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# 3 Keys to a Hole in One

Honesty, creativity and understanding often get golf course loans on the green

**L**ike many specialized asset classes, the market for golf course properties seems poised for an additional shake-up. Mortgage brokers must be prepared to navigate the next 12 to 18 months to help their golf-course-owner clients secure debt.

Similar to the challenges in other niche classes such as retail and hospitality, the golf course segment faces decreased liquidity, greater-than-normal default ratios, a multitude of loans with five-year maturities simultaneously coming due and decreasing participation of specialized lenders.

Like other small categories, the golf course market has trended downward in the past four years. In 2005, about \$3.6 billion of golf-related investment was financed, according to the World Golf Foundation. This decreased substantially in 2007, dropped to a minimal figure in 2008 and only rebounded slightly in 2009.

In the past 24 months, participation in this asset class has constricted. Major lenders have stepped back and no longer make loans to daily-fee, semiprivate and private golf courses.

Traditionally, regional and national banks have looked at this asset class with a slanted perspective. Many banks view golf courses as collateral assets that serve only to support residential-subdivision sales. They place little merit on historical cash flow and operations.

Now, regardless of how good a loan may appear, many banks already have their hands full with distressed assets and have little reason to seriously consider a golf course loan. In other cases, banks may have limited experience dealing with golf as a cash-flowing retail business and do not understand the business's revenue streams and debt requirements.

Compounding the situation, many course-owners now find themselves classified as distressed-asset owners. Often, this is because they are overleveraged, their original loans were granted at higher loan-to-value (LTV) levels than today's limits or they have experienced a significant revenue decline.

Despite the challenges, there are three key elements that mortgage brokers can consider to position a golf course property to a lender today.

## 1. Be honest

First, provide your borrowers with a realistic perspective of today's market, its capital limitations and its requirements. Course-owners should be prepared to demonstrate that their operation generates positive cash flow, can meet the debt-service coverage, is in a viable market geographically and demographically, and can continue positive operating revenue.

Honestly represent the course and its ownership to a lender, as well. A lender must feel confident that it is seeing real borrowers who can commit. Continuously shopping unrealistic deals is the equivalent of crying wolf, and you risk destroying your credibility with lenders.

## 2. Think creatively

In today's market, brokers must present potential deals to lenders in a realistic light. If a golf course owner's financials appear marginal, you can actively pursue other ways to help your client meet a lender's cash and debt-service requirements before presenting the deal.

Principal lenders are no longer interested in holding quantities of collateral, and they will appreciate prior risk reduction. Alternative-financing options include subordinated

mezzanine lending; finding other additional equity capital; presenting a third-party letter of credit for debt-service support; or developing a special, tax-exempt mortgage security.

Mezzanine financing fills the gap between the senior loan and the property's equity. It often takes the form of a second mortgage. But even in mezzanine financing, a golf course owner may find more-creative options. One could include structuring the agreement as an equity arrangement, with the new, outside investor receiving stock or interests that provide an immediate lower return but a potentially larger future return.

Other viable sources of capital include private-equity funds, institutional and individual investors, and hedge funds. In many cases, brokers themselves are the best source of information about alternative financiers seeking investment opportunities and can direct course-owners toward potential sources.

A third-party letter of credit can be an affordable option if a family member or friend agrees to loan them money. The letter may be written as an "evergreen" agreement that will continuously renew until a lender's specified debt-service coverage is met.

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More common in the housing segment, special tax-exempt mortgage securities or bonds also may be an option for golf course owners. These private-activity bonds are revenue bonds, with the course-owner repaying the investor in amounts sufficient to meet the debt-service requirement. Although this is more expensive to structure, it may enhance the property's equity in the long term. You can investigate potential investors through hedge funds or specialized lenders.

Help your clients investigate any strategy they can use to ensure they can meet a principal lender's debt-service-coverage requirement thoroughly and put it in standby mode before presenting a deal.

### 3. Manage expectations

It is likely that loan structures and property-valuation methods have changed since your course-owner client last financed. Advise your clients of the asset class's new nuances and the constraints they will face.

It is important that they understand that LTV requirements have changed. Lenders no longer make loans to golf course owners at 75-percent to 80-percent LTVs. They may require 60-percent to 70-percent LTVs, at best.

In addition, the principal lender's appraiser typically will do the property valuation. Most national lenders will not accept an appraisal prepared for a borrower or a self-generated evaluation. To manage your borrower's expectations, contact a recognized appraiser in the field to get a valuation estimate before presenting the deal to a lender.

Finally, advise your clients to focus on rates, not spreads. It is true that everyone talks about spreads getting wider, but it is the rate that is important. In fact, rates are similar to what they were for this asset class 48 months ago.

A specialized lender tends to maintain consistency in terms, rates and spreads. Lenders may consider loans to golf course owners with less-than-perfect credentials,

but borrowers should be braced to accept an incremental rate to offset the loan's risk.

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Across many specialized asset classes, including the golf course segment, lenders recently have seen an inordinate number of prospective loans that realistically will never close. Brokers working with golf course properties can take pre-emptive, positive steps to overcome marginal deals' shortcomings before presenting them to a lender.

Despite the predicted limited liquidity in the capital markets, tough competition for financing and prevalence of distressed assets, good deals can still get made and the business of golf will continue as a viable asset class. Understanding the asset class can be simple if you approach it like any other real estate-based business. If the course location is good, is in a stable market with limited competition and has a good operating history, the loan likely will close. ●