Why You Need a Full Financial Workout Even During a Boom

It is easy to skip critical steps during an economic growth period, but completing a structured workout is essential in good times and bad.

By **Kelsi Maree Borland**

During a boom, it can be easy to skip critical steps and rely on the momentum of the market, but ultimately, you'll get caught when the music stops. During good times and bad, **George Mitsanas** of **Newmark Realty Capital** says the completing a complete financial structured work out is essential to risk management, even in a growth period.

"Exceptions define rules, and that is certainly true for boom cycle debt and risk management. As an example, I can point to the odyssey of the Arrive tower. This recently completed 43-story mixed-use tower in Seattle's Belltown survived a tumultuous restructuring to become a triumph of tenacity in Seattle under new sponsorship," Mitsanas, a principal at Newmark Realty Capital, tells GlobeSt.com. "This well-timed and well-conceived project required salvaging nearly $331 million in equity and debt for a project in one the nation's healthiest markets. Distress happens, and when it does, having the experience to address, navigate and resolve issues to satisfy obligations is essential."

For developers and redevelopment projects, this risk management tool can be essential as the economic conditions can shift during the project period. "Developers naturally face a long list of challenges that can derail a project and put capital at risk," says Mitsanas. "Entitlement or construction delays from local politics or activists. Boom cycle labor, construction, and commodity scarcity and/or price spikes; or, in the case of a project like Arrive, a breakdown in sponsorship ethics and management. These factors can stress budgets, alter timelines and compel a complete reassessment of feasibility in a healthy market."

When taking local market patterns into account, proper workouts become even more essential. Real estate is a highly local asset class, and investors must understand both national and local market trends. "All real estate is local and not all local markets are created equal. The way space use evolves in a neighborhood, submarket or region will have significant impact on financing terms and debt structure," says Mitsanas. "Macro-economic trends that change regional employment dynamics or the way goods are transacted can undermine original underwriting and debt performance."

Market patterns also change based on the asset class. Retail, for example, is considered higher risk because it is in the midst of a major revolution. Likewise, office assets have also seen changes in tenant demand. "If you look at challenges facing the retail sector today, there is a

fundamental shift in the way goods are purchased and consumed, which in turn affects the way real estate is used, occupied and performs," says Mitsanas. "This has also happened in the office sector, where we continue to see shifts in space demand from an evolving white-collar workplace. A structured workout can resurrect a non-performing asset to meet new market realities and preserve lender funds."

This is one way to mitigate risk during a downside. Mitsanas adds that developing and maintaining a relationship with capital partners is essential as well to risk management. "Be proactive and prioritize your relationship with your servicer during the good times so channels of communication are open if and when distress arises or, more importantly, is looming," he says. "Also, develop a standing relationship with a capital markets expert like NRC that you trust and that understands your unique investment goals, deal structure and return targets. You want a professional relationship that specializes in debt structure and is constantly reviewing options for optimized structure to maximize available leverage, rates and timing in whatever the cycle. There are too many variables and when that is the case, have a specialist on speed dial."