Venture Pays $40Mln for D.C. Offices; Assumes $33.15Mln of CMBS Debt

Commercial Real Estate Direct Staff Report

A venture of Davis Cos. and American Real Estate Partners has paid $40 million for two adjoining office properties with 114,473 square feet in downtown Washington, D.C.

Guardian Realty Investors of Bethesda, Md., sold the properties: 1140 19th St. NW, which has 65,275 sf, and 1146 19th St. NW, with 48,198 sf. The deal was brokered by Cassidy Turley and includes 50,000 sf of additional development rights.

The properties back $33.15 million of debt that matures next June and was securitized through JPMorgan Chase Commercial Mortgage Securities Trust, 2007-LDP12.

Davis Cos., a Boston investment manager, and American Real Estate, a Herndon, Va., investor with leasing and construction capabilities, assumed the debt, which requires only interest payments and has a 5.749 percent coupon.

The venture will be in the market for replacement financing before the debt matures. In the meantime, it plans a major renovation of the properties.

Jonathan Davis, chief executive of Davis Cos., said the deal continues his firm's established strategy of "acquiring B-class properties in A-class market areas and bringing the assets up to A levels." The two buildings are indeed class-B properties near the middle of Washington's central business district, within three blocks of Dupont Circle and two mass transit stations.

Davis said the venture is planning to renovate the buildings' façades and common areas, as well as improve management levels. The venture is also trying to determine if and how it would use the development rights it acquired to expand the properties.

He also said that Davis and American Real Estate are in the market to joint venture on other value-add office property investments in the Washington, D.C., area.

The two properties' combined $2.28 million of net cash flow last year was 1.17 times the amount need to service their debt. However, the 1140 building's $1.03 million of cash flow last year was just 97 percent of the debt-service requirement for its $19.8 million portion of the debt, according to servicer data compiled by Morningstar, formerly Realpoint.

The properties' combined 90 percent occupancy rate compares to Washington's overall 89.7 percent occupancy rate in the first quarter, according to Cassidy Turley. The brokerage expects the market's occupancy to increase to at least 92 percent by next year because of increasing demand and virtually no new construction activity.

Davis Cos. is invested in the venture on behalf of its first investment fund, Davis Investment Ventures Value Opportunity Fund I, which raised $230 million of equity commitments last year and has been expected to use leverage to a level that would boost its overall investment capability to $1 billion.

The Washington deal is one of the few conventional equity investments by the fund, which has focused on acquiring debt that it can foreclose on to take the underlying collateral or from owners that obtained their assets through foreclosures.

The fund acquired the Valley Forge Office Center, a 258,345-sf complex in Wayne, Pa., after buying and foreclosing on its $44 million of debt that had been securitized through Credit Suisse First Boston Mortgage Securities Corp., 2005-C5. It paid $32 million for the debt.

The loan matured last year without being paid off by the property's previous owner, Keystone Property Group, which acquired it in 2005 for $64 million. The suburban Philadelphia complex, at 530 and 580 Swedesford Road, is fully leased through 2015 and has been generating about $4 million of annual cash flow. But tenants occupying about 90 percent of its space have vacated, leaving the property essentially dark.

The Davis fund is expected to try to buy out the leases of the tenants that have vacated, GE Transportation Logistics and Independence Blue Cross, as well as reposition the property. The repositioning, like the planned work in Washington, would include installing a new façade and general upgrades to common areas.

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