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MFLoan Update - February 1, 2011

Lender Update

As the year began most lenders finished up their pipelines and took a short breather. Because of the increase in rates at the end of last year, January began slowly. However, it picked as borrower realized that the best rates are gone and they better start their deals before rates go up again. Besides lenders dealing with borrower reaction to the higher rates they are also dealing with how the rate increase effects their underwriting. With rates up loan proceeds are being cut. Lenders are trying to move some loans to shorter maturities in order to keep the rate where the borrower wants it, but on many deals that effects loan proceeds because of underwriting floors or balloon calculations. It's a dance to get the right mix.

January is typically the conference season for institutional lenders. This year is no difference. So far no real news has come out of the meetings, just optimism about the New Year. Most of the meetings are done so focus on deals should reignite. The last big meeting is the Mortgage Bankers Association meeting next week. We expect the participants to show continued optimism, lenders announcing they are back in the market or are increasing their mortgage allocation, but not much more. We don't expect any new programs or significant policy change from the Agency lenders who are the main lenders today.

Freddie and Fannie are still dueling it out for most deals. Freddie is better loan for larger, higher quality properties in top markets. Their CME product is offering the best 10 year rate around. Fannie is winning more of those smaller deals ($5-$10 million) and has a lower 7 year rate. Fannie is also the winner on small loans (under $5 million) as Freddie does not want to play in that area.

We do not expect many major changes from the agency lenders, but there are some process changes on the horizon. Fannie Mae will be issuing new loan documents; as of this point there is limited news as to how they are different, so more to come. There are also roomers' they will be increasing their borrower scrutiny by increasing liquidity requirements. On a positive side we expect them to formally loosen pre-review requirements in some markets and the pre review requirements for larger deals.

This may be the year of the CMBS comeback, at least if you base it on the number of CMBS shops that are opening. In 2010 CMBS lenders did just over $10 billion, but they expect to do more than 5x that in 2011. In fact they are expected to exceed 2010 loan volumes by the end of February. However, very little of this is multifamily. For now they cannot compete with the agency lenders who have lower rates/higher proceeds. We are anxiously watching these lenders, but for now it's just wait and see.

HUD is still backed up and processing is still slow. You hear stories of 12+ month processing times, though some lenders with good local office relationships can still get 223 (f) deals done in 6-9 months. The other issue is the new HUD rules and some process changes are rolling through the system. Besides the LTV changes the most important items for a borrower to watch are the need for an accounting review of current income and expense numbers & the need for historical tax returns. Also, there is more scrutiny of replacement reserves, both up front and on-going, so expect these deals to capture a lot of the additional free cash flow as reserves (i.e. capital improvements). This may make HUD less compelling from an ROI basis, but it will make sure your property stays in good condition.

Rate Update

With the exception of the last two days, January has been the first month in quite a few where treasury rates stayed relatively stable. This is a relief after the 1% increase in the 10 year treasury over the last quarter of the year. As we know the recent drop in rates is due to the Egyptian political situation. For now this has created a slight flight to quality and reduction in treasury rates, however most expected outcomes for this situation will result in a calming of the markets and rates returning to non crisis levels. This is a good example of how short term items can, if you are lucky, get you an unexpected lower rate. Fortunately or unfortunately we see many items like this on the horizon.

Our biggest concern over the next few months is how the US congress will affect the bond markets. The new congress's focus on budget cutting can be positive, but you never know how the bond markets might react to different proposals and demagoguery. The biggest issue is how the raising of the debt ceiling will be treated. While this is discussed in congress and the press bond rates will fluctuate based on the political winds. This might create some opportunities for borrowers who are ready to take advantage of these swings, but it also could create sleepless nights for anyone with deals in process.

As for spreads they have dropped 5-10 Bps over the last month. Spreads are well over 200 Bps which is somewhat high from a historical perspective. This means lenders do have room to reduce their spreads as treasury rates increase to keep borrower rates relatively steady. The question is will they? The increasing competition in the multifamily market will dictate this change, but it may take a while.

Most experts seem to agree the trend will be higher for rates this year with many predicting a 1% or higher increase in the 10 year treasury by the end of the year. This could be forestalled for a while if the economy falters or the international political situation deteriorates. However we expect rates for multifamily borrower to rise this year. Borrowers who have loans that are maturing in the next 12 (maybe 24) months, should start tracking the loan market and think about refinancing now. Today's rate is very low and it is highly unlikely they will be this low when you have to refinance. Also, a higher rate may reduce your loan proceeds to a level that you find unpalatable.

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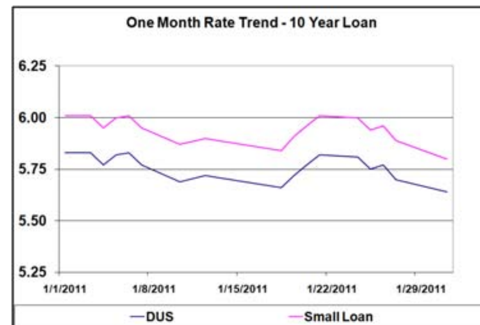
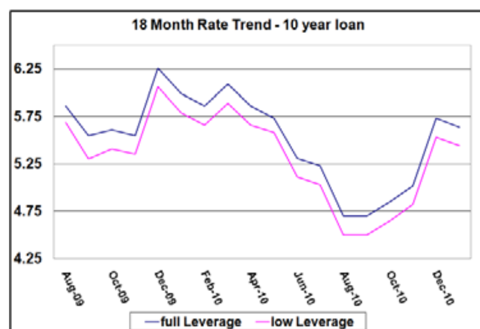
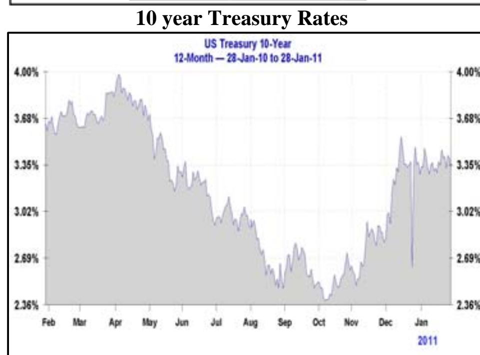




10 year Treasury Rates



Key Rate Indices			
	Current	Last Month	Change
6-mo. Libor	0.45%	0.46%	- 1 Bps
1- yr Libor	0.78%	0.78%	-
Prime	3.25%	3.25%	-
Fed Funds	0.25%	0.25%	-
1 year CMT	0.27%	0.32%	- 5 Bps
5-Yr Treasury	1.96%	2.00%	- 4 Bps
10-Yr Treasury	3.39%	3.28%	+11 Bps

Current Apartment Rates		
	5-Year	10-Year
Freddie Mac	4.25% - 4.75%	5.25%-6.25%
Fannie Mae	4.15% - 4.75%	5.25%-6.00%
FHA/HUD	4.50% - 6.00%	
Life Co's	4.25%-5.75%	5.40%-6.50%
Banks	5.00% - 6.25%	6.00% - 7.50%

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