

Creative Commercial Underwriting: Maximum Leverage on Negative Cash Flow Properties

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CIRCLE BANK

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Creative commercial underwriting

Circle Bank blends the traditional cash-flow underwriting of commercial lending with the debt-to-income (**DTI**) personal credit analysis used in residential lending. **This hybrid underwriting method allows higher LTVs, which means more cash in the buyer's pocket.**

- ▶ DSCRs as low as .70 : 1.
- ▶ Personal DTI ratio as much as 50%.

Let's compare traditional underwriting to Circle Bank's approach...

Example: Apartment building purchase.

Traditional Analysis

Purchase Price	\$1,500,000
Allowable DSCR	1.10 : 1
Allowable LTV	75%
Gross Income	\$100,000 per year
Interest Rate	6.75%, fixed for 5 yrs.
Amortization	qualify at interest only

Traditional cash flow analysis

Gross Income (GI)	\$100,000
<u>Less Vacancy Rate (5%)</u>	<u>\$ 5,000</u>
= Effective Gross Income (EGI)	\$ 95,000

Property Taxes	\$ 17,100	(1.14% of PP)
Insurance	\$ 5,000	
Reserves (3% of EGI)	\$ 2,850	
Maintenance (3% of EGI)	\$ 2,850	
Management (5% of EGI)	\$ 4,750	
<u>Miscellaneous (4% of EGI)</u>	<u>\$ 3,800</u>	
= Total Expenses	\$ 36,350	

Net Operating Income (NOI) **\$ 58,650**

Traditional cash flow analysis

Allowable DSCR: 1.10 : 1

Calculate Debt Service:

$$\text{NOI} \div \text{DCR} = \text{Debt Service (DS)}$$
$$\$58,650 \div 1.10 = \$53,318$$

Calculate Loan Amount:

$$\text{DS} \div \text{Rate} = \text{Loan Amount (LA)}$$
$$\$53,318 \div 6.75\% = \mathbf{\$789,899}$$

LTV = 53%

Minimum Leverage

The traditional underwriting approach, even with favorable low interest-only rates, often requires *huge* down payments in order to achieve positive cash flow. Is there a better way?

Underwriting a negative cash flow

- ▶ At **Circle Bank**, we calculate the difference between the NOI and the loan payment.
- ▶ The difference is then added to the borrower's *personal* debt load, like a car payment.
- ▶ We then calculate the borrower's projected *personal* debt-to-income (DTI) ratio. Debts include monthly housing costs plus all other monthly obligations, including the projected negative. Income is taken from tax returns and year-to-date income.
- ▶ *If the total ratio is 50% or less, we are within the guidelines.*

The Circle Bank apartment analysis

Gross Income (GI)	\$100,000	
<u>Less Vacancy Rate (5%)</u>	<u>\$ 5,000</u>	
= Effective Gross Income (EGI)	\$ 95,000	
Property Taxes	\$ 17,100	(1.14% of PP)
Insurance	\$ 5,000	
Reserves (3% of EGI)	\$ 2,850	
Maintenance (3% of EGI)	\$ 2,850	
Management (0% EGI)	\$ 0	
<u>Miscellaneous (4% of EGI)</u>	<u>\$ 3,800</u>	
= Total Expenses	\$ 31,600	
Net Operating Income (NOI)	\$ 63,400	

The Circle Bank apartment analysis

Allowable DSCR: .70 : 1

Calculate Debt Service:

$$\text{NOI} \div \text{DCR} = \text{Debt Service (DS)}$$
$$\$63,400 \div .70 = \$90,571$$

Calculate Loan Amount:

$$\text{DS} \div \text{Rate} = \text{Loan Amount (LA)}$$
$$\$90,571 \div 8.125\% (\text{I/O}) = \$1,114,725$$

LTV = 74.3%

Maximum Leverage

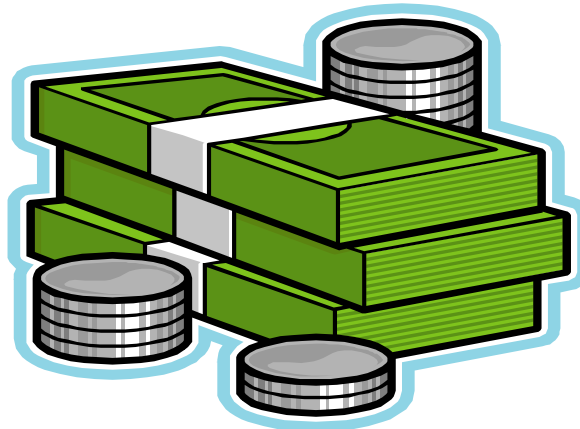
Circle Bank's non-traditional approach lets the buyers keep *more money* in their pockets, which is better used to improve the property which increases the rental income, and thereby increasing the value of the property.

Comparison: traditional vs. creative

	Traditional	Circle Bank	Difference
Purch. Price	\$1,500,000	\$1,500,000	
GI	\$100,000	\$100,000	
Rate	6.75%	8.125%	+ 1.375%
Payments	360	Interest only	
Amortization	360	Interest only	
NOI	\$58,650	\$63,400	+ \$4,750
Exp. Ratio	38.30%	33.30%	- 5%
DSRC Ratio	1.10	.70	- .40
DTI Ratio	?	50%	
LTV	53%	74.3%	+ 21.3%
Down Pmt.	\$711,000	\$385,275	- \$325,725
Max LA	\$789,000	\$1,144,725	+ \$345,725

Creative commercial underwriting

Mo' money for your borrowers!
Mo' sales for you!



The Circle Bank advantage

- ▶ .70 DSCRs on purchases of *all property types*.
- ▶ No management expense for owner-operators.
- ▶ Actual property taxes on refinances.

- ▶ “Make-sense” streamlined decisions.
- ▶ Down payments as low as 15% (75-10-15).
- ▶ Stated income to 60% LTV.

- ▶ “Strong” borrowers buying “weak” properties OK.
- ▶ Global cash flow underwriting.
- ▶ Creative solutions.

Conclusion

- ▶ **Don't get caught in the commodity trap.**
Our hybrid underwriting approach and creativity offers value-added solutions.
- ▶ **The lowest rate isn't always the best deal.**
Can your clients make more money by leveraging a purchase? With a smaller down payment, they can preserve their liquidity, make improvements, increase their cash flow and increase the value of the property. Or buy another investment property.

Conclusion

Circle Bank's hybrid underwriting approach puts more money on the table for your borrowers. Most professional investors don't know that they can get purchase money loans with DSCRs as low as .70.

Go forth and thrive!



Please call me to help you size your deals.
I wish you success!

Mark Skolnick • Circle Bank

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