CMBS, SBA help thaw capital market

ATLANTA—The capital markets are loosening, banks are jumping back into the fray, and SBA financing is set to push progress in secondary markets. Yes, the realm of hotel financing is clearly headed in the right direction, but after hitting rock bottom, it really had nowhere else to go, according to a panel held during the Hunter Hotel Investment Conference.

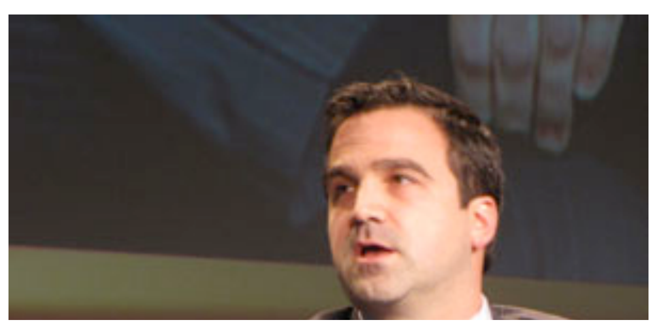
"Today we've clearly hit the bottom. It's been positive (revenue per available room) since March 2010. That is bringing people back to the market where they can see it in the data. There are more people that can finance deals," said Jim Merkel, president of RockBridge Capital in Columbus, Ohio.

Two years ago, only one or two lenders were doing deals, said Jim Fitzgerald, managing director of hotel investments for Chicago-based Principal Global Investors. Six months ago, that number jumped to between six and eight. Now, there are approximately a dozen commercial mortgage-backed securities players in addition to portfolio lenders who actively are contributing financing in the market.

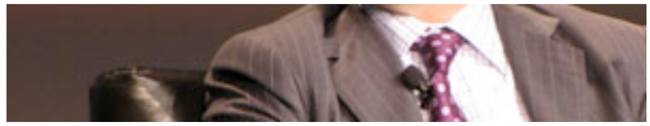
The CMBS players' presence is particularly noteworthy. Only 18 months ago, CMBS was declared dead in the water. Now the lending vehicle is beginning to coast.

"I think it's moving now," said W. Michael Murphy, who serves as head of lodging and leisure capital for Atlanta-based First Fidelity Companies.

"CMBS market is a permanent vehicle," Merkel added. "With the banking environment getting healthy and stronger, I think that will have a greater impact on creating a flow through this period of time."



Those securitizations have been "very well-received on Wall Street thus far," Fitzgerald said. Qualifying borrowers should expect 65% loan-to-value with pretty firm debt yields to the tune of 12-14% he said.



RevPAR increases are helping to thaw the capital markets, said Jim Merkel, president of RockBridge Capital.

What borrowers need to know

Expect a lot of opportunities in the coming year as lenders begin to clear their balance sheets aggressively, Merkel said.

Extend-and-pretend was in their best interest at the time, but that's starting to wane, he added. Banks are fatigued and are ready to move on.

"They're ready to move (troubled assets), and they feel more confident … that there's a market for their position," Merkel said, adding he's seen a lot more distressed transactions in recent months.

So what does every borrower need to know in order to take advantage?

First, all lenders are not created equal. "A special servicer isn't really a lender versus a balance sheet lender," Fitzgerald said. Working with special servicers can prove especially difficult, as they're restricted by financial guidelines and have many parties to appease.

Second, you have to have a good track record.

"Sponsorship is awfully important," Merkel said. "In any environment, you have to have a track record."

But strong sponsorship isn't a cure-all—a fact that brought the panel to its third piece of advice for borrowers: "You've really got to get educated and find out what condition your banks are in," said Randy Griffin, president of CSRA Business Lending in Augusta, Georgia.

The United States went into the downturn with approximately 8,500 FDIC-insured financial institutions, he added. There will be between 6,000 and 6,500 by the time the country is in the clear.

As such, a long-standing relationship and good track record with a regional bank could be moot if that bank's restricted by tighter regulations or is fighting against its own insolvency.

Finally and perhaps most obvious: Bring cash to the table.

"There are a lot more arrows in the quiver when you come to the table with capital," Fitzgerald said. "If you're not, then it's very difficult as a fiduciary to justify just rolling on a transaction."

SBA gets rolling in secondary markets

Major urban markets might be swinging to first-quarter upturns, but there are secondary and tertiary locations that have been much slower to rebound. Fortunately, the jobs bill that was signed into law September 2010 introduced three changes to the Small Business Administration's 504 loan program that will positively impact small- and mid-market financing, according to Griffin.

1. *Increase in maximum loan amount*

The maximum loan amount has increased to US$5 million from US$2 million. The loan can be used on second hotel mortgages for projects as large as US$14 million.

2. 504 can be used for refinancing

While refinances under the 504 loan were previously ineligible, the new bill allows refinances under certain conditions for a period of two years starting on 28 February and ending in late September 2012. For other stipulations, consult a SBA lending representative.

Stricter regulations can limit regional banks' ability to lend, said Randy Griffin, president of CSRA Business Lending.

3. Larger hotel owners are now eligible

The SBA increased the maximum size a company can be to qualify for SBA loan programs. The new rule requires the combined business net worth of the applicant to be no greater than US$15 million and that the applicant business have an average profit the past two years of no more than US$5 million to be eligible.

Construction financing possible, but not plausible

Construction financing was a huge part of Murphy's business at the First Fidelity Companies. "That business has gone away for the moment," he said.

Still, construction financing is available in very certain circumstances, the panelists agreed.

"I think we'll see a resurgence of it, first with very specialized requirements," Murphy said.

"There are some markets where you can build below the market value …" Merkel added. "Those with the better credit and the better track record are going to get those deals done. There are those opportunities."