

# **COMMERCIAL REAL ESTATE**

## **LESSONS LEARNED AND CONTINUING CONCERNS**

**New England Directors College**

**2011**

# TODAY'S AGENDA

- Lessons Learned
- Construction & Development Case Study
- Lending Scenarios



Division of Risk Management Supervision

# **10 LESSONS LEARNED IN REAL ESTATE LENDING**

- **A National Survey of Bank CEOs and Chief Lending Officers**



Division of Risk Management Supervision

# 1

**The cyclical nature of real estate markets was either ignored, unanticipated, or underestimated.**



2

**Equity from borrowers ranged from minimal to non-existent.**



Division of Risk Management Supervision

3

**An emphasis on “loan to value” in lieu of sound cash flow and NOI analysis**



Division of Risk Management Supervision

4

**Feasibility analysis on investor  
construction loans was either  
woefully inadequate or non-  
existent**



Division of Risk Management Supervision

5

**Appraisal analysis and review  
by institutions and lenders was  
inadequate**



Division of Risk Management Supervision

6

**Exit strategies were never  
developed or adhered to**



Division of Risk Management Supervision

7

**Lending personnel were  
under-trained and/or under-  
educated in the realities of real  
estate lending**



Division of Risk Management Supervision

8

**Lenders were fee and volume  
driven, not quality driven**



Division of Risk Management Supervision

# 9

## **Inadequate evaluation and understanding of borrower's overall financial condition**



Division of Risk Management Supervision

10

**Institutions failed to correlate  
lending practices to what was  
(and is) a fundamentally  
illiquid asset**



Division of Risk Management Supervision

# CASE STUDY

- Borrower - Sterling Developers, LLC
- First State Bank
- \$300 million asset size
- 2-rated overall and 2-rated asset quality



Division of Risk Management Supervision

# Your Assignment

- Review Credit Memo
- Review except from Appraisal
- Come up with:
  1. Strengths
  2. Concerns (potential red flags)
  3. What else you would need



# QUESTIONS?



Division of Risk Management Supervision