

LISTENING TO LENDERS

Their capital forecast for 2019

BY BRANDI SMITH

The switch to 2019 is an opportunity to celebrate the year that was and look ahead to the year to come. As it pertains to commercial real estate, a big part of the future, as well as the past, is lending.

To determine what the new year has in store, REDNews reached out to Greg Young, senior vice president of Grandbridge Real Estate Capital, which offers comprehensive capital solutions for commercial and multifamily real estate assets, and William Dampier, vice president of commercial lending at City Bank, which provides a number of commercial loans aimed at helping the Houston community grow and prosper.

Interest rates, already bumped up by the Fed in late December, will be of particular interest this year.

"We're currently in the second longest expansion of the economy in U.S. history. Job creation remains strong," Young says. "It wouldn't surprise me at all if they didn't raise them again in 2019."

Dampier, on the other hand, has penciled in at least two interest rate bumps into his budget for this year.

"I think the market might be a little bare for next year," he explains. "I don't know if the Fed is just raising the rates a little too quickly, but in the event that the market does see a recession, the Fed does need some ammunition."

Even with the recent increase, rates have been near historic lows, so it's logical that the Fed would want some breathing room in case the economy slides toward a recession. Those hikes, however, can have a significant impact on the commercial real estate industry.

"It makes it harder for some deals to cash flow and to make sense," Dampier says. "Sellers are collecting rent at all-time highs, so there's not a lot of motivation these days to sell if they don't have to. We're starting to see where, I think, it becomes a standoff and you have to see who blinks first: the buyer or the seller."

The bottom line for Young is simple: the raising-rate environment means the all-in cost of capital is going to go up.

"I suspect the ten year treasury going forward will continue to go up. It wouldn't surprise me at all if we saw a ten-year treasury around 3.3 to 3.4 this time next year," he says. "The real question is: what happens with credit spreads?"

Now is the time for planning and, possibly, limiting growth, according to Dampier.

"If you were anticipating eight percent growth in 2018, maybe you're only looking at five percent growth for 2019," he explains. "Over the past 12 to 18 months, we have definitely seen transaction accounts declined. Cap rates are suppressed."

That, Dampier argues, can make it more difficult for investors to identify a deal that makes sense to them. Lenders are taking a hard look at the numbers from a growth trajectory to evaluate how rate hikes will impact deals.

"The investors are really having to dig a little deeper, look a little longer. There still are deals out there, they are just harder to find. They're having to look a little bit broader and expand their market," he says. "We have recently started to do a few more deals to the east, toward the Beaumont market."

Dampier says even a few years ago, there were plenty of deals floating around Houston, so it wasn't necessary for investors to stretch their boundary. Now, they're stepping outside the city to evaluate potential opportunities in outside markets.

For Young, it's not necessarily about when to finance, but where to find financing. Changes to lending practices have increased interest in alternative capital services, such as debt funds. Young continues that Fannie Mae and Freddie Mac remain en vogue as lenders.



GREG YOUNG



WILLIAM DAMPIER

"They're going to continue to be in high demand," he says.

CMBS obviously remains an option as well.

"Life insurance companies, Grandbridge Real Estate Capital's bread and butter, continue to add commercial mortgage loans to their portfolio. The thing we love about them is that those guys are always in business. They're never out of the market," he says.

While CMBS is always one choice, Young argues there are several capital solutions available in the marketplace.

"One of the reasons why people hire us is because we're giving them access to all of these different sources of capital. There are certain shops out there that tend to gravitate toward a single capital alternative," he says. "At Grandbridge, we enjoy unparalleled access to capital. The real value we offer our client base is placing them in the capital solution that best fits their needs."

Overall in 2019, 'a little bearish' is how Dampier describes City Bank's approach. He says he'll keep an eye on the stock market as the interest rate hikes take effect.

"It's definitely making you really evaluate these deals because you're seeing some lenders out there that are willing to stretch to possibly hit their budget and to make their investors happy," he says. "We're not putting ourselves in harm's way to try to make a deal work."

Young predicts the overall supply of capital, which is higher than he's seen it in his 16 years in the industry, will be the same in 2019.

"I've got more money than I have deals," he says.

Since the year is just getting started, we will have to wait and see how the lending environment responds to predicted changes.

