LESSON TEN: SOLVING FOR THE "UNDERWRITTEN NOI"

The permanent lender will start with the stabilized NOI and then make a series of deductions from the NOI, to get to the magical "Underwritten NOI" figure. It is from this number that the loan is sized.

1.1 DEDUCTIONS

Deductions are shown in the example transaction and may include the following:

1. Vacancy: Even if the building is fully leased, the lender will make deductions to the NOI for vacancy. The maximum occupancy is 95%. The lender will use the lesser of 95% or the market occupancy.
2. Tenant rollover assumptions: This is a prediction of what will happen with rolling tenants. Typical rates are 75% renewal, 25% departure. The impact is felt in the T/I and leasing commissions.
3. Average lease term: Typically 3, 5, or 10 years: depends on the asset and market (the shorter the lease term, the more roll, the more roll, the more escrow required). Positives and Negatives of long leases
4. Tenant improvements: Typically broken into:
    - Renewal tenants: less dollars needed to renew tenants office is typically $5.
    - New tenants: more dollars needed to get a tenant into the space. Can be up to $30 for office.
5. Leasing commissions: Commissions are paid on both new and renewal leases. New leases are typically 6-7% of total "economic value." Renewal leases are typically 2-3% of total economic value
6. Capital reserves: The lender will want to build an escrow account for annual maintenance. Typical structural reserves are $.10-.50 per square foot, per year, depending on the age and condition of the building.
7. Releasing down time: The space will be "dark" during the releasing. Investors will forecast 1-6 months of downtime.