
20th Annual LA/OC Market Trends Seminar

Everett (Allen) Greer
Greer Advisors, LLC

January 24, 2013

Greer Advisors, LLC

Goals of Presentation

- Disclaimers
- Market Drivers – Economy, Interest Rates
- Financial Regulations (Dodd-Frank)
- Capital Market Trends - CMBS, REITs, CDS
- Risk Pricing
- Market Conditions (Sales Volume, Price PSF, Cap Rates)
- Rents, Vacancies
- Outlook & Forecast

■ Market Drivers

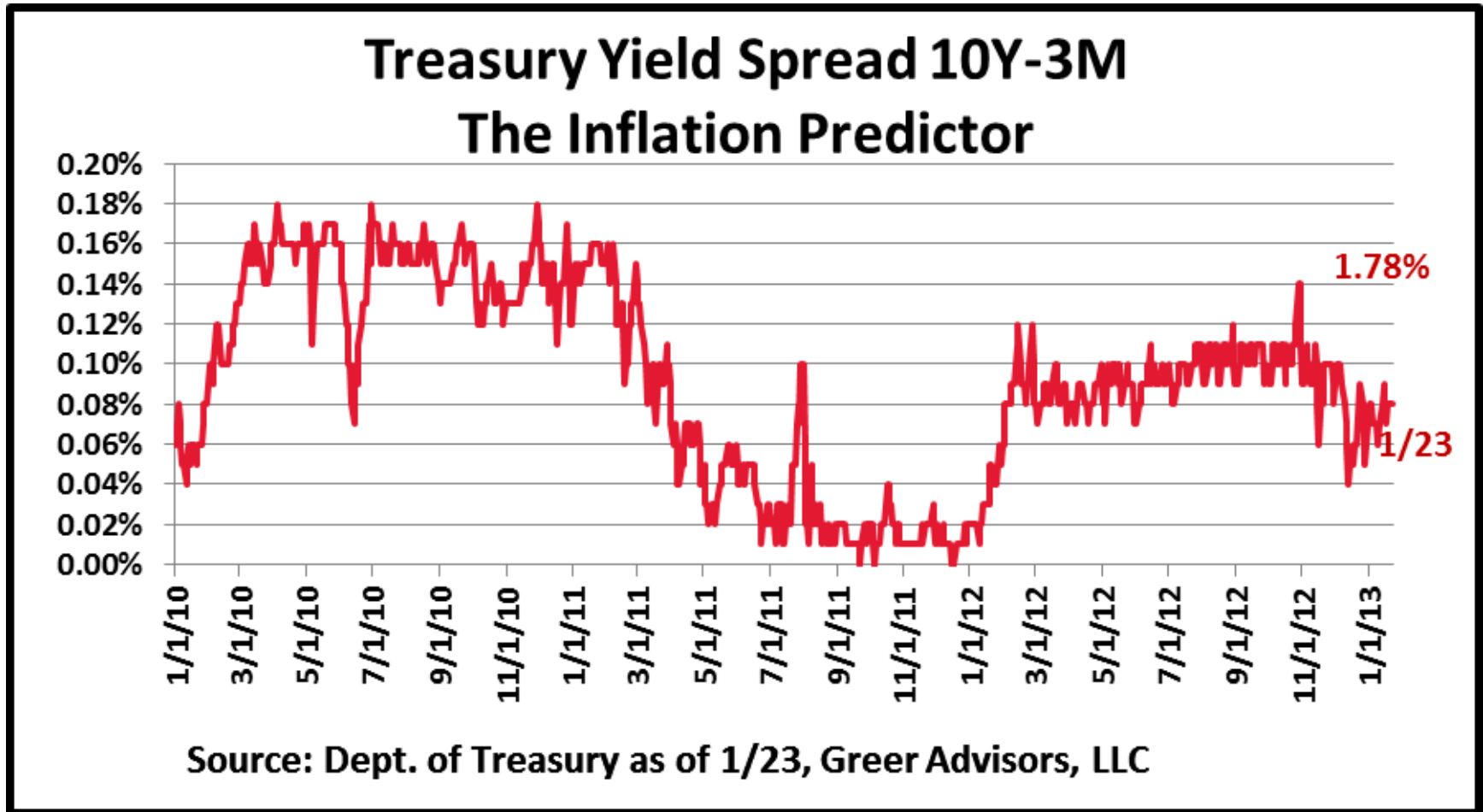
Key Interest Rate

10 Year Treasury Yields



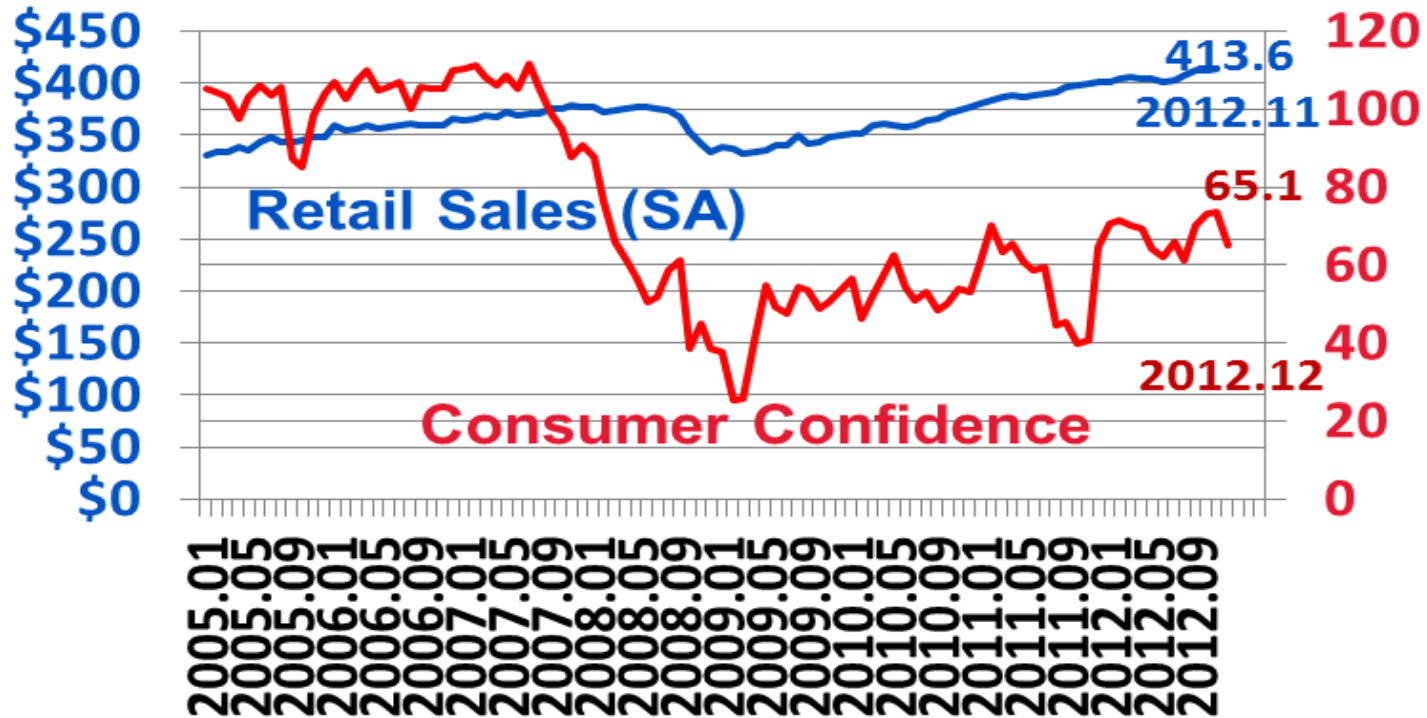
Source: Dept. of Treasury as of 1/23, Greer Advisors,

Inflation



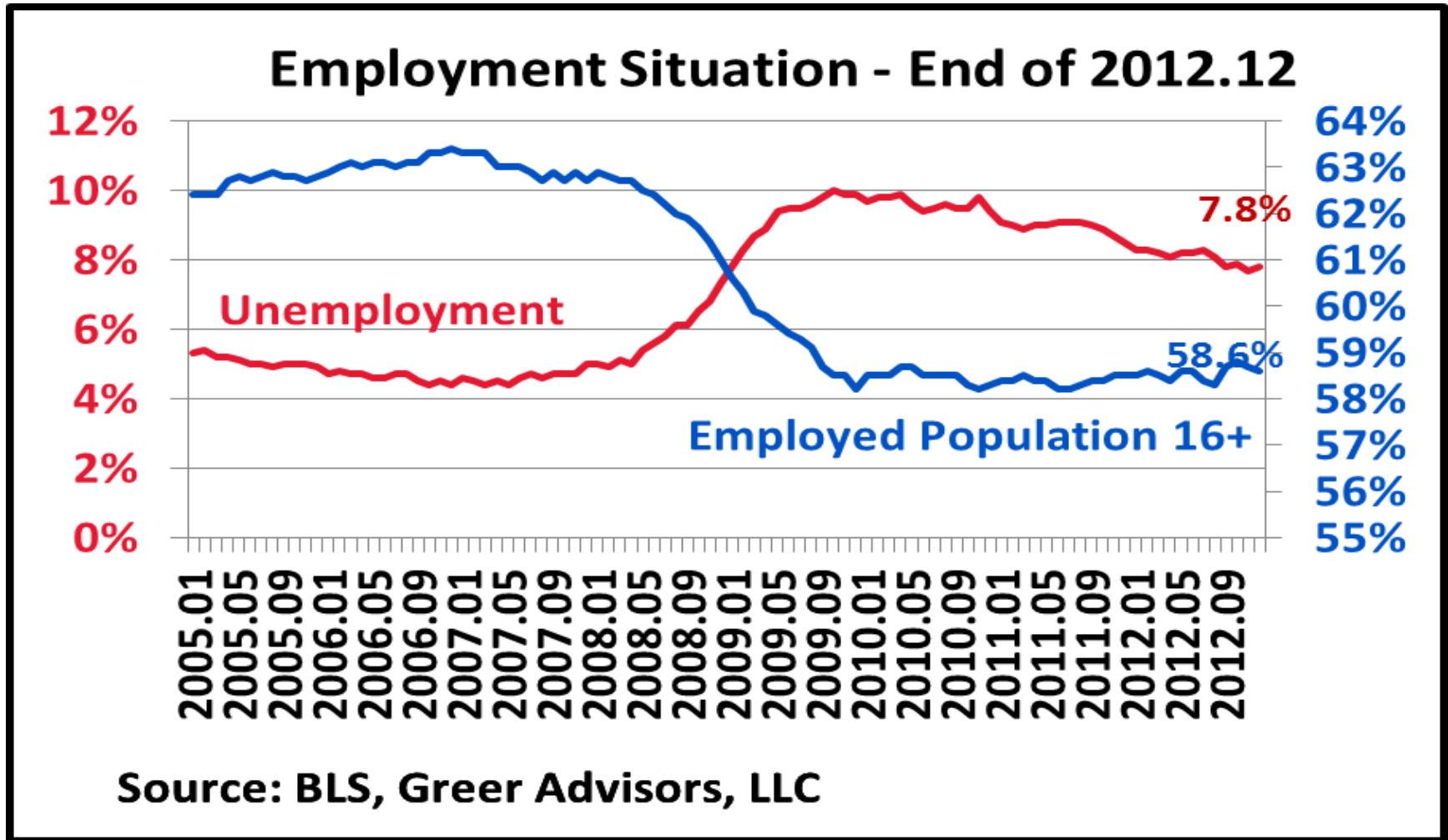
Economy – Consumer Confidence & Sales

Key Economic Indicators



Source: Conference Board, Census, Greer Advisors, LLC

Economy – Employment



Los Angeles 10.9% as of November

Economy

Consumer Side

- Consumer Confidence is Poor at 69.2 (April Conf. Board)
- Unemployment Remains High, especially in SoCal
- England Might Pull Out of EU
- Liquidity, Leverage, Interest (for non-AAA Debt) – Poor
- Retail Sales are OK, the Rest is near Flat Line

Investment Banks

- Capital IQ and Deal Logic show LBO's 😊 / M&A on the rise
- Record Profits

■ Financial Regulations

Financial Regulations

Dodd-Frank Wall Street Reform & Consumer Protection Act

- 16 Titles – See Summary on Wikipedia – Post TARP 😊
 - 243 Rules to be created (reportedly >50% not done)
 - 67 Studies required (>50% not done)
 - 22 New Periodic Reports
- Restructure of Regulators, elimination of OTS
 - Financial Stability Oversight Council (New)
 - Office of Financial Research (New)
- Keys for Commercial Real Estate:
 - Rating Agency Reform
 - Securitization Reform (nominal change due to QIB clawbacks)
 - Derivatives – minimal change thus far due to “netting”

■ Troubled Asset Relief Program

Fiscal Cliff

Numerous Tax Breaks Might Go Away –Uncertainty Remains

- SFR Mortgage Deduction
- Capital Gains Exemption
- Wealth Tax
- Elimination of Several Other Exemptions
 - Estate Tax - \$10,000 / yr / child
 - Energy Credits (Sec 29)
 - Low Income Credits (Sec 42)
 - Historic Credits
- Overall Uncertainty

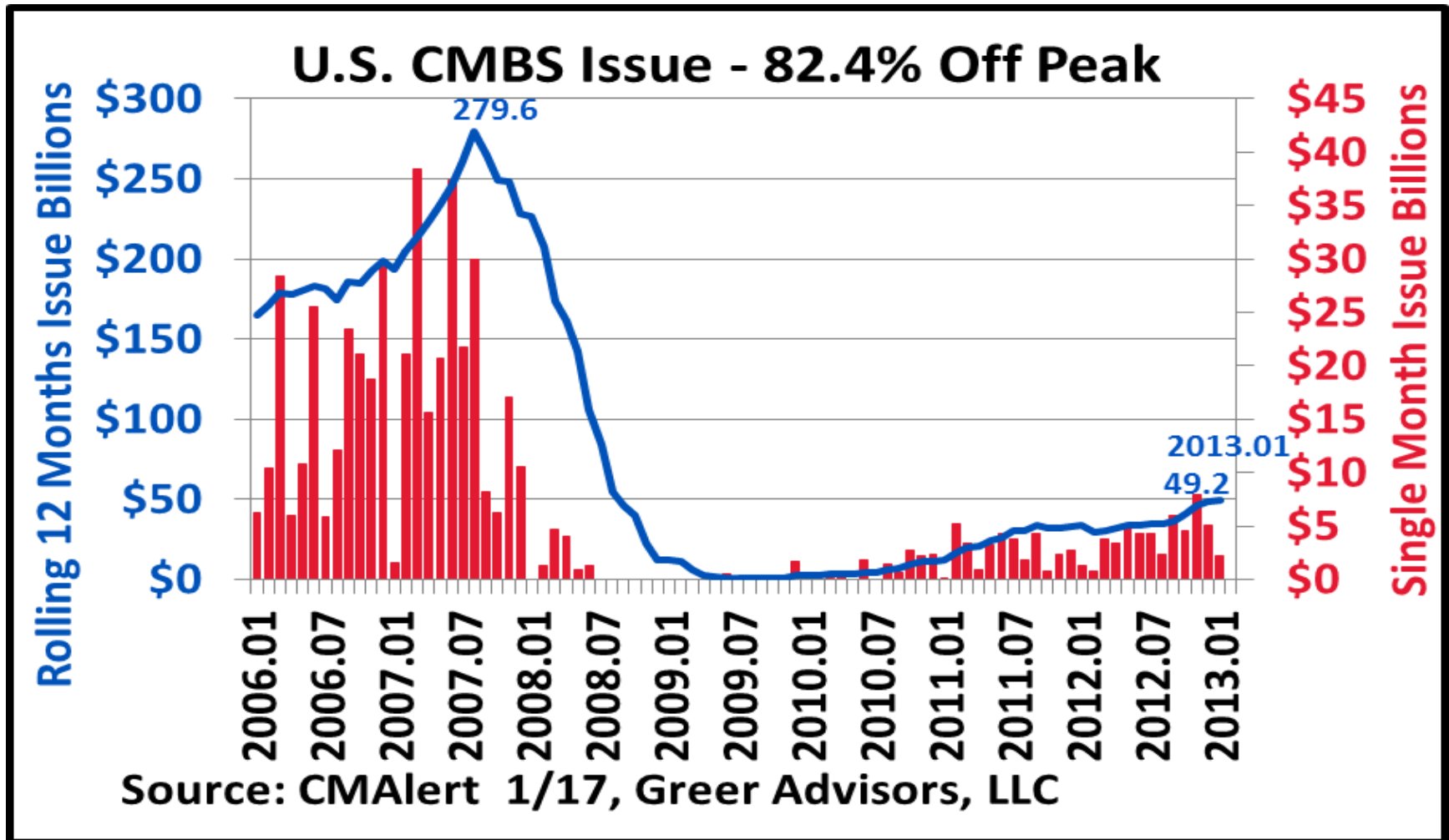
- Real Estate Capital Markets

Top 5 - Bottom 5 U.S. Markets by Vacancy

Industrial				Office				Retail			
	Metro	Vac %	Rent \$		Metro	Vac %	Rent \$		Metro	Vac %	Rent \$
1	Los Angeles	5.0%	\$7.09	1	Salt Lake City	6.9%	\$18.27	1	San Francisco	2.8%	\$28.82
2	Houston	5.2%	\$5.49	2	Albany/Schenec	7.3%	\$14.34	2	Miami-Dade Cou	3.9%	\$28.57
3	Salt Lake City	5.3%	\$4.57	3	New York City	7.4%	\$49.48	3	Boston	4.4%	\$15.59
4	Orange County (C	5.6%	\$8.01	4	Pittsburgh	7.9%	\$18.76	4	Pittsburgh	4.5%	\$11.49
5	Long Island (Ne	5.9%	\$10.27	5	Long Island (Ne	8.0%	\$26.42	5	Salt Lake City	4.5%	\$12.78
50	Atlanta	12.0%	\$3.80	50	Sacramento	15.9%	\$19.80	50	Memphis	9.6%	\$10.06
51	Phoenix	12.4%	\$6.23	51	Atlanta	15.9%	\$18.77	51	Sacramento	9.6%	\$16.08
52	Memphis	12.5%	\$2.71	52	Palm Beach Cou	15.9%	\$25.49	52	Atlanta	9.8%	\$12.81
53	Las Vegas	13.0%	\$5.83	53	Detroit	18.1%	\$17.82	53	Detroit	9.9%	\$11.94
54	Sacramento	13.2%	\$5.17	54	Las Vegas	18.3%	\$19.48	54	Las Vegas	10.3%	\$15.83
55	Dayton	13.4%	\$3.24	55	Phoenix	19.4%	\$19.95	55	Phoenix	11.2%	\$14.32
	National Avg	8.8%	\$5.18		National Avg	11.9%	\$21.63		National Avg	6.8%	\$14.43
1	Los Angeles	5.0%	\$7.09	34	Los Angeles	12.4%	\$28.26	14	Los Angeles	5.2%	\$24.02
4	Orange County (C	5.6%	\$8.01	39	Orange County (C	13.0%	\$22.23	21	Orange County (C	5.8%	\$21.97
13	Inland Empire (Ca	7.1%	\$4.99	43	Inland Empire (Ca	13.5%	\$18.46	47	Inland Empire (Ca	8.9%	\$16.57
32	San Diego	9.4%	\$9.82	36	San Diego	12.8%	\$25.50	9	San Diego	4.8%	\$20.84
	Min	5.0%	\$2.71		Min	6.9%	\$12.44		Min	2.8%	\$9.13
	Max	13.4%	\$12.92		Max	19.4%	\$49.48		Max	11.2%	\$28.82
	Spread	8.3%	\$10.21		Spread	12.4%	\$37.04		Spread	8.5%	\$19.69
Note: 1) Rents are Quoted Rents, 2) National Totals Cover all 140+ Markets, 3) Rankings limited to Top 55 Markets based on RBA											
Source: CoStar Group, Inc. Greer Advisors, LLC											

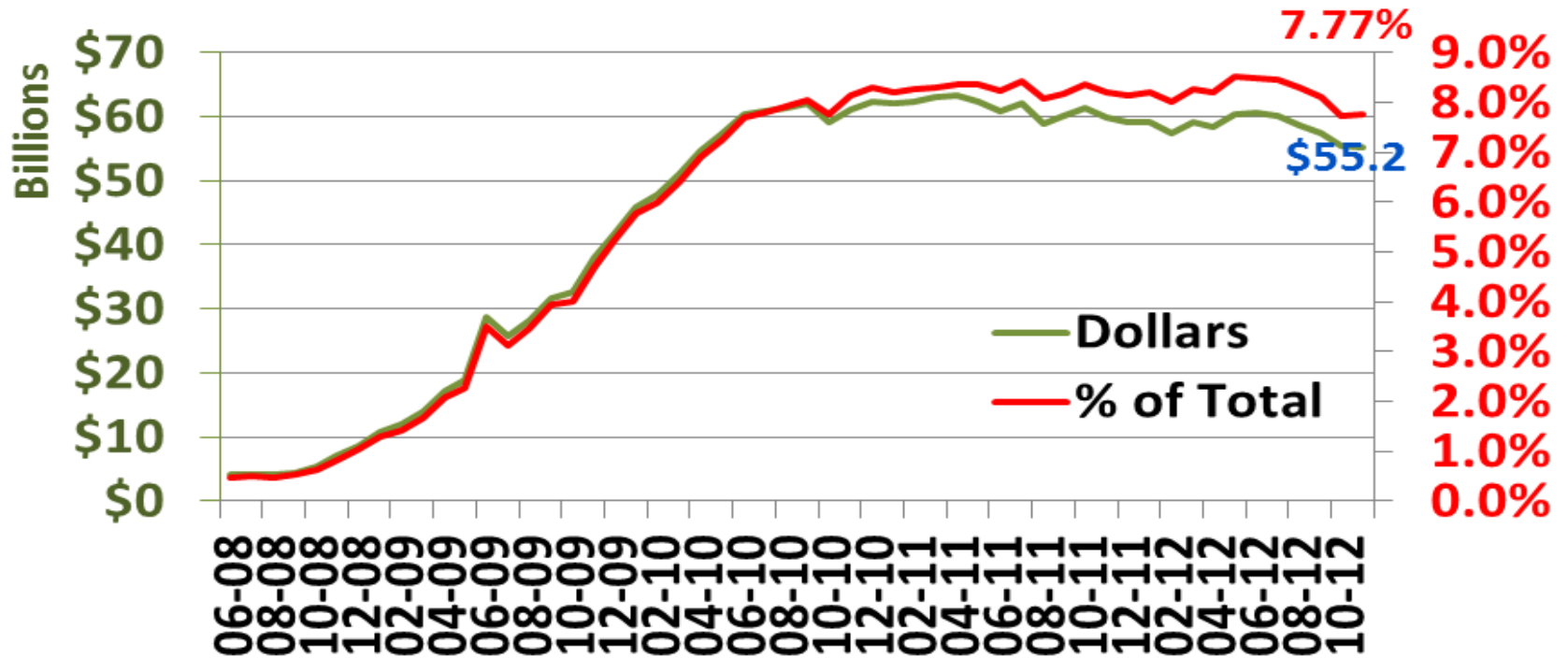
Source: CoStar as of End of 2012

CMBS Issuance – Still Off



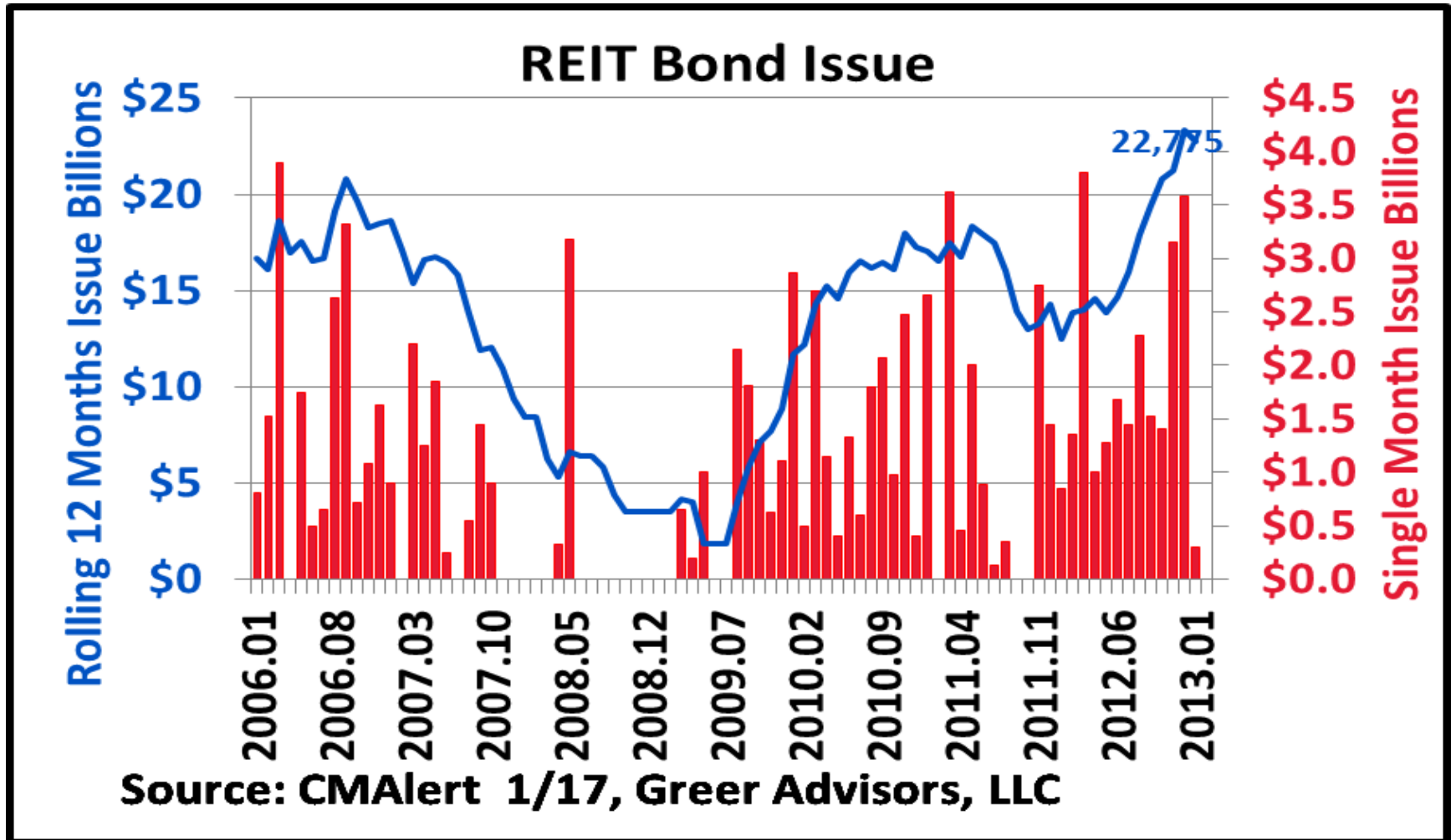
CMBS Delinquencies

CMBS Delinquencies - EOM Nov 2012

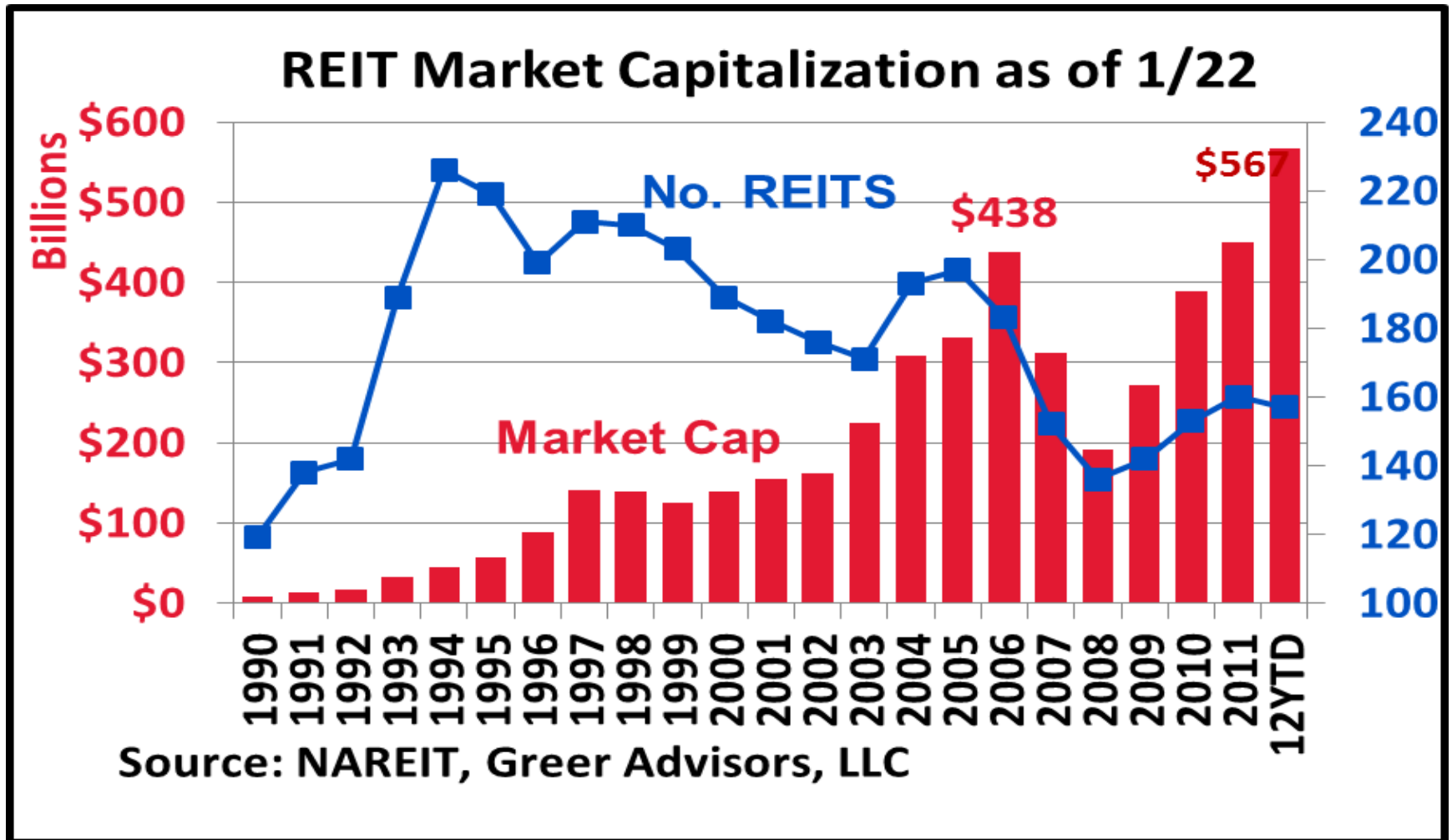


Source: Realpoint (fka Morningstar) , Greer Advisors, LLC

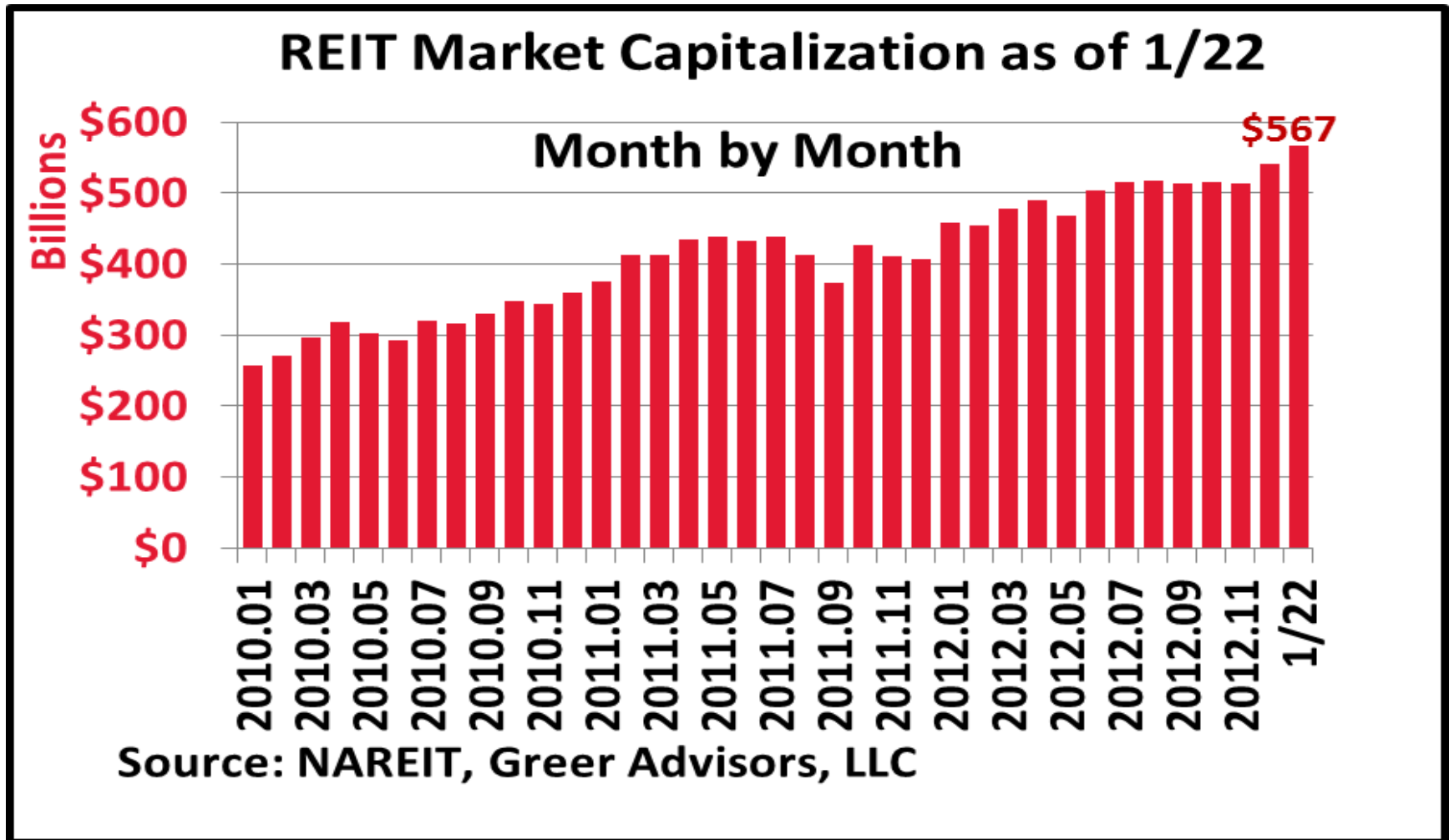
REIT Bond Issuance – New High



REIT Market Capitalization – Long Term

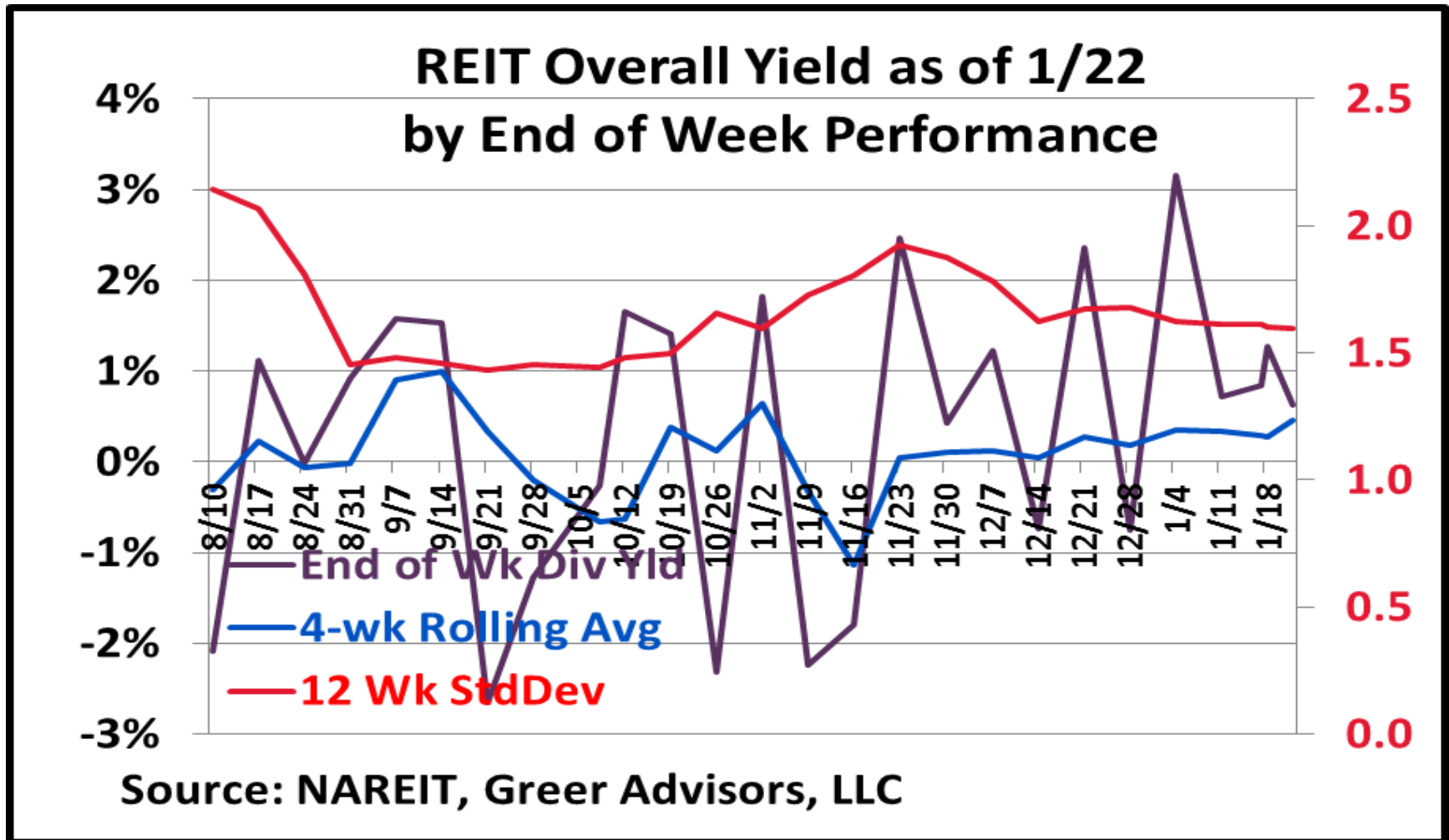


REIT Market Capitalization – Short Term

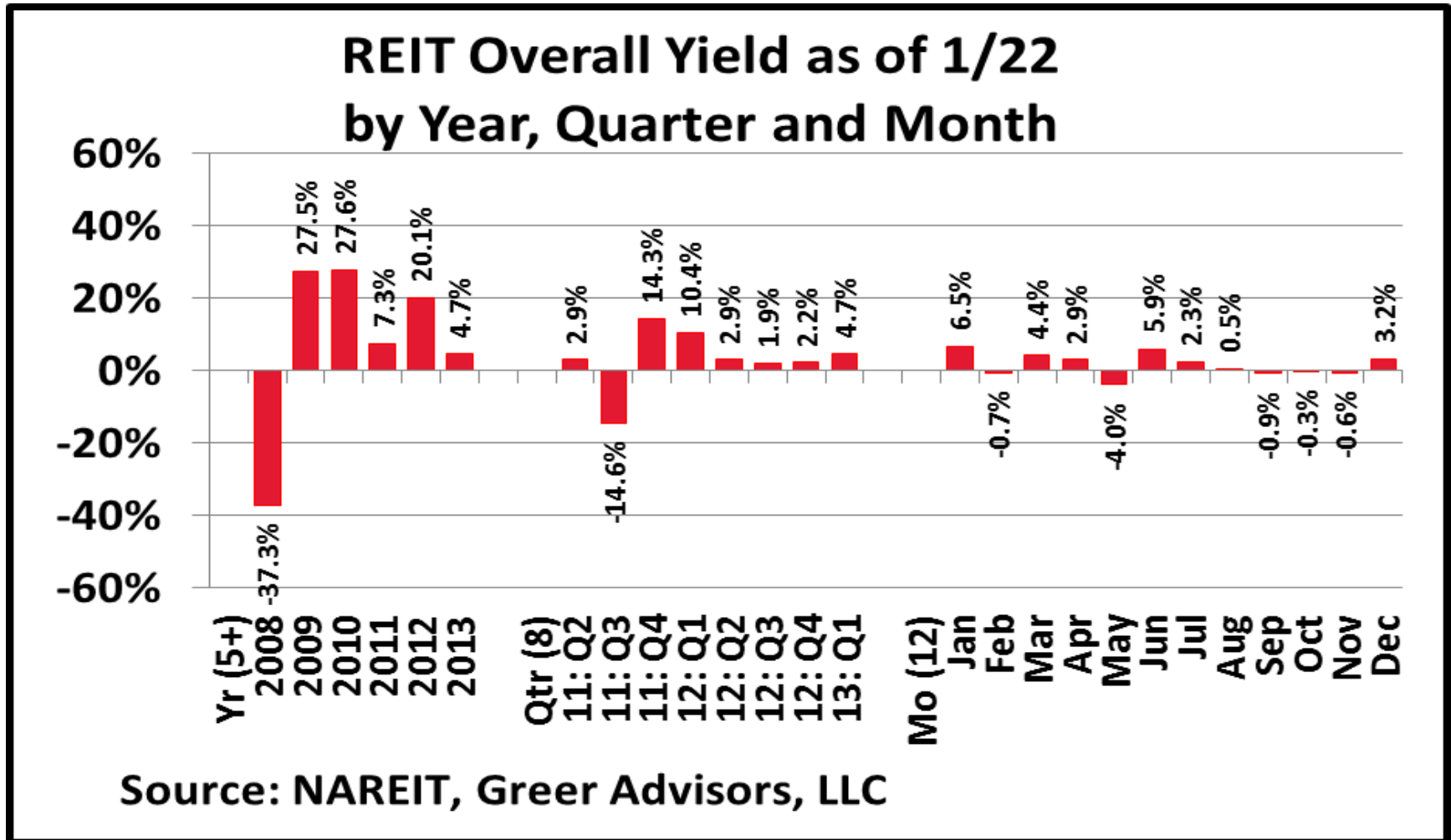


■ Risk Pricing

REIT Dividend Yield - Volatility



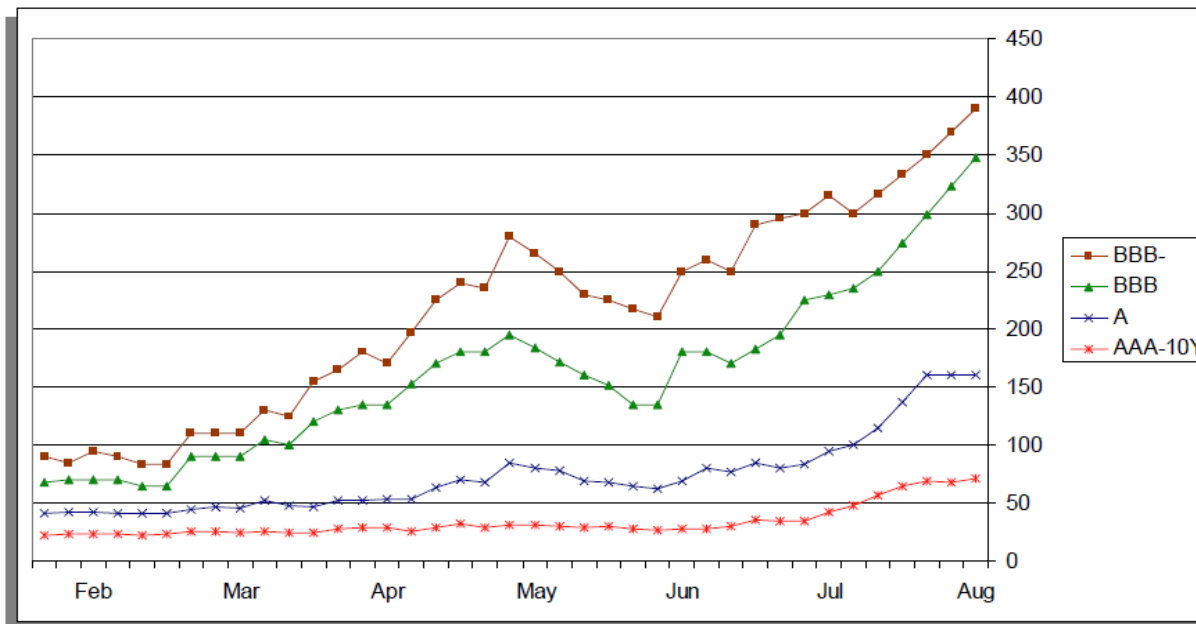
REIT Dividend Yield – Property Types



What Broke – CMBS Yield Rates Rose

- Slide from 8/3/2007 Presentation

CMBS Spreads are Widening - Pricing Trends



Source: CMAalert 8/10/07, CMAalert-Morgan Stanley 8/8/07, Bank of America - Real Estate Research

15 Note: All Spreads are quoted as "Spreads over Swap Rates"

Interest – What Broke - AAA vs BB Spreads

Greer CMBS / CMBx Yield RateTM				
Tranche	Yield	Suboord	Weight of Debt	Contribution to Total
AAA	2.27%	29.76%	70.24%	1.59%
AJ	3.14%	12.70%	17.06%	0.54%
AA	4.76%	10.63%	2.07%	0.10%
A	9.19%	8.00%	2.63%	0.24%
BBB	26.86%	4.72%	3.28%	0.88%
BBB-	28.20%	3.68%	1.04%	0.29%
BB	101.90%	2.69%	0.99%	1.01%
Unrated	176.00%	0.00%	2.69%	4.73%
Implied Overall Debt Yield			100.00%	9.38%
Loan to Value Ratio				75.00%
Class-A Equity Yield Total Yield			28.00%	14.04%
Class-B Equity Yield Total Yield			102.00%	32.54%

Notes: ① The table is somewhat complicated, as evidenced by the numerous footnotes. Several conclusions can be drawn. 1) If the 'Implied Overall Debt Yield' is greater than loan rates in the marketplace, the CMBS market CAN NOT recover because the required bond yields are too high to make debt affordable to borrowers. 2) When the spread between AAA and BB tranches is above 500 bps (now at 9,963 bps), the market can't recover because of risk aversion for lower-rated tranches. As a point of reference, January '07 AAA-BB CMBS spreads were around 65 bps. Lastly, the yields for each tranche provide tremendous insight into the pricing of risk premiums for each layer in the capital stack.

② MarkitTM Data and Calculations based on close of 1/23. Swap (10Yr) as of 1/22.

③ Coupon and Price data were from MarkitTM for AAA Senior through BB bonds. MarkitTM data was used as part of the calculations by Greer Advisors, LLC to determine Spreads. Subordination levels were from MarkitTM.

④ Profit / arbitrage opportunity for the issuer was ignored.

⑤ The yield spread for "unrated" classes were based on (BBB-yield minus BB yield) times 1.0, round to the nearest bp. Class-A property equity yield was assumed equal to the BBB- (last investment-grade piece) yield rounded to the nearest 100 bp. Class B property equity yield was assumed equal to the BB yield, rounded to 100 bps.

Bubble Creation & Bursting - Causes

Drivers Leading Up to Bubble

- Vicious Upward Cycle of Growth Created Buyer Greed
- Cheap Supply of Capital to Fund Loan Demand
- Unrealistic Growth & Profit Incentives Across Industry
- NSROs 😊 , Issuers, Originators – Misaligned Incentives

Drivers Causing Bubble to Burst

- “Never Before” Rise in Delinquency & Loss Rates
- Faith in Ratings Lost
- Risk went from “Under-priced” to “Over-priced”

■ National Statistical Rating Organization

■ Outlook & Forecast

Greer's Recovery Signs – Prereq's to Recovery

- \sqrt CDS Exposure under \$25 Trillion (i.e. under 50% of peak)
- \sqrt Stable or Decline in CMBx Yield Spreads for 6 weeks
- Re-emergence of CMBS market
 - New CMBS Market will include:
 - Issuer Keeps 1-5% 1st-loss piece
 - AAA Subordination near 30%....
 - AAA is 70%, not 90% of issue
- \sqrt REIT Market Capitalization (Total Value) Stabilizes or Increases for 6 months
- Consumer Confidence Rises and Stays Above 70 for 6 months
 - As of April 2012 (last report) index at 69.2 (1985=100)
- Risk Curve (AAA Sr. vs BB) flattens to under 500 bps. As of 4/25/2012 CMBx spread stands at 9,593 bps, nearly 100 pts

Greer's 3-Year Forecast as of 4/26/2012

- Barbell Modest Growth or Global Recession
 - Global Economy Heals or Not
- Cap Rates will Rise 0.5-2% during 2012-13
 - Mostly in class B/C
 - Trophy Class A will remain low until Flight to Quality Stops
- Margins (to 10 Yr Treasuries or LIBOR) will rise and settle at 300 ± 50 bps over 10 year Treasuries, but might over-correct in the short run, say 10Yr 400+ bps.
- Values have recovered slightly.
- Individual Market Performance will continue to vary widely.
 - 10-30% difference in Top vs Bottom
- Change Creates Opportunities – Build Businesses
- SBA remains very Active

Conclusions

- MBS Loss Rates Remain at All Time Highs
- Class A vs. B/C Big Cap Rate Spreads
- Reduced Leverage for ALL Investor Deals, More RECOURSE
- SBA will remain Only Source for High Leverage
- MBS – Very Very Slow Return. Need New Business Model
- Insurance Co's, Fannie/Freddie and Some Lenders are Active
- CASH WILL REMAIN KING!
- Rents / Vacancies Remain better than early 1990s

Quote of the Day

“...prediction is very difficult, especially when it’s about the future...”

~~NY Yankees #8, Yogi Bera~~

Niels Bohr

Nobel Laureate, 1922

Atomic Structure /

Quantum Mechanics



Questions / Answers

Greer Advisors, LLC

www.GreerAdvisors.com