

The 2008 Commercial Real Estate and Real Estate Security Outlook: U.S., U.K. and Euro-Zone

November 27, 2007

Brian P. Lancaster

Head of Structured Products

Research

704-715-1864 212-214-5135

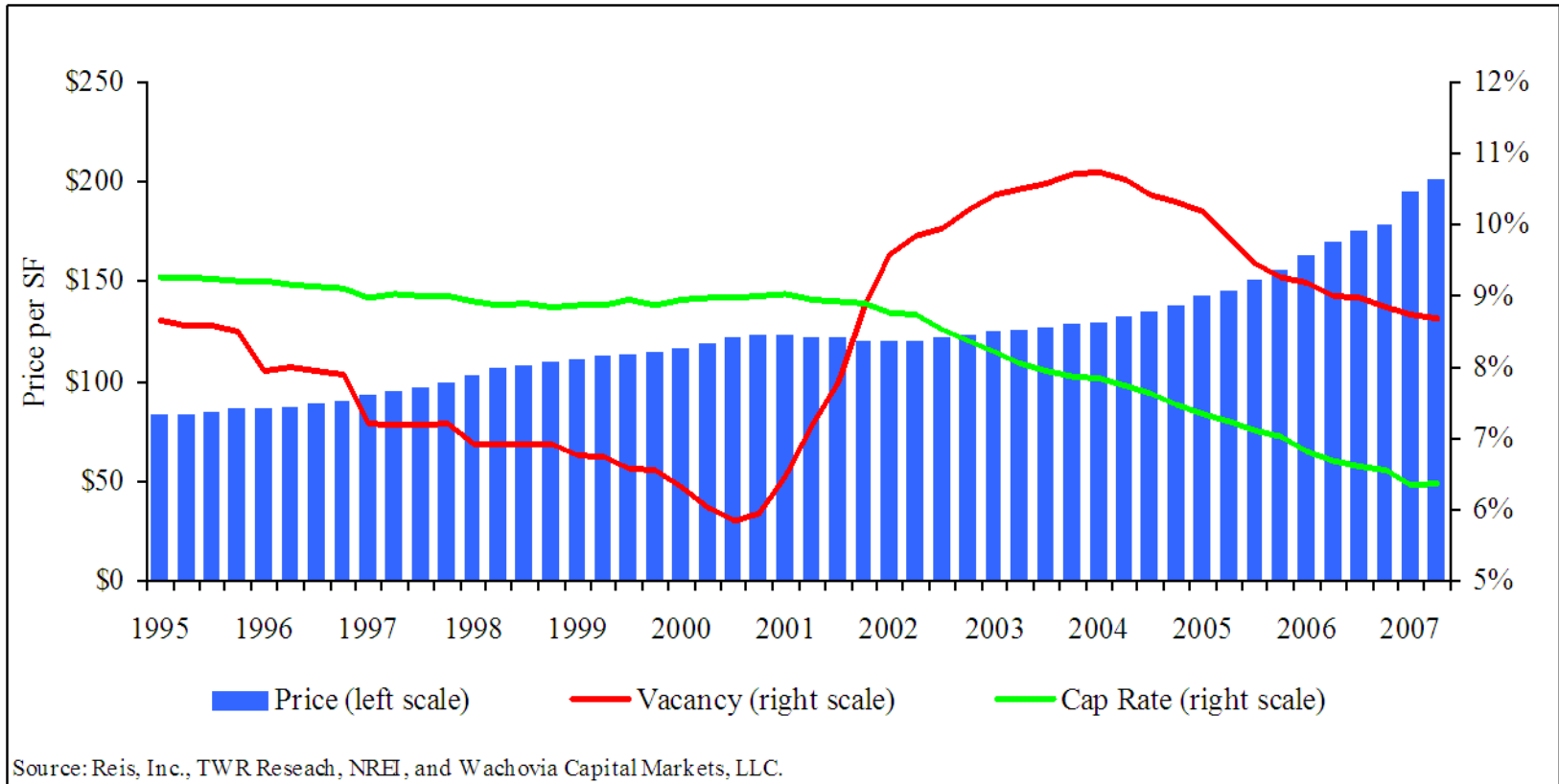
brian.lancaster@wachovia.com



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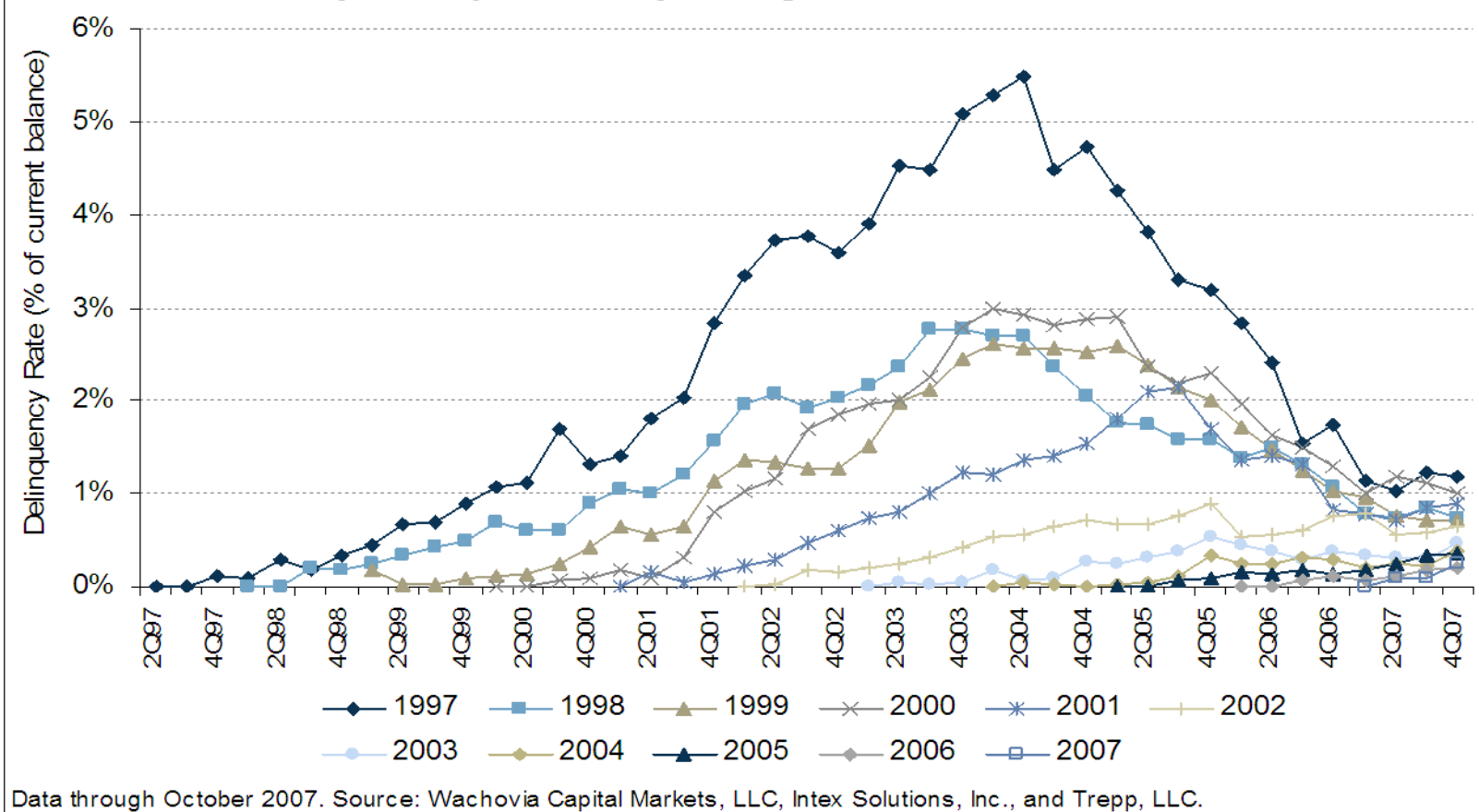
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U.S. Property Value Trends



- Plentiful liquidity pulled down cap and interest rates and helped offset deteriorating CRE fundamentals from the dot com crash and 9/11 until 2004.
- In 2004 the fundamentals also turned positive creating a “perfect positive storm” in CRE boosting CRE prices until the summer of 2007.

30+ Day Delinquencies by Vintage - CMBS Fixed Rate Deals



▪ This “perfect positive storm” brought U.S. CMBS, bank and life ins. co. CRE delinquencies to lowest historic levels (0.35%) causing U.S. CMBS defeasance and rating agency upgrades to soar.

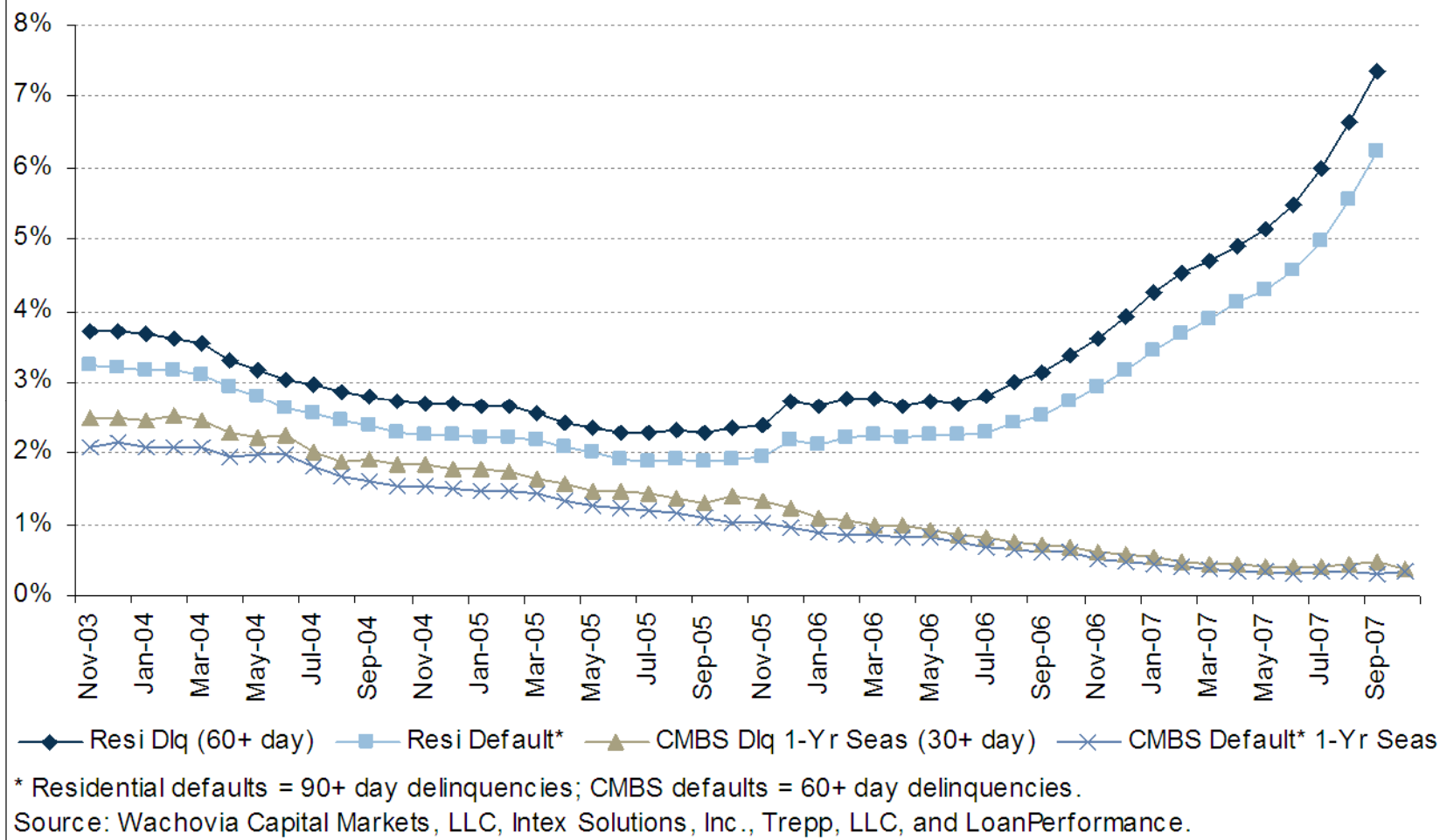
U.S. CMBS Rating Actions by Rating Agency

Year of Rating Action	Fitch			Moody's			S & P		
	Upgrade	Downgrade	U/D Ratio	Upgrade	Downgrade	U/D Ratio	Upgrade	Downgrade	U/D Ratio
1997	-	-	-	25	3	8.3	9	7	1.3
1998	-	-	-	56	8	7.0	39	7	5.6
1999	149	10	14.9	98	12	8.2	64	5	12.8
2000	229	26	8.8	91	19	4.8	88	22	4.0
2001	345	15	23.0	134	35	3.8	174	62	2.8
2002	374	125	3.0	57	190	-3.3	132	178	-1.3
2003	441	142	3.1	183	172	1.1	301	215	1.4
2004	623	108	5.8	290	204	1.4	508	164	3.1
2005	677	32	21.2	675	143	4.7	957	117	8.2
2006	1781	52	34.3	1120	116	9.7	889	116	7.7
2007 Q3	630	22	28.6	635	60	10.6	418	52	8.0
Total	5249	532	9.9	3364	962	3.5	3579	945	3.8

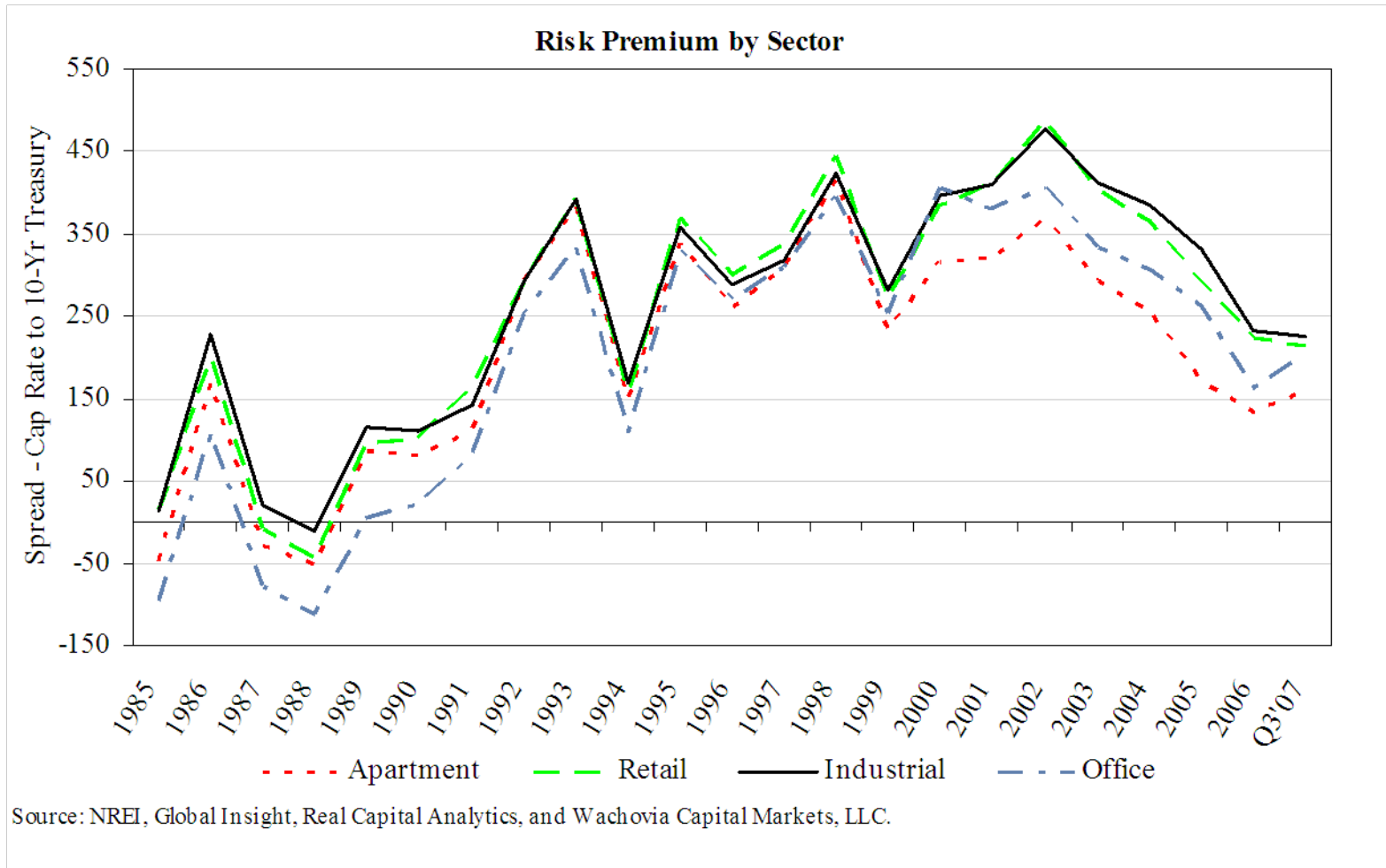
Source: Fitch, S&P, and Moody's.

- This “perfect positive storm” brought U.S. CMBS, bank and life ins. co. CRE delinquencies to lowest historic levels (0.35%) causing CMBS defeasance and rating agency upgrades to soar.

Residential and CMBS Delinquency and Default Rates

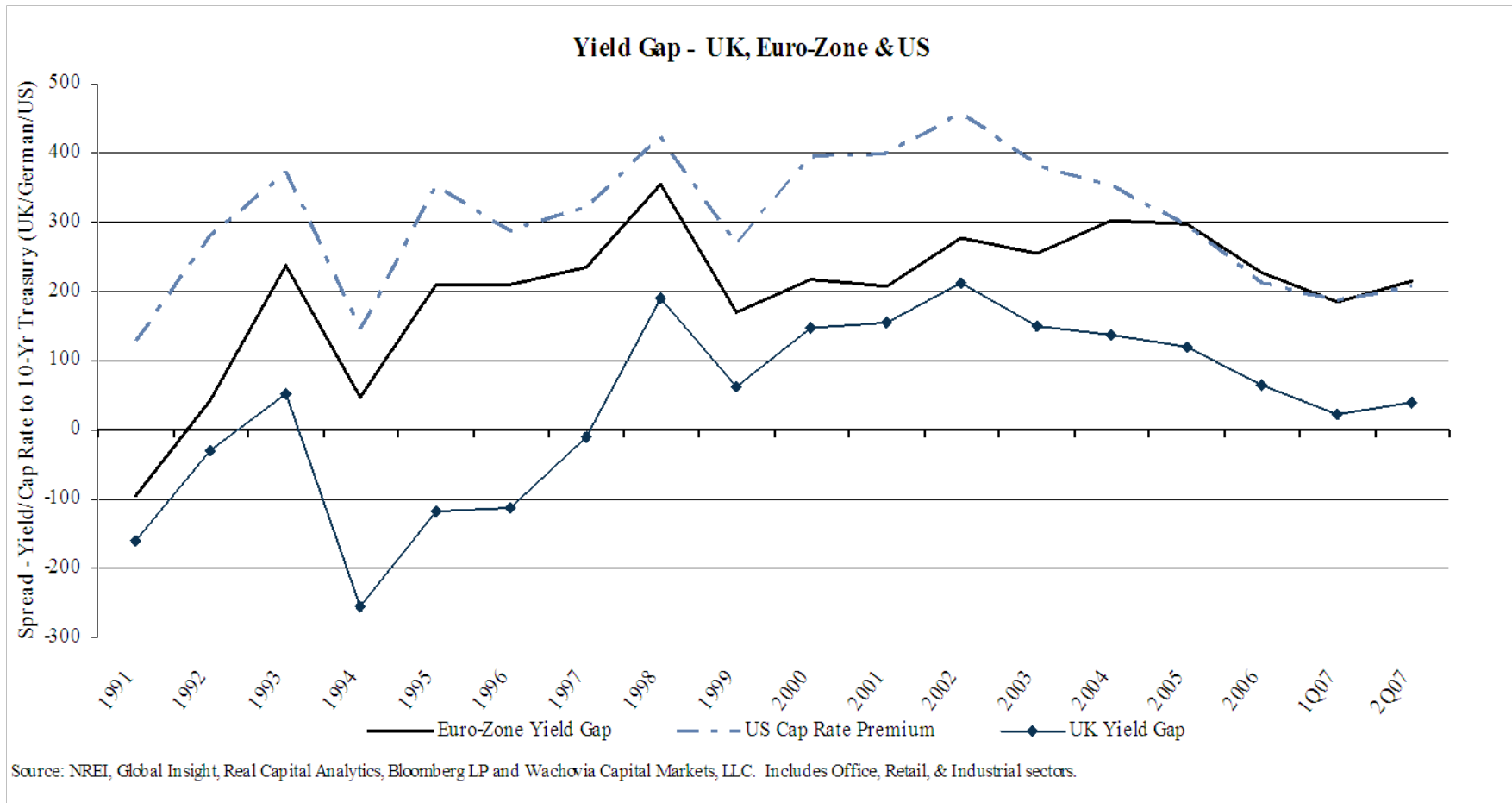


- A performance in marked contrast to the U.S. RMBS market.



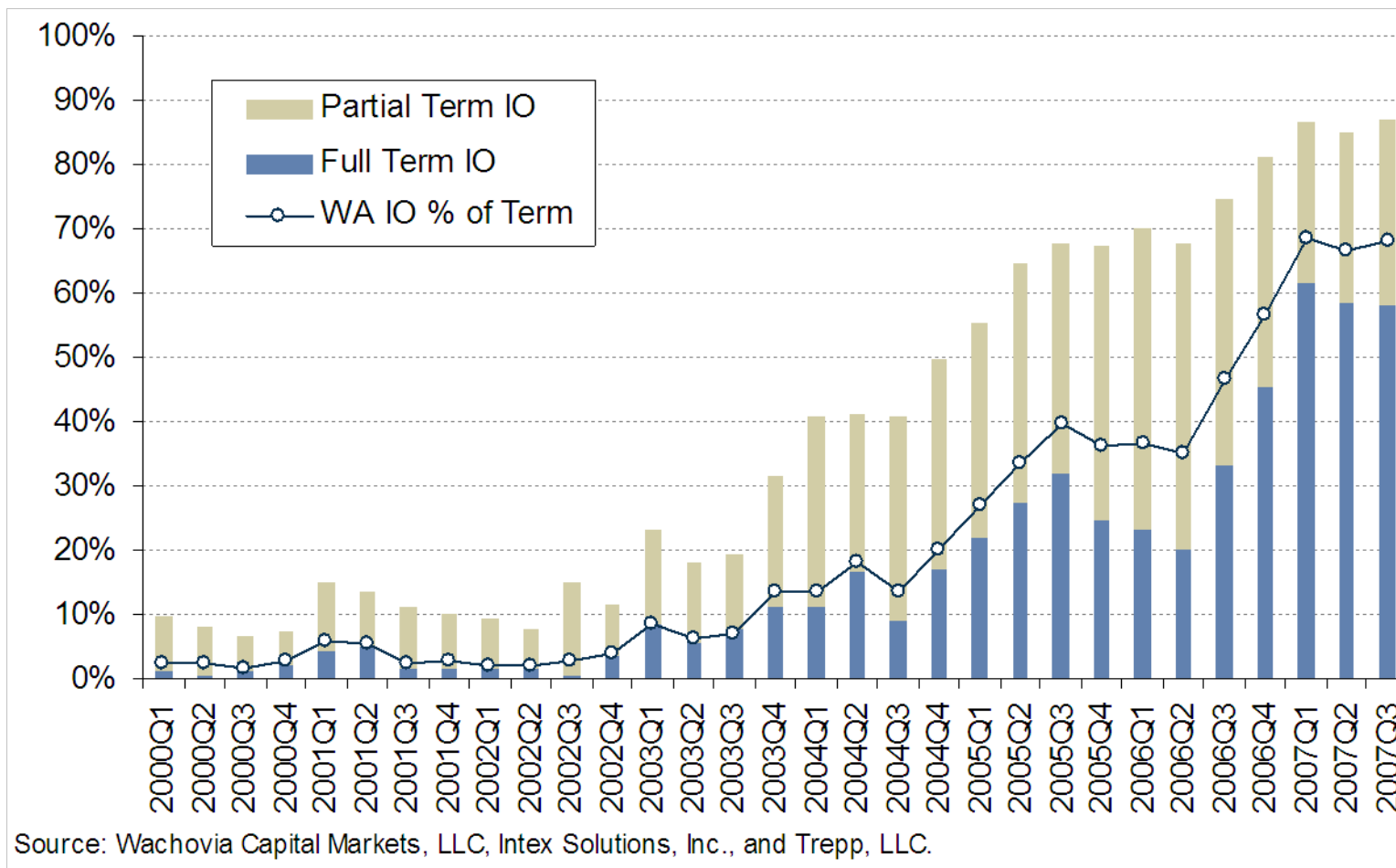
- Strong credit performance, plentiful liquidity and rising prices reduced U.S. CRE risk premiums increasing the likelihood of a rise in U.S. cap (“yields”) rates.

Strong Property Valuations in the U.S., U.K. and Eurozone: A Similar Tale

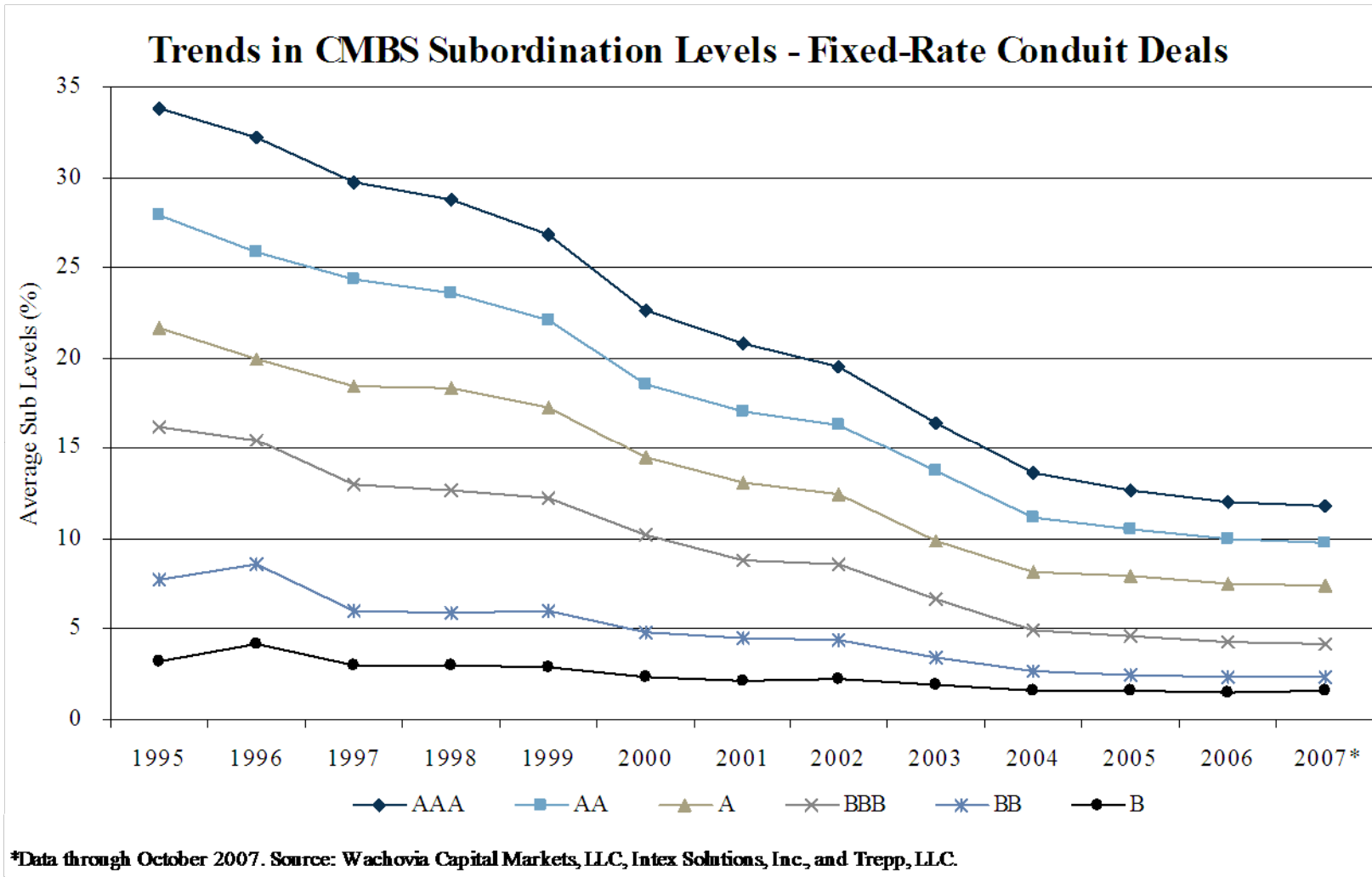


- The story is fairly much the same in the Euro-zone and United Kingdom.

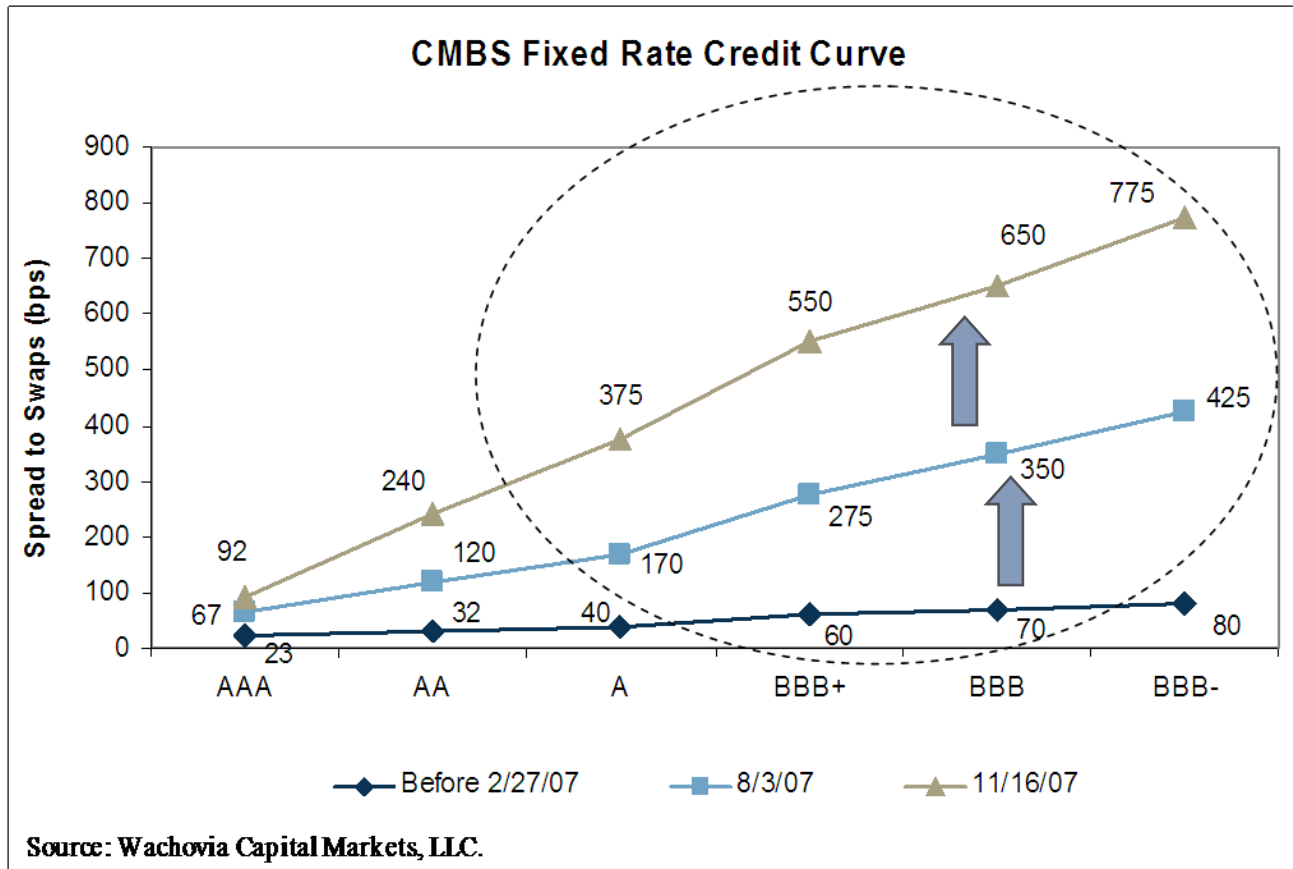
U.S. CMBS Underwriting Standards Declined—Increased IO%



■ Underwriting standards were pushed...



- And rating agency credit enhancement levels decreased.



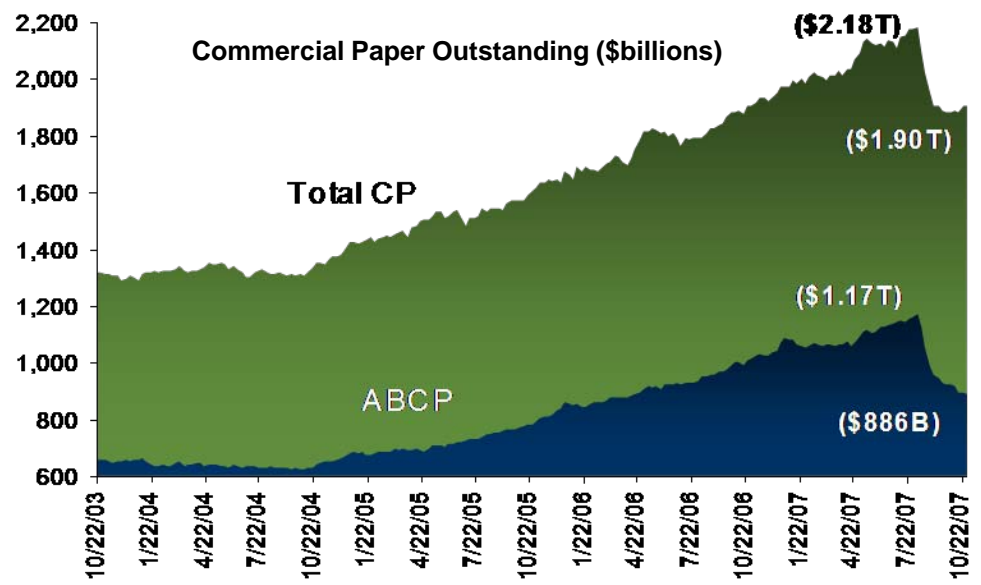
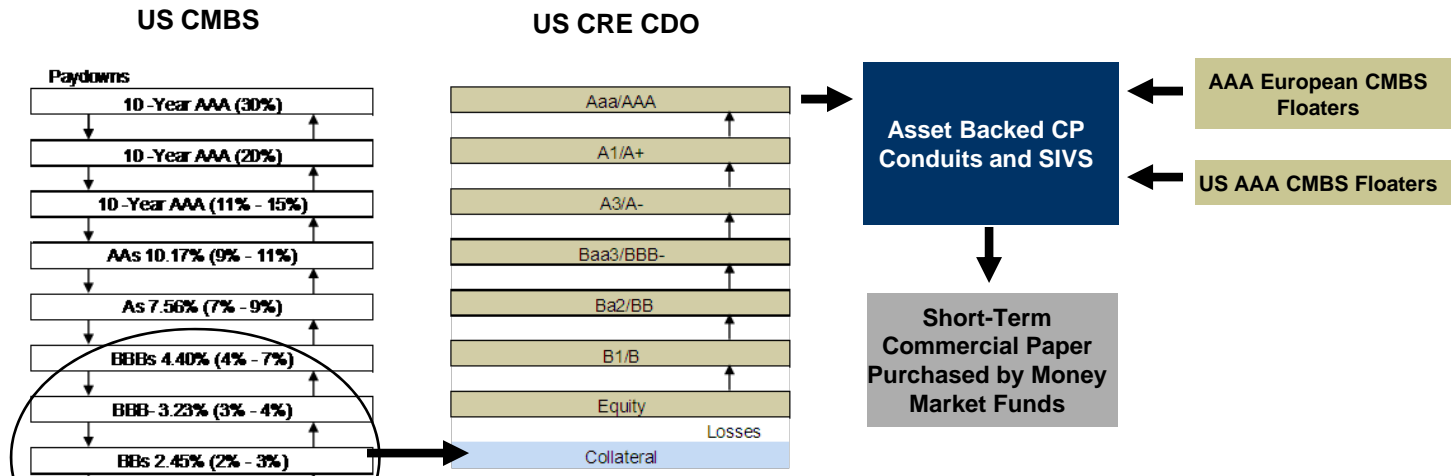
- The subprime induced credit crunch heightened investor credit concerns, reducing U.S. fixed rate CMBS demand, increased CMBS spreads and spread volatility and steepened the CMBS credit curve.

Impact of ABCP/SIV Collapse on CRE Financing

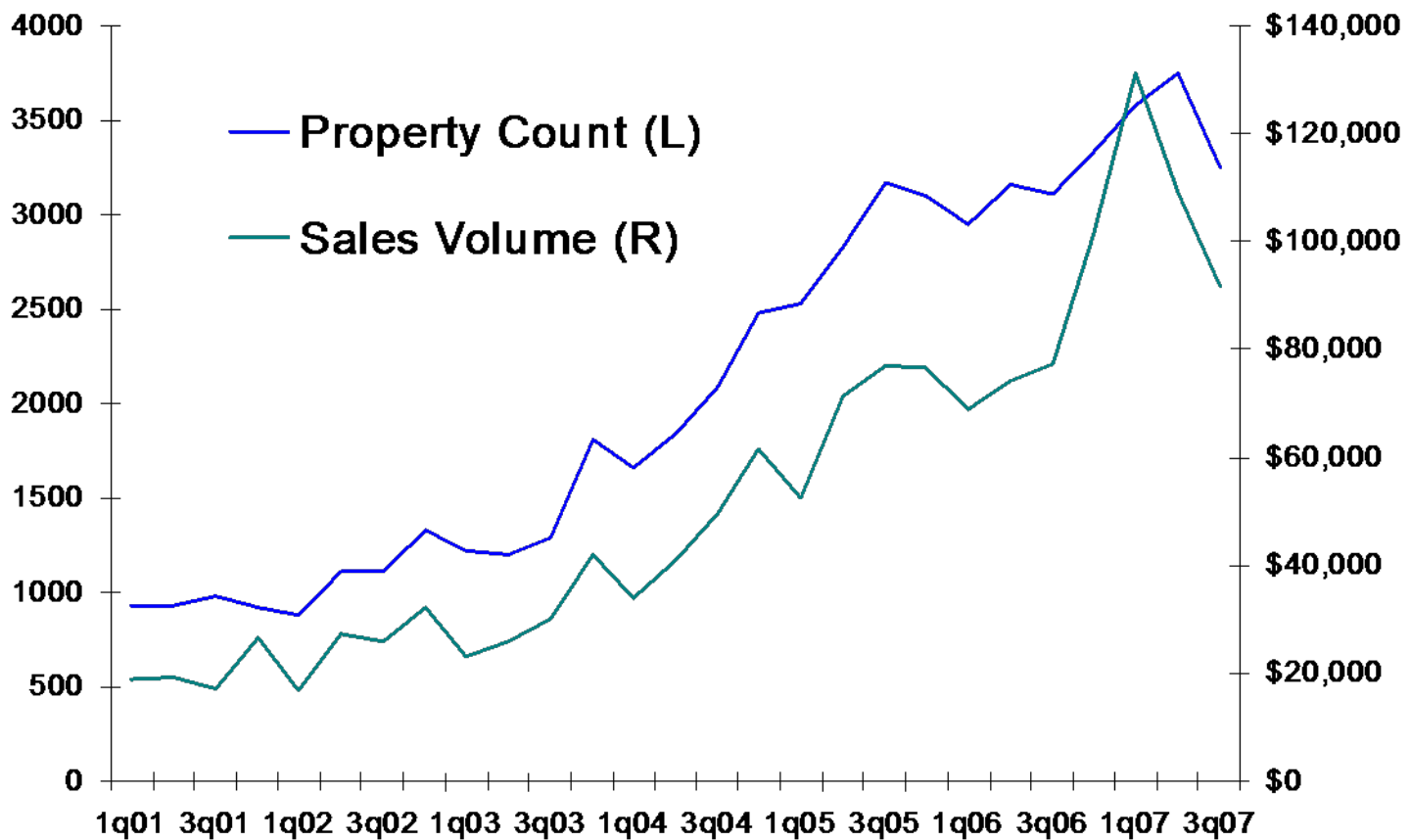
The collapse of the ABCP/SIV market also increased CRE borrowing costs in the U.S. and Europe by shutting down both the European and U.S. CMBS floater and CRE CDO markets.

In the U.S. CRE CDOs had financed/purchased mezzanine and B-piece CMBS caused the CMBS credit curve to steepen increasing borrower costs as well.

The closure of the CRE CDO markets has also increased B-note and mezz loan borrowing costs reducing the prices buyers will pay for CRE properties.



U.S. Commercial Real Estate Transaction Volume



Source: Wachovia Capital Markets, LLC, REIS, Inc., TWR Research, Smith Travel Research, Real Capital Analytics.

Originators have in turn reduced originations by 80%, leverage by 5% to 10% and increased borrowing costs from 50 bps to 225 bps over swaps currently. These tighter credit conditions are pushing U.S. transaction volume down...

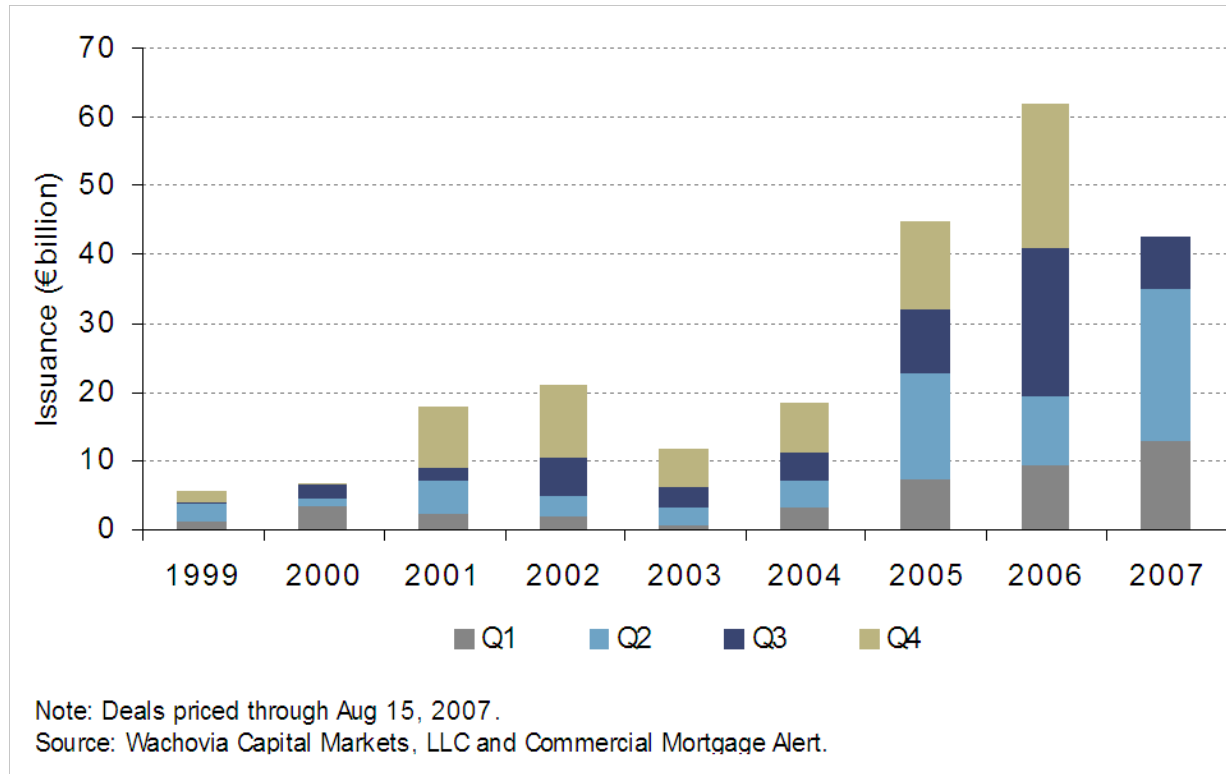
REIT Implied Change In U.S Commercial Property Values

Sector	Early	Early	11/02/07 Current	% Change In Equity Value			Assumed Sector Ave. Leverage	Implied Change In Prop. Value	Estimated Peak Cap Rate	Implied Forecasted Cap Rate	Forecast Change In Fwd Cap Rates
	Feb-07 High	Aug-07 Low		Peak to Trough	Trough To Current	Peak to Current					
Equity REITs	295.8	210.1	217.7	(29%)	4%	(26%)	50%	(13%)	5.65%	6.40%	75 bps
Large Cap	345.3	243.5	253.7	(29%)	4%	(27%)	50%	(13%)	5.25%	5.95%	70 bps
Small Cap	209.6	164.0	159.1	(22%)	(3%)	(24%)	50%	(12%)	6.50%	7.28%	78 bps
Retail	610.4	428.6	461.3	(30%)	8%	(24%)	50%	(12%)	6.00%	6.73%	73 bps
- Strip Centers	337.9	243.6	261.3	(28%)	7%	(23%)	50%	(11%)	5.75%	6.40%	65 bps
- Malls	505.9	346.5	374.7	(32%)	8%	(26%)	60%	(10%)	5.75%	6.35%	60 bps
Office	471.9	324.1	326.8	(31%)	1%	(31%)	50%	(15%)	4.75%	5.48%	73 bps
Warehouse	519.0	376.7	480.3	(27%)	27%	(7%)	50%	(4%)	6.25%	6.48%	23 bps
Hotels	147.0	111.6	106.2	(24%)	(5%)	(28%)	55%	(12%)	7.50%	8.44%	94 bps
Self-Storage	568.5	335.5	366.8	(41%)	9%	(35%)	50%	(18%)	6.50%	7.65%	115 bps
Diversified	251.8	174.3	172.4	(31%)	(1%)	(32%)	50%	(16%)	6.00%	6.95%	95 bps
Avg.	383.7	267.0	292.4	(29%)	8%	(24%)		(11%)	5.80%	6.47%	68 bps

Source: Bloomberg, Wachovia Capital Markets, LLC estimates

- and are likely to push U.S. cap rates up by 50bps and prices down by to 10%.
- Secondary and tertiary markets likely to be more greatly impacted.

European CMBS Issuance – A Similar Experience

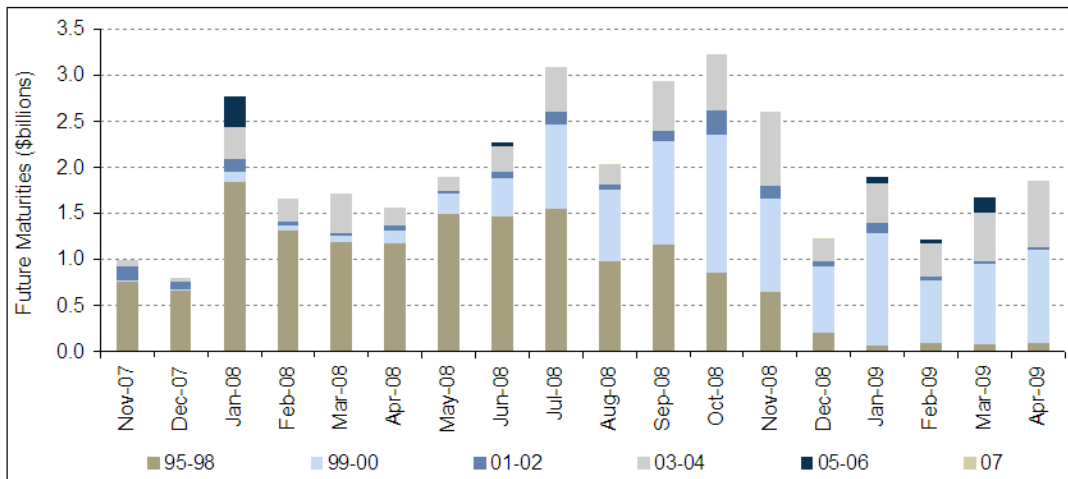


- No CMBS transactions priced in Europe since early August. (Two are currently being marketed).
- A number of deals have been pulled, gone radio silent or entered periods of “extended marketing.” Underwriters are showing a preference to hold collateral rather than “giving away” loans.
- New issue collateral still reflects early 2007 underwriting
- Future transaction structures may be required to simplify. As complex pro rata structures, separate loan buckets, etc. may be more difficult to market.

- In the U.K. and Euro-zone, the occupational market is holding in, with no significant increases in vacancies and delinquencies yet...
- Nonetheless, **tightening lending standards and higher loan margins in the U.K. and Euro-zone will likely give way to a decline in property values over the next 12 months.**
- Although the impact in the Euro-zone may be less than in the U.S. since CMBS and CRE CDOs are a smaller percent of Euro-zone CRE finance.
- The U.K.? While CMBS and CRE CDOs are smaller part of U.K. CRE finance, yield compression looks even greater than in the U.S. or Euro-zone.
- We are already seeing “yields” rise in the United Kingdom.
- CMBS severities in the U.S., Euro-zone and U.K. are all likely to increase.

Future Maturities by Deal Vintage - Fixed-Rate Conduit/Fusion Deals (\$billions)

Month	1995-1998	1999	2000	2001	2002	2003	2004	2005	2006	2007	TOTALS
Nov-07	0.76	0.01	-	-	0.15	0.08	-	-	-	-	1.00
Dec-07	0.66	0.01	-	0.08	0.01	0.03	0.00	-	-	-	0.79
Jan-08	1.85	0.10	0.01	0.13	-	0.28	0.06	0.34	-	-	2.77
Feb-08	1.31	0.05	0.01	0.03	0.00	0.25	-	-	-	-	1.66
Mar-08	1.18	0.04	0.03	0.03	-	0.32	0.12	-	-	-	1.72
Apr-08	1.17	0.12	0.02	0.01	0.03	0.17	0.02	-	-	0.01	1.57
May-08	1.49	0.21	0.02	0.02	-	0.15	-	-	-	-	1.89
Jun-08	1.47	0.35	0.06	0.07	0.01	0.24	0.04	0.04	-	-	2.28
Jul-08	1.55	0.80	0.11	0.13	0.02	0.35	0.14	0.00	-	-	3.09
Aug-08	0.97	0.68	0.11	0.04	0.01	0.17	0.04	-	-	0.01	2.04
Sep-08	1.16	0.97	0.16	0.05	0.05	0.26	0.29	-	-	-	2.93
Oct-08	0.85	1.43	0.08	0.05	0.21	0.48	0.13	-	-	-	3.23
Nov-08	0.65	0.92	0.09	0.10	0.04	0.31	0.50	-	-	-	2.61
Dec-08	0.20	0.69	0.03	0.03	0.02	0.06	0.18	0.00	-	0.02	1.24
Jan-09	0.06	1.15	0.08	0.06	0.04	0.01	0.43	0.07	-	-	1.90
Feb-09	0.09	0.66	0.02	0.00	0.03	0.02	0.34	0.04	0.00	-	1.22
Mar-09	0.08	0.82	0.06	0.00	0.02	-	0.52	0.17	-	-	1.67
Apr-09	0.09	0.92	0.10	0.02	0.01	0.05	0.67	-	-	-	1.85
TOTALS	15.57	9.92	0.98	0.87	0.66	3.24	3.48	0.67	0.00	0.04	35.44



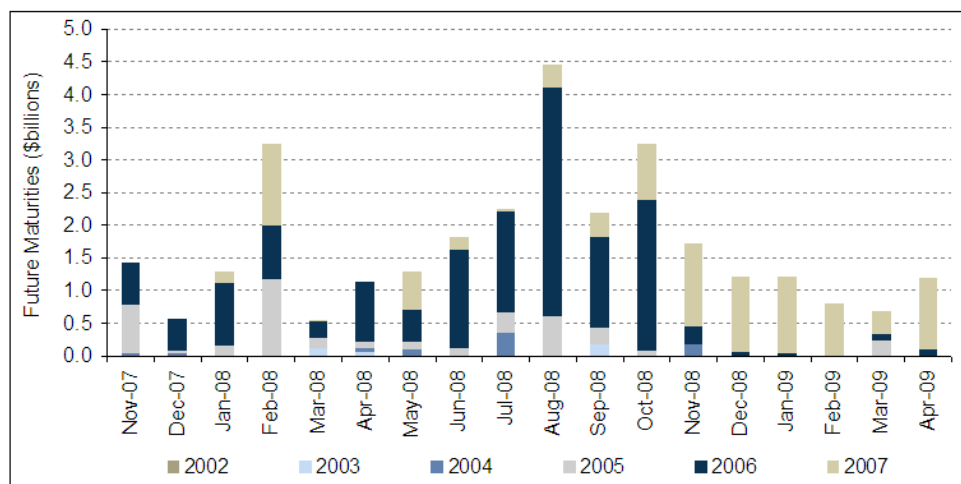
- Extension risk and refinancing risk are greater particularly for short term loans that have been recently originated.
- However, most U.S. fixed rate conduit loans coming due have significant seasoning and equity buildup.

Sources: Wachovia Capital Markets, LLC, Intex Solutions, Inc., Trepp, LLC.

Future Maturities by Deal Vintage - Large-Loan Floating-Rate Deals (\$billions)

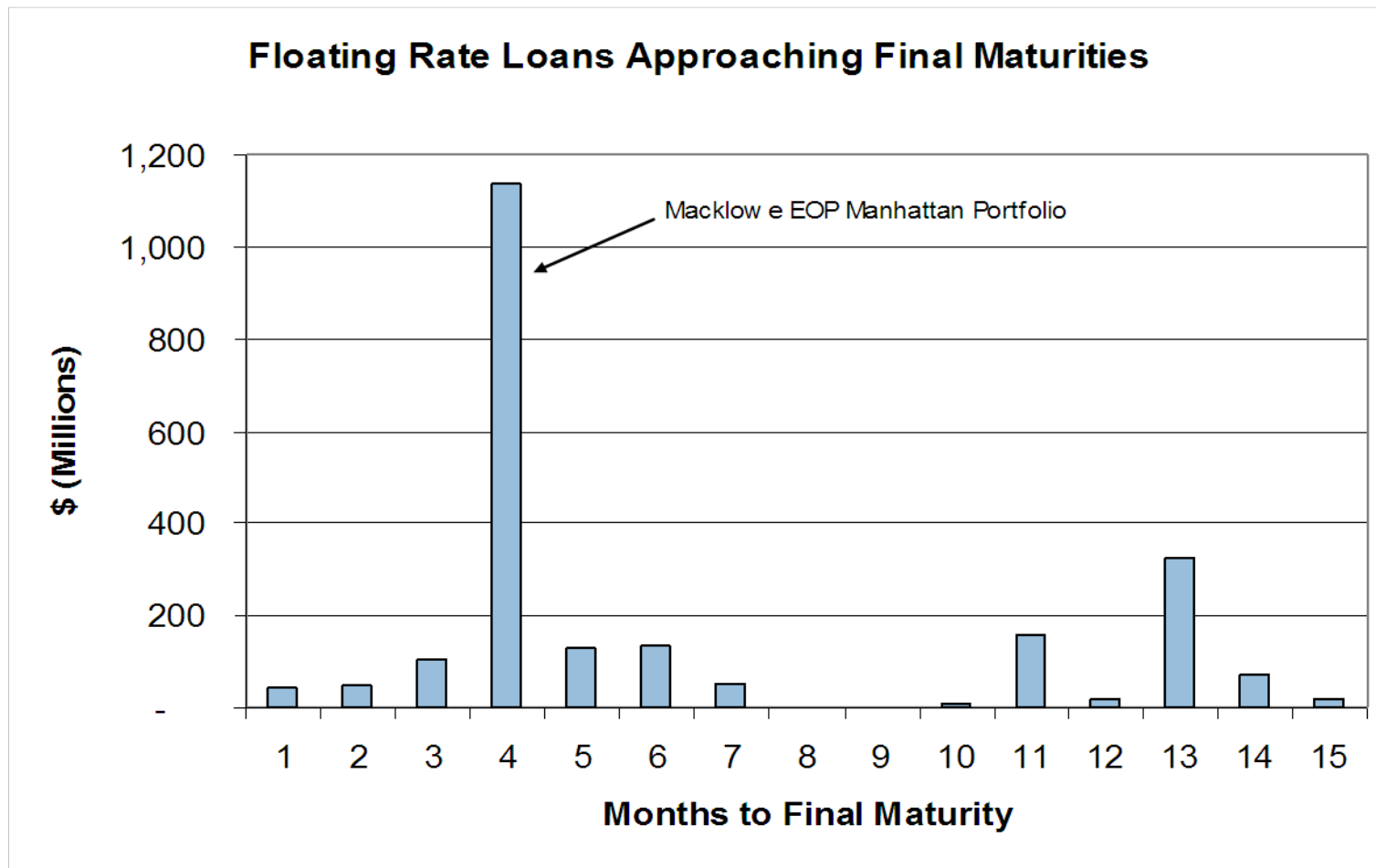
Month	2002	2003	2004	2005	2006	2007	TOTALS
Nov-07	-	-	0.04	0.75	0.65	-	1.44
Dec-07	-	-	0.04	0.04	0.48	-	0.56
Jan-08	-	-	-	0.17	0.95	0.17	1.28
Feb-08	-	-	-	1.17	0.84	1.25	3.25
Mar-08	-	0.13	-	0.14	0.26	0.02	0.55
Apr-08	-	0.06	0.05	0.11	0.90	-	1.13
May-08	-	-	0.10	0.13	0.47	0.60	1.30
Jun-08	-	-	-	0.13	1.49	0.20	1.83
Jul-08	-	-	0.35	0.33	1.53	0.05	2.25
Aug-08	-	-	0.01	0.61	3.50	0.35	4.46
Sep-08	-	0.17	-	0.27	1.39	0.37	2.20
Oct-08	-	-	-	0.08	2.31	0.86	3.25
Nov-08	-	-	0.17	-	0.28	1.27	1.72
Dec-08	-	-	-	-	0.05	1.17	1.22
Jan-09	-	-	-	-	0.04	1.17	1.22
Feb-09	-	-	-	-	0.01	0.80	0.81
Mar-09	-	-	-	0.23	0.10	0.36	0.69
Apr-09	-	-	-	-	0.11	1.09	1.20
TOTALS	-	0.36	0.75	4.17	15.36	9.73	30.37

• There are some U.S. floating rate loans, originated in the last year, that are coming due that could possibly extend although most can extend without defaulting.



Sources: Wachovia Capital Markets, LLC, Intex Solutions, Inc., Trepp, LLC.

U.S. Floating Rate Loans Up for Refinancing (no more extensions available)



- However there is headline risk as the large U.S. Macklowe EOP Manhattan portfolio is approaching final maturity and could default by February.

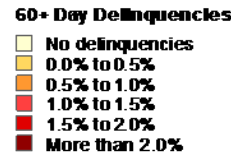
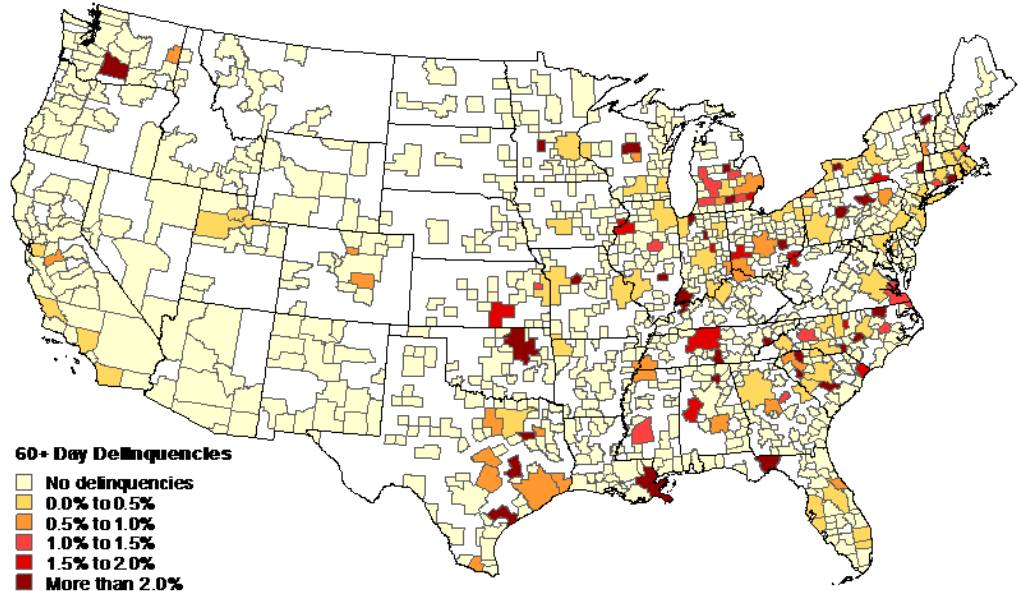
Strong Fundamentals are Likely to Suppress Rising Term Defaults in the U.S.

- We expect CMBS and on-balance sheet CRE loan defaults to gradually increase in 2008 due to heightened refinancing risk and weaker underwriting in 2006 and 2007 vintages.
- With cap rates set to rise, CRE fundamentals are key to credit performance. Fortunately 94% of the 200 CRE markets we forecast (18 mos.) are stable or growth markets which should temper credit deterioration.

▪ Cumulative 10 yr CMBS loan loss rate should rise from 2% to at least 3% to 4%.

Delinquencies - CMBS Fixed-Rate Deals

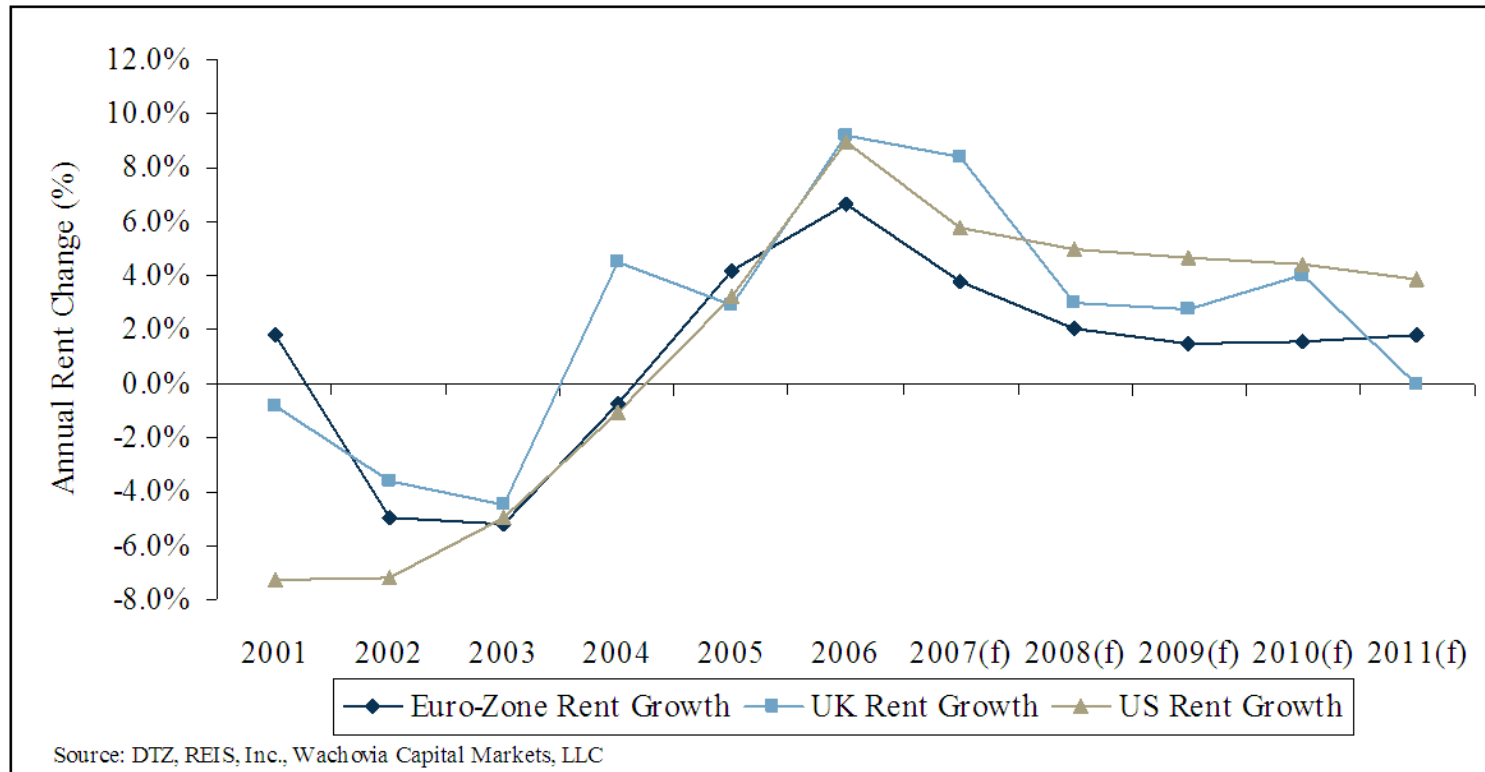
60+ Day Delinquencies by CBSA



Comparison of CRE Fundamental Forecast Results

Sector	Previous Forecast (Q1 2007)						Current Forecast (Q3 2007)					
	Effective Revenue	Effective Revenue	Overall Rating	No. of Metros with Revenue			Effective Revenue	Effective Revenue	Overall Rating	No. of Metros with Revenue		
	2007 F	2008 F		Declining	Stable	Growing	2007 F	2008 F		Declining	Stable	Growing
Apartment	3.4%	3.1%	Growth	1	19	34	3.1%	2.9%	Growth	3	27	23
Industrial	3.8%	3.5%	Growth	4	12	27	3.6%	2.8%	Growth	5	17	21
Office	7.0%	4.6%	Growth	1	14	39	7.0%	4.4%	Growth	2	23	28
Retail Shopping Centers	2.5%	2.4%	Growth	1	26	24	2.2%	2.1%	Stable	3	34	14
Hotel	5%-7%	3%-5%	Growth	NA	NA	NA	5%-7%	3%-5%	Growth	NA	NA	NA
Totals / Averages	4.5%	3.5%		7	71	124	4.4%	3.2%		13	101	86

And in the U.K. and Euro-zone: Historic and Forecast Office Rent Growth



- In addition, U.S., U.K. and Euro-zone office rent growth while all are likely to slow all are likely to remain positive thru 2010 **helping suppress term defaults.**
- U.S. office rent growth will continue to exceed Euro-zone rent growth and likely begin to overtake U.K. rent growth in 2008.

The Other Good News: Most of this if Not a Lot More is Already Priced in

Vintage Base For Loss Distribution	CMBX.3					Historical Assumptions / Break Even (Fair Value) Spreads			Beyond Scenarios
	Class	Coupon (bps)	Mid Trading Spreads as of 11/19/07 (bps)			Decreasing	Severity of Stress	Increasing	
			Low	Current	High	2.0*Defaults Severity +10%	2.5*Defaults Severity +10%	3.0*Defaults Severity +10%	
1996	AAA(30%)	8	6.4	79.1	79.1	no losses	no losses	no losses	
1998	AAA(30%)	8	6.4	79.1	79.1	no losses	no losses	no losses	
1996	AA	27	24.7	340.6	340.6	97.8	121.4	158.4	•
1998	AA	27	24.7	340.6	340.6	116.6	155.4	224.9	•
1996	A	62	50.0	433.8	506.3	123.1	180.1	249.9	•
1998	A	62	50.0	433.8	506.3	192.5	257.6	334.6	•
1996	BBB	200	145.0	783.8	798.7	404.9	614.1	817.5	•
1998	BBB	200	145.0	783.8	798.7	440.1	579.8	714.8	•
1996	BBB-	320	245.5	1,076.6	1,076.6	685.8	889.1	1,003.6	•
1998	BBB-	320	245.5	1,076.6	1,076.6	621.0	820.4	1,026.1	•
1996	BB	500	477.5	1,515.6	1,515.6	982.1	1,118.4	1,241.4	•
1998	BB	500	477.5	1,515.6	1,515.6	988.6	1,164.7	1,469.3	•

Source: Wachovia Capital Markets, LLC

* Means no writedowns to any underlying tranches under the scenario.

—shows approximately where the 11/19/07 traded spread falls within or between the scenarios.

- Current spread levels imply future default rates that are three to four times historic levels potentially creating opportunities!

The Bad News:

- U.S., U.K. and Euro-zone Commercial Real Estate Property values are all likely to come under pressure in 2008 because of the deterioration in the structured finance markets with cap rates/yields likely to rise.
- Commercial real estate security severities are likely to increase.
- Greatest risk is refinance or extension risk in CMBS floating rate securities.

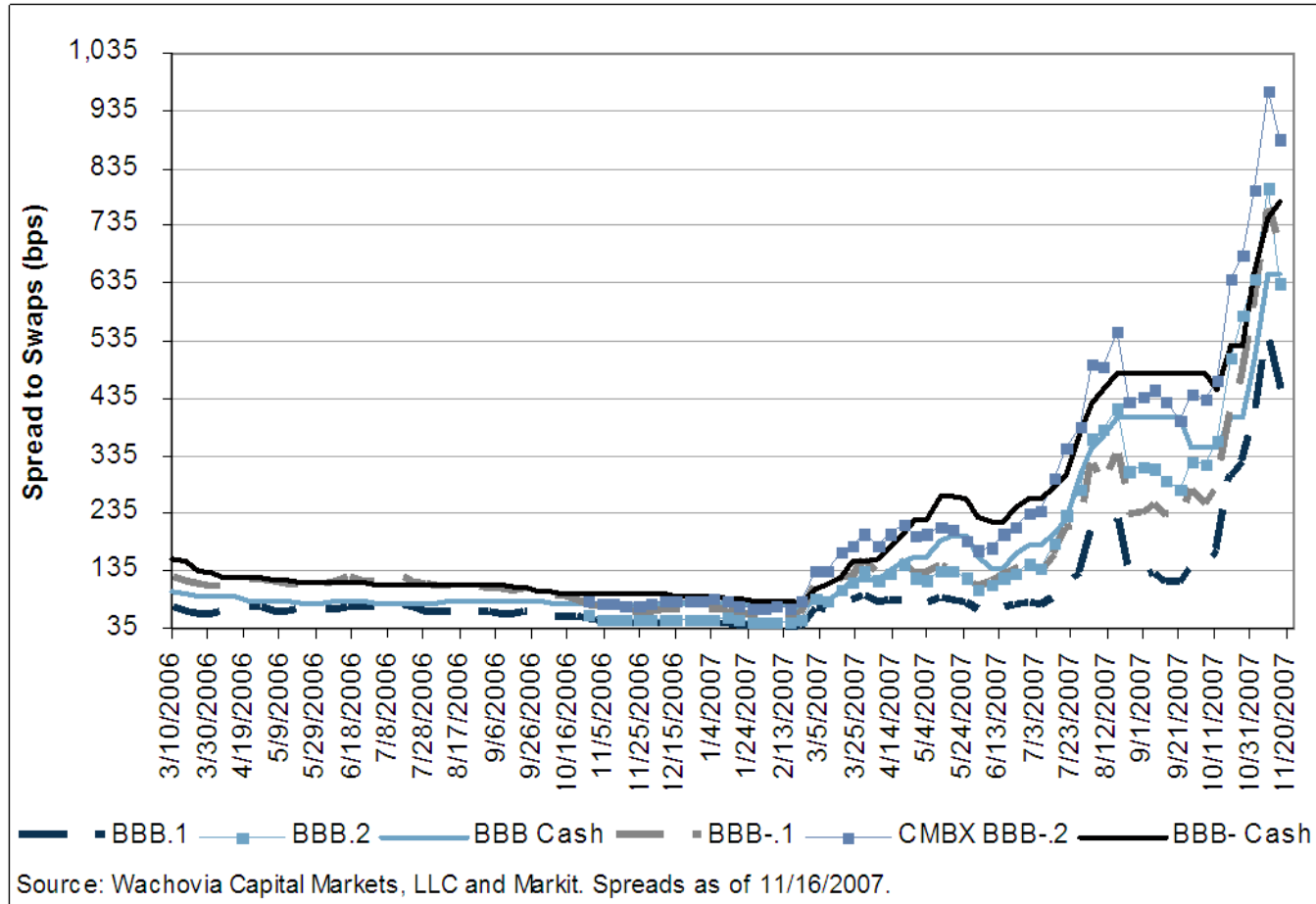
The Good News:

- Fortunately most of these in the U.S. may be extended. However the Macklowe portfolio at a maximum extension and could pose headline risk.
- Strong but weakening commercial real estate fundamentals are likely to suppress a significant rise in term defaults.
- In the U.S. 3 to 4 times the historic default level and 10% greater severities are already priced in creating potential opportunities.



- **Appendix**

CMBS and CMBX BBB & BBB- Spread Movements



Disclosure Appendix

Addition information is available on request.

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