Green Street
Commercial Mortgage Alert
THE WEEKLY UPDATE ON REAL ESTATE FINANCE & SECURITIZATION

# Mezz Lenders Prep for Surge in Originations

The field of high-yield lenders is getting more crowded amid a long-running pullback by originators of senior loans on commercial properties in the U.S.

**Commercial Mortgage Alert's** 12th annual survey of high-yield lenders has identified 163 shops that provide subordinate debt on commercial real estate via mezzanine loans, B-notes and preferred-equity investments. That total, including 101 firms that also finance construction projects, is up from 152 lenders that made the list a year ago and 144 in 2021 (see list on Pages 21 to 48).

Of the 115 survey respondents that divulged their 2022 volumes of subordinate debt and their comparable projections for this year, 88 are calling for an increase in their annual lending volume. Of the rest, 17 lenders predict their originations will decrease this year, and 10 expect to match last year's tally.

**Acore Capital** and **Blackstone** have the largest origination projections for this year, with each anticipating at least $2 billion. They're followed by **Affinius Capital** ($1.7 billion), **Rockwood Capital** ($1.58 billion), **Wells Fargo** ($1 billion to $1.5 billion) and **BlackRock** ($1 billion to $1.25 billion). **Citigroup, Goldman Sachs** and **IBI Volcano Investments** expect to originate $1.5 billion apiece this year, and **Deutsche Bank** projects $1.25 billion. Meanwhile, eight other lenders each weighed in with a $1 billion estimate for 2023: **Brookfield, BMO Capital, CIM Group, CPP Credit Investments, JPMorgan Chase, Morgan Stanley, New York Life Real Estate Investors** and **Oxford Properties,** the real estate arm of **Omers,** which represents Ontario municipal employees.

In a sign of increasing demand for subordinate financing, 12 firms are making their debut on the list of high-yield lenders this year, and another six are reappearing on it for the first time in two to four years. Among the firms never on the list before, those with the highest lending volume projections are IBI Volcano and **GreenBarn Investment,** which expects to originate at least $500 million of subordinate debt.

The rise in mezzanine originations comes amid a widespread pullback by senior lenders since early last year due to rising interest rates, rampant capital-market volatility and the regional bank crisis. Those factors also have sharply constrained commercial real estate sales and lending, triggering a plunge in property values.

As a result, subordinate financing has become a key part of refinancing or funding acquisitions of many properties. Mezzanine lenders are eager to meet that demand because they can achieve higher returns with less risk than was possible only a few years ago.

"This is a once-in-a-decade opportunity to originate high-quality mezzanine loans on a risk-adjusted basis," said **Invesco Real Estate** managing director **Charlie Rose.** "Mezzanine lenders are well-positioned to fill in the gap, as conventional lenders may be less active in the market and more constrained by their credit profiles."

The field of mezzanine lenders is likely to keep expanding, he said, because the fundamental credit quality of commercial real estate remains relatively solid outside the office sector. "From disruption comes opportunity," Rose added. "I expect the attractiveness of real estate credit is going to get a lot of attention in the near and moderate term."

The industry consensus is that subordinate lending will pick up markedly as more of the properties collateralizing a large wave of maturing debt are refinanced, recapitalized or sold over the next two years. Borrowers and potential buyers of commercial properties have been slow to accept prevailing interest rates and property values since the market soured last year, but market players said the looming maturities eventually will force their hand.

The loan offerings "we are seeing right now are [on] the lower-quality assets," said **King Street Capital Management** managing director **Mark Van Zandt.** The owners of such properties "have fewer options available to them as loans come due. As this process plays out later this year and next year, you will begin to see [opportunities to lend on] higher-quality assets with institutional sponsors."

Like most real estate investors in the current cycle, subordinate lenders are focusing heavily on multifamily and industrial properties. The outlook for office lending is murky, however, due to an acceleration of the work-from-home trend during the pandemic that has severely undermined efforts to project future rents and occupancy rates.

"Most investors want nothing to do with the asset class," Van Zandt said, noting that the U.S. already had "just way too much office space" before the pandemic. "I think there will be very selective [lending] opportunities that arise with outsize returns." ❖

**COMMERCIAL MORTGAGE ALERT:** June 9, 2023