3 CRE Q&A: Newmark's Ritchie on Investment Market

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Mark Ritchie, a principal with commercial mortgage banking firm Newmark, shared his insights into CRE lending in the coming year. The San Francisco-based firm commemorated its 25th year of operations, having placed more than $30 billion of commercial debt since its founding. Transactional volume exceeded $2 billion each of the past five years, including completion of $2.4 billion last year. The company expects 2017 to be consistent with that trend, as fence-sitters move to shore up financing needs. Refinancing likely will take center stage for investors with long-term hold assets, given the expectation that current rates will rise throughout the year.

Q: What are the challenges for commercial real estate financing in 2017?

A: Right now, we are dealing with perceptions and expectations. An example of perceptions is that long term interest rates are rising as we begin 2017, and we are already up about 100 basis points in rate from 2016. That may be true, but 2016 opened with the 10-year Treasury at 2.25%, only about 25 basis points below where today's treasury rates (2.50%) are. Though borrowers enjoyed a windfall when treasuries hit long time lows this past year, it's still an excellent environment to lock in long term debt.

Q: What impact has the Fed's actions had on CRE?

A: With the Federal Reserve's decision to raise short term rates at the end of 2016, expectations of additional increases in 2017 should focus owners on locking in their current and near future financing requirements, as markets perceive rates climbing significantly into 2017 and beyond. The new administration's focus on tax cuts and the currently robust nature of the economic cycle point to future inflation; a precursor to continued interest rate increases for real estate financing.

Q: In light of CMBS volatility, what do you see ahead for this component of the capital stack?

A: CMBS transactions were down significantly in 2016 for Newmark, similar to the wider marketplace due to a variety of factors. This is where expectations come into play. For a CMBS borrower, CMBS market volatility made it difficult to execute, particularly on acquisitions where the uncertainty associated with CMBS financing impacted the ability of buyer/seller to come to terms. For borrowers expecting life company execution on a Pacific Coastal market acquisition, current sale cap rates made it all but impossible for any buyer with less than 45% cash equity to fund.

We expect this trend to continue in 2017, as the market remains skittish on CMBS production. Of the transactions that Newmark closed in 2016, nearly all included the company as a servicer, as borrowers increasingly require a more dedicated level of service throughout the life of the loan. Attentive servicing will remain critical to CMBS performance and new issues in 2017.