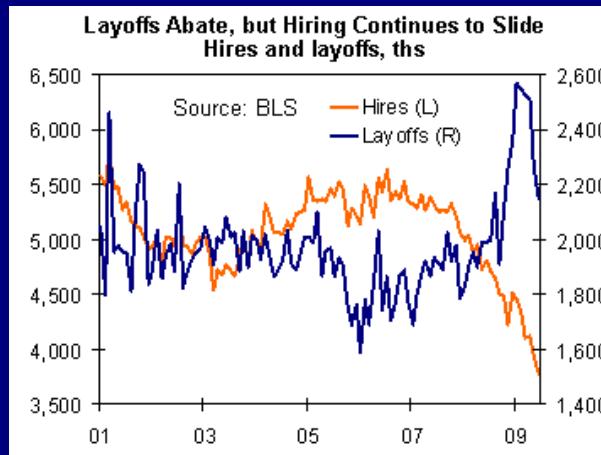
The Dow industrials held above the 10000 level as energy stocks rallied but the financial and technology sectors slumped.





The Good News: Employment Losses Slowing

Net Employment losses



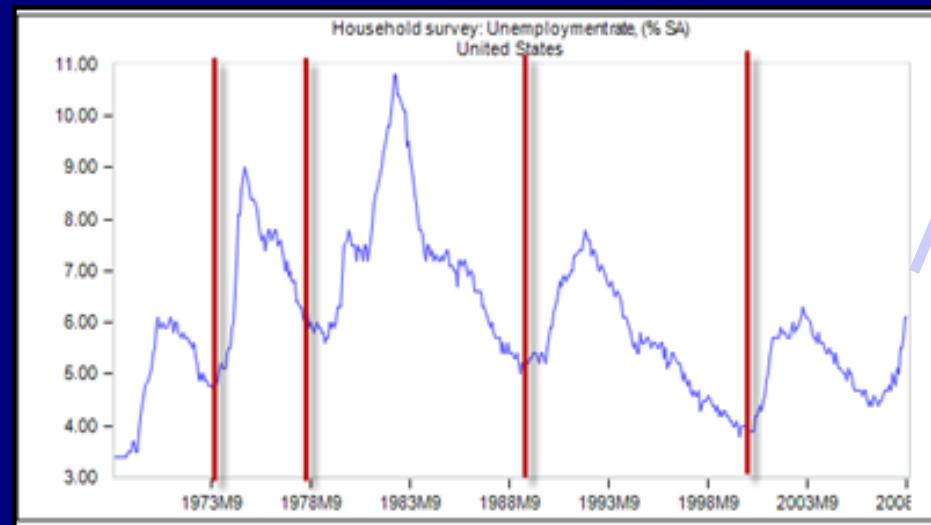
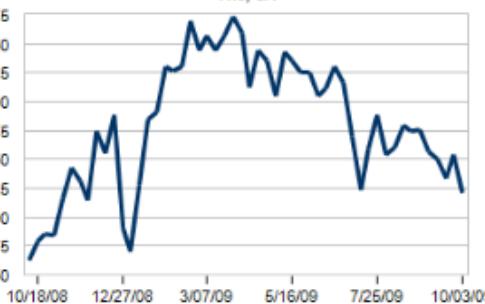
Jobless Claims Slowing?

United States: Jobless Claims

[Print](#) | [Definition](#) | [E-mail Alerts](#) | [Go To Source](#)

Actual: 521,000
Previous: ** 551,000
Moody's Economy.com: 540,000
Consensus: * 540,000
Coverage: 10/3/2009
Next Release: 10/15/2009
Archives: 10/8/2009
Updated: 10/8/2009 8:30 AM
Analysis By: Michael Bratus in West Chester

Weekly Jobless Claims
Ths, SA



10%



Click for annotation

Business Cycles: An Historical Comparison

U.S. Business Cycles Since World War II

Peak-to-trough % change

Peak	Trough	Real GDP	Industrial Production	Nonfarm Employment	Jobless Rate		
					Low	High	Change
Dec. 2007	Sept. 2009	-3.9%	-19.2%	-5.5%	4.4%	10.1%	5.7%
Mar. 2001	Nov. 2001	-0.4%	-6.3%	-2.0%	3.8%	6.3%	2.5%
July 1990	Mar. 1991	-1.3%	-4.3%	-1.5%	5.0%	7.8%	2.8%
July 1981	Nov. 1982	-2.9%	-9.5%	-3.1%	7.2%	10.8%	3.6%
Jan. 1980	July 1980	-2.2%	-6.2%	-1.3%	5.6%	7.8%	2.2%
Nov. 1973	Mar. 1975	-3.1%	-14.8%	-2.7%	4.6%	9.0%	4.4%
Dec. 1969	Nov. 1970	-1.0%	-5.8%	-1.4%	3.4%	6.1%	2.7%
Apr. 1960	Feb. 1961	-1.3%	-6.2%	-2.3%	4.8%	7.1%	2.3%
Aug. 1957	Apr. 1958	-3.8%	-12.7%	-4.4%	3.7%	7.5%	3.8%
July 1953	May 1954	-2.7%	-9.0%	-3.3%	2.5%	6.1%	3.6%
Nov. 1948	Oct. 1949	-1.7%	-8.6%	-5.1%	3.4%	7.9%	4.5%
Average		-2.0%	-8.3%	-2.7%	4.4%	7.6%	3.2%

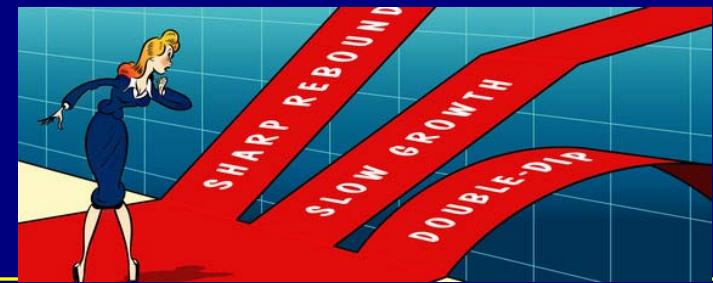
Sources: NBER, BEA, FRB, BLS, Moody's Economy.com



Critical Elements to Sustainable Recovery

For a Sustainable Recovery	Extremely Important	Important	Neither	Unimportant	Extremely Unimportant
Extend first-time homebuyer.	13%	48%	20%	16%	3%
Maintain of low interest rates.	20%	77%	3%	0%	0%
More access to business credit.	77%	23%	0%	0%	0%
Job growth vs. slowing losses.	69%	30%	2%	0%	0%
Improved consumer confidence.	57%	36%	7%	0%	0%
A rebound in the global economy.	30%	61%	8%	2%	0%
Reduction in federal deficit.	33%	36%	20%	11%	0%
Continue federal stimulus efforts.	3%	25%	38%	22%	12%
New tax breaks for businesses.	25%	44%	23%	7%	2%
Continued offshore capital flows.	13%	57%	25%	3%	2%

The Future Remains Uncertain



Seattle Respondents

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Federal Stimulus Funding: Pledged & Provided

	Pledged	Provided
Federal Reserve		
Term Securities Lending Facility	200	0
Commercial Paper Funding Facility**	1,800	42
TALF	1,000	43
Money Market Investor Funding Facility	540	0
TARP	700	575
Fed supplementary financing account	479	479
Back stop of Fannie Mae and Freddie Mac	400	97
Federal Deposit Insurance Corporation		
Guarantee of U.S. banks' debt*	1,400	330
Guarantee of Citigroup debt		10
Guarantee of Bank of America debt		3
Transaction deposit accounts	500	0
Federal Housing Administration		
Refinancing of mortgages	100	0
Congress		
Economic Stimulus Act of 2008	170	170
American Recovery and Reinvestment Act of 2009	787	787
Joint Fed, FDIC and Treasury		
Public-Private Investment Fund	1,000	0
Total		

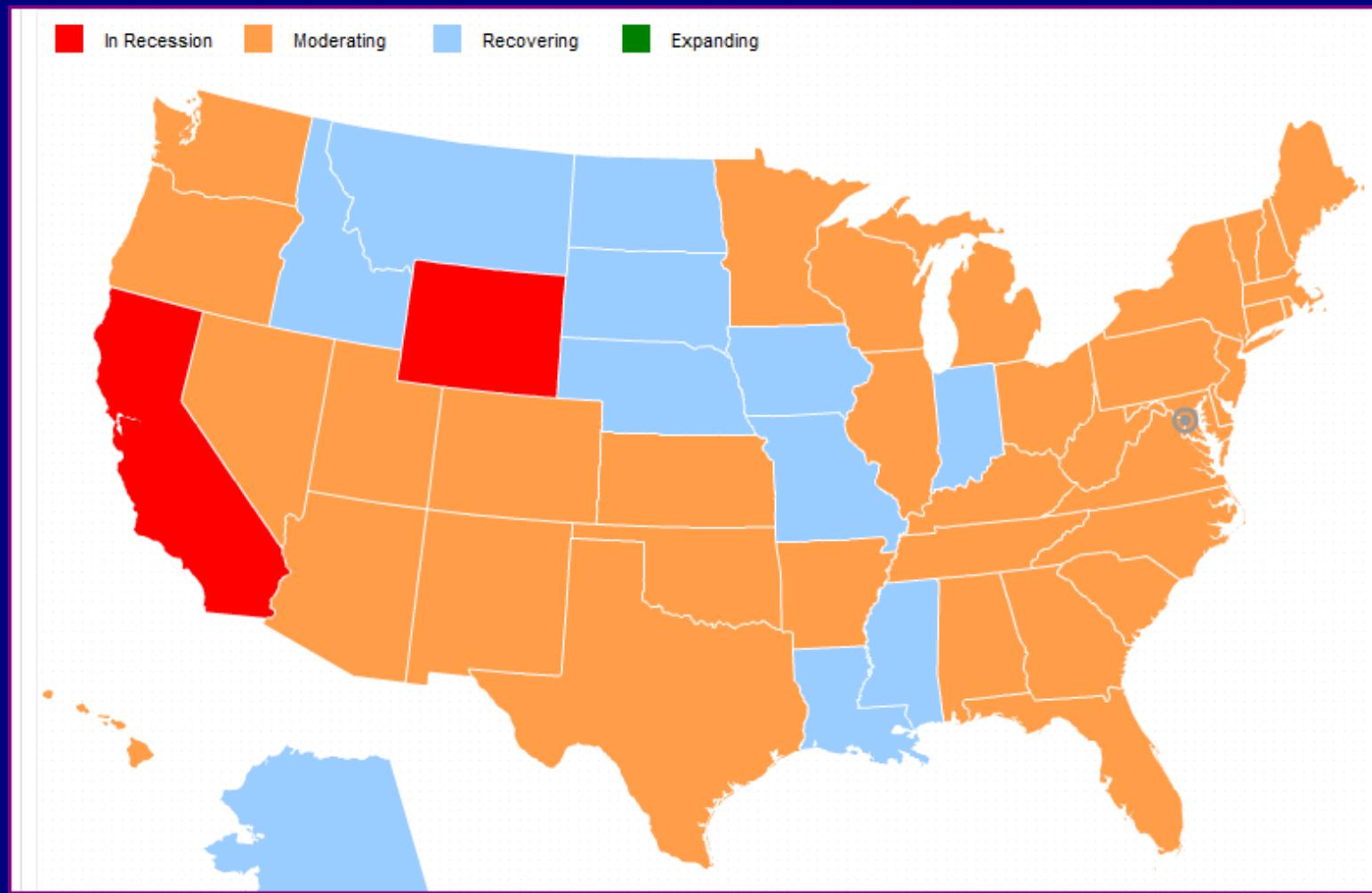
Sources: Fed, Treasury, FDIC, FHA, Moody's Economy.com

Major U.S. banks and securities firms are on pace to pay employees about \$140 billion this year -- a record high that shows compensation is rebounding despite scrutiny of Wall Street's pay culture. Top workers can expect to earn even more than in the peak year of 2007.

Wall Street on Track to Award Record Pay



US Recovery Status





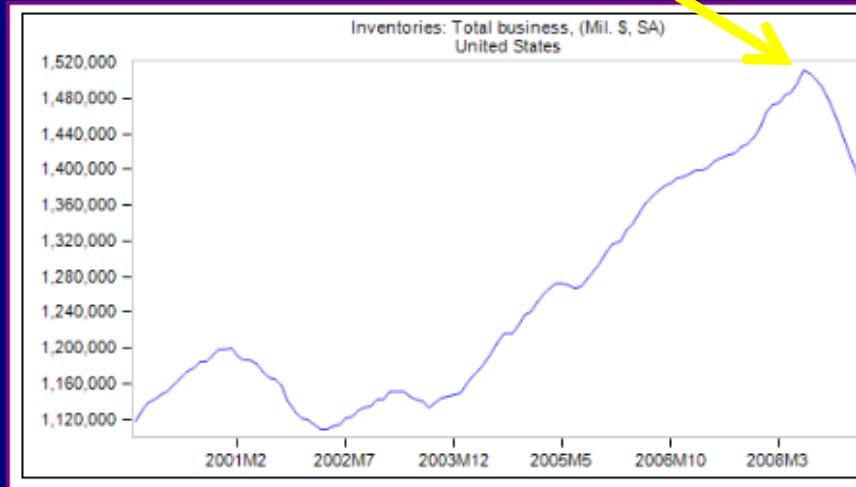
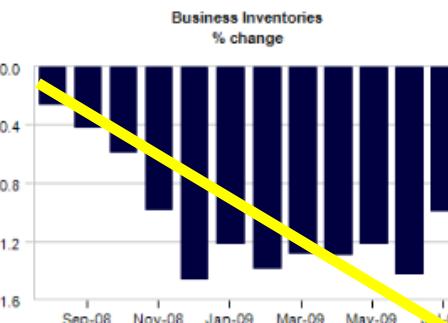
Business Inventories and Business Spending

Business Inventories

United States: Business Inventories (MTIS)

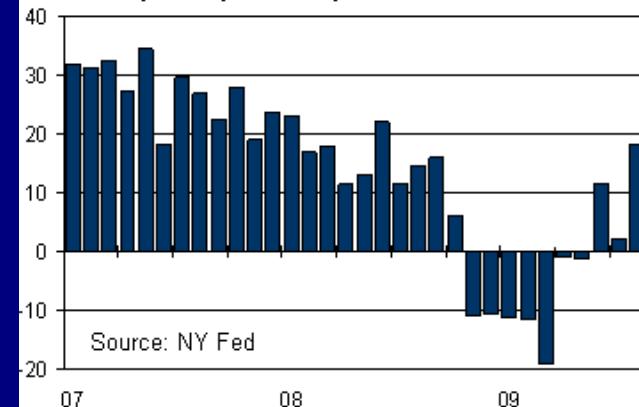
[Print](#) | [Definition](#) | [E-mail Alerts](#) | [Go To Source](#)

Actual:	-1.0%
Previous: **	-1.1%
Moody's Economy.com:	-1.1%
Consensus: *	-0.9%
Coverage:	July 2009
Next Release:	10/14/2009
Archives:	9/15/2009
Updated:	9/15/2009 10:00 AM
Analysis By:	Andrew Gledhill in West Chester



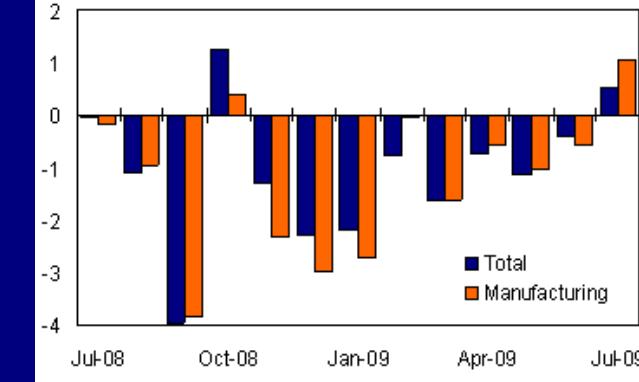
Business Spending

Business Spending Showing Signs of Stabilizing Capital expenditure plans, diffusion index



Good News: Manufacturing up

Hard Evidence of Manufacturing Rebound Industrial production, % change

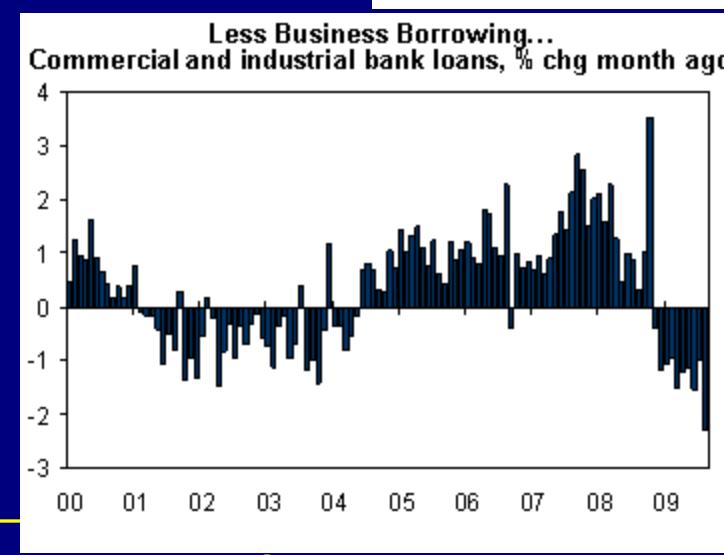
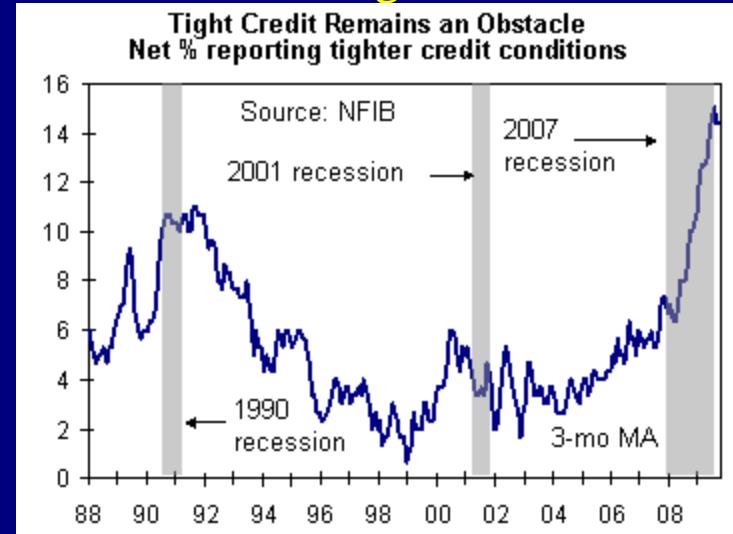




Focus on Small Business

- Small business report tighter credit
- Reactions
 - Cutting payrolls
 - Reducing inventory
 - Reducing capital spending
- Outlook
 - No near-term improvement

Credit Remains Tight for Business



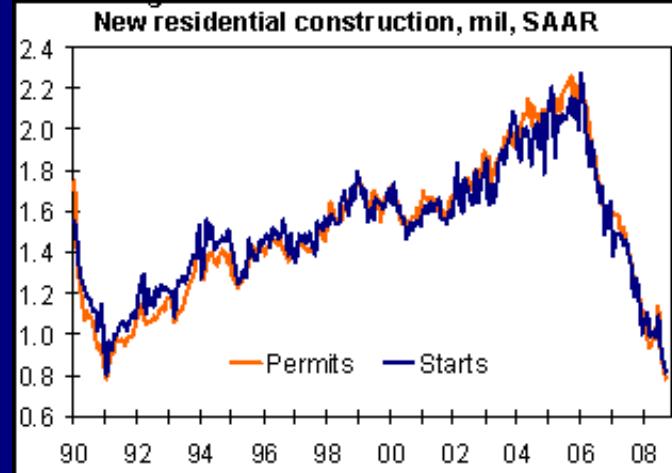
Source: economy.com

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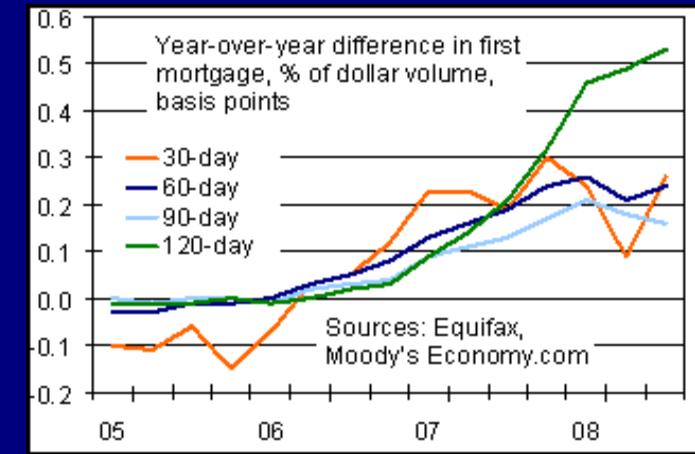


Housing Activity and Delinquency Rates

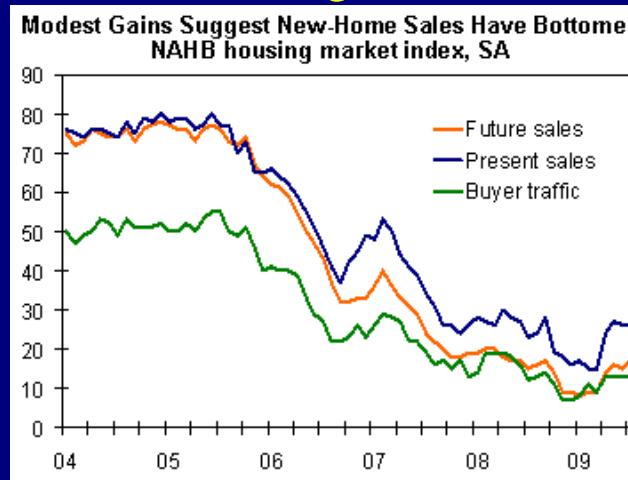
Construction



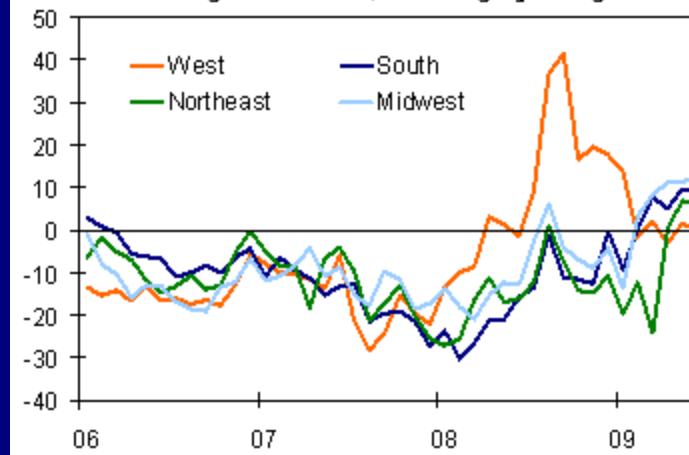
Delinquency & Default



Housing Index



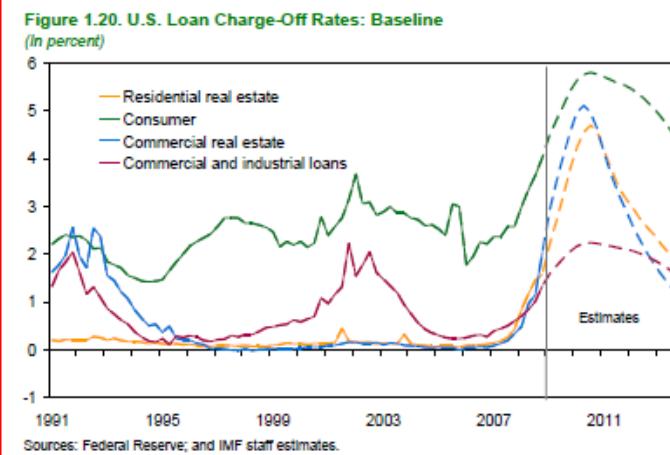
Distress Sales Play a Smaller Role Pending home sales, % change year ago





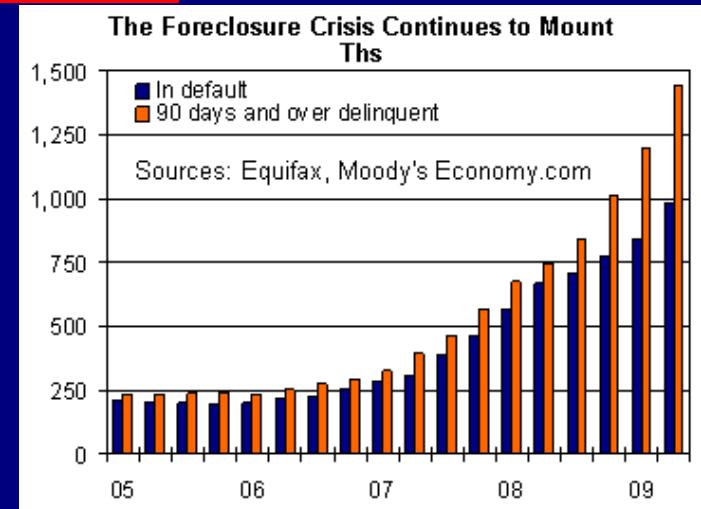
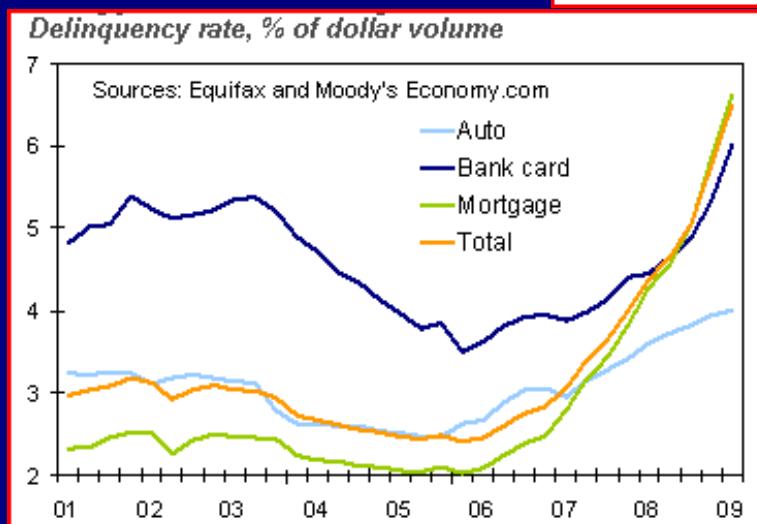
Residential Delinquencies, Foreclosures & Charge-Offs

Loan Charge-Off Rates to Rise



Delinquency Rates

Residential Foreclosures

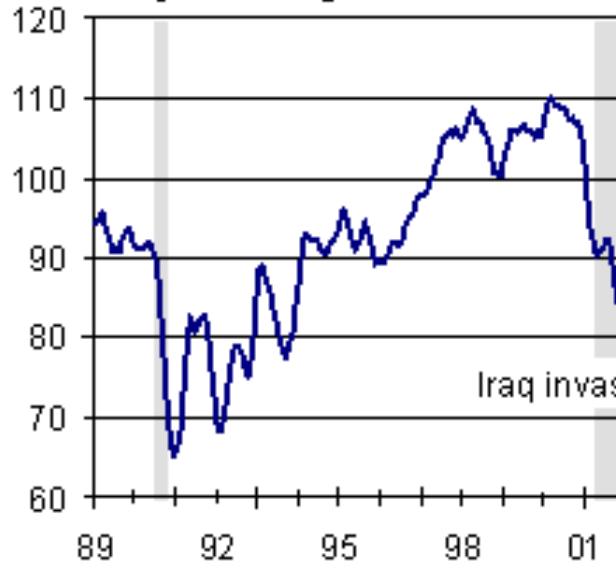




Consumer Confidence, Spending & Credit

Consumers Contracting

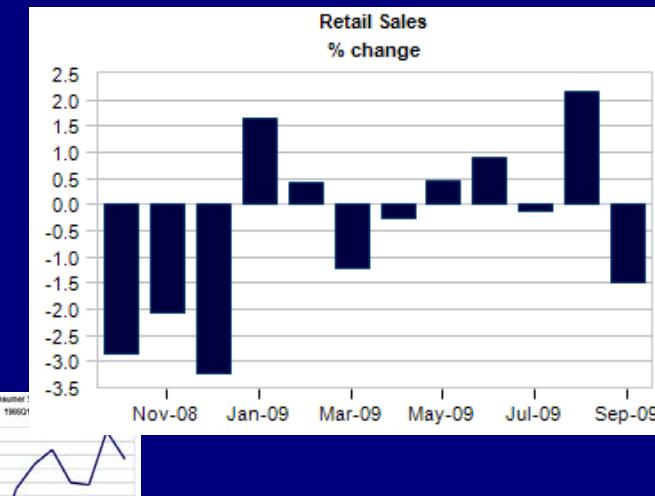
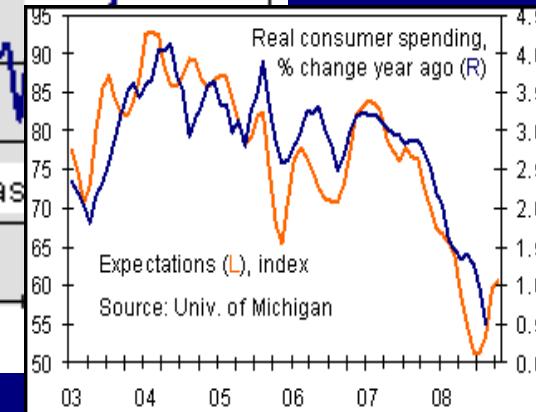
Consumers Are Very Jittery...
University of Michigan sentiment index, 1966Q1=100



Source: economy.com

As of October 2009, recent
uptick in retail sales on Year
over Year; partly weak 2008...

Consumers are over 70% of
GDP....



Butt...

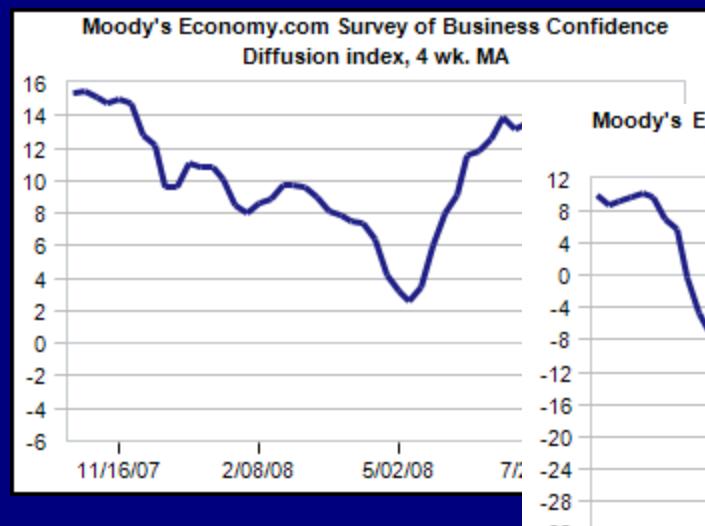
OCTOBER 14, 2009, 8:42 A.M. ET

Retail Sales Drop on Fall in Autos

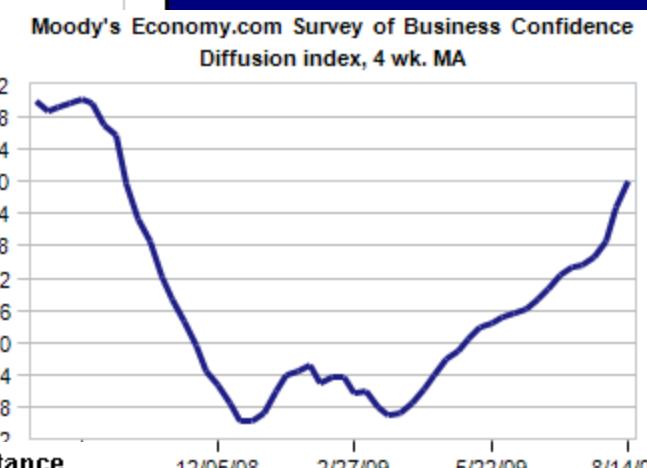


Global and Domestic Business Confidence

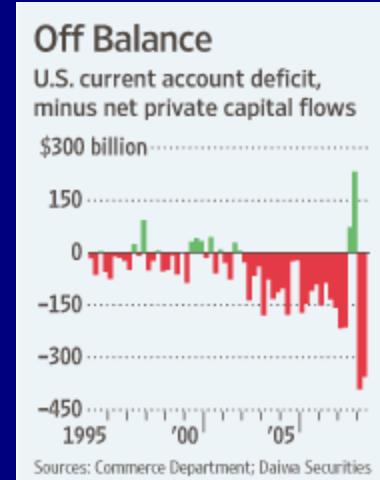
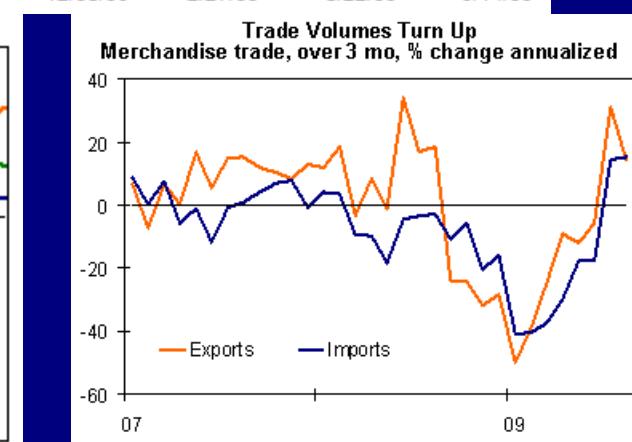
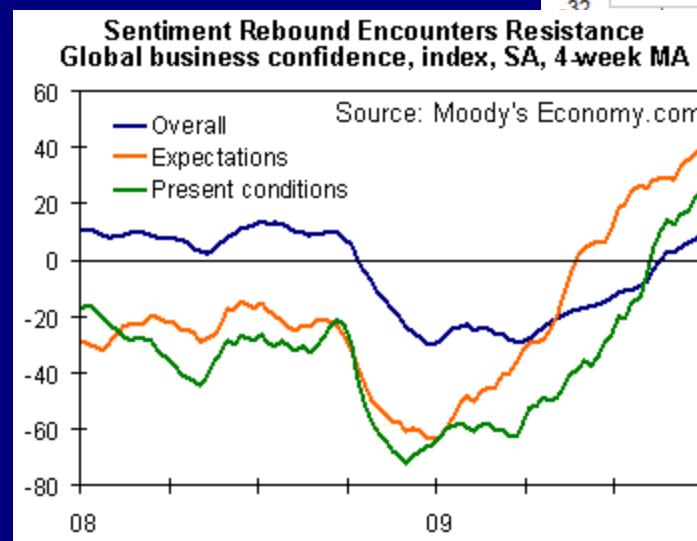
U.S. Business Confidence



Some improvement....



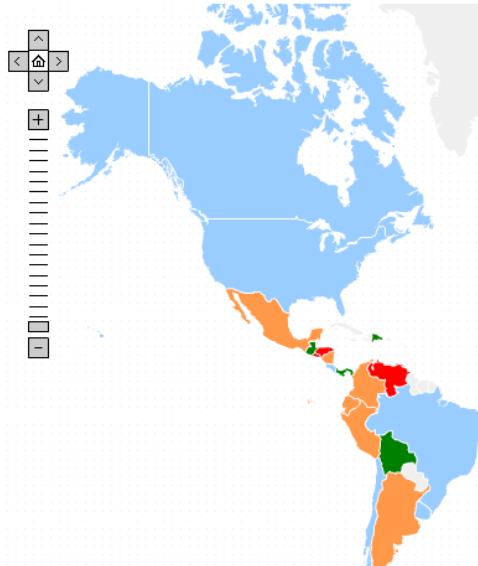
But, deficit....





Global Recession Map

About this Map
In Recessions Moderating Recovering Expanding



[Recession Watch Commentary »](#)
[Global Response Monitor »](#)
[U.S. Crisis Response »](#)

Global Emerging Market Composite Borrowing Rate %



Source: Merrill Lynch

World Summary

	2007	2008	2009F	2010F	2011F	2012F
Real GDP (%)	3.6	1.5	-2.6	2.2	3.7	4.5
Industrial production (%)	2.5	-2.3	-12.9	2.9	3.9	4.1
Employment growth (%)	1.5	1.4	0.1	1.2	1.6	1.8
Oil prices (WTI, US \$)	72.4	100.8	61.0	75.9	87.5	89.4
U.S. Federal Reserve monetary rate (year avg)	5.02	1.93	0.19	0.35	2.15	4.01
European Central Bank monetary rate (year avg)	3.94	3.69	1.13	1.06	2.28	3.63
Exchange rate: USD/EUR (year avg)	1.37	1.47	1.39	1.53	1.55	1.48
Exchange rate: JPY/USD (year avg)	118	103	98	102	103	100

Source: economy.com

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Part II Summary: The Economy

Macro-economic Environment

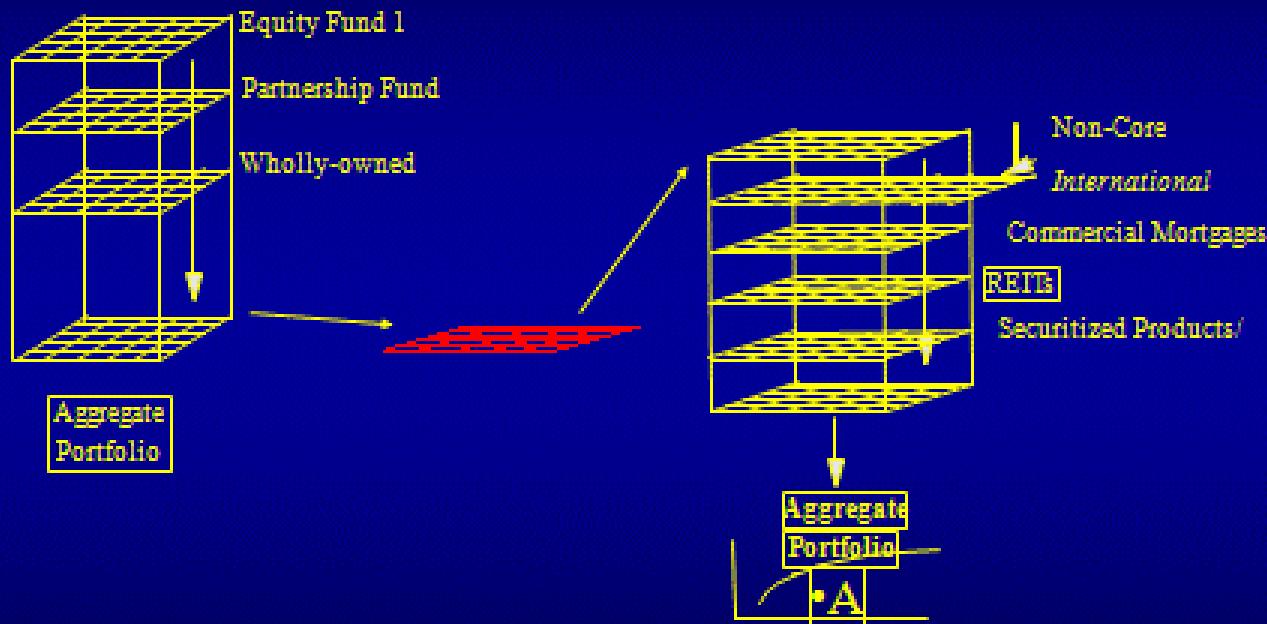
- Economy showing some signs of turning
- Businesses struggling, credit tight
- Consumers bearish



Part III: Real Estate Capital Markets

Holistic Portfolio Management: A Hybrid Approach

© JR DeLisle, Ph.D.





Current and Future National-Level Cap Rates

NAIOP National Forums vs. Seattle

Current		%	5.5%	6%	6.5%	7%	7.5%	8%	8.5%	9%	9.5%	10%	10.5%	11%	11.5%	12%	12.5%	13%
Answer Options																		
Institutional Grade Assets	0	0	3	1	3	6	14	6	9	1	3	0	0	0	1	0	0	
Distressed/Troubled Assets	0	0	0	0	0	0	1	3	2	1	15	1	2	2	9	1	3	
12 months																		
Answer Options	%	5.5%	6%	6.5%	7%	7.5%	8%	8.5%	9%	9.5%	10%	10.5%	11%	11.5%	12%	12.5%	13%	
Institutional Grade Assets	0	0	1	1	3	4	7	10	11	2	3	0	0	0	2	0	0	
Distressed/Troubled Assets	0	1	0	0	0	0	1	1	1	4	6	6	7	1	7	1	3	
3 years																		
Answer Options	%	5.5%	6%	6.5%	7%	7.5%	8%	8.5%	9%	9.5%	10%	10.5%	11%	11.5%	12%	12.5%	13%	
Institutional Grade Assets	1	0	2	0	9	9	6	5	7	4	3	0	0	0	0	0	0	
Distressed/Troubled Assets	0	0	1	1	0	0	2	4	6	4	13	2	5	0	4	0	0	



CBA: Properties for Sale Output

CBA: Properties for Sale

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 Multi Family Motel Rancher Mobile Home Park

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Central Business Dist
Commercial Core
Downtown/Mallard
Downtown Seattle
Lake Union
N. Seattle
Pioneer Square
Queen Anne/Alki Beach
S. Seattle
West Seattle

All Eastside
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Fremont
Kirkland
Redmond
Suburban Bellevue
Woodinville

Search Criteria:

Price Range:
Building SqFt:
Land SqFt:
Access:
Land Price/SqFt:
Map Page:
Street Address:

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Real Estate Process

Results: 60 [Previous](#) [1](#) [2](#) [3](#) [4](#) [5](#) [6](#) [Next 10](#) [New Search](#)

	Wilsonian Street Address: 4710 University Way NE - Seattle Total Building SqFt: 89,942 Cap Rate: 5.44 Brokerage: GVA Kidder Mathews
	Campus View Street Address: 4322 7th Ave NE - Seattle Total Building SqFt: 42,189 Cap Rate: 5.72 Brokerage: WPI Real Estate Services, Inc.
	Rivendell Street Address: 4719 15th Ave NE - Seattle Total Building SqFt: 34,962 Cap Rate: 5.28 Brokerage: GVA Kidder Mathews
	Gold's Gym of Seattle Street Address: 9701 Aurora Ave N - Seattle Total Building SqFt: 19,110 Cap Rate: 6.50 Brokerage: Northern Coast Real Estate Inc
	SGA - Shoreline Street Address: 14415 Greenwood Avenue N - Seattle Total Building SqFt: 17,640 Cap Rate: 6.04 Brokerage: CB Richard Ellis, Inc.
	SGA - Shoreline Street Address: 16325 NE 5th Ave - Shoreline \$per SQFT: \$45.03 Acres: 2.60 Brokerage: CB Richard Ellis, Inc.



Current and Future Seattle-Area Cap Rates

Our View on US

Current		5%	5.5%	6%	6.5%	7%	7.5%	8%	8.5%	9%	9.5%	10%	10.5%	11%	11.5%	12%	12.5%	13%
Answer Options		0	0	3	2	6	4	14	6	8	1	0	0	1	0	1	0	0
Institutional Grade A		0	0	0	0	0	1	4	0	3	1	13	3	4	0	6	1	4
Distressed/Troubled																		
12 months		5%	5.5%	6%	6.5%	7%	7.5%	8%	8.5%	9%	9.5%	10%	10.5%	11%	11.5%	12%	12.5%	13%
Answer Options		0	0	1	2	5	5	11	2	9	6	1	0	2	0	1	0	0
Institutional Grade A		0	0	1	0	0	0	2	2	2	0	12	1	9	1	4	0	4
Distressed/Troubled																		
3 years		5%	5.5%	6%	6.5%	7%	7.5%	8%	8.5%	9%	9.5%	10%	10.5%	11%	11.5%	12%	12.5%	13%
Answer Options		1	0	3	3	7	7	7	7	6	3	1	0	0	0	0	0	0
Institutional Grade A		0	0	0	1	0	0	4	7	3	5	12	1	3	0	4	0	1
Distressed/Troubled																		



Seattle Capital Market: Agree/Not

Answer Options	Strongly Agree	Agree	Neither	Disagree	Strongly Disagree
Opportunistic investors will make a strong move in 6 mo.	16%	56%	16%	12%	0%
Distressed assets will start flooding the market in the	14%	63%	13%	11%	0%
Real estate capital flows will be stagnant through 2010.	11%	56%	18%	15%	0%
The CMBS backlog & securitized capital will return in	0%	9%	20%	62%	9%
Commercial values will plummet 15-20% more over 12	11%	53%	11%	25%	2%
The government will help commercial debt market.	13%	34%	30%	18%	5%
Negative talk on commercial RE is just a bunch of hype.	0%	5%	12%	44%	39%
Transaction volume is picking up and will accelerate over	2%	32%	18%	46%	4%
Recourse debt will be required of buyers & refinances.	25%	58%	13%	4%	0%
Banks will get much more aggressive w/troubled assets.	14%	57%	14%	14%	0%



Capital Markets & Capital Flows

Positives

- Investment Preferences
 - Core assets at distressed prices
 - Major markets, strong assets
- Timing
 - Still waiting for bottom
 - Indecisive; slower to act
- Opportunities
 - Cash
 - Distress
 - Takeovers

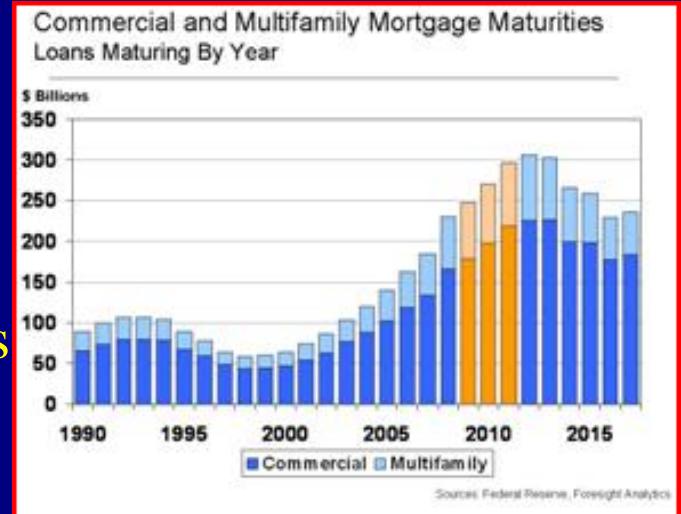
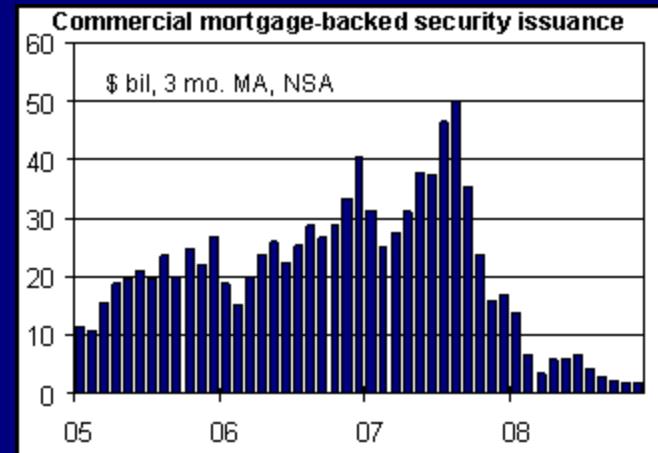
Negatives

- Decreased capital flows
 - Investors still frozen
 - Debt limited sources & tighter
 - Access & yield for equity
- Capital Market Challenges
 - Refinancing: volume & status
 - Weakening fundamentals
 - Surge in distressed assets
 - Valuations & mark-to-market
 - Growing pressure to act..



Commercial Leverage: Problems & Implications

- Tightened Credit
 - Higher DCRs and LVs
 - Hard valuations, less financial engineering
 - Recourse debt
 - Real equity positions
- Outlook for Commercial Debt
 - Limited supply; flight to quality
 - Tighter; increased equity and recourse
- Refinancing Crisis
 - No obvious sources of debt
 - Banks struggling with carry-over problems
 - No CMBS resurgence

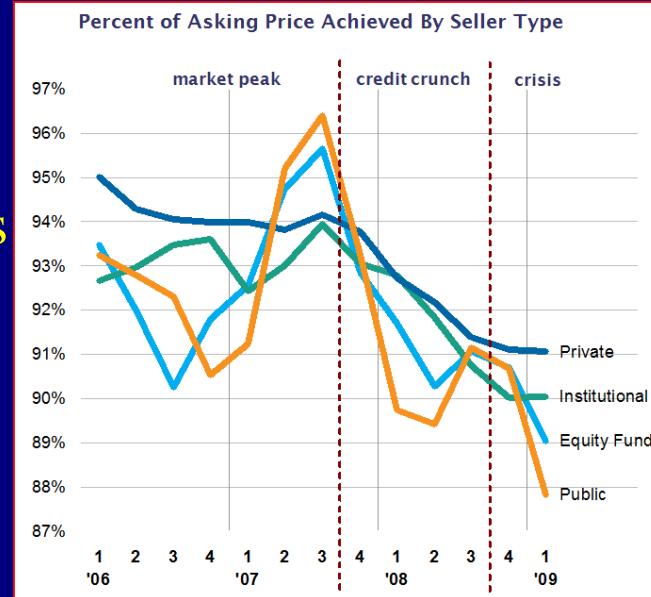




Bid/Ask Spread: Trends and Value Pressures

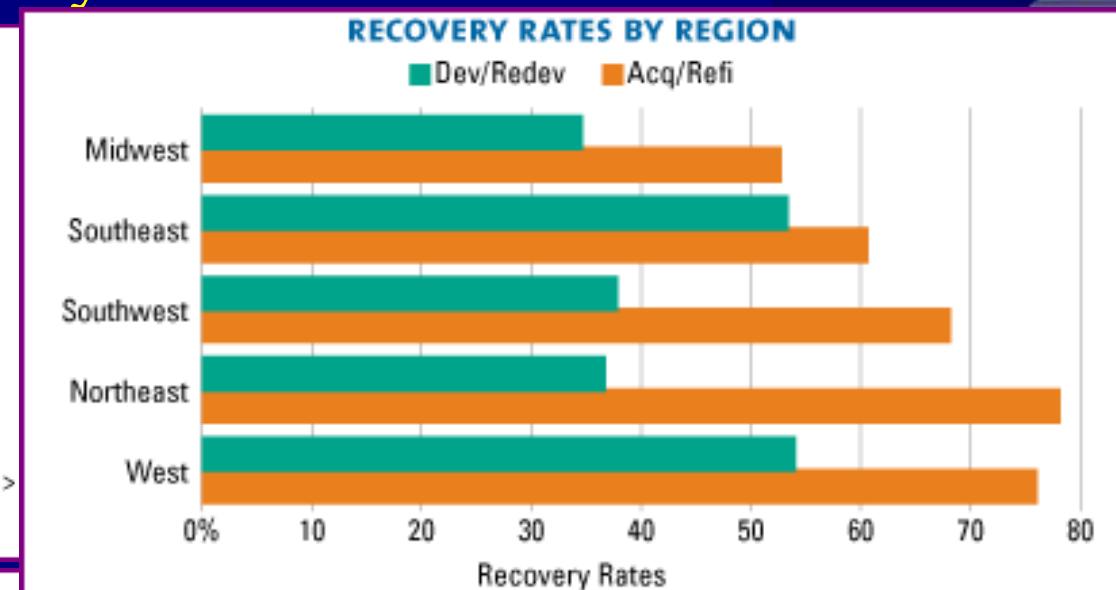
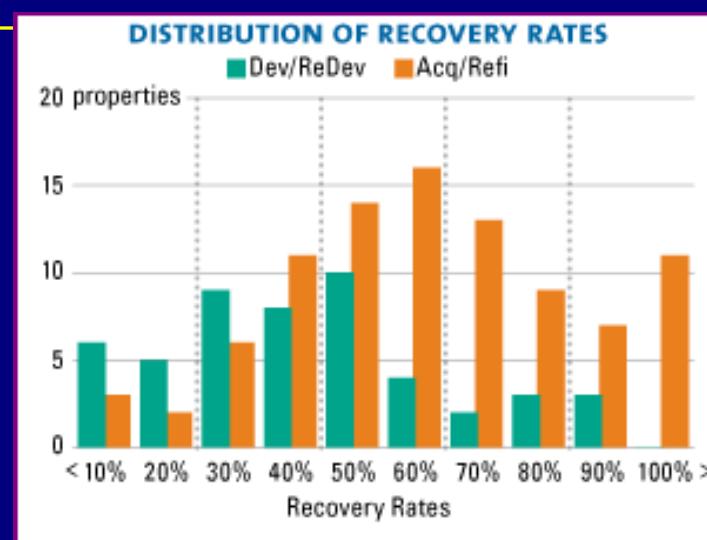


- Bid/Ask De-Compression
 - Distressed Sellers will have to act
 - Distressed Assets will face melt-down risks
- Mark-to-Market Accounts
 - NCREIF - 35% w/o Distressed Sales
 - Going Forward: Three Strikes
 - Comps Down as Assets Dumped
 - NOI Erosion, Vacancy & Rents
 - Debt & Equity Yields Up
- Appraisals under increasing scrutiny





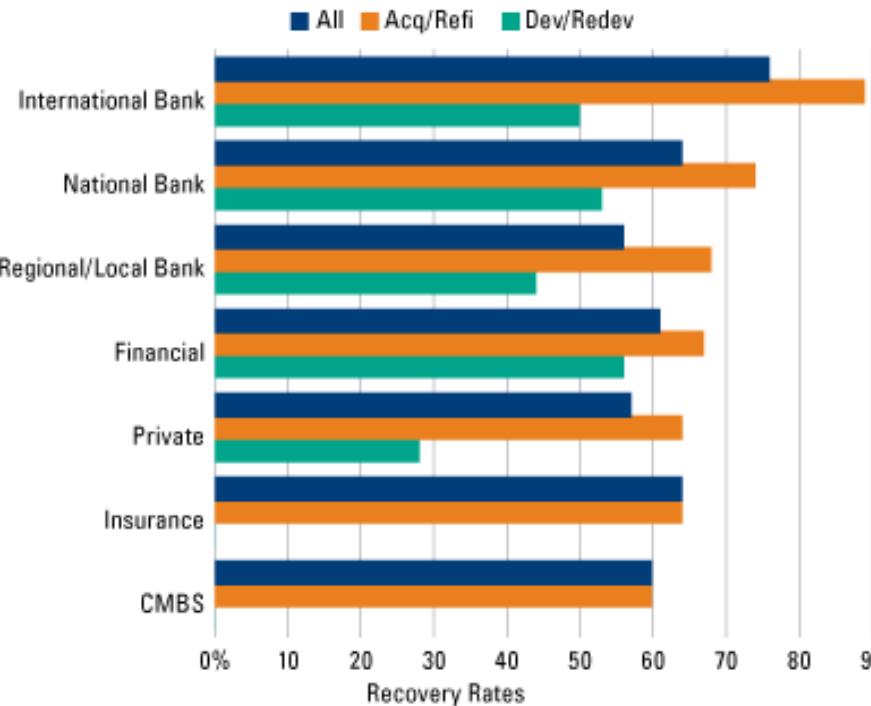
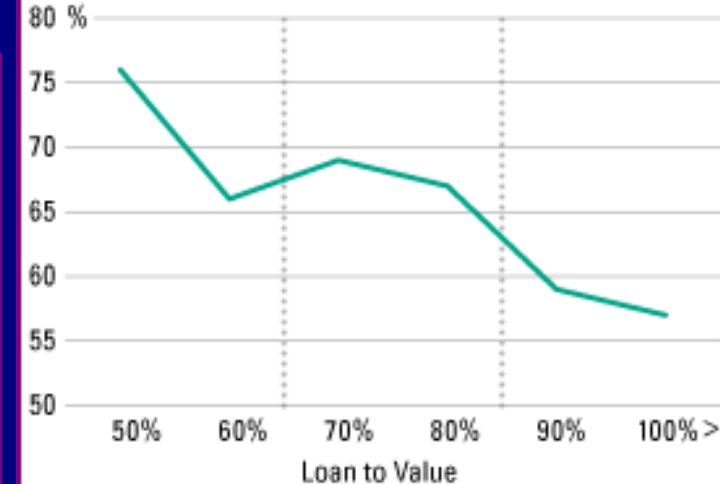
Distressed Loan Recovery Rates



Type	Balance Outstanding in \$ Millions	Number of Mtgs	Avg Recovery Rate
Const.	\$536.9	20	43%
Land Acq.	221.4	10	50%
Condo Conv.	97.6	8	52%
Redev.	389.6	13	52%
Total	\$1,245.5	51	48%
<hr/>			
Acquisition	1,690.6	71	68%
Refinance	275.2	23	59%
Total	\$1,965.8	94	66%
<hr/>			
Grand Total	\$3,211.3	145	60%



Distressed Asset Recovery by Source & Terms

RECOVERY RATES BY LENDER TYPES**RECOVERY RATES BY LTV ORIGINAL****RECOVERY RATES BY VINTAGE YEAR ORIGINATED**



Players in Distressed Asset Market



- REITs
 - Have reversed downward spiral
 - Significant new capital raised through Sept 2009
 - Low Dividends suggest accretive opportunities
- Global Investors
 - Western European
 - Middle East
 - Asia/Australia
- Domestic Funds
 - Significant growth in US
 - New Opportunity Funds
 - New Value-Plus Funds



REITs: Back to the Future?

- Changing Game?
 - Through June, raised \$12 billion in stock
 - Who?
 - Office: Boston Properties, Vornado Realty Trust
 - Retail: Regency Centers Simon Property Group
- Challenges
 - Existing Leverage
 - Eroding Fundamentals
 - Falling Property Values

Accretive?
Buy at 8-10,
payout 4-6

Property Sector/Subsector	Total Return (%)			Dividend Yield ²
	2008	September	Year to Date	
FTSE NAREIT Equity REIT Index	-37.73	6.40	17.00	4.02
Industrial/Office	-50.28	5.32	20.27	5.53
Industrial	-67.47	3.56	0.08	3.65
Office	-41.07	7.00	26.42	5.62
Mixed	-33.99	1.57	33.67	2.74
Retail	-48.36	6.20	16.59	3.72
Shopping Centers	-38.84	3.83	-5.28	1.08
Regional Malls	-60.60	8.92	42.03	6.96
Free Standing	-15.09	3.01	23.82	4.73
Residential	-24.89	12.51	18.96	4.91
Apartments	-25.13	12.66	18.77	2.99
Manufactured Homes	-20.18	9.90	24.62	0.91
Diversified	-28.25	10.75	8.63	6.41
Lodging/Resorts	-59.67	16.36	57.04	3.55
Health Care	-11.98	-1.33	11.14	5.09



Part III Summary: Real Estate Capital Markets

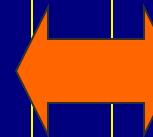


Macro-economic Environment

- Economy showing some signs of turning
- Businesses struggling, credit tight
- Consumers bearish

Real Estate Capital Market

- Still shut down; some activity increasing
- Rising Cap rates, tighter credit, picky sources
- Major challenge in de-levering





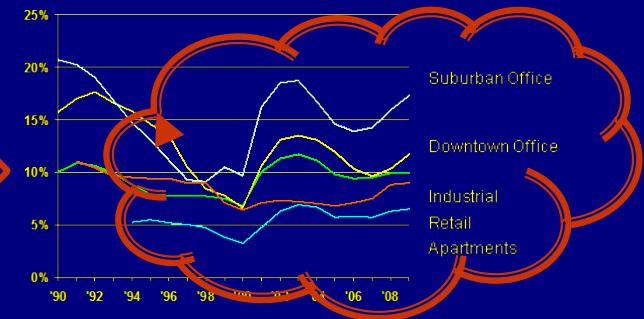
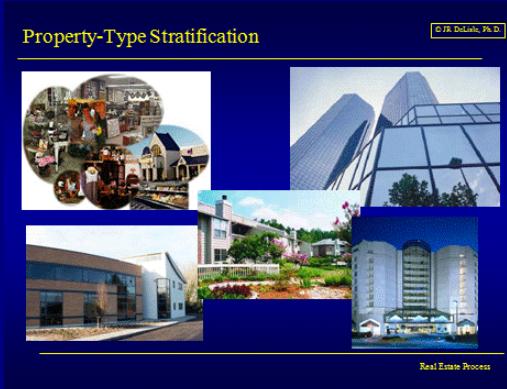
Part IV: Spatial Market

- Components of Spatial Market

- Demand

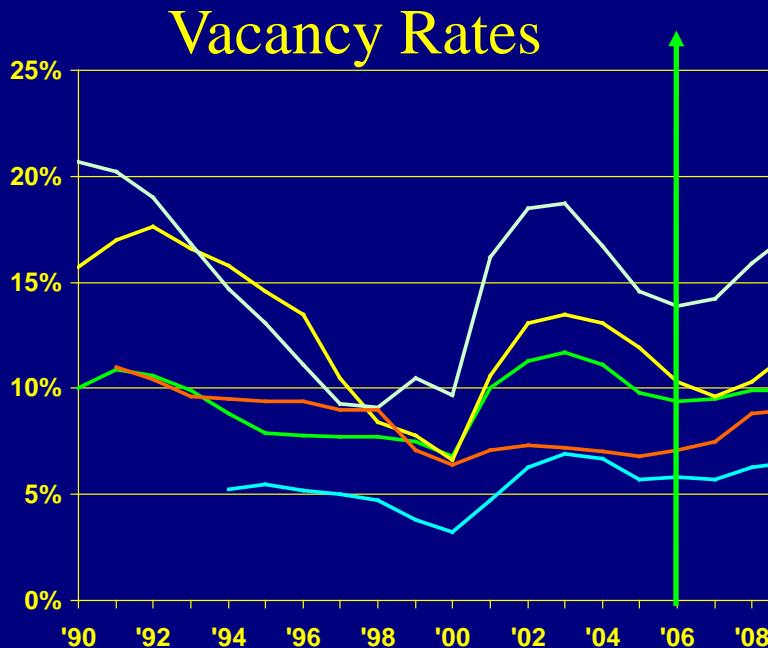


- Supply



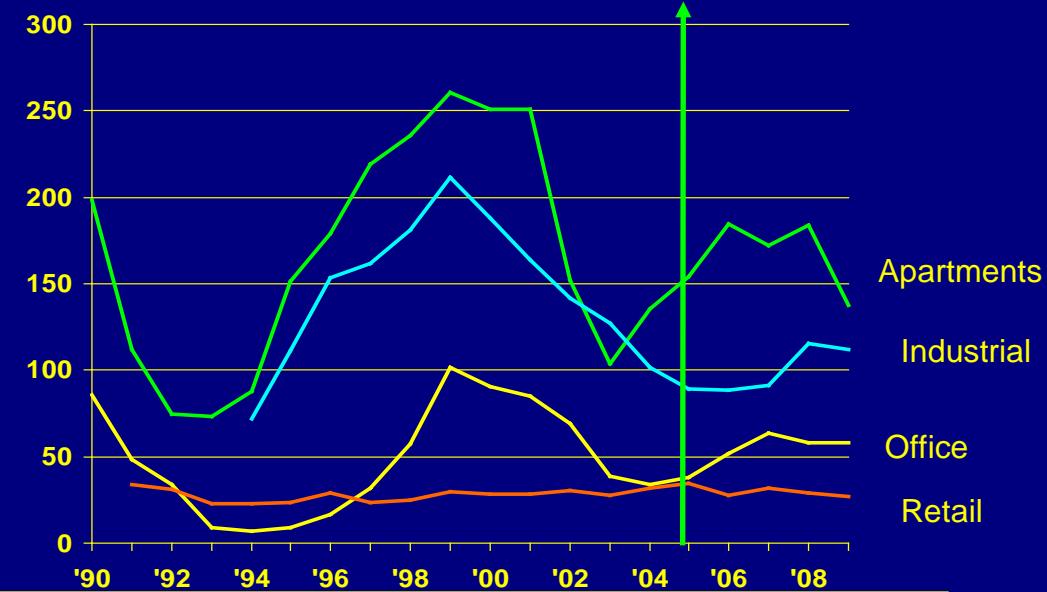


Commercial Market Fundamentals



Suburban
Office
Downtown
Office
Industrial
Retail
Apartments

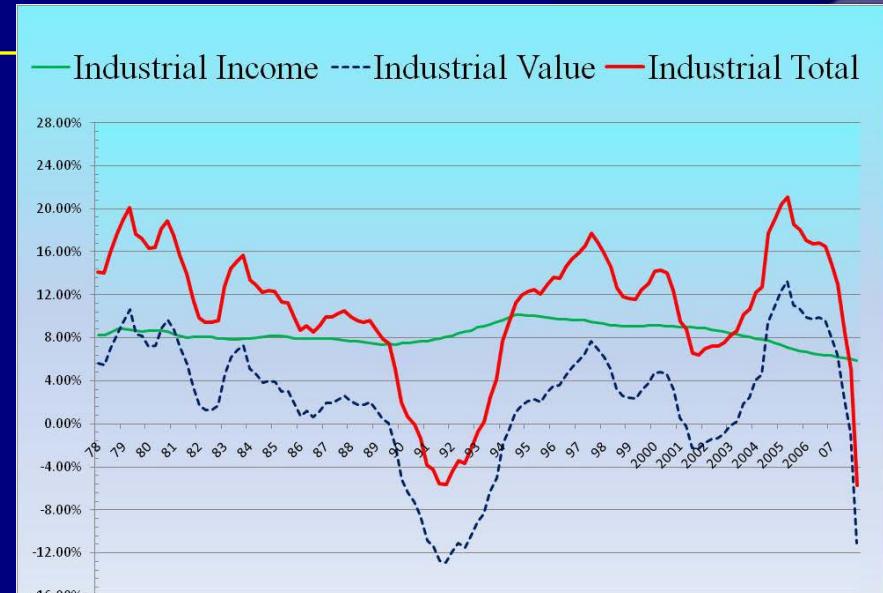
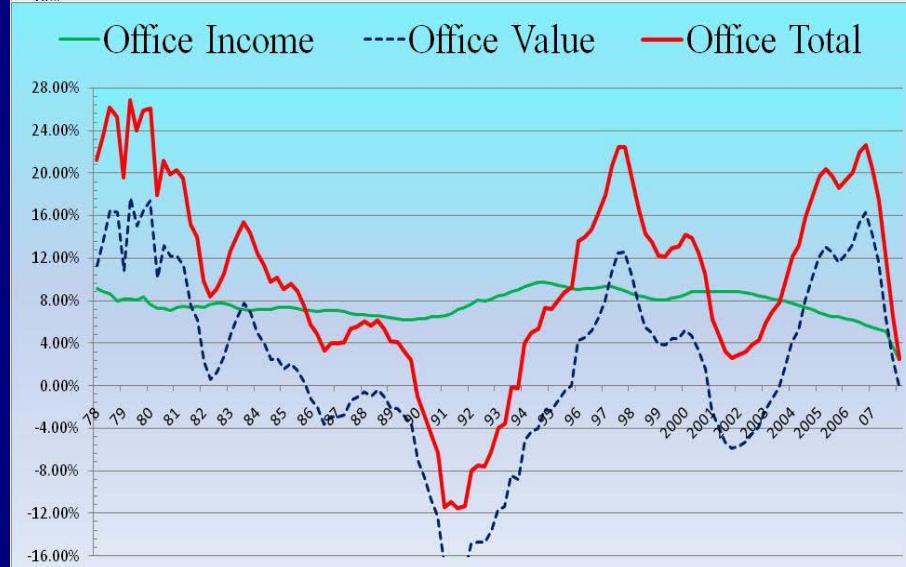
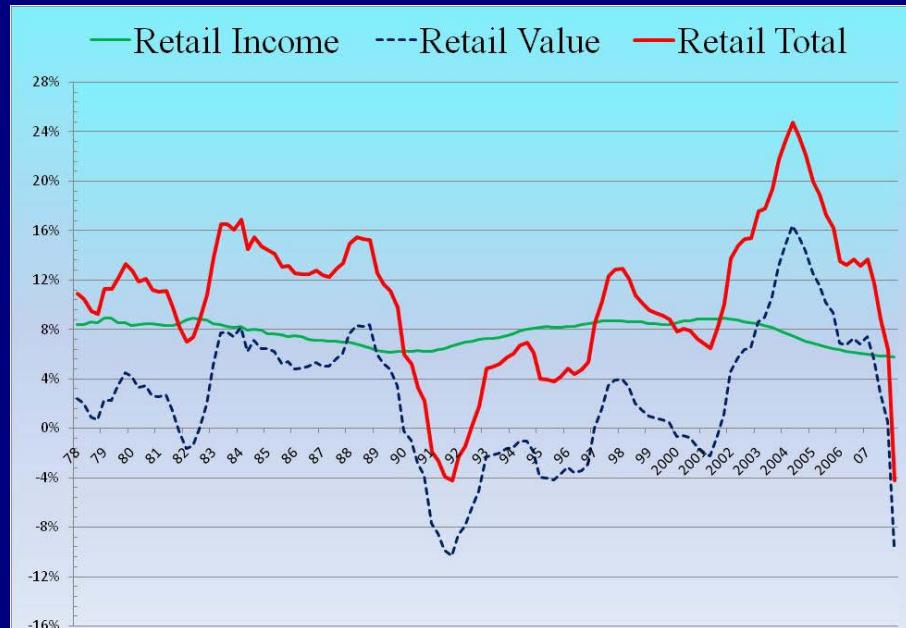
Development (msf)





NREIF Returns by Source by Property Type

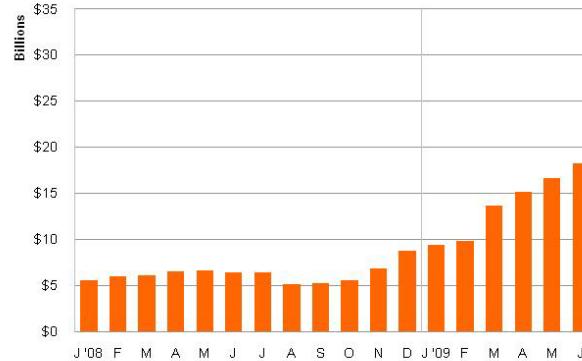
UNIVERSITY OF
WASHINGTON



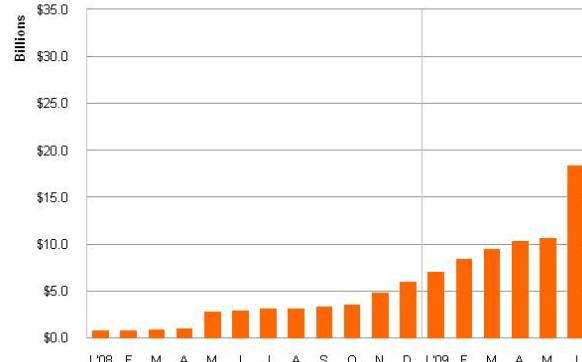


Growth in Distressed Assets by Property Type

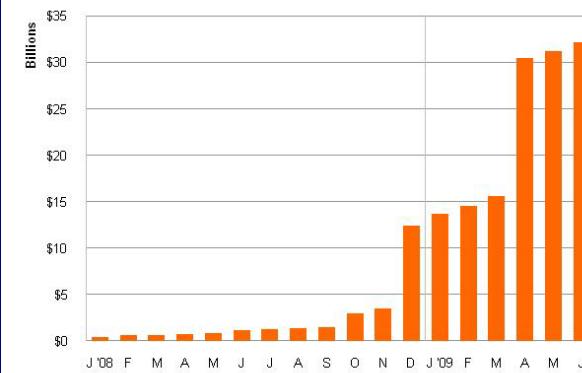
Monthly Cumulative Distress
Office



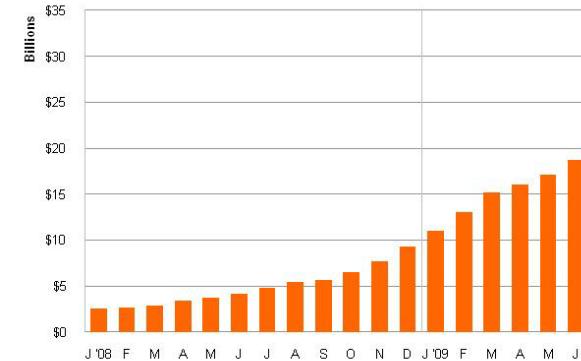
Monthly Cumulative Distress
Hotel



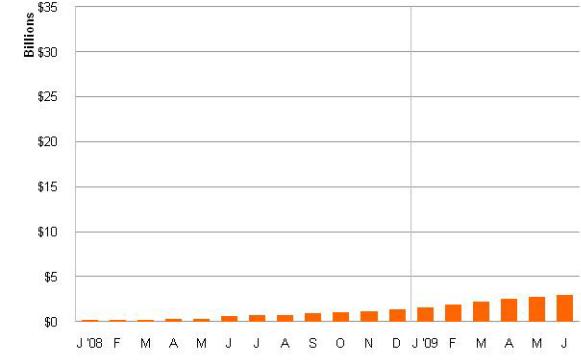
Monthly Cumulative Distress
Retail



Monthly Cumulative Distress
Apartment

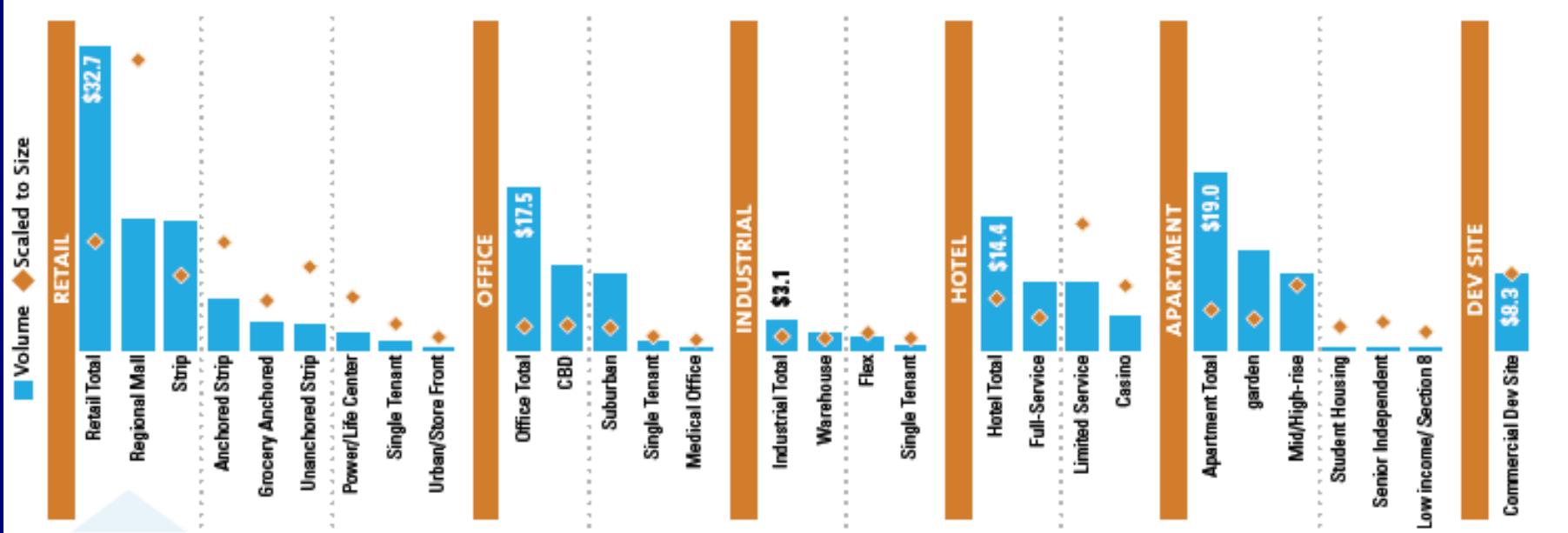


Monthly Cumulative Distress
Industrial



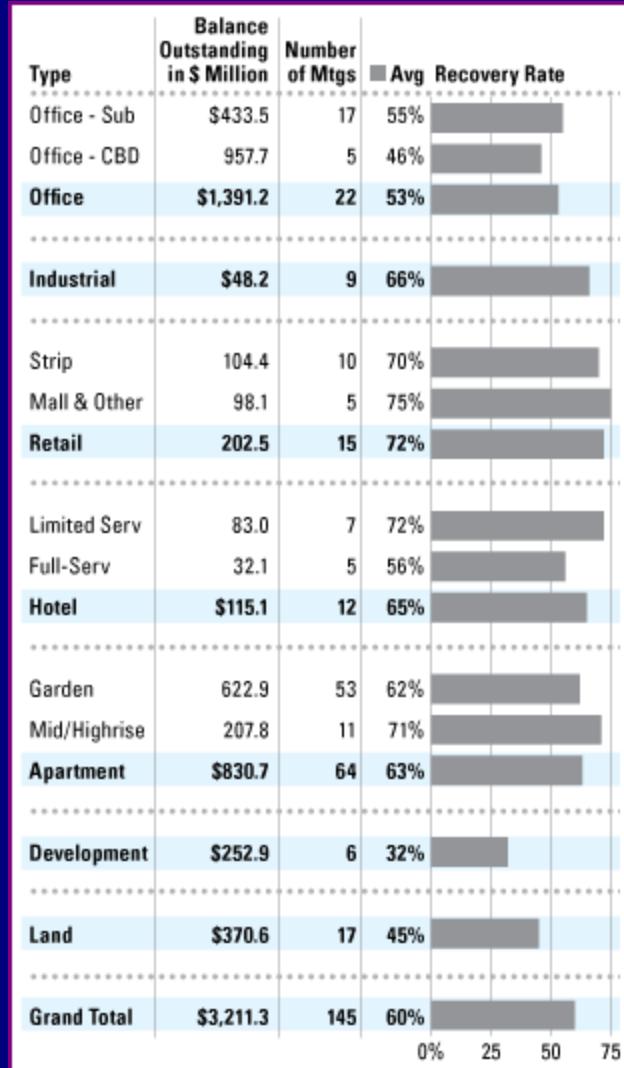


Distressed Assets by Property Type and Subtype





Distressed Loan Recovery by Property Type



Office 53%

Industrial 66%

Retail 72%

Hotel 65%

Apartment 63%

Development Land 32%
45%

Overall 60%



Seattle Real Estate Fundamentals: Yay/Nay?

Questions about Seattle Real Estate	Strongly Agree	Agree	Neither	Disagree	Strongly Disagree
Opportunistic investors will target Seattle in next 6	16%	55%	18%	11%	0%
Distressed assets will start flooding the Seattle market	7%	52%	13%	29%	0%
Through 2010, capital flows to Seattle will be stagnant.	2%	67%	11%	18%	2%
Commercial mortgages will be plentiful in Seattle next	2%	4%	11%	70%	14%
Seattle transactions are picking up and will accelerate	2%	34%	13%	50%	2%
Commercial values in Seattle will fall 15-20% over 12	5%	57%	14%	21%	2%
The negative talk about Seattle real estate is just hype.	2%	11%	13%	46%	29%
Commercial leasing activity is beginning to pick up.	4%	29%	27%	35%	5%
Owners of distressed Seattle assets will start to walk.	2%	80%	11%	7%	0%
The Seattle condo market will bottom out in early 2010.	4%	18%	20%	53%	5%

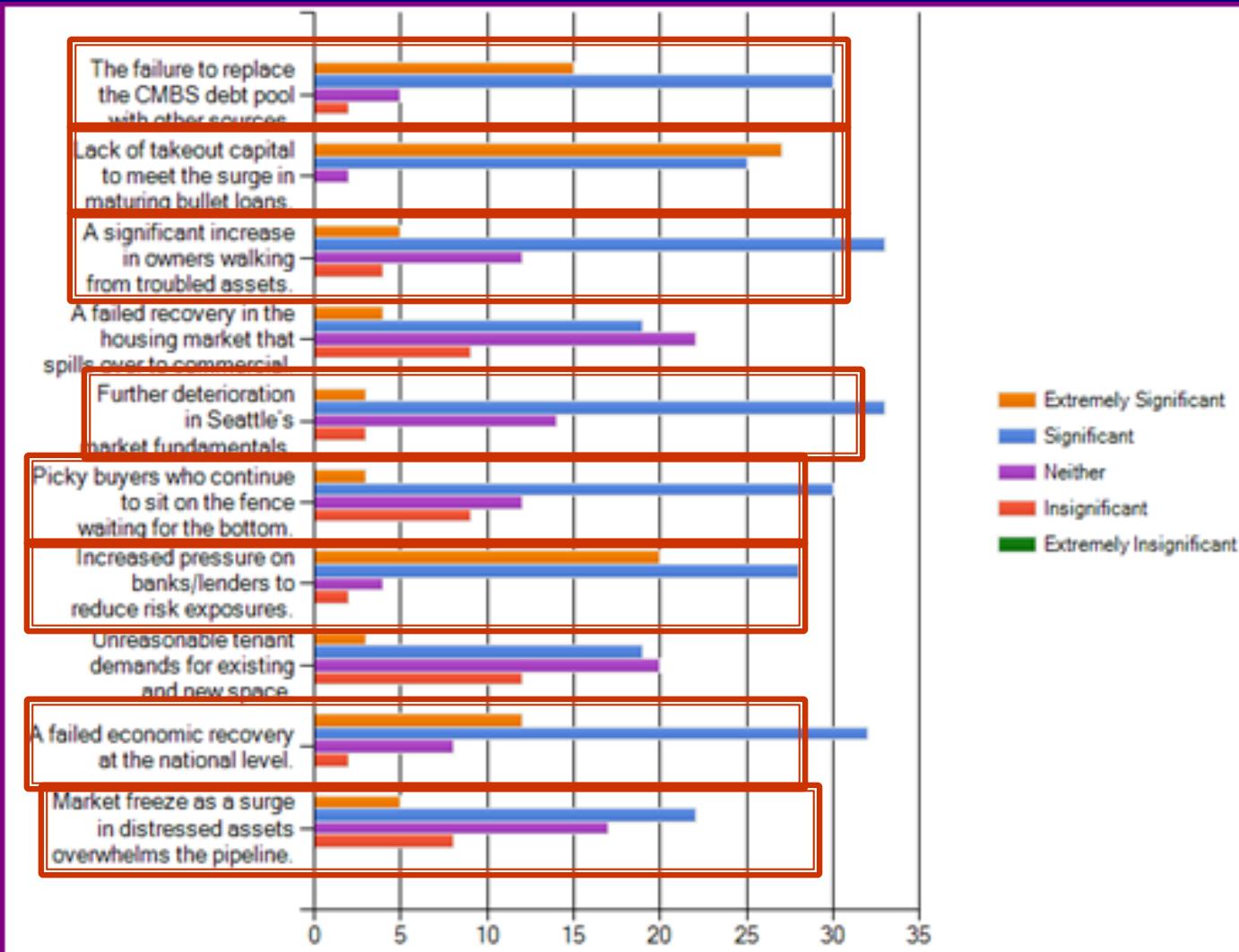


Additional Insights on Seattle Market

Statements on Seattle Commercial Market	Strongly Agree	Agree	Neither	Disagree	Strongly Disagree
Over next year, vacancy rates will dramatically rise.	4%	41%	27%	27%	2%
Developers on the sidelines for at least 18 months.	22%	69%	4%	5%	0%
The mantra "tenants rule" will carry into 2011.	16%	76%	5%	2%	0%
Opportunity funds will snap distressed RE, holding values.	0%	30%	28%	42%	0%
Local real estate will improve in pace with US economy.	2%	44%	9%	45%	0%
Commercial values in Seattle will fall 15-20% over 12 mo.	4%	60%	13%	22%	2%
A good note; local housing crisis behind us by mid-2010.	0%	45%	18%	35%	2%
Real estate fundamentals are good; too much negative	0%	15%	11%	64%	11%
Commercial vacancy rates to break all-time records.	7%	53%	18%	20%	2%
The local market will escape risks at national level.	0%	11%	11%	69%	9%



Seattle Market Risks: Significant/Not





Part IV Summary: The Spatial Markets

Macro-economic Environment

- Economy showing some signs of turning
- Businesses struggling, credit tight
- Consumers bearish

Real Estate Capital Market

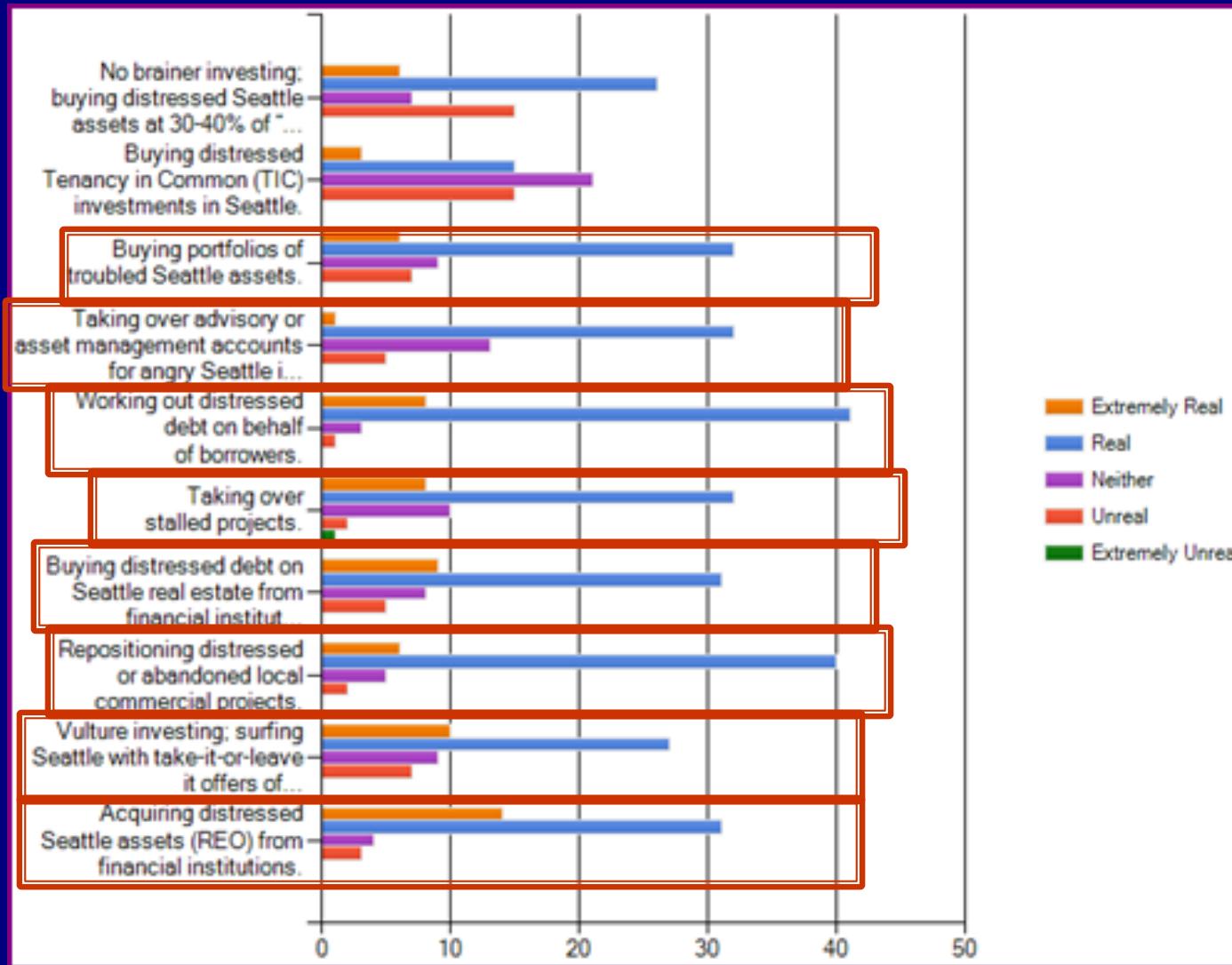
- Still shut down; some activity increasing
- Rising Cap rates, tighter credit, picky sources
- Major challenge in de-levering

Spatial Market

- Fundamentals continue to erode lagging economy
- Vacancy rates rising, rents falling
- Stagnant demand, leasing sluggish



Part V. “Real” Opportunities in Seattle RE





Players, Distress and Debt



- Players
 - Emergence of new players will create further problems
 - Many naïve buyers will clog up the system
 - Intermediaries will raise capital but struggle to deploy
 - Infrastructure not in place to deal with sheer volume of deals
- New Funds
 - Expect a spate of new funds, some with experience others not
 - Closed-end fund structures will be popular
 - Off-shore investors will be a major target for money managers
- Products
 - A spate of new products will be introduced to lay off risk
 - New Partnership arrangements will match expertise with capital



Re-merging Trends: 2010



- Commercial Leases
 - More complex negotiations
 - Early negotiations and renewals
 - Cannibalization threat by distressed owners will spill-over
 - Tenants will become more aggressive on rents & incentives
- Liquidity
 - Selling good assets at “fair value” will be difficult at best
 - Weaker assets will languish
 - Closing will be much more difficult
 - Shortage of capital for maintenance, TI's and capital needs
- Volume & Size
 - Over next 12-18 months, dramatic increase in transactions
 - More bundled transactions and bulk sales coming



Distress and Debt



- Distress
 - Not the “opportunity” many expect; not a “no-brainer” stage
 - Concept not well understood in a risk management context
 - Determination of what is curable and incurable will be key
 - Real danger that distress will turn to panic

- Debt
 - A major wild-card although market is discounting shortage
 - Money will be tight at best with recourse and equity increased
 - Seller financing will be critical to many transactions
 - Creative financing will re-emerge as a driver



Conclusion: What to do? Back to School?

- So, To Walk, To Talk, To Walk the Talk???That is the question....
 - There is no one answer....
 - Critical thinking and survival instincts will rule...
 - If not, there's always school....

JrD_{dR}

Professor James R. DeLisle, Ph.D.

October 20, 2009

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Overview

I am the Runstad Professor of Real Estate and Director of Graduate Real Estate Studies in the **College of Built Environments** at the **University of Washington** and the former Director of the **Rundstad Center for Real Estate Studies**.

This is a non-commercial website I have established to serve as a portal I can use to help advance the real estate discipline and improve market efficiency by disseminating some of my research, teaching and service materials. It also serves as a forum I can use to help me continue to bridge the gap between the academic community in which I currently reside and the professional community in which I have served in the past.



DrD

<http://jrdelisle.com>