RELA — Chandan Survey of Commercial Real Estate Lender Sentiment

Real Estate Lenders Association & Chandan Economics

Q3 2013

Released December 2013

Based on Survey Responses Collected Following Q3 2013

Advance Release
For Internal Use Only

Lenders Expecting Further Growth in Commercial Real Estate Loan Commitments

Report Lower Debt Yields, Easing Credit Standards

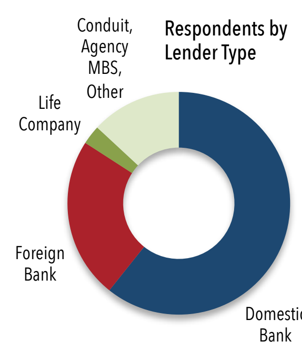
Commercial real estate lenders will be more active in the coming year, according to the Q3 2013 Survey of Commercial Real Estate Lender Sentiment. Across all property types†, 48 percent of respondents expect to grow originations over the next twelve months. While a large proportion of lenders anticipate that volume will be flat, only a small minority expects to reduce lending.

New opportunities for lending are expected to coincide with an improving borrower pool. Both for term loans and construction loans, demand from borrowers who meet prevailing underwriting criteria is expected to strengthen over the next year. Market-underwriting standards will ease in any case. Lenders expect market underwriting standards will ease and also report higher risk tolerances for loan-to-value ratios, loan sponsorship, and property location.

In focus questions about debt yields, lenders reported overwhelmingly that target debt yields for new loans have declined over the last year in spite of higher Treasury yields. A target apartment debt yield range of 8.0 percent to 8.5 percent was reported most frequently. Across commercial property types, the most commonly reported target debt yield range was 9.5 percent to 10.0 percent.

About the Survey of Commercial Real Estate Lender Sentiment

The RELA—Chandan Survey of Commercial Real Estate Lender Sentiment reports on lenders' expectations for mortgage origination volume, underwriting standards, and loan pricing in the commercial property sector. The survey is administered on a quarterly basis to the membership of the Real Estate Lenders Association (RELA), including domestic and foreign banks, life companies, agency lenders, and CMBS conduit lenders. Over the life of the survey, approximately 60 percent of respondents identify as domestic bank lenders. 23 percent of respondents identify as foreign bank lenders; 17 percent, as agency or conduit lenders or another lender type. 68 percent of respondents identify as national lenders; 32 percent, as focused on a particular market or region.



†Apartment, Office, Retail, Industrial, and Hotel

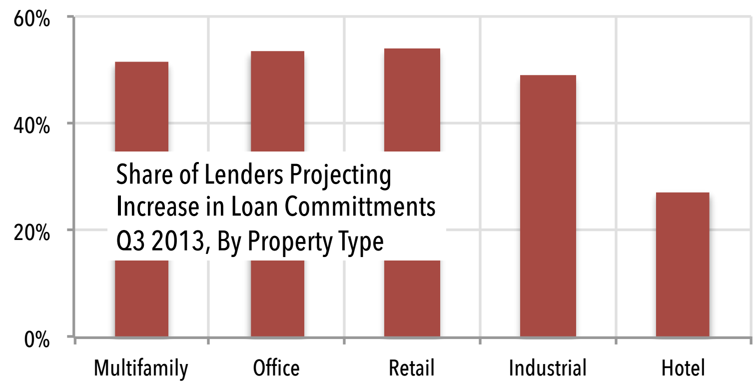
Survey responses are reported as net fractions, consistent with reporting by the Federal Reserve Board in the quarterly Senior Loan Officer Opinion Survey on Bank Lending Practices.

Lending Volume

As compared to the last twelve months, do you expect your institution to originate a larger dollar volume of new loan commitments over the next twelve months, excluding extending or restructuring loans currently in the portfolio?

Across all property types, 48 percent of lenders expect to grow the dollar volume of their lending activities over the next year. While most other lenders anticipate that activity will be flat, only a small minority expects to reduce real estate lending.

Lenders are most reserved in their outlook for the hotel sector, where they also expect that underwriting standards will remain fairly tight. Apartment lending is anticipated to grow in line with other property types, which may reflect expectations about reduced agency lending.



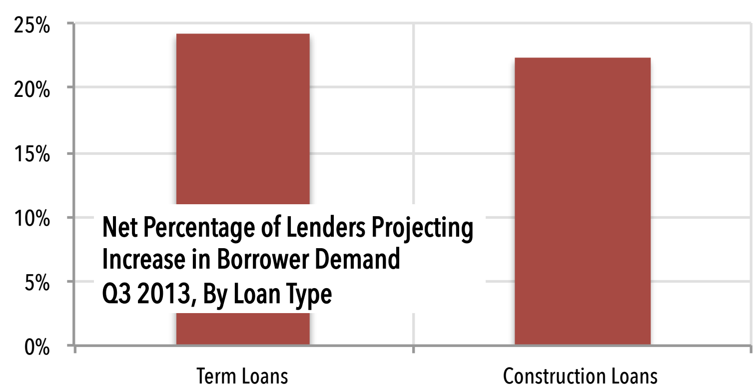
Increase in Loan Commitments Over Next Twelve Months	Yes	No / Unchanged
Apartment	51%	49%
Office	53%	47%
Retail	54%	46%
Industrial	49%	51%
Hotel	27%	73%
All Property Types	48%	52%

Demand for Financing

Do you expect borrower demand for loans that meet your institutions' credit risk profile to increase, decrease, or stay the same over the next twelve months?

Lenders expect that demand from borrowers that meet prevailing underwriting criteria will strengthen over the next year, both for term loans and construction loans.

A net share of 24 percent of lenders report demand for term loans will increase over the next twelve month. In comparison, 26 percent of lenders participating in the October 2013 Senior Loan Officer Opinion Survey on Bank Lending Practices (SLOS) reported stronger loan demand over the previous three months.



Increase in Loan Demand Over Next Twelve Months	Increase	No Change	Decrease	Net Increase
Term Loans	46%	31%	22%	24%
Construction Loans	46%	31%	23%	22%

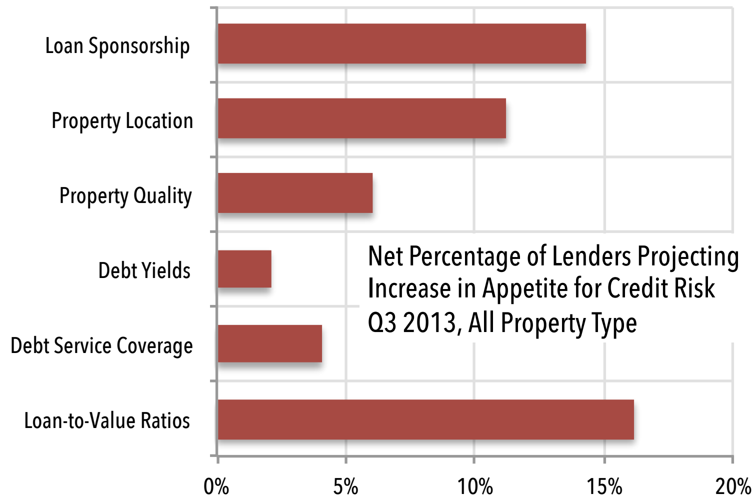
Percentages may not sum due to rounding

Lending Standards

Across all property types, do you expect your institution's credit risk appetite to increase, decrease, or stay the same in the following categories over the next twelve months?

Lenders anticipate an improving tolerance for risk over the next year, principally in terms of loan sponsorship, loan-to-value ratios, and property location. The last result is consistent with observably higher investment and lending activity in secondary and tertiary markets.

Facing the prospect of higher interest rates, lenders report they are less inclined to accept lower debt yields and debt service coverage ratios. Even at historically low going-in rates, current originations are showing sensitivity to refinancing risks at maturity from a rising rate environment.



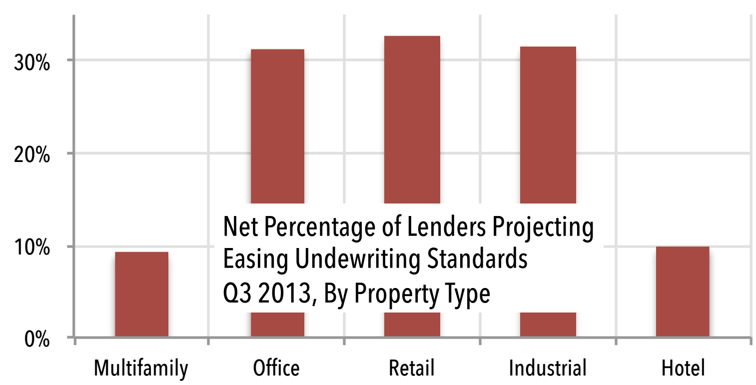
Change in Risk Appetite Over Next Twelve Months	Increase	No Change	Decrease	Net Increase
Loan-to-Value Ratios	21%	74%	5%	16%
Debt Service Coverage	17%	69%	13%	4%
Debt Yields	19%	65%	17%	2%
Property Quality	14%	78%	8%	6%
Property Location	19%	72%	8%	11%
Loan Sponsorship	20%	73%	6%	14%

Percentages may not sum due to rounding

Lending Standards

Do you expect market-underwriting standards to tighten, ease, or remain unchanged over the next twelve months?

Lenders expect that underwriting standards will ease over the next year for office, retail, and industrial properties. The net shares of respondents expecting easier multifamily and hotel terms are substantially lower, however. In the case of apartments, this reflects the relative maturity of the sector's recovery. Lending standards have already eased significantly from their crisis levels, supported by strong fundamentals and agency debt. In the hotel sector, lenders are more reserved in part because of the perceived additional risk of hotel lending.



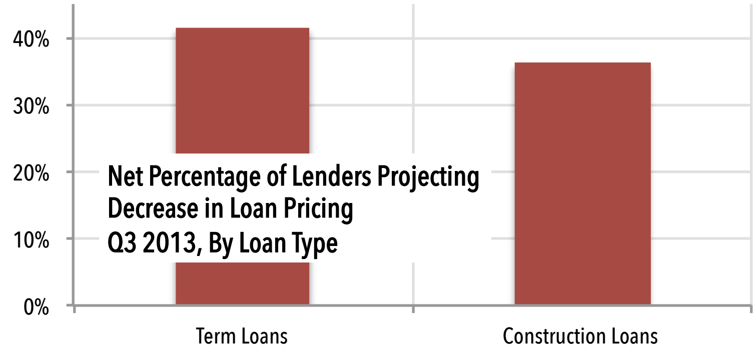
Change in Market Underwriting Over Next Twelve Months	Ease	No Change	Tighten	Net Easing
Apartment	40%	30%	31%	9%
Office	43%	44%	12%	31%
Retail	44%	45%	11%	33%
Industrial	40%	51%	9%	31%
Hotel	37%	37%	27%	10%

Percentages may not sum due to rounding

Loan Pricing

Do you expect market pricing for loans that meet your institution's credit risk profile to increase, decrease, or stay the same over the next twelve months?

Lenders expect pricing on term and construction loans to decline over the next twelve months.



Decrease in Loan Pricing Over Next Twelve Months	Increase	No Change	Decrease	Net Decrease
Term Loans	18%	22%	60%	41%
Construction Loans	15%	34%	51%	36%

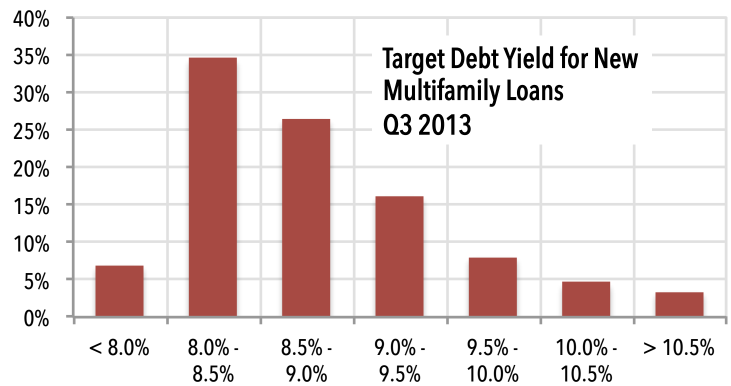
Percentages may not sum due to rounding

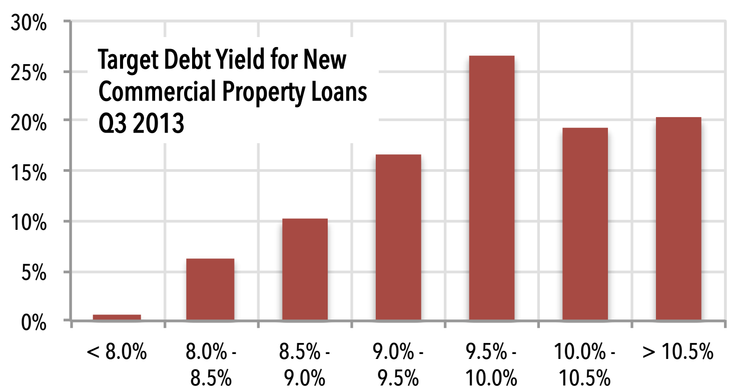
Focus Questions on Debt Yields

The Q3 2013 survey included two focus questions regarding lenders' target debt yields.

What initial debt yield (net operating income ÷ origination balance) does your institution currently target?

More than one-third of lenders reported a current target debt yield between 8.0 percent and 8.5 percent for new multifamily originations. More than half of lenders fell in the 100 basis point range from 8.0 percent to 9.0 percent. Few lenders reported targeting yields below 8.0 percent. However, a significant share reported targets above 9.0 percent, which may reflect lending on value-add and other non-core assets. The most common target debt yield range for commercial properties was 9.5 percent to 10.0 percent, 150 basis points higher than for apartments.





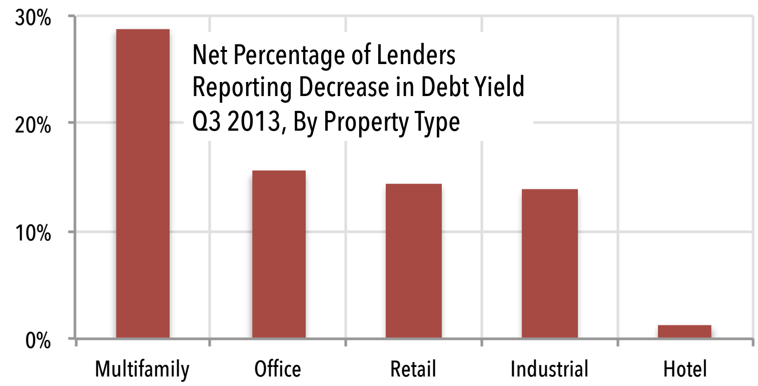
Target Debt Yield	< 8.0%	8.0% – 8.5%	8.5% – 9.0%	9.0% - 9.5%	9.5%–10.0%	10.0%–10.5%	10.5% +
Apartment	7%	**34%**	26%	16%	8%	5%	3%
Office	2%	7%	14%	18%	**32%**	16%	11%
Retail	0%	8%	10%	20%	**31%**	22%	9%
Industrial	0%	7%	9%	18%	**28%**	23%	15%
Hotel	0%	3%	6%	10%	12%	16%	**52%**

Mode for each property type shown in bold. Percentages may not sum due to rounding

Focus Questions on Debt Yields

Has your institution's debt yield target increased, decreased, or remained the same over the last twelve months?

In spite of higher risk-free yields on long-term Treasuries, lenders reported that debt yields had declined over the last year. Debt yields declined most consistently in the apartment sector, where the more mature recovery has already seen underwriting ease substantially and where debt yield spreads are narrower. For core commercial properties, where underwriting adjustments have lagged, fewer lenders reported that debt yields had fallen year-over-year. In the case of hotels, the net change in debt yields was essentially flat.



Change in Target Debt Yield During Prior Twelve Months	Increase	No Change	Decrease	Net Decrease
Apartment	13%	44%	42%	29%
Office	12%	60%	28%	16%
Retail	6%	74%	20%	14%
Industrial	6%	73%	20%	14%
Hotel	11%	77%	12%	1%

Percentages may not sum due to rounding

The RELA—Chandan Survey of Commercial Real Estate Lender Sentiment is published following the end of each calendar quarter and reflects survey responses collected in the preceding weeks from the RELA membership.

Inquiries regarding the RELA—Chandan survey and survey results can be directed to the Berman Group:

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The Real Estate Lenders Association

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The Real Estate Lenders Association, Inc. is a not-for-profit corporation formed in 1991 to provide a forum for real estate lenders and equity investors to advance their knowledge and expertise in their industry. RELA's focus is on education, networking, and opportunity. Membership in RELA is exclusive to institutions with commercial real estate debt and equity under their direct control.

Chandan Economics

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Chandan Economics is a leader in commercial real estate debt market research. Leveraging its database of commercial mortgages originated by balance sheet, agency, and conduit lenders, Chandan reports on national and market lending trends and provides credit risk analytics for banks, life companies, investors in CMBS and agency securities, regulators, and policymakers.