

Office outlook cloudy as foreclosures, loan workouts loom

By YUDISLAIDY FERNANDEZ

It's hard to forecast the future of office properties in the local commercial market, office analysts say, but more loan modifications and foreclosures are on the horizon as lenders make decisions on distressed assets on their books.

Jonathan Kingsley, managing director and executive vice president of commercial realty advisory firm Grubb & Ellis, says the volume of foreclosures is expected to increase as well as the number of commercial loan workouts.

A trend Mr. Kingsley says he is starting to see is that lenders are more likely to do workouts to help borrowers who they are confident can ride the economic storm, while those borrowers under water are likely to lose their properties as the banks prefer to foreclose and find a new buyer.

When determining value, he says those properties with a market value 50% or less than the purchase price "pretty much have no chance of recovery." But if the current value is only 20% to 30% less than the original price tag, Mr. Kingsley explained, there's a greater chance of recovery.

Grubb & Ellis reports in its 2010 real estate forecast released Monday that as lenders who delayed working through distressed assets start putting them on the market this year, sales volume is expected to rise by 20% to 30% from 2009.



Photo courtesy of Scott Minchew

'It's definitely a good time to be a buyer and tenant,' says Scott Minchew, president of commercial realty firm Scott Minchew & Co.

Prices, already 40% down from their peak in 2007, could decline another 10% to 20% as these properties are sold at lower prices to meet buyers' expectations, according to the report.

As a result of more commercial property sales, the investment market will begin to see a recovery, the report forecasts, indicating that high-leveraged buildings without the needed capital to attract new tenants are likely to reach new hands.

As sales volume increases this year because of sales of distressed assets moving through the foreclosure process, the discounted sale prices of many of these properties are to push the cap rate

on all major property types above 8%, the forecast indicates.

Timing is another factor that will determine what sells and when it sells.

Some lenders disposing of assets aren't willing to sell at deep discounts, said Mr. Kingsley of Grubb & Ellis. Often the banks prefer to keep the properties in service and manage them effectively until the best offer comes along.

The process can be time consuming, he says.

"Nobody wants to make that decision early on. They [lenders] want to do their best to bring the property to the best value," he said.

Scott Minchew, president of Miami-based commercial realty firm Scott Minchew & Co., says those commercial properties that hit the market will definitely have an audience as right now an array of buyers is waiting. Institutional investors and foreign nationals will make up the pool of buyers, he says, which could range from those willing to pay market values to bottom feeders.

"It's definitely a good time to be a buyer and tenant and a tough time to be a seller and landlord," Mr. Minchew said.

Every deal is going to be different, he added, because it depends on factors like how aggressive some buyers are and the position the bank is in.

"Everybody has their own parameters they have to meet," he says. "Every deal is going to be somewhat different..."

Banks that can hold off on selling certain properties will wait for the right deal, he says, "but those who can't will have to cut their losses and run."

Alex Zylberglait, vice president of investments and director at commercial realty firm Marcus & Millichap, agrees the future of many office assets will be determined on a case-by-case basis.

Some lenders are going to agree to loan workouts, such as restructuring the debt, extensions, forbearance, or new terms on the debt, he said.

But in instances in which a borrower with a particular commercial property in trouble has other well-performing assets, Mr. Zylberglait said, the bank might ask for additional capital. In cases in which the bank sees the borrower is in distress and unable to pay the debt, he said, the bank will take the property back to regain control of its future.

Deep-pocketed investors are definitely out there, Mr. Zylberglait says. The problem is not the money but the deal.

With the uncertainty in the commercial market, some investors may not want to buy at higher prices without knowing if the investment will have a high return down the line.

If overleveraged properties do start selling at deep discounts, Mr. Zylberglait says, it's going to impact the local office market, already experiencing higher vacancies and lower rental rates packed with



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concessions.

If the wave of distressed commercial assets is as some anticipate, Scott Coloney, president of Fort Lauderdale-based Foreclosure Response Team, says short sales could become a popular option as they did in 2009 for the housing market.

Mr. Coloney says his loss mitigation team and real estate professionals negotiate with the lender to sell the property at the best price the borrower and lender can reach.

He foresees more opportunities in the commercial market on the horizon as commercial property owners unable to raise more capital to restructure their debt in today's market find themselves facing foreclosure.

The buyers are waiting on the sidelines, Mr. Coloney says.

Although the buyer pool in the US has shrunk, he says, many international investors, such as Canadians, are looking for commercial properties priced right to snatch.

"We are doing a lot with the Internet to reach those international buyers..."