

The

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Commercial Joins the Credit Meltdown

It was inevitable. The consumer induced global credit crisis, beginning with the subprime residential mortgage nightmare and closely followed by heightened defaults in most other forms of consumer lending, has taken hold of commercial real estate lending. The severity of the problem has virtually shut down what was previously a very liquid market.

Where financial institutions were once able to sell loans and re-lend the proceeds of those

Over the past 90 days, our lending market has changed dramatically.

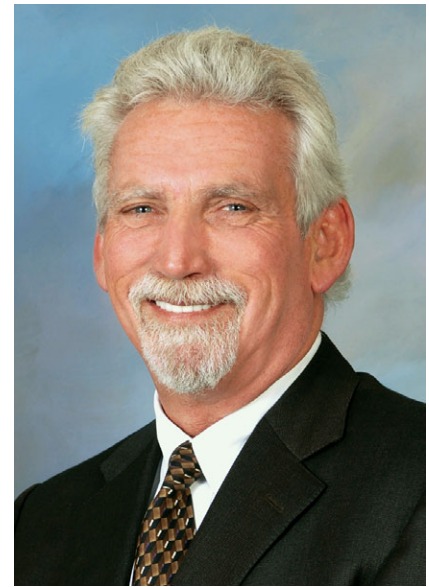
sales, over and over, no viable market currently exists for the sale of most any type of loan.

The almost universal decline in residential real estate values is beginning to spread to the commercial sector. Over the past 90 days, our lending market has changed dramatically.

A recent Federal Reserve survey of senior loan officers in banks is telling. **Eighty percent** of the banks responding indicated that they have tightened terms on commercial real estate loans.

This is the highest percentage since this question was added to the survey in 1990. Over one half of the banks responding reported weaker demand. The survey covered the 90 day period ending January 31, 2008. This is consistent with our experience in our lending area.

News reports are beginning to surface indicating increased defaults with loans packaged in commercial mortgage backed securities, the commercial cousins to securities stuffed with those wonderful subprime residential mortgages that have



Jim Davis, President, Southland EDC and NADCO Director At-Large

thus far resulted in something like \$100 billion in losses worldwide. And that story hasn't come close to playing out yet.

We can only hope that holders of the commercial backed securities don't suffer losses of the same magnitude.

The result for the 504 Program has been a mixed bag. Thanks to the government guarantee, the securities our loans are placed in each month still have buyers.

The bad news, though, is the higher interest rate spread demanded by investors, due to the uncertainty caused by

Continued on page 2

Inside

- **President's Message**
- **Jim Davis to Run for Re-election as NADCO At-Large-Director**
- **Robert Dodge honored with SBA Director's Award of Excellence**
- **Welcome New Staff Member, Stephanie Arrazola**
- **Staff Directory**

President's Message, *continued from page 1*

the credit crisis, has resulted in higher interest costs for our borrowers that wouldn't have been there were it not for the current crisis.

To my knowledge, there hasn't been an appreciable increase in 504 loan defaults.

Thankfully, the impact of this added spread has been negated by the recent Federal Reserve interest rate cuts. And, to my knowledge, there hasn't been an appreciable increase in 504 loan defaults. However, the situation is tenuous.

We haven't seen any problems in our loan portfolio as of yet. In fact, our delinquency rate is currently lower than it was a year ago. But with the current credit environment and the economy headed for what I believe is a certain recession, problems will arise, no matter how good your credit analysis is.

Loan quality is more important than ever.

For the preservation of the 504 Loan Program, it is absolutely critical that we, as an industry, acknowledge the realities of the economy and the pressures on real estate values, and lend accordingly.

The 10% equity cushion in our typical transaction doesn't go very far in today's market. Anyone who bought a sub-prime based mortgage bond will vouch for that. It's not a time to chase numbers; it's time for restraint, for sound underwriting, for quality loan transactions.

It is absolutely critical that we, as an industry, acknowledge the realities of the economy.

I don't know about you but after all that has happened over the past year in the credit markets, I'd have a difficult time sitting before a congressional committee and saying I didn't see it coming.■

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**NADCO Members:
There's an Election Coming...
No, the Other One.**

Since last May, it has been an honor and a privilege to represent the NADCO Membership as an At-Large Director on the NADCO Board.

We have accomplished a lot in those few months. On the tech issues front, we provided the SBA with a comprehensive update and revision of SOP 50 10 4.

I chaired the group working on Sub-Part A of the SOP wherein we integrated all changes and updates provided in tech issues memos since the original SOP was published in 1999! A monumental undertaking, we assembled a group of experts from the CDC industry that did a superb job.

We presented this body of work to the SBA last June. It would become the starting point for the agency to begin the re-write of this outdated and extremely cumbersome document. The new 50 10 SOP should be out of SBA clearance and out for comment early this spring.

Apparently, the SBA liked what they saw. Not only did they tell us so, they have since asked for a similar review of the loan servicing SOP, 50 50 4. So the tech issues committee is at it again, with a scheduled completion of the project this March.

As an At-Large Director, my responsibility extends to the entire membership of NADCO.

I promised to attend all of the NADCO Regional Meetings and was able to follow through on the promise. I had an opportunity to meet with many of you to discuss your needs and concerns and bring those issues to the Association. Three meetings in a little over five weeks are a bit much but thanks to my superb staff, I was barely missed. Wonder what they are trying to tell me?

Our individual success depends on the actions of all CDCs.

Perhaps most important to me were the issues of loan quality and ethics becoming high priorities of the Association for fiscal year 2008. I've ranted about these issues for years

Southland EDC Staff News

and made them my campaign emphasis last year.

In that our individual success depends on the actions of all, quality was and continues to be a major priority if we want the 504 Program to grow and succeed. Prudent loan making has never been more important than it is now, given the state of the economy and the global credit markets.

We must do all we can to influence our peers to make quality loans and support the SBA in its oversight efforts.

Much has been accomplished but there is still much to do.

I have therefore decided to run for re-election for At-Large Director this year. We must keep the pressure on those who believe loan numbers are more important than loan quality.

More than any time in the past 6 or 7 years, credit quality is most important. To me, with all that's going on in the credit markets, this seems obvious. And yet, there are still those CDCs who are selfishly driven by principals that may prove destructive to the entire industry.

I hope I can count on your support.



Robert Dodge Wins Award

Robert Dodge received the *Director's Award of Excellence* from Adalberto Quijada, SBA Santa Ana District Director. ■



Welcome New Staff Member, Stephanie Arrazola

Stephanie, our new Loan Closing Coordinator, is a recent graduate of California State University at Fullerton where she received a Bachelor of Arts in Business Administration. Her personal interests include reading, shopping, watching movies and traveling. ■

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