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**THANKS FOR WRITING IN**

Thanks for writing in. Please keep those cards and letters coming. Here are a few recent notes from savvy, regular readers and good friends:

“Deflation remains the issue and housing proves it.” - M.N., in a June email

“Your economic insight and sage perspective are right on point and I couldn't agree more with... all of it!” - D.M., bank special assets executive

“Your July editorial is horribly discouraging and right on target. I am unsure of a time in modern history when the president has been so completely incompetent and disinterested in

resuscitating the economy.”

- A.N., economist/housing expert

“I am going on record that the beginning of the long, slow, slide in the stock market is finally upon us. Yes, there will be some ‘bear’ rallies and some pockets of light in a sea of darkness, but, otherwise here it goes. The elements driving this are:

- No more Fed buying of T-bills or pumping cash into the economy and the market (i.e., the end of those funny little market moves up for no reason).
- Europe is in deep doo-doo, even if they don’t know it and their currency keeps running up...driving up the interest rates on the Euro reminds me of the pilot who flew the plane that crashed going from Brazil to France because he believed that tilting the nose up was the right solution, and he stalled out the jet.
- The housing hangover and drop in values is FINALLY coming back to roost, which will just kill consumers!
- Overall slow-down in economic growth in the U.S. and the rest of the world.”

- T.K., a Pathfinder investor, in a June 1, 2011 email

Please visit our newly redesigned Pathfinder website at [www.pathfinderfunds.com](http://www.pathfinderfunds.com).

Several of you have asked about guest-writing features for upcoming newsletters. If you have expertise in an area that could be of interest to our readers, please email us at [info@pathfinderfunds.com](mailto:info@pathfinderfunds.com) with information about your proposed subject matter – we will be happy to consider it for a future edition.

## CHARTING THE COURSE

### **You Just Can’t Make This Stuff Up**

By Mitch Siegler, Senior Managing Director

Financial kibitzers and semi-professional pundits like us can’t resist arcane data, graphs and charts. The art form – distilling these mountains of data into actionable investment strategies. This issue, we’re inspired by the old saw – a picture is worth 1,000 words – to present nine “truth is stranger than fiction” stories guaranteed to awaken the slumbering and give the rest of us something to ponder.



**U.S. credit rating downgrade – “No risk of that”:** Treasury Secretary Tim Geithner blasted S&P’s August downgrade of the U.S. from AAA to AA+. He said the credit ratings agency showed “terrible judgment and a stunning lack of knowledge about basic U.S. fiscal math.” In April, Geithner said “No risk of that,” in response to a CNN reporter, who asked

“Do you think there is any chance the U.S. could lose its AAA credit rating.” It wasn’t long ago that terms like “debt ceiling” and “credit rating” could be counted on to induce narcolepsy. Now, those terms are newspaper headlines.

**U.S. now in the 100%+ national debt/GDP club** – I wouldn’t want to belong to a club that would have me as a member. We think Groucho said it first, Woody Allen second. In August, the ratio of the Federal government’s accumulated debt to 2010 GDP exceeded 100%. According to *Agence French-Press*, the only other members of that auspicious club are “Japan (229%), Greece (152%), Jamaica (137%), Lebanon (134%), Italy (120%), Ireland (114%) and Iceland (103%).

***New York Times*’ sage advice – spend what you don’t have:** Reading the recent *New York Times* op-ed piece by Daniel Gross gives us heartburn about our kids’ futures. Mr. Gross debunks the widely held notion that consumers turned thrifty in the aftermath of the financial crisis. He cites a CardHub.com study which concludes that the huge overall decline in credit card debt is not the result of frugality and parsimony but rather because lenders wrote off \$124.1 billion in “uncollectible” balances. Meanwhile, Gross says “Mailboxes are again stuffed with credit card solicitations. Newspapers are filled with come-ons from car dealers offering 0% financing. The Federal Housing Authority offers mortgages for as little as 3% down.” Gross urges Americans to take on debt, saying “Unless you’re a multimillionaire, it’s difficult to make significant purchases...out of savings or cash flow from wages. The renewed willingness and confidence to spend money we don’t have is vital to the continuing recovery.” Now, we’re not going to take one for the team by borrowing for that new refrigerator, watch or vacation, but it sure would help the old economy if you did so.



**Chile a better credit than France:** The price of Credit Default Swaps (CDS) on a five-year, French government bond, rated AAA, is now much higher than the price of a five-year, Chilean government bond, rated several notches below, at A+. So, CDS traders are telling us something the ratings agencies aren’t – Chile is a better credit risk than France.

**Democrat businessmen frightened by President’s policies:** Steve Wynn, Chairman and CEO of Wynn Resorts, which employs 16,500 at its worldwide hotels and casinos, knows a thing or two about creating and growing businesses. Wynn, who built Golden Nugget, Mirage, Treasure Island, Bellagio, Wynn and Encore in Las Vegas and several leading properties in Macau is also a major Democrat supporter. “I am a Democrat businessman...telling you that the business community is frightened to death of the weird political philosophy of the President of the U.S. Until he is gone, everybody is going to be sitting on his thumbs,” says Wynn. “Obama is responsible for this fear in America,” he continues. “The guy keeps making speeches about redistribution [of wealth and the need] to do something to businesses that don’t invest, that are holding too much money. You know, we haven’t heard that kind of talk except from pure socialists,” Wynn concludes. In 2010, Wynn considered moving his corporate headquarters to Macau.

**China lectures U.S. on need for investor protections:** The Chinese State Administration of Foreign Exchange said in late July “We hope the U.S. government will earnestly adopt responsible policies to strengthen international market confidence and to respect and protect the interests of investors.” So, we have a leading Democrat businessman (above) who is so disgusted with the President that last year, he considered moving his headquarters to China and a leading Chinese government agency making statements about the U.S. “protecting the interests of investors.” It’s straight out of *Atlas Shrugged*.

**A weak dollar is a wonderful thing:** This little tidbit from BCA Research, a leading global investment research firm that charges clients tens of thousands for investment advice, caught our eye. “A weakening U.S. dollar has served the economy extremely well. It has helped trigger an export boom, inflated corporate earnings, lifted stock prices and avoided deflation – all without costing anything.” Really – a free lunch, heh? So, if we just copy the smart folks in Zimbabwe, Argentina, Greece and, of course, the Weimar Republic, we’ll have similar prosperity. Jeez.



**Throw the bums out:** The recent New York Times/CBS poll released in mid-September showed that just 12% of Americans approve of the way Congress is doing its job. This matches the all-time low from October, 2008. But, it gets worse. Just 6% of registered voters believe most Congressmen deserve to be reelected and 84% favor throwing the bums out and replacing them – hopefully, not with new bums. We contrarians are looking for the silver lining here – perhaps change is coming?

**President says soak the millionaires, billionaires and zillionaires** – The president rails against “millionaires and billionaires,” with false data about who really pays our taxes. The administration’s claims, echoed by Warren Buffett, that millionaires pay less in taxes than their secretaries, is balderdash. IRS data, compiled by *Forbes*, indicate that 99.6% of those earning more than \$1 million pay taxes at a much higher tax rate than secretaries. And an estimated 200,000 wealthy taxpayers – the folks who create new businesses and jobs – pay 20% of all federal income taxes.

Truth really is stranger than fiction. You just can’t make this stuff up.

*Mitch Siegler is Senior Managing Director of Pathfinder Partners, LLC. Prior to co-founding Pathfinder in 2006, Mitch founded and served as CEO of several companies and was a partner with a boutique investment banking and venture capital firm. He can be reached at [msiegler@pathfinderfunds.com](mailto:msiegler@pathfinderfunds.com).*



## SELECTED PATHFINDER CLOSED TRANSACTIONS

*Pathfinder Partners, LLC is the sponsor of the Pathfinder Opportunity funds, which acquire with institutional capital partners, distressed real estate properties and the underlying mortgages from financial institutions.*

<p><b>VISTA LAGO APARTMENTS</b></p> <p><i>\$3,200,000 defaulted senior mortgage on 102-unit apartment in Austin, TX</i></p> <p>September, 2011</p>	<p><b>BAROLO PLACE CONDOS</b></p> <p><i>16 residential condominiums in Scottsdale, AZ</i></p> <p>August, 2011</p>	<p><b>DORSEY PLACE CONDOS</b></p> <p><i>84 residential condominiums in Tempe, AZ</i></p> <p>July, 2011</p>
<p><b>DOBSON PLACE APARTMENTS</b></p> <p><i>120-unit apartment complex in Mesa, AZ</i></p> <p>July, 2011</p>	<p><b>THE SANCTUARY TOWNHOMES</b></p> <p><i>\$9,400,000 defaulted senior mortgage on 12 residential townhomes in Seattle, WA</i></p> <p>June, 2011</p>	<p><b>OTAY OFFICE CONDOS</b></p> <p><i>New, 68,000 square foot office condo project in Chula Vista, CA</i></p> <p>April, 2011</p>
<p><b>ORANGETHORPE OFFICE</b></p> <p><i>\$11,500,000 defaulted senior mortgage on 100,000 square foot office building in Anaheim, CA</i></p> <p>April, 2011</p>	<p><b>HUNTER'S CHASE CONDOS</b></p> <p><i>20 new residential condos in Denver, CO</i></p> <p>April, 2011</p>	<p><b>METRO LOFTS</b></p> <p><i>\$3,800,000 defaulted senior mortgage on a new, seven-unit mixed use project in Berkeley, CA</i></p> <p>December, 2010</p>
<p><b>LAS BRISAS CONDOMINIUMS</b></p> <p><i>18-unit condominium project in Long Beach, CA</i></p> <p>October, 2010</p>	<p><b>HAWTHORNE 44</b></p> <p><i>\$6,500,000 defaulted senior mortgage on new, 27-unit condo project in Portland, OR</i></p> <p>September, 2010</p>	<p><b>HEWITT ST. LOFTS</b></p> <p><i>\$12,500,000 defaulted senior mortgage on new, 33-unit condo project in Los Angeles, CA</i></p> <p>September, 2010</p>

## FINDING YOUR PATH

**“It’s the End of the World as We Know It (and I Feel Fine).”**

**By Lorne Polger, Senior Managing Director**



It didn’t feel like the end of the world to me back in 1987 when this R.E.M. song, and the “Document” album was released. I was filled with hope and enthusiasm as I was completing UCLA law school. My student loan payments were manageable, my prospects for my first job as a lawyer were abundant, and although the stock market took a big drop in October, no one was talking Great Depression II.

A lot has changed since 1987. Al Gore invented the Internet (maybe not). George Bush invaded Iraq. Interest rates have dropped by 70%. I lost my hair (if anyone finds it, please send me an email). But three economic things that are at the core of most Americans’ lives have changed dramatically. The value of residential real estate has plunged and the costs of health care and higher education have skyrocketed.

In 1987, no one was discussing underwater homes – even in coastal areas. It’s a far different story today, and the numbers are staggering and heading (still) in the wrong direction. CoreLogic, a leading provider of real estate analytics and business services, recently released second quarter negative equity data showing that almost 11 million people, or 22.5% of all residential properties with a mortgage, had negative equity. An additional 2.4 million borrowers had near-negative (less than 5%) equity. Together, negative and near-negative equity mortgages accounted for 27.5% of all residential properties with a mortgage.

In a healthy housing market, about 5% of homeowners are underwater. Roughly two-thirds of homeowners in Nevada with a mortgage have negative equity, the worst in the country. Arizona, Florida, Michigan and California are next, with up to 50% of homeowners underwater. Only nine states are below 10%. Quite a contrast.



Clearly, this affects consumer spending and confidence. If your mortgage has effectively become a road to nowhere, your likelihood of making discretionary purchases decreases. And, notwithstanding all the talk about lower interest rates, the reality is that the mortgage finance world has become one of “haves” and “have nots.” Those who don’t need a new loan, can get one. Those with the greatest need: fuggedaboutit. Put that in your pipe and smoke it, Washington.

This past month, the National Association of Home Builders Housing Market Index (the measure of confidence by homebuilders) fell from 15 to 14. The magic number where

builders feel more confident than not: 50. “Very little has changed in terms of housing market conditions so far this year,” said NAHB Chairman Bob Nielsen, a home builder from Reno, Nevada. “Builders continue to confront the same challenges in accessing construction credit, obtaining accurate appraisals for new homes, and competing against foreclosed properties that they have seen for some time. Beyond this, both builder and consumer confidence took a hit in recent weeks with the market disruptions caused by the S&P downgrade and congressional gridlock on the budget deficit.”

“The fact that the HMI continues to hover within such a narrow, low range reflects builders’ awareness that many consumers are simply unwilling or unable to move forward with a home purchase in today’s uncertain economic climate,” added NAHB Chief Economist David Crowe.

At Pathfinder, we continue to sell new residential product, but that’s only because we’re buying what other groups built for 50 cents on the dollar and resetting prices at similar margins. Generally, the numbers don’t pencil to be building at retail today.

People will always find a place to live, even if it means altering their lifestyle. There are a lot of renters out there today, and there is nothing wrong with that. That fact alone, over time, will lead to new residential development as our remaining stock of rental inventory continues to be swallowed up.

So, residential housing isn’t the worst problem or my biggest concern. My bigger fears lie with health care and education. And I’m really concerned these days.



I currently anticipate that the 2012 premium for my family’s health insurance (we are on an HMO with sizeable deductibles) will be nearly \$24,000. **That’s almost a 300% increase since 2007, the year we started this plan.** That, my friends, is a broken system, inflation at an unsustainable pace. Who can afford that? I never dug too deeply into the Obamacare plan when the legislation was passed. Has it helped? Has it hurt? Are more people receiving quality care today than before the bill? I have absolutely no idea. All I know is that at some point, the next straw breaks the camel’s back.

Much like I did with dental insurance years ago, the costs become so outrageous at some point, that self-insurance becomes a viable option. The difficulty with that argument, of course, is that nobody loses sleep over suffering a catastrophic dental injury.

Who’s making the money? Not the doctors. Every doctor that I know tells me they’re making less; that their insurance premiums are rising and their insurance reimbursements are shrinking. The hospitals? I don’t think so. Various hospital groups are closing and stock price performance isn’t impressive. According to a recent piece in *Forbes*, the average American hospital barely breaks even. The insurance carriers? Not based on earnings of the nation’s top health insurers.

We have a bloated system burdened by bureaucracy and a “CYA” mentality, and it’s killing us. And no one has the guts to really take a sharp red pen to it and start over.

I always like to end on a happy note and who doesn’t believe in education? As the parent of a California high school senior in the middle of her college search, I shake my head and wonder how it’s done. Rough budget for two kids going through private undergraduate schools over the next five to seven years: \$500,000. Oh, and that’s after tax dollars, so if you’re in a high income tax state like California, you’ll need to earn \$900,000 to pay the piper. Of course, those numbers were slightly less daunting when you could actually realize some gains in 529 plans and similar investment accounts. Unfortunately, when the market drops, the values of 529 plans drop like a rock. And, what are you really getting with an undergraduate degree anymore? We’re planning on financing graduate school as well.

In California, the system appears particularly broken. The University of California system (which today includes some of the finest public schools in the country, including Berkeley, UCLA and UC San Diego) just announced a 16% hike in tuition for 2012 and suggested that similar hikes will be required at least through 2014. That’s a 50% increase over three years. A little greater than the rate of inflation, you say? That’s nothing. In my last year of law school in 1987-1988, my in-state tuition at UCLA was approximately \$1,500. This year, it’s \$45,000 for in-state and \$55,000 for out-of-state tuition. And that doesn’t include room and board or basic living expenses. The medical school seems like a bargain at only \$32,000/year, but on their website, they note that books, labs, room and board and miscellaneous costs bring the total to about \$60,000, or a quarter million for four years. And if you’re an out of state student, why don’t you add about \$50,000 for good measure. After tax dollars, all.



I wasn’t happy writing those \$400/month checks to repay my student loans. But in hindsight, that sure sounds better than writing \$4,000/month checks. I’m an optimist, by nature, but this may very well be the first time in recent history where the prospects for our kids are dimmer than for their parents. How sad.

It may not be the end of the world as we know it, but I don’t feel so fine. R.E.M. announced their break up last month after playing together for 31 years. I’ll be the first to line up for tickets to the reunion tour, provided the world hasn’t ended before then.

*Lorne Polger is Senior Managing Director of Pathfinder Partners, LLC. Prior to co-founding Pathfinder in 2006, Lorne was a partner with a leading San Diego law firm, where he headed the Real Estate, Land Use and Environmental Law group. He can be reached at [lpolger@pathfinderfunds.com](mailto:lpolger@pathfinderfunds.com)*

## ZEITGEIST - SIGN OF THE TIMES

*A compendium of notable news articles relating to the economy, commercial lending and real estate which we've edited and commented upon.*

### **Average Foreclosure Timeline: 599 Days**

Here's an astounding statistic, courtesy of Lender Processing Services Inc. LPS' latest monthly "Mortgage Monitor" report indicates that the average time to conclude a foreclosure is 599 days. Judicial states are even worse – at the current rate of foreclosure sales, it will take 111 months to work through loans 90+ days delinquent or in foreclosure in those states. The news is better in non-judicial states – only 32 months.



According to RealtyTrac, in the second quarter, homes took 318 days, on average, to go from a notice of default, the first stage of foreclosure, to lender repossession – that's up from 298 days in the first quarter. (New York leads in longest foreclosure process, at 966 days or 2.6 years; Texas has the shortest at 92 days.)

Nearly 1.9 million loans are 90+ days delinquent but not yet in foreclosure. Of these, 42% of owners have not made payments in over a year (average delinquency of 397 days), a new record. More than 4.9 million loans are 90+ days delinquent or in foreclosure, according to LPS.

*[Editor's Note: Pathfinder Raintree, our joint venture which acquires foreclosed homes in San Diego, CA from the banks and through short sales has observed a speeding up of bank's decision-making process in the past few months. What used to take six months now seems to happen in just two or three. A good sign, we think.]*

### **One Million Foreclosures Delayed Until 2012**

An estimated one million foreclosure-related notices for defaults, auctions, and home repossessions that should be filed by lenders this year will be pushed back until next year, according to a report by RealtyTrac.

While the delays could give home owners more time to catch up on their payments and try to avoid foreclosure, housing experts warn this means the looming shadow inventory of distressed properties likely will continue to plague the real estate market even longer.

“The best-case scenario is we don't get back to normal levels of foreclosure activity until

2015, which means the housing market recovery gets delayed by at least a year,” says Rick Sharga, a senior vice president at RealtyTrac.

### **August Existing Home Sales Rise to Five-Month High; Lower Prices, Interest Rates Attracted Buyers into Struggling Market**

Sales climbed more than expected, up 7.7% from the previous month to an annual rate of 5.03 million units, the National Association of Realtors said in September. The median price was down 5.1% from a year earlier.

The outlook for housing prices remains grim. A survey by MacroMarkets LLC showed economists expect home prices to rise just 1.1% a year through 2015. That is less than a third of the annual pace clocked in the 13 years that preceded the housing bubble, the survey found. A separate report showed applications for mortgages edged up in September on higher refinancing activity but were held back by a lack of demand for purchases, according to the Mortgage Bankers Association.

Existing home sales have headed lower in 2011 and prices continue to weaken. One factor keeping prices low is the high rate of distressed sales. Sales of foreclosed homes by banks and owners seeking to avoid foreclosures accounted for 31% of August transactions, up from 29% in July.

### **CMBS Delinquency Rate Hits Record in July, Down in August, Up in September**

The commercial mortgage-backed securities market seems to take two steps forward and one step back. The rate of CMBS loans 30 or more days past due or in foreclosure, which declined in May and June, climbed 51 basis points in July, according to Trepp, LLC. Then, it fell 36 basis points in August to 9.52% before inching up to 9.56% in September.

#### **Delinquency Rates**

<b>Property Types - % 30 Days +</b>			
	<b>Aug-11</b>	<b>Jul-11</b>	<b>Jun-11</b>
<b>Industrial</b>	11.24	11.09	11.68
<b>Lodging</b>	13.76	15.04	13.87
<b>Multifamily</b>	16.44	16.94	16.48
<b>Office</b>	8.17	8.17	7.35
<b>Retail</b>	7.38	7.85	7.82
<b>Overall</b>	9.52	9.88	9.37

*Source: Trepp, LLC*

The swings in delinquency rates may be driven primarily by changes in reporting standards. For example, special servicers now considering loan modifications simultaneously initiate foreclosure proceedings to expedite the process if the modification doesn't work out. This parallel path to problem solving increases the delinquency rate. Additional highlights from the report:

- Office loans 30 days or more past due spiked 82 basis points in July and remained unchanged in September at 8.29%;
- Multifamily loans remain the worst among CMBS loans with a 16.96%

delinquency rate in September. This is skewed because much of the multifamily distress is concentrated among a few very large properties – the top 10 delinquent multifamily loans represent \$5.7 billion in loans or 37% of the total delinquent balance in the multifamily category.

### **Many Banks Lending Again**

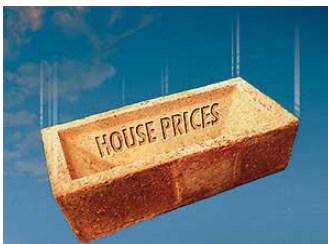
In the past, we've bemoaned the fact that banks, by and large, weren't lending. According to a new report issued by the FDIC, the severity of commercial real estate-related write-offs is gradually declining and lending is increasing. The report, based on data from the nation's 7,500 banks as of June 30, 2011, showed that banks continued to reduce commercial real estate loans on the books – primarily through loan sales, foreclosures and sales of foreclosed real estate. Meanwhile, new loans are rising, especially multifamily lending, which rose \$1.4 billion during the second quarter.

*[Editor's Note: There are nearly 1,000 fewer banks than at the start of the financial crisis in 2007. About 400 have been seized by the FDIC and approximately 600 have been merged with other institutions. Fewer banks means less competition, which also contributed to diminished lending these past few years.]*

### **Home Prices to Muddle Along Through 2015, Economists Say**

Economists, builders and mortgage experts are predicting the weak U.S. economy will continue to depress housing prices for years, leading to continued high foreclosures, limiting consumer spending and inhibiting a sustained economic recovery. According to a *Wall Street Journal* survey of 100 economists, the housing market is likely to remain under pressure through 2015. The survey was performed for MacroMarkets LLC, a financial technology company co-founded by Yale University economist Robert Shiller.

The survey finds that home prices are projected to decline 2.5% in 2011 and to increase just 1.1% per year through 2015. Nationwide, home prices have already fallen 31.6% from their 2005 peak, as measured by the S&P Case-Shiller 20-city index.



If the economists' forecast is accurate, housing will experience a "lost decade" in which home prices recover just a fraction of the losses they have sustained since 2005 between now and 2015, leaving millions of homeowners with little or no home equity. Aggregate homeowners' equity has fallen to 38.6% of home value from 59.7% in 2005.

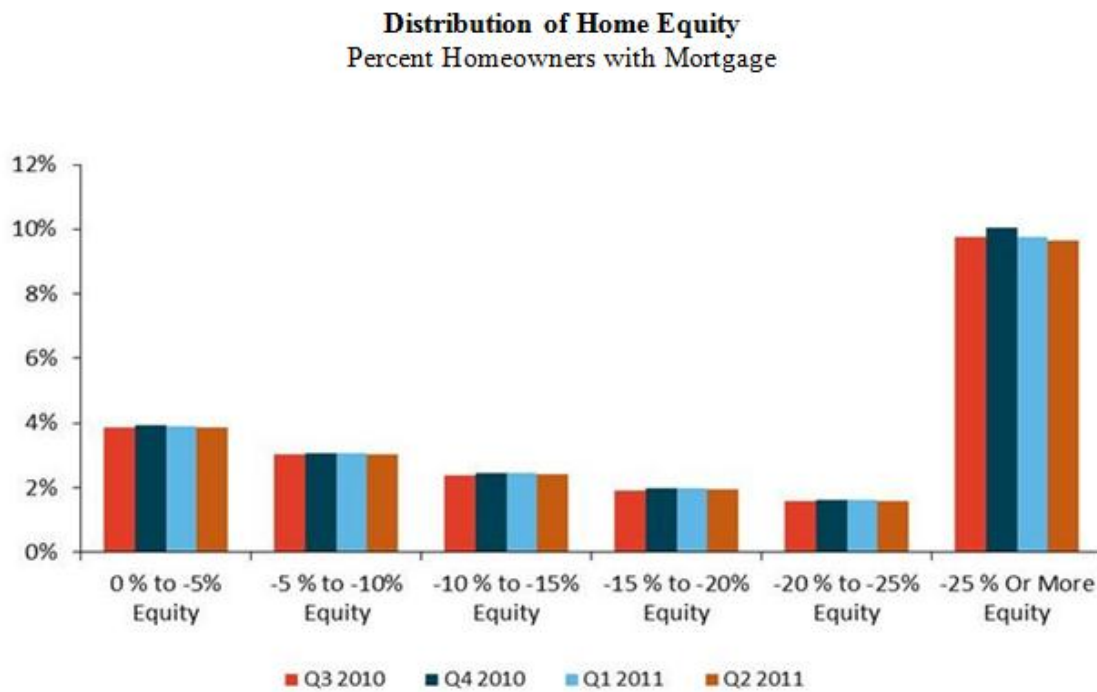
While mortgage rates have fallen to their lowest levels in decades, applications for home-purchase mortgages are mired near 15-year lows, according to the Mortgage Bankers Association. Applicants today face "a mountain of paperwork and never-ending re-verifications," said Stuart Miller, chief executive of home builder Lennar Corp., in an

earnings call Monday. Financing remains available to only “the most credit-worthy purchasers,” he said.

### 10.9 Million Homeowners with Negative Equity, per CoreLogic

CoreLogic released its second quarter, “negative equity” report in mid-September. It shows that 10.9 million or 22.5% of all residential properties with a mortgage were in negative equity at the end of the second quarter of 2011, down a smidgen from 22.7% in the first quarter. An additional 2.4 million borrowers had less than 5% equity, referred to as near-negative equity, in the second quarter. Together, negative equity and near-negative equity mortgages accounted for 27.5% of all U.S. residential properties with a mortgage.

Here are a couple of graphs from the report:



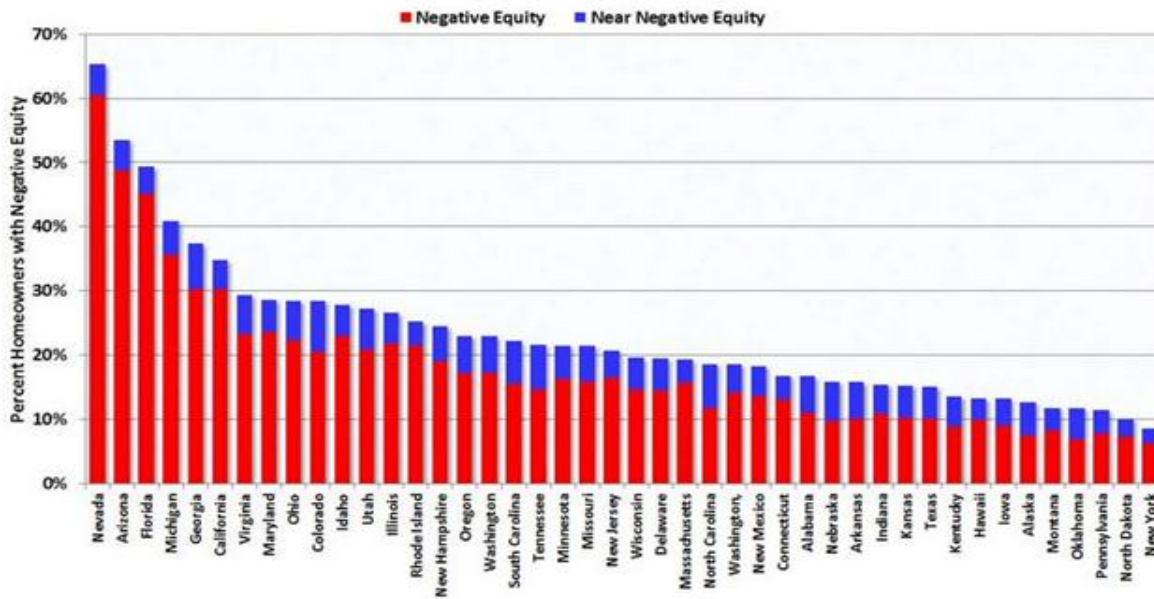
Source: CoreLogic

Nearly 10% of homeowners with mortgages have more than 25% negative equity. While this is trending down slightly, the decline is mostly the result of homes lost in foreclosure.

The graph below shows the breakdown of negative equity by state. Per CoreLogic, “Nevada had the highest negative equity percentage, with 60% of all of its mortgaged properties underwater, followed by Arizona (49%), Florida (45%), Michigan (36%) and California (30%).”

The negative equity share in the hardest hit states has improved. Over the past year, the average negative equity share for the top five states has declined from 41% to 38%. Nevada had the largest decline over the last year, with the negative equity share dropping from 68% to 60%. The reason for the Nevada decline, per CoreLogic is “the high number of foreclosures that led to lower numbers of remaining negative equity borrowers.”

**Percent Homeowners with Mortgage Negative Equity by State, Q2 2011**



Source: CoreLogic

*[Editor’s Note: As our friend Mark Hanson, housing guru extraordinaire points out, the true measure of distress is not only homeowners with negative equity but also those in a “near negative equity” situation. That’s because even if you have sufficient equity to break even on a sale, you need additional equity to pay the realtor’s commission and your closing costs as well as scrape up enough for the down payment on the next home. So, the problem is even larger than it appears at first blush.]*

### Phoenix Foreclosures Declining

Phoenix area foreclosures have been declining – from 43% of all home re-sales in January, 2011 to 31% in June, 2011. The rate is also down year-over-year – foreclosures constituted 36% of all re-sales in June, 2010.

Although the number of foreclosure pre-filings has declined for the past year, the pace of decline has slowed in recent months and foreclosures continue to be a substantial component of the market.

While lower prices, which Phoenix has seen for a number of years, improve affordability, they also negatively impact many potential sellers who find themselves “underwater” (owing more on their mortgages than their homes are now worth). Median prices increased from \$125,000 in May to \$126,500 in June, but median prices are well below June, 2010 levels of \$143,000. Median values for foreclosed properties showed similar declines – from \$155,600 in June, 2010 to \$132,000 in June, 2011.

*[Editor’s Note: Pathfinder believes sectors of the Phoenix market are bouncing along the bottom. We’ve made three multifamily acquisitions in Phoenix since July.]*

### **Economist Forecasts Steady Price Increases for Las Vegas Housing Market**

Economist Mark Boud, owner of Irvine CA-based Real Estate Economics, which tracks the Las Vegas housing market, says Vegas home prices (single-family homes, not condos or townhomes) will start rising in 2012 but won’t take off until after substantial jobs are created in 2014 and 2015. Las Vegas is the hardest hit housing market in the nation, with about one in ten homes currently vacant and an estimated 30,000 distressed homes either held by banks as inventory or in the foreclosure process, according to Boud.

Boud sees Las Vegas housing prices declining 2.6% in 2011 to a median price of \$133,175. That’s a 58% decline from the peak of \$316,575 in 2006. Boud sees prices rebounding from there – by 2.5% in 2012, 3.4% in 2013, 5.2% in 2014, 7.7% in 2015 and 8.8% in 2016, when the median price will reach \$174,500, Boud said. That’s 45% below 2006 levels – a decade later!

*[Editor’s Note: Las Vegas may be another “catfish” market, bouncing along the bottom, at least for entry level housing. Prices in Vegas were crushed during the real estate decline. Now, a friend who’s been buying foreclosed homes in Vegas for the past few years reports that prices paid at auction for the entry-level homes he targets have edged up from about \$40 to \$45 per square foot during the past couple of quarters.]*

### **The flip side of foreclosures – escalating apartment rents**

The national multifamily market continues to improve as average apartment rent increased to \$984 in the second quarter 2011, according to data firm RealFacts. Compared to the same period in 2010, asking rents rose 3.6% year over year and 1.5% over the previous quarter. Occupancy rates also increased slightly to 93.3% in the second quarter, slightly below the 19-year historical average of 94%. Based on the multifamily performance for the first half of 2011, rents nationally are expected to rise 3% this year.

### **Nearly 90% of New South Florida Condos Owned by Investors, Foreigners**

Only 13% of the 43,000 south Florida coastal condo units created and sold since during the real estate boom are owned by primary users who have filed for tax savings and added

property protection under the state's Homestead Exemption legislation, according to a report from Florida condo consultancy CondoVultures.com.

"This report finds that primary users account for only about one out in ten transactions in a new project in South Florida's seven largest coastal markets," said CondoVultures' Peter Zalewski. "Foreign investors with strong currencies and second-home buyers are clearly the lifeblood of the south Florida coastal condo market now. It is quite possible that a majority of the coastal condos built during the South Florida real estate boom are now being occupied by renters," Zalewski continued.



In Florida, residents are entitled to declare one Homestead Exemption, which provides considerable property tax savings and increased property right protections for full-time residents, on their primary residence. Investors and second-home buyers, who are more inclined to rent out their units, typically do not qualify for Homestead Exemption advantages in Florida. The study found that fewer than

5,500 owners of south Florida condos created since 2003 filed Homestead Exemptions. This means nearly 38,000 units are owned by investors and second-home buyers who are not primary residents, according to the report.

*[Editor's Note: San Diego realtors report that wealthy Mexican buyers have been scooping up multi-million dollar homes in La Jolla, Coronado and other garden spots like there's no tomorrow.]*

## **TRAILBLAZING: HUNTERS CHASE CONDOMINIUMS (PARKER, CO)** **Completing a stalled condominium project and providing quality housing**



*Hunter's Chase Condominiums*

The developer's original business plan for Hunter's Chase Condominiums nearly succeeded. His simple, straight-forward vision: to build and sell 60 reasonably priced and

stylish condominiums within a rapidly growing Denver sub-market. Everything went according to plan for the first 40 units, which were built and sold (the majority in 2005-2008) for average price of \$140,000. But, as the last 20 condos neared completion, the combination of a nationwide real estate meltdown and the developer's portfolio of struggling projects dealt a near fatal blow to the project.

As the developer was unable to complete the construction or keep the loan current, the project stalled. In 2010, the lender foreclosed and Hunter's Chase Condominiums became yet another victim of the nationwide real estate implosion.

Pathfinder leveraged its experience finishing partially built developments and acquired the remaining 20 units from the lender in April, 2011. Pathfinder completed construction in July and received offers on all 20 units on the opening sales weekend. The majority of the purchasers are first-time home buyers seeking newly constructed and reasonably priced condominiums.

The condos are all two bedroom, two bath units, ranging from 1,084 to 1,224 square feet. Each unit contains a washer/dryer, gas log fireplace, oversized walk-in closet and high-end appliance package. Additionally, eight of the units have detached one-car garages. By completing the construction quickly to take advantage of the summer sales season and dramatically resetting the cost basis, Pathfinder was able to complete a stalled development and provide quality, entry-level housing to the community.

## NOTABLES AND QUOTABLES

“Plain-vanilla, garden-variety business expansions and contractions that are influenced by the manufacturing inventory cycle tend to have recessions between five and ten years apart...This time, we are dealing with something different. This is a balance-sheet downturn...when businesses and households begin paying down debt and rebuilding the asset side of their balance sheets. Instead of spending, they save. It is a very natural thing to do but it hasn't happened in 80 years. And, it changes the whole nature of the economy. The U.S. economy has developed to provide goods and services to household spenders. That's why there are so many malls in America – ten times as much retail space per person as in France, for example. That's why such a large percentage of the U.S. population is employed in 'service sector' jobs – lending, selling, installing, maintaining and otherwise helping households spend money. Manufacturing may have declined in America but at least there was the service sector. The latest jobs report shows that even the service sector is no longer creating jobs like it used to. And no wonder. Consumer spending is slumping. It hasn't been so weak since WWII. Considering that population and price levels are still going up, an actual decline in consumer spending is a sign that the Great Correction is intensifying.”

- David Rosenberg, Chief Economist/Strategist, Gluskin Sheff &

Associates, Inc.

“The whole world is mad. Stocks will be dropping 30% and then rallying 20% and then dropping another 30% – that’s going to be the pattern. And whoever can’t live with that shouldn’t be buying equities at all.”

- Marc Faber, Publisher of the Gloom, Boom and Doom Report and a member of Barron’s Roundtable

“Those who are unaware they’re walking in darkness will never see the light.”

- Bruce Lee, martial arts expert and author

“After the next bout of coordinated global bank easing, I think we will transition into a slow, grinding, sideways market, rather than a repeat of the 2008 crash, and the bear market will bottom a few years from now as inflation rises and P/E ratios fall.”

- Dan Amoss, Editor, Strategic Short Report

“The Western world is in for a long slog through the muds of too much debt, bloated public sectors, sclerotic economies overburdened with regulatory costs and regulations and aging demographic trends.”

- Chris Mayer, Editor, Agora Financial

“People should understand that those who drink, those who smoke are doing more to help the state.”

- Aleksei L. Kudrin, Russian Finance Minister, encouraging people to drink and smoke more to help boost tax revenues

“Common sense is not so common.”

- Voltaire

There is no question that the momentum of the economy, leaving out the oil price issue, leaving out Euro problems that have emerged and very specifically leaving out the budget problems, this economy is really beginning to pick up momentum.”

- Alan Greenspan, former Chairman of Federal Reserve, whose low interest rate policy following the dot-com crash is now widely viewed as having sparked the housing bubble, which brought about the 2008 financial crisis and the ensuing Great Recession

“The future’s uncertain...but the end is always near.”

- Jim Morrison

“U.S. dollars have value because everybody thinks they have value. Everybody thinks they have value because in everybody’s experience, they have had value.”

- Milton Friedman, Nobel laureate economist

“Anything that cannot last forever, by definition, will not.”

- Ben Stein’s law (author and actor)

“We have a sense that bond investors are not being rewarded relative to the risks they are taking at the current moment.”

- Bill Gross, Founder and Co-Chief Investment Officer, PIMCO

“For centuries, banking was a respectable business based on names and reputations. Bankers were personally liable for their deeds and could be prosecuted down to the last cent. Being first in line to guarantee every risk, they were careful about whom they lent to. A bankruptcy often gave rise to a suicide, such was the dishonor. These days, the owners of financial establishments that go belly up are greeted with equanimity and invited to lunch. The big banks are limited liability companies that lend out other people’s money or speculate in it...After a career in finance, I look aghast on what has happened since the turn of the 21<sup>st</sup> century. The conclusion that I have come to is that the present financial crisis was caused by and is one of the most blatant manifestations of widespread moral decline in our society.”

- Georges Karlweis, former Chairman of Banque Privee Edmond de Rothschild, SA (Geneva)

“Lowering the cost of money in the middle of the yield curve will not put equity in the pockets of home owners who are underwater on their property. And it will not save the real estate market or put people back to work either. All the Fed has done is to guarantee that whatever paltry level of capital they have left – if any – will be gone once interest rates rise even slightly...this is a balance sheet recession which can’t be solved by creating another bubble in the bond market or by increasing the rate of inflation. In fact, all Bernanke has done is to ensure that once reality comes to the bond market, the pain involved with the adjustment process will be significantly worse. He has also ensured that the exit strategy – if there ever is one – will be much more problematic. Unfortunately, the Fed’s new dance will also ensure that inflation will be much more difficult to control.”

- Michael Pento, Pento Portfolio Strategies

“Never before in the history of time has more chaos been created in the name of stability.”

- Kevin Ferry, The Contrarian Corner

“Investors seem to be worried about owning anything other than canned goods.”

- Adam Sieminski, chief energy economist, Deutsche Bank, commenting on September 22, 2011 after two days in which the Dow Jones Industrial Average plummeted 675 points

“Adding to the challenge is the fact that banks are not lending...[they] are still holding cash and contracting lending activity...adding profits to their bottom lines, due partly from their ability to access money on the cheap, thanks to government backing of deposits, and by buying tradable assets such as government bonds. The inevitable too-big-too-fail taxpayer bailout, if something were to go wrong, is also quite reassuring for the large banks. In the ‘good old days,’ there was the 3-6-3 banking rule. Bankers would offer 3% interest to depositors, charge 6% on loans and then be on the golf course by 3pm. That rubric has now been replaced with a new one: give nothing to depositors, give nothing to those who want to borrow, buy tradable assets and get an easy 3% yield from government bonds.”

- National Association of Realtors Chief Economist Lawrence Yun, on the impact banks’ unwillingness to lend has had on the housing market

“[Bad debt] is dragging the nation’s economy underwater...in truth, we seem very paralyzed and slow to act...[policy makers and industry executives are] wasting time engaging in self-interested bickering while the housing market rots.”

- Lewis Ranieri, former Vice Chairman of Salomon Brothers, considered the “godfather” of the mortgage market for pioneering the mortgage securitization market. His comments were made during a speech in September, 2011 at a mortgage industry conference in which he warns of the growing risks of policy inaction

“The politicians obviously believe that the world will get back to good growth and great tax revenues [and the problems will be resolved]”. Hogwash – the likelihood of this scenario is right up there with winning the lottery.”

- Felix Zulauf, Zulauf Asset Management and a member of *Barron’s* roundtable, commenting on the Euro. Zulauf thinks a monetary union can only survive if the different member countries’ economies are homogenous or are a single fiscal and political entity, like the USA.

“With 9% unemployment, God could not get reelected.”

- John Mauldin, best-selling author and editor of *Thoughts from the Frontline* newsletter

## **Important Disclosures**

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Please add [msiegler@pathfinderfunds.com](mailto:msiegler@pathfinderfunds.com) to your address book to ensure that you continue to receive our notifications.