

January 16, 2012

A Denver Based Commercial Real Estate Investment and Management Company
Contact Ken Gillis at 303-407-8715

Banks Plan to Increase CRE Allocations in 2012, but Risk Remains a Watchword

In what appears to be a sign of things to come, U.S. Bank recently closed on an \$18 million construction loan for NoBe Bay, a 98-unit waterfront condominium project. What's notable about the deal isn't that it involves a new development. It's the fact that NoBe Bay is located in Miami Beach and the current owners, a joint venture between 13th Floor Investments and Key International, purchased the partially completed property out of foreclosure in June 2011. In the past month, U.S. Bank also closed on a \$29 million five-year floating-rate loan for two shopping centers in Pensacola, Fla. One of the centers came with a vacant K-Mart store. The other, anchored by TJ Maxx and Joann Fabrics, had a low level of small shop vacancy. Similarly, in mid-December, Wells Fargo provided a \$50 million first mortgage for The District at Green Valley Ranch, a 384,107-sq.-ft. retail center just outside Las Vegas. The loan featured a fixed 4.4 percent interest rate with a five-year term and a 63 percent loan-to-value (LTV) ratio. Two years ago, banks wouldn't come within a mile of a condo development in South Florida or a retail center in Nevada. But times have changed, says Arnaud Karsenti, managing principal of 13th Floor Investments, a Florida-based real estate investment and management firm. He and his partners were able to get a number of banks interested in the NoBe Bay project, including Bank of America and a couple of regional operators, and managed to secure financing in only three months. Of course, not every condo project in Miami will get the same consideration from traditional lenders. What made NoBe Bay attractive to U.S. Bank and Bank of America was the fact that by the time the owners started shopping for a loan, they had already paid all cash for the property, Karsenti notes. Plus, they purchased NoBe Bay at a significant discount to replacement cost, downplaying the risk to the bank. "In today's environment, banks are eager to lend, but they only want to lend on certain types of projects," Karsenti notes. That's a theme that will continue to play out throughout the next 12 months. In 2011, banks finally started to unload old real estate loans, freeing up capital to invest in new product, according to Tom Melody, co-head and executive managing director with the real estate investment banking group of Jones Lang LaSalle, a Chicago-based commercial real estate services firm. Plus, with interest rates at historically low levels, there are plenty of borrowers out there looking to lock in long-term deals. As of Jan. 3, the fixed interest rate on five-year U.S. Treasury notes stood at 0.827 percent, according to a report compiled by Cohen Financial, a Chicago-based national real estate capital services firm. The fixed rate on 10-year Treasury notes was at 1.868 percent. As recently as 2010, many banks would limit risk on commercial real estate loans by doing two- and three-year deals. That trend is starting to change. Given the high level of interest in securing new loans and the favorable market conditions, banks' commercial real estate originations have been trending up. Through the third quarter of 2011, the most recent period for which data is available, the Mortgage Bankers Association's (MBA) origination volume index for commercial banks rose to 169, on a scale where 100 equals the average quarterly origination volume in 2001. The figure was still far off the peak of 552 in the fourth quarter of 2006, but it was also 433 percent above commercial banks' mortgage originations during the same period last year. The average size of commercial real estate loans closed by banks went up as well, to \$11.8 million, from \$4.9 million in the third quarter of 2010. In 2012, those numbers will likely continue rising, according to Robert Bach, senior vice president and chief economist with the commercial real estate services firm Grubb & Ellis. "I see banks being a little more active in 2012," he notes. "The recent trend among them has been to loosen standards for commercial real estate loans and that's a good thing." For example, KeyBank, a national

lender based in Cleveland, plans to increase its balance sheet lending on commercial and multifamily properties by about \$1.2 billion this year, or 15 percent compared to 2011, according to Clay Sublett, senior vice president and CMBS manager with KeyBank Real Estate Capital. KeyBank had cleaned up its balance sheet months ago and has plenty of liquidity that isn't earning sufficient returns, which is why the bank is eager to come back into the commercial real estate sector. The bankers who spent the past few years handling workouts are being encouraged to seek new clients. At the same time, however, nobody wants to go back to 2006 or 2007, so there is a lot more attention paid to managing risk, Sublett says. "We are very focused on relationships instead of transactions," he notes. "We want permanent debt. So our big focus is 'don't chase transactions, chase relationships.'" In comparative terms, commercial and multifamily mortgages held by banks have performed well through the downturn when matched against other loan types, according to Jaime Woodwell, vice president of commercial/multifamily research with the MBA, an industry trade group based in Washington, D.C. As of third quarter, the 90-plus day delinquency rate for commercial and multifamily mortgages held by banks and thrifts stood at 3.75 percent, according to the MBA, down from a peak of 4.4 percent in the third quarter of 2010. Still, from 1998 through 2007, banks and thrifts consistently averaged a delinquency rate below 1.0 percent for commercial and multifamily loans. As a result, even as banks attempt to bring in more commercial real estate business in 2012, they will continue to be careful about the borrowers and projects they are willing to work with. Banks will likely start underwriting a significant number of construction loans in 2012, but those loans will be heavily focused on multifamily projects, which have done well over the past couple years, according to Kevin Phelan, co-chairman with brokerage firm Colliers International. Preference might also be given to student and senior housing projects. Retail and office developers, on the other hand, will have to show a significant amount of pre-leasing in order to qualify for a bank loan, and they will also have to be experienced in the property type they are building. In today's environment, when KeyBank closes a construction or acquisition loan, it's always with an eye toward transitioning to permanent financing, says Sublett. For example, the bank will provide credit facilities to REITs and institutional funds to acquire new assets, but will then refinance the properties through either the CMBS market or life insurance debt. What's more, KeyBank still doesn't quite feel comfortable underwriting loans without recourse. As a rule of thumb, any transaction with an LTV of 70 percent or higher will require some form of recourse, Sublett notes. In order for there to be no recourse, the LTV would have to be at 60 percent or less. "Everybody just got through a period when the term 'risk' got re-introduced to real estate lending," says Stephenson. "In 2006, it was almost like lenders were not pricing any risk into the deal. There is still some institutional memory, so I think banks will still control their risk profile." On the other hand, banks are becoming more open-minded about entering secondary and sometimes tertiary markets, if the underlying property fundamentals meet their criteria. The competition for business in gateway cities like New York and Washington, D.C. has gotten so heated, it's been hard to secure attractive returns, says Sublett. So in the year ahead KeyBank will be focusing on a lot of secondary cities, including Dallas, Houston, Indianapolis, Columbus, Salt Lake City and Denver. **(National Real Estate Investor/Elaine Misonzhkik)**

Davis Graham & Stubbs Signs 12-Year Lease

Davis Graham & Stubbs LLP announced Thursday that it's signed a new 12-year lease at its current 17th & Wazee Street location that will allow the firm to expand its offices by nearly 30 percent. Following the expansion, DGS will be the principal tenant in the Millennium Financial Center, occupying more than 110,000 square feet on five floors. The new commitment is in response to nearly 50 percent growth in the number of DGS attorneys in the building since the firm moved to LoDo in 2000. DGS, which celebrates its 97th anniversary this year, will begin occupancy of the additional space in 2014. Until then, the firm will lease temporary satellite offices three blocks away in the Tabor Center for about 20 of its 145 attorneys and their client service teams. **(Denver Business Journal)**

...

Economic Experts: 2012 to be a Solid Year for Colorado

While 2012 won't be a boom year in Colorado, economic experts said they're seeing "a light at the end of the tunnel" and they expect slow but steady growth this year. Some signs of the state's recovery include strong retail sales, a slight increase in building permits, stabilizing home prices and a rise in business leaders' confidence in the fourth quarter of 2011, said Rich Wobbekind, executive director of the Business Research Division at the University of Colorado Boulder Leeds School of Business. "The Leeds Business Confidence Index jumped a lot from the last quarter," Wobbekind said. "Business leaders are seeing a light at the end of the tunnel, especially considering they expect growth in the construction sector." He expects Colorado's economic growth to continue to outpace the nation's this year, with steady job growth and the unemployment rate remaining below the national rate. Wobbekind spoke Tuesday at the NAIOP Commercial Real Estate Development Association's 2012 economic forecast breakfast at the Ritz-Carlton, Denver. The other speakers at the breakfast were Tom Clark, CEO of the Metro Denver Economic Development Corp.; Ken Lund, executive director of the Colorado Office for Economic Development and International Trade; and Glenn Mueller, professor at the University of Denver Franklin L. Burns School of Real Estate and Construction Management. Lund, former managing partner of Denver-based law firm Holme Roberts & Owen (now Bryan Cave HRO), outlined the state's "bottom-up economic development initiative" at the forecast. "Our goal is to create a business-friendly environment in Colorado, and make the state government more responsive," Lund said. The state wants to build its business brand, he said. "People know we're a great place to live. We need to get the message out that Colorado is a great place to do business." The state also wants to increase capital investment here, foster innovation and technology, as well as make sure it is educating and training the workforce of the future, Lund said. Colorado is focusing on primary industry "clusters" as it works to bring business here. Some of the key industry clusters include aerospace, agriculture, tourism, bioscience, energy, financial services, information services, defense, health and wellness, and manufacturing. "We want to focus on the key industries we can leverage to get the most bang for our buck [in economic development]," Lund said. Clark said the year ahead for Colorado will be "solid, maybe even exciting," based on the record number of prospects that Metro Denver EDC worked with 2011, and is continuing to work with. The EDC's prospects for businesses wanting to operate in Colorado were up 20 percent in 2011 from the year before, and actual closings on deals for businesses to locate here were up 30 percent from 2010, Clark said.

Some of the high-profile businesses that announced last year that they were locating in Colorado include Arrow Electronics, General Electric solar panel plant, Intrawest, Bridgepoint Education, Coleman and DaVita. "There has been an incredible sea-change in the conversations we're having [with prospects]," Clark said. "It's going to be a very solid year." The panelists expressed some concern about getting a nonstop flight to Asia from Denver International Airport, handling increased costs of infrastructure projects such as RTD's FasTracks, paying for the rising cost of higher education and dealing with the struggling housing market. "If you can't get a nonstop flight to the world's largest market, you're at a disadvantage," Clark said. "We've way overbuilt in the housing market," said Mueller. "I don't think we burn off the excess supply until 2016. We're certainly not as bad as states like Arizona, California or Nevada, but we have a large overhang." (**Denver Business Journal**)

...

	CURRENT	1 MONTH PRIOR	1 YEAR PRIOR
FED TARGET RATE	.25	.25	.25
3 MONTH LIBOR	.57	.55	.30
PRIME RATE	3.25	3.25	3.25
10 YEAR TREASURY	1.89	1.90	3.30
30 YEAR TREASURY	2.91	2.90	4.49