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Banks Collapse Affecting Mortgage Rates, VC, PropTech

Repercussions reverberate throughout CRE.

By Richard Berger | March 14, 2023 at 08:31 AM

A drop in home mortgage rates, a pause (or even cut) by the Federal Reserve at its March 22 meeting, and the need to obtain new letters of credit are among the matters to ponder as commercial real estate companies and venture-capital groups sort through **the fallout of the collapse of Silicon Valley Bank and Signature Bank.**

SVB has approximately $2.6 billion of CRE private bank loans on its books, according to **its latest 10-K filing** with the Securities and Exchange Commission.

At the end of 2022, **Signature had by far the larger portfolio at $35.7 billion**, according its 2022 annual report, including multifamily, commercial property, acquisition, development, and construction, and home equity lines of credit.

Institutional Investors to Look for Better CRE Opportunities

Brad Case, PhD, CFA, CAIA, chief economist & director of research for Middleburg Communities, tells GlobeSt.com that the collapse of Silicon Valley Bank "has upset" the Federal Reserve's plan for interest rate hikes to combat inflation, “but they’ll have to resume hikes when the short-term liquidity danger is past.

“We believe the fight against inflation will be won by the end of the summer, so we expect interest rates to start declining (from the anti-inflation peak) by the end of this year,” he said.

The stock market remains overvalued whereas real estate values have taken a hit even though NOI growth remains strong, according to Case.

“Because of that, we expect institutional investors to look for better opportunities in real estate, which should cause downward pressure on cap rates,” he said.

30-Year Mortgage Rates Could Fall

Al Otero, portfolio manager at Armada ETF Advisors, tells GlobeSt.com that the collapse of SVB coupled with reports over the weekend that the Fed will undertake a major policy shift to guard against the risk of contagion has put interest rate markets into a tailspin, causing a rally in rates across the yield curve and an expectation that the Fed will now pause raising the funds rate at its March 21-22 policy session.

“The implications are that we could see a material reduction in mortgage rates going into the spring sales season, which would be a substantial positive for the housing market,” Otero said.

Mortgage News Daily listed 30-year fixed rates at 6.57% on Monday afternoon.

This PropTech Got Out Last Week

Smart laundry operator Tumble, a start-up that serves the multifamily industry, was a Silicon Valley Bank customer before pulling its money out last week.

It has limited exposure, according to Scott Patterson, its CEO and founder.

“Tumble is in a strong position,” Patterson said. “We’ve had great support from our investors and our multifamily network, who all helped us move quickly. It was the right call to fully back depositors using the fund set up after the Global Financial Crisis (GFC) and I applaud the Fed and Federal Deposit Insurance Corporation (FDIC)’s fast action to protect depositors.

As a startup, it is common practice to diversify banks (mostly because of the variety of products offered) and this diversification worked well for Tumble in this situation, Patterson said.

As for the long-term effects of losing a partner in our ecosystem like SVB, Patterson said he would hope that a larger bank takes the opportunity to swoop up the talent, relationships, and risk profile that was the majority of SVB.

“One of the biggest takeaways is that money moves extremely quickly,” he said. “At the same time, panic magnified the consequences of last week’s events. Evaluating banks holistically, from interest rates to overall risk profile, will undoubtedly be at the forefront of every company’s strategy.”

VCs Must Rethink One-Bank Relationships

Liza Benson is a partner at Moderne Ventures, a strategic venture capital firm approaching $450 AUM with investments in technology for the real estate, finance, and insurance industries.

“It would be hard to find a venture capitalist without a portfolio company that was banked by SVB,” said Benson, who had a minority portion of its portfolio banked by SVB.

“The Fed’s actions over the weekend were a necessary step to prevent bank runs at regional and technology-focused banks that could have caused a contagion many times worse. We are grateful the government played the necessary role of insuring all deposits.”

Benson said all venture capital firms are rethinking having a portfolio with all cash at one bank.

“Many lending agreements with banks require you only have that one account; I believe we are going to see much more pushback on this covenant,” she said.

“We are certainly going to be entering a period of much more volatility and a flight to quality. At Moderne, we are going to continue to invest in the best technologies-focused companies around real estate.”

PropTech Will ‘Push On’

Rasheq Zarif, Co-Founder and COO of ReWyre, tells GlobeSt.com that SVB played an important role in supporting and catalyzing American innovation. “Many startups would not be where they are today without the support it provided,” Zarif said.

“Those who think this spells disaster for the proptech sector are mistaken – SVB is not the only ingredient to continued industry success. Proptech will push on, helped by a clear and growing need for more sustainability, as well as the digitization of outmoded processes and systems across the real estate lifecycle.”

‘This Too, Will Pass’

Some venture capital groups focused on proptech are mostly taking it in stride, saying it won’t have any significant impact.

Morris DeFeo, Chair of the Corporate Department with New York law firm Herrick, Feinstein, tells GlobeSt.com that the collapse of SVB, the second largest bank failure in the US, and one of the very few since the financial crisis of 2008, may affect access to liquidity for some tech companies for a limited time.

“However, it is very unlikely to cause any significant impact unless it were to spread to the banking industry much more broadly, which seems very unlikely,” DeFeo said. “Very few banks have concentrated risk exposure in the tech space, and fewer, if any, have anything comparable to SVB’s position.

“I have no doubt that shareholders and board members in some tech companies are reaching out to management with varying degrees of anxiety, but this too will pass.”

‘Imploring’ Them to Seek Secondary Banking Partners

Ryan Freedman, founder and general partner, at Alpaca VC, tells GlobeSt.com, “We don’t see any specific risks or exposures that apply only to proptech startups – the regional banking crisis is going to apply to all US venture-backed startups.

“We are working with our founders to ensure that they can meet their payroll and other near-term cash requirements while also imploring them to seek a strategic secondary banking partner.”

Freedman said that the future of commercial banking will not look the same.

"Bank balances will be reserved for working capital and cash will be managed with proper treasury management made up of custodial money markets, treasuries, and short-term paper," he said. "This competency is typically not thought of in earlier stage companies, but it will become a core operational process for all companies going forward."

Must Get New Letters of Credit

Tony Natsis, name partner of Allen Matkins; and chair of the global real estate group tells GlobeSt.com that many of the smaller tech tenants – probably not including the mega tenants and FAANG tenants – and many of the smaller life science tenants – probably not including the mega life science tenants – use SVB as their primary bank in terms of deposits, lines of credit, and letters of credit.

"As such, the freezing of those deposits and instruments by the FDIC, and the possibility that the FDIC will not honor lines of credit and letters of credit (although they announced last night that they would honor deposits) has put those entities in the very awkward situation that they may not be able to make payroll and that their letters of credit that they issued in connection with lease transactions for the benefit of the landlords may no longer be valid," Natsis said.

"And they will have to replace those letters of credit with letters of credit from a new banking relationship, which would require additional liquid collateral that they may or may not have.

"So, it's a significant problem on an operational basis and on a leasing and occupancy basis for those entities."

Might Be No Liquidity to Pay Rent

Natsis said that this will also further impact landlords because there may be no liquidity for those entities to pay base rent.

"That may then trigger a landlord's lender to get involved in the immediate cash flow of a particular building and also cause a loan default at the same time because the landlord is unable to pay debt service," he said. "So, a lot of undesirable results could occur for tenants, tenants' employees, landlords, and lenders."

Natsis said that "undoubtedly," such companies will seek to bank with more traditional mega banks that stand an almost non-existent chance of failure because of their banking philosophy and platform and because the FDIC would never take them over because it would have a massively profound effect on the US economy in many ways.

"Also, landlords and their lenders will, undoubtedly, not accept letters of credit from banks that they cannot underwrite very closely and/or are not megabanks," Natsis said.

Proptech Companies Will 'Move Faster to Profitability'

Chad Gallagher, Co-Founder and Chief Investment & Growth Officer at Home365, tells GlobeSt.com, "The SVB collapse impact for proptech companies was muted when the Fed jumped in to secure ALL deposits. Before that announcement, there would have been an impact to the entire tech ecosystem including proptech companies as much-needed cash would have vanished and the major VC funds would provide cash to fund these Prop Tech companies have taken a major hit.

“Given the Fed jumped in to secure all deposits (both under and over $250,000), we would expect little to no impact on the PropTech community overall.”

Taking aside the SVB collapse, Gallagher said he believes proptech companies will move faster toward profitability and make fewer bets on loss-generating activities.

“Profitability is not a bad thing though; it ultimately makes the ecosystem more secure for the long-term,” he said.

Greater Reliance on Relationships

Mike Sroka, CEO & Co-Founder of Dealpath, tells GlobeSt.com that Silicon Valley Bank’s collapse has put a spotlight on the potential exposure of investing in short-term deposits in longer-term, fixed-rate assets and how bank runs can also happen at digital speed and scale.

“It serves as a strong reminder of the high value of working with vendors who are well capitalized, backed by industry leaders, with trusted and diversified banking partners, and who have positive momentum in the business,” Sroka said.

Regional Banks Play a Critical Role

Bobby Magnano, president, financial services, JLL, tells GlobeSt.com that JLL continues to study any implications it will have on commercial real estate and the wider financial services industry.

“As we turn to establish business continuity in support of our clients amidst this disruption, we are mindful of the customers and small businesses across the country that have been affected by the events this week,” Magnano said.

“Despite the current volatility, regional banks play an incredibly important role in strengthening our economy by offering diversity and value to customers in addition to providing access to lending for smaller businesses. We hope that the systems in place work to contain the situation and provide solutions moving forward. We will provide updates as this continues to unfold.”