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# Lack of market 'normalcy' makes valuation of space difficult

BY MARILYN BOWDEN

With very few sales of any class of commercial real estate consummated this year, brokers say it's tough to get a fix on current values.

"The reality of the market is nobody knows where values are at this point," said Jay Caplin, managing principal at Steelbridge Capital. "There aren't any deal metrics to serve as benchmarks because the market has been so devoid of transactions."

But certain areas will probably fare better than others, he said.

"In the short term, downtown and Brickell are a little grim, with all the new office space coming on line. Then the question becomes, what happens to the surrounding markets that compete with them? How are they impacted if downtown has a plethora of space and rates comes down?"

Commercial property values relate directly to occupancy levels, said Edgar Jones, regional development officer in Florida for The Rockefeller Group Development Corp.

"The bottom line is net operating incomes and rental," he said. "We're seeing deals being re-written, early negotiations on leases with some space givebacks involved, and rental rate reductions, and that's clearly impacted value."

Office vacancies are significantly up in Coral Gables, said Steve Nostrand, an executive vice president at Colliers Abood Wood-Fay. "Downtown Miami has got a lot of C and B product on the market," he said. "Aventura is interesting in that it's still a little bit difficult to find space."

For retail, "there's still more damage to come," he said. "There are pockets of our county, such as Kendall, where things are better than the overall statistics might indicate. But in general, tenants are leaving and lease rates are depressed.

"Multifamily is the market that is going to suffer the most, mostly because of fractured condos. Apartment buildings that sold for six caps two years ago are selling for nine and 10 today; office buildings that sold for six caps would be nine now. So there has been a huge swing in the market, and no one can put a finger on when we will come back to any sense of normalcy."

The cap he refers to is the capitalization rate of the investment, determined by dividing net operating income by cost. A "six cap" would be a 6% capitalization rate, a "nine cap" 9%.

There's a huge number of investors with cash in the marketplace, Mr. Nostrand said, but also still an enormous disconnect between the bid and the ask.

Photo by Marlene Quaroni

**Nobody knows where values are right now because there have been so few transactions, says principal Jay Caplin of Steelbridge Capital.**

"The perception is if you take a property to market today it is under distress," he said, "and offers will be 15%-30% below what you as a seller might have expected in a normal market.

"Buyers are looking for deep discounts for two reasons – uncertainty about the future and the difficulty of getting financing. So they go the ultra-conservative route and build in some risk avoidance."

There's been a significant increase in foreclosure filings for all types of commercial real estate over the past 60 days, Mr. Nostrand said.

"In Florida we have an unfair, burdensome foreclosure process. An uncontested foreclosure could take eight to 10 months – and then you have to file again to sell the property on the courthouse steps. So it could be 14 to 15 months before there's any kind of resolution.

"We anticipate banks will therefore want to sell those notes, and there may be a market bubbling up for them, but it's much riskier to buy the note than the property itself."

Perhaps most ominous is the huge quantity of commercial mortgage-backed securities maturing over the next five years, said Jack Lowell, managing director at Flagler Realty Group – $715 billion, according to the National Real Estate Investor, with a peak in 2012 of more than $200 billion.

Mr. Caplin said he's heard estimates of $160 billion coming due in 2010, "and there is not nearly enough capital to replace it. I think everybody is a little surprised at the severity and depth of the issue."

Most buildings in Coral Gables, downtown and Brickell are in institutional hands, Mr. Lowell said, and these strong investment groups will be able to maintain ownership. Owners with mortgages coming due have two choices – to try to refinance and pay down the mortgage or to sell the property.

"Over the next few years we will see a lot come to market," he said, "and cap rates will continue to go up as financing is still difficult."

"We're beginning to see some of these properties changing hands, via either mortgage buys or asset purchases," Mr. Jones said. "It's beginning to smell a lot like the Resolution Trust Corp. (RTC) days of the 1980s. Unless we come up with a better plan, it could easily deteriorate further."

The federal government is expanding programs for issuing commercial mortgage-backed securities paper, Mr. Lowell said, "But it remains to be seen whether the marketplace will accept it. Right now, that paper is not trading, so the jury is still out."