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RESURGENCE IN RETAIL LENDING

Quest for yield sparks growing competition among life companies and CMBS lenders.

By Brock Walter and James Leonard

Notwithstanding anemic economic growth and sluggish retail sales post-recession, the lending market for retail properties has seen a remarkable turnaround during the past 24 months. While the proverbial glass is not yet completely full, there are many aspects of the current lending environment that give good reason for retail developers and owners to smile.

Most significantly, liquidity has returned to the marketplace in a meaningful way. Chief investment officers of yield-starved life insurance companies are imploring their real estate production staffs to find as many deals that fit their criteria as they possibly can.

The same can be said for the loan securitization world, where strong demand for CMBS 2.0 has propelled that marketplace from complete dormancy 24 months ago to a competitive force on nearly every deal that is quoted in the market today.

Accelerants

Interest rates in both of these major lending buckets are at historical lows with 10-year money pricing on life company deals from 3.5 to 4.25 percent and 10-year money on CMBS transactions pricing between 4 and 4.5 percent.

Leverage points also have made a stunning turnaround, with life insurance companies generally comfortable at 70 percent loan to value, but willing to go up to 75 percent loan to value on particular deals.

CMBS lenders have again gained the reputation of being the higher loan-to-value alternative, typically at 75 percent for retail assets.

Most life insurance companies remain bullish on retail properties, as this asset class performed better through the recent economic downturn than other asset classes.

The grocery-anchored and credit-anchored properties with long-term leases in place remain most desired by life companies. However, unanchored or non-grocery-anchored deals with strong real estate fundamentals will continue to attract strong life insurance company interest.

Life insurance companies are finding incredible competition for deals that fit within their comfort zones, as indicated by the 3.5 percent, 10-year rates and 3.75 percent, 20-year self-amortizing interest rates currently available.

The CMBS market has continued its impressive resurgence. In 2012, total CMBS issuance was $50 billion and that figure is expected to grow to $100 billion in 2013. It is estimated that retail properties will occupy their historical 35 percent market share of this volume.

What's Changed?

Unlike the go-go days of CMBS 1.0 that ended abruptly in 2008, CMBS lenders in today's market are less likely to provide cash-out refinancing, and they are either not quoting deals with short-term rollover risk on anchor tenants or they are quoting those deals very conservatively. No longer is a modest tenant improvement and leasing commission reserve adequate compensation for significant rollover risk.

The four to five active B-piece buyers in today's securitized lending market continue to be the arbiters of which deals get done in the CMBS world. These buyers are paying far greater attention to strong real estate fundamentals than they did before the market collapse. While this means that many deals that were worthy of securitization in 2007 are not worthy today, it does (hopefully) lead to a more sustainable CMBS model moving forward.

That would be welcome news for property owners in secondary and tertiary markets and/or with properties that, for whatever reason, do not fall within the life company box.

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Walter

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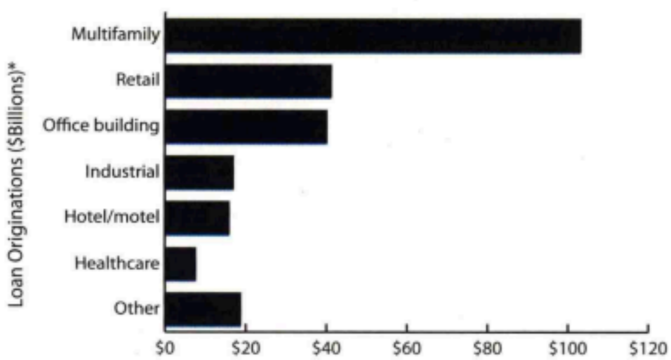
Leonard

Originations (As A Lender) By Property Type*



Retail property loans accounted for 17 percent, or $41.3 billion, of closed loan activity across the property types in 2012. The average loan size for retail properties was $7.7 million. Multifamily lending accounted for $103 bllion of closed loans, or 42 percent.

** Originations as a lender: Loans closed in own name (either for own account or for sale, and either originated directly or through an intermediary).*