MFLoan Update January 3, 2011

Year end thoughts

As someone who focuses primarily on multifamily finance, 2010 was a good year. Finding the right loan for any property during 2010 took a bit of shopping and good advice on how to present the deal to each lender, but finding a loan was definitely possible. Multifamily properties had the full support of GSE lenders throughout the economic crisis, and Freddie Mac, Fannie Mae and HUD supplied the majority of multifamily loans last year. But, they were not the only active lenders in the market. Some banks, both national and local, were also aggressive lending throughout the year and, for many properties, they were the most competitive or only lender. Life companies offered particularly competitive loans on larger, high-quality properties, especially for those borrowers looking for terms less than 10 years.

The most significant issues in getting loans approved last year related to borrower qualifications, market stability and property valuation. Freddie and Fannie have specific borrower net worth and liquidity requirements which preclude many borrowers from their programs. In many markets, especially secondary markets or those with severe economic turmoil, it was very difficult to find a lender to supply capital, even for quality properties. Borrowers needed to tell their stories to a number of lenders to find the right one who wants to make the loan despite the market issues.

Property valuation is always an issue, but with limited sale comparables last year, appraisals became much more of a wild card. Most sales last year were distressed, making it hard to find appropriate comparables to establish a value for a stabilized property. By the end of the year, many markets started to see increased sales, but the data points from distressed sales still had to be addressed.

Another commercial real estate issue in 2010 was fluctuation in interest rates. While rates have been relatively low for the whole year, the 10-year treasury chart looks like a roller coaster. Rates took a dramatic drop from mid-May until mid-October. Since then, they have risen rapidly, up over 1% in the last two months of the year. As expected, this rate movement affected deals from a DSCR perspective. More importantly, it has given many borrowers a false sense of rates. Some borrowers think the sub 5% rates of this summer are what they deserve. I wish this were the case, but it's most likely that those borrowers missed that boat. Rates today are still very good and are lower than at the beginning of 2010.

The biggest surprise of 2010 for me was how much work was needed to find the right lender for each property. For example, I recently financed a 208-unit property in Houma, Louisiana. The borrower considered a number of lenders including FHA/HUD, Freddie Mac, regional banks and Fannie Mae. While we could find a number of lenders willing to take on the deal, very few offered a loan that fit the borrower's needs. HUD could not get a loan done quickly enough, and Freddie Mac and the life companies we spoke to either took a pass on the deal or were short on loan proceeds on this B-quality property in a tertiary market. The borrower wanted a 10-year loan and the banks were not lending longer than five years. That left Fannie Mae. We spoke with six different DUS lenders about the deal and only one of those had any real interest or believed the value would be sufficient to support an 80% loan at the borrowers requested loan amount. In the end we went with the lender who believed in the deal and closed a loan with 5% more loan proceeds than the borrower initially requested. It took a good bit of shopping, packaging the loan properly and hand-holding, but in the end the borrower got a great deal. This shows how important it is to get quotes from multiple lenders. You can do this yourself or work with a trusted mortgage broker who can "clear the market" for you.

Looking to 2011, I see many of the same challenges as 2010. Freddie, Fannie and HUD will still be the most active lenders, but not the best lender for every property. Finding the right lender will still be difficult and require shopping the market and presenting the deal in the proper way. Rates will also continue to be a challenge. While I believe long term rates will still stay low from a historical perspective, they will fluctuate and most likely be higher at the end of next year. It's also likely that Libor and other short term rates will start to rise by year end. This will be a shock to those borrowers who are on floating-rate loans and have gotten used to those artificially low rates. It may be time for those borrowers to think about fixing their rate before it's too late.

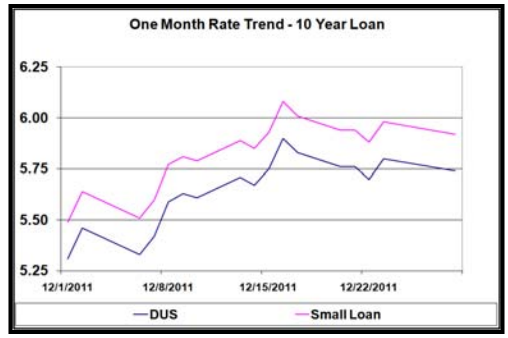
Rate Update

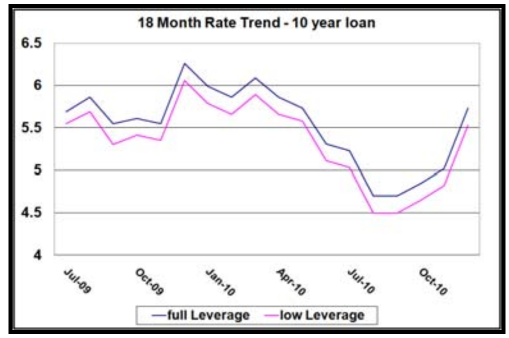
The story over the last month is that rates are up, well at least long term rates. Over the last month the 10 year treasury is up 29 Bps and the 5 year is up 30 Bps. This is on top of large increases in November. The game has changed, the almost historic rate drop last fall is over and we are getting back to low, but more normal rates. Remember we are still below rates at this time last year.

Freddie and Fannie rates have risen dramatically. While spreads have widened slightly the real change is due to the rise in treasuries. This means many deals can no longer support the same loan amounts. A 50 Bps increase in rates will lower loan proceeds by about 5% on a DSCR constrained loan. Borrowers may want to consider a 7 year loan to achieve better proceeds and rates.

At the end of the year banks and life companies moderated their rates, but don't expect this to continue into the New Year. They also must follow the realities of the treasury market. This is a bit frustrating remember why rates are rising. This is because of good economic news. If the good news continues then expect rates to continue upward throughout the New Year. My opinion is rates will stabilize in the first quarter and may even drop, but by the end of 2011 they will be higher.

Fannie Mae Rates





10 year Treasury Rates

Key Rate Indices			
	Current	Last Month	Change
6-mo. Libor	0.46%	0.46%	-
1- yr Libor	0.78%	0.79%	- 1 Bps
Prime	3.25%	3.25%	-
Fed Funds	0.25%	0.25%	-
1 year CMT	0.29%	0.27%	+ 2 Bps
5-Yr Treasury	1.93%	1.62%	+30 Bps
10-Yr Treasury	3.30%	3.01%	+29 Bps

Current Apartment Rates		
	5-Year	10-Year
Freddie Mac	4.50%-5.25%	5.40%-6.40%
Fannie Mae	4.25%-5.00%	5.50%-6.25%
FHA/HUD	4.50% - 6.00%	
Life Co's	4.25%-5.75%	5.40%-6.50%
Banks	5.25%-6.25%	6.50% - 7.50%

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