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Weekly review

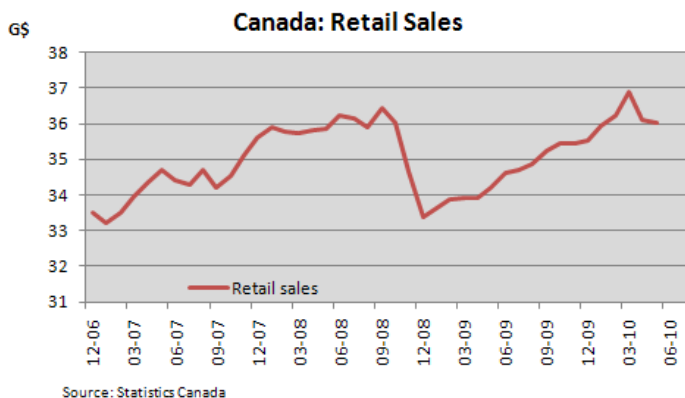
Otéra



Financial news

In Canada, according to Statistics Canada figures issued on July 22nd, retail sales unexpectedly slid back 0.2% in May (in current dollars), after a 2.2% drop in April. These two decreases came after five months of steady increase. Sales slumped in six of the eleven retail sub-sectors during the month. The most dramatic decline was 4.1% (in dollars) posted by construction material merchants. In Quebec, retail sales decreased 1.8%, essentially because of dwindling auto sales. This figure combines with housing sales, building permits and the jobless rate to forecast much slower economic growth in the second quarter (estimated at 2%). The longer Canadian consumers wait before opening their wallets, the longer it will take for the pace of the economy to pick up again afterwards.

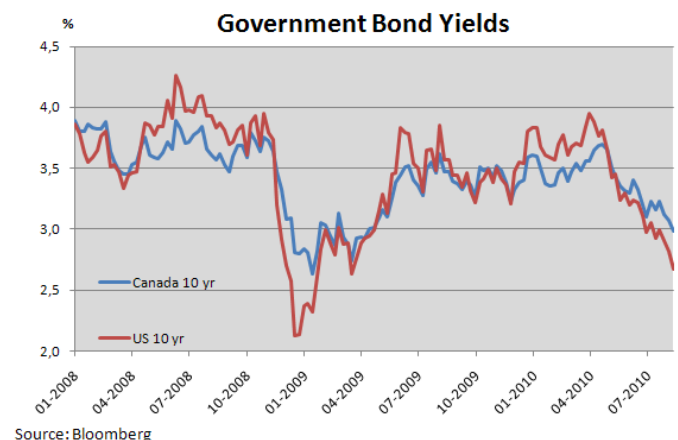
In the U.S., the American Federal Reserve, at the latest meeting of the Federal Open Market Committee (FOMC) on August 10th, surprised no one when it opted for the status quo and decided to keep the target range for its key interest rate at 0% to 0.25%. The Fed remains determined to support the stabilization of the financial system and proper functioning of the markets by reinvesting the sums collected on long-term bond securities coming to maturity (i.e. MBS) and resuming the purchase of Treasuries, thereby obviating the need to tighten monetary conditions anew. Despite some mitigation of the current crisis in European public finances, a number of disappointing economic statistics (e.g. the job and housing markets, the trade balance, and under-utilization of production capacity) have prompted the Fed will to keep its key interest rates exceptionally low for some time to come.



The bond market

This latest round of disappointing statistics regarding the U.S. economy and the simultaneous slowdown in worldwide economic recovery have pushed investors into hedge securities. These concerns helped maintain the downward trend of long-term bond rates. The Canadian ten-year bond rate posted a drop of 9 b.p. to end the week at 2.99%, while its U.S. counterpart dropped 15 b.p. to 2.67%.

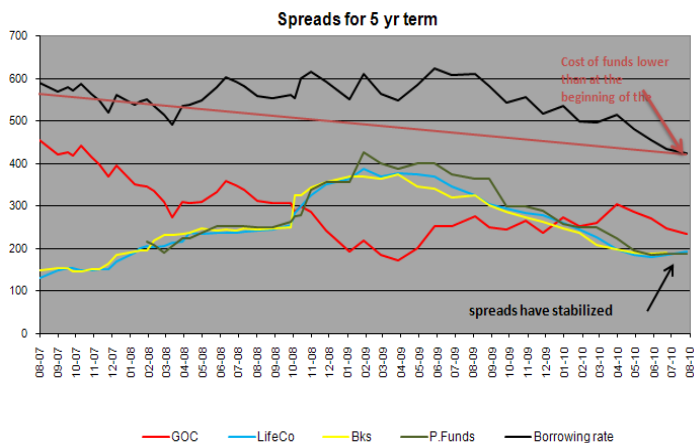
On July 20th, to no one's surprise, the Bank of Canada (BoC) raised its key interest rate 25 basis points (b.p.) for the second month in a row, and this rate now stands at 0.75%. In the press release announcing its totally expected decision, the BoC reminds market watchers that "Given the considerable uncertainty surrounding the outlook, any further reduction of monetary stimulus would have to be weighed carefully against domestic and global economic developments." The translation of this excerpt is that the BoC now feels that the Canadian economy will not hit its full stride until Q4 2011, and it has somewhat lowered its economic forecasts. It is accordingly giving itself six months longer to bring key interest rates to some sort of short-term neutrality, which most economists agree would lie somewhere between 2% and 3%. Despite the recent weakness of certain indicators, the interest rate level remains exceedingly low in Canada in light of the fact that economic recovery is considered well under way.



The debt market

After 15 consecutive months of decreases, commercial mortgage credit spreads are showing signs of stabilizing in Canada. Although 5- and 10-year spreads had reached respective peaks of 379 and

417 b.p. above GoC bonds in February 2009, they shrank back down to 185 and 200 points above GoC by late May 2010. The latest Otéra survey, dated August 2nd, reveals a slight increase in spreads of 5 to 11 b.p. compared to May. This increase was not strong enough to offset the substantial drop in bond rates, however, which means that mortgage rates are lower than ever (4.23% and 5.24% for 5- and 10-year terms). Second mortgages on quality properties are finding more and more takers. Mortgages featuring conservative ratios, quality borrowers and sound collateral are being offered at rates ranging from 7.5% to 9.5%. Construction loans, for their part, remain at CDOR + 350 to 400 b.p., although with a floor of 5.5% for certain lenders.



In the U.S., according to the Giliberto-Levy Commercial Mortgage Performance Index, commercial mortgages produced overall returns of 4.7% in Q2 which compare favourably with the 2.45% figure posted in Q1. The total return over the trailing twelve months is at 16.6%. This commendable performance can be explained mostly by the renewed demand for U.S. government bonds (thereby pushing yields down) and, to a lesser extent, by the current performance of commercial loans. Credit spreads on such loans appear to have remained fairly stable during the quarter. Ten-year loans (60-65% LTV), for their part, stood at 248 b.p. for the office sector, 207 b.p. for the multi-family residential sector and 247 b.p. for the industrial.

The volume of newly delinquent CMBS loans dropped for a fourth consecutive month in July, states Fitch Ratings, but nevertheless raised the delinquency rate from 8.14% to 8.25% last month. “Despite the slowdown in volume, loan defaults have not yet peaked,” said Fitch Managing Director Mary MacNeill. “Further weakness in loan performance is likely, particularly among later vintages.” Also in July, the 60-day+ delinquency rate for CRE CDOs in the U.S. decreased from 12.2% to 12% in June. This drop does not reflect an improvement in credit performance but rather the liquidation of delinquent assets, often at a heavy loss.

Still in the U.S., six new CMBS issues totalling US\$6.3 B should soon see the light of day and thus restore some measure of hope to a new issuance market that has been more than anaemic. J.P. Morgan has decided to follow up its June issue with another one in September, equally of the conduit type, for a sum of US\$1.2 B. Although Ladder Capital had chipped in 22% of the loans making up the collateral of the previous issue, this time the bank is alone. Deutsche Bank is also on line to issue a deal of US\$800 M towards the end of September, which would include collateral from Ladder Capital and Natixis. Likewise, Wells Fargo, Bank of America and Basis Investment will be

joining forces to bring to the market a multi-borrower issue of US\$850 M, anticipated for October. Three other single-borrower issues may also come out in the fall: the first, an offer of US\$2 B by Centerbridge Partners, will be used to sell off mortgages inherited when Extended Stay Hotels was restructured. The second is an US\$800-M issue secured by a Manhattan office building (245 Park Avenue), and the third is a US\$660-M issue that J.P. Morgan is apparently cooking up for Centro Properties (shopping centres).

The secondary American CMBS market remained fairly calm last month with only limited fluctuation of the spreads. The trend towards smaller spreads is continuing despite the volatility stemming from the capital markets and the mixed economic news of the last few weeks.

| Fixed Rate (Conduit) | Avg. Life | Spread (bp) | | |
|----------------------|-----------|-------------|--------------|------------|
| | | 8/11 | Week Earlier | 52-wk Avg. |
| AAA | 5.0 | S+173 | S+169 | +230 |
| | 10.0 | S+335 | S+330 | +439 |
| AA | 10.0 | S+2,438 | S+2,431 | +2,837 |
| A | 10.0 | S+2,975 | S+2,966 | +3,460 |
| BBB | 10.0 | T+4,195 | T+4,177 | +4,981 |

CMA, August 13, 2010

The average price of commercial properties in the U.S. has grown 8.6% since the market bottomed out in October 2009—at least so says the Moody’s/REAL commercial property price index (CPPI). The CPPI in fact posted its third month of increases in May (+3.6%). Its aggregate value, however, remains 38.9% lower than the peaks attained in 2007. The CPPI’s price monitoring, is based on repeat sales transactions. In May, for example, 107 repeat sales were surveyed, as compared to 114 in April, but for a total of US\$1.5 B—almost double the \$800 M posted in April. The volume can be considered low if compared to the number of transactions before the economic crisis, which affects the indices’ reliability somewhat. We can therefore still expect some fluctuations on that score.

