FINANCIAL LEVERAGE / FINANCING ALTERNATIVES

Financial Leverage: Allows an **Investor** to use less **Equity** to acquire an **Investment**, potentially achieve a higher **Leveraged Return** on **Equity**, and benefit from the **Tax Deductibility** of **Mortgage Interest**. **Investors** who desire a higher **Leveraged Return** on **Equity** might borrow at a higher **LTV** ratio, but as the **LTV** increases, **Risk** increases.

Positive and Negative Leverage: **Positive Leverage** is when the **Return** on **Equity** is higher with **Debt** than without, and **Negative Leverage** is when the **Return** on **Equity** is lower with **Debt** than without. With **Positive Leverage**, the higher the **LTV** ratio, the higher will be the **Leveraged Return** on **Equity.** With **Negative Leverage**, the higher the **LTV** ratio, the lower will be the **Leveraged Return** on **Equity**.

Loan Underwriting: The **Loan to Value Ratio (LTV)** and **Debt Service Coverage Ratio** (**DSCR**) are two of the key elements of a **Loan Underwriting**. Although the maximum **LTV** ratio and minimum **DSCR** levels vary with **Mortgage Market** conditions, **Lenders** are always more secure with a lower **LTV** ratio and a higher **DSCR**.

Prepayment Penalties, Yield Maintenance, Loan Lockouts: **Mortgage Loan** terms that make it costly or impossible for a **Borrower** to **Payoff** or **Refinance** a **Loan** before the contract **Maturity Date.**

Interest-Only Loan: **Borrower** pays only **Interest** on the **Loan**, with no **Principal Amortization**, and a **Balloon Payment** due at **Maturity**. Also called a "**Bullet Loan"**.

Negative Amortizing Loan: When the **Payment Rate** on a **Loan** is less than the **Accrual Rate** (i.e. **Interest** amount then due), there will be **Negative Amortization** and the **Loan Balance** will increase. Might be used when **Interest Rates** are very high.

Participating Loan: The **Lender** receives additional **Interest**, based on a formula, typically related to **Gross Income**, **NOI**, or **Cash Flow**, that is called a **Participation** or "**Equity Kicker**" but the **Lender** does not have any **Ownership Interest** in the **Property**.

Convertible Mortgage: When the **Lender** has the right to **Convert** part or all of the **Loan Principal** to an **Ownership Interest** in the **Property** at a specified time.

Mezzanine Loan: A **Loan** that is often **Secured** by the **Owner's Equity** in a **Property**, rather than by a **Mortgage** on the **Property** itself. Usually requires an **Inter-Creditor Agreement** between the **Mezzanine Lender** and the **First Mortgage Lender**.

Preferred Equity: An **Investment** in the **Ownership Interest** of a **Property,** that is not a **Mortgage**, with a **Preferred Return** that takes **Priority** over other **Equity Investors**.

Sale-Leaseback: An alternate means of **Monetizing** a **Property** where the **Seller** retains **Use** of the **Property** for the duration of the **Lease Term**. With a **Repurchase Option** in the **Lease**, the **Seller** may reacquire **Ownership** of the **Property** in the future.