

JCR Capital Market Update August, 2008

Dear Friends & Colleagues,

I have recently attended two distressed real estate conferences and I thought I would share “the buzz” with you.

In both cases, the conferences were primarily focused on those who were looking for distressed debt, or wanted to learn about it. There were no sellers to be found. Here is a summary:

For Sale Assets

- The residential markets are in free fall and have a long way to go. Oversupply is the theme.
- The combination of “outlying lots” and \$4.00 gas is further deteriorating the value of suburban residential land.
- Not many trades are occurring in land, as lenders are holding on.

Commercial Assets

- Fixed rate loans coming due in 2008 and 2009 will need to find a home. A refinance most likely will work, but sponsors will not be happy with proceeds or rates on new loans.
- Short term floating rate, value added loans that were securitized, that are now coming due are the “poster child” for problems. The combination of aggressive NOI growth assumptions and over-leverage will make these projects ineligible for refinancing. The question will be at what level can they be sold?
 - ✓ A price that repays the debt
 - ✓ A price that repays the debt and the equity

Bid/Ask Gap

- It’s still there and does not look like it’s going away any time soon. If regional and community banks take the write downs needed to “close the gap,” this could result in massive bank failures. The FDIC does not appear to be pushing these banks and many are hanging on.
- This situation will create “White Knight” opportunities with banks and sponsors (**a JCR Capital specialty**).

Commercial Assets: Early in the Game

- The consensus was that we are in the 2nd to 3rd inning for distressed commercial assets. The view is that commercial asset values will be slow to reset. It could be 2010 or 2011 as sellers hold on, expect a “slow grind” in value deterioration, that could be up to 10-20% depending on the market and asset class.

Dusting off the Workout Manual

The industry is getting re-acquainted with the following terms (again):

- Pre-negotiation letter
- Forbearance agreement
- Deed in lieu of foreclosure
- Release of guarantee
- Cash for keys
- Bankruptcy threats
- Judicial foreclosure
- Non-judicial foreclosure
- Redemption periods
- Reps and warranties

The Future

- Expect Wall Street regulation, and less structured products in the short term.
- The return to securitization will be slow and initially will only be for stabilized properties. Look for the following terms to be commonplace:
 - ✓ Higher spreads than in the past
 - ✓ 70-75% LTV
 - ✓ 25-30 year amortization
 - ✓ 1.25x debt service coverage on existing trailing 12 NOI
 - ✓ More underwriting on the sponsor
 - ✓ More underwriting on the market
 - ✓ More underwriting on the physical asset
 - ✓ More underwriting of the tenant rent roll
- Banks will be impaired and have longer memories – they will not be aggressive real estate underwriters.
- Look for more private capital to emerge to fill the void and expect high financing costs, which will be another factor in the decline of commercial real estate values.

Where to Turn: JCR Capital

JCR Capital is financing real estate transactions.

- Bridge loans: Income producing properties
- Hard money loans: Non-income producing properties
- Special situations: Equity, loan restructures
- Flexibility, creativity and speed
- **Fore more information, see <http://www.jcrcapital.com>**

All the Best,

Jay Rollins