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Investors to take big hit in Naperville office sale

By [Ryan Ori](#)



Washington Pointe, a four-story building along Interstate 88, is selling for less than half its price eight years ago. Photo from CoStar Group Inc.

After netting huge returns on its last distressed office deal in the western suburbs, a Boston real estate investment firm found another one: a half-empty building in Naperville.

A venture of Davis Cos. has a deal to buy Washington Pointe for about \$85 per square foot, or about \$14 million, according to people familiar with the transaction. The four-story building at 535 E. Diehl Road, along Interstate 88, is selling for less than half its price eight years ago.

Davis, known for buying distressed properties at a discount and turning them around, hopes for a repeat of a deal it pulled off in Oak Brook. The firm was part of a venture that bought the two-building Crossings complex in 2010 for about \$20 million in a deed-in-lieu of foreclosure deal. After leasing up the property, Davis and Northbrook-based partner Arthur Goldner & Associates Inc. sold the complex last year for \$35.7 million.

The price for the Naperville property represents a steep discount to the \$30.9 million a group of investors advised by El Segundo, California-based Griffin Capital Corp. paid for the 163,623-square-foot structure in 2006 during the pre-recession peak.

'HOPE NOTE'

The Griffin venture's 2006 acquisition was backed by a loan that was packaged into a commercial mortgage-backed securities (CMBS) offering for investors. By 2010, after the loss of tenant Millward Brown, a marketing firm that leased about 41 percent of the building, the Griffin venture faced a \$23.2 million foreclosure suit.

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With the four-story building's appraised value down to \$10.5 million, the owners negotiated a modification on debt that matures in 2016. The debt was split into a \$12 million loan that continues to collect interest and an \$11.2 million interest-free "hope note," a type of loan workout used by loan servicers unwilling to take back a distressed property after its value has plunged. The goal is to allow time for the property to regain some value, cutting investors' eventual loss.

"Instead of foreclosing immediately and selling into a bad market, they hoped to buy some time and eventually get some return on the hope note," said Joe McBride, an analyst at New York-based research firm Trepp LLC. "It wasn't a bad strategy by the special servicer. Recently we've seen them getting more and more of their money back in areas where property values have recovered more quickly."

SUBURBS SLOWER

Suburbs have been slower to bounce back in many areas of the country, though. Locally, suburban landlords have slowly pushed down overall vacancy to 23.4 percent during the third quarter, according to Chicago-based Jones Lang LaSalle Inc. — a nearly six-year low, but still a long-way from pre-recession levels below 20 percent.

The sale price implies Washington Pointe regained some value since hitting bottom, but not enough to prevent the hope note from being almost entirely wiped out.

"There have been cases recently where the hope note has been paid off entirely, which is a good sign," Mr. McBride said. "But these suburban offices are having a tough time in a lot of markets."

The Griffin venture is being represented in the sale by Paul Lundstedt and Dan Deuter of Los Angeles-based CBRE Inc.

Davis founder and CEO Jonathan G. Davis declined to comment, and a Griffin spokeswoman did not return a call.

The Griffin venture was unable to add tenants at underwritten rents because "other office properties are offering competitive rates and undercutting their basis," according to commentary from a Trepp loan report. The property's cash flow is too low to cover debt payments, with vacancy at 50 percent, according to the report.