
Wall Street and Commercial Real Estate

Everett Allen Greer,
Director of Research

February 20, 2008



Goals of Presentation

- Sub-Prime News
- CMBS / CDO / REIT Industries
- Size / Impact of Capital Markets
- Deal Structure – CMBS Example
- Capital Market Yields
- Rating Agencies / Risk Rating Trends
- Real Estate Trends
- Capitalization Rate — Interest Rate Lag
- What's New? What's Next?

What is a CMBS?

Commercial Mortgage Backed Security

- Type of pass-through security
- Commercial Mortgages are securitized into a pool. Rights to the revenue from the mortgages are divided into many smaller pieces (tranches, strips, slices), each with differing priorities. Proceeds are distributed to investors based on the priority of their tranche.

What is a CDO?

Collateralized Debt Obligation

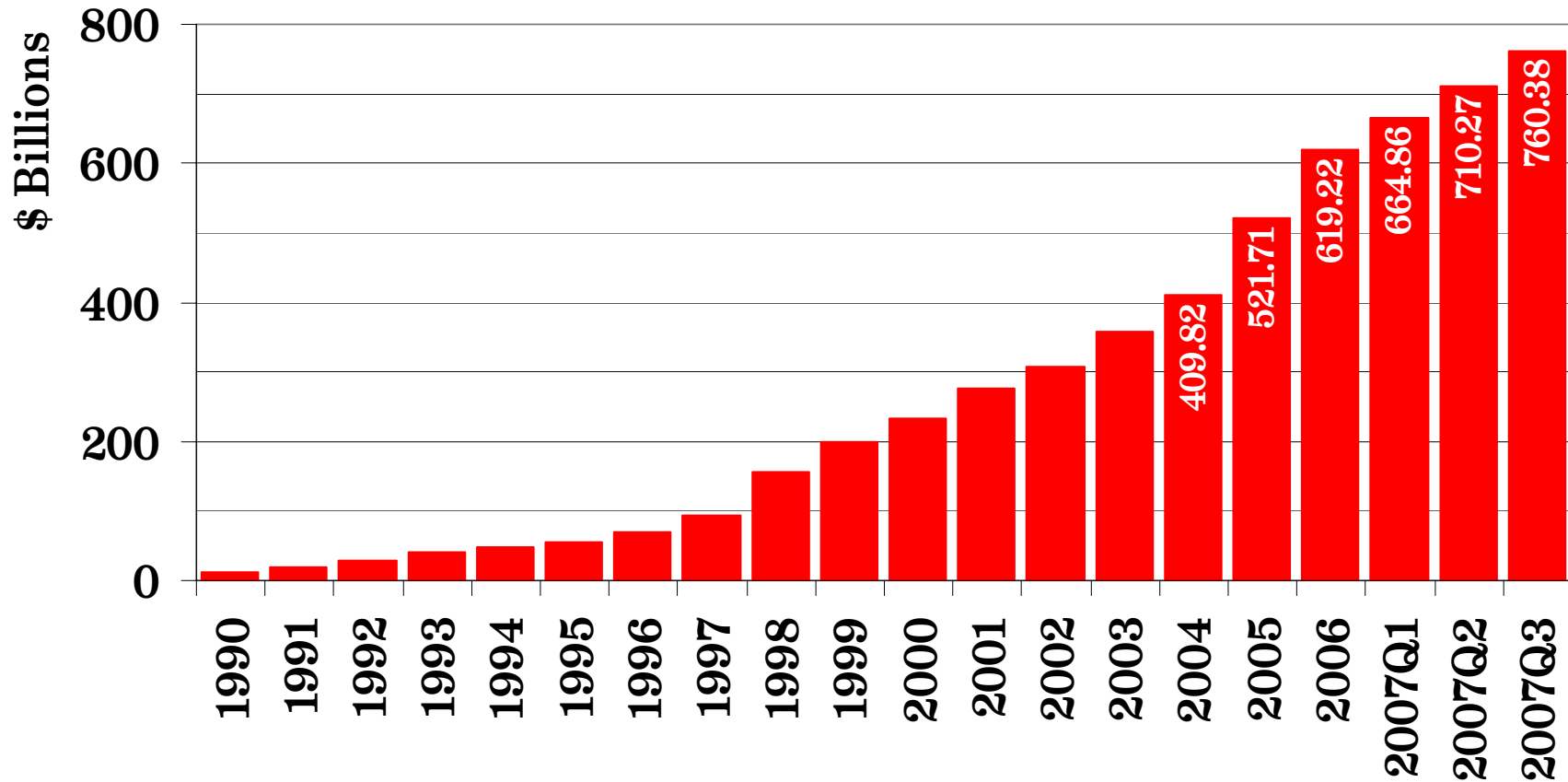
- Type of pass-through security
- CDOs are securitized debt pools, similar to CMBS, but debts can be CMBS/CDO paper, car/boat/plane loans, credit cards, or virtually any type of debt obligation. Rights to the revenue from the obligations are divided into many smaller pieces (tranches, strips, slices), each with differing priorities. Proceeds are distributed to investors based on the priority of their tranche.

What is REIT?

Real Estate Investment Trust

- Type of Pass-through Security
- Effectively a corporation
- 95% of income passed through to shareholders. No “corporate” tax. All earnings single-taxed at shareholder level.
- Current “Industry” Issues:
Definition of Assets, Max Debt Load, Yield

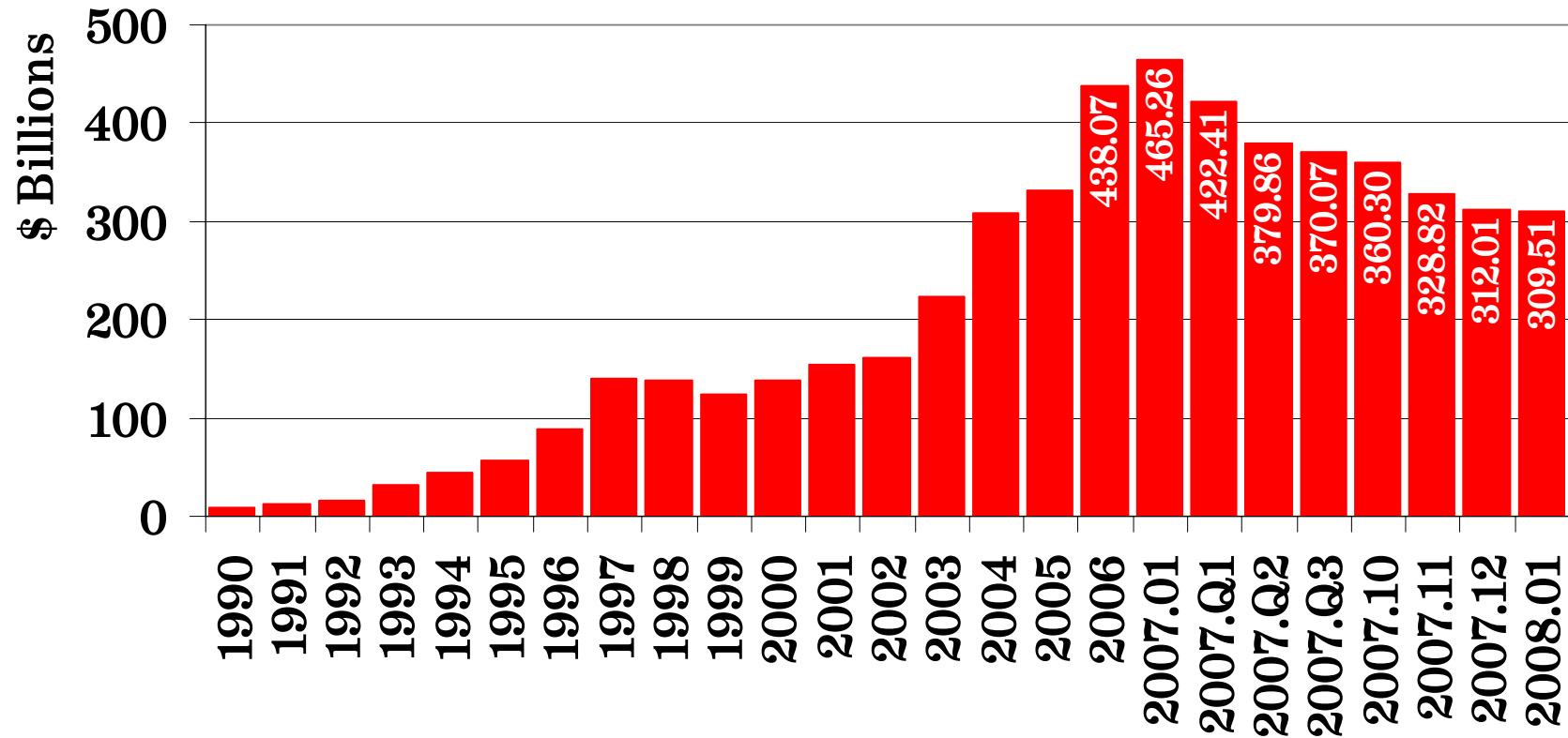
CMBS Outstandings in U.S.



Source: Federal Reserve, Flow of Funds, Z1-L.126-NSA, BAC - Real Estate Research

Note: Total of Multi-Family and Commercial Mortgage Asset Backed Securities.

REIT Market Capitalization



Source: NAREIT, Bank of America Real Estate Research

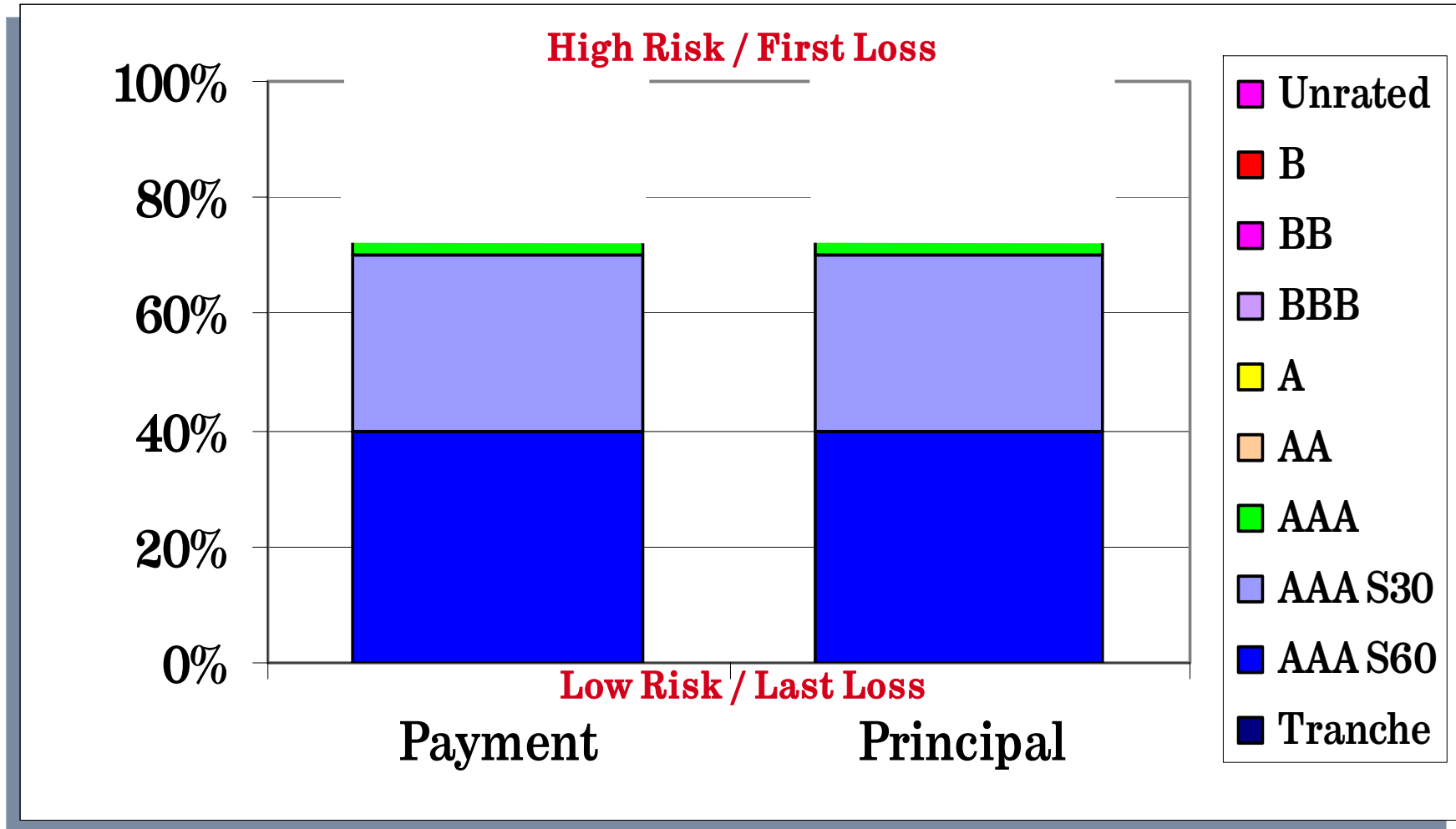
Note: Includes Equity, Debt and Hybrid REITS

Example of a “Typical” CMBS

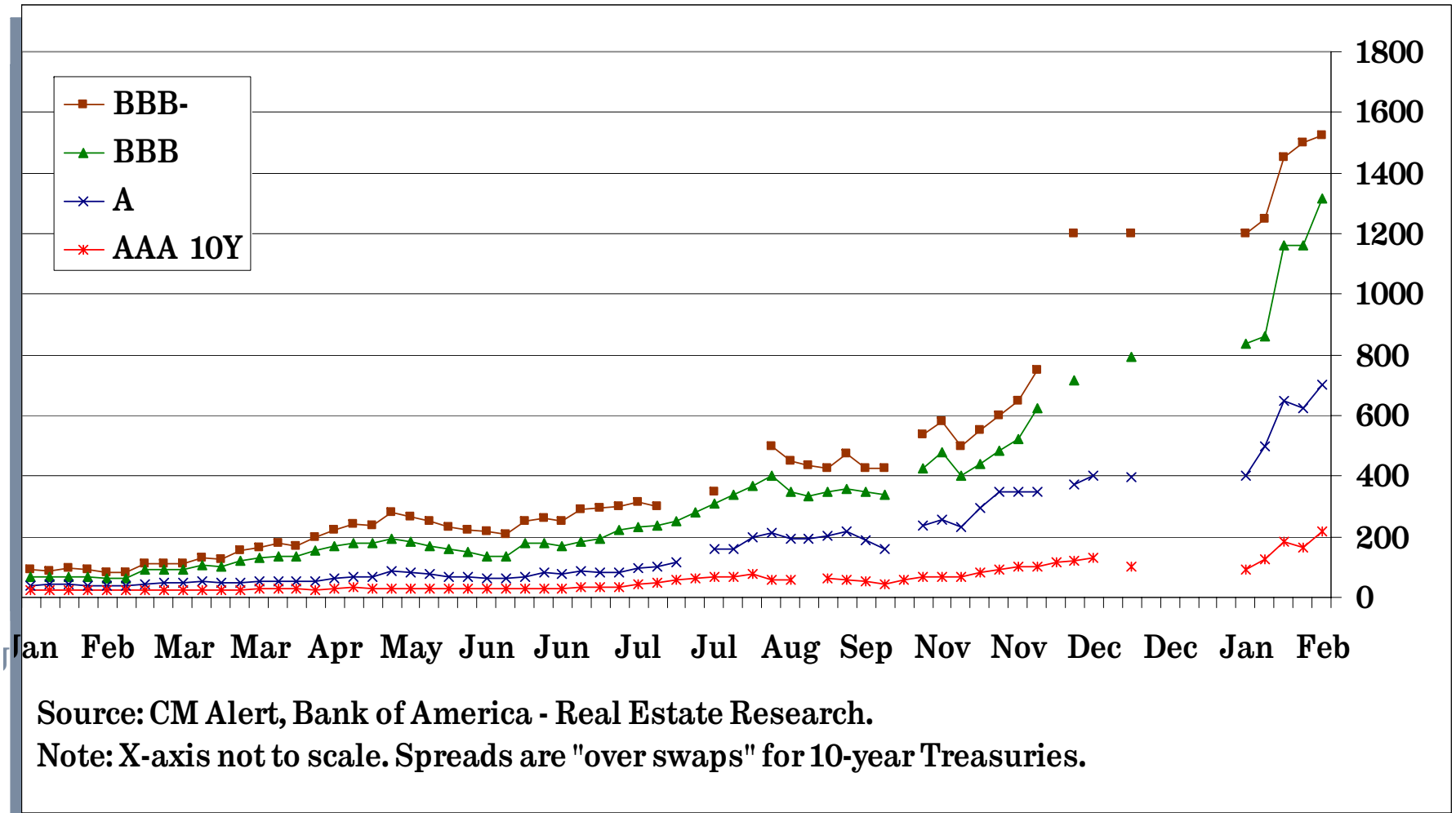
		No. Loans	250		
		Avg. Loan Size	\$10,000,000		
		Total Loan Amt.	\$2,500,000,000		
		Index Name	10-Year Treasury		
		Index Rate	5.000%		
		Avg. Margin	1.750%		
		Avg Yield	6.750%		
2007.01	2008.01	Tranche	Approximate	2007.01	2008.01
0.0020	0.0200	AAA S60	60.0%	5.200%	7.000%
0.0025	0.0210	AAA S30	30.0%	5.250%	7.100%
0.0030	0.0220	AAA	12.5%	5.300%	7.200%
0.0040	0.0450	AA	9.0%	5.400%	9.500%
0.0100	0.0700	A	8.0%	6.000%	12.000%
0.0175	0.1315	BBB	5.0%	6.750%	18.150%
0.0250	0.1450	BB	4.0%	7.500%	19.500%
0.0400	0.1600	B	2.5%	9.000%	21.000%
0.0500	0.2000	Unrated	0 to <2.5%	10.000%	25.000%
			Weighted Average Yield	5.494%	8.322%
		Implied Annual Excess Return		0.256%	-2.572%
		Note: Assumes 1% swap, agency, trust, servicer and other fees.		\$6,400,000	-\$64,300,000



Subordination Graph



CMBS Yield Spreads (Spread to Swap)

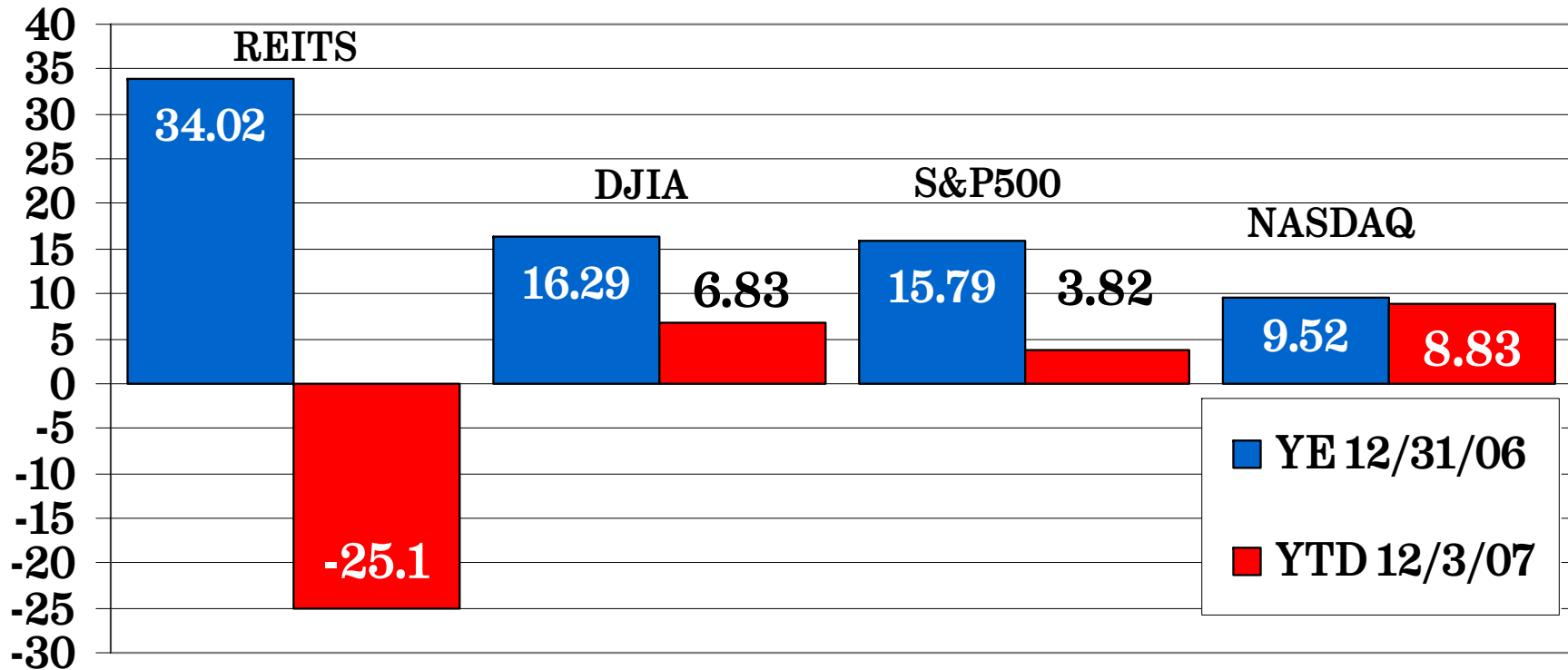


CMBS Spreads — Yield Rate Implications

Tranche	Rise in Yield	Weight	Debt v Equity	Total Weight	Impact
AAA	220	90%	75%	67.50%	148.50
A	700	4%	75%	3.00%	21.00
BBB	1315	3%	75%	2.25%	29.59
BBB-	1385	2%	75%	1.50%	20.78
Unrated	2000	1%	75%	0.75%	15.00
Class A Prop.	2000	100%	25%	25.00%	500.00
Note: Class A assumed to have no "unrated" tranche				Total	740.64
Class B- Prop.	2400	100%	25%	25.00%	600.00
Note: Class B- assumed 250 bps above "unrated"				Total	834.86

Note: Market for < BBB paper is gone! Pricing is uncertain!
Higher subordination = even greater impact.

Benchmark Returns — Changes so Fast!

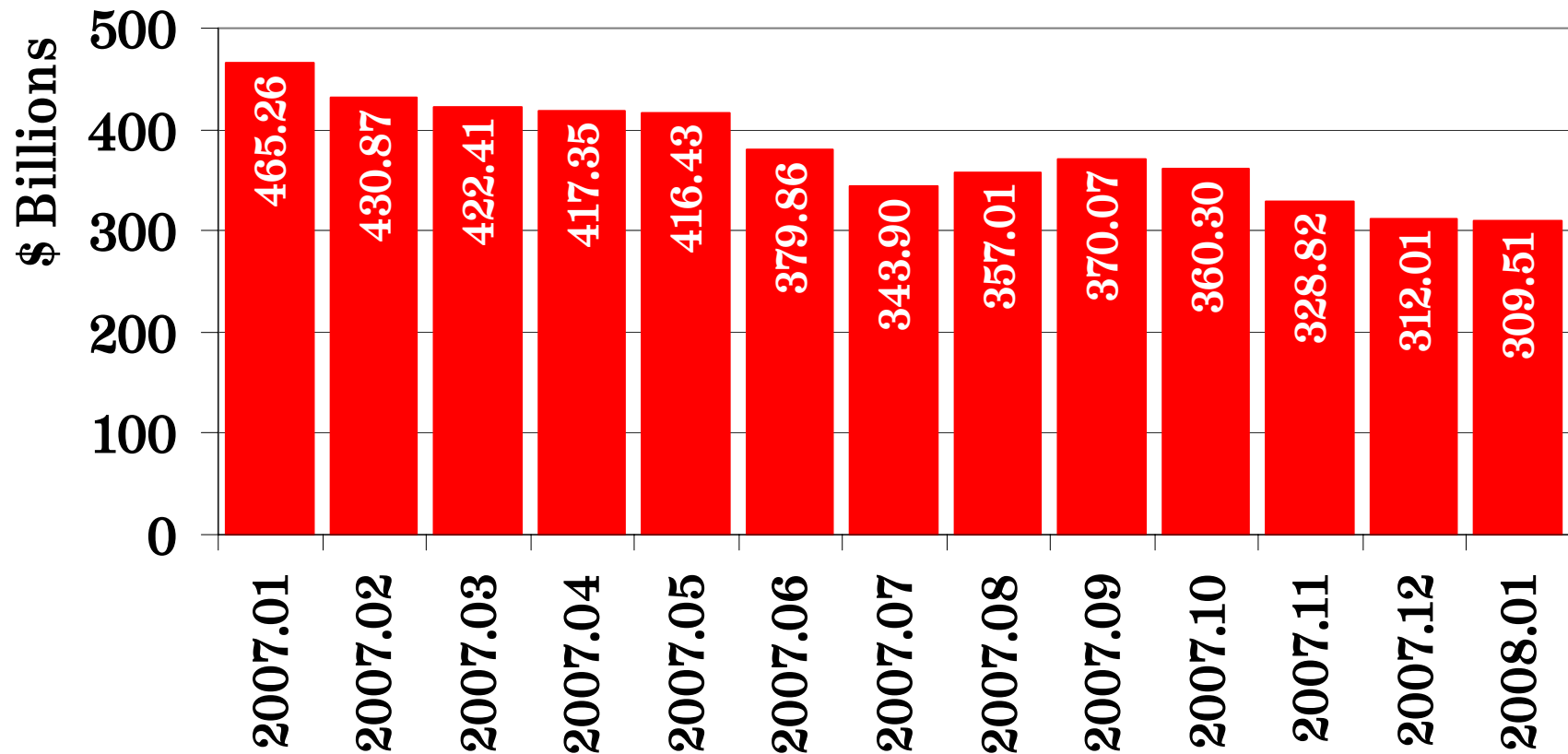


Source: NAREIT, Bank of America Real Estate Research.

Note: “Price Only” returns, excludes dividends.

YTD = REIT = 11/30/07; Dow, NASDAQ, S&P = 12/3/2007

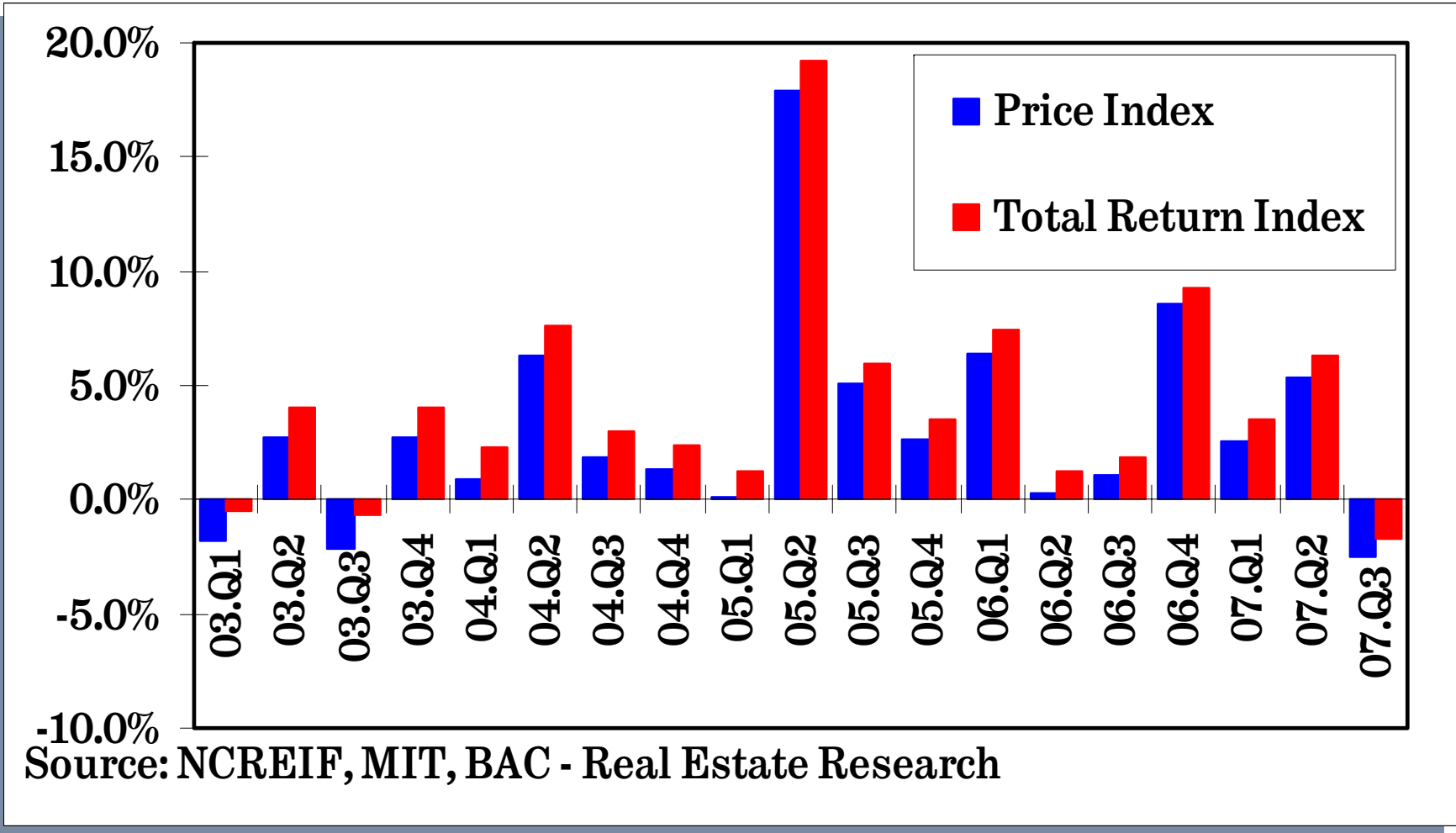
REITs Lose \$156 Billion or 33.5% of value



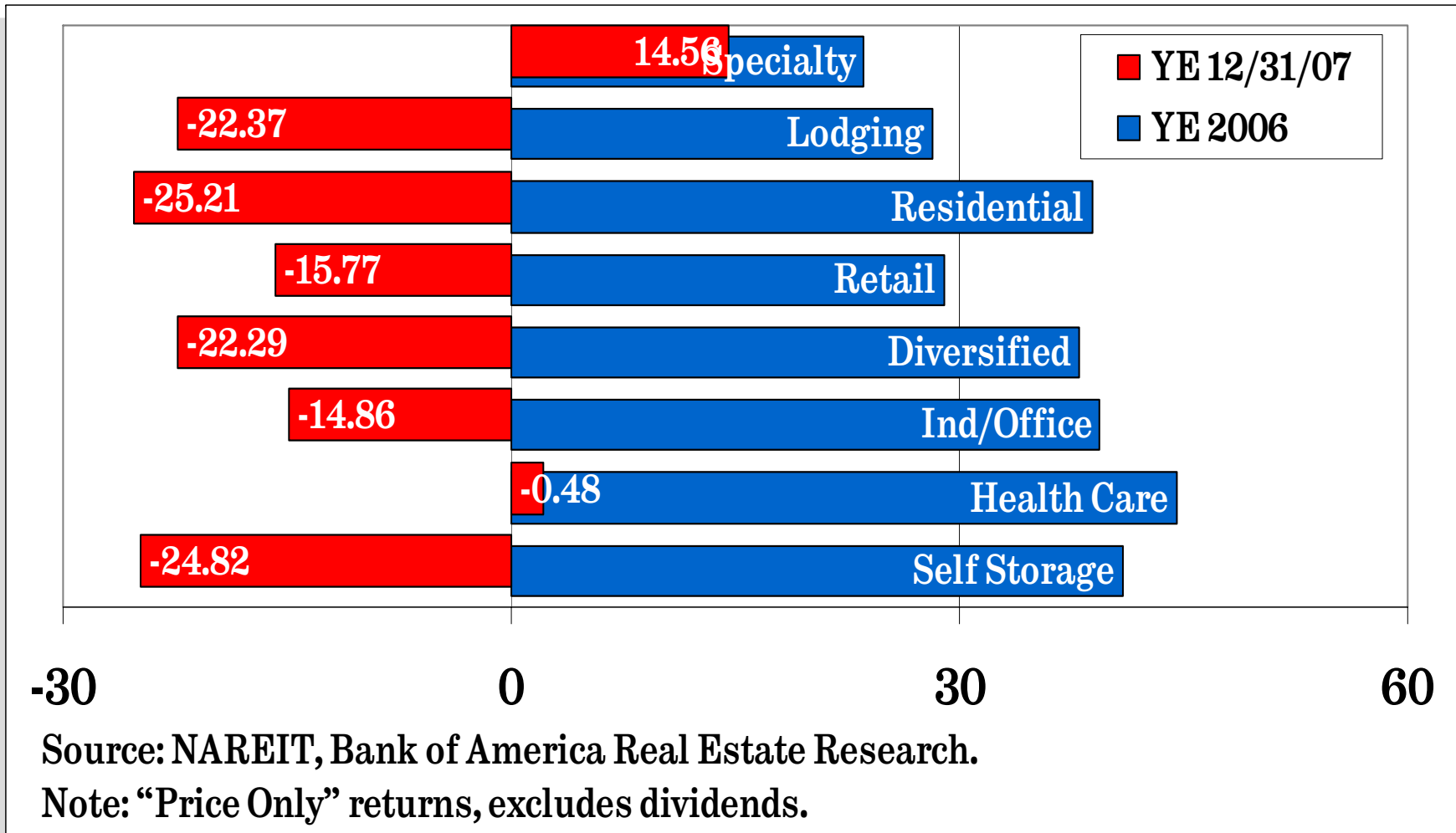
Source: NAREIT, Bank of America - Real Estate Research

Note: Includes Equity, Debt and Hybrid REITS

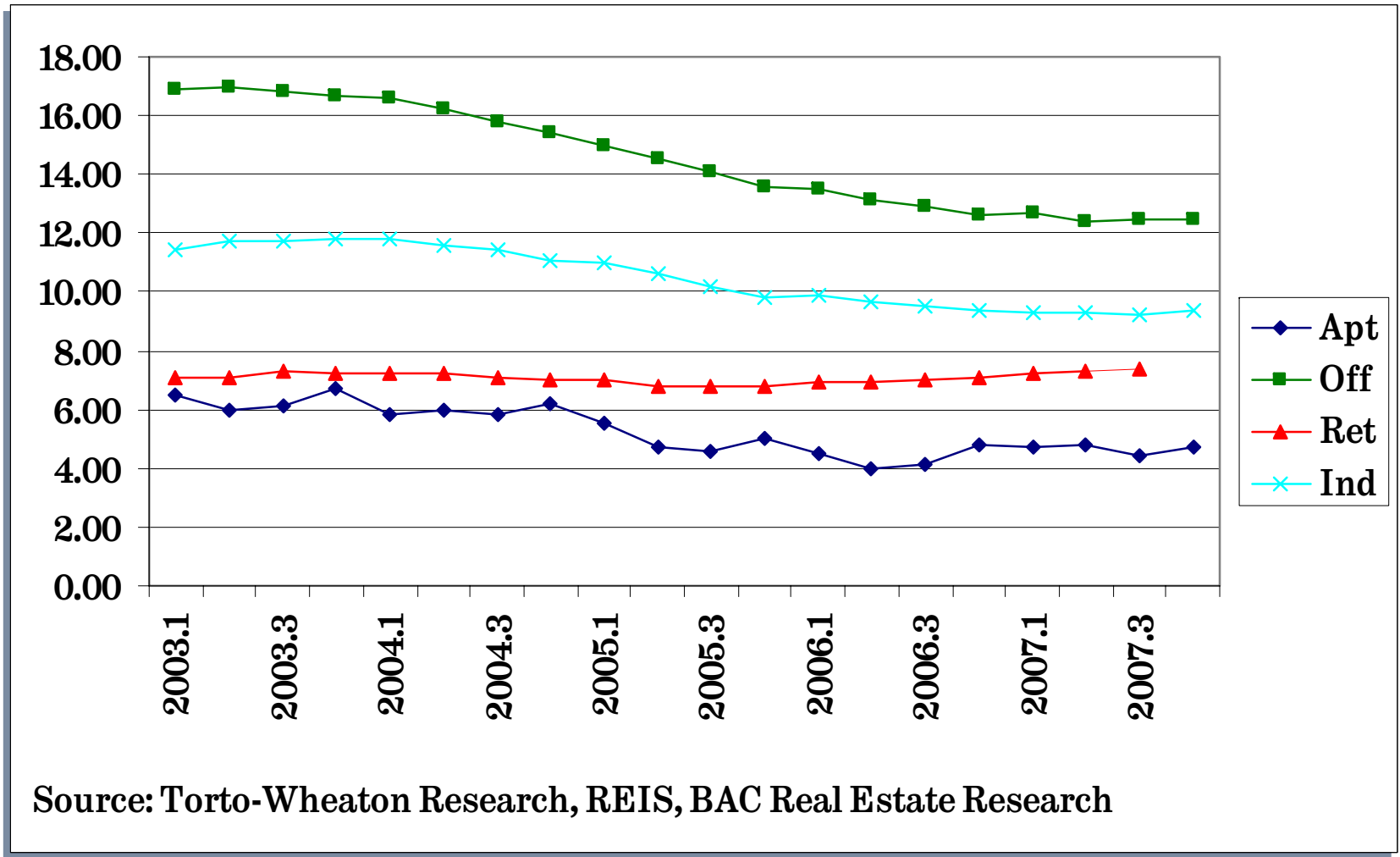
NCREIF 07.Q3 Price -2.5% / Total -1.7%



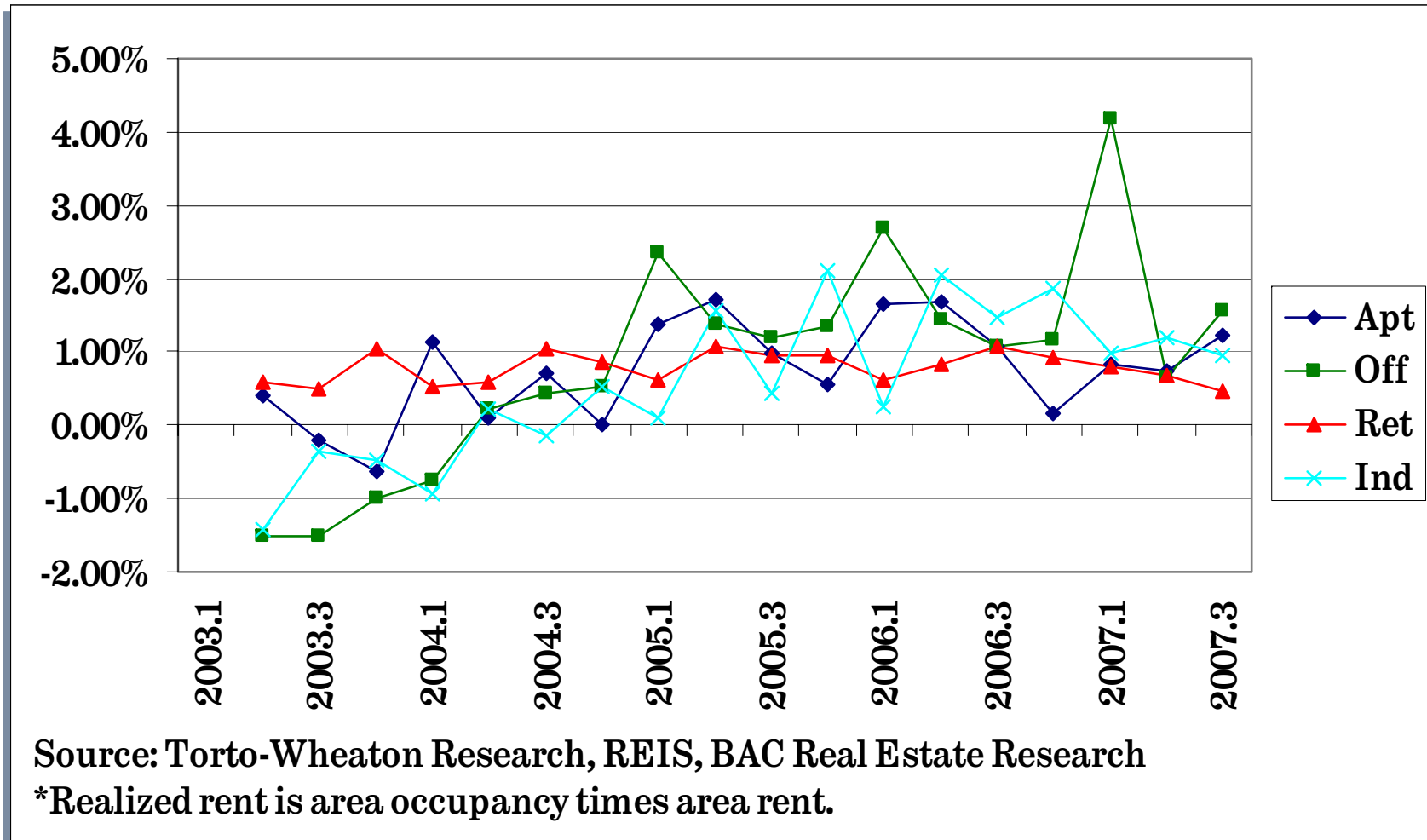
REIT Property Type Returns — Old vs. New



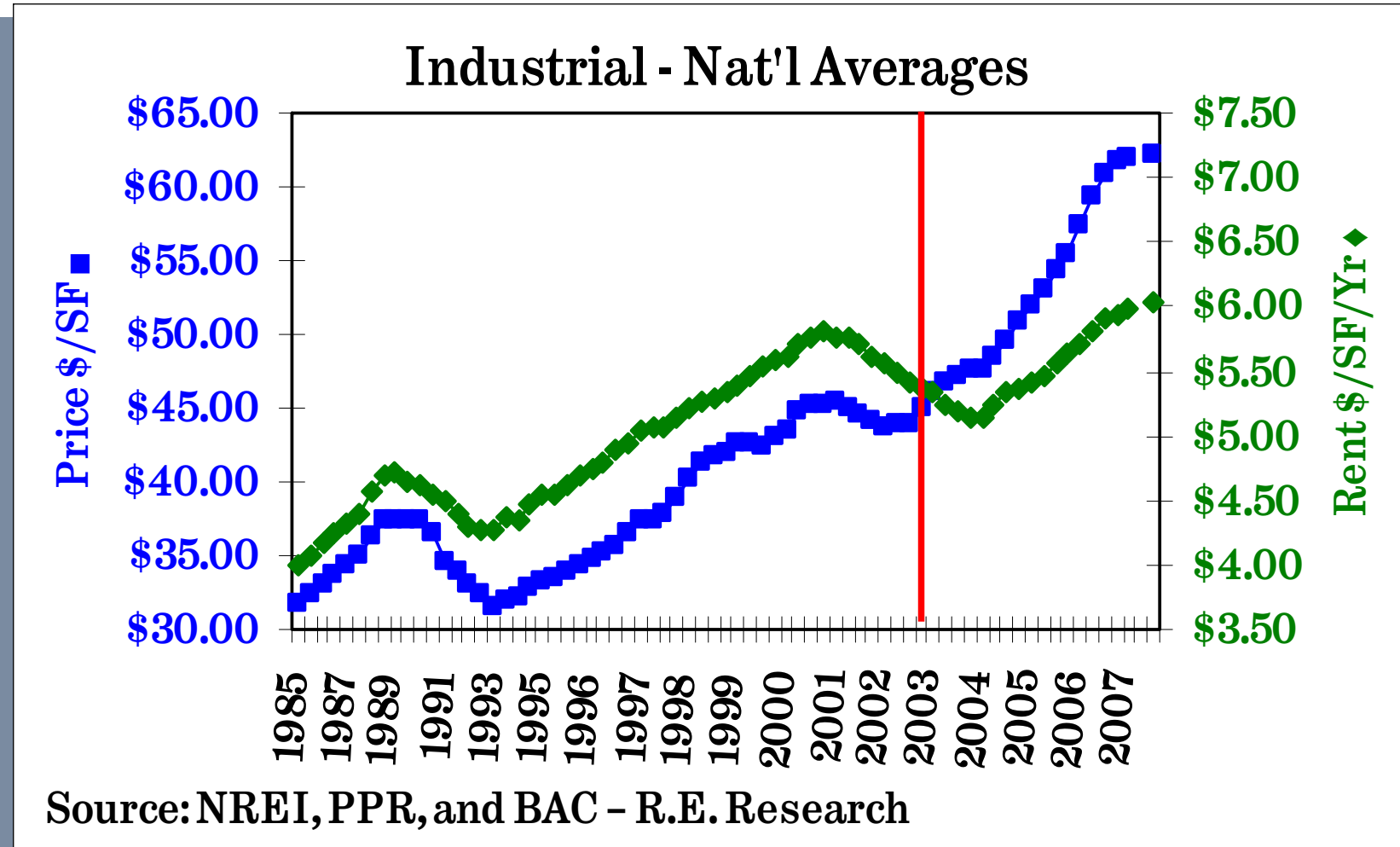
National Trend — Vacancy



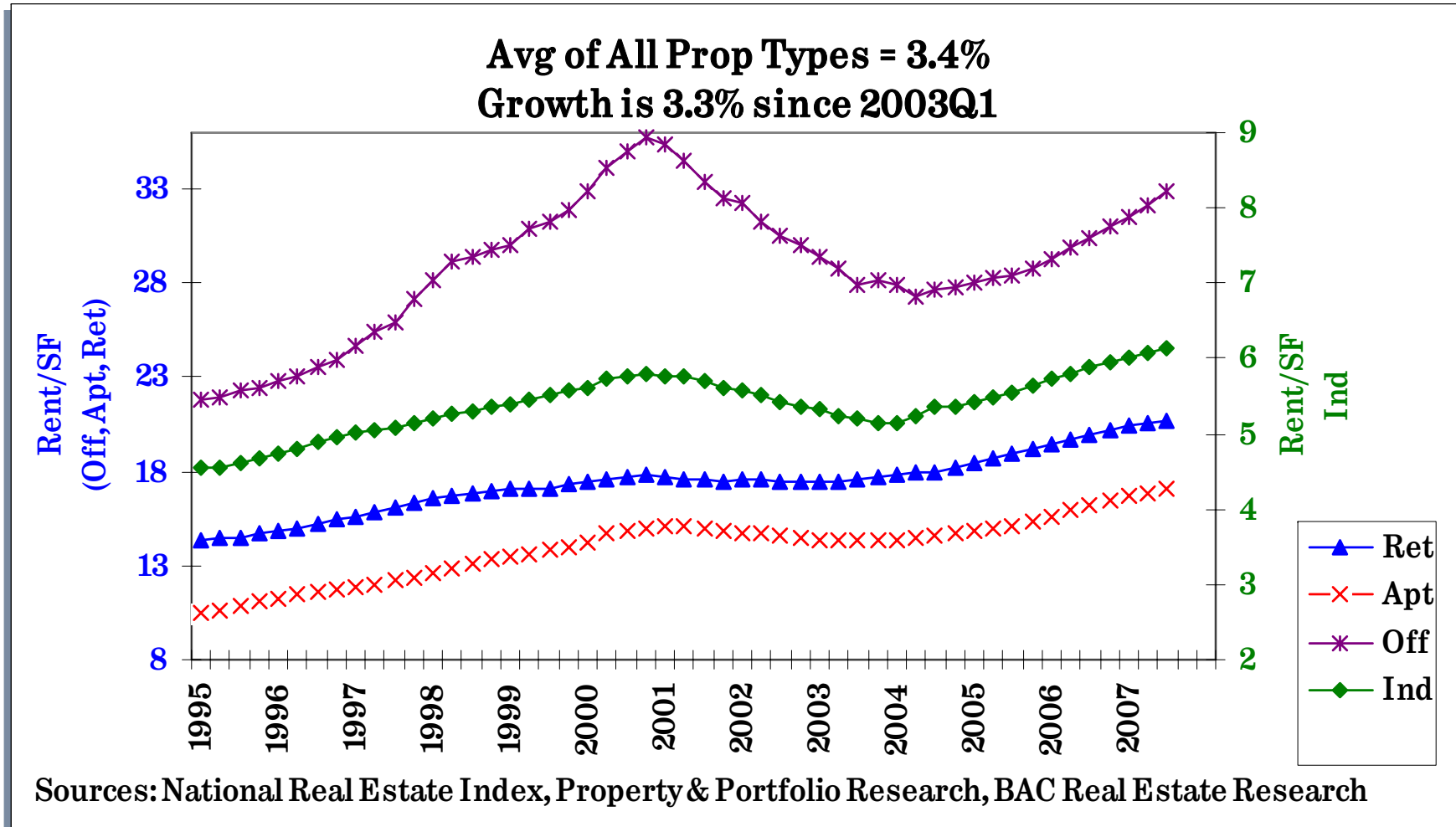
Realized Rent Growth



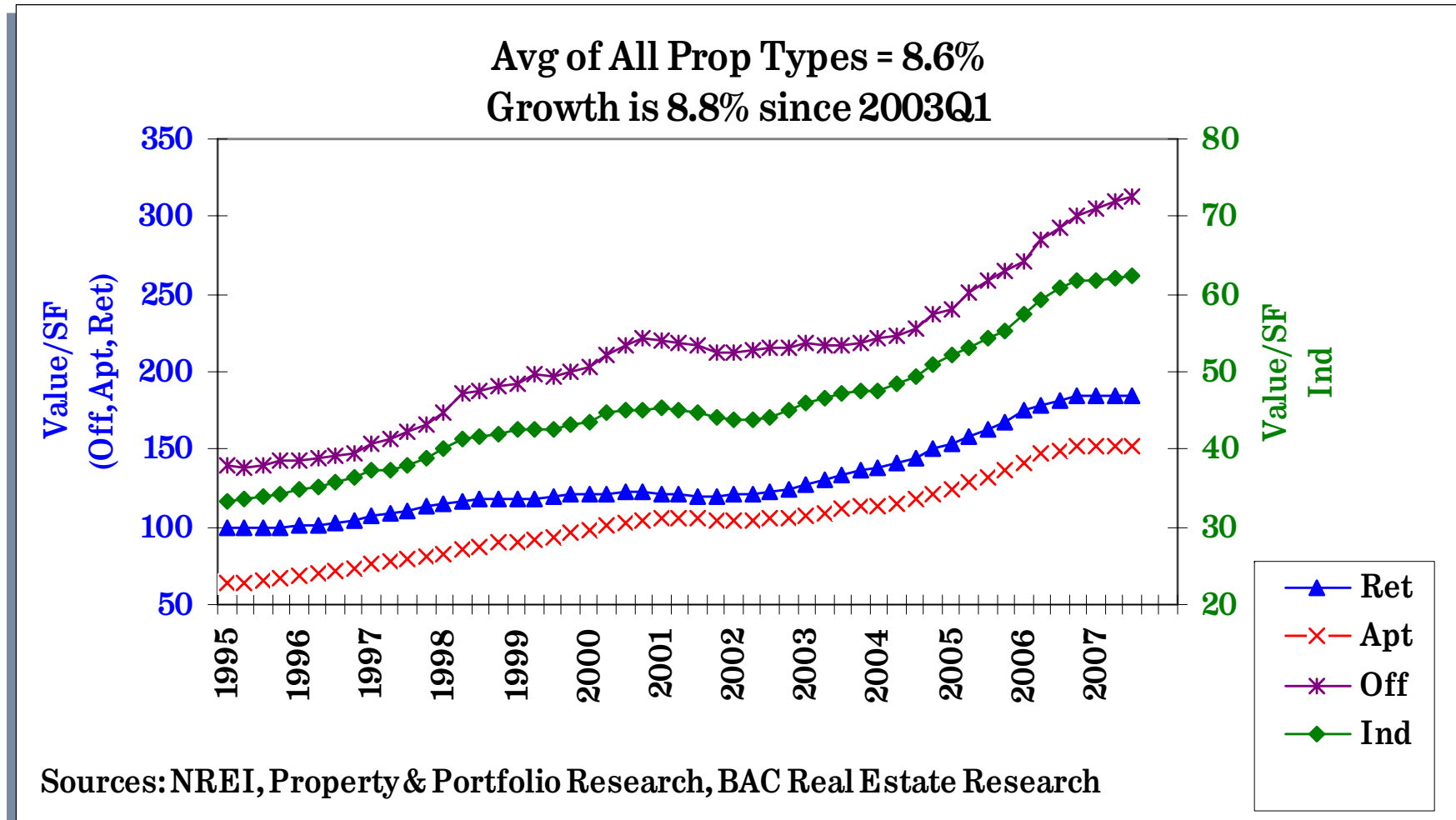
The Relationship Breaks in 2003



Market Trends — National Rents



Market Trends — National Values

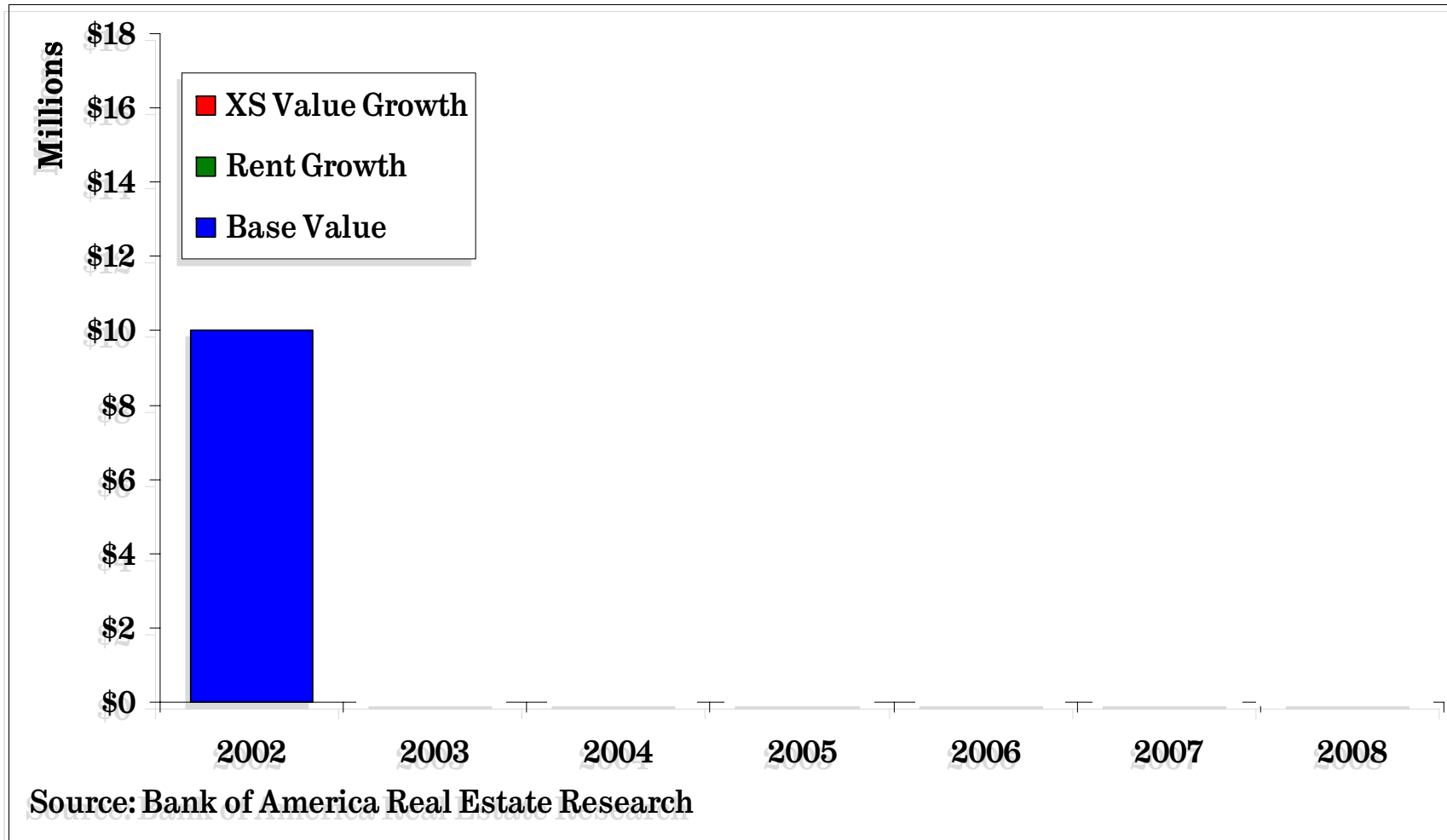


Growth Example — Value vs. Income

Year	Rent	RentG	Ind Cap	Value
2002	750,000	3.30%	7.50%	\$10,000,000

- Increase in value was only “interest rates” first 2 years. Momentum effect carried it further. What happens when it stops?

Rent versus Value Growth



News

- **Sub Prime Losses May Reach \$400 Billion (Bloomberg)**
- **CDO Losses May Reach \$260 Billion (Bloomberg)**
- **Citi, Deutsche, JP Morgan, Merrill, UBS, Wachovia, Wells, HSBC, SunTrust, Bear Stearns, Bank of America and more**
- **Moody's Announces layoffs – 11/30**
- **Credit Suisse Pulls Plug on Canadian Operation – 11/30**
- **Moody's Reports Decline in US Property Values – 11/20**
- **Artesia Mortgage Closes Atlanta & New Orleans 11/16**
- **Goldman Sachs Consolidates (5 regions to 3) – 11/16**

Source: CM Alert, Bloomberg.com, Various Papers.

Quote of the Day

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

~~NM Number, #8, No dia create~~

Conclusions

- CMBS Market – New Market Pricing
- REIT Industry – Down 25+ Percent
- NACREIF – Down Slightly
- Many Lenders are Closing or Reducing Volume
- Financing Costs Have Risen; Capitalization / Yield Rates
- Cash is KING
- Spread Between Rent vs Value Growth
- Rents/Vacancies Should continue to Perform
- Value(s) Undergoing Correction

.....see next slide!

Greer - 3 Year Forecast as of 2/20/2007

- Borrowing Rates for Commercial Real Estate will Rise
- Margins (to Treasury) will rise 200+ bps 2008-09
- Rent Growth will average 3% to 5% per year
- Value Growth will lag Rent Growth 30% over 2-3 years
- Values (National Average) will Fall 10-20% during 2008, and 5-15% during 2009. Individual market performance will vary widely, with “extreme” markets performing several times better (or worse) compared to the National Average.
- Capitalization Rates will Rise 2.0-2.5% over next 3 years (eg 5.0% become 7.25% = 30%+/- decline in value)

Bank of America

