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## 2010 ECONOMIC OUTLOOK

### Real estate

By **STAN BULLARD**

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When real estate emerges on the other side of the recession, look for a more heavily regulated, slower moving business focused on fundamentals than before the deep recession the industry helped produce.

In short, "real" factors will dominate real estate.

That goes for buyers of properties ranging from Parma bungalows to skyscrapers in downtown Cleveland.

"Money makes the commercial realty world go around," said attorney John "Jack" Waldeck, chair of Walter & Haverfield LLP's real estate unit, though the role of money applies to the residential real estate world, too. In this case, money is debt, the lubricant of the illiquid property business.

With less debt available and lenders demanding larger down payments for everything from homes to shopping centers, shock waves from the credit crunch will redefine what people want in properties, how they value them and the size of the real estate business that serves them.

"Five years ago, mom's home was not good enough" for most of her home-buying clients, said Rachel Torchia, owner of Gateway Title Agency in Brecksville. Back then, buyers could secure loans for bigger homes than their moms and dads owned. Now, she sees family members snap up homes in their parents' estates.

"The buyers who close are just happy they got a house," Mrs. Torchia said. "We're back to the '70s, where people buy a house with a plan to move up. They hope to get (just) enough (profit) to get into their next house."

David Sharkey, vice president of the Progressive Urban Real Estate residential brokerage in Cleveland, notes a similar shift in outlook.

"Real estate as investment used to be top of mind for home buyers," Mr. Sharkey said. "People were thinking, 'What can I sell it for in a few years?' Now the only ones who talk about (residential) real estate as an investment buy houses and rent them out for income."

Meanwhile, the constrained capital environment will change commercial real estate. Cash will be king, or queen. With more of their own or investors' cash in deals, developers and owners will be more cautious. Fundamentals, such as rent, will dominate the business again.

Look, too, for lower commercial property sales, and lower prices and values, based on the cash flow estimates lenders will accept to determine value. No longer will oversize loans promote higher prices.

"Investment real estate will be sold based on what the rent is. Cash flow estimates will be adjusted for what the market really is," said Robert Garber, a principal of Cresco Real Estate, a commercial brokerage in Independence. "It's going to take more (equity) to get deals done. It will take longer."

The crucial item will be how much — or how little — debt is available.

David Browning, managing director of the Cleveland office of CB Richard Ellis, doesn't think the pendulum will swing to cash-only deals becoming common among multimillion-dollar properties. But it will swing.

"To do real estate deals, you have to have equity and you have to have debt," Mr. Browning said. "You can't just give up. The lesson (of the financial crisis) is to be conservative."

### **Weeding-out time**

Fewer sales and lower selling prices plus properties fetching lower rents for shorter terms in a weak economy mean lower fees for sales and leasing agents and other service providers. More paperwork from increased regulation will slow down how quickly deals close, reducing volume and trimming profit margins.

"Some of the weaker players are being weeded out," said George Hutchinson, CEO of consultancy Allegro Realty Advisors in Independence. The result: fewer brokerages, fewer brokers, fewer service providers and fewer owners, with the latter owning more properties.

Real estate will regain vigor when economic fundamentals regain power, said Warren Morris, CEO of Ostendorf-Morris Colliers of Cleveland. "Our business does not come back until the jobs come back," he said.

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