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55 YEARS

As the end of the year draws near, plenty of capital remains available for commercial mortgages - by Michael Chase

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2017 started off with plenty of uncertainty. There were concerns over the unknown impact of the new administration, potential for tax reforms, the introduction or rollback of regulations, as well as whether commercial real estate markets had peaked. These issues, among others, left many investors on the sidelines at the start of the year.

However, one thing was certain: over $210 billion in commercial real estate loans were scheduled to mature in 2017.

Life Companies Offer Attractive Options

Fresh with new allocations, life insurance companies were aggressive to start the year. So long as commercial mortgages provide lenders with a strong relative value over alternative investments, borrowers can expect aggressive pricing for the right deals. In 2017 life insurance companies have consistently priced inside their industry peers for deals that fit their targets. As predicted, spreads have had room to compress to offset some of the rise in interest rates. For ultra-conservative loan requests, spreads below 100 basis points over Treasuries are not out of the question. Life companies can even offer the ability to lock in rates for up to 12 months forward, which can be attractive in the current interest rate environment.

Competition Among CMBS Lenders Narrows

CMBS lenders used the first quarter to adjust to new risk retention rules and then volumes picked up significantly. As of the end of the third quarter CMBS originations hit $59.9 billion, well ahead of the $44.4 billion over the same period in 2016. The CMBS industry appears to have successfully worked its way through the “wall of maturities.” An interesting note is that 50% of the 2017 originations have come from the top four lenders: Goldman Sachs, JP Morgan, Deutsche Bank and Citi Group. New regulations have forced many groups to abandon their CMBS platforms. With fewer competitors, the remaining participants may start realizing greater profitability. Early projections of $65 billion in total CMBS volume for 2017 have been adjusted up to $80 billion.

Banks Have Picked Up the Pace

While 2016 was dominated by commercial banks, 2017 has been a year of playing catch up. In the face of regulatory pressures, most banks continued pulling back on construction lending. Due to potential concentration risks, some banks also had to start shying away from certain asset types. In Boston this had a particular impact on multifamily lending. Also, in some cases, pricing was adjusted too widely in reaction to rate movements by the Fed and the uncertainty that clouded early forecasts for 2017. Anecdotally, our office heard from several Boston-area banks that the first quarter was marked with little to no activity in commercial mortgages. As

investment sales volumes picked up to start the second quarter and pricing was adjusted, banks started to pick up the pace and make up for their slow start.

Agencies Dominate—and Innovate

Agency lenders—Fannie Mae, Freddie Mac and FHA—continue to dominate the multifamily space, especially for borrowers seeking full-leverage, non-recourse financing. FHA has been able to fill some of the construction lending void left behind by the banks. Properties with affordable components or an ability to make modest investments in green improvements can allow borrowers to benefit greatly from lower rates and additional proceeds. New programs are constantly being tested and rolled out, including a possibility that Freddie Mac may introduce a construction lending program in 2018.

Opportunity Remains—If You Know Where to Look

One of the significant trends in 2017 is the availability of capital for opportunistic investments. The field is crowded by mortgage REITS, debt funds, crowd-funding platforms, former CMBS lenders, life companies and banks looking for greater yields, as well as private equity providers looking to start lending platforms. In prior years, pricing generally ranged from 8% to 15% or more. In 2017, the competition for bridge financing has driven pricing down to where it can start as low as 5.5% for some transactions.

Even as Treasury rates have started to climb, borrowers can still find an abundance of available capital and take advantage of lower spreads to achieve attractive rates for either permanent loans or opportunistic bridge debt.

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