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Finance, real estate leaders anticipate continued market slowdown

By SYDNE MOORE, Special to the Daily Transcript

A lineup of finance and commercial real estate leaders addressed today's volatile economic climate at the eighth annual Trigild Lender Conference, and all came to a common consensus: "The worst is yet to come." Most agreed that the situation will not start to improve until the first quarter of 2010.

Experts at the event named the credit crunch as the primary culprit in the commercial and residential real estate meltdown, as a record breaking crowd of leaders in the finance, legal and real estate industries convened downtown for the annual event, held Oct. 22-24.

"Until the credit markets ease, the economy will be extraordinarily strained," said keynote speaker Sam Chandan, Ph.D., chief economist and senior vice president of research for New York City-based **Reis Inc.** "Constraints on credit diminish consumer's capacity to spend, which affects all industries," he added. "No market is isolated, one thing impacts another."

Not surprisingly, the fundamental contributor to the dire situation is the residential housing slump. "We simply built too many housing units, and this problem is not going away," said Portland, Ore.-based William Conerly, Ph.D., also a keynote speaker and principal of **Conerly Consulting LLC**, chief economist of abclinvesting.com and author of "Businomics: From the Headlines to Your Bottomline -- How to Profit in Any Economic Cycle."

Fueled by soaring home values, consumers went on a spending spree, which has come to a veritable halt, Conerly said. Add to the mix a loss of consumer confidence and a tight lending market, and "you have a full blown recession," he said. "Banks do not make bad loans in bad times, only in good times," he pointed out. And these days, banks aren't even making good loans.

Even though the Fed is doling out money, "banks are nervous, as half of the assets in the whole banking system are real estate-related."

The final outcome remains to be seen. "It's still a mystery," said Conerly. "We don't know how much bank sheets have been compromised by all this."

Tough times on horizon for commercial real estate

While commercial real estate has not been overbuilt like residential, and commercial defaults remain relatively low, there are big problems in this arena as well. "The system is fragile," said panelist Clark Rogers, senior vice president of **KeyBank Real Estate Capital** in Kansas City, Mo., especially when you add on excessive risk taking and the lax oversight which created the situation.

"Commercial real estate debt is at a historic high," said Chandan, who provides commercial real estate performance information and analysis.

"Some commercial loans were based on inflated earnings, which turned out to be too optimistic," said panelist Bill Hoffman, president of San Diego-based **Trigild**, adding that the best loans for everybody concerned include a large amount of equity put into the deal.

There is just no exit strategy for the bad loans, and no way to address the rising tide of delinquencies and defaults. "Because of the difficulty in obtaining financing, more and more projects are coming out of the pipeline," Chandan said. "The potential for an imbalance -- in the demand for and supply of credit -- could emerge as the leading impediment to commercial real estate market stabilization."

Banks will continue to face challenges in extending credit, fueled by obstacles from recent years' growth in commercial real estate exposure, reduced profitability in commercial portfolios on higher delinquency management costs and spillovers from residential mortgages.

The bottom line? Commercial standards are much tighter than they were in the boom, and credit markets must ease to facilitate an orderly process of deleveraging and refinancing.

Commercial transactions will be muted through the end of the year and pricing will fall further, as "overleveraged borrowers sell assets under duress," Chandan said. "The offsetting impact of lower risk free rates has absolutely run its course." Stabilization will occur in the largest markets first, and then in secondary and tertiary markets. "In the meantime, we will see short-term loans coming to maturity, which will be difficult, and in some cases impossible, to refinance," Hoffman added.

In addition, the conference provided vital details and strategies for maximizing recovery on nonperforming commercial loans. Featuring a roster of well-known speakers and panelists, each conference section included industry experts discussing key market issues, among them: recovery options, intercreditor issues, sale and recovery, pricing assets realistically, problem loan areas, forecasts by property type and the Fed's Troubled Asset Relief Program (TARP). Also on the agenda: "Loan Recovery 101," a step-by-step look at the basics -- from warning signs to workouts to foreclosure.

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