COMMENTARY – *Bob Knakal*

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Realty Services

Debt is Available, No Matter What You Read

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Based upon what you read and hear about our building sales market today, one would think that there is absolutely no debt available in the capital markets. **Although there are significant stresses on the commercial mortgage market, there are still tremendous amounts of debt available to creditworthy borrowers for the acquisition of investment properties in New York City. I remain optimistic and I will tell you why.**

This article, and all further Commentaries by Bob Knakal, can be found on The Massey Knakal Reel – a blog for breaking sales, listing and neighborhood real estate news – at www.masseyknakal.com/blog

First, we must look at one question: Why all the negativity? Well, there are good reasons. On July 11 Indymac Bank was seized by federal regulators in what was the 2nd largest bank failure in US history. Indymac's $32 billion in assets was second only to the $40 billion in assets held by Continental Illinois Bank & Trust when it went bust in 1984. Indymac is a spinoff company of Countrywide Financial and specialized in Alt-A loans which required little or no documentation with respect to employment or income i.e., ability to repay the loan. You could say that they were the poster child of the lending excesses that exacerbated the subprime problems. The subprime crisis hit Indymac particularly hard based upon its residential loan portfolio. In addition, at the time the bank failed, 52% of its $1.067 billion in loans to homebuilders were in default.

Shortly thereafter, First National Bank of Nevada and First Heritage Bank of Newport Beach (Calif) followed suit and failed based upon bad loans. Last week, First Priority Bank became the 8th bank to fail in this cycle. This is after a two and one-half year period with no failures at all. The FDIC guarantees approximately $4.2 trillion deposited in banks and finds it necessary to increase insurance premiums, which are paid by the banks, due to the shaky outlook for the future. Presently, the FDIC has 90 banks on its "troubled bank list" which has historically had a 13% failure rate. Based upon current market conditions, it is expected that a significantly higher default rate will be experienced in the coming 18 months. In the form of a comparison, in the early '90s, 843 banks failed.

Furthermore, a recent study by Goldman Sachs shows that bank's willingness to lend money has not been this low since the late 1970s. The CMBS business, which accounted for approximately 50% of all commercial lending in 2007, has been invisible and there is a general malaise in the market about the ability of a buyer to get financing. **I said I was optimistic about the lending environment in the market, here's why:**

Interest rates are going to stay low. While talk of monetary policy tightening by the Fed has been on everyone's mind recently, some economists are now projecting rate cuts by year's end. The recent rally in two year treasuries, which was based upon the expectation that rates would increase, has retreated based upon the performance of recent economic indicators. Even the economists who predict a Federal Funds Rate of 1.5% by the first half of 2009 are sensitive to the fact that The Fed may be finished cutting rates. This is not because the economy is doing well or because inflation pressures are going to be sustained. Rather, it is because of credit contraction. Last Thursday, GDP data released showed that economic expansion is growing slower than projected, despite the economic stimulus package, which had a short term effect but which has already slowed. Last Friday, unemployment surged to 5.7%, a cyclical high. Meanwhile, oil prices are off by $25 per barrel and core inflation is less of a concern to the Fed. In Bernanke's last speech he indicated that there are ongoing stresses in the financial markets which are challenging US growth and that there was no imminent tightening. For these reasons, we believe the next meeting of the Fed this Thursday will be uneventful in terms of rate changes but telling in terms of rhetoric. Low rates are beneficial to our building sales market.

Of the 90 banks on the FDIC's list, none are in New York. Local banks are doing relatively well. A recent Wall Street Journal article indicated that, Hudson City Savings, Flushing Savings, Dime, Astoria and New York Community, among other

During Mr. Knakal's 24-year career, he has sold over 974 buildings having an aggregate market value of over $5.6 Billion. He was the top salesman, with partner Paul Massey, at Coldwell Banker Commercial (now CB Richard Ellis) in New York in 1986, 1987, and 1988 prior to forming Massey Knakal. In 1990, he was awarded Crain's New York Business "40 Under 40" awarded annually to 40 business people under forty years of age for outstanding achievement in the New York business community. In 2001, Mr. Knakal was named one of "The Top Dealmakers" by Real Estate New York Magazine. He has twice been the recipient of the Robert T. Lawrence Award in the Real Estate Board of New York's Most Ingenious Deal of the Year Contest. First in 2002, for the assemblage of the easterly blockfront of Second Avenue between 54th and 55th Streets. Then again in 2004 for the sale of the historic Gotham Book Mart at 41 West 47th Street.

Please give a call if you have questions about your property or the market in general.

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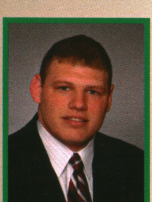

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local banks, didn't overreach in this most recent boom and are in relatively strong positions. This is positive as portfolio lenders are in business to lend money. Provided they have cash to lend, there has never been a better time to put money into the market. **Spreads, or the profitability, banks are making on loans today are 200-350 basis points over 10 year treasuries making them up to 10 times more profitable than they were 18 months ago.** Additionally, with loan to value ratios at 50%-65%, these loans are far less risky than loans made at 75%-90% loan to value. **Portfolio lenders' comfort zone on any one loan is about $30 million making properties worth $50 million or less much more financeable than larger properties.**

The CMBS market was given a shot in the arm last week as Lone Star Funds purchased $30.6 billion of Merrill Lynch's toxic collateralized debt obligations at a 78% discount to face value. Dozens of firms have raised funds to buy distressed mortgages. Two months ago the total equity available for this purpose was about $55 billion. Today this total stands at $100 billion. **It is thought that the Lone Star transaction creates a floor for the bad collateral which had a positive effect on financial's share prices as they rallied late last week.**

Furthermore, the commercial default rate is a miniscule 0.4%. This will increase based upon land loans which go bad within the next 12 months, but the rate will will remain relatively small.

So, with low rates and motivation for portfolio lenders to put dollars out high, debt is readily available for properties with stable cash flows. It is a given that these lenders are becoming more selective, as they should be, but the money is out there. We anticipate more competition among lenders as they fight over these highly profitable loans. **Spreads are likely to remain high and these profits will help to recapitalize the banking system.**

Our building sales market, particularly for properties under $50,000,000 in value, remains resilient. This is supported every day by the contracts we are signing for stable cash flow properties in all sectors of the market; multi-family, retail, office, and mixed use. Our contention remains that our volume slowdown is due to supply constraint, not waning demand.

– Bob