From the Washington Business Journal:
https://www.bizjournals.com/washington/stories/2010/08/02/story2.html

Distressed real estate funds come up empty

In the D.C. area, investors are finding there aren't many deals to be had yet

Aug 2, 2010, 12:00am EDT **Updated: Jul 30, 2010, 1:58pm EDT**

Back in 2009, the real estate vultures started circling, amassing cash to descend on the acres of commercial property expected to fall victim to the recession.

In Washington, investors formed several funds aimed at buying all this so-called "distressed" property. So far, many of those funds are flush with cash, but lean on actual investments, as Washington has mostly eluded the national real estate crash and lenders have held onto larger distressed properties.

Real estate opportunities in general are so few and far between, in fact, that some would-be investors are loathe to put their money in real estate investment funds at the moment.

Potomac-based Willco Cos. was expected to close its first fund last summer, but the commercial property development and investment company has yet to raise its $100 million target.

And that seems to be OK with them.

“I love the fact we are still in fundraising mode,” said Jason Goldblatt, Willco’s chief operating officer. “We are raising money not for the market we are seeing now, but really a market that’s six to 12 months out from now. I expect fundamentals to improve and markets to loosen up a bit to let us be active buyers.”

Eventually, the company plans to use the fund to target $250 million worth of investments — preferably in the kind of leased-up property that produces income for investors.

The fund currently has just $20 million worth of commitments, but Goldblatt expects to hit the $100 million mark in about six months.

Like Willco, other companies that announced ambitious plans in 2009 to pick up Washington-area real estate have yet to execute them.

About year ago, Marcus Partners closed on Marcus Capital Partners Fund I, a $210 million fund to invest in metro areas east of the Mississippi.The Boston-based real estate investment company promised to target a mix of properties — including office, biomedical, medical office and light industrial properties — but it has yet to use any of the money in D.C.

“The reality is the market has turned out to be a lot different than everyone would have hoped,” said Kyle O’Connor, who manages the fund and oversees the company’s investment activities in the D.C. and mid-Atlantic region. “It doesn’t mean you can’t invest, but it means if you had a narrowly defined focus, you may find a problem.”

The fund has been actively pursuing investment office space in such areas as Tysons Corner and north Bethesda. The problem, O'Connor says, is competition. The company was one of the finalists for The JBG Co.'s troubled Tycon 2 and Tycon 3 buildings in Vienna but lost out in a multiparty bidding war.

Here's just how much less distressed Washington is than some other parts of the country: LNR Corp., one of the nation's largest special servicers handling troubled loans, uses just one office to handle all of the distressed property between Boston and just south of D.C. By comparison, LNR has another office for distressed property in Atlanta alone.

All of that means the relatively scarce distressed properties in D.C. flash through the market like a summer storm, as evidenced by the high interest behind the Tycon 2 and 3 buildings, which were 69 percent and 38 percent vacant. (Investors like to see high vacancies in desirable locations like Tysons, because they present an opportunity to "add value" by adding rent-paying tenants.)

"For folks sitting on money today, it's difficult to find deals," Goldblatt said.

If anything, most of the assets swirling the market today are what real estate pros like to call "core-oriented deals" — established properties in desirable locations like 2175 K St. NW and 1225 Connecticut Ave. NW — which fund buyers often dismiss because there's no "value-add" opportunity to earn big returns by improving the property's situation, say real estate sources.

There hasn't been a drought of investment fund deals, however. Active investors like Angelo, Gordon & Co. and Rockpoint Group have been able to close several big deals this year, including the Shops at Georgetown Park and Washington Harbour, respectively. But only one of those — Georgetown Park — was distressed. It fetched three bids.

Another reason distressed deals have been hard to come by is because lenders have been slow to foreclose on struggling owners, often opting instead to extend the loan's due date.

That may be changing now, say those in the market. "We are seeing lenders start to make decisions, so there have been a lot of lender auctions," said Andy Glick, a principal at Rock Creek Property Group LLC, which used its 8-month-old $21 million fund to buy Pear Tree Village Center in Alexandria last year.

Glick is optimistic another purchase will occur in the next six months. "Every day it seems like there is a new opportunity we are evaluating," he said.

For year-old funds that have yet to buy Washington property, it's not time to freak out — yet. More than 270 loans financed with commercial mortgage-backed securities — and even more financed through traditional lenders — will need to be refinanced over the next two years.

"We are so early in the life of the fund," said Marcus Partners' O'Connor. "If we haven't put out a lot of money by 2013, that's an issue, but that's a long way off. The prudent thing to do is not try to make all your investments in 2010."