

An Attitude Adjustment

Sellers—not all distressed!—wrap their heads around a return to dealmaking

On the first Monday in January, one segment of the real estate world began to return to normal. The phones started ringing again. For all of 2009, may it rest in peace, the real estate transaction market was almost totally dysfunctional. Owners and developers with cash couldn't put it to work; first mortgage lenders couldn't deploy their allocations; and investment funds chose to let huge sums of committed capital remain idle. The most frequent topic of conversation was the total lack of interesting deals that virtually anyone was seeing. Yes, there were a few very high-profile large sales in New York—mostly flowing out of the Macklowe defaults—but the massive size of those deals limited the potential buyers to a very select few.

Since that Monday morning, however, the conversation has shifted. Many developers, owners and entrepreneurs who have been tracking and pursuing deals for months now seem to have a greater sense that these deals will likely get consummated in the near term. This optimism is due unquestionably to a change in the attitude of sellers—

not all of whom are distressed.

Sellers fall into a few classes. Most interesting are the opportunistic investors who bought smartly in the early part of the downturn, worked their investments in ways like foreclosing/wiping out/restructuring the junior debt or equity partners, or negotiating deed-in-lieu transactions with the original developer/borrower, and who now have the ability to sell a consolidated capital stack at a price that is not only profitable for the seller but also low enough to allow true value creation by a new developer who is willing to take on the risk of completing the project.

With big money flowing so freely from 2003 to 2007, many operators got in over their heads, buying substantially larger or more complicated properties than they had dealt with previously. Those with short-term debt are already mired in problems they may not survive, but many others have long-term debt that is

locked in at very low interest rates and with no amortization, allowing them to stay out of current distress/default so far. However, this latter group is going to need to accomplish major income appreciation at their properties to avoid maturity defaults when the debts finally come due (possibly in a higher-interest-rate, higher-cap-rate environment). Recognition of their difficult position in this uphill battle has set in among some in this situation, and they are reaching out to more es-



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tablished/experienced/liquid operators and seeking to form joint ventures.

Flight (and non-flight) capital from around the world is seeking entry into high-end Manhattan properties, and is willing to accept yields that are low enough to make even multi-generational family owners consider the possibility of selling or at least partially recapitalizing some of their high-profile assets, although it is likely that most of these transactions will

be accomplished very quietly.

For those owner/developers finding purchase opportunities that are attractive based on today's market fundamentals, or any owners holding cash-flowing properties with low to moderate existing leverage, low-rate financing abounds. Despite the common and frequently stated conviction that there is a dearth of mortgage money available today, the real state of the finance world is exactly the opposite—and has been since early 2009. A multitude of lenders remain eager to originate fixed-rate loans, and virtually all of them missed their target allocations last year.

There has been a tendency in the real estate media to blame the 2009 transaction drought on a short, or nonexistent, supply of mortgage money, but the truth is that what really occurred was an almost total lack of demand. While this was understandable with regard to acquisitions (given sellers' unrealistic asking prices), it was very surprising with regard to existing loan maturities and refinancings. Only a tiny portion of the existing stock of commercial mortgage loans carries an initial term of greater than

10 years, and many are written for five years or less. Assuming an average term of five to seven years, one would assume that 15 to 20 percent of all commercial loans would mature in any given year, and that 25 to 35 percent of all loans would have an impending maturity date within less than two years.

Clearly nowhere near that amount of property was financed or refinanced in the past 15 months, leaving a backlog of both healthy and unhealthy loan maturities on the horizon. With the demise of many of the previously more aggressive lenders, many borrowers are likely to find that their former "go-to" lenders are no longer viable sources.

Demand for money is now coming from many competing directions, and it appears that 2010 will finally bring the opportunity for investors and lenders to step up to the plate.

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Living-Wage Coalition? More Like No-Jobs Coalition!

The employment costs of nixing Related's Kingsbridge Armory project

The defeat of the Kingsbridge Armory project in the Bronx, by a coalition led by Stuart Applebaum of the Retail, Wholesale, and Department Store Union and Bronx Borough President Ruben Diaz Jr., was a harmful decision for the city coffers, for Bronx residents and for out-of-work New Yorkers.

Here are some of the lost economic benefits as a result of this coalition's position, which said no to the creation of real jobs.

In the midst of the worst economic recession in 70 years, we lost approximately 1,200 permanent jobs, many at higher salaries than the "No-Jobs Coalition" claimed; the estimated \$20 million in tax revenue could pay the salaries of 50 police officers, 50 firemen and 100 teachers—good-paying jobs that serve all New Yorkers.

As the city struggles to pay for affordable housing, social services, libraries, senior centers and other services for the most vulnerable

New Yorkers, we lost the hundreds of millions of dollars in economic activity that the substantial renovation of this long vacant landmark facility would generate, and more than 1,000 high-paying construction jobs at a time when job losses in this industry are mounting.

In opposing a major retail mall project, this No-Jobs Coalition said no to the prevailing-wage building-service jobs that would operate and maintain the complex, and no to more than \$300 million in direct capital investment in this underutilized iconic Bronx building.

In the borough with the highest unemployment rate, we lost the additional 2,200 other well-paying jobs that would be created to support the retail activity at the Armory.

Without this major economic development project, we lost jobs driving the trucks that would deliver building material during construction, and goods and products daily to the new

mall; we lost the administrative jobs these retail tenants would need; and we lost the opportunity for these new workers to get a raise in pay or a job promotion, an opportunity unavailable if you don't have a job.

Furthermore, focusing solely on mandating higher wages for these potential new jobs, the No-Jobs Coalition dismissed the voice of the local community board that voted to approve the development and that represents the residents of the area; it ignored the developer's argument that the mandated higher wage requirement would make it more difficult to attract cost-sensitive tenants to the Armory when competing against locations without this wage requirement, and would make an economically difficult project financially unfeasible.

All these benefits were sacrificed and all these reasons dismissed by the No-Jobs Coalition, whose sole purpose was to achieve their political demands of mandated higher wages for retail workers.

Unfortunately, the Kingsbridge Armory project is not the first project in which such demands have been made. It has been reasonable and

customary, as part of their land-use approval, for projects to mitigate impacts that they create. For instance, if a new project creates traffic congestion, it can be expected to fund roadway improvements that solve this problem. But more recently, projects are being asked not only to solve the problems they create but to offer enhanced economic benefits as a condition for approval.

In this political climate, project sponsors have deemed it necessary for approval to enter into agreements with similar coalitions, agreements that often include provisions for providing community benefits, such as job-training programs and neighborhood-based hiring quotas, that are unrelated to the project's potential impacts.

The No-Jobs Coalition's demand that the Kingsbridge Armory developer, Related Companies, require the retail mall's tenants to pay higher wages is another form of benefit agreement that is unrelated to any potential project impact. At great financial cost, Related refused to accept the coalition's unreasonable and self-serving demand and fought back against this dangerous trend.

The City Bar Association and others have questioned the appropriateness and legality of these benefit and side agreements, especially as the demands have escalated and no longer have any relationship to a project's impact. We are no longer asking whether the proposed land-use action would be compatible with the surrounding uses, would revitalize the neighborhood and would benefit the city—the reasons for City Council review. The only question, posed by these coalitions, is whether the project satisfies the special interest's demands. The planning and land-use process is being hijacked by these myopic coalitions, which want to advance their goals at any price.

We hope the public outcry over the rejection of the Kingsbridge Armory project will bring an end to both the misuse of the planning and land-use process and to the imposition of unreasonable demands, such as community benefits or mandated wage requirements, by self-serving special-interest coalitions.

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The Op-Ed