

## Real Estate Capital Markets Update – December 31, 2007

### Volume 9, Number 10

#### How Long Will It (the credit crises) Last?

Think 6 month (if you're an optimist) to a year (if you're a realist). Want a metric to know it's over, or at least coming to an end: no announcements—globally—of write-offs, forced liquidations, major personnel changes, “shotgun” mergers, etc. for three consecutive months.

#### Lloyd's “Wall of Worry”—“It's the counterintuitive indicator: many worries, buy; few worries, sell”

“Long a part of Wall Street lore, Lloyd's Wall of Worry (a trademark of Khaner Capital Management) is a quick, handy way to gauge the emotions of investors. As interpreted by money manager Lloyd Khaner, a low wall, with seven or fewer blocks, indicates a complacent, even overconfident market: Time to take profits. A high all, with 15 or more blocks, suggests a squeamish market: Look to buy at bargain prices. In the middle range, reading the wall gets tricky; knowing not only where the wall stands but whether it's headed up or down is the key.”

December 2007: “The Crunch That Stole Christmas”

Oil Prices: The first person to predict \$200 crude is permanently off my holiday card mailing list.

Consumer Spending: Shaken but no yet deterred.

U.S. Dollar: The stalled car in the center of the ring at the worldwide currency demolition derby.

Write-offs: Sure would be nice to end the year with a one-time, penalty-free \$2 trillion non-cash write-off of every investment vehicle we don't want or understand—a.k.a. “Do Over!”

European Economies: Be careful what you wish for: the now-stalwart Euro threatens to slow the region's manufacturing exports.

Iran: They say they aren't working on nukes for weapons, and the U.S. says it has no plans to attack—so what's all the fretting about? Creditability.

U.S. Economy: Ex-the slowdowns in housing, construction, retail, restaurants and banking, things are just peachy.

The Yen: Crushing the carry trade and in the running to be the supermodel-endorsed currency.

Inflation: Still a problem, but nothing a significant global economic slowdown wouldn't solve. On second thought...

Interest rates: When someone figures out how to get the long end of the yield curve to stop rising while the short end gets cut, please give the Fed a call at 1-800-PROBLEM.

Housing Prices: Looks like some European residential real estate markets have hopped on the careening American Toboggan.

Unemployment: Fingers and toes crossed that the rate stays below 5 percent.

U.S. Mortgages: Forget about calling Cousins Freddie and Fannie to bail us out of this mess. Go straight to the top: "Hello, Uncle Sam, can you spare a few hundred billion?"

Emerging Markets: Their financial markets are correlating with us more often than not. Let's hope their economic markets don't follow ours as well.

Structured Investment Vehicles: When the next SIV is officially priced by the Markey, it will be the trade heard 'round the world.

Mergers and Acquisitions: Busted deals are littering the financial landscape like candy wrappers at a movie theater. Plenty of sequels, no happy endings.

Dividends: Financial stress is pushing companies to cut or consider cutting their payouts. A bullet proof balance sheet is worth its weight in gold right now...well almost.

### **Beta Test Website for Responsible Property Investing**

The members of the Responsible Property Investing Center (which includes ULI) has developed a web site ([www.responsibleproperty.net](http://www.responsibleproperty.net)) which is now available in its "Beta" or test version. The web site is by no means complete; the members of the Center expect to add additional research reports, case studies, and a variety of resources over the next few months.

Please take a "test drive" and let us know ([blank@uli.org](mailto:blank@uli.org)) your reactions, suggestions, etc.

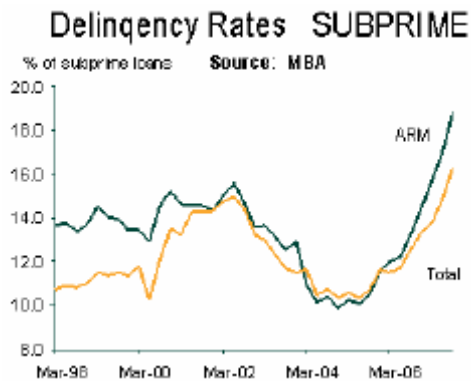
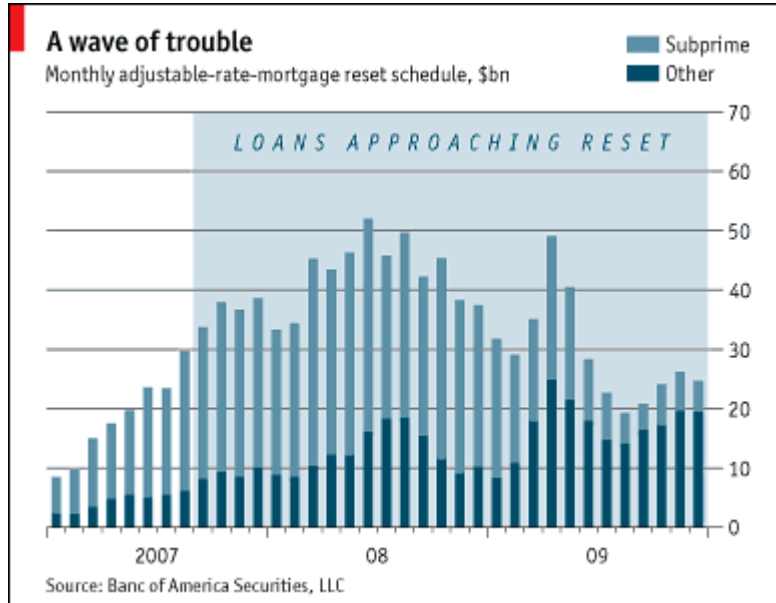
### **Special Comments: Notes from "The Punch Line...", published by Abraham Gulkowitz**

(Headlines and data in "The Punch Line" come from widely available publications including national and international newspapers, trade journals, economic and industrial bulletins and websites.)

### **Investors 'Stunned' by 20,000 Ratings Cuts [THAT IS NOT A TYPO!]**

Close to 20,000 asset-backed securities have been downgraded by the main ratings agencies this year as a result of the sub-prime mortgage crises in the U.S., a turn of events that has 'stunned' investors and provoked unprecedented levels of credit volatility this, a new report said.

## A Picture is Worth a 1,000 Words! Two Pictures are...Depressing



### Theatrics... 'Commercial Real Estate Market is Imploding'

Real estate deals are coming apart at the fastest pace since September 2001, when the economy was shrinking, because banks are tightening standards for loans, said Robert White, president of Real Capital Analytics, a New York-based research firm. About \$15 billion of commercial property (of \$10 million or more) are under contract in the U.S. compared with about \$70 billion at mid-year, White said. That's unusual because the number usually rises at year-end, he said.

### U.S. Commercial Real Estate

Investors have not returned to the commercial mortgage-backed securities (CMBS) market in significant numbers, and trust in the ratings agencies is reported very low. Since these other credit sources have dried up, banks and life insurance companies are picking up a considerable amount of commercial mortgage business. However, their willingness to add commercial mortgages to their balance sheets is said to be limited by portfolio allocation

considerations. Credit tightening continues to have the biggest impact on loans for speculative construction.

### Private Real Estate Equity

The National Council of Real Estate Investment Fiduciaries recently released the performance results of its National Property Index which is currently comprised of 5,585 properties having an estimated market value in excess of \$292 billion. The results on trailing 12-month (October 1, 2006 to September 30, 2007) were as follows:

	Total return	Income Return	Appreciation Return
All Property	17.3%	5.7%	11.1%
Multifamily	13.3%	4.9%	8.1%
Industrial	16.6%	6.4%	9.8%
Office	22.8%	5.7%	16.4%
Retail	12.9%	5.9%	6.7%

The release, which is available at NCREIF's web site at [www.ncreif.org](http://www.ncreif.org), provides information on a regional basis.

### Caution—Attitudinal Change Continue Occurring

According to the most recent survey (third quarter 2007) of institutional investor attitudes and opinions by Real Estate Research Corporation (RERC), attitudinal changes are continuing.

	3Q2007	2Q2007	1Q2007
Availability of Capital	5.9	8.2	8.7
Discipline of Capital	6.0	5.2	4.7
Scale: 1 (lowest) to 10 (highest).			

	3Q2007	2Q2007	1Q2007
Buy	5.6	4.0	4.7
Sell	5.6	7.9	7.3
Hold	6.4	6.3	6.1
Scale: 1 (lowest) to 10 (highest).			

## Conventional and Securitized Mortgages

### Indicated Spreads for Conduit Commercial Mortgages (as of December 15, 2007)

Spread over 5-Year Treasury Bonds	3.46%
Yield on 5-Year Treasury Bonds	<u>3.42%</u>
Indicated Rate	6.86%
Spread over 10-Year Treasury Bond	2.61%
Yield on 10-year Treasury Bond	<u>4.02%</u>
Indicated Rate	6.63%

### Indicated Spreads for Conventional Commercial Mortgages (as of December 13, 2007)

	Commercial Mortgage Rate Spreads for 5-10 Year Fixed-Rate Mortgages	
Property Type	<65% LTV	>65% LTV
Multifamily	+165 – 185	+180 – 220
Regional Malls	+165 – 185	+180 – 200
Strip/Power Centers	+170 – 190	+190 – 215
Multi-Tenant Industrial	+180 – 195	+190 – 200
CBD Office	+170 – 190	+195 – 210
Suburban Office	+180 – 200	+220 – 250
Full-Service Hotel	+180 – 190	+200 – 250
Limited-Service Hotel	+190 – 205	+220 – 260
	5-Year Treasury – 3.54%; 10-Year Treasury – 4.15%	
Source: Cushman & Wakefield Sonnenblick-Goldman, LLC.		