Flushing Financial Services Corporation NYC Real Estate Market Update with Francis ("Frank") Korzekwinski and D.A. Davidson Analyst Christopher Keith

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PRESENTATION

Chris Keith
Hello everyone, this is Chris Keith. I am the Northeast analyst with DA Davidson. I apologize for the delay and the lack of video, I was having some IT issues, but we're ready to get rolling now. So thank you all for taking the time to attend this event with CRE and multifamily expert, Frank Korzekwinski, who is the Head of Real Estate Lending at Flushing Financial, which is an over $8 billion asset bank headquartered in Uniondale, New York. And Frank, thank you very much for offering us your time and expertise in a very important subject matter. We appreciate your time.

Frank Korzekwinski
Thank you, Chris. Glad to be here.

Chris Keith
Great, and then for those attending, there should be an option on your screen to submit a question if you would like, which would then be forwarded to us. So let's go ahead and get things started. Let's start with an overview of Flushing Bank. And Frank, can you describe to us Flushing Bank in its primary lending activities?

Frank Korzekwinski
Sure, I'll give you a little bit of history of the company first. Flushing is a full service Community Bank that's been serving the metropolitan area since 1929. The majority of our real estate portfolio is focused in our primary market. As many of you may know, we serve…we have actually some of the most valuable real estate in the country right here in the New York area. We're focused primarily on the commercial real estate market, which we believe provides the economic engines for the neighborhoods we serve. Our focus is primarily on a local investor, these investors are generally multi-generational, and in the game for the long haul. With such a large market opportunity here, we're able to diversify our loan portfolio across a broad based asset class. We also do provide critical financing for non-traditional one to four family owner occupied investor real estate. We've developed a reputation as a true niche lender that enables us to consider investment opportunities that are other institutions in our focus. As we see competition, accelerating and pricing margins narrowing, we seek to move into different asset classes. Our size and our expertise allows' us to react timely to our customers' needs.

Chris Keith
Very good, Frank, I appreciate that overview. And so, what is the current makeup of your existing loan portfolio?

Frank Korzekwinski
Again, as I mentioned earlier, commercial real estate is our primary focus, it accounts about $4.2 billion of our loan book, multifamily accounts approximately $2.5 billion and non-owner occupied commercial real estate for about $1.7 billion. Multifamily has been a core book since the early 1990s. Again, we focus on multifamily property owners that have multiple properties under management in and around the metropolitan area. Again, our borrowers tend to be multi generational operators they value relationship lending and full banking services. We also find that many of our customers on other forms of real estate primarily non owner occupied commercial real estate in and around the metropolitan area. We book loans ranging from $500,000 to excess of $10 million.

On the smaller end, we focus on the mixed-use residential real estate in and around the five boroughs of New York City is a predominantly small balance loans. This market is somewhat unique to the New York region and has a very strong investor base. Yields are less competitive, rates on these type of transactions can be as much as 50 basis points higher than traditional multifamily, who's earned over the years that the mixed use market place has been very successful. We have relatively low historically lost [ph] content. It's a great introductory market for us to build relationships for customers in the future, as this market generally is a introduction to building multifamily and commercial real estate portfolios, and enables us to follow these investors as they begin to grow their portfolio.

We also have a very strong presence in the non-owner occupied commercial real estate market, focusing on shopping centers, medical office buildings and other mixed-use commercial properties. Typically, the properties we focus on are located in densely populated markets with traditional vibrant economic activity. Commercial real estate serves the vital source of economic engines of all the communities that we service. The loan transactions that we focus on generally have proven cash flow and the properties themselves are generally located in zones of favorable zoning uses that allow borrowers flexibility in operating their properties.

Chris Keith
Got it. And, I guess, are you planning any significant changes in that loan portfolio?

Frank Korzekwinski
We found that our lending strategies have proven to be very successful in the long term. We believe that maintaining a diverse loan portfolio is our best approach. Real estate is also a very solid form of collateral, it's not portable, and generally we change value over time. Again, I am getting back to the cash flows on these particular properties. We focus on the cash flow intently. We find that the cash flows tend to be steady and predictable. Our preference is to remain focused on the multifamily housing market, particularly to continue to focus on various types of collateral that are essential to the communities that we serve.

Chris Keith
Got it. That was a great overview, Frank. I appreciate that. And, I'd be remiss if we didn't touch on some COVID related topics. So clearly we know that the onset of COVID-19 was an unprecedented event for all Community Banks, and I just…could you talk to us a bit about how the onset affected Flushing Bank specifically and what your firm did to address customer needs?

Frank Korzekwinski
Certainly, I would say it was a very, very difficult time and all the years I have been lending, obviously I have seen nothing like it. Like many institutions, we were faced with an environment that was extremely challenging obviously the immediate future seemed to be unknown. Our focus was on immediately developing a strategy that would enable our workforce to work remotely. We did a great job with our technology team providing access to the systems in a relatively seamless fashion. We are able to get our workforce working remotely almost instantly, obviously it was doing enormous task, very short window to complete it in. Once we've gotten our technologies set up, we began a triage program focusing on the segments of our portfolio that we felt, were mostly affected and more immediately from the terms of the lockdown.

We took an approach that set aside a team of experienced lenders, we put on a new team, called special asset servicing. This team was to address the additional requests for assistance. We also had another team of individuals that's been with us for a long period of time in our portfolio management group. They were engaged in developing a protocol to review any request for assistance, prepare approval documentation, prepare the necessary agreements, following up on the agreements, coordinating any system changes and developing a tracking system to monitor the loans as they progress through the relief. Our SAS team was engaged with customers returning to regularly scheduled loan terms that to help any…with any subsequent request for assistance.

Some of the plan was more complicated than others. But as plans began to expire, borrowers were required to commit up to date financial information; they were requested to send us rent roles, bank statements, evidence of any amended lease terms, and any other items that we felt appropriate to get a handle on how things were progressing through the pandemic. Initially, we thought the scenario we were facing with the pandemic was going to be relatively short term, we came out of the box with lease terms of about 90 days, as the volume of the request accelerated and lockdown was extended. We began granting relief for up to 180 days. This seemed to be appropriate, because we weren't really sure how long the economy would be under a full lockdown. But clearly, 90 days was not going to be enough in the initial phases. We also found that the added relief proved to be very successful to our borrowers, as they were able to accumulate substantial operating cash from the income collected during the assistance period, thus enabling an overwhelming majority of our customers to return to regularly scheduled payments and sustained payments throughout the winter months.

Chris Keith
That's great. And so, Frank, you've touched on it a little bit. But how do you feel the company is progressing now through the recovery?

Frank Korzekwinski
Well, it's certainly a long way from March 2020. We've seen some tremendous success and the recovery continues to accelerate. We've had a successful campaign is less than $10 million of our loans that we've granted assistance to migrate it to nonaccrual, while only recording a minimal loss provision approximately $100,000. All loans that remain on assistance are making payments according to their approved plans. I'm happy to say our delinquency ratios have stabilized and returned closer to the pre-pandemic levels. We've had numerous conversations with our customers over the past year or so. And we've been encouraged by the reports that have been given with respect to the collections activity. And this has taken place across all asset classes. I think the hotel sector is definitely one of the soft spots in the market. However, the loosening of restrictions have started to bring back some critical events, mainly entertainment events and local travel is beginning to increase. Within the hotel market, the occupancy levels have improved considerably since the dark days of the pandemic. However, we're seeing the average daily rates remaining soft. Our hotel portfolio is largely concentrated outside Manhattan in and around the five boroughs of New York City. It has an ethnic focus, it's less dependent on business and international travel, and a somewhat community base. All of our hotel loans that remain on relief are paying current interest charges. All hotels are now open for business have been doing that for some time now. So overall, we've seen a very nice recovery from the dark days of April 2020.

Chris Keith
That's great, Frank, I appreciate that description. And I just want to briefly remind all the attendees that if you have a question that you'd like to flip in, feel free to click that button that should be on your screen to submit a question and it will be forwarded to us. So Frank, with all that said, are there any lending activities that you see recovering sooner rather than later?

Frank Korzekwinski
Well, certainly, you know, multifamily has had a tremendous recovery from the darkest days back in April and May of 2020. Significant progress has been made in a collections activity.

Vacancy rates have improved considerably. Manhattan has been a little bit of a challenge. We quite honestly saw as renters left Manhattan, they saw larger spaces in the outer boroughs and in the suburbs. The suburbs in the outer boroughs were already experiencing very low vacancy rates. This certainly has pushed the envelope a bit in terms of finding housing as people began to move out of the city. Particularly in the outer boroughs, and in the suburbs, there's little supply in terms of rental apartments, so that's kind of pushed up rents outside of Manhattan. More recently, we've been seeing some improvements in Manhattan; certain sections continue to experience higher levels of vacancies. These apartments are generally outside of the rent regulated environment and are considered free market rents.

In that particular marketplace, we continue to see leasing incentives being offered in order to bring people back into the city. These incentives can be, as much as, two months of free rent during the two year lease. However, that being said more recently, we're seeing a lot more leasing activity, and possibly a move away from any additional incentives. There are a various number of sub markets within the five boroughs of New York City, some are dependent on student housing, and also apartment shares. Student housing and apartment have seem to be having a little bit higher elevated levels of vacancies as compared to the rent stabilized and affordable housing market. Overall, we expect the rental housing market to continue to improve especially since the price of homes in the surrounding areas beginning to accelerate.

One key thing to note is Flushing Bank does not have any significant exposure to free market rentals. We focused on lending initiatives on affordable housing in and around the metropolitan avenue…metropolitan area. We estimate our current average rental portfolio to be somewhere around $1300 a month, versus free market rents closer to somewhere around $2,800 a month. So we've got a nice comfort zone in there. We're not expecting to see any declines in rents in the rent stabilized and affordable housing market.

Local retail is actually starting to see a very steady recovery as well. The economy is now open, malls and other large type facilities are struggling a little bit. That's largely due to the lock downs and restricted activities that we've experienced over the year...over the year or so. Larger franchise type operations really had a difficulty or difficult time reopening once the restrictions are beginning to be loosened. We also found that local store owners and providers proved to be resilient in finding ways to comply with the myriad of new rules related to operating in a COVID-19 environment. For these types of businesses, the initial startup costs were considerably less than larger franchises. We now see restaurants and bars being very active. During this period of time, we also found that landlords were willing to work with the operators in the stores and these offices, especially those that had proven track records. They often amended lease terms, granted concessions, and made additional accommodations to keep people in your space.

Overall, I have to say leasing activity is definitely increased. Entertainment venues including, as I mentioned earlier, bars and restaurants are now open and serving our less restricted basis. We see a tremendous pent up demand for social activity. People are gaining confidence in socializing, particularly as the vaccination process continues to improve and expand. We expect this market to improve at a more moderate pace than the multifamily and other non-owner occupied commercial real estate. So all in, I think, you know, particularly in the last 60 days or so, New York has taken on a different spin. People are out and about enjoying themselves, the weather is nice. Things are definitely looking up and forward.

Chris Keith

Yes, I think that that's a good segway, then Frank to get into some more specific market discussions. I'd like to start, particularly with multifamily. You've touched on it a bit. But can you tell us some more about what your outlook is on the New York City metro area as it fully opens. And as you've already stated that some of the activity has begun to return. But as it gets to full activity and a more kind of normal level what your outlook is for the New York City area?

Frank Korzekwinski
Well, the weather's nice as it's been the last couple days. It's looking very good. As I mentioned to you earlier, there's a pent up demand for entertainment, travel socialization. We've seen increased vaccination levels and if you combine that with the strong economic support that we've received from our government over the past year, we expect the economic activity to continue to improve. Particularly exciting is the return to work, which has begun to take place all around New York City in Manhattan. We're starting to see Midtown Manhattan fill up a bit, with all of the callback to work, we do expect people to be moving back into the city sooner than later. We also expect that the residential vacancy rates will begin to decline. And more appropriately, we expect a beginning of a positive absorption of smaller vacant retail spaces located throughout the metropolitan area.

Chris Keith
Got it? And so, I guess, what can you say about the current state of multifamily real estate in the market?

Frank Korzekwinski
So the markets been quiet, it's been that way, obviously, since the pandemic took hold, I guess a lot of investors have just been trying to hunker down and figure out what they need to do to survive through the pandemic. But overall, the market has steadily improved. Multifamily really started to come back alive probably sometime, September/October last year. Sales have been slow, but we're starting to see deals that will put together at about the height of the pandemic or just before it come back onto the market. Investors are coming back into the market, they're looking for deals, they're moving a little bit slow right now, but everybody seems to be out and about looking for something to do. One of the challenges that we face is there's little or no supply on the market. This is a product of a few things, owners right now are not willing to sell in a market that they may think is unstable. We've seen a tremendous appreciation in the last few years, and I don't think anyone is looking to, to sell anything less than the maximum price that they can achieve. A lot of the owners are multigenerational as I mentioned before, they feel that they have very stable projects. They've gotten through some very tough times in the past year. Things are beginning to look up. So, I guess, they're really more focused on any potential fallout in the market that may be coming as a result of any operators who may not have been able to survive through the pandemic. Many of them are actually looking for new deals. We're pretty excited about that. One of the other things that have really come to life recently is development. Obviously, with all the protocols with COVID-19 early on and through the latter half of 2020 a lot of projects were sideline, in the past six months or so these projects have come back online. They're active, and [indiscernible] everywhere, I'd be looking through the city, all five boroughs, a lot of development, we're pretty excited about that.

Chris Keith
And so then…so with all that said, what's your best guess on how long it'll take for the multifamily market to return to a more kind of normal environment?

Frank Korzekwinski
Very difficult question to answer. However, there's a couple different dynamics going on. One that we talked earlier is the affordable and right regulating housing market, that's doing fine. There's a tremendous shortage of space in the affordable housing market. However, I would expect over the next 18 months or so that we'll continue to see positive trends across the board. Obviously, unless there's a little bit of a rebound in the virus and any further restrictions are reintroduced. It seems that everybody's looking forward and looking ahead to try and get some deals moving. The free market environment that may take a little bit of time for us to recover from. My guess is over the next 18 months that will probably move along at a slower pace than the affordable housing market. And part of that has to do with the number of units that will be coming online, particularly in Long Island City and some areas like that. But overall, I think we're on good footing. And business is definitely starting to pick up.

Chris Keith
Great. And then what are you seeing with respect to rent collections today?

Frank Korzekwinski
Well, I'll tell you, with the eight of our special asset servicing team, we've been able to get some really good insights as to how the loan portfolio has been performing. We've also noticed that rent collections have improved considerably, I guess, when we first started back in April and March of 2020, there was a fear that no one was paying. But we actually found out that wasn't true. When we analyzed the rent collection reports and bank statements, we see that payments did continue even through the dark days. In order to keep things going many of our operators, in fact, probably all of them demonstrated a willingness to work with your tenants. Right now, we're seeing as many of our operators reporting rent collections in excess of 90%. Obviously, depending on the rent levels, particularly in a free market, there may be some concessions tied to keeping people in and working out any delinquencies. But overall, we're pretty excited about the rebound that we've been seeing.

Chris Keith
And then on the other hand, what level of vacancies are you seeing in the multifamily market?

Frank Korzekwinski
Again, it's a little bit all over the board, the most stable being the affordable housing marketplace, that probably is in the low 5% range. For the free market, we're seeing vacancies could be as much as 10% to 15%. Obviously, the 15% would be on the higher end of the market, new developments coming aligned or leasing up at a little bit of a slower pace. And obviously location is a little bit of a factor. And what I mean by that is, if you're serving…if you are building a building that was serving a particular niche, maybe a student housing or something like that, they're coming back a little bit slower. We do have some openings occurring here in New York City with some universities that are bringing students back into Manhattan for education now. I guess, they're beginning to line up there, their residences for the…for semester, but there is a bit of a supply in that market. So that might take a little bit of time to come back.

Chris Keith
Got it. And so, Frank, have you noticed any significant changes in investment activity?
Frank Korzekwinski

So again, as I mentioned earlier, we're seeing a pickup, particularly in the investors seeking new transactions. We've seen a number of portfolios begin to train to trade hands. Most of the slowdown obviously was due to the lockdown. So businesses over the past 11 months or so, borrowers focusing on managing their own affairs, and obviously as things looked a little bit rough, there really is no supply on the market, which actually brings a little bit of a calmness into the environment. Again, the people we speak to, they seem to have an appetite to look at new deals and are expressing desire to proceed on new deals. However, they are looking to proceed with caution.

Chris Keith
So then, with that said, what kind of impact or where do you see cap rates for multifamily properties heading in the near future?

Frank Korzekwinski
That's a good question and a tricky one. I can just tell you that the general trend that we're seeing in the appraisal report function is an upward movement. Appraisers have been making adjustments and cap rates that associated with many of the unknown effects of the pandemic. These adjustments are trying to account for any unknown loss of rent in the near future and any general lack of closed sales activities in the last six to nine months. Cap rates we've seen have ranged from a low 4.75 to, as much as, 5.5, and in some cases higher depending on the transaction of the cash flow location and things like that. We've seen some clean deals come in with verifiable rent streams, they would come in probably at the lower end of the market somewhere below 4.75, but for 4.75 to 5.5 is about what we're seeing. My guess is, if the effects of the pandemics subsides a little bit more and a few more transactions begin to occur, we might see a slight reduction in the cap rates moving forward.

Chris Keith
Got it? And then Frank, could you maybe give us some color around the foreclosure and eviction proceedings, maybe a bit of an outlook and where do you see that heading in your market?

Frank Korzekwinski
Sure. Well, that's the talk of the town these days. Obviously, the pandemic brought about an unusual concern for residential evictions and foreclosures. As it appears today, some of these concerns probably have gotten ahead of itself. While the initial outlook was grim and a moratorium appear to be warranted as it appears that landlords have done a really good job of working with the tenants to keep them in place. We still have some moratoriums here in Northeast with respect to evictions and foreclosures. We have looked at it a little bit differently, and have seen a tremendous amount of success on a part of our borrowers and tenants [ph] to keep people in place. We also noticed that the various stimulus programs added much needed liquidity and assistance, allowing many of the residential tenants and property owners to make payments of some level throughout the pandemic. More recently, we're seeing the unemployment begin to decline. We have some additional relief on the way to landlords, that money will be coming over the next 60 to 90 days or so, that should help residents catch up on past rent. Here in New York, we're optimistic that they'll put together some sort of plan to begin to unwind this moratorium sometime in the near future. One of the unusual statistics that we've located recently deals with the evictions in the greater metropolitan area that were filed prior to the pandemic, as recently as 2019, 93% of all eviction cases handled in New York, did not end up with an eviction being issued an eviction warrant being issued. So I think that's speaks well for the prospects of coming up with a plan to unwind the current eviction moratorium.
Chris Keith

Great. Thank you, Frank. I appreciate that overview of multifamily. I'd like to transition over to just traditional CRE. The first question I have is, what types of non-owner occupied commercial real estate properties, does Flushing Finance?

Frank Korzekwinski
We have a pretty broad based book of business. We really as I mentioned earlier focus on all of the essential services that are critical to the neighborhoods we serve. We have a nice presence in local shopping centers and strip centers. These generally have some sort of supermarket or food service theme to them. We have a nice little presence in medical office space. We have a very strong general commercial mixed use portfolio, dealing with all sorts of businesses located through the five boroughs of New York City. We have a little bit of a school portfolio doing very well facilities that are net leased by New York City school systems. We also do a little bit in the light industrial area, those properties become particularly valuable as residential developments taken off a lot of the remaining swath of industrial land in the metropolitan area.

Chris Keith
Got it. And from your perspective, how has COVID-19 affected the retail markets?

Frank Korzekwinski
Well, initially it was a severe disruption. Obviously, businesses were closed during the lockdown. They were closed for extended period of time. In many cases, some of these stores and offices were closed permanently. As things began to open up, the businesses were permitted to reopen. And the landlords and the property owners really work closely with each other to restructure leases and preserve businesses. We also learned that there was a core retail sector that really was not so internet sensitive. These were local services, such as salon supermarkets, small and large supermarkets, pet stores, medical services, and any…to some extent any kind of food service. Obviously, as soon as, the restrictions were loosened up, these stores opened up immediately, we sent some people out around the marketplace to walk through all the boroughs of New York City. And we've noticed that the small stores rebounded very, very quickly, it really didn't have very large staffs, the cost to re-operate was not that significant. That was a real, real nice bounce back in a dark day.

Our portfolio is centered around, what we call central business districts, where people frequently travel and meet, much of the portfolio is service related. We have no exposure to big box retail or enclosed malls. Again, the slower…the smaller businesses have much lower startup costs, and we're very adept at operating under pretty complex COVID restrictions. The rents in a typical Flushing project were generally below market pre pandemic. And this actually provided a strong incentive for the businesses and stores to work with their landlords to stay in their leases.

Chris Keith
That's helpful, Frank. I appreciate it. And then, what about the impact on the office market?

Frank Korzekwinski
The office market is just been an interesting aspect for us to focus on. I think it's a little bit early to tell what the long range outlook for the market is. Clearly, there's some skepticism, about the need for office space in the long term. What we find out is not every business or sector of a business can operate efficiently from a remote environment. Obviously, the cost advantage of operating remotely can be significant. We've been fortunate as there's been a trend of movement away from Manhattan into the outer boroughs, as well as, suburb for smaller office space. Our particular office portfolio is largely outside of Manhattan and includes a significant portion dedicated to medical space. Again, leases are generally long term, and they were at

below market rents pre-pandemic. Our projects are typically lower in size, not only dollar limit, but also square footage. We haven't seen any significant turnover at this point. But again, as I mentioned, these leases are long term.

Chris Keith
Right? And then what about cap rates, have you noticed any significant increases in the recent past?

Frank Korzekwinski
Again, like multifamily cap rates across the board are moving up, probably in the office building a little faster than multifamily. I think there's a lot more skepticism as to what the future of that market is going to be. It's really not uncommon for us to see transactions coming in about 5.5%, sometimes higher depending on the collateral. Again, sales activity remains low. Part of it is due to the pandemic and part is due to the uncertainty on the economy, and is also significantly less inventory on the market.

Chris Keith
And then is any one market affected more than the other?

Frank Korzekwinski
Well, I think the most challenging is probably the hotel in the entertainment travel related properties. Until recently they've remained challenged and likely to remain that way until the pandemic, environment fades, and the economy continues to show signs of recovery and strain. Other than that, I think things have moved along rather nicely.

Chris Keith
That's great. That was a great overview of both multifamily and commercial real estate Frank. I appreciate it. And I'd like to get in a little bit to kind of the business development for Flushing specifically. I mean, how does your organization develop new business?

Frank Korzekwinski
Sure. I just like to go back one step a little bit to talk about the hotel. In our portfolio in hotel industry is concentrated outside of Manhattan it's really a market that's unrelated to international travel and things like that. We're happy to report that all the hotels are moving forward and making payments according to their agreed upon plans. But having said that, I'm moving to the business development. We have, again, a nice book of business and a rather unique strategy. We have a team of individuals that work in what we call a residential mixed use team. This team focuses on smaller properties. They're generally multifamily residential properties, with some type of store two on the first floor and a few apartments above. We also work on owner occupied one to four family loans. We're very active for listening originations through our branch network and through a network of mortgage brokers that we've been working with for nearly 30 years. Approximately 30%-35% of our loans come from direct originations.

Our commercial real estate lending team is also a little bit unique. It's a team of lenders that focus on all asset classes, including multifamily and non-owner occupied commercial real estate. Loan relationships are deposit oriented and require full banking relationships. We do direct solicitations, and we also participate in the mortgage brokerage market. We're probably getting about 30% of our business right now direct from our own efforts. We are working closely with property owners, accountants, attorneys and any other centers of influence including managing agents of commercial real estate.

One other item that we have that's a little bit unique that helps us really stand out in the market is our team of professional bankers. Our lenders spend all their time developing the loan side of the transaction. Professional bankers are responsible for maintaining full service banking relationships for all real estate customers. They open new accounts, they solicit new business, they set up online banking, and mobile banking applications, and they provide full support when needed.

Chris Keith
So that's great Frank. I appreciate that description. And, we've talked a little bit about some of the markets that you serve. Are there any other particular niche markets that Flushing works with?

Frank Korzekwinski
I'm sure, we are generally known as a true niche lender here in New York, we work with a wide breadth of property types. We finance and attract loans that are what we call risk adjusted returns. We can handle appropriate risk adjusted returns. We provide financing for a six unit building. We can do a garden apartment complex, a walk up building, an elevated building. As well as, various types of commercial real estate. We find that landlords that we deal with often have diversified loan properties in their portfolio requiring various types of financing. We do our best to meet their needs across the board. We have an experienced team of lenders that have the ability to follow borrowers in any markets in the metropolitan area. So whatever it is, they're looking for, we generally find a way to accommodate them.

Chris Keith
Okay, and then before Frank, you mentioned that you have separate teams that that concentrate on lending, and then separately the full relationship and I think kind of deposit gathering. So you know, what types of deposits do you require from your borrowers?

Frank Korzekwinski
Well, our main focus obviously, would be the operating accounts. These buildings [ph] generally have predictable cash flows. So it's a very, very desirable account, we open those in the non-interest bearing DDA format. We also require at least security accounts that they remain on deposit here at Flushing through life alone. A professional bank is also routinely calling borrowers to discuss other core deposit opportunities. We have the ability with our professional bankers to provide remote capture services and mobile banking services to our customers. So while we may be based in Uniondale and have branches throughout the five boroughs of New York City, if you're operating in Northern Westchester County, we can service your accounts through either remote deposit or mobile banking. We do a lot of calling into these relationships, which often leads to new loans, as well as, new accounts.

Chris Keith
And then how do you remain competitive in your marketplace, Frank?

Frank Korzekwinski
Well, I'll tell you what I find all the years of working in this particular business, the primary driver has been the ability to serve your customers throughout this…throughout difficult times without disruptions. And we've done it in the early 90s. We've done it through the crisis of 9/11, through the great recession, and more recently through the pandemic. We've continued to produce loans and open new accounts during these very tumultuous times. Some of our competitors were either sidelined or not necessarily focused at that point in the market. So we've really done a great job of taking advantage of disruptions in the market. We also closed loans on many different types of properties, including retail, multifamily and a small mixed use.

We really feel that this is giving us the chance to demonstrate our commitment to our customers over the years.

Chris Keith
Yes, that that makes sense. I guess, turning over to the growth in the marketplace, what is your outlook in the intermediate term?

Frank Korzekwinski
We're very pleased to see the return of activity in recent months competitions become very active very quickly. There is a tremendous demand for asset growth. We're starting to see it come to fruition in pricing. We think growth could be a little bit challenge in the near term, but we're…we're very well committed to our growth strategy. We've established a consistent pattern of growth throughout various times of need through the last 30 years or so based on what we're seeing locally and activity. We do expect the second half of 2021 to start showing some sign of growth. We will remain focused on attracting loans that provide the best risk adjusted return. And we're really looking to stick with customers that provide the most robust banking relationships we actually feel is a strong opportunity to pick up the pace in our marketplace as several large mergers have recently been announced. This, again, will provide us an opportunity to add relationships, while some of these institutions work through their current deals.

Chris Keith
That's perfect. And then, you mentioned risk adjusted returns, Frank, I think that's a good segway into to kind of your recent and historic credit performance at Flushing. I think it's relatively well down that you've got a track record for low loss content, which I think implies a lower risk portfolio. What, Frank, would you attribute the success to?

Frank Korzekwinski
We try to keep it pretty basic. We have a history of working in a disciplined approach. We focus on cash flow lending. We look at the rents in place. We make sure that those loans can be paid based upon the income that's in there on day one. Historically, we've required relatively high debt coverage ratios that also results in a very low loan to value exposure. And I think one of the other things that helps us out considerably is the diversity of our loan portfolio, it's a very granular portfolio and enables us to spread our credit risk across multiple assets.

Chris Keith
And then how do you…how does Flushing manage credit on a regular basis?

Frank Korzekwinski
Probably the best way to answer that is, is through various independent processes, new credits are managed through a credit center that's independent of all lending teams. We also have an appraisal group that's separate independent that handles the entire appraisal process. We have an independent loan group…loan review group that reviews all the assets throughout the year. We also created a portfolio management team sometime back probably over 10 years ago. Their function is to oversee the financial statement review process, they conduct property inspections and oversee general collateral performance. They also have a very active, disciplined collection process. We are in constant contact with any and all of our delinquent accounts seeking alternatives other than foreclosures.

Chris Keith

That's perfect. I appreciate that description. Have you…has the pandemic forced you to make any kind of significant changes or led you to make any strategic changes to your lending criteria?

Frank Korzekwinski
Well, we've certainly looked very closely at what we've done in the last year, but I think overall we've remained committed to our consistent proven practices. Again, we're focused on collection activities. We want to make sure that recent collections will support the loan amount requested. In some cases, depending on the findings that we have, we may build in some loan payment reserves. Those reserves will stay in the place maybe 18, 24 months time, just to make sure that if there is a problem with the return of the pandemic, that the borrowers would be able to carry themselves through that process.

Chris Keith
Got it. And then I just want to quickly touch on your loan yield. It's kind of an above peer [ph] yield, and I'm curious just what do you attribute that that higher loan yield to?

Frank Korzekwinski
I think it goes back to, again, our strategy to ensure that we made…we maintain an appropriate risk reward relationship. We employ a risk based adjusted return strategy and all of our lending transactions. Giving our diverse loan book we can also attract business from varying asset…varying asset classes at appropriate levels of interest. Some of our competitors offer similar rates for all asset classes. We choose to distinguish between what we believe to be the appropriate level of risk and make adjustments accordingly. Approximately 83% of our loan book is located outside of Manhattan. As everyone knows, New York City proper [ph] is a very, very competitive market. It is price sensitive. Generally speaking, loans outside of Manhattan have a little bit of a premium spread in there. Loan size is also a differentiator for us. Our typical multifamily loan is probably somewhere around $1.3 million somewhere around there. Small loan transactions are generally less price sensitive and sometimes not as competitive. Our commercial real estate loans are generally in around a $2.5 million range. We also do focus very heavily on meaningful banking relationships, which helps us on the appropriate risk adjusted returns.

Chris Keith
Got it. And then, Frank what would you say is different about underwriting and Flushing versus others in the market?

Frank Korzekwinski
That’s a really good question. Probably tricky one to answer, we really don’t get to see credit criteria of most of our competitors, but again we do see the loans that we do not end up closing, and there are some differences in how we approach our lending decisions. Again, I think, the primary driver is, we focused on in place cash flow. We want to make sure that the loan pays for itself on day one. We also pay attention to what could happen potentially in the future. We do short [ph] rates…short test scenarios on loans. We want to make sure that if interest rates in the future would increase anywhere from 225 to 250 basis points over a five year period that the loan will still be able to support itself. We're also a little bit tight on debt coverage ratio requirements, which generally require DCRs in excess of our policy minimums. And that's reflected, as you can see in the charts with our overall performance. We bring a new deal in. We're very active in site inspections. Taking a look at what's going on in the property. We look at historical cash flows. We look at the information that's presented from the borrower. We take what we call a stabilized approach and typically what the stabilized approach does is, it enables us to stress the operating expenses in such a scenario that we know oil today, maybe $50 a

barrel or could be $60 another day or $30 another time. What we try to come up with an expense horizon that is not as favorable and is not as stressful as it could be in dire time. So what generally happens is the underwriting scenarios that we present, when we approve a loan have operating ratios typically in excess of what the borrower's income and expense statements are showing. There are a number of other nuances that we employ, but I think the best one is just to be consistent, stabilized approach over time.

Chris Keith
That's great, Frank. Thank you for that. And I just want to remind everyone, that if you have any questions, feel free to select that button on your screen and submit a question. So I've received one, and I'll go ahead and move over to that. The question is related to the mixed-use portfolio, and how occupancy is holding up in the first floor tenant in the mixed-use properties. So retail has been challenged for a while now and restaurants were severely impacted by the pandemic. Are you starting to see new leases signed or conversely, are you worried about lease renewals?

Frank Korzekwinski
Well, I'll take the first question with respect to new leases. Yes, we are seeing new leases being signed. As I mentioned earlier, most of the properties that we finance in this mixed-use portfolio are located in densely populated neighborhoods. Many of the residents in these neighborhoods use public transportation. They generally don't take all day trips to shopping centers and malls out in the suburbs. So there is a strong need for trade in the local communities to support those that live and shop in their own neighborhoods. They also have to remember that New York City is an extremely diverse community. We have it's a nation of people from all around the world. There are many different ethnic needs in various parts of various neighborhoods. In a five block area, you could have an Italian enclave. Three blocks later, you can have a Middle Eastern enclave. You can have a Spanish enclave another four blocks away. So not every neighborhood needs the same…the services that they would, let's say, in a sprawling suburban region. So we do see that these spaces, when they come on, on the market, they are being picked up. I also mentioned earlier in terms of renewals, many of the leases that we have in these small spaces are longer term, businesses have been around for 15-20 years, whether it's a pizza shop or a nail salon or a hair salon. These neighborhoods generally support strong economic activity, tends to not want to lose their leases and fear of having to pay more if they were evicted or if their business wasn't going to survive. The rents are also much lower in these spaces. With the exception of Manhattan, you could be talking about rents ranging from $35 to nearly $75 a square foot, when you're in New York City property [ph] in Manhattan that you could be paying $150, $200, $500 a square foot. Those are numbers that will probably have more difficult time releasing, but we're very confident in the mixed-use properties in and around the five boroughs of New York City.

CONCLUSION

Chris Keith
That's perfect. Thank you, Frank. And then we have no more questions at this time. So, Frank, I just want to sincerely thank you for your time, your experience and your insight into the markets have been completely invaluable. And I know that all of the individuals on the line will have certainly benefited from your thoughts. And thank you, everyone, for taking the time to participate and for your questions and everyone enjoy the rest of your day.

Frank Korzekwinski
Thank you, Chris. Thank you, everyone. I appreciate your time.