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THE WEEKLY UPDATE ON REAL ESTATE FINANCE AND SECURITIZATION

Key Scraps Small-Balance Program

KeyBank is shutting down a securitization program that specialized in small-balance loans, a niche once seen as the next frontier for commercial MBS.

The Cleveland bank launched its Key Commercial Mortgage Access program in 2005 and securitized its first batch of small-balance loans in a $237.5 million deal that priced in 2007 (Key Commercial Mortgage Securities Trust, 2007-SL1). Going into 2008, Key was hoping to originate $1.5 billion of small-balance loans for securitization. But then the CMBS market collapsed, and the 2007 issue turned out to be the bank's lone deal under the program.

With no U.S. CMBS deals having priced since mid-2008, Key recently decided to shutter the small-balance-loan operation as part of a broader effort to reduce exposure to commercial real estate. The bank laid off a half-dozen staffers in its CMBS program, most of whom left this week. Managing director **Charles Krawitz,** a former **LaSalle Bank** executive hired by Key in 2007 to expand the small-balance program, will stay on to close pending loans.

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APRIL 3, 2009

Treasury Plan Seen Spurring CMBS Sales

Veteran commercial MBS investors think there's a reasonable chance that the **U.S. Treasury Department's** new toxic-assets program will drive up prices enough to encourage institutions to unload their holdings of super-senior CMBS.

However, most observers feel the prospects are much less certain for the portion of the program aimed at spurring sales of distressed commercial mortgages.

While many of the program's details haven't been released, Wall Street analysts have started crunching numbers based on assumptions about the financing terms likely to be offered by the government. The consensus is that the Treasury Department will offer loan rates that will enable buyers of super-senior CMBS to achieve at least a 15% leveraged return. That yield, in turn, would work out to spreads of roughly 500-600 bp over swaps for super-senior bonds, according to some estimates.

If those guesses prove correct, the CMBS market is in line for a major rally. Spreads

See TREASURY on Page 10

Babson Seeks $3 Billion for Mortgage Fund

Babson Capital Management is seeking to raise $3 billion of equity for a fund that would originate plain-vanilla mortgages.

Babson, a real estate unit of **Massachusetts Mutual,** hopes to hold a first equity close this summer. That's an aggressive timeline, given the recent pullback by institutional investors. However, the firm is evidently banking that its relatively conservative strategy will appeal to investors looking to exploit the hole in the lending market left by the demise of securitization programs.

Investors said Babson has taken several steps to spur interest, including a reduced fee structure, a catch-up provision that is relatively favorable to limited partners and the participation of Mass Mutual as a co-investor.

The vehicle, Babson Capital Core Mortgage Fund 1, would underwrite senior mortgages according to insurance-company standards. It would target floating-rate loans with terms of 3-7 years and loan-to-value ratios of 65% or less. Coupons

See BABSON on Page 9

After Testing Market, RBC Pulls Portfolio

After selectively shopping a $740 million package of commercial mortgages, **RBC Capital** has formally pulled the offering — although some market players think the lender remains willing to sell at the right price.

The largest loan in the package was a $210 million fixed-rate mortgage on the Lipstick Building in Midtown Manhattan. RBC originated the loan in the summer of 2007, near the peak of the real estate market. It was subsequently unable to securitize the mortgage when the commercial MBS market seized up.

RBC began testing the interest in the portfolio late last year. It talked with selected brokers and provided details about the loans, with the idea of having them shopped quietly. But soon word started to leak out. That spooked RBC, which didn't want to appear to be dumping the loans. It feared that impression would further depress prices in an already-thin sales market.

RBC pulled the portfolio from the market in recent weeks and told investors

See RBC on Page 13

THE GRAPEVINE

John Ho, who built **Merrill Lynch's** Canadian conduit into the market leader, left the firm last week. Ho, a managing director, was reassigned last year to the U.S. securities-lending operation after spending a decade running the Canadian shop. Market players said Ho left to launch an operation that will acquire debt in Canada, the U.S. and South America. Prior to the collapse of the commercial MBS market, Merrill's Toronto-based conduit was the leading CMBS loan originator in Canada.

Former **Madison Realty Capital** principal **Mark Bahiri** has started **Emerald Creek Capital** in New York. The firm, which opened in March, provides short-term loans for up to $20 million, as well as asset-management services for wealthy individuals. Bahiri left New York-based Madison earlier this year. He brought two

See GRAPEVINE on Back Page

The bank's pullback reflects waning confidence that the CMBS market will revive anytime soon. But small-balance lending, involving mortgages of up to $10 million, has held up relatively well among portfolio lenders during the credit crisis. In the third quarter of 2008, U.S. lenders wrote a combined $33.5 billion of small-balance loans, a 6.4% increase from the third quarter of 2007, according to analytics firm **Boxwood Means.**

"There's a lot of opportunity in the small-balance space," Krawitz said. "The space has held up relatively well. You don't have values falling as rapidly."

When he arrived at Key in 2007, Krawitz had big plans for the conduit program, one of the few focused on small-balance loans. He talked about hiring 20-25 originators who could source up to 1,400 loans a year. Krawitz had led a similar effort at LaSalle and later ran the bank's multifamily-housing finance group.

Two other LaSalle alumni who joined Key around the same time as Krawitz were among those laid off this week. **Chad Eisenberg** and **Jon Willems** had worked on LaSalle's small-balance CMBS program. **Ryan Welsh,** who left LaSalle a year prior to joining Key, is expected to remain with Krawitz to work on pending deals. All three men were directors who reported to Krawitz.

Also cut this week were originators **Cory Lanman,** who covered the greater Seattle area; **Jason German** in Atlanta; and **Tony Pass** in Denver. ❖