KEYNOTE INTERVIEW

Seizing the refi opportunity in US multifamily credit

Debt funds looking to take advantage of the surge in refinancing must be able to lend at attractive rates based on a highly efficient cost structure in an increasingly competitive environment, argues Prospect Capital's Joseph Ryu

In commercial real estate, Prospect Capital has traditionally operated as an owner of value-add multifamily properties, managing roughly 22,000 apartment units in its current portfolio valued at $3.4 billion.

The firm has recently developed and launched a real estate private credit strategy, Prospect Credit REIT (PCRED). Joseph Ryu, the portfolio manager for PCRED, explains to *PERE Credit* why lending against US multifamily assets on reset valuations in an elevated rate environment provides a more favorable risk-adjusted return than investing in real estate equity in today's market.

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Q What are the key factors shaping US multifamily real estate markets?

We continue to see weakness in overbuilt markets. However, as new supply diminishes, those markets will demonstrate improving fundamentals, benefitting from continued demand and a structural housing shortage nationwide.

Newly delivered assets in overbuilt markets in the Sun Belt and assets acquired at peak valuations are contending with debt maturities and a refinancing gap compounded by higher rates.

Of the $3 trillion "maturity wall" there are roughly $1.2 trillion of multifamily mortgages maturing over the next five years. Under an "extend and pretend" paradigm, lenders have modified loan maturities, providing borrowers with additional time to arrange debt financings with the hope that rates will decline under what has been a persistent higher rate environment.

This has created a compelling opportunity to lend capital on good assets at lower valuations that are saddled with bad balance sheets.

Q Will we see more distressed situations emerging?

Although commercial and multifamily mortgage delinquency rates remain above pre-pandemic levels, we do not expect widespread distress to emanate outside of the office sector, particularly as debt capital markets remain liquid, lenders extend loan maturities and private credit managers continue to enter the space.

Debt fund managers whose strategies are propelled by securitizations have also witnessed rising delinquencies but as a cohort, they have been collapsing 2021-22 vintage CRE CLO securitizations at an increasing pace. With attractive spreads on bank warehouse financing lines available, managers are better able to work out troubled loans at better financing costs by calling CLOs that have been deleveraged since issuance.

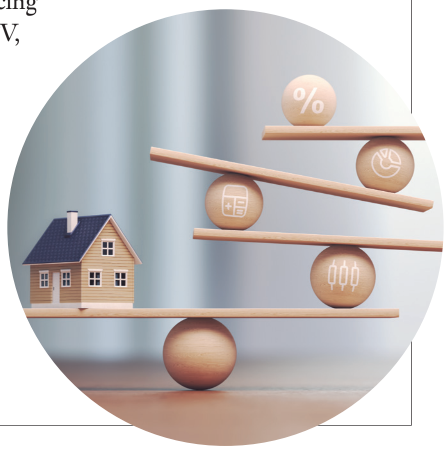
This has allowed bond investors to get repaid in full, serving to further buoy the strength and performance of the CLO market, bringing certain securitizations full cycle despite underperformance. Certain managers are left encumbered with the remaining transitional loans that are bridged to another bridge loan on a warehouse facility with the flexibility to allow borrowers more time to exit as underlying fundamentals slowly improve.

Q What financing options are available to borrowers?

The government-sponsored enterprises, Freddie Mac and Fannie Mae, continue to dominate the multifamily market, offering the most competitive low-cost, low-leverage senior mortgages for permanent, longer-term financings on stabilized assets. Many borrowers, however, don't qualify for GSE loans or require higher proceeds in the face of large refinancing gaps as GSEs are typically constrained to a 1.25x amortizing DSCR on in-place cashflows.

Life insurance companies, CMBS and banks can also provide competitive pricing on stabilized assets but banks continue to retrench from direct originations while expanding significantly into warehouse financing lines in the aftermath of the regional banking crisis. Alternative lenders have taken on market share, originating senior loans at higher detach points versus traditional permanent financing capital sources to address higher borrower financing requirements on transitional assets.

Targeting transitional senior financing opportunities up to 70-75 percent LTV, debt funds have rapidly grown to meet an increasing need in a market that is facing a proverbial wall of debt maturities in a higher rate environment. Debt funds typically originate senior whole loans utilizing leverage from a warehouse or repurchase facility or structure financings under a senior/mezz or senior/preferred equity approach to address borrower capital needs.



Q Where do you see the most attractive investment opportunity for alternative lenders?

The long-run fundamentals for the multifamily sector continue to be attractive and with $769 billion of loans maturing by 2027, alternative lenders will have a protracted opportunity to recapitalize multifamily assets facing financing shortfalls that cannot be solved by permanent debt capital providers.

The majority of the opportunities we evaluate today are refinancing requests, as acquisition activity remains depressed due to elevated borrowing, materials, labor and insurance costs.

Our current focus is on refinancings that satisfy our credit criteria. As investor confidence continues to grow through price discovery on rising transaction volumes, the opportunity set will expand to include acquisitions.

Focusing on 70-75 percent LTV financing opportunities enables us to generate attractive risk-adjusted returns compared to real estate equity.

Q What part of that opportunity are you targeting?

Our program is designed to provide additional leverage above permanent capital providers up to 70-75 percent on an as-is LTV basis, focusing on stabilized, cashflowing multifamily assets versus transitional or ground-up development opportunities. To execute on this strategy, our program is approved to issue preferred equity investments behind low-cost, low-leverage Freddie Mac senior loans with a robust package of mezzanine debt-like enforcement rights and remedies.

This allows us to issue an equivalent total financing solution compared to a senior debt fund that is often priced at a more attractive blended cost of capital. Utilizing Freddie Mac senior financing that is priced inside of debt fund warehouse financing rates allows our strategy to generate 13-14 percent IRRs on stabilized assets, which rival absolute returns on real estate equity strategies.

Furthermore, we can offer this financing at a fixed rate over five years,

> *"With $769 billion of loans maturing by 2027, alternative lenders will have a protracted opportunity to recapitalize multifamily assets"*

whereas debt funds typically offer three-year initial maturities on a floating rate basis, subject to rate floors in-place at closing. Although a three-year term may be sufficient for many business plans, extensions are typically tied to performance hurdles and additional fees.

Our approach therefore targets stabilized assets with minimal business plan execution risk and does not lean into credits higher up the risk spectrum such as lease-up and construction loans.

Our check sizes typically range between $5 million to $15 million, which allows us to pursue institutional quality assets that are often under the radar of larger debt funds. Targeting smaller check sizes allows us to be nimble and capitalize on opportunities that can also provide incremental return.

Q How do you manage downside risk when recapitalizing multifamily assets?

To manage downside risk, not only are we targeting cashflowing multifamily assets, but we are also focused on underwriting properties and borrowers that qualify for agency financing.

By originating preferred equity investments behind Freddie Mac senior loans, we are focusing on stabilized assets owned by qualified sponsors. We target well-located, post-2000 vintage assets, sponsored by operators with strong track records. From a risk standpoint, we are not exposed to sponsor lease-up, construction completion, development risk or meaningful deferred maintenance concerns.

We are very disciplined in our underwriting, using a conservative approach that incorporates a reset from peak property valuations. We rely upon in-place rents to ensure that today's cash flows are sufficient to pay us current and our exit is furthermore not reliant upon rent growth or capital appreciation for our investment to be redeemed in full.

Our comprehensive investment and asset management teams conduct thorough equity level due diligence as we are a traditional owner-operator of agency financed multifamily properties. Our lending parameters include a comprehensive set of mezzanine debt-like enforcement rights and remedies approved by Freddie Mac which include a change of control and a forced sale right upon a major default. Under a change of control, our team is positioned to take over control of the property, protect our investment and act as credit enhancement to Freddie Mac.

To date, we have been successful in executing on this strategy and providing attractive financing solutions to qualified borrowers seeking five-year financing from Freddie Mac with additional co-terminus preferred equity proceeds with a certainty of execution. Based on our successful track record as an agency borrower with no defaults and as a strong multifamily sponsor, we are proud of the fact that we have been able to get our preferred equity parameters approved by Freddie Mac which is core to our strategy as a credit investor.

Q How do you see the market landscape evolving over the course of this year and 2026?

With a record number of debt funds in the market, the landscape is highly competitive not only for raising capital but in the pursuit of investment opportunities on dollars raised. Although debt originations are up nearly 50 percent year-on-year in the first half of 2025, acquisitions volumes remain depressed, which has incited a healthy amount of competition.

Liquid capital markets continue to fuel CMBS and CRE CLO issuance which appear priced to near perfection, reflecting perhaps that markets are seeing through macroeconomic and tariff induced uncertainties, in a risk-on environment.

We believe that as more clarity emerges, the market will continue to gain confidence while underlying property-level dynamics improve over time. With continued capital markets momentum and resilience, sponsors will become motivated sellers and we will be able to deploy more capital to support acquisitions.

As we take advantage of the ongoing refinancing wave, we believe it is prudent to stay focused on our strategy, generating contractual equity-like returns on preferred equity investments behind low-cost permanent, agency financings. Given strong investor appetite in a market with heightened competition, it's important for credit managers to maintain discipline and focus on quality in the pursuit of yield. ■

Distribution payments are not guaranteed and may be modified at the program's discretion.

An investor should carefully consider the fees and expenses and other information found in the Confidential Private Placement Memorandum (PPM), including the “Risk Factors” section, before making an investment decision.

This investment is for Accredited Investors only and a PPM can be provided to those Accredited Investors upon request. The Internal Revenue Code of 1986, as amended, imposes numerous constraints on the operations of REITs that do not apply to other investment vehicles. Failure to comply with certain constraints could have a material adverse impact on the Fund. For example, if we fail to qualify as a REIT and no relief provisions apply, our NAV and cash available for distribution to our stockholders could materially decrease. Many competitors are not subject to the operating constraints associated with REIT compliance.

A number of factors may prevent each of the Fund’s investments from generating sufficient net cash flow or may adversely affect their value, or both. These factors include, but are not limited to, national economic conditions, regional and local economic conditions (which may be adversely impacted by plant closings, business layoffs, industry slow-downs, weather conditions, natural disasters, and other factors), local real estate conditions (such as over-supply of or insufficient demand), changing demographics, perceptions by prospective tenants of the convenience, services, safety, and attractiveness of a property, the ability of property managers to provide capable management and adequate maintenance, the quality of a property’s construction and design, increases in costs of maintenance, insurance, and operations (including energy costs and real estate taxes), changes in applicable laws or regulations (including tax laws, zoning laws, or building codes), potential environmental and other legal liabilities, potential instability, default or bankruptcy of tenants in the properties owned by PCRED, and the relative illiquidity of real estate investments in general.

PCRED has a limited operating history.

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