Loan Vehicles:

Commercial real estate is an attractive investment option for many investors, as it offers the potential for significant returns. However, purchasing commercial real estate often requires significant capital, which may not be readily available. This is where commercial real estate loans come in. Here we will discuss the different types of loans for commercial real estate and their benefits.

Conventional Loans:

Conventional loans are the most common type of commercial real estate loans. These loans are usually provided by banks or other financial institutions and are secured by the property being purchased. Conventional loans generally have fixed or adjustable interest rates, and the loan term can range from 5 to 30 years. The main benefits of conventional loans are that they have low interest rates and long repayment periods, making them an attractive option for investors.

SBA 7(a) Loans:

Small Business Administration (SBA) 7(a) loans are government-backed loans that are designed to help small businesses purchase or refinance commercial real estate. These loans are provided by approved lenders, and the SBA guarantees a portion of the loan, which reduces the lender's risk. SBA 7(a) loans generally have longer repayment terms, lower down payment requirements, and lower interest rates than conventional loans, making them an attractive option for small business owners.

CMBS Loans:

Commercial Mortgage-Backed Securities (CMBS) loans are a type of loan that is secured by a pool of commercial real estate loans. These loans are packaged together and sold to investors as bonds. CMBS loans are attractive to borrowers because they offer flexible terms, including interest-only periods and balloon payments, and they typically have lower interest rates than conventional loans. However, they can be complex and are usually only available to borrowers with strong credit profiles.

Bridge Loans:

Bridge loans are short-term loans that are used to bridge the gap between the purchase of a new property and the sale of an existing property. These loans are usually provided by private lenders or hard money lenders and typically have higher interest rates and shorter repayment terms than other types of commercial real estate loans. Bridge loans are useful for investors who need to act quickly to secure a property or who need to make repairs or renovations before securing a permanent loan.

Agency Debt:

This type of financing is offered by government-sponsored enterprises such as Fannie Mae and Freddie Mac. It often has lower interest rates and longer repayment terms than conventional debt, but requires stricter underwriting standards.

Mezzanine Debt:

This is a form of financing that combines both debt and equity. It's typically used to fill the gap between the amount of equity invested and the total amount of debt required for a property. This can create a Loan to Cost (LTC) of 85% allowing the investor to bring less money to the table.

Recourse loans are those where the borrower and/or guarantor is personally liable for repaying the loan. In the event that the borrower defaults, the lender can go after the borrower's personal assets to recover the remaining loan balance. This means that the personal guarantor is responsible for repaying the loan in full, even if the collateral property is sold for less than the outstanding loan balance. This is mainly used by banks, private lenders, debt funds and hard money lenders.

On the other hand, non-recourse loans limit the lender's ability to go after the borrower or guarantor's personal assets in the event of a default. Instead, the lender can only recover the remaining balance from the collateral property itself. Non-recourse loans are typically only available to borrowers with strong financials, solid credit history, and high-quality collateral. This is one of the biggest advantages to using agency, CMBS, life company and even banks!

When it comes to guarantor requirements, recourse loans generally require a personal guarantor who is willing to take on the financial responsibility for repaying the loan in the event of a default. In contrast, non-recourse loans often do not require a personal guarantor, as the lender relies solely on the collateral property to recover the loan balance in the event of a default.

**Investor Structures**

General Partnerships:

In a general partnership, all partners share equal responsibility for the business's management, profits, and losses. Each partner has unlimited personal liability for the partnership's debts and obligations. This means that each partner's personal assets could be used to pay the partnership's debts. General partnerships are easy to form and do not require a formal agreement. They are also relatively easy to dissolve.

Benefits of General Partnerships:

1. Shared responsibility: Each partner in a general partnership has a say in the management of the business, and each partner's contribution is valued equally.
2. Simple to set up: General partnerships do not require a formal agreement, making them a quick and easy option for two or more people to start a business together.
3. No formal reporting requirements: General partnerships are not required to file formal reports with the government or maintain a certain level of record-keeping, making them less burdensome than other business structures.

Limited Partnerships:

Limited partnerships have at least one general partner and one or more limited partners. The general partner has full control over the partnership's management, while the limited partners have limited control and are not liable for the partnership's debts and obligations beyond their investment. Limited partners typically have little to no involvement in the day-to-day operations of the business.

Benefits of Limited Partnerships:

1. Limited liability: Limited partners are not personally liable for the partnership's debts and obligations beyond their investment in the partnership.
2. Flexibility: Limited partnerships allow for flexible investment opportunities, allowing investors to participate in the business's profits without having to be involved in the day-to-day operations.
3. Tax benefits: Limited partnerships are pass-through entities, meaning that the partnership's income is only taxed once, at the partner level, avoiding the double taxation that corporations may face.

**Return Metrics**

As a real estate investor, it's important to understand the factors that can impact the calculation of financial metrics such as Internal Rate of Return (IRR), Cash-on-Cash (CoC) Return, and Equity Multiple (EM). Here are some key factors to consider:

Cash-On-Cash Return:

Cash-on-cash return measures the annual return on an investor's initial investment. This metric compares the annual cash flow generated by the property to the amount of cash invested. For example, if an investor invests $500,000 in a property and receives $50,000 in annual cash flow, the cash-on-cash return would be 10%. Cash-on-cash return is a simple metric that is easy to understand and calculate, making it a popular metric for evaluating real estate investments.

Internal Rate of Return (IRR):

Internal rate of return (IRR) measures the total return of an investment over its entire holding period. IRR takes into account the time value of money, meaning that it considers the timing of cash flows and the discount rate. IRR is calculated using a complex formula, and it can be challenging to understand for individuals who are not well-versed in finance. IRR is a useful metric for comparing the returns of different investments with varying holding periods and cash flow timing.

Equity Multiple:

The equity multiple measures the total return on an investment relative to the amount of equity invested. This metric takes into account both cash flow and equity appreciation. For example, if an investor invests $500,000 in a property and receives $50,000 in annual cash flow and sells the property for $1,000,000 after five years, the equity multiple would be 2.0x. Equity multiple is a useful metric for evaluating the total return of an investment, taking into account both cash flow and appreciation.

The following parameters can affect the returns.

Property type and location: Different types of properties and locations can have varying risk and return profiles, which can impact the calculation of these metrics. Capital expenditures: The amount and timing of capital expenditures required for the property can affect the cash flow projections and ultimately impact the calculation of these metrics.

Financing structure: The financing structure of the investment can impact the cash flow projections and ultimately impact the calculation of these metrics. This is what is currently really affecting the market. with high interest rates and low cap rates making deals pencil is becoming harder and harder to do.

Market conditions: Economic and market conditions can affect the cash flow projections and ultimately impact the calculation of these metrics.

Holding period: The length of time that the investment is held can impact the calculation of these metrics, as it affects the timing and amount of cash flows and the potential for capital appreciation or depreciation.

Operating expenses: The amount and timing of operating expenses can impact the cash flow projections and ultimately impact the calculation of these metrics.

Exit strategy: The planned exit strategy for the investment can impact the calculation of these metrics, as it affects the timing and amount of cash flows and the potential for capital gains or losses.

By considering these factors, real estate investors can make more informed decisions and accurately evaluate the profitability and potential risks of their investments.

**Benefits of Investing in CRE**

Investing in real estate has been a tried and tested way of building wealth for centuries. With the potential for substantial returns and the ability to generate passive income, it is not surprising that many people see real estate as the best way to grow their wealth.

Here are some of the reasons why investing in real estate is the best way to grow wealth:

Appreciation

Real estate has a track record of appreciating in value over time. While the market can be volatile in the short term, real estate tends to appreciate steadily over the long term. This means that if you invest in a property today, you could potentially sell it for a higher price in the future, generating a significant return on your investment.

Cash Flow

Real estate investments can generate passive income through rental income. This is a great way to generate a consistent cash flow, which can be reinvested to further grow your portfolio. With the right investment strategy and property management, rental income can be a reliable source of income for years to come.

Tax Benefits

Real estate investments offer many tax benefits, including deductions for mortgage interest, property taxes, and depreciation. These deductions can reduce your tax liability, increasing your net income and helping you grow your wealth.

Diversification

Investing in real estate can help diversify your investment portfolio. Real estate investments do not necessarily move in tandem with the stock market, providing a hedge against market volatility. This means that real estate investments can help reduce the risk of your overall investment portfolio.

Control

Real estate investments offer more control than other forms of investment. As the owner of the property, you can make decisions about how to manage and maintain the property, which can directly impact the value of your investment. This level of control can provide investors with a greater sense of security and peace of mind.

In conclusion, investing in real estate is a proven way to build wealth. With the potential for appreciation, cash flow, tax benefits, diversification, and control, it is not surprising that many people see real estate as the best way to grow their wealth. However, like any investment, it is important to do your research and seek professional advice to make informed decisions about your investment strategy.