

Silver Lining

Troubled Market Positions Loan Servicers for Opportunity

By Eugene Gilligan

Borrowers may be having trouble refinancing 10-year loans that are maturing, and loan originations may have dropped sharply, but the troubled commercial real estate market opens the door for some loan servicers to step to the front of the line.

"What is happening in loan servicing is obviously a reflection of the credit market crunch," said Midland Loan Services Inc. executive vice president Stacey Berger. "CMBS borrowers are having greater difficulty in refinancing maturing loans, but most seem to accomplish payoffs. While extensions and defaults are increasing, the percentages are still small and manageable."

Shorter-term loans are also exhibiting stress. "Short-term floating-rate loans have become more problematic than fixed-rate loans," he said, explaining that the maturing fixed-rate loans were typically originated in 1998 and 1999 and were more conservatively underwritten. Berger added that they have been amortized down and the properties have appreciated.

Grandbridge Real Estate Capital L.L.C. senior

vice president & servicing co-manager Joseph Lovell reported a slowdown in payoffs for his firm's \$22.5 billion in loans. "We attribute (it) partially to borrowers experiencing greater difficulty making an exit from their existing loans," he said.

All this grief—high leverage levels in loans, plummeting property values and constricted credit markets—in some cases translates into bad things happening to good companies. And there lies the opportunity for stable loan servicing companies to develop solutions to serve worthy borrowers.

Hudson Realty Capital L.L.C. director Heather Mutterperl, who services a portfolio of loans originated by her company, considers extensions for worthy borrowers that are having trouble selling or refinancing their properties. "Hudson reviews each investment individually, and for properties that we believe can execute the business plan, we set a reasonable time frame and extend the loan accordingly," she said.

Grandbridge is also making the exception the rule when possible. "We have seen a slight uptick in borrower requests for temporary relief, such as going interest only for a short period or extension requests," said senior vice president & head of asset management Russell Richardson.

Special servicing offerings are also needed now more than ever. "There is going to be a huge amount of distress and a real need for special servicing," said Andrew Miller, principal of Miller Frishman Group, an advisory, property management and brokerage firm. Falling property values and ebbing property-level income have caused loans to go out of balance, he said. "Loans that

have debt-service-coverage ratios that used to be 1.2 fall to zero."

So to serve that needy market, Miller Frishman and Johnson Capital in October formed Johnson

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—Heather Mutterperl, Hudson Realty Capital L.L.C.

Capital Special Servicing to advise lenders of all types of loans. It will also offer property management and leasing services.

In addition to all the trouble the economy is having with existing loans, the decline in new originations may force some loan servicers to exit the business. And that would create opportunities for larger servicing companies to step in. Smaller banks may want to sell their servicing operations, for example, Berger noted. Loan servicing consolidation may follow the recent mergers among major banks, as well. In the cases of JPMorgan Chase & Co.'s purchase of Washington Mutual and Wells Fargo & Co.'s acquisition of Wachovia, for example, each entity operates a loan servicing line.

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It's All Uphill

All commercial property types experienced increased delinquencies in September. Lodging delinquencies moved higher but remain at low levels. But could the sector's current state be the calm before the storm? Retail delinquencies continued their climb to \$803.8 million after stalling in August. As consumers rattled by the credit crisis and loss of confidence trim their spending, retailers will have an increasingly difficult time luring shoppers in. As they close stores at a rapid pace, leading to dark spaces and decreased foot traffic, retail centers are likely to be under operating pressure, which will ultimately translate into higher retail delinquencies.

Source: Standard & Poor's
www.standardandpoors.com • Larry Kay • 212-438-2504

(delinquencies in millions of dollars)

