08.18.08

This past weekend I read a couple of articles that got me thinking - which is always dangerous.

The first was the story on Lehman Brothers apparently trying to sell their ENTIRE $40 +/- Billion real estate portfolio --- it didn't say whether it was a mix of loans and equity or just loans. The story said that a number of big players were looking at it, but there was still a sizable "bid-ask spread" even with a substantial Lehman guarantee of some sort. It will be interesting to see how this turns out. When you combine such a deal with Merrill's huge sale of loans to Lone Star you wonder if this is signaling the turn of the market. In many ways it reminds me of the S&L crisis in the 90-s. As that market tanked capital dried up. There were lots of hand-wringing conferences on the "capital crisis". Well it wasn't really a capital crisis - there was plenty of capital out there -- it was a "confidence crisis". There was no confidence that the market had finally bottomed out and nobody wanted to buy or lend until that happened. We were fortunate that the former American Airlines CEO - William Casey, I think, --who took over the RTC understood that we would never find the market bottom by selling off - on a one-off basis --the billion of dollars of assets the RTC had taken over from failed banks and S&Ls. As the person who negotiated probably the very first asset management deal with the RTC I can confirm his view. We would still be working out those assets, if he hadn't changed the process --- by assembling large pools of assets and auctioning them off with no minimum bids. It was amazing how quickly that process cleared the market and capital returned --- and it began a great 15 year run for real estate. With the Merrill sale and the possible Lehman sale we may be seeing the same phenomena. If that occurs the market may begin to recover sooner that I would have thought. To accomplish that, however, many real estate owners and lenders are going to suffer some or even lots of pain as they take the write-downs required to lure buyers back to the market . On the other hand another article on Friday on the FT seemed to indicate that most troubled debt buyers are holding back. Howard Marks at Oaktree says its still too early to buy as more losses are coming. I guess that is what makes a market. One of the articles asked whether Lehman could even afford to take the necessary write-downs. If that sale makes - or doesn't - it might be a pretty good market indicator.

After reading the bulk sales stories and getting (for me) a tiny bit optimistic, I then read the piece on Prof. Nouriel Roubini @ NYU in yesterday's NYT Magazine -- which I recommend reading. Roubini is, as you probably know, pretty bearish in his outlook (he's been called a "PermaBear") but he was damned accurate in calling early the housing crisis including the Fannie-Freddie problem. He thinks we have a lot further to fall as there is still too much problem debt out there - not just housing, but credit card, auto, corporate, LBO, commercial real estate, etc debt - that was generated by the same deeply flawed underwriting, securitization, & rating techniques that created the sub-prime debt crisis. He says "we don't have a sub prime mortgage market, we have a subprime financial system". If he is right then we will see a lot more banks go under and the remaining "healthy" banks will really tighten up their lending standards which will put a further damper on the recovery.

Its going to be interesting over the next few months.

Ted