

Vol. 38, No. 16

August 27, 2012

CONDUITS USE A/B STRUCTURE FOR HOTELS

Watch for an increase of conduits to underwrite hotel loans using an A/B capital stack structure. **Morgan Stanley, JP Morgan Chase, Wells Fargo and Ladder Capital** will be among the active lenders in this space. Don't be surprised to see additional conduits such as **Goldman Sachs, Cantor Fitzgerald, BofA and Deutsche Bank** follow suit in Q4. The senior piece will be combined with a B note from the same lender. Conduits will then securitize the senior piece and hold the B note on balance sheets. CMBS lenders will look toward an A/B structure to raise leverage to 75%.

Debt yield for A/B structured deals will often be lower, with many coming in around 9.5%. This structure will work well for over-leveraged refis coming due. Hotels constructed in 2008 or 2009 may not be operating at targeted levels yet. It will allow hotels to refi mortgages at a low interest rate without infusing new equity. Look for many of these deals to emerge for hotels and resort properties in slow-to-recover markets.

Borrowers will be attracted to this structure because they view it as one loan with one set of loan documents. Lenders prefer it given that both the A and B piece will be collateralized by the real estate with an intercreditor agreement. Due to the same lender allocating funds for the A and B piece, there will be a stronger surety it will close. Mezz will occur with CMBS but will be riskier because the mezz loan will not be secured by the real estate and will need a separate set of loan docs. If there's an issue, mezz lenders can only go after the equity not the real estate.

Conduits will further loosen underwriting overall with select loans emerging at 9% to 10% debt yield. On average, CMBS will focus on a debt yield around 11%. Banks and life companies will stick to higher debt yields of 12% to 14%. CMBS five- to 10-year pricing for hotels will range from 4.75% to 5%. Floating-rate bank loans will be at historic lows coming in at 2.75% to 3%, but will be riskier in the long run. Leverage for senior debt will top out at 70% from the conduits. Amortization will reach 30 years on 65% leveraged loans and will be 25 years for loans at 70%.

Underwriting will be based on a trailing-12. Many conduits will constrain occupancy to 75%, meaning lenders will underwrite the NOI using 75% occupancy, even if the actual occupancy is higher. This will help ensure that even if the asset's occupancy dips in the future, the loan will be secure. Conduits will allocate loans for nearly every hotel brand, including IHG, Hilton, Hyatt, Wyndham, Marriott and Starwood this year. CMBS will be less specific about brand and location, instead looking for stable or improving operations.

PREFERRED EQUITY STACKS UP FOR MULTIFAMILY

Look for preferred equity investors to push leverage as high as 95% for multifamily, while mezz tops out at 85%. Most senior lenders will favor pref. equity over mezz due to the structure. Agency lenders will not allow mezz behind their loans, leaving pref. equity to answer the call. Banks will look to pref. equity on loans for Class C and older products. Borrowers benefit from the upside due to the lower risk and lower yield position to the equity partner. It also lets the borrower keep more control over major decisions.

Keep an eye out for equity investors to offer more favorable subordinate structures in order to be competitive. Look for many preferred equity investors to want borrowers to provide 15% to 20% of the equity piece or around 5% to 10% of the total capital stack. Investors will want IRRs in the 12% to 20% range. Pref. equity will be a favorable way for equity partners to invest in multifamily and push the risk on the sponsor.

Continued on Next Page

DEAL OF THE WEEK

Property Type: Single-tenant net leased special-use property in Florence, Ky.

Loan: \$4M non-recourse refi

Lender: **GE Commercial Finance**

Leverage: Approximately 60%

Rate: Mid-5%

Proceeds of the loan will be used to refinance a maturing CMBS loan and for a cash out of around \$500K. Many lenders shied away from the deal because the property is occupied by a single, non-investment grade tenant, which would be problematic if the tenant vacated. The asset's location in a secondary market also limited the number of interested lenders. Brown obtained three quotes, of which two were non-recourse. The borrower chose GE due to additional loan proceeds offered above the original loan. GE was comfortable with the deal because of the moderate leverage on a per square foot basis and based on a "go dark" value. GE's leverage tops out at 70% so it was attracted to the lower leverage needs.

The tenant's unique industry requires a specialized buildout. GE was secure with the track record of the sponsor and its experience in the sector. There was also a feasible conversion plan in place should the tenant vacate the building. This deal was able to attain a favorable interest rate given the special use of the real estate and private credit of the single tenant. The 10-year, fixed-rate loan has a 20-year amortization. The first two years will be interest only.

CBRE Capital Markets: 101 W. Washington St., Suite 100 E., Indianapolis, IN 46204. Jason Brown, VP, (317) 269-1123. jason.brown@cbre.com

PREFERRED EQUITY STACKS UP FOR MULTIFAMILY...

Continued from Page 1

Newport Realty Capital launches a new preferred equity program in conjunction with Fannie Mae DUS financing with leverage up to 80% in soft markets. Markets in Ohio, Michigan and Florida, along with Houston, Phoenix and Las Vegas will be targeted. The lender targets deals in its \$5M to \$30M sweet spot.

Dominion Corporation starts at \$5M for preferred equity with all classes of multifamily considered. The investor will stay away from development or full rehab deals, except for projects in major MSAs with favorable demographics. Dominion looks for 12% to 16% IRRs. **Pensam Capital** will focus on deals in the \$1M to \$7M range, which will be a smaller deal size than many other investors. Properties on the East Coast, Midwest and Texas will be targeted.

Regional Capital Group allocates preferred equity as low as \$1M and provides up to 90% leverage. The investor will work with Class A, B and C properties, along with those in need of stabilization. **UC Funding** will quote deals in the \$3M to \$30M range. Leverage will reach 90%-plus. **Terra Capital** seeks out deals that need \$15M to \$100M total capitalization. Leverage will go up to 85% and IRRs will be in the low to mid-teens. **Northwestern Mutual** and **LEM Capital** will also be active. Opportunity funds will get involved in the \$30M-plus deals, while institutional providers will seek out transactions under \$20M.

Preferred equity investors will want borrowers with multiple holdings, around two to five similar properties. A favorable track record of converting or upgrading properties will also be helpful. The borrower will need a clean credit history without defaults, a net worth close to the loan amount and a reasonable amount of liquidity. Borrowers will need to show the ability to execute the business plans.

Targeted properties will have a minimum of 150 units. Pref. equity investors favor properties that operate at levels that cover all operating expenses and underlying debt requirements. Investors will consider properties without cash flow that could be repositioned. Well-managed properties with seasoned sponsors will see plenty of lender attention. Investors will look for product with an upside, based on repositioning or turning an asset around.

BANKS & LENDERS

American Equity Life Insurance Company: 6000 Westown Parkway, West Des Moines, IA 50266. John Matovina, CEO, (515) 457-1813. jmatovina@american-equity.com

BMO Harris Bank: 111 W. Monroe, Chicago, IL 60603. Dan Hampton, SVP-Head of U.S. Commercial Real Estate, (317) 269-1370. dan.hampton@harrisbank.com

Cantor Fitzgerald: 110 E. 59th St., Sixth Floor, New York, NY 10022. Michael May, Senior Managing Director, (212) 610-2319. mmay@cantor.com

Dominion Corporation: 11355 W. Olympic Blvd., Suite 210, Los Angeles, CA 90064. Keith Olson, SVP, (310) 477-3041. keitho@dominfin.com

EverBank: 501 Riverside Ave., Jacksonville, FL 32202. Robert Clements, CEO, (888) 882-3837.

Investors Bank: 101 JFK Parkway, Short Hills, NJ 07078. (973) 232-3010.

Kinecta Federal Credit Union: P.O. Box 10003, Manhattan Beach, CA 90266. (877) 896-8525.

LEM Capital L.P.: Cira Centre, 2929 Arch St., Philadelphia, PA 19104. Ira Lubert, Partner, (215) 972-2200. ira@lemcapital.com

Newport Capital Advisors: 18111 Preston Road, Suite 650, Dallas, TX 75252. Jeffrey Juster, CEO, (469) 364-6553. jjuster@newcapllc.com

Northwestern Mutual: 720 E. Wisconsin Ave. N16, Milwaukee, WI 53202. Gregory Walz, Managing Director, (414) 665-6557. gregwalz@northwesternmutual.com

Peapack-Gladstone Bank: 500 Hills Drive, Suite 300, P.O. Box 700, Bedminster, NJ 07921. Mike Giacobello, SVP of Retail Sales & Support, (908) 234-0700. consumerloans@pgbank.com

Pensam Capital: 777 Brickell Ave., Suite 1200, Miami, FL 33131. Michael Stein, Principal, (786) 587-1547. mstein@pensamcapital.com

“SMALL” DEAL OF THE WEEK

Property Type: North Central Place, an office building in Phoenix
 Loan: \$2.8M Refi
 Lender: **Mutual of Omaha Bank**
 Leverage: 60%
 Rate: Low 5%

Proceeds went toward paying off an existing bank loan with Union Bank, tenant improvements and leasing commission dollars. Churney was able to lower the interest rate on the new loan with a competitive rate from the lender. Mutual of Omaha typically does not consider office as a targeted asset class. However, the lender was attracted to the deal because it would like to partner on additional loans with the strong borrower.

Mutual of Omaha also liked the asset's strong historical performance, favorable location with high visibility and well-maintained presence. The asset outperformed the sub-market. North Central Place was 97% occupied at the time of closing in a market with 18% vacancy rates. This was a 10-year loan, with 25-year amortization.

Johnson Capital: 5080 N. 40th St., Suite 300, Phoenix, AZ 85018. Neal Churney, SVP, (602) 522-0065.
 neal.churney@johnsoncapital.com

LENDERS INCREASE SELF-STORAGE ORIGINATIONS...

Continued from Page 3

Conduits, including **Wells Fargo**, **Cantor Fitzgerald** and **Prudential** will be the most aggressive on self storage. Count on Wells to work on deals in the \$1M to \$10M range. Wells and Prudential will provide leverage up to 75% for assets with debt yield at 9% to 9.5%. Also keep an eye out for **BofA**, **Ladder Capital** and **Citi** to be active. CMBS will offer 30-year amortization on 10-year, fixed-rates loans. The conduits will start to consider product in secondary markets with less experienced sponsors.

Life companies will also be aggressive. They will focus on the most favorable properties in strong markets and will avoid mom-and-pop operators. **American Equity's** self-storage loans will start at \$2.5M. **RiverSource (Columbia Management)** will consider deals under \$5M. **John Hancock** will focus on the \$15M to \$20M deals. **Protective Life** and **Advantus Capital Management** will underwrite loans as well. **Kinecta Federal Credit Union** will provide up to 30-year amortization.

Keep an eye out for lenders to favor the strong NOI and lower cost of construction on self storage. Regional banks such as **BBVA Compass**, **EverBank**, **Fifth Third Bank** and **Charter One (Citizens Bank)** will offer five- and seven-year terms. Count on banks to originate attractive fixed-rate pricing with relationship borrowers.

Class A and B properties will see the most lenders coming to the table, while B- and C assets will have a harder time. Portfolio deals will obtain more lender attention than one-off transactions. Loans under \$4M will be difficult to finance unless part of a portfolio deal. Properties with occupancy in the 80% to 90% area will be the most sought after. Balance sheet strength and improving historical operating performances will weigh heavily on the amount of equity required. Sponsors with an experienced track record and portfolios of properties will be targeted. Borrowers will need lock-box arrangements, cash management agreements and restrictive covenants.

Lenders will favor cities that were not saturated with new development in the last cycle. Look for markets in Texas, California, Florida, Michigan, Georgia and North Carolina to experience the most self-storage lending activity going forward. Washington, D.C., Atlanta, Charlotte, N.C., Raleigh-Durham, N.C., and Tampa, Fla., should also see some activity. Deals in coastal infill markets, including San Diego, Los Angeles, the Bay Area and Orange County, Calif., will be highly sought after.

DEALMAKER DATABANK**CBRE Capital Markets**

101 E. Kennedy Blvd., Suite 1500, Tampa, FL 33602
 Donald Jennewein, Managing Director -Debt & Equity Finance
 (813) 221-7226
 donald.jennewein@cbre.com

Eastern Union Commercial

Jay Bidnick, Managing Director
 (845) 596-5146
 jbidnick@easternuc.com

George Smith Partners

10250 Constellation Blvd., Suite 2700, Los Angeles, CA 90067
 Steve Orchard, SVP
 (310) 867-2974
 sorchard@gspartners.com

HFF

9 Greenway Plaza, Suite 700, Houston, TX 77046
 Aaron Swerdlin, Senior Managing Director; Colby Mueck, Director
 (713) 852-3537; (713) 852-3575
 aswerdlin@hfflp.com; cmueck@hfflp.com

HFF

1450 Brickell Ave., Suite 2950, Miami, FL 33131
 Max Comess, Director
 (305) 448-1333
 mcomess@hfflp.com

HREC Investment Advisors

6400 S. Fiddlers Green Circle, Suite 1730,
 Greenwood Village, CO 80111
 Geoffrey Davis, President/Senior Principal
 (303) 267-0057
 gdavis@hrec.com

Johnson Capital

2656 E. Bayshore Road, Palo Alto, CA 94303
 Tom Bracken, SVP
 (650) 331-3040
 thomasbracken@johnsoncapital.com

Marcus & Millichap Capital Corp.

1201 Main St., Suite 1480, Columbia, SC 29201
 Bruce Stankavage, Associate-National Self Storage Group
 (843) 492-7422
 bruce.stankavage@marcusmillichap.com

Marcus & Millichap Capital Corp.

8310-2 N. Capital of Texas Highway, Suite 110, Austin, TX 78731
 Michael Laurencelle, Associate Director
 (512) 338-7849
 michael.laurencelle@marcusmillichap.com

Newmark Realty Capital

6060 Center Drive, Suite 800, Los Angeles, CA 90045
 Braden Turnbull, Principal
 (310) 846-5301
 bturnbull@newmarkrealtycapital.com

Quantum Capital Partners Inc.

9777 Wilshire Blvd., Suite 504, Beverly Hills, CA 90210
 Jonathan Hakakha, Managing Director
 (310) 734-8786
 jhakakha@quantumcp.com

CBRE arranges \$20M with ING for the refinance of five office properties located in Orlando, Winter Park and Altamonte Springs, Fla. The LTV was 58%. Interest came in at 4.65%. This was a 20-year loan, with 20-year amortization.

Eastern Union completes a \$7M refi loan with Peapack Gladstone Bank for a MOB in Toms River, N.J. LTV was below 50%. Interest came in at 3.95%. This was a seven-year, non-recourse loan.

George Smith Partners works on preferred equity for an apartment property in Houston. The property had a five-year, project-level IRR of 17%. This was an 80/20 equity co-invest but 50/50 in the event of capital call as a result of cost overrun.

HFF arranges a \$4.55M refinance with RiverSource for Austin Highway Self Storage in San Antonio. The low-leverage, 10-year loan had an interest rate fixed at mid-4%. The lender liked that the property was located in a favorable infill area.

HFF's hotel group sources debt and equity for hotel construction, acquisition and recapitalization. During the past year, it has closed transactions ranging from \$4M to \$400M on behalf of institutions, funds, operators and private investors.

HREC is currently working on refis of hotels facing maturity defaults where the current loan underwriting does not support a refinance at the par value of the original note. The company rebuilds the capital stack to get an acceptable payoff number for the original loan.

Bracken focuses on more structured financing for projects in Northern California and the Pacific Northwest.

Stankavage primarily handles the Mid-Atlantic region and has been involved in the self-storage asset class as an owner, operator, manager, developer, buyer and seller since 1999.

Marcus & Millichap finalizes an \$11.5M CMBS loan with Wells Fargo for the refinance of a self-storage portfolio located throughout Texas. The LTV was 71.5%. Interest came in at 5.4%. This was a 10-year loan, with 30-year amortization.

Newmark Realty works on a \$4.5M loan with a life company for a 100,000-s.f., self-storage facility in Riverside County, Calif. The LTV was 58%. This was a 10-year loan, with 30-year amortization. Interest came in at 4%.

Quantum Capital teams up with a community bank to arrange \$5.46M for the acquisition of Temecula Corporate Place Center, a multitenant office building in Southern California. The LTV was 80% and LTC was 70%. Interest was fixed for five years at sub-5%.

LENDERS EYE MOBs

Growth in the medical industry will keep lenders on their toes for medical office building (MOB) loans. Most life companies will max leverage at 65%, with a few going higher. CMBS will provide 75% leverage. Keep an eye out for banks to loosen rates and push leverage up to the 75% threshold to compete. Properties in favorable locations will see debt yield starting at 9%. Rates will be as low as 4.5% for 10-year deals. Five- or seven-year loans will see rates under 4%. Lenders will want 20% to 25% equity from the borrower. DSC will start at 1.25x. Class A deals will be able to obtain non-recourse money.

Life companies will consider deals starting at \$5M but most prefer loans above \$20M. **Northwestern Mutual** will target buildings in A locations. CMBS lenders will be aggressive and swoop up the product that does not fit in the LCs boxes, including MOBs in secondary or tertiary markets and those not near a major, creditworthy hospital. Conduits will also shoot for a \$5M loan minimum. Count on **Wells Fargo, GE, UBS, Goldman Sachs, BofA, Citi** and **Cantor Fitzgerald** to be aggressive. Private lender **Regional Capital Group** prefers \$10M and above deals, but will drop to \$3M for MOBs. The lender will provide 100% leverage for buildings owned and leased by an investment grade hospital.

Banks will be more comfortable with non-recourse money for lower leverage deals. Regional banks will go as low as \$1M. Major banks will seek out loans above \$10M. **BMO Harris Bank** targets loans in its \$5M to \$25M sweet spot and will underwrite leverage above 75% for favorable assets. BMO will consider construction loans for Class A and B product. Regional banks such as **TD Bank, People's United Bank** and **Investors Bank** will favor MOBs over traditional office. **California Bank & Trust** will provide adjustable-rate loans for medical office. **Peapack Gladstone Bank** will offer interest under 4%.

Watch lenders unable to compete for multifamily loans to turn toward MOBs. There will always be a need for medical properties and demand should increase as the Baby Boomers age. Lenders will be more likely to look past some hurdles on MOB deals.

Lenders will target stable tenants, favorable demographics and strong consistent cash flow. Location will be the most important factor. Properties close to major healthcare providers in densely populated markets will catch lenders' eyes. Count on lenders to look closely at price per square foot and the global cash flow of the borrower. Look for lenders to desire 18 months of debt service liquidity and net worth of two times the loan amount.

Construction loans will need favorable pre-leasing with credit tenants. Lenders will be confident in MOB properties with a single tenant, as long as it's creditworthy. Tenants have a tendency to stay in MOBs long-term because they invest more in the infrastructure. Look for increased activity in Las Vegas and Arizona. New Jersey, New York, Washington, D.C., and Boston will see some activity.

The Crittenden Report
Email: editorcr@crittendennews.com

Customer Service
Tel: (800) 421-3483 Fax: (619) 923-3518
E-mail: membership@crittendenresearch.com



Newsroom Fax: (619) 923-3294

The Crittenden Report on Real Estate Financing™ is published by Crittenden Research, Inc., 45 Leveroni Court, Suite 204, Novato, CA 94949. Send address changes to *The Crittenden Report on Real Estate Financing*™, P.O. Box 1150, Novato, CA 94948-1150. Contents copyright © 2012 Crittenden Research, Inc. Sample reports may be requested online at www.crittendenonline.com.

Crittenden publishes *The Apartment Report*™, *The Crittenden Report on Real Estate Financing*™, *Crittenden Real Estate Buyers*™ and *Crittenden Retail Space*™. For more information on our reports go to www.crittendenonline.com.

The Crittenden Report on Real Estate Financing™ is protected by copyright. It is illegal under federal law to make and distribute copies of this report in any form without permission, including without limitation, photocopies, faxes, e-mails, digital scans and postings on an intranet site. Violators risk criminal penalties and up to \$100,000 in damages per offense. Please contact our customer service department at (800) 421-3483 for information regarding site licenses, to request reprints of articles or to inquire about permission to make copies.

Crittenden makes every effort to ensure the accuracy of the information published in *The Crittenden Report on Real Estate Financing*™. Crittenden uses only those sources it determines are accurate and reliable, but no guaranty or warranty with regard to the information is made or implied. Information in *The Crittenden Report on Real Estate Financing*™ is subject to change. Crittenden does not accept fees nor is it a business partner with any companies or firms mentioned in this publication.