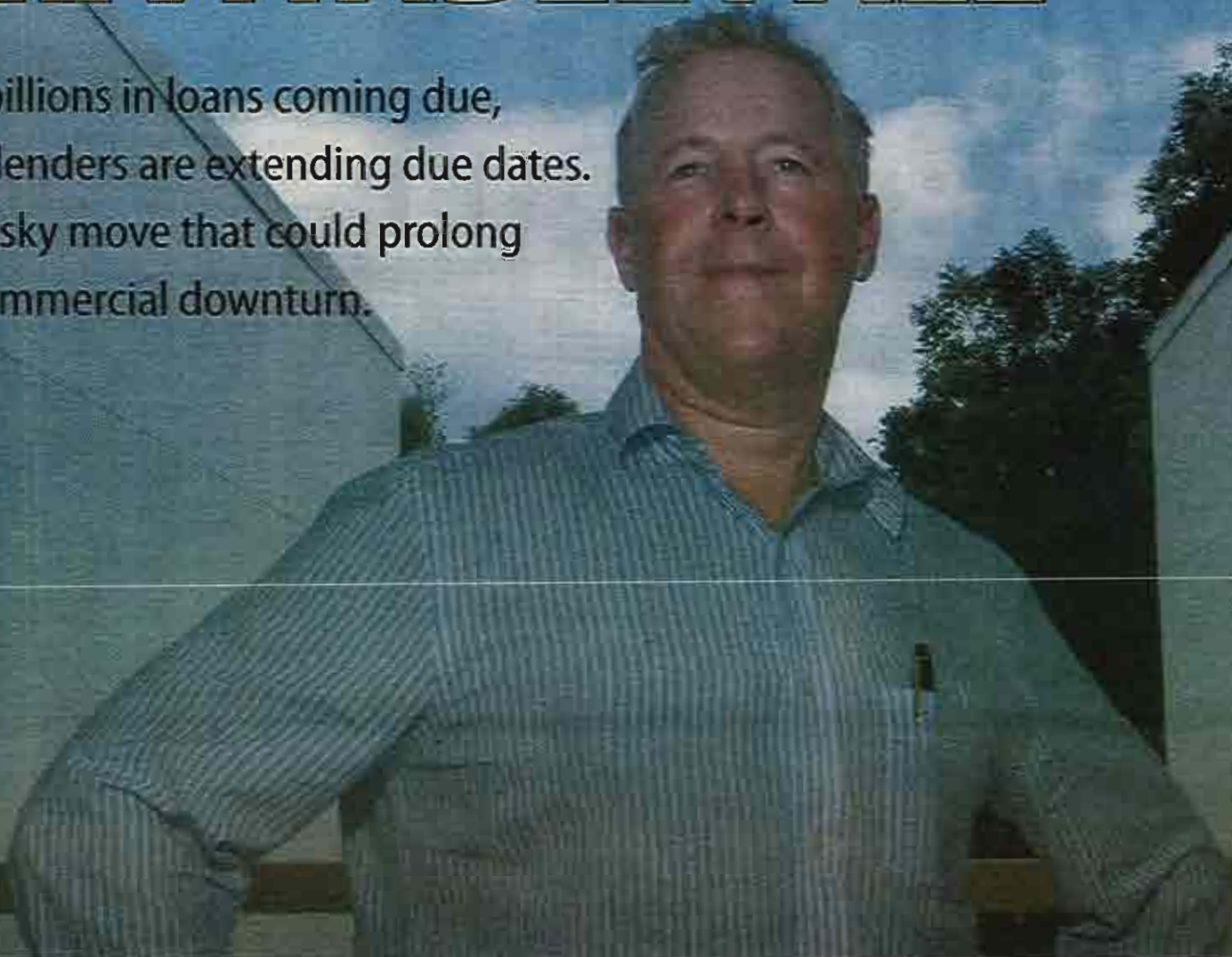


SPECIAL REPORT: Commercial Real Estate Annual Report

DELAYING THE INEVITABLE FALL

With billions in loans coming due, some lenders are extending due dates. It's a risky move that could prolong the commercial downturn.



MELANIE BELL

Tom Godart of PMA Sales Group says lenders are stalling so they can avoid having to foreclose or write off the value of a bad loan or asset.

by Polyana da Costa
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The commercial real estate market is a ticking bomb waiting to go off.

It's a bubble ready to burst. It's a ... well, pick a cliché. No matter how they say it, industry experts have been making catastrophic predictions about

the commercial market for months now.

But why hasn't the market collapsed yet? Loans on commercial properties continue to come due and many borrowers have repeatedly reported they can't refinance their debt. You would expect that by now the market would be flooded with foreclosures.

But it's not.

There are about \$9.4 billion worth of distressed commercial loans in South Florida and only

about 13 percent of that, or \$1.3 billion worth, has been taken back by lenders, according to Real Capital Analytics.

The reason is that commercial banks have been flexible — too flexible, some critics say — in extending maturity dates and giving borrowers forbearance as loans come due.

Some extensions are as short as three to six months; others allow borrowers up to two years to repay the debt. The most common is a year extension with an additional six months extension once that expires.

The strategy allows lenders to avoid having to seize properties that have lost value and then write off their losses.

But critics say this simply puts off the problem because the credit and commercial real estate markets, especially retail and office sectors, will not have recovered by the time these loans again come due.

It could take a generation for

SEE COMING DUE, PAGE AA4



A.M. HOLT

ontheweb
Video report with the Daily Business Review's Polyana da Costa on DailyBusinessReview.com

Hines received a one-year extension on a \$91 million loan on the 45-acre Airport Corporate Center that matured in March. In 2010 Hines has the option to extend the payoff another six months, and a company spokesman said by then the company is confident it will be able to refinance.

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FROM PAGE AA2

COMING DUE: Borrowers hope to refinance when credit improves

the commercial real estate market to return to the kind of deals seen during the boom years of 2005 to 2007, according to a recent report by Jones Lang LaSalle.

"I think many lenders are delaying the inevitable," said Tom Godart, a broker-associate at Boca Raton-based PMA Sales Group. "They are stalling."

Godart represents user-buyers who want to acquire discounted properties and mortgage notes backed by commercial properties from banks.

He said lenders are doing whatever is necessary to avoid having to foreclose or to write off the value of a bad loan or asset, including converting loans in default into interest-free loans for a buyer willing to assume the full debt.

Some lenders also are waiting months, sometimes even a year, to file a foreclosure after a loan goes into default.

"If they admit to the real value of those assets, the FDIC would be looking at them as insolvent," Godart said.

Troubles at Capmark Financial Group, which posted a \$1.6 billion quarterly loss on Sept. 2 and said it might go bankrupt, are an alarming sign for many local and

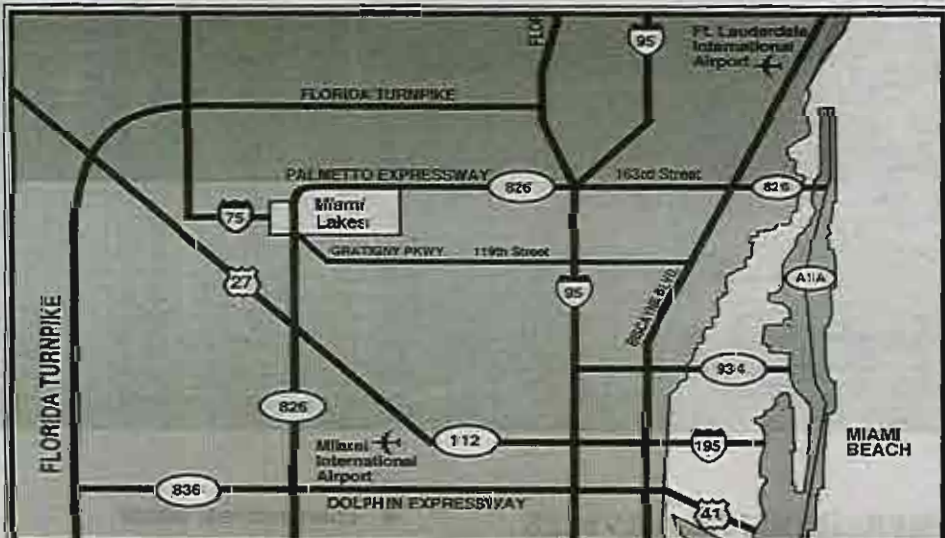
national lenders who realize that big losses in the real estate market will be inevitable.

U.S. banks hold about half of the more than \$3.5 trillion of loans that are backed by commercial properties. The commercial mortgage-backed securities (CMBS) market holds another 25 percent, and insurance companies and government sponsored agencies such as Fannie Mae and Freddie Mac account for the rest. Nearly \$1 trillion in commercial loans are to mature by the end of 2010, analysts estimate.

"It's a snowball," said real estate attorney Dale Bergman, a partner in Arnstein & Lehr in Fort Lauderdale. "Loans are coming due, we still have a tight credit market, vacancy rates are increasing, many borrowers no longer have the cash flow to support the financing and borrowers [who bought in the peak] are extremely under water."

Bergman said he represents a potential buyer of a Miami office building with \$30 million-plus loan that is in default.

The lender, who Bergman would not identify, waited a year after the loan went



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Catalfumo Co. let a \$30 million loan on the retail property at 3801 Design Center Drive go into default in order to negotiate with the lender. But the lender foreclosed, and Catalfumo attorney Jim Jacoby said negotiations are continuing.



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into default to file a foreclosure action. Last year, he said, the bank wasn't even willing to talk about selling the note at discount. This year, the bank said it would sell the loan for about \$12 million to \$14 million, but buyers now say the property now may not even be worth that.

"There is going to be a lot of pressure on these banks," Bergman said.

And as much as lenders try to avoid recognizing their losses the will reach at dead end at some point.

Take Las Olas Centre in Fort Lauderdale, for example. Wachovia Bank extended the maturity date several times on the approximately \$219 million in loans on that property. The lender filed a foreclosure lawsuit in Broward Circuit Court in August after BF Las Olas — a subsidiary of BentleyForbes, a Los Angeles-based commercial real estate investment company — was unable to repay the loan. According to the Broward County property appraiser, the taxable value of the two buildings is \$153.89 million, much less than the debt on it.

with Bank of America acting as trustee.

Hines received a one-year extension to pay off the loan. After March 2010 Hines has the option to extend the payoff another six months, according to county records.

Michael Harrison, senior vice president for Hines Southeast Region, said he is confident the company will be able to refinance by then.

"We are already starting to see some signs of improvement [in the credit market], and we continue to explore our longer-term options," he said.

Harrison said the property is 93 percent leased and is not overleveraged.

Before they agree to refinancing or loan extensions, lenders are requiring many borrowers to invest more money in properties to cover the difference between what is owed

TROUBLED LOANS BY SECTOR

	Distressed loans	Foreclosed Assets
Hotel	\$1.2 billion	\$38 million
Retail	\$1 billion	\$166 million
Office	\$829 million	\$8.7 million
Industrial	\$134 million	\$37.1 million
Multifamily	\$3.1 billion	\$1 billion
Development	\$1.84 billion	\$12.5 million
Development site	\$1 billion	\$102 million

Source: Real Capital Analytics

SEE COMING DUE, PAGE AA6



"Loans are coming due, we still have a tight credit market, vacancy rates are increasing, many borrowers no longer have the cash flow to support the financing and borrowers [who bought in the peak] are extremely underwater."

DALE BERGMAN
ARNSTEIN & LEHR

HOTEL, RETAIL WOES

In South Florida, hotel and retail properties are the two areas of biggest concern in the commercial sector.

Amid the decline in tourism there is \$1.2 billion worth of distressed hotel loans in South Florida, according to Real Capital.

The recession, job losses and slow sales have contributed to about \$1 billion in distressed loans backed by retail properties and about \$829 million troubled loans backed by office properties.

Many of these borrowers, ranging from owners of small properties to investors in major commercial complexes, think that if they are given extensions to try to weather the recession, they will be able to refinance in a year or so.

Hines, the giant real estate investment trust, is one of the many companies that shares that belief.

Hines bought the 45-acre Airport Corporate Center in 2006, at the peak of the market, for about \$157 million, but commercial real estate values have tanked since then.

Earlier this year, Hines received an extension on a \$91 million loan that matured in March. The loan is part of a CMBS package

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FROM PAGE AA5

COMING DUE: Some borrowers forced to default to negotiate

and what the property is now worth. Harrison would not disclose if Hines had to provide additional cash to the lender.

CATALFUMO LOAN

When it comes to CMBS loans, not all borrowers may be able to obtain extensions or concessions.

Palm Beach Gardens-based Catalfumo Co. has been trying for months to renegotiate a \$30 million CMBS loan that is backed by a 145,000-square-foot retail center in Palm Beach Gardens.

Jim Jacoby, Catalfumo's attorney, said the center's tenants, three furniture stores, have been hurt by slow sales and have asked Catalfumo to reduce the rent by about 20 percent. Jacoby wouldn't disclose the rents but said the loan agreement does not allow reductions without the lender's approval.

He was told that only "special servicers," the representatives that negotiate with borrowers in default, could approve lower rents.

Jacoby said Catalfumo had to stop paying the mortgage and fall into default in order to be able to negotiate.

In July, 90 days after Catalfumo defaulted, Bank of America, acting as trustee, filed to foreclose.

"We are still working on it," Jacoby

said. "The special servicers have their hands full. They have a lot of these. It's not like you can walk into your neighborhood bank and talk to someone about your loan. That would be much easier."

Being forced into default in order to be able to negotiate with CMBS servicers has become common. But new rules adopted by the U.S. Treasury Department this month are expected to encourage CBMS servicers to negotiate loans prior to default, said Jim Shindell, a partner with Bilzin Sumberg Baena Price & Axelrod.

The Treasury Department said Sept. 16 that it would allow CMBS lenders to refinance some loans without paying tax penalties.

"One of the things servicers were concerned about is that their tax status could be challenged by the IRS [if a loan was modified prior to default]," Shindell said. "It's too early to tell what will be the impact of the new regulations but it's definitely a step in the right direction."

Jacoby said Catalfumo has been successful in renegotiating loan terms with banks on its other projects and properties.

Howard Taft of the Aztec Group, a Miami-based real estate investment banking firm, agrees CMBS lenders have been more aggressive in pursu-



A.M. HOLT

Attorney Steve Silverman, who represents owners of distressed properties trying to work out loans, expects more loan modifications in the commercial sector because "banks are not set up to take property back."



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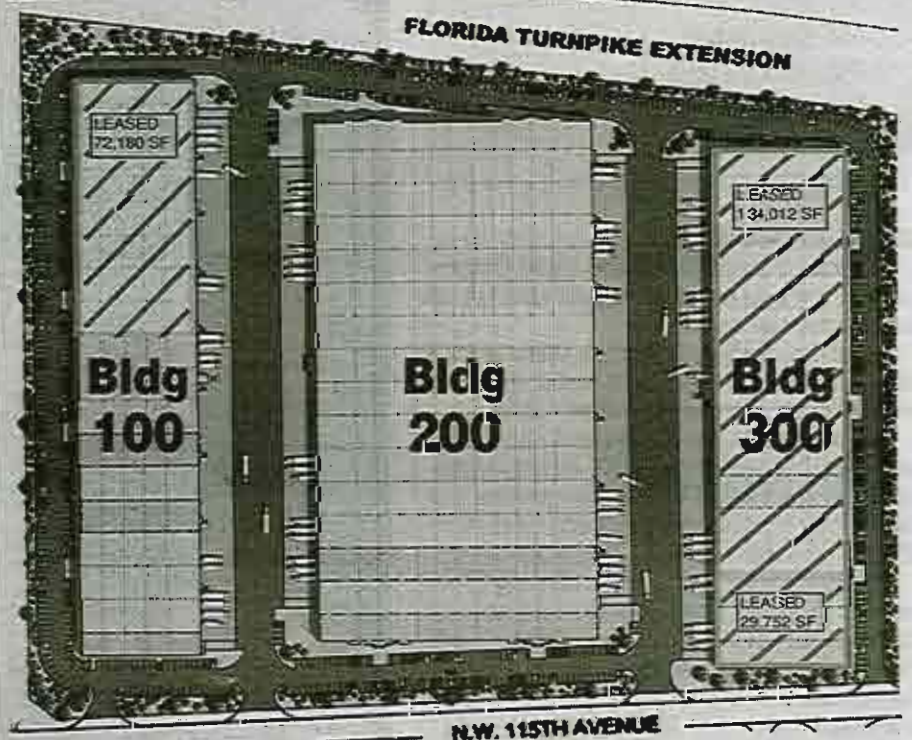
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ing foreclosures and less lenient with borrowers. Taft said he was working on a deal involving a retail center and an apartment complex in Miami with CMBS financing. The lenders decided to file foreclosure, take back the properties and manage them until they can sell in three or five years.

Banks, he said, have an option to delay — a strategy that he does not criticize.

"I don't think we need to have all these commercial properties in foreclosure," he said. "Extending is the best thing now until we get out of this phase in the economy."

Taft recognizes that banks are "kicking the can down the street a little bit" when they extend loans on properties that are often under water and have high vacancies.

Still, a lender that takes over a commercial property now risks a substantial loss if it sells in the current distressed market, Taft said. Lenders that do end up foreclosing on the properties will have to hire management companies to lease the property and manage it for a couple of years until they are able to sell it.

"So, why not let the owner keep the property and manage it?" he asked.

But critics of this tactic say the risk is a prolonging of the commercial real estate market downturn.

CUT OUT THE CANCER

Gustaf Arnoldsson, managing member of Stonemason Partners in Miami Beach, which manages several bank-owned properties, said lenders have told him they are avoiding taking back the assets even if the property owner isn't paying the mortgage because they don't want to have to manage it. Arnoldsson said that is simply adding to the problem.

"Instead of letting the cancer spread, they should just amputate the leg and move on," Arnoldsson said.

"They think it's better to force the owner to manage the property even when he is not paying, but the owner knows he will lose the property so he is poorly managing it and the asset becomes more distressed and loses more value."

Banks used this delaying tactic with residential assets for the nearly three years after the residential market started to decline. Only recently have they begun to accept the losses and sell the bad loans and troubled assets at deep discounts, said Steve Silverman, a lawyer who represents owners of distressed properties trying to workout loans with lenders.

"We've seen that in residential, and we are going to see that with the commercial sector," said Silverman, a partner with Kluger Kaplan Silverman Katzen & Levine. "Banks are not set up to take property back. The one way to avoid that is to provide forbearance agreements or provide a modification, which can take all sorts of different forms."

Godart said it could be a year before banks see the enormity of the problem and are forced to take over commercial assets and sell at a loss.

He said the problem will get worse before it improves. Godart expects another wave of retail property owners to default on loans — even those who are fully leased and now have enough cash flow.

"Forget about the rents tenants are paying today," he said. "As soon as their lease is up, or even before, they are going to ask for much lower rents or they will move somewhere else because the center next door is half vacant and the owner is willing to lease space for less. The values of those retail centers will tank."

As with the residential market, banks will be forced to take over the assets and try to sell, he said. And again mirroring the residential market, lenders will try to get the most value

for their properties and vulture buyers and investors will hunt for bargains as they try to acquire distressed commercial properties.

Companies and investors have already started several acquisition funds in preparation for the discounted commercial property purchases, including Hines.

Arnoldsson said his company recently formed a fund that is planning to acquire \$100 million in commercial real estate when distressed owners decide to accept the losses and sell.

When will that happen? Arnoldsson predicts the day will come when banks will employ more special asset managers than lending officers.

"Then they will take the losses," he said.

Polyana da Costa can be reached at (561) 820-2065.

TROUBLED COMMERCIAL LOANS

	Total value of distressed loans	Total value of lender owned real estate
Miami-Dade	\$5.8 billion	\$746 million
Broward	\$1.8 billion	\$250 million
Palm Beach	\$1.84 billion	\$420 million
South Florida	\$9.4 billion	\$1.3 billion

Source: Real Capital Analytics



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