with Bob Knakal

Who's lending and for what?

Q: *What are the conditions in the current financing market and what are the differences between the market for income producing properties versus construction and development?*

A: The building sales market has been very volatile in terms of volume and value. After several consecutive quarters of increased volume, sales activity experienced a setback in the third quarter of 2010.

Since prices dropped approximately 32% in 2009 from the peak in 2007, they have been bouncing along the bottom with vacillations up and down depending on product type and sub-market. While these dynamics have been in effect, the financing market has continued to get stronger, quarter after quarter.

To understand today's financing market, we must look at how policy has impacted banking operations. The Fed's highly accommodative monetary policy has allowed for the recapitalization of the banking industry.

Today, banks borrow at rates close to zero and are able to achieve spreads of 300 to 600 basis points. Just three years ago, the lending environment was so competitive these spreads were only 30 to 50 basis points.

Presently, banks are lending at lower loan-to-value ratios and are sizing loans based upon values significantly below where they had been. Therefore, these loans are much lower on a per square foot basis than they were previously. Every dollar a bank lends today is nearly 10 times as profitable and are less risky.

For this reason, banks are aggressively looking to lend into today's marketplace. Clearly, multifamily is the property type that most lenders are interested in. Other income producing properties such as office buildings, retail and mixed-use properties also command great interest from banks.

While many banks will quote 75% loan-to-value ratios, debt service coverage requirements rarely allow financing of more than 50% to 60%. This is particularly true in the multifamily sector where yields remain at relatively low levels. Many of the buyers of our properties routinely inject 40% to 50% equity into their acquisitions.

On the construction financing front, the list of banks willing to make loans has been steadily increasing. Here, typical loan-to-value ratios are also 50% to 60%. These loans also usually contain a recourse component. We have even seen banks compete aggressively to lend on construction projects where residential condominiums were to be built.

The availability of financing exerts a positive impact on today's building sales market. If we only had greater supply of properties for sale to take advantage of it!

Robert Knakal is the chairman and founding partner of Massey Knakal Realty Services.