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THE WEEKLY UPDATE ON REAL ESTATE FINANCE AND SECURITIZATION

Small-Balance Lenders Hang On

Swept up in the market turmoil along with everyone else, small-balance lenders are hunkering down and waiting for conditions to improve.

Programs that originate small-balance commercial mortgages have substantially reduced their origination goals for this year. For example, **KeyBank's** program, which originally planned to write $1.5 billion of mortgages, has cut that target in half.

Small-balance commercial mortgages were particularly hard-hit by the subprime meltdown. Because borrowers are often owners of mom-and-pop businesses, and loans typically are the size of mortgages on large homes, the sector is closely tied to the performance of the housing market.

Still, players like Key and **Principal Real Estate Investors** remain committed to the sector.

"This is a good space to go into," said Key managing director **Charles Krawitz.** "It's a very sturdy marketplace. You have a plethora of very, very conservative owners who don't want to get in over their heads with leverage."

Krawitz, who joined Key last summer to beef up its small-balance lending operation, said the unit has accumulated enough loans to launch a commercial MBS offering. If the securitization market doesn't improve, Key will sell the mortgages to other banks as whole loans.

The small-balance sector has traditionally been highly fragmented, with relatively small commercial banks accounting for the bulk of originations. But securitization shops and other larger players have moved in over the past couple of years.

The origination of small-balance loans — generally defined as ranging in size up to $5 million — declined in the second half of last year after several years of steady growth. Third-quarter volume was $31.3 billion, down 14.7% from a year earlier and down 8.3% from the previous quarter, according to **Randy Fuchs,** a principal of analytics firm **Boxwood Means.** Though fourth-quarter numbers are not yet available,

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FEBRUARY 8, 2008

2 Small-Balance Lenders Hang On
3 DekaBank to Step Up US Lending
3 Risk Cited for Maturing 5-Year Loans
3 S&P: CMBS Delinquencies to Rise
4 Apollo Taps Prudential, Barclays
7 REIT Lines Up Freddie Facility
8 Seminary Project Gets Helaba Loan
9 Witkoff Seeks Funding for Project
10 Mortgages Gained 5.6% Last Year

THE GRAPEVINE

Canadian lender **Colliers International** has pulled the plug on its conduit after barely three years of operation. Securitization chief **Ross Brennan** will oversee the sale of C$200 million ($198 million) of warehoused loans. The unit's other 14 staffers were laid off late last month. The Colliers conduit shop was a small but steady contributor to Canadian conduit deals, supplying a total of C$545 million of mortgages. The CMBS market downturn has already claimed two other Canadian casualties. The conduit units of **Capmark** and **Credit Suisse** closed late last year.

Prudential Financial this week became the latest player to disclose losses in its commercial MBS operation. The insurer, which securitized $3.6 billion of commercial mortgages last year, took a $49 million CMBS loss in the fourth quarter. Overall, the company reported $871 million of quarterly net income, down 16% from a year earlier.

Brian Schwartz, who invested in CMBS for **Sailfish Capital Partners** of Stamford,

See GRAPEVINE on Back Page

Weak Market Prompts Wells to Exit TOP Deal

Citing poor market conditions, **Wells Fargo** has pulled its loans from the latest "TOP" brand securitization.

Wells originally planned to contribute about $200 million of fixed-rate mortgages to the transaction. Now its longtime TOP partners — **Morgan Stanley, Bear Stearns** and **Principal Commercial** — will proceed with a scaled-down $1.2 billion deal. The offering, which is the 29th in the TOP series, hit the market this week and is on track to price next week, which would make it the first transaction of the year.

Wells emphasized that it remains committed to the long-running TOP program and will participate in future deals when conditions improve. However, it decided that it made no sense to securitize loans at a time when CMBS spreads are at record highs. "We didn't feel there was any urgency to sell good loans with spreads blown out at these levels," said senior managing director **Adam Davis,** who heads the

See TOP on Page 7

Shorting on CMBX Drives Up Cash Spreads

Commercial MBS investors watched in despair this week as fast-money players flooded the synthetic market, pushing CMBS spreads out to stratospheric levels.

The trading was mostly in the CMBX, an index that permits investors to take long or short positions in synthetic instruments tied to pools of CMBS deals. The heaviest demand was on the short side. Investors betting that the market will fall sought to buy protection against CMBS losses, driving up both CMBX and CMBS spreads.

A small number of cash bonds were offered in the secondary market. Late in the week, for example, an investor offered to pay 210 bp over swaps for a batch of 10-year, super-senior notes floated last year. It was unclear if the seller accepted the offer. But spreads clearly were dramatically wider from the previous week, when they fluctuated between 140 bp and a then-record 175 bp.

Trading was so thin on the cash side this week that some investors were hesitant to conclude that any new benchmarks had been set. "This market is so schizophrenic

See SPREADS on Page 6

Taubman Taps Syndicates to Refinance Malls

Taubman Realty, which in the past often relied on securitized mortgages, has turned to portfolio lenders to refinance two big malls.

Eurohypo landed the mandates to lead $575 million of floating-rate loans for the mall operator and its partners. Eurohypo has agreed to lend about $250 million on Fair Oaks Mall in Fairfax, Va., with **Calyon** and **PB Capital** expected to be brought in as co-lead arrangers. In addition, a Eurohypo syndicate has already closed on a $325 million mortgage backed by International Plaza mall in Tampa.

Both properties previously had securitized mortgages. But when Taubman marketed the new assignments, no securitization programs stepped up. Commercial banks, both domestic and foreign, dominated the bidding.

"Wall Street is just a big wreck in the road," said a lender at a foreign commercial bank. "Everybody's just steering around it and getting on with their business."

Both of the new loans carry three-year terms, with conditional options for

See TAUBMAN on Page 9

Fuchs projected that activity fell again, probably to between $25 billion and $28 billion.

The weak market has already caused some small-balance lenders to pull out of the market. **CBA Commercial,** which was launched in 2004 by boutique merchant bank **Cheslock Bakker & Associates,** went out of business late in October after a last-minute bid to line up equity fell apart.

Impac Commercial Mortgage and **Greenpoint Mortgage** are also out of the sector. ❖