

Commercial BUZZ

Straight From the Experts: The latest **BUZZ** in Commercial Real Estate



by Ray Hankamer

Comments by Jack Cohen of Cohen Financial: "It is clear now that really low interest rates drove really high leverage and really high leverage drove bloated values. Without the leverage in the system, values have collapsed anywhere from 30 to 60 percent on otherwise healthy real estate...given the fact that our economy lost 8 million jobs since 2007 and still has not ended job loss, the issue is when we will reach the point where job growth will drive tenant growth... This past year, considering their real estate investments, the user of capital finally had to recognize that the frequency and amplitude of three distinct cycles—the cycles of brick and mortar, the cycles of the capital markets, the cycles of the economy go hand-in-hand. If we see these cycles overlaid on top of one another, where they converge is opportunity and where they diverge is risk. The risk associated with uncertain real estate values today has never been more paramount... For higher quality properties with relatively stable cash flows, CMBS offered lower borrowing costs and greater all-in leverage. This siphoned off the better lending opportunities, pressuring banks to become more concentrated in riskier types of lending... banks hold the riskiest commercial real estate debt... we cannot legislate against greed or stupidity.

My view of the past generation is those borrowers were "brick and mortar" professionals who knew how to make money from real estate. It was a real estate business that they operated but ran into trouble when the capital markets themselves imploded. By contrast, my judgment of the borrowing community today is, they are by and large, capital markets financiers who lack the comparative "brick and mortar" skill set of professionals 20 years ago, to actually turn the real estate as a business around—that is what the industry needs most right now. Is the borrower "brick and mortar" skilled? Does he know how to get the real estate turned around with stable and increasing cash flow available for debt service? Can he take the economic loss? Answers to these questions, more than any, will dictate how much longer the real estate industry toils in disaster.

Back in September, Stephen Mihm wrote in the Boston Globe that modern finance is far from the stabilizing force that mainstream economists portrayed. Rather it is a system that creates the illusion of stability while simultaneously creating the conditions for an inevitable and dramatic collapse... [argued that] John Maynard Keynes' collective work amounted to a powerful argument that capitalism was by its very nature unstable and prone to collapse... success inevitably encourages competition and borrowers and lenders take on more risk in the reasonable hope of making more money... [but]... success

breeds a disregard of the possibility of failure... as people forget that failure is a possibility, a "euphoric economy" eventually develops fueled by the rise of far riskier borrowers, those whose income could cover interest payments but not the principal... "

Comments by **Harold D. Hunt in Tierra Grande** on accurate valuation of real estate: "Pick up the newspaper, turn on the television or log on to the Internet, and you can find the price of a publicly traded stock almost immediately. With commercial real estate, it's not so simple. Commercial properties are not publicly traded on a daily basis. As a result, market values—the prices that would be paid in an open and competitive market—are significantly more difficult to obtain... Since the 1980s, globalization of capital flows and the securitization of real estate debt have worked together to dramatically increase the volatility of real estate capitalization rates... Capital market forces can now easily overwhelm property market fundamentals... as a result, capital markets have become commercial real estate's best friend, or its worst enemy... Investors accepted lower yields from commercial real estate despite a sharp deterioration in market conditions and property earnings. As a result, cap rate compression (lower cap rates) completely overwhelmed the negative effects of falling property income (lower NOI) until late 2007... Credit markets seized almost overnight as the true risk was discovered to be much higher than imagined."

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SOUTHEAST TEXAS

Commercial real estate industry starting to recover, experts say

The Dallas Morning News

By Steve Brown / The Dallas Morning News / February 5, 2010

The CEO of one of the country's top commercial property firms says the industry is turning the corner, and a Texas real estate economist agrees.

"It's evident that the market has started some kind of recovery," John Santora, president of real estate service firm Cushman & Wakefield's Americas division, said Thursday. "Overall, the fundamentals either improved in the second half of 2009 or the deterioration began to slow."

"From a leasing perspective, the market came back in the second half of the year," Santora said at an economic forecast seminar his company sponsored Thursday morning in Dallas. While companies are taking advantage of lower real estate costs to do long-term deals, the outlook for commercial property owners is still troubled," he said.

"Many landlords are still facing liquidity issues, particularly owners who purchased properties at the peak of the market," Santora said. "Their

equity is gone. That will mean bargains for new buyers," he said.

"You are going to see some great opportunities to acquire assets in the next year and 24 months," Santora said. "And from everything I hear, there is enough money on the sidelines."

"Dallas' downtown area has double the office vacancy of most other major cities," he said, "but the rest of the commercial property sector is in much better shape."

"You are out-performing the broader market," Santora said. "We have something to feel a little positive about."

Mark Dotzour, chief economist for the Real Estate Center at Texas A&M University, told real estate executives that the commercial market should be in full recovery by next year.

"In 2012, if you are not in the market, you are going to be too late," said Dotzour, who predicts investors will snap up buildings.

"There are billions of dollars of dry powder sitting on the sidelines itching to go," he said. "You have people out there ready to fire all kinds of cannons at real estate."

"Banks holding back on property foreclosures are delaying the market comeback," he said.

"If the banks would put that property out on the market, you'd see a massive resurgence of transactions, and you'd see prices firm up," Dotzour said. "But the financial system is not solvent enough to let that happen."

He predicts that the commercial property sector will go through a period of little or no construction. "The bottom line is we are not going to build anything in this country for the next three years," Dotzour said.

But that may not help some owners who paid too much before the downturn. "If you bought anything in 2006 or 2007, you made a mistake."

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Texas Adds 50,000 Jobs in Fourth Quarter

from The Dallas Business Journal / February 8, 2010

Texas added 50,000 new jobs in the fourth quarter and activity in the new housing sector remains strong in both Dallas and Houston, according to a new study by SigmaBleyzer. The Lone Star State has one of the lowest unemployment rates in the nation. The positive quarterly job numbers come despite the state losing 24,000 jobs in the construction, trade, transportation and hospitality sectors in December. According to a recent Texas Workforce Commission report, Texas experienced employment increases in education, health care, mining and logging.

The study also focused on the broader economy of Texas, which remains under a downturn, but holds a positive outlook for the coming year. Among residential housing, some signs of recovery are beginning to emerge, according to the report. Texas has one of the fastest population growth rates in the country, which the report says should sustain long-term demand for housing. According to the U.S. Census Bureau, about 27 percent of all new privately-owned housing units in the nation's 20 largest cities were located in Dallas or Houston.

The state's export activity continues to recover as high oil prices and improving foreign demand for high-tech manufacturing increase.

Dallas Business Journal

Texas remains the largest exporter for the eighth consecutive year. In the first 11 months of 2009, Texas exports only fell by 18 percent, compared to the 21 percent decline nationally.

"This resilience of Texas exporters should help keep the state's economy on more sustainable footing as the U.S. economic recovery becomes increasingly dependent on the strength of foreign demand," the report by the Houston-based private equity firm stated.

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Got Mold? Southeast Texas Now Has A Solution

911Restoration™ is a Water Damage & Restoration Company serving local communities all around the United States and Canada. They provide water damage repair, sewage backup cleanup, mold inspection and removal, fire damage restoration and other clean-up services. Their services are aimed at providing customers with a safe environment and better air quality while often able to work directly with their customer's insurance company. **911Restoration™** provides services for both residential and commercial locations using the most eco-friendly materials and standards.

Though founded in 1978, **911Restoration™** operated as a small, struggling business until two friends, Idan Shpizear and Peleg Lindenberg, moved to the States from Israel and became a true "Coming to America" success story. While working together at a carpet cleaning business, they began to recognize the potential of the restoration industry. Working through language and custom barriers, they quickly discovered that they were unable to qualify for a loan. After much sweat equity and hardwork, they pooled their resources (a whopping \$3500 and a Volvo as an office) and formed the new **911Restoration™** in 1999.

Despite the declining economy, 911Restoration™ has grown into a multi-million dollar business. With over 20 offices across the USA and Canada - in cities like Houston, Dallas, San Francisco, Miami, Portland, and Toronto - the company has hired over 75 employees since 2009 and is expected to open 30 more offices by the close of 2010.

Success, however, has not changed a core value in the company's mission statement: Giving Back to the Community. **911Restoration™** has donated time, money, and resources to many charities while it has been in business.

Branch locations often work directly with their communities to meet the needs of local residents. In December 2009, the Van Nuys, CA branch donated 500 meals to the Union Rescue Mission in Los Angeles to feed the homeless for Christmas. The company was also part of the relief efforts in the New Orleans area after Hurricane Katrina and in Houston after Hurricane Ike, providing clean-up, mold removal and

restoration services for families in need. "We believe in giving back," CEO of 911 Restoration, Shay Kalmanovich said. "A little kindness goes a long way."



This month we highlight our Dallas and Houston offices. Mike McNatt is the General Manager for **911Restoration™** - DFW, in Dallas, TX. Mike holds a Masters Degree in Business Administration and Bachelor of Science in Business Management. He brings to **911Restoration™** a diverse background in sales and business development, including certification as a Project Management Professional and experience in business-to-business sales. Michael joined the 911 Restoration team in 2009, and is IICRC certified in water restoration. He can be contacted at (972) 607-3778 or toll free at (888) 243-6653.



Eli Elkayam, General Manager of **911Restoration™ - Houston**, spent five years as the Project Manager for **911Restoration™ - Los Angeles**. With an extensive background in the construction industry, Eli thrived at the Los Angeles office. He quickly became an expert in mold and water damage - earning certificates in both - and adding to his general contractor and HVAC experience. Three years ago he was asked to open **911Restoration™ - Houston** and was relocated to the area. Eli and his team have had great success in Houston, and have worked hard to build relationships with their clients and insurance companies. Eli can be reached at (281) 770-7982 or toll free at (888) 243-6653.

Both Mike and Eli look forward to helping you with all your restoration needs.



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