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Morgan Stanley to Give Up 5 San Francisco Towers Bought at Peak

By Dan Levy - Dec 17, 2009

Dec. 17 (Bloomberg) -- Morgan Stanley, the securities firm that spent more than $8 billion on commercial property in 2007, plans to relinquish five San Francisco office buildings to its lender two years after purchasing them from Blackstone Group LP near the top of the market.

The bank has been negotiating an "orderly transfer" of the towers since earlier this year, Alyson Barnes, a Morgan Stanley spokeswoman, said yesterday in a telephone interview. AREA Property Partners will take over the buildings. Barnes declined to say when the transfer will occur.

"This isn't a default or foreclosure situation," Barnes said. "We are going to give them the properties to get out of the loan obligation."

The San Francisco transfer would mark the second real estate deal to unravel this year for Morgan Stanley, which bet big on the property markets as prices were rising. The firm last month agreed to surrender 17 million square feet of office buildings to Barclays Capital after acquiring them for $6.5 billion in 2007 from Crescent Real Estate Equities. U.S. commercial real estate prices have dropped 43 percent from October 2007's peak, Moody's Investors Service said last month.

"It's not surprising this deal ran into trouble," Michael Knott, senior analyst at Green Street Advisors in Newport Beach, California, said in an interview. "It was eye-opening among a group of eye-opening deals. There was almost no price too high in 2007 for office space in top gateway markets."

Lost Value

The Morgan Stanley buildings may have lost as much as 50 percent since the purchase, he estimated.

Morgan Stanley bought 10 San Francisco buildings in the city's financial district as part of a $2.5 billion purchase from Blackstone Group in May 2007. The buildings were formerly owned by billionaire investor Sam Zell's Equity Office Properties and acquired by Blackstone in its $39 billion buyout of the real estate firm earlier that year.

The buildings Morgan Stanley is giving up are One Post, 201 California St., Foundry Square I, 60 Spear St. and 188 Embarcadero, Barnes said. The bank will continue to own the five other office buildings it acquired in the deal, Barnes said.

Morgan Stanley, based in New York, was the biggest property investor among Wall Street firms at the time of the purchase. The transaction made the company one of the largest office landlords in San Francisco, with the purchase giving the bank 3.9 million square feet of office space there.

Defaults Rise

Commercial mortgage defaults more than doubled in the third quarter from a year earlier as occupancies fell, according to Real Estate Econometrics LLC. Office vacancies will reach a near-record 19 percent in the first quarter of 2011, broker CB Richard Ellis Group Inc. estimated.

Property sales financed with commercial mortgage-backed securities plunged 95 percent from a record $237 billion in 2007, according to JPMorgan Chase & Co. A lack of securitized debt is driving down values, which may fall 55 percent from their peak, Moody's said.

San Francisco prime office rents fell 37 percent in the third quarter from a year earlier, the biggest decline since 2001, as companies cut jobs, Colliers International said. The vacancy rate rose to 14 percent, the highest since 2005. Almost 1.4 million square feet of space was returned to the market in the first nine months of the year.

Morgan Stanley last month agreed to hand over Crescent to Barclays, ending the firm's obligation on a $2 billion loan after taking almost $1 billion in losses.

When Morgan Stanley acquired it, Crescent owned 54 office buildings in cities including Dallas, Houston, Denver, Miami and Las Vegas. It also owned the Canyon Ranch spa and resort, residential developments in Scottsdale, Arizona; Vail Valley, Colorado; and Lake Tahoe, California.

The San Francisco Business Times earlier reported Morgan Stanley's plans to transfer the five buildings.

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