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## MEZZ PROVIDERS GROW

Real estate equity investors will gain ground providing mezzanine loans as the collateralized debt obligation market remains closed, probably for the rest of the year. Investors looking for high-risk debt returns move away from traditional lenders to money managers who know what owning a property is all about. Trophy office buyer **Shorenstein Properties** will invest a portion of its latest \$1.3B investment fund to mezzanine debt. It competes against **Investcorp** and **KBS Realty**, which also target Class A office deals. On the smaller end of the spectrum, **RCP Capital** plans to increase its mezzanine and equity lending next year as it prepares to raise capital for a second fund.

The first two investments of Shorenstein Realty Investors Nine, LP, were mezzanine purchases. The San Francisco-based company had only done one other mezzanine investment for another fund before these loan purchases. But Managing Director **Mark McCarthy** wants to do more mezz purchases as well as direct originations. The bulk of the fund is still dedicated to property acquisitions. But now it will be able to invest in more Class A opportunities.

Shorenstein has always targeted the top echelon of office buildings in each major market. Its staff has spent time investigating and underwriting this small class of properties. If another investor wants to make a purchase or needs a refi and can't get a large enough first mortgage, Shorenstein's team can likely step in to quickly close a loan. Don't be surprised if it takes mezz pieces on assets it lost as a buyer or places debt on assets it has owned in the past.

The company's September debt deals include spending approximately \$40M for a junior interest in a \$66.8M mezzanine loan, part of a total \$216.8M construction financing for Moffett Towers in Sunnyvale, Calif. It also purchased a \$50M mezzanine loan for 660 Madison Ave., N.Y. Shorenstein's mezz investments are longer term, typically coterminous with the first mortgage. McCarthy will also originate loans that will likely be priced in the mid-teens.

It may run against Investcorp to provide mezz debt on some Class A deals, especially in Shorenstein's Western territory, as the foreign money manager adds workers to the Golden State. Principal **Brian Kelley** and Managing Director **Joel Moody** moved to Los Angeles to open a new office. Investcorp has been in expansion mode, investing a record \$420M of equity during the most recent fiscal year ending June 30.

Investcorp often looks for more opportunistic transactions with rental upside through better management and leasing. It launched TryLyn-Investcorp Mezzanine Partners I LP this year, a \$100M equity fund in partnership with **TriLyn LLC**, another investment adviser. Its loans can go as high as 90% of the capital stack. Rates earlier this year were starting at 4% above LIBOR. But this fund is leveraged itself, and as LIBOR slips and mezz debt demand increases, expect Investcorp to raise its spreads to get the 7% to 10% IRRs its investors are accustomed to.

The CDO market used to be a great place for an owner or developer of an alternative property to get mezzanine debt. But now, boutique equity investors can help. RCP Capital plans to increase volume by \$80M next year by originating approximately \$180M of mezzanine, bridge and short-term equity deals nationwide. Co-CEOs **Richard Myers** and **Donna Arp** are selective though. Of the approximate 1,200 opportunities that cross their desks each year, they will fund only about 25.

KBS Realty Advisors originates mezz debt through its non-traded REIT, KBS Real Estate Investment Trust. Most deals will be five to seven years. KBS understands value-added strategies. CEO **Chuck Schreiber** feels comfortable taking over properties it underwrites if the sponsor gets waterboarded.

## CONTACTS

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