

EMPYREAN

FUNDING AND MANAGEMENT

Just when things were settling down, the volatility returns in a massive way. In the last three trading days we have seen dramatic swings in the yields on the 10 year treasuries and mortgage backed securities along with major indices worldwide. After relative calm, it appears that uncertainty may once again be taking hold of the markets. Added to the uncertainty, massive amounts of debt are being brought to the market by public companies and the U.S. Treasury to raise money to finance the massive deficit and continued spending. Unfortunately, without the massive spending, economic conditions may worsen dramatically leaving very little room to cut back on current spending. Recent gains in home sales and the slowdown in unemployment figures may be an aberration as economic uncertainty continues. Meanwhile, global industrial output continues to decline and consumers scramble to increase their savings.

The expected next "big shoe" to drop is the commercial loan and real estate market. The commercial real estate market as a whole includes about \$3.40 trillion as reported by the Wall Street Journal. There is about \$700B in outstanding loans connected to the commercial market that's been securitized and sold in bonds that were typically underwritten on 5, 7 and 10 year durations. A large part of these loans will start coming due in the coming years. Due to current delinquencies and vacancies borrowers will have a difficult time securing financing to pay off their existing debts as underwriting standards have also become much more conservative than the height of the market. Additionally, commercial banks, especially local ones, have loaded up on commercial loans over the last ten plus years and stand to take substantial losses on their portfolios.

Given all the current issues plaguing the market, opportunities still abound as prices drop on all asset types. Single family residences are much more abundant as inventories continue to rise and prices continue to drop creating more affordable pricing across all home prices. Commercial real estate valuations also are feeling the pinch as sellers that are in need of selling are having a very tough time finding buyers that are ready, willing and able to close. Additionally, buyers are becoming more concerned with the level of delinquent tenants and leases not being renewed. The lack of new tenants caused by reduced consumer spending is the main reason why retail sales and expansion is practically non-existent. Multi-family continues to be the safest asset classes as vacancy rates in most cities continue to be limited and rents haven't dropped significantly in most markets.

Unlike my regular optimistic columns, tough times demand honest disclosure. So although my tone is negative, there is a way to cope with these tough economic times. Conservatism and caution are the only the way we move forward. Long term financing is still available for projects that make sense as our terrific residential home mortgages that meet standard traditional underwriting guidelines. As always, I will continue to keep you posted of market conditions as we go forward and am available to discuss your financing and investment needs.

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