



Commentary

*Equity Office Properties Flips or Flops?  
Where Have They Landed?*

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*Insight beyond the rating.*

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## OVERVIEW

In the first half of 2007, Blackstone's \$39.2 billion purchase of Equity Office Properties (EOP) was the industry's hot topic. At the same time, many real estate professionals were balking at the high price it paid. Then, in Blackstone-fashion, it turned around and immediately sold many of these properties for a profit. The subsequent sales generally implied cap rates below 5% and mind-boggling prices per square foot. Today, these buyers are saddled with loads of debt, depressed real estate values and rising vacancies. If one bought a CMBS transaction in 2007, you likely have exposure to at least one loan secured by a Blackstone-EOP flipped property and you too may soon feel the consequences of these inflated prices and over-leveraged loans.

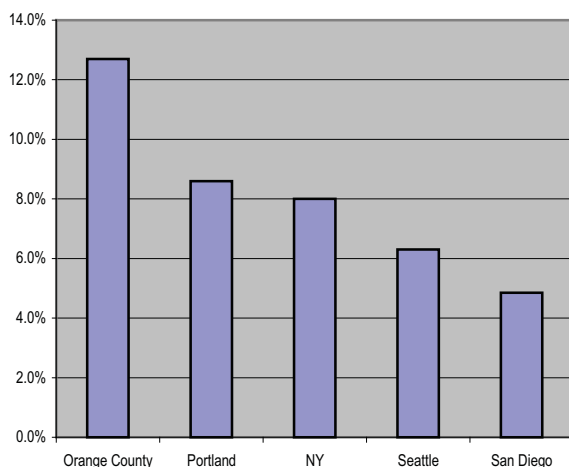
Now, nearly three years following the closing, DBRS is interested in reporting the updated performance of some of the securitized EOP-Blackstone flips. The results are simply not good. The losers are prominent real estate investors across major markets. The loans were made assuming cash flow growth and in most instances, just the opposite has occurred. It does appear that some loans will make it to maturity but all will face tremendous refinance risk.

Some highlights of the study are summarized below:

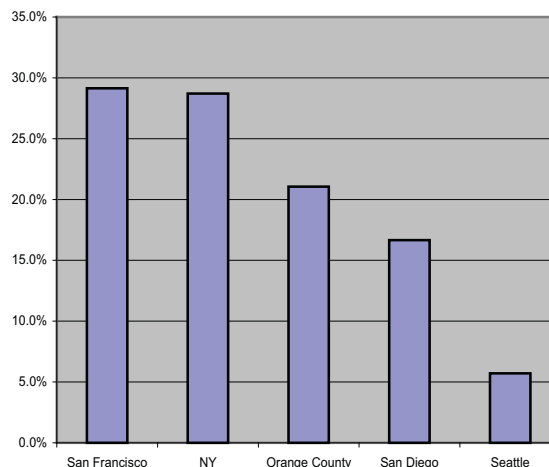
- Assuming an 8% cap rate, no loans have sponsor equity remaining.
- Two loans have experienced mezzanine loan defaults.
- Five loans are in special servicing.
- 12 loans are on the servicer's watchlist.
- No loan has achieved the underwritten pro forma net cash flow (NCF). In fact, those underwritten to projections have experienced a 37.6% NCF decline compared to the pro forma.
- For the 19 loans that reported both the borrower's NCF at issuance and a YE2008 NCF, 14 have experienced a NCF decline.
- Of the 26 fixed rate loans, 15 are below 1.0x, based on mortgage debt and YE2008 reported NCF.
- For the 27 loans that reported a YE2008 NCF, 17 have debt yields that are below 6.5%. The average debt yield for the 27 loans is 5.3%, less than half of what is required in today's lending environment.
- Every loan is structured as interest-only and lacks amortization making the exit debt yield no better than the current measure.

Since Q2 2007, the approximate time of many of these bulk sales, availability rates and rental rates have taken a turn for the worse in nearly all of the markets. While some markets have deteriorated only moderately, some have gotten quite bad. The graphs below display the worst performing markets in terms of both availability rate increases and rental rate decreases.

**Largest Increase in Availability Rate**



**Largest Declines in Rental Rate**





## If It Was Up In The Air In 2007, Where Has It Landed Starting In 2010?

### THE KEYS TO SOME SAN FRANCISCO AND NEW YORK PROPERTIES HAVE LANDED ON SOMEONE ELSE'S DESK.

In New York, Harry B. Macklowe purchased in February 2007 and subsequently lost seven EOP-Blackstone flip properties after he was unable to refinance the \$7 billion in short-term, high-interest debt he used to buy them. Morgan Stanley bought ten San Francisco buildings in the city's financial district as part of a \$2.5 billion purchase from Blackstone in May 2007. Five properties collateralized one floating-rate loan. It was recently announced that Morgan Stanley will be giving back the keys for these five properties to its mezzanine lenders. The bank will continue to own the other five properties it acquired in the deal. DBRS was not able to identify whether the additional five properties have debt that was securitized. The good news is that the trust collateral remains current and there is sufficient debt service coverage on the first mortgage floating-rate loan. Even considering the loan was underwritten to an as-stabilized NCF and the YE2008 performance is 29% short of the projection, the NCF still sufficiently covers the floating-rate payments. Furthermore, assuming a 9.0% debt constant on the first mortgage, the DSCR, based on YE2008, would be 1.25x.

#### San Francisco MSA

Loan Name	Deal Name	YE2008 DSCR		Loan PSF		Debt Yield	
		Whole Loan	A-Note	Whole Loan	A-Note	Whole Loan	A-Note
San Francisco Office Portfolio	LBFR 2007-LLFA	1.81	2.37	\$187.47	\$145.95	11.2%	14.4%

San Francisco Office Portfolio is 7-months into its extension options with 29-months remaining. Applying an 8% cap rate to the YE2008 NCF for the portfolio, results in a \$264.4 million value. This represents a 56% loss to the overall debt, all contained to the mezzanine loans. The trust asset should continue to perform fine. Based on this information, the first mortgage is considered refinance-able with an 11.2% debt yield, based on YE2008 NCF.

#### San Francisco MSA (continued)

Loan Name	A-note Balance (mm)	% of the pool	LTV		Estimated A-Note Loss (mm)
			Whole Loan	A-Note	
San Francisco Office Portfolio Roll-Up	\$146.6	7.6%	71.2%	55.4%	-

Although the trust performance remains healthy, the question investors now have to ask themselves is "Who is my new sponsor?" The excessive mezzanine debt burden eventually buried the sponsor. The first mortgage exposure of \$187 psf and the A-note of \$146 psf are very reasonable. However, the total debt of \$464 psf is recipe for disaster.<sup>1</sup>

1. The trust has a 50% interest in one of the properties (One Post) and additional indebtedness is allowed on the other 50% interest, so in order to calculate indebtedness per square foot, DBRS cut the property's square feet in half. Also, if the 50% interest of One Post incurred the maximum leverage allowed and it was all first mortgage, the debt yield would decline to 8%, which could have difficulty refinancing



## SOME LOANS HAVE LANDED IN SPECIAL SERVICING.

There are four loans, securitized in three transactions, located in the Los Angeles and Orange County MSAs that are now in special servicing. They all have one thing in common, the sponsor.

Maguire Properties paid Blackstone \$2.9 billion for properties in Los Angeles and Orange County and subsequently sold several properties shortly after the purchase. DBRS was able to find seven CMBS loans secured by some of these properties in Orange County. The remaining properties were either sold shortly after purchase from Blackstone or financed but not securitized.

It was announced in December 2009 that Maguire would be defaulting on six Orange County properties, three of which secure CMBS loans. In addition, it was announced that another Orange County EOP-Blackstone flip acquired by Maguire, Griffin Towers, was being foreclosed upon by the lender. Although DBRS can not verify whether securitized debt was used, it is worth mentioning the estimated loss. There is currently \$145 million of debt outstanding on Griffin Towers, but reportedly the lender is anticipating receiving bids between \$90 million and \$100 million. At the low end, this results in a value per square foot of \$165. By comparison, the three loans in special servicing in Orange County have leverage in excess of \$300 psf, indicating that losses could be quite high. Only one property, Stadium Towers Plaza, has an updated appraised value. It represents a very large 76% decline from the appraised value at issuance, and values the property at \$131 psf.

### Orange County MSA

Loan Name	Deal Name	YE2008 DSCR		Loan PSF		Debt Yield	
		Whole Loan	A-Note	Whole Loan	A-Note	Whole Loan	A-Note
Maguire Anaheim Portfolio	GSMS 2007-GG10	0.75	0.75	\$310.34	\$310.34	4.3%	4.3%
3800 Chapman	GSMS 2007-GG10	0.17	0.17	\$282.20	\$282.20	1.0%	1.0%
City Tower	CSMC 2007-C4	0.82	0.82	\$280.44	\$280.44	4.4%	4.4%
2600 Michelson	CSMC 2007-C4	0.86	0.86	\$309.17	\$309.17	4.6%	4.6%
Main Plaza	CSMC 2007-C3	NAV	NAV	\$275.67	\$275.67	3.1%	3.1%
Stadium Towers Plaza	JPMCC 2007-LDP11	0.47	0.59	\$388.73	\$323.42	2.7%	3.3%
18581 Teller Avenue	GCCFC 2007-GG11	1.21	1.21	\$232.32	\$232.32	6.9%	6.9%

The seven CMBS loans in Orange County appear to all have been underwritten to optimistic pro forma projections, and none have met those projections to date. On average, YE2008 NCF is 46% lower than the issuer UW NCF, with the decline ranging from as little as 13% to as much as 87%. However, the one loan with the 87% cash flow decline has a Q3 2009 annualized NCF that would reduce the decline to 48%, which is in-line with most of the other loans. There is only one loan out of seven that has a DSCR above 1.0x, and it represents less than 5% of the total value of the properties.



**Orange County MSA (continued)**

Loan Name	A-note Balance (mm)	% of the pool	LTV*		Estimated A-Note Loss (mm)
			Whole Loan	A-Note	
Maguire Anaheim Portfolio	\$103.5	1.4%	184.9%	184.9%	\$47.5
3800 Chapman	\$44.4	0.6%	200.5%	200.5%	\$22.2
City Tower	\$115.0	5.6%	181.8%	181.8%	\$51.7
2600 Michelson	\$95.0	4.6%	175.1%	175.1%	\$40.7
Main Plaza	\$160.7	6.0%	254.9%	254.9%	\$97.6
Stadium Towers Plaza	\$83.2	1.9%	292.4%	243.2%	\$49.0
18581 Teller Avenue	\$20.0	0.7%	115.4%	115.4%	\$2.7

The Maguire acquisition included two properties in downtown Los Angeles. Two California Plaza is on the servicer's watchlist due to a low YE2008 DSCR of 0.92x. 550 South Hope Street is more than 90-days delinquent and was transferred to the special servicer in August 2009. Both loans were underwritten to stabilized pro forma cash flows. Both loans had an in-place issuer DSCR of approximately 1.0x, with the stabilized DSCR above 1.20x. For both loans, cash flow performance to date has been worse than the in-place DSCR and has come nowhere near achieving the pro forma figures. 550 South Hope has a total debt of \$200 million, with \$35 million consisting of a subordinate B-note held outside the trust. The DSCR figures above are based on the A-note balance. Two California Plaza has no subordinate debt. The debt yield on both properties is less than half of what would be required in today's market.

**Los Angeles MSA**

Loan Name	Deal Name	YE2008 DSCR		Loan PSF		Debt Yield	
		Whole Loan	A-Note	Whole Loan	A-Note	Whole Loan	A-Note
Two California Plaza	GSMS 2007-GG10	0.92	0.92	\$353.43	\$353.43	5.1%	5.1%
550 South Hope St.	GSMS 2007-GG10	0.78	0.96	\$353.09	\$291.30	4.5%	5.4%

The special servicer has received an updated appraisal for 550 South Hope Street that values the property at \$121 million. This represents a 49% reduction from the appraised value at issuance. If the property was liquidated at this amount, a \$44 million loss would be incurred by the trust. Since GSMS 2007-GG10 is a very large deal (greater than \$7 billion), this loss would represent only 0.6% of the deal balance. As the DSCR is near 1.0x, it appears that Maguire will be keeping the loan current for the foreseeable future in hopes that the pro forma cash flow is eventually achieved. While this lowers the risk of having to liquidate into the current poor environment, the loan will face tremendous refinance risk even if cash flow does grow substantially.

**Los Angeles MSA (continued)**

Loan Name	A-note Balance (mm)	% of the pool	LTV*		Estimated A-note Loss (mm)
			Whole Loan	A-Note	
Two California Plaza	\$470.0	6.2%	156.2%	156.2%	\$169.1
550 South Hope St.	\$165.0	2.6%	179.0%	147.7%	\$53.3



Callahan Capital Partners and Morgan Stanley Real Estate Funds acquired a 2.8 million square foot, five-building portfolio in the Denver MSA for \$770 million (\$275 psf). DBRS verified that two of the properties, Tabor Center and U.S. Bank Tower, secure a securitized fixed-rate crossed-portfolio loan. The remaining three secure a securitized floating-rate loan (Denver EOP Portfolio).

The Tabor Center and U.S. Bank Tower loan is current and in special servicing, as of October 2009, as a result of a loan modification request, due to operating shortfalls at the property. Oddly, the property performance actually seems to be improving. While the borrower issuance NCF of \$16.9 million was much lower than the issuer UW NCF of \$19 million, the properties seems to be approaching the projected NCF with each passing year; going from \$18.6 million in 2008, to \$18.9 million (annualized) as of Q1 2009. Based on YE2008 NCF, the loan covers debt service at 1.08x.

The loan exposure of \$252 psf is considered relatively high for the Denver MSA, but the assets are considered Class A. The loan was originated as a five-year loan, with maturity on April 8, 2012. It will be interesting to see if the loan gets modified, considering it is currently performing, and what, if anything, the special service will require from the borrower.

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**Denver MSA**

Loan Name	Deal Name	YE2008 DSCR		Loan PSF		Debt Yield	
		Whole Loan	A-Note	Whole Loan	A-Note	Whole Loan	A-Note
Tabor Center & U.S. Bank Tower	MSC 2007-IQ14	1.08	1.08	\$252.03	\$252.03	6.2%	6.2%
EOP Denver Portfolio	MSC 2007-XLF9	2.09	2.09	\$70.69	\$70.69	13.3%	13.3%

In addition to three office buildings, the Denver EOP Portfolio contains one undeveloped portion of a commercial real estate condominium project. The loan is current, as of January 2010. It appears that the loan was underwritten to an as-stabilized cash flow of \$16.5 million that was much higher than the in-place 2007 NCF of \$12.8 million. The loan was conservatively sized at \$71 psf and the cash flow covered debt service on the in-place issuance NCF at 1.83x. However, there is a total of \$129.4 million of mezzanine debt in place, bringing the all-in leverage point to \$154. Taking the mezzanine debt into account, the loan was underwater based on the in-place issuance NCF with a DSCR of 0.81x.

The YE2008 NCF of \$14.7 million is approximately 14.4% higher than the issuance NCF, and translates into a DSCR of 1.91x. Applying an 8% cap rate to the YE2008 NCF, results in a portfolio value of \$183.5 million. This represents a 23% loss to the overall debt, but losses are fully contained to the mezzanine loans. Performance at the properties seems to be improving, and if the YE2008 NCF were to stabilize, the debt yield would be 13.3%, making refinance of the mortgage debt achievable.

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**Denver MSA (continued)**

Loan Name	A-note Balance (mm)	% of the pool	LTV*		Estimated A-note Loss (mm)
			Whole Loan	A-Note	
Tabor Center & U.S. Bank Tower	\$300.0	6.2%	129.5%	129.5%	\$68.4
EOP Denver Portfolio	\$110.2	9.6%	60.1%	60.1%	-



## SOME LOANS ARE LIKELY HEADED TO SPECIAL SERVICING.

The Irvine Co. purchased 17 buildings in San Diego County for an undisclosed amount from Blackstone. DBRS identified six loans, secured by six unique properties, that have been securitized in six different transactions. The overriding message with these loans is consistent, high leverage and underwriting based on pro-forma cash flow. Each of the loans is on the servicer's watchlist for a low DSCR. Based on the YE2008 NCF, the DSCR is consistently below 1.0x, six of which are below 0.73x, based on the whole loan. Updated performance has fallen short of stabilized underwritten net cash flow by as much as 23% to 48%. In addition, four of the six properties have experienced a decline from as-is cash flow at origination.

### San Diego MSA

Loan Name	Deal Name	YE2008 DSCR		Loan PSF		Debt Yield	
		Whole Loan	A-Note	Whole Loan	A-Note	Whole Loan	A-Note
Pacifica Tower	BACM 2007-3	0.61	0.71	\$584.18	\$529.26	3.6%	4.0%
Smith Barney Building	BACM 2007-5	0.95	1.08	\$585.98	\$529.13	5.5%	6.1%
La Jolla Executive Tower	BACM 2007-4	0.70	0.77	\$510.56	\$461.10	3.9%	4.3%
Centerside II	WACH 2007-C32	0.64	0.86	\$414.97	\$310.62	3.6%	4.8%
La Jolla Center I	WACH 2007-C33	0.65	0.90	\$502.47	\$363.23	3.7%	5.1%
La Jolla Center II	WACH 2007-C34	0.73	1.19	\$510.04	\$312.83	4.1%	6.7%

Although subordinate B-notes were carved out of all of the loans, the size of three of those notes was not meaningful and the leverage per square foot, even on the A-note, for these three loans exceeds \$460. The last three have B-notes that exceed 25% of the whole loan amount, which helps somewhat as the A-note per square foot is still high but more palatable. Based on the entire first mortgage, all of the loans are below water, five are significant (less than 0.73x), based on YE2008 NCF. If the loans manage to make it to maturity, refinancing will be a challenge. The average debt yield for all six is 4.1%, ranging from 3.6% to 5.5%. Estimating losses, based on an 8% cap rate and YE2008 NCF, would result in losses to the CMBS trusts for the three loans with small B-notes, while losses to the other three loans would be contained to the B-note.

### San Diego MSA (continued)

Loan Name	A-note Balance (mm)	% of the pool	LTV*		Estimated A-note Loss (mm)
			Whole Loan	A-Note	
Pacifica Tower	\$166.3	5.2%	222.2%	201.3%	\$83.7
Smith Barney Building	\$99.6	6.0%	145.9%	131.7%	\$24.0
La Jolla Executive Tower	\$106.8	5.3%	204.2%	184.4%	\$48.9
Centerside II	\$89.3	3.1%	220.4%	165.0%	\$35.2
La Jolla Center I	\$60.0	2.2%	217.7%	157.4%	\$21.9
La Jolla Center II	\$46.0	2.0%	193.4%	118.6%	\$7.2

Hines Interests Limited Partnership bought, in a deal with an estimated value of \$750 million, 32 properties in the Sacramento MSA. DBRS identified seven of these properties that have been securitized in three CMBS transactions. Two properties secure two loans; respectively, in two deals. Three crossed loans (considered one loan for discussion purposes below) located in a third deal, are collateralized by



five properties. Two of the loans are performing as expected with YE2008 DSCR of 1.43x and 1.39x, respectively. These two were not underwritten to projected NCF. However, they each have refinance risk considering their relatively low debt yields of 7.9% and 7.7%, respectively.

#### Sacramento MSA

Loan Name	Deal Name	YE2008 DSCR		Loan PSF		Debt Yield	
		Whole Loan	A-Note	Whole Loan	A-Note	Whole Loan	A-Note
Douglas Corporate Center I & II	ML-CFC 2007-8	1.43	1.43	\$168.71	\$168.71	7.9%	7.9%
300 Capitol Mall	ML-CFC 2007-9	0.98	0.98	\$272.23	\$272.23	6.8%	6.8%
Hines Office Portfolio (3 crossed loans)	BACM 2007-4	1.39	1.39	\$203.37	\$203.37	7.7%	7.7%

The third loan, secured by 300 Capitol Mall, is on the servicer's watchlist due to a low YE2008 DSCR of 0.98x. However, occupancy has increased and some rent commencement dates have passed in 2009, ultimately showing an improvement in partial year 2009 performance. It was underwritten to a stabilized pro-forma cash flow, and YE2008 NCF was still 23% below the pro-forma cash flow. Hines reportedly paid \$130 million, reflecting \$272 psf, which would be considered high in the Sacramento MSA. While the loan's performance appears to be improving in 2009, it will face refinance risk even if cash flow does grow substantially.

#### Sacramento MSA (continued)

Loan Name	A-note Balance (mm)	% of the pool	LTV*		Estimated A-note Loss (mm)
			Whole Loan	A-Note	
Douglas Corporate Center I & II	\$36.0	1.5%	101.5%	101.5%	\$0.5
300 Capitol Mall	\$104.3	3.7%	117.5%	117.5%	\$15.5
Hines Office Portfolio (3 crossed loans)	\$237.3	10.7%	103.2%	103.2%	\$7.4

### SOME LOANS ARE TREADING ON THIN ICE.

Thomas Properties Group (TPG) purchased ten Class A office properties in the central business district (CBD) and suburbs of Austin for \$1.15 billion. The portfolio has a total of 3.5 million square feet, 2.5 million square feet of which is in the CBD. We have identified the five CBD buildings, all of which were securitized in LBCMT 2007-C3. The five properties each secure a separate non-crossed loan. These properties represent over 80% of the purchase price of the whole portfolio, based on appraised value. No purchase price allocations are available. The remaining properties, located in the suburbs, do not appear to have been securitized.

The loans have been structured with a subordinate debt in the form of two credit facilities that are collateralized by all five properties. The larger of the facilities was fully funded, at issuance, in the amount of \$192.5 million. The smaller facility was intended to be a \$100 million revolver that could be drawn upon throughout the term of the loan. However, the credit facility lender was Lehman Brothers (also part of the borrowing entity) and this facility has been restructured. It is unclear from public information exactly how it works, but it appears the facility limit is much lower than before and might be partially funded by the sponsors. As such, total debt calculations are based on the mortgage debt plus pro-rata allocations of the \$192.5 million term-credit facility. This facility represents 36% of the entire debt package.



### Austin MSA

Loan Name	Deal Name	YE2008 DSCR		Loan PSF		Debt Yield	
		Whole Loan	A-Note	Whole Loan	A-Note	Whole Loan	A-Note
300 West 6th	LBCMT 2007-C3	0.68	1.07	\$445.72	\$284.35	4.1%	6.4%
Frost Bank Tower	LBCMT 2007-C3	1.16	1.82	\$181.12	\$115.54	7.0%	11.0%
One Congress Plaza	LBCMT 2007-C3	1.09	1.72	\$173.36	\$110.60	6.7%	10.4%
One American Center	LBCMT 2007-C3	1.16	1.82	\$158.27	\$100.97	7.0%	11.0%
San Jacinto Center	LBCMT 2007-C3	1.14	1.78	\$166.80	\$106.41	6.9%	10.8%

Only one loan of the five properties, 300 W. 6th Street, is on the watchlist. This loan carried much higher leverage at issuance than the other loans. The YE2008 DSCR is relatively low at 1.07x, however, based on total debt (A-note plus credit facility) the DSCR falls to 0.68x. The UW NCF for all the loans was based on in-place rental rates, and as such, YE2008 NCF for all five loans is either stable or higher than it was at issuance. However, the mortgage debt for 300 W. 6th Street was clearly sized for a higher cash flow than was UW. This is evidenced by the very low 1.02x UW DSCR for an interest-only loan paying a 6.01% coupon.

The YE2008 debt yield (when including credit facility debt) for 300 W. 6th Street is extremely low at only 4.1%; whereas, the other four loans are much higher, near 7%. Based on mortgage debt in the trust only, these figures increase to 6.4% for 300 W. 6th Street and 11% for the other four loans. Based on the low debt yield for 300 W. 6th Street, this looks like the one loan that could be in the most serious danger of causing significant losses to the trust.

### Austin MSA (continued)

Loan Name	A-note Balance (mm)	% of the pool	LTV		Estimated A-Note Loss (mm)
			Whole Loan	A-Note	
300 West 6th	\$127.0	6.2%	195.6%	124.8%	\$25.2
Frost Bank Tower	\$61.3	3.0%	113.6%	72.5%	-
One Congress Plaza	\$57.0	2.8%	120.1%	76.6%	-
One American Center	\$50.9	2.5%	114.4%	73.0%	-
San Jacinto Center	\$43.0	2.1%	116.5%	74.3%	-

Utilizing an 8% cap rate and YE2008 NCF, TPG is out of the money on all five loans. While only one loan appears to be severely overleveraged based on mortgage debt, the \$192.5 million credit facility is collateralized by all five loans. The YE2008 NCF from all five properties results in a DSCR of 0.97x on the total debt load. To the extent that cash flows at the property remain fairly stable, TPG will likely be able to keep current on its debt-service payments and hold on to the properties for the foreseeable future. However, the above valuation for 300 W. 6th Street would result in a \$25 million principal loss to LBCMT 2007-C3. This represents less than 1% of the current deal balance and indicates that these loans do not pose a large threat to senior bondholders.

Beacon Capital acquired Blackstone properties located in the Seattle and Washington DC markets for \$6.5 billion. This securitized portfolio of 20 properties represents a portion of that total acquisition. The properties secure a loan that is split into seven pari passu pieces, across six CMBS transactions, whereby two of the pari passu pieces share a subordinate B-note. One of the securitized pieces is currently on the servicer's watchlist for low coverage, but the other 6 pieces are not. Reporting is different depending on which loan piece is being analyzed. The reported DSCR at issuance and the current DSCR



is different depending on the transaction. The loan per square foot is also different depending on what square footage the issuer included in the collateral square footage. DBRS excluded the cash flow pledge properties from the per square foot calculation because the assets themselves are not security for the loan. Additionally, the whole-loan balance is reported differently by servicers from deal to deal and in some cases is not accounted for in the loan per square foot calculation, thus leaving investors to potentially assume these are relatively low levered assets. These reporting discrepancies are due to the different servicers that report on each piece, which can be a great source of confusion for a complex loan.

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**Seattle & Washington, D.C. MSA**

Loan Name	Deal Name	DBRS DSCR		Loan PSF		Debt Yield	
		Whole Loan	A-Note	Whole Loan	A-Note	Whole Loan	A-Note
Beacon Seattle & Washington D.C. Portfolio	Various	0.85	0.87	\$354.12	\$346.78	4.9%	5.0%

The issuance UW NCF, which was a pro-forma figure, is approximately 21% higher than the YE2008 NCF. DBRS used its calculation of NCF to complete the statistics in the chart above, which excludes the cash flow pledge properties and takes into account additional actual vacancy at another property. It is unlikely that the portfolio will achieve the underwritten cash flow at any time within the next five-years, given current rental rate trends. The projected NCF, at issuance, assumed growth upon top-of-the-market numbers. This loan was UW with limited cushion and has been hovering near 1.10x since issuance. CoStar is showing direct availability around 25% for the Seattle assets with average rents of \$35.50 psf. Vacancy for the portfolio has shot up by 15% from 2007, while rents have fallen by about \$5 psf. The DC properties compare favorably, with vacancy of just 10% and gross rents in the neighborhood of \$56 psf. Though vacancy has increased in the DC properties as it did in Seattle, rental rates generally stayed flat.

Although the NCF covers mortgage debt service today, it is likely less than 1.0x when the mezzanine debt is taken into account. The Beacon loan is considered high leverage. For the portfolio as a whole, the high amount of leverage is apparent when you note the debt yield of just 6.3%, based on the YE2008 NCF. In addition, three of the 20 properties in the portfolio are considered cash-flow assets so their square footage is not included in a loan per square foot calculation. The loan per square foot for the total debt is \$381. The loan per square foot for the mortgage debt is \$354, and for just the A-note it is \$347 psf.

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**Seattle & Washington, D.C. MSAs (continued)**

Loan Name	A-note Balance (mm)	% of the pool	LTV		Estimated A-note Loss (mm)
			Whole Loan	A-Note	
Beacon Seattle & Washington D.C. Portfolio	\$2,644.0	Various	162.8%	159.4%	\$985.4

**AND SOME HAVE LANDED ON SOLID GROUND...FOR NOW.**

Although a few of the loans have low term default risk, refinance risk is a common theme with all of the loans covered in this report.

Shorenstein Realty Investors purchased the former 46-property, EOP Portland portfolio (more than 4 million square feet) from Blackstone for a reported \$1.2 billion, or roughly \$300 psf. The UW NCF took into account future contractual rent bumps through the lease term and a slightly inflated occupancy rate, and the loan has performed at or above issuance projections since origination. Coverage has been hovering around the 1.34x UW DSCR.




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**Portland MSA**

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Loan Name	Deal Name	YE2008 DSCR		Loan PSF		Debt Yield	
		Whole Loan	A-Note	Whole Loan	A-Note	Whole Loan	A-Note
Shorenstein Portland Portfolio	GSMS 2007-GG10	1.33	1.33	\$179.60	\$179.60	7.5%	7.5%

The loan is \$180 psf. Although the leverage point may seem somewhat high for the Portland market, especially considering that many of the assets are outside of the CBD, in comparison to the other financings discussed herein, this leverage is considered moderate. There is no subordinate or mezzanine debt in place, nor is there any allowed in the future. The properties are performing in line with issuance expectations, which sufficiently covers the interest-only payments. Term default is low compared to other loans, although the loan's relatively low (7.5%) debt yield is a reminder of the higher leverage on the loan and the difficulties it may face at refinance.

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**Portland MSA (continued)**

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Loan Name	A-note Balance (mm)	% of the pool	LTV		Estimated A-note Loss (mm)
			Whole Loan	A-Note	
Shorenstein Portland Portfolio	\$697.2	9.2%	106.7%	106.7%	\$43.5

**CONCLUSION**

The dismantling of Equity Office Properties sheds some light on the egregious practices of the times, and the consequences the CMBS trusts will suffer as a result. High leverage, coupled with unrealistic cash flow projections at issuance, and anticipated NCF decline is a consistent theme throughout these loans. It is not unlike the story of other trophy office buildings financed and securitized in 2007. DBRS used YE2008 NCF throughout the report but it is our belief that these cash flows, for the most part, will fall further over the upcoming years. Additionally, DBRS applied an 8% capitalization rate to estimate losses, for consistency purposes only, and we do not expect that this rate is accurate for all properties, in all markets. As expected, due to long term leases, office properties will be one of the last property types to suffer the effects of aggressive underwriting and economic decline, but based on the performance of these loans, hard times are coming fast. In isolation, these may not cause significant hardship to each respective trust, but combined with other struggling loans, estimated losses are projected to escalate beyond the original investment grade floor, for most transactions.



## Appendix A: Study Highlights

Loan Name	No Equity Remaining (a)	Mezzanine Loan Default	Transferred to Special Servicing	On Servicer's Watchlist	NCF Decline from borrower's issuance	YE2008 Financials Below 1.0x	Debt Yield Below 6.5%	Market Rental Rate Deterioration	Market Availability Increase
Macklowe EOP Manhattan Portfolio (b)	x	x						x	x
San Francisco Office Portfolio	x	x						x	x
Maguire Anaheim Portfolio	x		x			x	x	x	x
3800 Chapman	x			x		x	x	x	x
City Tower	x			x		x	x	x	x
2600 Michelson	x		x			x	x	x	x
Main Plaza (c)	x			x			x	x	x
Stadium Towers Plaza	x		x			x	x	x	x
18581 Teller Avenue	x							x	x
Two California Plaza	x			x		x	x		x
550 South Hope St.	x		x			x	x		x
Tabor Center & U.S. Bank Tower	x		x				x		x
Denver EOP Portfolio	x								x
Pacifica Tower	x			x		x	x	x	x
Smith Barney Building	x			x		x	x	x	x
La Jolla Executive Tower	x			x		x	x	x	x
Centerside II	x			x		x	x	x	x
La Jolla Center I	x			x		x	x	x	x
La Jolla Center II	x			x		x	x	x	x
Douglas Corporate Center I & II	x							x	x
300 Capitol Mall	x			x		x		x	x
Hines Office Portfolio	x							x	x
300 West 6th	x			x		x	x		x
Frost Bank Tower	x								x
One Congress Plaza	x								x
One American Center	x								x
San Jacinto Center	x								x
Beacon Seattle & Washington D.C. Portfolio	x			x			x	x	x
Shorenstein Portland Portfolio	x								x

Note: All data based on January 2010 reporting.

(a) Assuming an 8% capitalization rate.

(b) Limited data because loan is no longer in the pool.

(c) YE2008 NCF not available.



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## Notes & Glossary

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### Notes

**ADR** = average daily rate  
**Avg. HH** = 2000 average annual household income  
**BR** = bedroom  
**capex** = capital expenditures  
**CBD** = central business district  
**CMBS** = commercial mortgage-backed securities  
**DSCR** = debt service coverage ratio  
**EGI** = effective gross income  
**F&B** = food & beverage  
**FF&E** = furniture fixtures & equipment  
**G&A** = general and administrative  
**GPR** = gross potential rent  
**IO** = interest only  
**LC** = leasing commission  
**LTV** = loan-to-value  
**MHC** = mobile home community  
**MTM** = month to month  
**MSA** = metropolitan statistical area  
**n.a.** = not available  
**n/a** = not applicable  
**NCF** = net cash flow  
**NNN** = triple net  
**NOI** = net operating income  
**NRA** = net rentable area  
**NR – PIF** = not rated – paid in full  
**OSAR** = operating statement analysis report  
**PPL** = pari passu loan  
**psf** = per square foot  
**R&M** = repairs & maintenance  
**REIT** = real estate investment trust  
**RevPAR** = revenue per available room  
**sf** = square foot/square feet  
**SPE** = special purpose entity  
**TI** = tenant improvement  
**TIC** = tenants in common  
**T-12** = trailing 12 months  
**UW** = underwriting  
**WA** = weighted average  
**WAC** = weighted-average coupon  
**WH** = warehouse  
**x** = times  
**YE** = year-end  
**YTD** = year-to-date

### Glossary

**capital expenditure (capex)** – Costs incurred in the improvement of a property that will have a life of more than one year.

**debt service coverage ratio (DSCR)** – A measure of a mortgaged property's ability to cover monthly debt service payments, defined as the ratio of net operating income (NOI) or net cash flow (NCF) to the debt service payments.

**debt yield** - Calculation is YE2008 NCF divided by outstanding balance. The Beacon Seattle & Washington D.C. Portfolios are the only exception whereby DBRS NCF was used.

**effective gross income (EGI)** – Rental revenue minus vacancies plus miscellaneous income.

**issuer UW** – Issuer underwritten from Annex A or servicer reports.

**loan-to-value (LTV)** – The ratio between the principal amount of the mortgage balance, at origination or thereafter, and the most recent appraised value of the underlying real estate collateral, generally from origination. Calculation based on YE 2008 NCF and an 8% capitalization rate. The Beacon Seattle & Washington D.C. Portfolios are the only exceptions whereby DBRS NCF was used.

**net cash flow (NCF)** – The revenues earned by a property's ongoing operations less the expenses associated with such operations and the capital costs of tenant improvements, leasing commissions and capital expenditures (or reserves). Moreover, NCF is net operating income (NOI) less tenant improvements, leasing commissions and capital expenditures.

**NNN (triple net)** – A lease that requires the tenant to pay operating expenses such as property taxes, insurance and maintenance, in addition to the rent.

**net operating income (NOI)** – The revenues earned by a property's ongoing operations less the expenses associated with such operations but before mortgage payments, tenant improvements, replacement reserves and leasing commissions.

**net rentable area (NRA)** – The area (sf) for which rent can be charged. NRA includes the tenant's premises plus an allocation of the common area directly benefiting the tenant, such as common corridors and restrooms.

**revenue per available room (RevPAR)** – A measure that divides revenue by the number of available rooms, not the number of occupied rooms. It is a measure of how well the hotel has been able to fill rooms in the off-season, when demand is low even if rates are also low, and how well it fills the rooms and maximizes the rate in the high season, when there is high demand for hotel rooms.

**tenant improvements (TIs)** – The expense to physically improve the property or space, such as new improvements or remodeling, paid by the borrower.

**weighted average (WA)** – Calculation is weighted by the size of each mortgage in the pool.

**weighted-average coupon (WAC)** – The average coupon or interest payment on a set of mortgages, weighted by the size of each mortgage in the pool

**whole loan** - Calculation includes all first mortgage debt and excludes mezzanine debt

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