1Q 2008 PwC Korpacz RE Investor Survey Clip Report (As of 04-15-2008)

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PricewaterhouseCoopers 1Q 2008 Korpacz Real Estate Investor Survey Sees 'Rough Road' Ahead for Commercial Real Estate Industry and Investors

Prime Newswire
Posted: 2008-03-17 09:03:49

NEW YORK, March 17, 2008 (PRIME NEWSWIRE) -- The recurring waves of news about the housing downturn, job losses, the ongoing credit crunch and general slowing in the U.S. economy have begun to overflow into the commercial real estate sector, according to the 1Q 2008 edition of PricewaterhouseCoopers Korpacz Real Estate Investor Survey(r).

The survey found telltale signs of weakness in office, retail, lodging and leasing activity, while areas less affected by the broad economy, such as industrial and warehouse properties, remain stable. Rental apartments are the only area of commercial real estate benefiting as supply tightens, homeownership rates decline and the number of renters grows.

"Unexpected job losses in January and February -- particularly in the financial industries -- are beginning to have an impact on office space demand in a number of markets," said Tim Conlon, U.S. real estate leader for PricewaterhouseCoopers. "At the same time, widespread cutbacks in consumer spending are causing more pain for the nation's retail sector."

"Even though the underlying fundamentals of commercial real estate are still sound, there are noticeable cracks forming in the foundation," said Susan M. Smith, editor-in-chief of PricewaterhouseCoopers Korpacz Real Estate Investor Survey(r) and manager in PwC's real estate business advisory services group. "As a result, there is a palpable sense of uncertainty among investors we spoke with and surveyed this quarter," she said.

The report reviews comments by analysts forecasting declines in commercial real estate values of 20 percent or more, and questions how much of today's uncertainty is grounded in reality and how much is simply psychological: "Such (analyst) reports capture the attention of newsrooms and quickly filter to the industry. Has the economic prognosis for 2008 infected analysts such that commercial real estate values are really at such risk? Theoretically, it is possible for commercial real estate values to drop to the degree forecasted by these analysts. Practically, it may not be."

"(The) relationship between economics and real estate is not always clear cut. Both are cyclical and need to be looked at jointly, as well as independently, especially during fragile times of economic uncertainty," the report notes.

Other key findings include:

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* Despite year-over-year declines in absorption, overall
     absorption remains positive for many of the nation's central
     business district (CBD) markets, with rental rates holding
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steady and even rising in some markets. (For this quarter, the average initial-year market rent change rate for the CBD office market held relatively steady at 4.05 percent -- one of the highest rates ever recorded for this market in the Survey.)

* In the national suburban office market, the pace of leasing has decelerated noticeably. Even so, developers have forged ahead with new office projects that continue to increase the level of supply in many markets. At the same time, the amount of speculative space has greatly increased, growing from 60.0 percent to 85.0 percent of the total suburban office market. Suburban office markets posting some of the highest additions to supply in the fourth quarter of 2007 included Phoenix (4.0 million square feet), Northern Virginia (3.2 million square feet) and Dallas (2.7 million square feet).

* The subprime mortgage crisis is actually helping to enhance the national apartment market as woes in the residential market force more people back into the rental pool, while existing renters find the idea of homeownership to be cost-prohibitive. In addition, a continued restraint on new building by apartment developers is holding down the level of supply.

Additional findings by sector include:

Retail

Declining consumer confidence, a sharp rise in personal bankruptcy filings and a drop-off in consumer spending are taking their toll in the regional mall market. In December, 2007, comparable same-store retail sales posted a 0.10 percent year-over-year decrease, compared to a year-over-year growth rate of 3.8 percent in the prior month and 3.1 percent a year earlier. At the same time, the Consumer Confidence Index fell from 90.6 in December 2007 to 75.0 in February 2008 -- the lowest in 12 months, and well below the 103 average throughout much of 2007.

Lackluster retail sales growth and weaker consumer spending are also causing would-be investors in the national power center market to exercise much more scrutiny and more conservative underwriting, with big-box retailers maintaining a significant role in the sector. According to investors surveyed, overall cap rates (OARs) continue to vary based on a power center's percentage of big-box space, averaging 7.13 percent for properties with 100.0 percent big-box space, compared to 7.27 percent for properties where 85.0 percent of the gross leasable area (GLA) is occupied by big-box tenants and 7.38 percent for properties where 75.0 percent of the GLA is occupied by big-box tenants.

Rising vacancy rates continue to impact community/neighborhood shopping centers -- the result of a slowdown in tenant expansions and constant additions to supply. In the fourth quarter of 2007, approximately 12.0 million square feet were completed in the U.S. community/neighborhood shopping center sector -- the highest quarterly total in three years. Even so, regions with significant population growth report relatively strong results, including West Coast markets such as Orange County, Los Angeles, Seattle, San Francisco and San Diego, as well as certain infill areas such as Suburban Maryland and Northern Virginia. In addition, soaring population growth in Georgia has led to strong demand for retail goods and services, making Atlanta a top pick for institutional investors looking to acquire strip shopping center assets.

Office

In the face of declining absorption levels in many major central business districts (CBDs) during the past several months, the recently released U.S. employment figures showing reconfigured job losses of 22,000 in January and 63,000 in February added a new concern for landlords and investors. Among the hardest hit were office-using employment sectors such as financial services and professional-and-business service entities. Individual CBDs that reported sharp declines in overall absorption in 2007 included Chicago, midtown and downtown Manhattan, Houston and Washington, D.C. In contrast, CBDs that reported strong gains in overall absorption in 2007 included Los Angeles, Atlanta, Bellevue, WA and Baltimore.

In the national suburban office market, leasing activity slowed noticeably thanks to a continuing sluggish economy. Even so, the pace of new construction, much of it speculative space, continued to increase -- leading to growing investor concerns about the long-term effects of oversupply. Suburban office markets posting some of the highest additions to supply in the fourth quarter of 2007 included Phoenix (4.0 million square feet), Northern Virginia (3.2

million square feet) and Dallas (2.7 million square feet).

Industrial

Although individual market performances vary, overall, the national flex/R&D market is seeing a steady increase in demand, thanks to steady growth in the high-tech sector and higher rental rates in comparable office building locations. The tightest markets tend to be located along the West Coast and include long-standing favorites like Silicon Valley, La Jolla and Los Angeles/Orange County. During the past quarter, the average overall cap rate for the national flex/R&D market stood at 7.47 percent, 100 basis points above that for the national warehouse market. Even though investments in flex/R&D can run "hot and cold," the potential for higher returns is quite appealing to investors, the report says.

Warehouse

Favorable supply-demand fundamentals and the sector's minimal sensitivity to changing consumer spending habits or job growth are helping to reinforce the warehouse sector's image as a "safe haven" for many investors. And while the credit crunch did affect would-be buyers' ability to acquire debt toward the end of 2007 (resulting in a 22.0 percent decline in sales of significant properties in the fourth quarter), huge portfolios in the first half of 2007 made it a record year in terms of sales volume. All told, more than $46.0 billion of industrial properties changed hands in 2007, a 7.0 percent increase over 2006. Warehouse markets that attracted the most dollars from investors in 2007 were Los Angles ($2.9 billion), Chicago ($2.2 billion), Seattle ($1.1 billion), Dallas ($1.1 billion), and Atlanta ($1.0 billion). Warehouse markets reporting the highest average prices per square foot included the New York City boroughs ($152.00 per square foot), San Diego ($149.00 per square foot), Los Angeles ($140.00 per square foot) and Orange County ($131.00 per square foot).

Apartments

Growth in the number of renters -- due in part to residential owners, hard-pressed by the subprime mortgage fallout, returning to the market, and also to the inability of existing renters to afford to become homebuyers -- is actually helping to spur demand in the national apartment market. At the same time, apartment developers nationwide have exercised a continued restraint on new building, thereby holding down additions to supply. At year-end 2007, the top five apartment markets in terms of lowest vacancy rates were New York (2.1 percent), Long Island (3.0 percent), Northern New Jersey (3.2 percent), Fairfield County, CT (3.3 percent) and Central New Jersey (3.4 percent). The top five apartment markets for total sales volume in 2007 were Manhattan ($8.0 billion), Washington D.C./Northern Virginia ($3.7 billion), New York City boroughs ($2.0 billion), Chicago ($1.9 billion) and Los Angeles ($1.6 billion).

Net Lease

The old saying that "cash is king" became especially evident in the national net lease market as transaction activity plunged during the fourth quarter of 2007 -- a sharp response to the ongoing credit crisis. Between the third and fourth quarters of 2007 the number of net lease assets sold fell 73.0 percent -- down from 12,266 in the third quarter to a mere 3,290 in the fourth quarter of 2007. The greatest drop in transactions (77.6 percent) occurred in the office sector, where a total of 18,164 net lease assets were available for sale at year-end 2007, down about 25 percent from the third quarter. Retail assets led the offerings (9,558 assets), followed by office (5,082 assets) and industrial (3,528 assets).

National Lodging

The slowdown in the U.S. economy, combined with increasing consumer restraint in discretionary spending are being felt in the U.S. lodging industry, which experienced a slowing in the growth of two key industry averages, average daily rate (ADR) and revenue per available room (RevPAR) in 2007. Even so, industry profits are forecast to rise steadily -- from $28.0 billion in 2007 to $29.6 billion in 2008 and $32.5 billion in 2009.

At the same time, growth in new supply has accelerated over the past two years, with room starts rising from 139,700 in 2006 to 141,500 in 2007. These numbers compare favorably to the construction levels recorded between 2001 and 2005, when new room starts ranged from 68,400 in 2002 to 90,500 in 2001 and averaged 80,220. Even though no immediate threat of an oversupply exists, many investors express concern about the timing of many new projects, although their fears seem to be eased somewhat by the fact that stricter underwriting guidelines from lenders, high land prices, and higher construction costs for material and labor will likely lead to the delay, postponement or cancellation of some projects.

PricewaterhouseCoopers Korpacz Real Estate Investor Survey(r), now in its 21st year of publication, is one of the industry's longest continuously produced quarterly surveys. The current report provides detailed overviews of 29 separate markets, including the national retail markets (regional mall, power center and strip shopping centers);

overviews of 18 major office markets, including the recently added markets of Charlotte, Denver, Phoenix and San Diego; and national overviews of the CBD and Suburban Office, Flex/R&D, Warehouse, Apartment, Net Lease and National Lodging Markets. The report also features up-to-date commentaries concerning Valuation Issues, Technology News and Trends and Economic News. New this quarter is a forecast of overall capitalization rates, as well as a breakout of key indicators -- discount rates, overall cap rates, and residual cap rates -- for each surveyed market.

Information about subscribing to PricewaterhouseCoopers Korpacz Real Estate Investor Survey(r) can be found at www.pwcreval.com. Members of the media can obtain an electronic copy of the full report by contacting Thomas Derr at thomas.derr@us.pwc.com or (646) 471-8268.

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Its global real estate professionals offer in-depth experience in a wide range of financial accounting and reporting issues; global tax solutions; investment fund structuring; capital market transactions; securitization issues; technological applications; systems and operations; due diligence and transaction support; and valuation management.

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Commercial Real Estate Investors See Rough Road Ahead, Despite Strong Fundamentals

Commercial real estate investors see a rough road ahead according to the latest quarterly PricewaterhouseCoopers Korpacz Real Estate Investor Survey (www.pwcreval.com), released today.

New York, NY (PRWEB) March 18, 2008 -- Commercial real estate investors see a rough road ahead according to the latest quarterly **PricewaterhouseCoopers Korpacz Real Estate Investor Survey** (www.pwcreval.com), released today. According to the report, the commercial real estate market is showing telltale signs of weakness in office, retail, lodging and leasing activity, while areas less affected by the broad economy, such as industrial and warehouse properties, remain stable. Rental apartments are the only area of commercial real estate benefiting as supply tightens, homeownership rates decline and the number of renters grows.

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"Even though the underlying fundamentals of commercial real estate are still sound, there are noticeable cracks forming in the foundation," said **Susan M. Smith**, editor-in-chief of PricewaterhouseCoopers Korpacz Real Estate Investor Survey® and manager in PwC's real estate business advisory services group. "As a result, there is a palpable sense of uncertainty among investors we spoke with and surveyed this quarter," she said.

Key findings include:

Retail
Declining consumer confidence, a sharp rise in personal bankruptcy filings and a drop-off in consumer spending are taking their toll in the regional mall market. Lackluster retail sales growth and weaker consumer spending is causing would-be investors in the national power center market to exercise much more scrutiny and more conservative underwriting, with big-box retailers maintaining a significant role in the sector.

Rising vacancy rates continue to impact community/neighborhood shopping centers – the result of a slowdown in tenant expansions and constant additions to supply. In the fourth quarter of 2007, approximately 12.0 million square feet were completed in the U.S. community/neighborhood shopping center sector – the highest quarterly total in three years. Even so, regions with significant population growth report relatively strong results, including West Coast markets such as Orange County, Los Angeles, Seattle, San Francisco and San Diego, as well as certain infill areas such as Suburban Maryland and Northern Virginia.

Office
The ongoing decline in U.S. employment has added a new concern for landlords and investors of office properties. Among the hardest hit were office-using employment sectors such as financial services and professional-and-business service entities. Individual commercial business districts (CBDs) that reported sharp declines in overall absorption of office space in 2007 included Chicago, midtown and downtown Manhattan, Houston and Washington, DC. In contrast, CBDs that reported strong gains in Los Angeles, Atlanta, Bellevue, WA and Baltimore.

In the national suburban office market, leasing activity also slowed noticeably. Even so, the pace of new construction, much of it speculative space, continued to increase – leading to growing investor concerns about the long-term effects of oversupply. Suburban office markets posting some of the highest additions to supply in the fourth quarter of 2007 included Phoenix (4.0 million square feet), Northern Virginia (3.2 million square feet) and Dallas (2.7 million square feet).

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Although individual market performances vary, overall the national flex/R&D market is seeing a steady increase in demand, thanks to steady growth in the high-tech sector and higher rental rates in comparable office building locations. The tightest markets tend to be located along the West Coast and include long-standing favorites like Silicon Valley, La Jolla and Los Angeles/Orange County. During the past quarter, the average overall cap rate for the national flex/R&D market stood at 7.47 percent, 100 basis points above that for the national warehouse market. Even though investments in flex/R&D can run "hot and cold," the potential for higher returns is quite appealing to investors, the report says.

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Favorable supply-demand fundamentals and the sector's minimal sensitivity to changing consumer spending habits or job growth is helping to reinforce the warehouse sector's image as a "safe haven" for many investors. And while the credit crunch did affect would-be buyers' ability to acquire debt toward the end of 2007, huge portfolios in the first half of 2007 made it a record year in terms of sales volume.

Net Lease
The old saying that "cash is king" became especially evident in the national net lease market as transaction activity plunged during the fourth quarter of 2007 – a sharp response to the ongoing credit crisis. Between the third and fourth quarters of 2007 the number of net lease assets sold fell 73.0 percent. The greatest drop in transactions, occurred in the office sector, where a total of 18,164 net lease assets were available for sale at year-end 2007, down about 25 percent from the third quarter. Retail assets led the offerings, followed by office, and industrial.

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Real Estate

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http://realty.blogforward.com/news/3421/commercial-real-estate-investors-see-rough-road-ahead-despite-strong-fundamentals.html

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Source: PRWeb: Business Real Estate

CPN: Commercial Property News

Survey Says Commercial Real Estate Headed for Turbulence

March 17, 2008
By: Barbra Murray, Contributing Editor

After years of multi-billion-dollar transactions and mega-developments, much of the commercial real estate sector is beginning to feel the burn as the economy loses speed, jobs disappear and the lending market continues to stifle borrowers, according to the **First Quarter 2008 PricewaterhouseCoopers Korpacz Real Estate Investor Survey**. However, the future may not be as grim as some would think.

There are exceptions but overall, the national office, retail and hospitality markets are losing steam. Development in suburban office markets, particularly speculative projects, continues despite the fact that leasing activity has declined. The regional retail market is suffering as consumers bull back on spending, thereby leading to retailers' vacating of space. And after rebounding from the sudden decline induced by 9/11, the hotel industry is not flourishing as it had been, as is evidenced by slowdowns in the overall ADR and RevPar. "Are we at the tip of the iceberg?", **Susan Smith,** PwC Korpacz survey editor-in-chief and manager in PwC's Real Estate Business Advisory Services Group, pondered when speaking to *CPN* today. "Yes. I think we're going to see more job loss as a lot of banks and financial institutions are going to have layoffs in the next few months."

Yet each commercial real estate sector has its upside. In the office market, overall absorption in a significant number of central business districts is still positive, and rental rates are stable if not on the rise in some markets. The retail sector is growing stronger in areas with rapidly booming populations, such as Southern California's major metropolitan areas, as well as San Francisco and Seattle. And lodging industry profits are expected to increase at a steady pace, going from $28 billion in 2007, to an anticipated $29.6 million this year, and $32.5 billion in 2009.

While there is some bad news for the national office, retail and lodging markets, on the whole, the industrial and apartment sectors appear to be quite healthy. Prompted by continued growth in the high-tech industry and increasingly high office rents, the flex/R&D market is experiencing higher demand. Additionally, the warehouse market is doing well, as it is not significantly affected by decreases in consumer spending or job losses. And with the single-family housing market having taken a massive plunge, the apartment market is, conversely, on the rise, benefiting from the vast pool of previous homeowners now seeking rentals.

Overall, while bumps in the road will continue for commercial real estate, a return to the good times may not be too far away. "The industry has learned from past mistakes," Smith said. "So with the relative balance of supply and demand, we're hopeful that commercial real estate will persevere and pull out of the recession relatively quickly."

Monday, Mar. 17 2008

Economic Weakness Rattles Commercial Real Estate Investors

John Spence
MarketWatch Pulse

BOSTON -- The residential housing bust, job losses, credit problems and weakness in the U.S. economy are spilling into commercial real estate, according to a first-quarter survey from PricewaterhouseCoopers. "Unexpected job losses in January and February -- particularly in the financial industries -- are beginning to have an impact on office space demand in a number of markets. At the same time, widespread cutbacks in consumer spending are causing more pain for the nation's retail sector," said **Tim Conlon**, U.S. real estate leader for **PricewaterhouseCoopers**. "Even though the underlying fundamentals of commercial real estate are still sound, there are noticeable cracks forming in the foundation. As a result, there is a palpable sense of uncertainty among investors we spoke with and surveyed this quarter," added **Susan Smith**, editor-in-chief of the **PricewaterhouseCoopers Korpacz Real Estate Investor Survey**.

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ATLANTA BUSINESS CHRONICLE

Monday, March 17, 2008 - 11:10 AM EDT

PricewaterhouseCoopers: Atlanta office market made absorption gains in '07

Atlanta Business Chronicle

PricewaterhouseCoopers Korpacz' Real Estate Investor survey for the first quarter of 2008 has noted growing weakness in office, retail, lodging and leasing activity, but the news wasn't all bad for Atlanta.

The report said Atlanta's central business district was one of the few among the major metros to show strong gains in overall absorption in 2007. The report describes Atlanta's office market as a buyer's market. This is due mostly to office closings, downsizings of mortgage-related firms, the consolidation of space after mergers and continuing construction, especially in the suburban market. The report noted some 4.5 million square feet of new office space in the Atlanta suburbs is set to come online this year and in 2009.

However, investors are beginning to worry the weakening Atlanta job market could boost vacancy levels that already rank among nation's highest.

Atlanta's warehouse market also fared well, attracting some $1 billion from investors last year, the report said. And the continuing population boom in Georgia has caused strong demand for retail goods and services, making Atlanta a top pick for institutional investors who want to buy strip shopping center assets.

Nationally, the housing downturn, job losses, ongoing credit crunch and slowing of the U.S. economy has started to overflow into the commercial real estate sector, the report said. The survey found signs of weakness in office, retail, lodging and leasing activity, while areas less affected by the broad economy, such as industrial and warehouse properties, remained stable. Rental apartments are the only area of commercial real estate benefiting as supply tightens, home ownership rates decline and the number of renters grows, the report noted.

"Even though the underlying fundamentals of commercial real estate are still sound, there are noticeable cracks forming in the foundation," said **Susan M. Smith**, editor-in-chief of **PricewaterhouseCoopers Korpacz Real Estate Investor Survey** and manager in PwC's real estate business advisory services group. "As a result, there is a palpable sense of uncertainty among investors we spoke with and surveyed this quarter," she said.

The Atlanta Journal-Constitution
ajc.com
Business

Skyline: Novare assembles tracts in Midtown:

INSIDE METRO ATLANTA COMMERCIAL REAL ESTATE

Staff
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20 March 2008
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Atlanta's biggest condominium builder, Novare, has assembled several tracts in Midtown a half-mile south of the future Trump Tower, Databank says.

Novare, the developer of Viewpoint and the residences at 3630 Peachtree, is focusing on Spring Street between 12th and 13th streets, where it might build more than 400 units and possibly retail, Databank says.

The **real estate** sales tracker counts four Novare purchases there costing $4.7 million, $5.3 million, $3.8 million and $2.5 million.

Other well-known Novare projects are Eclipse, Metropolis, Gallery, the Atlantic and Twelve Centennial Park.

IN THE WORKS

Ram, a development company based in Palm Beach Gardens, Fla., has opened an office at the Biltmore, 817 West Peachtree St. in Midtown.

"We are extremely bullish about Atlanta and have a number of new projects in progress in this area at the moment," said Ken Baye, Ram senior vice president in charge of the new Atlanta office.

Ram plans to build midrise, loft-style apartments on the 17.4-acre former Home Depot Expo site, now home to the PGA Superstore. The site is close to the Lindbergh MARTA station. Construction is expected to begin in the summer.

Ram also bought 6.6 acres in Snellville and plans to redevelop the former Home Depot Landscape Supply site, plus 4.5 acres on Scenic Highway, into a retail center.

ABOUT THE MARKET

Population growth in Georgia has led to strong demand for retail goods and services, making Atlanta a top pick for institutional investors looking to acquire strip shopping center assets, according to the first-quarter **PricewaterhouseCoopers Korpacz Real Estate Investor Survey.**

As for offices, Atlanta has increasingly become a buyer's market --- the result of office closings, downsizings of mortgage-related firms, consolidation of space because of corporate mergers

and new construction, particularly in the suburban market, where 4.5 million square feet of new office space is scheduled for delivery this year and next, the survey says.

It goes on to say that Atlanta was fifth in the nation last year in warehouse investment. While Chicago, New York, Houston and Washington saw sharp declines in central business district office space absorption, Atlanta saw a gain, according to the report.

TODAY'S BIG NUMBER

$18.4

In millions, the selling price of the Hampton Hills apartment complex on Roswell Road in Dunwoody.

Source: Databank

TRANSACTIONS

The Simpson Organization of Atlanta paid SunTrust Bank $8.2 million for its office building and 4.8 acres at 121 Perimeter Center West, according to Databank.

The property is near the W Atlanta-Perimeter Hotel. The bank is leasing back the space. GE Capital loaned $5.5 million in the deal.

Russell New Urban Development has acquired 3.2 acres worth $3 million south of the Georgia Dome to build condominiums, Databank says.

The seller was Carver Bible College. Russell plans to build condos next year or in 2010, Databank says.

NOW SELLING

Atlanta **real estate** investment company Branch Properties is selling 0.85 of an acre at Camp Creek Pointe, a mixed-use development in East Point across from Camp Creek Marketplace. The asking price is $2.7 million.

Branch bought 14.5 acres there two years ago for $4.5 million.

The tract, at Camp Creek Parkway and North Commerce Drive near I-285, is being developed and will contain a Starbucks and T-Mobile store housed in a 4,400-square-foot building.

Camp Creek Pointe's other developments include two hotels nearing completion: a 128-room Courtyard Marriott scheduled to open in July and 119-room Hampton Suites scheduled to open in May.

The property is three miles from Hartsfield-Jackson International Airport. Greg Hagan is the broker.

COMING UP

Central Atlanta Progress and the Atlanta Downtown Improvement District are scheduled to hold their annual meeting Wednesday at the Georgia World Congress Center. Networking begins at 7 a.m. and the meeting an hour later. For more information, go to www.atlantadowntown.com .

ULI Atlanta and Emory University will hold a panel discussion Wednesday on "Walkable Cities: Gauging Atlanta's Progress." The event begins at 6 p.m. at the Goizueta Business School.

For more information, go to www.uli.org/events/index.cfm?id=3398 or call 1-800-321-5011. To register, go to www.uli.org/register/index.cfm?id=3398 .

To have an item considered for publication in Skyline, please send it to Kevin Duffy at The Atlanta Journal-Constitution, P.O. Box 4689, Atlanta, GA 30030; or to kduffy@ajc.com. Include proper names and positions. Photographs must carry identification and can't be returned. In order for us to contact you, please include a phone number and/or e-mail address.

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The Washington Times

Business

Office space slowing down

March 20, 2008

The slowdown in commercial real estate that some industry executives said would bypass the Washington area appears to have arrived.

All three of the region's submarkets — Washington, suburban Maryland and Northern Virginia — are reporting slower sales and leasing activity as they finish compiling statistics for 2007, according to the financial services firm **PricewaterhouseCoopers**.

The vacancy rate in suburban Maryland rose from 10.3 percent at the beginning of 2007 to 11.9 percent by the end of the year, the firm said in a report this week.

Vacancy rates in Washington and Northern Virginia held steady, but leasing activity and sales inquiries slowed.

Similar trends are continuing into 2008.

"Unexpected job losses in January and February — particularly in the financial industries — are beginning to have an impact on office space demand in a number of markets," said **Tim Conlon, U.S. real estate leader for PricewaterhouseCoopers.** "At the same time, widespread cutbacks in consumer spending are causing more pain for the nation's retail sector."

Demand for commercial space in Northern Virginia was diluted by a fast construction pace. In the fourth quarter of last year, 3.2 million square feet of commercial space was added to Northern Virginia's market, which ranked with the Phoenix area as having the fastest growth rates for office properties in suburban markets nationwide.

Any downturn in the Washington area's real estate market is slight compared with other regions.

The American Institute of Architects reported this week that its Architecture Billings Index dropped to its lowest level since the dot-com bust of October 2001.

"This is a clear indication that there could be tougher times ahead for design firms and a noticeable slowdown in commercial construction projects coming online in the foreseeable future," said Kermit Baker, chief economist for the American Institute of Architects.

Gloomy forecasts for the Washington area could not be found in a different market forecast this week by the real estate services firm Marcus & Millichap.

While the rest of the country is confronting job losses, employers are expected to create 25,000 new jobs in the Washington area this year, Marcus & Millichap reported. Office vacancies in the District are likely to end the year at a moderately healthy rate of 9.9 percent.

"Properties in close-in suburbs become more valuable every year, and the redevelopment of old

assets in areas such as College Park and Falls Church could provide significant returns for patient investors," said Ramon Kochavi, Marcus & Millichap's Washington regional manager.

• Construction bids are due next week on Camden USA's planned 682,000-square-foot mixed-use apartment and retail complex at 60 L St. NE in the so-called NoMa neighborhood.

The two-building complex would be surrounded by other NoMa — North of Massachusetts Avenue — projects that are transforming the neighborhood into a vibrant business and residential submarket. The other projects include National Public Radio's new headquarters, a new Justice Department building and Bristol Group's NoMa Station.

Work on the first building, with about 300,000 square feet and 319 apartments, is scheduled to be completed in 2010.

• *Property Lines runs on Thursdays. Call Tom Ramstack at 202/636-3180 or e-mail tramstack@washingtontimes.com.*

CHICAGOBUSINESS
POWERED BY CRAIN'S

Investors forecast dip in local office values

By Eddie Baeb
March 24, 2008

(Crain's) — Office building investors are down on Chicago.

In the quarterly **PricewaterhouseCoopers Korpacz Real Estate Investor Survey**, Chicago was the only one of 18 markets in the survey where respondents forecast property values to fall over the next year.

Investors predict values will drop 1.3% in the Chicago area, compared with expectations of a 2.2% gain for downtown office buildings nationwide and a smaller 0.3% gain for suburban office buildings.

In the Chicago area, office buildings' overall capitalization rates — the measure of first-year yields — are forecast to climb from 7% today to 7.3% in six months. Downtown buildings nationwide, meanwhile, stand at 6.63% today and are forecast to climb 28 basis points to 6.91%, according to the survey. Cap rates tend to rise when prices fall.

CAP RATES, VALUES

Institutional investors are predicting that overall capitalization rates, the measure of first-year yields, of office buildings in Chicago will rise while prices will fall. Chicago was the only market included in the survey where investors forecast a decline in value.

	1st-qtr. cap rate	Change in cap rates forcast for next 6 months	Value change forecast for next 12 months
Chicago	7.0%	+30 basis points	-1.3%
Atlanta	7.1%	+37.5 basis points	+1.2%
Boston	7.3%	+25 basis points	+1.4%
Dallas	8.0%	+37.5 basis points	+1.7%
Houston	7.3%	+79.2 basis points	+3.43%
Los Angeles	6.16%	+20.8 basis points	+2.94%
Manhattan	5.55%	+25 basis points	+6.21%
San Francisco	6.11%	+28.1 basis points	+4.61%
Washington, D.C.	6.16%	+16.7 basis points	+4.06%
Nat'l Downtown	6.63%	+28.1 basis points	+2.23%
Na'tl Suburban	7.13%	+42.5 basis points	+0.27%

Source: PricewaterhouseCoopers Korpacz Real Estate Investor Survey

"Investors perceive Chicago as having a little more risk," says **Susan Smith**, a manager in the real estate group of **PricewaterhouseCoopers LLP** and editor-in-chief of the Korpacz survey. "Chicago is definitely lagging the other markets."

To Robert Six, senior vice-president of marketing and leasing with Chicago-based Zeller Realty Group, the survey results suggest that investors think Chicago's absorption — the measure of office space demand — will continue to decelerate and become negative. Also, he says, people are growing increasingly concerned about the economy, and are anxious to see whether investors who bought buildings in highly leveraged deals in recent years can succeed.

There have been so few office building sales in recent months that it is difficult for investors to gauge what is happening with prices.

“If the first quarter is any indication, volume has fallen off the precipice,” Mr. Six says.

One survey respondent puts the stalemate between buyers and sellers more colorfully: “No one wants to be the first one to jump off the diving board and test the water only to find out the pool’s been drained.”

But clearly, the landlord’s market that was apparent the last couple years may be short-lived. Already, according to the survey, conditions may be moving back to favoring tenants even before 2009, when several new office towers are to open downtown.

Of the 18 major office markets in the survey, Chicago landlords were offering among the most lucrative concession packages to tenants, including an average of more than five months of free rent.

“This figure reflects (the Chicago market’s) current struggles due to a slow-moving recovery and persistent additions to supply,” the Korpacz report says.

The PricewatehouseCoopers survey is sent to about 130 institutional investors each quarter.

Business

Reports pointing to downturn in office rentals

By Robert Manor, TRIBUNE REPORTER
519 words
21 March 2008
Chicago Tribune
Chicago Final
3
English
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If anyone needed further proof that the economy is heading into recession, several reports on commercial real estate provide it, including one released Thursday that showed Chicago is not immune to a downturn in demand for office space.

"The housing recession is now migrating into other parts of the economy, and we are seeing a drop in employment," said Paul Kasriel, chief economist for Northern Trust Co. "That is going to lower the demand for office space."

Jones Lang LaSalle's "Skyline Review," released Thursday, said Chicago's office market may get through 2008 without too much damage, but that 2009 will likely be much worse.

The company said downtown Chicago's vacancy rate for top-quality offices is now a little below 8 percent.

"An economic downturn coupled with significant new inventory could push the Class A vacancy rate back up to 11 percent by late 2009," said Rena Christofidis, vice president of Chicago Market Research at Jones Lang.

That is considered high enough that tenants can demand concessions and breaks on rent, but is well below 2007's national average of 15 percent.

Class A buildings are first-class properties that typically have the lowest vacancy rate, and 11 percent is considered uncomfortably high.

In recent months the Bank of America has bought LaSalle Bank, while the Chicago Mercantile Exchange acquired the Chicago Board of Trade.

Jones Lang LaSalle noted that the four companies occupy space in 11 buildings, and that a significant part of that office space is likely to go back on the market, increasing available supply.

On the other hand, Chicago's financial services industry, a huge tenant of office space, has avoided the kind of meltdown seen at Bear Stearns Cos. and other companies.

Economists say commercial real estate downturns typically occur after weakness appears in residential real estate, which is in the deepest slump in more than 50 years. And commercial real estate's troubles typically become apparent after an economic downturn has been under way for some time.

Douglas Porter, deputy chief economist of BMO Capital Markets, said the weakening in commercial real estate is apt to grow worse.

"That is a sector we have become increasingly concerned about in the last couple months," Porter said.

Moody's/REAL Commercial Property Price Indices show that prices nationwide dropped for the third consecutive month in January and are 2.4 percent below their peak in October.

" Moody's expects commercial property prices to fall approximately 15 to 20 percent before bottoming out," the company said.

In a report called "Rough Road Ahead for Investors," **PricewaterhouseCoopers** says job losses and financial markets turmoil are likely to bruise commercial real estate.

"After speaking to numerous investors this quarter, I am sorry to write that things will probably get worse before they get better," said **Susan Smith**, editor of the report.

As with all kinds of real estate, local conditions greatly affect prices and rents. The numbers **PricewaterhouseCoopers** and Moody's cite apply to many U.S. markets.

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rmanor@tribune.com

Los Angeles Times

SUNDAY PROFILE

He quietly built an empire

One of Southern California's largest office landlords, Dan Emmett prefers keeping a low profile and is notoriously press shy.

By Roger Vincent, Los Angeles Times Staff Writer
March 23, 2008

One of Southern California's largest office landlords, Dan Emmett, apparently missed all the memos from Donald Trump about how to act like a real estate mogul.

Although his company owns one of the most desirable office towers in the region, Emmett's personal office is blocks away in a Santa Monica low-rise. On his utilitarian desk, homemade paper signs taped to boxes say "in" and "out."

Notoriously press shy, the 68-year-old Emmett is so little known that people often assume his first name is Douglas because the company he co-founded in 1971 with Jon Douglas is called Douglas Emmett Inc. Each of them put up $7,500 to start developing apartment houses on the Westside.

"I get called Doug all the time," Emmett said.

Today Douglas Emmett is a public company with more than $6 billion in assets including the tallest building in Santa Monica, which consistently commands some of the highest office rental rates in the region and has few vacancies.

"We bought it during a recession," Emmett explained, as if the purchase might be considered extravagant because "trophy properties usually trade at a premium."

Buying real estate at the right time sounds simple enough, but Emmett has a special knack for it, said Douglas, who is no longer involved in daily operations of the company. "The guy has great intuition and great judgment."

Because profits were hard to come by in the early years, Douglas started a residential real estate brokerage on the side "to get some cash we could live on," he said. By the time the partners sold it in 1997, Jon Douglas Co. was one of the biggest brokerages in the country.

Meanwhile Emmett, as chairman of Douglas Emmett, kept a low profile while acquiring buildings in desirable locations, especially the Westside.

Most of them are offices the company leases to small white-collar businesses, but Douglas Emmett also owns a handful of prime oceanfront apartment buildings in Santa Monica and Hawaii, along

with the Sherman Oaks Galleria.

The storied mall celebrated in pop culture as the lair of the San Fernando "Valley Girl" was renovated by Douglas Emmett in the late 1990s and turned into a combined office, shopping and entertainment complex.

In recent months, waves of news about the housing downturn, job losses and ongoing credit crunch have begun to depress the commercial real estate sector. **PricewaterhouseCoopers** last week reported that employment cutbacks were beginning to have an effect on office space demand in several markets, and some analysts are forecasting declines in commercial real estate values of 20% or more.

The downturn may create pitfalls for Douglas Emmett as well as opportunities -- with the backing of its institutional investors such as pension funds -- to pick up more properties, the chairman said.

"We're not immune to national trends," Emmett said. "But our fundamentals are still excellent. Rents are higher than they have ever been."

Although he has avoided the limelight, Emmett is a lifelong Republican and an environmental activist. Being a stalwart Republican pushing a "green" agenda makes him a bit of an oddity, he said.

"It's a tragedy," Emmett said, that environmentalism "got pigeonholed" as a Democratic Party platform plank, because it should be a nonpartisan issue.

While working on a statewide green building initiative with Gov. Arnold Schwarzenegger, Emmett said, it became clear to him that laws and public policies lagged behind science and public awareness.

To help prepare lawyers to address such challenges, Emmett recently contributed $5 million to establish a center on climate change and endow a chair in environmental law at UCLA Law School -- the first such program in the nation.

"It's a pathbreaking gift," said Michael Schill, dean of the law school. And it will be used to leverage another $5 million in donations to match it.

"This will allow us to become the No. 1 environmental law program in the country," Schill said. "We will translate research findings into something people will be able to implement."

Emmett's aversion to publicity was nurtured by his father, a farmer in California's Central Valley. He was a World War I veteran and pilot who commuted by plane to Sacramento to serve in the state Assembly before his son was born. To a young Emmett he repeated the old ditty about "fools' names and fools' faces" often appearing in public places.

In years when the family farm's crops and cattle were good, the Emmetts vacationed abroad and the future businessman picked up an urge for adventure. Emmett became an avid outdoorsman who has skied, dived, kayaked and bicycled all over the globe. He climbed most of the world's seven highest mountains and led the second successful U.S. climb of Mt. Everest.

Tall and lean, Emmett still looks athletic even though he no longer scales tall peaks. He's not shy, but friends describe him as reserved and courtly.

"He is a true gentleman in a rough-and-tough industry," said former competitor Richard Ziman.

Emmett's affinity for the outdoors and the nudging of his children prompted him to look into the green movement. An experimental energy-reduction program at one of his company's buildings in the early 1990s led to more than 50% savings in energy costs, and "we became hooked as businesspeople," he said.

From then on, energy-saving practices became standard for Douglas Emmett buildings.

"Dan is a serious, dedicated entrepreneur who has been very disciplined," said Ziman, who sold Arden Realty Inc. for more than $3 billion in 2005. "That's why he has been singularly successful over the years."

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Rocky Mountain News.com

Denver office market out-performing nation

Monday, March 17 at 1:53 PM

The Denver office market, led by downtown, is out-performing the nation as a whole, shows the first-quarter **PricewaterhouseCoopers Korpacz survey** of commercial real estate industry leaders and investors.

Nationwide, the commercial real estate industry – especially retail and office – sectors are weakening.

The CBD's vacancy rate is slightly below 9 percent, according to Cushman & Wakefield, while Class-A downtown space has on overall vacancy rate of 5.9 percent in the fourth quarter, down from 6.1 percent in the third quarter, according to Cushman & Wakefield.

"Diminishing available space has resulted in speculative development in the CBD," according to the report. It points to 1001 Seventeenth Street and 1400 Wewatta Street projects, which together will add about a millions square feet of space when they open later this year.

In addition, another new building, 1900 Sixteenth Street, will bring another 335,000 square feet of new space to the market.

"These additions to inventory are anticipated to ease the tightness in the CBD over the next 18 to 24 months, according to the report.

"Favorable vacancy rates and resulting rental rate growth continue to attract investors to the Denver office market," the report continues. "However, the velocity of transactions has slowed relative to the robust activity in early 2007."

The report also notes that cap rates rose by 22 percent, at an average of 6.63 percent in the first quarter, which is to be expected given the slowdown in sales and unstable capital markets.

"We do not see a major surge in overall cap rates," one person who responded to the **PricewaterhouseCoopers Korpacz survey** said. "We will see a truing up of cash flows before we see dramatic increases in yield rates."

Rebchook on Real Estate
Insights gleaned from John Rebchook's 25 years of reporting on Denver's residential and commercial real estate. Send your questions and comments to rebchookj@rockymountainnews.com.

The Star-Ledger
THE VOICE OF NEW JERSEY

Commercial real estate faces a gloomy future

IAN T. SHEARN
STAR-LEDGER STAFF
761 words
20 March 2008
The Star-Ledger
FINAL
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English
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The tone was upbeat and the discourse was cautiously optimistic during a recent commercial real-estate panel discussion in Newark: Despite a slumping economy, Newark, they said, is poised for an exciting and prosperous run.

Then the PowerPoint prognosticators took the podium and sobered up the breakfast crowd.

First, Philip Lipper, senior managing director for Studley, displayed a series of fever charts, which quantified the white-hot New York City market and showed how New Jersey, in several key areas, has fallen below national trend lines during the past three years.

Then Rae Rosen, the senior economist and assistant vice president for the Federal Reserve Bank of New York, clinically sucked the air out of the room.

Unemployment is rising, office vacancy rates are increasing, the housing market is in terrible shape and New Jersey will feel the pinch when Manhattan starts cooling off, she explained with her own series of flat-line charts. And with a recession looming, if not already upon us, New Jersey's economy will "closely track the U.S. economy," she said.

"I really feel bad for the doom and gloom here," she said at the Newark Regional Business Partnership gathering.

Most prognosticators, brokers and builders are predicting a tough year or two ahead in office, retail, lodging and leasing activity - all of which are effected by the broad economy. Where there are 250 construction cranes currently in action in New York City, new construction of office and retail projects is slowing considerably in the Garden State.

Office vacancy rates are one of the key indicators of how a market is faring. Northern and Central Jersey Class A vacancy rates historically ran well under the national average. In 2003, they were about 5 percent lower than the rest of the country. Now, they are nearly 5 percent higher.

While the underlying fundamentals of the commercial real-estate industry are "sound," said **Susan Smith**, editor of **Pricewaterhouse Coopers Korpacz Real Estate Investor Survey**, "there are noticeable cracks forming in the foundation. As a result, there is a palpable sense of uncertainty among investors."

A growing number of bankruptcies and foreclosures, combined with dropping employment, has shaken consumer confidence, which is reflected in dipping sales at malls and retail outlets.

The credit crisis that has shown no signs of abating - and this week claimed investment banking firm Bear Stearns as a victim - also makes it exceedingly difficult to find financing for big projects. And the Federal Reserve's strategy of cutting interest rates could take months to work through the system.

A Goldman Sachs report this week suggested the credit crunch and the likelihood of a recession will make it a difficult year for most real-estate investment trusts.

Of course, there is no sense of panic, as there is in the housing market. Rather, there is a growing wait-and-see mentality.

Those yearning for some good news can look to New Jersey's industrial/logistics industry, which, though not immune, is less dependent on the nation's economic winds.

On Monday, for example, AMB Property Corporation completed the AMB Liberty Logistics Center on a long-vacant piece of land near Newark Liberty International Airport. On the same day, the company announced the acquisition of a 50-acre former landfill, where it will build an 878,000-square-foot warehouse.

The nation's second-largest port allows "New Jersey to perform well in good times and bad," said Paul Rosen, AMB's east region manager. "But I don't think anyone's immune."

And though AMB remains active, officials there have put off a couple of big capital deals, and will wait a year or so to see how the economy goes, Rosen said. "If we're going to pull the trigger, it's going to have to be a very good deal for us."

While the warehouse market is struggling around Exits 7A and 8A of the N.J. Turnpike - where three 1-million-square-foot buildings remain empty - areas closer to the port are becoming attractive, said Rob Kossar, executive vice president for Jones Lang LaSalle. There, you will find a number of projects, totaling 20 million square feet, in the pipeline, he said.

"The real critical issue now is transportation costs," Kossar said. "For some companies, the closer you can get to the port, the better off you are."

Ian T. Shearn may be reached at (973) 392-1671.

Graphic Credit: THE STAR-LEDGER/SOURCE: Studley

CHART: Worse than average

nj.com
Everything Jersey

The Times

Commercial real estate faces uncertain future

Thursday, March 20, 2008

By IAN T. SHEARN
Newhouse News Service

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AMERICAN PUBLIC MEDIA™

Friday, March 21, 2008

Mixed news for commerical real estate

The good news: the commercial real estate market is in better shape than the residential one. The bad news: it's a rough road ahead. Lisa talks to **Susan Smith** about what's to come.

TEXT OF INTERVIEW

Lisa Napoli: Lost in the headlines of the subprime mess is the story of commercial real estate.

It's not suffering quite the way residential real estate has, but **PricewaterhouseCoopers** has just surveyed the commercial landscape and the title it gave the report speaks volumes: it's called "Rough Road Ahead for Investors."

You'd have to have a pretty strong stomach to plunk any money into the commercial real estate world right now.

Susan Smith is editor-in-chief of the report.

Napoli: Susan, what rough patches are you seeing?

Susan Smith: For the past ten years, I think investors on the commercial side were really loving every moment of what was going on: rents were rising and the deal flow was great and it seemed like everything was moving along really fine and now, all of a sudden, buyers and sellers aren't seeing eye to eye on pricing and we're also seeing, in some sectors, possibly an increase of new space, space that developers started to build when the economy was doing really well and market conditions were great and unfortunately, those projects now are getting ready to be delivered at a time when demand is slowing down.

Napoli: Is there a connection between the residential downturn and the commercial downturn? Are there similarities?

Smith: You know, the one thing I think you really have to keep in mind is that the residential market and the commercial property market, they're really two very different markets and at the beginning of last year when we started with the subprime mortgage

problems in the residential side, you were really seeing a lot of problems because of an oversupply of space and you know, we were fortunate enough in the commercial side to not have that. Unfortunately, what happened was all of the subprime problems and the mortgages and the lending, it really put a red flag throughout the whole entire financial industry and it made lending more difficult not only on the residential side, but also in the commercial side.

Napoli: But it does seem like both markets are linked to what happens to me as an individual even if I have no money in the game, no skin in the game, so to speak, right?

Smith: No, absolutely. They are linked and when something happens in the overall economy, it's felt probably first with the consumer and then it trickles its way out into every aspect, but again, it's just really important also to realize that the commercial side is definitely healthier than what's going on in the residential side.

Napoli: And that's the upshot of this report, even though you've titled it "Rough Road Ahead for Investors"?

Smith: I believe so, because there's more difficulty in going out and finding that property that you want to buy or even listing a property and trying to sell it, so in terms of what buyers and sellers were used to over the last ten years and what they're encountering now, it's definitely going to be a rough road, but it's also important to realize that there are opportunities out there for investors. It's just a matter of what your strategy is and I always like to think that real estate investors are optimistic.

Napoli: You also have to have a pretty strong stomach, I'd imagine.

Smith: I think you do, I think you do. People always say to me "well, you're in real estate, I can't believe you don't own so much real estate" and I say I know what goes into it. I know how people react to all the things you have to watch in real estate: what's going on with employment and what's going on with the consumer and to me, there's just too much to focus on that it does... you need a strong stomach and good optimism.

Napoli: Thank you so much for your time Susan. I appreciate it.

Smith: Thank you. Have a good day.

Napoli: Susan Smith is with PricewaterhouseCoopers.

SmartBrief

Survey shows turbulence in commercial real estate market

REAL ESTATE INVESTMENT SMARTBRIEF | 03/18/2008

Commercial real estate is headed for a turbulent period, according to the First Quarter 2008 PricewaterhouseCoopers Korpacz Real Estate Investor Survey. With few exceptions, most sectors of the commercial real estate market are showing signs of a slowdown. "I think we're going to see more job loss as a lot of banks and financial institutions are going to have layoffs in the next few months," said **Susan Smith, PwC Korpacz survey** editor-in-chief.

Commercial Property News (03/17)

The New Zealand Herald:
nzherald.co.nz

Rates staying high despite Fed help

5:00AM Wednesday March 19, 2008
By Bob Ivry and Sharon L. Lynch

US Federal Reserve Chairman Ben Bernanke can't revive the housing market and the banks are no help.

The US Federal Reserve has cut interest rates five times since September and last week pumped US$200 billion into the financial system. Its New York branch has provided funds to help rescue Bear Stearns.

Those initiatives haven't brought down mortgage rates for residential borrowers in the US, whose success in refinancing or buying would help bolster the economy.

The interest rate on a 30-year fixed-rate mortgage has climbed to 6.37 per cent from 5.5 per cent since January 24, according to the Mortgage Bankers Association, as financial institutions try to cover $195 billion in mortgage-related losses and save capital for future losses.

"The mortgage rate isn't down as much as it should be because the banks are in desperate straits and they need to maintain a larger spread than they normally would," said Alan Nevin, chief economist with the California Building Industry Association in Sacramento.

"The banks need to generate income and the easiest way to do that is to broaden the spread. If they pay 3.5 per cent and charge 6 per cent, that's a lot of money."

Over the past 10 years, the average spread between 10-year US Treasuries and 30-year fixed-rate mortgages has been 1.75 per cent. Last week it was 2.83 per cent, pushing mortgage costs up.

The Fed cut its target for federal funds 13 times from January 3, 2001, to June 25, 2003. Following the moves, mortgage costs fell eight times and rose five times, according to Bankrate.com.

That has little to do with Fed policy and instead reflects the lack of confidence of investors, who aren't buying securities backed by home loans, says Kenneth Rosen, chairman of Rosen Real Estate Securities and chairman of the Fisher Center for Real Estate at the University of California.

"No one wants to lend much of anything today," Rosen said. "The secondary market system for many loans has broken down. People don't trust the paper. We have an investor strike going on."

The Fed last week agreed to make US$200 billion available to securities firms by lending Treasuries in exchange for mortgage-backed securities because many private investors have quit buying mortgage-backed bonds. Record home foreclosures sent premiums on Fannie Mae and Freddie Mac-backed securities to the highest in 22 years this month.

"Banks are trying to increase their reserves to get through this period where we have greater uncertainty, and also uncertainty about future losses," said Delores Conway, director of the Casden Real Estate Economics Forecast at the University of Southern California in Los Angeles.

Home-loan issuance will drop by 15 per cent this year, according to the Mortgage Bankers Association.

BUYOUT COULD BULLDOZE PLANS

JPMorgan Chase's buyout of Bear Stearns and its Manhattan headquarters may prompt JPMorgan to pull out of its commitment to build at the World Trade Centre site.

New York-based JPMorgan, the third-largest US bank, said it will build a US$2 billion, 40-storey skyscraper at Ground Zero on the site of the former Deutsche Bank AG building.

Those plans are now in question as mortgage-related losses decimate Wall St banks, which have fired more than 30,000 workers in the past seven months and written down or lost at least US$195 billion.

"Who wants to commit to occupying a certain amount of square footage when you don't know what the future is going to hold, and whether or not you'll need those employees?" said **Susan Smith**, manager of the real estate business advisory services group for **PricewaterhouseCoopers LLP** in New York. "We just don't have confidence about the future."

- BLOOMBERG

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FINANCIAL REVIEW

Property

Ground Zero tower rethink

215 words
19 March 2008
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Following its purchase of fellow investment bank, Bear Stearns, for around US$240 million ($261 million), JPMorgan Chase said it will relocate to the New York building previously occupied by the embattled lender and would review plans, announced last June, to build a US$2 billion, 40-storey skyscraper at Ground Zero, the World Trade Center site where the former Deutsche Bank building stands. According to Real Capital Analytics director of market analysis in New York, Dan Fasulo, an asset like the Bear Stearns edifice 'would be on the top of the list for every major **real estate** investor'.

However, with Wall Street banks pummelled by around US$195 billion in losses in the fallout of the sub-prime mortgage crisis, **PricewaterhouseCoopers real estate** business advisory services group manager, **Susan Smith**, said few firms operating in the finance sector were confident enough about what the future held to 'commit to occupying a certain amount of square footage' in the busy business district of the world's largest economy.

Number of Mentions in original article: Deutsche Bank, JPMorgan, JPMorgan Chase, **PricewaterhouseCoopers, real estate** business advisory services group manager Susan Smith, Bear Stearns, Ground Zero, World Trade Center, Real Capital Analytics, director of market analysis in New York Dan Fasulo, Wall Street

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Independent.ie

Bear's HQ is worth six times firm

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JPMorgan Chase & Co's $240m buyout of Bear Stearnsincludes a six-year-old midtown Manhattan tower worth $1.5bn that may make JPMorgan back out of its commitment to build at the World Trade Centre site.

Bear Stearns's 45-story headquarters at 383 Madison Ave sits across 47th Street from JPMorgan's office building, has underground access to Grand Central Station and has an octagonal tower, giving it eight corner offices on most floors.

"It would be on the top of the list for every major real estate investor," Dan Fasulo, director of market analysis for Real Capital Analytics Inc in New York, said. "Given how hard it is to find a site in midtown, I'd find it hard to believe JPMorgan would give it up."

The Bear Stearns building, worth about six times the price JPMorgan will pay for the entire firm, throws into question JPMorgan's plan to build a $2bn40-story skyscraper on the site of the former Deutsche Bank AG building, which was damaged on September 11 and is being demolished, at a time of growing uncertainty in the financial services industry.

"Who wants to commit to occupying a certain amount of square footage when you don't know what the future is going to hold, and whether or not you'll need those employees?" **Susan Smith**, manager of the real estate business advisory services group for **PricewaterhouseCoopers** LLP in New York, said.
The 1.2million square-foot Bear Stearns building has seven open floors that are each 42,000 square feet. They would accommodate about 14,000 traders.

That might not be big enough to satisfy JPMorgan, Barry Gosin, chief executive officer of Newmark Knight Frank, the third largest brokerage in New York City, said.

"If you were building today, 65,000 usable square feet is the minimum space for trading," Gosin said. " Bear Stearns's space is small. They're not a trading firm."

The plan for JPMorgan's downtown tower calls for six trading floors, each with up to 60,000 square feet, the company said.

The bank said in June last year that it would bring about 7,000 investment banking employees to lower Manhattan and retain the corporate headquarters at 270 Park Ave and renovate it.

(Bloomberg)

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Is commercial real estate next?

Experts debate whether it will follow the residential market into a slump

By **Janet Morrissey**
March 24, 2008

The ever-deepening housing crisis has Wall Street nervously watching to see if the upheaval will spill over into the commercial real estate market. At the moment, experts are split as to how much and how quickly the credit debacle will move into the commercial sector.

New York-based Goldman Sachs & Co. is predicting that commercial real estate values will tumble 21% to 26% through 2009. The firm said higher financing costs and slower demand for commercial real estate during an economic downturn will take a toll on pricing.

"Price declines have been the single most important driver of defaults in commercial real estate," Goldman analyst Richard Ramsden wrote in a February report, "U.S. Commercial Real Estate: High Losses, Slow Burn."

"We believe that as commercial real estate prices decline and investors' equity is reduced, there is a greater risk of borrowers defaulting on payments," he wrote.

Mr. Ramsden noted similarities between commercial and subprime real estate lending: Both sectors enjoyed frothy price increases as a result of access to cheap capital and easy credit, and both experienced securitization. The percentage of commercial loans that were packaged up into commercial mortgage-backed securities surged to 46% in 2007, from 29% in 2003, a situation that contributed to the lax underwriting standards, he wrote.

"As a result, we believe that pricing in both asset classes is significantly above long-term trends," Mr. Ramsden wrote, adding that he expects losses from commercial real estate loans to hit $183 billion, compared with his loss estimate of $211 billion for subprime mortgages.

However, CB Richard Ellis, a New York property services firm, thinks that the debt market has pushed the panic button and that concerns about commercial real estate defaults are overblown.

"The credit markets have overreacted to the likely increase in commercial mortgage defaults and losses — perhaps overestimating future default rates by as much as three times," according to a report from the firm last week.

While CB Richard Ellis expects that commercial vacancy rates will tick up over the next few years, it predicts that vacancies will peak at levels lower than the previous high set in 2002-03.

Jamie Goodwell, senior director of research for commercial and multifamily mortgages at the -Washington-based Mortgage Bankers Association, said that at the end of last year, delinquency rates on commercial loans were at or near record low levels. The delinquency rate in the commercial mortgage-backed securities sector also was lower than in nine of the past 10 years, he added.

Mr. Goodwell shrugs off the volatility in the CMBX index, which tracks insurance on bonds that are backed by commercial real estate loans on office buildings, hotels and retailers, noting that many of those playing in this derivatives area are macro-hedge funds and others that are "playing larger macro trends" as opposed to analyzing commercial real estate fundamentals.

John Bonfiglio, group managing director at New York-based Fitch Ratings Ltd., also believes the CMBX pricing overstates potential defaults in the commercial sector. He said the triple-A tranche, for example, is currently pricing in a 19% loss, which is more than twice the size of the sector's highest historic loss of 8%.

"Certainly there are stresses in the world, but we don't see it anywhere near that dire," Mr. Bonfiglio said.

He surmises that many of the people jumping into the CMBX market were formerly shorting the ABX market, which tracks residential real estate.

"A lot of hedge funds made a lot of money shorting ABX, so they thought that maybe they should come into commercial mortgage-backed securities and short that," Mr. Bonfiglio said.

Still, most analysts and investors agree the commercial market has slowed.

"Even though the underlying fundamentals of commercial real estate are still sound, there are noticeable cracks forming in the foundation," said **Susan Smith**, manager in **PricewaterhouseCoopers**' real estate business advisory services group in New York. "As a result, there is a palpable sense of uncertainty among investors."

Nouriel Roubini, a professor at New York University's Stern School of Business and founder of New York-based RGE Monitor, an economic research firm, thinks that it's only a matter of time before commercial real estate falters.

"The same kind of reckless lending practices that occurred in subprime also were occurring in commercial real estate — things like really high loan-to-value ratios and inflated estimations of how much rent would increase," he said.

Mr. Roubini noted that spreads on the CMBX index have widened significantly in recent months, "suggesting that a huge amount of defaults on existing commercial real estate loans" are on the horizon.

At the same time, demand for new commercial loans has dried up, making financing for new projects difficult and expensive, he said.

"The market for new commercial real estate loans is totally frozen like the one for subprime new originations," Mr. Roubini said.

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CoStar GROUP NEWS

March 26, 2008
Written by **Randyl Drummer**

Apts. A Smooth(er) Ride For Investors in a Choppy Market

Despite Subprime Pain-Related Gains In Multifamily, Declines In Investor Confidence Reveal 'Noticeable Cracks' in CRE Fundamentals

PricewaterhouseCooper LLP gives some simple advice in its latest survey of investors: Buckle up; we could be in for a bumpy ride.

While this is true for apartment owners and investors, they may be benefiting from an especially good set of shock absorbers. A pair of recent reports provides fresh evidence that the rental apartment business is continuing to hold its own, and maybe even strengthen -- as expectations continue to falter for office, hotel, retail, and to a lesser extent, industrial activity.

Among major asset types, the national apartment market is the only commercial real estate sector experiencing increased demand at present, as more people are squeezed into the renter's pool by the subprime mortgage fallout, according to the first-quarter **PricewaterhouseCoopers' Korpacz Real Estate Investor Survey**. That pool already includes existing renters stymied in their ability to move into homeownership by the softening economy, high interest rates and tighter lending criteria, along with an increasing demographic influx of Echo Boomers and aging Baby Boomers. They're now being joined by thousands of homeowners forced back into rental housing due to foreclosure.

The competition for a relatively constrained supply of new apartment inventory from multifamily developers is exerting downward pressure on vacancies and upward pressure on rents. Those kinds of metrics are attracting investors to such top-shelf investment sales markets as New York, Washington, D.C./Northern Virginia, Chicago and Los Angeles, according to PricewaterhouseCoopers.

Although many experts have predicted that the "shadow market" of condos converted to rental buildings, notably in Washington, D.C. and South Florida, would drive up vacancies, they're apparently being absorbed. With fewer than 100,000 units of new supply expected to be delivered annually in 2008 and 2009, vacancies are only expected to rise modestly, from 5.6% in the fourth quarter to 6% and 6.3%, over the next two years, respectively, according to the Korpacz report.

"Interestingly, it appears that the shadow market in many areas is not being exacerbated by additions to supply. Instead, it is being (offset) by the aforementioned increases in the number of renters," according to the report.

"Since apartment supply is constrained, markets with low housing affordability should perform well," commented one survey participant.

Eager Buyers Circle Distressed Deals

With an abundance of property on the market and numerous eager buyers, 2008 could still turn out to be another banner transaction year for apartments, according to the Korpacz report, which surveyed 125 real estate investors and specialists from pension funds, insurance companies, REITs, mortgage bankers and developers. In South Florida, for example, where the subprime crisis has been particularly harsh, buyers are aggressively pursuing bank-owned properties and assets held by speculators from the busted condo craze.

How many of those deals get done, and whether the buyer or seller prevails in final pricing, remains to be seen. Average overall cap rates on all-cash unleveraged multifamily transactions are expanding modestly, rising four basis points in the first quarter to a projected 5.79%, after falling 10 basis points a year ago, according to the Korpacz survey. Cap rate expansion is expected to continue for at least the next six months, with an average 46-basis-point gain across all markets.

Risk-adverse investors are snapping up a lot of the deals. Of the record $98.6 billion spent in multifamily transactions last year, 40% of acquisitions were by pension funds, life companies and other institutional investors, according to the latest Commercial Real Estate Outlook published earlier this month by the National Association of Realtors. Private investors were just as active, accounting for another 40% of transactions.

Average apartment rents are expected to rise 5.3% in 2008, up from a 3.1% increase in 2007, while average vacancies remain below the tipping point for a landlord's market in many areas, according to the NAR. Markets with the lowest apartment vacancies include Northern New Jersey, San Jose, Miami, Salt Lake City and San Diego -- all with vacancy rates of 2.9% or less. The association predicts net absorption of 245,800 units in the 59 metro areas it tracks in 2008, up from 234,400 last year.

'Cracked Foundation'

Other commercial property sectors are feeling the pain more acutely. Even though the underlying fundamentals of commercial real estate are still sound, "there are noticeable cracks forming in the foundation," said **Susan M. Smith,** editor-in-chief of **PricewaterhouseCoopers Korpacz Real Estate Investor Survey** and manager in PwC's real estate business advisory services group.

"There is a palpable sense of uncertainty among investors we spoke with and surveyed this quarter," Smith said.

NAR Chief Economist Lawrence Yun said the commercial real estate market is essentially treading water, with no significant changes in vacancy rates or rent growth.

"Under normal circumstances, near-full occupancy coupled with positive rent growth would be of strong interest to investors, but we are not seeing that. The credit crunch has filtered into the commercial real estate market," Yun said.

Investors appear to be taking a wait-and-see attitude, added Patricia Nooney of St. Louis, chair of the NAR's Commercial Alliance Committee.

"Even with fairly stable fundamentals and capital available from institutional investors, it appears investor confidence has declined, and some private investors have had problems obtaining financing. Commercial real estate investment set a new record in 2007, but now that we are in a period of economic uncertainty, transaction volume is likely to decline."

Here's a breakdown of conditions in other sectors included in the **PricewaterhouseCoopers** survey:

Office
Declining employment has added a new concern for landlords and investors of office properties, with such sectors as financial services and professional-and-business service entities hardest hit. CBDs that reported sharp declines in overall absorption in 2007 included Chicago, midtown and downtown Manhattan, Houston and Washington, D.C. CBDs reporting strong gains included Los Angeles, Atlanta, Bellevue, WA and Baltimore.

Leasing also slowed noticeably in suburban office. Even so, the pace of new construction, much of it spec, continued to increase, sparking concerns about oversupply. Suburban office markets posting some of the highest additions to supply in the fourth quarter of 2007 included Phoenix, Northern Virginia and Dallas.

Industrial/Warehouse
Overall, the national flex/R&D market is seeing a steady increase in demand, thanks to steady growth in the high-tech sector and higher rental rates in comparable office space. The tightest markets tend to be located along the West Coast and include long-standing favorites like Silicon Valley, La Jolla and Los Angeles/Orange County. Favorable supply-demand fundamentals and the limited exposure to changing employment or consumer spending trends is helping to reinforce the warehouse sector's image as a safe investment haven. Huge warehouse portfolio sales in the first half of 2007 made it a record year for sales volume.

Retail
Declining consumer confidence, a sharp rise in personal bankruptcy filings and a drop in consumer spending is causing lackluster retail sales growth and hurting the regional mall market *(for more on this, refer to today's Costar Advisor retail story on the health of the American mall)*. Would-be investors in power centers are holding back. A slowdown in tenant expansions and growth in supply are causing vacancy rates to rise amongst all shopping center types, however, community and neighborhood shopping centers are seeing the sharpest increase.

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Last updated: March 28, 2008 11:25am

Using Technology to Survive in a Slowing Economy

By Noreen Seebacher

Metro

There's little good news in **PricewaterhouseCoopers' first quarter 2008 Korpacz Real Estate Investor Survey**. The report, which notes that "bleak news reports about the dismal state of the US economy" are everywhere, warns some office markets could weaken significantly in 2009 and 2010 and predicts the retail sector could be negatively impacted by a decline in consumer spending.

So what should commercial real estate companies do now? The report suggests turning to technology. "Companies can capitalize on the slower business climate by engaging their key application users to review the effectiveness of their current application suite," it notes.

Scott Metro, a partner in the Real Estate Systems and Process Assurance unit at professional services firm PricewaterhouseCoopers, identifies spreadsheet replacement software as a specific area of interest. Metro says many real estate companies are installing sophisticated software to shore up data security and flexibility--and resolve what he calls "spreadsheet overload." Metro predicts spreadsheet replacement software will become increasingly important to commercial real estate professionals in 2008 and 2009 as they seek competitive advantages in a softening market.

In a PricewaterhouseCoopers report on technology trends for 2008, Metro notes that real estate companies use spreadsheets to store vast amounts of information, as well as forecast property performance and create models for acquisition financing. "In fact, it is not uncommon to find that Microsoft Excel is used to maintain a quick reference list of properties and their key attributes," he adds.

But he says Microsoft's Excel, the most common spreadsheet software, pales in comparison to some of the newer applications. "Compared to most real estate applications, like accounting and property management systems, spreadsheets are poorly controlled. It is cumbersome to control unofficial copies of analyses, determine who made changes to files and/or find out whether any of the links that bind multiple worksheets together have been broken or corrupted," he says.

Spreadsheet replacement software allows companies to track changes in a spreadsheet and select the people authorized to alter such things as budget numbers, rental rates and income forecasts. The software also consolidates scattered bits of information and gives companies the ability to dig deeper into data to analyze, for instance, the construction expenses for a mixed-use project.

“The first time you see these and see what they can do, there is a ‘wow’ factor,” Metro says. "To suggest that spreadsheets can be replaced with specific applications is infeasible and, in many cases, imprudent. The flexibility of such tools allows users with varying levels of technology expertise to quickly run complex analyses."

Real estate companies now are in the early stages of large-scale adoption of spreadsheet replacement systems, Metro adds. Many companies are implementing tools that work almost exactly like spreadsheets, or even some that are, in fact, spreadsheets with special “add-ins”

"But they're much more controllable and offer better audit trails than traditional programs," he says. SAP Business Planning and Consolidation (formerly known as OutlookSoft) and Infor's Extensity are two examples of software tools that look, function, and have the flexibility of spreadsheets, but with tighter controls and audit trails.

Real estate companies are embracing the new software to stay ahead of the competition. But there's another reason, Metro speculates: "The market has slowed, but many companies are optimistic it will turn around relatively quickly. They don’t want to lay off staff, so they're tackling projects that they were probably too busy to do before, including reviewing their technology."

Pensions&Investments
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Changes in accounting rules hurt realty values

Arleen Jacobius
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New accounting rules could make the decline in commercial realty values look worse for many real estate investment managers.

In the past, managers could use a property's purchase price as its fair value.

No more. Under Financial Accounting Statement 157 - which goes into effect for fiscal years starting after Nov. 15, 2007 - managers will have to use the expected sale price, even if it's lower than the book value.

In a down economy, accounting changes could cause some managers to rack up hefty unrealized losses.

"Because of the nature of the market or the return expectations, the value of the property could be less than you paid for it a few years ago. The value could be impaired," said Timothy Croushore managing director, Mesirow Financial Holdings Inc., Chicago.

Commercial real estate already had taken a big hit across several property types and investors anticipate the outlook will worsen next quarter.

Overall, institutional investors expect capitalization rates - the net operating income divided by the value of a property - to further rise across all property types, driving down returns in the second quarter, according to **PricewaterhouseCoopers' first quarter 2008 Korpacz Real Estate Investor's Survey**. Mall cap rates could grow 25 basis points to 100 basis points. Central business district offices cap rates are expected to grow up to 75 basis points. Apartment cap rates are expected to grow about 46 basis points

Indeed, institutional investors in the fourth quarter said cash was a better investment than commercial real estate, stocks or bonds, according to a Real Estate Research Corp. survey released in February. Institutional investors expected lower rental growth and higher expenses among most property types in the first quarter of 2008, the RERC survey noted.

That gloomy outlook means that fair value prices under the new accounting rules could fall below purchase prices.

"In the year of acquisition, there may be write-downs, particularly in portfolios in which managers have been assuming that acquisition price approximates fair value," said Dovid M. Frankel, partner at real estate consulting firm Ernst & Young, New York. "The new fair value rules reflect an exit price, which would not take into account transaction costs, which potentially could bring about a different reported fair value."

Second hit for REITs

Investment managers with real estate investment trust portfolios might be doubly hurt because other new accounting rules remove a liquidity discount they had enjoyed for owning a large company's public stock.

"If you invest in public companies, you will not be able to apply a liquidity discount in determining fair value of your investment," Mr. Frankel said.

For all investment managers, there also could be a reduction in their portfolio property values because they can no longer count the purchase costs as part of the properties' value, Mr. Frankel said.

Investors, however, could benefit because the rules might require managers to report valuations in the same way. Standardized valuations would also make it more difficult for investment managers to hide drops in property value by holding them at cost on the books, inflating the value of their portfolios.

To make matters even more complex, not every fund manager uses the same method to value property. Under FAS 159 - also going into effect this year - companies can choose to measure many financial instruments such as commercial mortgage-backed securities investments at fair value. But companies cannot adopt this rule retroactively and, once elected, consultants say they can't switch back and forth between account methods.

A 2007 Ernst & Young survey of real estate private equity funds revealed that half of the funds report at fair value, and the other half use a historical cost formula.

How fair value is measured could greatly impact the value of each property in a portfolio, said Scott Farb, managing principal in the Los Angeles office of Reznick Group PC, a real estate consulting firm.

Take an investment fund that bought a portfolio in June 2007, for $2 billion, but today couldn't sell it for more than $1.7 billion. Under historical cost reporting, the fund would value the portfolio on its books at its cost, or $2 billion. Under the new fair value accounting rules, the portfolio would be valued at $1.7 billion.

"Under historical cost, the building would not be impaired because you could recover the cost of the property. It's a less stringent test," Mr. Farb said. "If you are a pension fund or investment company that is required to report under the fair value method, you would report the property at $1.7 billion."

Real estate debt managers such as mortgage REITs might benefit from choosing the fair value option because they already use the fair value method for valuing assets such as CMBS investments, Mr. Frankel said.

In any case, all investment managers will have to adjust to the new way of defining "fair value." Under the new definition, investment managers would need to identify the principal or most advantageous market for the property, the investors in that market and how they would value the property, said James Wilson, senior managing director in the valuation practice of Mesirow Financial.

Photo Caption: Changing how fair value is measured could have a big impact on a portfolio, Scott Farb says.

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news-journalonline.com
THE INDEPENDENT VOICE OF VOLUSIA ANF FLAGLER COUNTIES

April 13, 2008

It's a Mall, Mall World

Commercial construction has many wondering if area is being overbuilt

By CECIL G. BRUMLEY and VALERIE WHITNEY
Business Writers

The sleek, new Portofino Square strip center is a jarring site as it sits empty along Nova Road in South Daytona.

More daunting is the large expanse of bare earth awaiting the Pavilion at Port Orange.

As rampant construction continues, commercial centers in Volusia and Flagler counties seem to be teetering between catching up with the surge of population growth of the past few years and stretching to the point of being overbuilt.

COMMERCIAL LAG

Commercial construction always lags behind residential construction, said David Lusby, vice president of Palm Coast Holdings, the master developer for the huge Palm Coast Town Center. "Commercial is driven off of rooftops."

The numbers bear that out. While residential construction permits ballooned to more than $1.2 billion in 2005, commercial construction has remained at about $500 million the past few years.

The population, of course, has ballooned along with the residential construction. Since 2000, Volusia County's population has grown by about 67,000 people while Flagler County's population has nearly doubled with 40,000 more residents.

"The residential demographics have changed so dramatically, the retail has just been catching up," said Lusby, whose Town Center project will see a second large retail complex open this summer with a Super Target, Books-A-Million, TJ Maxx and more, following a Publix-anchored center opening last year.

While based in Chattanooga, Tenn., CBL & Associates quickly learned this market after buying Volusia Mall and realized there was room for more commercial development.

"We know that market well," said Geoff Smith, CBL's vice president of development.

As of the end of 2007, Volusia Mall was at 98 percent occupancy, Smith said.

With that level of business, CBL broke ground this year on the Pavilion. A hybrid lifestyle and power center with more than 500,000 square feet of space.

The Pavilion is starting out with a powerful lineup of stores, unlike a lot of strip centers, and that should make a big difference, Smith said.

Much of the Pavilion is a traditional lifestyle center, arranged in village fashion with a combination of retail shops, anchored by a Belk department store; a 12-screen Hollywood Theatres cinema; a Barnes & Noble; and restaurants with walkways and benches arranged in a park-like setting. But it also has a strip of big-box stores with a Circuit City, Michaels and PetSmart.

"We didn't do that because we had to so it would work, but because we felt the combination would make it even stronger," Smith said.

BIGGER DOING BETTER

The large Palm Coast and Port Orange centers have already attracted several well-known retailers, but smaller centers have not been so lucky.

Although Portofino Square developer John Hinton said he has sold about half of the 13 condo units there, nothing had moved in because until recently a sewer problem had to be corrected. New owners include a chiropractor, a beauty shop, a kitchen and bath center, and a flight simulator school.

Still, he has noticed a slowdown in the market, said Hinton, who chose to sell rather than lease units in Portofino. "There is a lot of interest, but people keep hearing a recession. Because of that, small business owners are hesitant even though there is money there for those who qualify."

The first quarter edition of the **2008 PricewaterhouseCoopers Korpacz Real Estate Investor Survey** predicts a rough road ahead for commercial real estate because of the housing downturn, job losses, ongoing credit crunch and general slowing of the economy. "The survey found telltale signs of weakness in office, retail, lodging and leasing activity, while areas less affected by the broad economy, such as industrial and warehouse properties, remain stable," the report stated.

It continued, "Rising vacancy rates continue to impact community/neighborhood shopping centers -- the result of a slowdown in tenant expansions and constant additions to supply. In the fourth quarter of 2007, approximately 12 million square feet were completed in the U.S. community/neighborhood center sector -- the highest quarterly total in three years."

OVERBUILT

"Overbuilt? It all depends on who you talk to," said developer Bill Humbert. "There are more strips than I have ever seen before."

Humbert built the Palm Coast Parkway Business Center years ago, which he sold last year. That center thrived before more shopping centers starting getting built in Flagler, Humbert said.

But his current project, Ridgewood Shoppes, sits empty. "There has been a lot of interest but the new buyer -- a doctor -- is particular about who he wants in there. He wants to use three units himself."

When developer Hassan Saboungi and his dad, Mike Saboungi, built the roughly 25,000-square-foot Twin Fountains strip center on Beville Road in South Daytona, they also constructed14 office/warehouse units in the back. They sold out within a week.

But finding tenants for the retail center has not been as easy despite the heavy traffic on Beville. The center recently welcomed the offices of United Cerebral Palsy. It joins a lineup that includes a sandwich shop, an ice cream shop, a florist and a nail shop.

"We have had steady interest and a number of inquiries from people that are testing the market," said Hassan Saboungi, vice president of Saboungi Construction Inc.

Saboungi thinks the slowdown in rentals is more about timing than about an overabundance of space, though. "The small business person is hesitant to move into another location. They are trying to be

conservative," he said. Saboungi also developed another strip center, Nova Fountains, not far from Reed Canal Road. The 18,000-square-foot center also has several available units. So far, he has a commitment from a hair salon and Tomoka Labs has opened there.

The economic malaise caused one developer to change his plans for a project on State Road 44 in New Smyrna Beach, deciding to sell lots and let someone else build.

Jerry Evans had more success with a project on West International Speedway Boulevard. Speedway Village Shoppes is nearly full with several name retailers, including a FedEx/Kinkos shop.

For the State Road 44 project, " 'There was not enough interest from national retailers," he said in an interview in February.

Charles Lichtigman, whose Charles Wayne Properties has long been one of the area's largest commercial real estate firms, is even more critical of what is going on.

"In general, we are overbuilt and it is in locations that don't make retail sense," Lichtigman said. "The kinds of things that make sense for a strip center are high traffic roads and visibility directly from the road, and not a lot of trees hiding the buildings."

IMPACT FELT

Old shopping centers have been fortunate to maintain interest, even filling the space left when big anchors pull out. For example, Holly Hill Plaza at Mason Avenue and Nova Road has an Aldi grocery store and a Ross Stores' dd Discounts filling the space left by an Albertsons supermarket. The vacant space left at Promenade at Nova and Beville Roads by Winn-Dixie is getting filled with a Planet Fitness and a Steve & Barry's.

"Good space is still in demand," Lichtigman said, noting the demand is still there for Granada Plaza and Bellair Plaza, both built in the 1960s.

But with all of the new construction, it could take one to two years and even longer for the market to swallow the space, which resulted from bad planning decisions during boom times, he said. "In some cases, owners will probably have to lower their rents."

There's also the problem of the environmental impact of all the construction.

Clay Henderson, a land-use attorney and environmentalist, said strip centers are relatively easy to get permits for, but have their drawbacks.

"It's an easy land use, but at the same time, it's a lazy land use," Henderson said.

Strip centers lead to more urban sprawl, he said, and "eat up concurrency" requirements for curb cuts on main roads.

"It becomes death by a thousand paper cuts," he said. "(Strip centers) tear at the heart of the uniqueness of your community, and makes them all look alike."

THE FUTURE

Judging by plans on the drawing board, the impact of strip centers will continue.

Several large projects have been proposed for the two-county area, especially at the 472 Activity Center in Deltona and Orange City where developers are seeking approval for three huge shopping center. Deltona Village, Sandhill Pointe and Victoria Pointe would add more than 2 million square feet of space.

Developers also have other projects both large and small throughout Volusia and Flagler counties. But how much will actually get built is in doubt.

John Wanamaker, who has been developing some small projects in West Volusia, doesn't think more than one of the three will get built.

"I don't think we have the demographics to support two," Wanamaker said earlier this year. "I don't know where they are getting the houses from to justify this. There are not a lot of rooftops, for example, going up toward Daytona Beach."

There has already been a Kohl's-anchored power center built in West Volusia and other retail centers, he said. "When they were developed, their usage numbers considered West Volusia as part of the customer base for those centers."

Lichtigman also anticipates some slowness in filling some of the larger shopping centers planned for the area because the pace of residential construction has slowed down, he said. Ultimately, the community will grow up around these sites.

The Pavilion should do well, he said. Besides retail shops, the center will have a multi-cinema that will attract people to the shopping center. "Port Orange has needed another theater for the last 12 to 15 years. It wasn't financially feasible to develop that alone. But it works as part of a larger project."

And, of course, Wal-Mart also still has plans for more stores, which would suck up a lot of retail business. The company is looking at down-sizing a store at Madeline Avenue and Nova Road in Port Orange, but it also has Supercenters planned for Daytona Beach and Palm Coast.

In fact, the Wal-Mart in Flagler County is next to one of two "developments of regional impact" that have been approved besides Town Center. The State Road 100 development would only have 50,000 square feet of retail along Old Kings Road north of S.R. 100, but a Supercenter is generally 200,000 square feet.

However, Palm Coast Park would have 1.5 million square feet of retail space.

With the immediate future uncertain, a long-range project like Palm Coast Park isn't worth mentioning just yet.

While Sawmill Creek, the first residential phase of Palm Coast Park has begun, anything else there is just too far down the road, Lusby said. "There are no imminent plans for retail or shopping."

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Financial “terrorism” hits property market

Shock waves could be felt for up to 3 years, experts say

By Arleen Jacobius
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Real estate is in its worst slump since the 1980s, but insiders say the market could hit bottom several times over the next 12 to 36 months.

The culprit is the credit crunch, which is drying up financing and causing investors to flee. The problem: Just when things start to look better, another financial bomb explodes on Wall Street. The shock waves might keep real estate managers and investors reeling for years to come, experts say.

“It's like terrorism,” said Jack Foster, managing director and head of Franklin Templeton Real Estate Advisors, a real estate fund of funds firm in New York.

As a result, the market is in the doldrums. There are about 70% fewer transactions than a year ago and investors must pony up more cash for each deal that does get done.

Many buyers are choosing to sit it out until the market calms down. “There are half as many bids as there used to be,” said Bill Krauch, managing director of New York real estate manager ING Clarion Partners.
TIAA-CREF bought much less property last year than in 2005 and 2006, said Tom Garbutt, managing director and head of global real estate at the New York money manager.

Pension funds and other institutional investors are holding off on making new commitments.

For example, the $15.4 billion New Mexico State Investment Council, Santa Fe, is monitoring the market but is not actively pursuing any deals, said Charles Wollmann, spokesman. “Our baseline for returns has been elevated and there are a lot of deals that we just aren't going to get serious about in this market environment,” he said.

PricewaterhouseCoopers, in its **first quarter 2008 Korpacz Real Estate Investor Survey**, said major real estate players including pension funds “have large sums of capital to invest, (but) uncertainty surrounding the depth of the correction has many of them walking on eggshells.”

During the fourth quarter of 2007, real estate investors rated the investment outlook for cash higher than for commercial real estate, stocks or bonds, according to a real estate survey of institutional investors by Real Estate Research Corp., Chicago.

Some institutional investors are not buying real estate this year because the drop in the equities market has caused their real estate and other alternative investment allocations to exceed their targets, Mr. Foster said.

Others, such as the Oregon Investment Council, which oversees the $64.9 billion Oregon Public Employees Retirement Fund, have added a few investments in response to the market. The council made commitments to a few new real estate debt funds in response to current and near-term market changes, but is keeping to its long-term strategy, said Brad Child, senior investment officer at the Tigard-based council.

Refinancing woes

It's also tough to value properties, and lenders are offering only small loans, said Michael McMenomy, global head of investor services at CB Richard Ellis Investors LLC, Los Angeles.

What's more, opportunistic real estate managers — whose portfolios typically contain 70% to 80% debt — and others layering on debt will face refinancing problems in the next 12 to possibly 36 months, TIAA-CREF's Mr. Garbutt said.

Until about six months ago, debt was cheap and available. As a result, many investment managers got three-year loans with two one-year extensions. Managers are likely to extend these loans as long as they can because they can't refinance. However, the managers will have a problem when the extension periods are over.

“There will be an issue of deleveraging these strategies,” Mr. Garbutt said.

Troubled real estate investment managers might bundle the properties into real estate investment trusts — as some did in the 1990s — or enter into deals with existing REITs, Franklin Templeton's Mr. Foster said.

But REITs have constraints, Mr. McMenomy said. They can only buy properties that have small amounts of leverage because their portfolios use little debt.

Still, some real estate investment managers might not have a choice. If they hold properties longer than they had planned, their returns could take a serious hit, Mr. Foster said.

Overall, prices across commercial real estate sectors have fallen only 5% to 15% so far, Mr. Garbutt estimated.

Promising niches

Seeking opportunities, managers are raising funds for what they consider more promising niches of the real estate market.

A number of real estate investment firms have launched distressed opportunity funds to take advantage of an expected wave of foreclosures and restructurings. For example, New-York based Apollo Real Estate Advisors' year-old debt arm, Apollo Real Estate Finance Corp., just began buying distressed securities.

Managers also are raising money for international funds. Just last month, Apollo closed a $1.4 billion European real estate fund, dwarfing the $700 million Apollo Real Estate Fund V it closed in 2006.

Executives at ING Clarion, already a global investor, expect to see opportunities abroad, especially in Asia. "The Asian markets are still very, very strong," Mr. Krauch said. ING Clarion executives also plan to invest in Latin America next year, Mr. Krauch said. The firm already invests in Mexico.

In the U.S., ING Clarion is buying land for property development projects while land prices are down.

"We will build into the recovery rather then wait two years for a recovery and then build," he said. "We see declines in land prices, especially in the residential sector and, to a lesser extent, in the industrial and retail or shopping center sectors."

The idea is to buy land while it's cheap and start the construction process, which can take anywhere from nine months for an industrial project to 18 to 24 months in other commercial real estate sectors, Mr. Krauch said.

Both Mr. McMenomy of CB Richard Ellis and Mr. Garbutt of TIAA-CREF said cash buyers have an edge in this market. TIAA-CREF's portfolio has average debt of about 20%, and real estate executives expect to buy many properties with no debt, Mr. Garbutt said.

"This is a time to be a careful acquirer of property and to build a real estate portfolio at competitive price points," Mr. McMenomy said.

But that does not mean that opportunistic real estate investment firms that buy with more leverage will sit out this market.

"They live for distress and want to buy when prices are cheap, cheap, cheap," Mr. Foster said. Many of these investors are waiting on the sidelines for a bottom to the market, he said.

"I think we are 12 months away (from the beginnings of a recovery). I believe the reality, like terrorism, is not going away, nor will the subprime crisis," Mr. Foster said. "It's not going away because so little is known about what will happen. We will have surprises for a couple of years."

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New Industry Accounting Rules Forge CBRE Practice

By Ben Johnson
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In response to a variety of new accounting standards and continued calls for increased reporting transparency, Los Angeles-based CB Richard Ellis has launched a Financial and Tax Reporting Services practice. Part of the brokerage giant's Valuation and Advisory Services Group, the new practice is led by managing director Kyle Redfearn based in Dallas.

"The ever-increasing scrutiny around financial and tax reporting transparency requires professionals who are well versed in valuation trends and issues as well as the regulatory reporting environment," says Thomas McDonnell, president of CB Richard Ellis' Valuation and Advisory Services Group.

Among CBRE's new services are valuations required for financial and tax accounting and reporting that follow guidance set forth by the Financial Accounting Standards Board (FASB), International Accounting Standards Board (IASB) and the Internal Revenue Service (IRS).

Redfearn brings with him more than 17 years of real estate valuation and consulting experience encompassing all major property types throughout the U.S. and internationally. Prior to joining CBRE, he headed up the real estate valuation group in the Tax and Financial Reporting practice at Houlihan Lokey Howard & Zukin. Before that, he was a senior manager at Deloitte & Touche, where he focused on financial and tax reporting valuations and assisted the firm's audit teams as a valuation review specialist.

Redfearn's services come at a time when the regulatory environment is increasingly complex. For example, FASB has created a new rule, known as Financial Accounting Statement (FAS) 157, which requires institutional investors to value their commercial real estate holdings based on the expected sale price rather than the purchase price. Parts of the rule were originally set to take effect in the first quarter of 2008, but FASB recently delayed implementation until early 2009, giving companies more time to study the rule. FAS 157 is intended to create a more universal method of measuring and reporting asset valuations beyond the internal models most institutions use.

“In developing this statement, the board considered the need for increased value consistency and comparability in fair value measurements and for expanded disclosures about fair value measurements,” according to a recent FASB statement.

For now, institutional investors and their accounting firms remain mum about the true extent of the rule’s impact, but many feel the industry will suffer no ill effects.

“I’ve got questions about it that haven’t been resolved yet,” says Redfearn, “but it’s not going to change my approach since I already focus on market-oriented valuations.”

According to George Yungmann, senior vice president of financial standards for the National Association of Real Estate Investment Trusts (NAREIT), publicly traded REITs will not be affected by FAS 157. “For me, it is a non-issue with relationship to investment properties. Our companies are already using those standards. It was delayed for technical reasons rather than for its potential impact on the industry.”

For many, though, the rule comes at an inconvenient time for the industry as commercial real estate values continue to fall. Earlier this year, a Goldman Sachs analyst predicted that commercial real estate values through 2009 could drop by as much as 26% from peak to trough. Values have already been dropping for months.

According to the latest Moody’s/REAL Commercial Property Index, values for commercial real estate holdings by institutions fell for the third month in a row, by 0.6% in January. The index is now 2.4% below its high achieved in October 2007.

At the same time, capitalization rates are on the rise, which is leading to lower earnings expectations because the properties on their books are falling in value. A majority of institutional investors in a recent **Korpacz Real Estate Investor survey** expect overall cap rates to increase by an average of 35.5 basis points over the next six months.

“As 2008 gets underway, we can expect capitalization rates to continue to increase,” says Kenneth Riggs, president and CEO of Chicago-based Real Estate Research Corp. “We may see these rates increase more quickly on a regional level, as they seem to be doing in the Midwest and East regions, although the West and South regions are seeing a little less movement.”

Many institutional investors are also voicing a preference for cash over commercial real estate, stocks or bonds on a risk-adjusted basis, according to a fourth-quarter survey by Real Estate Research. These investors also are expecting lower rental growth and higher expenses among most property types in the first quarter of 2008.