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Jonathan Davis of The Davis Cos. speaks at SIOR breakfast event

February 12, 2009 - Spotlights

The New England Chapter of SIOR held its first breakfast event of the year at the Newton Marriott on Thursday, Jan. 2nd. The guest speaker was Jonathan Davis, CEO of The Davis Companies. Approximately 45 SIORs and guests attended this event as Davis discussed the macro issues with the nation's economy and shared his thoughts on how real estate will play a role in the recovery. Over the last 3 decades, the Davis Cos. (founded in 1976) and affiliates have acquired and developed approximately 100 properties totaling almost \$2 billion in investments. There is over \$200 million of development underway and they manage a portfolio in excess of \$4.5 million. Its most recent projects include the renovation and development of Charles River Plaza and Reservoir Woods.

Greg Klemmer, Chapter president, first welcomed the audience and thanked Jim Boudrot and Ned Leeming for organizing the event. He also announced that Bob Cleary as become the Chapter's chair of admissions while Garry Holmes, Mark Stevens and Peter Hayes will handle chapter recruitment. Klemmer's goal is to expedite the interest of many of the younger brokers and corporates into the SIOR membership. He then introduced Jonathan Davis.

Davis began with his overview of macro economics of the U.S. starting back in the early 1990s. He felt that today we have too much housing inventory that has to be first absorbed. The number of mortgages in the U.S. with higher amounts than the value of the asset is now at 25% and that is considered high. The federal money given to banks has not stimulated the economy because banks still believe that they may have future questionable loans that might default. The banks are building up reserves with the federal monies. Davis then stated that the bad news now is that the CMBS market is shut down and trading at 1600 BPs over Treasuries with AAA rated paper. In the past the CMBS market was trading at less than 100 BP. The spread has widened enormously and this action is on AAA rated paper. Other lower rated paper is not being reviewed.

The good news is threesome. 1) There is a coordinated effort domestically today which is more efficient. 2) We have a smart President, and 3) There is a consensus from everyone on the efforts to be pursued.

Davis then went on to make the following points:

- * The U.S. has to extend answers beyond the U.S. borders with any solutions. This will take a global effort.
- * Davis has been in past recessions, but this one is different and will require a different solution. But then the other recessions were different as well. He does not know how long this recession will take, but we have a solid world system and the international financial structure is sound. There is more communications internationally and more focus with coordinated efforts with nations.
- * We will see a recovery and there will be growth but he is not sure when. He feels that this

recession will be deep and long.

Davis went on to state that \$700 billion has been spent in the TARP program and \$100-350 billion for foreclosures. The \$700 billion is equal to \$2,500 per person in the U.S. that will be spent. There has to be a lot of creativity and quickness for this program to be successful.

The Boston Impact

As Davis transitioned from macro to micro, he was very upbeat about the economy for the Boston region. As compared to other U.S. regions, Boston is relatively in good shape. Boston may have a 6% unemployment for '09, but the U.S. unemployment prediction is 9%.

Broker Opportunities

Davis then stated that there is a place in this down economy for brokers to make money. He felt that the business opportunities would be with tenant renewals. Davis has a 95% occupancy with his portfolio and tenants are not moving. But the challenge is with current vacant buildings. There is not much tenant growth and in fact a little space retraction. He is now negotiating more blended lower rental rates if the terms are extended.

The Davis Cos. Assets

Davis has 1.2 million s/f of space at Reservoir Woods in Waltham that can be built in the next 10 years. As of May '08, he has completed 180,000 s/f which is now vacant. He is just now getting some leasing activity at 10-15% lower rents than he pro forma. So he sees the economy effects but he believes the building will be full in the next 3-6 months. Overbuilding has not been significant in the Boston market in commercial real estate as it has been in other real estate sectors due to the dot.com. We just came out of the dot.com recession so there was a hold-back on further development until the extra space was absorbed. He feels going forward there will be an increase of sublet space and he sees more job creation from the federal spending. Davis could not predict the recession recovery, but stated it could be in 2010-11 or 2012.

There is a yawning gap right now between price and bids on investment sales due to the debt crisis and not due to a real estate crisis. He felt that owners' balance sheets in real estate were very sound and properties are well capitalized. Some institutional owners, however, are having struggles due to various factors such as mark to market and investors that want to be out of the real estate assets and asking for their money. But for the most part, Davis felt that commercial real estate was under-leveraged and not much vacancies. He stated that landlords should want to "blend and extend" with existing tenants.

For the future, Davis was unequivocal in stating that we will see inflation. After the next 3-4 years, as interest rates rise so will inflation and real estate will be the right asset to own to hedge against the inflation.

Conclusion

Davis wrapped up his session by stating that there is no significant amount of new development. He is focused on administering to the needs of institutions and buying up loans of financial companies as an investment that he feels are trading at 65-75% of face value. Yields are higher than imagined. He is extremely optimistic about the Boston area. With strong companies in tech such as Apple, Boston offers the top brilliant minds for that industry. Health care technology is big in Boston and for the world. We also have a dangerous world and technology is important in warfare. Boston is very well positioned for the recovery.