
Wall Street and Commercial Real Estate

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Appraisal Institute – Market Trends

Goals of Presentation

- Market Drivers
- Real Estate Capital Markets
- Real Estate Market Performance
- Conclusions & Forecast

Note: PPT Deck will be posted to www.GreerAdvisors.com

Most information is updated via Newsletter, sign up on web site.

■ Market Drivers

Supply / Demand vs. Financing

Supply / Demand – Impacts Rent & Vacancy less on Value

- Most Demand ties to Jobs – Drives Vacancy (1), Rents (2)
 - Office – FIRE Employment, Portion of Service Employment
 - Retail – Household (HH) Formations, Income Growth
 - Industrial – Manufacturing & Distribution (Logistics)
 - Multifamily – HH Formations, non-Top 25% of HH Income
 - Hotel – Corporate Travel – Office & Industrial Employment

Financing **DRIVES VALUE!** Low Interest = High Value

- Availability
- Rate and Term
- Leverage
- Recourse

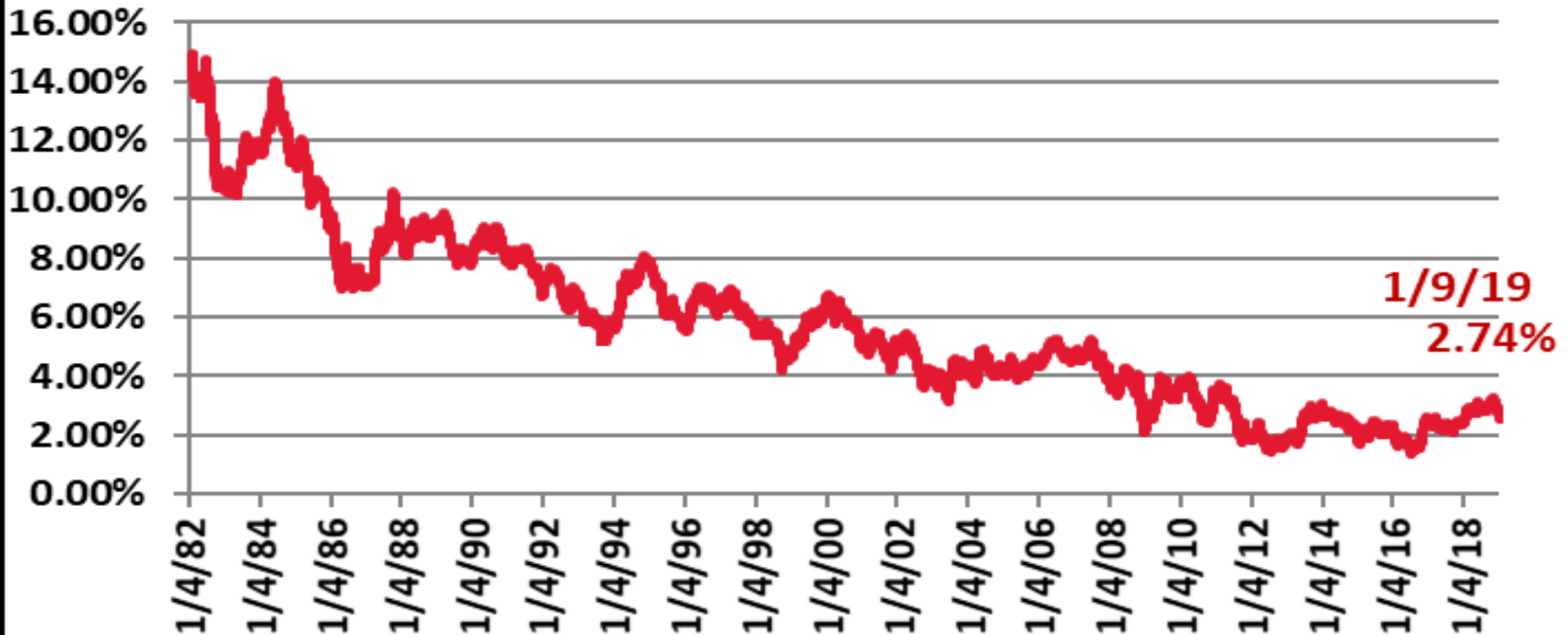
** This is mostly due to the drop in interest rates for CRE loans since the advent of CMBS.

Currency wars / restrictions, trade wars, FRB Rate Hikes, Global Turmoil, e.g. U.S. v China, Global perception of America

- International Investment **

Interest Rates – Long Term View 1982+

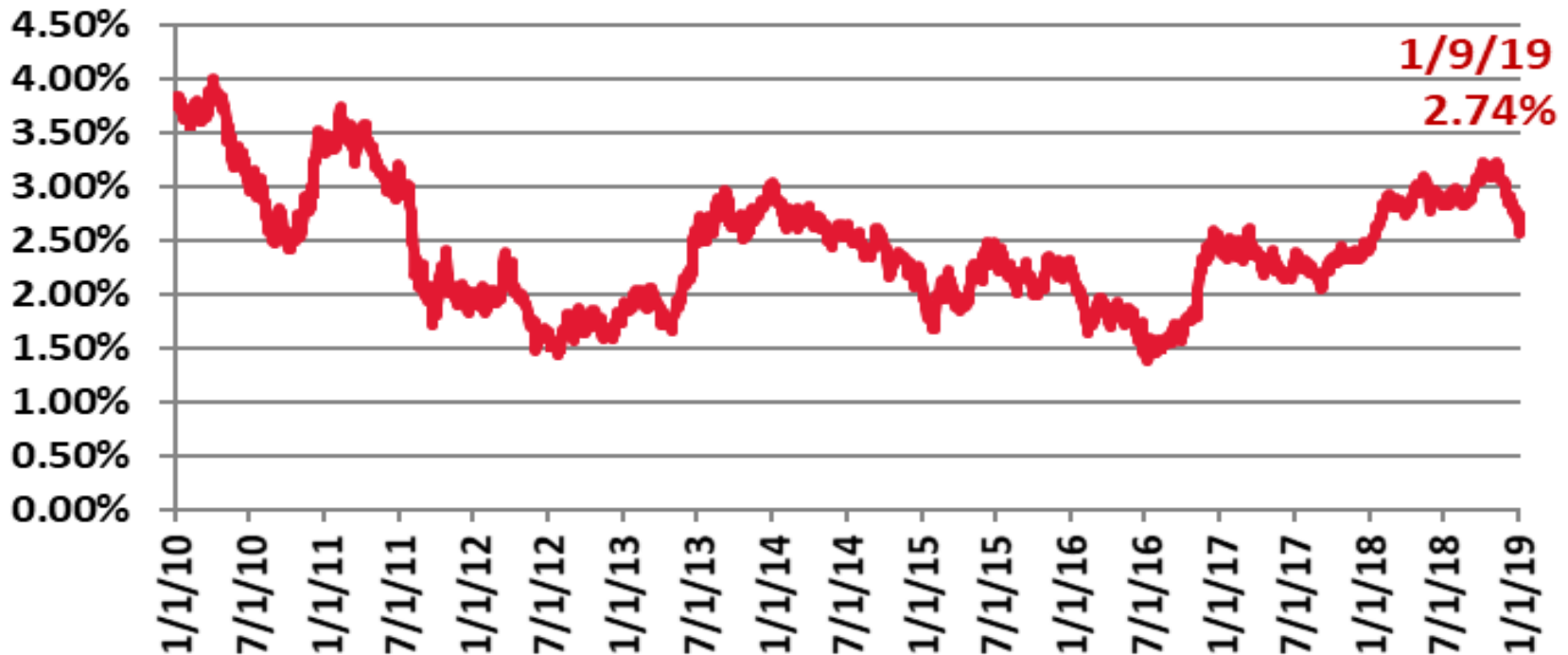
10 Year Treasury Yields - Long View



Source: Dept. of Treasury as of 1/9/19, Greer Advisors,

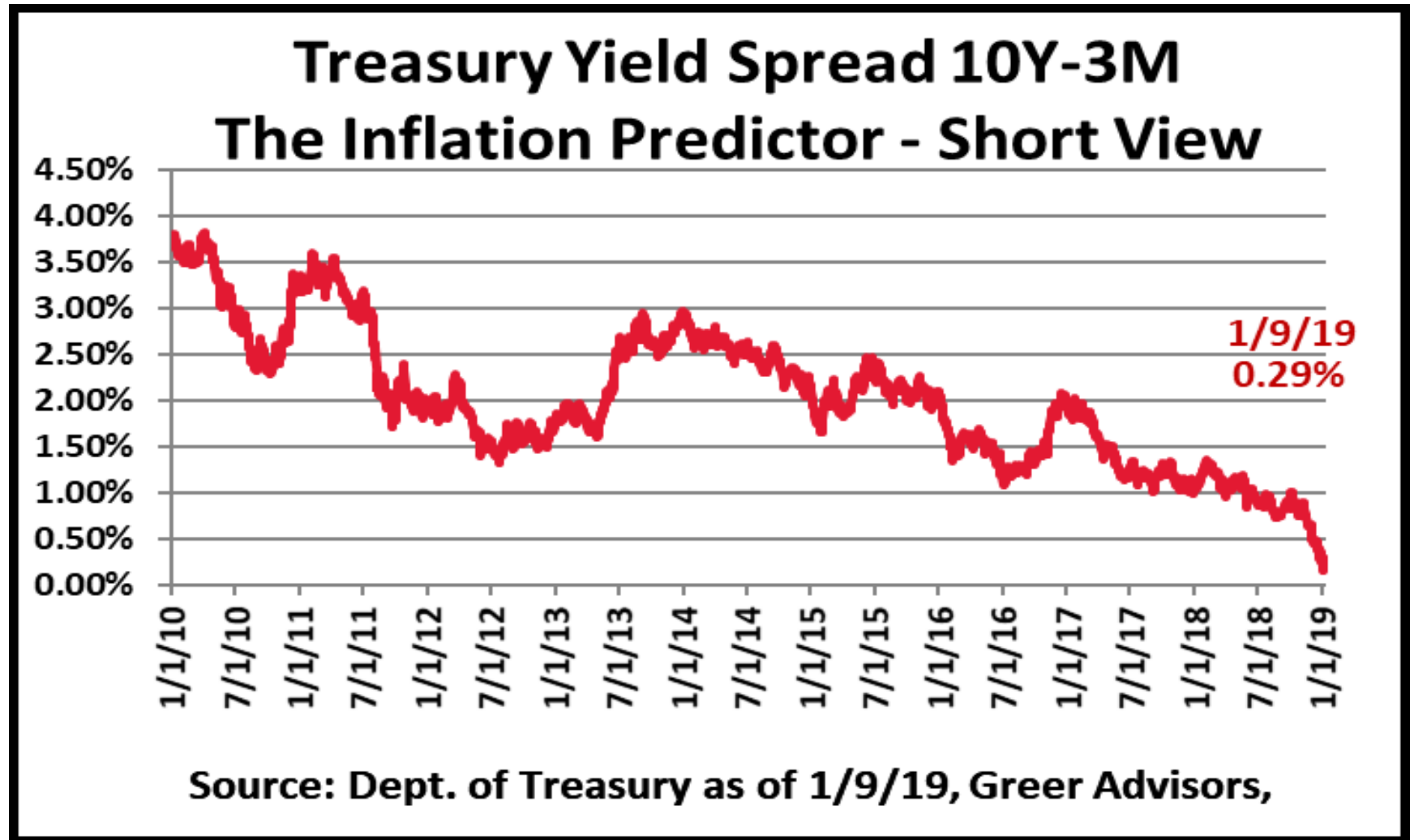
Interest Rates – Short Term View – 2010+

10 Year Treasury Yields - Short View



Source: Dept. of Treasury as of 1/9/19, Greer Advisors,

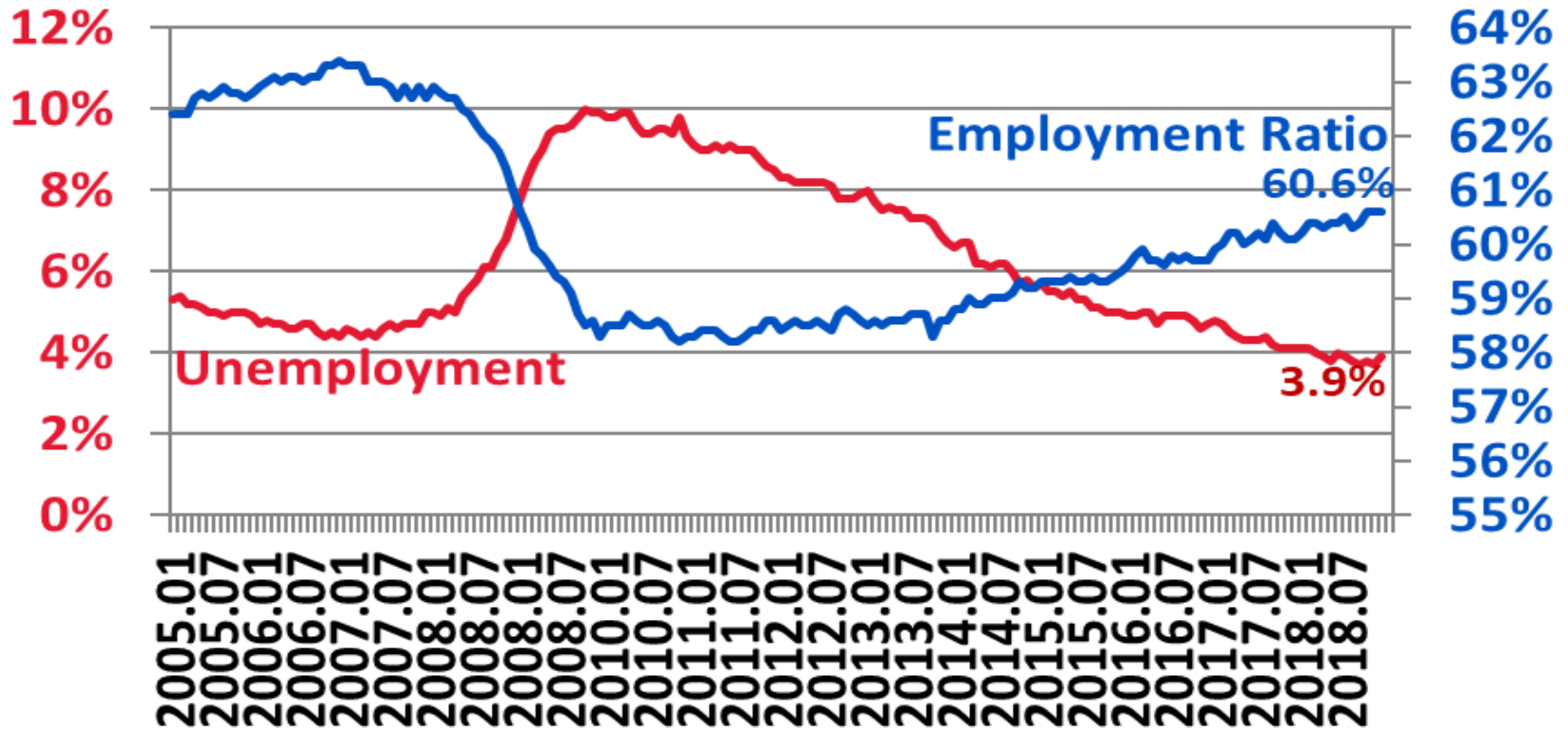
Inflation



Note: When Interest Rates > GDP growth, this can go to negative aka deflation, as it did in the early 80's with 12-15% 10 Yrs

Key Economic Indicators

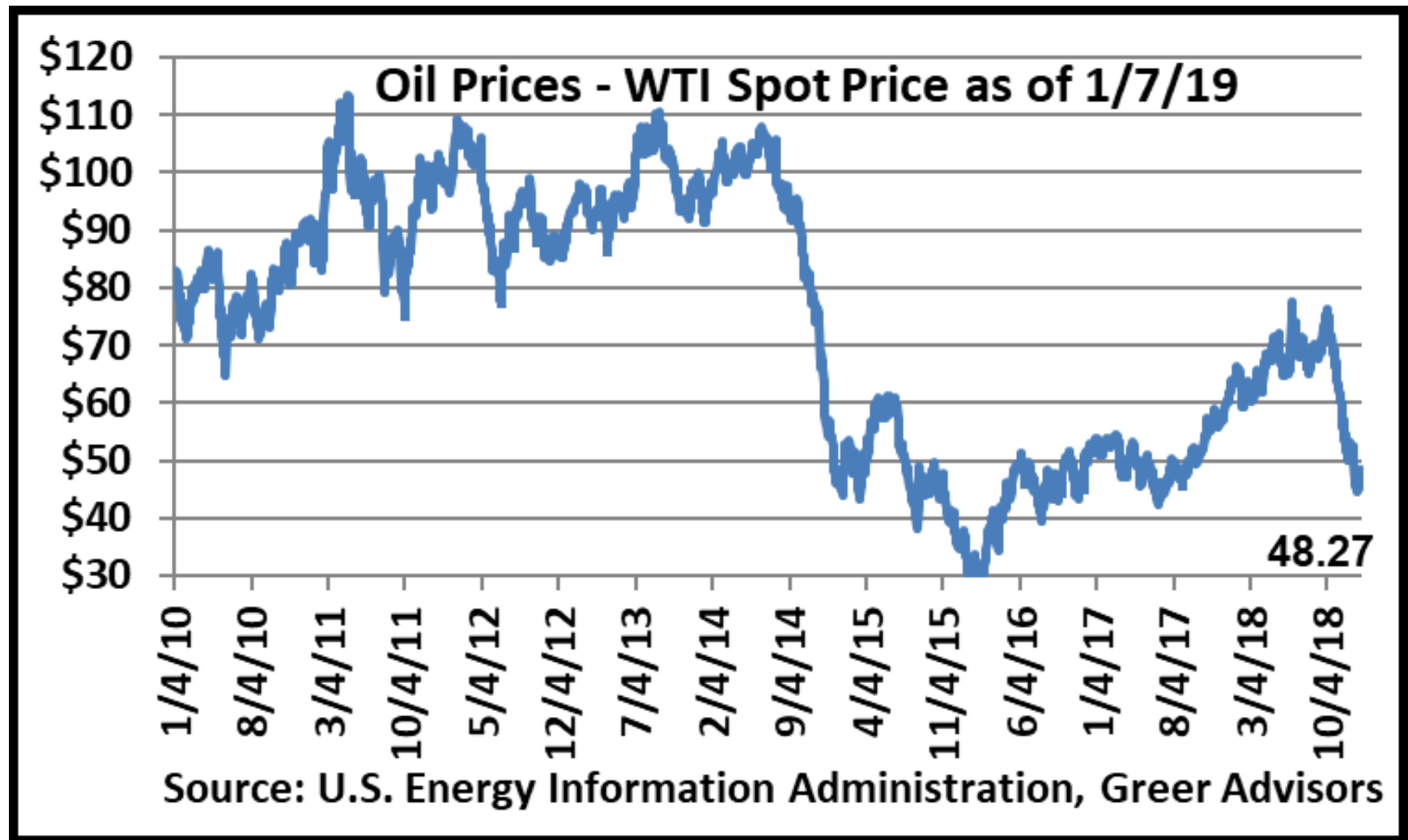
Employment Situation - End of 2018.12



Source: BLS, Greer Advisors, LLC

8 Employment Ratio, aka Employment Population Ratio =
Employed persons 16 years and over, divided by the population.

Oil Prices Remain Low, EIA

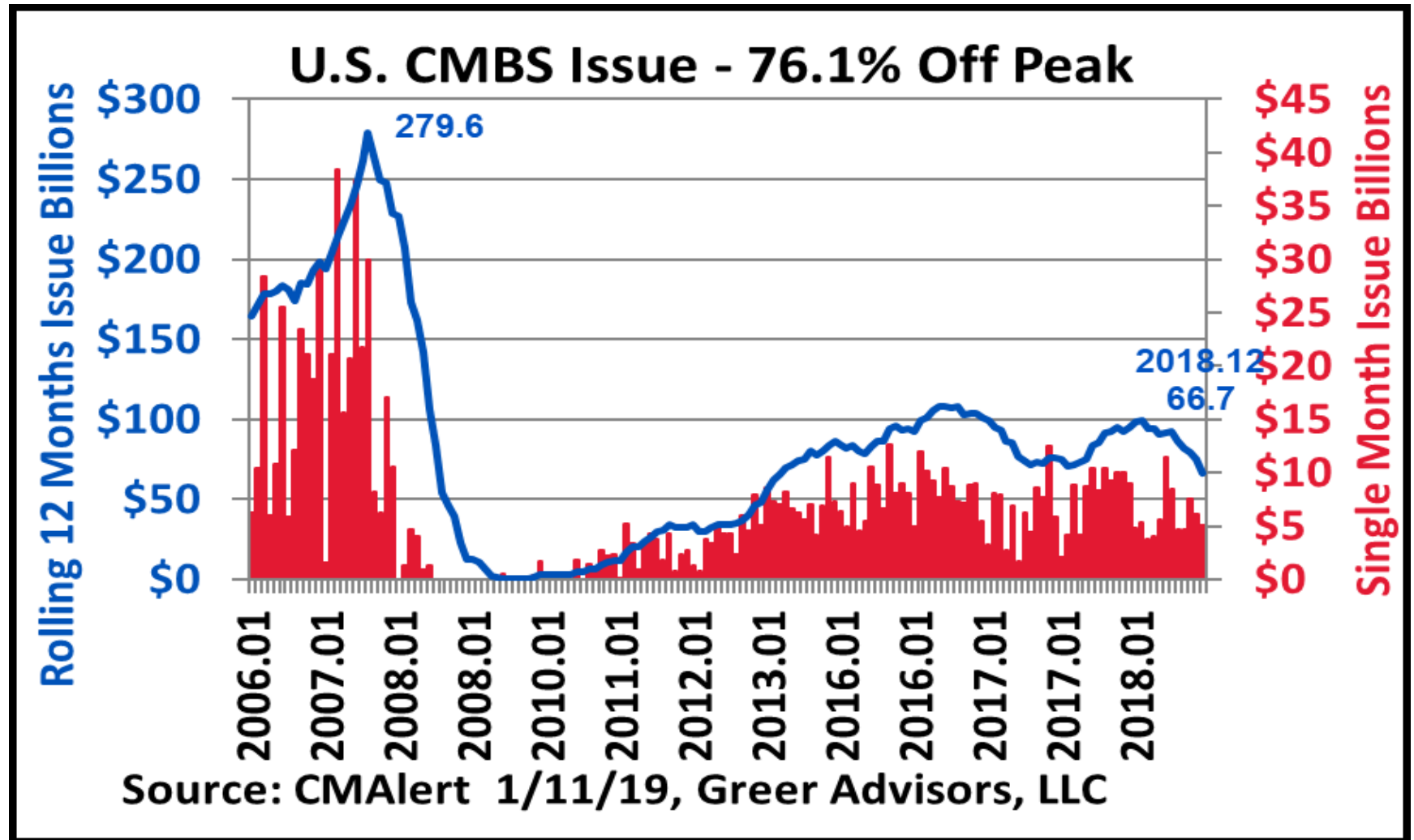


9 U.S. uses West Texas Intermediate Crude Oil, which is a much higher grade of crude than that used by many other countries.

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- Real Estate Capital Markets

CMBS Issuance - Rising from Floor

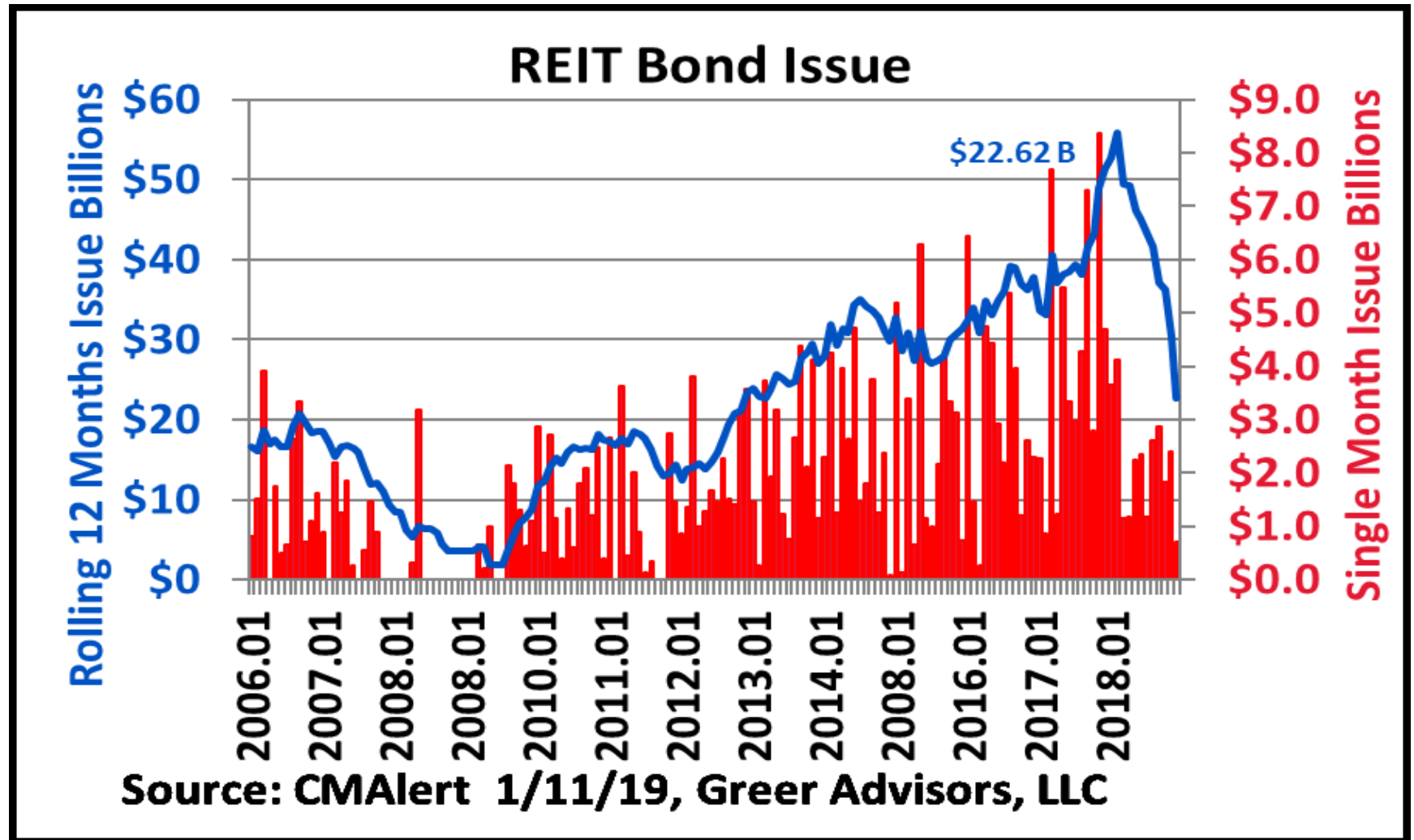


Through End of December 2018

11 Methodology Change effective 2018.01

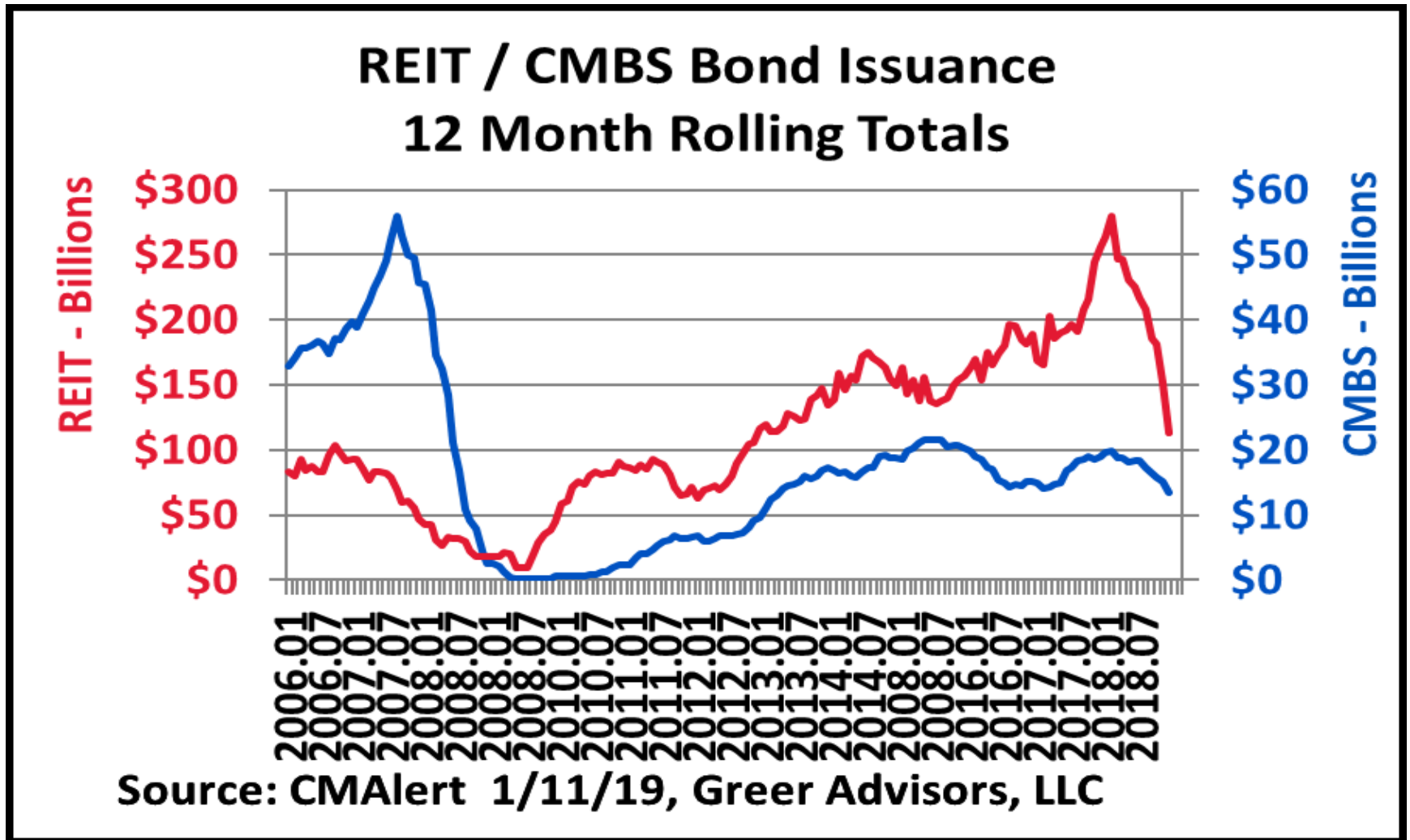
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REIT Bond Issuance – Continued Growth



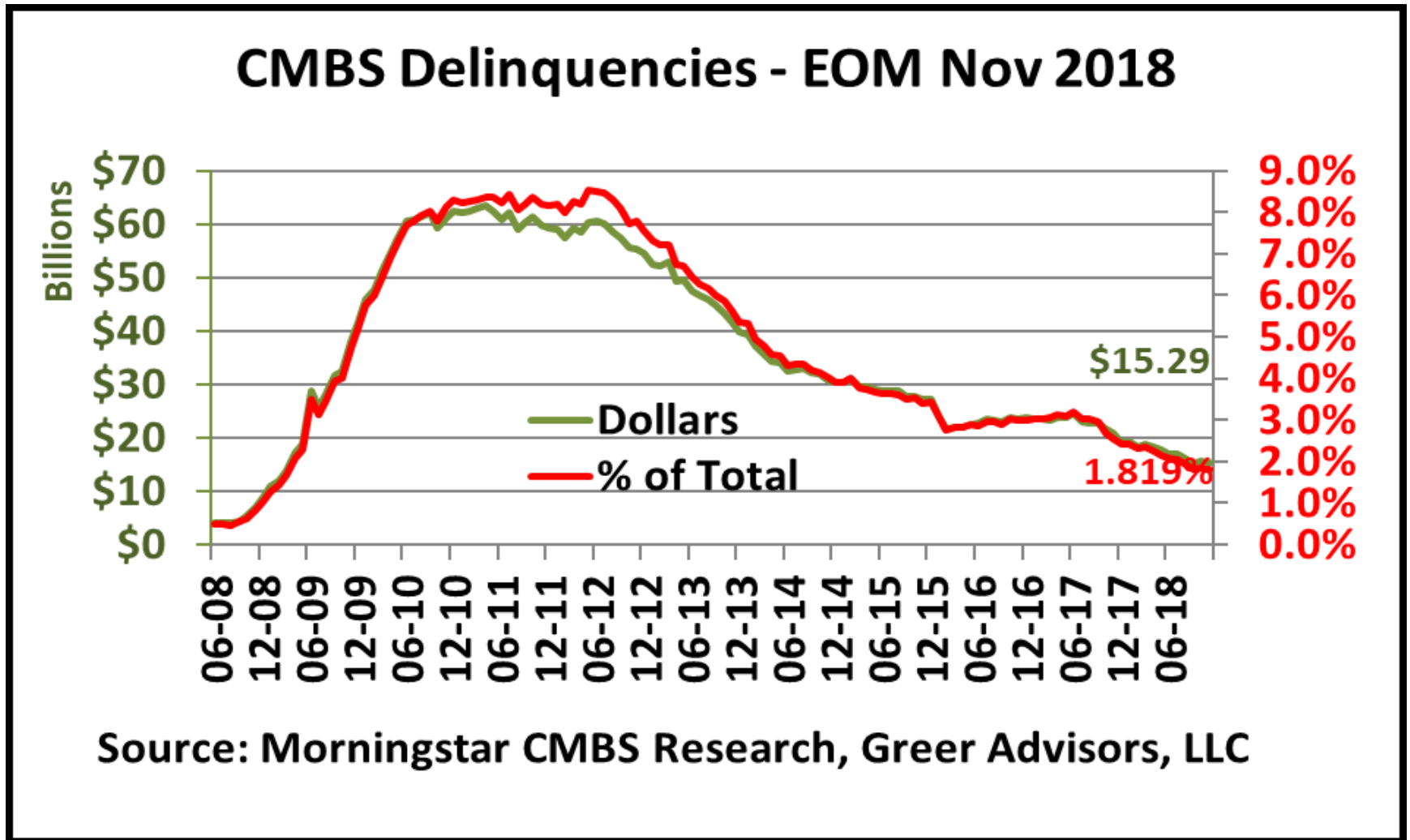
Through End of December 2018

REIT Bond Issuance – Continued Growth



Through End of December 2018

CMBS Delinquencies – Rise, Fall & Stabilize



CMBS Delinquencies by Property Type

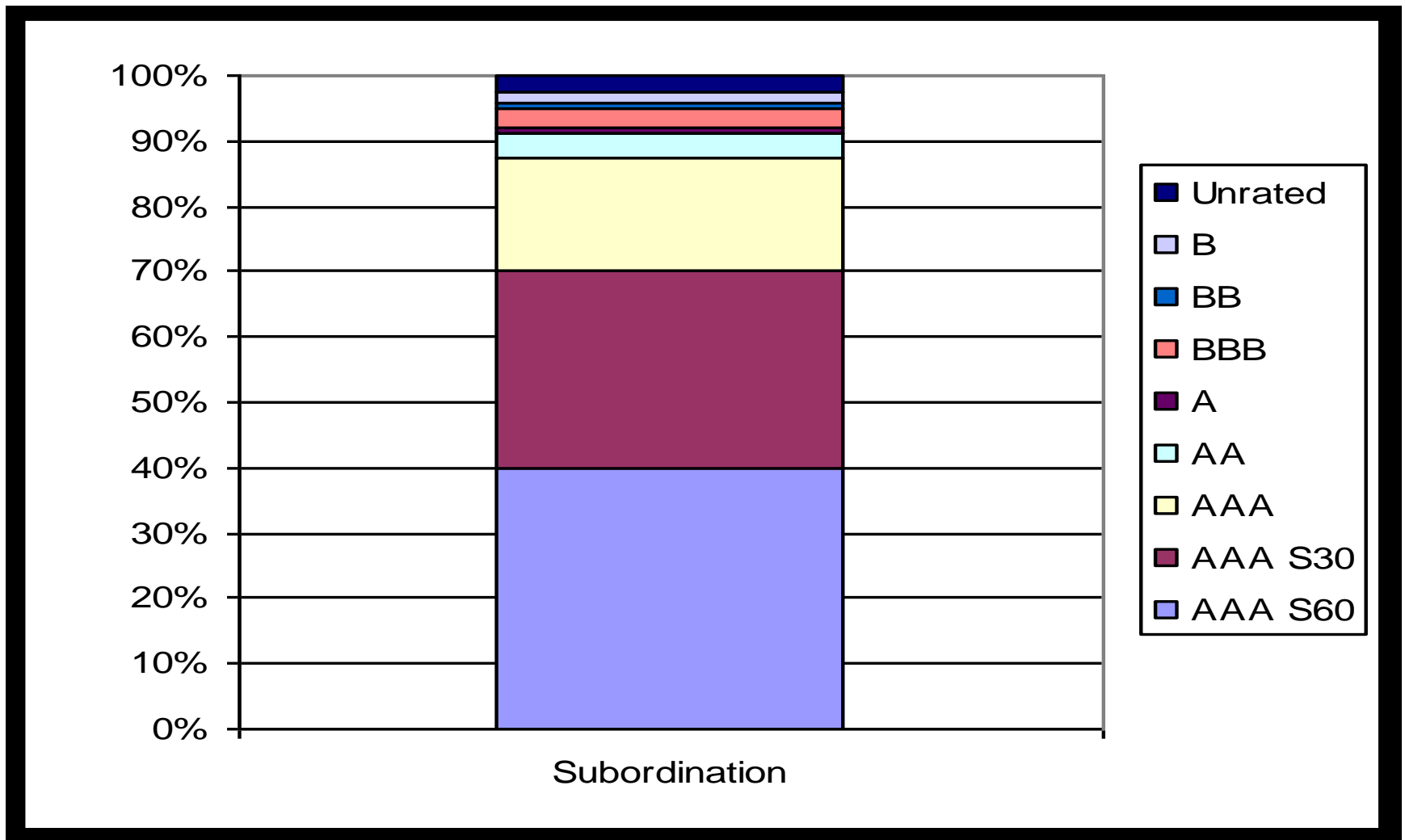
Trailing 12-Month Delinquency by Property Type												
Property Type	12/17	*1/18	2/18	3/18	4/18	5/18	6/18	7/18	8/18	9/18	10/18	11/18
Healthcare	1.77	1.77	1.77	1.82	1.83	1.80	2.21	2.21	1.92	1.94	1.95	1.98
Hotel	2.47	2.48	2.48	2.49	2.29	2.13	2.06	2.09	1.95	1.91	1.78	1.74
Industrial	4.44	4.52	4.59	4.31	3.73	3.64	3.65	3.45	3.23	2.51	2.44	2.12
Multifamily	0.32	0.32	0.31	0.36	0.30	0.32	0.30	0.34	0.30	0.30	0.34	0.32
Office	5.48	5.24	4.99	5.17	5.00	4.59	4.32	4.22	3.90	3.74	3.66	3.66
Other	2.15	2.14	2.13	2.05	1.84	1.85	1.91	2.04	1.72	1.71	1.63	1.46
Retail	5.67	5.63	5.59	5.61	5.61	5.47	5.40	5.22	5.24	4.74	5.09	5.13
* 1/18 data was not published due to new format. The average of 12/17 and 2/18 is shown.												
Source: Morningstar Credit Ratings, LLC, Greer Advisors, LLC												

CMBS Delinquencies by Year – Worst 10

Delinquency by Year of Issuance - Worst 10 Years				
Year	\$ Total Year	# Loans	% CMBS Univ.	% Delinq.
2007 Total	9,923,078,030	613	1.25	51.80
2006 Total	4,821,486,788	265	0.61	25.17
2005 Total	1,519,259,916	79	0.19	7.93
2008 Total	685,640,531	45	0.09	3.58
2014 Total	522,854,232	63	0.07	2.73
2013 Total	358,695,374	42	0.05	1.87
2015 Total	288,208,940	45	0.04	1.50
2012 Total	275,007,522	18	0.03	1.44
2004 Total	236,952,534	23	0.03	1.24
2016 Total	108,536,583	61	0.01	0.57
Top 10 Totals	18,739,720,450	1,254	2.37	97.83
Source: Morningstar Credit Ratings, LLC, Greer Advisors, LLC				

■ Risk Analysis

Bond Stack - Subordination



Note: The names of tranches have changed over years, and differ by rating agency. Markit's TM definition for CMBx is theirs.

Players in “Simple” CDS/C?Bx (Derivative)

Business Issues Bonds



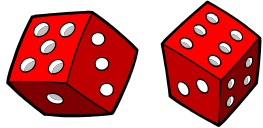
Bonds initially rated too poor for market, eg “BB”

Rating Agency Rates Bonds

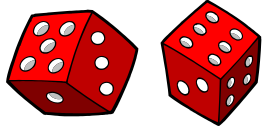


Gives loss forecast & amount required for “AA” rating

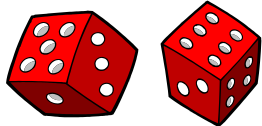
Side Bet 1



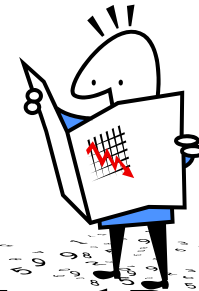
Side Bet 2



Side Bet 3



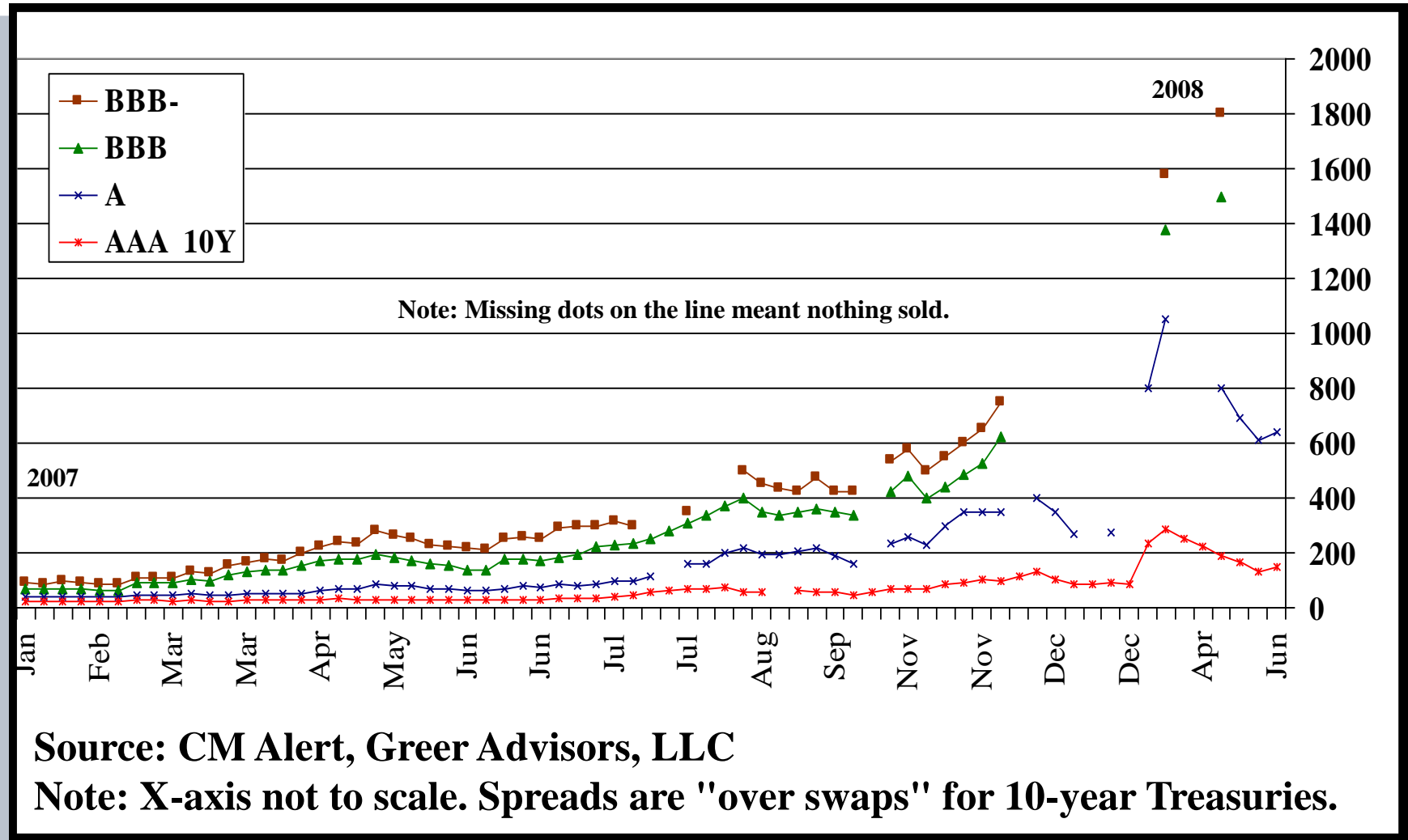
Investment Bank issues CDS (aka Credit Enhances Debt) creates buyers on both side. Protection Seller v. Buyer



Pension Fund Buys Bonds with CDS enhancement
Thinks it's AA investment

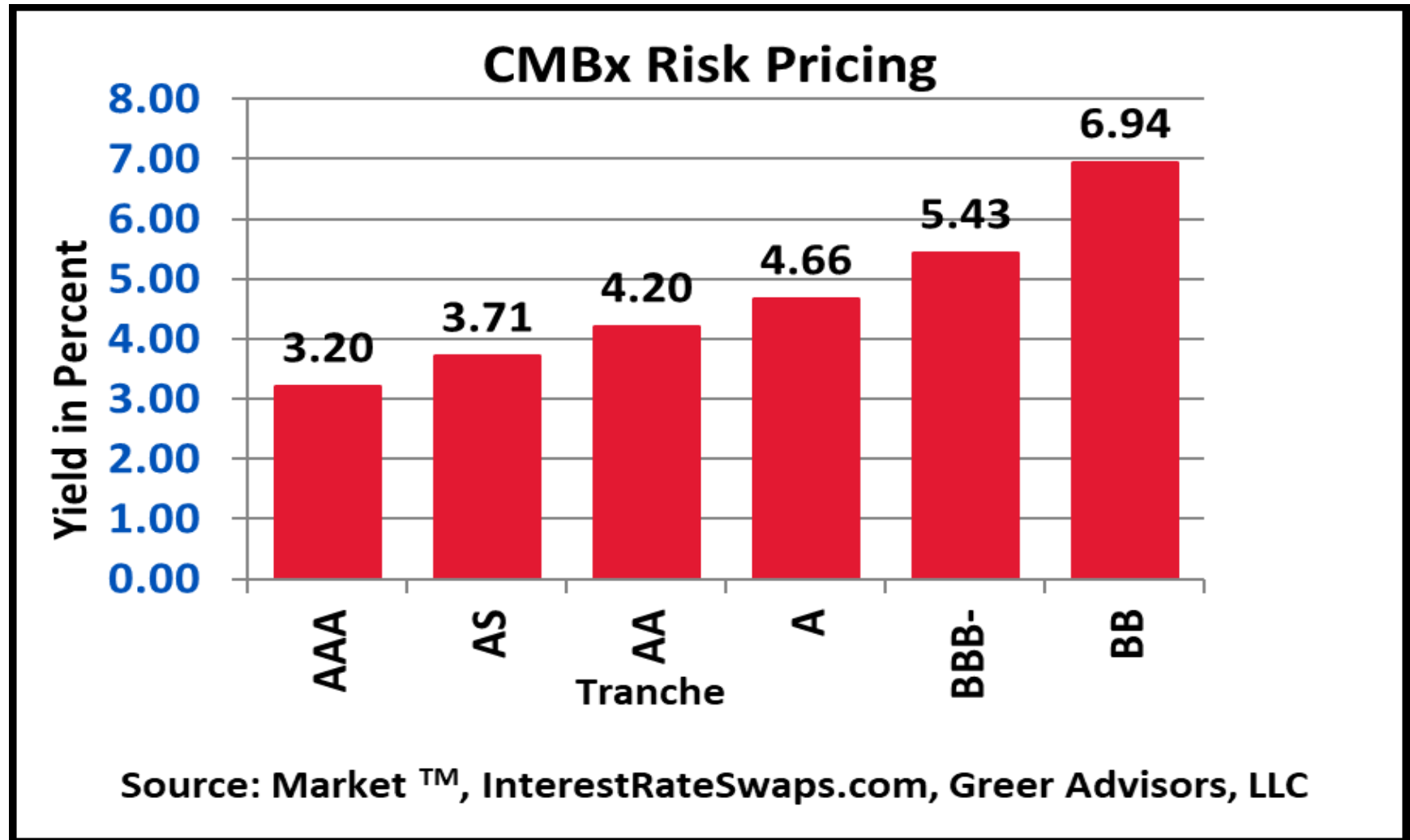
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CMBS Yield Spreads (Swap Spread, bps) Old



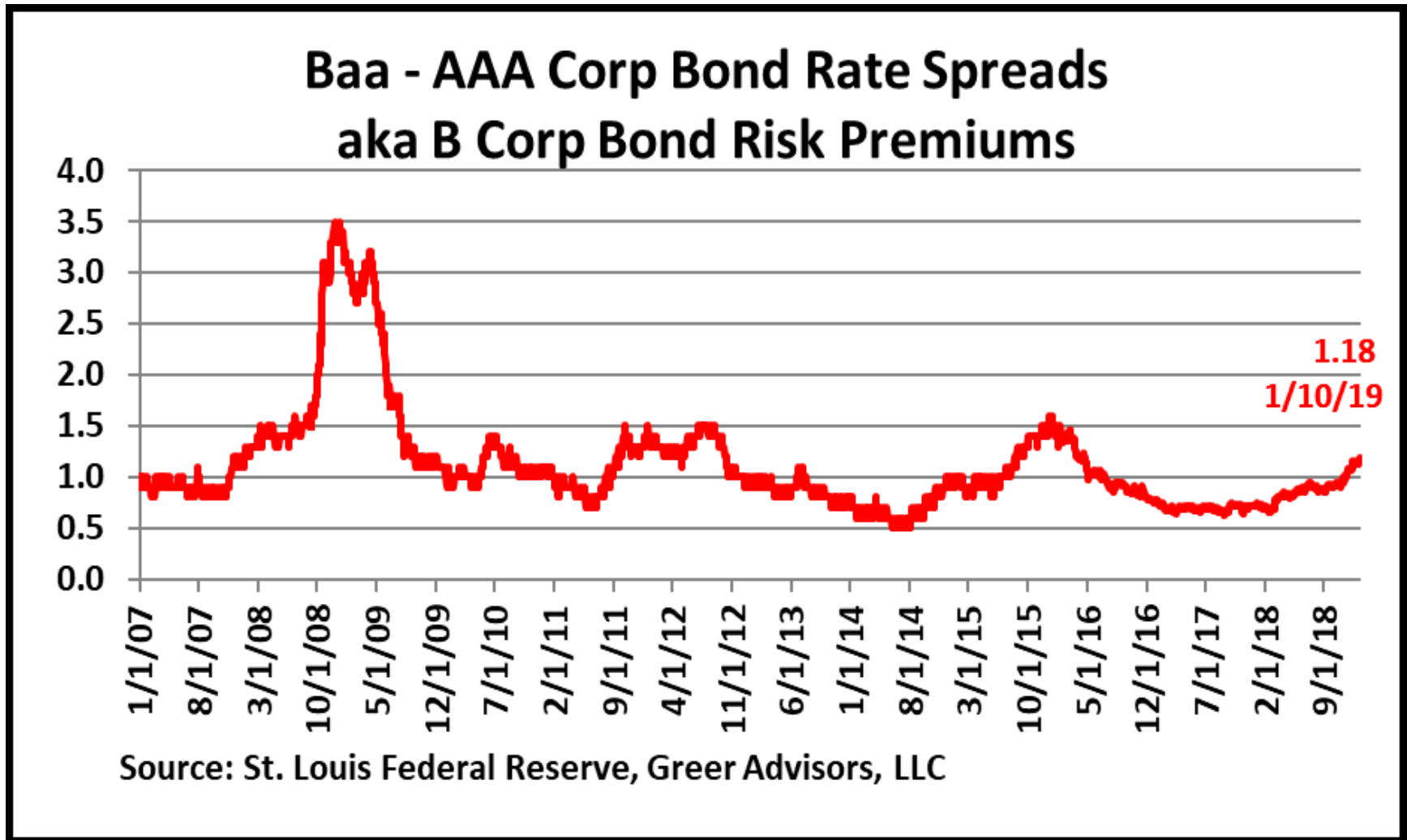
Note: This is what I sent throughout BofA in 2007-2009.

RISK PREMIUM – CMBx Derivative Pricing



Spread to Swap by Tranche as of 1/10, Swap as of 1/9

RISK PREMIUM – Bond World



- **Conclusions & Forecast**

Conclusions and Forecast

- A softening of Dodd Frank (per Trump's Plan) could (big maybe) be good for Commercial Real Estate. Soften not eliminate!
- Rent & Vacancy rates continue to improve across the Country for most (not all) markets and most property types
- Rent & Vacancy rate continue to improve across most of SoCal for most markets and most property types
- Most Markets are now well above 2007 Rent Levels
- Continued Low Oil Prices had been Keeping Interest Rates Low
- Fed rate hikes are now impacting Capitalization and Yield Rates

Conclusions and Forecast - continued

- Chinese Restrictions on Exporting of Currency Might Impact Demand for U.S. Real Estate, especially in Top markets...Roughly \$6T in 2016 to current Target of \$1T
- A Sudden Rise in Oil Prices Could be Devastating
- Tech & Oil Markets Have Improved the Most
- CMBS Issue has steadily increased since the 2007/2009 fall, but remains much lower than pre-fall levels, i.e. good thing
- CMBS Delinquencies Have Dropped to sub 2.0%, lowest since April of 2009 when they were 2.066%
- 2019 Forecast - CRE values will remain near flat and may drop slightly in most markets due to increases in interest rates, currency restrictions, and general fears of event risk
- REIT & CMBS Issue is Falling

Questions / Answers



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Top Questions & Answers from Event

- The Employment Ratio is impacted by many people accepting lower-paying jobs and part-time jobs; hence, the effective ratio is probably much lower.
- Many wealthy Chinese investors in the U.S. are ‘parking’ their money rather than investing. Partially due to fears that if they go back to China, they could be found guilty of the currency export laws; hence, they might not go back...ever. Therefore, expect a lag effect on U.S. markets related to the currency restriction. It will impact our CRE markets within a few years.
- REITS have done better than CMBS because REITS are perceived as a better class of investment, i.e. lower risk.
- Low oil prices benefit the U.S., but hurt oil-producing countries, e.g. OPEC, Russia, Venezuela, etc. A drop in price increases event risk. An increase increases inflation and interest rates.
- Tariff wars are mostly politicking. Expect talks, retaliation tariffs, but no major changes. Politics as usual!