Walker & Dunlop

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Charles Nabhan: We're running a few minutes behind schedule so we're going to start up right now. My name is Charles Nabhan. On behalf of the Wells Fargo specialty finance research team and Joel Houck, I'd like to welcome you to our conference. Joining me today are CEO of Walker & Dunlop, Willy Walker, and CFO, Steve Theobald.

Just to give you a little background, Walker & Dunlop is one of the largest capital providers to the multifamily real estate space. The Company was founded in 1937. And to highlight some of the accomplishments in the recent year, Walker & Dunlop was the largest Fannie DUS lender for the third year in a row and the third largest Freddie Mac Program Plus lender. Additionally, the Company expanded its brokerage platform offerings through the addition of Johnson Capital.

And just using that as a starting point for Q&A, the Company has made several investments during the past year to really grow and enhance the business. And you know maybe we could start off by walking us through some of those, some of those investments and explain how they complement the overall business mix and what should we -- what we should expect going forward?

Willy Walker: Thanks, Chuck. Good morning and thanks for having us here. I guess if you look at the refinancing wave that is taking place right now in commercial real estate we have built to today, if you will, over the last three years as we went out and acquired CWCapital in 2012 then bought, brought on a number of people in the brokerage business across the country, bought Johnson Capital in November of last year, and then just recently bought Engler Financial, our first foray into the investment sales space. All of that was focused on what is happening in the market right now, which is that you have these huge volume increases in refinancings on commercial properties and you also have a ton of activity going on in the asset purchase and sale space as commercial real estate becomes an increasingly attractive investment for both foreign capital as well as domestic capital.

So, really it is just broadening the product offering of W&D. As you mentioned, Chuck, being Fannie's largest partner for the last three years and growing dramatically with Freddie Mac has really positioned us extremely well in the multifamily financing space. We did 16.7% of Freddie's volume in Q1 on a -- on the largest Q1 that either Fannie or

Freddie had ever done. And so our relevance to the two agencies is, if you will, bigger than ever and we have our multifamily borrowers coming to us time and time again. And we're in the process of growing into other asset classes of office retail and hospitality as we continue to focus on multi.

Steve Theobald: Right. And one of the other areas we've invested in that I think complements that is the CMBS conduit where we have a joint venture with, with Fortress to do CMBS lending for multifamily as well as all other commercial real estate asset classes.

Charles Nabhan: Okay, could you give us an update on that CMBS business and maybe talk about your outlook for issuance in the space and how you're positioned to capitalize on, on that opportunity?

Willy Walker: So we've been contributing to you guys. So, how Wells Fargo goes is to some degree how W&D goes. I believe in first 4 months of the year, 25 billion had been originated yet there was another 20 billion in the month of May up for being securitized. So you'll get to the end of May, beginning of June with, you know, 45, 50 billion having been done in the CMBS space. Clearly not at the clip that it was back in 2007 of $230 billion, but you know looking at a, you know, greater than $100 billion year in the CMBS space. So very much back up and on its feet. And we have been -- we have done less volume than we had planned for and hoped but it's been more profitable business than we had planned and hoped for. So we'll actually take the profitability all day and nonetheless it is margins on other securitizations have come down, we have been fortunate to have really good collateral that is priced very, very well into it.

I would say the other thing is that as the agencies have widened over the last month as they were waiting for FHFA to take action on their caps, CMBS could actually price on top of or inside of the, of the agencies. I think that that was a short-lived phenomena. We had in our conduit a big surge in deals and apps out on multifamily for about a three-week period. And now that the agencies have gotten relief from FHFA and are turning around and getting back into the market, I think that that is going to be a thing of the past, if you will, for the time being where conduits aren't pricing on top of the agencies and the agencies start to take the lion's share of deal flow back.

Charles Nabhan: And you mentioned the relief from the FHFA in terms of the exceptions to the lending cap -- the FHFA lending caps for 2015. What do you think that will mean for the remainder of the year, in terms of volume and activity in the marketplace?

Willy Walker: So Fannie and Freddie are both trying to determine how much of the book that they've already done gets reclassified as affordable because the new guidelines on affordability allowed for a lot of the business that they'd done up until this point in the year to fall into new buckets where they don't count against the cap. And then they're also waiting for FHFA to come back with clarifications on what high income markets are, to define them. And then they'll be looking at their book of business going forward and saying, okay, that's a deal that's in LA. That's defined as a high income market. Therefore, the affordability component goes up, if you will, or the ability to do it and have it fit into the affordability bucket changes. And as a result, they then will either be pricing very, very aggressively on loans that don't count against the cap or holding back a little bit on those that have absolutely no affordability component to them.

The numbers that have been thrown around by both Fannie and Freddie is that the adjustment to the caps gives them somewhere between 40 and 45 billion of lending capacity for 2015. To put that in historic context, in 2012 Fannie had done 35 billion before FHFA came in and backed them off. Now, they've done 30 --

Steve Theobald: Three.

Willy Walker: 33 billion before FHFA came in and backed them off to doing 30. So being able to do 40 to 45 is at almost all-time record amounts and for Freddie Mac, who was at a cap of 26 billion last year was moved up to a cap of 30 billion at the beginning of this year and now has the ability to do 40 to 45. It's a, it's a, you know, it's game on if you will. They both did, Chuck, just over -- Fannie did 10.5 billion and Freddie did 10 billion in the first quarter. So if you -- if they've got 40 to 45 billion, they can stay pretty much on that run rate for the rest of the year.

I think big question mark that a lot of people have right now is that there are some huge portfolio deals out there, huge, where a number of large private equity firms as well as other types of investors are looking to buy portfolios and refinance the entire portfolio. And so how much of their capacity gets used up by a couple mega transactions is a good, is a big question.

We did a $670 million deal in the first quarter with New Senior and we also did $403 million portfolio in northern Virginia in the first quarter, which you know those were pretty big deals for us. I know there are a couple multibillion dollar deals running around out there that both we and others are chasing. And so it will be interesting to see how those play, whether those go agency and how much of the caps they end up using.

The final thing I'd say on that is just what FHFA did I think is exceedingly positive for their view on multifamily. The fact that they raised the caps, then found out that the market was bigger than they'd expected and came out with I think a very, very constructive solve in a very short timeframe shows that Mel Watt as director and his staff are focused on making sure that Fannie and Freddie play a very significant role in multifamily financing markets. And we'll see where 2016 goes as it relates to the scorecard. But them moving as quickly as they did and giving the relief that they did is I think a very positive sign going forward.

Charles Nabhan: You touched on the Engler Financial acquisition as your entry into the investment sales space. Could you talk about the plans to scale off of that platform and the opportunity you see in that business?

Willy Walker: We'd like to be in three new MSAs by the end of the year. And so we are out looking for teams of brokers in those three specific cities where we would like to grow this year. And obviously if other opportunities come across, we will, we will take advantage of it. With our platform, we've got 22 offices across the country and we have fantastic relationships with borrowers, given our size and scale in the multifamily lending space.

So, the opportunity we see is to take the Engler platform and their way of doing business, which we believe is very, very, if you will, similar to the way that Walker & Dunlop approaches our business and then go out and bring on, if you will, not necessarily stars in the brokerage space, but the number twos and the number threes. Because (A) they'll come across more cheaply, (B) they're probably ready to step up and take on their own books of business.

But the final point is that we have really great relationships with the borrowers. We have the national platform and the national brand. So you don't really need that star person who is on one of our competitor platforms to come across to Walker & Dunlop and bring their book. We can get someone who's extremely good, who can leverage off of the Engler knowledge base and market presence in investment sales and the Walker & Dunlop physical platform brand and client relationships to be able to expand the platform.

So we think that there's a way to do this, if you will, I don't want to say on the cheap, because I think that that's a disservice to the people that we tried to hire, but not having to go out and pay at quite honestly the top of the market, top market prices to get people to come across.

I would note that there's been a bunch of movement in this space just recently. This morning it was announced that a team just decamped from HFF to move over to Secured Eastdil and so given that that's a joint venture with Wells Fargo, congratulations to you guys. But there's a bunch of movement going on right now. Top brokerage teams know that they are highly sought after and they are, they are unfortunately for us in some instances and in our benefit in others, they are moving for top dollar these days.

Charles Nabhan: Okay. Willy, we talked about the tailwinds from a regulatory standpoint with the FHFA and the current administration, but you know underpinning that opportunity and tailwind is a wave of debt maturities. Could you talk about that, that opportunity? What that means and what that means for the space?

Willy Walker: So you have hundreds of billions of dollars of commercial real estate debt that needs to be refinanced in '15, '16, and '17 across all asset classes. And we and the other major providers of capital to that space are going to be the big beneficiaries. We have scaled the platform over the last several years to be in exactly the position we are in today and our Q1 results show that the refinancing wave is here and that we have the size, scale, and brand to be able to take advantage of it.

As it relates to the regulatory backdrop, I do think that the latest actions by FHFA are very positive. Invariably, people often say, so what happens after 2016? Cause nothing is happening on GSE reform between now and the 2016 presidential election. If you ended up getting one party controlling the White House, the Senate, and the House, which there are very long odds on right now, you might get something on GSE reform in the next Congress. But if you have any kind of split of power and it's going to be very hard for the Republicans to hold the Senate, it's impossible for the Democrats to win the House and obviously the White House is a coin flip, likely we will have divided power. Likely we will be in the exact same situation we are in today, which is that trying to get the momentum towards GSE reform is going to be hugely, hugely difficult.

And so all the action then sits at FHFA and at the regulator. And what we have seen from Mel Watt in his first year as regulator is a, if you will, for all practical purposes, a pro-GSE standpoint or a pro-GSE approach to his role as regulator. And so for those of us that do a lot of business at the agencies, specifically in the multifamily space, it's probably got a pretty good run here.

Charles Nabhan: One of the ways that you've capitalized on the opportunity in the space is through your interim lending business. Could you maybe give our investors and attendees a sense of what that, what that business does and provide us an update on the activities in that space?

Willy Walker: You want to do that?

Steve Theobald: Sure. Happy to. So, we started a program to use our balance sheet to finance interim or bridge loan opportunities in the multifamily space. Late in 2012 and it really started to get traction in 2013, end of the first quarter we had about 250 million on the balance sheet. As I said, it's all multifamily. The objective here is to get in front of borrowers who aren't quite ready for that Fannie, Freddie or HUD permanent loan, who otherwise in the past would have gone to a bank or you know potentially even an insurance company for financing. And by using our balance sheet, we can you know strategically originate loans to these borrowers and then be in a position to take the loan to Fannie, Freddie or HUD when it's, when it's ready.

So we've been exceedingly pleased with the results there. Credit quality has been very good. Returns have been in the, you know, mid teens on an invested capital. And we've had great success in taking the loans that have matured or been ready to pay off into that permanent financing. So our returns are great even without the benefit of that, but with that it's, you know, been exceedingly positive for the Company.

Charles Nabhan: Great. The GSEs have added a, added a number of products, new products and capabilities over the past few years to help them better compete with financial institutions. Could you talk about some of those products, the impact they've had on the competitive environment and, you know if you see further innovation occurring within the GSE product set?

Willy Walker: So Freddie Mac was not in the manufactured housing space and was allowed in by FHFA last year. W&D did Freddie's first manufactured housing loan and we were their largest manufactured housing partner in 2014. And manufactured housing is outside of the cap, so it's a great space for us to have real scale and great client relationships.

Both agencies have been very focused on affordable as well as small loans and have had to innovate in that space to meet the caps or meet the desires of FHFA. Those are tough spaces to compete with commercial banks, to be honest. Your retail, you know, store on every corner has access to small loans that the agencies and companies like Walker & Dunlop don't have access to. And so trying to compete with the Wells Fargo's and the JP Morgan's of this world for small multifamily loans is extremely difficult. And then on the affordable side, you all have CRA requirements that require you to go and lend in those types of markets. And so with your cheap deposits competing against the likes of JP Morgan Chase and Wells Fargo for affordable business is also quite difficult. So, both the agencies are having to really hone in on those two specialty products and try and innovate.

The other product that they rolled out was a pre-stab product which was competing against our balance sheet. So to the program you just asked Steve about and what Steve was talking about, a year ago we didn't have a whole lot of competition in that space. Both Fannie and Freddie created products last year to compete in the pre-stab space. With them running into the caps and having to ask for the relief that they just got, both of them have pulled back from the pre-stab space. And so we think that there's a great opportunity right now as it relates to our balance sheet lending to be able to do a lot of the pre-stab/interim lending where the agencies did step in there and now they've pulled back out.

Charles Nabhan: Okay. Could you explain the dynamics of your gain on sale margin and how concentrations in Fannie and Freddie in fixed versus variable loans impact that margin? And you know as a follow-up to that, I think one of the underappreciated opportunities within the -- within your lending book is the opportunity to refinance floating rate originations into fixed rate products down the road. So if you could just, you know, give us some color on those areas and just help us parse the dynamics of the gain on sale margin?

Willy Walker: So, you want to go?

Steve Theobald: Yeah, I'll jump in on, on that. So, yeah I think the nature of the question here is if you look at our gain on sale margin, it has come down over the last couple of years from you know the high point probably in the fourth quarter of 2012. Most of that has been a result of you know increased competition in the market, pricing you know between Fannie and Freddie, driving a decrease in the amount of servicing revenue we've recognized on our Fannie Mae portfolio.

I think from our perspective, we're really a, you know, bottom-line focused company and really focus our attention on the operating margin, which you know we have an objective to keep into the, in the mid 20% range. And so, you know, as the margins come down, we've been managing the cost structure. We've had an increase in volumes and as a result, you know our operating margin over the last year has, has actually increased and was in excess of 30% in the first quarter with the, with the volumes we did. So that's really been our focus.

If you kind of pull back on the margin a little bit, the gain on sale margin, the mix does matter. So as more of our business has been Freddie Mac versus Fannie Mae, that's had, had an impact. As more of our business has been variable rate versus fixed rate, that's also -- has an impact primarily on the noncash revenue. So our mortgage servicing gains on a floating rate deal, even though the servicing fees on the loans themselves are at least as high if not higher than the fixed-rate deals, mortgage servicing rate we book is lower because we limit ourselves to a two-year expected life on those loans, just because of the, of lower prepayment fee associated with paying those loans early. So less noncash revenue translates into lower gain on sale margin, but from an EBITDA perspective, it's generating much higher servicing fees than what we were, were getting before.

And to, to Chuck's point, as those loans either refinance at some point, because the borrower wants to lock in a long-term fixed rate as the yield curve starts to move, we have an opportunity to, you know, refinance that loan in a relatively short period of time. The other benefit to our P&L is the mortgage servicing rate is amortized over two years. So to the extent that that loan sits, you know, on our servicing portfolio for longer than two years, we're generating cash servicing fees with no corresponding amortization at the

MSR. So, get a benefit of that down the road as well.

Charles Nabhan: Okay. You know I think one of the themes of the day is interest rate sensitivity. And you know obviously Walker is a C Corp not a REIT, like many of the presenters are today here, here today. But nonetheless there is a degree of interest rate sensitivity. And you know I was hoping maybe you could talk about that and how potential rise in short-term rates at the end of the year could, could impact your financials and your business?

Willy Walker: So, our borrowers clearly aren't concerned with interest rates, if you look at Q1 and the amount of floating rate debt that we put out in Q1. I think that that's less to do with their bet on the Fed raising rates and more to do with (A) the prepayment flexibility as Steve just talked about in doing a variable rate deal versus a fixed rate deal and second of all, the, the delta that exists today between variable rate financing and fixed rate financing when you're buying assets at extremely low cap rates. And as a result of that, many, many borrowers are opting to go with floating rate and take the risk and obviously all of them are putting caps on it, so there's, you know, their interest rate sensitivity is capped.

As it relates to whether rates start to move once the Fed moves, I, on the short term, on the short end of the curve, obviously rates are going to move when the Fed raises rates. I am less convinced that the long-end of the curve is going to move at all when they start to raise short-term rates. The amount of foreign capital chasing sovereign returns with a positive number in front of them is growing, it seems by the day. And as a result of that, I think that it's going to take quite a bit of movement by the Fed to get the long end of the curve to move. And as a result, I think that what ends up happening is a lot of our borrowers move off of short-term variable rate and move more towards long-term fixed but at rates that are very, very reasonable for a period of time.

And then it'll all start to move and the real question is how far does it move? Right now the loans that we're putting into our portfolio we feel exceedingly good about from a debt service covering and LTD standpoint. The only variable that we lose any sleep over right now is where's the ten-year ten years from now as, on these loans that might have either a significant amount or full-term IO and what are you looking at from a refi risk of a bullet at the end of that ten-year period? And so, we think that we take very conservative views as it relates to where rates will be and where the ten-year is ten years from now. But if you could tell me where the ten-year is ten years from now, Chuck, and be within, you know, 100 basis points, I'd, you know, be really excited to hear it. So, we feel really good about where things are.

But one other piece to our business model is that first of all, all of this debt that needs -- that is maturing has to be redone. So even though we're in a very low interest rate environment today, if rates move, it still needs to get done. The second thing is that if rates move precipitously that would mean that people are looking for mezz preferred equity and a firm of our size and entrepreneurial nature I would put forth, we can go and figure out how to meet that demand and need for different types of capital. And the final thing is that we've got about a billion dollars in escrows on our, in our loan portfolio that today is earning almost nothing because it's all parked in short-term vehicles. If rates start to move there, we start to make some money off of that billion dollars of escrows. And so we have a little bit of a hedge there as it relates to, if there is some point in the curve where that incremental loan doesn't get originated as rates move up, you're also picking up in our business model additional interest income off of those escrows.

Charles Nabhan: Right.

Steve Theobald: Yeah, I was just going to add that from a balance sheet perspective, we are asset sensitive because of the escrow deposits. So, most of our lending operations, whether it's on balance sheet or our loans held for sale, are pretty well match funded and our term debt, our senior debt, which is about 170 million is a floating rate instrument with 100 basis point LIBOR floor. So there's quite a bit of movement in short rates before that starts to increase. And we have a billion dollars of escrow deposits that as Willy mentioned, you know, don't earn very much now that are tied to short-term rates. So as rates rise, I do expect us to benefit from that from a balance sheet standpoint.

Charles Nabhan: You touched on demand trends which are obviously quite strong at this point. But, can you maybe talk about supply and what you're seeing, you know, across the various markets?

Willy Walker: As far as the competitive landscape?

Charles Nabhan: Yeah.

Willy Walker: You know what are there? There are 30 conduits up and running right now and I said previously that there's probably a billion -- $100 billion of capital that comes out of conduit world. There's the life insurance companies are typically good for around $50 billion of capital on an annual basis to commercial real estate. The agencies will put out about $80 billion, give or take a little bit, between the two of them this year. And then you've got the commercial banks.

And one of the big differences in 2015 from 2013 is that when the agencies pulled back in 2013, the banks had been out of the commercial real estate lending space. There weren't a lot of cranes up across the country, so there weren't a lot of construction loans for banks to put capital out on. And so banks moved into both variable rate as well as fixed rate commercial lending in 2013 in a big way. Backed up the bus and took a lot of multifamily, took a lot of office, took a lot of everything.

And I think that two things have happened. One they all filled up and sort of said okay, great, we've got our allocation for a while. Two, is that the regulatory environment as it relates to Basel III as it relates to Dodd-Frank has got a lot of banks wondering whether they want to load up on MSRs at this time. And then the final piece to it is that specifically in the multifamily space, both of the agencies figured out how to compete with the banks on a variable rate product. In 2013, the agencies' variable rate product was terrible. Today, their variable rate product is fantastic.

And so I would just put forth that in our core multifamily business, the agencies are competing and beating the banks a lot other than in those two pockets that I talked about, small loans and affordable, which is somewhat ridiculous because that's where FHFA wants them to be lending. But that's a whole different story. But and then life insurance companies will continue to win on the lower leverage Class A deals in major cities in pretty much all food groups and the conduits are, are winning on the higher leverage across all asset classes. And there's plenty of capital out there. It's not back to 2007, you know, it's not back to 2007 spreads and leverage levels and you know 1.05 debt service cover if you're lucky. But it's, you know, it's heating up. It's definitely heating up. What I don't see stupid deals being done, but we're starting to see some deals that make you scratch your head.

Charles Nabhan: You've talked about building off of your existing businesses to add scale, but are there any areas which you're currently not active in, which you would like to be in?

Willy Walker: We want to have a national investment sales platform in multi. We'd like to scale that out into other asset classes. I had someone call me this week and say, hey, I've got an office building in DC. I'm looking at hiring this firm and that firm to do BOV on it as well as take a look at what it would do to refinance it. And I wrote them back and said, I can't give you a BOV on an office building in DC but I certainly can take a look at the financing side. So having those two sides of it would be great. The issue is, how much time does it take to build it? How much scale do you need to be able to actually have that in the marketplace? And then also, where are we in the cycle?

Right, so, one of the things that we consistently focus on is our business is taking advantage of the growth in the markets today but also has a huge piece of it that is countercyclical. 2009 and 2010 were fantastic years for Walker & Dunlop, fantastic. And our core agency lending business and our HUD business are fully countercyclical and our servicing portfolio that this year will kick off over $100 million in revenue keeps on going in good times and in bad.

And so a lot of our competitors who are just in the brokerage space/transaction space, they fly when things are good and all you've got to do is look at a couple of their stock prices in 2009 and they sink like a rock in bad times. We think we have a really durable business model that has some very important countercyclical pieces to it. So the question to us is, how much do you want to expand in this up market beyond what we do today and use our capital wisely to either grow in our core markets today or expand out? And then the second thing is how much capital do we hold on to so that when those other companies' valuations drop like a rock as they did last time around, can we step in and potentially fix some things up on the cheap?

Charles Nabhan: The servicing business has been one of the steadier revenue streams within the overall mix. Could you talk about some of the, some of the steps you've taken to build out that business? Perhaps, you know, adding servicing rights through the broker, the broker platform and also some of the efficiencies you've, you've gained off of that business as well?

Steve Theobald: Sure, I'll take that one. So, I mean servicing in our business is very scale oriented. So as we have, you know, consistently grown our servicing portfolio, the underlying economics of that continued to, to improve. You know we're at the point where we don't really have to add, you know, much in the way of personnel costs when we're originating at the levels we're, we're currently originating at. We did Johnson Capital acquisition in November, brought over a small HUD portfolio. Didn't have to add any resources to, to cover that. So it's really, you know, add scale from an economics perspective. So our objective there is to continue to, to build that and grow it.

Yeah, I think for us the primary value of the servicing is the prepayment and protected nature of it. Roughly 90% of our servicing fees are protected by prepayment fees that if the borrower pays the loan off early, we get paid essentially the, you know, discounted value of our future servicing. So it's a really powerful differentiator for us relative to say a residential real estate portfolio. So we don't have the volatility in that number and if you can see that in our financial statements in the steady growth in that revenue line over the last three years.

Charles Nabhan: Okay. We -- running close to the end here. I guess at this point we have a couple minutes left if there are any questions from the audience, we could take them at this point.

Unidentified Audience Member: Is this on? Yeah. Good morning. Could you address any risks that you see or stated another way, what are the biggest risks you see in multifamily? Are there any particular markets that you're concerned about? And, you know, maybe perhaps Houston as an example of a market that you might be concerned about? Thank you.

Willy Walker: So, there, there are great markets and there not so great markets in the country today as it relates to macro fundamentals. But every deal that we do is on a micro basis. Every single loan that we put out, we go and visit the property. We do a full underwriting of the actual property and all of the comps around it. And so, you know, San Francisco is a market that's on fire. Are there stupid loans to make in San Francisco today? There clearly are. DC has been a market that's been underperforming. Are there still good loans to do in DC? Lots of them. So, as it relates to a market like Houston, (A) we don't have a ton of exposure in Houston and (B) we have not seen as it relates to our overall portfolio, at the end of Q1 we had 13 basis points of our at-risk portfolio 60 days delinquent. Okay, so really nothing. It was zero at the end of Q3 and it was 2 basis points at the end of Q4. And so it's a, it's a great time from a credit cycle standpoint as it relates to the performance of these portfolios. The real question right now is back to the money we're putting out, how's it look five years from now, seven years from now, ten years from now?

I'd also say if you look at the credit quality, when I went into to meet with FHFA to talk about Fannie and Freddie and their caps about a month ago, I wanted them to get a sense of what our lending criteria was with Fannie and Freddie and how it had changed between 2014 and 2015. So we looked at all of the deals that we did for Fannie and Freddie in Q1 '14 versus Q1 '15. Q1 '14, the average loan to value was 68%. It moved up to 70% in Q1 of 2015. In Q1 of '14, the average debt service cover was 1.47 and in Q1 of '15 it was 1.45. So as I said to FHFA, we'll do 70% 1.45 debt service cover loans for the rest of our careers and be extremely happy doing those.

So, you haven't, from an underwriting standpoint, gotten to silliness. The silliness up until now has been both on price as well as IO. And it's the IO component that has been, you know, sort of the I don't want to say, it's made it so that the funds have been exceedingly active because they're getting, seven, ten year, full time IO loans. Their promotes are going through the roof and they can actually make the numbers work on a 4.5 or 4.25 cap rate, okay. And so I think that this sort of cooling off period over the last month where the agencies were sort of backed off a bunch, waited for FHFA to come out and are now coming back into the market, (A) their price isn't going to be as tight as it was previously. They're going to price under the market but not significantly. And the second thing is they're going to back off the IO. And I think that's, quite honestly, quite healthy for the market.

Yeah.

Unidentified Audience Member: (inaudible)

Willy Walker: Yeah.

Unidentified Audience Member: What's the difference in the spread between a head scratcher and a stupid deal?

Willy Walker: So, the, the head scratchers are recaps of portfolios that were bought in 2012, are being redone today where really the only variable that's changed is the cap rate. But they're doing a cash out refi. You still have tons of debt service cover on the deal and it's cash flowing perfectly. So as a, as the holder of the 70% loan and the risk associated with that 70% loan, we love it all day long. But you got to sort of scratch your head as the person who bought the portfolio and I'm obviously speaking specifically about one deal that we financed where the, where the buyer of the portfolio is doing a $20 million cash out refi 3 years later purely because we've had cap rates, cap rate compression and because NOI has grown significantly to the point where they can now put on a huge amount more leverage and put a big check in their back pocket.

I don't love that deal but as it relates to the actual property, cash flow and the loan we have on it, we're fine doing it. But you scratch your head a little bit in doing that. That's just one that sort of, it just -- that's not what we would like to do in a perfect world and at the same time it's where the competitive market is. If that refi and the cash out refi was being done at an 85% loan at a 1.25 debt service cover or 1.20 debt service cover, I'd be really concerned. But that had plenty of coverage and it was a lower leverage deal that we were fine doing it.

So, but that's where you start to see people stretching for deals, stretching to do deals. And the cash out refi, where someone has held the asset for 2.5 years and they're putting 20 million bucks in their back pocket, they're basically, in that situation, they basically took all their equity out of it. Okay, so they're not going to BK the deal. They're not going to walk away from it. It's a great investment for them and it's flowing perfectly well. But, we don't like doing big, big cash out refi's. Just don't. Those are the deals that typically go bad on you.

Charles Nabhan: Great. Please join me in thanking Willy and Steve.

Willy Walker: Thank you.

Steve Theobald: Thanks.