INDUSTRY EXPERT OPINION REPORT

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WHAT TYPES OF NNN PROPERTIES ARE THE EASIEST TO FINANCE? WHAT TYPES OF NNN PROPERTIES ARE THE HARDEST TO FINANCE?

WENTZEL: To a great extent, three criteria impact the feasibility of net lease financing: Credit quality, location and lease term. Assets with investment grade (or equivalent) tenants, good locations, and long term leases (20-25 years) are easiest to finance. Without one or two of these criteria, financing becomes increasingly difficult. Below investment grade tenants, tertiary markets, and short term leases are major concerns and can negatively impact the ability to obtain financing for a property.

Over the last 12 months high quality assets have been in strong demand; drug stores such as "Walgreens" being the perfect example. As a result of this strong demand, cap rates for high quality assets have been driven down to the low/mid 6 percent range. Investors are now looking for higher returns and have started focusing on properties that may not have all 3 of the criteria mentioned above. Around the end of 2010, an increasing number of investors became willing to sacrifice one or two of those criteria for better yields.

Washington D.C., New York, Boston, Chicago, Dallas, L.A and San Francisco are all popular locations for acquiring net leased assets and urban infill locations with good demographics are highly sought after.

WHAT TYPES OF LENDERS ARE FINANCING THE NNN PROPERTIES?

WENTZEL: Local and regional banks have been very active depending on geographic location and how they have weathered the recession. In New England, for example, and other major metro areas, local lenders are very aggressive. Most insurance companies are very picky and majority will only finance assets with investment grade tenants, lease terms of at least 15 years and strong locations.

Recently, the CMBS market has been very active in lending for net lease deals in contrast to the 2004-2006 era when they avoided single tenant properties. In the last 12-16 months, CMBS lenders have done more net lease financing than insurance companies and unlike most insurance companies, the CMBS lenders are more willing to deal with shorter lease terms, longer loan amortizations and more varied locations.

WHAT TYPES OF LOAN STRUCTURES ARE BEING EMPLOYED FOR THE FINANCING OF NNN PROPERTIES?

WENTZEL: Most structures are 5-10 years with amortizations ranging from 20-30 years. The loan to value range can exist anywhere from 60-65% (insurance companies) to 70-75% (CMBS). Banks usually have a loan to value range of 60-75%, 5-10 year loan terms and 20-25 amortization periods.

As expected, properties with longer lease terms, investment grade tenants and good locations can command more flexible and advantageous loan terms.

WHAT RECENT TRENDS HAVE YOU OBSERVED IN THE NET LEASE MARKET?

WENTZEL: The lack of new product entering the market has created competition among both buyers and lenders. As a result, it appears that lender spreads will continue to tighten in the coming months and investors and lenders will become more flexible in regards to the 3 key deal criteria (credit tenant, lease term, location).

Fueled by increasing optimism about the economy, companies are now thinking about expansion as opposed to 6-12 months ago and investors are teaming up with developers to fund new projects. In such deals, investors may agree to purchase a property upon completion with a forward commitment (including purchase price and cap rate). Additionally, we are also seeing investors funding construction for developers in order to own the property upon completion and obtain better returns than are available in acquiring existing properties

WHAT WERE YOUR FEELINGS ABOUT THE NET LEASE MARKET BEFORE THE CONFERENCE? AFTER?

WENTZEL: Bullish going into it and bullish going out of it due to low supply high demand. People are now trying to find niches where they can get higher returns by sacrificing tenant credit, location or lease term. As an example, some investors are looking for stronger locations with shorter lease terms while others are seeking stronger tenant financial profiles and sacrificing location or lease term.

HOW DO YOU SEE THE NET LEASE MARKET TRENDING IN THE NEXT 6 MONTHS? 1 YEAR?

WENTZEL: I believe in the short term, cap rates will continue to compress as investors will continue to look for niches where they can obtain better returns. However, over the next year, there is a strong possibility that inflation and interest rates will pick up – forcing cap rates higher. A year from now, if inflation and interest rates start climbing, corporate bonds could generate 6-7% returns that would compete with the current cap rates of NNN properties.

WHAT NET LEASE SECTORS DO YOU THINK WILL PERFORM THE STRONGEST?

WENTZEL: As the economy strengthens the industrial sector will continue to improve and more product should enter the market as companies expand. Retail should do OK and more product will probably enter the market. In many geographic areas, office is still hampered by oversupply. However, if the fundamentals are correct, the assets will still retain value.

FOR MORE INFORMATION

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