First Quarter 2017 Recap
Capital Markets Report

NVC

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The 10-year Treasury yield has fluctuated between 2.34% and 2.60% in the first quarter of 2017 similar to its December 31st closing rate of 2.45%. For the most part, all-in rates for Class A properties have seen little movement since last quarter, as spreads have either widened or contracted in offset to the associated rate change. Lenders appear to be intent at holding rates constant for the time being.

The general consensus is that the Fed will raise short-term interest rates several times in 2017 as was indicated at the March meeting. The main contributor to low long-term interest rates has been the Fed's decision to keep rates low during the recession and the recovery. Commercial real estate is generally debt intensive with the majority of loans having an LTV of 65% or less. The rise in interest rates may have a slight effect on property values but strong fundamentals and wide availability of debt should impede any outsized decrease. Interest rates are still near historical lows and investors recognize this fact.

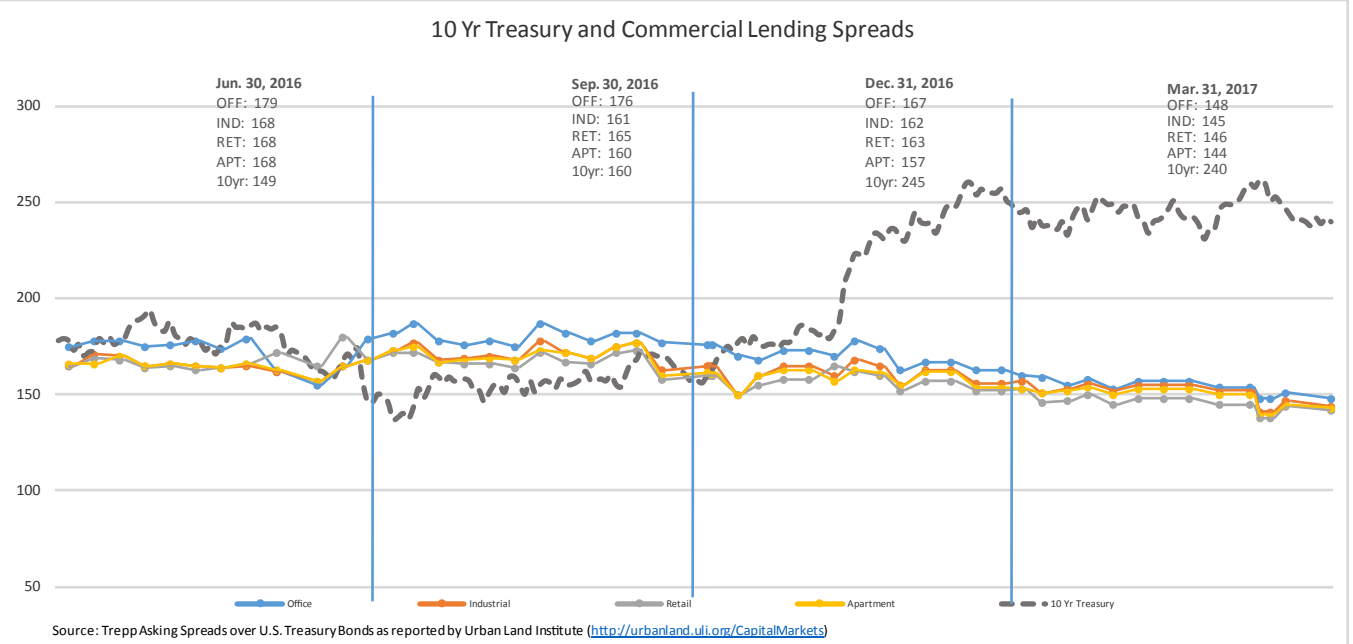
Commercial property deal volume fell 47% year-over-year in January, the largest monthly decline since 2009. Transaction activity for this January puts the market back somewhere at levels last seen in early 2013. Pricing is generally holding steady as buyers are becoming more cautious in their approach, as many believe the real estate cycle is in the late stages. Deal volume may continue to drop off as the expectations of buyers and sellers deviate.

Risk retention rules introduced as part of the Dodd-Frank Act, which took effect on Dec. 24, 2016, require CMBS originators to retain a 5 percent interest in transactions they originate. In 2016, CMBS issuances experienced an ample drop in transaction volume to $70 billion from north of $100 billion in 2015. While this was largely a result of the macroeconomic volatility in the first quarter 2016, concerns persist that risk retention may further compound the conduit market's struggles going forward. According to some mortgage loan originators, risk retention requirements could see CMBS loan pricing jump 15 to 25 basis points in 2017.

2017 should also see an increase in non-traditional lenders and non-bank lenders. Mortgage real estate investment trusts, debt funds and development firms have played an increasing role in the market particularly with mezzanine loans. Mezzanine loans allow groups normally associated with development to find similar yields without taking the construction/lease up risk that the sponsors assume. The non-traditional lender sector of the market has usually accounted for around 20 percent of total lending volume in recent times, according to CBRE research, and is likely to play a larger role as traditional lenders face capital constraints.

While bank lending on new construction is down over the past 12 months, banks are still expected to play a substantial role for funding mid-sized transactions that are not as attractive to life insurance lenders. Many insurance companies have larger allocations this year than they did in 2016 and are prepared to selectively fill the gap created by increased regulations on banks and CMBS lenders.

Commercial Lending Spreads



Source: Trepp Asking Spreads over U.S. Treasury Bonds as reported by Urban Land Institute (http://urbanland.uli.org/CapitalMarkets)

Property Type	History			Recent Transactions		Concluded Spreads	
	2Q16 Spreads	3Q16 Spreads	4Q16 Spreads	Spread Range (bps)[1]	Average	1Q17[2]	Change from 4Q16
Office							
CBD	175	170	170	165 - 195	171	170	0
Suburban	215	210	210	190 - 300	206	210	0
Retail							
Grocery Anchored	200	200	200	170 - 245	199	200	0
Power Center	245	245	245	160 - 295	238	245	0
Unanchored	260	260	260	250 - 300	275	260	0
Multifamily	175	170	170	150 - 206	172	170	0
Industrial	190	185	185	145 - 225	185	185	0
Hotel	235	235	235	195 - 275	226	235	0
Construction	290	300	300	300 - 325	306	300	0

[1]NVC Survey of institutional lenders and brokers for loans of $10 million or more for 10 year terms.

[2]Asking Spreads over U.S. Ten-Year Treasury Bonds for properties with 50% to 59% LTV.

NVC surveyed a variety of lenders and financial intermediaries to understand current trends in the capital markets and support our determination of market rates based on recent transactions. Responses to the survey, and general sentiments, are provided below:

A respondent from a pension fund adviser reported that "life companies are aggressively bidding for top tier assets/sponsorship. The early activity in 2017 is primarily a function of this year's allocations needing to be met. CMBS lending is active, albeit for those lenders that have a risk retention solution for the 5% of the loan that they must retain. If you don't have a large balance sheet to fund the initial loan then the deal has too much execution risk for my liking." Morningstar Credit Rating and Trepp issued a flat forecast for CMBS production in 2017.

One mortgage banker from a national firm stated that "Life companies have lots of money to put out this year. They expect business to be as good this year as last and typical core deals are pricing with spreads of 165 to 180."

Life companies continue to lend on the low LTV, class "A" financing and are also lending to top tier sponsors on construction to permanent financings with terms of 15 years. Banks are unable to compete with loans that have a long term attached to them. Since the credit crisis, banks have made up a significant portion of lending volume, roughly 40%. That number fell to 30% towards the end of 2016 a result of the new regulations and a tightening credit process. Life companies picked up the decrease by the banks in the second half of 2016 and accounted for 35% of lending.

Several other respondents reported that spreads were in the 170 to 180 range for quality 10 year deals during the first quarter.

A commercial real estate lender from a large national bank said "our pipeline has decreased slightly given a reduced comfort level in the multifamily and hospitality sectors give large new supplies and historically high rents and ADRs. Spreads are between 275 and 375 for construction loans depending on leverage, location and sponsor. Our spreads are similar to last quarter and we do not anticipate significant movement in the near term. We have been doing some multifamily construction loans with spreads in the high 2's which is 25 - 50 bps higher than a year ago."

Recent Originations						
Property Type	Date	Fin Type	Spread	Coupon Rate	LTV	Term/IO/Am
Grocery Anchored Retail	Nov-16	Variable	215	2.66%	50%	7/7/0
Grocery Anchored Retail	Oct-16	Variable	210	2.61%	60%	7/7/0
Grocery Anchored Retail	Sep-16	Fixed	245	4.03%	70%	10/0/30
Grocery Anchored Retail	Nov-16	Fixed	173	3.33%	60%	7/7/30
Grocery Anchored Retail	Oct-16	Fixed	225	4.01%	65%	10/0/30
Multifamily	Jan-17	Fixed	150	3.85%	55%	10/10/30
Multifamily	Feb-17	Fixed	154	3.84%	63%	10/0/30
Multifamily	Dec-16	Variable	206	2.85%	60%	10/5/30
Multifamily	Oct-16	Variable	170	2.21%	50%	3/3/0
Multifamily	Oct-16	Variable	180	2.31%	65%	3/3/0
CBD Office	Feb-17	Fixed	155	3.90%	50%	10/10/30
CBD Office	Sep-16	Fixed	195	3.53%	65%	10/0/30
CBD Office	Nov-16	Variable	190	2.41%	55%	10/5/30
CBD Office	Sep-16	Fixed	180	3.38%	60%	10/0/30
CBD Office	Nov-16	Fixed	200	3.75%	60%	10/2/30
Industrial	Aug-16	Fixed	185	3.70%	60%	10/0/30
Industrial	Sep-16	Fixed	205	4.00%	65%	10/10/30
Industrial	Jul-16	Fixed	180	3.75%	70%	10/0/30
Industrial	Jul-16	Fixed	190	3.75%	60%	10/2/30
Industrial	Oct-16	Fixed	195	3.90%	65%	10/10/30
Construction	Sep-16	Variable	315	3.66%	65%	3/3/0
Construction	Jun-16	Variable	300	3.44%	70%	3/3/0
Construction	Oct-16	Variable	325	3.78%	65%	3/3/0
Construction	Aug-16	Variable	300	3.51%	65%	3/3/0
Construction	Nov-16	Variable	310	3.71%	65%	3/3/0
Suburban Office	Jan-17	Variable	210	2.87%	65%	10/2/30
Suburban Office	Jan-17	Variable	260	3.37%	60%	3/3/0
Suburban Office	Sep-16	Fixed	235	3.93%	70%	10/3/30
Suburban Office	Sep-16	Fixed	230	3.88%	70%	10/0/30
Suburban Office	Nov-16	Fixed	230	4.15%	65%	10/3/30

NVC Survey of institutional lenders and brokers for loans of $10 million or more

NVC's involvement in debt valuations and analysis includes a variety of assignments, from detailed reasonableness testing of portfolio loan ratings to opining on the impact of senior debt on the market value of the underlying real estate collateral. Our analysis considers loan-to-value, interest rate, remaining term, amortization, loan fees, penalties and other elements relevant to the assignment and prevailing market conditions.

In addition to individual loan valuation assignments, we currently mark to market more than 250 debt instruments for more than a dozen funds totaling $10 billion in loan balances.

About NVC

National Valuation Consultants, Inc. (NVC) is one of the largest privately held commercial real estate valuation and consulting companies in the U.S. with offices in Atlanta, Chicago, Cincinnati, Dallas, Denver, Houston, Parsippany and Tampa.

Since its inception in 1991, NVC has been focused on delivering high quality services to our growing client base, while maintaining the individual client touch. Our Valuation and Advisory Services groups provide a variety of valuation and consulting services to some of the largest companies and real estate funds in North America for the uses ranging from financial reporting and portfolio analysis to loan underwriting requirement and litigation.

With our extensive research department, highly experienced valuation staff, and central control, we are able to consistently exceed our client's expectations, while handling the most complicated valuation and consulting assignments.

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