



Commercial Lending School

CRE Lending—*Retail Income Properties*

October 20, 2025



David H. Ruffin | *Principal*



Today's Speaker



David Ruffin
Principal
IntelliCredit

- 51+ Years in Banking
- 16 years as Chief Credit Officer / Commercial Lender
- 3,000+ Loan Reviews
- ~350 Capital Raise or M&A Due Diligences
- Former Co-Founder of Credit Risk Management
- Prolific author and speaker on credit risk topics

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What Do You Think?



Loan & Deposit Growth / Yields & Cost of Funds



CAVA Loan / Deposit Growth Trends: Banks <\$10B



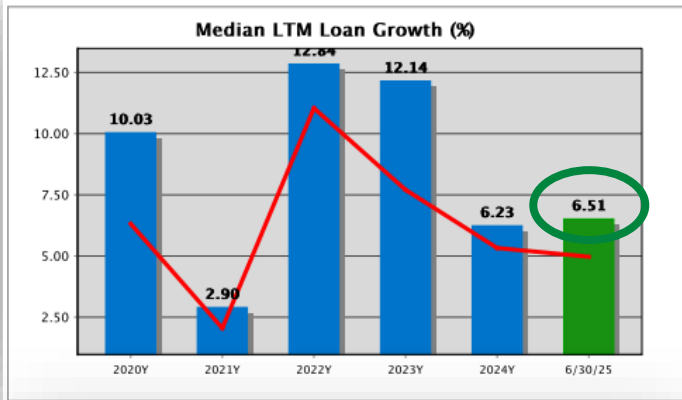
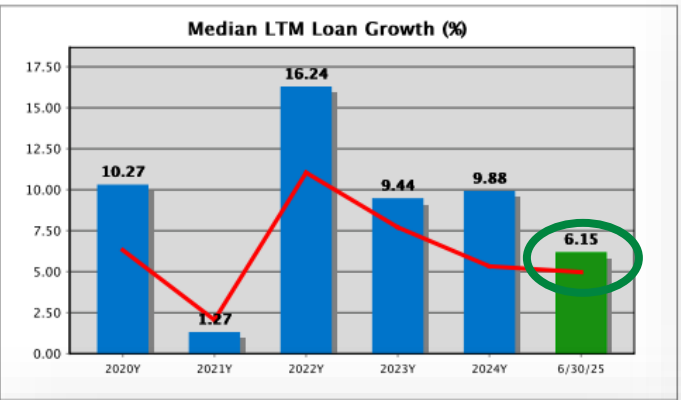
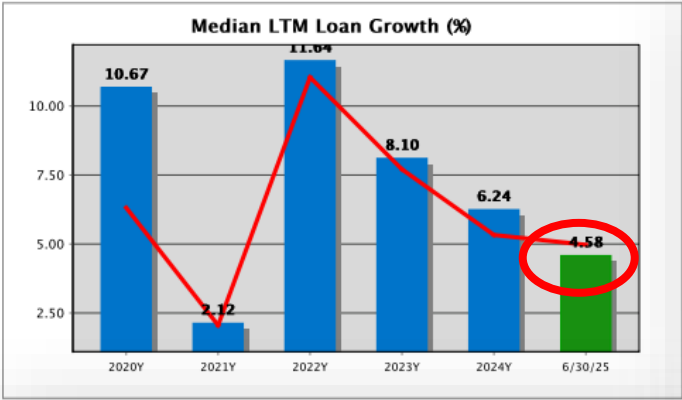
Q2 '25 Call Report Data

VA

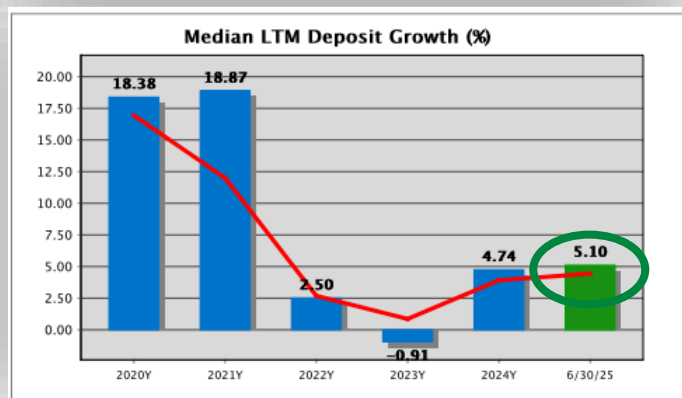
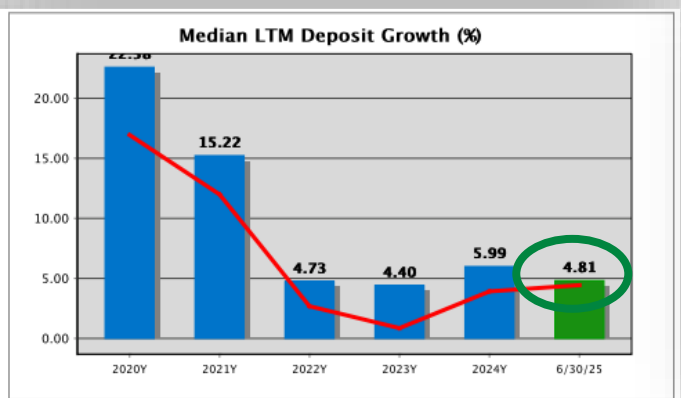
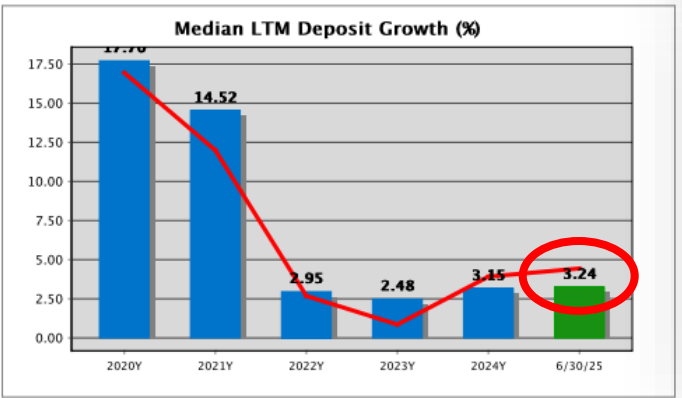
NC

SC

Loans

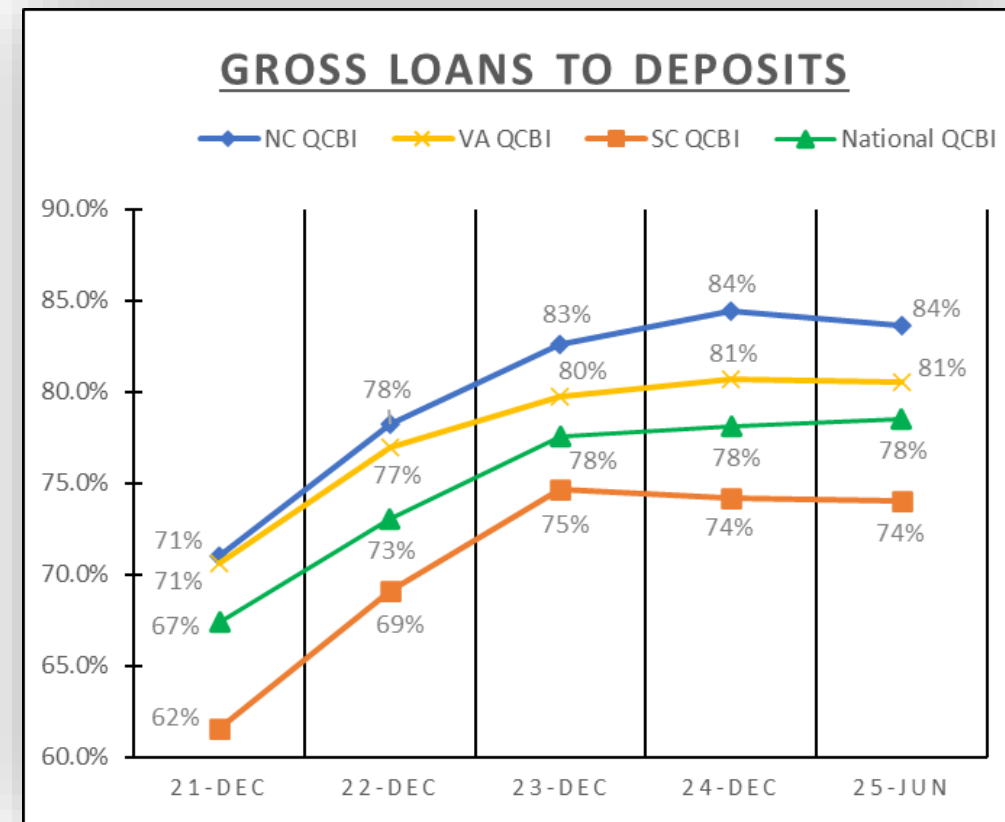
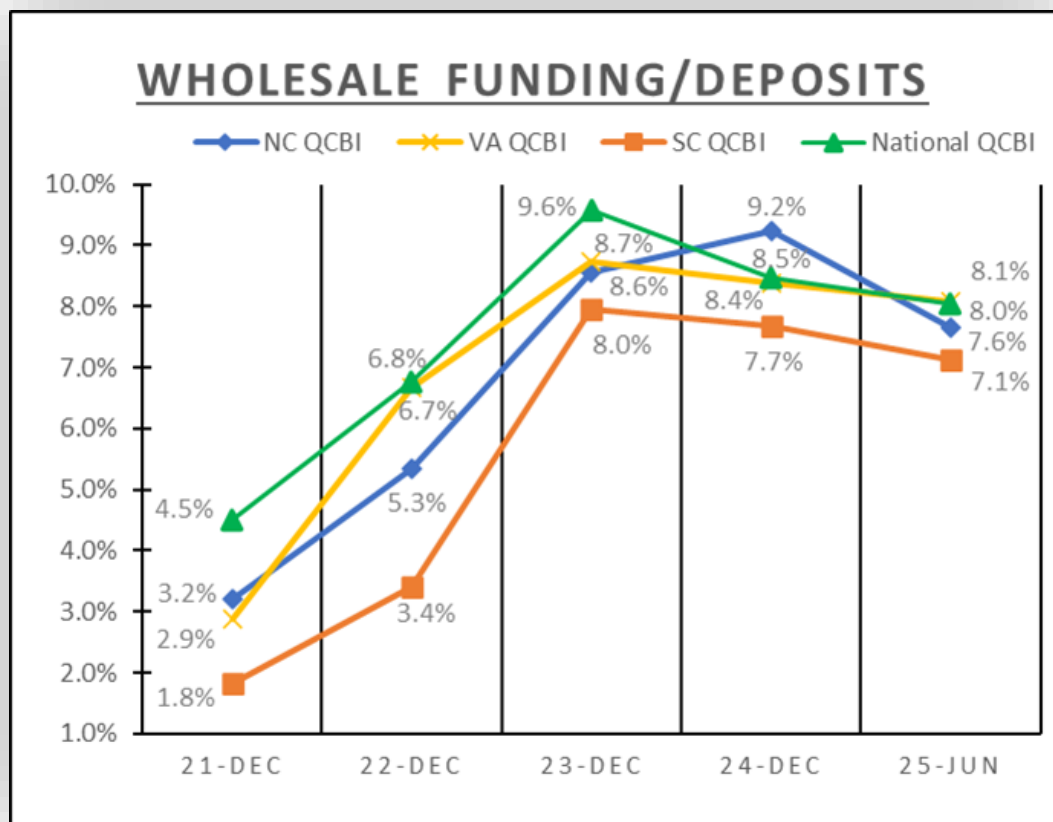


Deposits



CAVA Wholesale Funding / Loans-to-Deposits: Banks <\$10B

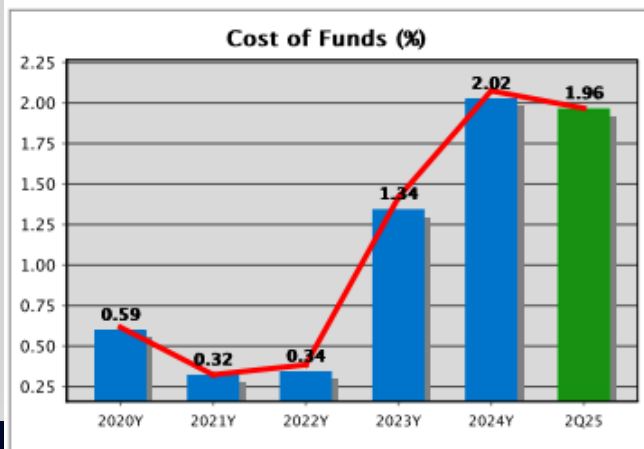
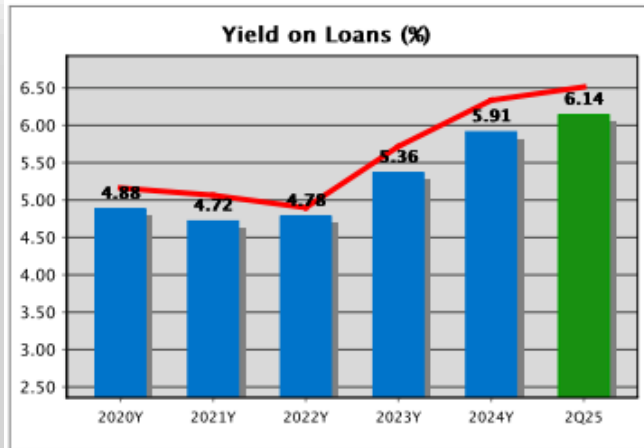
Q2 '25 Call Report Data



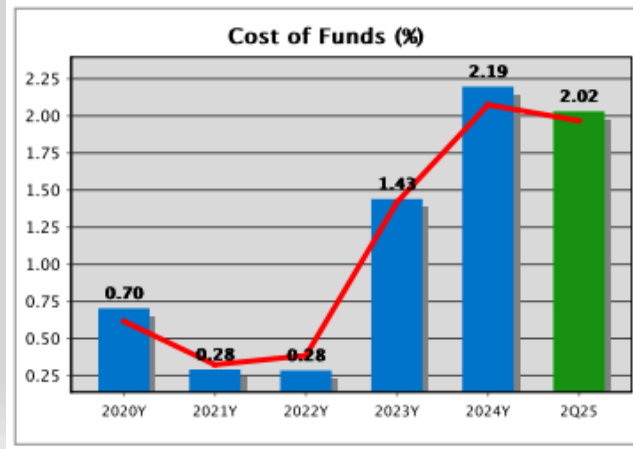
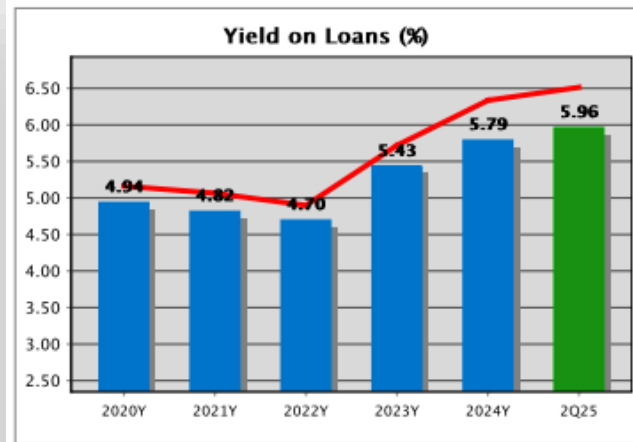
CAVA Loan Yields / Cost of Funds Trends <\$10B

Mixed-to-Below National Trends

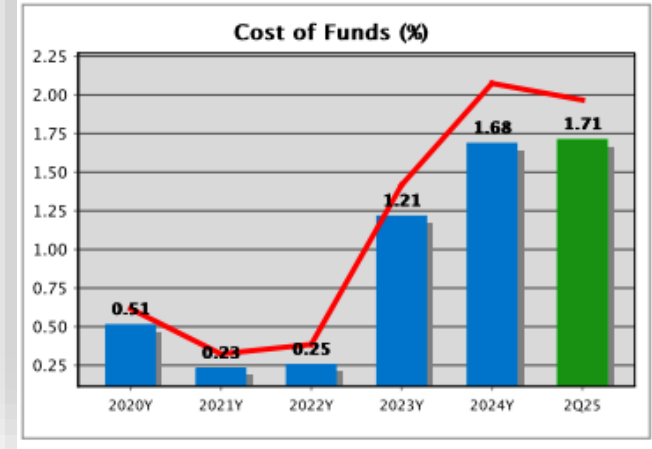
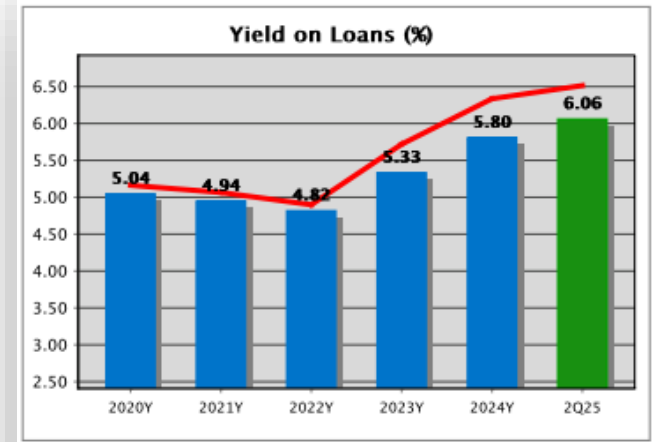
VA



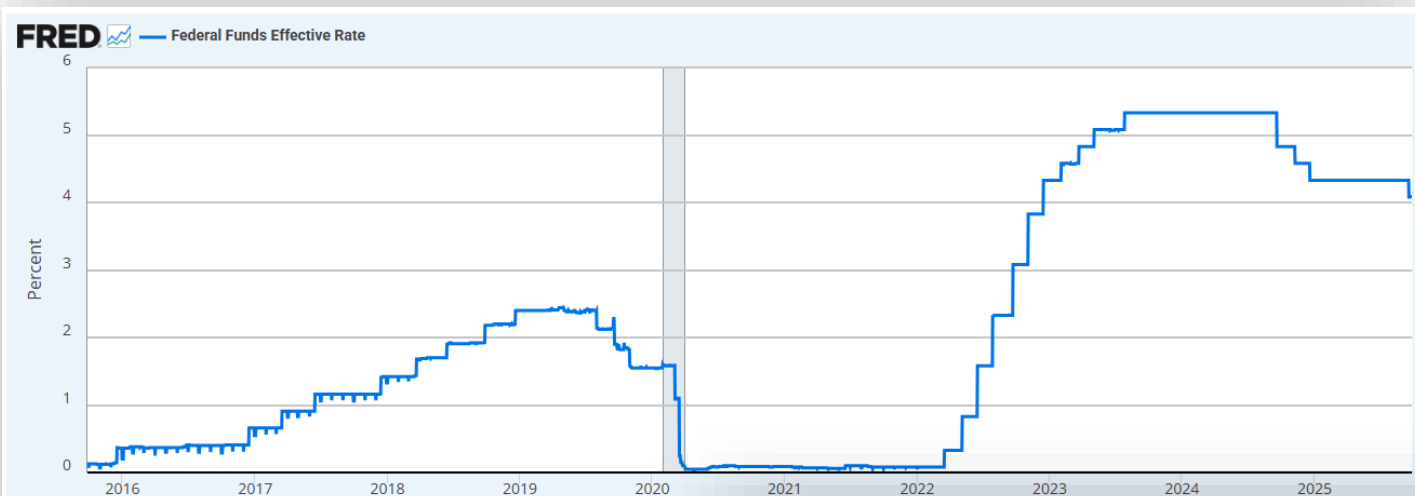
NC



SC



Fed Funds Rate (Last 10 years / Last 50 years)



Source: Board of Governors of the Federal Reserve System (US) via FRED®
Shaded areas indicate U.S. recessions.

👉 Last 10 Years

Last 52 Years 👉



Source: Board of Governors of the Federal Reserve System (US) via FRED®
Shaded areas indicate U.S. recessions.

fred.stlouisfed.org

Fullscreen

First Half '25 Credit Landscape & Performance



What's the Current Credit Landscape?



The word “challenging” comes up in most surveys; trends we’re seeing are:

Growing uncertainty about the economy (particularly short-term)

Rate and inflation shocks continuing to have negative credit implications

CRE segment obsolescence is growing (*teleconferencing / digital shopping / remote work*)

Disproportionate CRE exposure at smaller banks

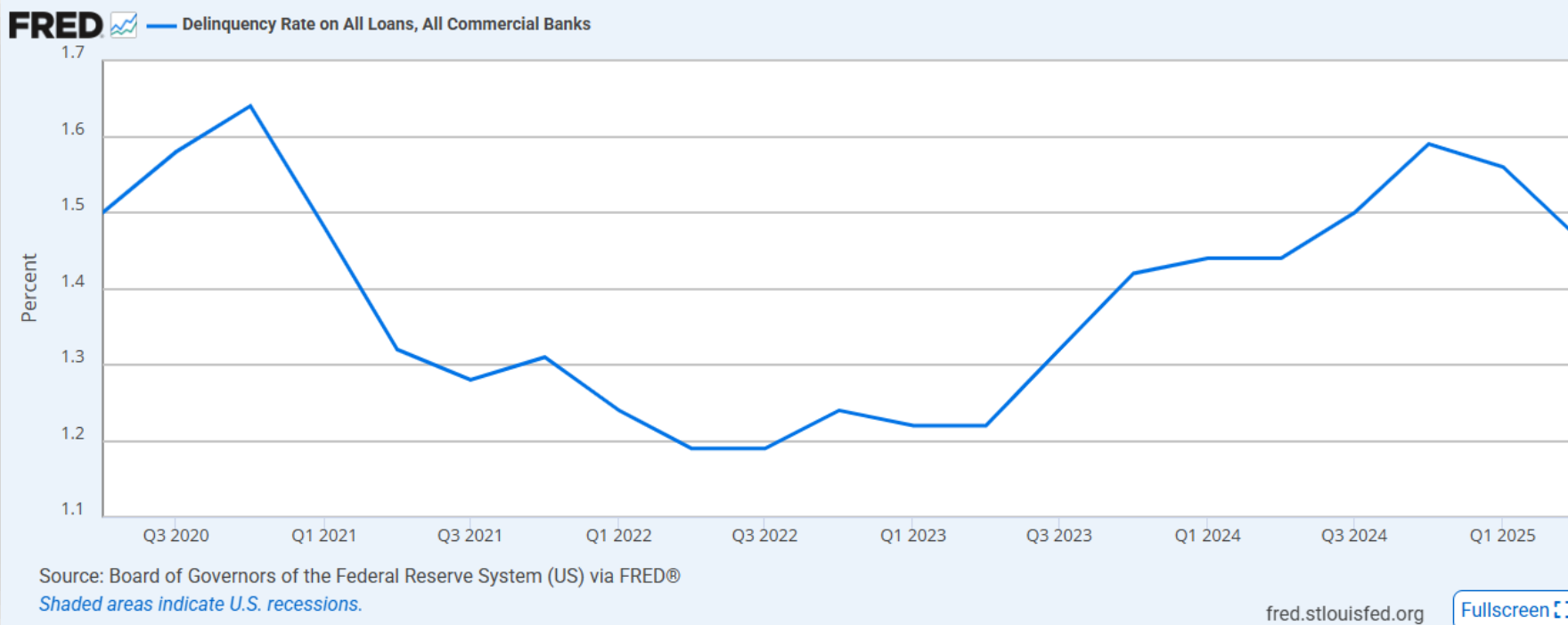
Growing lenders’ negative sentiment on credit quality—contrasted w/c-suite optimism

Increased loan review risk downgrades over the past several months

Credit risk may be replacing rate risk in M&A space

Regulatory scrutiny: *credit processes vs. transactional credit weakness*

Delinquencies all loans last 5 years—*consumers leading*



30-day Past Dues*

SF Mortgages	1.79
Credit Cards	3.05
Consumer Loans	2.76
CRE Loans	1.57
Business Loans	1.28

*Q2 '25

Trifecta of Loan Quality: Banks <\$10B

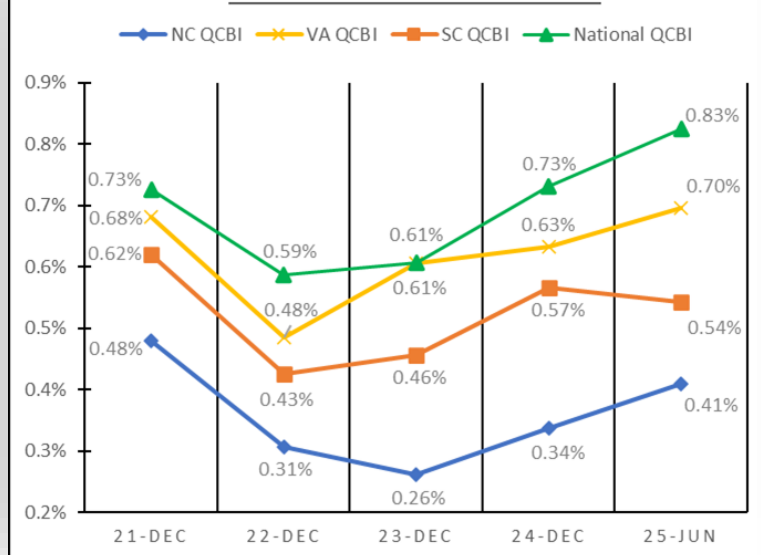


Q2 '25 Call Report Data QwickAnalytics®

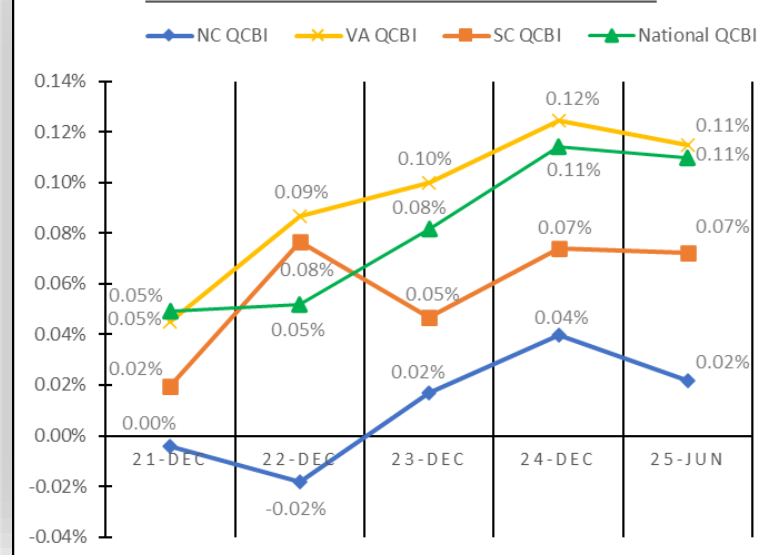


VA / NC / SC / National

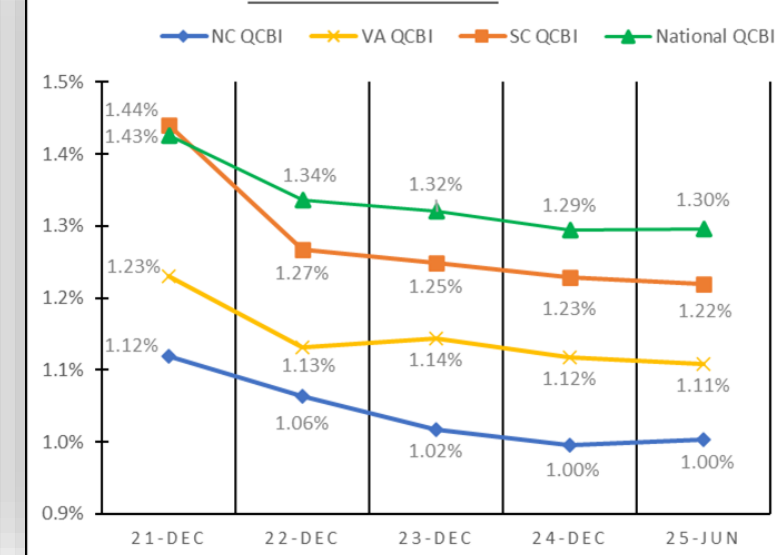
TOTAL NPL TO LOANS



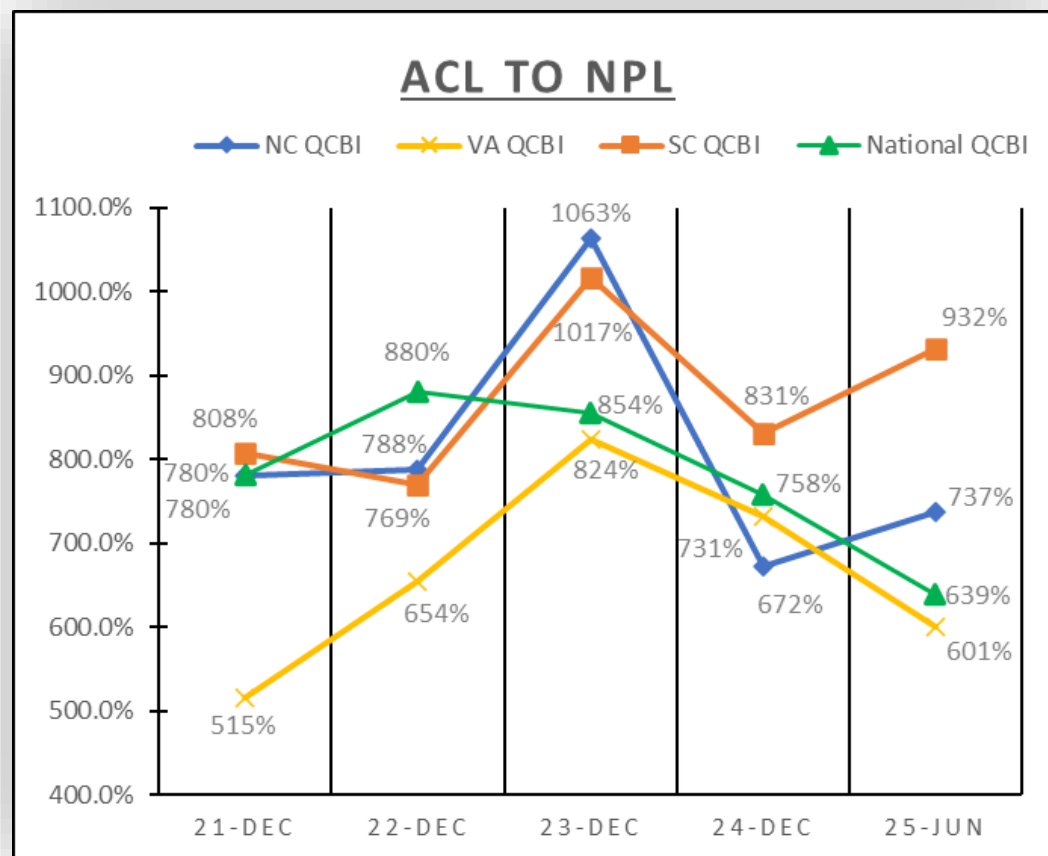
NET CHARGE-OFFS TO LOANS



ACL TO LOANS



Trifecta of Loan Quality: Banks <\$10B



QwickAnalytics®

Q2 '25 Call Report Data

ACL Coverage of NCL's YOY as of Q1 '25:

- Community Banks: ↓42%
- All Banks: ↓ 8%

The reserve coverage ratios declined due to non-current loans increasing at pace greater than provisions.

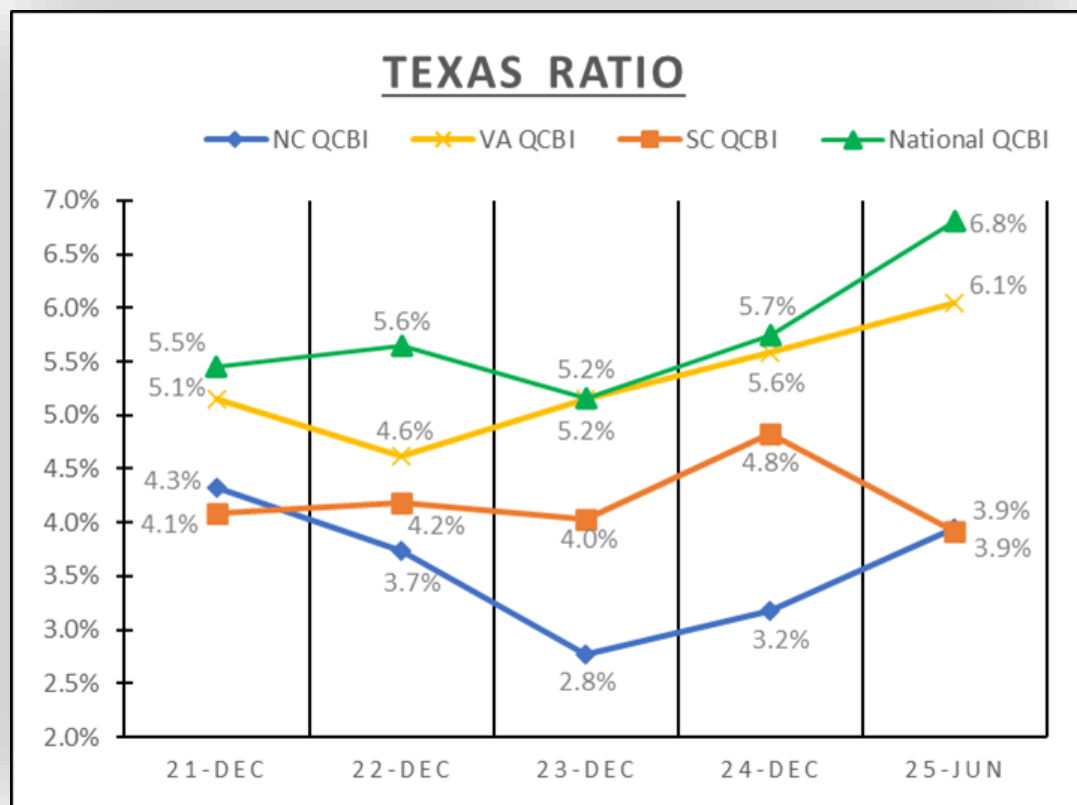
Source: FDIC

Texas Ratio: Banks <\$10B

Q2 '25 Call Report Data

VA / NC / SC / National

QwickAnalytics®



Texas Ratio Defined:

$$\frac{\text{Non-Performing Assets (NPA)} + \text{Loans 90+ Days Past Due}}{\text{Tangible Common Equity} + \text{Loan Loss Reserves}}$$

Credit Stress Indicator - The ratio essentially compares the bank's problem assets to the capital available to absorb losses.

When this curve turns upward, recall the small-bank dilemma:

- Reluctance to act against known borrowers
- Outsized capital and reputational hit from losses
- Heavy reliance on real estate—the most illiquid problem asset

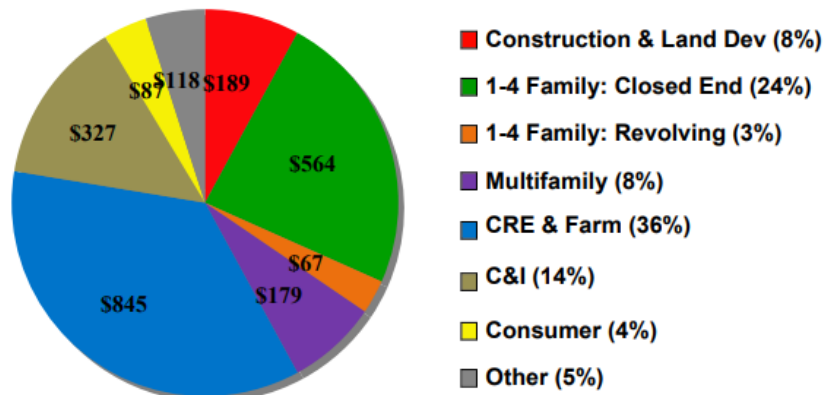
So, Let's Look Specifically at CRE



CAVA & National RE Exposure: Banks <\$10B

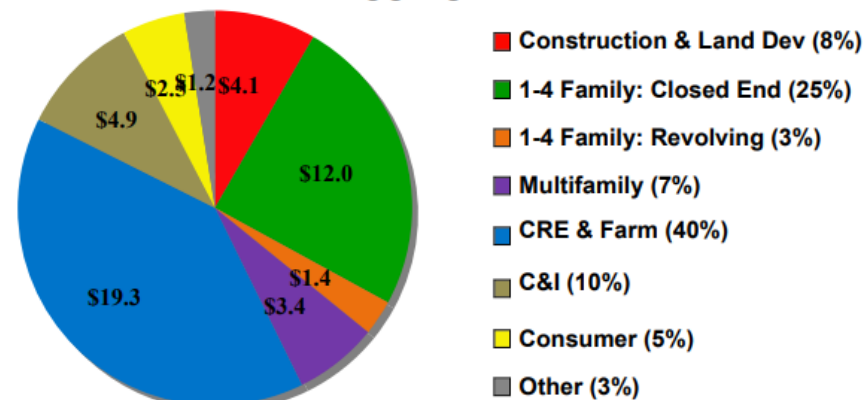


National Aggregate Loan Mix



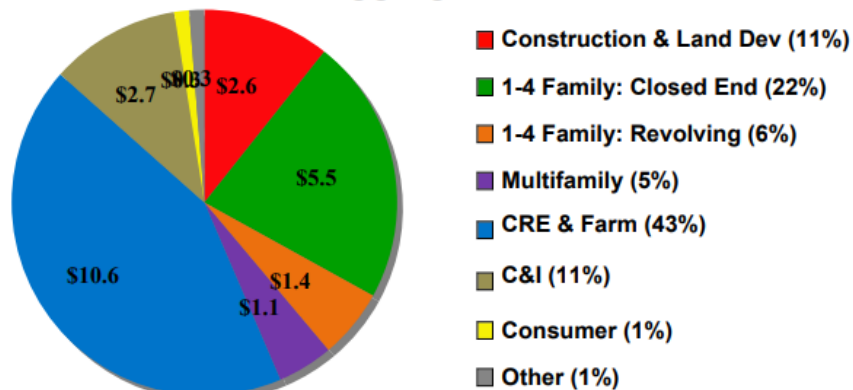
US: 79% RE

State Aggregate Loan Mix



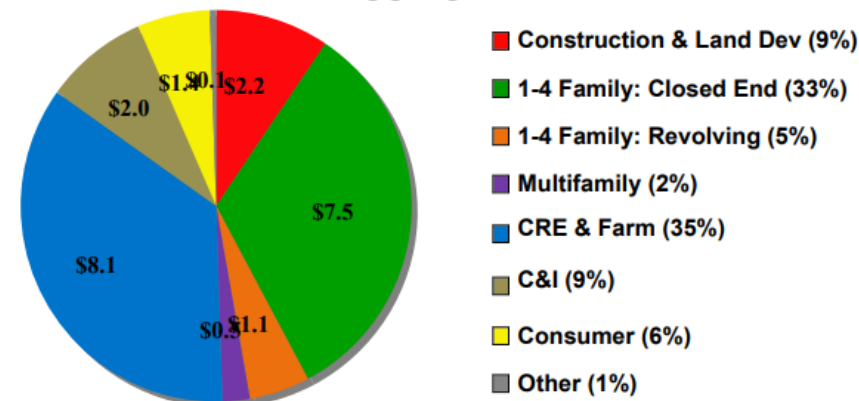
VA: 83 %RE

State Aggregate Loan Mix



NC: 87% RE

State Aggregate Loan Mix



SC: 84% RE

(\$ billions)

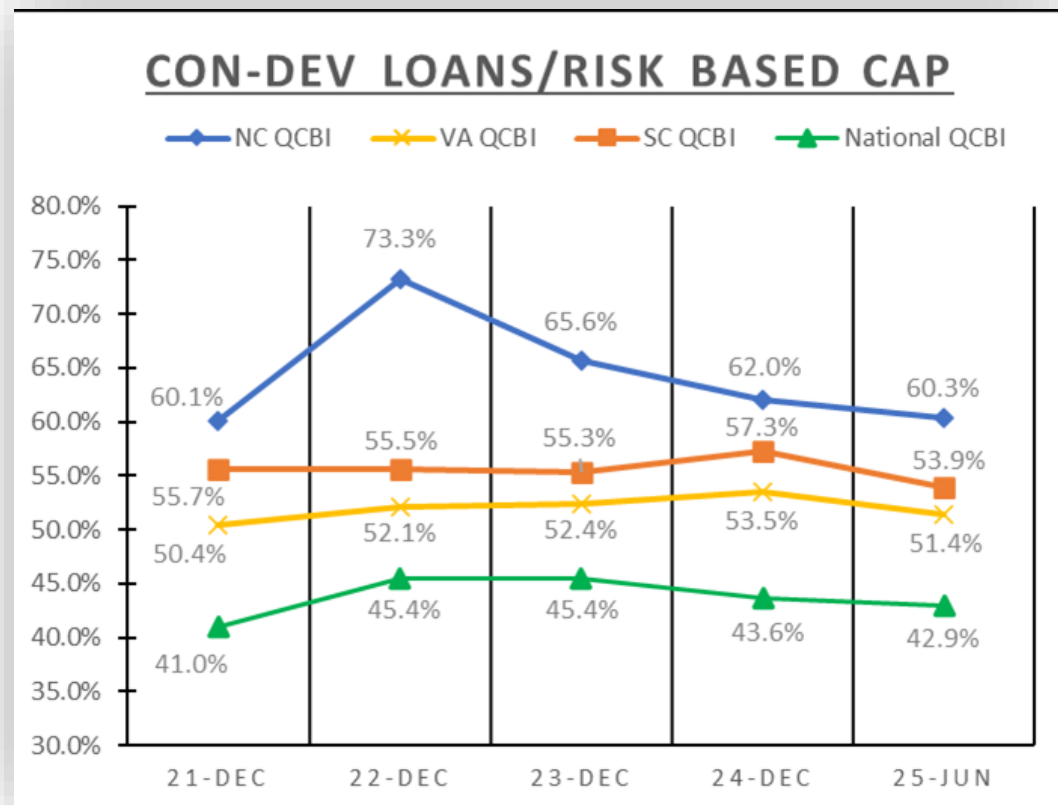
CAVA CRE Concentrations: Banks <\$10B



Regulatory Guidance:
≤ 100% RBC

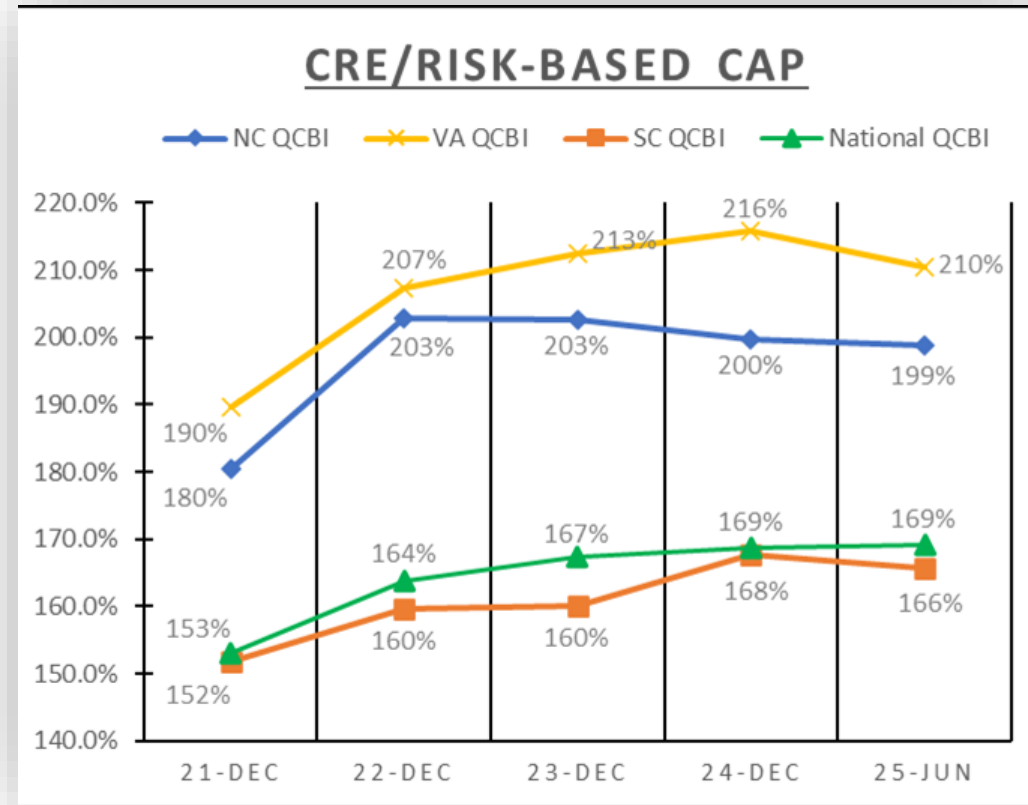
Q2 '25 Call Report Data*

Regulatory Guidance:
≤ 300% RBC



NC: 4 / SC: 3 / VA: 5 / National: 181

↑ 100%



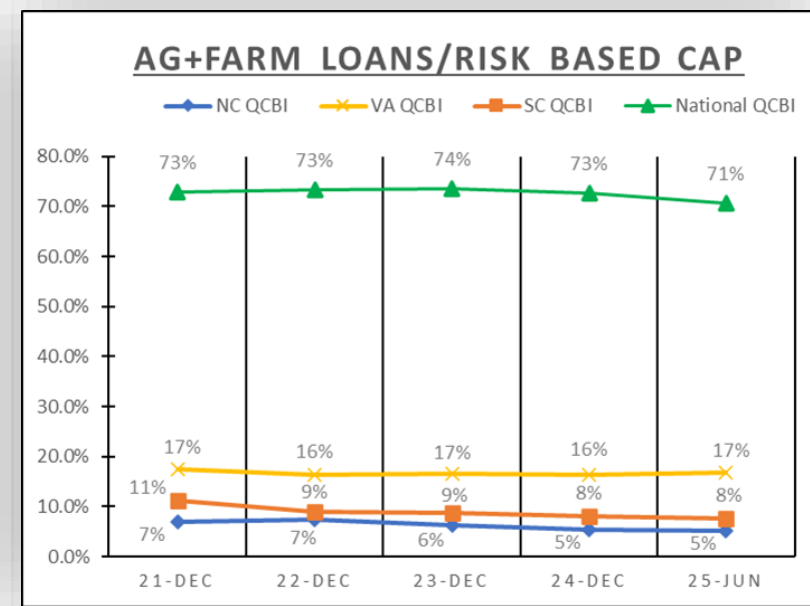
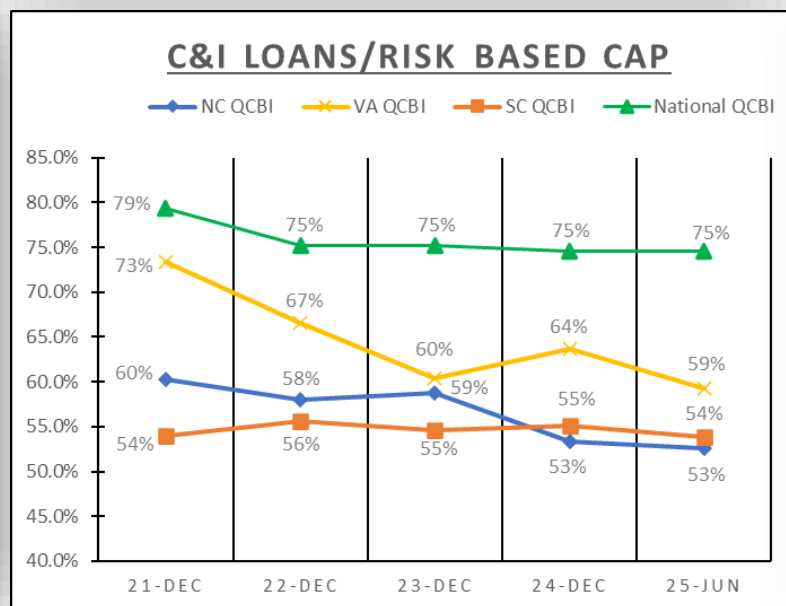
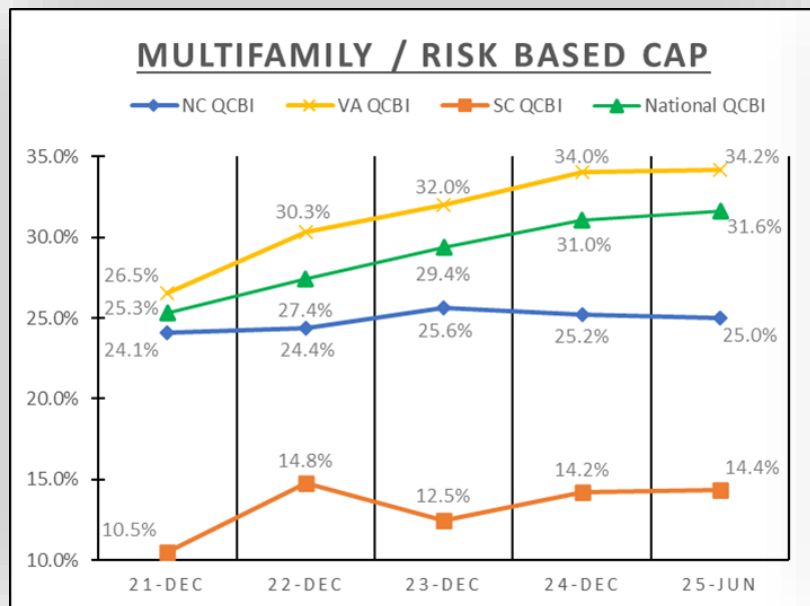
NC: 3 / SC: 3 / VA: 9 / National: 299

↑ 300%

Other CAVA Concentrations: Banks <\$10B



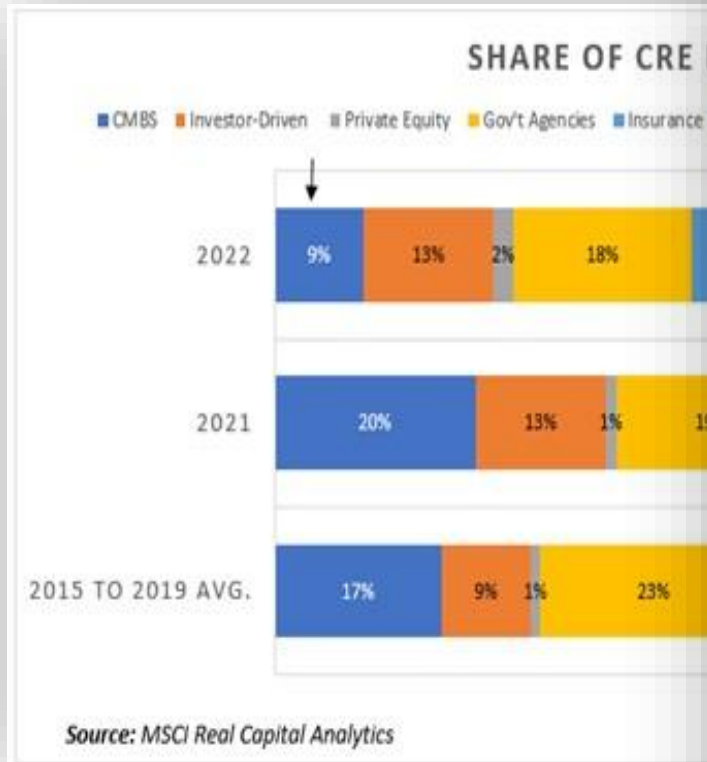
VA / NC / SC / National



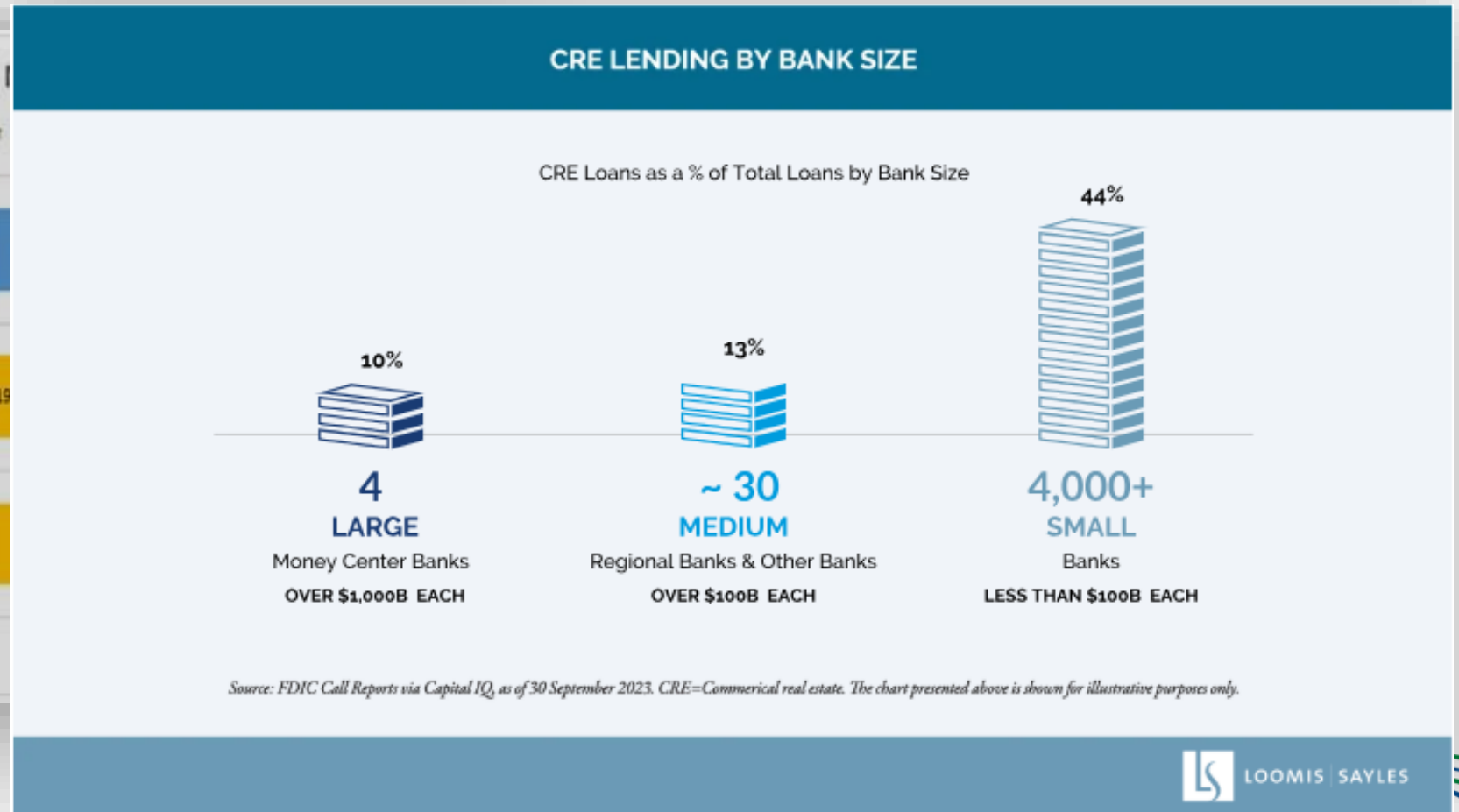
Community And Regional Banks: *CRE Exposure Disproportionately Higher!*



All CRE Funding Sources

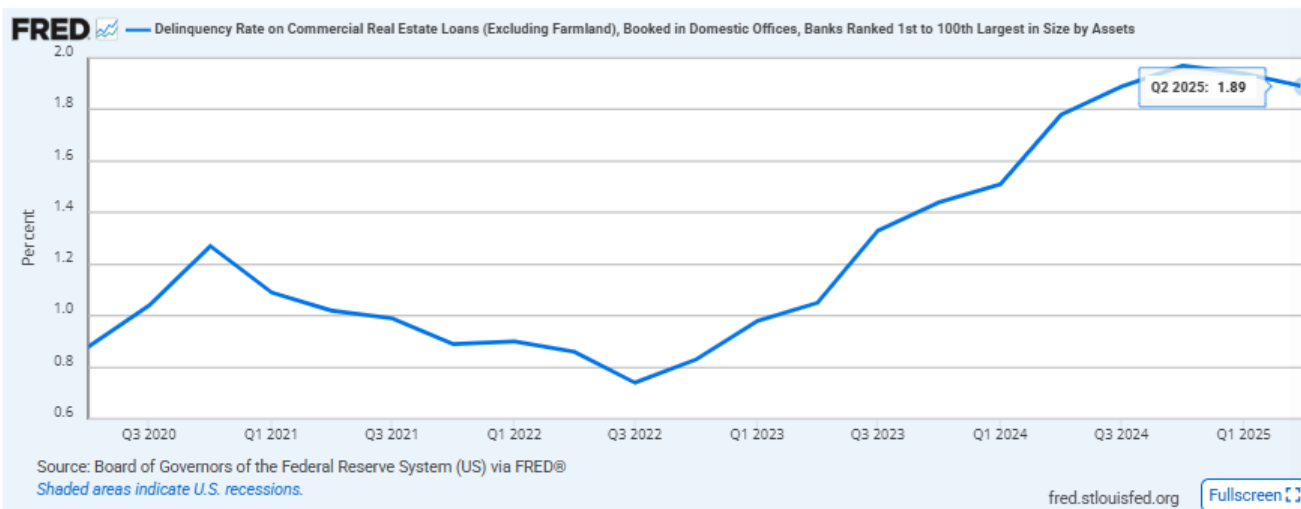


Per Loomis Sayles



Rising CRE Delinquencies vs. Maturity Wall

5-Year Historical Bank CRE Delinquencies



CRED iQ reports a delinquency rate of 8.1%, special servicing at 10.1%, and overall CMBS distress at 10.8% in June 2025. Of matured loans, about 37% are non-performing.

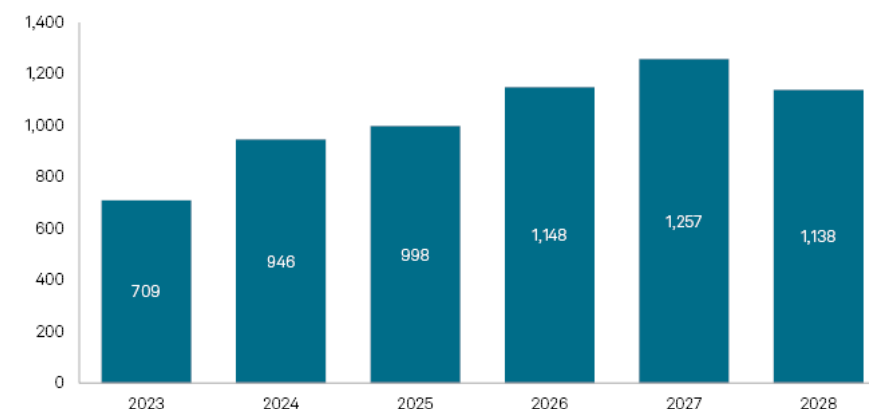


~\$2.4T CRE Maturities in '26 & '27

Maturity Wall Looming

Maturity Data per S&P Global: [Link](#)

Roughly \$950B of US commercial real estate mortgages are estimated to mature in 2024 (\$B)



Data compiled Aug. 19, 2024.

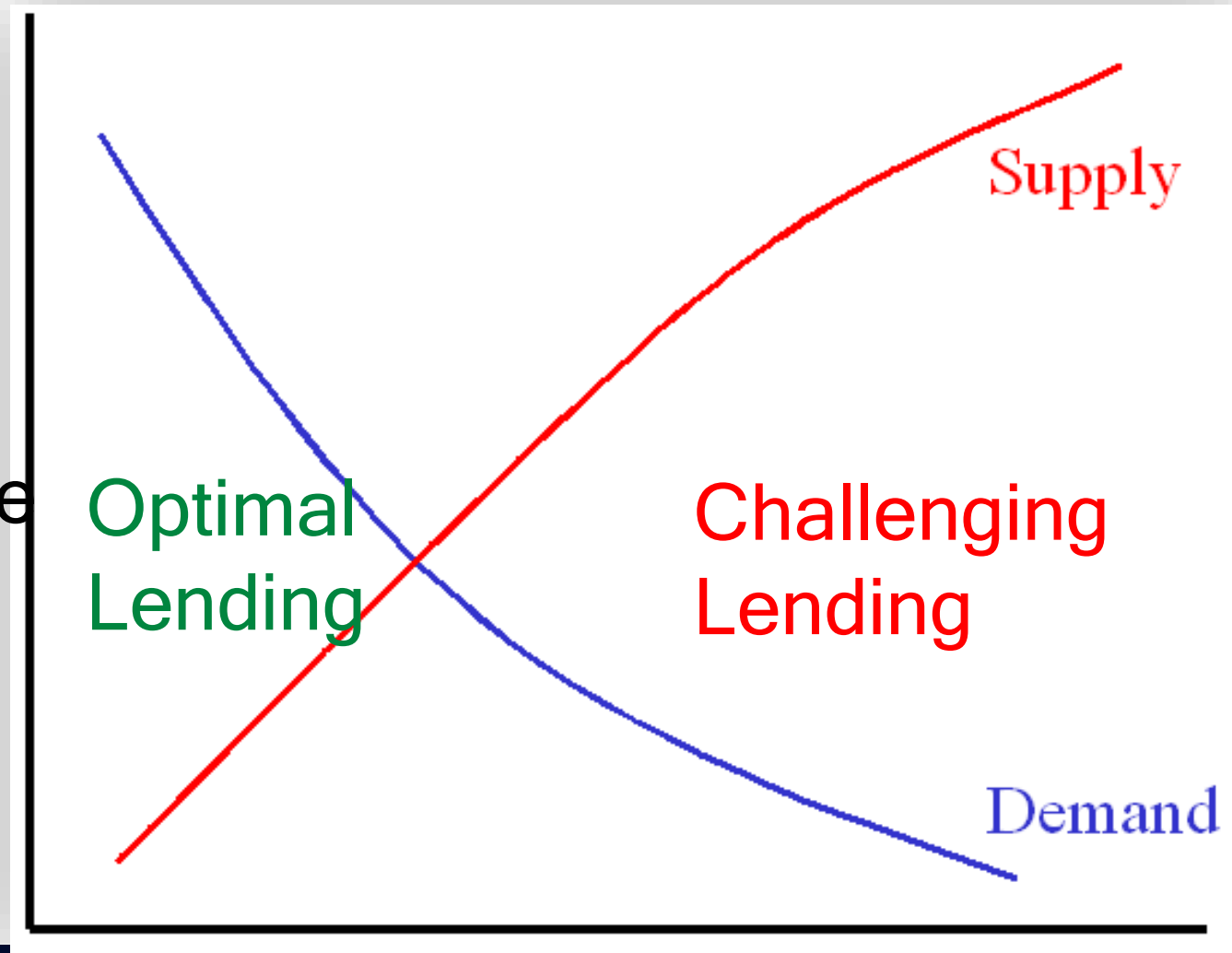
Industry data (e.g., from S&P LCD and Refinitiv LPC) shows a sharp increase in “amend-and-extend” activity in syndicated loan markets throughout 2024-2025, especially for leveraged and commercial real estate loans. In many cases, **over 50% of refinancings this year were structured as modifications rather than full repricings.**



Most Fundamental Metric In CRE – *Whatever The Type*



\$ Value



Units Available



Two halves of the same walnut:

1. One of which we're instinctively familiar: *underwriting the project / borrower for repayment capacity*
2. The other, emerging as equally important: *determining the market's supply and demand dynamic—and related industry.*

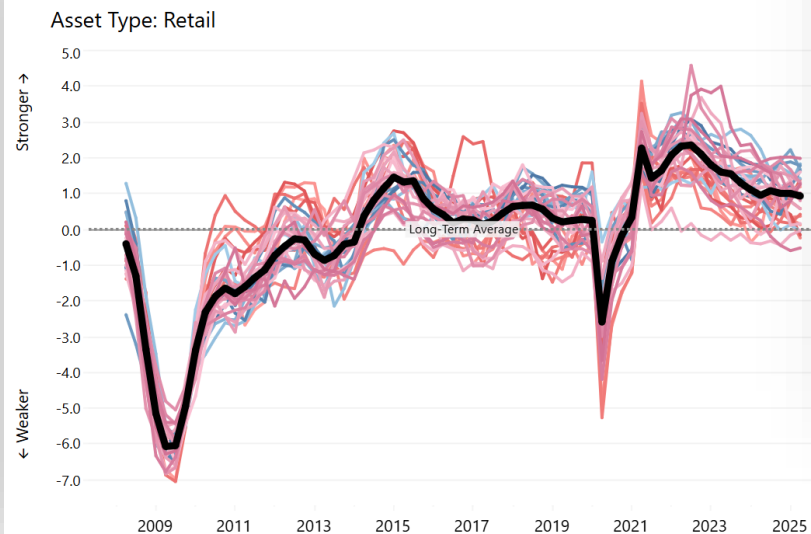
CAVA Retail CRE *(Trends since Q1 '08 / CREMI as of Q2 '25)*



CAVA Retail Composite: +0.91

Commercial Real Estate Market Index

CREMI Scores Over Time: CBSA Multiselect



Source:
ATL Fed
CRE Market Index

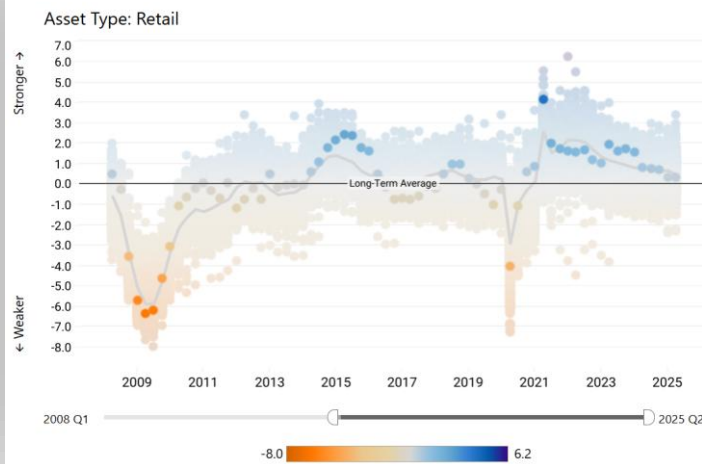


Roanoke, VA: +0.30

Commercial Real Estate Market Index

CREMI Scores Over Time: All CBSAs

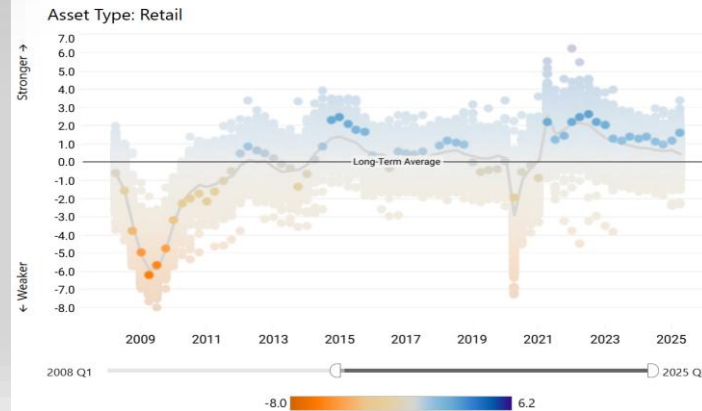
Black Line = Median All CBSA CREMI Scores, Colored Circle = Individual CBSA CREMI Score



Commercial Real Estate Market Index

CREMI Scores Over Time: All CBSAs

Black Line = Median All CBSA CREMI Scores, Colored Circle = Individual CBSA CREMI Score

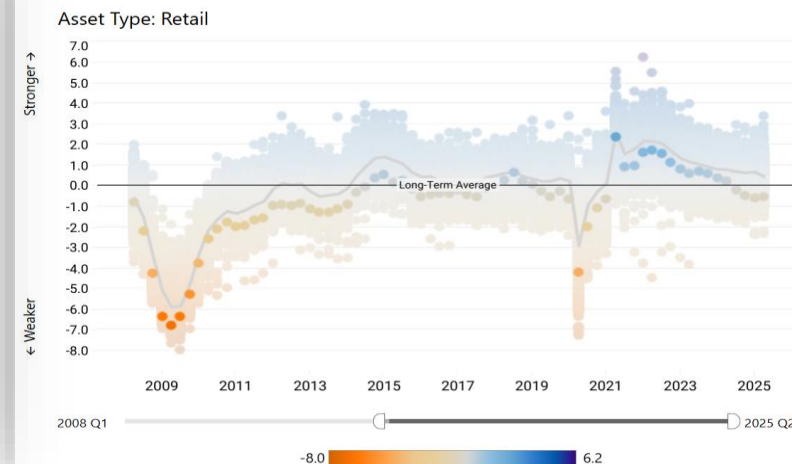


Charlotte, NC: -0.54

Commercial Real Estate Market Index

CREMI Scores Over Time: All CBSAs

Black Line = Median All CBSA CREMI Scores, Colored Circle = Individual CBSA CREMI Score



Florence, SC: +1.61



No more denial...CRE stress is growing!



Less Stress	More Stress
Owner-occupied	Multifamily
Datacenters	Office
Healthcare	Hospitality
Smaller retail	Farmland
	Industrial
	Larger retail
	Specialty RE (e.g. Vinyards)
	1-4 family housing ??

IntelliCredit's perspective per:

- Extensive loan reviews
- M&A due diligences
- 30+ conferences LTM
- Regulatory commentaries
- Expert analyses
- Bond trends
- REIT trends

Estimated: \$800B CRE loans scheduled to mature in '25!

Improving CRE Portfolio Management



- Deepen CRE concentration assessments (to include all material subsets)
- Improve econometric / market data on lending footprint
- Enhance portfolio analytics / MIS data to detect emerging “hotspots”
- Adapt policies / underwriting to sync with conditions
- Anticipate maturities months in advance (for re-pricing impacts)
- Embrace multiple stress test modes
- Expand loan review
- Integrate with strategic and capital plans
- Communicate effectively with both *Boards* and *Management*

Industry Risks are Growing!



Sector / Industry

Restaurants, hospitality, discretionary retail

Housing & construction materials

Automotive, household goods, retail

Telecom, tech, healthcare

Leveraged/junk-rated firms

Private credit-backed emerging sectors

Key Risks & Credit Stress Indicators

Very high SBA default rates; revenue-sensitive

Higher interest rates; rising defaults

Tariff exposure; credit spread spikes

Elevated default risk per industry forecasts

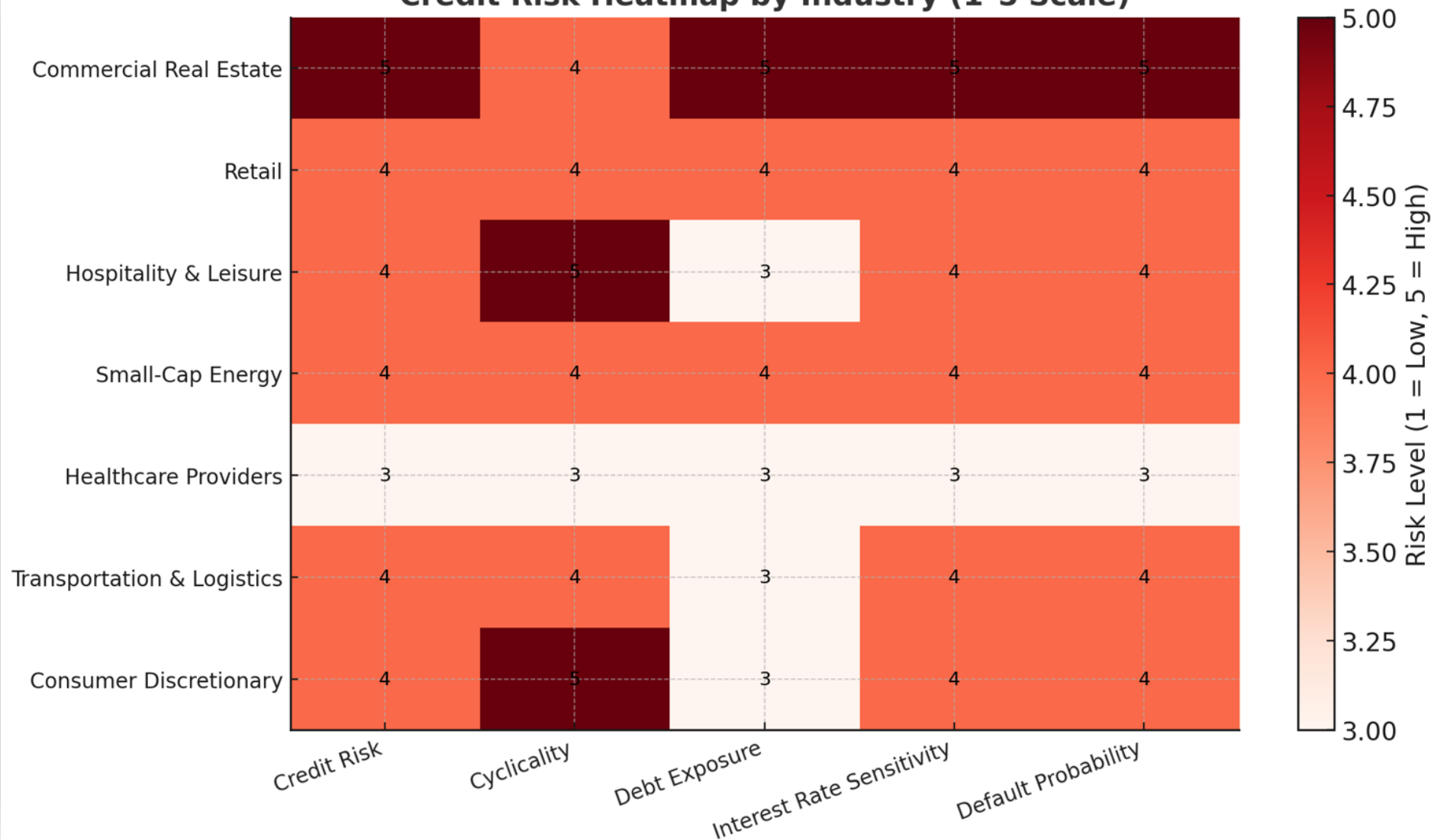
High default probabilities, rising early-warning signals

Risky balance sheets, over-leveraged growth

Industry Risks are Growing!



Credit Risk Heatmap by Industry (1-5 Scale)



--Source:
ChatGPT-informed by
S&P/Moody's data

Optimal Strategies for Managing Heightened Credit Stress:

1. Assess CRE & industry risks
2. Establish contingencies
3. Leverage portfolio analytics
4. Tie stress testing to enhanced loan review
5. Accept credit management is a *long game.*



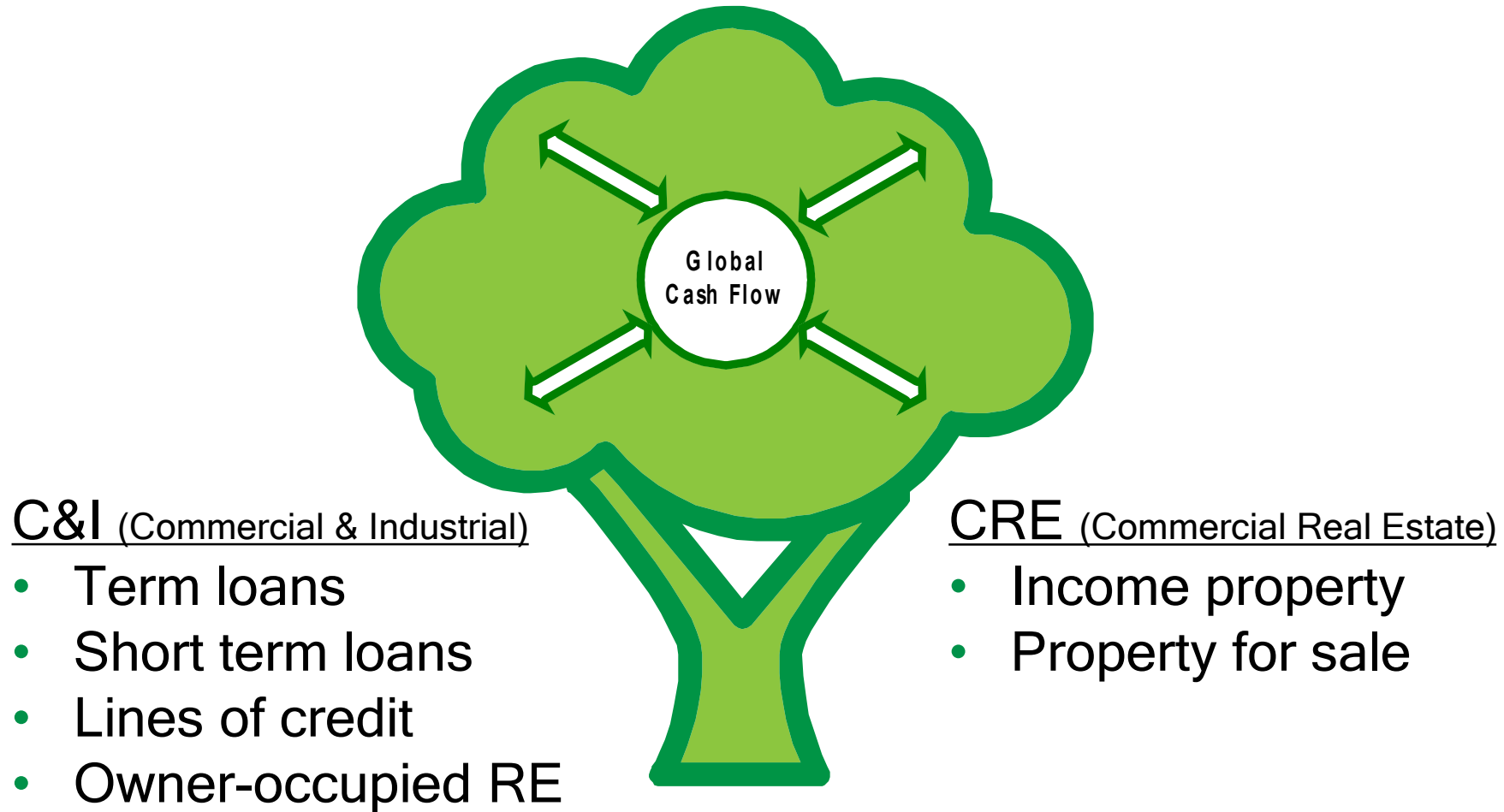
IntelliCredit®



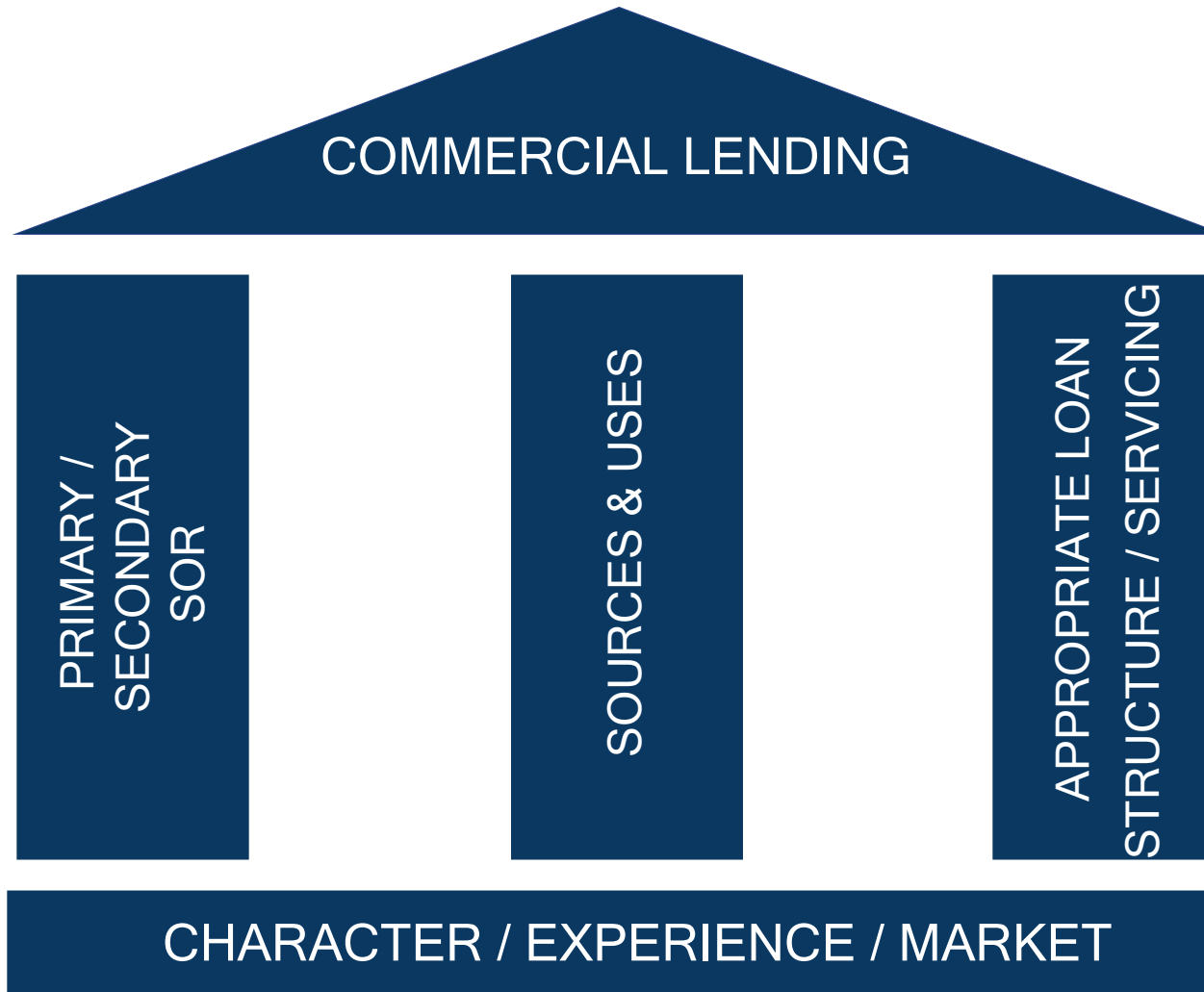
Key CRE (Retail Income Property) Concepts & Case Study



The *Commercial Lending* tree has two branches- underwritten very differently



Key Pillars of Commercial Lending



Real Estate Underwriting Rules of Thumb—*for Bankers*



- The project and builder/developer should be analyzed separately for primary, then secondary support
- ALL components of the borrower's credit relationships must be analyzed
- The loan's complexity and size must be matched by the bank's expertise and time commitment.

Why do a Global Cash Flow?



You Want to Know:

Will operations and investments “outside” of the borrower provide excess cash to help repay your loan?

Or

Will these outside “activities” cash away from your borrower, thus straining repayment ability?



Keys to Analyzing the Project / Borrower's Repayment Capacity ?

Keys to analyze retail income properties



1. Property Cash Flow & Debt Service Coverage

- NOI
- DSCR
- Occupancy

2. Tenant Quality & Lease Terms

- Tenant creditworthiness
- Lease structure & duration

3. Location & Market Fundamentals

- Demographics, visibility, & foot/traffic patterns
- Competition & vacancy trends

4. Loan & Capital Structure

- LTV
- Rate & amortization
- Reserves / contingencies

5. Property Condition & Characteristics

- Age & condition
- Layout / adaptability
- Environmental / structural issues

6. Borrower / Guarantor Strength & Experience

- Track record
- Financial condition
- Management plan

7. Exit Strategy & Market Liquidity

- Capacity to re-finance or sell
- Market liquidity

Regulatory Loan-to-Value (LTV) Limits



Raw land	65%
Land development	75%
Construction:	
- <i>Commercial, multifamily, other nonresidential</i>	80%
- <i>1- to 4-family residential</i>	85%
Improved commercial property	85%

Regulatory Loan-to-Cost Limits (%)



Type	Purchase LTV/LTC	Build LTV/LTC	Refinance LTV/LTC
Raw Land	65/65	N/A	65/X
Improved Land	75/75	75/100	75/X
Commercial Construction	N/A	80/100	80/X
Commercial Permanent	85/85	N/A	85/X
1-4 Family Construction	N/A	85/100	85/X
1-4 Family Permanent	<90/<90	N/A	<90/X

Regulatory LTV limits / regs / guidance



- **Do not apply for:**
 - Loans with government guaranty
 - Loans to be sold promptly w/o recourse to Bank
- **All loans exceeding LTV limits must be formally reported to Board of Directors**
- **Other CRE Hot buttons:**
 - 300% (CRE) /100% (CA&D) 2005 guidance

Types of RE valuations



- **Appraisal**
 - performed by State Certified Appraiser or higher
 - strict federal content guidelines
- **Evaluation**
 - usually performed by Bank
 - bank decides criteria -- “satisfy principles of safe and sound banking.”
 - tax value, broker’s opinion, etc.

Appraisal “approach” options



- *Sales* - Based on recent sales of comparable or “comp” properties.
- *Cost* - Current cost to construct/duplicate less any existing depreciation.
- *Income* - Current value of future income
 - Recurring Income: capitalization
 - Development: Discounted Cash Flow

When Appraisal is required



>\$250M for “real estate related transactions” except

- Abundance of caution
- Business purpose (not RE dependent) secured by RE (up to \$1MM)
 - OOCRE, Farmland, Timber
- Renewal
 - no cash out
 - no change in property or market

General RE Valuation Issues



<u>Property Type</u>	<u>Valuation Driver</u>
Existing SF Residence	Comp Sales
Proposed SF Residence	a) Comp Sales b) Cost
Investment RE	a) NOI - Lease Rates, b) Cap Rate
Hotel	a) NOI - ADR, Exp mgmt b) Cap rate
Residential S/D	Absorption rate
Religious Org-Sanctuary	Cost

Existing vs Proposed Improvements



- **For Existing**

Valuation = “As Is”

- **For Proposed**

Valuation =

“As Is” and

“As Built,” or “As Improved”

Loan-to-Value Ratio (Developments)



$$\frac{\text{Loan Amount}}{\text{Appraised Value of Project}} = ? \%$$

Retail:

$$\frac{\$450,000}{\$800,000} = 56\%^*$$

Wholesale:

$$\frac{\$450,000}{\$600,000} = 75\%^{**}$$

*With imputed value of improvements and profits

**As is (in bulk)

Loan-to-Value Ratio (With Junior Liens)



$$\frac{\text{Loan Amount}}{\text{Appraised Value of Project}} = ? \%$$

Combined LTV:

$$\frac{\$540,000 \text{ (1st Lien)} + \$100,000^*}{\$800,000} = 80\%$$

More Liberal:

$$\frac{\$540,000 \text{ (1st Lien)}}{\$800,000} = 67.5\% \quad \$260,000 \text{ (Equity)} \times 80\% = \$208,000^*$$

*Proposed 2nd Lien Loan

Leases



Leases represent the market acceptance of the project. Determine:

- Term of the lease(s)
- Market vs. stated rents
- Obligations of the lessor / lessee
 - Inducements to sign up
 - “Triple Net” Leases
- Assignability of the lease
- If the lessee is a *credit tenant*.

Types of CRE Leases (*Gross or Full-Service Lease*)



- Typically means the rental rate of the property includes all operating expenses associated with the property such as janitorial services, property maintenance, utilities, and property taxes. This is the simplest form of a commercial lease and is most common in multi-tenant office properties catering to smaller businesses (1-15 person businesses).
- While a Gross Lease has the vast majority of operating expenses included in monthly rent, the language within the lease typically states the landlord has the right to pass down to the tenants any future increases in those expenses on a pro rata basis. For example, if during the summer months a building incurs more air conditioning/electrical expense than was estimated, the tenants will receive a bill.

Types of CRE Leases (*Net Lease*)



- The landlord charges a lower base rent for the commercial space, plus some or all of "usual costs," which are expenses associated with the operation, maintenance, and use of the property that the landlord pays. These can include real estate taxes; property insurance; and common area maintenance items (CAMS). CAMS include janitorial services, property management fees, sewer, water, trash collection, landscaping, parking lots, fire sprinklers, and expenses associated with commonly shared areas or services.
- There are several types of Net Leases:

Types of CRE Leases (*Net Leases—Single Net*)



- The tenant pays base rent plus a pro-rata share of the building's property tax (meaning a portion of the total bill based on the proportion of total building space leased by the tenant). The tenant also pays utilities and janitorial services. The landlord covers all other building expenses.

Types of CRE Leases (*Net Leases–Double Net*)



- The tenant is responsible for base rent plus a pro-rata share of property taxes and property insurance. The landlord covers expenses for structural repairs and common area maintenance. The tenant once again is responsible for their own janitorial and utility expenses.

Types of CRE Leases (*Net Leases—Triple Net*)



- (NNN Lease) - This is the most popular type of Net Lease for commercial freestanding buildings and retail space. In this lease, the tenant pays all or part of the three "nets"--property taxes, insurance, and CAMS--on top of a base monthly rent. Common area utilities and operating expenses are usually lumped in as well; for example, the cost for staffing a lobby attendant would be part of the NNN fees. The tenants also pay the costs of their own occupancy, including janitorial services, utilities, and their own insurance and taxes. Typically, landlords estimate the amount of the expenses to be covered and charge tenants a portion of the expenses based on the proportion of total building space they lease.
- When reviewing a NNN Lease, bankers should maintain an awareness that such leases tend to be more landlord-friendly. The fees included and the caps on the amounts those fees can be increased by annually should be carefully reviewed. Additionally, an awareness should be maintained that NNN Leases can fluctuate from month to month and year to year as operating expenses increase or decrease, making a tenant's expense forecasting tricky.
- While NNN Leases are more landlord-friendly, there are tenant benefits. Transparency is one as tenants can see business operating expenses in relation to what they are charged. Cost savings in operating expenses are passed on to the tenant rather to the landlord. In addition, the monthly rent in a NNN Lease is potentially lower than in a Gross Lease, as tenants have a higher level of responsibility for the building.

Types of CRE Leases (*Net Leases–Absolute Triple Net*)

- This is a less common option that is more rigid and binding than the NNN Lease, where tenants carry every imaginable real estate risk, for example, being responsible for construction expenses to rebuild after a catastrophe, or for continuing to pay rent even after the building has been condemned. Aptly called the "hell-or-high-water lease," tenants have ultimate responsibility for the building no matter what.

Types of CRE Leases *(Modified Gross or Net, Industrial Gross)*

- As the Gross Lease tends to be more tenant-friendly and the Net Lease tends to be more landlord-friendly, there exists a compromise lease for the convenience of both parties. The Modified Gross Lease is similar to a Gross Lease in that the rent is paid in one lump sum, which can include any or all of the "nets"--property taxes, insurance, and CAMS. Utilities and janitorial services are typically excluded from the rent and are covered by the tenant. Tenants and landlords negotiate which "nets" are included in the base rental rate.
- The Modified Gross Lease is more popular with tenants, because its flexibility translates into an easier agreement between tenant and landlord. Unlike the NNN Lease, if insurance, taxes or CAM charges increase, the lease rate does not change. Of course, if those expenses decrease, the cost savings is passed on to the landlord. As janitorial service and utilities are typically not covered, tenants can better control how much they spend compared to a Gross Lease.
- This type of lease is most common with industrial or warehouse space. In most cases, tenants of industrial properties will have a Gross Lease that has been modified so some of the expense categories (usually electrical) will be charged in addition to monthly rent. All other property expenses are included in the regular monthly rent.

Types of CRE Leases (*Percentage*)



- This is technically not a separate type of lease because the manner in which expenses are paid fall within one of the preceding categories. However, this type of lease is included here as the manner in which the amount of lease payments is determined is unique. In this type of lease, the tenant is responsible for paying base rent on the property, as well as a monthly percentage of revenue earned from the business occupying the rented space. These leases are most often used in retail spaces, specifically malls.

Cash Flow Analysis - General



Operating Company Cash Flow	CRE Cash Flow
Sales	PGI (Potential Gross Income)
- COGS	- Vacancy & Collection Loss
= Gross Profit	= EGI (Effective Gross Income)
- Operating Expenses	- Operating Expenses
= Operating Profit	= NOI (Net Operating Income) 
- Other Expenses (Interest)	- Leasing Commissions & T.I.'s
= Net Income	- Replacement Reserves
	= Cash Flow Avail. for Debt Service
For Debt Service Coverage:	For Debt Service Coverage:
<u>Net Income + (Dep., Int., Amort., Etc.)</u>	<u>Cash Flow Available for Debt Service</u>
Annual Debt Service	Annual Debt Service

Major determinant of value



Income Property Valuation: Net Operating Income (NOI)



Gross Rents	\$128,000
5% vacancy	- 6,400
Effective Gross Income	121,600
30% Operating expenses	- 36,600
Net Operating Income (NOI)	85,000
Annual debt service	<u>- 68,200</u>
Net Cash Flow	\$ 16,800

Income Property: Debt Service Coverage (DSC)



Amount of debt—agnostic to Cap Rate value!

Net Operating Income (NOI)	\$85,000
	÷
Annual Debt Service	\$68,200
Debt Service Coverage	1.25X

Value by Capitalization Rate (Cap Rate)



A short-cut of the *income approach* used in appraisals is valuation by cap rate:

$$\text{Value / selling price of property} = \frac{\text{Net Operating Income}}{\text{Capitalization Rate (\%)}}$$

Examples:

$$1. \quad \$850,000 = \frac{\$85,000}{10\%}$$

$$2. \quad \$653,846 = \frac{\$85,000}{13\%}$$

Income Property Value: *Capitalization Rate*



- Applies to any income generating asset
- A theoretical figure defined as:

“A rate of return that a ‘reasonable’ investor would expect/demand if they were buying an asset of similar size, type, etc.”

- The number one item you pay an appraiser to determine for you!

Direct Capitalization vs. Discounted Cash Flow



- Direct Capitalization:

A single year's income is divided by an income rate to reach an indication of value and yield capitalization; it reflects the return *on* and the return *of* investment. It's a simpler, more one-dimensional approach— a short-hand version of DCS below.

- Discounted Cash Flow:

Future benefits are converted into a value by discounting them at an appropriate yield rate that reflects projected changes in income, value and yield; the distinction between return *on* and return *of* capital is explicit.

Discounted Cash Flow Analysis



	<u>2012</u>	<u>2013</u>	<u>2014</u>
<i>Gross Rents</i>	\$72,500	\$74,800	\$79,650
<i>Oper. Expenses</i>	12,350	13,500	16,800
<i>NOI</i>	<u>60,150</u>	<u>61,300</u>	<u>62,850</u>

Present Value of Income @13% Discount Rate

60,150 X 0.884956 = \$ 53,230

61,300 X 0.783147 = \$ 48,007

62,850 X 0.693050 = \$ 43,558

= \$144,795

Present Value of Net Resale @ 13% (in 2014)

\$485,000 (Projected Resale \$) X 0.693050 = \$336,129

Total Present Value \$480,924

Which method is best?



- *Direct capitalization* assumes everything about one year is frozen in time.
- *DCF* requires that various assumptions be made about the future when the future is unknown

What are examples of where one or the other should best be used?

Which method is best? *Direct Capitalization* or *DCF*?



<u><i>Project Type</i></u>	<u><i>Best Method</i></u>
Apartments with stable rents (5 year loan)	Direct
Apartments with fluctuating rents dependent on projections	DCF
Warehouse with long term tenants at stable market conditions	Direct
Shopping center with defined recapture strategy	DCF

Debt Yield Analysis



$$\text{DEBT YIELD} = \frac{\text{Net Operating Income}}{\text{Loan Amount}}$$

$$\text{Debt Yield (18.9\%)} = \frac{\$85,000 \text{ (NOI)}}{\$450,000 \text{ (Loan Amount)}}$$

Key attributes

- Focuses on debt vs. value (how long to get out of a loan)
- Inverse of CAP rate: *greater %* is better

Example:

$$100 \div 18.9 = 5.29 \text{ Years}$$

$$100 \div 10 = 10 \text{ Years}$$

- Unlike DSC: not susceptible to interest rate swings.

How to Perform Income Property Repayment Analysis



Income Property NOI Calculator

Revenues			
	Size (Sq Ft)	Rate	
Grocery	35,000	\$ 8.00	\$ 280,000.00
Subway	8,000	\$ 10.00	\$ 80,000.00
Locals	15,000	\$ 12.00	\$ 180,000.00
Gross Income			\$ 540,000.00
Less Vacancy (15% of local space)	15.00%		\$ 27,000.00
Effective Gross Income			\$ 513,000.00
Expenses			
Advertising			\$ 5,000.00
Cleaning and maintenance			\$ 16,200.00
Depreciation*			\$ 15,000.00
Legal and other professional			\$ 20,000.00
Insurance			\$ 3,000.00
Interest*			\$ 17,000.00
Management			\$ 19,000.00
Repairs			\$ 21,000.00
Supplies			\$ 11,000.00
RE Taxes			\$ 5,400.00
Utilities			\$ 10,400.00
Total Expenses			\$ 143,000.00
NOI (Net Operating Income)			
*(Effective Gross Income-Total Expenses+Depreciation+Interest)			\$ 402,000.00

Income Property Loan Analysis Calculator

Step	Inputs	Outputs
1. NOI	\$ 402,000	
2. Property Value (NOI/Cap Rate)	Cap Rate 10.00%	\$ 4,020,000
3. Annual DSC by NOI (NOI/DSC)	DSC Ratio 1.30	\$ 309,231
4. Optimum Loan Amount (\$DSC/Cap Rate)		\$ 3,092,308
5. Debt Yield (NOI/Optimum Loan Amount)		13.00%
Years to Pay-off (1.00/Debt Yield)		7.69

Calculate a NOI based on the following



- **Adjusted Gross Revenue (factoring in vacancy): \$800,009.80**
- **Operating Expenses**
 - Advertising: \$6,500
 - Maintenance: \$18,500
 - Depreciation: \$22,000
 - Legal & Professional: \$26,000
 - Insurance: \$12,000
 - Interest: \$23,500
 - Management: \$25,000
 - Repairs: \$28,000
 - Supplies: \$21,500
 - RE Taxes: \$15,500
 - Utilities: \$19,000

Assuming the NOI, calculate the following



- **Property Value (at 10% Cap Rate)**
 - $\text{NOI} \div \text{Cap Rate}$
- **Annual Debt Service Coverage (DSC) (at 1.30 DSC)**
 - $\text{NOI} \div \text{DSC}$
- **Optimum Loan Principal Amount**
 - $\text{\$DSC} \div \text{Cap Rate}$
- **Debt Yield**
 - $\text{NOI} \div \text{Optimum Loan Amount}$

Common (but Bad) ideas to make the deal “work” for Income Property

- Amortization schedule > useful (non-renovated) life of property
- Accepting “fake” equity in RE as “real.”
- Presuming individual strength without analysis
- Accepting unrealistic Lease Projections
 - New Property - better than market terms
 - Existing Property - new owner can do better than previous (better than market)

Other key metrics often used (often from investors' perspectives)

- **Internal Rate of Return (IRR)**

Used to measure a project's profitability. This metric accounts for initial investment costs, cash flow, and property sale proceeds. The higher the IRR, the more attractive the project.

- **Cash-on-Cash Return (CCR)**

...or cash yield, is a common metric in the commercial real estate industry. The rate of return measures the annual pre-tax cash flow divided by the total cash invested. This figure measures the investment's performance.

- **Gross Rent Multiplier (GRM)**

For an easy assessment tool to compare properties, the gross rent multiplier metric can help narrow down the best opportunities. To calculate this, divide the property's price by its potential gross annual income. If a property is listed for \$500,000 and carries an annual income of \$100,000, then the GRM is 5. GRM works best when ranking similar properties in relatively close proximity. Note that it does not factor operating expenses, market fluctuations, or loan amortization.

- **Operating Expense Ratio (OER)**

Add the day-to-day operating expenses-insurance, landscaping, maintenance, utilities, taxes, management fees, et al.-but not any mortgage repayments or capital improvements. Then, divide the total operating expenses by your potential rental income. Essentially, the lower the OER, the more profitable the property.

Stress Testing



- **Current/accurate data dependent**
 - Rent rolls
 - NOI
 - Independent market trends & valuations (REIS / CoStar)
- **Loanable amount**
- **Break-even analysis**
- **Stress scenarios**
 - LTV
 - NOI
 - Cap Rate
 - DSC

Closing Thoughts

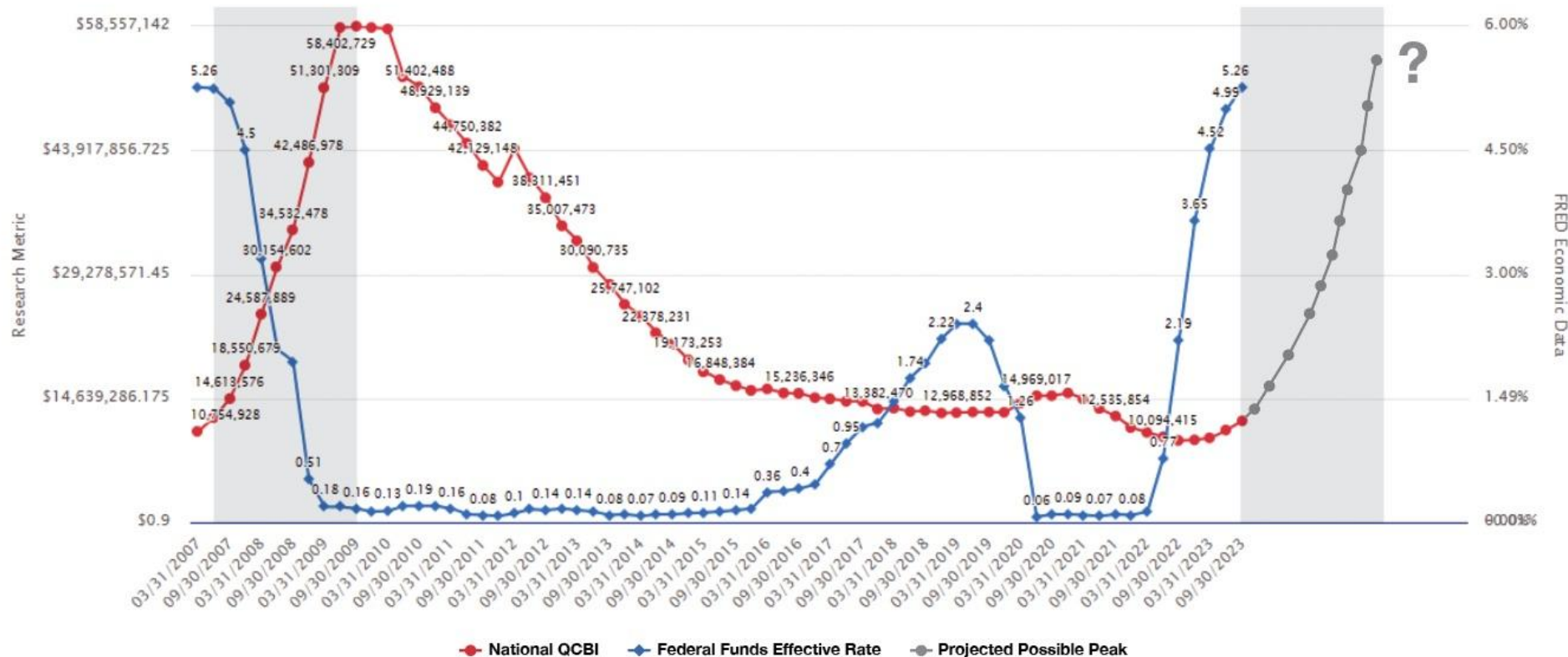


Not so soon (celebrating rate peaks)....



History Shows Non-Performing Loans

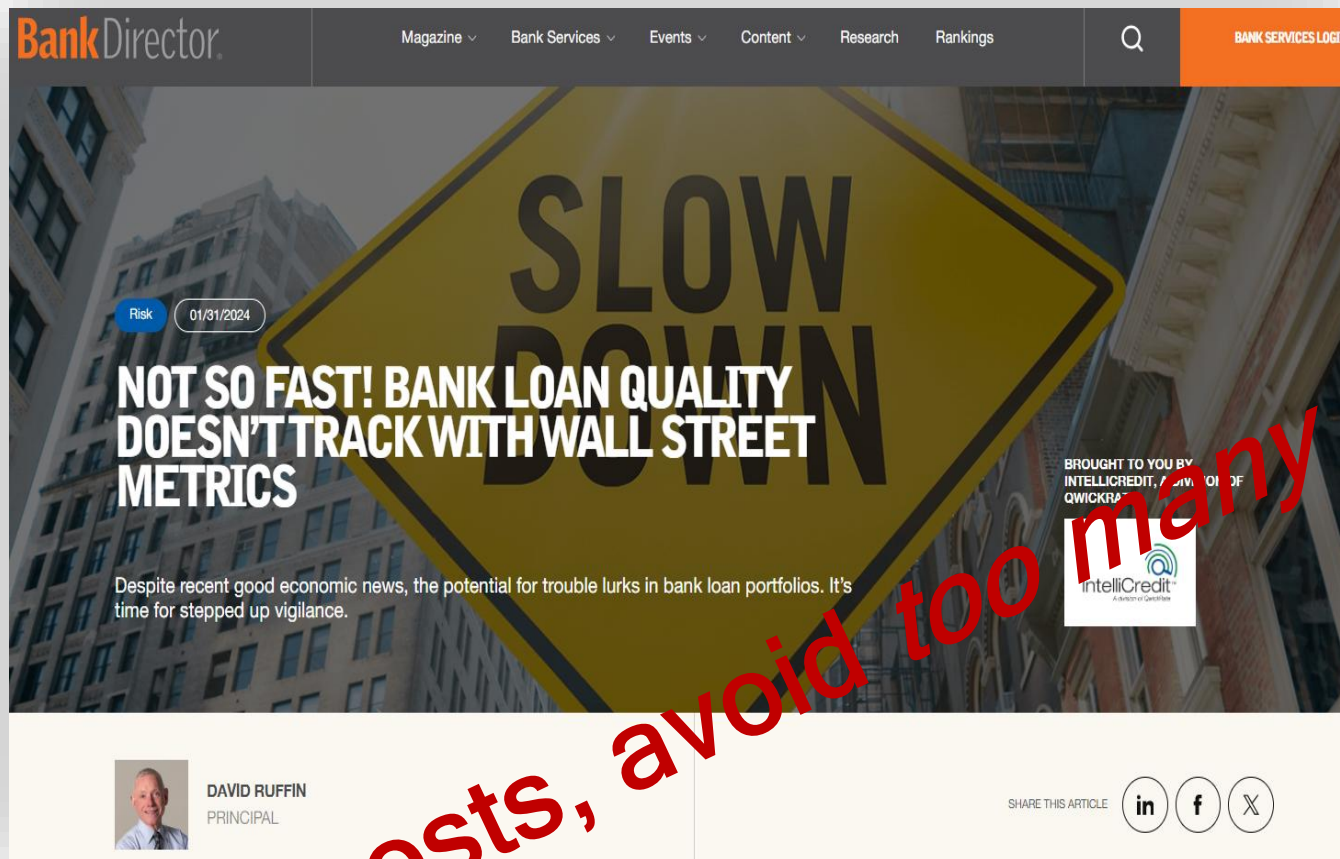
Peak Two Years After Fed Rate Cuts



QwickAnalytics®

QCBI:
Banks $\leq$ \$10B
in Assets

In conclusion



<https://www.bankdirector.com/article/not-so-fast-bank-loan-quality-doesnt-track-with-wall-street-metrics/>



The Good:

- Reserves & capital cushions
- Some risk has left our space
- Overall job market resilience
- Inflation abating
- Rates appear paused

The Bad:

- Smaller banks' CRE exposure
- Trailing NPL effects
- Segments of consumers struggling

The Now:

- Heightened regulatory scrutiny
- New focus on more robust
 - loan reviews
 - stress testing
 - portfolio analytics





Please Reach Out for any
Credit Portfolio Review Needs.
Also, Deeply Experienced in M&A / Re-Caps.

Real-time combo:

Loan Review / Portfolio Analytics / Loan-level Stress Testing



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Q & A