



“We Scrambled, And Spoke With Well Over 100 Banks. Not One Will Provide Financing”

Description

“Credit started tightening six to nine months ago,” said the developer, a close friend, entrepreneur, with large residential projects across the nation. “It started with the money center banks,” he continued. “This pushed us to regional banks for our latest projects, but then SVB happened.” The market froze.

“The lender for our latest 30-story project in a tier-one city backed out, so we scrambled, and spoke with well over 100 banks. Not one will provide financing.” His firm is a leader in their market niche. A strong track record.

“The Fed is going to have to inject liquidity and slash rates to break this financing freeze on new construction.” Not only have higher rates failed to push home prices down materially, but they are now reducing new supply.

“And here’s something I’ve never seen. When we start a new project, we take out a construction loan. We rush to finish the project, start renting the apartments, repay the loan, and refinance at a lower rate.” The new loans typically have less risk and thus a lower rate than the original construction loans, which are structured with 3yr maturities plus an option to extend for 2yrs.

“But now, we have legacy construction loans with a 4.0%-4.5% interest rate, and we’ll extend those out for the full five-year term even though the projects are complete. If we paid them back and refinanced with permanent debt, the rates would probably be 6.5% fixed with no pre-pay option or 8.5%-9.0% floating. There’s no way anyone is going to pay back those low-rate loans that were originated before the hiking cycle.”

This is a new dynamic for banks. Their low-rate loans are being extended at the same time their deposit base is shrinking.

“We developed properties right through the 2008 cycle. What’s unfolding now is something else, new construction is going to hit the wall. The dramatic pace of interest rate increases has flipped everyone

upside down,” he said, well positioned. “Happy to sit on vacant lots. I can be patient.”

By Eric Peters, CIO of One River Asset Management

Category

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