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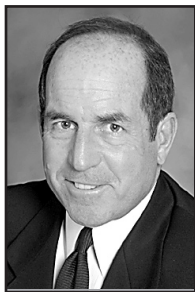
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Investment capital sits on sidelines, seeks opportunity

At midyear 2008, the predictions that emanated from January's crystal ball seemed to all come true. We are fully into another economic cycle and at this point if you watch the Dow Jones averages of the New York Stock Exchange's industrial stocks, it is a bear market. The Dow Jones averages are widely held to be a barometer of economic performance that accurately predicts profit performance nine months in advance. At early July, the Dow was down 20 percent from last October's high and there appeared to be more bad news to follow from increasing oil costs and illiquidity in firms providing capital resources and financial services.

Rising energy costs are leading to inflation in construction, manufacturing and food products. Anticipated increases in interest rates will not only add another level of cost, but will slow down and deter business growth. Consumer confidence has dropped significantly and nationwide job losses are up 1.5 million from one year ago.

What can we expect for the near term and the future? If



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the cycles that began in 1969, 1974, 1980 and 2000 are ones that we might use to gain insight, then we are likely to experience a continuing challenge for the foreseeable future. Certainly the balance of 2008 and likely the entire year of 2009 will be spent adjusting to the new economic rules. Because Denver is well-positioned to ride out this down portion of the cycle, the impact to the local economy will not be nearly as bad as is being experienced in manufacturing centers such as Detroit and overdeveloped housing markets in Florida, Las Vegas and Phoenix.

Increased gasoline costs have become the No. 1 concern for consumers. As consumers struggle to balance family budgets in the face of significant increases in costs, changes

in driving and consumption habits are being imposed in efforts to keep personal debt in check. Credit card debt is at an all-time high, and banks are expected to experience another hit to their financial stability as individuals find themselves unable to keep their personal financial situations in order.

No industry or geographic position has found itself immune from the impact of these conditions. The commercial real estate industry of Colorado is no different. New restrictions by lenders have all but stopped new construction projects. The underwriting criteria used by lenders in reviewing new projects has reduced leverage and increased equity requirements to the point of making all but a relatively few projects unfinancable.

The investment real estate industry is repositioning itself in an effort to correctly price both the more expensive costs of acquisition as well as the increased risks of property ownership. Since lenders will not give value to unoccupied space, investors may find themselves either on the sidelines until the property's finan-

cial performance improves, or they must pay less for a property to reflect the new underwriting criteria. All of these changes have resulted in a more-than-50 percent reduction in real estate investment transactions and dollar volume from one year ago. It is fair to say this is not the end of the cycle and more retractions in the industry can be expected before the picture improves. If interest rates increase, then cap rates also must rise and this will add another element to the pricing of a property.

What is promising about this situation is the amount of capital that is on the sidelines seeking correctly priced opportunities. Real estate is a legitimate asset class for investment by both large institutions as well as individuals. This simply becomes a case of waiting until pricing reaches its appropriate level. How long will this take? If the past is an indicator, then one might expect this process to last another 18 months, until the new market conditions are both recognized and established.▲