

The Draw of Commercial Loans

Many brokers are taking on commercial deals — here are some reasons why

By **Michael Zaslav**, vice president of sales, Commercial Loan Capital LLC

WITH THE SLOWDOWN OF THE RESIDENTIAL real estate market in the past year, many mortgage brokers have diversified their business to include commercial financing.

There are several reasons why residential mortgage brokers are switching to commercial finance or adding it to their product arsenals. These include factors such as commercial loans being unique, having less-restrictive lending guidelines, being less rate-driven and having less competition. In addition, commercial loans often are an easy sell if borrowers have a need and have nowhere else to turn.

■ **Unique quality:** Every time the phone rings, a commercial mortgage broker can't predict what the call is about. Every loan is different. For instance, one borrower could be looking to buy an apartment building for long-term investment in St. Louis with great cash flow, while another wants to buy an apartment building in California and flip it for profit in one year with low cash flow.

■ **Larger loan sizes and fees:** From multibillion-dollar casinos to multimillion-dollar high-rise buildings, commercial loan sizes are much larger on average across the country.

This often translates to larger fees for the brokers and account executives. There is so much competition for residential A-paper mortgages among lenders, banks and brokers that regardless of loan size, the fee is considerably less. Borrowers have so many options.

On the commercial side, on the other hand, an owner of an auto-repair shop who needs cash out and who can't verify income has fewer options. In addition, the fee for that loan would be greater.

Because of fewer options, larger loan sizes and less competition, commercial loans can be more profitable on average compared to residential.

■ **Less rate-driven:** Most commercial loans are not rate-driven because the need for commercial loans is so different compared to residential. Many self-employed commercial borrowers can't verify their income because of the large write-offs they take against their business. Therefore, when they go to get cash out, their net income does not cover the loan.

In these cases, traditional banks often will not consider such loans because their guidelines require verifying tax returns, and banks are strict in limiting cash out. In addition, most banks require a written explanation that indicates the need for the cash, limiting the clients' options as to where to go for the cash. If you find borrowers with a serious need and they can't verify their income, the only thing you have to sell to them is the monthly payment.

■ **Less competition:** There is less competition for commercial deals because every deal is so different and because fewer investors and banks can offer borrowers exactly what they need. This becomes a much easier sell as borrowers have no other option.

Let's assume a borrower owns an auto-repair shop with a fair market value of \$1 million and has a 680 credit score or greater. This borrower has a serious need, has no other options and is using the money as an investment for his business.

Many commercial lenders can get this borrower as much as \$800,000 cash out to make improvements to the building, to hire new staff

and to purchase new equipment without ever verifying financials.

This becomes an easy sell because banks typically will not give this borrower \$800,000 in cash without verifying income, especially on an industrial property. The rate thus becomes completely irrelevant, and the mortgage interest is 100-percent tax-deductible.

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The decline in the residential market has not had a strong effect on the commercial market. Nationwide, the commercial real estate market is growing, and rental income and property values are still increasing.

The interest-rate hike of the past few years has not affected the commercial business because most commercial borrowers invest the money for profit. As long as the monthly payment is affordable, a commercial loan makes sense for borrowers who are looking for cash out to purchase new equipment, to hire a new work crew or to purchase a new building and who are showing losses on their tax returns. 



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