

EMPYREAN

FUNDING AND MANAGEMENT

So what's all the hype? Amazingly, many economists and analysts are predicting an end to the recession by the 4th quarter 2009. Unfortunately, the chances of that happening appear to be very slim to non-existent. With the recent reading on employment increasing to 8.9% which happens to be the highest level since 1983, massive reduction in lending and increasing savings rates with consumers it's very unlikely that we will see any type of a significant uptick in economic conditions in 2009. If you take into account the amount of workers that are now part-time and the reduction in working hours and wage deflation, unemployment is well north of 10%. Additionally, fears of near term inflation are completely baseless. In nearly any inflation scenario, rising wages play an important part in any economic recovery which is clearly not the case.

Fortunately, there is some good news as the pace of decline in various segments of the market has slowed dramatically. Current fundraising by institutions is progressing very nicely with many companies having success raising capital on the open markets. Libor rate spreads have also dropped which signals that bank to bank lending is starting to flow again and confidence may be returning to the market.

As I wrote earlier, a financial crisis led recession will take a lot longer to recover. This time around will be no different. The biggest concern to the economic recovery is the habits of the American consumer. Instead of spending and borrowing with little or no savings, people are now reducing their debt and increasing their savings to levels north of 4% of income. This type of savings rates may cause massive deflation as consumers save for their futures causing excess capacity and a massive reduction in overall global trade. This will also cause destruction of jobs up and down the food chain and in numerous industries. There will be fewer cars made, less demand for financial service jobs and a very slow recovery in housing construction. Overall, as we consume less there will be a need for fewer jobs to make "stuff."

Interestingly, the rules of the game are being changed as we go along. General Growth, the largest operator of malls, filed for bankruptcy protection and in a very controversial move took all 166 malls they operate into bankruptcy as well. General Growth was the largest issuer of Commercial Mortgage-Backed Securities (CMBS), which is how the great majority of commercial mortgages are created. The lenders thought they had direct access to the cash flow of the malls. Some of those malls are quite profitable and thus the lenders are very secure. With the filing of all 166 properties, money from the profitable properties will go towards the unprofitable properties possibly forcing all lenders to share in the loss which basically renders their mortgage unsecured. Imagine if a lender doesn't have confidence in their secured loan. Will they ever lend again?

Lastly, shame on the banks. They borrow billions in taxpayer dollars in times of need and now want to repay the loans and wish to redeem the warrants that they issued in return for the loans they took out. The problem is that the value of these warrants in many cases have gone up tremendously and the taxpayer should reap the profits to help offset the losses that we will sustain elsewhere. If TARP borrowers are allowed to repay the TARP funds and redeem their warrants, the taxpayers once again end up with the short end of the stick.

As always, I will keep you posted of market events as the pot thickens. In the interim, many new lenders have entered the market to take advantage of the tremendous opportunities left behind by the exodus of the "big" lenders and the secondary market. Feel free to call or email your loan scenario for a simple review. Rates are very attractive if the request makes sense. Have a wonderful Memorial Day in our great nation.

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Your referrals are the lifeblood of our business!