DISTRICT OF COLUMBIA
BUILDING INDUSTRY
ASSOCIATION

Testimony of
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"Credit Crunch: Hearing on the Effects on
Federal Leasing and Construction"
Before the Subcommittee on Economic Development
Public Buildings and Emergency Management
Eleanor Holmes Norton, Chair

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2167 Rayburn House Office Building
Washington, DC

Good Morning Congresswoman Norton and members of the Subcommittee on Economic Development, Public Buildings and Emergency Management.

I am Steven Grigg, President of Republic Properties Corporation. I am testifying today in behalf of the District of Columbia Building Industry Association (DCBIA) as past president and as a member of its Executive Committee. DCBIA is a not-for-profit organization, representing nearly 500 real estate development firms and related businesses in the District of Columbia.

As today's headlines make clear, the credit crunch is having a direct and broad impact on the development, leasing and management of commercial office space nationwide. The District of Columbia and the National Capital Region are neither distinct nor immune from those problems.

The collapse of conventional debt financing for development projects and the permanent financing market are working in tandem to make new development or major renovations of existing buildings much more difficult and expensive. With the collapse of securitized debt markets, and with the values of existing loan portfolios in doubt, lenders have become reluctant to assume any new risk, underwriting standards have tightened, and loan to value ratios have shrunk.

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The result is higher borrowing costs and higher levels of required equity participation – if capital funding is available at all. Meanwhile, equity investors are re-pricing their conceivable participation to reflect higher perceived risk.

The Federal Government ("Government") is a major user of office space and is not immune from the impact of this credit crunch. It is probable that the Government has not seen the impact of the credit situation thus far as existing vacant space is absorbed-up; however, that will inevitably change. Larger procurements, with prospectus level rents that were established some time ago, are going to see less competition now and going forward.

The Government is a special class of user for commercial office space; hence, Government leases are essentially "flat" for various terms. Space leased by the Government used to be advantaged by steady, prompt payments for rent. The margins associated with rental income have declined as a result of problems in the timing and amount of reimbursements for increases in real estate pass-thrus and operating expenses, which are indexed to CPI increases. Both of these business realities and underwriting standards have increasingly noted these changes in dealing with Federal Government leases and occupancies. Either the system has to change – or face rents will have to dramatically increase to reflect these conditions.

The Government's Prospectus rent levels and expectations of various tenant agencies will have to be adjusted upward in the future. While we believe that availability of financing will eventually be eased, the effective increased costs will become more predominant over the coming years.

Thank you for your attention. I would be pleased to answer any questions.