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The Economos Group is the Largest Seller of Office Buildings in Orange County

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THE PROPERTY REPORT

Maguire's Poor Timing May Lead to Subprime Trouble

Buildings Recently Bought From EOP Contain Batch Of Lenders in Shaky Sector

By JENNIFER S. FORSYTH

Investors in **Maguire Properties Inc.** are hoping St. Patrick's Day brought this real-estate investment trust some Irish gold, because over the past few weeks all they have seen is bad luck.

Late last year, Maguire put itself on the auction block, hoping to take advantage of the high prices that private-equity firms were paying for REITs. But even as other REITs sold at a feverish pace, Maguire couldn't find any takers at its price. In February, it conceded as much, saying it was better off "continuing to run the company publicly."

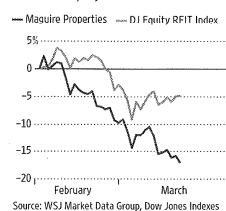
Now more bad news. On Feb. 20, Maguire said it would pay \$3 billion to buy 24 buildings that **Blackstone Group** acquired in its recent deal for Equity Office Properties Trust. The buildings were in Maguire's backyard of Southern California, one of the country's strongest office markets.

But it turns out about 10% of the tenants in the EOP Orange County properties are subprime mortgage lenders—an industry that has nose-dived in the past few weeks. Maguire's stock price has taken a tumble as well—down 16% since Feb. 1, compared with a 5% drop for the REIT sector.

"It almost points to unbelievably

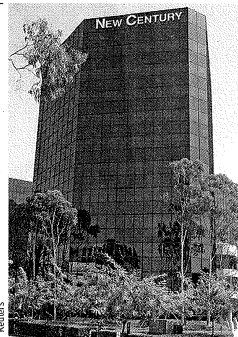
Subprime Suffering

Maguire Properties share performance vs. the DJ Equity REIT Index



Source: WSJ Market Data Group, Dow Jones Indexes

New Century leases space in this Irvine, Calif., building from Maguire Properties.



REUTERS

poor timing in buying the EOP portfolio," says Michael Knott, senior analyst with Green Street Advisors, an independent trading and research firm based in Newport Beach, Calif.

Even without EOP, Maguire would be wrestling with the subprime-lending fallout. Orange County-based **New Century Financial Corp.**, a REIT that was the second-largest lender to subprime mortgage borrowers, leases about 267,000 square feet in two Maguire buildings at Park Place in Irvine, and is scheduled to be lead tenant in a 20-story building Maguire is developing at 3161 Michelson, also in Irvine. New Century can get out of its leases

only if it files for bankruptcy protection.

Maguire's chief executive officer, Robert Maguire III, was unavailable for comment. But in public statements he presented the leases with subprime lenders as a potential opportunity: If these tenants cancel their leases, Maguire can sign up new ones at higher rents. For example, rents now are 25% higher than the \$35.27 per square foot New Century is paying for the top floors of 3161 Michelson, the company says.

Real-estate experts agree that Southern California will perform well over the long term, but they worry that the market could go through a short-term shakeout, particularly in Orange

County, if many mortgage companies return sublease space to the market.

Maguire's story looked very different just four months ago. At a time of fevered merger activity, Maguire directors believed it was prudent to pursue "strategic alternatives"—meaning a sale of the company. On paper, the Los Angeles REIT seemed a delectable morsel for a real-estate-hungry private-equity firm. After all, Maguire held a string of California buildings—many of them trophy properties—and development sites for more.

But Maguire proved that even at a time when many REITs are being taken private at a premium, a company can be too pricey. Bids were likely in the low \$40s per share, but Mr. Maguire is believed to have wanted at least \$50. "The purported prices were not what they should be," Mr. Maguire said in a recent conference call.

Then, to show the market it was serious about its renewed focus as a public company, Maguire announced excitedly that it would buy EOP's buildings in Orange County and downtown Los Angeles. "The Blackstone acquisition gave us an incredible unique opportunity and a rare chance to quickly and efficiently extend our asset base and grow our revenues," Mr. Maguire said at the time. The company said it would look for a joint-venture partner for the transaction.

But analysts questioned whether Maguire was paying too high a price and whether it should take on more debt when its debt ratio, at 65%, was already higher than the industry average. They also criticized the \$100 million

break-up fee Maguire must pay Blackstone if it is unable to close the deal.

Then came the news, ferreted out by Merrill Lynch analyst Ian Weissman last week, that subprime lenders make up about 10% of the tenants in the EOP Orange County buildings.

Making matters worse, Maguire is attempting to sell 17 properties in Glendale, San Diego and Orange County, including 11 of the soon-to-be-acquired EOP assets in Orange County. Mr. Weissman estimated that 15% of the space in the EOP buildings in Orange County that Maguire wants to sell is rented to subprime lenders. That raises questions as to whether Maguire will be able to get its \$2 billion price. Already some potential investors are striking the properties from their wish lists, unsure about the leasing atmosphere, especially given the eight buildings under construction in Orange County.

Included in that group is **KBS Realty Advisors**, a private-equity real-estate company in Newport Beach, Calif. "We are very sensitive about the specific tenants and occupancy in the Orange County market," said Charles Schreiber Jr., KBS chief executive.

Yet, William Halford, chief executive of **Bixby Land Co.**, a family-owned REIT, said his company is interested in some of the Orange County properties. With so much capital flowing into California commercial real estate, he predicts Maguire will find buyers for all 17 buildings. "Will they get their price?" he says. "I don't know, but you may be surprised."

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