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Spotlight on Credit Tenant Lease Financing September 2016

This month's spotlight focuses on Credit Tenant Lease ("CTL") financing. Credit Tenant Lease financing is an alternative source of financing for single tenant net-leased real estate assets supported by credit tenants, typically investment grade with published credit ratings by Moody's or Standard & Poor's. While a bond lease (a lease where the lessee performs all obligations related to the leased premises) is the ideal structure for CTL loans, triple net leases, and even double net leases (if appropriate reserves for expenses are deducted) can qualify. CTL loans can be closed within 45 calendar days from application, offering real estate owners and developers the opportunity for faster execution for construction, acquisition, and refinance loans. Emphasizing the credit quality of the tenant, a CTL loan is primarily underwritten on the underlying credit of the tenant and is collateralized with a first lien on the property and assignment of the lease payments.

CTL financing has developed into one of the most aggressive forms of structured financing in recent years. These aggressive standards generally include high loan-to-cost ratios and low DSCRs. Maximum LTV is usually up to 95%, and sometimes even over 100%. Borrowers can typically lock interest rates upon acceptance of the commitment and payment of all deposits. They can expect pricing at a spread over Treasury yields or above the average life, with the spread correlating with the quality of credit, size of transaction, lease structure, and transaction structure.

CTL structures are attractive to property owners for several reasons. First, due to the low DSCR requirements, borrowers can acquire assets with significantly less equity. Second, for investors looking to offset passive income with passive losses, the "zero cash-flow" nature of the deal provides the ability to generate material after tax returns due to the write off of depreciation and interest expense on the property.

Credit Tenant Lease Overview

- Rates: Typically fixed spread over Treasury yields or the average life
- Term: Self-amortizing structure over underlying lease period
- Leverage: 70% to 95%, sometimes up to 100%; DSCR as low as 1.0x
- Product Type: Retail, Office, Industrial
- Recourse: Non-recourse
- Investors typically view the financing as a bond rather than a real estate loa

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Rates Comparison Chart

	Current September 2016	Year Ago September 2015
3-Month LIBOR	0.81%	0.31%
5-Year Swap	1.10%	1.62%
10-Year Swap	1.54%	2.18%
5-Year Treasury	1.15%	1.73%
10-Year Treasury	1.43%	2.28%

Recent Transactions

THE TRAILS APARTMENTS
Dallas, TX

Close Date:	August 2016
Units:	20

WOODLEY PARK MIXED-USE
Washington, D.C.

Close Date:	August 2016
Units:	2 residential, 1 commercial

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