

IS BRIDGE FINANCING FOR YOUR TRANSACTION?

AN ARBOR WHITE PAPER



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OVERVIEW

The commercial real estate market recovery has continued despite global and macro-economic instability. Investment returns wouldn't be where they are today without their share of supporting factors, including the strength of the multifamily real estate sector, where investors are doing well in rising numbers. The availability of relatively inexpensive multifamily financing has clearly helped draw the attention of savvy investors.

"There is a large variety of financing options today for multifamily investors, with institutions like Fannie Mae, Freddie Mac and FHA providing what many believe are the best available options," said Ivan Kaufman, Arbor Commercial Mortgage's Chairman and CEO. "But with the stabilization of the commercial real estate market other alternative financing options have additionally emerged, serving more specialized needs, including critical interim financing. For those needs, quite often the right product is a bridge loan.

THE BRIDGE DEMAND

Two factors have combined to produce the bridge financing demand we see today within commercial real estate and the multifamily arena in particular. First, there exists many cash-starved and distressed commercial properties across the country. But these distressed properties often present great opportunities for strategic investors, especially in the multifamily sector, where fundamentals and investment returns are the strongest in comparison to the other commercial real estate asset classes. With permanent financing lenders maintaining their high levels of underwriting standards these days, there are many strong investment scenarios nationwide that would suffer without short-term bridge financing supporting investors on their way to eventual permanent debt. We continue to see many properties as great candidates for bridge financing. These include assets that are capital-starved, over-leveraged or part of larger portfolios, where investors are forced to sell because they are financially impaired or have reached discounted payoff or short sale agreements with their lenders.

The list of transactions requiring bridge financing is a long one these days and also includes traditional acquisitions, refinancing, debt buy-backs with fresh equity, properties in lease-up, acquisitions with rehab components and acquisitions with nearly completed new construction.

OPTIMIZING YOUR PERMANENT FINANCING

In other circumstances, there are many investors whose assets do qualify for permanent debt, but choose to delay that option in favor of a one- to three-year bridge loan. The strategy here is that with an asset — in its owner's judgment — still underperforming, available permanent loan leverage will be less than what it would be following a few more years of seasoning and stabilization under a bridge loan. The investment opportunities that are in lock step with the increasing availability of competitively priced bridge financing are clear when looking deeper into the multifamily sector today, and not only because of its strong fundamentals and returns. Multifamily assets have short-term leases and, therefore, respond more rapidly to market changes, meaning a bridge loan is often

all an investor needs in the interim to quickly turn around an underperforming property. With investment possibilities like this in large supply, combined with strong multifamily returns, bridge-financing demand has been especially strong.

LOOK FOR ONE LENDER

With any bridge loan, the borrower must always have an eye on the permanent loan exit strategy, and within the multifamily sector, long-term Fannie Mae, Freddie Mac, FHA and CMBS financing is often the best execution. Ideally, though, in order to keep take-out fees at a minimum and optimize the efficiency of the overall bridge-to-permanent loan process, borrowers will look for lenders that can provide both bridge and permanent financing in a one-stop-shop format.

Arbor was the bridge lender in a recent transaction that exemplifies this type of demand. The borrower on a 98-unit multifamily property in Dallas needed a recapitalization in order to bring its asset to full stabilization following a major propertywide renovation. But the borrower was seeking a one-stop shop to provide both the interim and eventual permanent financing. Arbor provided the \$14.5 million bridge loan that allowed the asset to be recapitalized and stabilized with rapidly rising rents. Arbor simultaneously began work on the asset's permanent loan through Fannie Mae, satisfying the borrower's original parameters and providing an execution efficiency not seen if a bridge lender and a separate permanent loan lender were separately brought into the transaction scenario.

OUTLOOK FOR BRIDGE FINANCING

Taking a look further into the bridge lending market, there also seems to be a developing separation between lenders that will only transact above \$20 million deals and a special few that will also serve the below \$20 million market. Above \$20 million, loan pricing seems to be consistent across the board with so many lenders serving the space. However, pricing seems to be much wider below the \$20 million mark, with fewer lenders present. Certain savvy lenders have taken note of the strong bridge financing demand below \$20 million and are increasingly targeting the space, which is often viewed as an underserved market.

While it seems that conditions are nearly perfect for investors to take advantage of current bridge lending options and their associated investment opportunities, it begs the question of when and why conditions could change. The simple answer, without being able to predict significant macro-economic changes, is that attractive and highly available commercial bridge financing should be here to stay for some time in response to a steady amount of over-aggressive loans rolling off lenders' books, resulting in a continual supply of distressed or cash-starved properties. Or, in another way of looking at it, the unique and strong investment opportunities found today should continue to exist for the foreseeable future thanks to the critical support of bridge financing.

ABOUT US

For over 25 years, Uniondale, NY-based Arbor Realty Trust, Inc. (NYSE: ABR) has been helping multifamily and commercial real estate clients achieve their financial goals by focusing on growing long-term relationships and conducting business as not simply another real estate lender, but a partner. We value our clients to such an extent that we are more comfortable calling them partners, and their relationships with Arbor are the foundation of our business.

Founded by Chairman and CEO Ivan Kaufman, Arbor Realty Trust, Inc. is a real estate investment trust and direct lender specializing in loan origination and servicing for multifamily, seniors housing, healthcare, single-family rental portfolios and other diverse commercial real estate assets. Arbor is a Top 10 Fannie Mae DUS® Multifamily Lender by volume and a Top Fannie Mae Small Loan lender, a Freddie Mac Optigo® Seller/Servicer and a Top Freddie Mac Small Balance Loan Lender. Arbor is also a Fannie Mae and Freddie Mac Seniors Housing Lender, an FHA Multifamily Accelerated Processing (MAP)/LEAN Lender, a HUD-approved LIHTC Lender as well as a CMBS, Bridge, Mezzanine and Preferred Equity lender, consistently building on its reputation for service, quality and flexibility. With a current servicing portfolio of more than \$20 billion, Arbor is a primary commercial loan servicer and special servicer rated by Standard & Poor's with an Above Average rating. Arbor is also on the Standard & Poor's Select Servicer List and is a primary commercial loan servicer and loan level special servicer rated by Fitch Ratings. Arbor Realty Trust is externally managed and advised by Arbor Commercial Mortgage, LLC. ■

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