



## INDEPENDENT OPINION / ANGST BETWEEN BUYERS AND SELLERS

### BID/ASK GAP BRINGS INVESTMENT SALES TO A HALT

APR 16, 2008 11:16 AM

Real estate brokers had hoped the steep decline in investment sales of retail properties in the last quarter of 2007 was a temporary setback. Now it's well into the second quarter of 2008 and little has changed.

In February, the volume of investment sales in the retail sector was a paltry \$1.1 billion, according to data recently released by Real Capital Analytics, **an 88 percent drop from a year ago**. The figure was also down from January 2008, by 55 percent. At the same time, the ratio of new listings to closings rose, to 4-to-1 in February, from 2-to-1 the previous month. And as there were few deals under contract in March, the figures aren't likely to improve.

The credit crunch caused the initial drop-off. Highly leveraged buyers that previously dominated the market can no longer get financing and have exited the scene.

But there's more at work. A rift has emerged between buyers and sellers. Sellers have moderated their expectations to some degree, as evidenced by rising cap rates, especially on class-B and class-C assets. The problem, industry observer's note, is that not enough of them have done so. Special services firms and institutional sellers understand that they might have to accept discounts. But almost every private investor with a property on offer has to be counseled about the changes that have taken place in the market since last summer, says Stephannie Mower, executive vice president and managing director of investment services with PM Realty Group, a Houston-based real estate services firm.

A lack of clarity on appropriate pricing levels might be partly to blame. Real Capital Analytics reports that from June of 2007 to March 2008, average cap rates on retail properties moved by 30 basis points, to 6.9 percent. But the firm's managing director Dan Fasulo has told our sister publication the *National Real Estate Investor* the numbers are skewed because they are limited to price increases on the best assets, the only kind that has been trading hands in the past few months.

Faced with a lack of reliable statistics, sellers still expect to see cap rates in the 5 percent and low 6 percent on freestanding single-tenant properties, says Jim Koury, managing director of retail investment sales with Jones Lang LaSalle, a Chicago-based commercial real estate services firm, while buyers tend to look closer to 6.5 percent and 7 percent. With multi-tenant shopping centers, sellers tend to be as much as 50 basis points off the average 7 percent cap rate.

That has affected transaction volume. When private investors find out they'll have to accept a discount, in about 20 percent of cases, they decide not to go through with the sale, according to Mower. "Many of them bought these assets in the past five years and still expect to get an unbelievable return on their investment," she says.

Stonemar Properties, a New York City-based real estate investment firm that plans to buy up to \$150 million worth of centers this year, is under contract for only one acquisition so far, a 180,000-square-foot property in Northeastern United States that features a \$29.5 million price tag and a cap rate in the mid-7 percent. The slow start to the year has been due both to the difficulty of finding appropriately priced assets and the reluctance on the part of many sellers to bring their properties to market during a down period, says Jonathan Gould, CEO of Stonemar.

"I think sellers' expectations have lowered, but they have not lowered enough," Gould notes. "But there is a lot less wheeling and dealing going on in general. The number of properties available for sale is down substantially compared to last year."

Meanwhile, with so few deals in progress, even experienced brokers can find themselves at a loss how to value new offerings. In more than 20 percent of transactions, the listing price is lowered by an average of 5 percent, says Mower.

In one listing handled by brokerage firm Sperry Van Ness, a Wal-Mart-anchored shopping center in a tertiary market in the Midwest remained on offer for almost 60 days without getting much interest, recalls Joseph French, national director of retail properties with the firm. With cap rates for similar properties averaging 7 percent in the past six months, the firm's brokers figured a 9 percent rate would guarantee a flood of bidders. Sperry Van Ness ended up having to raise the rate to 10 percent to generate offers.

"In a different market, we would have sold that very quickly and probably at a different cap rate," French says. "But what's happened is buyers have more options and they are more cautious. If they don't get one property, they just go to the next."

Sellers should expect cap rates to climb another 25 basis points to 50 basis points before the market hits bottom, according to Koury. Mower predicts that prices will drop another 5 percent to 10 percent.

-- Elaine Misonzhnik