

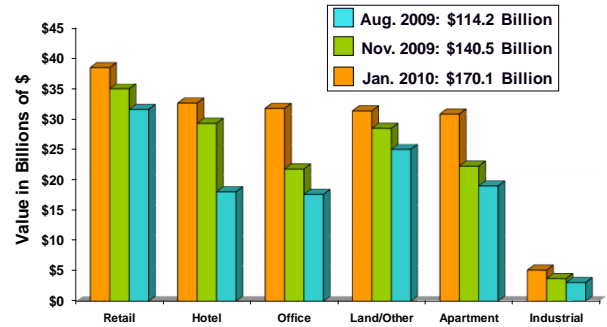
**Distress: Growth Continues, But at a Slower Pace**

Nationally, the total value of **distressed commercial real estate** is \$170.1 billion, including properties in distress, foreclosure, and lender REO, according to data from Real Capital Analytics. This is an increase of 21% (\$29.6 billion) since our November report and 49% (\$55.9 billion) since August. The rate of growth has slowed from its peak during the first half of 2009, when the total value was doubling every three months. We believe that this slow-down reflects the continued willingness of many lenders to extend debt obligations to traditionally qualified borrowers, with or without credit enhancement.

But the real test of velocity of distress will come in 2010 – 2011, as +/- \$600 billion in loans come due and experts predict up to 350 banks may fail.

As was the case last quarter, retail properties are the largest segment of the distressed market, with \$38.5 billion, compared to \$35.0 billion in November. Notably, distressed office properties grew by \$10.0 billion since November to \$31.8 billion — a 46% increase.

**Change in U.S. Distressed Commercial Real Estate August 2009 — January 2010**



Source: Real Capital Analytics, graphic by Delta Associates; January 2010. Note: Includes properties in default or foreclosure, plus lender REO.

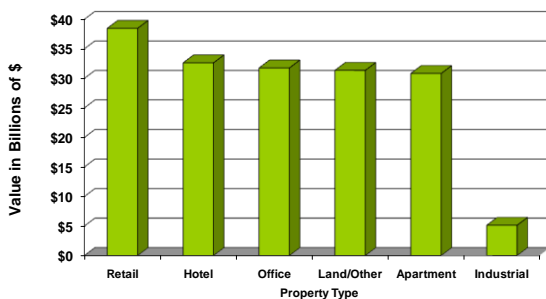
Every product type recorded an increase.

- Once again, office properties increased the most, up 46% to \$31.8 billion and into third place.
- Apartment properties rose markedly, as well, and are close behind with \$30.8 billion, up 28%.

**Stressed Commercial Real Estate Assets**

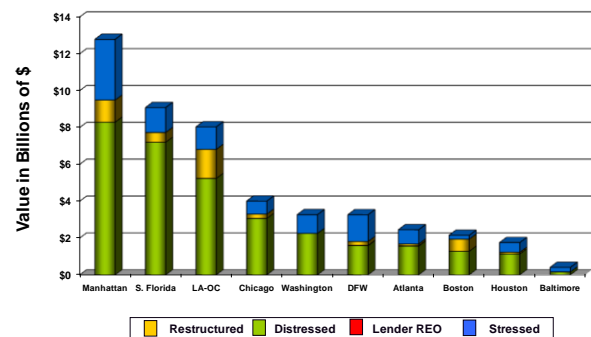
While the volume of distressed assets is significant, also consider the looming volume of **stressed commercial real estate assets**: These properties have characteristics of concern in the short term — maturing loans, bankrupt tenants, underperformance, financially troubled owner, or other significant obstacles that could potentially lead to distress in the future.

**U.S. Distressed Commercial Real Estate by Type January 2010**



Source: Real Capital Analytics, graphic by Delta Associates; January 2010. Note: Includes properties in default or foreclosure, plus lender REO.

**U.S. Stressed Commercial Real Estate by Market January 2010**



Source: Real Capital Analytics, graphic by Delta Associates; January 2010. Note: Value based on loan amount.

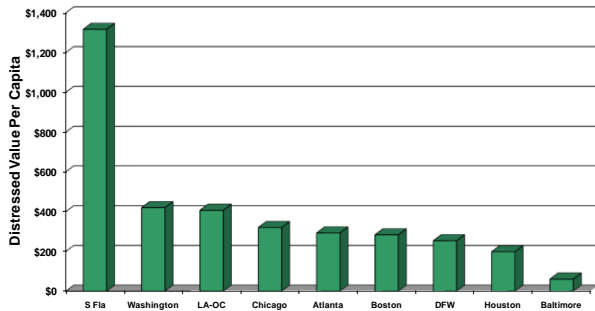
Watch for Volume 7 in this reporting series in March 2010. If you would like to subscribe free of charge, send your request to: [David.Parham@DeltaAssociates.com](mailto:David.Parham@DeltaAssociates.com).

The Manhattan market continues to have the highest volume of distressed real estate assets (followed by South Florida), and it also has \$3.3 billion in potentially distressed (what we call “stressed”) real estate assets as of January 2010. Turmoil in the financial industry, coupled with the housing

slowdown, has threatened the performance of many buildings and potential developments in Manhattan.

South Florida, with \$1,317 in distressed property per capita, has the highest ratio per capita other than Manhattan. The Washington, DC area market, which we have featured in this issue, has the next highest at \$420 per capita.

**Distressed Commercial Real Estate Value Per Capita  
January 2010**

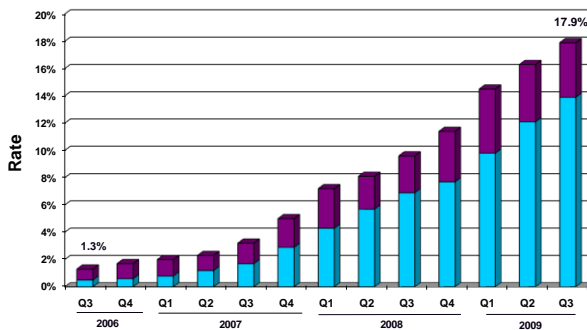


Source: Real Capital Analytics, graphic by Delta Associates; January 2010. Note: Excludes Manhattan at \$5,071 per capita. Includes properties in default or foreclosure, and lender REO. Value based on loan amount.

**Delinquency Rates: Continued Rise**

While single-family and condo loans account for most of the delinquency problems with construction loans, estimates indicate that delinquency rates for apartments and commercial properties are on the way up as well, according to Foresight Analytics. The delinquency rate has risen steadily over the past two years from 5.0% in the 4<sup>th</sup> Quarter of 2007 to 17.9% in the 3<sup>rd</sup> Quarter of 2009. The non-accrual rate, which rose from 2.9% to 14.1% in the same period, is largely responsible for the increase in total delinquency.

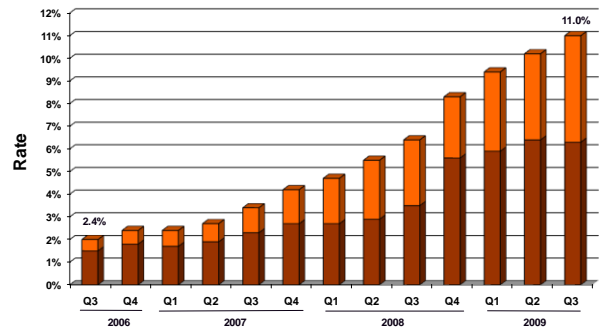
**Total Delinquency and Nonaccrual Rates  
Construction Loans**



Source: FDIC, Foresight Analytics, graphic by Delta Associates; January 2010.

In the first-lien single-family mortgage sector, total delinquency grew to 11.0% in the 3<sup>rd</sup> Quarter, with a 4.7% nonaccrual rate — 0.9% more than in the 2<sup>nd</sup> Quarter and the highest rate since 1992. In comparison, total delinquency was 6.4% in the 3<sup>rd</sup> Quarter of 2008, with 2.9% for nonaccruals. The rise in nonaccruals indicates that lenders are more frequently classifying serious delinquencies as nonaccrual rather than making concessions to borrowers on the most substantial loan modifications, according to Foresight Analytics.

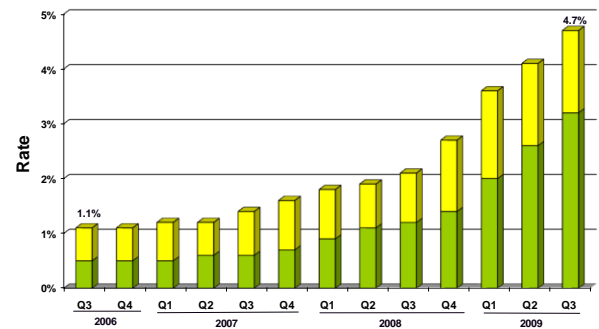
**Total Delinquency and Nonaccrual Rates  
Residential Mortgages**



Source: FDIC, Foresight Analytics, graphic by Delta Associates; November 2009.

The commercial mortgage sector's total delinquency rate grew to 4.7% in the 3<sup>rd</sup> Quarter of 2009, compared to 4.1% in the 2<sup>nd</sup> Quarter and 2.1% one year ago. Again, a 3.2% non-accrual rate is the main factor contributing to overall growth, accounting for 68% of the total delinquency. In comparison, the 3<sup>rd</sup> Quarter 2008 non-accrual rate was 1.2%.

**Total Delinquency and Nonaccrual Rates  
Commercial Mortgages**

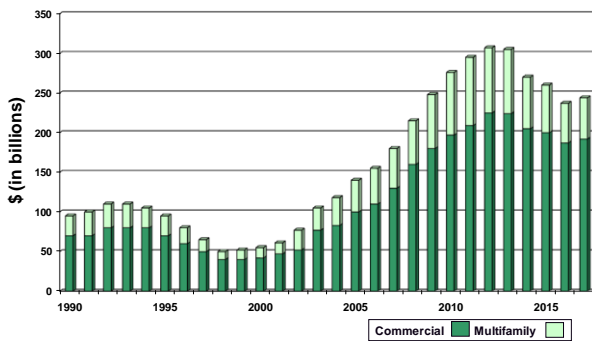


Source: FDIC, Foresight Analytics, graphic by Delta Associates; November 2009.

**Mortgage Defaults and Maturities Rising**

The commercial mortgage default rate rose from 2.88% in the second quarter of 2009 to 3.4% in the 3<sup>rd</sup> Quarter, according to Real Estate Econometrics, and it is projected to reach 4.2% by the end of 2009. As reported in the *Financial Times*, there was a \$50.3 billion balance of commercial mortgages that were delinquent or in default in the 3<sup>rd</sup> quarter. In addition, the total volume of commercial and multifamily mortgage maturities continues to increase — rising to approximately \$275 billion in 2010, and to more than \$300 billion per year in 2012 and 2013, according to data from Foresight Analytics. More than 80% of the commercial mortgages that will mature in the next two years are held by banks. Refinancing these maturing mortgages remains difficult due to the weak economy, tight capital, falling property values, and new mortgage originations.

**Commercial and Multifamily Mortgage Maturities Loans Maturing by Year**

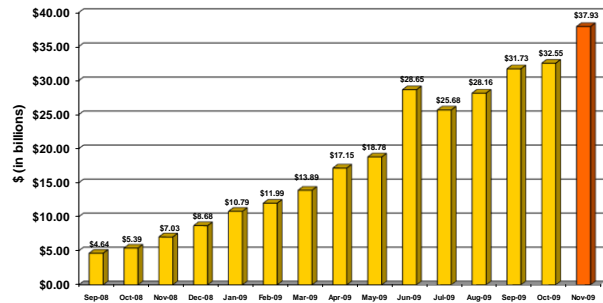


Source: Federal Reserve, Foresight Analytics; January 2010.

**CMBS Delinquency: Continued Growth**

Realpoint Research reports that, from November 2008 to November 2009, the trailing 12-month delinquent unpaid balance of commercial mortgage-backed securities (CMBS) rose by \$30.9 billion, or 440%, to \$37.9 billion. The delinquent balance is 4.7% of the total unpaid CMBS balance of \$806.1 billion. Both the delinquent unpaid balance and ratio to total balance continued their cyclical rise in November, reflecting a steady increase from historic lows at the peak of the market in mid-2007.

**Monthly CMBS Delinquency**



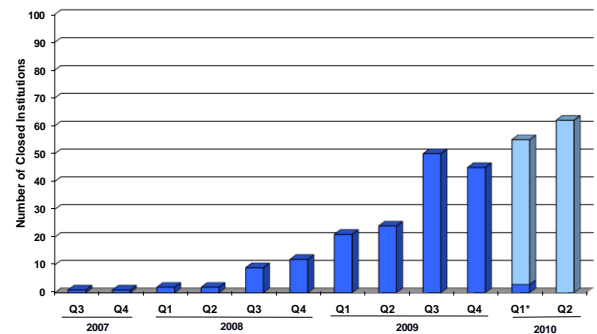
Source: Realpoint Research; January 2010.

Realpoint Research projects that the delinquent unpaid CMBS balance will increase to between \$50 and \$60 billion, with a delinquency ratio of more than 6%, by the middle of 2010.

**Tough Sledding for Banks Ahead**

With delinquency rates continuing to climb and increasing mortgage maturities, we expect a tougher environment ahead for banks. Bank failures have become increasingly frequent, with 25 in all of 2008 and a whopping 140 in all of 2009. Foresight Analytics projects about 120 additional bank failures in the first half of 2010.

**Bank Failures Current Cycle and Near-term Forecast**



Source: FDIC, Foresight Analytics; January 2010.

\* As of 1/15/2010

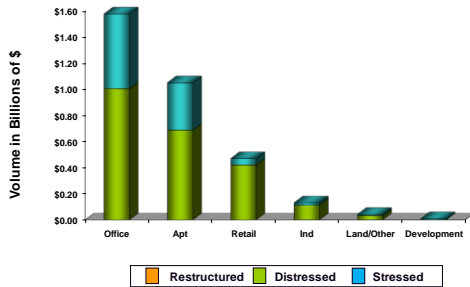
**Featured Metro: Washington, DC Area Moderate Distress Levels; Office and Apartments Lead the Way**

Washington, DC area distressed office properties have a substantial lead in total volume over the apartment sector, including both stressed and distressed assets. However, the apartment sector's combined volume is also quite high relative to other



property types. The volume of distressed office assets in the Washington area exceeds \$1.0 billion, while stressed office assets total about \$571 million.

**Distressed Commercial Real Estate  
By Severity and Property Type  
Washington, DC Area**

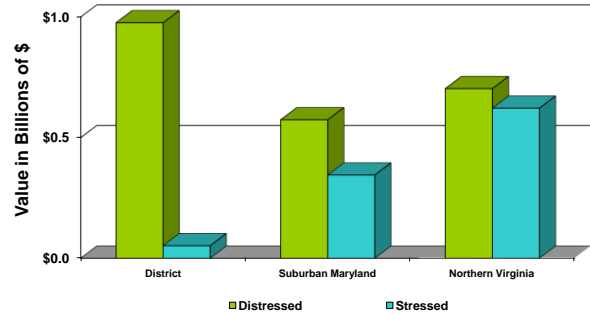


Source: Real Capital Analytics, graphic by Delta Associates; January 2010.

In the Washington area, the District of Columbia has the highest volume of distressed assets – \$976 million – while Northern Virginia has the highest volume of stressed assets – \$622 million. The large volume of distressed assets in the District of

Columbia is due primarily to a portfolio of office properties owned by Tishman Speyer, including International Square, 1201 F Street, and 1717 Pennsylvania Avenue. In addition, The Dumont and Senate Square, two large condominium projects by Broadway Management, have run into problems.

**Distressed Commercial Real Estate  
By Substate Area  
Washington Metro Area**



Source: Real Capital Analytics, Delta Associates; January 2010.

Note: Distressed includes properties in default or foreclosure, plus lender REO.



Delta Associates, the research affiliate of Transwestern, is a firm of experienced professionals offering, consulting, valuation, and data services to the commercial real estate industry for over 25 years. The firm's practice is organized in four related areas:

1. **Valuation** services for partial interests in commercial real estate assets.
2. **Consulting**, research and advisory services for commercial real estate projects, including market studies, market entry strategies, asset performance enhancement studies, pre-acquisition due diligence, and financial and fiscal impact analyses.
3. **Distressed asset recovery services** to include property performance analyses and enhancement studies, debt structuring evaluation and note valuations, portfolio assembly due diligence, valuations, and litigation support.
4. **Subscription data** for selected metro regions for office, industrial, retail, condominium, and apartment markets.

For further information about Delta Associates and to see all of our publications, please browse our web site at:

[www.DeltaAssociates.com](http://www.DeltaAssociates.com)

**Consulting and Advisory Services**

Gregory H. Leisch, CRE  
Chief Executive  
500 Montgomery Street, Suite 600  
Alexandria, VA 22314  
(703) 836-5700; Fax (703) 836-5765  
Greg.Leisch@DeltaAssociates.com

**Government Services**

Craig Powell  
2101 Wilson Blvd., Suite 200  
Arlington, VA 22201  
(703) 516-2263; Fax (703) 516-2299  
Craig.Powell@DeltaAssociates.com

**Market Publications Group**

Alexander (Sandy) Paul  
National Research Director  
500 Montgomery Street, Suite 600  
Alexandria, VA 22314  
(703)299-6373; Fax (703) 836-5765  
Alexander.Paul@DeltaAssociates.com

General email: Info@DeltaAssociates.com

## Distressed Asset Recovery Team



Delta Associates has partnered with Baker Tilly, Fore Consulting, Blackwell Advisors, and Appian Corporation to form the Distressed Asset Recovery Team (DART). This partnership offers services to government entities as well as borrowers and lenders to assist with the resolution of stressed real estate matters during this time of economic turmoil. These workout services include:

1. Property performance analysis
2. Debt restructuring analysis and note valuations
3. Investment advisory and portfolio assembly due diligence
4. Asset performance enhancement analysis
5. Valuation services
6. Forensic accounting and tax impact analysis
7. Litigation support and dispute resolution services

For more information, please contact Greg Leisch, Delta's CEO, at: [Greg.Leisch@DeltaAssociates.com](mailto:Greg.Leisch@DeltaAssociates.com)